

November 09, 2010

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Rating	Accumulate
Price	Rs3,425
Target Price	Rs3,484
Implied Upside	1.7%
Sensex	20,852

(Prices as on November 8, 2010)

#### Trading data

Market Cap. (Rs bn)	2,175.0
Shares o/s (m)	635.0
3M Avg. Daily value (Rs m)	7056.3

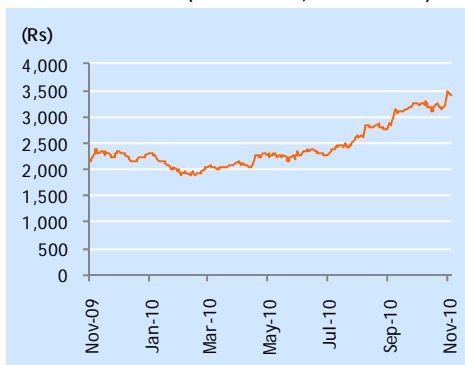
#### Major shareholders

Promoters	59.40%
Foreign	13.99%
Domestic Inst.	15.54%
Public & Other	11.07%

#### Stock Performance

(%)	1M	6M	12M
Absolute	5.5	53.9	55.3
Relative	2.5	29.5	26.3

Price Performance (RIC: SBI.BO, BB: SBIN IN)



Source: Bloomberg

## State Bank of India

### Healthy operating performance; asset quality woes continue

- Strong core performance, asset quality surprises negatively:** State Bank of India (SBI) reported net profit of Rs25.0bn, up 0.5% YoY, but down 14.2% QoQ, significantly lower than our as well as street estimates. The financials include the impact of amalgamation of State Bank of Indore (SBIIn) (3.4% of SBI's assets as on Mar'10) with effect from August 26, 2010 and hence are not strictly comparable. Key positives were 1) Robust 44.7% YoY and 11.1% QoQ NII growth driven by healthy 19.0% YoY increase in net advances coupled with a smart 25bps QoQ improvement in the net interest margin to 3.43% 2) Growth in CASA deposits (27.7% YoY) outpacing the overall deposits growth (10.7% YoY) resulting in 28bps QoQ improvement in CASA ratio to 47.8%, which is impressive 3) Core fee income grew very strongly by 40% YoY and 22% QoQ (however, treasury gains remained subdued). Adjusting for SBIIn amalgamation, advances and deposits grew by 15.2% and 7.2% YoY respectively. The key negatives were continued high slippages at Rs44.1bn (or ~3.1% annualized) for SBI portfolio and Rs8.5bn worth slippages of the SBIIn portfolio. Higher loan loss provisions (up 24.8% QoQ) to meet the RBI guideline of 70% provision cover (currently at 62.8%) affected bottom-line. Staff expenses include Rs3bn towards gratuity provision along with Rs1.8bn write back of excess provisions made earlier towards wage arrears. Consolidated PAT declined by 22.5% YoY and 29.8% QoQ to Rs23.6bn, despite associate banks reporting Rs8.1bn PAT on account of various provisions related to SBIIn.
- Slippages remain high; outlook uncertain:** Gross slippages in Q2FY11 increased to Rs44.1bn on account of slippages from agri sector (Rs2.1bn), exposure towards Dubai World (Rs2.5bn) and from restructured portfolio (Rs6.6bn). Cumulative slippages from the restructured portfolio now stand at 14.5% and management expects it to go up to 17-18%. Though slippages are likely to continue, management foresees higher recovery and upgradations in H2, which could likely have lower impact on earnings.
- Valuations and outlook:** SBI has performed well on the core operating front. However, continued high level of slippages remains a cause of concern and overshadow an otherwise strong operating performance. We believe continued slippages and the stipulation to meet the 70% provision cover guideline could likely keep bottom-line under pressure. We have revised our FY11E estimates downwards by ~4% to factor in higher provisions on teaser loans. Though asset quality issues may act as an overhang on the stock in the near term, we maintain our 'Accumulate' rating on the stock with a revised one-yr fwd SOTP price target of Rs3,484 (avg. of FY12 and FY13 SOTP values).

