

**YES BANK***Growth unlimited*

Yes Bank continues to step on the growth accelerator, and has grown 16% Q-o-Q and 86% Y-o-Y, well above the system growth of 20%, capitalising on short-term lending opportunities. Strong business traction has offset the 10bps decline in reported margins, resulting in an impressive 20% Q-o-Q NII growth, ahead of our estimates. Fee income has, however, been moderate once again, and coupled with MTM loss of INR 150 mn, pulled down other income. The bank's asset quality continues to be benign with positives emerging from lower NPL provisions.

#### ■ Growth unlimited: Advance book up 86% Y-o-Y

Led by strong disbursement to infrastructure and engineering sectors, Yes Bank once again delivered robust advances growth of 86% Y-o-Y. Quality of the book improved as proportion of large corporate loans increased to 70% from 65% a year ago - a function of incremental lending to telecom operators. Deposits grew 107% Y-o-Y, largely buoyed by IPO floats under the ASBA scheme. Management expects loan book growth of 40-45% in FY11E.

#### ■ Fee income growth below expectation

Over the past few quarters, fee income has picked up only modestly. During the quarter, transaction banking fee income was relatively subdued, up only 9% Y-o-Y. Management expects increased traction, going forward, as it leverages new business relationships. Financial advisory fees (savior in Q1) came off 16% Q-o-Q, but grew 13% Y-o-Y, reflecting lumpiness in income stream. During the quarter, MTM loss of ~200 mn pulled down the financial market income stream (down 72% Y-o-Y).

#### ■ Outlook and valuations: Strong momentum; maintain 'BUY'

Led by higher-than-expected advance growth and lower credit cost, we are revising our earning estimate by 8% and 15% for FY11 and FY12 respectively. With capital in place, we expect Yes Bank could grow well above system, delivering superior earnings (at ~44% CAGR over FY10-12E) and ramping RoEs up to an attractive level in a short time span (~23% in FY12E). Also, management has demonstrated its strong execution capabilities by managing the bank during the cyclical downturn. The stock is currently trading at 2.6x FY12E adjusted book and 12.1x FY12E earnings. We maintain 'BUY/Sector Outperformer' on the stock.

**Financials**

Year to March	Q2FY11	Q2FY10	Growth %	Q1FY11	Growth %	FY10	FY11E
Net int. inc. (INR mn)	3,132	1,760	77.9	2,621	19.5	7,880	12,793
Net profit (INR mn)	1,763	1,117	57.8	1,564	12.7	4,776	7,139
Adj.B/V per share (INR)						91	110
Diluted EPS (INR)	5.1	3.8	36.4	4.6	11.8	14.1	21.0
Price / Adj. book (x)						3.9	3.2
Price/ PPOP (x)						15.5	10.3
Diluted P/E (x)						25.1	16.8

**October 20, 2010**

Reuters: YESB.BO Bloomberg: YES IN

**EDELWEISS 4D RATINGS**

Absolute Rating	<b>BUY</b>
Rating Relative to Sector	<b>Outperformer</b>
Risk Rating Relative to Sector	<b>Medium</b>
Sector Relative to Market	<b>Equalweight</b>

Note:

Please refer last page of the report for rating explanation

**MARKET DATA**

CMP	:	INR 352
52-week range (INR)	:	365 / 214
Share in issue (mn)	:	339.7
M cap (INR bn/USD mn)	:	122 /2,742
Avg. Daily Vol. BSE/NSE ('000):	:	2,608.7

**SHARE HOLDING PATTERN (%)**

Promoters*	:	26.7
MFs, FIs & Banks	:	15.3
FIIIs	:	47.1
Others	:	10.9
* Promoters pledged shares (% of share in issue)	:	1.0

**PRICE PERFORMANCE (%)**

	Stock	Nifty	EW Banks and Financial Services Index
1 month	5.3	2.4	1.1
3 months	16.5	11.9	20.1
12 months	44.1	17.2	32.2

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- **Branch expansion strategy: Key growth driver**

Over the next few quarters, as balance sheet continues to grow (well above industry), building a deposit franchise will be extremely critical. The subdued interest rate environment has enabled the bank to maintain higher margins. Margins could, however, be hit, if branch expansion/improving productivity from new branch strategy does not lead to lower yet stable retail deposit franchise or improve the current account balances from existing relationships. The bank is currently operating 171 branches and intends to reach 250 branches by June 2011. Delay in increasing the branch network/presence could be a key risk to the bank's ambition of increasing CASA ratio by ~2-3% points Y-o-Y.

