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Sector View

Positive

Banking

You can still *bank* on this sector…

The Bank Nifty put up a strong performance in the last three months, gaining 23% YoY vs. Nifty gaining just 3%. The southward movement in CPI to 4.38%, 10 year G-sec yields declining to 7.9% (>50 bps in three months) and growing expectation of a repo rate cut have continued the momentum in banking stocks. Banking credit growth moderated to 10.6% YoY at ₹ 6303481 crore as on December 12, 2014 as growth in the large corporate segment and big ticket infra loans are not yet visible while past sanctions are dwindling now. Incrementally, retail loans contributed 43.2% of incremental YTD credit, growing faster at 16.3% YoY as on October 2014. Hence, total credit growth expectation is still muted around 13-14% for FY15E. Though the new government has driven acceleration in sentiments, the pick-up in capex or improvement in mid corporate performance is still not visible leading to subdued growth and the key concern area of asset quality stress continuing.

Sector GNPA rose 6.7% QoQ in September 2014 quarter to ₹ 275550 crore forming 4.4% of advances while restructured assets (RA) were at ~6.1% of advances (₹ 375000 crore-September 2014). We expect 10% GNPA rise by FY16E after 19% rise expected in FY15 for coverage banks.

Exhibit 1: Banking Sector – Coverage Summary

Sector / Company	CMP (₹)	TP(₹)	Rating	M Cap (₹ Cr)	EPS (₹) FY14	EPS (₹) FY15E	EPS (₹) FY16E	P/E (x) FY14	P/E (x) FY15E	P/E (x) FY16E	P/ABV (x) FY14	P/ABV (x) FY15E	P/ABV (x) FY16E	RoA (%) FY14	RoA (%) FY15E	RoA (%) FY16E	RoE (%) FY14	RoE (%) FY15E	RoE (%) FY16E
Bank of India (BANIND)	300	317	Buy	17,937	42.4	46.3	54.6	7.1	6.5	5.5	0.9	1.0	0.9	0.5	0.5	0.5	10.1	9.6	10.7
Bank of Baroda (BANBAR)	1,071	1,250	Buy	45,133	105.4	136.1	160.4	10.2	7.9	6.7	1.6	1.4	1.2	0.8	0.8	0.8	13.4	15.2	15.8
Dena Bank (DENBAN)	58	60	Hold	3,141	10.3	8.5	14.4	5.7	6.9	4.1	0.7	0.8	0.8	0.5	0.3	0.5	8.5	6.3	10.2
Punjab National Bank (PUNBAN)	223	279	Buy	40,000	18.5	20.7	25.1	12.1	10.8	8.9	1.6	1.6	1.4	0.6	0.6	0.7	9.7	10.0	11.1
State Bank of India (STABAN)	308	374	Buy	230,243	14.6	18.5	21.3	21.1	16.7	14.5	2.6	2.4	2.2	0.6	0.7	0.7	10.0	11.1	11.7
Syndicate Bank (SYNBN)	126	141	Hold	7,593	27.4	25.0	32.2	4.6	5.0	3.9	1.0	1.0	0.9	0.7	0.6	0.6	15.2	12.6	14.8
Axis Bank (UTIBAN)	497	550	Buy	117,251	26.5	30.2	33.8	18.8	16.5	14.7	3.1	2.7	2.4	1.7	1.7	1.7	17.4	17.2	16.5
City Union Bank (CITUNI)	93	100	Hold	4,498	6.4	6.6	8.6	14.5	14.0	10.8	2.8	2.2	1.9	1.4	1.4	1.6	18.9	16.6	17.5
Development Credit Bank (DCB)	121	124	Hold	3,145	6.0	6.3	7.1	20.1	19.3	17.0	3.0	2.4	2.2	1.3	1.2	1.2	14.8	13.5	12.5
Federal Bank (FEDBAN)	148	164	Buy	12,663	9.8	11.9	14.3	15.1	12.5	10.4	1.9	1.7	1.5	1.2	1.3	1.3	12.6	13.8	14.8
HDFC Bank (HDFBAN)	951	1,036	Hold	226,974	35.3	41.3	50.4	26.9	23.0	18.9	5.3	4.0	3.4	1.9	1.9	2.0	21.3	19.8	19.0
Indusind Bank (INDBA)	783	845	Buy	41,038	26.8	33.3	41.5	29.2	23.5	18.9	4.7	4.0	3.4	1.8	1.8	1.9	16.9	18.0	19.2
Jammu & Kashmir Bank (JAMKAS)	150	152	Hold	7,264	24.4	17.9	27.6	6.1	8.4	5.4	1.3	1.4	1.2	1.6	1.0	1.4	22.3	14.3	19.4
Kotak Mahindra Bank (KOTMAH)	1,244	1,250	Hold	95,368	19.5	22.1	25.7	63.8	56.4	48.3	8.0	7.2	6.3	1.8	1.8	1.8	13.8	13.0	13.4
South Indian Bank (SOUINO)	28	28	Hold	3,738	3.8	3.7	4.1	7.4	7.5	6.9	1.3	1.2	1.1	1.0	0.8	0.8	16.6	13.5	14.7
Yes Bank (YESBAN)	744	797	Hold	30,960	44.9	48.3	61.9	16.6	15.4	12.0	3.8	2.7	2.2	1.6	1.7	1.6	25.0	21.3	20.1

