SSKI
INDIA RESEARCH

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UTI Bank

Rs466
OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs130bn; US $3.1bn

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Result: Q4FY07
Comment: Sustained strong performance, upgrading estimates
Last report: 12 January 2007 (Price Rs499; Recommendation: Outperformer)

Key valuation metrics

Year to 31 March	2005	2006	2007E	2008E	2009E
Net profit (Rs mn)	3,346	4,851	6,590	8,247	10,349
yoy growth (%)	20.2	45.0	35.9	25.1	25.5
Shares in issue (mn)	274	279	282	282	282
EPS (Rs)	13.2	17.6	23.5	29.3	36.7
EPS growth (%)	9.8	32.6	34.0	24.5	25.5
PE (x)	35.2	26.5	19.8	15.9	12.7
Book value (Rs/share)	88.0	103.1	114.8	138.6	168.8
Adj. Book value (Rs/share)	83.3	99.2	108.5	129.1	156.7
P/ Adj. Book (x)	5.6	4.7	4.3	3.6	3.0
ROAE (%)	18.9	18.4	21.6	23.1	23.9

UTI Bank has delivered a robust set of numbers for Q4FY07. Net profit has grown to Rs2.12bn in the quarter (40% yoy growth), which is well above our expectations of Rs1.91bn. Continued acceleration in loan growth, and impressive performance on fee income marginally offset by slight moderation in margins (ex. CRR income credit) are the key takeaways from the results. Positive surprise emanating from lower than expected has also contributed to the surge in profits. The bank's CASA ratio has improved by 300bp Q0Q, driven by impressive growth in savings and current account balances. The bank has indicated its intention for equity dilution in the current fiscal to shore up its Tier I capital. The management is quite confident of sustaining growth momentum without credit quality getting adversely impacted in the near term. We have upgraded our EPS estimates by 3.0 % and 3.8% (pre-dilution) for FY08 and FY09 respectively on the back of a higher than expected increase in core earnings. We expect the bank to deliver 28.7% CAGR in earnings with average RoE of 21.7% over FY06-09 (pre-dilution). We reiterate Outperformer.

KEY HIGHLIGHTS

❑ Continued momentum in loan growth

UTI Bank has reported 65% yoy growth in its loan book on the back of a sharp increase of 77% yoy in corporate which compensates for the slight moderation in retail advances growth of 38%. The proportion of retail advances has declined 24.2% of the total loan book from 28% previous quarter due to retirement of personal loans of Rs15bn. which were given under the scheme of Delhi Development Authority (DDA)* from Q1FY07.

*Note: *(The DDA deal involves margin funding to prospective home buyers, offering marginally lower yields wherein the bank finances against the letter issued by DDA, which is 100% secured. Post allotment of homes, the unsuccessfully applications are refunded).*

❑ One-time interest credit on CRR balances helps bank maintain margins

While margins have remained relatively stable yoy at 2.7% in Q4FY07, the Q4FY07 quarter includes CRR income credit (June-Dec 2006) to the tune of ~Rs110mn, which if excluded has resulted in margins declining by 6-8bps yoy. This yoy decline (ex CRR) in Q4FY07 is on back of rising cost of funds, which has risen by 84bps yoy.

Exhibit 1: Yield and margins

For the quarter ended (%)	Q4FY06	Q3FY07	Q4FY07
Yield on advances	8.79	9.18	9.67
Yield on investments	7.02	7.65	7.51
Cost of funds (reported)	5.08	5.53	5.92
NIM (reported)	2.96	3.00	3.06
NIM (calculated)	2.70	2.67	2.69

Source: Company, SSKI Research, yield on advances / investments / NIMs computed on quarterly average balances

❑ ... leading to strong growth in Net Interest Income

UTI Bank's Net Interest Income (NII) has grown by 48% yoy in Q4FY07, which is largely in line with our estimate.

