

Current	Previous
<b>CMP : Rs. 97</b>	
<b>Rating : BUY</b>	<b>Rating : NA</b>
<b>Target : Rs. 113</b>	<b>Target : NA</b>

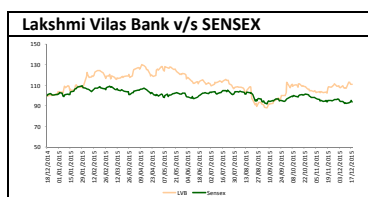
STOCK INFO	
Bse	534690
Nse	LAKSHVILAS
Bloomberg	LVB IN
Reuters	LVLS.NS
Sector	Private Sector Banks
Face Value (Rs)	10
Equity Capital (Rs Mn)	1795
Mkt Cap (Rs Mn)	16,331
52w H/L (Rs)	111 / 64
Avg Daily Vol (Bse+Nse)	927,897

SHAREHOLDING PATTERN (as on Sept. 2015)	%
Promoter	9.7
FII	9.1
DII	7.7
Others	73.5

Source: BSE

STOCK PER. (%)	1m	3m	12m
LVB	8%	16%	11%
Sensex	0%	-3%	-6%

Source: Capitaline, IndiaNivesh Research



Source: Capitaline, IndiaNivesh Research

## Company Background

Lakshmi Vilas Bank (LVB) is a small old generation private sector bank from south India with largely regional operations and especially in the state of Tamilnadu. The bank is able to grow its business at a CAGR of 20% to Rs 383 bn and Net Profit at a CAGR of 34% in the last 5 Years. As of FY15, LVB has network of 400 branches & 820 ATMs. Going forward the bank is expected to grow its presence in urban and metro cities across PAN India. In a bid to shed its 'old-generation' image, LVB has strengthened its top management and has undertaken a rebranding exercise to evolve as a new-age bank.

## Investment Rationale:

### Business growth to remain healthy with significant focus on SME / Retail segments:

LVB's business has grown at a healthy pace of 20% CAGR over FY10-15 attributed by 21% and 19% CAGR growth in Advances and Deposits over the same period, respectively. We believe this business growth momentum to continue over FY15-17E mainly led by retail and SME segments. We expect the bank's advances and deposits to grow at a CAGR of 18% and 16%, respectively over FY15-17E.

### Branch expansion to drive CASA growth going ahead:

LVB wants to increase the share of low-cost CASA deposits from 14% as of FY14 to 25% by increasing the share of CASA by 2% every year. The Bank management is also planning to add 70 to 80 branches per year going forward. We expect the expansion of branch network is likely to help CASA deposits to grow at a CAGR of 26% over FY15-17E and CASA ratio is likely to improve to 19.5% by FY17E.

### Return Ratios are likely to improve backed by improved asset quality:

The bank posted a decent improvement in FY15 as the bank reported Return on Equity (RoE) of 10.1% and Return on Assets (RoA) of 0.6% from RoE of 5.8% and RoA of 0.3% as of FY14. LVB's concerted efforts to reduce costs, along with lower provisions and write-offs should drive profitability. We expect the bank's net profit to grow at a CAGR of 26% over FY15-17E.

### Steady improvement visible; Asset quality continue to improve:

There has been a tremendous improvement in LVB's asset quality over the past few quarters, driven by significant reduction in slippages and substantial recoveries / upgradations and selling of a few NPAs. The Gross NPA has reduced from 5.6% in Q3FY14 to 2.8% at end of Q4FY15. The Net NPA has also fallen to 1.9% from 4.3% in the same period. We expect Gross NPA / Net NPA to improve further to 1.6% / 0.9%, respectively by FY17E.

## Outlook and Valuation:

LVB is on the right track of recovery with improvement in economy. We believe that LVB will continue with its healthy growth, while maintaining its healthy capitalisation and stable asset quality over the medium term. At CMP of Rs 97/-, the stock is trading at P/ABV of 1.1x and 1.0x for FY16E and FY17E respectively. With improving return profile, we believe it provides attractive risk reward opportunity. Hence we recommend 'BUY' rating on the stock with target price of Rs 113/-, valuing it at 1.3x P/ABV of FY17E (+16% upside).

## Financial Highlights:

Rs mn	NII	PAT	EPS (Rs)	ROA (%)	ROE (%)	BV (Rs)	ABV (Rs)	P/E	P/BV	P/ABV
FY12	3,712	1,070	11	0.7	11.6	98	80	9.2	1.0	1.3
FY13	3,920	916	9	0.5	9.3	104	75	8.9	0.8	1.1
FY14	4,860	597	6	0.3	5.8	108	63	11.3	0.6	1.1
FY15	5,267	1,323	7	0.6	10.1	87	70	12.1	1.0	1.3
FY16E	6,521	1,719	10	0.6	10.6	94	82	9.3	1.0	1.1
FY17E	7,685	2,143	12	0.7	12.2	103	91	7.5	0.9	1.0

Source: Company, IndiaNivesh Research

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## Financials:

Income Statement (Rs mn)	FY13	FY14	FY15	FY16E	FY17E
Interest Income	17,605	19,840	22,145	25,872	29,644
Interest Expense	13,685	14,979	16,879	19,352	21,959
<b>Net Interest Income</b>	<b>3,920</b>	<b>4,860</b>	<b>5,267</b>	<b>6,521</b>	<b>7,685</b>
Non Interest Income	1,971	2,180	2,840	3,184	3,870
Net Income	5,891	7,040	8,107	9,704	11,555
Operating Expenses	3,379	3,950	4,343	5,193	6,095
Total Income	19,576	22,019	24,986	29,056	33,514
Total Expenditure	17,065	18,929	21,221	24,544	28,054
<b>Pre Provisioning Profit</b>	<b>2,511</b>	<b>3,090</b>	<b>3,764</b>	<b>4,512</b>	<b>5,460</b>
Provisions	1,134	2,686	1,882	2,066	2,412
<b>Profit Before Tax</b>	<b>1,378</b>	<b>404</b>	<b>1,882</b>	<b>2,446</b>	<b>3,049</b>
Tax	462	-193	559	727	906
<b>Net Profit</b>	<b>916</b>	<b>597</b>	<b>1,323</b>	<b>1,719</b>	<b>2,143</b>

Balance Sheet (Rs Mn)	FY13	FY14	FY15	FY16E	FY17E
<b>Liabilities</b>					
Capital	975	976	1,792	1,795	1,795
Reserves and Surplus	9,168	9,560	13,770	15,002	16,614
Deposits	156,190	185,729	219,642	256,405	297,840
Borrowings	4,800	4,581	4,581	6,603	7,774
Other Liabilities and Provisions	5,534	5,685	7,270	8,061	8,908
<b>Total Liabilities</b>	<b>176,667</b>	<b>206,532</b>	<b>247,054</b>	<b>287,866</b>	<b>332,931</b>
<b>Assets</b>					
Cash And Balances	8,719	13,117	13,187	14,743	16,381
Investments	43,245	56,887	61,038	69,972	79,790
Advances	117,028	128,892	163,520	192,088	226,165
Fixed Assets	1,898	2,005	2,434	2,556	2,684
Other Assets	5,776	5,630	6,875	8,507	7,911
<b>Total Assets</b>	<b>176,667</b>	<b>206,532</b>	<b>247,054</b>	<b>287,866</b>	<b>332,931</b>

