

October 14, 2010

REDUCE

Price	Target Price
Rs 1,563	Rs1,200
Sensex	20,498

Price Performance

(%)	1M	3M	6M	12M
Absolute	10	19	36	51
Rel. to Sensex	4	4	17	27

Source: Bloomberg

Stock Details

Sector	Banks
Reuters	AXBK.BO
Bloomberg	AXSB@IN
Equity Capital (Rs mn)	4088
Face Value (Rs)	10
No of shares o/s (mn)	409
52 Week H/L (Rs)	1,608/889
Market Cap (Rs bn/USD mn)	639/14,468
Daily Avg Vol (No of shares)	1449264
Daily Avg Turnover (US\$ mn)	46.0

Shareholding Pattern (%)

	S'10	J'10	M'10
Promoters	37.5	37.7	38.5
FII/NRI	46.0	44.2	42.1
Institutions	5.5	6.5	7.1
Private Corp	6.4	6.9	7.9
Public	4.6	4.7	4.4

Kashyap Jhaveri

kashyap.jhaveri@emkayglobal.com
+91 22 6612 1249

Pradeep Agrawal

pradeep.agrawal@emkayglobal.com
+91 22 6612 1340

Earnings growth healthy; Slippage remains high

- **Axis Bank's (AXSB) Q2FY11 NII at Rs16.2bn marginally ahead of expectations driven by 36% growth in advances and 18bps expansion in NIMs**
- **Higher growth in NII was partially offset by lower trading gains and higher operating expenditure**
- **Slippages continue to remain high resulting in higher credit costs. Slippages for Q2FY11 at 1.7% vis-à-vis 1.5% in FY10 and 1.6% in Q1FY11**
- **Valuations unattractive at 3.0x FY12E ABV with slippages remaining high. Continue REDUCE rating with TP of Rs1,200**

NII growth marginally above expectations

AXSB's NII has grown by 40.5% yoy to Rs16.2bn, marginally ahead of our expectation. The growth in NII was driven by 36.5% yoy growth in advances and stable NIM's at 3.3%.

Higher investment and advances yield offsets rise in cost of funds

The bank NIM's remained stable during the quarter as higher investment and advances yield offset negative impact of rise in cost of funds. The yield on investment rose by 93bps qoq to 7.5%, while yield on advances rose by 18bps qoq to 8.9%. **The sharp rise in the investment yields is on account of booking of gains in the liquid mutual funds which is included in interest income on investments.** This helped the bank to negate the 14bps rise in its cost of funds, and hence stable NIM's.

Yield analysis

%	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (bps)	QoQ (bps)
Yield on advances*	9.8	9.6	8.8	8.7	8.9	-94	18
Yield on investments*	7.0	6.7	6.5	6.6	7.5	53	93
Yield on assets*	7.8	7.6	7.2	7.2	7.4	-37	26
Cost of funds*	4.7	4.1	3.7	3.9	4.1	-54	21
NIM*	3.1	3.6	3.5	3.3	3.3	18	5
Yield on assets	8.9	8.8	8.6	8.3	8.4	-50	11
Cost of funds	5.4	4.8	4.5	4.6	4.8	-66	14
NIM (Reported)	3.5	4.0	4.1	3.7	3.7	16	-3

Source: Company, Emkay Research

Note:* Calculated on basis of average quarterly balances

Valuation table

Y/E March 31	Net income	Net profit	EPS (Rs)	ABV (Rs)	RoA (%)	RoE (%)	PE (x)	P/ABV (x)
FY2009	65,831	18,154	50.6	268.3	1.4	19.1	30.5	5.7
FY2010	87,757	25,144	62.1	373.7	1.5	19.2	22.0	4.1
FY2011E	109,402	33,036	80.8	433.4	1.6	19.0	16.8	3.6
FY2012E	136,276	42,033	102.0	512.1	1.6	20.6	13.2	3.0

