6 November 2023

MOTILAL OSWAL FINANCIAL SERVICES

the CornerOffice
Interaction with the CMO

Spends momentum robust; remain watchful on near-term margins

Credit cost to witness a gradual moderation

We organized an interactive session with Mr Girish Budhiraja, Chief Sales & Marketing Officer, Ms Rashmi Mohanty, Chief Financial Officer and Mr. Shantanu Srivastava, Chief Risk Officer at SBI Cards to discuss the outlook of the credit card industry and the key business metrics of SBICARD. Key insights from the discussion are highlighted below:

Spends momentum healthy; festive demand to aid overall business activity

SBICARD has strengthened its position as the second largest card player in the country with a market share of 19.2% in O/S cards and 17.9% in overall spending. O/S cards for SBICARD stood at 17.9m in Sep'23 vs. 14.8m in Sep'22 and the company expects the card base for the industry to grow at ~18-20% over the next few years. Industry spends too are growing at a healthy run rate and stands close to its all-time high at INR1.4t during Sep'23. Further, buoyed by the demand in festive season, the spends momentum is likely to maintain a healthy rate and the company expects retail card spends to register a CAGR of 25% over the next few years.

Online spends robust; Rupay cards remain an interesting business opportunity

POS spends have picked up across all key categories, though the mix of online spends continues to remain robust at ~55-57%. Rupay cards in the portfolio stands at 10% with the company being the largest player in RuPay credit cards. Currently, 9% of RuPay cardholders actively use UPI, with an average monthly spending of INR11,000. This trend bodes well for overall spending, especially in Tier 2-3 cities where the POS infrastructure is limited.

SBI Cards and Payment Services

Mr. Girish Budhiraja – Chief Sales & Marketing Officer

Mr. Budhiraja joined SBI Card on 22 Oct'12 and has been a part of SBI group, for almost a decade. He has handled several key assignments, across India with a total experience of ~28 years.An Engineering Graduate, Mr. Budhiraja has completed B tech from IIT, Dhanbad and has done masters in business administration from IIM, Bangalore.

Static revolver mix coupled with rising CoF to keep near-term margins under check

SBICARD's revolver rate has been static for the past several quarters at 24% (down 10% from the 2QFY21-levels). The company has tried to mitigate the impact fromlower revolve rate by increasing the mix of EMI customers. Consequently, the combined percentage of Revolve and EMI loans has risen to 62% (300bp YoY increase). The company expects the revolve rate to be sticky in the near term though the mix of EMI customers will likely show an improving trend. Management expects the cost of funds to witness slight pressure going forward as the rate environment has hardened further, keeping near-term margins under check. SBIC has about 65% of the borrowings from short-term funds, re-pricing of which is likely to exert pressure on overall funding costs. SBI Cards has reported NIM compression of 12b QoQ in 2QFY24 and has guided for near-term margin pressure to continue before it recovers in FY25.

Credit Cost to stay elevated; normalization likely to happen in a few quarters

Credit cost is expected to stay elevated over the near term, reflecting a slight increase in systemic stress with respect to unsecured loans. The company has witnessed higher stress from the 2019 vintage and indicated that the share of this portfolio in total NEA has declined to 14% and 2018 cohort stands at ~8% currently. SBICARD has implemented several portfolio and account monitoring measures to detect early warning signs, effectively limiting the levels of asset quality stress. Credit Bureau reports that the delinquency in credit cards and PL is showing an uptick and there is a pick-up in 30-day and 90-day delinquencies. SBI Cards has thus indicated the presence of some stress build-up in the consumer loan portfolio. Consequently, we anticipate that credit costs will remain elevated in the near term, with projected FY24E credit costs at 6.4% vs 6.0% in FY23.

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Sourcing from Banca and Open channel at equal weights; focus shifted to tier 2 cities and below

Incremental sourcing from the Banca channel has improved and now forms ~49% of the total card sourcing vs. 42% on an outstanding basis. In terms of new sourcing, Tier-2 & 3 now form 51% of the incremental sourcing (vs. 46% on an outstanding basis) with the customers typically undertaking utility-based spends. Further, the mix of self-employed category in the new card sourcing has also increased to 41%, reflecting the change in the geographical mix. SBIC had witnessed issues in Tier 3 & 4 cities and has taken corrective steps to control issues in this book. SBICARD believes that the linking of Rupay cards with UPI is useful for Tier 2-4 cities as these cities lack the POS infrastructure which augurs well for overall card spending in these geographies.

