Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Company Update

# State Bank of India
## Standing Tall

| Bank | Sharekhan code: SBIN |
|---|---|
| **Reco/View: Buy** ↔ | CMP: **Rs. 570** |
| | Price Target: **Rs. 680** ↑ |

↑ Upgrade ↔ Maintain ↓ Downgrade

### 3R MATRIX

| | + | = | - |
|---|---|---|---|
| Right Sector (RS) | ✓ | | |
| Right Quality (RQ) | ✓ | | |
| Right Valuation (RV) | ✓ | | |

+ Positive = Neutral – Negative

### What has changed in 3R MATRIX

| | Old | | New |
|---|---|---|---|
| RS | | ↔ | |
| RQ | | ↔ | |
| RV | | ↔ | |

### ESG Disclosure Score NEW

ESG RISK RATING 29.88

Updated Jul 08, 2022

**Medium Risk**

| NEGL | LOW | MED | HIGH | SEVERE |
|---|---|---|---|---|
| 0-10 | 10-20 | 20-30 | 30-40 | 40+ |

*Source: Morningstar*

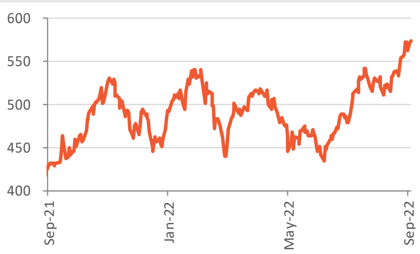
### Company details

| | |
|---|---|
| Market cap: | Rs. 5,08,524 cr |
| 52-week high/low: | Rs. 579 / 425 |
| NSE volume: (No of shares) | 137.3 lakh |
| BSE code: | 500112 |
| NSE code: | SBIN |
| Free float: (No of shares) | 383.8 cr |

### Shareholding (%)

| | |
|---|---|
| Promoters | 57.6 |
| FII | 9.6 |
| DII | 25.1 |
| Others | 7.7 |

### Price chart




### Price performance

| (%) | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | 11.5 | 26.4 | 16.1 | 29.8 |
| Relative to Sensex | 10.4 | 13.2 | 12.3 | 29.1 |

*Sharekhan Research, Bloomberg*


### Summary

- We see continued outperformance in the stock, given that SBI remains the key beneficiary of improved outlook for the overall sector, led by acceleration in credit growth and benign credit cost over the medium term.
- We expect 10-15 bps margin improvement from FY22, led by repricing of loans in the next 3-12 months and strong retail growth in high-yield segments.
- Strong PPoP growth along with benign credit costs (due to sustained improvement in corporate credit cycle) should lead to improvement in return ratios in the near to medium term.
- At the CMP, SBI trades at 1.1x and 1.0x its FY2023E/FY2024E core ABV. We retain our Buy rating on SBI with a revised PT of Rs. 680. It is our top pick among PSU banks with strong balance sheet strength and improved core operating metrics.


**State Bank of India (SBI) has reported steady performance in asset-quality metrics. The bank has seen sharp reduction in overall stressed assets in the past few quarters because of which there has been continued outperformance in the stock. Now as the macro-economic environment is improving, we see upside risk to SBI's earnings from higher margins on account of a decline in excess liquidity and increasing rates, sustained healthy loan growth, contained opex growth, and lower credit costs. This should drive strong improvement in return ratios in the near to medium term. Hence, we expect further rerating in the stock.**

