kotak Institutional Equities

Banks/Diversified Financials

India

ATTRACTIVE

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UPDATE

BSE-30: 39,839

Banks to show improvement, muted quarter for NBFCs. As seen in the past few quarters, banks are likely to report further improvement in key metrics. Impairment ratios to decline led by lower slippages as well as high provisions for bad loans. 1QFY20 has a few one-offs, with merged financials for two banks, while the base has one-off recovery income. It was a muted quarter for most non-banks with weak loan growth, stable to compressed NIM even as asset quality held on well in most segments.

Banks: no big headwinds to worry about for the quarter as earnings recovery underway

We expect banks under coverage to show stable operating performance and recovery in earnings trajectory though there are a few one-offs for the quarter: (1) we would see the merged financials reported for BoB (with Dena and Vijaya) and IndusInd Bank (with Bharat Financial), (2) the base quarter had one-off net interest income (Bhushan Steel), (3) treasury income support would be higher given the interest rate movement. Loan growth has slowed to ~12% yoy which would put pressure on revenue growth and we expect the decelerating trends to be more visible in retail oriented loan books like HDFC Bank and IndusInd Bank.

Asset quality to show further improvement; slippages to ease considerably

The early warning indicators as reported by RBI in the financial stability report in the previous fortnight reaffirms our hypothesis that the pending stress to be recognized by the banks is not too high. We expect gross and net NPLs to show further improvement as we see slippages declining further. Resolution through the IBC framework has slowed as several high profile cases could not reach a conclusion as anticipated earlier. However, progress continues outside through settlements/upgradation/write-offs etc. Real estate exposure for banks is not too worrisome while exposure to a few NBFCs is likely to be an area of concern though it is unlikely to translate into NPLs this quarter for any of the banks

An unchanged outlook with a positive view on banks with corporate balance sheets

Among banks, we maintain our positive outlook on corporate banks (ICICI Bank and SBI) given their inexpensive valuations and visibility of steady progress towards RoE normalization in FY2020/21. Yes Bank would have the most challenging quarter while there is likely to be a lot of focus on asset quality even for IndusInd Bank and RBL Bank. Slowdown in revenue growth (loan and non-interest income) for banks like HDFC Bank is likely to dominate the discussion for the quarter. We see limited business concerns for Federal Bank and SFBs like Equitas, AU and Ujjivan which are seeing steady improvement in core performance. Sharp rise in ticket size and risks emerging from rapid growth in MFI AUMs in eastern India would be a key discussion area for banks which have a high share of MFI loans.

Diversified financials: a muted quarter

1QFY20E was a muted quarter for most non-banks with weak loan growth, stable to compressed NIM even as asset quality held on well in most segments. Slowdown across autos, weakness in rural cash flows and delay in Government spending led to muted performance in vehicle finance. Retail home loan sales were likely stable but slowdown in developer/LAP segment affected overall loan growth for HFCs. Asset quality performance was likely strong, in line with the trends observed over the previous few quarters. Rise in NPLs in the wholesale lending segment, especially developer loans, remains a major overhang on the sector. We hence expect non-banks to remain a bit cautious on liquidity and growth over the next few months; management commentary in this regard will be crucial.

M B Mahesh, CFA
mb.mahesh@kotak.com
Mumbai: +91-22-4336-0886

Nischint Chawathe
nischint.chawathe@kotak.com
Mumbai: +91-22-4336-0887

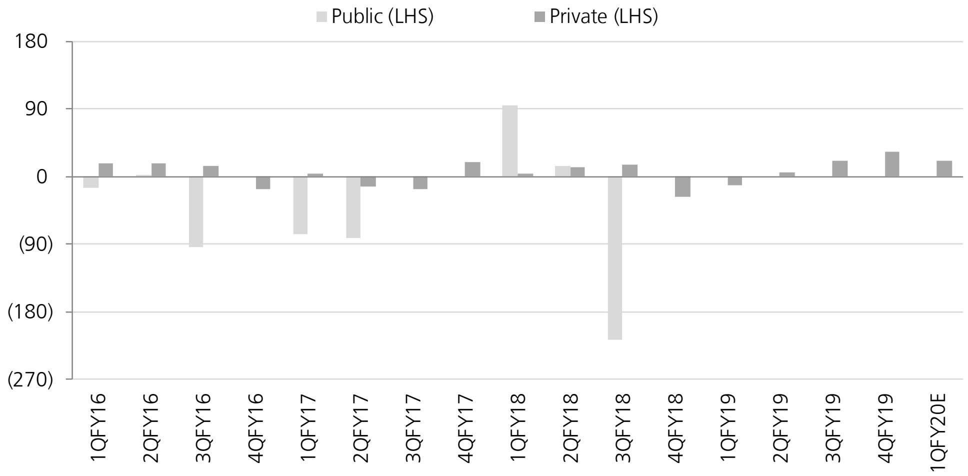
Dipanjan Ghosh
dipanjan.ghosh@kotak.com
Mumbai: +91-22-4336-0888

Shrey Singh
shrey.singh@kotak.com
Mumbai: +91-22-4336-0895

Venkat Madasu
venkat.madasu@kotak.com
Mumbai: +91-22-4336-0889

Kotak Institutional Equities Research
kotak.research@kotak.com
Mumbai: +91-22-4336-0000

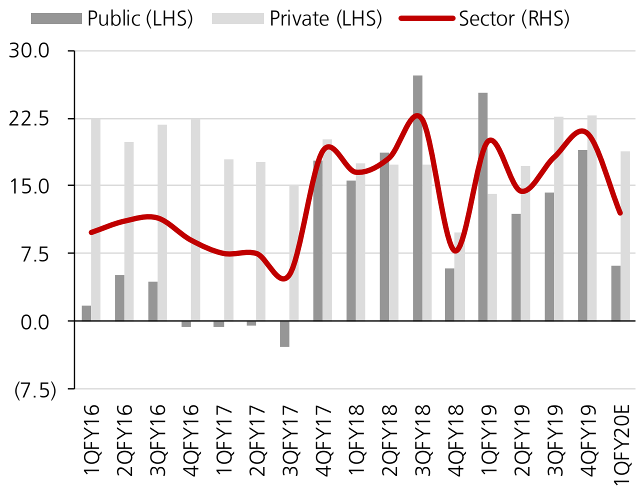
Exhibit 1: Private banks' profitability to improve going ahead
Yoy growth in PAT, March fiscal year-ends, 1QFY16-1QFY20E (%)



Notes:
(1) PAT for public banks and the overall sector was negative in 4QFY18

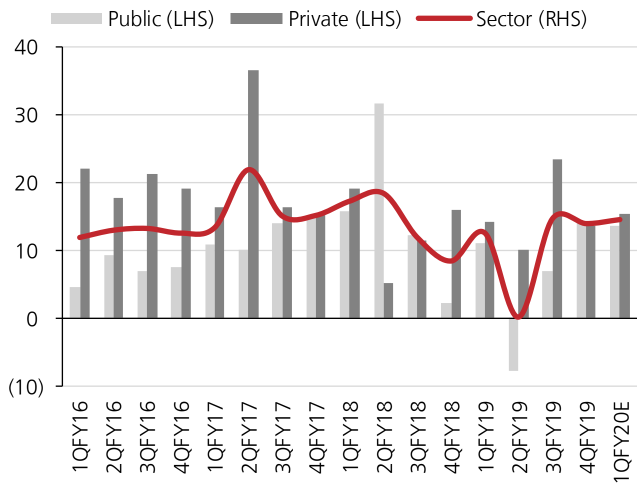
Source: Companies, Kotak Institutional Equities estimates

Exhibit 2: NII growth momentum retained qoq
Growth in NII, March fiscal year-ends, 1QFY16-1QFY20E (%)



Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Improvement in non-interest income to drive revenue growth
Revenue growth, March fiscal year-ends, 1QFY16-1QFY20E (%)



Note:
(1) Base quarter had one off impact of stake sale in subsidiaries by ICICI Bank and SBI.

Source: Company, Kotak Institutional Equities estimates

Exhibit 4: Earnings to show strong performance for a second consecutive quarter
YoY and QoQ growth in NII, PPoP and earnings, March fiscal year-ends, 1QFY19-1QFY20E

	Net interest income					Pre-provisioning profit					PAT				
	1QFY19 (Rs mn)	4QFY19 (Rs mn)	1QFY20E (Rs mn)	YoY (%)	QoQ (%)	1QFY19 (Rs mn)	4QFY19 (Rs mn)	1QFY20E (Rs mn)	YoY (%)	QoQ (%)	1QFY19 (Rs mn)	4QFY19 (Rs mn)	1QFY20E (Rs mn)	YoY (%)	QoQ (%)
Banks															
Public banks															
Bank of Baroda	43,811	50,670	67,703	55	34	30,056	38,608	47,982	60	24	5,283	(9,914)	9,507	80	NM
Canara Bank	38,829	35,002	33,736	(13)	(4)	29,328	29,735	27,907	(5)	(6)	2,815	(5,515)	2,830	1	NM
PNB	46,919	42,003	43,734	(7)	4	41,947	28,612	31,066	(26)	9	(9,400)	(47,496)	(12,024)	NM	NM
State Bank of India	217,984	229,538	225,207	3	(2)	119,731	169,331	151,738	27	(10)	(48,759)	8,384	25,357	NM	202
Union Bank	26,261	26,015	26,686	2	3	20,888	17,302	17,890	(14)	3	1,295	(33,692)	(8,212)	(734)	NM
Old private banks															
City Union Bank	3,748	4,206	4,223	13	0	2,994	3,378	3,374	13	(0)	1,616	1,751	1,829	13	4
Federal Bank	9,801	10,965	11,067	13	1	6,029	7,548	6,851	14	(9)	2,627	3,815	3,461	32	(9)
Karur Vysya Bank	5,836	6,192	6,157	6	(1)	4,596	4,648	4,691	2	1	459	600	554	21	(8)
J&K Bank	7,792	9,313	9,159	18	(2)	3,498	6,006	3,863	10	(36)	526	2,148	641	22	(70)
New private banks															
Axis Bank	51,668	57,056	58,978	14	3	43,720	50,144	49,943	14	(0)	7,011	15,051	16,946	142	13
Bandhan Bank	10,372	12,575	13,862	34	10	8,205	11,532	11,189	36	(3)	4,817	6,509	6,271	30	(4)
DCB Bank	2,730	3,009	3,123	14	4	1,414	1,853	1,749	24	(6)	695	963	879	26	(9)
HDFC Bank	108,136	130,895	129,579	20	(1)	86,478	108,436	106,904	24	(1)	46,014	58,851	55,140	20	(6)
ICICI Bank	61,019	76,201	72,519	19	(5)	58,084	62,334	61,943	7	(1)	(1,196)	9,691	13,931	NM	44
IndusInd Bank	21,224	22,324	27,716	31	24	19,111	20,677	22,655	19	10	10,357	3,601	9,498	(8)	164
RBL	5,527	7,387	7,534	36	2	4,323	5,600	5,550	28	(1)	1,900	2,472	2,502	32	1
Yes Bank	22,191	25,059	22,650	2	(10)	24,547	13,234	13,609	(45)	3	12,604	(15,066)	(5,786)	(146)	NM
Small finance banks															
AU	2,864	3,869	3,992	39	3	8,205	11,532	11,189	36	(3)	768	1,182	1,147	49	(3)
Equitas	2,544	3,331	3,568	40	7	761	1,263	1,370	80	8	354	687	663	87	(4)
Ujjivan	2,224	2,863	3,249	46	13	833	853	1,044	25	22	451	638	662	47	4
Total banks	691,478	758,471	774,441	12	2	514,748	592,623	582,507	13	(2)	40,239	4,659	125,796	213	2,600
Public banks	373,803	383,227	397,065	6	4	241,950	283,587	276,583	14	(2)	(48,766)	(88,234)	17,458	NM	NM
Private banks	317,675	375,244	377,376	19	1	272,798	309,036	305,924	12	(1)	89,005	92,893	108,338	22	17

Source: Company, Kotak Institutional Equities estimates

Exhibit 5: Strong recovery in profitability
Yoy growth in PAT, March fiscal year-ends, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Public banks					
Bank of Baroda	160	20	322	NM	80
Canara Bank	11.9	15.1	152.5	NM	0.5
PNB	(373.7)	(908.5)	7.1	NM	NM
State Bank of India	(343.1)	(40.3)	NM	NM	NM
Union Bank	11.1	NM	NM	NM	(734.0)
Old private banks					
City Union Bank	15.2	16.0	15.2	15.1	13.1
Federal Bank	25.0	0.9	28.1	163.1	31.7
Karur Vysya Bank	(69.0)	10.7	(70.3)	18.7	20.7
J&K Bank	74.9	30.9	43.2	656.1	21.8
New private banks					
Axis Bank	(46.3)	82.6	131.4	NM	141.7
Bandhan Bank	47.5	47.3	10.4	67.8	30.2
DCB Bank	6.6	24.7	51.0	50.0	26.5
HDFC Bank	18.2	20.6	20.3	22.6	19.8
ICICI Bank	(105.8)	(55.8)	(2.7)	(5.0)	NM
IndusInd Bank	23.8	4.6	5.2	(62.2)	(8.3)
RBL	34.8	35.8	36.2	38.8	31.7
Yes Bank	30.5	(3.8)	(7.0)	(227.7)	(145.9)
Small finance banks					
AU	24.3	33.9	20.8	42.4	49.3
Equitas	126.5	355.2	NM	96.6	87.3
Ujjivan	NM	NM	54.3	(1.5)	46.8
Total banks	**(69.1)**	**(31.9)**	**150.0**	**NM**	**212.6**
Public sector banks	**(266.9)**	**(321.9)**	**NM**	**NM**	**NM**
Private sector banks	**(12.0)**	**4.8**	**21.1**	**33.6**	**21.7**

Note:
1) "NM" indicates loss in the base quarter and profit in current quarter.

