

Yes Bank | BUY

Q&A with the management

We recently met the senior management of Yes Bank to get a qualitative understanding of the impact of recent RBI guidelines on stressed assets, recent growth trends as well as medium-term outlook. We present our key takeaways below in a Q&A format.

- **Q: What is the impact the recent RBI guidelines on stressed assets impacting Yes Bank and the credit costs outlook thereof?**

For Yes Bank, the impact of the recent RBI guidelines on our Restructured Book as well as on exposures to entities with systemic exposures above INR1Bn is minimal and it doesn't alter the Bank's outlook on its credit / asset quality parameters. The Bank has been proactively de-risking its portfolio in the above categories pursuant to the issuance of the IBC-List 1 in June 2017.

JMFL View: Such exposures (i.e. above INR20bn in size) will primarily be accounts that are under "watchlists" declared by some of the larger corporate banks (e.g. ICICIB, SBIN and AXSB) and we estimate the size of this pool to be INR700-800bn for the industry. While lenders will need to accelerate implementation of resolution plans over the next 6-9months for these assets, we believe a significant proportion of these assets will be referred to IBC.

- **Q: The revised framework calls for uniform recognition of an asset across all lenders. In that case, can NPL recognition for Yes Bank increase even though LGDs remain in-line with past trends?**

The circular doesn't specifically mandate a uniform recognition of an asset across all lenders. The recognition is still governed by the extant IRAC norms. So if a borrower is servicing dues of Bank A, Bank A can continue to classify the account as 'Standard'. However this circular specifically calls for activating a 'Resolution Plan' at the first instance of default which could potentially mean that companies / borrowers > INR 20bn could end up into NCLT incase Resolution Plans aren't implemented within 180 days. As mentioned earlier, there is minimal impact for the Bank on this.

JMFL view: Yes Bank's exposures to some of the stressed groups were a) Predominantly towards entities that were "non-stressed" within the group / i.e. bankruptcy remote structures; b) were collateralized by assets that were of significantly higher realizable value or backed by imminent cashflows.

Given the bankruptcy remote nature of structures, we believe Yes Bank's GNPLs should not see any material increase under the revised stressed asset framework in our view.

- **Q: How do you view these structured corporate lending opportunities over the medium-term. While these are lucrative fee/yield opportunities for the bank, it also adds a degree of risk/opaqueity for outsiders?**

The period 2014-16 presented the Bank with some opportunities in the last-mile



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Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	450
Upside/(Downside)	45.8%
Previous Price Target	450
Change	0.0%

Key Data – YES IN

Current Market Price	INR309
Market cap (bn)	INR710.3/US\$11.0
Free Float	71%
Shares in issue (mn)	2,282.4
Diluted share (mn)	
3-mon avg daily val (mn)	INR3,545.9/US\$54.7
52-week range	383/275
Sensex/Nifty	33,704/10,360
INR/US\$	64.8

Price Performance

%	1M	6M	12M
Absolute	-11.6	-10.3	8.0
Relative*	-6.9	-16.1	-8.2

* To the BSE Sensex

Financial Summary

	(INR mn)				
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Profit	25,394	33,301	41,656	53,862	72,171
Net Profit (YoY) (%)	26.6%	31.1%	25.1%	29.3%	34.0%
Assets (YoY) (%)	21.4%	30.1%	31.0%	23.4%	24.0%
ROA (%)	1.7%	1.8%	1.7%	1.7%	1.9%
ROE (%)	19.9%	18.6%	17.5%	19.2%	21.3%
EPS	12.1	14.6	18.3	23.6	31.6
EPS (YoY) (%)	25.8%	20.8%	25.1%	29.3%	34.0%
PE (x)	25.6	21.2	16.9	13.1	9.8
BV	66	97	112	134	163
BV (YoY) (%)	17.3%	47.4%	16.4%	18.8%	21.9%
P/BV (x)	4.71	3.20	2.75	2.31	1.90

