

Initiating Coverage
January 18, 2011

Axis Bank Ltd.



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Axis Bank

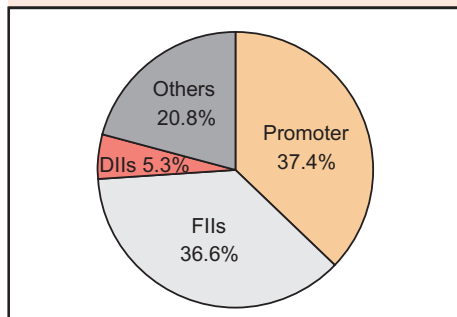
Easy Access to Customers...

January 18, 2011

Key Stock Data	
Sector	Private Bank
CMP	₹1227.55
52-wk High / Low	₹1608/967.15
Market Cap	₹497.36bn (\$10931mn)
Avg 6m daily vol.	212003
BSE Sensex	18882.25
Reco	'Buy'
TP	₹1415

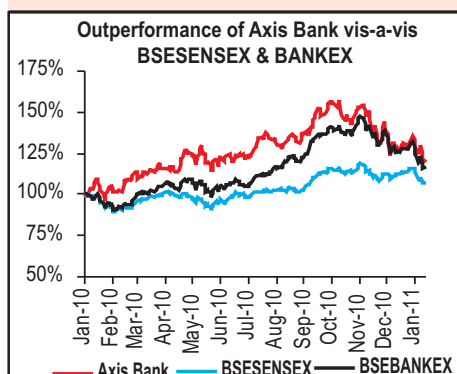
Stock Codes	
Bloomberg Code	AXSB.IN
Reuters Code	AXBK.BO
BSE Code	532215
NSE Code	AXISBANK
Face Value	₹10per share

Shareholding Pattern (30th Sept, 2010)



Price Performance (%)			
1 Mth	3 Mths	6 Mths	1 Yr
-7.0%	-16.8%	5.8%	29.8%

Stock Price Performance



Axis Bank Ltd. (formerly known as UTI Bank Ltd.) incorporated in 1994 is one of the new generation private sector banks, which has established a track record of expanding its business at a faster pace than the industry. The bank was jointly promoted by the Specified Undertaking of the Unit Trust of India (SUUTI), Life Insurance Corporation (LIC), General Insurance Corporation (GIC), and other four PSU insurance companies i.e. National Insurance Company Ltd., The New India Assurance Company Ltd., The Oriental Insurance Company Ltd. and United India Insurance Company Ltd. In terms of asset size and market capitalization, Axis Bank ranks third amongst the private sector banks and has got a network of 1120 branches/ extension counters, 5303 ATM's as of Dec-10 across India and international presence in Singapore, Hong Kong and Dubai. It has five wholly-owned subsidiaries namely, Axis Securities and Sales Ltd., Axis Private Equity Ltd., Axis Trustee Services Ltd., Axis Asset Management Company Ltd. and Axis Mutual Fund Trustee Ltd.

- Diversified loan book with highly rated Corporate and mid-corporate advances constituting more than 50% of the total advances.
- Healthy CASA ratio of ~44% provides respite to cost of funds and likely to sustain NIM in coming years.
- Growth in core business revenues, fee income and better cost efficiency measures will enhance bank's earnings quality.
- The bank is well capitalized and in a position to meet lending targets. The core operating performance and growth is expected to increase ROE and ROA in future.
- The asset quality of the bank is comfortable and has been maintained consistently, resulting in reduction of gross and net NPA ratios.
- An all-share deal worth ₹2067cr with one of India's leading financial services firm, Enam Securities Ltd would enhance positive synergies in future.

(continued...)

Key Financials

Particulars	FY08	FY09	FY10	FY11E	FY12E
Advances	59661.15	81556.76	104343.12	128488.92	149564.34
Deposits	87626.22	117374.11	141300.22	163908.26	186035.87
NII	2585.35	3686.21	5004.49	6785.06	8593.25
Total Income	8800.80	13732.36	15583.80	19313.85	23376.91
Profit after Tax	1071.03	1815.36	2514.53	3283.51	3907.71
EPS (₹)	29.94	50.57	62.06	80.11	93.37
Book Value (₹)	245.13	284.53	396.00	453.82	517.49
Adjusted Book Value (₹)	238.19	275.41	385.66	442.57	505.52
RONW (%)	17.6%	19.1%	19.2%	19.0%	19.4%
ROA (%)	1.2%	1.4%	1.5%	1.7%	1.7%

(E- Keynote Capitals Institutional Research Estimates)

The key concerns are:

- a) Any possible rise in NPAs could see higher provisions than estimated, and may impact profitability and ROE.
- b) Competition from other private banks.

At CMP of ₹1227.55, the stock is trading at 3.2x FY10 price to adjusted book and is expected to trade at 2.8x FY11E and 2.4x FY12E price to adjusted book. Considering the overall growth prospects of the bank, we recommend a 'Buy', assigning a multiple of 2.8x FY12E price to adjusted book to arrive at the target price of ₹1415 per share for a period of one year.

Investment Rationale:

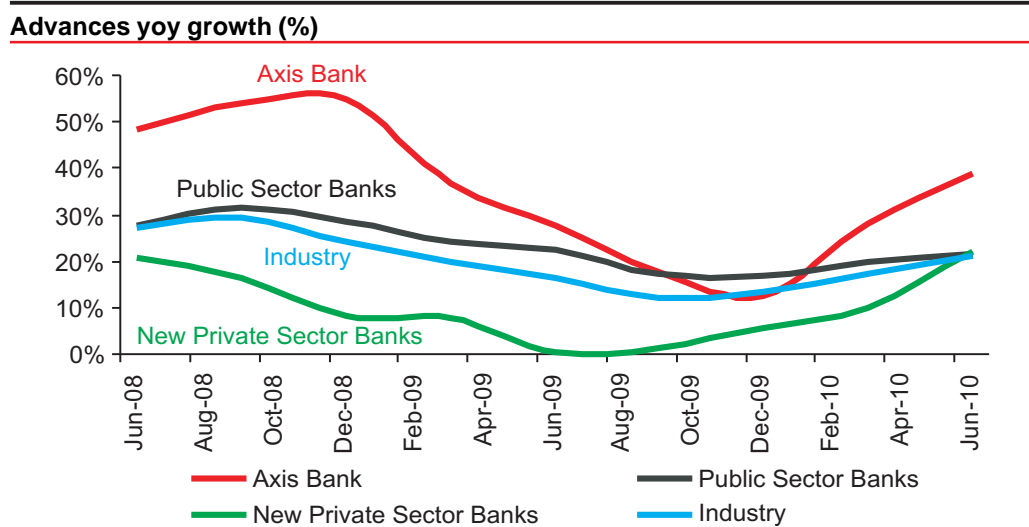
1. Healthy Advances growth:

The Bank's loan book grew at a CAGR of 46.2% stands at ₹104343cr during FY06-10. With revival in the macro-economic conditions, we expect momentum in loan growth to continue in future. The banking industry will register the loan growth largely driven by increase in consumption demand and infrastructure activities.

The growth of bank's loan book clearly surpasses the industry and other banks. It grew by 39.1% (yoy) in 1QFY11, 36.5% (yoy) in 2QFY11 and 45.7% (yoy) in 3QFY11 and is expected to increase by 23.1% in FY11E.

Chart 1

Advances yoy growth more than the industry and other banks

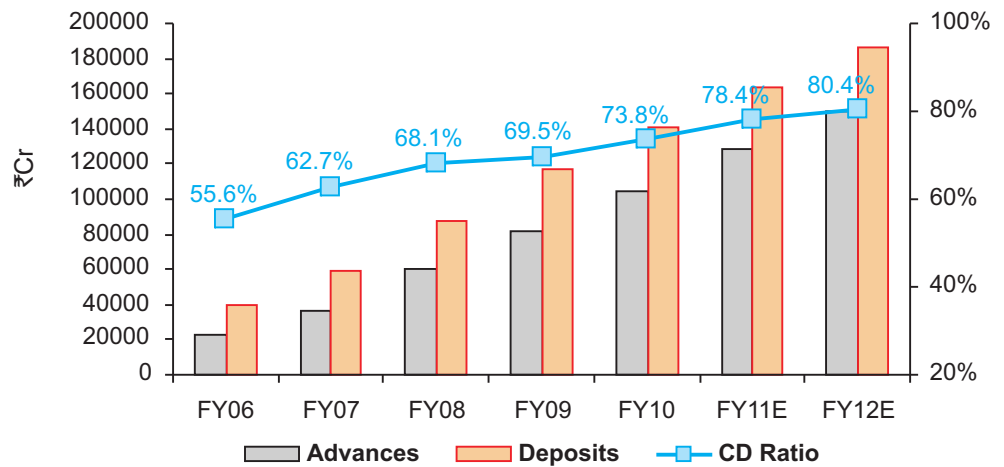


(Source: RBI & Keynote Capitals Institutional Research)

Increase in CD ratio more than the industry average indicates strong demand in credit disbursement compared to deposit mobilization. The same trend is expected to be continued in FY12E at 80.4%, leading to better yield on advances and improvement in utilization of funds.

