

Initiating Coverage Axis Bank Ltd

05-October-2020



Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Private Sector Bank	Rs.443.35	Buy at LTP and add further on dips to Rs.400-408 band	Rs.480	Rs.516	2 quarters

HDFC Scrip Code	AXIBAN
BSE Code	532215
NSE Code	AXISBANK
Bloomberg	AXSB
CMP Oct 01, 2020	443
Equity Capital (Rsbn)	5.62
Face Value (Rs)	2
Equity Share O/S (bn)	2.81
Market Cap (Rsbn)	1356.72
Book Value (Rs)	268
Avg. 52 Wk Volumes	24994039
52 Week High	765.9
52 Week Low	285

Share holding Pattern % (Jun, 2020)	
Promoters	15.99
Institutions	70.37
Non Institutions	13.64
Total	100.0

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Our Take:

Axis Bank's healthy capital base, fairly granular liability franchise along with improved risk practices (post CEO change in Jan 2019) places it in a relatively better position to combat the current uncertainty which has emerged post Covid. The bank has robust retail loan book composition (53% of total advances) and even on the corporate portfolio (37% of total advances as on Q1FY21 v/s 46% in Q1FY17), it has been continuously focusing on derisking the book. This has improved the quality of the book significantly. Recent Top management rejig as well as a well-articulated business plan are indicative of a DNA change. The strategic re-orientation at the bank will bode well in the longer run. The bank reported a strong Q1FY21 results and moratorium number improvement (9.1% of loans in Q1FY21 v/s 25-28% in Q4FY20) was also a positive surprise. However, for the short to medium term, we remain cautious and have a moderate growth outlook for the sector. The BB and below pool is likely to increase which coupled with the high share of loans under moratorium, would drive elevated slippages over FY21E.

Axis Bank remains well capitalised, with a strong deposit franchise and high quality customer base. Operating profit growth would remain muted in FY21E due to revenue pressures, however would be enough to absorb the elevated provisions. Axis Bank could recover well post-Covid in terms of growth parameters and return ratios.

Valuations & Recommendation:

We have estimated 9% CAGR growth in NII and 173% CAGR growth in Net Profit (due to lower base in FY20) over FY20 to FY22E. ROAA is expected to improve to 1.2% from current 0.2%; while the Loan book is estimated to rise at 12% CAGR over same time period. GNPA might rise up to 5.68% in FY21E from the recent reading of 4.7%. However it is likely to start normalizing by FY22 at 4%. Looking at current weak economic scenario we have factored in slippages of ~3.3% over FY21-22E. The pace of reduction in credit costs, improvement in earnings & return metrics could get delayed by 1.0-1.5 years owing to the COVID-19 crisis. Valuations seem inexpensive, we feel that investors can buy Axis Bank at LTP of Rs.443 (1.2x FY22E core ABV+ subsidiaries value after holding company discount) and add further on dips to Rs.400-408 band (1.1x FY22E core ABV+ subsidiaries value after holding company discount) for SOTP based Base case fair value of Rs.480 (1.35x FY22E core ABV+ subsidiaries value after holding company discount) and the Bull case fair value of Rs.516 (1.45x FY22E ABV+ subsidiaries value after holding company discount) over the next 6 months.

Financial Summary

Particulars (Rsbm)	Q1FY21	Q1FY20	YoY-%	Q4FY20	QoQ-%	FY19	FY20	FY21E	FY22E
NII	69.9	58.4	19.5%	68.1	2.6%	217.1	252.1	261.3	300.6
PPOP	58.4	58.9	-0.8%	58.5	-0.1%	190.1	234.4	245.7	279.9
PAT	11.1	13.7	-18.8%	(13.9)	-180.1%	46.8	16.3	87.9	121.9
EPS						18.2	5.8	31.1	43.2
ROAE (%)						7.2	2.1	9.8	12.2
ROAA (%)						0.63	0.19	0.93	1.18
Adj. BVPS						215	268	291	344
P/ Adj BV (x)						1.97	1.57	1.44	1.21
P/E (x)						23.4	73.2	13.5	9.6

(Source: Company, HDFC sec)

Recent Developments

The events at YES and various other Co-operative Banks have impacted depositor sentiments, causing them to become more risk-averse. This will lead to deposit polarization towards large private banks and PSBs. Axis Bank with established brand name and widespread branch network is likely to benefit in longer term. This was also evident in recent results where, deposits registered a ~17% and ~16% growth in Q4FY20 and Q1FY21 respectively with higher growth in term deposits.

