

# Axis Bank

Rs846

**OUTPERFORMER**

EVENT UPDATE: ALL FOR GOOD REASON!

**Mkt Cap: Rs303.6bn; US\$6.4bn**

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Axis Bank plans to raise capital, ~Rs60bn at current market price, implying an upto ~20% dilution of current equity base. The capital raising comes in the context of reviving credit growth potential and consequently depleting Tier-I CRAR, and plausible organic/inorganic foray into the life insurance business given the CEO's strong credentials. Whilst myopically the capital raising appears to be RoE dilutive (down by ~370bp in FY10E and ~550bp in FY11E), given the durability of the bank's RoA (and thereby sustainable RoE) in turn buoyed by its strong liability franchise and sticky fee income business, we are convinced that any correction offers an attractive entry point. Historically, the stock has rallied around capital raisings, with the one on the anvil likely to be no exception. We are currently maintaining our earning estimates, and are convinced that the bank would eventually leverage the capital efficiently to deliver an improving RoE (~18% by FY12E). A sensitivity assuming full capital raising in FY10 at current price and factoring growth in credit assets of 30% for FY10E and 25% for FY11 translates into (i) an upgrade in earning estimates of 4.9% for FY10E and 9.8% for FY11E; (ii) increase in book value of 36% for FY10E to Rs459 per share and 19% for FY11E to Rs477 per share; and (iii) ~20% upgrade in FY11E price target to Rs1150 (~2.4x FY11E fully diluted adjusted book value). Axis Bank is one of our top picks in the banking space and IDFC-SSKI Universe. Reiterate Outperformer.

## Key valuation metrics

Year to 31 March				Pre-capital raising		Post-capital raising at Rs845.6 per share	
	2007	2008	2009	2010E	2011E	2010E	2011E
Net profit (Rs mn)	6,590	10,709	18,154	23,607	29,184	24,760	32,054
yoy growth (%)	35.9	62.5	69.5	30.0	23.6	36.4	29.5
Shares in issue (mn)	282	358	359	359	359	430	430
EPS (Rs)	23.5	33.5	50.7	65.8	81.3	62.7	74.5
EPS growth (%)	34.0	42.4	51.2	29.8	23.6	23.8	18.7
PE (x)	35.9	25.2	16.7	12.9	10.4	13.5	11.4
Book value (Rs/share)	121.1	274.3	285.0	336.8	399.8	458.9	476.7
Adj. Book value (Rs/share)	115.5	242.3	282.9	343.7	408.9	426.7	484.2
P/ Adj. Book (x)	7.3	3.5	3.0	2.5	2.1	2.0	1.7
ROAE (%)	21.0	17.6	19.1	21.2	22.1	17.5	16.6

## CAPITAL RAISING ON THE CARDS...

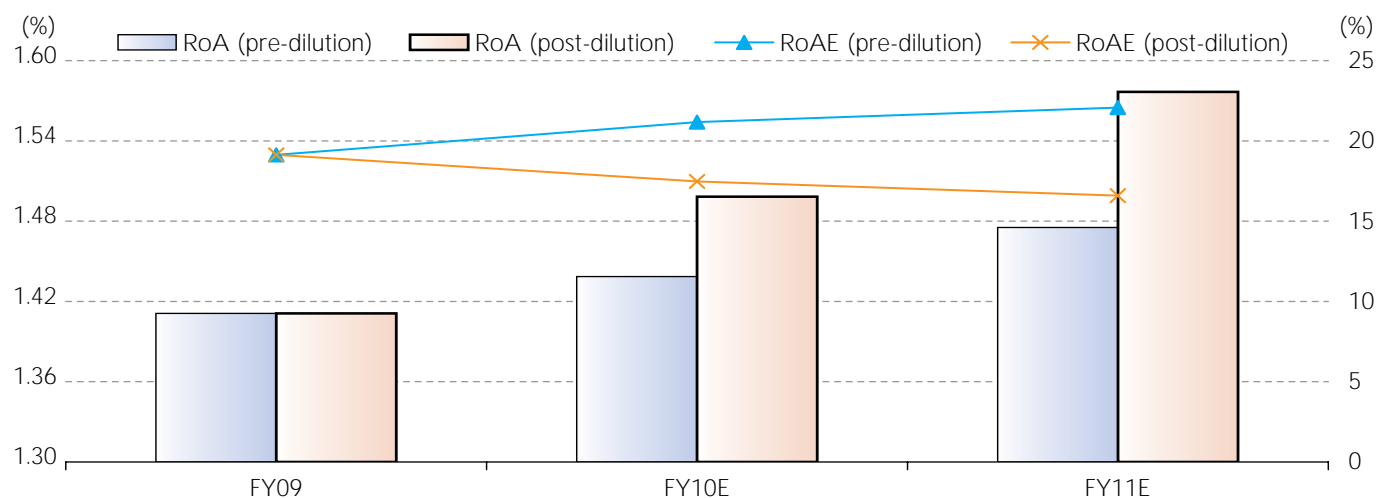
Recently, the board of Axis Bank ('AXSB') approved a Tier -I capital raising by issue of upto 71.4mn equity shares through a GDR or a QIP issuance or a preferential issue to the promoters. This translates into an upto ~20% dilution of the current equity base. At current market price, this amounts to a fund raising of ~Rs60bn. The bank intends to raise capital in the wake of reviving credit demand in H2FY10, and consequently depleting Tier-I CRAR; and (iii) possibly to foray into life insurance organically/ inorganically, given the CEO's extensive experience in running a successful franchise. The bank's Tier I capital adequacy ratio stood at 9.39% with total CAR of 15.28% as of June 2009.

