

January 27, 2012

| | |
|--------------------------|----------------------|
| Reco | Previous Reco |
| Reduce | Hold |
| CMP | Target Price |
| Rs353 | Rs320 |
| EPS change FY12E/13E (%) | 14.7/5.8 |
| Target Price change (%) | NA |
| Nifty | 5,205 |
| Sensex | 17,234 |

Price Performance

| (%) | 1M | 3M | 6M | 12M |
|---------------|----|----|-----|------|
| Absolute | 28 | 11 | (9) | (23) |
| Rel. to Nifty | 16 | 11 | (4) | (17) |

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

| | |
|-----------------------------|-----------|
| Sector | Banks |
| Bloomberg | BOI@IN |
| Equity Capital (Rs mn) | 5465 |
| Face Value(Rs) | 10 |
| No of shares o/s (mn) | 546 |
| 52 Week H/L | 498/261 |
| Market Cap (Rs bn/USD mn) | 193/3,913 |
| Daily Avg Volume (No of sh) | 731289 |
| Daily Avg Turnover (US\$m) | 4.7 |

Shareholding Pattern (%)

| | Dec-11 | Sep-11 | Jun-11 |
|--------------|--------|--------|--------|
| Promoters | 65.9 | 65.9 | 65.9 |
| FII/NRI | 15.7 | 15.3 | 15.5 |
| Institutions | 11.9 | 12.4 | 12.4 |
| Private Corp | 1.0 | 0.8 | 0.7 |
| Public | 5.6 | 5.7 | 5.6 |

Source: Capitaline

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- BOI's Q3FY12 PAT at Rs7.2bn ahead of estimates driven by higher than expected NII at Rs20.7bn and higher than expected recoveries (3x yoy and 2x qoq)
- Loans grew aggressively 6.2% qoq led by foreign (weak INR) and sharp growth in retail+agri (7.6% qoq), CRE (11% qoq) and infrastructure (20% qoq)
- Though reported slippages came off sharply to Rs5.2bn, it is net of some recoveries. Actual gross slippages ~Rs8-9bn. Sharp rise in restructuring ex-GTL at Rs17.6bn
- Net NPL/networth still stands at 21%, RoAs may still not look beyond 1% in FY13E due to elevated credit costs. Downgrade to REDUCE with TP of Rs320

Better P&L numbers; slippages come off but restructuring pains

BOI's Q3FY12 NII at Rs20.7bn was marginally above our estimates. NII growth at 4.1% yoy was led by 6% qoq growth in loan portfolio and 13bps yoy improvement in NIMs. Further sequential doubling of in recoveries aided net profit growth of 45% qoq to Rs7.2bn.

The slippage came off sharply to Rs5.2bn for the quarter. However, we believe that these may also be after netting off the recoveries from the slippages of H1FY12. The actual slippages for the quarter may have been Rs10bn. These also include Rs5.1bn from one single account in aviation. Though, the NPA profile improved, the restructuring took off all the sheen with the advances worth Rs17.6bn (ex-GTL) being restructured during the quarter. Thus, the stressed assets (net NPLs+restr assets) went up to 7.7% of advances vs 7.2% in Q2FY12.

Yield analysis

| % | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (bps) | QoQ (bps) |
|--------------------|--------|--------|--------|--------|--------|-----------|-----------|
| Yield on assets* | 7.4 | 7.8 | 7.6 | 7.9 | 8.0 | 56 | 9 |
| Cost of funds* | 4.7 | 4.9 | 5.5 | 5.7 | 5.7 | 95 | -4 |
| NIM* | 2.7 | 2.8 | 2.1 | 2.2 | 2.3 | -39 | 13 |
| Yield on Advances# | 8.8 | 8.8 | 8.9 | 9.4 | 9.5 | 67 | 4 |
| Yield on Funds# | 7.4 | 7.8 | 7.6 | 8.1 | 8.0 | 56 | -7 |
| Cost of Deposit# | 5.0 | 5.3 | 6.0 | 6.1 | 6.0 | 99 | -13 |
| Cost of funds# | 4.7 | 4.9 | 5.5 | 5.6 | 5.7 | 95 | 8 |
| NIM# | 3.1 | 2.9 | 2.2 | 2.4 | 2.6 | -54 | 11 |
| NIM-Domestic# | 3.5 | 3.4 | 2.4 | 2.8 | 2.9 | -58 | 14 |
| NIM-Foreign# | 1.5 | 1.2 | 1.2 | 1.2 | 1.4 | -7 | 18 |

