



Indian Bank

STOCK INFO.	BLOOMBERG
BSE SENSEX: 10,683	INBK IN
	REUTERS CODE
S&P CNX: 3,235	INBA.BO

21 October 2008

Buy

Previous Recommendation: Buy

Rs135

Equity Shares (m)	429.8
52-Week Range	256/78
1,6,12 Rel.Perf.(%)	24/23/39
M.Cap. (Rs b)	58.1
M.Cap. (US\$ b)	1.2

YEAR	NET INCOME	PAT	EPS	EPS	P/E	P/BV	CAR	ROE	ROA	P/ABV
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	(%)	(X)
3/07A	26,052	7,598	17.7	20.5	7.6	1.8	14.1	29.9	1.5	1.8
3/08A	30,596	10,087	23.5	32.8	5.8	1.3	12.9	25.8	1.6	1.3
3/09E	35,205	11,762	27.4	16.6	4.9	1.1	11.4	23.3	1.6	1.1
3/10E	39,322	13,324	31.0	13.3	4.4	0.9	10.3	22.1	1.5	0.9

Indian Bank's 2QFY09 results were higher than our estimates. Reported NII grew 45% YoY (adjusted NII up 42% YoY) v/s our est. of 24% YoY growth. Margins improved sharply during the quarter.

- NIMs improved 66bp QoQ (63bp YoY) to 3.86% in 2QFY09.
- Business growth remains strong with loans growing 49% YoY and 8% QoQ to Rs481b. Deposits grew 20% YoY and 4% QoQ to Rs646b. The bank has reduced its investment book (~Rs20b) during the quarter which also helped to grow the loan book aggressively.
- The bank shed Rs2.6b of bulk deposits and reduced its share to 10.3% (11.2% in 1QFY09).
- Other income (ex-trading profits and recoveries) grew 24% YoY to Rs1.6b.
- Asset quality continues to remain strong with the GNPA ratio below 1% and provision coverage ratio of 82%. The bank has comfortable CAR of 11.27% (tier I at 10.1%).

Maintain Buy: We like the bank's strategy of relying on core retail deposits to grow its loan book in this uncertain environment. We expect EPS of Rs27.4 in FY09 and BV of Rs128. RoE and RoA would be 23% and 1.6% in FY09. The stock trades at 1.1x FY09E BV and 4.9x FY09E EPS. On FY10 estimates, the stock trades at 0.9x BV and 4.4x EPS. **Maintain Buy.**

Y/E MARCH	QUARTERLY PERFORMANCE										(RS MILLION)	
	FY08				FY09				FY08	FY09E		
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE				
Interest Income	11,952	12,574	13,754	13,600	15,018	16,882	17,726	18,182	51,508	67,807		
Interest Expense	7,124	7,862	8,137	8,468	9,623	10,063	10,868	11,322	31,591	41,877		
Net Interest Income	4,828	4,712	5,617	5,132	5,395	6,818	6,857	6,860	19,917	25,931		
% Change (Y-o-Y)	24.8	9.1	35.7	-6.7	11.7	44.7	22.1	33.7	11.8	30.2		
Other Income	1,815	2,357	3,006	3,129	2,432	2,128	2,287	2,427	10,679	9,274		
Net Income	6,644	7,069	8,623	8,261	7,827	8,946	9,145	9,286	30,596	35,205		
Operating Expenses	3,346	3,635	3,991	3,031	3,461	3,618	3,708	3,735	14,003	14,522		
Operating Profit	3,297	3,434	4,632	5,230	4,366	5,328	5,436	5,552	16,593	20,682		
% Change (Y-o-Y)	43.7	15.5	59.6	-3.4	32.4	55.1	17.4	6.2	17.4	15.1		
Other Provisions	907	497	1,057	1,782	1,690	1,089	800	1,420	4,243	4,999		
Profit before Tax	2,390	2,937	3,575	3,448	2,676	4,239	4,636	4,132	12,350	15,683		
Tax Provisions	270	461	500	1,031	500	1,409	1,113	899	2,262	3,921		
Net Profit	2,120	2,476	3,075	2,417	2,176	2,829	3,523	3,233	10,087	11,762		
% Change (Y-o-Y)	28.7	46.4	61.4	2.7	2.6	14.3	14.6	33.8	32.8	16.6		
Interest Expense/Interest Income (%)	59.6	62.5	59.2	62.3	64.1	59.6	61.3	62.3	61.3	61.8		
Other Income/Net Income (%)	27.3	33.3	34.9	37.9	31.1	23.8	25.0	26.1	34.9	26.3		
Cost to Income Ratio (%)	50.4	51.4	46.3	36.7	44.2	40.4	40.6	40.2	45.8	41.3		
Provisions/Operating Profits (%)	27.5	14.5	22.8	34.1	38.7	20.4	14.7	25.6	25.6	24.2		
Tax Rate (%)	11.3	15.7	14.0	29.9	18.7	33.3	24.0	21.7	18.3	25.0		

