IDFC SSKI

INDIA RESEARCH

IDBI Bank

Rs95

UNDERPERFORMER

RESULT NOTE

Mkt Cap: Rs69.0bn; US$1.41bn

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Result: **Q1FY10**
Comment: **Subdued earnings**
Revision: **Expect earnings to grow by 20% yoy in FY11**

Key valuation metrics

Year to March 31 (Rs m)	NII	yoy chg (%)	Net profit	yoy chg (%)	EPS (Rs)	P/ Adj.Bk (x)	PER (x)	RoE (%)
FY07	6,579	44.3	6,303	12.4	8.7	1.13	10.9	12.3
FY08	6,569	-0.2	7,295	15.7	10.1	3.65	9.5	11.1
FY09	13,263	101.9	8,585	17.7	11.8	1.66	8.0	14.6
FY10E*	15,358	39.3	7,128	-17.0	9.8	1.40	9.7	9.7
FY11E*	19,154	24.7	8,571	20.3	11.8	1.29	8.1	10.7

** Excludes recoveries*

HIGHLIGHTS OF Q1FY10 RESULTS

IDBI Bank reported a muted PAT growth of 7.5% yoy to Rs1.7bn in Q1FY10, well below our estimates, owing to significantly higher provisioning expenses and lower NII growth.

- NII below expectations…: NII came in at Rs3.2bn (a 389% yoy growth over a low base), below our estimate of Rs4.2bn (adjusted for recoveries as the bank is reporting recoveries in non-interest income from this quarter), due to lower loan growth (5% qoq decline) and a ~50bp qoq decline in calculated NIMs.
- …as margins contract sequentially: Despite a sharp decline in wholesale borrowing costs, calculated margins declined by ~50bp qoq to 0.73% in Q1FY10. Contraction in margins was led by (i) investment of ~Rs8bn made in low yielding SLR securities during the quarter, (ii) decline in CASA ratio by ~320bp yoy to 11.5%, and (ii) deterioration of 700bp+ qoq in CD ratio to 84.8%.
- Restructurings rise; asset quality remains a key monitorable: The bank incrementally restructured Rs59bn of standard advances during the quarter (6.0% of net advances as of June '09), taking the overall restructured advances to ~Rs90bn (9.2% of net advances). Management indicated that of the incremental advances restructured during the quarter, bulk pertain to 3 large accounts. Gross NPAs also increased by ~40bp qoq to 1.77% (Rs3.1bn rise in absolute terms).
- Jump in provisioning expenses; coverage declines: Earnings were subdued on account of elevated provisions of Rs5.6bn. On account of advances restructured, the bank made provisions of Rs5.2bn (~9% of advances) during the quarter. NPA provisions were lower at Rs370m, leading to a ~280bp qoq and 100bp yoy decline in coverage ratio to 31.1%.
- Robust treasury gains; traction in core fee income: Other income grew over 100% yoy to Rs7.6bn on the back of strong treasury gains of Rs4.7bn. Core fee income (CEB) gained ground, up 97% yoy buoyed by trade credit (LCs, guarantees) and syndication business. Recoveries came in Rs260m, as against Rs270m in Q1FY09.
- Strong deposit growth; CASA ratio slips: Owing to ample liquidity in the system, deposit growth remained strong at 59% yoy and 3% qoq. However, CASA ratio declined by ~330bp qoq to 11.5% as (i) outflow of the year-end

floats led to 30% qoq decline in current deposits, and (ii) savings deposits increased at a lower pace of 16% yoy as against 65% yoy growth in term deposits.

- Capital adequacy remains a concern: Tier-1 ratio came in at 7.1%, with overall CRAR at 12.3%. The bank raised Rs5bn of Upper Tier-II bonds, with 15 year maturity during the quarter (coupon rate at 8.95%). Management indicated that it has sufficient headroom to raise hybrid capital to sustain growth for another 12 months, and has approached the government for equity infusion in the near term.
- Introducing FY11 numbers: We are forecasting a profit growth of 20% yoy in FY11 to Rs8.6bn, driven by a 22% yoy growth in credit and a marginal uptick in margins. NII is estimated at Rs19.1bn – a 25% yoy growth.

