AMBIT
Acumen at work

SBI Cards

NOT RATED

PRE-IPO NOTE | **December 26, 2019**

Sound fundamentals, Challenging macros

Low penetration in SBI customer base plus strong distribution means SBI Cards' card base can grow at ~23% CAGR over FY19-24. Increased focus on EMI products can lead to loan book growing at even faster pace at ~46% CAGR during this period. However, growth in fee income could fall given stagnating per card spends, market-share loss to UPI and potential regulatory cap on MDR charges. Whilst asset quality has held up till now, a slowing economy and job growth can lead to increase in NPAs, in line with global experience. Expected valuations at ~12x FY20E post money P/B is at ~243% premium to Amex/Discovery and ~83% premium to some high growth and/or high RoE Indian lenders. High growth and higher RoE justify a premium, but lack of optionality to diversify in other businesses mean that premium should be limited.

Competitive position: POSITIVE Changes to this position: POSITIVE

High growth potential

SBI Cards' outstanding card base has grown at a CAGR of 28% over FY15-1HFY20 (vs industry CAGR of 22%) with market share of ~18% at Sep'19. With low credit card penetration in SBI customers (credit card to debit card ratio of 3% vs ~31% for the private sector banks), strong brand name and distribution, SBI Cards has potential to grow its card base at ~23% CAGR over the next 5 years leading to market share of ~22.5% by FY24.

Interest income a big driver but fee income could be a drag

Interest earning loan book has the potential to grow at 46% CAGR (vs 21% CAGR in cards), if the loan book/trailing 3-month spends ratio of SBI Cards converges towards market leader HDFC Bank (67%/104% for SBI Cards/HDFCB at 1HFY20). However, stagnating per card spends (since FY18 at ₹10-11k), UPI payments gaining share at expense of cards (53% market share in 1HFY20 from only 1% in FY17) and any regulatory cap on MDR/Interchange fee (as proposed by a RBI committee) could slow fee income growth.

Stable asset quality but will it sustain? US is a good case study of risks

SBI Cards' gross NPA ratio and credit cost remained in narrow range of 2.3%-2.8% and 3.2%-3.7%, respectively over FY17-1HFY20. However, asset quality could come under risk amidst weak GDP/job growth in India. A study of US credit card industry suggests **(i)** credit costs increased 5x from the bottom and were as high as 11% during times of weak GDP, and **(ii)** delinquencies levels for <30 year population is 2X times of the >30 year in USA; latter becomes pertinent as incremental growth (35% in FY19) for SBI Cards was from younger population (<30 years) and tier-3/4 towns.

Premium for growth but no optionality value should cap valuations

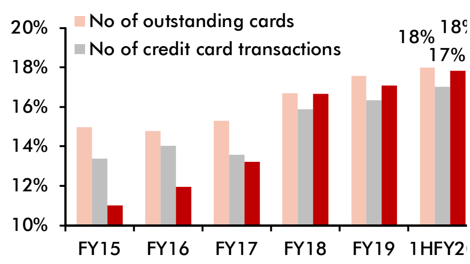
Expected valuations of ~12x FY20E P/B is 243% premium to US credit card companies, Amex/Discovery, despite RoE being similar. However, higher earnings growth of ~41% for SBI Cards vs ~16-19% for Amex/Discovery should command a higher premium over US card companies. Expected valuations are also at ~83% premium to average valuation of high growth and/or high RoE lenders like HDFC Bank, Bajaj Finance, Bandhan Bank, AU Finance and Aavas Financiers. However, unlike these other lenders, SBI Cards is a mono-line business with no optionality to get into other businesses given parent SBI's presence in other businesses. This lack of optionality mean that the company is exposed to vagaries of credit card business compared to other lenders and hence should also be a factor determining valuations.

