

**Yes Bank Ltd**

April 29, 2008

CMP:Rs.167

Target Price:Rs.233

Recommendation: BUY

BSE Code	532648
NSE Symbol	Yes BANK
Bloomberg code	YES IN
Reuters code	YESB.BO
ISIN	INE528G01019

Yes bank is one of the leading private sector bank in India and has shown robust growth. With a network of 67 branches across 57 locations it has built up a strong client base in the corporate sector. Its knowledge driven banking approach is unique in the industry and built up a strong relationship with its clients. Looking at its exponential growth in the business mix and consistency in profitability we believe the stock is undervalued and provides an investment opportunity for decent return in the short/medium term.

**Company Report**
**Key Data**

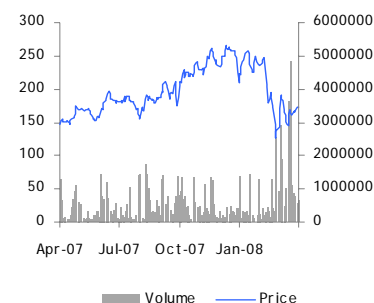
Sensex	17125.98
52 week H/L	277 / 120
Outstanding Shares (mIn)	295.79
Avg. Wkly Volumes (shrs)	431,903
Market Cap (Rs mIn)	49,396.93
Face value	10

Source: Capitaline

**Share Holding Pattern (%)**

Promoters	33.97
Institutions	0.87
FII's/NRI's	55.86
Non Promoter Corp. Hold	1.49
Public & Others	7.82

Source: Company

**Price Volume Analysis**


Source: Capitaline

**Investment Rationale**
**Wholesale Banking: Growing Business through Knowledge Banking Approach:**

We believe the wholesale banking segment will be the main value driver for the growth of the Yes bank. This segment not only contributes to the interest income but also to its other income. Yes bank is able to leverage its relationship with its customers to provide fee based services such as forex derivative, financial market consultancy and other value added products which eventually result in maintaining 50:50 ratio between net interest income and fee based income.

**Deposit Growth & CASA ratio:**

We expect the bank's deposit to grow at a CAGR of 61% till FY10E compared to 23.1% in the industry mainly because of new branch rollout. The higher growth is also accompanied by high proportion of CASA ratio. We expect bank to report 12.5% CASA in FY09E and 15% in FY10E. the growth in deposits is low compared to last year but the difference is because of the branch compositions.

**Profitability & Margins are to be Maintained:**

We expect net interest income to grow at CAGR of 45.4% and net profit to grow at CAGR of 36.3% in during FY08A-FY10E. NIM margin is expected at 2.7% in FY09E and 3% in FY10E. After considering the equity dilution of 20mn equity shares, EPS for the bank would stand at Rs.9.7 in FY09E and Rs.15.2 in FY10E. The book value will stand at Rs.64.2 in FY09E and Rs.85.7 in FY10E.

**Valuation:**

With a strong growth in profitability (37% CAGR) and maintenance of NIM at 3%, we value the bank at Rs.233 which will discount the FY10E book value by 2.7 times. The target price is also justified by PEG ratio of 0.65.

**Financial Summary**

(Rs in Million)

Year	NII	Non Int Income	PAT	EPS	Book Value	P/BV
2007	1713.5	1945.7	943.7	3.4	28.1	6.2
2008	3367.1	3545.3	2000.2	6.8	44.6	3.7
2009E	5892.1	5438.9	3066.6	9.7	64.2	2.6
2010E	10497.4	9689.9	5138.5	15.2	85.7	1.9

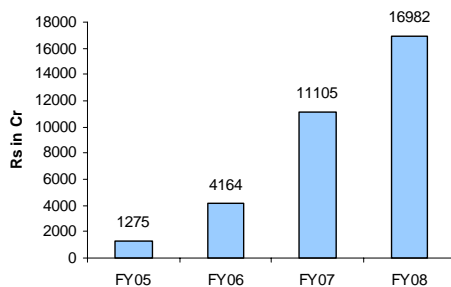
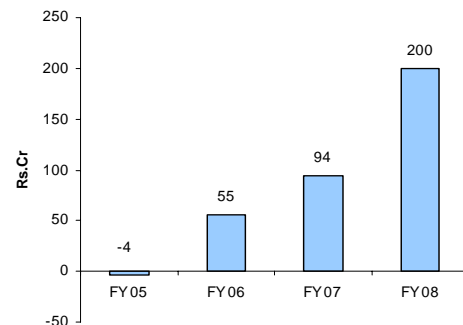
Source: ULJK Research

