Sharekhan by BNP PARIBAS

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Stock Update

Result Update

IndusInd Bank

Steady Q1, lower credit cost drives strong earnings

Banks	Sharekhan code: INDUSINDBK
Reco/View: Buy ↔	CMP: **Rs. 1,390** / Price Target: **Rs. 1,650** ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- IndusInd Bank (IIB) reported PAT at Rs. 2,124 crore (up 32% y-o-y/4% q-o-q), led by ~21% y-o-y decline in provisions and ~13% y-o-y growth in operating profit, which translated into RoA/RoEof ~1.9%/15.4%.
- Despite strong loan growth (up 22% y-o-y/4% q-o-q), stable NIMs at 4.29% q-o-q, and healthy core fee income (up 19% y-o-y/ 2% q-o-q), core operating profit grew at a slower pace by 15% y-o-y/1% q-o-q mainly due to higher opex growth (up 22% y-o-y/6% q-o-q).
- Annualised total credit cost stood at 134 bps (as of average advances) vs. 146 bps q-o-q and 205 bps y-o-y. The bank is guiding for lower credit cost at 110-130 bps in the coming quarters. Overall, asset quality remained stable.
- Near-term business trends look comfortable, and the franchise is looking towards more predictable performance, which is a key positive. At the CMP, the stock trades at 1.7x/1.5x its FY2024E/FY2025E BV. We maintain Buy with a revised PT of Rs. 1,650.

IndusInd Bank (IIB) reported steady in-line performance in Q1FY2024. Net interest income (NII) grew by 18% y-o-y/4% q-o-q, aided by strong growth in advances and stable margins. Net interest margin (NIM) marginally improved by 1 bps q-o-q at 4.29%. Core fee income grew by 19% y-o-y/2% q-o-q. Total operating expenses grew by 22% y-o-y/6% q-o-q, driven by increased investments in technology, branch/distribution network, employee addition, annual appraisal, and higher retail business volumes. Opex-to-average assets stood at 2.8% vs. 2.7% q-o-q. Total provisions fell by 21% y-o-y and 4% q-o-q. However, the bank has utilised contingent provisions of Rs. 200 crore. The bank continued to maintain contingent provisions of Rs. 1,700 crore (0.6% of advances). PBT grew by 32% y-o-y/4% q-o-q. Overall asset quality remained stable across the portfolio; however, slippages from the vehicle segment were higher due to seasonality factor. GNPA and NNPA ratios were at 1.94% and 0. 58%, respectively. Provisioning coverage ratio (PCR) was stable at ~71%. Total slippages were lower by 16% q-o-q (2.2% annualised versus 2.7% q-o-q). Restructured book declined to 0.66% vs. 0.84% q-o-q. Its SMA 1 and 2 improved to 23 bps vs. 32 bps q-o-q. Advances grew by 22% y-o-y/4% q-o-q, driven by broad-based growth across the portfolio. Deposits grew by 15% y-o-y/3% q-o-q. CASA deposits grew by 6% y-o-y/3% q-o-q. Retail deposits as per the LCR grew by 21% y-o-y /5% q-o-q and constitute 43% of the overall deposit base.

Key positives

- Strong business momentum and healthy retail deposits growth (21% y-o-y/5% q-o-q).
- Stable NIM despite cost of funds increasing steadily.
- Lower credit cost at 134 bps vs. 146 bps q-o-q and 205 bps y-o-y.

Key negatives

- Higher opex growth led to moderation in core operating profit growth. Opex to average assets stood.

Management Commentary

- The bank is confident of sustaining strong earnings growth, led by robust loan growth, stable NIM, and sustained lower credit cost. Loan growth is expected to be broad across the retail and wholesale segments.
- NIMs are expected at 4.2-4.3% in FY2024. Credit cost is expected at 110-130 bps. Cost-to-income ratio would remain higher at 45% in FY2024, as the bank continues to invest in the franchise for future growth; and it is expected to moderate in FY2025 to 41-43%.

