

Equities

15 October 2010 | 10 pages

AXIS Bank (AXBK.BO)

2Q11 Results: Growing – Steadily but Surely

- **2Q11 profits up 38%; in line with our estimates** — Axis had another strong quarter – profits were up 38% yoy, led by robust loan growth, pickup in fee income and stable net interest margins. While the P&L could have some concerns, (fees, costs and provisioning), the balance sheet looks fine – growth is high (and more balanced), deposit mix remains strong and asset quality well under control. There will likely be some moderation in growth, but returns are likely to sustain.
- **P&L appears to be largely derisked** — Axis's NIMs were largely stable at 368bps (management guides for some more moderation), treasury gains declined further, operating costs were higher and so were provisioning levels. We believe the current moderated P&L structure reflects a consolidation in the bank's growth profile – it has room to cushion some impact of a moderation in margins and appears more sustainable medium term.
- **Balanced growth, strong deposit mix, but slippages remain high** — Loan book growth at 36.5% yoy was strong, but is moderating (+1.8% qoq) and should come down further. However, it is more balanced than the past (though slightly skewed toward large, mid corporates) and also more granular – we believe better balances its risk profile. Asset quality deterioration remained high (2% slippage again) and management remains watchful, says retail NPLs have peaked but SME, restructured portfolio could slip. Overall though, NPLs are well under control, coverage is up to 80%, credit costs likely to reduce, but only gradually.
- **Raising earnings, target price, Maintain Hold (2L)** — We transfer primary coverage to Manish Chowdhary from Aditya Narain, raise our FY11-12E earnings 6-7% & EVA-based TP to Rs1,630 (benchmarked off 3x FY12 P/BV) incorporating higher NIMs. The stock has outperformed by 20% in 6 months, reflects sustainability of its operating and return profile, but also leaves little room for further gains.

Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2009A	18,154	48.84	50.9	32.0	5.5	19.1	0.7
2010A	25,145	63.51	30.0	24.6	3.9	19.2	0.9
2011E	32,726	78.10	23.0	20.0	3.4	18.8	1.0
2012E	39,523	94.32	20.8	16.6	2.9	19.4	1.0
2013E	46,517	111.01	17.7	14.1	2.4	19.4	1.1

Source: Powered by dataCentral

- Company Update
- Target price change
- Estimate change
- Transfer of coverage

Hold/Low Risk	2L
Price (14 Oct 10)	Rs1,563.45
Target price	Rs1,630.00
	from Rs1,335.00
Expected share price return	4.3%
Expected dividend yield	1.0%
Expected total return	5.2%
Market Cap	Rs639,203M
	US\$14,408M

Price Performance (RIC: AXBK.BO, BB: AXSB IN)



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Fiscal year end 31-Mar	2009	2010	2011E	2012E	2013E
Valuation Ratios					
P/E adjusted (x)	32.0	24.6	20.0	16.6	14.1
P/E reported (x)	32.0	24.6	20.0	16.6	14.1
P/BV (x)	5.5	3.9	3.4	2.9	2.4
P/Adjusted BV diluted (x)	5.7	4.1	3.5	3.0	2.5
Dividend yield (%)	0.7	0.9	1.0	1.0	1.1
Per Share Data (Rs)					
EPS adjusted	48.84	63.51	78.10	94.32	111.01
EPS reported	48.84	63.51	78.10	94.32	111.01
BVPS	284.50	395.99	461.76	543.31	641.11
Tangible BVPS	284.50	395.99	461.76	543.31	641.11
Adjusted BVPS diluted	273.93	382.90	446.50	525.35	619.92
DPS	11.71	14.01	15.00	16.00	17.00
Profit & Loss (RsM)					
Net interest income	36,862	50,045	63,696	75,739	90,115
Fees and commissions	21,733	25,652	32,065	39,440	47,328
Other operating Income	7,236	13,806	11,497	13,525	16,211
Total operating income	65,831	89,503	107,258	128,703	153,654
Total operating expenses	-28,582	-37,097	-46,648	-57,143	-68,952
Oper. profit bef. provisions	37,249	52,406	60,610	71,561	84,702
Bad debt provisions	-9,032	-14,126	-10,775	-11,378	-13,924
Non-operating/exceptionals	-362	234	-250	-300	-299
Pre-tax profit	27,855	38,514	49,585	59,883	70,479
Tax	-9,701	-13,368	-16,859	-20,360	-23,963
Extraord./Min. Int./Pref. Div.	0	0	0	0	0
Attributable profit	18,154	25,145	32,726	39,523	46,517
Adjusted earnings	18,154	25,145	32,726	39,523	46,517
Growth Rates (%)					
EPS adjusted	50.9	30.0	23.0	20.8	17.7
Oper. profit bef. prov.	67.3	40.7	15.7	18.1	18.4
Balance Sheet (RsM)					
Total assets	1,477,220	1,806,479	2,225,327	2,666,544	3,196,064
Avg interest earning assets	1,204,744	1,556,187	1,927,868	2,349,152	2,822,494
Customer loans	821,274	1,052,421	1,311,717	1,612,170	1,980,813
Gross NPLs	8,978	13,180	18,574	24,613	30,596
Liab. & shar. funds	1,477,220	1,806,479	2,225,327	2,666,544	3,196,064
Total customer deposits	1,173,741	1,413,002	1,766,253	2,131,858	2,574,949
Reserve for loan losses	5,706	8,990	15,261	19,883	24,968
Shareholders' equity	102,136	160,446	187,094	220,135	259,762
Profitability/Solvency Ratios (%)					
ROE adjusted	19.1	19.2	18.8	19.4	19.4
Net interest margin	3.06	3.22	3.30	3.22	3.19
Cost/income ratio	43.4	41.4	43.5	44.4	44.9
Cash cost/average assets	2.2	2.3	2.3	2.3	2.4
NPLs/customer loans	1.1	1.3	1.4	1.5	1.5
Reserve for loan losses/NPLs	63.6	68.2	82.2	80.8	81.6
Bad debt prov./avg. cust. loans	1.3	1.5	0.9	0.8	0.8
Loans/deposit ratio	70.0	74.5	74.3	75.6	76.9
Tier 1 capital ratio	9.3	11.2	10.0	9.5	9.1
Total capital ratio	13.7	15.8	15.2	14.8	14.1

