Indian financials

Sector outlook

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India

Financial services

Management meeting notes

Banking monthly

What's inside?

Takeaways: Management meeting and interviews

In our recent meetings, banks highlighted that continuity of a tight monetary policy stance would put risks to their targets on growth and margins. Banks with higher share of wholesale funding are feeling much stronger pressure than banks with a stronger deposit franchise. Banks are looking to manage cost pressure by raising Base Rates and the spreads that they charge to borrowers. Prospect of higher agriculture GDP growth led by better monsoons, uptick in government spending near elections and political actions for infrastructure projects are the key silver-linings. Asset quality headwinds are likely to persist and hence banks have significantly increased focus on monitoring and recoveries. Private banks are also focussing on improving their operating performance to partly offset a slower growth in topline.

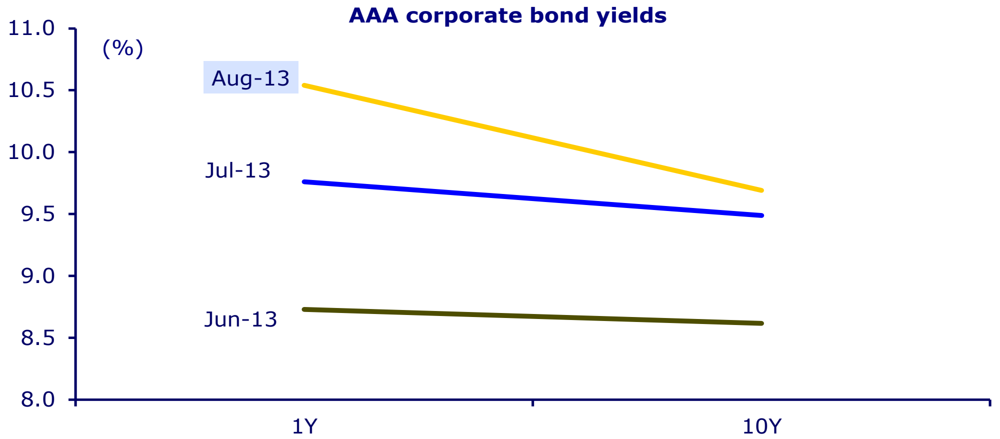
Sector round-up: RBI tweaks monetary policies; banks underperform

Over past month, Bankex (down 10%) underperformed Sensex (down 4%) largely due to investor concerns about depreciation of Rupee and continuity of high interest rates. During August, the RBI partly relaxed some measures to ease liquidity and interest rates. While the rates still remain high and yield curve is inverted, the permission to transfer G-Secs from AFS to HTM pool, based on pre-tightening values, will minimise treasury losses that could have been a big risk to earnings of PSU banks in FY14. This week, Dr. Raghuram Rajan will take charge as the new governor of RBI (central bank) for a term of 3 years upon retirement of Dr. D. Subbarao.

Update on insurance and mutual funds–June / July 2013

During June-13, annualised NBP of sector declined by 15% YoY led by a 24% YoY decline in premiums of LIC; private insurance companies reported a marginal growth of 5% YoY. Among the private players, while Max, HDFC Life and ICICI Pru gained market share, Reliance and Kotak lost share during the month. During Jul-13, assets of mutual funds grew by 4% YoY, but declined 6% MoM due to outflows from debt as well as equity funds. Since the tightening of monetary policy mutual funds have seen reasonable outflows from debt funds and in July equity funds also saw net outflows.

Chart of the month: Yield remain high and curve is inverted



Source: Bloomberg, CLSA

Banking sector update

Bankex relative performance

Figure 1

Banks' have underperformed the market this month...

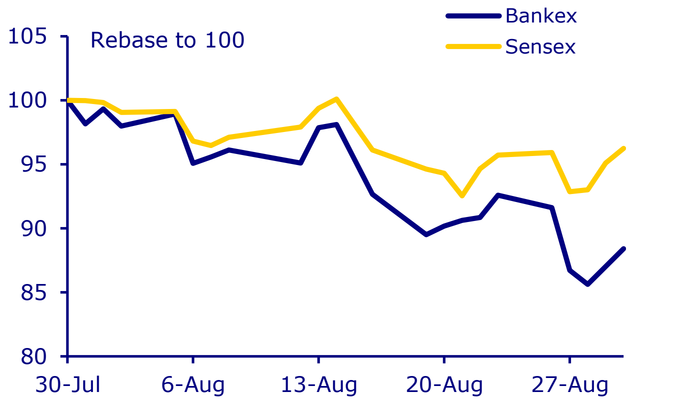
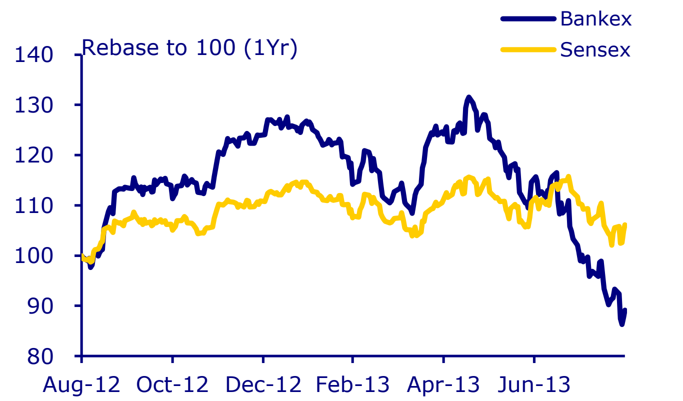


Figure 2

... and over past year



Source: Bloomberg, CLSA

Regulatory and sector newsflow

RBI plans to buy back G-Secs worth Rs80bn through OMOs

- **RBI** plans to **buy back government securities** worth **Rs80bn** through **open market operations (OMO)** on August 30 to **ease liquidity in the market**.
- **RBI** has announced a series of measures to **ease liquidity**, **support growth** and **minimize banks' MTM losses** on their G-Sec portfolio.

RBI has announced measures to ease liquidity, support growth and minimise banks' MTM losses

- As per media reports, **RBI may lower** the **group exposure norm for banks**. As per the current norms, banks' exposures to a group are capped at 40% of their capital funds for non-infrastructure sectors and 50% for infrastructure projects.
- **RBI** plans to **conduct** auctions of **cash management bills worth Rs220bn** as part of its **liquidity management strategy**.
- The **Cabinet Committee on Investment** has set a **60-day deadline** for ministries to clear **36 infrastructure projects** in power, coal and highways sectors.
- The **Finance Ministry** may **delay the capital infusion** worth **Rs140bn** for **PSU banks** intended to help them meet the Basel III norms. The Finance Ministry had earlier asked banks to either explore ways to conserve capital or revisit their credit growth targets.
- **National Housing Bank** has **lowered** the **risk weights** on **commercial real estate loans** for residential projects. The risk-weights for HFCs are now in line with those of banks.
- **IRDA** has increased the **debt investment limit** for Life Insurance Corporation of India from 15% to 20% of paid up capital. An additional 5% investment can also be made subject to approval from the board.

Company newsflows

- **ICICI Bank** has **raised interest rates** of **short term deposits** by 50-75bps.

ICICI Bank has raised its Base Rate by 25bps to 10%.

- **ICICI Bank** has raised its **Base Rate by 25bps to 10%.**
- **SBI** has indicated that they expect a **capital infusion of Rs40bn** from the **government** during FY14. As per the management, this change will make it easier for the company to comply with RBI's regulations for new bank licenses.
- **SBI** has **raised interest rates** on **deposits over Rs10m** by up to 1.5% for maturities less than one year.

Axis Bank has raised its Base Rate by 25bps to 10.25%

- **HDFC Bank** has raised its **Base Rate** by 20bps to **9.8%.**
- **Axis Bank** has raised its **Base Rate by 25bps to 10.25%.**
- **Kotak Mahindra Bank** has raised its **Base Rate by 25bps to 10%.**
- **Bank of Baroda** has **sought capital infusion of Rs18bn from the government**. The bank's Tier-I capital adequacy ratio is at 9.6% as of June 2013.
- **Canara Bank** has indicated that they **don't plan to raise lending rates** in the near term.
- **OBC** has raised **interest rates** on **term deposits** having maturity of **1-2 years** by 25bps to **9%**.

Interesting interviews

D Subbarao (Governor, RBI) (link)

It is very important for credit to continue to go to productive sectors.

We are going to put in more measures to see that NPA level is controlled across the asset quality of banks. It is very important for credit to continue to go to productive sectors. It is true that NPA in public sector banks is higher because their decision variables are different and therefore NPAs are higher than private sector banks. In the Reserve Bank, we are concerned about it. It is a growing concern. Even on last Tuesday, when we met at the bank, we spoke about this.

Pratip Chaudhuri (Chairman, SBI) (link)

The margin has committed about 3.49%

The margin has committed about 3.49% if you account for the income we have earned from the liquid mutual fund and, as I said, the June quarter was a slow quarter. In spite of that, the margin has held on and we continue to maintain our guidance for domestic net interest margin between 3.5 and 3.6% and what gives us the confidence is that we have about Rs500-700bn which has been invested in CPs and CDs and low yield government securities. So as these get re-priced and replaced with new corporate loans, we expect an increase in the realisation on our investments or the loans.

Arundhati Bhattacharya (MD, SBI) (link)

The first thing on RBI's mind is to calm the volatility in the market

If one looks at RBI, the first thing on their minds is to calm the volatility in the market and to ensure that the exchange rates go down in a measured manner. Therefore, what they had done was to make the rupee expensive and as such, the measures were aimed at the short-end of the curve. However, what has happened is that the entire curve has got afflicted and we have seen rates rising quite sharply at the longer-end as well. Now, as a result of that, RBI has brought in a few loosening measures and as a result of that again we have seen the bond yields on the 10-year has drop. We have a very big retail franchise; we are not at all dependent on wholesale funding in order to fund the assets on our balance sheet. To that extent we are much better protected.

Vikram Limaye (Executive Director, IDFC) (link)

The funding environment is quite challenging in the current time

The funding environment is quite challenging in the current time particularly because it is very difficult to raise money from bond markets. From that standpoint, the only source of funding available is the bank market. Therefore from our perspective last year and for last 24 months we have borrowed quite heavily from the bond market, which was giving us much better rates than bank market. For any incremental loans that we end up doing that are financed from the bank market, there will be a squeeze on margins. Our focus this year is going to be to try and figure out low risk growth opportunities because the core project pipeline for infrastructure is quite weak. If you are going to lend to high quality corporates then in the current environment high quality corporates are getting pretty good rates.

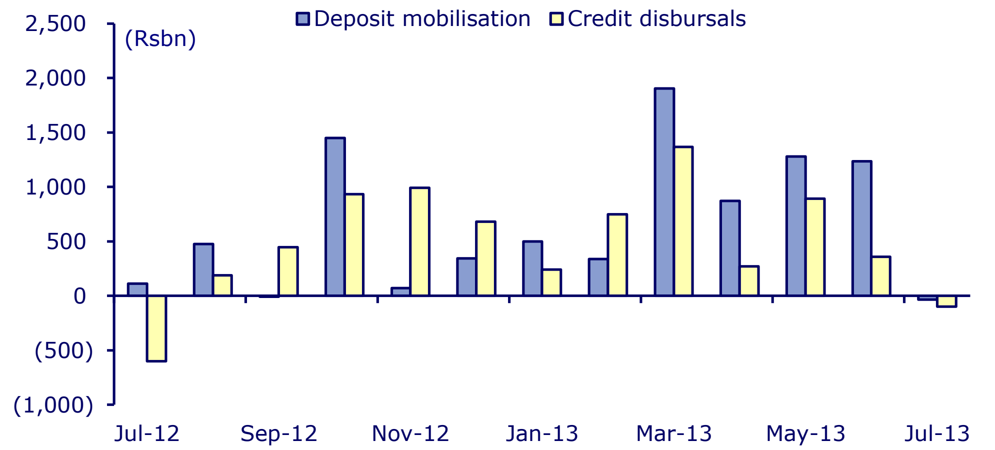
Please see other news and interviews in pages 23-29.

