

November 15, 2016

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Rating	Accumulate
Price	Rs161
Target Price	Rs170
Implied Upside	5.6%
Sensex	26,819
Nifty	8,296

(Prices as on November 11, 2016)

Trading data

Market Cap. (Rs bn)	371.3
Shares o/s (m)	2,310.5
3M Avg. Daily value (Rs m)	1468.2

Major shareholders

Promoters	59.24%
Foreign	12.35%
Domestic Inst.	21.63%
Public & Other	6.78%

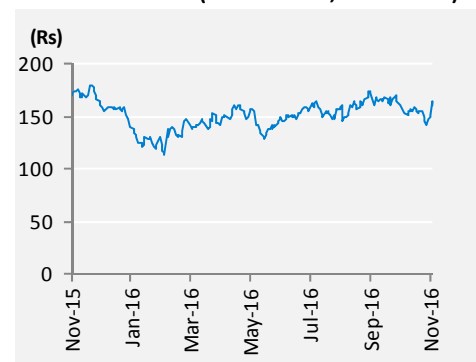
Stock Performance

(%)	1M	6M	12M
Absolute	(0.8)	2.5	(7.5)
Relative	3.7	(2.3)	(11.2)

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2017	9.0	10.4	-14.1
2018	15.0	17.4	-14.1

Price Performance (RIC: BOB.BO, BB: BOB IN)



Source: Bloomberg

BOB reported PAT of Rs5.52bn (PLe: Rs5.12bn) which was in-line with expectations. Earnings were supported by better NII growth, robust other income and lower provisions from lower slippages. Lower fresh slippages of Rs22.5bn came as a surprise with better upgrade/recovery keeping asset quality stable. It maintained its asset quality guidance for Rs150bn of slippages and GNPA of Rs450-500bn (Rs430bn as at Q2FY17) for FY17E. The management is extremely confident on where they stand on the slippages as well as asset quality and hence have seen an overall improvement in the total stressed assets ie (SMA1+SMA2+Standard Restructured+GNPA). In addition, while the overall business has been run down in 1HFY17, we expect improvement to be seen in 2HFY17 and a significant improvement in growth to return in FY18 thereby where many initiatives set in to accrue on business growth and profitability in FY18, which will help it regain better return ratios as well as old glory. We have adjusted our estimates to factor in lower business growth & increased credit cost. We have adjusted our Net NPAs in ABV to 70% (from 100%). We upgrade to Accumulate with increased PT of Rs171 (from Rs137) based on 1.4x Mar-18 ABV.

- **Better NII & lower provisions help earnings:** Though bank's business de-grew, NII growth was better at 6% YoY as bank got benefit of CoF in domestic business & yield benefit in overseas biz. As a result, margins improved by 6bps QoQ to 2.29%. Bank expects margins to improve further to 2.5% from both yield improvement and lower CoF. Earnings were in-line as provisions were lower on decline in slippages and robust other income boosted by treasury gains.

Contd...2

Key financials (Y/e March)	2015	2016	2017E	2018E
Net interest income	131,872	127,398	133,863	141,052
Growth (%)	10.2	(3.4)	5.1	5.4
Operating profit	99,151	88,156	95,321	99,434
PAT	33,984	(53,955)	20,721	34,569
EPS (Rs)	15.5	(23.8)	9.0	15.0
Growth (%)	(27.0)	(253.3)	(137.6)	66.8
Net DPS (Rs)	3.8	—	1.8	3.0

Profitability & Valuation	2015	2016	2017E	2018E
NIM (%)	1.92	1.84	1.97	1.96
RoAE (%)	9.0	(13.5)	5.1	8.0
RoAA (%)	0.49	(0.78)	0.30	0.48
P / BV (x)	0.9	1.0	1.0	0.9
P / ABV (x)	1.1	1.7	1.6	1.3
PE (x)	10.3	(6.7)	17.9	10.7
Net dividend yield (%)	2.4	—	1.1	1.9

