देना बैंक
DENA BANK

NIRMAL BANG
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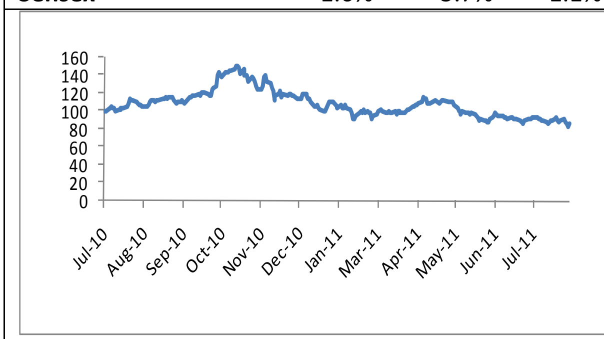
Initiating Coverage — Dena Bank Ltd

Recommendation	**BUY**
CMP (01/08/2011)	**Rs. 85**
Target	**Rs. 129**
Sector	**Banking**

Stock Details

BSE Code	532121
NSE Code	DENABANK
Bloomberg Code	DBNK IN
Market Cap (Rs. Crs)	2,848
Free Float (%)	42.0
52- wk HI/Low	151/79
Avg. volume BSE (Quarterly)	248165
Face Value (Rs.)	10
Dividend (FY 2011)	22%
Shares o/s (in Crs)	33.44

Relative Performance	1 Mth	3 Mth	1 Yr
Dena Bank	-4.5%	-21.5%	-14.0%
Sensex	-1.6%	-5.7%	1.1%



Shareholding Pattern as on 30/06/2011

Promoters Holding	58.01%
FII, Banks & Institutions	21.54%
Corporate Bodies	4.56%
Public & others	15.89%

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Snapshot

Dena bank is a Government owned bank with its head office located in Mumbai. The bank has a network of 1297 branches, 507 ATMs and 12 extension counters as on 30th June 2011 with a total business of Rs.103,973 crs. The bank is mainly concentrated in the Gujarat state (approximately 41% of total branches) and has a major presence in rural area. Out of its total branches, ~56% are in rural and semi-urban areas.

Investment Rationale

Focus on high yielding assets:

Dena Bank's loan portfolio has historically been inclined towards corporate lending which contributed above 50% of the total advances. However, the bank has now shifted its focus more on SME & Retail segment to exploit the potential in these high yielding segments. The bank is targeting a 25% growth in its retail portfolio for FY12E.

Strong CASA:

Dena Bank's strength lies in having strong concentration of branches in the CASA rich western regions of the country. On account of having a strong branch network, Dena Bank has been able to register one of the highest CASA ratios among the PSU banks. Management continues to focus on CASA share by increasing the client base by 20% in FY12E.

Protection of NIMs:

With increasing interest rates and cost of deposits, NIMs is expected to remain under pressure. However, Management in confident that the bank will be able to maintain NIMs to around 3% for 12E. We have factored in a 20 bps decline in NIMs. Going forward, we expect NII to grow at CAGR of ~16.4% for FY11-FY13E resulting from higher CASA deposits, focus on retail and SME portfolio and availability of adequate capital.

Asset quality to remain a cause of concern in near term:

Asset quality has been a concern for Dena Bank. In near term, exposure to power sector and migration to system based NPA recognition can have an impact on the bank's asset quality. We have factored in higher provisions in FY12E. However, we believe that the bank will see an improvement in the long term with regards to its asset quality, on back of recoveries and steps taken to contain fresh slippages by way of constant monitoring.

