

State Bank of India

BSE SENSEX

25,774

S&P CNX

7,891



Stock Info

Bloomberg	SBIN IN
Equity Shares (m)	7,762.8
52-Week Range (INR)	305/148
1, 6, 12 Rel. Per (%)	-8/-28/-33
M.Cap. (INR b)	1,374.4
M.Cap. (USD b)	20.6
Avg Val (INRm)	4,180.8
Free float (%)	39.8

Financials Snapshot (INR b)

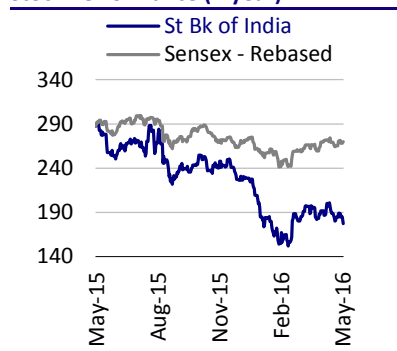
Y/E Mar	2016E	2017E	2018E
NII	552	625	702
OP	397	452	512
NP	101	147	177
EPS (INR)	16.4	24.1	28.7
EPS Gr. %	-28.0	47.3	19.1
Cons. BV (INR)	223.3	242.9	266.2
P/E (x)	10.2	6.9	5.8
P/BV (x)	0.7	0.7	0.6
RoE (%)	7.8	10.2	11.3
RoA (%)	0.5	0.6	0.6

Shareholding pattern (%)

As On	Mar-16	Dec-15	Mar-15
Promoter	60.2	60.2	58.6
DII	18.8	18.4	18.7
FII	10.9	12.1	13.9
Others	10.1	9.3	8.8

FII Includes depository receipts

Stock Performance (1-year)


CMP: INR177
TP: INR215 (+21%)
Buy

Seeks in-principle approval for merger with associate banks

Long-term synergy benefits to outweigh near-term challenges; Biggest challenge – employee integration

Event: State Bank of India (SBIN) has asked for "**in principle sanction**" from GoI to enter into negotiations with associate banks (SBBJ, SBH, SBM, SBP and SBT) and Bharatiya Mahila Bank Limited (BMB) to acquire their businesses including assets and liabilities.

Our view: Long-term synergy benefits to outweigh near-term challenges

- Merger with associate banks has been a long-pending agenda. We value SBIN on consolidated basis. As the integration cost and dilution associated with the merger is not meaningful, it is unlikely to change our target price. BMB operations are small (loans of ~INR10b; net worth of INR10b+); hence, are unlikely to be meaningful from a merger perspective.
- Dilution at the current market cap on account of merger (minority shareholding in SBBJ/SBT/SBM at 25%/21%/10%) is likely to be ~1.2%. At the current market cap, total value for minority shareholders of associate banks stands at INR16.1b. Merger is positive for listed associate banks. Currently, associate banks are trading at ~0.5x P/BV (TTM) as against the parent, SBIN's ~0.8x.
- Branch rationalization, if executed well, would be one of the key synergy benefits from the merger. Cost savings on account of treasury operations, audit, technology, etc would lower cost-to-income ratio in the long term.
- Immediate negative impact would be from pension liability provisions (due to different employee benefit structures) and harmonization of accounting policies for NPA recognition. Consolidated CET1 ratio remains at 9%+.
- From a business perspective, merger with associate banks will provide significant long-term benefits. However, integration of 70k+ employees (34% of the parent workforce; size of business is 25% of the parent's) will be a key challenge. Further, we are surprised with the move of merging all associate banks at one go. In our view, one-by-one merger or amalgamating all associate banks together and then merging the entity with SBIN could have significantly reduced integration risk.

