Sharekhan
by BNP PARIBAS

Banking
Sailing steady in testing times

Q4FY2021 Results Preview

Sector: Banking

Sector View

Private Banks	Positive
PSU Banks	Neutral

Q4FY2021 quarter is expected to see steady earnings outlook because continued uptick in economic recovery and ease in liquidity conditions. However, post the Supreme Court's (SC) direction on recognition of non-performing assets (NPA), the street would watch closely on the disclosures on asset quality. Even though overall credit growth has improved from Q3 run-rate at ~7% y-o-y, we expect larger and well-capitalised banks (such as HDFC Bank, ICICI Bank, Axis Bank, and SBI) to report better advances growth and continue to gain market share. While the banking sector has seen improvement in systemic loan growth, performance is likely to be far from balanced. A few segments such as improvement in disbursements (healthy for segments such as retail, home, auto, LAP, and gold loans) are expected to lead growth, as they revert to pre-COVID levels. However, segments such as unsecured book and micro loans are likely to still remain soft as banks are likely to have been cautious about them. So far, overall asset-quality trends have fared better than expectations, led by sharp improvement in collection efficiency and a lower restructuring book, but the outlook because of the recent surge in COVID-19 cases would make management's commentary on growth and asset-quality outlook key to watch out for. With the SC's stay on NPA recognition being finally withdrawn, the overhang on the banking sector has gone away. We believe the focus shifts back on actual NPAs and the recovery process thereof. Management commentary on resumption of collections and recovery efforts will be keenly watched out. Q4 saw an increase in bonds yields, which could impact the treasury book and gains that banks were sitting on. We expect the quantum of treasury gains to decline on a sequential basis.

Most private banks (PBs) have been progressively de-risking their loan book by preferring to target the better-rated corporate segment and de-bulking of advances, which is likely to continue to be seen in Q4 as well. Most PBs had frontloaded their NPAs, which indicates that while slippages are likely to be elevated, credit cost is likely to be manageable for larger players. We expect performances of mid-size PBs to remain mixed, given asset-quality challenges (relatively high restructuring book, vulnerable segment, and low collection efficiency) as compared to larger peers. While many PBs have proactively provided for proforma NPAs, the revert in pandemic cases is likely to allow them maintain additional provision buffers, which will help limit the impact on profitability. For PSU banks (PSB), we believe credit growth is likely to be at or below system level growth (constrained by the need to conserve capital). We expect their legacy NPAs to keep the credit cost to remain elevated. We expect SBI to continue to be the best performer in the PSB space. For overall banks, we expect incrementally improved credit growth outlook for FY2022E/FY2023E and expect them to gradually wean off surplus liquidity on the balance sheet (which would reduce the drag on margins). We expect banks to continue to strengthen their balance sheets, helped by the recent capital raise (for both PSBs and PBs).

Outlook

We retain preference for PBs and SBI: The economy is showing signs of gradual return to recovery, which augurs well for long-term demand outlook. However, potential risks exist to economic recovery and global challenges (due to the pandemic), which are also present. However, this time the vaccination is likely to cushion the impact on the earnings front (especially on the asset-quality recognition part). Hence, we expect the gradual return to normalised business traction to be positive for banking companies. During Q4, we expect stronger PBs to show sequentially better growth, helped by healthy capital levels, which will provide support to margins. The recent spate of capital raising has been positive for balance sheet strengthening, and gradually reducing liquidity buffer will be positive support for margins and medium-term return ratios. We hope to see more clarity and granular information sharing on the book as lenders will share their strategy to align their portfolio and work with borrowers to recover loans. Agriculture is likely to be a relatively bright spot.

Valuation

We prefer large corporate/retail PBs and SBI among PSBs and see potential for them to gain market share as the situation normalises. Healthy market share gains and CASA ratio increase will be facilitators for improvement in return ratios.

Key risks:

Due to resurgence of COVID 19, economic recovery may be prolonged. The economic distress may lead to further risk-off behaviour impacting profitability and growth outlook.

