KRChoksey INSTITUTIONAL

IndusInd Bank Ltd.

RESULT UPDATE

13th October, 2017

IndusInd Bank Ltd.

Another stellar quarter

CMP	Target	Potential Upside	Market Cap (INR Mn)	Recommendation	Sector
INR 1747	**INR 1889**	**8.1%**	**10,43,770**	**ACCUMULATE**	**BFSI**

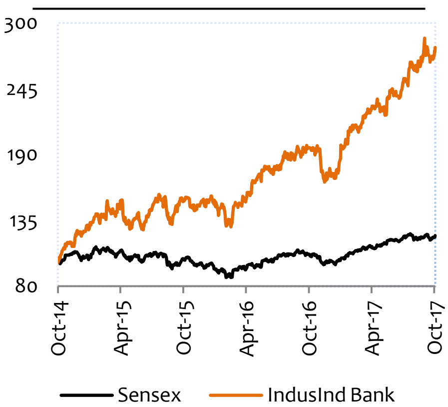
Result highlights

- Advances have grown at 24.5% yoy. On back of stable NIMs of 4%, NII has grown by 24.7%. With a strong other income growth of 23.8%, total income has grown by 23.8% to Rs. 30,086 mn.
- On the operational expenses front, employee costs have grown by 18.4% yoy while other expenses have grown by 20.3%, resulting in an overall opex growth of 19.7%. With a 157 bps improvement in C/I ratio (at 45.7% vs. 47.3% for Q2FY17), operating profit has grown by 27.5%. The improvement in opex is in-line with the management strategy.
- Provisioning expense has grown by 37% yoy, resulting in annualized credit costs of 0.7%. Credit costs remain unchanged due to stable asset quality. Gross NPA have reduced by 1 bps qoq to 1.08% while net NPA remains unchanged at 0.44%.
- As a result of robust advances growth, stable NIMs, improved C/I, stable asset quality and low credit costs, the bank has delivered an ROE of 16% (vs. 14.7% for Q2FY17 and 15.6% for Q1FY18).

MARKET DATA

Shares outs (Mn)	599
EquityCap (INR Mn)	5990
Mkt Cap (INR Mn)	1043770
52 Wk H/L (INR)	1818/1038
Volume Avg (3m K)	1122.9
Face Value (INR)	10
Bloomberg Code	IIB IN

SHARE PRICE PERFORMANCE



MARKET INFO

SENSEX	32182
NIFTY	10096

KEY FINANCIALS

Particulars (INR Mn)	FY15	FY16	FY17	FY18E	FY19E	FY20E
Net Interest Income	34,202.8	45,165.7	60,626.0	73,648.9	87,243.2	1,06,436.7
Pre-provision profits	30,982.2	41,414.2	54,510.2	67,022.7	81,129.8	99,890.4
Net Profit	17,937.2	22,864.5	28,678.9	36,670.8	45,325.2	56,509.8
EPS (₹)	33.9	38.4	47.9	61.3	75.8	94.5
BVPS (₹)	200.8	297.2	344.9	397.0	461.3	541.5
ABVPS (₹)	196.8	291.8	337.6	388.8	452.2	532.0
P/E (x)	25.7	28.9	30.9	28.5	23.1	18.5
P/ABV (x)	4.4	3.8	4.4	4.5	3.9	3.3

Source: Company, KRChoksey Research

Advances growth momentum continues on back of market-share gains

IndusInd Bank (IIB) has delivered a stellar advances growth of 24.5% during the quarter despite country economics not being very supportive (sluggish private capex, low credit demand, slowing GDP growth). The management attributes such strong growth to business being taken over from other financial institutions including PSU banks which are facing several constraints.

While the corporate segment has grown at 26% yoy, consumer finance division has seen 22% growth. Though corporate segment continues to maintain its growth momentum (27% average growth for last 6 quarters), consumer finance segment growth has slowed down over the same period with average growth rate being 25%. As a result of such strong growth, corporate segment now forms 59.8% of the total book (vs. 59% for Q2FY17). Nonetheless, we do expect a combined over growth of at least 22% over FY17-20 driven mainly by opportunities thrown up by the PSU banks and market share gains.

Within the corporate segment, the bank's growth has been strongest in the large corporate segment which grew by 31% yoy and forms 49% of the corporate book. Mid-size and small corporate segments grew by 22% each. On the retail side, the bank saw 15% growth in CV loans partially driven by "reinventorization" post receding adverse impact of GST (CV sales up 25% yoy during September). UVs grew by 17%, equipment financing by 28%, car loans by 17%, 2w by 5% and tractors by 56%.