Source: Company Data; PL Research

- **Consolidation continues in biz growth:** Bank continued to consolidate its business both in domestic & overseas as it continues to focus on profitable growth & better margins and work on being a sole banker esp. in mid-corporate. In Q2FY17, the average loan book de-grew by 7.4% YoY and bank expects some more calibration to continue in ensuing quarter, but has a healthy sanction pipeline. Despite a reduction in average Rs300bn in credit and an additional Rs200bn shifting to NPAs, the NII growth was commendable. On liabilities side, bank's average CASA continued to be on track mainly from SA growth (grew 14% YoY), while demonetisation move is expected to help to some extent.
- **Lower slippage & recovery/upgrade keeps asset quality stable:** Slippages came off to Rs22.5 v/s Rs55.3bn in Q1FY17, while better recovery/upgrades of Rs26bn v/s Rs24bn helped retain stable asset quality. Bank improved its PCR to 63% from 60% with view of improving further towards 65%. It has also seen its SMA-2 level improve by Rs40-50bn to Rs125.7bn indicating lowering stress.

Exhibit 1: Q2FY17 Financials – Better performance with stable asset quality

P&L (Rs m)	Q2FY17	Q2FY16	YoY gr. (%)	Q1FY17	QoQ gr. (%)
Interest Income	1,04,852	1,11,564	(6.0)	1,04,335	0.5
Interest Expense	70,591	79,119	(10.8)	70,624	(0.0)
Net Interest Income (NII)	34,261	32,445	5.6	33,711	1.6
- Treasury income	5,460	2,241	143.6	5,570	(2.0)
Other income	15,614	11,440	36.5	14,444	8.1
Total income	49,875	43,885	13.6	48,155	3.6
Operating expenses	22,973	20,515	12.0	21,460	7.1
-Staff expenses	11,685	10,440	11.9	11,081	5.4
-Other expenses	11,288	10,075	12.0	10,379	8.8
Operating profit	26,902	23,370	15.1	26,695	0.8
Core operating profit	18,712	18,601	0.6	18,485	1.2
Total provisions	17,958	18,917	(5.1)	20,041	(10.4)
Profit before tax	8,944	4,453	NA	6,654	34.4
Tax	3,422	3,208	6.7	2,418	41.5
Profit after tax	5,521	1,245	NA	4,236	30
Balance sheet (Rs m)					
Deposits	56,75,312	61,24,578	(7.3)	56,21,737	1.0
Advances	35,41,496	41,48,998	(14.6)	36,27,664	(2.4)
Profitability ratios					
RoaA	0.3	0.1	26	0.3	8
RoaE	5.4	5.0	41	6.5	(111)
NIM	2.3	2.1	21	2.2	6
Yield on Advances	7.3	7.6	(35)	7.2	3
Cost of Deposits	4.8	5.1	(26)	4.7	11
Asset Quality					
Gross NPA (Rs m)	4,29,493	2,37,103	81.1	4,29,917	(0.1)
Net NPA (Rs m)	1,93,420	1,27,978	51.1	2,07,838	(6.9)
Gross NPL ratio	11.4	5.6	579	11.2	20
Net NPL ratio	5.5	3.1	238	5.7	(27)
Coverage ratio	55.0	46.0	894	51.7	331
O/S Std. restr. assets (Rs m)	1,38,600	2,29,300	(39.6)	1,41,640	(2.1)
Std. rest. Assets/ Total	3.9	5.5	(161)	3.9	1
Business & Other Ratios					
Low-cost deposit mix	34.2	32.0	228	33.8	40
Cost-income ratio	46.1	46.7	(69)	44.6	150
Non int. inc / total income	31.3	26.1	524	30.0	131
Credit deposit ratio	62.4	67.7	(534)	64.5	(213)
CAR	12.9	12.5	43	13.1	(13)
Tier-I	10.6	9.9	67	10.7	(11)