In July, deposit mobilisation was worse than last year

Banking trends

Figure 3

During Jul-13, decline in credit disbursals was lower as compared to Jul-12

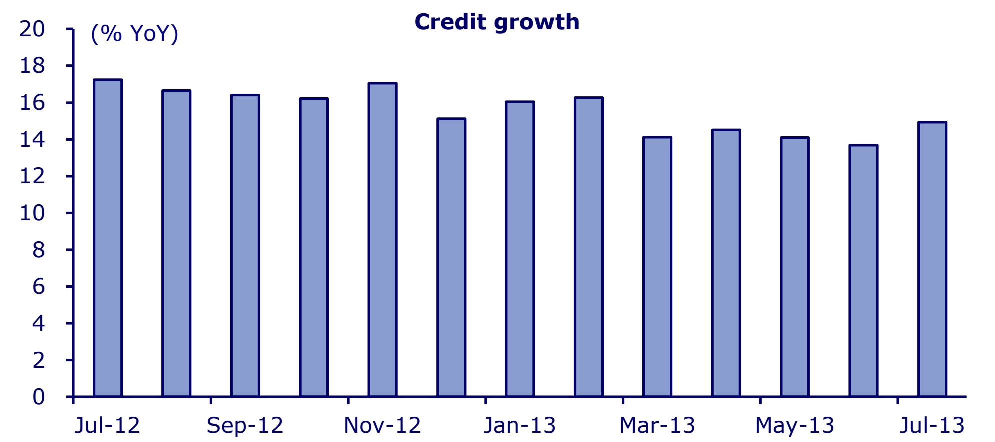


Note: As on 26th Jul-13. Source: RBI, CLSA

RBI expects credit to grow 15% YoY during FY14

Figure 4

Credit growth picked up to 15% YoY

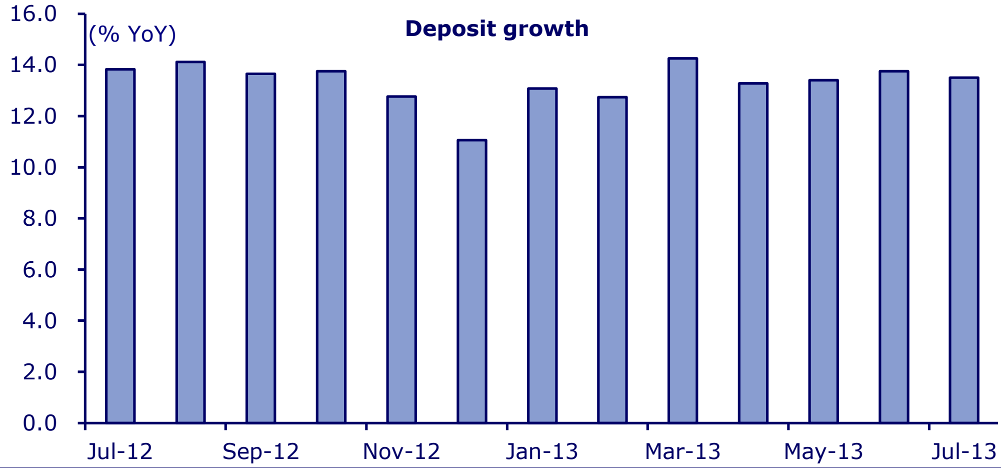


Note: As on 26th Jul-13. Source: RBI, CLSA

RBI expects deposits to grow 14% YoY during FY14

Figure 5

Deposits growth moderated to 13% YoY



Note: As on 26th Jul-13. Source: RBI, CLSA

Loans growth to agriculture improved by 100bps to 11%

Credit to Small & large industries saw faster growth

Healthy growth in infra, textile, chemical and metal sectors

Credit to telecom sector has declined YoY

Loans to services sector grew at slower pace due to moderation in loans to NBFCs and transport operators

Housing loans growth saw an uptick in July

Credit growth improved across segments in July

Figure6

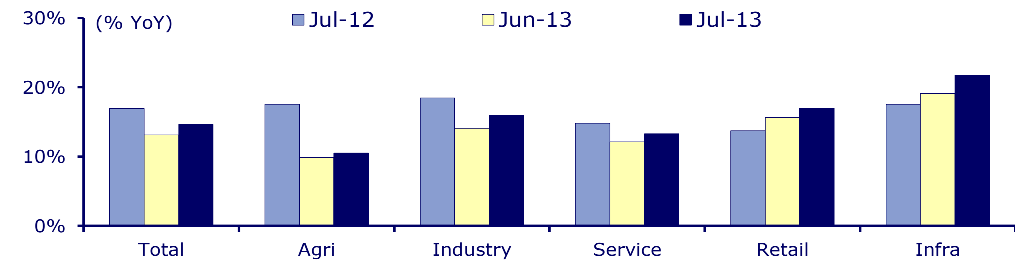
Key trends in Sector credit - Growth and share: Jul-13

	Amount	Share	Growth
	Rsbn	% of loans	% YoY
Gross Bank Credit	**50,883**	**100%**	**15%**
Food Credit	988	2%	6%
Non-food Credit	**49,894**	**98%**	**15%**
Agriculture & Allied Activities	**6,027**	**12%**	**11%**
Industry	**22,774**	**45%**	**16%**
By size			
Micro & Small	2,910	6%	20%
Medium	1,318	3%	-1%
Large	18,546	36%	17%
By key sectors			
Textiles	1,834	4%	15%
Petroleum etc	535	1%	3%
Chemicals	1,445	3%	21%
Basic Metal & Metal Product	3,191	6%	20%
Infrastructure	7,840	15%	22%
Power	4,552	9%	31%
Telecommunications	897	2%	-4%
Roads	1,445	3%	23%
Other Infrastructure	945	2%	10%
Services	**11,671**	**23%**	**13%**
Transport Operators	816	2%	3%
Trade	2,803	6%	21%
Commercial Real Estate	1,338	3%	16%
NBFCs	2,565	5%	5%
Other Services	2,906	6%	14%
Personal Loans	**9,423**	**19%**	**17%**
Housing	4,910	10%	18%
Loans on deposits	581	1%	17%
Loans against shares	31	0%	13%
Credit Card	231	0%	4%
Education	566	1%	9%
Auto	1,168	2%	23%

Source: RBI, CLSA

Figure 7

Sector-wise credit growth: Jul-13

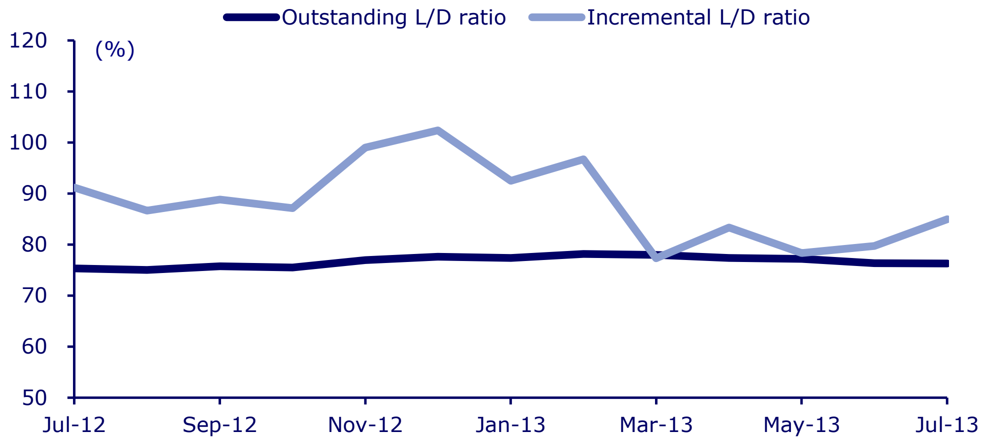


Source: RBI, CLSA

Incremental LDR increased to 85%

Figure 8

Loan deposit ratio was at 76%

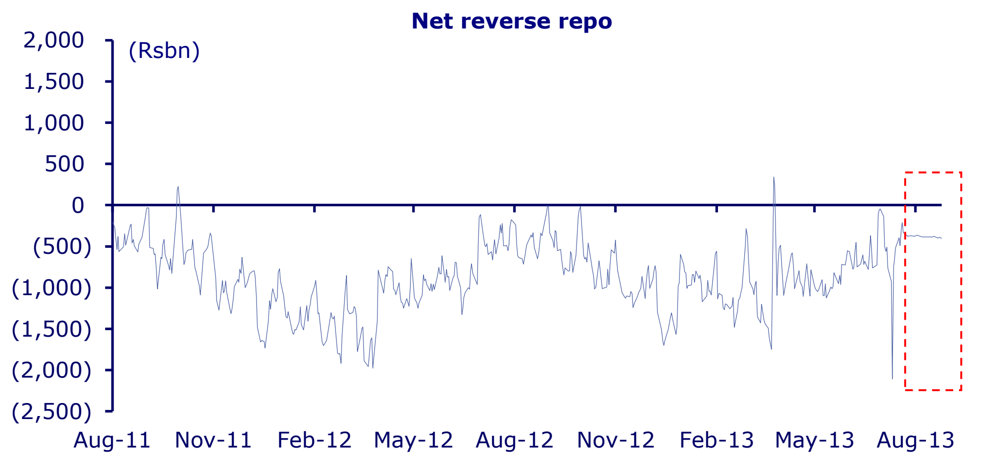


Note: As on 26th Jul-13. Source: RBI, CLSA

In July, RBI capped LAF borrowings to 0.5% of banks' liabilities

Figure 9

Borrowing through LAF window has been stable at Rs360-380bn



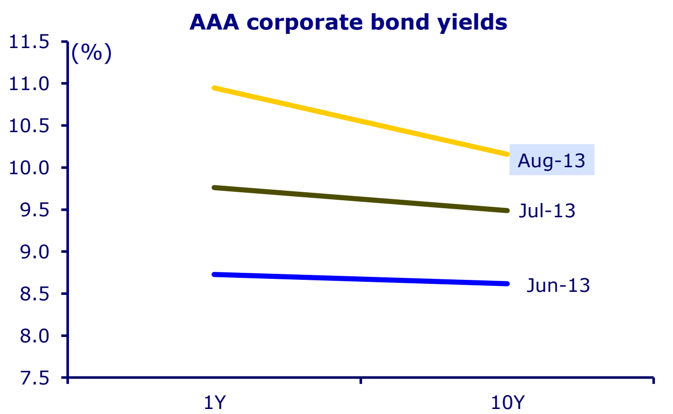
Source: Bloomberg, CLSA

Figure 10

During August, 10-year yields spiked up …

Figure 11

…and yield curve moved-up and became inverted



Source: Bloomberg, CLSA

INR has depreciated beyond Rs65/US$

HDFC has raised its lending rates by 25 bps

Figure 12

Interest rate movement

(%)	May-13	Jun-13	Jul-13	Aug-13
Mortgage Rates				
HDFC	10.15-10.9	10.15-10.9	10.15-10.9	10.40-11.15
Base Rate	9.60-10.25	9.60-10.25	9.60-10.25	9.70-10.25
1year deposit rates	6.5-8.5	6.5-8.5	6.5-8.8	6.5-8.8
10yr Bond Yield	7.2	7.5	8.2	8.6
Call money rate (low-high)	6.6-7.4	6.4-7.4	5.5-10.1	5.5-10.1
INR/US$	57.1	60.3	60.8	65.7

Source: Bloomberg, RBI, Companies, CLSA

Banks have raised their short term deposit rates

ICICI, HDFC Bank and Axis have raised their Base Rate by 20-25bps

SBI doesn't plan to raise it Base Rate in near term

Figure 13

Matrix of interest rates

	Base Rate	Retail deposit rates		
		<1Yr.	1-3Yr.	3-5Yr.
State Bank of India	9.70	6.50	8.75	8.75
ICICI Bank	10.00	7.75	9.00	8.75
Axis Bank	10.25	8.75	9.00	8.75
HDFC Bank	9.80	8.75	9.00	8.75
Bank of Baroda	10.25	7.75	8.75	8.90
Bank of India	10.00	8.00	9.00	9.00
Union Bank of India	10.00	8.15	9.00	9.00

Source: Banks, CLSA

Macro trends

While WPI inflation was higher MoM, IIP declined further during July

Figure 14

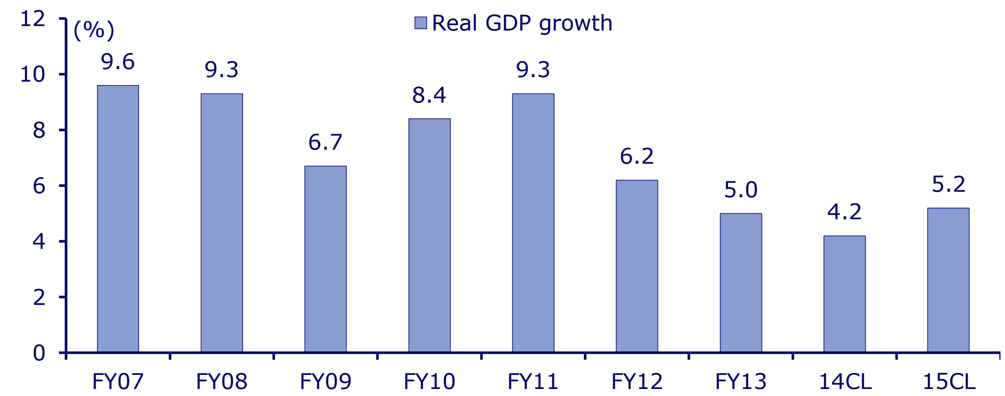
Particulars	Feb-13	Mar-13	Apr-13	May-13	Jun-13	Jul-13
WPI (%)	7.3	5.7	4.8	4.6	4.9	5.8
Forex Reserves (US$bn)	258	260	264	259	255	252
M3 growth (%)	12	14	12	12	13	13
Bank Credit (Rsbn)	51,260	52,628	53,464	53,409	53,792	54,150
Agg. Deposits (Rsbn)	65,611	67,514	69,049	68,835	69,665	70,902
IIP growth (%)	0.6	3.4	1.9	(1.6)	(2.2)	Na
- Basic (%)	(1.8)	3.0	2.0	(0.4)	(1.9)	Na
- Capital (%)	9.1	9.0	(0.1)	(2.7)	(6.6)	Na
- Intermediate (%)	(0.8)	2.4	2.6	1.5	1.1	Na
- Consumer (%)	0.8	1.8	2.1	(4.0)	(2.3)	Na
+ Consumer durables (%)	(2.6)	(4.4)	(8.9)	(10.4)	(10.5)	Na
+ Consumer non-durables (%)	3.2	6.9	11.5	1.7	5.0	Na

Source: Government of India, RBI, CLSA

Our economist has cut forecast of GDP growth during FY14 to 4.2%

Figure 15

Trends in GDP growth and estimates



Source: Government of India, CLSA

Industry interactions

IDFC (IDFC IN – 81 – BUY)

Macro environment

- Expect GDP growth to be in the range of 5% during FY14 with a weak investment cycle.

Outcome of the upcoming elections will be crucial to revive the investment cycle

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Infrastructure sector

- Very few new projects investments are coming up in infrastructure.
- While SEB reforms have been positive for the power sector, incremental investments remain weak.

Regulatory clarity on road projects and telecom auctions will be crucial

- Regulatory clarity on road projects and telecom auctions will be crucial for incremental investment in these sectors.

