

## State Bank of India

### NPL stresses overshadow NIM improvement

- **SBI reported strong operating numbers**, ahead of market expectations, but that was overshadowed by high loan delinquencies at 4.1%. Overall PAT of Rs 28.1 bn (up 12.4% y/y) was 10.4% ahead of consensus (slightly below JPM) but the weak asset quality detracted from the relevance of reported numbers. Management is targeting improvement in 2H, but much of that depends on the economic cycle.
- **Gross NPLs jumped 22% q/q** to Rs 339bn, reaching a ratio of 4.1%. Incremental gross delinquency jumped to Rs 80bn (4.1% of opening loan book, annualized), with the stress coming from multiple quarters. Management did point to a couple of lumpy accounts which they expect to reverse in the coming quarters - from the agro and textile sectors. To achieve its target of 1.7% net NPLs by FY12-end, we think SBI will have to get some support from an improving macro.
- **Operating earnings were strong**, with NIMs surprising on the upside, mainly from loan pricing. The new management is commercially focused and very aggressive with pricing - also, the base rate system is pushing up loan yields, though somewhat at the cost of raising the credit risk pricing. There are no signs of a savings rate hike yet - if SBI and the larger banks can hold rates, we see SBI NIMs improving from here.
- **Capital issues are getting sorted out.** The management expects at least Rs 30-40bn of capital infusion by the government by end-FY12 (more if it's a rights issue) - also, efforts at improving the RWA/loans ratio should yield around 40-50 bp in T1 CAR by end-FY12. We think the bank should be able to haul the T1 above 9% by end-FY12.
- **We see the near term remaining challenging** for SBI, with little sign of asset quality stresses abating. We think the undemanding valuation does make the stock attractive for the long term; however, that's only for the patient investor willing to look through short-term volatility.

## Overweight

SBI.BO, SBIN IN

Price: Rs1,997.30

Price Target: Rs2,400.00

### India

#### Financials

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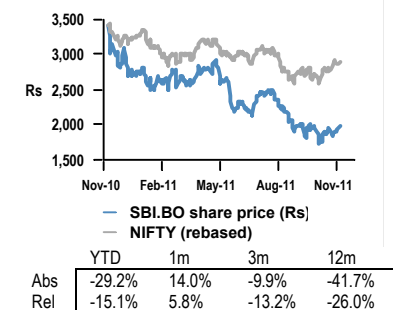
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#### Price Performance



#### State Bank of India (Reuters: SBI.BO, Bloomberg: SBIN IN)

Year-end Mar (Rs in mn)	FY10A	FY11A	FY12E	FY13E	FY14E
Operating Profit (Rs mn)	225,518	321,781	384,516	447,962	524,124
Net Profit (Rs mn)	116,982	111,798	162,667	209,692	244,328
Cash EPS (Rs)	184.26	176.06	233.22	300.64	350.30
Fully Diluted EPS (Rs)	153.21	159.35	222.89	287.73	343.13
DPS (Rs)	30.00	30.00	36.00	43.20	51.84
EPS growth (%)	4.1%	(4.4%)	32.5%	28.9%	16.5%
ROE	15.0%	13.4%	16.7%	17.4%	17.5%
P/E	10.8	11.3	8.6	6.6	5.7
BVPS (Rs)	1,309.46	1,314.53	1,602.89	1,852.99	2,142.63
P/BV	1.5	1.5	1.2	1.1	0.9
Div. Yield	1.5%	1.5%	1.8%	2.2%	2.6%

Source: Company data, Bloomberg, J.P. Morgan estimates.

#### Company Data

52-wk range (Rs)	3,515.00 - 1,708.55
Market cap (Rs mn)	1,268,286
Market cap (\$ mn)	25,825
Shares outstanding (mn)	635
Fiscal Year End	Mar
Price (Rs)	1,997.30
Date Of Price	08 Nov 11
Avg daily value (Rs mn)	1,279.6
Avg daily value (\$ mn)	26.1
AVG_	

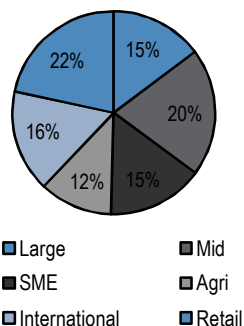
#### See page 8 for analyst certification and important disclosures, including non-US analyst disclosures.

