

Development Credit Bank

Recommendation	BUY
CMP (15/10/2012)	Rs. 46
Target Price	Rs. 65
Sector	Banking

Stock Details	
BSE Code	532772
NSE Code	DCB
Bloomberg Code	DEVB IN
Market Cap (Rs cr)	1,110
Free Float (%)	80.8%
52- wk HI/Lo (Rs)	63/31
Avg. volume BSE (Quarterly)	491,894
Face Value (Rs)	10.0
Dividend (FY 12)	0%
Shares o/s (Cr)	24.07

Relative Performance	1Mth	3Mth	1Yr
DCB	15.0%	1.6%	6.8%
Sensex	4.6%	8.4%	10.6%



Shareholding Pattern		30 th Sep 12
Promoters Holding		19.2%
Institutional (Incl. FII)		22.1%
Corporate Bodies		10.7%
Public & others		48.0%

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Results broadly in line with expectations

Development Credit Bank (DCB)'s results were broadly in line with estimates with PAT increasing by 66.4% YoY and 17% QoQ to Rs 22.1 cr. The improvement efforts of the bank are yielding results in the form of traction in the banks fee income and controlled credit cost. DCB's operational restructuring is expected to improve cost efficiency. We expect RoE and RoA for the bank to show a continuous improvement (RoE from 7.7% in FY12 to 11.3% in FY14E and RoA from 0.7% in FY12 to 1.0% in FY14E). *At current levels the stock is trading at attractive levels (PE of 11.94x and 9.7x of FY13E and FY14E EPS & at P/ABV of 1.19x and 1.06x of FY13E and FY14E respectively) and therefore we continue to maintain BUY rating on the stock. Our target price for the stock is Rs 65 based on P/ABV multiple of 1.5x on FY14E Adj book value of Rs.43.4 per share.*

➤ NIM's increase aided by lower cost of funds

Net Interest Margin (NIM) improved sequentially to 3.24% vs 3.18% in Q1FY13 as the cost of funds witnessed decline. Going forward, Management expects to witness improvement in NIMs driven by strong growth in advances towards the end of the quarter and declining cost of funds. We expect NIMs to improve to 3.3% for FY13E and 3.4% for FY14E.

➤ Non-interest income flattish on sequential basis

Non Interest Income was flat on sequential basis but increased YoY by 17.3% to Rs 27.5 crs. The bank is witnessing traction in its core fee income which increased both QoQ and YoY. However, lower treasury gains led to flattish growth on sequential basis. We expect non-interest income to grow 17.1% and 13.8% in FY13E and FY14E respectively.

➤ Improvement in cost to income ratio

The cost to income ratio of the bank stood at 71.9% as compared to 74.6% in Q2FY12 and 72.8% in Q1FY13. We expect cost to income ratio to come down to 68.5% in FY13E and 65.3% in FY14E driven by cost efficiencies.

➤ Asset quality continues to show improvement

The asset quality showed a significant improvement with Gross NPA in absolute terms declining by 13.3% YoY and 4.3% QoQ. Gross NPA ratio and Net NPA ratio were at 3.86% and 0.68% respectively in Q2FY13. Fresh slippages stood at Rs 11 cr vs Rs 20 cr in Q1FY13. The slippages during the quarter pertain to 4 accounts in the SME and MSME loan book. Going forward, the bank does not expect any major stress on its asset quality in its retail and SME book. We expect the bank's GNPA's to come down to 3.7% in FY13E and 3.23% in FY14E.

➤ Loan book grows both sequentially and YoY

DCB reported growth both on QoQ and YoY basis (+ 31.4% YoY and 4.1% QoQ) at Rs 5,671 cr driven by all the segment of the banks be it corporate banking, mortgage and SME book. The bank has recently forayed in gold loan portfolio which constituted 1% of the loan book. Management has mentioned that the pipeline for the SME book continues to remain strong. We have factored in 23.0% growth in advances in FY13E and 21.9% growth in FY14E.

