

ICICI Bank

Rs1085
OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs1,248bn; US\$27.3bn

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Result: Q3FY11

Comment: Staying the course

Revision: Earnings upgraded by 4.1% for FY11E and 1.9% for FY12E

Key valuation metrics

Year to March 31 (Rs m)	NII	yoy chg (%)	Net profit	yoy chg (%)	EPS (Rs)	Adj. Book Value per share (Rs)	P/ Adj.Bk (x)	PER (x)	RoE (%)
FY08	73,041	29.6	41,577	33.7	37.4	418	2.60	29.0	11.7
FY09	83,666	14.5	37,581	(9.6)	33.8	445	2.44	32.1	7.8
FY10	81,144	(3.0)	40,250	7.1	36.1	463	2.34	30.0	8.0
FY11E	89,350	10.1	52,558	30.6	45.7	478	2.27	23.7	9.9
FY12E	111,926	25.3	67,552	28.5	58.7	515	1.54	18.5	11.8

Key highlights

ICICI Bank reported strong results with a net profit of Rs14.4bn (up 31% yoy), ahead of our estimate of Rs13.9bn. Core performance exhibited strength as NII and fee income gained traction, provisions expenses declined sharply, and CASA ratio remained robust, leading to a 25bp yoy expansion in RoA to 1.5%. Advances grew 6% qoq as corporate loan momentum remained strong and the decline in retail was arrested.

- **Strong growth in NII...:** NII came in at ~Rs23.1bn, ahead of our estimates, led by traction in loan book and sequentially steady margins.
- **...as margins remain steady:** Reported margins were steady qoq as well as yoy at 2.6% as the benefit of increasing yields was offset by higher cost of funds. The management indicated that the bank is earning a margin of 3% on the domestic book, while the international book is delivering a NIM of ~85bp (up from 50bp in FY10 and 80bp in Q2FY11). With spreads on incremental international business higher at ~125bp, international margins are expected to rise further to ~100bp. (Exhibit 2).
- **Traction in credit offtake; expected to gain pace:** Credit increased by 6.4% qoq, led by strong momentum in corporate loans and a pause in the decline of retail loans (a 1% sequential expansion). On the corporate book, traction was led by working capital and term loans, though project finance loans remained muted. The composition of the retail book remained largely stable and the bank reiterated its intent to grow secured auto loans (26%) and mortgage loans (66%) in the segment. Retail disbursements grew by a robust 34% yoy to Rs71bn (flat qoq), of which Rs40bn emanated from mortgage loans. Going forward, we expect the robust corporate sanctions pipeline to drive loan book momentum (~22% CAGR over FY10-12E). (Exhibits 5 & 6).
- **Provisioning expenses decline qoq; coverage ratio inches up:** The management indicated that delinquencies remained low in the quarter, which aided a 27% qoq decline in provisions expenses to Rs4.6bn, as against Rs6.4bn in Q2FY11. Correspondingly, the bank's coverage ratio increased by 330bp qoq to 71.8%, ahead of the

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regulatory requirement of 70%. With coverage ratio requirement met and slippages on a decline, credit costs are expected to taper off significantly from here. Net restructured loans stood at Rs25.6bn (~1.2% of net advances), flat sequentially. While Rs6bn of loans were restructured during the quarter, a similar amount was also repaid over the quarter. (Exhibit 7).

