

YES BANK

INR 153

*Good growth off a small base*

BUY

YES BANK's Q4FY07 results were in line with our expectations. Net profit grew 102% Y-o-Y and 23% Q-o-Q to INR 309 mn. Net interest income growth of 84% Y-o-Y, was however, lower than our estimates which was offset by higher non-interest income.

Key Highlights

(1) Net interest income grew 84% Y-o-Y, (2) net interest margin declined by 40bps to 2.6%, (3) balance sheet expanded by 167% Y-o-Y, (4) fee-based income improved robustly by 132%, (5) number of branches increased to 40, and (6) the bank plans to launch retail brokerage business in FY08

We tweak our profit estimate slightly upwards for FY08E and FY09E while we expect 11% equity dilution in FY08E (earlier assumption 14%) and introducing 10% dilution in FY09E. This leads to revision in FY08E EPS estimate to INR 5 from INR 4.8 and in FY09E EPS estimate to INR 7.3 from INR 7.8. We expect the bank to deliver 47% EPS CAGR over FY07-09E. The stock currently trades at 3.5x FY08E book and 30x FY08E and 21x FY09E earnings. We like the bank for its high operating growth, quality management and strong traction from fee based income. We maintain 'BUY'.

* Business continues to grow strongly

Advances grew 161% to INR 63 bn, while deposits grew 182% to INR 82 bn. Share of SME loan book has declined slightly to 35% in March 2007. Corporate loans form 65% of the total loan book as against 63% in Q3FY07. Contribution from the retail credit, currently at less than 1%, is expected to improve further with the bank leveraging on its growing branch network. Investment book grew 127% to INR 31 bn. We expect the bank to attain 81% CAGR in loans over FY07-09E.

Cost of funds was high during this quarter due heavy reliance on wholesale funds, which put pressure on margins. Yield on advances declined sequentially due to the bank's priority sector lending during this quarter; rise in cost of funds decreased the NIMs by 42bps to 2.58%. The proportion of CASA in total deposits also came down to below 6% in March 2007 as against 7.3% in December 2006.

Financials

Year to March	Q4FY07	Q4FY06	growth %	Q3FY07	growth %	FY07E	FY08E
Net int. inc. (INR mn)	463	252	83.8	496	(6.7)	3,598	3,598
Net profit (INR mn)	309	153	101.7	251	23.1	943	1,547
B/V per share (INR)						28.1	44.2
EPS (INR)	1.1	0.6	93.0	0.9	18.3	3.4	5.0
Price/ Book (x)						5.4	3.5
Price/ PPOP (x)						25.3	15.7
Price/ Earnings (x)						45.4	30.6

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Reuters : YESB.BO
Bloomberg : YES IN

Market Data

52-week range (INR) : 171 / 67
Share in issue (mn) : 280.0
M cap (INR bn/USD mn) : 42.8 / 1,045.1
Avg. Daily Vol. BSE ('000) : 659.5

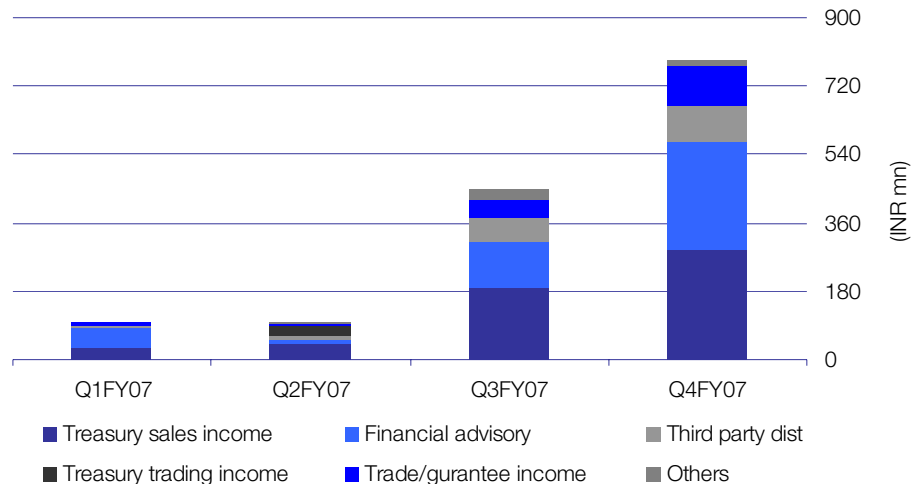
Share Holding Pattern (%)

