

Sector: Banks & Finance
Result Update

	Change
Reco: Hold	↔
CMP: Rs. 110	
Price Target: Rs. 120	↓

↑ Upgrade ↔ No change ↓ Downgrade

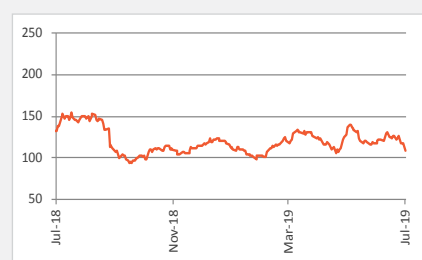
Company details

Market cap:	Rs. 42,140 cr
52-week high/low:	Rs. 157/91
NSE volume: (No of shares)	207.9 lakh
BSE code:	532134
NSE code:	BANKBARODA
Sharekhan code:	BANKBARODA
Free float: (No of shares)	118.4 cr

Shareholding (%)

Promoters	69.2
FII	6.4
DII	11.1
Others	13.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-6.8	-11.9	-2.5	-16.9
Relative to Sensex	-3.9	-9.7	-7.5	-20.1

Sharekhan Research, Bloomberg

Bank of Baroda (BoB) saw the first quarter where the merged entity reported results and the performance was modest in our view with Net interest income (NII) growth of 2.61% y-o-y and profit of Rs. 710 crore for Q1FY20 as against the loss of Rs. 49 crore in Q1FY19. The reported prior period numbers are not comparable with the present reported numbers. Hence, we have used the re-stated prior period numbers of P&L for comparison. The merger has not only thrown up integration issues (as expected), but overhang on asset-quality performance of the post-merger bank is another point of concern and we believe asset quality is likely to be the key monitorable in the medium term. Going forward, we expect NIM performance to be muted, but asset quality performance is expected to be the key monitorable. Capital burn has been higher than anticipated (CET-1 erodes by 189 BPS since Q4FY2019), which is necessitating growth capital infusion, most likely in FY2020E itself. We maintain our Hold rating with a revised price target (PT) of Rs. 120.

Key positives

- ♦ The bank has 88.67% PCR in NCLT accounts of the amalgamated entity and a recovery/resolution therefrom is likely to result in the release of provisions.
- ♦ In Q1FY2020, ~70% of the slippage was from the watchlist of March 2019 of the amalgamated book.

Key negatives

- ♦ Asset-quality performance, credit cost wise as well as exposure to stressed corporates etc., continues to be lacklustre.

Our Call

Valuation – BoB currently trades at <1.0x its FY2021E book value. However, post the merger, growth outlook has weakened and asset-quality performance is still facing challenges. Considering the risks, we maintain our Hold rating with a revised PT of Rs. 120.

Key Risks

Capital burn has also been higher than anticipated (CET-1 erodes by 189 BPS since Q4FY2019) and the bank has indicated its requirement of growth capital infusion in FY2020E – a delay in which may impact growth rates.

	Rs cr			
Valuation				
Particulars	FY18	FY19	FY20E	FY21E
Net interest income (Rs)	15,522	18,684	20,356	21,611
Net profit (Rs)	-2,432	434	4,759	5,780
EPS (Rs)	-9.2	1.6	17.8	21.7
PE (x)	-12.0	67.8	7.1	5.8
BVPS (Rs)	152.0	179.5	168.1	185.2
P/BV (x)	0.7	0.6	0.8	0.7
RoE (%)	-5.8	0.9	9.6	11.5
RoA (%)	-0.3	0.1	0.6	0.7