- **Healthy growth in core fee income:** Core fee income grew by a strong 14% yoy to Rs16.3bn in Q3FY11, led by growth in corporate and international fees. On the corporate side, syndication and lending fees contributed to the traction, while on the international front remittances and lending-related fees exhibited strength. While retail fees continued to decline yoy, it was steady qoq. The bank booked treasury gains of Rs210m in Q3FY11. Overall other income increased by 5% yoy to Rs17.5bn. (Exhibit 4).
- **Elevated CASA ratio:** In line with the bank's strategy of fortifying its liability franchise, CASA deposits grew by 23% yoy while CASA ratio improved by 20bp qoq to 44.2% (39.6% in Q3FY10). Current deposits increased by 16% yoy and savings deposits increased by 27% yoy. Average CASA increased from 39.2% in Q2FY11 to 40.3% in Q3FY11. (Exhibit 3).
- **Operating expenses:** Operating expenses increased by 26% yoy and 9% qoq to Rs17.2bn – affected by aggressive branch rollout in the previous quarter (275 branches added in Q1FY11), expenses for the Bank of Rajasthan merger and bonus provisions made in the quarter. The management indicated that Rs900m of cost pertained to the full impact of the BoR merger in Q2FY11. We expect operating costs to increase in tandem with asset growth, keeping the ratio of opex to average assets stable at current levels (~1.75% in Q3FY11).
- **Subsidiaries maintain leadership:** The buoyant capital markets have driven an uptick in the performance of ICICI's life insurance subsidiary. ICICI Prudential Life's APE increased ahead of the peers in Q3FY11 (up 10% yoy); the insurer reported PAT of Rs1.3bn (including surplus from non-participating policyholders' funds). Notably, the insurer maintained NBAP margin of 17.6% in Q3FY11 despite the new IRDA guidelines coming into effect. General insurance business premium increased to Rs10.1bn in Q3FY11 from Rs8.3bn in Q3FY10.

Valuations & view

After two years of calibrated growth, ICICI Bank delivered a sharp expansion in core profitability this quarter. Consistent delivery on its plan to increase CASA ratio, improve credit quality and curtail costs, has paid off with the bank's RoA surging to 1.5%. We believe ICICI is now firmly en route to the next phase of its strategy – delivering high profitability with acceleration in balance sheet growth. Owing to better-than-expected traction in NII as also emerging visibility on credit costs, we are increasing our earnings estimates by 4.1% for FY11 and 1.9% for FY12. We expect the bank to deliver 30% CAGR in earnings, driven by steeply declining credit costs, expanding margins and strong loan growth. We see a 370bp rise in core business RoE to ~14% over FY10-12. This, we believe, would drive a structural re-rating of the stock from 1.8x currently to 2.5x core book. We reiterate our Outperformer stance with a 12-month price target of Rs1,450 (Rs215/ share for non-banking investments and 2.5x FY12E core book). ICICI Bank remains our top pick in the Indian financials space.

ICICI Bank - SOTP

	(Rs bn)		(Rs/ share)		Valuation methodology
	FY11	FY12	FY11	FY12	
Life insurance	252	277	151	165	30% discount to DCF value
Non-life insurance	10	10	9	9	10x FY10 earnings
Asset Management	19	19	17	17	5% of AuM
ICICI Ventures	9	9	8	8	10% of AuM
ICICI Securities	18	18	16	16	Comparables
Total subsidiaries	308	333	201	215	
ICICI Bank core value	1,297	1,414	1,124	1,235	2.5x banking book
Total value (Rs per share)			1,325	1,450	

