

BUY

TP: Rs 900 | ▲ 27%

AXIS BANK

| Banking

| 30 July 2019

Asset quality disappoints

Axis Bank's (AXSB) Q1FY20 PAT at Rs 13.7bn fell short of our/consensus estimates on high provisions. Asset quality was a miss as AXSB disclosed Rs 67bn of exposure to recent stressed groups not classified as NPA nor in the 'BB & below' pool. Slippages rose to Rs 48bn (vs. Rs 30bn in Q4), but the 'BB & below' book was stable at Rs 75bn given downgrades worth ~Rs 22bn. Domestic loan growth at 19% YoY was steered by retail, while NIM dipped 4bps QoQ to 3.4%. We cut FY20/FY21 EPS by 9-12% but maintain our Mar'20 TP at Rs 900.

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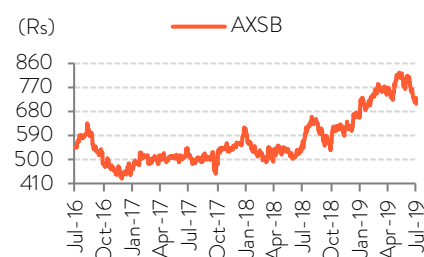
Miss on asset quality: AXSB identified its exposure (incl. loans, investments and NFB) to eight stressed corporate groups at Rs 122bn. Ex-NPA and 'BB & below' exposure, this pool stands at Rs 67bn. The bank already has additional provisions worth Rs 23.6bn, ~60% of which are towards these stressed groups. Its 'BB & below' rated pool was stable at Rs 75bn as slippages/reductions here were offset by downgrades of a similar quantum. Gross slippages at Rs 48bn included corporate slippages worth Rs 21.3bn centred around two lumpy accounts in the power and shipping sectors.

Ticker/Price	AXSB IN/Rs 708
Market cap	US\$ 26.4bn
Shares o/s	2,569mn
3M ADV	US\$ 90.3mn
52wk high/low	Rs 828/Rs 535
Promoter/FPI/DII	26%/50%/24%

Source: NSE

Retail drives loan growth: Despite strong 19% YoY growth in the domestic book, loan growth was subdued at 12.7% as AXSB's overseas book declined 34%. Retail continues to propel domestic growth with personal loans, credit cards and auto loans being the key drivers. Management retained its guidance of posting domestic loan growth 5-7% above industry levels. NIM is guided to stay stable with an upward bias in FY20 but improve to 3.5-3.8% thereafter.

STOCK PERFORMANCE



Source: NSE

Maintain BUY: We cut FY20/FY21 EPS by 9-12% on higher credit costs, and reduce our core book multiple to 2.3x from 2.5x earlier. Our Mar'20 TP remains at Rs 900 after building in the capital raise and warrant conversion. Reiterate BUY as we believe AXSB is well placed to play the turning asset quality cycle.

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	2,757	46,766	98,113	138,808	187,115
EPS (Rs)	1.1	18.2	36.1	48.5	65.3
P/E (x)	636.8	38.9	19.6	14.6	10.8
P/BV (x)	2.9	2.7	2.1	1.9	1.7
ROA (%)	0.0	0.6	1.1	1.3	1.5
ROE (%)	0.5	7.2	12.1	13.7	16.4

Source: Company, BOBCAPS Research

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Important disclosures, including any required research certifications, are provided at the end of this report.



FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q1FY20	Q4FY19	Q1FY19	YoY (%)	QoQ (%)
Income Statement					
Net interest income	58,437	57,056	51,668	13.1	2.4
Non-interest income	38,688	35,263	29,250	32.3	9.7
Net total income	97,124	92,319	80,918	20.0	5.2
Staff expenses	13,068	11,423	12,278	6.4	14.4
Other operating expenses	25,128	30,752	24,920	0.8	(18.3)
Total operating expenses	38,197	42,175	37,198	2.7	(9.4)
Pre-provisioning profit	58,928	50,144	43,720	34.8	17.5
Total provisions	38,146	27,114	33,377	14.3	40.7
Profit before tax	20,782	23,030	10,343	100.9	(9.8)
Tax	7,081	7,979	3,333	112.5	(11.3)
Profit after tax	13,701	15,051	7,011	95.4	(9.0)
Key Balance Sheet Items					
Loans	4,972,760	4,947,980	4,410,745	12.7	0.5
Retail Loans	2,582,050	2,458,120	2,116,480	22.0	5.0
Retail as a % of total advances	51.9	49.7	48.0	394bps	224bps
Deposits	5,406,777	5,484,713	4,470,793	20.9	(1.4)
CASA ratio (%)	41.3	44.4	46.9	(556bps)	(304bps)
Loan to deposit ratio (%)	92.0	90.2	98.7	(668bps)	176bps
Margin Components (%)					
Cost of funds	5.7	5.7	5.2	47bps	1bps
Net interest margin	3.4	3.4	3.5	(6bps)	(4bps)
Key Ratios (%)					
Cost/Income	39.3	45.7	46.0	(664bps)	(636bps)
Tax rate	34.1	34.6	32.2	185bps	(57bps)
Capital Adequacy Ratios (%)					
Tier I ratio	12.9	12.5	13.2	(32bps)	36bps
Tier II ratio	3.2	3.3	3.5	(33bps)	(14bps)
Total CAR ratio	16.1	15.8	16.7	(65bps)	22bps
Asset Quality Ratios					
Gross NPAs	294,049	297,894	326,624	(10.0)	(1.3)
Net NPAs	110,375	112,756	149,016	(25.9)	(2.1)
Gross NPA ratio (%)	5.3	5.3	6.5	(127bps)	(1bps)
Net NPA ratio (%)	2.0	2.1	3.1	(105bps)	(2bps)
Provision coverage (%)	62.5	62.1	54.4	809bps	31bps

Source: Company, BOBCAPS Research

Valuation methodology

We cut FY20/FY21 EPS estimates by 9-12% on higher credit costs, and reduce our core book multiple to 2.3x from 2.5x earlier considering dilution puts the 18% ROE guidance by FY22 at risk. Our Mar'20 target price remains at Rs 900 after building in the capital raise and warrant conversion. Reiterate BUY as we believe AXSB is well placed to play the turning asset quality cycle.

Our target price is derived using the SOTP method wherein (a) the core book has been adjusted for investment in subsidiaries and valued at Rs 856/sh based on a two-stage Gordon growth model (given that we expect the business to continue growing much faster than the industry for the next few years), and (b) subsidiaries are valued at Rs 44/sh.

FIG 2 – REVISED ESTIMATES

Particulars	Earlier estimates		New estimates		Change (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net interest income (Rs mn)	259,947	324,103	248,084	307,192	(4.6)	(5.2)
Pre-provisioning profit (Rs mn)	232,420	292,820	231,480	289,471	(0.4)	(1.1)
Profit after tax (Rs mn)	111,784	152,277	98,113	138,808	(12.2)	(8.8)

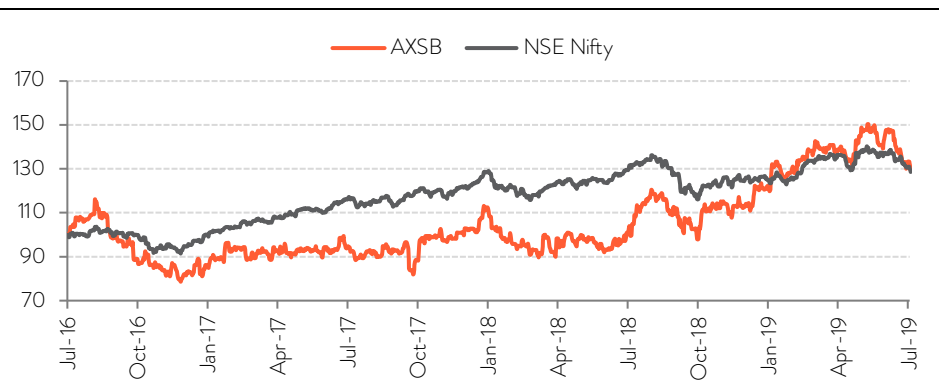
Source: Company

FIG 3 – SOTP VALUATION

Particulars	Company Value (Rs bn)	Stake in Company (%)	Value for AXSB (Rs bn)	Per Share (Rs)	Contribution to TP (%)	Comments
Core Business	2,450	100	2,450	856	95	Valued at 2.3x FY21E P/BV on Gordon Growth Model
Axis AMC	72	75	54	19	2	7% of Q1FY20 AAUM
Axis Finance	44	100	44	16	2	2.5x FY21E P/BV
Axis Capital	14	100	14	5	1	15x FY21E P/E
Axis Securities	14	100	14	5	1	15x FY21E P/E
Sum-of-the-Parts			2,577	900		

