

South Indian Bank

17 January 2020

Reuters: SIBK.BO; Bloomberg: SIB IN

Margin expands, asset quality guidance retained

South Indian Bank (SIB) reported 3QFY20 results with the key takeaways being: (1) Corporate slippages story largely over; NPA ratio at peak as per guidance (2) NIM expands for the third consecutive quarter, driven by higher growth in retail (3) Retail continues to be the focus, driven by mortgages, gold and auto loans; corporate growth flat. (See *comprehensive analyst meet takeaways* on page 2 for *significant incremental colour*). Per se, on the key P&L items, SIBL posted Nil growth of 16% YoY at Rs6,018mn, PPOP growth of 15% YoY at Rs3,831mn and PAT growth of 8% YoY at Rs905mn. We have revised our estimates for FY20/FY21/FY22 and have retained Buy rating on SIB, revising our target price to Rs14 (from Rs 13 earlier), valuing the stock at 0.4x H1FY22E P/BV.

Corporate slippages story largely over; NPA ratio at peak as per guidance: Gross slippages for the quarter were Rs3.61bn (down 17% QoQ) (Rs103.7bn for 9MFY20). Large accounts that slipped during the quarter included an HFC (Rs1.14bn) and a fitness-related company (Rs0.75bn), both declared as stressed earlier. The management's guidance of H2FY20 gross slippages being contained below Rs5bn may not materialize, given the 3QFY20 run-rate. For FY21, gross slippage guidance stands at Rs8-10bn. Reductions during the quarter were Rs2.63bn (down 41% QoQ) (cash recoveries: Rs0.45bn, upgrades: Rs0.54bn, sale to ARC: Rs0.17bn and write-offs: Rs1.46bn). Write-offs were 56% of the total reductions. The stressed irrigation account continues to be standard (Rs0.5bn). For FY21, the management reiterated its guidance of Rs5bn worth of recoveries. As per the bank, most of the large corporate stress has been recognized. In the MSME segment, 15-20% of the restructured book is expected to slip into NPA. However, the bank has primary security as well as sizeable collateral security in most of these MSME accounts. Problems in the MSME portfolio are not sector-specific but rather a function of the adverse economic environment. The management has guided for a PCR of 60% by end-FY21. As a result, provisioning run-rate upto 4QFY21 is expected to be elevated (~Rs2bn per quarter). As per management, the NPA ratios have peaked out and are unlikely to breach current levels.

NIM expands for the third consecutive quarter, driven by higher growth in retail: NIM expanded 3bps QoQ to 2.72%. The bank has seen higher growth in the higher yielding non-corporate portfolio, which has been partially instrumental in driving NIM expansion. Yield on advances has expanded 4bps QoQ. Since 4QFY19, yield on advances has expanded by 31bps. At the same time, cost of deposits for the quarter stood at 6.14%, down 10bps QoQ; down 16bps since 4QFY19. Liability diversification during the quarter has been impressive. The bank has shed bulk deposits (down 3% YoY) while retail deposits (RTDs + CASA) have grown 13% YoY to Rs707.03bn (83% of total deposits; +282bps YoY). The bank has guided for NIM of 2.7% going forward.

Retail continues to be the focus, driven by mortgages, gold and auto loans; corporate growth flat: Housing book grew 22% YoY/3% QoQ, gold loan book grew 38% YoY/14% QoQ, LAP grew 35% YoY/5% QoQ, business loan portfolio is down 18% YoY/8% QoQ, vehicle loans grew 17% YoY. The bank continues to focus on increasing the share of retail and MSME. Given the credit growth performance in 9MFY20 and taking into account the current macro environment, we have lowered our loan book growth estimates. Low capital adequacy could pose as a growth constraint in the following years.

Valuation and outlook: We have revised our Nil estimates by 1.2%/2.9%/0.8%, PPOP estimates by 2.3%/-1.0%/-5.0% and PAT estimates by 9.9%/3.1%/-4.6% for FY20/FY21/FY22, respectively. We have retained Buy rating on SIB, revising our target price to Rs14 (from Rs 13 earlier), valuing the stock at 0.4x H1FY22E P/BV.

