

## ICICI Bank

STOCK INFO. BLOOMBERG  
BSE Sensex: 8,377 ICICIBC IN  
REUTERS CODE  
S&P CNX: 2,537 ICBK.BO

13 October 2005

Neutral

Previous Recommendation: Neutral

Rs526

Equity Shares (m)	736.8
52-Week Range (Rs)	616/278
1,6,12 Rel.Perf.(%)	-1/-2/35
M.Cap. (Rs b)	387.2
M.Cap. (US\$ b)	8.6

YEAR	NET INCOME	PAT	EPS	EPS	P/E	P/BV	CAR	ROAE	ROAA	P/ABV
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	(%)	(X)
3/05A	62,552	20,052	27.2	2.5	19.3	3.1	11.8	19.5	1.4	3.4
3/06E	85,181	24,507	28.0	2.7	18.8	2.2	14.0	14.5	1.2	2.3
3/07E	107,472	31,450	35.9	28.3	14.7	2.0	13.5	14.1	1.2	2.1

ICICI Bank continued to witness strong growth in its core business, with loan growth of 56% and deposit growth of 68% in 2QFY06. NII grew 39%, while core fee income grew 31%. Overall, margins remained stable at 2.4%, with growth driven by volumes for both fund as well as non-fund segments. With Dabhol going off from the book of ICICI Bank, both gross as well as net NPAs witnessed a sharp improvement. Net NPAs now stand at 0.97%.

- Strong balance sheet expansion – retail drives growth
- NIMs constant at 2.4%, fee growth steady
- Asset quality improves sharply, as Dabhol gets settled
- Raising capital to support future growth

While we expect margins to remain stable, we believe that strong volume growth coupled with strong traction in fee revenues will drive earnings growth for the bank. Improving performance of its subsidiaries will act as a key valuation driver for the bank. However, the near-term stock performance is likely to be driven by the forthcoming equity issuance and the issue price. The additional capital would result in depressed RoE for FY06 and FY07. However, since the issue would happen at 2.7-2.8x FY06E BV (pre-issue), it would be book value accretive. The stock trades at 18.8x FY06E EPS and 2.2x FY06E book value. We maintain our **Neutral** rating.

QUARTERLY PERFORMANCE										(RS MILLION)
Y/E MARCH	FY05				FY06				FY05	FY06E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Interest Income	21,958	22,305	23,784	26,052	29,978	32,133	32,346	35,848	94,099	130,304
Interest Expense	15,652	15,453	16,452	18,151	21,465	22,598	22,375	24,800	65,709	91,238
<b>Net Interest Income</b>	<b>6,306</b>	<b>6,852</b>	<b>7,332</b>	<b>7,901</b>	<b>8,512</b>	<b>9,535</b>	<b>9,971</b>	<b>11,048</b>	<b>28,390</b>	<b>39,066</b>
Growth (%)	38.7	45.1	42.8	44.4	35.0	39.2	36.0	39.8	42.9	37.6
Other Income	6,577	8,354	8,907	10,323	10,905	11,115	11,200	12,895	34,161	46,115
<b>Net Income</b>	<b>12,883</b>	<b>15,206</b>	<b>16,239</b>	<b>18,224</b>	<b>19,417</b>	<b>20,650</b>	<b>21,171</b>	<b>23,943</b>	<b>62,552</b>	<b>85,181</b>
Operating Expenses	7,324	7,688	8,527	9,452	9,710	10,210	10,600	10,916	32,991	41,435
<b>Operating Profit</b>	<b>5,558</b>	<b>7,518</b>	<b>7,712</b>	<b>8,772</b>	<b>9,708</b>	<b>10,440</b>	<b>10,571</b>	<b>13,027</b>	<b>29,560</b>	<b>43,746</b>
Growth (%)	10.2	8.5	13.2	45.6	74.7	38.9	37.1	48.5	19.1	48.0
Provisions and Contingencies	458	1,947	1,082	800	2,979	3,038	2,600	2,883	4,288	11,500
<b>Profit before tax</b>	<b>5,100</b>	<b>5,571</b>	<b>6,630</b>	<b>7,971</b>	<b>6,729</b>	<b>7,402</b>	<b>7,971</b>	<b>10,144</b>	<b>25,272</b>	<b>32,246</b>
Provision for Taxes	793	1,150	1,453	1,824	1,429	1,602	1,833	2,875	5,220	7,739
<b>Net Profit</b>	<b>4,307</b>	<b>4,421</b>	<b>5,177</b>	<b>6,147</b>	<b>5,300</b>	<b>5,800</b>	<b>6,138</b>	<b>7,269</b>	<b>20,052</b>	<b>24,507</b>
Growth (%)	26.6	10.1	17.6	35.0	23.0	31.2	18.6	18.3	22.5	22.2
Interest Expense/Interest Income (%)	71.3	69.3	69.2	69.7	71.6	70.3	69.2	69.2	69.8	70.0
Other Income/Net Income (%)	51.1	54.9	54.9	56.6	56.2	53.8	52.9	53.9	54.6	54.1
Cost /Income (%)	56.9	50.6	52.5	51.9	50.0	49.4	50.1	45.6	52.7	48.6

