

ICICI Bank

 BSE code: 532174
 NSE code: ICICIBK

CMP: Rs 918
Target: Rs 1,080
SUBSCRIBE

Abhishek Agarwal (91-22) 6612 4753 abhishek.a@religare.in	Dinesh Shukla (91-22) 6612 4739 dinesh.shukla@religare.in
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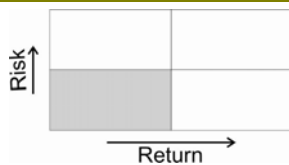
Company data

Particulars	
Market cap (Rs bn / US\$ bn)	825.6/ 20.1
Outstanding equity shares (bn)	0.9
52-week high/low (Rs)	1,007/465
2-month average daily volume	305,744

Financial snapshot

Particulars	FY07	FY08E	FY09E
NII (Rs bn)	66.4	87.3	113.6
Growth (%)	40.9	31.6	30.1
Adj net profit (Rs bn)	31.1	41.1	53.2
Growth (%)	22.2	32.1	29.6
FDEPS (Rs)	34.6	36.7	47.5
Growth (%)	20.9	6.1	29.6
P/E (x)	26.6	25.0	19.3
RoE (%)	13.4	11.5	10.9

Risk-return profile



Shareholding pattern

(%)	Mar-07	Dec-06
Promoters	NA	NA
FIs	71.6	71.4
Banks & FIs	16.4	17.3
Public	12.0	11.3

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
ICICI Bank	918	(3.5)	11.4	5.8
Sensex	14,080	(1.6)	18.9	8.2
BSE Bankex	7,479	(1.6)	10.8	5.2

Hitting the high notes

Strong business growth to continue; Recommend Subscribe to follow-on issue

Investment rationale

- ❖ Follow-on public issue in the domestic market along with an ADS offering of equity for a total of Rs 200bn
- ❖ Issue to be highly book-value accretive with BV expected to rise to Rs 424 at the end of FY08 from Rs 274 as at end-FY07
- ❖ Business to continue growing faster than the industry, with a focus on raising CASA deposits; Increasing low-cost deposits and infusion of funds via equity offering to strengthen margins
- ❖ RoE to improve as further equity dilution is unlikely over the next 2-3 years; Subsidiary insurance business expected to fund capital requirements independently, improving financial leverage
- ❖ Recent sale of stake in ICICI Financial Services (IFSL) has resulted in enhanced subsidiary valuations

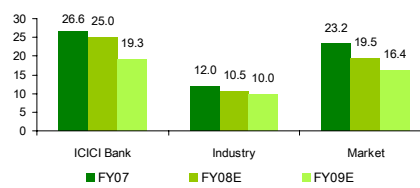
Key concerns

- ❖ Higher NPLs would continue to be a key concern in the rising interest rate environment; however, most retail loans are secured by collateral
- ❖ Any diversion of funds to meet the capital requirement of subsidiaries could impact RoE and may lead to earlier-than-expected equity dilution

Valuation

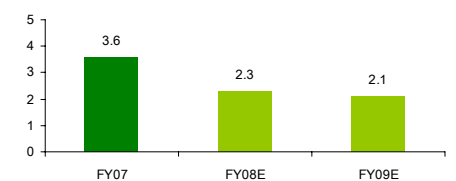
- ❖ We have valued ICICI Bank at Rs 1,080 on the basis of an SOTP valuation, after assigning a 25% holding discount for its 100% stake in IFSL; Subscribe

P/E multiple (x)



Source: Religare Research

P/ABV multiple (x)



Source: Religare Research

Equity issue of Rs 200bn

Issue comprises domestic and ADS offering in equal proportion

ICICI Bank is coming out with a follow-on equity issue in the domestic market to raise Rs 87.5bn (excluding a greenshoe option of Rs 13.1bn). The price band of the issue has been fixed at Rs 885-950, and is slated to open on 19 June 2007 and close on 22 June 2007. The bank will also be raising an equivalent amount from an ADS offering. This will be the third time in the last four years that the bank has tapped the capital markets to raise funds in order to support its aggressive growth. We believe the current issue would be sufficient to meet capital requirements for the next 2-3 years.

