

Bank of Baroda (BOB IN)

Concerns put to rest

INDIA | BANKING | Quarterly Update

15 February 2016

Top takeaways from Q3FY16

- BOB reported a loss of Rs 33.4bn due to slippages amounting to Rs 156bn as a result of RBI's asset quality review (AQR). It has recognized entire pain in one go, leaving no uncertainty for the future.
- Operating performance suffered as pre-provision profit declined 27% yoy to Rs 17bn, led by fall in NII (-18% yoy) and weak growth in non-interest income (2.1% yoy).
- Slippage spiked at Rs 156bn (H1 slippages was Rs 88bn), as a result GNPA increased 412bps qoq to 9.68%, and increase in NNPA 259 bps qoq to 4.12%.

Key highlights

- NII declined 4.6% yoy Rs 32.4bn due to weak loan growth (+7.6% yoy) and decline in NIM by 48 bps qoq 32bps yoy to 2.08%. Sequential compression in NIM is due to interest reversal owing high slippage.
- Weak growth in non-interest income due to flattish fee income of Rs 2.9bn (0.2% yoy), recovery from written-off assets at Rs 0.2bn (-33%) and forex income at Rs 2.9bn (14% yoy).

Management comments / concall takeaways

- AQR related Slippages amounted to Rs 105bn of which Rs 31bn was recognized in Q2 and Rs 74bn was recognized in Q3. Going forward, slippages will return to normal level.
- The stock of 5:25 refinance scheme and SDR is at Rs 54bn (standard Rs19bn) and Rs 24bn (standard Rs5bn) respectively. SMA-2 a/c reduced to Rs 150bn (Rs 300bn in Q1)
- CAR is comfortable at 12.2% (tier-1 of 9.57%) to grow business in near term, hence will not request capital from govt, and will avoid equity dilution for next 12-18 months.
- Will look to improve capital position by divestment in non-core investment, rebalancing the portfolio and bringing down unutilised credit lines.
- Management expects to grow the business with focus on profitability. Internal target to reach RoE of 8-12% in FY17 & 16% by FY18.

Outlook and valuation: Profitability to remain key focus area which may result some change in loan portfolio. The loan book may remain subdued as the bank trims down non profitability business like buyer's credit. The issue of asset quality as well as overhang pertaining to equity dilution has been arrested by the management. We believe the bank is well capitalized to grow for next 18-24 months and reach ~13% RoE by FY18. At CMP of Rs114, the stock trades at 1x FY17E ABVPS of Rs116 and 0.8x ABVPS of Rs143. Given the deterioration on asset quality, we cut our price target from Rs210 to Rs140. Maintain our Buy rating on the stock.

(Rs bn)	Q3FY16	Q3FY15	yoy %	Q2FY16	qoq %	vs. expect. %	Comments
Net interest income	27.1	32.9	-17.7	32.4	-16.6	-16.8	NII declined due to interest reversals on higher slippage
NIM (%)	1.7	2.2	(48bps)	2.1	(36bps)	(38bps)	Base rate cut and interest reversal resulted in lower yields impacting NIM
Advances	3843	3936	-2.4	4149	-7.4	-7.9	Decline led by fall in SME credit and weak growth in corporate loans
Corporate advances	1181	1175	0.5	1320	-10.5		
Retail advances	517	487	6.1	522	-0.9		Home loans contributed the most in retail loans.
Deposit	5897	5646	4.4	6125	-3.7	-1.9	Term deposit grew 8% yoy and CASA deposit declined 5% yoy
CASA	1415	1491	-5.1	1541	-8.2		Current account declined 32%, while savings account grew 7% yoy
CASA %	29.1	32.4	(330bps)	32.0	(285bps)		
Core fee	8.5	8.1	4.6	8.4	0.9		Weak growth in commission, exchange and brokerage led to weak growth
Trading gain	2.4	2.4	-1.1	2.2	7.5		
Operating expenses	21.1	20.4	3.8	20.5	3.1	1.9	Staff expenses increased 3% yoy, other opex increased 5% yoy
Cost to income ratio (%)	59.1	49.3	980bps	49.3	984bps		
Provision	61.6	12.6	388.4	18.9	225.9	242.5	NPA (Rs 65bn)/ Inv. depreciation (Rs 0.3bn)/ Standard provision (Rs -3.7bn)
PAT	-33.4	3.3	Na	1.2	Na	-1141.7	Higher NPA and weak operating performance result in net loss
Slippage	156.0	31.4	397.7	18.5	742.3		AQR led to high slippages (Total AQR Rs 105 bn – Q2 Rs26bn; Q3 Rs74bn)
GNPA	9.7	3.9	583bps	5.6	412bps		
NNPA	5.7	2.1	356bps	3.1	259bps		Provision Coverage ratio declined 553bps to 52.7%
Tier 1 Capital %	12.2	9.6	257bps	9.9	226bps		