Exhibit 1: Share of SBI associates in SBIN banking business profitability

% of Banking business	FY12	FY13	FY14	FY15	FY16
NII	20.8	22.5	21.8	20.6	21.6
Total income	19.7	18.6	18.3	18.3	17.3
Operating expenses	20.5	21.5	20.8	20.0	20.2
Operating Profits	20.6	22.1	20.9	19.3	20.8
Profit before tax	22.1	20.3	19.5	20.0	14.2
Profit after tax	23.6	20.7	20.3	19.6	13.6

Note: FY16E data for SBI parent is based on our estimate

Source: MOSL, Company

#1 Increase in employee cost due to merger – a key thing to watch out for; Long term synergies remain

Currently, SBI (P) has three layer of retirement benefits for employees' v/s two layer benefits at associate banks. Hence, we expect superannuation cost impact immediately post-merger. Further, pay structure at SBI (P) is superior (due to some perks) to associate banks which could result in increase of employee staff costs. We expect immediate benefit from rationalization of treasury department and reduction in other admin expenses (for instance, one AGM, one Finance Dept, one HR department, etc.).

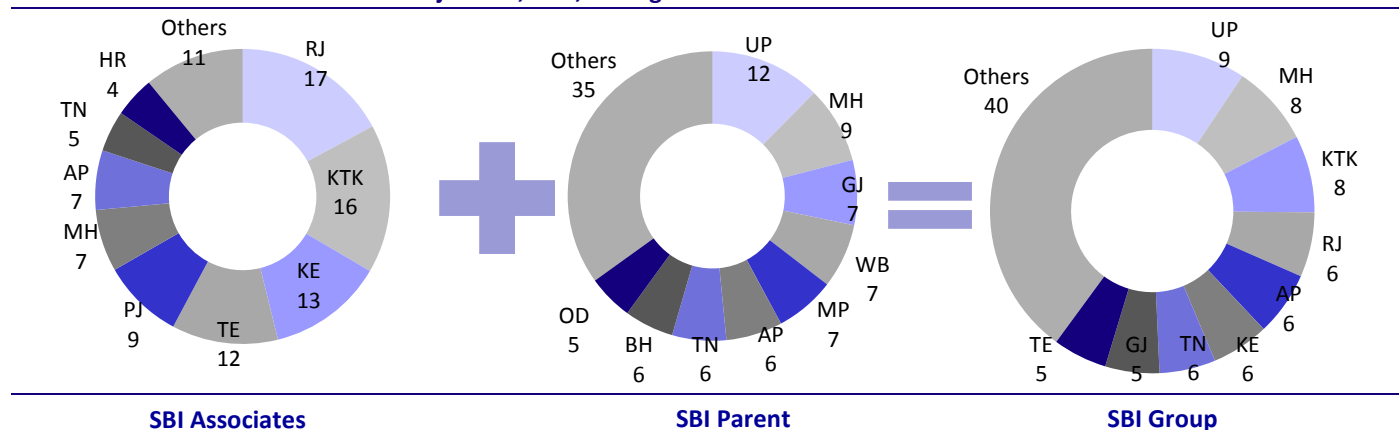
Exhibit 2: Cost per employee at associate banks lower than SBI parent

	No of employees	Emp expenses	Cost/Emp (INR M)
SBIN	213,148	251,754	1.18
SBI Asso.	71,953	58,643	0.82
SBT	13,775	10,724	0.78
SBM	10,193	9,761	0.96
SBBJ	13,529	11,260	0.83
SBH	23,806	15,962	0.67
SBM	10,650	10,937	1.03

Source: MOSL, Company

#2 Branch and ATM rationalization to be the key driver of synergy benefits

Currently, SBI standalone has 17,000+ branches and is the market leader in almost all states. Post-merger with associate banks, SBI will have 24,000+ branches with market share in states like Rajasthan, A.P., Telangana amongst other closer to 30% - which in our view could get rationalized over time.

Exhibit 3: Branches market share in Rajasthan, A.P., Telangana ~30% - an area of cost rationalization

Source: MOSL, Company

#3 Consolidated asset quality pressures remain elevated; Net stressed loans at SBI Subs stands at ~9%

Asset quality pressures persists at both parent and consolidated levels with SBI group net stressed loans 7%+ and subs at 9%+. Credit costs at associate banks are at 2%+ with PCR at ~45% - in-line with SBI (P).