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Figure 1. Axis Bank: 2Q11 Results: Key Highlights (Rupees Million, Percent)

	2Q11	2Q10	YoY %	1Q11	QoQ%	CIRA Comments
Interest Income	36,243	28,604	26.7	33,256	9.0	
Interest Expense	(20,092)	(17,107)	17.4	(18,118)	10.9	
Net Interest Income	16,151	11,497	40.5	15,138	6.7	NIMs slightly better than expected
Fee-Based Income	9,248	8,416	9.9	7,430	24.5	Overall moderate - sluggish growth especially for third party product distribution
Other Non-Interest Income	1,084	2,240	-51.6	2,578	-57.9	Falling trend continues, though sharper than expected
Non Interest Income	10,332	10,656	-3.0	10,008	3.2	
Operating Income	26,483	22,153	19.5	25,146	5.3	
Operating Expenses	(11,620)	(9,095)	27.8	(10,645)	9.2	Higher employee costs and branch network expansion push expenses up; management expects expense growth to remain at current levels
Pre-Provision Profit	14,864	13,058	13.8	14,501	2.5	
Charges for Bad Debts	(3,210)	(5,040)	-36.3	(3,040)	5.6	Above estimates; management appears more confident of arresting slippages than earlier, though falls short of specific guidance
Other Operating Items	(578)	51	NM	(290)	99.2	
Operating Profit	11,076	8,069	37.3	11,171	-0.8	
Tax	(3,725)	(2,752)	35.3	(3,752)	-0.7	
Net Profit	7,351	5,316	38.3	7,419	-0.9	Overall in-line with estimates; qualitatively healthy with strong growth and relatively stable NIMs
Customer Loans	1,105,928	810,444	36.5	1,086,090	1.8	Management says growth is likely to remain a bit sluggish, expects to grow at 30% above industry levels
Customer Deposits	1,568,871	1,155,990	35.7	1,474,790	6.4	Healthy savings deposits growth drives low cost deposit base to a robust 41.5%
AIEA	1,754,079	1,307,063	34.2	1,633,217	7.4	
AIBL	1,715,136	1,155,990	48.4	1,627,818	5.4	
Total Assets	1,998,331	1,517,135	31.7	1,894,590	5.5	
Avg Assets	2,014,587	1,464,278	37.6	2,797,830	-28.0	
Non-Performing Loans (NPL)	13,624	11,317	20.4	13,409	1.6	Overall slippages still around 2% - especially coming from SME. While retail portfolio is stabilizing, slippage from restructured book likely to continue
Loan Loss Reserves (LLR)	(9,530)	(7,150)	33.3	(9,245)	3.1	
Shareholders' Funds	176,822	145,590	21.5	168,890	4.7	
Book Value Per Share	432	362	19.4	418	3.4	Tier 1 capital adequacy at 10.68% including profits for 1H11
Key Ratios (%)	2Q11	2Q10	Bps Δ YoY	1Q11	Bps Δ QoQ	
ROAA (annualized)	1.46	1.45	1	1.06	40	
ROAE (annualized)	16.63	14.61	202	17.57	-94	
Net Interest Margin (bps)	368	352	16	371	-244	NIMs down 3bps qoq, better than expected - management continues to guide lower
Fee Inc/Operating Income	34.9	38.0	-307	29.5	537	
Other Non-Interest Inc/Op Inc	39.0	48.1	-909	39.8	-78	
Op. Cost/ Operating Income	43.9	41.1	282	42.3	154	Expect costs to remain at elevated levels
Loan-to-Deposit Ratio (LDR)	70.5	70.1	38	73.6	-315	
NPL/Loan Ratio	1.2	1.4	-16	1.23	0	
LLR/NPL Ratio	70	63	678	69	101	80.2% coverage levels including written off accounts

