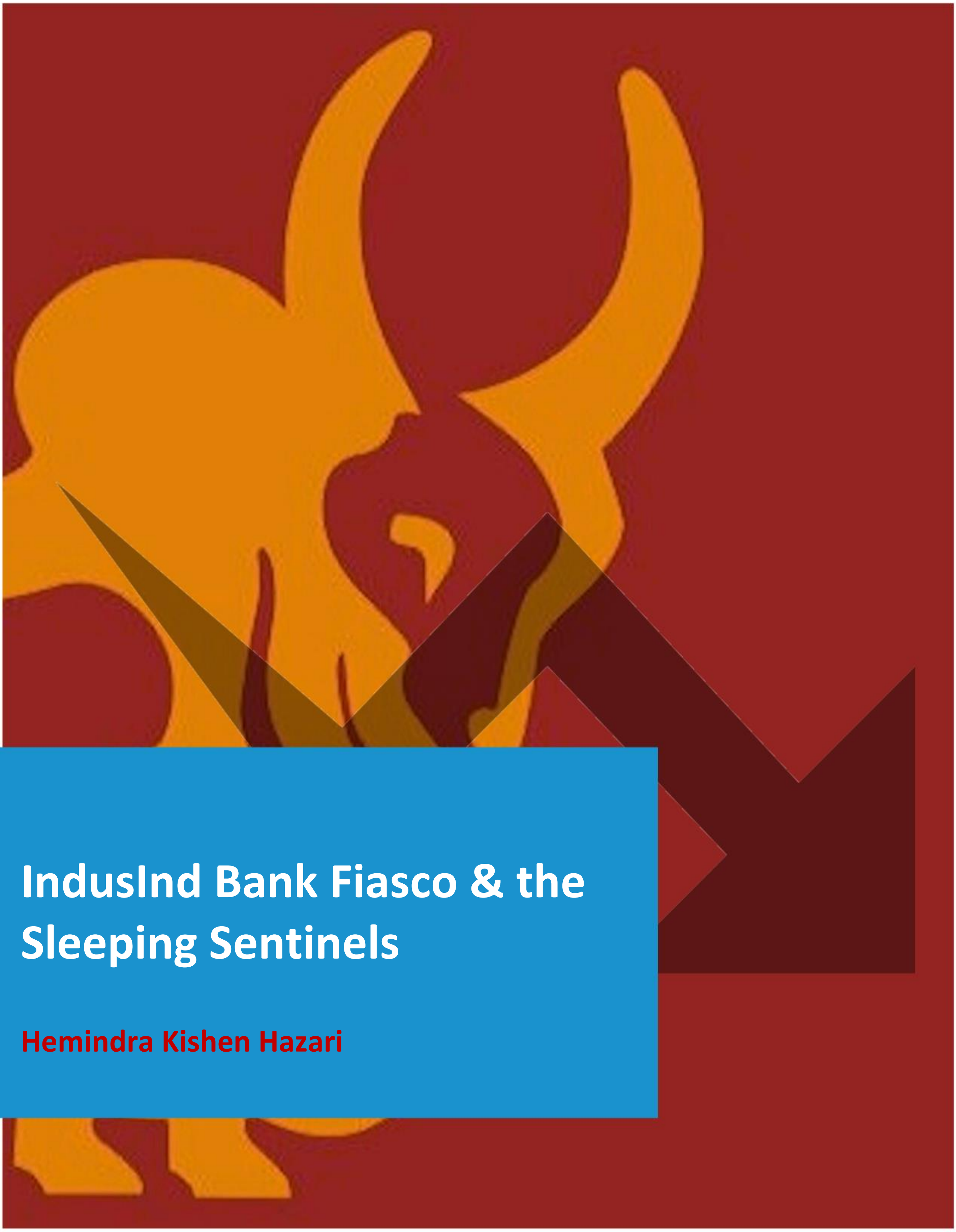

IndusInd Bank Fiasco & the Sleeping Sentinels

Hemindra Kishen Hazari

HKH
hemindrahazari.com

Hemindra Kishen Hazari

is a Securities & Exchange Board of India (SEBI) registered research analyst with over 25 years’ experience in the Indian capital markets. He has specialized in research on banking and the macro-economy. He has managerial experience of establishing profitable equities business, and leading and mentoring analysts. He has worked with prominent global and domestic capital market firms and in the course of his career he has interacted with Indian companies and institutional investors, foreign and Indian .

He is known for his non-consensus views on the market and on stocks. He not only critically evaluates corporate governance in companies, but also examines the entire ecosystem comprising of audit firms, regulators, sell-side and credit rating analysts and the business media.

As an independent analyst, he was one of the first to caution about the impending asset quality and corporate governance problems in Indian private sector banks, and his critical analysis on the performance of some CEOs finally led to the banking regulator refusing an extension to their tenures.

Early in his career he was fortunate to have been mentored by the late N L Hingorani in corporate financial analysis and business strategy. He is also grateful to the Research Unit for Political Economy (RUPE) for their inputs.

An alumnus of Cathedral & John Connon School, St. Xavier’s College, Mumbai & the University of South Carolina, Columbia, his academic background is rooted in the Humanities.

IndusInd Fiasco Should Not Surprise Us. The Three Year Silence Should Appal Us

The recent spectacular collapse in the share price of one-time market favourite IndusInd Bank no doubt reflects poorly on its board of directors and former chief executive officer, Romesh Sobti, who retired on March 23, 2020. But it is also a scathing censure of the entire ecosystem which is meant to provide the public and the investors early warnings of the real state of affairs. Far from ringing the alarm bells, the business media, led by *Financial Express* and the *Business Standard*, were busy crowning Romesh Sobti, "Banker of the Year" in early 2019. Meanwhile, sell-side analysts continued to remain bullish on the bank right through its descent to an 8-year low. Apparently, the twin lures of corporate advertising and corporate access ("exclusive" interviews, non-deal roadshows, participation in broker conferences and meeting sell-side's institutional clients) were more important and lucrative than attending to the work of principled journalism and capital market research. And finally, the regulator restricted itself to light-touch regulation.

Indices Performance Vs Indusind Bank

%	1 week	1 mth	3 mth	6 mth	1 yr	2 yr	5 yr
NIFTY-50	4.6	-26	-28.7	-25.3	-24.7	-14.7	3.8
NIFTY Bank	-2.3	-35.3	-38.7	-34.6	-34.4	-19.1	10.7
Indusind Bank	**22.3**	**-63.2**	**-73.0**	**-72.2**	**-77.2**	**-77.0**	**-53.3**

Indices and Indusind Bank's share price performance is as on March 27, 2020
Source: Moneycontrol

As a Securities and Exchange Board of India (SEBI) registered independent analyst, I commenced publishing a series of critical articles on IndusInd Bank from April 25, 2017. In these articles, I consistently cautioned my institutional clients and readers regarding the high-risk strategy of IndusInd Bank, its dubious accounting, the sheer incompetence of its credit and risk departments, and the lack of accountability of its senior management led by Romesh Sobti. All these issues were in the public domain and could have been easily examined by experienced banking reporters and the specialised sell-side banking analysts that regularly cover IndusInd Bank. Sadly, I remained a voice in the wilderness exposing the bank, while others continued to harp on what a great investment opportunity the bank presented under its dynamic leadership.

Sell-Side Coverage of IndusInd Bank

Date	BUY	HOLD	SELL	Total	Price	12 Mth Price Target	Potential Return
					Rs	Rs	%
28 April 2017	43	6	2	51	1,445	1,566	8.4
15 October 2018	41	10	0	51	1,627	2,022	24.3
23 May 2019	42	10	0	52	1,599	1,874	17.2
15 October 2019	41	11	1	53	1,257	1,614	28.4
20 March 2020	40	13	4	53	440	1,605	264.8

Source: Bloomberg

There is something fundamentally wrong in the capital market when a prominent private sector bank, majority-owned by institutional investors, mainly foreign, makes such a rapid share price descent even as an army of business reporters and dedicated sell side analysts continue to remain optimistic regarding the bank.

The free market is said to have self-correcting mechanisms, with multiple sentinels constantly monitoring the situation. But what the Yes Bank failure and the IndusInd Bank fiasco suggest is that there are strong incentives for the watchers on the wall to take a nap. Their job security and prosperity are best guaranteed by remaining on intimate terms with those they are meant to be monitoring; in less kind language, doing corporate public relations. Such is the reality of the present capital market.

Indusind Bank 8-Year Share Price History

Source: Moneycontrol

This ebook documents all my research notes published on IndusInd Bank since April 25, 2017, tracing the origins of this bank's descent. Since my research was carried out solely on the basis of information in the public domain, any banking journalist or research analyst could also have done it. Hopefully, it may encourage some of them to show the mirror, warts and all, to those preened and pampered bankers who play with depositors' money with little accountability.

Hemindra Kishen Hazari
March 29, 2020. Mumbai.

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IndusInd Bank - Is the One-Off Exposure a Reflection of Its Risk Management?

Tuesday, April 25, 2017.

IndusInd Bank's quarter ended March 31, 2017 (4QFY2017) was impacted by a "one-off" exposure to a company whose cement operations is in the process of being acquired by a top-rated company. While sell-side analysts regard it as a blip in the secular positive outlook on the bank, they are failing to appreciate that such a transaction is a reflection on the bank's corporate credit underwriting and risk management. The obsession to report higher fees to command premium stock market valuation may be compelling banks to undertake such transactions which prudent banks may not consider. IndusInd Bank's premium valuation currently reflects its superior asset quality and earnings growth but in the light of this disclosure, investors may need to reexamine the bank's risk appetite.

IndusInd Bank, one of the darlings of the stock market reported its fourth-quarter results for the period ended March 31, 2017 (4QFY2017) on April 19, 2017. Although the bank reported a 21.2% yoy growth in net profits to Rs7.52bn, loan provisions shot up by 101% yoy on account of a

> "one-off provision of Rs 122 crores [Rs1.22bn] against a large corporate account classified as 'Standard Advance' pursuant to specific RBI [Reserve Bank of India] advice in this regard. The Bank's exposure which is due for repayment in June 2017 relates to a bridge loan for a Merger & Acquisition transaction in cement industry."

Media reports identified the corporate exposure as Jaiprakash Associates' (a stressed account in the banking industry) cement assets which were being sold to UltraTech Cement. IndusInd Bank and Jaiprakash Associates have till date not refuted these media stories. It appears that IndusInd Bank, (possibly with other banks) provided a bridge loan to Jaiprakash Associates to meet some claims of creditors who otherwise would not have agreed to the sale of the company's cement assets to UltraTech and IndusInd Bank claims that post the deal, the bank's bridge loan will have priority in the settlement.

Many prominent brokerage reports were dismissive of this one-off charge which the bank could absorb in the 4QFY2017 and they reiterated their "Buy" recommendation and raised the target price on IndusInd Bank.

Nomura, in its report dated April 19, 2017 said,

> "Asset quality – **a tad weaker** [bold ours]: (1) INR1.2bn of provisions taken on standard loans which will be reversed in 1QFY18 – related to a short-term financing opportunity; ...Maintain Buy and increase PT to INR 1,640 (3.5x FY19 BV) from Rs 1,400."

While *Kotak Institutional Equities* in its report of April 20, 2017 stated,

> "**Slight blip** [bold ours] due to high provisions. Gross NPL (0.9%) and net NPL (0.4%) ratios were stable qoq. However, provisioning cost was higher in the quarter at ~140 bps after including the Rs 1.2 bn standard asset provision against a bridge loan to fund M&A transaction in the cement sector. Maintain ADD. TP at Rs1,500 (from Rs1,400)."

While sell side banking analysts regard IndusInd Bank's bridge loan exposure to Jaiprakash Associates as a "slight blip" unworthy of deeper analysis, it provides an insight into the credit underwriting culture and corporate credit risk management at the bank.

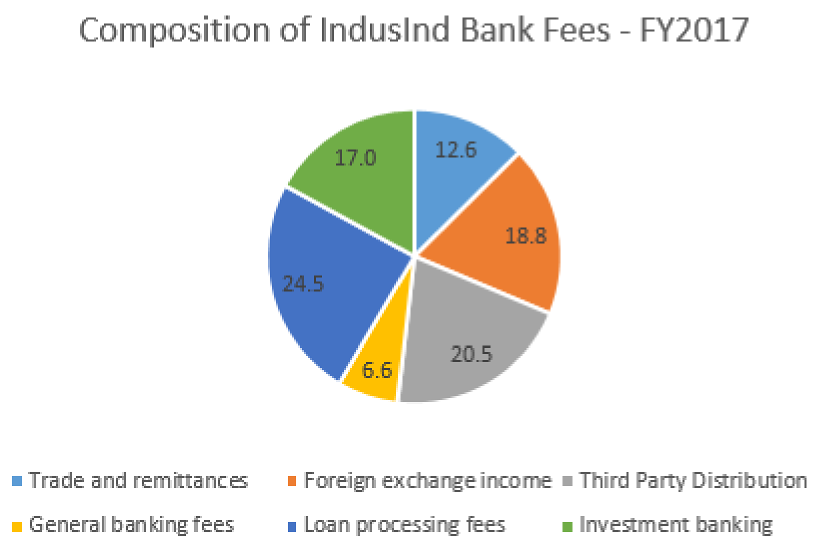
Jaiprakash Associates has a long history of financial overreach. CARE, a domestic credit rating agency, as on December 30 and 31, 2016, rated Jayprakash Associates short and long-term rating as 'D" (default). The credit rating and the history of this company did not prevent IndusInd Bank from providing a bridge loan to clear some of the company's creditor dues so as to facilitate the acquisition by UltraTech Cement. To settle select creditors' dues to permit the acquisition to be finalised, the existing consortium of bankers could have extended further funds or the banks could have financed 'AAA' rated and low-risk Ultratech Cement and it could have extended finance to Jayprakash Associates. As Jayprakash Associates was rated as default and had also defaulted on fixed deposits to the public what was the compulsion for IndusInd Bank to participate in such a transaction which finally resulted in the banking regulator to compel the bank to provide for it?

IndusInd Bank Fee Income

Rsmn	FY2016	FY2017	Growth
Trade and remittances	3,230	4,389	35.9%
Foreign exchange income	6,393	6,559	2.6%
Third Party Distribution	4,906	7,147	45.7%
General banking fees	1,849	2,316	25.3%
Loan processing fees	**6,626**	**8,542**	**28.9%**
Investment banking	**4,721**	**5,940**	**25.8%**
Total	27,725	34,893	25.9%

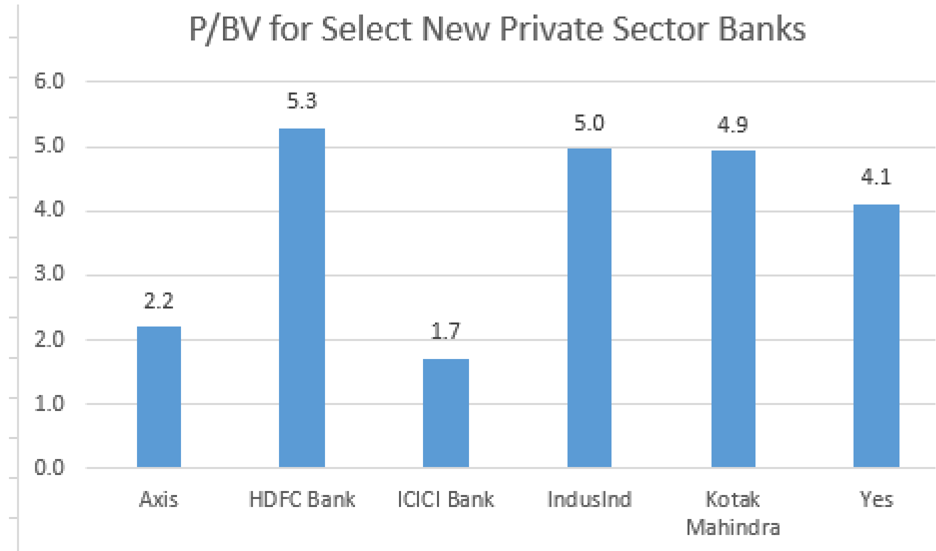
Source: IndusInd Bank

New private sector banks have an insatiable appetite for fee income as the capital market gives a premium valuation to banks which report high fee income on the mistaken belief that fees have less risk. Senior bank officials' remuneration, promotion and stock options are also determined by the quantum of fees generated by them. When banks finance high-risk transactions they do so by charging a premium interest rate, significant fees and demanding more collateral. However, in the case of a company like Jaiprakash Associates, it is unlikely that the company would have been able to provide any collateral to IndusInd Bank as its numerous existing bankers would have already secured all the company's assets. Hence IndusInd Bank for this transaction would have in all likelihood charged huge fees and a higher interest rate to compensate for the lack of collateral.



