

Axis Bank

Earnings to normalize with stabilizing credit costs

Axis is the third-largest private sector bank in India in terms of asset size, with a balance sheet of ~7.1 lakh cr and advances of 4.48 lakh cr (of which retail contributes 48.6%). It has a network of over 3,882 branches with CASA of 47.7%. The appointment of Amitabh Chaudhary as MD & CEO for three years beginning from January 01, 2019, shrinking stressed asset and incremental lending to high rated corporates would aid Axis Bank to restore investor confidence.

Nearing end of NPA recognition and incremental lending to high rated corporates: Axis Bank's GNPA was lower at 1.67% in FY2016, however it peaked at 6.77% in FY2018, largely owing to legacy corporate loans (Watchlist). Consequently, slippages jumped from 2.6% in FY2016 to 8% in FY2018. However, slippages for Q2FY2019 were lowest in past nine quarters. As on Q2FY2019, 60% of the bank's stressed asset pool has been recognised as NPAs, hence we expect the pace of incremental slippages to decline. Shift towards high rated corporates (FY2016 - 62% to Q2FY2019 - 79%), reduction in slippages and healthy coverage of 58% (if we include technical write-off, 73%) on NPLs would keep credit cost under control.

Improvement in NIM and return ratio: Axis Bank's NIM has been under pressure owing to higher slippages. However, we expect NIM to improve 30bps to 3.4% by FY2020 led by (1) lower interest reversal, (2) bank has increased MCLR by 50bps in last three quarters and 54% advances are linked to MCLR, (3) opened 578 branches, which would help them to strengthen retail asset book but at the same it would also help them to garner CASA and retail deposits.

Return ratio to improve: Asset quality issue has adversely impacted ROE/ROA. We expect decline in credit cost and improvement in net interest margin along with growth in advances to normalize the return ratios.

Outlook & Valuation: Axis Bank currently trades at 2.1x its FY2020E price to book value (after adjusting value of subsidiaries). We expect the stock to get re-rated owing to (1) new leadership, (2) limited stressed loan pool, (3) improvement in return ratios (ROA/ROE – 1.1%/12.2% by FY2020E). We recommend Buy on the stock, with a target price of ₹750.

Key Financials

| Y/E March (₹ cr) | FY16 | FY17 | FY18 | FY19E | FY20E |
|------------------|--------|--------|--------|--------|--------|
| NII | 16,833 | 18,093 | 18,618 | 21,771 | 26,195 |
| % chg | 18 | 7 | 3 | 17 | 20 |
| Net profit | 8,224 | 3,679 | 276 | 4,331 | 8,769 |
| % chg | 12 | -55 | (93) | 1,471 | 102 |
| NIM (%) | 3.6 | 3.4 | 3.1 | 3.2 | 3.4 |
| EPS (₹) | 32 | 14 | 1 | 17 | 34 |
| P/E (x) | 20 | 44 | 585 | 37 | 18 |
| P/ABV (x) | 3.1 | 3.0 | 2.8 | 2.5 | 2.2 |
| RoA (%) | 1.6 | 0.6 | 0.0 | 0.6 | 1.1 |
| RoE (%) | 17 | 7 | 0 | 7 | 12 |

Source: Company, Angel Research; Note: CMP as of 1/1/19

BUY

| | |
|--------------|------|
| CMP | ₹620 |
| Target Price | ₹750 |

| | |
|-------------------|-----------|
| Investment Period | 12 Months |
|-------------------|-----------|

Stock Info

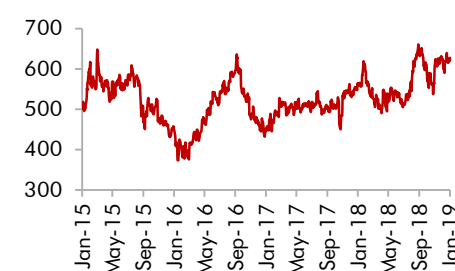
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|--------------------|-----------|
| Sector | Banking |
| Market Cap (₹ cr) | 1,59,051 |
| Beta | 1.4 |
| 52 Week High / Low | 676/477 |
| Avg. Daily Volume | 7,72,545 |
| Face Value (₹) | 2 |
| BSE Sensex | 35,891 |
| Nifty | 10,792 |
| Reuters Code | AXBK.NS |
| Bloomberg Code | AXSB.NATL |