E: MSt Estimates

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RESULTS ANALYSIS (RS M)

	2QFY09	2QFY08	YOY GR. %	1QFY09	QOQ GR. %	FY07	FY08	FY09E
Interest Income	16,882	12,574	34	15,018	12	41,948	51,508	67,807
Interest Expense	10,063	7,862	28	9,623	5	24,126	31,591	41,877
Net Interest Income (NII)	6,818	4,712	45	5,395	26	17,822	19,917	25,931
Other Income	2,128	2,357	(10)	2,432	(13)	8,231	10,679	9,274
- Fees and others	1,561	1,263	24	1,653	(6)	3,963	5,138	6,524
- Trading Profits	30	603	(95)	244	(88)	493	2,412	750
- Recovery from w/off	537	491	9	535	0	3,774	3,129	2,000
Net Income	8,946	7,069	27	7,827	14	26,052	30,596	35,205
Total Operating Costs	3,618	3,635	(0)	3,461	5	12,467	14,003	14,522
- Staff Costs	2,475	2,520	(2)	2,478	(0)	8,787	9,674	10,053
- Other Opex	1,143	1,115	3	983	16	3,680	4,329	4,470
Operating Profit	5,328	3,434	55	4,366	22	13,586	16,593	20,682
Provisions	1,089	497	119	1,690	(36)	4,744	4,243	4,999
PBT	4,239	2,937	44	2,676	58	8,842	12,350	15,683
Tax	1,409	461	205	500	182	1,244	2,262	3,921
Tax rate %	33	16		19		14	18	25
PAT	2,829	2,476	14	2,176	30	7,598	10,087	11,762
Deposits	646,140	537,470	20	622,150	4	470,909	610,459	695,924
CASA Ratio %	33	34		34		35	32	33
Advances	480,920	322,070	49	444,760	8	290,581	398,387	505,952
Gross NPA %	1.0	1.6		1.0		1.9	1.2	1.4
Net NPA %	0.2	0.3		0.2		0.4	0.2	0.5
Yields on Advances %*	10.8	10.0		9.7		9.9	10.2	11.3
NIM %**	3.9	3.2		3.2		3.5	3.2	3.6
Tier I CAR %	10.1	12.3		10.6		12.3	11.4	10.3
Tier II CAR %	1.2	1.6		1.3		1.9	1.5	1.5
Branches	1,575	1,488		1,553		1,443	1,541	1,625

* Calculated, ** Reported

Highlights

Strong growth in net interest income: Reported NII grew 45% YoY (v/s our est. of 24%) and 26% QoQ to Rs6.8b. Adjusted for interest on recoveries NII grew 42% YoY and 22% QoQ to Rs6.3b. Interest income arising from recoveries of the written-off accounts was Rs489m (v/s Rs210m in 1QFY09 and Rs246m in 2QFY08). Strong growth in NII came on the back of the 63bp YoY improvement in NIMs and 49% YoY growth in loans.

