

June 1, 2024

SECTOR REPORT | Sector: Banks

Banking Sector Report

Credit cost, margin and other aspects

While credit cost, at the aggregate sector level, is not a major problem, there clearly are distinct winners and losers on either side of the spectrum of credit cost performance. In this regard, we draw the following key conclusions (1) Banks whose actual FY24 credit cost most exceeded FY24E consensus (negative read) are IDFCB, RBL and IIB, the latter on an adjusted analysis (2) Banks whose actual FY24 credit cost most lagged FY24E consensus (positive read) are AXSB, CUB, FED and BOB. Further, (3) BOB and INBK have a larger share of MCLR book, which implies that the potential impact of upcoming rate cuts would be more manageable (4) Structurally, over 5 years, AXSB, CSB and ICICI are the banks which have seen the most constructive rise in share of higher-yielding loans (5) INBK have the most improved liability profile over the past 12 months and without resorting to premium SA rates.

Banks whose actual FY24 credit cost most exceeded FY24E consensus (negative read) are IDFCB, RBL and IIB, the latter on adjusted basis

IDFCB and RBL missed consensus by 26 and 10 bps, respectively. IIB roughly met consensus but its utilisation of contingent provisions made credit cost look better by 28 bps. Notably, these are banks that have *already* been in our least preferred list and this analysis of credit cost gives us incremental reason to remain cautious on these names.

Banks whose actual FY24 credit cost most lagged FY24E consensus (positive read) are AXSB, CUB, FED and BOB

AXSB, CUB, FED and BOB beat consensus by 23, 18, 16 and 9 bps, respectively. Again, notably, some of these banks have *already* been in our most preferred list and which remain so, viz. BOB, FED and AXSB. On the other hand, we had recently upgraded CUB for the first time since we started covering it 3 years ago. We believe that comparing actual credit cost in FY24 to Bloomberg consensus is key to understanding how banks are delivering compared with what is priced in.

BOB and INBK have a larger share of MCLR book, which implies that the potential impact of upcoming rate cuts would be more manageable

The share of non-EBLR floating rate book for BOB and INBK is 63% and 60%, respectively. A higher share of MCLR-linked loans implies that the impact of declining rates would be felt in slower staggered manner and, also, on both side of the balance sheet, with the net impact on margin being concomitantly lower. KMB has a high share of EBLR loans at ~59% and, hence, is technically more vulnerable. The relatively lower loan to deposit ratio for INBK, SBI and BOB stood at 74.8%, 75.3% and 80.3%, respectively continues to provide a near-term cushion, *ceteris paribus*.

Structurally, over 5 years, AXSB, CSB and ICICI are the banks which have seen the most constructive rise in share of higher-yielding loans

Over FY19-24, the share of low-yield loans has declined 15.5%, 12.4%, 10.4%, 10.3% and 9.6%, respectively, for these banks. However, we do not regard the outstanding loan book mix of IDFCB and RBL to be optimal since the share of high/very-high yield loans is sub-optimally high. Hence, we regard the evolution of AXSB, ICICI and CSB to be most admirable in this regard.

INBK has the most improved liability profile over the past 12 months and without resorting to premium SA rates

INBK has seen the greatest improvement in share of LCR retail deposits over 12 months, amounting to ~800 bps, respectively. Importantly, this has been achieved without premium SA rates.

We most prefer BOB, FED, AXSB, INBK, SBI and ICICI whereas we least prefer KMB, IIB, IDFCB, RBL and DCB

Our top 6 consists of a judicious mix of PSU and private sector banks. We had upgraded CUB to BUY in Feb 2024 and we believe it is an interesting smallcap play. We had also upgraded HDFCB to BUY in Feb 2024 but it is quite low in our pecking order. 3 of our least preferred names, viz. IIB, IDFCB and RBL, have distinctly cyclical business models.

Recommendation table

Company	Rating	TP
BOB	BUY	350
FED	BUY	210
AXSB	BUY	1475
INBK	BUY	715
SBIN	BUY	1025
ICICIBC	BUY	1375
CUB	BUY	175
CSBBANK	BUY	400
HDFCB	BUY	1850
KMB	ADD	2000
IIB	ADD	1735
IDFCFB	ADD	90
RBK	ADD	290
DCB	ADD	150

N.B. In order of investment preference

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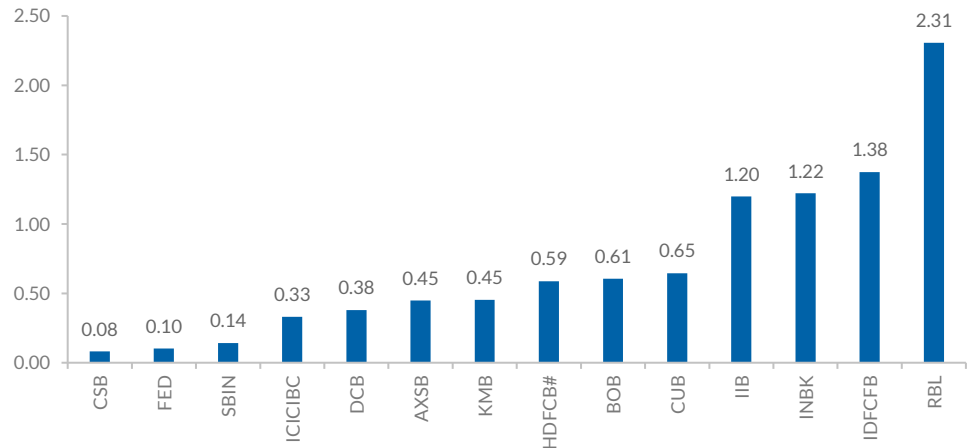
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Asset Quality Aspects

Exhibit 1: Annualised Credit Cost – FY24A - %

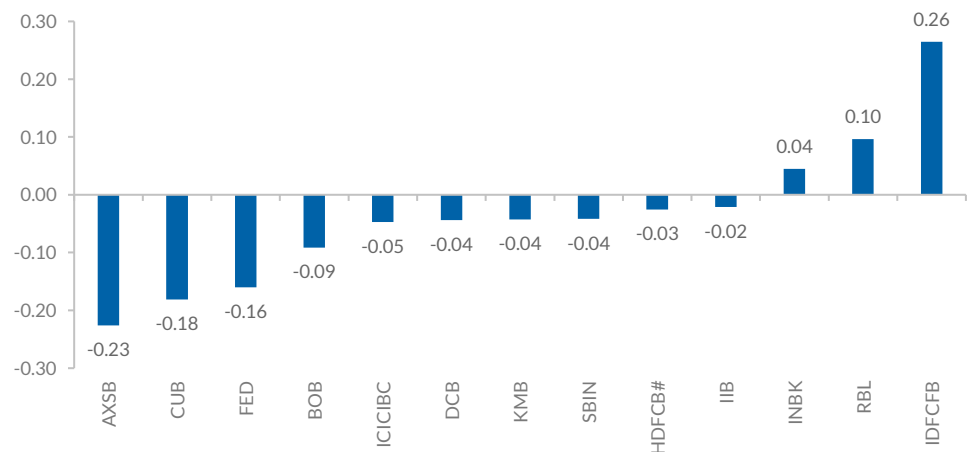


Source: Companies, YES Sec

Banks whose actual FY24 credit cost most exceeded FY24E consensus (negative read) are IDFCB, RBL and IIB, the latter on adjusted basis

IDFCB and RBL missed consensus by 26 and 10 bps, respectively. IIB roughly met consensus but its utilisation of contingent provisions made credit cost look better by 28 bps. Notably, these are banks that have *already* been in our least preferred list and this analysis of credit cost gives us incremental reason to remain cautious on these names.

Exhibit 2: Annualised Credit Cost – FY24 – Actual - Consensus- %



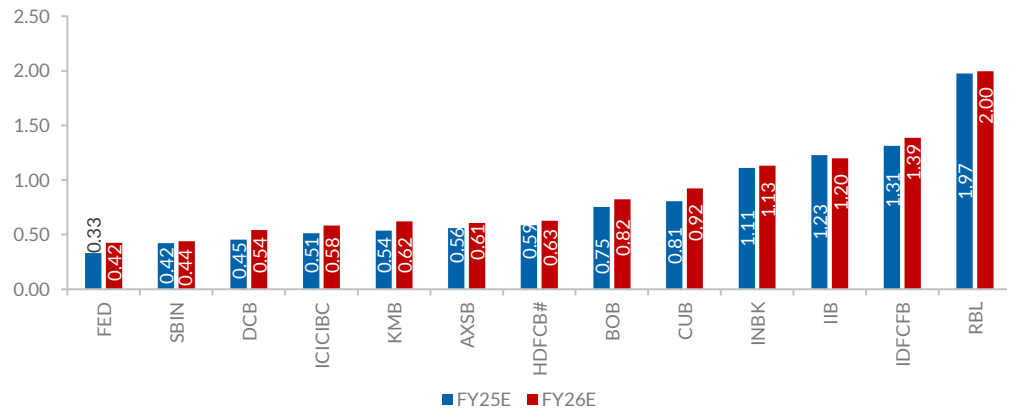
Source: Companies, YES Sec

Banks whose actual FY24 credit cost most lagged FY24E consensus (positive read) are AXSB, CUB, FED and BOB

AXSB, CUB, FED and BOB beat consensus by 23, 18, 16 and 9 bps, respectively. Again, notably, some of these banks have *already* been in our most preferred list and which remain so, viz. BOB, FED and AXSB. On the other hand, we had recently upgraded CUB for the first time since we started covering it 3 years ago. We believe that comparing actual credit cost in FY24 to Bloomberg consensus is key to understanding how banks are delivering compared with what is priced in.

