Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Axis Bank

Good Q1; risk reward attractive

Banks	Sharekhan code: AXISBANK
Reco/View: Buy ↔	CMP: Rs. 728
	Price Target: Rs. 940 ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 26.15

Updated Jul 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

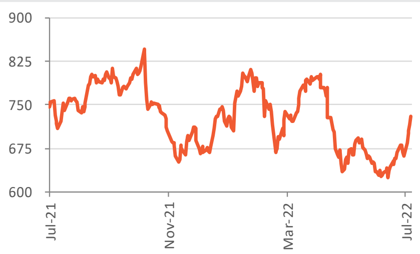
Company details

Market cap:	Rs. 2,23,663 cr
52-week high/low:	Rs. 867 / 618
NSE volume: (No of shares)	103.9 lakh
BSE code:	532215
NSE code:	AXISBANK
Free float: (No of shares)	263.97 cr

Shareholding (%)

Promoters	-
FII	50.9
DII	41.2
Others	7.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	16.1	-6.8	3.3	-3.6
Relative to Sensex	6.9	-6.1	10.0	-10.3

Sharekhan Research, Bloomberg

Summary

- Axis Bank reported a PAT of Rs. 4,125 crores (up by 91% y-o-y and flat q-o-q) above the consensus' and our expectations of Rs. 3,987 crores, primarily on account of reversal of provision on account of restructured pool and other non-NPA provisions due to which total provisions reported were lower at 21 bps annualized.
- Core credit cost for the quarter stood at 44 bps vs 34 bps q-o-q and 186 bps y-o-y. Slippages were lower by 7.5% q-o-q. Asset quality saw improvement with both GNPA and NNPA ratios fell by 6 bps q-o-q and 9 bps q-o-q to 2.76% and 0.64% during the quarter.
- NII growth was robust at 21% y-o-y / 6% q-o-q with improvement in margins by 11 bps q-o-q and 14 bps y-o-y at 3.6%. However loan growth reported at 14% y-o-y lagged its peers. Core Operating profits grew at a healthy pace by 17% y-o-y / 5% q-o-q led by healthy NII growth offsetting higher opex growth (32% y-o-y/ -1% q-o-q).
- The stock currently trades at 1.6x/1.3x its FY2023E and FY2024E core BV. We maintain our buy rating on the stock with an unchanged price target of Rs. 940. We believe its valuations are reasonable and risk-reward is attractive considering improving return ratios outlook going forward.

Axis Bank reported in line operating performance with the consensus. Net interest income (NII) grew by ~21% y-o-y and ~6% q-o-q, aided by margin improvement by 14 bps y-o-y and 11 bps q-o-q reported at 3.6% along with healthy retail loan growth (25% y-o-y). Core fee income grew by 34% y-o-y but was down 5% q-o-q. Total operating expenses grew by ~32% y-o-y/ -1% q-o-q primarily on account of higher disbursements volumes, higher tech spends and employee expenses (due to addition in headcount, one off fair value change in ESOP and annual increments). Core operating profits grew at a healthy pace by 17% y-o-y / 5% q-o-q led by healthy NII growth offsetting higher opex growth (32% y-o-y/ -1% q-o-q). Provisions declined by ~89% y-o-y/~64% q-o-q primarily on account of reversal of provision on account of restructured pool and other non-NPA provisions due to which total provisions reported were lower at 21 bps annualized. However, core credit cost for the quarter stood at 44 bps vs 34 bps q-o-q and 186 bps y-o-y annualized. PAT grew by 91% y-o-y/ flat q-o-q mainly due to lower provisions. Asset quality saw improvement with both GNPA and NNPA ratios fell by 6 bps q-o-q and 9 bps q-o-q to 2.76% and 0.64% in Q1FY23. PCR at 77% vs 75%. Slippages were lower at Rs. 3,684 crore vs Rs. 3,981 crore down by 7.5% q-o-q. Restructured book stood at 0.49% of advances vs 0.55% q-o-q. BB and below rated book reduced sequentially by 13% to Rs. 8,173 crore vs Rs. 9,384 crores q-o-q. Advances grew by ~14% y-o-y and were down by ~1% q-o-q. Retail loans & SME book clocked healthy growth of 25% y-o-y and 27% y-o-y respectively however, Corporate book degrew by 4% y-o-y. Deposits grew by 13% y-o-y. Average CASA grew by 16% y-o-y vs 19% in Q4FY22. CASA ratio stands at 43.7%. This quarter also retail term deposits growth was muted at 1% y-o-y vs 4% y-o-y as the bank is reclassifying retail TD-based on ownership versus size-based classification earlier.