Source: IndusInd Bank

For the last 7 years, IndusInd Bank has been aggressively growing its fees from corporate business and analysts and the stock market rewarded the bank with a premium valuation as it was considered low-risk. **The Jaiprakash Associates transaction and the banking regulator compelling the bank to provide for it is an indicator that the bank may be taking on higher risk than is warranted for its superior valuation.**



Source: Moneycontrol

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What No One Likes to Mention about Indusind Bank

Monday, December 18, 2017.

Retail-focused new private sector banks, the darlings of the capital market, are facing the ire of the banking regulator. Nearly two months after the Reserve Bank of India (RBI) compelled HDFC Bank to classify a large account as non-performing, thus qualifying the blue-blooded bank for 'divergence' (from RBI findings), comes news that the regulator has fined Indusind Bank for misreporting its results and contravention of regulatory restrictions pertaining to non-fund based facilities for the year ended March 31, 2016. Although Indusind Bank in its latest annual report disclosed significant RBI NPA divergence, the business media and sell-side research conveniently ignored the disclosure, as they are overwhelmingly bullish on the bank. The misreporting of accounts and the penalty by the RBI, though, reflects poorly on the bank and its senior management and should be a warning signal for investors. On December 18, 2017, Indusind Bank will be included in the prestigious Bombay Stock Exchange Sensex index of 30 companies, it is ironic that such a historic event is preceded by a penalty for its accounts not depicting a true and fair view.

On December 13, 2017, in a surprising development, the RBI, the banking regulator penalised Indusind Bank, Rs 30 mn (US$ 0.5 mn)

> "for non-compliance with the directions issued by RBI on Income Recognition and Asset Classification (IRAC) norms and contravention of regulatory restrictions pertaining to non-fund based (NFB) facilities."

On April 18, 2017, a RBI notification instructed banks to disclose the divergence in their reported NPAs as detected by the regulator for the year ended March 31, 2016, in a prescribed format if it exceeded a certain threshold. A day later, when Indusind Bank declared its 4QFY2017/FY2017 results, an analyst asked Romesh Sobti, Chief Executive Officer (CEO), Indusind Bank whether the bank would report RBI divergence. To which Sobti replied,

> "All banks will disclose, we will also disclose. There is no skipping that…It should not be a large number."

Nearly a month later, when the bank's annual report for the year ended March 31, 2017 (FY2017) was released, it disclosed that the bank's gross NPAs divergence for FY2016 was an alarming 72%, far exceeding the RBI's threshold limit of 15%; its net NPAs, as determined by the RBI, were nearly twice its reported and audited number. And, in contrast to Sobti's statement that the divergence was universal, prominent banks like the State Bank of India (SBI), HDFC Bank, Bank of Baroda, Bank of India, Union Bank of India and Kotak Mahindra Bank did not report RBI divergence for FY2016.

Indusind Bank - Misreporting of Results for the Year Ended March 31, 2016

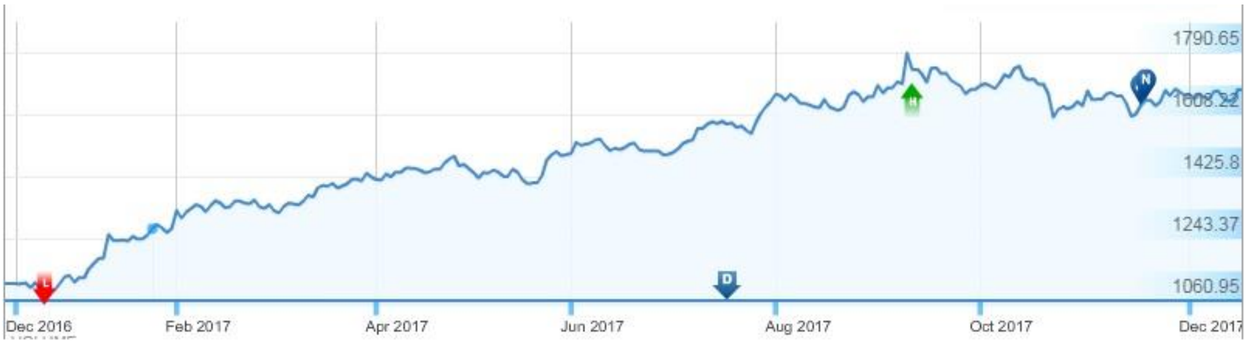
Rsmn	
Gross NPAs Reported	7,768
Gross NPAs as assessed by RBI	13,370
Divergence in Gross NPA	**5,602**
Net NPAs Reported	3,218
Net NPAs as assessed by RBI	6,376
Divergence in Net NPAs	**3,158**
Provisions for NPAs	4,551
Provisions for NPAs as assessed by RBI	6,995
Divergence in Provisions	2,444
Reported Net Profits	22,865
Net Profits as assessed by RBI	21,373
Divergence in Net Profits	-1,492
Divergence (%)	
Gross NPA	**72.1**
Net NPA	**98.1**
Provisions	53.7
Net Profits	-6.5

Source: Indusind Bank

In a note to the disclosure, the bank stated that of the gross NPA divergence of Rs 5.6 bn, Rs 3.56 bn was repaid as of March 31, 2017. Such an explanation is irrelevant as the accounts as on FY2016 were misleading. The entire amount should have been classified as NPA, and when the amount was recovered it could have been reclassified as standard in FY2017. Furthermore, the RBI threshold for reporting divergence at 15% is liberal, as Indian asset classification is rule-based and hence a bank should have marginal difference at best between its reported NPAs and the assessment by the regulator.

Despite the disclosure being present in Indusind Bank's annual report, sell-side analysts and the media strangely chose not to highlight this critical development. Such an omission was indeed perplexing, as there were no concerns regarding the bank's asset quality, and the bank was trading at a price to book value multiple of nearly 5x; hence such a development should have been immediately highlighted, as it was price sensitive information.

Indusind Bank One year Share price History



Source: Moneycontrol

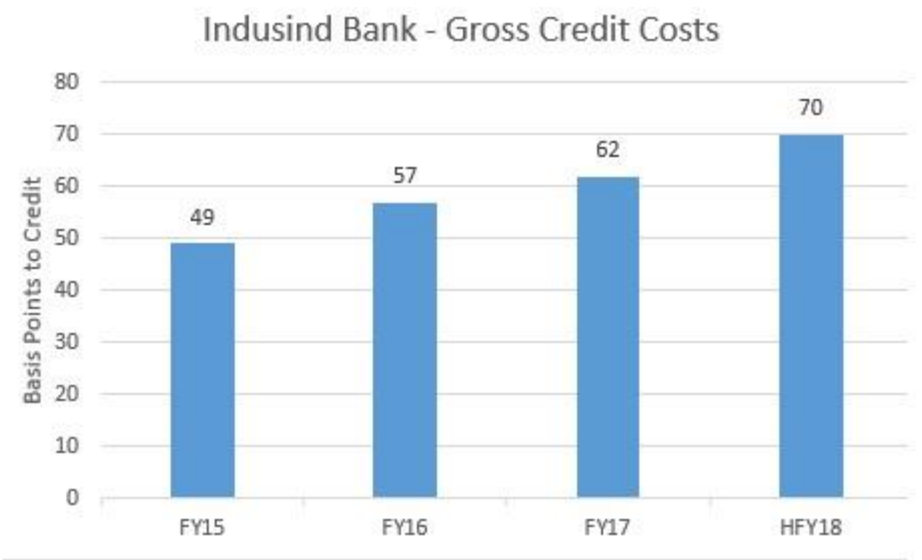
The only explanation for the omission by the sell-side to broadcast Indusind Bank's misreporting of its FY2016 results is that the consensus view was bullish on the bank – in end-April 2017, according to Bloomberg, 52 analysts covered the bank and 87% had a "Buy" recommendation. Typically, when the consensus view is bullish and the share price is also rising, sell-side analysts are reluctant to highlight any negative analysis on a stock which is a market favourite, as such companies are prize candidates for corporate access for brokerages. In internal appraisals of sell-side research, corporate access has significant weightage, as analysts arrange meetings with the companies they cover for institutional clients, apart from inviting them for conferences and non-deal roadshows. In such a compromised environment, published research eschews critical analysis of prominent companies. Critical commentary on companies, if at all undertaken by the sell-side is disbursed through non-public communication; whispers, emails, phone calls and one-to-one meetings. The public standing of most sell-side research is to be non-controversial on their coverage and be flag bearers of the companies they cover.

It is also no surprise that even after the RBI imposed a penalty on Indusind Bank for misreporting its FY2016 results, sell-side research has chosen to ignore the development by not publishing any updates and analysis of the regulator's displeasure. When the gross NPA divergence exceeds 15% of the reported amount and the regulator imposes a penalty, it is a serious offence, as there exists a high possibility of the bank evergreening its bad loans and its entire reported asset quality lacking credibility, and hence sell-side research and the business media should extensively cover the development and further investigate the bank. But even two days after the penalty, this writer is unable to find any sell-side analysis nor any further investigative reporting by the media on this development.

The RBI penalty of Rs 30 mn was imposed on Indusind Bank for two issues: NPA divergence and contravention of regulatory restrictions pertaining to non-fund based (NFB) facilities. In many cases, regulatory action on banks' NFB facilities pertains to evergreening of loans as banks replace fund-based poor quality loans with guarantees and letters of credit thereby classifying the asset as standard. Replying to a questionnaire, sent by this writer, Indusind Bank said,

> "the second count relates to a 'procedural aspect' of non fund business which has nothing to do with asset quality issues of such non fund customer."

Hence it is possible that the regulator fined the bank for not taking permission from the consortium of bankers when it provided corporate(s) with NFB facilities. Such practices are widespread. However, earlier RBI cautioned banks, but did not penalize them when such instances were detected.



HFY18 is annualized.
Source: Indusind Bank

Despite Indusind Bank's low gross NPA of 1.08% and 26% yoy growth in net profits for the half year ended September 30, 2017 (1HFY2018), annualized gross credit costs have increased. And it is not a healthy sign for a bank to report divergence and be penalised by the statutory regulator for mis-reporting of its accounts. Such an issue casts poor light on the bank's CEO, audit committee and the auditor, and even though, thankfully, the divergence was not repeated in FY2017, investors need to be vigilant regarding Indusind Bank. On December 18, 2017, Indusind Bank will be included in the prestigious Bombay Stock Exchange Sensex index of 30 companies. It is ironic that such a historic event is preceded by a penalty for its accounts not depicting a true and fair view.

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Indusind Bank - Who Cares about 'Divergence'?

Friday, April 20, 2018.

In a stunning blow to the credibility of Indusind Bank, its board of directors, Romesh Sobti, chief executive officer and Russell I Parera, auditor and partner, Price Waterhouse, the bank reported that it had mis-reported its accounts for the year ended March 31, 2017. This was its second consecutive year of mis-reporting. The regulatory strategy of naming and shaming a bank by disclosing the difference between the regulator's assessment and the bank's view of its non-performing assets is clearly ineffective. It is shameful for any bank to mis-report accounts for a single year; for a bank to report two successive years of fudged accounts without any accountability for its CEO and the auditor speaks volumes on the quality of corporate governance. The regulator also does not seem to mind that banks are merrily reporting 'divergence' for successive years under the same key managerial individuals and auditors and they are able to retain their posts to continue with such a performance. Such malpractices renders meaningless any analysis of reported numbers. This is especially shocking for a bank which trades at 5.4x P/BV. It should also be shocking, but unfortunately is on expected lines, that analysts remain silent and are unwilling to aggressively hold management accountable, on fears of losing corporate access on a market favourite bank. For reporting two consecutive years of untrustworthy accounts, Indusind Bank joins the Hall of Shame and is in the company of Axis and Yes Bank.

The main event of the bank's 4QFY2018 results reported on April 18, 2018 was not that the bank was able to meet consensus estimates, but that it reported a second successive year of misreported accounts. More worryingly, the divergence, in absolute and percentage terms, was higher than in the previous year, indicating that the problems in regulatory compliance are only getting worse at the bank.

‘Divergence’ Reported by Indusind Bank

Rsmn	FY2016	FY2017	Increase (%)
Gross NPAs Reported	7,768	10,549	35.8
Gross NPAs as assessed by RBI	13,370	24,051	79.9
Divergence in Gross NPA	**5,602**	**13,502**	**141.0**
Net NPAs Reported	3,218	4,389	36.4
Net NPAs as assessed by RBI	6,376	14,400	125.8
Divergence in Net NPAs	**3,158**	**10,011**	**217.0**
Provisions for NPAs	4,551	6,160	35.3
Provisions for NPAs as assessed by RBI	6,995	9,651	38.0
Divergence in Provisions	**2,444**	**3,491**	**42.9**
Reported Net Profits	22,865	28,679	25.4
Net Profits as assessed by RBI	21,373	26,396	23.5
Divergence in Net Profits	**-1,492**	**-2,283**	**53.0**
Divergence (%)			
Gross NPA	**72.1**	**128.0**	
Net NPA	**98.1**	**228.1**	
Provisions	53.7	56.7	
Net Profits	-6.5	-8.0	

Source: Indusind Bank

The Indusind Bank explanation for the divergence, attempting to highlight that the majority of it was addressed in FY2018, is irrelevant. The recoveries achieved, bad loans fully repaid, NPAs sold to asset reconstruction companies and other banks also classifying the account as ‘standard’ have no meaning, and no weightage must be subscribed to the bank’s defence. Investors must be aware of the factual audited position as on the year end. Subsequent events post the cut-off date are meaningless. Prudent accounting practice indicates the bank should have classified all these assets as NPAs. If and when recoveries or asset sales took place, the proceeds could have been written back. This is the normal practice and one cannot use this justification to explain the serious offense of under-reporting NPAs to boost the bank’s valuation.

The current position as on March 31, 2018 is as under:

	Divergence in NPA	1350.20
	Of Which:	
a)	Large standard cement M&A “bridge loan” provided for as per IRAC norms in March 2017 and fully repaid in June 2017	518.52
b)	Loans fully repaid	257.80
c)	Loans classified as NPA prior to Divergence report and already included in GNPA	236.00
d)	Loan sold to Asset Recontruction Company	118.80
e)	Accounts under divergence upgraded to “Standard”	Nil
f)	Loans written off	33.18
g)	Loans to a toll road project classified as NPA by the Bank, currently being considered by consortium banks as "Standard"	104.20
h)	Balance of divergence recognised as GNPA as of 31 March 2018	81.70
	Total impact on GNPA in Q-IV (items g +h)	**185.90**

Source: Indusind Bank

Indusind Bank's conduct is shocking, as it is a market favourite bank, with considerable institutional and foreign ownership, and at 5.4x P/BV it is expensive by global and Indian standards. The secular growth in its share price and premium valuation leaves no room for such serious regulatory transgressions.

One Year Share Price Performance of Indusind Bank

Source: Moneycontrol

The numerous and experienced sell-side analysts who track the bank have so far remained silent when the bank disclosed in its FY2017 annual report that it had mis-reported FY2016 accounts. Their silence continued when the regulator fined the bank on December 13, 2017 for fudging the books. Even on the analysts' call to report its FY2018 results, the analysts chose to not grill the CEO and the management for this huge regulatory lapse which exposes the entire credibility of the accounts and the valuation in the stock market.

The surge in share price despite such setbacks indicates the market is also oblivious to spurious accounts, management culpability and docile analysts. The regulator's conduct in all this also undermines financial credibility, and more importantly, financial stability, as the reporting of divergence by prominent, market favourite banks has become par for the course. When the regulator merely taps the wrists after the first offence, is it any surprise that the offender repeats the act?

