RESULT UPDATE

STATE BANK OF INDIA

Gradually treading towards quality

India Equity Research| Banking and Financial Services

State Bank of India's (SBI) Q3FY13 PAT of INR33.9bn came lower than our estimate. The disappointment was largely on back of: (1) 46% QoQ jump in provisions to INR26.6bn—NPL led (INR27.6bn) and (2) slower traction at NII level (up 1.6% QoQ) largely led by stable margin (down 3bps QoQ) to 3.31%. Headline asset quality deteriorated with slippages higher at 3.4% (3.0% in Q2FY13). However, management indicated INR20bn accounts have already been upgraded during Q4FY13, adjusting for which slippages would have been modest (at 2.6%). Further upgrades (at INR18.4bn) are a positive; management expects higher run rate in Q4FY13. Loan book grew to INR10tn (up 5.6% QoQ)—large corporate group (power+ telecom) led CD ratio stands at 87%. Asset quality should improve as we anticipate FY14 to be year of economic recovery. SBI will be key beneficiary due to granular nature of its slippages. Maintain 'BUY'.

Note: This report contains Q3FY13/Q2FY13 analyst meet highlights

Adjusted slippages trending lower

SBI's slippages, adjusted for accounts to be restructured in Q4FY13 (INR20bn), came in at INR61.7bn, down QoQ. Segment-wise analysis indicates that pressure in retail, agri, large corporates and international banking is receding, whereas SME and mid-corporates' risks have stabilised. Going forward, management expects lower slippages (wholesale reversal) coupled with higher recoveries.

Restructured book at 2.4%; benefit of reclassification reaped

Restructuring during Q3FY13 came in at INR28bn. However, SBI reclassified INR150bn (accounts performing satisfactorily for two years) from restructured book, as per RBI guidelines, leading to outstanding restructured book at INR238bn (2.4% of advances). Restructuring pipeline stands at INR37bn (excluding Suzlon- INR13bn).

Outlook & valuations: Asset quality to improve; maintain 'BUY'

SBI's asset quality, though a stickier problem, is likely to be resolved as we believe FY14 will be a year of macro economic recovery. We expect RoA/RoE of 1.0%/15.4% on back of loan book CAGR of 18% over FY12-14E and NIMs (calc.) of ~3.2%. Adjusting INR230 for non-banking subsidiaries, SBI's banking business is trading at 1.2x FY14E P/ABV. Maintain **'BUY/Sector Outperformer'** with target price of INR2,779.

Financials (INR mn)

Year to March	Q3FY13	Q3FY12	*Growth %*	Q2FY13	*Growth %*	FY12	FY13E	FY14E
Net int. inc.	111,545	114,659	*(2.7)*	109,738	*1.6*	432,911	446,989	504,773
Net profit (INR mn)	33,961	32,631	*4.1*	36,581	*(7.2)*	117,073	144,775	162,477
B/V per share (INR)						1,251	1,442	1,639
EPS (INR)	50.6	51.4	*(1.5)*	54.5	*(7.2)*	174.5	211.5	237.4
Price/ Book (x)						1.8	1.5	1.4
Price/ Earnings (x)						12.7	10.5	9.3

EDELWEISS 4D RATINGS

Absolute Rating	**BUY**
Rating Relative to Sector	Outperformer
Risk Rating Relative to Sector	Low
Sector Relative to Market	Overweight

MARKET DATA *(R: SBI.BO, B: SBIN IN)*

CMP	: INR 2,216
Target Price	: INR 2,779
52-week range (INR)	: 2,552 / 1,802
Share in issue (mn)	: 671.0
M cap (INR bn/USD mn)	: 1,487/ 27,570
Avg. Daily Vol.BSE/NSE('000)	: 3,099.4

SHARE HOLDING PATTERN (%)

	Current	Q2FY13	Q1FY13
Promoters *	61.6	61.6	61.6
MF's, FI's & BK's	17.2	17.2	17.3
FII's	9.7	9.1	8.5
Others	11.5	12.1	12.6

** Promoters pledged shares (% of share in issue) : NIL*

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Banks and Financial Services Index
1 month	(11.4)	(2.1)	10.6
3 months	2.0	3.8	4.7
12 months	0.7	8.9	22.7

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Margin dip curtailed; outlook stable

SBI's yield on advances came in at 10.75% (down 12bps QoQ) riding on higher interest income reversal and aggressive rates on SME and industrial side. This, coupled with flattish cost of deposits, led to 6bps QoQ decline in domestic margin to 3.63%. However, global margins were reported at 3.31% (down only 3bps QoQ) largely supported by stable overseas margins at 1.42%. Management continues to maintain a stable margin outlook and expects to deliver 3.70-3.75% in domestic margin given the substantial relief on CRR and repo rates coupled with higher investment yield as substantial portion of HTM is maturing in coming quarters which are relatively at lower yield (average yield of ~7.35). Also, incremental benefit is to be derived, from higher CD ratio (currently stands at 87%)—it currently carries excess liquidity of INR500bn. We are building in margin of 3.2% over FY13-14.

