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## AJCON NEWSLETTER

Volume I

### VIEW ON INDIAN EQUITY MARKETS



Currently Indian equity markets are trading at P/E of 17x. Sensex has corrected from a peak of 21,000 levels in November 2010 and touched 18,170 levels recently. We believe, markets has overreacted and factored in inflationary concerns and interest rate hike. Although markets may remain volatile in the near term, it would present investors with good buying opportunity. With due consideration to the fact that Chinese market is also trading at a P/E of 17x, interest in Indian markets would remain intact, going forward.

At current levels and on further dips of 1-3%, investors can consider investing in sectors like Banking, Capital goods (on account of reviving corporate capex cycle) and defensive sector like Pharmaceuticals. We like companies present in the banking and pharma space and believe that there are huge potential upsides, on which investors can cash in.

In the Banking space, players in the PSU space offer a good opportunity, while generic players targeting US market in the pharma space have a huge potential.

### SNAPSHOT OF MONETARY POLICY

The recent monetary policy was as per our expectations. With due consideration to macroeconomic factors, especially spike in inflation, Reserve Bank of India (RBI) was on a hawkish stance. RBI increased the repo and reverse repo rates by 25 basis points (bps) each.

The repo rate stands at 6.5 percent and the reverse repo rate at 5.5 percent. It has retained the cash reserve ratio

(CRR) at 6 percent of net demand and time liabilities (NDTL) of banks. Since mid-March 2010, the Reserve Bank has cumulatively increased the repo rate by 175 bps and the reverse repo rate by 225 bps. Additionally, the CRR was increased by 100 bps. Banks have responded to this calibrated tightening by raising their deposit and lending rates, suggesting strong monetary policy transmission.

We at Ajcon, believe, RBI's hawkish stance would not impact the performance of the banks significantly although inflationary concerns may put pressure on the economy going forward.

According to the RBI, while inflation is likely to soften in the coming months, it is likely to stay elevated above the earlier anticipated path. It had earlier projected overall inflation to be at 5.5 percent by March end, but overall inflation for December shot up to 8.43 percent on high prices of food items, from 7.48 percent in November. Continued high food inflation is the main cause for the overall inflation holding up. The central believes that return of inflation to a more acceptable level would be gradual.

RBI has also raised the March 2011 inflation forecast to seven percent from 5.5 percent and warned that higher food prices could become entrenched if steps to boost output are not taken. The Wholesale Price Index (WPI) in December rose to 8.4 percent and October gains were raised to 9.1 percent. Food prices are advancing at more than 15 percent.

The policy measures are aimed to contain the spill over from rise in food and fuel prices to generalized inflation, control inflationary pressures, which may be aggravated by food price rise.

We believe, 8.9% GDP growth in H1FY11 indicates that economy is operating close to RBI's growth guidance. This growth is mainly attributable to strong domestic factors, viz., a) good agricultural growth, b) strong export performance in recent months.

We are bullish on PSU banks like State Bank of India, Bank of Baroda, Bank of India, Uco Bank, Indian Overseas Bank and in the private sector, we prefer Axis Bank for investors with a long term horizon.

## 1) STATE BANK OF INDIA (SBI)

**Good NII growth, improvement in NIMs:** The bank witnessed strong yoy growth of 43.3% and qoq growth of 11.5% to touch Rs.90.5 bn in Q3FY11. NIMs improved 18 bps on qoq basis to touch 3.6% in Q3FY11. Improvement in NIMs is on account of higher C/D ratio, increase in CASA to 48.2% (9MFY11) as compared to 46.7% as on March 2010, and higher yield on advances. Going ahead, NIMs are expected to be at current levels with an upward bias as large deposits that SBI had accumulated in December 2008 are due for repricing over CY11. In addition, SBI is aggressive in hiking deposit rates. This would help SBI to improve its NIMs in the future.

**Strong growth in advances:** Advances growth was robust in Q3FY11. It witnessed yoy growth of 19%. This was mainly driven by corporate segment which registered yoy growth of 28%, followed by 21% yoy growth in retail segment.

**Improvement in asset quality:** In Q3FY11, the bank's gross NPA's declined by 18 bps on qoq basis to touch 3.17%. Its provision coverage ratio stood at 64% and the bank guided on no need for provisions on teaser rate loans.