- **Reported margins decline 10bps, to 3.1%**

Yes Bank's reported margins declined 10bps to 3.1%. Spreads, however, declined 50bps, led by 10bps fall in yield on advances and 40bps rise in cost of funds (first increase after six quarters). Impact of higher leverage also contributed to margin decline. Higher investment yields, coupled with higher average credit deposit ratio, compensated for the spread decline. In the medium term, given the expected steeping of the yield curve and the bank's ambition of growing 2x the industry, we believe margins will come under pressure. We are building in margins of 2.82% in FY11 against 2.67% in FY10.

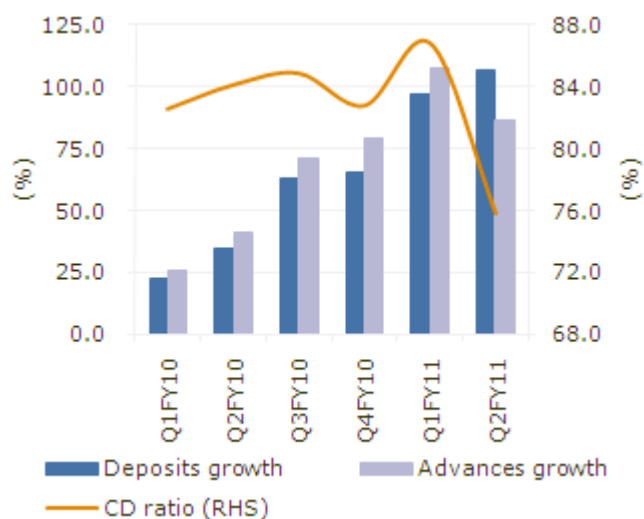
- **Asset quality: Good gets better**

Yes Bank's headline asset quality indicators improved due to controlled slippages and higher recoveries. With weak assets of INR 1.36 bn (reported gross non-performing assets (NPAs) + standard asset restructuring) below ~1%, we believe the bank will be able to capitalise on reviving corporate credit demand while its competitors deal with asset quality pressures.

- **Higher core income aiding cost to income improvement**

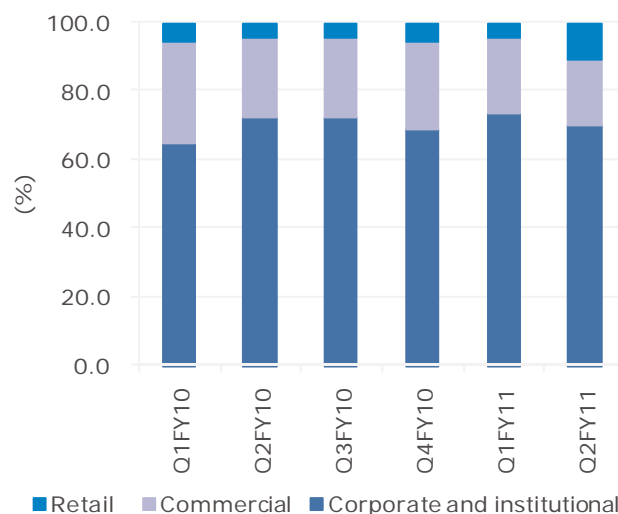
The bank's cost-to-income ratio for the quarter declined 200bps Q-o-Q, to 37.7%, an impressive statistic due to strong growth in the core income. During Q2FY11, it added ~176 employees, taking the total employee strength to 3626. With the stated objective of expanding branch network by 70 and adding 100 employees per month, cost-to-income ratio has an upward bias. We have built in cost-to-income ratio at 37% for over FY11-12.