Indusind Bank Results

Rs mn	4QFY2017	3QFY2018	4QFY2018	QoQ (%)	YoY (%)
Net Interest Income	**16,675**	**18,948**	**20,076**	**6.0**	**20.4**
Other Income	12,113	11,868	12,085	1.8	-0.2
Total Income	28,788	30,816	32,161	4.4	11.7
Overheads	-13,065	-14,169	-14,467	2.1	10.7
Operating Profit	**15,723**	**16,647**	**17,694**	**6.3**	**12.5**
Income Tax	-3,905	-4,922	-4,808	-2.3	23.1
Bad Debt Provisions	-4,301	-2,361	-3,356	42.1	-22.0
Total Provisions	-8,206	-7,283	-8,164	12.1	-0.5
Net Profit	**7,517**	**9,364**	**9,530**	**1.8**	**26.8**
Gross NPAs	**10,549**	**14,987**	**17,049**	**13.8**	**61.6**
Net NPAs	4,389	5,922	7,457	25.9	69.9
Gross NPAs (%)	**0.93**	**1.16**	**1.17**	**0.01**	**0.24**
Net NPAs (%)	0.39	0.46	0.51	0.05	0.12

Source: Indusind Bank

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Are IndusInd Bank's Credit and Risk Departments Run by Financial Illiterates?

Wednesday, October 17, 2018.

Indusind Bank, one of the stock market darlings and foreign investor favourites, startled the capital market with a mere 5% rise in net earnings. Earnings rose to Rs 9.2 bn for the quarter ended September 30, 2018 (2QFY2019), as compared with the consensus estimate of Rs 11 bn. This was on account of a charge of Rs 2.75 bn for the fast collapsing IL&FS, an infrastructure developer and financer. What is shocking is that Indusind, a bank which trades at 4.2x P/BV, one of the most expensive multiples in the world, did not disclose its total exposure to the beleaguered leviathan.

More importantly, it had provided a bridge loan of a substantial amount to IL&FS 3 months ago, when a cursory analysis of IL&FS's financials would have revealed it has been insolvent since FY2014. Apparently, a bank which reports unrealistically low non-performing loans, which investors enthusiastically lap up, provides large loans without either analysing the borrower's financials or worse, analyses the accounts without comprehending the basics of financial analysis. Indusind Bank, under the leadership of Romesh Sobti, its CEO is now not only a serial mis-reporter (2 successive years of fudged accounts were detected by the regulator), but is also incapable of rudimentary financial analysis of corporate borrowers. It is time investors challenged whether such a bank deserves such steep valuation multiples.

On October 15, 2018, Indusind Bank shocked the market with a mere 4.5% growth in net profits to Rs 9.2 bn for 2QFY2019 as compared with the consensus estimate of Rs 11 bn. This is a far cry from the 25% yoy growth that it had been consistently reporting in the past. The consistency of its high growth in earnings and its pristine asset quality (gross NPAs around 1%) led to a premium P/B multiple of 4-5x. Investors and sell-side analysts also chose to ignore that the regulator had found that for 2 years in a row, FY2016 and FY2017, under the leadership of Romesh Sobti, the CEO, Indusind had been caught fudging its books. The unexpected charge of Rs 2.75 bn for its undisclosed exposure on IL&FS should be a wake-up call on how the bank lends public money.

Not only can Indusind Bank's accounts not be trusted (although the bank claimed in its results conference call that for FY2018 the regulator may give it a clean sheet), but it appears it is incapable of analysing a large borrower's accounts. Just as it wants the public to have blind faith in its own accounts, it appears to extend the same faith when it lends public money to its borrowers based entirely on an external credit rating agencies ratings of the borrower.

IDFC Securities, an Indian broker, in their results report on Indusind Bank dated October 15, 2018 stated,

> "We believe IIB [Indusind Bank] has an exposure of Rs24bn to IL&FS though management did not quantify. The exposure is broadly to two entities 1) ChenaniNashri Tunnel 2) IL&FS parent. Mgmt believes that there will be no haircuts on the first because the project is rated AAA (SO). The second exposure to the parent was taken very recently (3 months ago) and is rated D. This exposure was given as liquidity funding – akin to a bridge loan till IL&FS could complete its rights issue. But after the disbursal, IL&FS was downgraded and the rights issue has been delayed. Management believes that as soon as rights or a liquidity infusion happens, IIB will be repaid… We do not know the break up between the two [ChenaniNashri and IL&FS parent] but we believe a higher amount would have gone to the parent."

Assuming *IDFC Securities*' estimate of Indusind Bank's IL&FS exposure of Rs 24 bn is realistic, it is significant, as it constitutes nearly 10% of the bank's capital and 2.4% of its corporate banking portfolio in 2QFY2019. It appears that a significant increase in the bank's exposure to NBFCs in the non-housing finance category from 4QFY2018 was on account of IL&FS

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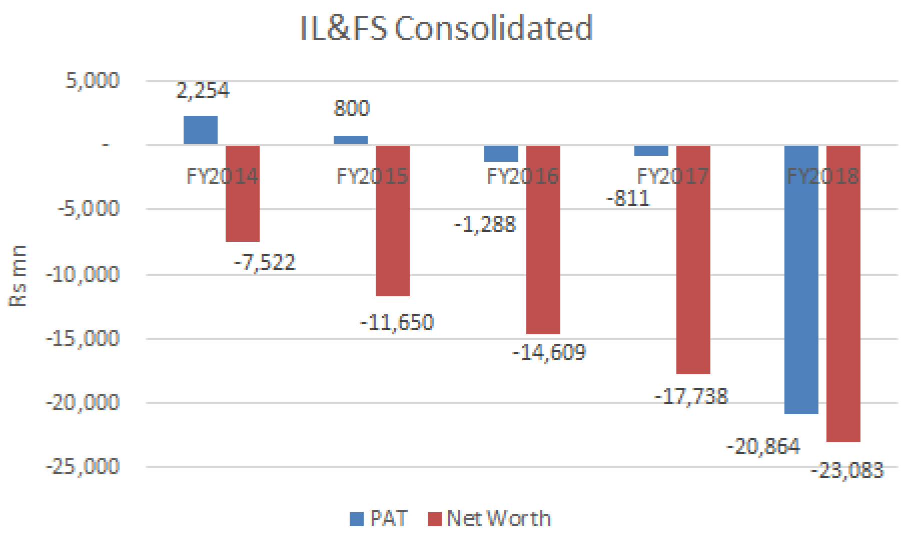
Indusind Bank's NBFC (Non Housing Finance) Exposure

Rsmn	4QFY18	1QFY19	2QFY19	Increase 2Q over 4Q
NBFC (Non-Hsg)				
Fund-based	35,408	49,972	73,687	38,279
Non-Fund Based	12,295	15,212	12,805	510
Total	47,703	65,184	86,492	38,789

Source: Indusind Bank

What is fascinating and very revealing is that on the results call, not a single analyst asked on what basis the bank had lent such a significant amount to a large non-bank finance company (NBFC). The IL&FS group had started defaulting on its dues in June 2018 and the first reports became public in early September. It is possible that the bank may have disbursed the IL&FS loan prior to these reports but it is inexcusable for the bank to have not analysed IL&FS's publicly available financial accounts and only relied on the naïve credit rating agencies investment rating (here and here) on the company prior to giving the bridge loan.



Source: IL&FS

A cursory analysis of the consolidated accounts of IL&FS which is available on its website would have revealed that the company was not only loss-making but that it was insolvent (according to regulatory guidelines, intangibles have to be reduced from equity capital) since FY2014 i.e. for the last 5 years. When Indusind Bank lent the funds around June 2018, IL&FS's FY2018 accounts were not released, but the losses and its insolvency is clearly revealed from FY2014 till FY2017. It therefore appears that it lent a significant amount based entirely on the rating agencies rating or that the bank's credit and risk departments are incapable of basic financial analysis.

If Indusind Bank had lent knowing that IL&FS was insolvent, it would have taken adequate liquid security, which clearly is not the case, as it has provided Rs 2.75 bn on an account which is currently standard. This entire episode reflects extremely poorly on Indusind Bank, its CEO, its board of directors and in particular its credit and risk management departments.

While it is true that other banks/NBFCs and mutual funds also exclusively relied on the woefully incompetent credit rating agencies' rating of IL&FS without doing an independent analysis of IL&FS's consolidated accounts, it is inexcusable for a bank which trades at 4-5x P/BV and reports around 1% gross NPAs to lend funds in such a negligent manner.

Indusind Bank Underperforms Indices since August 2018

	02-Aug-18	16-Oct-18	Change (%)
Indusind (Rs)	2,023	1,621	-19.9
NIFTY-50	11,245	10,585	-5.9
Bank NIFTY	27,356	25,590	-6.5

Source: Moneycontrol

Investors in Indusind Bank received the first warning that all was not well with the leadership of Romesh Sobti when the bank disclosed that for two successive years, FY2016 and FY2017 the regulator had detected that the bank's accounts were untrustworthy and had even fined the bank. Since August 2, 2018, Indusind Bank has severely under-performed the market. Now we know that the bank is incapable of undertaking basic financial analysis of companies and prefers to rely exclusively on credit rating agencies whose misdeeds were totally exposed in the sub-prime bubble. With its present antics revealed to all and sundry, investors in Indusind Bank should question the foundation of this glitzy bank, the darling of sell-side analysts. It may already be late in the day.

Indusind Bank 2 Year Share Price History

Source: Moneycontrol

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Memo to Indusind Bank CEO: Read RBI Circulars

Friday, October 26, 2018.

Romesh Sobti, CEO, Indusind Bank, is a veteran banker with 43 years' experience. He recently went on record to defend the bank's substantial bridge loan to the fast-collapsing IL&FS, a systemically important non-deposit-taking core investment company. Sadly, he found this writer's earlier insight on Indusind to be "nasty" and "ill-informed". In doing so, he publicly broadcast the state of his knowledge on critical areas of financial accounting and regulatory stipulations for computing solvency. If his views are shared by the important credit and risk management departments of the bank, shareholders should be concerned, as the bank trades at an expensive 3.8x P/BV. But further, the regulator should wake up and take notice.

Sonia Shenoy, senior editor, CNBCTV18, on October, 23, 2018, asked Romesh Sobti, CEO Indusind Bank the following question:

> On what basis did the bank lend to IL&FS, at the time when the lending was done were you aware that the company was loss-making and insolvent? I am just trying to understand whether the risk department [of Indusind Bank] had cleared it at the time?

Romesh Sobti, CEO, Indusind Bank replied,

> Yes, somebody has written a nasty article on that. I think the ill-informed article saying that the company was insolvent. You just have to look at the balance sheet, somebody has to read balance sheets properly and understand when they talk about intangible for a holding company like IL&FS and what it means – these annuity flows and receivable had come from the SPVs [Special Purpose Vehicles]. If you look at the balance sheet of IL&FS, it was never insolvent. If it was insolvent, how is it that rating agency giving AAA for the last five years?

That "somebody" was yours truly and the "nasty …ill-informed article" is the insight that this writer had authored on October 17, 2018.

This writer sent a questionnaire to Indusind Bank after Romesh Sobti's interview with CNBCTV18. In it he inquired what estimate Indusind Bank's credit and risk management department had made for IL&FS's equity, and what Reserve Bank of India (RBI) notifications the bank could cite to defend Sobti's views on intangible assets and IL&FS's solvency in the interview.

Indusind Bank's head of investor relations responded and said,

> "Please do your regulatory analysis as that should be in the public domain and maybe so also should be the company's auditor position too."

In an earlier article published in the media, on September 30, 2018, this writer had explained and provided the detailed workings of the calculation of IL&FS's net worth and specifically stated,

> "In IL&FS the bulk of the intangible assets are rights under SCA which the annual report states,
> "Under Service Concession Arrangement (SCA), where a Special Purpose Vehicle (SPV) has received the right to charge users of a public service, such rights are recognized and classified as "Intangible Assets".

Such a right is an unconditional right to receive consideration; however the amounts are contingent to the extent that the public uses the service." (p. 262 FY2018 annual report).

The value of a right in a tangible asset which is based on annuity flows and receivables from an SPV which are readily quantifiable and arise out of expected cash flows can be materially different from those of an intangible asset for which cash flows are dependent on a number of contingencies. There is hence a distinct and material difference between annuity flows, receivables from a tangible asset and the value of a right to receive consideration in an intangible asset.

Management and auditors test the valuations of intangibles every year and write them down when necessary. The quality of IL&FS's intangibles is evident as in FY2018, the company commenced marking down the intangibles. It booked Rs 2.95 bn as impairment of Service Concession Agreement (SCA), when it sold its entire (50%) stake in the NAM Expressway on August 16, 2018 (post the balance sheet date) for a mere Rs 600 mn to Ramky Infrastructure. This highlighted how over-valued this particular intangible was on its books (see p. 316 FY2018 annual report) .

Regardless of whether auditors have approved the valuation of intangible assets, the Reserve Bank of India's regulations are clear that intangibles have to be written down from equity for the calculation of shareholder funds.

As per RBI's Master Circular on, "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015"

"2. (1) (i) "breakup value" means the equity capital and reserves **as reduced by intangible assets** [bold ours] and revaluation reserves, divided by the number of equity shares of the investee company;
2. (1) (xx) "owned fund" means paid up equity capital, preference shares which are compulsorily convertible into equity, free reserves, balance in share premium account and capital reserves representing surplus arising out of sale proceeds of asset, excluding reserves created by revaluation of asset, **as reduced by accumulated loss balance, book value of intangible assets** [bold ours] and deferred revenue expenditure, if any;

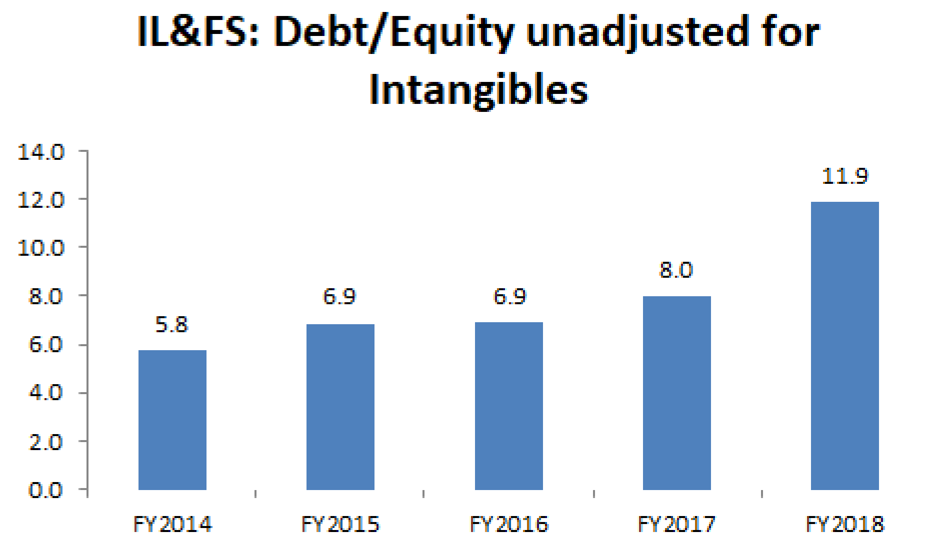
IL&FS Consolidated Net Worth

Rs mn	FY2014	FY2015	FY2016	FY2017	FY2018
Equity	1,181	1,284	1,284	1,284	1,284
Reported Reserves	57,272	59,343	62,595	65,417	44,448
Revaluation Reserves	0	0	0	-5,661	-5,529
Deferred Tax Asset	0	-1,755	-3,427	-3,830	-3,522
Minority Interests	27,236	34,029	42,168	43,883	39,032
Intangible asset	-63,076	-98,079	-148,835	-180,540	-200,041
Intangibles under development	-85,063	-93,451	-81,698	-80,367	-88,813
Goodwill	-12,773	-17,870	-18,176	-17,567	-17,687
Net Worth	**-75,223**	**-116,498**	**-146,090**	**-177,381**	**-230,828**

Source: IL&FS

Reducing for intangibles in the calculation of IL&FS's net worth clearly reveals that the company has had a negative net worth since FY2014 and it has kept deteriorating since then.

Another ratio to determine financial health is debt-equity. As per Para 12 of the RBI Master Circular, "Regulatory Framework for Core Investment Companies (CICs)" the debt equity of a company like IL&FS should not exceed 2.5 times. Even a liberal, unrealistic scenario of equity inclusive of preference debt, and not adjusting for intangibles, reveals that IL&FS's consolidated debt-equity significantly exceeded 2.5 from FY2014.