- **NIMs to trend higher:** Out of the total advances, 74% are floating loans – 40% are linked to MCLR, 11% are linked to other EBLR, and 23% are linked to the repo rate. A higher mix of floating loans and increased CASA mix (~44%) will support margins in a rising interest rate environment. The bank reported strong LCR of 138% and lower CD ratio of ~70% in Q1FY2023, thus the bank has been exhibiting its pricing power in terms of pricing of deposits as it has increased retail TD rates only by ~40 bps, while majority of the hike is passed on to bulk deposits (180-200 bps), which have lower share. The bank is also witnessing acceleration in loan growth (+16% YoY, 3% QoQ) in Q1FY2023, led by the retail segment (+19% YoY, 3% QoQ). We expect 10-20 bps margin improvement from FY2022, led by repricing of loans and strong retail growth in the high-yield segment.
- **Steady asset-quality trends and, in turn, lower credit cost:** We do not foresee any material asset-quality risk and expect overall asset quality to improve further. Corporate asset quality remains strong and in the SME book, especially ECLGS has not seen incremental stress formation. We have seen strong rebound in retail growth, especially the unsecured book, but here the focus is still on higher-quality customer segments (majorly government salaried). GNPLs in the retail segment are best-in-class in the industry. In Q1FY2023, core credit cost stood at 62 bps annualised (calculated as a % of average advances) with ~80 bps of net slippages. Restructured book stands at ~1% of advances and SMA 1 and 2 book stands at 0.25% of advances. However, the bank carries additional non-NPA provisions at ~1% of advances. We believe lower stress in the system, additional provisions, and higher coverage ratio (75%) will drive lower credit cost for the bank.

**Revision in estimates:** We have increased our FY2023E/FY2024E earnings estimates, factoring in higher margins and lower credit cost. Moreover, we have introduced FY2025E numbers in this note.

### Our Call

**Valuation –** At the CMP, SBI trades at 1.1x and 1.0x its FY2023E and FY2024E core ABV, respectively. SBI's operating metrics continue to see improvement along with healthy system loan growth and lower credit cost should drive improvement in return ratio in the near to medium term. The balance sheet is strong and capital levels are adequate to achieve growth. The bank is well positioned to gain market share on the business front. SBI's strong deposit franchise and better performance from subsidiaries are likely to favour the business. We maintain our Buy rating on SBI with a revised PT of Rs. 680. SBI remains our top pick among PSUs.

### Key Risks

Economic slowdown due to which slower loan growth and higher-than-anticipated credit cost especially from small business loans portfolio and wheels could affect earnings.

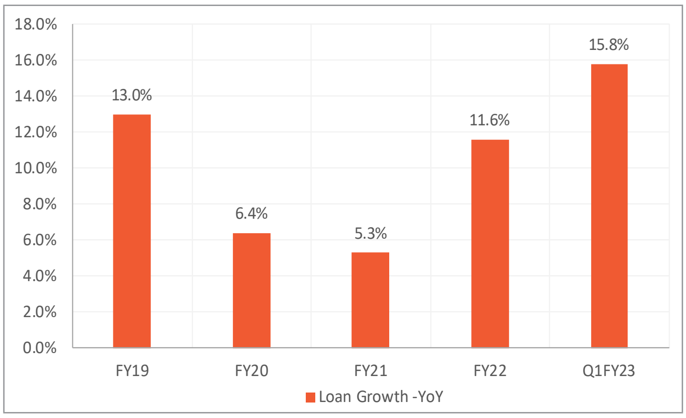
**Valuation (Standalone)** Rs cr

| Particulars | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|
| NII | 1,20,708 | 1,38,682 | 1,52,772 | 1,72,913 |
| PAT | 31,676 | 39,270 | 49,175 | 58,792 |
| EPS (Rs.) | 35.5 | 44.0 | 55.1 | 65.9 |
| P/E (x) | 11.1 | 8.9 | 7.1 | 6.0 |
| P/ABV (x) | 1.3 | 1.1 | 1.0 | 0.8 |
| RoE (%) | 11.9 | 13.1 | 14.3 | 14.8 |
| RoA (%) | 0.7 | 0.8 | 0.9 | 0.9 |