Source: Company, ICICIdirect.com Research

Analyst's name

Kajal Gandhi
kajal.gandhi@icicisecurities.com
Vasant Lohiya
vasant.lohiya@icicisecurities.com
Sheetal Ashar
sheetal.ashar@icicisecurities.com

We analysed the branch and employee matrix for the banking sector, which is indicating the valuation gap in store for future. We even performed an RoE and P/ABV matrix based charting for our coverage universe.

Large private banks like HDFC Bank and IndusInd Bank are trading at premium valuations with strong RoE >20% while Kotak Mahindra Bank trades rich over 6x P/ABV. Accordingly, the basket of large PSU banks like SBI, PNB and BoB appear strong for upside while Axis Bank, among large private banks, offers an opportunity for further appreciation with reasonable valuations.

We maintain our bullish stance on select large PSU banks and expect consistency in private banks to continue with stable performance. We have raised target prices based on revised market multiples. Accordingly, Axis Bank, PNB are our top picks in banking sector in the current environment based on our sector valuation analysis (Mcap/branch). We prefer SBI as it is market leader with lower stress levels in asset quality.

Valuation – Sector analysis on M/Cap per branch

We have used two pronged valuation methodology -1) Per branch and employee matrix for the banking sector, which is indicating the valuation gap in store for future and 2) Performed an RoE and P/ABV matrix based charting for our coverage universe wherein we visualise the expensive still maintain their position while the cheaper banks still lag in valuation. Stocks with higher CASA per branch and other matrix are available cheap and certain banks are trading higher than justified multiples.

Exhibit 2: Relative positioning on market cap per branch and employee basis as well as CASA per branch

₹ crore	Market Cap per branch	Market Cap per employee	CASA per branch	Deposit per branch	Business per branch	Business per employee	Trailing P/E Ratio(NSE)	Trailing P/BV(NSE)	Dividend Yield - %(NSE)
Kotak Mah. Bank	157.7	3.6	31.1	97.6	185.3	4.2	58.8	7.8	0.1
IndusInd Bank	67.7	2.6	32.7	100.5	192.0	7.4	25.6	4.7	0.5
HDFC Bank	66.8	3.3	48.4	107.9	197.0	9.8	24.6	5.2	0.7
Yes Bank	54.3	3.5	29.2	132.5	231.8	14.8	17.3	3.0	1.0
Axis Bank	48.2	2.7	52.6	117.0	212.7	12.0	17.2	3.0	0.8
DCB	35.8	1.5	27.5	109.8	196.4	8.3	20.8	2.5	0.0
ING Vysya Bank	28.8	1.6	24.7	74.0	138.3	7.7	23.9	2.3	0.7
St Bk of India	14.1	1.0	37.3	86.8	162.2	11.7	19.4	1.9	1.0
City Union Bank	12.6	1.3	9.2	51.8	89.7	9.0	14.7	2.3	1.0
Karur Vysya Bank	11.4	0.9	14.8	72.2	128.3	10.6	15.8	1.8	2.0
Federal Bank	10.6	1.2	15.9	50.9	87.9	9.9	12.9	1.8	1.4
J & K Bank	9.3	2.1	34.9	89.2	148.9	33.9	8.3	1.3	3.3
Bank of Baroda	9.1	1.0	29.7	115.3	195.8	21.0	9.6	1.3	2.1
IDBI Bank	7.8	0.7	38.4	169.9	312.3	26.4	12.9	0.5	1.5
PNB	6.9	0.6	29.4	76.8	136.3	12.7	11.5	1.2	0.9
South Ind.Bank	4.6	0.5	12.4	59.8	105.4	11.8	8.3	1.1	3.0
Oriental Bank	4.5	0.5	22.1	91.0	156.4	17.0	8.0	0.7	2.4
Karnataka Bank	4.4	0.4	17.2	67.6	114.9	9.6	7.1	0.9	2.8
Canara Bank	4.2	0.4	21.7	88.5	151.8	14.8	8.1	0.8	2.6
Indian Bank	4.0	0.5	19.6	72.0	126.3	14.6	8.5	0.8	2.3
Bank of India	4.0	0.4	23.6	102.7	182.5	19.6	6.7	0.7	1.7
Union Bank (I)	3.6	0.4	22.7	76.9	136.1	15.6	7.2	0.8	1.8
St Bk of Bikaner	3.6	0.3	25.4	64.4	120.2	10.3	5.6	0.8	2.5
UCO Bank	2.7	0.3	20.4	68.9	120.6	14.2	6.5	0.7	3.2
St Bk of Mysore	2.7	0.2	21.8	65.2	117.6	10.2	7.0	0.6	0.6
Central Bank	2.6	0.3	17.5	52.5	91.3	10.3	23.4	0.9	0.0
Vijaya Bank	2.6	0.3	15.1	82.2	136.1	16.1	8.8	0.7	4.1
Dhanlaxmi Bank	2.6	0.3	10.0	45.6	75.4	8.3	0.0	0.7	0.0
Corporation Bank	2.6	0.3	19.5	95.7	163.5	18.1	9.3	0.5	2.2
Allahabad Bank	2.4	0.3	21.1	67.2	115.8	13.4	9.2	0.6	2.0
Andhra Bank	2.4	0.3	16.6	67.1	118.0	13.3	13.0	0.6	1.3
Syndicate Bank	2.3	0.3	17.2	65.3	118.8	14.2	4.8	0.7	4.5
Dena Bank	1.9	0.3	19.0	67.4	114.9	16.9	7.8	0.5	3.9
Pun. & Sind Bank	1.8	0.3	13.3	63.7	106.7	16.0	8.8	0.5	2.5
United Bank (I)	1.4	0.2	20.6	55.7	88.6	10.7	0.0	0.6	0.0