Chart 1: CD ratio comes upto 76%



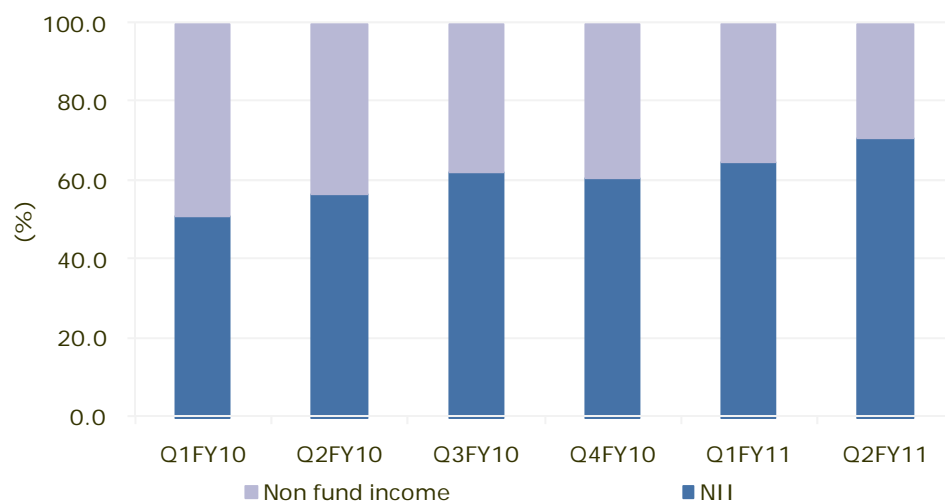
Source: Company, Edelweiss research

Chart 2: Loan book break-up



Source: Company, Edelweiss research

Chart 3: Strong NII; dwarfing share of non-fund income



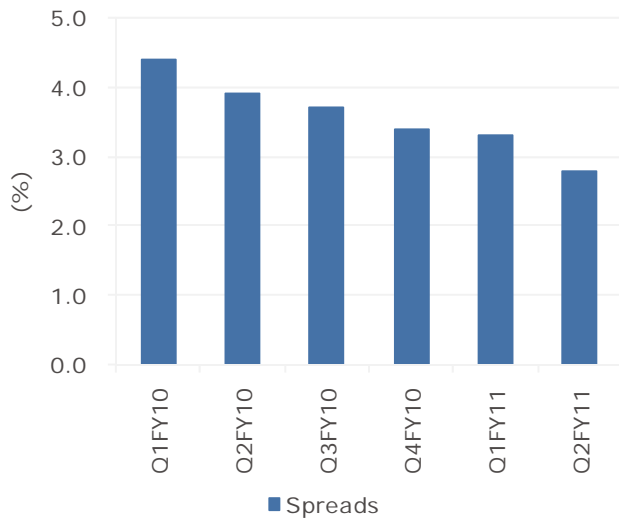
Source: Company, Edelweiss research

Table 1: Financial markets registered decline due to MTM losses

(INR mn)	Q2FY11	Q2FY10	Growth (%)	Q1FY11	Growth (%)
Financial markets	141	496	(71.6)	226	(37.6)
Financial advisory	637	563	13.1	761	(16.3)
Third party distribution	148	104	42.3	109	35.8
Transaction banking	383	353	8.5	343	11.7