E: Inquire Estimates

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### Strong balance sheet expansion – retail drives growth

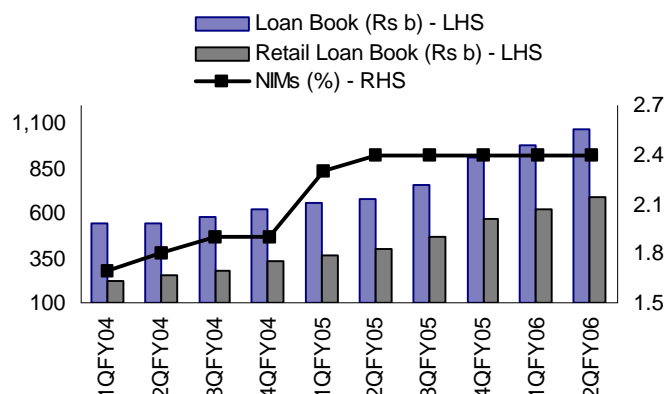
ICICI Bank has grown its balance sheet aggressively by 43% YoY and 4.4% QoQ to Rs1,892b. This has been fuelled by aggressive deposit raising and strong growth in loans (mainly fuelled by retail). While the bank has started to witness traction in its corporate loans, it is still the retail loans that are fuelling loan growth for the bank. Retail loans have increased by 73% YoY. The proportion of retail has increased to 64% of total loans and 61% of customer assets.

In order to support this strong loan growth, the bank is aggressively growing its deposit base. Overall deposit base has increased by 68% YoY and 6% QoQ. The deposit costs on a YoY basis have gone up from 4.4% to 4.9%. However, the bank has also raised rates for housing and auto loans (both constitute nearly 50% of the loan book) over the last six months. On account of better yields on the loan book, it has been able to sustain margins at 2.4%.

### NIMs constant at 2.4%

Net interest margins (NIMs) have remained flat for ICICI Bank over the last five quarters at 2.4%. This is despite an improving asset yield for the bank. ICICI Bank is focused on volumes, which is turn is resulting in higher deposit cost (CASA for the bank is just 23%), as it needs to raise resources aggressively to support loan growth. We believe that NII will remain a function of volumes over the next few quarters. Even as yields expand (the bank has raised 50bp on its floating rate home loans effective from July 2005 and on auto loans from June 2005), the higher deposit cost will result in margins being steady at current levels.

QUARTERLY TREND OF LOAN BOOK AND RETAIL LOANS



Source: Company/Motilal Oswal Securities

### Securitization has been a regular feature

The bank has securitized Rs50b of retail assets during the quarter, which has generated gains of Rs1.72b (18% of NII). Securitization has been a regular feature and ICICI Bank has consistently been deriving 15-19% of its revenues from securitization over the last six quarters.

SECURITIZATION A REGULAR CONTRIBUTOR TO NII (RS M)

	JUN-04	SEP-04	DEC-04	MAR-05	JUN-05	SEP-05
<b>Assets</b>						
Securitized	30,000	46,000	52,000	46,000	25,000	50,000
Gains in NII	1,200	1,300	1,400	1,200	1,447	1,716
<b>Sec Income</b>						
as a % of NII	19.0	19.0	19.1	15.2	17.0	18.0
NII	6306	6852	7332	7901	8512	9535
Growth (%)	38.7	45.1	42.8	44.4	35.0	39.2
<b>NII less</b>						
Securitisation	5,106	5,552	5,932	6,701	7,065	7,819
Growth (%)					38.4	40.8

