

IndusInd Bank | BUY

Operationally strong ; IL & FS exposure leads to PAT miss

IndusInd Bank reported an operationally strong quarter in 2QFY19, with operating profit up 22% YoY (in-line with JMFe). However, IIB's PAT missed our estimates by 15%, largely driven by elevated provisions on account of exposures to the IL & FS group (currently classified as standard). IIB made contingency provisions of INR 2.75 bn against the account (14% of PPOP), resulting in flattish PAT in 2QFY19 (+4.6% YoY). The exposure to the group, although not quantified by management, is on 2 counts a) At the SPV level to a completed and currently tolling tunnel project (AAA rated recently) and b) At the holdco level, where IIB has first right to any liquidity support to holdco/ rights issue etc. The IL & FS exposure, which could be between 0.6-1% of loans (in our view), remains a key monitorable for IIB going forward. Operationally, loan growth was strong (+32% YoY) while margins contracted 8bps QoQ to 3.84% in 2QFY19. The NIM softness could be temporary in our view, as MCLR-based loans get re-priced for IIB. We cut our PAT estimates (for IIB + BFIL merged entity) by 2% for FY19E and reduce our TP by 2% to INR 2,075. Maintain BUY.

- **NIM softness appears temporary:** With the recent MCLR hikes starting to catch up, the yield on advances inched up 29bps QoQ to 11.44%. However, the increase in the overall blended yield on assets was moderate at 12bps QoQ when compared to the overall increase in cost of funds (20bps QoQ). As a result, NIMs softened by 8bps QoQ to 3.84%. However, given that the full impact of the MCLR hikes will be seen over the next few quarters, we expect the NIMs to bounce back and remain on a healthy trajectory. This should be further supported by high yielding assets from the BHAFIN portfolio.
- **Growth remains strong and all round:** Loan growth continued to remain robust in 2Q19 (+32% YoY), with both corporate (+35% YoY) and consumer finance (+29% YoY) witnessing strong growth. Growth within retail loans was secular, apart from the LAP portfolio, where management cited pricing pressures. IIB added 1mn customers in 2QFY19 – total customer base now stands at c.13mn, well on track to achieve its PC4 objective of 20mn customers by FY20. Momentum on the CASA front remained strong and it now stands at 44% of deposits. IIB's Real estate exposure has picked up in the recent past (+62bps QoQ) to 4.1% and management has guided for reduction in these exposures through sell-downs.
- **Elevated provision on account of exposure to IL & FS :** IIB made elevated provisions (INR 2.75bn) on account of exposures to the IL & FS group (currently classified as standard). The exposure to the group, although not quantified by management, is on 2 counts a) At the SPV level to a completed and currently tolling tunnel project (AAA rated recently) and b) At the holdco level, where IIB has first right to any liquidity support to holdco/ rights issue etc. Adjusting for these one-off elevated provisions, credit cost for IIB was largely stable in 2QFY19: specific credit cost was at 56bps, while GNPLs declined 6bps QoQ to 1.09%.



Sameer Bhise

sameer.bhise@jmfl.com | Tel: (91 22) 66303489

S Parameswaran

S.Parameswaran@jmfl.com | Tel: (91 22) 66303075

Akshay Jain

akshay.jain@jmfl.com | Tel: (91 22) 66303099

Karan Singh CFA FRM

karan.uberoi@jmfl.com | Tel: (91 22) 66303082

Nikhil Walecha

nikhil.walecha@jmfl.com | Tel: (91 22) 66303027

Bunny Babjee

bunny.babjee@jmfl.com | Tel: (91 22) 66303263

Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	2,075
Upside/(Downside)	27.5%
Previous Price Target	2,120
Change	-2.2%

Key Data – IIB IN

Current Market Price	INR1,627
Market cap (bn)	INR978.3/US\$13.3
Free Float	78%
Shares in issue (mn)	598.1
Diluted share (mn)	
3-mon avg daily val (mn)	INR2,891.4/US\$39.2
52-week range	2,038/1,551
Sensex/Nifty	34,865/10,513
INR/US\$	73.8

Price Performance

%	1M	6M	12M
Absolute	-13.1	-12.6	-7.1
Relative*	-5.1	-14.3	-13.5

* To the BSE Sensex

Financial Summary	(INR mn)				
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Net Profit	22,864	28,679	36,090	55,088	75,787
Net Profit (YoY) (%)	27.5%	25.4%	25.7%	35.6%	37.6%
Assets (YoY) (%)	25.4%	27.6%	24.1%	29.3%	25.8%
ROA (%)	1.8%	1.8%	1.8%	2.0%	2.2%
ROE (%)	16.6%	15.3%	19.5%	18.0%	20.9%
EPS	38.4	47.9	60.1	78.7	108.2
EPS (YoY) (%)	13.4%	24.8%	25.3%	35.6%	37.6%
PE (x)	42.3	33.9	27.1	20.7	15.0
BV	291	339	391	471.2	562.6
BV (YoY) (%)	50.4%	16.5%	15.4%	16.5%	19.4%
P/BV (x)	5.60	4.80	4.16	3.45	2.89

