Axis Bank

7 August 2008

Initiating Coverage

Recommendation	BUY
CMP (INR)	743
Target (INR)	900

Key Data	
Bloomberg Code	AXSB.IN
BSE Code	532215
NSE Code	AXISBANK
Face Value	10.00
Market Cap (Rs. Mn)	265796.19
52-week high	1291.50
52-week low	534.00

Shareholding Pattern	
Promoters	44.11%
MFs, FIs and Banks	9.60%
FIIs	32.45%
Others	13.84%

Key Financials (Rs. Mn.)	FY2008	FY2009E	FY 2010E
Net Interest Income	25,853.53	41,838.88	71,201.62
Non Interest Income	17,920.19	26,640.72	40,272.16
Fee income as % non-intr income	73.70%	79.32%	83.95%
Total Income	43,773.72	68,479.60	111,473.78
Operating Expenses	21,549.27	35,489.17	58,595.11
Operating Profit	22,224.45	32,990.43	52,878.68
Provisions & Contingencies incl. taxes	11,548.86	16,495.22	26,439.34
PAT	10,675.59	16,495.22	26,439.34

Source: Company Data, DDAV Research

Analyst

Divyanshi Dayanand

Transforming to sustainable profitability:

The bank underwent a major re-branding exercise in the previous financial year, the result of which was seen in a new age customer centric bank emerging- one with strong fundamentals and a huge business base. The third largest private sector bank in India has shown consistent high growth in the previous years. The net interest margins are in the range of 3.5% levels, one of the highest in the industry. The bank has recently increased its PLR by 50 bps, this along with high proportion of CASA (second highest in the industry at 46%) will help in stable growth in margins. It is the market leader in the foreign currency travel card segment. To concentrate primarily on organic growth the bank has expanded its business network in both domestic and overseas market. The number of branches which currently stand at 713 and is expected to go up to 1030 by 2010. As a result of this the business has seen a growth of 53% YoY. The business momentum is expected to continue at a steady pace with focus on high yield sectors and strict monitoring on asset quality.

The bank promises a sustainable growth going forward and a value investment idea for a 12-month plus time horizon. We initiate the coverage with a BUY rating on the bank with a target price of Rs 900.

Key Highlights

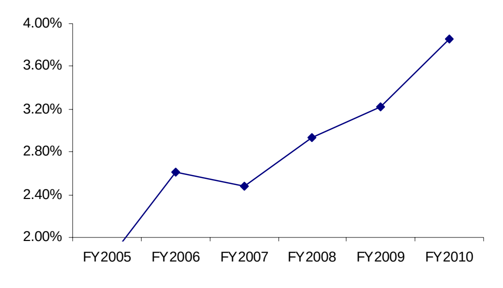
- The Net Interest income (NII) stood at Rs 25853 million for FY08 a growth of 76% growth YoY. The bank has its NIMs at 3.5% levels up from previous levels of 3%. These margins are expected to be stable going forward. The fee based income has been one of the growth drivers for the business of the bank.
- The gross NPA and net NPA levels have shown a steady decline and currently stand at 0.83% and 0.42% respectively for the quarter ended 30th June 2008. The bank has in place proper monitoring procedures in place so as to have a consistent asset quality in the portfolio.
- The bank's subsidiaries- Axis Sales Ltd- which specializes in marketing and sales of credit cards, Axis Private Equity –which manages investments, venture capital funds and offshore funds and an unnamed subsidiary which will function as an AMC after the approval of SEBI; have helped in increasing the base of the business and also added on to the productivity of the business.
- The business per employee has shown a CAGR of 40% over 4 years, this currently stands at Rs 99 million.
- The Deposits, where in low cost deposits form 46%, have shown a growth of around 49% YoY, while advances have grown by 61% YoY, with a proportion of 43% in the retail segment. Going forward the growth is expected to remain above industry average on account of robust expansion plans.
- The provisions have increased by 90% YoY for FY08 on account of mark to market losses and derivative contracts. The provisioning coverage is adequate at around 57% to care of these losses going forward.