**ULJK Research**

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**Background:**

Yes Bank is promoted by Mr. Rana Kapoor in 2004. Since its inception, the bank has shown consistent growth in its business mix and profitability. Since FY06 the total assets of the bank has grown at CAGR of 202%, Net profit has grown at CAGR of 190% and their branch network has increased from 7 branches in FY06 to 67 branches in FY08. Its emphasis on knowledge banking which focuses to provide financial assistance to its customers and also provide knowledge of the particular sector, gives it a niche position in the market. Mr. Rana Kapoor has built up a strong management with well-known professionals from the financial services industry. As on 31<sup>st</sup> March 2007, it has network of 67 branches, 75 offsite ATMs and 2 Central Processing Centers at Mumbai and Gurgaon.

**Asset Growth**

**Net Profit Growth**


(Source: ULJK Research, Company)

**Business Segments:**

Yes bank has strategically carved out its revenue generation segment over a period of time. It enters each segment only after it has secured appropriate infrastructure support to service that segment. This strategy is evident from its branch presence in NCR and Mumbai, which helps it to concentrate more on wholesale banking. The classification of the different business segments are as under.

**Revenue Breakup of Segments in FY08**

Particulars	%age
Treasury Operation	34.4%
Corporate Banking	55.0%
Retail Banking	7.3%
Other Operation	3.3%

(Source: ULJK Research, Company)

**Treasury Operation:** Treasury operation focuses on the service related to financial market like forex derivative, credit derivative transaction on behalf of bank customers and proprietary trading.

**Corporate Banking:** This segment is focused on lending and borrowing to corporate clients including services like Project Finance, financial restructuring and cash management services.

**Retail Banking:** This segment is very small in terms of total business as the bank is not keen to actively develop it. Operation includes selling of wealth management products and small business loans to professional and small entrepreneurs.

**Other Banking Operation:** Yes bank is also active in third party product sale like Mutual Funds, Insurance and other Financial Service products. This segment contributes in range of 12%-14% of the non interest income during last several quarters. Once the branch network got established and operations picks up, a larger contribution of income from this segment is expected.

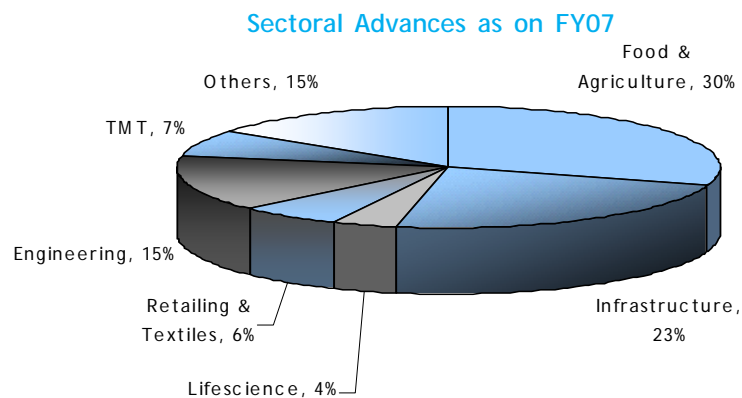
**Investment Rationale:**

**Wholesale Banking: Growing Business through Knowledge Banking Approach...**

Yes bank focuses more on wholesale banking, which includes providing banking services to large and mid size corporate customers. Its services include working capital finance, trade and transactional services, treasury services and investment banking solutions. To cater to this high growth and competitive market, the bank has adopted a knowledge-driven banking approach. It not only lends to its customers, but also provides in dept knowledge about the sector and the business. This knowledge-driven approaches helps the bank to cater to each segment with customized solution, helping it to build a strong relationship with its clients. The bank has come out with reports on sectors like Agriculture, Infrastructure, Life Science, Information Technology and Media helping the bank to attract more clients from these sectors which are on high growth trajectory.

We feel Yes Bank has carefully structured its wholesale banking business and is taking strategic steps to cater to this segment. With Curb's on external commercial borrowing (ECB's) for more then \$20mn in place, Indian companies are more likely to look for raising debt in the domestic market. This provides an opportunity for the bank to grow its business by leveraging its access to funds and the strong relationship it enjoys with the Indian corporates. The segment also provides greater security in terms of low NPA as compared to retail segment. The bank has segmented its client base on the basis of their revenue to have clear focus on each category of of clients viz Emerging Corporate Division and Business Banking Division. Its Emerging Corporate Division caters to customers having Revenue of Rs. 1000mn to Rs. 7500mn and Business Banking division caters to customers having revenue in the range of Rs. 100mn to Rs. 1000mn. The branch network is also strategically built in the business and industry centric region.

