

## Axis Bank

### Axis to continue business growth

**Despite slow down in the industry, Axis Bank continues to deliver strong business growth:** Axis Bank has been able to outpace the industry growth delivering 19% CAGR in loan book over FY12-16. The key driving force has been the retail business (39% CAGR), whose share has gone up to 41% from 21% during the same period. The management has been reiterating its stand on pick up in retail loans, which is visible from the 24.3% growth during Q1FY17. Corporate loans also witnessed strong growth during Q1FY17 by 21%. Hence, we believe the bank has potential to deliver 20% CAGR in loan for next 2-3 years & sharp moderation in growth is unlikely.

**Asset quality woes restricted to the watch list:** Axis bank came out with a watch list of ₹22,628cr worth of loans at the end of Q4FY16, estimating 60% of that could fall into NPA over the next 2 years with a bias towards higher slippages in FY17. Accordingly, the bank saw slippages of ₹3,638cr in Q1FY17, reducing the watch list amount by 10.3%. Almost 74% of the slippages (₹2,680cr) came from the watch list, while slippages from non watch list corporate book accounted for 6% of the gross slippages.

Balance 20% slippages came from Non Corporate book. As expected, large part of the slippages came from the corporate loans within the watch list. While, it is a known fact that in absolute terms there would be a rise in NPA and their ratio will go up. However, there is low probability of negative surprise from the non watch list accounts turning into large scale NPAs.

**We expect RoE to bounce back in FY18:** Axis Bank has maintained RoE of 16-17% over the last 3 years. Their ability to contain credit cost and higher traction in fee income were the driving forces behind the strong RoE. However, the management has already come out with a watch list and has given a higher credit cost guidance of 125-150 bps for FY17 vs 92 bps/ 83 bps/110 bps in FY14/FY15/16, respectively. This indicates that bottom-line will be under pressure. While, FY17 will see RoE falling to 13.6% vs 16.8% in FY16, we expect the same to bounce back to 16.5% by FY18. Ability to grow retail loans would be one of the keys for maintaining strong RoE & we believe the bank will be able to sustain RoE of 16-17% in the medium term.

**Outlook and valuation:** Declaring the watch list gave the much required clarity on the book for the Bank. While credit cost will remain high and in turn RoE will be under pressure for FY17; once the cleaning up process is over, we can expect RoE rebounding and Axis Bank can be a re-rating candidate. At the current levels, the stock trades at 2x its FY18E Adj BV of ₹268. Thus, we believe the current corrections in the stock gives long term investors an opportunity to enter the stock. **We upgrade the stock to a BUY with a target price of ₹630.**

#### Key financials (Standalone)

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
<b>Nil</b>	<b>14,224</b>	<b>16,833</b>	<b>19,077</b>	<b>22,035</b>
% chg	19.0	18.3	13.3	15.5
<b>Net profit</b>	<b>7,358</b>	<b>8,224</b>	<b>7,723</b>	<b>10,669</b>
% chg	18.3	11.8	-6.1	38.2
NIM (%)	3.5	3.6	3.5	3.4
<b>EPS (₹)</b>	<b>31.0</b>	<b>34.5</b>	<b>32.3</b>	<b>44.6</b>
P/E (x)	17.7	15.9	17.0	12.3
P/ABV (x)	2.6	2.4	2.1	1.9
RoA (%)	1.7	1.7	1.3	1.6
RoE (%)	17.9	16.8	13.6	16.5

Source: Company, Angel Research; Note: CMP as of October 5, 2016

## BUY

CMP	₹536
Target Price	₹630

Investment Period	12 Months
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#### Stock Info

Sector	Banking
Market Cap (₹ cr)	1,28,019
Beta	1.4
52 Week High / Low	638 / 367
Avg. Daily Volume	879,954
Face Value (₹)	2
BSE Sensex	28,221
Nifty	8,744
Reuters Code	AXBK.BO
Bloomberg Code	AXSB@IN

#### Shareholding Pattern (%)

Promoters	29.7
MF / Banks / Indian Fls	14.2
FII / NRIs / OCBs	48.1
Indian Public / Others	8.0