Growth strategy

- The sharp rise in interest rates is impacting its cost-advantage over banks and can curtail loan growth and spreads.

IDFC plans to focus on lending to corporates with higher credit ratings

- IDFC plans to focus on lending to corporates with higher credit ratings during FY14.
- Its loan approval process has become more stringent and approval rate of new projects has declined considerably.

Asset quality

Management expects stressed loans to rise

- Management expects stressed loans to rise as exposures to gas based projects (~3% of loans) may get restructured.
- Impact on earnings would be manageable as it has created significant buffer against credit risks with total provisions at 1.9% of loans.

Banking licence

Converting to a bank will help IDFC to diversify its business

- Converting to a bank will help IDFC to achieve its key long term objective of asset diversification.
- IDFC will be able to offer wider range of products to existing customers, diversify beyond infrastructure to retail segment and diversify its source of funds.
- If IDFC does manage to get a banking license, it will take 18-30 months operationalize the bank structure
- ROA will see a decline in the initial years however increase in leverage and Casa franchise will drive long term ROEs to 15-16%.

SBI (SBIN IN – 1,514 – BUY)

Loans

Well rated corporates are now finding the CP market to be too costly

- Well rated corporates, who were accessing the CP market, are now finding the CP market to be too costly and are swinging back into loans.
- Those corporates who were accessing the ECB markets are also finding that it is better to remain in INR at this point in time rather than take a risk on the foreign currency loan side.

Expect loan growth to be in the range of 19-20%

- Expect loan growth to be in the range of 18-20% during FY14.
- The bank is witnessing strong traction in mortgage segment. Nearly 20% of mortgages are takeover of loans.

Margins

Expect NIMs to be in the range of 3.5-3.6%

- Expect domestic NIMs to be in the range of 3.5-3.6% over FY14.
- Management does not intend to raise lending rates in near term.

Deposits

Bank is not dependent on wholesale funding at all

- Bank is not dependent on wholesale funding at all hence it is least impacted by the sharp rise in interest rates.
- Bank has seen a rise in deposits since the volatility in markets rose as bank deposits are considered to be a safe harbour.

Asset Quality

Rise in interest rates will add to asset quality pressures

- Slippage during 1QFY14 was mainly due to SME and agri portfolio.
- Good monsoons this year has been a positive for our agri loans and we will be able to see some pullback in NPAs.
- Rise in interest rates will add to asset quality pressures.
- SME segment however, remains an area of concern.

Pensions and employee costs

Pension liabilities increased by Rs24bn due to change in life expectancy assumptions

- Due to change in life expectancy assumptions, the bank's pension liability increased by Rs24bn.
- The bank will be providing additional provision of Rs6bn each quarter during FY14 towards this.

Capital raising

- Expect Rs40bn capital infusion from the government during FY14.

Power Finance Corporation (POWF IN – 109 – OPF)

Developments in power sector

- Banks have started lending to SEBs in some states.

PFC and REC have provided longer term support as transitional funding to SEBs

- PFC and REC have provided longer term support as transitional funding to SEBs- there is no moratorium on interest, but principal has a moratorium of up to 3 years.
- Pooling of price for imported coal has been agreed to by CCEA.
- Gas issue is also being addressed through the real impact will be assessed later.
- EGoM will consider priority of natural gas allocation among sectors
- Standard bidding documents for Case I and Case II is yet to be finalised.

Lending business

- Current loan growth of 24% is being boosted by lending to SEBs against the transitional funding and compensated for slower growth in loans to power-generation segment (78% of loans) to 15%.

Incremental sanctions are also strong

- Incremental sanctions are also strong, up 38% YoY, led by sanctions to government's power projects.

Asset quality

- The NPL levels are stable with gross NPL ratio at 0.7% of loans and net NPL ratio of 0.6%.
- However, there was an uptick in the restructured loans to 6% of loans; >85% of restructured loans faced delay in commissioning of the project whereas rest face some pressure on profitability.

A larger proportion of projects are getting commissioned in FY14

- A larger proportion of projects are getting commissioned in FY14 and hence if they don't get adequate fuel linkage or aren't able to generate adequate revenues, they may need restructuring.

Interest rates and spreads

- Compared to loan growth, NII growth is much stronger at +35% as spreads have expanded.
- However, the recent rise in interest rates may put pressure on spreads.

Forex borrowings form 6% of loans of which about 15% is hedged

- Forex borrowings form 6% of loans of which about 15% is hedged, but with the volatility in Rupee PFC is looking to manage forex risks.

Cholamandalam Finance (CIFC – 213– No Rec)

Businesses

Vehicle finance business forms +70% of total assets

- The vehicle finance business forms +70% of total assets where the company focuses on commercial vehicles, tractors and cars.
- Loans against properties form +25% of total assets and company focusses on loans to self-employed people.
- While competition in CV business remains stable, slowdown in the new CV market has increased the focus on used CV market opportunity

Focus on efficiencies

Improvement in operating efficiencies is driving expansion in ROA

- Cholamandalam Finance has improved efficiencies through process improvement and management of customer relationships
- The company has been able to improve retention ratio of customers to +25% and this can be improved further as best in class NBFCs have retention ratio of 60-70%.
- Operating expenses to assets ratio dropped by ~30bps to 3.7% and this has been the key driver of ROA.
- The company is expecting further improvement in ROA – from ~2% now to ~3% over the coming 3 years.
- The company is mostly focused on non-urban areas that form 70% of business; its share remains high even in new expansion.

Long-term plan

Targeting to grow at a healthy pace of 25-30%

- Targeting to grow profits at a healthy pace of 25-30% driven by growth in assets and improvement in productivity.
- Chola is also testing some new business models like rural financing, housing loans for self-employed and SME to drive long term growth.
- In the coming years, exposure to these segments will remain small at ~3% of assets and these should not drag earnings by >3%.
- Chola has not applied for a banking license due to onerous conditions for compliance – reserve requirements and priority sector loans.

Interest rates and ALM

Rse in wholesale funding costs will push-up funding costs

- The sharp rise in wholesale funding costs will push-up funding costs.
- Interest rates on bank loans have increased with hike in (1) Base Rates and (2) spreads over Base Rates.
- However, liquidity conditions should be stable as the ALM is balanced.

Capital adequacy

Tier I CAR is at 11%

- Total capital adequacy ratio is at 19%, of which Tier I CAR is at 11%.
- Currently promoters own ~58% of the company and would be willing to dilute to raise capital for growth.

Vakrangee Softwares Limited (VKI IN – 75– No Rec)

Current businesses

India's largest E-Governance company

- Vakrangee Softwares Limited (VSL) is India's largest E-Governance company with 20 years of e-governance focus.
- It has handled various e-governance projects including election automation, public distribution system, UIDAI (Aadhaar), financial inclusion etc.
- VSL has coordinated enrolment of 30m Aadhaar cards till date.

Future businesses

To set-up & manage 50,000 rural bank branches

- VSL has exclusive mandate to set-up & manage 50,000 rural bank branches in the states of Maharashtra, Rajasthan, and Delhi by FY15.
- It is also allowed to provide business-to-consumer and government-to-consumer services from these outlets.

Rural branch business

The company is empanelled with 31 banks

- The company is empanelled with 31 banks (mostly PSU banks) to set-up rural bank branches.
- VSL has the exclusive mandate to set-up & manage 50,000 bank branches in the states of Maharashtra, Rajasthan, and Delhi by FY15; the current network is near 3,200.
- It will offer more than 30 banking services from these branches including deposit accounts, loans, remittances, insurance and recoveries.
- VSL has also tied-up with LIC, GIC, Vodafone, Airtel, Tata Motors, Mahindra & Mahindra to offer non-banking services.
- VSL will operating to village level entrepreneurs (VLE) and will work as an agent for the bank.

Business will be operated in an asset-light format

- The business will be operated in an asset-light format with sharing of investments and revenues between VLS and franchisee.

Current financials, market cap and shareholding

Trades at +30x trailing PE

- Key financials for FY13: Revenues Rs15bn, Ebitda Rs4bn and Net profit Rs1.1bn.
- Over past 3 years, revenues have grown at +50% and profit has grown at +60% Cagr
- The ROCE is at 27% and company has manageable leverage of 0.8x.
- The current market cap of company is at Rs33bn (trailing PE of 33x)
- Promoters own 39% of equity and LIC is the largest institutional owner at 6.5%.

Stock performance and valuations

Figure 16

Banks have underperformed Sensex over last month…

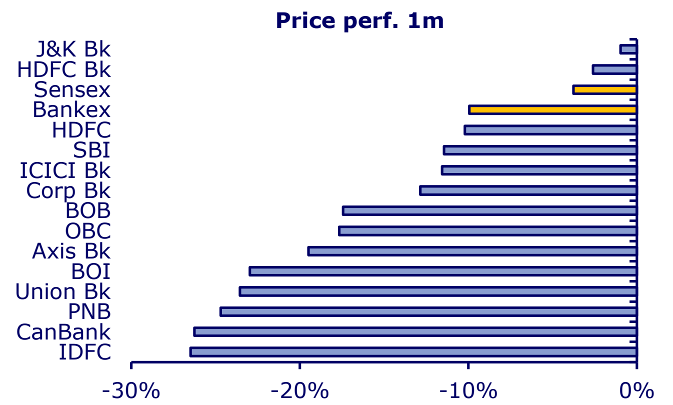
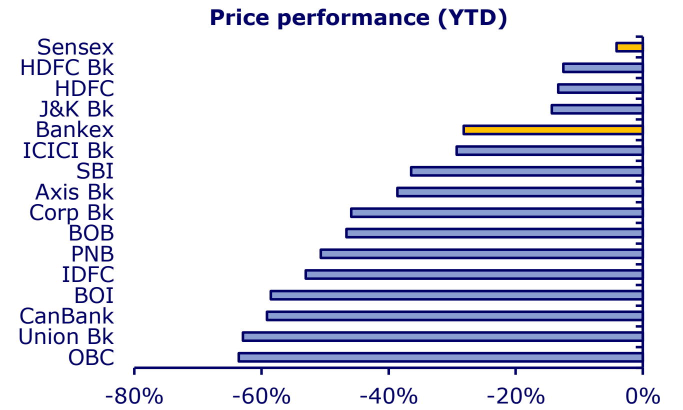


Figure 17

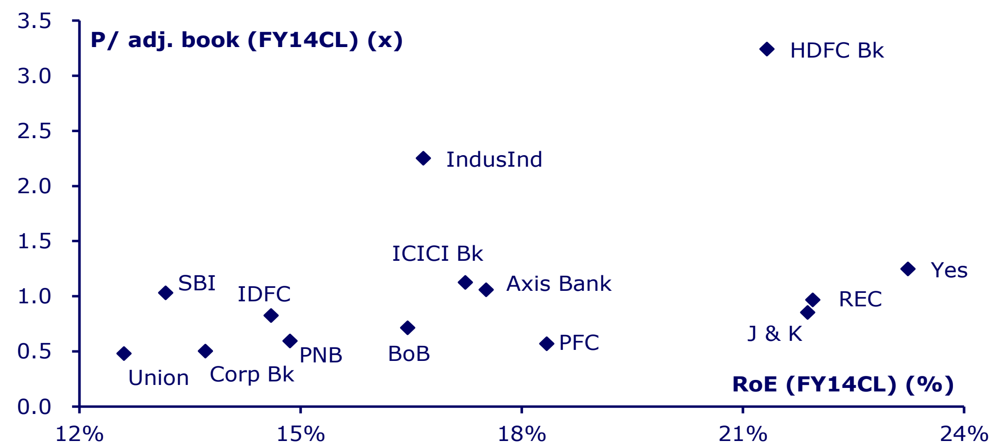
…as well as on a YTD basis



Source: CLSA , Bloomberg

Figure 18

Risk-return trade-off for financials



* Based on sustainable RoE. Source: CLSA; ICICI Bank and SBI are adjusted for investment in subs

Figure19

Recommendation summary

Name	Price (Rs)	Rec	P/ABV , FY14CL	ROAE, FY14CL
SBI	1,514	BUY	1.0	13%
ICICI Bank	804	BUY	1.1	17%
HDFC	718	BUY	3.3	24%
HDFC Bank	594	BUY	3.2	21%
Axis Bank	836	BUY	1.1	18%
Yes Bank	243	O-PF	0.8	15%
PNB	430	BUY	0.6	15%
BOB	463	O-PF	0.7	16%
BOI	142	O-PF	0.5	12%
Canara	202	U-PF	0.5	12%
Corp Bk	250	U-PF	0.5	14%
OBC	127	U-PF	0.4	11%
Union	102	O-PF	0.5	13%
J & K	1,111	BUY	1.0	22%
IDFC	81	BUY	0.8	15%
IndusInd Bank	357	BUY	2.6	17%