IPO/OFS Snapshot

Particulars	₹ mn
Pre-money	
Expected valuation	650,000
Networth (1HFY20)	43,814
Net profit (TTM)	12,120
No of shares (#mn)	932
BVPS (1HFY20)	47.0
PB (Trailing, 1HFY20)	14.8
PE (TTM)	53.6
Offer details	
Stake offload in OFS (%)	14%
Amount offload in OFS	91,000
IPO Issue size	5,000
Expected issue price (₹/sh)	697
Post-money	
BVPS (FY20E)	59.7
Net Profit (FY20E)	14,518
PB (FY20E)	11.7
PE (FY20E)	45.1

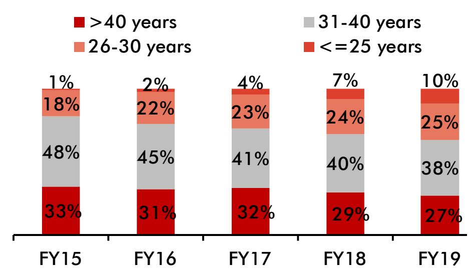
Source: Company, Ambit Capital Research

SBI Cards – Growing market share



Source: RBI, Company, Ambit Capital research

Industry - Increasing originations among millennials (persons below 30 years)



Source: Company, Ambit Capital research

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A fast growing, higher RoE business

SBI Cards was incorporated in 1998 as a result of JV between SBI ("Promoter") and GE Capital. In 2017, GE Capital exited the business and the stake was acquired by Carlyle group (26% stake) and SBI (74% stake). SBI Cards is the second largest credit card issuer in India (18% market share) with its market share increasing across parameters (No. of cards/transactions, value of transactions, etc.). The company's PAT CAGR of 65% over FY17-1HFY20 with RoE expanding to ~37% in 1HFY20. The distribution strength of parent, because of its customer base and branch network is the main strength of the company. Tapping onto favourable demographic dividend, Tier-II/III/smaller cities provides ample opportunities in this sector. The proposed IPO consists of fresh issuance to raise ₹5bn and offer for sale of ~14% stake of existing holders. The media reports suggest pre-money valuation of ₹650bn for the company which translates into 15X Sep'19 networth and 54X TTM earnings. Our back-of-the-envelope calculations show post money 12X FY20 BVPS and 45X FY20E earnings.

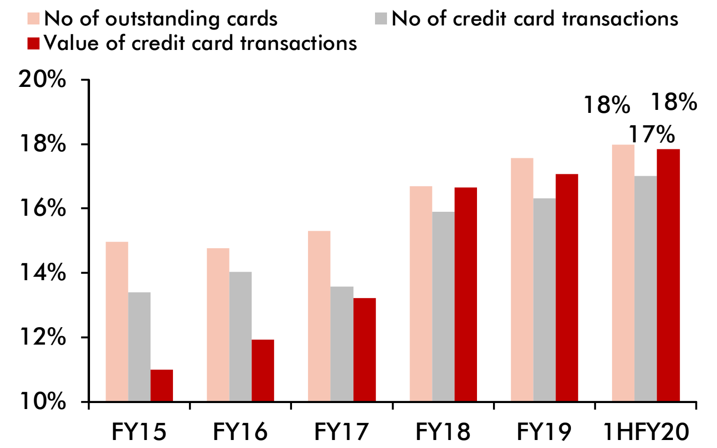
SBI Cards and Payment Services Limited ("SBI Cards") is the second largest credit card issuer in India as on September 2019 with **18% market share** in outstanding cards. Incorporated since 1998, SBI Cards is a "Non-Deposit accepting Systemically Important Non-Banking Financial Company (NBFC-ND-SI)".

State Bank of India (SBI) owns 74% in the company and the rest (26%) is owned by CA Rover (controlled by the Carlyle Group). Prior to December 2017, SBI had 60% stake with GE Capital, owning remaining 40%. In December 2017, GE Capital completely exited from the company. Post this event, the SBI increased its stake to 74%, while CA Rover bought the remaining 26% stake.

