

**SEPTEMBER 21, 2018**
**UPDATE**

Coverage view: **Attractive**

Price (₹): **319**

Target price (₹): **250**

BSE-30: **37,121**

**Uncertain future.** Ending months of speculation, **RBI has declined the highly debated extension of tenor for the current MD and CEO of the bank.** This turn of events creates uncertainty and puts the focus on (1) candidates who can take on this challenging role, (2) strategy shift, (3) capital adequacy ratios and (4) potential impact on earnings, especially from corporate banking fees. We capture these uncertainties through a higher cost of equity, resulting in a cut in target price to ₹250 (₹335 earlier). SELL stays.

**Company data and valuation summary**

Yes Bank

**Stock data**

52-week range (Rs) (high,low)	404-285
Market Cap. (Rs bn)	736.8

**Shareholding pattern (%)**

Promoters	20.0
FII	42.5
MFs	11.6

Price performance (%)	1M	3M	12M
Absolute	(18.8)	(3.5)	(14.5)
Rel. to BSE-30	(17.0)	(8.3)	(25.4)

**Forecasts/Valuations**

	2018	2019E	2020E
EPS (Rs)	18.3	19.8	21.7
EPS growth (%)	25.7	8.1	9.5
P/E (X)	17.4	16.1	14.7
NII (Rs bn)	77.4	94.8	109.9
Net profits (Rs bn)	42.2	45.7	50.0
BVPS	108.0	122.7	140.2
P/B (X)	3.0	2.6	2.3
ROE (%)	17.7	16.6	15.9
Div. Yield (%)	0.7	1.0	1.1

**Yes Bank's MD and CEO Rana Kapoor to step down by January 31, 2019**

RBI has curtailed the tenor of MD and CEO, Mr Rana Kapoor to January 31, 2019 ending months of speculation on his extension. The board and shareholders had approved Kapoor's extension for a period of three years. The board is scheduled to meet on September 25, 2018 to decide a future course of action.

**Risks that investors need to be cognizant of for the next few quarters**

Investors need to be cognizant of the following risks: (1) CET-1 at 9.5% implies limited headroom to grow. Raising capital after this uncertainty will not be easy. The bank could be left with an unappetizing choice of slowing down pace of growth, release capital by loan sell down or raise capital at not-so attractive valuations, (2) as a founding member of the bank, Kapoor has left a deep imprint on strategy, operations and execution, a tough act to follow. It will be interesting to see if the new CEO carries on with the existing strategy (a tough act) or makes adjustments (which would carry a cost). (3) Developing the earlier point, an internal or external CEO would different sets of challenges. An external candidate may bring in a fresh set of thinking and actions to lead the bank leading to unpleasant decisions (loan mix, risk appetite and profitability) which can be quite disruptive to the existing business model. An internal candidate would not trigger concerns of disruption but would struggle to match the effectiveness of the current CEO, (4) attrition of senior management bears watching, and (5) sustainability of high earnings contribution from corporate banking bears closer watching. (6) The corporate NPL cycle is turning favorable, which is positive, however, one would always be worried for chunky company specific exposures that are not easily identifiable from the outside.

**Risks have increased, resulting in a cut in target price. Maintain SELL rating**

We maintain our negative stance on the bank but revise our TP to ₹250 from (₹335 earlier) valuing the bank at 1.8X book (2.4X earlier) and 12X March 2020 EPS for RoEs in the range of ~15-17% in the medium term. We have captured the risks mentioned earlier through a higher cost of equity (14.5% from 13.75% earlier). We have also moderated the medium-term growth rate. Despite the recent underperformance, the stock has considerable further scope for underperformance. Retain SELL.

