Yes Bank YESB.NS YES IN

BANKS

NOMURA
EQUITY RESEARCH

Upgrade to Buy with TP of INR615

New branch licenses to boost CASA growth, drive strong NIM expansion

January 28, 2013

Rating Up from Neutral	**Buy**
Target price Increased from 425	INR 615
Closing price January 24, 2013	INR 508
Potential upside	+21.1%

Action: Upgrade to Buy on expected inflection in CASA growth led by large sanction in new branch licenses; TP revised up to INR615

We upgrade Yes Bank to Buy from Neutral and increase our TP to INR615 from INR425. We believe a recent grant of 146 new branch licenses improves the outlook significantly for savings account traction going forward and underscores the RBI's appreciation of the bank's growth trajectory. We highlight how the RBI's grant of a high number of tier-1 licenses has typically preceded RoA improvement for other private sector banks (Figures 7 to 11). We expect Yes's licenses (which pertain to tier-1 cities) to get implemented over next 18months and improve the bank's CASA ratio to 26% for FY15F from 18.3% as of Q3FY13. We expect this improvement to structurally improve the NIM to 3.45% by FY15F from 2.95% for FY13F. We believe this should drive a 15-20bp RoA improvement over next two years, despite an expected marginal increase in both opex and loan loss provisions. Although we hike our FY14F LLP estimate to 34bps, we expect lower stress on asset quality going forward given the rate cycle outlook and Yes's proactive risk management so far. Although we have built in a 10-15bp hike in the cost-asset ratio over next two years, we think the bank is creating operating leverage and will be able to use it from FY15 onwards.

Catalyst: Strong uptick in CASA deposits, stable asset quality

Valuation: Upgrading to Buy; TP raised to INR615

Our TP increases to INR615 from INR425 as we roll forward to FY14F, increase our FY14F earnings estimate by 12% and factor in 12% in equity dilution in H1FY14F. We retain our 1-yr fwd P/ABV multiple of 2.7x for FY14F adj. RoE of 21.6% and RoA of 1.6%.

31 Mar	FY12		FY13F		FY14F		FY15F
Currency (INR)	Actual	Old	New	Old	New	Old	New
PPOP (mn)	15,402	20,322	20,677	24,989	27,266	30,719	34,424
Reported net profit (mn)	9,770	12,496	12,583	14,755	16,000	17,926	20,043
Normalised net profit (mn)	9,770	12,496	12,583	14,755	16,000	17,926	20,043
FD normalised EPS	27.23	36.32	34.62	42.89	40.28	52.10	49.16
FD norm. EPS growth (%)	34.2	27.9	27.1	18.1	16.4	21.5	22.0
FD normalised P/E (x)	18.6	N/A	14.7	N/A	12.6	N/A	10.3
Price/adj. book (x)	3.9	N/A	3.2	N/A	2.2	N/A	1.9
Price/book (x)	3.8	N/A	3.1	N/A	2.2	N/A	1.9
Dividend yield (%)	0.8	N/A	1.0	N/A	1.3	N/A	1.5
ROE (%)	23.1	24.0	24.1	23.2	21.3	23.4	19.9
ROA (%)	1.5	1.5	1.5	1.5	1.6	1.5	1.7

Source: Company data, Nomura estimates

Key company data: *See page 2 for company data and detailed price/index chart.*

Anchor themes

Expect strong CASA momentum and shft tin loan book mix to drive earnings trajectory

Nomura vs consensus

Our PAT is in-line with consensus for FY14F. We are building in LLPs of 34bps for FY14F.

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See Appendix A-1 for analyst certification, important disclosures and the status of non-US analysts.

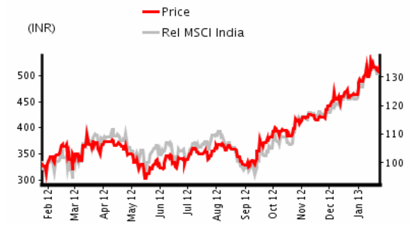
Key data on Yes Bank

Profit and Loss (INRmn)

