

15 October 2018

IndusInd Bank

Core trends intact despite high provisions; maintaining a Buy

Rating: **Buy**

Target Price: ₹1,914

Share Price: ₹1,623

Another quarter of strong credit and operating profit growth was reported by IndusInd Bank. Provisions made for the exposure to IL&FS, however, led to lower profitability. We are sanguine about its loan-growth prospects and its asset quality, given a low stressed pipeline and insignificant restructured portfolio. We retain our Buy recommendation.

Benign asset quality. We expect the bank to maintain stable asset quality over FY19-20, aided by its well-diversified loan mix. Slippages softened to 1% (a many-quarter low) and we do not expect any negative surprises on the asset quality front in coming quarters as the bank has a negligible stressed pipeline on the corporate side (barring exposure to IL&FS, for which it has adequately provided) and low risk on its vehicle-finance portfolio.

Robust growth in credit book maintained. The loan book grew 32% y/y, driven by high growth in both the corporate book (up 35% y/y) and retail (up 29% y/y). We expect mid-20s loan growth to continue in the medium term. Management intends to focus on the retail portfolio to drive growth. Its tier-1 capital ratio of 13.9% suffices to support its medium-term loan-growth plans.

NIM declines, BHAFIN acquisition to ease pressure. NIM was ~3.84%, down 8bps sequentially, on account of a sharp increase in the cost of funds (up 20bps sequentially). While we see strong pricing power on the corporate side, with the high portion of retail lending on fixed rate however, we could see additional pressure on NIM in coming quarters. Acquisition of BHAFIN would likely act as a fillip, leading to easing of pressure on NIM.

Valuation. Our Oct'19 target of ₹1,914 is based on the two-stage DDM model. This implies a ~3.6x P/ABV multiple on its FY20e book. **Risks:** Lumpy slippages from the corporate book; volatility in asset quality, post-merger.

Key financials (YE Mar)	FY16	FY17	FY18	FY19e	FY20e
Net interest income (₹ m)	45,166	60,626	74,974	92,157	1,15,777
Pre-provisioning profit (₹ m)	41,414	54,510	66,561	81,856	1,01,377
Provisions (₹ m)	6,722	10,913	11,754	14,700	17,374
PAT (₹ m)	22,864	28,679	36,060	43,987	55,022
EPS (₹)	38	48	60	73	92
NIM (%)	3.9	4.1	4.0	3.8	3.8
Cost-Income (%)	47	47	46	46	45
RoE (%)	16.2	15.0	16.2	17.1	18.3
RoA (%)	1.8	1.8	1.8	1.8	1.8
Advances growth (%)	28.5	27.9	28.2	26.0	26.0
GNPA (%)	0.9	0.9	1.2	1.1	1.0
CAR (%)	15.5	15.3	15.0	14.6	13.9
P / E (x)	42.4	34.0	27.1	22.3	17.8
P / BV (x)	5.5	4.7	4.1	3.5	3.0
P / ABV (x)	5.6	4.8	4.2	3.6	3.1

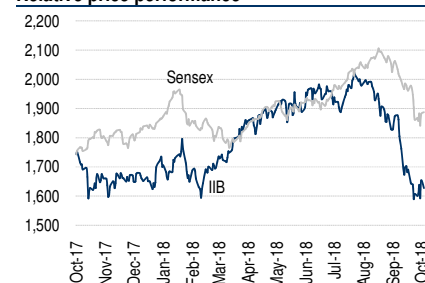
Source: Company, Anand Rathi Research

Key data	IIB IN / INBK.BO
52-week high / low	₹2,038 / 1,551
Sensex / Nifty	34865 / 10513
3-m average volume	\$39.2m
Market cap	₹978bn / \$13,252m
Shares outstanding	601m

Shareholding pattern (%)	Sep '18	Jun '18	Mar '18
Promoters	16.7	16.8	16.8
- of which, Pledged	26.5	26.5	26.5
Free float	83.3	83.2	83.2
- Foreign institutions	52.2	52.6	52.1
- Domestic institutions	10.2	10.6	11.2
- Public	20.9	20.0	20.0