Source: Company; Sharekhan estimates

Weak operating performance: In Q1FY20, BoB reported merged entity's numbers (it has merged two erstwhile PSU Banks with itself). Hence, reported prior period numbers are not comparable with the present reported numbers. However, the bank has provided the re-stated prior period numbers of the P&L for comparison basis, which we have used to analyse P&L performance. On re-stated basis comparison, we find that Q1FY20 results were modest, with slow growth (as expected due to integration), but the bank also reported weak performance on the asset-quality front. Net interest income (NII) grew by 2.61% y-o-y to Rs. 6,496 crore because of muted advances growth. Non-interest income (OI) increased by 16.12% y-o-y to Rs. 641 crore and was helped mainly by strong treasury gains of Rs. 338 crore (up 123.84% y-o-y) during the quarter. However, here too, core fee income performance was relatively tepid and grew by 7.86% y-o-y to Rs. 1,276 crore. Moreover, as a result of tepid domestic advances growth of 5.18% y-o-y, net interest margin (NIM) during the quarter declined by 6 BPS q-o-q to 2.62%, led by dip in international margins and a decline in domestic investment yields. However, BoB has been steadily reducing its reliance on high-cost bulk deposits, which should aid in higher margins going forward. Notably, total provisions during the quarter declined by 14.22% y-o-y to Rs. 3,566 crore, of which NPA provisions declined by 10.84% y-o-y. This also resulted in maintaining stable credit cost of 2.04% sequentially. However, high provision coverage ratio (PCR), including technical write-off (two) remained largely stable at 77.34% in Q1FY2020 (which is highest levels amongst peers). Helped by lower provisions, the bank reported profit of Rs. 710 crore for the quarter as compared to loss of Rs. 49 crore in Q1FY2019 (in re-stated Q1FY2019).

Domestic loan growth muted: During Q1FY20, BoB had muted loan book traction of 6.44% y-o-y, with domestic book growing at a slower pace of 5.18% y-o-y to Rs. 5,33,054 crore, led by retail loan growth of 20.5% y-o-y. International book witnessed healthy growth of 13.63% y-o-y, largely due to international book of merged entity. The retail segment's growth was largely fueled by 17.13% y-o-y rise in home loan portfolio. Deposits growth for the quarter stood at 6.38% y-o-y, with domestic deposits rising by 8.87% y-o-y to Rs. 7,85,861 crore. Overall CASA deposits declined by 39 BPS y-o-y, while domestic CASA declined by 66 BPS y-o-y. Domestic CASA ratio during the quarter stood at 36.55%. The bank has been steadily reducing its reliance on high-cost bulk deposits, which should aid in higher margins (prior period comparisons taken from the company's presentation).

Asset-quality deteriorates: BoB witnessed deterioration in its asset quality as its GNPA ratio and net NPA ratio increased by 26 BPS and 30 BPS to 10.28% and 3.95%, respectively, on a sequential basis. Fresh NPA worth Rs. 5,583 crore slipped into the NPA category as against Rs. 6,554 crore in Q4FY2019. Of the total slippages, agriculture reported Rs. 1,281 crore, MSME reported Rs. 1,340 crore, corporate reported Rs. 1,593 crore and retail reported Rs. 876 crore. The bank effected write-off of Rs. 4,532 crore, which even though is lower than Rs. 7,652 crore in Q4FY2019, we believe is still on the higher side and helped the bank contain GNPA's. In addition, credit cost remained stable at 2.04% in Q1FY2020 from 2.03% in Q4FY2019 due to lower provisions. Exposure to accounts under NCLT-1 list was Rs. 5,820 crore (carry 97.42% provisions) and for NCLT-2 list was Rs. 6,957 crore (carry 84.86% provisions). The bank has given the stressed asset watchlist to be at Rs. 16,501 crore, which includes some of the stressed corporate accounts (in housing finance, financial conglomerated, wind power and plastic tanks) and it avers that all stressed accounts under SMA included in the watchlist. However, high slippage ratio of the merged banks continues to be high and poses a concern on medium-term asset performance and credit cost.

