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IDFC SSKI

INDIA RESEARCH

ING Vysya Bank

Rs292
OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs29.9bn; US$645mn

Analyst:	**Pathik Gandotra (91-22-6638 3304; pathik@idfcsski.com)**
	Neha Agrawal (91-22-6638 3237; neha@idfcsski.com)
	Chinmaya Garg (91-22-6638 3325; chinmaya@idfcsski.com)

Result:	**Q2FY10**
Comment:	**Margins expand; asset quality a key monitorable!**
Revision:	**Lowering FY10 earning estimates by 2%**

Key valuation metrics

Year to March 31 (Rs m)	NII	yoy chg (%)	Net profit	yoy chg (%)	EPS (Rs)	Adj. Bk Val (Rs/ share)	P/ Adj.Bk (x)	PER (x)	RoE (%)
FY07	4,456	2.4	889	886.6	9.8	95.9	3.0	29.9	9.4
FY08	4,984	11.9	1,569	76.6	15.3	126.2	2.3	19.1	13.0
FY09	6,496	30.3	1,888	20.3	18.4	137.2	2.1	15.9	12.5
FY10E	7,731	19.0	2,400	27.1	20.1	176.0	1.7	14.5	12.6
FY11E	9,530	23.3	3,050	27.1	25.6	201.8	1.4	11.4	12.9

HIGHLIGHTS OF Q2FY10 RESULTS

ING Vysya Bank ('VYSB') delivered net profit growth of Rs535mn (as against our estimate of Rs583mn), a growth of ~14% yoy. The underperformance was primarily attributable to higher provisions (of which ~34% were on account of one large restructured account).

- Robust NII growth; as margins expand: NII came in at Rs1.9bn, a ~22% yoy and ~11% qoq increase, ahead of our estimates, owing to strong expansion in margins. NIMs improved by 25bp qoq to 3.1% buoyed by (i) declining cost of funds as high-cost deposits re-priced at lower rates; (ii) CASA evidenced an uptick; and (iii) benefit of capital raised. (Exhibit 1 & 2)
- Gross NPAs rise; 0.9% of incremental restructurings: Gross and Net NPAs increased by 50-55bp qoq to 2.57% and 1.78% respectively. In absolute terms, Gross NPAs rose by Rs1bn qoq. Consequently, provision coverage declined by over ~600bp qoq to 31.5%. VYSB continues to hold excess general provisions of ~Rs400mn. In Q2FY10, 0.9% of outstanding advances (Rs1.5bn) were restructured. Since Mar '09, cumulative restructured assets stood at ~Rs3.1bn, amounting to 1.9% of net advances. (Exhibit 6)
- Higher provisions dampen bottom-line: VYSB made Rs626mn of total provisions, of which Rs210mn pertain to one large restructured account (~20% of loan amount). The higher than expected provisions in turn dampened bottom-line growth.
- Loan growth muted, CD ratio improves: Loan book growth was muted at ~3% yoy and 1.5% qoq to ~Rs164bn. Concurrently, deposit growth was also at a calibrated pace of ~8% yoy (a marginal de-growth qoq) leading to a 140bp qoq rise in CD ratio. Loan mix remained stable sequentially with retail comprising ~58% of total book, the balance being wholesale. The bank's personal loan book remains small at ~Rs3bn, ~2% of total loan book as of Sept '09. (Exhibit 2 & 5)