Estimates revision (%)	FY19e	FY20e
NII	(4.5)	(5.1)
EPS	(6.4)	(6.8)
RoE	(5.7)	(5.3)

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
Net interest income	45,166	60,626	74,974	92,157	1,15,777
NII growth (%)	32.1	34.2	23.7	22.9	25.6
Non-interest income	32,969	41,715	47,501	58,092	69,906
Income	78,135	1,02,341	1,22,475	1,50,248	1,85,682
Income growth (%)	34.2	31.0	19.7	22.7	23.6
Operating expenses	36,721	47,831	55,914	68,393	84,305
PPOP	41,414	54,510	66,561	81,856	1,01,377
PPOP growth (%)	33.7	31.6	22.1	23.0	23.8
Provisions	6,722	10,913	11,754	14,700	17,374
PBT	34,693	43,597	54,807	67,156	84,003
Tax	11,828	14,918	18,747	23,169	28,981
PAT	22,864	28,679	36,060	43,987	55,022
PAT growth (%)	27.5	25.4	25.7	22.0	25.1
FDEPS (₹ /sh)	38.4	47.9	60.1	73.2	91.5
DPS (₹ /sh)	5.9	6.0	7.5	9.1	11.4

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
Share capital	5,950	5,981	6,002	6,013	6,013
Reserves & surplus	170,872	200,328	232,268	270,757	318,902
Deposits	930,003	1,265,722	1,516,392	1,865,162	2,294,149
Borrowings	221,559	224,537	382,891	459,469	539,876
Minority interests	0	0	0	0	0
Total liabilities	1,400,570	1,786,484	2,216,262	2,715,615	3,337,426
Advances	884,193	1,130,805	1,449,537	1,826,416	2,301,284
Investments	312,143	367,021	500,767	600,921	721,105
Cash & bank bal	45,210	77,487	109,624	122,779	137,512
Fixed & other assets	12,553	13,352	13,398	14,067	14,771
Total assets	1,400,570	1,786,484	2,216,272	2,715,615	3,337,426
No. of shares (m)	595	598	600	601	601
Deposits growth (%)	25.4	36.1	19.8	23.0	23.0
Advances growth (%)	28.5	27.9	28.2	26.0	26.0

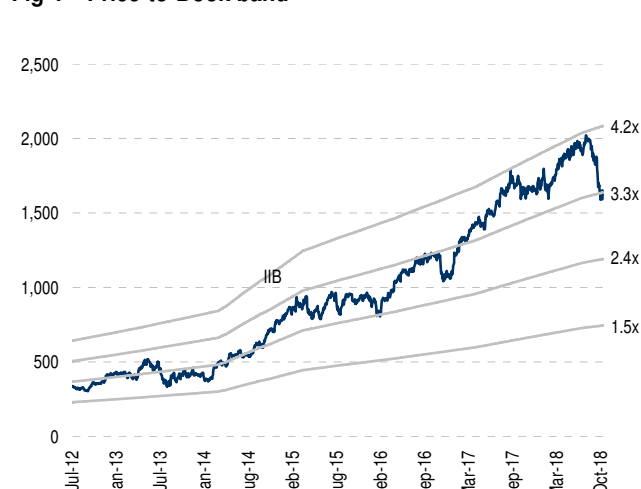
Source: Company, Anand Rathi Research

Fig 3 – Ratio analysis

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
NIM	3.9	4.1	4.0	3.8	3.8
Other inc. / total inc.	42.2	40.8	38.8	38.7	37.6
Cost-income	47.0	46.7	45.7	45.5	45.4
Provision coverage	58.6	58.4	56.3	58.5	59.4
Dividend payout	15.4	12.5	12.5	12.5	12.5
Credit-deposit	95.1	89.3	95.6	97.9	100.3
Investment-deposit	33.6	29.0	33.0	32.2	31.4
Gross NPA	0.9	0.9	1.2	1.1	1.0
Net NPA	0.4	0.4	0.5	0.5	0.4
BV (₹)	297.2	344.9	397.0	460.3	540.4
Adj. BV (₹)	293.4	339.8	388.3	450.7	529.9
CAR (%)	15.5	15.3	15.0	14.6	13.9
- Tier 1	14.9	14.7	14.6	14.0	13.3
RoE	16.2	15.0	16.2	17.1	18.3
RoA	1.8	1.8	1.8	1.8	1.8