## Ratios

Per share data (Rs)	FY13	FY14	FY15	FY16E	FY17E
EPS	9.4	6.1	7.4	9.6	11.9
DPS	3.0	1.0	2.0	2.2	2.5
BV	104.0	108.0	86.9	93.6	102.6
ABV	74.9	62.5	70.0	82.1	91.3

## Valuation (%)

P/E	8.9	11.3	12.1	9.3	7.5
P/BV	0.8	0.6	1.0	1.0	0.9
P/ABV	1.1	1.1	1.3	1.1	1.0
Div Yield	3.6	1.4	2.2	2.5	2.8

## Spreads (%)

Yield on Advances	12.7	12.9	11.7	11.5	11.3
Yield on Investments	7.8	7.6	8.1	7.9	7.7
Yield on Funds	11.5	11.5	10.8	10.6	10.4
Cost of Deposits	8.7	8.4	8.0	0.0	0.0
Cost of Borrowings	13.1	14.2	13.4	0.0	0.0
Cost of Funds	8.9	8.5	8.1	7.9	7.7

## Capital (%)

CAR	12.3	10.9	11.3	10.5	10.0
Tier I	9.2	7.9	9.3	8.6	8.2
Tier II	3.2	3.0	2.0	1.9	1.8

## Asset (%)

GNPA	3.9	4.2	2.8	1.9	1.6
NNPA	2.4	3.4	1.9	1.1	0.9
PCR	54.5	53.2	60.8	70.0	70.0

## Management (%)

Credit / Deposit	74.9	69.4	74.4	74.9	75.9
Cost / Income	57.4	56.1	53.6	53.5	52.7
CASA	14.5	14.2	16.7	18.0	19.5

## Earnings (%)

NIM	2.6	2.8	2.6	2.7	2.7
ROE	9.3	5.8	10.1	10.6	12.2
ROA	0.5	0.3	0.6	0.6	0.7

## Liquidity (%)

C&B / D&B	5.4	6.9	5.9	5.6	5.4
C&B / Deposit	5.6	7.1	6.0	5.8	5.5

\*C&B: Cash & Bank Balance; D: Deposits; B: Borrowings; DD: Demand Deposits

## Growth Ratios (%)

Advances	14.9	10.1	26.9	17.5	17.7
Deposits	10.7	18.9	18.3	16.7	16.2
Total Assets	8.8	16.9	19.6	16.5	15.7
Networth	5.8	3.9	47.7	7.9	9.6
NII	5.6	24.0	8.4	23.8	17.9
Pre Provisioning Profit	6.7	23.0	21.8	19.9	21.0
Provisions	3.6	136.9	-29.9	9.7	16.7
Net Profit	-14.4	-34.9	121.7	30.0	24.6

Source: Company, IndiaNivesh Research

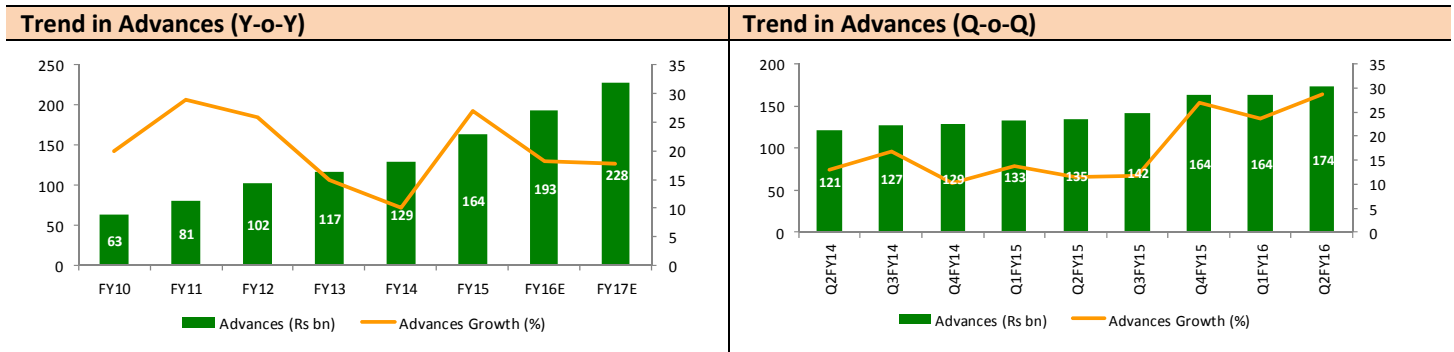
**Investment Rationale:**

**Business growth to remain healthy with significant focus on SME / Retail segments:**

*We expect the bank's advances to grow at a CAGR of 18% over FY15-17E.*

LVB's business has grown at a healthy pace of 20% CAGR over FY10-15 attributed by 21% and 19% CAGR growth in Advances and Deposits over the same period, respectively. In FY15, LVB reported 27% y-o-y growth in its advances to Rs 164 bn mainly led by corporate segment. In addition to, the bank also had a benefit of small base.

Going forward, the company's focus will be more on retail and SME segments. The management has guided for 22% y-o-y growth in advances mainly led by 25% y-o-y growth in retail and SME segments in FY16. In order to achieve this, the bank has made some of its personal, home loan and loan against property products more attractive. It is also aggressively marketing these products. However, we remain cautious and expect gradual pick up in retail / SME loan book. For lending towards large corporate, the management would like to remain conservative and would avoid sectors which are prone to higher default risk and limit incremental lending to highly rated corporates. We expect the bank's advances to grow at a CAGR of 18% over FY15-17E.

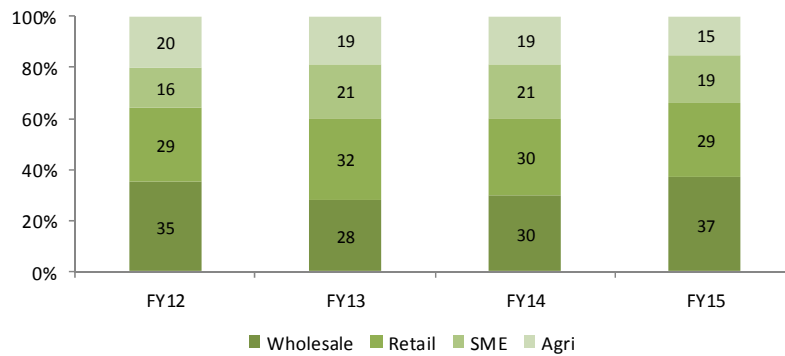


Source: Company, IndiaNivesh Research

Source: Company, IndiaNivesh Research

Exposure to Wholesale, Retail, SME and Agri stood at 37%, 29%, 19% and 15%, respectively as of FY15. The management would like to maintain the loan portfolio mix, more or less, at the current level or the retail and SME percentage level should be slightly higher in FY16.

**Composition of Loan Book (in terms of %)**



Source: Company, IndiaNivesh Research

*Majorly present in the state of Tamilnadu*

LVB like most of its peers; was primarily lender to Retail and SME/MSME customers which were largely located in the state of Tamilnadu. However, the bank will have the benefit of it as the average credit growth in Tamilnadu has remained higher than the average credit growth of the whole country. As the bank also foresees good business potential in Tamilnadu, it has shifted its corporate office to Chennai from Karur.

