

April 10, 2017

LKP Bytes

Lakshmi Vilas Bank

Outperformer

LKP

Since 1948

Industry: Banking

Lakshmi Vilas Bank (LVB) is an old generation private sector bank incorporated in the year 1926. Headquartered in Chennai, LVB has granular customer segmentation and a business of ₹474.64 bn. With a substantial foothold in the Southern states and a dominant presence in Tamil Nadu, LVB has a network of 460 branches and 926 ATMs across 16 states in India. LVB, with competitive interest rates and increase in advertising efforts has a customer base of 2.8 mn. In Q3FY17, for the first time in its 90 year history, LVB accessed the public markets to raise direct equity which it did through a successful QIP to the extent of ₹1.68 bn.

Q3 Financial Performance

Due to higher repayments and credit weakness witnessed on account of DeMon, LVB's loan book degrew sequentially to ₹197 bn in Q3FY17 (-2.7% QoQ). However, the loan book expanded 8.5% YoY mainly driven by the growth in advances towards the retail and MSME sector. A healthy SA growth (70.9% YoY) led to an increase in CASA to ₹59.4 bn (49.8% YoY) in 9MFY17 causing deposits to augment to ₹277.51 bn (15.9% YoY). Strong momentum witnessed in CASA which expanded 22.28% QoQ due to DeMon led to a growth of 4% QoQ in deposits. Consequently, CASA as a share of deposits increased 411 bps sequentially to 21.42% in Q3FY17.

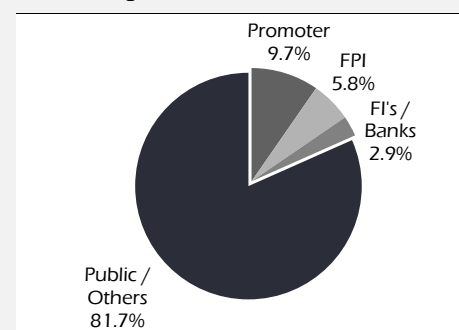
In Q3FY17, a downward movement of 12bps QoQ in NIM to 2.72% was witnessed mainly due to a decline in Credit-Deposit ratio to 71.04% (487bps QoQ). Asset quality remained flat sequentially with Gross NPA deteriorating to 2.78% (8bps QoQ) and Net NPAs improving to 1.82% (-5 bps QoQ). As compared to ₹1.73 bn in Q2FY17, fresh slippages remained moderate at ₹0.87 bn in Q3FY17. Provision coverage ratio improved 234bps QoQ to 62.21% in Q3FY17.

Operating profit increased to ₹1.71 bn (8.22% QoQ) on account of a strong surge in other income which augmented to ₹1.5 bn (13.9% QoQ) and an increase in NII to ₹1.91 bn (2.12% QoQ). While the increase in NII was largely driven by drop in the interest cost, higher treasury gains contributed to the sharp rise in other income. OPEX increased 5.77% QoQ to ₹1.69 bn due to 11.7% rise in employee cost on account of staff augmentation. Strong total income caused a sequential decline in the Cost to Income ratio by 57bps to 49.7% in Q3FY17. Sequentially, PAT expanded 20.87% QoQ to ₹0.78 bn on account of a 23.18% QoQ decrease in Provisions and Contingencies. The Return on Assets ratio improved 12bps to 0.98 while the Return on Equity ratio increased 279bps to 18.18 in Q3FY17.

Stock Data

Current Market Price (₹)	165
12 month Target (₹)	190
Potential upside (%)	15
Market Cap (₹ bn)	32
52-Week Range (₹)	174 / 78
Reuters	LVB IN.
Bloomberg	LVL5.NS
BSE / NSE Code	534690 / LAKSHVILAS