Key financials ( Y/e March)	2009	2010	2011E	2012E
Net interest income (Rs m)	208,731	236,714	305,429	374,267
Growth (%)	22.6	13.4	29.0	22.5
Operating profit (Rs m)	179,152	183,209	249,585	326,030
PAT (Rs m)	91,212	91,672	111,365	158,959
EPS (Rs)	143.7	144.4	154.2	220.1
Growth (%)	34.8	0.5	6.8	42.7
Net DPS (Rs)	29.0	30.0	31.0	32.0

Source: Company Data; PL Research

Profitability & Valuation	2009	2010	2011E	2012E
NIM (%)**	2.5	2.3	2.7	2.8
RoAE (%)	17.1	14.8	13.9	15.7
RoAA (%)	1.1	0.9	1.0	1.2
P / BV (x)*	3.7	3.1	2.4	2.1
P / ABV (x)*	4.1	3.5	2.5	2.1
PE (x)*	21.4	20.6	19.0	13.0
Net dividend yield (%)	0.8	0.9	0.9	0.9

Source: Company Data; PL Research \*\*Calculated on average assets \*Refer Page 5

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**Q2FY11 Result Overview (Rs m)**

Y/e March	Q2FY11	Q2FY10	YoY gr. (%)	Q1FY11	H1FY11	H1FY10	YoY gr. (%)
Interest Income	198,081	177,759	11.4	184,521	382,602	352,486	8.5
Interest Expense	116,932	121,671	(3.9)	111,484	228,416	246,149	(7.2)
<b>Net Interest Income</b>	<b>81,149</b>	<b>56,088</b>	<b>44.7</b>	<b>73,037</b>	<b>154,186</b>	<b>106,337</b>	<b>45.0</b>
Non-Interest Income	40,052	35,252	13.6	36,900	76,952	70,939	8.5
Treasury Income	1,973	5,454	(63.8)	1,734	3,707	12,542	(70.4)
CEB	29,450	21,030	40.0	24,096	53,546	39,650	35.0
Forex Income	3,087	5,237	(41.1)	5,025	8,112	9,941	(18.4)
Other Income	5,542	3,531	57.0	6,044	11,586	8,806	31.6
<b>Net total Income</b>	<b>121,201</b>	<b>91,340</b>	<b>32.7</b>	<b>109,937</b>	<b>231,138</b>	<b>177,276</b>	<b>30.4</b>
Operating Expenses	57,631	42,990	34.1	48,593	106,224	92,187	15.2
Employee	36,758	26,341	39.5	30,739	67,497	60,454	11.6
Other operating expenses	20,873	16,648	25.4	17,854	38,727	31,733	22.0
<b>Operating profit</b>	<b>63,570</b>	<b>48,350</b>	<b>31.5</b>	<b>61,344</b>	<b>124,914</b>	<b>85,089</b>	<b>46.8</b>
Core operating profits	56,055	39,366	42.4	53,565	109,620	63,741	72.0
Provisions	26,215	10,161	158.0	15,514	41,728	11,888	251.0
Loan loss provisions	21,625	11,023	96.2	17,334	38,959	24,465	59.2
Other provisions	4,590	(862)	—	(1,820)	2,770	(12,577)	—
<b>Profit before tax</b>	<b>37,355</b>	<b>38,189</b>	<b>(2.2)</b>	<b>45,830</b>	<b>83,185</b>	<b>73,201</b>	<b>13.6</b>
Tax	12,342	13,289	(7.1)	16,688	29,030	24,997	16.1
<b>Net Profit after tax</b>	<b>25,014</b>	<b>24,900</b>	<b>0.5</b>	<b>29,142</b>	<b>54,156</b>	<b>48,204</b>	<b>12.3</b>
<b>Asset Quality</b>							
Gross NPA's	232,046	173,758	33.5	208,252	232,046	173,758	33.5
<i>Gross NPA's (%)</i>	<i>3.4</i>	<i>3.0</i>		<i>3.1</i>	<i>3.4</i>	<i>3.0</i>	
Net NPA's	116,012	99,273	16.9	110,744	116,012	99,273	16.9
<i>Net NPA's (%)</i>	<i>1.7</i>	<i>1.7</i>		<i>1.7</i>	<i>1.7</i>	<i>1.7</i>	
Coverage	50.0	42.9		46.8	50.0	42.9	
<b>Capital Adequacy (%)</b>							
<i>CAR</i>	<i>13.2</i>	<i>14.1</i>		<i>13.5</i>	<i>13.2</i>	<i>14.1</i>	
<i>Tier 1</i>	<i>9.6</i>	<i>9.8</i>		<i>9.8</i>	<i>9.6</i>	<i>9.8</i>	
<i>NIM – Reported (%)</i>	<i>3.4</i>	<i>2.6</i>		<i>3.2</i>	<i>3.3</i>	<i>2.4</i>	
<i>NIM – Calculated (%)</i>	<i>3.0</i>	<i>2.3</i>		<i>2.7</i>	<i>2.8</i>	<i>2.2</i>	
<b>Balance Sheet Items</b>							
Deposits	8,553,450	7,729,040	10.7	8,152,970	8,553,450	7,729,040	10.7
CASA	3,771,400	2,952,480	27.7	3,556,392	3,771,400	2,952,480	27.7
<i>CASA Ratio (%)</i>	<i>47.8</i>	<i>41.0</i>		<i>47.5</i>	<i>47.8</i>	<i>41.0</i>	
Advances	6,807,490	5,722,140	19.0	6,532,200	6,807,490	5,722,140	19.0