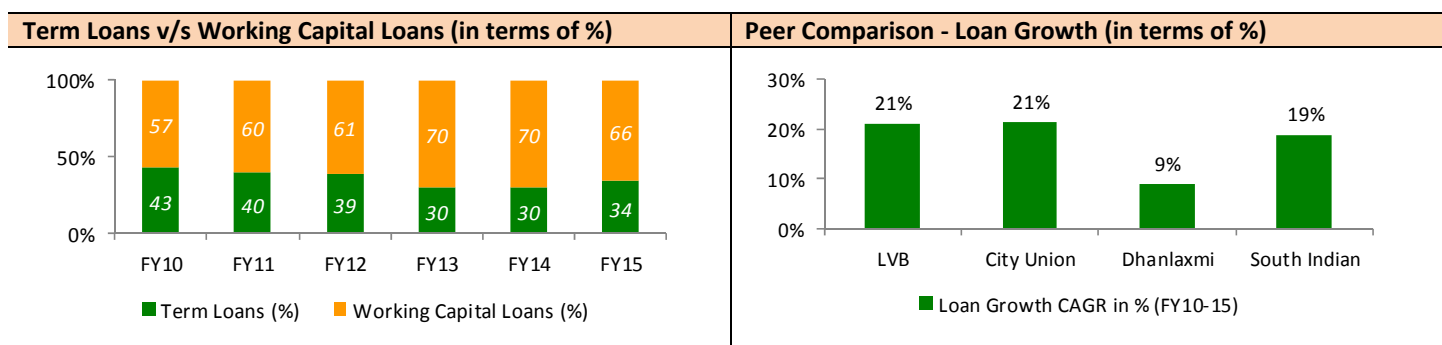
**Credit Growth (in terms of %)**

Region	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Northern	28.2	21.9	22.8	22.5	27.8	17.0	14.3
North-Eastern	26.7	18.7	15.9	20.0	14.1	18.7	14.2
Eastern	27.7	20.4	19.2	22.7	18.2	17.0	14.2
Central	26.5	19.3	18.0	21.6	19.7	16.7	19.2
Western	29.2	23.4	16.2	10.3	20.5	16.9	14.7
Southern	28.5	24.6	21.6	19.0	20.5	18.4	15.6
- Tamilnadu	26.8	22.5	16.5	21.7	22.0	18.3	17.8
<b>All India</b>	<b>28.5</b>	<b>22.8</b>	<b>19.3</b>	<b>17.1</b>	<b>21.9</b>	<b>17.3</b>	<b>15.1</b>
LVB		6.8	35.7	19.9	28.9	25.9	14.9

Source: Company, RBI, IndiaNivesh Research

*Continue to prefer short term / working capital loans*

The bank continues to prefer short term / working capital loans as that provides better liquidity with healthy margins. In addition to, the residual maturity of these loans also remains very low.



Source: Company, IndiaNivesh Research

Source: Company, IndiaNivesh Research

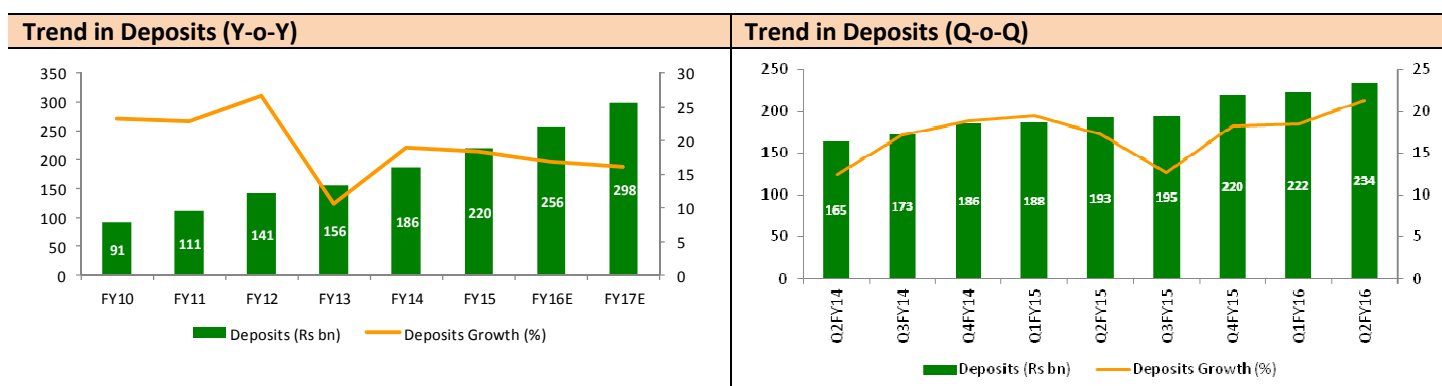
*Liability profile remains largely retail funded and retail term deposits constitute 66% of total deposits as of FY15*

*We expect the bank's deposits to grow at a CAGR of 16% over FY15-17E.*

**Thrust towards retail deposits to continue:**

In FY15, LVB reported 18% y-o-y growth in its deposits to Rs 220 bn helped by 39% y-o-y growth in CASA deposits and 15% y-o-y growth in term deposits. LVB's liability profile remains largely retail funded. The management has increased the share of retail term deposits to 66% in FY15 from 55% in FY14, while simultaneously reducing the share of bulk deposits. Retail deposits are more stable while bulk deposits hit the business hard when withdrawn suddenly.

We expect the bank's deposits to grow at a CAGR of 16% over FY15-17E.



Source: Company, IndiaNivesh Research

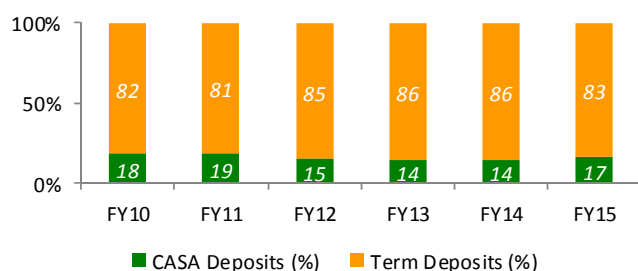
Source: Company, IndiaNivesh Research

## Deposits Growth (in terms of %)

Region	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Northern	22.5	25.5	19.3	12.6	15.2	10.6	13.0
North-East	22.1	24.0	26.5	24.8	19.7	15.1	16.6
Eastern	20.9	23.5	24.9	19.3	16.2	19.9	16.3
Central	19.7	20.7	24.2	16.7	18.1	17.7	18.8
Western	29.6	26.7	21.2	20.8	20.1	9.7	12.9
Southern	23.0	21.8	22.8	14.1	18.2	17.7	13.5
- Tamilnad	22.4	22.2	23.6	15.6	20.7	16.6	11.7
<b>All India</b>	<b>24.2</b>	<b>24.2</b>	<b>21.9</b>	<b>16.9</b>	<b>17.9</b>	<b>13.8</b>	<b>14.2</b>
LVB		11.9	31.0	23.3	22.9	26.6	10.7

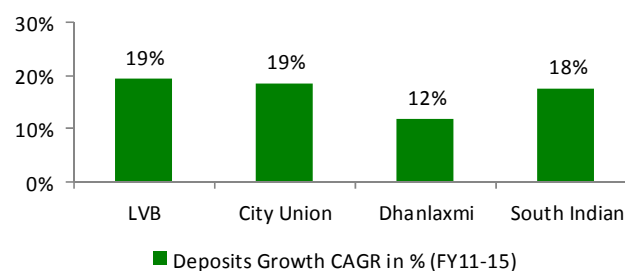
Source: Company, RBI, IndiaNivesh Research