Source: Companies, Kotak Institutional Equities estimates

BANKS: SLOWDOWN IN LOAN GROWTH

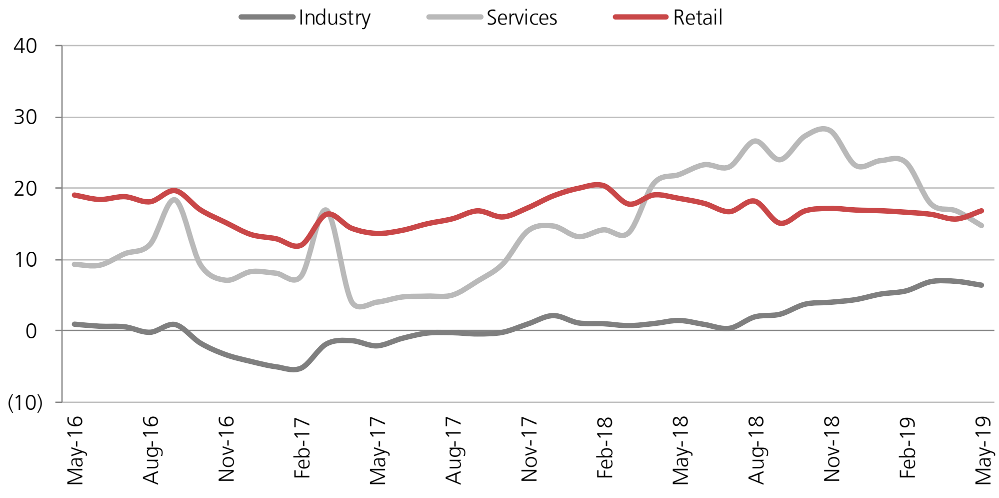
System loan growth has slowed down; Unsecured loan growth down to ~25% yoy in May 2019

As per the latest available data (May 2019) for the banking system, loan growth has slowed down to ~12% yoy, compared to 15% in 4QFY19. Muted increase in corporate loans, slowdown in retail unsecured credit and decrease in the sharp pace of growth in lending to NBFCs have led to subdued loan growth. Corporate loan growth is muted at marginally higher than 5% yoy, though it has shown signs of reversal at a slow pace. Lending to large industries is slightly higher. Most banks are focused on lending to better rated corporates. There however exists diversity in corporate lending across sectors with some segments like renewable energy attracting strong credit growth compared to others like iron and steel.

Retail loan growth has reduced from peak levels by ~100-200 bps. The pace of growth in unsecured retail credit has reduced to 25% from peak levels of ~35% observed during FY2019. The pace of growth in credit cards has seen a slight dip over the last few months. Housing loans have seen a modest upward push to 20% yoy. There has been a slowdown in lending towards secured products like auto and commercial vehicle financing mainly on low growth in the industry. Demand for commercial vehicles will likely pick pace over the next few months on account of pre-buying due to new BS-VI norms.

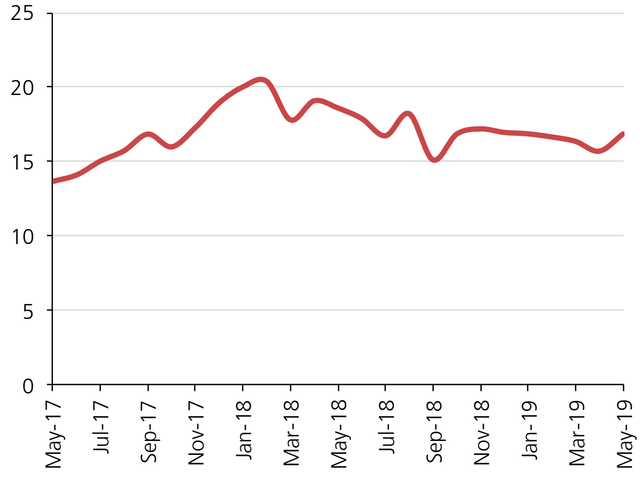
The relative tightening of liquidity resulted in an increase in the borrowing cost of alternative sources of borrowings like commercial papers and debentures. This made bank funding for NBFCs an important medium to maintain liquidity resulting in robust growth of lending to NBFCs at ~50% yoy in 2HFY19. Loan growth to NBFCs has reduced to 40% in May 2019.

Exhibit 6: Credit growth has slowed down in recent months
Yoy credit growth across industry, services and retail segments, March fiscal year-ends, May 2016- May 2019 (%)



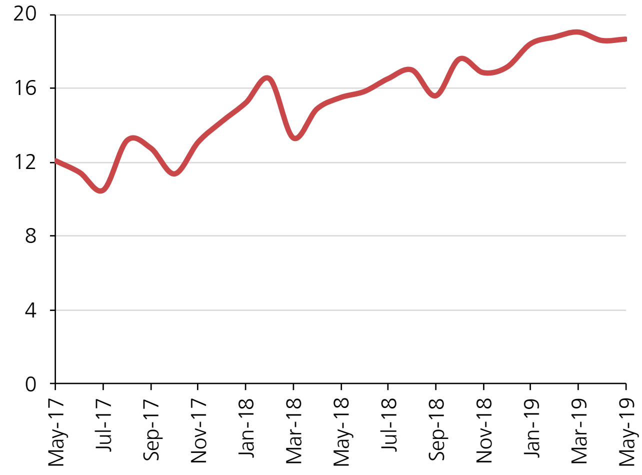
Source: RBI, Kotak Institutional Equities

Exhibit 7: Retail loan growth has started to moderate
Growth in retail loans, March fiscal year-ends, May 2017- May 2019 (%)



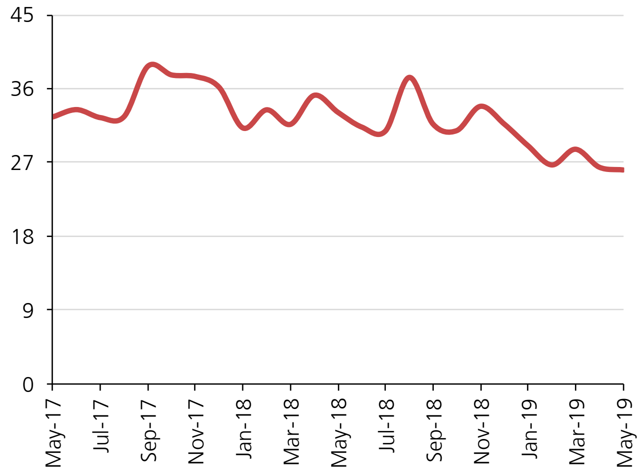
Source: RBI, Kotak Institutional Equities

Exhibit 8: Housing loans continue to show strong growth at 19% yoy
Growth in housing loans, March fiscal year-ends, May 2017- May 2019 (%)



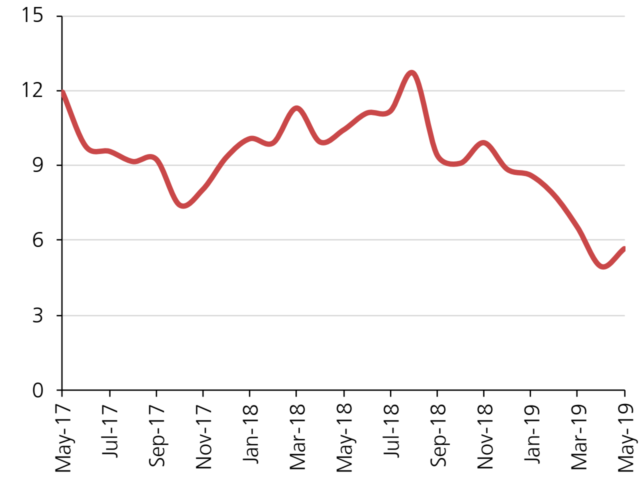
Source: RBI, Kotak Institutional Equities

Exhibit 9: Credit card loan growth has slowed down
Growth in credit card receivable, March fiscal year-ends, May 2017- May 2019 (%)



Source: RBI, Kotak Institutional Equities

Exhibit 10: Auto loans growth decelerates to ~5% yoy
Growth in vehicle loans, March fiscal year-ends, May 2017- May 2019 (%)



Source: RBI, Kotak Institutional Equities

Corporate loan growth remains muted. Corporate loan growth trends were broadly unchanged during the quarter as corporate loans increased at a tepid pace (marginally higher than 5% yoy growth) in May 2019 as per the latest RBI release. Corporate loans continue to increase albeit a slow pace. Slowdown in capex investments has led to lower fresh disbursements in the space. Rising slippages from the corporate book from 2HFY18 clubbed with lower disbursements led to muted loan growth in this segment. However, loan growth varies across segments in the corporate space. While lending to the overall infrastructure space remains low, fresh disbursements in the renewables space have increased. Most banks have increased focus towards lending to better rated corporates where the competition is relatively higher. The share of A+ and above rated loans in the overall corporate loan mix has increased over the last few quarters.

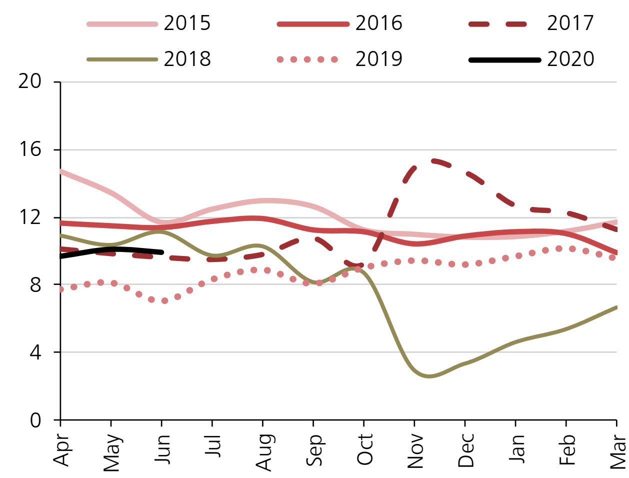
On the positive side we see a few new developments. Competition from alternate markets like commercial papers or debentures has weakened substantially which has led to an increase in bank funding for NBFCs. Loan growth in the service sector has seen a sharp rise with loans to NBFCs witnessing 40% yoy growth in May 2019. The pace of growth is slower than that witnessed during 2HFY19 (immediately post the crisis). Most NBFCs witnessed a 50-100 bps rise in incremental cost of market borrowings led by rising rates of CPs and NCDs and have reverted to bank borrowings to fuel growth.

Unsecured loan growth has slowed down. Retail loan growth at 17% yoy in April-May 2019 was broadly similar to that of the last few quarters. However, the pace of growth in unsecured loans has started to slow down to ~25% from 35% during FY2019. Housing loans have started to pick momentum post 2-3 quarters of sluggish growth from 2QFY18 onwards (up 20% yoy in May 2019). Rising cost of funds for HFCs leading to a slowdown in disbursements by smaller players and increasing sell down of loans by these players will further boost housing loans for banks in the near-term. Competition however continues to rise in the retail space as PSU banks have started to shift focus towards retail loans in the absence of corporate loan growth. Additionally, with some PSU banks moving out of the PCA framework, competition in the retail segment is expected to intensify further.

We expect retail loan growth to witness a period of slowdown over the next few months in select segments. As per our discussion with TransUnion CIBIL, loan inquiries have declined in unsecured loans (remain high on absolute basis on a low base). The gradual slowdown in retail loans will lead to a drop in the pace of overall loan growth.

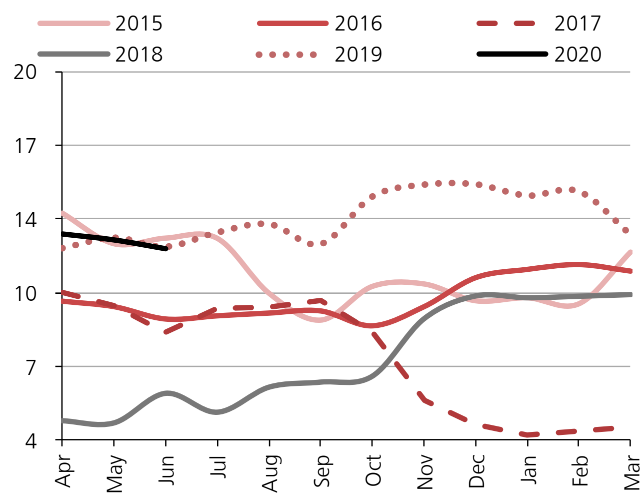
Small Finance Banks accelerate loan growth. Small Finance Banks will deliver robust AUM growth led by strong growth in the MFI space and pick up in business momentum in the new segments. MFI industry has seen strong growth at ~45% over the last two quarters. While Equitas saw a rapid decline in the MFI book post demonetization, MFI loans revived in 3QFY19. Asset quality in the MFI segment has been stable for banks over the last few quarters (PAR-30 stable at <1%). Collections efficiency continued to improve across most areas which were affected by demonetization. Cashless disbursements have also started to pick pace. Rise in other retail loans like housing and vehicle finance will further fuel growth for Small Finance Banks.

Exhibit 11: Deposits growth stable at 10% yoy
Yoy growth in deposits, March fiscal year-ends, 2015 – June 2019 (%)



Source: RBI, Kotak Institutional Equities

Exhibit 12: Loan growth has dropped to 12% yoy
Yoy growth in advances, March fiscal year-ends, 2015 – June 2019 (%)



Source: RBI, Kotak Institutional Equities

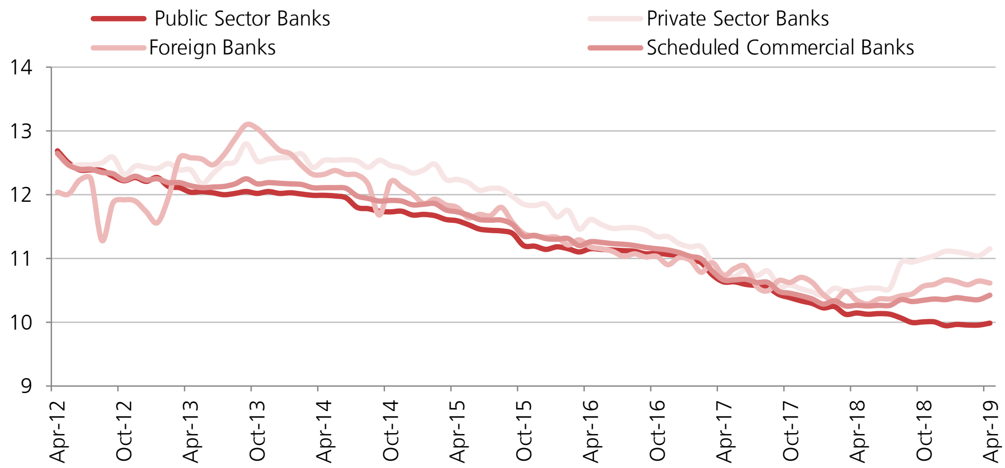
Deposit growth stable qoq at 10% yoy

Deposit growth at 10% yoy levels in 1QFY20 (similar to last two quarters) is broadly similar to pre-demonetization levels but still lags loan growth. CASA ratios will be broadly stable for most players in the absence of strong growth in CA. Retail TDs will likely grow at a swift pace. Most banks have, however, marginally reduced their term deposit rates in recent months. Weighted average term deposit rates are stable over the past seven months. Historically, the correlation between the rise in term deposit rates and growth in term deposits has been positive, although weak. The main challenge remains in the structure of the deposits and lending markets where the shift in market share on deposits has been slower for private banks as compared to loans, especially large ticket corporate loans.

