



## Vijaya Bank

STOCK INFO.	BLOOMBERG
BSE SENSEX: 12,858	VJYBK IN
	REUTERS CODE
S&P CNX: 3,711	VJBK.BO

18 October 2006

Neutral

Previous Recommendation: Neutral

Rs56

Equity Shares (m)	433.5
52-Week Range	72/33
1,6,12 Rel.Perf.(%)	2/-2/-61
M.Cap. (Rs b)	24.5
M.Cap. (US\$ b)	0.5

YEAR	NET INCOME	PAT	EPS	EPS	P/E	P/BV	CAR	ROE	ROA	P/ABV
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	(%)	(X)
3/06A	13,418	1,269	2.9	-66.6	19.3	1.5	11.9	7.8	0.4	1.6
3/07E	13,705	2,915	6.7	129.7	8.4	1.3	11.1	16.5	0.9	1.4
3/08E	15,680	3,776	8.7	29.6	6.5	1.1	10.3	18.8	0.9	1.2

Vijaya Bank 2QFY07 results were below our expectation. NII grew by only 11.6% YoY to Rs2.6b against our expectation of 16% growth. Loan book grew by 26% YoY in 2QFY07, while deposits have grown at 23% YoY. NIMs in 1HFY07 declined by 24bp YoY to 3.1%, as falling CASA resulted in increase in cost of deposits. Vijaya Bank's treasury gains declined 75% YoY. Non-interest income, other than treasury, growth was steady at 20% YoY. Asset quality improved further with gross NPAs and net NPAs declining to 2.6% and 0.6%, respectively in 2QFY07.

- ✍ Business growth steady; Deposit up by 23% while advances grow by 26%
- ✍ NII growth disappoints; Margins decline
- ✍ Core other income grows 20% YoY; treasury income declines
- ✍ Asset quality stable

Post 2QFY07 results, on back of margin pressure we have lowered our NII growth estimates for FY07 by 3%, although on back of expected lower provisions, we have upgraded our earnings by 3%. We expect the bank to report an EPS of Rs6.7 in FY07E and Rs8.7 in FY08E. At CMP, the stock is trading at a P/E of 6.5x FY08E EPS and P/BV of 1.1x FY08E BV. We maintain **Neutral**.

### QUARTERLY PERFORMANCE

(RS MILLION)

Y/E MARCH	FY 06				FY 07				FY 06	FY 07E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Interest Income	5,550	5,715	5,953	5,900	6,134	6,742	6,965	7,127	23,118	26,968
Interest Expense	3,178	3,386	3,362	3,464	3,551	4,144	4,244	4,300	13,390	16,239
<b>Net Interest Income</b>	<b>2,372</b>	<b>2,329</b>	<b>2,591</b>	<b>2,436</b>	<b>2,583</b>	<b>2,598</b>	<b>2,721</b>	<b>2,828</b>	<b>9,728</b>	<b>10,730</b>
% Change (Y-o-Y)	1.5	-4.5	3.4	-5.0	8.9	11.6	5.0	16.1	-1.2	10.3
Other Income	1,027	941	731	992	866	718	685	706	3,690	2,975
<b>Net Income</b>	<b>3,399</b>	<b>3,269</b>	<b>3,322</b>	<b>3,428</b>	<b>3,450</b>	<b>3,316</b>	<b>3,406</b>	<b>3,534</b>	<b>13,418</b>	<b>13,705</b>
% Change (Y-o-Y)	-2.3	-0.1	4.0	-0.2	1.5	1.4	2.5	3.1	0.4	2.1
Operating Expenses	1,376	1,634	1,612	1,613	1,498	1,550	1,725	1,733	6,235	6,507
<b>Operating Profit</b>	<b>2,023</b>	<b>1,635</b>	<b>1,710</b>	<b>1,815</b>	<b>1,951</b>	<b>1,766</b>	<b>1,681</b>	<b>1,800</b>	<b>7,182</b>	<b>7,198</b>
Other Provisions	1,944	536	731	2,177	1,105	475	740	830	5,388	3,150
Tax Provisions	-196	348	390	-17	120	268	269	477	526	1,133
<b>Net Profit</b>	<b>275</b>	<b>751</b>	<b>588</b>	<b>-345</b>	<b>726</b>	<b>1,023</b>	<b>672</b>	<b>493</b>	<b>1,269</b>	<b>2,915</b>
% Change (Y-o-Y)	-71.8	5.2	5.7	-122.1	163.7	36.3	14.2	NA	-66.6	129.7
Cost to Income Ratio (%)	40.5	50.0	48.5	47.1	43.4	46.7	50.7	49.0	46.5	47.5
Interest Expense/Interest Income (%)	57.3	59.3	56.5	58.7	57.9	61.5	60.9	60.3	57.9	60.2
Other Income/Net Income (%)	30.2	28.8	22.0	28.9	25.1	21.7	20.1	20.0	27.5	21.7