Other highlights

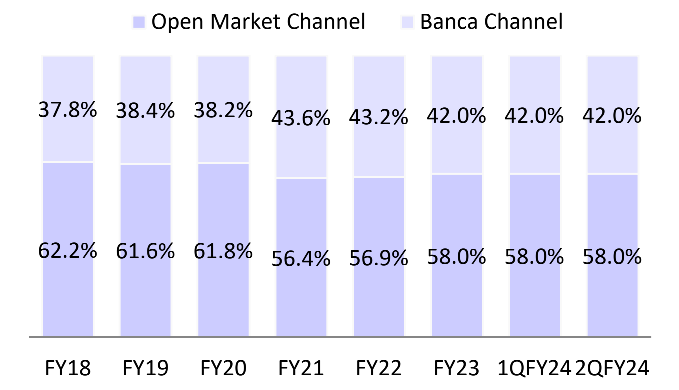
- Revolver customers have a lower tenor of ~2-4 months with higher interest rate of ~42% than EMI customers who have a tenor of ~9-12 months with an interest rate of ~18-20%.
- Most of the subvention book is re-priced; Flexi pay is of 11-12 months tenor and some part is yet to be re-priced. Flexi rates had come down earlier and now the rates are 200bp higher than the lower levels seen in Jul-Aug'22. Encash rates are broadly similar; and subvention has gone up by 100- 200bp.
- In the open market, when acquiring new customers, the company exclusively targets creditworthy individuals. It looks for existing credit card customers with a healthy CIBIL score of 720+. On the banca side, the company aims to acquire new to credit and new to credit card customer.
- SBI Cards has effectively managed stress within the 2019 cohort, and the portfolio-level strategies have yielded positive results. However, the management has noted a slight increase in stress, with some customers facing challenges in repayment. The proportion of the 2019 cohort has declined to 14% from 16% of NEA.
- SBI Card has witnessed some stress in Tier 3 and 4 cities, after which, it exited some of these cities. SBICARD expects the stress levels to be elevated in 3Q, though this is not due to any specific cohort and reflects the ongoing systemic trends.
- The company has tied up with Reliance retail and has launched Reliance SBI Credit card on 31st October, aimed toward garnering more share in retail spending.

Valuation and view: Near-term profitability suppressed; Estimate earnings to accelerate from FY25E

SBICARD has been reporting a mixed performance as spends momentum has been strong, while higher credit cost and lower margins are dragging earnings. The mix of revolvers remain static, while management indicated that the recent hardening of interest rates will exert pressure on funding costs in the coming quarters. This could drive further margin compression over 2HFY24 as the outlook on any increase in the mix of EMI and Revolver loans remains uncertain. Management indicated for a slight rise in stress levels, which will likely keep credit costs elevated over the near term. However, on the positive side, spending growth remains healthy, while the company maintains a healthy traction in new card additions. Reversal in rate cycle and the lagged improvement in revolver mix remain the key triggers. We expect SBICARD to report 35% earnings CAGR over FY24-26E, with a superior RoA/RoE of ~5.6%/~26% by FY26E, while earnings growth for the current fiscal is expected to remain modest. We reiterate our **BUY rating with a TP of INR900 (premised on 22x Sep'25E EPS).**

