Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Axis Bank Ltd

Operationally below expectations but lower credit cost drove higher adjusted earnings

Banks	Sharekhan code: AXISBANK

Reco/View: Buy	↔	CMP: **Rs. 881**	Price Target: **Rs. 1,140**	↔

↑ 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 27.33

Updated Mar 08, 2023

Medium Risk

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

Source: Morningstar

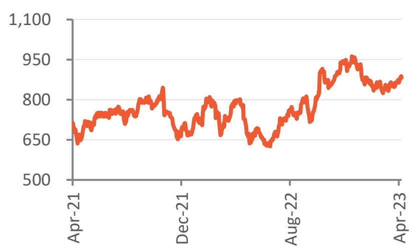
Company details

Market cap:	Rs. 2,71,114 cr
52-week high/low:	Rs. 970 / 618
NSE volume: (No of shares)	103.8 lakh
BSE code:	532215
NSE code:	AXISBANK
Free float: (No of shares)	273.9 cr

Shareholding (%)

Promoters	-
FII	49.1
DII	40.2
Others	10.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.8	0.8	-3.7	15.0
Relative to Sensex	0.3	1.3	-5.1	9.0

Sharekhan Research, Bloomberg

Summary

- Axis Bank reported a loss of Rs. 5,728 crore in Q4FY23 on the back of one-time non-recurring items aggregating to Rs. 12,490 crores comprising of (a) full amortization of Intangibles and Goodwill in relation to the purchase consideration paid for acquisition of Citibank India's Consumer Business; (b) amount charged towards policy harmonization on operating expenses and provisions for Citi business and (c) one-time stamp duty charges paid on the acquisition.
- Adjusted for non-recurring items, the bank reported PAT of Rs. 6,625 (up 61% y-o-y/ 13% q-o-q) mainly driven by lower credit cost (only ~15 bps annualized) which was higher than street expectations however on the operational front, bank reported lower than expected PPoP at Rs. 9,168 crore (up 42% y-o-y/ down 1% q-o-q).
- NIMs were broadly stable q-o-q at 4.22% versus expectations of higher margins trajectory along with higher opex growth (14% y-o-y/ 9% q-o-q) led to weaker performance on operational front than expected. Overall YoY and QoQ numbers are not comparable due to inclusion of Citi business numbers w.e.f March 01, 2023.
- Ex. Citi portfolio, deposit growth (+7% q-o-q) sequentially has picked up driven by healthy CASA traction in line with loan growth (+7% q-o-q) which is a key positive. The bank is broadly delivering performance closer to its frontline peers. Strong retail deposits mobilisation remains the key monitorables going forward. We maintain our Buy rating on the stock with an unchanged PT of Rs. 1,140. Stock currently trades at 1.7x/1.5x/1.4x its FY2024E/FY2025E core BV estimates.

Axis Bank's numbers are not comparable on y-o-y and q-o-q basis due to inclusion of Citi bank business numbers for 1 month during the quarter. Numbers lagged expectations on operational front. Net interest income (NII) grew by ~33% y-o-y and ~2% q-o-q. NIMs were broadly stable q-o-q declined by 4 bps quarter to 4.22%. There was an adverse impact of 6 bps on NIMs due to higher average LCR maintained during the quarter (129% vs 116% q-o-q) and in the last quarter there was a~ 5 bps positive impact on NIMs attributable towards one-time interest income recovery on restructured account. Core fee income grew by 24% y-o-y/14% q-o-q. Retail assets (excluding cards and payments) fee grew by 22% y-o-y/12% q-o-q. Retail cards and payments fee grew by 50% y-o-y/14% q-o-q. Corporate and commercial banking fees together grew by 12% y-o-y/13% q-o-q. The bank reported treasury profit of Rs. 83 crore during the quarter vs. Rs. 428 crore in the last quarter. Total operating expenses grew by ~14% y-o-y/9% q-o-q. Opex to average assets stood at 2.4% vs 2.3% q-o-q. Ex integration cost of Citi portfolio, opex to Avg. Assets ratio was stable at 2.3% q-o-q. Operating profit (PPoP) grew by 42% y-o-y / down 1% q-o-q. Credit cost stood at 15 bps (annualised) vs. 72 bps q-o-q. Asset quality saw sharp improvement with both GNPA and NNPA ratios declining by 36 bps q-o-q and 8 bps q-o-q to 2.02% and 0.39%, respectively. PCR remained stable q-o-q at ~81% Slippages were down by 11% q-o-q (1.9% annualised vs. 2.3% q-o-q). Recoveries and upgrades were also strong along with higher write offs during the quarter. Restructured book stood at 0.24% of advances vs. 0.33% q-o-q. BB+ and below-rated book reduced sequentially to 0.7% of advances vs. 0.9% q-o-q. Total provision buffers stood at 1.3% of advances. Ex. Citi portfolio, Advances grew by ~16% y-o-y and ~7% q-o-q. Retail loans and SME book grew by 15% y-o-y and 23% y-o-y, respectively. Corporate book grew by 14% y-o-y. Total deposits ex. Citi portfolio grew by 10% y-o-y/7% q-o-q. CA balances grew by 15% y-o-y/ 16% while SA balances grew by 11% y-o-y/7% q-o-q. Term deposits grew by 8% y-o-y/4% q-o-q. CASA ratio (incl. Citi deposits) increased to 47.2% vs. 45.0% y-o-y.

