



## Oriental Bank of Commerce

STOCK INFO.	BLOOMBERG
BSE Sensex: 14,110	OBC IN
	REUTERS CODE
S&P CNX: 4,090	ORBC.BO

24 January 2007

Neutral

Previous Recommendation: Neutral

Rs223

Equity Shares (m)	250.5
52-Week Range	281/139
1,6,12 Rel. Perf.(%)	-4/0/-60
M.Cap. (Rs b)	55.9
M.Cap. (US\$ b)	1.3

YEAR	NET INCOME	PAT	EPS	EPS	P/E	P/BV	CAR	ROE	ROA	P/ABV
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	(%)	(X)
3/06A	21,578	8,031	32.1	-18.9	7.0	1.3	12.5	18.9	1.4	1.3
3/07E	22,926	9,129	36.4	13.7	6.1	1.1	12.0	16.8	1.4	1.1
3/08E	25,689	9,316	37.2	2.0	6.0	0.9	11.3	15.6	1.3	1.0

Oriental Bank of Commerce (OBC) has continued to report marginal growth in core NII. While core NII growth of 7% YoY to Rs4.2b was higher than our estimate, margins contracted on a YoY basis. PAT grew 19% YoY mainly on account of lower provisioning and lower taxes. Continued recoveries enabled a QoQ reduction in gross NPAs while net NPAs were flat.

- ⚡ NII grows 7% YoY; margins expand QoQ
- ⚡ Deposits up 23% YoY, loans grow 25% YoY
- ⚡ Core fee income up; trading income declines
- ⚡ Asset quality maintained QoQ

Further improvement in asset quality and continued recoveries are key things to watch out for. However, we believe that lower margins will continue to drag OBC's core operating earnings. On continued strong recoveries and lower provisions, we have upgraded our EPS estimate by 8% for FY07, but maintain our EPS estimate for FY08. OBC trades at 6x FY08E EPS and 0.9x FY08E book value (adjusted for goodwill). We maintain **Neutral**.

### QUARTERLY PERFORMANCE

(Rs Million)

	FY06				FY07				FY06	FY07E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Interest Income	9,876	10,069	10,499	10,747	11,353	12,822	13,137	13,436	41,189	50,749
Interest Expense	5,846	6,027	6,549	6,717	7,244	8,695	8,924	9,073	25,139	33,936
<b>Net Interest Income</b>	<b>4,030</b>	<b>4,042</b>	<b>3,950</b>	<b>4,030</b>	<b>4,110</b>	<b>4,128</b>	<b>4,213</b>	<b>4,363</b>	<b>16,051</b>	<b>16,814</b>
% Change (YoY)	6.8	4.7	5.4	3.9	2.0	2.1	6.7	8.3	5.3	4.8
Other Income	955	1,720	1,263	1,590	1,687	1,579	1,330	1,517	5,528	6,113
<b>Net Income</b>	<b>4,986</b>	<b>5,762</b>	<b>5,213</b>	<b>5,619</b>	<b>5,797</b>	<b>5,707</b>	<b>5,543</b>	<b>5,880</b>	<b>21,578</b>	<b>22,926</b>
% Change (YoY)	4.5	27.4	-1.1	-0.1	16.3	-1.0	6.3	4.6	6.4	6.2
Operating Expenses	2,136	2,503	2,225	2,795	2,287	2,566	2,476	2,694	9,659	10,023
<b>Operating Profit</b>	<b>2,850</b>	<b>3,259</b>	<b>2,988</b>	<b>2,824</b>	<b>3,510</b>	<b>3,141</b>	<b>3,067</b>	<b>3,186</b>	<b>11,919</b>	<b>12,904</b>
Provision & Contingencies	1,028	324	309	610	1,477	-737	81	380	2,271	1,200
<b>PBT</b>	<b>1,822</b>	<b>2,935</b>	<b>2,679</b>	<b>2,214</b>	<b>2,033</b>	<b>3,878</b>	<b>2,986</b>	<b>2,806</b>	<b>9,649</b>	<b>11,704</b>
Tax Provisions	775	670	633	-460	481	771	550	774	1,617	2,575
<b>Net Profit</b>	<b>1,048</b>	<b>2,265</b>	<b>2,047</b>	<b>2,673</b>	<b>1,553</b>	<b>3,108</b>	<b>2,437</b>	<b>2,032</b>	<b>8,031</b>	<b>9,129</b>
% Change (YoY)	-42.0	5.4	59.7	12.5	48.2	37.2	19.1	-24.0	5.6	13.7
Cost to Income Ratio (%)	42.8	43.4	42.7	49.7	39.4	43.4	44.7	45.8	44.8	43.7
Int Exp/ Int Earned (%)	59.2	59.9	62.4	62.5	63.8	59.9	67.9	67.5	61.0	66.9
Other Income / Net Income (%)	19.2	29.9	24.2	28.3	29.1	29.9	24.0	25.8	25.6	26.7

