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Yes Bank

Company Update

BUY

Price	**Rs183**
Target Price	**Rs238**
Investment Period	**12 Months**

Stock Info

Sector	Banking
Market Cap (Rs cr)	5402.60
Beta	1.13
52 Week High / Low	278/121
Avg Daily Volume	433663
Face Value (Rs)	10

BSE Sensex	16,371
Nifty	4,942

BSE Code	532648
NSE Code	YESBANK
Reuters Code	YESB.BO
Bloomberg Code	YES IN

Shareholding Pattern (%)	
Promoters	34.1
MF / Banks / Indian FIs	6.4
FII / NRIs / OCBs	52.5
Indian Public / Others	7.0

Abs.	3m	1yr	3yr*
Sensex (%)	(19.0)	27.1	124.1
Yes Bank (%)	(26.7)	28.4	200.0

*Note: *since listing on 12/07/2005*

Vaibhav Agrawal

Tel: 022 - 4040 3800 Ext: 333

E-mail:vaibhav.agrawal@angeltrade.com

High Growth Trajectory Intact

We believe that the risks developing in Yes Bank's Forex Derivative business are manageable and the structural growth potential of the Bank is intact. The Bank is on a high growth trajectory, has embarked on building a strong brand and has an impressive pool of intellectual capital. We expect 66% CAGR in Deposits and Advances and 53% CAGR in EPS over FY2007-10E. We have factored in 15% reduction in EPS estimates for FY2009E and FY2010E taking a conservative view on the Forex Derivatives business and revised our estimated FY2010E ABV downwards from Rs99 to Rs88. At Rs186, the stock is trading at 2.1x our revised FY2010E Adjusted Book Value (ABV) of Rs88. ***We value the Bank at 2.7x our revised FY2010E ABV to arrive at a 12-month Target Price of Rs238 (down 17% from our earlier Target Price of Rs289), implying an upside of 28%. We maintain a Buy on the stock.***

- **Wholesale business to continue to drive Profits:** Income from Forex Derivatives constitutes 33% of Treasury Income and 8% of overall Revenue. Plain-vanilla Forex products and Debt Market activities (comprising 66% of Treasury Income), Investment Banking and Transaction Banking are expected to continue contributing strongly to Fee Income. While we expect NIMs to be 2.4-2.5% during FY2009E and FY2010E, sustainable margin levers include low-cost retail deposits and changes in segmental credit mix in favour of SME and retail lending.

- **Retail banking - Building a strong brand:** Yes Bank is developing its Retail business around comprehensive wealth management solutions targeting affluent customers. Broadly, this segment comprises about 2% of Indian households, but contributes 21% of aggregate annual household savings. The Bank's cutting edge payment and distribution technologies, superior service levels and ability for incremental innovation pit it against the foreign banks. Further, by FY2009, it will have more branches (120+) than the largest foreign bank in India viz., Standard Chartered Bank with 81 branches.

- **Sound Management with convincing track record:** Yes Bank has an A-list top management team, which brings to the table rich experience from the best banks in India. The Bank's high growth trajectory, strong branding and franchise, and impressive pool of intellectual capital are also expected to make it an attractive acquisition target, post the impending liberalisation of Regulatory norms governing foreign banks.

Key Financials

Y/E March (Rs cr)	FY2007	FY2008E	FY2009E	FY2010E
NII	**171.4**	**328.1**	**609.3**	**995.8**
% chg	*94.6*	*91.5*	*85.7*	*63.4*
Net Profit	**94.4**	**189.6**	**268.0**	**404.5**
% chg	*70.4*	*100.9*	*41.4*	*50.9*
NIM (%)	2.3	2.2	2.4	2.5
EPS (Rs)	**3.4**	**6.4**	**8.5**	**12.**1
P/E (x)	54.3	28.4	21.5	15.1
P/ABV (x)	6.5	4.1	2.8	2.1
RoAA (%)	1.2	1.2	1.0	1.0
RoANW (%)	13.9	18.1	16.1	16.3

Source: Company, Angel Research

Forex Derivatives: Recent Developments

In the past few months, movements in Forex rates of Euro, Swiss Franc and Japanese Yen against the US Dollar contrary to expectations have resulted in numerous Indian corporates incurring large MTM losses on their exposure to Forex Derivatives. This has led to concerns about Yes Bank's Forex Derivative business. We have dealt with this matter straightaway to address investment concerns arising on this account. Based on our discussions with the management and general understanding of the sectoral impact, we believe that the risks developing in the Forex Derivatives business are manageable and the structural growth potential intact.

Forex Derivatives are unlikely to be a source of proprietary MTM losses or liquidity risk for Indian banks

First off, it is important to note that Indian banks are not allowed to keep open positions in respect of these contracts over a marginal limit fixed by the RBI. Therefore, they will not suffer MTM losses on their own proprietary accounts. Secondly, the derivative contracts entered into with customers are backed by mirror contracts with international counterparties even in terms of cash flows i.e. a situation of calls being made by counterparties on Indian banks without a similar arrangement to recover the same from customers is unlikely, minimizing liquidity risk for banks.

A matter of credit risk; Nil defaults so far for Yes Bank

Specifically, in the case of Yes Bank, we have been informed that most of these contracts do not have a system of margin calls, but rather have regular (usually monthly or quarterly) cash settlements. At present, the Bank has not faced a situation where a customer has reneged on any settlements that have fallen due. Nonetheless, the relevant risk arising out of this situation that needs to be addressed is that of customers defaulting on future settlements - this is essentially a credit risk from the Bank's perspective.

Why material credit losses too are unlikely

Low probability of an 'inability to pay' scenario: The Bank has about 50 clients in its Forex Derivatives business. Of the total exposure, about 85% is to clients with turnover exceeding Rs500cr & balance with clients having turnover exceeding Rs200cr. The weighted average credit rating (on the Bank's internal scale) is 'A' and 50% of exposure relates to clients rated 'AA' and above. The approval process for entering into contracts is identical to the credit approval process for loans. (Yes Bank to date has Nil Gross NPAs - a testament to its customer profile and credit approval process). Although these contracts are not usually backed by collateral and while exposure on account of MTM losses of customers may not have been recovered in the form of a margin call in 85-90% cases, the profile of customers suggests that probability of default, due to inability to pay, is low.

Weak grounds for an 'unwillingness to pay' scenario: We believe that the grounds for default by going into litigation to render contracts void appear weak based on available information. Forex Derivatives have been prevalent and legally allowed in India since the past 15-20 years and especially in the past few years, many corporates have utilized them to their pecuniary advantage. We believe, banks are unlikely to be caught on the wrong foot so far as compliance with the letter of the law is concerned i.e. in terms of having documentation serving as proof of underlying from client, board approvals, contract notes, etc. Moreover, as per RBI Guidelines, banks take undertakings from customers to the effect that the same exposure has not been hedged with any other bank that could in effect lead to speculative positions.

Beyond this, further due diligence for banks would tend to become onerous. It seems unrealistic to expect banks to bear losses that customers have suffered due to speculative positions taken willingly. So far, media reports of customers suing banks on grounds of 'mis-selling' seem to relate to customers that have suffered losses disproportionate to their networth, suggesting that an 'inability to pay' may be the real genesis of these lawsuits as well.

Some credit loss factored into estimates conservatively: In spite of this, we have arrived at a broad estimate of likely MTM losses of Yes Bank's customers of Rs450cr (based on information contained in annual reports, discussions with the Bank as well as discussions with other banks). According to the management, about 70-80% of the customers have not squared off positions. Out of this MTM loss of Rs450cr, a large portion would likely have a corresponding underlying (trade receivable or ECB) and in effect the MTM loss of customers would only be a notional or opportunity loss. Actual losses would only be on speculative positions.

Yet, on a conservative basis, we have factored in credit losses arising out of customer defaults to the extent of 10% of estimated MTM losses in our projections. Considering that the weighted average residual maturity of the derivative contracts is intimated to be about 19-20 months, we have provided for this loss equally over FY2009E and FY2010E. Further downside risks to our estimates could arise from new information coming to light, since information in the public domain about Forex Derivatives is limited and the situation dynamic.

Exhibit 1: Probable Credit loss & relevant portion of fee income affected

Potential credit loss due to customer default	(Rs cr)	Fee income for 9MFY2008	(Rs cr)
Contingent liability on Forex & Derivatives (FY2007)	50,000	Total Operating Income, of which	477
Contingent liability on Forex & Derivatives (FY2008E)	75,000	Non-interest income, of which	249
- Rupee interest rate swaps (estimated) *	27,000	Total treasury income, of which (approx.)	114
- Plain vanilla Forex contracts (estimated) *	30,000	- Debt markets income	33%
- Forex Derivatives (estimated) *	18,000	- Plain-vanilla Forex income	33%
Less: Double-counting #	9,000	**- Forex Derivatives (risk of slowdown)**	**33%**
- Notional amount of Forex derivative contracts	**9,000**		
Estimated MTM loss of customers			
(assumed at 5% of notional)	450	Net worth (Dec 2007)	1,250
- Large Corporates [Turnover>750cr] ^	315	Net Profits (9MFY2008)	136
- Emerging corporates [Turnover>200cr]	135		
Total loss on customer default projected over			
FY2009E & FY2010E	**45**		

*Source: Company, Angel Broking. Note: * in same proportion as FY2007. # due to reporting convention. ^ 72% as per management.*

Impact on Fee income going forward

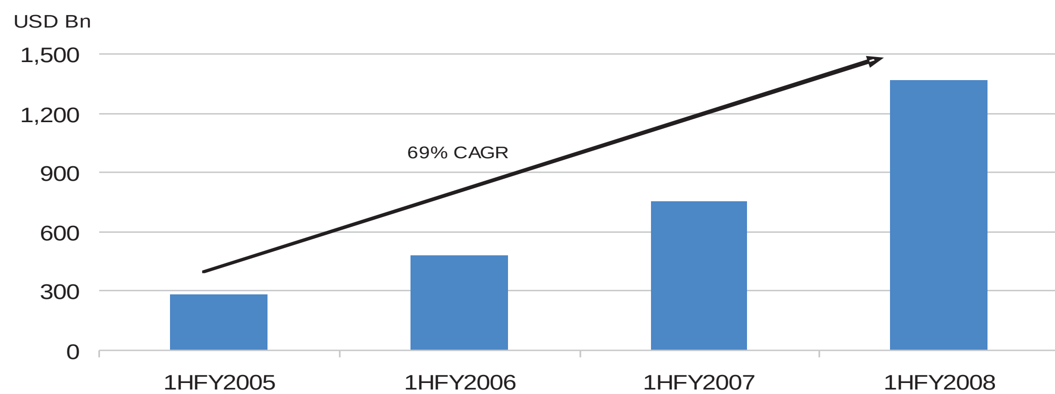
Forex Derivatives no doubt a material portion of overall business: About 8-10% of Yes Bank's Total Operating Income (Net Interest Income + Fee Income) has been coming from the Forex Derivatives business (it contributes about 1/3rd of Treasury Income as per the management). Going forward, this income stream is likely to see a slowdown, especially in the near-term. Moreover, costs incurred to run the business are essentially fixed in nature – therefore, any reduction in revenues would directly impact Profit before Taxes (PBT) in the near-term. Accordingly, to be on the conservative side, we have reduced our PBT projections for 4QFY2008E, FY2009E and FY2010E substantially, to provide a reasonable margin of safety. Together with the above-mentioned credit losses factored in, as well as a general risk of slowdown in fee income streams dependent on capital markets (like Investment Banking and Commission from cross-selling Mutual funds and Unit-linked Insurance policies), we have reduced PBT projections by about 15%, 15% & 14% for 4QFY2008E, FY2009E & FY2010E respectively.

Forex Derivatives likely to revive in the medium-term: We believe that in the medium-term, this business could very well revive, as the fact remains that a large portion of derivative contracts add substantial value to customers as an effective means of hedging their interest rate and currency risks.

RBI Regulations expected: We expect the RBI to come out with regulations governing these products – this could be a risk to our hypothesis of medium-term revival. However, we are inclined to believe that the regulations could infact be enabling, to the extent that they make the business more orderly and robust from the risk-management point-of-view.

Part of Forex Derivatives business to shift to Plain-vanilla Forex contracts: With robust growth in foreign trade as well as capital flows, Forex turnover in the merchant segment has been growing at 60-70% CAGR in the past 3-4 years. Therefore, the overall treasury business of Yes Bank is likely to continue growing at a robust rate. Infact, a large part of the volumes from the Forex Derivatives business also should shift to Plain-vanilla Forex products, albeit a relatively low-margin business. Taking into account the positive outlook on the Debt market and Plain-vanilla Forex business, we expect the Treasury division to contribute about 35% of overall Fee Income in FY2009E and FY2010E (as against about 44% in FY2008E).

Exhibit 2: Aggregate Forex turnover in the merchant segment



Source: Company, Angel Research. Note: Aggregate Forex Turnover includes spot, forward and cancellation

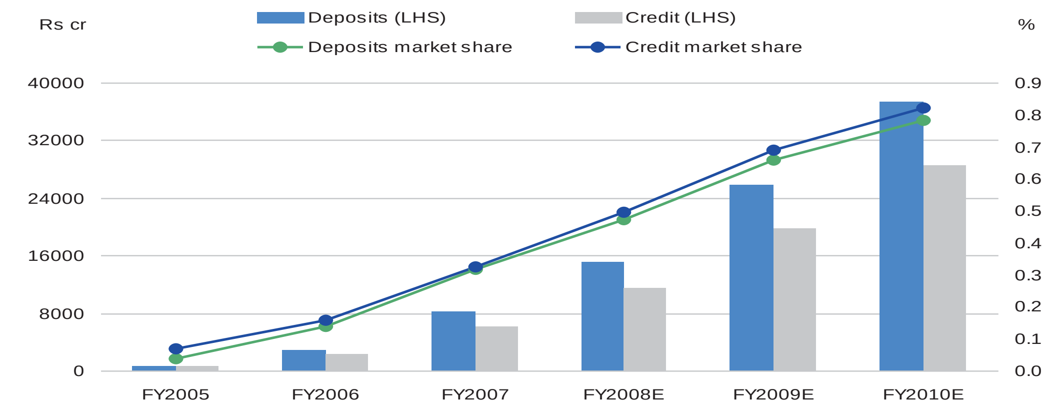
The Wholesale Bank: Business and financial analysis

Wholesale business to continue driving profits

Albeit the Forex Derivatives development is a setback for the Bank in the short-term, the rest of the Bank is in good shape and set to deliver strong growth and profitability. Over the past 2 years, Yes Bank has demonstrated strong execution ability in scaling up its Fee-driven Wholesale business.