Source: CLSA

Figure 20

Valuation Summary

	Private banks					PSU banks									NBFCs			
	ICICI Bk	HDFC Bk	Axis Bank	IndusInd	Yes Bk	SBI Consol	PNB	BoB	BoI	Canara	Union	Corp Bk	OBC	J & K	HDFC	IDFC	PFC	REC
BBG	ICICIBC IB	HDFCB IB	AXSB IB	IIB IS	YES IB	SBIN IB	PNB IB	BOB IB	BOI IB	CBK IB	UNBK IB	CRPBK IB	OBC IB	JKBK IB	HDFC IB	IDFC IB	POWF IB	RECL IB
Mkt Price	804	594	836	357	243	1,514	430	463	142	202	102	250	127	1,111	718	81	109	169
Recommendation	BUY	BUY	BUY	BUY	O-PF	BUY	BUY	O-PF	O-PF	U-PF	O-PF	U-PF	U-PF	BUY	BUY	BUY	O-PF	O-PF
Price Target (Rs)	1,400	830	1,720	600	450	2,340	800	595	210	265	140	285	140	1,550	1,050	150	120	180
Market Cap.(US$m)	15,464	23,548	6,518	3,111	1,454	17,265	2,533	3,260	1,415	1,495	1,011	637	618	898	18,503	2,042	2,394	2,773
Avg. trading (US$m)	72	38	50	16	38	89	13	15	7	8	7	1	4	2	55	19	11	6
Valuation ratios																		
Reported PB (x)																		
FY13	1.4	3.9	1.2	2.4	1.5	0.8	0.5	0.6	0.4	0.4	0.4	0.4	0.3	1.1	4.4	0.9	0.6	1.0
FY14CL	1.3	3.3	1.0	2.1	1.2	0.7	0.4	0.5	0.3	0.3	0.3	0.4	0.3	0.9	4.0	0.8	0.5	0.8
FY15CL	1.1	2.8	0.9	1.8	1.0	0.7	0.4	0.5	0.3	0.3	0.3	0.3	0.2	0.8	3.5	0.7	0.5	0.7
Adjusted PB (x)																		
FY13	1.3	3.8	1.2	2.6	1.5	1.0	0.6	0.7	0.5	0.5	0.5	0.5	0.4	1.1	4.0	0.9	0.6	1.0
FY14CL	1.1	3.2	1.1	2.3	1.2	1.0	0.6	0.7	0.5	0.5	0.5	0.5	0.4	1.0	3.3	0.8	0.6	0.9
FY15CL	1.0	2.8	0.9	2.0	1.0	0.9	0.6	0.7	0.5	0.5	0.5	0.5	0.4	0.8	2.7	0.7	0.5	0.7
Adjusted PE (x)																		
FY13	7.9	20.9	7.1	16.7	6.7	5.4	3.1	4.0	2.8	3.1	2.6	2.6	2.4	5.1	13.2	6.0	3.8	5.1
FY14CL	6.6	16.8	6.3	13.7	5.9	5.5	3.0	3.4	2.5	3.0	2.4	2.3	2.0	4.6	11.0	5.7	3.0	4.0
FY15CL	5.2	13.7	5.3	10.8	4.8	4.3	2.6	2.9	2.4	2.6	2.3	2.5	2.2	4.1	9.0	4.9	2.6	3.5
Dividend Yield (%)																		
FY14CL	3.2%	1.2%	2.6%	1.1%	2.8%	2.6%	6.8%	4.2%	6.3%	6.7%	7.9%	7.1%	8.0%	4.9%	2.0%	3.4%	6.6%	5.0%
Subsidiary and others (Rs/ share)																		
FY13	231					104									296	8		
FY14CL	244					118									307	7		
FY15CL	268					136									322	6		
ROA (%)																		
FY13	1.6%	1.8%	1.7%	1.6%	1.5%	0.9%	1.0%	1.0%	0.7%	0.7%	0.8%	0.8%	0.7%	1.6%	2.7%	2.8%	2.5%	2.7%
FY14CL	1.7%	1.9%	1.7%	1.7%	1.3%	0.8%	1.0%	1.0%	0.6%	0.7%	0.7%	0.6%	0.7%	1.5%	2.7%	2.6%	2.6%	2.9%
FY15CL	1.8%	1.9%	1.6%	1.7%	1.3%	0.9%	1.0%	1.0%	0.6%	0.7%	0.7%	0.6%	0.7%	1.5%	2.7%	2.7%	2.6%	2.8%
Core ROE (%)																		
FY13	16%	20%	19%	17%	25%	15%	16%	16%	12%	12%	14%	16%	11%	24%	26%	15%	17%	20%
FY14CL	17%	21%	18%	17%	23%	13%	15%	16%	12%	12%	13%	14%	11%	22%	24%	15%	18%	22%
FY15CL	18%	22%	18%	18%	23%	15%	15%	17%	13%	12%	13%	14%	12%	21%	25%	15%	18%	21%

Source: CLSA

Figure 21

Valuation Summary

	Private banks					PSU banks									NBFCs			
	ICICI Bk	HDFC Bk	Axis Bank	IndusInd	Yes Bk	SBI Consol	PNB	BoB	BoI	Canara	Union	Corp Bk	OBC	J & K	HDFC	IDFC	PFC	REC
EPS (Rs)																		
FY13	72	28	118	21	37	261	137	117	52	65	39	97	54	218	32	12	29	33
FY14CL	85	35	133	26	42	255	146	134	57	68	43	109	62	239	37	13	36	42
FY15CL	103	43	159	33	50	319	167	160	59	79	44	100	59	273	44	15	41	48
Cagr FY13-15CL	**19%**	**24%**	**16%**	**24%**	**17%**	**11%**	**10%**	**17%**	**7%**	**10%**	**6%**	**1%**	**5%**	**12%**	**17%**	**12%**	**20%**	**21%**
Tier I Car (%)																		
FY13	12.8%	11.1%	12.2%	13.8%	9.1%	9.5%	9.8%	10.3%	8.2%	9.8%	8.2%	8.3%	9.2%	10.9%	13.9%	20.0%	16.8%	16.1%
FY14CL	11.6%	10.7%	11.4%	12.8%	8.6%	8.6%	8.9%	9.9%	7.8%	8.7%	7.8%	7.5%	8.4%	11.1%	13.5%	19.9%	16.4%	15.9%
FY15CL	11.3%	10.3%	10.7%	11.9%	8.3%	8.3%	8.6%	9.4%	7.3%	8.5%	7.4%	7.1%	8.1%	11.1%	12.9%	19.6%	16.1%	16.1%
NIM (%)																		
FY13	3.1%	4.4%	3.3%	3.4%	2.8%	3.3%	3.4%	2.4%	2.2%	2.2%	2.8%	2.1%	2.7%	3.6%	3.7%	3.9%	4.3%	4.6%
FY14CL	3.3%	4.5%	3.4%	3.6%	2.8%	3.4%	3.5%	2.5%	2.3%	2.2%	2.7%	2.0%	2.8%	3.6%	3.7%	3.6%	4.2%	4.5%
FY15CL	3.4%	4.5%	3.4%	3.6%	2.8%	3.3%	3.5%	2.5%	2.3%	2.2%	2.8%	2.1%	2.8%	3.6%	3.7%	3.8%	4.2%	4.3%
Casa (% of deposits)																		
FY13	42%	47%	44%	29%	19%	45%	39%	25%	26%	24%	31%	22%	25%	39%	NA	NA	NA	NA
FY14CL	42%	48%	44%	31%	22%	44%	40%	26%	25%	24%	31%	21%	24%	39%	NA	NA	NA	NA
FY15CL	42%	47%	43%	32%	26%	44%	40%	26%	25%	24%	31%	21%	24%	39%	NA	NA	NA	NA
Loan growth (%)																		
FY13	14%	23%	16%	26%	24%	21%	5%	14%	16%	4%	17%	18%	15%	19%	21%	16%	23%	26%
FY14CL	18%	23%	20%	26%	22%	17%	14%	15%	16%	12%	15%	16%	13%	17%	19%	12%	16%	19%
FY15CL	19%	23%	21%	26%	22%	17%	16%	16%	16%	14%	15%	16%	15%	17%	19%	15%	16%	16%
Fee growth (%)																		
FY13	2%	15%	13%	36%	40%	-3%	-1%	8%	2%	2%	8%	2%	-2%	8%	-10%	18%	4%	16%
FY14CL	14%	14%	15%	30%	25%	6%	10%	13%	11%	12%	10%	7%	10%	7%	15%	16%	42%	12%
FY15CL	16%	18%	18%	30%	25%	15%	12%	14%	13%	12%	11%	10%	12%	7%	15%	16%	-21%	12%
Gross NPL ratio (% of loans)																		
FY13	3.3%	1.0%	1.2%	1.0%	0.2%	4.8%	4.2%	2.4%	3.0%	2.6%	3.0%	1.7%	3.2%	1.5%	0.7%	0.1%	0.7%	0.4%
FY14CL	3.4%	1.2%	1.7%	1.4%	0.6%	5.7%	5.2%	3.5%	3.8%	3.5%	3.5%	2.7%	4.0%	1.7%	0.7%	0.7%	1.5%	1.0%
FY15CL	3.6%	1.3%	2.0%	1.8%	0.9%	5.8%	6.1%	4.6%	4.4%	4.1%	4.1%	3.6%	4.8%	2.0%	0.7%	1.2%	1.8%	1.2%
Net NPL ratio (% of loans)																		
FY13	0.8%	0.2%	0.4%	0.3%	0.0%	2.1%	2.3%	1.3%	2.1%	2.2%	1.6%	1.2%	2.3%	0.1%	0.3%	-1.2%	0.6%	0.3%
FY14CL	0.9%	0.3%	0.5%	0.4%	0.2%	2.9%	3.0%	1.9%	2.5%	3.0%	2.0%	1.8%	2.8%	0.3%	0.3%	-0.9%	1.3%	0.7%
FY15CL	1.0%	0.4%	0.6%	0.6%	0.3%	2.9%	3.7%	2.5%	2.8%	3.5%	2.3%	2.5%	3.3%	0.4%	0.3%	-0.6%	1.5%	0.8%
Restructured loans (% of loans)	2.0%	0.2%	2.1%	0.3%	0.3%	3.0%	10.5%	6.5%	5.2%	8.0%	6.5%	6.8%	8.0%	3.8%				

