



Mixed Performance; Maintain Sell

Karnataka Bank (KBL) Q1FY22 results were a mixed bag with improved NIM and lower C-I but with higher restructuring and lower non-interest income. NII was up 7%/25% YoY/QoQ led by improvement in NIM by 9bps/57bps YoY/QoQ to 2.98%. The loan book was down 4.5% YoY and up 0.2% QoQ to Rs 51,791 Cr. Loan mix composition included Retail/Mid-Corporate/Large Corporate at 52%/34%/14% as the bank has run down its large corporate book from 30% in Mar'19. Non-interest income growth was muted, down 55%/37% YoY/QoQ. C-I ratio has improved to 48.9% from 53.9% QoQ. This led to PPOP growth of 8% QoQ but down 39% YoY to Rs 414 Cr. G/NNPAs marginally improved to 4.8%/3% from 4.9%/3.2% QoQ. Provisions declined 28% YoY but were up 8% QoQ to Rs 368 Cr. PAT was down 46% YoY and up 238% QoQ to Rs 106 Cr, supported by a tax write-back of Rs 60 Cr during the quarter.

Slippages for Q1FY21 stood at Rs 414 Cr (vs. Rs 1,176 Cr in Q4FY21). The Restructured book is up 54.5% QoQ to Rs 2,685 Cr and is ~5.2% of loans (3.3% in Q4FY21). It included ~Rs 300 Cr from a large corporate account and ~Rs 900 Cr from Retail and Mid-Corporate. Possible slippages from this book is ~10%. SMA2 accounts stood at ~4.2% at Rs 2,246 Cr. RWA to total assets increased to 59.03% from 58.14% QoQ. The management indicated credit costs to be in the range of 2.1% and loan growth of ~15% for FY22.

While up-tick in NIMs is encouraging, concerns on high restructured book persist. Threat and potential impact from the third wave of Covid could be more detrimental for smaller banks such as KBL with higher credit costs and lagging loan growth affecting profitability. The proposal of QIP placement is keenly eyed. We maintain SELL on the stock with a target of Rs 50/share (~0.25x FY23E ABV).

Key Result Takeaways

Business growth

- **Advances** de-grew 4.5% YoY and was up 0.2% to Rs 51,791 Cr. Retail now forms more than 50% while Mid/Large Corporate stood at 34%/14% respectively. The bank is actively undertaking digital loan underwriting for Housing, Car, and MSME Loans.
- The management expects better traction in the **Gold loan book** since ~48% of its branches are in rural areas which will help augment the growth in this book.
- **Deposit** traction of 6.1% YoY to Rs 76,215 Cr was led by CASA deposit, up 14.1%. Retail deposits was up 2.9% YoY to Rs 52,720 Cr. CASA ratio stood at 30.8%, down 67bps QoQ and up 216 bps YoY.

Asset quality

- **Slippage** of Rs 414 Cr (all below 50 Cr category) included more than half from MSME at Rs 255 Cr. Other sector slippages stood at Rs 43 Cr from Agri, Rs 7 Cr from CRE, Rs 58 Cr from Housing Loan, Rs 18 Cr from Mortgages, Rs 11 Cr from Vehicle Loans, and Rs 8 Cr from Personal Loans. Segment-wise NPAs include ~6% in Retail and ~5% in Mid-corporate.
- The management indicated **recoveries** of ~Rs 120 Cr over the next 2-3 months from a coffee account with Rs 17 Cr already recovered.
- The **restructuring portfolio** stood at ~Rs 2,685 Cr (5.2% of loans) up from Rs 1,738 Cr (~3.3% in Q4FY21). Of this, Rs 271 Cr, ~10% are NPAs.