ADJUSTED NII (RS M)

	2Q	2Q	% CHG.	1Q	%CHG.	1H	1H	%
	FY09	FY08	(YOY)	FY09	(QOQ)	FY09	FY08	CHG.
Interest Income	16,882	12,574	34.3	15,018	12.4	31,899	24,526	30.1
Interest Expenses	10,063	7,862	28.0	9,623	4.6	19,686	14,986	31.4
Reported NII	6,818	4,712	44.7	5,395	26.4	12,214	9,540	28.0
Less: Rec. of Int. on NPA	489	246	99.3	210	133.3	699	466	50.1
Adjusted NII	6,329	4,466	41.7	5,186	22.1	11,515	9,075	26.9

Source: Company/MOSL

Margins improved sharply in 2QFY09: During 2QFY09, margins improved by 63bp YoY and 66bp QoQ to 3.86% on back of the strong growth in loans and increase in PLR. The bank increased its lending rates by 75bp from 1 July 2008 and by 75bp from August 2008. A large part of the growth in loans arrived in June 2008 and 2QFY09. Significant growth in loans in last four months and increase in PLR by 150bp drove substantial growth in interest income (60% YoY). Yield on loans improved 96bp QoQ and 121bp YoY to 11.5% while cost of deposits increased 15bp YoY (fell 14bp QoQ to 6.1%). In 1HFY09, deposits increased by Rs36b and loans by Rs83b. The bank had built up significant liquidity in 4QFY08 when the C-D ratio was 65%. This has now increased to 74%. The bank also reduced its low-yielding investment book by ~Rs20b to fund high-yielding loans. Incremental C-D ratio of 200%+ in 1HFY09 also helped the bank improve margins.

Business growth remains strong: The bank posted 47% YoY (8% QoQ) growth in loans to Rs481b and deposits increased 20% YoY (4% QoQ) to Rs646b. A large part of the growth in deposits came from growth in core deposits. The bank's core deposits grew 11% YTD v/s 6% YTD growth in overall deposits. The bank shed ~Rs20b of bulk deposits YTD (~Rs2.6b QoQ) in 1HFY09. The share of bulk deposits fell from 14.3% in FY08 to 11.2% in 1QFY09 and 10.3% in 1HFY09.

Indian Bank has the lowest share of bulk deposits in the system and management intends to maintain this state in the current environment. CASA ratio has decreased from 34% in 2QFY08 to 33% in 2QFY09 (down from 33.8% in 1QFY09). Management stated that it would slow down credit in the second half and growth rates would moderate going forward. The management is targeting deposit growth of 14% and loan growth of 25% in FY09.

Operating profits higher v/s est. backed by strong core operating performance: The fee income (non-interest income excluding recoveries and gains) grew 24% to Rs1.56b. Despite the strong growth in fee based income, other income fell by 10% YoY to Rs2.2b, largely due to lower trading profits. Treasury gains declined from Rs603m in 2QFY08 to 30m. Recovery from written-off accounts was Rs537m in 2QFY09 v/s Rs491m in 2QFY08 and Rs535m in 1QFY09. Operating expenses remained almost flat YoY. Employee cost fell 2% YoY, as the bank had accounted for transitional liability for AS 15 of 1HFY08 in 2QFY08 itself. Cost to income ratio fell from 51.4% in 2QFY08 to 40.4% in 2QFY09

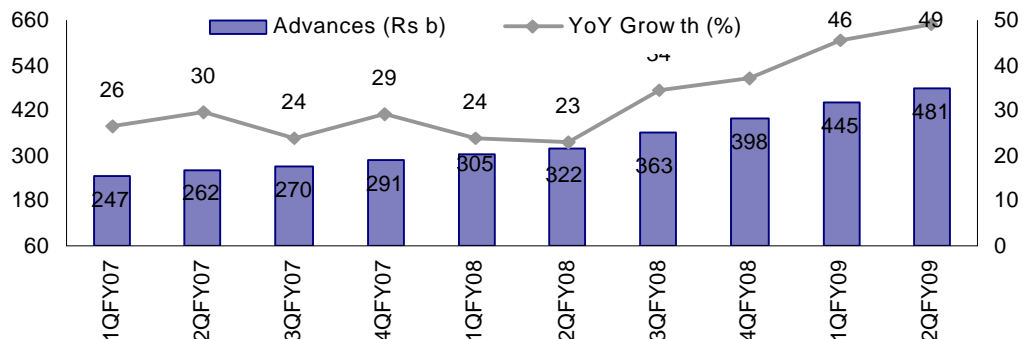
Increased provisioning expenses in the quarter: Provisions were high at Rs1.08b v/s our est. of Rs800m. Management has stated that it had accounted Rs450m in respect of the likely wage increase in FY09. Management expects a one-time impact of Rs1b for the wage increase shortfall. On the back of the strong growth in loan book, management provided Rs400m for standard assets. The tax rate has also increased from 19% in 1QFY09 and 16% in 2QFY08 to 33% in 2QFY09.