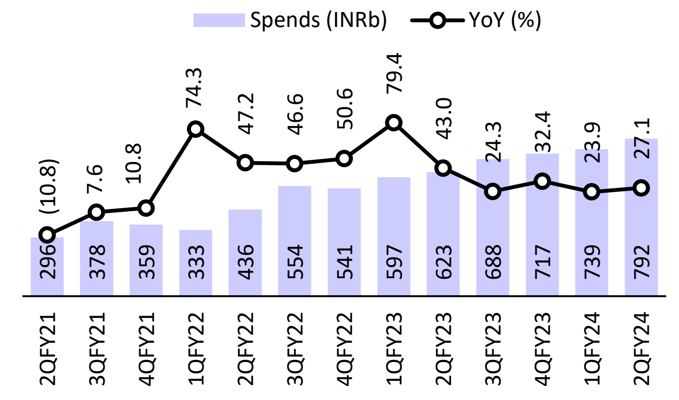
Story in charts

Exhibit 1: Open market channel accounts for ~58% of outstanding cards



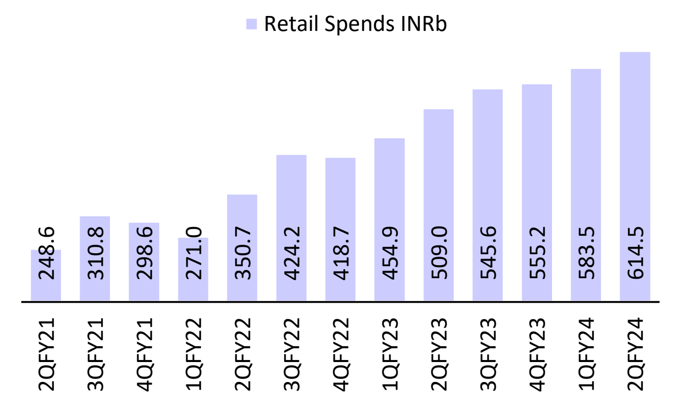
Source: MOFSL, Company

Exhibit 2: Spends remains strong and grew 27% YoY (up 7% QoQ)