Source: Capitaline, ICICIdirect.com Research, Mcap used as on 19/12/2014

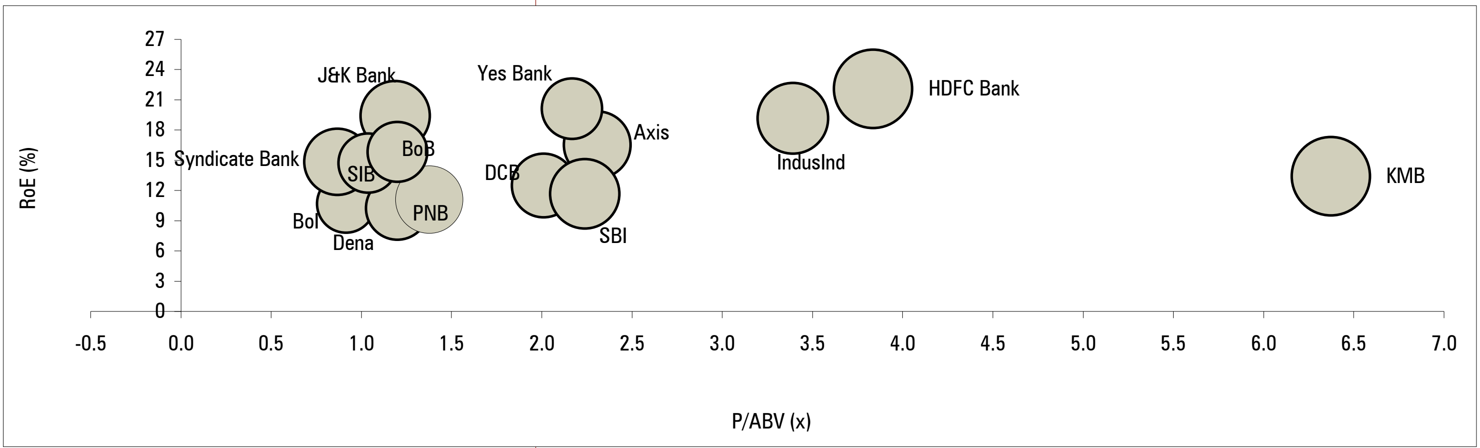
Mcap/branch based valuation is ₹ 67 crore per branch at the highest level except Kotak Mahindra Bank (not comparable). Top two banks have a CASA of ₹ 33 crore per branch (IndusInd Bank), at ₹ 48 crore/branch (HDFC Bank), business per employee of ₹ 7.4 crore (IndusInd Bank) and at ₹ 9.8 crore (HDFC Bank). In contrast, in the same league of private banks, Axis Bank is available at ₹ 48.2 crore Mcap per branch with a better CASA per branch of ₹ 52 crore offering potential for appreciation.

Similarly, among large cap PSU banks, SBI trades at ₹ 14.1 crore market cap per branch while PNB is far distant at ₹ 6.9 per branch offering a

significant gap bridging at least close to BoB trading at ₹ 9.1 crore/branch. Other large PSU banks trade at <₹ 5 crore and nowhere close due to higher stress levels and lower profits.
We have raised our target multiples for banks with the probability of a beta play on a reviving economy, MTM gains on declining G-Sec yields and bridging Mcap per branch gap.

In the RoE and P/ABV bubble chart - Large private banks like HDFC Bank and IndusInd Bank are trading at premium valuations with strong RoE >20%, while Kotak Mahindra Bank is trading rich over 6x P/ABV. Accordingly, the basket of large PSU banks like SBI, PNB and BoB appears strong for upside while Axis Bank, among large private banks, offer an opportunity with reasonable valuations.