SHARE HOLDING PATTERN (%)

Particulars	Jun 17	Mar 17	Dec 16
Promoters	14.97	14.98	14.99
FIIs	43.1	43.34	43.14
DIIs	12.68	12.31	12.45
Others	29.26	29.37	29.43
Total	100	100	100

22%

Advances CAGR between FY 17 and FY 19E

21%

NII CAGR between FY 17 and FY 19E

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IndusInd Bank Ltd.

Stable NIMs on back of strong CASA traction and competitive pricing

NIMs for the quarter remained steady at 4%. Although our calculated NIMs show slight deterioration, we feel it is insignificant given the advances growth delivered by the bank. Yields on corporate financing came down by 38 bps qoq while yield contraction on consumer financing was 12 bps qoq. However, these contractions have been negated to a large extent by strong CASA traction (42% versus 38% for Q1FY18 and 37% for Q2FY17) which has helped bring down overall cost of funds by 39 bps qoq and 50 bps yoy. Such developments reinforce our confidence in the management's strategy of achieving 4% NIMs by working towards reducing cost of funds through building a strong CASA base and on a broader note, a stable funding base.

CASA growth during the quarter was 46% yoy and 18% qoq. Within CASA, CA de-grew by 4% while SA nearly doubled by growing 95%. The management attributes such strong CASA performance to its branches becoming more mature. 75% of the total branches now more than 2 years old and have matured significantly enough. As these branches grow older and become more mature CASA traction in these branches is expected to increase. Besides increased customer acquisitions, the bank has also seen an increase in average ticket sizes. Government business has also been instrumental in growing CASA strongly.

Strong fee income supported total income growth and contributed to profitability

Core fee income during the quarter grew by ~23% while overall non-interest income grew by 22%. With fee and forex income forming 85.3% (versus 83.4% for Q1FY18 and 85.1% for Q2FY17) of the total, we are of the view that the bank's quality of other/non-interest income also improved. Most of the fee income growth came on account of strong advances growth, wherein fees on renewals and new loans contributed significantly. Going forward, over FY18-20, we estimate non-interest income to grow by 22%.

Robust asset quality profile without any NCLT overhang

Gross NPAs in percentage terms have shown a 1 bp improvement, moving to 1.08% against 1.09% as of Q1FY18. With PCR remaining more or less the same at 60%, net NPAs remained unchanged too at 0.44%. Given the currently prevailing stress in the banking sector, IIB's asset quality stands out. What is even more noteworthy is that the bank has not suffered any asset quality deterioration. Overall slippages during the quarter have come down to 1.7% and have declined sequentially since Q4FY16 when they peaked at 2.5%. As a result of robust asset quality and declining slippages, credit costs have come down as well and stood at 65 bps versus 71 bps for Q1FY18.

Segment-wise, corporate asset quality saw some deterioration sequentially where GNPAs have increased by ~10 bps to 1.1% however the pace of addition of new stress has reduced significantly as indicated by a declining slippage of 1.7% versus 2.1% during Q1FY18. We expect slippages on the corporate book to come down further as the bank increases its exposure towards better rated corporates. Within the consumer finance division, asset quality improved immensely with GNPAs reducing by 20 bps to 1.1% with pace of slippages reducing to 1.8% versus 2.3% witnessed during Q1FY18. The improvement in retail book's asset quality was broad-based and was across all the sub-segments. Most notable improvement in the retail book was in CV, UV and construction equipment.

With respect to NCLT exposure, out of the total number of accounts identified by the RBI so far, the bank has exposure to 8 accounts. Of these 8 accounts, one is under restructuring, another one is negligible in terms of size and the remaining 6 make up about Rs. 385 crore (0.3% of advances) on which the bank maintains a PCR of 65%. Going forward, we expect asset quality to improve further over FY18-20 on account of tight underwriting skills and declining slippages.