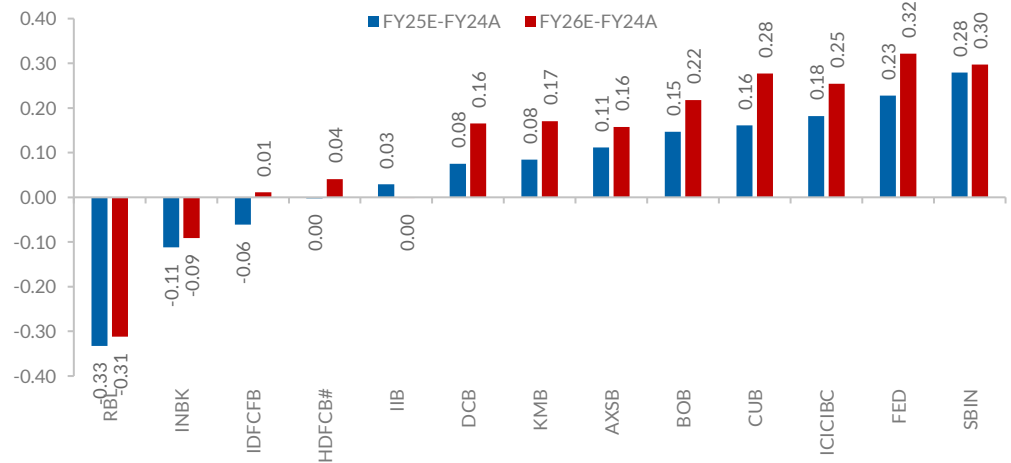
We also take this opportunity to examine credit cost consensus that the street has currently pencilled in for FY25E/26E

Exhibit 3: Prospective Consensus Credit Cost – Absolute level – FY25E-FY26E - %



Source: Companies, YES Sec

Exhibit 4: Credit Cost – Differential – FY25E over FY24A, FY26E over FY24A - %



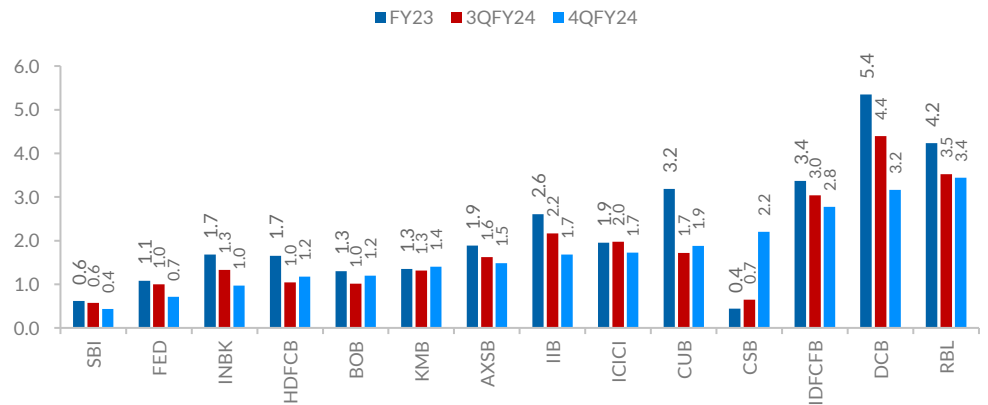
Source: Companies, YES Sec

Additional Asset Quality Aspects

Recent gross slippage trends for RBL, DCB and IDFCB are still not satisfactory

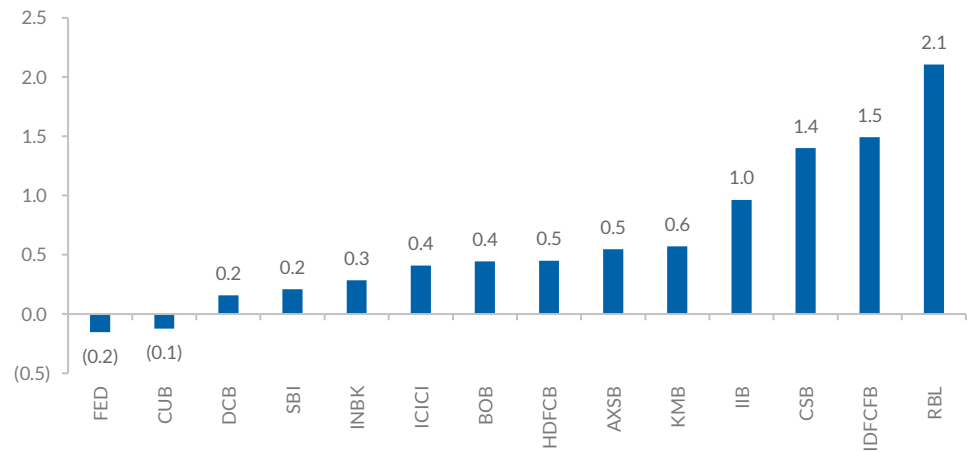
The gross slippage ratio of RBL, DCB and IDFCB in 4Q are 3.4%, 3.2% and 2.8%, respectively, which are on the higher side.

Exhibit 5: Annualised Gross Slippage Ratio* - Absolute level - FY23, 3QFY24 and 4QFY24- %



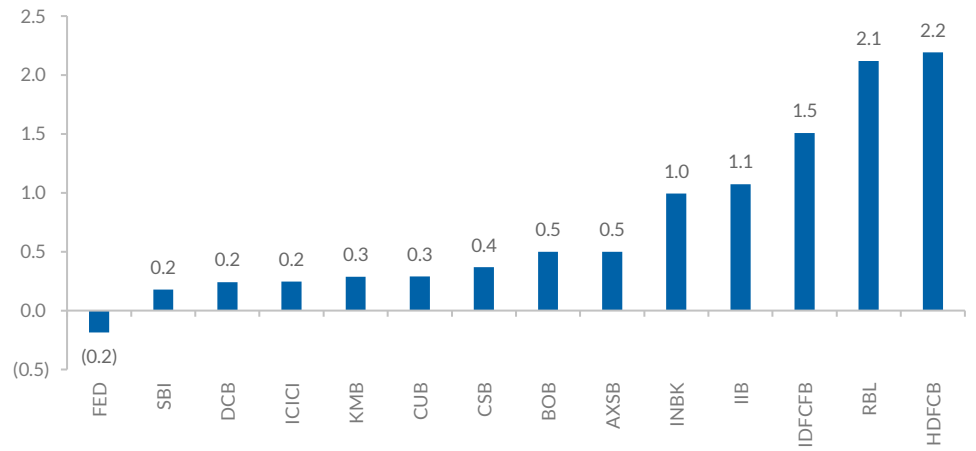
Source: Companies, YES Sec, *Annualised Gross NPA Addition Ratio

Exhibit 6: Annualised Net Slippage Ratio - Absolute level - 4QFY24 - %



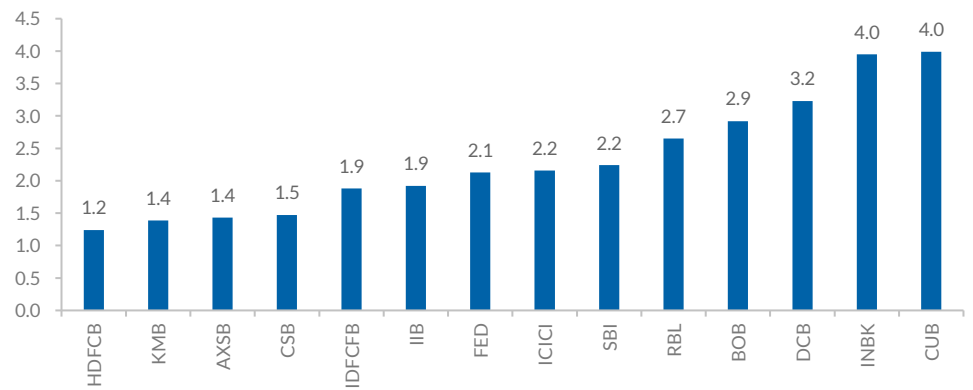
Source: Companies, YES Sec

Exhibit 7: Annualised Credit Cost – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

Exhibit 8: Gross NPA – Absolute level - 4QFY24 - %

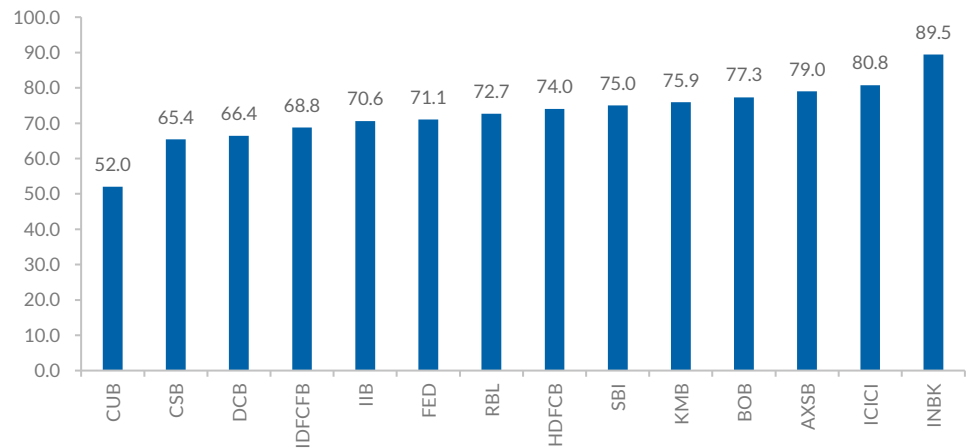


Source: Companies, YES Sec

INBK, ICICI, AXSB, BOB and KMB are the best-provisioned banks from a PCR standpoint

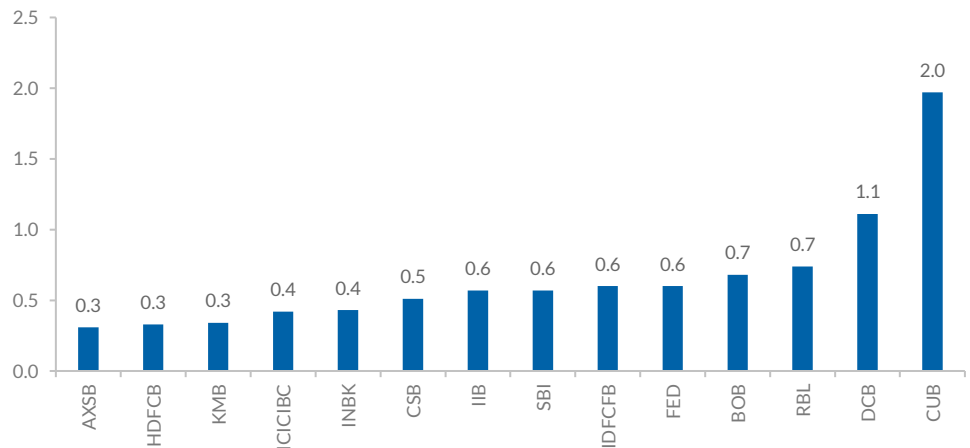
The PCR of INBK, ICICI, AXSB, BOB and KMB is 89.5%, 80.8%, 79.0%, 77.3% and 75.9%, respectively and indicative of healthy specific provision coverage.

