

**BUY**

TP: Rs 1,850 | ▲ 23%

**INDUSIND BANK**

| Banking

| 12 July 2019

**No major surprises**

IndusInd Bank (IIB) has reported consolidated numbers for Q1FY20 post-merger with Bharat Financial (BHAFIN). PAT at Rs 14bn (+38% YoY) beat estimates largely due to below-expected provisions. Exposure to potentially stressed groups declined to 1.67% of loans vs. 1.9% in Q4FY19, while SMA-2 loans halved to 0.17%. Loan growth at 28% YoY remained in line with Q4 despite the merger, as BHAFIN had tightened lending norms in a few states. The bank is opening 40-50k savings accounts of BHAFIN customers each day.

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**Asset quality remains manageable:** GNPA increased 5bps QoQ to 2.15% in Q1, while the coverage ratio remained low at 43%. Exposure to stressed groups declined to 1.67% of loans in part due to repayments. The SMA-1 & 2 book nearly halved to 0.35%. Management asserted that SPVs of IL&FS are adequately provided for and even believes a write-back of some of these provisions is possible. FY20 credit cost guidance has been maintained at 65bps.

Ticker/Price	IIB IN/Rs 1,510
Market cap	US\$ 13.3bn
Shares o/s	603mn
3M ADV	US\$ 98.0mn
52wk high/low	Rs 2,038/Rs 1,333
Promoter/FPI/DII	17%/52%/31%

Source: NSE

**Loan growth in line with Q4:** IIB's vehicle finance book grew ~24% YoY backed by secular growth across CVs, two-wheelers, three-wheelers and tractors. The non-vehicle finance/corporate book grew >20%/15-20%. Management continues to guide for mid-twenties growth overall in FY20.

**STOCK PERFORMANCE**

Source: NSE

**BHAFIN update:** AUM at Rs 175bn grew 26% YoY in Q1 but was flat QoQ. Management has guided for 35% growth in FY20 supported by a 22-25% increase in borrowers and 10-15% rise in ticket size. In terms of liability accretion, IIB is opening 40-50k savings accounts of BHAFIN customers a day.

**Maintain BUY with TP of Rs 1,850:** We introduce estimates for FY22 and for post-merger financials. We continue to value the stock at 3x FY21E P/BV as merger synergies are expected to raise ROE to ~19% by FY21E.

**KEY FINANCIALS**

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	36,060	33,011	55,180	75,410	98,007
EPS (Rs)	60.2	54.9	84.2	106.5	138.4
P/E (x)	25.1	27.5	17.9	14.2	10.9
P/BV (x)	3.9	3.5	3.0	2.4	2.0
ROA (%)	1.8	1.3	1.7	1.8	1.9
ROE (%)	16.2	13.1	17.5	18.6	20.0