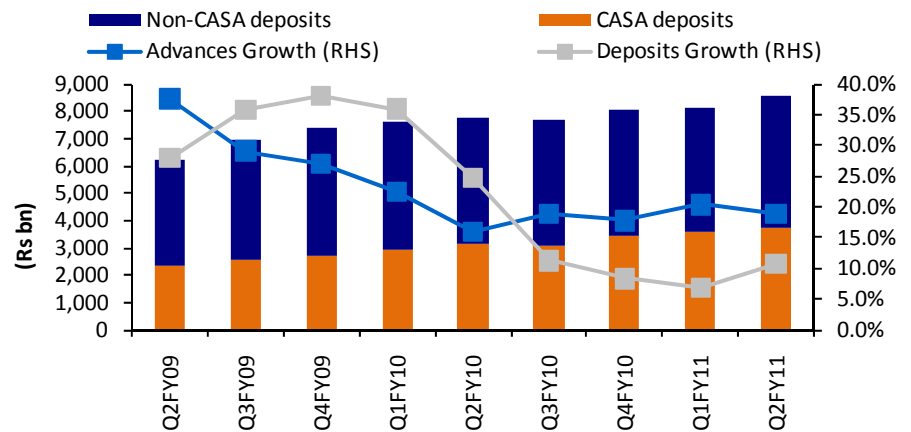
Source: Company Data, PL Research

Net advances grew by 19.0% YoY and 4.2%

QoQ. SBI's market share in advances increased by 46bps YoY and 48bps QoQ to 17.03% in Q2FY11. Deposits grew by 10.7% YoY and 4.9% QoQ. However, excluding SBI's advances and deposits, the advances and deposits growth stood at 15.2% and 7.2% YoY, respectively.

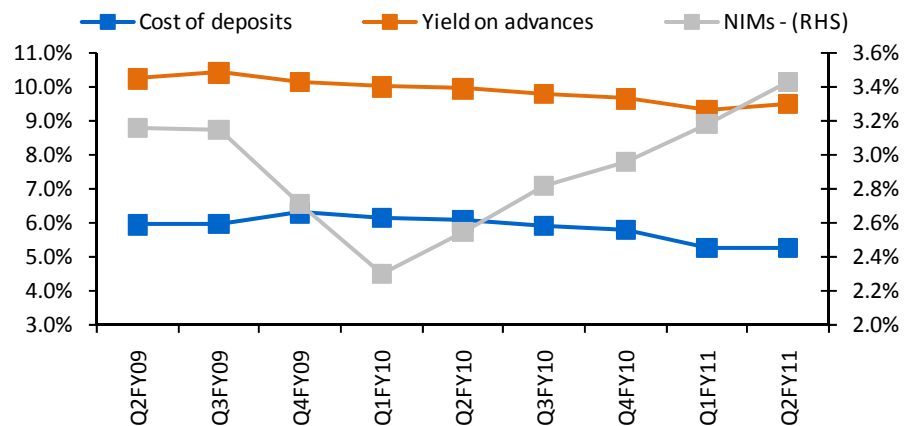
Importantly, CASA deposits grew much faster by 27.7% YoY and 6.0% QoQ, leading to 28bps QoQ improvement in CASA ratio to 47.8%.

