

Date: 23 March, 2007

Every week, the ICICIdirect research team selects a stock based on fundamental and/or technical parameters, which is likely to give a return of 20% or more over a 3-6 month perspective.

Dena Bank (DENBAN)

Current Price: Rs 34

Target Price: Rs 41

Potential upside: 20%

Time Frame: 6 mths

Dena Bank, a leading mid-size public sector bank, has witnessed a significant improvement in asset quality. This coupled with its good resource profile, should help it maintain earnings growth.

Background

Dena Bank was incorporated in May 1938 under the name Devkaran Nanjee Banking Company Ltd. It became public limited company in December 1939 and later the name was changed to Dena Bank. In July 1969, along with 13 other major banks, it was nationalised. The government's stake in the bank is 51.19%, preventing possibility of any further dilution. The bank has a pan-India presence with 1,036 branches and 263 ATMs. It is particularly strong in Gujarat and Maharashtra, which contribute around 60% in its total business. In January 2005, the bank raised Rs 80 crores by way of share capital and Rs 136 crore through the share premium from the second public issue. The bank's total business size as of December 2006 was Rs 42,735 crore and it has set a target of Rs 50,000 crores by end-FY07. Retail credit accounted for 19% of its disbursement and small and medium enterprises (SMEs) 17% as of December 2006.

Investment Rationale

Good liability profile with high CASA

Dena Bank's resource profile with current account savings account (CASA) deposits accounting for 43% is one of the best in industry and prevents any steep rise in cost of funds. Its net interest margins (NIMs) have improved from 2.9% in March 2006 to 3.14% in December 2006. They are expected to stabilize around 2.9 - 3% during the next couple of years. Net interest income (NII) is set to grow at 13% in FY08. For the first nine months of FY07, NII has grown 11% y-o-y to Rs 622.4 crore.

Moderate credit growth

Advances for 9MFY07 grew 31.5% y-o-y, in line with industry to Rs 16,945 crore. Advances are expected to grow at 20% and deposits at 17% in FY08. The bank has taken several initiatives to control fresh slippages and as a broader strategy in loan book, it is focusing more on retail, agriculture and SME loans rather than going for big corporate loans where it suffered huge NPAs in past.

Good progress on asset quality front

There has been a considerable improvement in asset quality with gross NPAs falling from 6.44% in March 2006 to 4.99% in December 2006. Its net NPAs have also declined from 3.04% to 2.47% during the same period. However, the absolute amount of gross NPAs is quite large at Rs 857 crore in December 2006. The bank has a tough target of bringing down gross NPAs to below 4% and net NPAs below 2% by end 2007 and management seems to be going in line with the same. The bank hopes to recover NPAs worth Rs 200 crore in Fy07.

Risks and Concerns

Capitalisation issues

The bank's capital adequacy ratio at 12.04% as on December 2006 remains to be one of its major concern areas. With government stake at 51%, there is no scope for further dilution. Access to hybrid capital will be the saviour for the bank. Future growth may be restrained to the tune of future retained profits.

Pressure on margins due to rising interest rates

Rising interest rates remains a key concern for the sector as a whole as it they put pressure on cost of funds thereby affecting margin expansion in future.

Financials

Advances grew 26% y-o-y to Rs 14,231 crore in FY06. Though PBT has risen to Rs 49.7 crore in FY06 from a loss of Rs. 4.78 crore in FY05, net profits rose just 20% from Rs 61 crore in FY05 to Rs 73 crore mainly due to write back of tax provision. Net profit for the first nine months of FY07 has been Rs 157.7 crore from a loss of Rs 57.4 crore. Earnings are estimated to grow at 15-20% in FY08E. Its operating efficiency measured in terms of operating expenses as a percentage of average assets at 2.2% is broadly in line with other PSU banks. Dena Bank's RoA at 0.8% as of December 2006 has improved substantially from 0.29% in Fy06.

Key Financial Ratios					
	2006/03	2005/03	2004/03	2003/03	2002/03
EPS	2.54	2.13	11.14	5.52	0.54
CEPS	4.37	3.57	12.86	6.88	1.7
Book Value	37.15	34.61	45.1	41.76	47.22
Dividend/Share	0	0	0	0	0
OPM	-4.29	6.04	16.2	20.51	15.24
RONW	1.56	13.51	24.73	13.19	1.16
Debt/Equity	22.17	20.25	19.67	19.09	15.72
Ratio	0.49	0.38	0.51	0.6	0.81
Interest Cover	1.09	1.19	1.38	1.43	1.28

Valuation

At the current price of Rs.34, the stock trades at attractive valuations of 1.0x its FY07E ABV and 0.9x its FY08E. We expect the bank to continue steady earnings growth in future and show further improvement in RoA. The bank has substantially de-risked its investment portfolio by shifting securities to held-to-maturity (HTM) category. Securities in the available-for-sale (AFS) category account for less than 35% of total investment book. It has also modified the duration of AFS portfolio to less than 2 years. For 9MFY07, the bank has an annualized return on net worth of 22%. We expect the stock to trade at least 1x its FY08E ABV, giving us a target price of Rs 41, an upside of 20% over the next 6 months.



Technical Outlook

The stock made a bottom at Rs 28 from where it bounced back sharply. It has now crossed its short-term resistances at Rs 31 and Rs 32. These levels will provide support on the downside. The stock is trading very close to its 200-day EMA, which makes it attractive to accumulate. The daily RSI indicator has got into overbought zone, which could result in the stock consolidating before making a fresh move above Rs 35. However, the MACD indicator still indicates oversold.

ICICIdirect Research Desk

ICICI Brokerage Services Limited,
2nd Floor, Stanrose House,
Appasaheb Marathe Road,
Prabhadevi, Mumbai - 400 025
research@icicidirect.com

DISCLAIMER: The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Brokerage Services Limited. "The author of the report does not hold any investment/open position in any of the companies mentioned in this report. ICICI Brokerage Services Limited (IBSL) may be holding a small number of shares/ an open position in the above referred companies as on the date of release of this report." This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and may not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgement by any recipient. The recipient should independently evaluate the investment risks. IBSL and affiliates accept no liabilities for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Actual results may differ materially from those set forth in projections. IBSL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject IBSL and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.