

## IDFC Bank Ltd. (IDFB.BO): First take: Below expectations on higher credit costs; Sell

IDFC Bank **reported a net profit** of Rs0.9bn (vs GSe net profit Rs2.0bn) as loan loss provisions came in much higher than expectations (+28% vs GSe) as well as higher operating expenses (+14% vs GSe). As such, core operating profit missed our estimate by 28%.

**Key takeaways** from the results were **(1)** loans under moratorium reduced to 28% from 35% earlier but still remained elevated when compared to other private banks, especially with a high proportion in the wholesale segment (35%); **(2)** credit costs were higher than GSe as the bank made further COVID-related provisions of Rs3.8bn, which implied cover on loans under moratorium was c.2.5%. But with coverage on stress loans remaining relatively low at c.60%, we believe the cost of risk could remain high, and **(3)** weak loan growth (-5% yoy) as disbursements (especially retail) were significantly impacted for the majority of the quarter.

We remain Sell-rated with a 12m TP of Rs18/share.

### Key highlights:

- **Moratorium:** Loans under moratorium reduced to c.28% on the overall portfolio from 35% in April, in terms of value. Within segments, around 23% of retail loans are under moratorium, while on the wholesale side, it is higher at 35%. We note that despite the reduction, moratorium levels still remained elevated when compared to other banks and could therefore, keep the risk of deterioration in asset quality higher in the coming quarters. While the bank has noted that it is targeting a reduction to 10% of loans by August, we would look for how collection efficiencies trend given the surge in local lockdowns which could impact operations especially in the rural segment.
- **Asset quality:** GNPLs decreased sequentially to 2.0% of loans in the quarter (-60bps qoq), significantly lower compared to our estimate of 3.7%. Within retail, GNPL reduced to 0.9% of loans from 2.2% in 4Q'20; however we note that this includes the benefit of moratorium and asset classification standstill as per RBI norms, and therefore could potentially result in higher slippages once moratorium is lifted. Stress loans reduced marginally to 11% of loans versus 11.5% in 4Q'20. We remain cautious on the asset quality given exposure to segments such as MSME/LAP (c.27% of credit books), consumer loan (c.22%)

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and wholesale loans (c.35%).

- Credit costs were 3.6% of loans, ahead of our estimate of 3.0% as the bank made additional COVID-related provisions of Rs3.8bn, taking cumulative provisions to Rs6bn (Rs2.3bn taken in 4Q'20). As a result, the amount of provision buffers came in at c.2.5% of the loan book under moratorium. PCR on GNPLs increased to 75% from 65% in 4Q'20.
- **Loan growth:** Overall reported credit book declined by 5% yoy/was flat sequentially; however the composition of retail loans (as % of funded assets) continues to improve to 65% (vs 50% year ago) with mgmt. targeting 70% retail by FY24. Within retail loan growth of 26% yoy, MSME (+5% yoy), consumer loans/mortgage (+20% yoy) and rural microfinance (+39% yoy) drove the growth - segments where we would be cautious over the near to medium term.
- **Deposit growth:** Progress on deposits continues with core retail deposits (retail CASA + retail term deposits) increasing 139% yoy, signifying the sustainable nature of the growing deposits. Margins trended up sharply to 5.0% (+40/180bps qoq/yoy) on loan mix shift; lower calculated cost of funds at c.7.2% in the quarter.
- **Capital position:** The bank successfully raised Rs20bn in 1Q'21 through the preferential route, taking the CET-1 ratio to 14.58% in the quarter (vs 13.30% in 4Q'20).

We have a Sell rating with a 12 month SOTP based TP of Rs18. Key risks - Stronger-than-expected execution on the liabilities front leading to better margins, benign asset quality.

