

April 28, 2008

**India**  
**India Banks**

## Indian Overseas Bank (IOBK.IN - INR 144.10) 1-Overweight

Operating Results

Srikanth Vadlamani  
91.22.4037.4191  
svadlama@lehman.com  
LBSPL, India

Deepak Reddy  
91.22.4037.4190  
dereddy@lehman.com  
LBSPL, India

**In-line performance; Maintain 1-OW**

### Investment Conclusion

- IOB's reported 4QFY08 NII was in line with our estimates. Though MTM losses were substantial, earnings were above our estimates on account of surprise in other income – primarily recoveries and trading gains. We maintain our 1-OW rating on favourable risk reward.

### Summary

- NII of INR6.8 bn was in line with our expectation.
- Other income came in at INR3.5 bn vis-à-vis our estimate of INR1.2 bn. The surprise was due to the INR1.1 bn of recoveries and INR1.3 bn of trading gains booked this quarter.
- Asset quality has clearly seen some signs of deterioration with net inc NPA of 1.1%, but we believe that the extent of deterioration is lower than that indicated by headline numbers, given the high amount of recoveries.
- As expected, MTM losses were substantial at INR2.2 bn, which were booked under the provisioning line. The bank was affected by the high AFS proportion of 33% and the increase of G-sec yields by 30bp during the quarter.
- With the bank's profitability among the highest in the sector, we believe current valuations at 1.4x FY09E BV are not demanding. We maintain our 1-OW rating.

### Stock Rating

New: 1-Overweight  
Old: 1-Overweight

### Target Price

New: INR 200.00  
Old: INR 200.00

**Sector View:** 1-Positive

FY Mar	2007A	2008E		2009E		2010E	
		Actual	Old	New	Old	New	Old
Currency INR							
Adjusted Net Profit	10084.0	12312.0	12312.0	14615.0	14615.0	17463.0	17463.0
Adjusted EPS	15.3	21.7	21.7	26.8	26.8	32.1	32.1
Adjusted PE Ratio	9.4	6.6	6.6	5.4	5.4	4.5	4.5
BVPS	68.5	85.0	85.0	105.0	105.0	130.0	130.0
P/BV	2.1	1.7	1.7	1.4	1.4	1.1	1.1
ROE	23.3	26.5	26.5	26.5	26.5	25.9	25.9
Dividend Yield	N/A	N/A	N/A	N/A	N/A	N/A	N/A

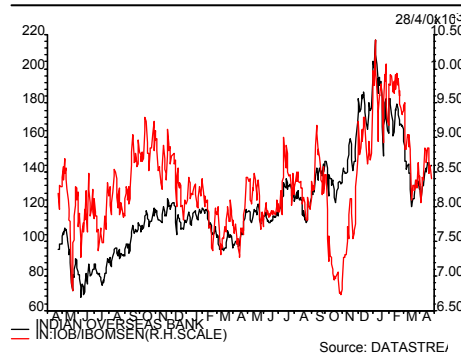
### Market Data

Market Cap (mn)	78505.7
Shares Outstanding (mn)	544.8
Free float (%)	N/A
Trading Volume	15100.0
Convertible	0
Share per ADR	N/A

### Financial Summary

Net Interest Margin	3.4
Net NPL/Loans	0.6
PL provisions/Loans	0.4
Tier 1 ratio	8.6

### Stock Overview



Reuters IOBK.IN  
Bloomberg IOB IN  
ADR

Performance	1M	3M	12M
Absolute %	7.1	-20.1	26.9
Rel. Market %	-0.4	-13.4	0.1
Rel. Sector %	-	-	-

52 Week Range 216.80 - 110.10

Figure 1: 4QFY08 results

(INR mn)	4QFY07	3QFY08	4QFY08	4QFY08E	YoY (%)	QoQ (%)
Net interest income	7,682	6,560	6,823	6,882	-11	4
Non-interest income	1,905	2,195	3,521	1,121	85	60
Operating income	9,587	8,755	10,344	8,003	8	18
Operating expenses	(3,970)	(3,824)	(3,929)	(4,065)	-1	3
Operating profit	5,617	4,931	6,415	3,938	14	30
Provision charges	(1,820)	(367)	(2,398)	(1,084)	32	554
Net profit	2,898	3,082	3,060	2,115	6	-1

Source: Company data, Lehman Brothers estimates

**Lehman Brothers does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report.**

Investors should consider this report as only a single factor in making their investment decision.