Abs. (%)	3m	1yr	3yr
Sensex	3.9	8.1	42.3
Axis Bank	0.2	4.6	150.5

#### 3-year price chart



Source: Company, Angel Research

#### Siddharth Purohit

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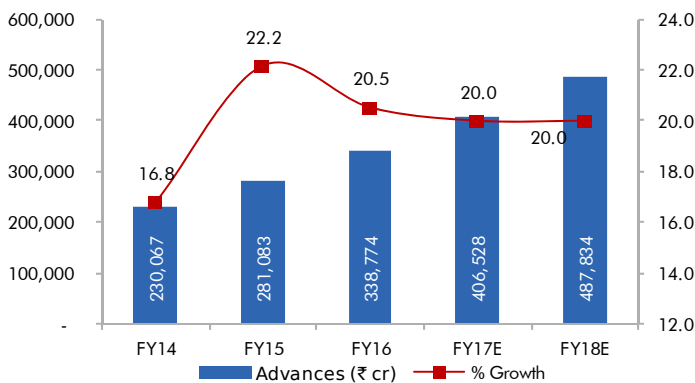
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## Should we expect moderation in growth?

Axis Bank has been able to outpace the industry growth and has delivered 19% CAGR in loan book over FY12-16. The key driving force behind the growth has been the retail business, which had delivered a staggering 39% CAGR over the same period. Axis has been able to increase the share of retail loans from 22% to 41% during the same period. It seems there is further scope for the bank to increase its share of retail loans.

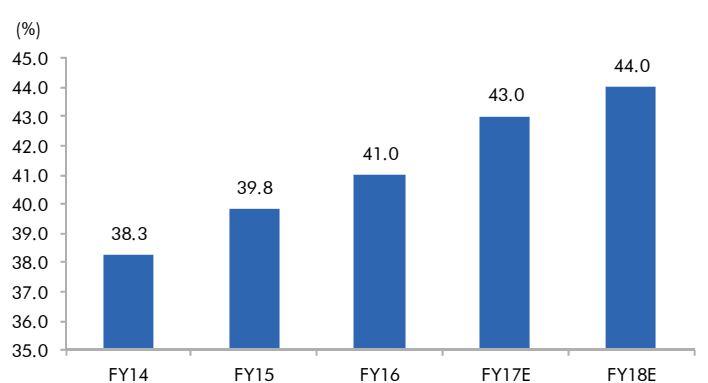
In the last 4 years, the management has aggressively expanded the retail credit book and that too without compromising in the asset quality. During Q1FY17, slippages ratio in the retail loan book stood at 0.7% compared to 4.2% overall slippages and 7.5% corporate slippages. The management has been reiterating that retail will continue to grow stronger and retail loans grew by 24.3% during Q1FY17. On the other hand, even the corporate loan book has witnessed strong growth during Q1FY17 by 21%. Hence, we believe the bank has enough potential to deliver 20% CAGR for next 2-3 years and sharp moderation in the business growth is very unlikely.