Exhibit 9: Provision Coverage Ratio (Ex. TWO) – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

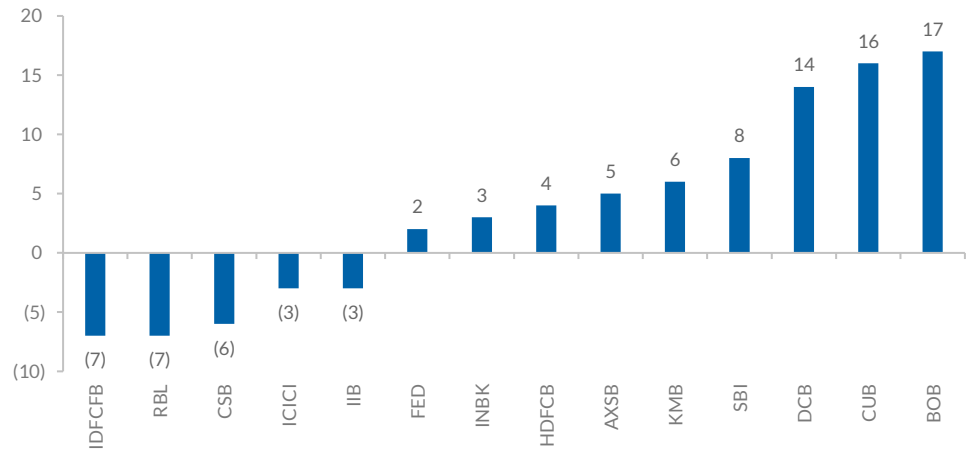
Exhibit 10: Net NPA – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

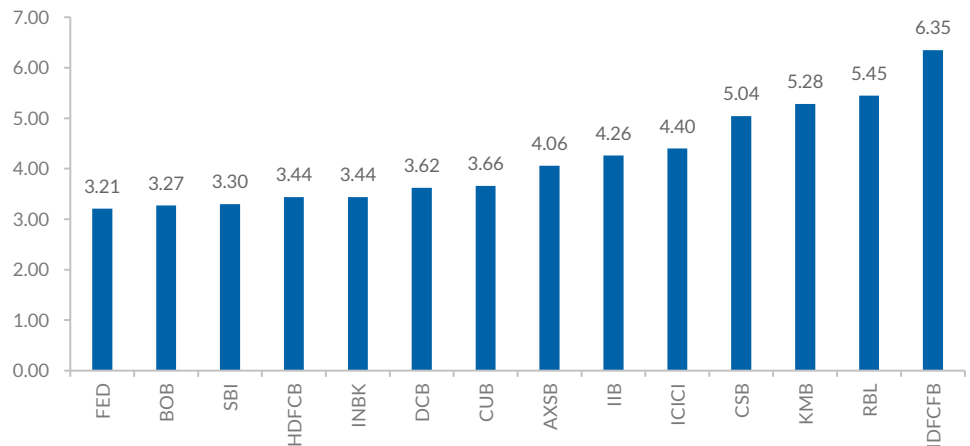
Margin Aspects

Exhibit 11: Sequential change in NIM – 4QFY24 over 3QFY24 - bps



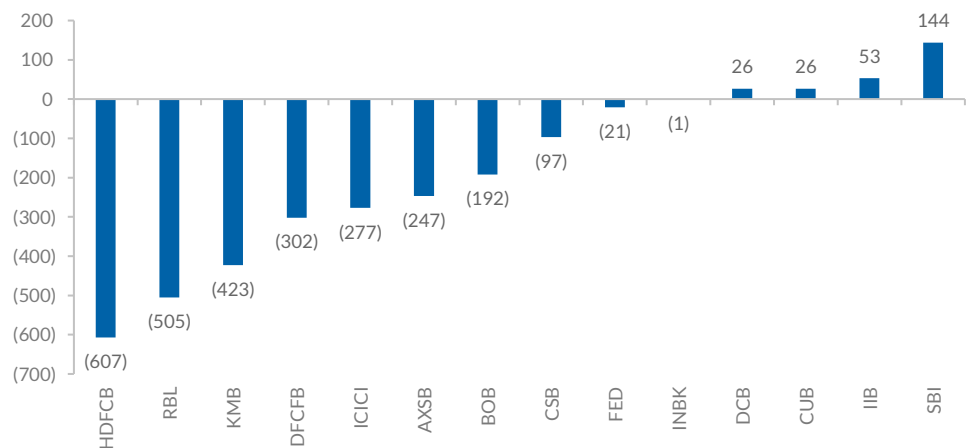
Source: Companies, YES Sec

Exhibit 12: Net Interest Margin – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

Exhibit 13: Sequential change in Loan to Deposit ratio – 4QFY24 over 3QFY24 - bps

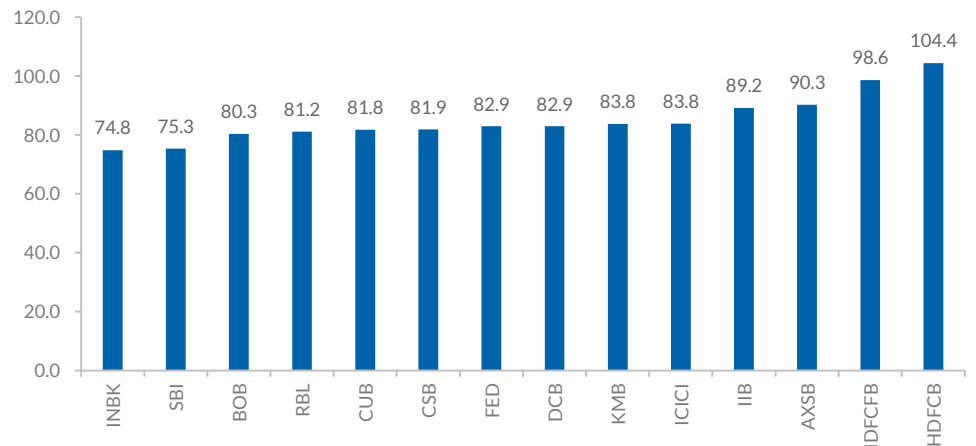


Source: Companies, YES Sec

Post the merger, HDFCB is now at a high loan to deposit ratio (LDR), while IDFCB was already at a high LDR

The LDR for HDFCB and IDFCB is 104.4% and 98.6%, respectively, which is the highest in our coverage universe.

Exhibit 14: Loan to Deposit ratio - Absolute level - 4QFY24 - %

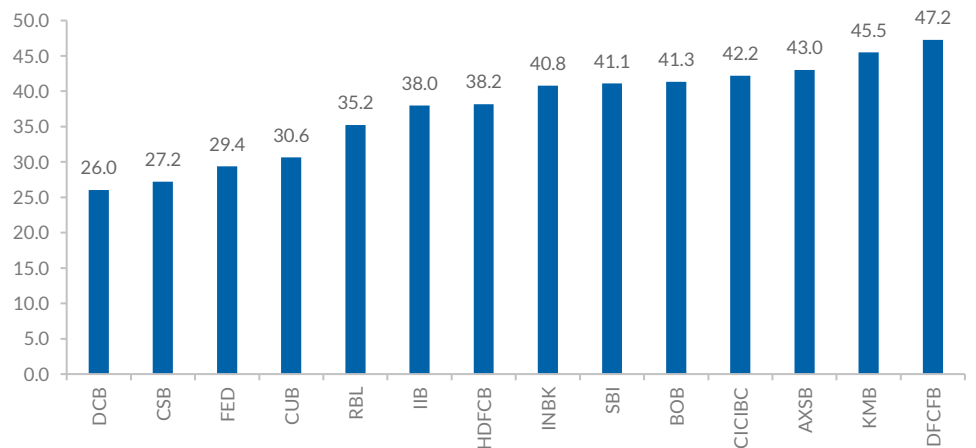


Source: Companies, YES Sec

Driven by the Citi acquisition, AXSB has a healthy CASA ratio without dependence on premium SA rates

IDFCB, KMB and AXSB have the healthiest CASA ratios of 47.2%, 45.5% and 43.0% but KMB and IDFCB have achieved the same using premium SA rates.

Exhibit 15: CASA ratio - Absolute level - 4QFY24 - %

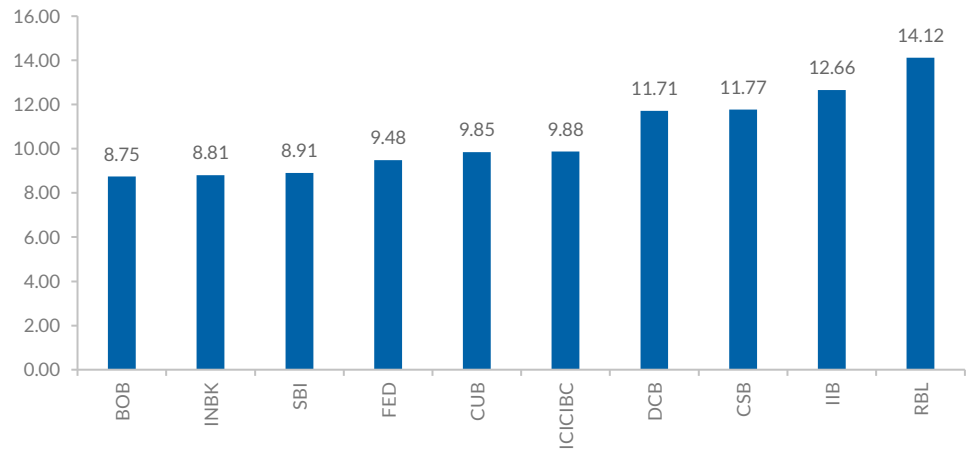


Source: Companies, YES Sec

We regard high yield on advances for RBL, IIB and DCB as reflective of a largely cyclical and sub-optimal business model

The yield on advances for RBL, IIB, CSB and DCB was 14.12%, 12.66%, 11.77% and 11.71%, respectively and the highest in our coverage universe.

Exhibit 16: Yield on Advances – Absolute level - 4QFY24 - %

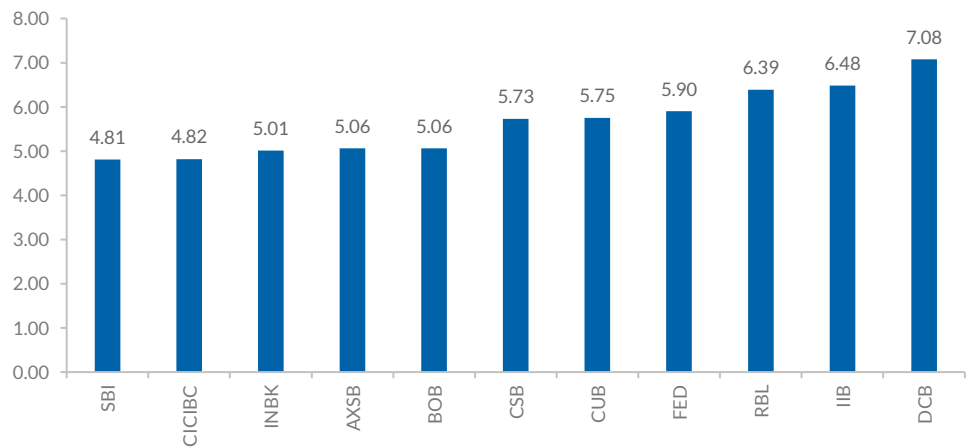


Source: Companies, YES Sec

AXSB has the fourth best cost of deposits behind SBI, ICICI and INBK and will try to bridge the gap

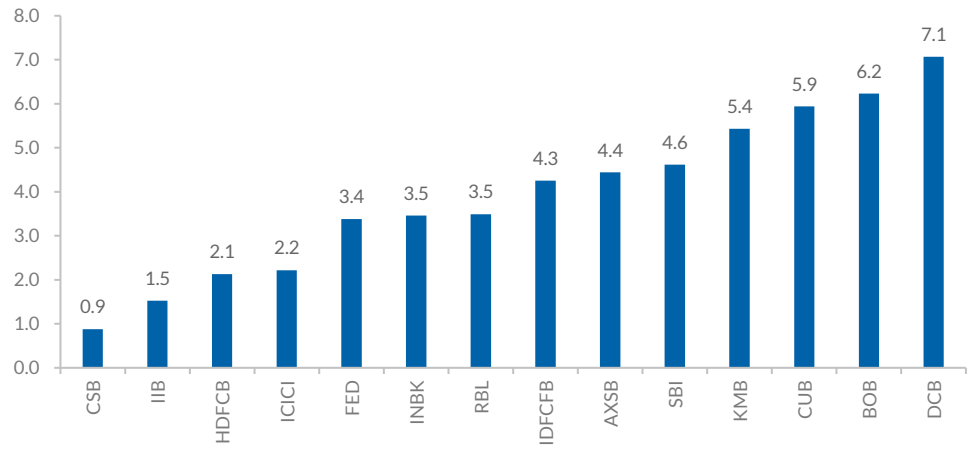
SBI, ICICI, INBK and AXSB have the lowest cost of deposits at 4.81%, 4.82%, 5.01% and 5.06%, respectively, in our coverage universe.