Our Call

Valuation – We maintain our Buy rating on the stock with a revised PT of Rs. 1,650: At the CMP, IIB trades at 1.7x/1.5x its FY2024E/FY2025E BV estimates. Strong loan growth momentum and lower credit cost are likely to support earnings growth, and this should keep RoEs at ~15% in the near term. Retail is showing strong momentum, while the MFI business is seeing a steady recovery. The corporate book is also growing at a healthy pace. We believe NIMs have levers for improvement in H2FY2024 through the asset mix, thereby improving the return ratio as the cost of funds is expected to peak in H1FY2024. **Key monitorable:** Mobilisation of retail and granular deposits.

Key Risks

Economic slowdown that can lead to slower loan growth, higher-than-anticipated credit costs, slow growth in the retail liability franchise.

Valuation Rs cr

Particulars	FY2	FY23	FY24E	FY25E
Net Interest Income	15,001	17,592	19,770	23,946
Net profit	4,611	7,390	9,102	10,606
EPS (Rs.)	59.5	95.2	116.7	136.0
P/E (x)	23.4	14.6	11.9	10.2
P/BV (x)	2.3	2.0	1.7	1.5
RoE (%)	10.1	14.4	15.4	15.4
RoA (%)	1.2	1.7	1.9	1.9

Source: Sharekhan Research

3R MATRIX

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

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS	Positive	↔	Positive
RQ	Neutral	↔	Neutral
RV	Positive	↔	Positive

ESG Disclosure Score NEW

ESG RISK RATING 30.24
Updated Jul 08, 2023

High Risk

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

Source: Morningstar

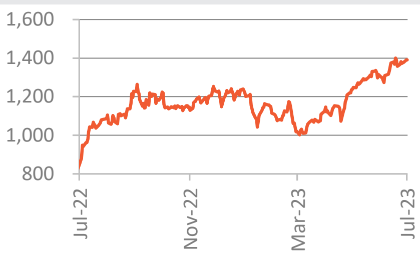
Company details

Market cap:	Rs. 1,07,890 cr
52-week high/low:	Rs. 1,414/ 816
NSE volume: (No of shares)	36.7 lakh
BSE code:	532187
NSE code:	INDUSINDBK
Free float: (No of shares)	65.2 cr

Shareholding (%)

Promoters	16.5
FII	42.3
DII	26.7
Others	14.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.8	21.2	13.7	63.3
Relative to Sensex	1.5	9.7	3.5	39.1

Sharekhan Research, Bloomberg

Key result highlights

- **Strong loan growth and stable margins drive steady NII growth:** NII grew by 18% y-o-y/4% q-o-q, aided by strong growth in advances and stable margins. NIM marginally improved by 1 bps q-o-q to 4.29% despite a 39-bps increase in cost of funds on a q-o-q basis. Cost of deposits increased by 31-bps q-o-q to 6.12% and is expected to peak out by H1FY2024. Increasing retail mix, repricing of corporate book, and higher disbursement yield in the fixed rate book would keep margins stable, thereby offsetting the increase in cost of funds, led by deposit repricing in H1FY2024. The bank is guiding for 4.2-4.3% NIM going forward. We believe NIMs have levers for improvement in H2FY2024 through the asset mix, thereby improving return ratio as cost of funds is expected to peak out in H1FY2024, partly offset by lower yields in the corporate segment.

- **Loan growth was broad-based:** Advances grew by 22% y-o-y/4% q-o-q. The share of retail loans stood at ~54%, with vehicle loans comprising 26%, non-vehicle finance book (mainly business banking, PL, CC, LAP) comprising 17%, and microfinance loans at 11%. The vehicle loan book grew by 21% y-o-y/ 4% q-o-q (slow down seen in tractor and two wheeler segments, while the remaining segments continued to grow at a healthy pace). The non-vehicle book grew by 30% y-o-y/7% q-o-q. The MFI book grew by 9% y-o-y/ down 1% q-o-q. The wholesale corporate book grew by 22% y-o-y/4% q-o-q, led by higher growth in the small corporate book. LCR during the quarter was 132% versus 123% q-o-q. Overall loan growth is expected to be broad-based with the retail and wholesale mix broadly at 55:45. At the same time, the bank is scaling up new product lines such as affluent banking, NRI banking, tractor finance, affordable housing, and merchant advances.