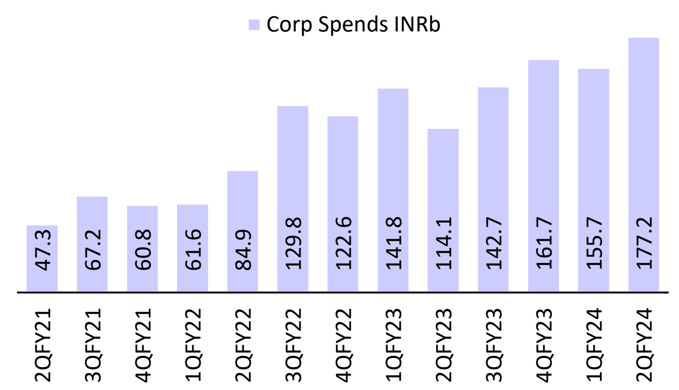
Source: MOFSL, Company

Exhibit 3: Retail spends robust at ~INR614.5b



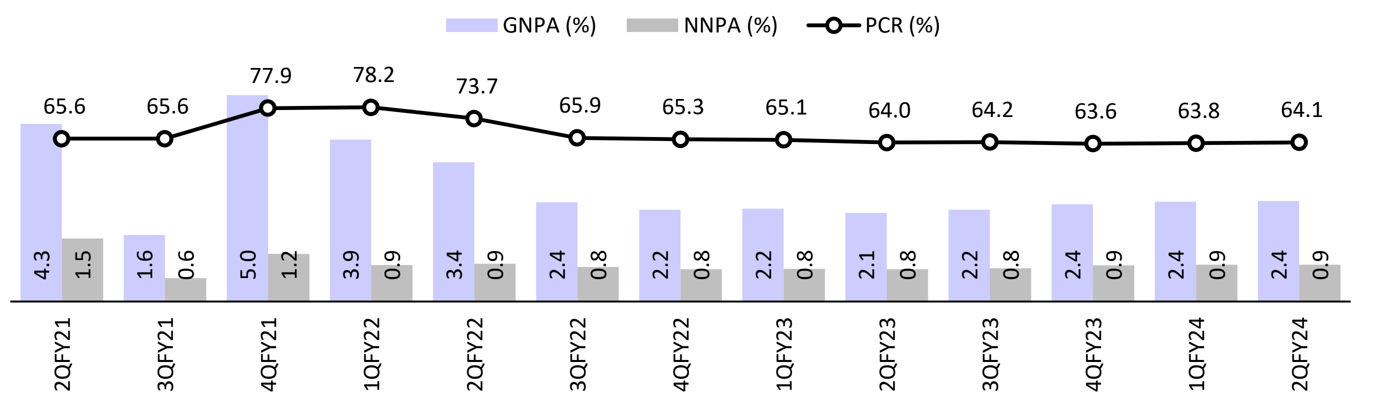
Source: MOFSL, Company, RBI

Exhibit 4: Corporate spends increased to INR177b



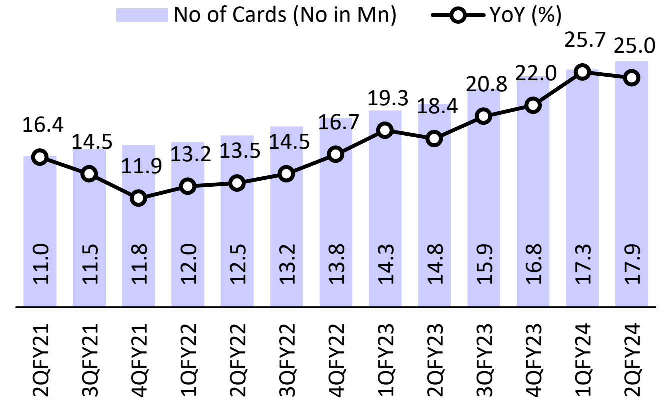
Source: MOFSL, Company, RBI

Exhibit 5: Asset quality ratios broadly stable QoQ at 2.4%/0.9%; PCR improves to ~64%



