

South Indian Bank

BSE SENSEX	S&P CNX	Rs22	Buy							
19,008	5,697									
Bloomberg	SIB IN									
Equity Shares (m)	1,130.1									
52-Week Range	30/13									
1,6,12 Rel.Perf.(%)	-6/12/38									
M.Cap. (Rs b)	24.9									
M.Cap. (US\$ b)	0.5									
YEAR	NET INCOME	PAT	EPS	EPS	P/E	BY	P/BY	P/ABY	ROAA	ROAE
END	(RS M)	(RS M)	(RS)	GR. (%)	(X)	(RS)	(X)	(X)	(%)	(%)
3/10A	7,768	2,338	2.1	20.0	10.6	13.1	1.7	1.7	1.0	16.8
3/11E	9,635	2,765	2.4	18.3	9.0	15.0	1.5	1.5	1.0	17.4
3/12E	11,542	3,322	2.9	20.1	7.5	17.2	1.3	1.3	0.9	18.2
3/13E	13,765	4,002	3.5	20.5	6.2	19.9	1.1	1.1	0.9	19.1

South Indian Bank's reported net profit for 3QFY11 grew ~21% YoY to Rs754m (5% higher than our estimate). However, adjusting for the proportionate understatement of interest expenses in 3QFY10, net profit was up 62% YoY. Higher than expected non-interest income and lower employee cost resulted in higher than expected earnings. Key highlights are:

- Loan growth remained strong at 29% YoY and 6% QoQ (in line with the industry trend) to Rs192b. Deposits grew 31% YoY and 8% QoQ to Rs270b. CD ratio declined marginally to 71% v/s 72% a quarter ago.
- Reported NII grew 19% YoY to Rs2b (in line with our estimate). However, adjusting for the proportionate understatement of interest expenses last year, NII growth would have been higher at 39% YoY.
- For 9MFY11, NIM improved to 3% v/s 2.8% (adjusted) in 9MFY10 and declined marginally by 3bp in 3QFY11 compared to 1HFY11. Our calculations show that NIM for 3QFY11 declined by 8bp as compared with 2QFY11.
- In absolute terms, GNPA increased 11% QoQ. In percentage terms, GNPA was up 6bp QoQ to 1.3%. Slippages during the quarter amounted to Rs485m (one large account of Rs180m slipped during the quarter). With PCR remaining stable sequentially at ~71%, NNPA ratio remained stable at 0.4%.
- Provisions increased to Rs298m v/s Rs68m in 2QFY11 and Rs195m in 3QFY10. Higher provision towards NPA at Rs193m (on back of higher slippages) and increase in provision towards standard assets at Rs98m were the key reasons for the rise.
- SIB continues to have strong capitalization, with CAR at ~14.9% and tier-I CAR at ~12.3%.

Valuation and view: We expect SIB to report EPS of Rs2.4 and BV of Rs15 in FY11, and EPS of Rs2.9 and BV of Rs17.2 in FY12. We expect its RoA to sustain at 0.9-1% whereas increased leverage would help drive RoE to ~18% by FY12. The stock trades at 1.3x FY12E BV. Maintain **Buy** with a target price of Rs27 (1.6x FY12E BV).