**QUICK NUMBERS**

- **Mr. Rana Kapoor's tenor as MD and CEO of Yes Bank ends by January 31, 2019**
- **Board to meet on September 25, 2018 to decide the future course of action**
- **Maintain SELL. Revise TP to ₹250 (from ₹335 earlier)**

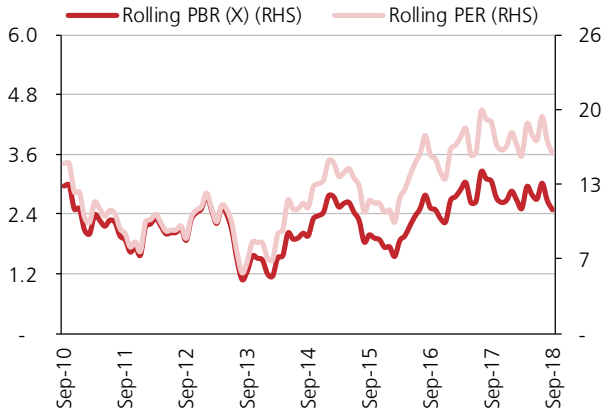
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**Exhibit 1: Yes Bank trading at 2.5X one-year forward book (adj.)**  
 March fiscal year-ends, September 2010- September 2018 (X)



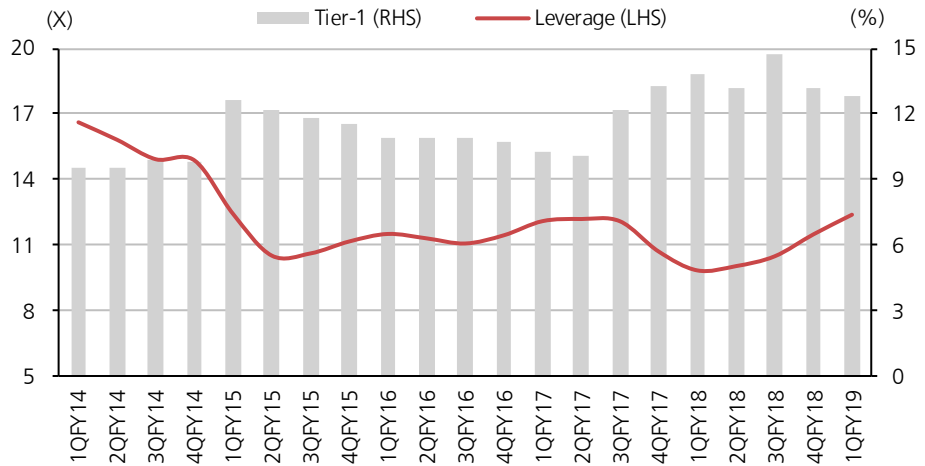
Source: Company, Bloomberg estimates, Kotak Institutional Equities

**Exhibit 2: Yes bank trading premium in line with peers**  
 Yes Bank trading premium to peers, September 2010-September 2018(X)



Source: Company, Bloomberg estimates, Kotak Institutional Equities

**Exhibit 3: Capital consumption remains high**  
 Total assets to net worth, March fiscal year-ends, 1QFY14-1QFY19 (X)



Source: Company, Kotak Institutional Equities

**Exhibit 4: Contribution of corporate banking fees continues to rise**

Break-up of fee income, March fiscal year-ends, 2008-1QFY19 (%)

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	1QFY19
Corporate trade and cash management	19	24	30	28	26	25	24	17	11	13	13
Retail banking	9	7	10	9	11	12	20	23	22	22	20
Forex, debt capital markets and securities	25	21	24	11	6	22	13	10	17	11	21
Corporate banking fees	21	31	39	38	39	32	37	39	35	38	40
Treasury trading and others	26	17	(3)	14	18	9	6	12	15	16	7

Note:

1) Treasury and trading income has been clubbed with forex, DCM and securities.

Source: Company, Kotak Institutional Equities

**Exhibit 5: Yes Bank is targeting to improve the share of retail loans to overall loans**

Break-up of loans, March fiscal year-ends, 2008-1QFY19 (%)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	YoY (%)
Loan book	1,059	1,102	1,171	1,323	1,400	1,487	1,715	2,035	2,147	53
Corporate and institutional	715	748	807	895	953	1,002	1,161	1,382	1,452	52
Business banking	117	118	125	139	139	147	170	197	187	35
Micro and small	128	141	138	163	161	168	182	208	208	29
Retail	100	95	101	126	147	169	202	248	301	105
% of loan book										
Corporate and institutional	68	68	69	68	68	67	68	68	68	-50 bps
Business banking	11	11	11	11	10	10	10	10	9	-120 bps
Micro and small	12	13	12	12	12	11	11	10	10	-180 bps
Retail	9	9	9	10	11	11	12	12	14	350 bps

