

BANK OF BARODA

Looking better; consolidation a concern

India Equity Research | Banking and Financial Services

We met Bank of Baroda's (BoB) management to gauge bank's performance on critical parameters. a) The management sounded confident in managing credit cost in FY18 at a level below FY17 due to adequate provisioning coverage they hold – covered slightly above 50% on exposure to 10 accounts they have which are considered for IBC forming 18% of GNPLs; also though top 50 exposures form 40% of GNPLs, its covered to the extent of 53%. b) After trailing industry average growth for past many quarter being in consolidation phase, now with internal restructuring and focus it should get back to industry average credit growth. This further supported by improved NIMs (CD ratio, lower deposit rates, better international NIMs) will support revenue growth traction. Given earnings growth visibility and attractive valuation of 0.9x FY19 P/BV, we maintain 'BUY'. However, key risk to our call will be consolidation in PSU banking space (given uncertainty, execution risk, pricing etc) which might adversely impact fundamentally strong leading bank like BOB.

Adequately coverage implies lower incremental hit

Given strong coverage, incremental impact of RBI's directive on recognition will be limited. Having said that some provisions may accrue following unsecured exposure towards these accounts, but nothing significantly at variance than under seasoning impact in the base case. We have seen bank reporting sequential GNPLs dip over last couple of quarters and they expect trend to continue. Qualitatively: a) higher focus on granularity (largest account of INR20bn); & b) relatively lower SMA-II accounts (ex-restructured book) at INR80bn (2-3% of loans) render comfort. BoB maintains in worst case their GNPLs would touch INR450-460bn. We believe credit cost will be in the range of 175-190bps over FY18/FY19 – better off as compared to other PSU banks.

Outlook and valuations: Improving visibility; retain 'BUY'

Gradually earnings visibility for the bank is improving. Even after factoring higher credit cost, improving NIMs and growth will help it report RoEs upwards of 10% by FY19E. Though bank is well placed on capital, they have taken approval of INR60bn capital raising - while it could be a growth capital, we may not rule out possibility of inorganic growth. Considering valuation of 0.9x FY19E P/BV (even factoring in higher stress) and strong capital position, we maintain 'BUY/SP' with TP of INR210. Key risk: Consolidation amongst PSU banks.

Financials

(INRMn)

Year to March	FY16	FY17	FY18E	FY19E
Net revenue	1,77,387	2,02,714	2,19,062	2,54,643
Net profit	(53,956)	13,831	30,248	45,490
Diluted EPS (INR)	(23.4)	6.0	13.1	19.7
BV (INR)	156.1	156.6	166.2	182.4
Price/ book (x)	1.0	1.0	1.0	0.9
Diluted P/E (x)	(6.9)	27.0	12.4	8.2
ROE (%)	(14.2)	3.8	8.1	11.3

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Overweight

MARKET DATA (R: BOB.BO, B: BOB IN)

CMP	: INR 162
Target Price	: INR 210
52-week range (INR)	: 203 / 135
Share in issue (mn)	: 2,304.2
M cap (INR bn/USD mn)	: 372 / 5,762
Avg. Daily Vol.BSE/NSE('000)	: 10,262.6

SHARE HOLDING PATTERN (%)

	Current	Q3FY17	Q2FY17
Promoters *	59.2	59.2	59.2
MF's, FI's & BK's	20.6	21.2	21.7
FII's	11.8	11.6	11.9
Others	8.4	7.9	7.1
* Promoters pledged shares (% of share in issue)	:	NIL	

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Banks and Financial Services Index
1 month	(9.5)	(0.4)	(0.8)
3 months	(6.1)	4.1	7.2
12 months	3.4	15.4	27.8

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While a little slow, transformation journey on track

After couple of years of consolidation, Q4FY17 saw signs of bank's return to growth path (loans grew >9% QoQ), management's expect this to continue. Meanwhile, improving NIMs on a) better CD ratio b) lower deposit cost (TD rates reduced in April) and c) better international NIMs will feed into improving core profitability. BoB is operationally geared in right direction, but needs to sustain momentum to catch up with sector averages.