Large corporate group aids advances rebound

Overall advances came in healthy at INR10tn (up 5.6%/16.1% QoQ/YoY). Within this, domestic book grew 13.8% and international 28.4% (24% adjusted for INR depreciation). The key driver was large corporates (at 25.8% YoY)—power + telecomm—with benefits also reaped from loans shifting from other competitors due to aggressive positioning of loans. The cautious stance on mid-corporates and SME is reflected in their muted annual growth rates. Management indicated that incremental lending to SME is largely towards guaranteed loans with smaller ticket sizes. Hence, the overall portfolio quality is improving. Also, with 80% of incremental agri advances—another pain point from the NPA angle (with 9.7% GNPA) coming by way of gold loans—currently stands at INR303bn (30% of overall agri book vis-à-vis 19% a year ago), which should aid asset quality. Management has indicated that it is has witnessed increased traction over the past three months with current run rate of ~17.2%, thereby making SBI confident of achieving 18% loan book growth for FY13. Deposit growth was healthy at 15.6% YoY to INR11.6tn. Domestic CASA inched up to 45.5% (up 60bps QoQ) due to traction in saving accounts, up 3.6% QoQ. However, this was offset to an extent by moderate current balances (flat QoQ). The bank expects to achieve deposit growth rate of 14% plus for FY13.

Fee income growth supported by higher trading profit

SBI reported non-interest income growth of 9% QoQ, largely on back of higher trading profits (up 81.5% QoQ)—impressive performance on bond portfolio. However, weakness continued in CEB income, which fell 3.2% YoY largely due to slowdown in government business (down ~29% YoY). We are building in fee income CAGR of 11% over FY12-14.

Controlled operating expenses aids bottom line

Operating expenses during the quarter came in modest at INR70bn (flat QoQ) largely on back of controlled staff expenses (lower requirement for pension provisions) and other opex. (down 1% QoQ). However, lower staff expenses were aided by the fact that SBI did not provide for wage revisions (divergent from trend followed by peer PSU banks), but will start making it from Q4FY13 assuming 15% rise in wages. It will be INR1.8-2.0bn per month; hence, will have to make INR9-10bn provision for five months in Q4FY13.

Other highlights

- Will open 400 branches in Q4FY13. Has recruited junior staff to suffice expansion till July-August 2013.
- Foreign offices' non-interest income more than doubled to INR5.3bn. Operating profit grew 49% to INR9.8bn in Q3FY13 (44% growth adjusting for INR depreciation).
- Slippage from international book came in at INR2.22bn (consisting of 8-10 accounts).
- Profit on sale of investments of INR4.18bn: Equity INR2.14bn (MF INR1.67bn), bonds INR1.2bn and foreign income INR840mn.
- Writeback in domestic bonds at INR2bn; standard asset provisioning of INR630mn.
- Investment break up: INR3.43tn—INR2.31tn is in HTM and INR1.12tn in AFS (INR40bn is non SLR). AFS modified duration is 1.81 years.
- Slippage during Q3FY13 came at elevated levels of INR81.7bn (3.4% vis-à-vis 3% in Q2FY13)—MCG (pharma + steel + few chunky accounts (INR20bn) already upgraded during Q4) led. This, coupled with modest recoveries of INR9bn (down 7% YoY), led to 9% QoQ jump in GNPA (5.3% of advances). PCR (including technical write-offs) dropped 130bps to 61.5%.
- Management expects government infusion of INR30bn to take Tier 1 : 10%.
- We are building in capital infusion of INR30bn by FY13 with price of INR2,250 amounting to 13.3mn shares.

Table 1: Loan growth rebounds; deposits come in healthy

	Q312	Q412	Q113	Q213	Q313
Advances (INR bn)	8,694	8,936	9,458	9,560	10,091
Growth Q-o-Q (%)	*7.3*	*2.8*	*5.8*	*1.1*	*5.6*
Growth Y-o-Y	*17.5*	*18.1*	*20.0*	*17.9*	*16.1*
Deposits (INR bn)	10,010	10,436	11,029	11,336	11,567
Growth Q-o-Q (%)	*2.9*	*4.3*	*5.7*	*2.8*	*2.0*
Growth Y-o-Y	*13.9*	*11.7*	*16.1*	*16.5*	*15.6*
CD ratio	*86.9*	*85.6*	*85.8*	*84.3*	*87.2*

Table 2: Advances to incrementally see increased growth from retail/large corporate

	Q312	Q412	Q113	Q213	Q313
Large and mid	33.5	32.8	32.7	33.1	32.9
SME	17.6	15.6	14.2	15.1	15.7
Housing	11.4	11.5	11.1	11.2	11.2
Agri	11.7	13.1	12.7	12.0	11.4
International	15.4	15.2	17.4	16.5	17.1
Education	1.4	1.4	1.3	1.4	1.3
Auto loans	2.0	2.8	2.8	2.2	2.3
Others (retail)	5.3	4.7	4.4	5.2	5.0
Others	1.6	3.0	3.3	3.2	3.1
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Company