Despite weak economic scenario, the bank reported strong quarterly result in Q1FY21. NII and PPOP growth were healthy at 19.5% and 15.8% respectively. PAT dipped 18.8% YoY to Rs 11.1bn. However, adjusted for the net impact of changes in accounting policy (NII reserve, fee recognition and provisions), PAT would have been Rs 16.3bn (+18.7% YoY). Sharp improvement in moratorium numbers was a positive surprise. It came in at 9.7% of loans compared to 25-28% of loans in Q4FY20. As per the management, borrowers representing 90% of the second moratorium formed part of the first moratorium, and 70-80% of the borrowers who had availed of the first one paid in June. In case of gross slippages (1.6% ann.) 21% were recognized as per the bank's credit and risk assessment criteria (technically not NPAs); 77% of corporate slippages were from the BB and below rated pool of loans. Provision Coverage Ratio (PCR) increased ~576bps QoQ to 74.8%.

Bank remains well capitalized with Tier 1 Capital of 14.4% and CAR of 17.5% as of Jun-20. This will act as a cushion against any probable uncertain eventuality of further asset quality shocks and lower CASA. In July 2020, Axis had raised Rs.100bn through QIP issuance at a price of Rs.420.

The bank has robust retail loan book composition (~81% secured; 82% salaried customers); SME (85% secured; 85% lending SME 3 and above category) ticket size less than 20Mn and even for the corporate portfolio, the bank has continued to focus on derisking the book by reducing concentration risk and pivoting the same towards better rated entities and groups. As at end of Jun-20, the proportion of loans to those rated A- and above stood at 82%, up from 79% in fiscal 2018 and almost all its incremental growth in loans came from 'AAA' and 'AA' rated clients. At the same time, the bank has also pivoted the book towards shorter tenure loans with 37% of the book being of less-than-a-year tenure.

Max-life JV: The bank announced that it has entered into a JV with Max Financial, to increase its stake in Max Life Insurance to 30% which has been recently reduced to 18%. Regulatory approval is awaited and will be the key. We have not modeled the impact of this transaction in our estimates. Valuation of stake will be dependent on the tax adj. BV of MAXL as on transaction date. If value creation fails, Axis Bank has a right to trigger put option at price of Rs 294/share.

Long term Triggers

Axis Bank has consistently focused on de-risking its loan book by reducing corporate portfolio and focusing on high margin less risky retail segment. Over the past few years Axis's loan book mix has changed tremendously, Retail book now consists of 53% of the total book vs. mere 42% in Q1FY17. Although the Bank has significantly grown its Retail loan book over the years, the book continues to remain largely secured with high proportion of existing Bank customers. The secured loans constitute 81% to the book and more than 72% of retail assets are sourced from existing customer.

Recent Top management rejig as well as a well-articulated business plan are indicative of a DNA change. The company's strategic re-orientation like increased profit consciousness, granularity on both sides of the balance Sheet and better quality corporate lending etc. are pointing that bank is headed in the right direction.

The subsidiaries of Axis Bank continue to perform well, and have scaled to a level where they are now able to complement the bank's overall strategy. As they grow bigger they might also help the bank in hedging against downturns in specific segments and access multiple growth avenues.

What could go wrong?