Chart 2

Business Mix



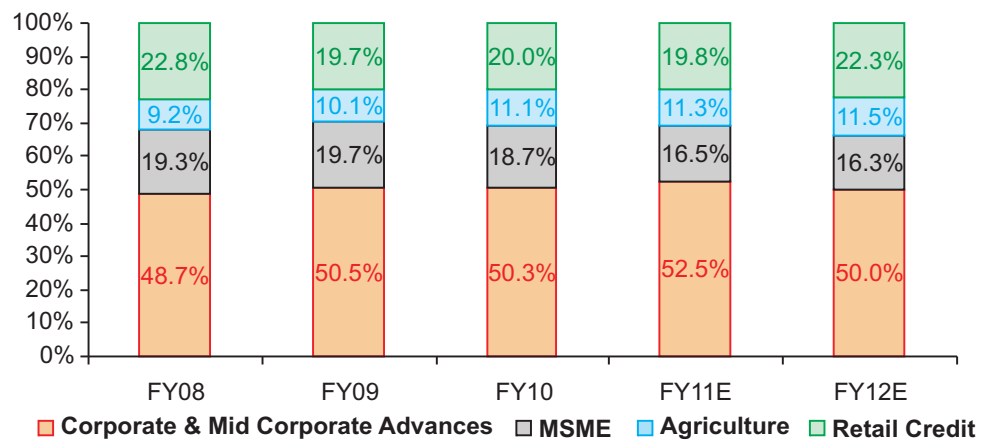
(E: Keynote Capitals Institutional Research Estimates)

The bank has a well-diversified loan book with large & mid corporate loan book accounting for 50% of the loan portfolio. It is seen from the past trend that its overall loan mix will not witness any significant change and will remain focused on growing its retail loan book in future. It is expected that its retail loan portfolio to increase ~22% by FY12E, on account of the surge in demand in retail credit within sectors like home loans, auto loans etc.

Chart 3

The bank is more focusing on loan book expansion in large and mid-corporate segment

Loan Book



(E: Keynote Capitals Institutional Research Estimates)

As of Sept-10, the share of corporate loans to the total portfolio increased to ~57% on account of the one-off lending to the telecom and infrastructure sector. Going forward it is expected that the share of corporate loans to the total portfolio will decrease and stabilize around 50%.

The Corporate, SME and Agriculture loan book is well diversified with maximum exposure in Financial companies of 12.7% followed by 11.6% in Infrastructure as of Dec-10. Out of the total Corporate advances of the bank, the high rated loan book constitutes around 73% as of Dec-10, having advantage of low risk through a diversified loan book.

Well diversified and high-rated loan book

Industry-wise exposure	Sep-10
Financial Companies	12.7%
Infrastructure	11.6%
Power Generation & Distribution	9.7%
Metal & metal products	7.9%
Engineering incl. electronics	6.1%
Telecommunication Services	5.0%
Trade	4.7%
Real estate	3.7%
Petrochemical & Petroleum Products	3.5%
Food processing	3.4%
Others	31.6%

(Source: Company & Keynote Capitals Institutional Research)

Amongst the leading new private players, Axis bank's Retail loans as percentage to gross Advances stands lowest at 19% at the end of Sept-10, and has highest proportion of home loans (secured loans), at 73%.

Retail and home loans of three largest new private banks

(₹Cr)

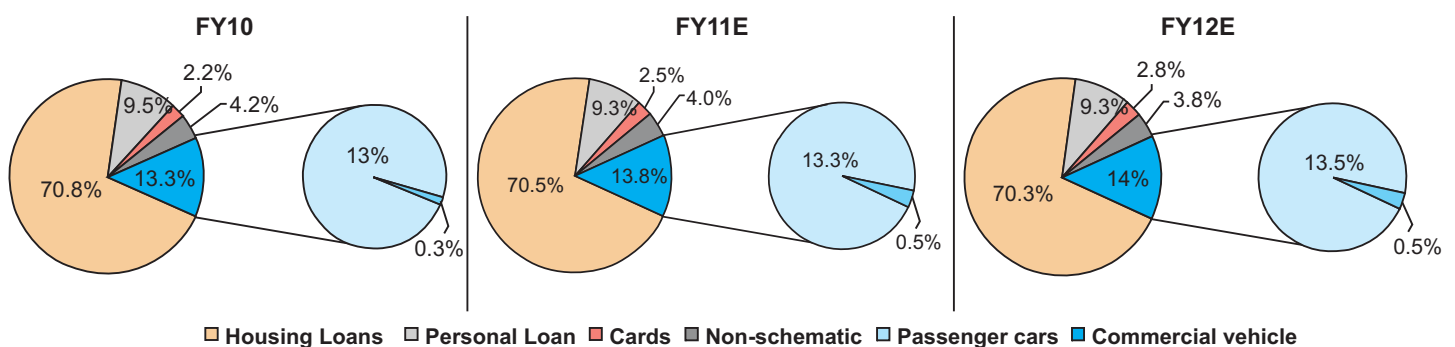
Particulars	Axis Bank			HDFC Bank			ICICI Bank		
	FY08	FY09	FY10	FY08	FY09	FY10	FY08	FY09	FY10
Retail Loans	13592	16052	20823	39327	61154	69994	131663	106972	77918
% to gross Advances	22.8%	19.7%	20.0%	58.1%	61.0%	55.0%	58.4%	49.0%	43.0%
Housing Loans	7747	10434	14743	-	3500	8700	68741	57765	46751
% to Retail loans	57.0%	65.0%	70.8%	-	5.7%	12.4%	52.2%	54.0%	60.0%

(Source: Company & Keynote Capitals Institutional Research)

Under the Retail loan category, auto loans have been consistently maintained at 13% between FY08-10. The bank's focus on secured loans i.e. housing and auto loans are likely to be enhanced.

Chart 4

Retail Loans break-up (%)



(E: Keynote Capitals Institutional Research Estimates)

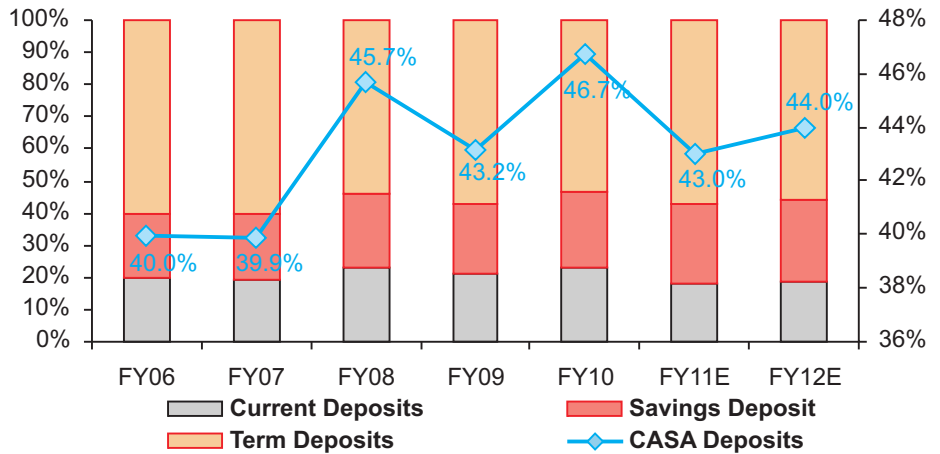
2. Deposit Mix:

During FY06-10, the bank's deposit grew at a CAGR of 34.8% (₹141300cr), current deposit at 35.1% (₹32167.7cr) and savings deposit grew at 47.3% (₹33861.8cr).