Year-end 31 Mar	FY11	FY12	FY13F	FY14F	FY15F
Interest income	40,417	63,074	82,475	100,183	120,632
Interest expense	-27,948	-46,917	-60,350	-69,887	-82,198
Net interest income	12,469	16,156	22,125	30,296	38,435
Net fees and commissions	5,984	6,744	9,384	11,370	13,730
Trading related profits	1,018	1,828	2,433	2,822	3,373
Other operating revenue	-769	-1	-2	0	0
Non-interest income	6,233	8,571	11,816	14,192	17,103
Operating income	18,702	24,728	33,941	44,488	55,538
Depreciation	0	0	0	0	0
Amortisation	0	0	0	0	0
Operating expenses	-3,175	-4,574	-6,445	-7,725	-9,666
Employee share expense	-3,623	-4,752	-6,819	-9,497	-11,447
Op. profit before provisions	11,904	15,402	20,677	27,266	34,424
Provisions for bad debt	-359	-116	-1,597	-1,758	-2,293
Other provision charges	-623	-786	-342	-892	-1,296
Operating profit	10,922	14,500	18,738	24,615	30,835
Other non-operating income	0	0	0	0	0
Associates & JCEs	0	0	0	0	0
Pre-tax profit	10,922	14,500	18,738	24,615	30,835
Income tax	-3,650	-4,730	-6,156	-8,615	-10,792
Net profit after tax	7,271	9,770	12,583	16,000	20,043
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	7,271	9,770	12,583	16,000	20,043
Extraordinary items	0	0	0	0	0
Reported NPAT	7,271	9,770	12,583	16,000	20,043
Dividends	-1,012	-1,641	-2,208	-2,995	-3,752
Transfer to reserves	6,259	8,129	10,374	13,005	16,291
Valuation and ratio analysis					
Reported P/E (x)	24.1	18.2	14.4	12.4	10.2
Normalised P/E (x)	24.1	18.2	14.4	12.4	10.2
FD normalised P/E (x)	25.0	18.6	14.7	12.6	10.3
FD normalised P/E at price target (x)	30.3	22.6	17.8	15.3	12.5
Dividend yield (%)	0.5	0.8	1.0	1.3	1.5
Price/book (x)	4.6	3.8	3.1	2.2	1.9
Price/adjusted book (x)	4.8	3.9	3.2	2.2	1.9
Net interest margin (%)	2.88	2.68	2.93	3.26	3.45
Yield on interest earning assets (%)	9.32	10.46	10.90	10.79	10.81
Cost of interest bearing liabilities (%)	6.64	8.09	8.35	7.90	7.81
Net interest spread (%)	2.68	2.37	2.56	2.89	3.01
Non-interest/operating income (%)	33.3	34.7	34.8	31.9	30.8
Cost to income (%)	36.3	37.7	39.1	38.7	38.0
Effective tax rate (%)	33.4	32.6	32.9	35.0	35.0
Dividend payout (%)	13.9	16.8	17.6	18.7	18.7
ROE (%)	21.1	23.1	24.1	21.3	19.9
ROA (%)	1.52	1.47	1.52	1.59	1.66
Operating ROE (%)	31.7	34.2	35.8	32.7	30.6
Operating ROA (%)	2.29	2.19	2.27	2.44	2.55
Growth (%)					
Net interest income	60.1	29.6	36.9	36.9	26.9
Non-interest income	6.6	37.5	37.9	20.1	20.5
Non-interest expenses	30.5	44.1	40.9	19.9	25.1
Pre-provision earnings	37.9	29.4	34.2	31.9	26.3
Net profit	52.2	34.4	28.8	27.2	25.3
Normalised EPS	34.6	32.2	26.8	16.1	22.0
Normalised FDEPS	36.4	34.2	27.1	16.4	22.0

Source: Company data, Nomura estimates

Relative performance chart (one year)



Source: ThomsonReuters, Nomura research

(%)	1M	3M	12M
Absolute (INR)	10.0	27.2	59.0
Absolute (USD)	12.6	27.1	48.0
Relative to index	7.6	20.5	41.5
Market cap (USDmn)	3,325.8		
Estimated free float (%)	68.9		
52-week range (INR)	545/285		
3-mth avg daily turnover (USDmn)	19.77		
Major shareholders (%)			
Madhu Kapoor	10.0		

Source: Thomson Reuters, Nomura research

Notes

Balance Sheet (INRmn)