About Axis Bank:

Axis Bank was the first of the new private banks to have begun operations in 1994, after the Government of India allowed new private banks to be established. The Bank was promoted jointly by the Administrator of the specified undertaking of the Unit Trust of India (UTI - I), Life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC) and other four PSU insurance companies, i.e. National Insurance Company Ltd., The New India Assurance Company Ltd., The Oriental Insurance Company Ltd. and United India Insurance Company Ltd. The bank had a successful re-branding from UTI bank to Axis bank in 2007. The Bank has maintained its No.1 rank as Debt Arranger as assessed by Prime Database for the year ended March'08.

The bank currently has 713 outlets- branches and extension counters with around 9 million customer accounts, the branch network is expected to increase to 1000 plus by 2010, with its presence in 433 locations across India. The international presence has also being boosted by the bank, with representative offices and branches across locations (including Shanghai Dubai Hong Kong and Singapore), the bank's total assets under operations for overseas business stands at $1.8 billion.

NIM



Source: Company Data, DDAV Research

The CAMEL ride:

- **Capital Adequacy:** The capital adequacy ratio for the year ended march 2008 stands at 13.99% with Tier I at 10.39% while Tier II at 3.60%. The bank has applied Basel II along with Basel I norms from the current financial year onwards, as a result of which the operating risk is also under the standardized measurement purview now. The bank has focused on low risk weighted assets such that the capital deployment is efficient. During the FY 07-08 to augment capital for maintaining the momentum of business growth, the bank raised equity capital of Rs. 453. 4 million through simultaneous offerings of follow-on Global Depositary Receipts (GDRs), a Qualified Institutional Placement (QIP) and a preferential allotment of equity shares to the promoters of the bank. In addition, it has also raised US Dollars 60 million (equivalent to Rs. 24.312 mn) as Upper Tier II Capital from Singapore under its MTN Program.

Rs. Mn.

Capital Adequacy as on 31st March 2008	Basel II	Basel I
Tier I capital- Shareholder's Funds	882.70	882.25
Tier II Capital:		
Bonds qualified as Tier II	157.29	157.29
Upper Tier II capital	114.84	114.84
Other Eligible as Tier II	34.26	34.26
Total Capital	1189.09	1188.64
Total Risk weighted assets & contingencies	8499.00	8671.96
CAR	13.99%	13.73%
Tier I	10.39%	10.17%
Tier II	3.60%	3.56%

Source: Company Data, DDAV Research

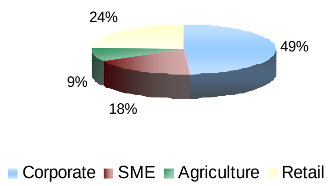
The special arm of UTI (SUUTI) which currently has 27.11% stake in the bank, is planning to dilute 17% stake through block deals. The SUUTI has to dilute the stake fully by 2009 end, and has to meet redemption payment obligations, estimated at Rs 19,000 crore. However, SUUTI has claimed that it would not have to sell its shares in Axis Bank to meet its redemption requirements. RBI will also be in approval of this move as it does not want one single entity to hold more than 10 per cent in a bank.

- Asset Quality: The asset quality has seen improvement over the previous financial year. The gross NPAs as a percentage of advances stood at 0.83%, while the net NPAs as a proportion to advances were at 0.42%; declining from previous levels of 1.10% and 0.61% respectively. The provision coverage stood at 57%, which is considerably above the industry average. The unsecured advances form 16% of the total advances portfolio. The priority sector constitutes 27% of the total portfolio, while the retail assets form 24% of the advances. The delinquency levels are expected to be stable at current levels on account of major thrust on SME and retail sector. Moreover the concentration on the interest rate sensitive sectors being high at around 21% of the corporate portfolio also supports the fact.