Source: Company, Kotak Institutional Equities

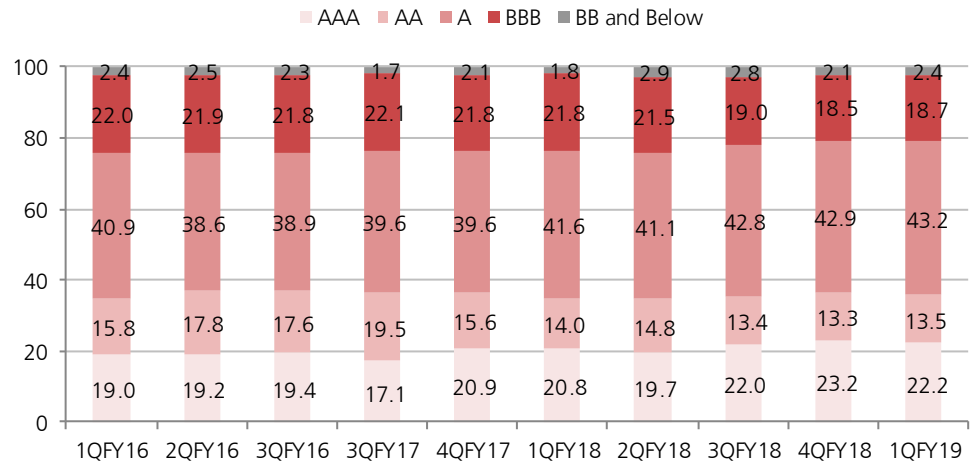
**Exhibit 6: Yes Bank has seen a qoq rise in exposure to telecom and iron and steel sectors**

Break-up of customer assets, March fiscal year-ends, 2013-1QFY19 (%)

	2013	2014	2015	2016	2017	2018	1QFY19
Electricity	3.0	4.8	8.3	8.7	11.3	9.2	9.3
Commercial real estate	-	0.0	0.0	6.8	5.8	5.9	5.8
Other real estate	-	0.0	0.0	0.9	0.8	0.5	0.4
Tech, ITES, Media	3.4	3.4	2.9	1.4	1.2	1.0	1.0
Food processing	4.6	4.4	3.2	2.7	2.4	2.4	2.4
Iron & Steel	5.7	3.5	3.3	2.2	1.8	2.0	2.6
Social & Commercial	2.1	1.8	2.7	2.4	2.7	2.5	2.4
Vehicles & equipments	2.4	2.8	3.1	2.5	2.4	2.8	2.8
Construction/ EPC	3.1	2.9	3.1	6.0	7.3	7.9	8.1
Other metal and metal	2.4	2.3	2.0	2.4	2.5	3.1	2.3
Telecom	2.4	3.1	2.2	4.5	4.9	2.2	3.6
Textiles	0.6	0.7	0.5	0.9	1.4	1.5	1.4
Aviation	0.3	0.3	0.2	0.6	1.0	0.8	0.9
Other industries	29.7	68.4	66.8	58.0	54.5	58.2	57.0

Source: Company, Kotak Institutional Equities

**Exhibit 7: Share of AA and above rated corporates has increased yoy**  
 Credit rating of corporate portfolio, March fiscal year-ends, 1QFY16-1QFY19 (%)