Table 1: Balance sheet consolidation done, growth momentum likely to sustain....

(%)	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17
Advances (INR mn)	38,37,702	36,27,664	35,41,496	34,99,601	38,32,592
Advances growth Y-o-Y	(10.3)	(11.2)	(14.6)	(8.9)	(0.1)
Advances growth Q-o-Q	(0.1)	(5.5)	(2.4)	(1.2)	9.5
Deposits (INR mn)	57,40,379	56,21,737	56,75,312	58,98,589	60,16,752
Deposits growth Y-o-Y	(7.0)	(5.2)	(7.3)	0.0	4.8
Deposits growth Q-o-Q	(2.7)	(2.1)	1.0	3.9	2.0
Overseas advances growth Y-o-Y	(11.5)	(15.4)	(21.6)	(20.1)	(12.3)
Domestic advances growth Y-o-Y	(9.8)	(9.1)	(11.2)	(3.5)	5.4
CD ratio	66.9	64.5	62.4	59.3	63.7

Table 2: ... to be supported by retail and corporate segment

(%)	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17
International	31.4	30.9	30.4	28.6	27.6
Domestic	68.6	69.1	69.6	71.4	72.4
Retail	13.3	14.0	14.5	14.7	15.1
- Housing	6.5	7.1	7.4	7.6	7.9
Agriculture	9.1	11.3	12.0	12.2	11.5
SME	14.1	17.4	15.7	15.2	14.0
Corporate and others	32.1	26.3	27.4	29.4	31.8

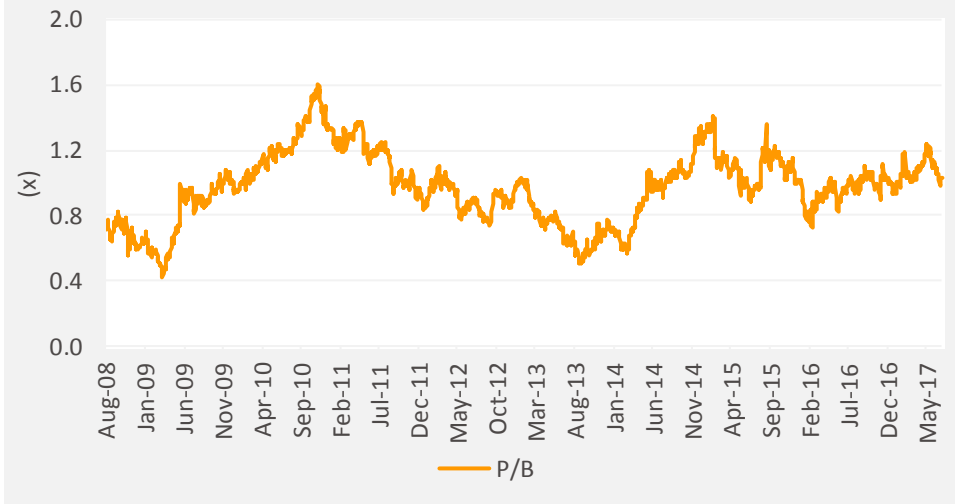
Table 3: Sequential decline in GNPLs will likely continue

	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17
Incremental slippages (%)	6.2	6.4	3.2	4.7	4.7
Gross NPA (INR mn)	4,05,210	4,29,917	4,29,493	4,26,424	4,27,187
Gross NPA (%)	10.0	11.2	11.4	11.4	10.5
Net NPA (INR mn)	1,94,065	2,07,838	1,93,420	1,90,063	1,80,802
Net NPA (%)	5.1	5.7	5.5	5.4	4.7
Provision coverage (%)	52.1	51.7	55.0	55.4	57.7

Table 4: NIMs likely to improve with levers at play for both in overseas as well as domestic NIMs

(%)	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17
Domestic NIM	2.7	2.8	2.9	2.5	2.5
Overseas NIM	0.9	1.0	1.0	1.0	1.2
Global NIM	2.2	2.2	2.3	2.1	2.2