**Exhibit 1: Loan Book growth %**



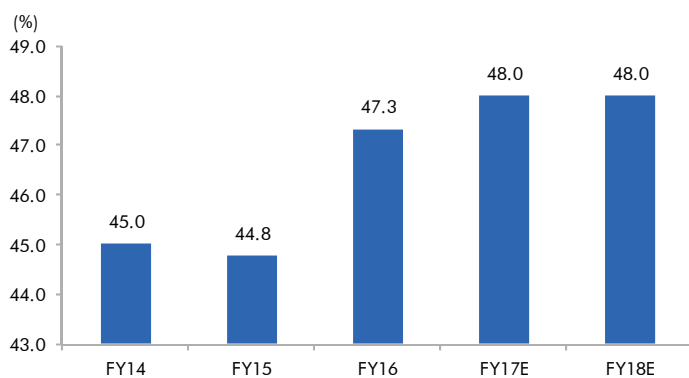
Source: Company, Angel Research

**Exhibit 2: Retail Loan Book %**



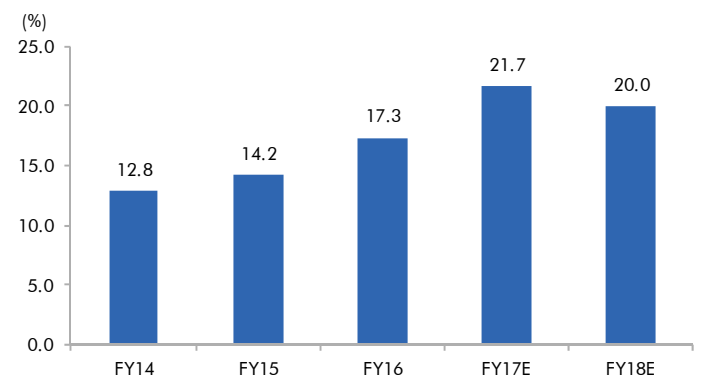
Source: Company, Angel Research

**Exhibit 3: CASA %**



Source: Company, Angel Research

**Exhibit 4: CASA Growth remains strong**



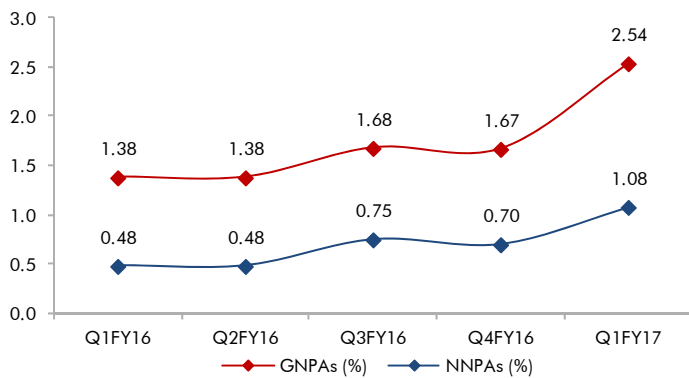
Source: Company, Angel Research

### Can asset quality further deteriorate for Axis Bank?

The bank came out with strong disclosure at the end of Q4FY16 in which, the management outlined that ~₹22,628cr worth of loans were under stress and estimated ~60% could fall into NPA over the next eight quarters. Further, large part of the incremental NPA from this account are likely to come up in FY17 itself. Accordingly, the bank saw slippages of ₹3,638cr during Q1FY17. The watch list amount was reduced by 10.3% post slippages from that account.

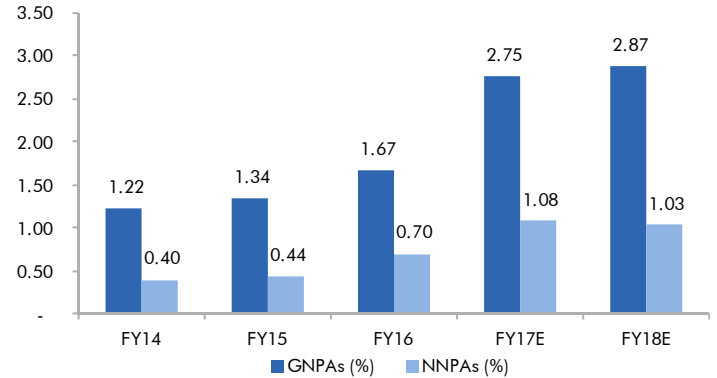
A close watch into the slippages shows that ₹2,680cr i.e 74% of the total slippages came from the watch list itself, while slippages from non watch list corporate book accounted for 6% of the gross slippages. The balance 20% slippages came from Non Corporate book. This indicates that, as expected, large part of the slippages is in fact coming in from the corporate segment within the watch list. While, it is a known fact that in absolute terms there would be a rise in NPA and the NPA ratios will go up. However, there is low probability of negative surprises from the non watch list accounts turning into large scale NPAs.

