

## Bank of India

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

22 August 2006

*Previous Recommendation: Buy*
**Buy**
**Rs133**

We met the management of Bank of India (BoI). Key takeaways from the meeting are:

**Focusing on qualitative growth:** The bank aims to achieve a steady growth of 20%-25% in its loan book and 18%-20% in deposits. The bank has plans to focus on quality loans, with a focus on SME, agriculture and retail that can realize reasonable margins. Also, the bank does not intend to raise funds at a high cost to fund balance sheet growth. In FY06 and 1QFY07, BoI's loan and deposit growth has been below industry average (deposits grew by 19%, loans grew by 17% and 22%, respectively), as the bank focussed on margins as compared to volumes.

**Margins improve on back of PLR hike; endeavor to maintain margins:** Post the PLR hike in May, 50% of the loan book has been re-priced in 1QFY07, resulting in improved global spreads (up by 29bp YoY to 2.9%). Management has also stated that they would again be raising their PLR by at least 25bp in their forthcoming board meeting. We believe these two PLR hikes should result in improved yields on advances (1QFY07 at 8.15%) over the next few quarters. We also expect the bank to limit its rise in costs, as the bank has ~42% in CASA (for domestic deposits). Overall, management was confident of maintaining or improving (by ~10bp) upon their global spreads from 1QFY07 levels in FY07.

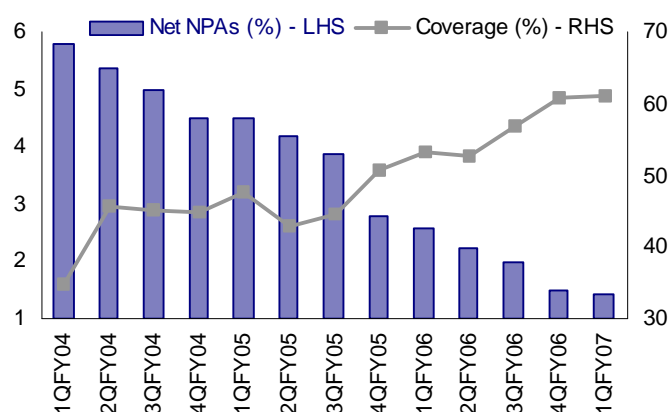
**SPREAD MOVEMENT (%)**

	1QFY07	1QFY06
<b>Global Spreads (%)</b>		
Yield on Advances	8.2	7.4
Yield on Investments	7.2	6.9
Yield on Funds	7.1	6.6
Cost of Deposits	4.3	4.0
Cost of Funds	4.2	3.9
<b>Global Spreads</b>	<b>2.9</b>	<b>2.6</b>
<b>Domestic Spread (%)</b>		
Yield on Funds	7.4	7.2
Cost of Funds	4.2	4.2
<b>Domestic Spreads</b>	<b>3.2</b>	<b>2.9</b>

Source: Company/ Motilal Oswal Securities

**Cost to Income ratio to decline post FY08:** Bank of India is probably the only bank which is expensing the costs related to its CBS resulting in higher C-I ratio and hence, does not expect its technology related costs to increase post FY08. By end-FY07, the bank is likely to have at least 1,000 branches under CBS (750 branches currently under CBS track 66% of the business), which would command 80% of the business. Further, as employee retirements are likely to be considerable, these expenses are also likely to grow marginally (5%-7%) from current levels.

**Provisions to decline, resulting in higher profitability growth:** BoI has been aggressively providing for NPAs in the last few years, which has also affected its profitability growth. BoI's asset quality has been improving steadily on back of higher provisions (net NPAs at 1.4% in 1QFY07). With net NPAs at 1.4% currently, we expect provisioning to slow down once the bank reaches net NPAs of below 1%. The management has indicated their objective to achieve net NPAs of below 1% by end-FY07, which in our view is likely to be very comfortable as large recoveries happen in the second half of the fiscal.

**NET NPAS (%)**


Source: Company/ Motilal Oswal Securities

**New pension norms effect to be minimal:** Only 15% of BoI'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, if any, is expected after the implementation of AS-15.