## CASA Deposits v/s Term Deposits (in terms of %)



Source: Company, IndiaNivesh Research

## Peer Comparison - Deposits Growth (in terms of %)



Source: Company, IndiaNivesh Research

## Branch expansion to drive CASA growth going ahead:

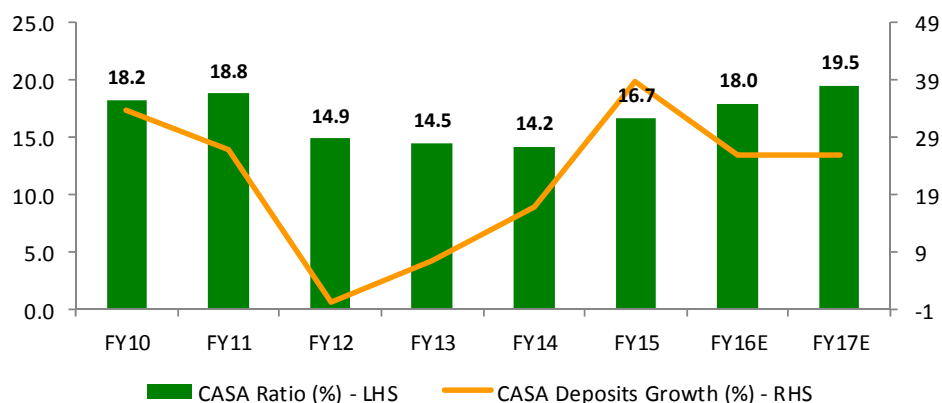
*CASA share to increase by 2% every year and eventually take it to 25%*

*CASA deposits to grow at a CAGR of 26% over FY15-17E*

LVB wants to increase share of low-cost CASA deposits from 14% as of FY14 to 25%. LVB is planning to increase the share of CASA by 2% every year to eventually take it to 25%. In order to make it attractive for customers, the bank raised the interest payable on SA balances from 4% to 5% per annum for accounts maintaining a balance of Rs 1 lakh and above. As a result, the CASA ratio of the bank improved to 16.7% as of Q4FY15 from 14.2% as of Q4FY14.

In FY15, LVB added 39 branches which helped it to increase its total branch network to 400. We believe this move will support the bank's strategy to focus and improve its CASA ratio further. In addition to, the Bank management is also planning to add 70 to 80 branches per year going forward. Thus expansion of branch network is likely to improve CASA deposit growth at a CAGR of 26% over FY15-17E and CASA ratio is likely to improve to 19.5% by FY17E. The bank can also continue to maintain its focus on retail term deposits. In addition to, LVB has also hired ~300 employees, (~9% of its employee base) mainly to source CASA deposits.

## Trend in CASA Ratio (Y-o-Y)



Source: Company, IndiaNivesh Research

**Network**

Particulars	FY12	FY13	FY14	FY15
Branches	290	291	361	400
Addition	16	1	70	39
ATM	541	651	688	820

Source: Company Filings, IndiaNivesh Research

**Geographic Presence (FY15)**

Region	Number of	
	Branches	% share
North India	12	3
West India	28	7
South India	347	87
East India	7	2
Central India	6	2
<b>Total</b>	<b>400</b>	<b>100</b>

Source: Company Filings, IndiaNivesh Research

**Branch Segmentation**

Category	Number of	
	Branches	% share
Rural	88	22
Semi Urban	136	34
Urban	108	27
Metro	68	17
<b>Total</b>	<b>400</b>	<b>100</b>

Source: Company Filings, IndiaNivesh Research

**Customer Segmentation**

Category	FY15 (mn)	% share
Rural	0.45	17
Semi Urban	1.09	41
Urban	0.75	28
Metro	0.37	14
<b>Total</b>	<b>2.67</b>	<b>100</b>

Source: Company Filings, IndiaNivesh Research

**Slow but steady improvement in Margins is likely due to increasing CASA share:**

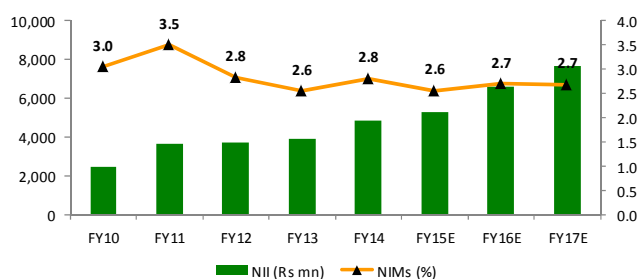
We expect NIM to improve to 2.7% by the end of FY16E

Net Interest Income (NII) to grow at a CAGR of 20% over FY15-17E

Net Interest Margin (NIM) off-late were largely volatile owing to higher slippages and consequent interest reversals. NIM (calc) was at 2.6% in FY15 as compared to 2.8% in FY14. The majority of incremental disbursement towards the end of year also impacted NIM in FY15. We expect NIM to improve to 2.7% by the end of FY16E through increasing the share of low-cost CASA deposits in its total deposits. The bank has already taken number of initiatives to increase the share of CASA deposits. In addition to, with slippages likely peaked out and higher share of retail term deposits margins should stabilize in the coming period. As expected, during declining interest rate scenario, the bank with higher share of SME / MSME book would be able to hold rates at relatively higher levels however would be able to re-price deposits at lower rate. Thus, probability of gaining margins momentum remains further high.

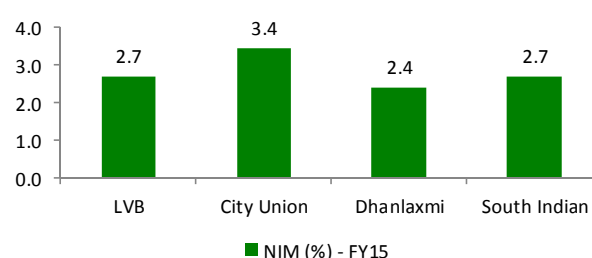
With improved margins and healthy growth in advances, we expect Net Interest Income (NII) to grow at a CAGR of 20% over FY15-17E.

**Trend in Net Interest Income and Net Interest Margins (Y-o-Y)**



Source: Company, IndiaNivesh Research

**Peer Comparison – Net Interest Margin (in terms of %)**



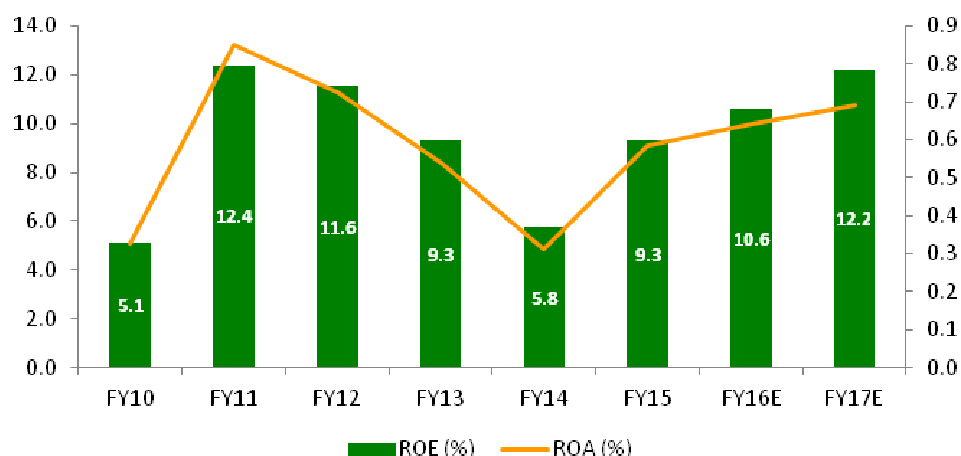
Source: Company, IndiaNivesh Research

**Return ratios likely to improve backed by improved asset quality:**

The bank's net profit to grow at a CAGR of 26% over FY15-17E

Higher credit cost (due to higher slippages) and lower other income translated into lower return ratios for LVB. However, the bank posted a decent improvement in FY15 as the bank reported Return on Equity (RoE) of 10.1% and Return on Assets (RoA) of 0.6% from RoE of 5.8% and RoA of 0.3% as of FY14. As the bank had to make a one-time provisioning of Rs 400 mn during FY14, it translated into lower return ratios. Going forward, as the management's strategy materialize, the return ratios are likely to improve further. LVB's concerted efforts to reduce costs, along with lower provisions and write-offs should drive profitability. We expect the bank's net profit to grow at a CAGR of 26% over FY15-17E.