Leaders for Q4FY2021: HDFC Bank, ICICI Bank, and SBI

Laggards for Q4FY2021: BOI and PNB

Preferred Picks:

Private banks: ICICI Bank, HDFC Bank, Kotak Mahindra Bank, and AU Small Finance Bank

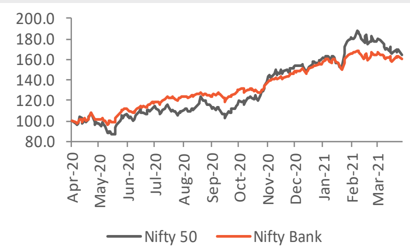
Public sector bank: SBI

Our coverage universe

Companies	CMP (Rs)	Reco.	PT (Rs)
AU Small Finance	1,233	Buy	1,500
Axis Bank	688	Buy	900
Bank of Baroda	74	Hold	75
Bank of India	69	Hold	UR
City Union Bank	166	Buy	225
Federal Bank	79	Buy	95
HDFC Bank	1,447	Buy	1,810
ICICI Bank	578	Buy	770
IndusInd Bank	946	Buy	1,340
Kotak Mahindra Bank	1,792	Buy	2,130
Punjab National Bank	38	Hold	42
RBL Bank	216	Buy	UR
State Bank of India	285	Buy	460

UR - Under review

Price chart



Q3FY2021 earnings estimates

Company	Net Interest Income (Rs Cr)				PPoP (Rs Cr)				PAT (Rs Cr)			
	Q4FY21E	Q4FY20	YoY %	QoQ %	Q4FY21E	Q4FY20	YoY %	QoQ %	Q4FY21E	Q4FY20	YoY %	QoQ %
PSU Banks												
State Bank of India	29,751	22,766.9	30.7	3.2	18,235	15,733.8	15.9	5.6	6,540	3,580.8	82.6	27.4
Bank of Baroda	7,826	6,798.2	15.1	1.0	5,537	5,120.8	8.1	-1.0	1,268	506.6	150.2	19.5
Punjab National Bank	8,586	4,678.0	83.5	3.3	6,372	3,932.4	62.0	-0.3	948	(697.1)	NA	87.3
Bank of India	3,797	3,793.1	0.1	1.5	2,618	2,652.6	-1.3	-7.7	548	(3,571.4)	NA	1.3
Total PSU Banks	**49,960**	**38,036**	**31.3**	**2.8**	**32,762**	**27,440**	**19.4**	**2.1**	**9,303**	**(181)**	**NA**	**28.5**
Private Banks												
ICICI Bank	10,205	8,926.9	14.3	2.9	8,813	7,390.1	19.2	-0.1	5,100	1,221.4	317.6	3.3
Axis Bank	7,698	6,453.0	19.3	5.1	6,348	5,851.1	8.5	4.1	1,664	(1,387.8)	NA	49.0
HDFC Bank	16,655	15,203.4	9.5	2.1	14,895	12,958.2	14.9	-1.9	8,689	6,927.0	25.4	-0.8
Federal Bank	1,478	1,216.0	21.6	2.9	928	959.3	-3.3	-3.6	396	301.2	31.4	-2.0
IndusInd Bank	3,560	3,231.2	10.2	4.5	3,050	2,836.2	7.5	2.9	938	301.8	210.6	12.9
Kotak Mahindra Bank	4,214	3,559.7	18.4	5.2	3,404	2,725.3	24.9	10.4	2,103	1,266.6	66.1	13.5
RBL Bank	974	1,021.0	-4.6	5.5	845	751.9	12.4	15.4	163	114.4	42.9	133.7
City Union Bank	499	419.5	18.9	2.0	400	335.1	19.5	-12.6	167	(95.3)	NA	-2.0
AU Small Finance Bank	701	554.9	26.4	10.8	690	315.8	118.4	-21.0	277	122.3	126.1	-42.3
Total Private Banks	**45,282**	**40,031**	**13.1**	**3.3**	**38,682**	**33,807**	**14.4**	**1.0**	**19,221**	**8,649**	**122.2**	**5.9**