Source: IDFC Securities Research

Quarterly results

P&L (Rs m)	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	FY10	FY11E	FY12E
Net interest income	20,581	20,349	19,911	22,044	23,117	81,144	89,350	111,926
yoy growth (%)	3.4	(4.9)	0.3	8.3	12.3	(3.0)	10.1	25.3
Non interest income	16,730	18,908	16,805	15,780	17,490	74,777	68,746	83,588
yoy growth (%)	(33.5)	13.0	(19.6)	(13.5)	4.5	(1.7)	(8.1)	21.6
Fee income	14,220	15,210	14,130	15,900	16,250	62,967	68,346	79,588
yoy growth (%)	5.6	13.3	7.1	14.6	14.3	(12.1)	8.5	16.4
Trading	(260)	1,960	1,040	(1,440)	210	6,809	(3,350)	250
Net revenue	37,311	39,258	36,716	37,824	40,607	155,920	158,096	195,514
Op expenses	13,624	15,269	14,835	15,704	17,179	58,598	65,277	78,251
yoy growth (%)	(21.4)	(7.9)	(4.0)	10.2	26.1	(16.8)	11.4	19.9
Operating profit	23,687	23,989	21,881	22,120	23,428	97,322	92,820	117,262
yoy growth (%)	(14.5)	11.3	(13.5)	(9.2)	(1.1)	9.0	(4.6)	26.3
Provisions	10,022	9,898	7,978	6,410	4,650	43,869	22,743	24,726
yoy growth (%)	(0.5)	(8.7)	(39.7)	(40.2)	(53.6)	15.2	(48.2)	8.7
PBT	13,665	14,091	13,903	15,710	18,778	53,453	70,077	92,537
Tax	2,660	4,036	3,643	3,350	4,410	16,008	17,519	24,985
PAT	11,005	10,056	10,260	12,360	14,368	40,250	52,558	67,552
yoy growth (%)	(13.5)	35.2	16.8	18.8	30.6	7.1	30.6	28.5
Key Ratios (%)								
NIMs (reported)	2.6	2.6	2.5	2.6	2.6			
NIMs (calculated)	2.3	2.3	2.2	2.3	2.4	2.2	2.3	2.4
Fee income /avg assets	1.6	1.7	1.6	1.7	1.7	1.7	1.7	1.7
Non-fund rev/Avg assets	1.9	2.1	1.8	1.7	1.8	2.0	1.7	1.8
Op expense/avg assets	1.5	1.7	1.6	1.7	1.8	1.6	1.7	1.7
Cost/Net rev.	36.5	38.9	40.4	41.5	42.3			
Prov/avg assets	1.1	1.1	0.9	0.7	0.5	1.2	0.6	0.5
Tax/PBT	19.5	28.6	26.2	21.3	23.5	29.9	25.0	27.0
RoA	1.2	1.1	1.1	1.3	1.5	1.1	1.3	1.4
CRAR	19.4	19.4	20.2	20.2	19.8			
Tier-I	14.2	14.0	14.0	13.8	13.7			
CD ratio	90.7	89.7	91.8	87.0	94.9			
Balance Sheet (Rs bn)								
Credit	1,793	1,812	1,844	1,942	2,067			
yoy change (%)	(15.6)	(17.0)	(6.9)	1.8	15.3			
Deposits	1,977	2,020	2,009	2,231	2,177			
yoy change (%)	(5.5)	(7.5)	(4.4)	12.8	10.2			

Calculated ratios are on average quarterly balance

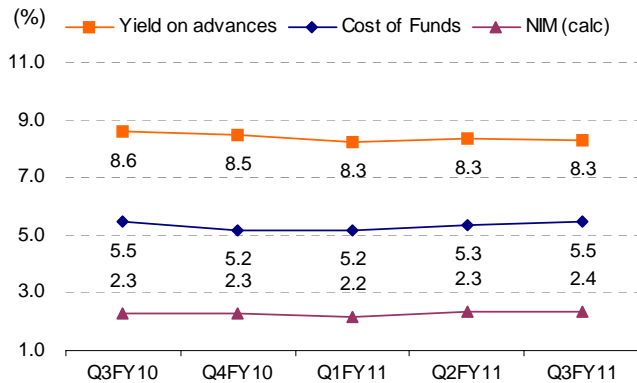
Exhibit 1: Overseas subsidiaries' asset and liability profile

UK subsidiary	As of Dec'10	US\$ m	Comments
Assets			
Loans & advances to customers	57%	3,955	Increased from 50% in Sep'09. Also includes securities re-classified as loans. ~80% of total loan book is exposure to Indian corporates, the balance being to U.K. companies
Bonds/notes of FIIs	16%	1,127	Exposure to senior debt of banks being run-down opportunistically (down from 25% in Dec'09)
Asset backed securities	2%	119	Down from 6% in Dec'08 as the bank re-classified US\$137mn as loans, and also continues to reduce exposure
Other investments	5%	357	
Cash & liquid securities	17%	1,155	Sharp rise of 40% qoq; excess liquidity owing to volatile environment
India-linked investments	4%	287	Includes US\$122m of India-linked credit derivatives
Total assets	100%	7,000	
Liabilities			
Term Deposits	51%	3,556	Proportion of retail term deposits up to 75% of deposits from 69% in Jun'10. Regulation permits the bank to lend retail term deposits (unlike demand deposit). Increased credit deployment to rub-off positively on margins
Long-term Debt	10%	840	
Syndicated Loans	8%	560	
Demand Deposits	16%	1,008	
Net worth	9%	651	PAT of US\$ 12.1m in Q3
Other liabilities	6%	385	
Total Liabilities	100%	7,000	Capital adequacy ratio at 21.2%

