Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

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 30.24

Updated Aug 08, 2023

High Risk

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

Source: Morningstar

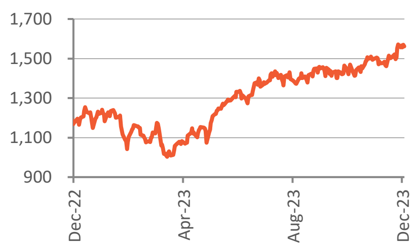
Company details

Market cap:	Rs. 1,22,283 cr
52-week high/low:	Rs. 1,591 / 990
NSE volume: (No of shares)	33.2 lakh
BSE code:	532187
NSE code:	INDUSINDBK
Free float: (No of shares)	66.1 cr

Shareholding (%)

Promoters	16.5
FII	41.5
DII	28.7
Others	13.4

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-0.4	11.1	30.2	31.7
Relative to Sensex	1.5	7.1	20.6	21.2

Sharekhan Research, Bloomberg

IndusInd Bank

Sector Outperformer

Banks	Sharekhan code: INDUSINDBK	
Reco/View: Buy ↔	CMP: Rs. 1,572	Price Target: Rs. 1,850 ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- We maintain a Buy on IndusInd Bank (IIB) with a revised PT of Rs. 1,850. The stock has re-rated itself closer to frontline banks and we expect further re-rating to occur given sustained earnings progression and strengthening of the liability franchise.
- The bank is likely to outpace the sector in terms of earnings growth, led by stable margins, strong loan growth visibility and further improvement in credit costs.
- Key focus is on strengthening the franchise and delivering sustained healthy RoA/RoE trajectory with lower RWA growth.
- The stock trades at 1.7x/1.4x its BV estimates for FY2025E/FY2026E vs. avg RoA trajectory expected at ~2.0% over the next two years. We have added FY26E numbers and have roll forward our valuations to FY26E.

IndusInd Bank (IIB) has been progressing well on guided lines as per the planning cycle and thus the stock has re-rated itself closer to frontline banks and we expect further re-rating to happen given sustained earnings progression and strengthening of liability franchise. Overall loan growth is expected to be broad-based with the retail and wholesale mix broadly at 55:45. The bank is targeting a loan growth of 18-23% y-o-y in FY2024. Net interest margin (NIM) is expected to be stable at ~4.3% despite rise in cost of funds fully offset by an increase in yields and improvement in asset mix. The bank is also speeding up its efforts to improve the retail liability franchise, which is a key positive. About 87% of incremental deposits in the past three years have come from retail term deposits and CASA. Retail deposits as per the LCR are now at 44% versus 26% in FY2019. Increasing share of retail deposits has been a key focus area for the bank. The bank has acknowledged the learning due to the challenges it faced in the past due to higher reliance on wholesale deposits and borrowings.

- **Stable margins:** Despite a sharp rise in cost of deposits (up ~54 bps in H1FY24 from FY23), the bank has still managed to report stable NIMs -~4.3%, led by better yields and mix. The bank further expects ~20 bps increase in cost of deposits in H2FY24. Increasing retail mix, repricing of corporate book, and higher disbursement yield in the fixed rate book would keep margins stable, thereby offsetting the rise in cost of funds, led by deposit repricing. Thus, the bank is guiding for margins at ~4.3% for FY2024. Overall, the sector is reporting lower margins versus stable margins trajectory at the bank, thereby outperforming peers on net Interest income (NII) growth.
- **Strong momentum likely to sustain:** Loans grew by ~21% y-o-y / ~5% q-o-q in H1FY24. Retail advances (excluding microfinance (MFI) and business banking) were up by ~27% y-o-y, showing steady growth. The microfinance book grew by ~16% y-o-y/~7% q-o-q, reflecting improved momentum. Vehicle finance book also showed healthy growth across most segments. The wholesale corporate book grew by 18% y-o-y/3% q-o-q. The bank reported higher than the industry's average growth and loan growth has been broad based. In the retail segment, the bank possesses a strong domain expertise in its focus segments – Vehicle and MFI business. Moreover, its underwriting practices have been tested in this segment as these portfolios have seen a downcycle. The large corporate book is expected to grow in line with the system's growth and the bank is aiming for higher growth in the small corporate book. Additionally, the bank is investing in new growth engines such as affluent banking, NRI banking, tractor finance, affordable housing, and merchant advances. Thus, a well-diversified loan book with a rising share of retail loans along with healthy capital ratios gives strong growth visibility.
- **Asset quality outlook stable, credit costs to fall further:** Overall asset quality trends are broadly stable across the portfolio. Total credit cost stood at 130 bps (as of average advances) in H1FY2024. The bank is guiding for improvement in credit cost by ~20 bps in the coming quarters. Accelerated provisions made in the past few quarters (in turn maintaining healthy PCR at ~71%), lower fresh slippages, and additional non-NPA provision buffer (0.5% of advances) along withunwinding of the restructured book led by recoveries and upgrades will enable further drop in credit cost and would drive strong earnings growth.