Valuation & Recommendation

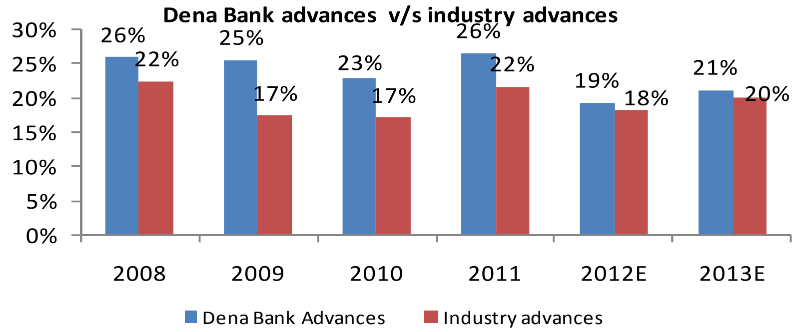
At CMP of Rs 85, the stock is trading at 0.8x of its FY12E ABV and 0.68x its FY13E ABV whereas on PE it is trading at 4.19x and 3.49x in FY12E and FY13E respectively. Looking at the historical trend we value it at 1.2x P/ABV of FY12E. Based on our estimated book value of Rs.108 per share for FY 2012E and P/ABV target multiple of 1.2x we arrive at a target price of Rs.129. **We recommend BUY on the stock with target price of Rs.129 indicating a potential upside of 50%**

Year	NII (Rs. Crs)	Growth %	Profit before provisioning (Rs. Crs)	Margin %	PAT (Rs. Crs)	EPS (Rs)	P/E (x)	Adj. BVPS (Rs.)	P/ABV (x)	ROE %
FY 10A	1,100	3.1%	841	49.8%	511	17.82	4.79	73.0	1.17	21.4%
FY 11A	1,763	60.3%	1,224	53.3%	612	18.34	4.66	92.0	0.93	19.5%
FY 12E	2,017	14.4%	1,480	56.0%	679	20.37	4.19	107.1	0.80	17.2%
FY 13E	2,390	18.5%	1,768	56.5%	816	24.48	3.49	126.2	0.68	17.8%

Investment Rationale

Sustained growth above industry average

Dena bank has been able to sustain growth in advances above industry average. The bank's advances have grown at a CAGR of 25% over FY07-FY11 compared to 20% CAGR growth in the industry. Going forward we expect advances to grow at CAGR of 20.5% for FY11-FY13E.



Source: Company data, RBI, Nirmal Bang Research

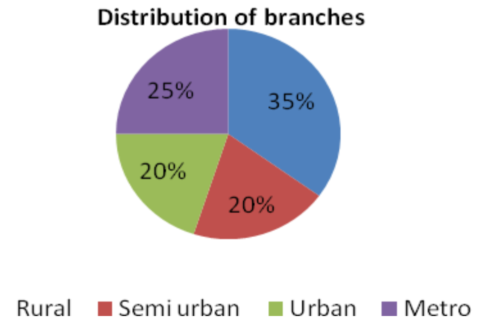
As per Mckinsey & Co's report dated 26th March 2011, the state of Gujarat has witnessed growth at the rate of 11% in 2011 as compared to the all Indian growth average of 9%.During the period 2005-2010, the real GDP growth in Gujarat has been 11.3% which is the highest amongst the other states in India. Dena Bank has major presence in the state of Gujarat (approximately 41% of the total branches are located in Gujarat. We believe that the higher exposure in Gujarat state will help the bank in garnering higher CASA and enjoy a better advances growth.

Change in mix: Focus on high yielding assets:

Dena Bank's loan portfolio has historically been inclined towards corporate lending which contributed above 50% of the total advances. However, the bank has now shifted its focus more on SME & Retail segment to exploit the potential in these high yielding segments. Currently, the agriculture, SME & Retail contributes approximately 43% of the current loan book. The retail portfolio grew by 14%, SME by 20% and Agricultural loans grew by 32% in FY11. We believe that growth in the bank's advances will be achieved from high yielding SME & Retail portfolio. The bank is targeting a 25% growth in its retail portfolio for FY12E.

