

Company Flash

5 March 2008 | 7 pages

ICICI Bank (ICBK.BO)

Offshore Exposure – A Little More Than Met the Eye

- New disclosures, exposures and negative surprises** — ICBK has stated, (following a government statement) that cumulative MTM losses on its international business are \$264m (Rs10.5b), as at Jan end. This is well ahead of the Dec 07 disclosed cumulative provisioning of about \$70m. New MTMs a mix of a) further markdown on disclosed CDS portfolio and b) new disclosure, of a previous markdown, on its non-India exposure. The new disclosure is the bigger disappointment and risk; combined, should hurt earnings and valuations.
- Additional P&L charge of Rs3b – and a Rs4b subsidiary markdown not previously disclosed** — What is new a) increased MTM write-downs on its CDS (India related) book of about Rs3b likely in 4Q08 about 15% of PBT for now – well ahead of our Rs1.5b expectation (and spreads have moved adversely since); b) estimated Rs4b balance-sheet charge on international investments from its UK subsidiary – already accounted for in Dec 07, but not disclosed.
- Is it still a MTM issue only, or could there be credit risks** — ICBK's earlier markdowns were on its CDS exposure to large Indian corporates – implied limited credit risks. The newly disclosed markdowns are, however, primarily on its international investments (30% of total exposure); while management suggests these are largely investment grade, we believe there is a higher possibility of credit risk here, and raises the risk profile of this portfolio.
- The fundamental issue is the offshore strategy** — While the stock has probably already adjusted to new disclosures, the larger issue is international business. It is large, relatively low return and risky – the strategy needs some adjustments.

Buy/Low Risk	1L
Price (04 Mar 08)	Rs971.90
Target price	Rs1,510.00
Expected share price return	55.4%
Expected dividend yield	1.1%
Expected total return	56.4%
Market Cap	Rs1,081,331M US\$26,842M

Price Performance (RIC: ICBK.BO, BB: ICICIB IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2006A	25,397	28.13	5.2	34.6	3.9	14.6	0.9
2007A	31,097	34.46	22.5	28.2	3.6	13.4	1.0
2008E	43,396	39.12	13.5	24.8	2.2	12.1	1.1
2009E	58,356	52.60	34.5	18.5	2.0	11.7	1.1
2010E	78,380	70.65	34.3	13.8	1.9	14.3	1.2

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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¹Citigroup Global Markets India Private Limited

Figure 1. ICICI Bank Offshore Exposure Write downs

	Already disclosed		New Disclosure	
	Amount (Rsb)	Accounted	Amount (Rsb)	Accounted
2Q 08	1.5	P&L - ICBK		
3Q08	1.2	P&L - ICBK	4.0	BS - subsidiary
Already Done	2.7	P&L - ICBK	4.0	BS - subsidiary
Current (Jan 08)			3.0	P&L - ICBK
Current (Jan 08)			0.7	BS - subsidiary
Additional P&L provisioning in 4Q08			3.0	
% of 4Q08E PBT			15%	
% of FY08 BV			1%	
Total Cost	2.7		7.7	10.4

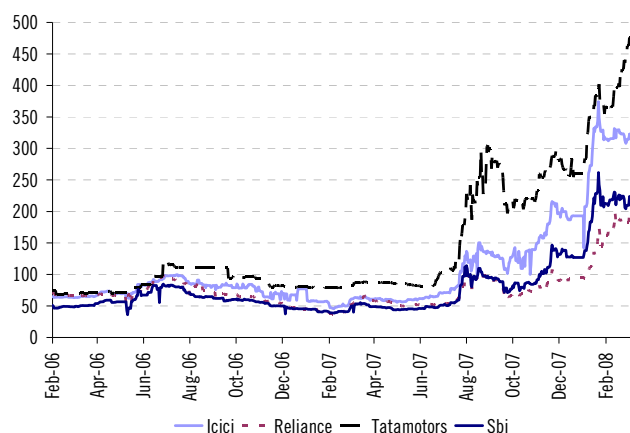
Source: Citi Investment Research

Figure 2. ICICI Bank Offshore Exposure (Rs bn., %)

Total offshore Exposure	Rs. bn	Funded/ Non Funded	% of assets
Government	21	Funded	0.50%
Associates etc.	98	Funded	2.50%
Others (details below)	60	Mixed	1.50%
Loans	359	Funded	9.10%
Cash	179	Funded	4.50%
Total	717	Mixed	18.10%
<i>Of this</i>			
India Exposure	70%		
Us Exposure	30%		
<i>Others; Instrument</i>			
CDS	40	Non Funded	1.00%
CLN's	5	Funded	0.10%
CDO	15	Funded	0.40%
Total	60		1.50%
<i>Others; Geography</i>			
Indian Corporate	42	Funded	1.10%
Others	18		0.50%
Total	60		1.50%

