ICICI Bank Ltd.

RESULT UPDATE

31st July, 2017

ICICI Bank Ltd

Asset quality still worrisome, slippages to decline

CMP	Target	Potential Upside	Market Cap (INR Mn)	Recommendation	Sector
INR 296	INR 395	34%	18,98,370	BUY	BFSI

Result highlights

ICICI Bank continued to post a weak quarter with advances growth of 3.3% yoy and PAT de-growth of 8.2% yoy along with gross NPAs expanding by 10 bps qoq to 7.99% (net NPAs at 4.86% vs. 4.89% for Q4FY17). Total interest income for the quarter came in at Rs. 134591 mn, up 1% yoy, down -0.8% qoq on back of muted advances growth and contraction in yields which declined 19 bps qoq and 40 bps yoy. Slight expansion in NIM, of 6 bps on yoy basis (helped by improved deposits mix), has helped NII expand by 8.4% on yoy (but down 6.2% qoq). Non-interest income during the quarter was Rs. 33879 mn mostly driven by fee and treasury income growth of 10.3% and 11.7% respectively. Total income was up 4.5%, flat qoq. On account of deterioration in operational metrics (cost/income up 299 bps yoy) and elevated credit costs, profitability continued to remain under pressure with PBT de-growing by 4.7% on yoy basis (up 16.3% qoq) on account of 10% de-growth in provisioning expense). PAT de-grew by 8.2% yoy and grew 1.2% qoq. On the asset quality front, fresh slippages were down to Rs. 49760 mn, which brought fresh slippage ratio down to 4.7%, a substantial improvement qoq.

MARKET DATA

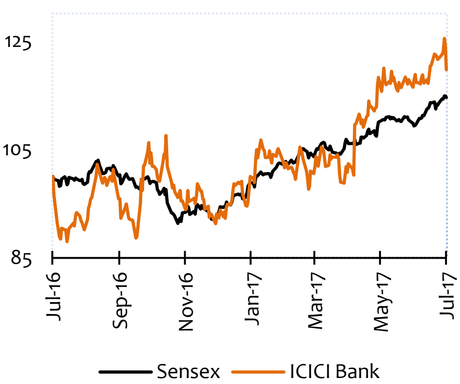
Shares outs (Mn)	6413
EquityCap (INR Mn)	12827
Mkt Cap (INR Mn)	1898370
52 Wk H/L (INR)	315/215
Volume Avg (3m K)	21473.8
Face Value (INR)	2
Bloomberg Code	ICICIBC IN

KEY FINANCIALS

Particulars (INR Mn)	FY15	FY16	FY17	FY18E	FY19E	FY20E
Net Interest Income	1,90,396	2,12,240	2,17,373	2,34,302	2,57,509	2,83,530
Pre-provision profits	1,97,199	2,38,635	2,64,867	2,87,519	3,19,124	3,53,590
Net Profit	1,11,752	97,267	98,015	1,11,047	1,24,727	1,39,234
EPS (₹)	19.3	16.7	16.8	19.1	21.4	23.9
BVPS (₹)	138.7	154.3	171.6	188.4	201.8	216.8
ABVPS (₹)	127.9	132.0	128.3	143.7	156.9	172.3
P/ABV (x)	2.3	1.6	2.0	2.1	1.9	1.7

Source: Company, KRChoksey Research

SHARE PRICE PERFORMANCE



Slippages show signs of slowing down however asset quality still worrisome

Although gross NPAs have deteriorated to 7.99% during the quarter, the slippages have come down to Rs. 49760 mn (lowest in last 7 quarters), which is down 55% qoq and 40% yoy (fresh slippage at 4.7% vs. 10.8% for Q4FY17 and 8.1% for Q1FY17). With increased provisioning cover, Net NPAs now stand at 4.86%, up 185 bps yoy and down 3 bps qoq. The decline in net NPAs, although marginal, indicates that the bank is becoming more prudent with respect to provisioning for its bad assets.

