20 July 2009
BSE Sensex: 14745

IDFC SSKI
INDIA RESEARCH

Allahabad Bank

Rs79
UPGRADE TO OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs35.4bn; US$740mn

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Result: Q1FY10
Comment: Strong performance; traction ahead
Revision: FY10 earnings upgraded by 6.8% and expect PAT growth of 12% in FY11

Key valuation metrics

Year to March 31 (Rs m)	NII	yoy chg (%)	Net profit	yoy chg (%)	EPS (Rs)	P/ Adj.Bk (x)	PER (x)	RoE (%)
FY07	17,507	11.0	7,501	28.9	16.8	1.0	4.7	22.6
FY08	17,808	1.7	9,748	29.9	21.8	0.8	3.6	24.5
FY09	21,586	21.2	7,686	-21.2	17.2	0.7	4.6	16.4
FY10E	25,379	17.6	8,718	13.4	19.5	0.6	4.1	16.3
FY11E	28,347	11.7	9,779	12.2	21.9	0.5	3.6	16.0

HIGHLIGHTS OF Q1FY10 RESULTS

Allahabad Bank ('ALBK') reported strong PAT growth of 224% yoy (on a low base) to Rs3.1bn in Q1FY10, well ahead of our estimates. The outperformance was driven by stellar treasury gains and lower provisioning expenses.

- **Strong NII performance; steady margins:** NII came in at Rs6.3bn, a growth of 27% yoy, ahead of our estimates of Rs5.6bn, buoyed by strong growth in advances and steady margins. Margins remained stable at 3% sequentially as the decline in funding costs offset the decline in yields. Cost of funds declined by 20bp qoq and 35bps yoy due to sustained trimming of bulk deposits, down to ~3% of deposits from ~8% in Mar '09. On the other hand, slower growth in saving deposits led to a 144bp yoy and 90bp qoq decline in CASA ratio to 33.7% (reported at 34.1% of aggregate deposits). (Exhibit 1 & 2)
- **Stellar treasury gains buoy non-fund income:** Robust trading profits of Rs2.1bn – at 36% of operating profits – led to strong 200%+ yoy growth in other income. Commission and exchange fee increased by 36% yoy to Rs1.5bn, driven by strong credit off-take and traction in trade credit (LCs & guarantees) during the quarter. (Exhibit 3)
- **Strong balance sheet growth:** Gross credit stood at Rs610bn – a growth of 21% yoy and 3% qoq driven by growth in corporate loans. As deposit growth also remained strong at 22% yoy and 5% qoq to Rs894bn, CD ratio has remained largely stable on a yoy basis at 68%. (Exhibit 4)
- **Lower provisions owing to MTM write-back; sharp rise in coverage:** Provisions were well below expectations at Rs396m, as against Rs2.0bn in Q1FY09 and Rs2.5bn in Q4FY09. Sharp decline can be attributed to MTM write-back of Rs2.1bn during the quarter. Utilizing the treasury gains, the bank made higher NPA provisions of Rs2.5bn, leading to a sharp improvement in coverage to 80% from 61% in Q4FY09 (60% in Q1FY09). (Exhibit 6)
- **Steady Gross NPAs; pending restructurings completed:** ALBK restructured standard advances worth Rs1.4bn (0.23% of loans) during Q1FY10, indicated to be pending as of March 2009. Now the cumulative restructured accounts stand at 4.5% of the advances as of June 2009. At the same time, % of Gross NPAs remained stable sequentially at 1.8% (Rs148m rise in absolute terms). (Exhibit 5)

- **Introducing FY11 numbers:** We see a profit growth of 12% yoy in FY11 to Rs9.8bn, driven by 20% growth in credit. NII is estimated at Rs28.3bn – 11.7% yoy growth, and we expect fee income to grow at 15% yoy.

VALUATIONS & VIEW

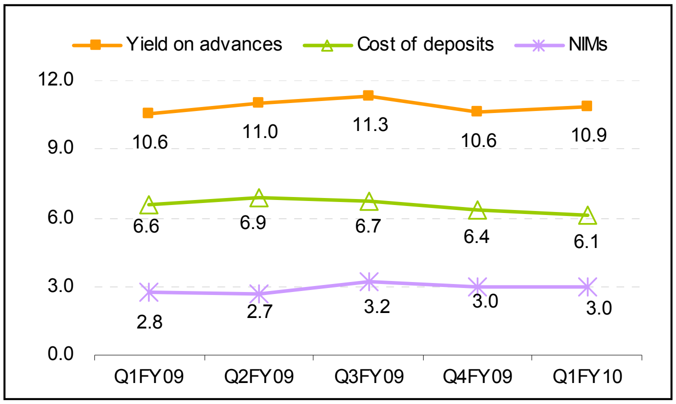
Allahabad Bank's earnings surpassed our estimates on the back of stellar net treasury gains. At the same time, core performance has witnessed an uptick with traction in NII driven by healthy credit growth and steady margins. Fee income remained robust and the bank utilized strong treasury gains to significantly bolster the coverage ratio (now at 80%). Asset quality remains stable with restructured accounts hovering at industry levels. However, with 48% of the investment book in AFS category (including liquid mutual funds) the earnings remain sensitive to movement in yields. Factoring in higher treasury gains and improvement in the operating metrics, we are upgrading our FY10 earnings estimates by 6.8%. We expect the bank to deliver 12.8% CAGR in profit over FY09-11E and with average RoE of ~16%. In view of improving core performance and receding asset quality pressures, the current valuations of 0.61x FY10E and 0.54x FY11E adjusted book appear cheap. Upgrade to Outperformer with a price target of Rs114.