## Trend in Return Ratios (Y-o-Y)

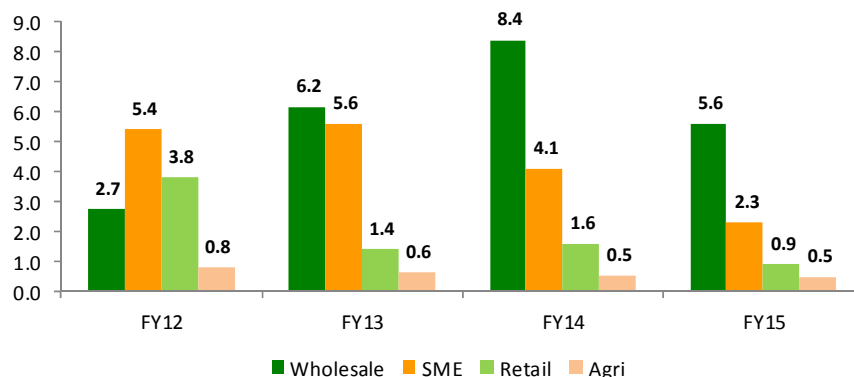


Source: Company, IndiaNivesh Research

## Steady improvement visible; Asset quality continue to improve:

LVB's Gross NPAs and Net NPA increased from 1.9% and 0.9% as of FY11 to 4.2% and 3.4% as of FY14, respectively. However, majority of this increase came from large corporates. If we analyse sector-wise Gross NPA data then Gross NPA from industry was 0.3% as of FY11 which increased to 8.8% as of FY14. During the same period, the asset quality of SME and retail loans improved significantly.

## Composition of Gross NPA (in terms of %)



Source: Company, IndiaNivesh Research

## Top ten Industry Wise distribution of Exposures - as of FY15

Industry Classification	% of total	Fund Based	% of total	Non-Fund Based
Infrastructure	6	14,376	14	2,442
Textiles	4	9,188	5	891
Basic Metal and Metal Products	4	8,380	11	1,983
Food Processing	3	5,880	5	945
Chemicals and Chemical Products	1	2,954	11	1,980
All Engineering	1	2,014	6	1,132
Mining and Quarrying	1	2,190	0	29
Cement and Cement Products	1	1,582	0	7
Beverages (excluding Tea & Coffee) and Tobacco	1	1,317	0	9
Gems and Jewellery	0	1,057	0	59
<b>Total</b>	<b>100</b>	<b>2,28,322</b>	<b>100</b>	<b>17,699</b>

Source: Company Filings, IndiaNivesh Research

*Improvement in NPA was the result of significant reduction in slippages and substantial recoveries / upgradations during FY15*

However, there has been a tremendous improvement in LVB's asset quality over the past few quarters, driven by significant reduction in slippages and substantial recoveries / upgradations and selling of a few NPAs. This has amounted to clearing of its books and the Gross NPA has reduced from 5.6% in Q3FY14 to 2.8% at the end of Q4FY15. The Net NPA has also fallen to 1.9% from 4.3% in the same period. LVB sold assets worth Rs 420 mn in FY14 and Rs 1.6 bn in FY15 to asset reconstruction companies (ARCs) to reduce the NPA pain in the large corporate book. In FY15, it has also restructured loans worth Rs 4.3 bn (Rs 2.7 bn in FY14) of corporate loans. There was no restructuring pipeline at the end of FY15. In contrast to industry trend, the management doesn't expect any slippages from its restructured portfolio and expects to upgrade Rs 1.0 bn of assets in FY16.

**Trend in Gross NPA (Y-o-Y)**

Movement of Gross NPAs: (Rs mn)	FY11	FY12	FY13	FY14	FY15
Opening balance of gross NPAs	3,252	1,578	3,077	4,599	5,465
Additions during the year	1,375	2,830	4,002	6,687	2,563
% of opening net advances	2.2	3.5	3.9	5.7	2.0
Reductions during the year	3,049	1,330	2,480	5,821	3,482
% of opening gross NPAs	93.8	84.3	80.6	126.6	63.7
Closing balance of gross NPAs	1,578	3,077	4,599	5,465	4,546

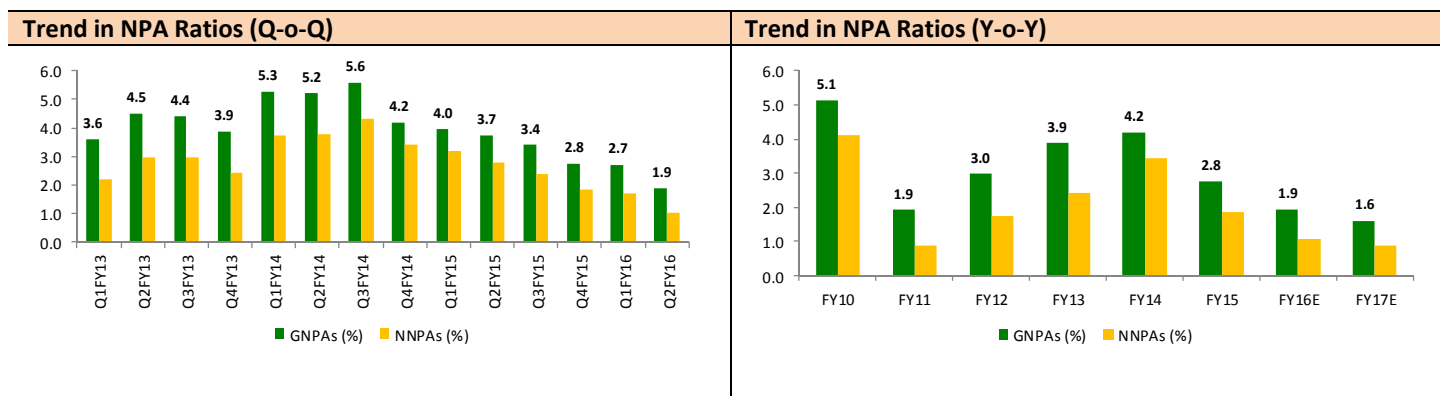
Source: Company, IndiaNivesh Research

*Strengthened credit monitoring system and stepped up recovery efforts*

The management of the bank is confident of trimming its bad assets in the coming quarters, despite the uncertain macro-economic environment. The bank has tightened its loan sanction process, strengthened credit monitoring system and stepped up recovery efforts. These initiatives have helped reduce its bad loans.