**Exhibit 5: GNPA's & NNPA's Ratio Quarterly trend**



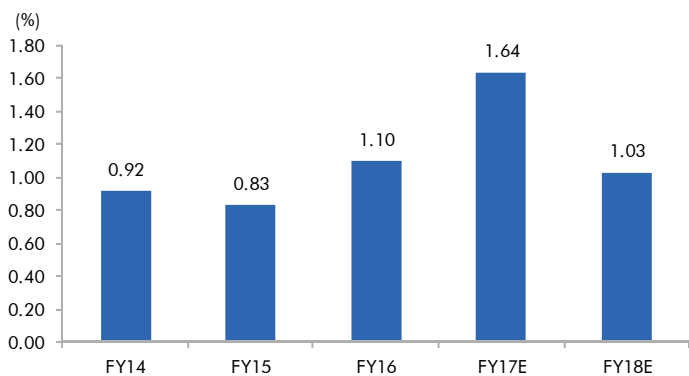
Source: Company, Angel Research;

**Exhibit 6: GNPA's & NNPA's Ratio yearly trend**



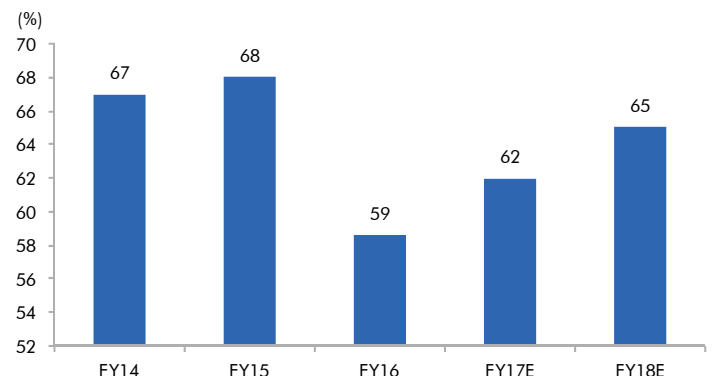
Source: Company, Angel Research

**Exhibit 7: Credit Cost %**



Source: Company, Angel Research

**Exhibit 8: PCR %**

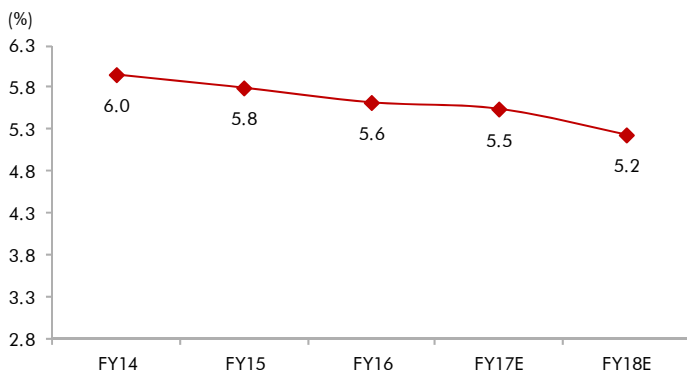


Source: Company, Angel Research

### How sustainable is the RoE?

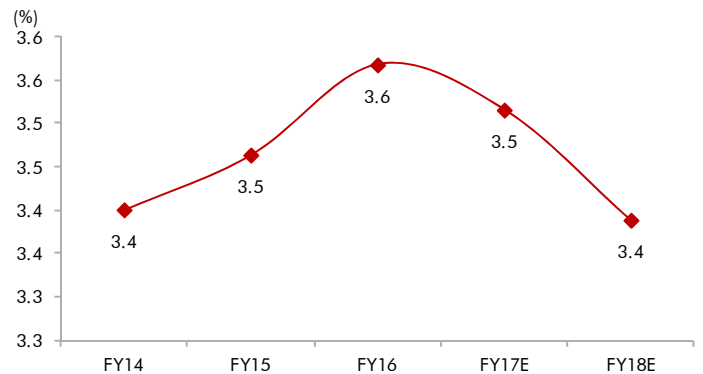
Axis Bank has maintained RoE of 16-17% over the last three years. Their ability to contain credit cost and higher traction in fee income were the driving forces behind the strong RoE. However, the management has already come out with a watch list and has given a higher credit cost guidance of 125-150 bps for FY17 vs 92 bps/ 83 bps/110 bps in FY14/FY15/16, respectively. This indicates that bottom-line will be under pressure. However, we have factored in a credit cost of 164 bps for FY17 and 103 bps for FY18. While, FY17 will see RoE falling to 13.6% vs 16.8% in FY16, we expect the same to bounce back to 16.5% by FY18 end. Ability to sustain the retail loans would be one of the keys for maintaining strong RoE and we believe the bank will be able to sustain RoE of 16-17% in the medium term.

