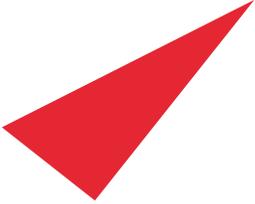


Pick of the Week

Karnataka Bank Ltd.

May 26, 2025



Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
BFSI – Pvt. Bank	Rs 196	Buy in Rs 192-200 band & add on dips in Rs 174-182 band	Rs 219	Rs 239	2-3 quarters

HDFC Scrip Code	KARBANEQNR
BSE Code	532652
NSE Code	KTKBANK
Bloomberg	KBL IN
CMP May 23, 2025	196.2
Equity Capital (Rs Cr)	377.9
Face Value (Rs)	10
Equity Share O/S (Cr)	37.8
Market Cap (Rs Cr)	7416
Adj. Book Value (Rs)	279.9
Avg. 52 Wk Volumes	1721754
52 Week High	245.0
52 Week Low	162.2

Share holding Pattern % (Mar 2025)	
Promoters	0.0
Institutions	31.0
Non Institutions	69.0
Total	100.0



* Refer at the end for explanation on Risk Ratings

Fundamental Research Analyst

Atul Karwa

atul.karwa@hdfcsec.com

Our Take:

Karnataka Bank (KBL) is a century-old scheduled commercial bank with presence predominantly in South India. Over the past few years, the bank has strengthened its top management, invested in digital infrastructure, set up dedicated collection teams, and tied up with multiple financial institutions to launch and cross-sell new products. FY25 witnessed a muted loan book growth due to a slowdown in economic activity and a change in product mix. With the bank leaning towards direct-to-corporate and higher-yielding retail loans, NIMs and return ratios are expected to improve in the coming years.

Investments in digital initiatives are likely to drive operating costs lower. We believe fresh slippages and credit costs will remain benign due to higher recoveries and improved credit assessment. The restructured book is also contracting, which should release growth capital for the bank. Capitalization levels remain comfortable post the equity raise the bank made in FY24.

Valuation & Recommendation:

The bank's reduced provisioning requirement is likely to aid profitability and return ratios, which are expected to remain stable. We feel that investors can buy the stock in the band of Rs 192-200 and add on dips in the Rs 174-182 band (0.51x FY27E ABV) for a base case fair value of Rs 219 (0.63x FY27E ABV) and a bull case fair value of Rs 239 (0.69x FY27E ABV) over the next 2-3 quarters.

Financial Summary:

Particulars (Rs cr)	Q4FY25	Q4FY24	YoY (%)	Q3FY25	QoQ (%)	FY24	FY25	FY26E	FY27E
Net Interest Income	781	834	-6.4	793	-1.5	3299	3310	3360	3871
PPoP	375	500	-25.0	433	-13.4	2188	1827	1960	2365
APAT	252	274	-8.0	284	-11.0	1331	1272	1293	1555
Diluted EPS (Rs)	6.7	7.3	-8.1	7.5	-11.0	35.3	33.7	34.2	41.1
P/E (x)						5.7	5.9	5.8	4.9
P/ABV (x)						0.8	0.7	0.7	0.6
RoAA (%)						1.2	1.1	1.0	1.1

Q4Y25 Result Update

KBL reported subdued results for Q4FY25 as PAT declined 8% YoY to Rs 252cr on account of lower NII. NII declined 6/2% YoY/QoQ on NIM compression by 34/4 bps YoY/QoQ to 2.98%. Yields declined 39bps YoY to 9.43% while CoF increased 24bps to 5.83%. Opex growth was elevated at 11/30% YoY/QoQ, driven by higher employee expenses (+20/53% YoY/QoQ) resulting in a higher C-I Ratio at 69% vs 60.1% YoY. Consequently, PPOP de-grew by 25/13% YoY/QoQ to Rs 375cr. Loan book grew 7% YoY to Rs 76,541cr. RoA/RoE compressed 11/208bps YoY to 0.81/8.56%.