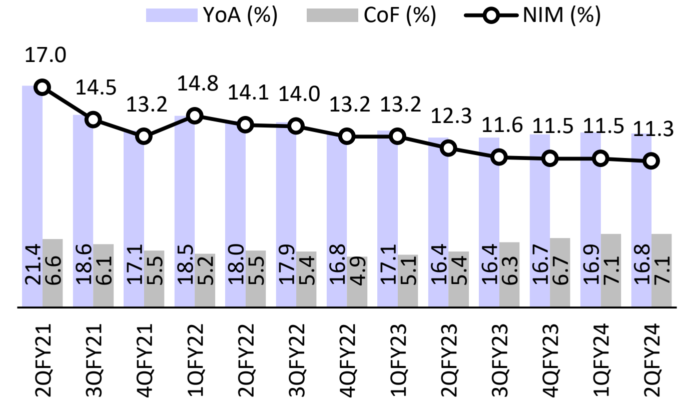
Source: MOFSL, Company

Exhibit 6: No of cards up 25% YoY to 17.9m



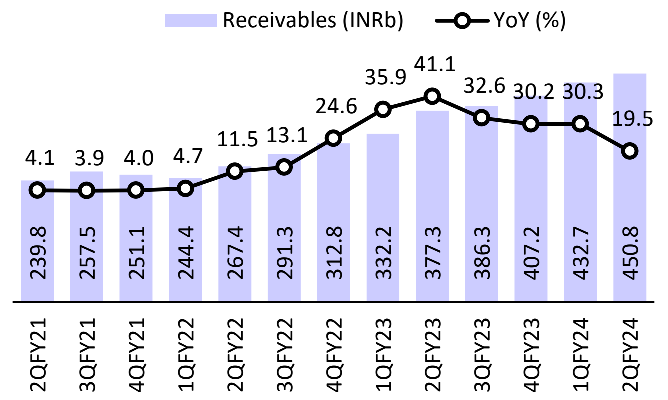
Source: MOFSL, Company

Exhibit 7: NIMs continue to remain under pressure at 11.3%



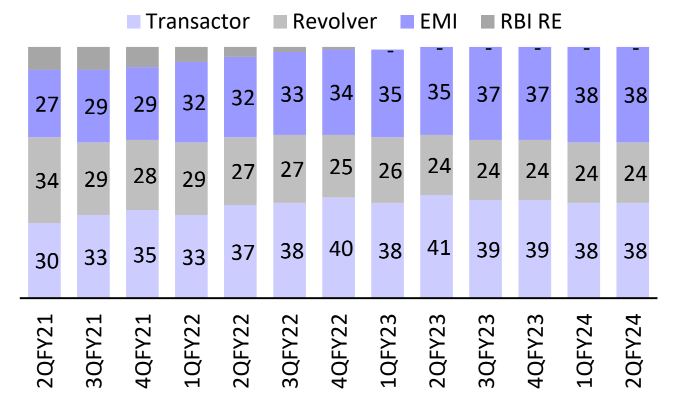
Source: MOFSL, Company

Exhibit 8: Receivables up 20% YoY to ~INR451b



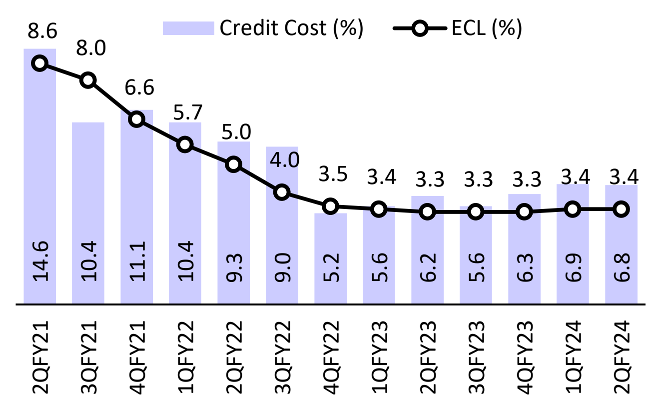
Source: MOFSL, Company

Exhibit 9: Revolver + EMI mix has risen 300bp YoY to 62%



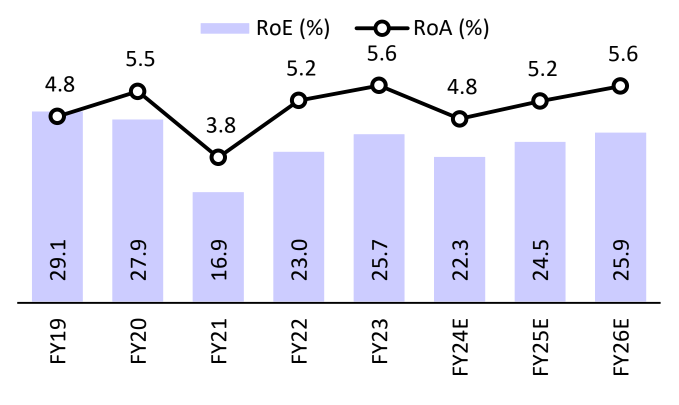
Source: MOFSL, Company

Exhibit 10: Credit cost stood at 6.8%; ECL stable at 3.4%



Source: MOFSL, Company

Exhibit 11: Estimate FY26E RoA/RoE at 5.6%/25.9%



Source: MOFSL, Company

Financials and valuations

Income Statement

(INR m)

Y/E March	FY21	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	49,277	48,212	60,502	79,731	1,01,531	1,28,652
Interest Expense	10,434	10,273	16,476	26,682	32,273	38,892
Net Interest Income	**38,843**	**37,939**	**44,025**	**53,048**	**69,258**	**89,760**
Growth (%)	9.7	-2.3	16.0	20.5	30.6	29.6
Non Interest Income	47,859	64,803	82,353	96,395	1,19,744	1,50,604
Total Income	**86,702**	**1,02,742**	**1,26,379**	**1,49,443**	**1,89,002**	**2,40,364**
Growth (%)	2.6	18.5	23.0	18.3	26.5	27.2
Operating Expenses	47,079	58,462	74,484	87,383	1,08,080	1,36,334
Pre Provision Profits	**39,623**	**44,280**	**51,895**	**62,060**	**80,922**	**1,04,030**
Growth (%)	8.0	11.8	17.2	19.6	30.4	28.6
Provisions (excl tax)	26,386	22,558	21,591	29,411	36,343	44,378
PBT	**13,237**	**21,722**	**30,304**	**32,649**	**44,579**	**59,653**
Tax	3,392	5,560	7,721	8,326	11,368	15,211
Tax Rate (%)	25.6	25.6	25.5	25.5	25.5	25.5
PAT	**9,845**	**16,161**	**22,583**	**24,324**	**33,211**	**44,441**
Growth (%)	-20.9	64.2	39.7	7.7	36.5	33.8
OCI	128	102	(28)	-	-	-
Total Comprehensive Income	**9,974**	**16,263**	**22,555**	**24,324**	**33,211**	**44,441**
Growth (%)	-19.7	63.1	38.7	7.8	36.5	33.8

Balance Sheet

Y/E March	FY21	FY22	FY23	FY24E	FY25E	FY26E
Share Capital	9,405	9,432	9,461	9,461	9,461	9,461
Reserves & Surplus	53,615	68,095	88,840	1,10,797	1,41,169	1,82,772
Net Worth	**63,020**	**77,527**	**98,301**	**1,20,257**	**1,50,630**	**1,92,233**
Borrowings	1,78,948	2,29,825	3,11,096	3,88,870	4,83,366	5,96,956
Other Liabilities & Prov.	28,161	39,133	46,059	56,652	70,816	88,519
Total Liabilities	**2,70,129**	**3,46,484**	**4,55,456**	**5,65,780**	**7,04,811**	**8,77,709**
Current Assets	7,201	11,064	13,545	15,983	19,179	23,015
Investments	**9,576**	**12,972**	**21,397**	**25,676**	**31,839**	**39,798**
Growth (%)	65,347.3	35.5	64.9	20.0	24.0	25.0
Loans	**2,34,591**	**3,01,873**	**3,93,610**	**4,94,768**	**6,20,438**	**7,76,789**
Growth (%)	2.8	28.7	30.4	25.7	25.4	25.2
Fixed Assets	3,182	4,537	5,737	6,023	6,385	6,768
Other Assets	15,579	16,039	21,168	23,330	26,970	31,339
Total Assets	**2,70,129**	**3,46,484**	**4,55,456**	**5,65,780**	**7,04,811**	**8,77,709**

