

15<sup>th</sup> January, 2013

Analyst:  
Vipul Goyal  
vipul@thirdwavesolutions.in

## KEY INFORMATION

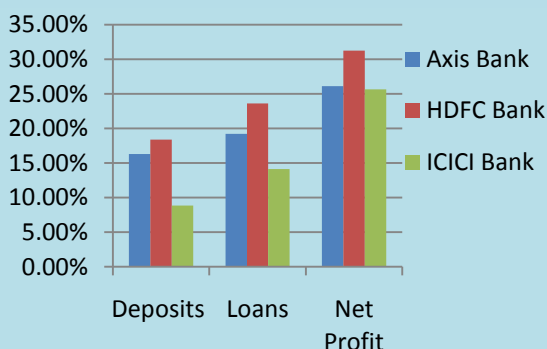
Company: Axis Bank  
Sector: Banks – Private Sector  
Ticker Symbol: AXISBANK  
Current Price: 1400  
P/E: 13.7 P/B: 2.6

## Peer Comparison

	Axis Bank	HDFC Bank	ICICI Bank
Turnover (Cr.)	22,000	33,252	37,995
Net Profit Margin	19.18%	15.86%	20.89%
ROE	20.29%	18.9%	13.62%
P/E	13.7	30.5	17.2
P/B	2.6	5.4	2.3
CAGR	37.58%	32.26%	9.62%

	Yes Bank	Kotak Mahindra Bank
Turnover (Cr.)	6,307	8,470
Net Profit Margin	3.76%	21.85%
ROE	5.6%	15.46%
P/E	17.7	26.1
P/B	3.7	3.8
CAGR	60.75%	33.71%

## Growth Rate for the past year



Please refer to the last page for important disclosures.

## Overview

### About the Company:

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 four other 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.

### Business:

Axis Bank has a total of 1622 Branches and 9924 ATMs in India. There has been growth in the retail segment with retail loans growing by 35% in the last fiscal year (2011-2012); savings account deposits growing by 26% and term deposits increasing by 43%. Most of the retail loans are home loans (75%) and 89% of all the retail loans are secured.

Axis Bank is one of the leading lenders to the infrastructure sector, and the lending in this segment increased by 23% last fiscal year. The current account deposits grew by 8% year-on-year, but 17% on a daily average basis. The Bank also undertook a few transactions of investment banking (including 5 IPOs) aggregating Rs. 8,750 Cr.

### Highlights:

Axis Bank had a growth of about 45% in the total revenues (however, the growth in operating revenue was 20%) and a growth of 25% in net profit. On total revenue of Rs. 22,000 Cr. the company managed to make a net profit of Rs. 4,218 Cr (19.18%).

Net Interest Margin has decreased slightly from last year, from 3.65% to 3.59%. There has been a considerable increase in the Cost of Funds, from 4.96 to 6.28. The Capital Adequacy ratio has improved from 12.65% to 13.66% with the help of the issue of new bonds (Tier-II Capital).

## Industry and Financial Analysis

### Industry View:

The year 2011-2012 has not been the best for almost all the industries, particularly due to the global slowdown. There has been a great amount of macroeconomic uncertainty which has taken its toll on the businesses across the world, including the banking sector. In addition, due to the global uncertainty there has been a reduction in the foreign capital inflow. Lastly, the high inflation of nearly 9-10% has kept the savings rate (% of money saved) relatively low in India and the demand for loans has slowed down. Hence all in all, it has been a difficult year for the industry.

Despite going through a slowdown, the banks in India have managed to achieve considerable growth owing to the fact the banking penetration in India is much lower than that of the other economies around the globe. Therefore, there is a huge potential for the sector which is currently untapped.

A lot of factors look set to change in the near future and the global outlook already looks much better than it did 6 months ago. It is widely expected that RBI will reduce the rates in the calendar year 2013 which should bode well for the Indian banking sector. With a rate reduction, there will be a spur in the demand for capital at a lower cost.

### Financial Analysis:

Axis Bank's P/E multiple of 13.7x is well below its competitors such as HDFC Bank and ICICI Bank. It has traded historically in the range of 40x (pre-2008 crash) to 6x.

Axis bank has a P/E of 13.7 at the current price of 1350. This is well below that of its competitors and we believe that it is undervalued in that respect. In comparison, HDFC Bank has a P/E of 30, ICICI Bank and YES Bank have a P/E of around 17 and Kotak Mahindra Bank has a P/E of around 26. Similar story with the P/B ratio where Axis Bank and ICICI Bank have a P/B ratio in the whereabouts of 2.5 compared to others which trade at near 4 to 5.

Axis Bank has had a very high rate of growth at a 5 year CAGR of revenue of 37.5% (more than HDFC Bank's 32.2%). However, it is less than that of Yes Bank, which has grown at a phenomenal rate of 60%, but that is mainly because of a low base and the high savings rate (rate of return on a savings account) given by Yes Bank. Axis Bank has an average Net Profit Margin of 19% but a better-than-average ROE of 20% (as compared to other banking stocks).

Axis Bank capital adequacy ratio and Net NPA ratio shows that it is running on safe grounds, with low risk of insolvency and small amount of bad loans on its books.

The Capital Adequacy ratio of 13.66% is well above the required 9%, with Tier-I capital alone accounting for 9.45%. It is low compared to the other private banks in the industry like HDFC Bank which has a Capital Adequacy Ratio of 16.5% or ICICI Bank, which has a capital adequacy ratio of 18.5%, but as long as it is comfortably above the 9% requirement, there is no cause for alarm.