Broadly stable margins sequentially

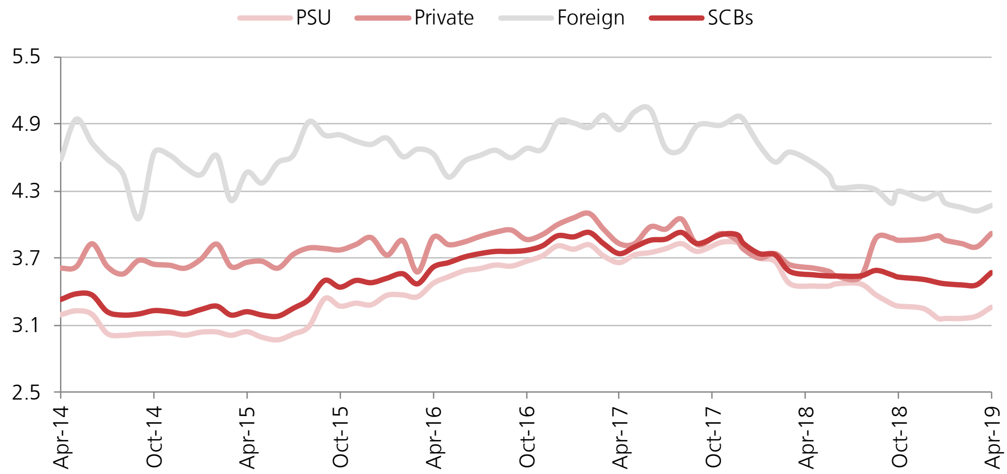
We forecast NIM (calculated) to be stable for most banks. Most banks have decreased MCLR rates in May-June 2019. Additionally, share of high yielding unsecured loans has decreased. This will likely lead to pressure on margins. Drop in TD rates over the same period will likely offset the impact leading to stable qoq margins. Going ahead, NIM will be an interplay of (1) drop in interest reversals, (2) revival in loan growth, (3) one-off interest recognition from select accounts resolved under various resolution schemes and (4) increase in share of retail loans in the overall loan mix. As such, we expect NIM expansion for select corporate banks like ICICI, Axis and SBI over the medium-term.

Exhibit 13: Weighted average lending rates have marginally inched up
Bank group-wise weighted average lending rates, April 2012 – April 2019 (%)



Source: RBI, Kotak Institutional Equities

Exhibit 14: Spread between lending and term deposit rates is stable at 350 bps
Bank group-wise spread between weighted average lending and weighted average term deposit rates, April 2014 – April 2019 (%)



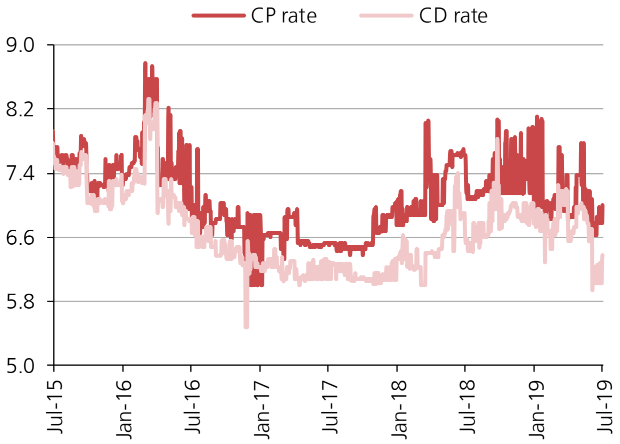
Source: RBI, Kotak Institutional Equities

Exhibit 15: NII growth to accelerate further for corporate banks
YoY growth in NII, March fiscal year-ends, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Public banks					
Bank of Baroda	28.7	20.8	7.9	26.6	54.5
Canara Bank	43.1	17.9	3.7	17.2	(13.1)
PNB	21.7	(1.0)	7.6	37.1	(6.8)
State Bank of India	23.8	12.5	21.4	14.9	3.3
Union Bank	17.1	7.4	(2.1)	18.6	1.6
Old private banks					
City Union Bank	9.5	12.2	14.5	14.3	12.7
Federal Bank	22.4	13.7	13.4	17.5	12.9
Karur Vysya Bank	8.4	4.3	3.4	(3.7)	5.5
J&K Bank	9.4	9.6	13.0	42.0	17.5
New private banks					
Axis Bank	11.9	15.3	18.4	20.6	14.1
Bandhan Bank	39.5	55.3	53.6	45.6	33.7
DCB	17.1	13.6	17.2	14.1	14.4
HDFC Bank	15.4	20.6	21.9	22.8	19.8
ICICI Bank	9.2	12.4	20.5	26.5	18.8
IndusInd Bank	19.6	21.0	20.8	11.2	30.6
RBL	46.1	41.1	40.2	47.6	36.3
Yes Bank	22.7	28.2	41.2	16.3	2.1
Small finance banks					
AU	56.1	46.1	39.0	34.9	39.4
Equitas	17.9	21.7	37.2	34.0	40.2
Ujjivan	60.9	45.4	30.2	35.8	46.1
Total	19.9	14.4	18.2	20.8	12.0
Public banks	25.3	11.8	14.2	18.9	6.2
Private banks	14.1	17.2	22.7	22.8	18.8

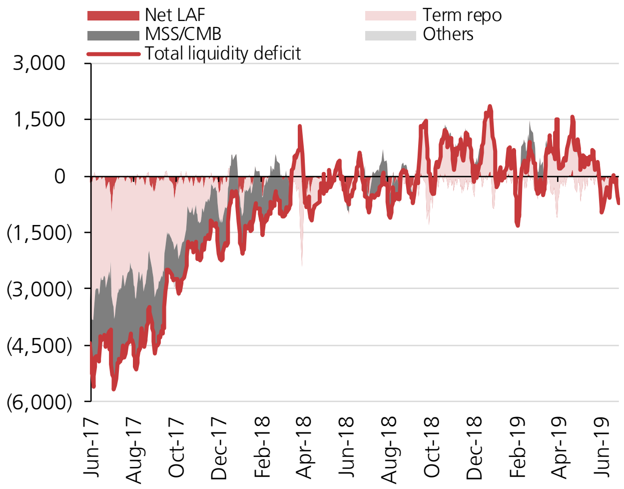
Source: Company, Kotak Institutional Equities estimates

Exhibit 16: CP and CD rates declined in 1QFY20
CP and CD rates, June 2015- June 2019 (%)



Source: Bloomberg, Kotak Institutional Equities

Exhibit 17: Liquidity surplus in recent months
Liquidity basket, June 2017-June 2019 (₹ bn)



Source: Bloomberg, RBI, Kotak Institutional Equities

Exhibit 18: SBI's MCLR rates were down 10 bps qoq in 1QFY20
SBI MCLR rates, June 2017–June 2019 (%)

	Jun-17	Sep-17	Jan-18	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	May-19	Jun-19
Overnight	7.75	7.75	7.70	7.80	7.90	8.10	8.20	8.20	8.10	8.10
One month	7.85	7.85	7.80	7.80	7.90	8.10	8.20	8.20	8.10	8.10
Three month	7.90	7.90	7.85	7.85	7.95	8.15	8.25	8.25	8.15	8.15
Six month	7.95	7.95	7.90	8.00	8.10	8.30	8.40	8.40	8.30	8.30
One year	8.00	8.00	7.95	8.15	8.25	8.45	8.55	8.55	8.45	8.45
Two years	8.10	8.10	8.05	8.25	8.35	8.55	8.65	8.65	8.55	8.55
Three years	8.15	8.15	8.10	8.35	8.45	8.65	8.75	8.75	8.65	8.65

Source: Company, Kotak Institutional Equities

Improvement in treasury income will drive non-interest income

Non-interest income will grow at a modest pace in 1QFY20 driven by improvement in treasury income and revival in pace of growth of fee income. Growth in fee income will moderate due to increasing competition in the retail space and muted activity on the corporate side. Retail fee income (mostly card related) will drive growth in fees apart from the sale of third party products. Income from recovery of written-off loans in 1QFY20 will be lower than 2HFY19 owing to the slowdown of resolution of lumpy stressed accounts under NCLT.

Exhibit 19: Improvement in treasury income to support earnings
Growth in treasury income, March fiscal year-ends, 1QFY19–1QFY20E (%)

	Income from treasury (Rs mn)					Income from treasury (% of PBT)				
	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Public banks										
Bank of Baroda	1,050	870	3,820	4,160	5,000	13	13	51	NM	37
Canara Bank	610	70	920	2,420	5,333	17	NM	24	NM	119
PNB	2,320	1,890	4,190	2,520	4,200	NM	NM	121	NM	NM
State Bank of India	(83,620)	(4,210)	84,190	21,490	13,750	NM	(45)	213	256	54
Union Bank	1,940	820	1,100	1,880	2,422	NM	70	83	NM	NM
Old private banks										
City Union Bank	193	213	208	256	306	9	9	9	10	12
Federal Bank	490	510	550	740	567	12	12	11	13	11
Karur Vysya Bank	70	(210)	270	570	350	19	(14)	110	51	43
J&K Bank	92	(259)	108	2,190	100	10	(15)	6	98	11
New private banks										
Axis Bank	1,030	1,360	3,790	3,540	3,000	10	12	15	15	12
DCB Bank	153	31	112	90	143	15	3	10	7	9
HDFC Bank	(2,832)	(328)	4,740	2,289	4,167	(4)	(0)	6	3	5
ICICI Bank	7,660	(350)	4,790	1,560	4,250	NM	(3)	25	20	27
IndusInd Bank	1,370	990	2,030	1,400	1,100	9	7	13	28	8
RBL Bank	370	81	277	205	275	13	3	8	6	7
Yes Bank	1,700	820	(592)	50	813	9	6	(4)	NM	NM
Total	**(68,249)**	**2,044**	**109,367**	**41,604**	**44,453**	**(109)**	**3**	**50**	**NM**	**30**
Public banks	**(77,700)**	**(560)**	**94,220**	**32,470**	**30,706**	**NM**	**NM**	**170**	**NM**	**233**
Private banks	**9,451**	**2,604**	**15,147**	**9,134**	**13,747**	**8**	**2**	**9**	**9**	**10**

Note:
1) "NM" indicates PBT loss in the quarter.

Source: Companies, Kotak Institutional Equities estimates

Exhibit 20: Short-term yields have declined
Yield of 1-year G-Sec, July 2013- July 2019 (%)

Source: Bloomberg, Kotak Institutional Equities

Exhibit 21: Long-term yields declined in 1QFY20
Yield of 10-year G-Sec, July 2013- July 2019 (%)

Source: Bloomberg, Kotak Institutional Equities

Asset quality will improve further

Slippages are expected to normalize going ahead as most of the corporate sector stressed assets have broadly been recognized in FY2019. Most of the restructured assets (including restructuring under various RBI dispensations) have slipped into NPLs. As we have highlighted in our previous notes, early warning indicators and SMA-0/1/2 trends do not indicate build-up of stress in any specific sector. As such slippages are expected to normalize going ahead. While slippages from the corporate sector will be lower, slippages from agriculture and SME segments might see a modest increase in the quarter. MFI slippages will likely increase from cyclone affected areas of Odisha.

Credit cost will decline in 1QFY20 as most banks have sufficiently provided for select stressed accounts under NCLT or other resolution schemes and incremental provision will mostly be ageing related. Most banks maintain comfortable coverage of >75% on accounts under NCLT-1 and 2.

Exhibit 22: Provision coverage ratios improved in 4QFY19
Calculated provision coverage ratio, 4QFY18-4QFY19 (%)

	Exc write-off					Inc write-off				
	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19
Public banks										
BoB	58.4	59.9	61.8	64.0	67.6	67.2	69.1	70.8	73.5	78.7
Canara	39.9	40.2	40.8	40.4	41.5	58.1	60.7	61.4	62.5	68.1
PNB	43.8	47.1	52.9	54.1	61.7	58.4	61.8	66.9	68.9	74.5
SBI	50.4	53.4	53.9	56.9	61.9	66.2	69.3	70.7	74.6	78.7
Union	50.7	50.0	50.8	51.4	58.3	57.2	56.5	57.7	58.8	66.2
Old private banks										
City Union Bank	44.6	44.4	41.3	40.8	39.5	64.0	65.0	65.0	65.0	63.0
Federal Bank	44.5	43.5	43.6	45.9	50.1	65.0	64.7	63.4	64.2	67.0
Karur Vysya Bank	38.2	41.4	44.7	43.4	45.6	56.5	56.5	58.5	56.1	56.9
J&K Bank	53.5	55.4	59.0	55.5	47.9	65.8	66.8	69.5	65.8	64.3
New private banks										
Axis Bank	51.6	54.4	58.9	60.4	62.1					
DCB	60.2	61.6	62.1	63.3	65.1					
HDFC Bank	69.8	69.5	70.0	69.7	71.4					
ICICI Bank	48.4	54.8	59.5	68.4	70.7					
Yes	50.0	55.3	47.8	44.2	43.1					
RBL	44.3	46.4	47.1	47.8	50.0					
IndusInd Bank	56.3	56.2	55.8	47.7	43.0					

Source: Company, Kotak Institutional Equities

Exhibit 23: Restructured loans and net NPLs to total loans are at ~4% for public banks, ~3% for private banks

Restructured loans and net NPLs, March fiscal year-ends, 4QFY18-4QFY19 (%)