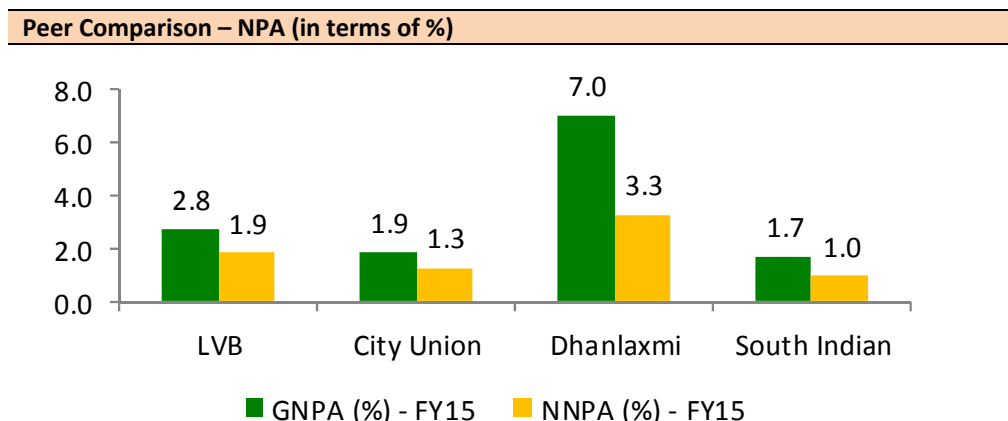
*Expecting gross NPA to decline to 1.6% & Net NPA to decline to 0.9% by FY17E*

Overall, the bank has strengthened its systems and processes. With minimal incremental slippages, healthy recoveries and secured loan growth. We expect Gross NPA to decline to 1.6% by FY17E from 2.8% in FY15 and Net NPA to improve further to 0.9% by FY17E from 1.9% in FY15. Our comfort on asset quality is also an outcome of consistency in management's efforts on recoveries from stressed assets. Also, as the economy improves the stress in the system will reduce.



Source: Company, IndiaNivesh Research

Source: Company, IndiaNivesh Research



Source: Company, IndiaNivesh Research

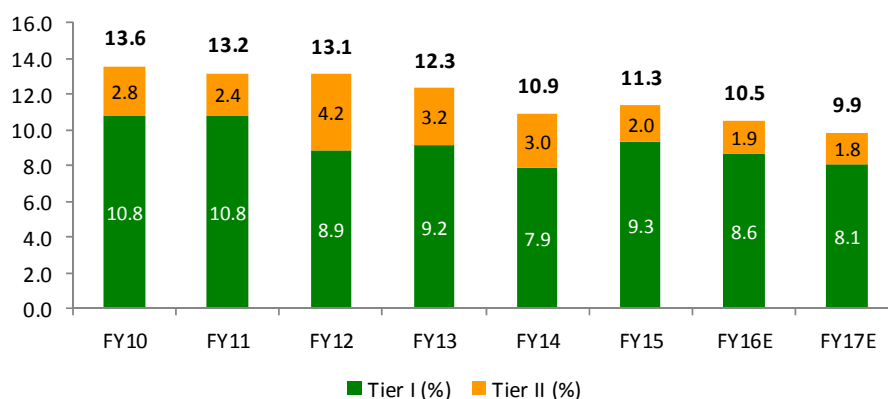


*Bank is planning to raise Rs. 3.0 bn in H2FY16 to support its current growth momentum*

### Comfortable Capital Adequacy Ratio (CAR) for next phase of growth:

LVB's capitalisation has remained healthy with CAR of 11.3% under BASEL III as of FY15 which was supported by the bank's rights issue of Rs 4.1bn. The bank's Tier I capital adequacy ratio (CAR) has remained well above 8% during the past six years. However, with a focus on high growth by the management, the bank has to raise capital in FY16. The bank is planning to raise Tier I capital of Rs 3.0 bn in H2FY16. In addition to, the bank has also headroom available to raise Tier II capital of Rs 1.0 bn to support its growth strategy.

#### Trend in Capital Adequacy Ratios (Y-o-Y)



Source: Company, IndiaNivesh Research

### Company Update:

*Rebranding exercise aimed at making it more customers friendly*

- The bank has undertaken a rebranding exercise aimed at making it more customers friendly. In a bid to shed its 'old-generation' image, the bank has strengthened its top management and signed on Ernst and Young as the consultant to evolve as a new-age bank. With focus on fine-tuning its offerings to attract the youth, the bank is strengthening its technology-enabled products such as Internet and mobile banking.
- Max Life Insurance and LVB have entered into a 5 years bancassurance tie-up for distribution of the Max Life's insurance products through the 400 branches of the bank. Under this alliance, LVB has become a corporate agent for Max Life Insurance and will offer a complete bouquet of life insurance solutions and post sales services to its customers which will help the bank to increase its other income.

*Bancassurance tie-up for distribution of the Max Life's insurance products*

### Q2FY16 Result Update:

Net Interest Income (NII) of LVB increased at a healthy pace of 20% y-o-y (+10% q-o-q) to Rs 1,603 mn in Q2FY16 driven by 29% y-o-y growth in advances. LVB's Non Interest Income increased marginally at 2% y-o-y (-19% q-o-q) to Rs 637 mn due to lower treasury income. Operating expenses increased 21% y-o-y (+12% q-o-q) to Rs 1,286 mn mainly due to 24% y-o-y increased in other operating expenses as the bank has added almost 40+ branches in the last one year. The bank has a network of 409 branches and 820 ATMs as of Q2FY16.

Pre Provisioning Profit (PPP) increased at a moderate pace of 6% y-o-y (-13% q-o-q) to Rs 954 mn due to lower treasury income. Provisions decreased 30% y-o-y (-41% q-o-q) to Rs 356 mn helped by provision write-back of Rs 198 mn towards investment. As a result, net profit increased 42% y-o-y (+11% q-o-q) to Rs 448 mn in Q2FY16.

Advances grew at a healthy pace of 29% y-o-y (+6% q-o-q) to Rs 174 bn largely led by term loans. Deposits grew 21% y-o-y (+5% q-o-q) to Rs 234 bn supported by strong growth in CASA deposits. The asset quality continues to improve as Gross NPA and Net NPA improved 83 bps and 71 bps sequentially to 1.89% and 1.01%, respectively. However, it was supported by some of the assets sales to ARCs. The bank sold assets worth Rs 1.42 bn to ARCs and booked the loss of Rs 548 mn. The loss will be amortized over 8 quarters. The bank had outstanding security receipts (SRs) of Rs 2.8 bn as of Q2FY16. Overall, LVB reported good set of numbers in Q2FY16 and it is on right track of recovery and ready to ride on growth momentum once economy starts improving.

Rs mn	Q2FY16	Q1FY16	Q2FY15	% QoQ	% YoY
Interest Income	6,342	6,141	5,512	3	15
Interest on advances	5,012	4,856	4,211	3	19
Income on Investments	1,315	1,270	1,202	4	9
Others	14	15	98	-7	-85
Interest Expense	4,739	4,689	4,171	1	14
<b>Net Interest Income</b>	<b>1,603</b>	<b>1,452</b>	<b>1,341</b>	<b>10</b>	<b>20</b>
Non Interest Income	637	790	627	-19	2
Total Net Income	2,240	2,242	1,968	0	14
Operating Expenses	1,286	1,146	1,064	12	21
Employee Cost	615	585	520	5	18
Other Operating Exp.	671	561	543	20	24
Total Income	6,979	6,931	6,139	1	14
Total Expenditure	6,025	5,835	5,235	3	15
<b>Pre Provisioning Profit</b>	<b>954</b>	<b>1,096</b>	<b>904</b>	<b>-13</b>	<b>6</b>
Provisions	356	603	509	-41	-30
Profit Before Tax	598	493	395	21	51
Tax	150	90	80	67	88
<b>Net Profit</b>	<b>448</b>	<b>403</b>	<b>315</b>	<b>11</b>	<b>42</b>
EPS - Diluted (Rs)	2.50	2.24	2.56	12	-2

