

BUY
TP: INR 400.00
▲ 22.0%

Bank of India

BOI IN

Operating performance to improve; risk-reward good

BOI's management, in our recent interaction, seemed confident on asset quality and improvement in operating performance in H2FY13. The bank is guiding for a sharp improvement in slippages and reduction in GNPLs in H2FY13. NIMs are also likely to improve from the low levels of 2.2%-2.4%, aided by improvement in slippages and C/D ratio. At current valuation of 0.8x FY14E BV, the stock is trading at a discount to peers, which will narrow on asset quality improvement. Upgrade to BUY; revised Mar'14 TP Rs 400.

- ➔ **Slippages likely to have peaked:** BOI's asset quality has remained volatile in the past 2-3 years, resulting in a de-rating of the stock. Slippages were high in H1FY13 at Rs 44.8bn (4.2% on an annualised basis); consequently, GNPLs/NNPLs rose from Rs 58.9bn/Rs 36.6bn (2.34%/1.5%) in Mar'12 to Rs 89bn/Rs 52bn (3.42%/2.04%) in Sep'12. However, incremental slippages in H2FY13 are likely to improve significantly. Recoveries have also remained healthy; hence GNPLs are likely to decline. Restructuring could remain high (H1FY13 restructuring at Rs 46bn).
- ➔ **NIMs likely to improve:** BOI's NIMs (down to ~2.3% in H1FY13 from 2.9% in FY11) have remained under pressure due to strain on asset quality. However, NIMs are likely to improve with lower slippages. Domestic C/D ratio is also low at 67% and improvement in C/D ratio would support NIMs.
- ➔ **Credit growth to pick up in Q4FY13:** Overall advances have grown by only 2% in H1FY13, whereas deposits have grown by 4.5%. However, the management expects advances to pick up in Q4FY13.
- ➔ **Improvement in asset quality and macro outlook key catalysts; upgrade to BUY:** BOI is currently trading at a 32% discount to its five year average P/one-year forward BV of 1.2x. At current valuations, the stock is also trading at a discount to large nationalised banks. Risk-reward is favourable in our view given likely improvement in asset quality, peaking of rates and likely pick-up in growth in FY14.

Financial Highlights

Y/E 31 Mar	FY11A	FY12A	FY13E	FY14E	FY15E
Net interest income (INR mln)	78,106	83,134	93,245	110,794	131,800
Net revenues (INR mln)	104,524	116,346	129,623	150,689	175,470
Pre-provision profits (INR mln)	53,842	66,939	73,722	86,402	101,540
Adj. PAT (INR mln)	24,887	26,775	29,842	38,053	44,843
Adj. EPS (INR)	45.5	46.6	51.9	66.2	78.1
ROE (%)	17.3	15.0	14.2	16.0	16.5
ROA (%)	0.8	0.7	0.7	0.8	0.8
Gross NPA (%)	2.2	2.3	3.4	3.4	3.4
Tier I ratio (%)	8.3	8.7	8.2	7.9	7.6
P/BV (x)	1.6	1.1	0.8	0.7	0.7
P/E (x)	10.5	7.8	6.3	5.0	4.2

Source: Company, Bloomberg, RCML Research

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PRICE CLOSE (19 Dec 12)