While the Bank's retail business will require substantial capital and operating expenditure over the next 2 years, the Bank's successful wholesale business will continue to drive revenues and profitability. We expect 66% CAGR in deposits and advances over FY2007-10E, more than 3 times the expected industry growth rate.

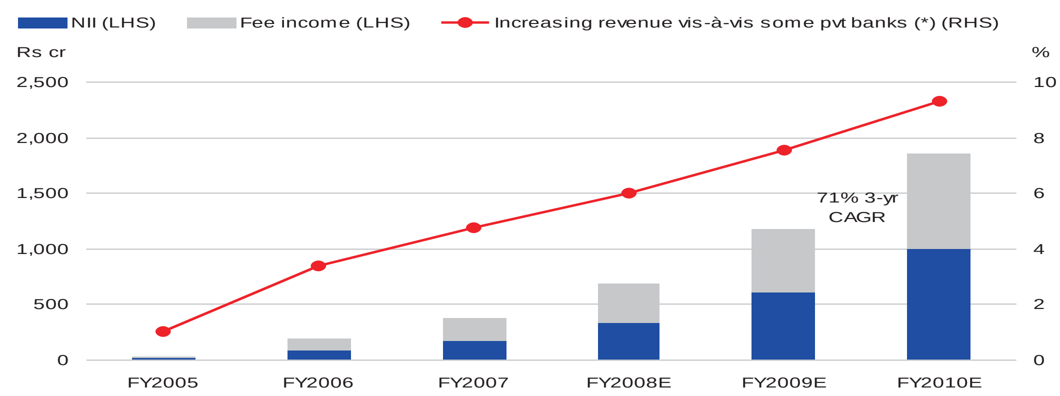
Exhibit 3: Strong growth expected in Balance Sheet



Source: RBI, Company, Angel Research

Similarly, even after factoring in the fall in income due to the Forex Derivatives business, we expect 71% CAGR in operating income over FY2007-10E.

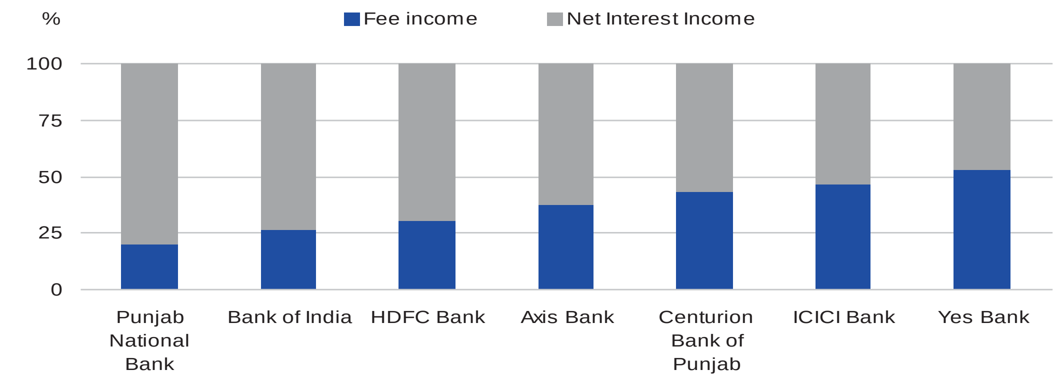
Exhibit 4: Equally strong growth expected in core income



*Note: * calculated as: [NII+Fee of YesBK] as % of [NII+Fee of HDFCBK+AXISBK] to give an idea of the relative pace at which YesBK is growing.*

Notably, Yes Bank does earn a substantial portion of its income from fee-based sources vis-à-vis peers. As fee income requires far less capital, it enables the Bank to deliver better RoEs than it could otherwise have at this stage of its evolution. Forex Derivatives apart, each of the fee income streams continue to show good traction and we expect contribution from fee income to remain strong, albeit not as high as in FY2007 (46% of total income in FY2010E vis-à-vis 54% in FY2007).

Exhibit 5: Greater proportion of fee income vis-à-vis peers (nos. relate to FY2007)



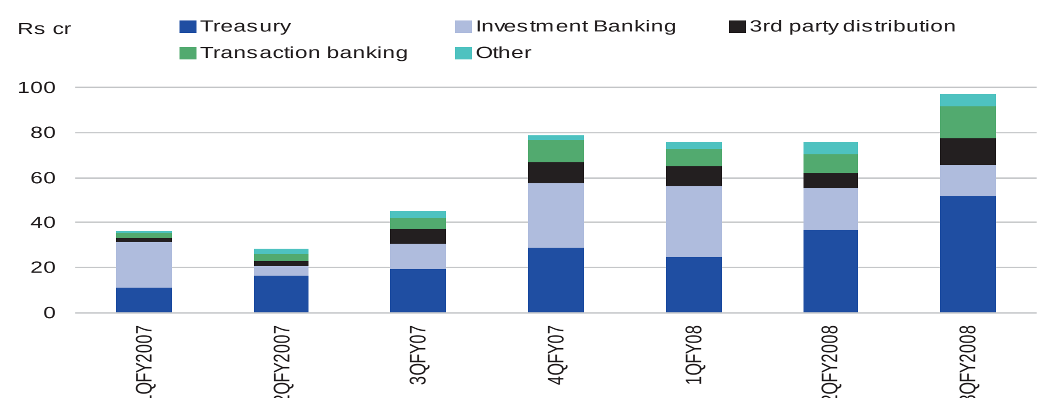
Source: Company, Angel Research

Traction in multiple Fee Income streams

As mentioned above, about 35% of overall Fee Income is expected to come from the Treasury business going forward. The Bank has also built an enviable track record in the Investment Banking business, quickly moving up the rankings in League tables, especially in Cross-border Outbound M&A transactions. (Annexure 1 presents details about the Bank's performance so far in this business, including prominent deals like Suzlon's US$1.4bn acquisition of Repower). While there may be some slowdown in this business due to dampened Capital markets globally, the management has guided that the pipeline of deals is quite strong. We expect the division to continue contributing about 20-25% of overall Fee Income.

Income from sale of Mutual Fund units and Max New York Insurance policies is one of the most rapidly growing businesses of Yes Bank. (This business is analysed in subsequent sections of the Report on the Bank's Retail business). Income from Cash Management Services and traditional Fee Income streams like Bank Guarantees, LCs, etc. is also expected to grow at a robust rate as the Bank continues to expand its Distribution reach. We expect about 20-25% of overall Fee Income to come from this segment.

Exhibit 6: Fee-income growth and mix across last 6 quarters



Source: Company, Angel Research

Net Interest Margins and other drivers of core profitability

Efficient underwriting of risk

Flexible, innovative financing structures and efficient underwriting of risks (aided by the knowledge banking approach) have enabled the Bank to earn amongst the highest yield on advances compared to a cross-section of banks, despite having negligible SME & retail exposure, at the same time maintaining impeccable asset quality. The nature of assets have required a high capital charge, but in light of large real estate portfolio & low SLR holdings, it represents a superior yield v/s capital charge trade-off. (At the end of this section, we have presented a Dupont Analysis of the Bank's ROE. Also, Annexure 2 contains exhibits depicting the financial ratios affecting the Bank's RoE for FY2007 vis-à-vis other banks).

Eventually though, the present industry dynamics favor banks with robust fee income streams and high proportion of CaSa deposits – Yes Bank has the former, needs the latter (and has a credible strategy to get there)

Business (deposits + credit) growth in the current phase of Yes Bank's evolution is bound to be dictated by the industry's inherent size imperatives - a large balance sheet is a competitive advantage. We expect business to grow at a 3-year CAGR of 66% over FY2007-10E, more than 3 times the expected industry growth - but then, with wholesale deposits, this is not the major constraint, on a small base. The real casualties are margins. It essentially means that the Bank must sink in equity to meet capital adequacy requirements even though the pure lending business is not very profitable on an RoE-basis yet. (We believe that the near-term should be more properly viewed as a gestation period). But in the medium term, the Bank has 2 key margin levers: CaSa and credit mix. As stated earlier, Fee Income, which consumes little or no regulatory capital, will sustain profitability in the near term (and beyond).

Margin levers – many, in the medium term

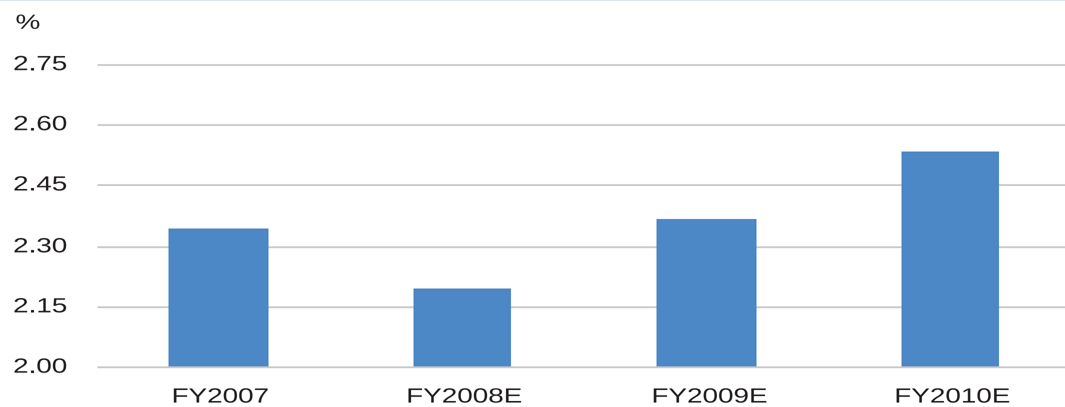
CaSa is a crucial lever: detailed in subsequent sections

Changing segmental credit mix to increase yields further: The Bank’s intention to focus on SME lending in the near term and also personal loans in the medium term (as described in Annexure 3) will help increase yield on advances further. Moreover, the Bank relies on purchase of assets & RIDF (low-yield NABARD deposits meant as a substitute for banks with low direct-lending to Agriculture) for meeting its priority sector lending requirements. In 1HFY2008, the Bank set up its agri & rural banking division to increase direct lending to priority sectors, engage with micro-finance institutions (MFIs) and develop business correspondent models, given the highly lucrative yields (~20%) and low credit costs (~1%) being experienced by MFIs following the Grameen bank model.

Repricing behaviour of loans & deposits and near–term NIM outlook: In terms of repricing behaviour, Yes Bank's assets have a similar profile as most other domestic banks. However, being essentially a wholesale bank at present, its deposits are short-term in nature and tend to reprice faster than those of other banks. This subjects the Bank to greater volatility in NIMs and can be disadvantageous in an increasing interest rate environment. (For instance, in FY2008E v/s. FY2007). However, given the present expectation of softening interest rates in the medium-term (albeit keeping in mind the near-term overhang of significantly high inflation, with the WPI increasing 6.7% yoy), even if NIMs of the sector as a whole come under pressure, relatively Yes Bank is likely to face lesser pressure on its NIMs. This will give it greater leeway in the NIM v/s Balance Sheet expansion trade-off.

While we expect the Bank to post NIMs of about 2.2% for FY2008E, based on our analysis, NIMs are expected to thereafter improve steadily (on a structural level) as Current and Savings deposits increase with expanding retail operations and credit mix changes favorably.

Exhibit 7: NIMs to improve steadily (on a structural level)



Source: Company, Angel Research

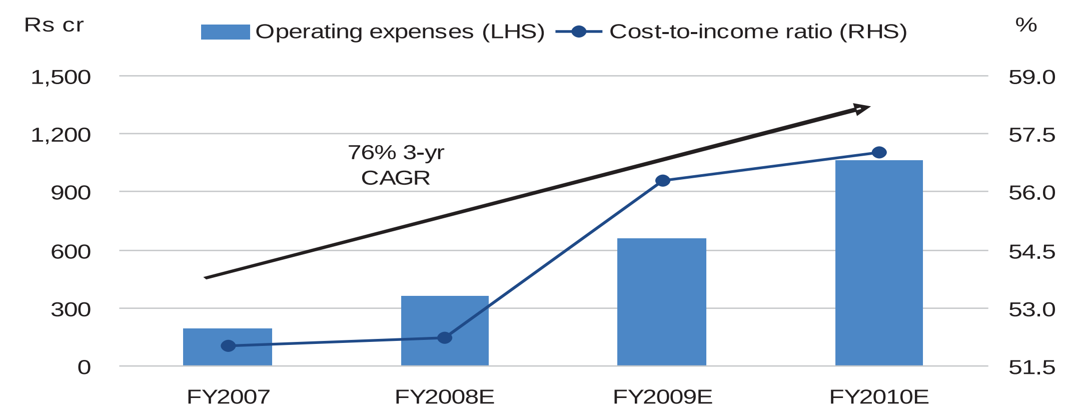
Capital adequacy

The Bank's Capital adequacy stood at 14% at the end of 3QFY2008, of which Tier I capital was 9%. The Bank plans to raise about Rs500-600cr of equity capital (leading to 6-7% dilution) in the next 6-12 months. Infact, given the Bank's scorching pace of growth, frequent equity infusions will be inevitable. Accordingly, in our explicit 2-year forecast we have factored in another 6.5% dilution in FY2010 as well. (For projected dilutions we have conservatively factored 15% price appreciation per annum). This should broadly enable the Bank to maintain its capital adequacy above 12%.