As at 31 Mar	FY11	FY12	FY13F	FY14F	FY15F	Notes
Cash and equivalents	30,760	23,325	26,113	31,713	38,900	
Inter-bank lending	4,200	12,530	2,720	3,258	3,921	
Deposits with central bank	0	0	0	0	0	
Total securities	188,288	277,573	373,342	449,521	533,641	
Other interest earning assets	0	0	0	0	0	
Gross loans	344,350	380,550	467,807	565,017	683,549	
Less provisions	-714	-664	-1,136	-2,777	-4,837	
Net loans	343,636	379,886	466,671	562,240	678,712	
Long-term investments	0	0	0	0	0	
Fixed assets	1,324	1,771	2,631	3,931	5,231	
Goodwill	0	0	0	0	0	
Other intangible assets	0	0	0	0	0	
Other non IEAs	21,861	41,535	42,169	50,243	60,177	
Total assets	590,070	736,621	913,647	1,100,907	1,320,581	
Customer deposits	459,389	491,517	602,124	735,867	918,784	
Bank deposits, CDs, debentures	33,330	93,432	140,629	140,629	140,629	
Other interest bearing liabilities	33,579	48,133	70,171	80,171	90,171	
Total interest bearing liabilities	526,298	633,082	812,924	956,667	1,149,584	
Non interest bearing liabilities	25,831	56,773	42,948	51,460	61,927	
Total liabilities	552,129	689,855	855,871	1,008,127	1,211,511	
Minority interest	0	0	0	0	0	
Common stock	3,471	3,530	3,576	4,007	4,007	
Preferred stock	0	0	0	0	0	
Retained earnings	34,469	43,236	54,200	88,773	105,064	
Reserves for credit losses	0	0	0	0	0	
Proposed dividends	0	0	0	0	0	
Other equity	0	0	0	0	0	
Shareholders' equity	37,941	46,766	57,776	92,780	109,071	
Total liabilities and equity	590,070	736,621	913,647	1,100,908	1,320,582	
Non-performing assets (INR)	805	839	1,516	3,713	6,373	
Balance sheet ratios (%)						
Loans to deposits	75.0	77.4	77.7	76.8	74.4	
Equity to assets	6.4	6.3	6.3	8.4	8.3	
Asset quality & capital						
NPAs/gross loans (%)	0.2	0.2	0.3	0.7	0.9	
Bad debt charge/gross loans (%)	0.10	0.03	0.34	0.31	0.34	
Loss reserves/assets (%)	0.12	0.09	0.12	0.25	0.37	
Loss reserves/NPAs (%)	88.6	79.2	74.9	74.8	75.9	
Tier 1 capital ratio (%)	9.7	9.9	9.3	11.9	11.6	
Total capital ratio (%)	16.5	17.9	18.3	20.6	19.8	
Growth (%)						
Loan growth	54.8	10.5	22.8	20.5	20.7	
Interest earning assets	62.1	25.0	25.8	20.4	19.8	
Interest bearing liabilities	66.8	20.3	28.4	17.7	20.2	
Asset growth	62.2	24.8	24.0	20.5	20.0	
Deposit growth	71.4	7.0	22.5	22.2	24.9	
Per share						
Reported EPS (INR)	21.06	27.84	35.31	41.01	50.02	
Norm EPS (INR)	21.06	27.84	35.31	41.01	50.02	
Fully diluted norm EPS (INR)	20.29	27.23	34.62	40.28	49.16	
DPS (INR)	2.42	3.93	5.19	6.45	7.87	
PPOP PS (INR)	34.48	43.89	58.02	69.88	85.91	
BVPS (INR)	109.29	132.49	161.58	231.55	272.20	
ABVPS (INR)	106.24	128.61	157.76	228.14	268.79	
NTAPS (INR)	109.29	132.49	161.58	231.55	272.20	

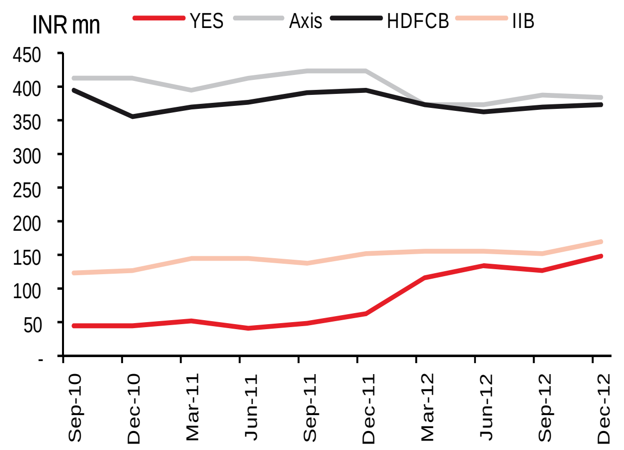
Source: Company data, Nomura estimates

We expect a 65% increase in tier-1 licenses to drive savings account inflection

We believe the grant of 146 new licenses (compared to 59 given in the previous tranche in Nov 11) alters the landscape completely for Yes Bank's network expansion trajectory. These licenses imply a 65% increase over Yes Bank's current number of tier-1 branches (219 as of Dec 12 out of 413 overall branches) and should greatly increase the bank's penetration in these CASA-rich centers. We expect Yes to execute these 146 new licenses, along with 60-70 tier-2 to -6 branches, over the next 18-21 months, taking the bank close to 700 branches by Mar 15 from 412 at present. We change our savings deposit per branch (lagged by 1 year) assumption to INR220mn for FY14F from INR171mn earlier and consequently our CASA ratio estimate moves up to 23.6% for FY14F from 21% earlier. We expect CASA ratio improvement to structurally drive NIMs higher and we revise our FY14F NIM estimate to 3.3% from 3.2% earlier.

