

**BUY**

TP: Rs 900 | ▲ 26%

**AXIS BANK**

| Banking

| 22 January 2020

## Stressed book still elevated

Axis Bank's (AXSB) Q3FY20 PAT at ~Rs 18bn missed estimates due to above-expected provisions. Asset quality was a major disappointment as slippages surged to Rs 62bn while the outstanding stressed BB-&-below pool remained elevated at Rs 97bn (1.8% of loans). An HFC account slipped into NPA from the BB-&-below book and two accounts (telecom & broking) were downgraded into the pool. Management highlighted potential pressure on NIM and credit costs in Q4. We cut FY20-FY22 EPS by 5-35% and roll to a Mar'21 TP of Rs 900 (vs. Rs 950).

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**Higher slippages dent asset quality:** Gross slippages increased to Rs 62bn vs. Rs 50bn in Q2 due to higher retail and corporate slippages. However, the outstanding stressed BB-&-below pool remained elevated at Rs 97bn (1.8% of loans) due to downgrades of a telecom and a broking account into the pool. NNPA in the retail book stood at <0.5% but slippages were higher due to stress in the CV segment. AXSB is also witnessing increasing risk in its MFI book, largely from Assam and Karnataka (together <10% of its MFI portfolio).

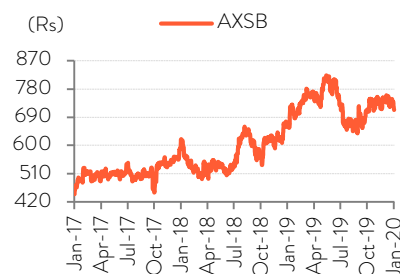
Ticker/Price	AXSB IN/Rs 713
Market cap	US\$ 26.2bn
Shares o/s	2,620mn
3M ADV	US\$ 88.8mn
52wk high/low	Rs 828/Rs 623
Promoter/FPI/DII	26%/50%/24%

Source: NSE

Asset quality divergence for FY19 was below disclosure levels while the SMA-2 book stood at 0.35%. Credit cost for Q4 hinges on recoveries from large case resolution and provision coverage levels.

**Loan growth stable; NIM improves:** AXSB's loan book grew 16% YoY driven by 25%/16% growth in the retail/domestic corporate segments. Guidance of FY20 domestic loan growth being 5-7% higher than industry was maintained. NIM improved 6bps QoQ on better spreads and benefits of the recent capital raise.

## STOCK PERFORMANCE



Source: NSE

**Maintain BUY:** We cut FY20/FY21/FY22 EPS by 35%/2%/5% to build in higher provisions and roll over to a revised Mar'21 TP of Rs 900 (vs. Rs 950). Maintain BUY as we believe normalisation in credit costs is a few quarters away.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Net interest income	186,177	217,082	245,413	304,064	378,806
NII growth (%)	2.9	16.6	13.1	23.9	24.6
Adj. net profit (Rs mn)	2,757	46,766	56,263	149,051	186,092
EPS (Rs)	1.1	18.2	20.9	52.9	66.1
P/E (x)	641.3	39.1	34.1	13.5	10.8
P/BV (x)	2.9	2.7	2.3	2.0	1.8
ROA (%)	0.0	0.6	0.6	1.4	1.5
ROE (%)	0.5	7.2	7.4	16.1	17.5

