

Bank of Baroda

STOCK INFO. BLOOMBERG
BSE Sensex: 11,503 BOB IN
REUTERS CODE
S&P CNX: 3,365 BOB.BO

22 August 2006

Previous Recommendation: Buy

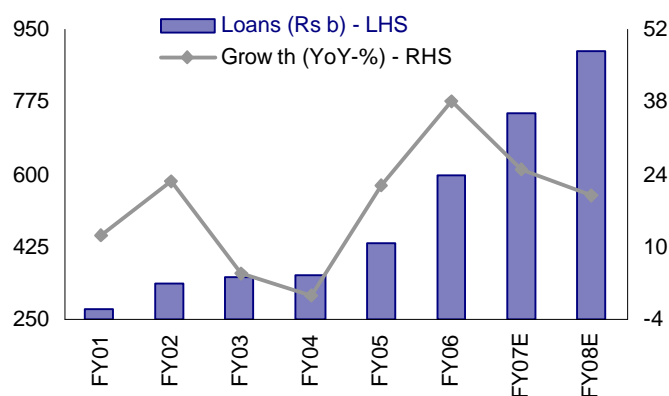
Buy

Rs237

We met the management of Bank of Baroda (BoB). Key takeaways from the meeting are:

Focusing on volume: Management guided for loan growth of over 30% in FY07. As BoB did not witness any increase in balance sheet size between FY02-04, management is planning a catch up now by growing loan book aggressively. A large part of this growth is likely to come from retail (17% of total loans and 20% of domestic loans, YoY growth of 57% in 1QFY07). BOB would also focus to grow their SME book faster, as this segment is better yielding than the corporate sector, even on a risk adjusted basis. In terms of deposits, we believe that BoB can fund a 30% loan growth with a 15%-16% in deposits as it has excess SLR on its book.

TREND IN LOAN AND GROWTH

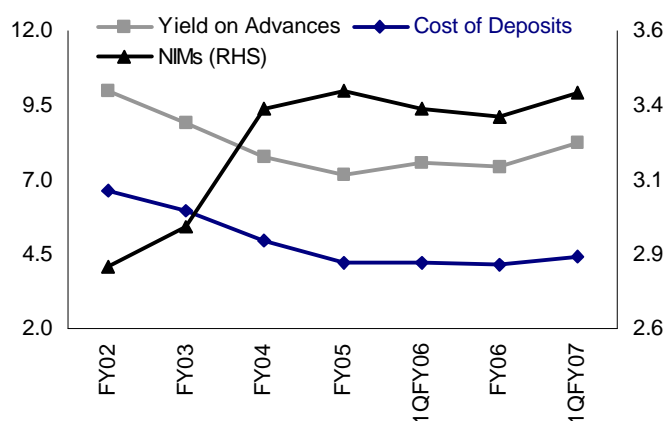


Source: Company/ Motilal Oswal Securities

NIMs to be stable: BoB has been most aggressive amongst the PSU banks in raising PLR (100bp hike in May and August). As a result, NIMs are up 5bp YoY in 1QFY07. The full impact of May PLR hike will be reflected in 2QFY07 and coupled with the recent increase in PLR, we

expect yield to improve resulting in better margins in 2QFY07. For FY07, we are assuming stable margins, as cost of funds will increase in 2HFY07 coupled with decline in investment yields.

MOVEMENT IN MARGINS (%)

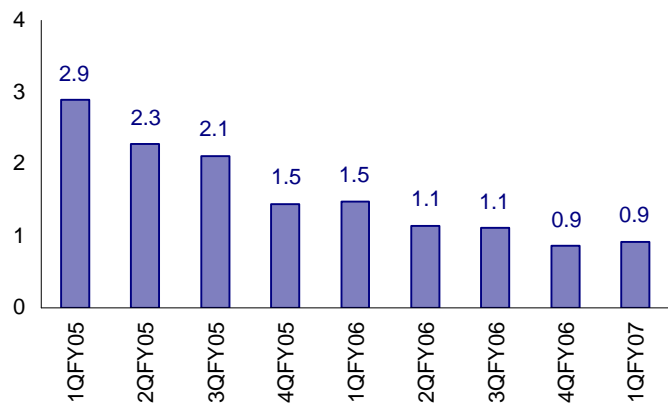


Source: Company/ Motilal Oswal Securities

Investment book - cushioned: BoB has transferred securities worth Rs50b to HTM in 1QFY07 and taken a hit of Rs0.9b. 76% of the SLR book of BoB is now in in HTM; modified duration of AFS portfolio has been reduced to 2.2 years and has a cushion up to a 10-year yield of 8.35%. The bank has excess SLR of 3.5% of NDTL.

