

Yes Bank

26 September 2018

Reuters: YESB.NS; Bloomberg: YES IN

Reflexivity Is Not My Friend

We take cognizance of events post-19th September and their real impact on the business outlook for Yes Bank (YBL). (1) The high quantum of YBL stock price decline on 21st September, we aver, was on the back of sentiment and not fundamentals. However, the same is going to have a durable impact on investor sentiment and, therefore, ultimately, on capital raising capacity for YBL (2) Press release dated 24th September re-iterates credit cost guidance for FY19 at 50bps-70bps, thereby maintaining uncertainty regarding how Divergence in FY17-end asset quality might be addressed. Uncertainty may continue to dampen sentiment of a section of the investor community. (3) Press release dated 25th September (outcome of Board Meeting) mentions formation of "Search & Selection Committee" for new CEO but also seeks to appoint Mr. Rajat Monga and Mr. Pralay Mondal (both Senior Group Presidents) as Executive Directors "to ensure a long-term succession plan within Yes Bank". How RBI might view the said appointments of aforementioned internal candidates adds another dimension of uncertainty. (4) Apart from lower capital raising capacity, a new propensity to, on balance, accept lower-risk credits on the balance sheet could negatively impact with both loan growth and loan yield. As a consequence of these reasons, we revise estimates lower and also assign a lower multiple for YBL, to factor in continued impact on return ratios beyond FY21E. We retain Buy rating with a Target Price of Rs299, valuing YBL at 1.6 1HFY21E P/BV.

High quantum of YBL stock price decline on 21st September is going to have a durable impact on investor sentiment and, therefore, ultimately, on capital raising capacity for YBL: YBL stock price declined 29% on 21st September well beyond warranted by fundamentals. However, such a large price decline is likely to have a durable impact on investor sentiment. In any case, a significantly lower stock price makes a successful capital raise far less amenable, ceteris paribus. Damage to investor sentiment is more key given lower capital raising capacity will directly impact growth outlook.

Re-iteration of credit cost guidance for FY19 at 50-70bps creates uncertainty with regard to how Divergence will be addressed and might dampen sentiment of a section of the investor community: Prima facie, re-iteration of credit cost guidance at lower levels seems to imply that Divergence with regard to FY17-end asset quality may not be recognized as NPA with completeness and without rapid upgrade back to standard loan classification. Thus, uncertainty with regard to asset classification may continue till further concrete clarity emerges on this front. Uncertainty will not be viewed positively by a section of the investor community.

Preparing a "succession plan" in favour of internal candidates will be reviewed long and hard by the RBI: While it is perhaps not exactly clear what is implied by "succession plan", it is possible that it refers to Mr. Rajat Monga / Mr. Pralay Mondal assuming the post of CEO at some future date. How exactly this will be viewed by the RBI is not exactly understood at this stage but it is in the realm of possibility that RBI would regard them as individuals affiliated to Mr. Rana Kapoor and, therefore, prepared to effectively act in concert with the latter. This also adds another dimension of uncertainty.

Regardless of who will be appointed CEO at YBL, this event will cause YBL to take on lower risk, on balance, on the balance sheet: Lower propensity to take risk, due to risk aversion as well as capital constraint, will mean leaving out credit of relatively higher risk that YBL earlier had the appetite to assume. Lower-risk lending will also have a yield-dilutive impact. Both of these aspects, apart from lower capital raising capacity, will combine to have a negative impact on both loan growth and net interest margin. Since there remains the possibility of addressing Divergence by way of NPA recognition, we also revise credit cost estimates higher.

Valuation and outlook: We revise (1) FY18-21E loan CAGR lower from 33% to 28% (2) reduce yield on loans by 10-30 bps across FY19E-21E and (3) increased slippage ratio by 20 bps across FY19E-21E (with concomitant rise in credit costs) to reflect the considerations above. Our NII estimates for FY19E/20E/21E are revised lower by -4%/-8%/-13%, PPOP estimates are revised lower by -5%/-9%/-13% and PAT estimates by -11%/-12%/-15%. We assign a multiple of 1.6x to 1HFY21E P/BV to arrive at our Target Price of Rs 299 (compared with Rs 461 earlier).