Exhibit 4: Standard restructured loans of SBI Group stands at ~INR705b

	FY12	FY13	FY14	FY15	FY16
SBP	26,411	47,907	73,129	95,997	67,198
SBM	24,760	29,671	33,466	35,808	17,307
SBBJ	27,834	37,708	46,215	67,083	50,662
SBT	10,313	21,140	37,459	42,170	34,886
SBH	9,864	29,676	47,364	71,796	48,853
Subs Total	99,181	166,102	237,633	312,854	218,906
SBI	163,400	322,280	430,500	558,430	485,970
Consolidated	262,581	488,382	668,133	871,284	704,876
Subs as % of Consol	38	34	36	36	31

Note: FY16 data for SBP and SBI (P) is based on our estimate.

Source: MOSL, Company

Exhibit 5: Net NPA of SBI Group stands at ~INR616b

	FY12	FY13	FY14	FY15	FY16
SBP	8,484	11,942	24,045	30,492	32,682
SBM	7,684	12,088	16,303	11,216	22,572
SBBJ	9,454	13,033	17,709	17,692	20,052
SBT	8,536	9,886	19,285	13,987	19,026
SBH	10,020	14,487	29,849	23,485	37,432
Subs Total	44,178	61,435	107,190	96,872	131,762
SBI	158,189	219,565	310,961	275,906	484,635
Consolidated	202,366	280,999	418,151	372,777	616,397
Subs as % of Consol	22	22	26	26	21

Note: FY16 data for SBI (P) is based on our estimate.

Source: MOSL, Company

Exhibit 6: Net stressed loans (%) of SBI Group stands at ~7%

	FY12	FY13	FY14	FY15	FY16
SBP	5.5	8.1	12.7	16.0	12.1
SBM	8.1	9.3	10.0	9.0	7.4
SBBJ	7.6	8.8	9.9	12.1	9.7
SBT	3.4	4.6	8.2	8.1	8.2
SBH	2.6	4.9	8.0	9.0	7.7
Subs Total	5.0	6.8	9.7	10.9	9.1
SBI	3.7	5.2	6.1	6.4	6.7
Consolidated	4.0	5.6	6.9	7.4	7.2

Note: FY16 data for SBI (P) is based on our estimate.

Source: MOSL, Company

Exhibit 7: Consolidated slippages ratio in FY16 was 4.2% v/s 2.7% in FY15

	Slippages (INR m)		Slippages ratio (%)	
	FY15	FY16	FY15	FY16
SBP	47,085	92,309	5.9	11.2
SBM	18,955	35,734	3.6	6.6
SBBJ	16,875	27,195	2.4	3.7
SBT	44,749	52,362	6.5	8.0
SBH	30,493	58,188	2.9	5.2
Subs Total	158,156	265,787	4.2	6.9
SBI (P)	294,440	507,010	2.4	3.9
Consolidated	452,596	772,797	2.7	4.2

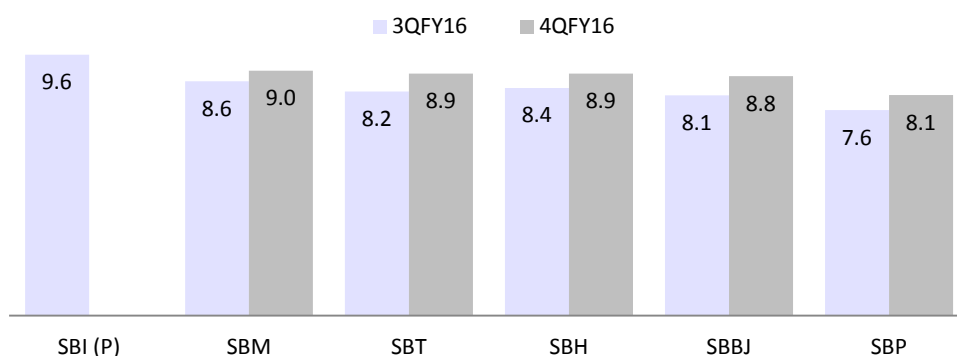
Note: FY16 data for SBI (P) is based on our estimate.