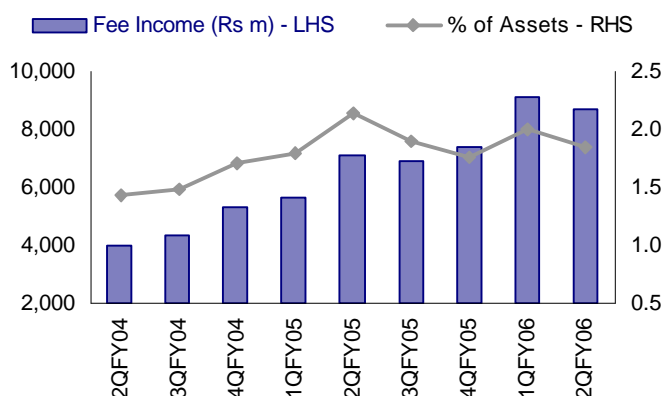
Source: Company/Motilal Oswal Securities

### Fee growth continues to outperform

A key highlight for ICICI Bank is the continued traction in its core fee revenues. Fees (non interest non treasury) to total assets are now at 1.8%. In 2QFY05, core fees increased by 31% to Rs7.04b, while other non fund income (dividend income, asset management income, etc) declined marginally by 5% YoY. Nearly 60% of the fees are from retail. Further, 10% of the fees come from its international operations. With a strong fee focus, we expect the growth in fee income to remain strong for the bank, going forward.

The bank has managed to grow its income from treasury by 95% to Rs2.4b, which has been mainly driven by gains from its eICICI equity portfolio. Equity gains out of the eICICI portfolio were Rs1.1b (gains from sale of shares of IDFC included). Other equity gains were Rs0.6b during the quarter.

#### FEE INCOME – STRONG GROWTH OVER THE LAST FEW QUARTERS

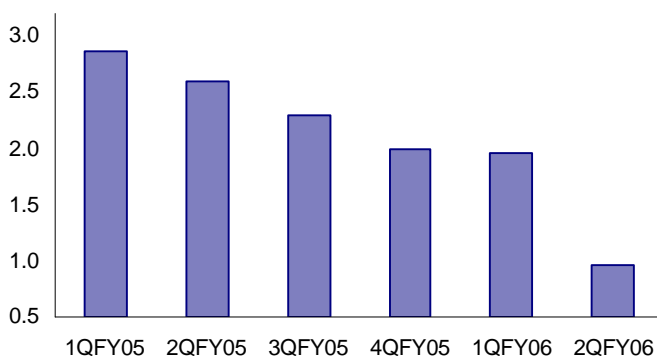


Source: Company/Motilal Oswal Securities

#### Asset quality improves sharply as Dabhol gets resolved

As Dabhol has got off the books of ICICI Bank, both its gross and net NPAs have improved sharply during the quarter. While there are no concrete numbers available, we believe that Dabhol was nearly 20-22% of the total gross NPAs and the bank had provision coverage of 33-35% against it.

#### NET NPAS (%)



Source: Company/Motilal Oswal Securities

Under the Dabhol restructuring, Ratnagiri Gas, a company formed by NTPC and GAIL has taken over Dabhol's assets. Under a court ruling, since the underlying collateral has been sold and the exposure now is towards Ratnagiri Gas, ICICI Bank could treat it as a performing asset.

#### Raising capital to support growth

ICICI Bank would be raising capital to the tune of Rs70b, with a greenshoe option of 15%. While a capital issue was necessary in order to support loan growth and also the investments in its subsidiaries, it has come sooner than market expectations.

In our projections, we have factored in fresh capital of Rs70b, being raised at Rs500 per share, which will result in a 19% dilution.

#### CHANGE IN BV & ROE ESTIMATES DUE TO CAPITAL RAISING

	PRE ISSUE	POST ISSUE
BV (FY06) – Rs	199	242
BV (FY07) – Rs	230	268
RoE (FY06) - %	18.2	14.5
RoE (FY07) - %	19.1	14.1

\* Capital raising of Rs70b, at Rs500 per share

#### Valuation and view

While we expect margins to remain stable, we believe that strong volume growth coupled with strong traction in fee revenues will drive earnings growth for the bank. Improving performance of its subsidiaries will act as a key valuation driver for the bank.

However, the near-term stock performance is likely to be driven by the forthcoming equity issuance and the issue price. The near-term implication of the issue will be depressed RoE for FY06 and FY07. However, since the issue would happen at 2.7-2.8x FY06E BV (pre-issue), it would be book value accretive for ICICI Bank. The stock trades at 18.8x FY06E EPS and 2.2x FY06E book value. We maintain our **Neutral** rating.