Asset quality improved marginally with GNPA/NNPA down 3/8bps QoQ and stood at 3.08/1.31%. Annualised credit costs were benign at 16bps as compared to 103/44bps YoY/QoQ aided by healthy recoveries. The standard restructured book declined 37/11% YoY/QoQ to Rs 995cr, constituting 1.3% of loans. SMA-2 was stable at 1.2% (down 6bps QoQ).

Management guidance for FY26:

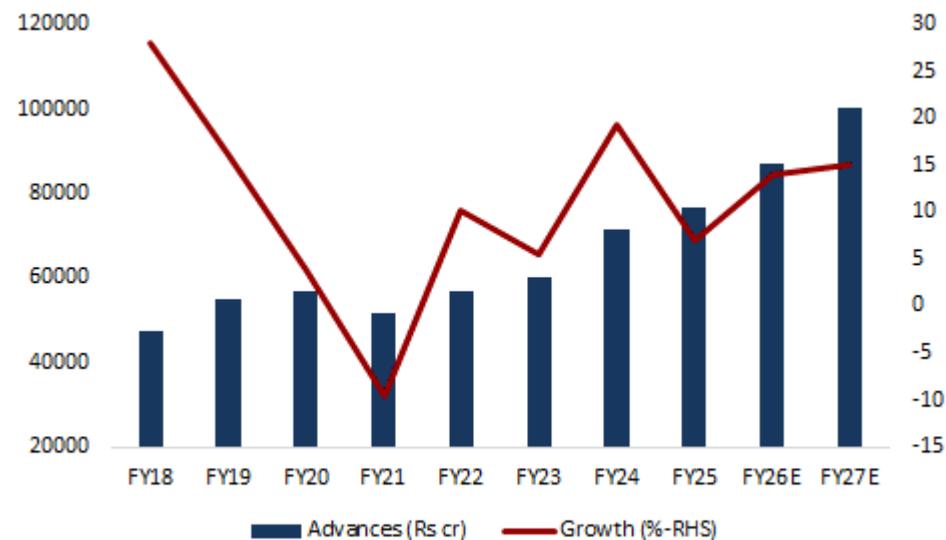
- NIM – 3.2-3.4%
- Cost-Income – 53-56%
- RoA – 1.1-1.2%
- NNPA – 0.9-1.1%

Key Triggers

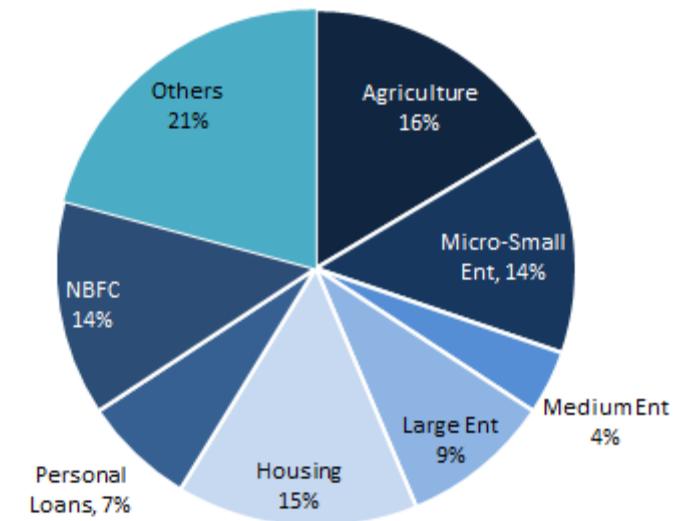
Advances growth to pick up with focus on retail

Growth in advances was muted for FY25 at 7% YoY on account of a slowdown in credit growth in the economy as well as churn in bank's portfolio. KBL relied on corporate loans in the past for its growth as it was setting up its retail infrastructure. Going forward, it plans to focus on growing the retail book where the yields are much higher. In the last financial year, it has launched 15 products, and five each in liabilities, retail, and in the MSME segments. The Retail book has grown ~16% YoY in FY25 and accounts for 50% of the total advances. We expect KBL's loan book to expand ~15% CAGR over FY25-FY27 with the share of retail advances increasing further.

