

29 January 2013

Bank of India

Core earnings weak, lower taxes drive profits; Sell

Rating: **Sell**

Target Price: ₹342

Share Price: ₹355

Key takeaways

Credit growth modest, NIM declines. At 20% yoy, the Bank of India's advances growth was modest on account of subdued growth in corporate (18.4% yoy) and SME (4.5% yoy). Deposits grew slower than credit at 13.6% yoy, resulting in credit-to-deposits increasing 422bps yoy to 79.2%. Adjusting for the interest on income tax refund, NIM declined 32bps yoy (12bps qoq) to 2.31%, led by a 37-bp yoy (10-bp qoq) drop in the share of CASA to 25.2%. We estimate a 25.4% CAGR in business over FY12-15, with CAGRs of 23.6% in advances and 26.7% in deposits over the same period.

Fee-based income weak, productivity declines. While core fee-income declined 8.6% yoy, treasury profits grew 20.8% yoy and comprised 4.6% of pre-provisioning profits (4.1% in 3QFY12). Also, income on foreign exchange transactions (₹1.8bn) and recoveries (₹2.46bn) supported non-interest income growth of 10% yoy. Productivity suffered, with core cost-income rising 229bps yoy (261bps qoq) to 44% and cost-to-assets rising 10bps qoq to 1.42%.

Asset quality improves, yet high slippages persist. Despite fresh slippages of ₹12.2bn (2.1% of loans), gross NPA fell 3.1% qoq, led by aggressive write-offs of ₹8.1bn. During the quarter, the bank saw fresh restructuring of ₹22.1bn (annualized, 3.8% of loans), with total restructured loans at ₹181.4bn (6.6% of overall loans). With tier-1 capital of 7.6%, the bank's capital cushion is stretched by the high restructured book and net NPA (1.97%). Perceptions of default risk would persist until the economic environment improves, restricting a sharp short-term valuation re-rating.

Our take. We expect the bank's modest core earnings and high NPA provisioning to hold its RoE below its past peak. Hence, we maintain our Sell rating. At our Mar'14 target, the stock would trade at a PABV of 1x FY13e and 0.8x FY14e. Our target is based on the two-stage DDM (CoE: 15.5%; beta: 1.2; Rf: 8%). **Risk:** Sharp improvement in asset quality.

| Quarterly results (YE: Mar) | 3QFY12 | 3QFY13 | % yoy | 9MFY12 | 9MFY13 | % yoy |
|------------------------------|--------|--------|--------|--------|--------|----------|
| Net interest income (₹m) | 20,675 | 23,085 | 11.7 | 58,124 | 65,480 | 12.7 |
| Non-interest income (₹m) | 8,522 | 9,371 | 10.0 | 23,541 | 26,721 | 13.5 |
| Operating expenses (₹m) | 11,878 | 13,898 | 17.0 | 34,871 | 38,367 | 10.0 |
| Cost-to-income (%) | 40.7 | 42.8 | 214bps | 42.7 | 41.6 | (109)bps |
| Pre-provisioning profit (₹m) | 17,319 | 18,558 | 7.2 | 46,793 | 53,834 | 15.0 |
| Provisions (₹m) | 6,931 | 9,158 | 32.1 | 24,147 | 29,401 | 21.8 |
| PBT (₹m) | 10,388 | 9,400 | (9.5) | 22,647 | 24,433 | 7.9 |
| Tax (₹m) | 3,227 | 1,365 | (57.7) | 5,399 | 4,505 | (16.6) |
| PAT (₹m) | 7,161 | 8,035 | 12.2 | 17,248 | 19,928 | 15.5 |
| EPS (₹) | 13.1 | 14.0 | 6.9 | 31.6 | 34.7 | 10.0 |