Table 3: Strong sequential growth seen in large corporate and SME loans

(INR mn)	Q313	Q312	Growth (%)	Q213	Growth (%)
Large and mid	3,317	2,915	*13.8*	3,162	*4.9*
SME	1,586	1,530	*3.7*	1,447	*9.6*
Housing	1,132	990	*14.3*	1,074	*5.4*
Agri	1,154	1,019	*13.3*	1,151	*0.3*
International	1,721	1,341	*28.4*	1,581	*8.9*
Education	136	124	*9.7*	134	*1.3*
Auto loans	228	174	*31.3*	211	*8.3*
Total	**10,091**	**8,694**	***16.1***	**9,560**	***5.6***

Table 4: GNPA at 5.49% as the pace of slippages increase

(INR bn)	Q312	Q412	Q113	Q213	Q313
Gross NPA (INR bn)	401	397	472	492	535
Growth Q-o-Q (%)	*18.1*	*(1.1)*	*18.9*	*4.3*	*8.6*
Gross NPA (%)	4.6	4.4	5.0	5.2	5.3
Net NPA (INR bn)	188	158	203	226	254
Growth Q-o-Q (%)	*16.6*	*(15.9)*	*28.5*	*11.3*	*12.2*
Net NPA (%)	2.2	1.8	2.2	2.4	2.6
Provision coverage (Excl. AUCA) (%)	53.1	60.1	56.9	54.0	52.5
Provision coverage (Incl. AUCA) (%)	62.5	68.0	64.3	62.8	61.5

Table 5: Slippages higher at 3.4%; adjusted for restructuring it would have been 2.6%

Closing gross NPA	Q312	Q412	Q113	Q213	Q313
Opening gross NPA	339	401	397	472	493
Slippage	82	46	108	72	82
Incremental slippages	*4.0*	*2.1*	*4.9*	*3.0*	*3.4*
Upgradation and recovery	20	47	33	31	28
Write off	0.4	2.8	0.8	19.7	11.2
Closing gross NPA	401	397	472	493	535

Table 6: NIMs off by further 3bps to 3.31%

Reported	Q312	Q412	Q113	Q213	Q313
Cost of deposits	5.9	6.0	6.2	6.3	6.3
Yield on advances	10.9	11.1	10.9	10.9	10.8
Net interest Margin	4.1	3.9	3.6	3.3	3.3
CASA	47.5	46.6	46.1	45.0	45.5
CD ratio	76.7	77.7	78.7	79.7	80.7

Table 7: Other income let down by muted CEB

	Q313	Q312	Growth (%)	Q213	Growth (%)
Commission, exchange, brokerage	25,587	26,420	*(3.2)*	24,492	*4.5*
Forex income	4,401	2,860	*53.9*	3,198	*37.6*
Fee based income	29,988	29,280	*2.4*	27,690	*8.3*
Profit on sale of investments	4,178	(10,900)	*(138.3)*	2,302	*81.5*
Dividend	-	530		666	
Others	2,318	2,360	*(1.8)*	2,809	*(17.5)*
Total income	**36,484**	**21,270**	***71.5***	**33,466**	***9.0***

Source: Company

Table 8: Outstanding restructured book stands at INR238bn

(INR mn)	Standard Category	NPA Category	Total
Upto 2010	168,970	36,270	205,240
2010-11	31,460	28,920	60,380
2011-12	68,940	24,580	93,520
Q1FY13	12,440	2,850	15,290
Q2FY13	68,490	4,790	73,280
Q3FY13	(125,090)	2,500	(122,590)
IBG - Cumulative	13,240	9,470	22,710
Total	**238,450**	**109,380**	**347,830**

Table 9: Slippages largely driven in Mid Corp, SME and agri segments

(INR mn)	Corp	IBG	SME	Agri	Retail	Total
Cash recovery+ upgrades	6,060	3,210	8,510	2,920	7,270	27,970
Write offs	5,600	2,070	3,040		510	11,220
Gross reduction	11,660	5,280	11,550	2,920	7,780	39,190
Fresh slippages	43,810	2,220	21,120	8,670	5,930	81,750
Net increase	32,150	(3,060)	9,570	5,750	(1,850)	42,560
Slippage (%)	5.5	0.6	5.8	3.0	1.2	3.4

Table 10: Banking subsidiaries profitability

(INR mn)	9MFY12	9MFY13	Growth
SBBJ	4,040	5,520	36.6
SBH	8,170	8,700	6.5
SBM	2,530	3,400	34.4
SBP	5,200	5,430	4.4
SBT	3,580	4,490	25.4
Overall	23,520	27,540	17.1

Table 11: Non-banking subsidiaries profitability

(INR mn)	9MFY12	9MFY13	Growth (%)
SBI Capital Markets	1,660	2,120	27.7
SBI Funds Management P	530	630	18.9
SBI Life Insurance	2,650	4,220	59.2
SBI DFHI	310	600	93.5
SBI Cards & Payment Services P	340	850	150.0
Total	5,540	8,800	58.8