Source: Company, Emkay Research

Key financials – Quarterly

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Net Interest Income	11,497	13,491	14,601	15,138	16,151	40.5	6.7	31,289	21,953	42.5
Other Income	10,656	9,881	9,335	10,008	10,332	-3.0	3.2	20,340	20,241	0.5
Fee Income	7,190	7,997	7,796	7,431	8,485	18.0	14.2	15,916	13,456	18.3
Net Income	22,153	23,372	23,936	25,146	26,483	19.5	5.3	51,629	42,194	22.4
Total Operating Expenses	9,095	9,626	10,098	10,645	11,620	27.8	9.2	22,265	17,374	28.2
As % Of Net Income	41.1	41.2	42.2	42.3	43.9			43.1	41.2	
Employee Expenses	3,042	3,085	3,338	4,164	4,053	33.2	-2.7	8,217	6,135	33.9
As % Of Net Income	13.7	13.2	13.9	16.6	15.3			15.9	14.5	
Other Expenses	6,053	6,540	6,761	6,481	7,567	25.0	16.8	14,048	11,238	25.0
As % Of Net Income	27.3	28.0	28.2	25.8	28.6			27.2	26.6	
Operating Profit	13,058	13,746	13,838	14,501	14,864	13.8	2.5	29,364	24,821	18.3
As % Of Net Income	58.9	58.8	57.8	57.7	56.1			56.9	58.8	
Provisions	4,989	3,731	2,019	3,330	3,788	-24.1	13.8	7,118	8,142	-12.6
Prov for NPA	4,875	3,580	1,775	3,040	3,210	-34.1	5.6	6,250	8,235	-24.1
PBT	8,069	10,015	11,820	11,171	11,076	37.3	-0.9	22,246	16,679	33.4
Total Tax	2,752	3,455	4,171	3,752	3,725	35.3	-0.7	7,476	5,743	30.2
Adjusted PAT	5,316	6,560	7,649	7,419	7,351	38.3	-0.9	14,770	10,937	35.1
Extra Ordinary Items	0	0	0	0	0					
Reported PAT	5,316	6,560	7,649	7,419	7,351	38.3	-0.9	14,770	10,937	35.1
Reported EPS	13.2	16.3	18.9	18.2	18.0	35.9	-1.3	36.2	28.9	25.3

Source: Company, Emkay Research

Advances growth stood at 36.5%yoy/1.8%qoq

The advances grew by a strong 36.5%yoy to Rs1.1tn benefiting from low base of last year. However, sequentially the growth was just 1.8%, largely inline with industry levels.

The growth was driven by large corporate segment as it grew by 5.9% qoq. The retail and SME loans remained flat even as loans to agriculture shrank by 14.3%qoq.

Advances mix

Rs bn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	% of total
Large corporates	401	416	525	601	637	58.9	5.9	57.6
Mid-corporate/SME	150	165	195	168	168	12.0	0.0	15.2
Agriculture	79	78	115	106	91	14.2	-14.3	8.2
Retail	180	189	208	211	210	16.8	-0.3	19.0
CV/CE	2	2	1	-	-	NA	NA	NA
Personal loans	18	15	20	21	17	-6.6	-20.3	1.5
Mortgages	120	134	147	150	153	27.2	2.5	13.9
Car Loans	23	28	27	27	27	16.8	-0.3	2.5
Credit cards	5	4	5	4	4	-22.1	-0.3	0.4
Others	11	6	9	8	8	-22.1	-0.3	0.8
Total	810	848	1,043	1,086	1,106	36.5	1.8	100.0

Source: Company, Emkay Research

Deposit profile improved further

During the quarter, CASA mix improved by 138bps sequentially to 41.5%, led by 11.5%qoq growth in saving deposit and 9.0%qoq growth in current deposits.

CASA Mix

Rs bn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Savings Deposits	215	223	322	245	274	27.6	11.5
Current Deposits	280	296	339	347	378	35.0	9.0
Term deposits	661	619	753	882	917	38.7	3.9
Total Deposits	1,156	1,139	1,413	1,475	1,569	35.7	6.4
CASA	42.8	45.6	46.7	40.2	41.5	-124	138

Source: Company, Emkay Research

Fee income growth led by corp banking and capital markets

The fee income picked up significantly during the quarter as it grew by 18.0%yoy and 14.4%qoq to Rs8.5bn, against negative sequential growth in the earlier two quarters. The growth was primarily led by 38.4%yoy growth in corporate banking and 23.1%yoy growth in capital markets.