Source: Company, Emkay Research Note:* Calculated on basis of average quarterly balances # reported

Valuation table

| Y/E March 31 | Net income | Net profit | EPS (Rs) | ABV (Rs) | RoA (%) | RoE (%) | PE (x) | P/ABV (x) |
|--------------|------------|------------|----------|----------|---------|---------|--------|-----------|
| FY2010 | 83,726 | 17,410 | 33.1 | 201.4 | 0.7 | 14.2 | 11.1 | 1.8 |
| FY2011 | 104,524 | 24,885 | 45.5 | 256.3 | 0.8 | 17.3 | 7.8 | 1.4 |
| FY2012E | 111,368 | 27,737 | 50.7 | 252.5 | 0.7 | 16.2 | 7.0 | 1.4 |
| FY2013E | 128,983 | 35,138 | 64.2 | 317.1 | 0.8 | 17.8 | 5.5 | 1.1 |

Source: Company, Emkay Research

Key financials – Quarterly

| Rs mn | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (%) | QoQ (%) | YTD' 12 | YTD' 11 | YoY (%) |
|--------------------------|--------|--------|--------|--------|--------|---------|---------|---------|---------|---------|
| Net Interest Income | 19,869 | 23,072 | 18,410 | 19,039 | 20,674 | 4.1 | 8.6 | 58,123 | 55,034 | 5.6 |
| Other Income | 6,483 | 8,230 | 6,601 | 8,418 | 8,522 | 31.4 | 1.2 | 23,541 | 18,188 | 29.4 |
| <i>Fee Income</i> | 2,838 | 3,465 | 2,737 | 3,258 | 3,204 | 12.9 | -1.7 | 9,199 | 8,345 | 10.2 |
| Net Income | 26,352 | 31,302 | 25,011 | 27,457 | 29,196 | 10.8 | 6.3 | 81,663 | 73,222 | 11.5 |
| Total Operating Expenses | 12,464 | 19,251 | 11,051 | 11,942 | 11,878 | -4.7 | -0.5 | 34,871 | 31,431 | 10.9 |
| As % Of Net Income | 47.3 | 61.5 | 44.2 | 43.5 | 40.7 | | | 42.7 | 42.9 | |
| Employee Expenses | 8,369 | 14,616 | 7,000 | 7,275 | 7,589 | -9.3 | 4.3 | 21,864 | 20,138 | 8.6 |
| As % Of Net Income | 31.8 | 46.7 | 28.0 | 26.5 | 26.0 | | | 26.8 | 27.5 | |
| Other Expenses | 4,094 | 4,635 | 4,052 | 4,667 | 4,289 | 4.8 | -8.1 | 13,007 | 11,293 | 15.2 |
| As % Of Net Income | 15.5 | 14.8 | 16.2 | 17.0 | 14.7 | | | 15.9 | 15.4 | |
| Operating Profit | 13,888 | 12,051 | 13,959 | 15,515 | 17,318 | 24.7 | 11.6 | 46,792 | 41,791 | 12.0 |
| As % Of Net Income | 52.7 | 38.5 | 55.8 | 56.5 | 59.3 | | | 57.3 | 57.1 | |
| Provisions | 4,979 | 4,777 | 5,672 | 11,544 | 5,431 | 9.1 | -53.0 | 22,647 | 14,112 | 60.5 |
| <i>Prov for NPA</i> | 1,236 | 3,367 | 3,880 | 8,240 | 3,330 | 169.4 | -59.6 | 15,450 | 7,177 | 115.3 |
| PBT | 8,909 | 7,274 | 8,287 | 3,971 | 10,387 | 16.6 | 161.6 | 22,645 | 27,679 | -18.2 |
| Total Tax | 2,377 | 2,340 | 3,111 | -940 | 3,227 | 35.8 | -443.4 | 5,398 | 7,727 | -30.1 |
| Adjusted PAT | 6,533 | 4,934 | 5,176 | 4,911 | 8,194 | 25.4 | 66.9 | 18,281 | 19,953 | -8.4 |
| Extra Ordinary Items | 0 | 0 | 0 | 0 | 1,500 | | | 1,500 | 0 | |
| Reported PAT | 6,533 | 4,934 | 5,176 | 4,911 | 7,160 | 9.6 | 45.8 | 17,247 | 19,953 | -13.6 |
| Reported EPS | 12.4 | 9.0 | 9.5 | 9.0 | 13.1 | 5.3 | 45.8 | 31.5 | 37.9 | -16.9 |