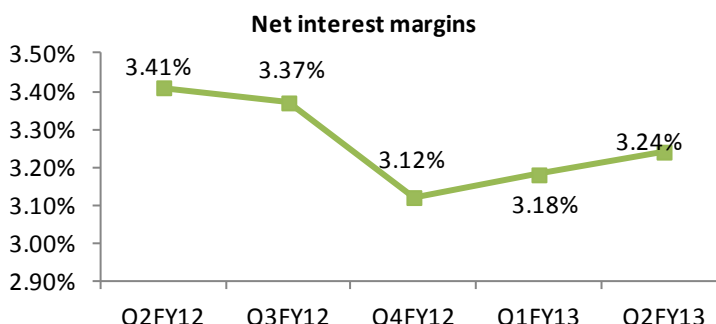
Year	NII (Rs cr)	Growth (%)	PBP (Rs cr)	Margin (%)	PAT (Rs cr)	EPS (Rs)	PE (x)	Adj BVPS (Rs)	P/ABV (x)	RoE (%)
FY11A	189	33.6%	86	13.3%	21	1.07	43.10	26.8	1.72	3.9%
FY12A	228	20.4%	84	10.2%	55	2.62	17.57	34.9	1.32	7.7%
FY13E	284	24.6%	127	13.1%	93	3.85	11.94	38.7	1.19	10.2%
FY14E	327	15.4%	160	14.9%	114	4.74	9.70	43.4	1.06	11.3%

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NIM's increase aided by lower cost of funds

Net Interest Income increased by 4.7% on QoQ basis and 13.3% YoY to Rs 67 crs in Q2FY13. Net Interest Margin (NIM) of the bank stood at 3.24% in Q2FY13 as compared to 3.18% in Q1FY13 and 3.41% in Q2FY12. NIMs witnessed an improvement sequentially as the cost of funds witnessed decline from 7.8% in Q1FY13 to 7.74% in Q2FY13.

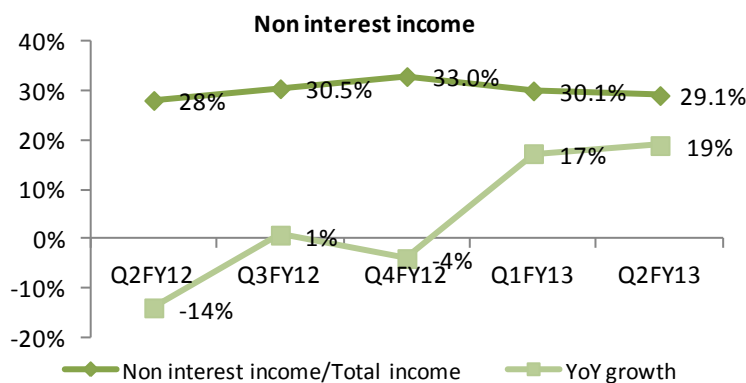
Going forward, Management stated that the strong growth in advances towards the end of Q2FY13 and lower cost of funds will help in improving the NIMs. However, maintaining a cautious stance Management expects that NIMs will be broadly in the range of 300-325 bps for FY13E. We expect NIMs to improve to 3.3% for FY13E and 3.4% for FY14E.



Source: Company data, Nirmal Bang Research

Non-interest income flattish on sequential basis

Non Interest Income was flat on sequential basis but increased YoY by 17.3% to Rs 27.5 crs. The bank's core fee income increased 27.7% YoY but increased 7.4% QoQ to Rs 21.7 cr. Treasury gains declined both YoY and QoQ during the quarter. The share of non interest income as % of total income declined from 30.1% in Q1FY13 to 29.1% in Q2FY13. However, on YoY basis the share improved. We expect non-interest income to grow 17.1% and 13.8% in FY13E and FY14E respectively.

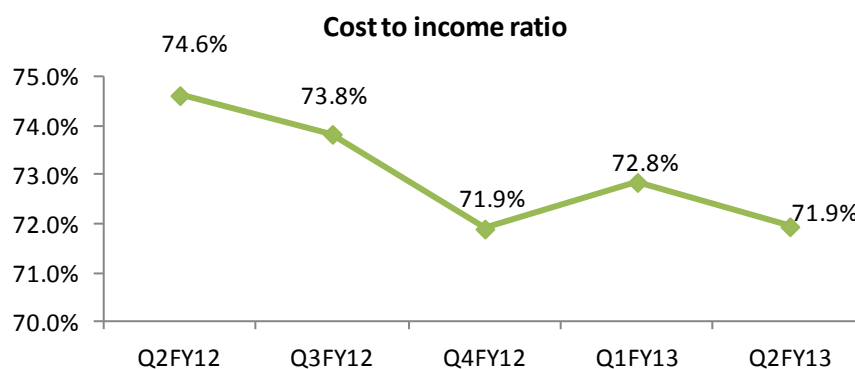


Source: Company data, Nirmal Bang Research

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Improvement in cost to income ratio