- Management: The 10-member management team is under the chairmanship of Mr. P.J. Nayak, who is also the CEO of the bank. The cost per unit of money lent, a measure of efficiency of the management policies, remained stable at 0.4. The business per employee has grown at a CAGR of 30% in two years and currently stands at Rs 99 million. With the robust expansion plans for branch network and specific focus on cost efficiency, the business is expected to show a further growth of around 15% YoY.

- Earnings sustainability: The bank has shown consistent high growth for the prior financial years. The NII has shown a growth of 76% YoY with NIM at 3.47% considerably up from previous levels of 2.74% . The cost of funds has increased to 5.5%, which is expected to go up further to 6% levels on account of rising interest costs. The core operating profit has increased 70% YoY and is expected to grow at around 50% for the coming years. The RoE for FY08 stood at 17% a decline from previous level of 19%, mainly on account of capital raising exercise taken up. The RoA stood at 1.1% up from previous levels of 1%. The pre-provisioning profits have also seen a steady growth and presently stood at Rs 22.2 bn. The cost to income ratio has marginally increased to 49.23% from previous levels of 49.1%, mainly on account of high marketing costs undertaken in the year. Going forward the ratio is expected to be stable at 50% levels.

Advances Portfolio

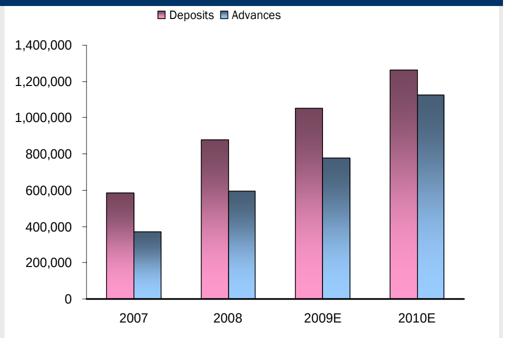


Source: Company Data, DDAV Research

Earnings Performance	FY2008	FY2009E	FY 2010E
Return on Assets	1.17%	1.23%	1.39%
Return on Equity	17.56%	17.66%	24.43%
Interest Spread Ratio	6.70%	7.56%	7.18%
Earnings spread Ratio	2.28%	1.67%	1.43%
Intermediation cost ratio	2.36%	2.64%	3.07%

Source: Company Data, DDAV Research

Deposits and Advances



Source: Company Data, DDAV Research

- **Liquidity:** The credit to deposit ratio stood at 68%. with the RBI now giving strict directions to the banks to stick to the growth targets the ratio is expected to be stable around 70% going forward, which leaves the bank in a very comfortable liquidity zone. The RBI has raised the CRR to 9% with effect from 30th August 2008, while the repo rate too has been raised to 9%, both of which point to a high interest rate scenario for a medium term. The result of which could be felt on the proportion of CASA which may go down, and term deposits which may go up. Similarly on the credit side the growth is expected to slow down. Currently the bank's long term credit to deposit ratio stood at 86%, this is expected to be around 90% going forward.

Valuation

The stock is currently trading at Rs. 743.05; 16.11x FY09E earnings levels and 2.68x FY09E P/ABV. We recommend "Buy" for the stock, with a 12-month Horizon. The target price is Rs 900, 3.3x FY09E P/ABV, a potential upside of 22%.

Valuation Matrix

Particulars	FY2008	FY2009E	FY 2010E
Net Profit (Rs Mn)	10,675.59	16,495.22	26,439.34
EPS	29.84	46.11	73.91
Growth%	28.21%	54.51%	60.28%
Interest Earned/Total Income	79.60%	79.89%	79.79%
P/E (X)	24.90	16.11	10.05
PEG Ratio	0.88	0.30	0.17
BV (INR)	245.13	277.00	328.03
P/BV (X)	3.03	2.68	2.27
ABV (INR)	239.12	269.19	316.72
P/ABV (X)	3.11	2.76	2.35
RoE (%)	12.17%	16.65%	22.53%
RoA (%)	1.17%	1.23%	1.39%
Current Mcap/Assets	24.26%	16.73%	11.95%

Source: Company Data, DDAV Research

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