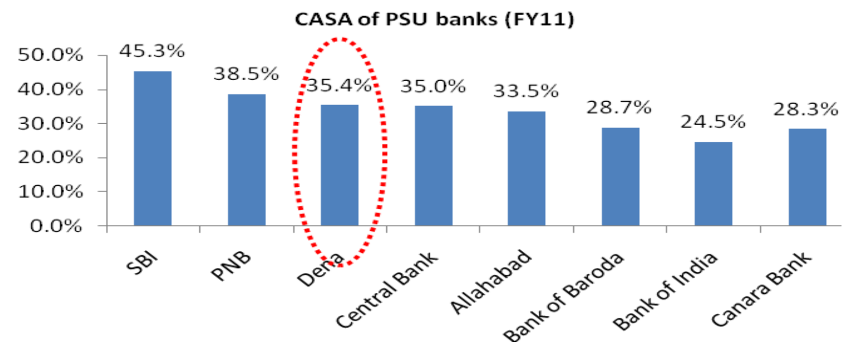
Strong CASA:

Dena Bank's strength lies in having strong concentration of branches in the CASA rich western regions of the country. Approximately 65% of the Bank's branches are located in the western India and the bank also has strong presence in the rural and semi-urban areas which gives the bank access to low-cost deposits which helps the bank in garnering higher CASA.



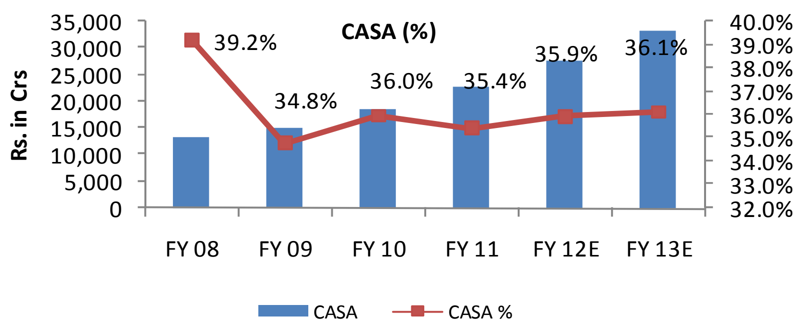
Source: Company data, Nirmal Bang Research

On account of having a strong branch network in CASA rich regions, Dena Bank has been able to register one of the highest CASA ratios among the PSU banks. In Q1FY12, the Bank's CASA ratio stood at a healthy 35.2%, which is amongst the best in industry.



Source: Company data, Nirmal Bang Research

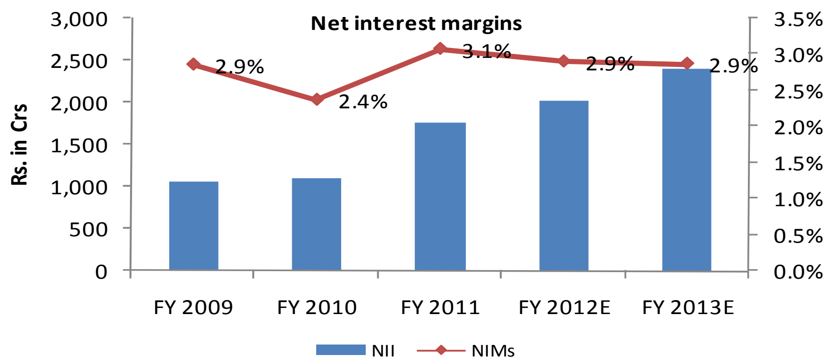
Management intends to continue to focus on increasing its CASA share. To increase and tap new business, the bank has set a target to add 155 new branches of which 55 would be opened in rural areas for the purpose of financial inclusion plan. This would help to attract more CASA deposits and tap new SME clients.



Source: Company data, Nirmal Bang Research

Protection of NIMs

With increasing interest rates and cost of deposits, NIMs is expected to remain under pressure. However, a recent equity infusion of Rs 600 crs will help the bank to maintain margins in FY12. The bank's NIMs stood at 2.9% in Q1FY12 which was in line with expectations of the Management as the management had expected around 20 bps decline. Management is confident that the bank will be able to maintain NIMs at around 3% for FY12E. Nevertheless, we factor in a 20 bps decline in margins for FY12. Going forward, we expect NII to grow at CAGR of ~16.4% for FY11-FY13E resulting from higher CASA deposits, focus on retail and SME portfolio and availability of adequate capital.