*Source: Company; Sharekhan estimates*

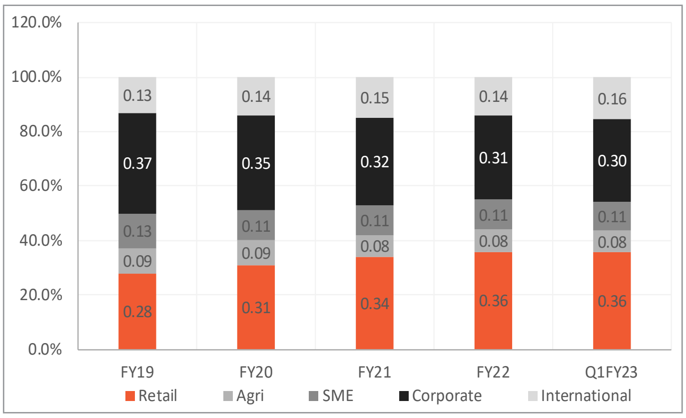
Loan growth is gaining traction (16% y-o-y/3% q-o-q)in Q1FY23 led by retail portfolio and working capital utilisation levels are improving in the corporate book. Retail portfolio growth was healthy at 19% y-o-y/ 3% q-o-q in Q1FY23 versus ~15% y-o-y in FY2022. Within retail loans, share of home loans and Xpress credit (personal loans) both cumulatively accounts for ~81% are growing well. The bank is seeing good success in rolling out pre-approved personal loan offers through the YONO app. Higher growth in the personal loans portfolio for the bank is not worrying because a large proportion (~95%) of the borrowers in this segment are salaried employees – evenly distributed between government employee accounts and corporate salaried accounts. The current penetration of Xpress Credit is at a mere 30% of its corporate salary depositor's base, thus providing significant room for growth. The bank could post higher growth in the SME book in FY2023E vs. 10% in FY2022 as it has increased customer proposition by adding a two-tier relationship manager system with digital features. The improved growth outlook in the corporate book is led by better demand and is likely to continue. Moreover, there has been improvement in granularity in loan book, as its share of retail loans has inched up to ~36% from ~25% in FY2017.

**Loan growth has started to pick up**




*Source: Company, Sharekhan Research*

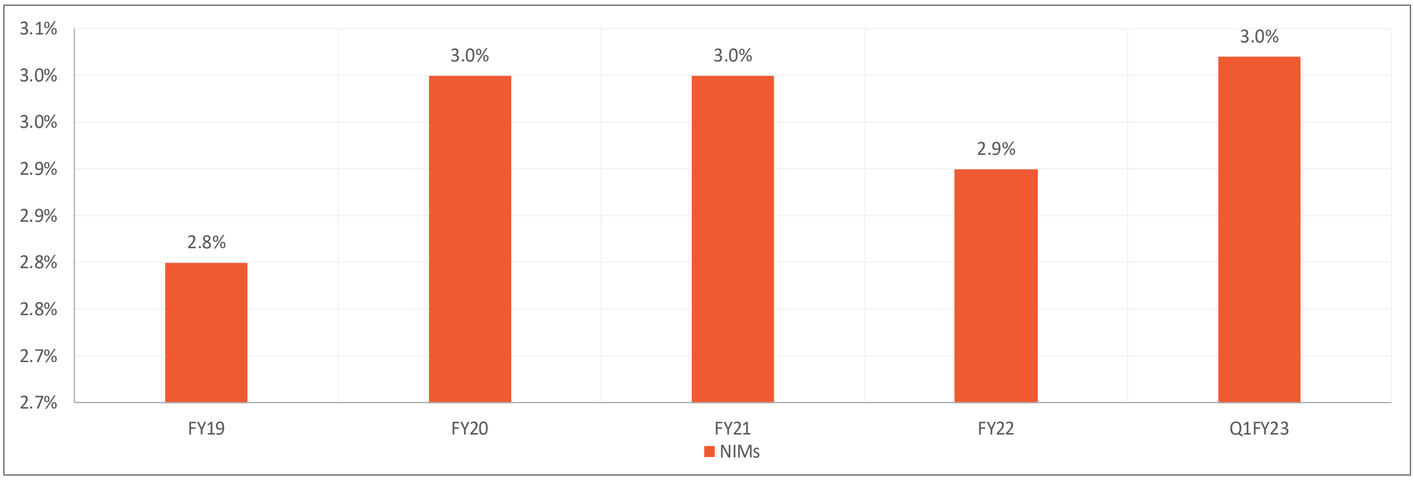
**Loan Mix - Share of Retail loans inching up**




