

Industry Focus

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India Banks

1QFY10 Preview: Strong Headline, Modest Underlying

- **Headline profit growth 34%, operating at 8%** — Banks will likely be the standout sector this quarter on headlines – we estimate 34% YoY growth (28% in 4Q09), with possible upside. The operating performance will be a lot more moderate – ex trading gains, operating profits should rise 8%yoy, though a step-up from 4Q09 when they fell 2%. The disconnect – significant bond portfolio mark-downs because of higher rate in 1Q09, which will not be there this time. Potential upsides to aggregates from bond portfolio write-backs and lower loan provisions.
- **Operational strain, accounting gain** — This will be a tough operating quarter, as we believe a) Margins – will fall 10-15bps; b) Fee growth – will moderate to 7% (in some cases offset by capital market gains); and c) Underlying loan growth – will moderate. While there could be some support from moderating costs; excluding trading gains, operating profits will rise only 8%. The headlines will however see accounting and valuation gains – no bond portfolio erosion (possibilities of revaluation), possibly high trading gains, and while we factor in high loan loss provisioning, it might not show in the current quarter.
- **Moderating growth, asset strain unlikely to show up meaningfully** — Overall system growth has moderated to 15-16% – this should be in the numbers (and undermine margins and fees), but asset quality pressures could well be moderate (mix of easing pressure, and relatively recent restructuring). We should see balance-sheets sitting on surplus liquidity, slightly inflated bond portfolios and weaker deposit mixes (lower CASA).
- **Private banks should do better on operating performance, after 4 quarters** — This should be a better quarter for private banks – they should manage margins better, make gains on costs, and probably also manage liquidity better. They will however continue to lag on headline profits – growing 25% vs. the Govt banks' 40%, given their lower bond portfolio sensitivity to interest rates.
- **Stay overweight, but possible near term pressures** — We remain moderately overweight on the sector, but cautious near term; given uncertainties on growth, asset quality and, importantly interest rates (which could have the most pronounced near-term impact). Our preferred picks – Axis, HDFC Bank, and Yes (among private banks) and SBI, PNB and Canara (among government banks).

See Appendix A-1 for Analyst Certification and important disclosures.

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Figure 1. Indian Banks – 1Q10 Preview (Rupees Million)

	Private Banks			Government Banks				Sector				
	1Q10	YoY Change	QoQ Change	1Q10	YoY Change	QoQ Change	1Q10	YoY Change	QoQ Change			
	Rsm	%	%	Rsm	%	%	Rsm	%	%			%
Interest Income	207,021	9.4%	-1.8%	393,153	23.3%	-2.3%	600,174	18.1%	-2.1%			
Interest Expense	-132,745	6.7%	-4.1%	-277,376	28.6%	-2.7%	-410,121	20.5%	-3.1%			
Net Interest Income	74,276	14.6%	2.4%	115,777	12.2%	-1.3%	190,053	13.1%	0.1%			
Fee-Based Income	35,084	-3.9%	3.0%	43,121	17.0%	-26.2%	78,205	6.6%	-15.4%			
Other Non-Interest Income	7,166	4328.3%	-61.2%	10,059	32.4%	-68.0%	17,225	122.0%	-65.5%			
Non Interest Income	43,138	14.7%	-19.3%	53,180	19.7%	-40.8%	96,317	17.4%	-32.8%			
Operating Income	117,414	14.7%	-6.8%	168,957	14.4%	-18.5%	286,371	14.5%	-14.1%			
Operating Expenses	(52,324)	3.5%	-5.1%	(83,996)	24.3%	-3.7%	(136,320)	15.4%	-4.2%			
Pre-Provision Profit	65,090	25.5%	-8.1%	84,960	6.1%	-29.2%	150,050	13.8%	-21.4%			
Pre-Provision ex trading	57,924	12.0%	10.6%	74,901	3.4%	-15.4%	132,825	7.0%	-5.7%			
Charges for Bad Debts	(21,898)	64.8%	-4.1%	(18,972)	1448.7%	-27.5%	(40,869)	181.6%	-16.6%			
Other Operating Items	0	-100%	-100%	0	-100%	-100%	0	-100%	-100%			
Pre-Tax Profit	43,193	24.2%	-8.2%	65,988	40.5%	-27.1%	109,181	33.5%	-20.6%			
Tax	(11,757)	20.9%	-22.9%	(19,379)	44.7%	-31.9%	(31,136)	34.7%	-28.8%			
Minorities	(13)	NM	-88.4%	0	NM	NM	(13)	NM	-88.4%			
Net Profit	31,426	25.0%	-0.7%	46,609	38.8%	-24.8%	78,036	32.9%	-16.7%			