This research report has been prepared in whole or in part by research analysts that are not registered/qualified as research analysts with FINRA.

**PLEASE SEE ANALYST(S) CERTIFICATION(S) ON PAGE 3 AND IMPORTANT DISCLOSURES INCLUDING FOREIGN AFFILIATE DISCLOSURES BEGINNING ON PAGE 5**

**4QFY08 results – Key highlights**

**NII in line with our expectation**

IOB reported net interest income (NII) of INR6.8 billion (a 13% YoY decline on a high base), in line with our expectation. Loan growth continued to be strong and at 27% YoY, it is among the highest in the sector. Margins at 3.3% were broadly flat QoQ. While lending yields were down 40bp QoQ, NII was driven by the 116% incremental C/D ratio.

**Significant recoveries and trading gains boost non-interest income**

Other income came in at INR3.5 billion vis-à-vis our estimate of INR1.2 billion. The surprise was on account of significant recoveries from written-off accounts amounting to INR1.1 billion and also due to INR1.3 billion of trading gains.

**Higher provisions on substantial MTM losses**

As expected, the mark-to-market (MTM) losses on the government securities (G-sec) portfolio were substantial on account of the high proportion of AFS portfolio (about 33%). The bank's trading strategy may have taken a hit due to the adverse movement in yields, which were up about 30bp from December 2007 to March 2008. The bank booked INR2.2 billion of MTM losses on the provisioning line.

**Signs of deterioration in asset quality, but cushion from high recoveries**

The bank reported net incremental NPA of 1.1% in 4Q [1Q (0.4%), 2Q (-0.5%), and 3Q (0.4%)]. While this is clearly a deterioration vis-à-vis the trend seen so far, we highlight that there have been substantial recoveries from written-off accounts as well. Hence, the extent of deterioration is not as material as indicated by the headline numbers, in our view.

**Adjusting BV for the AS15 transitional liability deduction; we maintain our 1-Overweight rating**

The bank has deducted an amount of INR1.28 billion (net of deferred tax, charged through P&L) from revenue reserves to fund the transitional liability on short-term employee benefits under AS15. The pension gap funding continues to be routed through the P&L. Adjusting for this the revised BV per share now stands at INR102 and INR127 for FY09E and FY10E, respectively, compared with the earlier INR105 and INR130.

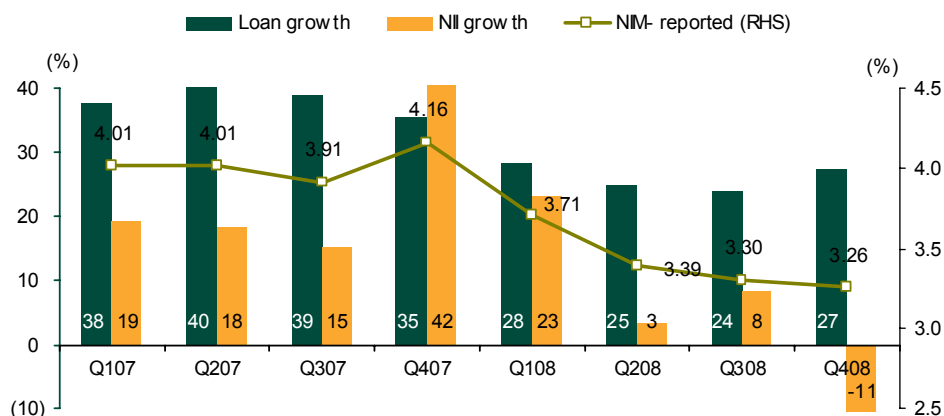
The stock is currently trading at 1.4x FY09E BV and 5.5x FY09E earnings. With the bank delivering profitability among the highest in the sector, we believe current valuations are not demanding. We maintain our 1-Overweight rating on the stock.