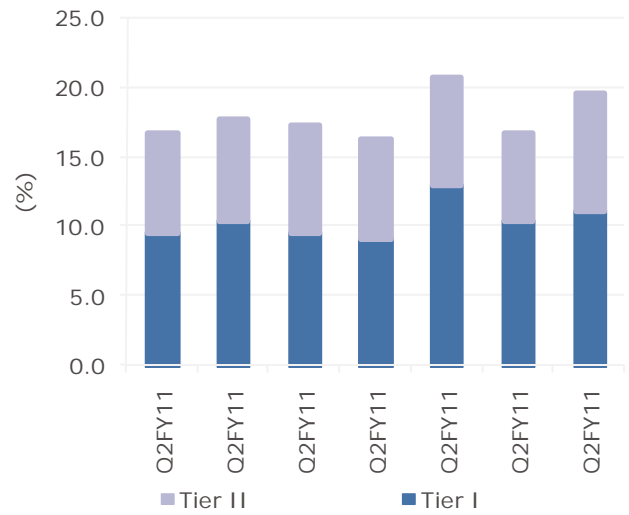
Source: Company, Edelweiss research

**Chart 4: Declining loan yields put pressure on spreads**



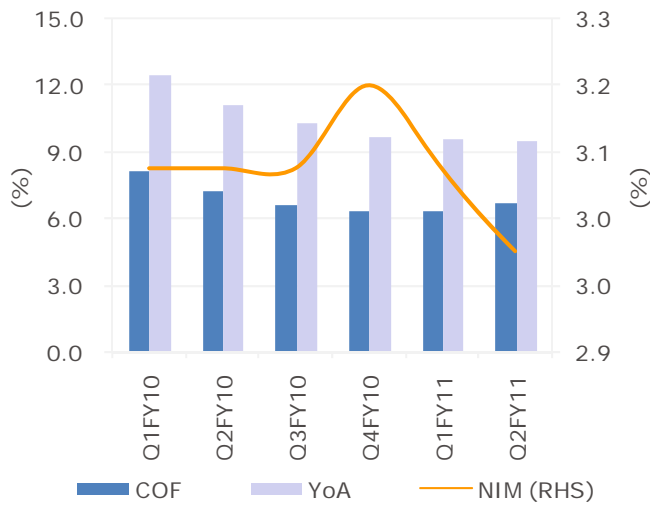
Source: Company, Edelweiss research

**Chart 5: Capital adequacy comfortable**



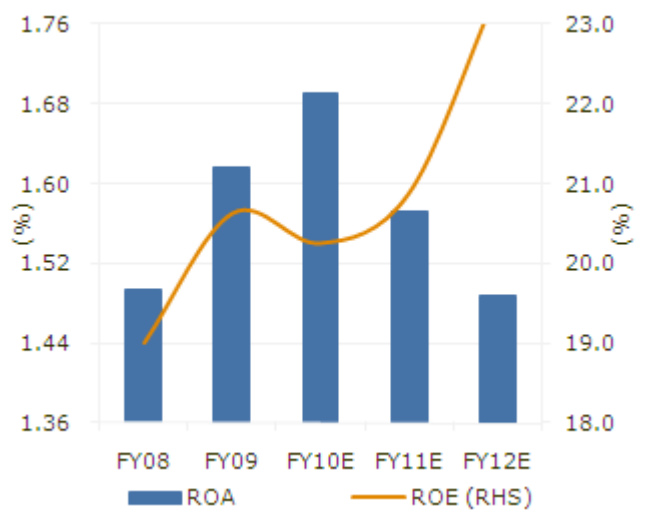
Source: Company, Edelweiss research

**Chart 6: NIMs came off marginally**



Source: Company, Edelweiss research

**Chart 7: ROEs to touch 23.4% by FY12**



Source: Company, Edelweiss research

## Financials snapshot

(INR mn)

Year to March	Q2FY11	Q2FY10	Growth (%)	Q1FY11	Growth (%)	FY10	FY11E	FY12E
Interest on advances	7,252	4,165	74.1	5,579	30.0	17,715	29,228	47,735
Interest on investments	2,245	1,237	81.4	1,766	27.1	5,859	8,788	12,554
Interest on other resources	28	18	57.5	29	(3.4)	123	174	236
Other interest income	14	10	36.0	18	(24.9)	5,812	5,862	7,721
Interest income	9,538	5,430	75.7	7,392	29.0	23,697	38,191	60,524
Interest expenses	6,406	3,670	74.6	4,771	34.3	15,818	25,398	42,848
Net interest income	3,132	1,760	77.9	2,621	19.5	7,880	12,793	17,677
Other income	1,310	1,355	(3.3)	1,438	(8.9)	5,812	5,862	7,721
Fee income	1,310	1,355	(3.3)	1,438	(8.9)	4,825	5,862	7,621
Operating expenses	1,628	1,197	35.9	1,570	3.7	5,007	7,046	9,271
Staff expense	878	622	41.1	812	8.0	2,569	3,764	5,196
Other opex	750	575	30.3	758	(1.0)	2,438	3,282	4,075
Pre prov profit (PPP)	2,814	1,918	46.7	2,490	13.0	7,697	11,609	16,026
Provisions	174	234	(25.4)	126	38.9	1,419	922	1,189
Loan loss provisions	0	234	(100.0)	196		1,265	992	1,189
Profit before tax	2,640	1,684	56.7	2,364	11.7	7,265	10,687	14,937
Provision for tax	877	567	54.6	800	9.6	2,489	3,548	5,079
Profit after tax	1,763	1,117	57.8	1,564	12.7	4,776	7,139	9,858
EPS (INR)	5.1	3.8	36.4	4.6	11.8	14.1	21.0	29.0

## Ratios

NII / GII	32.8	32.4		35.5		33.3	33.5	29.2
Cost - income	36.6	38.4		38.7		36.6	37.8	36.5
Provisions / PPOP	6.2	12.2		5.0		18.4	7.9	7.4
Tax rate	33.2	33.7		33.9		34.3	33.2	34.0
CD ratio	75.8	84.1		86.8		86.1	81.7	82.2
CASA	10.1	9.6		10.5		10.5	12.0	13.5
Capital adequacy (%)	19.4	17.3		16.6		16.6	20.6	15.3
NIM (%)	3.0	3.1		3.1		2.8	2.8	2.7