### Trend in business growth



Source: Company Data, PL Research

### Trend in net interest margins

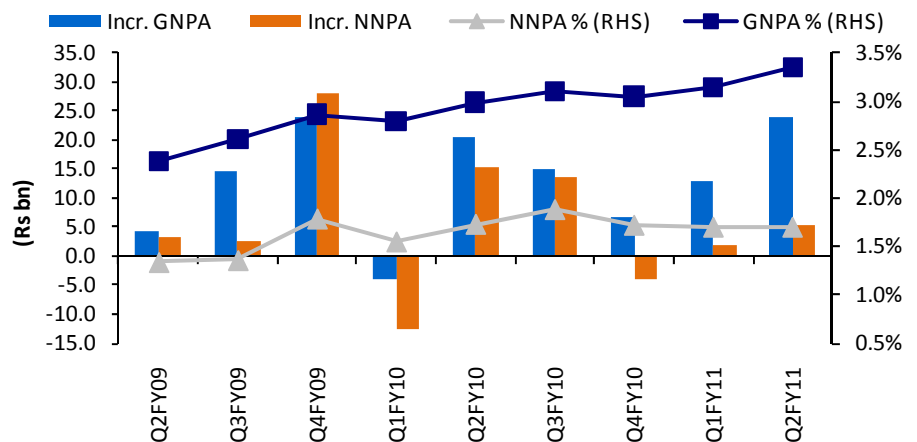


Source: Company Data, PL Research

NIM continued to improve for the fifth consecutive quarter as it increased by 25bps QoQ to 3.43%.

Improvement in margins could be explained through 20bps QoQ improvement in yields on advances due to the PLR hike effected during the quarter, which the cost of deposits declined by 2bps QoQ on account of re-pricing of high cost deposits and improvement in CASA ratio.

### Trend in Q-o-Q change in NPAs



Source: Company Data, PL Research

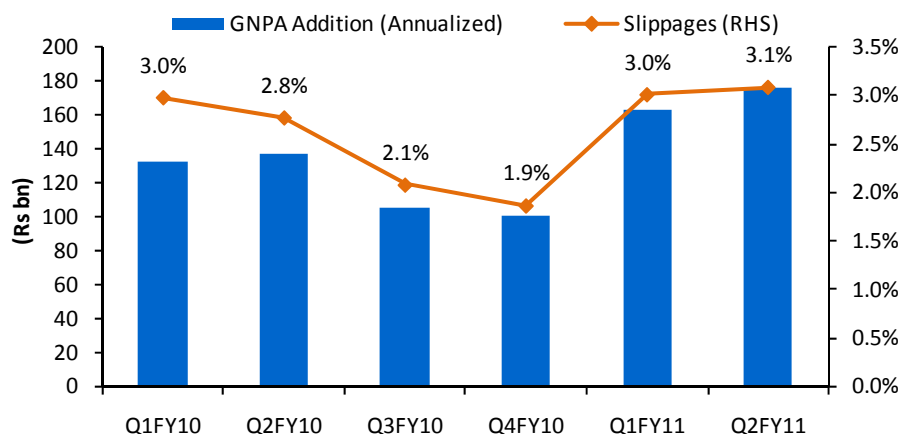
GNPAs increased by 11.4% QoQ, continuing the trend of sequential increase for the fifth consecutive quarter albeit at faster pace this quarter on the back of higher slippages from the agri and restructured portfolio.

Provision coverage improved to 50.0% and including technically written-off accounts, it stood at 62.8% v/s 60.7% in the previous quarter.

Gross slippages during the quarter increased sharply to Rs44.1bn v/s Rs40.8bn last quarter mainly on account of significant slippages from the agri segment (Rs2.1bn), exposure towards Dubai World (Rs2.5bn) and from restructured portfolio (Rs6.6bn), taking the overall slippages from the restructured portfolio to 14.5%.