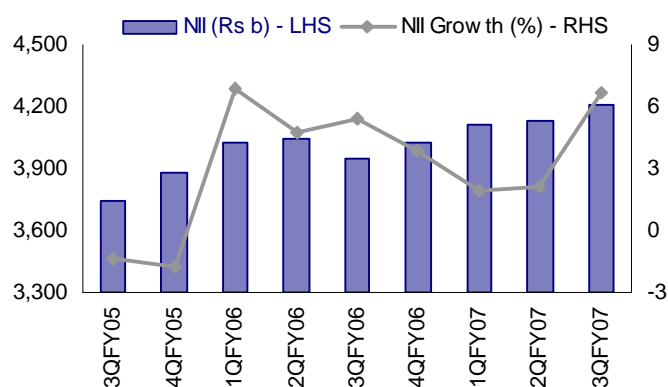
E: M OSt Estimates

Oriental Bank of Commerce (OBC) has continued to report marginal growth in core NII. While core NII growth of 7% YoY to Rs4.2b was higher than our estimate, margins contracted on a YoY basis. PAT grew 19% YoY mainly on account of lower provisioning and lower taxes. Continued recoveries enabled a QoQ reduction in gross NPAs while net NPAs were flat.

### NII grows 7% YoY; margins expand QoQ

OBC reported 7% YoY growth in core NII to Rs4.2b. Pressure on margins continued on the back of lower yielding Global Trust Bank (GTB) assets and rising deposit costs. Margins contracted on a YoY basis. However, on a QoQ basis, the bank was able to control its deposit cost, resulting in margins expanding from 2.54% in 2QFY07 to 2.75% in 3QFY07.

TREND IN NII



Source: Company / Motilal Oswal Securities

Cost of deposits has increased (60bp YoY) to 5.7% in 3QFY07, while yields on investments have declined by 40bp YoY to 8%. Yields on advances have moved up post-PLR hike and now are up 60bp YoY to 8.5%. We believe that GTB's operations continue to earn negligible margins, in turn impacting OBC's overall margins.

While a QoQ improvement in margins is positive, we believe that with investment yields still being at 8% and likely to re-price downward, overall margin pressure is likely to continue.

BREAKDOWN OF MARGINS (%)

	9MFY06	FY06	1QFY07	1HFY07	9MFY07
Avg Yield on Advances	7.9	7.9	8.1	8.5	8.5
Avg Yield on Investments	8.4	8.4	8.2	8.1	8.0
Avg Cost of Deposits	5.1	5.1	5.3	5.6	5.7
<b>NIMs</b>	<b>2.9</b>	<b>2.8</b>	<b>2.6</b>	<b>2.5</b>	<b>2.6</b>

Source: Company / Motilal Oswal Securities

### Deposits up 23% YoY, loans grow 25% YoY

On the business front, the bank has grown its loan book by 25% YoY to Rs415b. Deposits have grown 23% YoY to Rs607b. CASA ratio has been maintained at ~30%. The bank slowed down the growth in retail loans to just 9% YoY. Total retail credit portfolio increased from Rs63.2b as at end-3QFY06 to Rs68.8b as at end-3QFY07. Home loans increased from Rs46b as at end-3QFY06 to Rs56b as at end-3QFY07, reflecting growth of 16% and constituting 13% of net credit.