Exhibit 3: RoE, P/ABV bubble chart matrix with NIM as size of bubble



Source: Company, ICICIdirect.com Research, Prices as on 19/12/2014

The **Insurance Bill** ordinance has been approved in cabinet and if passed in coming weeks by President, can turn out to be a positive for NBFCs having direct exposure to insurance via joint owned subsidiaries (~74% owned) like HDFC Ltd, Reliance Capital in our NBFC coverage universe and also banks with insurance joint ventures (ownership ~74%) like SBI, Kotak Mahindra Bank, etc.

We maintain our bullish stance on select large PSU banks and expect consistency in private banks to continue with a stable performance. Axis Bank, PNB are our top picks in banking sector in the current environment based on our sector valuation analysis (Mcap/branch). We prefer SBI as it is the market leader with lower stress levels in asset quality.

Expected movement from here-on:

Triggers for PSU bank…

- Ten-year G-Sec yields falling ~60 bps have raised expectations of improved profits in H2FY15 for PSU banks wherein MTM gains will be seen largely in reversal of provisions and trading profits if realised. (4-16% on FY15E PAT - benefit for 40 bps yield decline)
- Plans to bring down the government stake in PSU banks to 52% are more prominent now whereby, in case of continuous dilution over time ₹ 87000 crore of capital can be raised. Issues relating to capital adequacy may be moderated
- Restructuring windows issued by the RBI for existing and new infra loans will ease pressure on future NPA accretions
- Valuations still offer upside from >one year time horizon

Triggers for private bank…

- Valuations to stay rich and continue at P/ABV multiples, consistency in price appreciation for select private banks
- Improving growth and incremental profits to be more beneficial in BV accretion vs. PSU banks as valuation multiples are high
- Capital adequacy at comfortable position for private banks
- Being strong in retail and housing loans, infrastructure bond (providing CRR, SLR, PSL relief) issuances have been rising and can improve NIM

Investment book gains to surge in H2FY15 profit

The benchmark 10 year G-Sec yield has fallen to ~7.91% currently, which is a decline of ~60 bps, since the beginning of Q3FY15. The same decline during the entire Q2FY15 was 23 bps. During Q3FY15, inflation declined faster than expected (CPI down to 4.38% in November 2014) and global commodity prices, particularly crude, remained subdued. This has underpinned the belief that inflation is now structurally on a glide path. This, in turn, has enhanced expectations of rate cuts by RBI in CY15.

Such a sharp fall in bond yields and consequent increase in bond prices augurs well for the investment portfolio of banks, especially in case of PSU banks, as they can book gains and/or reduce their MTM provisions on such portfolio. However, we believe, during Q3FY15 such a benefit would not reflect much in their other income but would be reflected in the form of reduced provisions. As rate cuts are expected to happen in CY15, G-secs would witness a further decline. Probably, during Q2FY16, we expect banks to book profits on their bond portfolio.

In our coverage universe, for a 40 bps yield movement, FY15E PAT of PSBs will be impacted positively by 5% to 13% with PNB, Dena Bank and Syndicate Bank being major beneficiaries. Private banks will be impacted by 1.2-5.8% with Axis Bank and J&K Bank witnessing a higher impact.

Exhibit 4: Sharp decline in G-sec yields to help banks raise MTM and trading gains from AFS investments ….

Q2FY15 Banks	Investment book (₹ crore)	AFS (₹ crore)	Modified duration (in years) AFS	Impact of yield movement of 40 bps (₹ crore)	Impact of yield movement of 30 bps (₹ crore)	PAT (₹ crore) FY15E	Impact on PAT of 40 bps yield movement (%)	Impact on PAT of 30 bps yield movement (%)
Public sector banks								
Bank of India	115,813	13,567	3.8	208.4	156.3	2,976	4.9	3.7
Bank of Baroda	129,927	18,024	3.1	224.9	168.7	5,844	2.7	2.0
Dena Bank	34998	4866	3.9	76.7	57.5	423	12.7	9.5
PNB	141,528	44,112	3.5	622.9	467.1	3,740.1	11.7	8.7
SBI	485,734	109,954	2.3	1,011.6	758.7	13,817	5.1	3.8
Syndicate Bank	61,096	16,024	4.6	294.8	221.1	1,561	13.2	9.9
OBC*	58,284	13,794	4.7	258.8	194.1	1,340	13.5	10.1
Canara Bank*	146,395	43,716	4.3	743.2	557.4	3,100	16.8	12.6
Private sector banks								
Axis Bank	114284	33371	3.5	461.9	346.4	7094	4.6	3.4
City Union Bank	6,900.5	1,358.0	1.9	10.5	7.9	391.8	1.9	1.4
DCB	3,340	630	1.2	3.0	2.3	176	1.2	0.9
J&K Bank	23,626.2	7,854.5	2.3	72.3	54.2	867.5	5.8	4.4

*Source: Company, ICICIdirect.com Research, * Not under coverage, AFS- Available for Sale*

Government holding up to 52% if approved, capital booster over time

The Union Cabinet recently approved the proposal to pare down its equity holding in PSU banks to 52%. However, the bill is yet to be passed in Parliament. In the press release, the government said "*while permitting banks to raise capital from the market, banks would be advised to preserve the government holding at minimum 52% and increase the public shareholding in a phased manner through the issue of shares largely to retail investors that is to common citizens of this country".*

The government's idea seems to be to maintain its control on PSU banks as well as improve their performance by making structural changes in the functioning of state owned banks. Further, it wants retail investor participation to increase as shares will largely be issued to them.