Source: Company data, JM Financial. Note: Valuations as of 8/Mar/2018

JM Financial Research is also available on:
Bloomberg - JMFR <GO>,
Thomson Publisher & Reuters
S&P Capital IQ and FactSet

Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

financing. However, today the stressed assets are going through resolutions and changing hands from stressed balance sheets to stronger balance sheets and a result of which last mile financing opportunities are getting replaced with opportunities to finance the buyer of these assets. Also, Yes Bank is incrementally able to grab a higher market share in the highly rated corporate names. Growth opportunities are therefore available with a much lower risk profile. We also believe that the competitive landscape is benign which is allowing reasonable spreads on such incremental growth opportunities. Importantly on an overall profitability basis, we expect meaningful cross-sell opportunities in these bigger groups resulting into higher share of fee / float income.

Lastly the new RBI circular will also provide refinancing opportunities for Banks like ours subject to risk objectives being fully met.

JMFL view: The structured finance book for Yes Bank stands at ~5-6% of overall funded exposure of the bank and we do not expect it to expand significantly in terms of contribution to overall exposure pie given that the bank is incrementally gaining presence across better rated corporate as well as rapidly expanding its SME & Retail franchise.

- **Q: How does one view the exposure to the real estate sector esp. developer financing? It stands at 9.2% of total exposure of the bank (incl. exposure to Social and Commercial Infrastructure) as of Dec-17.**

Historically, loss rates for Yes Bank towards real estate sector have been lower than all other corporate loans. In addition, bank has been one of the earlier lenders to the real estate sector and has ensured strong focus on “liquidity of collateral” and early warning signals to drive its strong asset quality performance in this segment. The collateral cover in real estate exposures is richly valued and as such we don’t expect credit loss events on these exposures.

JMFL view: Given market concerns with respect to real estate exposures being rated BBB or below, we believe since exposures are at individual project (SPV) level, these won’t attract high ratings.

- **Q: How do you see the retail opportunity given intense competition? Is Yes Bank a late entrant to the party?**

YES Bank is approaching retail from a franchise perspective rather than viewing it as a tactical opportunity. What this means is that we have been penetrating the ecosystems of the retail segments over last 2-3 years. With all products in place we now have the ability to provide comprehensive solutions to our customers. Current focus however is to build quality and in the process test our processes, risk filters. We also don’t find all retail products to be favorable from a risk return perspective and are therefore consciously avoiding those segments. However if at all risks were to precipitate in these segments, we will be prepared to benefit from higher acquisitions at that time as the risk-rewards ratios emerge favourably with better visibility on underlying risks.

Summary

As the stressed asset resolution framework goes through regulatory overhaul, we draw comfort on YES Bank’s asset quality based on its predominantly non-consortium exposures, proactive risk management, adequate cash-flow backed collateral cover and strong recovery capabilities. Moreover, YES is incrementally breaking into high-rated corporate accounts, which we believe will enable it to continue to deliver high risk-adjusted returns. Maintain BUY.

Valuation and 12 M TP

Our positive view on YES is based on a) its strong PPOP engine b) robust growth trajectory c) strong recovery capabilities and d) valuations which we believe adequately factor the risks. Maintain BUY with TP of INR 450 valuing Yes at 2.9x fully adjusted FY20E BVPS.

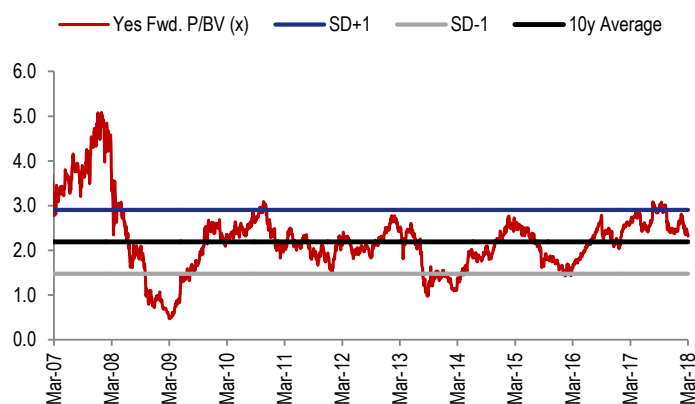
We value Yes Bank on a two-stage Gordon Growth Model. Our assumptions are as follows:

Exhibit 1. Valuation summary

Initial no. of years	10
Growth rate for the first 10 years	16.0%
Payout ratio for the first 10 years	20.0%
Perpetual growth rate	4.0%
Perpetual payout ratio	80.0%
K1	2.3
K2	12.3
Fully adjusted FY20E BVPS	154.3
Target P/BV	2.9
Fair value (rounded off) (INR)	450

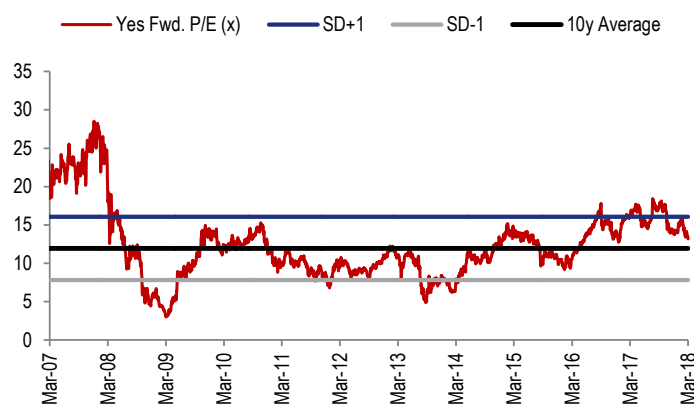
Source: Company, JM Financial

Exhibit 2. Yes Bank: One year fwd Price to Book (P/B)



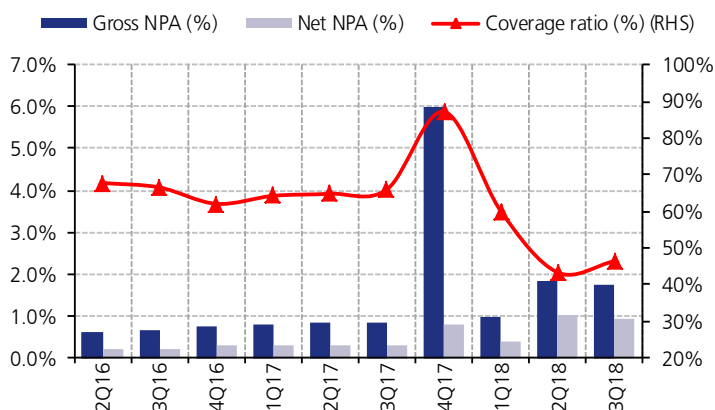
Source: Company, JM Financial

Exhibit 3. Yes Bank: One year fwd Price to earnings (P/E)