Key positives

- Strong NII growth led by NIMs improvement (14 bps y-o-y & 11 bps q-o-q) at 3.60%.
- Asset quality stable with benign core credit cost

Key negatives

- Higher operating expenses growth (32% y-o-y) led by tech spends, business volume and employee expenses.
- Overall loan growth lagged peers mainly due to slow down in corporate book.
- Retail term deposits growth muted.

Management Commentary

- Robust growth in key identified focus area for assets i.e (Retail, SME and mid-corporate segment) with granularity. NIMs aspirational range 3.7-3.8%. Expect improvement in next 8-10 quarter.
- The bank is confident of delivering cost to Avg asset ratio (at ~2%) over the medium term, as it currently intends to capitalize on the benign credit cycle rather than pass lower credit cost to the bottom line for future accelerated growth and improvement in efficiencies.

Revision in estimates – We have increased our FY2023E/24E earnings estimates factoring in margin improvement.

Our Call

Valuation – We maintain our Buy rating with an unchanged PT of Rs. 940: Axis Bank currently trades at 1.6x/1.3x its FY2023E/FY2024E core BV. The bank is looking for a sustainable growth path in terms of advances growth, led by retail, SME, and mid-corporate segments in a granular manner along with focus on mobilization of low-cost granular liability and higher spending on tech. New digital product initiatives, both in assets and liability segments, are growing well, as reflected in the strong acquisition growth. The bank's continuous efforts of growing asset franchise in a granular manner (retail loans account for 59% of the total book), focus on mobilization of low-cost granular deposits, improvement in impaired loans would allow benign credit cost, margin improvement and improved return ratios matrix, would bode well for good earnings compounding going ahead. With high PCR and a strong balance sheet, the bank can absorb shocks from any unanticipated future risk. We believe its valuations are reasonable, given structural improvement visible in the franchise and provides attractive risk-reward.

Key Risks

Economic slowdown due to which slower loan growth and higher than anticipated credit cost especially from the 'BB and below-rated corporate portfolio and the unsecured retail book could affect earnings.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Net Interest Income	29,239	33,132	40,334	47,280
Net profit	6,589	13,026	17,725	21,415
EPS (Rs.)	22.1	42.4	57.7	69.8
P/E (x)	30.5	15.9	11.7	9.7
P/Core BV (x)	2.0	1.8	1.6	1.3
RoE	7.1	12.0	14.3	14.9
RoA	0.7	1.2	1.4	1.5

Source: Company; Sharekhan estimates

Key result highlights

- **Robust NII growth led by margin improvement:** Net interest income (NII) grew by ~21% y-o-y and ~6% q-o-q, aided by margin improvement by 14 bps y-o-y and 11 bps q-o-q reported at 3.6% also aided by healthy retail loan growth (25% y-o-y). Improvement in margins came from loan mix towards higher yield product, reduction in lower-yielding RIDF book, improvement in LDR and run down of lower yield overseas corporate book. Expect further improvement in net interest margin over the medium term, which will be driven by – a. Loan growth skewed towards higher yield segment; b. Higher rate cycle, will help floating rate loans to reprice faster (Over the past years, the share of floating rate loans and repo-linked loans within that has improved sharply for the bank), while liabilities are expected to reprice with lag and with less quantum; c. Improvement in low-cost granular deposit base; d. Reduced share of low-yielding RIDF bonds. Overall, there should be an upward trajectory seen in margins in the near term.

- **Accelerated investments for future growth:** The bank continues to make significant investments in building digital and new-age tech capabilities. The bank is also investing in required talent. Overall, tech spends and other higher operating expenses are weighing on core PPOP growth and, hence, profitability. Axis Bank has still guided for elevated costs to assets ratio > 2% in the near term and it would moderate over the medium term. However, this will not affect the bank's profitability, as it intends to capitalize on the benign credit cycle rather than pass lower credit costs to the bottom line. We believe accelerated investments in building digital capabilities bode well for future growth and moderation of opex over the medium is positive.

- **Benign core credit cost:** Provisions declined by ~89% y-o-y/~64% q-o-q primarily on account of reversal of provision on account of the restructured pool and other non-NPA provisions due to which total provisions reported were lower at 21 bps annualized. However, core credit cost for the quarter stood at 44 bps vs 34 bps q-o-q and 186 bps y-o-y annualized. Total COVID-19 contingent provisions stood at Rs. 5,012 crores as at June 2022.