Source: Company data, JM Financial. Note: Valuations as of 15/Oct/2018

JM Financial Research is also available on:
Bloomberg - JMFR <GO>,
Thomson Publisher & Reuters
S&P Capital IQ and FactSet

Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

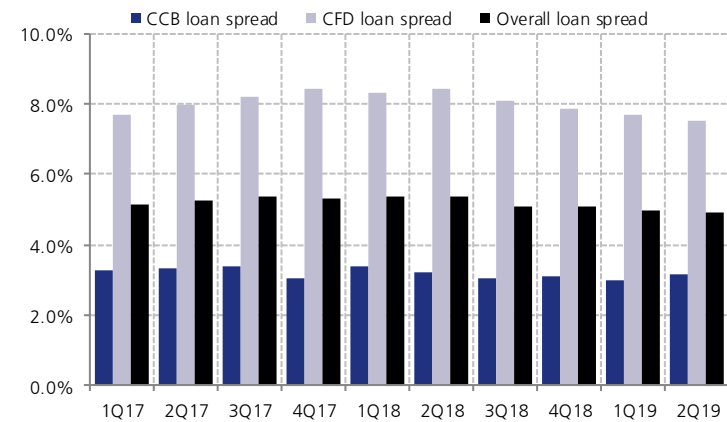
Key Quarterly trends

Exhibit 1. IIB : 2Q19 – Results summary (INR mn)

Earnings Table (Rs mn)	2Q18	1Q19	2Q19	YoY (%)	QoQ (%)
NII	18,210	21,224	22,033	21.0%	3.8%
Fee based Income	8,300	9,370	9,950	19.9%	6.2%
Exchange Profits	1,830	2,280	2,230	21.9%	-2.2%
Trading Profits	1,750	1,370	990	-43.4%	-27.7%
Misc Income	-4	-4	3	-165.1%	-170.0%
Non-Interest income	11,876	13,016	13,173	10.9%	1.2%
Total Income	30,086	34,240	35,206	17.0%	2.8%
Employee Cost	4,450	4,620	4,582	3.0%	-0.8%
Other Operating Expenses	9,300	10,509	10,699	15.0%	1.8%
Total Operating Expenses	13,751	15,129	15,281	11.1%	1.0%
Operating Profit	16,335	19,111	19,924	22.0%	4.3%
Loan Loss Provisions	2,220	2,090	2,000	-9.9%	-4.3%
Total Provisions	2,938	3,500	5,903	100.9%	68.6%
PBT	13,398	15,611	14,022	4.7%	-10.2%
Tax	4,597	5,254	4,819	4.8%	-8.3%
Reported Profit	8,801	10,357	9,203	4.6%	-11.1%
Balance sheet (Rs bn)					
Deposits	1,414.4	1,588.6	1,682.2	18.9%	5.9%
Net Advances	1,231.8	1,506.8	1,631.4	32.4%	8.3%
Total Assets	1,950.3	2,288.8	2,483.2	27.3%	8.5%
Low-cost Deposits (%)	42.0%	43.4%	42.6%	0.6%	-0.8%
Loan-Deposit ratio (%)	87.1%	94.8%	97.0%	9.9%	2.1%
Key Ratios					
Credit Quality					
Gross NPAs (Rs. mn.)	13,453	17,406	17,814	32.4%	2.3%
Net NPAs (Rs. mn.)	5,369	7,624	7,876	46.7%	3.3%
Gross NPA (%)	1.08%	1.15%	1.09%	0.00%	-0.06%
Net NPA (%)	0.44%	0.51%	0.48%	0.05%	-0.02%
Loan Loss Provisions (%)	0.80%	0.63%	0.56%	-0.24%	-0.07%
Coverage Ratio (%)	60.1%	56.2%	55.8%	-4.3%	-0.4%
Capital Adequacy					
Tier I (%)	15.09%	14.29%	13.86%	-1.23%	-0.43%
CAR (%)	15.63%	14.70%	14.28%	-1.35%	-0.42%
Du-pont Analysis					
NII / Assets (%)	3.78%	3.77%	3.69%	-0.08%	-0.08%
Non-Interest Inc. / Assets (%)	2.46%	2.31%	2.21%	-0.25%	-0.10%
Operating Cost / Assets (%)	2.85%	2.69%	2.56%	-0.29%	-0.12%
Operating Profits / Assets (%)	3.39%	3.39%	3.34%	-0.05%	-0.05%
Provisions / Assets (%)	0.61%	0.62%	0.99%	0.38%	0.37%
ROA (%)	1.83%	1.84%	1.54%	-0.28%	-0.30%