## Balance sheet data (INR bn)

Advances	303	163	86.2	263	15.6	222	360	507
Deposits	400	194	106.6	302	32.3	268	451	628
CD ratio	76	84		87		83	80	81

## Asset quality (INR mn)

Gross NPA	677	500	35.4	597	13.5	602	392	392
Gross NPA (%)	0.2	0.3		0.2		0.3	0.1	0.1
Net NPA	172	126	36.6	111	54.7	130	120	116
Net NPA (%)	0.06	0.08		0.04		0.06	0.03	0.02
Provision coverage (%)	74.7	74.9		81.4		78.4	69.4	70.3

- **Company Description**

YES BANK is a private Indian bank promoted by Rana Kapoor and Ashok Kapur with financial support from Rabobank Nederland, and global institutional private equity investors –AIF Capital, and ChrysCapital. It is operational since November 2004 and is the only greenfield bank approved by RBI in last decade. It has market cap of USD 2.7 bn and balance sheet of ~INR 517 bn. It has branch network of 173 at the end of Q2FY11 and a CASA ratio of 10.1%. Corporate lending forms 70% of its book, commercial 22% and retail 5%.

- **Investment Theme**

YES BANK is one of the few private sector banks with product depth, sustainable competitive edge, and strong growth. Given the underlying credit demand and small asset book, the loan book is expected to grow at more than 35% for the next two years. The bank's high proportion of fee income enables high return on assets (of 1.6%+) and indicates its potential of generating higher than presently reported RoE (20%+), once the capital ratios normalise. Considering the bank's strong fundamentals reflected in its product width, adept management, and technological prowess, we find it to be the perfect acquisition candidate for a foreign player, once the regulations ease.

- **Key Risks**

Lower CASA can be a negative for the bank at this point of time when most banks are banking on their franchise network.

In the event of demand for credit dying down as in the current scenario, lack of pricing power can impact its margins adversely (due to nascent deposit franchise).

## Financial Statements

<b>Income statement</b>		<b>(INR mn)</b>				
Year to March	FY08	FY09	FY10	FY11E	FY12E	
Interest income	13,108	20,033	23,697	38,191	60,524	
Interest expenses	9,741	14,921	15,818	25,398	42,848	
Net interest income	3,367	5,112	7,880	12,793	17,677	
Non interest income	3,609	4,571	5,812	5,862	7,721	
- <i>Fee &amp; forex income</i>	2,273	2,739	4,283	5,203	6,764	
- <i>Misc. income</i>	745	345	543	659	857	
- <i>Investment profits</i>	591	1,486	986	0	100	
Net revenues	6,976	9,682	13,691	18,655	25,398	
Operating expense	3,473	4,187	5,007	7,046	9,271	
- <i>Employee exp</i>	2,024	2,180	2,569	3,764	5,196	
- <i>Other opex</i>	1,449	2,007	2,438	3,282	4,075	
Preprovision profit	3,503	5,495	8,684	11,609	16,126	
Provisions	438	836	1,419	922	1,189	
- <i>Loan loss provisions</i>	204	836	1,265	992	1,189	
- <i>Investment depreciation</i>	133	0	154	(70)	0	
- <i>Other provisions</i>	101	0	0	0	0	
PBT	3,065	4,659	7,265	10,687	14,937	
Taxes	1,063	1,621	2,489	3,548	5,079	
PAT	2,002	3,038	4,776	7,139	9,858	
Reported PAT	2,002	3,038	4,776	7,139	9,858	
EPS	6.8	10.2	14.1	21.0	29.0	
DPS	0.0	0.0	1.5	1.5	1.5	
Payout ratio (%)	0.0	0.0	12.5	8.2	6.0	

### Growth ratios (%)

Year to March	FY08	FY09	FY10	FY11E	FY12E
NII growth	96.5	51.8	54.1	62.4	38.2
Fees growth	57.1	20.5	56.4	21.5	30.0
Opex growth	54.2	20.6	19.6	40.7	31.6
PPOP growth	113.9	37.7	92.0	50.8	38.0
PPP growth	138.7	56.9	58.0	33.7	38.9
Provisions growth	1,291.3	90.8	51.3	(21.6)	19.9
PAT growth	114.2	51.7	57.2	49.5	38.1