Our Call

Valuation – We maintain our Buy rating on the stock with a revised TP of Rs. 1,850.

At CMP, IIB trades at 1.7x/1.4x its FY2025E/FY2026E BV estimates. Strong loan growth momentum, stable NIMs and lower credit cost are likely to support return ratios and earnings trajectory and this should keep RoEs at ~15% in the near to medium term. The stock has re-rated itself closer to frontline banks and we expect further re-rating to happen given sustained earnings progression and strengthening of liability franchise.

Key Risks

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

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E	FY26E
Net Interest Income	15,001	17,592	20,887	24,428	28,974
Net profit	4,611	7,390	9,183	10,336	12,721
EPS (Rs.)	59.5	95.2	118.2	132.7	163.1
P/E (x)	26.4	16.5	13.3	11.8	9.6
P/BV (x)	2.6	2.2	1.9	1.7	1.4
RoE (%)	10.1	14.4	15.5	15.0	15.8
RoA (%)	1.2	1.7	1.9	1.9	2.0

Source: Company; Sharekhan estimates

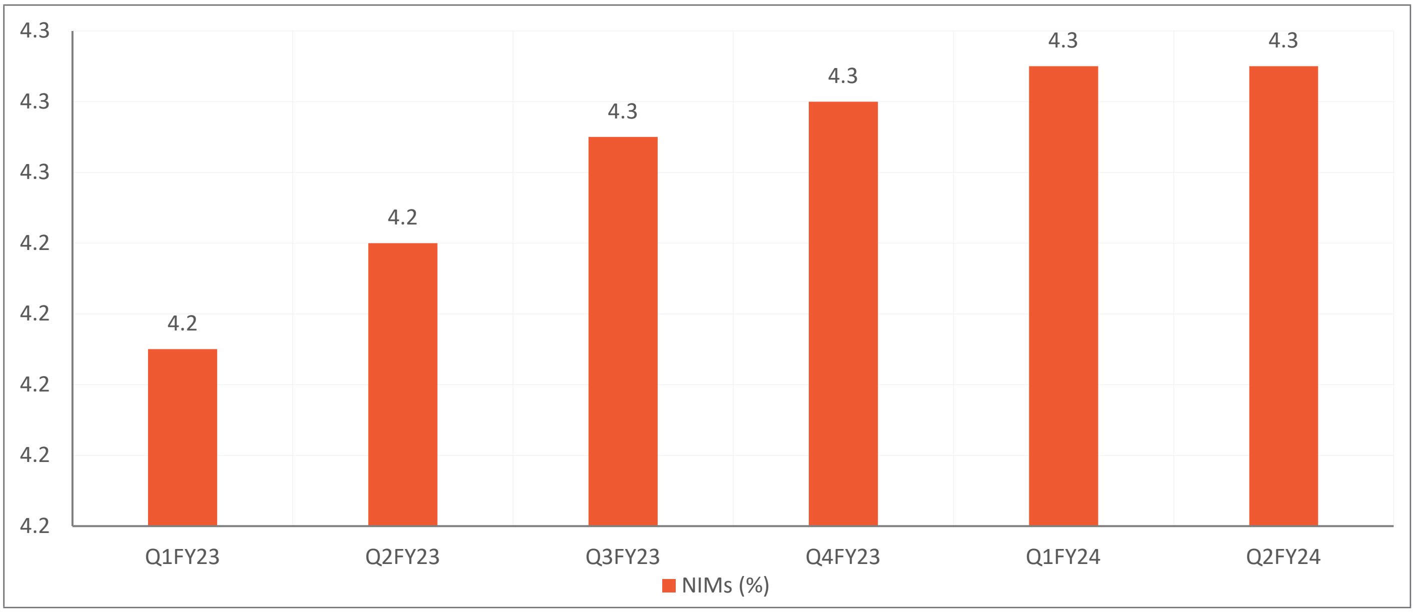
Stock Update

Company Update

NIMs stable despite cost of funds continues to rise sharply

The bank reported stable NIMs at ~4.3% during H1FY24 despite the cost of funds increased by ~54 bps in H1FY24 from FY23. Expectations is that cost of deposits would further inch up by ~20 bps over the next 2 quarters however, it expects to maintain NIM in the target range of 4.2-4.3%. 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.

Trend in NIMs



Source: Company data, Sharekhan Research

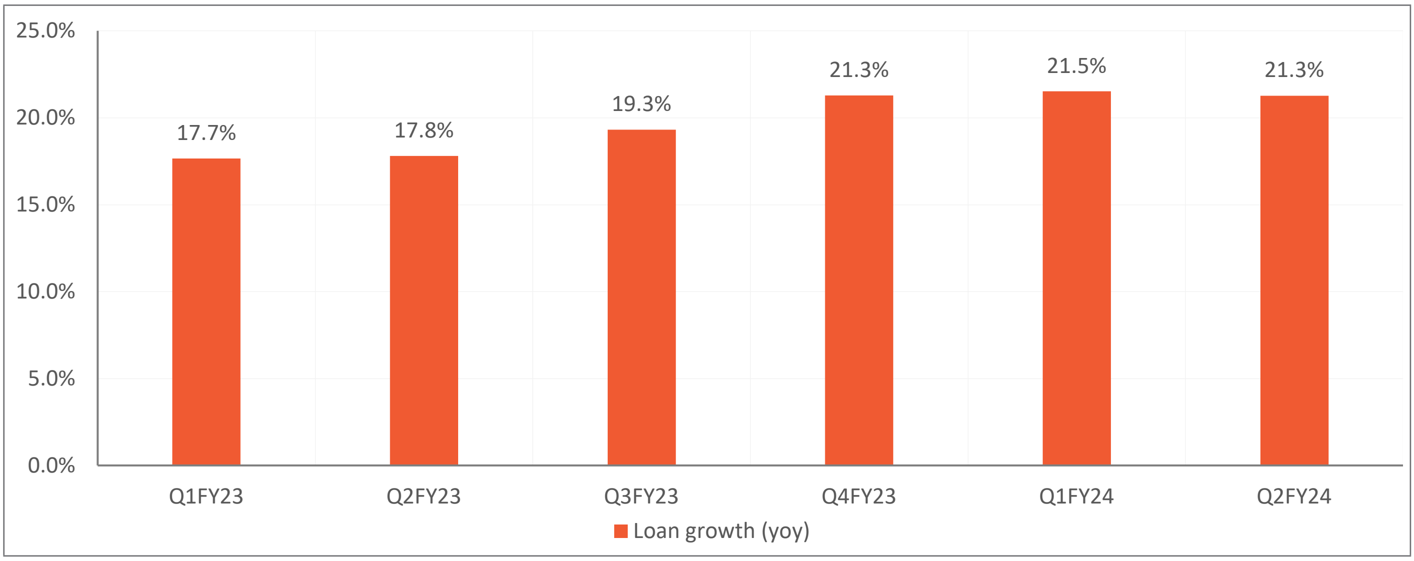
Strong loan growth momentum

The bank has been reporting steady and broad-based growth in loan book higher than industry growth.

It is eyeing strong growth momentum across segments targeting loan growth of 18-23% y-o-y.

The bank's CD ratio stands at ~88%, which is at an elevated level. However, the bank indicated that it is comfortable with the CD ratio in the range of 86-89%.

