REDUCE (Maintain)

CMP: **INR 901** Target Price: **INR 850** ▼ -6%

ICICI Securities

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11 March 2025

India | Equity Research | Company Update

IndusInd Bank

Banking

Bank reports discrepancy in derivative book

IndusInd Bank (IIB) has communicated a preliminary one-time hit of ~2.35% of net-worth on its derivative portfolio. We peg the pre-tax hit at ~INR 20bn–21bn. IIB mentioned that these derivative positions pertain to foreign currency deposits/borrowings conversion and not to any client/industry exposure. Since 1 Apr'24, the bank has stopped internal hedging, post which, around Sep'24, it identified the discrepancies. The hit is likely to be routed through P&L in Q4FY25, which in our view, could severely dent reported profitability; may even report a loss in Q4FY25. We recently downgraded the stock to **REDUCE** (link here) on the curtailed term extension of the incumbent MD & CEO. We believe the discrepancies reflect poorly on internal control. Maintain **REDUCE**.

Bank reports ~INR 20bn–21bn discrepancies in derivative book

During an internal review of processes relating to other asset and other liability accounts of its derivative portfolio, post implementation of RBI's new regulations effective 1 Apr'24, IIB noted discrepancies in these account balances. The bank's internal review has estimated an adverse impact of ~2.35% of net-worth. We believe the hit is on a post-tax basis; in an absolute term, the hit comes out at ~INR 20-21bn. IIB has also appointed a reputed external agency to independently review. The final report of the external agency is likely to be out by end-Mar'25.

Reflects poorly on internal control; Q4FY25 may report loss

The bank mentioned that these derivative positions pertain to foreign currency deposits/borrowings conversion. In simple words, while the MTM on external hedge was reflecting true picture, the internal hedge had different methodology; leading to the bank over-reporting NII / trading gains and thus overall profits. The discrepancy was visible in cases where the actual tenure of the internal and external legs was not similar due to premature rundown. Since 1 Apr'24, IIB has stopped the internal hedging, post which, around Sep'24, it identified the discrepancies. We believe this reflects poorly on internal controls. The hit is likely to run through P&L, and the bank could even report a loss in Q4FY25.

Maintain REDUCE on heightened near-term uncertainty

We maintain our recently downgraded rating on IIB at **REDUCE** (link). Our TP of INR 850 remains unchanged, valuing the stock at ~0.9x FY26E ABV. **Risks**: Better-than-expected growth; and seamless management transition.

Financial Summary

Y/E March	FY24A	FY25E	FY26E	FY27E
NII (INR bn)	206.2	211.8	239.0	281.4
Op. profit (INR bn)	157.4	145.7	159.4	192.5
Net Profit (INR bn)	89.5	60.6	75.2	96.0
EPS (INR)	115.0	77.8	96.6	123.4
EPS % change YoY	20.7	(32.3)	24.2	27.7
ABV (INR)	784.1	844.2	924.1	1,025.4
P/BV (x)	1.1	1.0	0.9	0.8
P/ABV (x)	1.1	1.1	1.0	0.9
Return on Assets (%)	1.8	1.1	1.3	1.4
Return on Equity (%)	15.3	9.3	10.6	12.3

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Market Data

Market Cap (INR)	702bn
Market Cap (USD)	8,032mn
Bloomberg Code	IIB IN
Reuters Code	INBK.BO
52-week Range (INR)	1,576 /881
Free Float (%)	85.0
ADTV-3M (mn) (USD)	59.8

Price Performance (%)	3m	6m	12m
Absolute	(8.5)	(37.3)	(42.4)
Relative to Sensex	0.6	(27.7)	(42.4)

ESG Score	2023	2024	Change
ESG score	**80.4**	**80.2**	**(0.2)**
Environment	75.2	77.6	2.4
Social	74.5	74.6	0.1
Governance	86.6	85.5	(1.1)

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: SES ESG, I-sec research

Previous Reports

09-03-2025: Company Update

20-02-2025: Banking: Q3FY25 review

Takeaways and our reading from the conference call

Bank identifies ~INR 20-21bn hit on derivative portfolio

- During an internal review of processes relating to other asset and other liability accounts of the derivative portfolio, post implementation of RBI Master Direction, applicable from 1 Apr'24, the bank noted some discrepancies in these account balances.
- The bank's internal review estimates an adverse impact of ~2.35% of net-worth.
- The above is post tax; thus, the pre-tax is even higher at ~INR 20–21bn.
- The hit is unlikely to be adjusted through General Reserves and would be routed through P&L.
- The difference has been accumulated with time and pertains to FY24, or earlier period.