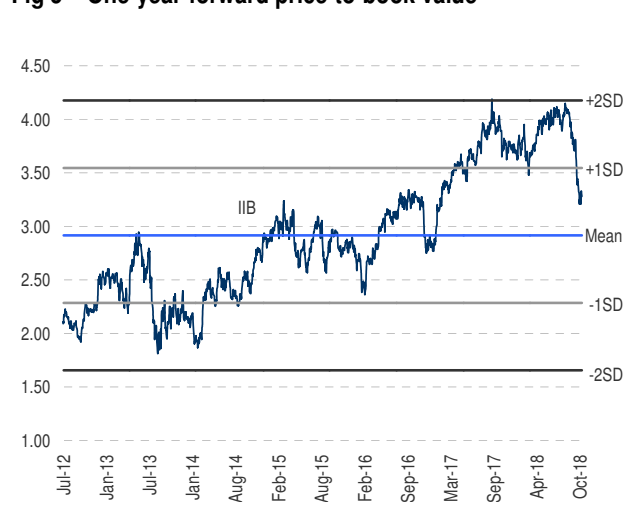
Source: Company, Anand Rathi Research

Fig 4 – Price-to-Book band



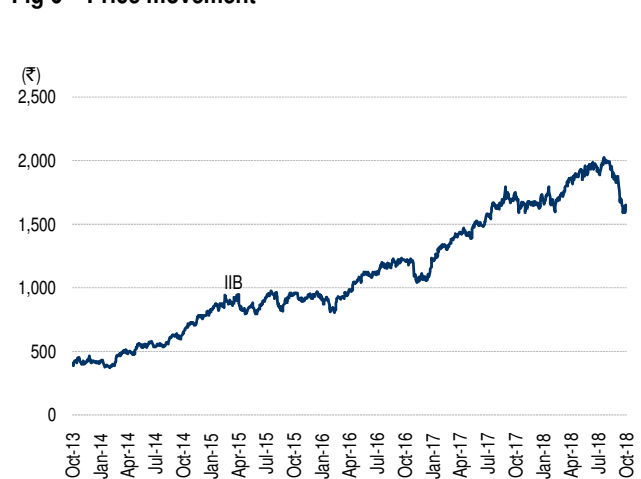
Source: Bloomberg

Fig 5 – One-year-forward price-to-book value



Source: Company, Anand Rathi Research

Fig 6 – Price movement



Source: Bloomberg

Key Highlights

Asset quality

- We expect slippages to ease from current levels on account of the
 - a) negligible restructured book (11bps of the total book),
 - b) low SMA2 and
 - c) downshift in the weighted-average risk score for the vehicle-finance portfolio (1.8 for Sep'18, down from 1.85 in Sep'16).
- ₹2.75bn was contingently provided toward the IL&FS exposure. Management stated that, in the worst case, a 25% additional provision could be made.
- Management expects credit cost for FY19 to come at ~50-60bps.

Fig 7 – Segment-wise results

Break-up of GNPA (₹ m)	FY18				FY19	
	Q1	Q2	Q3	Q4	Q1	Q2
Opening balance	10,550	12,720	13,460	14,990	17,050	17,410
Slippages	6,080	4,980	4,080	8,600	4,750	4,190
Gross-slippage ratio (%)	0.52	0.40	0.32	0.59	0.32	1.03
Reductions	3,910	4,240	2,550	6,540	4,390	3,790
Closing balance	12,720	13,460	14,990	17,050	17,410	17,810
Total GNPA	12,717	13,453	14,987	17,049	17,406	17,814
GNPA (%)	1.09	1.08	1.16	1.17	1.15	1.09
NNPA (%)	0.44	0.44	0.46	0.51	0.51	0.48

Source: Company, Anand Rathi Research

Fig 8 – Gross NPA - Segment wise (Consumer Finance)