BUY

Sector: Banking

CMP: Rs11

Target Price: Rs14

Upside: 26%

Raghav Garg, CFA

Research Analyst

raghav.garg@nirmalbang.com

+91-22-6273 8192

Arjun Bagga

Research Associate

arjun.bagga@nirmalbang.com

+91-22-6273 8111

Key Data

Current Shares O/S (mn)	1,809.7
Mkt Cap (Rsbn/US\$m)	19.8/278.9
52 Wk H / L (Rs)	19/9
Daily Vol. (3M NSE Avg.)	5,107,860

Price Performance (%)

	1 M	6 M	1 Yr
South Indian Bank	4.8	(17.7)	(30.3)
Nifty Index	1.5	5.7	13.3

Source: Bloomberg

Y/E March (Rsmn)	Q3FY20	Q3FY19	Q2FY20	YoY (%)	QoQ (%)
Interest income	19,673	17,352	19,540	13.4	0.7
Interest expenses	13,655	12,155	13,697	12.3	(0.3)
Net interest income	6,018	5,196	5,843	15.8	3.0
NIM (%)	2.72	2.66	2.69	6 bps	3 bps
Non-interest income	2,204	1,868	2,492	18.0	(11.6)
Total income	8,222	7,064	8,335	16.4	(1.4)
Staff costs	2,396	2,022	2,332	18.5	2.7
Other operating expenses	1,995	1,722	1,889	15.9	5.6
Total operating expenses	4,391	3,744	4,221	17.3	4.0
Cost-to-income (%)	53.4	53.0	50.6	40 bps	276 bps
Pre-provisioning operating profit	3,831	3,320	4,115	15.4	(6.9)
Provisions	2,609	2,031	3,063	28.5	(14.8)
PBT	1,222	1,289	1,051	(5.2)	16.3
Tax	317	450	206	(29.7)	53.5
-Effective tax rate	25.9	34.9	19.6	-904 bps	628 bps
PAT	905	838	845	8.0	7.2
EPS (Rs)	0.50	0.46	0.47	8.0	7.2
Deposits	848,740	776,650	829,470	9.3	2.3
Advances	643,290	592,560	629,934	8.6	2.1

Source: Company, Nirmal Bang Institutional Equities Research

Comprehensive Analyst Meet Takeaways

Asset Quality

- During the quarter, out of four stressed accounts specified in 2QFY20;
 - HFC and fitness-related account slipped into NPA;
 - NBFC account was sold out;
 - Irrigation sector account (~Rs 0.5bn exposure) remains standard.
- Bank expects 15-20% slippages from the MSME restructured portfolio. However, the bank has sizeable collateral and primary security available on these accounts. The stress in such accounts is neither sector specific, nor state/region specific.
- GNPA's have peaked out and are unlikely to exceed the 4.96% mark going forward. The bank has guided for Rs 8-10bn slippages and Rs5-6bn recoveries in FY21.
- The SMA 2 stands at 2.71% (vs 3.51% QoQ). None of the accounts over Rs1bn is in SMA2. Only 1 account over Rs0.5bn is in SMA2.
- The breakup of movement in GNPA's during the quarter is as follows:
 - Slippages: Rs3.61bn
 - Cash recovery: Rs0.45bn
 - Upgrades: Rs0.54bn
 - Sales to ARC: Rs 0.17bn
 - Write-offs: Rs1.46bn
- During the quarter, 3 accounts were identified as fraud. 1 account is a road asset of a major group where the exposure was taken in 2012-13. The other 2 accounts were from the Textile and FMCG sectors.
- As per the bank, it has taken recovery actions in larger value cases, including selling the land and property.
- The company has guided for FY21 provisions of Rs8bn.
- The bank doesn't expect any surprises in retail/MSME asset quality. However, agri slippages may be slightly elevated in March due to seasonality.
- The NBFC sale to ARC entailed a low haircut and was done through a 15/85 structure.
- Total portfolio LGD is 24%; retail portfolio LGD is 14%.
- The bank targets to augment PCR ratio to 60% by FY21.
- The RBI audit is complete and there is no divergence.

