

BUY

TP: Rs 1,550 | ▲26%

INDUSIND BANK

| Banking

| 10 October 2019

Asset quality blip, loan growth drops

IndusInd Bank's (IIB) Q2FY20 PAT grew 52% YoY to Rs 14bn, largely due to 32% YoY growth in NII and 5bps QoQ NIM expansion to 4.1%. IIB made accelerated provisions worth Rs 3.6bn which drove PCR higher to 50% vs. 43% in Q1. Tax savings adjusted for DTA mark-down were Rs 1.9bn. Exposure to stressed groups fell to 1.1% but asset quality deteriorated as slippages rose to Rs 9.6bn and SMA-2 loan share spiked to 0.58%. Loan growth plunged to 21% YoY – we cut FY20-FY22 EPS by 12-20% on slow growth and lower our Sep'20 TP to Rs 1,550 (vs. Rs 1,850).

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Miss on asset quality: IIB's exposure to stressed groups declined to 1.1% in Q2 (1.7% in Q1) and is expected to dip further to 0.8% in Q3 given repayments. But overall slippages (ex-technical) climbed to Rs 9.6bn vs. Rs 7.3bn in Q1. Also, SMA-2 loans rose to Rs 11.4bn (0.58% of loans) vs. Rs 3.2bn (0.17%) in Q1.

GNPA in the MFI segment rose to 0.94% (vs. 0.61% in Q1) given floods across multiple states. However, repayments have begun and collection efficiency in the portfolio is back to 98-99%. IIB has signed inter-creditor agreements for 0.18% of loans and, barring the vehicle finance (VF) portfolio, recognises NPAs on a daily basis across segments.

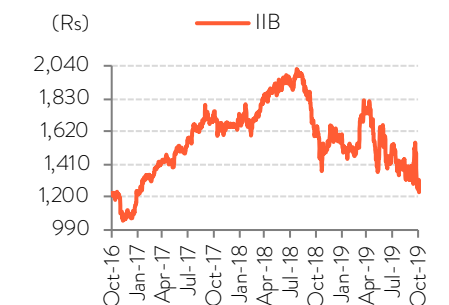
Loan growth moderates: Loan growth at 21% YoY was the lowest in recent times. IIB's VF book grew 21% YoY and non-VF retail was up 18% while MFI grew 23%. Corporate loans grew ~14% on average but with repayments and sale of assets worth Rs 30bn (Rs 60bn in Q1), overall growth slipped to ~7% YoY.

Maintain BUY with revised TP of Rs 1,550: We pare FY20-FY22 EPS by 12-20% to factor in slower growth and a marginal rise in credit costs. We now value the stock at 2.3x Sep'21E BV to arrive at a TP of Rs 1,550 (vs. Rs 1,850).

Ticker/Price	IIB IN/Rs 1,229
Market cap	US\$ 10.4bn
Shares o/s	603mn
3M ADV	US\$ 109.7mn
52wk high/low	Rs 1,834/Rs 1,188
Promoter/FPI/DII	17%/52%/31%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
Net interest income	74,974	88,462	121,131	141,941	177,991
NII growth (%)	23.7	18.0	36.9	17.2	25.4
Adj. net profit (Rs mn)	36,060	33,011	54,079	69,042	89,751
EPS (Rs)	60.2	54.9	82.5	97.5	126.8
P/E (x)	20.4	22.4	14.9	12.6	9.7
P/BV (x)	3.1	2.8	2.4	2.0	1.7
ROA (%)	1.8	1.3	1.7	1.7	1.8
ROE (%)	16.2	13.1	17.2	17.2	18.7

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q2FY20	Q2FY19	Q1FY20	YoY (%)	QoQ (%)
Income statement					
Net interest income	29,094	22,033	28,440	32.0	2.3
Non-interest income	17,272	13,173	16,633	31.1	3.8
Core fee	14,680	12,180	14,210	20.5	3.3
Securities / MM / FX Trading	2,590	990	2,410	161.6	7.5
Net total income	46,365	35,206	45,072	31.7	2.9
Staff expenses	7,165	4,582	6,472	56.4	10.7
Other expenses	12,966	10,699	12,691	21.2	2.2
Total operating expenses	20,131	15,281	19,163	31.7	5.1
Pre-provisioning profit	26,234	19,924	25,910	31.7	1.3
Provisions	7,377	5,903	4,306	25.0	71.3
Profit before tax	18,857	14,022	21,603	34.5	(12.7)
Tax	4,848	4,819	7,278	0.6	(33.4)
Profit after tax	14,010	9,203	14,325	52.2	(2.2)
Balance sheet					
Loans	1,971,126	1,631,443	1,935,200	20.8	1.9
Deposits	2,071,934	1,682,193	2,005,860	23.2	3.3
CASA ratio (%)	41.4	43.6	43.1	(219bps)	(171bps)
Yields and margins (%)					
Yield on advances	12.0	11.4	12.0	60bps	4bps
Yield on assets	10.0	9.5	10.0	52bps	1bps
Cost of deposits	6.7	6.5	6.9	16bps	(16bps)
Cost of funds	5.9	5.6	5.9	26bps	(4bps)
Net interest margin	4.1	3.8	4.1	26bps	5bps
Key ratios (%)					
Cost / income ratio	43.4	43.4	42.5	1bps	90bps
Tax rate	25.7	34.4	33.7	(866bps)	(798bps)
Loan to deposit ratio	95.1	97.0	96.5	(185bps)	(134bps)
Capital adequacy (%)					
Tier I	14.3	13.9	14.5	41bps	(20bps)
Total CAR	14.7	14.3	14.9	42bps	(20bps)
Asset quality					
Gross NPA	43,702	17,814	41,997	145.3	4.1
Net NPA	22,026	7,876	23,805	179.7	(7.5)
Coverage ratio (%)	49.6	55.8	43.3	(619bps)	628bps
Gross NPA ratio (%)	2.2	1.1	2.2	110bps	4bps
Net NPA ratio (%)	1.1	0.5	1.2	64bps	(11bps)