- Fee income holds up: Other income grew by ~23% yoy to Rs1.52bn, contributing ~44% of net revenues. During the quarter, the bank booked profit on sale of investments of ~Rs220mn (~15% of operating profit).Non-trading income held up at Rs1.3bn (up by ~9% yoy), driven by higher recoveries of Rs130mn (Rs80mn in Q2FY09) and ~33% yoy growth in wealth management fees. Derivates & forex fees was lower sequentially(Exhibit 4)
- Operating leverage continues to accrue: Expenses increased by ~6% yoy to ~Rs2bn, with non-employee expenses remaining flat yoy. Employee expenses were seen to increase at a higher pace of ~12% yoy due to higher provision for employee benefits. Consequently, while cost ratios have shown a significant decline on a yoy basis, there was some uptrend qoq. Cost to income ratio has declined by ~240bp over Mar '09 levels to ~58% in Q2FY10.
- Uptick in CASA...as deposits de-grow; saving balances rise: CASA improved by ~230bp qoq to 31.1% as term deposit de-grew by 6% qoq. In Q2FY10, year-end current account flows/ short-term deposits led to reported CASA being elevated at 32.7%. Saving deposits increased by 5.5% qoq. (Exhibit 3)

VALUATIONS & VIEW

In Q2FY10, ING Vysya Bank reported NII performance ahead of our estimates, whilst bottom-line was dampened by higher provisions on one large corporate account. Key operating metrics demonstrated an encouraging trend sequentially with NIMs up 25bp and CASA up 230bp. However, the bank's asset quality remains a key monitorable as NPLs rose by ~55bp qoq and provision coverage slipped by ~600bp qoq to 31.5%. Going forward we see an improving ROA trend on the back of improving margins (buoyed by an increasing CASA share), accelerated credit growth (after a muted Q2FY10), strategic focus on cross-selling fee based products as well as growing retail loan book. However, we are building in conservative level of NPA provisions and lower asset growth, thereby lowering our FY10 earning estimates by 2%. A strong management team and continued parent support further reinforce our view. We expect a 27% CAGR in the bank's earnings over FY09-11E (also buoyed by operating leverage), with RoA rising to ~0.8% by FY11. Stock is currently trading at 1.4x FY11E adjusted book. Reiterate Outperformer with a 12-month price target of Rs360 (~1.8x FY11E adjusted book).

Quarterly results

Rs m	Q2FY09	Q3FY09	Q4FY09	Q1FY10	Q2FY10	FY09	FY10E	FY11E	Comments
Interest income	**5,316**	**6,202**	**6,097**	**5,831**	**5,389**	**22,399**	**23,576**	**29,150**	
Interest expense	3,751	4,475	4,473	4,112	3,475	15,903	15,845	19,620	
Net Interest income	1,566	1,727	1,624	1,719	1,914	6,496	7,731	9,530	Ahead of estimates as NIMs expand 25bp qoq; volumes remain muted
yoy growth (%)	*43.5*	*19.2*	*15.6*	*8.8*	*22.2*	*30.3*	*19.0*	*23.3*	
Non-interest income	1,236	1,491	1,471	1,597	1,516	5,477	6,501	7,332	Rs220mn of trading gains; Rs45mn last year
Fee income	1,191	1,391	1,331	1,347	1,296	5,177	5,901	7,082	Driven by higher wealth mgmt fees & recoveries
Net revenue	2,801	3,218	3,095	3,316	3,430	11,973	14,232	16,862	
Operating expenses	1,885	2,153	1,874	1,894	1,994	7,725	8,373	9,547	Employee expenses appear relatively higher due to yoy rise in retirement benefits. Other expenses flat yoy
Operating profit	**916**	**1,065**	**1,221**	**1,422**	**1,436**	**4,248**	**5,860**	**7,314**	
Provisions	216	216	455	487	626	1,302	2,168	2,622	Rs210mn pertains to one large restructured account; excess general provisions of Rs400mn
PBT	**700**	**849**	**766**	**935**	**810**	**2,947**	**3,692**	**4,692**	
Tax	230	329	274	332	275	1,059	1,292	1,642	
PAT	**470**	**520**	**491**	**603**	**535**	**1,888**	**2,400**	**3,050**	Lower than estimates due to higher provisions
yoy growth (%)	*2.2*	*21.8*	*14.6*	*48.3*	*13.8*	*20*	*27*	*27*	
Ratios (%)									
NIMs - reported	2.9	2.9	2.8	2.9	3.1				Buoyed by lower cost of funds, float from capital raised, and uptick in CASA
NIMs – calc*	2.4	2.5	2.1	2.2	2.6	2.3	2.3	2.4	
Non fund rev/Avg assets	1.9	2.1	1.9	2.1	2.0	1.9	1.9	1.9	
Prov/avg assets	0.3	0.5	0.6	0.6	0.8	0.5	0.6	0.7	Remains a key monitorable
Op Exp / Avg assets	2.9	3.1	2.5	2.5	2.7	2.7	2.5	2.4	
Cost/Net revenue	67.3	66.9	60.6	57.1	58.1	64.5	58.8	56.6	Operating leverage accrues over the year
RoA	0.7	0.7	0.6	0.8	0.7	0.7	0.7	0.8	
Tax/PBT	32.9	38.7	35.8	35.5	34.0	35.9	35.0	35.0	
CRAR	10.5	10.7	11.7	12.2	14.5				
Tier-I CRAR	6.7	7.0	6.9	7.4	9.7				Rs4.15bn of capital raised through QIP and preferential allotment
CD ratio	75.9	71.5	67.3	71.4	72.8				As term deposits retired (down ~6% qoq), CD ratio improves despite muted credit growth
Balance Sheet (Rs bn)									
Advances	158.7	160.1	167.5	161.5	163.8				Credit growth muted at 1.5% qoq reflecting the environment and cautious stance given rising NPLs
yoy growth (%)	*26.3*	*19.4*	*14.3*	*11.9*	*3.3*				
Deposit	209.0	224.0	248.9	226.1	225.0				flat qoq driven by ~6% de-growth in term deposits; Current up ~22% and Savings up by 5.5% qoq
yoy growth (%)	*22.7*	*25.4*	*21.4*	*10.9*	*7.7*				