Source: Company, Emkay Research

NIM expansion led by higher yields and controlled costs

The calculated NIMs (BOI reports spreads) expanded by 13bps qoq to 2.3% for couple of reasons:

- The international book which grew by 18% qoq was shifted in favour of ECBs vs trade finance earlier, resulting in 30bps qoq expansion in yields. However, this also reflected in higher RWA/TA
- Cost of domestic deposits remained stable at 7.1% driven by the redemption of high cost term deposits even as the domestic advances yields improved by 20bps due to increase in base rate last quarter

Weak INR/ECB and domestic- retail/agri drive loan growth

Loan growth at 19.5% (6.2% qoq) was primarily driven by strong growth on the international front (67% yoy / 18.1% qoq). A large part of growth on international front was due to INR depreciation and ECB financing. On the domestic front, loan portfolio at Rs1.6tn remained flat qoq (up mere 6% yoy).

However, within domestic loan book too, the mix tilted more in favor of retail+agri which grew by 7.6% qoq. Within industry, the growth was driven by three key industries, viz., CRE (11% qoq), infrastructure (20% qoq) and metal products (6% qoq)

Advances mix

| Rs bn | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (%) | QoQ (%) |
|-------------------|--------------|--------------|--------------|--------------|--------------|-------------|------------|
| Foreign | 419 | 510 | 538 | 591 | 698 | 66.8 | 18.1 |
| Mid-corporate/SME | 279 | 356 | 339 | 305 | 312 | 11.8 | 2.1 |
| Agriculture | 205 | 227 | 222 | 196 | 208 | 1.2 | 5.8 |
| Retail | 156 | 166 | 163 | 164 | 180 | 15.3 | 9.8 |
| Others | 869 | 902 | 887 | 913 | 934 | 7.5 | 2.3 |
| Total | 1,928 | 2,162 | 2,149 | 2,170 | 2,304 | 19.5 | 6.2 |

Source: Company, Emkay Research

Note: There has been some re-classification between retail and agri as well as the infrastructure loans. Hence, the numbers on yoy and qoq basis are not comparable

But it also drives RWAs faster than total assets

Due to shift in the international loan book in favor of ECB from trade finance also drove up the RWA/TA ratio from 58-59% over last couple of quarters to 61%.

Strong SB growth and lower term deposits drive CASA

The deposits for the quarter were mainly driven by foreign deposits growth. However, commendably, the savings deposits grew by 14% qoq. Besides, with redemption of some high cost domestic term deposits, the CASA mix improved by 80bps qoq.

CASA Mix

| Rs bn | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (%) | QoQ (%) |
|------------------------|--------|--------|--------|--------|--------|---------|---------|
| Savings Deposits | 136 | 144 | 153 | 131 | 150 | 9.9 | 13.9 |
| Current Deposits | 557 | 587 | 588 | 635 | 636 | 14.3 | 0.1 |
| CASA | 693 | 731 | 742 | 767 | 786 | 13.4 | 2.5 |
| Domestic term deposits | 1,454 | 1,798 | 1,714 | 1,679 | 1,657 | 13.9 | -1.3 |
| Foreign deposits | 378 | 459 | 475 | 545 | 630 | 66.6 | 15.5 |
| Total Deposits | 2,525 | 2,989 | 2,931 | 2,991 | 3,073 | 21.7 | 2.7 |
| CASA (%) | 32.3 | 28.9 | 30.2 | 31.3 | 32.2 | -10 | 82 |

