Motilal Oswal

the Corner Office
Interaction with the CEO

Oriental Bank of Commerce

Mr SL Bansal
Chairman and Managing Director

Mr SL Bansal has assumed charge as CMD of OBC in March 2012 and has tenure till September 2014. Mr Bansal started his career as a Probationary Officer in Union Bank of India, where he gained vast experience in different roles. In 2010, he became Executive Director of United Bank of India.

Realigning business strategy: Focus on qualitative growth

NPA management, recoveries to be key focus area

- **De-bulking of balance sheet, with change in branch banking strategy to improve operating parameters**
- **To improve CASA ratio by capitalizing on strong foothold in CASA-rich northern states - targets CASA ratio of 25% by CY12 as against 22% as at the end of CY11**
- **Credit monitoring and NPA recovery to be key focus area**
- **To increase granularity in loan portfolio by increasing focus on SME and retail portfolio**

We met the new CMD of Oriental Bank of Commerce (OBC), Mr SL Bansal to gain insights into the bank's strategies and its roadmap under the new leadership. Our key takeaways:

De-bulking the balance sheet - A key requirement for improving operating parameters: In the last few years, strong loan growth and focus on bulk business led to a decline in OBC's CASA ratio and impacted margins. As a strategy, Mr Bansal intends to de-bulk the balance sheet. Accordingly, only select branches would focus on the wholesale business while the others would focus on the retail, SME and mid-corporate segments. In the process of realignment of its balance sheet, the bank is willing to grow moderately.

Improving CASA ratio - To leverage strong foothold in CASA-rich northern region: OBC's CASA ratio has been lower among state-owned banks at ~22% as against the industry average of ~30%. As at December 2011, the bank had ~1,750 branches, with very strong presence in the CASA-rich northern region. The management is planning various initiatives to improve CASA ratio and to leverage upon its strong foothold in the CASA-rich belt. Shedding of bulk deposits would also help to improve CASA ratio. The management targets CASA ratio of 25% by the end of CY12 as compared to 22% in December 2011.

NPA management and recoveries - A key focus area: Recoveries from NPAs and strengthening of credit appraisal at all levels to improve asset quality would be OBC's key focus areas. Moreover, with the help of technology, credit monitoring processes should advance considerably. The management is also considering providing preemptive restructuring of assets where the borrower has been temporarily impacted by economic slowdown.

Valuation and view - Maintain Buy: We expect near-term margins to be under pressure due to (1) tight liquidity conditions, (2) lower CASA ratio, and (3) higher proportion of deposits at preferential rates. However, we believe the new management's focus to improve the balance sheet, even at the cost of growth, is a step in the right direction. Though core operating parameters are under pressure, a strong management at the helm of affairs and low valuations are comforting. We expect OBC to report RoA of 0.7% and RoE of ~12% over FY12/13. The stock trades at 0.7x FY12E and 0.6x FY13E BV. Maintain **Buy**.

Stock Info

CMP (INR) - 2 Apr. 2012	256
Bloomberg	OBC IN
Equity Shares (m)	291.8
52-Week Range (INR)	406/190
1,6,12 Rel.Perf.(%)	-11/-20/-24
M.Cap.(INR b)/(USD b)	75/2

Financial and valuation summary

Year End	Net Income (INR m)	PAT (INR m)	EPS (INR)	EPS Gr. (%)	P/E (X)	BV (INR)	P/BV (X)	P/ABV (X)	RoAA (%)	RoAE (%)
3/11A	51,376	15,029	51.5	13.7	5.0	350	0.7	0.8	1.0	17.1
3/12E	55,131	12,006	41.1	-20.1	6.2	381	0.7	0.8	0.7	11.3
3/13E	63,292	13,992	48.0	16.6	5.3	418	0.6	0.7	0.7	12.0
3/14E	72,935	15,474	53.0	10.6	4.8	459	0.6	0.6	0.7	12.1

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We met the new CMD of Oriental Bank of Commerce (OBC), Mr SL Bansal to gain insights into the bank's strategies and its roadmap under the new leadership. Mr Bansal has tenure of at least 10 quarters till September 2014, ensuring longevity of the new strategies.