E: MOST Estimates

Vijaya Bank 2QFY07 results were below our expectation. NII grew by only 11.6% YoY to Rs2.6b against our expectation of 16% growth. Loan book grew by 26% YoY in 2QFY07, while deposits have grown at 23% YoY. NIMs in 1HFY07 declined by 24bp YoY to 3.1%, as falling CASA resulted in increase in cost of deposits. Vijaya Bank's treasury gains declined 75% YoY. Non-interest income, other than treasury, growth was steady at 20% YoY. Asset quality improved further with gross NPAs and net NPAs declining to 2.6% and 0.6%, respectively in 2QFY07.

### Deposit up by 23% while advances grow by 26%

Vijaya Bank reported a YoY business growth of 24% to Rs516b, with net advances growing by 26% YoY to Rs196b and deposits growing by 23% to Rs320b in 2QFY07. Bank is targeting total business of Rs600b by FY07, comprising deposits of Rs360b and advances of Rs240b.

Net advances grew by 26% YoY to Rs196b in 2QFY07. The growth in advances came from all quarters; with retail Advances growth of 20% YoY to Rs68b. Priority sector advances grew by 15% YoY to Rs84b as against Rs74b in 2QFY06. Priority sector advances as percentage to net bank advances stood at 43.5% in 2QFY07. Agricultural advances increased from Rs23b in 2QFY06 to Rs26b, recording a growth of 12% YoY. Agricultural advances now constitute 13.4% of net bank advances. Advances to SMEs stood at Rs14.7b constituting 7.6% of net bank advances, while advances to SSI stood at Rs10.6b constituting 5.5% of net bank advances.

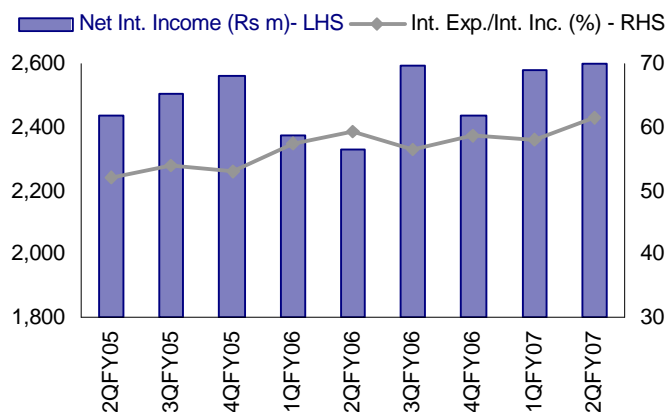
Deposits also grew by 23% to Rs320b, with CASA growing by 19% YoY to Rs102b in 2QFY07. Savings deposits increased from Rs58b to Rs70b YoY, recording growth of 22% in 2QFY07. Demand deposits increased from Rs28b to Rs32b, recording a growth of 13%. However, percentage of low cost deposit to total deposits has declined YoY from 33% to 32% in 2QFY07.

### NII growth disappoints; margins decline

NII grew by only 11.6% YoY to Rs2.6b against our expectation of 16% growth. The bank also had a one-time

interest on income tax refund of Rs68m in 2QFY07, excluding which NII growth is 8.6% YoY. Decline in CASA resulted in banks interest expense increasing faster than income resulting in lower NII growth.

#### TREND IN NII



Source: Company / Motilal Oswal Securities

NIMs in 1HFY07 declined by 24bp YoY to 3.1%, as falling CASA resulted in increase in cost of deposits from 4.96% in 1HFY06 to 5.2% in 1HFY07. Investment yields were relatively stable, while advances yields moved up by 21bp YoY to 9.1% in 1HFY07. Management expects margins to improve from 3QFY07 on back of PLR increase (effective from second week of September 2006 by 25bp) effect coming in to play.