Fee income

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Corporate banking	2,500	2,550	3,066	2,650	3,460	38.4	30.6	6,110	4,510	35.5
Business banking	960	890	780	940	920	-4.2	-2.1	1,860	1,850	0.5
Capital markets	130	850	420	200	160	23.1	-20.0	360	310	16.1
Retail banking	2,140	2,460	2,330	2,050	2,300	7.5	12.2	4,350	4,040	7.7
Treasury	1,470	1,247	1,200	1,580	1,650	12.2	4.4	3,230	2,760	17.0
Total fee income	7,194	7,997	7,796	7,420	8,490	18.0	14.4	15,910	13,464	18.2
Trading gains/(losses)	2,240	1,696	1,027	1,957	1,084	-51.6	-44.6	3,041	5,500	-44.7
Others	1,226	187	512	620	763	-37.8	23.2	1,383	1,285	7.6
Total	10,656	9,881	9,335	10,008	10,332	-3.0	3.2	20,340	20,241	0.5

Source: Company, Emkay Research

Retail fees continue to remain drag

The retail fees continued to be drag on overall fee income as the third party product income shrank by 25% yoy. Due to almost negligible growth in retail portfolio, the retail processing fee income also grew by just 8% yoy/flat qoq.

Provision expenses remain high driven by NPAs...

The provision expenses during the quarter remained high driven by NPA provisions of Rs3.2bn. We expect the provision expenses to remain high at 1.5% of advances for FY11 driven by higher slippages.

Break up of provisions

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
NPAs	4,875	3,580	1,775	3,040	3,210	-34.1	5.6	6,250	8,235	-24.1
As % of advances	0.6	0.4	0.2	0.3	0.3			0.6	1.0	
Investment Depreciation	-55	63	206	350	0	-100.0	-100.0	350	-535	-165.4
Others	169	88	37	-60	578	241.2	-1,063.3	518	442	17.1
Total	4,989	3,731	2,019	3,330	3,788	-24.1	13.8	7,118	8,142	-12.6

Source: Company, Emkay Research

...As slippages continue to remain high

The slippage rate for the quarter remained stable over preceding quarter at 1.6% (1.5% in FY10, 1.6% in Q1FY11). The total slippages during the quarter stood at Rs4.5bn of which Rs920mn was from the restructured standard assets. The slippages are still high resulting in higher NPA provisions.

The management has guided towards the slippage number remaining higher in coming quarters too. We have built in FY11 slippages of Rs20bn in our numbers.

NPA profile

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Gross NPAs	11,317	11,735	13,180	13,409	13,624	20.4	1.6
Net NPAs	4,167	4,296	4,190	4,134	4,094	-1.8	-1.0
Gross NPAs (%)	1.2	1.2	1.1	1.1	1.1		
Net NPAs (%)	0.5	0.5	0.4	0.4	0.3		
Net NPAs/Net worth (%)	2.8	2.7	2.6	2.4	2.3		
Provision cover (%)	63.2	63.4	68.2	69.2	70.0		

Source: Company, Emkay Research

Valuation and view

We expect Axis Bank to report a CAGR of 24.6% in operating income and 28.1% in the earnings over FY10-12E driven by 27% growth in the customer assets. The slippage rate for AXSB has still remained high at 1.5% with pressure particularly from the SME segment. We believe that the current valuations at 3.6x FY11E ABV and 3.0x FY12E ABV are unattractive. Hence we maintain our REDUCE rating on the stock with price target of Rs1,200.