Source: Company Data, PL Research

Key Q2FY17 Analyst Meet Highlights

Business growth & outlook -

- **Loan Outlook** – The management has made conscious efforts in making a shift from the normal PSUs banks way of dealing with customers in CAGs to more relationship oriented business focus for corporates, while still improving the working on the small ticket SME & Retail. Expects some more calibration in business which can restrict loans growth in FY17.
- **International business** – Overseas lending declined by 8% QoQ as bank has been shedding low yielding buyer's credit and enhancing high yielding local credit. Bank will be consolidating the overseas lending portfolio.
- **Liabilities** – Daily average CASA has been on track to achieve 35% (34% currently) on back of strong SA growth. Bank has been shedding bulk deposits and now has only Rs27bn which will be shed in the Q3FY17.
- **Demonetization of currency** – Bank has received Rs115bn as deposits of which Rs22.0bn were as exchange, while Rs95bn were in form of CASA (Rs25bn CA & Rs70bn SA) which is 7-7.5% of domestic CASA deposit base. While BOB has a 4% market share, expects to improve the wallet share in this to 5%.

Margins/Opex

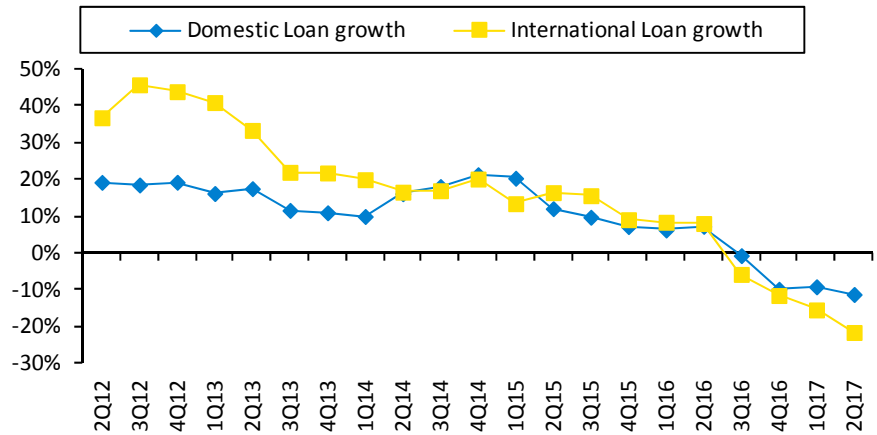
- Margins improved mainly from domestic side on lower slippages, with international margins being stable. Bank expects domestic margins to improve to 3% (from 2.8%) , while they aspire to take international margins to 1-1.5% from the current 0.98%.
- Bank has covered most of the pension liability and has increased run rate of Rs800mn on existing pension on back of lower yields.

Asset quality -

- **Slippages** – Bank's slippages declined sharply to Rs29bn v/s Rs60bn in Q1FY17 mainly in granular accounts. In 1QFY17, there were increased slippages from smaller accounts where there have been recoveries too in the current quarter.
- **Upgrades/Recoveries** – Bank has been seeing good upgrade/recoveries (Rs50bn in H1FY17) which were mostly from granular accounts from where BOB is consortium leader/main banker.
- Bank has systematically increasing the PCR and target its PCR towards 65% (63% currently incl. technical w.off).
- **Outlook** – Bank continued to maintain its guidance of Rs150bn of slippages (~Rs80bn in H1FY17), while upgrade/recovery of ~Rs100bn (Rs50bn in H1FY17) which could take GNPA's will be in range of Rs450bn - Rs500bn by FY17 end. But

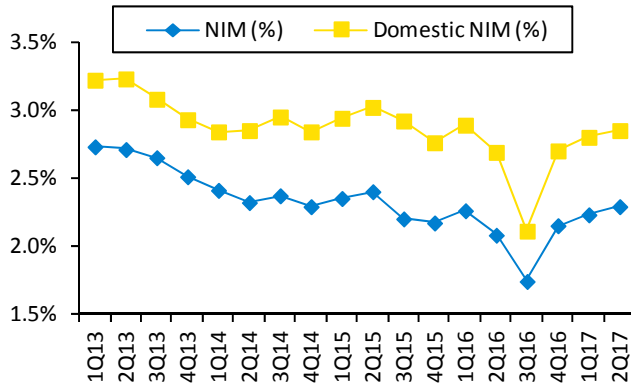
bank targets 2% Net NPAs by FY2019 (from 5.5% currently), which effectively means a significant improvement in asset quality going forward.

