

**SELL**

TP: Rs 90 | ▼ 9%

**YES BANK**

Banking

17 July 2019

## Yet another miss on asset quality

**Yes Bank's (YES) Q1FY20 PAT at Rs 1.1bn beat our/consensus estimates on higher non-interest income and below-expected provisions. But Q1 was marred by key negatives: (a) a rise in the 'BB & below' rated pool to 9.4% of exposure post rating downgrades; (b) a spike in slippages to Rs 62bn with only 40% coming from the watchlist, raising concerns over the list's authenticity; and (c) a ~50bps QoQ drop in CET-1 to 8%, increasing the risk of high dilution. We slash FY20/FY21 EPS by 70%/40%, leading to a revised Mar'20 TP of Rs 90 (vs. Rs 210).**

Vikesh Mehta

research@bobcaps.in

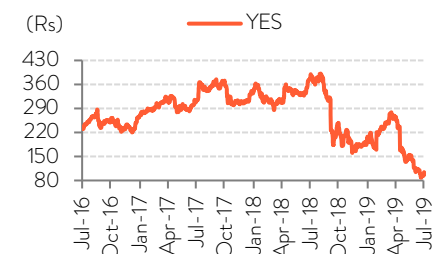
**Exposure to 'BB & below' pool rises to 9.4%:** YES's Q1 GNPA ratio rose to 5% due to a spike in slippages to Rs 62bn (Rs 35bn in Q4). Management stated that ~40% of slippages were from its Rs 100bn watchlist, while the rest were from the 'BB & below' book. The share of this book increased to 9.4% vs. 7.1% in Q4 driven by ratings downgrades for investments in two financial services groups. YES made Rs 11.1bn MTM provision (20-30% of exposure) on these investments. Real estate exposure is at Rs 240bn, 25% being sub-investment grade/NPA with the rest at minimal risk of slippage. Corporate SMA-2 exposure is at ~Rs 4bn.

Ticker/Price	YES IN/Rs 98
Market cap	US\$ 3.3bn
Shares o/s	2,309mn
3M ADV	US\$ 172.0mn
52wk high/low	Rs 404/Rs 86
Promoter/FPI/DII	20%/40%/41%

Source: NSE

**Capital raising in Q2:** The bank's CET-1 ratio dropped ~50bps QoQ to 8% due to revised RBI regulations, investment rating downgrades and a change in operational risks. However, management highlighted that it may raise capital in Q2 and sees scope for diluting >10% equity.

## STOCK PERFORMANCE



Source: NSE

**Maintain SELL:** We scale back our FY20/FY21 earnings estimates by 70%/40% to factor in slower loan growth, higher slippages and a rise in credit costs, while cutting our target P/ABV multiple to 1.2x FY21E (from 1.7x earlier). Despite the stock trading at low valuations of 0.9x FY21E P/BV, we remain sellers as we await clarity on stabilisation of the 'BB & below' rated pool, adherence to credit cost guidance, and capital raising.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	42,245	17,203	10,117	28,573	42,520
EPS (Rs)	18.4	7.5	3.9	9.6	13.0
P/E (x)	5.3	13.2	24.9	10.2	7.6
P/BV (x)	0.9	0.8	0.8	0.9	0.9
ROA (%)	1.6	0.5	0.2	0.6	0.8
ROE (%)	17.7	6.5	3.4	8.4	11.4