Business and Loan Growth

- Growth for other states (ex-Kerala) was optically lower because of the decline in corporate book, which is concentrated in Mumbai, Delhi and Hyderabad. Excluding south, retail and MSME growth was 15%.
- The bank has not taken any road project/BOT/EPC in the last 5 years.
- The bank is comfortable with 30% share of corporate loans.
- Of the Rs73bn large corporate exposure, NBFCs are a large part (~6.89% of total loan book). As per the bank, most NBFC accounts are AA/AAA rated. NBFC exposure would be maintained at current levels.
- The bank has no exposure to telecom/EPC/entertainment/aviation sectors.
- The bank aspires to grow at 18-20% in FY21, however, slower growth in the broader economy may lead to lower growth for the bank.
- The bank aspires to grow retail and agri portfolio at 20%.

Margin, Liabilities and Liquidity

- NIM guidance is for 2.7%.
- As per the bank, there has been no impact on its liabilities due to the developments in cooperative banks and other private sector banks. The bank does not offer higher deposit rates to attract customers.

Fee and Other Income

- Given the insurance tie-ups, the bank expects better traction in terms of distribution fee and overall 3rd party income.
- During the quarter, PSLC income was Rs160mn, recovery on written off accounts was Rs30mn and interest on IT refund was Rs 150mn.
- The bank's life insurance tie-ups are Kotak Life, SBI Life and LIC; general insurance tie-ups are Bajaj Allianz, New India and Bharti AXA.

Operating expenses

- As per the bank, there has been stability in branch count owing to branch rationalization and its policy of opening extension branches and converting to full fledged branches only where there is a real benefit.

Capital adequacy

- The bank has received Board approval for issuing AT1 bonds upto Rs5bn. Pricing for the bonds is yet to be decided.
- As per the bank, it is comfortable with current leverage levels, but would like to be better capitalized.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Net interest income	19,655	20,197	23,297	25,553	27,729
Pre-provisioning operating profit	14,808	12,390	14,794	15,039	15,934
PAT	3,349	2,475	3,440	4,477	5,050
EPS (Rs)	1.9	1.4	1.9	2.5	2.8
BV (Rs)	29.0	29.5	31.2	33.4	36.0
P/E (x)	6.0	8.1	5.8	4.5	4.0
P/BV (x)	0.4	0.4	0.4	0.3	0.3
GNPAs (%)	3.6	4.9	5.0	4.8	4.7
NNPAs (%)	2.6	3.5	3.2	2.7	2.3
RoA (%)	0.4	0.3	0.4	0.4	0.4
RoE (%)	6.6	4.7	6.3	7.7	8.0

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Actual performance versus our estimates

(Rsmn)	Q3FY20	Q3FY19	Q2FY20	YoY (%)	QoQ (%)	Q3FY20E	Devi. (%)
Net interest income	6,018	5,196	5,843	15.8	3.0	5,932	1.5
Pre-provisioning operating profit	3,831	3,320	4,115	15.4	(6.9)	4,136	(7.4)
PAT	905	838	845	8.0	7.2	890	1.7