Growth in Advances



Advances Mix

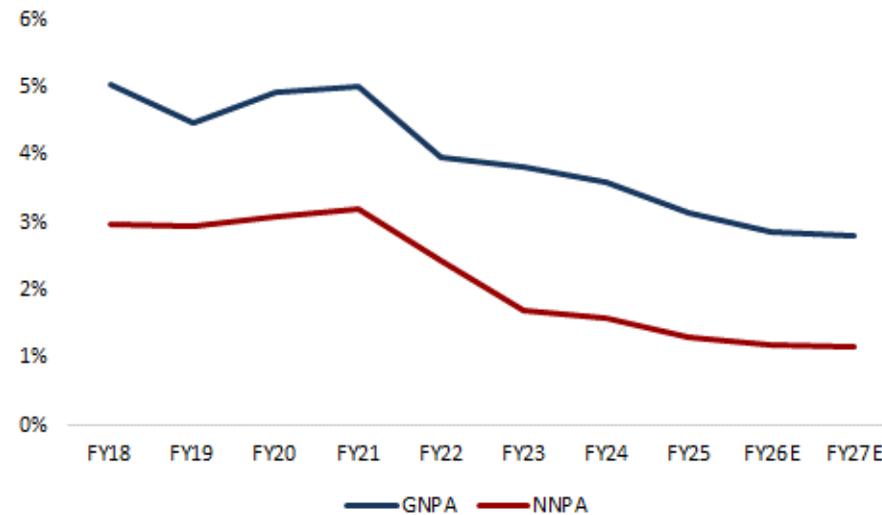


(Source: Company, HDFC sec)

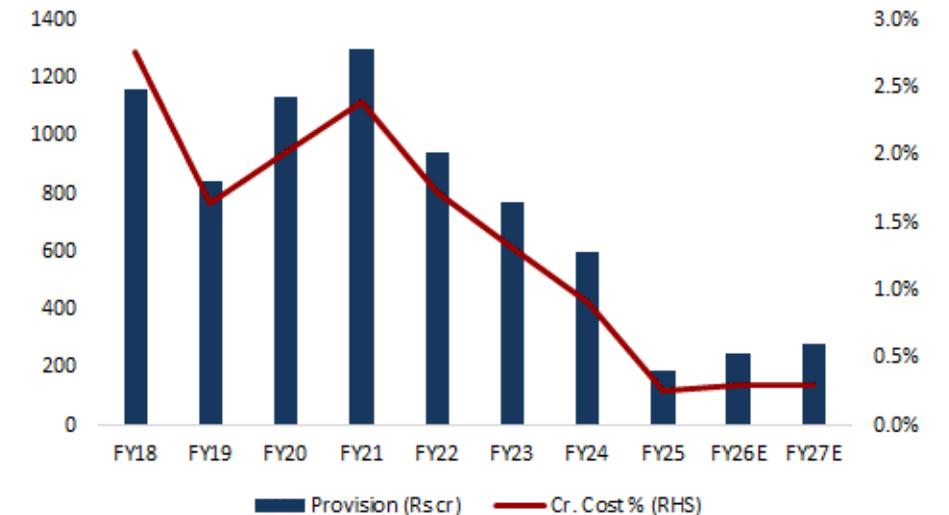
Moderate slippages and recoveries to drive asset quality improvement

The asset quality of the bank has been on an improvement trajectory since the Covid pandemic. It has strengthened credit underwriting mechanism, set-up a dedicated collection team and enhanced monitoring to arrest the asset quality deterioration. GNPA/NNPA improved to 3.14/1.31% in FY25 from 3.61/1.58% in FY24. Slippages have also come down significantly, with gross slippages of 1.7% in FY25 against 2.8% in FY24. With a lower stress pipeline, net slippages are expected to remain moderate. We expect credit costs to stay in the range of 0.5% and GNPA/NNPA to improve further.