Source: Company

Chart 1: Valuation of 0.9x P/BV (even factoring in higher stress) lends comfort

Source: Bloomberg, Edelweiss research

Company Description

Established in 1908 by Maharaja Sayajirao Gaekwad of Baroda, BoB was one of the 14 banks that were nationalised in 1969. With nearly 5,422 branches within India and over 107 offices abroad, and a balance sheet size of over ~INR6.9tn, BoB is amongst the top 5 Indian banks in terms of balance sheet size and third largest amongst PSU banks in deposit franchise. It has a well-diversified balance sheet within India, while it has leveraged its international branch network to build a >25% balance sheet from outside India. It has been one of the early players to have identified the potential and importance of international presence and is currently operating through its eight banking subsidiaries apart from the parent.

Since FY06, the bank has charted a new growth strategy under project “Parivartan”, rebranding itself, energising its century old brand.

Investment Theme

Gradually earnings visibility for the bank is improving. Even after factoring higher credit cost, improving NIMs and growth will help it report RoEs upwards of 10% by FY19E. Though bank is well placed on capital, but they have taken approval of INR60bn capital raising, while it could be a growth capital but we may not rule out possibility of inorganic growth. Considering valuation of 0.9x FY19E P/BV (even factoring in higher stress) and strong capital position, we maintain ‘BUY/SP’ with TP of INR210.

Key Risks

- Sharper-than-expected decline in net interest margins
- Sharper-than-expected slippage in asset quality
- International book can throw lumpy slippages

Financial Statements

Key Assumptions

Year to March	FY16	FY17E	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.2	6.5	7.1	7.7
Inflation (Avg)	4.9	4.8	5.0	5.2
Repo rate (exit rate)	6.8	6.3	6.3	6.3
USD/INR (Avg)	65.0	67.5	67.0	67.0
Sector				
Credit growth	9.3	9.0	12.0	14.0
Deposit growth	8.6	14.0	12.0	13.0
CRR	4.0	4.0	4.0	4.0
SLR	20.8	20.0	20.0	20.0
G-sec yield	7.5	6.5	6.5	6.5
Company				
Op. metric assumpt. (%)				
Yield on advances	7.3	7.2	7.4	7.4
Yield on investments	9.0	7.6	7.7	7.8
Yield on asset	6.6	6.5	6.5	6.5
Cost of funds	4.8	4.5	4.4	4.3
Net interest margins	1.9	2.1	2.2	2.3
Cost of deposits	4.9	4.5	4.4	4.3
Cost of borrowings	6.3	6.3	6.4	6.6
Spread	1.8	2.0	2.1	2.3
Balance sheet assumption (%)				
Credit growth	(10.4)	(0.0)	12.0	15.0
Deposit growth	(7.0)	4.8	14.7	14.2
SLR ratio	17.3	18.6	21.5	21.0
Low-cost deposits	26.4	32.2	30.2	30.6
Net NPA ratio	5.1	4.7	3.9	3.2
Net NPA / Equity	53.8	50.0	43.1	37.3
Capital adequacy	13.2	12.2	11.4	10.6
Incremental slippage	6.4	3.4	0.9	1.0
Provision coverage	52.1	57.7	62.0	65.1

Income statement

(INR mn)