*Source: Company, Sharekhan Research*

Out of the total advances, 74% are floating loans – 40% are linked to MCLR, 11% are linked to other EBLR, and 23% are linked to the repo rate. Increased mix of floating loans and higher CASA mix (~44%) will support margins in a rising interest rate environment. It has strong LCR of 138% and lower CD ratio of ~ 70% in Q1FY2023. Thus, the bank has been exhibiting its pricing power in terms of pricing of deposits as it has increased retail TD rates only by ~40 bps, while majority of the hike is passed on to bulk deposits (180-200 bps), which have lower share. The bank is also witnessing acceleration in loan growth (+16% y-o-y, 3% q-o-q) in Q1FY2023, led by the retail segment (+19% y-o-y, 3% q-o-q). We expect 10-20 bps improvement in margins from FY2022, led by repricing of loans and strong retail growth in the high-yield segment.

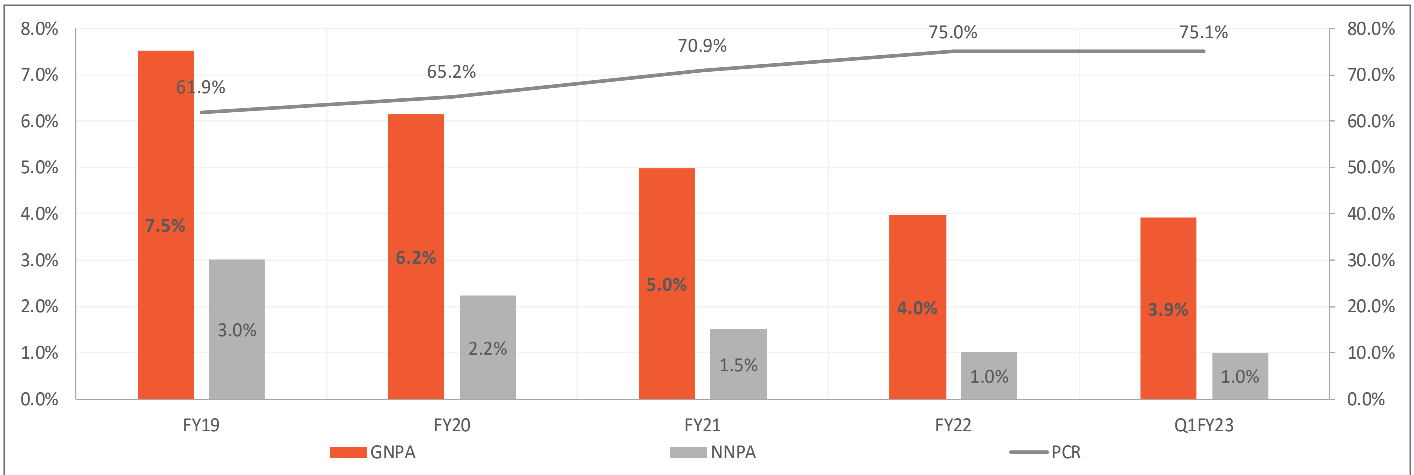
**NIMs are expected to improve by 10-15 bps going forward**