Source: MOSL, Company

#4 Well above regulatory capital requirement; however, growth capital still a challenge due to low double digit ROE

Consolidated CET1 ratio stood at ~9.4% as of 3QFY16; post RBI's relaxation (revaluation reserve, FCTR and DTA part of CET1), CET1 capital for associate banks have improved by 50-90bp in 4QFY16 (except SBP, all associate banks have at least 9% CET1). We expect some capital relief from subsidiaries due to revaluation of assets and healthy capital base of BMB (INR10b+). However, internal capital generation for SBIN remains moderate (9-10% RoE) resulting in growth capital constraint.

Exhibit 8: Except SBP, all associate banks have close to 9% CET1 ratio (%)



Note: We do not have SBIN 4QFY16 CET1 ratio. As per management interview, SBI has close to INR200b+ of **benefit from revaluation reserve**

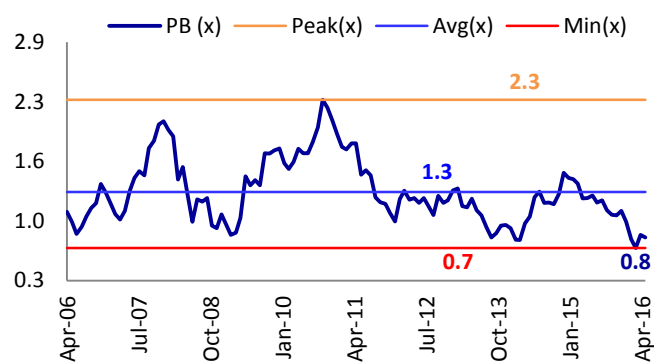
Source: MOSL, Company

Valuation and view

SBIN is highly levered to macro-economic conditions and improvement in investment climate and interest rates would assuage asset quality fears. Our credit costs assumptions remain very conservative. A 10bp decline in credit cost would lead to RoA benefit of ~5bp+. While the medium to long term outlook remains positive near term challenges remains on account of stress assets recognition, overhang of merger and chairman retirement by September 2016.

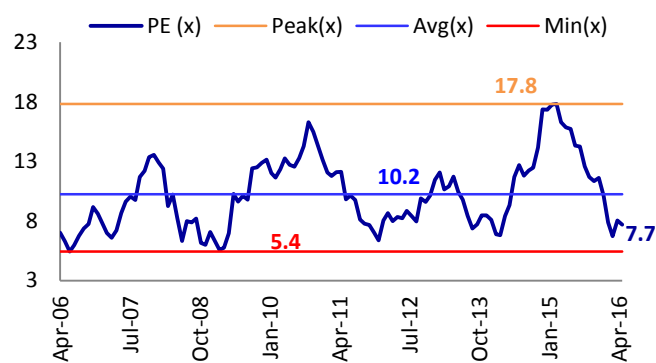
Our long term positive view on SBIN is driven by a) lowest NSL at ~6.5%, b) relatively healthy PCR of 65% (incl. technical w/o), c) conservation of capital, d) healthy capitalization (CET of ~10%, post RBI relaxation), e) strong liability franchise (Retail deposits of >95%) and f) focus on core operating profitability. In our view, valuations at 0.6x FY18E consol. P/BV and 6x FY18E consol. P/E largely factors in negative. **Buy.**

Exhibit 9: SBIN: 1yr forward P/BV (x)



Source: MOSL, Company

Exhibit 10: SBIN: 1yr forward P/E (x)



Source: MOSL, Company

Exhibit 11: Consolidated financial performance (INR b)