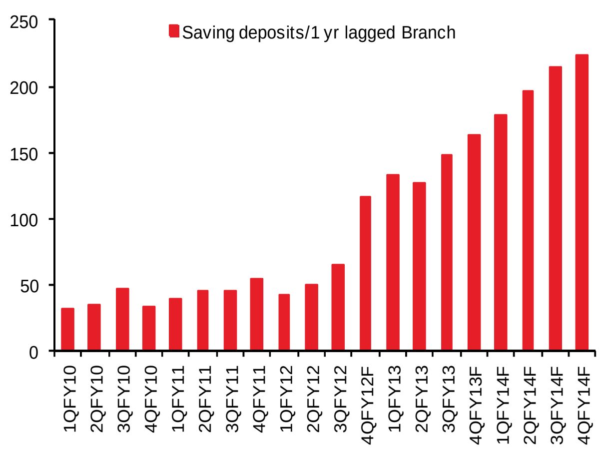
Helped by savings rate deregulation, Yes bank has inched up closer to IndusInd Bank's savings deposit per branch ratio (Fig-1) over the last few quarters. We believe these new licenses will help determine the trajectory to the next level – where Axis and HDFC Bank currently operate. We highlight how the annual growth in tier-1 branches impacts the savings deposit per branch ratio for private sector banks (Figures 3 to 6). As is evident, a 30% plus y-y increase in tier-1 branches from FY02 to FY05 helped improve the SA (savings deposit) ratio for both HDFC and Axis Bank. In FY11 and FY12, a similar growth helped both IndusInd and Yes Banks to improve their SA ratio, and given that we expect these licenses to imply 40% plus growth in FY14F and FY15F in these branches, we expect this ratio to move higher into the INR200-250mn per branch range over next two years.

Fig. 1: SA per 1-yr lagged branch trend comparison



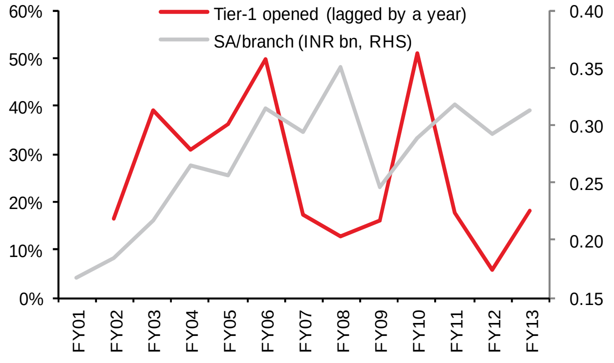
Source: Company data, Nomura estimates

Fig. 2: Yes Bank: SA per 1 yr lagged branch trend



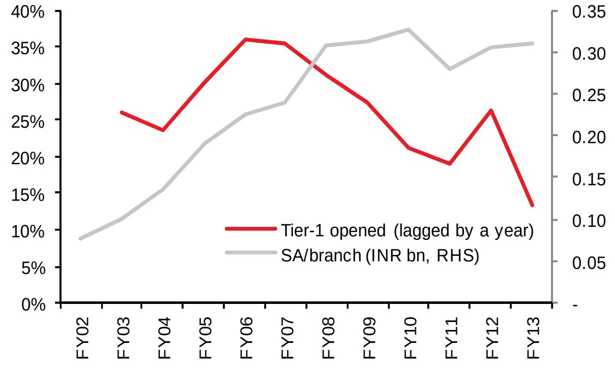
Source: Company data, Nomura estimates

Fig. 3: HDFC Bank: Tier-1 branch addition vs SA/branch



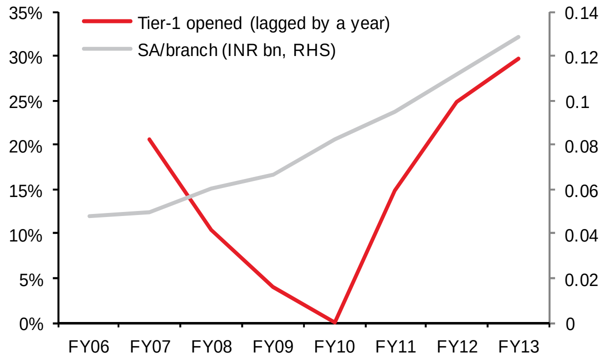
Source: RBI, Company data, Nomura research