#### NIMS BREAK-DOWN (%)

	1HFY06	FY06	1QFY07	1HFY07
Yield on Advances	8.86	8.83	9.02	9.07
Yield on Investments	8.00	8.10	7.99	7.97
Cost of Funds	4.40	4.43	4.56	4.68
Cost of Deposits	4.96	4.97	5.02	5.20
<b>Net Interest Margins</b>	<b>3.36</b>	<b>3.20</b>	<b>3.34</b>	<b>3.12</b>

Source: Company / Motilal Oswal Securities

### Core other income grows 20% YoY; treasury income declines

Vijaya bank's core other income grew YoY by 20% to Rs612m in 2QFY07. Vijaya Bank's treasury gains declined 75% YoY. 70% of bank's investment book is in HTM and on the AFS front, the duration has been reduced to 0.9 years, with a cushion up to 8%.

### Provisions lower than expectations

Vijaya bank made provisions of Rs475m in 2QFY07, as against our expectation of Rs650m. Vijaya bank has written-back Rs230m of investment provision in 2QFY07 due to a decline in yields. NPA provisions were higher on QoQ basis to Rs373m. The bank has changed the method of amortization of premium on investment under HTM category from Straight Line Method to Constant Yield Method from 1QFY07, resulting in lower amortization to the extent of Rs92m in 2QFY07.

#### PROVISIONS (RS M)

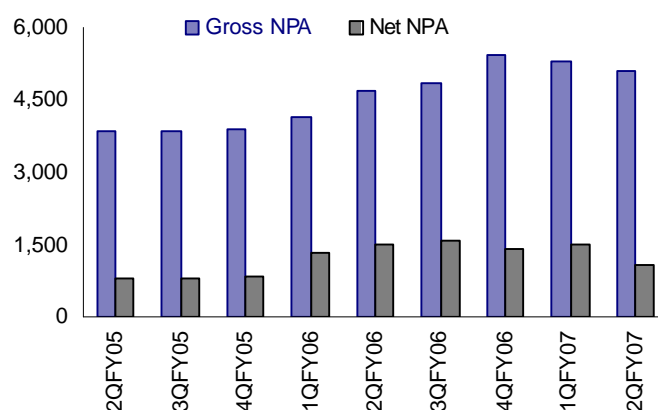
	2QFY07
NPA	373
Std. Asset	116
Bad Debt Written-off	49
Amortization	168
Dep. Write-back	-230
<b>Total Provisions</b>	<b>475</b>

Source: Company / Motilal Oswal Securities

### Asset quality stable

Asset quality improved further with gross NPAs and net NPAs declining to 2.6% and 0.6%, respectively in 2QFY07. In absolute basis, gross NPAs and net NPAs on QoQ basis have declined by 4% and 36%, respectively. Provision cover now stands at 79%.

#### TREND IN NPAs



Source: Company / Motilal Oswal Securities

### Valuation and view

Post 2QFY07 results, on back of margin pressure we have lowered our NII growth estimates for FY07 by 3%, although on back of expected lower provisions, we have upgraded our earnings by 3%. We expect the bank to report an EPS of Rs6.7 in FY07E and Rs8.7 in FY08E. At CMP, the stock is trading at a P/E of 6.5x FY08E EPS and P/BV of 1.1x FY08E BV. We maintain **Neutral**.

## Vijaya Bank: an investment profile

### Company description

Vijaya Bank, established in 1932, is a mid-sized Bangalore based state-owned bank having a balance sheet size of Rs~340b. The bank has made public offerings in 2001 and 2003, after which the government's stake has reduced to 54%. It has a network of 929 branches, with approximately 386 branches under CBS covering almost 75% of bank's business.

### Key investment arguments

- ✍ Consistently grown its loan book with greater thrust on retail advances.
- ✍ Asset quality is one of the best in the sector with net NPAs at 0.6%.
- ✍ Sufficient capital adequacy ratio of 11.8%, of which Tier 1 is 8.5%.

### Key investment risks

- ✍ Since the government's stake is 54%, there is not much room for further dilution.

### Recent developments

- ✍ Mr T Valliappan was recently appointed Executive Director of Vijaya Bank.
- ✍ Vijaya Bank has raised Rs2.5b through a 10-year bond issue. These bonds, rated AA+ are priced at 9.25% and would comprise part of the banks Tier-II capital.