Promoters : 35.9
MFs, Fls & Banks : 1.2
Fls : 49.3
Others : 13.5

*** Robust non-interest income**

Non-interest income grew 132% on the back of strong revenues from financial markets (customer-related treasury products) and financial advisory business. The major contribution was from the treasury segment that formed 37% of the total non-interest income. YES BANK was the lead manager of Advanta India Ltd’s IPO and is also the financial advisor and arranger to Suzlon Energy for its proposed acquisition of Repower systems. Third party distribution grew 50% over the quarter with trade and guarantee income doubling Q-o-Q. We expect the bank to deliver 45% CAGR in its fee income.

Chart 1: Strong traction in non interest income



Source: Company, Edelweiss research

*** Expanding reach**

The bank is in the process of expanding its branch network and has opened 13 more branches during this quarter, taking total number of branches to 40. It plans to increase its branches further (60 by June 2007), to give its retail venture a meaningful shape. The bank’s total number of employees is at 2443 as of March 2007 as against 2161 in December 2006.

*** Other details**

Provisions during the quarter were high at INR 127 mn. This is due to provision due to investment depreciation and higher general provisioning during the quarter. The provisions for NPA were nil as asset quality remained spotless. Asset quality for the bank remained healthy with zero net non-performing assets. The bank generated return on assets (RoA) of 1.28% and return of equity (RoE) of 16.4% in Q4FY07.

*** Capital infusion likely**

Capital adequacy stood at 13.6% (Tier I at 8.2%) as of March 2007. The bank infused INR 1.2 bn through equity placement to Swiss Re (at INR 120 per share) and raised subordinated debt (lower Tier II) of INR 1.8 bn during the year. It also raised INR 1.98 bn of upper Tier II during the quarter. We expect YES BANK to raise additional capital in next six months, and are therefore building in 10% equity dilution (around USD 100 mn) in FY08E. We are introducing 10% equity dilution in FY09E.

* Valuations

The stock currently trades at 3.5x FY08E book and 30x FY08E and 21x FY09E earnings. We expect the bank to deliver 15% ROE and 47% EPS CAGR over FY07-09E. We believe the stock should command higher multiple for its high potential growth. We like YES BANK for its strong management, ability to generate high fee income, high expected growth, and M&A probability (once the regulations ease). We maintain 'BUY'.

Financials snapshot							(INR mn)		
Year to March	Q4FY07	Q4FY06	Growth (%)	Q3FY07	Growth (%)	FY06	FY07	FY08E	
Interest on advances	1,467	477	207.7	1,214	20.8	1,361	4,226	10,597	
Interest on investments	498	172	189.3	373	33.5	476	1,467	4,110	
Interest on other resources	56	17	227.1	23	138.6	65	139	188	
Interest income	2,024	675	199.9	1,608	25.9	1,902	5,832	14,894	
Interest expenses	1,561	423	269.1	1,112	40.4	1,047	4,163	11,296	
Net interest income	463	252	83.8	496	(6.7)	855	1,669	3,598	
Fee Income	787	339	132.4	449	75.3	958	1,959	2,927	
Operating expenses	653	255	156.0	467	39.9	861	1,935	3,504	
Staff expense	391	146	167.3	273	43.2	501	1,175	2,274	
Other opex	262	109	140.7	194	35.3	360	760	1,230	
Pre prov profit (PPP)	598	336	78.0	479	24.8	952	1,694	3,022	
Provisions	127	89	42.5	98	29.7	147	288	767	
Profit before tax	471	247	90.9	381	23.5	845	1,436	2,355	
Provision for tax	162	93	73.1	130	24.3	291	493	808	
Profit after tax	309	153	101.7	251	23.1	554	943	1,547	
EPS (INR)	1.1	0.6	93.0	0.9	18.3	2.0	3.4	5.0	
Ratios									
NII / GII	22.9	37.3		30.9		44.9	28.6	24.2	
Cost - income	52.2	43.2		49.3		46.5	52.9	52.9	
Provisions / PPOP	21.2	26.5		20.4		15.4	17.0	25.4	
Tax rate	34.4	37.9		34.1		34.5	34.3	34.3	
Balance sheet data									
Advances (INR bn)	62.9	24.1	161.3	48.0	31.0	24.1	62.9	125.8	
Deposits (INR bn)	82.2	29.1	182.4	54.6	50.5	29.1	82.2	158.2	
Investments (INR bn)	30.7	13.5	127.4	22.2	38.4	13.5	30.7	46.0	
Net NPA(%)	0.0	0.0		0.0		0.0	0.0	0.1	
Capital adequacy (%)	13.6	16.4		14.3		16.4	13.6	10.8	
NIM (%)	2.6	3.3		3.0		3.3	2.4	2.6	