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q1FY20	Q4FY19	Q1FY19	YoY (%)	QoQ (%)
<b>Net interest income</b>	<b>28,440</b>	<b>22,324</b>	<b>21,224</b>	<b>34.0</b>	<b>27.4</b>
<b>Non-interest income</b>	<b>16,633</b>	<b>15,590</b>	<b>13,016</b>	<b>27.8</b>	<b>6.7</b>
Core fee	14,210	14,200	11,650	22.0	0.1
Securities / MM / FX Trading	2,410	1,400	1,370	75.9	72.1
<b>Net total income</b>	<b>45,072</b>	<b>37,914</b>	<b>34,240</b>	<b>31.6</b>	<b>18.9</b>
Staff expenses	6,472	4,812	4,620	40.1	34.5
Other expenses	12,691	12,431	10,509	20.8	2.1
<b>Total operating expenses</b>	<b>19,163</b>	<b>17,243</b>	<b>15,129</b>	<b>26.7</b>	<b>11.1</b>
<b>Pre-provisioning profit</b>	<b>25,910</b>	<b>20,671</b>	<b>19,111</b>	<b>35.6</b>	<b>25.3</b>
<b>Provisions</b>	<b>4,306</b>	<b>15,607</b>	<b>3,500</b>	<b>23.0</b>	<b>(72.4)</b>
<b>Profit before tax</b>	<b>21,603</b>	<b>5,064</b>	<b>15,611</b>	<b>38.4</b>	<b>326.6</b>
Tax	7,278	1,469	5,254	38.5	395.5
<b>Profit after tax</b>	<b>14,325</b>	<b>3,595</b>	<b>10,357</b>	<b>38.3</b>	<b>298.5</b>
<b>Balance Sheet</b>					
Loans	1,935,200	1,863,935	1,506,750	28.4	3.8
Deposits	2,005,860	1,948,679	1,588,620	26.3	2.9
CASA ratio (%)	43.1	43.1	43.4	(28bps)	0bps
<b>Yields and margins (%)</b>					
Yield on advances	12.0	11.3	11.2	85bps	75bps
Yield on assets	10.0	9.5	9.4	63bps	48bps
Cost of deposits	6.9	6.8	6.2	66bps	6bps
Cost of funds	5.9	5.9	5.4	50bps	2bps
<b>Net interest margin</b>	<b>4.1</b>	<b>3.6</b>	<b>3.9</b>	<b>13bps</b>	<b>46bps</b>
<b>Key ratios (%)</b>					
Cost / income ratio	42.5	45.5	44.2	(167bps)	(296bps)
Tax rate	33.7	29.0	33.7	4bps	468bps
Loan to deposit ratio	96.5	95.7	94.8	163bps	83bps
<b>Capital adequacy (%)</b>					
Tier I	14.5	13.7	14.3	18bps	77bps
Total CAR	14.9	14.2	14.7	20bps	74bps
<b>Asset Quality</b>					
Gross NPAs	41,997	39,474	17,406	141.3	6.4
Net NPAs	23,805	22,483	7,624	212.3	5.9
Coverage ratio (%)	43.3	43.0	56.2	(1,289bps)	27bps
Gross NPA ratio (%)	2.2	2.1	1.2	100bps	5bps
Net NPA ratio (%)	1.2	1.2	0.5	72bps	2bps

Source: Company, BOBCAPS Research

## Valuation methodology

We expect IIB to continue growing much higher than the industry for the next few years and hence use the two-stage Gordon growth model to set our target price as it captures valuations in a high-growth stage. In this report, we introduce estimates for FY22 and for post-merger financials. On credit costs, we build in a forecast of 110bps/90bps for FY20/FY21 in light of IIB's exposure to stressed groups.

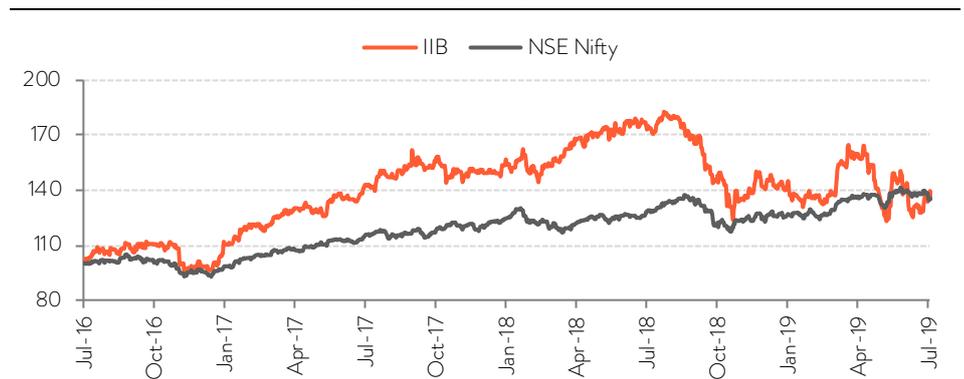
IIB is currently trading at 2.4x FY21E P/BV. We continue to value the stock at 3x FY21E P/BV as we believe the BHAFIN acquisition substantially fortifies the bank's liability franchise. Our Mar'20 target price remains unchanged at Rs 1,850 – maintain BUY.

