

Business Standard

Multiple triggers could boost Axis Bank's return ratios, say analysts

Lower credit cost, operating leverage and shift in loan mix are key positives

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Axis Bank | Photo: Shutterstock

Outperforming closest peer ICICI Bank, the stock of Axis Bank has gained a sharp 30 per cent since the start of 2019, when the new Managing Director and Chief Executive Officer Amitabh Chaudhary took charge. Analysts highlight multiple triggers which could boost the bank's return ratios going ahead. HDFC Securities' Darpin Shah and Aakash Dattani believe that improving asset quality (with rising coverage), better risk practices, focus on high-yielding retail products, and cost consciousness will drive earnings. This should also improve the return ratio (return on assets and return on equity) of the bank.

Brokerages also expect the trend of lower slippages (accounts turning bad) in FY19 that improve the overall earnings to continue, though there could be some effect from macro headwinds.

Decline in stressed assets and sub-investment-grade loan accounts (indicates high default probability) shows that the asset-quality cycle, mainly from the corporate pool, has peaked out. This along with the management's confidence in terms of retail asset quality is expected to lower slippages. In fact, higher share of retail assets (50 per cent of total advances as of March 2019) offers further comfort in terms of asset quality.

The bank's annual report points to a strong risk management architecture that has helped keep asset quality in retail better than peer average. With slippages likely to contract by over 100 basis points over the next two years, provisioning as a percentage of assets (credit cost) would also come down by 100 basis points in FY20 and 30 basis points a year after. Gross non-performing assets (NPAs) or bad loans should also trend lower. Besides, improvement in provision coverage ratio (including write offs) to 77 per cent in FY19 from 65 per cent in FY18, will further curb incremental provisioning requirement for the bank, states a Motilal Oswal Financial Services report.

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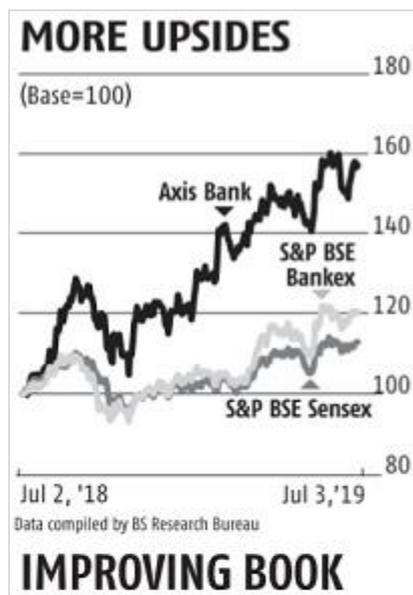
Further provisioning comfort also stems from the bank's aim to move towards conservative approach on provisioning, risk and compliance. It has increased provisioning over and above the regulatory requirement on weak yet standard assets.

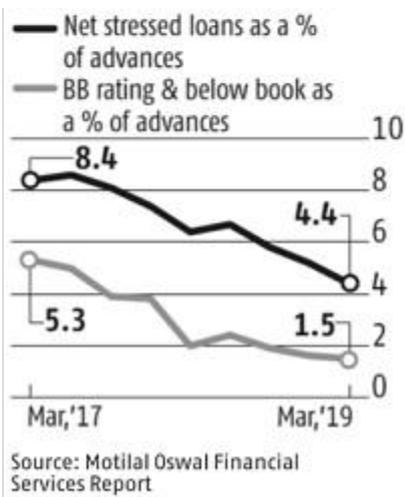
This apart, lower operating cost amid higher focus on technology and falling proportion of branch format despite branch additions of around 900 over the next few years, would also help.

There is also a shift in retail product mix with higher share of high-yield products such as credit card, personal loan, among others. This should help in taking care of the bank's top line even as the cost of deposits is likely to rise amid lukewarm deposit growth of the banking industry. Even for Axis Bank cost of term deposits was 22 basis point higher in FY19. As per the annual report, the bank's focus is now on retail term deposit besides current and savings accounts.

In fact, Chaudhary believes that the banking industry has seen return of credit growth and pricing power on account of shift in credit demand from NBFCs and bond markets back to banks. Axis Bank seems to be well positioned to leverage this opportunity given its branch network (4,050 branches) and capital position (capital adequacy 15.8 per cent as of March 2019).

Overall, if the bank performs as per the expectations, sharp upsides in the stock cannot be ruled out. Some analysts expect upsides of 11-14 per cent over the next year from current levels.





KEY LEVERS

| Figures in % | FY17 | FY18 | FY19 | FY20E | FY21E |
|------------------|------|------|------|-------|-------|
| Provisioning | 3.1 | 4.1 | 2.2 | 1.2 | 0.9 |
| Operating cost | 2.2 | 2.2 | 2.1 | 2.1 | 2.0 |
| Return on assets | 0.7 | 0.0 | 0.6 | 1.1 | 1.4 |
| Return on equity | 6.8 | 0.5 | 7.2 | 13.3 | 16.2 |
| Gross NPAs | 5.0 | 6.8 | 5.3 | 4.5 | 3.5 |

E: estimated, Barring gross NPAs, figures are as a percentage of average assets except for return on equity NPAs: non-performing assets
Sources: Bank and brokerage reports