*Source: Company, Sharekhan Research*

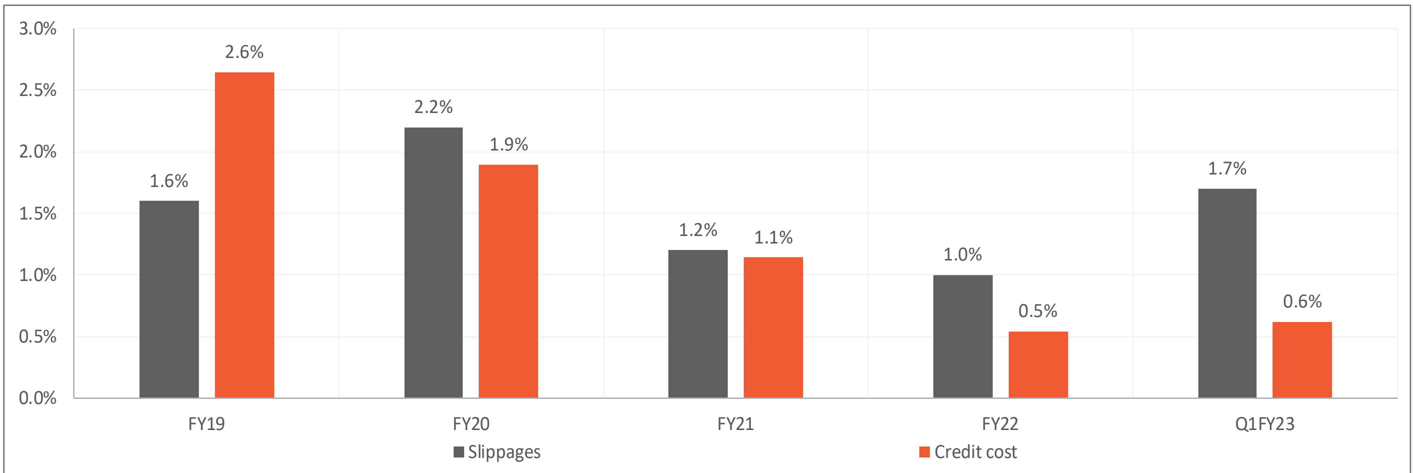
The bank has strengthened its balance Sheet by creating higher provisions on stressed accounts. The bank's continued focus on improving underwriting has manifested in controlled slippages of ~1% in FY2022/1.7% in Q1FY2023 and negligible SMA book – ~25 bps. NNPA ratio, thus, dropped to 1% (a historical low), while PCR increased to 75% (85% on the corporate book). Higher provisions on stressed accounts (100% on SREI and Future Group) places it well, while higher recoveries from AUCA book would limit the overall provisioning requirement. Management has guided for a run-rate of Rs. 8,000 crore-10,000 crore of recoveries from written-off accounts in FY2023E. Restructured loans (on account of COVID-19) stood at ~1% of loans. Additionally, the bank has another ~0.25% of loans of other restructured advances not related to COVID-19 restructuring. However, the bank carries additional non-NPA provisions, which stands at ~1% of advances. The bank is seeing healthy repayment trends in the restructured book. ECLGS loans stand at 1.2% of the total book, and this book has seen less than 2% slippages so far. The bank maintains 100% provisions against the SR book, which is a key positive. GNPLs in the retail segment are best-in-class in the industry. Now, 89% of the corporate book is being rated in investment grade, which is also a key positive. Risk Weighted Assets (RWA) to total assets are less than 50%, which indicates strong book quality. Further, the bank's exposure to the power/telecom sectors remains comfortable, with the bulk of exposure towards PSU entities and better-rated corporates. Granularity and borrower profile has significantly improved. All this should prevent asset-quality deterioration and lower credit cost in FY2023E/FY2024E.

**Steady asset quality along with higher PCR**




*Source: Company, Sharekhan Research*

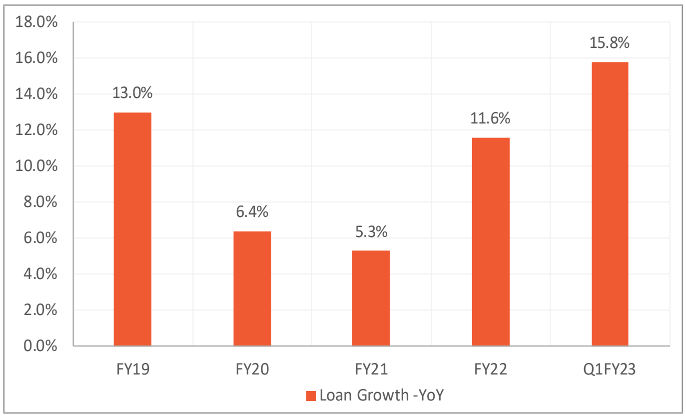
**Slippages and Core Credit cost are expected to be benign**