Source: Company Reports and CIRA Estimates

Figure 2. Government Banks – 1Q10 Result Expectations

	Net interest Income			Pre-Provision Profit			Net Profit		
	1Q10	YoY	QoQ	1Q10	YoY	QoQ	1Q10	YoY	QoQ
	Rsm	%	%	Rsm	%	%	Rsm	%	%
State Bank of India	48,265	0%	0%	34,061	-14%	-35%	18,787	15%	-31%
Punjab National Bank	18,376	27%	-4%	12,680	29%	-20%	6,560	28%	-24%
Bank of Baroda	13,830	31%	-6%	10,290	20%	-21%	5,493	48%	-27%
Union Bank	9,155	13%	-1%	6,718	9%	-26%	3,455	51%	-26%
Canara Bank	13,056	28%	0%	10,302	46%	-19%	5,987	388%	-17%
Corporation bank	4,139	9%	-3%	3,991	24%	-41%	2,325	26%	-11%
Oriental Bank of commerce	4,889	9%	6%	3,905	10%	-27%	2,309	5%	18%
Andhra Bank	4,067	17%	3%	3,013	47%	-30%	1,693	118%	-16%
Central Bank of India	6,057	27%	40%	3,176	43%	-30%	1,249	111%	100%
Government Banks	121,834	13%	0%	88,136	7%	-29%	47,858	40%	-24%

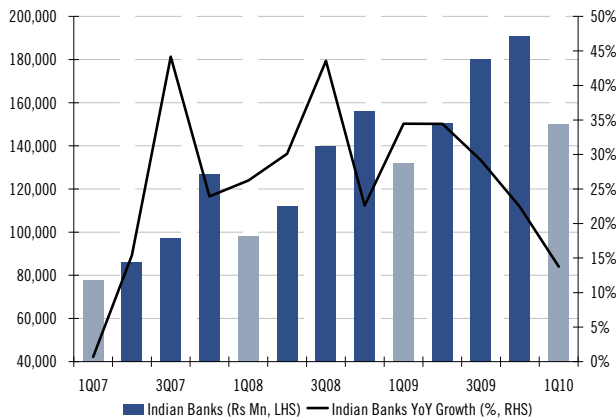
Source: Company Reports and CIRA Estimates

Figure 3. Private Banks – 1Q10 Result Expectations

	Net interest Income			Pre-Provision Profit			Net Profit		
	1Q10	YoY	QoQ	1Q10	YoY	QoQ	1Q10	YoY	QoQ
	Rsm	%	%	Rsm	%	%	Rsm	%	%
ICICI Bank	22,383	7%	5%	20,846	22%	-3%	7,317	1%	-2%
HDFC bank	19,986	16%	8%	13,962	36%	-11%	6,498	40%	3%
Axis Bank	9,896	22%	-4%	9,503	18%	-17%	4,452	35%	-23%
Kotak	6,054	5%	-4%	4,188	38%	-2%	2,255	26%	32%
IDFC	2,609	22%	3%	3,991	30%	41%	2,722	26%	134%
Yes Bank	1,620	43%	4%	1,390	22%	-10%	784	44%	-2%
Federal Bank	3,131	13%	-2%	2,699	6%	-15%	1,256	84%	10%
Private Banks	74,276	15%	2%	65,090	25%	-8%	31,426	25%	-1%