In our analysis, we observed that nine banks have government holding in excess of 70% while the rest have between 50% and 70%. As per our calculations, selling government's stake in excess of 52% in the market would help PSU banks raise only ~₹ 47500 crore based on current market capitalisation. However, if fresh issue of shares to public is done to bring down the government's stake to 52%, the funds that can be raised gets enhanced to ₹ 87000 crore.

It should be noted that the above estimated amount will be raised in a phased manner and not in the short-term. This is because, as stated earlier, in case the holding in some banks is above 80% then paring it to 52% will be a gradual process than in one go. Further, the amount may also be higher than estimated by us as we have based our calculations on current market capitalisation, which may increase, going ahead.

Exhibit 5: Possible capital raising- if government sells PSU banks stake directly or with fresh issuances indirect dilution, government holding is brought down to 52%

Banks	Mcap	Govt holding (%)	Excess govt stake >52% (%)	Expected capital that can be raised if govt 'sells' its excess stake	Capital raised as % of Networth	Net Worth (₹ crore)	Expected capital if dilution is only via fresh issue of shares (₹ crore)
Allahabad Bank	6,859.4	58.9	6.9	473.3	4.3	10,948.6	910.2
Andhra Bank	5,077	60.1	8.1	413.2	4.7	8,737.5	794.7
Bank of Baroda	45,609	56.3	4.3	1,942.9	5.4	35,987.2	3,736.4
Bank of India	18,709	66.7	14.7	2,750.2	10.5	26,180.2	5,288.9
Bank of Maha	4,418	79.8	27.8	1,228.1	18.3	6,702.6	2,361.7
Canara Bank	20,217	69.0	17.0	3,436.9	14.2	24,121.9	6,609.4
Central Bank	12,417	84.2	32.2	3,998.3	31.0	12,913.1	7,689.0
Corporation Bank	5,259	63.3	11.3	595.9	5.9	10,085.1	1,145.9
Dena Bank	3,079	58.0	6.0	185.0	2.9	6,330.6	355.9
IOB	#N/A	73.8	21.8	#N/A	#N/A	14,356.3	#N/A
Indian Bank	9,199	81.5	29.5	2,714.7	23.5	11,535.6	5,220.6
Oriental Bank	9,564	59.1	7.1	681.9	5.3	12,779.4	1,311.3
Pun. & Sind Bank	2,416	79.6	27.6	667.4	14.1	4,720.5	1,283.5
Punjab Natl.Bank	40,434	58.9	6.9	2,777.8	8.1	34,487.1	1,068.4
St Bk of India	229,720	58.6	6.6	15,161.5	12.8	118,282.3	29,156.7
Syndicate Bank	7,739	67.4	15.4	1,191.0	10.9	10,897.6	2,290.3
Uco Bank	8,037	77.2	25.2	2,025.2	19.0	10,638.9	3,894.6
Union Bank (I)	14,518	60.5	8.5	1,229.7	7.2	17,016.0	2,364.8
United Bank (I)	2,816	78.9	26.9	758.2	17.0	4,448.5	1,458.1
Vijaya Bank	4,042	74.1	22.1	891.7	15.8	5,638.9	1,714.8
IDBI Bank	11,148	76.5	24.5	2,731.1	12.5	21,926.0	5,252.2
Total	#N/A			#N/A			#N/A

Source: Capitaline, Banks, ICICIdirect.com Research, Market Cap as on December 22, 2014

GNPA market share (₹ crore and %)

PSU coverage	Q2FY15	Market share	FY15E
Bank of India	14,127	5.1	15,029
Bank of Baroda	13,058	4.7	14,271
Dena Bank	3,861	1.4	4,175
Punjab National Bank	20,752	7.5	22,785
State Bank of India	60,712	22.0	69,820
Syndicate Bank	6,049	2.2	6,215
Private coverage			
Axis Bank	3,613	1.3	3,827
City Union Bank	338	0.1	368
Development Credit Bank	169	0.1	200
Federal Bank	1,031	0.4	1,191
HDFC Bank	3,362	1.2	3,888
Indusind Bank	655	0.2	788
Jammu & Kashmir Bank	2,187	0.8	2,445
Kotak Mahindra Bank	1,165	0.4	1,407
South Indian Bank	553	0.2	719
Yes Bank	222	0.1	277

Source: Capitaline, Company, ICICIdirect.com Research

*Market share based on 40 banks

Asset quality pressure stays; meaningful respite sill 2-3 quarters away

For the industry, as a whole, asset quality pressure continued. Large PSU banks, ex-SBI, saw a substantial surge in GNPA and NNPA. Total GNPA rose 17% YoY to ₹ 275550 crore forming 4.4% of credit vs. 4.2% with higher provisions continuing. Ex-SBI, GNPA rose 26% YoY for industry and 24.5% YoY for PSU banks. However, the NNPA increased by ₹ 12163 crore to ₹ 156996 crore in Q2 vs. ₹ 7974 crore in Q1. This was the highest addition in the last four quarters. Restructured assets did not witness a substantial increase QoQ. As asset quality pressures continue, provisions surged 27.6% QoQ to ₹ 21407 crore.