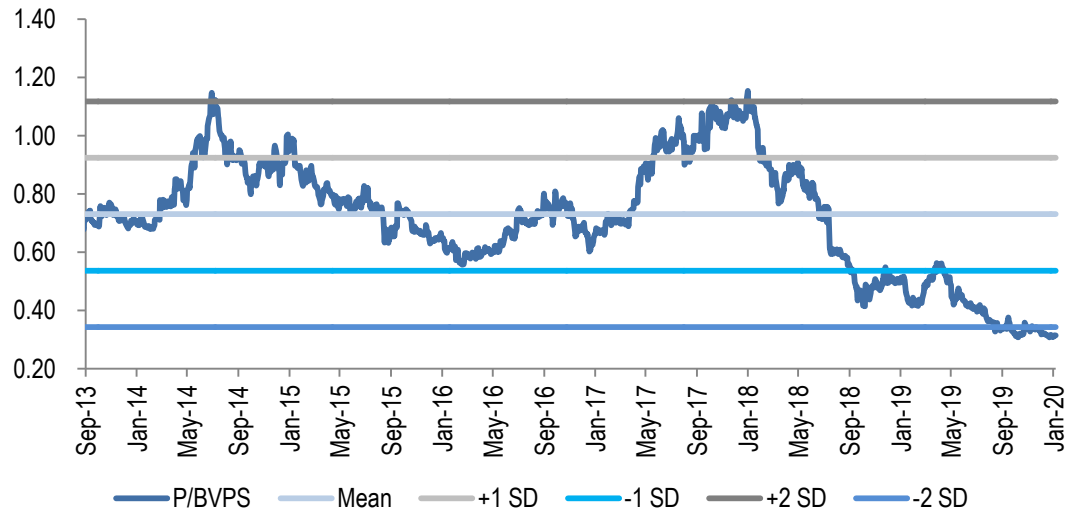
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

	Revised Estimate			Earlier Estimate			% Revision		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Net Interest Income (Rs mn)	23,297	25,553	27,729	23,020	24,843	27,510	1.2	2.9	0.8
NIMs (%)	2.7	2.7	2.7	2.6	2.5	2.5	6 bps	16 bps	15 bps
Operating Profit (Rs mn)	14,794	15,039	15,934	14,462	15,195	16,775	2.3	(1.0)	(5.0)
Profit after tax (Rs mn)	3,440	4,477	5,050	3,131	4,343	5,294	9.9	3.1	(4.6)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Interest Income	61,928	68,765	78,047	84,774	91,825
Interest expense	42,273	48,568	54,751	59,221	64,096
Net interest income	19,655	20,197	23,297	25,553	27,729
Non-interest income	8,372	7,262	8,537	8,239	8,792
Net Revenue	28,028	27,459	31,834	33,791	36,521
Operating Expense	13,220	15,069	17,040	18,752	20,587
-Employee Exp	7,132	8,214	9,364	10,301	11,331
-Other Exp	6,088	6,855	7,675	8,451	9,256
Operating profit	14,808	12,390	14,794	15,039	15,934
Provisions	9,809	8,585	10,113	9,056	9,186
PBT	4,999	3,805	4,681	5,983	6,749
Taxes	1,650	1,330	1,240	1,506	1,699
PAT	3,349	2,475	3,440	4,477	5,050

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Share capital	1,809	1,810	1,810	1,810	1,810
Reserves & Surplus	50,623	51,561	54,609	58,695	63,353
Shareholder's Funds	52,432	53,371	56,419	60,504	65,162
Deposits	720,296	804,201	884,621	964,237	1,051,019
Borrowings	40,434	49,032	53,445	45,428	52,242
Other liabilities	13,697	16,188	24,356	36,532	50,610
Total liabilities	826,859	922,792	1,018,842	1,106,702	1,219,033
Cash/Equivalent	42,210	48,228	53,917	58,769	62,626
Advances	545,629	626,937	673,958	734,614	808,075
Investments	183,631	190,814	223,500	233,137	252,972
Fixed Assets	6,808	7,087	7,795	8,575	9,432
Other assets	48,581	49,727	59,672	71,607	85,928
Total assets	826,859	922,792	1,018,842	1,106,702	1,219,033