Exhibit 17: Cost of Deposits – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

Exhibit 18: Sequential Net Interest Income Growth – 4QFY24 over 3QFY24 - %



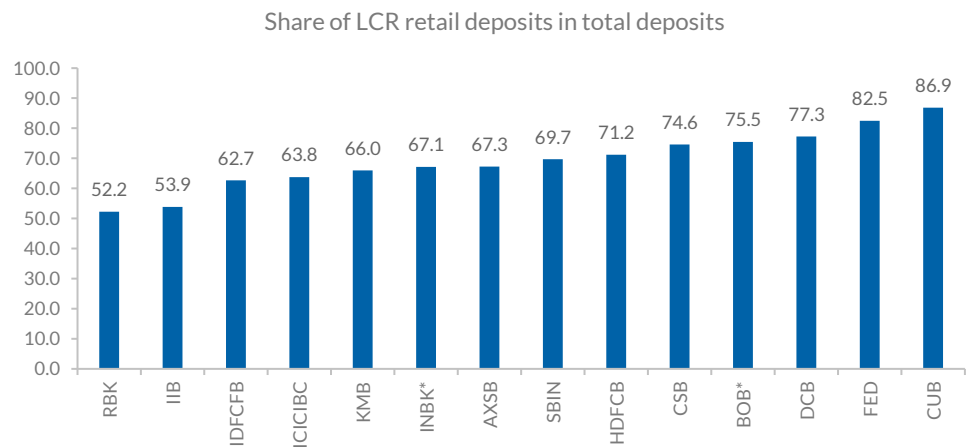
Source: Companies, YES Sec

Granularity of Deposits

CUB and FED have the highest share of LCR retail deposits in our coverage universe

CUB and FED have the highest share of LCR retail deposits at 86.6% and 82.5%, respectively. However, CUB's high share is partly the result of not growing the loan book and hence, not needing to raise wholesale deposits. On the other hand, FED has normalised its business model, reducing its excessive dependence on retail deposits in pursuit of growth.

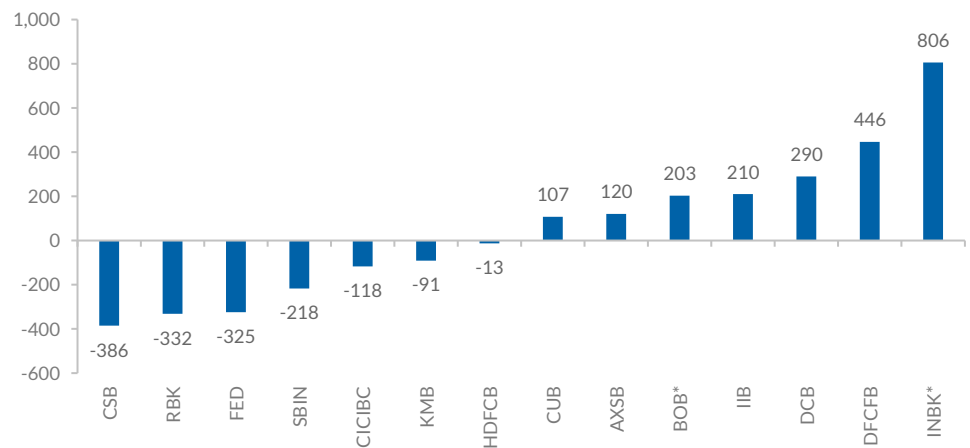
Exhibit 19: Share of LCR Retail Deposits- 4QFY24 - %



Source: Companies, YES Sec – Research, *For 3QFY24

INBK and IDFCFB have seen the greatest improvement in share of LCR retail deposits over 12 months

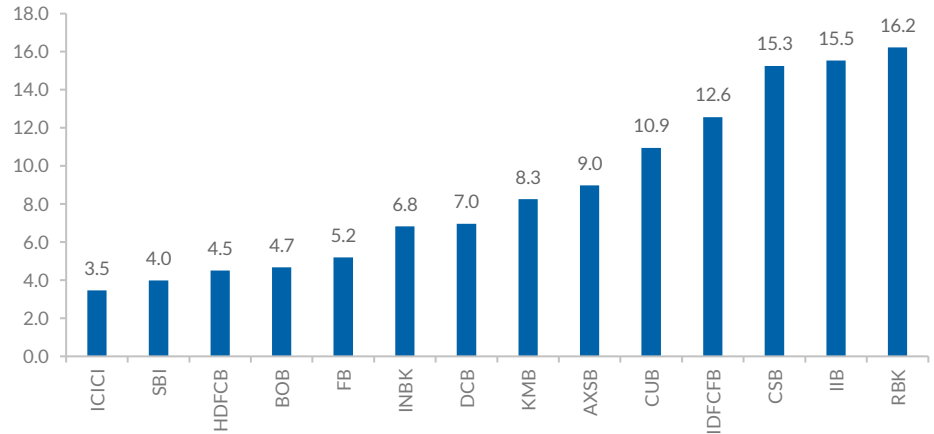
Exhibit 20: Change in Share of LCR Retail Deposits – 4QFY23 to 4QFY24 - bps



Source: Companies, YES Sec – Research, *For 3QFY24

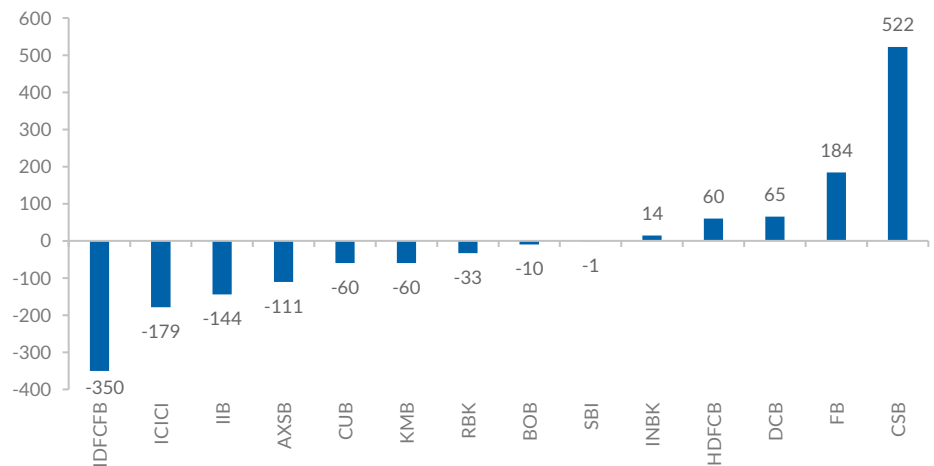
N.B. LCR retail deposits are the unweighted values of Retail deposits and deposits from small business customers as per LCR disclosures. The share of retail deposits is calculated as the unweighted values of Retail deposits and deposits from small business customers divided by sum of unweighted values of Retail deposits and deposits from small business customers + Unsecured wholesale funding + Secured wholesale funding as per LCR disclosures.

Exhibit 21: Share of 20 largest depositors in total deposits – March 2023 - %



Source: Companies, YES Sec - Research

Exhibit 22: Change in Share of 20 largest depositors - FY23 - bps



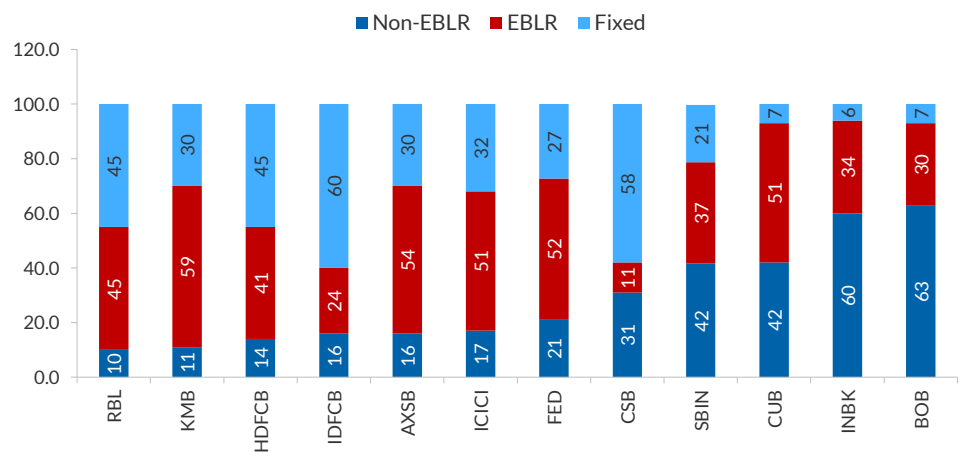
Source: Companies, YES Sec - Research

Loan Book by Rate Category

We do not think that the upcoming rate cut cycle is particularly important given the cumulative quantum of rate cuts is likely to be shallow

While it is important to look at loan book mix at rate category, the RBI may only cut key interest rates by a total of 50 bps, reducing the danger to yield erosion in the relative sense.

Exhibit 23: Break-up of loan book by rate category - %

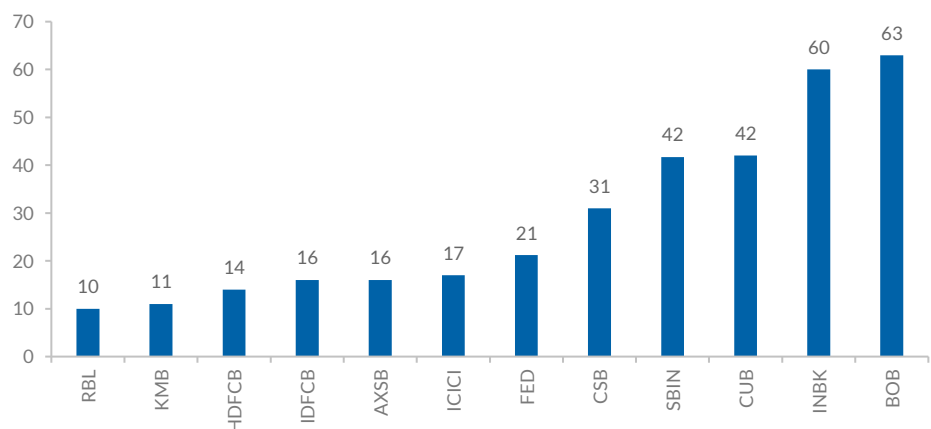


Source: Companies, YES Sec – Research, Sorted on non-EBLR

BOB and INBK have a larger share of non-EBLR floating rate loan book, which implies that the impact of declining rates would be more manageable

A higher share of non-EBLR floating rate book implies a higher share of MCLR book as MCLR is the lion’s share of the non-EBLR floating rate book. The share of non-EBLR floating rate book for BOB and INBK is 63% and 60%, respectively. A higher share of MCLR-linked loans implies that the impact of declining rates would be felt in slower staggered manner and also, on both side of the balance sheet, with the net impact on margin being concomitantly lower.

