CHOLA SECURITIES

South Indian Bank

BUY

Sector: Banking /Mid-Cap | Earnings Update – 1QFY19

23 July 2018

Background: South Indian Bank (SIB), among the mid-sized banks in the private sector space, operates a network of about 855 branches and about 1,386 ATMs. The bank's business is largely skewed towards the Southern state with half of its branches located in Kerala. SIB has established a strong brand recall among the Keralite-NRI Diaspora. With no identifiable promoters SIB is run by a team of professionals. As of 1QFY19 the bank had deposits of ~INR 725bn and a loan book of ~INR 562bn. The bank looks to add a maximum of ~40 branches including extension counter in the coming quarters.

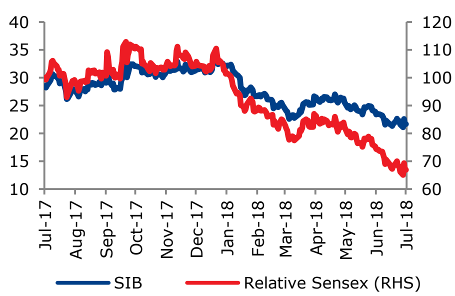
Sensex	36,719
Nifty	11,085
Price	INR 19
Target Price	INR 26
Recommendation	BUY
52 Week High/Low	INR 34.8/18.4
Bloomberg / Reuters	SIB IN/SBK.BO
Equity (shares in mn)	1,808.4
Mkt. Cap in mn	INR 33,636.4/$ 489.2
Avg. Daily Vol. ('000)	10,887
Avg. Daily Vol. (mn)	INR 202.5 /$ 2.9

Shareholding	Jun 17	Mar 18	Jun 18
Promoters (%)	0.00	0.00	0.00
FII (%)	38.04	31.65	32.33
DII (%)	13.09	15.55	14.94
Others (%)	44.11	52.80	52.73
Pledge (% of promoter holding)	0.00	0.00	0.00

Valuation Summary (INR bn)

Y/E March	2018	2019E	2020E
Net Interest Inc	19.7	20.7	24.3
Other Inc	8.4	5.2	5.5
Pre Prov Profit	14.8	11.5	15.0
PAT	3.3	1.1	4.9
EPS	1.9	0.6	2.7
EPS growth (%)	14.2	(66.0)	333.6
PE	10.0	29.5	6.8
P /ABV	0.9	0.8	0.7
Div Yield (%)	2.2	3.8	3.8
ROA (%)	0.6	0.1	0.5
ROE (%)	6.8	2.2	9.2
Tier – 1 (%)	10.5	10.2	10.3
CAR (%)	12.7	12.2	11.8

Performance %	1M	3M	12M
SIB	-7.3	-18.1	-23.9
Sensex	3.0	5.6	13.8



Disappointing quarter with higher slippages and lower other income

- SIB's loan book showed a steady growth of 18.8% YoY in 1QFY19 (1.9% QoQ) in line with our estimates to INR 561.6bn (CSEC estimate of INR 568.18bn). The growth was predominantly led by Retail (29.3% YoY, 10.7% QoQ) and SME & Agriculture (18.4%YoY, 0.5% QoQ) segments. Management has guided that their focus will continue to be on these segments and the loan book would grow at ~20% in FY19E.
- Within the Retail portfolio, growth was largely driven by Manufacturing (37.6% YoY, 14.8% QoQ) and Service & Traders (35.1% YoY, 14.8% QoQ) segments. Gold loans recorded a healthy growth of 5.8% YoY vs. a slower growth of 2.7% FY18.
- Deposits grew by 10.2% YoY (0.6% QoQ) to INR 725bn (vs. CSEC estimate of INR 738bn), with Savings account deposits growing at 10.5%YoY (6.1% QoQ). Overall CASA grew by 24.7% YoY. However, the share of CASA in total deposits fell to 24.7% from 25.2% in 1QFY18, due to higher growth (11%YoY) witnessed in Time Deposits and de-growth in current account deposits (-3.9% YoY). NRI Deposits constituting 27% of total deposits grew by a healthy 12.9% YoY (4.1% QoQ).
- Net Interest Income growth was muted at 7.3% YoY (0.5% QoQ) and it stood at INR 4.9bn (vs. CSEC estimate of INR4.7bn), due to a 56bps YoY (-27bps QoQ) fall in yield on advances. Cost of funds also declined by 4bps YoY to 5.58% (up18bps QoQ). Consequently, NIMs dipped by only 20bps YoY (-13bps QoQ) to 2.6%. Going forward, the management expects the NIM to reach 2.8 by FY19E, owing to the revision in MCLR rates in May (+20bps) and June (+5bps) 2018, which will be reflected in NIMs in another 6 months.
- GNPA in absolute numbers shot up by 50.5% YoY (28.9% QoQ) and NNPA (absolute numbers) by 53.4% YoY (28.1% QoQ), with major slippages coming from 6 corporate accounts totalling to INR 3.08bn - a social infra project (INR 1.05bn), 2 accounts from cashew industry (INR 1.17bn), an EPC account (INR 220mn), a non-EPC contractor (INR 330mn) and a educational institution (INR 310mn), which were classified as NPA under the principle of inherent weakness. This apart, retail slippages (incl. MSME) were recorded at INR 2.98bn. The management had earlier guided for a 1% slippage ratio for FY19, which has now appeared in 1QFY19 itself. Any further slippages in the coming quarters would lead to a greater divergence from the company's guidance.
- Other Income tanked by 33.5% YoY to INR 1.5bn (vs. CSEC's estimate of INR 1.9bn), due to muted growth of 9.3%YoY in fee income, lower treasury profits and no sale of PSLC certificates in 1QFY19. Operating profit also de-grew by 28.9% YoY (-13.3%QoQ) to INR 2.69bn.
- Provisioning costs in 1QFY19 rose by 3.2%, on account higher slipages and carry- over of 4QFY18's provision MTM and gratuity which was entirely written off in 1QFY19. PCR fell to 39.1% from 41.2% in 4QFY18. Cost to Income ratio went up to 57.9% on the back of lower other income and 23% YoY rise in opex. PAT tanked by 77% to INR 230mn (vs. CSEC's estimate of INR 1.01bn).

Valuation:

The Stock currently trades at 0.7x P/ABV of FY20E. SIB continues to shift its focus from corporate loans towards Retail & SME loans which would help them contain the credit costs and maintain the margins at current levels. Fresh slippages in this quarter is a disappointment, however the management is confident about recovering the dues in FY19 itself. We maintain a BUY rating on the stock and revise the target price to INR 26, implying a 1X P/AB FY20E.

Risk: Recoveries lower than expected; tougher ramp up of retail loan book; higher credit costs due to ECL model (IND-AS).

Results Summary 1QFY19

Y/E March (INR bn)	1QFY19	1QFY18	YoY Growth	4QFY18	QoQ Growth
Net Interest Income	4.94	4.61	7.3%	4.92	0.4%
Other Income	1.46	2.19	-33.5%	1.79	-18.3%
Pre Provisioning Profit	2.70	3.79	-28.9%	3.11	-13.3%
PAT	0.23	1.01	-77.3%	1.14	-79.8%
Cost / Income (%)	57.88	44.19		53.66	
Gross NPA (%)	4.54	3.61		3.59	
Net NPA (%)	3.27	2.54		2.60	
Prov Coverage ratio (%)	39.10	44.64		41.20	
CAR (%)	12.23	12.13		12.70	

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