

Banking on Banks? Better Go Private

Although valuations and stock prices are high, experts recommend parking your funds in private sector banks due to lower NPAs, better market share, quality of management, transparency and openness, says **Prashant Mahesh**

PSU bank stocks are down and out. The State Bank of India has plunged to ₹1,741 from ₹2,051, Canara Bank has fallen to ₹245 from ₹371, and Bank of India has tumbled to ₹205 from ₹289 in a span of a year. Many PSU banks are trading below their book value. Bank of India trades at a P/BV of 0.54, while Canara Bank trades at a P/BV of 0.48. SBI is trading at a P/BV of 1.31. Despite these beaten down valuations, there are no takers for these stocks.

Banking analysts continue to prefer private sector banks like ICICI Bank, HDFC Bank, Kotak Mahindra Bank and Axis Bank, among others, despite a spurt in stock prices and rise in valuations. Stocks of HDFC Bank has moved up to ₹750 from ₹610, Kotak Bank to ₹765 from ₹631 and ICICI Bank to ₹1,250 from ₹1,012. HDFC Bank trades at a Price to Book value (P/BV) of 4.9, while ICICI trades at a P/BV of 2.1.

Analysts justify their preference for private banks by citing a host of parameters: lower NPAs, gain in market share, better disclosures and continuity in top management, and so on. "Private banks are preferred due to their high quality portfolio, aggressive management, higher transparency and focus on the retail segment," says Sadanand Shetty, senior VP and fund manager, Taurus Mutual Fund. Others also point towards the deteriorating financial health of state-owned banks.

"Due to rising bad debt, public sector banks will remain dependent on the government for capital infusion. This will dilute the book value and lead to lower re-

turns in the long run," says Dipen Shah, head (PCG Research), Kotak Securities.

Way Ahead of Competition

In the last two decade, private sector banks — ICICI Bank, HDFC Bank, Yes Bank, Axis Bank and so on — have been gaining market share at the expense of state-owned banks. For example, they have increased their current account savings account (CASA) market share to 17% in 2013 from 14% in 2009. "The focus on retail segment has helped new private sector banks in the last five years when the economy passed through a slowdown," says Alpesh Mehta, banking analyst, Motilal Oswal Securities. However, public sector banks continued to focus on the corporate loan segment in this period, which proved to be a bad

Focus on retail has helped new private banks in the last five years when the economy slowed down

strategy. "With consumption pattern changing further in favour of discretionary spending, good growth is likely in consumer loans namely home loans, auto loans and credit cards," says Mehta. With private sector banks eyeing growth in semi-urban and rural areas, they are likely to further eat into the existing market share of state-owned banks, say analysts.

Quality of management and higher disclosures are other favourable factors attracting investors towards private sector banks. "PSU bank chiefs see frequent changes, giving them very little time to execute. As compared to this, private sector banks have seen

Stocks to Bank on

	CMP (₹)	Price to Book Value
ICICI Bank	1,257	2.1
HDFC Bank	746	4.9
Axis Bank	1,430	2.03
Kotak Mahindra Bank	771	3.59
IndusInd Bank	490	3.45
Yes Bank	379	2.35

Source: ETIG

CMP: Current Market Price



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Vikas Gupta
Exec VP, Arthaveda Fund Management

higher management continuity," says Alok Ranjan, portfolio manager, Way2Wealth. For example, Aditya Puri and team has been leading HDFC Bank for the last 20 years. Ranjan asks investors to bet on HDFC Bank, Yes Bank and ICICI Bank with two to three year horizon. Private banks also score big on transparency. "Private banks are more transparent and open than public sector banks," says Sadanand Shetty.

NPAs Continue to Drag PSU Banks

According to RBI data, net Non Performing Assets (NPAs) of public sector banks rose to 2.02% in 2012-13 from 1.53% in the previous year. Net NPAs of private sector banks rose marginally to 0.45% from 0.42% during the same period. Public sector banks have resorted to restructuring of loans to avoid bad

debt. Restructured accounts have grown at a compound annual growth rate of 47.86% in public sector banks, compared to 8.12% for private sector banks. "Many PSU banks have poor credit appraisal systems and they have restructured loans. All these will lead to a further rise in NPAs," says Vikas Gupta, executive vice president, Arthaveda Fund Management. To tackle higher NPAs, banks may need higher capital, which the government may have to provide them. "Due to higher NPAs, PSU banks will depend on the government for incremental capital infusion, which will lower returns and further dilute the book value," says Shah. His top picks in the space are ICICI Bank, followed by HDFC Bank.

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