

Axis Bank: Counting on better times

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Despite asset quality concerns, the bank should be able to show healthy growth

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The RBI's asset quality review has spared few banks. Private banks that had managed to keep their stressed loans at bay also felt the heat last fiscal. Axis Bank with its higher exposure to troubled sectors, such as power and infrastructure, has been caught in the bad loans tangle, with gross non-performing assets (GNPA) zooming by 48 per cent (year-on-year) as of March 2016.

Through last fiscal, the bank's asset quality deteriorated, impacting the stock price. From its peak levels last year, the stock has lost about 15 per cent.

Axis Bank first took a sharp hit after its September 2015 quarter earnings, when investors were disappointed by the sale of two accounts worth ₹1,820 crore to asset reconstruction companies (ARCs), as this meant a substantial jump in its stressed assets.

In the December quarter, the bank added ₹2,082 crore to bad loans, half of this owing to the RBI's asset quality review. In the March quarter, while the bank added a lower ₹1,474 crore to bad loans, stressed assets addition of about ₹7,300 crore for FY16 has been a cause for worry.

But while the bank is likely to see some more pain in the current fiscal, investors can use the price correction as an opportunity to buy the stock for the long term.

Growth in loans

For one, after its fall, the stock now trades at 1.9 times its one-year forward book value, which is lower than its five-year historical average of about two times.

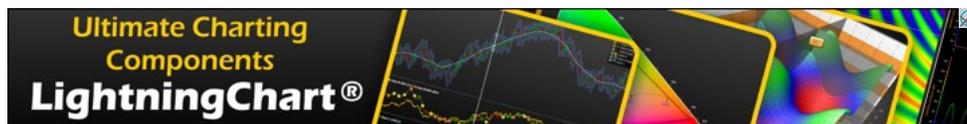
Given an expected earnings growth of 20-22 per cent over the next two years, there is scope for upside in the stock from the current levels. Despite the moderate earnings performance (12 per cent growth) in FY16, the bank is well capitalised — tier I capital ratio is at 12.5 per cent — to cushion earnings and fund its next leg of growth.

While the bank continues to witness stress in its corporate loan book, its retail segment has been on a strong wicket. The bank's loan growth in 2015-16 was driven by 24 per cent growth in retail loans. The 21 per cent overall growth in loans has thus been far higher than the banking sector's abysmal 8-9 per cent growth levels.

Building a healthy deposit base has helped Axis Bank maintain its net interest margin (NIM) within a band of 3.5-3.8 per cent over the last five years.

Most public sector banks have seen margins come under pressure due to weak credit growth, lower retail exposure and fall in share of low-cost current account and savings bank (CASA) deposits. In this scenario, the ability of private banks, including Axis Bank, to improve margins is significant.

Lower cost of funds helped Axis Bank increase its net interest margin for the year ended March 2016 by about 16 basis points over the previous year. This despite lending rates falling aggressively over the past year following RBI's rate cuts. The bank's CASA deposits grew 17 per cent in 2015-16, constituting 47 per cent of total deposits compared with 45 per cent last year. However, NIM may come under pressure under the new marginal cost of funds-based lending rate, as about 80 per cent of Axis Bank's loans are floating rate loans.



Watch list

Axis Bank has created a watch list, which it believes could be the key source of future stress in the corporate loan book. Outstanding accounts of around ₹22,600 crore are on the watch list, which is about 13 per cent of the bank's corporate loans and 6 per cent of its total loans. Corporate loans for Axis Bank are about 45 per cent of total loans.

The bank expects 60 per cent of these accounts to become bad loans in the next eight quarters. Iron & steel and power constitute a chunk of this list (23-24 per cent each).

Interestingly, about 72 per cent of restructured and SDR loans are on the watch list. Axis Bank has restructured loans to the tune of ₹3,740 crore under the 5:25 scheme and ₹575 crore under strategic debt restructuring (SDR) in FY16.

The management still remains cautious on asset quality for the current fiscal, with expectations of slippages similar to that seen last fiscal.

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