

South Indian Bank

All corporate problems recognised , outlook optimistic

May 15, 2018

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Rating	BUY
Price	Rs26
Target Price	Rs40
Implied Upside	53.8%
Sensex	35,544
Nifty	10,802

(Prices as on May 15, 2018)

Trading data

Market Cap. (Rs bn)	47.2
Shares o/s (m)	1,808.8
3M Avg. Daily value (Rs m)	289.7

Major shareholders

Promoters	0.00%
Foreign	31.65%
Domestic Inst.	15.55%
Public & Other	52.80%

Stock Performance

(%)	1M	6M	12M
Absolute	4.0	(13.1)	5.9
Relative	0.0	(21.6)	(11.3)

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2019	3.5	3.6	-0.4
2020	4.6	4.6	-1.1

Price Performance (RIC: SIBK.BO, BB: SIB IN)



Source: Bloomberg

SIB earnings were below estimates with PAT of Rs1.14bn (PLe: Rs1.24bn) on weaker operating performance. Bank's slippages were higher at Rs6.14bn than expected due to implementation of RBIs rules on treatment of restructured assets. These were majorly from corporate and 50% from the restructured book, but asset quality deterioration was contained on sale of NPA to ARC. Management has guided much lower slippages and credit cost going forward, while continue to be positive on delivering strong loan growth & steady NIMs. Lower PCR of ~41% can be of risk to higher provisions but some recoveries & lower slippages can help improve PCR. Retain BUY with TP of Rs40 based on 1.4x Mar-20E ABV.

- **Slower operating performance:** Core PPOP grew by 13% YoY much slower than anticipated on slower NII growth of 12% YoY on interest reversals from slippages and pressure on NIMs which fell by 20bps QoQ to 2.73%. Non-treasury other income was better on back of better fees but that was offset by higher opex cost from both gratuity assumption change (amortized over four quarters) and infrastructure expenses (new central loan financing facility).
- **Strong loan growth in-line with guidance:** Loan growth of 17.5% remained strong and in-line with guidance, mainly driven by retail/agri and focused approach on corporate (below Rs1.0bn exposures). Management continued to be upbeat on loan growth with target of 20% YoY in FY19 (internal target of 25%) with focus continuing on retail/agri/SME and also as bank has completed its centralization of loan process which should start reflecting in better growth and lower opex impact.
- **Asset quality deteriorates:** Bank reported slippages of Rs6.14bn of which Rs4.8bn was from corporate book, which was slightly high. Slippages from the retail/SME were relatively lower, while agri slippages were seasonally high. Bank has utilized forbearance on provisions amortization in four quarters on investment depreciation, NCLT related provisions (40% PCR v/s 50% PCR required) and ageing related provisions are likely to be high with bank guiding for 100bps of loans. Overall asset quality was contained by sale of NPA to ARC on better cash consideration (50% of net value) and held +50% PCR. Going ahead, bank targets a PCR of 60% (excl. technical) by Sep'19 on back of expected recoveries coupled with lower slippages.

Key financials (Y/e March)	2017	2018	2019E	2020E
Net interest income	16,754	19,655	22,123	25,616
Growth (%)	11.0	17.3	12.6	15.8
Operating profit	12,146	14,808	16,293	18,562
PAT	3,925	3,349	6,416	8,261
EPS (Rs)	2.5	1.9	3.5	4.6
Growth (%)	0.9	(25.5)	91.3	28.8
Net DPS (Rs)	—	0.4	0.5	0.7

Profitability & Valuation	2017	2018	2019E	2020E
NIM (%)	2.43	2.50	2.55	2.64
RoAE (%)	9.0	6.6	11.6	13.5
RoAA (%)	0.57	0.43	0.74	0.85
P / BV (x)	1.0	0.9	0.9	0.8
P / ABV (x)	1.2	1.3	1.1	0.9
PE (x)	10.5	14.1	7.4	5.7
Net dividend yield (%)	—	1.5	1.9	2.5

Source: Company Data; PL Research

Exhibit 1: Slower operating performance but lower provisions help earnings

NII growth has been better but was slightly lower than expectations

Other income was strong on back of strong loan processing fees and Fx income

Opex was higher mainly on gratuity changes and centralisation of bank processes & operations

Provisions were lower than expectations but NPA provisions run rate to be similar to FY18