Exhibit 2: Business continues to de-grow as BOB is judiciously rationalizing



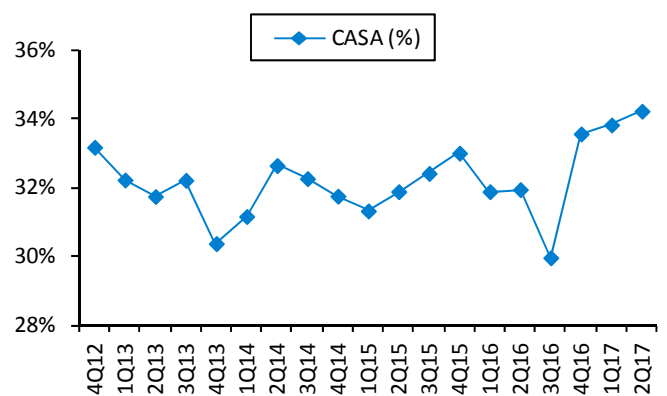
Source: Company Data, PL Research

Exhibit 3: Margins improve on back improved CoF and better yields in Overseas business



Source: Company Data, PL Research

Exhibit 4: CASA mix has been improving further at ~34% on back of SA growth



Source: Company Data, PL Research

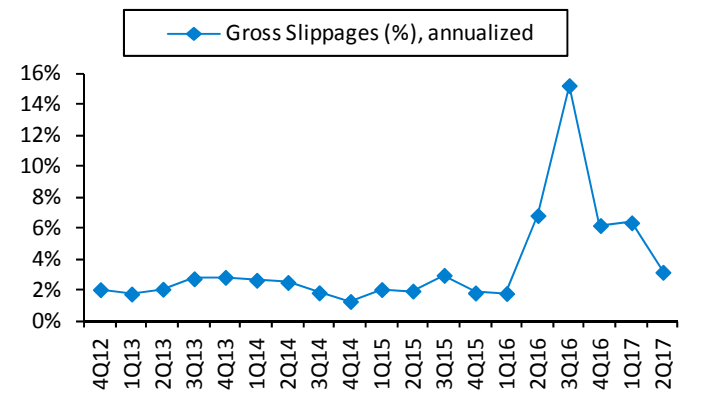
Exhibit 5: Stressed book remained stable with slippages dropping down to normalized levels

	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17
Opening NPAs	118,759	120,868	132,685	154,530	162,522	172,740	237,099	3,89,339	405,239	429,904
Gross Slippages	20,221	17,570	30,420	17,893	19,079	69,623	157,850	59,320	60,960	28,610
Recovery	5,626	2,780	2,380	10,291	3,002	3,344	3,110	14,340	10,810	16,530
Up-gradations	7,412	2,350	1,800	6,753	5,265	793	140	17,660	14,010	10,340
Write offs	5,073	3,680	3,280	3,538	686	1,122	2,360	11,420	11,430	2,160
Closing	120,868	130,576	154,530	162,522	172,740	237,103	389,339	405,239	429,904	429,484
Annualized Slippages %	2.08%	1.83%	3.15%	1.82%	1.78%	6.37%	15.0%	5.24%	5.76%	2.48%

Restructuring Incremental	9,860	11,750	15,980	40,830	1,470	1,149	2,503	3,980	-	-
O/s Standard Restructured	228,320	224,170	230,988	259,050	255,411	229,300	171,350	137,350	141,640	138,600
% of loans	6.0%	5.8%	5.9%	6.1%	6.3%	5.5%	4.5%	3.6%	3.9%	3.9%