- **Retail deposit growth was strong:** Overall deposits grew by 15% y-o-y/3% q-o-q. CASA deposits grew by 6% y-o-y/3% q-o-q. CA balances grew by 40% y-o-y/down 3% q-o-q, while SA balances picked up sequentially by 6% after the decline seen in the last three quarters as previously there were some outflows on account of bulky government deposits. Retail deposits as per LCR grew by 21% y-o-y/5% q-o-q and now constitute 43% of the overall deposits base. The bank is prioritising on rapid retail deposits mobilisation through – Focus on affluent/NRI deposits, branch expansion along with segmentation based on sectors, increasing digital ecosystem penetration, increased share in current accounts and lastly pricing retail term deposits competitively.

- **Stable asset quality:** Overall, asset quality remained stable across the portfolio; however, slippages from the vehicle segment were higher. GNPA and NNPA ratios were at 1.94% and 0.58%, respectively. PCR was stable at ~ 71%. Total slippages were lower by 16% q-o-q (2.2% annualised versus 2.7% q-o-q). The restructured book declined to 0.66% vs. 0.84% q-o-q. Its SMA 1 and 2 improved to 23 bps vs. 32 bps q-o-q. Slippages were at Rs. 1,376 crore vs. Rs. 1,603 crore q-o-q. Recoveries and upgrades stood at Rs. 541 crore versus Rs. 918 crore q-o-q. Write-offs were at Rs. 720 crore versus Rs. 569 crore q-o-q. Net SR reduced to 44 bps from 51 bps q-o-q. In the vehicle finance segment, slippages were higher q-o-q due to the seasonality factor; while, in the remaining portfolio segments, slippages were lower on a q-o-q basis. The bank expects slippages to normalise in the vehicle segment in the coming quarter.

Results Rs cr

Particulars	1QFY24	1QFY23	4QFY23	Y-o-Y	Q-o-Q
Interest Inc.	10,730	8,182	10,021	31%	7%
Interest Expenses	5,863	4,057	5,351	45%	10%
Net Interest Income	**4,867**	**4,125**	**4,669**	**18%**	**4%**
NIM (%)	4.29	4.21	4.28	2%	0%
Core Fee Income	2,119	1,783	2,087	19%	2%
Other Income	91	146	64	-38%	43%
Net Income	**7,077**	**6,054**	**6,820**	**17%**	**4%**
Employee Expenses	863	660	836	31%	3%
Other Opex	2,384	2,000	2,231	19%	7%
Total Opex	**3,247**	**2,660**	**3,067**	**22%**	**6%**
Cost to Income Ratio	45.9%	43.9%	45.0%		
Pre-Provision Profit	**3,830**	**3,394**	**3,753**	**13%**	**2%**
Provisions & Contingencies - Total	992	1,251	1,030	-21%	-4%
Profit Before Tax	**2,838**	**2,143**	**2,723**	**32%**	**4%**
Tax	715	539	682	33%	5%
Effective Tax Rate	25%	25%	25%		
Reported Profits	**2,124**	**1,603**	**2,041**	**32%**	**4%**
Basic EPS (Rs.)	27.4	20.7	26.3	32%	4%
Diluted EPS (Rs.)	27.3	20.7	26.3	32%	4%
RoA (%)	1.9	1.7	1.9		
Advances	3,01,317	2,47,960	2,89,924	22%	4%
Deposits	3,47,047	3,02,719	3,36,438	15%	3%
Gross NPA	**5,941**	**5,933**	**5,826**	**0%**	**2%**
Gross NPA Ratio (%)	1.94	2.35	1.98		
Net NPA	**1,747**	**1,661**	**1,715**	**5%**	**2%**
Net NPAs Ratio (%)	0.58	0.67	0.59		
PCR – Calculated	70.6%	72.0%	70.6%		

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Deposit mobilisation to be in focus; banks with a superior liability franchise placed better

System-level credit offtake grew by ~15.4% y-o-y in the fortnight ending June 16, 2023, indicating loan growth has been sustaining, given distinct signs of an improving economy, revival of investments, and strong demand. On the other hand, deposits rose by ~12.1%. The gap between advances and deposits growth is narrowing and is expected to further narrow as real deposit rates increase gradually. We should see some moderation in loan growth due to a higher base in FY2024, but loan growth is expected to remain healthy. Margins have likely peaked out in Q4FY2023. The overall asset-quality outlook continues to remain stable to positive for the sector. We believe banks with a robust capital base, strong deposit franchise, and asset quality (with high coverage and provision buffers) are well-placed to capture growth opportunities.