The bank's employee expenses increased 3.5% QoQ and 8.0% YoY in Q2FY13 to Rs 34.1 cr. Other expenses were higher 13.3% YoY however was flat on QoQ basis. The cost to income ratio of the bank stood at 71.9% as compared to 74.6% in Q2FY12 and 72.8% in Q1FY13. Management targets to increase the branch network to ~100 by FY13E from 87 branches currently. Management expects to bring down the cost to income ratio to sub 70% in FY13E and further below 60% in next 2-3 years driven by the expansion in business and cost efficiencies. We expect cost to income ratio to come down to 68.5% in FY13E and 65.3% in FY14E.

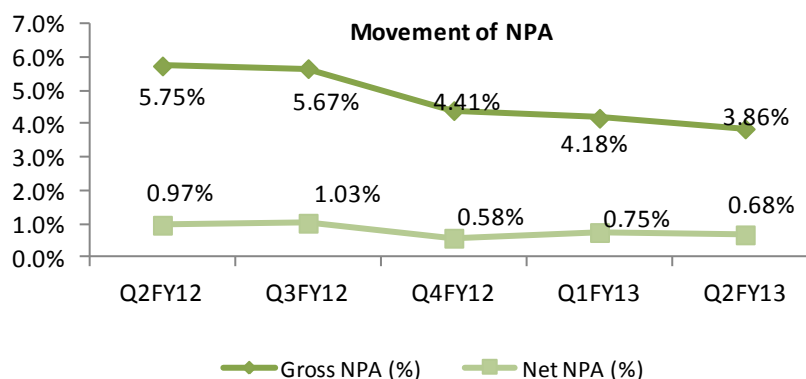


Source: Company data, Nirmal Bang Research

Asset quality continues to show improvement

The asset quality of the bank showed a significant improvement with Gross NPA in absolute terms declining by 13.3% YoY and 4.3% QoQ. Gross NPA ratio and Net NPA ratio were at 3.86% and 0.68% respectively in Q2FY13. Fresh slippages during the quarter stood at Rs 11 crs vs Rs 20 cr of slippage in Q1FY13. The slippages pertain to 4 accounts in the SME and MSME loan book. Going forward, the bank does not expect any major stress on its asset quality in its retail and SME book.

The provision coverage ratio improved to 89.25% in Q2FY13 as against 87.89% in Q2FY12. We expect the bank's Gross NPAs to come down to 3.85% in FY13E and 3.46% in FY14E.



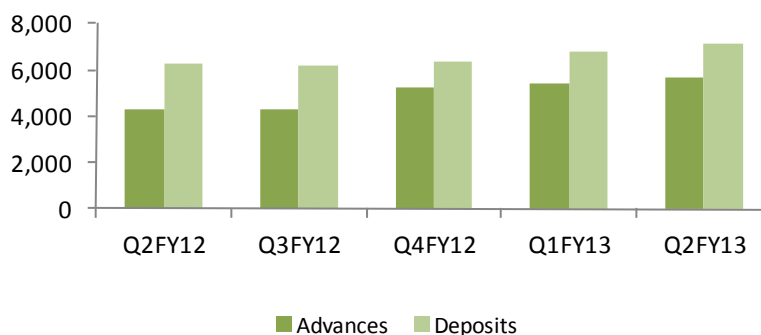
Source: Company data, Nirmal Bang Research

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Loan book grows both sequentially and YoY