**FIG 2 – VALUATION SNAPSHOT**

Components of Gordon growth model	Assumptions (%)
Risk-free rate (%)	7.0
Equity risk premium (%)	5.0
Beta	1.1
Cost of equity (%)	12.4
Blended ROE (%)	19.2
Initial high growth period (yrs)	10.0
Payout ratio of high-growth phase (%)	20.0
Long-term growth (%)	5
Long-term dividend payout ratio (%)	75
Justified P/BV multiple (x)	3
Adj. BVPS (Rs)	621
Value per share (Rs)	1,850

Source: Company, BOBCAPS Research

**FIG 3 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- Romesh Sobti's term as MD and CEO will end on 23 Mar 2020 as he reaches the upper age limit of ~70 years. While the board has indicated that succession planning is in place, any hiccups or senior management exits that may take place during this transition period could negatively impact the stock.
- BHAFIN may open the door to unexpected surprises, especially on the asset quality front, given the nature of its business.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19P	FY20E	FY21E	FY22E
<b>Net interest income</b>	<b>74,974</b>	<b>88,462</b>	<b>132,702</b>	<b>168,839</b>	<b>211,357</b>
NII growth (%)	23.7	18.0	50.0	27.2	25.2
Non-interest income	47,501	56,467	66,379	82,065	100,739
Total income	122,475	144,929	199,081	250,904	312,096
Operating expenses	(55,914)	(64,047)	(88,309)	(108,093)	(129,994)
Operating profit	66,561	80,882	110,771	142,811	182,103
Operating profit growth (%)	22.1	21.5	37.0	28.9	27.5
Provisions	(11,754)	(31,077)	(27,517)	(29,035)	(34,233)
PBT	54,807	49,806	83,254	113,776	147,869
Tax	(18,747)	(16,795)	(28,074)	(38,366)	(49,862)
<b>Reported net profit</b>	<b>36,060</b>	<b>33,011</b>	<b>55,180</b>	<b>75,410</b>	<b>98,007</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>36,060</b>	<b>33,011</b>	<b>55,180</b>	<b>75,410</b>	<b>98,007</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19P	FY20E	FY21E	FY22E
Equity capital	6,002	6,027	7,081	7,081	7,081
Reserves & surplus	232,414	260,833	355,196	440,117	524,365
Net worth	238,416	266,860	362,277	447,197	531,446
Deposits	1,516,392	1,948,679	2,451,447	3,083,256	3,880,158
Borrowings	382,891	473,211	766,171	929,925	1,116,779
Other liabilities & provisions	78,563	89,444	94,535	99,918	105,612
<b>Total liabilities and equities</b>	<b>2,216,262</b>	<b>2,778,194</b>	<b>3,674,430</b>	<b>4,560,296</b>	<b>5,633,996</b>
Cash & bank balance	132,159	147,834	158,191	169,474	181,773
Investments	500,767	592,662	736,539	924,644	1,137,352
Advances	1,449,537	1,863,935	2,496,999	3,121,969	3,903,369
Fixed & Other assets	133,799	173,764	282,702	344,209	411,502
<b>Total assets</b>	<b>2,216,262</b>	<b>2,778,194</b>	<b>3,674,430</b>	<b>4,560,296</b>	<b>5,633,996</b>
Deposit growth (%)	19.8	28.5	25.8	25.8	25.8
Advances growth (%)	28.2	28.6	34.0	25.0	25.0

### Per Share

Y/E 31 Mar (Rs)	FY18A	FY19P	FY20E	FY21E	FY22E
EPS	60.2	54.9	84.2	106.5	138.4
Dividend per share	7.2	7.5	9.4	12.8	16.6
Book value per share	391.2	436.8	506.5	626.4	745.4

Source: Company, BOBCAPS Research

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19P	FY20E	FY21E	FY22E
P/E	25.1	27.5	17.9	14.2	10.9
P/BV	3.9	3.5	3.0	2.4	2.0
Dividend yield (%)	0.5	0.5	0.6	0.8	1.1