Trend in Loan growth



Source: Company data, Sharekhan Research

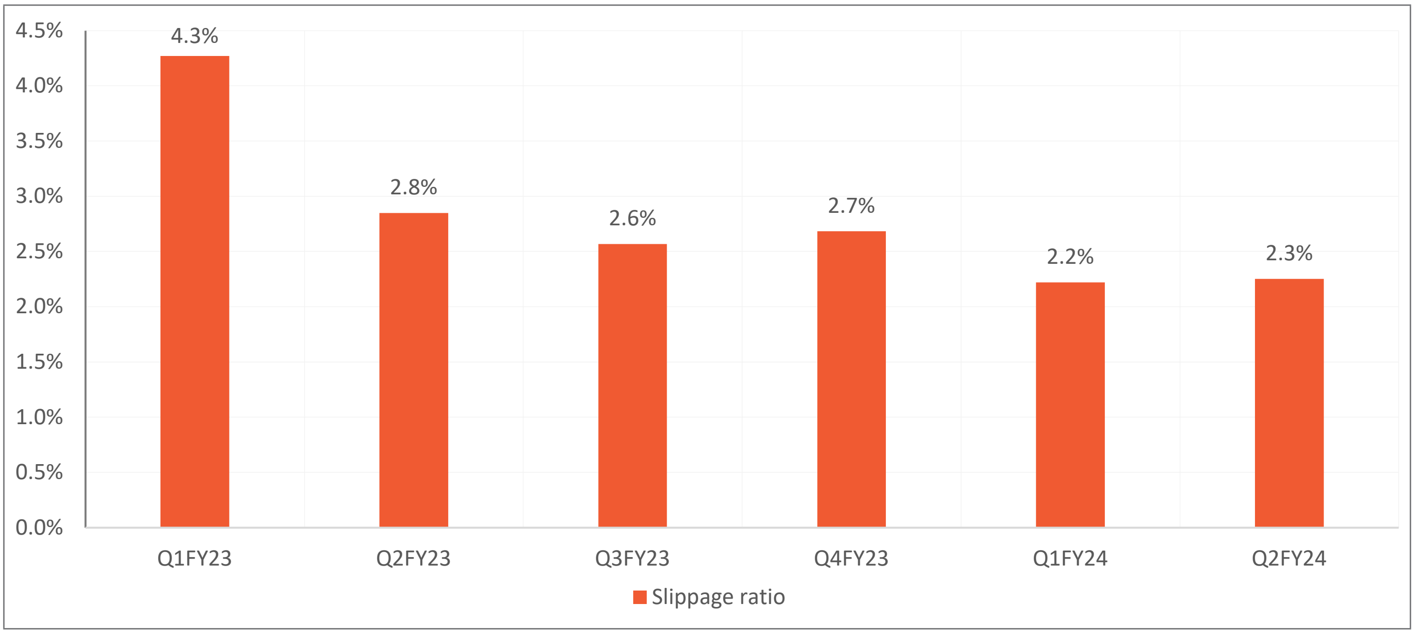
Asset quality outlook stable

Overall asset quality trends are broadly stable across the portfolio. The bank reported fresh slippages of ~Rs 2800 crore (~2.2% of trailing 12M loans) in H1FY24. The bank expects total slippages of ~Rs 5,000 crore during FY2024E. Total credit cost stood at 130 bps (as of average advances) in H1FY2024. The bank is guiding for improvement in credit cost by ~20 bps in the coming quarters.

Accelerated provisions made in the past few quarters (in turn maintaining healthy PCR at ~71%), lower fresh slippages, and additional non-NPA provision buffer (0.5% of advances) along with unwinding of the restructured book led by recoveries and upgrades will enable further drop in credit cost and would drive strong earnings growth.

The bank holds a net Securities receipts book amounting to ~40 bps of advances (down q-o-q from ~45 bps). SMA1 and SMA2 book stood at ~6 bps and ~20 bps of advances, respectively.