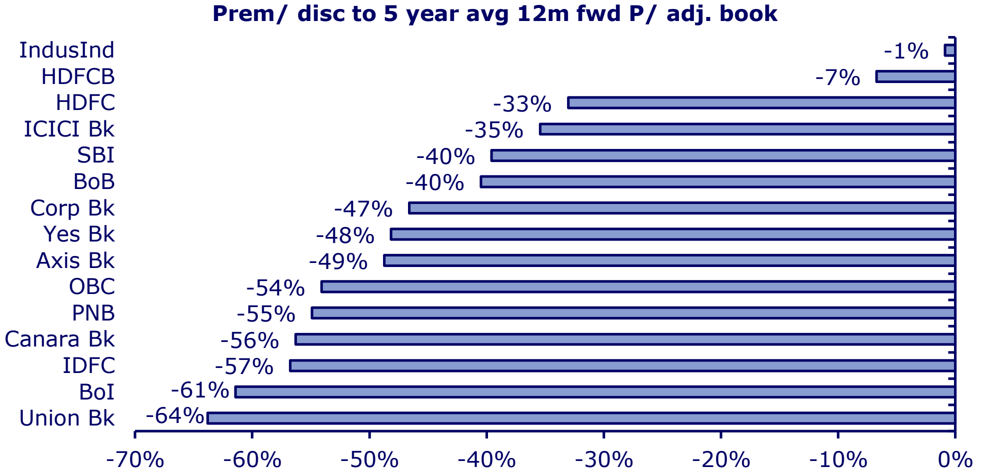
Source: CLSA

Valuations

Most banks trade near five year average

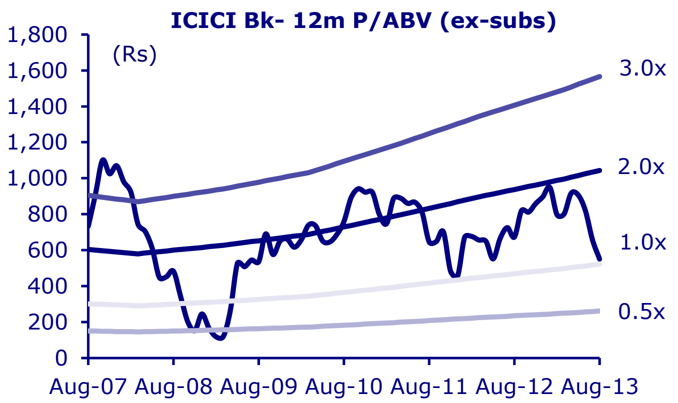
Figure 22

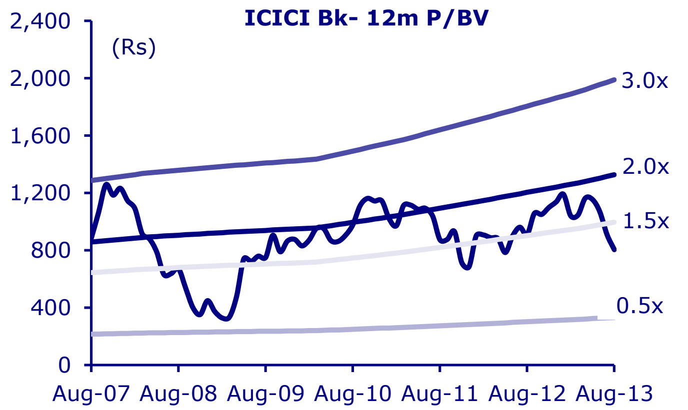
Premium/ discount to five year average

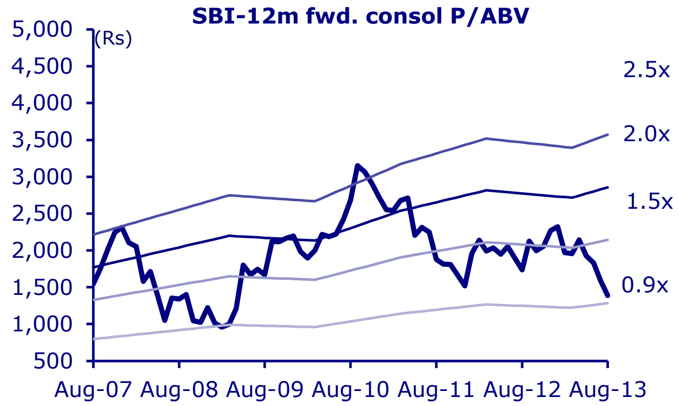


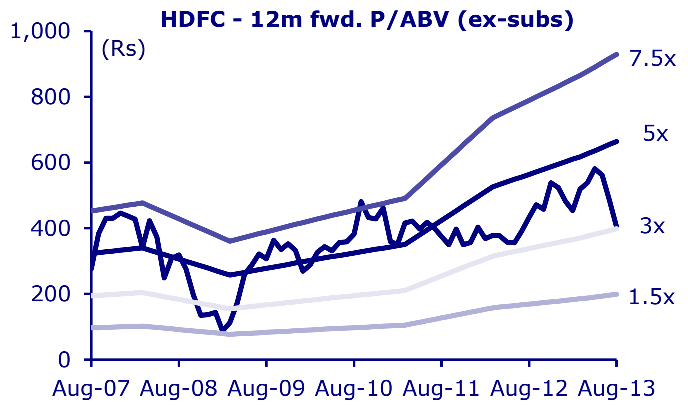
Source: CLSA

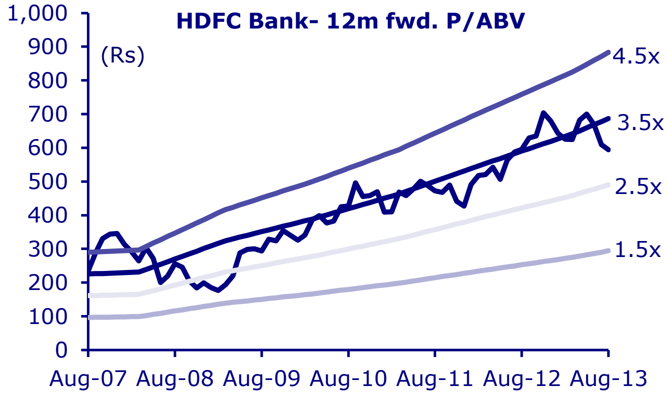
Valuation band charts

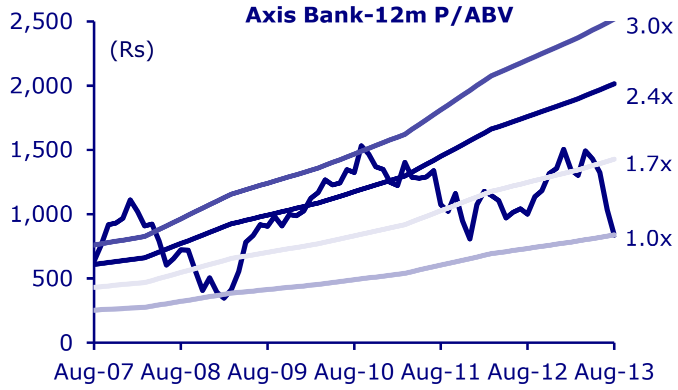


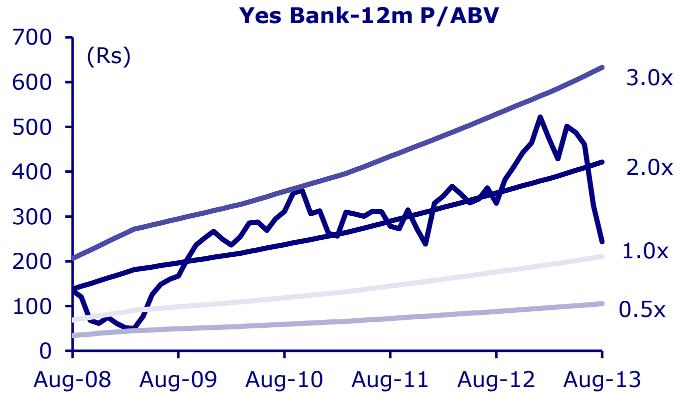


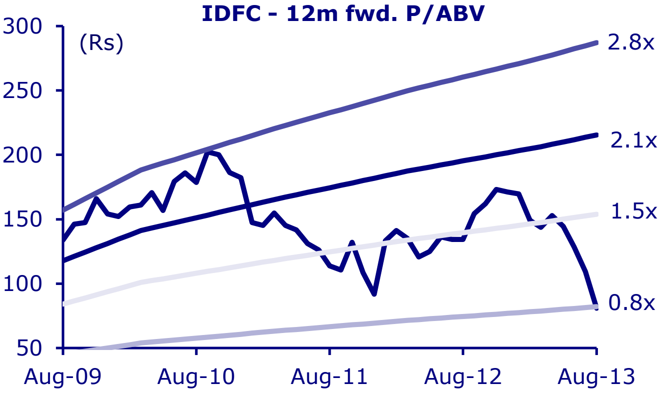


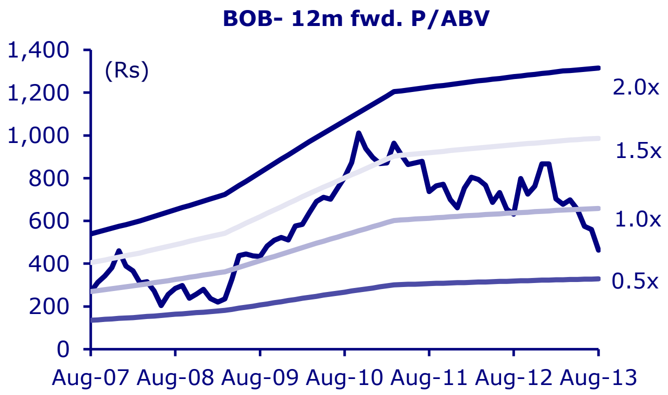


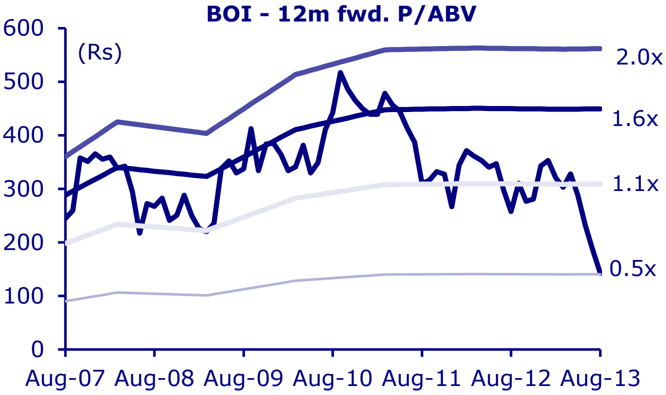


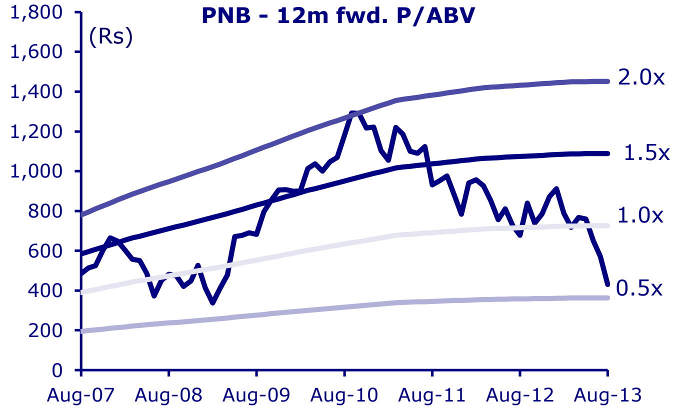


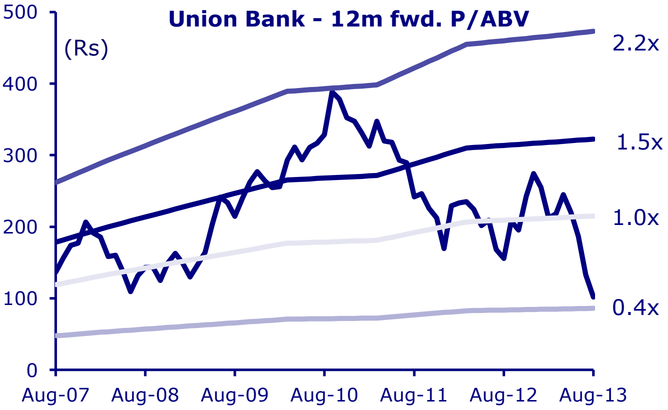












Source: CLSA ; Valuations for ICICI Bank, SBI and HDFC are adjusted for investment in subsidiaries.

Insurance- Premium decline continues

During Jun-13, annualised NBP of sector declined 15% YoY largely due to a 24% YoY decline in LIC's premiums. Premiums for private insurers grew marginally by 5%YoY. LIC's premiums have been declining in each of the past twelve months. Among the private players, Kotak and Reliance Life reported healthy growth in NBP. During the month, LIC's market share was flat at 59%. Irda has extended the deadline for implementation of new norms for traditional insurance products by two months.

LIC drives fall in NBP; private players see marginal growth

- During Jun-13, LIC reported a 24% YoY drop in new business premiums.
- Private sector reported a marginal NBP growth of 5% YoY.

15% decline in NBP of insurers largely due to LIC

- NBP for the sector declined by 15% YoY, largely due to decline in LIC's new business premiums.
- LIC's market share was flat MoM at 59%.

Private players report NBP growth in June; HDFC Life saw a sharp decline

- Among the private players, Reliance and Kotak reported healthy growth in premiums.

ICICI Pru Life reported a NBP decline of 6% YoY

- During June, HDFC Life reported NBP decline of 28% YoY and ICICI Pru reported growth of 6%YoY.

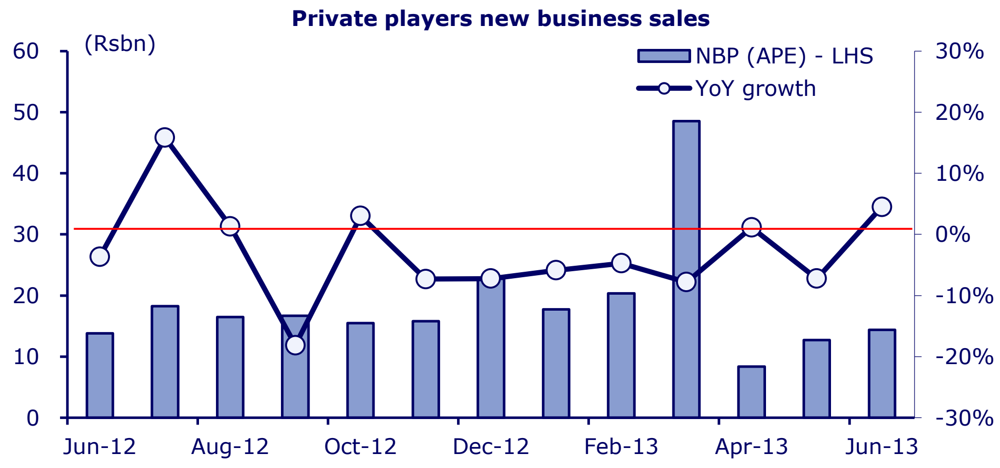
New bancassurance guidelines to be announced in the near term

New bancassurance guidelines to be released soon

- IRDA has indicated that the new bancassurance guidelines will be released over the next month.
- While the current norms allow one bank to tie up with one life, one non-life and one health insurance company, the new norms may allow tie-ups with multiple banks.
- Media reports indicate that as per the draft guidelines banks, which opt to be insurance brokers, will have to cap business from their own group companies at 25% of total annual sales.

Figure 23

In Jun-13, NBP of private players grew by 5% YoY

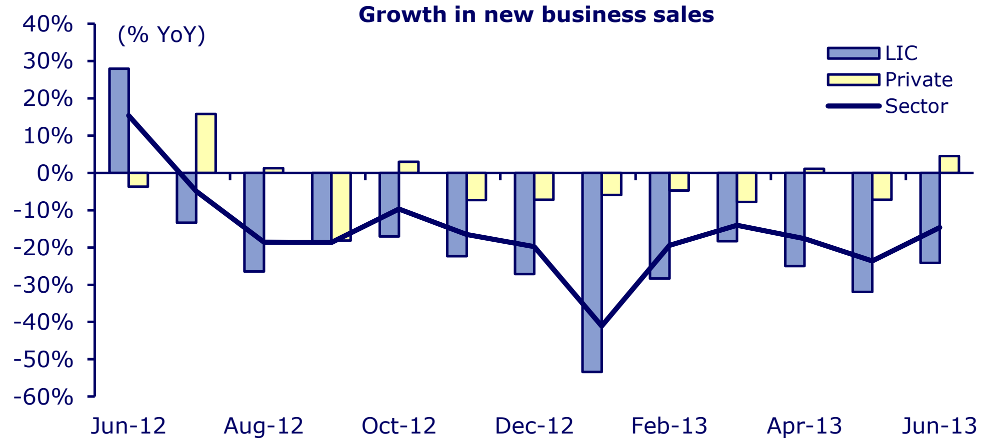


Source: IRDA, CLSA

Decline in premiums was driven by a 25% YoY fall in LIC's premiums

Figure 24

Sector new business premium (APE) declined by 15% YoY



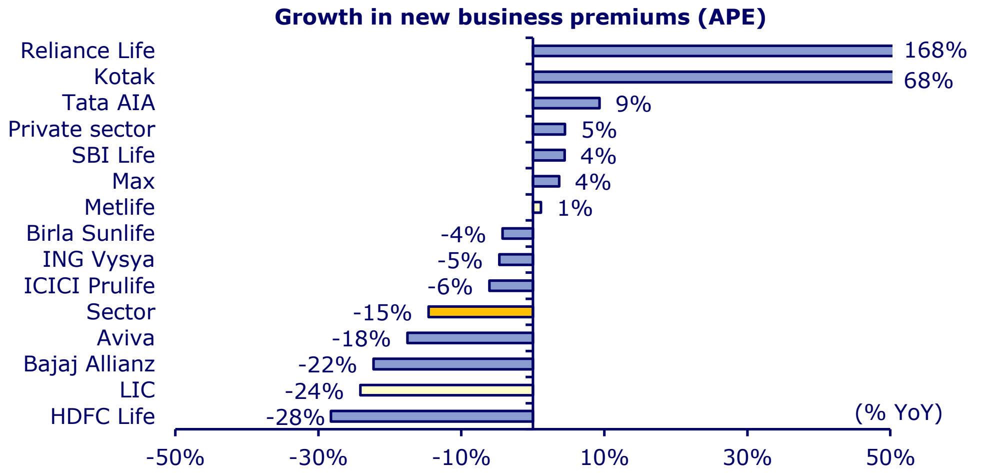
APE: Annualised premium equivalent. Source: IRDA, CLSA