INR 327.95

MARKET CAP

INR 188,414 mln
USD 3,453 mln

SHARES O/S

574.5 mln

FREE FLOAT

37.3%

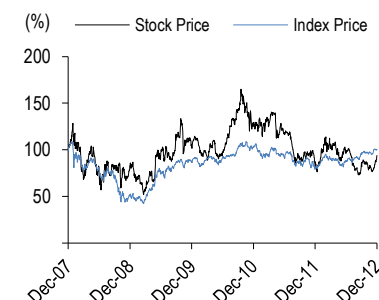
3M AVG DAILY VOLUME./VALUE

1.0 mln/ USD 5.7 mln

52 WK HIGH

INR 396.90

52 WK LOW

INR 255.00


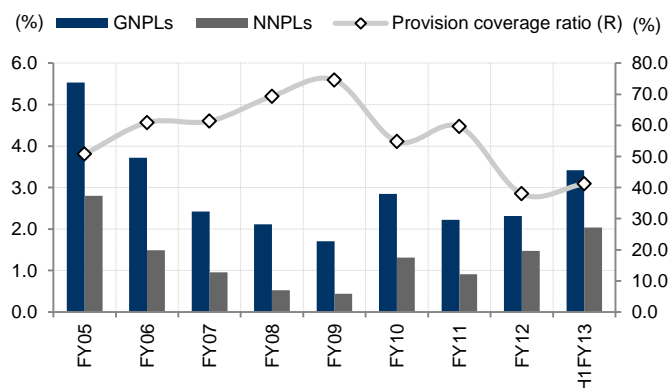


Asset quality likely to improve in H2FY13

BOI's asset quality has remained volatile in the past few years, which, we believe, is the key reason for a de-rating in the stock. Total slippages increased from average 1.5% over FY05-FY08 to 2.6% in FY09-FY10. Slippages declined to 1.7% in FY11 but again increased to 2.5% in FY12 due to slowdown in economy and migration to system-based recognition in NPLs. Slippages have remained high in H1FY13, also at ~4.2% of advances on an annualised basis. Provision coverage ratio too declined from a healthy 75% in Mar'09 to 38% in Mar'12 and 41% in Sep'12.

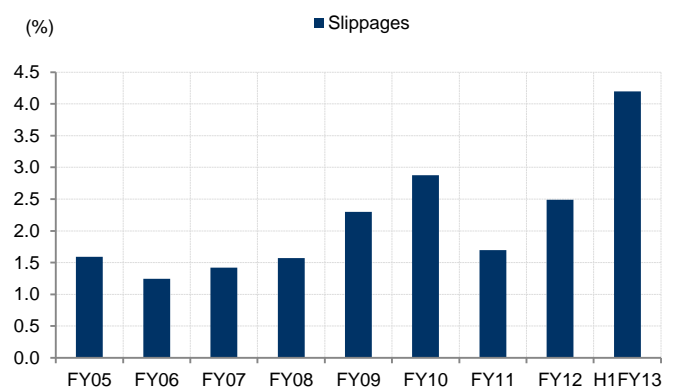
Asset quality volatile; slippages dipped in FY11 but again rose in FY12 on slowdown in economy and migration to system-based recognition in NPLs

Fig 1 - Asset quality and PCR have deteriorated



Source: Company, RCML Research

Fig 2 - Slippages have increased in the past 18 months



Source: Company, RCML Research

Asset quality performance has remained volatile on a quarterly basis also. Total slippages were very high at Rs 45bn in H1FY12, but declined to ~Rs 9bn in H2FY12. However, slippages again increased to Rs 44.8bn in H1FY13 due to pressure on the corporate and SME segments.

Fig 3 - Asset quality trend – Quarterly

(Rs mn)	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
Movement of NPLs										
Opening GNPLs	48,826	47,946	48,696	45,421	48,116	57,911	65,481	63,866	58,940	67,518
Additions	6,180	8,184	4,765	9,993	16,837	28,217	5,196	3,770	17,470	27,334
Reductions	7,060	7,434	8,040	7,298	7,042	20,647	6,811	8,696	9,173	5,866
- Write-offs/Others	2,555	4,430	-145	3,661	3,469	16,209	2,822	NA	3,352	97
Closing	47,946	48,696	45,421	48,116	57,911	65,481	63,866	58,940	67,237	88,986
Slippages (% annu.)	1.67	2.18	1.21	2.37	3.81	6.22	1.08	0.71	3.25	5.1
GNPLs	47,945	48,696	45,421	48,116	57,910	65,481	63,860	58,940	67,518	88,986
GNPLs (%)	2.70%	2.60%	2.40%	2.20%	2.70%	3.00%	2.70%	2.30%	2.60%	3.40%
NNPLs	20,612	20,704	16,603	19,450	26,897	42,446	40,931	36,564	44,134	52,283
NNPLs (%)	1.20%	1.10%	0.90%	0.90%	1.30%	2.00%	1.80%	1.50%	1.70%	2.00%

Source: Company, RCML Research

BOI's management, in our recent interaction, indicated that slippages have likely peaked in H1FY13. It expects asset quality to improve considerably in H2FY13 with significant dip in slippages and healthy recoveries. Consequently, GNPLs could decline in absolute terms in H2FY13.