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q1FY20	Q4FY19	Q1FY19	YoY (%)	QoQ (%)
<b>Net interest income</b>	<b>22,809</b>	<b>25,059</b>	<b>22,191</b>	<b>2.8</b>	<b>(9.0)</b>
Non-interest income	12,727	5,317	16,941	(24.9)	139.4
-Corporate trade & cash management	1,995	2,098	2,162	(7.7)	(4.9)
-Forex, debt capital markets & securities	6,561	110	4,603	42.5	5,864.5
-Corporate banking fees	610	(1,117)	6,827	(91.1)	(154.6)
-Retail banking fees	3,474	4,061	3,329	4.4	(14.5)
<b>Net total income</b>	<b>35,535</b>	<b>30,376</b>	<b>39,133</b>	<b>(9.2)</b>	<b>17.0</b>
Total operating expenses	15,944	17,142	14,586	9.3	(7.0)
<b>Pre-provisioning profit</b>	<b>19,591</b>	<b>13,234</b>	<b>24,547</b>	<b>(20.2)</b>	<b>48.0</b>
Provisions	17,841	36,617	6,257	185.2	(51.3)
Profit before tax	1,750	(23,383)	18,291	(90.4)	(107.5)
Tax	612	(8,317)	5,687	(89.2)	(107.4)
<b>Profit after tax</b>	<b>1,138</b>	<b>(15,066)</b>	<b>12,604</b>	<b>(91.0)</b>	<b>(107.6)</b>
<b>Key balance sheet items</b>					
Loans	2,363,002	2,414,996	2,147,201	10.1	(2.2)
Deposits	2,259,015	2,276,102	2,133,945	5.9	(0.8)
CASA ratio (%)	30.2	33.1	35.1	(495bps)	(290bps)
<b>Margin components (%)</b>					
Yield on advances	10.0	10.2	10.0	0bps	(20bps)
Cost of funds	6.8	6.7	6.3	50bps	10bps
Net interest margin	2.8	3.1	3.3	(50bps)	(30bps)
<b>Key ratios (%)</b>					
Cost/Income	44.9	56.4	37.3	760bps	(1,156bps)
Non-int. income/Net-total income	35.8	17.5	43.3	(748bps)	1,831bps
LDR	104.6	106.1	100.6	398bps	(150bps)
<b>Capital adequacy ratios (%)</b>					
Tier-I ratio	10.7	11.3	12.8	(210bps)	(60bps)
Tier-II ratio	5.0	5.2	4.1	90bps	(20bps)
Total CAR ratio	15.7	16.5	16.9	(120bps)	(80bps)
<b>Asset quality</b>					
Gross NPA	120,921	78,826	28,245	328.1	53.4
Net NPA	68,833	44,849	12,626	445.2	53.5
Gross NPA ratio (%)	5.01	3.2	1.3	370bps	179bps
Net NPA ratio (%)	2.91	1.9	0.6	232bps	105bps
Coverage ratio (%)	43.1	43.1	55.3	(1,222bps)	(3bps)

Source: Company, BOBCAPS Research

## Valuation methodology

We introduce FY22 estimates while paring our FY20/FY21 earnings estimates by 70%/40% to factor in slower loan growth, higher slippages and a subsequent rise in credit costs. Despite the stock trading at low valuations of 0.9x FY21E P/BV, we remain sellers as we await clarity on stabilisation of the 'BB & below' rated pool, adherence to credit cost guidance, and capital raising.

Our Mar'20 target price for YES stands revised to Rs 90 from Rs 210 earlier, set at a target multiple of 1.2x FY21E P/ABV (revised from 1.7x earlier). While structural changes by the new leadership are geared toward building a solid franchise in the long run and are essential to restore investor confidence, any rerating of the stock will hinge on effective execution of the new strategy. Maintain SELL.

**FIG 2 – REVISED ESTIMATES**

Particulars	Old		New		Change (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net interest income (Rs mn)	112,583	133,363	97,867	103,467	(13.1)	(22.4)
Pre-provisioning profit (Rs mn)	85,822	96,967	70,410	74,752	(18.0)	(22.9)
Profit after tax (Rs mn)	31,788	40,431	10,117	28,573	(68.2)	(29.3)
EPS (Rs)	13	16	4	10	(70.3)	(40.8)

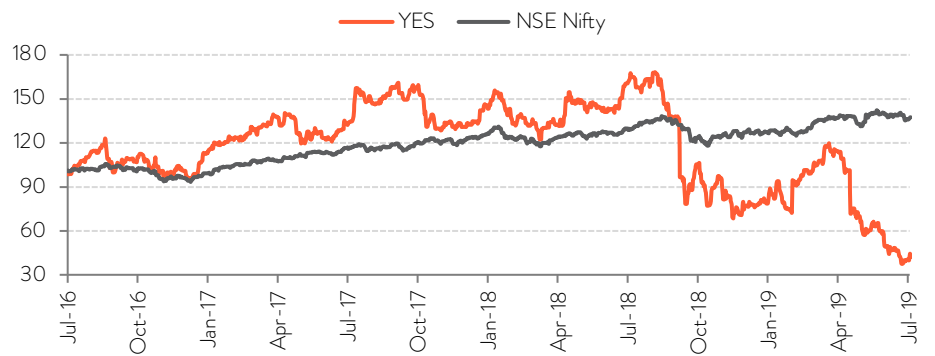
Source: BOBCAPS Research

**FIG 3 – VALUATION SNAPSHOT**

Gordon growth model	Assumptions
Risk-free rate (%)	7.0
Equity risk premium (%)	5.0
Beta	1.4
Cost of equity (%)	14.2
Blended ROE (%)	15.3
Initial high growth period (yrs)	10.0
Payout ratio of high-growth phase (%)	20.0
Long-term growth (%)	3.1
Long-term dividend payout ratio (%)	80.0
Justified P/BV multiple (x)	1.2
Adj. BVPS (Rs)	73
<b>Value per share (Rs)</b>	<b>90</b>