Results (unaudited standalone)

					Rs cr
Particulars	Q1FY20	Q1FY19	YoY %	Q4FY19	QoQ %
Interest income	18,945.3	11,639.9	62.8	13,314.2	42.3
Interest Expense	12,447.2	7,258.8	71.5	8,247.2	50.9
Net Interest income	6,498.1	4,381.1	48.3	5,067.0	28.2
Non-interest income	1,915.6	1,147.8	66.9	1,970.4	-2.8
Net total Income	8,413.7	5,528.9	52.2	7,037.4	19.6
Operating Expenses	4,137.5	2,523.3	64.0	3,176.6	30.2
Pre-provisioning profit	4,276.2	3,005.6	42.3	3,860.8	10.8
Provisions	3,284.9	2,165.6	51.7	5,399.3	-39.2
Profit before tax	991.4	840.0	18.0	-1,538.5	NA
Tax	281.5	311.7	-9.7	-547.1	NA
Profit after tax	709.9	528.3	34.4	-991.4	NA

Source: Company, Sharekhan Research; Note: YoY & QoQ numbers are strictly not comparable

Results at a Glance - Amalgamated entity (Standalone Basis; prior period restated)

				Rs cr
Particulars	Quarterly results			% change
	Q1FY20	Q1FY19		
Interest Income	18,943	17,339		8.87
Interest Expenses	12,447	11,069		12.45
Net Interest Income (NII)	6,496	6,331		2.61
Customer fee income	1,276	1,183		7.86
Customer Income (NII + fee income)	7,772	7,514		3.43
Other non interest income	641	552		16.12
a) trading gains - profit from sale of investments	338	151		123.84
b) recovery from TWO	203	267		-23.97
Operating income (NII + Other income)	8,413	8,066		4.30
Operating expenses	4,137	3,947		4.81
of which employee cost	1,939	2,000		-3.05
Operating profit	4,276	4,118		3.84
Total provisions	3,566	4,167		-14.22
of which Provision for NPA	3,168	3,553		-10.84
Profit before Tax	991	174		469.54
Provision for Tax	281	223		26.01
Net Profit	710	-49		NA

Source: Company, Sharekhan Research

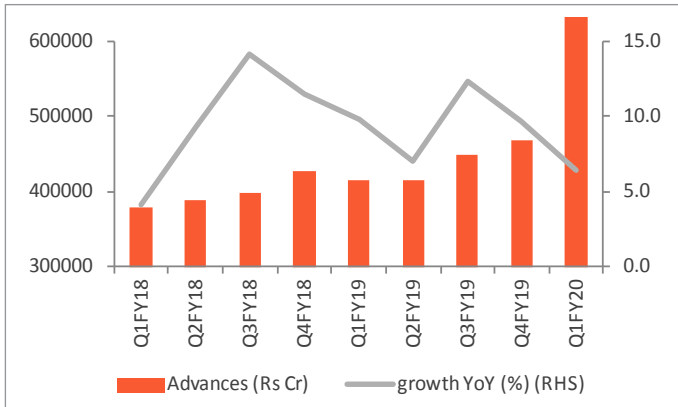
Movement of NPAs

									Rs cr
Particulars	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20
Gross NPAs (Rs)	461.73	463.07	484.80	564.80	558.75	551.2	531.8	482.3	697.14
QoQ addition (Rs)	34.54	1.34	21.74	80.00	-6.06	-7.53	-19.37	-49.51	214.81
Net NPAs (Rs)	195.19	195.73	198.52	234.83	223.84	210.6	191.3	156.1	250.30
QoQ addition(Rs)	14.39	0.53	2.80	36.31	-10.99	-13.25	-19.29	-35.22	94.21
Gross NPA (%)	11.40%	11.16%	11.31%	12.26%	12.46%	11.78%	11.01%	9.61%	10.28%
Net NPA (%)	5.17%	5.05%	4.97%	5.49%	5.40%	4.86%	4.26%	3.33%	3.95%