Further, the bank made recoveries of Rs. 27750 mn on account of completion of sale of cement business of one of its borrowers and the subsequent transfer of debt to a AAA-rated entity. This borrower was classified as an NPA after slipping into the non-performing category during Q4FY17. The slippages of Rs. 53780 mn during Q4FY18 accounted for 47% of the total slippages, excluding which fresh slippage would have been 5.6% for Q4FY17. Provisioning on this account has been reversed.

During Q1FY18, the bank saw slippages of Rs. 14760 mn from the restructured accounts and slippages from exposure to 'below investment grade' book was Rs. 3590 mn. Wholesale and SME segment saw slippages of Rs. 40970 mn, of which 48% were on account of slippages relating to exposure rated below investment grade, restructured portfolio and devolvement of non-fund facilities of accounts classified as NPAs in prior periods, while the balance 52% coming mostly from one account in the electronics and engineering sector.

MARKET INFO

SENSEX	32310
NIFTY	10015

With respect to the 12 accounts identified by the RBI, the bank's exposure is Rs. 68890 mn (a total of 9 accounts) plus Rs. 3510 mn in non-funded exposures. Provisioning against these exposure, of which 97% are secured, is to the extent of 41% with Rs. 6470 mn more to go over the remaining 3 quarters of FY18.

With respect to the drill-down list of the bank, there was an increase from Rs. 190390 mn in Q4FY17 to Rs. 203580 mn in Q1FY18. The increase was comprised of Rs. 2590 mn net increase in exposure, Rs. 14200 mn downgrade to below investment grade and Rs. 3590 mn of slippage to NPA.

SHARE HOLDING PATTERN (%)

Particulars	Jun 17	Mar 17	Dec 16
Promoters	0	0	0
FIIs	34.94	34.94	34.98
DIIs	30.23	30.23	30.41
Others	34.83	34.83	34.61
Total	100	100	100

10%

Advances CAGR between FY 17 and FY 20E

9%

NII CAGR between FY 17 and FY 20E

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Overall, the bank believes there was improvement in asset quality in the form of lower slippages. Further into FY18 and beyond, the bank has guided for declining slippages though lumpy slippages from outside the monitored list has not been ruled out. Therefore, we expect stress levels to remain elevated for the bank.

Advances growth muted; focus towards retail, SME and better rated corporates

The domestic advances growth for the quarter was 10.9%, with retail growing 18.6% yoy, domestic coporate de-growing by 2.8% yoy, SME growing 18.4% yoy and international portfolio de-growing 25%. We believe retail and SME portfolio growth rates have been more or less in line with the industry trend so far, however on the domestic corporate side, the bank's focus was divided between the ones classified as NPAs, restructured or under the drilldown list and the others being classified as better-rated ones. Excluding the former category of domestic corporate loans (where the focus was on collections), the bank has seen healthy growth in the portfolio (led by better rated exposures). Share of retail loans in the total portfolio has increased at the cost of other segments whose share decreased. Going forward, the bank expects to growth the retail portfolio at 18-20%, SME portfolio at 15-20%. On the corporate front, the management has guided that the growth should pick as share of better-rated corporates increases and on the international front, the bank has guided for its share in the total mix to decline as it is not a focus area.

Yields under pressure; NIMs could compress on account of changing loan portfolio characteristics

Yields on advances contracted by 41 bps yoy and 19 bps qoq. On the whole, the bank was of the view that the yields declined and will continue to move downward for FY18. The reasons cited for yield deterioration were migration from base rate to MCLR, re-pricing of existing loans and incremental lending at lower yields. Currently, of the total floating rate book that the bank has, 55% is linked to MCLR. Going forward, the yields are expected to decline as share of MCLR-linked loans increases as well as due to incremental lending to better-rated corporates. NIMs for the quarter were 3.27% (vs. 3.57% for Q4FY17 and 3.16% for Q1FY17). Some part of the NIM contraction on qoq basis was because Q4FY17 NIMs were positively impacted by interest collections from some NPAs. While domestic NIMs are expected to hold above 3% on back of reduction in deposit rates which the bank is planning, international NIMs are unlikely to change and are expected to remain at 73 bps.

CASA ratio for the bank improved to 49.0% (vs. 45.1% in Q1FY17) which supported NIMs on yoy basis to a certain extent.