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.

The stock is currently trading at 2.4x FY21E P/BV. We sharply reduce our loan growth projections and raise credit cost estimates, which drives a 12-20% reduction in EPS estimates for FY20-FY22. We also lower our target P/B multiple to 2.3x from 2.6x earlier in light of the uncertainty surrounding IIB's asset quality. Using the Gordon growth model, we arrive at a revised Sep'20 target price of Rs 1,550 (vs. Rs 1,850 earlier). Maintain BUY.

FIG 2 – REVISED ESTIMATES

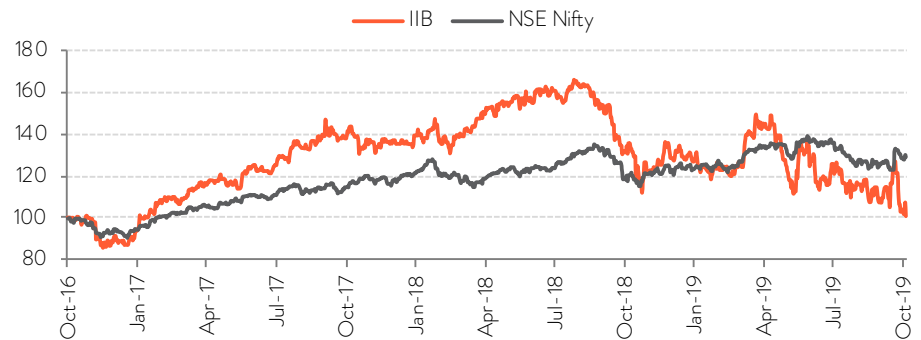
Particulars (Rs mn)	Old			New			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Net interest income	132,974	168,819	211,734	121,131	141,941	177,991	(8.9)	(15.9)	(15.9)
Pre-provisioning profit	112,343	143,770	182,575	102,928	122,133	155,378	(8.4)	(15.0)	(14.9)
Profit after tax	61,174	85,353	110,360	54,079	69,042	89,751	(11.6)	(19.1)	(18.7)
EPS (Rs)	93	121	156	83	98	127	(11.6)	(19.1)	(18.7)

Source: BOBCAPS Research

FIG 3 – VALUATION SNAPSHOT

Components of Gordon growth model	Assumptions (%)
Risk-free rate (%)	7.0
Equity risk premium (%)	5.0
Beta	1.4
Cost of equity (%)	14.2
Blended ROE (%)	19.6
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)	2
Adj. BVPS (Rs)	668
Value per share (Rs)	1,550

Source: Company, BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE

Source: NSE

Key risks

- Romesh Solti'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
Net interest income	74,974	88,462	121,131	141,941	177,991
NII growth (%)	23.7	18.0	36.9	17.2	25.4
Non-interest income	47,501	56,467	67,794	82,027	101,316
Total income	122,475	144,929	188,925	223,969	279,307
Operating expenses	(55,914)	(64,047)	(85,996)	(101,835)	(123,929)
Operating profit	66,561	80,882	102,928	122,133	155,378
Operating profit growth (%)	22.1	21.5	27.3	18.7	27.2
Provisions	(11,754)	(31,077)	(27,654)	(29,335)	(34,746)
PBT	54,807	49,806	75,274	92,798	120,633
Tax	(18,747)	(16,795)	(21,195)	(23,756)	(30,882)
Reported net profit	36,060	33,011	54,079	69,042	89,751
Adjustments	0	0	0	0	0
Adjusted net profit	36,060	33,011	54,079	69,042	89,751

