Gearing Up for Growth After a Year of Consolidation!

We interacted with the management of Karnataka Bank (KTKBANK) represented by the MD CEO Mr. Srikrishnan H, and Mr. Soham Roy (Investor Relations), to reflect upon the transformative journey the bank has undertaken and highlight the growth roadmap for the bank as it readies to embark on its next leg of growth.

Key Takeaways

- **Teams and Processes Strengthened**: As a part of its transformative journey under the new management, the bank undertook the reorganisation of several departments, strengthening underwriting capabilities, working towards freeing the bandwidth of branches alongside strengthening its management and business teams across functions, with key managerial positions being filled. The bank has also tried to enhance its digital capabilities and effectively bridge its technological gaps. Additionally, along with its traditional branch-led business sourcing model, the bank has sharpened its focus on sales-led, digital and partnership-led (for select products).
- **Growth to accelerate from FY26E onwards:** In FY25, the slower credit growth of 7% YoY can be primarily attributed to the portfolio churn towards retail loans and mid/direct-to-corporate lending away from the opportunistic lower-yielding large and PSU/NBFC lending that the bank pursued earlier. Under its strategy to improve the share of direct-to-corporate loans, the bank has seen a ~Rs 1,300 Cr churn from the NBFC advances to the direct-to-corporate segment in FY25. During the year, of the total accretion of ~Rs 5,000 Cr to the portfolio, a majority was from the retail assets, while the contribution to the mid/direct-to-corporate book was lower at Rs 1,500 Cr.
  The bank will continue to focus on the RAM segment, particularly Retail Assets (Housing, Vehicle, Gold Loans). Currently, KTKBANK has limited exposure to unsecured segments (<10% of the portfolio), which was largely to opportunistic PSU entities. The bank will continue to remain cautious while pursuing growth in the unsecured lending space. Currently, the bank's focus in the unsecured space will remain on credit line on UPI, co-lending with select MSMEs and digital personal and SME Loans with pre-approvals. **The management has guided for credit growth of 12-14% (net, while retiring bulk advances) in FY26E, with the pace of growth further accelerating going into FY27E. We expect KTKBANK to deliver a ~15% CAGR credit growth over FY25-27E.**
- **Deposit mix retailization to continue:** The bank has taken major initiatives to replace high-cost bulk deposits with retail deposits, which is evident from the fall in its share from 8% in FY24 to ~6% in FY25. Hereon, the focus will remain on the mobilisation of Retail TDs and CASA Deposits. **Going into FY26, the bank will look to moderate deposit growth, given its comfortable positioning on LDR. The management has indicated that the bank will look to improve its LDR to 80% from ~74% currently. Thus, we expect deposit growth to be lower vs credit growth at ~13% CAGR over FY25-27E.**
- **Margin improvement levers present**: The shift in the portfolio mix towards RAM portfolio and better-yielding mid/direct-to-corporate lending is expected to support NIMs. Moreover, ~70% of the bank's portfolio is linked to T-bills, contrary to the bank's peers' portfolios being repo-linked. Thus, the impact of the rate cuts is expected to be relatively shallow. Alongside the better yields from the favourable product mix, the bank has also reduced its deposit rates and adjusted the deposit tenor. The impact of these rate actions is expected to reflect in the CoD/CoF in the forthcoming quarters. **Thus, the management expects NIM improvement to the tune of 15-20bps.**

Outlook and Valuation

With investments made and strengthening processes and teams ripe to yield results, we expect KTKBANK to resume its growth journey, though gradually from FY26E onwards. Focus on granular retail deposits, particularly CASA deposits, remains unabated. We believe KTKBANK has multiple levers in place to protect and improve its margins over the medium term, thereby enabling the bank to improve RoAs. With a majority of the investments already made, Opex growth is expected to remain modest, driving cost ratios downwards. We expect RoA/RoE to remain at 1.1-1.2%/10-13% over FY25-27E, driven by the aforementioned factors. **Growth delivery on guided lines, and sustenance remain key levers for a meaningful re-rating in the stock**. **We maintain our BUY recommendation on the stock on inexpensive valuations. We value the stock at 0.75x FY27E ABV to arrive at a target price of Rs 270/share, implying an upside of 38% from the CMP.**

(CMP as of 23rd May, 2025)	
CMP (Rs)	196
Upside /Downside (%)	38%
High/Low (Rs)	245/162
Market cap (Cr)	7,410
Avg. daily vol. (6m) Shrs.	13,33,389
No. of shares (Cr)	37.8

Shareholding (%)