Key positives

- CASA growth picked up ex. Citi portfolio.
- Strong return ratios profile ex. Citi portfolio – ROA ~1.8% and ROE ~ 18.4% in FY2023.
- Benign Credit cost

Key negatives

- Opex growth was higher due to higher retail business volumes, tech expenses, increments and integration cost.
- Retail term deposits growth (ex. Citi portfolio) was muted.

Management Commentary

- The bank is confident of sustaining healthy asset growth however as macro environment continues to remain volatile, the franchise is cognizant of risk in the near term, Bank is confident of growing 400-600 bps higher than system growth in medium to long term.
- Management guided that it has cushion for improvement in NIMs – a) Improving asset mix, b) Normalisation of excess liquidity, c) Further repricing of floating book, d) Increasing disbursement yield on fixed book however sharp increase in cost of deposits in coming quarters could restrict improvement as system deposit growth is still lagging loan growth. Endeavor is to sustain the current NIMs trajectory.
- The bank maintained its stance of delivering cost-to-average asset ratio (at ~2%) over the medium term (ex – Citi portfolio integration cost).

Our Call

Valuation – We maintain our Buy rating with an unchanged PT of Rs. 1,140: Axis Bank currently trades at 1.7x/1.5x its FY2024E/FY2025E core BV estimates. It is well positioned for closing the valuation gap with peers as it reports consistent steady performance on a sustained basis going ahead. We see a challenging FY2024 for most banks from an NIM contraction perspective but return ratios are likely to hold up well with negligible downside risks, although Axis Bank has additional levers to protect NIMs. With risks on asset quality on the lower side, we continue to forecast a benign credit cost in FY24. We also acknowledge that it would probably take a year to understand full benefits and challenges related to Citi business acquisition. Key monitorable from here on will be customer retention & employee attrition in Citi business going ahead however as the size of this transaction is relatively small compared to net worth which gives the additional comfort.

Key Risks

Economic slowdown due to which slower loan growth, higher-than-anticipated credit cost, slower growth in retail deposit franchise, lower-than-expected margins, and transition of Citi's portfolio not on expected lines.

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Net Interest Income	33,132	42,946	48,321	53,386
Net profit	13,026	9,580	23,788	26,164
EPS (Rs.)	42.4	31.0	77.3	85.0
P/E (x)	19.6	26.7	10.7	9.7
P/BV (x)	2.2	2.0	1.7	1.5
RoE	12.0	8.0	17.4	16.2
RoA	1.2	0.8	1.7	1.7