Chart 5

Branch expansion to strengthen the CASA ratio

Deposit Mix (%)



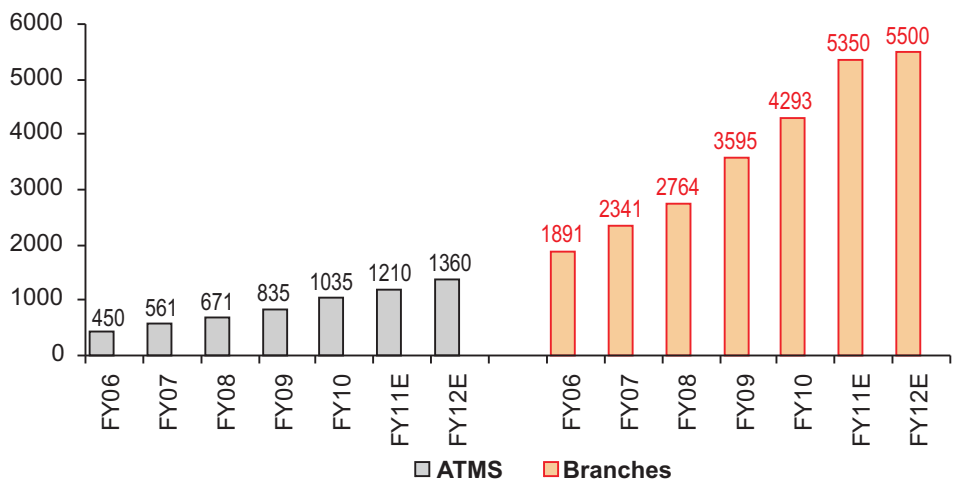
(E: Keynote Capitals Institutional Research Estimates)

CASA deposits grew at a CAGR of 40.5% stands at ₹66029.54cr over FY06-10, reporting a CASA ratio of 46.7% in FY10. It outpaced the CAGR growth of term deposit of 30.8% which stands at ₹75270.7cr for the same period. The management is continuously focusing on improving its CASA deposits and thereby reducing its cost of funds. Due to progress in Branch expansion activities, the remarkable achievement has been made in improving the CASA ratio.

The bank seize the opportunity to increase the business through expansion of distribution network to various customers whereby promote the Retail, Agriculture & SME segments including the sale of third party products. The Bank crossed a landmark in Mar-10 by opening its 1000th branch in Mumbai and is now present in all States and Union Territories (except Lakshadweep) and is pioneer in ATM sharing arrangements. The distribution network covers 734 centres in India and 4 centres in overseas as on Dec-10.

Chart 6

Network



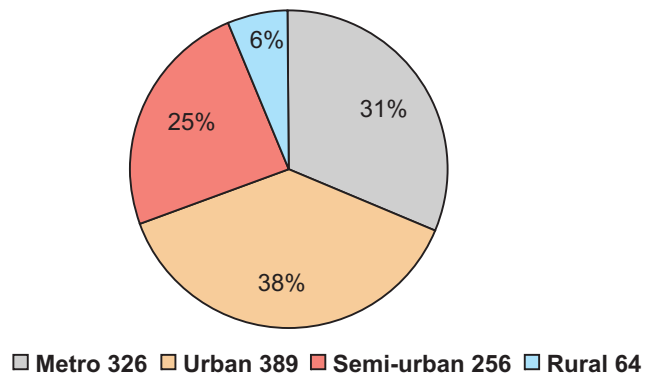
(E: Keynote Capitals Institutional Research Estimates)

Increase in branch and ATMs networking in domestic and overseas countries.

Further, the process of spreading to overseas network has already been initiated by opening foreign branches in major financial hubs in Asia i.e. Singapore, Hong Kong and Dubai, and representative offices at Shanghai and Dubai, and strategic alliances with banks and exchange houses in the Gulf Co-operation Council (GCC) countries. While the branches at Singapore, Hong Kong and DIFC-Dubai enable the bank to partner with Indian corporates doing business globally, the Dubai Representative Office and the arrangement with GCC based banks and exchange houses provides access to the NRI population. The Shanghai Representative Office apart from providing presence in the key market of China fulfills the regulatory requirement of establishing a branch in course of time to enhance the ability of the bank to tap business opportunities emanating from that region. As on Dec-10, the total assets works out to 4.59bn USD through overseas operations.

Chart 7

No of branches-FY10 (1035)



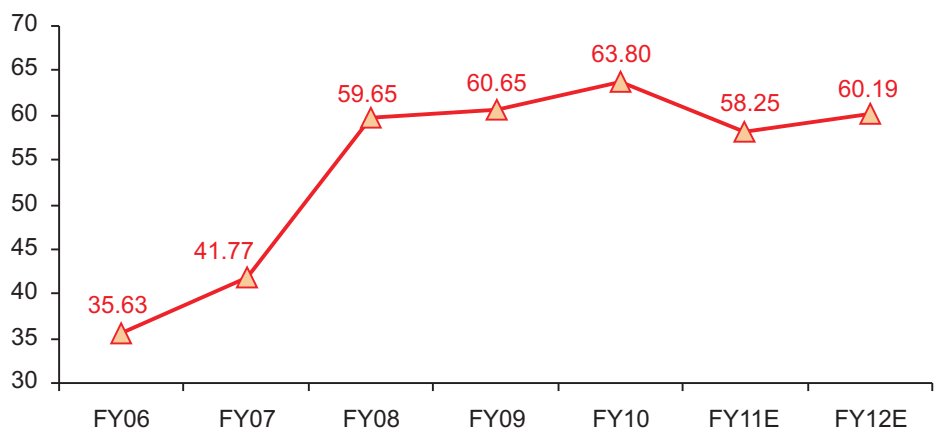
(E: Keynote Capitals Institutional Research Estimates)

During FY10, the bank has a network of 1027 branches and 8 extension counters and targets to add ~200 branches to its network in this fiscal, thereby supporting CASA growth in future which will reduce the overall cost of funds in an increasing interest rate cycle and support NIM. We expect CASA ratio to be sustained at ~44.5% and thus resulting an increase in CASA per branch in coming years.

Chart 8

Casa per branch (₹Cr)

Enhancement in CASA per branch in future



(E: Keynote Capitals Institutional Research Estimates)

Highest CASA per branch among the three largest bank:

Particulars	Axis Bank		HDFC Bank		ICICI Bank	
	FY09	FY10	FY09	FY10	FY09	FY10
CASA (₹Cr)	50643.7	66029.5	63359.7	87103.9	62667.8	84215.8
Branches	835	1035	1412	1725	1438	1741
Casa per branch (₹Cr)	60.65	63.80	44.87	50.50	43.58	48.37

(Source: Company & Keynote Capitals Institutional Research)

3. Net Interest Income and NIM:

The bank posted strong growth in NII at a CAGR of 46.9% stands at ₹5004.49cr during FY06-10, on account of robust growth in loans and advances. Enhancing NII will be continued for another few quarters inspite of rise in the cost/ average asset. The low proportion of retail loans has resulted better fee income to asset among its peers.

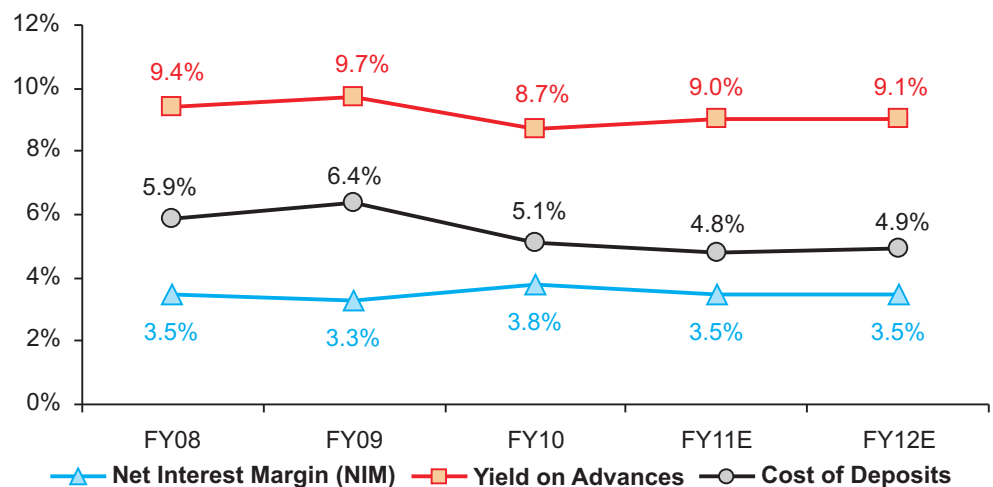
Particulars	Axis Bank		HDFC Bank		ICICI Bank	
	FY09	FY10	FY09	FY10	FY09	FY10
NII to average asset	2.9%	3.0%	4.7%	4.1%	2.1%	2.2%
Fee to average asset	1.9%	1.8%	1.9%	1.7%	1.7%	1.5%
Cost to average asset	2.2%	2.3%	2.6%	2.8%	1.8%	1.6%

(Source: Company & Keynote Capitals Institutional Research)

Chart 9

Return Ratios

NII growth and NIM expansion are likely to be key earnings drivers in FY12E.



(E: Keynote Capitals Institutional Research Estimates)

Savings deposits growth has been maintained above 30% during the past five quarters, supporting the rapid expansion in NIM. Higher CASA ratio and re-pricing of advances enabled the bank to reduce the cost of funds and increase the yields which supported NIM in FY10. The bank reported a NIM of 3.8% in FY10, 3.7% in 1QFY11 & 2QFY11 and 3.8% in 3QFY11. Increase in policy rates has led to the marginal increase in deposit rates and stable yield on advances due to adequate liquidity in the system, which will put some pressure on NIM in the short run. However, as demand for credit picks up, yield on advances will improve, as banks will be in a better position to be able to pass on the increase in interest rates to the borrowers. Furthermore, introduction of base rate will result in banks withdrawing the flow of advances to Corporates for the short term at lower interest rates, indicating an upward direction for lending rates. Hence, yields on advances are expected to pick up from the 2HFY11, enabling the bank to maintain its NIM guidance of 3.5% going forward.