	Restructured loans (%)					Net NPLs (%)					Net NPL and restructured loans (%)				
	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19
Public banks															
BoB	1.3	NA	NA	NA	NA	5.5	5.4	4.9	4.3	3.3	6.8	NA	NA	NA	NA
Canara	1.0	1.1	1.0	0.9	1.0	7.5	6.9	6.5	6.4	5.4	8.5	8.0	7.5	7.3	6.4
PNB	1.2	0.9	0.2	0.2	0.2	11.2	10.6	8.9	8.2	6.6	12.4	11.5	9.1	8.4	6.7
SBI	0.3	NA	NA	NA	NA	5.7	5.3	4.8	4.0	3.0	6.0	NA	NA	NA	NA
Union	0.4	0.3	0.4	0.4	0.4	8.4	8.7	8.4	8.3	6.9	8.8	9.0	8.8	8.6	7.3
Old private banks															
City Union	0.0	0.0	0.0	0.0	0.2	1.7	1.7	1.7	1.7	1.8	1.7	1.7	1.7	1.7	2.0
Federal	0.9	0.6	0.6	0.6	0.5	1.7	1.7	1.8	1.7	1.5	2.6	2.3	2.4	2.3	2.0
Karur Vysya	0.6	0.1	0.1	0.0	0.1	4.2	4.5	4.4	5.0	5.0	4.7	4.6	4.5	5.0	5.1
J&K	8.2	6.9	6.2	5.8	4.9	4.9	4.7	3.9	4.7	4.9	13.1	11.6	10.1	10.5	9.8
Private															
Axis	0.2	0.2	0.2	0.1	0.2	3.4	3.1	2.5	2.4	2.1	3.6	3.3	2.7	2.5	2.2
DCB	NA	NA	NA	NA	0.1	0.7	0.7	0.7	0.7	0.7	NA	NA	NA	NA	0.7
HDFC Bank	0.0	NA	NA	NA	NA	0.4	0.4	0.4	0.4	0.4	0.4	NA	NA	NA	NA
ICICI	0.3	0.3	0.3	0.1	0.1	5.4	4.7	4.1	2.9	2.3	5.7	5.0	4.3	3.0	2.4
IndusInd	0.1	0.0	0.1	0.1	0.1	0.5	0.5	0.5	0.6	1.2	0.6	0.6	0.6	0.7	1.3
RBL	0.1	0.1	0.1	0.1	0.0	0.8	0.8	0.7	0.7	0.7	0.9	0.9	0.8	0.8	0.7
Yes	0.0	0.0	0.1	0.1	0.1	0.6	0.6	0.8	1.2	1.9	0.7	0.6	0.9	1.3	1.9
Total	0.7	0.7	0.5	0.5	0.4	4.8	4.4	4.0	3.5	2.9	5.4	5.1	4.5	4.0	3.3
Public banks	0.6	0.8	0.5	0.5	0.5	6.4	6.0	5.5	4.8	3.8	7.0	6.8	6.0	5.3	4.3
Private banks	0.5	0.6	0.6	0.5	0.4	2.3	2.1	1.8	1.6	1.5	2.8	2.6	2.4	2.1	1.9

Source: Company, Kotak Institutional Equities

Exhibit 24: Credit cost to moderate going ahead

Credit cost of banks, March fiscal year-ends, 1QFY19-1QFY20E (Rs mn)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Public banks					
Bank of Baroda	1.7	1.4	3.0	4.7	2.0
Canara Bank	2.4	2.4	2.6	4.8	2.2
Punjab National Bank	4.8	7.2	2.4	8.0	4.1
State Bank of India	2.8	2.1	2.7	3.2	2.1
Union Bank	2.2	1.9	2.7	7.0	3.6
Old private banks					
City Union Bank	1.0	0.6	1.0	0.9	1.0
Federal Bank	0.7	0.7	0.8	0.6	0.5
Karur Vysya Bank	3.2	1.8	3.6	2.2	3.0
J&K Bank	1.6	0.8	1.5	2.4	1.7
New private banks					
Axis Bank	2.8	2.4	2.8	1.3	1.2
Bandhan	0.7	1.1	5.6	1.6	1.4
DCB	0.6	0.5	0.7	0.6	0.6
HDFC Bank	0.9	0.8	1.1	0.8	1.0
ICICI Bank	4.6	2.9	3.0	3.7	3.1
IndusInd Bank	0.6	1.2	1.3	4.3	1.6
RBL	1.0	1.0	1.2	1.2	1.0
Yes Bank	0.7	0.9	1.3	5.6	3.8
Small finance banks					
AU	0.6	0.3	0.4	0.3	0.3
Equitas	0.9	1.2	0.9	0.8	1.1
Ujjivan	0.8	0.3	0.3	0.4	0.5

Source: Companies, Kotak Institutional Equities estimates

DIVERSIFIED FINANCIALS: A MUTED QUARTER

1QFY20E was a muted quarter for most non-banks with weak loan growth, stable to compressed NIM even as asset quality held on well in most segments. Slowdown across autos, weakness in rural cash flows and delay in government spending led to muted performance in vehicle finance. Retail home loan sales were likely stable but slowdown in developer/LAP segment affected overall loan growth for HFCs. Asset quality performance was likely strong, in line with the trends observed over the previous few quarters. Rise in NPLs in the wholesale lending segment, especially developer loans, remains a major overhang on the sector. We hence expect NBFCs/HFCs to remain a bit cautious on liquidity and growth over the next few months; management commentary in this regard will be crucial.

Loan growth weak

Loan growth across most NBFCs (including HFCs) was weak expect Bajaj Finance. Seasonal trends suggest that 1Q is a weak quarter. Slowdown across segments of auto finance will likely affect disbursements and loan growth for auto finance NBFCs. Shriram Transport (on the back of weak CV sales), Mahindra Finance (reflecting weak rural demand), Chola and Magma will likely report 1-3% qoq loan growth. In housing finance, retail home loans disbursements were stable, if not strong, but wholesale business is almost on a standstill for most players. HFCs under coverage have a cautious call on the developer lending segment and will likely continue to go slow; this will bring down its overall loan growth. Rise in gold prices will boost growth for Muthoot Finance.

Mixed trends in NIM

Most NBFCs will likely reported stable to weak NIM. A couple of factors at play (1) rise in funding costs in 2HFY19 and moderation in bond yields thereafter, (2) rise in benchmark lending rates over the last few months – rate hikes have been incremental in vehicle finance while passed on the entire book in case of home loans; developer lending rates have increased significantly, (3) this was followed by reduction in lending rates in CVs and retail home loans over the last few months, (4) shifting portfolio towards higher-yield loans and (5) higher cash/liquid assets on balance sheet. In case of Mahindra Finance, rise in NPLs in 1Q also leads to lower NIM as the company does not recognize income on ECL. In this backdrop, it is challenging to forecast NIMs for the quarter. NIM for most NBFCs surprised in 4QFY19 due to effective transmission of rate hikes. Broadly, we expect stable NIM for most NBFCs as the rate hike and transmission has been effected. In case of home loans, a reduction in home loan rates, post these hikes, is already visible. On the other hand, the impact of rise in borrowings cost is yet to be fully reflected for Shriram twins and Magma.

Focus on liquidity

While liquidity was not a constraint for most part of the quarter, concerns on impact of defaults and rating downgrades of NBFCs raised some anxieties and likely prompted NBFCs to get a bit cautious. NBFCs are better placed to face any potential liquidity or credit crises (than August 2018) due to well matched ALMs and higher cash/liquidly assets on balance sheet. NBFCs have made conscious efforts to diversify its funding sources like foreign bonds, retail NCDs etc; rise in loan securitization/assignment has also been a significant avenue.

Asset quality on track

Our discussion with industry participants suggests that loan recoveries remained strong; this has been the key area of focus by NBFCs over the last three quarters while new business was weak. Seasonally, 1Q tends to be a weak quarter and hence there may be a qoq rise in NPLs. However, the medium-term trend of improvement in asset quality may be extrapolated. Slowdown in infrastructure spending and cash strain pre-elections affected collections in April, recoveries likely bounced back in May. Concerns on droughts and weak rural cash flows emerged in June and will likely lead to rise in GNPLs for Mahindra Finance and other rural players. The key concern for the sector has been GNPLs trajectory in the developer lending segment. In this backdrop, a rise in retail NPLs, albeit marginal, may not be ruled out.

Exhibit 25: Mixed trends in earnings growth for NBFCs/HFCs in 1QFY20E
Quarterly trends in yoy PAT growth, March fiscal year-ends, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Bajaj Finance	81	54	54	57	55
Cholamandalam	37	48	39	2	14
HDFC	54	25	(60)	27	50
IIFL Finance	66	73	8	73	(48)
LICHF	36	12	26	17	21
L&T Finance (lending)	48	67	58	49	14
Magma Finance	75	5	65	7	6
Mahindra Finance	34	133	(20)	87	11
Muthoot Finance	43	9	1	1	18
PNBHF	50	33	32	51	32
Shriram Transport	25	23	17	(22)	15
Shriram City Union Finance	15	6	2	1,008	15

Note:
(1) All numbers are based on Ind-AS

Source: Company, Kotak Institutional Equities estimates

Exhibit 26: Most NBFCs/HFCs to witness moderate growth in core PBT in 1QFY20E
Quarterly trends in yoy core PBT growth, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Bajaj Finance	82	55	54	58	53
Cholamandalam	36	48	37	7	14
HDFC	21	15	16	20	14
IIFL Finance	68	69	13	59	(48)
LICHF	33	17	20	21	25
L&T Finance (lending)	75	127	72	64	19
Magma Finance	637	15	102	2	19
Mahindra Finance	38	122	(14)	74	10
Muthoot Finance	39	1	5	(3)	20
PNBHF	53	35	31	44	31
Shriram Transport	25	24	18	(29)	32
Shriram City Union Finance	15	4	1	929	15

Note:
(1) All numbers are based on Ind-AS

Source: Company, Kotak Institutional Equities estimates

Exhibit 27: QoQ loan growth weak
Quarterly trends in qoq core PBT growth, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Bajaj Finance	13	8	10	5	10
Cholamandalam	6	5	6	8	3
HDFC	4	3	3	5	5
IIFL Finance	8	9	1	7	2
LICHF	1	4	3	7	3
L&T Finance (lending)	2	6	4	5	(0)
Magma Finance	1	4	(1)	3	2
Mahindra Finance	11	1	6	6	3
Muthoot Finance	6	4	0	5	8
PNBHF	10	7	9	6	3
Shriram Transport	4	4	(1)	1	2
Shriram City Union Finance	6	2	(4)	3	6

Source: Company, Kotak Institutional Equities estimates

Exhibit 28: YoY loan growth lower than 4QFY19 for most
Quarterly trends in yoy loan growth, March fiscal year-ends, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Bajaj Finance	35	38	41	41	37
Cholamandalam	30	31	29	26	23
HDFC	18	17	15	15	16
IIFL Finance	44	40	37	29	21
LICHF	15	16	16	16	19
L&T Finance (lending)	26	26	23	17	15
Magma Finance	3	6	6	8	9
Mahindra Finance	21	26	30	27	18
Muthoot Finance	11	17	15	18	19
PNBHF	47	43	38	36	27
Shriram Transport	22	21	14	9	6
Shriram City Union Finance	20	18	9	7	7

Note:
(1) All numbers are based on Ind-AS

Source: Company, Kotak Institutional Equities estimates

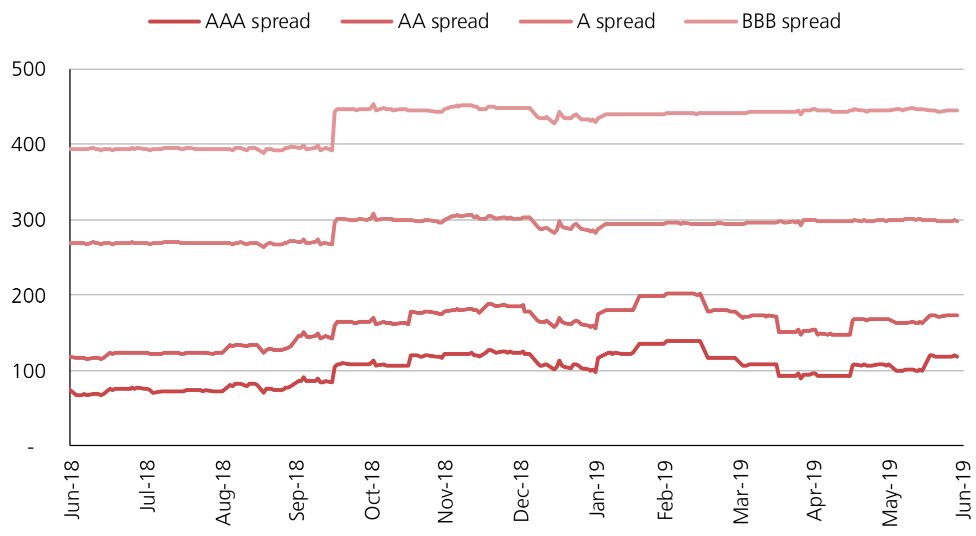
Exhibit 29: NIM (calculated) roughly flat qoq
Quarterly trends in NIM, March fiscal year-ends, 1QFY19-1QFY20E (%)

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20E
Bajaj Finance	10.1	9.6	9.9	9.7	9.8
Cholamandalam	7.4	7.0	7.1	6.9	6.8
HDFC	2.7	2.5	2.6	2.8	2.6
IIFL Finance	7.4	6.8	6.8	8.3	8.3
L&T Finance Holdings	5.0	5.2	5.6	5.4	5.7
LIC Housing Finance	2.4	2.4	2.4	2.6	2.5
Magma Finance	8.1	8.6	8.2	7.8	7.8
Mahindra Finance	7.6	7.9	7.9	8.1	7.9
Muthoot Finance	14.8	13.9	13.5	14.6	14.7
PNB Housing Finance	2.8	2.3	2.1	2.6	2.6
Shriam City Union Finance	13.2	13.9	12.5	12.9	12.8
Shriram Transport Finance	7.5	8.0	7.8	7.3	7.2

Note:
(1) All numbers are based on Ind-AS

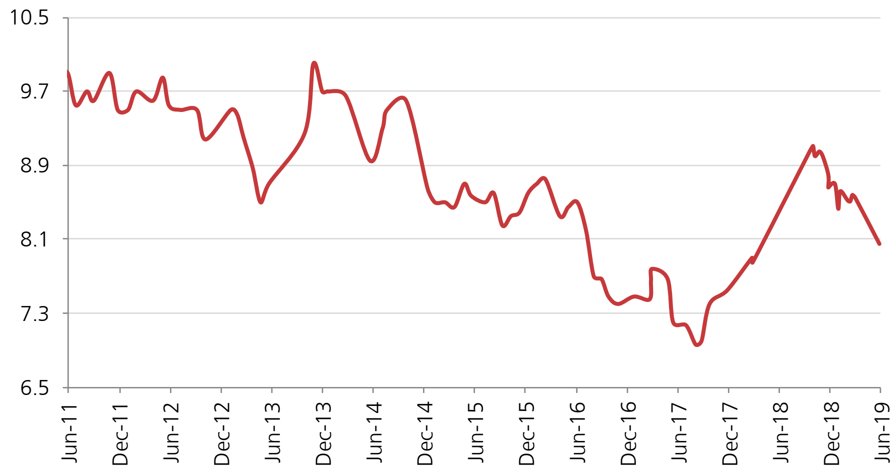
Source: Company, Kotak Institutional Equities estimates