Source: Company

Table 12: SOTP valuation pegged at INR 2,779

Subsidiaries	Method	(INR mn)	PB/PE (x)	Value (INR mn)	Stake (%)	Value-SBI (INR mn)	Per share (INR)
Banking business (A)	P/ABV (x)	1,163,212	1.5	1,744,818		1,744,818	2,550
Subs							
Asset management	% of AUMs (FY13E)	690,000	5.5	37,950	63.0	23,909	35
Life insurance	Appraisal value (xNBAP)	88,228	1.8	154,399	74.0	114,255	167
SBI capital market	P/E	3,906	12.0	46,872	100.0	46,872	68
Value of subs (B)				**239,221**		**185,036**	**270**
Value of subs (at 15% holding co discount)							230
Value per share (INR) (A+B)							**2,779**

Source: Edelweiss research

Financials snapshot (INR mn)

Year to March	Q3FY13	Q3FY12	*Growth (%)*	Q2FY13	*Growth (%)*	YTD13	FY13E	FY14E
Interest on advances	228,002	208,914	*9.1*	225,381	*1.2*	674,729	885,714	1,013,703
Interest on investments	70,720	64,131	*10.3*	67,147	*5.3*	201,598	253,342	279,055
Interest on other resources	1,097	1,072	*2.4*	1,180	*(7.0)*	3,790	20,922	21,553
Interest income	303,436	276,614	*9.7*	296,068	*2.5*	888,672	1,159,979	1,314,311
Interest expenses	191,892	161,956	*18.5*	186,330	*3.0*	556,200	712,990	809,538
Net interest income	111,545	114,659	*(2.7)*	109,738	*1.6*	332,471	446,989	504,773
Other income	36,485	21,260	*71.6*	33,466	*9.0*	104,939	162,454	176,950
Operating expenses	70,122	63,318	*10.7*	69,668	*0.7*	204,200	296,200	317,749
Staff expense	43,512	41,633	*4.5*	42,802	*1.7*	127,685	191,794	205,139
Other opex	26,610	21,685	*22.7*	26,866	*(1.0)*	76,514	104,407	112,609
Pre prov op profit (PPP)	77,908	72,600	*7.3*	73,536	*5.9*	233,211	301,743	351,975
Provisions	26,679	24,074	*10.8*	18,256	*46.1*	69,498	94,879	118,912
Loan loss provisions	27,662	30,061	*(8.0)*	18,372	*50.6*	73,934	97,379	106,912
Others	(983)	(5,987)	*(83.6)*	(116)	*747.9*	(4,435)	(2,500)	12,000
Profit before tax	51,229	48,526	*5.6*	55,281	*(7.3)*	163,712	218,364	245,063
Provision for tax	17,268	15,895	*8.6*	18,699	*(7.7)*	55,655	73,589	82,586
Profit after tax	33,961	32,631	*4.1*	36,581	*(7.2)*	108,058	144,775	162,477
EPS (INR)	50.6	51.4	*(1.5)*	54.5	*(7.2)*	161	211.5	237.4
Ratios								
NII / GII	36.8	41.5		37.1		37.4	38.5	38.4
Provisions / PPOP	34.2	33.2		24.8		29.8	31.4	33.8
Tax rate	33.7	32.8		33.8		34.0	33.7	33.7
Asset quality								
Gross NPA (INR bn)	535	401	*33.3*	492	*8.6*	535	545	618
Gross NPA (%)	0.1	4.6		0.1		0.1	5.2	5.0
Net NPA (INR bn)	254	188	*34.9*	226	*12.2*	254	251	270
Net NPA (%)	2.6	2.2		2.4		2.6	2.4	2.2

Key takeaways from SBI's Q3FY13 analyst meet

1. **Asset quality related**
   - Out of ***fresh addition to GNPLs of INR 82 bn, INR 15-20 bn have got restructured in January under CDR cell (several large accounts)*** and will get upgraded in this quarter.
   - Out of INR 65 bn of slippages in corporate sector, ***INR 8.7 bn has come from iron & steel and INR 14 bn in trading segment*** (mainly government companies).
   - Slippages in international book of INR 2.2 bn was spread across 7-8 accounts.
   - With ***restructured assets performing satisfactorily for 2 years, INR 125 bn has been taken off from restructured pool to INR 235 bn***. Fresh restructuring was INR 28 bn in Q3FY13.
   - INR 26 bn of loans slipped from restructured pool in this quarter.
   - ***Suzlon is a standard restructured account today*** and it has never fall into NPL.
   - Provisioning coverage for standalone bank maintained at 61.5%.
   - Gross NPLs in associate banks range from 3.1-3.8%.

2. **Margins**
   - Cost of deposits 6.31%; yield on advances down due to interest income reversal and aggressive rates on SME and industrial side. Margins reported at 3.72% for 9MFY12.
   - Proportion of savings deposit up from 37.4% in Q2FY13 to 38.1% and retail TD proportion up from 77.8% to 78.6%.

3. **Advance growth**
   - Sanctions have halved in 9MFY13 compared to 9MFY12. YTD it has witnessed sanctions flowing from fertilize, energy and power.
   - Home loans have grown by 13.5% to INR 1.13 tn.
   - Telecom growth is much higher at 60% plus.
   - Agri build up being better and there would be no need to deploy funds in RIDF
   - Despite CD ratio touching 77%, it is still sitting with excess liquidity of INR 500 bn which will support growth going forward.

