

RETAIL EQUITY RESEARCH

Bank of Baroda (BOB)

Banking

BSE CODE: 532134

NSE CODE: BANKBARODA

Bloomberg CODE: BOB:IN

SENSEX: 33,588

BUY

Rating as per Large Cap

12 month investment period

CMP Rs. 178 TARGET Rs. 208 RETURN 17% 24th November, 2017

Green shoots visible but sustainability holds key...

BOB is one of India's largest banks with strong domestic presence spanning across 5,422 branches. The bank also has significant international presence with a network of 106 branches across 25 countries.

- Net interest income (NII) increased at a moderate pace of 9% YoY on the back of healthy growth of 14% YoY in domestic loan book.
- Gross/Net non-performing assets (NPAs) of the bank improved by 24/12 bps QoQ to 11.4%/5.2%.
- We expect slippages to decline gradually and asset quality to improve going ahead with Gross/Net NPA ratios to decline to 8.5%/3.2% by FY19.
- We expect net profit to increase at a CAGR of 64% (albeit on a lower base) over FY17-19E led by improvement in margins coupled with lower provisions.
- Given the management's focus on cleaning up the B/S and laying the foundation for sustainable growth. Hence, we maintain a BUY rating on the stock with a revised upward TP of Rs208 (P/ABV of 1.6x for FY19E).

Advances growth driven by domestic retail advances

BOB's loan book grew at a modest pace of 9% YoY mainly led by domestic advances. Domestic loan book witnessed healthy trends (↑14% YoY) aided by strong growth in retail advances (↑26% YoY) and stable growth in wholesale credit (↑15% YoY). Within retail, home loans outperformed (↑34% YoY) aided by portfolio buyouts. However, the bank continues to curtail its low yielding international loan book (↓1% YoY). On liabilities front, while low cost CASA deposits grew at a robust pace of 24% YoY, term deposits declined by 5% YoY. As a result, total deposits increased at a muted pace of 3% YoY. CASA ratio improved by 580 bps YoY to 33.4%. Going forward, we expect advances to grow at a healthy pace of 11% CAGR over FY17-19E mainly led by retail and agri loan books.

Healthy operating performance

Net interest income (NII) increased at a moderate pace of 9% YoY (in line with our expectation) on the back of healthy growth in domestic loan book. However, net interest margin (NIM) declined by 27 bps YoY to 2.5% as incremental exposure to good quality accounts suppressed the yield on advances (↓125 bps YoY). We expect NIM to improve from hereon (2.8% in FY19E) on account of declining interest reversal cases coupled with increasing retail share in the total loan book. Provisions increased at a much faster pace of 30% YoY as BOB continued to provide aggressively against stressed accounts. As a result, net profit declined by 35.6% YoY (below our expectation). We have also increased our credit cost estimate for FY18E by 10 bps to 2.1%. Going forward, we expect net profit to increase at a CAGR of 64% (albeit on a lower base) over FY17-19E led by improvement in margins along with lower provisions.

Slippages dipped; Sustenance crucial

BOB's asset quality improved marginally as fresh slippages declined by 41% QoQ. Hence, Gross/Net non-performing assets (NPA) improved by 24/12 bps sequentially to 11.2%/5.1%. Provision coverage ratio also (PCR) improved by 90 bps QoQ to 67.2% as the bank continues to make provisions judiciously. The Bank has total exposure to the tune of Rs77bn towards first list of loan accounts referred to IBC/NCLT. Notably, all these loans have already been classified as NPAs and currently the Bank holds PCR of ~54% for these accounts. We believe that some green shoots are visible and expect asset quality to improve gradually from hereon. We project Gross/Net NPA ratios to decline to 8.5%/3.2% by FY19.