Fig. 4: Axis Bank: Tier-1 branch addition vs SA/branch



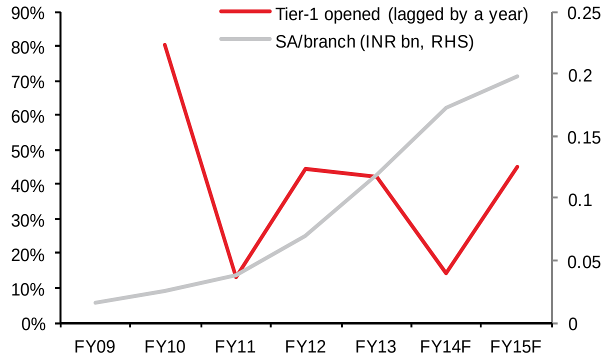
Source: RBI, Company data, Nomura research

Fig. 5: IndusInd Bank: Tier-1 branch addition vs SA/branch



Source: RBI, Company data, Nomura research

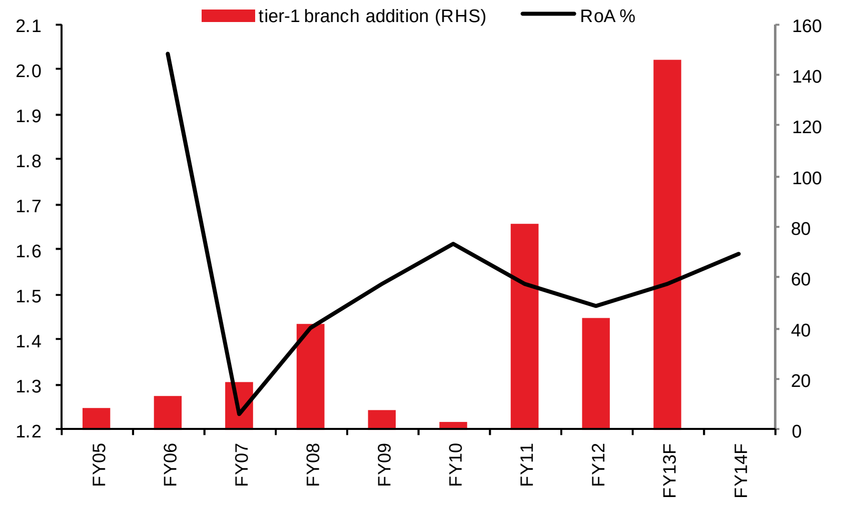
Fig. 6: Yes Bank: Tier-1 branch addition vs SA/branch



Source: RBI, Company data, Nomura research

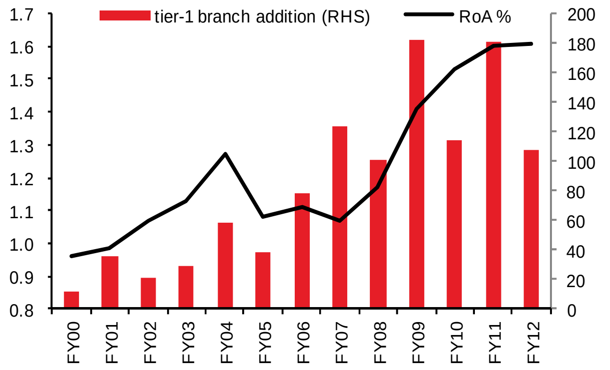
We highlight in the charts below (Figures 7 to 11) how in many cases, a sharp increase in new branch approvals has preceded a marked improvement in a bank's RoA.

Fig. 7: Yes bank: Tier-1 license approvals vs RoA



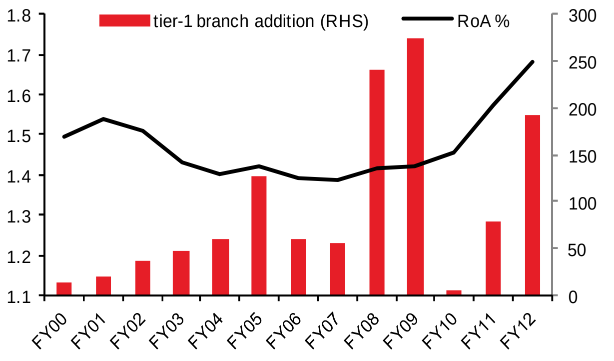
Source: RBI, company data, Nomura estimate

Fig. 8: Axis Bank: Tier-1 license approvals vs RoA



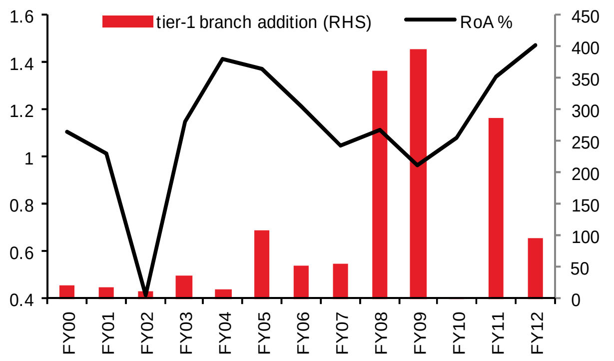
Source: RBI, company data, Nomura research