Source: Company, Sharekhan Research

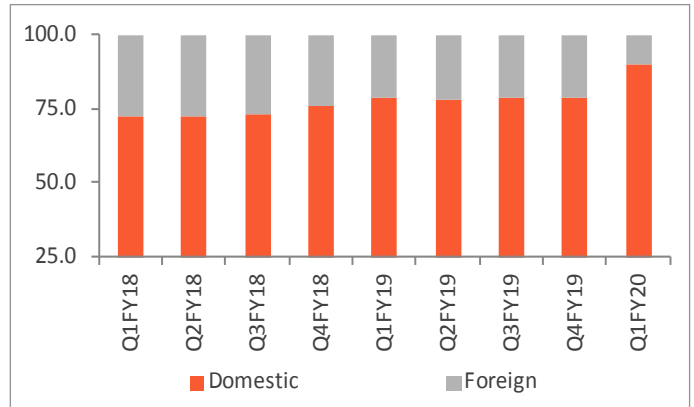
Financials in charts

Advances trend



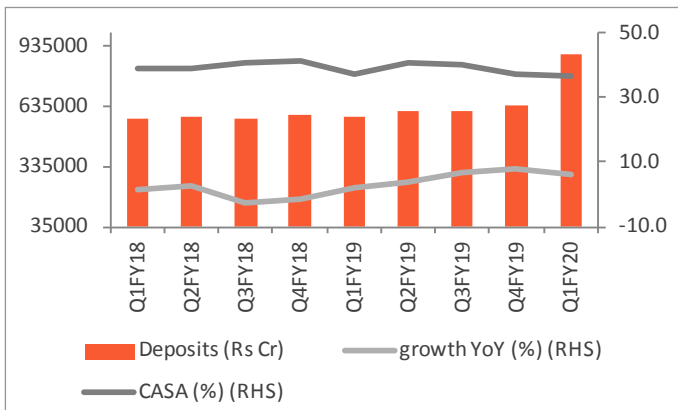
Source: Company, Sharekhan Research

Loan Mix



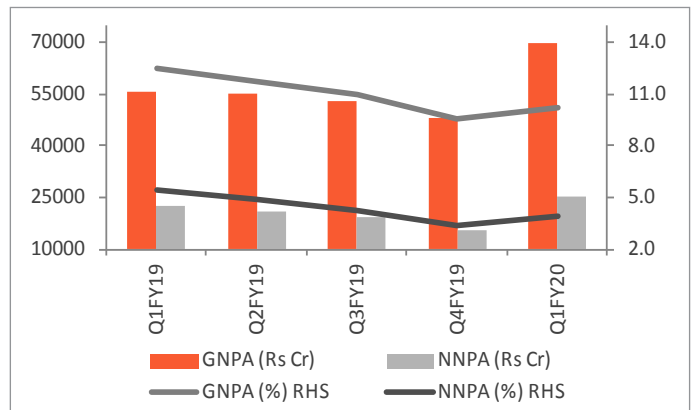
Source: Company, Sharekhan Research

Deposits trend



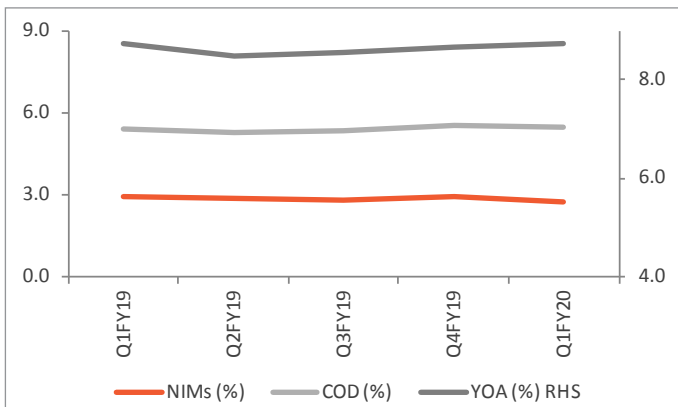
Source: Company, Sharekhan Research

Asset Quality Movement



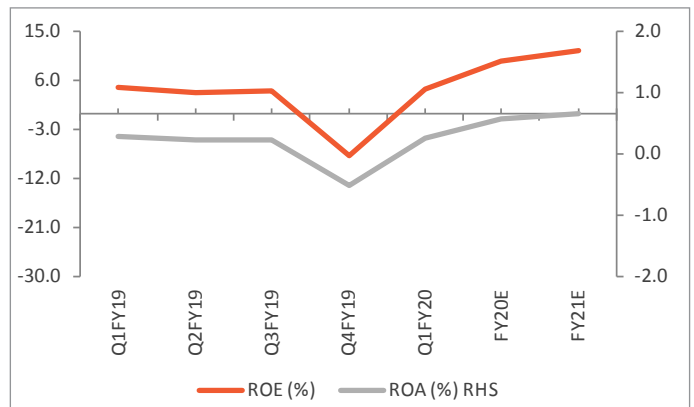
Source: Company, Sharekhan Research

NIMs, Yields on Advances, Cost of Deposits



Source: Company, Sharekhan Research

Return Ratios



Source: Company, Sharekhan Estimates

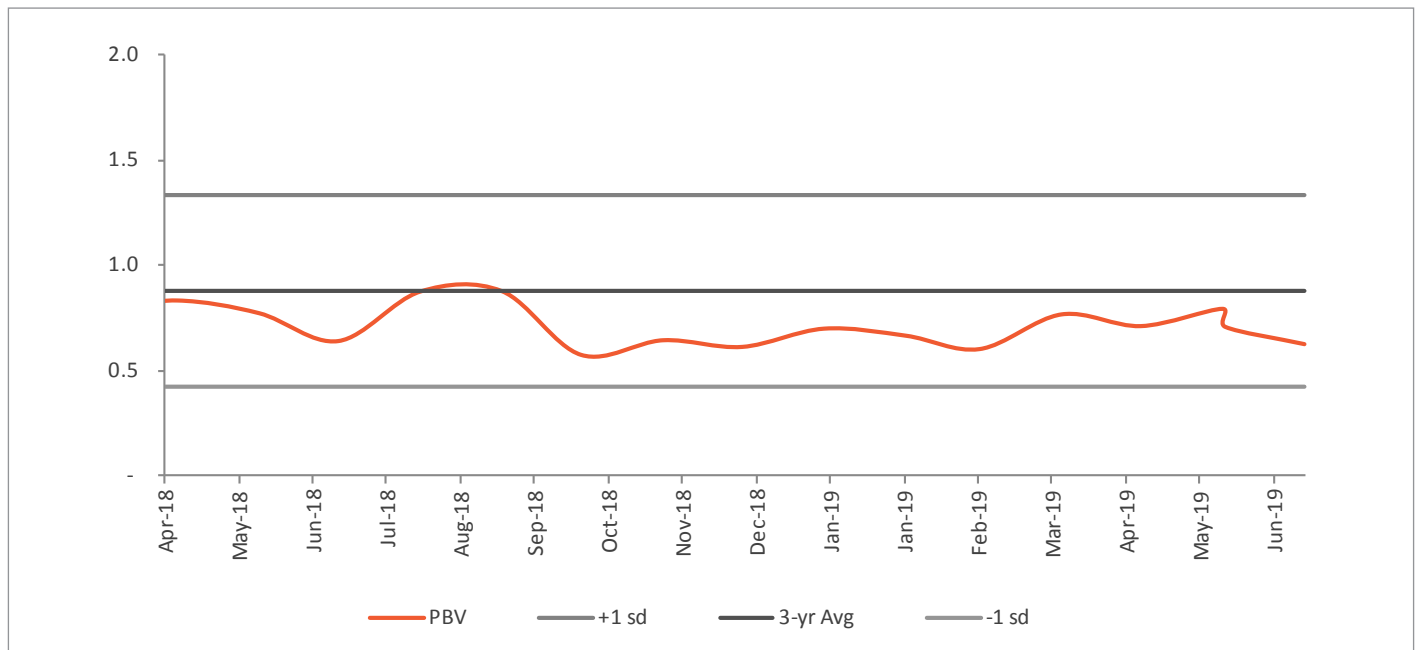
Outlook

BoB saw the first quarter where the merged entity reported results and performance was modest in our view. The merger has not only thrown up integration issues (as expected), but also the overhang on asset-quality performance of the post-merger bank is another point of concern. The bank may have reduced its liability pricing, but softening yields may keep NIM performance muted. Continued high slippages rate, despite the so-called upfronting and cleaning up of its book seen in prior quarters along with the current weak environment for several corporate segments is an overhang for the stock, which is likely to keep upsides limited. Capital burn has also been higher than anticipated (CET-1 erodes by 189 BPS since Q4FY2019) and the bank has indicated that it will be looking to have growth capital infusion in FY2020E, delay in which may impact growth rates. Going ahead, we believe asset quality is likely to be the key monitorable in the medium term.