Source: Company, Anand Rathi Research

| Key data | BOI IN / BOI.BO |
|--------------------|--------------------|
| 52-week high / low | ₹408 / ₹254 |
| Sensex / Nifty | 20103 / 6075 |
| 3-m average volume | US\$6.8m |
| Market cap | ₹204bn / US\$3.8bn |
| Shares outstanding | 574.5m |

| Shareholding pattern (%) | Dec-12 | Sep-12 | Jun-12 |
|--------------------------|--------|--------|--------|
| Promoters | 62.7 | 62.7 | 62.7 |
| - of which, Pledged | - | - | - |
| Free Float | 37.3 | 37.3 | 37.3 |
| - Foreign Institutions | 14.1 | 14.4 | 15.0 |
| - Domestic Institutions | 16.5 | 16.2 | 16.1 |
| - Public | 6.7 | 6.7 | 6.2 |

| Financials (YE: Mar) | FY13e | FY14e |
|--------------------------|--------|---------|
| Net interest income (₹m) | 91,144 | 118,526 |
| Net profit (₹m) | 31,693 | 48,153 |
| EPS (₹) | 55.2 | 83.8 |
| Growth (%) | 18.4 | 51.9 |
| PE (x) | 5.8 | 3.8 |
| PABV (x) | 1.1 | 0.9 |
| RoE (%) | 14.2 | 18.8 |
| RoA (%) | 0.8 | 0.9 |
| Dividend yield (%) | 2.3 | 3.5 |
| Net NPA (%) | 1.8 | 1.7 |

Source: Anand Rathi Research

Clyton Fernandes

+9122 6626 6744
clytonfernandes@rathi.com

Kaitav Shah

+9122 6626 6545
kaitavshah@rathi.com

Anand Rathi Shares and Stock Brokers Limited (hereinafter "ARSSBL") is a full service brokerage and equities research firm and the views expressed therein are solely of ARSSBL and not of the companies which have been covered in the Research Report. This report is intended for the sole use of the Recipient and is to be circulated only within India and to no countries outside India. Disclosures and analyst certifications are present in Appendix.

Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹m)

| Year-end: Mar | FY11 | FY12 | FY13e | FY14e | FY15e |
|----------------------|---------|---------|---------|---------|---------|
| Net interest income | 78,107 | 83,134 | 91,144 | 118,526 | 150,822 |
| NII growth (%) | 35.7 | 6.4 | 9.6 | 30.0 | 27.2 |
| Non-interest inc | 26,418 | 33,212 | 37,642 | 41,336 | 45,737 |
| Total income | 104,525 | 116,346 | 128,786 | 159,862 | 196,559 |
| Total Inc growth (%) | 24.8 | 11.3 | 10.7 | 24.1 | 23.0 |
| Op. expenses | 50,682 | 49,407 | 53,446 | 68,581 | 85,896 |
| Operating profit | 53,842 | 66,939 | 75,340 | 91,281 | 110,663 |
| Op profit growth (%) | 14.4 | 24.3 | 12.5 | 21.2 | 21.2 |
| Provisions | 18,888 | 31,164 | 36,213 | 31,090 | 36,896 |
| PBT | 34,954 | 35,775 | 39,127 | 60,191 | 73,767 |
| Tax | 10,067 | 9,000 | 7,434 | 12,038 | 16,598 |
| PAT | 24,887 | 26,775 | 31,693 | 48,153 | 57,169 |
| PAT growth (%) | 42.9 | 7.6 | 18.4 | 51.9 | 18.7 |
| FDEPS (₹/share) | 45.5 | 46.6 | 55.2 | 83.8 | 99.5 |
| DPS (₹/share) | 7.0 | 7.0 | 8.3 | 12.6 | 14.9 |