Key Financials (Standalone)

(Rs Cr)	FY20	FY21P	FY22E	FY23E
NII	2,030	2,183	2,423	2,738
PPOP	1,657	1,999	1,845	1,974
Net Profit	432	483	433	502
EPS (Rs)	13.9	15.5	13.9	16.2
ABV	135.6	161.7	182.6	216.7
P/ABV	0.30	0.27	0.25	0.24
ROAA	0.5	0.6	0.5	0.5
NNPA (%)	3.1	3.2	3.0	2.8

Source: Company, Axis Research9

(CMP as of July 28, 2021)

CMP (Rs)	58
Upside /Downside (%)	-14%
High/Low (Rs)	73/40
Market cap (Cr)	1789
Avg. daily vol. (6m) Shrs.	8,76,784
No. of shares (Cr)	31.1

Shareholding (%)

	Jun-21	Mar-21	Dec-20
Promoter	0.0	0.0	0.0
FIs	10.0	9.4	8.1
MFs / UTI	0.2	0.2	0.4
Banks / FIs	5.6	5.6	5.6
Others	84.2	84.8	85.8

Financial & Valuations

Y/E Mar (Rs. cr)	2021P	2022E	2023E
NII	2,183	2,423	2,738
PPOP	1,999	1,770	1,716
Net Profit	483	415	437
EPS (Rs.)	15.5	13.4	14.1
ABV	161.7	182.0	216.1
P/ABV	0.3	0.3	0.2
ROAA	0.6	0.4	0.4
NNPA (%)	3.2	3.0	2.8

Change in Estimates (%)

Y/E Mar	FY22E	FY23E
NII	0.0	-0.9
PPOP	-13.9	-14.6
PAT	-18.7	-19.0

Axis vs. Consensus

EPS Estimates	2022E	2023E
Axis	13.9	16.2
Consensus	14.6	18.2
Mean Consensus TP (12M)		75.0

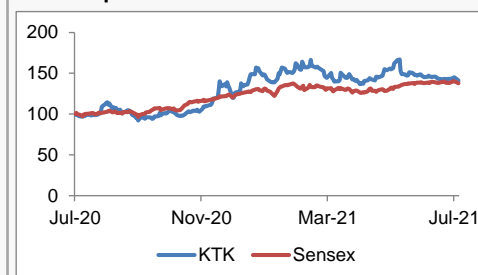
ESG disclosure Score**

Environmental Disclosure	7.1
Social Disclosure Score	36.7
Governance Disclosure Score	51.8
Total ESG Disclosure Score	25.9

Source: Bloomberg, Scale: 0.1-100

**Note: This score measures the amount of ESG data a company reports publicly, and does not measure the company's performance on any data point. All scores are based on 2020 disclosures

Relative performance



Source: Capitaline, Axis Securities

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Asset quality (Cont'd)

- **RWA** to total assets increased to 59.03% from 58.14% QoQ and down from 62.8% YoY.
- Under **SMA2**, 5 Cr and above is Rs 450 Cr and below 5 Cr is Rs 1,796 Cr.
- **PCR** (including Technical w/off) stood at 72.24% vs 70.05% QoQ. PCR (excluding Technical w/off) was 39.08% vs. 36.56% QoQ.
- As of Mar'21, **NCLT** cases stood at 34 amounting to Rs 1,462 Cr, and are fully provided for. The SR portfolio of Rs 394 Cr has ~43% coverage.
- Infra accounts have ~97% coverage while Agri is 67%, MSME 60%, CRE 78%, Personal Loans 42%, and Housing is at 55%.

Others

- **CAR** improved to 14.6% (Tier 1 at 12.1%) from 13.4% YoY (Tier 1 at 11.7%). The bank is planning for a QIP placement after the approval of the shareholders.

Change in Estimates
(Rs Cr)

	Revised		Old		%Change	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
NII	2423	2738	2423	2763	0.0	-0.9
PPOP	1845	1974	2144	2312	-13.9	-14.6
PAT	433	502	532	620	-18.7	-19.0
EPS	13.9	16.2	17.1	19.9	-18.6	-18.8

Source: Company, Axis Research

Valuation & Outlook

While the recent trends of improving NIMs and better CAR are positives, concerns on restructuring exist. The management indicated credit costs at ~2.1% and loan growth of ~15% for FY22. We believe, higher credit costs and lagging loan growth amidst uncertain macro conditions will impact the earnings outlook for smaller banks such as KBL. The potential threat of a third wave of Covid-19 remains a key downside risk. We maintain a SELL on the stock with a target of Rs 50/share (~0.25x FY23E ABV).