### Valuation and view

- ✍ Healthy loan growth, clean asset portfolio makes Vijaya Bank an efficient bank.
- ✍ The stock trades at 6.5x FY08E EPS and 1.1x FY08E BV. We maintain **Neutral**.

### Sector view

- ✍ YTD loan growth of 30%+, highest in last 12 years.
- ✍ Volatility in interest rates would impact treasury income.
- ✍ Benefits of significant improvement in asset quality not yet factored in earnings, valuations.
- ✍ We maintain an overweight stance on the sector.

#### COMPARATIVE VALUATIONS

		VIJAYA BANK	PNB	CANARA
P/E (x)	FY07E	8.4	10.4	8.0
	FY08E	6.5	7.9	7.0
P/ABV (x)	FY07E	1.4	1.6	1.5
	FY08E	1.2	1.4	1.2
RoE (%)	FY07E	16.5	15.7	18.7
	FY08E	18.8	18.1	18.5
RoA (%)	FY07E	0.9	1.0	1.0
	FY08E	0.9	1.2	1.1

#### SHAREHOLDING PATTERN (%)

	SEP-06	JUN-06	SEP-05
Promoter	53.9	53.9	53.9
Domestic Inst	5.2	5.8	6.6
Foreign	18.6	16.8	17.9
Others	22.3	23.5	21.6

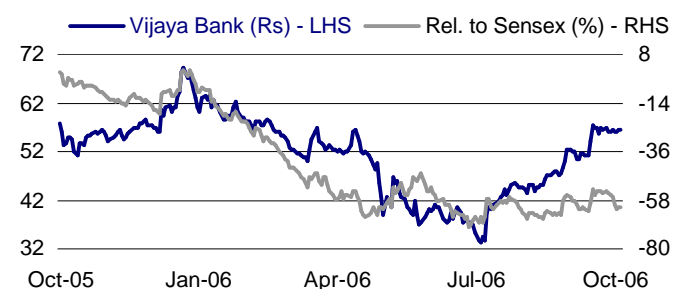
#### EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	6.7	7.0	-4.3
FY08	8.7	8.3	4.8

#### TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
56	63	11.6	Neutral

#### STOCK PERFORMANCE (1 YEAR)



**INCOME STATEMENT** (Rs Million)

Y/E MARCH	2005	2006	2007E	2008E	2009E
Interest Income	20,943	23,118	26,968	32,083	38,517
Interest Expended	11,098	13,390	16,239	19,679	23,975
<b>Net Interest Income</b>	<b>9,845</b>	<b>9,728</b>	<b>10,730</b>	<b>12,405</b>	<b>14,541</b>
Change (%)	17.5	-12	10.3	15.6	17.2
Other Income	3,513	3,690	2,975	3,275	3,400
<b>Net Income</b>	<b>13,359</b>	<b>13,418</b>	<b>13,705</b>	<b>15,680</b>	<b>17,941</b>
Change (%)	-2.0	0.4	2.1	14.4	14.4
Operating Expenses	5,492	6,235	6,507	7,060	7,681
<b>Operating Income</b>	<b>7,867</b>	<b>7,182</b>	<b>7,198</b>	<b>8,619</b>	<b>10,260</b>
Change (%)	-9.1	-8.7	0.2	19.7	19.0
Other Provisions	4,142	5,388	3,150	3,375	3,900
<b>PBT</b>	<b>3,725</b>	<b>1,795</b>	<b>4,048</b>	<b>5,244</b>	<b>6,360</b>
Tax	-78	526	1,133	1,468	1,781
Tax Rate (%)	-2.1	29.3	28.0	28.0	28.0
<b>PAT</b>	<b>3,802</b>	<b>1,269</b>	<b>2,915</b>	<b>3,776</b>	<b>4,579</b>
Change (%)	-7.6	-66.6	129.7	29.6	21.3
Proposed Dividend	1,225	434	867	1,084	1,301