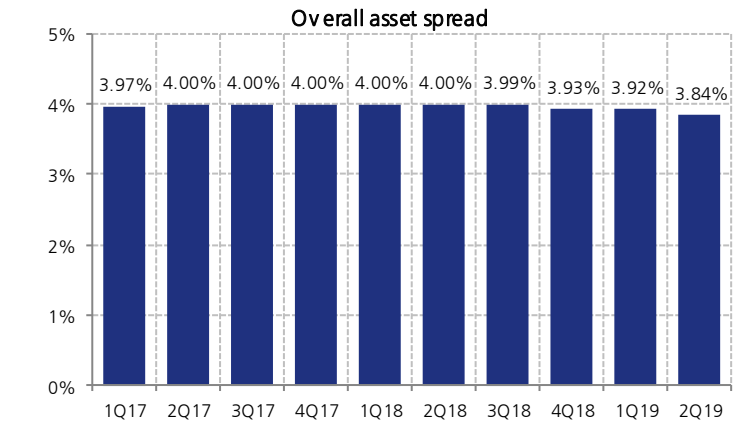
Source: Company, JM Financial

Exhibit 2. IndusInd Bank: Loan book spreads



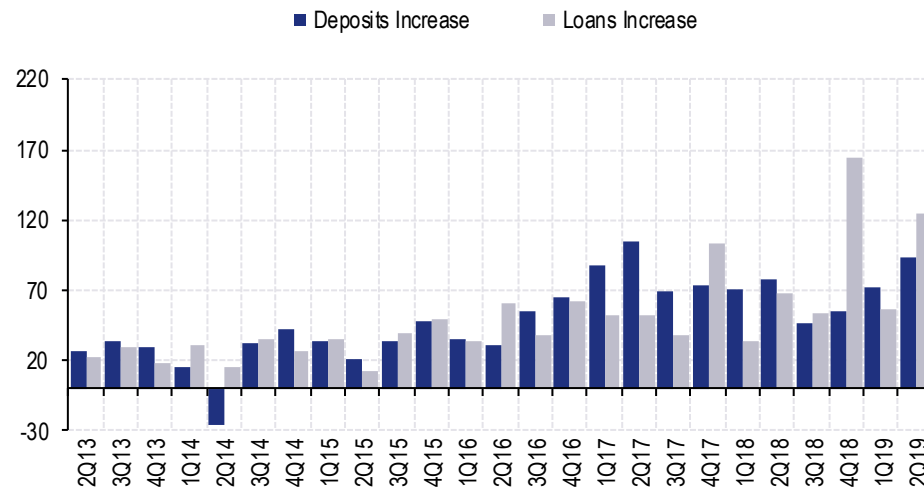
Source: Company, JM Financial

Exhibit 3. IndusInd Bank: Overall asset spread contracted marginally



Source: Company, JM Financial

Exhibit 4. IIB : Balance sheet growth momentum continues



Source: Company, JM Financial

Exhibit 5. IndusInd Bank: Risk weighted assets composition

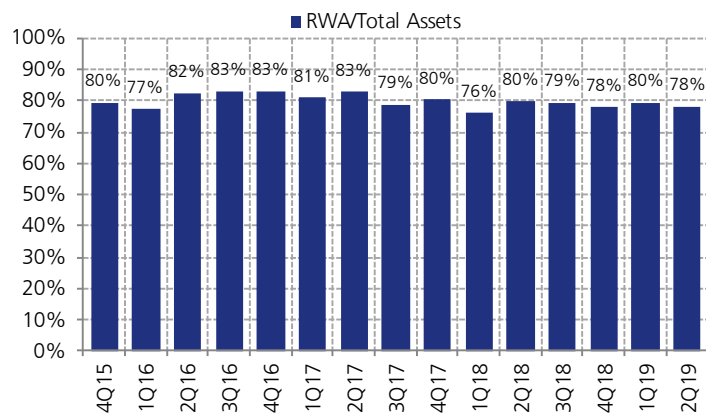
RWAs Composition (Rs bn)	2Q18	1Q19	2Q19	YoY (%)	QoQ (%)
Credit risk, CVA and UFCE	1329	1534	1,666	25.3%	8.6%
Market risk	83	98	86	3.6%	-12.1%
Operational risk	148	188	188	27.1%	0.0%
Total RWAs	1,561	1,820	1,940	24.3%	6.6%
Loans	1,232	1,507	1,631	32.4%	8.3%
Exposure					
- Fund based exposure	1,653	1,815	1,993	20.6%	9.8%
- Non-Fund based exposure	630	698	836	32.7%	19.7%
Total exposure	2,283	2,513	2,829	23.9%	12.6%
RWA/ Total loans	127%	121%	119%	-7.7%	-1.9%
RWA/ Total exposure	68%	72%	69%	0.2%	-3.9%