In case of our coverage universe, overall fresh slippages were lower sequentially except for PNB and Syndicate Bank in the PSU space and Axis Bank in the private space. In terms of total stressed assets (GNPA + restructured assets) ratio Dena Bank, PNB and J&K Bank are at the highest levels as seen in the below table. For the industry, the stress asset ratio would be ~10.5% with restructured assets forming ~6.1% of credit or ~₹ 375000 crore.

Our discussions with the managements reveal that though the sentiment has improved, an actual improvement on the ground has not taken place as yet. With various stalled projects getting clearances, an actual reflection in terms of improving recovery and decline in closing GNPA is expected to take place only after two or three quarters. As credit growth remains subdued, GNPA and NNPA ratio percentages appear elevated.

We expect GNPA and NNPA growth for our coverage universe at 15% CAGR each to ₹ 162550 crore and ₹ 82651 crore, respectively, by FY16E.

Exhibit 6: Pace of stressed asset addition moderating

Q2FY15	Advances	Restructured assets (₹ crore)	RA to advances (%)	GNPA (₹ crore)	NNPA (₹ crore)	Total stressed (RA + GNPA)	Stressed (%)	GNPA (%)	NNPA (%)	Coverage ratio (%)	FY15E PAT (₹ cr)
PSU Banks											
Bank of India	399,288	11,738	2.9	14,127	9,101	25865	6.5	3.5	2.3	56.3	2,976
Bank of Baroda	385,766	22,417	5.8	13,058	6,705	35475	9.2	3.3	1.7	65.4	5,844
Dena Bank	73,855	8,347	11.3	3,861	2,648	12208	16.5	5.1	3.6	51.9	423
PNB	357,093	34,012	9.5	20,752	11,618	54764	15.3	5.7	3.3	59.1	3,740
SBI	1,209,648	61,249	5.1	60,712	32,997	121961	10.1	4.9	2.7	62.7	13,817
Syndicate Bank	173,845	10,736	6.2	6,049	3,825	16785	9.7	3.4	2.2	65.4	1,561
Private banks											
Axis Bank	242,198	6,690	2.8	3,613	1,180	10303	4.3	0.4	0.4	78.0	7,094
City Union Bank	16,758	250.2	1	338	219	588	3.5	2.0	1.3	61.1	392
DCB	8,793	83	0.9	169	94	252	2.9	1.9	1.1	76.8	176
Federal Bank	48,466	2,400	5.0	1,031	319	3431	7.1	2.1	0.7	85.1	1,016
HDFC Bank	327,273	327	0.1	3,362	917	3689	1.1	1.0	0.3	74.0	10,404
IndusInd Bank	59,931	312	0.5	655	195	966	1.6	1.1	0.3	70.2	1,752
J&K Bank	45,072	1,269	2.8	2,187	1,109	3456	7.7	4.7	2.5	54.9	867
Kotak Mahindra Bank	60,948	160	0.3	1,165	611	1325	2.2	1.9	1.0	53.9	1,700
South Indian Bank	35,871	355	1.0	553	553	908	2.5	0.0	1.6	62.9	503
Yes Bank	62,030	116	0.2	222	54	339	0.5	0.4	0.1	75.8	2,004

Source: Company, ICICIdirect.com Research

Credit growth tottering around lower double digits

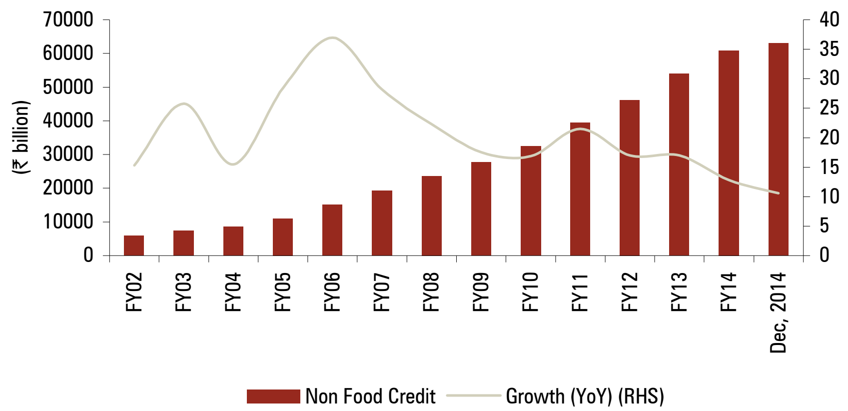
The credit traction of the banking system has continued to remain subdued. It fell to one of the lowest levels in the past decade to 9.7% YoY as on September 2014 before improving a bit to 10.6% YoY (mid-December 2014) to ₹ 6303481 crore. This was largely owing to muted traction in the Industry segment & services segment (accounting for 44% and 23% of total credit, respectively), which increased at a slower rate of 7.8% YoY and 8.9% YoY to ₹ 2540200 crore and ₹ 1357800 crore, respectively, as on October 2014. Personal loans supported overall credit traction by clocking growth of 16.3% YoY to ₹ 1128100 crore.