### Operating ratios (%)

Year to March	FY08	FY09	FY10	FY11E	FY12E
Yield on advances	11.8	13.6	10.2	10.1	11.0
Yield on investments	9.0	8.2	6.8	6.7	6.7
Yield on assets	9.8	10.7	8.4	8.4	9.1
Net interest margins	2.5	2.7	2.8	2.8	2.7
Cost of funds	7.5	8.1	5.8	5.9	6.8
Cost of deposits	7.9	8.3	5.8	5.8	6.7
Cost of borrowings	7.9	9.8	7.8	8.1	8.4
Spread	2.3	2.6	2.6	2.5	2.3
Cost-income	49.8	43.2	36.6	37.8	36.5
Tax rate	34.7	34.8	34.3	33.2	34.0

<b>Balance sheet</b>					<b>(INR mn)</b>
Year to March	FY08	FY09	FY10	FY11E	FY12E
<b>Liabilities</b>					
Equity capital	2,958	2,970	3,397	3,397	3,397
Reserves	10,231	13,272	27,499	34,050	43,320
Net worth	13,189	16,242	30,896	37,446	46,716
Sub bonds/pref cap	7,275	15,126	0	3,000	9,000
Deposits	132,732	161,694	267,986	451,287	628,498
Borrowings	9,862	21,891	47,491	57,991	72,991
Other liabilities	6,774	14,055	17,453	17,358	17,591
<b>Total</b>	<b>169,832</b>	<b>229,008</b>	<b>363,825</b>	<b>567,082</b>	<b>774,796</b>
<b>Assets</b>					
Loans	94,303	124,031	221,931	359,529	506,935
Investments					
<i>Gilts</i>	<i>35,964</i>	<i>46,801</i>	<i>67,865</i>	<i>127,319</i>	<i>175,372</i>
<i>Others</i>	<i>14,973</i>	<i>24,369</i>	<i>34,235</i>	<i>35,905</i>	<i>37,659</i>
Cash & equi	16,276	19,227	26,733	34,426	47,502
Fixed assets	1,012	1,311	1,155	958	1,167
Other assets	7,305	13,269	11,907	8,945	6,160
<b>Total</b>	<b>169,832</b>	<b>229,008</b>	<b>363,825</b>	<b>567,082</b>	<b>774,796</b>
<b>Balance sheet ratios (%)</b>					
Credit growth	49.5	32.8	71.9	59.8	40.1
Deposit growth	61.5	21.8	65.7	68.4	39.3
EA growth	51.6	32.8	63.6	58.8	37.7
SLR ratio	25.2	25.5	21.5	25.0	25.0
C-D ratio	76.2	83.0	86.1	81.7	82.2
Low-cost deposits	8.5	8.7	10.5	12.0	13.5
Gross NPA ratio	0.1	0.7	0.3	0.1	0.1
Net NPA ratio	0.1	0.3	0.1	0.0	0.0
Provision coverage	20.0	51.5	78.4	69.4	70.3
Incremental slippage	0.2	0.9	0.9	0.3	0.4
Net NPA / Equity	0.6	2.5	0.4	0.3	0.2
Capital adequacy	13.6	16.6	20.6	15.3	15.1
- Tier 1	8.5	9.5	12.9	14.0	12.7
Book value (INR)	44.6	54.7	91.0	110.2	137.5
<b>ROA decomposition (%)</b>					
Year to March	FY08	FY09	FY10	FY11E	FY12E
<b>ROA decomposition (%)</b>					
Net interest income/Assets	2.5	2.7	2.8	2.8	2.67
Fees/Assets	2.3	1.6	1.7	1.3	1.2
Investment profits/Assets	0.4	0.8	0.3	0.0	0.0
Net revenues/Assets	5.2	5.2	4.8	4.1	3.8
Operating expense/Assets	(2.6)	(2.2)	(1.8)	(1.6)	(1.4)
Provisions/Assets	(0.3)	(0.4)	(0.5)	(0.2)	(0.2)
Taxes/Assets	(0.8)	(0.9)	(0.9)	(0.8)	(0.8)
Total costs/Assets	(3.7)	(3.5)	(3.2)	(2.5)	(2.3)
ROA	1.5	1.6	1.7	1.6	1.5
Equity/Assets	7.9	7.8	8.3	7.5	6.4
ROAE	19.0	20.6	20.3	20.9	23.4