Buy (Maintain)

CMP RS 114 / TARGET RS 140 (+23%)

COMPANY DATA

O/S SHARES (MN) :	2304
MARKET CAP (RSBN) :	267
MARKET CAP (USDBN) :	3.9
52 - WK HI/LO (RS) :	216 / 113
LIQUIDITY 3M (USDMN) :	13.6
PAR VALUE (RS) :	10

SHARE HOLDING PATTERN, %

	Sep 15	Jun 15	Mar 15
FII / NRI :	59.2	57.5	57.5
FI / MF :	12.9	14.4	17.3
NON PRO :	21.2	20.7	17.8
PUBLIC :	1.0	1.0	0.9
GOVT :	6.5	7.2	7.3

Key Financials

Rs mn	FY16E	FY17E	FY18E
Pre-prov ROE (%)	21.3	25.2	29.6
Pre-prov ROA (%)	1.2	1.3	1.5
Net Profit	-15	35	54
% growth	-145.6	-327.4	54.0
Adj BVPS (Rs)	102.4	116.0	142.8
ROE (%)	(4.0)	8.9	12.7
P/E (x)	-17.0	7.5	4.9
Adj P/BV (x)	1.11	0.98	0.80
EPS (Rs)	-6.7	15.2	23.5

CHANGE IN ESTIMATES

Rs bn	Revised Est.		% Revision	
	FY16E	FY17E	FY16E	FY17E
NII	124	145	-5	-9
PPP	82	99	-10	-12
Core PAT	-15	35	-165	-14
EPS (Rs)	-7	15	-166	-10

Manish Agarwalla, Pradeep Agrawal, Pares Jain

Result update

(Rs mn)	Q3FY16	Q3FY15	yoy growth	Q2FY16	qoq growth
Interest earned	106,140	107,180	-1.0	111,564	-4.9
Interest expended	79,087	74,319	6.4	79,119	0.0
Net interest income	27,053	32,861	-17.7	32,445	-16.6
Net interest margin	1.72	2.20	-0.48	2.08	-17.31
Non-interest income	11,129	10,904	2.1	11,440	-2.7
Total Income	38,183	43,765	-12.8	43,885	-13.0
Total operating expenses	21,141	20,375	3.8	20,515	3.1
Payroll costs	11,548	11,198	3.1	10,440	10.6
Others	9,593	9,177	4.5	10,075	-4.8
Pre-provision Profit	17,041	23,390	-27.1	23,370	-27.1
Provisions & Contingencies	61,646	12,623	388.4	18,917	225.9
% Operating income	361.7	54.0	307.8	80.9	280.8
PBT	-44,604	10,768	Na	4,453	Na
Provision for Taxes	-11,184	7,428	-250.6	3,208	-448.6
% of PBT	25.1	69.0	-43.9	72.0	-47.0
Net Profit	-33,420	3,340	Na	1,245	Na
Equity	4,621	4,307	7.3	4,621	0.0
EPS, Rs	-72.3	7.8	Na	2.7	-Na
Advances	3,842,721	3,936,305	-2.4	4,148,998	-7.4
Deposits	5,896,872	5,645,997	4.4	6,124,578	-3.7
Advances / Deposits (%)	65.2	69.7	-4.6	67.7	-3.8
Gross NPAs	389,341	154,530	152.0	237,103	64.2
Gross NPAs (%)	9.7	3.9	5.8	5.6	4.1
Net NPAs	218,062	82,913	163.0	127,978	70.4
Net NPAs (%)	5.7	2.1	3.6	3.1	2.6
CAR – Total	12.2	12.4	-0.2	12.5	-0.3