Exhibit 30: Credit spreads haven't normalized after the October 2018 spike
India 5-year corporate bond spreads to G-Secs, June 2018-June 2019, (bps)



Source: Company, Bloomberg, Kotak Institutional Equities

Exhibit 31: Bond borrowings rates have declined in 1QFY20
HDFC –Yields on 1-10 year bonds, May 2011- May 2019 (%)



Source: Prime Database, Bloomberg

Exhibit 32: Most NBFCs have a significant share of borrowings from banks
Composition of borrowings, March fiscal year-ends, 4QFY17-4QFY19 (% of total)

	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19
HDFC	3,197,160	3,325,260	3,406,360	3,547,280	3,652,660
Term loans	15	16	18	21	21
Bonds/ debenture/ CPs	57	54	54	49	50
Deposits	29	30	28	30	29
LICHF	1,453,390	1,477,350	1,544,510	1,602,910	1,706,290
Bank	10	12	16	14	15
NCDs	79	74	68	74	75
Tier-II	2	2	1	1	1
Deposit	5	5	4	5	4
NHB	1	1	1	1	1
CP and others	3	7	9	5	4
PNBHF	542,683	604,400	636,268	691,660	723,620
Banks	8	18	20	17	18
NCDs	38	37	33	30	28
Cp and others	17	17	12	11	10
Public deposit	19	19	18	17	17
ECB	2	3	2	6	6
NHB	7	6	5	7	8
Assignment	9	-	10	12	13
L&TFH					
Term loan	36	35	36	36	39
NCDs and Others	48	45	46	48	47
LOC/CC/WCL/STL	NA	NA	NA	NA	NA
CP	16	20	18	16	14
STFH	821,310	853,000	882,020	895,460	879,680
Public deposits	10	10	10	11	12
Term loans	23	21	22	21	21
CPs (incl embedded NCDs)	6	6	8	7	4
Subordinated debts	6	6	5	7	7
Securitization	21	22	19	20	20
Bonds	34	29	29	33	35
Other borrowings	1	6	6	2	2
SCUF	198,300	214,010	216,760	233,730	223,950
Retail	15	17	15	16	17
Bank borrowings	55	59	55	54	59
Market borrowings	30	24	30	30	24
Chola	382,930	409,800	470,610	472,340	505,670
Bank	39	36	39	39	49
CP	10	15	15	16	11
Debenture	25	27	26	25	21
Subordinated debt	26	22	20	20	19
Mahindra Finance					
Bank loans	30	30	31	31	28
NCDs	48	44	42	42	44
FDs	8	8	8	8	11
CP/ ICD	12	16	17	17	9
Securitisation/ assignment	2	1	2	2	8
Muthoot Finance					
Gold bonds	4	3	3	3	2
Listed NCDs	21	31	31	29	28
Bank loans	53	47	49	48	49
CPs	13	12	12	16	18
Subordinated debt	5	4	3	2	2
Others	4	3	3	2	2
Magma					
Banks	68	66	63	67	63
DCM	20	23	28	24	28
Others	12	10	9	9	9
Bajaj Finance					
Banks	31	30	34	32	34
NCDs	43	37	35	36	38
Subordinate debt	6	6	5	5	5
Deposits	12	14	15	14	15
CPs	6	12	9	11	7
CBLO	2	2	2	1	0

Source: Company, Kotak Institutional Equities

Exhibit 33: High CP/NCD redemptions of NBFC/HFCs in upcoming months
Schedule of CP/NCD redemptions of NBFC/HFCs to mutual funds, September 2018- May 2019 (Rs bn)

	Sep-18				Feb-19				Mar-19				Apr-19				May-19			
	CPs	NCDs	Total	(% of total)	CPs	NCDs	Total	% of total)	CPs	NCDs	Total	% of total)	CPs	NCDs	Total	% of total)	CPs	NCDs	Total	% of total)
Sep-18	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Oct-18	627	66	693	14	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Nov-18	1,109	62	1,171	23	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Dec-18	393	96	489	10	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Jan-19	75	43	118	2	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Feb-19	122	81	204	4	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Mar-19	37	167	204	4	623	211	835	19	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Apr-19	2	81	83	2	421	96	517	12	408	95	503	11	NA	NA	NA	NA	NA	NA	NA	NA
May-19	0	34	34	1	428	43	471	11	632	49	681	15	636	51	687	16	NA	NA	NA	NA
Jun-19	14	122	136	3	74	126	200	4	339	151	490	11	511	160	671	15	657	158	815	17
Jul-19	-	56	56	1	3	43	46	1	10	47	57	1	135	49	184	4	502	55	557	12
Aug-19	9	110	119	2	19	101	120	3	33	89	122	3	38	91	129	3	284	102	386	8
Sep-19	-	117	117	2	22	106	128	3	49	107	157	3	53	111	164	4	60	111	171	4
Oct-19	-	42	42	1	0	34	35	1	3	37	40	1	4	38	42	1	11	45	56	1
Nov-19	-	56	56	1	33	41	74	2	39	46	85	2	40	49	90	2	68	53	121	3
Dec-19	-	40	40	1	73	52	124	3	72	54	127	3	80	56	136	3	84	60	144	3
Jan-20	-	60	60	1	17	60	77	2	23	62	85	2	23	56	79	2	28	58	86	2
Feb-20	-	58	58	1	42	69	111	2	61	72	133	3	64	73	137	3	87	77	164	3
Total NBFC/HFCs	2,396	2,683	5,080	100	1,755	2,702	4,457	100	1,731	2,874	4,606	100	1,658	2,734	4,393	100	1,883	2,906	4,789	100

Source: ACE MF Database, Kotak Institutional Equities

Key highlights of 1QFY20E for non-banks under coverage

- **Bajaj Finance**. We expect loan growth to remain strong at 37% yoy, marginally lower than 41% in 4QFY19. NIM is likely to expand qoq by 10 bps to 9.8%, in line with seasonal trends. We expect cost-income ratio to improve to 55% from 57% qoq due to higher contribution of the consumer business. Trends in loan growth remains key monitorable.

- **Cholamandalam**. We expect loan growth to moderate to 23% from 26% on the back of slowdown in CVs. Competition in CV finance and high liquidity on balance sheet will put pressure on NIM although partially offset by falling funding costs. Credit cost is seasonally high in 1Q even as trends over the past few quarters were strong. Cost-to-income will likely remain elevated as the company continues to invest in new branches. Its loan growth guidance (cut to 15% for FY2020E in 4QFY19 earnings call) is crucial.

- **HDFC**. We expect HDFC to deliver 17% retail loan growth; this will drive 15% growth in overall loans. Pressure on retail home loan rates will likely lead to marginal compression in NIM to 2.6% (2.8% in 4QFY19). High PAT growth will be driven by capital gains of Rs19 bn from stake-sale in Gruh Finance. Trends in NPLs, in the backdrop of challenges in the developer lending segment, will be crucial to monitor.

- **ICICI Lombard**. We expect premium growth to remain muted at 7% yoy (6% in 2MFY20). Combined ratio will likely remain stable at 98%. We build in investment yield of 8% (7.9-8% in the past two quarters, 10.8% in 1QFY19). Its guidance on growth and loss ratio in the motor segment will be crucial.

- **IIFL Holdings/Finance**. We expect IIFL Finance's loan growth to be depressed at 2% qoq due to slowdown in the real estate business; loan book will be down 5% yoy due to sell-down of the CV business in 4QFY19. NIM (excluding one-offs) will likely remain stable qoq at 8.3%. Trends in loan growth and NPL in real estate book will be key sensitivity for the stock.

- **L&T Finance Holdings**. We expect LTFH's loan growth to moderate to 15% from 18% due to slowdown in wholesale loans. Strong growth in high-yield rural and real estate loans will likely boost NIM by 75 bps to 5.7%. Operating expenses ratio will likely remain stable qoq at 1.4% of loans. Trends in real estate and microfinance will be crucial to monitor.

- **LIC Housing Finance.** We expect loan growth to moderate to 3% qoq (19% yoy) from 7% qoq in 4QFY19 as non-housing segments slow down. NIMs will likely moderate 10 bps qoq to 2.5%, reflecting pressure on yields in the retail business. We expect GNPLs to increase qoq (key sensitivity for the stock) in line with seasonal trends; GNPLs have anyway been on an uptrend over the past few quarters.

- **Magma Fincorp.** We expect loan growth to remain muted at 9%, reflecting slowdown in vehicles sales, even as the housing finance business will likely remain strong. Rise in borrowing costs since 3QFY19 coupled with declining rates on CV loans will put pressure on NIM. Trends in collections will likely remain strong. Loan growth and early warning indicators are key to monitor.

- **Mahindra Finance.** Weakness in vehicle sales will lead to muted loan growth (3% qoq, down from 6% qoq in FY2019). Qoq rise in NPLs, in line with seasonal trends and fears of droughts in June, is likely to lead to 15 bps qoq compression in NIM to 7.9% even as falling bond yield and increase in vehicles finance lending rates will support incremental spreads. Provisions remain challenging to forecast for MMFS considering the qoq volatility in recoveries. Its guidance on growth and asset quality for FY2020E is crucial.

- **Muthoot Finance.** We expect Muthoot Finance to report strong (19% yoy and 8% qoq) growth in loan book on the back of 4% rise in gold prices. NIM is likely to remain stable qoq at 14.7%. Operating expenses ratio will likely remain stable yoy at 4.9%. GNPLs/provisions are likely to remain low supported by rising gold prices. Guidance on loan growth, in the backdrop of rising gold prices, is crucial.

- **PNB Housing Finance.** We expect PNBHF to deliver 27% yoy and 3% qoq growth (6% qoq growth in 4QFY19) due to slowdown in wholesale loans. Increase in benchmark lending rates will support calculated NIM to touch 2.6% (2.57% in 4QFY19 and 2.8% in 1QFY19). Provisions will likely remain high in line with seasonal trends; rise in NPLs/provisions in wholesale loans will remain key sensitivity to our estimates. Trends in wholesale book NPLs and NIM are crucial for the stock.

- **Shriram City Union Finance.** We expect SCUF to deliver 7% yoy loan growth (7% in 4QFY19) as the overall business environment remains weak. NIM will likely compress 15 bps qoq to reflect higher funding costs in 2HFY19. We expect recoveries to remain strong, leading to lower NPLs. Cost/AUM will likely remain stable qoq and yoy at 5%. Its guidance on NIM and loan growth will be crucial.

- **Shriram Transport Finance.** We expect STFC's loan growth to remain muted (6% yoy and 2% qoq, 1% qoq in 4QFY19) on the back of weak CV volumes. Rise in borrowing costs in 2HFY19 will lead to 15 bps qoq NIM compression to 7.2%. Recoveries are likely to remain strong. We expect cost/AUM ratio to moderate to 1.5% from 1.6% qoq. Growth guidance for FY2020E coupled with incremental funding costs will be crucial to monitor.

Exhibit 34: Key valuation metrics of banks and NBFCs
March fiscal year-ends, 2020E-2021E

	Reco.	Fair Value (Rs)	Price 3-Jul-19	Market cap. US $bn	EPS (Rs) 2020E	EPS (Rs) 2021E	PER (X) 2020E	PER (X) 2021E	ABVPS (Rs) 2020E	ABVPS (Rs) 2021E	APBR (X) 2020E	APBR (X) 2021E	RoE (%) 2020E	RoE (%) 2021E
Public banks														
Bank of Baroda	ADD	145	126	7.0	21	25	6.0	5.0	122	156	1.0	0.8	14.5	14.2
Canara Bank	ADD	315	288	3.1	53	72	5.5	4.0	328	420	0.9	0.7	10.4	12.7
PNB	ADD	105	81	5.4	9	14	8.6	5.9	61	78	1.3	1.0	9.9	12.7
SBI	BUY	410	366	47.4	37	51	10.0	7.1	214	279	1.7	1.3	13.8	16.6
Union Bank	ADD	105	84	2.1	9	21	9.3	3.9	74	117	1.1	0.7	6.3	13.7
Old private banks														
City Union Bank	ADD	215	213	2.3	11	12	19.9	17.8	68	77	3.1	2.8	15.3	15.1
Federal Bank	BUY	130	110	3.2	9	10	12.3	10.6	67	74	1.6	1.5	12.7	13.4
Karur Vysya Bank	ADD	85	70	0.8	4	9	18.0	8.1	65	73	1.1	1.0	4.8	10.1
J&K Bank	BUY	90	41	0.3	10	17	4.2	2.4	120	139	0.3	0.3	7.8	12.7
New private banks														
Axis Bank	REDUCE	730	806	30.6	46	55	17.5	14.5	283	336	2.8	2.4	16.4	16.7
Bandhan Bank	SELL	475	555	9.6	18	24	30.2	23.5	100	123	5.5	4.5	21.4	20.7
DCB Bank	BUY	230	231	1.0	13	17	17.3	13.8	100	114	2.3	2.0	13.5	14.9
IndusInd Bank	ADD	1,750	1,471	12.9	78	100	18.8	14.7	507	586	2.9	2.5	17.5	17.5
HDFC Bank	ADD	2,400	2,490	98.6	90	109	27.8	22.9	607	690	4.1	3.6	15.4	16.5
ICICI Bank	BUY	460	436	40.8	25	31	17.5	13.9	174	201	2.5	2.2	14.0	15.7
ICICI standalone		-	307	28.7	22	28	13.7	10.8	160	187	1.9	1.6	13.7	15.5
RBL Bank	SELL	560	652	4.0	30	37	21.9	17.9	194	222	3.4	2.9	15.7	16.8
Yes Bank	SELL	170	100	3.4	4	12	24.5	8.1	96	112	1.0	0.9	3.5	10.0
Small finance banks														
AU Small Finance Bank	SELL	500	696	3.0	16	23	42.3	30.2	139	162	5.0	4.3	13.2	14.8
Equitas	BUY	180	121	0.6	10	13	12.2	9.3	78	91	1.5	1.3	12.8	14.5
Ujjivan	ADD	375	298	0.5	23	30	12.7	9.9	178	203	1.7	1.5	13.7	15.6
NBFCs														
Bajaj Finance	SELL	2,500	3,715	31.3	92	122	40.6	30.5	422	530	8.8	7.0	24.0	25.6
Bajaj Finserv	REDUCE	7,250	8,430	19.5	307	384	27.4	21.9	1,829	2,194	4.6	3.8	18.3	19.1
Cholamandalam	ADD	295	292	3.3	18	21	16.4	13.9	94	113	3.1	2.6	20.5	20.3
HDFC	ADD	2,175	2,277	56.9	62	71	36.5	32.0	485	529	4.7	4.3	13.4	14.0
HDFC core			1,268	31.7	50	57	25.5	22.2	358	402	3.5	3.2	15.0	15.3
IIFL Holdings	REDUCE	185	146	0.7	15	18	9.9	8.3	125	137	1.2	1.1	12.3	13.5
LIC Hsg Fin	ADD	550	569	4.2	57	67	9.9	8.5	369	423	1.5	1.3	16.6	16.9
L&T Finance Holdings	REDUCE	140	120	3.5	13	15	9.3	8.2	79	92	1.5	1.3	18.0	17.2
Mahindra Finance	ADD	500	394	3.5	31	36	12.5	11.0	199	224	2.0	1.8	16.7	16.9
Muthoot Finance	ADD	625	637	3.7	54	60	11.9	10.7	283	326	2.3	2.0	20.3	19.6
PNB Housing Finance	REDUCE	700	777	1.9	69	77	11.3	10.1	506	569	1.5	1.4	14.5	14.4
Shriram City Union Finance	ADD	1,900	1,559	1.5	156	189	10.0	8.3	1,103	1,265	1.4	1.2	15.1	16.0
Shriram Transport	BUY	1,425	1,085	3.6	129	145	8.4	7.5	806	925	1.3	1.2	17.1	16.8