Exhibit 24: Share of Non-EBLR floating loans in total loan book - %

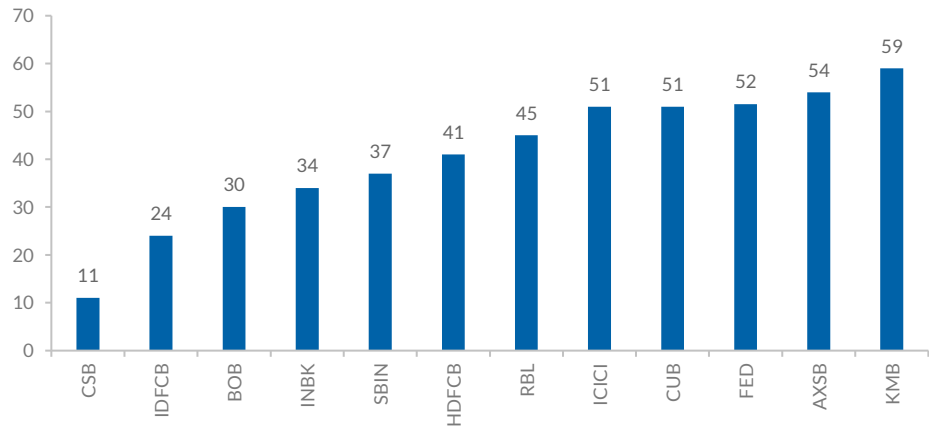


Source: Companies, YES Sec – Research

KMB has a high share of EBLR loans and, hence, is technically more vulnerable to the upcoming rate cut cycle

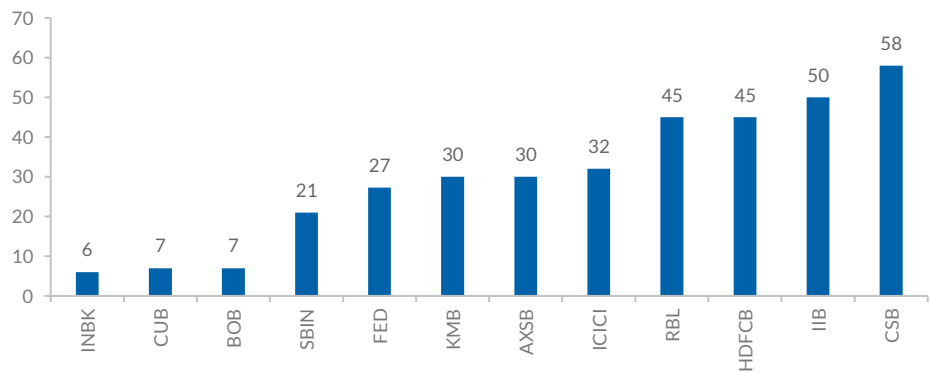
The share of EBLR loans for KMB is about 59%. If the RBI starts cutting interest rates, the yield of this bank would be impacted more.

Exhibit 25: Share of EBLR loans in total loan book - %



Source: Companies, YES Sec – Research

Exhibit 26: Share of fixed loans in total loan book - %



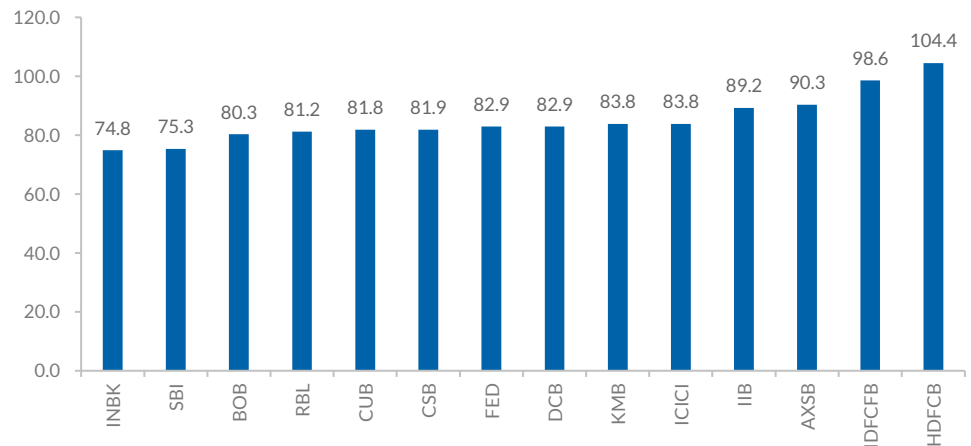
Source: Companies, YES Sec – Research

Liquidity Aspects

Loan to deposit ratio is the lowest for INBK, SBI and BOB in our coverage universe

The loan to deposit ratio for INBK, SBI and BOB stood at 74.8%, 75.3% and 80.3%, respectively. This provides a near-term cushion, ceteris paribus, from a need to raise deposits fast to meet loan demand.

Exhibit 27: Loan to Deposits Ratio - 4QFY24 - %

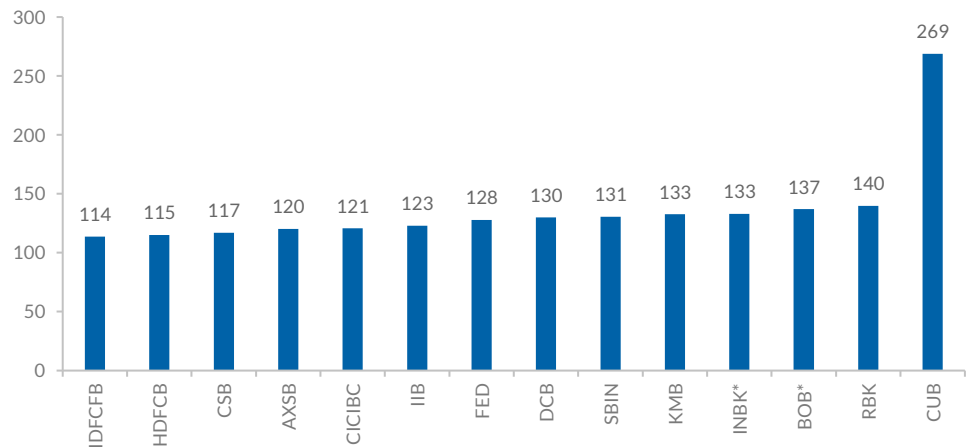


Source: Companies, YES Sec - Research

CUB has by far the highest LCR in our coverage universe and hence, is very comfortably placed on the liquidity front

CUB's high LCR is in consonance with its conservative approach in general.

Exhibit 28: Liquidity Coverage Ratio - 4QFY24 - %



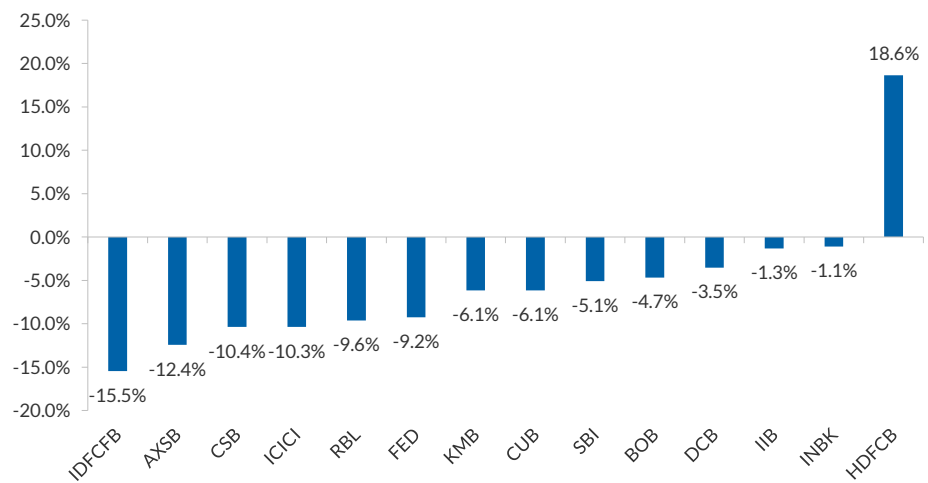
Source: Companies, YES Sec - Research, * for 3QFY24

Evolution of Loan book mix by Yield bucket and loan book mix

Over a 5-year period, IDFCB, AXSB, CSB, ICICI and RBL are the banks which have seen the greatest decline in low-yield loans

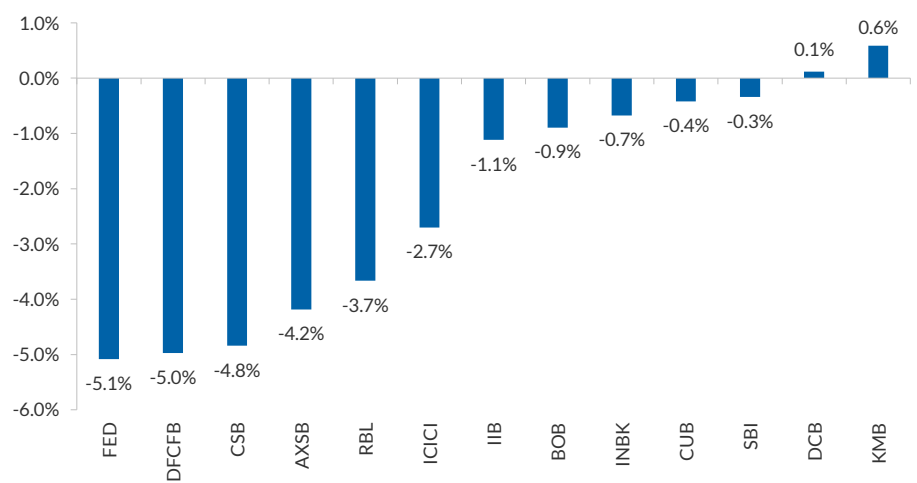
Over FY19-24, the share of low-yield loans has declined 15.5%, 12.4%, 10.4%, 10.3% and 9.6%, respectively. However, we do not regard the outstanding loan book mix of IDFCB and RBL to be optimal since the share of high/very-high yield loans are sub-optimally high. Hence, we regard the evolution of AXSB, ICICI and CSB to be most admirable in this regard.