4. **Others**
   - Consolidated PAT of INR 46.5 bn up 7.6% YoY.
   - Has not made any provisions for wage revision in Q3FY13 but will start making it from Q4FY13 assuming 15% rise in wages. It will be INR 1.8-2.0 bn per months; hence will have to make INR 9-10 bn provision for 5 months in Q4FY13
   - Core fee income down 3%
   - Foreign offices non-interest income more than doubled to INR 5.3 bn. Operating profit grew 49% to INR 9.8 bn in Q3FY13 (44% growth adjusting for rupee depreciation).
   - Not looking for merger of associate banks in the near term: every merger would cost INR 15 bn of capital; don't want to channelize energies in this direction at this point in time.

5. Outlook

- ***Loan*** growth expected to be 18% in FY13 – surprise mainly coming from corporate side.
- NIMs guided between 3.70-3.75% due to substantial relief on CRR and repo rates. Net interest margin of 3.72% maintained even in January 2013.
- Will open 400 branches in Q4FY13 – has recruited junior staff to suffice expansion till July-August 2013.
- Restructuring pipeline for next 2-3 quarters of INR 37 bn (of which fund based will be INR 25 bn) – excluding Suzlon.

6. Datapoints

- Profit on sale of investments of INR 4.18 bn: Equity INR 2.14 bn (MF INR 1.67 bn), bonds INR 1.2 bn and foreign income INR 840 mn.
- Writeback in domestic bonds at INR 2 bn; standard asset provisioning of INR 630 mn.
- Tier 1 capital at 9.5% (including 9MFY13 profits)
- RWA INR 9.44 tn
- SBI Life insurance: PAT of INR 4.22 bn in 9MFY13; with this kind of internal accruals don't think there will any requirement of capital infusion.
- Investment breakup INR 3.43 tn – INR 2.31 tn is in HTM and INR 1.12 tn in AFS (INR 40 bn is non SLR). AFS modified duration is 1.81 years.

Key highlights of Q2FY13 analyst meet

1. **Asset quality related**
    - **Upgrades due to restructuring is ~INR16bn during the quarter (Hotel Leela and Visa Steel).**
    - **Of the INR470bn exposure to power sector, the exposure to troubles SEBs is only INR30bn that too secured by state guarantees (UP and Tamil Nadu).**
    - **Telecom exposure is only to pre 2007 companies with no exposure to the new players in this segment.**
    - **40% of the crop loans within the agri portfolio is collateralized by gold. Total gold loans stand at INR270bn which makes it the largest gold loan portfolio.**
    - **The bank abstained from write-offs as it reduces attention to NPAs but where full provision done in the corporate segment the write offs are done.**
    - **Aggressive recovery and upgrades efforts have given good results and also quite a few of slippages of Q1FY13 was temporary and technical in nature.**
    - **Suzlon:** Under restructuring, but inherent strengths given large order book and assets that can be sold but debt is the problem area. Most of the lenders have agreed for the account to be restructured. Funding by ST sources (including FCCBs) led to the problem. Prudential provision of INR1.15bn done though account is performing.
    - **Kingfisher:** As such there is no direct relation between the Diageo deal and Kingfisher and the bank hopes that the positives from the deal gets passed on to the bankers as well. INR12bn of exposure is fully provided for by the bank. Further lending is unlikely and want the promoters to put in more equity. INR6bn of provision was taken to provide in full in Q1FY13.
    - **Over the past 2-3 years the bank have not seen difference of opinion on NPA with that of RBI. The bank is conservative in this regard. Last year the difference was only INR4.0bn. Happens in small value SME accounts. Current year audit will be over by Q3FY13 end.**
    - Given the stress in the Mid-corporate segment the bank has become risk averse. Within this also textile, Iron & Steel and construction are the problem areas. The sequential increase is on account of disbursements to guaranteed accounts with ticket size of less than INR10mn.
    - Education loans above INR0.75mn are collateralized.

2. **Retail business related**
    - **HOME LOANS:**
        - INR1.5bn sanctions per day is the rate for home loans and hence INR300-320bn addition to home loans portfolio anticipated. INR60bn is the likely increase in O/S book by Q3FY13 end (INR14bn done in October itself) and expect to close the year with INR1.2-1.3tn of home loans (30% growth rate).
        - To speed up processes in home loans particularly in balance transfer cases bank willing to wait for a month to get documents with adequate checks in place. Also the amount goes directly in the account of the transferor bank. INR300mn daily transfers happening under this.

- Bank is focused on garnering SA balances and ~20k assistants (at INR25k all inclusive salary per month) are recruited with focus on SA accretion from new branches among other retail products.
- In auto the market share of 20% implies that the bank is now the market leader. **Car loan** sanctions take place in 48 hours

3. Others

- INR600-700bn liquidity at the bank which will be channelized to advances as the demand picks up.
- **Dividend will come from subsidiaries** only in the end of the year after taking into stock their capital position.
- **Fund transfer charges were waived off** to prevent flight of CASA deposits from the bank. This however is reflecting in lower fee income.
- **Pension corpus is moved to a separate tax exempt fund** which is earning well for the bank and hence the top up requirements to meet pension obligations have reduced thereby reducing the pension provisions in the employee costs.
- Highest deposit rate today is 8.5% and is the lowest in the industry.
- Working with ATM installing companies to increase the footprints of ATMs.
- Increase in home loans business is driving the Life Insurance business as well given the stress on credit insurance.
- **50k policies being done under the scheme of INR0.4mn insurance for INR100 payment under accident insurance.**
- **International NIM decline** is explained by drop in trade finance margins which is the main business. (rates down from LIBOR+200bps to LIBOR+150-175bps)

Guidance

- Tier 1 likely to close at 10% at the end of FY13E.
- 3.75-3.8% margin guidance for domestic business as the excess liquidity utilization will aid margins. Global margins expected to continue at 3.45-3.5%.
- Further decline in deposit rates is difficult as further drop will pull it down than post office rate leading to flight of deposits.