Year to March	FY16	FY17E	FY18E	FY19E
Interest income	440,613	421,999	459,476	529,924
Interest expended	313,214	286,866	304,839	342,534
Net interest income	127,398	135,133	154,637	187,390
Non interest income	49,989	67,581	64,425	67,253
- Fee & forex income	27,538	29,946	33,937	38,916
- Misc. income	10,640	11,455	11,989	13,337
- Investment profits	11,810	26,180	18,500	15,000
Net revenue	177,387	202,714	219,062	254,643
Operating expense	89,231	92,963	102,617	112,733
- Employee exp	49,780	46,378	53,029	59,946
- Other opex	39,451	46,585	49,589	52,787
Preprovision profit	88,156	109,751	116,445	141,910
Provisions	155,136	85,024	76,115	81,257
Loan loss provisions	140,077	84,570	74,815	78,957
Investment depreciation	3,415	190	300	300
Other provisions	11,645	264	1,000	2,000
Profit Before Tax	(66,981)	24,727	40,330	60,653
Less: Provision for Tax	(13,025)	10,896	10,083	15,163
Profit After Tax	(53,956)	13,831	30,248	45,490
Reported Profit	(53,956)	13,831	30,248	45,490
Adj. Diluted EPS (INR)	(23.4)	6.0	13.1	19.7
Dividend per share (DPS)	-	1.2	3.0	3.0
Dividend Payout Ratio(%)	-	23.1	26.5	17.6

Growth ratios (%)

Year to March	FY16	FY17E	FY18E	FY19E
NII growth	(3.4)	6.1	14.4	21.2
Fees growth	10.7	8.7	13.3	14.7
Opex growth	16.3	4.2	10.4	9.9
PPOP growth	(14.3)	9.5	17.2	29.6
PPP growth	(11.1)	24.5	6.1	21.9
Provisions growth	245.2	(45.2)	(10.5)	6.8
Adjusted Profit	(258.8)	(125.6)	118.7	50.4

Operating ratios

Year to March	FY16	FY17E	FY18E	FY19E
Yield on advances	7.3	7.2	7.4	7.4
Yield on investments	9.0	7.6	7.7	7.8
Yield on assets	6.6	6.5	6.5	6.5
Cost of funds	4.8	4.5	4.4	4.3
Net interest margins	1.9	2.1	2.2	2.3
Cost of deposits	4.9	4.5	4.4	4.3
Cost of borrowings	6.3	6.3	6.4	6.6
Spread	1.8	2.0	2.1	2.3
Cost-income	50.3	45.9	46.8	44.3
Tax rate	19.4	44.1	25.0	25.0

Balance sheet (INR mn)				
As on 31st March	FY16	FY17E	FY18E	FY19E
Share capital	4,621	4,621	4,621	4,621
Reserves & Surplus	356,107	357,150	379,395	416,883
Net worth	360,728	361,770	384,016	421,504
Sub bonds/pref cap	71,417	81,417	91,417	101,417
Deposits	5,740,379	6,016,752	6,902,439	7,879,653
Total Borrowings	263,300	224,697	245,097	265,497
Other liabilities	236,679	222,856	222,670	251,617
Total liabilities	6,672,503	6,907,492	7,845,640	8,919,688
Loans	3,837,702	3,832,592	4,292,503	4,936,379
Cash and Equivalents	1,339,005	1,504,699	1,594,637	1,805,133
Gilts	1,036,531	1,159,428	1,536,733	1,710,494
Others	167,975	136,877	151,730	168,061
Fixed assets	21,276	16,322	12,677	8,805
Other Assets	270,016	257,574	257,360	290,816
Total assets	6,672,503	6,907,492	7,845,640	8,919,688
BVPS (INR)	156.1	156.6	166.2	182.4
Credit growth	(10.4)	(0.0)	12.0	15.0
Deposit growth	(7.0)	4.8	14.7	14.2
EA growth	(8.7)	4.0	14.2	13.8
SLR ratio	17.3	18.6	21.5	21.0
C-D ratio	67.6	64.5	63.0	63.4
Low-cost deposits	26.4	32.2	30.2	30.6
Provision coverage	52.1	57.7	62.0	65.1
Gross NPA ratio	10.3	10.6	9.6	8.6
Net NPA ratio	5.1	4.7	3.9	3.2
Incremental slippage	6.4	3.4	0.9	1.0
Net NPA / Equity	53.8	50.0	43.1	37.3
Capital adequacy	13.2	12.2	11.4	10.6
- Tier 1	10.8	9.9	9.1	8.3