Asset quality remains strong with GNPA below 1%; provisions coverage ratio 80%+: Gross NPA ratio and net NPA ratios are one of the lowest in the industry at 0.98% (up 3bp QoQ and down 60bp YoY) and 0.18% (up 1bp QoQ and down 9bp QoQ) respectively in September 2008. Provision coverage ratio remains stable QoQ and YoY at ~82%. In absolute terms, GNPA grew 12% QoQ (down 8% YoY) and NNPA grew 13% QoQ (down 2% YoY). Management stated that this was on account of a couple of corporates (real estate) wherein payments were delayed, and expects recoveries/upgradation of these accounts in 3QFY09. The bank had already accounted for the farm loan waiver package in 1QFY09.

Maintain Buy: We like the bank's strategy of relying on core deposits to grow its loan book in this current uncertain environment. We expect EPS to be Rs27 in FY09 and BV at Rs128. We expect RoE and RoA to be 23% and 1.6% in FY09. The stock is trading at 1.1x FY09E BV and 4.9x FY09E EPS. On FY10 estimates, the stock is trading at 0.9x book value and 4.4x EPS. **Maintain Buy.**

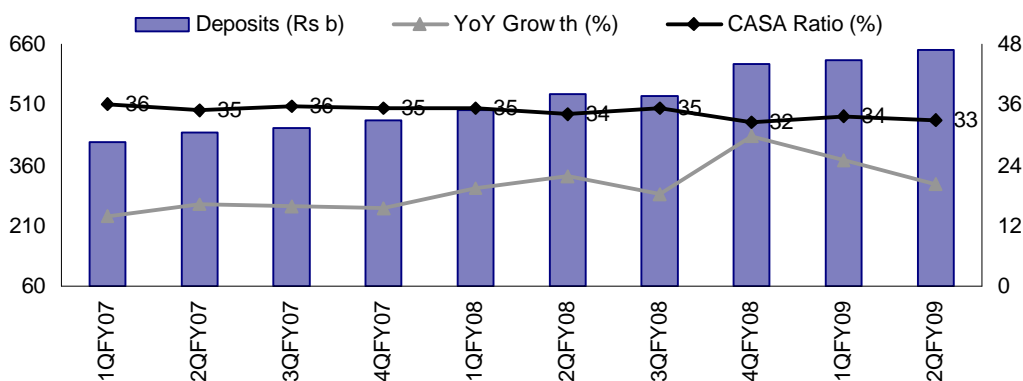
GROWTH IN ADVANCES REMAINS STRONG

QoQ loans increased by 8%; higher than industry



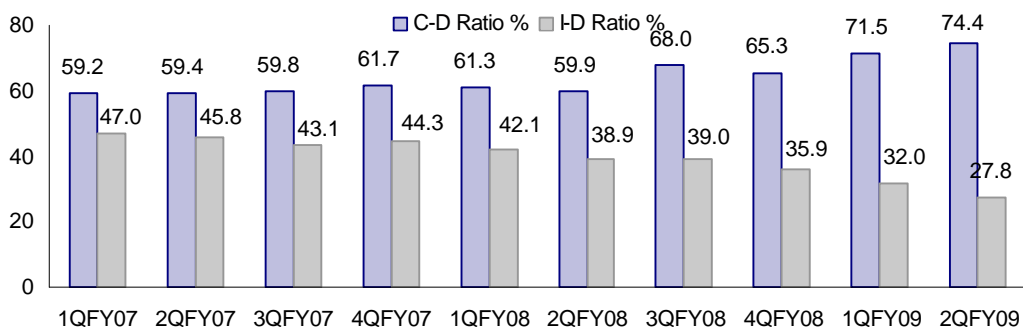
DEPOSITS GREW 20% YOY, CASA RATIO FELL 80BP QOQ