Canada subsidiary	As of Dec'10	CAD\$m	Comments
Assets			
Loans & advances to customers	66%	3,107	Indian corporates comprise ~80% of total exposure
Federally insured mortgages	7%	315	
Asset backed securities	2%	80	
Other investments	8%	367	
Cash & liquid securities	15%	714	
India-linked investments	3%	118	Includes CAD 80m of India-linked credit derivatives
Total assets	100%	4,700	
Liabilities			
Term Deposits	60%	2,829	Retail term deposits comprise the bulk
Borrowings	2%	75	
Demand Deposits	15%	710	
Net worth	21%	978	
Other liabilities	2%	108	
Total Liabilities	100%	4,700	Capital adequacy ratio at 26.1%

Eurasia subsidiary	As of Dec'10	US\$m	Comments
Loans & advances to customers	33%	120	Running-off
Corporate bonds	2%	6	
Retail loans	16%	58	Largely mortgages
Cash & liquid securities	46%	169	
Others	4%	14	Capital adequacy at 31.8%
Total assets	100%	367	

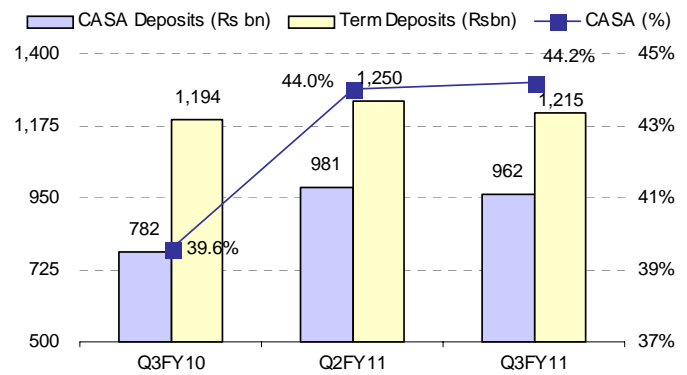
Exhibit 2: Margins remain steady



- Domestic NIMs at 3.0% and international margins increased at ~85bps (up from 50bp in FY10 and 80bp in Q2).

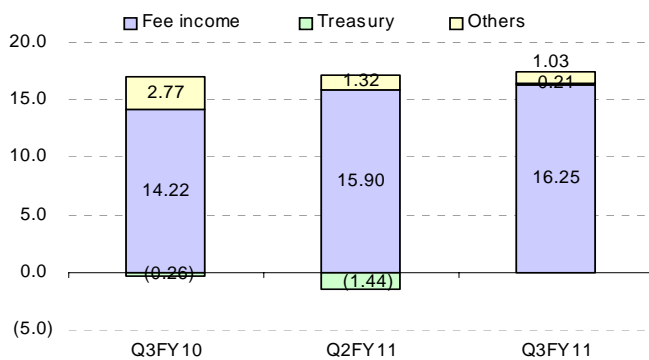
* Calculated on average quarterly balances

Exhibit 3: Momentum in CASA sustained



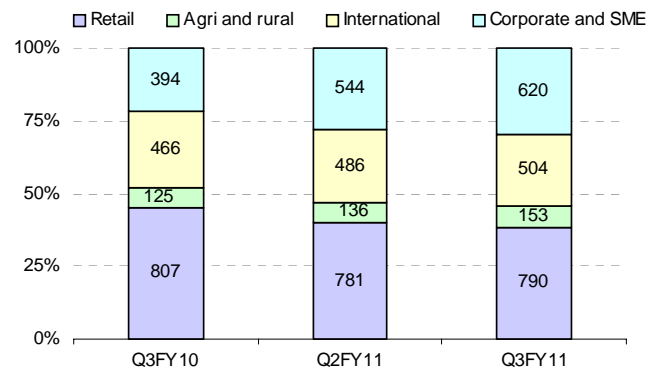
- De-leveraging & increased branches drive CASA up 20bp qoq
- Savings deposits up 2% qoq, while current deposits decline 9% qoq on tight liquidity