Reliance and Kotak reported growth in premiums

ICICI and HDFC reported decline in premiums

Figure 25

YoY growth trends for Jun-13

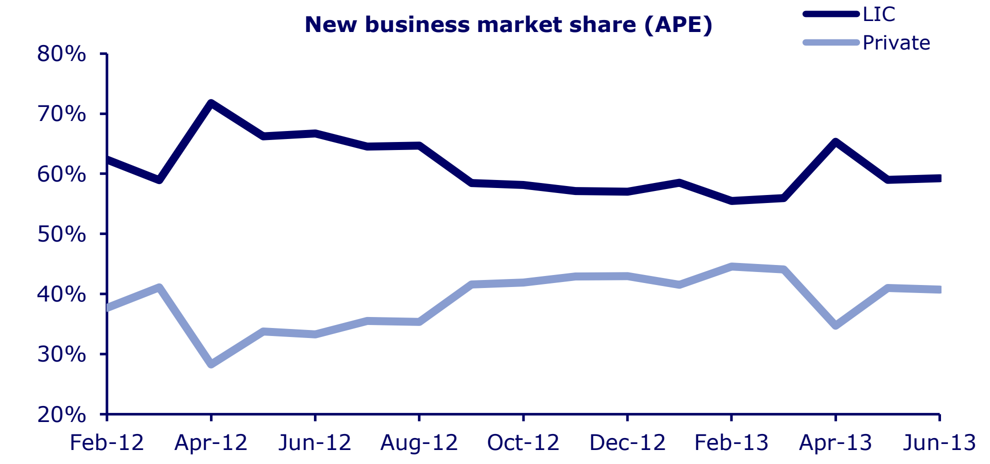


Source: IRDA, CLSA

Every year, LIC gains market share during April due to slower business in private insurance companies

Figure 26

LIC's market share during the month was flat



Source: IRDA, CLSA

Figure 5

Distribution of market share, Jun-13

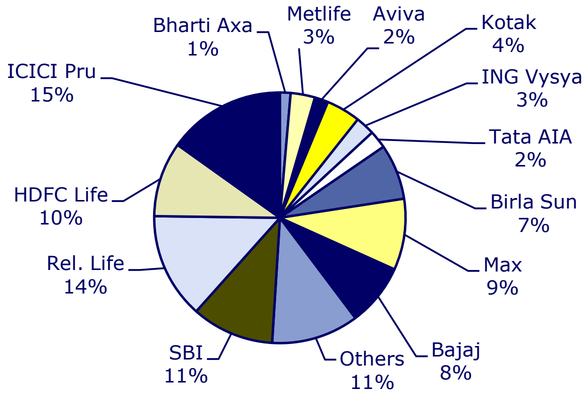
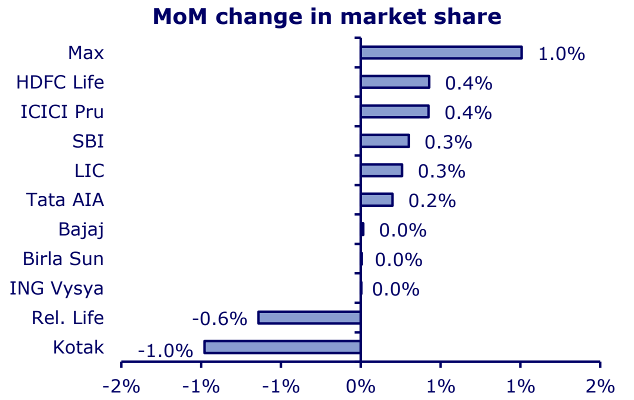


Figure 6

MoM change in market share, Jun-13



Source: IRDA, CLSA

Insurance valuation summary

Figure 10

Insurance valuations matrix

Particulars (FY15) (Rsm)	ICICI Pru. Life	HDFC Std. Life	Max Life	SBI Life
FYP	51,312	54,268	21,538	32,494
Single Premium	11,065	2,178	5,606	61,265
Renewal Premium	88,391	86,252	54,739	56,470
Total Premium	**150,768**	**142,698**	**81,882**	**150,228**
AUM (Rsbn)	853	549	351	950
NBAP margin(%)	**12%**	**14%**	**13%**	**12%**
NBAP	6,268	7,359	2,804	4,818
Multiple (x)	**11**	**12**	**13**	**11**
Value of the Company (Rsm)	289,976	168,083	87,748	135,460
Value of the Company (US$m)	5,272	3,056	1,595	2,463
Value of Parents stake (US$m)	3,901	2,261	1,117	1,823
Indian Partner & Stake	**ICICI Bank, 74%**	**HDFC Ltd, 72%**	**Max India, 71%, Axis Bank 3%**	**SBI, 74%**
Foreign Partner & Stake	**Prudential Plc, 26%**	**Standard Life, 26%**	**Mitsui 26%**	**Cardiff SA, 26%**
Value/share to Parent company (Rs)*	**149**	**63**	**188**	**120**

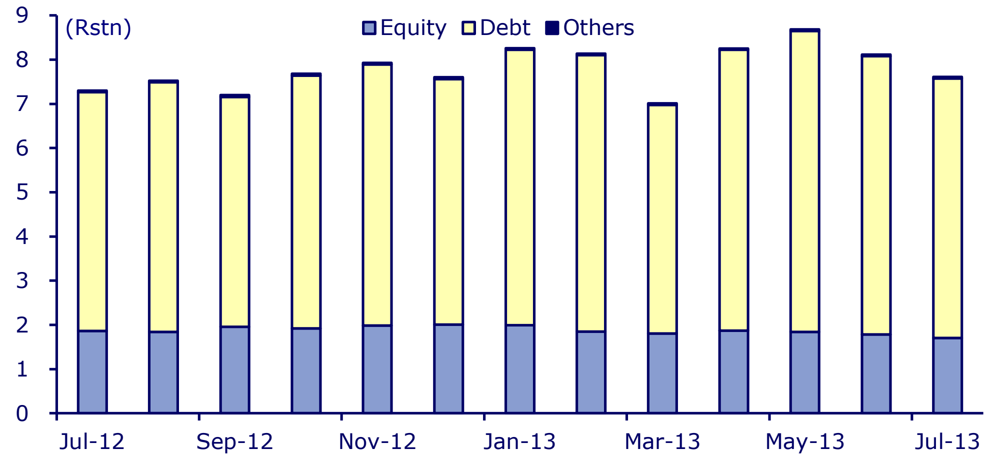
Source: CLSA ; * Post a 20% holding company discount; Valuations are based on an Appraisal value

Mutual fund trends- July 2013

AUMs grew 4%YoY

Figure 27

AUMs declined by 6% MoM to Rs7.6tn

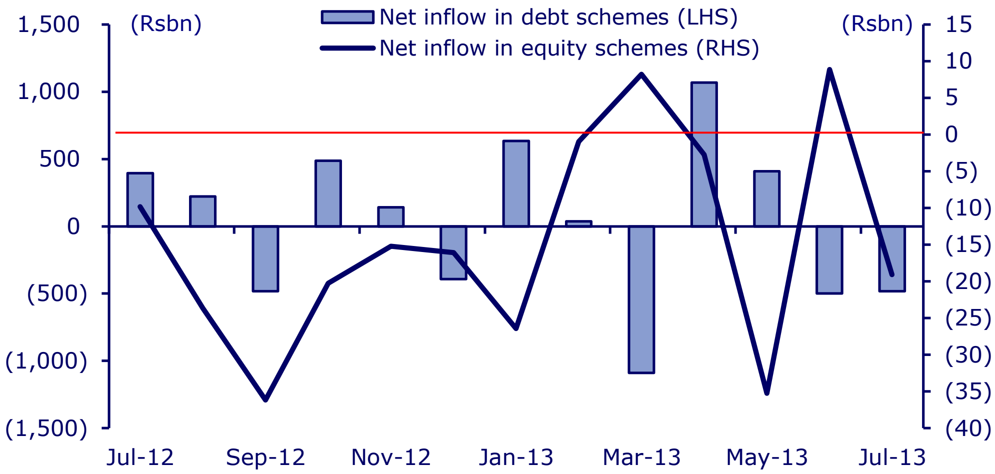


Source: AMFI, CLSA

Equity schemes also saw outflows on the back of redemptions

Figure 28

Debt schemes saw outflows due to sharp rise in interest rates

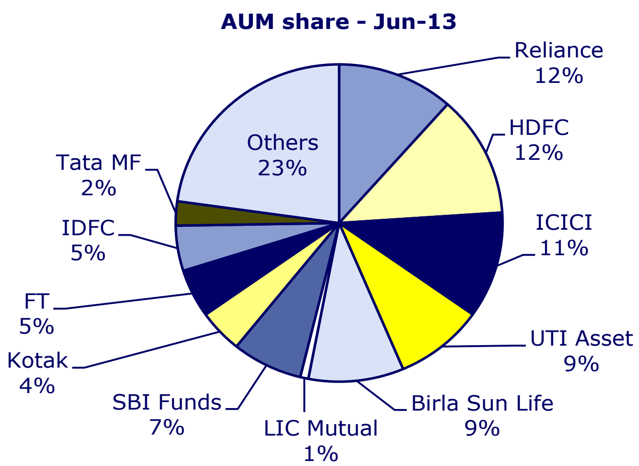


Source: AMFI, CLSA

Mar-13 growth for Top-5
HDFC: +13% YoY
Reliance: +21% YoY
ICICI: +26% YoY
Birla: +19% YoY
UTI: +23% YoY

Figure 29

Market share among mutual funds, Jun-13



Source: AMFI, CLSA

Take a look!

Extract from parting speech by RBI's governor Dr. D Subbarao

Ears close to ground

When I was appointed Governor of the Reserve Bank in 2008, I went to call on the Prime Minister before I took charge. A man of few words as we all know, he told me one thing that stuck in my mind: "Subbarao, you are moving from long experience in the IAS into the Reserve Bank. In the Reserve Bank, one runs the risk of losing touch with the real world. With your mind space fully taken up by issues like interest rates, liquidity traps and monetary policy transmission, it is easy to forget that monetary policy is also about reducing hunger and malnutrition, putting children in school, creating jobs, building roads and bridges and increasing the productivity of our farms and firms. Keep your ear close to the ground.

Lessons from crisis

As someone said, this crisis was too valuable to waste. In the event, we learnt several lessons in crisis management. I will only list the important ones. First, we learnt that in a global environment of such uncertainty and unpredictability, policy action has to be swift, certain and reassuring. Also, during crisis times, it helps enormously if governments and central banks act, and are seen to be acting, in concert. Second, we learnt that action is important, but communication is even more important. When the economic environment is uncertain, market players and economic agents look up to governments and central banks for both reassurance and clarity. Indeed, communication was a critical tool all central banks, including India, adopted in those heady autumn days of 2008. The third lesson we learnt is that even in a multi-nation crisis, governments and central banks have to adapt their response to domestic conditions.

Thank God, the Reserve Bank exists

A final thought on this issue of autonomy and accountability. There has been a lot of media coverage on policy differences between the government and the Reserve Bank. Gerard Schroeder, the former German Chancellor, once said, "I am often frustrated by the Bundesbank. But thank God, it exists." I do hope Finance Minister Chidambaram will one day say, "I am often frustrated by the Reserve Bank, so frustrated that I want to go for a walk, even if I have to walk alone. But thank God, the Reserve Bank exists".

For link to full speech click **here.**

Other important news and interviews

Regulatory and sector newsflow

RBI has decided to open a forex swap window to for dollar requirements of PSU OMCs

- **RBI** has decided to **open a foreign exchange swap window** to meet the **daily dollar requirements** of the three **public sector oil marketing companies.**
- **RBI**, in a discussion paper, has indicated that it **might not be mandatory for existing foreign banks** to **convert** themselves **into subsidiaries** of their parent banks.
- **RBI** has **raised** the **rate of interest subvention** on pre and post shipment rupee **export credit** for certain employment oriented export sectors **by 100bps to 3%**.
- **RBI** has **allowed banks** to **exclude incremental FCNR (B**) and **NRE deposits** with tenor of more than 3 years, **from their liabilities (NDTL)**. Hence banks will not have to provide **CRR/SLR** on these deposits. This relaxation is only for deposits mobilised by banks after 24th August.

RBI has raised the interest rates on FCNR (B) deposits by 100bps

- **RBI** has **raised** the **interest rates on FCNR (B)** deposits having maturity in the range of 3-5 years from **Libor + 300bps to Libor + 400bps.** This will enable banks to incentivize deposits from NRIs.
- **RBI** has urged **PSU banks** to look at **derivative products** to deal with **interest rate risks.**
- **RBI** has asked **banks to increase credit allocation** and proportion of **branches** in **rural areas.**
- **RBI** received 194 bids for Rs272bn at the **auction** of the **35-day cash management bills.** It accepted 114 bids aggregating Rs110bn with **the yield to maturity of 11.7%.**
- **RBI Dy. Governor** has expressed that **second restructuring of loans to Microfinance Institutions** will **not get any provisioning benefit** and **banks** will have **to provide 15% of restructured amount as provision.**
- **RBI** has tightened hedging rules by making it **mandatory** for **foreign institutional investors** to obtain **consent** of **holders of participatory note** (P-Note) and **derivative instruments before hedging.**
- The **Finance Ministry** has asked **PSU banks** to strictly **monitor large corporate houses** that have accounts with several banks and have **defaulted in their payments** with any other PSU banks.

