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BANKING | Q1FY21 Preview | 13 July 2020

Navigating uncertain waters

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We believe the true picture of banks' asset quality in Q1FY21 will be masked by the loan moratorium as this will rein in slippages. Credit costs are likely to stay elevated as banks build further contingent buffers to protect their balance sheets from Covid-19 downside risks. Considering the sluggish economic activity, we expect subdued loan growth for most of our coverage (ex-HDFCB), in the range of 4-12% YoY. NIMs are projected to decline 8-10bps on average despite deposit rate cuts, given the pressure on yields and increased risk aversion among banks.

Moratorium to keep slippages in check: In our view, slippages will remain muted in Q1 as stressed accounts continue to benefit from extension of the moratorium till August-end coupled with the absence of major account downgrades. The moratorium will remain the key area of discussion as the share of loans under its phase-2 extension (Jun-Aug) is likely to be lower than phase-1 (Mar-May). Stress recognition will begin once this relief measure ends but we believe credit costs will stay high due to improving provision coverage and building of contingency buffers against Covid-19.

Subdued loan growth trends: Overall loan growth trends are likely to remain muted for most banks under coverage, in the range of 4-12% YoY, due to the lockdown. Latest data on systemic credit released by RBI suggests growth remains sluggish at 6%. Proforma business updates point to softer loan growth by Federal Bank (8% YoY) and IndusInd Bank (4% YoY). However, HDFC Bank continues to exhibit strong growth at 21%.

NIMs likely to decline marginally: A sharp reduction in deposit rates, including savings rate, coupled with lower interest reversals is likely to cushion NIMs. But a bulk of the banking sector's loan portfolio is still linked to MCLR where both large/mid-sized private banks and public banks have cut rates by 15-90bps since Jan'20. Moreover, most banks have turned risk-averse to protect their balance sheets, dampening growth in high-yielding unsecured loans, which could drive down margins by an average of 8-10bps in Q1.

Treasury income could cushion earnings to some extent: State Bank of India and ICICI Bank should get a boost from gains on stake sales in their subsidiaries. G-sec yields have declined by ~25bps QoQ in Q1FY21 which should also help banks post strong treasury gains.

RECOMMENDATION SNAPSHOT

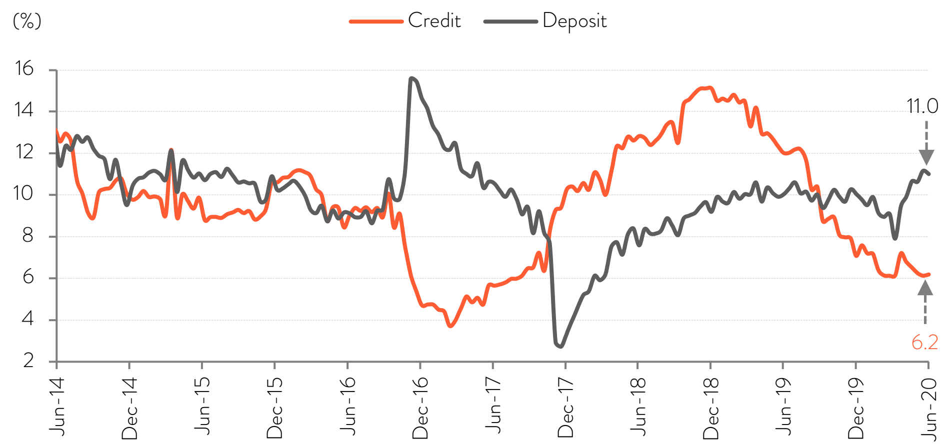
Ticker	Rating
AXSB IN	BUY
CBK IN	ADD
DCBB IN	SELL
FB IN	ADD
HDFCB IN	BUY
ICICIBC IN	BUY
IDFCFB IN	ADD
IIB IN	BUY
KMB IN	BUY
RBK IN	ADD
SBIN IN	ADD