	FY18				FY19	
	Q1	Q2	Q3	Q4	Q1	Q2
Commercial vehicles	1.12	1.02	0.93	0.99	0.91	0.93
Utility vehicles	1.42	1.37	1.25	1.28	1.38	1.32
Construction equipment	1.07	0.97	1.06	1.07	0.88	0.73
Small CVs	1.33	1.10	1.22	1.27	1.09	1.27
2-wheelers	3.55	3.55	3.78	3.81	3.67	3.87
Cars	0.74	0.68	0.62	0.67	0.69	0.80
LAP / HL / PL	1.02	0.37	0.56	0.59	0.39	0.60
Tractors	0.85	1.06	1.15	1.29	1.20	1.72
Credit Cards	1.21	1.48	1.65	1.61	1.77	1.78
Total	1.25	1.19	1.10	1.13	1.04	1.13

Source: Company, Anand Rathi Research

Fig 9 – NPA - Corporate (%)

	FY18				FY19	
	Q1	Q2	Q3	Q4	Q1	Q2
GNPA	0.98	1.12	1.21	1.20	1.23	1.07
Slippages	2.03	1.55	0.75	2.46	0.92	0.37
Credit cost	0.62	0.76	0.39	0.67	0.35	0.57

Source: Company, Anand Rathi Research

Core fee income

“Other income” clocked a strong ~32% CAGR over FY08-18; now, it constitutes ~37% of income. In the quarter, it rose ~17% y/y despite a ~43% drop in trading income. We expect the growth momentum in core fee income to be in line with balance-sheet growth over FY19-20.

Fig 10 – Segment-wise results

Fee income (₹ m)	FY18				FY19	
	Q1	Q2	Q3	Q4	Q1	Q2
General banking fees	640	650	700	650	800	910
Processing fees	1,960	2,140	2,420	2,280	2,300	2,600
FX	1,980	1,830	2,020	1,970	2,280	2,230
Insurance	2,100	2,370	2,560	2,730	2,780	2,800
Investment banking	1,750	1,860	1,800	1,970	2,080	2,130
Trade & remittances	1,310	1,280	1,270	1,530	1,410	1,510
Total	9,740	10,130	10,770	11,130	11,650	12,180

Source: Company, Anand Rathi Research

Loan book

- The bank sold off ₹85bn loans in the quarter (₹80bn the quarter prior).
- Re-pricing of loan book was done in the quarter: corporate book 53bps, retail book 17bps.

Fig 11 – Break-up of advances

(₹ %)	FY13	FY14	FY15	FY16	FY17	FY18	Q1 FY19	Q2 FY19
Corporate and commercial banking (CCB)	49.5	55.0	58.7	58.7	59.7	60.5	60.0	61.0
Corporate banking	41.3	45.0	45.7	47.4	47.5	48.3	47.5	48.8
Small business	8.1	10.1	13.0	11.3	12.3	12.3	12.6	12.2
Consumer finance division (CFD)	50.5	45.0	41.3	41.3	40.3	39.5	40.0	39.0
Commercial vehicles	22.5	17.4	15.4	15.9	13.8	13.7	13.7	13.5
Equipment financing	6.1	5.2	4.1	3.7	3.6	3.8	4.0	3.9
Two-wheelers	4.3	4.6	4.1	3.4	2.9	2.5	2.5	2.4
Car loans	4.6	4.8	4.6	4.4	4.1	3.7	3.7	3.6
Utility vehicles + 3W	8.8	7.2	5.6	6.5	5.8	5.6	5.7	5.6
Home loans + LAP	3.4	4.9	6.5	5.9	6.2	5.5	5.4	5.1
Personal loans + credit cards	0.8	0.8	1.0	1.4	3.8	4.7	4.9	5.0
Total	100	100	100	100	100	100	100	100