Asset quality worsens 1QFY07; likely to improve: NPAs have increased as the bank has recognized a couple of big accounts as non-performing. Gross NPAs have risen 16bp to 4.06% QoQ, while net NPAs have increased by 5bp to 0.92%. Management has guided that, going forward; it does expect NPA levels to decline, as it expects strong recoveries and upgradations. Provision cover stands at comfortable 78%.

TREND IN NET NPAs (%)



Source: Company/ Motilal Oswal Securities

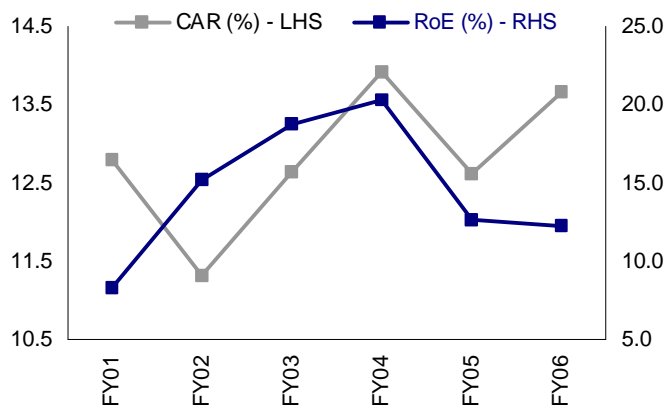
Slow in technology implementation: BoB is amongst the only large PSU bank which has been slow in implementing CBS. Only 500 branches of the 2,740 odd branches are under CBS, which the management stated that it would go up to 750 branches end-FY07.

New pension norms effect to be minimal: Only 40% of BoB’s employee base has opted for the pension scheme. As the bank has been providing for pension related expenses on actuarial basis management has stated that they expect minimal impact, on implementation of AS-15.

Highly capitalized leading to low RoEs: BoB’s Tier 1 CAR post-equity issuance is 11%. Management plans to raise additional Rs10b in perpetual debt to maintain CAR

above 12% (currently CAR is 12.4%). As the bank is highly capitalized, RoE is low at ~12-13%.

HIGH CAPITALIZATION LEADING TO LOW ROES



Source: Company/ Motilal Oswal Securities

Lower provisioning to drive earnings: During 1QFY07, the bank made high provisions (Rs3b, 55% of operating profit) for HTM transfer, MTM hit and NPAs (due to recognition of new NPAs). However, these is unlikely to recur in the following quarters which is likely to result in strong net earnings for the bank going forward.

Valuation and recommendation: Strong loan growth coupled with lower provisioning requirement going forward will drive a 20% CAGR in profit during FY06-08 period. Maintain **Buy** at 8.7x FY07E EPS and 1x FY07E BV.

INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Interest Income	61,471	64,314	71,000	86,227	101,594
Interest Expended	35,755	34,521	38,751	48,700	59,443
Net Int. Income	25,716	29,793	32,249	37,527	42,150
Change (%)	22.3	15.9	8.2	16.4	12.3
Other Income	17,190	13,048	11,916	10,677	11,424
Net Income	42,906	42,841	44,165	48,204	53,575
Change (%)	27.5	-0.2	3.1	9.1	11.1
Operating Expenses	18,053	19,822	23,848	26,236	28,968
Operating Income	24,853	23,019	20,318	21,967	24,607
Change (%)	44.8	-7.4	-11.7	8.1	12.0
Other Provisions	9,524	14,388	9,173	8,150	8,200
PBT	15,329	8,631	11,145	13,817	16,407
Tax	5,659	1,863	2,876	3,869	4,594
Tax Rate (%)	36.9	21.6	25.8	28.0	28.0
PAT	9,670	6,768	8,269	9,948	11,813
Change (%)	25.1	-30.0	22.2	20.3	18.7
Proposed Dividend	1,906	1,670	2,077	2,193	2,559