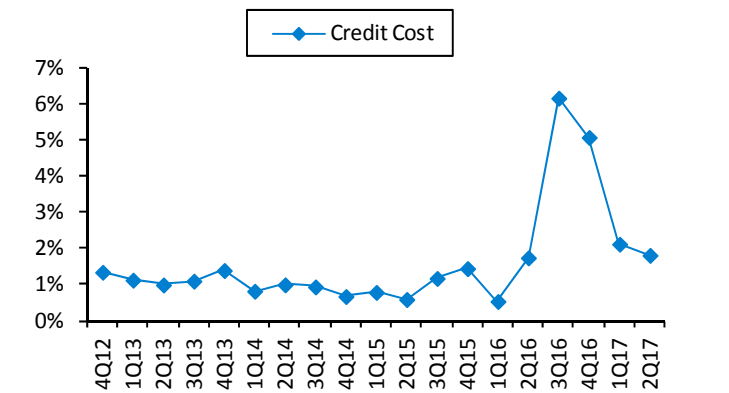
Source: Company Data, PL Research

Exhibit 6: Fresh slippages rate have been coming off to normalized levels



Source: Company Data, PL Research

Exhibit 7: Credit cost was flat but will remain at similar levels as bank wants to increase PCR



Source: Company Data, PL Research

Exhibit 8: Return ratios to start improving on better margins and lower provisions in FY18

ROAE decomposition	2011	2012	2013	2014	2015	2016	2017E	2018E
Net Interest Income/Assets	2.83%	2.63%	2.33%	2.03%	1.96%	1.91%	2.08%	2.08%
Fees/Assets	0.76%	0.72%	0.62%	0.63%	0.51%	0.57%	0.62%	0.75%
Investment profits/Assets	0.14%	0.15%	0.13%	0.13%	0.15%	0.18%	0.26%	0.21%
Net revenues/Assets	3.74%	3.50%	3.08%	2.79%	2.62%	2.66%	2.95%	3.04%
Operating Expense/Assets	-1.49%	-1.31%	-1.23%	-1.20%	-1.14%	-1.34%	-1.47%	-1.57%
Provisions/Assets	-0.43%	-0.65%	-0.86%	-0.65%	-0.67%	-2.33%	-1.01%	-0.75%
Taxes/Assets	-0.45%	-0.26%	-0.07%	-0.16%	-0.30%	0.20%	-0.15%	-0.21%
Total Costs/Assets	-2.37%	-2.23%	-2.16%	-2.02%	-2.11%	-2.15%	-1.15%	-1.06%
ROAA	1.36%	1.28%	0.92%	0.77%	0.51%	-0.81%	0.32%	0.51%
Equity/Assets	5.40%	5.87%	5.90%	5.66%	5.65%	6.01%	6.36%	6.37%
ROAE	25.3%	21.7%	15.7%	13.6%	9.2%	-14.4%	5.6%	8.9%

Source: Company Data, PL Research

Exhibit 9: Earnings change table - We have tweaked our earnings to factor in higher credit costs and ABVPS increases as we factor in lower NPAs due to stable economic scenario

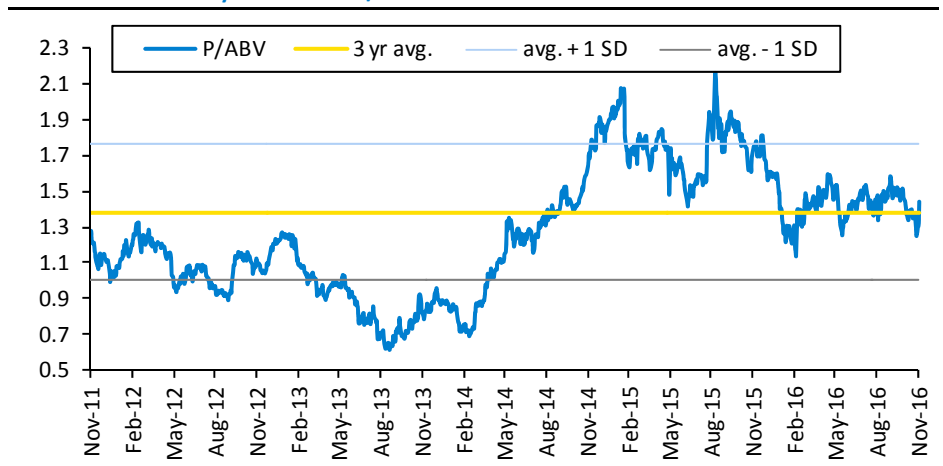
(Rs m)	Old		Revised		% Change	
	FY17E	FY18E	FY17E	FY18E	FY17E	FY18E
Net interest income	1,34,570	1,49,748	1,33,863	1,41,052	(0.5)	(5.8)
Operating profit	94,071	1,06,675	95,321	99,434	1.3	(6.8)
Net profit	28,353	50,416	20,721	34,569	(26.9)	(31.4)
EPS (Rs)	12.3	21.8	9.0	15.0	(26.9)	(31.4)
ABVPS (Rs)	68.5	96.4	100.3	123.7	46.3	28.3
Price target (Rs)	137		171		24.5	
Recommendation	REDUCE		ACCUMULATE			