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### Company Description

SBI is the largest bank in India with a 59% government stake. It has a loan book of ~US\$225bn with exposure corporate, SME, retail, international and Agri sectors and forms >20% of total system credit. It has the highest number of branch network and strong rural presence leading to high CASA at ~48%.

### Loan Break up



Source: Company data.

### EPS: J.P. Morgan vs. consensus

	J. P. Morgan	Consensus
FY12E	235	175
FY13E	307	232

Source: Bloomberg, J.P. Morgan estimates.

### P&L sensitivity metrics

	EBITDA Impact (%)	EPS Impact (%)
NIMs		
Impact of each 10bps	5.4%	7.0%
Cost to Income		
Impact of each 100bps	3.2%	4.2%
Provisions/Assets		
Impact of each 10bps	0.0%	7.0%

Source: J.P. Morgan estimates.

### Price target and valuation analysis

Our Mar-12 PT for SBI to Rs2400 based on Gordon growth model with a normalised ROE of 16.8% and 2nd stage growth of 17% and Rs100/share for the insurance business. Our PT implies 1.5x FY12E book and 10x FY12E EPS.

ROE	16.8%
2nd stage growth	17.0%
Terminal growth	5.0%
Insurance business valuation	100.3
<b>Mar-12 PT</b>	2400
Implied FY12 P/B ex insurance	1.43

### Normalised ROE

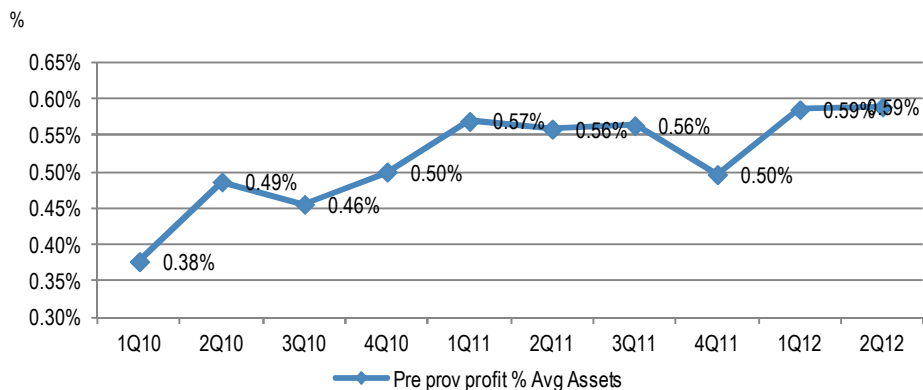
NII/Assets	3.1%
Other income/assets	1.2%
Revenues/assets	4.3%
Costs/assets	2.1%
Provisions/assets	0.6%
ROA	1.0%
ROE	16.8%

Key downside risks are slower economic growth leading to higher delinquencies and slower loan growth.

### Improving pre provision profits as a percentage of total assets

We note that the pre provision profits as a percentage of the average assets is at the highest over the last few quarters as shown in the chart below.

Figure 1: Quarterly pre provision profit % average assets



Source: Company reports

### ROE improvement is driven by the higher net interest income

We have shown the ROE break-up in the table below. We note that NII % Assets have steadily improved over the past quarters from 2.06% in 1Q 10 to 3.29% in 2Q 12 and this has helped in driving the ROE higher.