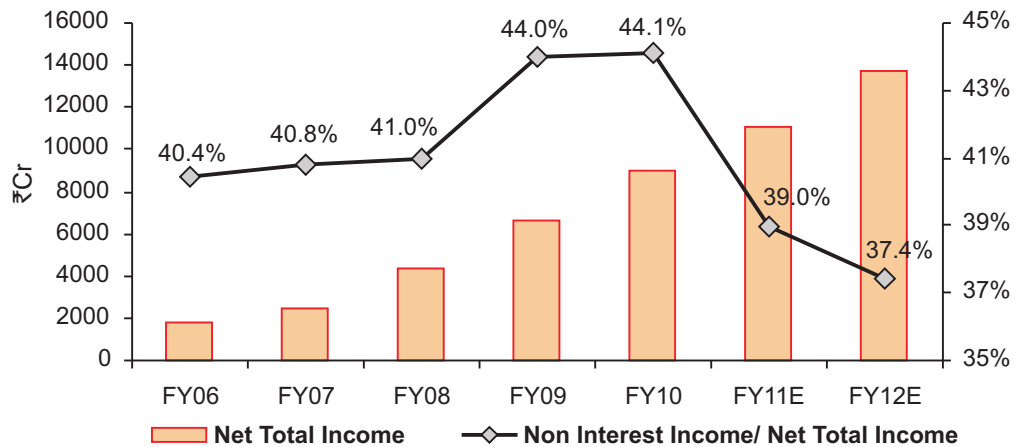
4. Earnings Quality:

a. Non-Interest income:

The bank's earnings are evenly distributed between core interest income and the non-interest income. Its non-interest income grew at a CAGR of 56.8% stands at ₹3945.78cr over FY06-10. Though the bank is maintaining its non-interest income as a proportion of total income above 40%, we may expect a marginal decrease due to more focus on core banking in coming years.

Chart 10

Return Ratios

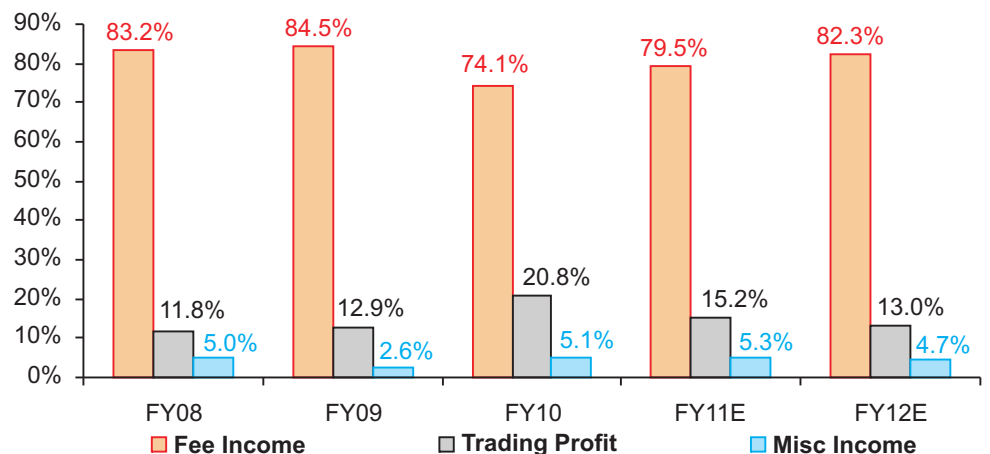


(E: Keynote Capitals Institutional Research Estimates)

The bank earns non-interest income from fee income and trading profits. It has developed a strong and diversified fee-income stream to complement its core lending operations and ensure less volatility in the overall fee-income. It has healthy deposits franchise and leadership position in debt syndication, augmenting its position to leverage the spread and fee-income opportunity from infrastructure and capex-related credit demand. In FY11, banks are likely to get negatively impacted due to rise in bond yields, which may lead to mark-to-market losses in the available for sale (AFS) and held for trading (HFT) portfolio. As of Dec-10, out of the total investment portfolio, the bank's AFS and HFT portfolio constitutes 36.6% and 3.3% respectively, making the investment portfolio susceptible to increase in yields. However, its less dependence on volatile treasury profits (constitutes only ~18% of the non-interest income) reflects the quality and stability of non-interest income.

Chart 11

Non-Interest Income break-up

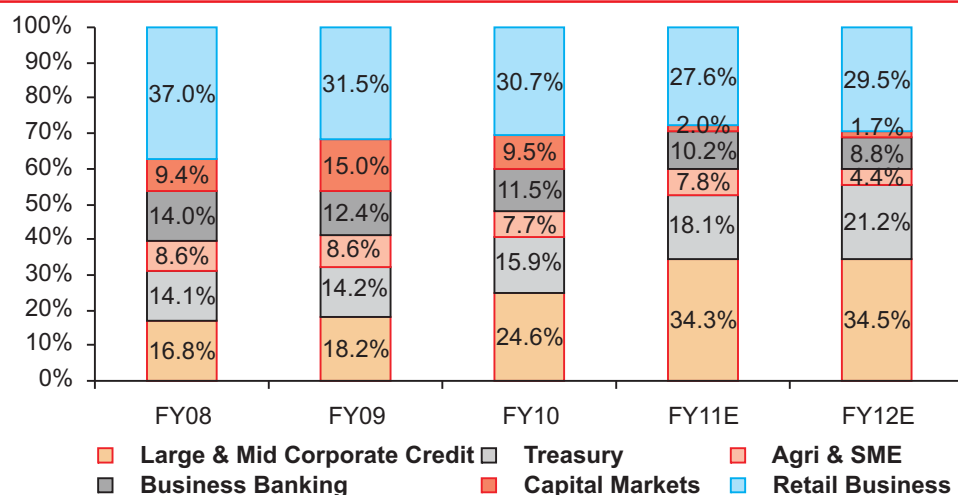


(E: Keynote Capitals Institutional Research Estimates)

The bank derives majority of its fee income from Large & Mid Corporate and Retail segments. In the corporate segment, fee income is generated from cash management services, forex services, merchant banking services and debt syndication. In the Retail segment, the bank earns fee income by selling third party products, processing fees, debit and credit cards. Also earns fee income from Treasury, Agriculture & SME Banking, Business Banking and Capital Market segments.

Chart 12

Fee Income break-up



(E: Keynote Capitals Institutional Research Estimates)

The fee income from Corporate and Retail business is expected to grow due to the various programmes undertaken by the bank which are as follows:

1. Restructuring of Retail Banking into two groups namely; Mass and Mass Affluent and Affluent segments in order to become more customer-centric, rather than product-centric.
2. Addressing the needs of the Mass Affluent segment and also to take the Priority Banking to a larger set of customers and locations. The Bank has set up 11 new Priority Lounges during FY10 (in 3 new centres) in the country.
3. Being the fourth largest debit card issuer in the industry with a base of 147 lac debit cards issued till 31 March 2010, it has designed 14 variants cards for different customer segments.
4. First to launch a Platinum Chip Debit Card in the country, and is presently offered exclusively to the Priority Banking customer segment. In the prepaid cards market, the Bank has attained a leadership position offering a bouquet of products suited to a variety of needs.
5. Focuses on distribution of third party products, with a special thrust on mutual funds and Bancassurance and is a leading distributor of mutual funds in the country, adding 90,000 new customers in FY10.
6. Continuing to retain its leadership position in the infrastructure debt market and syndication of debt issues.

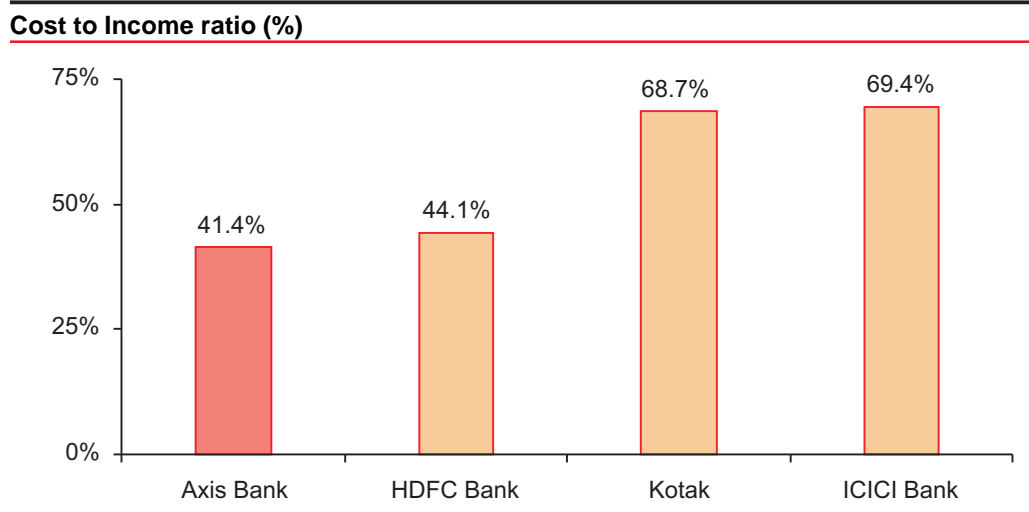
b. Rise in Operating expenses:

The bank managed to reduce the cost to income ratio (41.4%) over the years through implementation of CBS across its branches. Branch expansion plans in another couple of

years may stabilize the cost to income ratio at ~44%. However, it has maintained higher operating efficiency (measured by cost to income ratio) compared to its peers, enabling to increase its earning's quality.