Yes Bank has strategically built its advance portfolio based on its knowledge and growth scenario for the particular sector and that too while meeting with the priority sector lending norms. The 30% of advances to Food & Agri business and 23% to infrastructure sector indicate the management strategy towards its lending mix. But we feel the concentrated advance portfolio is a risky strategy as any slowdown in the high advance sector may hinder the business growth for the bank and the chances of sector non performing when the lean period is high.



(Source: ULJK Research, Company)

**Merchant Banking Business is a Focus Area for Yes Bank:**

The Bank has built up a strong investment banking division which provides services in the field of M&A, private equity and IPO syndication and advises corporates on getting long term finance for their projects. So far, the division has completed approx 24 M&A transaction, 14 Private Equity Syndication and 19 capital markets & acquisition financing. We believe Yes bank will be able to develop its investment banking business by leveraging its knowledge banking approach, creditability with financial corporation and its ability to handle legal issues effectively with help of relationship with prominent legal and tax firms.

We believe the wholesale banking segment will be the main value driver for the growth of the Yes bank as the segment not only contributes to the interest income but also to non interest income. Leveraging its relationship with customers to provide fee based service like forex derivative, financial market consultancy and other value added product will boost the non interest income and results in maintaining good balance between Net interest Income and Fee based income.

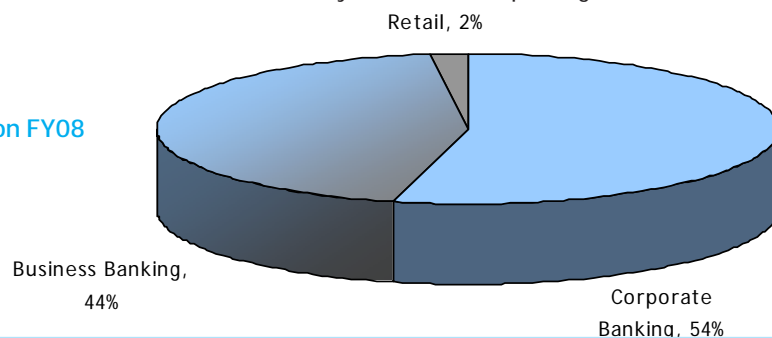
**Retail Banking: Still Out of Radar to Avoid High Risk**

Yes bank is not active on the retail banking front in terms of offering products like Personal Loan, Credit Card as it believes the segment is of high risk business. Management is not keen to increase the retail business at present. However, they are having some trial operation with a small portfolio of personal Loan which is of just Rs.30Cr. Overall retail portfolio is just 2% of the total loan portfolio which include business loan to individual in the range of Rs.5Lac to Rs.30Lac. As per the management, this business segment has high probability of assets turning into NPA.

Yes Bank' has adopted a deposit centric strategy for its retail business. It is targeting to mobilize deposits by selling of wealth management products and investment advisory services to its clients. The bank has tied up with all the AMCs in India for selling of their mutual fund products. Clients can invest directly in mutual fund schemes of 15 AMCs online. In insurance space, it has tied up with Max New York Life and Bajaj Allianz for life insurance and general insurance respectively. In spite of slower presence, the bank is providing technological advanced services to its customers. Its net banking service has RTGS and NEFT facilities. The concept of 7:11 banking in residential and small commercial areas help customers to visit branch at their convenient time.

Looking at the high NPA level of private sector banks like ICICI(1.5%), CBOP (1.7%) and Kotak Bank(1.55%) ,which have active presence in retail banking; we feel that Yes bank's strategy to go slow on the retail lending business is justified. However, this could lead to lower acceptance among the customers and may hinder its deposit growth.