Operating expenses and Cost-to-income Ratio

In subsequent sections we have described the kind of expenditure that the Bank's retail expansion will entail – apart from capex, a lot of revenue expenditure will also be in the nature of gestation-period investment. Further, operating expenditure will also increase in line with growth in existing divisions. Moreover, wage inflation is expected to be in the range of 15-20% for private banks. The 'broadening base of the pyramid' will provide some relief to the otherwise rapid increase in operating expenses (opex) – while the staff strength is expected to double in FY2008, most of the new hiring will be of sales persons, with salary structures having a low fixed component and variable pay linking to corresponding revenue for the Bank. We expect opex to grow at a 3-year CAGR of 76% over FY2007-10E. The Cost-to-income ratio is expected to show an increasing trend during the explicit forecast period, increasing from 52% in FY2007 to 57% in FY2010E, exacerbated on account of the setbacks in the Forex Derivatives business.

Exhibit 8: Rapid growth in operating expenses, in line with revenues



Source: Company, Angel Research

Increase in credit costs

Yes Bank presently has Nil Gross NPAs - but its credit book is unseasoned. NPAs are likely to emerge and approach industry levels (if high interest rates persist longer than expected or the business cycle changes then the probability of NPA slippages increasing would be higher). Accordingly, we have factored in 0.6% slippages in FY2009E and 0.8% in FY2010E. Given below is a sensitivity table, indicating changes in key financials if slippages are progressively higher.

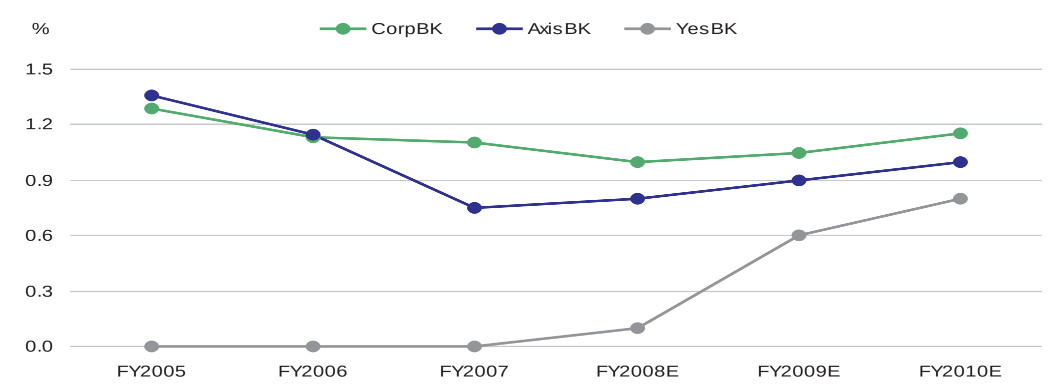
Exhibit 9: Sensitivity analysis (in respect of slippages)

		Slippages				
		0.60	**0.75**	**0.90**	**1.05**	**1.20**
NPA Provision	FY09E	0.2	0.2	0.3	0.3	0.4
as % of avg assets	FY10E	0.3	0.3	0.4	0.5	0.5
PAT (Rs cr)	FY09E	268	259	251	242	234
	FY10E	404	390	375	360	345
RoA (%)	FY09E	1.0	1.0	0.9	0.9	0.9
	FY10E	1.0	1.0	0.9	0.9	0.8
RoE (%)	FY09E	16.1	15.6	15.1	14.6	14.2
	FY10E	16.3	15.8	15.3	14.8	14.2
PAT YoY	FY09E	41	37	32	28	23
growth (%)	FY10E	51	50	50	49	48
PAT CAGR (%)	FY08-10E	62	60	58	56	54
BVPS (Rs)	FY09E	64	64	64	64	63
	FY10E	88	87	87	86	85
EPS (Rs)	FY09E	9	8	8	8	7
	FY10E	12	12	11	11	10

Source: Angel Research. Note: FY2010E slippages assumed at 0.2% higher than FY2009E slippages in each instance.

Two other banks under our coverage with similar credit mix (i.e. skewed towards corporate assets) and strong risk management viz., Axis Bank and Corporation Bank, experienced slippages of 0.75% and 1.1% respectively in FY2007 (and we expect them to maintain similar levels of slippages over FY2008-10E). Although Yes Bank is a Nil NPA bank with an even higher proportion of corporate advances, we have conservatively factored into our projections for the Bank, an increase in slippages to 0.8% by FY2010E.

Exhibit 10: Trend in slippages for a cross-section of banks (under coverage)



Source: Company, Angel Research

Dupont Analysis

Exhibit 11: Dupont Analysis

	HDFC Bank	Axis Bank	Yes Bank				Comments
	FY2007	FY2007	FY2007	FY2008E	FY2009E	FY2010E	
Net Interest Income (NII)	4.50	2.55	2.25	2.11	2.27	2.44	Yes Bank earns a reasonably high yield on assets considering its credit mix (mainly corporates) which keep provision costs low. NII is low mainly on account of its present reliance on high-cost wholesale deposits. Going forward, we have factored in structural margin levers such as low-cost retail Deposits and SME lending. (Provision cost was high in FY2007 due to one-time high Std. asset provisions)
Provisions & Conting.	1.41	0.60	0.46	0.26	0.40	0.45	
Adjusted NII	3.09	1.95	1.79	1.85	1.87	1.99	
Non-Interest Income	1.83	1.64	2.63	2.30	2.12	2.11	Treasury, Investment Banking, Transaction Banking, Bancassurance, etc. contribute to relatively high proportion of (less capital consuming) Fee Income. Assumed to decline going forward due to conservative assumptions for Forex Derivatives business.
Operating Income	4.93	3.60	4.42	4.15	3.99	4.10	
Operating Expenses	2.94	1.98	2.54	2.30	2.47	2.60	A large part of operating expenses should be more properly viewed as gestation period expenses that will normalise in the medium to long-term
Profit before Taxes	1.99	1.62	1.88	1.85	1.52	1.50	
Taxes	0.60	0.55	0.65	0.63	0.52	0.51	
Profit After Taxes (RoA)	1.39	1.07	1.24	1.22	1.00	0.99	Near-term RoA lower mainly due to conservative assumptions for Forex Derivatives business. Bank has many levers for improving RoA (as described in the Report)
Leverage	14.04	19.63	11.23	14.86	16.08	16.41	We have factored in normalised leverage, keeping in mind the need for regular dilutions to keep Capital Adequacy above 12% (FY2007 leverage distorted due to capital raised near year-end, tends to normalise quickly for a fast-growing bank like Yes Bank)
ROE	19.46	21.04	13.88	18.10	16.08	16.26	In the medium-term, the Bank can deliver RoEs of 17-19%. Our Target P/ABV multiple of 2.7x represents a 30% discount to the Target multiple for HDFC Bank and Axis Bank to factor in execution risk and structurally lower RoEs in the near term. We believe it compares favorably, keeping in mind the higher growth trajectory of Yes Bank.

Source: Company, Angel Research

Incubation of retail banking operations: a compelling wealth creation proposition

Next up in the Bank's well calibrated business plan is the incubation of a differentiated retail liabilities and wealth management business in tier II & tier III cities. The Bank is targeting the 'mass affluent' customer segment (see next section for more details on this segment), primarily in the Northern and Western regions of the country. About 60 retail-focussed branches are expected to open by July, 2008 (increasing to a total of about 190 such branches by FY2010E). (Annexure 4 presents studies vindicating the Bank's locational and channel strategy).

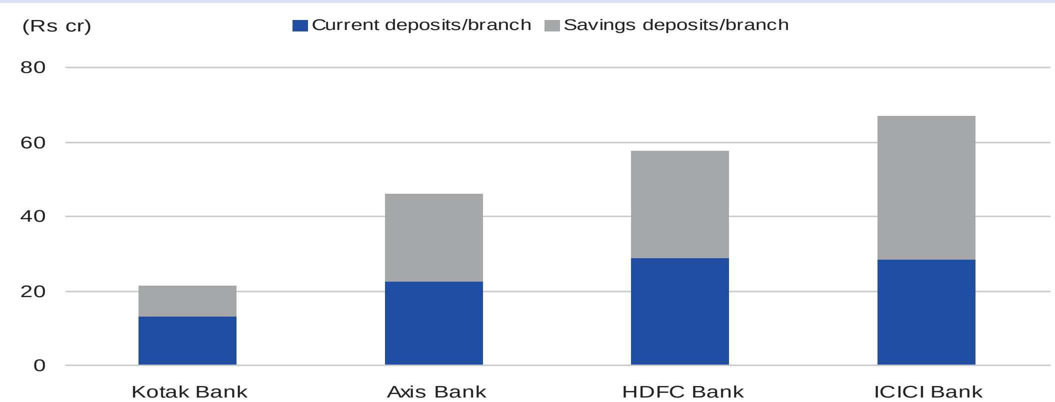
This branch expansion will involve upfront capex on furniture & fixtures, and also operating expenditure on lease and staff compensation (of an altogether higher order than the capex) that will exceed the income generated by the branches during the average gestation period of 18 to 24 months. But in the medium and long term, this branch expansion will add a lot of value. Additional Net Interest Income that a branch can generate in the medium to long-term is of the order of 3x to 5x the operating expense involved in running it (let alone the fee income from wealth management). [Note that RoEs for banks, though, are very much a function of regulatory capital requirements].

- **Core low-cost deposits**

Core deposits (i.e. Current & Savings accounts or CaSa) cost ~2% p.a. Benchmarked against cost of bulk deposits of 9-10%, a bank can earn an additional spread of 8% on these deposits. Thus, on a core deposit base of Rs15cr, a branch can generate additional Net Interest Income (NII) of Rs1.2cr. As the following chart depicts, the average CaSa per branch can increase, though over a period of time, to Rs40-60cr, generating NII of Rs3-5cr on branch-related operating expenses of about Rs1.2-1.5cr.

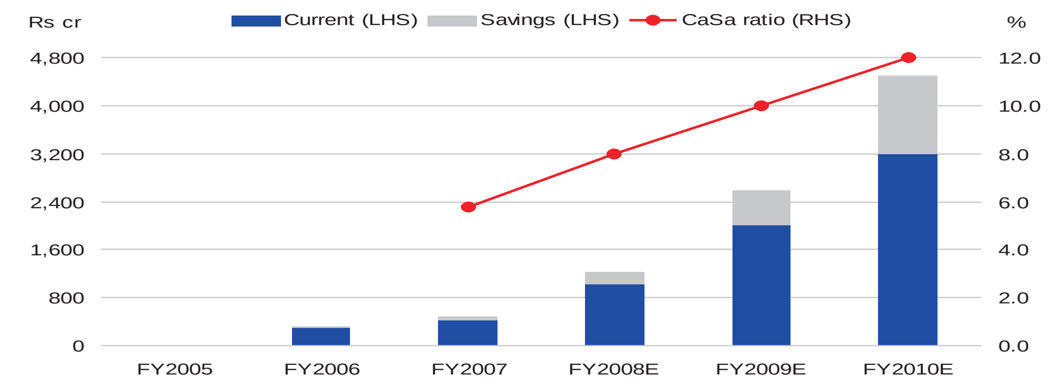
In our forecasts for Yes Bank, we have factored in average CaSa (including current deposits from wholesale branches) of Rs15cr per branch by FY2009E, increasing gradually to Rs18cr by FY2010E. Based on our projections, proportion of CaSa deposits will increase from 6% to 12% by FY2010E, while the long-term potential is evidently even greater.

Exhibit 12: Average CaSa/Branch for new private sector banks



Source: Company, Angel Research. Note: Nos. relate to FY2007

Exhibit 13: Yes Bank's projected growth in CaSa (long-term potential far greater)

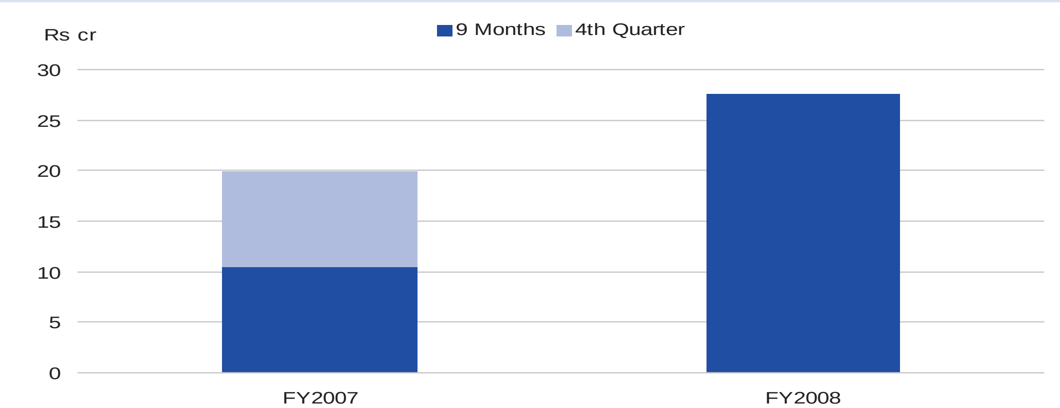


Source: Company, Angel Research

- **Bancassurance**

A huge customer base underpins bancassurance models of most large banks. The sales intensity for tapping into this customer base is low, making it a lucrative avenue for leveraging their existing franchise. The lack of such a customer base has, however, not stopped Yes Bank from entering into the growing bancassurance business. On the contrary, the Bank has adopted a high sales intensity, 'feet-on-street' model. This model will be driven by dedicated insurance advisers, domiciled in every retail branch, who will not just cross-sell to existing customers but also attempt to strike new customer relationships. Traction in this business is evident - while the Bank earned distribution commission of Rs20cr in FY2007, it earned a commission of Rs28cr in 9MFY2008 itself, with the typically busy 4th Quarter still to go. (While the structural growth outlook remains strong, we percieve some downside risks to near-term growth emanating from dampened capital markets. Accordingly, we have conservatively factored in a relatively sedate 55% CAGR from this income stream over FY2008-10E and it is possible that the Bank may well exceed this).