The 2nd biggest and a fast growing company

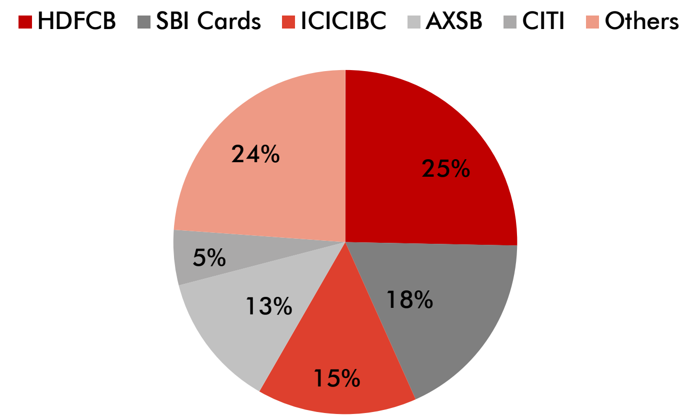
SBI Cards had 18% market share in number of outstanding credit cards at Sep'19 and 17%/18% share number of credit card transactions/value of credit card transactions in 1HFY20. Market share of SBI in most of these parameters have increased over the years. SBI is the second biggest credit card issuer in India after HDFC Bank.

Exhibit 1: SBI Cards – Growing market share across parameters



Source: RBI, Company, Ambit Capital research

Exhibit 2: Top-5 players in credit card industry have 76% market share (1HFY20)



Source: RBI, Company, Ambit Capital research

Exhibit 3: Market share in Credit cards as of 1HFY20 – Second largest player across major parameters

1HFY20	No of Outstanding credit cards	No of transactions-ATM	No of transactions-POS	ATM – withdrawals (value)	POS Spends (value)
HDFCB	25%	23%	26%	27%	28%
SBI Cards	**18%**	**16%**	**17%**	**14%**	**18%**
ICICIBC	15%	6%	15%	5%	11%
AXSB	13%	10%	10%	10%	11%
RBK	4%	13%	4%	9%	4%
KMB	4%	5%	3%	5%	3%
IIB	2%	2%	2%	2%	4%
YES	1%	1%	1%	1%	1%

Source: RBI, Ambit Capital research

Robust growth with increasing RoE

Over FY17-1HFY20, SBI Cards' PAT CAGR was 65% driven by 38% CAGR in balance sheet during this period and RoA expanding from 4.0% in FY17 to 6.5% in 1HFY20. The key drivers of RoA expansion between FY17 and 1HFY20 have been **(i)** improvement in operational efficiency with cost-to-asset ratio decreasing from 22.2% in FY18 to 20.5%; and **(ii)** fee income increasing from 19.7 of average assets in FY18 to 22.1% in 1HFY20.

Exhibit 4: Financial Snapshot – SBI Cards

All in ₹ mn except growth	FY17	FY18	FY19	1HFY20	FY18	FY19	1HFY20
Income Statement						YoY growth (%)	
Net Interest Income	**13,597**	**20,485**	**25,585**	**15,902**	**51%**	**25%**	**29%**
Non-Interest Income	15,829	26,102	37,111	24,656	65%	42%	50%
Net Income							
Opex	18,390	29,393	37,903	22,955	60%	29%	29%
Operating Profit	**11,036**	**17,194**	**24,793**	**17,604**	**56%**	**44%**	**60%**
Provisions and write-offs	5,320	8,001	11,477	7,258	50%	43%	39%
PBT	**5,716**	**9,193**	**13,316**	**10,346**	**61%**	**45%**	**78%**
Taxes	1,988	3,182	4,689	3,087	60%	47%	52%
PAT	**3,729**	**6,011**	**8,627**	**7,259**	**61%**	**44%**	**93%**
Balance sheet							
Networth	14,488	23,531	35,817	43,099	62%	52%	35%
Borrowings (Incl. Debt securities)	77,295	104,148	124,537	161,810	35%	20%	45%
Advances	99,829	140,455	179,087	222,795	41%	28%	42%
Total assets	**107,650**	**156,860**	**202,396**	**244,591**	**46%**	**29%**	**39%**
Du Pont analysis							
Interest Income		20.9%	19.9%	19.8%			
Interest Expenses		5.4%	5.7%	5.6%			
Net Interest Income		**15.5%**	**14.2%**	**14.2%**			
Other Income		19.7%	20.7%	22.1%			
Total Income		**35.2%**	**34.9%**	**36.3%**			
Employee expenses		1.5%	2.2%	1.9%			
Operating expenses		20.8%	18.9%	18.6%			
Total operating expenses		**22.2%**	**21.1%**	**20.5%**			
Pre Provisioning profits		**13.0%**	**13.8%**	**15.8%**			
Provisions		6.0%	6.4%	6.5%			
PBT		**7.0%**	**7.4%**	**9.3%**			
Tax		2.4%	2.6%	2.8%			
RoA (calculated)		**4.5%**	**4.8%**	**6.5%**			
Leverage (x)		7.0	6.1	5.7			
RoE (calculated)		**31.6%**	**29.1%**	**36.8%**			