	Sep-24	Dec-24	Mar-25
Promoter	0.0	0.0	0.0
FIIs	10.3	11.2	12.9
MFs / UTI	21.6	19.7	17.5
Others	68.1	69.1	69.6

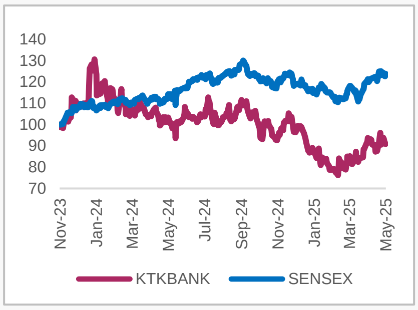
Financial & Valuations

Y/E Mar (Rs Cr)	FY25	FY26E	FY27E
NII	3,310	3,636	4,369
PPOP	1,827	2,022	2,599
Net Profit	1,272	1,236	1,590
EPS (Rs)	33.7	32.7	42.1
ABV (Rs)	293.2	322.9	358.5
P/ABV (x)	0.7	0.6	0.5
RoA (%)	1.2	1.1	1.2
NNPA (%)	1.3	1.1	0.9

Change in Estimates (%)

Y/E Mar	FY26E	FY27E
NII	-	-
PPOP	-	-
PAT	-	-

Relative performance



Source: AceEquity, Axis Securities Research

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Key Takeaways (Contd.)

Asset Quality stress under control: KTKBANK has seen an impressive improvement in asset quality driven by controlled slippages and a healthy pace of recoveries. **The bank does not expect any negative surprises on asset quality, even from the restructured book. Going into FY26, the bank expects to contain slippages at <2%.** Furthermore, the bank has been focusing on recoveries from smaller accounts. The bank is also making efforts to ramp up its PCR (currently at ~58%) to align it with its peer banks. **The management has guided to improve PCR by 1% each quarter, which could imply higher credit costs in the interim. Despite this, the management remains confident of containing credit costs at ~50bps in FY26E**.

Opex growth controlled; Cost Ratio improvement underway: KTKBANK's Opex growth is expected to remain under control, with expenses only if they align with the business model. The bank will continue to invest in tech infrastructure. **Driven by controlled Opex, the management expects the C-I Ratio to improve to 55-56% in FY26 vs 60% in FY25.**

Key Risks to Our Estimates and TP

- The key risk to our estimates remains a slowdown in overall credit momentum, which could potentially derail earnings momentum for the bank.
- Asset Quality challenges could pose challenges for credit costs and impact our earnings estimates.

Financials (Standalone)

Profit & Loss

(Rs Cr)

Y/E March	FY24	FY25	FY26E	FY27E
Net Interest Income	**3,299**	**3,310**	**3,636**	**4,369**
Other Income	1,319	1,270	1,399	1,557
Total Income	**4,618**	**4,580**	**5,035**	**5,927**
Total Operating Exp	2,454	2,753	3,013	3,327
PPOP	**2,163**	**1,827**	**2,022**	**2,599**
Provisions & Contingencies	601	186	370	473
PBT	**1,563**	**1,641**	**1,652**	**2,126**
Provision for Tax	256	368	416	536
PAT	**1,306**	**1,272**	**1,236**	**1,590**

Source: Company, Axis Securities Research

Balance Sheet

(Rs Cr)

Y/E March	FY24	FY25	FY26E	FY27E
SOURCES OF FUNDS				
Equity Share Capital	377	378	378	378
Reserves & Surplus	10,471	11,707	12,758	14,109
Net Worth	**10,848**	**12,085**	**13,136**	**14,487**
Deposits	98,058	1,04,807	1,17,179	1,32,661
Borrowings	1,02,457	1,06,748	1,19,849	1,38,514
Other Liabilities	**2,779**	**2,128**	**2,382**	**2,740**
Total Liabilities	**1,16,085**	**1,20,962**	**1,35,366**	**1,55,742**
APPLICATION OF FUNDS				
Cash & Bank Balance	7,993	7,984	8,224	8,979
Investments	24,302	24,537	26,964	30,527
Advances	71,509	76,541	87,268	1,01,383
Fixed & Other Assets	12,281	11,899	12,910	14,854
Total Assets	**1,16,085**	**1,20,962**	**1,35,366**	**1,55,742**