Valuation & Recommendation:

IndusInd Bank has delivered yet another quarter of superior performance with a strong advances, deposits and CASA growth, implying strong market-share gains. The bank is targeting a loan book growth of 25-30% annually over Planning Cycle 4 and we believe the bank should be able to deliver on its guidance and outperform the industry by a wide margin. The bank's strategy on garnering CASA deposits is also paying off as indicated by strong Q2FY18 performance where in CASA has touched 42%, growing 46% yoy. With strong CASA traction, the bank will be able to lower its cost of funds. Although this is likely to provide room for NIM expansion, the bank's strategy is to cap NIMs at 4% and therefore maintain NIMs at healthy levels. An outcome of this strategy will be lower yields for borrowers which will help bank acquire customers/borrowers. Along with a strong growth in advances, we expect non-interest income to grow at a similar pace as well thereby contributing significantly to the bank's profitability. Further improvement in operational costs (targeting 200 bps reduction in C/I by FY20) and reduction in credit costs by way of better quality lending is expected to drive RoA/RoE towards 1.9%/19% by FY20. **At current price of Rs. 1,747, IIB is trading at 3.3x FY20E adjusted book value. Given the outlook for the bank, we revise our target price upwards and value the bank at 3.5x P/ABV FY20E and arrive at a target price of Rs. 1,889 per share offering a potential upside of 8.1%. Hence, we recommend to ACCUMULATE the stock.**

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IndusInd Bank Ltd.

Particulars (INR Mn)					
Income Statement	**Q2FY18**	**Q2FY17**	**Q1FY18**	**Y-o-Y**	**Q-o-Q**
Interest income	42,084	34,857	41,355	20.7%	1.8%
Interest expense	23,874	20,254	23,615	17.9%	1.1%
Net interest income	**18,210**	**14,603**	**17,741**	**24.7%**	**2.6%**
Noninterest income	11,876	9,704	11,673	22.4%	1.7%
Total income	**30,086**	**24,307**	**29,413**	**23.8%**	**2.3%**
- Employee costs	4,450	3,758	4,222	18.4%	5.4%
- Other operating expenses	9,300	7,733	9,306	20.3%	-0.1%
Operating expenses	13,751	11,491	13,528	19.7%	1.6%
Pre-provision profit	**16,335**	**12,817**	**15,885**	**27.5%**	**2.8%**
Provisions	2,938	2,139	3,100	37.3%	-5.2%
Profit before tax	**13,398**	**10,678**	**12,786**	**25.5%**	**4.8%**
Tax expense	4,597	3,635	4,420	26.4%	4.0%
Net profit	**8,801**	**7,043**	**8,365**	**25.0%**	**5.2%**

Source: Company, KRChoksey Research

Balance Sheet items	Q2FY18	Q2FY17	Q1FY18	Y-o-Y	Q-o-Q
Deposits	14,14,406	11,23,133	13,36,730	25.9%	5.8%
CASA deposits	5,97,750	4,10,340	5,05,010	45.7%	18.4%
CASA (%)	42.3%	36.5%	37.8%	5.73	4.48
Borrowings	2,35,577	1,90,783	2,74,040	23.5%	-14.0%
Investments	4,21,459	3,65,491	4,21,470	15.3%	0.0%
Advances	12,31,808	9,89,491	11,64,070	24.5%	5.8%
Total Assets	19,50,317	15,78,376	19,06,500	23.6%	2.3%
Capital adequacy ratio (%)	15.63%	15.32%	16.18%	0.31	-0.55
Spread Analysis	**Q2FY18**	**Q2FY17**	**Q1FY18**	**Y-o-Y**	**Q-o-Q**
Yield on avg advances (%)	10.7%	11.4%	11.2%	-0.70	-0.55
Yield on avg interest earning assets (%)	9.2%	9.5%	9.3%	-0.34	-0.09
Cost of funds (%)	5.8%	6.2%	5.9%	-0.38	-0.08
NIM (%)	4.0%	4.0%	4.0%	-0.02	0.00
Asset quality	**Q2FY18**	**Q2FY17**	**Q1FY18**	**Y-o-Y**	**Q-o-Q**
Gross NPA	13,453	8,990	12,717	49.6%	5.8%
Net NPA	5,369	3,692	5,083	45.4%	5.6%
GNPA (%)	1.08%	0.90%	1.09%	0.18	-0.01
NNPA (%)	0.44%	0.37%	0.44%	0.07	0.00
Provision coverage (%)	60%	59%	60%	1.15	0.06
Key ratios	**Q2FY18**	**Q2FY17**	**Q1FY18**	**Y-o-Y**	**Q-o-Q**
Cost to income ratio (%)	45.7%	47.3%	46.0%	-1.57	-0.29
Credit cost (%)	0.7%	0.6%	0.8%	0.08	-0.07
C/D ratio (%)	87%	88%	87%	-1.01	0.01
RoA (%)	1.8%	1.8%	1.8%	0.02	0.05
Leverage (x)	8.9	8.3	8.9		
RoE (%)	16.0%	14.7%	15.6%	1.28	0.46

Source: Company, KRChoksey Research

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IndusInd Bank Ltd.