Within our coverage universe, PSU banks grew 12% YoY dragged lower by SBI, which grew at only 9.7% YoY while excluding SBI, the growth stood at 15% YoY. Private banks maintained their healthy traction of 20% YoY. Overall, our coverage universe grew above industry by 14% YoY to ₹ 3506835 crore as on September 2014.

Incrementally retail loans contributed 43.2% of incremental YTD credit, growing faster at 16.3% YoY as at October 2014

Credit growth is expected to stay muted for FY15, where 13-14% may be a reasonable assumption with retail contributing a larger share. However, during FY16, the credit traction is estimated to be better than FY15 led by corporate capex revival.

Exhibit 7: Credit traction continues to be muted



Source: Company, ICICIdirect.com Research

The RBI in one of its monetary policy statements has also shed light on deceleration in credit growth.

"Partly, this sharp deceleration is on account of a high base – monetary tightening to curb exchange market pressures in July-September last year raised interest rates on alternative sources of funds and pushed up the demand for credit from the banking system. Adjusting for this base effect, non-food credit growth would have been ~11% in September 2014. Corporates have also opted to raise financing through alternative sources such as commercial paper, which are significantly larger than a year ago. Finance from other non-bank sources such as foreign direct investment and external commercial borrowing has also increased. Also, a few banks have sold stressed loans to asset reconstruction companies, and so these loans no longer appear as bank credit. Net bank credit is also lower because of repayments of loans by entities that have received payments by government departments and public enterprises, and because oil marketing companies' borrowing is lower. Finally, the slowdown in credit growth is more pronounced in public sector banks but how much of this is because of needed bank balance sheet restructuring, repayments of stressed loans, or increased risk aversion is to be established. Going forward, as the investment cycle gathers momentum and overall demand picks up, banks will need to prepare to meet financing requirements as the credit cycle also turns."

Annexure

Exhibit 8: Quarterly margin trend – Expect decline to be arrested from H2FY15

NIM (%)	Q2FY13	Q3FY13	Q4FY13	Q1FY14	Q2FY14	Q3FY14	Q4FY14	Q1FY15	Q2FY15
PSU coverage									
Bank of India	2.4	2.4	2.5	2.5	2.3	2.4	2.3	2.2	2.3
Bank of Baroda	2.7	2.7	2.5	2.4	2.3	2.4	2.3	2.4	2.4
Dena Bank	2.9	2.9	2.5	2.6	2.6	2.7	2.3	2.2	2.3
Punjab National Bank	3.5	3.5	3.5	3.5	3.5	3.6	3.2	3.4	3.2
State Bank of India	3.5	3.4	3.3	3.2	3.2	3.2	3.2	3.1	3.1
Syndicate Bank	3.3	3.3	3.0	2.8	2.9	2.8	2.8	2.5	2.6
Private coverage									
Axis Bank	3.5	3.6	3.7	3.9	3.8	3.7	3.9	3.9	4.0
City Union Bank	3.3	3.5	3.4	3.6	3.5	3.6	3.3	3.3	3.5
Development Credit Bank	3.2	3.4	3.5	3.4	3.7	3.6	3.6	3.7	3.7
Indusind bank	3.3	3.5	3.7	3.7	3.7	3.7	3.8	3.7	3.6
Federal Bank	3.6	3.5	3.1	3.1	3.3	3.2	3.6	3.3	3.4
HDFC Bank	4.2	4.3	4.5	4.6	4.3	4.2	4.4	4.4	4.5
Jammu & Kashmir Bank	3.9	4.1	4.1	4.2	4.3	4.0	4.1	3.6	4.0
Kotak Mahindra Bank	4.6	4.6	4.6	4.8	4.9	4.9	4.9	5.0	5.0
South Indian Bank	3.1	3.2	3.2	2.9	3.1	3.0	3.0	2.7	2.8
Yes Bank	2.9	3.0	3.0	3.0	2.9	2.9	3.0	3.0	3.2

Source: Company, ICICIdirect.com Research

Exhibit 9: Financials of industry as on Q2FY15 (listed banks + SBI associates)