Exhibit 29: 5-year delta in loan book composition - Low Yield - FY19 to FY24 - %



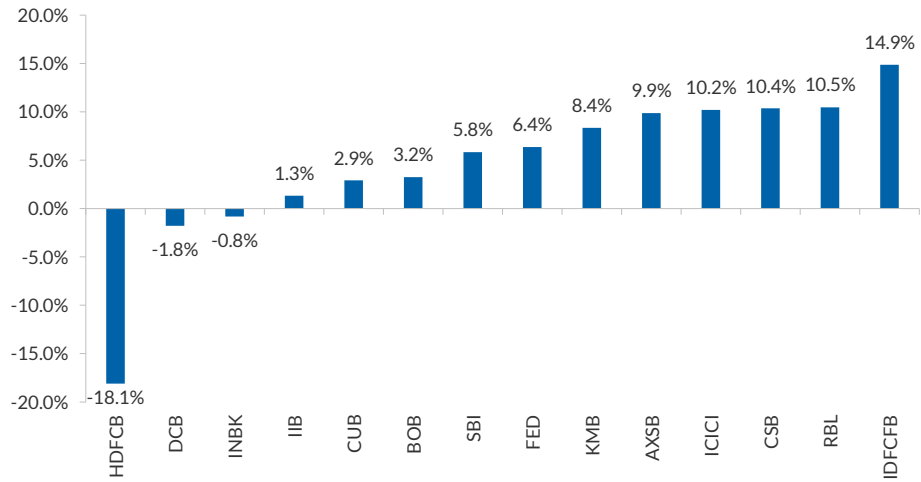
Source: Companies, YES Sec – Research

Exhibit 30: 1-year delta in loan book composition - Low Yield - FY23 to FY24 - %



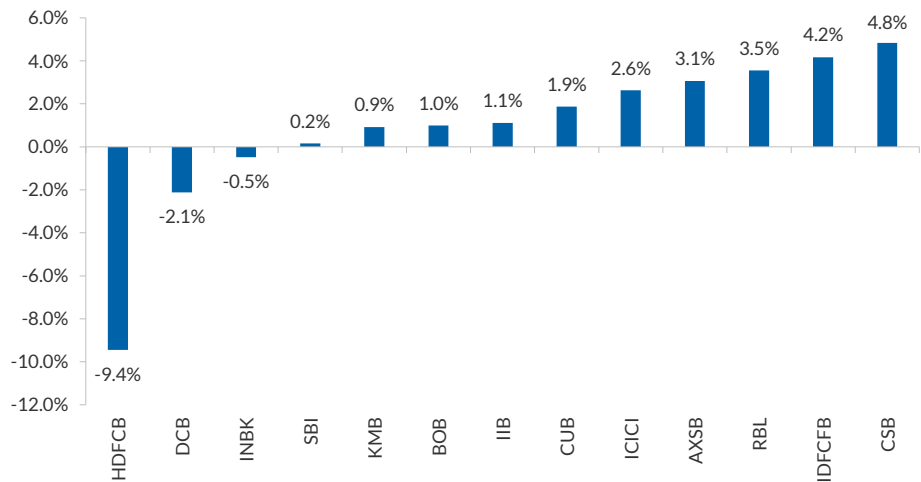
Source: Companies, YES Sec – Research

Exhibit 31: 5-year delta in loan book composition – High + Very Yield – FY19 to FY24 - %



Source: Companies, YES Sec – Research

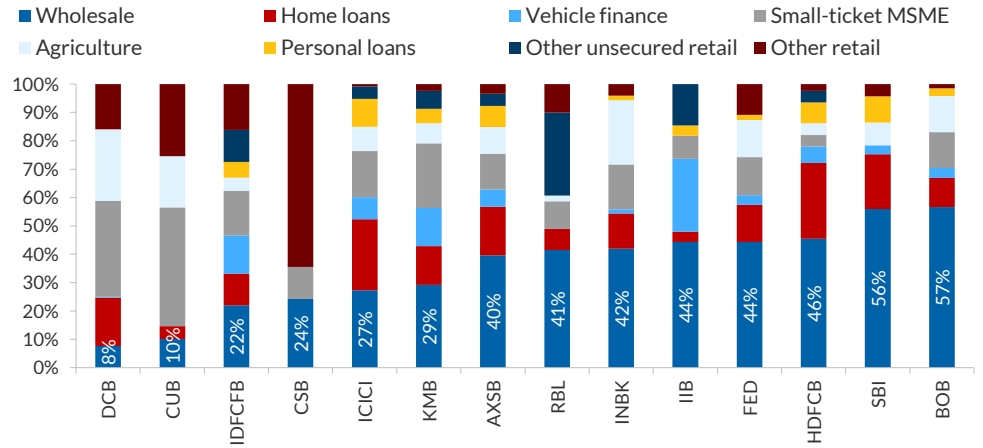
Exhibit 32: 1-year delta in loan book composition – High + Very Yield – FY23 to FY24 - %



Source: Companies, YES Sec – Research

N.B.: We have sub-divided loan books into (i) low yield, (ii) inter-mediate yield (iii) high yield and (iv) very high yield on the basis of yield profiles of the segmental buckets that had been arrived at earlier. We earmarked (1) wholesale loans and home loans as low-yield, (2) agri loans as inter-mediate-yield, (3) vehicle loans, small-ticket MSME, personal loans and other retail loans as high-yield and (4) other unsecured retail (credit card dues and microfinance) as very high-yield.

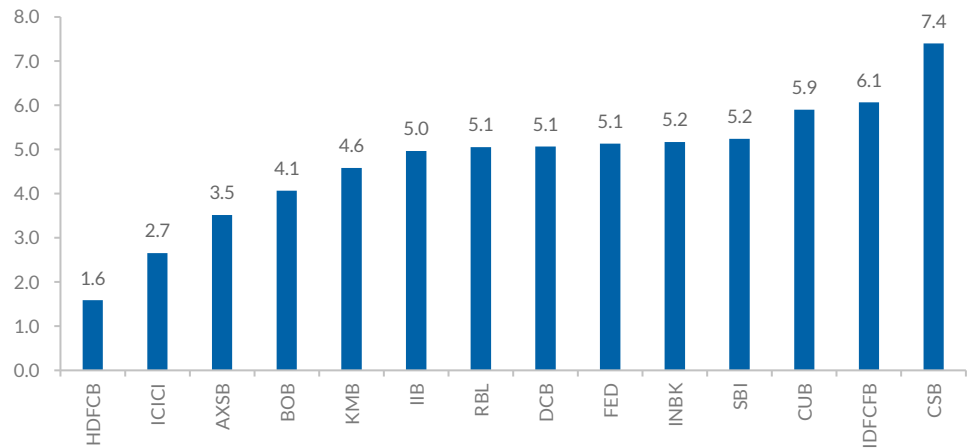
Exhibit 33: Loan book composition as per distinctly comparable buckets - 4QFY24 - %



Source: Companies, YES Sec – Research, Sorted on share of wholesale loans

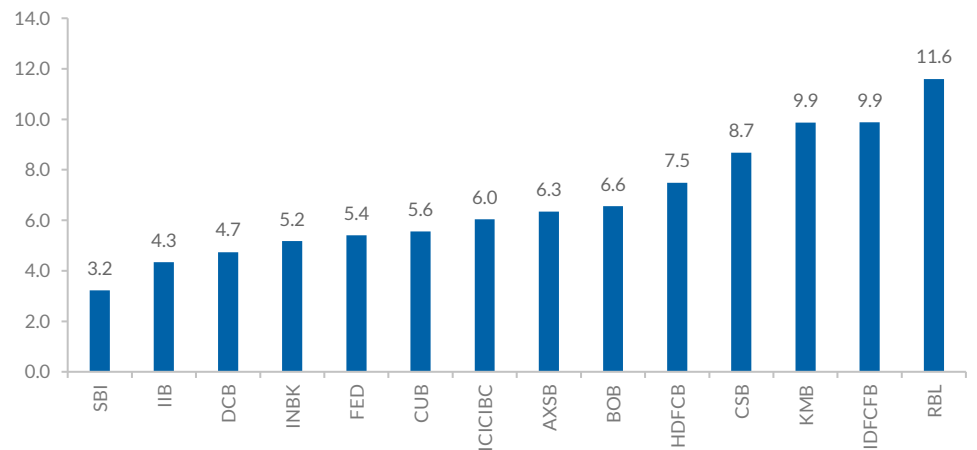
Balance sheet Growth

Exhibit 34: Sequential Loan Growth – 4QFY24 over 3QFY24 - %



Source: Companies, YES Sec

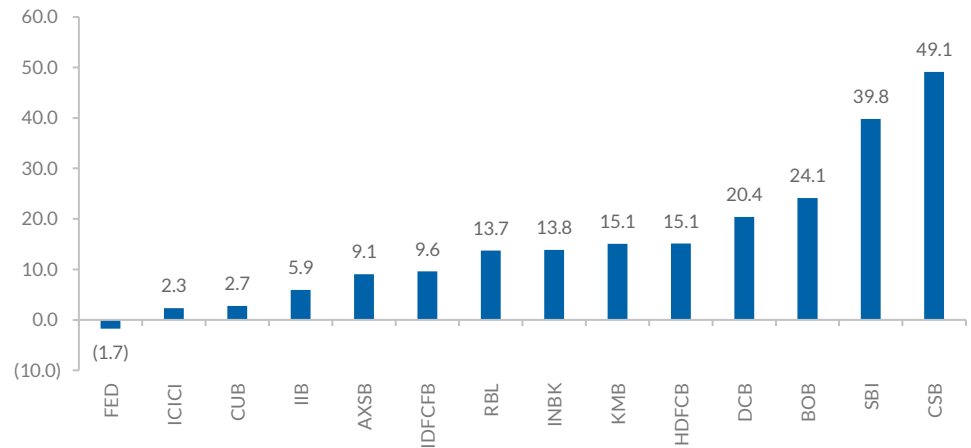
Exhibit 35: Sequential Deposits Growth – 4QFY24 over 3QFY24 - %



Source: Companies, YES Sec

Fee Income Aspects

Exhibit 36: Sequential Core Fee Growth – 4QFY24 over 3QFY24 - %

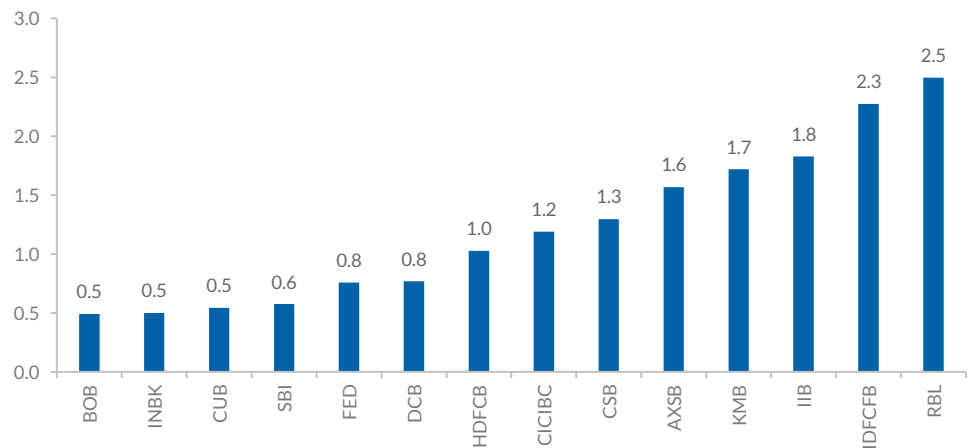


Source: Companies, YES Sec

Fee income to assets is healthy for AXSB without dependence on ultra-small unsecured ticket lending

The fee income to assets for RBL, IDFCB, IIB, KMB and AXSB is 2.5%, 2.3%, 1.8%, 1.7% and 1.6%, respectively and the highest in our coverage universe.