Source: Company data, Nirmal Bang Research

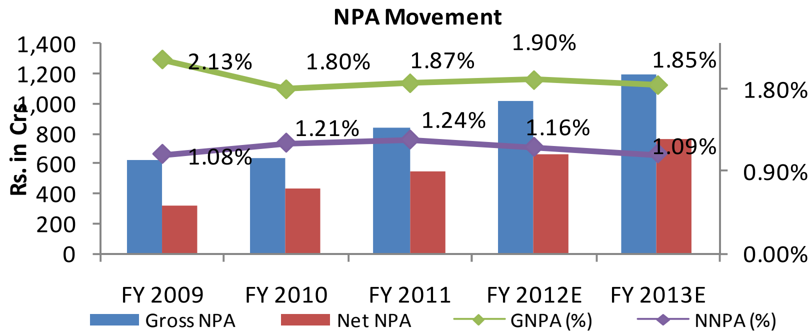
Asset quality to remain a cause of concern in near term

Asset quality has been a concern for Dena Bank, but with increasing efforts taken by the bank to recover & minimize the new slippages, the bank has been able to maintain NPA levels in the comfortable zone. The bank has set up recovery teams and specialized monitoring systems to take care of the asset quality. This has started showing good results as recoveries have increased. The bank expects higher recoveries in FY12E.

However, there are some near term concerns for the bank. The bank has a very high exposure of approximately Rs.9000 crs in the power sector and out of this around Rs.6000 crs (March 2011) are to State Electricity Boards (SEBs) on a short-term working capital basis. This is a cause of concern as the current outlook for SEBs (especially Tamil Nadu which has around 10% exposure of total SEBs) is not very good. Even the Management has become cautious over this fact and is focusing on reducing its exposure to SEBs. This is evident from the fact that the bank has been successful in reducing its exposure to SEBs from Rs.6000 crs in March 2011 to Rs.5180 crs in June 2011.

Moreover, the bank has not yet shifted to 100% system based NPA recognition. The bank still has to migrate its "Rs.50 lakhs and below" portfolio to system based NPA recognition. This constitutes around 18% of the total advance portfolio of the bank. As observed by other banks' performance, we believe that migrating to system based NPA recognition can lead to higher slippages. However, the Management is confident that the slippages won't be higher and targets to reduce its Gross NPAs from 1.8% in FY11 to 1.6% in FY12.

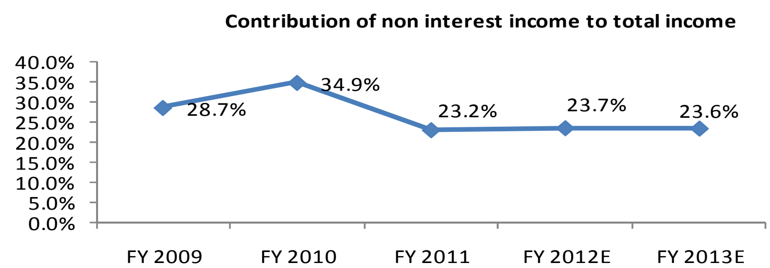
Going forward, we expect Gross NPAs and Net NPAs to remain higher in FY12 owing to the reasons mentioned above. We expect Gross NPAs to remain high at 1.9% and Net NPAs at 1.16% for FY12E. We have factored in higher provisioning at Rs 466 crs in FY12E as compared to Rs 325 crs in FY11. However, from FY13E onwards we believe that the bank will witness an improvement in its asset quality on the back of recoveries, steps taken to contain fresh slippages by way of constant monitoring and adequate provisions provided by the bank.