Source: Company Data, PL Research

Exhibit 10: We increase our TP to Rs171 (from Rs137) based on 1.4x Mar-18 ABV.

PT calculation and upside	
Fair price - EVA	170
Fair price - Two stage GGM	171
Average of the two	171
Target P/ABV	1.4
Target P/E	11.4
Current price, Rs	161
Upside (%)	6%
Dividend yield (%)	1%
Total return (%)	7%

Source: Company Data, PL Research

Exhibit 11: BOB one year forward P/ABV historical trends


Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2015	2016	2017E	2018E
Int. Earned from Adv.	308,027	297,962	284,949	290,138
Int. Earned from Inv.	94,310	106,732	110,975	118,446
Others	27,299	35,918	26,141	26,129
Total Interest Income	429,636	440,613	422,065	434,713
Interest expense	297,763	313,214	288,203	293,661
NII	131,872	127,398	133,863	141,052
Growth (%)	10.2	(3.4)	5.1	5.4
Treasury Income	10,070	11,790	16,506	14,030
NTNII	33,950	38,199	39,981	50,930
Non Interest Income	44,020	49,989	56,487	64,960
Total Income	473,655	490,601	478,552	499,673
Growth (%)	9.1	3.6	(2.5)	4.4
Operating Expense	76,741	89,231	95,029	106,578
Operating Profit	99,151	88,156	95,321	99,434
Growth (%)	6.7	(11.1)	8.1	4.3
NPA Provisions	37,859	137,660	64,589	49,010
Investment Provisions	(1,494)	3,410	682	136
Total Provisions	44,945	155,137	64,848	50,745
PBT	54,206	(66,981)	30,472	48,689
Tax Provisions	20,222	(13,025)	9,751	14,120
Effective Tax Rate (%)	37.3	19.4	32.0	29.0
PAT	33,984	(53,955)	20,721	34,569
Growth (%)	(25.2)	(258.8)	(138.4)	66.8

Balance Sheet (Rs m)

Y/e March	2015	2016	2017E	2018E
Par Value	2	2	2	2
No. of equity shares	2,218	2,310	2,310	2,310
Equity	4,436	4,621	4,621	4,621
Networth	398,353	401,990	417,720	444,249
Adj. Networth	317,659	207,925	210,841	276,976
Deposits	6,175,595	5,740,379	5,855,186	6,323,601
Growth (%)	8.6	(7.0)	2.0	8.0
Low Cost deposits	1,629,689	1,513,345	1,598,466	1,751,638
% of total deposits	26.4	26.4	27.3	27.7
Total Liabilities	7,149,885	6,713,765	6,892,211	7,481,719
Net Advances	4,280,651	3,837,702	3,760,948	4,080,628
Growth (%)	7.8	(10.3)	(2.0)	8.5
Investments	1,168,122	1,204,505	1,352,166	1,471,807
Total Assets	7,149,885	6,713,765	6,892,211	7,481,719

Source: Company Data, PL Research.