Advance Portfolio as on FY08



(Source: ULJK Research, Company)

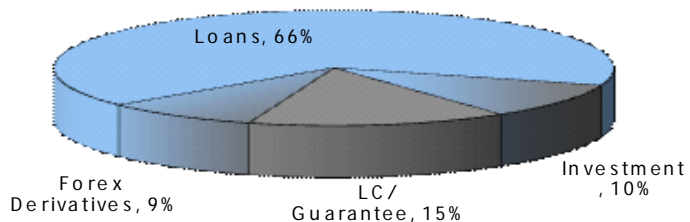
**Forex Derivative Business : The Hype and the Truth:**

Recently there was a media buzz in the market about the huge forex losses for the bank due to default by its clients. The buzz was also supported by depreciation in dollar against major currencies like Yen, Euro and Pound. The buzz seemed to be realistic because the bank has a good amount of exposure in forex derivative transaction as can be seen from non interest income.

Bank management has cleared all the media buzz when they announced the Q4FY08 result which reveled a good set of numbers and virtually no losses from the derivative business. Even though company has reported NPA in this quarter, this was related to personal loan and agricultural loan. According to the Bank Management, it has in total 130 clients in derivative segment. 70% of the total forex exposure is to large corporates having revenue of more then Rs.7500mn and 30% to medium size corporates having revenue between Rs.1500mn to 7500mn. This classification has helped the bank to manage the risk on a/c of derivative losses. The only loss reported was from one client who has taken legal steps in September 2007. But bank has already settled the issue by out of court settlement.

We believe that the bank management is quite clear in their business model in restricting derivative services to select clients on basis of profile of their customers to large & small corporates. As a matter of policy bank has not offered the services to SME clients and has thereby able to manage the risk of default. Also,only 9% of the total Risk Weighted Assets are in to forex derivatives, which is a strong point for its business. Though, there is a provision of recording NPA over 90 days,as per bank management, they are not witnessing any problem in collecting dues and clients are constantly maintaining their margins. Given the recent performance and its revenue classification approach in servicing clients, we believe the Yes Bank management is well prepared to tackle the situation without affecting the company fundamentals.

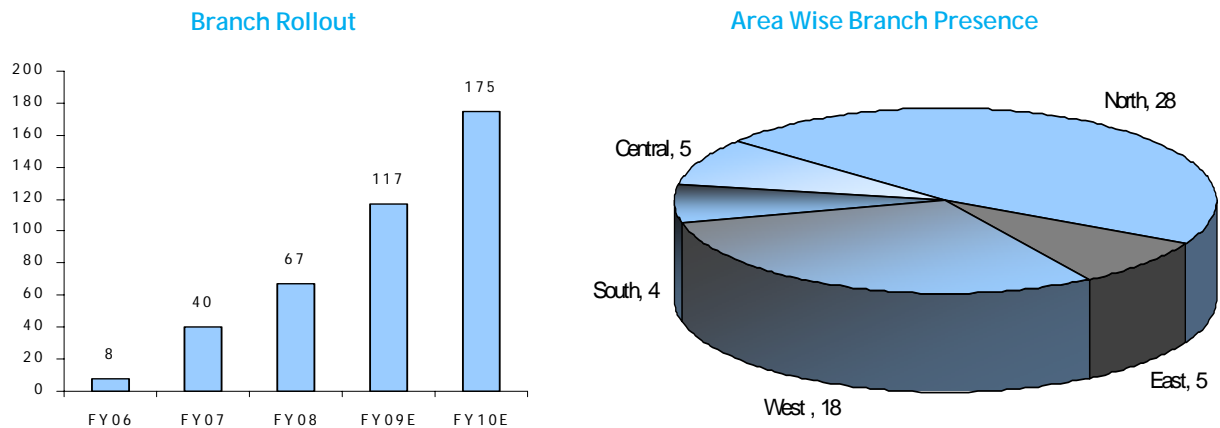
**Classification of Risk Weighted Assets as on FY08**



(Source: ULJK Research, Company)

**Branch Network : Cut in target but still well positioned to achieve the growth rate.**

Yes bank has revised the branch target for FY09 and FY10 to 117 and 175 branches from the previous target of 175 and 250 respectively. The bank has cited regulatory and legal hurdles for the cut in branch roll out. However, this drop will not have significant loss in business growth as the bank is not focusing on the retail business segment. The branches are mainly used for increasing its deposit resources and selling its wealth management products. These new mid or small branches will help the hub branches in carrying over its business. In spite of the cut in the branch rollout, Yes Bank targets to achieve the 250 branches by September 2010, effectively delaying the expansion plan by six months.