Shareholding Pattern (%)

| | |
|-------------------------|------|
| Promoters | 25.0 |
| MF / Banks / Indian Fls | 11.4 |
| FII / NRIs / OCBs | 55.3 |
| Indian Public / Others | 8.3 |

| Abs. (%) | 3m | 1yr | 3yr |
|----------|-------|------|------|
| Sensex | (0.7) | 7.3 | 37.9 |
| LTFH | 5.8 | 11.9 | 38.9 |

3-year price chart



Source: Company, Angel Research

Jaikishan Parmar

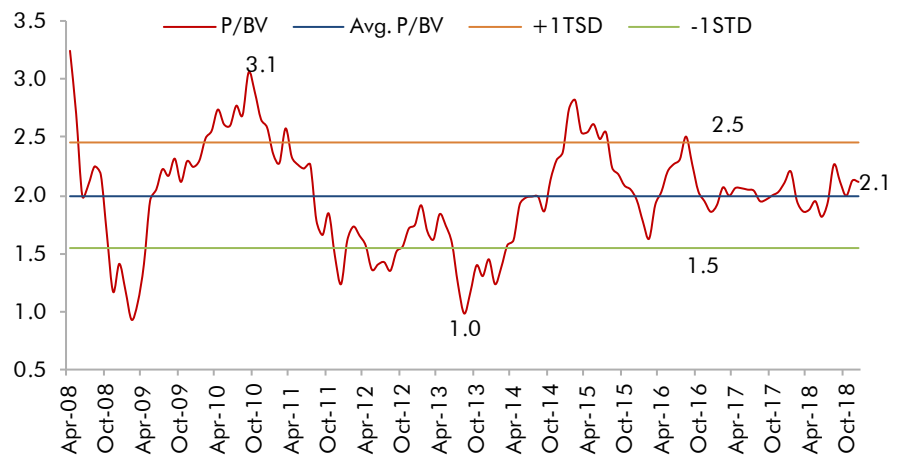
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Research Analyst

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Exhibit 1: SOTP valuation summary

| Sum of the parts | Stake in Company % | Valuation Methodology | Value/Share ₹ |
|---------------------|--------------------|-----------------------|---------------|
| Core Business | 100.0 | 2.5x FY20E ABV | 721.8 |
| Axis Capital Ltd | 100 | 15x FY20E PAT | 9.3 |
| Axis MF | 75 | 20x FY20E PAT | 3.3 |
| Axis Fin | 100 | 2x FY20E Book Value | 11.9 |
| Axis Sec | 100 | 15x FY20E PAT | 4.6 |
| Sum of Parts | | | 751.0 |