■ Company Outlook – Improving with each passing quarter and the franchise is looking towards a more predictable performance

Focus on strong granular growth, risk management framework, and its strategy to create counter-cyclical buffers will act as cushions. Asset-quality outlook is expected to be stable over the medium term, which should lead to lower slippages and, in turn, reduced credit cost. Near-term business trends look comfortable for the bank and the franchise is looking towards a more predictable performance. Strong loan growth momentum and lower credit cost in the near to medium term augur well for earnings growth.

■ Valuation – We maintain our Buy rating on the stock with a revised PT of Rs. 1,650

At the CMP, IIB trades at 1.7x/1.5x its FY2024E/FY2025E BV estimates. Strong loan growth momentum and lower credit cost are likely to support earnings growth, and this should keep RoEs at ~15% in the near term. Retail is showing strong momentum, while the MFI business is seeing a steady recovery. The corporate book is also growing at a healthy pace. We believe NIMs have levers for improvement in H2FY2024 through the asset mix, thereby improving the return ratio as the cost of funds is expected to peak in H1FY2024. **Key monitorable:** Mobilisation of retail and granular deposits.

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
IndusInd Bank	1,390	1,07,890	11.9	10.2	1.7	1.5	15.4	15.4	1.9	1.9
Federal Bank	135	28,539	7.9	6.9	1.1	1.0	15.6	15.3	1.3	1.3

Source: Company, Sharekhan estimates

About the company

IIB is the fifth largest private bank promoted by Hinduja Group in India. It has a strong pan-India presence with 2,606 branches as of June 2023. The bank is a market leader in most of the product categories in the vehicle finance segment, which forms around 26% of overall loans. Overall, the retail-to-wholesale mix stands at 54:46. The bank is well-placed with adequate capital levels. Capital adequacy ratio (CAR) stands at 18.4%.

Investment theme

IIB has addressed the past challenges and is now focusing on strong granular growth, robust risk management framework, and its strategy to create counter-cyclical buffers, which will act as cushions. Asset-quality outlook is expected to be stable over the medium term, which should lead to lower slippages and, in turn, reduced credit cost. Near-term business trends look comfortable for the bank and the franchise is looking towards a more predictable performance. Strong loan growth momentum and lower credit cost in the near to medium term augur well for earnings growth.

Key Risks

- Economic slowdown that can lead to slower loan growth, higher-than-anticipated credit costs, slow growth in the retail liability franchise.

Additional Data

Key management personnel

Mr. Sumant Kathpalia	CEO and Managing Director
Mr. Arun Khurana	Deputy CEO
Mr. AG Shriram	Head – Consumer Finance
Mr. Sanjeev Anand	Head – Corporate, Commercial, Rural, and Inclusive Banking
Mr. Gobind Jain	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	IndusInd International Holdings Ltd.	11.5
2	AIA Co Ltd	8.2
3	INDUSIND Ltd	3.6
4	Route One Offshore Master Fund	3.3
5	SBI FUNDS MANAGEMENT LTD.	3.3
6	DF International Partners	2.8
7	LIFE INSURANCE CORP OF INDIA	2.8
8	BRIDGE INDIA FUND	2.5
9	DRAGSA INDIA EQUITIES III LP	2.1
10	SFSPVI Ltd	2.1

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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Registration and Contact Details: Name of Research Analyst - Sharekhan Limited, Research Analyst Regn No.: INH000006183. (CIN): - U99999MH1995PLC087498. Registered Office: The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA. Tel: 022-6115000.

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Compliance Officer: Ms. Binkle Oza; Tel: 022-61169602; email id: complianceofficer@sharekhan.com

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