All in ₹ mn except growth	FY17	FY18	FY19	1HFY20	FY18	FY19	1HFY20
Reported ratios							
Yield on loans	21.3%	22.2%	21.6%	21.3%			
Cost of Funds	7.4%	7.2%	8.1%	8.0%			
NIM	15.3%	16.5%	15.5%	15.3%			
Cost to Income Ratio (%)	62.5%	63.1%	60.5%	56.6%			
Gross NPA (%)	2.34%	2.83%	2.44%	2.33%			
Net NPA (%)	0.76%	0.94%	0.83%	0.78%			
Tier I ratio	11.3%	12.4%	14.7%	14.8%			
CAR	15.7%	18.3%	20.0%	19.0%			

Source: Company, Ambit Capital research **1HFY20 ratios are annualized*

Partnership with promoter SBI

The nature of relationship between SBI Cards and its promoter SBI is governed by the various agreements that have been executed over a period time.

Exhibit 5: The relationship between SBI and SBI Cards are governed by the major agreements signed over the years

Type of agreement	Date of agreement	Description
Licensing agreement	Sep-2009	Provides non-exclusive and non-transferable right to use SBI logo for its business operations Requires to pay certain royalty fee to SBI within two months from the end of every FY Can be terminated on the happening of specified events termination of the SHA/failure to pay the royalty fee/change in the composition of Board/ **shareholding of SBI going below 26%**
Bank Distribution Agreement	Nov-2019	Provides branch relationship executives of SBI Cards at select branches of SBI Provides referrals through walk-in customers/business analytics/customer relationship management/YONO app and other channels
CSP MoU	Mar-2016	Provides credit cards services to corporate salary account holders of SBI
SBI UPI Agreement	Sep-2017	Provides the facility to pay credit card bills using the SBI Pay mobile application in lieu of per transaction fee
Electronic Transfer Agreement	Mar-2017	Provides electronic transfer services to SBI Cards for making payments to customers/vendors/dealers/in lieu of agreed fee agreement.
Cash Management Services Agreement	Jun-2018	Provides certain facilities (drop box clearance/cheques processing/banking and recon services) to SBI Cards customers in lieu of agreed fee

Source: Company, Ambit Capital research

Independent Board with vast experience

As per the shareholder agreement ("SHA") signed among SBI Cards, SBI and CA Rover, a maximum of ten directors are allowed into the board with following clauses:

- SBI has right to nominate four directors which includes the managing director and chief executive officer
- CA Rover has right to nominate one director of the company
- The five independent directors will be appointed in consultation with SBI and CA Rover

The current composition of the board complies with above clauses. The board is vastly experienced with most of them have strong banking business background. (See details of directors in Annexure 1)

Experienced management team

The top management team of SBI Cards is quite experienced with majority of them having background in cards, payments and banking industry. Few of them were earlier associated with SBIBPMSL (SBI Business Process and Management Services Limited) which got amalgamated with SBI Cards in 2018. (See details of top management in annexure 2). The compensation of the top management (barring who are deputed from SBI) is market linked rather than being pegged to compensation structure of the parent SBI.