(Source: ULJK Research, Company)

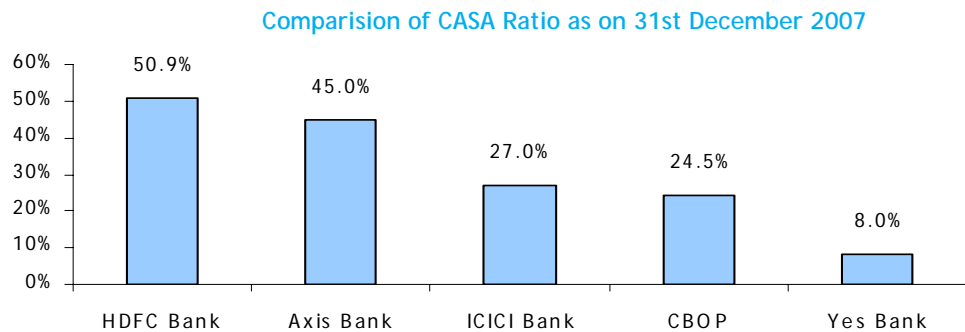
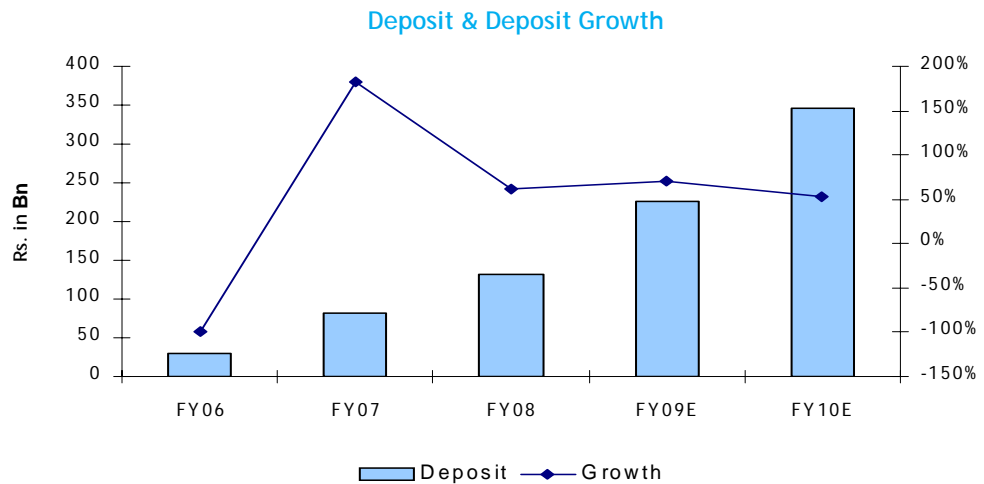
**Growth in Deposit Mix :**

Deposits act as a raw material for the banking business and have a considerable impact on cost of the funds, thereby affecting the margin and profitability of the bank. A high CASA ratio helps in reducing the interest cost, thereby increasing spreads. Yes bank is constantly increasing its deposit base by expanding its branch locations and also attracting customers by offering higher interest rates. It has reported a CAGR of 114% in deposit for period FY06A-FY08A. As the average age of the branches is very low (less than 12 months) and bank is constantly rolling out new branches, we feel the growth in deposit will continue going ahead but with a slower pace. We expect a CAGR of 61% in deposit till FY10E.

CASA as a percentage of total deposit was at 8.5% in FY08 and the bank is taking every step to increase it to 12.5% in FY09 and 15% in FY10. It aims to achieve a CASA ratio of 20% by FY10-FY11. We feel the bank will be able to achieve its targeted CASA ratio on back of its branch rollout programme.

Even the CASA ratio of the bank is quite low compared to industry peers, we feel once the branch network is in place, deposit mobilization will not seem to affect the growth of the bank. As Yes Bank is a recent entrant in the banking business and its CASA is growing at triple digit growth

(138.5% in FY08), there is every reason to believe that it will be able to increase its CASA proportion going ahead once all its branch network get set.



(Source: ULJK Research, Company)

**Profitability : Margins are Expected to be Maintained With Consistent Growth:**

In spite of being a new entrant in the private banking sector, Yes bank has not only been able to manage its profit growth but also managed to maintain the NIM margin on par with its Industry peers. During FY06 to FY08, it has reported 90% CAGR in net profit which increased from Rs.553mn in FY06 to Rs.2000mn in FY08. The growth in net profit is supported by the high content of non interest income in its total income which the bank earns on various fee-based service provided to customers including forex derivatives, financial advisory and other financial services. The bank’s management is well focused to grow the fee based business segment, which help bank to achieve a distinct place in the traditional banking market.