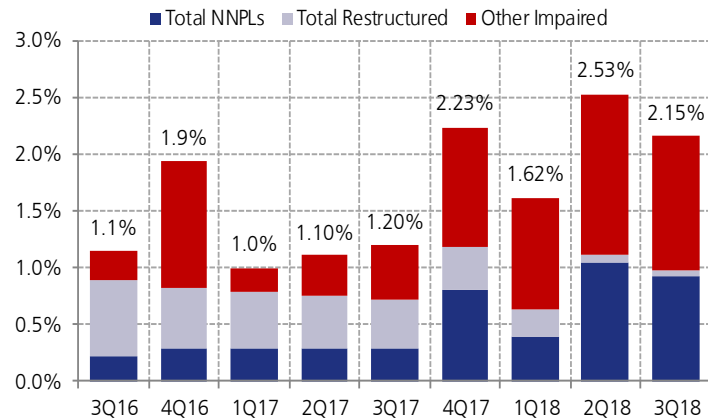
Source: Company, JM Financial

Exhibit 4. Yes Bank: Asset quality improved sequentially



Source: Company, JM Financial

Exhibit 5. Yes Bank: Net stress on loan book (%) coming off



Source: Company, JM Financial

Exhibit 6. Yes Bank : Sensitive sector exposure

Sector/ Rating - Exposure (%)	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
(A) Electricity	9.3%	9.1%	9.8%	11.3%	10.6%	9.8%	8.8%
AAA/AA rated investments	1.0%	0.7%	0.4%	0.8%	0.2%	NA	NA
T&D	1.5%	1.3%	1.3%	1.6%	1.4%	NA	NA
Renewable Exposures(Green-Financing)	2.8%	2.8%	4.3%	4.8%	4.9%	NA	NA
- of which operational	2.2%	2.5%	2.2%	2.6%	2.8%	NA	NA
Non-Renewable	4.0%	4.3%	3.9%	4.0%	4.1%	3.4%	3.4%
- of which operational	4.0%	4.3%	3.9%	4.0%	4.1%	3.4%	3.4%
Exposure to SEBs	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
(B) Iron & Steel	1.9%	1.7%	1.8%	1.8%	1.9%	2.0%	2.0%
A or above rated	1.3%	1.1%	1.3%	1.3%	1.4%	1.6%	1.6%
(C) EPC	5.6%	5.8%	6.1%	7.3%	7.3%	na	na
A or above rated	3.8%	3.8%	3.8%	4.4%	3.8%	na	na
(D) Telecom				4.9%	3.9%	3.9%	2.3%
A and above rated				4.2%	3.8%	3.7%	2.1%

Source: Company, JM Financial

Exhibit 7. Private sector banks : Contingent liabilities (INR bn)

	AXSB		ICICIB		HDFCB		IIB		YES		KMB	
(INR bn)	As a % of total		As a % of total		As a % of total		As a % of total		As a % of total		As a % of total	
1 Claims against the bank not acknowledged	5	0.1%	46	0.5%	12	0.1%	5	0.1%	0	0.0%	12	0.6%
2 Liability for partly paid investments	-	0.0%	0	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%
3 Liability on account of outstanding forward exchange and derivative contracts	5,187	77.5%	8,814	85.5%	7,422	90.8%	3,530	86.9%	3,092	81.5%	1,552	80.4%
4 Guarantees given on behalf of constituents	811	12.1%	930	9.0%	367	4.5%	390	9.6%	239	6.3%	249	12.9%
- In India	764	11.4%	727	7.0%	366	4.5%	389	9.6%	239	6.3%	-	0.0%
- Outside India	48	0.7%	203	2.0%	1	0.0%	1	0.0%		0.0%	-	0.0%
5 Acceptances, endorsements and other obligations	335	5.0%	478	4.6%	360	4.4%	127	3.1%	319	8.4%	115	6.0%
6 Other items for which the Bank is contingently liable	358	5.3%	41	0.4%	18	0.2%	11	0.3%	146	3.8%	2	0.1%
Total contingent Liabilities	6,696	100.0%	10,310	100.0%	8,179	100.0%	4,064	100.0%	3,796	100.0%	1,931	100.0%
Networth	558		999		895		206		221		276	
Total Assets	6,015		7,718		8,638		1,786		2,151		2,146	
Total contingent Liabilities as % of												
- Networth	1200.9%		1031.6%		914.2%		1969.8%		1721.1%		699.1%	
- Total Assets	111.3%		133.6%		94.7%		227.5%		176.5%		90.0%	
Guarantees as a % of												
- Networth	145.5%		93.1%		41.0%		188.9%		108.2%		90.1%	
- Total Assets	13.5%		12.0%		4.3%		21.8%		11.1%		11.6%	

Source: Company, JM Financial

Financial Tables (Standalone)