BUY

Sector: Banking

CMP: Rs220

Target Price: Rs299

Upside: 36%

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Key Data

Current Shares O/S (mn)	2,308.1
Mkt Cap (Rsbn/US\$bn)	507.1/7.0
52 Wk H / L (Rs)	404/197
Daily Vol. (3M NSE Avg.)	25,967,700

Price Performance (%)

	1 M	6 M	1 Yr
Yes Bank	(41.3)	(27.6)	(39.1)
Nifty Index	(4.2)	9.2	12.1

Source: Bloomberg

Exhibit 1: Change in our estimates

	Revised Estimate			Earlier Estimate			% Revision		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Net interest income (Rsmn)	103,735	134,276	169,023	108,221	146,678	193,519	(4.1)	(8.5)	(12.7)
Net interest margin (%)	3.1	3.1	3.2	3.2	3.2	3.3	-7 bps	-10 bps	-16 bps
Operating profit (Rsmn)	104,168	133,345	180,931	109,154	147,293	209,131	(4.6)	(9.5)	(13.5)
Profit after tax (Rsmn)	53,497	72,136	103,758	60,121	81,687	121,644	(11.0)	(11.7)	(14.7)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: One-year forward P/BV


Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 3: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Interest income	164,246	202,674	289,425	376,765	463,434
Interest expenses	106,273	125,304	185,690	242,490	294,411
Net interest income	57,973	77,371	103,735	134,276	169,023
Fee income	31,400	41,380	59,788	77,279	100,463
Other income	10,168	10,859	12,157	16,476	19,814
Net revenues	99,540	129,609	175,681	228,031	289,301
Operating expenses	41,165	52,128	71,513	94,685	108,370
-Employee expenses	18,050	21,889	25,596	29,771	31,091
-Other expenses	23,115	30,239	45,917	64,915	77,279
Pre-provision profit	58,375	77,481	104,168	133,345	180,931
Provisions	7,934	15,538	23,112	24,048	23,722
-Loan-loss provision	7,466	12,476	23,112	24,048	23,722
-Provisions for investment	522	2,599	-	-	-
-Other provisions	(54)	463	-	-	-
PBT	50,441	61,943	81,056	109,298	157,208
Taxes	17,140	19,697	27,559	37,161	53,451
PAT	33,301	42,246	53,497	72,136	103,758

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Equity capital	4,565	4,606	4,606	4,606	5,067
Reserves & surplus	215,975	252,977	298,990	364,474	534,438
Shareholders' funds	220,540	257,583	303,596	369,080	539,504
Deposits	1,428,738	2,007,381	2,719,750	3,406,677	4,351,201
-Current deposits	190,878	288,257	407,962	511,002	652,680
-Saving deposits	327,818	443,505	639,141	851,669	1,131,312
-Term deposit	910,042	1,275,620	1,672,646	2,044,006	2,567,209
Borrowings	386,067	748,936	1,008,651	1,185,837	1,265,902
Other liabilities	115,254	110,556	156,839	200,509	238,797
Total liabilities	2,150,599	3,124,456	4,188,837	5,162,103	6,395,404
Cash/Equivalent	195,494	247,344	329,725	412,156	515,195
Advances	1,322,627	2,035,339	2,747,707	3,434,634	4,293,292
Investments	500,318	683,989	937,009	1,122,480	1,354,318
Fixed assets	6,835	8,324	9,989	11,986	15,582
Other assets	125,325	149,460	164,406	180,847	217,017
Total assets	2,150,599	3,124,456	4,188,837	5,162,103	6,395,404