**Exhibit 9: Cost Funds have declined**



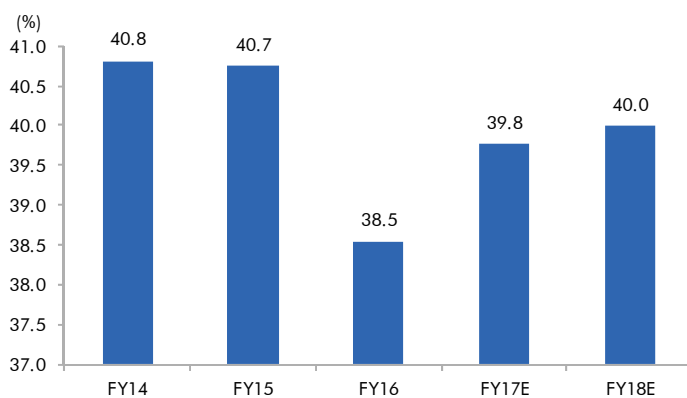
Source: Company, Angel Research;

**Exhibit 10: NIM Trend**



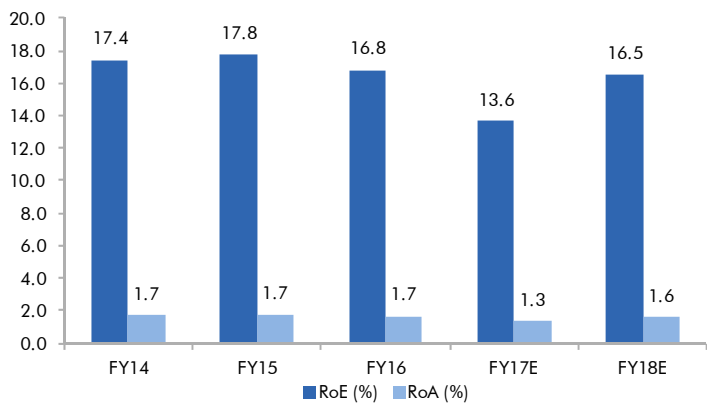
Source: Company, Angel Research

**Exhibit 11: Cost/ Income Ratio**



Source: Company, Angel Research;

**Exhibit 12: ROE & ROA%**



Source: Company, Angel Research

### **Is re-rating possible in the near term and how valuations look as compared to peers?**

Both Axis Bank and ICICI Bank came out with strong disclosures during Q4FY16 results. In absolute terms, both the banks have declared assets, which are sticky and have potential to slip into NPA. However, the management of Axis Bank estimated 60% of the ₹22,628 cr worth of loans, which are under watch list, could fall into NPA category over the next eight quarters. While, the watch list was 13% of the corporate assets, which seems high; it gave the much required clarity on the book. Credit cost will remain high and in turn RoE will be under pressure for FY17; but once the cleaning up process is over, we can expect RoE rebounding and Axis Bank can be a re-rating candidate.

At the CMP, the stock trades at 2x its FY18E Adj BV of ₹ 268. We believe that the current corrections in the stock give long term investors an opportunity to enter the stock. **We upgrade the stock to a BUY with a target price of ₹630.**

### **Company Background**

Axis Bank is India's third largest private sector bank, after ICICI and HDFC. The bank is promoted by government institutions led by UTI (SUUTI currently holds 12% stake in the bank). It has an extensive network of 3006 branches and 12,871 ATMs spread across 1,882 centers. The bank's strong growth has been backed by robust retail branch expansion, strong corporate relationships and a wide range of fee income products.