- Recent COVID-19 breakout is likely to have multiple order and far reaching impact on the banking sector. Credit growth is already heading southwards and given the extensive nature of the lockdown, asset quality issues are likely to spread many sectors. On-going stress in Corporate and SME segment might accelerate and in fact retail loan segment might emerge as new source of stress.
- Lower than expected loan growth and greater than expected deterioration in asset quality remains key risk to our thesis.
- Surprisingly, Axis Bank's moratorium (by value) dipped to 9.7% of loans (vs 25-28% of loans in 4QFY20). This sharp drop is encouraging. This number could however be closer to 15% (incl. overdue morat-1 customers). We think that credit cost could remain elevated at 1.93% over FY21-22E. This could also be due to expected increase in 'BB' & below book as rating downgrade cycle accelerates.
- Even after significant improvement, 18% of the corporate loan book is still BBB & below rated. A significant influx into the BB and below rated pool of corporate loans may eventually precipitate into higher slippages.
- Softer growth in CASA could increase the cost of funds and impact margins.
- Slower than expected growth of subsidiaries can impact consolidated profitability of the bank.

Company Profile:

Axis Bank is one of the first new generation private sector banks to have begun operations in 1994. The Bank was promoted in 1993, jointly by Specified Undertaking of Unit Trust of India (SUUTI) (then known as Unit Trust of India), LIC, GIC, NIC, NIA, OIC and UIL. The shareholding of Unit Trust of India was subsequently transferred to SUUTI, an entity established in 2003.

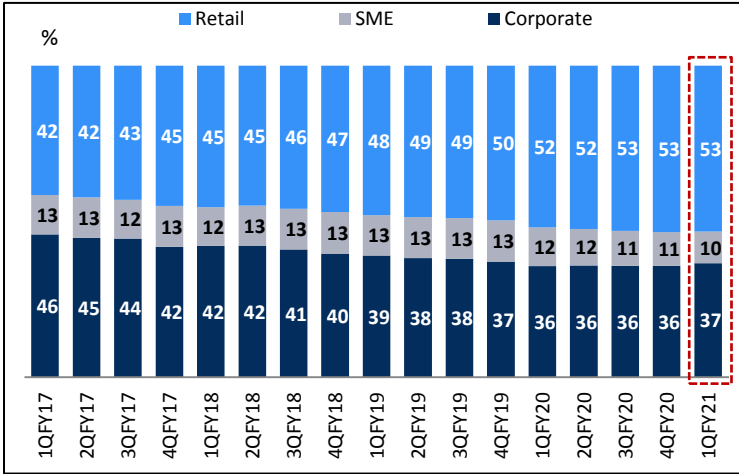
Axis Bank is the third largest private sector banks in India with a 5.5% share in loans in FY20. The bank offers the entire spectrum of financial services to customer segments like large and mid-sized corporates, MSMEs, and agriculture and retail businesses. With its 4528 domestic branches (and 2559 extension counters) and 11,971 ATMs across the country as on Jun-20, the bank's network has spread across many cities and towns, enabling it to reach out to a large cross-section of customers with an array of products and services. The bank also has ten overseas offices, with branches in Singapore, Hong Kong, Dubai (at the DIFC), Shanghai and Colombo, representative offices in Dubai, Abu Dhabi, Dhaka and Sharjah, and an overseas subsidiary in London, UK.

It has built an impressive deposit franchise over the past ten years, with a ~41% CASA ratio. Its well-diversified loan book of Rs5.7tn, as of March 2020, is spread across retail, SME, and mid and large corporates. Among subsidiaries, Axis Mutual Fund has fared well with 121% YoY growth in profits, which along with profits from other subsidiaries led 83% growth in dividends from subsidiaries.