**Recap bonds to provide further liquidity:** BoI has Rs17b worth of recap bonds, which can not be treated as a part of SLR. As a result of which the bank will have additional cushion to grow its lending book without investing in SLR securities. On a rough estimate, BoI can grow its domestic loan book by 7-8% without making SLR investments.

**Will raise hybrid capital:** BoI's CAR is 10.4% while Tier 1 CAR is 6.65% in 1QFY07. The management has ruled out any equity (GoI holding of 69.5%) issuance in FY07. The bank is likely to raise US\$200m through hybrid instruments in October 2006 to shore up Tier 1 CAR.

**Valuation and recommendation:** BoI is likely to be a beneficiary of low operating expenses, steady NII growth and very low risk on AFS portfolio. We expect profit growth of 23% in FY07 and 21% in FY08. The stock trades at 7.5x FY07E EPS and 1.2x FY07E BV. Reiterate **Buy**.

INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Interest Income	57,959	60,315	70,287	85,500	101,738
Interest Expended	35,945	37,946	43,967	54,226	64,209
<b>Net Interest Income</b>	<b>22,014</b>	<b>22,369</b>	<b>26,320</b>	<b>31,275</b>	<b>37,528</b>
Change (%)	8.1	16	17.7	18.8	20.0
Other Income	17,920	11,560	11,844	11,545	11,960
<b>Net Income</b>	<b>39,934</b>	<b>33,929</b>	<b>38,164</b>	<b>42,820</b>	<b>49,489</b>
Change (%)	8.6	-15.0	2.5	12.2	15.6
Operating Expenses	17,515	19,323	21,151	24,494	28,161
<b>Operating Income</b>	<b>22,419</b>	<b>14,606</b>	<b>17,012</b>	<b>18,326</b>	<b>21,328</b>
Change (%)	10.4	-34.8	16.5	7.7	16.4
Other Provisions	8,910	9,993	7,859	6,800	6,800
<b>PBT</b>	<b>13,509</b>	<b>4,613</b>	<b>9,154</b>	<b>11,526</b>	<b>14,528</b>
Tax	3,426	1,210	2,142	2,881	3,995
Tax Rate (%)	25.4	26.2	23.4	25.0	27.5
<b>PAT</b>	<b>10,083</b>	<b>3,403</b>	<b>7,012</b>	<b>8,644</b>	<b>10,533</b>
Change (%)	18.5	-66.3	106.0	23.3	218
Proposed Dividend	1,650	976	1,660	1,953	2,441

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Capital	4,881	4,881	4,881	4,881	4,881
Reserves & Surplus	35,215	39,767	44,507	51,199	59,291
<b>Net Worth</b>	<b>40,097</b>	<b>44,649</b>	<b>49,389</b>	<b>56,081</b>	<b>64,173</b>
<b>Deposits</b>	<b>710,031</b>	<b>788,214</b>	<b>939,320</b>	<b>1,089,611</b>	<b>1,253,053</b>
Change (%)	10.8	11.0	19.2	16.0	15.0
Borrowings	63,808	79,605	88,425	110,531	123,795
Other Liabilities & Prov.	34,664	37,314	45,159	49,675	54,643
<b>Total Liabilities</b>	<b>848,600</b>	<b>949,782</b>	<b>1,122,293</b>	<b>1,305,898</b>	<b>1,495,663</b>
Current Assets	85,579	75,263	114,021	127,233	143,258
<b>Investments</b>	<b>271,629</b>	<b>286,863</b>	<b>317,818</b>	<b>368,668</b>	<b>423,969</b>
Change (%)	11.2	5.6	10.8	16.0	15.0
<b>Advances</b>	<b>458,559</b>	<b>555,289</b>	<b>651,727</b>	<b>769,038</b>	<b>884,394</b>
Change (%)	7.6	21.1	17.4	18.0	15.0
Net Fixed Assets	7,986	8,142	8,100	7,881	7,657
Other Assets	24,847	24,225	30,628	33,079	36,386
<b>Total Assets</b>	<b>848,600</b>	<b>949,782</b>	<b>1,122,293</b>	<b>1,305,899</b>	<b>1,495,664</b>