QUARTERLY PERFORMANCE

									(RS MILLION)	
	FY10				FY11				FY10	FY11E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Interest Income	4,653	4,689	4,878	5,138	5,401	5,795	6,227	6,827	19,357	24,250
Interest Expense	3,128	3,037	3,160	4,349	3,728	3,822	4,179	4,735	13,674	16,463
Net Interest Income	1,524	1,652	1,718	789	1,674	1,973	2,048	2,092	5,683	7,786
% Change (Y-o-Y)	48.3	28.5	17.5	-46.7	9.8	19.4	19.2	165.2	8.7	37.0
Other Income	560	655	431	439	417	449	497	487	2,085	1,849
Net Income	2,084	2,307	2,149	1,227	2,090	2,422	2,545	2,578	7,768	9,635
% Change (Y-o-Y)	52.1	39.9	11.6	-36.2	0.3	5.0	18.4	110.1	13.0	24.0
Operating Expenses	1,015	968	967	711	1,046	1,174	1,116	1,153	3,662	4,489
Operating Profit	1,069	1,339	1,182	516	1,044	1,248	1,429	1,425	4,106	5,146
% Change (Y-o-Y)	54.1	44.0	18.0	-46.4	-2.3	-6.8	20.9	176.2	14.5	25.3
Other Provisions	104	165	195	-31	167	68	298	422	433	956
Profit Before Tax	965	1,174	987	547	877	1,180	1,130	1,003	3,673	4,190
Tax Provisions	364	448	363	161	293	410	377	345	1,336	1,425
Net Profit	601	726	625	386	584	770	754	657	2,338	2,765
% Change (Y-o-Y)	55.6	40.3	15.2	-23.2	-2.8	6.1	20.7	70.2	20.0	18.3
Interest Expense/Interest Income (%)	67.2	64.8	64.8	84.6	69.0	66.0	67.1	69.4	70.6	67.9
Other Income/Net Income (%)	26.9	28.4	20.1	35.7	19.9	18.5	19.5	18.9	26.8	19.2
Cost to Income Ratio (%)	48.7	42.0	45.0	58.0	50.1	48.5	43.9	44.7	47.1	46.6
Provisions/Operating Profits (%)	9.8	12.3	16.5	-6.0	16.0	5.5	20.9	29.6	10.5	18.6
Tax Rate (%)	37.7	38.2	36.7	29.4	33.4	34.7	33.3	34.4	36.4	34.0

E: MOSL Estimates

RESULTS ANALYSIS (RS M)

	3QFY11	3QFY10	YOY GR. %	2QFY11	QOQ GR. %	FY10	FY11E	FY12E
Interest Income	6,227	4,878	28	5,795	7	19,357	24,250	31,468
Interest Expense	4,179	3,160	32	3,822	9	13,674	16,463	22,095
Net Interest Income (NII)	2,048	1,718	19	1,973	4	5,683	7,786	9,373
Other Income	497	431	15	449	11	2,085	1,849	2,169
- Commission and Fees	352	283	25	340	4	1,100	1,336	1,603
- Forex Income	48	51	-7	46	3	204	188	216
- Trading Profits	97	97	0	62	56	780	325	350
Net Income	2,545	2,149	18	2,422	5	7,768	9,635	11,542
Total Operating Costs	1,116	967	15	1,174	-5	3,662	4,489	5,276
- Staff Costs	691	616	12	774	-11	2,263	2,853	3,313
- Other Opex	426	352	21	400	6	1,399	1,636	1,963
Operating Profit	1,429	1,182	21	1,248	14	4,106	5,146	6,266
Provisions	298	195	53	68	NA	433	956	1,232
PBT	1,130	987	14	1,180	-4	3,673	4,190	5,034
Tax	377	363	4	410	-8	1,336	1,425	1,711
Tax rate %	33	37		35		36	34	34
PAT	754	625	21	770	-2	2,338	2,765	3,322
Deposits	269,980	206,429	31	250,604	8	230,115	287,644	355,240
CASA Ratio %	22.4	24.2		23.9		23.1	22.5	21.7
Advances	191,880	148,674	29	180,290	6	158,229	200,951	251,189
Gross NPA	2,536	2,139	19	2,277	11	2,110	2,690	3,086
Gross NPA %	1.3	1.5		1.3		1.3	1.3	1.2
Net NPA	743	567	31	671	11	616	807	926
Net NPA %	0.4	0.4		0.4		0.4	0.4	0.4
Yields on Advances %*	10.7	11.4		10.6		11.0	10.7	11.2
Cost of Deposits %*	6.4	7.0		6.3		6.5	6.2	6.7
NIM %*	3.0	2.8		3.0		2.7	3.0	2.9
Branches	614	573		610		575	625	675

* Cumulative Reported, Calculated for full year nos

Business growth remains strong

Loans grew 29% YoY and 6% QoQ to Rs192b, while deposits grew 31% YoY and 8% QoQ to Rs270b. CD ratio declined marginally to 71% v/s 72% a quarter ago. A rising rate scenario resulted in CASA growth moderating to 21% YoY and flat QoQ. CASA ratio declined ~150bp QoQ to 22.4%. NRE deposits at the end of 3QFY11 were Rs37b.

9MFY11 margin firm

NII growth on a reported basis was up 19% YoY. However, but for the proportionate understatement of interest expenses in 3QFY10, NII growth would be higher at 39% YoY. For 9MFY11, NIM improved to 3% v/s 2.8% (adjusted) in 9MFY10 and declined marginally by 3bp in 3QFY11 compared to 1HFY11. Our calculations show that NIM for 3QFY11 declined by 8bp as compared with 2QFY11.