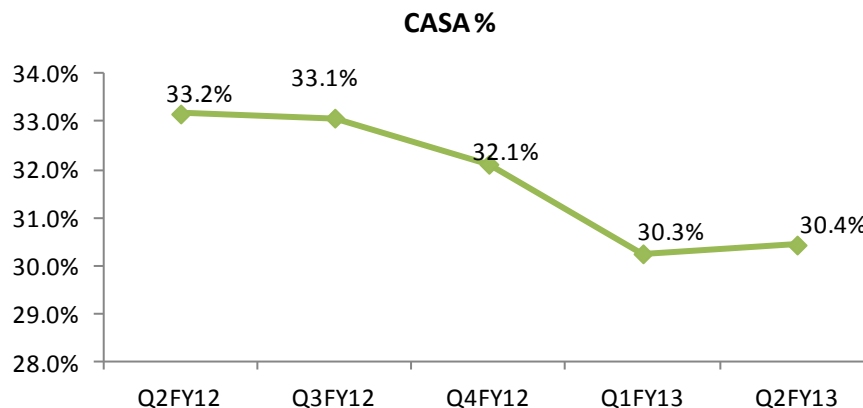
DCB reported growth both on QoQ and YoY basis (+ 31.4% YoY and 4.1% QoQ) at Rs 5,671 cr. The growth came across all the segments; corporate banking segment (3.95% QoQ and 37.9% YoY), bank’s mortgage book (+8.9% QoQ and 27.9% YoY). Bank’s SME and micro SME segment increased 7.1% QoQ and 37.2% YoY. Management has mentioned that the pipeline for the SME book continues to remain strong. Apart from entering into CV financing DCB has also forayed in Gold loan portfolio. The gold loan contributed around 1% of the total loan book and the book size stands lower than Rs 100 cr. Management targets loan book to grow at 25% for FY13E. We have factored in 23.0% growth in advances in FY13E and 21.9% growth in FY14E.

Deposits grew at 14.0% on YoY and 4.5% on QoQ basis. Credit to deposit ratio stood at 79.8% in Q2FY13. Borrowings continued to decline on QoQ basis resulting from the growth in deposits. Borrowing declined 12.9% QoQ (up 4.0% YoY) while Investments declined 0.2% QoQ (down 4.7% QoQ). NRI deposits stands at around 5% of the total deposits and bank intends to focus more on increasing the NRI deposits.



Source: Company data, Nirmal Bang Research

The bank’s CASA ratio witnessed marginal improvement on QoQ basis after declining for 5 consecutive quarters and stood at 30.4% in Q2FY13. However, on YoY basis CASA declined. The proportion of Retail deposits declined to 83.2% as compared to 80.8% in Q2FY12. Despite this, Management expects to maintain the CASA ratio above 30%. We expect CASA ratio to remain flat at 31.0% for FY13E and 31.4% for FY14E.



Source: Company data, Nirmal Bang Research

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Income Statement (Rs cr)	Q2FY13	Q2FY12	YoY (%)	Q1FY13	QoQ (%)
Interest Earned	219.9	178.5	23.2%	213.5	3.0%
Interest Expended	153.0	119.4	28.1%	149.6	2.3%
Net Interest Income	67.0	59.1	13.3%	63.9	4.7%
Other Income	27.5	23.1	19.0%	27.5	0.1%
Total Income	94.5	82.2	14.9%	91.4	3.3%
Payment to employees	34.1	31.5	8.0%	32.9	3.5%
Other operating expenses	33.9	29.8	13.7%	33.7	0.6%
Total operating expenses	68.0	61.4	10.8%	66.6	2.0%
Profit before provisioning	26.5	20.9	27.0%	24.8	6.8%
Provisions	4.4	7.5	(42.1%)	5.9	(26.2%)
Profit before tax	22.1	13.3	66.1%	18.9	17.1%
Tax	0.0	0.0	N/A	0.0	N/A
Profit after tax	22.1	13.3	66.1%	18.9	17.1%
No of shares	24.1	20.0	N/A	24.1	N/A
EPS	0.9	0.7	38.2%	0.8	17.1%

Source: Company data, Nirmal Bang Research

- Net Profit has shown a growth of 66.1% YoY at Rs 22.1 cr as compared to Rs 13.3 cr in Q2FY12 mainly due to 42.1% YoY decline in provisioning expense at Rs 4.4 crs vs 7.5 crs and no tax expense during the quarter.
- EPS for Q2FY13 stood at Rs 0.9 vs Rs 0.7 in Q2FY12.
- Capital Adequacy Ratio stood at 13.97% as on June 2012 of which Tier I Ratio stood at 12.71%.
- There won't be any tax liability for the bank in FY13E and FY14E as the bank has unabsorbed losses. We have not assumed the same in our estimates for FY13E and FY14E.

Valuation and Recommendation

The improvement efforts of the bank are showing results in the form of traction in the banks overall profitability driven by NII, fee income and controlled credit cost (expected range 0.5% for FY13E). We believe that the bank will thrive on improvement efforts over the next couple of years. Moreover, DCB's operational restructuring is expected to improve cost efficiency. We expect RoE and RoA for the bank to show a continuous improvement (RoE from 7.7% in FY12 to 11.3% in FY14E and RoA from 0.7% in FY12 to 1.0% in FY14E).