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Key ratios

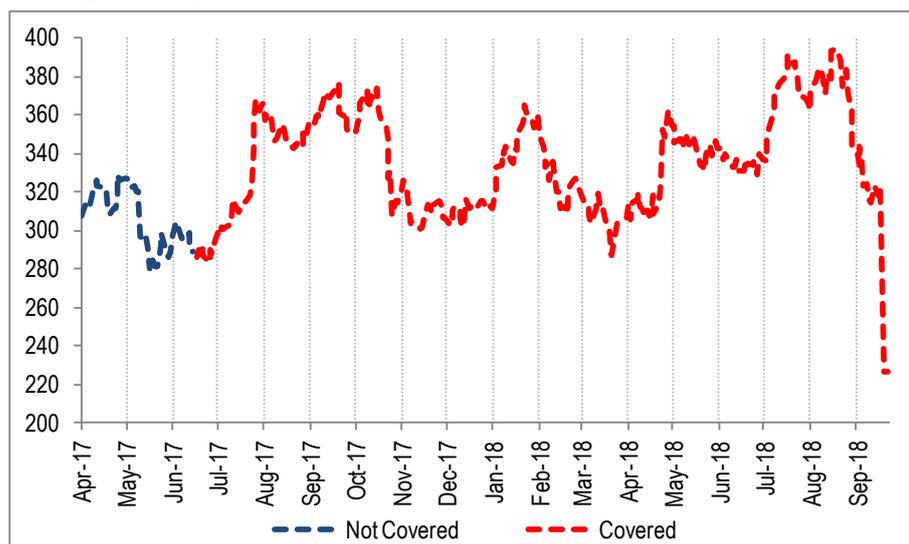
Y/E March	FY17	FY18	FY19E	FY20E	FY21E
Growth (%)					
NII growth	26.9	33.5	34.1	29.4	25.9
Pre-provision profit growth	35.7	32.7	34.4	28.0	35.7
PAT growth	31.1	26.9	26.6	34.8	43.8
Business (%)					
Deposit growth	27.9	40.5	35.5	25.3	27.7
Advance growth	34.7	53.9	35.0	25.0	25.0
Business growth	31.1	46.9	35.2	25.1	26.4
CD	92.6	101.4	101.0	100.8	98.7
CASA	36.3	36.5	38.5	40.0	41.0
Operating efficiency (%)					
Cost-to-income	41.4	40.2	40.7	41.5	37.5
Cost-to-assets	2.2	2.0	2.0	2.0	1.9
Productivity (Rsmn)					
Business per branch	2751.4	3675.2	4653.2	5473.0	6524.1
Business per employee	136.7	221.7	282.0	333.7	411.9
Profit per branch	33.3	38.4	45.5	57.7	78.3
Profit per employee	1.7	2.3	2.8	3.5	4.9
Spread (%)					
Yield on advances	10.6	9.2	9.2	9.3	9.2
Yield on investments	7.7	6.9	7.4	7.5	7.5
Cost of deposits	6.4	5.5	5.6	5.8	5.7
Yield on assets	9.6	8.5	8.6	8.7	8.7
Cost of funds	6.5	5.5	5.7	5.8	5.8
NIM	3.4	3.2	3.1	3.1	3.2
Capital adequacy (%)					
Tier I	13.3	13.2	12.4	12.1	12.6
Tier II	3.7	5.2	4.3	3.5	2.5
Total CAR	17.0	18.4	16.7	15.5	15.0
Asset quality (%)					
Gross NPAs	1.5	1.3	1.4	1.4	1.5
Net NPAs	0.8	0.6	0.5	0.5	0.4
Specific provision coverage	46.5	49.7	61.3	63.8	70.0
Slippage	2.3	4.9	1.4	1.4	1.4
Credit cost	0.6	0.7	1.0	0.8	0.6
Return (%)					
RoE	18.6	17.7	19.1	21.4	22.8
RoA	1.8	1.6	1.5	1.5	1.8
RoRWA	2.1	1.9	1.8	1.9	2.2
Per share					
EPS	15.1	18.4	23.2	31.3	42.9
BV	96.6	111.8	131.8	160.3	213.0
ABV	91.9	106.1	125.4	152.7	205.5
Valuation (x)					
P/E	14.6	11.9	9.5	7.0	5.1
P/BV	2.3	2.0	1.7	1.4	1.0
P/ABV	2.4	2.1	1.8	1.4	1.1

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
19 June 2017	Buy	286	362
27 July 2017	Buy	344	420
27 October 2017	Buy	331	429
19 January 2018	Buy	341	435
27 April 2018	Buy	352	439
27 July 2018	Buy	370	461
21 September 2018	Buy	319	461
26 September 2018	Buy	220	299

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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