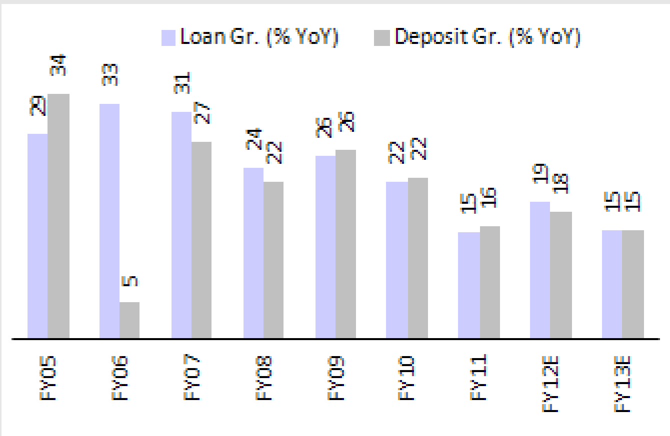
Some of the advantages for Mr Bansal while taking over as CMD of OBC are:

1. Meaningful stint with OBC – In the early stage of his career, he headed various branches/regions in North and Central India.
2. Throughout his career, he has been a banker involved with credit functions.
3. He brings with him the experience of successful improvement in key parameters of United Bank of India where he worked as Executive Director.

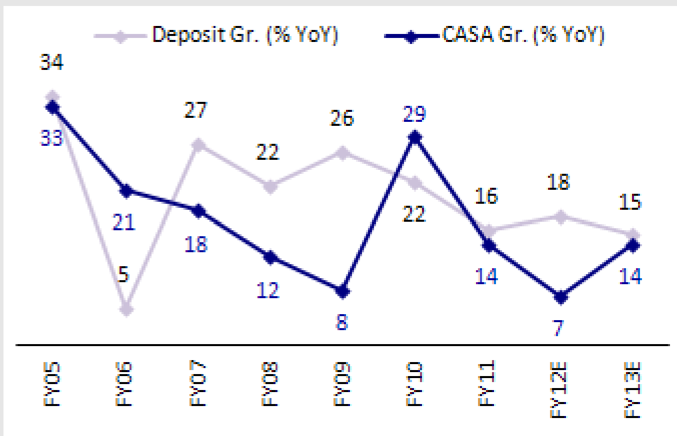
De-bulking the balance sheet: A key requirement for improving operating parameters

- Over the past few years, OBC's focus has shifted towards bulk business to rapidly grow the balance sheet. This has taken a toll on its core operating performance. Margins and CASA have been impacted significantly due to the rapidly growing bulk business.
- Mr Bansal wants to de-bulk the balance sheet although in the process the bank may have to grow at a moderate pace in the near-term.
- To achieve the desired results, OBC has shifted the bulk business to select branches (dedicated for wholesale banking) which would be monitored directly from the Head Office (HO). Meanwhile, the other branches have been directed to strengthen focus on SME, retail and mid-corporate segments.

Expect business growth to moderate



Deposit mobilization to be led by CASA deposits



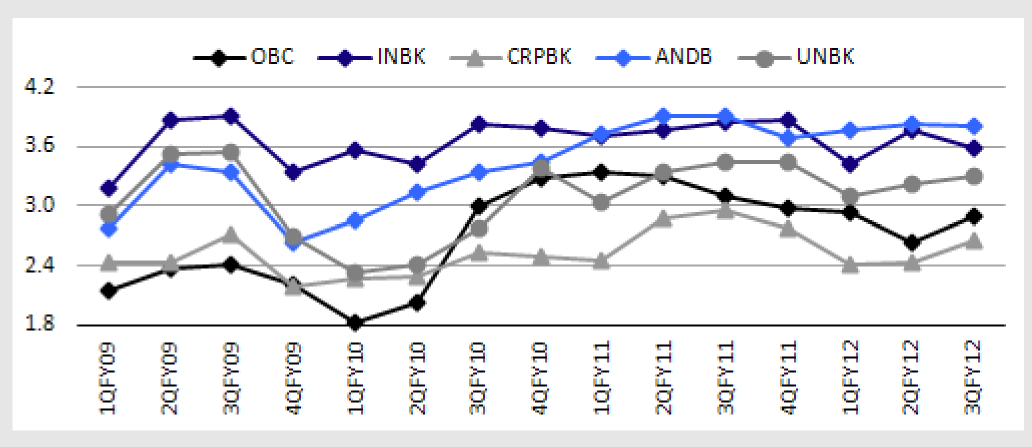
Source: Company/MOSL

Focus on de-bulking balance sheet to lead to moderation in business growth

Shedding of bulk deposits to lead to overall moderation in deposit growth; CASA growth likely to improve