Figure 2: 4QFY08 results

(INR mn)	4QFY07	3QFY08	4QFY08	4QFY08E	YoY (%)	QoQ (%)
Net interest income	7,682	6,560	6,823	6,882	-11	4
Non-interest income	1,905	2,195	3,521	1,121	85	60
Operating income	9,587	8,755	10,344	8,003	8	18
Operating expenses	(3,970)	(3,824)	(3,929)	(4,065)	-1	3
Operating profit	5,617	4,931	6,415	3,938	14	30
Provision charges	(1,820)	(367)	(2,398)	(1,084)	32	554
Profit before tax	3,797	4,564	4,017	2,854	6	-12
Tax provided	(900)	(1,482)	(957)	(740)	6	-35
Tax rate	24%	32%	24%	26%		
Net profit	2,898	3,082	3,060	2,115	6	-1
Advances	479,227	546,215	610,576	588,254	27	12

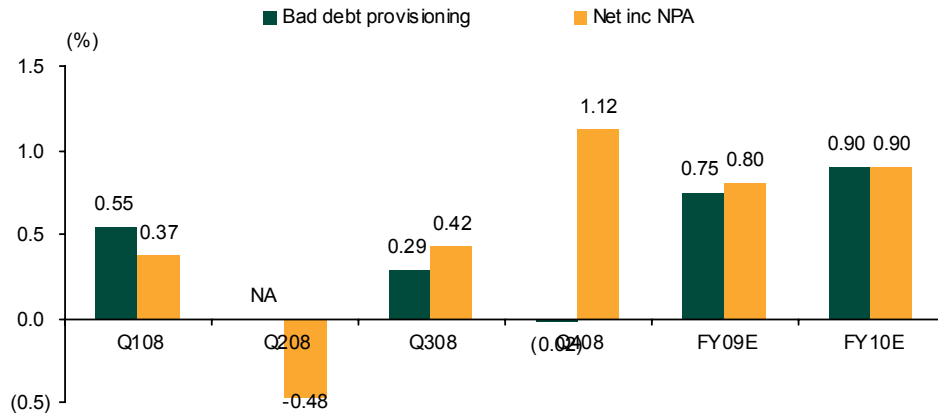
Source: Company data, Lehman Brothers estimates

Figure 3: Loan growth, NII growth and margins



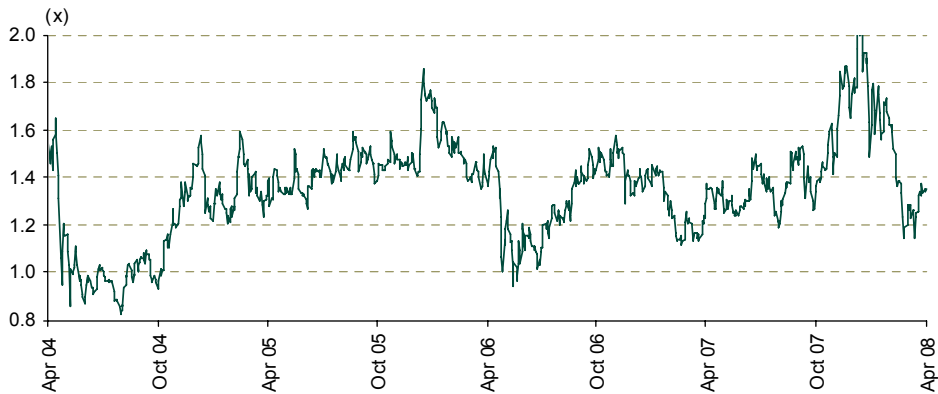
Source: Company data, Lehman Brothers research

Figure 4: Asset quality trend and provisioning estimates



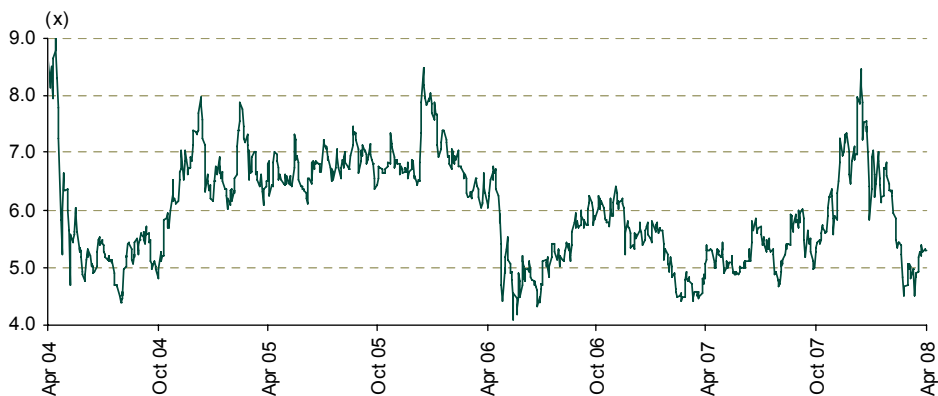
Source: Company data, Lehman Brothers estimates

Figure 5: One-year forward P/BV



Source: Lehman Brothers research

Figure 6: One-year forward P/E



Source: Lehman Brothers research

**Analyst Certification:**

We, Srikanth Vadlamani and Deepak Reddy, hereby certify (1) that the views expressed in this research Company Note accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Company Note and (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Company Note.