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Key ratios

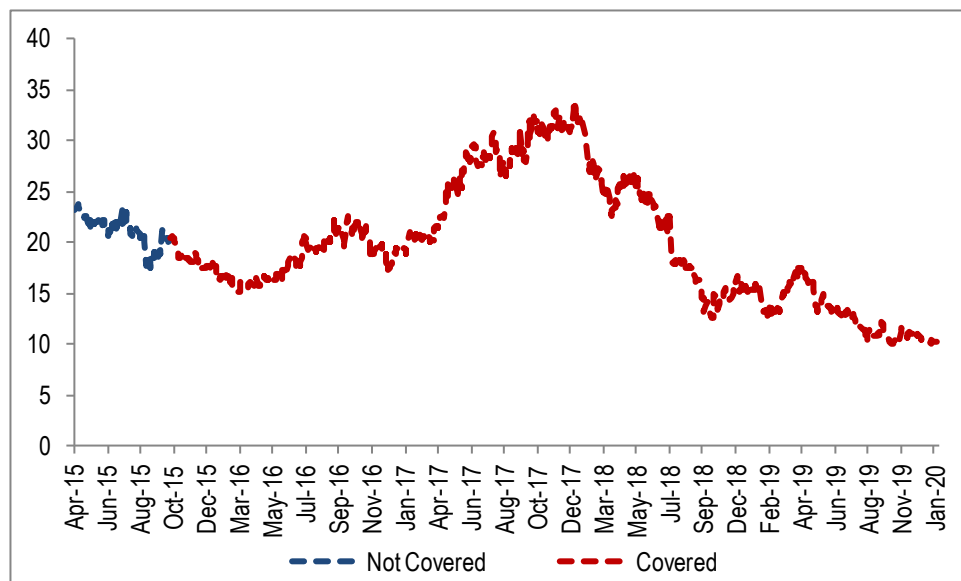
Y/E March	FY18	FY19	FY20E	FY21E	FY22E
Growth (%)					
NII growth	17.3	2.8	15.3	9.7	8.5
Pre-provision profit growth	21.9	-16.3	19.4	1.7	6.0
PAT growth	-14.7	-26.1	39.0	30.1	12.8
Business (%)					
Deposit growth	8.9	11.6	10.0	9.0	9.0
Advance growth	17.6	14.9	7.5	9.0	10.0
CD	75.8	78.0	76.2	76.2	76.9
CASA	23.8	24.2	24.6	25.2	25.8
Operating efficiency (%)					
Cost-to-income	47.2	54.9	53.5	55.5	56.4
Cost-to-assets	1.7	1.7	1.8	1.8	1.8
Spreads (%)					
Yield on advances	9.4	9.2	9.5	9.5	9.5
Yield on investments	6.7	6.9	6.8	6.9	6.9
Cost of deposits	5.8	6.0	6.2	6.2	6.1
Cost of funds	5.9	6.0	6.1	6.1	6.1
NIMs	2.8	2.6	2.7	2.7	2.7
Capital adequacy (%)					
Tier I	10.4	10.0	9.8	9.6	9.4
Tier II	2.3	2.6	2.4	2.4	2.4
Total CAR	12.7	12.6	12.2	12.0	11.8
Asset Quality (%)					
Gross NPA	3.6	4.9	5.0	4.8	4.7
Net NPA	2.6	3.5	3.2	2.7	2.3
Provision coverage	27.3	29.9	37.2	45.8	52.8
Slippage	3.6	3.2	1.8	1.5	1.5
Credit-cost	1.4	1.2	1.2	1.1	1.0
Return (%)					
ROE	6.6	4.7	6.3	7.7	8.0
ROA	0.4	0.3	0.4	0.4	0.4
RORWA	0.7	0.5	0.6	0.7	0.8
Per share					
EPS	1.9	1.4	1.9	2.5	2.8
BV	29.0	29.5	31.2	33.4	36.0
ABV	21.0	17.4	19.2	22.6	25.8
Valuation					
P/E	6.0	8.1	5.8	4.5	4.0
P/BV	0.4	0.4	0.4	0.3	0.3
P/ABV	0.5	0.6	0.6	0.5	0.4

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 March 2018	Buy	23	28
15 May 2018	Buy	26	30
23 July 2018	Buy	18	26
9 October 2018	Buy	13	18
16 October 2018	Buy	15	21
21 January 2019	Buy	14	20
8 April 2019	Buy	18	21
10 May 2019	Buy	15	20
8 July 2019	Buy	13	15
26 July 2019	Buy	13	15
7 October 2019	Buy	11	13
18 October 2019	Buy	10	13
8 January 2020	Buy	10	13
17 January 2020	Buy	11	14

Rating track graph



DISCLOSURES

This Report is published by Nirmal Bang Equities Private Limited (hereinafter referred to as "NBEPL") for private circulation. NBEPL is a registered Research Analyst under SEBI (Research Analyst) Regulations, 2014 having Registration no. INH000001436. NBEPL is also a registered Stock Broker with National Stock Exchange of India Limited and BSE Limited in cash and derivatives segments.