Loan growth remained strong on continued focus from granular retail/MSME

Margins were slightly under pressure on back of sharper decline in loan yields and interest reversals

Slippages were high led by corporate which came from standard restructured and non-restructured asset book

CASA mix remained steady

Bank shall raise Tier II bonds in medium term and also equity capital at right opportunity

(Rs m)	Q4FY18	Q4FY17	YoY gr. (%)	Q3FY18	QoQ gr. (%)
Interest Income	15,890	14,707	8.0	15,770	0.8
Interest Expended	10,968	10,316	6.3	10,676	2.7
Net interest income (NII)	4,922	4,391	12.1	5,094	(3.4)
-Treasury income	130	180	(27.8)	110	18.2
Other income	1,787	1,377	29.7	1,588	12.5
Total income	6,709	5,768	16.3	6,682	0.4
Operating expenses	3,600	2,960	21.6	3,381	6.5
-Staff expenses	1,933	1,662	16.3	1,849	4.6
-Other expenses	1,667	1,298	28.4	1,532	8.8
Operating profit	3,109	2,808	10.7	3,302	(5.8)
Core operating profit	2,979	2,628	13.3	3,192	(6.7)
Total provisions	1,486	1,653	(10.1)	1,543	(3.7)
Profit before tax	1,623	1,155	40.5	1,759	(7.7)
Tax	482	400	20.5	609	(20.9)
Profit after tax	1,141	755	51.0	1,150	(0.8)
Balance sheet (Rs m)					
Deposits	7,20,296	6,61,175	8.9	6,81,090	5.8
Advances	5,45,629	4,63,895	17.6	5,16,380	5.7
Ratios (%)					
Profitability ratios					
Yield on Advances	9.61%	9.97%	(36)	9.88%	9.61%
Cost of Funds	5.40%	5.72%	(32)	5.40%	5.40%
NIM	2.73%	2.74%	(1)	2.88%	2.73%
RoAA	0.56%	0.42%	14	0.58%	0.56%
Asset Quality					
Gross NPL (Rs m)	19,803	11,490	72.3	17,746	19,803
Net NPL (Rs m)	14,158	6,746	109.9	12,108	14,158
Gross NPL ratio (%)	3.59	2.45	114	3.40	3.59
Net NPL ratio (%)	2.59	1.45	114	2.35	2.59
Coverage ratio (Reported) (%)	41.20	55.10	(1,390)	49.35	(815)
Business & Other Ratios					
CASA mix	23.80	23.80	-	24.86	(106)
Cost-income ratio	53.66	51.32	234	50.59	307
Non int. inc / total income	26.63	23.87	276	23.77	287
Credit deposit ratio	75.75	70.16	559	75.82	(7)
CAR	12.70	12.37	33	12.51	19
Tier-I	10.40	10.90	(50)	10.10	30

Source: Company Data, PL Research

Key Q4FY18 Concall Highlights

Balance sheet

- **Loan book** – Strong traction of 18-19% YoY growth remained across segments with Retail/MSME continuing to lead growth. Growth also improved in the corporate book (14% YoY). **Outlook** – Bank continued to maintain its loan growth guidance of 20% in FY19 mainly led by non-corporate segment.
- **Liabilities** – CASA growth was much slower at 9% YoY owing to base effect of demonetisation. **Outlook:** Bank expects CASA growth to improve on retail incl. NRI deposits builds up going ahead and reach 30% by FY20 (23.8% in FY18).

Margins:

- Margins were slightly under pressure at 2.73% for 4Q18 owing to pressure on loan yields and also on interest reversals of Rs180mn. **Outlook** – Bank continues to maintain margin guidance of 2.85% and 3.0% for FY19 and FY20 respectively (2.84% for FY18).

Opex/Branches:

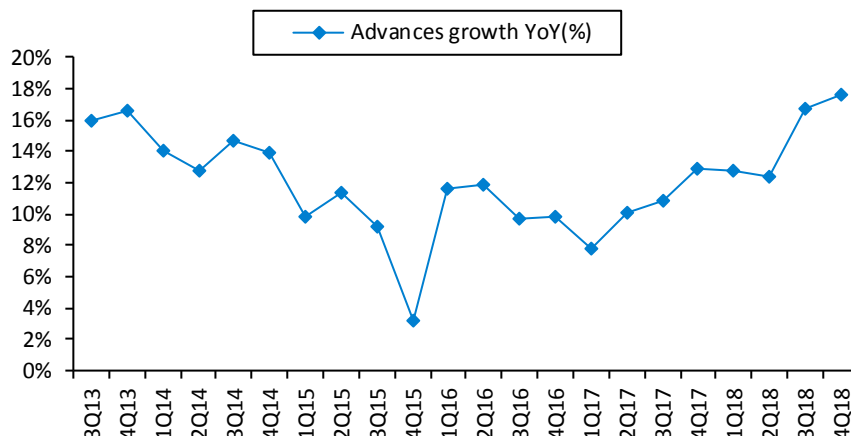
- Other Opex cost was high as bank centralised operations which led to addition of people and increase in Infra, however the same shall even out going ahead. On employee front, bank has provided 1/4th of gratuity provision and requires to provide Rs200mn in FY19 in next 3 quarters. **Outlook:** Bank guides other Opex cost to grow at 10-12% YoY in FY19 as it plans to add 5 branches in AP region and 10 branches in rest of India where already clusters are formed.

Asset Quality:

- **Stress accretion** – Bank witnessed Rs6.14bn of slippages with Rs4.8bn corporate exposure from 4 road sector A/cs amounting Rs3.53bn of which 2 A/cs pertain to standard Restructured and one gold jewellery manufacturer in Kerala. SME book sees some stress mainly in cashew sector and gold a/cs are facing problems on export payments. Bank has only one A/c in 5:25 scheme amounting Rs3bn. **Outlook:** Management expects slippages of Rs6bn in FY19.
- **ARC Sale** – Bank has sold one EPC A/c this quarter having exposure of Rs4.78bn carrying provision of Rs2.94bn at Rs1.65bn of which they received 50 cash. O/s SR book stands at Rs13.56bn which also carries provision of Rs2.6bn.
- **Credit cost** – **Outlook:** Bank guided for credit cost to remain at Rs6bn for FY19 which is at similar level to FY18. Bank has taken the benefit and requires to provides 10% on NCLT A/cs in 1Q19 having exposure of Rs3.3bn with PCR of 40%. Bank expects to strengthen its balance sheet and improve its PCR to 60% excl. technical write-off by Sep-19.

Others:

- Bank expects to raise capital in FY19 as it finds opportunities due to increase in growth. For the time being, it will raise Tier ii bonds. CRAR and Tier I is at 12.7% and 10.4% respectively.

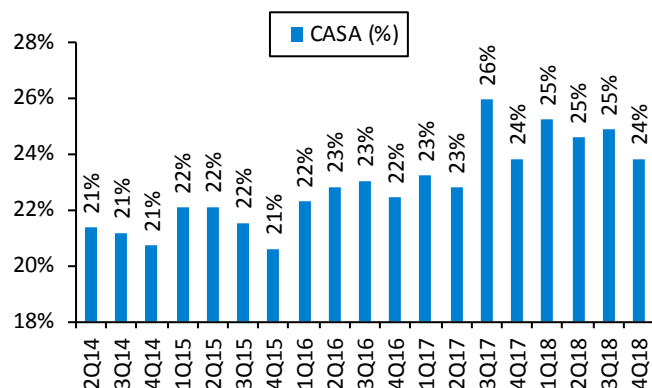
Exhibit 2: Loan book growth was better as focus remains on non-corporate growth


Source: Company Data, PL Research

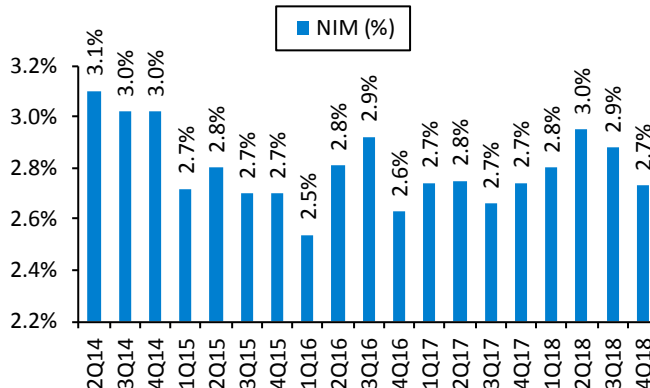
Exhibit 3: Loan growth was better led by Retail/MSME