Source: Company, BOBCAPS Research

**FIG 4 – RELATIVE STOCK PERFORMANCE**



Source: NSE

### Key risks

- If YES manages to raise enough capital at regular intervals to deliver strong growth, our estimates could be at risk.
- If economic conditions turn conducive, the bank may not see material asset quality risks.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Net interest income</b>	<b>77,370</b>	<b>98,090</b>	<b>97,867</b>	<b>103,467</b>	<b>115,905</b>
NII growth (%)	33.5	26.8	(0.2)	5.7	12.0
Non-interest income	52,238	45,902	43,380	45,420	48,701
Total income	129,608	143,992	141,246	148,886	164,605
Operating expenses	(52,128)	(62,643)	(70,837)	(74,134)	(80,485)
Operating profit	77,480	81,349	70,410	74,752	84,121
Operating profit growth (%)	32.7	5.0	(13.4)	6.2	12.5
Provisions	(15,538)	(57,776)	(55,309)	(32,106)	(20,658)
PBT	61,942	23,573	15,101	42,647	63,463
Tax	(19,697)	(6,371)	(4,983)	(14,073)	(20,943)
<b>Reported net profit</b>	<b>42,245</b>	<b>17,203</b>	<b>10,117</b>	<b>28,573</b>	<b>42,520</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>42,245</b>	<b>17,203</b>	<b>10,117</b>	<b>28,573</b>	<b>42,520</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Equity capital	4,606	4,630	5,630	6,230	6,830
Reserves & surplus	252,977	264,412	323,526	348,754	386,296
Net worth	257,583	269,042	329,156	354,984	393,126
Deposits	2,007,381	2,276,102	2,503,712	2,854,232	3,367,993
Borrowings	748,936	1,084,241	1,324,479	1,618,612	1,978,881
Other liabilities & provisions	110,556	178,877	214,652	257,583	309,099
<b>Total liabilities and equities</b>	<b>3,124,456</b>	<b>3,808,262</b>	<b>4,372,000</b>	<b>5,085,410</b>	<b>6,049,099</b>
Cash & bank balance	247,344	268,895	298,694	333,940	375,704
Investments	683,989	895,220	1,055,283	1,263,596	1,515,251
Advances	2,035,339	2,414,996	2,584,046	2,894,131	3,328,251
Fixed & Other assets	157,784	229,150	433,977	593,742	829,893
<b>Total assets</b>	<b>3,124,456</b>	<b>3,808,262</b>	<b>4,372,000</b>	<b>5,085,410</b>	<b>6,049,099</b>
Deposit growth (%)	40.5	13.4	10.0	14.0	18.0
Advances growth (%)	53.9	18.7	7.0	12.0	15.0

### Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
EPS	18.4	7.5	3.9	9.6	13.0
Dividend per share	2.4	2.7	0.0	0.9	1.2
Book value per share	111.8	116.2	116.9	114.0	115.1

Source: Company, BOBCAPS Research

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
P/E	5.3	13.2	24.9	10.2	7.6
P/BV	0.9	0.8	0.8	0.9	0.9
Dividend yield (%)	2.4	2.7	0.0	0.9	1.3

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Net interest income	2.9	2.8	2.4	2.2	2.1
Non-interest income	2.0	1.3	1.1	1.0	0.9
Operating expenses	2.0	1.8	1.7	1.6	1.4
Pre-provisioning profit	2.9	2.3	1.7	1.6	1.5
Provisions	0.6	1.7	1.4	0.7	0.4
PBT	2.3	0.7	0.4	0.9	1.1
Tax	0.7	0.2	0.1	0.3	0.4
ROA	1.6	0.5	0.2	0.6	0.8
Leverage (x)	11.0	13.2	13.7	13.8	14.9
ROE	17.7	6.5	3.4	8.4	11.4

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Net interest income	33.5	26.8	(0.2)	5.7	12.0
Pre-provisioning profit	32.7	5.0	(13.4)	6.2	12.5
EPS	21.3	(59.6)	(47.1)	144.3	35.1
<b>Profitability &amp; Return ratios (%)</b>					
Net interest margin	3.1	3.0	2.6	2.5	2.4
Fees / Avg. assets	1.6	1.0	0.8	0.7	0.7
Cost-Income	40.2	43.5	50.2	49.8	48.9
ROE	17.7	6.5	3.4	8.4	11.4
ROA	1.6	0.5	0.2	0.6	0.8
<b>Asset quality (%)</b>					
GNPA	1.3	3.2	7.5	6.8	6.0
NNPA	0.6	1.9	4.7	4.0	3.2
Provision coverage	50.0	43.1	39.1	43.1	48.0
<b>Ratios (%)</b>					
Credit-Deposit	101.4	106.1	103.2	101.4	98.8
Investment-Deposit	34.1	39.3	42.1	44.3	45.0
CAR	18.4	16.5	14.8	13.7	13.3
Tier-1	13.2	11.3	10.0	9.3	9.2

Source: Company, BOBCAPS Research

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### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: YES BANK (YES IN)



B – Buy, A – Add, R – Reduce, S – Sell

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