Higher reliance on core deposits; bulk deposit share reduces to 10%



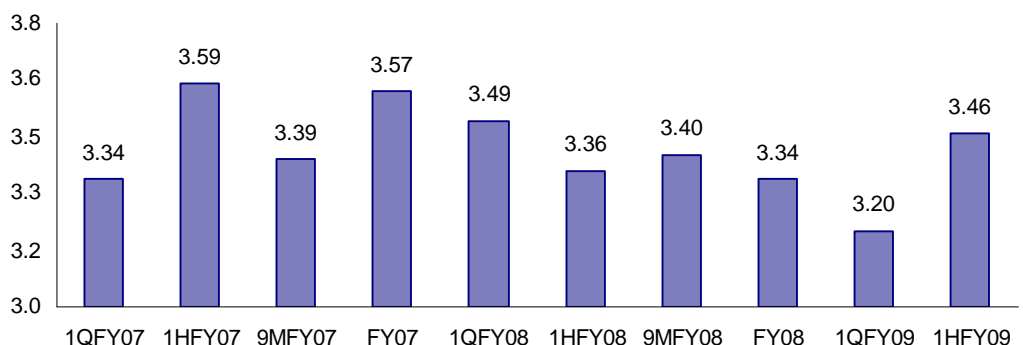
C-D RATIO INCREASED TO 74% FROM 65% IN FY08

Strong build-up of liquidity in 4QFY08 and robust loan growth (partially funded by reduction in investment book) led to incremental C-D ratio of 200%+



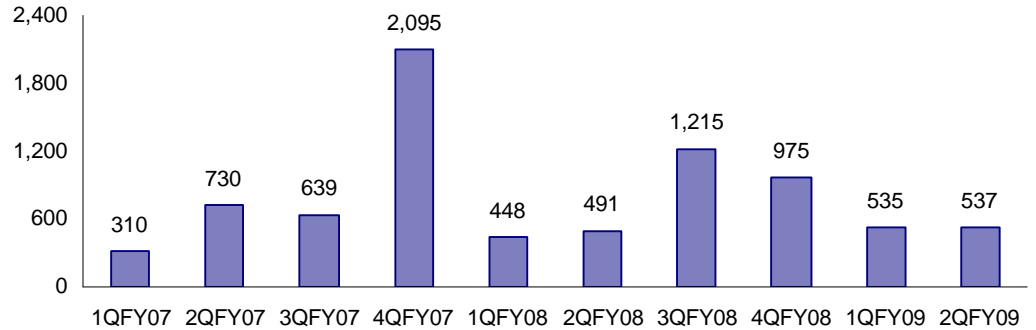
SIGNIFICANT IMPROVEMENT IN MARGINS

Rise in PLR by 150bp, incremental CD ratio of 200%+ led to margin improvement



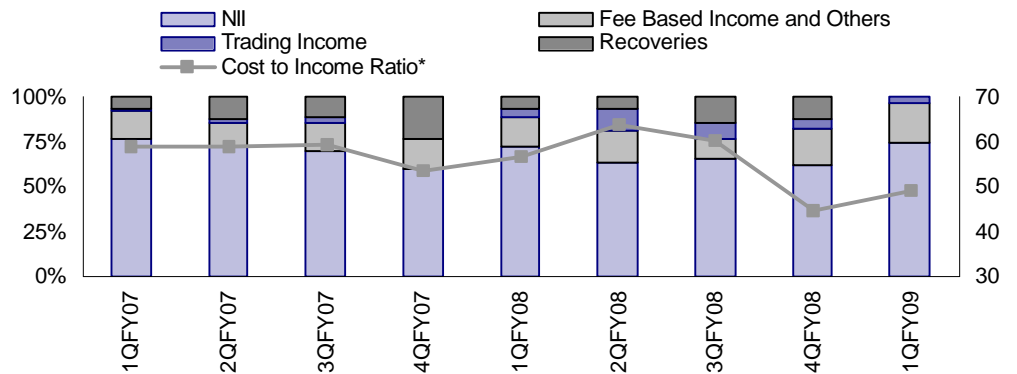
Source: Company/Motilal Oswal Securities