We also note that the Indian government has recently taken many steps to improve investor sentiments in certain stressed sector (like Power, infrastructure) and to restore the growth momentum of economy. With core inflation below its target rate of 5%, the



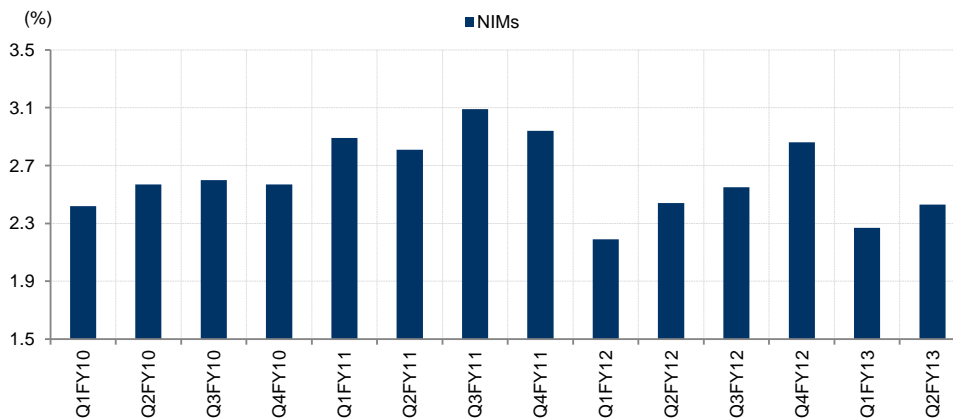
RBI, in its recent mid-quarter monetary policy, has indicated that the focus of monetary policy will now shift to growth. Our economist expects policy rate cuts of 100bps+ in the next 12 months. We believe PSU banks, including BOI, would be among the biggest beneficiary of a pick-up in GDP growth, reduction in stress in some sectors like power and lower rates given their high exposure to corporate and SME segments.

NIMs likely to improve in H2FY13

NIMs have been under pressure in the past few quarters. Overall NIMs have come down from 2.9%-3.1% levels in FY11 to 2.3%-2.4% in H1FY13. This was driven by higher slippages and restructuring. However, the management is guiding for improvement in NIMs to 2.6%-2.8%. Domestic C/D ratio is currently low at 67% and the management expects an improvement in C/D ratio going forward. Improvement in asset quality will also support NIMs in the near term.

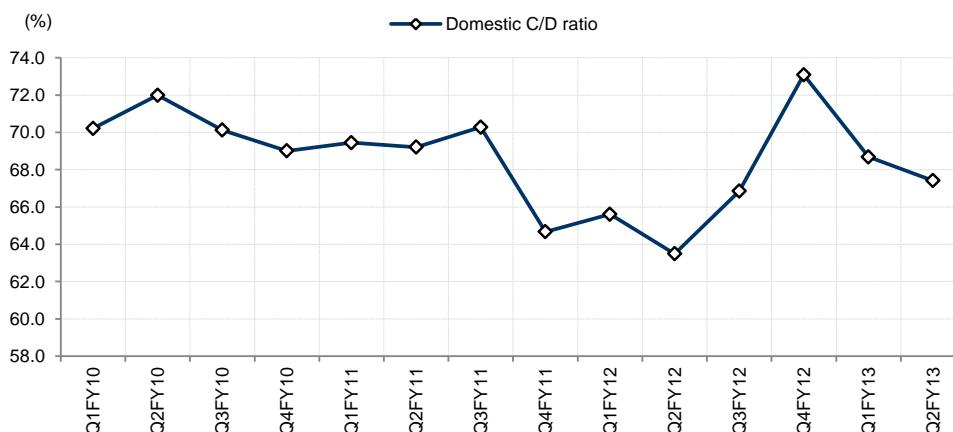
Management is guiding for an improvement in NIMs to 2.6%-2.8%. Improvement in asset quality to also support NIMs near term

Fig 4 - NIMs lower than historical average



Source: Company, RCML Research

Fig 5 - C/D ratio low at 67%



Source: Company, RCML Research

Risk-reward favourable due to attractive valuations and likely improvement in core operating performance

BOI's ROAs/ROEs has declined from an average 1.2%/26% over FY07-FY09 to 0.7%/15.5% in FY10-FY12 due to pressure on NIMs and asset quality. Profitability remained under pressure in H1FY13 also due to higher NPL provisions and decline in NIMs. However, we expect operating performance to bottom in FY13 and ROAs/ROEs to improve from FY14, driven by pick-up in GDP growth.