Source: Company, JM Financial

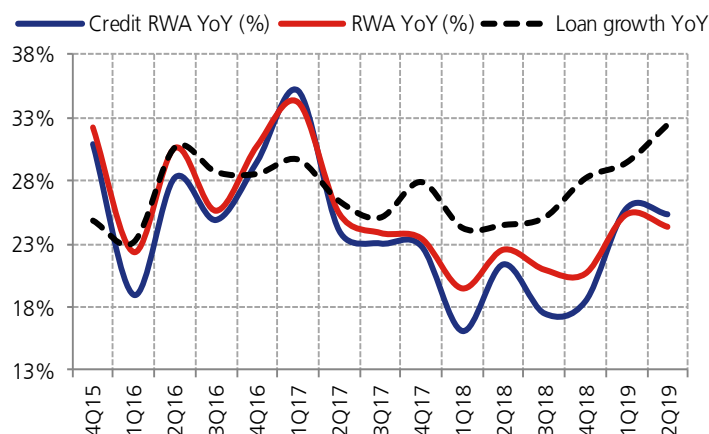
Exhibit 6. IndusInd Bank: Loan book mix; Consumer finance growing strong

Loan Book Composition (Rs bn)	2Q18	1Q19	2Q19	YoY (%)	QoQ (%)
Consumer Finance					
Comm. Vehicle Loans	163.8	207.0	219.9	34.2%	6.2%
Utility Vehicle Loans	25.1	30.3	32.0	27.3%	5.8%
Small CV (Incl 3Ws)	23.9	27.3	28.9	20.7%	5.6%
2Ws loans	32.9	37.5	38.7	17.6%	3.0%
Car loans	50.4	56.0	58.9	16.9%	5.2%
Tractor	22.7	28.6	30.8	35.8%	7.9%
Equipment Financing	46.0	59.9	62.9	36.7%	4.9%
Credit card	21.6	29.8	31.9	47.5%	6.8%
LAP	75.5	81.8	83.2	10.3%	1.8%
Others (Home, Personal)	32.6	44.4	49.2	50.8%	11.0%
Total	494.7	602.6	636.4	28.7%	5.6%
Corporate & commercial Banking					
Large corporates	361.3	449.6	494.7	36.9%	10.0%
Mid size corporates	235.7	265.4	300.9	27.7%	13.3%
Small corporates	140.2	189.1	199.4	42.3%	5.5%
Total	737.2	904.1	995.0	35.0%	10.1%
Total Advances	1,231.8	1,506.8	1,631.4	32.4%	8.3%
Loan Mix (%)					
Consumer Finance					
Comm. Vehicle Loans	13.3%	13.7%	13.5%	0.2%	-0.3%
Utility Vehicle Loans	2.0%	2.0%	2.0%	-0.1%	0.0%
Small CV (Incl 3Ws)	1.9%	1.8%	1.8%	-0.2%	0.0%
2Ws loans	2.7%	2.5%	2.4%	-0.3%	-0.1%
Car loans	4.1%	3.7%	3.6%	-0.5%	-0.1%
Tractor	1.8%	1.9%	1.9%	0.0%	0.0%
Equipment Financing	3.7%	4.0%	3.9%	0.1%	-0.1%
Credit card	1.8%	2.0%	2.0%	0.2%	0.0%
LAP	6.1%	5.4%	5.1%	-1.0%	-0.3%
Others (Home, Personal)	2.6%	2.9%	3.0%	0.4%	0.1%
Total	40.2%	40.0%	39.0%	-1.1%	-1.0%
Corporate & commercial Banking					
Large corporates	29.3%	29.8%	30.3%	1.0%	0.5%
Mid size corporates	19.1%	17.6%	18.4%	-0.7%	0.8%
Small corporates	11.4%	12.6%	12.2%	0.8%	-0.3%
Total	59.8%	60.0%	61.0%	1.1%	1.0%
Total Advances	100%	100%	100%		