## ICICI Bank: an investment profile

### Company description

ICICI Bank was incorporated in 1994 under the leadership of the erstwhile ICICI. Bank of Madura was merged with it during 2001. In 2002, it underwent a reverse merger with its promoter ICICI and emerged as the largest private sector bank in India. This was followed by a fundamental shift in the business profile from project and corporate business towards retail loans. The bank has a balance sheet size of Rs1,677b and has a wide geographical reach with 505 branches and extension counters and over 2,000 internet kiosks spread across the country.

### Key investment arguments

- Robust loan growth with margin stability will result in significant growth in net interest income; fee income is expected to remain buoyant
- Enjoys leadership in most of the retail loan segments
- Subsidiaries hold significant values

### Key investment risks

- Net NPAs have declined below 1%; however higher delinquency may arise on account of robust loan book expansion
- Frequent capital dilution in order to support growth

### Recent developments

- Has approved raising Rs70b capital, along with a green shoe option of 15%. This might result in an equity dilution of 19%.
- Dabhol has been settled, which has resulted in a sharp improvement in asset quality for ICICI Bank.

### Valuation and view

- Robust loan growth, high fee income and reductions in net NPAs will be the key triggers to look for in the stock.
- The stock trades at 18.8x FY06E earnings and 2.3x FY06E adjusted book value.

### Sector view

- Loan growth of 30% at the beginning of capex cycle
- Volatility in interest rates will impact bond gains
- Benefits of significant improvement in asset quality, yet not factored in earnings, valuations
- We maintain an overweight stance on the sector

#### COMPARATIVE VALUATIONS

		ICICI BANK	HDFC BANK	HDFC
P/E (x)	FY06E	18.8	23.8	19.4
	FY07E	14.7	18.0	15.8
P/BV (x)	FY06E	2.2	4.0	5.2
	FY07E	2.0	3.4	4.3
RoE (%)	FY06E	14.5	18.1	29.6
	FY07E	14.1	20.3	30.0
RoA (%)	FY06E	1.2	1.5	2.8
	FY07E	1.2	1.6	2.8

#### SHAREHOLDING PATTERN (%)

	SEP.05	JUN.05	SEP.04
Promoters	0.0	0.0	0.0
Domestic Institutions	17.2	16.8	17.9
FII's/FDIs	72.8	72.6	69.6
Others	10.0	10.6	12.5

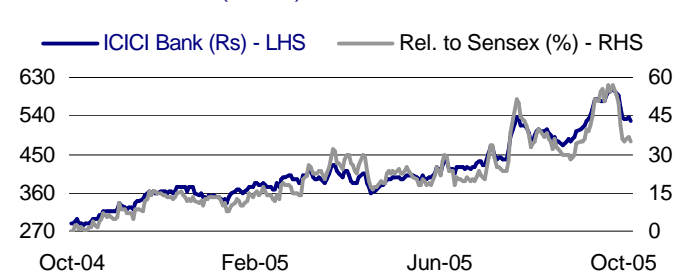
#### EPS: INQUIRE FORECAST VS CONSENSUS (RS)

	INQUIRE FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY06	28.0	33.1	-15.4
FY07	35.9	39.8	-9.8

#### TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
526	-	-	Neutral

#### STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT (Rs Million)					
Y/E MARCH	2003	2004	2005	2006E	2007E
Interest Income	93,681	90,023	94,099	130,304	154,939
Interest Expended	79,440	70,152	65,709	91,238	101,214
<b>Net Int. Income</b>	<b>14,241</b>	<b>19,871</b>	<b>28,390</b>	<b>39,066</b>	<b>53,725</b>
Change (%)	140.1	39.5	42.9	37.6	37.5
Other Income	31,588	30,649	34,161	46,115	53,748
<b>Net Income</b>	<b>45,829</b>	<b>50,520</b>	<b>62,552</b>	<b>85,181</b>	<b>107,472</b>
Operating Expenses	20,117	25,712	32,991	41,435	51,390
<b>Oper. Income</b>	<b>25,712</b>	<b>24,807</b>	<b>29,560</b>	<b>43,746</b>	<b>56,083</b>
Change (%)	371.7	-3.5	19.2	48.0	28.2
Other Provisions	17,908	5,790	4,288	11,500	13,000
<b>PBT</b>	<b>7,804</b>	<b>19,018</b>	<b>25,272</b>	<b>32,246</b>	<b>43,083</b>
Tax	-4,258	2,651	5,220	7,739	11,632
<b>PAT</b>	<b>12,062</b>	<b>16,367</b>	<b>20,052</b>	<b>24,507</b>	<b>31,450</b>
Change (%)	367.0	35.7	22.5	22.2	28.3
Proposed Dividend	4,595	5,441	6,263	7,891	8,768