Exhibit 14: Income from 3rd party distribution grew 165% YoY in 9MFY2008



Source: Company, Angel Research

- **Other wealth management products**

In addition to insurance, Yes Bank will offer a single-point, comprehensive wealth management solution to meet the needs of its affluent customers. The Bank has an online distribution platform for mutual funds. Taking it one step further, real estate and even art have been added to the product suite. To complete the offering, the Bank has also begun demat and retail broking operations. The Retail Broking business is based on a direct online broking platform. Essentially, investment advisers at the branches will offer wealth management services, and the Bank will be in a position to distribute most of the products required by the customer.

Service differentiation & product innovation (the Technology and Human Resource dimensions) and Customer segmentation (the Franchise dimension) - evolution of a distinct brand

At the centre of Yes Bank's business plan is a differentiated service proposition that targets affluent customer segments and is high on convenience, innovation and aspirational value. We expect this differentiation to eventually evolve into a distinct brand with which the Bank's target customers will form strong associations - an arguably sustainable, competitive advantage.

Admittedly, the Bank will face formidable competition from larger, well-entrenched and trusted private banks for a share of the savings that will move over a period of time from public sector banks unable to provide an emerging, aspirational middle class with the desired service level. We acknowledge the significant execution risks underlying the business plans - moving from a wholesale to a retail business will be a different ball game altogether: dealing with a different class of customers, managing an increasing span of control, managing the evolution of a brand, winning the trust of customers, etc. The Bank does however score favorably on several fronts, as enunciated below.

Customer segmentation

Yes Bank intends to focus on the 'mass affluent' - customers with annual income greater than Rs500,000. Broadly, this segment comprises about 2% of Indian households, but contributes 21% of aggregate annual household savings. Importantly, by 2025, 15% of households are projected to become 'mass affluent' - they will contribute 60% of aggregate annual household savings. (Annexure 5 presents an analysis of the vast potential of 'Mass Affluent' customer segment).

To build this franchise, the Bank has brought onboard its team, Mr. Suhail Kazmi, as President-Retail banking & Wealth Management. He was formerly the Western Region Head for consumer banking with ABN AMRO - this foreign bank is reputed to have a superior, wealth management- focussed, retail banking presence in India. And infact, that is the kind of bank that Yes Bank is positioning itself against - it aims to be a domestic bank offering services on par with foreign banks having a presence in India.

The advantage it holds over them? RBI's support in expanding its branch network. Infact, by the end of FY2009, the Bank will have a product suite matching foreign banks and significantly, it will have more branches than the largest foreign bank in India - Standard Chartered Bank with 81 branches.

Service differentiation & product innovation

Yes Bank intends to compensate for a small physical network by offering advanced payment systems that encourages customers to make greater use of its high quality, online and mobile delivery channels. For instance, Yes Bank was one of the first banks in India to offer Online RTGS and NEFT to its customers. Also on offer will be a host of value-added services such as higher service quality and branch experience than existing Private banks, Long banking hours (7AM to 11 PM) at select branches, etc. We believe the Bank is building a track record in offering first-to-market incremental convenience and incremental innovation. Eventually, we feel, these small things will add up to create a distinct brand proposition, which, we believe, will constitute a sustainable competitive advantage for Yes Bank. We also like the sales-driven character of the organisation and the cutting edge technology backbone that it boasts of. (Annexure 6 takes a more detailed look at the Bank's strategy of Service differentiation & product innovation).

Eventually, management quality, depth and track record make the investment proposition credible

Ability to attract talent – at the core of the Bank's success

The Bank's promoter and MD, Mr. Rana Kapoor, has built an A-list top management team, which brings to the table rich experience from the best banks in India - including Bank of America, ABN AMRO, Citibank, ICICI Bank, Rabo India and HDFC Bank, amongst others. Highly experienced and qualified senior level management professionals are responsible for core divisions of the Bank – the Bank has Mr.Ajay Mahajan of Bank of America heading the Treasury Business, Mr.Aditya Sanghi of Rabo India heading the Investment Banking business, Mr.Sunil Gulati of GE Commercial Finance heading the Corporate business and Mr.Suhail Kazmi of ABN AMRO heading the Retail business, amongst others.

Track record: superior business strategy; impeccable execution and brand-building

We have attempted to predicate our investment case for the Bank on its successful track record so far. A lot of the Bank's value is derived from its projected growth – and the projections are credible only because of the track record that the Bank is building in executing a well-calibrated business plan, which leverages its strengths within the bounds of constraints like balance sheet size, branch network, etc. – at the same time steadily overcoming each of the constraints.

Relationship with RBI: an intangible asset

Yes Bank holds the distinction of being the only greenfield private sector bank to be set-up in India in the last decade. The Bank has not faced problems in securing the branch licenses it desires (the RBI enjoys an element of discretion in the licensing process). Also in favor of the Bank, we feel, are its chosen business segments (corporate lending, knowledge banking, IB, etc.), that we feel carry lower regulatory risk (in the near term at least) than for instance, non-collateralized personal loans, mortgages, capital market exposures, etc. The proposed focus on 'mass affluent' is also ultimately for mobilizing resources; on the asset side, the Bank has a large agri & food processing portfolio, as well as plans to increase its outreach by engaging with micro-finance institutions and building its own field technologies – thus achieving some semblance of balance on the financial inclusion front.

Further growth avenues: complementary financial services businesses like retail broking & private equity

There are a host of financial services businesses (insurance, broking, asset management, etc.) that many Indian banks have successfully built over the past few years, which leverage their distribution and franchise to provide customers with a comprehensive range of financial products (in the process creating tremendous shareholder wealth). Yes Bank too, intends to explore various opportunities at appropriate stages of its growth. To start with, the Bank is setting up an online retail broking venture to complete its wealth management offering. It has taken a 30% stake in an asset reconstruction company which has received RBI approval. It is setting up a USD100 mn food and agri business private equity fund. A USD100 mn healthcare fund (as a 50% JV with Gilde Investments of Netherlands) and an emerging corporates fund are also in the pipeline. The Bank expects to have about USD1-2 bn under management by FY2010 – on which the revenue model will be the standard 2% asset management fee and 20% carry. We have not factored in the upside from these and other potential lines of businesses in our present forecasts.

Ability to raise capital (at increasing premium)

We see intellectual capital as the real challenge for the Bank – as long as that is in place, financial capital should continue to be available. The Bank has infact showed an ability to place equity privately at a premium to even the prevailing market price (for instance, the Rs120cr placement to Swiss Re at Rs120/share when the market price was about Rs90).

An ideal acquisition target for foreign banks post liberalisation

In this report, the central theme emerging is that of a bank which is on a high-growth trajectory, is well-positioned, strongly branded, unfettered by legacy issues and has an impressive pool of intellectual capital, supported by an advanced technology backbone. We feel, this will make the Bank one of the most attractive acquisition targets in the Indian banking industry, after the impending liberalization of regulatory norms governing foreign banks [FY2009 commonly acknowledged as the 'due date' for this liberalization, though we feel non-resolution of capitalization and consolidation issues in PSU banks may push this date further].

The Indian promoters hold 19%, while Holland's Rabo Bank holds another 14.3% as FDI (apart from 5% more as FII). The Indian promoters have let it be known that Rabo Bank is only a financial investor and would like to monetize its holding once its NBFC, Rabo India Finance can be run as a bank post the abovementioned impending liberalization. The Indian promoters have expressed an openness to strategic investment by a 'large, MNC bank of global repute', post-liberalization. At that point, Yes Bank would have a comprehensive domestic footprint, and an alliance with a strategic partner having a global footprint and vying for entry into the Indian market, would be a win-win situation.

Investment Risks

Execution risk

Yes Bank faces significant execution risks in its metamorphosis from a wholesale bank having 1,200 corporate / emerging corporate clients to a retail bank targeting 30,000 SME customers and a huge number of retail customers (new customer acquisitions of the magnitude of 3-5lacs and beyond over the next few years). Challenges include:

- **Winning the trust of potential customers:** Banks are public trust institutions. Trust and long-term stability are crucial factors in convincing customers to bank their life savings. Bank failures like United Western Bank would only have exacerbated this concern.

[We believe a bank can build trust over a period of time by adopting the highest standards of risk management and corporate governance as well as inculcating an image of being a benevolent partner to its customers]

- **Small phsyical footprint vis-à-vis competition:** Without the convenience of a city-wide network of branches and owned ATMs, widespread customer acceptance may be delayed, thereby prolonging gestation period.

[Studies indicate that customers increasingly prefer transacting online and via mobile wherever possible - we have already described how Yes Bank's 'High-touch' delivery model is a key strength]

- **Disproportionate operational risk:** Hiccups/glitches in scaling up internal processes may lead to customer dissatisfaction, delay in product roll-outs, financial losses, etc.

[Standardization of internal processes and high level of IT-enabled automation can mitigate this risk]

Shortage of intellectual capital

In our opinion, this is a major challenge that the Bank faces. There are 2 issues here.

One, as the Bank expands rapidly, it will face stiff competition from not just other banks, but also corporates across industries, for a scarce human resource pool. Wage inflation in excess of 15-18% is a definite downside risk. More importantly, successful execution of the Bank's business plan hinges on quality manpower at all levels of the organization - an enduring shortage of the same would magnify execution risk.

The second risk is a high rate of attrition. Retaining talent is a complex challenge for knowledge-driven organizations like Yes Bank. Already, there have been a few high-profile exits at top management level (with the Risk management function seeing 3 changes at the top within a year).

The Bank has an attractive ESOP program in place (with a 4-year vesting period) to incentivise top management. As described earlier, 75% of the staff strength comprises of salespersons - their compensation is driven by performance-incentives. For knowledge-intensive roles, the Bank has a conscious strategy of building bench-strength, especially at the middle and lower levels.

Downturn in capital markets activity

A downturn in capital markets activity would directly affect the Bank's investment banking revenue stream constituting about 15% of the Bank's revenue. It would also have a direct dampening effect on the Bank's foray's into retail broking and private equity. Cross-selling of mutual funds and unit-linked insurance policies could also see a slowdown.

Increase in credit costs

Yes Bank presently has Nil gross NPAs - but its credit book is unseasoned. As the book goes through a longer period of high interest rates (especially when the business cycle changes), NPAs are likely to emerge and approach industry levels. Accordingly, we have factored in 0.6% slippages in FY2009E and 0.8% in FY2010E.

Valuations

At Rs186, the stock is trading at 2.1x our revised FY2010E Adjusted Book Value (ABV) of Rs88. We are reducing our 1-year forward target P/ABV multiple from 2.9x to 2.7x in light of lower RoE expectations in the near and medium-term (down to 16% for FY2010E as against 17% earlier). The multiple represents a 30% discount to the FY2010E P/ABV multiple of 3.9x at which we have valued HDFC Bank to take into account higher execution risk for a small bank like Yes Bank.

On account of 15% reduction in FY2009E EPS and 14% reduction in FY2010E EPS as well as lower price assumed for projected dilutions, we are revising our estimated FY2010E ABV downwards from Rs99 to Rs88. Accordingly, we arrive at a revised 12-month Target price of Rs238, which is 17.6% lower than our previous target price of Rs289. As described earlier, to be on the conservative side, we have reduced our estimates for the Bank and to the extent that the Bank continues to deliver healthy results, with minimal hit on the Forex Derivatives front, there would be upside to our estimates.

Since listing in July 2005, the Bank has traded in the range of 2.5-3.9x its 1-yr forward ABV. The median 1-yr forward P/ABV multiple during this period has been 3.2x and our Target multiple represents a 19% discount to this as well.

Given Yes Bank's relatively higher growth trajectory (supported by regular book accretive dilutions), we believe our Target Multiple compares favorably with the FY2010E P/ABV multiple at which we have valued HDFCBK (3.9x) and AXISBK (4.1x).