Source: Company, JM Financial

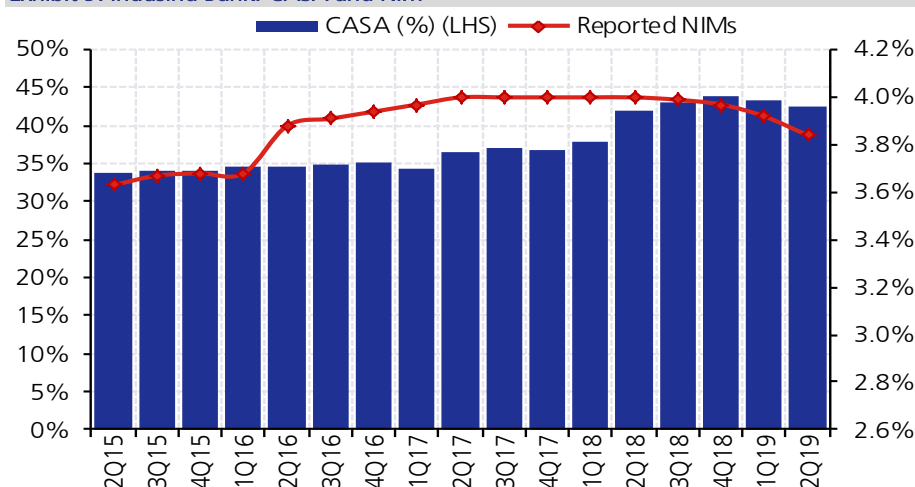
Exhibit 7. IndusInd Bank: Risk weighted assets as % of total

