

Shubh Nivesh



CMP: ₹ 228

Target: ₹ 285 (25%)

Target Period: 6-12 months

Sep 18, 2023

BUY (HIGH CONVICTION IDEA)

Geographic expansion & new age tech adoption to aid growth...

About the stock: Incorporated in 1924, Karnataka Bank is a south based private sector bank with large presence in state of Karnataka. With ~46% of branches in rural & semi urban areas, the bank focusses on retail, MSME & agri segment (share of agri/ MSME at ~37.4% of advances).

- Pan India presence with 901 branches of which 575 branches are in the state of Karnataka
- Bank has large customer base of 1.3 crore; employee strength at 8652

Investment Rationale:

- **Focussing on geographic and digital expansion to aid credit growth:** Focus on core strength (agri & MSME loans) and renewed emphasize on retail loans (increasing share from 45.5% in FY20 to 50.3% in FY23) is expected to keep credit growth healthy. Management targets credit growth at 17-18% in FY24E and further to double business in 3 – 3.5 years. Product development & benchmarking pricing with market has been undertaken to focus on retail loans. Further, number of home loan processing hubs has been increased from 5 to 8 to enhance capacity in retail loans. To ensure efficient and sustainable growth, partnership remains key focus area with tie-ups across financial domain including credit cards, co-lending, insurance, demat services and AMC. While the bank has set up outbound sales team implementing business centric & outward facing culture, centralisation of operations (by setting up a technology & digital hub in Bengaluru) is expected to release bandwidth for front-end activities thereby focussing on improving product penetration.
- **Focus to keep margins steady; moderation in credit cost to aid RoA:** Cost of funds is expected to increase in near term, however, focus on liabilities accretion (tapping government business, outbound sales team & product launches), improvement in CD ratio (75-80%) and shift from low yield business (target to increase share of gold loan at 7-8%) is expected to offset pressure thereby keeping margins steady at 3.5-3.7%. Building up distribution & technological capacities (tech budget of ₹200 crore for FY24E) is expected to keep opex higher, though moderation in credit cost is seen to sustain RoA at ~1.2%.
- **Asset quality remains strength; GNPA to decline further:** Asset quality has been on improving trend with GNPA declining from 4.9% in FY18 to 3.7% in Q1FY24. Focus on core under writing standards overlaying digital capabilities is expected to keep slippages in control. Management targets NNPA to decline to ~1.2% (at 1.43% as of Q1FY24) and credit cost to remain steady at current level.

Rating and Target Price

- Strategy to harness core competency with focus on geographic & product expansion along with investment in digital technology is expected to aid growth and asset quality. Steady margins and prudent asset quality is expected to offset higher opex thereby sustaining RoA at ~1.2% in FY24-25E.
- At CMP, the stock is trading 0.7x FY25E ABV which seems relatively lower. Assigning a multiple of ~0.9x FY25E ABV, we ascribe target of ₹ 285 per share and a **BUY** rating

Key Financial Summary

₹ crore	FY19	FY20	FY21	FY22	FY23	4 year CAGR (FY20-23)	FY24E	FY25E	2 year CAGR (FY23-25)
NII	1905.1	2030.4	2183.2	2491.0	3185.1	68.0%	3463.8	3840.3	9.8%
PPP	1449.8	1656.8	1999.1	1634.0	2208.2	72.9%	2332.3	2622.5	9.0%
PAT	477.2	431.8	482.6	508.6	1180.2	50.7%	1295.5	1453.7	11.0%
BV	204.7	192.1	213.7	228.0	263.0		298.21	337.77	
P/E	135.0	164.2	146.9	139.5	60.3		55.0	49.0	
P/ABV	1.1	1.2	1.1	1.0	0.9		0.8	0.7	
RoA	0.6	0.5	0.6	0.6	1.2		1.2	1.2	
RoE	8.2	7.2	7.3	7.2	15.4		13.9	13.8	

Source: Company, ICICI Direct Research



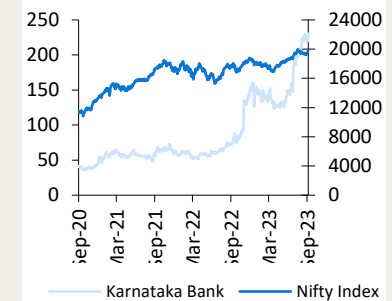
Particulars

Particulars	Amount
Market Capitalisation	₹7131 crore
52 week H/L	248/ 76
Net Worth	8,213
Face Value	10.00
DII Holding (%)	6.00
FII Holding (%)	21.03

Shareholding pattern

	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23
Promoter	0.0	0.0	0.0	0.0	0.0
FII	15.5	18.2	19.8	20.3	21.0
DII	5.3	5.3	5.4	5.7	6.0
Others	79.2	76.5	74.8	74.0	73.0

Price Chart



Recent Event & Key risks

- Focus on retail advances with share increasing from 45.5% in FY20 to 50.3% in FY23
- **Key Risk:** (i) Accretion of liabilities at competitive price, (ii) Slower growth in advances could keep CI elevated and thus impact earnings

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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