Break-up of Advances	Q4FY18	Q4FY17	YoY gr. (%)	Q3FY18	QoQ gr. (%)
Agri	79,190	66,330	19.4	75,690	4.6
MSME	1,29,650	1,09,840	18.0	1,32,550	(2.2)
Retail	1,37,870	1,15,660	19.2	1,30,270	5.8
Corporate	2,04,380	1,79,010	14.2	1,85,980	9.9
Total Advances	5,51,090	4,70,840	17.0	5,24,490	5.1
Agri	14.4%	14.1%	0.3	14.4%	(6.1)
MSME	23.5%	23.3%	0.2	25.3%	(174.6)
Retail	25.0%	24.6%	0.5	24.8%	18.0
Corporate	37.1%	38.0%	(0.9)	35.5%	162.7

Source: Company Data, PL Research

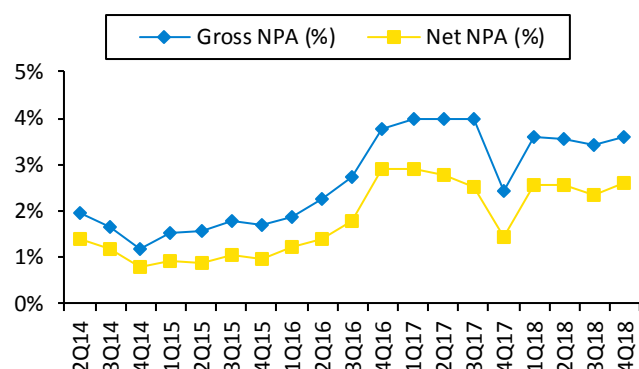
Exhibit 4: CASA growth was slower on base effect


Source: Company Data, PL Research

Exhibit 5: Margins came off sequentially on pressure from loan yields


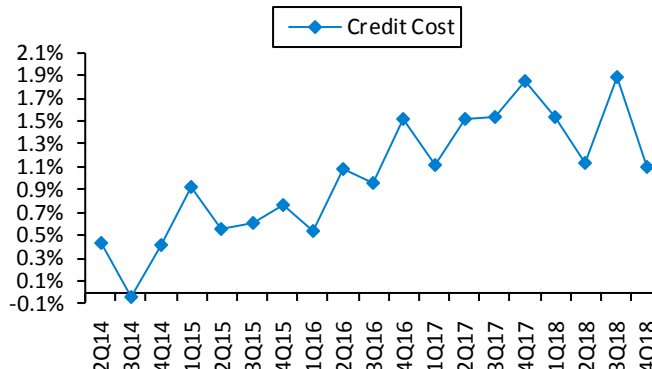
Source: Company Data, PL Research

Exhibit 6: Though higher slippages, asset quality deterioration was contained by sale of NPA to ARC



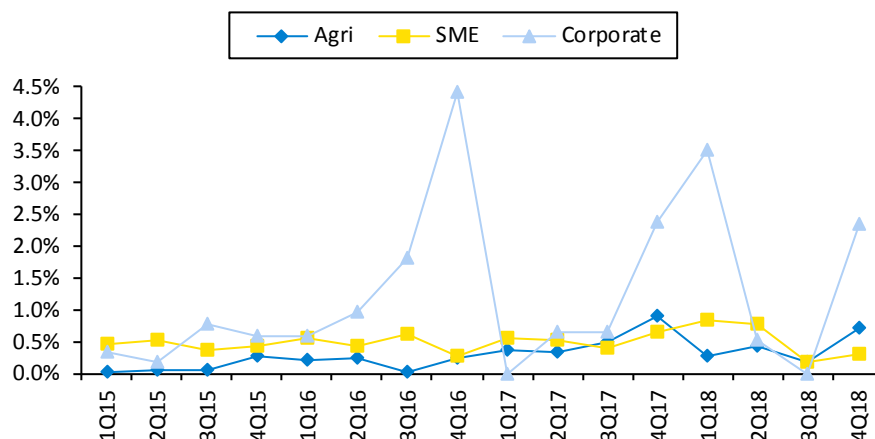
Source: Company Data, PL Research

Exhibit 7: Credit cost came down as bank takes benefit of RBI dispensation on provisions



Source: Company Data, PL Research

Exhibit 8: Incremental slippages were quite high from corporate



Source: Company Data, PL Research

Exhibit 9: Estimates change table- We tweak our estimates slightly on business growth, factoring in pressure on margin and higher opex