Table 1: SBI ROE break up quarterly

ROE Break up	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12
Net Interest Income/Assets	2.06%	2.26%	2.49%	2.59%	2.71%	2.85%	3.02%	2.63%	3.14%	3.29%
Fees/Assets	1.17%	1.20%	1.16%	1.57%	1.31%	1.34%	1.03%	1.46%	1.09%	1.07%
Investment profits/Assets	0.29%	0.22%	0.17%	0.16%	0.06%	0.07%	0.07%	0.11%	0.05%	0.01%
Net revenues/Assets	3.53%	3.68%	3.82%	4.33%	4.08%	4.26%	4.12%	4.21%	4.28%	4.37%
Operating Expense/Assets	-2.02%	-1.73%	-2.00%	-2.33%	-1.81%	-2.03%	-1.87%	-2.22%	-1.94%	-2.01%
Provisions/Assets	-0.07%	-0.41%	-0.34%	-0.90%	-0.58%	-0.92%	-0.68%	-1.36%	-1.34%	-1.07%
Taxes/Assets	-0.48%	-0.54%	-0.51%	-0.38%	-0.62%	-0.43%	-0.63%	-0.62%	-0.49%	-0.40%
Total Costs/Assets	-2.57%	-2.67%	-2.84%	-3.61%	-3.00%	-3.38%	-3.18%	-4.20%	-3.77%	-3.48%
ROA	0.96%	1.00%	0.98%	0.72%	1.08%	0.88%	0.94%	0.01%	0.51%	0.89%
Equity/Assets	6.01%	6.13%	6.25%	6.23%	6.13%	5.97%	5.94%	5.69%	5.26%	5.29%
ROE	15.8%	16.2%	15.5%	11.4%	17.3%	14.3%	15.5%	0.1%	9.6%	16.5%

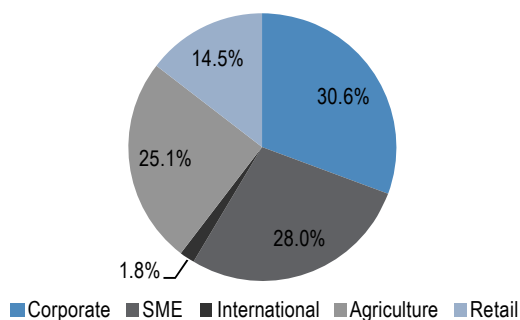
Source: Company reports & J.P. Morgan estimates

**Slippages in 2Q 12 are mostly from the corporate and the SME**

SME and corporate segment accounts for 59% of the fresh slippages of 2Q 12 as shown in the chart below.

**Figure 2: Fresh slippages in 2Q 12 by segment**

%



Source: Company reports.

We have shown in the table below the detailed split of the slippages in the corporate and SME in the table below. We note that most of the slippages are coming from the Iron/steel + Metal + Mining and Agro based industries.

**Table 2: Slippages in the corporate and the SME split**

Rs mn, %

Fresh slippages	2Q 12 %	2Q 12 Rs mn
Iron/Steel+ Metal + Mining	10.2%	4,770
Agro based	27.0%	12,680
Govt sponsored	5.8%	2,740
Textiles	6.2%	2,890
Engineering	1.9%	890
Gems & Jewellery	4.7%	2,190
Infrastructure	1.3%	620
Hospitality	5.1%	2,380
Paper/Plastics	3.7%	1,720
Trading & Retail	2.6%	1,200
Education	1.4%	650
IT	0.3%	120
Miscellaneous	30.1%	14,120
<b>Grand Total</b>	<b>100.0%</b>	<b>46,970</b>

Source: Company reports.