(₹ crore)	Q2FY15	Q1FY15	Q4FY14	Q3FY14	Q2FY14	Q1FY14	YoY (%)	QoQ (%)
NII	67664	65868	65203	63201	61352	59406	10.3	2.7
Growth YoY	**10.3**	**10.9**	**12.8**	**11.5**	**12.8**	**10.7**		
Other income	25275	24101	29792	22375	20562	26808	22.9	4.9
Growth YoY	**22.9**	**-10.1**	**9.4**	**7.9**	**9.4**	**44.2**		
Total operating exp.	45188	42072	42899	41376	40683	38724	11.1	7.4
Staff cost	24700	24152	23178	23446	23043	22796	7.2	2.3
Operating profit	47751	47898	52096	44200	41231	47490	15.8	-0.3
Growth YoY	**15.8**	**0.9**	**15.6**	**3.0**	**3.8**	**17.3**		
Provision	21407	16776	25670	21446	21580	18438	-0.8	27.6
PBT	26328	31108	26406	22736	19638	29042	34.1	-15.4
PAT	18207	20919	20007	15353	14145	20276	28.7	-13.0
Growth YoY	**28.7**	**3.2**	**-0.9**	**-21.1**	**-25.0**	**1.9**		
GNPA	275550	258228	248210	249795	235273	213299	17.1	6.7
Growth YoY	**17.1**	**21.1**	**35.1**	**36.8**	**38.1**	**40.7**		
NNPA	156996	144833	136859	142197	131695	117201	19.2	8.4
Growth YoY	**19.2**	**23.6**	**44.5**	**51.4**	**52.5**	**60.9**		

Source: Capitaline, Company, ICICIdirect.com Research

ICICIdirect.com coverage universe (Banking)

	CMP			M Cap	EPS (₹)			P/E (x)			P/ABV (x)			RoA (%)			RoE (%)		
Sector / Company	(₹)	TP(₹)	Rating	(₹ Cr)	FY14	FY15E	FY16E	FY14	FY15E	FY16E	FY14	FY15E	FY16E	FY14	FY15E	FY16E	FY14	FY15E	FY16E
Bank of India (BANIND)	300	317	Buy	17,937	42	46	55	7.1	6.5	5.5	0.9	1.0	0.9	0.5	0.5	0.5	10	10	11
Bank of Baroda (BANBAR)	1,071	1,250	Buy	45,133	105	136	160	10.2	7.9	6.7	1.6	1.4	1.2	0.8	0.8	0.8	13	15	16
Dena Bank (DENBAN)	58	60	Hold	3,141	10	9	14	5.7	6.9	4.1	0.7	0.8	0.8	0.5	0.3	0.5	9	6	10
Punjab National Bank (PUNBAN)	223	279	Buy	7,874	18	21	25	12.1	10.8	8.9	1.6	1.6	1.4	0.6	0.6	0.7	10	10	11
State Bank of India (STABAN)	308	374	Buy	230,243	15	19	21	21.1	16.7	14.5	2.6	2.4	2.2	0.6	0.7	0.7	10	11	12
Syndicate Bank (SYNBN)	126	141	Hold	7,593	27	25	32	4.6	5.0	3.9	1.0	1.0	0.9	0.7	0.6	0.6	15	13	15
Axis Bank (UTIBAN)	497	550	Buy	117,251	26	30	34	18.8	16.5	14.7	3.1	2.7	2.4	1.7	1.7	1.7	17	17	17
City Union Bank (CITUNI)	93	100	Hold	4,498	6	7	9	14.5	14.0	10.8	2.8	2.2	1.9	1.4	1.4	1.6	19	17	17
Development Credit Bank (DCB)	121	124	Hold	3,145	6	6	7	20.1	19.3	17.0	3.0	2.4	2.2	1.3	1.2	1.2	15	13	12
Federal Bank (FEDBAN)	148	164	Buy	12,663	10	12	14	15.1	12.5	10.4	1.9	1.7	1.5	1.2	1.3	1.3	13	14	15
HDFC Bank (HDFBAN)	951	1,036	Hold	226,974	35	41	50	26.9	23.0	18.9	5.3	4.0	3.4	1.9	1.9	2.0	21	20	19
Indusind Bank (INDBA)	783	845	Buy	41,038	27	33	41	29.2	23.5	18.9	4.7	4.0	3.4	1.8	1.8	1.9	17	18	19
Jammu & Kashmir Bank(JAMKAS)	150	152	Hold	7,264	24	18	28	6.1	8.4	5.4	1.3	1.4	1.2	1.6	1.0	1.4	22	14	19
Kotak Mahindra Bank (KOTMAH)	1,244	1,250	Hold	95,368	20	22	26	63.8	56.4	48.3	8.0	7.2	6.3	1.8	1.8	1.8	14	13	13
South Indian Bank (SOUINO)	28	28	Hold	3,738	4	4	4	7.4	7.5	6.9	1.3	1.2	1.1	1.0	0.8	0.8	17	14	15
Yes Bank (YESBAN)	744	797	Hold	30,960	45	48	62	16.6	15.4	12.0	3.8	2.7	2.2	1.6	1.7	1.8	25	21	20

Source: Company, ICICIdirect.com Research

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Pankaj Pandey **Head – Research** **pankaj.pandey@icicisecurities.com**

ICICIdirect.com Research Desk,
ICICI Securities Limited,
1st Floor, Akruti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

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