Quarterly results

P&L (Rs m)	Q1FY09	Q2FY09	Q3FY09	Q4FY09	Q1FY10	FY09	FY10E	FY11E	Remarks
Total intt income	17,326	18,460	18,980	19,151	20,082	73,647	82,028	96,568	
Interest expense	12,371	13,524	12,939	13,227	13,791	52,061	56,649	68,221	
Net interest income	**4,955**	**4,935**	**6,041**	**5,924**	**6,291**	**21,586**	**25,379**	**28,347**	Above estimates buoyed by strong credit off-take and steady margins
yoy growth (%)	*9.8*	*19.0*	*44.5*	*42.5*	*27.0*	*21.2*	*17.6*	*11.7*	
Other income	**1,170**	**1,312**	**4,084**	**4,583**	**3,695**	**11,419**	**9,719**	**10,050**	Buoyed by stellar trading gains
yoy growth (%)	*23.6*	*(15.7)*	*2.0*	*59.6*	*215.7*	*33.4*	*(14.9)*	*3.4*	
Fee income	849	1,236	1,201	2,137	1,555	5,692	7,119	8,150	Strong growth driven by traction in trade credit (LCs/ guarantees)
Trading	322	77	2,883	2,446	2,140	6,863	3,800	3,000	~36% of operating profits - primarily on G-Sec book
Net revenue	**6,125**	**6,248**	**10,125**	**10,507**	**9,986**	**33,006**	**35,098**	**38,398**	
Operating expenses	3,058	3,105	3,465	4,366	4,079	13,994	16,505	17,805	Includes Rs800mn of wage hike provision in Q1FY10
yoy growth (%)	*20.9*	*15.6*	*27.8*	*39.2*	*43.0*	*20.9*	*17.9*	*7.9*	
Operating profit	**3,067**	**3,142**	**6,661**	**6,141**	**5,906**	**19,011**	**18,593**	**20,593**	
yoy growth (%)	*6.2*	*4.9*	*27.8*	*66.0*	*92.6*	*28.5*	*(2.2)*	*10.8*	
Provisions	2,022	2,665	1,030	2,537	396	8,254	5,581	6,212	Sharp decline owing to Rs2.1bn of MTM write back; NPA provisions high at Rs2.5bn
PBT	**1,045**	**477**	**5,631**	**3,604**	**5,510**	**10,758**	**13,012**	**14,381**	
Tax	111	60	1,936	964	2,481	3,072	4,294	4,602	
PAT	**934**	**417**	**3,695**	**2,640**	**3,029**	**7,686**	**8,718**	**9,779**	Ahead of expectations due to stellar net treasury gains
yoy growth (%)	*(53.4)*	*(82.6)*	*1.2*	*55.7*	*224.4*	*(21.2)*	*13.4*	*12.2*	
Ratios (%)									
NIM (reported)	2.8	2.7	3.2	3.0	3.0				Supported by declining costs as the bank trims bulk deposits
NIM (calc*)	2.4	2.3	2.8	2.6	2.5	2.4	2.4	2.3	
Non fund revenues/Avg assets	0.6	0.6	1.9	2.0	1.5	1.2	0.8	0.7	Robust treasury gains
Operating expenses/avg assets	1.5	1.5	1.6	1.9	1.6	1.5	1.5	1.4	
Cost/Net revenue	49.9	49.7	34.2	41.6	40.9	42.4	47.0	46.4	Wage hike provision made
Tot prov/avg assets	1.0	1.3	0.5	1.1	0.2	0.9	0.5	0.5	
RoA	0.4	0.2	1.7	1.1	1.2	0.9	0.8	0.8	
Tax/PBT	10.6	12.6	34.4	26.8	45.0	28.6	33.0	32.0	Elevated due to higher treasury gains
Overall CRAR	4.0	4.0	4.0	5.1	4.7				Comfortably capitalized for growth in the near term
Tier I CRAR	7.6	7.5	8.2	8.0	7.9				
CD ratio	68.6	70.2	70.2	70.0	68.2				Steady on a yoy basis as credit off-take remains robust
Balance Sheet (Rs bn)									
Credit	502	517	528	594	610				Above industry growth of 3% qoq growth driven by corporate loans
yoy change (%)	26.0	23.4	15.2	18.1	21.4				
Deposits	732	736	751	850	894				5% qoq growth
yoy change (%)	16.5	11.8	10.4	18.6	22.1				