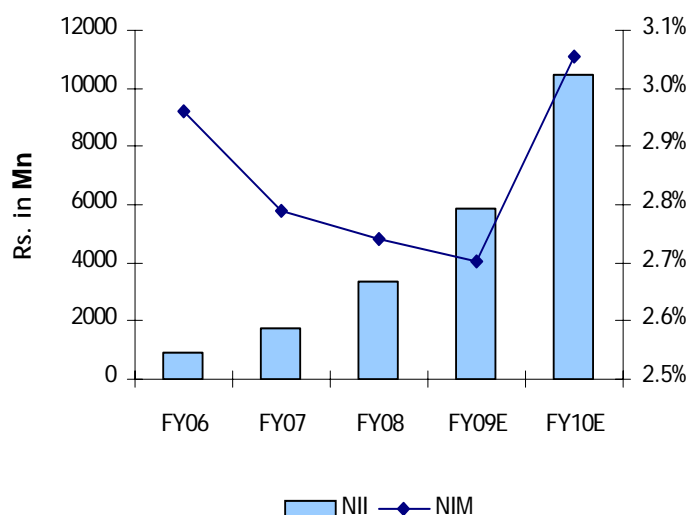
Yes bank has registered CAGR of 56% in Net Interest Income during FY06A-FY08A and maintained a NIM margin at 2.74% during FY08. We expect net interest income to grow at CAGR of 45.4% during FY08A-FY10E supported by a consistent growth in advances and investment and improved CASA ratio, reducing the cost of funds. CASA of the bank stands at 8.5% and grown at the rate of 138.2% during FY08. As the bank will be adding 57 new branches, we expect a surge in CASA ratio during the period, which may reach up to 15% level during FY10E. We expect the bank to maintain NIM margin at 2.7% in FY09E and 3.0% in FY10E. Over all NIM is expected to grow at the rate of 45.5% during FY08A-FY10E.



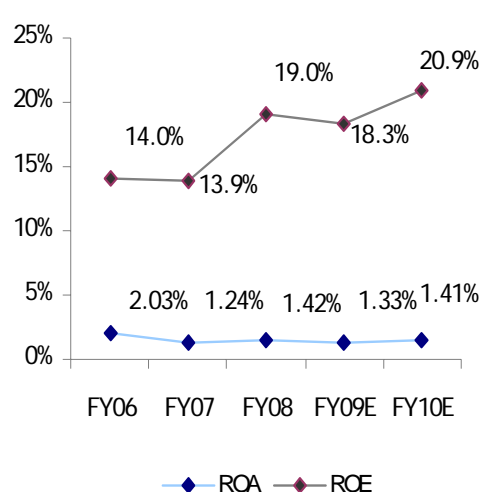
During the period FY06-FY08 non-interest income has contributed to the range of 51%-53%. We expect the same trend to continue in future as the bank has already made a good presence in the market and has built its non-interest income portfolio with constant management focus. The focus to increase non interest income will result in de risking its business from the change in the interest rates in the economy. The major part of this segment income comes from Financial Advisory Services and Financial Market Services, which include service like Forex derivatives, Forex transaction on behalf of clients and other capital market operation. These two services contributes approx 68% of the total non-interest income.

Overall we expect a CAGR growth of 36.3% in net profit till FY10 taking net profit to Rs.5063mn in FY10E from Rs.2000mn in the recently concluded financial year FY08, reflecting the growth prospect and value proposition of the company. We expect the bank to post EPS of Rs.9.68 in FY09E and EPS of Rs.15.25 in FY10E.