Source: Company data, Nirmal Bang Research

Focus on non interest income

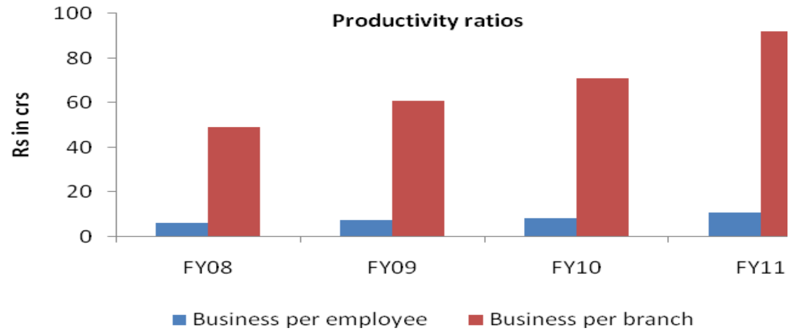
The bank's non interest income has shown a dismal growth in and had been a point of concern for the bank. However, now the Management is confident of a revival in its non interest income in the coming quarters. The Bank is leveraging its relationship with its current customer base to increase the non fund based business to increase the fee based income. The Bank has tied up with all the top mutual funds to distribute their products through the bank's branches. The bank is also focusing on core banking solution (CBS) to enable its customer's branch banking. Moreover, the bank is focusing on recoveries which will further boost the bank's bottom line performance. Management guided for 20-25% fee income growth in FY12. The greater focus on retail and SME lending is likely to boost fee income growth for the bank; we factor in 17.5% CAGR over FY11-FY13E.



Source: Company data, Nirmal Bang Research

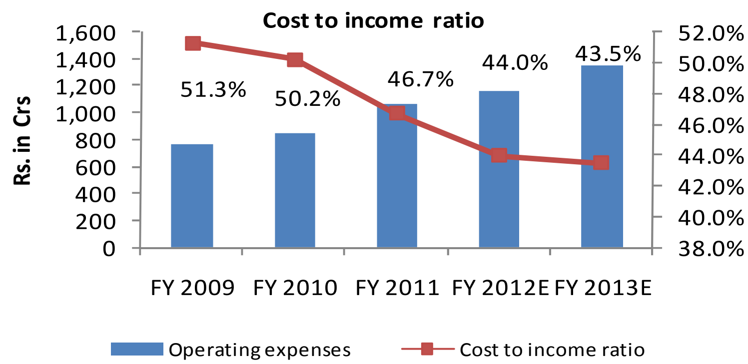
Improved productivity and cost to income ratio:

Dena bank has consistently improved its performance through optimum utilization of staff and branches. To further improve staff productivity, various steps have been taken by the bank like specialized training, recruitment of specialized officers and incentive schemes etc. Dena bank's total business per employee stands at Rs.10.83 crs and total business per branch improved to Rs.88.44 crs in Q1FY12.



Source: Company data, Nirmal Bang Research

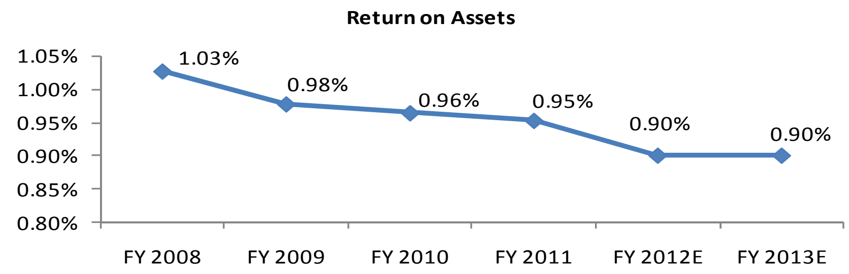
Despite the increase in employee cost owing to gratuity and second pension liabilities, the bank has been able to maintain its cost to income ratio for FY11 at 46.7% and 46.1% for Q1FY12. Going forward, we expect higher growth in income than cost i.e. operating profit to grow by 20.2% CAGR over FY11-FY13E mainly due to protection in margins and higher fee income. Operating expenses are expected to grow by 12.4% over FY11-FY13E mainly due to network expansion plans of the bank leading to lower cost to income ratio of 44.0% and 43.5% in FY12E and FY113E respectively.