Improving asset quality....



...leading to lower credit costs



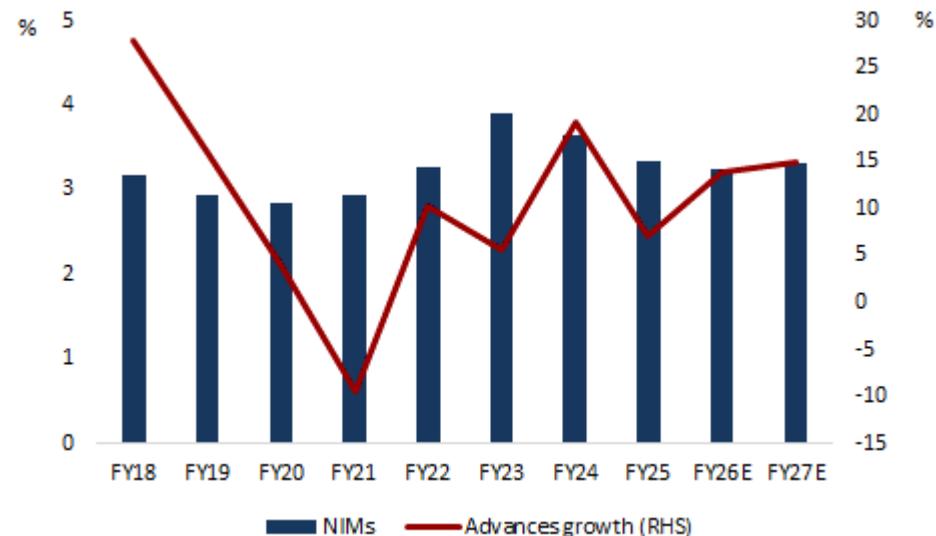
Source: Company, HDFCsec

Restructured advances have also seen sharp reduction of 37% YoY to Rs 995cr. Off these, ~50% is standard, with timely repayments. However, owing to regulatory requirements of not classifying a restructured account as standard until 30% of the repayment is done, these accounts continue to remain in the restructured book. The bank has also set up a collection team for the retail vertical as it looks to accelerate growth in the portfolio, while avoiding any accidents on the asset quality front. Upgradation of these accounts could further improve profitability.

NIMs to expand

KBL is focusing on increasing the share of higher yielding retail assets which is likely to drive its NIM expansion. The management has guided for NIMs of 3.2-3.4% in FY26 against 3.2% in FY25. Within corporate loans, the bank is looking to replace its low yielding NBFC advances to direct-to-corporate and retail loans. The bank replaced ~Rs 1200cr of low-yielding NBFCs to higher-yielding direct-to-corporate advances in FY25.

NIMs to witness 10-15bps expansion



Source: Company, HDFCsec

Comfortable capitalization level

KBL's capitalisation profile remains comfortable with a capital ratio of 19.85% as of Mar'25 remains comfortable compared to the regulatory requirement of 9.50%. The capitalisation levels were supported by the equity capital raise of Rs 1500cr in FY24, which will aid its growth plans for the medium term. We expect KBL to maintain comfortable capital cushions over and above the regulatory requirements as well as the negative triggers.

Return ratios to remain stable

Profits of KBL was impacted in FY25 due to certain one-off expenses like Actuarial Provisioning for Employee Retiral Benefits, increase in salaries due to 12th Bipartite Settlement and changes in some accounting policies. Further NII growth was muted due to higher cost of funds. Improved asset quality and higher recoveries would drive lower credit costs. Various cost rationalization efforts, including renegotiating rentals, vendor commercials, and keeping operating expenses under check are happening. With the increase in NII and NIM we believe cost to income should come down to about 55-56% by FY27.