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **High attrition:** The new management has reorganised several functions internally and hired talent for key positions from outside the bank. In our view, changing too many things simultaneously could unbalance the existing working culture and lead to higher attrition.
- **Performance of subsidiaries:** Slower capital markets activity can mute the performance of subsidiaries.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net interest income	186,177	217,082	248,084	307,192	384,219
NII growth (%)	2.9	16.6	14.3	23.8	25.1
Non-interest income	109,671	131,303	160,134	189,836	230,525
Total income	295,848	348,385	408,218	497,029	614,744
Operating expenses	(139,903)	(158,334)	(176,738)	(207,557)	(245,537)
Operating profit	155,945	190,051	231,480	289,471	369,207
Operating profit growth (%)	(11.3)	21.9	21.8	25.1	27.5
Provisions	(154,729)	(120,310)	(85,042)	(82,296)	(89,931)
PBT	1,216	69,741	146,438	207,176	279,276
Tax	1,541	(22,975)	(48,324)	(68,368)	(92,161)
Reported net profit	2,757	46,766	98,113	138,808	187,115
Adjustments	0	0	0	0	0
Adjusted net profit	2,757	46,766	98,113	138,808	187,115

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Equity capital	5,133	5,143	5,728	5,728	5,728
Reserves & surplus	629,320	661,620	947,115	1,060,937	1,214,372
Net worth	634,453	666,763	952,843	1,066,665	1,220,100
Deposits	4,536,227	5,484,713	6,412,250	7,666,641	9,211,952
Borrowings	1,410,661	1,458,258	1,626,196	1,839,437	2,109,181
Other liabilities & provisions	331,955	400,231	520,301	676,391	879,308
Total liabilities and equities	6,913,296	8,009,965	9,511,589	11,249,135	13,420,541
Cash & bank balance	434,549	672,046	724,905	782,570	845,499
Investments	1,538,761	1,749,693	2,029,670	2,388,324	2,842,518
Advances	4,396,503	4,947,980	5,739,656	6,772,795	8,127,354
Fixed & Other assets	543,483	640,246	1,017,358	1,305,446	1,605,171
Total assets	6,913,296	8,009,965	9,511,589	11,249,135	13,420,541
Deposit growth (%)	9.5	20.9	16.9	19.6	20.2
Advances growth (%)	17.8	12.5	16.0	18.0	20.0

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
EPS	1.1	18.2	36.1	48.5	65.3
Dividend per share	5.5	0.0	6.2	8.7	11.8
Book value per share	247.2	259.3	332.7	372.4	426.0

Source: Company, BOBCAPS Research

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
P/E	636.8	38.9	19.6	14.6	10.8
P/BV	2.9	2.7	2.1	1.9	1.7
Dividend yield (%)	0.8	0.0	0.9	1.2	1.7

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Net interest income	2.9	2.9	2.8	3.0	3.1
Non-interest income	1.7	1.8	1.8	1.8	1.9
Operating expenses	2.2	2.1	2.0	2.0	2.0
Pre-provisioning profit	2.4	2.5	2.6	2.8	3.0
Provisions	2.4	1.6	1.0	0.8	0.7
PBT	0.0	0.9	1.7	2.0	2.3
Tax	0.0	0.3	0.6	0.7	0.7
ROA	0.0	0.6	1.1	1.3	1.5
Leverage (x)	10.8	11.5	10.8	10.3	10.8
ROE	0.5	7.2	12.1	13.7	16.4

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Net interest income	2.9	16.6	14.3	23.8	25.1
Pre-provisioning profit	(11.3)	21.9	21.8	25.1	27.5
EPS	(92.8)	1538.1	98.3	34.3	34.8
Profitability & Return ratios (%)					
Net interest margin	3.1	3.2	3.1	3.3	3.5
Fees / Avg. assets	1.2	1.2	1.2	1.3	1.3
Cost-Income	47.3	45.4	43.3	41.8	39.9
ROE	0.5	7.2	12.1	13.7	16.4
ROA	0.0	0.6	1.1	1.3	1.5
Asset quality (%)					
GNPA	7.5	5.8	5.2	4.4	3.7
NNPA	3.8	2.3	2.0	1.5	1.2
Provision coverage	51.6	62.1	62.7	66.3	68.7
Ratios (%)					
Credit-Deposit	96.9	90.2	89.5	88.3	88.2
Investment-Deposit	33.9	31.9	31.7	31.2	30.9
CAR	16.6	15.8	18.2	16.6	15.5
Tier-1	13.0	12.5	15.1	13.9	13.1

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

HISTORICAL RATINGS AND TARGET PRICE: AXIS BANK (AXSB IN)



B – Buy, A – Add, R – Reduce, S – Sell

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