Higher share of bulk business in overall business is leading to volatility in margins. Higher thrust on CASA and focus on high yielding retail and SME segments should propel margins upwards

Margins, though improved, remain below peers (%)

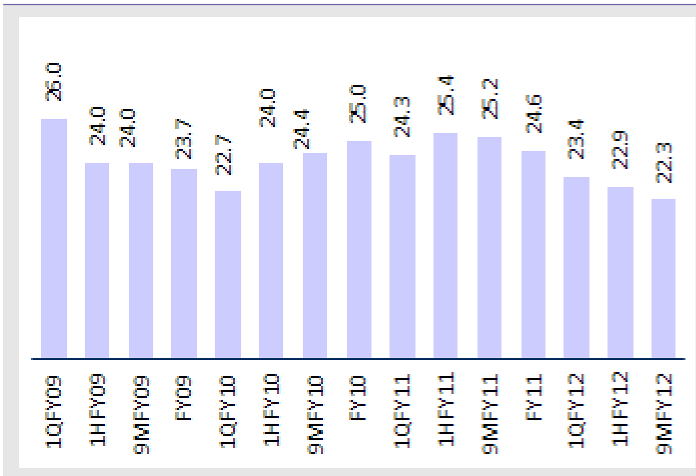


Source: Company/MOSL

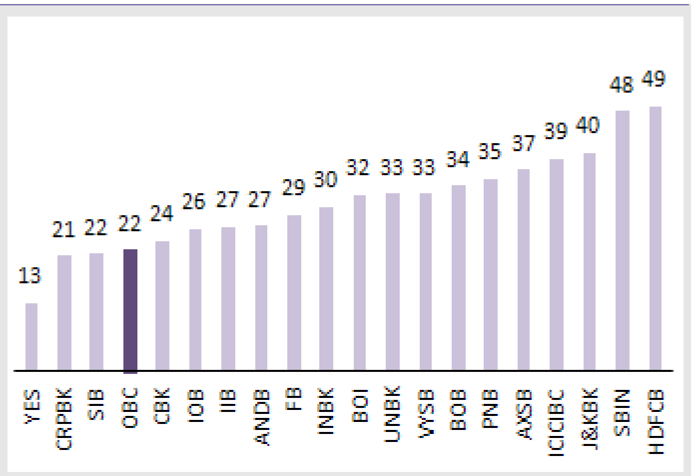
Improving CASA ratio: To leverage strong foothold in CASA-rich northern region

- OBC's CASA ratio has been at the lower end among state-owned banks at ~22% as against the industry average of ~30%. The steep decline in CASA ratio has been on the back of rapid increase in the bank's bulk business.
- As at December 2011, the bank had ~1,750 branches, with very strong presence in the CASA-rich northern region. The management is planning various initiatives to improve CASA ratio and to leverage upon its strong foothold in the CASA-rich belt. Shedding of bulk deposits would also help to improve CASA ratio.
- The management targets CASA ratio of 25% by the end of CY12 as compared to 22% in December 2011.

CASA ratio continues to decline (%) ...