### Core fee income up; trading income declines

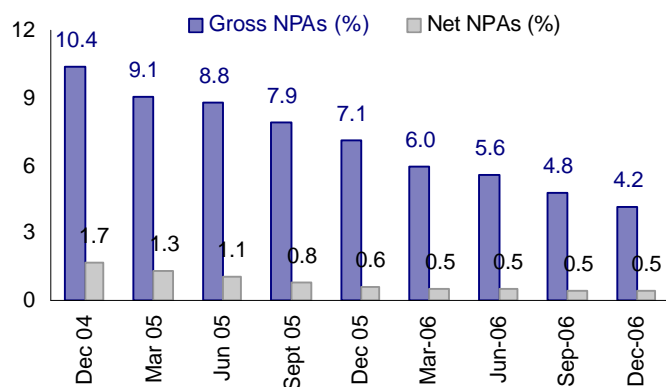
The bank has booked treasury income of Rs336m in 3QFY07, driven by debt as well as equities. In 3QFY06, it had booked treasury income of Rs500m. Core non-interest other income increased 30% YoY to Rs994m. Here again, we believe that recoveries from written off accounts have driven this growth.

### NPA provisions written back; asset quality maintained QoQ

The bank continued to write back NPA provisions on the back of continued cash recoveries. It recovered bad loans of Rs7b in 9MFY07 (Rs1.9b in 3QFY07) as against Rs4b (Rs0.8b in 3QFY06) in 9MFY06.

While gross NPAs have declined 56bp QoQ to 4.2% in 3QFY07, net NPAs are largely unchanged at 0.5%. In absolute terms, gross NPAs reduced by 5% QoQ to Rs17.5b, while net NPAs increased by 5% QoQ to Rs1.8b. As the bank has been writing back its excess provisions, net NPAs have remained flat over the last few quarters.

## TREND IN NPA



Source: Company /Motilal Oswal Securities

**Valuation and view**

Further improvement in asset quality and continued recoveries are key things to watch out for. However, we believe that lower margins will continue to drag OBC's core operating earnings. On continued strong recoveries and lower provisions, we have upgraded our EPS estimate by 8% for FY07, but maintain our EPS estimate for FY08. OBC trades at 6x FY08E EPS and 0.9x FY08E book value (adjusted for goodwill). We maintain **Neutral**.

## Oriental Bank of Commerce: an investment profile

### Company description

Oriental Bank of Commerce (OBC), established in 1943, is a North India-based state-owned bank, with a balance sheet size of Rs550b+. The government owns 51% of the bank's equity. After the merger with Global Trust Bank (GTB) in August 2004, OBC has acquired a pan-India presence and has a network of over 1,200 branches. Though most of OBC's ratios post-merger have deteriorated, we believe that the bank has strong recovery procedures in place to tackle the bad loans and turn around GTB's loss-making operations.

### Key investment arguments

- ✎ Aggressive loan growth to continue, with higher retail focus, branch expansion in industrial belts, and credit disbursements from GTB branches.
- ✎ Cost to income ratio would reduce, as GTB's high cost borrowings are repaid and salary levels are brought in line with OBC's.
- ✎ Sustained cash recoveries from GTB's NPAs would result in higher NIMs and superior asset quality.

### Key investment risks

- ✎ Cash recoveries, NPA reduction could be less than expected.

### Recent developments

- ✎ The Oriental Bank of Commerce, Indian Bank and Corporation Bank business alliance is considering sharing payment modes and launching a joint credit card.
- ✎ OBC intends to raise Tier-I capital by issuing perpetual bonds on private placement basis, not exceeding Rs2.5b.

### Valuation and view

- ✎ The stock trades at 6x FY08E EPS and 0.9x FY08E BV. We maintain **Neutral**.