Exhibit 37: Fee Income to Average Total Assets – Absolute level - 4QFY24 - %

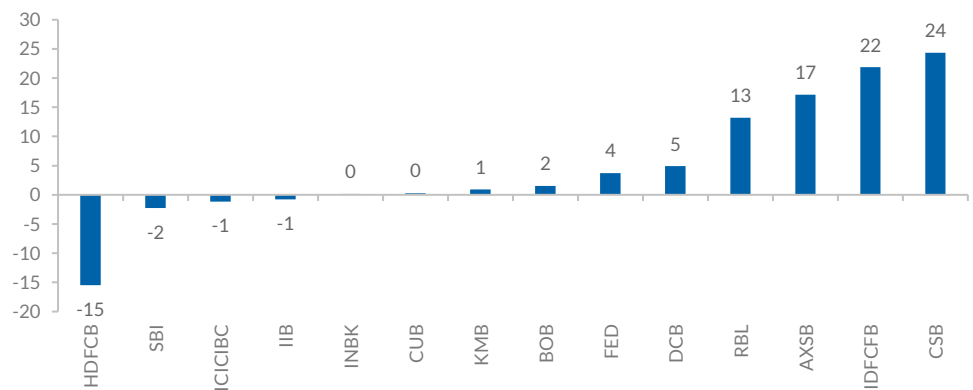


Source: Companies, YES Sec

AXSB is the largecap bank with the most improved fee income to assets in FY24 compared with FY23, admittedly due to the Citi acquisition likely contributing

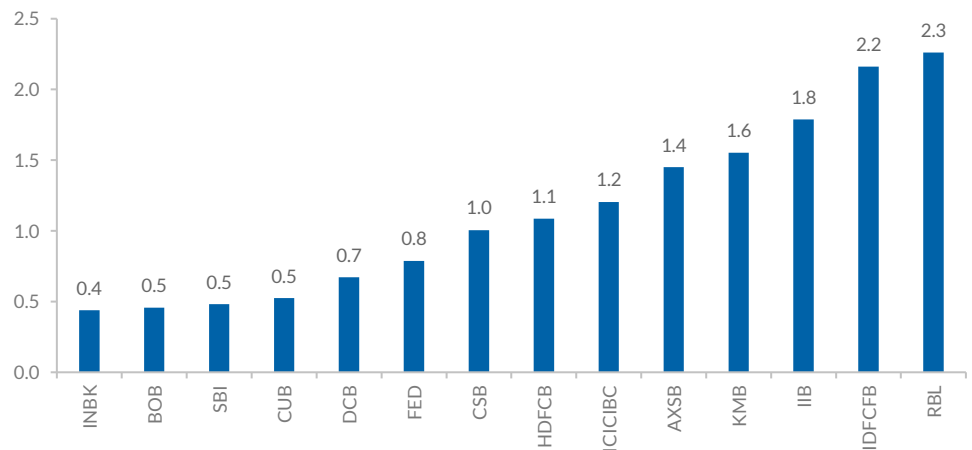
The fee income to assets for AXSB has risen 17bps in FY24 compared with FY23. The Citi acquisition has brought a material credit cards business to the fold, which would have provided a fillip to fee income. The rise has also been healthy for CSB, IDFCB and RBL at 24 bps, 22 bps and 13 bps, respectively. However, IDFCB and RBL are achieving this basis a sub-optimal dependence on small-ticket unsecured lending.

Exhibit 38: Change in Fee Income to Average Assets–FY24 over FY23 - bps



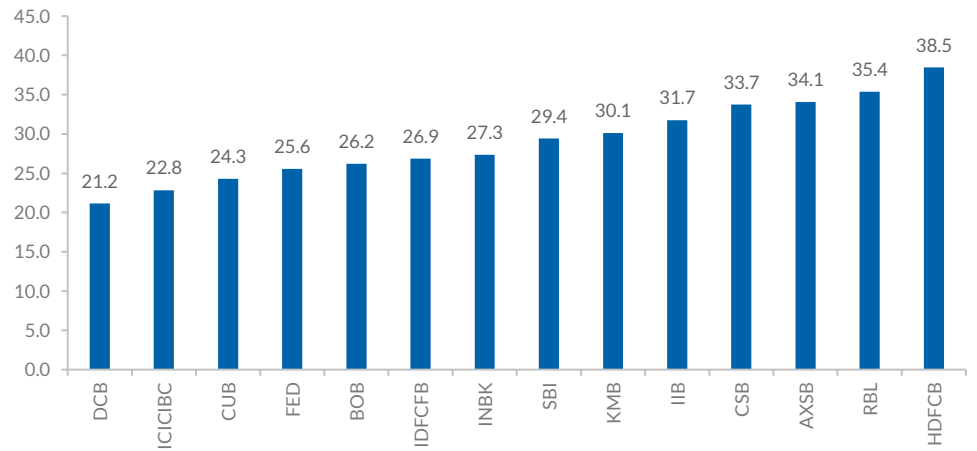
Source: Companies, YES Sec

Exhibit 39: Fee income to average total assets–FY24 - %



Source: Companies, YES Sec

Exhibit 40: Non-Interest Income to Total income - Absolute level - 4QFY24 - %



Source: Companies, YES Sec

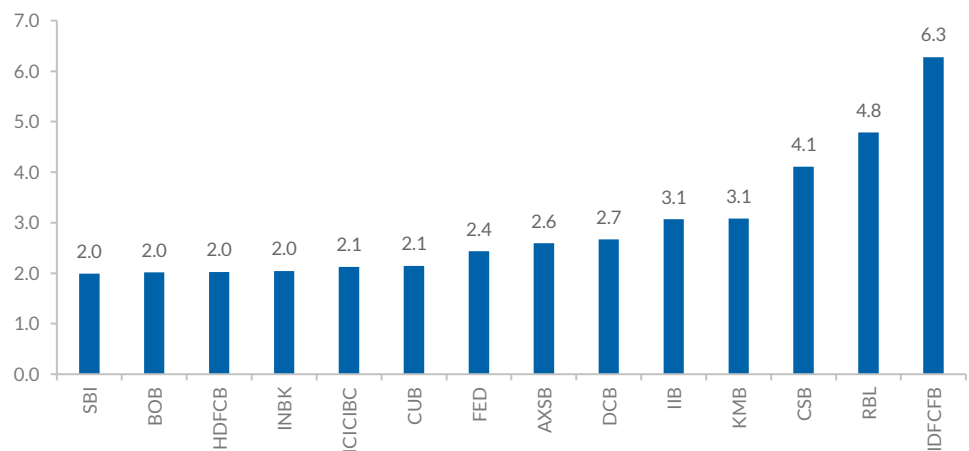
Operating Expense Aspects

Opex to assets is elevated for IDFCB, RBL, CSB, KMB, IIB and DCB given the nature of their business models

The opex to assets for IDFCB, RBL, CSB, KMB and IIB is 6.3%, 4.8%, 4.1%, 3.1% and 3.1% respectively and is the highest in our coverage universe.

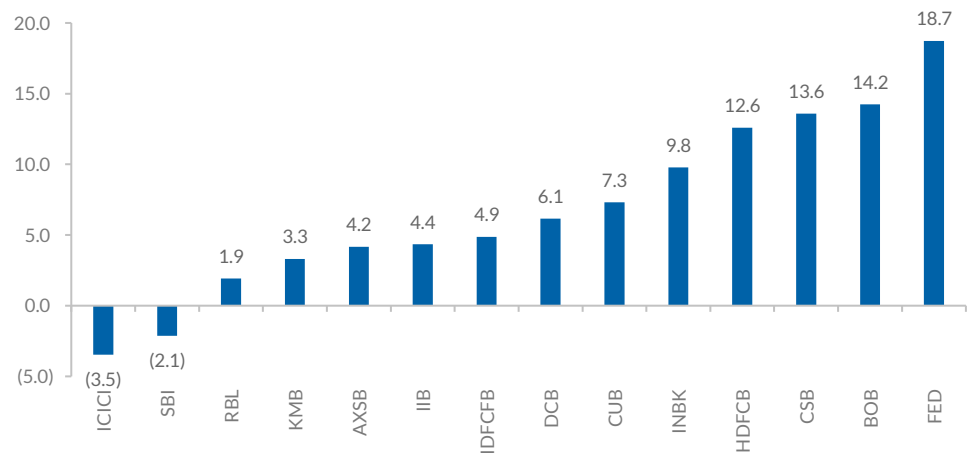
AXSB's opex to assets is somewhat elevated at 2.6% since the bank is utilising the good times to make transformational investments for the future rather than just for incremental change. Despite these investments, the RoE of the bank is close to 20%.

Exhibit 41: Opex to Average Total Assets – Absolute level - 4QFY24 - %



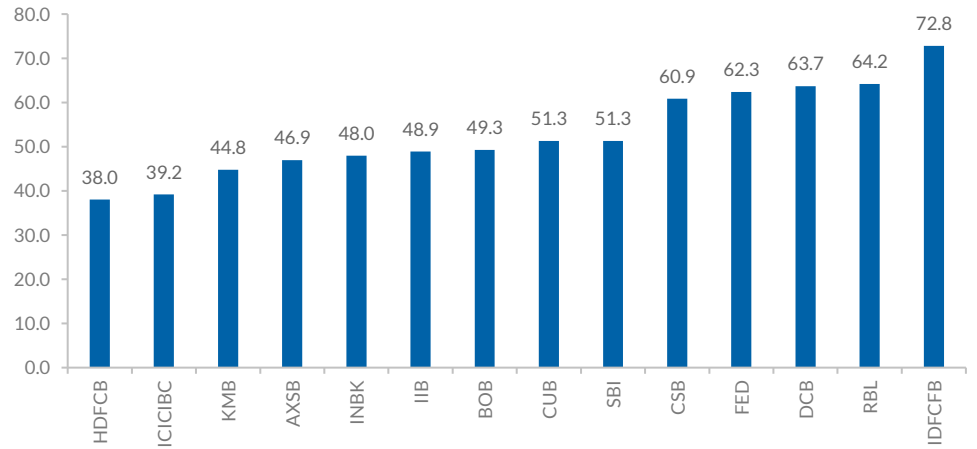
Source: Companies, YES Sec

Exhibit 42: Sequential Opex Growth – 4QFY24 over 3QFY24 - %



Source: Companies, YES Sec

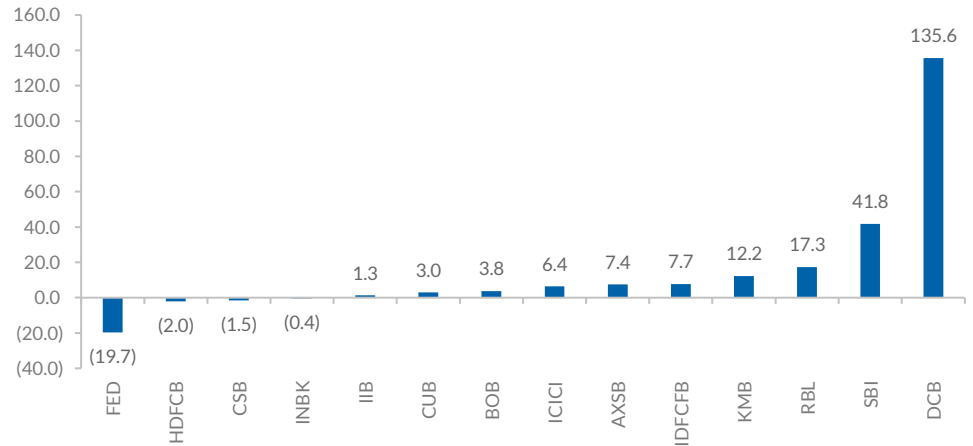
Exhibit 43: Cost to Income Ratio - Absolute level - 4QFY24 - %