**Valuation metrics**

Year to March	FY08	FY09	FY10	FY11E	FY12E
Diluted EPS (INR)	6.8	10.2	14.1	21.0	29.0
<i>EPS growth (%)</i>	<i>102.8</i>	<i>51.1</i>	<i>37.5</i>	<i>49.5</i>	<i>38.1</i>
Book value per share (INR)	44.6	54.7	91.0	110.2	137.5
Adjusted book value/share (INR)	44.4	53.7	90.7	110.0	137.3
Diluted P/E (x)	52.1	34.4	25.1	16.8	12.1
Price/ BV (x)	7.9	6.4	3.9	3.2	2.6
Price/ ABV (x)	7.9	6.6	3.9	3.2	2.6
Dividend yield (%)	0.0	0.0	0.4	0.4	0.4
Price to income (x)	23.3	20.6	16.5	13.1	10.2
Price to PPOP (x)	35.8	26.1	15.5	10.3	7.5



Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Allahabad Bank	BUY	SO	H	Axis Bank	BUY	SO	M
Bank of Baroda	BUY	SO	L	Federal Bank	BUY	SO	M
HDFC	HOLD	SU	L	HDFC Bank	HOLD	SP	L
ICICI Bank	BUY	SO	L	Indian Overseas Bank	HOLD	SU	H
Infrastructure Development Finance Co Ltd	HOLD	SU	M	ING Vysya	BUY	SP	H
Karnataka Bank	BUY	SO	L	Kotak Mahindra Bank	BUY	SP	L
LIC Housing Finance	BUY	SP	M	Manappuram General Finance	HOLD	SU	M
Oriental Bank Of Commerce	BUY	SU	H	Power Finance Corp	BUY	SO	L
Punjab National Bank	BUY	SO	L	Reliance Capital	HOLD	SP	M
Rural Electrification Corporation	BUY	SO	L	Shriram City Union Finance	BUY	SP	H
South Indian Bank	BUY	SO	H	SREI Infrastructure Finance	UNDER REVIEW	SO	L
State Bank of India	BUY	SP	L	Syndicate Bank	BUY	SP	H
Union Bank Of India	BUY	SO	L	Yes Bank	BUY	SO	M

## ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

## RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

## RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

## SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

Edelweiss  
Ideas create, values protect



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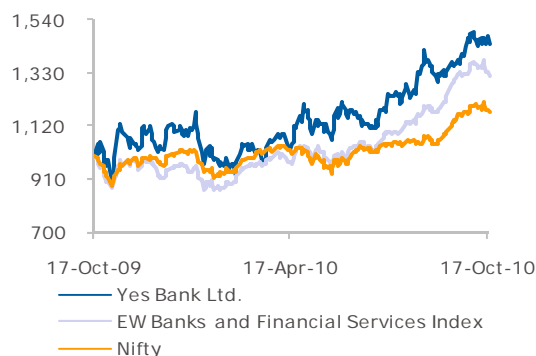
**Coverage group(s) of stocks by primary analyst(s): Banking and Financial Services**

Allahabad Bank, Axis Bank, Bank of Baroda, Federal Bank, HDFC, HDFC Bank, ICICI Bank, Infrastructure Development Finance Co Ltd, Indian Overseas Bank, Karnataka Bank, Kotak Mahindra Bank, LIC Housing Finance, Manappuram General Finance, Oriental Bank Of Commerce, Punjab National Bank, Power Finance Corp, Reliance Capital, Rural Electrification Corporation, State Bank of India, Shriram City Union Finance, South Indian Bank, Syndicate Bank, SREI Infrastructure Finance, Union Bank Of India, ING Vysya, Yes Bank

**Yes Bank**



**EW Indices**



**Distribution of Ratings / Market Cap**

**Edelweiss Research Coverage Universe**

	Buy	Hold	Reduce	Total
Rating Distribution*	116	45	12	176
* 3 stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	110	53	13	

**Recent Research**

Date	Company	Title	Price (INR)	Recos
19-Oct-10	<b>HDFC Bank</b>	Marching on; <i>Result Update</i>	2,369	Hold
19-Oct-10	<b>Manappuram General Finance</b>	Growth strong; valuations fair; <i>Result Update</i>	139	Hold
18-Oct-10	<b>ING Vysya Bank</b>	Receding concerns on asset quality and growth; <i>Result Update</i>	381	Buy

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