Datapoints

- **GNPA breakup**
  - MCG: INR170bn @9.47%
  - SME: INR144bn @7.86%
  - Agri: INR93bn @ 9.74%
  - Retail: 50bn @ 2.64%
  - CAG: INR20bn @ 1.1%
- RIDF investments at INR170bn
- Q2FY13 NIM: Domestic-3.68, International-1.42, Blended-3.34

Company Description

SBI is India's largest commercial bank with balance sheet size of INR ~14.6 tn and a market cap of INR1.5tn. It has nearly 14,556 branches on standalone basis and ~19,698 branches including associates. Over the past two years, the bank has increased its focus on retail credit to provide itself the necessary growth momentum and improve spreads. Further, to manage operations better, SBI has integrated its treasury operations and has a common technology platform across all its six subsidiary banks. The bank merged State Bank of Saurashtra and State Bank of Indore with itself. This has increased synergies amongst its banking subsidiaries.

Investment Theme

We expect SBI to be the biggest beneficiary of any improvement in economic outlook, pick up in corporate credit, continued retail credit growth, given its extensive reach and client relationships. We expect the bank to attain over 18% CAGR in loan book over next two years. Retail and international businesses would be the key growth drivers for the bank. Of SBI's six associate banks, State Bank of Travancore, State Bank of Mysore, and State Bank of Bikaner and Jaipur are already listed. Management has expressed its intent to unlock values of its investment in associate banks through a public issue. We are positive about the long term potential of this stock, given its wide network and strong franchise.

Key Risks

- Macro economic risk is the biggest risk for SBI, given its size and exposures.
- Increasing geographic penetration by newer private sector banks can lead to faster than expected decline in market share.

Financial Statements

Key Assumptions

Year to March	FY12	FY13E	FY14E	FY15E
Macro				
GDP(Y-o-Y %)	6.5	5.5	6.5	7.0
Inflation (Avg)	8.8	7.8	6.0	6.0
Repo rate (exit rate)	8.5	7.5	6.8	6.0
USD/INR (Avg)	47.9	54.5	54.0	52.0
Sector				
Credit growth	17.1	17.0	16.0	17.0
Deposit growth	13.4	15.0	14.0	17.0
CRR	4.8	4.3	4.3	4.3
SLR	24.0	23.0	23.0	23.0
G-sec yield	8.5	7.8	7.4	7.5
Company				
Yield on advances	10.0	9.4	9.1	9.0
Yield on investments	8.2	7.8	7.5	7.2
Yield on asset	8.7	8.4	8.2	8.1
Net interest margins	3.5	3.2	3.2	3.2
Cost of funds	5.2	5.3	5.2	5.0
Cost of deposits	5.6	5.7	5.6	5.4
Cost of borrowings	6.2	5.9	5.5	5.3
Spread	3.4	3.1	3.0	3.1
Credit growth	14.1	17.8	17.3	17.4
Deposit growth	11.7	14.3	17.1	17.0
SLR ratio	22.7	23.0	22.5	22.0
Low-cost deposits	44.8	45.0	45.0	45.0
Gross NPA ratio	4.5	5.2	5.0	4.5
Provision coverage	60.1	54.0	56.3	59.1
Incremental slippage	3.2	3.8	3.0	2.5
Capital adequacy	11.6	11.1	10.6	10.1

Income statement (INR mn)

Year to March	FY12	FY13E	FY14E	FY15E
Interest income	1,065,215	1,159,979	1,314,311	1,505,398
Interest expended	632,304	712,990	809,538	909,434
Net interest income	432,911	446,989	504,773	595,964
Non interest income	143,515	162,454	176,950	192,290
- Fee & forex income	135,231	132,930	145,506	159,305
- Misc. income	17,922	18,025	19,444	20,985
- Investment profits	(9,639)	11,500	12,000	12,000
Net revenue	576,425	609,443	681,723	788,254
Operating expense	260,690	296,200	317,749	350,360
- Employee exp	169,740	191,794	205,139	228,940
- Other opex	90,950	104,407	112,609	121,420
Preprovision profit	315,735	313,243	363,975	437,895
Provisions	130,902	94,879	118,912	143,869
Loan loss provisions	114,941	97,379	106,912	131,869
Investment depreciation	6,637	(11,000)	2,000	2,000
Other provisions	9,324	8,500	10,000	10,000
Profit before tax	184,833	218,364	245,063	294,025
Provision for tax	67,760	73,589	82,586	99,087
Reported PAT	117,073	144,775	162,477	194,939
Diluted EPS (INR)	174.5	211.5	237.4	284.8
Dividend per share (INR)	35.0	35.0	35.0	35.0
Dividend payout (%)	22.5	19.1	17.0	14.2