Issue size

	Total*
Issue (Rs bn)	175.0
Greenshoe option (Rs bn)	26.3
Total (Rs bn)	201.3
No. of shares (bn) @ Rs 950	0.21
No. of shares (bn) @ Rs 885	0.23

Source: Company, Religare Research *Issue comprises domestic and ADS offering of equity in equal proportion

Mode of payment

	Retail bidders & existing shareholders	Non-institutional bidders
On submission of bid-cum-application form	Rs 250	Rs 250
On allotment	Rs 250	Balance amount
On first call (within 6 mths)	Balance amount	
OR		
On submission of bid-cum-application form	100% of bid amt	100% of bid amt

Source: Company, Religare Research

We estimate that BV will rise to Rs 424 at the end of FY08 from Rs 274 as at end-FY07

Equity issue to be highly book-value accretive

The equity offering amounts to 23-25% of the pre-issue equity capital. The current offering, at the price band of Rs 885-950, would be highly book-value accretive considering the end-FY07 book value (BV) of Rs 274. We estimate that BV would increase to Rs 424 at the end of FY08.

Business update

Higher corporate loan demand to offset slowing retail growth

Retail lending has been the key loan growth driver for ICICI Bank over the last 2-3 years. The management now expects retail lending to slow down to around 20-25% levels during the current fiscal from 39% in FY07. However, the slower growth in retail lending would be offset by higher demand for loans from the corporate segment. Further, the bank is focusing on the rural segment as well as international business to drive growth.

Enhanced focus on raising low-cost deposits...

ICICI Bank's CASA deposits have remained low compared to peers, largely because substantial funding requirements were met through erstwhile ICICI borrowings. Delays in obtaining branch licenses also hampered the growth of CASA deposits. However, with the acquisition of Sangli Bank and the set up of 141 new branches in Q4FY07, we expect the bank to garner more low-cost deposits in future. Further, with the infusion of funds from its current equity offering, we believe ICICI Bank would be able to reduce its dependence on deposits for funding and thus curtail its cost of funds.

Increased CASA deposits and infusion of funds via equity offering to strengthen NIM

...leading to improved margins

So far, the higher cost of funding has put pressure on the bank's net interest margins (NIM). Going ahead, the likely increase in proportion of CASA deposits and availability of funds from the equity offering would strengthen the bank's NIM.

Collateral-based loans reduce risk of NPLs

Incrementally higher NPLs could continue to be a big concern for ICICI Bank, considering that annual loan growth over the last three years has been in the region of 40-45%. But since a major portion of the lending has been towards the retail segment (especially housing), where loans are secured by collateral, we believe that NPLs would not pose a serious problem.

Return ratios expected to improve

ICICI Bank's relatively lower RoE (at 13.4% in FY07) could be explained by the fact that it has funded substantial capital requirements of its subsidiaries which are yet to yield returns. Further, the bank's aggressive retail lending strategy necessitated frequent equity infusion to sustain capital adequacy. The management has now stated that the proceeds from the current issue would be fully utilised towards meeting credit demand, while the capital needs of its subsidiary insurance business would be independently met by the insurance company. Thus, with the increased leverage, the bank's RoE should start improving.

Sale of 5.9% stake in IFSL for Rs 26.5bn values subsidiary at Rs 401/share of ICICI Bank

Stake sale in ICICI Financial Services has enhanced subsidiary valuations

ICICI Bank has transferred its stake in four businesses to its 100% subsidiary – ICICI Financial Services (IFSL – formerly ICICI Holdings), as shown in the table below. Further, the bank has received firm commitments from investors for buying a 5.9% stake in IFSL for Rs 26.5bn. At this price, the subsidiary would be valued at Rs 449bn or Rs 401/share of ICICI Bank. This valuation is at a substantial premium to consensus expectations.

Transfer of businesses to ICICI Financial Services

Businesses transferred	ICICI Bank's stake (%)
ICICI Prudential Life Insurance Company	74
ICICI Lombard General Insurance	74
Prudential ICICI Asset Management Company	51
Prudential ICICI Trust	51

Source: Company

Valuation

SOTP target price of Rs 1,080

We have valued ICICI Bank using a sum-of-the-parts approach (SOTP). If we were to consider the pricing of the above stake sale, the fair value for ICICI Bank including its investments in other subsidiaries would work out to Rs 1,180. However, considering that IFSL is a 100% subsidiary, we have built in a 25% holding company discount, which gives us a target price of Rs 1,080.