Chart 13

Better cost efficiencies leading to increase in productivity ratios and profitability



(E: Keynote Capitals Institutional Research Estimates)

Hence, the healthier core business growth, increase in fee income and higher operating efficiency will lead to the better profitability in future.

5. Adequately capitalized to support earnings quality:

The bank is well capitalized and in a position to meet lending targets in coming years. It has been raising sufficient capital at regular intervals to ensure growth in its balance sheet. During FY10, the bank had undertaken a Qualified Institutional Placement (QIP), follow-on Global Depository Receipt (GDR) issue and preferential allotment to raise capital amounting to ₹3816.14cr and consequently increased its Capital Adequacy Ratio (CAR) in FY10. The infusion of Tier I capital would facilitate to raise Tier II capital in future, which will further reinforce CAR and enable the bank to grow its loan book and capitalize on emerging growth opportunities. At the end of 2QFY11, CAR stood at 13.68% and tier I ratio was 9.77%, well above the required regulatory limit.

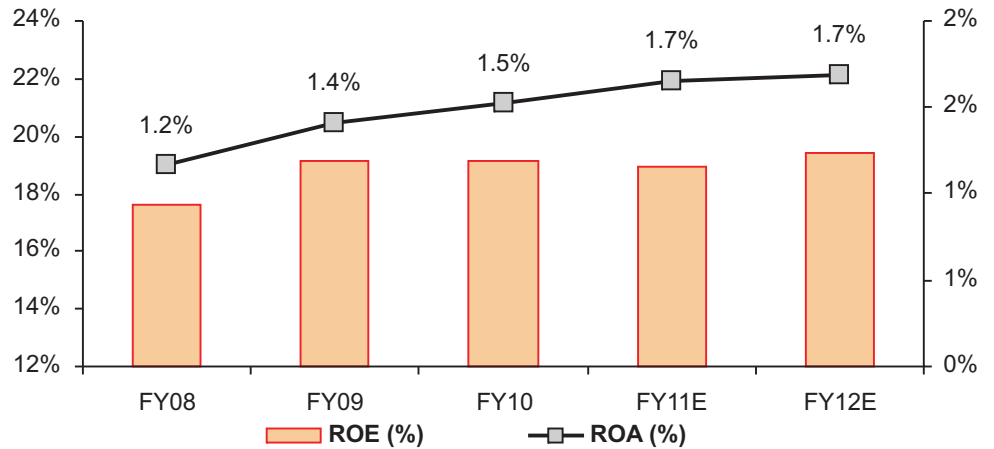
Capital Structure	FY06	FY07	FY08	FY09	FY10
Tier I Ratio	7.3%	6.4%	10.2%	9.3%	11.2%
Tier II Ratio	3.8%	5.2%	3.6%	4.4%	4.6%
Total Capital Ratio	11.1%	11.6%	13.7%	13.7%	15.8%

(Source: Company & Keynote Capitals Institutional Research)

The bank has a higher return on average equity (ROE) and return on average assets (ROA) of ~19.2% and 1.5% respectively, during the financial year ending 2010. In FY11, we expect ROA to sustain at this levels and ROE to decline marginally to 19.0% on account of slippages from restructured loan portfolio and dilution in equity following the capital raised worth ₹3816.14cr in 2QFY10. Nevertheless, we expect return ratios to improve in FY12 on growth momentum in loan book and higher margins.

Chart 14

Return Ratios (%)



(E: Keynote Capitals Institutional Research Estimates)

The potential in corporate loan growth and momentum in capital market enhance the fee income prospects to achieve the upturn in return ratios by the financial year ending 2012.

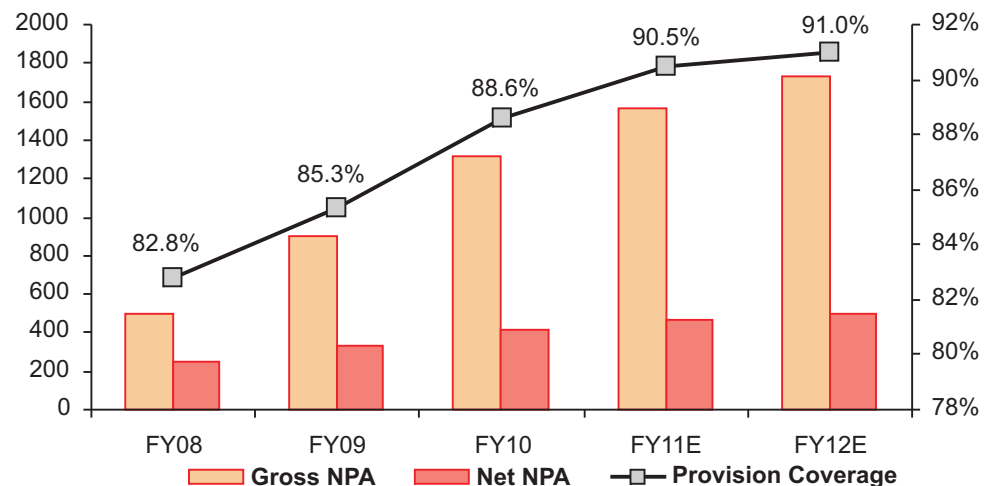
6. Stable Asset Quality:

The asset quality of the bank is comfortable with gross and net NPA ratios of 1.2% and 0.3% respectively, as of Dec-2010. Provision coverage stands at 91.4% including technical write-offs well above RBI's mandate of 70%. We expect the same to continue and the gross and net NPA ratio may be maintained around 1.2% & 0.3% respectively, in another couple of years.

Restructuring exercise paved the way to improve the asset quality

Chart 15

Asset Quality (₹Cr)



(E: Keynote Capitals Institutional Research Estimates)

Sequentially, the slippage ratio has broadly been declining to 1.7% in 2QFY11 from 2.2% in FY2010

The bank's restructured loan portfolio aggregates to ₹2286.10cr as on FY 2010 or 2.0% of gross advances. Of which, Large & Mid-Corporate credit comprises of 69.3%, SME and Agriculture loans consists of 21.1% and 6.1% respectively and Capital Markets comprises of 3.5%. The bank faces the risk of slippages from its restructured loan portfolio, particularly from the SME and agricultural segment which can improve the NPAs. The higher provision coverage will enable the bank to maintain the NPA levels going forward.

Segment-wise non-performing assets

(as of FY10)

Particulars	% of NPAs to total advances in that sector
Agriculture and allied activities	2.3%
MSME	1.0%
Services	0.7%
Personal Loans	1.9%

(Source: Company & Keynote Capitals Institutional Research)

7. Positive Synergies expected from tie-up with ENAM Securities Ltd in coming years:

Axis Bank has entered into an all-share deal worth ₹2067cr with one of India's leading financial services firm, Enam Securities Ltd, following which the investment banking, corporate advisory services and equity distribution business of the latter will be merged with the bank's wholly-owned subsidiary. As part of the deal, Enam Securities will enter into a five-year non-compete agreement with Axis Bank and the bank will have the right to use the Enam brand name for two years. However, ENAM will retain its AMC, PMS and insurance broking business and will be free to compete with Axis Bank.

The Key points of the deal are as follows:

- The Shareholders of Enam Securities will own 3.3% equity stake in Axis Bank post the deal.
- The Co-founder and Chairman of Enam Securities will get a position on the board of the bank as an independent director, while one the key Director of Enam Securities will become the MD & CEO of the new subsidiary.
- However, the deal required an approval of the Shareholders, Reserve Bank of India (RBI), the Securities and Exchange Board of India and the High Courts of Gujarat and Mumbai and is expected to be completed in 4-6 months.