Source: Company, Anand Rathi Research

Quarterly snapshot

Fig 12 – Income statement

	FY18				FY19	
(₹ m)	Q1	Q2	Q3	Q4	Q1	Q2
Interest income	41,355	42,084	42,868	46,501	50,682	54,381
Interest expense	23,615	23,874	23,920	26,425	29,457	32,348
NII	17,741	18,210	18,948	20,076	21,224	22,033
Y/Y growth (%)	30.8	24.7	20.0	20.4	19.6	21.0
Non-interest income	11,673	11,876	11,868	12,085	13,016	13,173
Trading profits	1,930	1,750	1,100	950	1,370	990
Total Income	29,413	30,086	30,816	32,161	34,240	35,206
Y/Y growth (%)	26.3	23.8	18.7	11.7	16.4	17.0
Operating expenses	13,528	13,751	14,169	14,467	15,129	15,281
Of which staff cost	4,222	4,450	4,600	4,535	4,620	4,582
PPOP	15,885	16,335	16,647	17,694	19,111	19,924
Y/Y growth (%)	28.8	27.5	22.1	12.5	20.3	22.0
Total provisions	3,100	2,938	2,362	3,356	3,500	5,903
PBT	12,786	13,398	14,285	14,338	15,611	14,022
Tax	4,420	4,597	4,923	4,808	5,254	4,819
PAT	8,365	8,801	9,363	9,531	10,357	9,203
Y/Y growth (%)	26.5	25.0	24.7	26.8	23.8	4.6

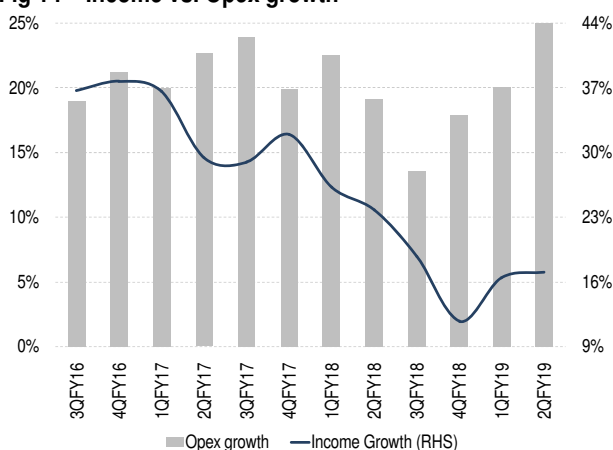
Source: Company, Anand Rathi Research

Fig 13 – Balance sheet

	FY18				FY19	
(₹ m)	Q1	Q2	Q3	Q4	Q1	Q2
Equity capital	5,990	5,989	6,000	6,002	6,002	6,013
Reserves & Surplus	209,020	213,727	223,400	2,32,414	243,210	247,632
Deposits	1,336,730	1,414,406	1,460,860	1,516,392	1,588,620	1,682,193
Borrowings	274,040	235,577	233,670	382,891	370,400	428,281
Other Liabilities	80,720	80,619	83,090	78,563	80,560	119,080
Equity and Liabilities	1,906,500	1,950,317	2,007,020	2,216,262	2,288,792	2,483,199
Deposits y/y growth (%)	31.4	25.9	22.5	19.8	18.8	18.9
Deposits q/q growth (%)	5.6	5.8	3.3	3.8	4.8	5.9
Assets						
Cash and cash balances	201,690	183,087	135,880	132,159	119,900	183,326
Advances	1,164,070	1,231,808	1,285,420	1,449,537	1,506,750	1,631,443
Investments	421,470	421,459	461,710	500,767	526,730	500,885
Other assets	119,270	113,962	124,020	133,809	135,410	167,545
Total Assets	1,906,500	1,950,317	2,007,020	2,216,262	2,288,790	2,483,199
Advances y/y growth (%)	24.3	24.5	25.1	28.2	29.4	32.4
Advances q/q growth (%)	2.9	5.8	4.4	12.8	3.9	8.3