Source: IL&FS

It is very apparent that Indusind, in evaluating the creditworthiness of IL&FS, did not do any analysis based on RBI's guidelines to determine the solvency of IL&FS; or that the bank's critical credit and risk management departments are financially illiterate. In all likelihood, Indusind Bank gave a substantial bridge loan to IL&FS (estimated at around 10% of its own capital) based entirely on the incompetent credit rating agencies' 'AAA' rating, and on the false assumption that the rights issue would be successful. Indusind may have also succumbed to the attractive upfront fees and high coupon on the loan it charged IL&FS, although the bank has declined to disclose these details.

Interestingly, T.T. Ram Mohan, (Professor, Finance and Economics at Indian Institute of Management, Ahmedabad) an independent director, Indusind Bank and columnist at *Business Standard*, in his article on IL&FS dated October 25, 2018 stated,

> "With the public shareholders not subscribing to the rights issue, the prospects of a bailout [of IL&FS] appear to be fading. The decision to not subscribe makes sense. What shareholder would want more exposure to a company whose very solvency is in doubt?"

There appears to be a difference of opinion between the CEO of Indusind Bank's view of the solvency of IL&FS and that of his own board member; or the solvency in IL&FS markedly deteriorated in the short span between Indusind Bank disbursing the bridge loan and the present moment.

From Romesh Sobti's public utterances it appears he is unable to distinguish between valuation of rights to charge users of a public service, which is an intangible asset, and annuities and receivables from tangible assets. He and the bank also appear ill-informed on the regulator's mandatory regulations on determining solvency for non-bank finance companies and systemically important non-deposit taking core investment companies. The fact the credit and risk management department of Indusind Bank could have approved such a large loan to IL&FS, and worse, that the CEO should continue to publicly defend it, hardly casts a good light on a bank which trades at 3.8x P/BV.

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Is IL&FS the Only Cockroach in Indusind Bank's Portfolio?

Friday, November 2, 2018.

Post the public disclosure of bank borrowings by the board of IL&FS, where the scale of Indusind Bank's unsecured exposure to the insolvent parent company became apparent, the bank finally disclosed its total exposure to the beleaguered leviathan in the late hours of October 31. In the analysts call arranged by the bank the following day to discuss this disclosure, nobody in the senior management of the bank was held to account for 8% of the bank's capital going up in smoke. (Nor did the servile sell-side analysts demand such accountability.) The absence of basic financial analysis by the bank for providing the Rs 20 bn bridge loan may well be an example of how Indusind Bank evaluates large ticket loans. Investors should be concerned about how many such loans have been liberally handed out to book lucrative fees upfront. The stock market, though, rewarded the bank for its disclosure, and the stock closed 2.8% up in a flat market.

The new IL&FS board appointed by the Indian government publicly released a progress report and a possible future strategy for IL&FS which was filed with the stock exchanges at 17:22 (IST) on October 31, 2018. In the report, IL&FS's debt by type of lender and by secured and unsecured was revealed as of October 8, 2018.

Type of Security (whether secured or unsecured)	Entity Level in IL&FS Structure where borrowing is availed	Category of Creditor and exposure to outstanding fund based facilities (as of October 8, 2018) (in INR Mn)										Total (in INR Mn)
		Nationalised Banks	NCDs	Other Banks	Financial Institutions	Foreign Banks	Commercial Paper	NBFC	Corporates	State Govt.	Others	
Secured		**343,264**	**192,467**	**60,252**	**77,790**	**39,227**		**10,812**	**528**		**9,247**	**733,586**
	IL&FS (as the ultimate parent company)	14,550	95,186	8,750	6,046	1,000						125,532
	At the level of the key holding companies (below IL&FS) or a lower level holding co	87,709	23,910	29,093	7,600	16,676		2,421	130		8,719	176,257
	Operating Level	241,005	73,371	22,409	64,144	21,552		8,391	397		528	431,797
Unsecured		**10,556**	**65,204**	**34,110**	**13,587**	**21,080**	**30,283**	**6,264**	**10,498**	**6,020**	**10,970**	**208,570**
	IL&FS (as the ultimate parent company)		69	20,000	8,137	2,600	19,323		4,865			54,993
	At the level of the key holding companies (below IL&FS) or a lower level holding co	6,489	35,655	3,210		2,425	2,980	653			4,585	56,754
	Operating Level	4,067	29,480	10,900	5,450	16,055	7,980	5,611	5,632	6,020	6,385	96,823
Total		**353,820**	**257,670**	**94,362**	**91,377**	**60,307**	**30,283**	**17,076**	**11,025**	**6,020**	**20,216**	**942,156**

Source: IL&FS p. 18 of Report

Post Indusind Bank's 2QFY2019 results, where analysts estimated the bank's exposure to IL&FS at around Rs 24 bn, the majority of it being an unsecured bridge loan to the parent, it became apparent from the table in the report that the Rs 20 bn unsecured loan given to the parent company in the 'other banks' category was the loan given by Indusind Bank.

During the Indusind Bank's results call, the bank had refused to disclose its total exposure to the IL&FS group, and had maintained its silence even during media interviews post its results. In contrast, L&T Finance and Yes Bank had disclosed the quantum of their exposure (here and here) to IL&FS.

Once the IL&FS board released its report, Indusind Bank was left with little choice and released its disclosure to the stock exchanges 5 1/2 hours later. The bank stated that it had Rs 20 bn exposure as a bridge loan to the IL&FS parent, Rs 10 bn to the other operating entities of the IL&FS group and an additional Rs 250 mn in non-fund based exposure to the operating entities. Indusind's total exposure to IL&FS is Rs 30.25 bn, 12% of the bank's capital (CET1 Rs 249 bn) as on September 30, 2018. Since IL&FS is an insolvent company (and indeed has been for the past 5 years), the bank will in all likelihood have to write-off its entire exposure to the parent company. The bank's meagre provision of only Rs 2.75 bn in 2QFY2019 is clearly inadequate, and it may have to provide an additional Rs 17.25 bn in 2HFY2019. Even on its exposure to the step down IL&FS operative companies of Rs 10.25 bn, the bank may have to take a haircut. The bank reported 1HFY2019 net profits of Rs 19.56 bn. and just providing for its bridge loan exposure will wipe-out the bulk of its 2HFY2019 net profits.

The stock market took the disclosure in its stride, and Indusind Bank's share price closed nearly 3% up at Rs 1,464 on a day when the market index closed flat. It appears the market had already discounted the bank's exposure to IL&FS. However, there are two critical issues which need to be factored.

First, is the lack of accountability of any individual in the senior management of the bank for putting 12% of the bank's capital at risk. Some may argue that in providing a bridge loan for a rights issue to an 'AAA' rated company which had a board approval from shareholder directors such as LIC and SBI, and had taken all the possible precautions in the form of covenants did not require to do a financial analysis of IL&FS prior to giving the loan, and hence senior management should not be held responsible. The fact remains it is unusual for a 'AAA' rated company to seek a bridge loan prior to a rights issue and the bank should have investigated why such a company urgently required funds. Even a preliminary analysis of the financials would have revealed that IL&FS was loss-making and was insolvent for the last 5 years, as regulatory guidelines mandate the writing down of intangibles from equity. It is apparent that either no such financial analysis was done, or that the bank's credit and risk management are financially illiterate. **It is not surprising that on the analysts call on November 1, not a single question was posed on accountability of the senior management of the bank.**

Secondly, the bank's bridge loan to IL&FS reveals the huge risk appetite of the bank. It was willing to bet around 8% of the bank's capital on a supposedly safe bet, without doing the basic financial analysis of the corporate borrower and being totally reliant on credit rating agencies rating, despite their credibility being totally exposed in the global sub-prime crisis. Investors should now be concerned regarding how the bank gives loans to other companies and what risks are the bank and its risk management department taking. Is IL&FS the only cockroach to crawl out from this market favourite bank (trades at an expensive 3.8x P/BV) or is it the first of many more to come?

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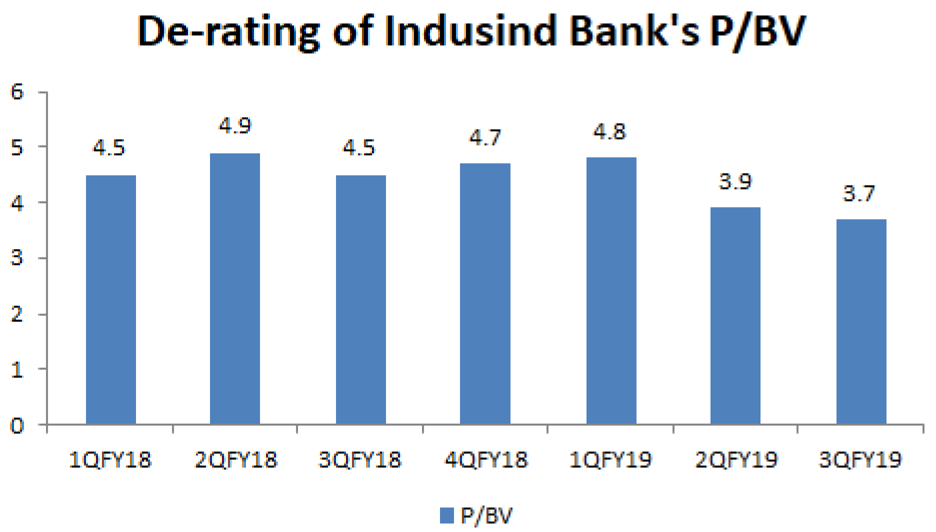
Bleak Future for Indusind Bank

Friday, January 11, 2019.

Indusind Bank's reckless decision to provide a Rs 20 bn (8% of the bank's capital) unsecured bridge loan to IL&FS, an insolvent infrastructure company has led to a significant de-rating of its valuation multiple. In the 3QFY2019 results call, Romesh Sobti, the bank's CEO believes that the bank will eventually need to provide only 40-50% of this exposure and the bank has currently provided only 26.5%. The bank's guidance on this appears to be as optimistic as its initial appraisal when it disbursed the loan, without any apparent scrutiny of the company's financials. Shareholders in the bank need to be more realistic and factor a 100% write-off on the unsecured IL&FS exposure and need to examine all the bank's loans more carefully for similar high-risk lending. The glory days of this once fancied stock are over and a bleak future beckons.



P/BV is on date of announcement of quarterly results
Source: Indusind Bank

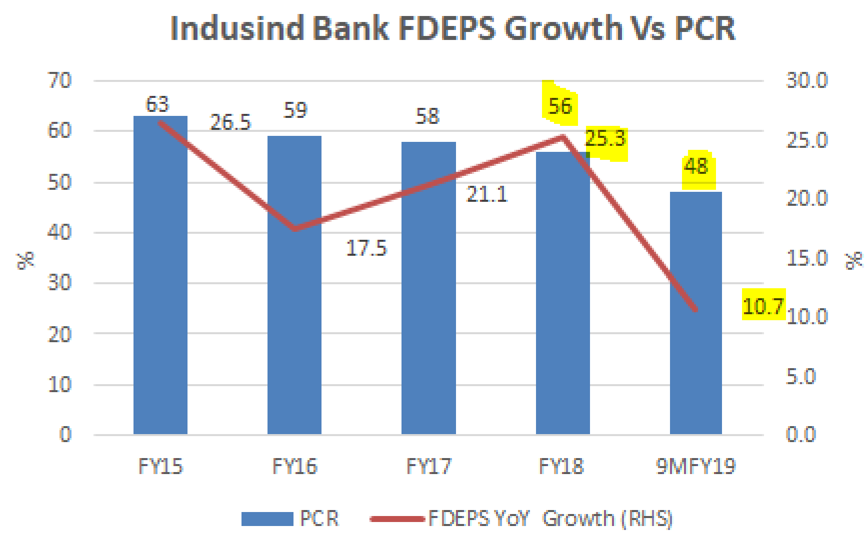
Ever since IL&FS's default became public in early September 2018, Indusind Bank's valuation has been de-rated. The stock used to trade at a P/BV of 4.5-4.9x since 1QFY2018 and it currently trades at 3.7x P/BV. The de-rating has been driven by its significant IL&FS exposure of Rs 30.25 bn (12% of bank's capital) and in particular the Rs 20 bn unsecured bridge loan the bank extended sometime in early FY2019 without any proper due diligence to the infrastructure company. As a result of the bridge loan, Indusind Bank has the dubious distinction of being amongst the top 5 creditors of IL&FS.

11.2. Pursuant to the requirement of the NCLAT order granting the Moratorium, notice has been issued by the NCLAT to appear before it has been issued to the top five creditors of the IL&FS Group, being the State Bank of India, Bank of Baroda, Power Finance Corporation, Bank of India and IndusInd Bank. The Board expects to continue its efforts for continuation of the Moratorium as per the directions of the NCLAT.

Source: IL&FS p. 26

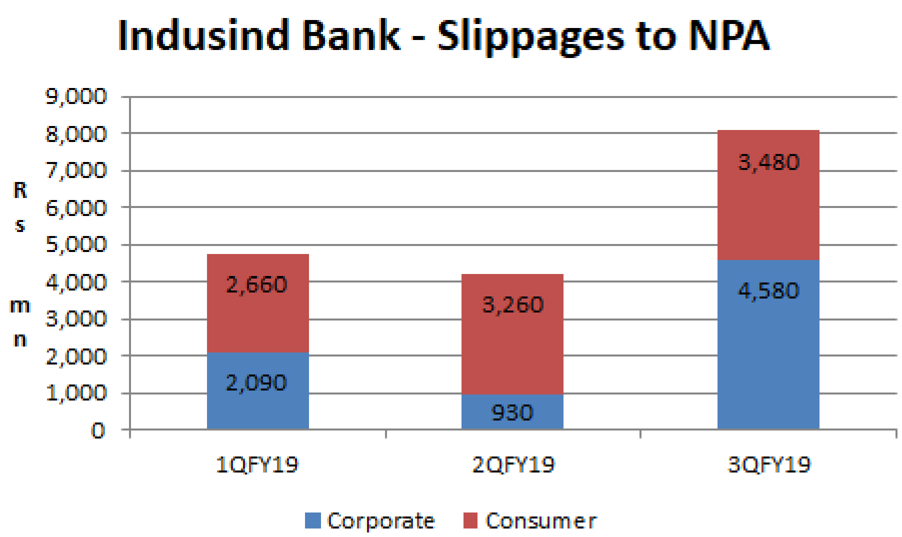
During the 3QFY2019 results call, Romesh Sobti, the bank's CEO informed analysts that by 4QFY2019 the bank "would make enough and more provisions" on the IL&FS bridge loan exposure to "make us more comfortable" and that the bank will provide 40-50% of this exposure. As of 3QFY2019, the bank had provided 27.5% of the

Rs 20 bn bridge loan and nil on the remaining Rs 10.25 bn to the step down subsidiaries of IL&FS. He also said that the entire IL&FS exposure is classified as standard and the bank has been accruing interest on the loans. As per RBI norms, for unsecured infrastructure non-performing assets (NPAs) banks have to provide 20% in the 1st year of the NPA and thereafter 100%. Since IL&FS has had a negative net worth for the last 5 years and Indusind Bank gave the bridge loan around mid-2018, prudence demands that it provides 100% on this loan at the earliest. As per a Reuters news story, citing anonymous sources, the RBI has instructed banks to classify IL&FS as a NPA in 3QFY2019. Indusind Bank shareholders should therefore not only expect significant additional provisions in the 4QFY2019 but also reversal of the interest booked on the entire IL&FS loans.



Source: Indusind Bank

Even excluding its IL&FS exposure, asset quality stress is building up in the bank and it is starkly visible in its declining Provision Coverage Ratio (PCR). Since FY2015 till FY2018 the bank use to report annual FDEPS growth rate of 17.5-26.5% and maintained a PCR between 56-63%. For the 9 month period ended December 31, 2018, the annual FDEPS growth rate dropped to 10.7% and more alarmingly, the PCR had fallen to 48%. Assuming the entire IL&FS exposure was classified as NPA and the contingent provisions of Rs 5.3 bn was classified as bad debt provisions, the PCR in 3QFY2019 would drop to 30%.



Source: Indusind Bank

Even though the bank reported gross NPAs of 1.1%, the corporate slippages (excluding IL&FS) are on the rise as some accounts in the construction sector slipped in the 3QFY2019. However, in a depressed economic environment, the bank reported high annual growth rates in its loans of 39% to Rs 1,051 bn in corporate and 36% to Rs 680 bn in consumer in the 3QFY2019. Such high growth rates in loans may not be a prudent strategy and may result in additional problems in the future.