Source: Company, JM Financial

Exhibit 8. IndusInd Bank: Growth in credit RWA

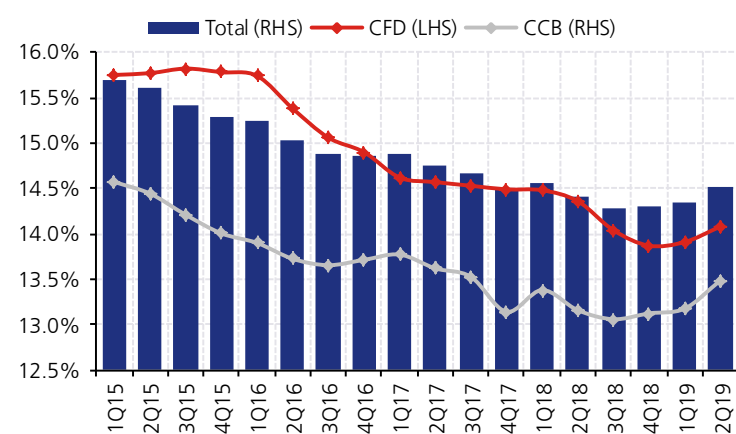
Source: Company, JM Financial

Exhibit 9. Indusind Bank: CASA and NIM



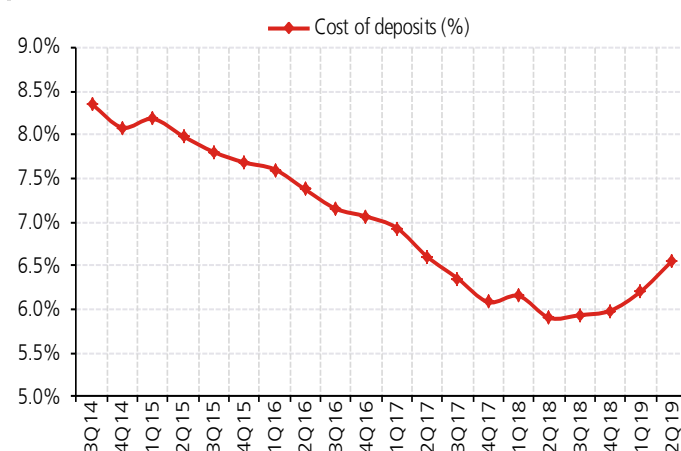
Source: Company, JM Financial

Exhibit 10. Indusind Bank: Yield on loans trends



Source: Company, JM Financial

Exhibit 11. Indusind Bank: Cost of deposits trends



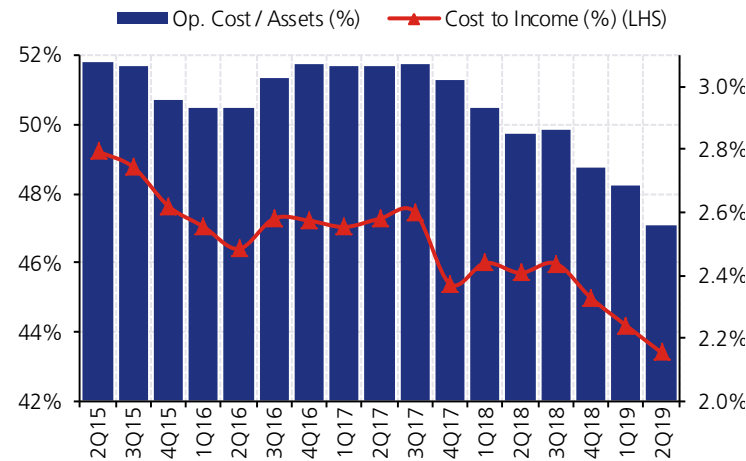
Source: Company, JM Financial

Exhibit 12. Indusind Bank: Fee income composition

Fee income Composition (Rs mn)	2Q18	1Q19	2Q19	YoY (%)	QoQ (%)
Trade & Remittances	1,280	1,410	1,510	18.0%	7.1%
Loan Processing Fees	2,140	2,300	2,600	21.5%	13.0%
FX income	1,830	2,280	2,230	21.9%	-2.2%
TPP Dist income (MF, Insurance)	2,370	2,780	2,800	18.1%	0.7%
Investment Banking Income	1,860	2,080	2,130	14.5%	2.4%
General Banking fee	650	800	910	40.0%	13.8%
Total	10,130	11,650	12,180	20.2%	4.5%

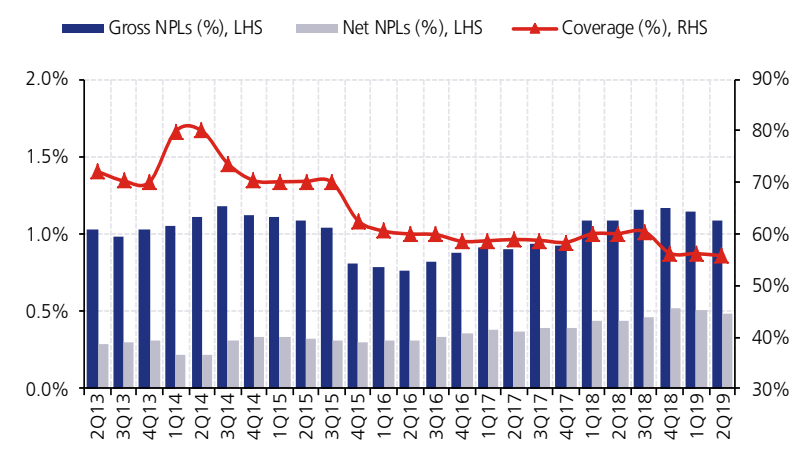
Source: Company, JM Financial

Exhibit 13. IndusInd Bank: Operating costs and cost to income trends



Source: Company, JM Financial

Exhibit 14. IndusInd Bank: Trends in credit costs and NPL ratios (%)



Source: Company, JM Financial

Valuation and 12M TP

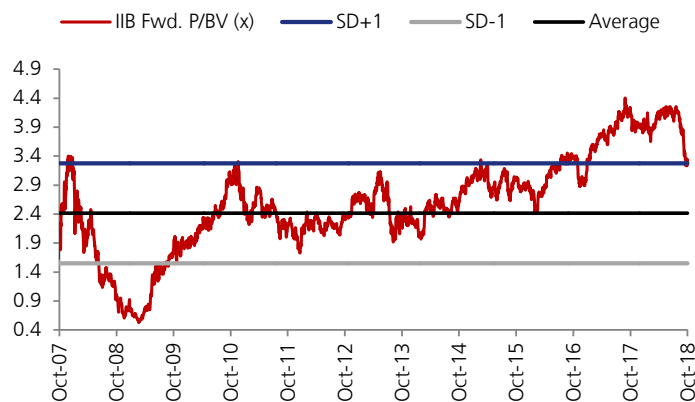
We value IndusInd Bank on a two-stage Gordon Growth Model. Our assumptions are as follows:

Exhibit 15. Valuation Summary

Initial no of years	10
Growth rate for the first 10 years (%)	18.8%
Pay out ratio for the first 10 years (%)	7%
Perpetual growth rate (%)	4.0%
Perpetual payout ratio (%)	80.0%
K1	0.96
K2	17.43
Fully adjusted FY20E BVPS (INR)	559
Target P/BV (x)	3.7x
Fair value (rounded off)	2,075

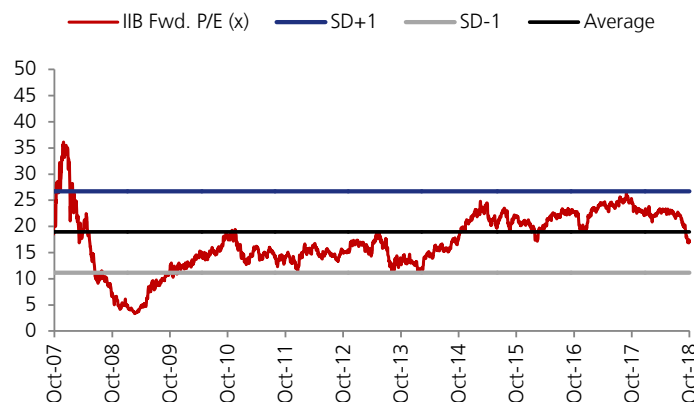
Source: Company, JM Financial

Exhibit 16. One year fwd Price / BVPS



Source: Company, JM Financial

Exhibit 17. One year fwd Price / earnings



Source: Company, JM Financial

Financial Tables (Standalone)