...and remains well below peers (%)



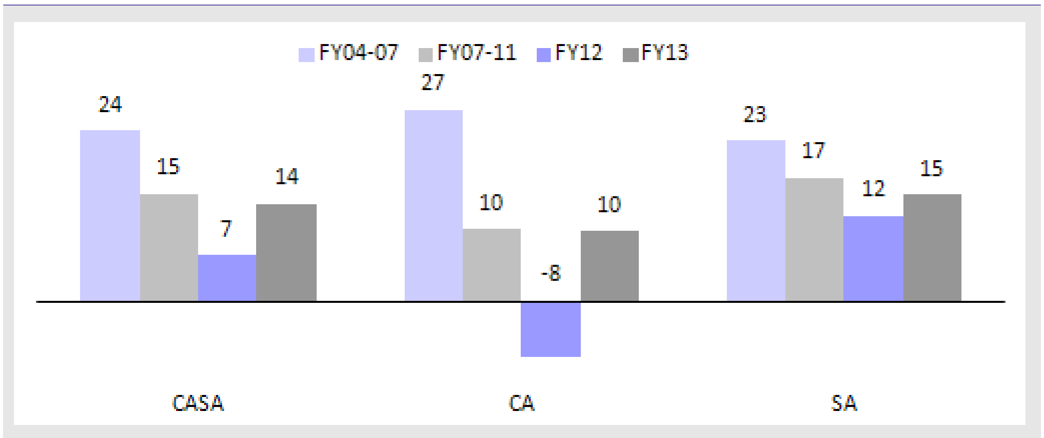
Source: Company/MOSL

Strong loan growth coupled with moderating CASA growth leading to decline in CASA ratio

Despite strong presence in CASA-rich region, OBC's CASA ratio remains well below peers

Expect CASA growth to improve in FY13, led by traction in SA deposits

CASA growth to bounce back (% YoY)

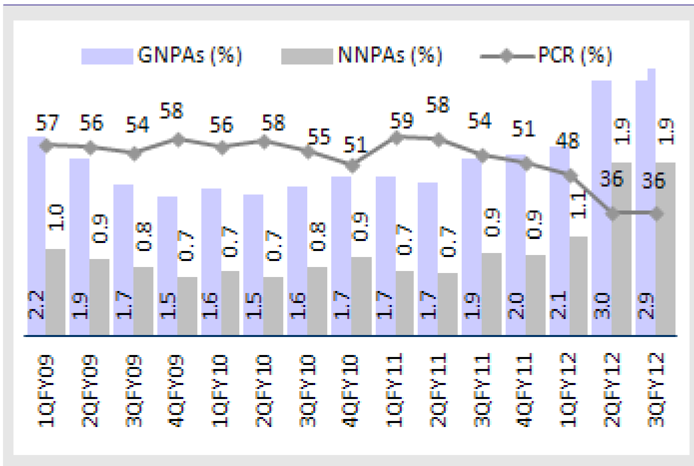


Source: Company/MOSL

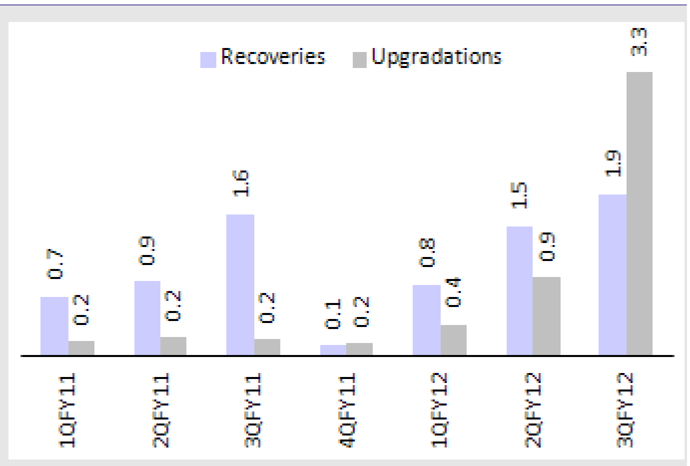
NPA management and recoveries: A key focus area

- Credit monitoring and recoveries from NPA accounts would also be OBC's key focus areas. To improve asset quality, the management is planning to strengthen credit appraisal at all levels. Moreover, with the help of technology, credit monitoring processes should advance considerably.
- The management is also considering providing preemptive restructuring of assets where the borrower has been temporarily impacted by economic slowdown.
- The healthy momentum in recoveries continues and the trends during 4QFY12 too looks encouraging. To expedite the recovery process, the bank is: (1) holding recovery camps across the country and offering a one-time settlement (OTS) scheme to small borrowers (less than INR1m category) based on their repayment capacity, and (2) implementing action under SARFAESI Act to accelerate disposal of assets and improve recoveries.