Source: Company, Sharekhan Research

Valuations

Company	CMP (Rs)	Reco/View	Target Price (Rs)	BVPS		P/BV	
				FY22E	FY23E	FY22E	FY23E
PSU Banks							
State Bank of India	285	Buy	460	226.3	280.7	1.3	1.0
Bank of Baroda	74	Hold	75	162.0	171.0	0.5	0.4
Punjab National Bank	38	Hold	42	48.0	67.6	0.8	0.6
Bank of India	69	Hold	UR	131.0	155.0	0.5	0.4
Private Banks							
ICICI Bank	578	Buy	770	235.6	262.6	2.5	2.2
Axis Bank	688	Buy	900	321.9	247.9	2.1	2.8
HDFC Bank	1447	Buy	1810	398.1	452.5	3.6	3.2
Federal Bank	79	Buy	95	87.4	97.3	0.9	0.8
IndusInd Bank	946	Buy	1340	586.9	661.7	1.6	1.4
Kotak Mahindra Bank	1792	Buy	2130	373.6	422.3	4.8	4.2
RBL Bank	216	Buy	UR	246.7	271.5	0.9	0.8
City Union Bank	166	Buy	225	91.4	107.8	1.8	1.5
AU Small Finance	1233	Buy	1500	231.9	294.9	5.3	4.2

Source: Company, Sharekhan Research
UR: Price targets Under review

Q4FY2021 Banking earnings preview

Company-wise key expectations

Company	y-o-y (%)	q-o-q (%)	Comment
Axis Bank			
NII	19.3	5.1	We expect loan growth at ~8% y-o-y with a greater focus on the retail segment. NIM likely to be sequentially flat (helped by improving funding cost benefits). We expect slippages to be lower on a q-o-q basis.
PPOP	8.5	4.1	
PAT	(219.9)	49.0	
AU Small Finance Bank			
NII	26.4	10.8	We expect AUM growth to improve sequentially, and disbursements are expected to normalise further. We expect NIM to be stable with a positive bias. Deposit momentum is likely to sustain. We expect cost growth to pick-up as business activity resumes to earlier levels. We expect provisions to sequentially elevate in the anticipated front loading of slippages; gains from Aavas stake sale to benefit PAT.
PPOP	118.4	(21.0)	
PAT	126.1	(42.3)	
City Union Bank			
NII	18.9	2.0	We expect cautious loan growth at mid-single digits during the quarter. Hence, NII growth is likely to be similar to loan growth. We expect NIM to be flat. Impact of slowdown on SME portfolio and the collection/restructuring will be a key discussion area.
PPOP	19.5	(12.6)	
PAT	(274.7)	(2.0)	
FEDERAL BANK			
NII	21.6	2.9	We expect loan growth to improve led by retail and SME businesses. We expect the outlook to improve going forward. NIM is likely to be stable q-o-q with slippages at <2% of loans. Focus would be on management commentary and impact on the SME portfolio of the bank.
PPOP	(3.3)	(3.6)	
PAT	31.4	(2.0)	
Indusind Bank			
NII	10.2	4.5	Operating parameters may remain subdued. Loan growth to be flat but strong deposit growth and CASA recovery would help NIMs. We expect higher provisions to mute profit growth, mainly as sectors such as CV, rural, and select corporates, are expected to weaken. Management commentary on asset quality and credit cost outlook will be keenly monitored.
PPOP	7.5	2.9	
PAT	210.6	12.9	
ICICI BANK			
NII	14.3	2.9	We expect strong pre-provision operating profit (PPOP) growth due to improved NII and advances traction. Loan growth to be at mid-teens and stable NIM. Asset quality to be largely stable. Credit costs likely to trend down on a q-o-q basis. Management commentary on asset quality and lockdown impact will be keenly monitored.
PPOP	19.2	(0.1)	
PAT	317.6	3.3	
HDFC Bank			
NII	9.5	2.1	We expect loan growth to be strong, a cautious outlook on growth continue. Retail loan growth may be optically slower due to weak volume growth in auto, while growth in the unsecured portfolio may remain strong. Fee income growth to pick up. Healthy business traction expected.
PPOP	14.9	(1.9)	
PAT	25.4	(0.8)	
RBL Bank			
NII	(4.6)	5.5	We expect revenue growth to be slower than earlier, but deposit movement is likely to be the bright spot. Management commentary and present position will be keenly watched out for. Moreover, conditions in retail and MFI business are dynamic and will be key monitorable for near-term business performance.
PPOP	12.4	15.4	
PAT	42.9	133.7	
State Bank of India			
NII	30.7	3.2	We expect loan growth to be marginally better than industry levels at high single digits with stable NIM (core) due to easing of cost of funds. Treasury income may be expected, and few corporate loan recoveries to benefit.
PPOP	15.9	5.6	
PAT	6.0	27.4	

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