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (₹m)

| Year-end: Mar | FY11 | FY12 | FY13e | FY14e | FY15e |
|----------------------|-----------|-----------|-----------|-----------|-----------|
| Share capital | 5,472 | 5,745 | 5,745 | 5,745 | 5,745 |
| Reserves & surplus | 167,435 | 203,873 | 230,057 | 269,841 | 317,075 |
| Deposits | 2,988,858 | 3,182,160 | 3,708,303 | 5,183,885 | 6,479,856 |
| Borrowings | 349,961 | 453,577 | 514,991 | 584,956 | 664,687 |
| Minority interests | - | - | - | - | - |
| Total liabilities | 3,511,725 | 3,845,355 | 4,459,097 | 6,044,427 | 7,467,363 |
| Advances | 2,130,962 | 2,488,333 | 2,929,559 | 3,758,316 | 4,697,895 |
| Investments | 858,724 | 867,536 | 964,159 | 1,503,327 | 1,879,158 |
| Cash & bank bal | 373,100 | 347,113 | 418,228 | 583,318 | 643,886 |
| Fixed & other assets | 148,940 | 142,373 | 147,150 | 199,466 | 246,423 |
| Total assets | 3,511,725 | 3,845,355 | 4,459,097 | 6,044,427 | 7,467,363 |
| No. of shares (m) | 547 | 575 | 575 | 575 | 575 |
| Deposits growth (%) | 30.1 | 6.5 | 16.5 | 39.8 | 25.0 |
| Advances growth (%) | 26.5 | 16.8 | 17.7 | 28.3 | 25.0 |

Source: Company, Anand Rathi Research

Fig 3 – Key ratios

| Year-end: Mar | FY11 | FY12 | FY13e | FY14e | FY15e |
|---------------------------|-------|-------|-------|-------|-------|
| NIM (%) | 2.6 | 2.4 | 2.3 | 2.3 | 2.3 |
| Other inc / total inc (%) | 25.3 | 28.5 | 29.2 | 25.9 | 23.3 |
| Cost-income (%) | 48.5 | 42.5 | 41.5 | 42.9 | 43.7 |
| Provision coverage (%) | 59.6 | 38.0 | 38.0 | 30.3 | 26.9 |
| Dividend payout (%) | 15.4 | 15.0 | 15.0 | 15.0 | 15.0 |
| Credit-deposit (%) | 71.3 | 78.2 | 79.0 | 72.5 | 72.5 |
| Investment-deposit (%) | 28.7 | 27.3 | 26.0 | 29.0 | 29.0 |
| Gross NPA (%) | 2.3 | 2.4 | 3.0 | 2.4 | 2.0 |
| Net NPA (%) | 0.9 | 1.5 | 1.8 | 1.7 | 1.5 |
| BV (₹) | 316.0 | 364.9 | 410.4 | 479.7 | 561.9 |
| Adj. BV (₹) | 256.3 | 279.7 | 295.1 | 348.0 | 419.9 |
| CAR (%) | 12.3 | 12.1 | 11.4 | 10.2 | 9.5 |
| - Tier 1 (%) | 8.5 | 8.7 | 8.3 | 7.5 | 7.1 |
| RoE (%) | 15.8 | 14.0 | 14.2 | 18.8 | 19.1 |
| RoA (%) | 0.8 | 0.7 | 0.8 | 0.9 | 0.8 |