Yield on loans improved to 10.7% in 9MFY11 from 10.6% in 1HFY11 (11.4% in 9MFY10; down 70bp YoY). Yield on investments improved from 6.29% in 1HFY11 to 6.35% in 9MFY11. Cost of deposits increased by 6bp to 6.4% in 9MFY11 from 1HFY11. Higher cost of deposits was offset by higher yield on assets, leading to stable margin. Management has guided that margins would be maintained at 2.8-3% in FY11/12.

Fee income growth remains strong; C/I declines

Fee income (ex-forex) was up 25% YoY and ~4% QoQ to Rs352m. Income from forex was muted both on a QoQ and YoY basis. Treasury gains for the quarter were Rs97m (muted YoY) as against Rs62m a quarter ago. Opex increased 15% YoY but declined 5% QoQ, led by ~11% QoQ drop in employee cost.

Management has ascertained liability related towards gratuity and second pension option to be Rs1.5b at the end of 2QFY11, which it plans to amortize over a period of three years (subject to regulatory approvals). In 2QFY11, the bank provided for higher pension and gratuity related liability to cover the under-provisions of earlier quarters, resulting in higher employee expenses for the quarter. On the back of strong core operating profitability, core cost to income ratio declined to 45.6% in 3QFY11 v/s 49.7% in 2QFY11 and 47.1% in 3QFY10.

GNPA up 11% QoQ, led by one-off slippages

In absolute terms, GNPA increased 11% sequentially. In percentage terms, GNPA was up 6bp QoQ to 1.3%. Slippages during the quarter amounted to Rs485m (one large account of Rs180m slipped during the quarter), whereas recoveries and upgradations were at Rs227m. With PCR remaining stable sequentially at 71%, NNPA remained at 0.4%.

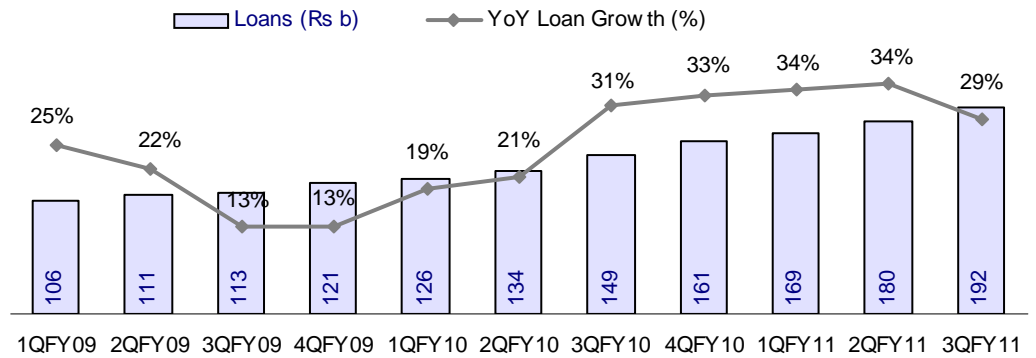
Provisions increased to Rs298m v/s Rs68m in 2QFY11 and Rs195m in 3QFY10. Higher provisions towards NPA at Rs193 (on back of higher slippages) and increase in provisions towards standard assets at Rs98m (~Rs60m was towards dual rate housing loans) were the key reasons for the rise.

Valuation and view

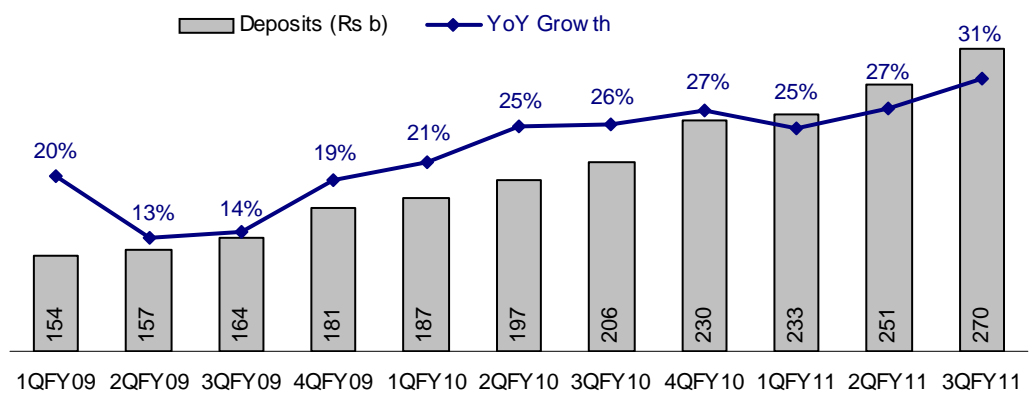
SIB has been growing at a healthy rate, with stable operating parameters. With increasing presence, healthy growth and robust asset quality, we believe the bank is well positioned to reap the benefits of strong economic growth.