Source: Company data, Nirmal Bang Research

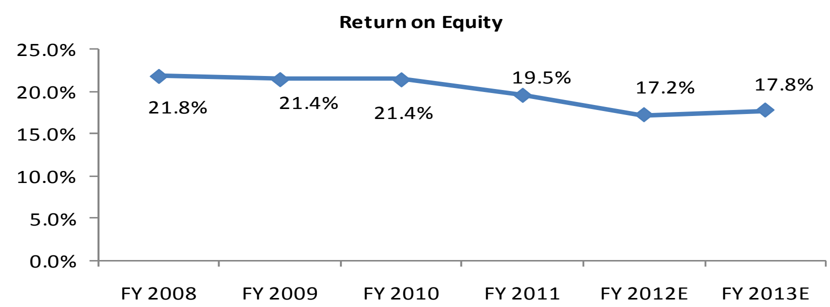
Stable return ratios:

Comparatively stable NIMs, traction in core fee income are likely to boost Dena Bank's core operating performance which in turn will help the bank to register stable return ratios going forward. We are positive on the bank's ability to strengthen its core business performance and fee income and lower its operating costs which would drive the profits of the company. Return ratios are looking subdued in FY12E owing to the equity dilution done in FY11.



Source: Company data, Nirmal Bang Research

We are factoring in a 20.2% CAGR in operating profit over FY11-FY13E. However, PAT growth is likely to be lower at ~15.5% CAGR during the same period due to higher provisions factored in to increase the coverage ratio. Management intends to reach 1% RoA by end of FY12E. We believe that the return ratio of the bank will improve with stable economic conditions and we expect RoA of 0.9% and RoE of 17.2% by FY12E.



Source: Company data, Nirmal Bang Research

Risk Concerns

- In the event of the macro-economic scenario worsening again, there is a strong possibility of higher-than-expected NPA provisions.
- More than expected slippages from the retail segment can have an impact on the company's valuation and impact the target price.
- A change in management could impact the bank's strategic target leading to a phase of uncertainty for the bank.

Peer Comparison

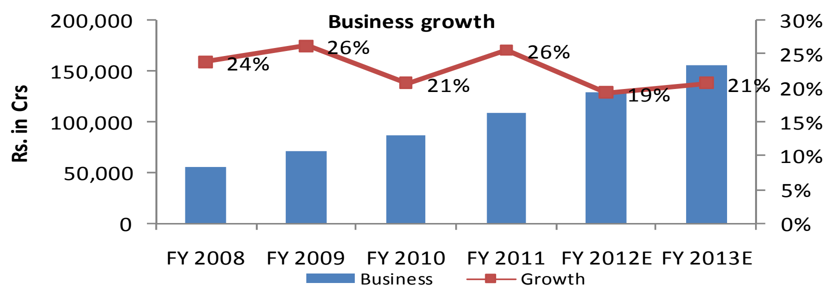
We are comparing Dena Bank with Andhra Bank, United Bank of India, Vijaya Bank and UCO Bank as these banks are mid-sized PSU banks having almost similar balance sheet size. Amongst the peer group we can see that Dena Bank is trading at a very attractive level.

	Dena Bank	Andhra Bank	United Bank	Vijaya Bank	UCO Bank
EPS *	20.3	26.4	19.7	13.2	17.0
Adj BV (Q1FY12)	95.1	116.9	82.4	54.2	55.3
P/E	4.19	5.11	4.72	4.78	5.01
P/ABV	0.89	1.15	1.13	1.16	1.54
RoE *	17.2%	21.0%	14.8%	16.4%	16.7%

** Based on Nirmal Bang estimates for Dena Bank and Bloomberg estimates for FY12 for others*

Company Background

The family of Devkaran Nanjee founded Dena Bank on May 26, 1938 with the name Devkaran Nanjee Banking Company Ltd. In December 1939, it became a public limited company and the name was changed to Dena Bank Ltd. In the year 1969, the Dena bank was nationalized. Dena bank is a government owned bank with its head office located in Mumbai. The bank has a network of 1297 branches, 507 ATMs and 12 extension counters as on 30th June 2011. As on 30th June 2011, bank had total business of Rs.103,973 crs. The bank is mainly concentrated in the Gujarat state. Dena bank has major presence in rural area and out of total branches, 56% are in rural and semi-urban areas.