Source: Company Reports, CIRA

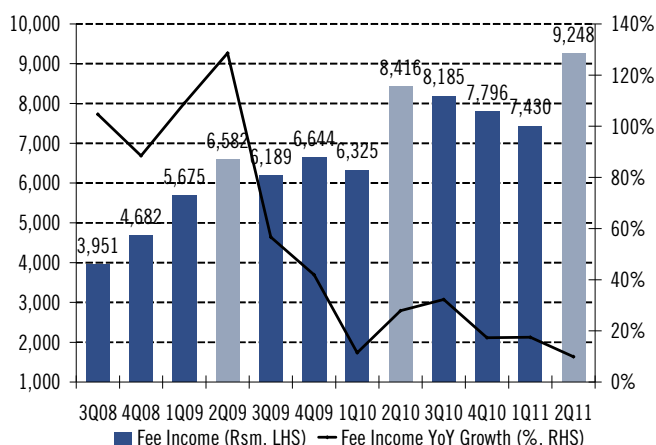
Figure 2. Axis Bank: 2Q11 Deposit and Loan Profile (Rupees Million, Percent)

Deposit Profile	2Q11	2Q10	YoY %	1Q11	QoQ%
Savings	378,120	280,070	35.0	347,030	9.0
Current	273,740	214,550	27.6	245,460	11.5
Low Cost Deposits	651,860	494,620	31.8	592,490	10.0
Term	917,010	661,370	38.7	882,300	3.9
Total Deposits	1,568,870	1,155,990	35.7	1,474,790	6.4
% CASA	41.5	42.8	-123.8	40.2	3.4

Loan Mix	2Q11	2Q10	YoY %	1Q11	QoQ%
Corporate	608,260	559,620	8.7	597,350	1.8
SME	168,120	-	NM	173,774	-3.3
Agricultural	90,730	70,980	27.8	108,609	-16.5
Retail	210,010	179,840	16.8	206,357	1.8
Total Advances	1,077,120	810,440	32.9	1,086,090	-0.8

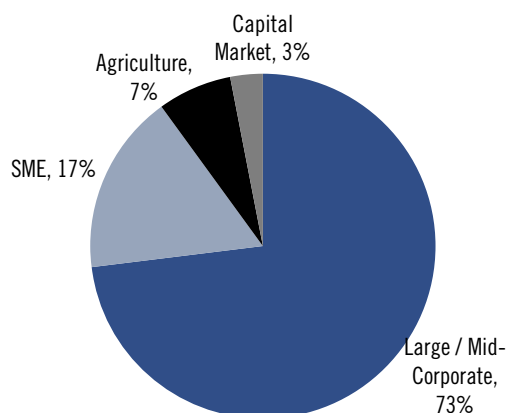
Source: Company Reports

Figure 3. Fee Income (Rsm) and its YoY Growth (%)



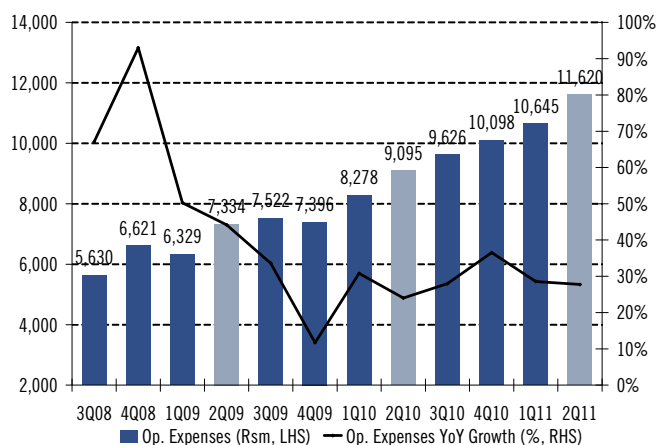
Source: Company Reports

Figure 5. Loans Restructured in 1QFY11 - Portfolio Break up (%)