The Synergies involved therein:

The bank is a dominant player in placement and syndication of debt issues and arranged debt aggregating ₹20330cr during 3QFY11. It was assessed by Prime Database as the No.1 Debt Arranger for the quarter ending June-10 and also by Bloomberg Underwriter league table for the period Jan-10 to Sep-10. Further, it was awarded the "Best Domestic Debt House in India" 2010 by Asiamoney and "Best Bond House in India" 2010 by Finance Asia and Euromoney. It lacks expertise in Institutional Broking and Investment Banking and was low on the league tables whereas Enam bagged the third place with a market share of 9.3% in the Indian domestic equity and rights issuances as per the Bloomberg league table for FY2010. Hence, with this deal, it will take over one of the top-three domestic firms in the primary equity issuance space.

The bank's wide distribution platform of almost 1088 branches and Enam's retail network will lead to an opportunity to build a leading retail franchise. The planned objective behind the deal is to expand its product and service offerings for corporate, institutional and individual clients, thereby enhancing the ability of the entity to serve client needs in a flawless manner across product categories and geographies. Hence, the merger is expected to bring positive synergies and will also help the bank to increase its fee income.

Financial Analysis:

Majority of the bank revenue is from the corporate segment followed by retail segment. The acquisition of the assets of Enam Securities will allow it to offer a complete portfolio of financial services to its clients, thus helping it to increase its revenue. For FY10, total

income of the businesses being acquired from Enam Securities stood at ₹242cr, with PBT of ₹92cr. From Apr-Oct, 2010, total income stood at ₹182cr, with PBT of ₹77cr. On an annualized basis, FY11 PAT works out to ~₹90cr, implying valuations of 22.97x FY11E earnings, which is at 39% premium to the listed brokerage companies (peers), on 1HFY11 annualized PAT basis.

Particulars	Market cap	Annualized PAT		P/E (x)	
		FY10	FY11E	FY10	FY11E
Edelweiss Capital	4380.33	229.20	254.92	19.11	17.18
India Infoline	3241.30	231.99	194.56	13.97	16.66
Motilal Oswal Fin.	2613.40	170.45	170.00	15.33	15.37
Total	10235.03	631.64	619.48	16.20	16.52
Enam Securities	2067.00	69.00	90.00	29.96	22.97
Premium (%)					39.0%

Source: Company & Keynote Capitals Institutional Research
(As on 18th Nov-10)

The impact of the deal is neutral for bank's capital adequacy and will have limited impact on its EPS as the merger is just ~3.3% of the market capitalization of the bank. As a part of the deal, 400 employees and net current assets worth ₹300cr of Enam will be transferred to the bank.

Particulars	Pre-Deal		Post-Deal	
	FY11E	FY12E	FY11E	FY12E
EPS (₹)	80.11	95.33	80.11	93.37
Adj. Book Value (₹)	442.57	515.97	442.57	505.52

E: Keynote Capitals Institutional Research Estimates

Other information

1. a) Axis Bank: Shareholding Pattern

Shareholding Pattern:	FY08	FY09	FY10	Dec-10
SUUTI	27.2%	27.1%	24.0%	23.7%
LIC	10.4%	10.4%	10.3%	9.6%
FII's	33.9%	23.4%	33.1%	36.6%
Others	28.5%	39.1%	32.6%	30.1%

(Source: Company & Keynote Capitals Institutional Research)

b) More than 1% holdings

(Dec-2010)

Name of the Shareholder	No of shares	% of Holding
Deutsche Securities Mauritius Ltd	9555860	2.3%
Genesis Indian Investment Company Ltd - General Sub Fund	9786478	2.4%
HSBC Bank Mauritius Ltd A/c Cinnamon Capital Ltd	19812210	4.8%
HSBC Bank Mauritius Ltd A/c HSBC IRIS Investments Mauritius Ltd	19609210	4.8%
ICICI Prudential Life Insurance Company Ltd	11073569	2.7%
Swiss Finance Corporation (Mauritius) Ltd - HSBC Securities Services	4325034	1.1%

2. Dividend History

Year End	FY05	FY06	FY07	FY08	FY09	FY10
Dividend-Amount	76.66	97.54	126.73	214.63	359.01	486.22
Dividend-%	28.0%	35.0%	45.0%	60.0%	100.0%	120.0%

(Source: Company & Keynote Capitals Institutional Research)

Risks and Concerns:

- Restructuring exercise in lending to different verticals under RBI's guidelines may lead to increase in NPAs and thus affecting the bank's asset quality. And increase in number of accounts turning into NPA's from the restructured portfolio would lead to increase in provisioning amount, having a negative impact on the profits.
- The bank can face stiff competition from other private banks and might reduce its market share in future.

Sector Outlook:

During 1HFY11, the Industry has achieved ~35% of the total expected credit off-take for this fiscal (assuming 20% credit growth for FY11) and is expected to improve in H2FY11 on account of sharp increase in short term rates, increase in commodity prices as well as Crude touching 90 US \$ per barrel coupled with rural demand. On the other hand, hike in deposits rate by most of the banks may lead to enhancement in deposit mobilization going forward. The current incremental CD ratio of the banking system is hovering around 75%, which indicates relatively strong demand in credit disbursement compared to deposit mobilization and we expect the increase for coming years as well due to strong economic activities.

Total Business Growth outlook:

(₹Cr)

Particulars	Deposit	Credit	CDRatio
Total Business as on Mar-10	4486574	3193906	71.2%
% Growth as per RBI Target	18.0%	20.0%	
Expected business as on Mar-11	5294157	3832687	72.4%
Less: Achieved in 1HFY11 (as on Sep-10)	4775300	3414487	71.5%
% Growth (YTD)	6.4%	6.9%	
Incremental Business for 2HFY11	518857	418200	80.6%

Source: RBI & Keynote Capitals Institutional Research

Investment book comparison of banks states that the current rise in yields beyond 8% will result in MTM losses for banks and PSU banks will have to provide for the same. Treasury gains are not seen in the next couple of quarters leading to non interest income of banks growing in line with business only. Most banks witnessed margin expansion during Q2FY11 on the back of increased PLRs along with increase in CASA ratio. However, margins are likely to witness some pressures on account of recent increase in the cost of deposit along with higher term deposit rates. On account of availability of the cheaper sources of funds and the new base rate system, there has been an increased activity in the commercial paper and external borrowings market. However, the scenario is now changing, as with the rising interest rates, CP rates are now closer to the base rate as against the case earlier, thereby leaving no scope of arbitrage for companies to raise funds through these alternative channels. Branch expansion by most of the banks, pension liabilities and restructuring of loan book resulting in higher provisioning is expected to impact more on public sector banks compared to private sector bank's earnings growth in H2FY11.

Monetary/Liquidity Scenario:

Faster credit growth has put pressure on the liquidity of Banks. In FY11, this scenario is likely to be seen as the high inflation rate has dissuaded investors to park their funds with banks, resulting in low deposit growth. The RBI recent Mid-Quarter Monetary Policy Review (Dec-10) has supported for additional liquidity measures to sustain growth in credit off take and maintain the growth momentum.

1. Repo rate, reverse repo rate were retained at 6.25% and 5.25% respectively.

2. The cash reserve ratio (CRR) maintained at 6.0% of net demand and time liabilities (NDTL) of scheduled banks.
3. Statutory liquidity ratio (SLR) of scheduled commercial banks (SCBs) reduced to 24% from 25% of their NDTL with effect from December 18, 2010.
4. Open market operation (OMO) auctions will be conducted for purchase of government securities for an aggregate amount of ₹48,000cr in the next one month.
5. Reduction in government borrowings to ₹6000cr as against ₹11000cr per week.

Future Outlook:

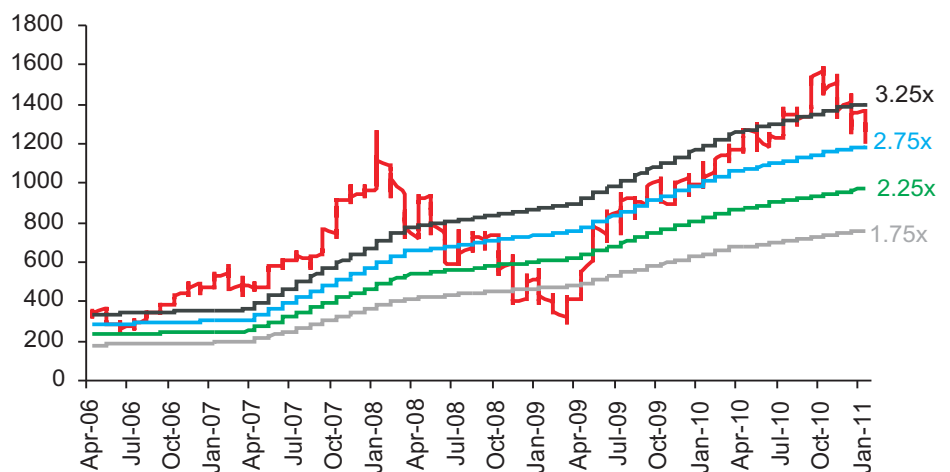
In FY11, the economy is expected to face stiff interest rates as inflation still hovers much over the estimated levels and liquidity getting weaker due to larger than expected credit growth, lower deposit growth and increased government borrowing. Going ahead, deposit rate increase, asset quality deterioration, inflation etc might impact banks negatively. Hence, we continue to remain cautious and any decline will be an opportunity for investment at one year horizon.