Outlook & Valuation

The Bank's new management is gradually reinstating confidence through major changes in operating structure which will start yielding desired outcome. Further, we also like management's focus on cleaning up the balance sheet and laying the foundation for sustainable growth. We continue to prefer BOB among public sector banks owing to its better capital position, able management and higher provision coverage ratio. Moreover, gradual improvement in asset quality will lead to better profitability. As a result, we expect RoA and RoE to improve to 0.5% and 9%, respectively by FY19E. Hence, we continue to maintain BUY rating on the stock with a revised upwards TP of Rs208 and value the bank at P/ABV of 1.6x for FY19E.

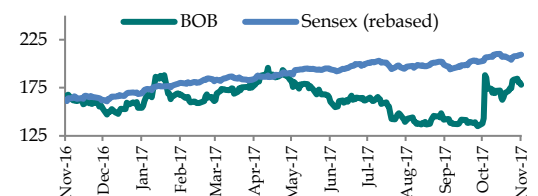
Company Data

Market Cap (cr)	Rs. 41,014
Outstanding Shares (cr)	230.4
Free Float	41%
Dividend Yield	-
52 week high	Rs. 207
52 week low	Rs. 134
6m average volume (cr)	1.4
Beta	2.8
Face value	Rs. 2

Shareholding (%)	Q4FY17	Q1FY18	Q2FY18
Promoters	59.2	59.2	59.2
FII's	11.8	12.0	12.9
MFs/Insti	20.6	21.2	18.7
Public	8.4	7.5	9.2
Others	-	-	-
Total	100.0	100.0	100.0

Price Performance	3 month	6 month	1 Year
Absolute Return	26.3%	-2.3%	9.6%
Absolute Sensex	6.4%	10.6%	28.9%
Relative Return*	20.1%	-14.2%	-18.1%

*over or under performance to benchmark index



Standalone (Rs.cr)	FY17A	FY18E	FY19E
Net Interest Income	13,513	14,858	16,690
Growth (%)	6%	10%	12%
NIM (%)	2.7	2.8	2.8
Pre Pro Profit	10,975	11,747	13,409
Growth (%)	24%	7%	14%
Net Profit	1,383	2,021	3,716
Growth (%)	-	46%	84%
EPS	6.0	8.7	16.1
Growth (%)	-	46%	84%
P/E	29.7	20.3	11.1
P/BV	1.0	1.0	0.9
P/ABV	1.9	1.9	1.4
RoE (%)	3.4	4.9	8.5
RoA (%)	0.2	0.3	0.5

Quarterly Financials (Standalone)

Profit & Loss Account

(Rs cr)	Q2FY18	Q2FY17	YoY Growth %	Q1FY18	QoQ Growth %
Interest Income	10,753	10,485	2.6	10,553	1.9
Interest on advances	7,146	6,840	4.5	6,935	3.0
Income on Investments	2,492	2,533	(1.6)	2,427	2.7
Others	1,116	1,113	0.3	1,191	(6.3)
Interest Expense	7,033	7,059	(0.4)	7,148	(1.6)
Net Interest Income	3,721	3,426	8.6	3,405	9.3
Non-Interest Income	1,737	1,561	11.2	1,551	12.0
Total Net Income	5,458	4,988	9.4	4,956	10.1
Operating Expenses	2,416	2,297	5.2	2,308	4.7
Employee Cost	1,213	1,169	3.8	1,015	19.5
Other Operating Exp.	1,203	1,129	6.5	1,293	(7.0)
Total Income	12,490	12,047	3.7	12,104	3.2
Total Expenditure	9,449	9,356	1.0	9,456	(0.1)
Pre-Provisioning profit	3,042	2,690	13.1	2,648	14.9
Provisions	2,329	1,796	29.7	2,368	(1.6)
Profit Before Tax	712	894	(20.3)	280	154.4
Tax	357	342	4.4	77	365.8
Net Profit	355	552	(35.6)	203	74.7
EPS - Diluted (Rs)	1.5	2.4	(35.6)	0.9	74.7

Business Performance (Rs cr)	Q2FY18	Q2FY17	YoY Growth %	Q1FY18	QoQ Growth %
Advances	387,302	354,150	9.4	377,607	2.6
Deposits	583,212	567,531	2.8	570,608	2.2
Business	970,514	921,681	5.3	948,214	2.4
Gross NPA	46,307	42,949	7.8	46,173	0.3
Net NPA	19,573	19,342	1.2	19,519	0.3