Growth ratios (%)

Year to March	FY12	FY13E	FY14E	FY15E
NII growth	33.1	3.3	12.9	18.1
Fees growth	3.8	(1.7)	9.5	9.5
Opex growth	13.3	13.6	7.3	10.3
PPOP growth	33.2	(7.3)	16.6	21.0
PPP growth	24.6	(0.8)	16.2	20.3
Provisions growth	36.6	(15.3)	9.8	23.3
Net profit	41.7	23.7	12.2	20.0

Operating ratios

Year to March	FY12	FY13E	FY14E	FY15E
Yield on advances	10.0	9.4	9.1	9.0
Yield on investments	8.2	7.8	7.5	7.2
Yield on assets	8.7	8.4	8.2	8.1
Net interest margins	3.5	3.2	3.2	3.2
Cost of funds	5.2	5.3	5.2	5.0
Cost of deposits	5.6	5.7	5.6	5.4
Cost of borrowings	6.2	5.9	5.5	5.3
Spread	3.4	3.1	3.0	3.1
Cost-income	45.2	48.6	46.6	44.4
Tax rate	36.7	33.7	33.7	33.7

Balance sheet				(INR mn)
As on 31st March	FY12	FY13E	FY14E	FY15E
Equity capital	6,710	6,844	6,844	6,844
Reserves & surplus	832,802	979,790	1,114,613	1,281,897
Net worth	839,512	986,633	1,121,456	1,288,741
Sub bonds/pref cap	368,364	383,364	398,364	426,364
Deposits	10,436,474	11,926,959	13,966,647	16,341,410
Borrowings	901,692	1,083,192	1,241,192	1,446,192
Other liabilities	809,151	989,210	1,136,735	1,308,605
Total liabilities	**13,355,192**	**15,369,358**	**17,864,396**	**20,811,334**
Loans	8,675,789	10,237,431	12,028,981	14,134,053
Cash and equivalents	971,632	921,077	1,042,873	1,220,016
Gilts	2,577,060	2,992,396	3,421,825	3,913,334
Others	544,916	589,944	642,445	699,065
Fixed assets	54,666	55,290	55,315	54,740
Other Assets	531,130	573,219	672,955	790,126
Total assets	**13,355,192**	**15,369,358**	**17,864,396**	**20,811,334**
Credit growth	14.1	17.8	17.3	17.4
Deposit growth	11.7	14.3	17.1	17.0
EA growth	8.7	15.4	16.2	16.5
SLR ratio	22.7	23.0	22.5	22.0
C-D ratio	84.4	86.9	87.1	87.4
Low-cost deposits	44.8	45.0	45.0	45.0
Gross NPA ratio	4.5	5.2	5.0	4.5
Net NPA ratio	1.8	2.4	2.2	1.9
Provision coverage	60.1	54.0	56.3	59.1
Incremental slippage	3.2	3.8	3.0	2.5
Capital adequacy	11.6	11.1	10.6	10.1
- Tier 1	9.8	9.8	9.3	8.9

RoE decomposition (%)

Year to March	FY12	FY13E	FY14E	FY15E
Net interest income/assets	3.5	3.2	3.2	3.2
Fees/Assets	1.2	1.1	1.0	1.0
Investment profits/Assets	(0.1)	0.1	0.1	0.1
Net revenues/assets	4.7	4.4	4.3	4.2
Operating expense/assets	(2.1)	(2.2)	(2.0)	(1.9)
Provisions/assets	(1.1)	(0.7)	(0.7)	(0.8)
Taxes/assets	(0.6)	(0.5)	(0.5)	(0.5)
Total costs/assets	(3.7)	(3.4)	(3.3)	(3.2)
ROA	1.0	1.1	1.0	1.1
Equity/assets	6.1	6.6	6.6	6.5
ROAE (%)	15.7	15.9	15.4	16.2

Valuation parameters

Year to March	FY12	FY13E	FY14E	FY15E
Diluted EPS (INR)	174.5	211.5	237.4	284.8
Y-o-Y growth (%)	*34.0*	*21.3*	*12.2*	*20.0*
Book value per share (INR)	1,251.1	1,441.7	1,638.7	1,883.1
Adjusted book value per share	1,086.0	1,185.2	1,362.2	1,608.9
Diluted PE (x)	12.7	10.5	9.3	7.8
Price/BV (x)	1.8	1.5	1.4	1.2
Price/ Adj. BV (x)	2.0	1.9	1.6	1.4
Dividend yield (%)	1.6	1.6	1.6	1.6
Price to income (x)	6.1	5.9	5.5	5.0