❑ A consistently improving deposit profile

Improvement in its deposit profile is one of the consistent features of UTI Bank's results for the past several quarters. The bank's CASA ratio has improved to 40% as of March 2007 from 37.1% as of December 2006 on the back of a sharp 50% yoy increase in savings deposits and 42% yoy growth in current account deposits. The number of savings accounts has gone up by 40% yoy to 4.73m as of March 2007. Government business and focus on SMEs are the key reasons for the higher current account balances. However, CASA ratio remained stable yoy.

❑ Strong fee income growth driven by both retail and corporate banking

Fee income growth has been maintained at a higher level of 60% yoy, as seen in the last two quarters. Maintaining its leading position in the placement and syndication of corporate bond market has led to strong growth in capital market income by 186% yoy. Higher transaction charges in retail banking, ATM sharing fees and the cards business has led to a surge in retail banking fee income (up 68% yoy growth).

The bank has entered in to a tie-up with Metlife India as its banc assurance partner in Q4FY07 and has already scaled up to become the third largest banc assurance partner in the industry. Additionally, the bank has rolled out credit card venture and has being leading the pack in incremental issuances. We believe that, going forward, these two businesses would supplement the growth in fee income for the bank.

Exhibit 2: Details of fee income

Q4FY07	Fee income (Rs m)	% of total fee income	yoy growth (%)
Corporate banking	640	26.8	48.8
Business banking	390	16.3	11.4
Capital markets	400	16.7	185.7
Retail banking	960	40.2	68.4
Total	**2,390**	**100.0**	**60.4**

Source: Company

❑ Operating expenses, ex staff costs rise…

UTI Bank's operating expenses have grown by 41.2%yoy in Q4FY07, which is higher than our estimate of a 35% yoy increase, mainly on the back of other operating expenses, which are up 40.8%yoy, while employee expenses have grown only by 42.3%yoy. Lower than estimated employee expense is largely due to the bank expensing out bonuses in Q3FY07. The bank's employee base has gone up by 52% yoy to ~9,980 by end-March 2007. In Q4FY07 itself, the bank recruited 605 employees. The bank has managed to reduce its operating expense to net revenue ratio to 44.8% from 48.4% in the preceding quarter.

❑ …driven by continued expansion in network

The bank increased its reach to 561 branches & extension counters and 2341 ATMs across 332 cities and towns. During the year it added 111 Branches & Extension Counters and 450 ATMs. During Q4FY07 alone, the bank has added 80 branches and 215 ATMs.

❑ Asset quality continues to improve

Improvement in asset quality continued in Q4FY07 with Gross NPAs down to 0.95% from 1.20% in Q3FY07 and 1.28% in FY06. Even in absolute basis, there was a qoq decline of Rs533mn in Gross NPAs. This reduction in Gross NPA enabled the bank to make lower provisions towards NPAs during the quarter. Net NPAs have improved to 0.61% as of March 2007 from 0.75% in March 2006. Net NPAs are ~8% of the bank's networth. Including write-offs, the bank has a healthy 76.2% coverage ratio. Provisions for standard assets are higher in the current quarter by Rs270m reflecting the higher provision undertaken by the management on personal loan portfolio in response to the RBI circular mandating higher provisioning requirements for certain classes of standard assets from 1% to 2.0%.

❑ Will require equity infusion in FY08

UTI Bank's Tier-I CAR stands at 6.42% as of March 2007 while the overall CAR is 11.57%. The Tier-I CAR of 6.42% is after issuance of Rs2.14bn and USD46m of perpetual bonds, while upper Tier-II capital was raised by issuing 15-year bonds in two tranches of USD150m and Rs3.1bn each. Upper Tier-II bonds of USD 150m were raised in Singapore as a part of the bank's MTN programme. Lower Tier 2 bonds to the tune of Rs3.9bn were also raised during the year. Though the current adequacy numbers are comfortable, we expect the bank to raise equity capital in FY08. We believe that the bank has entered a successful chain of growth, enabling it to raise fresh equity capital at every stage at richer valuations to fund its strong loan expansion.