The Gross NPA and Net NPA are at relatively safe levels of 0.95% and 0.25% respectively. These ratios are slightly below the industry average: ICICI Bank has Net NPA of 0.62%, Kotak Mahindra Bank has 0.5% and HDFC Bank has 0.2%.

CASA Ratio is 41% which is slightly lower than HDFC Bank's 47%. But both these banks have a better than average Deposits/Total Debt Ratio and hence Axis Bank should do fine in this regard as well.

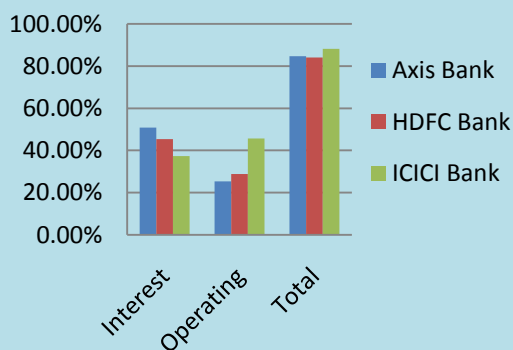
The Net Interest Margin, at around 3.59% is slightly lower than the average, with HDFC Bank and Kotak Mahindra Bank having better net interest margins of 4.22% and 4.8% respectively. On the brighter side, it is better than ICICI bank which has a very low margin of 2.73% for FY11-12.

Axis Bank has a cost of funds of 6.28% (which increased from 4.96% last year), whereas HDFC Bank has a cost of funds of 5.72%. This puts Axis Bank at a slight disadvantage in terms of profitability. But it manages to mitigate the effect through a more cost-efficient business strategy, resulting in lower operating expenses (as a percentage of revenue) than HDFC Bank, for example. Furthermore, looking at other banks like ICICI Bank which has a cost of funds of 6.33 and Yes Bank & Kotak Mahindra Bank, both of which have a cost of funds of above 8%, Axis Bank does not look at all bad at all; in fact, it has a relatively low cost of funds.

The CASA Ratio lies in an acceptable range of around 41%, which is around the average and is very stable at that level. HDFC Bank and ICICI Bank have slightly higher ratios of 47% and 43% but Kotak Mahindra Bank and Yes Bank have much lower ratios at 32% and 15% respectively.

In the last year, deposit growth rate and loan growth rate has slowed down for Axis Bank. This is a slight cause for concern as the same has not happened for all the other banks. Financial data for the last two quarters (Q1FY13 & Q2FY13) shows that growth has further slowed down. HDFC Bank has seen a much higher growth than Axis Bank over the past two quarters in revenue.

**Expenses as % of Total Revenue**



Source: TWS Research

The cost of funds has increased for all the private banks in the past year, and Axis Bank is no exception. But giving 4% on savings account insures a relatively low cost for the bank.

## Conclusion

---

Axis Bank is the leading lender to the Infrastructure segment, and if growth in India is revived, Axis Bank stands to gain the most in that respect.

With an expected growth of around 20%, convergence of the price multiple with the other banking stocks, Axis Bank has significant upside potential attached.

Since there is a lot of untapped market in India for financial services, achieving growth for banks should not be a problem in the coming future. Even though aggressive competitors like Kotak Mahindra Bank and Yes Bank are giving much higher savings rate, these banks will only grow their revenue, not their profitability. These banks already have a higher cost of funds than compared to others. By giving a higher savings rate, the cost of funds is going to increase even further and reduce their net interest margin and their profitability.

Axis Bank might grow at a slower rate than the aggressive banks, but it should yield better results for an investor, since it operates at better margins. In addition, one should not forget that there is still considerable growth in the bank. It might not be as much as the others, but growth of 20% (which can be expected from Axis Bank) should yield good results for the investor.

The bank has maintained a better than average margin since the past few years and we expect them to continue doing so. The management is not running the business aggressively and offering high savings rate, which bodes well for the profitability of the company.

The CEO and MD of the company Shikha Sharma, has recently stated that the ambition of the bank is to become the JP Morgan of India. The bank has a lot of ambition and will seek to grow further; with an able management supporting it.

Furthermore, Axis Bank is the leading lender to the Infrastructure segment, and if growth in India is revived, Axis Bank stands to gain the most in that respect.

In terms of financials, Axis Bank is average at the very least, if not above average. This gives enough margin of safety and leads us to believe that at a P/E of 13.7, with a favourable sector outlook and moderate growth prospects, it is undervalued and makes sense to buy for the long term.

## DISCLAIMER

---

The information and views presented in this report are prepared by Third Wave Solutions Pvt. Ltd (TWS) and is based on our analysis and upon sources that we consider reliable. We, however, do not vouch for the accuracy or the completeness thereof. This Newsletter is for restricted circulation only. The information furnished in this document is solely for your information and must not be reproduced or redistributed in any manner. Anyone having access to this document is required to observe such restrictions. The information in this document is for personal information and we are not soliciting any action based upon it. Recipients of this report should rely on their own investigation and take their own professional advice. Recommendation in this report may or may not suit risk reward preferences of individual investors and hence should not be completely relied upon. This is a fundamentals based report and may differ from a technical based report. TWS and/or its affiliates, officers, directors, employees, at all various locations may from time to time hold any long or short positions and /or have any direct or indirect interest resulting in monetary gains of any nature and /or have other potential conflict of interest with respect to any view expressed in this document. Recipients may please note that neither TWS nor any associate(s) accepts any liability or losses arising from the use of this information and views mentioned in this document. No part of this material may be duplicated in any form and/or redistributed without TWS prior written permission.