Result Update (Standalone)

(Rs Cr)

Y/E March	Q1FY22	Q1FY21	% YoY	Q4FY21	% QoQ
Net Interest Income	575	535	7.4	459	25.2
Non Interest Income	236	519	-54.5	373	-36.8
Operating expenses	396	377	5.2	449	-11.6
Staff Cost	224	202	11.3	240	-6.4
Pre provision profits	414	677	-38.8	384	8.0
Provisions and contingencies	368	509	-27.7	342	7.7
PBT	46	168	-72.5	42	10.2
Provision for Tax	-60	-28	NM	11	NM
PAT	106	196	-46.0	31	238.3
Deposits	76,215	71,854	6.1	75,655	0.7
Advances	51,791	54,209	-4.5	51,694	0.2
CD ratio (%)	68	75		68	
CASA (%)	30.8	28.7		31.5	
NIM (%)	2.98	2.89		2.41	
Cost-Income ratio (%)	48.9	35.8		53.9	
Gross NPAs (%)	4.8	4.6		4.9	
Net NPAs (%)	3.0	3.0		3.2	
Slippages (Rs cr)	414.2	166.8		1,176	
PCR (incl tech w/off)	72.2	67.9		70.1	
PCR (excl tech w/off)	39.1	36.2		36.6	

Source: Company, Axis Securities

Financials (Standalone)
Profit & Loss
(Rs Cr)

Y/E March	FY20	FY21P	FY22E	FY23E
Net Interest Income	2,030	2,183	2,423	2,738
Other Income	1,396	1,495	1,271	1,334
Total Income	3,427	3,678	3,694	4,073
Total Operating Exp	1,770	1,679	1,849	2,099
PPOP	1,657	1,999	1,845	1,974
Provisions & Contingencies	1,135	1,387	1,199	1,224
PBT	522	612	646	750
Provision for Tax	90	129	213	247
PAT	432	483	433	502

Source: Company, Axis Securities

Balance Sheet
(Rs Cr)

Y/E March	FY20	FY21P	FY22E	FY23E
SOURCES OF FUNDS				
Share Capital	311	311	311	311
Reserves	5,660	6,331	6,764	7,267
Shareholder's Funds	5,971	6,642	7,075	7,578
Total Deposits	71,785	75,655	80,194	88,214
Borrowings	4,065	1,765	4,482	4,482
Other Liabilities & Provisions	1,493	1,519	1,534	1,550
Total Liabilities	83,314	85,581	93,285	1,01,823
APPLICATION OF FUNDS				
Cash & Bank Balance	2,920	5,316	11,597	10,848
Investments	17,545	21,635	19,597	21,557
Advances	56,964	51,694	55,829	62,529
Fixed Assets & Other Assets	5,884	6,937	6,262	6,889
Total Assets	83,314	85,581	93,285	1,01,823