Important Disclosures:

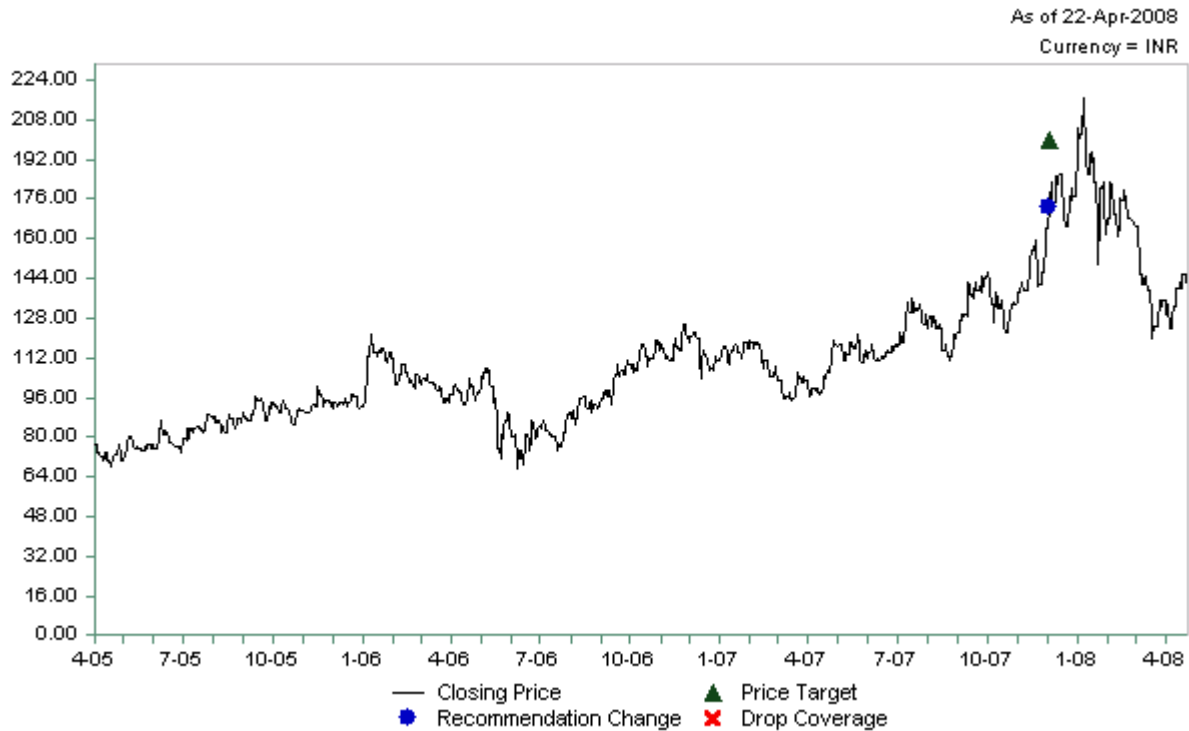
Indian Overseas Bank (IOBK.IN)

INR 144.10 (25-Apr-2008)

1-Overweight / 1-Positive

Rating and Price Target Chart:

### INDIAN OVERSEAS BANK



Currency=INR

Date	Closing Price	Rating	Price Target
03-Dec-07	172.15		200.00

Date	Closing Price	Rating	Price Target
03-Dec-07	172.15	1-Overweight	

FOR EXPLANATIONS OF RATINGS REFER TO THE STOCK RATING KEYS LOCATED ON THE PAGE FOLLOWING THE LAST PRICE CHART.

Lehman Brothers Inc. and/or its affiliates beneficially owns 1% or more of any class of common equity securities of Indian Overseas Bank as of the end of last month.

Lehman Brothers Inc. and/or an affiliate trade regularly in the shares of Indian Overseas Bank.

**Valuation Methodology:** We value IOB using a 'three-stage dividend discount model', with explicit forecasts up to FY10E, intermediate growth from FY10E-FY28E and 5% terminal growth in earnings beyond that. We are building in a sustainable ROE of 15.5% and a 16% CAGR in the intermediate phase over FY10E-FY19E and 9% CAGR over FY19E-FY28E.