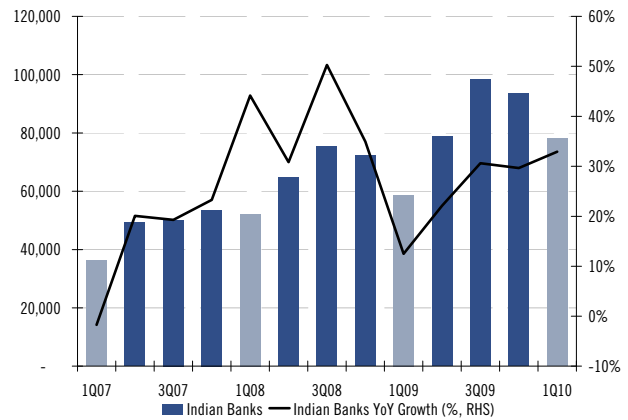
Source: Company Reports and CIRA Estimates

Figure 4. Indian Banks – Pre Provision Profits (Rupees Million, %)



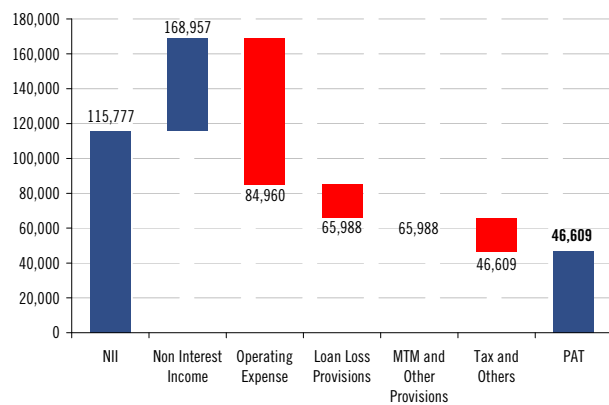
Source: Company Reports and CIRA Estimates

Figure 5. Indian Banks – Net Profits (Rupees Million, %)



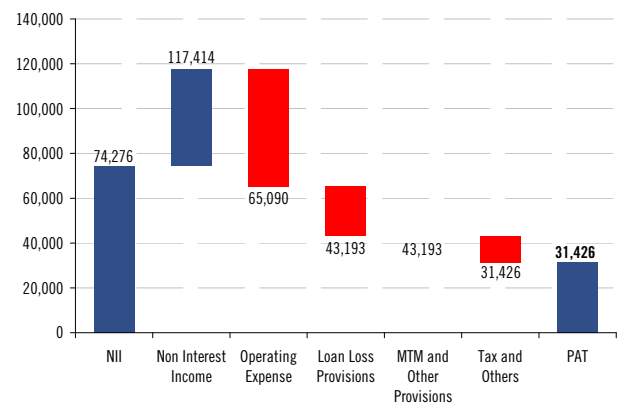
Source: Company Reports and CIRA Estimates

Figure 6. Govt. Banks – Profit & Loss – Bridge Chart (1Q10E, Rsm)



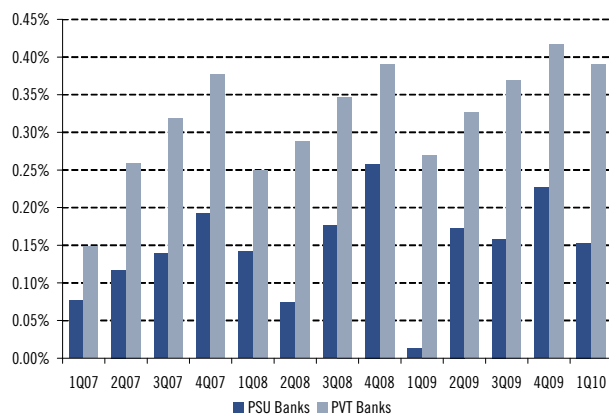
Source: Citi Investment Research and Analysis

Figure 7. Private Banks – Profit & Loss – Bridge Chart (1Q10E, Rsm)