	SBI ASSO. AGG					SBI PARENT					SBI BANKING BUSINESS				
	FY12	FY13	FY14	FY15	FY16	FY12	FY13	FY14	FY15	FY16	FY12	FY13	FY14	FY15	FY16
NII	114	129	137	143	152	433	443	493	550	552	547	572	630	693	704
% Change (Y-o-Y)	10.5	13.6	6.2	4.3	6.2	33.1	2.4	11.2	11.6	0.4	27.7	4.7	10.1	10.0	1.6
Other Income	35	37	42	50	55	144	160	186	226	264	179	197	227	276	320
% Change (Y-o-Y)	3.4	3.7	13.5	21.3	9.8	-9.3	11.7	15.7	21.7	17.1	-7.1	10.2	15.3	21.6	15.8
Net Income	149	166	179	193	207	576	604	678	776	817	725	769	857	969	1,024
% Change (Y-o-Y)	8.7	11.2	7.8	8.3	7.2	19.2	4.7	12.4	14.4	5.3	16.9	6.1	11.4	13.1	5.7
Operating Exp.	67	77	94	100	103	261	293	357	387	419	327	370	451	487	522
% Change (Y-o-Y)	9.0	16.0	21.3	6.6	2.8	13.3	12.3	22.0	8.3	8.4	12.4	13.1	21.9	7.9	7.3
Operating Profit	82	88	85	93	104	316	311	321	389	397	398	399	406	482	502
% Change (Y-o-Y)	8.5	7.3	-4.0	10.2	11.9	24.6	-1.6	3.3	21.2	2.1	20.9	0.3	1.7	18.9	4.0
Other Provisions	30	37	46	45	79	131	111	159	196	246	161	149	205	241	326
Profit before Tax	52	51	39	48	25	185	200	162	193	151	237	250	201	241	176
Tax Provisions	16	14	11	16	9	68	58	53	62	50	84	72	64	78	59
Net Profit	36	37	28	32	16	117	141	109	131	101	153	178	137	163	117
% Change (Y-o-Y)	0.8	1.4	-24.5	15.2	-50.3	41.7	20.5	-22.8	20.3	-22.8	29.3	16.0	-23.1	19.3	-28.2
Loan Gr. (YoY, %)	20.9	17.7	6.8	5.5	3.7	14.7	20.5	15.7	7.5	12.0	17.0	19.9	13.1	7.1	9.8
ROA	0.90	0.77	0.52	0.57	0.27	0.91	0.97	0.65	0.68	0.47	0.93	0.91	0.60	0.65	0.43
Cost to income (%)	44.8	46.8	52.6	51.8	49.7	45.2	48.5	52.7	49.8	51.3	45.1	48.1	52.7	50.2	51.0
Gross NPA (INR b)	85.4	115.9	182.1	167.8	238.0	396.8	511.9	616.1	567.3	813.4	482.1	627.8	798.2	735.1	1051.3
Gross NPA (%)	3.0	3.4	5.0	4.4	6.0	4.4	4.8	5.0	4.3	5.5	4.1	4.4	5.0	4.3	5.6
Net NPA (INR b)	44.2	61.4	107.2	96.9	131.8	158.2	219.6	311.0	275.9	484.6	202.4	281.0	418.2	372.8	616.4
Net NPA (%)	1.5	1.8	3.0	2.6	3.4	1.8	2.1	2.6	2.1	3.3	1.8	2.0	2.7	2.2	3.3
PCR (%)	48.3	47.0	41.1	42.3	44.6	60.1	57.1	49.5	51.4	40.4	58.0	55.2	47.6	49.3	41.4
Tax Rate (%)	30.7	27.4	28.9	33.6	36.4	36.7	29.3	32.7	32.2	33.0	35.3	28.9	31.9	32.5	33.5