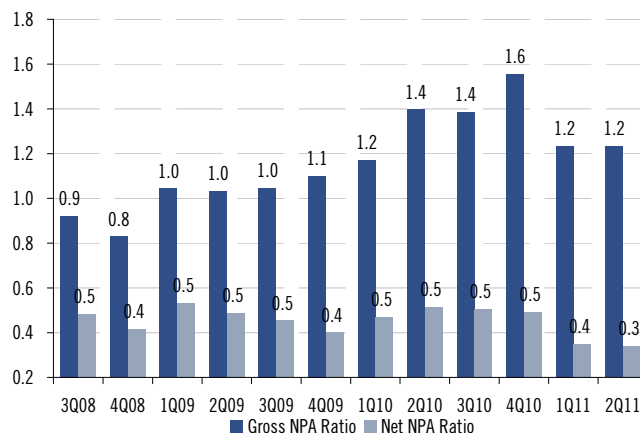
Source: Company Reports

Figure 4. Operating Expenses (Rsm) and its YoY Growth (%)



Source: Company Reports

Figure 6. Gross NPA and Net NPA Ratios (%)



Source: Citi Investment Research and Analysis

Figure 7. Earnings Revision Summary

	Net Profit			EPS			DPS		
	Old	New	% change	Old	New	% change	Old	New	% change
FY11E	30,798	32,726	6.3	73.5	78.1	6.3	12.5	15.0	20.0
FY12E	36,934	39,523	7.0	88.1	94.3	7.0	13.0	16.0	23.1
FY13E	NA	46,516	NA	NA	111.0	NA	NA	17.0	NA

Source: Citi Investment Research and Analysis estimates

AXIS Bank

Valuation

Our target price of Rs1,630 is based on an EVA model using the following key assumptions: a) risk-free rate of 8.0%, b) long-term loan loss of 100bps per annum (in-line with sector averages), and c) long-term cost-to-income ratio of 39%. We prefer using an EVA-based valuation benchmark to P/BV because EVA concentrates on the economic value creation of the bank. We use P/BV as a secondary valuation methodology. Believing that Axis should trade above government banks and in line with the highest multiples for large private-sector banks given its ROE, we ascribe 3.0x FY12E P/B to Axis, equating to Rs1,629.

Risks

We rate Axis Bank as Low Risk, in line with our quantitative risk-rating system, and to reflect the bank's well diversified loan portfolio and relatively healthy asset quality, along with its sustained high profitability. Key downside risks to achieving our target price include: 1) Greater than expected asset quality pressures, as Axis has grown rapidly; 2) Sharp slowdown in rapidly growing fee income; 3) The bank's large share of wholesale funding could be exposed to tighter funding; 4) Dependence on treasury returns; 5) New CEO, with possible clean-up and/or repositioning; and 6) A government-related entity is a dominant shareholder in Axis; any disorderly sale would have an impact on the stock. Key upside risks to our target price include: a) Stronger than expected economic recovery leading to a reversal in asset quality concerns; b) Sharp revival in loan growth; c) Continued easy liquidity and soft interest rate environment; and d) Rapid growth in fee income levels given its continued focus on distribution build-out.

Appendix A-1

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AXIS Bank (AXBK.BO)

Ratings and Target Price History

Fundamental Research

Analyst: Aditya Narain, CFA

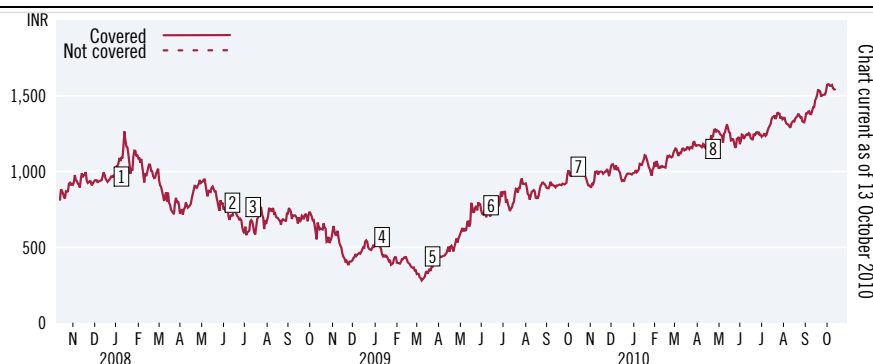


Chart current as of 13 October 2010

	Date	Rating	Target Price	Closing Price
1	9-Jan-08	2L	*1,215.00	1,095.60
2	13-Jun-08	*1L	*912.00	704.35
3	14-Jul-08	1L	*807.00	635.80

	Date	Rating	Target Price	Closing Price
4	11-Jan-09	1L	*710.00	485.75
5	24-Mar-09	*1M	*470.00	372.30
6	14-Jun-09	1M	*920.00	703.45

	Date	Rating	Target Price	Closing Price
7	15-Oct-09	*2M	*1,125.00	1,006.25
8	23-Apr-10	*2L	*1,335.00	1,233.40

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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