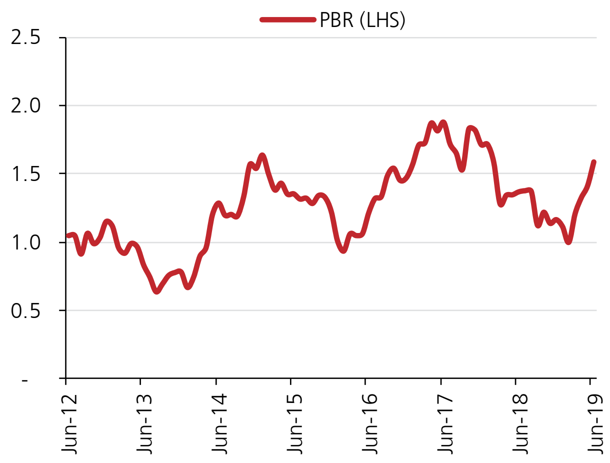
Source: Companies, Bloomberg, Kotak Institutional Equities estimates

Exhibit 35: BFSI stocks have underperformed the broader market in recent months
Stock price performance—absolute and relative (%)

	Change in price (%)					Relative performance to BSE-30 Index (%)					52 week high	52 week low
	1 month	3 month	6 month	12 month	Ytd	1 month	3 month	6 month	12 month	Ytd	(Rs)	(Rs)
Public banks												
Bank of Baroda	(4.6)	(5.0)	5.2	11.1	5.6	(3.5)	(7.3)	(6.2)	(1.4)	(4.4)	158	91
Canara Bank	5.7	0.9	4.1	17.6	4.6	6.7	(1.5)	(7.2)	4.4	(5.3)	302	205
Indian Bank	(10.0)	(5.7)	5.4	(23.7)	6.3	(8.9)	(8.0)	(6.0)	(32.3)	(3.8)	380	200
PNB	(1.0)	(14.0)	4.4	5.3	4.0	0.1	(16.1)	(7.0)	(6.5)	(5.8)	100	58
SBI	3.0	14.2	25.8	42.2	23.7	4.0	11.5	12.1	26.3	12.0	367	247
Union Bank	9.4	(11.7)	(5.6)	3.7	(2.5)	10.4	(13.8)	(15.9)	(7.9)	(11.7)	100	61
Old private banks												
City Union Bank	(0.3)	7.1	10.8	25.3	9.4	0.8	4.5	(1.3)	11.3	(0.9)	221	157
Federal Bank	2.0	15.3	19.3	31.8	17.7	3.1	12.6	6.4	17.1	6.6	110	67
Karur Vysya Bank	(12.3)	(4.6)	(23.2)	(24.9)	(21.1)	(11.1)	(6.9)	(31.6)	(33.3)	(28.6)	101	63
J&K Bank	(31.0)	(29.9)	4.9	(20.5)	7.7	(29.6)	(31.6)	(6.5)	(29.4)	(2.5)	66	33
New private banks												
Axis Bank	(0.8)	5.9	32.6	57.6	30.1	0.3	3.3	18.2	40.0	17.7	828	508
Bandhan Bank	(7.4)	0.9	4.0	(0.7)	1.0	(6.3)	(1.5)	(7.3)	(11.8)	(8.6)	742	368
DCB	(1.1)	15.7	37.0	38.6	36.3	(0.0)	12.9	22.1	23.1	23.4	245	140
IndusInd Bank	(11.6)	(17.1)	(5.7)	(24.6)	(8.0)	(10.4)	(19.1)	(16.0)	(33.1)	(16.8)	2,038	1,333
HDFC Bank	1.3	8.6	17.9	20.3	17.3	2.4	6.0	5.1	6.8	6.2	2,503	1,884
ICICI Bank	3.1	11.2	20.0	59.7	21.0	4.1	8.5	7.0	41.9	9.6	444	257
Yes Bank	(33.3)	(63.6)	(45.8)	(70.4)	(45.1)	(31.9)	(64.4)	(51.7)	(73.7)	(50.3)	404	99
Small finance banks												
AU Small Finance Bank	(0.1)	16.2	12.0	3.7	11.8	1.0	13.4	(0.2)	(7.9)	1.2	745	501
Equitas	(13.6)	(10.6)	(1.5)	(10.9)	(3.2)	(12.5)	(12.8)	(12.2)	(20.8)	(12.4)	163	78
Ujjivan	(17.8)	(9.8)	4.3	(22.1)	7.4	(16.6)	(12.0)	(7.0)	(30.8)	(2.8)	407	167
Non-banks												
Bajaj Finserv	1.0	13.9	32.1	43.2	30.2	2.0	11.2	17.7	27.2	17.8	8,575	4,955
Cholamandalam	(4.9)	(0.4)	21.4	(3.6)	15.7	(3.8)	(2.8)	8.2	(14.4)	4.8	324	208
Dewan housing	(26.5)	(43.8)	(64.7)	(86.7)	(66.7)	(25.2)	(45.2)	(68.5)	(88.2)	(69.8)	692	60
HDFC	2.1	13.1	17.6	21.1	15.7	3.1	10.4	4.8	7.6	4.7	2,287	1,645
IDFC	(6.0)	(20.3)	(14.3)	(21.9)	(16.9)	(4.9)	(22.3)	(23.6)	(30.6)	(24.7)	54	32
IIFL Holdings	(18.8)	(31.5)	(39.2)	(52.6)	(38.8)	(17.5)	(33.1)	(45.8)	(57.9)	(44.6)	358	136
LIC Housing Finance	1.7	4.7	20.9	20.3	16.3	2.7	2.2	7.8	6.8	5.3	584	388
L&T Finance Holdings	(12.2)	(21.4)	(17.8)	(19.1)	(21.7)	(44.9)	(67.5)	(73.1)	(84.5)	(74.5)	190	106
Magma Fincorp	0.6	9.5	22.2	(18.2)	20.1	1.6	6.9	8.9	(27.4)	8.8	168	81
MMFS	(9.4)	(5.5)	(13.9)	(15.1)	(16.7)	(8.3)	(7.8)	(23.3)	(24.6)	(24.6)	527	343
Muthoot Finance	(0.9)	4.5	28.5	64.0	23.4	0.2	2.0	14.5	45.6	11.7	657	356
PFC	4.6	11.4	26.0	80.9	24.4	4.6	11.4	26.0	80.9	24.4	139	68
REC	15.3	10.9	38.0	64.2	37.1	16.2	8.2	23.0	45.8	24.1	168	89
Shriram City Union Finance	0.6	(13.1)	(2.0)	(23.8)	(1.9)	1.7	(15.2)	(12.6)	(32.4)	(11.2)	2,139	1,301
Shriram Transport	(7.2)	(9.5)	(5.9)	(16.3)	(12.5)	(6.1)	(11.7)	(16.1)	(25.7)	(20.8)	1,477	902

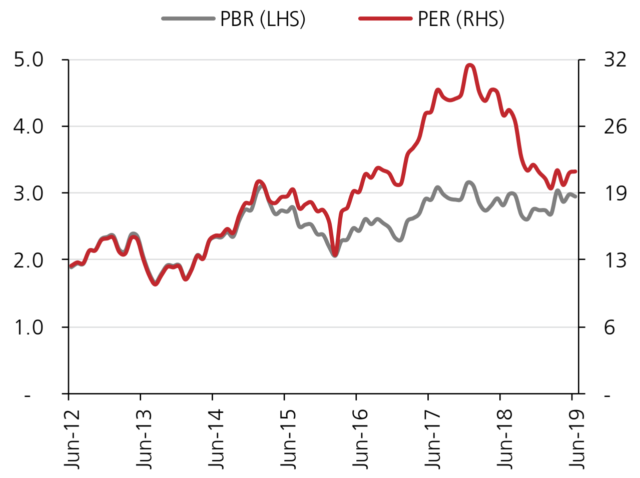
Source: Bloomberg

Exhibit 36: Public banks are trading at ~1.6X book (adj.)
Public banks – one-year forward PBR, June 2012- June 2019 (X)



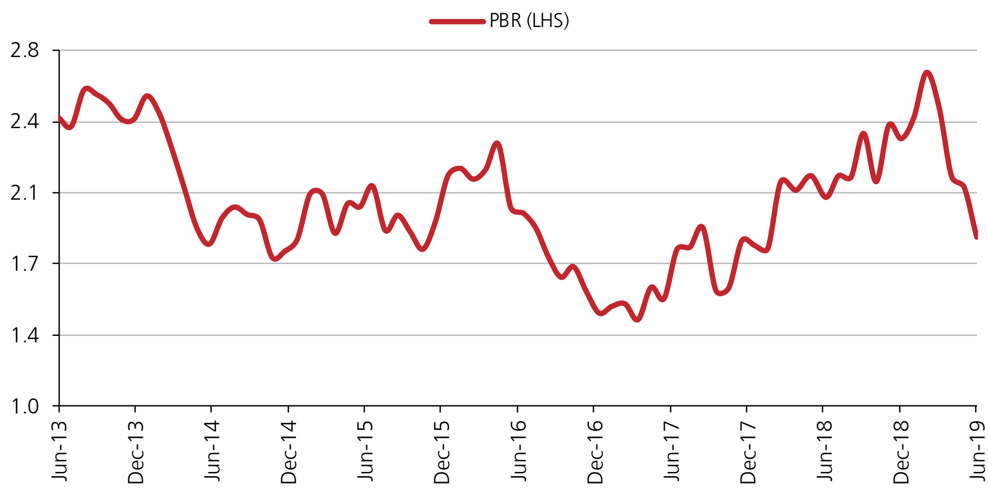
Source: Companies, Bloomberg, Kotak Institutional Equities estimates

Exhibit 37: Private banks are trading at 3X book (adj.)
Private banks – one-year forward PBR and PER, June 2012- June 2019 (X)



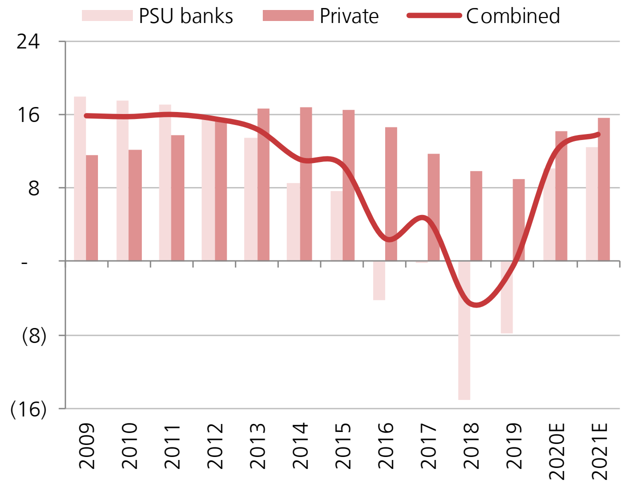
Source: Companies, Bloomberg, Kotak Institutional Equities estimates

Exhibit 38: Private banks' premium versus public banks continues steep decline
PBR (adj.) of private banks relative to public banks, June 2012- June 2019 (X)



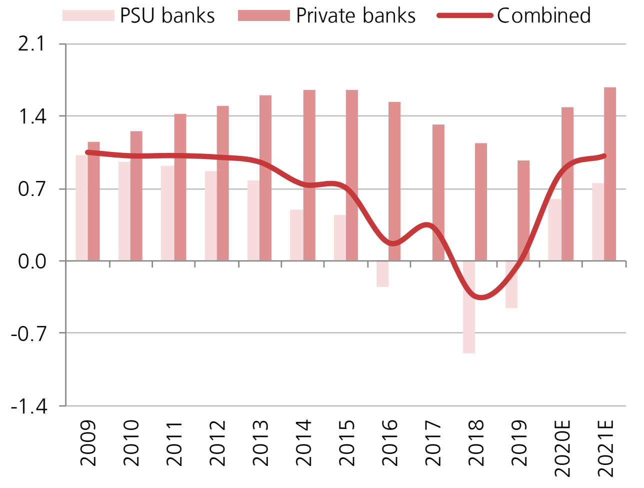
Source: Companies, Bloomberg, Kotak Institutional Equities estimates

Exhibit 39: RoEs likely to show improvement going ahead
RoE-public and private banks, March fiscal year-ends, 2009-2021E (%)



Source: Company, Kotak Institutional Equities estimates

Exhibit 40: RoAs likely to show improvement going ahead
RoA-public and private banks, March fiscal year-ends, 2009-2021E (%)