Company Description

YES BANK is a private Indian bank promoted by Rana Kapoor and Ashok Kapur with financial support from Rabobank Nederland, and three global institutional private equity investors - CVC Citigroup, AIF Capital, and ChrysCapital. It is operational since November 2004 and is the only greenfield bank approved by RBI in last decade. It has 40 branches as on March 31, 2007 and a CASA ratio of 5.8%. Corporate lending forms 65% of its book, while SME lending is at 35%. The bank plans to venture into retail finance in future.

Investment Theme

YES BANK is one of the few private sector banks with product depth, sustainable competitive edge, and strong growth. Given the strong underlying credit demand and small asset book, the loan book is expected to grow at more than 75% for the next two years. The bank's high proportion of fee income enables high return on assets (of 1.4%+) and indicates its potential of generating higher than presently reported RoE (14%-16%), 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

- ◆ There is an execution risk in its network expansion plan.
- ◆ In the event of demand for credit drying down, lack of pricing power can impact its margins adversely (due to nascent deposit franchise).
- ◆ Unseasoned credit book makes it vulnerable to an economic downturn.

Financial Statements

Income statement		(INR mn)				
Year to March	FY05	FY06	FY07E	FY08E	FY09E	
Interest income	300	1,902	5,832	14,894	24,778	
Interest expenses	119	1,047	4,163	11,296	18,777	
Net interest income	181	855	1,669	3,598	6,001	
Non interest income	182	998	1,990	3,027	4,235	
- Fee & forex income	148	897	1,910	2,865	4,012	
- Misc. income	8	61	49	61	74	
- Investment profits	26	40	30	100	150	
Net revenues	363	1,853	3,659	6,625	10,236	
Operating expense	400	861	1,935	3,504	5,261	
- Employee exp	213	501	1,175	2,274	3,340	
- Other opex	187	360	760	1,230	1,921	
Preprovision profit	(36)	992	1,724	3,122	4,975	
Provisions	19	148	288	767	1,220	
- Loan loss provisions	0	0	288	692	1,070	
- Investment depreciation	0	73	0	75	150	
- Other provisions	19	74	0	0	0	
PBT	(56)	844	1,436	2,355	3,755	
Taxes	(18)	291	493	808	1,288	
PAT	(38)	553	943	1,547	2,467	
Reported PAT	(38)	553	943	1,547	2,467	
EPS	(0.2)	2.0	3.4	5.0	7.3	
DPS	0.0	0.0	0.0	0.5	0.8	
Payout ratio (%)	0.0	0.0	0.0	10.0	10.3	

Growth ratios (%)

Year to March	FY05	FY06	FY07E	FY08E	FY09E
Nil growth	N.A	371.4	95.3	115.6	66.8
Fees growth	N.A	504.9	113.1	50.0	40.0
Opex growth	N.A	115.5	124.7	81.1	50.2
PPOP growth	N.A	(1,622.1)	78.1	78.4	59.7
PPP growth	N.A	(2,816.4)	73.9	81.1	59.4
Provisions growth	N.A	664.8	95.1	166.3	59.1
PAT growth	N.A	(1,571.3)	70.5	64.0	59.5

Operating ratios (%)

Year to March	FY05	FY06	FY07E	FY08E	FY09E
Yield on advances	6.1	8.6	9.7	11.2	11.4
Yield on investments	6.3	10.9	14.1	11.1	9.7
Yield on assets	5.0	7.3	8.4	10.6	10.4
Net interest margins	3.0	3.3	2.4	2.6	2.5
Cost of funds	2.2	4.5	6.3	8.2	8.1
Cost of deposits	5.4	6.2	7.6	8.3	8.1
Cost of borrowings	3.2	6.3	6.4	7.9	8.1
Spread	2.7	4.1	2.1	2.9	3.3
Cost-income	110.1	46.5	52.9	52.9	51.4
Tax rate	32.6	34.4	34.3	34.3	34.3