Key highlights from Q2FY18 earnings call:

- September CV sales were up 25% yoy partially due to "reinventorization". This partially drove CV financing demand.
- With respect to NCLT cases, the bank is in a very comfortable provisioning considering other corporate heavy banks are witnessing heavy adverse impact on their profitability due to provisioning related to NCLT cases. Bank's total exposure is to 6 accounts worth Rs. 385 crore. The bank maintains a PCR of 65% on this. In terms of further deterioration, the bank has ruled out any surprises from the NCLT cases as all of the stress from this section has played out.
- With respect to CASA traction and the bank's strategy to lower CoF, the bank is slowly/steadily building a stable funding base to reduce dependence on bulk deposits.
- Loan processing fee was strong during the quarter, helping fee income grow. Fee income was mostly a function of loan renewals and new loans.
- The bank reiterated that it wants to pursue MFI growth – whether organic or inorganic. The bank is also of the view that the micro-finance industry is slowly showing signs of resurgence and that the micro-finance slippages have playerdout.
- On the proposed Bharat Financial merger, the bank has cited various advantages that would be available to the combined entity. Cost of funds for the micro-financier will fall from day one which is a big positive. The risk weight on micro-finance loan will fall to 75% when the portfolio comes under the bank as opposed to 100% under a MF institution, which will result in unlocking of capital. Lastly, micro-finance loans are 100% PSL compliant.
- Liability play is another angle and is one of the biggest advantages for a micro finance institution to get merged with a bank.
- Corporate growth is coming on account of taking away business from other financial institutions. Private capex though is still very sluggish except for a few sectors such as renewable (about Rs. 1000 crore exposure for IIB) and power transmission (exposure is less than 1% of the total book).
- The bank is evaluating reducing savings deposits rates. Despite past reductions in the savings rate, the bank has not seen any significant reduction in client acquisition.
- The bank has not seen any material changes in its watch list and has seen exposure in mid corporate moving towards better rated entities.
- **Reasons for increase in CASA:**
  - 75% of the branches are now older than 2 years. The bank attributes increase in CASA to these branches which have sort of matured. As they grow older, CASA traction will improve further.
  - The bank has also seen increase in average ticket sizes and increased acquisitions in these older branches and as a result CASA has performed exceptionally well.
  - The bank is also getting good government business.
- The bank also feels it is quite competitive in terms of pricing loans and also enjoys one of the lowest interest rate risk in the industry.
- Total SRs on the book is Rs. 407 crore (net value).

IndusInd Bank Ltd.

Particulars (INR Mn)						
Income Statement	**FY2015**	**FY2016**	**FY2017**	**FY2018E**	**FY2019E**	**FY2020E**
Interest income	96,920	1,18,717	1,44,057	1,78,699	2,17,084	2,64,843
Interest expense	62,717	73,552	83,431	1,05,050	1,29,841	1,58,406
Net interest income	**34,203**	**45,166**	**60,626**	**73,649**	**87,243**	**1,06,437**
Non interest income	24,039	32,969	41,715	51,014	62,268	75,967
Total income	58,241	78,135	1,02,341	1,24,662	1,49,511	1,82,404
Operating expenses	27,259	36,721	47,831	57,640	68,381	82,513
Employee costs	9,805	12,361	15,210	17,492	20,116	23,133
Other operating expenses	17,455	24,360	32,621	40,148	48,266	59,381
Pre-provision profit	30,982	41,414	54,510	67,023	81,130	99,890
Provisions	3,891	6,722	10,913	11,277	12,228	13,986
Profit before tax	27,092	34,693	43,597	55,746	68,902	85,904
Tax expense	9,155	11,828	14,918	19,075	23,577	29,395
Net profit	**17,937**	**22,864**	**28,679**	**36,671**	**45,325**	**56,510**