NHB has received a proposal from mortgage firms to raise US$1.3bn under ECB route

- The **Central Bureau of Investigation (CBI)** has initiated an inquiry into cases of **defaulters of big loans from PSU banks**.
- The **Finance Ministry** plans to increase the **weightage given to debt recovery** in the **appraisals of top PSU bank managers** in an effort to stem the rising tide of bad loans at these lenders.
- **National Housing Bank**, (Housing Finance Companies regulator) has received a **proposal** from various mortgage firms including **HDFC and LIC Housing Finance** to raise about **US$1.3bn** under the **external commercial borrowing (ECB) route.**

NHB has raised the maximum tenure of public deposits for HFCs by 3 years to 10 yrs

- **National Housing Bank (NHB)** has raised the **maximum tenure of public deposits** that HFCs can raise from 7 years to 10 years.
- **IRDA** has come up with **regulations for licensing of banks** as **insurance brokers**. RBI has previously expressed concerns over allowing banks to act as brokers.

IRDA has come up with regulations for licensing of banks as insurance brokers

- **IRDA** has notified that **Insurance companies' investment in debt instruments** issued by **Housing Finance Companies (HFC) and Infrastructure Finance Companies (IFC)** will no longer be included under exposure to Financial and Insurance Activities. This will help HFCs and IFCs to attract long term funds from insurance companies.

- India's **WPI inflation** rose to **5.7% in July** compared to 4.9% in June.
- During June, **India's Index of Industrial Production** (IIP) **declined by 2.2%** as against a 1.6% decline in May.
- **CPI Inflation** declined marginally to 9.64% in July from 9.87% in June.
- As per media reports, **Aircel** has tied up nearly **Rs80bn in loans** as part of a move to **refinance its existing debt** from **IDFC** and **Credit Suisse**.

Banks have asked Lanco Infratech to recast the entire group debt of Rs 400bn

- As per media reports, banks have asked **Lanco Infratech** to recast the entire group debt of Rs 400bn rather than restructuring the debt of one subsidiary at a time.
- The **Power Ministry** plans to **seek Cabinet approval** for tweaking the Financial Restructuring Package for accommodating **Jharkhand, Bihar, Andhra Pradesh, Karnataka** in its debt rejig plan for the **SEBs**.
- **Essar Steel** has informed its lenders that it would have to seek restructuring of its debt or additional **Rs60bn** in loans. **SBI, IDBI Bank, Canara Bank, ICICI Bank, and PNB** are the **main lenders** to the company. It plans **to raise US$2bn** through **pre-export finance** to retire rupee-denominated debt.
- **A consortium led by State Bank of India** has taken possession of Kingfisher House, the corporate office of **Kingfisher Airlines** which owes about **Rs70bn to the lenders.**
- **Essar Oilfields Services**, a wholly owned subsidiary of **Essar Shipping**, plans to convert a part of its Rs3bn loan from rupee to US$.
- Ratings agency, **Standard & Poor's**, has maintained its **negative outlook on India.**

Moody's has downgraded the baseline credit assessments of PNB, Bank of Baroda and Canara Bank

- Ratings agency, **Moody's**, has **downgraded** the baseline credit assessments (BCA) of **Punjab National Bank** (from ba3 to ba1), **Bank of Baroda** (from ba2 to ba1) and **Canara Bank** (from ba2 to ba1) on the back of adverse economic environment.
- **SBI** has expressed that **banks may not lend** for **telecom spectrum purchases** if prices are kept high, like in the case of 3G spectrum auctions, as such funding is treated as unsecured loans.
- **Banks** are considering **introduction of voice biometrics** as an option for authenticating phone banking.

Company newsflows

- **The Finance Ministry** has sought relaxation in the **selection guidelines** for SBI Chairman to facilitate the inclusion of Mr A Krishna Kumar in the consideration set.
- **SBI** plans to **merge one of its associate banks** by the end of September.

SBI does not plan to increase lending rate

- **SBI does not plan to increase lending rates** in spite of some private banks increasing their Base Rates.
- **SBI** has appointed **Ms. Arundhati Bhattacharya** as **new CFO and MD** and promoted seven of its CGMs as deputy MDs.

SBI has appointed Ms. Arundhati Bhattacharya as new CFO and MD and promoted seven of its CGMs as deputy MDs

- **ICICI Bank** plans **to sell** one of its **residential buildings in central Mumbai** for about Rs1bn, in line with its strategy of offering its executives compensation for rent instead of accommodation.
- **ICICI Bank** has seized Jeera (Cumin Seeds) stock reportedly worth **Rs53m** at two **National Spot Exchange Ltd's (NSEL) warehouses** that had been pledged with the bank.
- **HDFC Bank** plans to open **300 new branches** across India during FY14.
- **Axis Bank** has raised **interest rates on non-resident external** (NRE) **fixed deposits** for above 3 years by 50-75bps and **FCNR-B deposits** of over three years by 1%.

HDFC Bank and Kotak Mahindra Bank plan to open 300 and 100 new branches respectively during FY14

Union Bank of India plans to raise Rs30bn to meet Basel III norms

OBC has sought Rs16bn during the current fiscal from the government

PFC plans to raise at least Rs1.5bn through private placement of tax-free bonds

- **Kotak Mahindra Bank** plans to **hire about 1,500-2,000 people** during FY14.
- **Kotak Mahindra Bank** has contested **IDBI Bank's claim** on key trademarks of Deccan Chronicle. The dispute is being adjudicated by the **Debt Recovery Tribunal.**
- **Kotak Mahindra Bank** plans to open **100 new branches** during FY14 to take its branch network to 550.
- **Punjab National Bank** has **raised interest rates on FCNR (B) deposits** of over three years by 1% across currencies.
- **Bank of Baroda** does not plan to raise money through the **Medium-Term -Note program** as the liquidity situation of its international operations is comfortable.
- **Ratnakar Bank** will be **acquiring Royal Bank of Scotland's business banking, credit cards and mortgage businesses** in India. **Yes Bank** and **IndusInd Bank** were also in the fray to acquire these assets.
- As per media reports, **Yes Bank's Rana Kapoor's efforts** to **reconcile** with **co-promoter Madhu Kapur** through an out-of-the-court settlement have not made much headway.
- **Union Bank** plans to open **branches in London, Sydney and Antwerp** during FY14.
- **Mr. Rakesh Sethi** has been appointed as **ED of Union Bank**. Prior to this role he was the General Manager at Bank of India.
- **Union Bank of India** plans **to raise Rs30bn** to meet Basel III norms after 2015.
- **Canara Bank** is considering to **takeover of assets and liabilities** of Bangalore-based **Amanath Cooperative Bank**.
- **Canara Bank** announced a **tie up with United India Insurance** for cross promotion of each other's products.
- **Canara Bank** is reportedly in talks with a number of **NBFCs**, including **Capital First**, **Bajaj Finserv** and **Indiabulls Finance**, to buy a part of their retail loan portfolio.
- **Corporation Bank** plans to **disburse around Rs100bn to the agriculture sector** during FY14. **State Bank of Travancore** has raised **interest rates on FCNR (B) deposits** of over three years by 1% across currencies.
- **Corporation Bank** plans **to open nine more SME loan centres** by the end FY14.
- **OBC** plans **to moderate its branch expansion plan** to 125-150 branches during FY14 in the wake of the current economic slowdown.
- **The Government** has appointed **V. Kannan** as **Chairman and Managing Director of Vijaya Bank**. Mr. Kannan, is currently the Executive Director at **Oriental Bank of Commerce**.
- **OBC** has **sought Rs16bn** during the current fiscal **from the government** to shore up its capital base.
- **RBI** has notified the **decrease in FII investment limit in IDFC Ltd** from 74% to 54%. IDFC's shareholders had reduced the limit on its foreign shareholding from 74% to 54% in order to move closer to the cap that applies to banks (49%)
- As per media reports, **IDFC** may not acquire **74% stake in Delhi-Gurgaon expressway.**
- **PFC** plans **to raise at least Rs1.5bn** through **private placement of tax-free bonds.**
- **REC plans to raise over Rs370bn** during FY14 through various instruments from both domestic and international markets.
- **REC** has sought **SEBI's approval to raise up to Rs50bn** through tax-free bonds.

Development Credit Bank has raised its Base Rateby 35bps to 10.85%

- **Development Credit Bank** has **raised its Base Rate** and **Benchmark Prime Lending Rate** by **35bps each** to 10.85% and 18.1%.
- **ING Vysya Bank** has **raised interest rates on deposits** by 25-50 basis points across maturities.
- **Federal Bank** has filed an application with **Foreign Investment Promotion Board (FIPB)** for increasing the foreign shareholding limit to 65%.

TPG has acquired a 22.6% stake in Shriram City Union Finance

- **Texas Pacific Group** has acquired a **22.6% stake in Shriram City Union Finance** for about Rs12bn.
- **IDBI Bank** plans to auction four newspaper titles owned by **Deccan Chronicle Holdings**, despite some other lender's staking claim on trademarks.
- **Lakshmi Vilas Bank** has raised its **Base Rate by 25bps to 11.25%.**
- **Reliance Life Insurance** is exploring **a distribution tie-up** with several banks and may offer a stake of up to 5% for the same.
- **United Bank of India** plans **to open 1,000 ATMs** and **about 250 branches** during FY14 to increase its delivery channel.
- As per media reports, **Manulife Financial Services** plans **to acquire Exide Industries' 26% stake in ING Life Insurance.**
- **Federal Bank** has raised **short term domestic term deposit rates** by up to 150bps. It has also raised **NRE term deposit rates** by 25bps to 9% for deposits with maturity of greater than 3 years.
- **Syndicate Bank** has raised interest rates of FCNR(B) deposits with maturity of greater than 3 years by 100bps.

Indian Overseas Bank plans to raise around US$500m through MTN Programme

- **Indian Overseas Bank** plans **to raise around US$500m** through **Medium Term Note Programme (MTN)** before December.
- **SREI BNP Paribas** has raised its **benchmark rate by 50bps to 17.75%.**
- **McGraw Hill Financial** has **raised its stake in Crisil by 15.1% to 68%** through purchase of shares worth Rs12.9bn.
- **Dena Bank** has raised **interest rates on FCNR (B) deposits** of over three years by 1% across currencies.
- **Andhra Bank** has raised its **Base Rate by 25bps to 10.25%.**
- **Karnataka Bank** has **increased interest rates on term deposits by 25-50bps** across various maturities.

IDBI Bank has merged some of the maturity buckets and increased the interest rates for its domestic retail term deposits

- **IDBI Bank** has merged some of the maturity buckets and **increased the interest rates** for its domestic retail term deposits.
- **IDBI Bank** has announced the **auctioning of four newspaper titles** owned by **Deccan Chronicle Holdings (DCHL).**
- **Muthoot Finance** plans to raise **NCDs worth Rs3bn** and has **filed draft prospectus** with **SEBI** (capital market regulator).
- **Everstone Capital** has **infused Rs2bn** in **Hinduja Leyland Finance**, an NBFC jointly owned by **Ashok Leyland** and other entities of the **Hinduja Group**.

Muthoot Finance has filed draft prospectus with SEBI to raise NCDs worth Rs3bn

- **Indiabulls Housing Finance** has acquired the **entire 42.5% holding of Amaprop** in its subsidiary, **Indiabulls Finance Company** for Rs2.6bn.
- As India's largest credit information company, **CIBIL** has **930 credit institutions** as its **members** and maintained information on over 290m consumer trades.

- **Karur Vysya Bank** has **received the board approval to raise up to Rs10bn** through QIP.

- **Mr. Jai Kumar Garg** has been appointed as **Executive Director of UCO Bank**. Prior to this role he was the General Manager at **Corporation Bank**.

- **Ms. Trishna Guha** has been appointed as **ED of Dena Bank**. She was the General Manager in **Allahabad Bank** previously.

- **Aviva** plans **to sell its 26% stake** in **Aviva India, the joint venture with Dabur.** As per media reports, the stake, which is valued around US$250m, could be sold either to another global insurer or to **Dabur.**

- **RBI** has appointed **Mr. Manoranjan Dash** as **an additional director on Dhanlaxmi Bank's board** due to the spike in bad loans of the bank.

- **Rajeev Rishi** has been appointed as **Chairman and Managing Director of Central Bank of India.** He was the **Executive Director at Indian Bank** previously.

Interesting interviews

Pratip Chaudhuri (Chairman, SBI) (link)

Incremental relief on CRR/SLR to my mind is not very material.

On the rupee and FCNR (B), these are only projections. We have to wait and see how much money comes in and I think Reserve Bank of India (RBI) raised the rupee rates to 8%, they took a long time to raise the FCNB rates. So by the time the rupee rates were raised to 8-9%, some people had even 9% rates because the difference between the domestic rates and the NRI rates will be done away with. So that is why we are seeing relatively slow dollar flow. I think now dollar flows have accelerated on the back of the increase in the treasury rates in US. So they would continue at a reasonable pace but incremental relief on CRR/SLR to my mind is not very material. Had the relief been given on entire corpus then it would have been more effective.

V R Iyer (CMD, Bank of India) (link)

The bank's liquidity position is fairly comfortable.