### SBI 2Q 2012 results summary

Table 3: SBI 2Q 2012 results summary

Rs mn, %

(Rs m)	2Q11	1Q12	2Q12	YoY	QoQ
Interest income	198,081	241,974	259,671	31.1%	7.3%
Interest expenses	116,932	144,979	155,452	32.9%	7.2%
Net interest income	81,149	96,995	104,219	28.4%	7.4%
Non-interest income	40,052	35,342	34,272	-14.4%	-3.0%
Operating expenses	57,631	59,913	63,749	10.6%	6.4%
Pre prov profit	63,570	72,424	74,743	17.6%	3.2%
Provisions	26,215	41,569	33,855	29.1%	-18.6%
Profit before tax	37,356	30,855	40,888	9.5%	32.5%
Provision for tax	12,342	15,020	12,784	3.6%	-14.9%
Profit after tax	25,014	15,836	28,104	12.4%	77.5%
NII / GII	41.0%	40.1%	40.1%	-0.8%	0.1%
Cost - Income	47.5%	45.3%	46.0%	-1.5%	0.8%
Prov / PPP	41.2%	57.4%	45.3%	4.1%	-12.1%
NIMs - (cum) reported	3.30%	3.62%	3.70%	0.4%	0.1%
NIMs - Qtrly	3.43%	3.62%	3.79%	0.4%	0.2%
Tax rate	33.0%	48.7%	31.3%	-1.8%	-17.4%
<b>Balance sheet data</b>					
Advances	6,932	7,882	8,106	16.9%	2.8%
Deposits	8,553	9,501	9,732	13.8%	2.4%
C/D ratio	81.0%	83.0%	83.3%	2.2%	0.3%
CASA Ratio	48.5%	47.9%	47.6%	-0.9%	-0.3%
<b>Asset quality</b>					
Gross NPL (Rs bn)	232,046	277,680	339,463	46.3%	22.2%
Net NPL (Rs bn)	116,012	124,350	161,205	39.0%	29.6%
Gross NPL (%)	3.4%	3.5%	4.2%	0.84%	0.67%
Net NPL (%)	1.7%	1.6%	2.0%	0.34%	0.43%
LLP/Loans	1.27%	1.57%	1.52%	0.2%	-0.1%
Coverage	50.0%	55.2%	52.5%	2.51%	-2.71%
ROA	0.97%	0.50%	0.69%	-0.28%	0.19%
Tier I (%)	9.62%	7.60%	7.47%	-2.15%	-0.13%
<b>Other income (Rs mn)</b>					
Core fees	32,537	29,641	30,810	-5.3%	3.9%
Others	5,542	4,012	3,182	-42.6%	-20.7%
Treasury	1,973	1,689	281	-85.8%	-83.4%

Source: Company reports.

Table 4: SBI (Consolidated basis) results summary

Rs mn, %

Consolidated	2Q11	1Q12	2Q12	YoY	QoQ
Interest on Advances	205,707	251,025	268,628	30.6%	7.0%
Interest on Invst	68,387	76,817	82,927	21.3%	8.0%
Interest on other res	5,096	6,327	5,462	7.2%	-13.7%
Interest income	279,190	334,169	357,018	27.9%	6.8%
Interest expenses	164,587	202,929	218,885	33.0%	7.9%
Net interest income	114,603	131,240	138,133	20.5%	5.3%
Other income	100,064	57,092	55,473	-44.6%	-2.8%
Operating expenses	132,863	95,867	98,587	-25.8%	2.8%
Pre prov profit	81,804	92,465	95,018	16.2%	2.8%
Provisions	40,420	49,444	43,749	8.2%	-11.5%
Profit before tax	41,384	43,021	51,269	23.9%	19.2%
Provision for tax	17,013	18,607	15,862	-6.8%	-14.8%
<b>Profit after tax</b>	<b>24,371</b>	<b>24,414</b>	<b>35,408</b>	<b>45.3%</b>	<b>45.0%</b>

Source: Company reports.