Source: Company, KRChoksey Research

Balance sheet	FY2015	FY2016	FY2017	FY2018E	FY2019E	FY2020E
SOURCES OF FUNDS						
Share capital	5,295	5,950	5,981	5,981	5,981	5,981
Reserves & surplus	1,01,151	1,71,010	2,00,480	2,31,611	2,70,089	3,18,062
Shareholders' funds	1,06,445	1,76,960	2,06,461	2,37,592	2,76,070	3,24,044
Borrowings	2,06,181	2,49,959	2,24,537	2,80,783	3,42,556	4,17,918
Deposits	7,41,344	9,30,003	12,65,722	15,91,106	19,41,149	23,68,202
Other liabilities & provisions	37,190	72,048	89,764	80,332	1,11,797	1,49,155
TOTAL LIABILITIES & EQUITY	**10,91,159**	**14,28,970**	**17,86,484**	**21,89,813**	**26,71,572**	**32,59,318**
USES OF FUNDS						
Cash and cash equivalent	1,07,791	1,01,119	1,86,283	1,64,726	2,00,966	2,45,179
Investments	2,48,594	3,40,543	3,67,021	5,14,769	6,28,019	7,66,183
Advances	6,87,882	8,84,193	11,30,805	13,79,582	16,83,090	20,53,370
Fixed assets	11,576	12,553	13,352	16,690	18,916	22,254
Other assets	35,316	90,561	89,023	1,14,045	1,40,581	1,72,332
TOTAL ASSETS	**10,91,159**	**14,28,970**	**17,86,484**	**21,89,813**	**26,71,572**	**32,59,318**

Source: Company, KRChoksey Research

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Key ratios	FY2015	FY2016	FY2017	FY2018E	FY2019E	FY2020E
Growth rates						
Advances (%)	24.8%	28.5%	27.9%	22.0%	22.0%	22.0%
Deposits (%)	22.5%	25.4%	36.1%	25.7%	22.0%	22.0%
Total assets (%)	25.4%	31.0%	25.0%	22.6%	22.0%	22.0%
NII (%)	18.3%	32.1%	34.2%	21.5%	18.5%	22.0%
Pre-provisioning profit (%)	19.3%	33.7%	31.6%	23.0%	21.0%	23.1%
PAT (%)	27.4%	27.5%	25.4%	27.9%	23.6%	24.7%
Balance sheet ratios						
Credit/Deposit (%)	92.8%	95.1%	89.3%	86.7%	86.7%	86.7%
CASA (%)	34.1%	35.2%	36.9%	38.0%	38.5%	39.0%
Advances/Total assets (%)	63.0%	61.9%	63.3%	63.0%	63.0%	63.0%
Leverage (x)	10.3	8.1	8.7	9.2	9.7	10.1
Operating efficiency						
Cost/income (%)	46.8%	47.0%	46.7%	46.2%	45.7%	45.2%
Opex/total assets (%)	2.8%	2.9%	3.0%	2.9%	2.8%	2.8%
Opex/total interest earning assets (%)	2.9%	3.1%	3.2%	3.1%	3.0%	3.0%
Profitability						
NIM (%)	3.6%	3.8%	4.0%	4.0%	3.8%	3.8%
RoA (%)	1.8%	1.8%	1.8%	1.8%	1.9%	1.9%
RoE (%)	18.8%	14.7%	15.4%	17.0%	18.1%	19.2%
Asset quality						
Gross NPA (%)	0.8%	0.9%	0.9%	0.9%	0.9%	0.9%
Net NPA (%)	0.3%	0.4%	0.4%	0.4%	0.3%	0.3%
PCR (%)	63%	59%	58%	62%	65%	70%
Slippage (%)	-0.1%	0.3%	0.3%	0.2%	0.2%	0.2%
Credit cost (%)	0.5%	0.6%	0.7%	0.6%	0.5%	0.4%
Per share data / Valuation						
EPS (Rs.)	33.9	38.4	47.9	61.3	75.8	94.5
BV (Rs.)	200.8	297.2	344.9	397.0	461.3	541.5
ABV (Rs.)	196.8	291.8	337.6	388.8	452.2	532.0
P/E (x)	25.7	28.9	30.9	28.5	23.1	18.5
P/BV (x)	4.3	3.7	4.3	4.4	3.8	3.2
P/ABV (x)	4.4	3.8	4.4	4.5	3.9	3.3

Source: Company, KRChoksey Research

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IndusInd Bank Ltd.

Indusind Bank Ltd.			
Date	CMP (INR)	TP (INR)	Recommendation
13-Oct-17	1747	1889	ACCUMULATE
12-July-17	1500	1681	ACCUMULATE
11-Jan-17	1,222	1,500	BUY
14-Oct-16	1,213	1,500	BUY
12-Jul-16	1,143	1,352	BUY
13-Jan-16	920	1,203	BUY
01-July-15	940	1,203	BUY
08-July-15	898	1,011	ACCUMULATE
18-Apr-15	876	1,011	BUY
13-Apr-15	945	955	HOLD
14-Jan-15	825	927	ACCUMULATE
07-Jan-15	798	850	ACCUMULATE
14-Oct-14	635	715	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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