❑ Some management and ownership concerns still remain

The tussle between RBI and UTI CMD over splitting the CMD post in to two separate functions, the ownership change after SUUTI sells it stake of 27.4% during FY08 and outcome of tussle for the brand 'UTI' between the bank and UTI AMC are the three key monitorables in FY08 .

❑ Upgrading estimates and price target; reiterate Outperformer

UTI Bank has shown impressive performance on the back of strong momentum in its core business areas. We are upgrading our FY07 and FY08 EPS estimates (pre-dilution) by 3.0% and 3.8% to Rs29.3and Rs36.7, respectively. The bank is likely to generate 28.7% CAGR in earnings over FY06-09 and average RoE of 21.7% (pre-dilution) over the same period. The stock currently trades at 3.6x FY08E and 3.0x FY09E adjusted book value. We reiterate Outperformer.

Earnings model

	Q4FY06	FY06	Q1FY07	Q2FY07	Q3FY07	Q4FY07	FY07E	FY08E	FY09E
Interest income	8,327	28,888	9,539	10,501	11,896	13,668	45,604	62,847	82,773
Non fund income	2,281	7,296	2,245	2,048	2,798	3,011	10,101	13,268	17,364
Trading profits	657	2,167	400	233	793	432	1,857	750	500
Fee Income	1,624	5,129	1,846	1,814	2,005	2,579	8,244	12,518	16,864
yoy growth (%)	*47.3*	*19.4*	*60.6*	*65.7*	*58.9*	*58.9*	*60.7*	*51.8*	*34.7*
Interest expenses	5,198	18,106	6,321	6,849	7,738	9,025	29,933	41,697	55,302
Net Interest Income	3,129	10,782	3,218	3,652	4,158	4,642	15,671	21,150	27,471
yoy growth (%)	*59.4*	*47.5*	*44.7*	*43.0*	*44.7*	*48.4*	*45.3*	*35.0*	*29.9*
Net revenue	5,409	18,079	5,463	5,699	6,956	7,653	25,772	34,418	44,835
Operating expenses	2,429	8,141	2,392	2,955	3,370	3,430	12,146	17,014	23,396
Employee related expenses	625	2,402	797	981	1,147	889	3,814	5,863	8,707
Other operating expenses	1,804	5,739	1,595	1,974	2,223	2,541	8,332	11,151	14,689
Operating profit	2,981	9,938	3,072	2,745	3,586	4,223	13,626	17,404	21,439
Provisions	682	2,625	1,248	588	763	1,065	3,664	4,908	5,758
PBT	2,299	7,313	1,824	2,157	2,824	3,158	9,962	12,496	15,681
Tax	782	2,462	618	738	977	1,039	3,372	4,249	5,332
PAT	1,517	4,851	1,206	1,420	1,846	2,119	6,590	8,247	10,349
yoy growth (%)	*30.2*	*45.0*	*30.1*	*30.2*	*40.2*	*39.6*	*35.9*	*25.1*	*25.5*
Ratios (%)									
NIM	2.70	2.46	2.51	2.59	2.67	2.69	2.60	2.62	2.64
Non fund revenue/Avg assets	1.97	1.67	1.75	1.45	1.79	1.74	1.68	1.64	1.67
Fee income /avg assets	1.40	1.08	1.44	1.29	1.29	1.49	1.30	1.46	1.53
Operating exp/avg assets	2.10	1.86	1.86	2.10	2.16	1.99	2.02	2.11	2.25
Cost/Net rev.	44.9	45.0	43.8	51.8	48.4	44.8	47.1	49.4	52.2
Prov/avg assets	0.6	0.6	1.0	0.4	0.5	0.6	0.6	0.6	0.6
PBT/Avg asets	2.0	1.7	1.4	1.5	1.8	1.8	1.7	1.5	1.5
Tax/PBT	34.0	33.7	33.9	34.2	34.6	32.9	33.8	34.0	34.0
RoA	1.3	1.1	0.9	1.0	1.2	1.2	1.1	1.0	1.0

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2. Neutral: Within 0-10% to Index
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