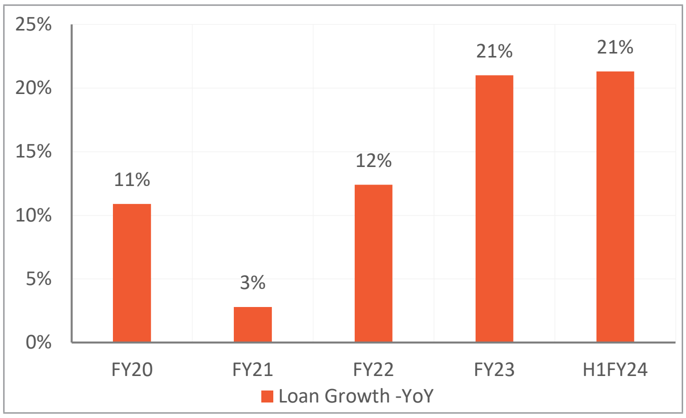
Trend in Slippage ratio



Source: Company data, Sharekhan Research

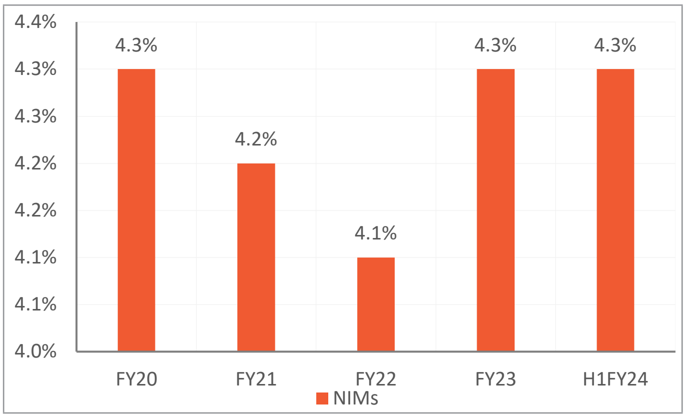
Financials in charts

Trend in Loan Growth



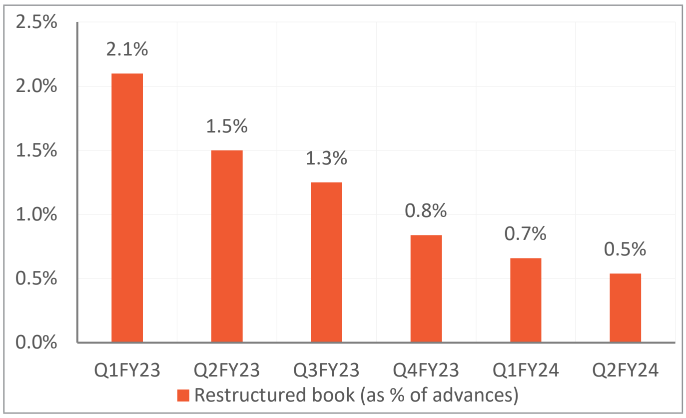
Source: Company, Sharekhan Research

Trend in NIMs



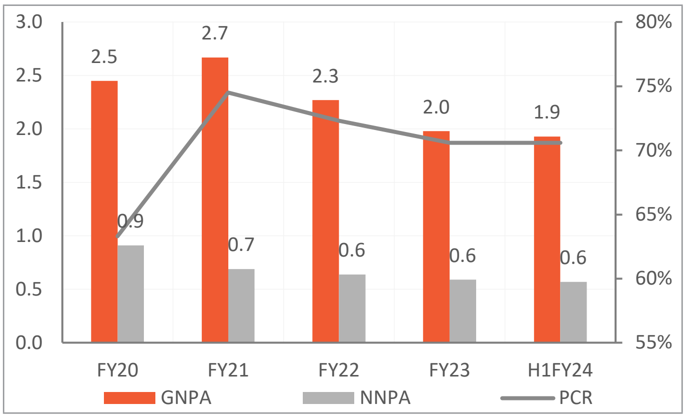
Source: Company, Sharekhan Research

Restructured book likely to fully run down by FY24



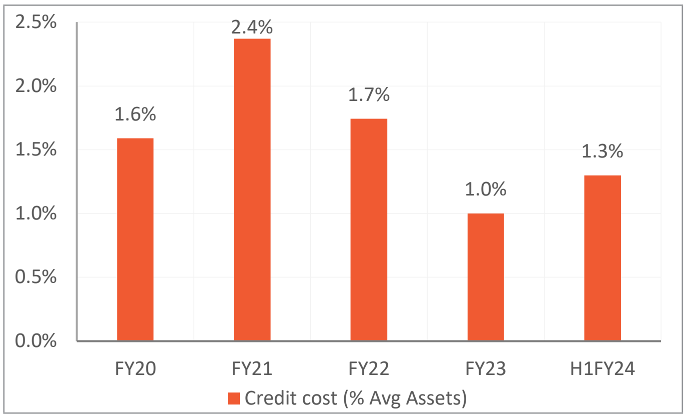
Source: Company, Sharekhan Research

Trend in Asset Quality



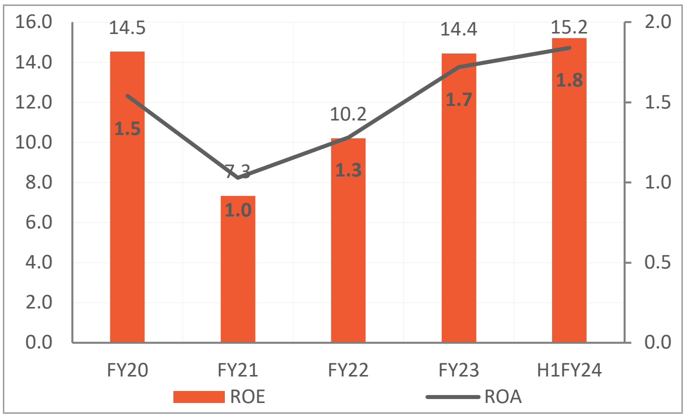
Source: Company, Sharekhan Research

Trend in Credit Cost



Source: Company, Sharekhan Research

Trend in Return Ratios



Source: Company, Sharekhan Research

Outlook and Valuation

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

System-level credit offtake grew by ~20.8% y-o-y in the fortnight ending December 01, 2023, indicating loan growth has been strong, given distinct signs of an improving economy, revival of investments, and strong demand. On the other hand, deposits rose by ~13.8%. 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 going ahead, but loan growth is expected to remain healthy. Margins have peaked out in Q4FY2023 and are expected to be lower going ahead led by repricing of deposit cost given limited room for repricing of asset book . 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**

IIB has navigated the past challenges and is progressing well on expected lines. Overall asset-quality outlook is expected to remain stable in the near to 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, stable NIMs, 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 TP of Rs. 1,850.**