**Income statement (Standalone)**

Y/E March (₹ cr)	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E
<b>Net Interest Income</b>	<b>8,018</b>	<b>9,666</b>	<b>11,952</b>	<b>14,224</b>	<b>16,833</b>	<b>19,077</b>	<b>22,035</b>
- YoY Growth (%)	22.2	20.6	23.6	19.0	18.3	13.3	15.5
<b>Other Income</b>	<b>5,420</b>	<b>6,551</b>	<b>7,405</b>	<b>8,365</b>	<b>9,371</b>	<b>11,149</b>	<b>12,884</b>
- YoY Growth (%)	17.0	20.9	13.0	13.0	12.0	19.0	15.6
<b>Operating Income</b>	<b>13,438</b>	<b>16,217</b>	<b>19,357</b>	<b>22,589</b>	<b>26,204</b>	<b>30,226</b>	<b>34,919</b>
- YoY Growth (%)	20.0	20.7	19.4	16.7	16.0	15.3	15.5
<b>Operating Expenses</b>	<b>6,007</b>	<b>6,914</b>	<b>7,901</b>	<b>9,204</b>	<b>10,101</b>	<b>12,018</b>	<b>13,963</b>
- YoY Growth (%)	25.7	15.1	14.3	16.5	9.7	19.0	16.2
<b>Pre - Provision Profit</b>	<b>7,431</b>	<b>9,303</b>	<b>11,456</b>	<b>13,385</b>	<b>16,104</b>	<b>18,209</b>	<b>20,956</b>
- YoY Growth (%)	15.8	25.2	23.1	16.8	20.3	13.1	15.1
<b>Prov. &amp; Cont.</b>	<b>1,143</b>	<b>1,750</b>	<b>2,107</b>	<b>2,329</b>	<b>3,710</b>	<b>6,652</b>	<b>5,031</b>
- YoY Growth (%)	(10.7)	53.1	20.4	10.5	59.3	79.3	(24.4)
<b>Profit Before Tax</b>	<b>6,288</b>	<b>7,553</b>	<b>9,349</b>	<b>11,057</b>	<b>12,394</b>	<b>11,557</b>	<b>15,924</b>
- YoY Growth (%)	22.4	20.1	23.8	18.3	12.1	(6.8)	37.8
<b>Prov. for Taxation</b>	<b>2,046</b>	<b>2,373</b>	<b>3,131</b>	<b>3,699</b>	<b>4,170</b>	<b>3,834</b>	<b>5,255</b>
- as a % of PBT	32.5	31.4	33.5	33.5	33.6%	33.2%	33.0%
<b>PAT</b>	<b>4,242</b>	<b>5,179</b>	<b>6,218</b>	<b>7,358</b>	<b>8,224</b>	<b>7,723</b>	<b>10,669</b>
- YoY Growth (%)	25.2	22.1	20.0	18.3	11.8	(6.1)	38.2

**Balance sheet (Standalone)**

Y/E March (₹ cr)	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E
Share Capital	413	468	470	474	477	477	478
Reserve & Surplus	22,395	32,640	37,751	43,463	52,688	59,635	68,704
Deposits	2,20,104	2,52,614	2,80,945	3,22,442	357,968	429,561	515,473
- Growth (%)	16.3	14.8	11.2	14.8	11.0	20.0	20.0
Borrowings	23,498	31,412	37,886	64,872	99,226	118,129	141,755
Other Liab. & Prov.	8,643	10,888	13,789	15,795	15,109	18,042	23,196
<b>Total Liabilities</b>	<b>2,85,628</b>	<b>3,40,561</b>	<b>3,83,245</b>	<b>4,61,932</b>	<b>525,468</b>	<b>625,845</b>	<b>749,607</b>
Cash Balances	10,703	14,792	17,041	19,819	22,361	21,478	25,774
Bank Balances	3,231	5,643	11,197	16,280	10,964	17,182	20,619
Investments	93,192	1,13,738	1,13,548	1,32,343	122,006	146,051	175,261
Advances	1,69,760	1,96,966	2,30,067	2,81,083	338,774	406,528	487,834
- Growth (%)	19.2	16.0	16.8	22.2	20.5	20.0	20.0
Fixed Assets	2,259	2,356	2,410	2,514	3,523	4,162	4,962
Other Assets	6,483	7,067	8,981	9,893	27,839	30,442	35,157
<b>Total Assets</b>	<b>2,85,628</b>	<b>3,40,561</b>	<b>3,83,245</b>	<b>4,61,932</b>	<b>525,468</b>	<b>625,845</b>	<b>749,607</b>
- Growth (%)	17.7	19.2	12.5	20.5	13.8	19.1	19.8