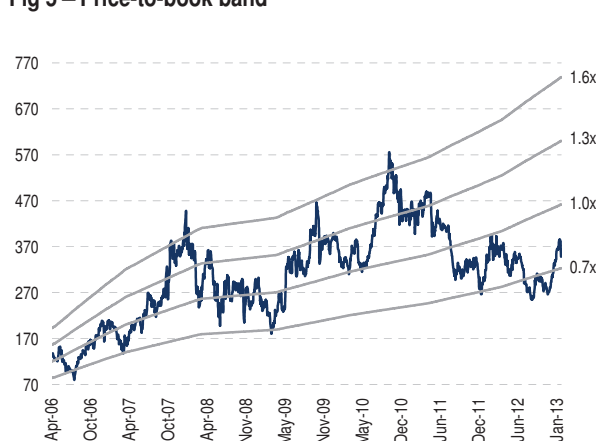
Source: Company, Anand Rathi Research

Fig 4 – PE band



Source: Bloomberg, Anand Rathi Research

Fig 5 – Price-to-book band



Source: Bloomberg, Anand Rathi Research

Fig 6 – Bank of India vs. Bankex



Source: Bloomberg

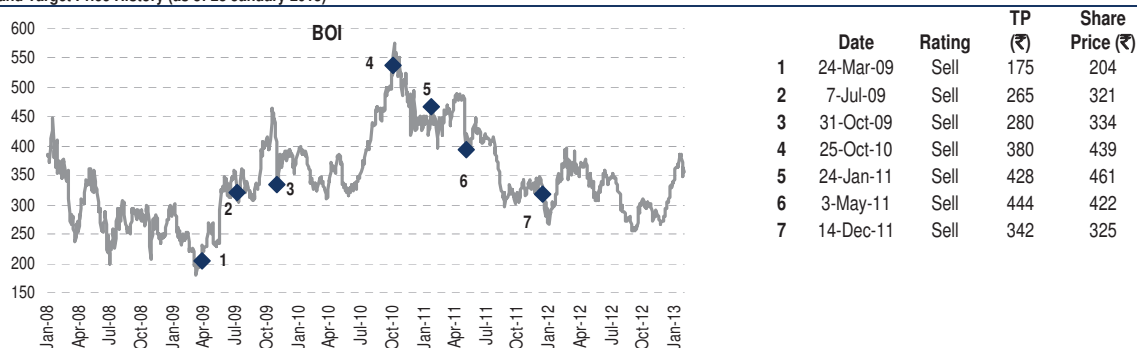
Appendix

Analyst Certification

The views expressed in this Research Report accurately reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this report. The research analysts are bound by stringent internal regulations and also legal and statutory requirements of the Securities and Exchange Board of India (hereinafter "SEBI") and the analysts' compensation are completely delinked from all the other companies and/or entities of Anand Rathi, and have no bearing whatsoever on any recommendation that they have given in the Research Report.

Important Disclosures on subject companies

Rating and Target Price History (as of 28 January 2013)



The research analysts, strategists, or research associates principally responsible for the preparation of Anand Rathi Research have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and overall investment banking revenues.

Anand Rathi Ratings Definitions

Analysts' ratings and the corresponding expected returns take into account our definitions of Large Caps (>US\$1bn) and Mid/Small Caps (<US\$1bn) as described in the Ratings Table below:

Ratings Guide

| | Buy | Hold | Sell |
|---------------------------|------|-------|------|
| Large Caps (>US\$1bn) | >15% | 5-15% | <5% |
| Mid/Small Caps (<US\$1bn) | >25% | 5-25% | <5% |

Anand Rathi Research Ratings Distribution (as of 29 Oct 2012)

| | Buy | Hold | Sell |
|---|-----|------|------|
| Anand Rathi Research stock coverage (155) | 65% | 25% | 10% |
| % who are investment banking clients | 5% | 3% | 0% |

Other Disclosures

This report has been issued by ARSSBL which is a SEBI regulated entity, and which is in full compliance with all rules and regulations as are applicable to its functioning and governance. The investors should note that ARSSBL is one of the companies comprising within ANAND RATHI group, and ANAND RATHI as a group consists of various companies which may include (but is not limited to) its subsidiaries, its affiliates, its group companies who may hold positions, views, stakes and may service the companies covered in this report independent of ARSSBL. Investors are cautioned to be aware that there could arise a potential conflict of interest in the views held by ARSSBL and other companies of Anand Rathi who maybe affiliated, connected or catering to the companies mentioned in the Research Report; even though, ARSSBL and Anand Rathi are fully compliant with all procedural and operational regulatory requirements. Thus, investors should not use this as a sole basis for making their investment decision and should consider the recommendations mentioned in the Research Report bearing in mind the aforementioned.