Indusind Bank's IL&FS bridge loan, low provisions and its high overall loan growth rates indicates the bank has a high risk appetite, the valuation multiple has already been de-rated and a bleak future awaits shareholders.

DISCLOSURE & CERTIFICATION

I, Hemindra Hazari, am a registered Research Analyst with the Securities and Exchange Board of India (Registration No. INH000000594) I have no position in Indusind Bank shares referenced in this note. Views expressed in this note accurately reflect my personal opinion about the referenced securities and issuers and/or other subject matter as appropriate. This note does not contain and is not based on any non-public, material information. To the best of my knowledge, the views expressed in this note comply with Indian law as well as applicable law in the country from which it is posted. I have not been commissioned to write this note or hold any specific opinion on the securities referenced therein. This note is for informational purposes only and is not intended to provide financial, investment or other professional advice. It should not be construed as an offer to sell, a solicitation of an offer to buy, or a recommendation for any security.

Indusind Bank: One More Disturbing Lapse of Judgment by the "Banker of the Year"

Thursday, April 25, 2019.

Romesh Sobti, the CEO of Indusind Bank, was recently crowned 'banker of the year' by a fawning business media, despite reporting two consecutive years of fudged accounts (FY2016 and FY2017) and putting nearly 8% of the bank's capital at risk in an ill-advised, unsecured loan to the insolvent IL&FS. We find that the lauded banker is also grappling with a Rs 5 bn loan to the liquidity-constrained investment company of the founder of the Essel media group (flagship, Zee Entertainment Enterprises). It remains a mystery why Indusind Bank gave such a high-risk loan in end-April 2018 and secured it against an illiquid, optionally convertible security of an unlisted associate company. To date the loan appears to barely retain its 'standard' classification, but the investment companies of the Zee founders have brought considerable grief to the mutual fund industry, exposing their poor credit appraisal and risk management policies. If the Zee founders are unable to divest assets and sell part of their holding in the flagship listed company, Indusind Bank shareholders will share the grief of the investors in debt mutual funds who had subscribed to the ill-fated paper issued by companies of the Zee founders. It is time the banking regulator also closely monitored the credit and risk systems at Indusind Bank. The coveted laurel gracing the head of Indusind Bank's CEO may turn out to be a crown of thorns for stakeholders of the bank, exposing once again the credit appraisal and risk mitigation policies in this bank.

The Indian debt mutual fund industry has been recently mauled on account of its considerable exposure to the investment companies of the founders of the Zee media group. It appears that mutual fund managers were not alone in taking on such high-risk investments. Indusind Bank also has a high-risk appetite. Probably a short time prior to disbursing a huge Rs 20 bn unsecured loan to the insolvent IL&FS, the bank on April 27, 2018 provided a loan of Rs 5 bn in two tranches to Sprit Infrapower and Multiventures Pvt Ltd, an unlisted investment company belonging to the founders of the Zee business media group.

Loans given by Indusind Bank to Sprit Infrapower on April 27, 2018

(j) *Extent and operation of the charge	At the request of the borrower Company i.e Sprit Infrapower & Multiventures Private Limited, the lender Indusind Bank Limited has enhanced a Loan / facility upto Rs. 200.00 Crores against the OCD as security given by the company.
(j) *Extent and operation of the charge	At the request of the borrower Company i.e Sprit Infrapower & Multiventures Private Limited, the lender Indusind Bank Limited has enhanced a Loan / facility upto Rs. 300.00 Crores against the OCD as security given by the company.

Source: Registrar of Companies

Charges Registered to Indusind Bank by Sprit Infrapower

Company / LLP Name: SPRIT INFRAPOWER & MULTIVENTURES PRIVATELIMITED

Charges Registered

SNo	SRN	Charge Id	Charge Holder Name	Date of Creation	Date of Modification	Date of Satisfaction	Amount	Address
1	G87358974	100177457	INDUSIND BANK LTD.	27/04/2018	-	-	2000000000.0	2401 GEN THIMMAYYA ROADCONTONMENTPUNEMa411001IN
2	G87359485	100177459	INDUSIND BANK LTD.	27/04/2018	-	-	3000000000.0	2401 GEN THIMMAYYA ROADCONTONMENTPUNEMa411001IN

Source: Registrar of Companies

The last 4 years' financial performance of Sprit Infrapower does not inspire confidence as the company's interest payments are higher than its total revenue, and the company has reported losses in the entire period. It has a huge debt of Rs 43.2 bn in FY2018 and the company's debt-equity ratio was an alarming 15.5:1. *Brickwork Rating*, the credit rating agency which rated Sprit Infrapower as investment grade for a debt issue in a note dated November 17, 2017 said,

> "However, the rating is constrained by unavailability of assured cash flows of the issuer at redemption, and dependency on the group support, refinance or alternatively liquidation of securities before the redemption due date to meet the obligations arising from the proposed NCD issue."

Financials of Sprit Infrapower

Rs mn	FY2015	FY2016	FY2017	FY2018
Equity	*0.1*	*0.1*	*0.1*	*0.1*
Reserves & Surplus	*-1,491*	*8,000*	*5,367*	*2,777*
Net Worth	**-1,491**	**8,000**	**5,367**	**2,777**
Preference Capital	*1*	*1*	*1*	*1*
Long Term Borrowings	*13,960*	*18,993*	*20,073*	*26,173*
Short Term Borrowings	*16,178*	*16,178*	*14,347*	*16,985*
Total Borrowings	**30,139**	**35,172**	**34,421**	**43,159**
Debt/Equity	**-**	**4.4**	**6.4**	**15.5**
Revenue from Operations	958	9	680	0
Other Income	26	254	244	646
Total Revenue	984	263	924	646
Costs	-958	-393	-925	-19
EBITDA	**26**	**-130**	**-1**	**627**
Interest	**-1,519**	**-2,155**	**-2,632**	**-3,218**
PBT	-1,493	-2,285	-2,633	-2,591
Tax	0	0	0	0
PAT	**-1,493**	**-2,285**	**-2,633**	**-2,591**

Source: Sprit Infrapower

What is further unusual in the loan given to Sprit Infrapower is the quality of the security. As per documents filed in the Registrar of Companies, 50 mn PAN India Network Infravest Ltd. (PANI) 0.1% Optionally Convertible Debentures (OCD) of face value Rs 100 aggregating to Rs 5 bn has been pledged as a security. It appears that the value of the security is same as the value of the loan, and the bank has not maintained the prudential margin normally associated with secured loans. Pertinently, Sprit Infrapower has a 49.9% equity stake in PANI, and it is an unlisted company.

Pledge of Securities to Indusind Bank for the Rs 5 bn Loan to Sprit Infrapower

Business Date: 27-Apr-2018

Pledge Master Report(Pledge Order)
National Securities Depository Limited

Print Date: 27-Apr-2018 12:37 PM

DP:INDUSIND BANK LTD.[IN300159]
DEPOSITORY DPT. PNA HOUSE, PLOT,NO. 57 & 57/1, 4TH FLR, STREET NO.17
MIDC, ANDHERI (EAST), MUMBAI,-400093
Phone: 022-61069200 Fax: 022-66238031

1) Pledge Instr. 2) Pledge Type 3) Unique ID	1) ISIN 2) ISIN Description 3) Execution Date	1) Pledged Quantity 2) Closed Quantity 3) Invoked Quantity	1) Status 2) Rejection Reasons 3) Internal Reference No.	1) Lock-In Release Date 2) Lock-In Reason 3) Closure Date 4) Agreement No.
1) 10000000475011 2) Pledge 3) 10000000475011	1) INE569W08015 2) PAN INDIA NETWORK INFRAVEST LIMITED 0.1 OCD 05FB21 FVRS100 3) 27/04/2018	1) 30,000,000 2) 3)	1) Pledged 2) 3) AW1000009493	1) 2) 3) 07-Jan-2021 4) 32959602
1) 10000000475012 2) Pledge 3) 10000000475012	1) INE569W08023 2) PAN INDIA NETWORK INFRAVEST LIMITED 0.1 OCD 03SP21 FVRS100 3) 27/04/2018	1) 20,000,000 2) 3)	1) Pledged 2) 3) AW1000009493	1) 2) 3) 07-Jan-2021 4) 32959602

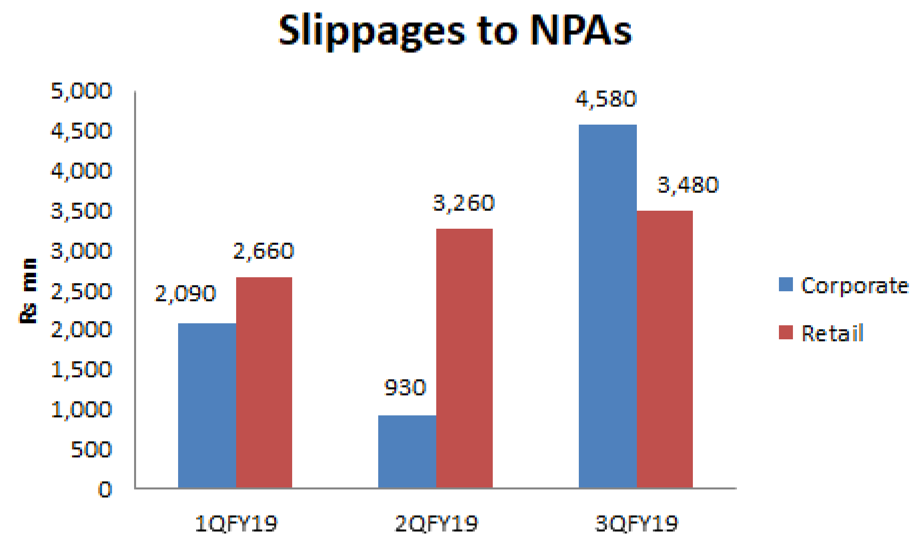
Source: Registrar of Companies

It defies explanation how Indusind Bank's credit appraisal and risk management department not only approved this loan but agreed to take an illiquid security of an optionally convertible debt of an associate company in the group. As the entire Zee founder group of investment companies is constrained on liquidity what value can Indusind Bank get from PANI if the security is to be invoked? Moreover, if the debt is converted into equity, how will the bank get an exit since PANI is an unlisted company? The mutual funds which had invested in Sprit's debt securities had taken a cover of 1-1.5x of Zee Entertainment Enterprises equity shares, and even those shares proved to be illiquid when they wanted to sell it after the company was unable to redeem its debt.

Now, like the mutual fund industry, Indusind Bank will also have to depend on the founders of Zee to sell part of their stake in listed companies or divest assets to recover their loans.

It is apparent that the bank's exposure to Sprit Infrapower is high-risk, and the probability of the account being classified as NPA is high, as the same company has in effect defaulted to the mutual funds. In case it becomes a NPA for the bank, the chances of a total write-off are high, on account of the poor security.

An analysis of Indusind Bank's additions to NPAs in the 3 quarters of FY2019, reveals that the single loan of Rs 5 bn to Sprit Infrapower exceeds the entire corporate slippages in each of the quarters. The Sprit Infrapower loan also exceeds the entire retail slippages in each of the 3 quarters. Hence if the account is classified as NPA, as it should, it can have a material impact on a quarter's NPA and credit costs for Indusind Bank.



Source: Indusind Bank

This analyst had earlier highlighted that contrary to the bank's lofty valuations, shareholders need to carefully scrutinise the credit appraisal, risk management and credibility of the accounts at Indusind Bank. The recent instances of the bank's unsecured loan to the insolvent IL&FS and its high-risk exposure to Sprit Infrapower heighten concerns of poor credit appraisal and inadequate risk management at the bank. Not only should shareholders be concerned, but the banking regulator should also examine these processes at the bank before a major mishap occurs. The coveted laurel on the bank's CEO's head may well turn into a crown of thorns for stakeholders of the bank.

Note: An email was sent to Indusind Bank but no reply or acknowledgement has been received.

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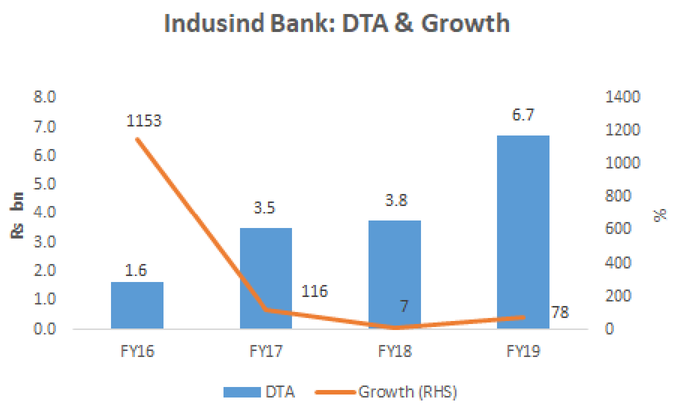
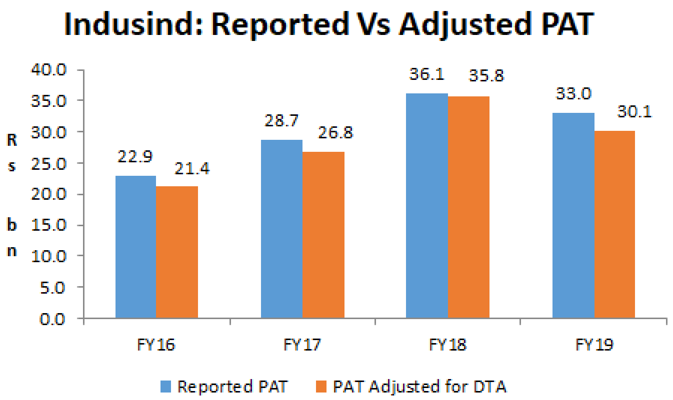
Sell-Side Analysts' Blind Faith in IndusInd Bank Need Not Blind Investors

Monday, May 27, 2019.

Indusind Bank not only declared 4QFY2019 results far below consensus expectations, but FY2019 net profits have been inflated by a significant increase in net deferred tax asset (DTA). As usual, the business media and sell-side analysts have ignored the significance of the rise in DTA in inflating profits in the case of HDFC Bank, Yes Bank and now at Indusind Bank. The sell-side, in near unanimity, is bullish on a bank which reported two consecutive years of fudged accounts, and whose credit and risk management made an ill-advised, large unsecured loan to the insolvent IL&FS and the bank consistently guided for a much lower provision for this loan than warranted. The sell-side is, instead, enthused by the bank's disclosure that its stressed exposure is only 1.9% of its loans. Such is the quality of analysis in an over-brokered market.

On May 22, 2019, Indusind Bank reported its 4QFY2019 net profits of Rs 3.6 bn (62% yoy decline) as compared with a CNBCTV-18 consensus estimate of Rs 7.4 bn. Not only was the reported profit far lower than the expectation, but the media and the sell-side conveniently ignored the 78% increase in net DTA to Rs 6.7 bn. Although Indusind Bank did not disclose the DTA in its analyst presentation, it was quantified in its Basle 3 disclosure. Factoring the increase in the DTA, Indusind Bank's net profit is lower by 9% as compared with the reported Rs 33 bn. More worryingly, on the analyst call not a single question was posed to the bank on its DTA and the reasons for the large increase. It is apparent that, for the 54 analysts tracked by Bloomberg who cover Indusind Bank, the intangible DTA is a non-issue, especially when its increase results in inflation in net profits.