## Exhibit 1: IDFC Bank - 1Q'21 results summary

IDFC First Bank					Var.	Var.	
Rs mn unless stated	Q1FY20	Q4FY20	Q1FY21	Q1FY21E	Q-o-Q	Y-o-Y	Act vs est
<b>Income statement</b>							
Interest income	37,931	39,559	38,314	37,894	-3%	1%	1%
Interest expenses	26,187	23,924	22,055	21,297	-8%	-16%	4%
<b>Net Interest Income</b>	<b>11,745</b>	<b>15,635</b>	<b>16,259</b>	<b>16,597</b>	<b>4%</b>	<b>38%</b>	<b>-2%</b>
<b>Non Interest income</b>	<b>3,105</b>	<b>7,510</b>	<b>4,850</b>	<b>2,740</b>	<b>-35%</b>	<b>56%</b>	<b>77%</b>
Fee income	3,010	4,320	1,480	1,740	-66%	-51%	-15%
Capital gains	90	3,190	3,370	1,000	6%	3644%	237%
<b>Total income pre loan loss provision</b>	<b>14,849</b>	<b>23,145</b>	<b>21,109</b>	<b>19,337</b>	<b>-9%</b>	<b>42%</b>	<b>9%</b>
<b>Operating expenses</b>	<b>11,672</b>	<b>15,275</b>	<b>12,191</b>	<b>10,677</b>	<b>-20%</b>	<b>4%</b>	<b>14%</b>
<b>Preprovision profit</b>	<b>3,177</b>	<b>7,870</b>	<b>8,918</b>	<b>8,660</b>	<b>13%</b>	<b>181%</b>	<b>3%</b>
<b>Core PPOP</b>	<b>3,087</b>	<b>4,680</b>	<b>5,548</b>	<b>7,660</b>	<b>19%</b>	<b>80%</b>	<b>-28%</b>
<b>Provisions</b>	<b>12,808</b>	<b>6,790</b>	<b>7,641</b>	<b>5,973</b>	<b>13%</b>	<b>-40%</b>	<b>28%</b>
Profit before tax	-9,630	1,080	1,277	2,686	18%	-113%	-52%
Tax	-3,457	358	340	672	-5%	-110%	-49%
<b>Net profit</b>	<b>-6,174</b>	<b>722</b>	<b>937</b>	<b>2,015</b>	<b>30%</b>	<b>-115%</b>	<b>-54%</b>
<b>Key balance sheet items (Rs mn)</b>							
<b>Deposits</b>	<b>662,260</b>	<b>651,080</b>	<b>698,320</b>	<b>667,357</b>	<b>7%</b>	<b>5%</b>	<b>5%</b>
CASA		206,610	234,910	217,851			8%
CASA Ratio (%)	15%	32%	34%	33%			
<b>Advances</b>	<b>900,098</b>	<b>860,638</b>	<b>856,863</b>	<b>796,436</b>	<b>0%</b>	<b>-5%</b>	<b>8%</b>
<b>Key analytics</b>							
<b>NIM (calc)</b>	<b>3.16</b>	<b>4.60</b>	<b>4.96</b>	<b>5.00</b>			
Cost/Income (ex capital gains) (%)	79%	77%	69%	58%			
Credit costs (%)	5.69	3.16	3.57	3.00			
<b>Asset quality</b>							
Gross NPA	24,186	22,796	17,417	30,121	-24%	-28%	-42%
Gross NPA (%)	2.7	2.6	2.0	3.7			
Net NPA	12,151	8,086	4,366	10,464	-46%	-64%	-58%
Net NPA (%)	1.3	0.9	0.5	1.3			
Coverage ratio (%)	49.8	64.5	74.9	65.3			

Source: Company data, Goldman Sachs Global Investment Research

IDFB.BO	12m Price Target: <b>Rs18.00</b>	Price: <b>Rs27.85</b>	Downside: <b>35.4%</b>		
<b>Sell</b>  Market cap: Rs134.0bn / \$1.8bn 3m ADTV: NA India India Financials M&A Rank: 3	<b>GS Forecast</b>				
	Net inc. (Rs mn)	3/20	3/21E	3/22E	3/23E
	EPS (Rs)	(28,636.0)	347.2	8,811.1	11,805.0
	EPS growth (%)	(5.95)	0.07	1.83	2.45
	P/E (X)	(46.4)	101.2	2,437.7	34.0
	P/B (X)	NM	NM	15.2	11.3
	ROA (%)	1.3	0.9	0.8	0.8
	ROE (%)	(1.8)	0.0	0.6	0.7
	Price/PPOP (X)	(17.1)	0.2	5.6	7.1
	Dividend yield (%)	6.1	4.4	4.1	3.3
EPS (Rs)	3/20	6/20E	9/20E	12/20E	
	0.15	0.42	(0.36)	(0.36)	

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 28 Jul 2020 close.

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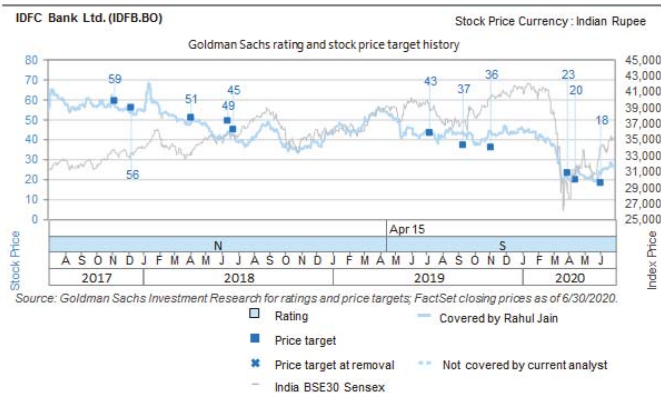
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