Balance sheet					(INR mn)
Year to March	FY05	FY06	FY07E	FY08E	FY09E
Liabilities					
Equity capital	2,000	2,700	2,800	3,097	3,377
Reserves	132	3,027	5,070	10,604	17,412
Net worth	2,132	5,727	7,871	13,701	20,789
Sub bonds/pref cap	0	1,000	4,250	9,250	12,750
Deposits	6,630	29,104	82,204	158,247	260,983
Borrowings	3,697	4,648	8,673	8,673	9,673
Other liabilities	292	1,163	1,398	2,391	3,916
Total	12,752	41,641	104,395	192,262	308,111
Assets					
Loans	7,610	24,071	62,897	125,794	207,560
Investments					
<i>Gilts</i>	<i>2,687</i>	<i>8,119</i>	<i>20,551</i>	<i>34,814</i>	<i>52,197</i>
<i>Others</i>	<i>1,262</i>	<i>5,382</i>	<i>10,154</i>	<i>11,227</i>	<i>14,976</i>
Cash & equi	530	2,156	5,597	10,775	17,770
Fixed Assets	196	347	460	535	572
Other Assets	467	1,566	4,736	9,117	15,036
Total	12,752	41,641	104,395	192,262	308,111
Balance sheet ratios					
Credit growth	0.0	216.3	161.3	100.0	65.0
Deposit growth	0.0	338.9	182.5	92.5	64.9
EA growth	0.0	228.6	149.7	84.1	60.2
SLR ratio	26.0	24.1	25.0	22.0	20.0
C-D ratio	133.7	93.6	81.9	84.3	83.8
Low-cost deposits	1.4	10.7	5.0	12.0	17.0
Gross NPA ratio	0.0	0.0	0.1	0.2	0.2
Net NPA ratio	0.0	0.0	0.0	0.1	0.0
Provision coverage	0.0	0.0	0.0	28.9	77.4
Incremental slippage	0.0	0.0	0.4	0.4	0.4
Capital adequacy	18.8	16.4	13.6	10.8	10.1
- Tier 1	18.6	13.8	8.2	7.2	7.2

Ratios					
Year to March	FY05	FY06	FY07E	FY08E	FY09E
ROA decomposition (%)					
Net interest income/Assets	3.0	3.3	2.4	2.6	2.5
Fees/Assets	2.6	3.7	2.8	2.1	1.7
Investment profits/Assets	0.4	0.2	0.0	0.1	0.1
Net revenues/Assets	6.0	7.2	5.3	4.7	4.3
Operating expense/Assets	(6.6)	(3.3)	(2.8)	(2.5)	(2.2)
Provisions/Assets	(0.3)	(0.6)	(0.4)	(0.5)	(0.5)
Taxes/Assets	0.3	(1.1)	(0.7)	(0.6)	(0.5)
Total costs/Assets	(6.6)	(5.0)	(3.9)	(3.6)	(3.3)
ROA	(0.6)	2.1	1.4	1.1	1.0
Equity/Assets	17.6	15.2	9.8	7.7	7.3
ROE	(3.5)	14.1	13.9	14.3	14.3

Valuation metrics

Year to March	FY05	FY06	FY07E	FY08E	FY09E
EPS	(0.2)	2.0	3.4	5.0	7.3
<i>EPS growth (%)</i>	<i>NA</i>	<i>(1,189.8)</i>	<i>64.4</i>	<i>48.3</i>	<i>46.2</i>
Book value per share	10.7	21.2	28.1	44.2	61.6
Adjusted book value/share	10.7	21.2	28.0	43.9	61.4
Price/Earnings	(813.6)	74.7	45.4	30.6	20.9
Price/ BV	14.3	7.2	5.4	3.5	2.5
Price/ ABV	14.3	7.2	5.5	3.5	2.5
Dividend yield (%)	<i>0.0</i>	<i>0.0</i>	<i>0.0</i>	<i>0.3</i>	<i>0.5</i>
Price to income	89.3	31.3	15.7	11.4	8.6
Price to PPOP	(489.4)	43.4	25.3	15.7	10.7

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RATING INTERPRETATION

Buy	Expected to appreciate more than 20% over a 12-month period	Reduce	Expected to depreciate up to 10% over a 12-month period
Accumulate	Expected to appreciate up to 20% over a 12-month period	Sell	Expected to depreciate more than 10% over a 12-month period
Trading Buy	Expected to appreciate more than 10% over a 45-day period	Trading Sell	Expected to depreciate more than 10% over a 45-day period

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