*Source: Company, Sharekhan Research*

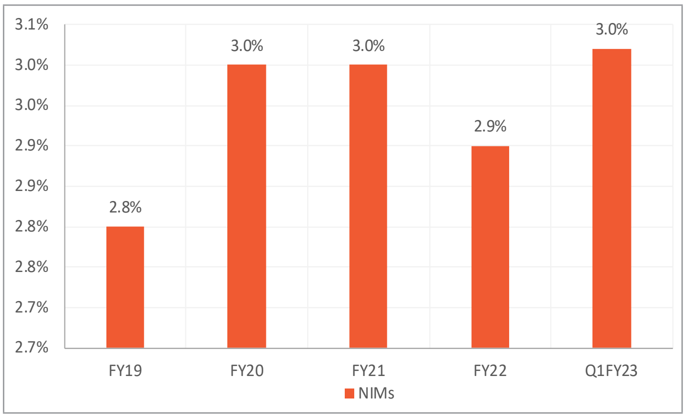
## Financials in charts

### Loan growth has started to pick up



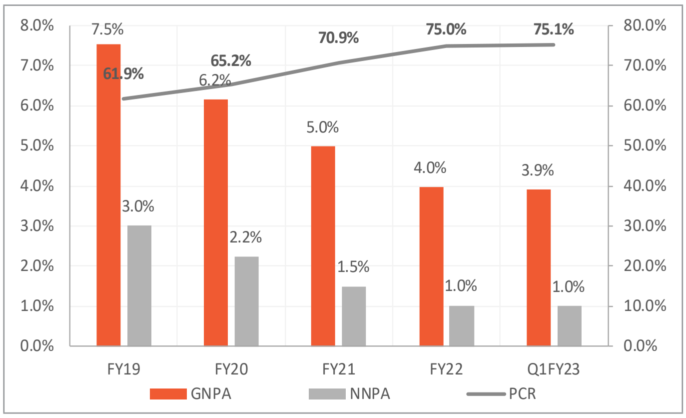

*Source: Company, Sharekhan Research*

### NIMs are expected to improve by 10-15 bps going forward



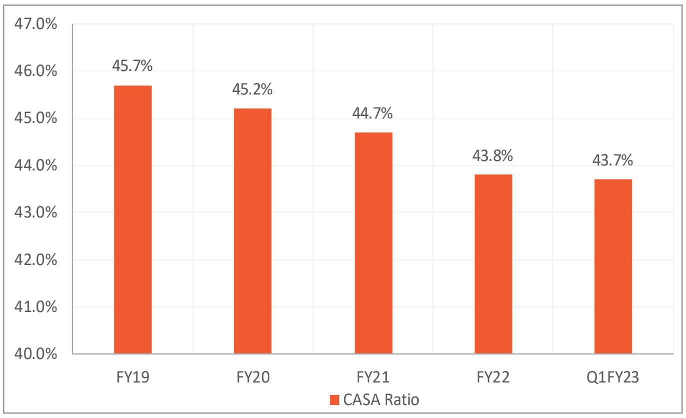

*Source: Company, Sharekhan Research*

### Steady asset quality along with higher PCR



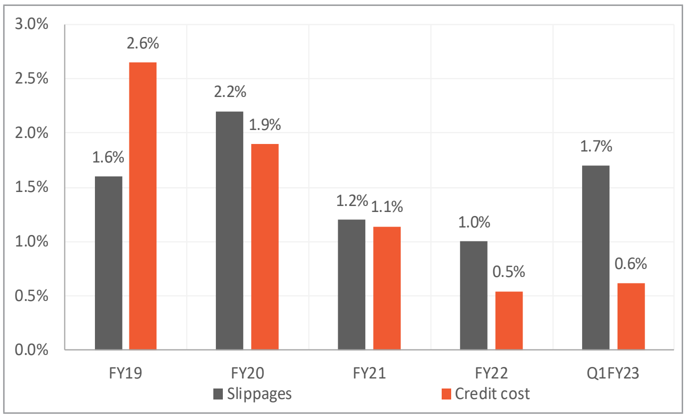

*Source: Company, Sharekhan Research*

### Healthy CASA Ratio



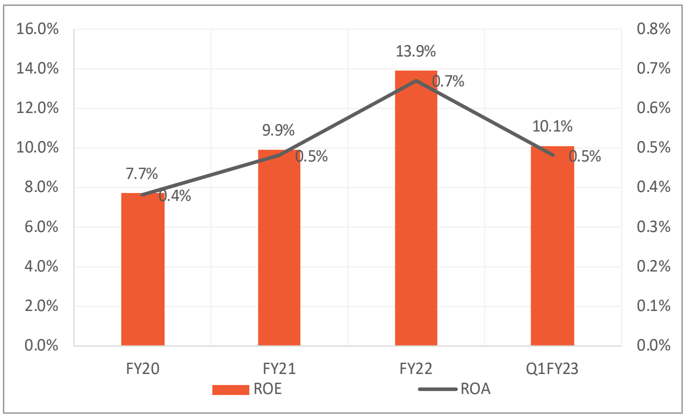

*Source: Company, Sharekhan Research*

### Slippages and Core Credit cost are expected to be benign




*Source: Company, Sharekhan Research*

### Return Ratios expected to improve going forward




*Source: Company, Sharekhan Research*

## Outlook and Valuation

### ■ Sector View – Accelerating credit growth; Top private banks and top PSUs placed better

System-level credit offtake grew by ~15.5% y-o-y in the fortnight ending August 26, 2022, indicating loan growth has been sustaining, given distinct signs of improving economy and revival of investments and loan demand. On the other hand, deposits rose by ~9.5%, which also reflects a healthier economic scenario but are trailing advanced growth. The bottom-up story is intact, and we should see loan growth accelerate, while margins would continue to expand in a higher interest rate cycle. Asset quality is not a big issue from the end of the corporate loan, as only de-leveraging is being observed. From the retail side, there could be some pressure, but nothing is significant. Asset quality is likely to remain stable, except for the MFI segment. Banks are in a sweet spot in terms of fundamentals and reasonable valuations. In the past two years, banks have been cautious on lending to the 'BB and below' category, thus the general risk, which they are carrying on the corporate portfolio, is low. On the retail loans front, due to COVID-19, banks have already seen one downcycle. Most of the exposure has been taken into credit cost. In