Fig. 9: HDFC Bank: Tier-1 license approvals vs RoA



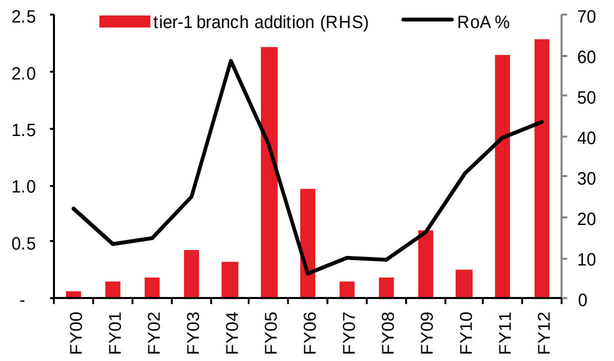
Source: RBI, company data, Nomura research

Fig. 10: ICICI Bank: Tier-1 license approvals vs RoA



Source: RBI, company data, Nomura research

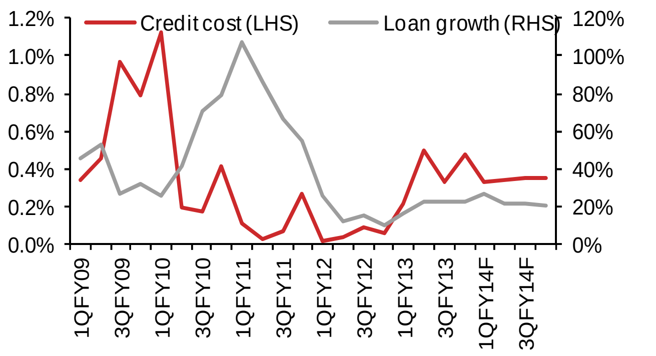
Fig. 11: IndusInd Bank: Tier-1 license approvals vs RoA



Source: RBI, company data, Nomura research

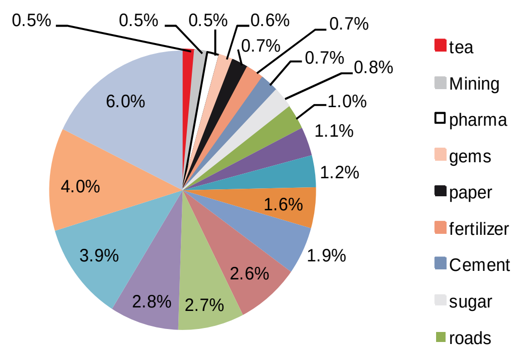
Expect asset quality to be stable. Yes bank has managed its loan loss provisions (LLPs) well within 40bps over the last 3-4 years, despite prudent provisioning on a few big accounts. We expect that with a well-diversified loan book (exposure to any sector is well within 5% proportion of overall book) and a likely benefit from a benign rate cycle, Yes bank should see its asset quality to hold stable. However, we have increased our FY14F LLP estimate to 34bps from 29bps.

Fig. 12: Loan growth vs LLPs



Source: Company data, Nomura estimates

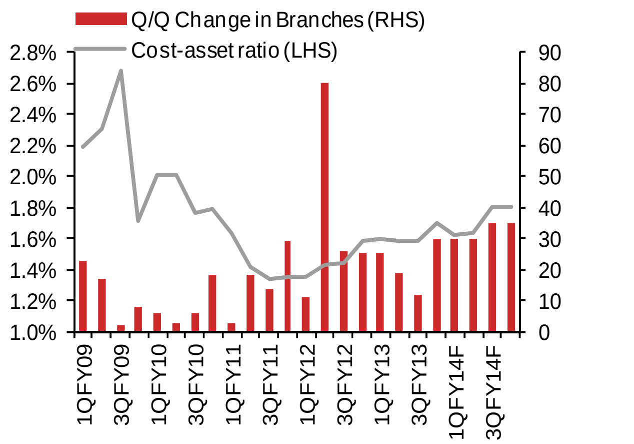
Fig. 13: Funded exposure to various sectors as on 2QFY13