Retail fee income strong and expected to continue; operational expenses to moderate

Fee income for the quarter grew by 10% to Rs. 23770 mn, mostly driven by retail fee income which in turn was driven by credit cards and forex, while corporate fee income remained subdued. On consolidated basis, fee income growth was strong at 20.6% yoy and premium income grew by 26.9% yoy. Going forward, the bank expects total fee income growth to remain at current levels with retail fee growing strongly and corporate fee growth remaining low.

Operational expenses for the quarter rose by 12.5% yoy, down 1.9% qoq. The bank added about 1300 employee during the quarter which should partly explain the rise in employee cost (which is up 17.1% yoy and 2.1% qoq). Going forward, the management has outlined enhancement of productivity and expenses moderation as some of the key objectives.

Valuation & recommendation: Q1FY18 performance was a mixed bag with earnings and asset quality deteriorating on one hand and slippages reducing on the other hand. Amongst the positives were increasing share of retail book, reduction/de-growth in slippages, clarity with respect to further bulky slippages and management's guidance on NPA reduction going forward. Although, we do not expect rapid improvement in asset quality, we do believe that the management's strategy to lend only to better rated corporates and retail focus will help the bank improve on its asset quality gradually over the years. Given this, we expect asset quality overhang to keep profitability under pressure. We also believe the bank's subsidiaries (especially the insurance ones) to create significant value. We therefore value the bank at 1.9x FY19E ABVPS and we value the subsidiaries at Rs. 97 per share, thus arriving at a SOTP value of Rs. 395 per share, which offers an upside of 34% from current levels. We maintain our rating at BUY.

Key Ratios	Q1FY18	Q1FY17	Q4FY17	Y-o-Y	Q-o-Q
Yield on avg advances (calc.)	8.5%	8.9%	8.7%	-41	-19
NIM (calc.)	3.2%	3.1%	3.4%	6	-22
Cost to income ratio	42.3%	39.3%	43.1%	299	-80
Effective tax rate	20.4%	17.3%	8.5%	309	1187
Gross NPAs	431476	275629	425515	57%	1%
Net NPAs	253062	153084	254510	65%	-1%
GNPA %	7.99%	5.28%	7.89%	271	10
NNPA %	4.86%	3.01%	4.89%	185	-3
CD ratio	95.4%	106.0%	94.7%	-1054	71
Capital adequacy ratio	17.69%	16.22%	17.39%	147	30
RoA %	1.08%	1.23%	1.05%	-15	3
Leverage (x)	7.6	7.9	7.7		
RoE %	8.1%	9.7%	8.1%	-157	4

Source: Company, KRChoksey Research

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Financials:

Income Statement (INR Mn)	Q1FY18	Q1FY17	Q4FY17	Y-o-Y	Q-o-Q
Interest income	134591	133303	135685	1.0%	-0.8%
Interest expense	78693	81717	76064	-3.7%	3.5%
Net interest income	55898	51585	59622	8.4%	-6.2%
Noninterest income	33879	34293	30172	-1.2%	12.3%
Total income	89778	85878	89794	4.5%	0.0%
- Employee costs	15112	12906	14805	17.1%	2.1%
- Other operating expenses	22833	20824	23869	9.6%	-4.3%
Operating expenses	37944	33730	38674	12.5%	-1.9%
Pre-provision profit	51833	52148	51120	-0.6%	1.4%
Provisions	26087	25145	28982	3.7%	-10.0%
Profit before tax	25746	27002	22138	-4.7%	16.3%
Tax expense	5256	4679	1892	12.3%	177.8%
Net profit	20490	22324	20246	-8.2%	1.2%

Source: Company, KRChoksey Research

Balance Sheet items	Q1FY18	Q1FY17	Q4FY17	Y-o-Y	Q-o-Q
Deposits	4862540	4240862	4900391	14.7%	-0.8%
Borrowings	1414601	1740950	1475562	-18.7%	-4.1%
Investments	1854079	1683223	1615065	10.2%	14.8%
Advances	4640752	4494265	4642321	3.3%	0.0%
Total Assets	7609156	7272225	7717915	4.6%	-1.4%

Source: Company, KRChoksey Research

Key highlights from Q1FY18 earnings call:

•SME portfolio growth was 18.4% yoy.