Source: Company; Sharekhan estimates

Key result highlights

- **Margin outlook:** Net interest income (NII) grew by ~33% y-o-y and ~2% q-o-q. NIMs were broadly stable q-o-q declined by 4 bps quarter to 4.22%. There was an adverse impact of 6 bps on NIMs due to higher average LCR maintained during the quarter (129% vs 116% q-o-q) and in the last quarter there was a~ 5 bps positive impact on NIMs attributable towards one time interest income recovery on restructured account. Management guided that it has cushion for improvement in NIMs – a) A better asset mix, b) Normalization of excess liquidity, c) Further repricing of floating book, d) Increasing disbursement yield on fixed book however sharp increase in cost of deposits in coming quarters could restrict improvement as system deposit growth is still lagging loan growth. Endeavor is to sustain the current NIMs trajectory.
- **Capitalizing on the benign credit cycle:** The bank continues to make significant investments in building digital and new-age tech capabilities. The bank has maintained its stance of higher costs-to-assets ratio of >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 bottomline. We believe accelerated investments in building digital capabilities bode well for future growth and moderation of opex over the medium is positive. Additionally, opex growth was also lifted by higher retail business volumes, increments and integration cost due to the merger.
- **Credit costs to remain benign:** Credit cost stood at only 15 bps (annualised) during the quarter. With risks on asset quality on the lower side, the bank continues to forecast a benign credit cost in FY24. Total provision buffers stand at 1.3% of advances. Strong recoveries and upgrades have helped to keep credit cost lower in FY23. Overall asset quality continues to remain benign across the portfolio.
- **Confident of sustaining growth however cognizant of risk given macro volatility:** Ex. Citi portfolio, advances grew by ~16% y-o-y and ~7% q-o-q. Retail loans and SME book grew by 15% y-o-y and 23% y-o-y, respectively. In retail segment, home loans, LAP, personal loans, Credit cards and other loans grew by 5%/13%/18%/42% and 22% respectively on y-o-y basis. The corporate book grew by 14% y-o-y. 89% of the corporate book is now rated 'A and above' with 89% of incremental sanctions in FY2023 being to corporates rated A- and above. Bank is witnessing strong corporate loan demand driven by private capex from Iron and steel, CRE, Road and Infra projects, NBFC sector, etc. Average LCR during the quarter was ~129% vs ~116% q-o-q. The bank is confident of sustaining healthy asset growth however as macro environment continues to remain volatile, the franchise is cognizant of risk in the near term, the bank is confident of growing 400-600 bps higher than system growth in medium to long term.
- **Mobilisation of low-cost granular liability is key for sustaining healthy advances growth:** Ex. Citi portfolio, deposit growth (+7% q-o-q) sequentially has picked up driven by healthy CASA traction in line with loan growth (+7% q-o-q) which is a key positive. Total deposits ex-Citi portfolio grew by 10% y-o-y/7% q-o-q. CA balances grew by 15% y-o-y/ 16% while SA balances grew by 11% y-o-y/7% q-o-q. Term deposits grew by 8% y-o-y/4% q-o-q. CASA ratio (incl. Citi deposits) increased to 47.2% vs. 45.0% y-o-y. There has been visibility of improving quality in deposit franchise.
- **Asset quality gets better:** Asset quality has been continuously improving for the bank, with both GNPA and NNPA ratios falling by 36 bps q-o-q and 8 bps q-o-q to 2.02% and 0.39%, respectively. PCR stood at ~81% stable q-o-q. Gross slippages were reported at Rs. 3,375 crore vs. Rs. 3,807 crore q-o-q. Recoveries and upgrades stood at Rs. 2,699 crore vs. Rs. 2,088 crore q-o-q. Write-offs were at Rs. 2,429 crore vs. Rs.1,652 crore q-o-q. The restructured book stood at 0.24% of advances vs. 0.33% q-o-q. BB and below-rated book reduced sequentially to Rs. 5,522 crore vs. Rs. 7,076 crore q-o-q.
- **Looking for synergies:** Citi portfolio has been fully integrated with bank. The deal bolsters its market presence, especially in the growth of premium market share across wealth and cards business. Bank is working on the synergies, some of which are already yielding favorable outcomes. Employee integration has been done. Now the bank is engaging with Citi clients to offer greater proposition by cross selling its products.
- **Other:** The bank intends to open 500 branches in FY24.

Results (Standalone) Rs cr

Particulars	4QFY23	4QFY22	3QFY23	Y-o-Y %	Q-o-Q %
Interest Inc.	23,970	17,776	22,226	35%	8%
Interest Expenses	12,228	8,957	10,767	37%	14%
Net Interest Income	**11,742**	**8,819**	**11,459**	**33%**	**2%**
NIM (%)	4.22	3.49	4.26	21%	-1%
Core Fee Income	4,676	3,758	4,101	24%	14%
Other Income	219	465	564	-53%	-61%
Net Income	**16,637**	**13,042**	**16,125**	**28%**	**3%**
Employee Expenses	2,164	1,887	2,281	15%	-5%
Other Opex	5,306	4,690	4,566	13%	16%
Total Opex	**7,470**	**6,576**	**6,847**	**14%**	**9%**
Cost to Income Ratio	44.9%	50.4%	42.5%		
Pre Provision Profits	**9,168**	**6,466**	**9,277**	**42%**	**-1%**
Provisions & Contingencies – Total	306	987	1,438	-69%	-79%
Exceptional item	12,490	-	-	-	-
Profit Before Tax	**-3,628**	**5,478**	**7,840**	**-166%**	**-146%**
Tax	2,100	1,361	1,987	54%	6%
Effective Tax Rate	-58%	25%	25%		
Reported Profits	**-5,729**	**4,118**	**5,853**	**NM**	**NM**
Basic EPS (Rs)	-18.62	13.42	19.04	-239%	-198%
Diluted EPS (Rs)	-18.62	13.38	18.80	-239%	-199%
RoA (%)	-1.8	1.5	1.9		
Advances	8,45,303	7,07,947	7,62,075	19%	11%
Deposits	9,46,945	8,21,972	8,48,173	15%	12%
Gross NPA	**18,604**	**21,822**	**19,961**	**-15%**	**-7%**
Gross NPA Ratio (%)	2.02	2.82	2.38		
Net NPA	**3,559**	**5,512**	**3,830**	**-35%**	**-7%**
Net NPAs Ratio (%)	0.39	0.73	0.47		
PCR - Calculated	80.9%	74.7%	80.8%		