VALUATIONS & VIEW

In Q1FY10, IDBI Bank's earnings growth remained muted due to significantly higher provisioning expenses and lackluster NII growth. Asset quality remains a concern owing to significant restructurings (6% of the book during Q1FY10), slippages and a low coverage ratio. On the other hand, margins declined despite a sharp reduction in wholesale borrowing costs, as yields were bogged down by investments in low yielding G-Sec bonds to build up the SLR book (now at 24%). Further, CASA ratio remains low (11.47% as of June 2009) and makes margins vulnerable to market volatility. On the positive side, treasury gains were strong at Rs4.65bn (61% of operating profit) and fee income evidenced traction. We remain cautious on the tenacity of IDB Bank's core earnings and expect earnings to remain flat over FY09-11 with an average RoE of ~10% (low compared to PSU peers). We are maintaining our FY10 estimates with higher treasury gains being offset by rise in provisions and MAT payout. Whilst higher recoveries and trading gains offer an upside to our estimates, we expect stress on asset quality and subdued core performance to dent the earnings visibility and sustainability. The stock currently trades at 1.4x FY10E and 1.3x FY11E adj book. Maintain Underperformer.

Quarterly results

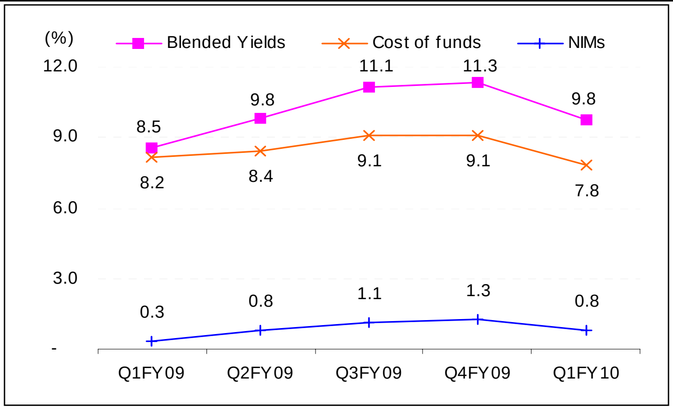
Rs m	Q1FY09	Q2FY09	Q3FY09	Q4FY09	Q1FY10	FY09	FY10E	FY11E	Comments
Total intt income	23,906	25,903	32,023	32,182	34,633	114,086	142,305	162,790	
Interest expense	23,256	24,683	27,310	27,808	31,469	103,057	126,947	143,636	
Net interest income	**650**	**1,220**	**4,713**	**4,374**	**3,164**	**11,029**	**15,358**	**19,154**	Lower due to muted asset growth and decline in margins
yoy growth (%)	*(258.1)*	*156.4*	*1,588.0*	*464.7*	*386.6*	*772.1*	*39.3*	*24.7*	
Other income	**3,485**	**4,271**	**3,110**	**5,163**	**7,556**	**16,129**	**18,582**	**17,168**	Robust treasury and traction in CEB
yoy growth (%)	*(30.9)*	*(19.9)*	*(46.3)*	*(3.9)*	*116.8*	*(24.3)*	*15.2*	*(7.6)*	
Recoveries	270	1,070	450	440	260	2,230	1,000	1,200	Remain low due to difficult operating environment
Trading gains	1,590	1,260	530	1,980	4,650	7,253	6,200	3,000	Rs3.6bn from G-Secs & Rs1.1bn from equities
Other income	1,625	1,941	2,130	2,743	2,646	6,646	11,382	12,968	Traction in CEB driven by non fund based income
Net revenue	**4,135**	**5,491**	**7,823**	**9,537**	**10,720**	**27,158**	**33,941**	**36,322**	
Operating expenses	2,119	2,646	3,917	4,698	3,159	13,379	15,962	18,627	Opened 29 new branches and 60 new ATMs in the quarter
Operating profit	**2,016**	**2,845**	**3,906**	**4,839**	**7,561**	**13,779**	**17,979**	**17,695**	
yoy growth (%)	*(21.6)*	*(19.1)*	*(0.5)*	*58.4*	*275.0*	*6.0*	*30.5*	*(1.6)*	
Total provisions	**199**	**1,000**	**1,435**	**1,117**	**5,603**	**3,923**	**9,593**	**7,611**	Well above estimates due to provisions on restructurings
PBT	**1,818**	**1,845**	**2,471**	**3,723**	**1,958**	**9,856**	**8,386**	**10,084**	
Tax	220	220	245	586	240	1,271	1,258	1,513	
PAT	**1,598**	**1,625**	**2,226**	**3,137**	**1,718**	**8,585**	**7,128**	**8,571**	Muted NII & elevated provisioning costs
yoy growth (%)	*4.4*	*4.5*	*26.6*	*27.8*	*7.5*	*17.7*	*(17.0)*	*20.3*	