•Domestic corporate portfolio: The focus is on lending to better rated corporate. Excluding the corporate portfolio which is classified as NPA, restructured or comes under the drilldown list, there was growth in the domestic corporate portfolio. Bank's strategy on this front is to lend incrementally to better rated corporate. On corporate exposure classified as NPA, restructured and under drilldown list, focus was on collections.

•Overseas portfolio declined substantially during the quarter.

•Upgradation of part of the cement account was on account of transfer of part of debt to a AAA-rated entity. Provisions on this account were reversed.

•The bank is focused on growing credit cards and personal loans by banking on selling opportunities to existing customers.

•Of the total slippages, Rs. 40.97 bn was from the corporate and SME segment. 52% of this came largely from one account in the electronic and engineering sector. For this this group, only the domestic company has slipped.

•Downgrade in drilldown list was largely on account of a Supreme Court judgement with respect to a power sector account. Of the total slippages in the drilldown list, Rs. 7.5 bn was already under 5/25.

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Key highlights from Q1FY18 earnings call (contd.):

•Telecom exposure is 1.5% of the total exposure.

•Q4FY17 NIM was positively impacted on account of higher collection from some NPAs. Q1FY18 NIM has been impacted by migration of MCLR (from base rate), repricing of existing loans and lower yield on incremental lending. This trend of lower gross yield in expected to continue for the rest of the year however the bank is also looking at reducing deposit rates in order to keep NIMs above 3%.

•Of the total floating rate loan book, 55% is MCLR-linked. Share of MCLR-linked book has been increasing since past few quarters.

•Retail fee was driven by credit cards and forex. Total growth in fee income is to stay current levels with retail fee growing strongly but corporate fee growth remaining subdued.

•During the quarter, the bank added 1300 employees. Going forward, focus will be on enhancing productivity. For the rest of the year, the bank will be targeting expense moderation.

•The bank has not ruled out lumpy slippages from outside the drilldown list during the current fiscal. However, slippages should declining from now on and be significantly lower than last year.

•Going forward, the bank expects retail book growth of 18-20%, SME book growth of 15-20%. Corporate which is currently muted should also witness a pick-up in growth. Share of international portfolio in the total is likely to shrink with NIMs remaining at current levels. Within the retail book, the bank expects unsecured part to grow at a higher rate on account of a lower base. On the SME front, the bank is focusing on more granular loans with better collateral.

•On the rural portfolio, the bank hasn't witnessed much stress as of now but will be closely monitoring this segment.

•As per the bank, admitting cases to NCLT will only instill discipline to decide resolutions in a time-bound manner. It will also instill some sense of urgency amongst the banks towards resolution.

•Impact of IND-AS will be higher provisioning as it will have to be carried out on expected loss basis. Further, under IND-AS, loans will be classified as under stage 1, 2 and 3 with stage 3 comprising of accounts classified as NPAs, restructured, accounts under drilldown list and RBI-identified accounts. Stage 2 will comprise of SMA2 and some of SMA1.

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Date	CMP (INR)	TP (INR)	Recommendation
31-Jul-17	296	395	BUY
6-Feb-17	285	338	BUY
9-Nov-16	268	338	BUY
1-Aug-16	263	300	ACCUMULATE
2-May-16	230	280	ACCUMULATE
29-Jan-16	233	314	BUY
2-Nov-15	277	345	BUY
29-Apr-15	327	400	BUY
13-Apr-15	318	400	BUY
2-Feb-15	352	400	ACCUMULATE
7-Jan-15	348	403	ACCUMULATE
3-Nov-14	334	363	ACCUMULATE
8-Oct-14	286	345	BUY
1-Aug-14	295	345	BUY

Rating Legend	
Our Rating	Upside
Buy	More than 15%
Accumulate	5% - 15%
Hold	0 – 5%
Reduce	-5% – 0
Sell	Less than -5%

Analyst Certification

We, Raghav Garg (B.Com, M.Com (Applied Finance)), research analyst and Amit Singh (B.E (Com), MMS-Finance), research associate, author and the name subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect my views about the subject issuer(s) or securities. I also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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