## ...A NEAR-TERM ROE DAMPNER...BUT SUSTAINABLE ROE INTACT

In our sensitivity analysis, we are factoring in (i) the full equity issuance at current market price of Rs845.6 per share in FY10 and; (ii) increasing our loan growth assumptions from 24% in FY10 and 19.4% in FY11 to ~28% in FY10 and 23.5% in FY11. Following is the impact on key metrics (Exhibit 2):

- **Book value up 36% in FY10E:** FY10E book value increases by ~Rs122 to Rs459 per share (up 36%) and FY11E book value increases by ~Rs77 to ~Rs477 per share (up ~19%)
- **Near-term RoE dampened...:** Consequently, average ROE over the next couple of years is subdued to 17% from the current ~22%.
- **...but sustainable RoE to remain intact in our view:** Notably, the sustainable RoE is intact as (i) RoA sees an improving trend even post capital raising, increasing by ~12% over FY09-11E to 1.58%; and (ii) eventually RoE would improve as the bank leverages to ~18% by FY12E (Exhibit 1).

Exhibit 1: Whilst RoE may be dampened subsequent to capital raising, RoA would remain on an uptrend



Source: Company, IDFC-SSKI Research

- **Capital adequacy:** As of Mar '09, the bank's Tier-I CRAR ratio stood at 9.3%. Subsequent to the full equity issuance, Tier- I CRAR would be enhanced to 11.8-12% .
- **Profit estimates:** Higher credit growth translates into higher net interest income, and thereby an upgrade of 4.9% for FY10E and 9.8% for FY11E. We are currently maintaining our estimates.
- **Valuations:** The stock is currently trading at 2.0x FY10E (fully diluted) and 1.7x FY11 (fully diluted) book, which offer an attractive entry point

## Exhibit 2: How the numbers stack-up post capital raising

Post-capital raising at Rs845.6	2009	2010E	2011E
Net profit (Rs mn)	18,154	24,760	32,054
yoy growth (%)	69.5	36.4	29.5
Shares in issue (mn)	359	430	430
EPS (Rs)	50.7	62.7	74.5
EPS growth (%)	51.2	23.8	18.7
PE (x)	16.7	13.5	11.4
Book value (Rs/share)	285.0	458.9	476.7
Adj. Book value (Rs/share)	282.9	426.7	484.2
P/ Adj. Book (x)	3.0	2.0	1.7
ROAE (%)	19.1	17.5	16.6