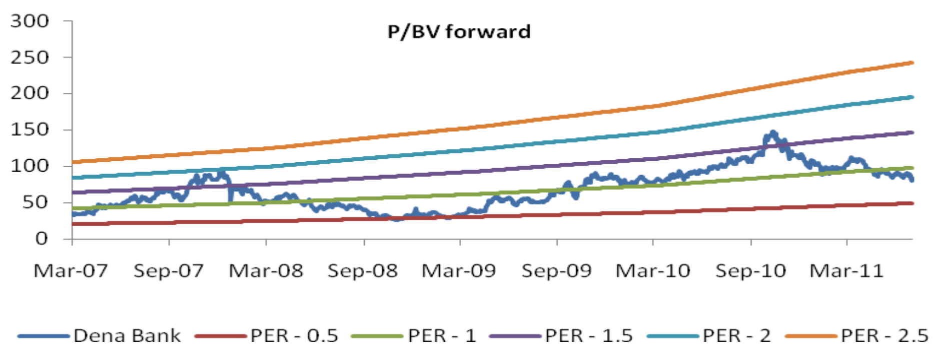
Source: Company data, Nirmal Bang Research

Valuation and Recommendation

We expect Dena Bank to improve its core operating metrics over the next couple of years, driven by focus on its liability franchise and core fee income with operating efficiency. Dena Bank is currently trading at a very attractive valuation amongst the banking business space. Increasing focus on high yield retail credit, strengthening of balance sheet and lower operating costs would improve efficiency and drive earnings going forward for Dena Bank.

Although we believe that there are some near term concerns for the bank in terms of asset quality, we feel that the stock price has already discounted this concern as the stock is trading at its historically lower valuations. We don't see a significant downside risk for the stock from this level. Moreover, we believe that the performance of the company will improve from here on and the stock will command a higher valuation.

At CMP of Rs 85, the stock is trading at 0.8x of its FY12E ABV and 0.68x its FY13E ABV whereas on PE it is trading at 4.19x and 3.49x in FY12E and FY13E respectively. Looking at the historical trend we value it at 1.2x P/ABV of FY12E. Based on our estimated book value of Rs.108 per share for FY 2012E and P/ABV target multiple of 1.2x we arrive at a target price of Rs.129. **We recommend BUY on the stock with target price of Rs.129 indicating a potential upside of 50%**



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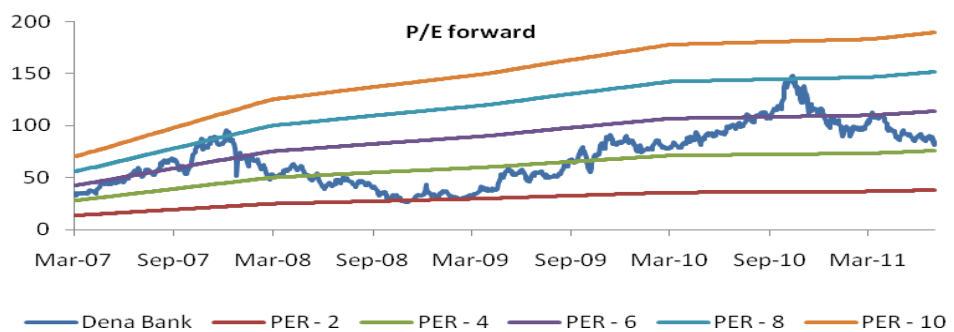

Source: Company data, Nirmal Bang Research

Financials

Profitability (Rs. Crs)	FY 2010	FY 2011	FY 2012E	FY 2013E
Interest earned	4,010	5,034	6,527	7,880
Interest expended	2,910	3,270	4,510	5,490
Net interest income	**1,100**	**1,763**	**2,017**	**2,390**
Non interest income	589	534	625	737
Total income	**1,689**	**2,297**	**2,642**	**3,127**
Operating expenses	848	1,073	1,162	1,359
Staff costs	512	688	746	873
Other Op Exp	336	385	415	486
Operating profit	**841**	**1,224**	**1,480**	**1,768**
Provisions	154	325	466	550
Profit before tax	687	899	1,013	1,218
Taxes	176	287	334	402
Net profit	**511**	**612**	**679**	**816**