** On average quarterly balances*

Exhibit 1: Margins expand...

%	Q2FY09	Q1FY10	Q2FY10	yoy chg	qoq chg
Calculated*					
Yield on advances	11.07	10.90	10.24	(0.83)	(0.66)
Yield on investments	6.71	5.47	5.38	(1.33)	(0.09)
Blended yield	9.78	8.88	8.52	(1.27)	(0.36)
Cost of funds	6.73	6.36	5.64	(1.09)	(0.72)
Loan spreads	4.33	4.54	4.60	0.26	0.06
Spreads	3.05	2.52	2.87	(0.18)	0.36
NIMs	2.37	2.24	2.58	0.20	0.34
Reported					
Yield on advances	11.17	11.26	10.51	(0.66)	(0.75)
Cost of deposits	6.67	6.35	5.47	(1.20)	(0.88)
Spreads	4.50	4.91	5.04	0.54	0.13
NIMs	2.87	2.85	3.10	0.23	0.25

- Deposit re-pricing, higher CASA and capital raised in Q2 lead to lower funding costs
- Yields come-off as asset re-price at lower rates

Exhibit 2: ...CD ratio improves

Rs bn	Q2FY09	Q1FY10	Q2FY10	Incr qoq	yoy gwth (% / bps)	qoq gwth (%/bps)
Advances	158.7	161.5	163.8	2.3	3.3	1.5
Deposits	209.0	226.1	225.0	(1.1)	7.7	(0.5)
CD ratio (%)	75.9	71.4	72.8	1.4	(309.4)	(140.0)

- Credit growth muted reflecting the challenging macro-economic environment and management's cautious strategy
- Deposits also grown at a calibrated pace, with 6% qoq decline in term deposits. Consequently, CD ratio increases by 140bp qoq