Valuations:

The bank's total business, multiple sources of sustainable fee-income, distribution network and vast customer base in CASA-franchise enable it to leverage significant business opportunities in the current rising interest rate scenario. This along with a balanced loan portfolio and high proportion of low-cost funds will help the bank to earn better margins compared to its peers. Considering the above factors, we initiate coverage on the stock arriving at a target price of ₹1415 per share by assigning a multiple of 2.8x FY12E price to adjusted book for the period of one year, with a 'Buy' recommendation. At CMP of ₹1227.55, the stock is trading at 3.2x FY10 price to adjusted book and is expected to trade at 2.8x FY11E and 2.4x FY12E price to adjusted book.

Chart 16

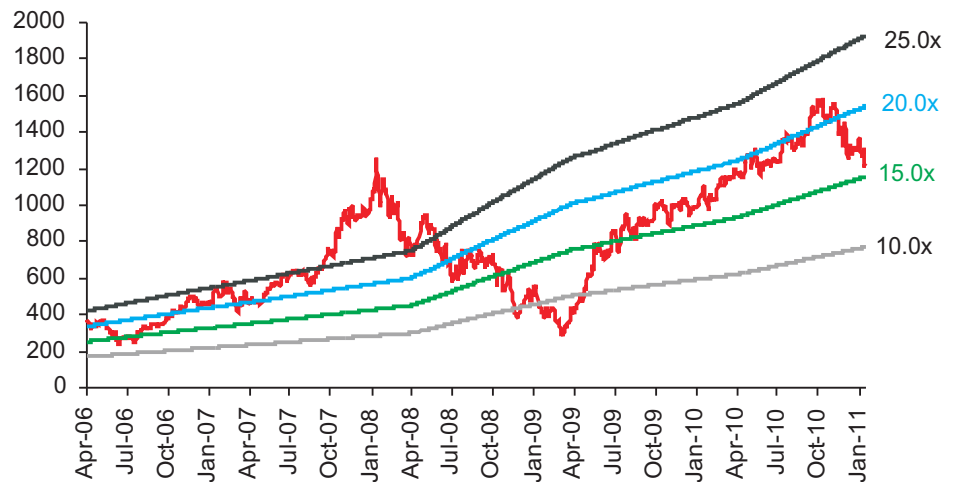
P/ABV Bands



(Source: Keynote Capitals Institutional Research)

Chart 18

PE Bands



(Source: Keynote Capitals Institutional Research)

Peer Comparisons:

Key Operating parameters of Peer Group (FY10)

(₹Cr)

Particulars	Axis Bank	HDFC Bank	ICICI Bank	Kotak
Net worth	16044.61	21519.58	51296.50	7910.94
Deposits	141300.22	167297.78	241572.30	21819.18
Advances	104343.12	126162.73	225778.13	29724.29
Total Income	15583.80	20270.00	59599.77	10108.93
Net Profit	2514.53	3003.65	4670.29	1307.00
NPM	16.1%	14.8%	7.8%	12.9%
EPS	62.06	63.62	39.84	18.77
Book Value	396.00	472.23	460.10	227.23
NIM (%)	3.8%	4.3%	2.5%	6.3%
Cost to income ratio	41.4%	44.1%	69.4%	68.7%
ROAA (%)	1.5%	1.5%	1.1%	1.7%
ROANW (%)	19.2%	16.5%	9.7%	13.3%
Gross NPAs (%)	1.3%	1.4%	4.2%	2.6%
Net NPAs (%)	0.4%	0.3%	1.7%	1.2%
Provision Coverage Ratio	88.6%	74.8%	59.5%	58.0%
Capital Adequacy Ratio	15.8%	17.4%	19.4%	18.4%
Business per employee (₹)	11.36	5.90	10.29	4.87
Market Price (₹)	1227.55	2075.30	1000.70	403.15
Market Capitalization	49736.64	94994.78	111567.04	14035.26
Paid up equity capital	405.17	457.74	1114.89	348.14

Source: Company & Keynote Capitals Institutional Research

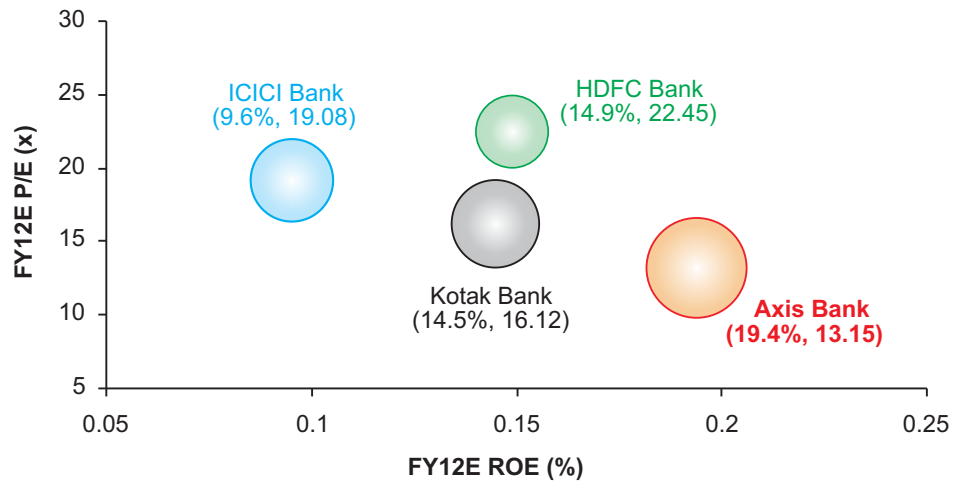
Forward Valuations:

Peers	P/E (x)		P/ABV (x)		ROE (%)	
	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Axis Bank	15.32	13.15	2.77	2.43	19.0%	19.4%
HDFC Bank	25.23	22.45	3.88	3.34	15.5%	14.9%
ICICI Bank	21.18	19.08	1.99	1.83	9.4%	9.6%
Kotak Bank	18.20	16.12	3.01	2.75	15.0%	14.5%

E: Keynote Capitals Institutional Research Estimates

Chart 18

Heading



(Source: Keynote Capitals Institutional Research)

Quarterly Performance Trends:

(₹Cr)

Particulars	Q1-FY10	Q2-FY10	Q3-FY10	Q4-FY10	Q1-FY11	Q2-FY11	Q3-FY11
Interest Earned	2905.56	2860.36	2883.65	2988.45	3325.59	3624.25	3838.31
Interest on advances	1973.56	1950.19	1987.88	2074.97	2310.89	2429.03	2600.55
Income from Investment	867.31	859.56	845.43	856.01	935.26	1123.54	1166.83
Interest on RBI balances & others	35.43	30.02	27.35	27.20	32.48	38.37	48.18
Others	29.26	20.59	22.99	30.27	46.96	33.31	22.75
Interest expended	1859.93	1710.68	1534.54	1528.38	1811.82	2009.15	2105.19
Net Interest Income	1045.63	1149.68	1349.11	1460.07	1513.77	1615.10	1733.12
Non-Interest Income	958.57	1065.58	988.09	933.54	1000.78	1033.24	1147.71
Net Total Income	2004.20	2215.26	2337.20	2393.61	2514.55	2648.34	2880.83
Operating Expenses	827.84	909.51	962.57	1009.80	1064.50	1161.99	1222.35
Staff costs	309.33	304.20	308.54	333.75	416.42	405.30	396.16
Other expenses	518.51	605.31	654.03	676.05	648.08	756.69	826.19
Pre-provisioning profit (PPP)	1176.36	1305.75	1374.63	1383.81	1450.05	1486.35	1658.48
Provisions and Contingencies	315.29	498.89	373.14	201.87	333.00	378.76	313.88
PBT	861.07	806.86	1001.49	1181.94	1117.05	1107.59	1344.60
Tax	299.03	275.22	345.51	417.07	375.17	372.45	453.24
PAT	562.04	531.64	655.98	764.87	741.88	735.14	891.36
EPS (₹)	13.87	13.12	16.19	18.88	18.31	18.14	21.75
Paid-up Equity Share Capital	278.69	281.63	357.71	359.01	405.17	409.90	409.90
% Gross NPAs to Gross Advances	1.2%	1.4%	1.4%	1.3%	1.2%	1.2%	1.2%
% Net NPAs to Net Advances	0.5%	0.5%	0.5%	0.4%	0.4%	0.4%	0.3%

Source: Company & Keynote Capitals Institutional Research

Financials

Profit & Loss Statements

(₹Cr)