Nature and cause of discrepancy

- The derivative position pertains to foreign currency deposits/borrowings conversion to INR. The derivative does not pertain to any client or industry exposure. The bank has been following the same practices/procedures for the last 5–7 years.
- The external trade was marked to market (MTM) which recorded the true value at period end. The internal trade was accounted using SWAP cost, impacting assets book (vs P&L). This would not create any difference if the underlying exposure would run its contractual tenure as both legs of the trade would set-off at the end of the period.
- However, in case, the exposure runs down prematurely, the external trade would record MTM immediately while internal trade was not adequately reflecting the true picture. In a way, the bank had instances of over-reported profitability.

Identification and action plan

- Since 1 Apr'24, the bank has stopped the internal hedging. Post which, around Sep'24, it identified some discrepancies.
- The discrepancies were identified internally. IIB has appointed an external auditor.
- The final report of the external agency is likely to be out by end-Mar'25. The final hit may be too early to compute as external investigation is ongoing. However, it believes that the final hit should be broadly around its estimates.

RBI supervision and succession

- CFO resignation did not have anything to do with this discrepancy, as per the bank.
- RBI risk-based supervision exercise had already concluded in Sep–Oct'24.
- No explanation given by RBI on one-year term extension. Board shall evaluate internal and external candidates for the MD & CEO position.

MFI

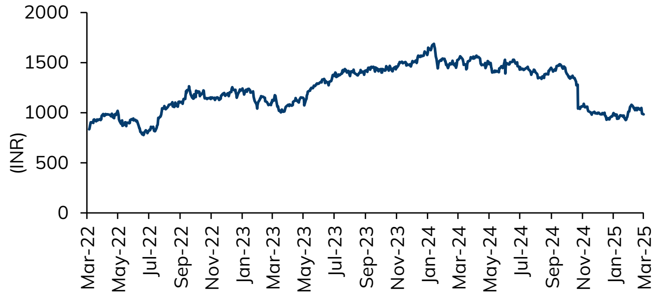
- On MFI, IIB mentioned that flow from X bucket is trending well, except for Karnataka, where flows are now stabilising. However, forward flow from bucket may continue to run through.
- Q4 may have some adverse impact; however, it is expected to start recovery from Q1FY26 onwards.

Exhibit 1: Shareholding pattern

	Jun'24	Sep'24	Dec'24
Promoters	16.4	16.4	16.3
Institutional investors	65.8	69.1	65.0
MFs and others	19.9	22.7	30.3
FIs/Bank	0.8	2.5	0.7
Insurance Cos.	6.7	9.3	9.3
FIIs	38.4	34.6	24.7
Others	17.8	14.5	18.7

Source: Bloomberg, I-Sec research

Exhibit 2: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 3: Profit & Loss

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
Interest income	4,57,482	5,08,898	5,63,383	6,39,101
Interest expense	2,51,323	2,97,143	3,24,344	3,57,657
Net interest income	**2,06,159**	**2,11,755**	**2,39,039**	**2,81,445**
Non-interest income	93,879	94,740	1,04,277	1,21,476
Operating income	**3,00,038**	**3,06,495**	**3,43,316**	**4,02,921**
Operating expense	1,42,635	1,60,750	1,83,895	2,10,384
Staff expense	38,953	43,741	49,158	55,221
Operating profit	**1,57,403**	**1,45,745**	**1,59,421**	**1,92,537**
Core operating profit	**1,53,319**	**1,42,745**	**1,56,421**	**1,88,037**
Provisions & Contingencies	37,987	64,795	58,920	64,188
Pre-tax profit	**1,19,415**	**80,950**	**1,00,501**	**1,28,349**
Tax (current + deferred)	29,918	20,375	25,296	32,305
Net Profit	**89,498**	**60,575**	**75,205**	**96,044**
Adjusted net profit	**89,498**	**60,575**	**75,205**	**96,044**