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	354,897	434,342	511,493
Net worth	238,416	266,860	361,977	441,423	518,574
Deposits	1,516,392	1,948,679	2,451,497	3,082,464	3,878,127
Borrowings	382,891	473,211	686,752	798,931	926,746
Other liabilities & provisions	78,563	89,444	94,489	99,823	105,463
Total liabilities and equities	2,216,262	2,778,194	3,594,715	4,422,641	5,428,909
Cash & bank balance	132,159	147,834	158,267	169,636	182,033
Investments	500,767	592,662	736,843	924,040	1,136,435
Advances	1,449,537	1,863,935	2,292,640	2,865,872	3,582,431
Fixed & Other assets	133,799	173,764	406,965	463,093	528,010
Total assets	2,216,262	2,778,194	3,594,715	4,422,641	5,428,909
Deposit growth (%)	19.8	28.5	25.8	25.7	25.8
Advances growth (%)	28.2	28.6	23.0	25.0	25.0

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19P	FY20E	FY21E	FY22E
EPS	60.2	54.9	82.5	97.5	126.8
Dividend per share	7.2	9.0	9.2	11.7	15.2
Book value per share	391.2	437.4	506.6	618.8	727.8

Source: Company, BOBCAPS Research

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19P	FY20E	FY21E	FY22E
P/E	20.4	22.4	14.9	12.6	9.7
P/BV	3.1	2.8	2.4	2.0	1.7
Dividend yield (%)	0.6	0.7	0.7	1.0	1.2

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19P	FY20E	FY21E	FY22E
Net interest income	3.7	3.5	3.8	3.5	3.6
Non-interest income	2.4	2.3	2.1	2.0	2.1
Operating expenses	2.8	2.6	2.7	2.5	2.5
Pre-provisioning profit	3.3	3.2	3.2	3.0	3.2
Provisions	0.6	1.2	0.9	0.7	0.7
PBT	2.7	2.0	2.4	2.3	2.4
Tax	0.9	0.7	0.7	0.6	0.6
ROA	1.8	1.3	1.7	1.7	1.8
Leverage (x)	9.0	9.9	10.1	10.0	10.3
ROE	16.2	13.1	17.2	17.2	18.7

Ratio Analysis

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
YoY growth (%)					
Net interest income	23.7	18.0	36.9	17.2	25.4
Pre-provisioning profit	22.1	21.5	27.3	18.7	27.2
EPS	25.2	(8.8)	50.3	18.2	30.0
Profitability & Return ratios (%)					
Net interest margin	4.0	3.8	4.2	4.0	4.0
Fees / Avg. assets	1.7	1.6	1.5	1.5	1.5
Cost-Income	45.7	44.2	45.5	45.5	44.4
ROE	16.2	13.1	17.2	17.2	18.7
ROA	1.8	1.3	1.7	1.7	1.8
Asset quality (%)					
GNPA	1.2	2.1	1.8	1.7	1.7
NNPA	0.5	1.2	0.5	0.3	0.1
Provision coverage	56.3	43.0	74.0	84.1	93.7
Ratios (%)					
Credit-Deposit	95.6	95.7	93.5	93.0	92.4
Investment-Deposit	33.0	30.4	30.1	30.0	29.3
CAR	15.0	14.2	14.3	14.1	13.4
Tier-1	14.6	13.7	13.9	13.6	12.9

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

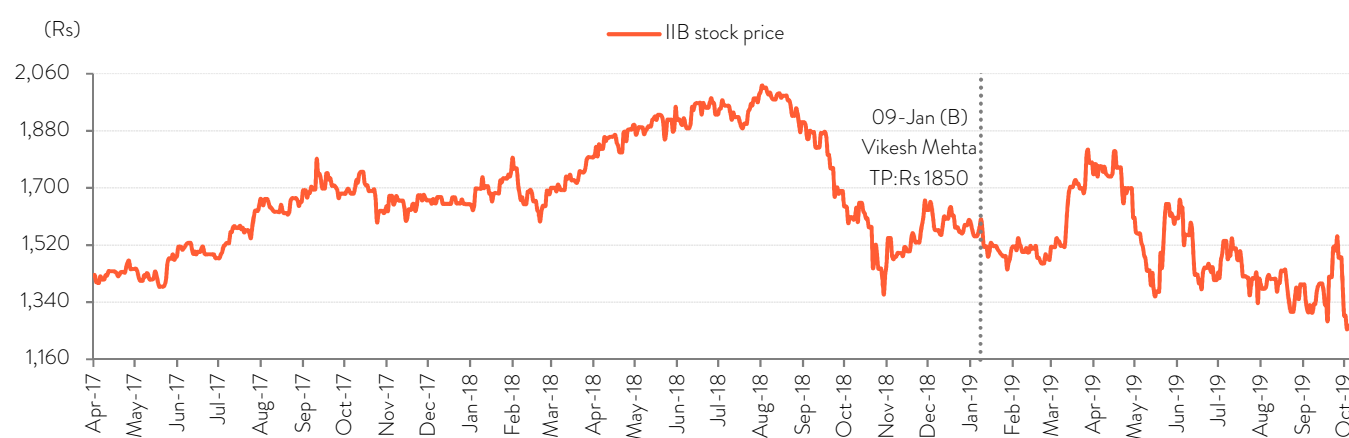
ADD – Expected return from >+5% to +15%

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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