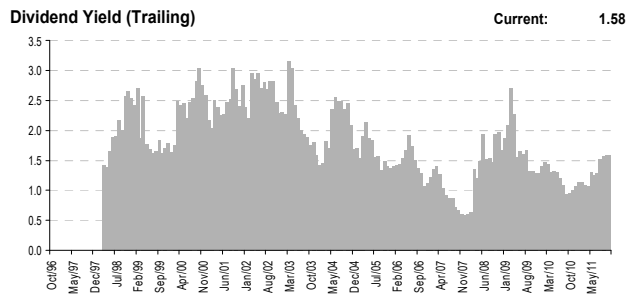
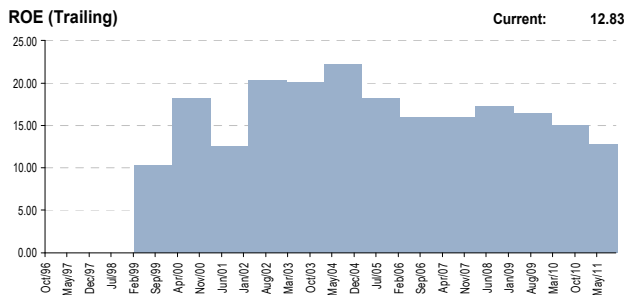
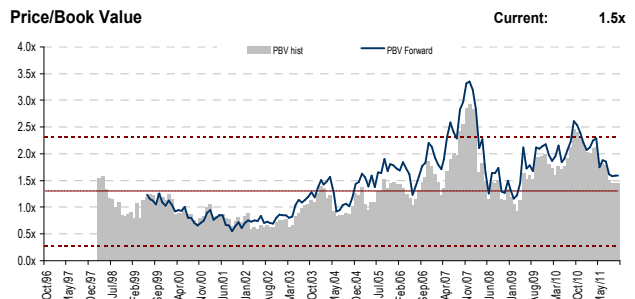
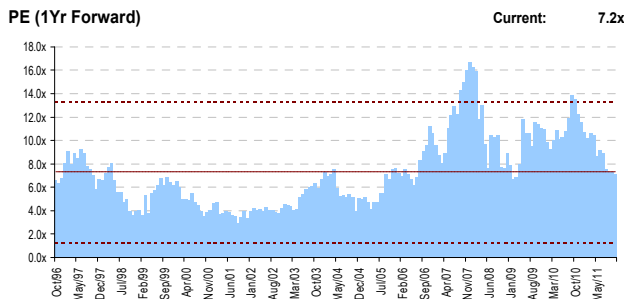
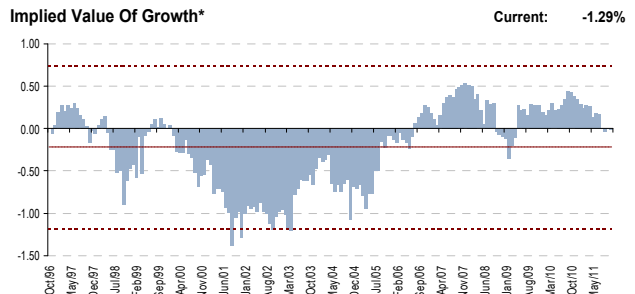
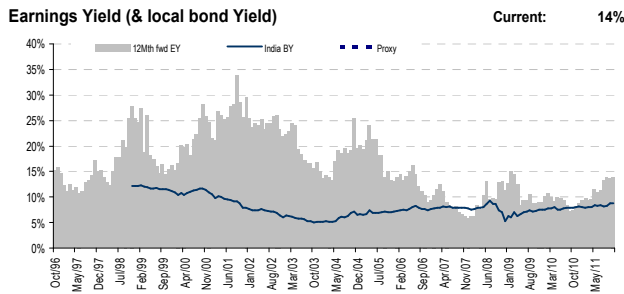
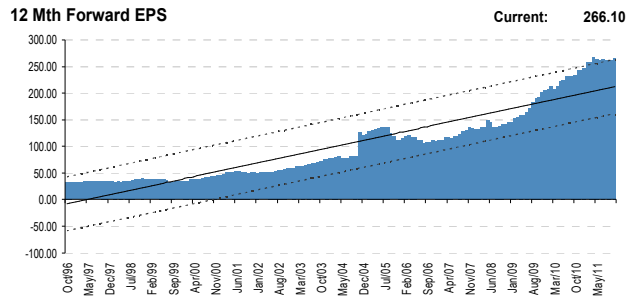
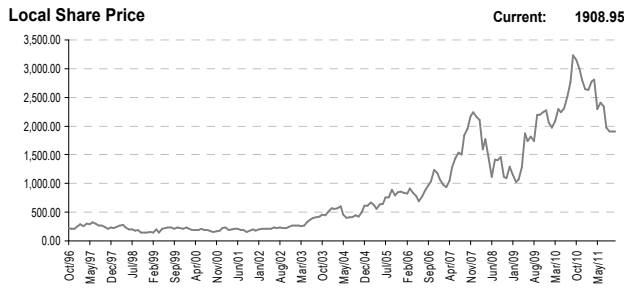
## State Bank of India: Summary of Financials