**Risks Which May Impede the Achievement of the Price Target:** Asset quality - A spike in incremental bad debts

Till date the asset quality of the bank has been robust but do note that there is a risk of higher NPA incidence given the high yielding lending portfolio. A higher than expect rise in bad debt incidence is a key risk.

**Important Disclosures Continued:**

The analysts responsible for preparing this report have received compensation based upon various factors including the firm's total revenues, a portion of which is generated by investment banking activities

With the exception of analysts who publish for either LBI or a branch of LBI, research analysts may not be associated persons of the member and therefore may not be subject to Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account.

Company Name	Ticker	Price (25-Apr-2008)	Stock / Sector Rating
Indian Overseas Bank	IOBK.IN	INR 144.10	1-Overweight / 1-Positive

**Guide to Lehman Brothers Equity Research Rating System:**

Lehman Brothers coverage analysts in Asia (ex Japan) use a relative rating system in which they rate stocks as 1-Overweight, 2- Equal weight or 3-Underweight (see definitions below) relative to the country index of the country in which a stock is listed.

In addition to the stock rating, we provide sector views which rate the outlook for the sector coverage universe as 1-Positive, 2-Neutral or 3-Negative (see definitions below). A rating system using terms such as buy, hold and sell is not the equivalent of our rating system. Investors should carefully read the entire research report including the definitions of all ratings and not infer its contents from ratings alone.

**Stock Rating**

**1-Overweight** - The stock is expected to outperform the unweighted expected total return of the relevant country index over a 12-month investment horizon.

**2-Equal weight** - The stock is expected to perform in line with the unweighted expected total return of the relevant country index over a 12- month investment horizon.

**3-Underweight** - The stock is expected to underperform the unweighted expected total return of the relevant country index over a 12-month investment horizon.

**RS-Rating Suspended** - The rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Lehman Brothers is acting in an advisory capacity in a merger or strategic transaction involving the company.

**Sector View**

**1-Positive** - sector coverage universe fundamentals/valuations are improving.

**2-Neutral** - sector coverage universe fundamentals/valuations are steady, neither improving nor deteriorating.

**3-Negative** - sector coverage universe fundamentals/valuations are deteriorating.

**Distribution of Ratings:**

Lehman Brothers Equity Research has 2159 companies under coverage.

38% have been assigned a 1-Overweight rating which, for purposes of mandatory regulatory disclosures, is classified as Buy rating, 30% of companies with this rating are investment banking clients of the Firm.

46% have been assigned a 2-Equal weight rating which, for purposes of mandatory regulatory disclosures, is classified as Hold rating, 35% of companies with this rating are investment banking clients of the Firm.

11% have been assigned a 3-Underweight rating which, for purposes of mandatory regulatory disclosures, is classified as Sell rating, 22% of companies with this rating are investment banking clients of the Firm.

**Lehman Brothers Inc. and Its Foreign Affiliates Involved in the Production of Equity Research**

<p><b>New York</b> Lehman Brothers Inc. (LBI, New York) 745 Seventh Avenue New York , NY 10019 Member, FINRA</p>	<p><b>London</b> Lehman Brothers International (Europe) (LBIE, London) 25 Bank Street London, E14 5LE, United Kingdom Regulated by FSA</p>	<p><b>Tokyo</b> Lehman Brothers Japan Inc. (LBJ, Tokyo) Roppongi Hills Mori Tower, 31st Floor 6-10-1 Roppongi, Minato-ku, Tokyo 106-6131, Japan Regulated by FSA</p>
<p><b>Mumbai</b> Lehman Brothers Inc., India Branch (LBI, India) Winchester, Off High Street, 9th Floor Hiranandani Business Park, Powai, Mumbai 400 076, India</p>	<p><b>Seoul</b> Lehman Brothers International (Europe) Seoul Branch (LBIE, Seoul) Hanwha Building, 12th Floor 110, Sokong-dong Chung-Ku Seoul 100-755, Korea Regulated by FSC</p>	<p><b>Hong Kong</b> Lehman Brothers Asia Limited - Hong Kong (LBAL, Hong Kong) Two International Finance Centre 8 Finance Street, 26th Floor Central, Hong Kong Regulated by SFC</p>