RECOVERIES FROM W/OFF ACCOUNTS SLOW DOWN IN THE LAST 2 QUARTERS

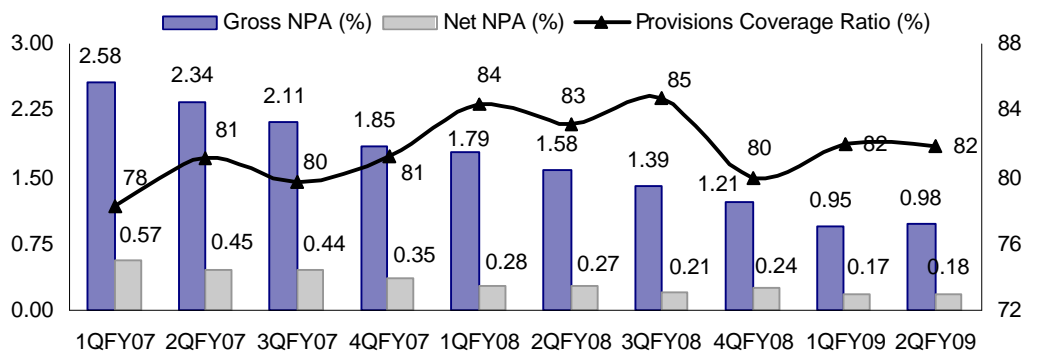


CORE OPERATING INCOME FORMS A HIGHER SHARE OF OPERATING INCOME

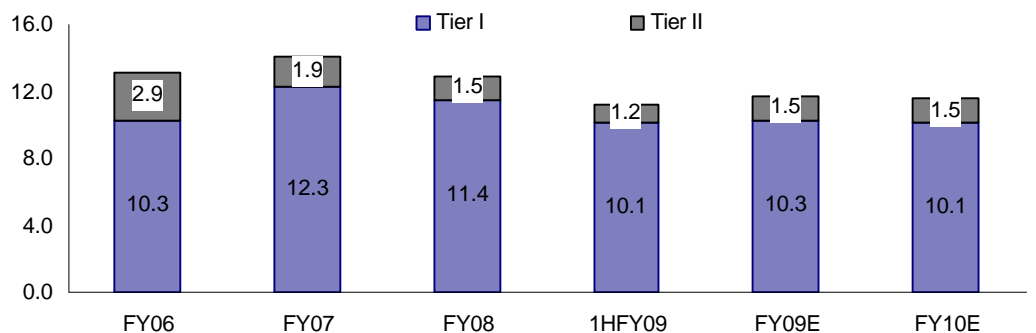
Strong growth in operating income and contained cost of operations lead to lower C-I ratio



ASSET QUALITY IS ONE OF THE BEST IN INDUSTRY



STRONG CAPITAL BASE TO SUPPORT GROWTH



Source: Company/Motilal Oswal Securities

Indian Bank: an investment profile

Company description

The bank commenced operations in 1907 and was nationalized in 1969. Indian Bank experienced some financial setbacks in the 1990s following the introduction of prudential norms by the RBI. It incurred losses in FY94 and between FY96-01. In March 2006, the bank reduced its share capital by writing off accumulated losses of Rs38.3b. This reduced its paid-up share capital from Rs45.7b to Rs7.4b. On 30 September 2006, the bank restructured its entire paid-up capital of Rs7.4b held by the GoI into perpetual non-cumulative preference share capital of Rs4b and equity share capital of Rs3.4b. To give effect to this restructuring, the bank issued 343.8m equity shares of Rs10 each to the GoI, without payment by the promoter. The bank has a pan-India network of 1,575 branches and 600+ ATMs with a strong presence in southern India, particularly Tamil Nadu.

Key investment arguments

- ✍ Strong CASA franchise and lower dependence on bulk deposits would keep cost of funds under control and margins higher than peers
- ✍ Asset quality is one of the best with gross NPAs at 1% and net NPA at mere 0.2%.
- ✍ We expect RoA and RoE to remain higher than industry standards at 1.5%+ and 20%+ for next couple of years.