We expect SIB to report EPS of Rs2.4 and BV of Rs15 in FY11, and EPS of Rs2.9 and BV of Rs17.2 in FY12. We expect its RoA to sustain at 0.9-1% whereas increased leverage would help drive RoE to ~18% by FY12. The stock trades at 1.3x FY12E BV. Maintain **Buy** with a target price of Rs27 (1.6x FY12E BV).

Strong loan growth

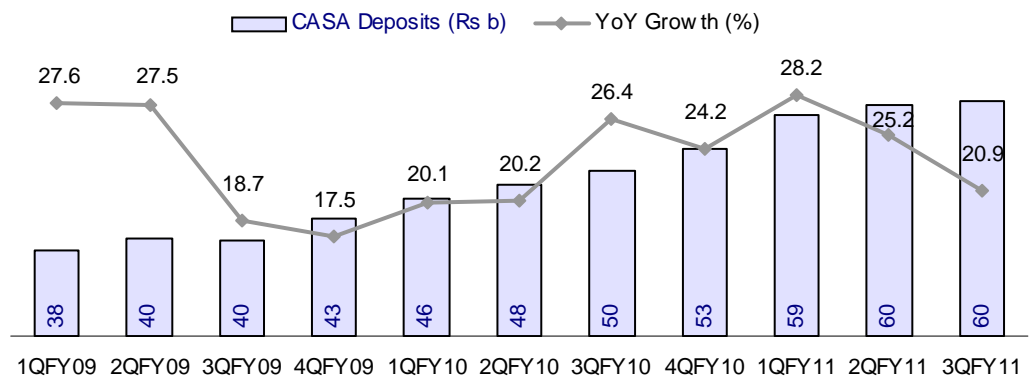


Trend in deposit growth



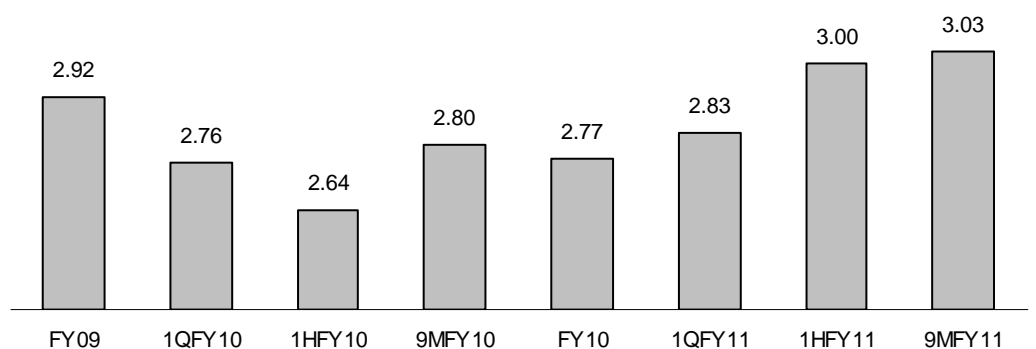
Increase in interest rates led to strong pick-up in deposits