terms of the MSME book, we need to be watchful. At present, we believe the banking sector is likely to see higher risk-off behaviour, with tactical market share gains for well-placed players. We believe large banks with a strong capital base and asset quality (with high coverage and provision buffers) are well placed to capture growth opportunities.

### ■ Company Outlook – Attractive play on the economy

SBI is an attractive play on the fast-growing Indian economy, with a healthy PCR, higher capital levels, strong liability franchise, improved core operating profitability, and improving asset-quality matrix. SBI has been reporting steady performance in asset-quality metrics and has seen sharp reduction in overall stressed assets because of which there has been continued outperformance in the stock. Now, as the macro-economic environment is improving, we see upside risk to SBI's earnings from higher margins because of a decline in excess liquidity and increasing rates, sustained healthy loan growth, contained opex growth along with credit costs moving lower. This should drive strong improvement in return ratios in the near to medium term, and we expect further rerating in the stock. SBI's pole position in terms of liability franchise, an enviable reach, and business strength make it well placed to ride over medium-term challenges.

### ■ Valuation – We maintain  Buy rating on SBI with a revised PT of Rs. 680

At the CMP, SBI trades at 1.1x and 1.0x its FY2023E and FY2024E core ABV, respectively.  SBI's operating metrics continue to see improvement along with healthy system loan growth and lower credit cost should drive improvement in return ratio in the near to medium term. The balance sheet is strong and capital levels are adequate to meet loan growth. The bank is well positioned to gain market share on the business front. SBI's strong deposit franchise and better performance from subsidiaries are likely to favour the business. We maintain our Buy rating on SBI with a revised PT of Rs. 680. SBI remains our top pick among PSUs.