**Ratio analysis (Standalone)**

Y/E March	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E
<b>Profitability ratios (%)</b>							
NIMs	3.1	3.2	3.4	3.5	3.6	3.5	3.4
Cost to Income Ratio	44.7	42.6	40.8	40.7	38.5	39.8	40.0
RoA	1.6	1.7	1.7	1.7	1.7	1.3	1.6
RoE	20.3	18.5	17.4	17.9	16.8	13.6	16.5
<b>B/S ratios (%)</b>							
CASA Ratio	41.5	44.4	45.0	44.8	47.3	48.0	48.0
Credit/Deposit Ratio	77.1	78.0	81.9	87.2	94.6	94.6	94.6
CAR	13.7	17.0	16.3	16.0	15.4	14.8	13.9
- Tier I	9.4	12.2	12.8	12.2	12.6	12.2	11.7
<b>Asset Quality (%)</b>							
Gross NPAs	1.1	1.2	1.4	1.4	1.7	2.8	2.9
Net NPAs	0.3	0.4	0.4	0.5	0.7	1.1	1.0
Slippages	1.3	1.2	1.3	1.2	2.5	1.6	0.8
Loan Loss Prov. /Avg. Assets	0.3	0.4	0.4	0.5	1.1	1.6	1.0
Provision Coverage	73.8	70.6	77.2	68.0	58.6	62.0	65.0
<b>Per Share Data (₹)</b>							
EPS	20.5	22.1	26.5	31.0	34.5	32.3	44.6
ABVPS	110.3	141.0	161.7	184.1	212.5	233.5	268.4
DPS	3.2	3.6	4.0	5.9	5.0	6.0	6.5
<b>Valuation Ratios</b>							
PER (x)	19.9	18.5	15.4	13.2	15.9	17.0	12.3
P/ABVPS (x)	3.7	2.9	2.5	2.2	2.4	2.1	1.9
Dividend Yield	0.8	0.9	1.0	1.4	0.9	1.1	1.2
<b>DuPont Analysis</b>							
NII	3.0	3.1	3.3	3.4	3.4	3.3	3.2
(-) Prov. Exp.	0.4	0.6	0.6	0.6	0.8	1.2	0.7
Adj. NII	2.6	2.5	2.7	2.8	2.7	2.2	2.5
Other Inc.	2.0	1.9	2.0	1.7	1.9	1.9	1.9
Op. Inc.	4.7	4.6	4.8	4.8	4.6	4.1	4.3
Opex	2.3	2.2	2.2	2.2	2.0	2.1	2.0
PBT	2.4	2.4	2.6	2.6	2.5	2.0	2.3
Taxes	0.8	0.8	0.9	0.9	0.8	0.7	0.8
<b>RoA</b>	<b>1.6</b>	<b>1.7</b>	<b>1.7</b>	<b>1.7</b>	<b>1.7</b>	<b>1.3</b>	<b>1.6</b>
Leverage	12.6	11.2	10.1	10.3	10.1	10.2	10.6
<b>RoE</b>	<b>20.3</b>	<b>18.5</b>	<b>17.4</b>	<b>17.9</b>	<b>16.8</b>	<b>13.6</b>	<b>16.5</b>

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### Disclosure of Interest Statement

### Axis Bank

1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

*Note: We have not considered any Exposure below ₹ 1 lakh for Angel, its Group companies and Directors*

**Ratings (Based on expected returns over 12 months investment period):**

Buy (> 15%)

Accumulate (5% to 15%)  
Reduce (-5% to -15%)

Neutral (-5 to 5%)  
Sell (< -15)