CASA growth moderates



CASA ratio declined ~150bp QoQ, as CASA growth remained muted sequentially

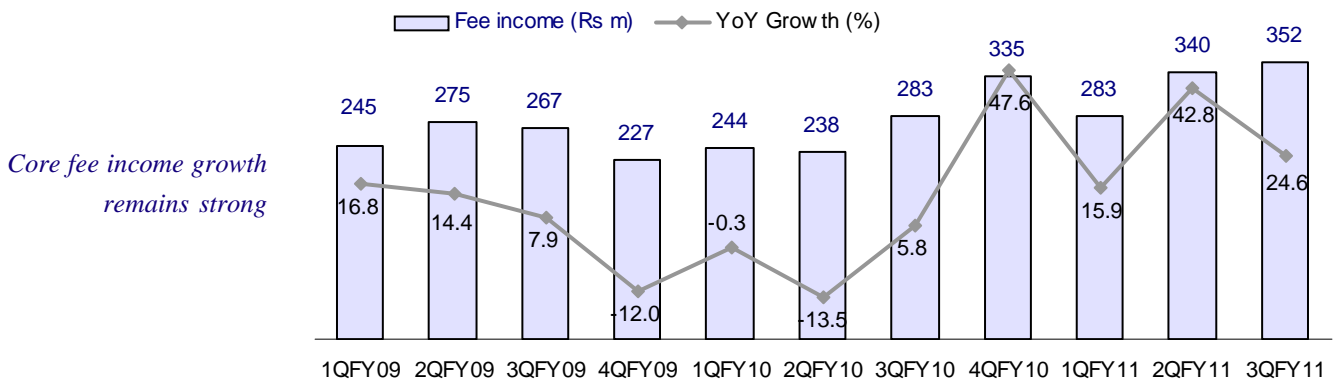
Trend in margins (%)



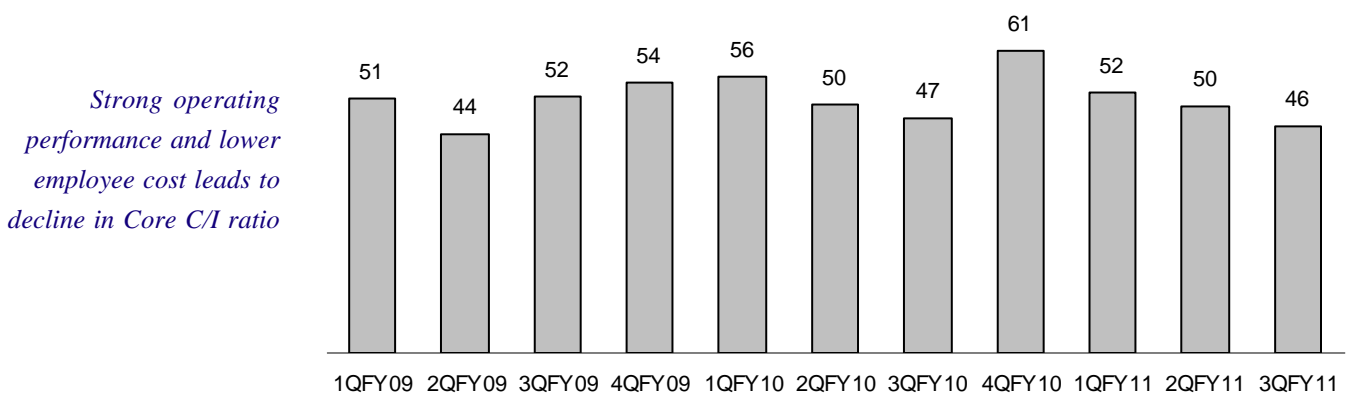
Higher cost of deposits was offset by higher yield on assets, leading to stable margins for 9MFY11; however, our calculations show that NIM for 3QFY11 declined marginally by 8bp QoQ