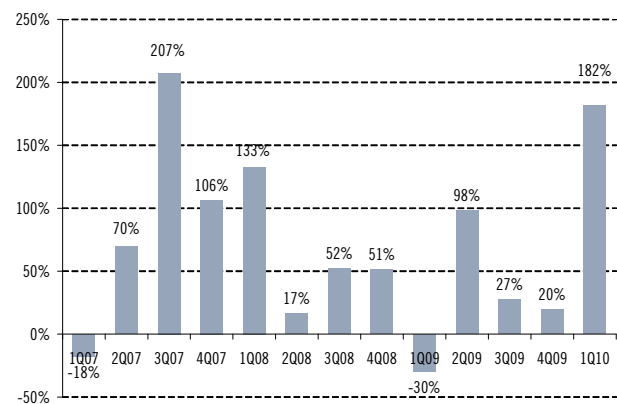
Source: Citi Investment Research and Analysis

Figure 8. Ratio of Loan Loss Provisioning to Opening Loans



Source: Company Reports and CIRA Estimates

Figure 9. Loan Loss Provisioning – YoY Growth (%)



Source: Company Reports and CIRA Estimates

Figure 10. Indian Banks – CIRA Valuation Table

	RIC Code	Price (Rs) 9-Jul	TP (Rs)	Rating	P/E (x) 2010E	P/B (x) 2010E	ROE (%) 2010E	ROA (%) 2010E	Div. Yld 2010E	M-Cap USD Mn	EPS Grth. 2010E	EPS Grth. 2011E	BVPS Grth. 2010E	BVPS Grth. 2011E
Private Sector Banks														
ICICI Bank	ICBK.BO	635.5	830	2M	17.5	1.4	8.1%	1.1%	1.7%	14,494	9%	27%	5%	7%
HDFC Bank	HDBK.BO	1388.8	1618	2L	19.8	3.3	18.9%	1.5%	0.6%	12,126	27%	32%	18%	21%
AXIS Bank	AXBK.BO	758.1	920	1M	12.4	2.3	19.9%	1.4%	1.3%	5,587	22%	27%	18%	20%
Kotak Mahindra Bank	KTKM.BO	560.3	639	3H	20.5	2.6	13.7%	2.2%	0.1%	3,978	45%	11%	14%	14%
Infrastructure Development Fin.	IDFC.BO	124.5	104	3M	16.3	2.3	15.1%	3.0%	1.0%	3,304	32%	15%	13%	13%
Yes Bank	YESB.BO	133.0	164	1M	11.4	2.0	19.2%	1.5%	0.0%	810	14%	25%	21%	22%
Federal Bank	FED.BO	220.9	314	1M	6.4	0.8	12.8%	1.4%	2.0%	773	17%	13%	11%	12%
Public Sector Banks														
State Bank of India	SBI.BO	1600.3	2122	1L	9.7	1.5	16.8%	1.0%	1.8%	20,815	14%	27%	14%	17%
Punjab National Bank	PNBK.BO	627.1	780	1M	5.8	1.1	21.3%	1.3%	3.2%	4,051	11%	15%	18%	18%
Bank of Baroda	BOB.BO	394.0	495	2M	6.2	1.0	16.7%	1.0%	2.3%	2,940	4%	17%	15%	16%
Canara Bank	CNBK.BO	242.3	310	1M	4.5	0.7	16.9%	1.0%	3.3%	2,035	7%	30%	15%	18%
Union Bank Of India	UNBK.BO	225.1	226	3L	6.3	1.1	19.0%	1.0%	2.2%	2,329	5%	11%	17%	16%
Oriental Bank of Commerce	ORBC.BO	161.7	250	1H	3.8	0.6	15.6%	0.9%	4.5%	830	19%	23%	13%	15%
Corporation Bank	CRBK.BO	299.0	425	1H	4.0	0.7	19.9%	1.1%	4.3%	879	19%	15%	18%	18%
Andhra Bank	ADBK.BO	79.2	87	3M	5.3	0.9	18.8%	1.0%	5.7%	787	12%	20%	13%	15%
Central Bank Of India	CBI.BO	91.5	78	3M	6.4	0.6	10.0%	0.4%	1.1%	758	12%	12%	10%	10%

Source: Citi Investment Research and Analysis

Appendix A-1

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