Exhibit 4: Non-interest income break up (Rs bn)



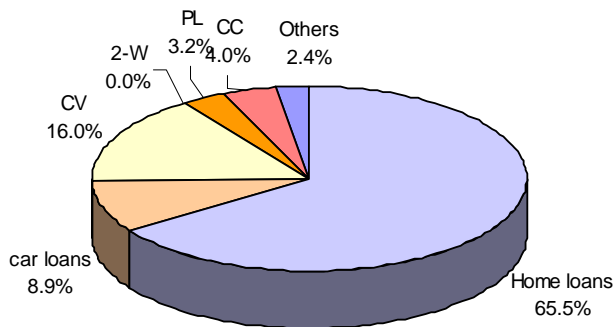
- Revival in fee led by corporate and international fees. Retail fees stable qoq
- Rs210m of treasury gain

Exhibit 5: Composition of loan book (Rs bn)



- Growth led by corporate sector led by working capital and term loans
- Pause in decline of retail loans – 1% qoq rise

Exhibit 6: Composition of retail loan book (%)



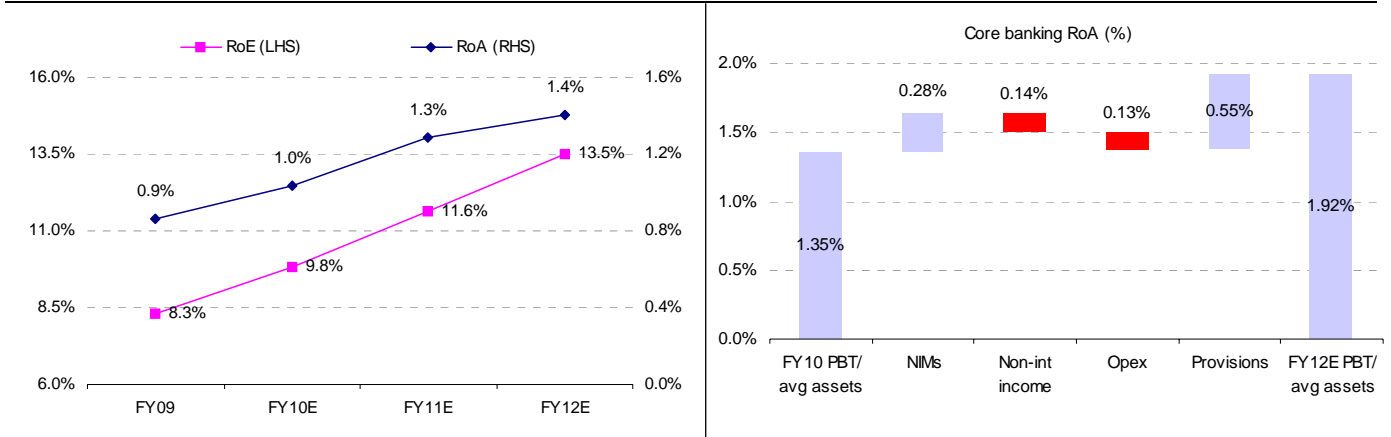
- Composition of retail book remains largely stable as mortgage loans comprise a significant proportion (66% of total)
- High risk loans continue to run off- now at 3% of total

Exhibit 7: Coverage ratio shored up

	Q3FY10	Q2FY11	Q3FY11	yoy growth	qoq growth
Gross NPLs (Rs bn)	89.26	101.41	101.87	14%	0%
Gross NPLs (%)	4.84%	5.06%	4.75%	(9)	(31)
Net NPLs (Rs bn)	43.57	31.92	28.73	-34%	-10%
Net NPLs (%)	2.43%	2.12%	1.39%	(104)	(73)
Provision coverage (%)	51.2	68.5	71.8	2,061	327

- Provision coverage stands at ~72%
- Net addition to gross NPAs negligible

Exhibit 8: See strong traction in core banking RoE and RoA ahead



Source: IDFC Securities Research

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2. Neutral: Within 0-5% to Index (upside or downside)
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