Source Company data, I-Sec research

Exhibit 4: Balance sheet

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
Cash and balance with RBI/Banks	3,68,016	4,18,489	4,81,546	5,49,798
Investments	10,65,267	11,55,496	12,55,752	14,03,857
Advances	34,32,983	37,48,246	41,14,582	46,73,480
Fixed assets	21,977	25,111	28,324	34,623
Other assets	2,61,108	3,13,875	3,85,896	4,76,477
Total assets	**51,49,352**	**56,61,217**	**62,66,101**	**71,38,234**
Deposits	38,47,929	42,87,090	48,01,721	54,99,376
Borrowings	4,76,114	4,94,601	5,48,793	6,09,488
Other liabilities and provisions	1,97,337	1,99,460	1,70,845	2,02,030
Share capital	7,783	7,783	7,783	7,783
Reserve & surplus	6,20,188	6,72,282	7,36,958	8,19,556
Total equity & liabilities	**51,49,352**	**56,61,217**	**62,66,101**	**71,38,234**
% Growth	12.5	9.9	10.7	13.9

Source Company data, I-Sec research

Exhibit 5: Key ratios

(Year ending March)

	FY24A	FY25E	FY26E	FY27E
No. of shares and per share data				
No. of shares (mn)	778	778	778	778
Adjusted EPS	115.0	77.8	96.6	123.4
Book Value per share	803	870	953	1,059
Adjusted BVPS	784	844	924	1,025
Valuation ratio				
PER (x)	7.8	11.6	9.3	7.3
Price/ Book (x)	1.1	1.0	0.9	0.9
Price/ Adjusted book (x)	1.1	1.1	1.0	0.9
Dividend Yield (%)	1.8	1.2	1.5	1.9
Profitability ratios (%)				
Yield on advances	12.0	11.6	11.8	12.0
Yields on Assets	9.4	9.4	9.4	9.5
Cost of deposits	6.0	6.4	6.3	6.2
Cost of funds	5.2	5.5	5.4	5.3
NIMs	4.5	4.2	4.3	4.5
Cost/Income	47.5	52.4	53.6	52.2
Dupont Analysis (as % of Avg Assets)				
Interest Income	9.4	9.4	9.4	9.5
Interest expended	5.2	5.5	5.4	5.3
Net Interest Income	**4.2**	**3.9**	**4.0**	**4.2**
Non-interest income	1.9	1.8	1.7	1.8
Trading gains	0.1	0.1	0.1	0.1
Fee income	1.8	1.7	1.7	1.7
Total Income	**6.2**	**5.7**	**5.8**	**6.0**
Total Cost	**2.9**	**3.0**	**3.1**	**3.1**
Staff costs	0.8	0.8	0.8	0.8
Non-staff costs	2.1	2.2	2.3	2.3
Operating Profit	**3.2**	**2.7**	**2.7**	**2.9**
Core Operating Profit	3.2	2.6	2.6	2.8
Non-tax Provisions	0.8	1.2	1.0	1.0
PBT	**2.5**	**1.5**	**1.7**	**1.9**
Tax Provisions	0.6	0.4	0.4	0.5
Return on Assets (%)	**1.8**	**1.1**	**1.3**	**1.4**
Leverage (x)	8.3	8.3	8.4	8.6
Return on Equity (%)	**15.3**	**9.3**	**10.6**	**12.3**
Asset quality ratios (%)				
Gross NPA	1.9	2.3	2.6	2.9
Net NPA	0.6	0.7	0.7	0.8
PCR	70.6	70.0	72.0	75.0
Gross Slippages	2.1	2.3	2.0	2.0
LLP / Avg loans	1.0	1.2	1.3	1.3
Total provisions / Avg loans	1.2	1.8	1.5	1.5
Net NPA / Networth	3.1	3.9	4.0	4.2
Capitalisation ratios (%)				
Core Equity Tier 1	15.8	15.0	15.0	14.7
Tier 1 cap. adequacy	15.8	15.0	15.0	14.7
Total cap. adequacy	17.2	16.3	16.1	15.7

Source Company data, I-Sec research

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