SWOT Analysis

Exhibit 6: SBI Cards' SWOT analysis

Strengths	Weaknesses
▪ **Strong support from the parent company:** The tutelage provided by SBI gives natural advantage to SBI Cards in growing its business. The advantages come in the form of brand, trust, access to vast customer base and distribution strength. For example: In FY19, **55% of the new customers were sourced from SBI's** customer base. ▪ **Strong track record:** With more than 20 years of operation, the company has deep expertise in this highly competitive credit card market. Ranked second largest credit card issuer, the company has consistently delivered with its PAT CAGR of 52% over FY17-19. ▪ **Diversified & strong distribution network:** A strong sales force team, ~33K members based out of 133 Indian cities to source the customers through various channels like physical points of sale, telesales and online. SBI Cards also works with 18 co-brand partners (highest in the industry) to market its credit card products. On top of these, access to extensive SBI network (~22K branches), digital and mobile platforms like SBI YONO provides diversified ways of accessing the potential customers.	▪ **Over-dependence on parent company:** Over dependence on the parent company can be negative if the parent (SBI): 1) terminates the right to use "SBI" and its logo; 2) provides similar support to the rivals of the company as the current agreements are not exclusive; 3) divest additional stake in the company in future (below 26%) so that same level of support cannot be sought, and 4) The brand "SBI" itself is adversely affected. ▪ **Over-dependence on co-branded partners:** In 1HFY20/FY19, the share of customers sourced from co-branded partners stand at 36%/30%. This share is increasing and this overdependence on third party rather than internal sales team for customer sourcing can be negative if the agreements between the company and co-branded partners are not renewed. Normally, the agreement between the company and co-branded partners is fixed (~3-5 years). ▪ **Lack of funding advantage:** The company is designated as "NBFC-ND-SI" which means it cannot accept public deposit and thus will solely have to depend on the borrowings for its funding requirement. Lack of diversified funding avenues as compared to its competitors which also includes full-fledged banks, SFBs put it at a disadvantage vs peers.
Opportunities	**Threats**
▪ **Tapping on the favourable demographic dividend:** Fairly young population, increasing urbanisation and increasing dependence on retail credit by the young population present unique opportunity to the company. o As per CRISIL, the share of population between the age of 30 and 59 ("working age population") will go up to 37% in 2020 from 31% in 2000. o The share of people in urban areas is expected to go up to 35% in 2021 from 28% in 2001 (still way below than 60% urban population in China). o Retail credit as a percentage of nominal GDP has gone up to 17% in FY19 from 11% in FY10. ▪ **Focus on Tier-II, III and smaller cities:** The share of new accounts opened from Tier-I, II and III cities have been 67%/19%/10% in FY17 to 42%/18%/14% in 1HFY20. Clearly, the share has gone down for the Tier-1 cities and focus has shifted to the smaller towns. This opens a door of vast potential for the company given the huge distribution network provided by the SBI. ▪ **Leveraging on strengths of patent SBI:** Number of credit cards of SBI Cards is just 3% of debit cards of SBI. This ratio is ~31% for private sector banks which implies huge opportunity for SBI Cards to leverage customer base of its parent. ▪ **Government focus on digital transactions:** The Government push for digital transactions which started from 2016 using JAM trinity (Jan Dhan, Aadhar and Mobile) is helping in changing the consumer preference structurally. This structural shift in the consumer preference will also help the credit card industry going forward.	▪ **Cap on Interchange fee/MDR:** The Interchange fee accounts for 21%/51% of the total revenue/fee income as of 1HFY20. This is substantial source of the revenue for the company and may come down if the RBI acts on capping the Interchange fee. The RBI has already capped/rationalised the Interchange fee charged in case of debit cards in 2017. The same can be extended to credit cards as well given high growth in this segment. ▪ **An unsecured portfolio amidst slowing economy:** Almost all (98.5% as at 1HFY20) of the portfolio is unsecured. This poses greater credit risks especially in the current time of economic distress. Going forward, the company may have to provide additional provisions for the credit losses which might impact its profitability. Experience of US card industry shows sharp increase in credit card delinquencies in times of slowing GDP/employment growth. ▪ **Intense competition from Banks, NBFCs, and Payment Banks, etc.:** Banks (e.g. HDFCB, IIB, RBL) have become more competitive in this space. Other modes of payments like mobile, UPIs are also able to attract large number of volumes. This can put both margin and growth pressure on the company, if not countered well.