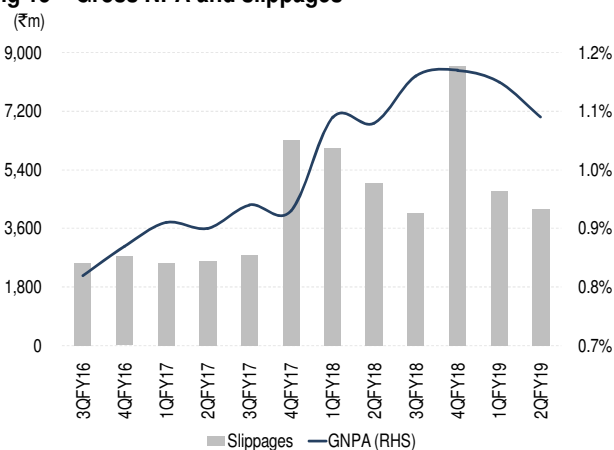
Source: Company, Anand Rathi Research

Fig 14 – Income vs. Opex growth



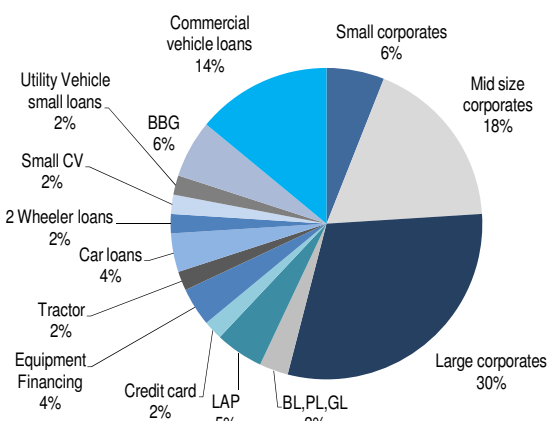
Source: Company, Anand Rathi Research

Fig 15 – Gross NPA and slippages



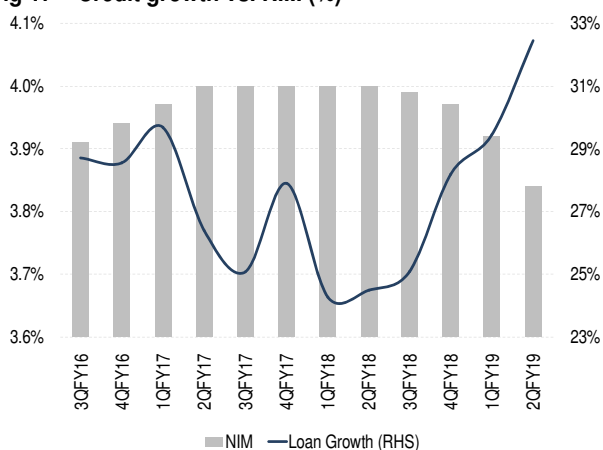
Source: Company, Anand Rathi Research

Fig 16 – Loan break-up



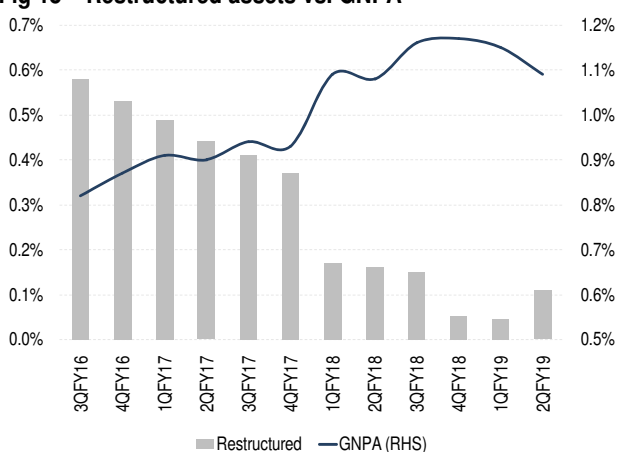
Source: Company, Anand Rathi Research

Fig 17 – Credit growth vs. NIM (%)