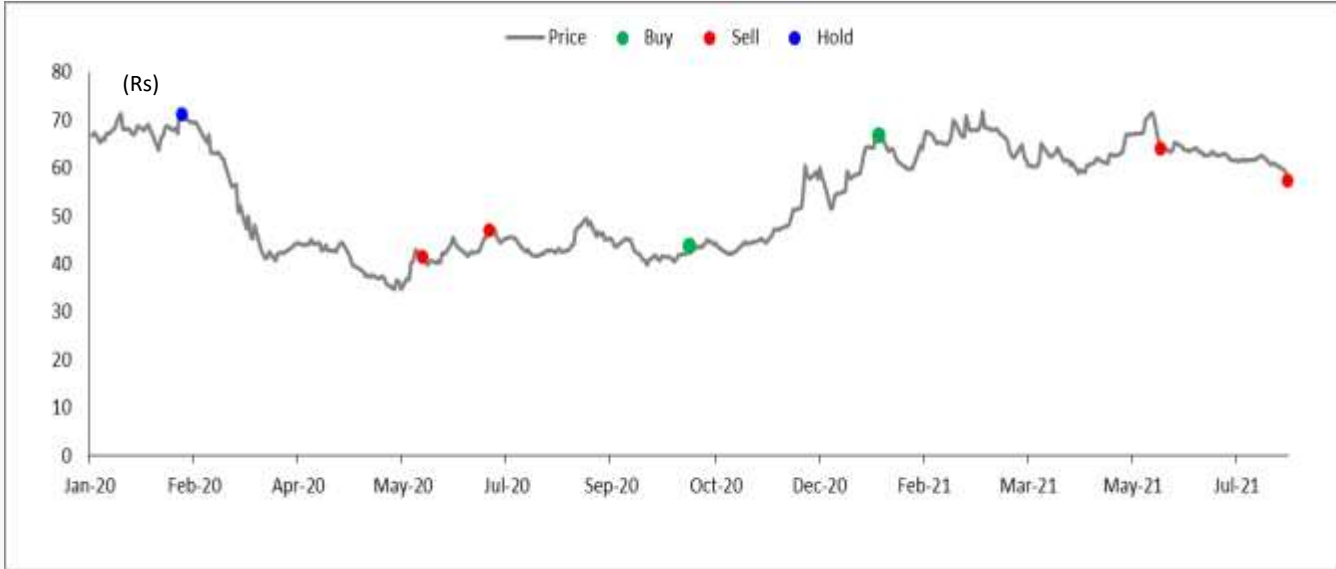
Source: Company, Axis Securities

Ratio Analysis
(%)

Y/E March	FY20	FY21P	FY22E	FY23E
VALUATION RATIOS				
EPS	13.9	15.5	13.9	16.2
Earnings Growth (%)	-21.4	11.8	-10.4	16.1
BVPS	192.0	213.7	227.6	243.7
Adj. BVPS	135.6	161.7	182.6	216.7
ROAA (%)	0.5	0.6	0.5	0.5
ROAE (%)	7.2	7.3	6.1	6.6
P/E (x)	4.2	3.7	4.2	3.6
P/ABV (x)	0.30	0.27	0.25	0.24
COSTS				
Cost-Asset (%)	2.12	1.96	1.98	2.06
Cost-Income (%)	51.6	45.6	50.1	51.5
BALANCE SHEET STRUCTURE RATIOS				
Loan Growth (%)	3.9	-9.3	8.0	12.0
Deposit Growth (%)	4.9	5.4	6.0	10.0
C/D Ratio (%)	79.4	68.3	69.6	70.9
CAR	12.7	14.9	12.6	12.4
CASA (%)	28.9	31.5	31.9	32.1
ASSET QUALITY				
Gross NPLs (%)	4.8	4.9	4.8	4.4
Net NPLs (%)	3.1	3.2	3.0	2.8
Slippage (%)	2.9	2.5	2.4	2.3
Credit Costs (%)	2.0	2.7	2.1	2.0
SPREADS				
Yield on Advances	9.2	9.1	9.1	9.1
Cost of Deposits	6.0	5.7	5.8	5.9
NIM	2.8	2.9	3.0	3.0

Source: Company, Axis Securities

Karnataka Bank Chart and Recommendation History



Date	Reco	TP	Research
14-Feb-20	HOLD	83	Result Update
08-Jun-20	Sell	37	Result Update
10-Jul-20	Sell	40	Result Update
14-Oct-20	BUY	48	Result Update
13-Jan-21	BUY	75	Result Update
28-May-21	Sell	60	Result Update
29-Jul-21	Sell	50	Result Update

Source: Axis Securities

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