Source: Company, PhillipCapital India Research

Financials

Income Statement

Y/E Mar, Rsbn	FY15	FY16e	FY17e	FY18e
Interest on Loans	308	303	318	363
Interest on Investments	97	109	120	134
Others	25	28	30	33
Total Interest Earned	430	439	468	529
Total Interest Expended	298	315	323	354
Net Interest Income	132	124	145	176
Total non-interest income	44	43	48	54
Total Income	176	167	193	229
Personnel Expenses	43	47	52	57
Other Expenses	34	38	42	46
Total Op expenses	77	85	94	103
Net Inc (Loss) before prov	99	82	99	126
Provision and contingencies	45	106	49	44
Net Inc (Loss) before tax	54	-24	50	82
Provision for Income Tax	20	-8	15	28
Net Profit	34	-15	35	54

Balance Sheet

Y/E Mar, Rsbn	FY15	FY16e	FY17e	FY18e
Assets				
Cash & Bal with RBI	1,484	1,368	1,504	1,655
Loans, Adv & Int accrued	4,281	4,146	4,644	5,341
Investments	1,266	1,459	1,615	1,827
Fixed Assets (Net)	29	31	34	37
Other assets	91	95	100	105
Total Assets	7,150	7,100	7,897	8,964
Liabilities				
Share capital	4	5	5	5
Reserves and Surplus	384	377	401	445
Hybrid Capital	19	21	23	25
Debt	102	107	112	118
Borrowing	232	255	280	308
Total Deposits	6,222	6,032	6,715	7,664
Other liab incld prov	177	294	352	392
Total Liabilities	7,150	7,100	7,897	8,964

Source: Company, PhillipCapital India Research Estimates

Valuation Ratios

	FY15	FY16e	FY17e	FY18e
Earnings and Valuation Ratios				
Pre-provision Operating RoAE (%)	26.9	21.3	25.2	29.6
RoAE (%)	9.2	(4.0)	8.9	12.7
Pre-provision Operating ROA (%)	1.4	1.2	1.3	1.5
RoAB (%)	0.5	(0.22)	0.48	0.65
EPS (Rs.)	15.3	(6.7)	15.2	23.5
Dividend per share (Rs.)	3.2	3.5	4.0	4.0
Book Value (Rs.)	179.6	169.0	179.3	197.8
Adj BV (Rs.)	148.9	102.4	116.0	142.8

Revenue Analysis

Interest income on IBA (%)	6.4	6.3	6.3	6.4
Interest cost on IBL (%)	4.7	4.9	4.8	4.6
NIM on IBA / AWF (%)	2.0	1.8	2.0	2.1
Core fee Inc / AWF (%)	0.4	0.4	0.4	0.4
Portfolio gains / Total Inc (%)	6.1	5.4	4.0	2.9
Op.Exp / TI (%)	46.3	53.6	50.5	46.2
Op.Exp / AWF (%)	1.1	1.2	1.3	1.2
Employee exps / Op exps (%)	55.5	55.1	55.1	55.1
Tax / Pre-tax earnings (%)	37.3	35.0	30.0	34.0

Asset Quality

GNPAs / Gr Adv (%)	3.8	9.1	8.4	7.1
NNPAs / Net Adv (%)	1.9	5.1	4.4	3.3

Growth Ratio

Loans (%)	7.8	(3.1)	12.0	15.0
Investments (%)	4.9	15.3	10.6	13.2
Deposits (%)	8.7	(3.0)	11.3	14.1
Networth (%)	10.7	(2.0)	6.1	10.3
Net Int Income (%)	10.2	(6.0)	17.0	21.1
Non-fund based income (%)	(8.7)	2.4	16.1	17.0
Non-Int Exp (%)	7.5	10.8	10.0	10.0
Profit Before Tax (%)	(1.4)	(144.0)	(311.2)	63.3
Net profit (%)	(24.1)	(145.6)	(327.4)	54.0