Moreover, Rs8.5bn worth slippages were contributed from the SBI portfolio, including which the annualized slippages stood even higher at 3.6%.

#### Trend in slippages based on previous years' closing advances



Source: PL Research, Company Data

Provision cover improved to 50.0% on account of excess provisions made during the quarter. Including technically written off accounts, the coverage ratio improves to 62.8% v/s 60.7% in Q1FY11 (Rs bn)

Period	31.03.2010			30.06.2010			30.09.2010		
	NPAs	Provision	%	NPAs	Provision	%	NPAs	Provision	%
Substandard	8,066	1,251	15.5%	8,542	1,358	15.9%	9,869	1,359	13.8%
Doubtful	8,672	4,617	53.2%	9,649	5,759	59.7%	10,182	6,641	65.2%
Loss	2,797	2,797	100.0%	2,634	2,634	100.0%	3,154	3,154	100.0%
<b>Whole Bank</b>	<b>19,535</b>	<b>8,665</b>	<b>44.4%</b>	<b>20,825</b>	<b>9,751</b>	<b>46.8%</b>	<b>23,205</b>	<b>^11,603</b>	<b>50.0%</b>

Source: Company Data, PL Research

^Includes excess provision to the tune of Rs4.5bn to meet the 70% provision cover

Fresh slippages stood elevated on the back of higher slippages from the agri, corporate and restructured portfolio (Rs bn)

Movement in NPAs	Q1FY11	Q2FY11	Segmental contribution to net increase in NPA	Q1FY11	Q2FY11
Opening GNPA	195.4	208.3	Corporate	1.0	13.9
Fresh Slippages	40.8	*52.7	International	(0.4)	3.0
Upgradation + Recoveries	21.6	20.9	SME	1.8	2.0
Write-offs	6.3	8.0	Agriculture	6.8	4.6
<b>Closing NPAs</b>	<b>208.3</b>	<b>232.1</b>	Retail	3.7	0.4

Source: Company Data, PL Research

\*Includes slippages worth Rs8.5bn from the SBI portfolio

**Reconciliation between expected and reported reserves****(Rs bn)**

Particulars	Standalone	Consolidated
Reserves as on March 2010	653.1	825.0
Add: H1FY11 PAT	54.2	57.3
	707.3	882.3
Add: SBI In Reserves (as on Jun'10) #	18.4	-
<b>Total Reserves</b>	<b>725.7</b>	<b>882.3</b>
Reported Reserves	716.0	882.6
<b>Difference in reserves</b>	<b>(9.7)</b>	<b>0.3</b>

We have tried to reconcile the difference between the reported standalone and consolidated PAT (loss of Rs1.4bn) despite associate banks reporting PAT of Rs8.1bn.

However, the difference in the standalone and consolidated PAT could be explained by various provisions (~Rs6-6.5bn towards pension and other provisions including loan loss provisions) pertaining to SBI In being adjusted against reserves.

Source: Company Data, PL Research

# Includes reserves as on March 2010 and reported PAT for quarter ended June 2010

**Reconciliation between standalone and consolidated PAT****(Rs bn)**

Particulars	Q2FY11
Consolidated PAT	23.6
SA PAT	25.0
Difference	(1.4)
Reported PAT for Associate Banks	8.1
<b>Implied difference</b>	<b>(9.4)</b>

Source: Company Data, PL Research

**SOTP Valuation**

Business	Basis	Multiple	Value/Share (FY12E)	% of SOTP	Multiple	Value/Share (FY13E)	% of SOTP
Standalone Core Banking	x ABV**	1.9	2,663	82.6%	1.9	3,081	82.3%
SBI (associate banks)	x ABV	1.3	310	9.6%	1.3	356	9.5%
SBI life	Appraisal Value	-	176	5.5%	-	218	5.8%
SBI Mutual Fund	% of AUM	5.0%	15	0.5%	5.0%	16	0.4%
SBI Capital Market	x PAT	12.0	25	0.8%	12.0	32	0.8%
Other investments	(UTI MF, NSE etc.)	-	36	1.1%	-	39	1.1%
<b>Total</b>			<b>3,225</b>	<b>100.0%</b>		<b>3,742</b>	<b>100.0%</b>

Source: Company Data, PL Research

\*\* Rs106 and Rs128 per share reduced for investment in subsidiaries from Book Value & Rs562 & Rs661 per share reduced from the CMP for value of subsidiary for FY12 and FY13 respectively. We have also applied a 15% holding company discount.