Key Financials**Profit and loss (Rs mn)**

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Net interest income	36,862	50,045	66,152	83,356
Other income	28,969	37,712	43,249	52,920
Net income	65,831	87,757	109,402	136,276
Operating expenses	28,582	37,097	45,004	54,484
Pre provision profit	37,249	50,660	64,398	81,792
PPP excl treasury	40,133	57,800	69,398	86,792
Provisions	9,397	12,148	14,343	18,106
Profit before tax	27,852	38,512	50,055	63,686
Tax	9,698	13,368	17,019	21,653
Tax rate	35%	35%	34%	34%
Profit after tax	18,154	25,144	33,036	42,033

Balance sheet (Rs mn)

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Liabilities				
Equity	3,590	4,052	4,087	4,122
Reserves	98,546	156,393	182,739	216,573
Net worth	102,136	160,444	186,826	220,695
Deposits	1,173,741	1,413,002	1,827,645	2,309,978
Borrowings	201,331	233,359	275,202	320,808
Total liabilities	1,477,208	1,806,805	2,289,673	2,851,482
Assets				
Cash and bank	150,169	152,064	217,529	274,937
Investments	322,534	421,516	502,881	625,876
Customer assets	956,338	1,181,664	1,517,671	1,899,287
Others	48,180	51,562	51,591	51,381
Total assets	1,477,208	1,806,805	2,289,673	2,851,482

As % of assets

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
NIM	3.2	3.3	3.5	3.5
Non-ll/avg assets	2.3	2.3	2.1	2.1
Fee income/avg assets	2.9	2.8	2.8	2.8
Opex/avg assets	2.2	2.3	2.2	2.1
Provisions/avg assets	1.5	1.9	1.5	1.4
PBT/avg assets	1.9	2.1	2.2	2.2
Tax/avg assets	0.7	0.7	0.7	0.8
RoA	1.4	1.5	1.6	1.6
RoAE	19.1	19.2	19.0	20.6
GNPA (%)	0.9	1.1	1.1	1.2
NNPA (%)	0.4	0.4	0.4	0.3

Valuations

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Net profit (Rs mn)	18,154	25,144	33,036	42,033
Shares in issue (mn)	359	405	409	412
EPS (Rs)	50.6	62.1	80.8	102.0
PER (x)	30.5	24.8	19.1	15.1
FDEPS(Rs)	50.6	70.0	92.0	117.1
FDPER (x)	30.5	22.0	16.8	13.2
Book value (Rs)	277.2	384.0	445.2	523.6
P/BV (x)	5.6	4.0	3.5	2.9
Adj book value (Rs)	268.3	373.7	433.4	512.1
P/ABV (x)	5.7	4.1	3.6	3.0
P/PPP (x)	14.9	12.3	9.8	7.8
Dividend yield (%)	0.6	0.8	1.0	1.2

Recommendation History: Axis Bank – AXSB IN

Date	Reports	Reco	CMP	Target
15/07/2010	Axis Bank Q1FY11 Result Update	Reduce	1,314	1,100
21/04/2010	Axis Bank Q4FY10 Result Update	Reduce	1,186	1,000
18/01/2010	Axis Bank Q3FY10 Result Update	Reduce	1,078	800
14/10/2009	Axis Bank Q2FY10 Result Update	Reduce	1,012	800

Recent Research Reports

Date	Reports	Reco	CMP	Target
23/09/2010	Crisil Company Update	NR	6,169	NR
18/08/2010	Banking Sector Update			
13/08/2010	State Bank of India Q1FY11 Result Update	Reduce	2,784	2,650
13/08/2010	ICRA Q1FY11 Result Update	Reduce	1,219	1,200

Emkay Global Financial Services Ltd.

Paragon Center, H -13 -16, 1st Floor, Pandurang Budhkar Marg, Worli, Mumbai – 400 013. Tel No. 6612 1212. Fax: 6624 2410

DISCLAIMER: This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. The manner of circulation and distribution of this document may be restricted by law or regulation in certain countries, including the United States. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Emkay Global Financial Services Ltd. is obligated to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon. Neither Emkay Global Financial Services Ltd., nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. We and our affiliates, officers, directors, and employees world wide, including persons involved in the preparation or issuance of this material may; (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender / borrower to such company(ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The same persons may have acted upon the information contained here. No part of this material may be duplicated in any form and/or redistributed without Emkay Global Financial Services Ltd.'s prior written consent. No part of this document may be distributed in Canada or used by private customers in the United Kingdom. In so far as this report includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.