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q3FY20	Q2FY20	Q3FY19	YoY (%)	QoQ (%)
<b>Income Statement</b>					
<b>Net interest income</b>	<b>64,530</b>	<b>61,018</b>	<b>56,037</b>	<b>15.2</b>	<b>5.8</b>
Non-interest income	37,866	38,958	40,007	(5.4)	(2.8)
<b>Net total income</b>	<b>102,396</b>	<b>99,976</b>	<b>96,044</b>	<b>6.6</b>	<b>2.4</b>
Staff expenses	13,652	12,750	12,026	13.5	7.1
Other operating expenses	31,316	27,711	28,771	8.8	13.0
<b>Total operating expenses</b>	<b>44,969</b>	<b>40,460</b>	<b>40,797</b>	<b>10.2</b>	<b>11.1</b>
Pre-provisioning profit	57,427	59,516	55,247	3.9	(3.5)
<b>Total provisions</b>	<b>34,709</b>	<b>35,184</b>	<b>30,545</b>	<b>13.6</b>	<b>(1.3)</b>
<b>Profit before tax</b>	<b>22,718</b>	<b>24,332</b>	<b>24,701</b>	<b>(8.0)</b>	<b>(6.6)</b>
Tax	5,148	25,453	7,893	(34.8)	(79.8)
<b>Profit after tax</b>	<b>17,570</b>	<b>(1,121)</b>	<b>16,809</b>	<b>4.5</b>	<b>(1,667.6)</b>
<b>Key balance sheet items</b>					
Loans	5,501,377	5,215,937	4,751,049	15.8	5.5
Deposits	5,916,755	5,839,585	5,140,921	15.1	1.3
CASA ratio (%)	41.2	41.1	45.8	(462bps)	9bps
Loan to deposit ratio (%)	93.0	89.3	92.4	56bps	366bps
<b>Margin components (%)</b>					
Cost of funds	5.4	5.6	5.4	(2bps)	(20bps)
Net interest margin	3.6	3.5	3.5	10bps	6bps
<b>Key Ratios (%)</b>					
Cost/Income	43.9	40.5	42.5	144bps	345bps
Tax rate	22.7	104.6	32.0	(929bps)	(8195bps)
<b>Capital Adequacy Ratios (%)</b>					
Tier I ratio	15.5	15.3	13.1	247bps	29bps
Tier II ratio	3.2	3.2	3.3	(15bps)	(2bps)
<b>Total CAR ratio</b>	<b>18.7</b>	<b>18.5</b>	<b>16.4</b>	<b>232bps</b>	<b>27bps</b>
<b>Asset Quality Ratios</b>					
Gross NPAs	300,730	290,714	308,547	(2.5)	3.4
Net NPAs	121,603	111,383	122,333	(0.6)	9.2
Gross NPA ratio (%)	5.0	5.0	5.8	(75bps)	(3bps)
Net NPA ratio (%)	2.1	2.0	2.4	(27bps)	10bps
Provision coverage (%)	59.6	61.7	60.4	(79bps)	(212bps)

Source: Company, BOBCAPS Research

## Valuation methodology

We cut our FY20/FY21/FY22 EPS estimates by 35%/2%/5% to factor in higher provisions but continue to believe credit costs will normalise sharply for corporate banks aided by the improvement in NPAs. Maintain BUY with a revised Mar'21 SOTP-based target price of Rs 900 (vs. Rs 950) on rollover.

For our SOTP valuation: (a) the core book has been adjusted for investment in subsidiaries and valued at Rs 850/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 50/sh.

**FIG 2 – REVISED ESTIMATES**

Particulars	New			Old			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Net interest income (Rs mn)	245,413	304,064	378,806	248,084	307,192	382,531	(1.1)	(1.0)	(1.0)
Pre-provisioning profit (Rs mn)	224,865	276,377	340,055	231,480	286,284	354,451	(2.9)	(3.5)	(4.1)
Profit after tax (Rs mn)	56,263	149,051	186,092	87,028	151,767	196,803	(35.4)	(1.8)	(5.4)

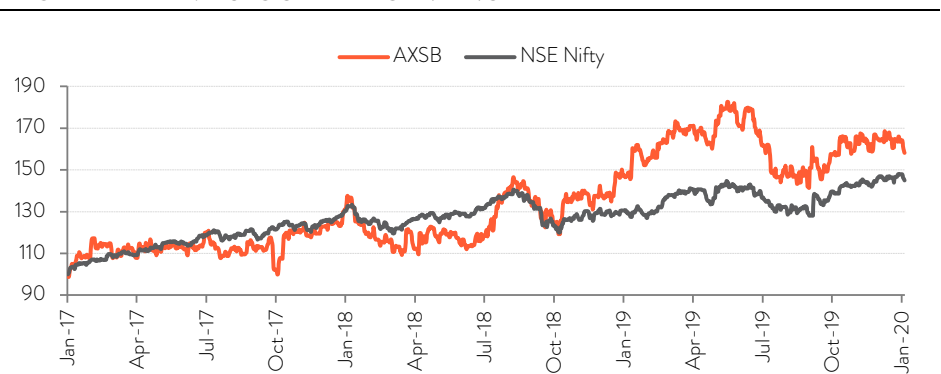
Source: BOBCAPS Research

**FIG 3 – SOTP VALUATION**

Sum of Parts	Company Value (Rs bn)	Stake in Company (%)	Value for AXSB (Rs bn)	Per Share (Rs)	Contribution to TP (%)	Comments
Core Business	2,394	100	2,394	850	94	Valued at 2.1x Mar'22 P/BV on Gordon Growth Model
Axis AMC	72	75	54	19	2	7% of Q1FY20 AAUM
Axis Finance	54	100	53	19	2	2.5x Mar'22 P/BV
Axis Capital	16	100	16	6	1	15x Mar'22 P/E
Axis Securities	17	100	17	6	1	15x Mar'22 P/E
<b>Sum of Parts</b>			<b>2,534</b>	<b>900</b>		