Return ratios



Source: Company, HDFCsec

Risks & Concerns

High geographic concentration

KBL derives more than half of its business from ~63% of its branches located in the state of Karnataka. Any change in the socio-political scenario or a natural calamity could impact its borrowers and worsen the asset quality.

Competitive intensity in its retail foray

Due to higher stress in corporate loans, most banks are looking at retail and MSME segments for growth. KBL is likely to face greater competitive intensity as it looks to expand its retail footprint, which might impact its fee income.

Deterioration in asset quality

Any deterioration in asset quality due to prolonged economic slowdown can result in higher provisioning requirements leading to lower profitability.

Absence of promoter group

The bank does not have a clearly identified promoter group or a large shareholder, which results in lower financial flexibility, lower drive and a relatively low likelihood of bail out support in case of any unforeseen distress.

Company Background

Established in 1924 at Mangalore, Karnataka Bank (KBL) is a leading 'A' Class Scheduled Commercial Bank in India. The bank took shape in the aftermath of patriotic zeal that engulfed the nation during the freedom movement of 20th Century India. Over the years the Bank grew with the merger of Sringeri Sharada Bank Ltd., Chitradurga Bank Ltd. and Bank of Karnataka. In 100 years of its presence KBL has built a network of 952 branches spread across 22 states and 2 Union Territories. KBL is not involved in insurance business but holds 6% stake in Universal Sampo General Insurance.

As a premier bank, it has developed comprehensive range of customized products & services suitable for every kind of market, trade or perceived need - Business or Personal. These include, borrowing facilities, deposits, providing optimum returns on surplus funds or helping with overseas transactions. It is transforming itself into a technologically advanced bank looking at the needs of the future.

Over the last five years, from FY20 to FY25, the bank's total business has grown at a CAGR of 9% to ~Rs 1.81 lakh crore, with advances growing at 10.4% to ~Rs 0.77 lakh crore and deposits growing at 8.5% to ~Rs 1.05 lakh crore. As of March'25, almost 60% of the bank's branches were in Karnataka, with South India accounting for 76%. The bank added 31 branches in FY25, taking the total network to 952 branches.

Karnataka Bank is undergoing a comprehensive structural transformation under new management, having evolved from a bank with a mediocre track record into a future-ready institution. After experiencing stability during FY05-13 followed by a stressed period in FY14-20, the bank has strategically rebuilt itself by replacing approximately half of its senior management team, including the CEO, CFO, CPO, and CIO, with external industry talent over the past two years. This transformation encompasses departmental reorganisation, robust underwriting processes, cross-selling initiatives, dedicated collection teams, enhanced technology frameworks, and strategic partnerships with insurance and wealth management companies. The bank now stands poised for growth rejuvenation, supported by a comfortable loan-to-deposit ratio and strong liquidity coverage ratio.

Financials

Income Statement

(Rs cr)	FY23	FY24	FY25	FY26E	FY27E
Interest Income	7220	8299	9014	9851	10912
Interest Expenses	4035	5000	5703	6242	6716
Net Interest Income	3185	3299	3310	3609	4196
Non interest income	993	1319	1270	1481	1601
Operating Income	4178	4618	4580	5090	5797
Operating Expenses	1901	2430	2753	2878	3101
PPoP	2276	2188	1827	2212	2696
Prov & Cont	767	601	186	259	288
Profit Before Tax	1509	1587	1641	1953	2408
Tax	261	256	368	469	607
PAT	1248	1331	1272	1484	1801