Pressure on asset quality has increased in line with industry



Momentum in recoveries remains strong (INR b)

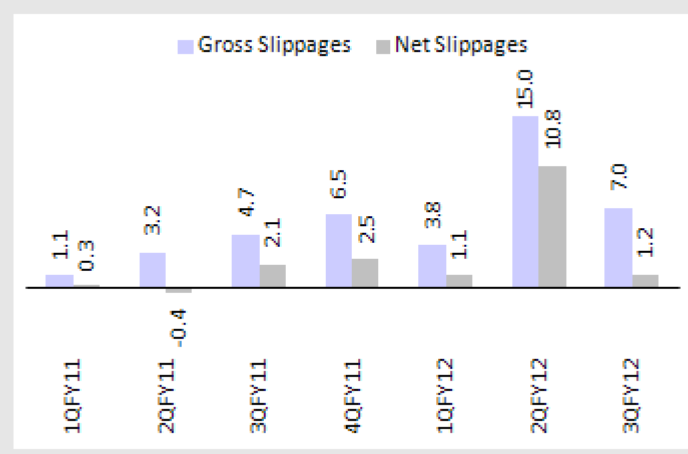


Source: Company/MOSL

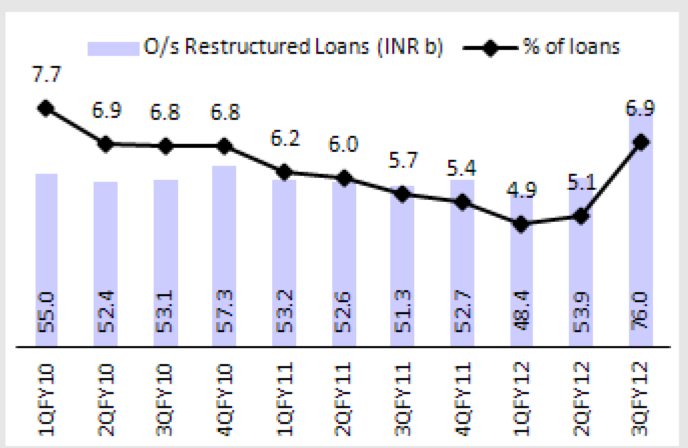
Economic moderation and system-based NPA recognition has led to higher slippages over the past few quarters

While momentum in recoveries remains strong, further steps initiated by the management could lead to positive surprise

Net slippages are trending downwards (INR b)



Restructured loans have increased in line with industry trends



Source: Company/MOSL

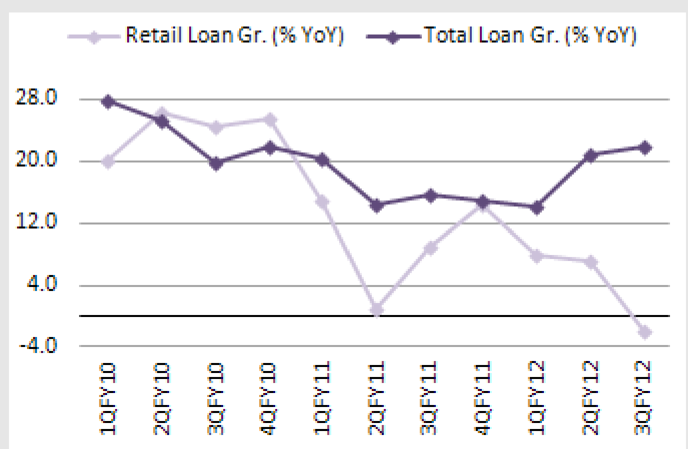
Despite higher gross slippages, net slippages have been lower due to increasing upgradations and recoveries

Restructured loans have been slightly higher than industry on account of certain large accounts getting restructured