**BALANCE SHEET** (Rs Million)

Y/E MARCH	2005	2006	2007E	2008E	2009E
Capital	4,335	4,335	4,335	4,335	4,335
Reserves & Surplus	11,557	12,356	14,404	17,096	20,375
<b>Net Worth</b>	<b>15,892</b>	<b>16,692</b>	<b>18,739</b>	<b>21,431</b>	<b>24,710</b>
<b>Deposits</b>	<b>256,180</b>	<b>277,093</b>	<b>324,199</b>	<b>379,312</b>	<b>443,796</b>
Change (%)	21.9	8.2	17.0	17.0	17.0
Borrowings	6,408	5,164	5,680	6,248	6,873
Other Liabilities & Prov.	14,875	16,398	18,858	21,687	24,940
<b>Total Liabilities</b>	<b>293,355</b>	<b>315,346</b>	<b>367,476</b>	<b>428,678</b>	<b>500,318</b>
Current Assets	16,146	28,351	32,755	35,570	35,682
Investments	120,687	111,797	117,387	123,256	131,884
Change (%)	11.4	-7.4	5.0	5.0	7.0
Advances	143,358	166,640	208,300	260,375	322,865
Change (%)	29.8	16.2	25.0	25.0	24.0
Net Fixed Assets	2,176	2,030	2,180	2,280	2,330
Other Assets	10,988	6,528	6,854	7,197	7,556
<b>Total Assets</b>	<b>293,355</b>	<b>315,346</b>	<b>367,476</b>	<b>428,678</b>	<b>500,318</b>

**ASSUMPTIONS** (%)

Deposit Growth	21.9	8.2	17.0	17.0	17.0
Advances Growth	29.8	16.2	25.0	25.0	24.0
Investments Growth	11.4	-7.4	5.0	5.0	7.0
Dividend	28.3	10.0	20.0	25.0	30.0
CRR	5.0	5.0	5.0	5.0	5.0

E: MOST Estimates

**RATIOS**

Y/E MARCH	2005	2006	2007E	2008E	2009E
<b>Spreads Analysis (%)</b>					
Avg. Yield - Earning Asset	8.2	7.9	8.3	8.5	8.6
Avg. Cost-Int. Bear. Liab.	4.7	4.9	5.3	5.5	5.7
Interest Spread	3.6	3.0	3.0	3.0	2.9
Net Interest Margin	3.9	3.3	3.3	3.3	3.2

**Profitability Ratios (%)**

RoE	26.0	7.8	16.5	18.8	19.8
RoA	14	0.4	0.9	0.9	10
Int. Expended/Int. Earned	53.0	57.9	60.2	61.3	62.2
Other Inc./Net Income	26.3	27.5	21.7	20.9	19.0

**Efficiency Ratios (%)**

Op. Exps./Net Income	41.1	46.5	47.5	45.0	42.8
Empl. Cost/Op. Exps.	58.1	60.8	58.8	58.0	56.9
Busi. per Empl. (Rs m)	31.3	36.7	42.1	50.1	59.6
NP per Empl. (Rs lac)	0.3	0.1	0.3	0.3	0.4

**Asset-Liability Profile (%)**

Adv./Deposit Ratio	56.0	60.1	64.3	68.6	72.8
Invest./Deposit Ratio	47.1	40.3	36.2	32.5	29.7
G-Sec/Invest. Ratio	87.5	85.2	89.2	89.2	87.6
Gross NPAs to Adv.	2.9	3.2	2.8	2.5	2.2
Net NPAs to Adv.	0.6	0.9	0.7	0.7	0.6
CAR	12.9	11.9	11.1	10.3	10.5
Tier 1	7.6	9.3	8.0	7.3	7.1

**VALUATION**

Book Value (Rs)	36.7	38.5	43.2	49.4	57.0
Price-BV (x)	15	15	13	11	10
Adjusted BV (Rs)	35.4	36.4	40.9	46.7	53.9
Price-ABV (x)	1.6	1.6	1.4	1.2	1.0
EPS (Rs)	8.8	2.9	6.7	8.7	10.6
EPS Growth (%)	-7.6	-66.6	129.7	29.6	21.3
Price-Earnings (x)	6.4	19.3	8.4	6.5	5.3
OPS (Rs)	18.1	16.6	16.6	19.9	23.7
OPS Growth (%)	-9.1	-8.7	0.2	19.7	19.0
Price-OP (x)	3.1	3.4	3.4	2.8	2.4

E: MOST Estimates

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<b>Disclosure of Interest Statement</b>	<b>Vijaya Bank</b>
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No



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