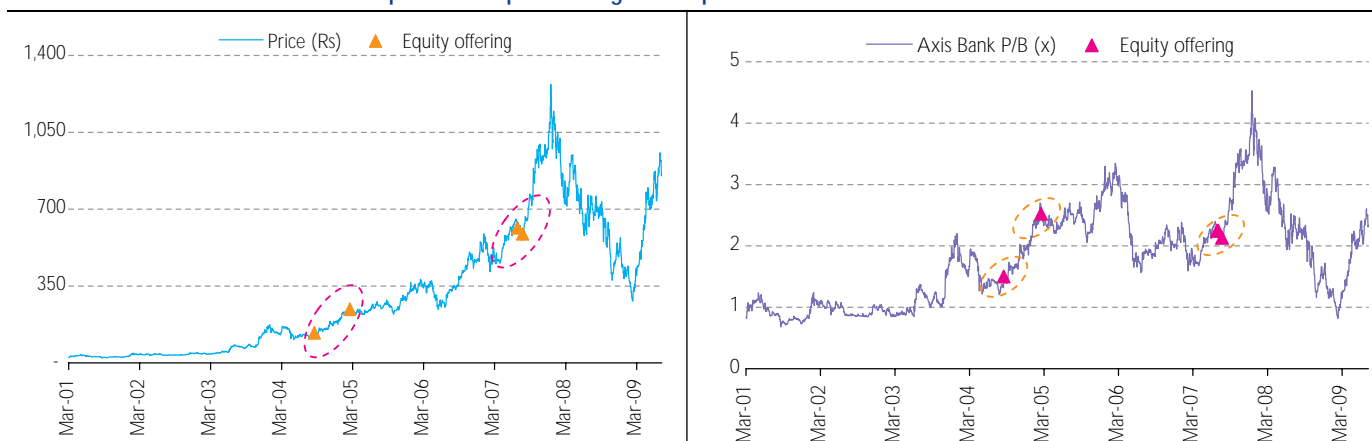
Pre-capital raising	2009	2010E	2011E
Net profit (Rs mn)	18,154	23,607	29,184
yoy growth (%)	69.5	30.0	23.6
Shares in issue (mn)	359	359	359
EPS (Rs)	50.7	65.8	81.3
EPS growth (%)	51.2	29.8	23.6
PE (x)	16.7	12.9	10.4
Book value (Rs/share)	285.0	336.8	399.8
Adj. Book value (Rs/share)	282.9	343.7	408.9
P/ Adj. Book (x)	3.0	2.5	2.1
ROAE (%)	19.1	21.2	22.1

Source: Company, IDFC-SSKI Research

## STOCK PERFORMANCE IN PAST CAPITAL RAISINGS

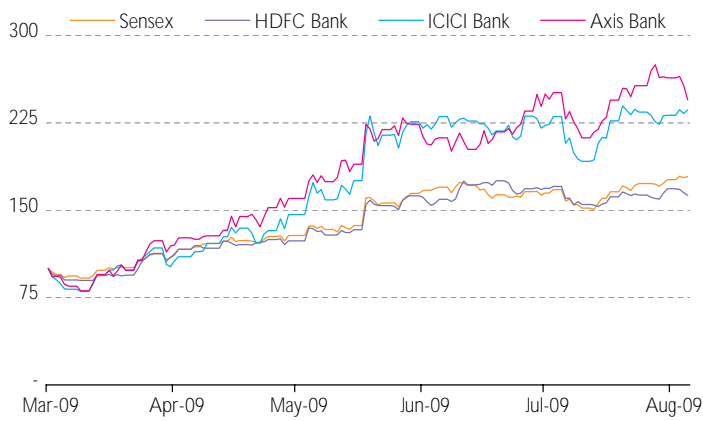
Historically, the stock has rallied around capital raisings, with the one on the anvil likely to be no exception (Exhibit 3). In the recent past, Axis Bank has outperformed peers on the back of robust core earnings performance, strong liability franchise and sustainability of fee income (Exhibit 4). While the capital raising would be RoE dampening in the near-term, our view is the bank would eventually leverage the capital raised to maintain the high RoA and sustainable RoE.

## Exhibit 3: Axis Bank's stock has run-up around capital raisings in the past

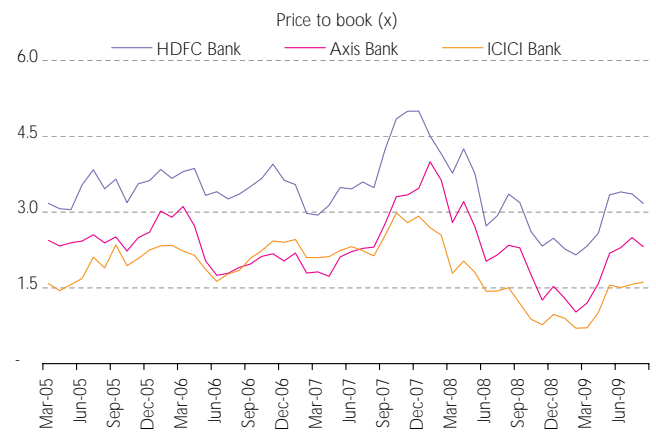


Source: Bloomberg, IDFC-SSKI Research

Exhibit 4: Axis Bank has outperformed in the recent past



...commanding premium valuations



Source: Bloomberg, IDFC-SSKI Research

## OUR VIEW

We are convinced that Axis Bank would eventually deploy the capital raised efficiently to generate high RoA, which would thereby result in an improving RoE. With the long-term sustainable franchise of the bank intact and given the strong liability franchise and receding asset quality pressures, we would buy into any correction. Axis Bank is one of our top picks in the banking space and IDFC-SSKI Universe. Reiterate Outperformer.

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2. Neutral: Within 0-10% to Index
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