COMPARATIVE VALUATIONS

		INDIAN BANK	IOB	BOI
P/E (x)	FY09E	4.9	3.6	6.1
	FY10E	4.4	3.2	5.3
P/BV (x)	FY09E	1.1	0.8	1.4
	FY10E	0.9	0.7	1.1
RoE (%)	FY09E	23.3	24.7	24.5
	FY10E	22.1	23.4	23.4
RoA (%)	FY09E	1.6	1.2	1.2
	FY10E	1.5	1.1	1.2

SHAREHOLDING PATTERN (%)

	SEP-08	JUN-08	SEP-07
Promoter	80.0	80.0	80.0
Domestic Inst	2.1	2.2	2.3
Foreign	13.6	13.8	14.0
Others	4.2	4.0	3.7

Key investment risks

- ✍ Lower recoveries from written off NPAs would lead to lower earnings growth
- ✍ Strong growth in loan book in past couple of quarters can lead to deterioration in asset quality in future

Recent developments

- ✍ Nil

Valuation and view

- ✍ We expect earnings to grow by 17% in FY09 and 13% in FY10. The stock is trading at 4.9x FY09E EPS of Rs27 and 1.1x FY09E book value of Rs128.
- ✍ We maintain a **Buy** rating on the stock.

Sector view

- ✍ YTD loan growth of 25% and deposit growth of 20%
- ✍ Concerns on macro economic factors like rising inflation, higher interest rates, slowing economic growth remain concerns in mid term
- ✍ Selective buying with favor for banks with higher earnings visibility from core operations.

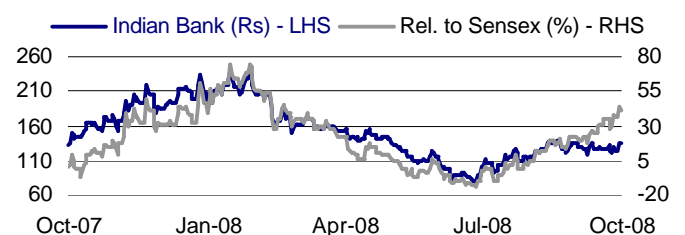
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY09	27.4	21.9	24.8
FY10	31.0	26.0	19.4

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
135	198	46.4	Buy

STOCK PERFORMANCE



INCOME STATEMENT						(Rs M Million)
Y/E MARCH	2006	2007	2008	2009E	2010E	
Interest Income	33,645	41,948	51,508	67,807	80,474	
Interest Expended	18,543	24,126	31,591	41,877	51,347	
Net Interest Income	15,102	17,822	19,917	25,931	29,127	
Change (%)	15.8	18.0	11.8	30.2	12.3	
Other Income	4,632	8,231	10,679	9,274	10,195	
- Recovery from written off acc.	1,815	3,774	3,129	2,000	1,800	
- Profit on sale on investments	759	493	2,412	750	900	
- Others	2,058	3,963	5,138	6,524	7,495	
Net Income	19,734	26,052	30,596	35,205	39,322	
Change (%)	5.4	32.0	17.4	15.1	11.7	
Operating Expenses	10,798	12,467	14,003	14,522	16,461	
- Staff Cost	7,886	8,787	9,674	10,053	11,592	
Operating Income	8,937	13,586	16,593	20,682	22,861	
Change (%)	-6.7	52.0	22.1	24.6	10.5	
Other Provisions	3,330	4,744	4,243	4,999	4,609	
P B T	5,607	8,842	12,350	15,683	18,251	
Tax	562	1,244	2,262	3,921	4,928	
Tax Rate (%)	10.0	14.1	18.3	25.0	27.0	
P A T	5,045	7,598	10,087	11,762	13,324	
Change (%)	23.5	50.6	32.8	16.6	13.3	
Proposed Dividend	2,529	1,289	1,918	2,634	2,855	