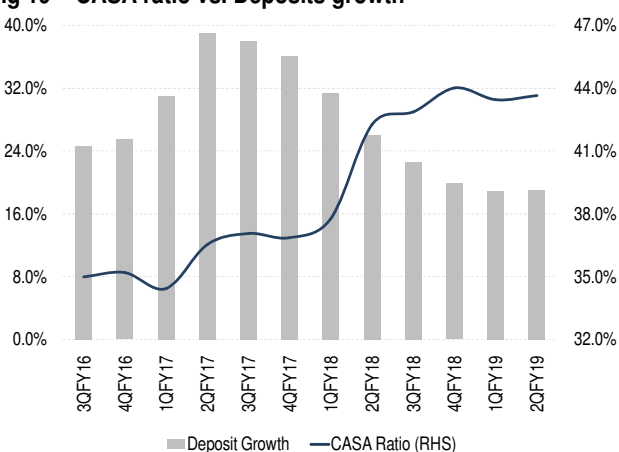
Source: Company, Anand Rathi Research

Fig 18 – Restructured assets vs. GNPA



Source: Company, Anand Rathi Research

Fig 19 – CASA ratio vs. Deposits growth



Source: Company, Anand Rathi Research

Valuation

- Our Oct'19 target of ₹1,914 is based on the two-stage DDM model. This implies a ~3.6x P/ABV multiple on its FY20e book.
- On the maturing of branches, CASA is likely to get a fillip, leading to lower cost of funding. Thus, there is further headroom for NIM expansion.

Fig 20 – Change in estimates

	FY19			FY20		
	New	Old	Chg %	New	Old	Chg %
Net interest income (₹ m)	92,157	96,512	(4.5)	1,15,777	1,21,961	(5.1)
EPS (₹)	73.2	78.1	(6.4)	91.5	98.2	(6.8)
RoE (%)	17.1	18.1	(5.7)	18.3	19.3	(5.3)

Source: Anand Rathi Research

Risks

- Lumpy slippages from the corporate book. Though unexpected, these would affect our forecasts.
- Any significant negative surprises on asset quality from the micro-finance book, post-merger.

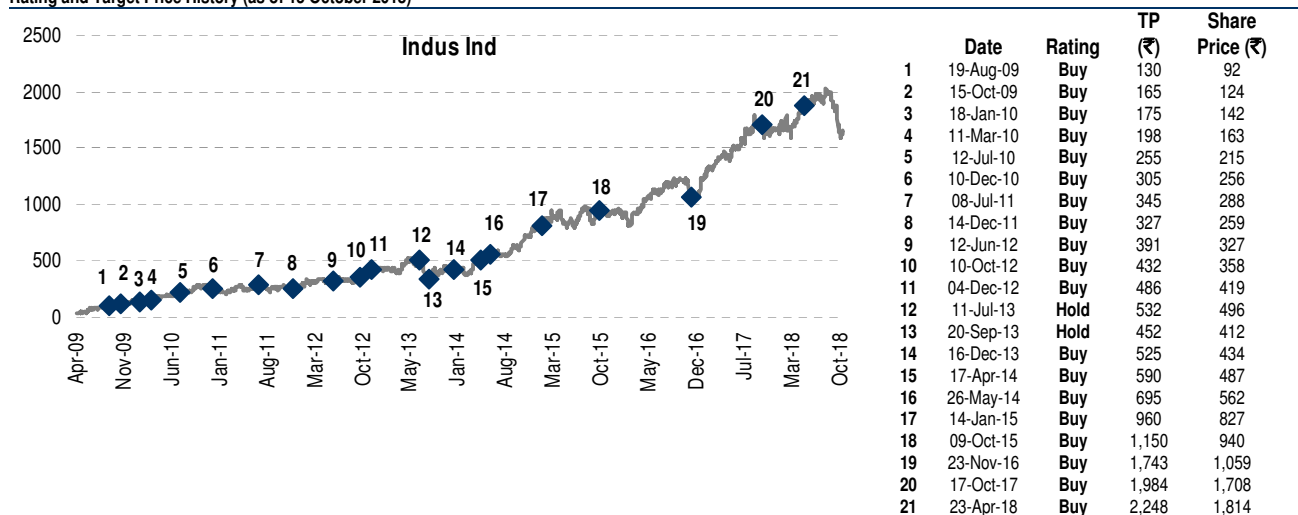
Appendix

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	Buy	Hold	Sell
Large Caps (>US\$1bn)	>15%	5-15%	<5%
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