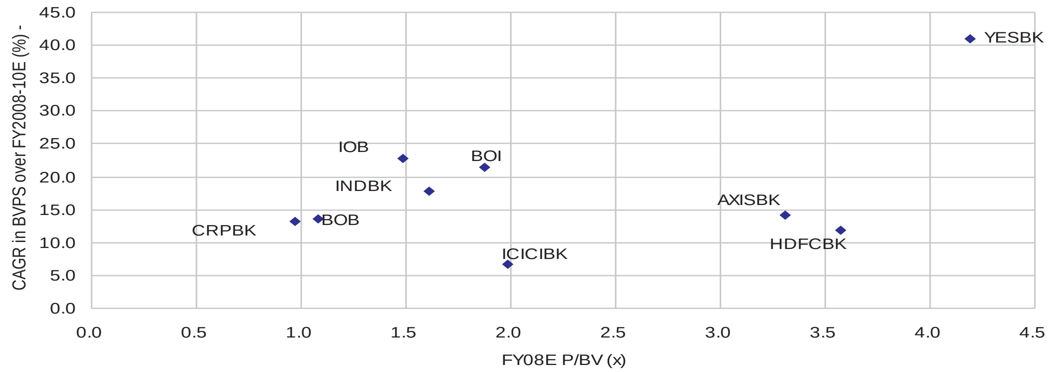
Infact, as our analysis of historical returns on HDFC Bank shows, the 2.3x to 4.4x 1-year forward P/ABV range which HDFC Bank has historically commanded, has progressively failed to capture a large portion of the wealth creation that the Bank has achieved over the past 12 years (35% CAGR in stock price between FY1996 and FY2007). We acknowledge that Yes Bank carries a high execution risk. However, we feel, at this stage in its evolution, the high growth rates that the Bank is expected to deliver should be accorded higher visibility than the incumbent private banks were during their early stages, on grounds of past investment experience in and proven business models of those private banks as well as by Yes Bank's own strengths (as described in this report). **Our 12 month Target price of Rs238 implies an upside of 28%. Hence, we maintain our Buy rating.**

Exhibit 15: Relative Valuation Matrix (FY2010E estimates)

Company	CMP	EPS	ABV	ROA	ROE	P/E	P/ABV
Axis Bank	805	54	312	1.3	18.1	15.0	2.6
Bank of Baroda	301	57	347	0.9	17.3	5.3	0.9
Bank of India	272	45	228	1.0	21.2	6.1	1.2
CBoP *	46	2	15	1.1	15.7	23.0	3.0
Corporation Bank	286	63	378	2.1	1.1	4.6	0.8
DCB *	91	8	52	1.1	12.8	11.4	1.8
HDFC Bank (post-merger)	1,401	72	503	1.4	15.3	19.4	2.8
ICICI Bank (incl. subsidiaries)	835	60	479	1.1	13.0	13.9	1.7
Indian Bank	171	30	137	1.5	24.0	5.7	1.3
IOB	136	32	135	1.4	26.2	4.2	1.0
PNB *	528	85	498	1.1	18.1	6.2	1.1
Union Bank *	146	29	160	0.9	19.9	5.1	0.9
Yes Bank	183	12	88	1.0	16.3	15.1	2.1

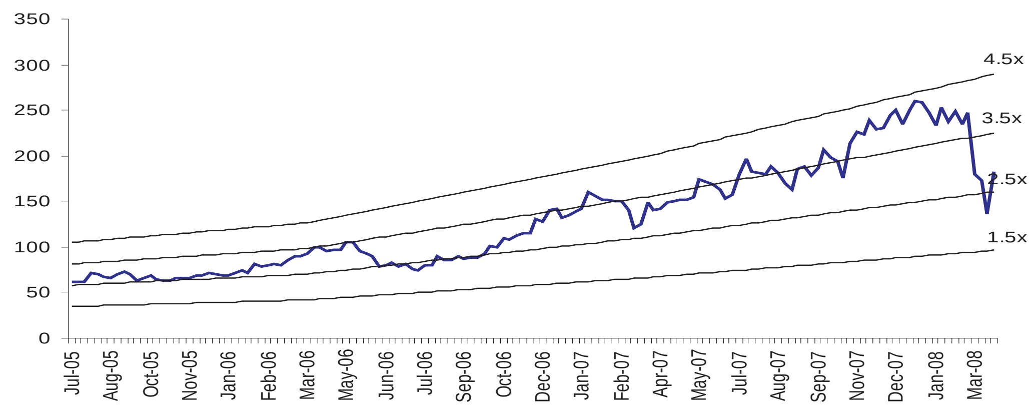
*Source: Company, Angel Research, * Bloomberg Estimates*

Exhibit 16: FY2008E P/ABV v/s 2-yr CAGR in ABV over FY2008-10E



Source: Bloomberg Estimates, Company, Angel Research. Note: ABV - Adjusted Book Value per share

Exhibit 17:Yes Bank's 1-yr forward P/ABV band

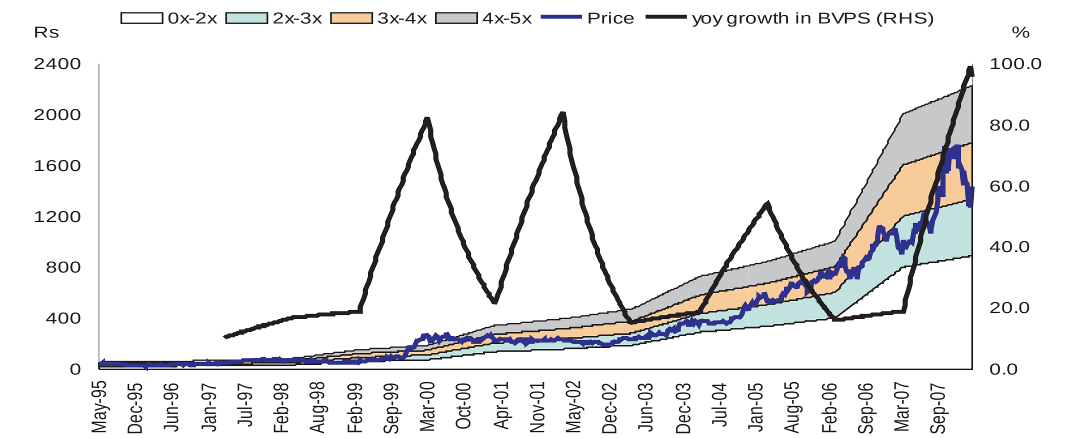


Source: Bloomberg, Company, Angel Research

Return on Investment on Private Banks – A Historical perspective

An analysis of HDFC Bank's valuations since FY1996 reveals that the multiples that the stock historically commanded failed to capture a large portion of the wealth creation that the Bank has achieved over the past 12 years. During this period the stock traded in the range of 2.3x to 4.4x its book value (and within a tighter range of 2.3x to 3.6x since FY2001, following the merger with Times Bank). The Bank delivered an average RoE of 20% and maintained an average payout of 24%. During the same period though, EPS grew at a CAGR of 38% and since Mar 1996 to date the stock delivered a 37% compounded return. Essentially, this was achieved through regular book accretive dilutions, driven by continuing visibility of high growth. Thus, 3 dilutions of 22%, 16% and 10% in FY2000, FY2002 and FY2005 respectively, enabled a consistent 30% CAGR in book value over a 12 year period. A 14% dilution in FY2008, together with further proposed dilution of 6% to HDFC, should enable it to exceed this growth rate in book value, with yoy growth of 100% in FY2008.

Exhibit 18: HDFCBK's 12-yr price band and YoY growth in BVPS



Source: Bloomberg Estimates, Company, Angel Research

An analysis of Axis Bank's valuations reveals a similar picture – While the Bank delivered an average RoE of 23% since FY1999 and maintained a payout of 28%, EPS grew at a CAGR of 33% and the stock delivered compounded returns of 52% (higher returns were partly driven by gradual rerating from sub 1x P/ABV multiples upto FY2003 to 2.5-2.8x levels presently, as the market continued to recognize and reward the Bank's transformation into a strong private sector bank with an evolving business model that offered attractive potential for wealth creation). Again, book accretive dilutions of 20% each in FY2003 and FY2005 enabled 29% CAGR in book value – infact, the Bank has shifted to a higher growth trajectory, with 100% YoY growth in book value in FY2008E to support business expansion.

Yes Bank's valuations also imply the need for regular book accretive dilutions. The Bank delivered a 32% YoY growth in book value in FY2007 on the back of a 3.7% dilution and a 58% yoy growth in book value in FY2008 on the back of a 5.25% dilution. We have factored in 2 dilutions of 6-7% each during our explicit forecast period upto FY2010E. We expect the Bank to raise the required capital at increasing premiums, driven by a high growth trajectory (as described in this report). We acknowledge that Yes Bank carries a high execution risk. However, we believe, at this stage in its evolution, the high growth rate that the Bank is expected to deliver has a higher visibility than the abovementioned banks enjoyed during their early stages, drawing on past investment experience in and proven business models of those private banks as well as by Yes Bank's own strengths (as described in this report). Thus, we believe, our target P/ABV multiple of 2.7x compares favorably with the FY2010E P/ABV multiple at which we have valued HDFCBK (3.9x) and AXISBK (4.1x).

Annexure 1: Investment banking - gaining credibility as an outbound transaction specialist

Yes Bank's Investment Banking division is one of the core profit-churning divisions of the Bank (apart from Treasury), contributing about 34% of the Bank's fee income in FY2007. The division has executed over 30 deals since January 2006, including prominent outbound cross-border deals like the USD1.4 bn acquisition of Repower by Suzlon Energy, the USD115 mn acquisition of Advanta Netherlands Holdings for United Phosporus, etc. in that period.

The division is headed by Mr. Aditya Sanghi (who was earlier the Head of Rabo India Finance's M&A division), and in a short period has moved up the Bloomberg M&A league tables - It was ranked 7 in outbound cross-border deals in 9MCY2007, ahead of Kotak Mahindra Capital (12th), Ambit (18th) and E&Y (19th).

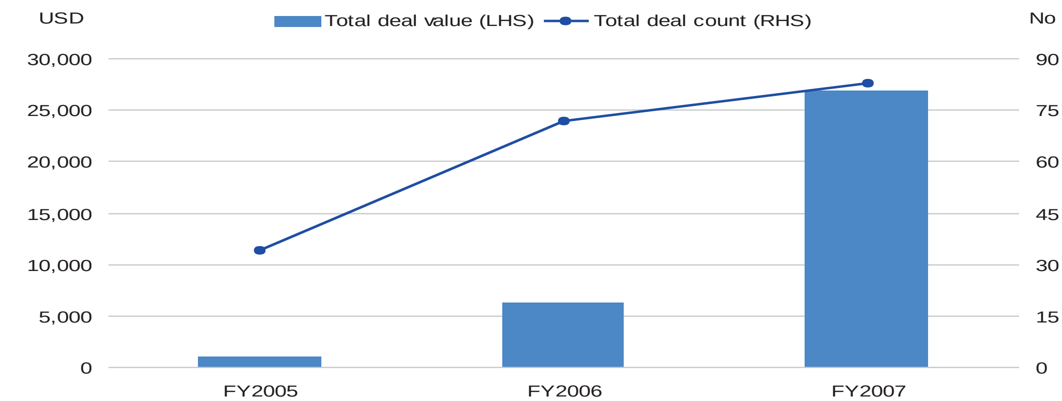
Exhibit 19: Bloomberg League table - outbound cross-border M&A deals in 9MCY07

Adviser	Rank	Market Share (%)	Deal Value (USD Mn)	Deal Count
UBS	1	34.6	8,304	5
Morgan Stanley	2	24.1	5,782	4
Evercore Partners Inc	3	23.8	5,706	1
ABN AMRO Bank NV	4	16.8	4,025	3
Credit Suisse	5	10.7	2,563	4
Citi	6	10.6	2,534	4
Yes Bank	**7**	**6.1**	**1,465**	**6**
Genuity Capital Markets	8	5.9	1,421	1
Standard Chartered PLC	9	5.6	1,342	3
Macquarie Bank Ltd	10	5.4	1,300	1
ICICI Bank	11	4.9	1,177	1
Kotak Mahindra Capital Company	12	3.2	778	5
HSBC	13	3.1	753	5
First Securities ASA	14	2.7	645	1
Deutsche Bank AG	15	2.5	610	2
Lehman Brothers	16	2.4	568	1
Rothschild	17	1.8	430	3
Ambit Corporate Finance Ltd	18	1.7	415	3
Ernst & Young	19	1.5	354	11
Jefferies & Co	20	1.4	335	2

Source: Bloomberg, Angel Research. Note: Market share has overlap since large deals with more than 1 advisor are included in each adviser's share

It must be noted that about 75% of the Bank's mandates (by deal value) have come from 1 client (Suzlon) & another 10% from another (Untied Phosporus). However, large deals like Suzlon-Repower should improve the Investment & merchant banking division's standing (especially in the growing outbound cross-border M&A market). The management eventually intends to hive off this division into a separate subsidiary.

Exhibit 20: Growing appetite for outbound cross-border M&A deals in India



Source: Bloomberg, Angel Research

Exhibit 21: Top 10 cross-border acquisitions since January 2004

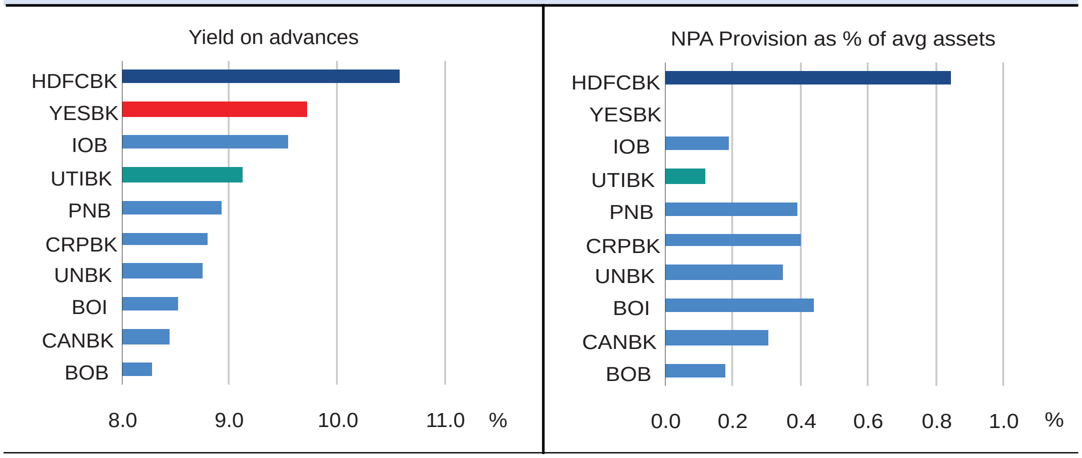
Announcement Date	Target Name	Acquirer Name	Deal Value (USD Mn)
17-Oct-06	CORUS GROUP PLC	TATA STEEL LIMITED	12,780
11-Feb-07	NOVELIS INC	HINDALCO INDUSTRIES LIMITED	5,706
15-Apr-07	ALGOMA STEEL INC	ESSAR GROUP	1,421
9-Feb-07	REPOWER SYSTEMS AG-REG'D	SUZLON ENERGY LIMITED & OTHERS	1,377
31-Mar-07	MULTIPLE TARGETS	TATA POWER COMPANY LIMITED	1,300
16-May-07	WHYTE & MACKAY	UNITED SPIRITS LIMITED	1,177
14-Aug-06	OMIMEX DE COLOMBIA LTD	MULTIPLE ACQUIRERS	800
23-Aug-06	ENERGY BRANDS INC	TATA GROUP	677
30-May-05	EGYPTIAN FERTILISER CO SAE	MULTIPLE ACQUIRERS	652
9-Jan-07	SINVEST ASA	ABAN OFFSHORE LIMITED	645