Source: Company, Axis Securities Research

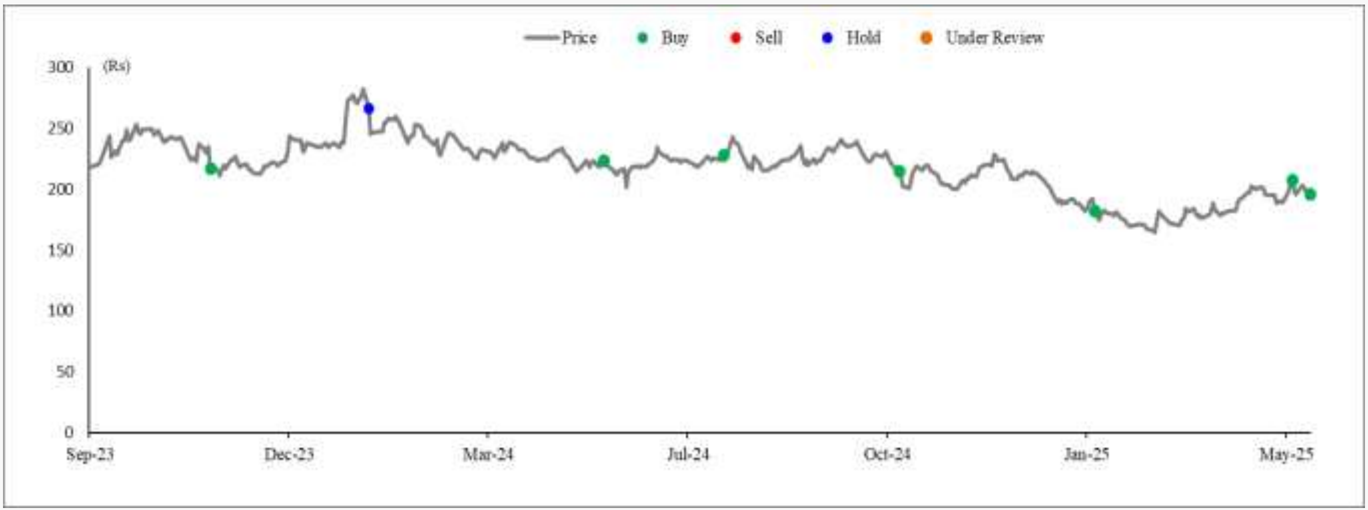
Ratio Analysis

(%)

Y/E March	FY24	FY25	FY26E	FY27E
VALUATION RATIOS				
EPS	34.6	33.7	32.7	42.1
Earnings Growth (%)	*-8.4*	*-2.8*	*-2.9*	*28.7*
BVPS	287.6	319.8	347.5	383.3
Adj. BVPS	257.6	293.2	322.9	358.5
ROAA (%)	1.2	1.2	1.1	1.2
ROAE (%)	13.7	12.0	11.0	12.9
P/E (x)	5.7	5.8	6.0	4.7
P/ABV (x)	0.8	0.7	0.6	0.5
PROFITABILITY				
NIM (%)	3.5	3.2	3.2	3.4
Cost-Income Ratio (%)	53.2	60.1	59.8	56.1
BALANCE SHEET STRUCTURE RATIOS				
Loan Growth (%)	19.3	7.0	14.0	16.2
Deposit Growth (%)	12.2	6.9	11.8	13.2
C/D Ratio (%)	72.9	73.0	74.5	76.4
Equity/Assets (%)	15.2	15.8	15.1	14.3
Equity/Loans (%)	9.3	10.0	9.7	9.3
CAR (%)	18.0	19.9	19.3	18.5
Tier 1 CAR (%)	16.2	18.4	17.9	17.2
ASSET QUALITY				
Gross NPLs (%)	3.6	3.1	2.7	2.3
Net NPLs (%)	1.6	1.3	1.1	0.9
Coverage Ratio (%)	56.2	58.2	60.0	60.0
Credit costs (%)	0.9	0.3	0.5	0.5
ROAA TREE				
Net Interest Income	3.1	2.8	2.8	3.0
Non-Interest Income	1.2	1.1	1.1	1.1
Operating Cost	2.3	2.3	2.4	2.3
Provisions	0.6	0.2	0.3	0.3
Tax	0.2	0.2	0.2	0.2
ROAA	1.2	1.2	1.1	1.2
Leverage (x)	11.3	10.3	10.2	10.5
ROAE	13.7	12.0	11.0	12.9

Source: Company, Axis Securities Research

Karnataka Bank Price Chart and Recommendation History



Date	Reco	TP	Research
03-Nov-23	BUY	250	Result Update
24-Jan-24	HOLD	275	Result Update
27-May-24	BUY	255	Result Update
25-Jul-24	BUY	275	Result Update
24-Oct-24	BUY	275	Result Update
03-Feb-25	BUY	255	Result Update
15-May-25	BUY	270	Result Update
26-May-25	BUY	270	Company Update

Source: Axis Securities Research

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