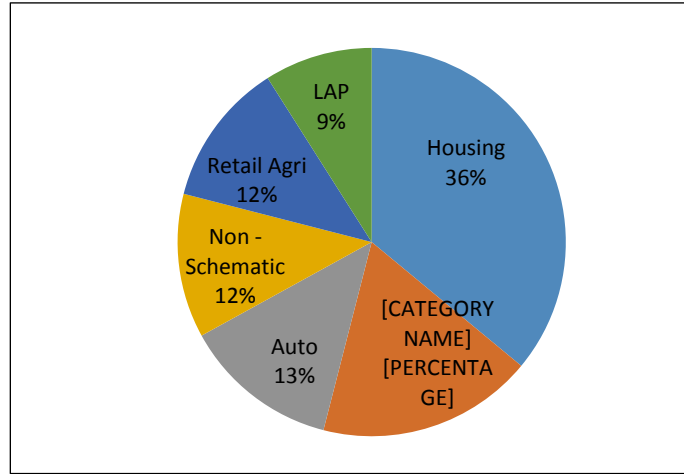
SoTP Valuation:

	Base Case	Bull Case	Rationale
Axis Bank –Standalone	456	492	1.35x / 1.45 Mar-22E ABV of Rs 338
Axis Finance (NBFC)	10	10	1.50x FY22E BV
Axis AMC (Asset Management)	13	13	20x FY22E PAT
Axis Capital (IB and Institutional Equity)	5	5	15x FY22E PAT
Axis Securities (Retail Broking and Cross-Sell)	2	2	18x FY22E PAT
Total Value of Subsidiaries (after 20% holding company discount)	24	24	
Total SOTP Value	480	516	