NBEPL has other business divisions with independent research teams separated by Chinese walls, and therefore may, at times, have different or contrary views on stocks and markets.

NBEPL or its associates have not been debarred / suspended by SEBI or any other regulatory authority for accessing / dealing in securities Market. NBEPL, its associates or analyst or his relatives do not hold any financial interest in the subject company. NBEPL or its associates or Analyst do not have any conflict or material conflict of interest at the time of publication of the research report with the subject company. NBEPL or its associates or Analyst or his relatives do not hold beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of this research report.

NBEPL or its associates / analyst has not received any compensation / managed or co-managed public offering of securities of the company covered by Analyst during the past twelve months. NBEPL or its associates have not received any compensation or other benefits from the company covered by Analyst or third party in connection with the research report. Analyst has not served as an officer, director or employee of Subject Company and NBEPL / analyst has not been engaged in market making activity of the subject company.

Analyst Certification: We, Raghav Garg, research analyst and Arjun Bagga, research associate, and the authors of this report, hereby certify that the views expressed in this research report accurately reflects our personal views about the subject securities, issuers, products, sectors or industries. It is also certified that no part of the compensation of the analysts was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research. The analysts are principally responsible for the preparation of this research report and have taken reasonable care to achieve and maintain independence and objectivity in making any recommendations.

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

This report is for the personal information of the authorized recipient and does not constitute to be any investment, legal or taxation advice to you. NBEPL is not soliciting any action based upon it. Nothing in this research shall be construed as a solicitation to buy or sell any security or product, or to engage in or refrain from engaging in any such transaction. In preparing this research, we did not take into account the investment objectives, financial situation and particular needs of the reader.

This research has been prepared for the general use of the clients of NBEPL and must not be copied, either in whole or in part, or distributed or redistributed to any other person in any form. If you are not the intended recipient you must not use or disclose the information in this research in any way. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. NBEPL will not treat recipients as customers by virtue of their receiving this report. This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject NBEPL & its group companies to registration or licensing requirements within such jurisdictions.

The report is based on the information obtained from sources believed to be reliable, but we do not make any representation or warranty that it is accurate, complete or up-to-date and it should not be relied upon as such. We accept no obligation to correct or update the information or opinions in it. NBEPL or any of its affiliates or employees shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. NBEPL or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This information is subject to change without any prior notice. NBEPL reserves its absolute discretion and right to make or refrain from making modifications and alterations to this statement from time to time. Nevertheless, NBEPL is committed to providing independent and transparent recommendations to its clients, and would be happy to provide information in response to specific client queries.

Before making an investment decision on the basis of this research, the reader needs to consider, with or without the assistance of an adviser, whether the advice is appropriate in light of their particular investment needs, objectives and financial circumstances. There are risks involved in securities trading. The price of securities can and does fluctuate, and an individual security may even become valueless. International investors are reminded of the additional risks inherent in international investments, such as currency fluctuations and international stock market or economic conditions, which may adversely affect the value of the investment. Opinions expressed are subject to change without any notice. Neither the company nor the director or the employees of NBEPL accept any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of this research and/or further communication in relation to this research. Here it may be noted that neither NBEPL, nor its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profit that may arise from or in connection with the use of the information contained in this report.

Copyright of this document vests exclusively with NBEPL.

Our reports are also available on our website www.nirmalbang.com

Access all our reports on Bloomberg, Thomson Reuters and Factset.

Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 6273 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 6273 8230, +91 22 6636 8833
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 6273 8102/8103, +91 22 6636 8830

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address

B-2, 301/302, Marathon Innova,
 Nr. Peninsula Corporate Park,
 Lower Parel (W), Mumbai-400013.

Board No. : 91 22 6273 8000/1; Fax. : 022 6273 8010