Exhibit 2: One Year Forward P/BV


Source: Company

Exhibit 3: Decline in slippages

| Particular (₹ cr) | 2QFY17 | 3QFY17 | 4QFY17 | 1QFY18 | 2QFY18 | 3QFY18 | 4QFY18 | 1QFY19 | 2QFY19 |
|------------------------|--------------|--------------|--------------|--------------|--------------|--------------|---------------|--------------|--------------|
| GNPA Opening | 9,553 | 16,379 | 20,467 | 21,280 | 22,031 | 27,402 | 25,001 | 34,249 | 32,662 |
| Fresh Slippage | 8,772 | 4,560 | 4,811 | 3,519 | 8,936 | 4,428 | 16,536 | 4,337 | 2,777 |
| Slippage | 2.5% | 1.3% | 1.3% | 0.9% | 2.2% | 1.1% | 3.8% | 1.0% | 0.6% |
| Slippage Annual | 9.9% | 5.3% | 5.2% | 3.7% | 8.7% | 4.2% | 15.0% | 3.9% | 2.4% |
| Upgrade & Rec | 1,073 | 350 | 2,804 | 306 | 1,048 | 4,008 | 3,401 | 2,917 | 2,186 |
| Write off | 873 | 122 | 1,194 | 2,462 | 2,517 | 2,821 | 3,887 | 3,007 | 2,315 |
| Closing GNPA | 16,379 | 20,467 | 21,280 | 22,031 | 27,402 | 25,001 | 34,249 | 32,662 | 30,938 |
| Prov | 8,618 | 12,172 | 12,654 | 12,265 | 13,350 | 13,232 | 17,657 | 17,760 | 18,222 |
| NPA | 7,761 | 8,295 | 8,626 | 9,766 | 14,052 | 11,769 | 16,592 | 14,902 | 12,716 |
| Prov | 3,623 | 3,796 | 2,581 | 2,342 | 3,140 | 2,811 | 7,180 | 3,338 | 2,927 |
| CC | 1.0% | 1.1% | 0.7% | 0.6% | 0.8% | 0.7% | 1.6% | 0.8% | 0.6% |
| CC Ann | 4.1% | 4.4% | 2.8% | 2.4% | 3.1% | 2.7% | 6.5% | 3.0% | 2.6% |

Source: Company

Income Statement

| Y/E March (₹ cr) | FY16 | FY17 | FY18 | FY19E | FY20E |
|-------------------------------|---------------|---------------|---------------|---------------|---------------|
| Net Interest Income | 16,833 | 18,093 | 18,618 | 21,771 | 26,195 |
| - YoY Growth (%) | 18 | 7 | 3 | 17 | 20 |
| Other Income | 9,371 | 11,691 | 10,967 | 11,466 | 13,137 |
| - YoY Growth (%) | 12 | 25 | (6) | 5 | 15 |
| Operating Income | 26,204 | 29,784 | 29,585 | 33,237 | 39,332 |
| - YoY Growth (%) | 16 | 14 | (1) | 12 | 18 |
| Operating Expenses | 10,101 | 12,200 | 13,990 | 15,704 | 17,878 |
| - YoY Growth (%) | 10 | 21 | 15 | 12 | 14 |
| Pre - Provision Profit | 16,104 | 17,585 | 15,594 | 17,533 | 21,454 |
| - YoY Growth (%) | 20 | 9 | (11) | 12 | 22 |
| Prov. & Cont. | 3,710 | 12,117 | 15,473 | 11,028 | 8,168 |
| - YoY Growth (%) | 59 | 227 | 28 | -29 | -26 |
| Profit Before Tax | 12,394 | 5,468 | 122 | 6,505 | 13,286 |
| - YoY Growth (%) | 12 | (56) | (98) | 5,251 | 104 |
| Prov. for Taxation | 4,170 | 1,788 | -154 | 2,174 | 4,517 |
| - as a % of PBT | 34 | 33 | (127) | 33 | 34 |
| PAT | 8,224 | 3,679 | 276 | 4,331 | 8,769 |
| - YoY Growth (%) | 12 | (55) | (93) | 1,471 | 102 |

Balance Sheet

| Y/E March (₹ cr) | FY16 | FY17 | FY18 | FY19E | FY20E |
|--------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Equity | 477 | 479 | 513 | 513 | 513 |
| Reserve & Surplus | 52,688 | 55,284 | 62,932 | 67,047 | 75,377 |
| Net worth | 53,165 | 55,763 | 63,445 | 67,561 | 75,891 |
| Deposits | 3,57,968 | 4,14,379 | 4,53,623 | 5,17,130 | 5,99,871 |
| - Growth (%) | 11 | 16 | 9 | 14 | 16 |
| Borrowings | 1,08,580 | 1,05,031 | 1,48,016 | 1,68,738 | 1,94,049 |
| Other Liab. & Prov. | 20,283 | 26,387 | 26,373 | 24,896 | 20,967 |
| Total Liabilities | 5,39,996 | 6,01,559 | 6,91,458 | 7,78,325 | 8,90,778 |
| Cash Balances | 22,361 | 30,858 | 35,481 | 42,269 | 43,033 |
| Bank Balances | 10,964 | 19,398 | 7,974 | 10,751 | 12,389 |
| Investments | 1,31,524 | 1,28,793 | 1,53,876 | 1,67,840 | 1,88,696 |
| Advances | 3,38,774 | 3,73,069 | 4,39,650 | 5,01,201 | 5,81,393 |
| - Growth (%) | 21 | 10 | 18 | 14 | 16 |
| Fixed Assets | 3,523 | 3,747 | 3,972 | 4,551 | 5,279 |
| Other Assets | 32,850 | 45,693 | 50,505 | 51,713 | 59,987 |
| Total Assets | 5,39,996 | 6,01,559 | 6,91,458 | 7,78,325 | 8,90,778 |
| - Growth (%) | 17 | 11 | 15 | 13 | 14 |