Advances	1,74,022	1,63,831	1,35,255	6	29
Deposits	2,34,453	2,22,395	1,93,149	5	21
Total Business	4,08,475	3,86,225	3,28,404	6	24
Investments	66,498	67,162	62,123	-1	7
Total Assets	2,63,327	2,30,992	2,18,779	14	20
Gross NPA	3,318	4,511	5,110	-26	-35
Net NPA	1,756	2,811	3,755	-38	-53

Key Ratios (%)	Q2FY16	Q1FY16	Q2FY15	QoQ bps	YoY bps
NIM	2.81	2.61	2.65	20	16
Cost of Deposits	8.32	8.35	8.61	-3	-29
Cost of Fund	7.52	7.62	7.84	-10	-32
Yield on Advances	12.33	12.21	12.80	12	-47
Yield on Investment	8.05	8.07	8.10	-2	-5
Yield on Fund	10.07	9.98	10.20	9	-13
Cost to Income*	57.41	51.13	54.06	628	335
Credit to Deposit*	74.22	73.67	70.03	56	420
CASA	17.12	17.42	15.68	-30	145
CAR	10.26	10.28	13.20	-2	-294
Tier I Capital	7.77	8.34	10.42	-57	-265
GNPA	1.89	2.72	3.72	-83	-183
NNPA	1.01	1.72	2.78	-71	-177
Provision Coverage	71.46	63.28	57.52	818	1394
ROE (Ann.)	11.66	10.76	9.86	90	180
ROA (Ann.)	0.71	0.65	0.59	6	12

Source: Company, IndiaNivesh Research; \*Calculated

## Outlook and Valuation:

LVB is on the right track of recovery with improvement in economy. We believe that LVB will continue with its healthy growth, while maintaining its healthy capitalisation and stable asset quality over the medium term. Advances and deposits are also likely to grow at a healthy pace. LVB has an average, but improving, earnings profile. The RoA and RoE were low at around 0.5% and 5.8%, respectively as of FY14. However, under the new management, the bank posted a decent improvement in FY15 with Return on Equity (RoE) of 10.1% and Return on Assets (RoA) of 0.6%. We expect the return ratios (12.2% of RoE and 0.7% of RoA by FY17E) to improve further driven by lower provisions and improving operational efficiency. We expect LVB's growth in income to outpace operating costs, thereby leading to improved cost-efficiencies. The management has guided to achieve RoA of 1.0% by FY18E.

At CMP of Rs 97/-, the stock is trading at P/ABV of 1.1x and 1.0x for FY16E and FY17E respectively. The valuation is below its historical average and trading at a discount of about 15% to its five years mean valuation. In addition to, the recent correction in stock price also gives good opportunity to investors to enter into the stock. With improving return profile, we believe it provides attractive risk reward opportunity. Hence we recommend 'BUY' rating on the stock with target price of Rs 113/-, valuing it at 1.3x P/ABV of FY17E. (+16% upside)

### Peers Comparison - Valuation

Company Name	ROE (%)			ROA (%)			P/E			P/ABV		
	FY15	FY16E	FY17E	FY15	FY16E	FY17E	FY15	FY16E	FY17E	FY15	FY16E	FY17E
LVB	10.1	10.6	12.2	0.6	0.6	0.7	13.2	10.2	8.1	1.4	1.2	1.1
CUB*	16.7	15.7	16.7	1.5	1.5	1.6	13.0	12.1	10.1	2.2	1.9	1.7
SIB*	8.8	12.4	14.1	0.6	0.7	0.8	8.8	6.6	5.2	0.8	0.7	0.6

Source: \*Bloomberg; IndiaNivesh Research; CMP as of December 24, 2015

### Peers Comparison - Financials (FY15)

Rs mn	NII	PAT	EPS (Rs)	ROA (%)	ROE (%)	BV (Rs)	ABV (Rs)	P/E	P/BV	P/ABV
LVB	5,267	1,323	7	0.6	10.1	86.9	70.0	13.2	1.1	1.4
CUB*	8,074	3,950	7	1.5	16.7	45.2	41.3	13.0	2.2	2.2
SIB*	13,662	3,072	2	0.6	8.8	26.6	24.0	8.8	0.9	0.8

Source: \*Bloomberg; IndiaNivesh Research; CMP as of December 22, 2015

## Risks & Concerns:

### Increase in interest rate:

We are not building in scenario of any material increase in interest rates from hereon as we believe that it is very unlikely scenario. However, if anything of this sort happens then it will pose a risk to our assumptions.

### Significant deterioration in asset quality:

Any significant deterioration in asset quality will affect our provisioning and slippages assumption and hence remains risk to our estimates.

### Higher regional exposure may prone to geo political risk

LVB like almost all other old private sector banks have higher exposure in the South India and mainly in Tamilnadu (59% of total branches as of FY15). Any major change in the state policies can affect our earnings estimates for the bank.

### Key Man Risk:

The investment thesis for the bank is sensitive to changes in the top management team.

## Company Background:

Lakshmi Vilas Bank (LVB) is a small old generation private sector bank from south India with largely regional operations and especially in the state of Tamilnadu. It has been established for more than 88 years and enjoys its own set of loyal customers and a network of 400+ branches and 800+ ATMs, supervised by 8 regional offices. Bank branches are spread across 15 states and 1 Union Territory, with deep penetration in Tamil Nadu (59% of total branches). Going forward the bank is expected to grow its presence in urban and metro cities across PAN India. The bank is active across the entire spectrum of customer segments – retail, mid-market and corporate. However, with focus on fine-tuning its offerings to attract the youth, the bank is strengthening its technology-enabled products such as Internet and mobile banking. It was 100% Core Banking Solution (CBS) in year 2008. In a bid to shed its 'old-generation' image, LVB has strengthened its top management and has undertaken a rebranding exercise to evolve as a new-age bank. The bank has also undertaken a rebranding exercise aimed at making it more customers friendly. The bank is able to grow its business at a CAGR of 20% to Rs 383 bn and Net Profit at a CAGR of 18% in the last 5 Years.

## Major Share Holders and Shareholding Pattern:

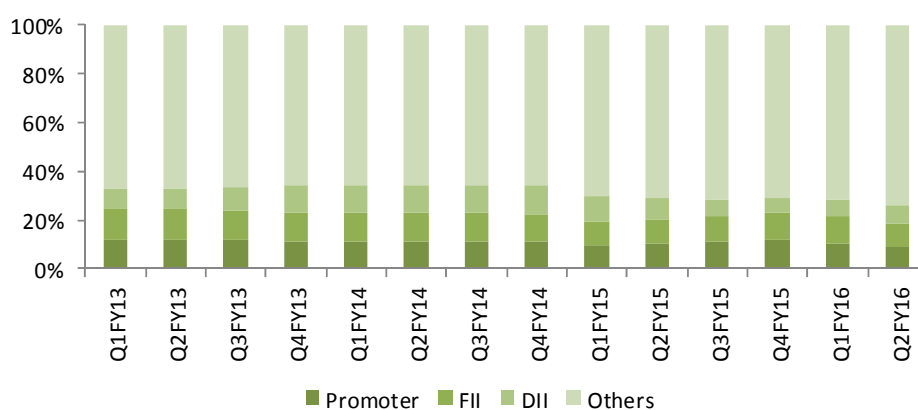
The promoters list, as per Capitaline, includes 29 'share holders' (of which 7 of them are corporate bodies and rests are individuals) with total holding of 9.7% as of Q2FY16.