SOTP valuation

(Rs/share)	Ascribing full value to IFSL	Ascribing 25% holding company discount for IFSL
Value of ICICI Bank (standalone)	724.6	724.6
Value of IFSL (Life insurance, general insurance, AUM)	401.3	300.9
Other investments	54.4	54.4
Total	1,180.3	1,080.0

Source: Religare Research

Trades at a discount to peers...

At Rs 355/share, the value of subsidiaries and other investments comprises a substantial portion of ICICI Bank's fair value. The bank's core valuation of Rs 725/share is at discount to other leading private banks. After the Rs 200bn domestic and ADS equity offerings, the stock would trade at P/ABV multiples of 2.3x and 2.1x on FY08E and FY09E respectively. The lower valuation is primarily on account of lower margins and return ratio parameters.

...but valuation parameters to improve; Subscribe

We believe ICICI Bank merits a higher valuation considering its position as the second largest bank in India, expected improvement in RoE over the next 2-3 years, and its stronghold in the private insurance business. We thus recommend that investors Subscribe to the issue.

**Available at a discount to
other leading private banks;
Subscribe**

Financials

Profit and Loss statement

(Rs bn)	FY06	FY07	FY08E	FY09E
Interest earned	143.1	229.9	310.3	403.9
Interest expended	96.0	163.6	223.0	290.3
Net interest income	47.1	66.4	87.3	113.6
Growth (%)	46.8	40.9	31.6	30.1
Non-interest income	41.8	59.3	72.0	87.8
Comm, Exchange & Brokerage	30.0	43.3	55.2	69.0
Growth (%)	33.2	41.8	21.4	22.0
Operating expenses	50.0	66.9	87.4	113.1
Pre-provisioning profits	38.9	58.7	71.9	88.3
Growth (%)	45.1	51.1	22.4	22.8
Provisions & contingencies	7.9	22.3	22.2	23.0
PBT	31.0	36.5	49.8	65.3
Income tax, Interest tax	5.5	5.4	8.7	12.1
Net profit	25.4	31.1	41.1	53.2
Growth (%)	26.7	22.2	32.1	29.6

Source: Company, Religare Research

Balance sheet

(Rs bn)	FY06	FY07E	FY08E	FY09E
Cash in hand & bal with RBI	89.3	187.1	225.3	268.7
Balance with banks, Money at call	81.1	184.1	211.8	232.9
Investments	715.5	912.6	1,103.2	1,326.2
Advances	1,461.6	1,958.7	2,610.9	3,355.0
Fixed assets (net)	39.8	39.2	40.2	41.2
Other assets	126.6	164.9	206.1	257.7
Total assets	2,513.9	3,446.6	4,397.5	5,481.7
Equity capital	12.4	12.5	14.7	14.7
Reserves & surplus	213.2	234.1	460.0	497.2
Net worth	222.1	243.1	471.2	508.4
Deposits	1,650.8	2,305.1	2,888.5	3,681.4
Current deposits (a)	165.7	213.8	272.5	350.2
Savings bank deposits (b)	209.4	288.4	389.3	525.6
Term deposits (c)	1,275.7	1,803.0	2,226.7	2,805.6
Borrowings (incl sub-ord bonds)	486.7	706.6	834.0	996.7
Other liabilities & provisions	150.8	188.2	200.3	291.6
Total liabilities	2,513.9	3,446.6	4,397.5	5,481.7

Source: Company, Religare Research

Recommendation history

Date	Event	Target (Rs)	Reco
19-June-07	FPO Note	1,080	Subscribe

Source: Religare Research

Key ratios

Year-end March	FY06	FY07E	FY08E	FY09E
Per share data				
Shares outstanding (bn)	0.9	0.9	1.1	1.1
EPS (Rs)	28.6	34.6	36.7	47.5
DPS (Rs)	8.5	10.0	10.0	12.5
Book value (Rs)	253.5	274.2	424.1	457.4
Adjusted book value (Rs)	241.7	252.1	400.8	427.4

Valuation ratios

Market price	918.0	918.0	918.0	918.0
P/E (x)	32.1	26.6	25.0	19.3
P/BV (x)	3.6	3.3	2.2	2.0
P/ABV (x)	3.8	3.6	2.3	2.1

Earnings quality (%)

Net interest margin	2.5	2.4	2.4	2.5
Yield on advances	8.6	9.4	9.9	10.2
Yield on investments	6.1	7.4	7.5	7.5
Cost of funds	4.4	5.9	6.3	6.7
Cost/Income	56.3	53.2	54.9	56.2
Return on average net worth	14.6	13.4	11.5	10.9
Return on average assets	1.2	1.0	1.0	1.1