Particulars	FY08	FY09	FY10	FY11E	FY12E
Interest Earned	7005.31	10835.48	11638.02	14981.56	18233.00
Interest on advances	4745.65	7465.86	7986.60	10234.09	12234.69
Income from Investment	2102.31	3051.50	3428.31	4456.64	5745.14
Interest on RBI balances & others	107.64	210.19	120.00	169.62	166.22
Others	49.71	107.93	103.11	121.22	86.95
Interest expended	4419.96	7149.27	6633.53	8196.51	9639.75
Net Interest Income	2585.35	3686.21	5004.49	6785.06	8593.25
Non-Interest Income	1795.49	2896.88	3945.78	4332.28	5143.91
Net Total Income	4380.84	6583.09	8950.27	11117.34	13737.16
Operating Expenses	2154.92	2858.21	3709.72	4762.81	5978.88
Staff costs	670.25	997.66	1255.82	1658.06	2150.24
Other expenses	1484.67	1860.55	2453.90	3104.75	3828.64
Pre-provisioning profit (PPP)	2225.92	3724.88	5240.55	6354.53	7758.28
Provisions and Contingencies	579.64	939.68	1389.19	1403.96	1835.46
PBT	1646.28	2785.20	3851.36	4950.56	5922.83
Tax	575.25	969.84	1336.83	1667.06	2015.12
PAT	1071.03	1815.36	2514.53	3283.51	3907.71
EPS (₹)	29.94	50.57	62.06	80.11	93.37
Book Value (₹)	245.13	284.53	396.00	453.82	517.49
Adjusted Book Value (₹)	238.19	275.41	385.66	442.57	505.52

(E - Keynote Capitals Institutional Research Estimates)

Balance Sheets

(₹Cr)

Particulars	FY08	FY09	FY10	FY11E	FY12E
Sources of Funds					
Paid-up Equity Share Capital	357.71	359.01	405.17	409.90	418.54
Reserves	8410.79	9855.79	15639.44	18192.37	21240.38
Net Worth	8768.50	10214.80	16044.61	18602.27	21658.92
Deposits	87626.22	117374.11	141300.22	163908.26	186035.87
Borrowings	5624.04	15519.87	17169.55	24035.17	29657.76
Other Liabilities & Provisions	7606.91	4650.07	6166.15	5028.38	6075.89
Total Liabilities	109625.67	147758.85	180680.53	211574.07	243428.44
Applications of Funds					
Cash & Balances with RBI	7305.66	9419.21	9473.88	11063.81	12248.04
Bal with Banks & money at call	5198.58	5597.69	5732.56	6867.19	6998.88
Investments	33705.10	46330.35	55974.81	62285.14	71623.81
Advances	59661.15	81556.76	104343.12	128488.92	149564.34
Fixed Assets	922.85	1072.89	1222.42	1318.78	1368.08
Other Assets	2832.33	3781.95	3933.74	1550.23	1625.28
Total Assets	109625.67	147758.85	180680.53	211574.07	243428.44

(E - Keynote Capitals Institutional Research Estimates)

Return Ratios (%)

	FY08	FY09	FY10	FY11(E)	FY12(E)
Net Interest Margin (NIM)	3.5%	3.3%	3.8%	3.5%	3.5%
Yield on Advances	9.4%	9.7%	8.7%	9.0%	9.1%
Yield on Investments	6.9%	7.6%	6.7%	7.5%	8.6%
Cost of Deposits	5.9%	6.4%	5.1%	4.8%	4.9%
Return on Average Assets	1.2%	1.4%	1.5%	1.7%	1.7%
Return on Average Net worth/ROAE	17.6%	19.1%	19.2%	19.0%	19.4%
Dividend Yield (%)	0.5%	0.8%	1.0%	1.2%	1.4%
Effective tax rate	34.9%	34.8%	34.7%	33.7%	34.0%

(E: Keynote Capitals Institutional Research Estimates)

Efficiency Ratios (%)

	FY08	FY09	FY10	FY11(E)	FY12(E)
Net Interest Income/ Net total Income	59.0%	56.0%	55.9%	61.0%	62.6%
Non Interest Income/ Net total Income	41.0%	44.0%	44.1%	39.0%	37.4%
Interest expended/ Interest earned	63.1%	66.0%	57.0%	54.7%	52.9%
Cost to income	49.2%	43.4%	41.4%	42.8%	43.5%
Opex/ Avg. assets	2.4%	2.2%	2.3%	2.4%	2.6%
Credit Deposit ratio (C-D ratio)	68.1%	69.5%	73.8%	78.4%	80.4%
Incremental C-D ratio	79.0%	73.6%	95.2%	106.8%	95.2%
Investment Deposit ratio (I-D ratio)	38.5%	39.5%	39.6%	38.0%	38.5%
Incremental I-D ratio	23.6%	42.4%	40.3%	27.9%	42.2%
Credit/ Assets	54.4%	55.2%	57.8%	60.7%	61.4%
Loan growth	61.8%	36.7%	27.9%	23.1%	16.4%
Deposits/Assets	79.9%	79.4%	78.2%	77.5%	76.4%
Deposit growth	49.1%	33.9%	20.4%	16.0%	13.5%

(E: Keynote Capitals Institutional Research Estimates)

Per share Data

	FY08	FY09	FY10	FY11(E)	FY12(E)
EPS (₹)	29.94	50.57	62.06	80.11	93.37
Book Value (₹)	245.13	284.53	396.00	453.82	517.49
Adjusted Book value (₹)	238.19	275.41	385.66	442.57	505.52

(E: Keynote Capitals Institutional Research Estimates)

Valuation ratios (%)

	FY08	FY09	FY10	FY11(E)	FY12(E)
P/e (x)	41.00	24.28	19.78	15.32	13.15
P/BV (x)	5.01	4.31	3.10	2.70	2.37
P/ABV (x)	5.15	4.46	3.18	2.77	2.43

(E: Keynote Capitals Institutional Research Estimates)

Growth ratios (%)

	FY08	FY09	FY10	FY11(E)	FY12(E)
Adjusted Book value	114.5%	15.6%	40.0%	14.8%	14.2%
Advances	61.8%	36.7%	27.9%	23.1%	16.4%
Deposits	49.1%	33.9%	20.4%	16.0%	13.5%
Investments	25.3%	37.5%	20.8%	11.3%	15.0%
Net interest income	73.2%	42.6%	35.8%	35.6%	26.6%
Non-interest Income	82.1%	61.3%	36.2%	9.8%	18.7%
Net total Income	76.8%	50.3%	36.0%	24.2%	23.6%
Pre-provisioning profit	76.1%	67.3%	40.7%	21.3%	22.1%
Net profit	62.5%	69.5%	38.5%	30.6%	19.0%
EPS	28.0%	68.9%	22.7%	29.1%	16.6%

(E: Keynote Capitals Institutional Research Estimates)

Productivity ratios (%)

	FY08	FY09	FY10	FY11(E)	FY12(E)
No. of employees (Avg)	12765	18117	21621	24864	27848
% growth	47.0%	41.9%	19.3%	15.0%	12.0%
No. of branches	671	835	1035	1210	1360
% growth	19.6%	24.4%	24.0%	16.9%	12.4%
No. of ATMs	2764	3595	4293	5350	5500
% growth	18.1%	30.1%	19.4%	24.6%	2.8%
Total Business (₹Cr)	147287	198931	245643	292397	335600
% growth	54.0%	35.1%	23.5%	19.0%	14.8%
Business per employee (₹Cr)	11.54	10.98	11.36	11.76	12.05
Business per branch (₹Cr)	219.50	238.24	237.34	241.65	246.76
Cost per employee (₹Cr)	0.17	0.16	0.17	0.19	0.21
Cost per branch (₹Cr)	3.21	3.42	3.58	3.94	4.40
Net Profit per employee (₹Cr)	0.08	0.10	0.12	0.13	0.14
Net Profit per branch (₹Cr)	1.60	2.17	2.43	2.71	2.87

(E: Keynote Capitals Institutional Research Estimates)

Asset quality

	FY08	FY09	FY10	FY11(E)	FY12(E)
Gross NPA (₹Cr)	494.61	897.77	1318.00	1564.45	1726.45
Net NPA (₹Cr)	248.29	327.13	419.00	461.51	500.67
Gross NPA ratio	0.8%	1.1%	1.3%	1.2%	1.2%
Net NPA ratio	0.4%	0.4%	0.4%	0.4%	0.3%
Provision Coverage	82.8%	85.3%	88.6%	90.5%	91.0%

(E: Keynote Capitals Institutional Research Estimates)

Asset Liability

	FY08	FY09	FY10	FY11(E)	FY12(E)
Credit-Deposit ratio	68.1%	69.5%	73.8%	78.4%	80.4%
Investment/Deposit	38.5%	39.5%	39.6%	38.0%	38.5%
Proportion of CASA deposits	45.7%	43.1%	46.7%	43.0%	44.0%

(E: Keynote Capitals Institutional Research Estimates)

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