**Income Statement (Rs m)**

Y/e March	2009	2010	2011E	2012E
Int. Earned from Adv.	464,047	506,326	582,345	739,628
Int. Earned from Invt.	155,741	177,363	200,202	229,869
Others	18,096	26,250	17,143	25,737
Total Interest Income	637,884	709,939	799,690	995,235
Interest expense	429,153	473,225	494,261	620,968
<b>NII</b>	<b>208,731</b>	<b>236,714</b>	<b>305,429</b>	<b>374,267</b>
Growth (%)	22.6	13.4	29.0	22.5
Treasury Income	25,667	21,168	7,500	9,000
NTNII	101,241	128,514	157,600	194,405
Non Interest Income	126,908	149,682	165,100	203,405
Total Income	764,792	859,621	964,790	1,198,640
Growth (%)	32.7	12.4	12.2	24.2
Operating Expense	156,487	203,187	220,945	251,642
<b>Operating Profit</b>	<b>179,152</b>	<b>183,209</b>	<b>249,585</b>	<b>326,030</b>
Growth (%)	36.7	2.3	36.2	30.6
NPA Provisions	24,750	46,223	74,656	76,933
Investment Provisions	7,072	(9,880)	461	1,560
Total Provisions	37,356	43,948	83,369	88,778
<b>PBT</b>	<b>141,797</b>	<b>139,261</b>	<b>166,216</b>	<b>237,252</b>
Tax Provisions	50,584	47,589	54,851	78,293
Effective Tax Rate (%)	35.7	34.2	33.0	33.0
<b>PAT</b>	<b>91,212</b>	<b>91,672</b>	<b>111,365</b>	<b>158,959</b>
Growth (%)	35.5	0.5	21.5	42.7

**Balance Sheet (Rs m)**

Y/e March	2009	2010	2011E	2012E
Par Value	10	10	10	10
No. of equity shares	635	635	722	722
Equity	6,349	6,350	7,221	7,221
Networth	579,477	659,493	945,693	1,078,675
Adj. Networth	482,703	550,792	870,530	1,006,717
Deposits	7,420,731	8,041,162	9,006,102	10,807,322
Growth (%)	38.1	8.4	12.0	20.0
Low Cost deposits	3,089,779	3,800,397	4,142,807	4,863,295
% of total deposits	41.6	47.3	46.0	45.0
<b>Total Liabilities</b>	<b>9,650,430</b>	<b>10,539,564</b>	<b>12,180,069</b>	<b>14,629,661</b>
Net Advances	5,425,032	6,319,141	7,669,514	9,426,457
Growth (%)	30.2	16.5	21.4	22.9
Investments	2,759,540	2,857,901	2,881,953	3,242,197
<b>Total Assets</b>	<b>9,650,430</b>	<b>10,539,564</b>	<b>12,180,069</b>	<b>14,629,661</b>

Source: Company Data, PL Research.

**Quarterly Financials (Rs m)**

Y/e March	Q3FY10	Q4FY10	Q1FY11	Q2FY11
Interest Income	177,797	179,656	184,521	198,081
Interest Expense	114,634	112,442	111,484	116,932
<b>Net Interest Income</b>	<b>63,163</b>	<b>67,214</b>	<b>73,037</b>	<b>81,149</b>
Non Interest Income	33,657	45,085	36,900	40,052
CEB	21,900	34,858	24,096	29,450
Treasury	4,370	4,256	1,734	1,973
<b>Net Total Income</b>	<b>96,820</b>	<b>112,300</b>	<b>109,937</b>	<b>121,201</b>
Operating Expenses	50,639	60,361	48,593	57,631
Employee Expenses	31,175	35,918	30,739	36,758
Other Expenses	19,464	24,443	17,854	20,873
<b>Operating Profit</b>	<b>46,182</b>	<b>51,939</b>	<b>61,344</b>	<b>63,570</b>
Core Operating Profit	41,811	47,683	59,610	61,597
Provisions	8,566	23,494	15,514	26,215
Loan loss provisions	4,437	21,868	17,334	21,625
Investment Depreciation	2,460	356	(2,983)	4,318
<b>Profit before tax</b>	<b>37,615</b>	<b>28,445</b>	<b>45,830</b>	<b>37,355</b>
Tax	12,825	9,779	16,688	12,342
<b>PAT before EO</b>	<b>24,791</b>	<b>18,666</b>	<b>29,142</b>	<b>25,014</b>
Extraordinary item	—	—	—	—
<b>PAT</b>	<b>24,791</b>	<b>18,666</b>	<b>29,142</b>	<b>25,014</b>