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19P	FY20E	FY21E	FY22E
Net interest income	3.7	3.5	4.1	4.1	4.1
Non-interest income	2.4	2.3	2.1	2.0	2.0
Operating expenses	2.8	2.6	2.7	2.6	2.6
Pre-provisioning profit	3.3	3.2	3.4	3.5	3.6
Provisions	0.6	1.2	0.9	0.7	0.7
PBT	2.7	2.0	2.6	2.8	2.9
Tax	0.9	0.7	0.9	0.9	1.0
ROA	1.8	1.3	1.7	1.8	1.9
Leverage (x)	9.0	9.9	10.3	10.2	10.4
ROE	16.2	13.1	17.5	18.6	20.0

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Net interest income	23.7	18.0	50.0	27.2	25.2
Pre-provisioning profit	22.1	21.5	37.0	28.9	27.5
EPS	25.2	(8.8)	53.4	26.5	30.0
<b>Profitability &amp; Return ratios (%)</b>					
Net interest margin	4.0	3.8	4.4	4.4	4.5
Fees / Avg. assets	1.7	1.6	1.6	1.5	1.5
Cost-Income	45.7	44.2	44.4	43.1	41.7
ROE	16.2	13.1	17.5	18.6	20.0
ROA	1.8	1.3	1.7	1.8	1.9
<b>Asset quality (%)</b>					
GNPA	1.2	1.6	1.5	1.6	1.6
NNPA	0.5	0.9	0.5	0.5	0.4
Provision coverage	56.3	45.5	68.8	70.9	78.0
<b>Ratios (%)</b>					
Credit-Deposit	95.6	95.7	101.9	101.3	100.6
Investment-Deposit	33.0	30.4	30.0	30.0	29.3
CAR	15.0	13.4	13.6	13.4	12.9
Tier-1	14.6	13.0	13.1	13.0	12.4

Source: Company, BOBCAPS Research

## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

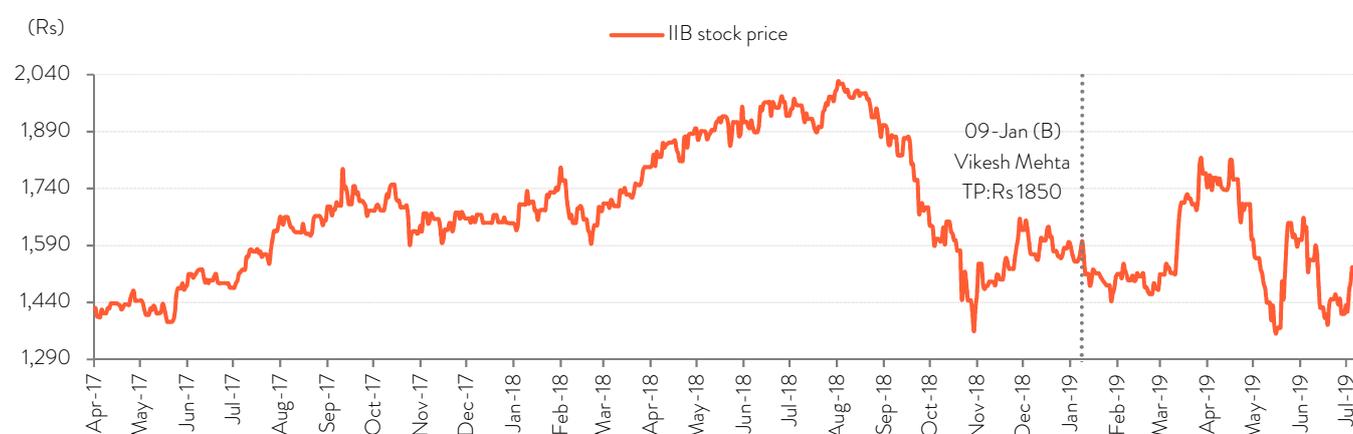
**ADD** – Expected return from >+5% to +15%

**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: INDUSIND BANK (IIB IN)



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

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