BALANCE SHEET						(Rs M Million)
Y/E MARCH	2006	2007	2008	2009E	2010E	
Capital	7,438	8,298	8,298	8,298	8,298	
- Equity Share Capital	7,438	4,298	4,298	4,298	4,298	
- Preference Share Capital	0	4,000	4,000	4,000	4,000	
Reserves & Surplus	17,476	30,110	43,810	52,896	63,323	
Net Worth	24,914	38,408	52,108	61,194	71,620	
Deposits	408,055	470,909	610,459	695,924	821,190	
Change (%)	17.2	15.4	29.6	14.0	18.0	
Borrowings	18,873	19,365	12,832	11,549	11,549	
Other Liabilities & Prov.	24,511	32,805	29,677	29,677	29,677	
Total Liabilities	476,353	561,486	705,077	798,344	934,037	
Current Assets	48,074	48,178	67,728	69,579	67,189	
Investments	190,170	208,777	219,151	197,236	221,890	
Change (%)	6.1	9.8	5.0	-10.0	12.5	
Advances	224,846	290,581	398,387	505,952	617,261	
Change (%)	22.3	29.2	37.1	27.0	22.0	
Net Fixed Assets	5,187	5,512	5,393	5,393	5,493	
Other Assets	8,075	8,439	14,418	20,185	22,204	
Total Assets	476,353	561,486	705,077	798,344	934,037	

ASSUMPTIONS	(%)				
Deposit Growth	17.2	15.4	29.6	14.0	18.0
Advances Growth	22.3	29.2	37.1	27.0	22.0
Investments Growth	6.1	9.8	5.0	-10.0	12.5
Provisions Coverage	73.6	81.3	80.0	64.5	47.1
Dividend	34.0	30.0	40.0	44.0	48.4

E: M OSt Estimates

RATIOS

Y/E MARCH	2006	2007	2008	2009E	2010E
Spreads Analysis (%)					
Avg. Yield-Earn. Assets	7.9	8.3	8.4	9.4	9.7
Avg. Cost-Int. Bear. Liab.	4.7	5.3	5.7	6.3	6.7
Interest Spread	3.2	3.1	2.7	3.1	3.0
Net Interest Margin	3.6	3.5	3.2	3.6	3.5

Profitability Ratios (%)

RoE	30.0	29.9	25.8	23.3	22.1
RoA	1.1	1.5	1.6	1.6	1.5
Int. Expended/Int. Earned	55.1	57.5	61.3	61.8	63.8
Other Inc./Net Income	23.5	31.6	34.9	26.3	25.9

Efficiency Ratios (%)

Op. Exps./Net Income	62.9	57.2	55.9	44.7	44.9
Empl. Cost/Op. Exps.	73.0	70.5	69.1	69.2	70.4
Busi. per Empl. (Rs m)	27.2	33.4	43.3	54.0	61.4
NP per Empl. (Rs lac)	2.4	3.6	4.9	5.7	6.2

*ex treasury and recovery from w/off accounts

Asset-Liability Profile (%)

Adv./Deposit Ratio	55.1	61.7	65.3	72.7	75.2
CASA Ratio	34.8	35.4	32.3	32.5	32.5
Invest./Deposit Ratio	46.6	44.3	35.9	28.3	27.0
G-Sec/Invest. Ratio	85.9	79.9	81.7	95.3	96.2
Gross NPAs to Adv. (%)	2.9	1.9	1.2	1.4	1.5
Net NPAs to Adv. (%)	0.8	0.4	0.2	0.5	0.8
CAR	13.2	14.1	12.9	11.8	11.6
Tier 1	10.3	12.3	11.4	10.3	10.1

VALUATION

Book Value (Rs)	54.3	75.0	106.9	128.2	152.5
Price-BV (x)	2.5	1.8	1.3	1.1	0.9
Adjusted BV (Rs)	52.8	74.2	106.2	126.2	148.6
Price-ABV (x)	2.6	1.8	1.3	1.1	0.9
EPS (Rs)	14.7	17.7	23.5	27.4	31.0
EPS Growth (%)	23.5	20.5	32.8	16.6	13.3
Price-Earnings (x)	9.2	7.6	5.8	4.9	4.4
OPS (Rs)	12.0	31.6	38.6	48.1	53.2
OPS Growth (%)	473.6	163.1	22.1	24.6	10.5
Price-OP (x)	0.0	0.0	0.0	0.0	0.0

E: Most Estimates



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Disclosure of Interest Statement

Indian Bank

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
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