### SBI - Financial Summary (Rs in mn)

Particulars	FY09	FY10	9MFY11
NII	290,406	236,709	244,680
Net Profit	91,212	91,660	82,440
CAR (%)	13.8	13.4	13.2
Gross NPA (%)	3.3	3.3	3.2
Net NPA (%)	1.8	1.7	1.6
NIM (%)	2.8	2.7	2.8#
ROE(%)	17.1	14.8	14.9
ROA(%)	1.1	0.94	0.96
Book Value (Rs.)	913	1,039	-
EPS (Rs.)	143.7	144.4	173.1*
P/BV(x)	2.9	2.5	-

Note:\*Annualized, #Q3FY11

## 2) BANK OF BARODA (BOB)

**Advances driving NII growth, NIMs improving:** It witnessed qoq growth of 12.5% in its Net Interest Income (NII) to touch Rs. 22.9 bn in Q3FY11. This was mainly on account of 7.4% sequential growth in advances. Net Interest Margin (NIMs) have improved by 20 bps on yoy basis and touched 3.2% in Q3FY11. It was on account of decline in cost of funds by 16 bps on yoy basis.

**Decline in Gross NPAs, lower slippages:** In Q3FY11, the bank witnessed decline in NPAs by 11 bps to touch 1.32%. Incremental slippages were at ~1% for 9MFY11 (Rs12.3bn) which is much lower compared to peers like Bank of India, Punjab National Bank, Union Bank of India etc.

**SME segment driving advances growth:** The bank witnessed strong growth in advances mainly in SME and Retail segment. On a yoy basis, SMEs segment witnessed growth of 24.8% whereas retail segment clocked a growth of 32.8%. On an overall basis, advances grew by 32.7% on yoy basis and 7.4% on qoq basis.

**Key highlights:** Bank guided for 25% profit growth in FY11. Management is confident of maintaining domestic NIMs in the range of 3.4 - 3.5%

### BOB - Financial Summary (Rs in mn)

Particulars	FY09	FY10	9MFY11
NII	51,234	59,395	61,884
Net Profit	22,272	30,583	29,473
CAR (%)	14.1	15.0	12.5
Gross NPA (%)	1.3	1.4	1.3
Net NPA (%)	0.3	0.34	0.36
NIM (%)	2.6	2.4	3#
ROE(%)	18.7	21.9	23.5#
ROA(%)	1.1	1.2	1.3#
Book Value (Rs.)	351	413	460
EPS (Rs.)	60.9	83.7	107.8#
P/BV(x)	2.4	2.0	1.8

### 3) BANK OF INDIA (BOI)

**Good NII growth, improvement in NIMs:** It witnessed yoy growth of 33% and qoq growth of 12% in its Net Interest Income (NII). This was mainly on account of 23% yoy loan growth and 5% growth on qoq basis. Net Interest Margin (NIMs) have improved by 49 bps on yoy basis and touched 3.61% in Q3FY11.

Improvement in NIMs was attributable to expansion in yield on advances by 31bps on qoq basis and decline in cost of funds. We believe the bank's performance in terms of NIMs is robust as it has been able to achieve improvement, despite a fall in CASA by 12bps to touch 32.2% in Q3FY11.

**Improvement in asset quality:** The management achieved its guidance on its asset quality. On a qoq basis, the bank had a tighter control on slippages. Gross slippages were down 30 bps in Q3FY11 as compared to 60 bps in Q2FY11. Higher recoveries and upgrades resulted in sequential decline of 6.7% of Gross NPA's on absolute basis. Gross NPA and Net NPA stood at 2.36% and 0.88% respectively as against 2.64% and 1.14% in Q2FY11. Going ahead, the management expects asset quality to stabilize.

#### BOI - Financial Summary (Rs in mn)

Particulars	FY09	FY10	9MFY11
NII	54,989	57,560	55,034
Net Profit	30,073	17,411	19,951
CAR (%)	13.0	12.9	12.4
Gross NPA (%)	1.7	2.9	2.4
Net NPA (%)	0.4	1.3	0.9#
NIM (%)	2.7	2.3	3.6#
ROE(%)	31	14	16
ROA(%)	1.5	0.7	0.9*
Book Value (Rs.)	224	243	237
EPS (Rs.)	52.8	64.4	50.7*
P/BV(x)	1.9	1.8	1.8

Note: \*Annualized, #Q3FY11

### 4) UCO BANK

**Strong NII and PAT growth in Q3FY11:** The bank witnessed a significant yoy increase of 22% in its net profit in Q3FY11 to touch Rs. 3 bn. NII increased by 69.11% to touch Rs 10.6 bn in Q3FY11.

**Capital adequacy concerns overdone:** Capital infusion worth Rs. 11.3 bn by government in H1FY11 has helped the bank to address the woes of lower capital adequacy. As on December 2010, its capital adequacy stood at 13.02% as per Basel II.

**Improvement in NIMs:** NIMs registered an improvement of 87bps on yoy basis to touch 3.11% in Q3FY11. This was on back of lower cost of funds.