Expect operating performance to bottom in FY13; ROAs/ROEs to improve from FY14, led by pick-up in GDP growth

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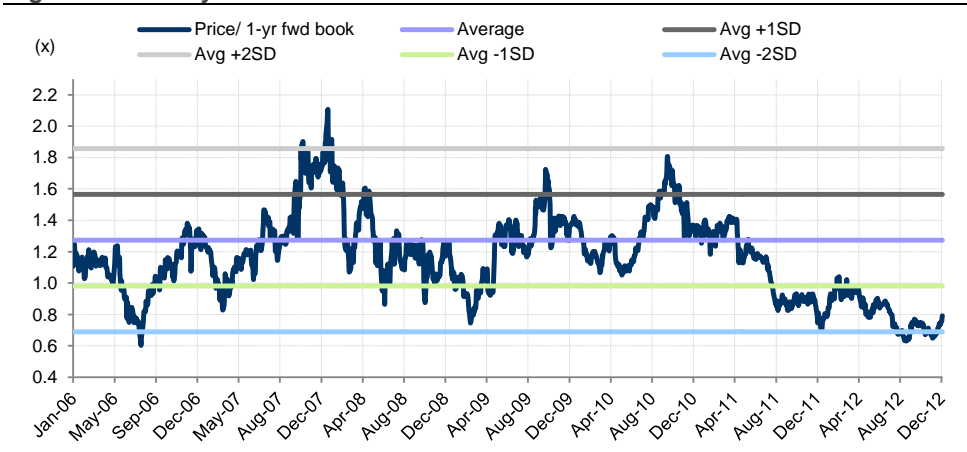
Company Update

INDIA

FINANCIALS

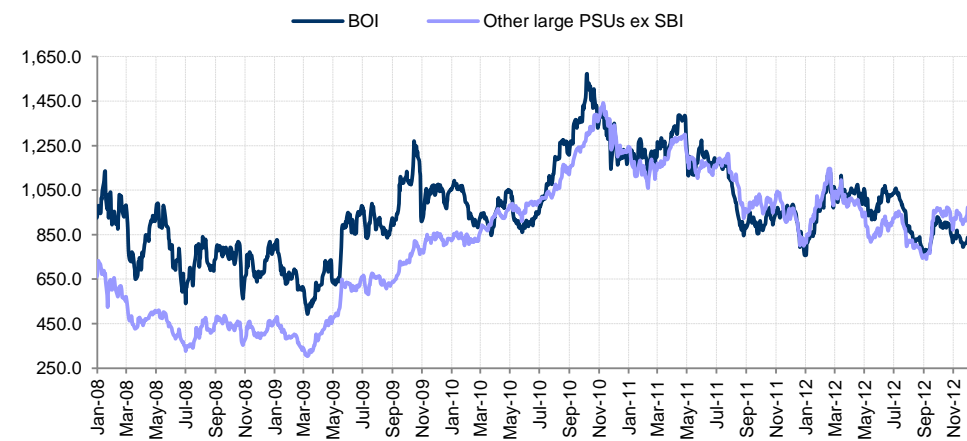
Despite the sharp run-up in the past three months, valuations are still attractive at 0.8x FY14E BV. We note that at current valuations, BOI is still trading at a 32% discount to its five year average P/one-year forward BV multiple of 1.2x. The bank is also trading at a discount to other large nationalised banks despite similar liability franchise. Given attractive valuations and likely improvement in core operating performance, we expect discount to its historical averages to decline in the coming quarters. We upgrade the stock to BUY from HOLD and raise our TP to Rs 400/share. At our TP, the stock would continue to trade at an attractive valuation of 0.9x FY14E BV (1.1x FY14E ABV) and 6.0x FY14E EPS.

Fig 6 - BOI: One-year forward P/BV



Source: RCML Research

Fig 7 - BOI vs. other large PSUs* (ex-SBI): price performance (Index: 1-Apr-03= 100)



Source: RCML Research *include Punjab National Bank, Bank of Baroda, Canara Bank and Union Bank of India

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Fig 1 - RCML Financials coverage universe: Valuation snapshot