Quarterly results (Contd)

Rs m	Q1FY09	Q2FY09	Q3FY09	Q4FY09	Q1FY10	FY09	FY10E	FY11E	Comments
Ratios (%)									
NIM (reported)	0.3	0.8	1.1	1.3	0.8				Lower yields due to PLR cuts & investments in G-Secs
NIM (calc)*	0.2	0.4	1.3	1.1	0.7	0.8	0.9	1.0	
Op expense/ avg assets	0.6	0.8	1.1	1.2	0.7	0.9	0.9	0.8	Plans to open 130 new branches in FY10 and 200 in FY11
Tot prov/ avg assets	0.1	0.3	0.4	0.3	1.3	0.3	0.5	0.3	
PBT/avg assets	0.6	0.6	0.7	0.9	0.5	0.7	0.4	0.5	
PAT/ avg assets	0.5	0.5	0.6	0.8	0.4	0.6	0.4	0.4	
Tax/PBT	12.1	11.9	9.9	15.7	12.3	12.9	15.0	15.0	Rise in MAT to lead to higher tax outflows
CD ratio	107.4	109.7	114.1	92.0	84.8				Decline in line with the industry wide trend
SLR		16	18	~22	24				Invested Rs8bn in G-Secs to reach regulatory minimum of 24%
CRAR	12.0	11.6	11.8	11.6	12.3				Raised Rs5bn of Tier-II bonds during the quarter
Tier -I	7.5	7.1	6.9	6.8	7.1				
Balance Sheet (Rs bn)									
Credit	781	871	922	1,034	980				Muted in line with the industry; ~20% qoq growth in retail driven by mortgages
yoy growth (%)	30.7	39.7	34.7	25.8	25.4				
Deposits	727	794	808	1,124	1,156				
yoy growth (%)	55.5	58.9	42.0	54.0	58.9				

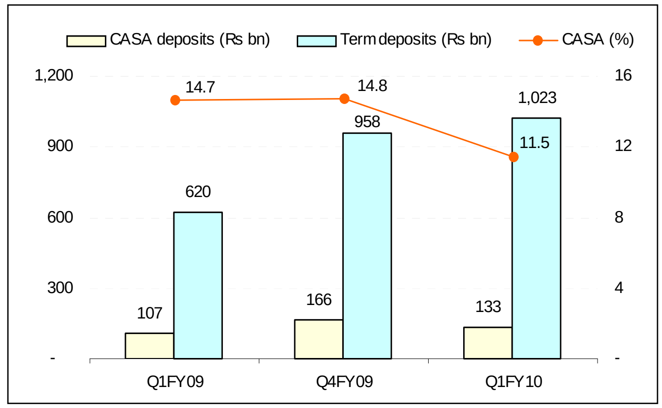
** Calculated on average quarterly balances*