Source: Company, Kotak Institutional Equities

**Exhibit 8: Yes Bank - key financial growth rates and ratios**  
March fiscal year-ends, 2016-2021E (%)

	2016	2017	2018	2019E	2020E	2021E
<b>Growth rates (%)</b>						
Net loan	30.0	34.7	53.9	14.8	17.2	17.2
Net fixed assets	47.6	45.9	21.9	11.2	(1.2)	(1.0)
Cash and bank balance	8.8	137.9	26.6	12.9	22.1	4.3
Total Asset	21.4	30.1	45.3	16.4	18.7	17.4
Deposits	22.5	27.9	40.5	17.0	19.5	17.2
Current	28.5	74.6	51.1	21.1	23.5	21.0
Savings	62.3	60.6	35.3	25.0	27.1	24.2
Net interest income	30.9	29.4	30.9	22.5	16.0	24.1
Loan loss provisions	43.3	39.4	67.0	48.9	9.2	17.2
Total other income	32.5	51.1	29.0	8.5	11.9	15.1
Net fee income	24.4	30.2	31.4	13.5	8.5	14.6
Operating expenses	30.3	40.1	26.5	15.4	29.2	18.5
Employee expenses	32.4	41.9	21.4	12.5	11.4	9.2
<b>Key ratios (%)</b>						
Yield on average earning assets	9.6	9.3	8.1	9.0	9.0	9.0
Yield on average loans	11.2	10.7	9.2	10.2	10.1	10.1
Yield on average investments	7.6	7.7	7.0	7.7	7.8	7.9
Average cost of funds	6.9	6.5	5.5	6.5	6.4	6.3
Interest on deposits	7.1	6.4	5.5	6.3	6.2	5.9
Difference	2.8	2.7	2.7	2.5	2.5	2.7
Net interest income/earning assets	3.2	3.3	3.1	3.0	2.9	3.1
New provisions/average net loans	0.6	0.6	0.7	0.9	0.8	0.8
Interest income/total income	62.7	59.1	59.4	62.3	63.2	64.9
Other income / total income	37.3	40.9	40.6	37.7	36.8	35.1
Fee income to total income	33.8	32.0	32.3	31.4	29.7	28.2
Operating expenses/total income	40.9	41.7	40.5	40.0	45.2	44.3
Tax rate	32.6	34.0	31.8	32.3	32.8	33.3
Dividend payout ratio	16.6	14.0	13.0	16.6	16.6	16.6
Share of deposits						
Current	9.8	13.3	14.4	14.9	15.4	15.9
Savings	18.3	22.9	22.1	23.6	25.1	26.6
Loans-to-deposit ratio	87.9	92.6	101.4	99.4	97.5	97.5
Equity/assets (EoY)	8.3	10.2	8.2	8.1	7.7	7.6
<b>Dupont analysis (%)</b>						
Net interest income	3.0	3.1	2.9	2.8	2.8	2.9
Loan loss provisions	0.4	0.4	0.5	0.5	0.5	0.5
Net other income	1.8	2.2	2.0	1.7	1.6	1.6
Operating expenses	2.0	2.2	2.0	1.8	2.0	2.0
(1- tax rate)	67.4	66.0	68.2	67.7	67.2	66.7
ROA	1.7	1.8	1.6	1.4	1.3	1.3
Average assets/average equity	11.8	10.6	11.0	12.3	12.7	13.1
ROE	19.9	18.6	17.7	16.6	15.9	17.2

Source: Company, Kotak Institutional Equities estimates

Exhibit 9: Yes Bank - key financials  
March fiscal year-ends, 2016-2021E (Rs mn)