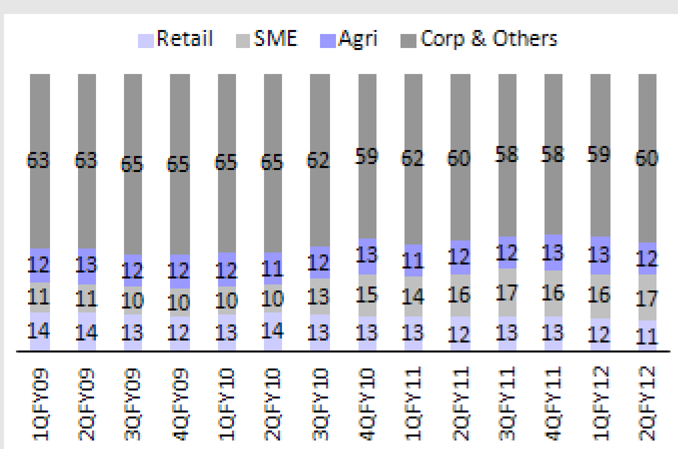
Focusing on SME / Retail portfolio: Capitalizing on key strength

- To reduce dependence on the wholesale business and to increase the share of high yielding assets in the overall mix, the management intends to focus on the SME and Retail portfolio.
- After shifting the wholesale business to select branches, the management has asked branches to focus on the SME/Retail business. The field officers have been directed to exercise discretionary powers to make eligible good credit prospects in line with the bank's systems and processes.
- In terms of the retail banking strategy, the branches have been advised to prepare retail credit budgets for the year and focus specifically on housing loans, vehicle loans and education loans to grow and de-risk the balance sheet.

Retail loan growth lags overall loan growth



Proportion of retail loans in overall loans declines (%)



Source: Company/MOSL

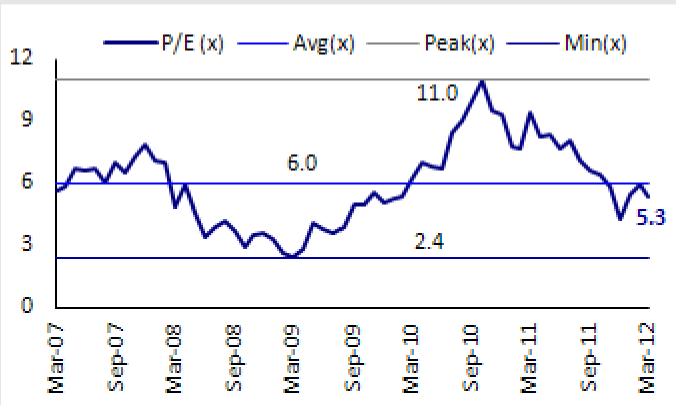
Retail loan growth to improve with increased focus on housing, vehicle and educational loans

Share of SME and retail segments to improve, led by the management's increased focus on these segments

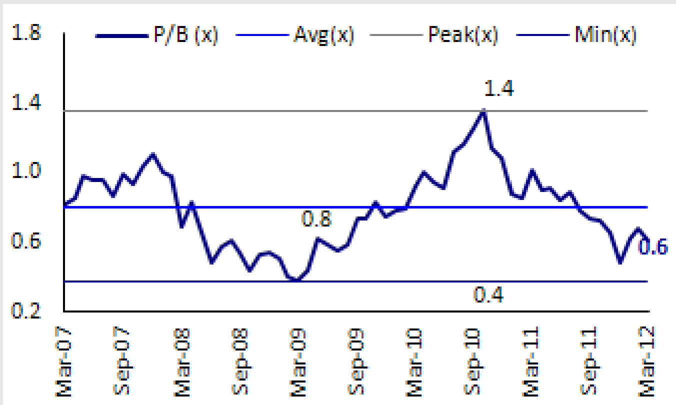
Valuation and view: Maintain Buy

- We expect near-term margins to be under pressure due to (1) tight liquidity conditions, (2) lower CASA ratio, and (3) higher proportion of deposits at preferential rates. However, we believe the new management's focus to improve the balance sheet, even at the cost of growth, is a step in the right direction.
- For improving core operating parameters, balance sheet consolidation is imperative, in our view. Outstanding standard restructured loan book stands at INR608b (5.6% of loans), and further restructuring expected in 1HCY12 remains a concern. Immediately after assuming office, the new CMD has taken NPA management and recoveries as focus areas, which should reduce stress.
- Though core operating parameters are under pressure, a strong management at the helm of affairs and low valuations are comforting.
- We expect the bank to report an EPS of INR41 for FY12 and INR48 for FY13, and BV of INR382 for FY12 and INR418 for FY13. It is likely to report RoA of 0.7% and RoE of ~12% over FY12/13. On the back of higher proportion of wholesale business, OBC has one of the lowest cost-to-income ratios in the industry, which remains its key strength. The stock trades at 0.7x FY12E and 0.6x FY13E BV. Maintain **Buy**.