Source: Company, Kotak Institutional Equities estimates

Exhibit 41: Quarterly result expectation for companies under coverage

				Change (%)		
	Jun-18	Mar-19	Jun-19E	yoy	qoq	Comments
Banks/Diversified financials						
AU Small Finance Bank						
Net interest income	2,864	3,869	3,992	39.4	3.2	We expect AUM growth to remain strong at ~45% yoy and off balance sheet loans to decline further. There would be focus on the progress and NIM improvement as there has been revenue pressure in recent quarters due to change in loan mix and pricing.
Pre-provision profit	1,383	1,954	1,941	40.4	(0.7)	
Other income	1,031	1,306	1,340	30.0	2.6	
Loan-loss provisions	210	190	200	(5.0)	5.0	We expect cost-income ratio similar to 4QFY19 levels at ~60%. Liability side should see further improvement on deposit contribution but mix should be a bit more favorable on wholesale side. Gross NPL ratios should see a marginal increase qoq, especially on the retail side
Adjusted PAT	768	1,182	1,147	49.3	(3.0)	
EPS (Rs/share)	2.8	4.1	3.9	39.2	(5.2)	
NIM (%)	5.8	5.1	4.8	-101 bps	-37 bps	
Axis Bank						
Net interest income	51,668	57,056	58,978	14.1	3.4	We expect loan growth at 13% yoy with greater focus on retail. NIM at 3.5% (unchanged qoq but there is a positive bias as pricing environment has been favorable for banks).
Pre-provision profit	43,720	50,144	49,943	14.2	(0.4)	
Fee income	21,170	30,200	27,521	30.0	(8.9)	
Treasury income (net)	(320)	30	3,000	NM	9,900.0	
Loan-loss provisions	30,660	16,380	15,561	(49.2)	(5.0)	We expect slippages of Rs25 bn (2% of loans) mostly from "below investment grade book". Expect more traction on recovery as well from write-off pool. No major concerns on asset quality.
Adjusted PAT	7,011	15,051	16,946	141.7	12.6	
EPS (Rs/share)	3.0	6.4	7.2	141.7	12.6	
Bajaj Finance						
Net interest income	22,455	27,382	29,800	32.7	8.8	We expect loan growth to remain strong at 37% yoy, marginally lower than 41% in 4QFY19.
Pre-provision profit	16,241	22,209	24,410	50.3	9.9	
Loan-loss provisions	3,268	4,093	4,500	37.7	10.0	
Adjusted PAT	8,359	11,761	12,942	54.8	10.0	NIM will likely expand qoq by 10 bps to 9.8%, in line with seasonal trends; we expect cost-income ratio to improve to 55% from 57% qoq due to higher contribution of the consumer business.
EPS (Rs/share)	15.3	21.5	23.7	54.8	10.0	
Net interest margin (%)	10.1	9.7	9.8			
AUM (Rs bn)	933	1,159	1,278	37.0	10.3	
Bandhan Bank						
Net interest income	10,372	12,575	13,862	33.7	10.2	We expect loan growth at ~40% yoy resulting in strong revenue growth of ~32% yoy. NIM to be flat qoq at ~9.5% of AUM.
Pre-provision profit	8,158	11,532	11,156	36.8	(3.3)	
Fee income	1,485	2,879	1,856	25.0	(35.5)	
Loan-loss provisions	536	1,537	1,522	184.1	(1.0)	We expect stable trends on asset quality. Commentary on loan growth, borrower indebtedness in key markets along would be key monitorables.
Adjusted PAT	4,817	6,509	6,271	30.2	(3.7)	
EPS (Rs/share)	4.4	5.5	5.3	19.5	(3.7)	
Bank of Baroda						
Net interest income	43,811	50,670	67,703	54.5	33.6	This would be the first quarter with the merged financials of BoB, Vijaya and Dena Bank. The bank has given an opening balance sheet but the net worth for 1QFY20 would be closely watched. YoY changes are not comparable given the recent changes at the bank level.
Pre-provision profit	30,056	38,608	47,982	59.6	24.3	
Fee income	7,680	9,620	8,448	10.0	(12.2)	
Treasury income (net)	(3,830)	7,600	4,500	NM	(40.8)	
Loan-loss provisions	17,597	55,500	33,300	89.2	(40.0)	We expect fresh slippages at <2% as the balance sheet (post M&A) with negligible surprises from Vijaya or Dena Bank. Coverage ratio to improve qoq. Progress of the merger would be discussed.
Adjusted PAT	5,283	(9,914)	9,507	80.0	NM	
EPS (Rs/share)	10.0	(18.7)	17.9	80.0	NM	
Canara Bank						
Net interest income	38,829	35,002	33,736	(13.1)	(3.6)	We expect 10% yoy loan growth but ~10 bps qoq decline in NIM (one-off) to 2.4%. The base quarter has one-off interest income from recovery of a bad loan. We expect to see a higher contribution from treasury this quarter.
Pre-provision profit	29,328	29,735	27,907	(4.8)	(6.1)	
Fee income	3,460	2,960	3,463	0.1	17.0	
Treasury income (net)	(1,970)	(1,780)	5,223	NM	NM	
Loan-loss provisions	23,240	51,518	23,183	(0.2)	(55.0)	We expect slippages of ~2% of loans and mostly from non-corporate loans but NPL decline would be slower as there were no major resolutions during the quarter. Coverage ratio to improve qoq.
Adjusted PAT	2,815	(5,515)	2,830	0.5	NM	
EPS (Rs/share)	3.8	(7.3)	3.8	(2.1)	NM	
Cholamandalam						
Net interest income	8,190	8,990	9,353	14.2	4.0	We expect loan growth to moderate to 23% from 26% on the back of slowdown in CVs. Credit cost is seasonally high in 1Q.
Pre-provision profit	5,374	5,170	5,801	8.0	12.2	
Loan-loss provisions	980	560	800	(18.4)	42.9	
Adjusted PAT	2,854	2,920	3,251	13.9	11.3	
EPS (Rs/share)	18.2	18.7	20.8	14.0	11.3	
Net interest margin (%)	7.4	6.9	6.8			Competition in CV finance and high liquidity on balance sheet will put pressure on NIM.
AUM (Rs bn)	453	543	558	23.0	2.7	
Opex/AUM (%)	2.6	2.9	2.6	1.1	(11.6)	
City Union Bank						
Net interest income	3,748	4,206	4,223	12.7	0.4	We expect loan growth to slowdown to ~15% yoy for the quarter. NII growth to be marginally lower than loan growth at 13% yoy. NIM would decline ~10bps at 4.3%.
Pre-provision profit	2,994	3,378	3,374	12.7	(0.1)	
Fee income	759	777	835	10.0	7.5	
Treasury income (net)	48	256	306	536.9	19.4	
Loan-loss provisions	673	754	829	23.3	10.0	We expect gross NPLs at ~3% (higher qoq); slippages are expected at ~2.2% of loans, mostly from small ticket loans.
Adjusted PAT	1,616	1,751	1,829	13.1	4.4	
EPS (Rs/share)	2.4	2.4	2.5	2.4	4.4	
DCB Bank						
Net interest income	2,730	3,009	3,123	14.4	3.8	We expect revenue growth at 14% yoy on the back of 14% yoy NII growth and 17% yoy loan growth. NIM unchanged qoq but there is some easing of pressure (portfolio level) on product segments which compete with NBFCs. Cost of deposits to be stable qoq. Performance in LAP would be the key monitorable given rising NPLs at the sector level.
Pre-provision profit	1,414	1,853	1,749	23.7	(5.6)	
Fee income	626	846	738	17.8	(12.7)	
Treasury income (net)	153	90	143	(6.6)	58.8	
Loan-loss provisions	299	330	363	21.4	10.0	We expect PAT growth at 27% yoy led by operating leverage. RoE progression for FY2020 would be the key monitorable as the progress in FY2019 has been impressive.
Adjusted PAT	695	963	879	26.5	(8.8)	
EPS (Rs/share)	2.2	3.1	2.8	28.6	(7.4)	

Source: Company, Kotak Institutional Equities

Quarterly result expectation for companies under coverage

	Jun-18	Mar-19	Jun-19E	Change (%) yoy	qoq	Comments
Equitas Holdings						
Net interest income	2,544	3,331	3,568	40.2	7.1	We expect AUM growth of ~45% yoy led by SME and auto loans. NIM unchanged qoq at 9%. Operating expenses is likely to be flat yoy resulting in an improvement in cost-income ratio to ~65-68%. The progress on deposits would be a key monitorable.
Non-interest income	612	683	700	14.4	2.4	
Pre-provision profit	761	1,263	1,370	80.1	8.5	
Loan-loss provisions	209	249	350	67.5	40.7	We expect impairment ratios to show further improvement with gross NPLs <3% on the back of loans growth and normalised slippages trends. Progress on listing would be discussed as not much has happened since March 2019.
Adjusted PAT	354	687	663	87.3	(3.5)	
EPS (Rs/share)	1.0	2.0	1.9	86.6	(3.5)	
Federal Bank						
Net interest income	9,801	10,965	11,067	12.9	0.9	We expect loan growth to be slower-than-past few quarters at ~17% yoy though retail and SME business should see solid traction. NIM would be flat to marginally positive
Pre-provision profit	6,029	7,548	6,851	13.6	(9.2)	
Treasury income (net)	190	500	412	116.7	(17.7)	
Loan-loss provisions	1,662	1,530	1,377	(17.1)	(10.0)	We expect slippages at ~1.5% of loans though we await to see if there is further stress from Kerala floods. RoA progression for FY2020 would be a key monitorable.
Adjusted PAT	2,627	3,815	3,461	31.7	(9.3)	
EPS (Rs/share)	2.7	3.8	3.5	30.9	(9.3)	
HDFC						
Net interest income	27,367	31,611	30,835	12.7	(2.5)	We expect HDFC to deliver 17% retail loan growth; this will drive 15% growth in overall loans.
Capital gains + Dividends	5,859	8,579	18,960	223.6	121.0	
Pre-provision profit	30,897	40,889	49,335	59.7	20.7	
Adjusted PAT	21,900	28,616	32,772	49.6	14.5	Pressure on retail home loan rates will likely lead to marginal compression in NIM to 2.6% (2.8% in 4QFY19); high PAT growth will be driven by capital gains of Rs19 bn from stake sale in Gruh Finance.
EPS (Rs/share)	13.0	16.6	19.0	46.4	14.5	
Net interest margin (%)	2.7	2.8	2.6			
AUM (Rs bn)	3,720	4,619	4,860	30.6	5.2	
HDFC Bank						
Net interest income	108,136	130,895	129,579	19.8	(1.0)	We expect loan growth to slowdown to ~17% yoy led resulting in slower NII growth at ~20% yoy. Retail loan growth slowdown is on account of weak volume growth in auto and a more cautious approach towards unsecured loans. Fee income growth from MFs to be slower yoy due to changes in regulations while asset and payment fees to grow at a slower rate.
Pre-provision profit	86,478	108,436	106,904	23.6	(1.4)	
Fee income	31,710	36,921	37,101	17.0	0.5	
Treasury income (net)	(2,832)	2,289	4,167	NM	82.0	
Loan-loss provisions	16,154	16,224	20,002	23.8	23.3	We expect gross NPL ratio (1.5% of loans) which is a marginal increase qoq. Growth in credit costs, especially from rural loans, would be a key monitorable.
Adjusted PAT	46,014	58,851	55,140	19.8	(6.3)	
EPS (Rs/share)	17.7	21.6	20.2	14.6	(6.3)	
ICICI Bank						
Net interest income	61,019	76,201	72,519	18.8	(4.8)	We expect core earnings (base quarter had stake sale gains of ICICI Life) trajectory to remain strong at ~15% yoy led by healthy loan growth (~15% yoy) and better NII growth (19% yoy). NIM to decline qoq by ~10bps due to lower one-offs.
Pre-provision profit	58,084	62,334	61,943	6.6	(0.6)	
Fee income	27,540	31,780	31,946	16.0	0.5	
Treasury income (net)	7,660	1,560	4,250	(44.5)	172.4	We expect reduction in gross NPLs on the back of write-offs. Credit costs to show a decline qoq led by lower slippages (~<1.7% of loans, primarily from agriculture). Below investment grade portfolio to decline qoq and coverage ratio to improve qoq.
Loan-loss provisions	59,713	54,514	46,300	(22.5)	(15.1)	
Adjusted PAT	(1,196)	9,691	13,931	NM	43.8	
IIFL Finance						
Net interest income	5,144	6,935	5,558	8.1	(19.8)	We expect IIFL Finance's loan growth to be depressed at 2% qoq due to slowdown in the real estate business; loan book will be down 5% yoy due to sell-down of the CV business in 4QFY19.
Pre-provision profit	3,346	5,265	3,558	6.3	(32.4)	
Loan-loss provisions	345	1,774	2,000	479.7	12.7	
Adjusted PAT	1,949	2,586	1,013	(48.0)	(60.8)	NIM (excluding one-offs) will likely remain stable qoq at 8.3%.
EPS (Rs/share)	6.1	8.1	3.2	(48.0)	(60.8)	
NIM (%)	7.4	10.3	8.3			
IndusInd Bank						
Net interest income	21,224	22,324	27,716	30.6	24.2	We are incorporating the merged financials of BHAFIN for the current quarter and hence, the yoy numbers are not comparable. There would be no immediate benefits of the merger as the transaction, though effective from January 01, 2018 was consumated only on July 04, 2019.
Pre-provision profit	18,211	20,677	22,605	24.1	9.3	
Fee income	11,646	14,190	14,397	23.6	1.5	
Treasury income (net)	470	1,400	1,050	123.4	(25.0)	
Loan-loss provisions	2,090	20,040	8,016	283.5	(60.0)	We expect the bank to make high provisions for their IL&FS exposure (holding company - 100% from 70%). We would look at their guidance on credit costs given the exposures they have to select corporates that are currently under stress.
Adjusted PAT	10,357	3,601	9,498	(8.3)	163.8	
EPS (Rs/share)	17.3	6.0	15.8	(8.7)	163.8	
NIM (%)	3.8	3.3	3.8	7 bps	49 bps	
J&K Bank						
Net interest income	7,792	9,313	9,159	17.5	(1.7)	Loan growth within J&K will be a healthy but we expect overall loan growth slower at ~10% yoy. NIM unchanged qoq at 3.9%.
Pre-provision profit	3,498	6,006	3,863	10.5	(35.7)	
Fee income	418	486	452	8.0	(6.9)	
Treasury income (net)	(345)	2,279	100	NM	(95.6)	
Loan-loss provisions	2,348	4,058	2,840	21.0	(30.0)	We expect fresh impairment ratios to decline sharply as IL&FS exposure has been fully reported. Movement of the restructured loan (5% of loans) would be the key monitorable along with any lumpy slippages due to change in management in the current quarter.
Adjusted PAT	526	2,148	641	21.8	(70.2)	
EPS (Rs/share)	0.9	3.9	1.2	21.8	(70.2)	
Karur Vysya Bank						
Net interest income	5,836	6,192	6,157	5.5	(0.6)	We expect earnings growth of ~20% yoy (low base) led by flat provisions but revenue growth to remain muted. Loan growth to remain sluggish at 4% yoy.
Pre-provision profit	4,596	4,648	4,691	2.1	0.9	
Fee income	1,867	2,239	2,035	9.0	(9.1)	
Treasury income (net)	(370)	150	264	NM	75.8	
Loan-loss provisions	3,850	2,790	3,767	(2.2)	35.0	We expect slippages to be higher at ~4% of loans as it is mostly coming from the SME exposure which was guided by the bank in 3QFY19. Guidance on slippage for the rest of FY2020 would be a key monitorable.
Adjusted PAT	459	600	554	20.7	(7.7)	
EPS (Rs/share)	3.8	4.9	4.5	20.7	(7.7)	