At CMP, IIB trades at 1.7x/1.4x its FY2025E/FY2026E BV estimates. Strong loan growth momentum, stable NIMs and lower credit cost are likely to support return ratios and earnings trajectory and this should keep RoEs at ~15% in the near to medium term. The stock has re-rated itself closer to frontline banks and we expect further re-rating to happen given sustained earnings progression and strengthening of liability franchise.

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	1,572	1,22,283	13.3	11.8	1.9	1.7	15.5	15.0	1.9	2.0
Federal Bank	154	37,456	10.0	8.8	1.3	1.1	14.6	13.7	1.3	1.3

Source: Company, Sharekhan estimates

About company

IIB is the fifth largest private bank promoted by Hinduja Group in India. It has a strong pan-India presence with 2,631 branches as of Sep 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 55:45. The bank is well-placed with adequate capital levels. Capital adequacy ratio (CAR) stands at 18.2%.

Investment theme

IIB is focusing on broad based granular growth with robust risk management framework, and its strategy to create counter-cyclical buffers will strengthen the franchise. Asset-quality outlook is expected to be stable in near term. Near-term business trends look comfortable for the bank and the franchise is looking towards a more predictable performance. Strong loan growth momentum, stable NIMs and lower credit cost in the near 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. Gobind Jain	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	IndusInd International Holdings Ltd.	11.52
2	AIA Co Ltd	8.17
3	INDUSIND Ltd	3.60
4	Route One Offshore Master Fund	3.27
5	SBI FUNDS MANAGEMENT LTD.	2.99
6	DF International Partners	2.77
7	LIFE INSURANCE CORP OF INDIA	2.76
8	BRIDGE INDIA FUND	2.46
9	DRAGSA INDIA EQUITIES III LP	2.12
10	HDFC AMC Co. Ltd	2.10

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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