FIG 1 – BOBCAPS BANKING UNIVERSE: Q1FY21 ESTIMATES

Particulars (Rs mn)	Q1FY21E	Q1FY20	Q4FY20	YoY (%)	QoQ (%)	Comments
Axis Bank						
Net interest income	67,116	58,437	68,077	14.9	(1.4)	Loan growth is expected to be ~12% YoY. We estimate lower slippages at ~2% of loans as the moratorium continues to be in force. PCR is expected to improve during the quarter.
Pre-provisioning profit	57,761	58,928	58,511	(2.0)	(1.3)	
Profit after tax	10,026	13,701	(13,878)	(26.8)	(172.2)	
DCB Bank						
Net interest income	3,193	3,048	3,237	4.8	(1.4)	NII growth is likely to be soft given muted loan growth and marginal decline in NIM. Loans under moratorium are forecast to decline. Asset quality in the mortgage and CV book will be key monitorables.
Pre-provisioning profit	1,888	1,665	2,121	13.3	(11.0)	
Profit after tax	820	811	688	1.1	19.2	
Federal Bank						
Net interest income	12,366	11,542	12,160	7.1	1.7	Expect 7% YoY growth in NII backed by 8% loan growth and largely stable margins. Share of loans under moratorium is likely to decline.
Pre-provisioning profit	8,003	7,828	9,593	2.2	(16.6)	
Profit after tax	3,225	3,842	3,012	(16.1)	7.1	
HDFC Bank						
Net interest income	155,127	132,943	152,041	16.7	2.0	Market share gains continue and loan growth trends remain robust. Margins are likely to remain stable. Commentary on asset quality should revolve around share of loans under moratorium and contingent provisions built by the bank.
Pre-provisioning profit	127,011	111,472	129,588	13.9	(2.0)	
Profit after tax	64,923	55,682	69,277	16.6	(6.3)	
ICICI Bank						
Net interest income	87,882	77,374	89,269	13.6	(1.6)	Expect loan growth to slow down to 7-8% YoY but steady NIM should drive ~14% YoY growth in NII. PPoP would be driven by gains of ~Rs 16bn from stake sale in life and general insurance.
Pre-provisioning profit	96,962	62,885	73,901	54.2	31.2	
Profit after tax	30,294	19,080	12,214	58.8	148.0	
IDFC First Bank						
Net interest income	15,568	11,745	15,635	32.6	(0.4)	Restructuring of the balance sheet continues with a focus on reducing share of wholesale loans and increasing retail loan share, thus driving strong NII growth estimates. Expect robust traction on retail deposits.
Pre-provisioning profit	5,331	3,177	5,198	67.8	2.6	
Profit after tax	1,101	(6,174)	715	NM	53.9	
IndusInd Bank						
Net interest income	32,056	28,440	32,312	12.7	(0.8)	Loan as well as deposit growth has come off materially. Performance of the CV/MFI portfolio and discussions around the moratorium will be keenly watched. Expect the bank to make Covid-related contingent provisions.
Pre-provisioning profit	26,800	25,910	28,362	3.4	(5.5)	
Profit after tax	3,785	14,325	3,018	(73.6)	25.4	
Kotak Bank						
Net interest income	37,179	31,730	35,597	17.2	4.4	Loan growth is forecast to remain subdued but solid margins driven by lower cost of funds should lead to healthy NII growth. We don't expect material slip-up in asset quality.
Pre-provisioning profit	28,280	23,989	27,253	17.9	3.8	
Profit after tax	14,910	13,602	12,666	9.6	17.7	
RBL Bank						
Net interest income	10,221	8,173	10,210	25.1	0.1	Loan growth should slow down while asset quality could deteriorate marginally. Credit card and MFI portfolios under moratorium will be keenly watched.
Pre-provisioning profit	7,488	6,188	7,648	21.0	(2.1)	
Profit after tax	1,533	2,671	1,144	(42.6)	34.0	
State Bank of India						
Net interest income	237,864	229,388	227,669	3.7	4.5	We forecast weak loan growth at 5-6% YoY while NIM moderates marginally despite the cut in deposit rates. One-time gain from stake sale in SBI Life Insurance will boost non-interest income. Slippages should remain in check given the moratorium.
Pre-provisioning profit	137,437	132,462	184,651	3.8	(25.6)	
Profit after tax	37,579	23,122	35,808	62.5	4.9	
Canara Bank						
Net interest income	52,048	32,406	33,185	60.6	56.8	The bank will report merged financials with Syndicate Bank and hence previous numbers are not comparable. Asset quality will be keenly watched as slippages remain elevated.
Pre-provisioning profit	33,589	24,400	20,409	37.7	64.6	
Profit after tax	(5,598)	3,291	(32,592)	(270.1)	(82.8)	

Source: BOBCAPS Research

FIG 2 – SYSTEMIC CREDIT GROWTH REMAINS SUBDUED



Source: RBI, BOBCAPS Research

FIG 3 – MCLR OF BANKS DOWN BY UP TO 90BPS SINCE JAN'20

Banks	1-year MCLR (%)						Change (bps)
	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jun-20 over Jan-20
AXSB	8.15	8.15	8.10	7.95	7.80	7.75	(40)
HDFCB	8.15	8.15	8.15	7.95	7.95	7.65	(50)
ICICIBC	8.20	8.20	8.15	8.00	7.75	7.70	(50)
IIB	9.30	9.30	9.25	9.25	9.25	9.15	(15)
KMB	8.40	8.35	8.35	8.10	7.90	7.75	(65)
CBK	8.35	8.20	8.20	7.85	7.85	7.65	(70)
SBIN	7.90	7.85	7.75	7.40	7.25	7.00	(90)
RBK	9.55	9.55	9.45	9.35	9.35	9.35	(20)
IDFCBFB	9.30	9.30	9.35	9.35	9.35	9.20	(10)
FB	8.90	8.90	8.80	8.60	8.41	8.40	(50)
DCBB	10.31	10.22	10.22	10.15	10.15	10.08	(23)

Source: RBI, BOBCAPS Research

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BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

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Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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