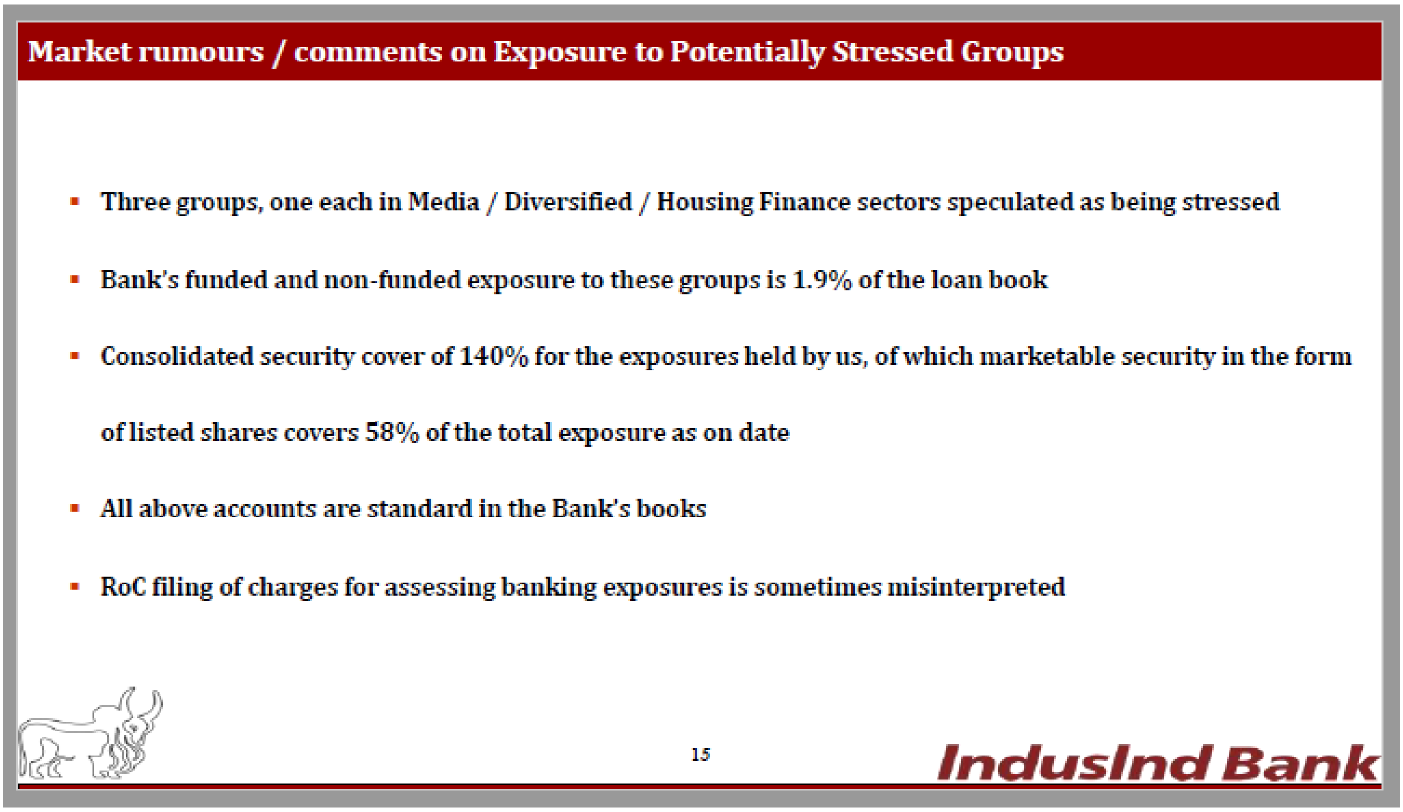
Source: Indusind Bank

This writer has been highlighting the concern regarding DTA being used to inflate bank profits since June 2017. Unfortunately, neither the market nor even the banking regulator is questioning banks on why DTA has been constantly rising when Indian Accounting Standard (IAS-22) admits that DTA can only be created for the short term, and it will have to get reversed as a charge to future profits. It is apparent that banks are utilising DTA to partly neutralise the impact of bad debt provisions to inflate current profits, but these banks are merely deferring the hit to profits to a future date. It is even more unfortunate that analysts are refusing to highlight such practices, and to caution investors that profits are being inflated on account of a rise in an intangible asset.

Indusind Bank's Exposure to Stress Corporates

In its 4QFY2019 presentation, Indusind Bank, to assuage the concerns of the market, disclosed that its high-risk exposure (fund-based and non-fund-based) to stressed groups like Anil Ambani, DHFL, Essel founders and others is only 1.9% of its loans, i.e. around Rs 35.4 bn or 13.4% of its CET-1. After this announcement, the stock rallied, as analysts were expecting the amount to be significantly higher, and in their results note this figured prominently in reaffirming their bullish call, despite the poor results.

Extract Analyst Presentation 4QFY2019 Results



Source: Indusind Bank

While the disclosure by Indusind Bank is a positive, this writer remains cautious on this number, as the bank's past history does not inspire confidence. Firstly, the bank reported fudged accounts in FY2016 and FY2017, and was even fined by the banking regulator. Pertinently, Indusind Bank did not penalise or discipline the CEO, Romesh Sobti, for the public shaming of the bank, even though, according to Section 46(1) in the Banking Regulation Act, 1949 (BRA), wilful mis-reporting information by banks is a criminal offence. A second concern is the manner in which the bank provided for its unsecured loan of Rs 20 bn to IL&FS, which it disbursed around July 2018. This loan became immediately problematic, as IL&FS group companies began defaulting in June 2018 (became public only in late September 2018). When IndusInd announced its 2QFY2019 results on October 15, 2018, it was public knowledge that IL&FS had defaulted and was insolvent. As per RBI norms, an unsecured non-performing loan requires 20-25% provisioning in its first year and requires 100% provision by the 366th day of its remaining a NPA. In 2QFY2019 Indusind Bank provided only Rs 2.75 bn on its Rs 20 bn unsecured exposure, i.e. 13.8%, and stated that the bank may have to eventually make a further 20-25%, aggregating to a maximum of 39% provision.

Extract Analyst Call Transcript 2QFY2019

Romesh Sobti: So this is the judgement call on what we think. First of all, there is no call to make a provision, it is a standard account. We expect the accounts will remain standard. We have seen the maturity profile of our exposures and the cash that we are holding. So at this point of time, this is our judgment call on the extent of provisioning that we would need and that is the call that we have made and this had been done in sort of conjunction and with validation from our statutory auditors as well. So the best case scenario of course is that we don't even provide this and we write it back and that scenario is equally possible. The scenario is possible that you may have to

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October 15, 2018

make another may be 20 to 25% of this provisioning higher than this, is possible, so both scenarios are possible is the judgment call at this point of time that this is prudential in terms of our exposure.

Source: Indusind Bank

At the time of its 3QFY2019 results on January 9, 2019, Indusind Bank revised its provision requirement for the unsecured loan to IL&FS to "between 40% and 50%."

Extract Analyst Call Transcript 3QFY2019

Mahrukh Adajania: And also any level of provisioning…50%, 60% you have in mind on the hold-co?

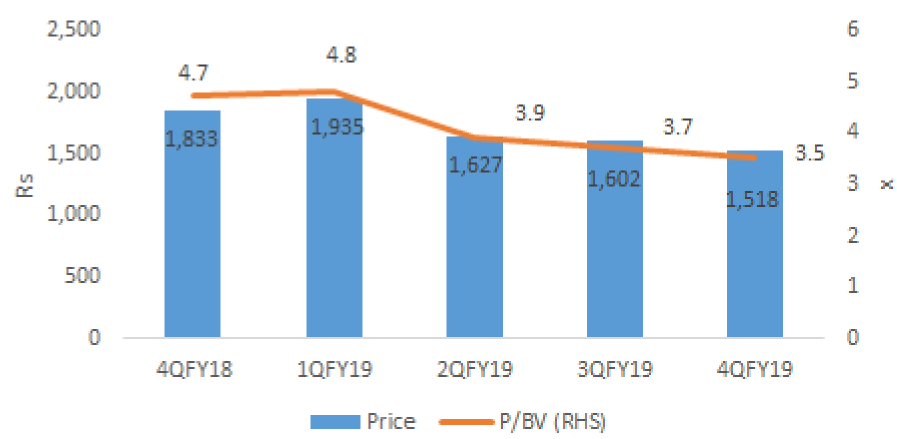
Romesh Sobti: Yes, so far it is all sort of guestimates, how much should you made, should you make 50 or 100 or 25 or whatever. Now we are getting to a stage that we have a good fix on the assets which belongs straight only to the holding company, not the SPVs and we have a number, we have a list and we have done a first cut analysis of the realizable value, we have made some provisions this quarter as well and I think we are going deeper into it to check with buyers on what value they are willing to give for their assets, because ultimately that is the realizable value and therefore we will get this quarter a much stronger fix on how much we would need to provide and our current sensing is it could be anything between 40% and 50%.

Source: Indusind Bank

In its 4QFY2019 results call, Indusind Bank stated that it had provided 70% for its unsecured loan and 25% for IL&FS group companies, where it has an exposure of Rs 10 bn. It was obvious after IL&FS's default became public in early September 2018 that it was an insolvent company with a negative net worth, and Indusind Bank needed to eventually provide 100% against the unsecured loan. Instead the bank initially only made a provision 13.8%, which it raised step by step to 70%, while always assuring analysts that it required a much lower level of provisioning.

With such a track record, investors have to be extremely cautious regarding the credibility of Indusind Bank's disclosures. However, the sell-side has no such concerns. Prior to the announcement of the 4QFY2019 results, according to Bloomberg, 79% (41) of the analysts covering the bank had a 'Buy' recommendation, and 21% (11) had a 'hold' recommendation (i.e., there was no "sell' recommendation), with an average 12 month price target of Rs 1,951. After the results, which majorly disappointed the street, there was no change in the recommendations, but the price target was revised downwards to Rs 1,874.

Indusind: Share Price & P/BV on Results Date



Source: Indusind Bank

Indusind Bank, since the announcement of its 4QFY2018 results on April 18, 2018 till the 4QFY2019 results has seen a 17% fall in its share price, and has underperformed the Nifty-50 by 28%. Its P/BV has been de-rated on concerns of its asset quality, which has led to a sharp fall in its profits. But despite these real concerns and evidence regarding the management's diminished credibility, the sell-side maintains its faith in the bank. Investors, though, need to be more careful.

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Sell Side Analysts on IndusInd Bank: A Load of Bull

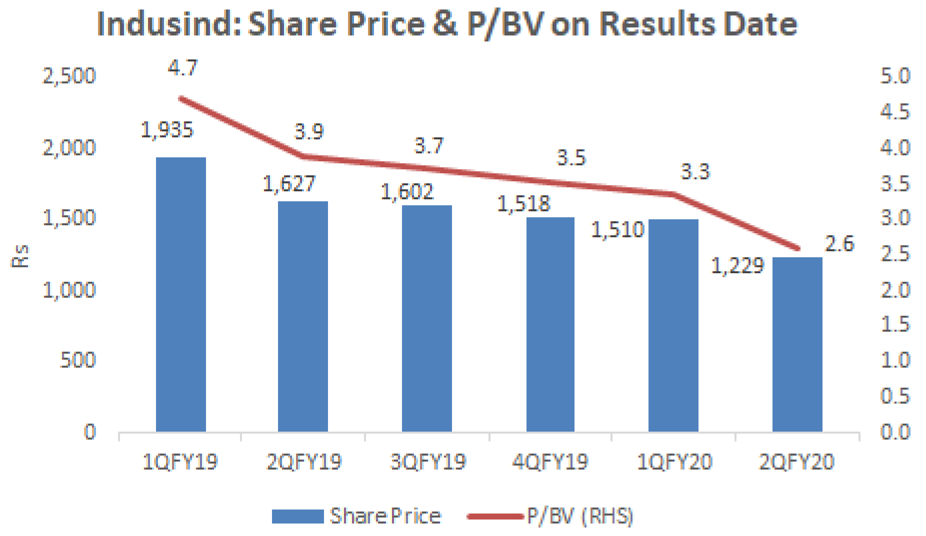
Thursday, October 17, 2019.

Indusind Bank, once a hot favourite of the market and of institutional investors, is fast losing its lustre. It has fallen by around 21% in the past year, and lost around US$ 1.4 bn for shareholders. But right through this decline, while the market had concerns on asset quality, the overwhelming majority of the 53 sell-side analysts continued to repose faith in the bank and its senior management by steadfastly maintaining their bullish view on the bank. This is despite the bank reporting significantly higher credit costs than the sell-side estimates, compelling them to increase their credit cost estimates for FY20E and FY21E and reduce their 12 month target price on Indusind Bank. Neither the sharp deterioration in asset quality, nor the downgrading of estimates, nor the fall in the share price, nor the opacity in CEO succession has deterred the loyalty of the sell-side to the bank. The safety of the herd ensures that there will be no accountability when bullish calls go horribly wrong. The continued sell-side devotion to Indusind Bank may result in a sour and not so happily-ever-after ending for the bank's shareholders.

Indusind Bank: 1 Year Share Price History

Source: Moneycontrol

Indusind Bank's quarterly earnings since 1QFY2019 have led to a consistent decline in its share price, and an even more severe de-rating in its critical P/BV multiple, which declined from 4.7x to 2.6x. In the past 1 year the bank's market capitalisation has lost nearly US$ 1.4 bn, and the stock has also underperformed the NIFTY-50 by nearly 30%. The issue is whether the large tribe of experienced sell-side analysts cautioned shareholders about such an outcome.



Source: Indusind Bank & HKH Research

For over 2 years, 51-53 dedicated sell-side banking analysts covered the Indian banking sector. Most of the global bulge bracket sell-side firms have a presence in India, in addition to the numerous domestic firms which operate mainly in India. In the case of Indusind Bank, the consensus sell-side view has been positive, with an overwhelming majority of the analysts maintaining a 'Buy' recommendation since April 28, 2017.

Sell-side Coverage of Indusind Bank as Tracked by Bloomberg

Date	'BUY'	'HOLD'	'SELL'	Total	Price	12 Mth Price Target	Potential Return
					Rs	Rs	%
28 April 2017	43	6	2	51	1,445	1,566	8.4
15 October 2018	41	10	0	51	1,627	2,022	24.3
23 May 2019	42	10	0	52	1,599	1,874	17.2
15 October 2019	41	11	1	53	1,257	1,614	28.4

Source: Bloomberg

What is interesting to note is that, despite Indusind Bank under the leadership of Romesh Sobti reporting two consecutive years of fudged accounts in FY2016 and FY2017 (see [Indusind Bank - Who Cares About 'Divergence'?]), giving an ill-advised, unsecured Rs 20 bn (around 10% of the bank's capital) bridge loan to the insolvent IL&FS (see [Are Indusind Bank's Credit and Risk Departments Run by Financial Illiterates?]) , and having [exposure] to stressed non-bank finance companies (NBFCs), the sell-side has remained supremely confident of its bullish outlook on the bank. On April 28, 2017, well before any of these negative developments took place, 43 analysts (84%) had a 'Buy' on the bank, and yet on October 15, 2019, when the negative information was in the public domain, 41 analysts (77%) had a 'Buy', as monitored by Bloomberg. Even though the stock market severely penalised the bank in that timespan, the sell-side were least bothered about changing their consensus bullish outlook.

Analysing select sell-side coverage of Indusind Bank, which should be a fair representative of the consensus bullish view on the bank, it is apparent that the sell-side has consistently underestimated the bank's asset quality issues, resulting in an upward revision of the bank's credit costs in their estimates. Despite the upward revision in credit costs and downward revision in earning forecasts and price targets, the sell-side refuses to change its positive view on the bank.

Kotak Institutional & IDFC Securities Coverage & Credit Cost Estimates on Indusind Bank

Sell-side	Date	FY19E	FY19A	FY20E	FY21E	Reco.	Share Price	PT	Return
		Credit Cost as % of Av. Loans					Rs	Rs	%
Kotak In.	16-10-18	2.1	-	2.4	2.7	Buy	1,627	1,850	13.7
Kotak In.	10-10-19	-	3.3	3.7	3.9	Add	1,229	1,500	22.1
IDFC Sec	19-04-18	0.8	-	0.8	-	Outperf.	1,834	2,100	14.5
IDFC Sec	10-10-19	-	1.2	0.9	1.1	Outperf.	1,229	1,380	12.3

Source: Kotak Institutional & IDFC Securities

This writer was one of the few if not the only analyst who cautioned investors since mid-December 2017 (see What No One Likes to Mention About Indusind Bank) and continued highlighting concerns on the integrity of its accounts, accountability of senior management and its poor credit and risk management in 2018 and 2019. This was from information in the public domain which the sell-side conveniently overlooked.

The tragedy is that the sell-side could have easily cautioned investors by sounding the alarm bells at an earlier stage, but, for reasons of corporate access, the large tribe of analysts believed it served their interests to give Indusind Bank the benefit of the doubt. Unfortunately, by proving their loyalty to the bank, the sell-side made their clients suffer. **When consensus bullish calls go horribly wrong, the safety of the herd ensures a lack of accountability. This allows 'research' to keep doing its real job: corporate public relations for the companies under coverage.**

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IndusInd Bank's Charge on Shareholder Funds: Obscurity Is the Best Policy?

Monday, 20 January 2020.