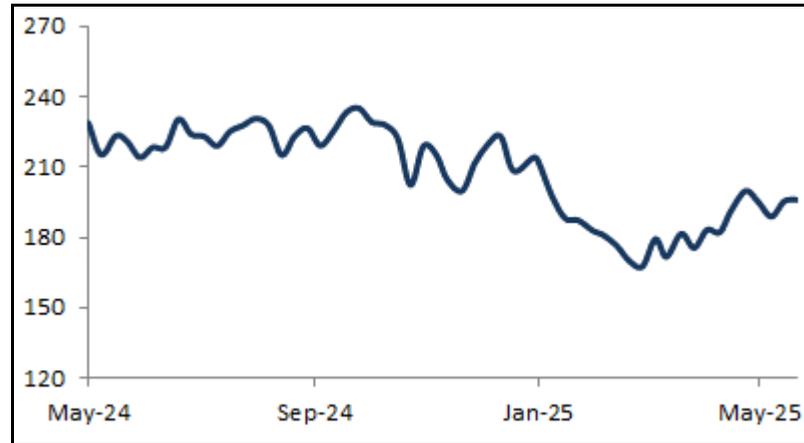
Balance Sheet

(Rs cr)	FY23	FY24	FY25	FY26E	FY27E
Share Capital	312	377	378	378	378
Reserves & Surplus	7901	10471	11707	12942	14437
Shareholder funds	8213	10849	12085	13320	14815
Deposits	87368	98058	104807	115013	127305
Borrowings	1563	4400	1941	3521	5017
Other Liab & Prov.	2017	2899	2128	2582	2009
SOURCES OF FUNDS	99161	116205	120961	134436	149146
Cash & Bank Balance	6159	7993	7984	8362	8529
Investment	23326	24302	24537	26407	29100
Advances	59952	71509	76541	88023	100346
Fixed Assets	875	915	991	1063	1118
Other Assets	8848	11487	10909	10582	10053
TOTAL ASSETS	99161	116205	120961	134436	149146

Ratio Analysis

Particulars	FY23	FY24	FY25	FY26E	FY27E
Return Ratios (%)					
Yield on adv	9.6	9.9	9.5	9.5	9.3
Cost of funds	4.7	5.2	5.5	5.5	5.4
NIM	3.9	3.7	3.3	3.3	3.4
RoAE	16.3	14.0	11.1	11.7	12.8
RoAA	1.3	1.2	1.1	1.2	1.3
Asset Quality Ratios (%)					
GNPA	3.8	3.6	3.1	2.8	2.8
NNPA	1.7	1.6	1.3	1.2	1.2
PCR	55.5	56.2	58.1	58.1	58.2
Growth Ratios (%)					
Advances	5.6	19.3	7.0	15.0	14.0
Borrowings	-32.5	181.5	-55.9	81.4	42.5
NII	27.9	3.6	0.4	9.0	16.3
PPoP	44.3	-3.9	-16.5	21.1	21.9
PAT	176.1	6.6	-4.4	16.6	21.4
Valuation Ratios					
EPS (Rs)	40.0	35.3	33.7	39.3	47.7
P/E (x)	4.9	5.6	5.8	5.0	4.1
Adj. BVPS (Rs)	213.9	244.2	279.9	311.4	347.7
P/ABV (x)	0.9	0.8	0.7	0.6	0.6
Dividend per share (Rs)	5.0	5.5	5.5	6.6	8.1
Dividend Yield (%)	2.5	2.8	2.8	3.4	4.1
Other Ratios					
Cost-Income	45.5	52.6	60.1	56.5	53.5
Credit-Deposit	68.6	72.9	73.0	76.5	78.8

Price chart



HDFC Sec Prime Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. These stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicity of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

Disclosure:

I, **Atul Karwa, Research Analyst, MMS**, author and the name subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. SEBI conducted the inspection and based on their observations have issued advise/warning. The said observations have been complied with. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

Research Analyst or his/her relative or HDFC Securities Ltd. **does not have** any financial interest in the subject company. Also Research Analyst or his relative or HDFC Securities Ltd. or its Associate may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Further Research Analyst or his relative or HDFC Securities Ltd. or its associate **does not have** any material conflict of interest.