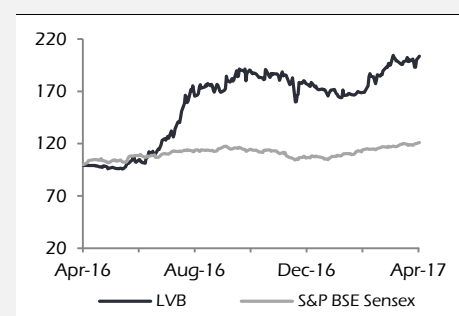
Shareholding Pattern



Key Operational Metrics

Particulars	Q4FY16	Q1FY17	Q2FY17	Q3FY17
NIM	2.8%	2.8%	2.8%	2.7%
PCR	68.6%	66.5%	59.9%	62.2%
Cost to Income	62.2%	52.8%	50.3%	49.7%
Cost of Funds	7.3%	7.0%	6.8%	6.7%
Yield on Adv.	12.2%	11.5%	11.5%	11.5%
Gross NPA	2.0%	2.1%	2.7%	2.8%
Net NPA	1.2%	1.3%	1.9%	1.8%
ROA	0.7%	0.8%	0.9%	1.0%
ROE	12.3%	15.0%	15.4%	18.2%
ABV (₹)	98.3	101.7	105.3	109.6

Relative Price Performance



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LKP Research

Outlook

With an intention to expand retail portfolio in its loan book, LVB aims to make its presence felt in mortgage loans and eventually grow in the two & four wheeler segment. India has steadily been improving in these sectors mainly due to population growth, urbanization, increase in disposable income, emergence of nuclear families, and upgradation in standard of living. The pace of remonetisation will continue to trigger a rebound in discretionary consumer spending aiding an expansion in retailing activity. In case of SME sector, LVB continues to focus on working capital financing ensuring stable asset quality due to backing from business cash flows and shorter period of advances. In order to elevate non funded services to the SME sector, various measures such as bank guarantees, treasury products, letter of credit etc. have been extended.

NIM has been resilient as the decline in cost of funds has been in tandem with the fall witnessed in yield on advances. As compared to its regional peers, LVB's CASA as a share of deposits is low and thus the management is focused on expanding CASA through customer base enlargement, increasing branch network, competitive interest rates, new services and innovative technology. Enlarging the share of low-cost CASA will enable LVB to bring down its overall cost of deposits ensuring an improvement in NIM. Though LVB has a very strong retail deposit franchise, maturities have been relatively small. Since rate changes happen only when deposit maturity and replacement occurs, LVB has not been able to take advantage of reducing cost of deposits. However, bias towards retail funding with low ALM mismatches will stabilize NIM going forward.

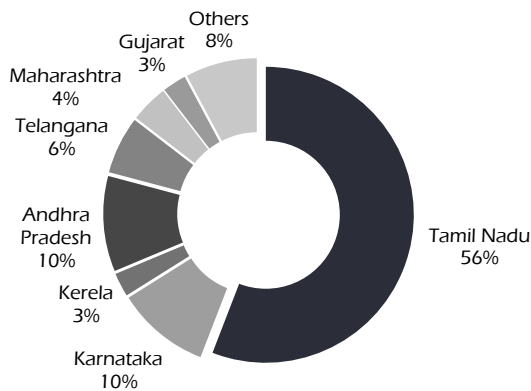
60% of the sectors contributing to LVB's GNPA exposure make up for only 20% of the loan book. Thus, a low percentage of advances are towards the sectors that form a substantial portion of the stressed assets indicating stability in quality of assets. Low concentration of restructured assets with a focus on reducing GNPA exposure to high risk sectors ensures diversification of portfolio risk and restricts asset quality stress. Diminishing slippages with increased recoveries and reduced write-offs signify improvement in asset lending policies. Reducing provisions as % of average assets with rising provision coverage ratio will enable enhancement in asset quality. The operating cost will be moderate going forward as LVB was in an investment phase encouraging staff augmentation. Focus on increasing other income will assist improvement in Cost to Income ratio.

LVB's focus to reduce costs, decrease slippages & write offs and grow retail base will be key drivers to improve profitability. Sustained branch productivity with aggressive expansion, implementation of innovative technology and continued focus staff training along with brand building signify healthy growth for LVB going forward. At the current price of ₹165, LVB, trading at 1.5x adjusted book value can be **ACCUMULATED** with a **one year price objective of ₹190**.