Profit & Loss (INR mn)					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Net Interest Income	45,166	60,626	74,974	1,17,825	1,52,105
Profit on Investments	1,453	2,769	3,638	2,500	2,500
Exchange Income	8,370	9,195	9,210	10,118	14,500
Fee & Other Income	23,147	29,751	34,653	50,668	64,177
Non-Interest Income	32,969	41,715	47,501	63,286	81,177
Total Income	78,135	1,02,341	1,22,475	1,81,111	2,33,282
Operating Expenses	36,721	47,831	55,914	79,444	98,642
Pre-provisioning Profits	41,414	54,510	66,561	1,01,666	1,34,640
Loan-Loss Provisions	6,141	10,506	8,380	14,700	18,135
Provisions on Investments	295	314	1,209	250	300
Others Provisions	286	94	2,165	3,250	500
Total Provisions	6,722	10,913	11,754	18,200	18,935
PBT	34,693	43,597	54,807	83,466	1,15,705
Tax	11,828	14,918	18,747	28,379	39,918
PAT (Pre-Extraordinaries)	22,864	28,679	36,060	55,088	75,787
Extra ordinaries (Net of Tax)	0	0	-	0	0
Reported Profits	22,864	28,679	36,060	55,088	75,787
Dividend paid	3,522	4,320	5,427	8,263	11,747
Retained Profits	19,343	24,359	30,633	46,825	64,040

Source: Company, JM Financial

Key Ratios					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Growth (YoY) (%)					
Deposits	25.4%	36.1%	19.8%	30.0%	27.0%
Advances	28.5%	27.9%	28.2%	27.0%	27.0%
Total Assets	25.4%	27.6%	24.1%	29.3%	25.8%
NII	32.1%	34.2%	23.7%	36.8%	29.1%
Non-interest Income	29.4%	26.5%	13.9%	25.9%	28.3%
Operating Expenses	27.9%	30.3%	16.9%	26.3%	24.2%
Operating Profits	33.7%	31.6%	22.1%	38.3%	32.4%
Core Operating profit	34.1%	29.5%	21.6%	41.9%	33.3%
Provisions	72.8%	62.4%	7.7%	28.6%	4.0%
Reported PAT	27.5%	25.4%	25.7%	35.6%	37.6%
Yields / Margins (%)					
Interest Spread	3.08%	3.28%	3.4%	3.9%	4.0%
NIM	3.82%	4.04%	4.0%	4.6%	4.6%
Profitability (%)					
Non-IR to Income	42.2%	40.8%	38.8%	34.9%	34.8%
Cost to Income	47.0%	46.7%	45.7%	43.9%	42.3%
ROA	1.82%	1.80%	1.8%	2.0%	2.2%
ROE	16.6%	15.3%	16.5%	18.0%	20.9%
Assets Quality (%)					
Slippages	1.24%	1.62%	3.0%	1.6%	1.5%
Gross NPA	0.87%	0.93%	1.2%	1.1%	1.1%
Net NPAs	0.36%	0.39%	0.5%	0.5%	0.4%
Provision Coverage	58.6%	58.4%	56.3%	60.0%	60.0%
Specific LLP	0.64%	0.70%	0.7%	0.7%	0.7%
Net NPAs / Networth	1.9%	2.2%	3.2%	2.7%	2.8%
Capital Adequacy (%)					
Tier I	14.92%	14.72%	14.6%	14.5%	14.0%
CAR	15.50%	15.31%	15.0%	14.8%	14.3%

Source: Company, JM Financial

Balance Sheet (INR mn)					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Equity Capital	5,950	5,981	6,002	7,004	7,004
Reserves & Surplus	1,67,065	1,96,582	2,28,646	3,23,017	3,87,057
Deposits	9,30,003	12,65,722	15,16,392	19,71,309	25,03,563
Borrowings	2,21,559	2,24,537	3,82,891	6,22,727	7,80,909
Other Liabilities	72,048	89,764	78,708	1,10,291	1,37,702
Total Liabilities	13,96,762	17,82,738	22,12,640	30,34,349	38,16,235
Investments	3,12,143	3,67,021	5,00,767	6,19,937	7,85,167
Net Advances	8,84,193	11,30,805	14,49,537	20,00,855	25,41,086
Cash & Equivalents	1,21,119	1,86,283	1,32,159	2,81,702	3,56,604
Fixed Assets	8,746	9,606	9,765	16,268	19,315
Other Assets	70,561	89,023	1,20,412	1,15,586	1,14,063
Total Assets	13,96,762	17,82,738	22,12,640	30,34,349	38,16,235