Profit & Loss					(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Interest Income	45,667	57,973	76,937	99,908	1,31,330
Profit on Investments	2,607	7,113	6,500	3,500	3,500
Exchange Income	-176	1,019	1,325	1,642	1,971
Fee & Other Income	24,690	33,436	45,647	56,669	69,487
Non-Interest Income	27,121	41,568	53,472	61,811	74,958
Total Income	72,789	99,541	1,30,409	1,61,719	2,06,288
Operating Expenses	29,764	41,165	52,055	64,926	80,569
Pre-provisioning Profits	43,025	58,375	78,353	96,793	1,25,719
Loan-Loss Provisions	5,361	7,466	15,238	14,561	15,535
Provisions on Investments	25	522	0	0	0
Others Provisions	-23	-54	0	0	0
Total Provisions	5,363	7,934	15,238	14,561	15,535
PBT	37,662	50,441	63,115	82,232	1,10,185
Tax	12,268	17,140	21,459	28,370	38,014
PAT (Pre-Extraordinaries)	25,394	33,301	41,656	53,862	72,171
Extra ordinaries (Net of Tax)	0	0	0	0	0
Reported Profits	25,394	33,301	41,656	53,862	72,171
Dividend paid	5,062	5,480	5,478	5,478	5,478
Retained Profits	20,333	27,821	36,178	48,384	66,693

Source: Company, JM Financial

Key Ratios					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Growth (YoY) (%)					
Deposits	22.5%	27.9%	30.0%	27.0%	27.0%
Advances	30.0%	34.7%	40.0%	30.0%	25.0%
Total Assets	21.4%	30.1%	31.0%	23.4%	24.0%
NII	30.9%	26.9%	32.7%	29.9%	31.5%
Non-interest Income	32.5%	53.3%	28.6%	15.6%	21.3%
Operating Expenses	30.3%	38.3%	26.5%	24.7%	24.1%
Operating Profits	32.4%	35.7%	34.2%	23.5%	29.9%
Core Operating profit	30.1%	26.8%	40.2%	29.8%	31.0%
Provisions	58.0%	47.9%	92.1%	-4.4%	6.7%
Reported PAT	26.6%	31.1%	25.1%	29.3%	34.0%
Yields / Margins (%)					
Interest Spread	2.73%	2.66%	2.62%	2.59%	2.80%
NIM	3.24%	3.25%	3.24%	3.26%	3.45%
Profitability (%)					
Non-IR to Income	37.3%	41.8%	41.0%	38.2%	36.3%
Cost to Income	40.9%	41.4%	39.9%	40.1%	39.1%
ROA	1.68%	1.75%	1.68%	1.71%	1.85%
ROE	19.9%	18.6%	17.5%	19.2%	21.3%
Assets Quality (%)					
Slippages	1.21%	2.69%	2.40%	1.65%	1.35%
Gross NPA	0.76%	1.52%	1.63%	1.31%	1.12%
Net NPAs	0.29%	0.81%	0.77%	0.56%	0.44%
Provision Coverage	62.0%	46.9%	53.0%	58.0%	61.0%
Specific LLP	0.57%	0.58%	0.87%	0.61%	0.49%
Net NPAs / Networth	2.1%	4.9%	5.6%	4.4%	3.6%
Capital Adequacy (%)					
Tier I	10.73%	13.32%	14.62%	13.33%	12.80%
CAR	16.45%	17.03%	17.85%	16.16%	15.52%

Source: Company, JM Financial

Balance Sheet						(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E	
Equity Capital	4,205	4,565	4,565	4,565	4,565	
Reserves & Surplus	1,33,661	2,15,976	2,52,154	3,00,538	3,67,232	
Deposits	11,17,195	14,28,739	18,57,360	23,58,847	29,95,736	
Borrowings	3,16,590	3,86,067	5,70,532	6,65,569	7,80,898	
Other Liabilities	80,983	1,15,253	1,32,541	1,45,795	1,60,375	
Total Liabilities	16,52,634	21,50,599	28,17,152	34,75,315	43,08,806	
Investments	4,88,385	5,00,318	6,65,144	8,28,137	10,17,392	
Net Advances	9,82,099	13,22,627	18,51,677	24,07,181	30,08,976	
Cash & Equivalents	82,184	1,95,494	2,08,311	1,63,640	1,86,453	
Fixed Assets	4,707	6,835	8,954	11,393	14,557	
Other Assets	95,259	1,25,325	83,066	64,964	81,428	
Total Assets	16,52,634	21,50,599	28,17,152	34,75,315	43,08,806	