### Sector view

- ✎ YTD loan growth of 30%+, highest in the last 12 years
- ✎ Volatility in interest rates would impact treasury.
- ✎ Benefits of significant improvement in asset quality not yet factored in earnings, valuations.
- ✎ We maintain an overweight stance on the sector.

#### COMPARATIVE VALUATIONS

		OBC	KARNATAKA	ICICI BK
P/E (x)	FY07E	6.1	7.0	26.5
	FY08E	6.0	6.1	21.5
P/ABV (x)	FY07E	1.1	1.2	3.8
	FY08E	1.0	1.0	3.4
RoE (%)	FY07E	16.8	16.9	14.0
	FY08E	15.6	17.0	15.5
RoA (%)	FY07E	1.4	1.2	1.1
	FY08E	1.3	1.3	1.0

#### SHAREHOLDING PATTERN (%)

	DEC-06	SEP-05	DEC-05
Promoter	51.1	51.1	51.1
Domestic Inst	22.0	20.8	19.9
Foreign	19.0	19.7	19.9
Others	7.9	8.4	9.1

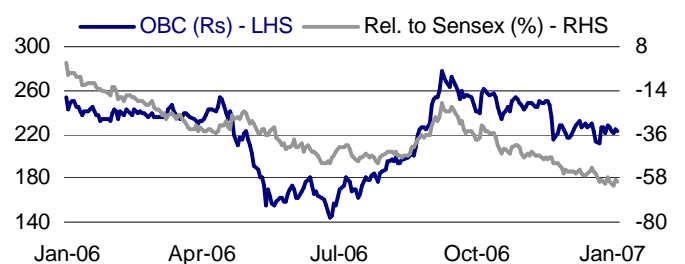
#### EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	36.4	32.2	13.1
FY08	37.2	36.3	2.6

#### TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
223	254	13.9	Neutral

#### STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2005	2006	2007E	2008E	2009E
Interest Income	35,719	41,189	50,749	59,337	69,131
Interest Expended	20,482	25,139	33,936	40,173	46,604
<b>Net Interest Income</b>	<b>15,237</b>	<b>16,051</b>	<b>16,814</b>	<b>19,164</b>	<b>22,527</b>
Change (%)	4.7	5.3	4.8	14.0	17.5
Other Income	5,052	5,528	6,113	6,525	7,100
<b>Net Income</b>	<b>20,289</b>	<b>21,578</b>	<b>22,926</b>	<b>25,689</b>	<b>29,626</b>
Change (%)	-6.8	6.4	6.2	2.1	15.3
Operating Expenses	7,957	9,659	10,023	11,101	12,413
<b>Operating Income</b>	<b>12,332</b>	<b>11,919</b>	<b>12,904</b>	<b>14,589</b>	<b>17,213</b>
Change (%)	-19.6	-3.3	8.3	13.1	18.0
Other Provisions	4,002	2,271	1,200	2,000	2,800
<b>PBT</b>	<b>8,330</b>	<b>9,649</b>	<b>11,704</b>	<b>12,589</b>	<b>14,413</b>
Tax	722	1,617	2,575	3,273	4,036
<b>PAT</b>	<b>7,608</b>	<b>8,031</b>	<b>9,129</b>	<b>9,316</b>	<b>10,378</b>
Change (%)	10.9	5.6	13.7	2.0	11.4
Proposed Dividend	659	1,286	1,403	1,528	1,754

