

Viewpoint

IndusInd's proposed acquisition of Bharat Financial to be value accretive

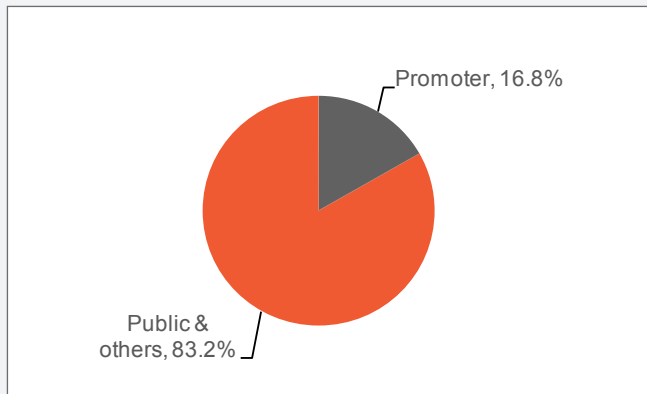
IndusInd Bank

View: Positive | CMP: Rs1,742

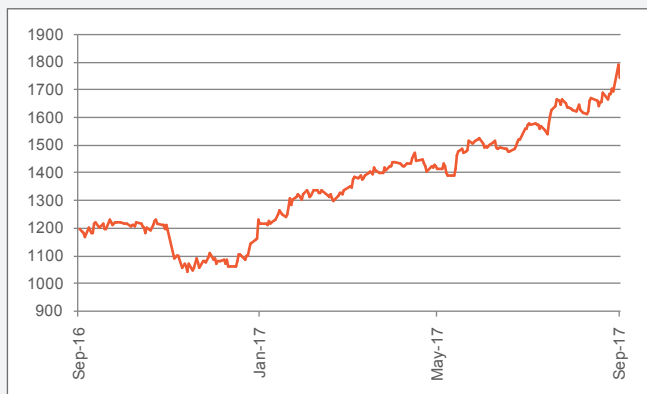
Company details

Market cap:	Rs104,283 Cr
52-week high/low:	Rs1818/1038
NSE volume: (No of shares)	9.7 lakh
BSE code:	532187
NSE code:	INDUSINDBK
Sharekhan code:	INDUSINDBK
Free float: (No of shares)	50.89 Cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	10.2	17.8	34.6	47.7
Relative to Sensex	7.8	14.8	21.0	31.7

Key points

- IndusInd Bank planning to acquire Bharat Financial Inclusion Services:** IndusInd Bank (IIB) has entered into an exclusivity agreement with Bharat Financial Inclusion Services (BFIN) to evaluate the possibility of a strategic deal (read takeover by IIB) between them. IIB's management indicated that the due diligence is presently on and a final decision is likely around a month's time. We believe the swap ratio will be an important thing to look at. Since our earlier update on the same issue (published in March 2017), IIB's share price has increased and, hence, presently the probable valuation is likely to be more favourable to IIB's shareholders. As per media reports, IIB will be exploring a share swap deal, wherein BFIN could be valued at Rs.13,000 crore-14,500 crore. At this valuation, the additional issue of IIB's shares to existing shareholders of BFIN could result in 12%-13.5% expansion in the equity capital of IIB (the merged entity), which we believe is better suited for IIB's shareholders.
- Outlook:** We believe the possible merger with BFIN would bring synergy benefits for IIB, like acquisition of high-yielding loans, enhanced priority sector lending and capital release from BFIN for the merged entity. However, these synergy benefits would accrue in the medium to long term.
- Valuation:** IIB currently trades at 3.9x FY2019E Price-to-Book Value (P/BV), which we feel is reasonable for a bank in a high growth phase with high ROE, ROA and excellent asset quality. IIB's resilient asset quality is a key positive and a distinct differentiator among peers. We maintain our Positive stance and expect a potential 10-12% upside from current levels.
- Significant synergy benefits may accrue due to the acquisition:** The acquisition has several strategic benefits that will be positive for the combined entity. BFIN currently has NIM of 9.1% (Q1FY2018) and financial cost (CoF) of 7.5%, which compared to IIB's CoF of 5.32% (for Q1FY2018) is significantly higher, and the reduction of which will aid to profitability as well as sustainable growth. Not only that, presently, BFIN is regulated under MFI rules, which put several restrictions on loan size, category of

borrowers, size of cash transactions apart from a spread cap and disallowing more than two MFIs to lend to a single borrower simultaneously. We believe, by being part of a bank, BFIN will benefit from greater operational flexibility, which should help growth and boost margins.