Quarterly Financials (Rs m)

Y/e March	Q3FY16	Q4FY16	Q1FY17	Q2FY17
Interest Income	106,140	110,144	104,335	104,852
Interest Expense	79,087	76,840	70,624	70,591
Net Interest Income	27,053	33,304	33,711	34,261
Non Interest Income	11,129	17,747	14,444	15,614
CEB	5,800	9,350	6,030	6,450
Treasury	2,410	4,810	2,640	2,730
Net Total Income	38,183	51,051	48,155	49,875
Operating Expenses	21,141	25,326	21,460	22,973
Employee Expenses	11,548	14,342	11,081	11,685
Other Expenses	9,593	10,985	10,379	11,288
Operating Profit	17,041	25,725	26,695	26,902
Core Operating Profit	14,631	20,915	24,055	24,172
Provisions	61,646	68,577	20,041	17,958
Loan loss provisions	64,740	48,800	19,860	16,305
Investment Depreciation	300	1,800	190	390
Profit before tax	(44,604)	(42,852)	6,654	8,944
Tax	(11,184)	(10,551)	2,418	3,422
PAT before EO	(33,420)	(32,301)	4,236	5,521
Extraordinary item	—	—	—	—
PAT	(33,420)	(32,301)	4,236	5,521

Key Ratios

Y/e March	2015	2016	2017E	2018E
CMP (Rs)	161	161	161	161
Equity Shrs. Os. (m)	2,218	2,310	2,310	2,310
Market Cap (Rs m)	356,401	371,292	371,292	371,292
M/Cap to AUM (%)	5.0	5.5	5.4	5.0
EPS (Rs)	15.5	(23.8)	9.0	15.0
Book Value (Rs)	175	156	163	174
Adj. BV (100%) (Rs)	150	97	100	124
P/E (x)	10.3	(6.7)	17.9	10.7
P/BV (x)	0.9	1.0	1.0	0.9
P/ABV (x)	1.1	1.7	1.6	1.3
DPS (Rs)	3.8	—	1.8	3.0
Dividend Yield (%)	2.4	—	1.1	1.9

Profitability (%)

Y/e March	2015	2016	2017E	2018E
NIM	1.9	1.8	2.0	2.0
RoAA	0.5	(0.8)	0.3	0.5
RoAE	9.0	(13.5)	5.1	8.0

Efficiency

Y/e March	2015	2016	2017E	2018E
Cost-Income Ratio (%)	43.6	50.3	49.9	51.7
C-D Ratio (%)	69.3	66.9	64.2	64.5
Business per Emp. (Rs m)	198	157	137	129
Profit per Emp. (Rs lacs)	6.4	(8.9)	3.0	4.3
Business per Branch (Rs m)	14,937	11,268	9,616	10,404
Profit per Branch (Rs m)	49	(63)	21	35

Asset Quality

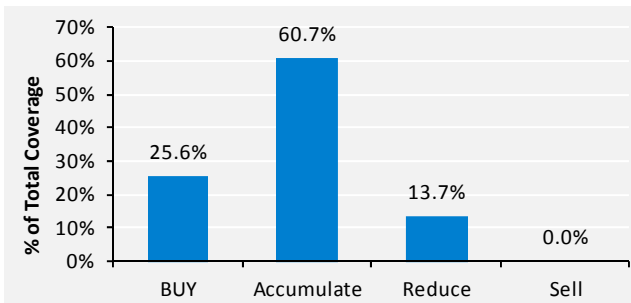
Y/e March	2015	2016	2017E	2018E
Gross NPAs (Rs m)	162,614	405,210	444,483	401,316
Net NPAs (Rs m)	80,695	194,065	206,879	167,273
Gr. NPAs to Gross Adv. (%)	3.8	10.6	11.8	9.8
Net NPAs to Net Adv. (%)	1.9	5.1	5.5	4.1
NPA Coverage (%)	50.4	52.1	53.5	58.3

Source: Company Data, PL Research.

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BUY	:	Over 15% Outperformance to Sensex over 12-months
Accumulate	:	Outperformance to Sensex over 12-months
Reduce	:	Underperformance to Sensex over 12-months
Sell	:	Over 15% underperformance to Sensex over 12-months
Trading Buy	:	Over 10% absolute upside in 1-month
Trading Sell	:	Over 10% absolute decline in 1-month
Not Rated (NR)	:	No specific call on the stock
Under Review (UR)	:	Rating likely to change shortly

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