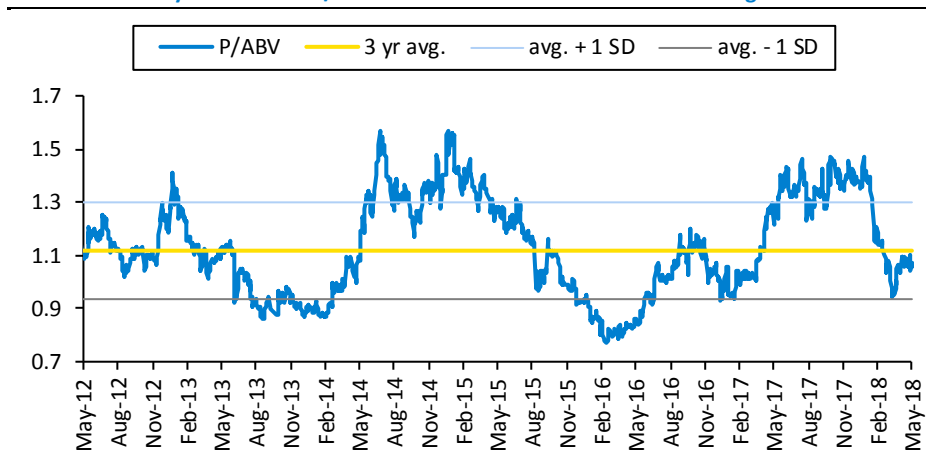
(Rs mn)	Old		Revised		% Change	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
NII	22,853	26,465	22,123	25,616	(3.2)	(3.2)
Operating profit	16,927	19,332	16,293	18,562	(3.7)	(4.0)
Net profit	6,750	8,671	6,417	8,262	(4.9)	(4.7)
EPS (Rs)	3.7	4.8	3.5	4.6	(5.2)	(5.0)
ABVPS (Rs)	24.7	29.4	24.0	29.1	(2.8)	(1.1)
Price target (Rs)	40		40		(0.1)	
Recommendation	BUY		BUY			

Source: Company Data, PL Research

Exhibit 10: We maintain our TP of Rs40 based on 1.4x Mar-20 ABV (rolled over from Sep-19)

PT calculation and upside	
Fair price - P/ABV	40
Target P/ABV	1.4
Target P/E	8.7
Current price, Rs	26
Upside (%)	54%
Dividend yield (%)	3%
Total return (%)	56%

Source: Company Data, PL Research

Exhibit 11: One year Forward P/ABV - SIB trades at below historical averages


Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2017	2018	2019E	2020E
Int. Earned from Adv.	44,474	47,692	56,024	66,741
Int. Earned from Inv.	12,335	12,695	11,615	10,280
Others	1,662	1,541	1,912	2,177
Total Interest Income	58,471	61,928	69,550	79,198
Interest expense	41,716	42,273	47,428	53,581
NII	16,754	19,655	22,123	25,616
Growth (%)	11.0	17.3	12.6	15.8
Treasury Income	2,525	1,810	1,500	1,200
NTNII	4,630	6,563	7,542	8,747
Non Interest Income	7,156	8,373	9,042	9,947
Total Income	65,626	70,301	78,593	89,144
Growth (%)	8.0	7.1	11.8	13.4
Operating Expense	11,764	13,220	14,872	17,001
Operating Profit	12,146	14,808	16,293	18,562
Growth (%)	38.1	21.9	10.0	13.9
NPA Provisions	6,218	6,864	5,961	5,651
Investment Provisions	362	3,162	350	100
Total Provisions	6,144	9,809	6,715	6,229
PBT	6,002	4,999	9,578	12,332
Tax Provisions	2,077	1,650	3,162	4,072
Effective Tax Rate (%)	34.6	33.0	33.0	33.0
PAT	3,925	3,349	6,416	8,261
Growth (%)	17.8	(14.7)	91.6	28.8

Balance Sheet (Rs m)

Y/e March	2017	2018	2019E	2020E
Par Value	1	1	1	1
No. of equity shares	1,803	1,809	1,809	1,809
Equity	1,803	1,809	1,809	1,809
Networth	48,455	52,432	57,760	64,606
Adj. Networth	41,709	38,277	45,785	55,077
Deposits	661,175	720,296	795,927	899,397
Growth (%)	18.7	8.9	10.5	13.0
Low Cost deposits	157,463	171,420	198,982	228,447
% of total deposits	23.8	23.8	25.0	25.4
Total Liabilities	743,091	826,859	911,524	1,026,303
Net Advances	463,895	545,629	646,570	766,186
Growth (%)	12.9	17.6	18.5	18.5
Investments	194,297	183,631	158,622	142,090
Total Assets	743,122	826,859	911,524	1,026,303

Source: Company Data, PL Research.