Income Statement						Growth Rates					
Rs in millions, year end Mar	FY10	FY11	FY12E	FY13E	FY14E		FY10	FY11	FY12E	FY13E	FY14E
NIM (as % of avg. assets)	2.5%	3.1%	3.3%	3.3%	3.2%	Loans	16.2%	16.1%	18.4%	18.1%	18.1%
Earning assets/assets	96.1%	96.2%	96.2%	96.3%	96.3%	Deposits	16.6%	30.0%	20.7%	17.8%	16.6%
Margins (% of earning assets)	2.4%	2.9%	3.1%	3.1%	3.1%	Assets	11.1%	13.6%	18.0%	17.1%	17.7%
						Equity	14.8%	0.4%	33.9%	15.6%	15.6%
Net Interest Income	334,432	455,500	564,475	660,083	773,558	RWA	11.9%	16.7%	18.0%	18.0%	18.0%
Total Non-Interest Income	157,472	184,197	207,653	249,481	286,550	Net Interest Income	15.2%	36.2%	23.9%	16.9%	17.2%
Fee Income	-	-	-	-	-	Non-Interest Income	19.9%	17.0%	12.7%	20.1%	14.9%
						of which Fee Grth	-	-	-	-	-
Other Operating Income	-	-	-	-	-	Revenues	10.3%	12.5%	17.5%	19.0%	19.6%
Total operating revenues	491,904	639,698	772,128	909,564	1,060,108	Costs	27.7%	19.3%	21.9%	19.1%	16.1%
						Pre-Provision Profits	5.9%	42.7%	19.5%	16.5%	17.0%
Operating costs	-266,387	-317,917	-387,612	-461,602	-535,984	Loan Loss Provisions	2.6%	116.4%	-2.9%	-8.2%	19.0%
						Pre-Tax	-	-	-	-	-
Pre-Prov. Profits	225,518	321,781	384,516	447,962	524,124	Attributable Income	4.1%	-4.4%	45.5%	28.9%	16.5%
Provisions	-61,563	-133,198	-129,351	-118,749	-141,303	EPS	4.1%	-4.5%	32.5%	28.9%	16.5%
Other Inc/Exp. (treasury Income)	19,712	10,614	7,200	9,000	5,000	DPS	19.2%	0.0%	20.0%	20.0%	20.0%
Exceptionals	0	0	0	0	0						
Pre-tax	183,666	199,197	262,365	338,213	387,822	<b>Balance Sheet Gearing</b>	<b>FY10</b>	<b>FY11</b>	<b>FY12E</b>	<b>FY13E</b>	<b>FY14E</b>
Tax	66,684	87,399	99,699	128,521	143,494	Loan/deposit	78.9%	81.4%	82.1%	81.5%	80.5%
Minorities	-	-	-	-	-	Investment/assets	5.6%	5.9%	5.7%	5.2%	4.8%
Other Distbn.	-	-	-	-	-	Loan/Assets	60.1%	61.2%	61.2%	61.6%	61.8%
Attributable Income	116,982	111,798	162,667	209,692	244,328	Customer deposits/liab.	81.8%	80.4%	80.7%	81.8%	83.0%
						LT debt/liabilities	8.4%	8.7%	8.6%	7.6%	6.8%
<b>Per Share Data Rs</b>	<b>FY10</b>	<b>FY11</b>	<b>FY12E</b>	<b>FY13E</b>	<b>FY14E</b>	<b>Asset Quality/Capital</b>	<b>FY10</b>	<b>FY11</b>	<b>FY12E</b>	<b>FY13E</b>	<b>FY14E</b>
EPS	184.26	176.06	233.22	300.64	350.30	Loan loss reserves/loans	-1.3%	-1.6%	-1.9%	-2.0%	-2.1%
DPS	30.00	30.00	36.00	43.20	51.84	NPLs/loans	2.8%	3.2%	3.4%	3.6%	3.8%