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
NII / Assets	3.03%	3.05%	3.10%	3.18%	3.37%
Other Income / Assets	1.80%	2.19%	2.15%	1.96%	1.93%
Total Income / Assets	4.83%	5.23%	5.25%	5.14%	5.30%
Cost / Assets	1.97%	2.16%	2.10%	2.06%	2.07%
PBP / Assets	2.85%	3.07%	3.15%	3.08%	3.23%
Provisions / Assets	0.36%	0.42%	0.61%	0.46%	0.40%
PBT / Assets	2.50%	2.65%	2.54%	2.61%	2.83%
Tax rate	32.6%	34.0%	34.0%	34.5%	34.5%
ROA	1.68%	1.75%	1.68%	1.71%	1.85%
RoRWAs	2.15%	2.09%	1.87%	1.82%	1.93%
Leverage	12.0	9.8	11.0	11.4	11.6
ROE	19.9%	18.6%	17.5%	19.2%	21.3%

Source: Company, JM Financial

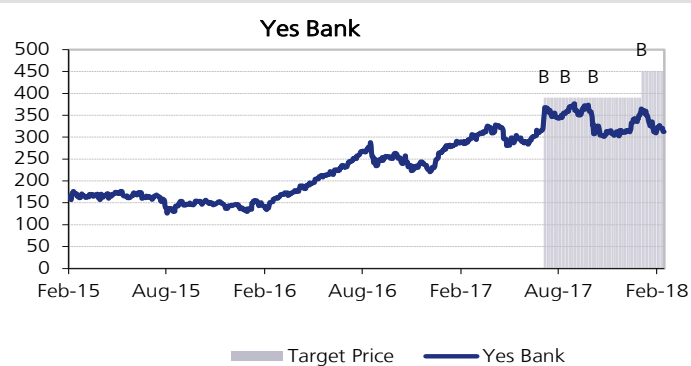
Valuations					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Shares in Issue	2,102.7	2,282.4	2,282.4	2,282.4	2,282.4
EPS (INR)	12.1	14.6	18.3	23.6	31.6
EPS (YoY) (%)	25.8%	20.8%	25.1%	29.3%	34.0%
PER (x)	25.6	21.2	16.9	13.1	9.8
BV (INR)	66	97	112	134	163
BV (YoY) (%)	17.3%	47.4%	16.4%	18.8%	21.9%
ABV (INR)	64	92	106	128	157
ABV (YoY) (%)	15.7%	43.2%	15.5%	20.4%	22.9%
P/BV (x)	4.71	3.20	2.75	2.31	1.90
P/ABV (x)	4.81	3.36	2.91	2.42	1.97
DPS (INR)	2.4	2.4	2.4	2.4	2.4
Div. yield (%)	0.8%	0.8%	0.8%	0.8%	0.8%

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	FY18E EPS (INR)	% Chg.	FY19E EPS (INR)	% Chg.	Target Price	% Chg.
26-Jul-17	18.6		23.5		390	
4-Sep-17	18.9	1.6	23.5	0.0	390	0.0
26-Oct-17	18.9	-0.1	23.5	-0.1	390	0.0
24-Jan-18	18.3	-3.2	23.6	0.4	450	15.4

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

(formerly known as JM Financial Securities Limited)

Corporate Identity Number: U67100MH2017PLC296081

Member of BSE Ltd., National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.

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Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
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Sell	Price expected to move downwards by more than 10%

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