In a stunning non-disclosure, Indusind Bank conveniently neglected to reveal, in its 3QFY2020 results, that it had reduced shareholder funds by around Rs 6.7 bn as a charge for frauds without charging it to profits. The bank reported a consolidated net profit of Rs 13.09 bn (Rs 14.01 bn in 2QFY2020); had the fraud amount been charged to profits, it would have reported only Rs 6.4 bn as net profit. While the Reserve Bank of India (RBI) permits this practice in case of frauds (banks are permitted to spread the provision over 4 quarters by reversing the debit to shareholder funds), the banking regulator also states that suitable disclosures have to be made pertaining to the amount of fraud and quantum of provision for it. As the bank did not disclose this amount of direct reduction from shareholder funds, it was the duty of Purushottam Nyati, partner, Haribhakhti & Co., the audit firm, to highlight it, which he, sadly, failed to do.

The charge of Rs 6.7 bn was only revealed by Indusind Bank in the results conference call when analysts enquired about the disparity between the shareholder funds and the net profits reported, and a vague disclosure in the analyst results presentation. Responding to this writer's queries on the lack of disclosure, Indusind Bank said that the explanation in fine print on the analyst presentation was "self explanatory." Unfortunately, this lack of transparency, which the RBI needs to investigate, adds to the litany of issues that this writer has been highlighting pertaining to the leadership of Romesh Sobti, CEO, Indusind Bank. These include untrustworthy financial accounts in FY2016 and FY2017, reckless lending to the insolvent IL&FS and other stressed groups, and the use of deferred taxes to inflate profits. With Sobti's retirement by March 2020, there will be a change in leadership at Indusind Bank, and shareholders should be extremely cautious regarding what else might emerge from the murky depths of this once fancied bank.

On January 14, 2020 Indusind Bank reported consolidated 3QFY2020 (quarter ended December 31, 2019) net profit of Rs 13.09 bn (2QFY2020 net profits Rs 14.01 bn). **Pertinently, there was no disclosure that the bank had taken a direct charge of around Rs 6.7 bn to shareholder funds, instead of the more prudent accounting treatment of a charge to profits.** The only comment made by the bank was in note 10 in the mandatory disclosure,

> "For the fraud detected during the quarter in respect of exposure towards two entities, Bank has made the necessary provision in accordance with the RBI guideline."

Notes to Accounts in Indusind Bank's 3QFY2020 Results.

Notes:

1 The consolidated financial statements of the Group comprise the financial statements of IndusInd Bank Limited (the Bank), Bharat Financial Inclusion Limited (BFIL), a wholly owned subsidiary, and IndusInd Marketing and Financial Services Private Limited (IMFS), an Associate of the Bank.

2 There has been no material change in the accounting policies adopted during the quarter / nine months ended December 31, 2019 as compared to those followed for the year ended March 31, 2019.

3 The working results for the quarter / nine months ended December 31, 2019 have been arrived at after considering provision for standard assets, including requirements for exposures to entities with Unhedged Foreign Currency Exposure, non-performing assets (NPAs), depreciation on investments, income-tax and other usual and necessary provisions.

4 The above financial results for the quarter / nine months ended December 31, 2019 were subjected to a Limited Review by the Statutory Auditors of the Bank. An unqualified / unmodified report has been issued by them thereon. These financial results were reviewed by the Audit Committee and subsequently have been taken on record and approved by the Board of Directors at its meeting held on January 14, 2020.

5 RBI Master Circular DBR.No.BP.BC.1/21.06.201/2015-16 dated July 01, 2015, as amended, on Basel III Capital Regulations contain guidelines on certain Pillar 3 and leverage ratio disclosure requirements that are to be made along with the publication of financial results. Accordingly, such applicable disclosures have been placed on the website of the Bank which can be accessed at the following link:
http://www.indusind.com/content/home/important-links/regulatory-disclosures-section.html
These disclosures have not been subjected to the Limited Review.

6 The Capital Adequacy Ratio of the Bank is computed on the basis of RBI guidelines applicable on the relevant reporting dates and the ratio for the corresponding previous period is not adjusted to consider the impact of subsequent changes if any, in the guidelines.

7 On October 14, 2017, the Board of Directors of the Bank and the erstwhile Bharat Financial Inclusion Limited (e-BFIL), at their respective meetings, approved a Composite Scheme of Arrangement (Scheme) under Section 230-232 of the Companies Act 2013 and other applicable laws and regulations. The Scheme inter alia contemplated the merger of e-BFIL with the Bank, a preferential allotment of Share Warrants to the Promoters, a simultaneous transfer of the Business Correspondent Undertaking (BC Undertaking) contained in e-BFIL to a wholly owned subsidiary of the Bank, and liquidation of the e-BFIL without winding up. For the purposes of the Scheme, IndusInd Financial Inclusion Limited (IFIL), a wholly owned subsidiary of the Bank, was incorporated on August 8, 2018 after obtaining requisite RBI approval. The National Company Law Tribunal Mumbai (NCLT) sanctioned the Scheme on June 10, 2019 with the Appointed Date set at January 1, 2018. The Scheme became effective on July 4, 2019 and accounting effects have been given during the nine months ended December 31, 2019. The accounting effects, in so far as it relates to merger of e-BFIL with the Bank, have been given under Accounting Standard 14 – Accounting for Amalgamation. Accordingly, the financial results for the quarter / nine months ended December 31, 2019 are not comparable with the previous periods.

8 Pursuant to the Scheme sanctioned by the NCLT as stated in para 7 above, on July 6, 2019, the Bank allotted 8,96,17,781 shares of Rs.10 each fully paid, to the eligible equity shareholders of e-BFIL in the ratio of 639 shares of the Bank for every 1000 shares of e-BFIL. Consequent to the receipt of subscription amount at 25% of the price of Rs.1,709 per Share Warrant, on July 6, 2019, the Bank allotted 1,57,70,985 Share Warrants to the Promoters of the Bank. Each Share Warrant is convertible to one equity share of the Bank fully paid, upon exercise of the option by paying the remaining 75% within 18 months of allotment. On July 04, 2019 the BC Undertaking contained in the merged entity was transferred to IFIL as a going concern for which IFIL allotted 4,37,03,500 equity shares of Rs.10 each fully paid to the Bank, and the e-BFIL was liquidated without winding up. Subsequently, in accordance with the Scheme sanctioned by NCLT, on August 02, 2019 IFIL has been renamed as Bharat Financial Inclusion Limited (BFIL).

9 In accordance with a clarification issued by RBI on May 8, 2019 regarding Debt Asset Swap Transactions, a provision of Rs.54.30 crores was made during the quarter ended March 31, 2019, by debiting Reserves and Surplus - Balance in Profit and Loss Account which was to be reversed by debiting Profit and Loss Account over the next three quarters. Accordingly Rs.18.10 crores has been debited during the quarter ended December 31, 2019 and cumulatively an amount of Rs. 54.30 crores has been debited during the nine months ended December 31, 2019.

10 For the fraud detected during the quarter in respect of exposure towards two entities, Bank has made necessary provision in accordance with the RBI guidelines.

11 During the quarter / nine months ended December 31, 2019, the Bank allotted 87467 shares and 765575 shares respectively, pursuant to the exercise of stock options by certain employees.

12 Previous periods / year figures have been regrouped / reclassified, where necessary to conform to current period / year classification.

Source: Indusind Bank

Only in slide 18 of the result presentation to analysts did the fine print state,

> "Note 2: Exposure 100% provided of which 25% debited to P&L and 75% drawn down from the Reserves (drawn down amount shall be debited to P&L equally over the 3 quarters."

But here again the amount was not disclosed by the bank, and this was the only disclosure by the bank that a certain unspecified amount was taken as a direct deduction from shareholder funds. Responding to a questionnaire from this analyst on the non-disclosure issue, Indusind Bank highlighted slide 18 as an adequate disclosure for its shareholders and stated that it is "self explanatory!!"

Extract from Indusind Bank's 3QFY2020 Analyst Presentation

Market rumours / comments on Exposure to Potentially Stressed Groups

- Three stressed groups, one each in Media / Diversified / Housing Finance sectors
- Bank's net funded and non-funded exposure to these groups is 0.47% of the loan book net of provisions held as under:

% of Loans	Q4FY19	Q1FY20	Q2FY20	Q3FY20
Media Group	0.4%	0.4%	0.3%	0.27%(1)
Diversified Group	1.0%	1.0%	0.5%	0.21%
HFC	0.4%	0.3%	0.3%	- (2)
Total	**1.9%**	**1.7%**	**1.1%**	**0.47%**

Note 1: Holding Company exposures at 0.14% and OpCo Cash Flow exposures at 0.12%

Note 2: Exposure 100% provided of which 25% debited to P&L and 75% drawn down from the Reserves (drawn down amount shall be debited to P&L equally over the next 3 quarters).

Source: Slide 18, Indusind Bank 3QFY2020 Results PPT

Balance Sheet

(Rs Crs)

	Q3FY20	Q3FY19	Y-o-Y (%)		Q2FY20	Q-o-Q (%)	
Capital & Liabilities							
Capital	693	602	15%	▲	693	-	▲
Reserves and Surplus	32,789	25,798	27%	▲	32,171	2%	▲
Share Warrant Subscription money	674	-	-	▲	674	-	▲
Deposits	2,16,713	1,75,701	23%	▲	2,07,193	5%	▲
Borrowings	46,813	44,536	5%	▲	44,558	5%	▲
Other Liabilities and Provisions	10,261	9,562	7%	▲	9,644	6%	▲
Total	**3,07,943**	**2,56,199**	20%	▲	**294,933**	4%	▲
Assets							
Cash and Balances with RBI	11,350	9,580	18%	▲	9,973	14%	▲
Balances with Banks	9,438	3,170	198%	▲	5,306	78%	▲
Investments	60,517	53,681	13%	▲	63,540	(5%)	▼
Advances	2,07,413	1,73,169	20%	▲	1,97,113	5%	▲
Fixed Assets	1,832	1,699	8%	▲	1,799	2%	▲
Other Assets	17,393	14,900	17%	▲	17,202	1%	▲
Total	**3,07,943**	**2,56,199**	20%	▲	**2,94,933**	4%	▲
Business (Advances + Deposit)	**4,24,127**	**3,48,870**	22%	▲	**4,04,306**	5%	▲

Source: Slide 19, Indusind Bank 3QFY2020 Results PPT

Even in the analyst conference call, none of the senior executives, including Romesh Sobti, voluntarily disclosed that such a large deduction had been taken below the line. It was only in response to analyst queries (p. 6 in transcript) based on the fine print note in note 18 and the marginal growth in shareholder funds in slide 19 that the bank revealed that it had taken around Rs 6.7 bn against shareholder funds.

While Romesh Sobti defended the accounting treatment as being in line with an April 18, 2016 RBI circular which permitted banks to spread a fraud hit over 4 quarters to smoothen the impact on provisions and profits, he failed to disclose to the analysts that the same circular also specified,

> **"(d) Banks shall make suitable disclosures with regard to number of frauds reported, amount involved in such frauds, quantum of provision made during the year and quantum of unamortised provision debited from 'other reserves' as at the end of the year."**

In the opinion of this writer, Indusind Bank should have explicitly disclosed the amount that it had charged to shareholder funds. It was also the duty of the auditor, Purushottam Nyati, partner, Haribhakhti & Co., to have highlighted the omission by Indusind Bank to shareholders. Such non-disclosures should be investigated by the banking regulator.

The only reason for the bank to take the fraud hit below the line was to inflate its 3QFY2020 net profits, as it would have had to report a severe decline in its earnings. From a capital adequacy position, it has no impact as in both cases, the capital adequacy remains the same. It is unfortunate that the bank decided to use the more liberal accounting treatment, and worse, that it did not chose to disclose it to shareholders.

Unfortunately for Indusind Bank, the non-disclosure is not an exception, but part of a litany of issues which this analyst has been highlighting. These reflect poorly on the board of directors and the CEO. These issues include reporting two successive years of fudged accounts in FY2016 and FY2017, a reckless unsecured loan of Rs 20 bn to the insolvent IL&FS, other high-risk loans to stressed groups, and, finally, the creation of deferred tax assets to inflate current profits.

It is apparent to this writer that Indusind Bank is facing strong headwinds on asset quality as it attempts to meet the street's estimates on earnings. Romesh Sobti will retire in March 2020, and in all probability he does not want to depart with a depressed net profit in his last year. Shareholders should be prepared for other nasty surprises to emerge from the murky depths of this once fancied bank.

DISCLOSURE & CERTIFICATION

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Will the New CEO Follow Consolidation, or Stick to Sobti's High-Risk Growth Strategy?

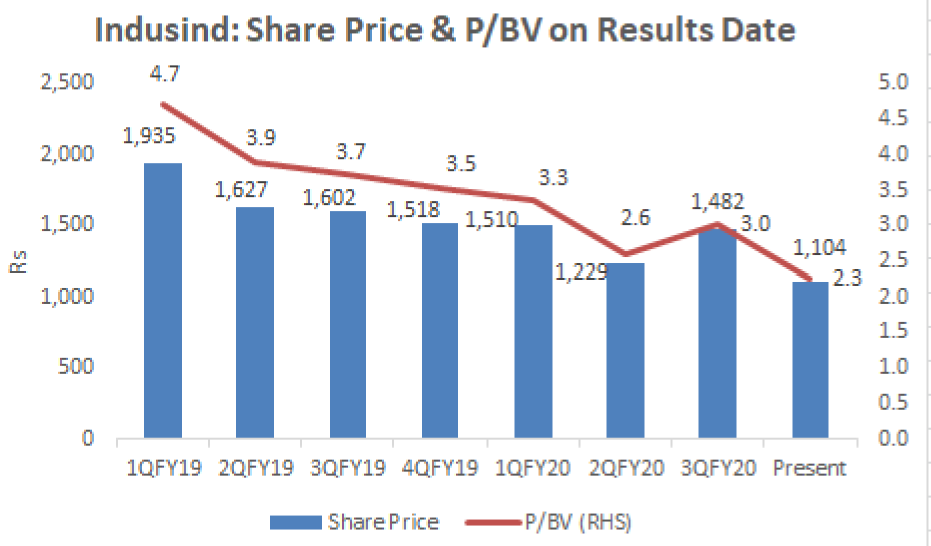
Monday, March 2, 2020.

On February 27, 2020 the Reserve Bank of India finally approved Sumant Kathpalia as the CEO who will succeed Romesh Sobti when the latter retires on March 23, 2020. Kathpalia, who has a background in consumer finance and wealth management, will be taking charge of a bank which is facing stiff headwinds due to ill-advised corporate loans. These have resulted in a steady decline in its share price since August 2018 and a massive de-rating in its all-important P/BV multiple.

Unfortunately for Kathpalia, the severity of the economic slowdown, which is likely to continue, will dictate the business strategy of Indusind Bank. He should be cautious on providing guidance on future profitability and aggressive asset growth. Axis Bank in early 2019, under the newly joined CEO, Amitabh Chaudhry, projected an optimistic future scenario. This initially resulted in an upsurge in the share price, but Axis has thereafter lost most of its gains as the bank struggles to achieve those rosy projections. The market has concerns regarding Indusind Bank's high-risk appetite. This has resulted in its troublesome telecom and real estate exposures, which may take time to resolve. This writer has been concerned about the bank's risk management and accounting integrity for some time, and Kathpalia will have to reassure the market that these critical areas have been addressed.

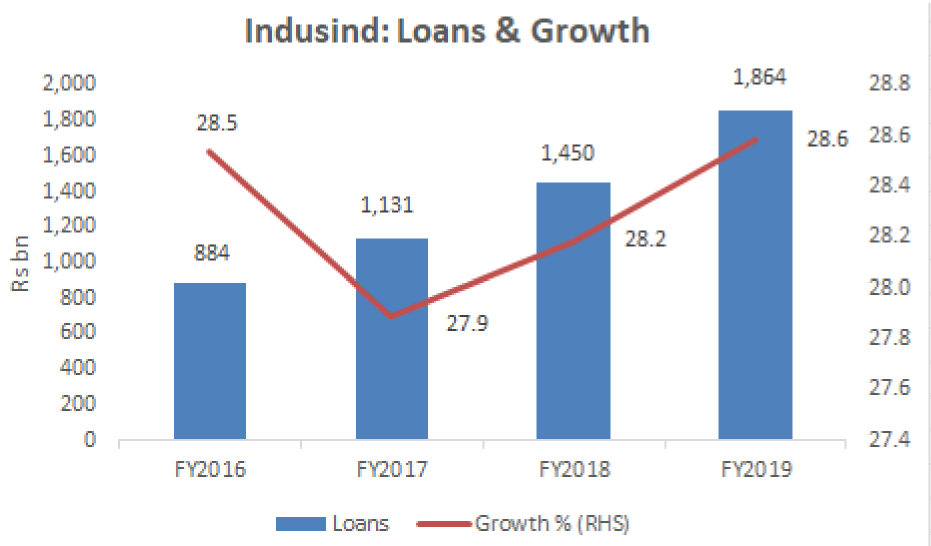
It may be more prudent for Kathpalia to not grow loans and instead focus on recovery, as acquiring quality assets in a deteriorating economy will be extremely difficult. No doubt, such a strategy may not be initially welcomed by the stock market, which normally tends to be growth focused. The strategy that this acolyte of Sobti should follow is to reverse the high growth strategy of his mentor, which has caused so much grief recently to shareholders. If Kathpalia implements a conservative strategy where the assets and top line remain constant, profits can increase in the medium term through lower credit costs, thus rewarding shareholders and regaining part of the bank's earlier glory.