Key Ratios (%)	Q2FY18	Q2FY17	YoY bps	Q1FY18	QoQ bps
Net Interest Margin	2.5	2.8	(27)	2.5	(2)
Cost of Funds	4.1	4.7	(58)	4.4	(29)
Yield on Advances	6.4	7.6	(125)	6.9	(51)
Yield on Investments	6.9	7.5	(68)	7.2	(30)
Yield on Funds	7.3	8.5	(126)	7.9	(60)
Cost to Income	44.3	46.1	(180)	46.6	(230)
Credit to Deposit	66.4	62.4	401	66.2	23
CASA	33.4	27.6	580	31.9	150
Capital Adequacy	11.6	12.9	(130)	11.8	(17)
Tier I Capital	9.6	10.6	(98)	9.8	(16)
Gross NPA	11.2	11.4	(19)	11.4	(24)
Net NPA	5.1	5.5	(41)	5.2	(12)
Provision Coverage	67.2	63.0	423	66.3	90
Credit Cost	2.4	2.0	38	2.5	(10)
RoE (Ann.)	3.3	5.4	(217)	2.0	128
RoA (Ann.)	0.2	0.3	(14)	0.1	8

Change in estimates

Year / Rs cr	Old estimates		New estimates		Change %	
	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Net Interest Income	14,893	16,818	14,858	16,690	-0.2	-0.8
Pre-Provisioning Profit	11,716	13,485	11,747	13,409	0.3	-0.6
Net Profit	3,113	3,735	2,021	3,716	-35.1	-0.5
EPS (Rs)	13.5	16.2	8.7	16.1	-35.2	-0.7

Source: Company, Geojit Research

Standalone Financials

Profit & Loss Account

Y.E March (Rs cr)	FY15A	FY16A	FY17A	FY18E	FY19E
Interest Income	42,964	44,061	42,200	43,577	46,909
Interest Expense	29,776	31,321	28,687	28,718	30,219
Net Interest Income	13,187	12,740	13,513	14,858	16,690
% Change	10.2	(3.4)	6.1	10.0	12.3
Non-Interest Income	4,401	4,999	6,758	6,603	7,417
Net Income	17,589	17,739	20,271	21,461	24,107
Operating Expenses	7,674	8,923	9,296	9,714	10,699
Total Income	47,365	49,060	48,958	50,180	54,326
Total Expenditure	37,450	40,245	37,983	38,432	40,917
Pre-Provisioning Profit	9,915	8,816	10,975	11,747	13,409
% Change	10.1	(11.1)	24.5	7.0	14.1
Provisions	4,495	15,514	8,502	8,685	7,778
Profit Before Tax	5,420	(6,698)	2,473	3,063	5,631
Tax	2,022	(1,303)	1,090	1,041	1,914
Tax Rate (%)	37	-	44	34	34
Net Profit	3,398	(5,396)	1,383	2,021	3,716
% Change	(20.2)	-	-	46.1	83.8
No. of Shares (cr)	222	231	231	231	231
EPS (Rs)	15.8	(23.9)	6.0	8.7	16.1
% Change	(24.9)	-	-	45.8	83.8