Source: MOSL, Company

Financials and Valuations

Income Statement (Standalone)					(INR Million)		
Y/E March	2012	2013	2014	2015	2016E	2017E	2018E
Interest Income	1,065,215	1,196,551	1,363,508	1,523,971	1,611,439	1,793,212	1,993,984
Interest Expense	632,304	753,258	870,686	973,818	1,059,000	1,168,455	1,292,100
Net Interest Income	432,911	443,293	492,822	550,152	552,439	624,756	701,884
Change (%)	33.1	2.4	11.2	11.6	0.4	13.1	12.3
Non Interest Income	143,514	160,368	185,529	225,759	264,452	287,809	316,368
Net Income	576,425	603,661	678,351	775,911	816,891	912,566	1,018,253
Change (%)	19.2	4.7	12.4	14.4	5.3	11.7	11.6
Operating Expenses	260,690	292,844	357,259	386,776	419,416	460,561	506,641
Pre Provision Profits	315,735	310,817	321,092	389,135	397,474	452,004	511,611
Change (%)	24.6	-1.6	3.3	21.2	2.1	13.7	13.2
Provisions (excl tax)	130,902	111,308	159,353	195,995	246,475	228,918	243,022
PBT	184,833	199,509	161,739	193,140	150,999	223,086	268,590
Tax	67,760	58,459	52,827	62,124	49,830	75,849	91,320
Tax Rate (%)	36.7	29.3	32.7	32.2	33.0	34.0	34.0
PAT	117,073	141,050	108,912	131,016	101,170	147,237	177,269
Change (%)	41.7	20.5	-22.8	20.3	-22.8	45.5	20.4
Cons. PAT post MI	153,431	179,162	141,738	169,943	127,202	187,340	223,057
Change (%)	43.6	16.8	-20.9	19.9	-25.2	47.3	19.1
				50	62	51	48
Balance Sheet							
Y/E March	2012	2013	2014	2015	2016E	2017E	2018E
Equity Share Capital	6,710	6,840	7,466	7,466	7,763	7,763	7,763
Reserves & Surplus	832,802	981,997	1,175,357	1,276,917	1,437,464	1,549,623	1,685,177
Net Worth	839,512	988,837	1,182,822	1,284,382	1,445,226	1,557,385	1,692,939
Deposits	10,436,474	12,027,396	13,944,085	15,767,932	17,660,084	20,132,496	23,152,371
Change (%)	11.7	15.2	15.9	13.1	12.0	14.0	15.0
of which CASA Dep	4,676,066	5,390,634	5,984,004	6,519,051	7,338,709	8,439,515	9,705,443
Change (%)	1.3	15.3	11.0	8.9	12.6	15.0	15.0
Borrowings	1,270,056	1,691,827	1,831,309	2,051,503	2,379,218	2,771,977	3,242,787
Other Liab. & Prov.	809,151	954,053	964,130	1,376,980	1,135,221	1,361,493	1,571,690
Total Liabilities	13,355,192	15,662,113	17,922,346	20,480,798	22,619,750	25,823,351	29,659,786
Current Assets	971,632	1,148,202	1,325,496	1,547,558	1,151,567	1,284,362	1,445,361
Investments	3,121,976	3,508,775	3,983,082	4,817,588	5,781,105	6,648,271	7,645,511
Change (%)	5.6	12.4	13.5	21.0	20.0	15.0	15.0
Loans	8,675,789	10,456,166	12,098,287	13,000,264	14,560,296	16,598,737	19,088,547
Change (%)	14.7	20.5	15.7	7.5	12.0	14.0	15.0
Fixed Assets	54,665	70,050	80,022	93,292	104,686	116,570	128,643
Other Assets	531,130	478,920	435,459	1,022,097	1,022,097	1,175,412	1,351,723
Total Assets	13,355,192	15,662,113	17,922,346	20,480,798	22,619,750	25,823,351	29,659,786
Asset Quality							
	(%)						
GNPA (INR m)	396,765	511,894	616,050	567,253	813,356	777,998	713,538
NNPA (INR m)	158,189	219,565	310,961	275,906	484,635	436,743	348,160
GNPA Ratio	4.45	4.76	4.97	4.27	5.46	4.59	3.67
NNPA Ratio	1.82	2.10	2.57	2.12	3.33	2.63	1.82
PCR (Excl Tech. W/O)	60.1	57.1	49.5	51.4	40.4	43.9	51.2
PCR (Incl Tech. W/O)	68.1	66.6	62.9	69.1	62.0	67.8	75.2