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2005	2006	2007E	2008E	2009E
Capital	1,925	2,505	2,505	2,505	2,505
Reserves & Surplus	31,345	49,202	54,468	59,796	65,959
<b>Net Worth</b>	<b>33,270</b>	<b>51,708</b>	<b>56,974</b>	<b>62,301</b>	<b>68,465</b>
<b>Deposits</b>	<b>478,503</b>	<b>501,975</b>	<b>592,330</b>	<b>681,180</b>	<b>783,356</b>
Change (%)	34.1	4.9	18.0	15.0	15.0
Borrowings	7,281	8,764	10,000	12,000	12,000
Other Liabilities & Prov.	21,640	26,927	29,620	32,582	35,840
<b>Total Liabilities</b>	<b>540,695</b>	<b>589,374</b>	<b>688,923</b>	<b>788,062</b>	<b>899,661</b>
Current Assets	75,433	55,257	51,225	56,574	69,364
Investments	183,422	168,176	181,630	196,160	211,853
Change (%)	9.2	-8.3	8.0	8.0	8.0
Advances	252,992	335,772	423,073	499,226	579,103
Change (%)	28.5	32.7	26.0	18.0	16.0
Net Fixed Assets	3,805	3,842	4,036	4,246	4,300
Other Assets	25,043	26,327	28,960	31,856	35,041
<b>Total Assets</b>	<b>540,695</b>	<b>589,374</b>	<b>688,923</b>	<b>788,062</b>	<b>899,661</b>

ASSUMPTIONS					
(%)					
Deposit Growth	34.1	4.9	18.0	15.0	15.0
Advances Growth	28.5	32.7	26.0	18.0	16.0
Investments Growth	9.2	-8.3	8.0	8.0	8.0
Dividend	34.2	51.3	56.0	61.0	70.0
GRR	5.0	5.0	5.0	5.0	5.0

E: M OSt Estimates

RATIOS					
Y/E MARCH	2005	2006	2007E	2008E	2009E
<b>Spreads Analysis (%)</b>					
Avg. Yield - Earning Asset	7.9	7.7	8.4	8.5	8.7
Avg. Cost-Int. Bear. Liab.	4.8	5.0	6.1	6.2	6.3
Interest Spread	3.0	2.7	2.3	2.3	2.4
Net Interest Margin	3.4	3.0	2.8	2.7	2.8

Profitability Ratios (%)					
RoE	25.3	18.9	16.8	15.6	15.9
RoA	16	14	14	13	12
Int. Expended/Int. Earned	57.3	61.0	66.9	67.7	67.4
Other Inc./Net Income	24.9	25.6	26.7	25.4	24.0

Efficiency Ratios (%)					
Op. Exps./Net Income	39.2	44.8	43.7	43.2	41.9
Empl. Cost/Op. Exps.	49.9	51.8	46.5	45.7	44.5
Busi. per Empl. (Rs m)	44.1	52.4	61.3	72.2	83.0
NP per Empl. (Rs m)	0.5	0.5	0.6	0.6	0.7

Asset-Liability Profile (%)					
Adv./Deposit Ratio	52.9	66.9	71.4	73.3	73.9
Invest./Deposit Ratio	38.3	33.5	30.7	28.8	27.0
G-Sec/Invest. Ratio	81.7	83.0	83.0	83.0	83.0
Gross NPAs to Adv.	9.1	5.9	5.2	4.6	4.1
Net NPAs to Adv.	1.3	0.5	0.4	0.5	0.4
CAR	9.2	12.5	12.0	11.3	10.5
Tier 1	5.4	11.7	11.0	10.0	9.0

VALUATION					
Book Value (Rs)*	121.9	177.1	207.9	239.0	273.4
Price-BV (x)	1.8	1.3	1.1	0.9	0.8
Adjusted BV (Rs)	110.9	172.9	203.3	232.9	267.2
Price-ABV (x)	2.0	1.3	1.1	1.0	0.8
EPS (Rs)	39.5	32.1	36.4	37.2	41.4
EPS Growth (%)	10.9	-18.9	13.7	2.0	11.4
Price-Earnings (x)	5.6	7.0	6.1	6.0	5.4
OPS (Rs)	64.0	47.6	51.5	58.2	68.7
OPS Growth (%)	-19.6	-25.7	8.3	13.1	18.0
Price-OP (x)	3.5	4.7	4.3	3.8	3.2

E: M OSt Estimates, \* BV adjusted for goodwill



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**Oriental Bank of Commerce**

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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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