OBC: One-year forward P/BV



OBC: One-year forward P/E



Source: Company/MOSL

Financials and Valuation

Income Statement

(INR Million)

Y/E March	2009	2010	2011	2012E	2013E	2014E
Interest Income	88,565	102,571	120,878	160,085	180,063	203,267
Interest Expense	68,600	73,497	79,103	117,365	130,864	146,129
Net Interest Income	**19,965**	**29,074**	**41,775**	**42,720**	**49,200**	**57,137**
Change (%)	19.5	45.6	43.7	2.3	15.2	16.1
Non Interest Income	10,713	12,000	9,601	12,411	14,092	15,798
Net Income	**30,678**	**41,075**	**51,376**	**55,131**	**63,292**	**72,935**
Change (%)	33.5	33.9	25.1	7.3	14.8	15.2
Operating Expenses	13,828	16,860	18,925	22,582	26,150	29,933
Pre Provision Profits	**16,850**	**24,215**	**32,451**	**32,548**	**37,141**	**43,002**
Change (%)	38.2	43.7	34.0	0.3	14.1	15.8
Provisions (excl tax)	5,255	8,176	12,065	15,639	16,412	20,078
PBT	**11,595**	**16,039**	**20,386**	**16,909**	**20,730**	**22,924**
Tax	2,540	4,692	5,357	4,904	6,737	7,450
Tax Rate (%)	21.9	29.3	26.3	29.0	32.5	32.5
PAT	**9,054**	**11,347**	**15,029**	**12,006**	**13,992**	**15,474**
Change (%)	7.7	25.3	32.4	-20.1	16.6	10.6
Equity Dividend (Incl tax)	**2,140**	**2,667**	**3,527**	**2,809**	**3,274**	**3,621**
Core PPP*	**12,036**	**19,980**	**31,698**	**30,798**	**34,891**	**40,652**
Change (%)	13.0	66.0	58.7	-2.8	13.3	16.5

*Core PPP is (NII+Fee income-Opex)

Balance Sheet

(INR Million)

Y/E March	2009	2010	2011	2012E	2013E	2014E
Equity Share Capital	2,505	2,505	2,918	2,918	2,918	2,918
Reserves & Surplus	71,529	79,874	108,054	116,940	127,348	138,891
Net Worth	**74,034**	**82,379**	**110,971**	**119,858**	**130,266**	**141,808**
Deposits	983,688	1,202,576	1,390,543	1,633,888	1,878,971	2,217,185
Change (%)	26.3	22.3	15.6	17.5	15.0	18.0
of which CASA Dep	**233,562**	**300,229**	**341,480**	**364,132**	**414,406**	**471,786**
Change (%)	7.5	28.5	13.7	6.6	13.8	13.8
Borrowings	27,220	48,870	56,392	88,381	100,413	111,386
Other Liabilities & Prov.	40,883	40,484	55,528	62,645	72,562	84,163
Total Liabilities	**1,125,826**	**1,374,310**	**1,613,434**	**1,904,771**	**2,182,211**	**2,554,542**
Current Assets	122,251	145,999	190,887	222,527	249,542	277,895
Investments	**284,890**	**357,853**	**420,748**	**483,860**	**556,439**	**656,598**
Change (%)	18.9	25.6	17.6	15.0	15.0	18.0
Loans	**685,004**	**834,893**	**959,082**	**1,141,308**	**1,312,504**	**1,548,755**
Change (%)	25.5	21.9	14.9	19.0	15.0	18.0
Fixed Assets	13,839	13,940	13,978	13,969	14,152	14,284
Other Assets	19,843	21,624	28,739	43,108	49,574	57,010
Total Assets	**1,125,826**	**1,374,310**	**1,613,434**	**1,904,771**	**2,182,211**	**2,554,542**