Source: Company, Kotak Institutional Equities

Quarterly result expectation of companies under coverage

	Jun-18	Mar-19	Jun-19E	Change (%) yoy	Change (%) qoq	Comments
LIC Housing Finance						
Net interest income	10,085	12,225	12,048	19.5	(1.5)	We expect loan growth to moderate to 3% qoq (19% yoy) from 7% qoq in 4QFY19 due to slowdown in non-housing segments.
Pre-provision profit	9,500	10,915	11,113	17.0	1.8	
Loan-loss provisions	1,610	1,052	1,250	(22.3)	18.8	
Adjusted PAT	5,686	6,936	6,904	21.4	(0.5)	NIMs will likely moderate 10 bps qoq to 2.5% reflecting pressure on yields in its retail business.
EPS (Rs/share)	11.3	13.7	13.7	21.4	(0.5)	
Net interest margin (%)	2.4	2.6	2.5			
Loan book (Rs bn)	1,687	1,946	2,005	18.9	3.0	
Mahindra & Mahindra Financial						
Net interest income	10,771	13,109	13,447	24.8	2.6	Weakness in vehicle sales will lead to muted loan growth (3% qoq, down from 6% qoq in FY2019).
Pre-provision profit	7,060	7,803	8,022	13.6	2.8	
Loan-loss provisions	2,938	(1,144)	3,500	19.1	NM	
Adjusted PAT	2,691	5,879	2,984	10.9	(49.2)	QoQ rise in NPLs will likely lead to 15 bps qoq compression in NIM to 7.9% even as falling bond yields and increase in lending rates will support incremental spreads.
EPS (Rs/share)	4.8	10.4	5.3	10.9	(49.2)	
Net interest margin (%)	7.6	8.1	7.9			
AUM (Rs bn)	587	671	691	17.7	3.0	
Opex/AUM (%)	2.9	3.4	3.3	15.9	(2.2)	
Magma Fincorp						
Net interest income	3,211	3,249	3,328	3.6	2.4	We expect loan growth to remain muted at 9% yoy reflecting slowdown in vehicle sales.
Pre-provision profit	1,733	1,679	1,758	1.5	4.7	
Loan-loss provisions	846	413	700	(17.2)	69.6	
Adjusted PAT	681	853	719	5.6	(15.7)	Rise in borrowings cost since 3QFY19 coupled with declining rates on CV loans will put pressure on NIM.
EPS (Rs/share)	2.9	3.6	3.0	5.6	(15.7)	
Net interest margin (%)	8.1	7.8	7.8			
AUM (Rs bn)	160	170	173	8.5	1.7	
Opex/AUM (%)	4.2	4.1	3.9	(7.4)	(4.1)	
Muthoot Finance						
Net interest income	11,092	12,209	13,089	18.0	7.2	We expect Muthoot Finance to report strong (19% yoy and 8% qoq) growth in loan book on the back of 4% rise in gold prices.
Pre-provision profit	7,576	8,146	9,109	20.2	11.8	
Loan-loss provisions	26	204	50	92.3	(75.5)	
Adjusted PAT	4,916	5,115	5,798	17.9	13.3	NIM will likely remain stable qoq at 14.7%; GNPLs/provisions will likely remain low supported by rising gold prices.
EPS (Rs/share)	12.3	12.8	14.5	17.9	13.3	
Net interest margin (%)	14.8	14.6	14.7			
AUM (Rs bn)	310	342	370	19.3	8.0	
PNB Housing Finance						
Net interest income	4,241	4,654	4,901	15.6	5.3	We expect PNBHF to deliver 27% yoy and 3% qoq growth (6% qoq growth in 4QFY19) due to slowdown in the wholesale segment.
Assignment Income	-	939	750			
Pre-provision profit	3,035	3,502	3,726	22.8	6.4	
Loan-loss provisions	440	101	600	36.3	493.5	
Adjusted PAT	1,401	1,748	1,605	14.6	(8.1)	Increase in benchmark lending rates will support calculated NIM at 2.6% (2.57% in 4QFY19 and 2.8% in 1QFY19).
EPS (Rs/share)	11.0	10.5	12.6	14.6	20.1	
Net interest margin (%)	2.8	2.6	2.6			
Loan book (Rs bn)	639	740	768	20.2	3.7	
Punjab National Bank						
Net interest income	46,919	42,003	43,734	(6.8)	4.1	We expect losses to be lower on the back of lower provisions. Decline in gross and net NPLs to continue (LLP at ~4%, annualised) but there is no major account for upgradation or slippage this quarter
Pre-provision profit	41,947	28,612	31,066	(25.9)	8.6	
Fee income	10,570	9,525	10,001	(5.4)	5.0	
Treasury income (net)	(4,860)	1,050	3,612	NM	244.0	
Loan-loss provisions	49,580	91,536	45,768	(7.7)	(50.0)	We expect strong contribution from treasury income given the decline in yields. Revenues not comparable yoy due to high one-off recovery from one large steel account in the base quarter. We expect loan growth at 8% and ~5bps NIM expansion qoq
Adjusted PAT	(9,400)	(47,496)	(12,024)	27.9	(74.7)	
EPS (Rs/share)	(3.4)	(10.3)	(2.6)	(23.3)	(74.7)	
RBL Bank						
Net interest income	5,527	7,387	7,534	36.3	2.0	We expect solid NII growth (~35% yoy) on the back of healthy loan growth (35% yoy) driven by robust traction cards and MFI business.
Pre-provision profit	4,323	5,600	5,550	28.4	(0.9)	
Treasury income (net)	370	205	275	(25.6)	34.4	
Loan-loss provisions	1,010	1,570	1,413	39.9	(10.0)	We expect high operating expense growth (~35% yoy) due to the cards business. We expect stable trends on asset quality though we would look at the commentary on their corporate exposure.
Adjusted PAT	1,900	2,472	2,502	31.7	1.2	
EPS (Rs/share)	5.1	6.6	6.7	31.7	1.2	
Shriram City Union Finance						
Net interest income	9,377	9,380	9,693	3.4	3.3	We expect SCUF to deliver 7% yoy loan growth (7% in 4QFY19) as the overall business environment remains weak.
Loan-loss provisions	2,154	1,830	1,850	(14.1)	1.1	
Adjusted PAT	2,296	2,513	2,641	15.0	5.1	NIM will likely compress 15 bps qoq to reflect higher funding costs in 2HFY19.
EPS (Rs/share)	34.8	38.1	40.1	15.0	5.1	
Net interest margin (%)	13.2	12.9	12.8			
AUM (Rs bn)	292	296	312	7.0	5.6	
Opex/AUM (%)	5.1	4.9	5.0			
Shriram Transport						
Net interest income	18,271	19,132	18,995	4.0	(0.7)	We expect STFC's loan growth to remain muted (6% yoy and 2% qoq, 1% qoq in 4QFY19) on the back of weak CV volumes.
Pre-provision profit	14,057	15,120	15,175	8.0	0.4	
Loan-loss provisions	5,227	5,398	5,350	2.4	(0.9)	
Adjusted PAT	5,729	7,460	6,583	14.9	(11.8)	Rise in borrowings cost in 2HFY19 will lead to 15 bps qoq NIM compression to 7.2%.
EPS (Rs/share)	25.2	32.9	29.0	14.9	(11.8)	
Net interest margin (%)	7.5	7.3	7.2			
AUM (Rs bn)	1,005	1,045	1,066	6.0	2.0	
Provisions/AUM (%)	2.1	2.1	2.0			

Source: Company, Kotak Institutional Equities estimates

Quarterly result expectation for companies under coverage

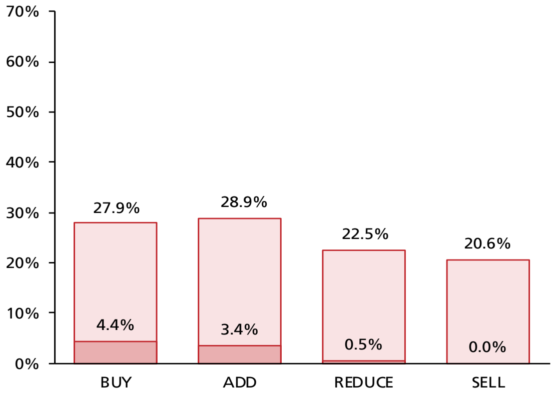
	Jun-18	Mar-19	Jun-19E	Change (%) yoy	Change (%) qoq	Comments
State Bank of India						
Net interest income	217,984	229,538	225,207	3.3	(1.9)	We expect loan growth at ~12% yoy and NIM unchanged qoq at ~2.9%. Non-interest income growth to be higher due to higher treasury income and income from written-off loans.
Pre-provision profit	119,731	169,331	151,738	26.7	(10.4)	
Fee income	49,760	85,890	53,243	7.0	(38.0)	
Treasury income (net)	(83,620)	21,490	13,750	NM	(36.0)	
Loan-loss provisions	130,380	173,360	112,684	(13.6)	(35.0)	We expect slippages at 1.6% of loans as recognition of large accounts is complete while gross NPLs could decline led by higher write-offs. Provisions would be high due to ageing of NPLs. RoE recovery would be a key monitorable.
Adjusted PAT	(48,759)	8,384	25,357	NM	202.4	
EPS (Rs/share)	(5.5)	0.9	2.8	NM	202.4	
Ujjivan Financial Services						
Net interest income	2,224	2,863	3,249	46.1	13.5	We expect Ujjivan to report strong PAT growth on the back of strong AUM growth (~45% yoy) driven by solid performance in MFI, housing space and SME financing.
Loan-loss provisions	151	124	144	(4.9)	15.8	
Adjusted PAT	451	638	662	46.8	3.7	
EPS (Rs/share)	3.8	5.3	5.5	46.8	3.7	We expect cost ratios to be high (~75%) as transition to a bank continues. Commentary on the path of listing of the bank as well as outlook on MFI loans would be key monitorable.
Union Bank						
Net interest income	26,261	26,015	26,686	1.6	2.6	We expect NII growth at 1% yoy driven by ~1% yoy loan growth. We expect NIM to be flat qoq at 2.3%.
Pre-provision profit	20,617	17,562	18,015	(12.6)	2.6	
Fee income	7,070	8,670	6,363	(10.0)	(26.6)	
Treasury income (net)	1,669	2,140	2,547	52.6	19.0	
Loan-loss provisions	17,780	56,820	28,410	59.8	(50.0)	We expect slippages to fall to ~2.5% of loans but provisions to remain high (ageing of NPLs). GNPL and net NPL to decline qoq.
Adjusted PAT	1,295	(33,692)	(8,212)	(734.0)	(75.6)	
EPS (Rs/share)	1.1	(19.1)	(4.7)	(520.2)	(75.6)	
YES Bank						
Net interest income	22,191	25,059	22,650	2.1	(9.6)	We expect loan growth to decelerate further to ~8% yoy and -4% qoq. Revenue pressure to remain high due to weak fee income growth (sharp decline) and NIM pressure (higher funding costs).
Pre-provision profit	24,547	13,234	13,609	(44.6)	2.8	
Fee income	15,241	5,267	6,743	(55.8)	28.0	
Treasury income (net)	1,700	50	813	(52.2)	1,525.0	Asset quality ratios could further deterioration (lumpy corporate exposure). Commentary from the new MD&CEO would be crucial as there have been a few more exposures where the bank has had exposure. The progress of "below investment grade", deposit profile and capital consumption would be a key monitorable.
Loan-loss provisions	3,799	33,700	21,905	476.6	(35.0)	
Adjusted PAT	12,604	(15,066)	(5,786)	(145.9)	(61.6)	
EPS (Rs/share)	5.5	(6.5)	(2.5)	(145.9)	(61.6)	

Source: Company, Kotak Institutional Equities

"Each of the analysts named below hereby certifies that, with respect to each subject company and its securities for which the analyst is responsible in this report, (1) all of the views expressed in this report accurately reflect his or her personal views about the subject companies and securities, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report: M. B. Mahesh, Nischint Chawathe, Dipanjan Ghosh, Shrey Singh and Venkat Madasu."

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Percentage of companies covered by Kotak Institutional Equities, within the specified category.

Percentage of companies within each category for which Kotak Institutional Equities and or its affiliates has provided investment banking services within the previous 12 months.

* The above categories are defined as follows: Buy = We expect this stock to deliver more than 15% returns over the next 12 months; Add = We expect this stock to deliver 5-15% returns over the next 12 months; Reduce = We expect this stock to deliver -5-+5% returns over the next 12 months; Sell = We expect this stock to deliver less than -5% returns over the next 12 months. Our target prices are also on a 12-month horizon basis. These ratings are used illustratively to comply with applicable regulations. As of 31/03/2019 Kotak Institutional Equities Investment Research had investment ratings on 204 equity securities.

Source: Kotak Institutional Equities — As of March 31, 2019

Ratings and other definitions/identifiers

Definitions of ratings

BUY. We expect this stock to deliver more than 15% returns over the next 12 months.

ADD. We expect this stock to deliver 5-15% returns over the next 12 months.

REDUCE. We expect this stock to deliver -5-+5% returns over the next 12 months.

SELL. We expect this stock to deliver <-5% returns over the next 12 months.

Our Fair Value estimates are also on a 12-month horizon basis.

Our Ratings System does not take into account short-term volatility in stock prices related to movements in the market. Hence, a particular Rating may not strictly be in accordance with the Rating System at all times.

Other definitions

Coverage view. The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: Attractive, Neutral, Cautious.

Other ratings/identifiers

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CS = Coverage Suspended. Kotak Securities has suspended coverage of this company.

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NA = Not Available or Not Applicable. The information is not available for display or is not applicable.

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Corporate Office
Kotak Securities Ltd.
27 BKC, Plot No. C-27, "G Block"
Bandra Kurla Complex, Bandra (E)
Mumbai 400 051, India
Tel: +91-22-43360000

Overseas Affiliates
Kotak Mahindra (UK) Ltd
8th Floor, Portsoken House
155-157 Minories
London EC3N 1LS
Tel: +44-20-7977-6900

Kotak Mahindra Inc
369 Lexington Avenue
28th Floor, New York
NY 10017, USA
Tel:+1 212 600 8856

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