** Calculated on average quarterly balances; # yoy and qoq change in basis points*

Exhibit 3: Uptick in CASA

Rs bn	Q2FY09	Q1FY10	Q2FY10	Incr Qoq	yoy gth (% / bps)	qoq gth (% / bps)
Savings Deposits	31.4	35.1	37.1	1.9	18.2	5.5
Current Deposits	29.4	29.9	36.4	6.5	23.7	21.9
Term Deposits	148.2	161.1	151.5	-9.6	2.2	-6.0
Deposits	**209.0**	**226.1**	**225.0**	**-1.1**	**7.7**	**-0.5**
CASA ratio (%)*	29.1	28.8	32.7	3.9	357.92	391.45
CASA deposits	60.8	65.0	73.5	8.5	20.9	13.0

- Adjusted for quarter-end flows, CASA improved by 230bp qoq in Q2FY10 to 31.1%
- Saving deposits grew 5.5% qoq, term deposits down by 6% qoq

** Adjusted for quarter-end current account flows, stands at 31.1% as of Sept '09*

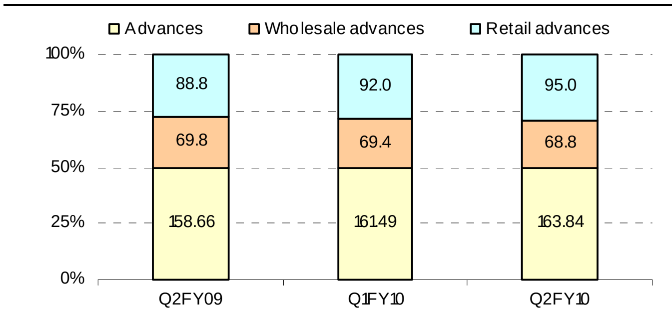
Exhibit 4: Fee income break-up (Rs mn)

Rs mn	Q2FY09	Q1FY10	Q2FY10	yoy gth (%)	qoq gwth (%)
Trade & CMS	220	210	200	(9.1)	(4.8)
Derivatives & Forex	175	260	180	2.9	(30.8)
Asset processing	245	150	230	(6.1)	53.3
Wealth management	150	110	200	33.3	81.8
Profit on sale of investments	45	250	220	388.9	(12.0)
Other income (liabilities & remittances)*	321	537	240	(25.2)	(55.3)
Recoveries & Misc	80	80	246	207.4	207.4
Non-trading income	**1,191**	**1,347**	**1,296**	**8.8**	**(3.8)**
Total non-fund income	**1,236**	**1,597**	**1,516**	**22.7**	**(5.1)**

- Non-trading income contributes ~44% of net revenue
- Growth buoyed by wealth management fees, higher recoveries and trading gains

** balancing figure*

Exhibit 5: Loan book composition stable (Rs bn)



- Loan mix stable qoq with retail comprising ~58% of total book
- ~3.3% yoy growth in advances, led by 7% yoy growth in retail book

Exhibit 6: Gross NPAs inch-up; coverage declines

	Q2FY09	Q1FY10	Q2FY10	yoy chg	qoq chg
Gross NPAs (Rs mn)	2,307	3,295	4,251	1,944	956
Gross NPA (%)	1.44	2.02	2.57	113	55
Net NPAs (Rs mn)	1,241	2,058	2,911	1,671	853
Net NPA (%)	0.78	1.27	1.78	100	51
Coverage (%)	46.2	37.5	31.5	(1,471)	(603)

- Gross NPAs and Net NPAs inch-up by 50-55bp qoq, while coverage declined by ~600bp qoq to 31.5%; Including write-offs and excess general provisions, the coverage ratio is higher
- Incremental restructurings remain low at Rs1.5bn (0.9% of net loans)