Asset Quality

(%)

GNPA (INR m)	10,581	14,688	19,205	33,829	40,089	45,357
NNPA (INR m)	4,424	7,238	9,382	22,242	23,959	22,421
GNPA Ratio	1.53	1.74	1.98	2.93	3.02	2.89
NNPA Ratio	0.65	0.87	0.98	1.95	1.83	1.45
PCR (Excl Tech. write off)	56.2	49.6	50.7	34.3	40.2	50.6
PCR (Incl Tech. Write off)	0.0	76.7	76.8	59.3	62.5	67.6

E: MOSL Estimates

Financials and Valuation

Ratios

Y/E March	2009	2010	2011	2012E	2013E	2014E
Spreads Analysis (%)						
Avg. Yield-Earning Assets	9.6	9.0	8.8	10.1	9.8	9.5
Avg. Yield on loans	10.6	10.0	10.0	11.6	11.1	10.6
Avg. Yield on Investments	8.2	7.7	7.1	7.4	7.3	7.3
Avg. Cost-Int. Bear. Liab.	7.5	6.5	5.9	7.4	7.1	6.8
Avg. Cost of Deposits	7.4	6.4	5.8	7.5	7.2	6.9
Interest Spread	2.1	2.5	3.0	2.7	2.7	2.7
Net Interest Margin	2.2	2.5	3.1	2.7	2.7	2.7
Profitability Ratios (%)						
RoE	14.8	16.5	17.1	11.3	12.0	12.1
RoA	0.9	0.9	1.0	0.7	0.7	0.7
Int. Expense/Int.Income	77.5	71.7	65.4	73.3	72.7	71.9
Fee Income/Net Income	19.2	18.9	17.2	19.3	18.7	18.4
Non Int. Inc./Net Income	34.9	29.2	18.7	22.5	22.3	21.7
Efficiency Ratios (%)						
Cost/Income*	53.5	45.8	37.4	42.3	42.8	42.4
Empl. Cost/Op. Exps.	54.7	57.6	55.4	55.7	54.7	53.0
Busi. per Empl. (INR m)	102.1	120.7	132.0	145.3	159.9	176.8
NP per Empl. (INR lac)	0.6	0.7	0.9	0.7	0.8	0.8
* ex treasury						
Asset-Liability Profile (%)						
Loans/Deposit Ratio	69.6	69.4	69.0	69.9	69.9	69.9
CASA Ratio	23.7	25.0	24.6	22.3	22.1	21.3
Investment/Deposit Ratio	29.0	29.8	30.3	29.6	29.6	29.6
G-Sec/Investment Ratio	88.0	91.9	87.2	87.8	84.4	84.4
Valuation						
Book Value (INR)	257.5	292.2	350.0	381.5	418.2	458.9
Price-BV (x)	1.0	0.9	0.7	0.7	0.6	0.6
Adjusted BV (INR)	246.1	273.4	329.1	331.9	364.8	408.9
Price-ABV (x)	1.0	0.9	0.8	0.8	0.7	0.6
EPS (INR)	36.1	45.3	51.5	41.1	48.0	53.0
Change (%)	7.7	25.3	13.7	-20.1	16.6	10.6
Price-Earnings (x)	7.1	5.7	5.0	6.2	5.3	4.8
Dividend Per Share (INR)	7.3	9.1	10.4	8.2	9.6	10.6
Dividend Yield (%)	2.9	3.6	4.1	3.2	3.7	4.1

E: MOSL Estimates

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The Economy Observer

the Corner Office
Interaction with the CEO

Wall of Worry?
the whistleblower series

Ground Reality

Expert Speak

The InSites
Takeaways from site visits

the PolicyMaker
Insights from bureaucrats

Travelog
the analyst's diary

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weekly

Dashboard
The Monthly Auto Update

TELE TALK TIME
Indian telecom monthly

GASOLINE
the oil & gas monthly

mPower
power utilities monthly

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