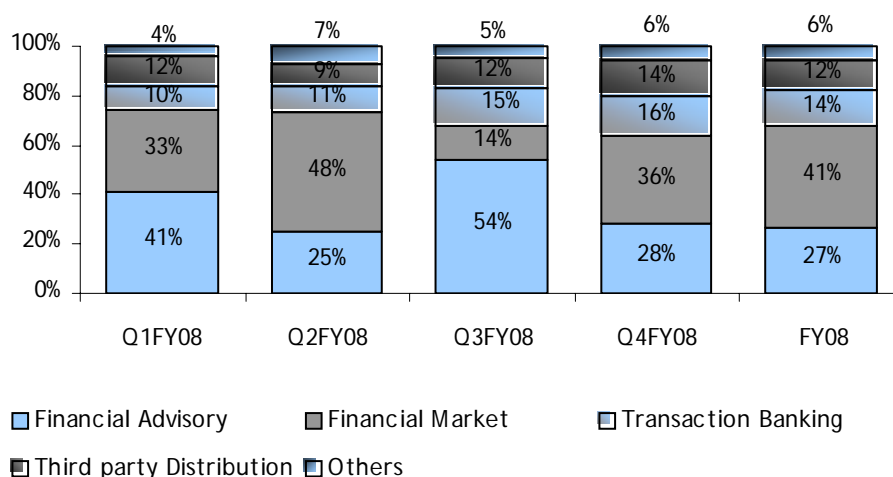
NII and NIM



ROA and ROE trend



Non Interest Income Composition



(Source: ULJK Research, Company)



### Q4FY08 Result:

The Q4FY08 result cleared the much-hyped buzz on the potential derivative losses, which market was talking about in recent times, one of the prime reason for poor performance of the stock. The net profit stood at Rs.645mn registering YoY growth rate of 108.7% and QoQ growth of 18.9%, supported by consistent growth in interest Income which stands at Rs.3884.8mn. The CASA ratio is slowly picking up and stands at 8.5%. Even on low CASA ratio compared to its peers, it is able to maintain NIM at 3.06% in line with industry peers. The Advance growth at 50% and Deposit growth at 61.5% is well placed and we expect the bank to drive this growth on the back its new branch rollout as well as from old branches as they are still at very young stage. The only point of concern we think is the declining CAR ratio. The CAR ratio stands at 13.6%, a decline of 60 basis point QoQ from 14.2%, which is near to its CAR maintenance target of 12.5% to fetch the same credit rating for its CD programme. The board has already approved the fresh issue of 2Cr of equity shares and it is expected to mop up the amount any time during mid FY09. But given the market condition, how the management will be able to get funding at good rate is important to watch. Overall we feel Q4FY08 was a good show from the bank and growth rate in profitability will continue in future.

### Quarterly Performance..

(Rs.in Mn)

Particulars	Q4FY08	% Change YoY	% Change QoQ	Q3FY08	Q4FY07
Net Interest Income	1084.8	134.2%	16.6%	930.4	463.1
Non Interest Income	1058.2	34.4%	9.3%	968.2	787.3
<b>Total Income</b>	<b>2143.0</b>	<b>71.4%</b>	<b>12.9%</b>	<b>1898.6</b>	<b>1250.4</b>
Operating Expenses	933.7	43.0%	5.0%	889.2	652.8
<b>Operating Profit</b>	<b>1209.3</b>	<b>102.4%</b>	<b>19.8%</b>	<b>1009.4</b>	<b>597.6</b>
Provisions & Contingencies	228.4	80.1%	45.3%	157.2	126.8
Provision for Tax	335.9	107.6%	8.4%	309.8	161.8
<b>Profit After Tax</b>	<b>645.0</b>	<b>108.7%</b>	<b>18.9%</b>	<b>542.4</b>	<b>309.0</b>

### Strong Management Team:

Yes bank has built a strong management team leading the bank to achieve a faster growth. Over the past four years since its inception, the bank is able to attract quality professionals to its management team who come with good amount of experience from prominent organization like Rabo Bank, Bank Of America, HDFC Bank, ICICI Bank etc. The strong management team at the senior level and quality talent at the middle level help the bank to increase its execution capability. Qualified personnel are extremely important for its approach of knowledge banking.

Banking sector require a quality talent base to serve clients with different products and requires a good understanding of other sectors and economy. We believe that the Yes Bank management is well experienced in the financial services market and will certainly lead on its growth trajectory.

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**Outlook:**

Since its inception, Yes Bank is able to maintain its business growth through one financial year to another and achieved a high double-digit growth in net profit since FY06. Concentrated focus on the wholesale banking business and introduction of value added service will help Yes Bank to achieve a commendable growth rate in the near future. Once its branch roll out programme, which is taking shape, is developed we will see a mature and consistent growth in its business. Presently, its branches are at very young age -- less than 12 months- which gives further visibility for growth in its business mix. Yes Bank's advances are more into the growing sectors of the economy like Agriculture & Food sector and Infrastructure sector. Food industry is witnessing growth on the back of retail growth as well as nuclear family model which demands more processed foods for readymade cooking. The agricultural sector is also booming with activities as big corporates are entering into farm cultivation and investing heavily into supply chains. Infrastructure spending in India is also witnessing a surge of activities and many public private projects are coming up in this sector in the next few years. The Government has planned an investment of \$500bn, in the Infrastructure space over the eleventh five year plan. All these surge in the respective sectors give boost to the prospect of the business for the bank. Keeping in mind all these value drivers we feel that yes bank is well positioned in its business segment and is well positioned to achieve the targeted growth rate.

