Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Axis Bank

In-line Q3; prudent provisioning a positive

Banks & Finance	Sharekhan code: AXISBANK	Result Update

Stock Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 632**	
Price Target: **Rs. 800**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

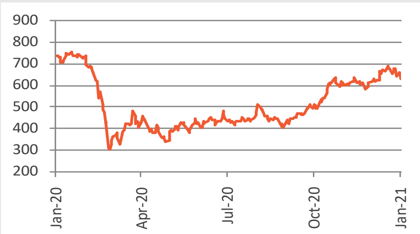
Company details

Market cap:	Rs. 193,467 cr
52-week high/low:	Rs. 766/285
NSE volume: (No of shares)	226.8 lakh
BSE code:	532215
NSE code:	AXISBANK
Free float: (No of shares)	264.4 cr

Shareholding (%)

Promoters	13.4
FII	56.8
DII	23.0
Others	6.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.3	25.2	44.6	-14.3
Relative to Sensex	2.2	6.4	21.4	-30.0

Sharekhan Research, Bloomberg

Summary

- Operational performance was in line with expectations; PAT hit by elevated provisions and slower growth in advances
- Asset quality improved q-o-q; front-loading of Provisions (on proforma basis) augurs well for long term; aggregate basis provision coverage is at 116% of GNPA
- Management's growth commentary on FY22E growth offers confidence; stock trades at 2x / 1.8x FY2022E / FY2023E ABVPS
- We maintain a Buy rating on stock with a revised price target (PT) of Rs. 800.

Operational performance was largely in line with expectations, but PAT slipped, owing to elevated provisions and slower advances growth. However, asset quality improved q-o-q. The front-loading of provisions on a proforma basis augurs well for the long term. Net interest income (NII) grew 14% y-o-y to Rs 7,373 crore and was in-line with estimates. NII (pre-interest reversals) grew 19% y-o-y to Rs 7,987 crore. Operating profit grew 6% y-o-y to Rs 6,096 crore, down 11% q-o-q and was in line with estimates. However, PAT was hit by elevated provisions of ~ Rs 1,050 crore on account of prudent expenses and provisioning charges and therefore fell by 12% y-o-y to Rs. 1,117 crore, lagging expectations. Net interest margin stood at 3.59% as against 3.57% for Q3FY20. NIM before interest reversals stood at 3.89%. Advances growth is improving, but still at sub-par levels, and the Loan book (including TLTRO^ investments) grew by 9% y-o-y, of which retail loans grew by 9% y-o-y and 4% q-o-q. Retail disbursements rose to all-time highs. Disbursements in secured segments like home loans, loans against property (LAP) & car loans grew 23% y-o-y, 11% y-o-y and 10% y-o-y respectively. Corporate loans (including TLTRO investments) grew 11% y-o-y, SME loan book grew 6% q-o-q.

Conservative policies have ensured adequate provisions. While cumulative provisions (standard + additional other than NPAs) translate to 2.08% of standard loans, aggregate provision coverage ratio (specific+ standard+ additional + COVID-19 provisions) stood at a healthy 116% of GNPA. Around 81% of the Retail book is secured. Also, reasonable Restructuring (PCR on overall restructured book is 26%), and bank has 100% provisions for the unsecured retail restructured book, though those loans classified as standard are positive for asset quality. The management commentary was positive and indicated that the FY2022E is likely to be strong year for growth and profitability, and most of the residual asset quality recognition is likely to be completed in FY2021 itself with minimal impact on provisions. Axis Bank is well-capitalised with a strong CRAR (Tier1 at 15.6%) helped by the recent fund-raising. Its digital prowess, improving business traction across segments, near-normal collection efficiency, and business strengths indicate an improving outlook. We have accordingly fine-tuned our earnings estimates. We maintain a Buy rating on the stock with a revised price target (PT) of Rs. 800.

Key positives

- On a QAB basis, CASA and Retal Term Deposits (RTD) grew 16% y-o-y. CASA ratio at 42%, improved 232 bps y-o-y and 158 bps q-o-q
- Decline in 'BB & below' rated pool across all three categories i.e. fund based, non-fund based and investments

Key negatives

- Slow growth of 5% y-o-y and 6% q-o-q in fee income (over Q2 FY2021). Retail fee contributed 64% of overall fee income.