Mumbai	Taipei	Sydney
Lehman Brothers Securities Private Limited (LBSP, India) Ceejay House, 11th Level, Plot F, Shivsagar Estate, Dr. Annie Besant Road, Worli, Mumbai 400018 Regulated by SEBI	Lehman Brothers Securities Taiwan Limited (LBSTL, Taiwan) Cathay Financial Center 12F 7 Sungren Road - Shin-Yi District Taipei, Taiwan Regulated by FSC	Lehman Brothers Australia Securities Pty Limited (LBAUL, Sydney) Level 33, 264 George Street Sydney NSW 2000, Australia Regulated by ASIC

This material has been prepared and/or issued by Lehman Brothers Inc., member SIPC, and/or one of its affiliates ("Lehman Brothers") and has been approved by Lehman Brothers International (Europe), authorized and regulated by the Financial Services Authority, in connection with its distribution in the European Economic Area. This material is distributed in Japan by Lehman Brothers Japan Inc., and in Hong Kong by Lehman Brothers Asia Limited. This material is distributed in Australia by Lehman Brothers Australia Securities Pty Limited, and in Singapore by Lehman Brothers Singapore Pte Ltd. Where this material is distributed by Lehman Brothers Singapore Pte Ltd, please note that it is intended for general circulation only and the recommendations contained herein does not take into account the specific investment objectives, financial situation or particular needs of any particular person. An investor should consult his Lehman Brothers' representative regarding the suitability of the product and take into account his specific investment objectives, financial situation or particular needs before he makes a commitment to purchase the investment product. This material is distributed in Korea by Lehman Brothers International (Europe) Seoul Branch, and in Taiwan by Lehman Brothers Securities Taiwan Limited. Where this material is distributed by Lehman Brothers Securities Taiwan Limited, please note that recommendations expressed herein are for reference only. Investors should carefully evaluate the investment risks and are reminded that they are solely responsible for their investment decisions. This document is for information purposes only and it should not be regarded as an offer to sell or as a solicitation of an offer to buy the securities or other instruments mentioned in it. No part of this document may be reproduced in any manner without the written permission of Lehman Brothers. With the exception of disclosures relating to Lehman Brothers, this research report is based on current public information that Lehman Brothers considers reliable, but we make no representation that it is accurate or complete, and it should not be relied on as such. In the case of any disclosure to the effect that Lehman Brothers Inc. or its affiliates beneficially own 1% or more of any class of common equity securities of the subject company, the computation of beneficial ownership of securities is based upon the methodology used to compute ownership under Section 13(d) of the United States' Securities Exchange Act of 1934. In the case of any disclosure to the effect that Lehman Brothers Inc. and/or its affiliates hold a short position of at least 1% of the outstanding share capital of a particular company, such disclosure relates solely to the ordinary share capital of the company. Accordingly, while such calculation represents Lehman Brothers' holdings net of any long position in the ordinary share capital of the company, such calculation excludes any rights or obligations that Lehman Brothers may otherwise have, or which may accrue in the future, with respect to such ordinary share capital. Similarly such calculation does not include any shares held or owned by Lehman Brothers where such shares are held under a wider agreement or arrangement (be it with a client or a counterparty) concerning the shares of such company (e.g. prime broking and/or stock lending activity). Any such disclosure represents the position of Lehman Brothers as of the last business day of the calendar month preceding the date of this report. This material is provided with the understanding that Lehman Brothers is not acting in a fiduciary capacity. Opinions expressed herein reflect the opinion of Lehman Brothers and are subject to change without notice. The products mentioned in this document may not be eligible for sale in some states or countries, and they may not be suitable for all types of investors. If an investor has any doubts about product suitability, he should consult his Lehman Brothers representative. The value of and the income produced by products may fluctuate, so that an investor may get back less than he invested. Value and income may be adversely affected by exchange rates, interest rates, or other factors. Past performance is not necessarily indicative of future results. If a product is income producing, part of the capital invested may be used to pay that income. © 2008 Lehman Brothers. All rights reserved. Additional information is available on request. Please contact a Lehman Brothers entity in your home jurisdiction.

Lehman Brothers policy for managing conflicts of interest in connection with investment research is available at [www.lehman.com/researchconflictspolicy](http://www.lehman.com/researchconflictspolicy). Complete disclosure information regarding companies covered by Lehman Brothers Equity Research, including ratings, earnings per share forecasts and price targets contained in reports covering U.S. companies is available at [www.lehman.com/disclosures](http://www.lehman.com/disclosures).