Quarterly (Rs. Crs)	Sept. 10	Dec. 10	Mar. 11	June.11
Net interest income	465	466	471	447
Non interest income	119	127	181	124
Total income	584	593	652	571
Operating expenses	259	277	309	263
Operating profit	326	316	343	308
Provisions	73	86	124	65
Profit before tax	253	231	219	242
Taxes	92	76	62	74
Net profit	161	155	157	168

Profitability Ratios	FY 2010	FY 2011	FY 2012E	FY 2013E
Cost / Income Ratio	50.2%	46.7%	44.0%	43.5%
Net profit margin	30.3%	26.6%	25.7%	26.1%
RONW	21.4%	19.5%	17.2%	17.8%

Growth Ratios	FY 2010	FY 2011	FY 2012E	FY 2013E
Advances growth	22.8%	26.4%	19.2%	21.1%
Deposit growth	19.3%	25.1%	19.3%	20.4%
NII growth	3.1%	60.3%	14.4%	18.5%
PAT growth	20.1%	19.7%	11.0%	20.2%
Pre prov profit growth	15.2%	45.6%	20.9%	19.5%
Non interest inc growtl	36.9%	-9.3%	17.0%	18.0%

Ratios	FY 2010	FY 2011	FY 2012E	FY 2013E
P/BV	1.03	0.83	0.71	0.60
P/ABV	1.17	0.93	0.80	0.68
P/E	4.79	4.66	4.19	3.49

Balance Sheet (Rs. Crs)	FY 2010	FY 2011	FY 2012E	FY 2013E
Deposits	51,344	64,210	76,592	92,242
(of which CASA)	*(18,461)*	*(22,742)*	*(27,518)*	*(33,297)*
Borrowings	1,562	1,692	1,830	1,984
Other liab and prov	2,079	1,281	1,537	1,768
Total liabilities	54,985	67,183	79,960	95,994
Equity capital	287	333	333	333
Reserves and surplus	2,315	3,323	3,904	4,611
Net worth	2,602	3,656	4,237	4,944
Total liab and equity	**57,587**	**70,838**	**84,197**	**100,939**
Cash and bank bal	5,115	5,409	6,768	7,804
Investments	15,694	18,769	22,010	26,318
Advances	35,462	44,828	53,432	64,692
Fixed assets	407	404	444	489
Other assets	908	1,429	1,543	1,636
Total assets	**57,587**	**70,838**	**84,197**	**100,939**

Key Ratios	FY 2010	FY 2011	FY 2012E	FY 2013E
Yield Ratios				
Avg Yield on Assets	8.7%	8.8%	9.4%	9.5%
Yield on Advances	9.4%	9.5%	10.3%	10.3%
Yield on Investments	6.8%	6.9%	7.2%	7.3%
Cost of Int Bearing Liab	6.0%	5.5%	6.2%	6.4%
Cost of Deposits	6.1%	5.6%	6.2%	6.3%
Net Interest Spread	2.7%	3.3%	3.1%	3.1%
NIM	2.4%	3.1%	2.9%	2.9%
Balance Sheet Ratios				
Gross NPA	1.80%	1.87%	1.90%	1.85%
Net NPA	1.21%	1.24%	1.16%	1.09%
Return on Assets	1.0%	1.0%	0.9%	0.9%
CASA	36.0%	35.4%	35.9%	36.1%
Loan-deposit ratio	69.1%	69.8%	69.8%	70.1%
CAR	12.8%	13.6%	12.7%	11.9%

Valuation Ratios	FY 2010	FY 2011	FY 2012E	FY 2013E
EPS	17.82	18.34	20.37	24.48
BVPS	83	103	120	142
Adjusted BVPS	73	92	107	126
Dividend per share	2.0	2.2	2.5	2.8
Dividend yield	2.3%	2.6%	2.9%	3.3%

Source: Company data, Nirmal Bang Research

NOTE

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