IDFC-SSKI INDIA

Analyst	Sector/Industry/Coverage	E-mail	Tel. +91-22-6638 3300
Pathik Gandotra	Head of Research; Financials, Strategy	pathik@idfcsski.com	91-22-6638 3304
Shirish Rane	Construction, Power, Cement	shirish@idfcsski.com	91-22-6638 3313
Nikhil Vora	FMCG, Media, Mid Caps, Education, Exchanges	nikhilvora@idfcsski.com	91-22-6638 3308
Ramnath S	Automobiles, Auto ancillaries, Real Estate, Oil & Gas	ramnaths@idfcsski.com	91-22-6638 3380
Nitin Agarwal	Pharmaceuticals	nitinagarwal@idfcsski.com	91-22-6638 3395
Chirag Shah	Metals & Mining,Telecom, Pipes, Textiles	chirag@idfcsski.com	91-22-6638 3306
Bhoomika Nair	Logistics, Engineering	bhoomika@idfcsski.com	91-22-6638 3337
Hitesh Shah	IT Services	hitesh.shah@idfcsski.com	91-22-6638 3358
Bhushan Gajaria	Retailing, FMCG, Media, Mid Caps	bhushangajaria@idfcsski.com	91-22-6638 3367
Ashish Shah	Construction, Power, Cement, Telecom	ashishshah@idfcsski.com	91-22-6638 3371
Salil Desai	Construction, Power, Cement	salil@idfcsski.com	91-22-6638 3373
Ritesh Shah	Pharmaceuticals, IT Services	riteshshah@idfcsski.com	91-22-6638 3376
Neha Agrawal	Financials	neha@idfcsski.com	91-22-6638 3237
Swati Nangalia	Mid Caps, Media, Exchanges	swati@idfcsski.com	91-22-6638 3260
Sameer Bhise	Strategy, Financials	sameer@idfcsski.com	91-22-6638 3390
Shweta Dewan	Mid Caps, Education, FMCG	shweta.dewan@idfcsski.com	91-22-6638 3290
Nikhil Salvi	Construction, Power, Cement	nikhil.salvi@idfcsski.com	91-22-6638 3239
Rajeev Desai	Real Estate	rajeev@idfcsski.com	91-22-6638 3231
Chinmaya Garg	Financials	chinmaya@idfcsski.com	91-22-6638 3325
Aniket Mhatre	Automobiles, Auto ancillaries	aniket@idfcsski.com	91-22-6638 3311
Probal Sen	Oil & Gas	probal@idfcsski.com	91-22-6638 3238
Saumil Mehta	Metals, Pipes	saumil.mehta@idfcsski.com	91-22-6638 3344
Rupesh Sonawale	Database Analyst	rupesh@idfcsski.com	91-22-6638 3382
Dharmesh Bhatt	Technical Analyst	dharmesh@idfcsski.com	91-22-6638 3392

Equity Sales/Dealing	Designation	E-mail	Tel. +91-22-6638 3300
Naishadh Paleja	MD, CEO	naishadh@idfcsski.com	91-22-6638 3211
Paresh Shah	MD, Dealing	paresh@idfcsski.com	91-22-6638 3341
Vishal Purohit	MD, Sales	vishal@idfcsski.com	91-22-6638 3212
Nikhil Gholani	MD, Sales	nikhil@idfcsski.com	91-22-6638 3363
Sanjay Panicker	Director, Sales	sanjay@idfcsski.com	91-22-6638 3368
V Navin Roy	Director, Sales	navin@idfcsski.com	91-22-6638 3370
Suchit Sehgal	AVP, Sales	suchit@idfcsski.com	91-22-6638 3247
Pawan Sharma	MD, Derivatives	pawan.sharma@idfcsski.com	91-22-6638 3213
Dipesh Shah	Director, Derivatives	dipeshshah@idfcsski.com	91-22-6638 3245
Jignesh Shah	AVP, Derivatives	jignesh@idfcsski.com	91 22 6638 3321
Sunil Pandit	Director, Sales trading	suniil@idfcsski.com	91-22-6638 3299
Mukesh Chaturvedi	SVP, Sales trading	mukesh@idfcsski.com	91-22-6638 3298
Viren Sompura	VP, Sales trading	viren@idfcsski.com	91-22-6638 3277
Rajashekhar Hiremath	VP, Sales trading	rajashekhar@idfcsski.com	91-22-6638 3243

Explanation of Ratings:

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

Disclosure of interest:

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