Source: Company

Key Ratio

| Y/E March | FY16 | FY17 | FY18 | FY19E | FY20E |
|---------------------------------|-------------|------------|------------|------------|-------------|
| Profitability ratios (%) | | | | | |
| NIMs | 3.6 | 3.4 | 3.1 | 3.2 | 3.4 |
| Cost to Income Ratio | 39 | 41 | 47 | 47 | 45 |
| RoA | 1.6 | 0.6 | 0.0 | 0.6 | 1.1 |
| RoE | 17 | 7 | 0 | 7 | 12 |
| B/S ratios (%) | | | | | |
| CASA Ratio | 47.3 | 51.4 | 53.8 | 53.8 | 53.8 |
| Credit/Deposit Ratio | 95 | 90 | 97 | 97 | 97 |
| Asset Quality (%) | | | | | |
| Gross NPAs | 1.67 | 5.04 | 6.77 | 5.0 | 4.0 |
| Net NPAs | 0.70 | 2.11 | 3.40 | 2.3 | 1.7 |
| Credit Cost | 1.1 | 3.2 | 3.5 | 2.2 | 1.4 |
| Provision Coverage | 0.58 | 0.58 | 0.50 | 0.54 | 0.58 |
| Per Share Data (₹) | | | | | |
| EPS | 32 | 14 | 1 | 17 | 34 |
| ABVPS (70% cover.) | 204 | 208 | 222 | 247 | 284 |
| DPS | 5 | 5 | 5 | 5 | 5 |
| Valuation Ratios | | | | | |
| PER (x) | 20 | 44 | 585 | 37 | 18 |
| P/ABVPS (x) | 3.1 | 3.0 | 2.8 | 2.5 | 2.2 |
| Dividend Yield (%) | 0.8 | 0.9 | 0.9 | 0.8 | 0.8 |
| DuPont Analysis | | | | | |
| Interest Income | 8.2 | 7.8 | 7.1 | 7.4 | 7.7 |
| Interest Expenses | 4.8 | 4.6 | 4.2 | 4.4 | 4.6 |
| NII | 3.4 | 3.2 | 2.9 | 3.0 | 3.1 |
| - Prov | 0.7 | 2.1 | 2.4 | 1.5 | 1.0 |
| Adj NII | 2.6 | 1.0 | 0.5 | 1.5 | 2.2 |
| Other Income | 1.9 | 2.0 | 1.7 | 1.6 | 1.6 |
| Total Income | 4.5 | 3.1 | 2.2 | 3.0 | 3.7 |
| Opex | 2.0 | 2.1 | 2.2 | 2.1 | 2.1 |
| PBT | 2.5 | 1.0 | 0.0 | 0.9 | 1.6 |
| TAX | 0.8 | 0.3 | -0.0 | 0.3 | 0.5 |
| RoA | 1.6 | 0.6 | 0.0 | 0.6 | 1.1 |
| Leverage | 10.2 | 10.5 | 10.8 | 11.2 | 11.6 |
| RoE | 16.8 | 6.8 | 0.5 | 6.6 | 12.2 |

Source: Note - Valuation done on closing price of 01/01/2019

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Axis Bank

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|---|----|
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| 2. Ownership of 1% or more of the stock by research analyst or Angel or associates or relatives | No |
| 3. Served as an officer, director or employee of the company covered under Research | No |
| 4. Broking relationship with company covered under Research | No |

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)