Source: Bloomberg, Angel Research

Annexure 2: Charts emphasizing ratios influencing Yes Bank's RoE

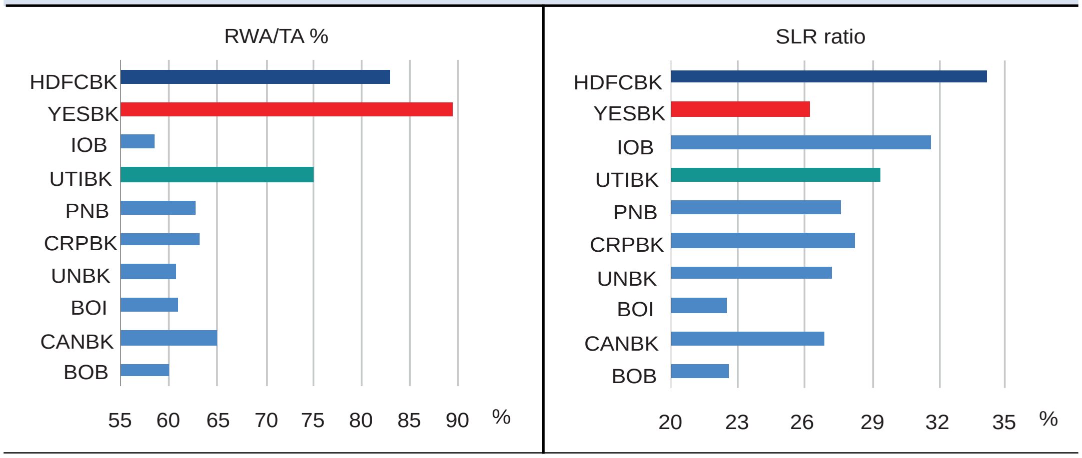
- Yes Bank's relatively superior underwriting of risk (Nos. relate to FY2007)

Exhibit 22: Superior yields, given corporate portfolio, especially, given nil credit costs



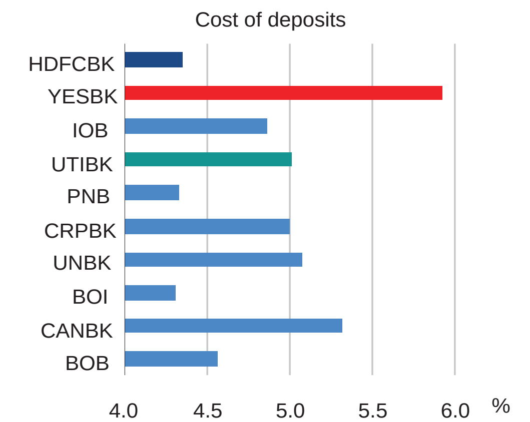
Source: Bloomberg, Angel Research

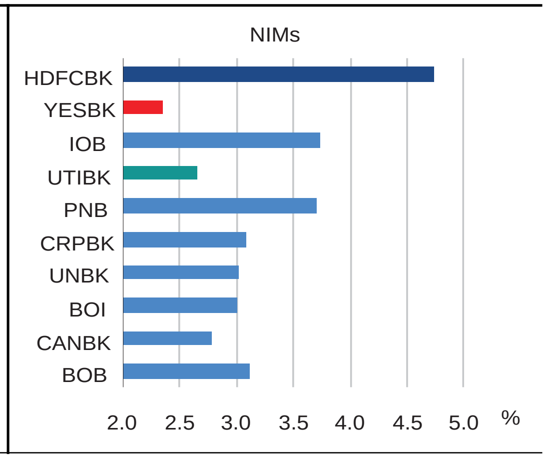
Exhibit 23: Reasonable capital charge for RWA (in light of relative SLR holding)

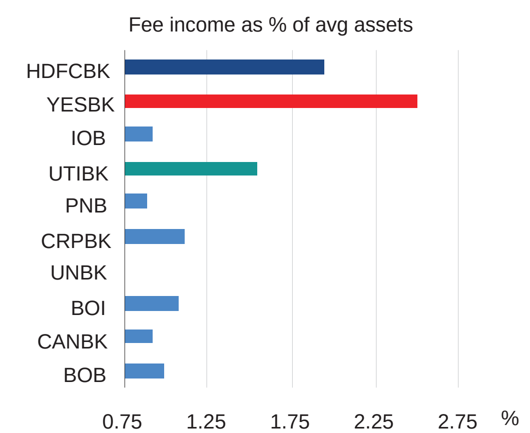


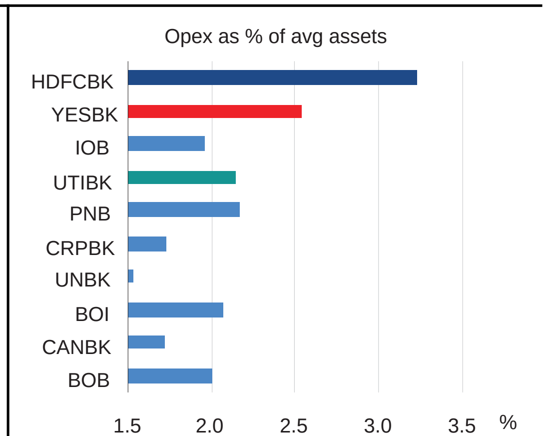
Source: Company, Angel Research. Note: RWA - Risk Weighted Assets

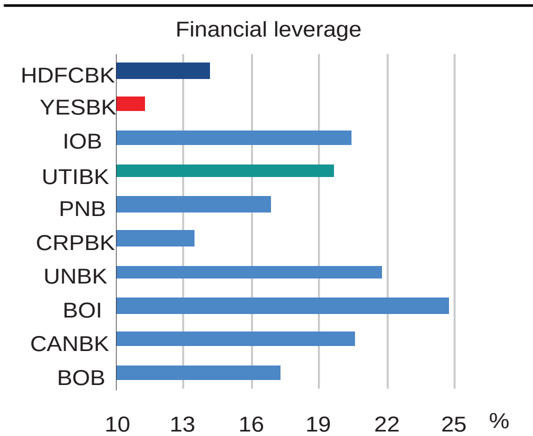
- Yes Bank's RoE for FY2007 - Interplay of bulk deposits-fed growth, robust fee income and gestation-period expenditure; financial leverage at a point in time relatively volatile for a small, growing bank like Yes Bank but normalizes quickly

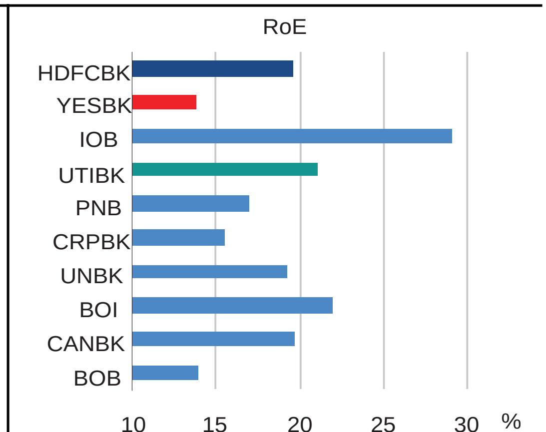










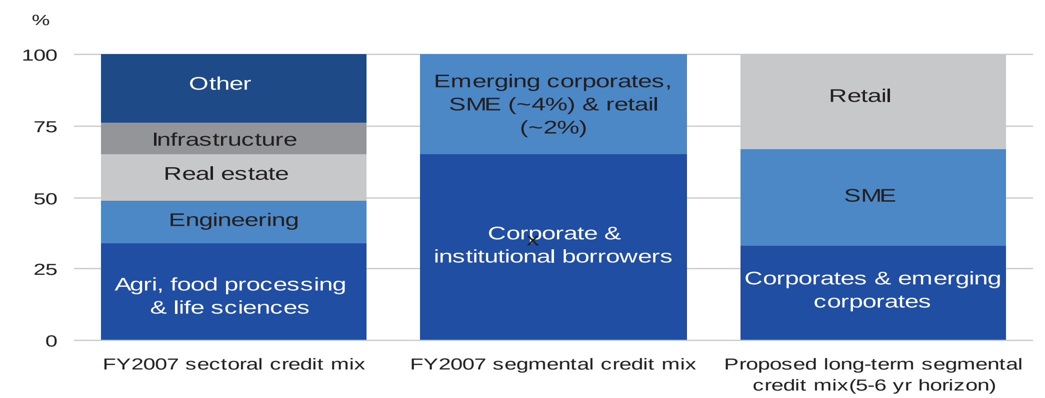


Source: Company, Angel Research

Annexure 3: Lending strategy - structured product offerings & knowledge banking approach

To date, Yes Bank has leveraged on strong relationships for lending to ~1,200 corporate and emerging corporate customers. The Bank has strong structuring capabilities for meeting specialised and complex client needs. Flexible, innovative financing structures and efficient underwriting of risks have enabled the Bank to earn high yield on advances inspite of having negligible SME & retail exposure, at the same time maintaining impeccable asset quality. (Note also, the 15% share of lending to commercial real estate, which offers lucrative risk-adjusted returns). The Bank often partners with government bodies and other institutions to prepare 'knowledge' reports (research reports on investment/development opportunities), which serve two purposes: serving as a means to access and connect with potential customers and providing intrinsic sectoral knowledge of the underlying risks while lending to these very customers, thereby enabling effective pricing and risk-taking.

Exhibit 24: Characteristics of the Bank's credit portfolio



Source: Bloomberg, Angel Research

SME lending

From this year, the Bank has shifted its thrust to the SME segment. By September 2008, it will have 45 branches in concentrated SME clusters, giving it access to 30,000 potential SME customers. SME loans command about 3-4% spread over corporate loans and constitute the key focus area of most domestic banks. One way in which Yes Bank intends to differentiate itself is through its newly setup SME Financial Advisory division, separate from its core Financial Advisory group, to focus on servicing the growing needs of emerging SME businesses.

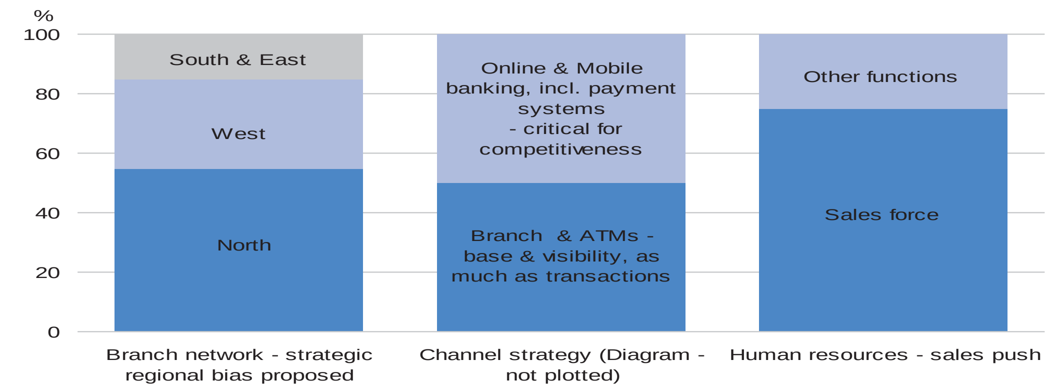
Retail lending

The Bank had so far consciously avoided retail lending due to its perception that this segment offered unfavorable risk-adjusted returns. However, evolving realignment of prices have made certain segments attractive, according to the Bank (corroborated by a major retail-lending bank).

Accordingly, the Bank is entering 5 or 6 major cities in select product categories like personal loans to salaried persons (especially employees of its corporate clients), small business loans and home equity loans – all of which offer very high yields. In the next stage, the Bank will enter the credit card segment as well.

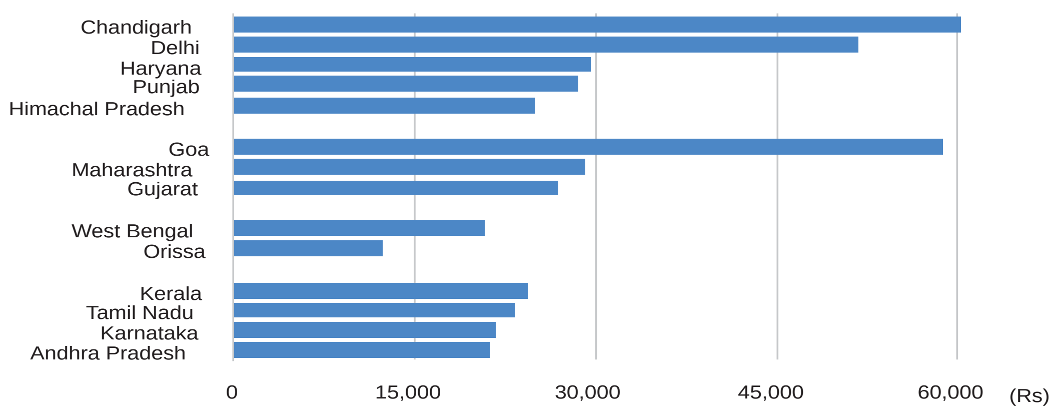
Annexure 4: Numbers support Yes Bank's regional and channel strategy for Retail business