Growth ratios (%)

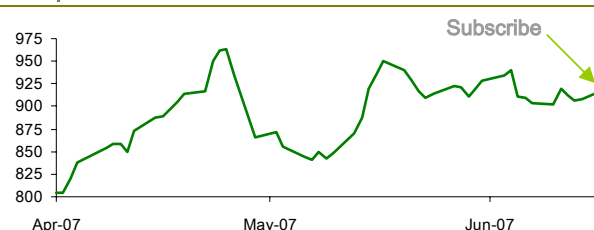
Net interest income	46.8	40.9	31.6	30.1
Other income	33.2	41.8	21.4	22.0
Total income	40.0	41.3	26.8	26.4
Pre-provisioning profit	45.1	51.1	22.4	22.8
Net profit	26.7	22.2	32.1	29.6
Advances	59.9	34.0	33.3	28.5
Deposits	65.4	39.6	25.3	27.4

Asset quality

Proportion of low-cost deposits (%)	22.7	21.8	22.9	23.8
Credit-Deposit ratio (x)	88.5	85.0	90.4	91.1
Investment/Deposit (%)	43.3	39.6	38.2	36.0
Net NPA ratio	0.7	1.0	1.0	1.0
CAR	13.3	11.7	14.6	12.3
Tier-I ratio	9.2	7.4	11.0	9.4

Source: Company, Religare Research

Stock performance



Source: Religare Research

RELIGARE RESEARCH

Fundamental Research

Amitabh Chakraborty, CFA, FRM	President - Equity	amitabh.chakraborty@religare.in	(91-22) 6612 4603
Piyush Parag	Auto, Auto Ancillaries, Shipping	piyush.parag@religare.in	(91-22) 6612 4730
Abhishek Agarwal	Bank, Agri-Commodities	abhishek.a@religare.in	(91-22) 6612 4753
Dinesh Shukla	Bank, Agri-Commodities	dinesh.shukla@religare.in	(91-22) 6612 4739
Ashish Kila	Capital Goods, Engineering, Power	ashish.kila@religare.in	(91-22) 6612 4768
Ronald Siyoni	Capital Goods, Engineering, Power	ronald.siyoni@religare.in	(91-22) 6612 4615
Dalpat Mehta	Cement, Textiles	dalpat.mehta@religare.in	(91-22) 6612 4696
Anurag Purohit	Information Technology, Telecom	anurag.purohit@religare.in	(91-22) 6612 4795
Hitesh Punjabi	Information Technology, Telecom	hitesh.punjabi@religare.in	(91-22) 6612 4769
Ram Patnaik	Media, FMCG	ram.patnaik@religare.in	(91-22) 6612 4752
Reema Deshkar	Media, FMCG	reema.deshkar@religare.in	(91-22) 6612 4764
Suman Memani	Mid-caps, Construction, Realty	suman.memani@religare.in	(91-22) 6612 4736
Sudeep Anand	Oil & Gas, Chemicals	sudeep.anand@religare.in	(91-22) 6612 4670
Bhawana Verma	Oil & Gas, Chemicals	bhawana.verma@religare.in	(91-22) 6612 4713
Alok Dalal	Pharmaceuticals	alok.dalal@religare.in	(91-22) 6612 4750

Derivatives Research

Anil Gupta	anil.g@religare.in	(91-22) 6612 4661
Samir Badami	samir.badami@religare.in	(91-22) 6612 4637
Somendra Agarwal	somendra.agarwal@religare.in	(91-22) 6612 4767

Production

Anisha deSa	anisha.desa@religare.in	(91-22) 6612 4729
R Murali	r.murali@religare.in	(91-22) 6612 4674
Rajesh Mhatre	rajesh.mhatre@religare.in	(91-22) 6612 4728

Administration

Shraddha Hosalkar	shraddha.hosalkar@religare.in	(91-22) 6612 4680
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Religare Securities Limited

Mumbai: 3rd Floor, Dheeraj Arma, Anant Kanekar Marg, Bandra (East), Mumbai-400 051. Phone: +91 22 66124600 Fax: +91 22 66124781

New Delhi: 19, Nehru Place, New Delhi - 110019, Phone: +91 11 30815100.

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