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Capital	2,945	2,945	3,655	3,655	3,655
Reserves & Surplus	48,364	53,332	74,789	82,544	91,798
Net Worth	51,309	56,278	78,444	86,200	95,454
Deposits	729,673	813,335	936,620	1,077,113	1,223,600
Change (%)	9.8	11.5	15.2	15.0	13.6
Borrowings	8,751	31,408	70,722	73,722	76,722
Other Liab. & Prov.	61,353	45,622	48,139	52,953	58,248
Total Liabilities	851,087	946,642	1,133,925	1,289,987	1,454,024
Current Assets	72,668	92,542	134,546	111,613	86,976
Investments	380,188	370,744	351,142	375,722	409,537
Change (%)	26.0	-2.5	-5.3	7.0	9.0
Advances	356,009	434,004	599,118	748,897	898,677
Change (%)	0.7	21.9	38.0	25.0	20.0
Net Fixed Assets	8,153	8,608	9,207	9,852	10,541
Other Assets	34,069	40,744	39,912	43,903	48,293
Total Assets	851,087	946,642	1,133,925	1,289,987	1,454,024

ASSUMPTIONS					
(%)					
Deposit Growth	9.8	11.5	15.2	15.0	13.6
Advances Growth	0.7	21.9	38.0	25.0	20.0
Investments Growth	26.0	-2.5	-5.3	7.0	9.0
Dividend	65.0	50.0	50.0	60.0	70.0
CRR	4.5	5.0	5.0	5.0	5.0

E: MOST Estimates

RATIOS					
Y/E MARCH	2004	2005	2006	2007E	2008E
Spreads Analysis (%)					
Avg. Yield-Earn. Asset	8.1	7.6	7.2	7.3	7.4
Avg. Cost-Int. Bear. L	5.1	4.4	4.2	4.5	4.9
Interest Spread	3.0	3.2	3.0	2.8	2.5
Net Interest Margin	3.4	3.5	3.3	3.2	3.1

Profitability Ratios (%)					
RoE	20.3	12.6	12.3	12.1	13.0
RoA	12	0.8	0.8	0.8	0.9
Int. Expended/Int. Earr	58.2	53.7	54.6	56.5	58.5
Other Inc./Net Income	40.1	30.5	27.0	22.1	21.3

Efficiency Ratios (%)					
Op. Exps./Net Income	42.1	46.3	54.0	54.4	54.1
Empl. Cost/Op. Exps.	69.4	69.7	63.9	62.9	61.1
Busi. per Empl. (Rs m)	27.3	316	35.9	45.2	55.2
NP per Empl. (Rs mln)	0.2	0.2	0.2	0.3	0.3

Asset-Liability Profile (%)					
Adv./Deposit Ratio	48.8	53.4	64.0	69.5	73.4
Invest./Deposit Ratio	52.1	45.6	37.5	34.9	33.5
G-Sec/Invest. Ratio	75.7	79.2	74.8	74.8	74.8
Gross NPAs to Adv.	10.3	7.2	3.9	3.4	3.0
Net NPAs to Adv.	2.9	1.4	0.9	0.6	0.5
CAR	13.9	12.6	13.3	12.3	11.7
Tier 1 (inc. IFR)	8.5	8.2	10.3	9.2	8.6

VALUATION					
Y/E MARCH	2004	2005	2006E	2007E	2008E
Book Value (Rs)	165.3	182.2	207.4	228.7	254.0
Price-BV (x)	14	13	11	10	0.9
Adjusted BV (Rs)	142.3	168.5	198.2	220.3	246.5
Price-ABV (x)	17	14	12	11	10
EPS (Rs)	32.8	23.0	22.6	27.2	32.3
EPS Growth (%)	25.1	-30.0	-16	20.3	18.7
Price-Earnings (x)	7.2	10.3	10.5	8.7	7.3
OPS (Rs)	84.4	78.2	55.6	60.1	67.3
OPS Growth (%)	44.7	-7.4	-28.9	8.1	12.0
Price-OP (x)	2.8	3.0	4.3	3.9	3.5

E: MOST Estimates



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Bank of Baroda

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

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