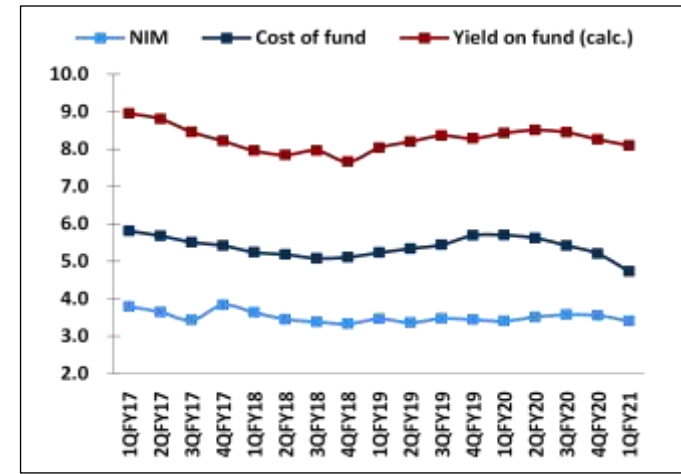
Loan Book Mix%



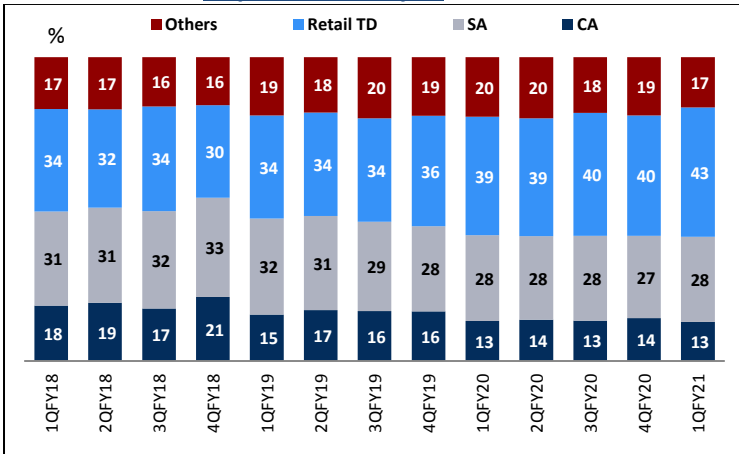
Retail Loan Book Mix%



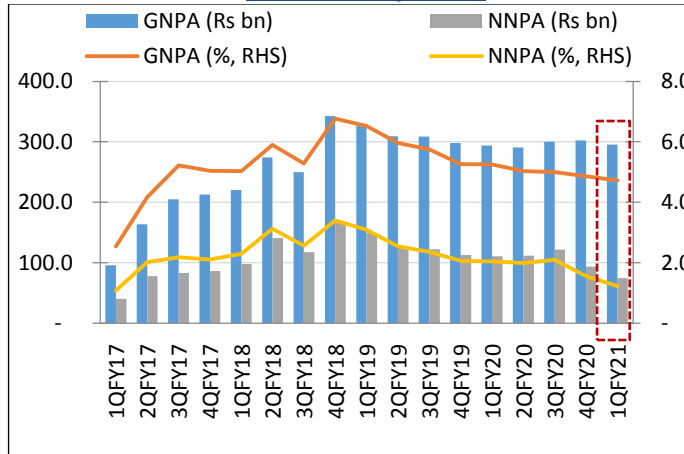
NIM%



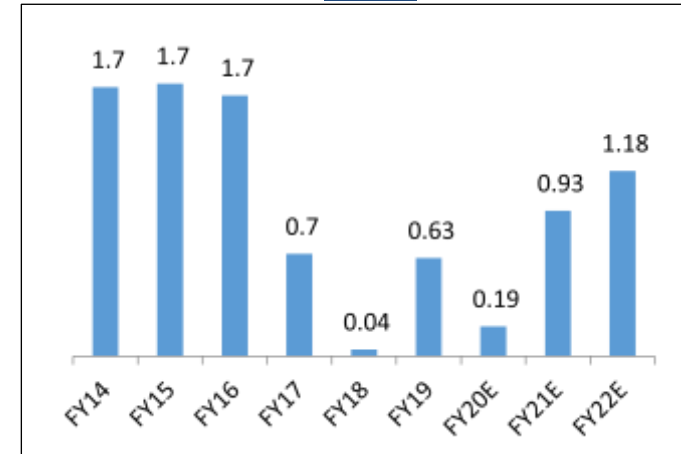
Deposit Break Up %



Asset Quality Trend



ROAA%



Financials

Income Statement (in Mn)

	FY19	FY20	FY21E	FY22E
Interest Earned	5,49,858	6,26,352	6,58,862	7,27,148
Interest Expended	3,32,776	3,74,290	3,97,542	4,26,589
Net Interest Income	2,17,082	2,52,062	2,61,320	3,00,559
Other Income	1,31,303	1,55,366	1,63,855	1,78,108
Fee Income (CEB)	88,537	96,919	93,512	1,14,848
Treasury Income	7,581	21,723	32,500	22,500
Total Income	3,48,385	4,07,428	4,25,175	4,78,667
Total Operating Exp	1,58,334	1,73,046	1,79,480	1,98,776
Employee Expense	47,473	53,210	55,500	58,908
PPOP	1,90,051	2,34,381	2,45,695	2,79,891
Provisions & Contingencies	1,20,310	1,85,339	1,28,296	1,17,010
Prov. for NPAs (incl. std prov.)	1,10,313	1,42,069	1,29,546	1,18,260
PBT	69,741	49,042	1,17,399	1,62,882
Provision for Tax	22,975	32,770	29,538	40,981
PAT	46,766	16,272	87,862	1,21,901

Balance Sheet (in Mn)

As at March	FY19	FY20	FY21E	FY22E
SOURCES OF FUNDS				
Share Capital	5,143	5,643	5,644	5,644
Reserves	6,61,620	8,43,835	9,31,697	10,47,502
Shareholder's Funds	6,66,763	8,49,478	9,37,341	10,53,146
Savings	15,41,288	17,35,916	19,26,867	21,19,554
Current	8,92,653	9,01,144	9,10,156	9,42,011
Term Deposit	30,50,772	37,63,989	41,67,631	49,14,019
Total Deposits	54,84,713	64,01,049	70,04,654	79,75,584
Borrowings	15,27,758	14,79,541	13,49,097	12,32,570
Other Liabilities & Provisions	3,30,731	4,21,579	4,84,502	5,56,989
Total Liabilities	80,09,965	91,51,648	97,75,594	108,18,290
APPLICATION OF FUNDS				
Cash & Bank Balance	6,72,046	9,72,683	6,39,311	5,00,720
Investments	17,49,693	15,67,343	19,16,871	20,80,816
G-Secs	11,68,229	12,19,181	15,41,024	16,74,873
Advances	49,47,980	57,14,242	62,34,142	71,78,026
Fixed Assets	40,366	43,129	45,285	47,550
Other Assets	5,99,880	8,54,252	9,39,984	10,11,178
Total Assets	80,09,965	91,51,648	97,75,594	108,18,290