Source: Company, Ambit Capital research

IPO is a combination of fresh issuance and offer for sale

The IPO consists of fresh issuance of ₹5bn (should result in additional issuance of ~7mn shares) and offer for sale of ~131mn shares of existing shareholders. The promoter SBI/CA Rover's stake should come down to ~69%/16% post IPO and OFS.

Exhibit 7: Promoter entity holding still high post IPO

Name of shareholders	Pre-IPO		Post-IPO	
	# of shares (mn)	% holding	# of shares (mn)	% holding
Promoter				
State Bank of India	689.9	74%	652.6	69%
Non-Promoter				
CA Rover Holdings(Carlyle Group)	242.4	26%	149.2	16%
IPO Subscriber*	0.0	0%	137.7	15%
Total	**932.3**	**100%**	**939.5**	**100%**

*Source: Company, Ambit Capital research; *Assuming an issue price of Rs697 (at 14.8x 1HFY20 P/B)*

The media reports suggest pre-money valuation of ₹65bn for the company which translates into multiple of ~15 times on Sep'19 networth and a multiple of ~54 times trailing 12-month earnings. Our back-of-the-envelope calculations show post money P/B multiple of ~12 times on Mar'20 BVPS and Earnings multiple of ~45 on FY20E earnings.

Exhibit 8: Reported IPO valuation, as quoted in the media reports*

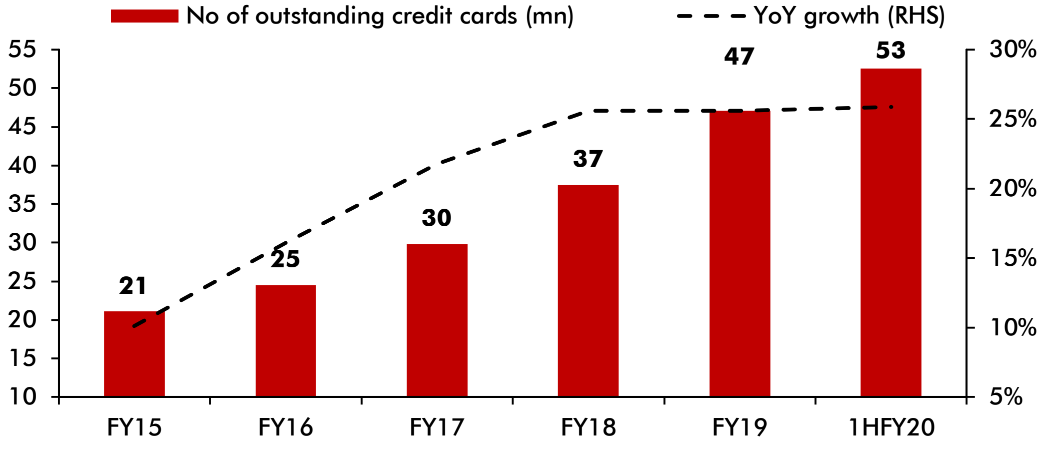
All number in ₹ mn except per share	Likely valuation
Pre-money	
Expected valuation for SBI Cards	650,000
Networth (1HFY20)	43,814
Net profit (TTM)	12,120
No of shares (#mn)	932
BVPS (1HFY20)	47.0
PB (Trailing, 1HFY20)	**14.8**
PE (TTM)	**53.6**
Offer details	
Stakes offload in OFS (%)	14%
Amount offload in OFS	91,000
IPO Issue size	5,000
Expected issue price (₹/share)	697
Post-money	
Valuation of SBI Cards	655,000
Networth (FY20E)	56,073
No of shares (#mn)	940
BVPS (FY20E)**	59.7
Net Profit (FY20E)**	14,518
PB (FY20E)	**11.7**
PE (FY20E)	**45.1**

*Source: Company, Ambit Capital research; **Net profit for FY20E is annualised. Networth/BVPS calculated by adding 1HFY20 PAT to 1HFY20 networth* * http://bit.ly/2sVGfBI

High growth industry, will growth sustain?