Asset Quality

Y/E March	FY21	FY22	FY23	FY24E	FY25E	FY26E
GNPA (INR m)	12,543	6,934	9,575	12,003	14,254	16,243
NNPA (INR m)	2,776	2,409	3,487	4,040	4,049	4,353
GNPA Ratio	5.0	2.2	2.4	2.4	2.3	2.1
NNPA Ratio	1.1	0.8	0.9	0.8	0.7	0.6
Slippage Ratio	12.8	8.0	6.0	6.3	5.8	5.6
Credit Cost	10.7	8.0	6.0	6.4	6.3	6.1
PCR (Excl Tech. write off)	77.9	65.3	63.6	66.3	71.6	73.2

E: MOFSL Estimates

Financials and valuations

Business Metrics

Y/E March	FY21	FY22	FY23	FY24E	FY25E	FY26E
Total No of Cards (Nos in Mn)	11.8	13.8	16.8	20.5	25.2	31.0
Total spends (INR b)	1,224.2	1,863.5	2,625.0	3,360.0	4,267.2	5,419.3
Spends per card (INR k)	103.5	135.4	156.2	163.9	169.3	174.8
Loans per card (INR)	19,844	21,927	23,429	24,140	24,611	25,051
Loans as % of spends	19.2	16.2	15.0	14.7	14.5	14.3
Fee income earned per card	3,305	3,796	3,931	3,914	4,018	4,105

Ratios

Y/E March	FY21	FY22	FY23	FY24E	FY25E	FY26E
Yield & Cost Ratios (%)						
Avg. Yield on loans	20.0	17.1	16.8	17.4	17.6	17.8
Avg. Cost of Borrowings	5.9	5.0	6.1	7.6	7.4	7.2
Interest Spread	**14.1**	**12.1**	**10.7**	**9.7**	**10.2**	**10.6**
Net Interest Margin	**15.8**	**13.5**	**12.2**	**11.5**	**12.0**	**12.4**
Capitalisation Ratios (%)						
Tier I	20.9	21.0	20.4	19.7	19.4	19.4
Tier II	3.9	2.8	2.7	2.1	1.6	1.2
CAR	24.8	23.8	23.1	21.7	21.0	20.7
Asset-Liability Profile (%)						
Cost/Assets	18.0	19.0	18.6	17.1	17.0	17.2
Cost/Total Income	54.3	56.9	58.9	58.5	57.2	56.7
Int. Expense/Int.Income	21.2	21.3	27.2	33.5	31.8	30.2
Fee Income/Total Income	45.1	50.9	52.3	53.7	53.6	53.0
Non Int. Inc./Total Income	55.2	63.1	65.2	64.5	63.4	62.7
Empl. Cost/Total Expense	10.4	8.1	7.5	7.5	7.4	7.2

Valuation

	FY21	FY22	FY23	FY24E	FY25E	FY26E
RoE	16.9	23.0	25.7	22.3	24.5	25.9
RoA	3.8	5.2	5.6	4.8	5.2	5.6
RoRWA	4.1	5.8	6.2	5.1	5.3	5.5
Book Value (INR)	67	82	104	127	159	203
Growth (%)	17.8	22.7	26.4	22.3	25.3	27.6
Price-BV (x)	**11.3**	**9.2**	**7.3**	**5.9**	**4.7**	**3.7**
Adjusted BV (INR)	65	80	101	124	156	200
Price-ABV (x)	**11.6**	**9.4**	**7.4**	**6.1**	**4.8**	**3.8**
EPS (INR)	10.5	17.2	23.9	25.7	35.1	47.0
Growth (%)	-25.3	63.8	39.3	7.5	36.5	33.8
Price-Earnings (x)	**72.0**	**43.9**	**31.5**	**29.3**	**21.5**	**16.1**

E: MOFSL Estimates

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SELL	< - 10%
NEUTRAL	< - 10 % to 15%
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