Bloomberg Code	CMP (Rs)	Target (Rs)	Reco	MCAP (Rs bn)	P/BV (x)		P/E (x)		EPS growth (%)	Average RoE (%)	Average RoA (%)	CASA (%)
					FY13E	FY14E	FY13E	FY14E	FY12-14E	FY12-14E	FY12-14E	FY12
PSU Banks												
SBIN IN	2,372	2,540	BUY	1,592	1.7	1.5	11.3	9.6	19.0	16.0	1.0	44.8
SBI #	1,836	2,004		1,232	1.4	1.2	9.1	7.7	19.2	16.6	0.9	44.8
PNB IN	851	825	Hold	289	1.0	0.8	6.1	4.9	10.0	18.7	1.0	35.3
BOB IN	861	900	BUY	337	1.2	1.0	7.0	6.0	8.9	19.3	1.1	26.9
BOI IN	328	400	BUY	188	0.8	0.7	6.3	5.0	19.2	15.1	0.7	26.7
CBK IN	476	440	HOLD	211	0.9	0.8	5.9	5.0	13.4	16.6	0.9	24.3
DBNK IN	118	135	BUY	41	0.8	0.7	4.3	3.8	16.3	20.7	1.0	34.6
UNBK IN	270	260	BUY	149	1.0	0.9	6.6	5.4	23.8	16.1	0.8	31.3
OBC IN	345	390	BUY	101	0.8	0.7	6.7	5.1	31.0	12.8	0.8	24.1
Private Banks												
ICICIB IN	1,139	1,125	HOLD	1,309	2.0	1.8	16.2	13.9	21.0	12.6	1.6	43.5
ICICI#	924	910		1,062	2.0	1.8	14.3	12.2	21.3	14.6	1.5	43.5
HDFCB IN	688	670	HOLD	1,628	4.6	3.9	24.1	19.3	27.3	20.4	1.8	48.4
AXSB IN	1,335	1,025	HOLD	570	2.1	1.8	11.3	9.7	15.6	19.8	1.6	41.5
YES IN	470	475	BUY	168	2.9	2.2	13.3	11.5	21.2	23.1	1.5	15.0
IIB IN	434	425	BUY	226	3.1	2.7	21.5	17.2	21.1	18.0	1.6	27.3
NBFCs												
HDFC IN	831	775	BUY	1,280	5.1	4.6	25.8	22.5	15.0	22.4	2.8	
HDFC #	599	543		923	5.5	4.7	19.7	17.2	17.8	33.4	2.8	
LICHF IN	288	300	BUY	145	2.2	1.9	13.1	10.4	23.5	18.8	1.6	
DEWH IN	183	340	BUY	21	0.9	0.8	6.3	5.1	17.7	16.0	1.4	
SHTF IN	766	650	BUY	174	2.4	2.0	12.3	10.4	15.3	21.9	3.6	
POWF IN	204	195	HOLD	269	1.1	1.0	6.7	6.7	14.7	17.6	2.7	
RECL IN	248	200	SELL	245	1.5	1.3	7.0	7.0	11.5	22.1	3.0	
MGFL IN	36	39	HOLD	30	1.1	0.9	5.9	5.4	(2.8)	21.9	4.5	
MMFS IN	1,096	950	BUY	125	2.8	2.4	15.7	12.7	18.4	21.7	3.7	
SCUF IN	871	900	BUY	46	2.1	1.8	10.6	9.1	20.9	22.6	3.8	
BAF IN	1,300	1450	BUY	54	2.0	1.7	12.1	9.7	16.7	21.1	3.6	

Source: RCML Research, Bloomberg # Adj. for subsidiaries



Per Share Data

Y/E 31 Mar (INR)	FY11A	FY12A	FY13E	FY14E	FY15E
Reported EPS	45.5	46.6	51.9	66.2	78.1
Adjusted EPS	45.5	46.6	51.9	66.2	78.1
DPS	7.0	7.0	8.0	10.2	12.0
Book value	291.9	343.3	385.9	440.3	504.3
Adjusted book value	266.6	295.7	307.4	355.0	408.9