- **Healthy growth in key identified focus area for assets i.e (Retail, SME and mid corporate segment) with granularity:** Net Advances grew by 14% y-o-y with the retail book growing by 25% y-o-y. The share of secured retail loans was ~ 79%, with home loans comprising 35% of the retail book. Home loans, small business banking and the rural loans portfolio grew 18% y-o-y, 74% y-o-y, & 42% y-o-y respectively. Unsecured personal loans and credit card advances grew 20% y-o-y and 42% y-o-y respectively. SME book grew by 27% y-o-y. However, the corporate book degrew by 4% y-o-y. Robust growth in retail and SME portfolio can be fully attributed to digital initiatives. Digital sourcing has increased significantly across products. Pricing on the wholesale corporate book did not make sense both on term loan side as well as working capital. Bank guided that once price returns to normalcy, loan growth will come back. The bank do not want to risk-adjusted returns.

- **Mobilisation of low-cost granular liability is key:** Deposits grew by 13% y-o-y. Average CASA grew by 16% y-o-y vs 19% in Q4FY22. CASA ratio stands at 43.7%. This quarter also retail term deposits growth was muted at 1% y-o-y vs 4% y-o-y as the bank is reclassifying retail TD-based on ownership versus size-based classification earlier.

- **Asset quality gets better:** Asset quality has been continuously improving for the bank with both GNPA and NNPA ratios falling by 6 bps q-o-q and 9 bps q-o-q to 2.76% and 0.64% in Q1FY23. PCR at 77%.vs 75% in Q4FY22. Gross slippages were reported at Rs.3,684 crore vs Rs 3,981 crore in Q4FY22. Recoveries & upgrades stood at Rs. 2,957 crore vs Rs. 3,763 crore in Q4FY22. Write-offs were at Rs.1,512 crore vs Rs.1,697 crore in Q4FY22. Restructured book stood at 0.49% of advances vs 0.55% q-o-q. BB and below rated book reduced sequentially by 13% to Rs. 8,173 crores vs Rs. 9,384 crore q-o-q.

- **Acquisition of Citi's retail business:** Bank is awaiting for CCI approval and its integration is expected to be completed by Q4FY23.

Results Rs cr

Particulars	Q1FY23	Q1FY22	Q4FY22	Y-o-Y %	Q-o-Q %
Interest Inc.	18,729	16,003	17,776	17%	5%
Interest Expenses	9,345	8,243	8,957	13%	4%
Net Interest Income	**9,384**	**7,760**	**8,819**	**21%**	**6%**
NIM (%)	3.60	3.46	3.49	4%	3%
Core Fee Income	3,576	2,668	3,758	34%	-5%
Other Income	-577	690	465	-184%	-224%
Net Income	**12,383**	**11,118**	**13,042**	**11%**	**-5%**
Employee Expenses	2,186	1,852	1,887	18%	16%
Other Opex	4,310	3,081	4,690	40%	-8%
Total Opex	**6,496**	**4,932**	**6,576**	**32%**	**-1%**
Cost to Income Ratio	52.5%	44.4%	50.4%		
Pre Provision Profits	**5,887**	**6,186**	**6,466**	**-5%**	**-9%**
Provisions & Contingencies - Total	359	3,302	987	-89%	-64%
Profit Before Tax	**5,528**	**2,884**	**5,478**	**92%**	**1%**
Tax	1,402	724	1,361	94%	3%
Effective Tax Rate	25%	25%	25%		
Reported Profits	**4,125**	**2,160**	**4,118**	**91%**	**0%**
Basic EPS (Rs)	13.43	7.05	13.42	90%	0%
Diluted EPS (Rs)	13.40	7.03	13.38	91%	0%
RoA (%)					
Advances	7,01,130	6,14,874	7,07,696	14%	-1%
Deposits	8,03,572	7,13,862	8,21,721	13%	-2%
Gross NPA	**21,037**	**25,950**	**21,822**	**-19%**	**-4%**
Gross NPA Ratio (%)	2.76	3.85	2.82		
Net NPA	**4,781**	**7,846**	**5,512**	**-39%**	**-13%**
Net NPAs Ratio (%)	0.64	1.20	0.73		
PCR - Calculated	77.3%	69.8%	74.7%		

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Credit growth accelerating; Top private banks placed better