Source: Company, Emkay Research

But it may have relied heavily on borrowings

We believe that BOI may have relied heavily on the borrowings during the quarter as

- There is a negative entry in the other interest income of Rs451mn, which may imply that BOI was net borrower in inter-bank money market
- The interest paid on borrowings is up 30% qoq
- The calculated cost of borrowings in up 200bps qoq to 10.7%

Higher recoveries help other income

Other income at Rs8.5bn (up 31%yoy/1.2%qoq) was primarily driven by improved recoveries from w/off accounts which jumped 3x yoy and doubled qoq.

Other income

| Rs mn | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (%) | QoQ (%) | YTD' 12 | YTD' 11 | YoY (%) |
|------------------------|--------------|--------------|--------------|--------------|--------------|-------------|------------|---------------|---------------|-------------|
| Fee/Commission income | 2,838 | 3,465 | 2,737 | 3,258 | 3,204 | 12.9 | -1.7 | 9,199 | 8,345 | 10.2 |
| Trading gains/(losses) | 592 | 1,267 | 1,097 | 1,544 | 712 | 20.3 | -53.9 | 3,353 | 1,952 | 71.8 |
| Forex gains/(losses) | 1,271 | 1,333 | 1,471 | 1,483 | 1,239 | -2.5 | -16.5 | 4,193 | 3,692 | 13.6 |
| Recoveries | 658 | 918 | 312 | 876 | 1,858 | 182.4 | 112.1 | 3,046 | 1,329 | 129.2 |
| Other non int income | 1,124 | 1,247 | 984 | 1,257 | 1,509 | 34.2 | 20.0 | 3,750 | 2,870 | 30.6 |
| Total | 6,483 | 8,230 | 6,601 | 8,418 | 8,522 | 31.4 | 1.2 | 23,541 | 18,188 | 29.4 |

Source: Company, Emkay Research

Higher recoveries help NPAs but restructured assets spike up

The slippages at Rs5.2bn were a sharp positive surprise. However, we will take that with a pinch of salt for few reasons:

- The slippages for the quarter have been reported after netting off the recoveries from H1FY12 slippages. Since, the slippages in just H1FY12 are 28% higher than FY11, we believe that recoveries from technical/small NPAs in H1FY12 would be significant
- The slippages from restructured assets was at Rs5.9bn, higher than Rs5.2bn total slippages implying that (a) above is plausible assumption
- Of the Rs5.2bn slippages, Rs5.1bn has come from one restructured account (aviation) slipping into NPA. Hence, the residual NPAs are just paltry Rs80mn

Hence, we believe that the actual gross slippages would be at least Rs10bn or more vis-à-vis reported number of Rs5.2bn.

Still, the restructured advances took the sheen completely out of good show on slippages. Even adjusted for restructuring of the GTL account, the residual restructuring advances are Rs17.5bn for Q3FY12. Thus, despite net NPL improving by 20bps to 1.8%, the total stresses assets moved up from 7.2% in Q2FY12 to 7.7% in Q3FY12.

NPA profile

| Rs mn | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (%) | QoQ (%) |
|------------------------|--------|--------|--------|--------|--------|---------|---------|
| Gross NPA (Rs mn) | 45,421 | 48,116 | 57,910 | 65,481 | 63,860 | 40.6 | -2.5 |
| Net NPA (Rs mn) | 16,603 | 19,450 | 26,897 | 42,446 | 40,931 | 146.5 | -3.6 |
| Gross NPA (%) | 2.4 | 2.2 | 2.7 | 3.0 | 2.7 | | |
| Net NPA (%) | 0.9 | 0.9 | 1.3 | 2.0 | 1.8 | | |
| Net NPLs/Net worth (%) | 10.2 | 11.2 | 15.1 | 22.8 | 20.9 | | |
| Provision cover (%) | 63.4 | 59.6 | 53.6 | 35.2 | 35.9 | | |