Source: Citigroup Investment Research estimates, company * as of Jun'07

Figure 3. Indicative Indian Corporate Offshore CDS Spreads increasing



Source: Bloomberg

Figure 4. Indicative Indian Corporate CDS Spread Movement

Company	ICICI	Reliance	Tata Motors	SBI
1 yr	426%	274%	477%	348%
2 yrs	125%	74%	163%	112%
Since Aug'07	171%	105%	122%	129%
Since Dec'07	67%	107%	83%	76%
Dec'07- Jan'08	63%	69%	41%	68%
Since 31 Jan'08	2%	23%	30%	5%

Source: Bloomberg , CIR *data as of 4 March'08

ICICI Bank

Company description

ICICI Bank was founded in 1994 by ICICI Ltd., which was then the country's leading development finance institution. It is a leader in retail lending, with more than 30% market share in all consumer-finance segments. ICICI Bank has international banking operations as its key focus area.

Investment strategy

Our Buy/Low Risk (1L) rating is premised on: (1) ICBK's broad exposure to the strong momentum in the Indian economy, and its strong market position in the Indian market; (2) a broad asset mix, which should reduce the risk and profitability strain from concentration; (3) the growing value of its subsidiary businesses; (4). the bank, in our view, offers one of the best exposures to the consumer finance and financial services opportunity in India, and has been at the forefront of building market leadership in most products; and (5) its strong and deep management team. ICICI Bank also offers large exposure to the corporate lending and capex cycle, which should be viewed against the economy's bright prospects.

Valuation

Our target price of Rs1,510 is based on our EVA model. Our target price incorporates Rs386 for its securities unit ; b) risk free rate – we factor in 7.75%. Our EVA methodology is a standard valuation measure for our India banking universe. Our target price is premised on the following: (1) a risk-free rate of 7.75%; (2) a long-term loan loss of 100bps; and (3) subsidiary value of Rs386 per share.

We also use the sum of parts methodology, benchmarking valuations to individual businesses. On our sum-of-the-parts methodology, our fair value for ICICI Bank is Rs1,383. We value ICICI Bank's banking business on a 2.25x FY09E PBV (2X FY09E PBV earlier), reflecting the leverage potential of the business as also peer company valuations, but also factor in the ROE, which is currently below its cost of capital. In addition, we are factoring in Rs386 as the value of its subsidiaries – specifically, these are; Life insurance Business at Rs246 per share (18X FY09E NBAP), General Insurance at Rs40 per share (20X FY09E PE), AMC at Rs27 per Share (8% of AUM), ICICI securities at Rs55 per Share (20X FY09E), Venture Fund at Rs21 per share (15% of FY09E AUM).

We prefer to use EVA as our primary methodology as we believe it better adjusts for the relatively dynamic cost of capital and better captures the long-term value of the business.

Risks

Our risk rating is Low based on our quantitative risk-rating system, which tracks 260-day historical share price volatility. The downside risks that could impede the shares from reaching our target price include: (1) continued deterioration in asset quality; (2) low margins, with a limited cushion if there is further downside pressure; (3) aggressive growth in a range of business areas raises the risk of some failures; (4) aggressive international operations where returns appear low, and risk levels relatively high, and (5) inability to leverage capital, which keeps ROEs low.

Appendix A-1

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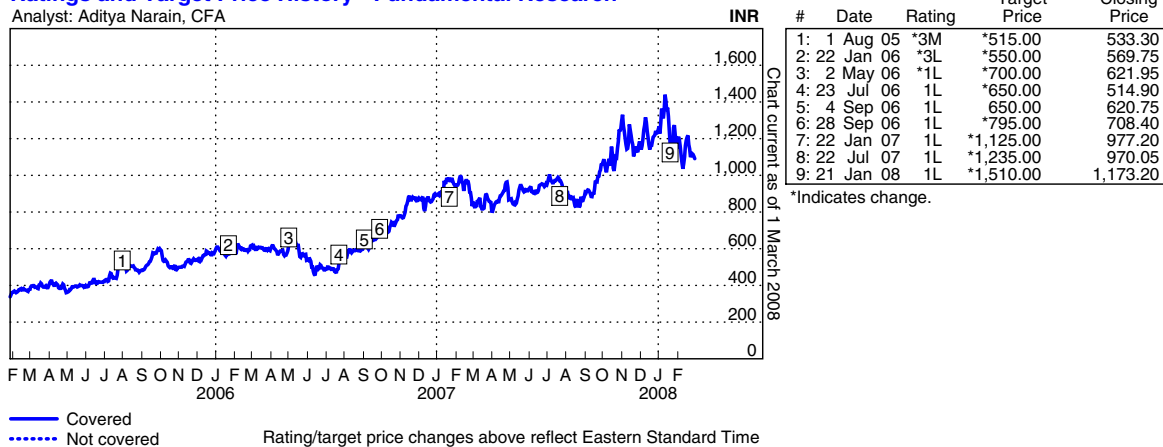
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Ratings and Target Price History - Fundamental Research

Analyst: Aditya Narain, CFA



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