Exhibit 25: Proposed channel characteristics



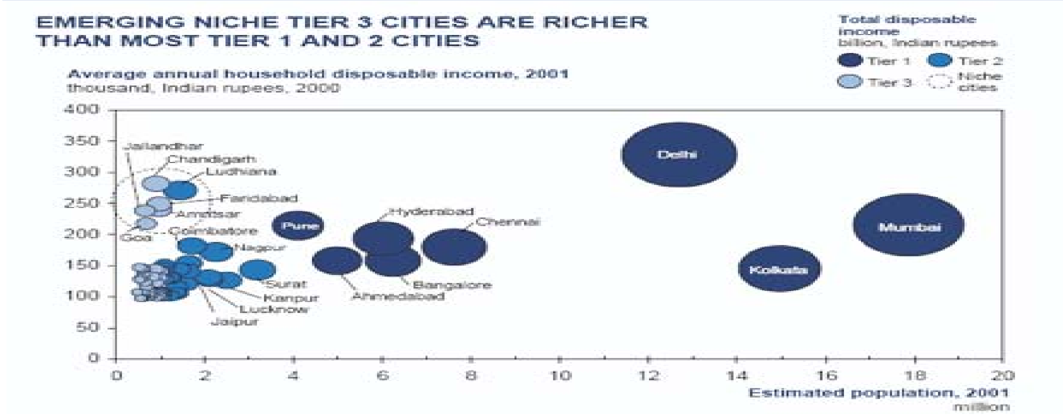
Source: Company, Angel Research

Exhibit 26: Per Capita NNP for Cross-section of States & Union Territories



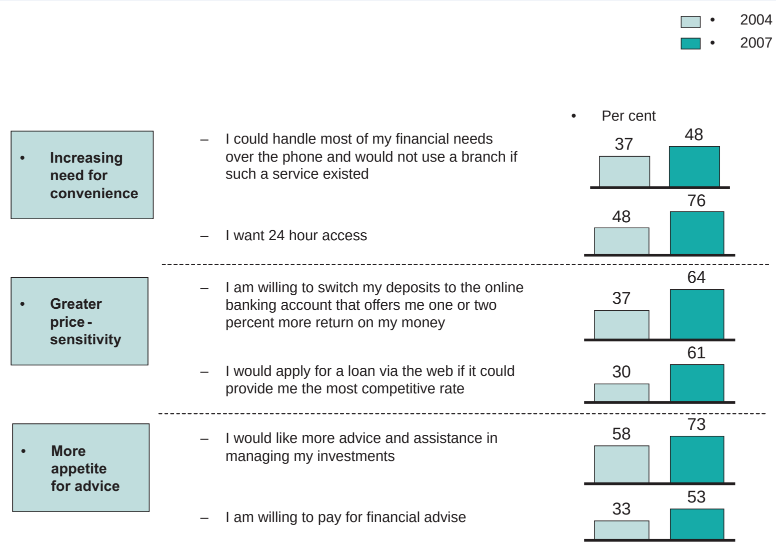
Source: CSO, Angel Research. Note: NNP - Net National Product

Exhibit 27: Many smaller cities now have relatively high per-capita income



Source: The Great Indian Middle Class, NCAER; MGI India Consumer Demand Model, v1.0; MGI Analysis

Exhibit 28: Indian retail consumers are rapidly becoming more sophisticated



Source: McKinsey PFS Survey of Urban Indian consumers; McKinsey analysis

Annexure 5: The 'Mass Affluent'

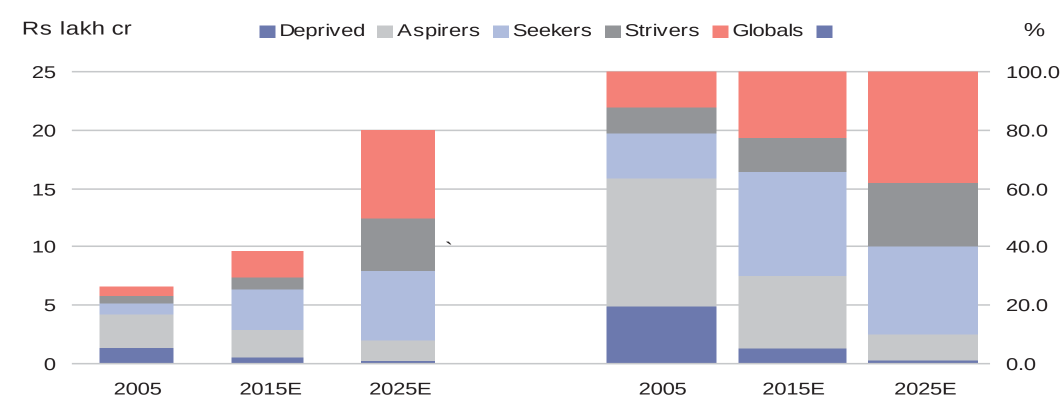
In their survey and analysis of Indian households, NCAER & Mckinsey Global Institute have classified households into the following (annual) income brackets: 'Globals' [>Rs10lacs]; 'Strivers' [Rs5lacs to Rs 10lacs]; 'Seekers' [Rs2lacs to Rs5lacs]; 'Aspirers' [Rs90,000 to Rs2lacs] and 'Deprived' [<Rs90,000]. By that classification, Yes Bank's target customers are globals and strivers (henceforth, we shall refer to them as the 'mass affluent').

These econometric projections facilitate an objective analysis and appreciation of the attractiveness of the mass affluent segment. In 2005, there were ~36lakh mass affluent households (~1.5cr people), whose aggregate annual savings were Rs1.4 lakh cr. Put differently, they comprised 2% of Indian households, but contributed 21% of the annual savings. Strong economic growth during 2005-2015 will mean that by 2015, 3.6% (90lakh) of Indian households will be 'mass affluent' – significantly, they will contribute 35% (Rs3.3 lakh cr) of aggregate annual savings.

Exhibit 29: Income bracket-wise household distribution

Source: NCAER, Mckinsey Global Institute, Angel Research

Exhibit 30: Income bracket-wise aggregate annual household savings

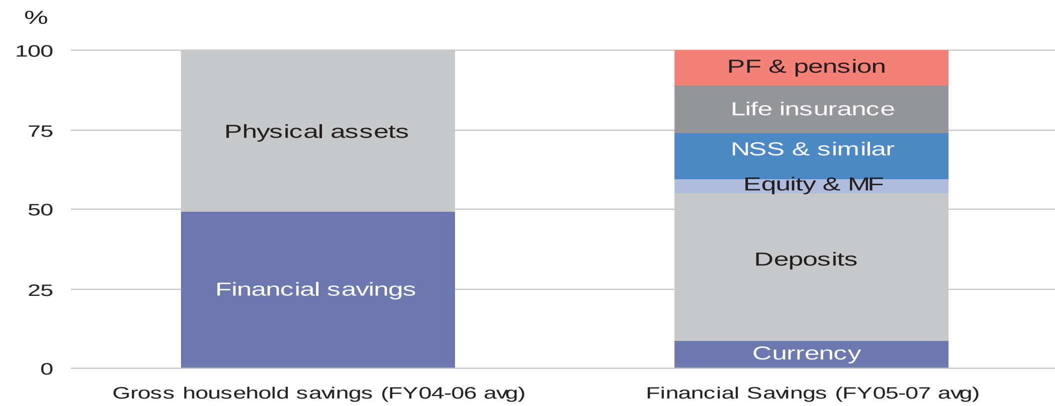


Source: NCAER, Mckinsey Global Institute, Angel Research

By the year 2025, the mass affluent will account for a massive portion of the economy – 4.3cr households with savings of Rs12 lakh cr. In percentages, 15% of the households accounting for a massive 60% of savings. (Drawing on the experience of developed western economies as well as an understanding of dynamics of the Indian economy, these projections capture the impact of increasing consumerism, increasing corporatisation and a deeper, more efficient financial system on savings, investments and spending patterns. For instance, savings of mass affluent households are expected to decline from 39% of income in 2005 to 28% by 2025, while those of other income brackets are expected to decline from 26% to 17% during the same period.)

Yes Bank's retail business model is centered around comprehensive wealth management solutions. This will effectively enable the Bank to earn percentages (be it interest spread, brokerage or asset management fees) over the entire financial savings pie of its chosen customer segment.

Exhibit 31: Composition of household savings



Source: RBI, Angel Research

Annexure 6: Service differentiation & product innovation

How does Yes Bank intend to provide its 'mass affluent' customers something more?

- **Advanced payment systems - a big draw**

Yes Bank intends to compensate for a small physical network by developing a 'high-touch' model that encourages customers to make greater use of its high quality, online and mobile delivery channels. Yes Bank was one of the first banks in India to offer Online RTGS and NEFT to its customers. RTGS is a critical development, in that it eliminates float for incumbent banks - consumers benefit by earning interest on what was previously a float. Inevitably, competitive pressures mean, every bank will begin to offer this facility. Also in the works, is the introduction of mobile payment solutions. Thus, what is an inherent disadvantage for Yes Bank - a small branch and ATM network - may prove to be an advantage in the future as customers migrate to cheaper, advanced payment systems as against the legacy systems that entailed large capital outlays for larger banks. In the near future, we do see the comparitively small physical network as a risk factor to customer acceptance. RBI's well-publicised move to make across-the-board ATM usage of any bank free of cost to the customer does however, remove a potentially significant deterrent to customer adoption of Yes Bank. The Bank has tie-ups to provide its customers with access to 23,000 ATMs for which it bears the Rs10 transaction cost.

- **Value added services - subjective, but not illusory**

We have already described the comprehensive range of wealth management solutions that the Bank has in its product suite comprising Deposits, Insurance, Mutual Funds, Stock Broking, Real Estate and Art. But then, most banks do provide these products & services as well. On some level, no doubt, Yes Bank will simply have to provide more for less to make inroads into its target markets - a case in point is the interest rate on its retail term deposits, 50 bps higher than the market rate. Also on offer will be a host of other value-adds:

  - Higher service quality and branch experience than existing Private banks – we feel, there are ongoing economic & cultural shifts in India's consumer class, underpinning the demand for such service levels.
  - Long banking hours (7AM to 11 PM) at select branches, etc.

Do the above represent a sustainable advantage or even an advantage? Probably NOT. But they are instances of first-to-market incremental convenience and incremental innovation. What one must appreciate is the culture underlying these offerings; once that is in place, one can expect numerous innovations to keep coming out of the Bank's stable. We feel the Bank is building a track record in this respect. Eventually, we feel, these small things will add up to create a distinct brand proposition, which, we feel, will constitute a sustainable competitive advantage for Yes Bank.

- **A sales-driven organisation with a cutting edge technology backbone**

Right from inception, the Bank has followed an HR model where-in many support functions like IT infrastructure management, etc. are outsourced and sales personnel are directly inducted onto the rolls of the company. The cutting-edge technology backbone includes I-Flex's Flexcube core-banking solution, Murex platform for Treasury, IT infrastructure ownership & management by Wipro Infotech and state-of-the-art (& cost-effective) central processing centres at Mumbai & Gurgaon.

The Bank's staff of about 3,000 people comprises of about 75% sales personnel and this mix is expected to continue in the future (the Bank intends to have a staff strength of about 4,500 people by the end of FY2008). Most of the salespersons are cross-trained to sell multiple products. For instance, during the life insurance lean season, those salespersons engage in CaSa mobilisation efforts. Strong relationships and high intensity sales push have been and will continue be a key determinant of the Bank's success, especially given its comparatively smaller physical network and unviable size for an advertising push at this stage.

Profit and Loss Account

Rs crore

Y/E March	FY2007	FY2008E	FY2009E	FY2010E
Net Interest Income	**171**	**328**	**609**	**996**
- YoY Growth (%)	94.6	91.5	85.7	63.4
Other Income	**201**	**357**	**567**	**862**
- YoY Growth (%)	101.1	78.0	58.7	52.0
Net Operating Income	**372**	**685**	**1,176**	**1,858**
- YoY Growth (%)	98.0	84.2	71.6	57.9
Operating Expenses	**194**	**358**	**662**	**1,060**
- YoY Growth (%)	124.7	85.0	85.0	60.0
Pre - Provision Profit	**179**	**327**	**514**	**798**
- YoY Growth (%)	75.4	83.4	57.0	55.2
Prov. and Contingencies	**35**	**40**	**108**	**185**
- YoY Growth (%)	101.3	15.2	168.7	71.5
Profit Before Tax	**144**	**287**	**406**	**613**
- YoY Growth (%)	70.1	99.9	41.4	50.9
Provision for Taxation	**49**	**98**	**138**	**208**
- as a % of PBT	34.3	34.0	34.0	34.0
PAT	**94**	**190**	**268**	**404**
- YoY Growth (%)	70.4	100.9	41.4	50.9

Key Ratios

Y/E March	FY2007	FY2008E	FY2009E	FY2010E
Per Share Data (Rs.)				
EPS	3.4	6.4	8.5	12.1
ABVPS	28.1	44.4	64.4	88.1
Profitability ratios (%)				
NIMs	2.3	2.2	2.4	2.5
Cost to Income ratio	52.0	52.2	56.3	57.0
ROA	1.2	1.2	1.0	1.0
ROE	13.9	18.1	16.1	16.3
Leverage (%)				
Loan deposit ratio	76.5	76.5	76.5	76.5
CAR	13.6	12.6	12.6	12.5
- Tier I	8.2	7.3	6.6	6.6
Asset Quality (%)				
Gross NPAs	-	0.1	0.4	0.8
Net NPAs	-	0.0	0.1	0.2
Slippages	-	0.1	0.6	0.8
Loan loss prov. /avg. assets	-	0.0	0.2	0.3
Valuation Ratios				
PER (x)	54.3	28.4	21.5	15.1
P/ABVPS (x)	6.5	4.1	2.8	2.1

Balance Sheet

Rs crore

Y/E March	FY2007	FY2008E	FY2009E	FY2010E
Share Capital	280	295	315	335
Reserve & Surplus	507	1,013	1,711	2,615
Deposits	8,220	15,208	25,853	37,487
- Growth (%)	182.5	85.0	70.0	45.0
Borrowings	867	1,401	2,182	2,884
Bond Capital	479	899	1,699	2,499
Other Liab. & Provisions	750	1,196	1,816	2,241
Total Liabilities	**11,103**	**20,010**	**33,575**	**48,060**
Cash in Hand and with RBI	390	1,113	1,892	2,728
Bal.with banks & call money	903	700	1,175	1,682
Investments	3,073	5,780	9,428	13,118
Advances	6,290	11,636	19,781	28,682
- Growth (%)	161.3	85.0	70.0	45.0
Fixed Assets	71	80	124	168
Other Assets	377	700	1,175	1,682
Total Assets	**11,103**	**20,010**	**33,575**	**48,060**
- Growth (%)	166.7	80.2	67.8	43.1