Further, the information herein has been obtained from various sources which we believe is reliable, and we do not guarantee its accuracy or completeness. Neither the information nor any opinion expressed herein constitutes an offer, or an invitation to make an offer, to buy or sell any securities or any options, futures or other derivatives related to such securities (hereinafter referred to as "Related Investments"). ARSSBL and/or Anand Rathi may trade for their own accounts as market maker / jobber and/or arbitrageur in any securities of the companies mentioned in the Research Report or in related investments, and may be on taking a different position from the ones which have been taken by the public orders. ARSSBL and/or Anand Rathi and its affiliates, directors, officers, and employees may have a long or short position in any securities of the companies mentioned in the Research Report or in Related Investments. ARSSBL and/or Anand Rathi, may from time to time, perform investment banking, investment management, financial advisory or any other services not explicitly mentioned herein, or solicit investment banking or other business from, any entity and/or company mentioned in this Research Report; however, the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the other companies of Anand Rathi, even though there might exist an inherent conflict of interest.

Furthermore, this Research Report is prepared for private circulation and use only. It does not have regard to the specific investment objectives, financial situation and the specific financial needs or objectives of any specific person who may receive this Research Report. Investors should seek financial advice regarding the appropriateness of investing in any securities or investment strategies discussed or recommended in this Research Report, and, should understand that statements regarding future prospects may or may not be realized, and we can not guarantee the same as analysis and valuation is a tool to enable investors to make investment decisions but, is not an exact and/or a precise science. Investors should note that income from such securities, if any, may fluctuate and that each security's price or value may rise or fall. Past performance is not necessarily a guide to future performance. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related investments mentioned in this report.

Other Disclosures pertaining to distribution of research in the United States of America

This material was produced by ARSSBL, solely for information purposes and for the use of the recipient. It is not to be reproduced under any circumstances and is not to be copied or made available to any person other than the recipient. It is distributed in the United States of America by Enclave Capital LLC (19 West 44th Street, Suite 1700, New York, NY 10036) and elsewhere in the world by ARSSBL or an authorized affiliate of ARSSBL (such entities and any other entity, directly or indirectly, controlled by ARSSBL, the "Affiliates"). This document does not constitute an offer of, or an invitation by or on behalf of ARSSBL or its Affiliates or any other company to any person, to buy or sell any security. The information contained herein has been obtained from published information and other sources, which ARSSBL or its Affiliates consider to be reliable. None of ARSSBL or its Affiliates accepts any liability or responsibility whatsoever for the accuracy or completeness of any such information. All estimates, expressions of opinion and other subjective judgments contained herein are made as of the date of this document. Emerging securities markets may be subject to risks significantly higher than more established markets. In particular, the political and economic environment, company practices and market prices and volumes may be subject to significant variations. The ability to assess such risks may also be limited due to significantly lower information quantity and quality. By accepting this document, you agree to be bound by all the foregoing provisions.

1. ARSSBL or its Affiliates may or may not have been beneficial owners of the securities mentioned in this report.
2. ARSSBL or its affiliates may have or not managed or co-managed a public offering of the securities mentioned in the report in the past 12 months.
3. ARSSBL or its affiliates may have or not received compensation for investment banking services from the issuer of these securities in the past 12 months and do not expect to receive compensation for investment banking services from the issuer of these securities within the next three months.
4. However, one or more of ARSSBL or its Affiliates may, from time to time, have a long or short position in any of the securities mentioned herein and may buy or sell those securities or options thereon, either on their own account or on behalf of their clients.
5. As of the publication of this report, ARSSBL does not make a market in the subject securities.
6. ARSSBL or its Affiliates may or may not, to the extent permitted by law, act upon or use the above material or the conclusions stated above, or the research or analysis on which they are based before the material is published to recipients and from time to time, provide investment banking, investment management or other services for or solicit to seek to obtain investment banking, or other securities business from, any entity referred to in this report.

Enclave Capital LLC is distributing this document in the United States of America. ARSSBL accepts responsibility for its contents. Any US customer wishing to effect transactions in any securities referred to herein or options thereon should do so only by contacting a representative of Enclave Capital LLC.

© 2013 Anand Rathi Shares and Stock Brokers Limited. All rights reserved. This report or any portion thereof may not be reprinted, sold or redistributed without the prior written consent of Anand Rathi Shares and Stock Brokers Limited.

Additional information on recommended securities/instruments is available on request.