System-level credit offtake grew by ~13.3% y-o-y in the fortnight ending June 17, 2022, indicating loan growth has been sustaining, given the distinct signs of improving economy and revival of investments and loan demand. On the other hand, deposits rose by ~9.8%, which also reflects a healthier economic scenario but are trailing advanced growth. The bottom-up story is intact and we should see loan growth accelerate, while margins would continue to expand in a higher interest rate cycle. Asset quality is not a big issue from the end of the corporate loan as only de-leveraging is being observed. From the retail side, there could be some pressure but nothing is significant. Asset quality is likely to remain stable except for the MFI segment. Banks are in a sweet spot in terms of fundamentals and reasonable valuations. In the past two years, banks have been cautious on lending to BB and below, thus general risk, that they are carrying on corporate portfolio is low. On the retail loans front, due to COVID-19, banks have already seen one downcycle. Most of the exposure has been taken into credit cost. In terms of MSME, we need to be watchful. At present, we believe the banking sector is likely to see higher risk-off behaviour, with tactical market share gains for well-placed players. We believe large banks with a strong capital base and asset quality (with high coverage and provision buffers) are well placed to capture growth opportunities.

■ Company outlook – Risk reward is attractive

We believe the bank is looking for a sustainable growth path in terms of advances growth, led by retail, SME, and mid-corporate segments in a granular manner along with a focus on mobilization of low-cost granular liability and higher spending on tech. The key is the higher mobilization of granular liability in the medium term to support sustainable growth. The bank's continuous efforts of growing asset franchise in granular manner (retail loans account for 59% of total book), focus on mobilization of low-cost granular deposits, improvement in impaired loans (allow benign credit cost), margin improvement and improved return ratios matrix, would bode well for good earnings compounding going ahead, which makes it an attractive franchise.

■ Valuation – We maintain our Buy rating with an unchanged PT of Rs. 940

Axis Bank currently trades at 1.6x/1.3x its FY2023E/FY2024E core BV. The bank is looking for a sustainable growth path in terms of advances growth, led by retail, SME, and mid-corporate segments in a granular manner along with a focus on mobilization of low-cost granular liability and higher spending on tech. New digital product initiatives, both in assets and liability segments, are growing well, as reflected in the strong acquisition growth. The bank's continuous efforts of growing asset franchise in a granular manner (retail loans account for 59% of total book), focus on mobilization of low-cost granular deposits, improvement in impaired loans would allow benign credit cost, margin improvement and improved return ratios matrix, would bode well for good earnings compounding going ahead. With high PCR and strong balance sheet, the bank can absorb shocks from any unanticipated future risk. We believe its valuations are reasonable, given structural improvement visible in the franchise and provides attractive risk reward.

Peer valuation

Particulars	CMP (Rs / Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Axis Bank	728	2,23,663	11.7	9.7	1.6	1.3	14.3	14.9	1.4	1.5
ICICI Bank	801	5,57,153	15.6	12.8	2.1	1.8	14.7	15.4	1.8	1.9

Source: Company, Sharekhan estimates

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 is looking for sustainable growth path in terms of advances growth, led by retail, SME, and mid-corporate segments in a granular manner along with focus on mobilization of low-cost granular liability and higher spending on tech. New digital product initiatives, both in assets and liability segments, are growing well, as reflected in the strong acquisition growth. Corporate loan book quality has also improved, which we believe is positive for its profitability and growth going forward. We believe bank will have benign credit cost over the medium term, margin improvement along high PCR are likely to bode well for earnings compounding going ahead.

Key Risks

Economic slowdown due to which slower loan growth and higher-than-anticipated credit cost especially from the 'BB and below'-rated corporate portfolio and unsecured retail book could affect earnings.

Additional Data

Key management personnel

Mr. Amitabh Chaudhary	MD and CEO
Mr. Rajiv Anand	Executive Director
Mr. Puneet Sharma	CFO and President

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	8.0
2	SBI Funds Management Pvt. Ltd.	4.2
3	Dodge & Cox	4.0
4	ICICI Prudential Asset Management Co. Ltd.	3.8
5	BlackRock Inc.	2.9
6	The Vanguard Group Inc.	2.8
7	FIL Ltd.	2.1
8	Bank of New York Mellon Corp.	1.9
9	Nippon Life India Asset Management Ltd.	1.9
10	HDFC Asset Management Ltd	1.9

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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Compliance Officer: Ms. Priya Sonavane; Tel: 022–61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

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