Source: Company/MOSL

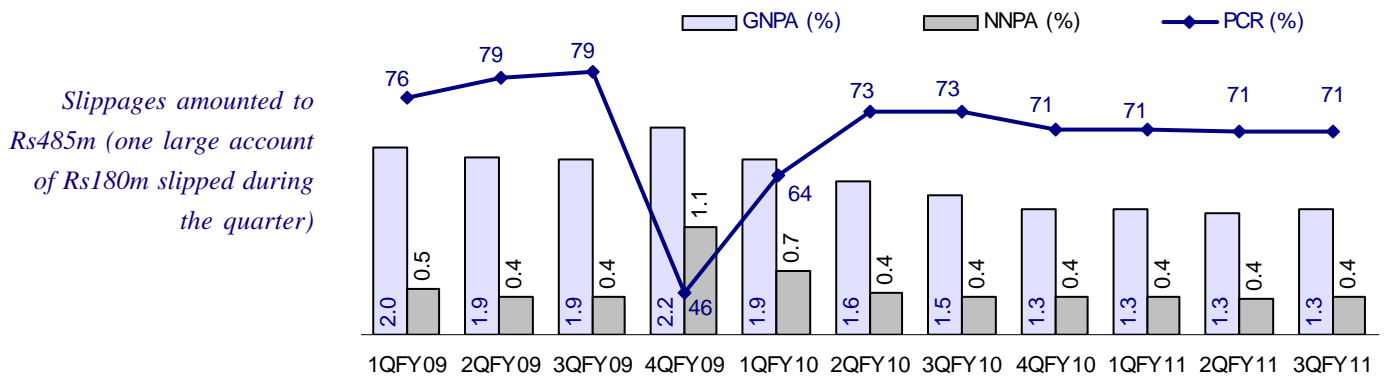
Trend in fee income



Core Cost/Income declines (%)



Asset quality stable QoQ



Source: Company/MOSL

South Indian Bank: an investment profile

Company description

South Indian Bank (SIB) is a private sector bank, with a strong presence in South India, particularly the state of Kerala (55% of total branches). It was the first among private sector banks in Kerala to become a scheduled bank in 1946 under the RBI Act. In 1964, the bank took over 12 banks, mostly in northern Kerala to increase its presence in the region. It has a network of 614 branches and 350+ ATMs, and total business of Rs462b.

Key investment arguments

- SIB has demonstrated consistent improvement in core operating performance over the last three years, with RoA expanding from 0.5% in FY06 to 1% in FY10.
- Asset quality has been stable (gross NPA of 1.3% and net NPA of 0.4%), with lowest restructuring (~2.6% of the loan book).
- High tier-1 ratio of ~12% can effectively be used for further leverage for dilution-free growth in coming years.

Key investment risks

- High dependence on southern states, particularly Kerala, increases the geographical risk.

Recent developments

- SIB's existing equity shares sub-divided into face value Re1 each as against Rs10 each.
- Mr Amitabha Guha has assumed office as Non-Executive Part-time Chairman from October 2010.

Valuation and view

- We expect SIB to report EPS of Rs2.4 and BV of Rs15 in FY11, and EPS of Rs2.9 and BV of Rs17.2 in FY12. We expect its RoA to sustain at 0.9-1% whereas increased leverage would help drive RoE to ~18% by FY12. The stock trades at 1.3x FY12E BV. Maintain **Buy** with a target price of Rs27 (1.6x FY12E BV).

Sector view

- Loan growth remains strong. However, rising inflation and increasing interest rates are the near-term headwinds for the sector.
- Our Economist expects current tightness in liquidity to start easing in 4QFY11, allaying the pressure of significant NIM compression.
- We believe that margins would start compressing, but gradually. With strong loan growth and high CD ratio, there is strong pricing power with banks.
- Banks with high CASA deposits and lower proportion of bulk deposits will be preferred bets.

Comparative valuations

		SIB	Fed.Bank	J&K
P/E (x)	FY11E	9.0	11.5	5.5
	FY12E	7.5	9.7	4.7
P/BV (x)	FY11E	1.5	1.3	1.0
	FY12E	1.3	1.1	0.9
RoE (%)	FY11E	17.4	11.5	20.2
	FY12E	18.2	12.3	20.2
RoA (%)	FY11E	1.0	1.2	1.4
	FY12E	0.9	1.2	1.4

Shareholding Pattern (%)

	Sep-10	Jun-10	Sep-09
Promoter	0.0	0.0	0.0
Domestic Inst	13.2	11.3	13.1
Foreign	37.6	40.3	37.1
Others	49.2	48.4	49.8

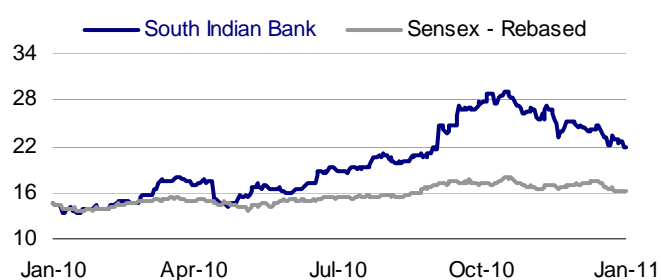
EPS: MOSL forecast v/s Consensus (Rs)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY11	2.4	2.5	-3.3
FY12	2.9	3.1	-5.5

Target Price and Recommendation

Current Price (Rs)	Target Price (Rs)	Upside (%)	Reco.
22	27	22.7	Buy

Stock performance (1 year)