Our Call

Valuation - Axis Bank is available at 2x / 1.8x FY2022E / FY2023E ABVPS and we believe valuations are reasonable and there is potential for re-rating once earnings and economic scenario normalises. A conservative provisioning policy, comfortable capitalisation, the overall franchise value and a high provision coverage ratio (PCR) are positives, which will help the bank ride over medium-term challenges and provide support to growth and valuations. The deal with Max Financial Services and other bancassurance partnerships augur well for fee income sustainability and growth in the long run. We maintain a Buy rating on the stock with a revised price target of Rs. 800.

Key Risks

Prolonged uncertainty due to intermittent lockdowns may impact growth, and rise in NPAs in unsecured and other retail segments can pose a risk to profitability.

Valuation Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net interest income	21,708	25,206	24,934	27,330	30,155
Net profit	4,676	1,627	5,485	9,392	10,024
EPS (Rs)	18.2	5.8	19.4	33.3	35.5
PE (x)	34.8	109.6	32.5	19.0	17.8
Adj book value (Rs/share)	213.3	263.1	297.3	321.9	347.9
P/ABV (x)	3.0	2.4	2.1	2.0	1.8
RoE (%)	7.2	2.1	6.1	9.5	9.4
RoA (%)	0.6	0.2	0.5	0.8	0.7

Source: Company; Sharekhan estimates

Key Concall Highlights

Wholesale book: The bank added 452 new clients relations in wholesale banking during the 9MFY2021. The bank is focusing on getting NIMs to a desired level, growth in wholesale franchise reflects desire to balance NIMs.

One AXIS brand: The brand showing strong performance and the brand is helping subsidiaries too.

Restructured loans: Bank has a 26% coverage on restructured loans. Chosen to front load and identify NPAs proactively.

Hopeful for FY2022E: Bank expects FY2022 to be better placed, and situation improving every month.

Demand resolution stood at 98% in December, much better than 94% in September. Recovery has been strong and in Q3 were even higher than pre-COVID results.

Cheque Bounce rates: While bounce rates remain high, collections have doubled and recoveries nearly 70% of pre-COVID levels.

Standard asset coverage of 2.7% makes Axis Bank well placed in terms of asset quality; bank expect loan demand to pick up in medium term.

Restructured loans: Restructured book stood at Rs. 2,709 crore or 0.42% of gross customer assets and overall restructured book will not exceed this levels. The number is less than the earlier estimate of 1.7% of loans. The bank is not granting any further restructuring on COVID-19 grounds. It has used ECLGS and restructuring selectively.

Reversals as per IRAC norms: Interest reversals are as per IRAC norms; fee incomes have been reduced from fee income line.

Provisions: The bank has not used any overlay in provisions, and has been as per IRAC norms. PAT hit by elevated provisions, these were over and above required as per IRAC norms.

NII provisions: The bank has not used nor increased NII provisions.

Collection of written-off assets too picked up, which indicates improvement in asset quality outlook going forward. Fee reversals stood at Rs. 134 crore.

Provisions Outlook: Q4 will see lower slippages, and the bank has a large standard asset provision. Slippages that may arise in Q4 will be provided for on an aggressive manner (higher). The bank will maintain high provisions.

Advances Growth: The bank does not aim to chase growth without pricing. There are opportunities in the wholesale book and demand in the corporate segment is for low-priced loans.

Overlap between proforma slippages stood at Rs. 6,900 crore and including the slippage in the BB-rated book was Rs 819 crore. Risk on retail assets exists and some of that may remain in Q4, but minimal provisions are required.

SME loan book has seen lot of ECLGS granted only to good quality borrowers with genuine problems, but who have the capacity to repay. The bank expects FY22E to be a strong year, all COVID-related issues likely to be provided for in FY2021 itself. The bank believes that large corporates have held up well so far NPA-wise and would sustain.

Guidance: The bank's approach is strengthening the balance Sheet (conservative provisions, high capital buffer etc) and new slippages are expected to be lower (but bank will provide aggressively). The bank has not however, not guided for credit cost. The bank remains prudent, but not as a reflection on impending stress.

Dipping into provisions: The bank has not utilised any of the COVID-19 provisions (Rs. 11,000 crore, same as Q2 FY2021). Proforma numbers have guided the Provision for P&L.

Retail Slippages: 85% of slippages are from the retail book since September (since the moratorium ended) and were absorbed during Q3. Given the uptick in collection and resolution, the bank expects Q4 and beyond to be better. All loans are adequately provided for. Recoveries from retail book have improved by 70% compared to last quarter, which is encouraging. The split was equal between secured and unsecured. Most slippages have already been recognised.