Source: Company, Emkay Research

Slippages

| Rs mn | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 | YoY (%) | QoQ (%) |
|--------------------|--------|--------|--------|--------|--------|---------|---------|
| Cumulative (Rs mn) | 19,129 | 29,122 | 16,837 | 45,054 | 50,250 | 162.7 | 11.5 |
| Quarterly (Rs mn) | 4,765 | 9,993 | 16,837 | 28,217 | 5,196 | 9.0 | -81.6 |
| Cumulative (%) | 1.0 | 1.3 | 0.8 | 2.1 | 2.2 | | |
| Quarterly (%) | 0.2 | 0.5 | 0.8 | 1.3 | 0.2 | | |

Source: Company, Emkay Research

Low LLPs are a disappointment

Despite having seen sharply higher slippages in H1FY12, the LLPs continue to remain significantly low. The LLPs as % of advances for M9FY12 was at 90bps compared with net slippages (gross less reco/upgrades) were at 2.2%. Hence, the lower PCR at 40% of incremental net slippages was a disappointment.

Capital remains a constrain; growth rate to ease

As we highlighted earlier, BOI's tier I CAR went down by sharp 61bps to 7.65% due to change in portfolio mix in favor of retail and ECB financing. Including profits for M9FY12, the tier I CAR would be at 8.4% (8.25% if adjusted for dividends). Still, with very high net NPLs/net worth ratio (21%), the growth rate is likely to ease to 15% CAGR over FY11-13E. The management has already approached Gol for capital infusion.

Valuations and view

Bank of India has been grappling with concerns over its asset quality for long now. During Q3FY12, the slippages concerns seem abated for while. But still with low PCR (60%), we would expect BOI to run a higher credit cost at average 85bps over FY11-13E, thereby dragging RoAs.

However, we have upgraded our earnings estimates by 14.7% in FY12E and 5.8% in FY13E to take into account lower than expected provisioning done over M9FY12 (despite high NPL ratios). We haven't changed our slippages or recoveries estimates and hence, there is no change in the ABV estimates.

The stock is currently quoting at 1.4x FY12E/1.1x FY13E ABV. We believe that the stock has run up ahead of the fundamentals and is quoting at the same valuations and BOB and PNB. We downgrade the stock to REDUCE with target price to Rs320.

We believe upside risk to our estimates could arise (1) if there is lowering of pressure on growth if Net NPLs / net worth ratio (21%) comes down and (2) if credit costs continue to trail the slippage rate though not warranted. Also, any surprise in form of lower slippages / improved recoveries will act as a positive for the bank and take the valuations upwards.

Key Financials

Income Statement (Rs. Mn)

| (Year Ending Mar 31) | FY10 | FY11 | FY12E | FY13E |
|----------------------|--------|---------|---------|---------|
| Net interest income | 57,560 | 78,106 | 78,848 | 92,593 |
| Other income | 26,166 | 26,418 | 32,520 | 36,390 |
| Net income | 83,726 | 104,524 | 111,368 | 128,983 |
| Operating expenses | 36,678 | 50,683 | 48,357 | 52,084 |
| Pre provision profit | 47,048 | 53,841 | 63,011 | 76,899 |
| PPP excl treasury | 53,011 | 57,060 | 67,611 | 81,499 |
| Provisions | 22,110 | 18,889 | 25,016 | 25,974 |
| Profit before tax | 24,938 | 34,952 | 37,995 | 50,925 |
| Tax | 7,528 | 10,067 | 10,259 | 15,787 |
| Tax rate | 30% | 29% | 27% | 31% |
| Profit after tax | 17,410 | 24,885 | 27,737 | 35,138 |