Financials and Valuation

INCOME STATEMENT							(Rs Million)
Y/E MARCH	2008	2009	2010	2011E	2012E	2013E	
Interest Income	12,912	16,869	19,357	24,250	31,468	39,450	
Interest Expense	9,151	11,640	13,674	16,463	22,095	28,257	
Net Interest Income	3,761	5,229	5,683	7,786	9,373	11,193	
<i>Change (%)</i>	<i>7.7</i>	<i>39.0</i>	<i>8.7</i>	<i>37.0</i>	<i>20.4</i>	<i>19.4</i>	
Non Interest Income	1,426	1,643	2,085	1,849	2,169	2,572	
Net Income	5,187	6,872	7,768	9,635	11,542	13,765	
<i>Change (%)</i>	<i>15.8</i>	<i>32.5</i>	<i>13.0</i>	<i>24.0</i>	<i>19.8</i>	<i>19.3</i>	
Operating Expenses	2,481	3,285	3,662	4,489	5,276	6,102	
Pre Provision Profits	2,707	3,587	4,106	5,146	6,266	7,663	
<i>Change (%)</i>	<i>18.2</i>	<i>32.5</i>	<i>14.5</i>	<i>25.3</i>	<i>21.8</i>	<i>22.3</i>	
Provisions (excl tax)	389	573	433	956	1,232	1,599	
PBT	2,318	3,014	3,673	4,190	5,034	6,064	
Tax	801	1,066	1,336	1,425	1,711	2,062	
<i>Tax Rate (%)</i>	<i>34.6</i>	<i>35.4</i>	<i>36.4</i>	<i>34.0</i>	<i>34.0</i>	<i>34.0</i>	
PAT	1,516	1,948	2,338	2,765	3,322	4,002	
<i>Change (%)</i>	<i>86.5</i>	<i>28.4</i>	<i>20.0</i>	<i>18.3</i>	<i>20.1</i>	<i>20.5</i>	
Extra Ordinary Item	-27	0	0	0	0	0	
Profits Post EO	1,489	1,948	2,338	2,765	3,322	4,002	
<i>Change (%)</i>	<i>43.0</i>	<i>30.8</i>	<i>20.0</i>	<i>18.3</i>	<i>20.1</i>	<i>20.5</i>	
Equity Dividend (Incl tax)	317	397	529	663	797	960	
Core PPP*	2,391	3,233	3,326	4,821	5,916	7,263	
<i>Change (%)</i>	<i>8.6</i>	<i>35.2</i>	<i>2.9</i>	<i>45.0</i>	<i>22.7</i>	<i>22.8</i>	
<i>*Core PPP is (Nil+Fee income-Opex)</i>							
BALANCE SHEET							(Rs Million)
Y/E MARCH	2008	2009	2010	2011E	2012E	2013E	
Equity Share Capital	904	1,130	1,130	1,130	1,130	1,130	
Reserves & Surplus	10,706	11,910	13,723	15,825	18,350	21,393	
Net Worth	11,610	13,040	14,853	16,955	19,480	22,523	
Deposits	151,561	180,923	230,115	287,644	355,240	438,722	
<i>Change (%)</i>	<i>23.8</i>	<i>19.4</i>	<i>27.2</i>	<i>25.0</i>	<i>23.5</i>	<i>23.5</i>	
of which CASA Dep	36,488	43,052	53,233	64,685	77,004	91,694	
<i>Change (%)</i>	<i>24.5</i>	<i>18.0</i>	<i>23.6</i>	<i>21.5</i>	<i>19.0</i>	<i>19.1</i>	
Borrowings	1,826	4,120	3,310	3,902	4,655	5,534	
Other Liabilities & Prov.	5,902	5,711	7,063	8,570	10,250	11,908	
Total Liabilities	170,899	203,794	255,340	317,070	389,625	478,687	
Current Assets	17,026	20,359	19,877	25,432	31,324	40,222	
Investments	45,722	60,752	71,556	84,436	100,057	120,068	
<i>Change (%)</i>	<i>33.3</i>	<i>32.9</i>	<i>17.8</i>	<i>18.0</i>	<i>18.5</i>	<i>20.0</i>	
Loans	104,537	118,479	158,229	200,951	251,189	310,218	
<i>Change (%)</i>	<i>32.0</i>	<i>13.3</i>	<i>33.6</i>	<i>27.0</i>	<i>25.0</i>	<i>23.5</i>	
Fixed Assets	1,128	1,363	1,525	1,683	1,801	1,874	
Other Assets	2,486	2,841	4,153	4,568	5,254	6,304	
Total Assets	170,899	203,794	255,340	317,070	389,625	478,687	
ASSET QUALITY							
GNPA (Rs M)	1,885	2,606	2,110	2,690	3,086	3,746	
NNPA (Rs M)	340	1,343	616	807	926	1,124	
GNPA Ratio	1.78	2.18	1.32	1.33	1.22	1.20	
NNPA Ratio	0.32	1.13	0.39	0.40	0.37	0.36	
PCR (Excl Tech. write off)	82.0	48.5	70.8	70.0	70.0	70.0	
<i>E: MOSL Estimates</i>							