Provision break-up: For the total provision taken for Q3, around Rs. 3,900 crore (on Proforma basis) was at borrower level and not facility level; and Rs. 1,000 crore of provisions were for prior recognised NPAs. Already at 45-50% lower than earlier slippage estimates. There is a residual portion in Q4, which will be lower than Q3.

Write-off policy are rule-based and not judgement-based.

Deposits: The bank has repaid a large chunk in non-retail wholesale deposits, and as credit growth improves, can revisit the same.

Collection efficiency between secured and unsecured and across the board s back to pre-COVID levels. Overall collection efficiency is 98% across board, and each month the trend is improving.

Proforma slippages are entirely from 'BB and below' book.

Floating provisions: Most provisions made are rule-based, except for COVID-19 and restructured loans. Will take Q4 whether they need to be carried forward, and presently, provisions taken are adequate.

Guidance earlier given on ROE/ROA remains aspirational, and are likely to return to normalized trajectory in FY22E.

Results Rs cr

Particulars	Q3FY21	Q3FY20	y-o-y (%)	Q2FY21	q-o-q (%)
Interest income	15,498.4	15,708.3	-1.3	16,062.9	-3.5
Interest expense	8,125.5	9,255.3	-12.2	8,736.8	-7.0
Net interest income	**7,372.9**	**6,453.0**	**14.3**	**7,326.1**	**0.6**
Non-interest income	3,776.0	3,786.6	-0.3	3,807.0	-0.8
Net total income	11,148.9	10,239.6	8.9	11,133.1	0.1
Operating expenses	5,053.3	4,496.9	12.4	4,235.6	19.3
Pre-provisioning profit	**6,095.6**	**5,742.7**	**6.1**	**6,897.4**	**-11.6**
Provisions	4,604.3	3,470.9	32.7	4,580.7	0.5
Profit before tax	1,491.3	2,271.8	-34.4	2,316.8	-35.6
Tax	374.6	514.8	-27.2	634.3	-40.9
Profit after tax	**1,116.7**	**1,757.0**	**-36.4**	**1,682.5**	**-33.6**

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view - Credit growth yet to pick up, private banks placed better

System level credit offtake, which is still subdued, is now improving, with credit growth of over 6% in the latest fortnight. On the other hand, deposits rose by ~12%, which indicate relatively healthy economic scenario. Moreover, the accommodative stance of the RBI, resulting in surplus liquidity, provides succour in terms of easy availability of funds and lower cost of funds for banks and financials. The end of the loan moratorium is a relief. Going forward, collection efficiency is likely to be a function of book quality, client profile, as well as economic pick-up. At present, we believe that the banking sector is likely to see increased risk-off behaviour, with tactical market share gains for well-placed players. We believe private banks, with improved capitalisation and strong asset quality (with high coverage and provisions buffers) are structurally better placed to take-off once the situation normalises.