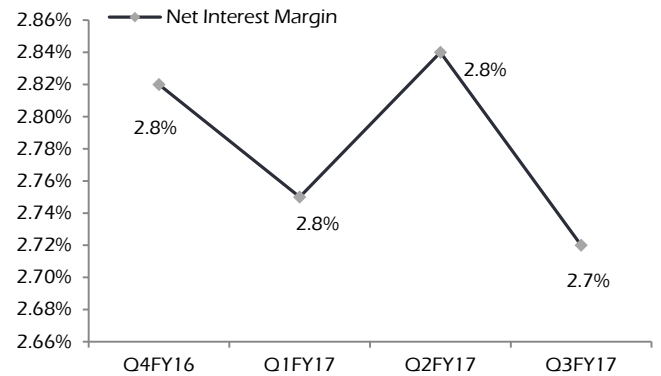
Quarterly Performance

Particulars (₹ Mn)	Q3FY17	Q2FY17	QoQ %	Q3FY16	YoY %	9MFY17	9MFY16	YoY %
Total Interest Earned (I)	7,290	6,984	4.4	6,537	11.5	21,131	19,020	11.1
Interest/ Discount on Advances/Bills	5,627	5,648	(0.4)	5,172	8.8	168,596	15,040	-
Income on Investments	1,587	1,305	21.6	1,310	21.1	4,149	3,887	6.7
Interest on balances with RBI and other interbank Funds	71.6	26.7	-	4.5	-	108	26	-
Others	5.4	4.3	25.5	50	(89.2)	14	67	(79.1)
Other Income (II)	1,502	1,319	13.9	693	116.7	3,713	2,120	75.1
Total Income (I) + (II)	8,793	8,303	5.9	7,231	21.6	24,844	21,140	17.5
Interest expended (III)	5,384	5,117	5.2	4,867	10.6	15,583	14,294	9.0
Operating Expenses (IV)	1,694	1,602	5.8	1,304	29.9	4,705	3,777	24.6
Employees Cost	912	817	11.7	670	36.1	2,493	1,911	30.5
Other Operating Expenses	782	785	(0.4)	634	23.3	2,212	1,866	18.5
Total Expenditure (III) + (IV)	7,078	6,719	5.3	6,171	14.7	20,287	18,070	12.3
Operating Profit before Provisions and Contingencies	1,714	1,584	8.2	1,060	61.8	4,557	3,070	48.5
Provisions (other than tax) and Contingencies	481	626	(23.2)	579	(17.0)	1,458	1,498	(2.7)
Profit (Loss) before tax	1,234	958	28.7	481	-	3,099	1,572	97.2
Tax expense	450	310	45.2	20	-	1,060	260	-
Net profit for the period	784	648	20.9	461	70.1	2,039	1,312	55.5