BALANCE SHEET (Rs Million)					
Y/E MARCH	2003	2004	2005	2006E	2007E
Capital	6,127	6,164	7,368	8,768	8,768
Reserves & Surplus	63,207	73,942	118,132	203,348	226,031
<b>Net Worth</b>	<b>69,333</b>	<b>80,106</b>	<b>125,500</b>	<b>212,116</b>	<b>234,798</b>
<b>Deposits</b>	<b>481,693</b>	<b>681,086</b>	<b>998,188</b>	<b>1,440,183</b>	<b>1,778,220</b>
Borrowings	343,024	307,402	335,445	413,500	503,500
Other Liab & Prov.	170,569	180,195	213,962	242,962	273,962
<b>Total Liabilities</b>	<b>1,068,120</b>	<b>1,252,289</b>	<b>1,676,594</b>	<b>2,312,261</b>	<b>2,793,980</b>
Current Assets	64,890	84,706	129,300	336,408	359,730
Investments	354,623	427,429	504,874	633,745	728,494
<b>Advances</b>	<b>532,794</b>	<b>620,955</b>	<b>914,052</b>	<b>1,175,670</b>	<b>1,502,352</b>
Net Fixed Assets	40,607	40,564	40,380	46,437	53,403
Other Assets	75,205	78,634	87,989	120,000	150,000
<b>Total Assets</b>	<b>1,068,120</b>	<b>1,252,289</b>	<b>1,676,594</b>	<b>2,312,261</b>	<b>2,793,980</b>

KEY ASSUMPTIONS (%)					
Y/E MARCH	2003	2004	2005	2006E	2007E
Deposit Growth	50.1	41.4	46.6	44.3	23.5
Advances Growth	13.3	16.5	47.2	28.6	27.8
Investments Growth	-1.2	20.5	18.1	25.5	15.0
CRR	4.8	4.5	5.0	5.0	5.0
Provision Coverage	43.8	53.3	44.6	50.1	50.0
Dividend	75.0	75.0	85.0	90.0	100.0

E: Most Estimates

RATIOS					
Y/E MARCH	2003	2004	2005	2006E	2007E
<b>Spreads Analysis (%)</b>					
Avg. Yield-Earn. Ass	9.8	8.7	7.0	7.5	7.2
Avg Cost-Int. Bear. L	8.3	6.9	5.2	5.3	4.5
Interest Spread	1.5	1.8	1.9	2.2	2.7
Net Interest Margin	1.5	1.9	2.1	2.3	2.5

Profitability Ratios (%)					
RoE	18.3	21.9	19.5	14.5	14.1
RoA	1.1	1.4	1.4	1.2	1.2
Int. Exp./Int. Earned	84.8	77.9	69.8	70.0	65.3
Other Inc./Net Inc.	68.9	60.7	54.6	54.1	50.0

Efficiency Ratios (%)					
Op Exp/Net Income	43.9	50.9	52.7	48.6	47.8
Empl. Cost/Op. Exp.	20.0	21.2	22.4	25.0	26.3
Business/Empl. (Rs)	123.7	95.7	106.2	113.7	121.5
NP/Empl. (Rs lac)	14.7	12.0	11.1	10.7	11.6

Asset Liability Profile (%)					
Adv./Dep. Ratio	110.6	91.2	91.6	81.6	84.5
Invest./Dep. Ratio	73.6	62.8	50.6	44.0	41.0
Gross NPAs to Adv	8.0	4.2	2.7	1.8	1.8
Net NPAs to Cust.	5.2	2.0	1.5	0.9	0.9
CAR	11.1	10.4	11.8	14.0	13.5
Tier 1	7.1	6.1	7.6	9.6	8.5

Valuation					
Book Value (Rs)	113.2	130.0	170.3	241.9	267.8
Price-BV (x)	4.6	4.0	3.1	2.2	2.0
Adjusted BV (Rs)	77.9	115.0	156.8	231.3	254.9
Price-ABV (x)	6.7	4.6	3.4	2.3	2.1
EPS (Rs)	19.7	26.6	27.2	28.0	35.9
EPS Growth	367.3	34.9	2.5	2.7	28.3
Price Earnings (x)	26.7	19.8	19.3	18.8	14.7
OPS (Rs)	42.0	40.2	40.1	49.9	64.0
Price-OP (x)	12.5	13.1	13.1	10.5	8.2

E: Most Estimates

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2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
MOST is not engaged in providing investment-banking services.	



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