Source: Company; Sharekhan Research

Outlook and Valuation

■ **Sector Outlook – Deposit mobilisation to remain in focus; banks with a superior liability franchise placed better**

Overall system-level credit offtake grew by ~15.7% y-o-y in the fortnight ending April 7, 2023 while deposits rose by ~10.2% but still trails advances growth. In the past 2-3 years, loan growth has been driven by majorly retail loans and off lately, we have seen MSME & SME loan offtake picking up. Corporate loan growth has been sluggish. The RBI has taken a pause in rate hikes as of now. In this backdrop, we believe credit to large industries/corporates is expected to pick up gradually driven by capex-led demand. However, we should see some moderation in loan growth due to a higher base going forward partially offset by a pick-up in corporate loan growth, but loan growth is expected to remain healthy. Margins improvement is likely to end by Q1FY24. Margin pressure if any due to sharp repricing of deposits is expected to get offset by opex growth moderation. Asset quality is not a concern right now as corporate lending has been muted in the past few years. From the retail & MSME side, there could be some pressure due to an adverse macro situation, but nothing is significant. Asset quality outlook remains stable to positive for the sector in near to medium term. We believe there would be tactical market share gains for well-placed players. Banks with a robust capital base, strong retail deposit franchise and with high coverage & provision buffers are well placed to capture new credit growth cycle.

■ **Company Outlook – Structural improvement visible in franchise**

We believe the bank is looking for a sustainable growth path in terms of advances growth, led by retail, SME, and corporate segments in a granular manner along with a focus on mobilisation of low-cost granular liability and higher spending on tech. The key is the higher mobilisation of granular retail liability in the near to medium term to support sustainable growth. The bank's continuous efforts of growing asset franchise in a granular manner, focus on mobilisation of low-cost granular deposits, benign credit costs environment, and sustaining improved return ratios matrix bode well for good earnings compounding going ahead, which makes it an attractive franchise. We acknowledge that it would probably take a year to understand the full benefits and challenges related to Citi business acquisition.

■ **Valuation – We maintain our Buy rating with an unchanged PT of Rs. 1,140**

Axis Bank currently trades at 1.7x/1.5x its FY2024E/FY2025E core BV estimates. It is well positioned for closing the valuation gap with peers as it reports consistent steady performance on a sustained basis going ahead. We see a challenging FY2024 for most banks from an NIM contraction perspective but return ratios are likely to hold up well with negligible downside risks, although Axis Bank has additional levers to protect NIMs. With risks on asset quality on the lower side, we continue to forecast a benign credit cost in FY24. We also acknowledge that it would probably take a year to understand full benefits and challenges related to Citi business acquisition. Key monitorable from here on will be customer retention & employee attrition in Citi business going ahead however as the size of this transaction is relatively small compared to net worth which gives the additional comfort.

Peer valuation

Particulars	CMP (Rs / Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY24E	FY25E	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Axis Bank	881	2,71,114	10.7	9.7	1.7	1.5	17.4	16.2	1.7	1.7
ICICI Bank	919	6,41,508	16.0	14.1	2.4	2.0	15.9	15.5	2.0	2.1

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. The bank had a network of 4,903 domestic branches as at March 2023. Capital adequacy ratio (CAR) stands at 17.64%.

Investment theme

Axis Bank is looking for sustainable growth path in terms of advances growth, led by retail, SME, and corporate segments in a granular manner along with focus on mobilisation 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. Balance sheet mix is also improving, which we believe is positive for its profitability and sustainable growth going forward. We believe the bank will have benign credit cost in near to medium term along high PCR and contingent buffers, which are likely to bode well for earnings compounding going ahead.

Key Risks

Economic slowdown due to which slower loan growth, higher-than-anticipated credit cost, slower growth in retail deposit franchise, lower-than-expected margins, and transition of Citi's portfolio not on expected lines.

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	7.96
2	SBI FUNDS MANAGEMENT LTD.	4.68
3	ICICI PRUDENTIAL ASSET MANAGEMENT CO. LTD.	3.27
4	DODGE & COX	3.23
5	BLACKROCK INC.	3.20
6	VANGUARD GROUP INC.	2.89
7	REPUBLIC OF SINGAPORE	2.29
8	FIL LTD.	2.14
9	HDFC AMC Ltd	2.13
10	BANK OF NEW YORK MELLON CORP	2.07

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

Sharekhan

by BNP PARIBAS

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