We believe that at current levels the stock is trading at attractive levels and therefore we continue to maintain BUY rating on the stock. Our target price for the stock is Rs 65 based on P/ABV multiple of 1.5x on its FY14E adjusted book value of Rs.43.4 per share.

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Financials

Profitability (Rs. Crs)	FY11	FY12	FY13E	FY14E	Balance Sheet (Rs. Crs)	FY11	FY12	FY13E	FY14E
Interest earned	536	717	847	940	Deposits	5,610	6,336	7,604	9,254
Interest expended	347	489	563	612	(of which CASA)	(1,976)	(2,035)	(2,357)	(2,906)
Net interest income	189	228	284	327	Borrowings	861	1,123	1,171	1,351
Non interest income	112	101	118	134	Other liab and prov	280	356	392	431
Total income	301	329	402	462	Total liabilities	6,751	7,815	9,167	11,036
Operating expenses	215	245	275	302	Equity capital	200	241	241	241
Staff costs	106	125	140	151	Reserves and surplus	419	618	711	825
Other Op Exp	109	120	136	151	Net worth	619	859	951	1,065
Profit before prov	86	84	127	160	Total liab and equity	7,372	8,677	10,121	12,105
Provisions	57	29	34	46	Cash and bank bal	487	457	601	882
Profit before tax	29	55	93	114	Investments	2,295	2,518	2,579	2,837
Taxes	8	0	0	0	Advances	4,271	5,284	6,502	7,925
Net profit	21	55	93	114	Fixed assets	128	185	194	204
Quarterly (Rs. Crs)	Dec.11	Mar.12	Jun.12	Sep.12	Other assets	191	233	245	257
Net interest income	59.7	57.1	63.9	67.0	Total assets	7,372	8,677	10,121	12,105
Non interest income	26	28	28	28					
Total income	86	85	91	94	Key Ratios	FY11	FY12	FY13E	FY14E
Operating expenses	63	61	67	68	Yield Ratios				
Operating profit	22	24	25	27	Avg Yield on Assets	8.4%	9.7%	9.7%	9.7%
Provisions	6.9	6.6	5.9	4.4	Yield on Advances	10.4%	11.2%	11.1%	11.0%
Profit before tax	16	17	19	22	Yield on Investments	6.1%	7.2%	7.2%	7.0%
Taxes	0	0	0	0	Cost of Int Bearing Liab	5.9%	7.0%	6.9%	6.6%
Net profit	16	17	19	22	Cost of Deposits	5.5%	6.7%	6.6%	6.3%
Profitability Ratios	FY11	FY12	FY13E	FY14E	Net Interest Spread	2.5%	2.7%	2.8%	3.0%
Cost / Income Ratio	71.4%	70.7%	68.5%	65.3%	NIM	3.1%	3.2%	3.3%	3.4%
Net profit margin	7.1%	16.8%	23.1%	24.7%	Balance Sheet Ratios				
RONW	3.9%	7.7%	10.2%	11.3%	Gross NPA	5.73%	4.40%	3.70%	3.23%
Growth Ratios	FY11	FY12	FY13E	FY14E	Net NPA	1.05%	0.57%	0.54%	0.47%
Advances growth	23.5%	23.7%	23.0%	21.9%	Return on Assets	0.3%	0.7%	1.0%	1.0%
Deposit growth	17.2%	12.9%	20.0%	21.7%	CASA	35.2%	32.1%	31.0%	31.4%
NII growth	33.6%	20.4%	24.6%	15.4%	Loan-deposit ratio	76.1%	83.4%	85.5%	85.6%
PAT growth	N/A	157.4%	68.4%	23.1%	CAR	13.3%	15.4%	13.6%	12.8%
Pre prov profit growth	78.2%	-2.6%	51.1%	26.5%	Dividend yield	0.0%	0.0%	0.0%	0.0%
Non interest inc growth	4.2%	-10.0%	17.1%	13.8%					
Ratios	FY11	FY12	FY13E	FY14E	Valuation Ratios	FY11	FY12	FY13E	FY14E
P/BV	1.63	1.29	1.16	1.04	EPS	1.07	2.62	3.85	4.74
P/ABV	1.72	1.32	1.19	1.06	BVPS	28.2	35.8	39.7	44.4
P/E	43.10	17.57	11.94	9.70	Adjusted BVPS	26.8	34.9	38.7	43.4

Source: Company data, Nirmal Bang Research

NOTES

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