**Key Ratios**

Y/e March	2009	2010	2011E	2012E
CMP (Rs)	3,425	3,425	3,425	3,425
Equity Shrs. Os. (m)	635	635	722	722
Market Cap (Rs m)	2,174,970	2,174,970	2,174,970	2,174,970
M/Cap to AUM (%)	22.5	20.6	17.9	14.9
EPS (Rs)	143.7	144.4	154.2	220.1
Book Value (Rs)	913	1,039	1,310	1,494
Adj. BV (75%) (Rs)	822	944	1,280	1,477
P/E (x)	21.4	20.6	19.0	13.0
P/BV (x)	3.7	3.1	2.4	2.1
P/ABV (x)	4.1	3.5	2.5	2.1
DPS (Rs)	29.0	30.0	31.0	32.0
Dividend Yield (%)	0.8	0.9	0.9	0.9

**Profitability (%)**

Y/e March	2009	2010	2011E	2012E
NIM	2.5	2.3	2.7	2.8
RoAA	1.1	0.9	1.0	1.2
RoAE	17.1	14.8	13.9	15.7

**Efficiency**

Y/e March	2009	2010	2011E	2012E
Cost-Income Ratio (%)	46.6	52.6	47.0	43.6
C-D Ratio (%)	73.1	78.6	85.2	87.2
Business per Emp. (Rs m)	63	72	72	80
Profit per Emp. (Rs m)	4	5	5	6
Business per Branch (Rs m)	1,117	1,149	1,283	1,445
Profit per Branch (Rs m)	8	7	9	11

**Asset Quality**

Y/e March	2009	2010	2011E	2012E
Gross NPAs (Rs m)	157,140	195,349	214,750	239,859
Net NPAs (Rs m)	96,774	108,702	75,163	71,958
Gr. NPAs to Gross Adv. (%)	2.9	3.0	2.8	2.5
Net NPAs to Net Adv. (%)	1.8	1.7	1.0	0.8
NPA Coverage (%)	38.4	44.4	65.0	70.0

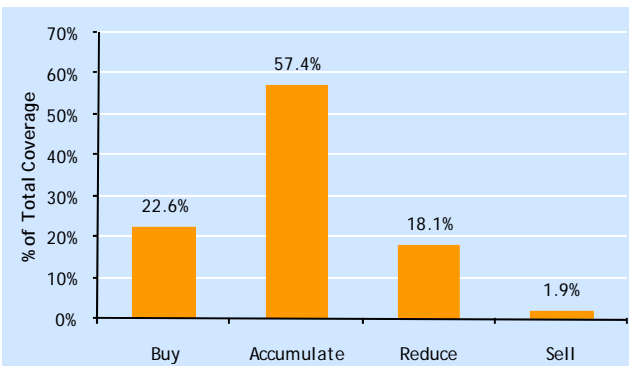
Source: Company Data, PL Research.

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#### Rating Distribution of Research Coverage



#### PL's Recommendation Nomenclature

<b>BUY</b>	: Over 15% Outperformance to Sensex over 12-months	<b>Accumulate</b>	: Outperformance to Sensex over 12-months
<b>Reduce</b>	: Underperformance to Sensex over 12-months	<b>Sell</b>	: Over 15% underperformance to Sensex over 12-months
<b>Trading Buy</b>	: Over 10% absolute upside in 1-month	<b>Trading Sell</b>	: Over 10% absolute decline in 1-month
<b>Not Rated (NR)</b>	: No specific call on the stock	<b>Under Review (UR)</b>	: Rating likely to change shortly

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