- ◆ **However, marginal dilution in asset quality is possible:** IIB has been consistently delivering value to its shareholders over recent times. The bank's high return ratios as well as strong asset

quality (Q1FY2018 GNPA and NNPA at 1.09% and 0.44%, respectively; net credit cost at 59BPS for FY2017) are in stark contrast to the dismal banking sector scenario and a strong indicator of the quality of IIB's balance sheet. However, we believe the merged entity may witness higher credit risk in the near term. BFIN's GNPA's (non AP) have of late jumped to ~6% of its loan book (Q1FY2018) and may remain elevated in the near to medium term, thereby impacting overall book quality of the merged entity.

Scenario analysis

Particulars	At Rs.900	At Rs.950	At Rs.1,000	At Rs.1,050	At Rs.1,100
BFIN CMP	900	950	1,000	1,050	1,100
IIB No. of PU Equity Shares (crore)	667.89	671.75	675.60	679.45	683.31
IIB % Dilution	11.5%	12.2%	12.8%	13.5%	14.1%

Valuations

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net Interest Income	3,420	4,517	6,063	7,986	10,354
Growth %	18%	32%	34%	32%	30%
PAT	1,794	2,286	2,868	3,674	4,708
Growth %	27%	27%	25%	28%	28%
EPS	33.9	38.4	48.2	61.7	79.1
BVPS	193.7	291.0	340.6	386.8	457.2
PE (x)	51.4	45.3	36.1	28.2	22.0
PBV (x)	9.0	6.0	5.1	4.5	3.8

Profit and loss statement

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net interest income	3420	4517	6063	7986	10354
Non-interest income	2404	3297	4171	5045	6151
Net total income	5824	7814	10234	13032	16505
Operating expenses	2726	3672	4783	6247	7992
Pre-provisioning profit	3098	4141	5451	6785	8514
Provisions	389	672	1091	1260	1434
Profit before tax	2709	3469	4360	5525	7079
Tax	915	1183	1492	1851	2372
Profit after tax	1794	2286	2868	3674	4708

Balance sheet

Particulars	FY15	FY16	FY17	FY18E	FY19E
Liabilities					
Networth	10,645	17,696	20,646	23,396	27,581
Deposits	74,134	93,000	126,572	155,684	191,491
Borrowings	20,618	24,996	22,454	31,137	38,298
Other liabilities & provisions	6,390	7,205	8,976	6,393	8,011
Total liabilities	111,787	142,897	178,648	216,609	265,381
Assets					
Cash & balances with RBI	4,035	4,521	7,749	12,766	15,702
Balances with banks & money at call	6,744	5,591	10,880	6,164	6,472
Investments	22,878	34,054	36,702	49,224	60,540
Advances	68,788	88,419	113,081	141,351	176,688
Fixed assets	1,158	1,255	1,332	1,519	1,671
Other assets	8,184	9,056	8,905	5,585	4,308
Total assets	111,787	142,897	178,648	216,609	265,381

Key Ratios					Rs cr
Particulars	FY15	FY16	FY17	FY18E	FY19E
Per share Data (Rs)					
Earnings	33.9	38.4	48.2	61.7	79.1
Dividend	4.0	4.5	6.0	5.9	7.5
Book value	193.7	291.0	340.6	386.8	457.2
Adj. book value	189.7	285.6	332.0	382.2	452.9
Spreads (%)					
Yield on Advances	12.5	11.8	11.4	11.2	11.0
Cost of Deposits	7.7	6.8	6.7	5.7	5.6
Net interest margins	3.7	4.0	4.3	4.5	4.7
Operating ratios (%)					
Credit to Deposit	92.8	95.1	89.3	90.8	92.3
Cost to income	46.8	47.0	46.7	47.9	48.4
CASA	34.1	35.2	36.9	37.5	38.1
Non interest income / Total income	41.3	42.2	40.8	38.7	37.3
Return ratios (%)					
RoE	18.2	16.1	16.2	16.7	18.5
RoA	1.6	1.6	1.6	1.7	1.8
Asset quality ratios (%)					
Gross NPA	0.8	0.9	0.9	1.1	1.2
Net NPA	0.3	0.4	0.4	0.2	0.1
Growth Ratios (%)					
Net interest income	18.3	32.1	34.2	31.7	29.6
Pre-provisioning profit	19.3	33.7	31.6	24.5	25.5
Profit after tax	27.4	27.5	25.4	28.1	28.1
Advances	24.8	28.5	27.9	25.0	25.0
Deposits	22.5	25.4	36.1	23.0	23.0
Valuation ratios (x)					
P/E (x)	51.4	45.3	36.1	28.2	22.0
P/BV (x)	9.0	6.0	5.1	4.5	3.8
P/ABV (x)	9.2	6.1	5.2	4.6	3.8

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