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
NII / Assets	3.60%	3.81%	3.8%	4.38%	4.44%
Other Income / Assets	2.63%	2.62%	2.4%	2.35%	2.37%
Total Income / Assets	6.22%	6.44%	6.1%	6.73%	6.81%
Cost / Assets	2.93%	3.01%	2.8%	2.95%	2.88%
PBP / Assets	3.30%	3.43%	3.3%	3.78%	3.93%
Provisions / Assets	0.54%	0.69%	0.6%	0.68%	0.55%
PBT / Assets	2.76%	2.74%	2.7%	3.10%	3.38%
Tax rate	34.1%	34.2%	34.2%	34.00%	34.50%
ROA	1.82%	1.80%	1.8%	2.05%	2.21%
RoRWAs	2.23%	2.21%	2.3%	2.69%	2.91%
Leverage	8.1	8.8	9.1	8.78	9.46
ROE	16.6%	15.3%	16.5%	18.0%	20.9%

Source: Company, JM Financial

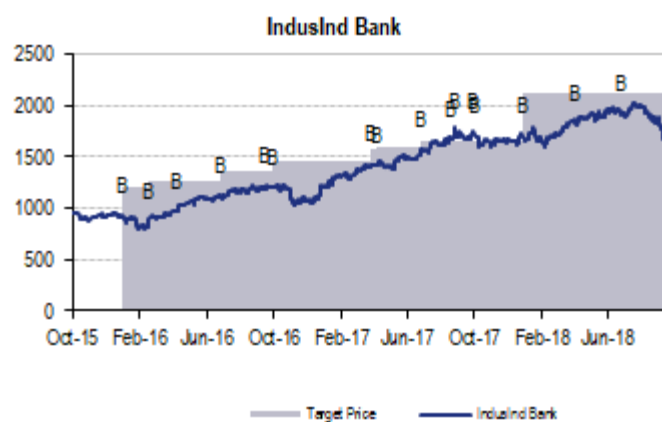
Valuations					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Shares in Issue	595.0	598.1	600.2	700.4	700.4
EPS (INR)	38.4	47.9	60.1	78.7	108.2
EPS (YoY) (%)	13.4%	24.8%	25.3%	35.6%	37.6%
PER (x)	42.3	33.9	27.1	20.7	15.0
BV (INR)	291	339	391	471	563
BV (YoY) (%)	50.4%	16.5%	15.4%	16.5%	19.4%
ABV (INR)	289	337	387	468	559
ABV (YoY) (%)	50.2%	16.4%	15.0%	16.5%	19.4%
P/BV (x)	5.60	4.80	4.2	3.5	2.9
P/ABV (x)	5.62	4.83	4.2	3.5	2.9
DPS (INR)	4.7	6.0	9.0	11.8	16.8
Div. yield (%)	0.3%	0.4%	0.6%	0.7%	1.0%

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	Recommendation	Target Price	% Chg.
13-Jan-16	Buy	1,200	
2-Mar-16	Buy	1,260	5.0
22-Apr-16	Buy	1,260	0.0
12-Jul-16	Buy	1,350	7.1
28-Sep-16	Buy	1,350	0.0
13-Oct-16	Buy	1,450	7.4
12-Apr-17	Buy	1,572	8.4
20-Apr-17	Buy	1,590	1.1
12-Jul-17	Buy	1,650	3.8
4-Sep-17	Buy	1,650	0.0
12-Sep-17	Buy	1,650	0.0
13-Oct-17	Buy	1,650	0.0
16-Oct-17	Buy	1,650	0.0
12-Jan-18	Buy	2,120	28.5
19-Apr-18	Buy	2,120	0.0
10-Jul-18	Buy	2,120	0.0

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

(formerly known as JM Financial Securities Limited)

Corporate Identity Number: U67100MH2017PLC296081

Member of BSE Ltd., National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.

SEBI Registration Nos.: Stock Broker - INZ000163434, Research Analyst – INH0000000610

Registered Office: 7th Floor, Cnergy, Appasaheb Marathe Marg, Prabhadevi, Mumbai 400 025, India.

Board: +9122 6630 3030 | Fax: +91 22 6630 3488 | Email: jmfinancial.research@jmfl.com | www.jmfl.comCompliance Officer: Mr. Sunny Shah | Tel: +91 22 6630 3383 | Email: sunny.shah@jmfl.com

Definition of ratings	
Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
Sell	Price expected to move downwards by more than 10%

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