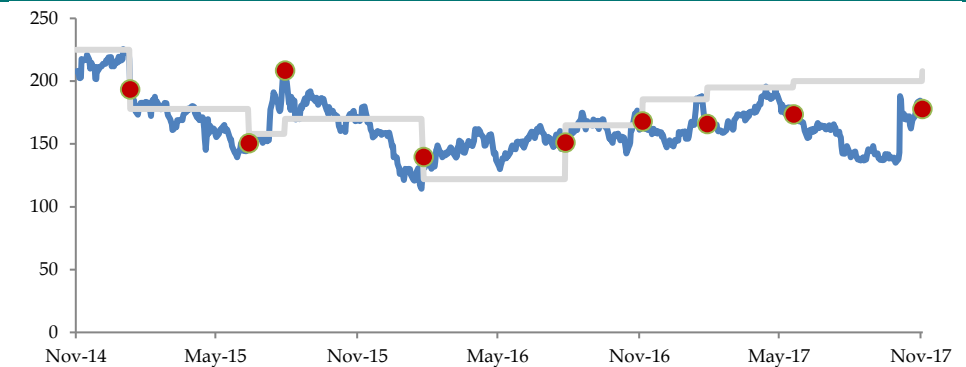
Balance Sheet

Y.E March (Rs cr)	FY15A	FY16A	FY17A	FY18E	FY19E
Liabilities					
Capital	444	462	462	462	462
Reserves & Surplus	39,392	39,737	39,841	41,474	44,747
Deposits	617,560	574,038	601,675	626,392	662,912
Borrowings	35,264	33,472	30,611	35,413	37,943
Other Liabilities & Provisions	22,329	23,668	22,286	22,486	22,877
Total Liabilities	714,989	671,376	694,875	726,228	768,940
Assets					
Cash & Balances	148,353	133,900	150,470	131,542	112,695
Investments	116,812	120,451	129,631	140,938	149,155
Advances	428,065	383,770	383,259	421,585	474,283
Fixed Assets	2,875	6,254	5,758	5,467	5,248
Other Assets	18,883	27,002	25,757	26,695	27,559
Total Assets	714,989	671,376	694,875	726,228	768,940

Ratios

Y.E March (Rs cr)	FY15A	FY16A	FY17A	FY18E	FY19E
EPS	15.8	(23.9)	6.0	8.7	16.1
DPS	3.2	0.0	0.0	1.4	1.6
BV	179.6	174.0	174.4	181.5	195.7
ABV	143.2	90.0	96.2	94.3	129.1
Valuation (%)					
P/E	11.2	-	29.7	20.3	11.1
P/BV	1.0	1.0	1.0	1.0	0.9
P/ABV	1.2	2.0	1.9	1.9	1.4
Div. Yield	1.8	0.0	0.7	0.8	0.9
Spreads (%)					
Yield on Advances	7.5	7.3	7.2	7.1	7.1
Yield on Investments	8.3	9.0	8.5	8.4	8.4
Yield on Funds	8.1	8.4	8.3	8.1	7.9
Cost of Funds	4.7	5.0	4.6	4.4	4.4
Capital (%)					
CAR	12.6	13.2	12.2	12.1	12.3
Tier I	9.9	10.8	9.9	9.8	10.0
Tier II	2.7	2.4	2.3	2.3	2.3
Asset (%)					
GNPA	3.7	10.0	10.5	11.1	8.5
NNPA	1.9	5.1	4.7	4.8	3.2
PCR	65.0	60.1	66.8	67.8	69.8
Management (%)					
Credit/ Deposit	69.3	66.9	63.7	67.3	71.5
Cost/ Income	43.6	50.3	45.9	45.3	44.4
CASA	26.4	26.4	32.2	33.2	33.7
Earnings (%)					
NIM	2.5	2.4	2.7	2.8	2.8
ROE	9.0	-	3.4	4.9	8.5
ROA	0.5	-	0.2	0.3	0.5

Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
30 January 2015	HOLD	178
03 July 2015	HOLD	158
19 August 2015	HOLD	170
15 February 2016	HOLD	122
17 August 2016	BUY	165
18 November 2016	BUY	186
17 February 2017	BUY	195
08 June 2017	BUY	200
24 November 2017	BUY	208

*Initiating Coverage

Investment Rating Criteria

Large Cap Stocks;			Mid Cap and Small Cap;		
Buy	-	Upside is above 10%.	Buy	-	Upside is above 15%.
Hold	-	Upside is between 0% - 10%.	Accumulate	-	Upside is between 10% - 15%.
Reduce	-	Downside is more than 0%.	Hold	-	Upside is between 0% - 10%.
			Reduce/Sell	-	Downside is more than 0%.
			To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.		

The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating. For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

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