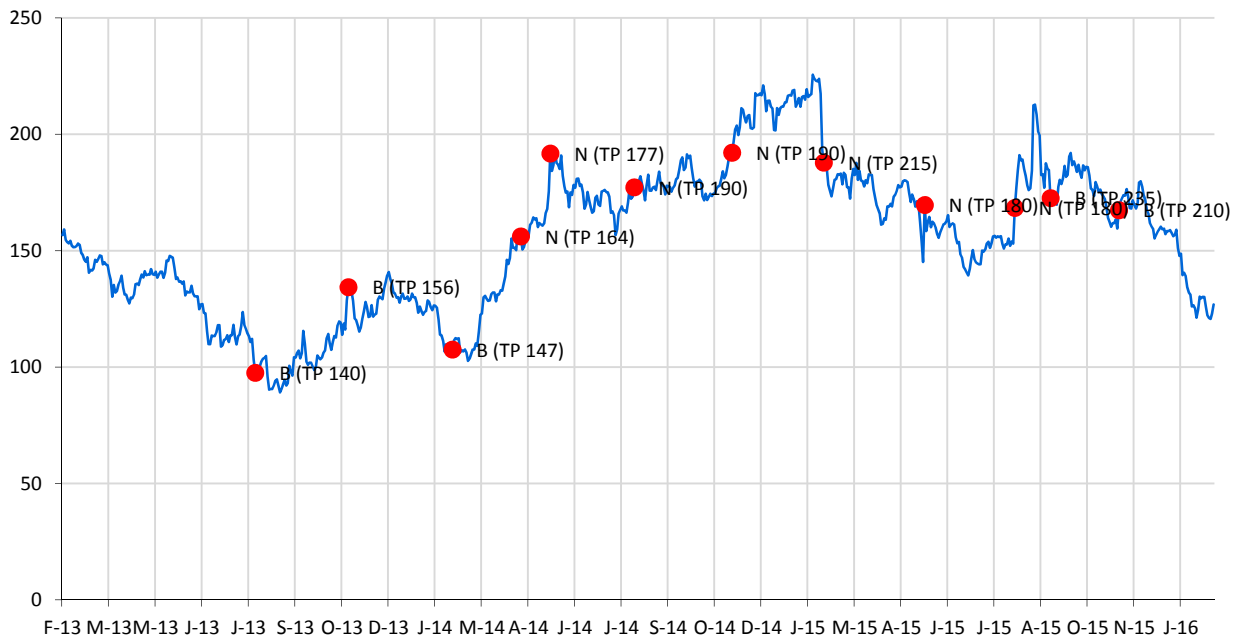
Asset / Liability Profile

Avg CASA / Deposits (%)	25.9	25.8	25.4	25.6
AvgAdv / AvgDep (%)	66.7	64.4	62.9	64.1
AvgInvst / AvgDep (%)	20.7	22.2	24.1	23.9
IncrAdv / Deposits (%)	62.6	70.8	72.9	73.4
Avg Cash / AvgDep (%)	23.4	23.3	22.5	22.0

Capital Adequacy Ratio:

Tier I (%)	12.6	12.5	12.0	11.5
Tier I (%)	9.9	9.8	9.4	9.2
Internal Capital Generation rate (%)	7.7	(6.1)	6.8	11.1
NNPAs to Equity (%)	20.3	52.4	46.9	36.8

Stock Price, Price Target and Rating History



Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	$\geq +15\%$	Target price is equal to or more than 15% of current market price
NEUTRAL	$-15\% > \text{to} < +15\%$	Target price is less than +15% but more than -15%
SELL	$\leq -15\%$	Target price is less than or equal to -15%.

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