ASSUMPTIONS					
(%)					
Deposit Growth	10.8	11.0	19.2	16.0	15.0
Advances Growth	7.6	21.1	17.4	18.0	15.0
Investments Growth	11.2	5.6	10.8	16.0	15.0
Average PLR	10.0	10.0	10.0	10.0	10.0
Dividend	33.8	20.0	34.0	40.0	50.0
GRR	4.5	5.0	5.0	5.0	5.0

E: MOST Estimates

RATIOS					
Y/E MARCH	2004	2005	2006	2007E	2008E
<b>Spreads Analysis (%)</b>					
Avg. Yield-Earn. Asset:	7.5	7.0	7.0	7.3	7.5
Avg. Cost-Int. Bear. Li:	4.9	4.6	4.6	4.9	5.0
Interest Spread	2.5	2.4	2.4	2.4	2.5
Net Interest Margin	2.8	2.6	2.6	2.7	2.8

**Profitability Ratios (%)**

RoE	26.7	8.0	14.9	16.4	17.5
RoA	13	0.4	0.7	0.7	0.8
Int. Expended/Int. Earned	62.0	62.9	62.6	63.4	63.1
Other Inc./Net Income	44.9	34.1	31.0	27.0	24.2

**Efficiency Ratios (%)**

Op. Exps./Net Income	43.9	57.0	55.4	57.2	56.9
Empl. Cost/Op. Exps.	66.9	65.4	62.8	61.2	59.5
Busi. per Empl. (Rs m)	26.0	29.5	34.8	41.3	48.5
NP per Empl. (Rs lac)	2.3	0.8	1.7	2.1	2.6

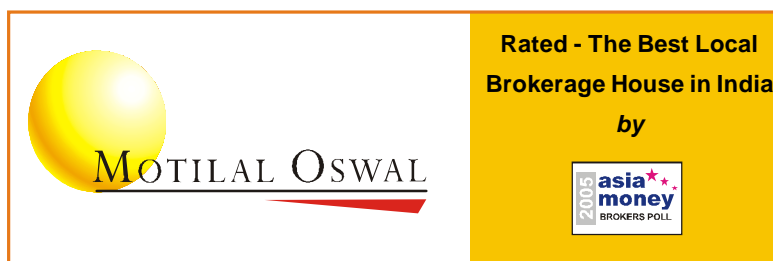
**Asset-Liability Profile (%)**

Adv./Deposit Ratio	64.6	70.4	69.4	70.6	70.6
Invest./Deposit Ratio	38.3	36.4	33.8	33.8	33.8
G-Sec/Invest. Ratio	67.9	69.6	71.6	64.8	59.1
Gross NPAs to Adv.	7.9	5.5	3.7	3.1	2.7
Net NPAs to Adv.	4.5	2.8	1.5	0.8	0.5
CAR	13.0	11.5	10.8	9.9	9.4
Tier 1	7.5	7.1	6.8	6.4	6.1

**VALUATION**

Book Value (Rs)	78.6	88.1	98.0	111.9	128.6
Price-BV (x)	17	15	14	12	10
Adjusted BV (Rs)	51.1	67.4	85.0	104	123
Price-ABV (x)	2.6	2.0	1.6	1.3	1.1
EPS (Rs)	20.7	7.0	14.4	17.7	21.6
EPS Growth (%)	18.5	-66.3	106.0	23.3	218
Price-Earnings (x)	6.4	19.0	9.2	7.5	6.2
OPS (Rs)	45.9	29.9	34.9	37.5	43.7
OPS Growth (%)	10.4	-34.8	16.5	7.7	16.4
Price-OP (x)	2.9	4.4	3.8	3.5	3.0

E: MOST Estimates



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**Bank of India**

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|---|----|
| 1. Analyst ownership of the stock                       | No |
| 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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