Financials and Valuation

RATIOS

Y/E MARCH	2008	2009	2010	2011E	2012E	2013E
Spreads Analysis (%)						
Avg. Yield-Earning Assets	9.1	9.7	9.1	9.2	9.7	9.9
Avg. Yield on loans	10.5	11.4	11.0	10.7	11.2	11.4
Avg. Yield on Investments	6.8	6.7	5.7	6.2	6.4	6.4
Avg. Cost-Int. Bear. Liab.	6.6	6.9	6.5	6.3	6.8	7.0
Avg. Cost of Deposits	6.5	6.8	6.5	6.2	6.7	6.9
Interest Spread	2.5	2.8	2.6	2.9	2.9	2.9
Net Interest Margin	2.7	3.0	2.7	3.0	2.9	2.8
Profitability Ratios (%)						
RoE	16.1	15.8	16.8	17.4	18.2	19.1
RoA	1.0	1.0	1.0	1.0	0.9	0.9
Int. Expense/Int. Income	70.9	69.0	70.6	67.9	70.2	71.6
Fee Income/Net Income	21.4	18.8	16.8	15.8	15.8	15.8
Non Int. Inc./Net Income	27.5	23.9	26.8	19.2	18.8	18.7
Efficiency Ratios (%)						
Cost/Income*	50.9	50.4	52.4	48.2	47.1	45.7
Empl. Cost/Op. Exps.	59.0	65.2	61.8	63.6	62.8	61.4
Busi. per Empl. (Rs m)	54.2	61.4	70.8	83.5	96.6	111.3
NP per Empl. (Rs lac)	3.5	4.3	4.8	5.3	5.9	6.6
* ex treasury						
Asset-Liability Profile (%)						
Loans/Deposit Ratio	69.0	65.5	68.8	69.9	70.7	70.7
CASA Ratio	24.1	23.8	23.1	22.5	21.7	20.9
Investment/Deposit Ratio	30.2	33.6	31.1	29.4	28.2	27.4
G-Sec/Investment Ratio	79.1	67.0	78.8	85.2	88.8	91.3
CAR	13.8	14.8	15.4	13.1	11.4	10.5
<i>Tier 1</i>	<i>12.1</i>	<i>13.2</i>	<i>12.4</i>	<i>10.9</i>	<i>9.6</i>	<i>9.1</i>
VALUATION						
Book Value (Rs)	12.8	11.5	13.1	15.0	17.2	19.9
<i>Change (%)</i>	<i>24.9</i>	<i>-10.1</i>	<i>13.9</i>	<i>14.2</i>	<i>14.9</i>	<i>15.6</i>
Price-BV (x)	1.7	1.9	1.7	1.5	1.3	1.1
Adjusted BV (Rs)	12.6	10.8	12.8	14.5	16.7	19.3
Price-ABV (x)	1.7	2.0	1.7	1.5	1.3	1.1
EPS (Rs)	1.6	1.7	2.1	2.4	2.9	3.5
<i>Change (%)</i>	<i>11.4</i>	<i>4.6</i>	<i>20.0</i>	<i>18.3</i>	<i>20.1</i>	<i>20.5</i>
Price-Earnings (x)	13.4	12.8	10.6	9.0	7.5	6.2
Dividend Per Share (Rs)	0.3	0.3	0.4	0.5	0.6	0.7
Dividend Yield (%)	1.4	1.4	1.8	2.3	2.7	3.3

E: MOSL Estimates

N O T E S



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Disclosure of Interest Statement

South Indian Bank

1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	Yes
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	Yes

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