Exhibit 1: Margins expand



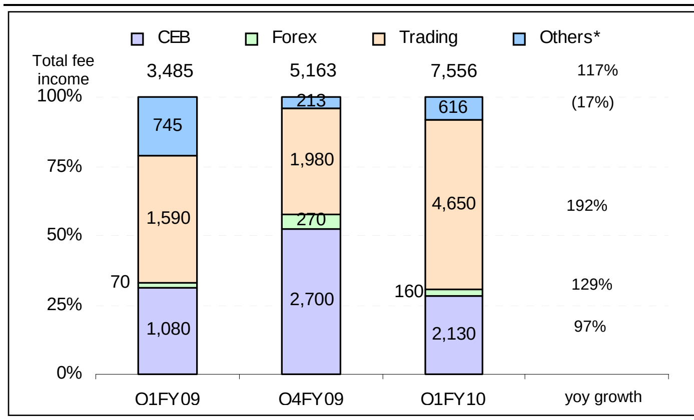
- Sequential decline in NIMs driven by lower yields
- Yields bogged down by the impact of PLR cuts and aggressive investments in the low yielding G-sec securities

Exhibit 2: CASA slips



- Strong deposit growth and outflow of year end floats leads to 300bp+ qoq and yoy decline in CASA to 11.47%
- Savings deposits grow by 16% yoy and current by 37% yoy

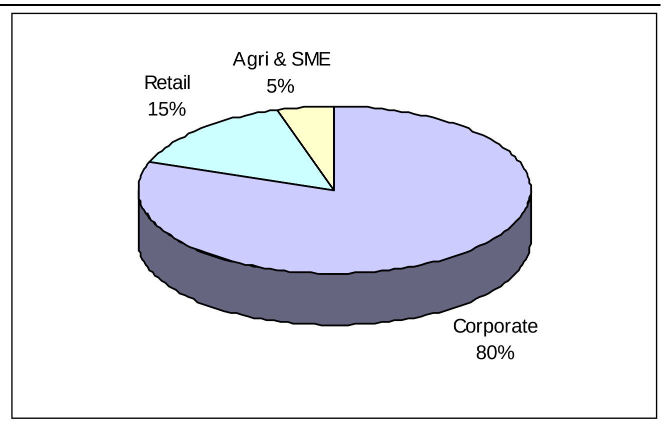
Exhibit 3: Non fund income remains strong (Rs m)



- ~120% yoy growth buoyed by robust treasury gains on G-Sec as well as equity book
- Traction in CEB buoyed by trade credit and syndication business

** Primarily loss on revaluation of investments*

Exhibit 4: Composition of advances book#



- Slowdown in credit off-take (25% yoy growth & 5% qoq decline)
- Retail loans grow by ~20% qoq dominated by mortgages

#Approximate

Exhibit 5: Rise in Gross NPAs as well as restructured accounts

	Q1FY09	Q4FY09	Q1FY10	Incremental (Rsm/bps)
Gross NPAs (Rs m)	15,782	14,357	17,480	3,124
Net NPAs (Rs m)	10,712	9,490	12,042	2,553
Gross NPAs (%)	1.98%	1.38%	1.77%	39
Net NPAs (%)	1.36%	0.92%	1.23%	31
Loan loss coverage (%)	32.1%	33.9%	31.1%	(279)
Restructured loans (Rs m)		31,320	59,000	
% of loans		3.0%	6.0%	

- Increase in Gross NPAs, even as the coverage ratio deteriorates
- Rs59bn of accounts, indicated to be pending as of March 2009, restructured during Q1FY10

Exhibit 6: Break up of provisions (Rs m)

	Q1FY09	Q4FY09	Q1FY10
Prov for NPA	180	430	370
Investment depr	-	620	-
Provision on restructuring			5,190
Others	20	67	43
Total	200	1,117	5,603

- Well above expectations due to higher restructurings
- Bulk of the provisioning attributable to a single restructured account

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