**Concern:****Much Emphasis on Wholesale Banking:**

Yes bank's operation is fully concentrated on the wholesale banking front which has an inherent risk of competition and any slowdown in the sectors may affect its income growth. Shying away from retail banking may result in losing considerable opportunity of growth from that sector.

**Concern Over CASA Ratio:**

CASA ratio for the bank is very low compared to other private sector banks which may negatively affect the cost of funds. Further delay in branch expansion may significantly affect the CASA ratio.

**Capital Raising Plan:**

The bank has planned to increase its capital in mid FY09 but given the current capital market situation the fund raising plan may face some serious difficulties. The capital raising is also crucial for the bank as it wants to maintain the CAR ratio at 12.5% level.

**Inability to meet Expansion Target :**

The bank will be unable to meet its branch expansion plans for FY09E and FY10E. Constant revision of branch expansion may slow down its deposit growth which is essential part of its strategy for future growth.

**Valuation:**

In spite of being a new entrant into the banking business, Yes bank has achieved a faster growth in its business mix and is able to manage its profitability level which is in line with industry peers. At Rs.173 the stock trades at a P/BV 2.6x and 1.9x on FY09E book value of Rs.64.17 and FY10E book Value of Rs.85.72 respectively. With a strong growth in profitability (37% CAGR) and maintenance of the NIM at 3% we value Yes bank at Rs.233. At the target price the stock will be the FY10E book value by 2.7times, also justified by PEG ratio of 0.65. Most of the private sector banks are trading in the range of 2x to 3.3x of their respective FY10E book value. We believe Yes bank is well placed on growth trajectory and is well positioned to capitalize on the growth opportunities available in the Indian banking sector particularly, in to wholesale banking. Thus we recommended BUY for Yes bank stock at current level with a target price of Rs.233 over a short to medium term horizon.



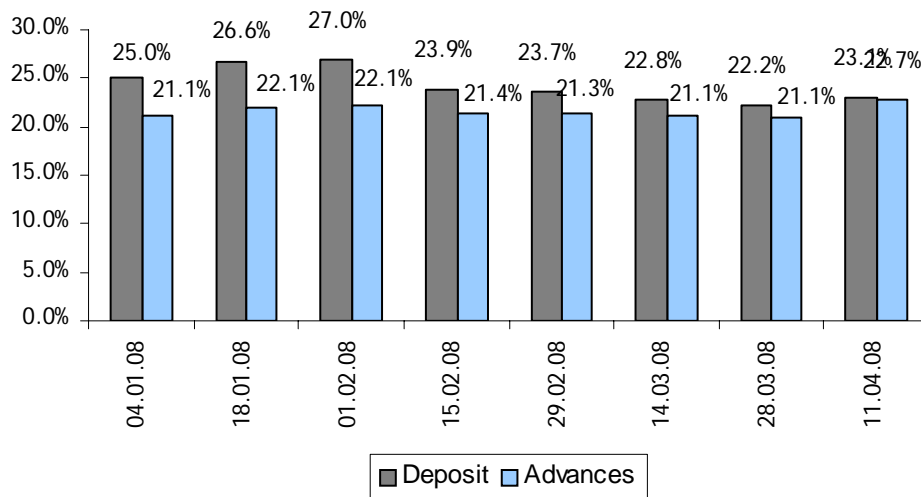
## Annexure

### Valuation Matrix

	CMP	Book Value		EPS		P/BV		PE	
	28.04.2008	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E
ICICI Bank	899.10	461.63	509.00	47.00	62.00	1.95	1.77	19.13	14.50
HDFC Bank	1506.00	342.80	441.00	56.65	45.00	4.39	3.41	26.58	33.47
Axis Bank	917.00	310.82	310.00	51.62	67.00	2.95	2.96	17.76	13.69
Kotak Bank	780.30	204.88	251.00	36.89	51.00	3.81	3.11	21.15	15.30

(Source :Bloomberg , ULJK Research)

### Deposit and Advances growth of Scheduled Commercial Banks in India



(Source: RBI)

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### Disclaimer Appendix

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