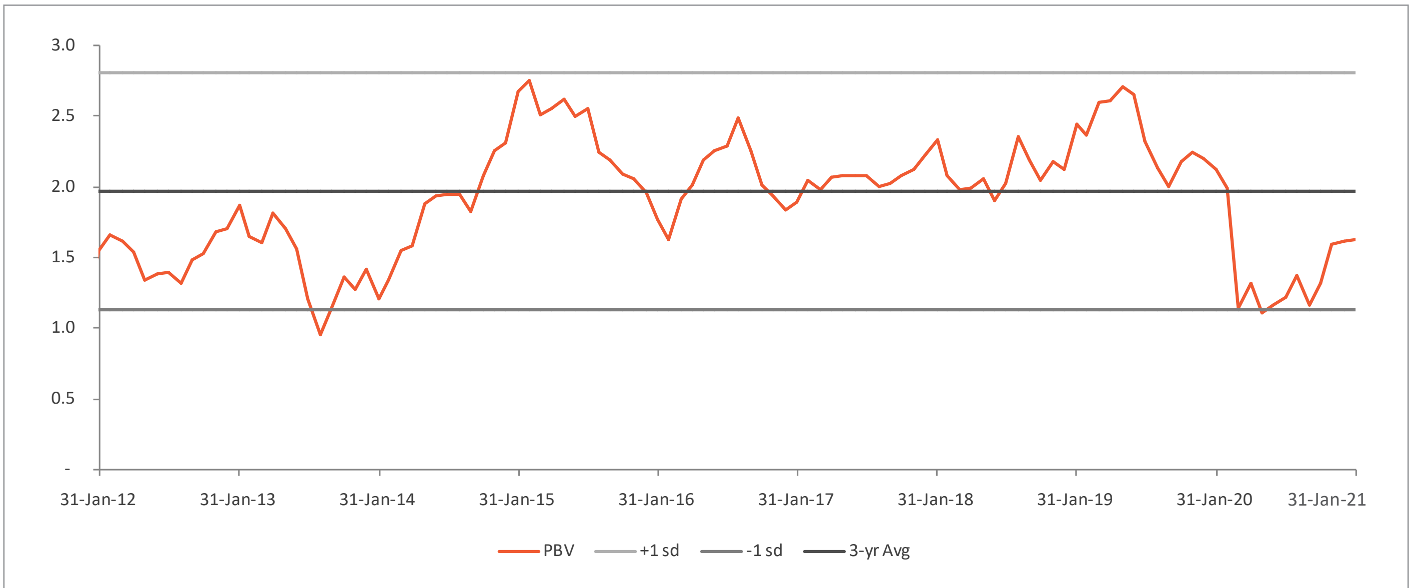
■ Company outlook - Looks promising

We believe that with Axis Bank's strong positioning, across retail, business banking and corporate with a pan-India presence, we expect the bank is likely to see lesser challenges to growth as and when it starts to unwind its cautious stance. Axis Bank has tightened underwriting standards and oversight and now been front-loading the provisions, which we believe is a positive and allows them to target growth in FY2022E unburdened from legacy issues. In the retail segment too, along with tighter underwriting criteria across product lines, collections efficiency has also been strengthened. The strong liabilities segment (led with retail term and CASA deposits) places it at a strong position with margin cushions. We believe that while Axis Bank is being prudent with a provision buffer, it is a long-term positive and will help to provide investor comfort.

■ Valuation - Maintain Buy with a price target of Rs. 800

Axis Bank is available at 2x / 1.8x FY2022E / FY2023E ABVPS and we believe valuations are reasonable and there is potential for re-rating once earnings and economic scenario normalises. A conservative provisioning policy, comfortable capitalisation, the overall franchise value and a high provision coverage ratio (PCR) are positives, which will help the bank ride over medium-term challenges and provide support to growth and valuations. The deal with Max Financial Services and other bancassurance partnerships augur well for fee income sustainability and growth in the long run. We maintain a Buy rating on the stock with a revised price target of Rs. 800.

One-year forward P/BV (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs)	P/BV (x)		P/E (x)		RoA (%)		RoE (%)	
		FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
AXIS BANK	632	1.9	1.8	32.5	19.0	3.9	10.2	0.3	0.8
HDFC BANK	1410	3.9	3.4	25.4	21.0	1.9	2.0	16.5	17.2
ICICI BANK	522	2.6	2.3	25.7	19.3	1.2	1.4	10.7	12.3

Source: Company, Sharekhan Research

About company

Axis Bank is the third-largest private sector bank in India. The bank offers the entire spectrum of financial services to customer segments covering large and mid-corporates, MSME, Agriculture and retail businesses. The bank has 11 subsidiaries which contribute and benefit from the bank's strong market position across categories.

Investment theme

Axis Bank has a well- diversified loan book having strengths in both retail and corporate segments. The bank's liability profile has improved significantly, which would be helpful in sustaining margins at healthy levels. Of late, the loan book quality is improving, which we believe is positive for its profitability and growth going forward. Due to the COvid-19 pandemic, the growth and credit costs are likely to be impacted for the sector including Axis Bank. However, we believe given the comfortable liquidity, the overall franchise value, healthy capitalization levels and a high provision coverage ratio (PCR) Axis bank will be able to ride over the medium-term challenges. The deal with MFS is also a long-term positive that can yield considerable benefits. At present we believe risk reward is favourable for long term investors.

Key Risks

Prolonged uncertainty due to intermittent lockdowns may impact growth, and rise in NPAs in unsecured and other retail segments can pose a risk to profitability.

Additional Data

Key management personnel

Mr Amitabh Chaudhry	MD & CEO
Mr Rajiv Anand	Excecutive Director
Mr Puneet Sharma	President & CFO
Mr Deepak Maheshwari	Group Excecutive & CCO

Source: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	8.3
2	Dodge & Cox	3.59
3	Unit Trust of India	3.37
4	SBI Funds Management Pvt Ltd	3.19
5	BC ASIA INVESTMENTS	3.12
6	Vanguard Group Inc/The	2.67
7	ICICI Prudential Asset Management	2.59
8	BlackRock Inc	2.47
9	FMR LLC	2.37
10	HDFC Trustee Co Ltd/India	2.13

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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