Source: Company data, Nomura research

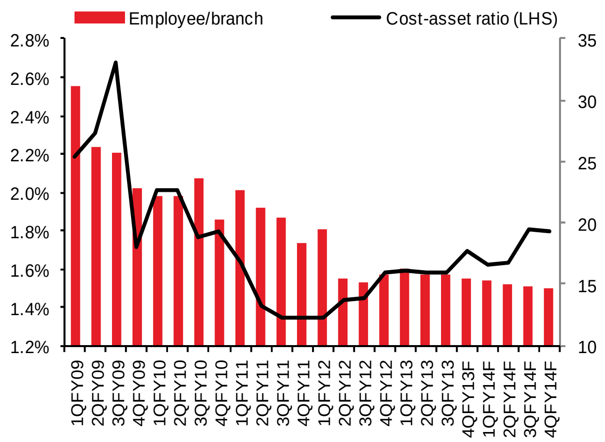
Expect opex ratio to remain stable: YES has been building up operating leverage over the last few quarters with its employee count per branch inching up. We expect the cost-to-asset ratio to increase marginally to 1.7% for FY15F from 1.6% in FY13F.

Fig. 14: Cost-asset ratio vs branch addition



Source: Company data, Nomura estimates

Fig. 15: Cost-asset ratio vs employee per branch



Source: Company data, Nomura estimates

Key assumption changes. We expect Yes Bank's loan growth to pick up and have revised it marginally higher to 21% for FY14F compared to 19.5% earlier. We haven't yet built in meaningful contribution from the retail segment as we expect YES to continue to build the platform till FY15. We have factored in USD400mn of equity raising in Q2FY14F. The assumption changes for FY14F are detailed in the table below.

Our target price increase of 45% (from INR425 to INR615) is driven by:

- 21% increase owing to rollover to FY14F ABV
- 12% increase owing to assumed dilution (equity raising of $400mn)
- 12% increase in earnings owing to better NIMs driven by higher CASA ratio
-

Fig. 16: Key FY14F estimate changes

Key FY14F estimate changes	Old	New
Loan growth	19.6%	20.5%
NII (INRmn)	28,288	30,296
NIM	3.20%	3.27%
CASA ratio	20.96%	23.55%
SA growth	51.65%	69.77%
SA/branch	170.5	223.0
Provisions for NPLs (INRmn)	1,446	1,758
LLPs	0.29%	0.34%
Delinquency (INRmn)	0.47%	0.48%
GNPL ratio	0.70%	0.66%
Provision coverage ratio	74.7%	74.8%
PAT (INRmn)	14,755	16,000
Cost of equity	15.4%	14.6%
Risk-free rate	8.5%	7.8%

Source: Nomura estimates

Fig. 17: Du-pont table

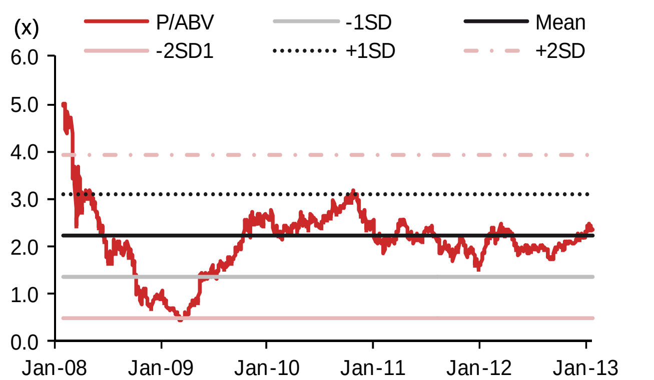
Y/E March	FY08	FY09	FY10	FY11	FY12F	FY13F	FY14F	FY15F
% of Average assets								
Interest Income	9.29%	10.05%	7.96%	8.47%	9.51%	10.00%	9.95%	9.96%
Interest Expense	6.94%	7.48%	5.34%	5.86%	7.07%	7.31%	6.94%	6.79%
Net-Interest Income	**2.35%**	**2.56%**	**2.63%**	**2.61%**	**2.44%**	**2.68%**	**3.01%**	**3.17%**
Non-Interest Income	2.57%	2.18%	1.97%	1.31%	1.29%	1.43%	1.41%	1.41%
Fee income	1.46%	1.18%	1.26%	1.25%	1.02%	1.14%	1.13%	1.13%
Treasury	0.58%	1.01%	0.71%	0.21%	0.28%	0.29%	0.28%	0.28%
Net Income	**4.92%**	**4.74%**	**4.60%**	**3.92%**	**3.73%**	**4.11%**	**4.42%**	**4.59%**
Operating Expenses	2.43%	2.10%	1.69%	1.43%	1.41%	1.61%	1.71%	1.74%
Operating Profit	2.49%	2.65%	2.91%	2.50%	2.32%	2.51%	2.71%	2.84%
Provisions	0.31%	0.31%	0.46%	0.21%	0.14%	0.24%	0.26%	0.30%
Taxes	0.76%	0.81%	0.84%	0.77%	0.71%	0.75%	0.86%	0.89%
RoA (%)	**1.42%**	**1.52%**	**1.61%**	**1.52%**	**1.47%**	**1.52%**	**1.59%**	**1.66%**
Avg.assets/avg equity (x)	13.6	13.9	12.9	14.2	16.1	16.2	13.6	12.2
RoE (%)	**19.3%**	**21.2%**	**20.8%**	**21.7%**	**23.7%**	**24.7%**	**21.6%**	**20.1%**