After considerable speculation in the media on the likely successor to Romesh Sobti, CEO Indusind Bank, the RBI finally approved Sumant Kathpalia as the next CEO. Kathpalia was head, consumer banking, Indusind Bank, and had joined the bank at around the time Sobti took charge as CEO. The announcement of Kathpalia's appointment less than a month before Sobti's retirement on March 23, 2020 has at least provided the much needed clarity to the capital market on the critical leadership issue.



Source: Indusind Bank & Moneycontrol

Kathpalia's background as a banker has been mainly in consumer banking and wealth management, with limited exposure to corporate banking, an area which is currently causing the bank considerable distress. Under Sobti Indusind Bank's share price since 2008 increased by 10.8x, richly rewarding its shareholders, but unfortunately in the last two years, the stock price has disappointed as the bank's accounting integrity and poor corporate risk management were thoroughly exposed. Since the announcement of its 1QFY19 (June 30, 2018) results, the share price has declined from Rs 1,935 to the current Rs 1,104, and its important P/BV has collapsed from 4.7x to the present 2.3x, undermining investor confidence in the bank.



Source: Indusind Bank

The aggressive loan growth of the bank in the past is presently showing up in rising non-performing loans (NPLs). During FY2020, not only are slippages to consumer NPLs steadily increasing, but certain large corporate loans are adding to the woes of the bank, with more expected from the bank's telecommunications and real estate exposure.

Indusind Bank: Slippages to Gross Non-performing Loans

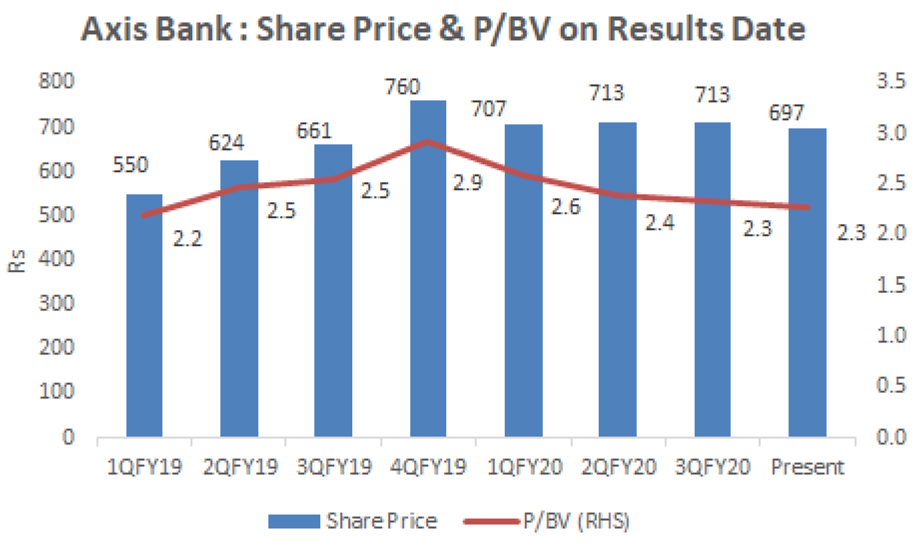
Rs mn	1QFY20	2QFY20	3QFY20
Corporate	1,750	3,370	12,370
Consumer	5,500	6,230	7,080
Total Slippages	7,250	9,600	19,450

Source: Indusind Bank

The critical issue for the capital market and for the bank's investors is what the future business strategy of Kathpalia will be, and whether he will he follow in his mentor's footsteps of high credit growth, or will be more prudent, and focus on consolidation and improving the internal risk management systems in the bank, as the economy is showing severe sign of stress. If he implements the former, the decline in the bank's share can only accelerate, as the high credit growth will result in even higher asset quality problems, while if he follows a strategy of consolidation with a concerted emphasis on asset recovery, the bank has a possibility of returning to its earlier glory.

A strategy based on consolidation may not initially win the bank laurels in the stock market, which normally wants to see asset growth and bigger market share. However, by maintaining constant assets and top line, and focusing on asset recovery and improving the bank's internal risk management systems, the bank may initially report lower profits from higher credit costs on the existing book, but thereafter the bank can achieve higher profit growth through lower credit costs. As the economy is going through a period of severe stress, large banks will find it extremely difficult to get sizeable retail and corporate assets of quality. If under such conditions bank grow their assets, there exists a high probability of higher credit costs. Unfortunately, some banks, to counter the existing asset quality issues, attempt to outgrow the problem by increasing asset growth, in the hope that the income from the new loans will compensate for the higher credit costs from the existing loans. However, when the economy is under stress, the new loans can compound the asset quality problem, worsening an already deteriorating situation.

Kathpalia should also be conservative in providing guidance to his strategy, keeping in mind how the initial optimistic guidance by Amitabh Chaudhry (Axis Bank CEO) when he took charge in January 2019 resulted in a surge in the share price, but thereafter the bank lost most of its gains as the bank's subsequent performance fell short of expectations.



Source: Axis Bank & Moneycontrol

Post March 24, 2020, when Kathpalia takes charge as CEO, he may inform the market on Indusind Bank's future strategy, and whether it will be a break from the aggressive asset growth strategy of his predecessor, or whether he will chart a more conservative path of consolidation. In the opinion of this writer, if he continues a strategy of increasing asset growth on retail and/or corporate, the bank's problems will only get compounded, while if he follows a prudent strategy of asset consolidation, it may result in short-term decline in profits, but will prove to be a more sustainable growth, rewarding shareholders.

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IndusInd Bank: Retaining the Captain of the Titanic for His Job Experience

Monday, March 23, 2020.

The savage mauling of Indusind Bank's share price in the last year, and especially in the last month, is a reflection of the unravelling of the bank's high-risk asset and fee growth strategy. A bank which use to trade at 5x P/BV is currently reduced to being valued at below BV. This speaks of a complete loss of confidence among equity investors. Such an event should have led to a deeper introspection by the bank's board of directors on the capability and competence of Romesh Sobti, chief executive officer (CEO), who will finally retire on March 23, 2020 after a stint of 12 years at the helm. With such a disastrous track record of share price under-performance stretching back 5 years, with depositors pulling out deposits from the bank, the board should have selected an individual from outside the bank and terminate all links with Sobti, once the latter completes his term.

Instead, the board of directors of Indusind Bank selected as Sobti's heir Sumant Kathpalia, a Sobti acolyte who had joined the bank along with his mentor from ABN Amro in 2008. But even further, the board is likely to appoint Sobti as a "full-time advisor" to guide the bank in this tumultuous phase of Sobti's own making. A CEO who was responsible for fudging two consecutive years (FY2016 and FY2017) of financial accounts (a travesty which is a criminal offence if proved to be "wilful"), betting nearly 8% of the bank's capital in an unsecured loan to an insolvent IL&FS, and making the bank take high risk exposure to stressed business groups in real estate, media and telecom should have been removed by the board, rather than rewarded by allowing him to influence business decisions as an "advisor". This is the pathetic state of corporate governance practised by private sector bank boards in India, and institutional investors and the banking regulator remain silent spectators to this charade.

The *Economic Times* on March 20, 2020 interviewed Romesh Sobti, CEO and Sumant Kathpalia, CEO-designate, Indusind Bank. Regarding Sobti's future association with the bank Kathpalia stated,

> "[Sobti] will play some role in the organisation and we continue to believe that he will mentor us and be an advisor to the bank as we move forward"

Sobti also clarified,

> "Basically, it is a full-time advisorship. It is an absolute non-executive role and mentorship in areas that both the management and the board will finalise…in the next few days"

Sometimes a board of directors likes to retain the expertise of CEOs who have rewarded shareholders and stakeholders and have an impressive track record of performance. On the completion of their tenure, the board may appoint such a person as an advisor to the company or advisor to the board. However, the share price of the Indusind Bank since mid-2018 has been on the decline, and it has fallen off the cliff since early February 2020, as the market has significant concerns regarding the high-risk exposures of the bank in the telecommunications, real estate and media sectors.

Indices Performance Vs Indusind Bank

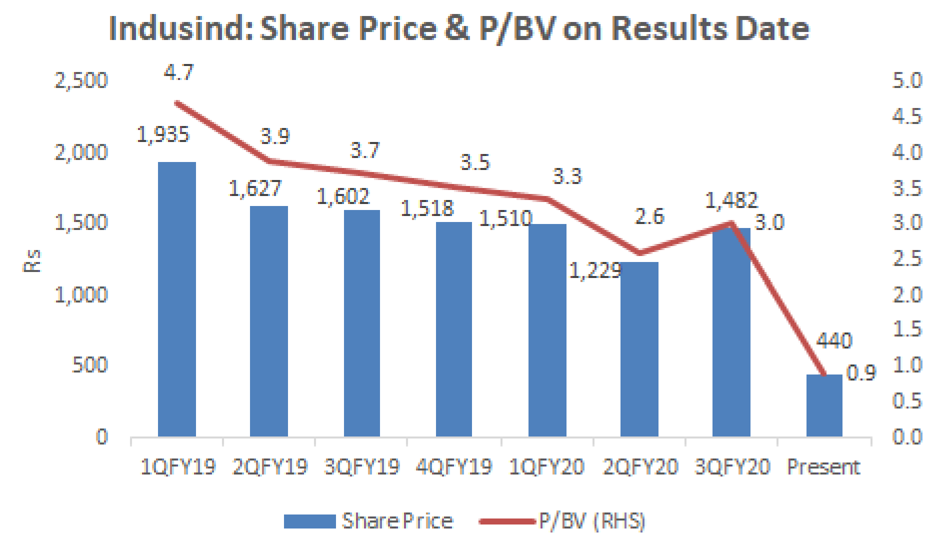
%	1 week	1 mth	3 mth	6 mth	1 yr	2 yr	5 yr
NIFTY-50	-13.8	-31.9	-32.6	-22.8	-28.3	-18.1	2.3
NIFTY Bank	-12.0	-34.3	-37.3	-29.9	-31.9	-16.2	8.0
Indusind	**-33.7**	**-62.4**	**-70.6**	**-70.9**	**-74.1**	**-74.6**	**-50.5**

Source: Moneycontrol

In April 2017, when Indusind Bank was trading at Rs 1,453 (PBV 5x), this writer was possibly the first (and unfortunately the only) analyst on the street to raise the red flag on a high-risk loan which the sell-side brushed aside as a "blip". I had explicitly cautioned,

> "The Jaiprakash Associates transaction and the banking regulator compelling the bank [Indusind Bank] to provide for it is an indicator that the bank may be taking on higher risk than is warranted for its superior valuation."

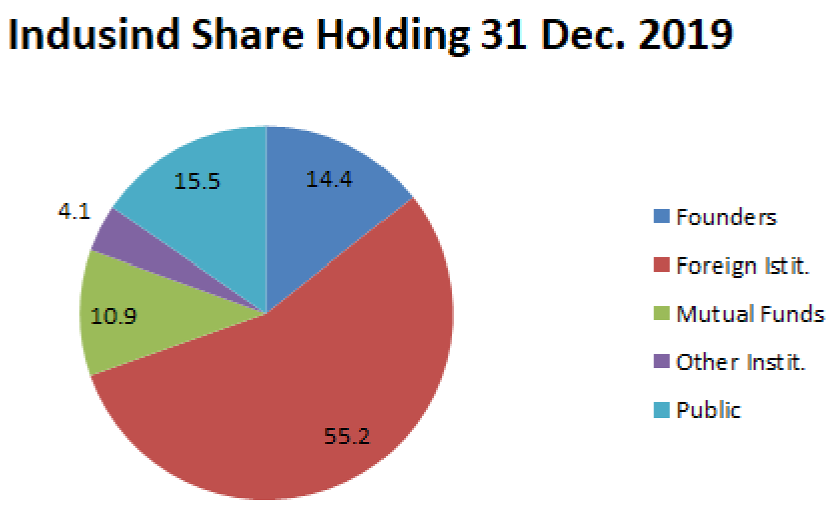
Thereafter this writer consistently continued to highlight and warn the shareholders of the mismanagement at the bank. The issues ranged from fudged accounts, which is a criminal offence if proved to be wilful, to the sheer incompetence of the bank's credit and risk departments in providing an unsecured loan constituting around 10% of the bank's equity to the insolvent IL&FS. I had exposed Sobti's ignorance in publicly defending the IL&FS loan. This writer again exposed the inadequacy of the bank's credit and risk department in providing loans to the investment companies of the founder of Zee media business group. Indusind Bank's significant exposure to Vodafone, estimated at Rs 40 bn (13% of CET1 as on 3QFY20), and the adverse Supreme Court judgement on Vodafone and other telecommunication companies has further compounded the problems for Indusind Bank.



Source: Moneycontrol, Indusind Bank

All these major issues which are senior management-inflicted, with the possible exception of Vodafone expose the leadership of Sobti. The issues confronting Indusind Bank have finally led to the bank being traded at below BV and Sobti as the CEO is to be held directly responsible. In the opinion of this writer, the board of directors should have removed Sobti in early 2018, when the regulator had detected the 2 consecutive years of mis-reported accounts. That was the time for the board to bring in a seasoned banker from outside. Instead, the board not only selected a close confidante of Sobti to succeed him when he retires, but is also likely to finalise an apparently lucrative assignment for Sobti to be appointed as an 'advisor' to the bank. This also raises the possibility that Sobti may continue to steer the bank as an advisor.

While the Indusind Bank board of directors and the founders seem to have a special affinity for Sobti, the non-founder shareholding (the majority), which includes prominent foreign and domestic institutional investors and the Reserve Bank of India, should ensure that Sobti has no further role in Indusind Bank once he retires as CEO.



Source: *Indusind Bank*

Rewarding bank CEOs for poor performance appears to be the norm in India's prominent private sector banks. In July 2017, the Axis Bank board of directors decided to reappoint Shikha Sharma for her fourth term as CEO despite considerable documented mismanagement at the bank. Fortunately the Reserve Bank of India truncated her fourth term, and the bank selected an outsider to succeed Sharma. On June 12, 2018, the Yes Bank shareholders with an "overwhelming majority" approved the reappointment of another term for Rana Kapoor, the founder-CEO, despite the bank reporting 2 consecutive years of fudged accounts in FY2016 and FY2017. The Reserve Bank of India rejected the board's choice. Currently Rana Kapoor is in judicial custody for money laundering and for allegedly receiving kickbacks of Rs 50 bn ($660 mn), and the bank has just emerged from a moratorium and a bailout led by State Bank of India.

What is pertinent to note is that Axis Bank, Yes Bank and Indusind Bank are prominent banks in the capital market, with significant institutional and foreign ownership, and are well covered by sell-side analysts. But, despite documented mismanagement in all 3 banks, there was no outcry of objections from the shareholders and the analysts with regard to reappointing Shikha Sharma and Rana Kapoor as CEOs; nor is there any concern regarding the continuance of Romesh Sobti as an advisor to Indusind Bank.

The experience with Yes Bank is a stark warning of the dangers of a founder-CEO who was allowed to take disastrous decisions without any board censure, and the current valuation of Indusind Bank is clearly revealing the capital market's complete lack of confidence. In such a bleak economic scenario compounded by the corona virus pandemic, Indusind Bank will do well to break all ties with Sobti and completely restructure the senior management, and reverse Sobti's high-risk asset growth strategy if it wants to restore investor and depositor confidence in the bank.

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