Peer comparison valuation

	Market cap	Diluted PE (X)		Price/ Adj. BV (X)		ROAE (%)	
Name	(USD mn)	FY13E	FY14E	FY13E	FY14E	FY13E	FY14E
State Bank of India	27,578	10.5	9.3	1.9	1.6	15.9	15.4
Allahabad Bank	1,346	4.5	3.5	0.8	0.7	15.6	17.5
Axis Bank	12,407	13.0	10.4	2.1	1.8	18.4	18.0
Bank of Baroda	5,781	6.5	5.2	1.1	1.0	17.0	18.3
Federal Bank	1,585	9.9	8.6	1.4	1.2	14.3	14.8
HDFC Bank	29,693	23.9	18.9	4.6	3.9	20.4	21.7
ICICI Bank	24,021	16.2	14.5	2.5	2.2	12.7	12.8
Indian Overseas Bank	1,100	7.0	4.8	0.7	0.6	7.7	10.5
IndusInd Bank	4,274	21.9	17.2	3.1	2.7	17.5	16.6
ING Vysya	1,660	14.4	11.4	2.0	1.7	14.7	16.1
Karnataka Bank	522	7.8	6.7	1.1	1.0	13.2	14.0
Oriental Bank Of Commerce	1,596	5.8	4.4	0.8	0.7	12.8	15.0
Punjab National Bank	5,348	5.8	4.9	1.2	1.0	17.5	17.7
South Indian Bank	623	0.7	0.5	0.2	0.1	24.9	25.2
Union Bank Of India	2,371	7.4	6.1	1.0	0.9	15.1	16.3
Yes Bank	3,330	13.5	10.7	3.1	2.4	24.9	25.2
Median	-	8.8	7.6	1.3	1.1	15.7	16.4
AVERAGE	-	10.5	8.6	1.7	1.5	16.4	17.2

Source: Edelweiss research

Additional Data

Directors Data

Pratip Chaudhuri	Chairman	Hemant G Contractor	Managing Director
Diwakar Gupta	Managing Director & CFO	A Krishna Kumar	Managing Director
Dileep C Choksi	Director	S Venkatachalam	Director
D Sundaram	Director	Parthasarathy Iyengar	Director
Jyoti Bhushan Mohapatra	Director	Deepak Ishwarbhai Amin	Director
D K Mittal	Nominee (Govt)		

Auditors - Kalyaniwalla & Mistry

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Life Insurance Corporation	10.66	HDFC Asset Management	1.99
Vanguard Group	0.88	Reliance Capital Trustee	0.77
UTI Asset Management	0.68	Dimensional Fund Advisor	0.66
SKAGEN AS	0.57	Blackrock Fund Advisors	0.42
Prudential ICICI Asset Management	0.35	SBI Fund Management	0.34

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
No Data Available			

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Allahabad Bank	BUY	SP	M	Axis Bank	BUY	SO	M
Bank of Baroda	BUY	SP	M	Federal Bank	BUY	SO	L
HDFC	HOLD	SP	L	HDFC Bank	HOLD	SP	L
ICICI Bank	BUY	SO	L	Indian Overseas Bank	HOLD	SU	M
IndusInd Bank	BUY	SP	L	Infrastructure Development Finance Co Ltd	BUY	SO	L
ING Vysya	BUY	SO	L	Karnataka Bank	BUY	SO	M
Kotak Mahindra Bank	REDUCE	SU	M	LIC Housing Finance	BUY	SO	M
Mahindra & Mahindra Financial Services	BUY	SO	M	Manappuram General Finance	BUY	SO	M
Multi Commodity Exchange of India	BUY	SO	M	Muthoot Finance	BUY	SO	M
Oriental Bank Of Commerce	BUY	SO	L	Power Finance Corp	BUY	SO	M
Punjab National Bank	HOLD	SU	M	Reliance Capital	BUY	SO	M
Rural Electrification Corporation	BUY	SO	M	Shriram City Union Finance	BUY	SO	M
South Indian Bank	HOLD	SP	M	State Bank of India	BUY	SO	L
Union Bank Of India	BUY	SO	M	Yes Bank	BUY	SO	M

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

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Coverage group(s) of stocks by primary analyst(s): Banking and Financial Services

Allahabad Bank, Axis Bank, Bank of Baroda, Federal Bank, HDFC, HDFC Bank, ICICI Bank, Infrastructure Development Finance Co Ltd, IndusInd Bank, Indian Overseas Bank, Karnataka Bank, Kotak Mahindra Bank, LIC Housing Finance, Multi Commodity Exchange of India, Manappuram General Finance, Mahindra & Mahindra Financial Services, Muthoot Finance, Oriental Bank Of Commerce, Punjab National Bank, Power Finance Corp, Reliance Capital, Rural Electrification Corporation, State Bank of India, Shriram City Union Finance, South Indian Bank, Union Bank Of India, ING Vysya, Yes Bank

Recent Research

Date	Company	Title	Price (INR)	Recos
14-Feb-13	**LIC Housing Finance**	Stress in developer loans; NIM improvement delayed; *Result Update*	252	Buy
06-Feb-13	**Mannapuram**	Auction under-recoveries, funding pressure dent earnings; *Result Update*	42	Buy
04-Feb-13	**Bank of Baroda**	Weak quarter-higher Slippages, lower growth; *Result Update*	804	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution* * - stocks under review	118	46	17	181

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	117	57	7

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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