**Asset quality under pressure, NPAs rising:** In Q3FY11, net non-performing assets (NPAs) of the bank went up at 1.13% versus 0.89%. Gross NPAs too were up at 2.57% versus 2.01% (yoy). Although the yields are improving, which may put pressure on NIMs; the bank is confident of protecting the NIMs at ~3%, going forward.

**Better performance expected in Q4FY11:** With steady improvement in NII, and focused efforts on recoveries, the bank is expected to improve its asset quality from next quarter onwards.

#### UCO Bank - Financial Summary (Rs in mn)

Particulars	FY09	FY10	9MFY11
NII	16,447	23,241	30,006
Net Profit	5,577	10,121	6,806
CAR (%)	11.9	13.2	13.0
Gross NPA (%)	2.2	1.9	2.6
Net NPA (%)	1.18	1.17	1.1
NIM (%)	2.30	2.26	3.1
ROE(%)	19.9	28.0	18.8
ROA(%)	0.59	0.87	0.67*
Book Value (Rs.)	51	66	66
EPS (Rs.)	10.2	18.4	16.5*
P/BV(x)	2.1	1.6	1.6

## 5) INDIAN OVERSEAS BANK (IOB)

**Good NII growth, improvement in NIMs:** It witnessed yoy growth of 42.2% in its Net Interest Income (NII) to touch Rs. 7.9 bn. This was mainly on account of 26% yoy growth in advances, 800 bps higher than average industry YTD credit growth. Net Interest Margin (NIMs) has improved by 58 bps on yoy basis and touched 3.27% in Q3FY11. Improvement in NIMs was attributable to increase in CASA ratio by 102 bps on yoy basis to touch 30.97% in Q3FY11.

**Decline in NPAs:** The asset quality of the bank improved in Q3FY11. Gross NPAs declined from 4.47% as on March 2010 to 3.26% in Q3FY11. Net NPAs also witnessed a decline from 2.52% as on March 2010 to 1.51% in Q3FY11.

**Fund raising plans:** It plans to raise US\$1bn through a five year bond issue in the overseas market. In addition, it has also approached the government for a QIP issue.

**Key risks:** Higher NPAs as compared to industry, low RoA of 0.6%, inefficient execution in cleaning up of loan book by new management.

### IOB - Financial Summary (Rs in mn)

Particulars	FY09	FY10	9MFY11
NII	28,696	31,679	29,928
Net Profit	13,258	7,070	6,382
CAR (%)	13.2	14.8	13.5#
Gross NPA (%)	2.5	4.5	3.3#
Net NPA (%)	1.3	2.5	1.5#
NIMs (%)	2.7	2.6	3.3#
ROE(%)	24.8	11.5	10.0
ROA(%)	1.2	0.6	0.6
Book Value (Rs.)	109	117	117
EPS (Rs.)	24.3	13	15.6*
P/BV(x)	1.2	1.1	1.09

Note:\*Annualized, #Q3FY11

## 6) AXIS BANK

**Share of CASA deposits improving:** In Q3FY11, the bank witnessed CASA improving by 77bps on qoq basis to touch 42.3%. This was on account of reduction in term deposits.

**Robust NII growth, improvement in NIMs:** It witnessed yoy growth of 45.7% in its Net Interest Income (NII) to touch Rs. 17.3 bn in Q3FY11. This was mainly on account of 45.7% growth in advances. Segments like corporate loans, mortgages and personal loans were the key drivers for robust growth of advances.

Net Interest Margin (NIMs) has improved by 13 bps on yoy basis and touched 3.8% in Q3FY11. Improvement in NIMs was mainly attributable to decline in cost of funds by 16 bps on yoy basis. Management expects some pressure in NIMs going forward. It expects a sequential decline of 15-20 bps in Q4FY11.

**Lower slippages, improving asset quality:** Slowdown in slippage rate from 1.5% in FY10 to 1.1% in Q3FY11 resulted in lower slippages in this quarter. Slippages stood at Rs. 3.3 bn which indicates a strong improvement in the banks provision coverage ratio (PCR). PCR has improved by 400bps to touch 74% in Q3FY11.

### AXIS Bank - Financial Summary (Rs in mn)

Particulars	FY09	FY10	9MFY11
NII	36,862	50,045	48,620
Net Profit	18,154	25,144	23,684
CAR (%)	13.7	15.8	12.5
Gross NPA (%)	0.9	1.1	1.1
Net NPA (%)	0.4	0.4	0.3
NIM (%)	2.9	3	3.8#
ROE(%)	19.1	19.2	-
ROA(%)	1.4	1.5	1.6*
Book Value (Rs.)	277	384	454
EPS (Rs.)	50.6	62.1	76*
P/BV(x)	4.5	3.3	2.8

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