### Top 10 Share Holders

Holder Name	Filing Date	% o/s	Institution Type	Country
STUPENDORS TRADERS PVT LTD	30-Jun-15	4.5	Other	INDIA
M N DASTUR & CO PVT LTD	30-Jun-15	4.1	Corporation	INDIA
MSDW MAURITIUS CO LTD	30-Jun-15	2.6	Corporation	MAURITIUS
MAX NEW YORK LIFE INS CO	30-Jun-15	2.4	Insurance Company	INDIA
JUPITER CAPITAL PVT LTD	30-Jun-15	2.1	Other	INDIA
MANKEKAR KEDAR SHIVANAND	30-Jun-15	2.1	n/a	n/a
PRADEEP K R	30-Jun-15	1.9	n/a	n/a
PRANAVA ELECTRONICS PVT	30-Jun-15	1.9	Corporation	INDIA
INDIA DEEP VALUE FUND	30-Jun-15	1.8	n/a	n/a
ALBULA INVESTMENT FUND LTD	30-Jun-15	1.7	Other	MAURITIUS

Source: Bloomberg; IndiaNivesh Research

### Trend in Share Holding Pattern (Q-o-Q)



Source: Company, IndiaNivesh Research

## Standalone Financial Statements:

Income Statement (Rs mn)	FY13	FY14	FY15	FY16E	FY17E
Interest Income	17,605	19,840	22,145	25,872	29,644
Interest Expense	13,685	14,979	16,879	19,352	21,959
<b>Net Interest Income</b>	<b>3,920</b>	<b>4,860</b>	<b>5,267</b>	<b>6,521</b>	<b>7,685</b>
Non Interest Income	1,971	2,180	2,840	3,184	3,870
Net Income	5,891	7,040	8,107	9,704	11,555
Operating Expenses	3,379	3,950	4,343	5,193	6,095
Total Income	19,576	22,019	24,986	29,056	33,514
Total Expenditure	17,065	18,929	21,221	24,544	28,054
<b>Pre Provisioning Profit</b>	<b>2,511</b>	<b>3,090</b>	<b>3,764</b>	<b>4,512</b>	<b>5,460</b>
Provisions	1,134	2,686	1,882	2,066	2,412
<b>Profit Before Tax</b>	<b>1,378</b>	<b>404</b>	<b>1,882</b>	<b>2,446</b>	<b>3,049</b>
Tax	462	-193	559	727	906
<b>Net Profit</b>	<b>916</b>	<b>597</b>	<b>1,323</b>	<b>1,719</b>	<b>2,143</b>

Balance Sheet (Rs Mn)	FY13	FY14	FY15	FY16E	FY17E
<b>Liabilities</b>					
Capital	975	976	1,792	1,795	1,795
Reserves and Surplus	9,168	9,560	13,770	15,002	16,614
Deposits	156,190	185,729	219,642	256,405	297,840
Borrowings	4,800	4,581	4,581	6,603	7,774
Other Liabilities and Provisions	5,534	5,685	7,270	8,061	8,908
<b>Total Liabilities</b>	<b>176,667</b>	<b>206,532</b>	<b>247,054</b>	<b>287,866</b>	<b>332,931</b>
<b>Assets</b>					
Cash And Balances	8,719	13,117	13,187	14,743	16,381
Investments	43,245	56,887	61,038	69,972	79,790
Advances	117,028	128,892	163,520	192,088	226,165
Fixed Assets	1,898	2,005	2,434	2,556	2,684
Other Assets	5,776	5,630	6,875	8,507	7,911
<b>Total Assets</b>	<b>176,667</b>	<b>206,532</b>	<b>247,054</b>	<b>287,866</b>	<b>332,931</b>

## Ratios

Per share data (Rs)	FY13	FY14	FY15	FY16E	FY17E
EPS	9.4	6.1	7.4	9.6	11.9
DPS	3.0	1.0	2.0	2.2	2.5
BV	104.0	108.0	86.9	93.6	102.6
ABV	74.9	62.5	70.0	82.1	91.3

## Valuation (%)

P/E	8.9	11.3	12.1	9.3	7.5
P/BV	0.8	0.6	1.0	1.0	0.9
P/ABV	1.1	1.1	1.3	1.1	1.0
Div Yield	3.6	1.4	2.2	2.5	2.8

## Spreads (%)

Yield on Advances	12.7	12.9	11.7	11.5	11.3
Yield on Investments	7.8	7.6	8.1	7.9	7.7
Yield on Funds	11.5	11.5	10.8	10.6	10.4
Cost of Deposits	8.7	8.4	8.0	0.0	0.0
Cost of Borrowings	13.1	14.2	13.4	0.0	0.0
Cost of Funds	8.9	8.5	8.1	7.9	7.7

## Capital (%)

CAR	12.3	10.9	11.3	10.5	10.0
Tier I	9.2	7.9	9.3	8.6	8.2
Tier II	3.2	3.0	2.0	1.9	1.8

## Asset (%)

GNPA	3.9	4.2	2.8	1.9	1.6
NNPA	2.4	3.4	1.9	1.1	0.9
PCR	54.5	53.2	60.8	70.0	70.0

## Management (%)

Credit / Deposit	74.9	69.4	74.4	74.9	75.9
Cost / Income	57.4	56.1	53.6	53.5	52.7
CASA	14.5	14.2	16.7	18.0	19.5

## Earnings (%)

NIM	2.6	2.8	2.6	2.7	2.7
ROE	9.3	5.8	10.1	10.6	12.2
ROA	0.5	0.3	0.6	0.6	0.7

## Liquidity (%)

C&B / D&B	5.4	6.9	5.9	5.6	5.4
C&B / Deposit	5.6	7.1	6.0	5.8	5.5

\*C&B: Cash & Bank Balance; D: Deposits; B: Borrowings; DD: Demand Deposits

## Growth Ratios (%)

Advances	14.9	10.1	26.9	17.5	17.7
Deposits	10.7	18.9	18.3	16.7	16.2
Total Assets	8.8	16.9	19.6	16.5	15.7
Networth	5.8	3.9	47.7	7.9	9.6
NII	5.6	24.0	8.4	23.8	17.9
Pre Provisioning Profit	6.7	23.0	21.8	19.9	21.0
Provisions	3.6	136.9	-29.9	9.7	16.7
Net Profit	-14.4	-34.9	121.7	30.0	24.6

Source: Company, IndiaNivesh Research

## Initiating Coverage

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NR = Not Rated. The investment rating and target price, if any, have been arrived at due to certain circumstances not in control of INSL

CS = Coverage Suspended. INSL has suspended coverage of this company.

UR=Under Review. Such e invest review happens when any developments have already occurred or likely to occur in target company & INSL analyst is waiting for some more information to draw conclusion on rating/target.

NA = Not Available or Not Applicable. The information is not available for display or is not applicable.

NM = Not Meaningful. The information is not meaningful and is therefore excluded.

Research Analyst has not served as an officer, director or employee of Subject Company

One year Price history of the daily closing price of the securities covered in this note is available at [www.nseindia.com](http://www.nseindia.com) and [www.economicstimes.indiatimes.com/markets/stocks/stock-quotes](http://www.economicstimes.indiatimes.com/markets/stocks/stock-quotes). (Choose name of company in the list browse companies and select 1 year in icon YTD in the price chart)



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