Valuation

BoB currently trades at <1.0x its FY2021E book value. However, post the merger, the growth outlook has weakened and asset-quality performance is still facing challenges. Considering the risks, we maintain our Hold rating with a revised PT of Rs. 120.

One-year forward P/BV (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP	P/BV(x)		P/E(x)		RoE (%)		RoA (%)	
	Rs/share	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Bank of Baroda	110	0.8	0.7	7.1	5.8	9.6	11.5	0.6	0.7
Bank of India	75	0.8	0.8	14.0	9.6	4.5	7.6	0.3	0.4
State Bank of India	341	1.5	1.4	19.3	15.2	6.9	8.3	0.4	0.5
Punjab National Bank	66	0.6	0.5	4.0	3.3	9.7	14.6	0.4	0.4

Source: Company, Sharekhan Estimates

About company

Bank of Baroda (BoB), established in 1908, is amongst the oldest commercial banks in India with a substantial footprint in the domestic and international markets. BoB has a wide presence overseas with almost one-third of the total business, coming from its international business. As of June 2019, BoB has a network of 9,444 domestic branches and 13,158 ATMs. The Bank has a significant international presence with a network of 100 overseas offices spanning 21 countries. The Bank has wholly owned subsidiaries including BOB Financial Solutions Limited (erstwhile BOB Cards Ltd.) and BOB Capital Markets. Bank of Baroda also has joint ventures for life insurance with India First Life Insurance and for asset management with Baroda Pioneer Asset Management. It has recently merged with Vijaya Bank (BS Size of Rs 1,77,847 crore) and Dena Bank (BS Size of Rs 1,20,860 crore) as of Mar 2018 to create an amalgamated entity and hence previous quarters will not be strictly comparable.

Investment theme

Bank of Baroda has a network of over 9,000+ branches, spread across the country and abroad, along with a diversified products and services portfolio and strong client relationships. Performance in terms of business growth as well as profitability and asset-quality improvement is gradual but in the desired direction. Notwithstanding the synergies that will accrue over a longer period, we believe near-term challenges in terms of asset quality and integration issues of merged entity may mute medium-term performance. Its strategy of business restructuring (reducing low yields business) and also the decision to gradually tone down the Off balance sheet exposure / foreign lending will be positive. Over the past two years, management has implemented significant structural changes in credit, risk management, technology, HR division and liability branches rationalisation as well, which are likely to continue post-merger in the integration phase, the benefits of which will be reaped in future but may keep upsides in a range in the medium term.

Key Risks

Capital burn has also been higher than anticipated (CET-1 erodes by 189 BPS since Q4FY2019) and the bank has indicated its requirement of growth capital infusion in FY2020E – a delay in which may impact growth rates.

Additional Data

Key management personnel

Dr. Hasmukh Adhia	Non-Executive Chairman
Shri P. S. Jayakumar	Managing Director & CEO
Smt. Papia Sengupta	Executive Director
Shri S. L. Jain	Executive Director
Shri Vikramaditya Singh Khichi	Executive Director

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Republic of India	43.50
2	HDFC Asset Management Co Ltd	4.00
3	Reliance Capital Trustee Co Ltd	3.50
4	Life Insurance Corp of India	2.70
5	ICICI Prudential Asset Management	2.10
6	Theleme Master Fund Ltd	2.10
7	Edgbaston Asian Equity Tru	0.70
8	Vanguard Group Inc/The	0.60
9	FIL Ltd	0.50
10	Dimensional Fund Advisors LP	0.40

Source: Bloomberg

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