E: MOSL Estimates

Financials and Valuations

Ratios

Y/E March	2012	2013	2014	2015	2016E	2017E	2018E
Spreads Analysis (%)							
Avg. Yield-Earning Assets	9.2	9.0	8.8	8.8	8.3	8.1	7.8
Avg. Yield on loans	10.0	9.5	9.1	9.0	8.3	8.1	7.8
Avg. Yield on Investments	7.9	8.2	8.5	8.0	8.0	7.8	7.5
Avg. Cost-Int. Bear. Liab.	5.7	5.9	5.9	5.8	5.6	5.4	5.2
Avg. Cost of Deposits	5.6	6.0	6.0	6.0	5.9	5.7	5.5
Interest Spread	3.6	3.0	2.9	3.0	2.7	2.6	2.6
Net Interest Margin	3.8	3.3	3.2	3.2	2.8	2.8	2.8

Profitability Ratios (%)

RoE	16.0	15.9	10.5	11.2	7.8	10.2	11.3
RoA	0.9	1.0	0.6	0.7	0.5	0.6	0.6
Consolidated RoE	17.2	16.3	11.1	11.9	8.1	10.7	11.7
Consolidated RoA	0.9	0.9	0.6	0.7	0.5	0.6	0.6

Efficiency Ratios (%)

Cost/Income*	45.3	50.3	55.6	54.0	56.7	55.5	54.4
Empl. Cost/Op. Exps.	65.1	62.8	63.0	60.9	60.0	58.1	56.2
Busi. per Empl. (INR m)	82.2	93.7	107.8	125.9	144.4	164.8	188.7
NP per Empl. (INR lac)	5.3	6.4	4.8	6.0	4.8	7.0	8.5

* ex treasury and recoveries

Asset-Liability Profile (%)

Loans/Deposit Ratio	83.1	86.9	86.8	82.4	82.4	82.4	82.4
CASA Ratio	44.8	44.8	42.9	41.3	41.6	41.9	41.9
Investment/Deposit Ratio	29.9	29.2	28.6	30.6	32.7	33.0	33.0
G-Sec/Investment Ratio	81.9	76.7	77.4	78.4	68.8	68.0	67.9
CAR	13.9	12.9	12.4	12.0	11.5	10.8	10.2
<i>Tier 1</i>	<i>9.8</i>	<i>9.5</i>	<i>9.7</i>	<i>9.6</i>	<i>9.3</i>	<i>8.9</i>	<i>8.5</i>

Valuation

Book Value (INR)	121	139	150	164	178	193	210
BV Growth (%)	19.8	14.8	7.8	9.0	8.8	8.1	9.1
Price-BV (x)	1.5	1.3	1.2	1.1	1.0	0.9	0.8
Consol BV (INR)	154	177	188	207	223	243	266
BV Growth (%)	18.3	14.8	6.5	10.0	7.8	8.8	9.6
Price-Consol BV (x)	1.1	0.9	0.9	0.8	0.7	0.7	0.6
Adjusted BV (INR)	105	117	121	138	135	153	179
Price-ABV (x)	1.7	1.5	1.5	1.3	1.3	1.2	1.0
Adjusted Consol BV	132	147	149	172	168	193	226
Price-Consol ABV (x)	1.3	1.1	1.1	1.0	1.0	0.9	0.7
EPS (INR)	17.4	20.6	14.6	17.5	13.0	19.0	22.8
EPS Growth (%)	34.0	18.2	-29.3	20.3	-25.7	45.5	20.4
Price-Earnings (x)	10.1	8.6	12.1	10.1	13.6	9.3	7.8
Consol EPS (INR)	22.9	26.2	19.0	22.8	16.4	24.1	28.7
Con. EPS Growth (%)	35.9	14.6	-27.5	19.9	-28.0	47.3	19.1
Price-Consol EPS (x)	7.3	6.4	8.7	7.4	10.2	6.9	5.8
Dividend Per Share (INR)	3.5	4.2	3.0	3.5	2.7	3.9	4.6
Dividend Yield (%)	2.0	2.3	1.7	2.0	1.5	2.2	2.6

E: MOSL Estimates

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