Payout	16.3%	17.0%	15.4%	14.4%	14.8%	Specific loan loss reserves/NPLs	-44.6%	-49.6%	-56.4%	-56.4%	-56.4%
Book value	1,309.46	1,314.53	1,602.89	1,852.99	2,142.63	Growth in NPLs	31.6%	29.8%	28.5%	23.3%	23.7%
Fully Diluted Shares	634.88	634.99	697.49	697.49	697.49	Tier 1 Ratio	9.5%	7.8%	9.3%	9.0%	8.8%
						Total CAR	13.4%	12.0%	13.4%	12.5%	11.8%
<b>Key Balance sheet Rs in millions</b>	<b>FY10</b>	<b>FY11</b>	<b>FY12E</b>	<b>FY13E</b>	<b>FY14E</b>	<b>Du-Pont Analysis</b>	<b>FY10</b>	<b>FY11</b>	<b>FY12E</b>	<b>FY13E</b>	<b>FY14E</b>
Net Loans	8,917,310	10,384,878	12,343,833	14,590,700	17,250,182	NIM (as % of avg. assets)	2.5%	3.1%	3.3%	3.3%	3.2%
LLR	111,147	160,431	234,147	288,782	357,341	Earning assets/assets	96.1%	96.2%	96.2%	96.3%	96.3%
Gross Loans	8,806,163	10,224,447	12,109,685	14,301,918	16,892,841	Margins (as % of Avg. Assets)	2.4%	2.9%	3.1%	3.1%	3.1%
NPLs	248,970	323,163	415,183	512,060	633,626	Non-Int. Rev./ Revenues	32.0%	28.8%	26.9%	27.4%	27.0%
Investments	815,183	968,601	1,110,728	1,191,256	1,290,696	Non IR/Avg. Assets	1.1%	1.2%	1.2%	1.2%	1.2%
Other earning assets	473,839	575,446	661,763	761,027	904,625	Revenue/Assets	3.6%	4.1%	4.3%	4.3%	4.3%
Avg. IEA	13,209,802	14,874,951	17,246,049	20,293,333	23,846,342	Cost/Income	54.2%	49.7%	50.2%	50.7%	50.6%
Goodwill	-	-	-	-	-	Cost/Assets	1.9%	2.1%	2.2%	2.2%	2.2%
Assets	14,475,026	16,449,168	19,415,145	22,739,855	26,774,564	Pre-Provision ROA	5.5%	6.2%	6.5%	6.5%	6.4%
						LLP/Loans	-0.8%	-1.4%	-1.2%	-0.9%	-0.9%
Deposits	11,164,646	12,555,625	14,756,404	17,552,991	20,984,758	Loan/Assets	59.6%	61.5%	62.3%	62.6%	63.0%
Long-term bond funding	1,220,646	1,424,708	1,661,498	1,733,296	1,810,046	Other Prov. Income/ Assets	0.1%	0.1%	0.0%	0.0%	0.0%
Other Borrowings	373,133	437,576	487,576	497,576	507,576	Operating ROA	1.6%	2.1%	2.1%	2.1%	2.1%
Avg. IBL	11,778,875	13,182,812	15,199,117	17,852,095	21,040,546	Pre-Tax ROA	5.2%	5.4%	5.8%	6.0%	5.9%
Avg. Assets	13,750,500	15,462,097	17,932,157	21,077,500	24,757,210	Tax rate	-	-	-	-	-
Common Equity	831,356	834,712	1,118,001	1,292,439	1,494,462	Minorities & Outside Distbn.	0.0%	0.0%	0.0%	0.0%	0.0%
RWA	9,069,176	10,584,651	12,489,888	14,738,068	17,390,920	ROA	0.9%	0.7%	0.9%	1.0%	1.0%
Avg. RWA	8,587,354	9,826,913	11,537,270	13,613,978	16,064,494	RORWA	1.4%	1.1%	1.4%	1.5%	1.5%
						Equity/Assets	5.7%	5.4%	5.4%	5.7%	5.6%
						ROE	15.0%	13.4%	16.7%	17.4%	17.5%