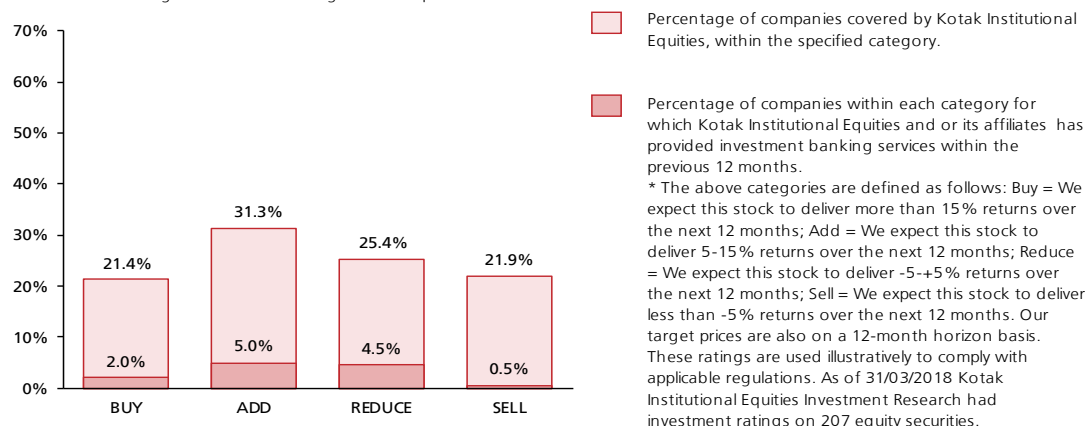
	2016	2017	2018	2019E	2020E	2021E
<b>Income statement (Rs mn)</b>						
Total interest income	135,334	165,374	202,686	288,683	338,423	400,426
Loans	97,115	123,225	154,778	221,935	256,852	300,394
Investments	35,082	37,968	41,025	58,597	72,410	89,470
Cash and deposits	3,138	4,180	6,882	8,152	9,161	10,563
Total interest expense	89,667	106,273	125,294	193,890	228,474	263,993
Deposits from customers	71,784	82,040	93,825	136,539	159,470	180,017
Net interest income	45,667	59,100	77,392	94,793	109,949	136,433
Loan loss provisions	5,361	7,474	12,480	18,577	20,290	23,777
Net interest income (after prov.)	40,307	51,627	64,912	76,216	89,659	112,656
Other income	27,121	40,969	52,829	57,310	64,121	73,799
Net fee income	24,592	32,009	42,071	47,741	51,784	59,328
Net capital gains	2,606	7,113	5,135	2,500	3,500	3,500
Net exchange gains	(176)	1,019	2,136	2,670	3,337	4,171
Operating expenses	29,764	41,686	52,735	60,845	78,631	93,162
Employee expenses	12,968	18,402	22,347	25,140	28,000	30,563
Depreciation on investments	25	522	2,599	4,500	-	-
Other Provisions	(23)	(54)	463	700	700	700
Pretax income	37,662	50,441	61,943	67,481	74,449	92,593
Tax provisions	12,268	17,140	19,697	21,796	24,419	30,833
Net Profit	25,394	33,301	42,246	45,685	50,030	61,760
% growth	26.6	31.1	26.9	8.1	9.5	23.4
Operating profit	40,419	51,270	72,351	88,758	91,939	113,570
% growth	27	24	31	14	9	26
Tax rate (%)	33	34	32	32	33	33
<b>Balance sheet (Rsmn)</b>						
Cash and bank balance	82,184	195,547	247,538	279,499	341,144	355,811
Cash	4,124	5,705	6,227	33,057	68,747	54,972
Balance with RBI	53,638	63,815	108,031	127,655	153,611	182,052
Balance with banks	556	667	976	976	976	976
Net value of investments	488,385	499,818	682,934	833,180	1,016,480	1,240,105
Govt. and other securities	351,863	354,805	488,861	607,229	752,384	930,327
Shares	628	2,369	644	644	644	644
Debentures and bonds	95,154	110,453	145,046	174,055	208,866	250,639
Net loans and advances	982,099	1,322,627	2,035,188	2,335,841	2,736,672	3,207,568
Fixed assets	4,707	6,868	8,373	9,312	9,198	9,110
Other assets	95,259	125,738	150,463	180,555	216,666	260,000
Total assets	1,652,634	2,150,597	3,124,497	3,638,387	4,320,160	5,072,593
Deposits	1,117,195	1,428,574	2,006,886	2,348,969	2,806,548	3,289,468
Borrowings and bills payable	319,759	391,992	758,087	886,962	1,064,355	1,277,225
Other liabilities	77,814	109,634	101,998	108,118	114,605	121,481
Total liabilities	1,514,768	1,930,201	2,866,971	3,344,049	3,985,508	4,688,175
Paid-up capital	4,205	4,565	4,606	4,606	4,606	4,606
Reserves & surplus	133,661	215,831	252,919	289,732	330,046	379,812
Total shareholders' equity	137,866	220,396	257,525	294,338	334,652	384,418

Source: Company, Kotak Institutional Equities estimates

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Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of June 30, 2018

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ADD. We expect this stock to deliver 5-15% returns over the next 12 months.

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SELL. We expect this stock to deliver <-5% returns over the next 12 months.

Our target prices are also on a 12-month horizon basis.

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