RoE decomposition (%)				
Year to March	FY16	FY17E	FY18E	FY19E
Net int. income/assets	1.9	2.1	2.2	2.3
Fees/Assets	0.6	0.6	0.6	0.6
Invst. profits/Assets	0.2	0.4	0.3	0.2
Net revenues/assets	2.7	3.1	3.1	3.1
Operating expense/assets	(1.3)	(1.4)	(1.4)	(1.4)
Provisions/assets	(2.3)	(1.3)	(1.1)	(1.0)
Taxes/assets	0.2	(0.2)	(0.1)	(0.2)
Total costs/assets	(3.5)	(2.9)	(2.7)	(2.6)
ROA	(0.8)	0.2	0.4	0.6
Equity/assets	5.7	5.6	5.2	5.0
ROAE (%)	(14.2)	3.8	8.1	11.3

Valuation parameters				
Year to March	FY16	FY17E	FY18E	FY19E
Adj. Diluted EPS (INR)	(23.4)	6.0	13.1	19.7
Y-o-Y growth (%)	(252.4)	(125.6)	118.7	50.4
BV per share (INR)	156.1	156.6	166.2	182.4
Adj. BV per share (INR)	97.3	101.8	116.1	134.9
Diluted P/E (x)	(6.9)	27.0	12.3	8.2
P/B (x)	1.0	1.0	1.0	0.9
Price/ Adj. BV (x)	1.7	1.6	1.4	1.2
Dividend Yield (%)	(0.0)	0.7	1.9	1.9

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		Price/ Adj. BV (X)		ROAE (%)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Bank of Baroda	5,762	12.3	8.2	1.4	1.2	8.1	11.3
Punjab National Bank	4,520	9.8	7.1	1.4	0.9	7.7	10.0
State Bank of India	36,545	12.1	9.9	1.7	1.4	11.0	12.2
Union Bank Of India	1,568	6.7	5.6	1.2	0.8	7.3	8.8
Median	-	11.0	7.7	1.4	1.0	7.9	10.7
AVERAGE	-	10.2	7.7	1.4	1.1	8.5	10.6

Source: Edelweiss research

Additional Data

Directors Data

Ravi Venkatesan	Non-Executive Chairman	P. S. Jayakumar	Managing Director & CEO
Papia Sengupta	Executive Director	Mayank K. Mehta	Executive Director
Ashok Kumar Garg	Executive Director	Prem Kumar Makkar	Director
Mohammad Mustafa	Director	R. Narayanaswamy	Director
Bharatkumar Dhirubhai Dangar	Director	Usha A Narayanan	Director
Biju Varkkey	Director	Ajay Kumar	Director
Gopal Krishan Agarwal	Director		

Auditors - S R Goyal & Co.

**as per last annual report*

Holding - Top 10

	Perc. Holding		Perc. Holding
Life Insurance Corporation of India	10.03	HDFC Asset Management	4.51
Theleme Master Fund	2.49	Bees R Shares Nifty	1.01
Birla Sun Life Asset Management	0.94	DSP Blackrock Investment Manager	0.86
Reliance Capital Trustee	0.79	UTI Asset Management	0.67
Vanguard Group	0.67	Kotak Mahindra	0.60

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
No Data Available			

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Allahabad Bank	HOLD	SU	M	Axis Bank	BUY	SO	M
Bajaj Finserv	BUY	SP	L	Bank of Baroda	BUY	SP	M
Bharat Financial Inclusion	BUY	SO	M	Capital First	BUY	SO	M
DCB Bank	REDUCE	SU	M	Dewan Housing Finance	BUY	SO	M
Equitas Holdings Ltd.	BUY	SO	M	Federal Bank	BUY	SP	L
HDFC	HOLD	SP	L	HDFC Bank	BUY	SO	L
ICICI Bank	BUY	SO	L	IDFC Bank	HOLD	SP	L
Indiabulls Housing Finance	BUY	SO	M	IndusInd Bank	BUY	SP	L
Karnataka Bank	BUY	SP	M	Kotak Mahindra Bank	HOLD	SP	M
L&T FINANCE HOLDINGS LTD	BUY	SO	M	LIC Housing Finance	BUY	SP	M
Magma Fincorp	BUY	SP	M	Mahindra & Mahindra Financial Services	HOLD	SU	M
Manappuram General Finance	BUY	SO	H	Max Financial Services	BUY	SO	L
Multi Commodity Exchange of India	BUY	SP	M	Muthoot Finance	BUY	SO	M
Oriental Bank Of Commerce	HOLD	SP	L	Power Finance Corp	BUY	SO	M
Punjab National Bank	BUY	SP	M	Reliance Capital	BUY	SP	M
Repco Home Finance	BUY	SO	M	Rural Electrification Corporation	BUY	SO	M
Shriram City Union Finance	BUY	SO	M	Shriram Transport Finance	BUY	SO	L
South Indian Bank	BUY	SP	M	State Bank of India	BUY	SP	L
Union Bank Of India	HOLD	SP	M	Yes Bank	BUY	SO	M