**Peer valuation**

| Particulars | CMP (Rs / Share) | MCAP (Rs Cr) | P/E (x) | | P/B (x) | | RoE (%) | | RoA (%) | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | FY23E | FY24E | FY23E | FY24E | FY23E | FY24E | FY23E | FY24E |
| State Bank of India | 570 | 5,08,524 | 8.9 | 7.1 | 1.1 | 1.0 | 13.1 | 14.3 | 0.8 | 0.9 |
| HDFC Bank | 1,519 | 8,45,463 | 18.8 | 15.9 | 2.9 | 2.4 | 16.5 | 16.8 | 1.9 | 1,9 |
| ICICI Bank | 915 | 6,37,618 | 18.5 | 15.2 | 2.5 | 2.2 | 14.7 | 15.4 | 1.8 | 1.9 |

*Source: Company, Sharekhan estimates*

## About company

SBI is the largest public-sector bank in terms of assets, deposits, branches, number of customers, and employees having pan-India presence. The bank has been designated by the Reserve Bank of India (RBI) as a domestic systemically important bank (D-SIB), which means that its continued functioning is critical for the economy. The bank is better capitalised than most PSU banks. The bank is well placed to gain market share as well as key clients by virtue of lesser competitive pressures. The bank is well placed to secure growth capital from the government, not only by virtue of being the largest bank, but also with operating parameters that have improved.

## Investment theme

SBI enjoys a dominant position and market share in the Indian banking space, which we expect to be maintained, by virtue of its deep penetration into both rural and urban markets. SBI has a strong presence in both retail liabilities as well as retail asset side along with its corporate relationships (due to its size, history, and market knowledge), which are key differentiators for it. In addition, due to its size, SBI is the market maker for interest rates, which not only puts it in a dominant position but also allows it a margin cushion. SBI has the largest customer base in the country, by virtue of its largest and pan-India network, which enables it to be the banker of preference across India and allows it to explore cross-sell opportunities.

## Key Risks

Economic slowdown due to which slower loan growth and higher-than-anticipated credit cost, especially from corporate and SME book, could affect earnings.

## Additional Data

**Key management personnel**

| | |
|---|---|
| Mr. Dinesh Kumar Khara | Chairman |
| Mr. Challa Sreenivasulu Setty | Managing Director |
| Mr. Ashwini Kumar Tewari | Managing Director |
| Mr. Swaminathan Janakiraman | Managing Director |
| Mr. Alok Kumar Choudhary | Managing Director |

*Source: Company Website*

**Top 10 shareholders**

| Sr. No. | Holder Name | Holding (%) |
|---|---|---|
| 1 | Life Insurance Corp of India | 8.2 |
| 2 | HDFC Asset Management Co. Ltd. | 2.5 |
| 3 | SBI Funds Management Pvt. Ltd. | 2.4 |
| 4 | ICICI Prudential Asset Management | 1.2 |
| 5 | Bank of New York Mellon | 1.2 |
| 6 | Nippon India | 1.1 |
| 7 | Aditya Birla Sun Life Asset Management | 1.1 |
| 8 | Kotak Mahindra Asset Management Co. | 0.8 |
| 9 | Mirae Asset Global Investments Co. | 0.7 |
| 10 | BlackRock Inc. | 0.7 |

*Source: Bloomberg*

## Understanding the Sharekhan 3R Matrix

| | |
|---|---|
| **Right Sector** | |
| Positive | Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies |
| Neutral | Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies |
| Negative | Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability. |
| **Right Quality** | |
| Positive | Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance. |
| Neutral | Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable |
| Negative | Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet |
| **Right Valuation** | |
| Positive | Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment. |
| Neutral | Trading at par to historical valuations and having limited scope of expansion in valuation multiples. |
| Negative | Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple. |

*Source: Sharekhan Research*

Sharekhan

by BNP PARIBAS

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For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

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