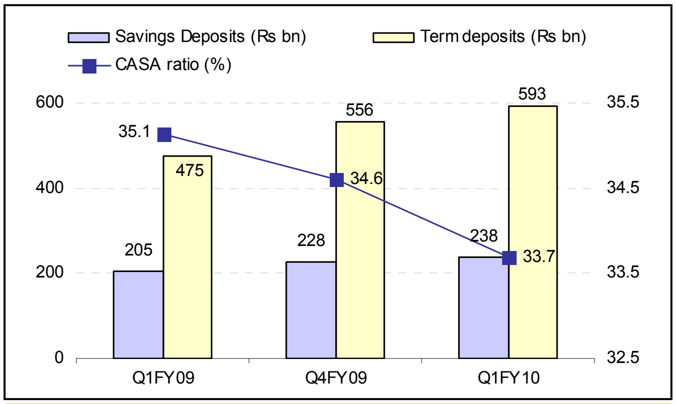
** Calculated on average quarterly balances*

Exhibit 1: Margins face stress (%)



- NIMs remain steady as funding costs decline and marginal uptick in yields
- Cost of funds declines as the bank focuses on trimming bulk deposits – down to 3% from 5% in FY09

Exhibit 2: Steady CASA



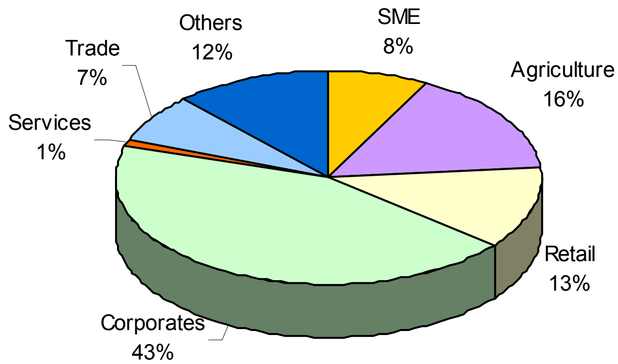
- CASA ratio slips by ~90bp qoq to 33.7% of overall deposits
- Savings deposits grow by 16% yoy, while current deposits at 20% yoy

Exhibit 3: Non fund income remains strong

Rs m	Q1FY09	Q4FY09	Q1FY10	yoy growth	qoq growth
CEB	1,073	2,077	1,465	37%	-29%
Trading	322	2,446	2,140	565%	-13%
Others	46	60	90	97%	50%
Total other income	1,170	4,583	3,695	216%	-19%

- Growth buoyed by robust treasury gains on G-Sec book
- CEB shows traction driven by trade credit and robust credit off-take

Exhibit 4: Composition of the loan book



- Growth (21% yoy) led by corporate loans
- Consistent rise in proportion of corporate loans (up to 43% from 38% in FY08)

Exhibit 5: Steady Gross NPAs

Rs m	Q1FY09	Q4FY09	Q1FY10	Incremental (Rs m/bps)
Gross NPA	9,383	10,782	10,931	148
Gross NPA (%)	1.9	1.8	1.8	(2)
Net NPA	3,713	4,191	2,198	(1,993)
Net NPA (%)	0.8	0.7	0.4	(35)
Coverage (%)	60.4	61.1	79.9	1,876
Restructured loans		25,640	27,070	1,430
As % of loans		4.3	4.5	23

- Gross NPAs steady; sharp improvement in coverage as the bank utilizes treasury gains to make excess provisions
- ~Rs1.4bn of incremental restructuring; total at Rs27bn

Exhibit 6: Break up of provisions (Rs m)

	Q1FY09	Q4FY09	Q1FY10	yoy growth(%)
Provision for NPA	(551)	1,882	2,510	NA
Provision for std assets	26	1	15	(43)
Provision for depr	2,641	230	(2,147)	(181)
Other provisions	(93)	423	19	(120)
Total Provisions	2,022	2,537	396	(80)

- Well below estimates on account of outsized MTM write-backs
- NPA provisions higher to improve the coverage ratio

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Explanation of Ratings:

1. Outperformer: More than 10% to Index
2. Neutral: Within 0-10% to Index
3. Underperformer: Less than 10% to Index

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