ABSOLUTE RATING

Ratings

Expected absolute returns over 12 months

Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings

Criteria

Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings

Criteria

Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings

Criteria

Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

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Coverage group(s) of stocks by primary analyst(s): Banking and Financial Services

Allahabad Bank, Axis Bank, Bharat Financial Inclusion, Bajaj Finserv, Bank of Baroda, Capital First, DCB Bank, Dewan Housing Finance, Equitas Holdings Ltd., Federal Bank, HDFC, HDFC Bank, ICICI Bank, IDFC Bank, Indiabulls Housing Finance, IndusInd Bank, Karnataka Bank, Kotak Mahindra Bank, LIC Housing Finance, L&T FINANCE HOLDINGS LTD, Max Financial Services, Multi Commodity Exchange of India, Manappuram General Finance, Magma Fincorp, Mahindra & Mahindra Financial Services, Muthoot Finance, Oriental Bank Of Commerce, Punjab National Bank, Power Finance Corp, Reliance Capital, Rural Electrification Corporation, Repco Home Finance, State Bank of India, Shriram City Union Finance, Shriram Transport Finance, South Indian Bank, Union Bank Of India, Yes Bank

Recent Research

Date	Company	Title	Price (INR)	Recos
30-Jun-17	Yes Bank	Clearing the air; Visit Note	1,438	Buy
15-Jun-17	Reliance Capital	Strategy enthusing, execution key; Event Update	600	Buy
14-Jun-17	Banking	Mixed quarter; bumpy ride ahead; Sector Update		

Distribution of Ratings / Market Cap

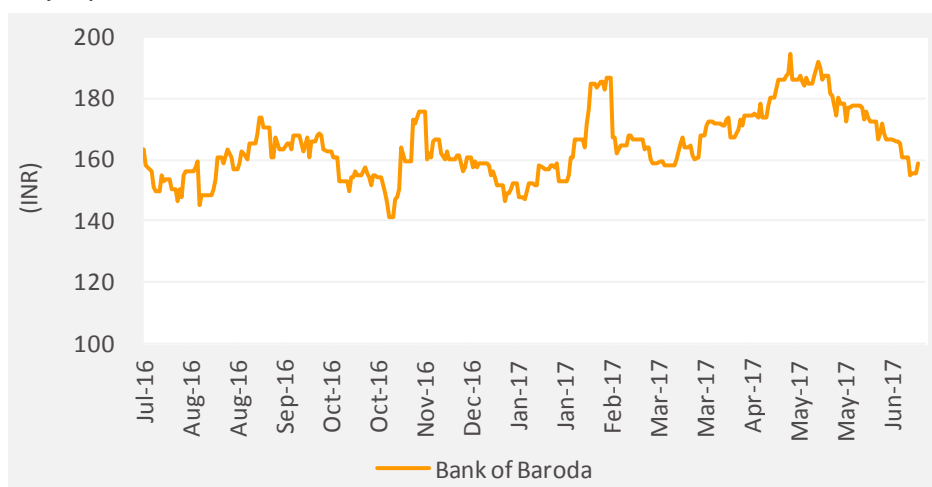
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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