Valuation Ratios

Y/E 31 Mar (x)	FY11A	FY12A	FY13E	FY14E	FY15E
P/E	10.5	7.8	6.3	5.0	4.2
P/BV	1.6	1.1	0.8	0.7	0.7
P/ABV	1.8	1.2	1.1	0.9	0.8

Financial Ratios

Y/E 31 Mar (%)	FY11A	FY12A	FY13E	FY14E	FY15E
Spread Analysis					
Yield on advances	8.1	8.8	8.6	8.5	8.5
Yield on investments	6.8	8.3	8.2	8.2	8.2
Cost of funds	4.9	6.0	6.0	5.9	5.9
NIMs	2.6	2.4	2.3	2.3	2.3
Operating Ratios					
Operating cost to income	48.5	42.5	43.1	42.7	42.1
Operating expenses / Avg assets	1.6	1.3	1.3	1.3	1.3
Proportion of CASA deposits	25.4	26.7	25.5	25.5	25.5
Non-int inc / Total income	25.3	28.5	28.1	26.5	24.9
Credit / Deposit ratio	71.3	78.2	78.7	78.7	78.7
Investment / Deposit	28.7	27.3	26.8	26.7	26.9
Asset Quality and Capital					
Gross NPA	2.2	2.3	3.4	3.4	3.4
Net NPA	0.9	1.5	2.0	2.0	1.9
Coverage ratio	59.6	38.0	41.1	42.1	44.9
CAR	12.2	12.0	11.8	11.5	11.2
Tier I ratio	8.3	8.7	8.2	7.9	7.6
Growth Ratios					
Net interest income	35.7	6.4	12.2	18.8	19.0
Non-interest income	1.0	25.7	9.5	9.7	9.5
Non-interest income (ex-treasury)	14.7	25.5	12.9	10.4	10.4
Pre-provisioning profit	14.4	24.3	10.1	17.2	17.5
Net profit	42.9	7.6	11.5	27.5	17.8
Assets	27.9	9.6	17.6	17.4	17.4
Advances	26.5	16.8	19.0	18.0	18.0
Deposits	30.1	6.5	18.3	18.0	18.0
Book value	19.9	17.6	12.4	14.1	14.5
EPS	37.4	2.5	11.5	27.5	17.8

DuPont Analysis

Y/E 31 Mar (%)	FY11A	FY12A	FY13E	FY14E	FY15E
Net interest income / Assets	2.5	2.3	2.2	2.3	2.3
Non-interest income / Assets	0.8	0.9	0.9	0.8	0.8
Operating expenses / Assets	1.6	1.3	1.3	1.3	1.3
Provisions / Assets	0.6	0.9	0.8	0.7	0.7
Taxes / Assets	0.3	0.2	0.2	0.3	0.3
ROA	0.8	0.7	0.7	0.8	0.8
Equity / Assets	4.6	4.9	5.0	4.8	4.7
ROAE	17.3	15.0	14.2	16.0	16.5



Profit and Loss Statement

Y/E 31 Mar (INR mln)	FY11A	FY12A	FY13E	FY14E	FY15E
Interest income	217,517	284,807	323,108	378,998	446,404
Interest expense	(139,411)	(201,673)	(229,862)	(268,204)	(314,603)
Net interest income	78,106	83,134	93,245	110,794	131,800
Non-interest income	26,418	33,212	36,378	39,895	43,670
Non-interest income (ex-treasury)	23,199	29,124	32,878	36,295	40,070
Net revenue	104,524	116,346	129,623	150,689	175,470
Operating expenses	(50,682)	(49,407)	(55,902)	(64,287)	(73,930)
Pre-provision profits	53,842	66,939	73,722	86,402	101,540
Provisions & contingencies	(18,888)	(31,164)	(33,665)	(32,041)	(37,480)
PBT	34,953	35,775	40,056	54,361	64,061
Extraordinaries	0	0	0	0	0
Income tax	(10,067)	(9,000)	(10,214)	(16,308)	(19,218)
Reported PAT	24,887	26,775	29,842	38,053	44,843
Adj. net profit	24,887	26,775	29,842	38,053	44,843

Balance Sheet

Y/E 31 Mar (INR mln)	FY11A	FY12A	FY13E	FY14E	FY15E
Cash in hand & bal with RBI	217,824	149,867	175,345	205,153	230,797
Bal with banks, money at call	155,276	197,245	230,777	270,009	303,760
Investments	858,724	867,536	1,008,608	1,186,829	1,409,858
Advances	2,130,962	2,488,333	2,961,117	3,494,118	4,123,059
Fixed assets (net)	24,807	27,716	28,409	29,119	31,303
Other assets	110,938	102,298	105,164	108,103	117,137
Total Assets	3,498,531	3,832,996	4,509,419	5,293,331	6,215,915
Equity capital	5,472	5,745	5,745	5,745	5,745
Reserves & surplus	154,240	191,514	215,984	247,187	283,958
Net worth (ex-pref capital)	159,712	197,259	221,729	252,933	289,704
Preference capital	0	0	0	0	0
Deposits	2,988,858	3,182,160	3,762,905	4,440,227	5,239,468
- CASA deposits	759,676	848,056	959,541	1,132,258	1,336,064
- Term deposits	2,229,182	2,334,105	2,803,364	3,307,969	3,903,404
Borrowings (+sub-ord bonds)	220,214	321,142	379,108	439,925	510,473
Other liabilities & provisions	129,747	132,434	145,678	160,245	176,270
Total Equity & Liabilities	3,498,531	3,832,996	4,509,419	5,293,331	6,215,915

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Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Expected absolute returns are based on the share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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