Source: Company reports and J.P. Morgan estimates.

**JPM Q-Profile**  
**State Bank of India (INDIA / Financials)**  
 As Of: 04-Nov-2011

**Global Equity Quantitative Analysis**  
 Quant\_Strategy@jpmorgan.com



**Summary**

State Bank of India		SEDOL		6100799		As Of:		4-Nov-11			
INDIA						Local Price:		1,908.95			
Financials						EPS:		266.10			
	Latest	Min	Max	Median	Average	2 S.D.+	2 S.D. -	% to Min	% to Max	% to Med	% to Avg
12mth Forward PE	7.17x	2.96	16.74	6.76	7.32	13.35	1.28	-59%	133%	-6%	2%
P/BV (Trailing)	1.45x	0.60	2.93	1.19	1.30	2.32	0.28	-59%	102%	-18%	-11%
Dividend Yield (Trailing)	1.58	0.59	3.15	1.71	1.82	3.04	0.61	-63%	99%	8%	16%
ROE (Trailing)	12.83	10.27	22.14	16.40	16.62	23.10	10.15	-20%	73%	28%	30%
Implied Value of Growth	-1.3%	-1.39	0.53	-0.09	-0.22	0.74	-1.17	-10688%	4236%	-623%	-1577%

Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, J.P. Morgan Calcs

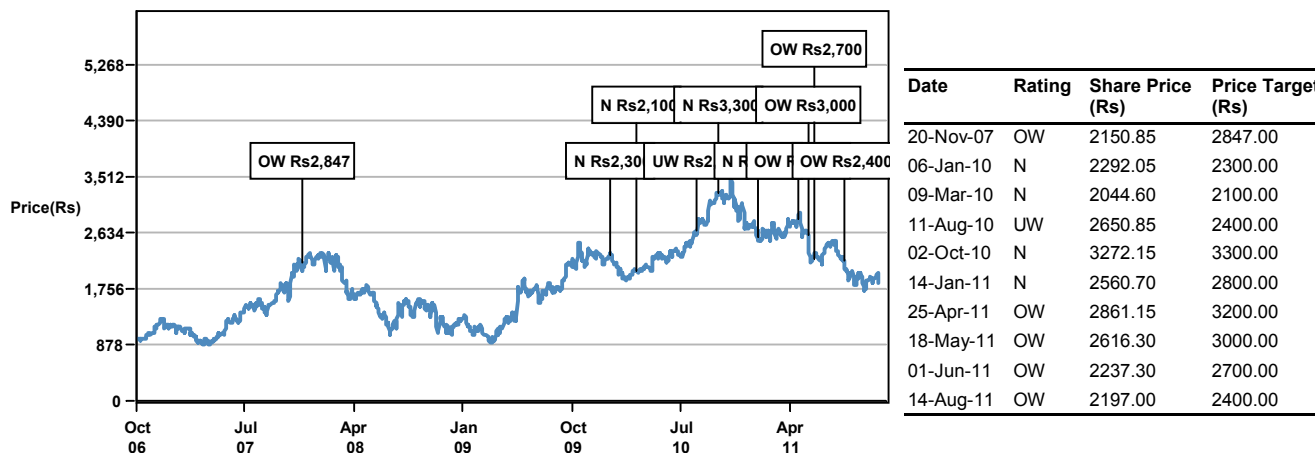
\* Implied Value Of Growth = (1 - EY/Cost of equity) where cost of equity = Bond Yield + 5.0% (ERP)

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State Bank of India (SBI.BO) Price Chart



Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Nov 20, 2007.

The chart(s) show J.P. Morgan's continuing coverage of the stocks; the current analysts may or may not have covered it over the entire period.

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IB clients*	51%	44%	33%
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