Source: Company data, Nomura estimates

Valuation methodology

We arrive at our revised target price of INR615 using a three-stage residual-income valuation method that assumes the following: 1) 21.1% CAGR for interest-earning assets over FY12-17F, 13.9% CAGR over FY17-25F and a terminal growth rate of 4%; 2) average ROE of 20.9% over FY12-25F and a 17.3% terminal ROE; and 3) discount rates ranging from 14.6% (current cost of equity) for FY12-17F, 12.25% for FY18-25F and an 10% terminal rate. At our TP, Yes bank should trade at 2.7x our FY14F ABV of INR228.1 and 15.3x our FY14F EPS of INR40.3 for an ROE of 21.6% for FY14F. We are building in capital infusion of USD 400mn in FY14F. Our methodology is unchanged.

Fig. 18: P/ABV chart



Source: Bloomberg, Nomura estimates

Fig. 19: P/E chart

Source: Bloomberg, Nomura estimates

Key risks

Key risks are a sharp deterioration in asset quality and slower-than-expected SA growth.

Appendix A-1

Analyst Certification

We, Abhishek Bhattacharya, Vijay Sarathi and Amit Nanavati, hereby certify (1) that the views expressed in this Research report accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Research report, (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Research report and (3) no part of our compensation is tied to any specific investment banking transactions performed by Nomura Securities International, Inc., Nomura International plc or any other Nomura Group company.

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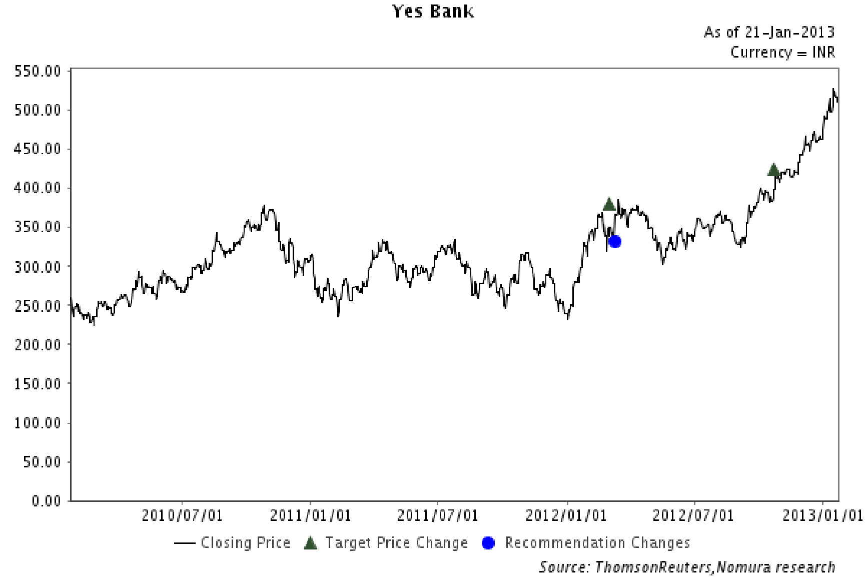
Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Yes Bank	YES IN	INR 508	24-1-2013	Buy	Not rated	

Yes Bank (YES IN) **INR 508 (24-1-2013)** Buy (Sector rating: Not rated)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
23-Oct-12		425.00	399.35
01-Mar-12	Neutral		340.00
01-Mar-12		380.00	340.00

For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We arrive at our target price of INR615 using a three-stage residual-income valuation method that assumes the following: 1) 21.1% CAGR for interest-earning assets over FY12-17F, 13.9% CAGR over FY17-25F and a terminal growth rate of 4%; 2) average ROE of 20.9% over FY12-25F and a 17.3% terminal ROE; and 3) discount rates ranging from 14.6% (current cost of equity) for FY12-17F, 12.25% for FY18-25F and an 10% terminal rate. At our TP, Yes bank should trade at 2.7x our FY14F ABV of INR228.1 and 15.3x our FY14F EPS of INR40.3 for an ROE of 21.6% for FY14F. We are building in capital infusion of USD 400mn in FY14F.

Risks that may impede the achievement of the target price Key risks are a sharp deterioration in asset quality and slower than expected SA growth.

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Explanation of Nomura's equity research rating system in Japan and Asia ex-Japan

STOCKS

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