The bank's liquidity position is fairly comfortable. We do not have any high liquidity mismatches. We also are not feeling the need to borrow in the marginal standing facility (MSF). The deposit growth was pretty decent in Q1. We have good deposits for that matter. I do agree that we will not be able to continue this way as in the current quarter's deposit growth, has not been to the level as it was in the Q1. So, maybe within a week or ten days, we will revisit that. Whether there is a case for us to increase the rate of interest from the deposits, we will also relook at the base rate increase

V R Iyer (CMD, Bank of India) (link)

We expected NIM to improve to 3.2% on the domestic side, in this financial year

A 25 basis points cut will impact income in the next nine months. But, I should also say our cost of funds have come down in the first three months. We are hoping improvement in retail deposit mobilisation will help us protect the margins. We expected NIM to improve to 3.2% on the domestic side, in this financial year, which is 3% in March quarter. On the international front, we see NIM rise from 1.05 to 1.20. We have high unutilised portion in fund-based and non-fund based facilities. We found that our pricing is high and not in line with the market. We are trying to revisit these issues. That should help in better utilisation of loans, which are already sanctioned. My credit-deposit ratio in domestic business is about 67 per cent, which means we have a lot of liquidity. This is also an area, which we are planning to improve.

R K Dubey (CMD, Canara Bank) (link)

There is some restructuring we expect to come in the coming three quarters.

Yes, there has been restructuring of assets and there has been more slippage than the upgradation. The recovery was a record one of Rs8.9bn and upgradation of more than Rs10bn. But the slippage has been more than Rs 28bn because of which our non-performing asset (NPA) has gone to 2.9%. There is some restructuring we expect to come in the coming three quarters. It may be around 15 accounts worth around Rs40-50bn. That may be

This year's good monsoon has given a comfort level to lend and recover.

Non-performing assets are low in the small retail segment.

About Rs 15bn worth of assets are in the restructuring pipeline

Around 22% of our advances are under gold portfolio, which is very well managed

coming in each quarter. Some may come in this quarter; some may come in December or March quarter. It may be one or two accounts less or more.

R K Dubey (CMD, Canara Bank) (link)

This year's good monsoon has given a comfort level to lend and recover. Since April, we have seen credit growth to agriculture sector of 42 per cent. Through the year, we expect to reach an overall growth of around 35 per cent. The recovery in Q1FY14 (Rs8.9bn) reconfirmed the belief that borrowers, particularly retail borrowers, do not intend to default. Understanding the situation, minimum sacrifice and adjustments has been the key to our recovery effort. We are restructuring or rescheduling education loans. This portfolio NPA worth Rs3.6bn was expected to come down to Rs1bn this year through negotiations with students or parents.

R K Dubey (CMD, Canara Bank) (link)

Non-performing assets are low in the small retail segment. What happens is that a big loan turns bad and that affects the entire loan book. But we have been focusing on recoveries very aggressively. Due to our stance on recoveries, we have managed to keep our non-performing assets under control. We will continue to focus on recoveries. We have bought down our net NPAs in the current quarter to 2.34%. We are not going to raise interest rate - at least in the next coming days. The environment is tough but we will watch and not raise interest rates suddenly and continue to keep the rates low for our customers. We are looking at a 20% loan growth in the coming year. Our agricultural loan book is growing more than 30%. Growth in the rural areas has been very good and we confident of good growth coming from these areas. Overall, our loan book should grow by around 20% in the next year.

S L Bansal (CMD, Oriental Bank of Commerce) (link)

About Rs 15bn worth of assets are in the restructuring pipeline, but as you are aware restructuring for discoms is already over and we are expecting that within the next 20 days the state governments will issue the bonds in Haryana, Rajasthan and Uttar Pradesh and about Rs16bn worth of bonds will be received, which will take off our assets book and then the restructured book will more or less will remain the same, closer to Rs100bn, as far as slippage is concerned. So long as there is stress in the economy, I cannot give you a commitment that slippages will come down. In the beginning of the year, we had given you clear cut direction that we expect slippages to be in the range of Rs7.5-8bn and overall slippages can be Rs32bn in the year and against that we expected our recovery to move from Rs20-22bn, so the gap between recovery and slippage comes down, that is our guidance and we continue to maintain that guidance.

S L Bansal (CMD, Oriental Bank of Commerce) (link)

Before July 15 most of the banks were sitting on reasonable amount of profits. Then all of a sudden the yields starts moving northwards and the banks were sitting on the huge losses. So, we made a representation to the RBI, which they have very kindly accepted. Now most of the securities can be accommodated in HTM category and whatever remaining securities are there in Available for Sale (AFS) category. Some losses will be there which can be amortised in the next three quarters. So it is a normal business, is a normal business risk. Going forward what is going to happen it is to be seen.

V A Joseph (MD & CEO, South Indian Bank) (link)

Even when the gold prices have fallen there are absolutely no issues as far as our bank is concerned, because we have been maintaining adequate margin. So it never happened that the price has fallen below the margin what we have been keeping. So we are quite comfortable. With the rise in gold prices now the securities have become much more than what is required. It has appreciated very well. So there are absolutely no issues. As far as South Indian Bank is concerned, as you maybe aware, around 22% of our advances are under gold portfolio, which is very well managed and there are absolutely no issues.

The increase in Base Rate is not to alleviate liquidity pressure

CVR Rajendran (ED, Bank of Maharashtra) (link)

The increase in Base Rate is not to alleviate liquidity pressure, as such it is to pass on the additional costs which we are incurring because of this liquidity pressure today. More than 30 percent of our deposits today are interest-sensitive deposits, which means more than Rs10m and unless we increase the cost of deposits we may not be in a position to retain these deposits. So it becomes absolutely essential to increase deposit rates. So we have increased between 150-200 bps on various short-term slabs. Base rate is nothing but a cost-plus contract, so naturally this has to be passed onto customers.

We had an AFS portfolio which was really sensitive to rate of interest.

S S Mundra (Chairman, Bank of Baroda) (link)

We had an AFS portfolio which was really sensitive to rate of interest. AFS portfolio would also carry the non-interest rate sensitive securities, treasury bills etc. which was around 14-14.5 percent, then of course the HTM and all other things are there. As far as relief is concerned, number one relief or no relief or what would have been the MTM situation would be ultimately the relevant date would have been 30th September when you are closing the books and you are marking it. If I would have been required believing that the peak yield which had gone up to 9.4% or so would have persisted till 30th September then I would have been required to provide something like Rs5bn towards the MTM. This now under the new dispensation would not be required to be provided for.

We have been a little more cautious in this part of the quarter

Umesh Revankar (MD, Shriram Transport Finance) (link)

We have been a little more cautious in this part of the quarter because we feel that unless the economy picks up, we should be little careful on the loan-to-value (LTV) fronts. We have reduced our LTV and are demanding more margins from the customers because we feel that by reducing the LTV controlling the demand is very much important at this stage rather than getting into lending or looking at the growth for time being.

As of now consumer loans is 40% of the business

Sanjiv Bajaj (MD, Bajaj Finserv) (link)

As of now consumer loans is 40% of the business, SME is 50% and commercial loans is 10%.For the first 20 years of Bajaj Finance, we only did consumer loans to finance our own motorcycles. Thereafter, we decided to de-risk our business and created the country’s first diversified NBFC. Construction equipment loans are a part of our commercial book, which we slowed down, given the current problems facing the infra space. However, we continue to cautiously build our consumer and SME business. Traditionally, PSU banks lend to SMEs. Only in the past few years have some private banks started lending to SMEs. The demand-supply gap is huge and there is enough opportunity. We lend to small and medium enterprises with annual revenues between Rs250-300m. Our loans are both for working and growth capital and mostly secured by mortgages. We focus on the larger SMEs and hence, while the typical SME loan size is Rs4-5m in the industry, our average loan size is Rs25m. Since we deal with comparatively larger SMEs, our risk is lower.

We are specialists in the business of infrastructure.

Hemant Kanoria (CMD, SREI Infrastructure Finance) (link)

We are specialists in the business of infrastructure. Though we have a large portfolio (Rs345bn in June) — primarily in construction and mining equipment — we do not have much exposure in stressed assets (especially) in road and power. In the equipment financing business we are well securitised. Many people are now trying to take action. But we saw the trend early and took necessary steps. We are cutting back on costs, and looking at increasing our fee-based income. Clients need specialists to help them in difficult times. So, we are looking at these opportunities. We made some short-term financing to Deccan. We got stuck. We have some properties and are adequately secured. But then there is a process to sell the property, pay lenders and so on. In hindsight, it was a mistake.

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Figure 30

India Banking calendar–September –October 2013

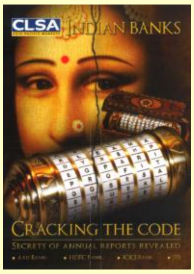
CLSA

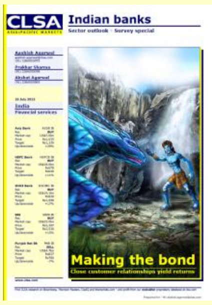
India: Banking calendar - September- October 2013

Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Sunday
September **2**	**3**	RBI: Fortnightly update **4**	**5**	RBI: Weekly stat. supplem **6**	**7**	**8**
Markets closed **9**	**10**	**11**	**12**	RBI: Weekly stat. supplem **13**	**14**	**15**
16	**17**	RBI: Fortnightly update **Mid-quarter monetary policy review** **18**	**19**	RBI: Weekly stat. supplem **20**	**21**	**22**
CLSA Hong Kong Forum **23**	**CLSA Hong Kong Forum** **24**	**CLSA Hong Kong Forum** **25**	**CLSA Hong Kong Forum** **26**	RBI: Weekly stat. supplem **CLSA Hong Kong Forum** **27**	**28**	**29**
30	**October** **1**	RBI: Fortnightly update **2**	**3**	RBI: Weekly stat. supplem **4**	**5**	**6**

Source: Bloomberg, News, CLSA

Latest CLSA financial sector research





New sector reports

1. Sector report, 'New main streets'
2. Sector report, 'Cracking the code' and four company reports
    a. SBI
    b. ICICI Bank
    c. HDFC Bank
    d. Axis Bank
3. Indian Banks – Making the bond

Links to sector reports

1. RBI eases a bit
2. 1QFY14 result review
3. Credit growth is picking up
4. 1QFY14 result preview
5. Public Service?
6. Provision on unhedged exposures
7. Impact of INR's weakness on banks
8. Bank license- a tough call for NBFCs
9. Final norms for restructuring
10. Disappointing quarter – 4QFY13 review

Links to company reports

1. **IDFC** – Roadshow Feedback (link)
2. **SBI** – Reality check (link)
3. **HDFC** – Benevolent change in norms (link)
4. **Union Bank** – Notes from management meeting (link)

1QFY14 result review notes

1. **SBI** – Asset quality pressure (link)
2. **HDFC Bank** – Stretching out (link)
3. **Axis Bank** – Balancing well (link)
4. **ICICI Bank** – Steady performance (link)

5. **Yes Bank** – Challenges ahead (link)
6. **IndusInd Bank** – Balancing Well (link)
7. **Canara Bank** – Pressure to persist (link)
8. **OBC** – Better on NPLs; Worse on treasury (link)
9. **J&K Bank** – Steady performer (link)
10. **Bank of India** – Stable asset quality (link)
11. **Bank of Baroda** – Asset quality disappoints (link)
12. **Union Bank** – A tough quarter (link)
13. **PNB** – Asset quality disappoints (link)
14. **HDFC** – Steady results (link)
15. **IDFC** – Headwinds priced in (link)
16. **REC** – Stable quarter (link)
17. **PFC** – Balance is Key (link)

Links to annual report analysis

1. **ICICI Bank** – FY13 Annual report analysis (link)
2. **HDFC Bank** – FY13 Annual report analysis (link)
3. **Axis Bank** – FY13 Annual report analysis (link)

Previous Banking Monthly: (07-August-2013)

Other detailed reports on banking sector

1. **Chindia banking**- On their way up (link)
2. **Personal banking survey**, 2011 (link)
3. **Banking sector report:** Coming of age (report, data book)

**This report is priced as on 30th August 2013*

Companies mentioned

Axis Bank (AXSB IB - RS835.8 - BUY)
Bank of Baroda (BOB IB - RS462.9 - OUTPERFORM)
Bank of India (BOI IB - RS142.3 - OUTPERFORM)
Canara Bank (CBK IB - RS202.4 - UNDERPERFORM)
Corporation Bank (CRPBK IB - RS250.1 - UNDERPERFORM)
HDFC (HDFC IB - RS718.0 - BUY)
HDFC Bank (HDFCB IB - RS593.8 - BUY)
ICICI Bank (ICICIBC IB - RS804.3 - BUY)
IDFC (IDFC IB - RS80.9 - BUY)
IndusInd Bank (IIB IS - RS356.8 - BUY)
Max India (MAX IB - RS161.7 - BUY)
OBC (OBC IB - RS127.1 - UNDERPERFORM)
PNB (PNB IB - RS430.1 - BUY)
Power Finance (POWF IB - RS108.8 - OUTPERFORM)
Rural Electrification (RECL IB - RS168.5 - OUTPERFORM)
SBI (SBIN IB - RS1,514.4 - BUY)
Union Bank (UNBK IB - RS101.7 - OUTPERFORM)
Yes Bank (YES IB - RS243.3 - OUTPERFORM)

Key to CLSA/CA Taiwan investment rankings: BUY: Total return expected to exceed market return AND provide 20% or greater absolute return; **O-PF**: Total return expected to be greater than market return but less than 20% absolute return; **U-PF**: Total return expected to be less than market return but expected to provide a positive absolute return; **SELL**: Total return expected to be less than market return AND to provide a negative absolute return. For relative performance, we benchmark the 12-month total return (including dividends) for the stock against the 12-month forecast return (including dividends) for the local market where the stock is traded. We define stocks we expect to provide returns of 100% or higher including dividends within three years as "Double Baggers".