Key Ratios (%)

| (Year Ending Mar 31) | FY10 | FY11 | FY12E | FY13E |
|-----------------------|------|------|-------|-------|
| NIM | 2.5 | 2.8 | 2.3 | 2.3 |
| Non-ll/avg assets | 1.0 | 0.8 | 0.9 | 0.8 |
| Fee income/avg assets | 0.4 | 0.4 | 0.4 | 0.4 |
| Opex/avg assets | 1.3 | 1.4 | 1.2 | 1.1 |
| Provisions/avg assets | 1.1 | 0.6 | 0.9 | 0.9 |
| PBT/avg assets | 0.9 | 1.0 | 1.0 | 1.1 |
| Tax/avg assets | 0.3 | 0.3 | 0.3 | 0.3 |
| RoA | 0.7 | 0.8 | 0.7 | 0.8 |
| RoAE | 14.2 | 17.3 | 16.2 | 17.8 |
| GNPA (%) | 3.1 | 2.5 | 2.9 | 2.6 |
| NNPA (%) | 1.3 | 0.9 | 1.8 | 1.3 |

Balance Sheet (Rs. Mn)

| (Year Ending Mar 31) | FY10 | FY11 | FY12E | FY13E |
|----------------------|-----------|-----------|-----------|-----------|
| Liabilities | | | | |
| Equity | 5,259 | 5,472 | 5,472 | 5,472 |
| Reserves | 137,041 | 167,435 | 190,050 | 219,426 |
| Net worth | 142,300 | 172,907 | 195,522 | 224,898 |
| Deposits | 2,297,619 | 2,988,858 | 3,401,278 | 4,067,776 |
| Borrowings | 309,745 | 349,960 | 380,290 | 412,432 |
| Total liabilities | 2,749,665 | 3,511,725 | 3,977,089 | 4,705,106 |
| Assets | | | | |
| Cash and bank | 312,301 | 373,100 | 322,908 | 405,034 |
| Investments | 649,440 | 831,037 | 1,019,122 | 1,245,497 |
| Customer assets | 1,706,269 | 2,158,649 | 2,476,024 | 2,880,005 |
| Others | 81,654 | 148,940 | 159,034 | 174,569 |
| Total assets | 2,749,665 | 3,511,725 | 3,977,089 | 4,705,106 |

Valuations Table

| (Year Ending Mar 31) | FY10 | FY11 | FY12E | FY13E |
|----------------------|--------|--------|--------|--------|
| Net profit (Rs mn) | 17,410 | 24,885 | 27,737 | 35,138 |
| Shares in issue (mn) | 526 | 547 | 547 | 547 |
| EPS (Rs) | 33.1 | 45.5 | 50.7 | 64.2 |
| PER (x) | 10.7 | 7.8 | 7.0 | 5.5 |
| FDEPS(Rs) | 31.8 | 45.5 | 50.7 | 64.2 |
| FDPER (x) | 11.1 | 7.8 | 7.0 | 5.5 |
| Book value (Rs) | 233.4 | 281.9 | 323.2 | 376.9 |
| P/BV (x) | 1.5 | 1.3 | 1.1 | 0.9 |
| Adj book value (Rs) | 201.4 | 256.3 | 252.5 | 317.1 |
| P/ABV (x) | 1.8 | 1.4 | 1.4 | 1.1 |
| P/PPP (x) | 3.9 | 3.6 | 3.1 | 2.5 |
| Dividend yield (%) | 2.0 | 2.0 | 2.3 | 2.5 |

Recommendation History: Bank of India – BOI IN

| Date | Reports | Reco | CMP | Target |
|------------|--|------------|-----|--------|
| 08/11/2011 | Bank of India Q2FY12 Result Update | Hold | 328 | 320 |
| 25/07/2011 | Bank of India Q1FY12 Result Update | Hold | 404 | 420 |
| 02/05/2011 | Bank of India Q4FY11 Result Update | Accumulate | 422 | 510 |
| 21/01/2011 | Bank of India Q3FY11 Result Update | Accumulate | 461 | 510 |

Recent Research Reports

| Date | Reports | Reco | CMP | Target |
|------------|--|------------|-----|--------|
| 25/01/2012 | Bank of Baroda Q3FY12 Result Update | Accumulate | 790 | 950 |
| 25/01/2012 | Union Bank of India Q3FY12 Result Update | Reduce | 207 | 210 |
| 24/01/2012 | Yes Bank Q3FY12 Result Update | Accumulate | 319 | 370 |
| 23/01/2012 | Federal Bank Q3FY12 Result Update | Accumulate | 383 | 425 |

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