Source: Companies, YES Sec

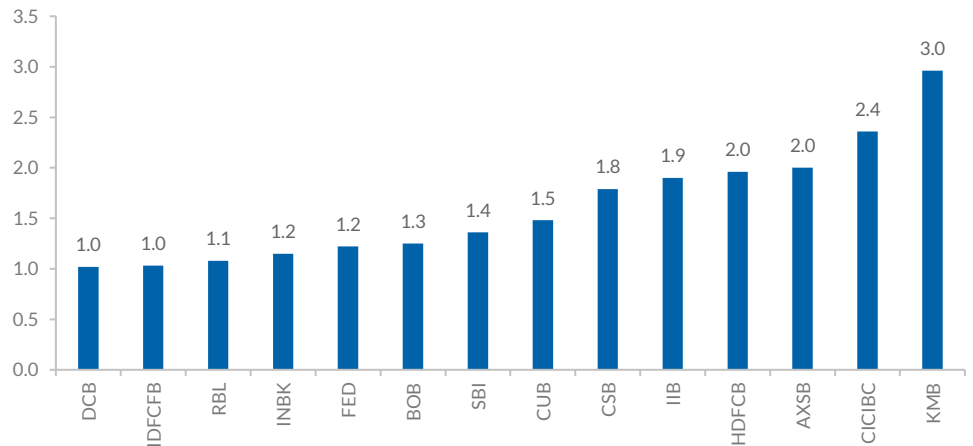
Profitability Aspects

Exhibit 44: Sequential Core PPOP Growth – 4QFY24 over 3QFY24 - %



Source: Companies, YES Sec

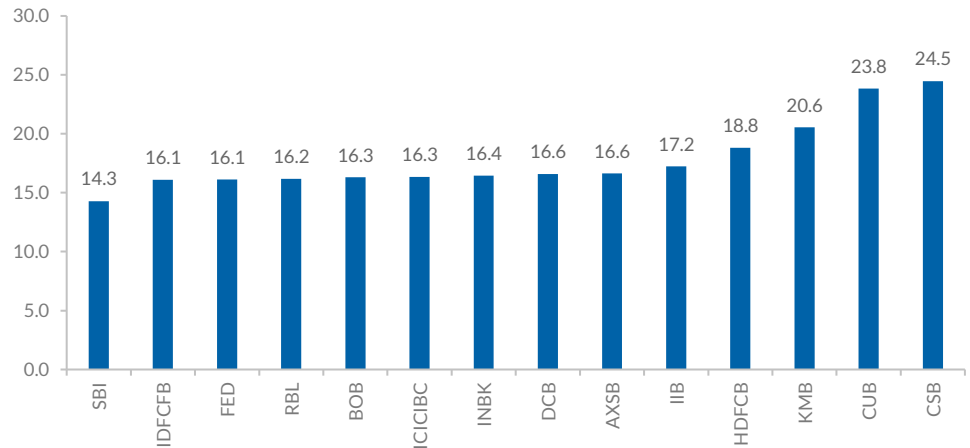
Exhibit 45: Annualised Return on Assets – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

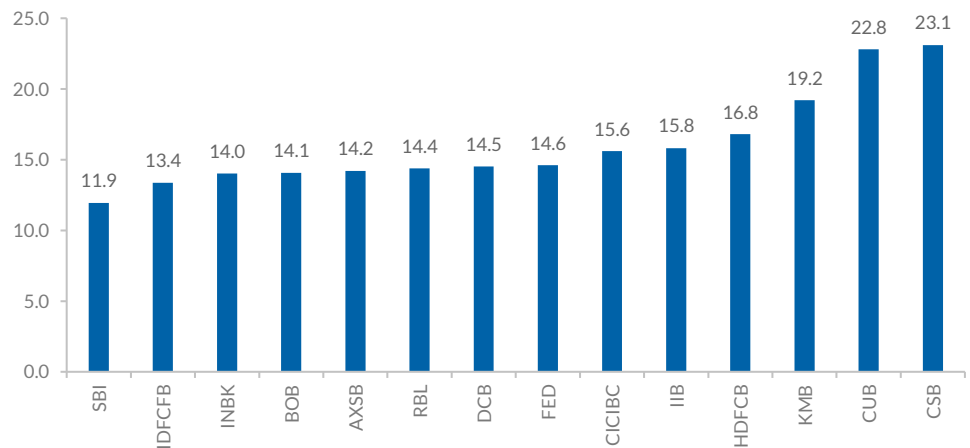
Capital Adequacy

Exhibit 46: Capital Adequacy Ratio (excl. profit) – Absolute level - 4QFY24 - %



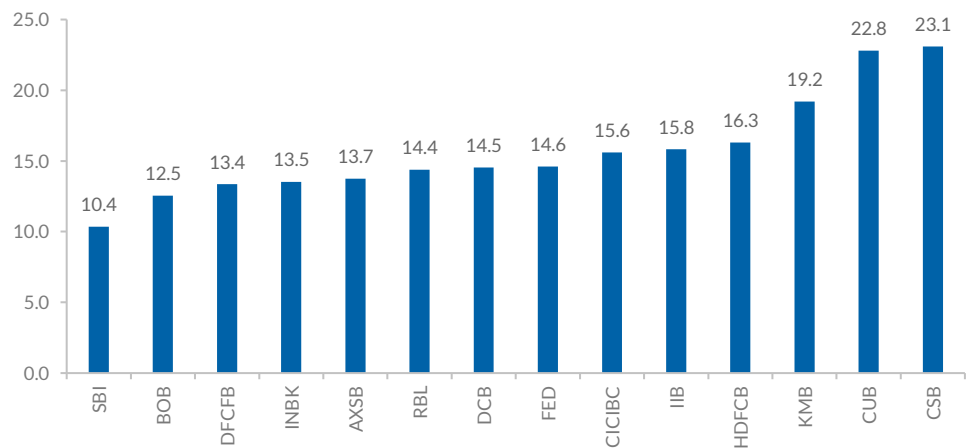
Source: Companies, YES Sec

Exhibit 47: Tier I Capital Ratio (excl. profit) – Absolute level - 4QFY24 - %



Source: Companies, YES Sec

Exhibit 48: CET 1 Capital Ratio (excl. profit) – Absolute level - 4QFY24 - %



Source: Companies, YES Sec; CET1 = Common equity tier 1

Valuation table for Coverage banks

Exhibit 49: Valuation Table (Coverage Banks – in the order of investment preference)

Bank	Rating	CMP	TP	Upside	EPS (Rs)			P/E (x)		
					FY24	FY25E	FY26E	FY24	FY25E	FY26E
Bank of Baroda	BUY	265	350	32	34.4	37.0	43.3	7.2	6.7	5.7
Federal Bank	BUY	162	210	30	15.3	18.0	21.6	9.7	8.2	6.8
Axis Bank	BUY	1162	1475	27	80.5	88.6	107.1	12.8	11.6	9.6
Indian Bank	BUY	568	715	26	59.9	70.8	83.0	9.5	8.0	6.8
State Bank of India	BUY	830	1025	23	68.4	73.9	88.0	8.4	7.8	6.5
ICICI Bank	BUY	1121	1375	23	58.2	66.4	73.4	15.8	13.8	12.5
City Union Bank	BUY	143	175	22	13.7	13.8	15.5	10.4	10.4	9.3
CSB Bank	BUY	330	400	21	32.7	35.3	42.0	10.1	9.3	7.9
HDFC Bank	BUY	1532	1850	21	80.0	89.7	110.5	16.4	14.7	11.9
Kotak M. Bank	ADD	1680	2000	19	69.3	68.9	81.4	14.8	14.9	12.6
Indusind Bank	ADD	1462	1735	19	115.0	127.7	150.4	12.7	11.4	9.7
IDFC First Bank	ADD	76	90	18	4.2	5.4	7.5	18.3	14.0	10.2
RBL Bank	ADD	246	290	18	19.3	25.0	32.6	12.8	9.9	7.5
DCB Bank	ADD	128	150	17	17.1	20.2	24.5	7.5	6.3	5.2

Bank	BVPS (Rs)			P/ BV (x)			ROE (%)			ROA (%)		
	FY24	FY25E	FY26E	FY24	FY25E	FY26E	FY24	FY25E	FY26E	FY24	FY25E	FY26E
Bank of Baroda	217	248	283	1.1	1.0	0.9	16.9	16.3	16.3	1.2	1.2	1.2
Federal Bank	119	136	157	1.2	1.1	0.9	14.7	14.1	14.8	1.3	1.3	1.3
Axis Bank	489	608	714	2.1	1.7	1.4	18.0	16.4	16.2	1.8	1.8	1.9
Indian Bank	433	490	557	1.3	1.2	1.0	15.2	15.3	15.9	1.1	1.1	1.2
State Bank of India	423	499	573	1.4	1.2	1.0	17.3	16.4	16.4	1.0	1.1	1.1
ICICI Bank	339	396	459	2.7	2.3	2.0	18.6	18.1	17.2	2.4	2.3	2.3
City Union Bank	113	126	141	1.3	1.1	1.0	12.8	11.5	11.6	1.5	1.4	1.4
CSB Bank	219	254	296	1.5	1.3	1.1	16.2	14.9	15.2	1.7	1.6	1.6
HDFC Bank	580	652	741	2.3	2.0	1.8	15.6	14.6	15.9	1.9	1.7	1.9
Kotak M. Bank	487	555	635	2.1	1.8	1.6	15.3	13.2	13.7	2.5	2.1	2.1
Indusind Bank	807	918	1,052	1.8	1.6	1.4	15.2	14.8	15.3	1.8	1.8	1.7
IDFC First Bank	45	50	56	1.7	1.5	1.4	10.2	11.4	14.1	1.1	1.2	1.3
RBL Bank	245	277	305	1.0	0.9	0.8	8.2	9.6	11.2	0.9	1.0	1.1
DCB Bank	162	180	203	0.8	0.7	0.6	11.1	11.8	12.8	0.9	0.9	0.9

Source: Companies, YES Sec – Research; Valuations are the implied valuations of standalone entity net of subsidiaries

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