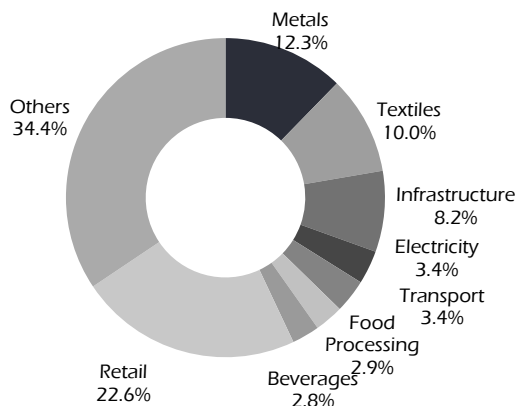
Branch Distribution



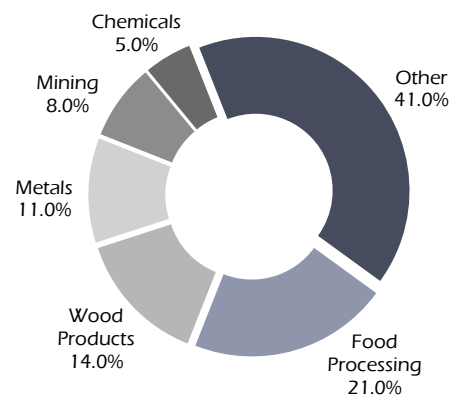
Net Interest Margin



Sector Wise Restructured Advances

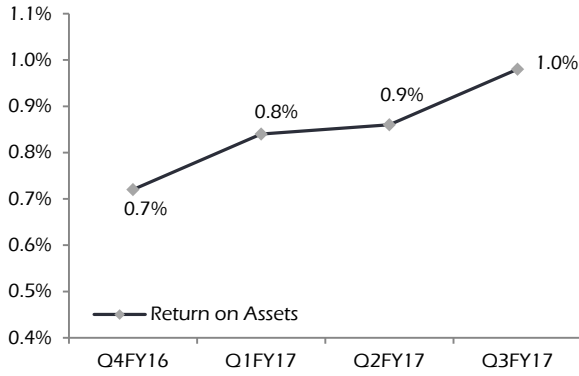


GNPA exposure to high risk sectors

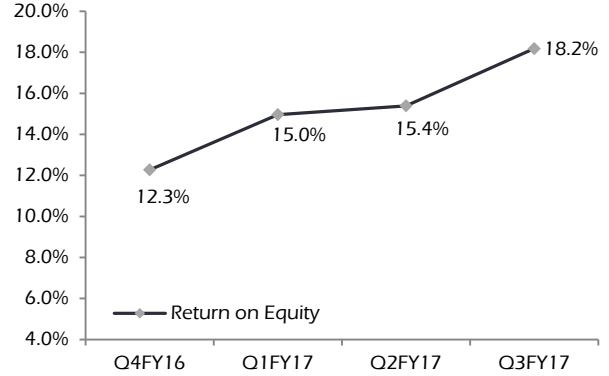


Source: Company, LKP Research

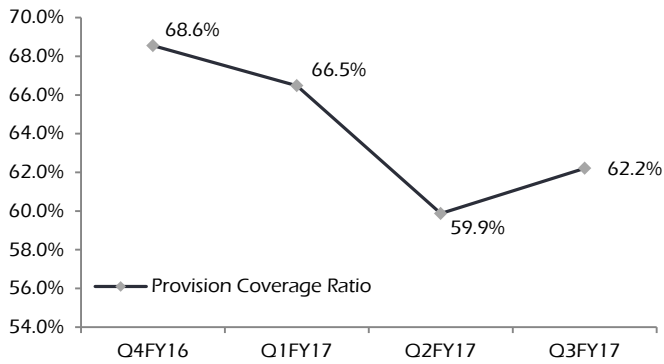
ROA



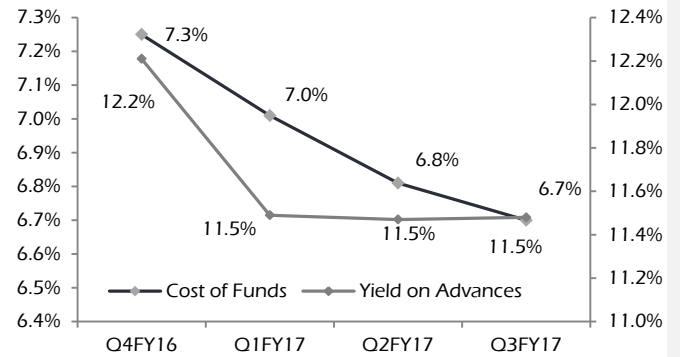
ROE



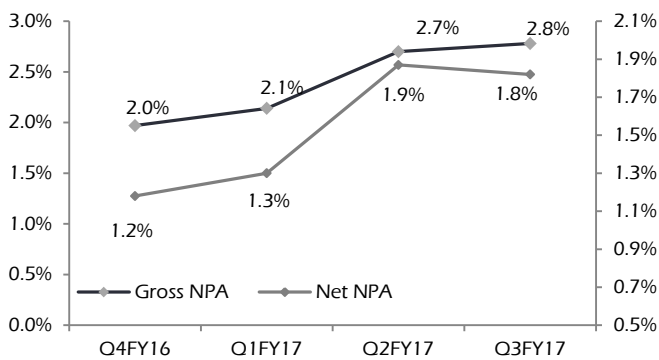
Provision Coverage Ratio



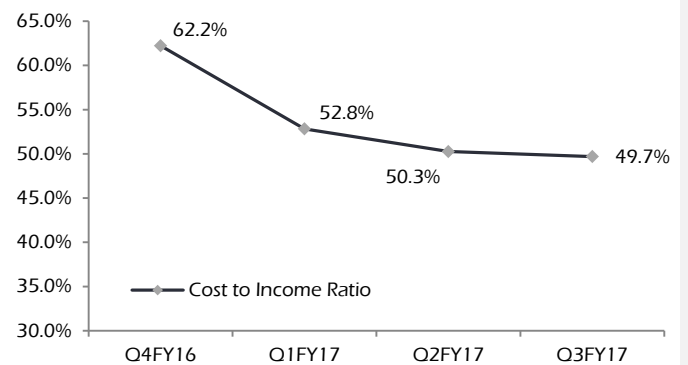
Cost of Funds & Yield on Advances



Gross NPA & Net NPA



Cost to Income Ratio



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