Source: BOBCAPS Research

**FIG 4 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- A worsening economic environment can impact our loan growth and credit cost assumptions and lead to deterioration in AXSB's asset quality.
- Slower capital markets activity can mute the performance of subsidiaries.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Net interest income</b>	<b>186,177</b>	<b>217,082</b>	<b>245,413</b>	<b>304,064</b>	<b>378,806</b>
NII growth (%)	2.9	16.6	13.1	23.9	24.6
Non-interest income	109,671	131,303	155,707	179,301	210,455
Total income	295,848	348,385	401,120	483,365	589,261
Operating expenses	(139,903)	(158,334)	(176,254)	(206,988)	(249,206)
Operating profit	155,945	190,051	224,865	276,377	340,055
Operating profit growth (%)	(11.3)	21.9	18.3	22.9	23.0
Provisions	(154,729)	(120,310)	(119,777)	(76,039)	(89,931)
PBT	1,216	69,741	105,088	200,337	250,124
Tax	1,541	(22,975)	(48,824)	(51,286)	(64,032)
<b>Reported net profit</b>	<b>2,757</b>	<b>46,766</b>	<b>56,263</b>	<b>149,051</b>	<b>186,092</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>2,757</b>	<b>46,766</b>	<b>56,263</b>	<b>149,051</b>	<b>186,092</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Equity capital	5,133	5,143	5,631	5,631	5,631
Reserves & surplus	629,320	661,620	857,894	980,116	1,132,712
Net worth	634,453	666,763	863,526	985,748	1,138,343
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
<b>Total liabilities and equities</b>	<b>6,913,296</b>	<b>8,009,965</b>	<b>9,422,272</b>	<b>11,168,217</b>	<b>13,338,784</b>
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	928,041	1,224,529	1,523,414
<b>Total assets</b>	<b>6,913,296</b>	<b>8,009,965</b>	<b>9,422,272</b>	<b>11,168,217</b>	<b>13,338,784</b>
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	20.9	52.9	66.1
Dividend per share	5.5	0.0	3.6	9.5	11.9
Book value per share	247.2	259.3	306.7	350.1	404.3

Source: Company, BOBCAPS Research

### Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
P/E	641.3	39.1	34.1	13.5	10.8
P/BV	2.9	2.7	2.3	2.0	1.8
Dividend yield (%)	0.8	0.0	0.5	1.3	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	1.7	1.7
Operating expenses	2.2	2.1	2.0	2.0	2.0
Pre-provisioning profit	2.4	2.5	2.6	2.7	2.8
Provisions	2.4	1.6	1.4	0.7	0.7
PBT	0.0	0.9	1.2	1.9	2.0
Tax	0.0	0.3	0.6	0.5	0.5
ROA	0.0	0.6	0.6	1.4	1.5
Leverage (x)	10.8	11.5	11.4	11.1	11.5
ROE	0.5	7.2	7.4	16.1	17.5

### Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Net interest income	2.9	16.6	13.1	23.9	24.6
Pre-provisioning profit	(11.3)	21.9	18.3	22.9	23.0
EPS	(92.8)	1538.1	14.7	153.4	24.9
<b>Profitability &amp; Return ratios (%)</b>					
Net interest margin	3.1	3.2	3.1	3.3	3.5
Fees / Avg. assets	1.2	1.2	1.2	1.2	1.2
Cost-Income	47.3	45.4	43.9	42.8	42.3
ROE	0.5	7.2	7.4	16.1	17.5
ROA	0.0	0.6	0.6	1.4	1.5
<b>Asset quality (%)</b>					
GNPA	7.5	5.8	5.2	4.4	3.7
NNPA	3.8	2.3	2.2	1.8	1.4
Provision coverage	51.6	62.1	58.2	60.2	62.7
<b>Ratios (%)</b>					
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	16.9	15.7	14.7
Tier-1	13.0	12.5	13.9	12.9	12.3

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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