Any holding in stock – No

HDFC Securities Limited (HSL) is a SEBI Registered Research Analyst having registration no. INH000002475.

Disclaimer:

This report has been prepared by HDFC Securities Ltd and is solely for information of the recipient only. The report must not be used as a singular basis of any investment decision. The views herein are of a general nature and do not consider the risk appetite or the particular circumstances of an individual investor; readers are requested to take professional advice before investing. This report may have been refined using AI tools to enhance clarity and readability. Nothing in this document should be construed as investment advice. Each recipient of this document should make such investigations as they deem necessary to arrive at an independent evaluation of an investment in securities of the companies referred to in this document (including merits and risks) and should consult their own advisors to determine merits and risks of such investment. The information and opinions contained herein have been compiled or arrived at, based upon information obtained in good faith from sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. Descriptions of any company or companies or their securities mentioned herein are not intended to be complete. HSL is not obliged to update this report for such changes. HSL has the right to make changes and modifications at any time.

This report is not directed to, or intended for display, downloading, printing, reproducing or for distribution to or use by, any person or entity who is a citizen or resident or located in any locality, state, country or other jurisdiction where such distribution, publication, reproduction, availability or use would be contrary to law or regulation or what would subject HSL or its affiliates to any registration or licensing requirement within such jurisdiction.

If this report is inadvertently sent or has reached any person in such country, especially, United States of America, the same should be ignored and brought to the attention of the sender. This document may not be reproduced, distributed or published in whole or in part, directly or indirectly, for any purposes or in any manner.

Foreign currencies denominated securities, wherever mentioned, are subject to exchange rate fluctuations, which could have an adverse effect on their value or price, or the income derived from them. In addition, investors in securities such as ADRs, the values of which are influenced by foreign currencies effectively assume currency risk. It should not be considered to be taken as an offer to sell or a solicitation to buy any security.

This document is not, and should not, be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. This report should not be construed as an invitation or solicitation to do business with HSL. HSL may from time to time solicit from, or perform broking, or other services for, any company mentioned in this mail and/or its attachments.

HSL and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

HSL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

HSL and other group companies, its directors, associates, employees may have various positions in any of the stocks, securities and financial instruments dealt in the report, or may make sell or purchase or other deals in these securities from time to time or may deal in other securities of the companies / organizations described in this report. As regards the associates of HSL please refer the website.

HSL or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

HSL or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction in the normal course of business.

HSL or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither HSL nor Research Analysts have any material conflict of interest at the time of publication of this report. Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. HSL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Research entity has not been engaged in market making activity for the subject company. Research analyst has not served as an officer, director or employee of the subject company. We have not received any compensation/benefits from the subject company or third party in connection with the Research Report.

Please note that HDFC Securities has a proprietary trading desk. This desk maintains an arm's length distance with the Research team and all its activities are segregated from Research activities. The proprietary desk operates independently, potentially leading to investment decisions that may deviate from research views.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Murli V Karkera Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

For grievance redressal contact Customer Care Team Email: customer care@hdfcsec.com Phone: (022) 3901 9400

HDFC Securities Limited, SEBI Reg. No.: NSE, BSE, MSEI, MCX: INZ000186937; AMFI Reg. No. ARN: 13549; PFRDA Reg. No. POP: 11092018; IRDA Corporate Agent License No.: CA0062; SEBI Research Analyst Reg. No.: INH000002475; SEBI Investment Adviser Reg. No.: INA000011538; CIN - U67120MH2000PLC152193

Investment in securities market are subject to market risks. Read all the related documents carefully before investing.

Mutual Funds Investments are subject to market risk. Please read the offer and scheme related documents carefully before investing.

Registration granted by SEBI, membership of BASL (in case of IAs) and certification from NISM in no way guarantee performance of the intermediary or provide any assurance of returns to investors.