Quarterly Financials (Rs m)

Y/e March	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Interest Income	14,907	15,362	15,770	15,890
Interest Expense	10,300	10,330	10,676	10,968
Net Interest Income	4,607	5,032	5,094	4,922
Non Interest Income	2,193	2,805	1,588	1,787
CEB	620	730	740	800
Treasury	890	680	110	130
Net Total Income	6,800	7,837	6,682	6,709
Operating Expenses	3,005	3,234	3,381	3,600
Employee Expenses	1,670	1,681	1,849	1,933
Other Expenses	1,336	1,554	1,532	1,667
Operating Profit	3,795	4,603	3,302	3,109
Core Operating Profit	2,905	3,923	3,192	2,979
Provisions	2,243	4,537	1,543	1,486
Loan loss provisions	1,775	1,344	2,363	1,455
Investment Depreciation	261	2,771	45	85
Profit before tax	1,552	66	1,759	1,623
Tax	537	23	609	482
PAT before EO	1,015	43	1,150	1,141
Extraordinary item	—	—	—	—
PAT	1,015	43	1,150	1,141

Key Ratios

Y/e March	2017	2018	2019E	2020E
CMP (Rs)	26	26	26	26
Equity Shrs. Os. (m)	1,803	1,809	1,809	1,809
Market Cap (Rs m)	47,054	47,210	47,210	47,210
M/Cap to AUM (%)	6.3	5.7	5.2	4.6
EPS (Rs)	2.5	1.9	3.5	4.6
Book Value (Rs)	26	28	31	34
Adj. BV (100%) (Rs)	22	20	24	29
P/E (x)	10.5	14.1	7.4	5.7
P/BV (x)	1.0	0.9	0.9	0.8
P/ABV (x)	1.2	1.3	1.1	0.9
DPS (Rs)	—	0.4	0.5	0.7
Dividend Yield (%)	—	1.5	1.9	2.5

Profitability (%)

Y/e March	2017	2018	2019E	2020E
NIM	2.4	2.5	2.5	2.6
RoAA	0.6	0.4	0.7	0.9
RoAE	9.0	6.6	11.6	13.5

Efficiency

Y/e March	2017	2018	2019E	2020E
Cost-Income Ratio (%)	49.2	47.2	47.7	47.8
C-D Ratio (%)	70.2	75.8	81.2	85.2
Business per Emp. (Rs m)	109	106	105	106
Profit per Emp. (Rs lacs)	3.8	2.8	4.7	5.2
Business per Branch (Rs m)	876	789	719	664
Profit per Branch (Rs m)	3	2	3	3

Asset Quality

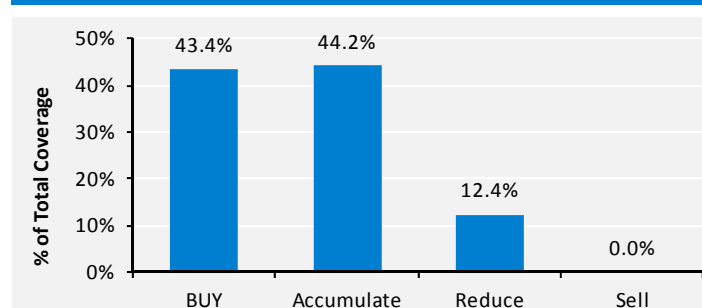
Y/e March	2017	2018	2019E	2020E
Gross NPAs (Rs m)	11,490	19,800	19,629	17,860
Net NPAs (Rs m)	6,746	14,155	11,975	9,530
Gr. NPAs to Gross Adv. (%)	2.5	3.6	3.0	2.3
Net NPAs to Net Adv. (%)	1.5	2.6	1.9	1.2
NPA Coverage (%)	41.3	28.5	39.0	46.6

Source: Company Data, PL Research.

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Reduce	: Underperformance to Sensex over 12-months
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Trading Buy	: Over 10% absolute upside in 1-month
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