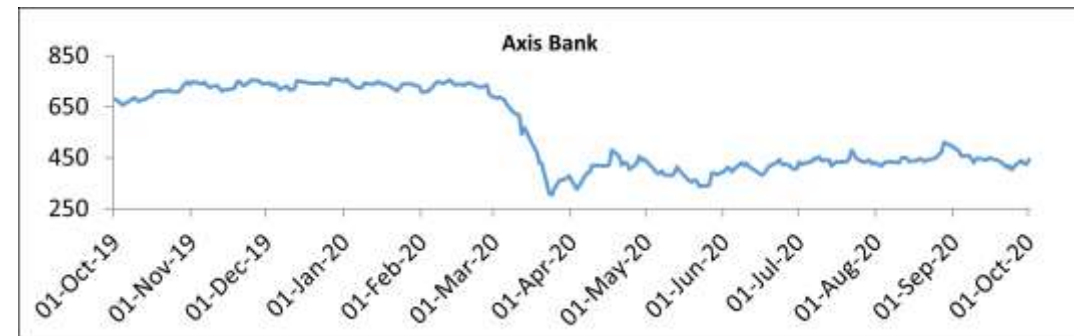
Key Ratios:

	FY19	FY20	FY21E	FY22E
VALUATION RATIOS				
EPS	18.2	5.8	31.1	43.2
Earnings Growth (%)	1,596.4	(65.2)	439.9	38.7
BVPS (ex reval.)	259.3	301.1	332.2	373.2
Adj. BVPS (ex reval. & 100% cover)	215.4	267.9	290.5	344.1
ROAA (%)	0.63	0.19	0.93	1.18
ROAE (%)	7.2	2.1	9.8	12.2
P/E (x)	23.4	73.2	13.5	9.6
P/ABV (x)	2.0	1.6	1.4	1.2
Dividend Yield (%)	0.2	-	-	0.5
PROFITABILITY				
Yield on Advances (%)	8.84	9.06	8.70	8.53
Yield on Investment (%)	6.90	6.78	6.60	6.50
Cost of Funds (%)	5.11	5.03	4.90	4.86
Cost of Deposits (%)	4.73	4.94	4.80	4.76
Core Spread (%)	3.74	4.03	3.80	3.67
NIM (%)	3.33	3.50	3.33	3.41
OPERATING EFFICIENCY				
Cost/Avg. Asset Ratio (%)	2.1	2.0	1.9	1.9
Cost-Income Ratio (Excl Treasury)	46.5	44.9	45.7	43.6

Key Ratios:

	FY19	FY20	FY21E	FY22E
BALANCE SHEET STRUCTURE RATIOS				
Loan Growth (%)	12.5	15.5	9.1	15.1
Deposit Growth (%)	20.9	16.7	9.4	13.9
C/D Ratio (%)	90.2	89.3	89.0	90.0
CASA (%)	44.4	41.2	40.5	38.4
Total Capital Adequacy Ratio (CAR)	15.8	17.5	17.5	17.5
Tier I CAR	12.5	14.5	14.6	14.8
Asset Quality				
Gross NPLs (Rsm)	2,97,954	3,02,338	3,54,001	2,87,265
Net NPLs (Rsm)	1,12,756	93,604	1,17,473	81,956
Gross NPLs (%)	5.26	4.86	5.68	4.00
Net NPLs (%)	2.06	1.56	1.88	1.14
Coverage Ratio (%)	62.2	69.0	66.8	71.5
Provision/Avg. Loans (%)	2.19	2.39	2.14	1.72

One Year Price Chart



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