Fund Management & Investment Advisory	**(☎ 022 - 4040 3800 / 2835 9600)**	
Ajay Jaiswal	Investment Strategist (Kolkata)	ajay.jaiswal@angeltrade.com
P. Phani Sekhar	Fund Manager	phani.sekhar@angeltrade.com
Research Team	**(☎ 022 - 4040 3800 / 2835 9600)**	
Hitesh Agrawal	Head - Research, Cement, Media	hitesh.agrawal@angeltrade.com
Sarabjit Kour Nangra	VP-Research, Pharmaceutical	sarabjit@angeltrade.com
Vaishali Jajoo	Automobile	vaishali.jajoo@angeltrade.com
Harit Shah	IT, Telecom	harit.shah@angeltrade.com
Rohit Nagraj	Oil & Gas	rohit.nagraj@angeltrade.com
Pawan Burde	Metals & Mining	pawan.burde@angeltrade.com
Vaibhav Agrawal	Banking	vaibhav.agrawal@angeltrade.com
Girish Solanki	Mid-cap	girish.solanki@angeltrade.com
Shailesh Kanani	Infrastructure & Real Estate	shailesh.kanani@angeltrade.com
Anand Shah	FMCG	anand.shah@angeltrade.com
Sulabh Agrawal	Mid-cap	sulabh.agrawal@angeltrade.com
Puneet Bambha	PMS	puneet.bambha@angeltrade.com
Amit Bagaria	PMS	amit.bagaria@angeltrade.com
Akshat Vyas	Research Associate (Pharmaceutical)	akshat.vyas@angeltrade.com
Reena Walia	Research Associate (Mid-cap)	reena.walia@angeltrade.com
Neha Idnany	Research Associate - (PMS)	neha.idnany@angeltrade.com
Sandeep Wagle	Chief Technical Analyst	sandeep@angeltrade.com
Ajit Joshi	AVP Technical Advisory Services	ajit.joshi@angeltrade.com
Milan Sanghvi	Sr. Technical Advisor	milan.sanghvi@angeltrade.com
Nitin Kunte	Technical Advisor	nitin.kunte@angeltrade.com
Brijesh Ail	Technical Analyst	brijesh@angeltrade.com
Vaishnavi Jagtap	Technical Analyst	vaishnavi.jagtap@angeltrade.com
Siddarth Bhamre	Fund Manager - Derivatives & Equities	siddarth.bhamre@angeltrade.com
Commodities Research Team		
Amar Singh	Research Head (Commodities)	amar.singh@angeltrade.com
Samson P	Sr. Technical Analyst	samsonp@angeltrade.com
Anuj Gupta	Sr. Technical Analyst	anuj.gupta@angeltrade.com
Girish Patki	Sr. Technical Analyst	girish.patki@angeltrade.com
Commodities Research Team (Fundamentals)		
Badruddin	Sr. Research Analyst (Agri)	badruddin@angeltrade.com
Mandar Pote	Research Analyst (Energy)	mandar.pote@angeltrade.com
Bharathi Shetty	Research Editor	bharathi.shetty@angeltrade.com
Bharat Patil	Production	bharat.patil@angeltrade.com

Research & Investment Advisory: Acme Plaza, 3rd Floor 'A' wing, M.V. Road, Opp Sangam Cinema, Andheri (E), Mumbai - 400 059

Ratings (Returns)	Buy (> 15%)	Accumulate (5 to 15%)	Neutral (5 to -5%)	Reduce (> -5%)	Sell (> -15%)

Corporate & Marketing Office	:	612, Acme Plaza, M.V. Road, Opp Sangam Cinema, Andheri (E), Mumbai - 400 059	Tel : (022) 4000 3600 / 2835 9600
Wealth Management	:	e-mail : wmshelpdesk@angeltrade.com	Tel : (022) 4035 3100
Investment Advisory Helpdesk	:	e-mail : advisory@angeltrade.com	Tel : (022) 4040 3800
Commodities	:	e-mail : commodities@angeltrade.com	Tel : (022) 4035 8600
Feedback	:	e-mail : feedback@angeltrade.com	Tel : (022) 2835 5000

Regional Offices:

Ahmedabad - Harshit Bhavsar
Tel: (079) 3007 0749 - 751

Bengaluru - Dhiraj Pandey
Tel: (080) 4153 6700 - 03

Chennai - Thiruneer Selvan
Tel: (044) 4226 9000 Fax: 2498 1742

Hyderabad - Shiva Shankar
Tel: (040) 6673 3573 / 74

Indore - Pramathu Chowksey
Tel: (0731) 3013 360 - 65

Jaipur - Ranveer Singh
Jaipur - 302 001 Tel: (0141) 222 3334

Kanpur - Vivek Singh
Tel: (0512) 3297 478/3017 700

Kolkata - Vijay Kothari
Tel: (033) 4009 9899

Lucknow - Ejaz Moyi
Tel: (0522) 6567 826

Nagpur - Sanchit Tiwari
Tel: (0712) 3041 500

Nashik - Nilesh Supekar
Tel: (0253) 6614 235/236

New Delhi - Rohit Pateria
Tel: (011) 4605 6600 / 4151 2555 / 2666

Pune - Sunita Magnani
Tel: (020) 2551 3143 / 2553 0912 - 14

Rajkot - Vijay Popat
Tel :(0281) 6451929 / 1910

Surat - Pinky Kothari
Tel: (0261) 6696 666

Visakhapatnam - Vamsi Krishna
Tel :(0891) 6620 572-75

Private Client Group Offices:

Mumbai - Prakarsh Gagdani
Tel: (022) 4040 3800 Fax: (022) 4040 3899

Ahmedabad (C. G. Road) - Arpit Shah
Tel: (079) 3007 4049 / 50

Rajkot (Pedak Road) - Murtuja Sadikot
Mobile : 98245 00252

Surat - Amit Keshwani
Tel : (0261) 6696 666

Sub - Broker Marketing:

Premier House - Pankaj Mungre
Tel: (022) 4035 8600

Branch Offices:

Andheri (Lokhandwala) - Muskaan Doultani
Tel : (022) 2639 2626 / 3255 0987

Andheri (W) - Dinesh Nihalani
Tel: (022) 2635 2345 / 6668 0021

Bandra (W) - Gyan Joshi
Tel: (022) 2655 5560 / 70

Bandra (W) - Faruq Wakani
Tel: (022) 6643 2694 - 99

Borivali (W) - Gautam Agarwal
Tel:(022) 2895 2600 / 1 / 2

Borivali (W) - Tarun Dhami
Tel: (022) 3092 1969 / 2892 8890

Chembur - Rajesh Mehta
Tel:(022) 6703 0210 / 11 /12

Chembur - (Basant) - Atul Dwivedi
Tel:(022) 3267 9114/ 15/ 16

Fort - Ajit Karandikar
Tel: (022) 2263 4050-55

Ghatkopar (E) - Ashwin Thakkar
Tel: (022) 6799 3185 - 88 / 2510 1525

Goregaon (W) - Sanjiv Dhami
Tel: (022) 2878 9401 / 02

Kalbadevi - Viren Ved
Tel: (022) 2243 5599 / 2242 5599

Kandivali (W) - Sachin Ghelani
Tel: (022) 2867 3800 / 2867 7032

Kandivali (Thakur Village) - Akharam Chaudhary
Tel: (022) 2846 1267 / 1654 / 2056 / 2076

Malad (E) - Satish Kanwarjani
Tel: (022) 2880 4440

Malad (W) - Tushar Shah
Tel: (022) 2880 0960 / 68

Mulund (W) - Niraj Anand
Tel: (022) 2562 2282

Powai (E) - Prashant Auti
Tel: (022) 40262170 / 1 / 2 / 3

Thane (W) - Rajesh Kumar
Tel: (022) 2539 0786 / 0789 / 0796

Vashi - Punit Chopra
Tel: (022) 2765 4749 / 2251

Vile Parle (W) - Dimple Shah
Tel: (022) 2610 2894 / 95

Ahmedabad (Bapu Nagar) - Milan Kanabar
Tel : (079) 3026 0204 / 0205

Ahmedabad (C. G. Road) - Ritesh Patel
Tel: (079) 4021 4023

Ahmedabad (Gurukul) - Kaivalya Shah
Tel: (079) 6522 5510 / 3012 5492-94

Ahmedabad (Kalupur) - Jicky Thomas
Tel: (079) 3240 7474 / 75

Ahmedabad (Maninagar) - Ashok Kumar
Tel: (079) 3048 0241 / 0242 / 0245

Ahmedabad (Ramdevnagar) - Krunal Pandya
Tel : (079) 2692 6401 / 51

Ahmedabad (Sabarmati) - Kaushik Rathi
Tel : (079) 2692 6401 / 51

Ahmedabad (Satellite) - Rishi Parghi
Tel: (079) 4000 1000

Ahmedabad (Shahibaug) - Chirag Raghvani
Tel: (079) 22861053 / 5 / 6

Amreli - Nishith Hemani
Tel: (02792) 228 800/231039-42

Anand - Alay Brahmbhatt
Tel : (02692) 267 041-45

Ankleshwar - Ankit Mathur
Tel: (02646) 652 681-85

Baroda - Rashmikant Thakar
Tel: (0265) 2226 103-04 / 6624 280

Baroda (Akota) - Jaydeep Shah
Tel: (0265) 2355 258 / 6499 286

Baroda (Manjalpur) - Chirag Patel
Mobile : 098252 27403

Bhavnagar - Apurva Dhami
Tel: (0278) 2512099 / 755 / 3001717 / 18

Bhopal - Sandeep Kothana
Tel :(0755) 3256 663 / 4024 000

Bikaner - Sharad Acharya
Tel :(0151) 2207 148 / 98281 03988

Deesa - Sandip Nayak
Mobile: 98795 19881

Gandhinagar - Vivek Thakker
Tel: (079) 4010 1010 - 31

Gondal - Lenin Trivedi
Tel: (02825) 240 693 / 4

Gurgaon - Pankaj Varma
Tel: (0124) 4218 704

Himatnagar - Sanjay Patel
Tel: (02772) 241 008 / 241346

Indore - Alok Rathi
Tel: (0731) 4042242 / 4044 366 / 4087 966

Jaipur - (Rajapark) Amit Kumar Garg
Tel: (0141) 4000 500, 94143 14448

Jalgaon - Sandeep Mundra
Tel: (0257) 3200 906

Jamnagar - Jwalant Shingala
Tel : (0288) 266 4941-44, 3217 790

Jodhpur - Bharat Purohit
Tel: (0291) 5100- 941 - 948 / 98284 26786

Junagadh - Nimesh Raichura
Tel : (0285) 2622 483 /2622 484

Kota - Sumit Maheshwari
Tel : (0744) 5100 470 / 2365 200

Mehsana - Alipt Doshi
Tel: (02762) 645 291 / 92

Nadiad - Vipul Patel
Tel : (0268) - 2527 230 / 31

Nashik - Nilesh Supekar
Tel: (0253) 6611 201 / 206

New Delhi (Bhikaji Cama Place) - Sumit zBhuttan
Tel: (011) 41659 711/12

New Delhi (Lawrence Rd.) - Sanjeev Kumar
Tel: (011) 3262 8699 / 8799

New Delhi (Pitampura) - Roopal Agarwal
Tel: (011) 4700 2380 / 84

New Delhi (Preet Vihar) -Gulshan Khurana
Tel: (011) 4242 1105 - 07

Noida - Amit Gupta
Tel : (0120) 4639900 / 1 / 9

Palanpur - Paresh Patel
Tel : (02742) 645 171 / 72

Patan - Shikha Saxena
Tel: (02766) 222 306

Patel Nagar - Harpreet Singh
Tel : (011) 45030 600

Porbandar - Ketan Thanki
Tel : (0286) 221 5310 / 31 / 221 5450

Pune - Sameer Amrute/Shraddha Gadekar
Tel : (020) 6620 6591 / 6620 6595

Pune - (Pentagon) Ishwar Magnani
Tel : (020) 6640 8300 / 3052 3220

Rajkot (202 Race Course) Prashant Ukani
Tel : (0281) 2921 568 / 99049 10001

Rajkot (Ardella) Hitesh Rupareliya
Tel : (0281) 2440 266 - 266

Rajkot (University Rd.) - Prashant Ukani
Tel : (0281) 2577408

Rajkot (Bhaktinagar) - Dhaval Dave
Tel : (0281) 236 1935 / 329 6881 / 329 8100

Rajkot (Indira Circle) - Denish Patel
Tel : (0281) 2585 751, 99258 84848

Rajkot (Orbit Plaza) - Hitesh Popat
Tel: (0281) 2463 291-94

Rajkot (Star Chambers) - Manish Baradia
Tel : (0281) 2233 230 / 50

Rajkot (Star Chambers) - Kiran Marthak
Tel : (0281) 2225 401 / 02 / 03

Secunderabad - Srinivas
Tel : (040) 6690 5192 / 3 / 4

Surat (Mahidharpura) - Sameet Kapadia
Tel: 2402 911 - 915

Surat (Parle Point) - Akshay Panwala
Tel : (0261) 2257 990 / 909

Surat (Ring Road) - Piyush Bothra
Tel : (0261) 6696 666

Surendranagar - Prashant Jani
Tel : (02752) 325905 / 223305

Udaipur - Anurag Jain
Tel - 098870 60723 / 099291 04723

Valsad - Vinod Kumbarwadia
Tel - (02632) 645 344 / 45

Vapi - Jalpa Desai
Tel: (0260) 2400 210 / 214 / 236

Varachha - Naimesh Bhavsar
(0261) 2551633 - 39

Vijayawada - Badrinath Majeti
Tel :(0866) 6636900 / 901/ 902 / 903