Credit card industry in India has grown at a healthy 22% CAGR over FY15-1HFY20 with outstanding credit cards at ~53mn at 1HFY20. However, credit card penetration is still low as compared to other financial products (Savings/current/deposit accounts, mutual funds, insurance, etc.). Also, the credit to debit card ratio is just ~6% for the system implying huge growth potential. The government nudge towards digital transactions can further provide impetus to the industry. However, within digital transactions, the share of credit cards (volume and value both) is consistently coming down from FY17 due to the arrival of UPI/mobile wallet payment systems. Also, per card spend has remained stagnant over FY18-1HFY20 mainly due to focus on smaller cities and younger population where purchasing power is low. Falling share of credit cards in digital transactions and falling per card spend are the key issues around which questions need to be asked to the management.

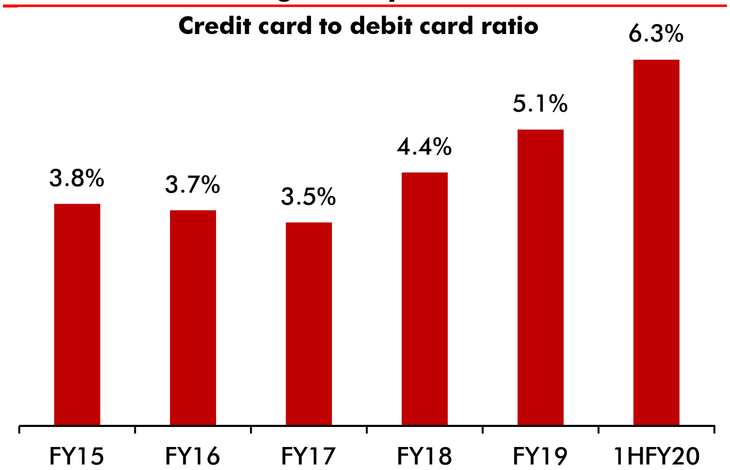
Exhibit 9: No. of credit cards outstanding has grown at CAGR of 22% over FY15-1HFY20



Source: RBI, Ambit Capital research

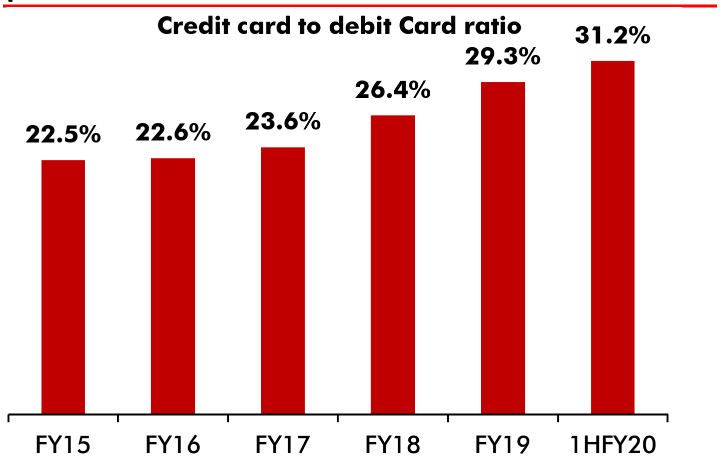
However, credit card outstanding in India is just ~6% of debit card outstanding and this has not improved meaningfully in recent times. Indian banks issuing ~297mn debit cards till Dec'19 to marginalized sections of the society under Jan Dhan scheme might have distorted this ratio. This could be seen in credit card to debit card ratio improving for private sector banks who were not active in opening Jan Dhan accounts.

Exhibit 10: Credit cards outstanding are only ~6% of the debit cards outstanding in the system…



Source: RBI, Ambit Capital research

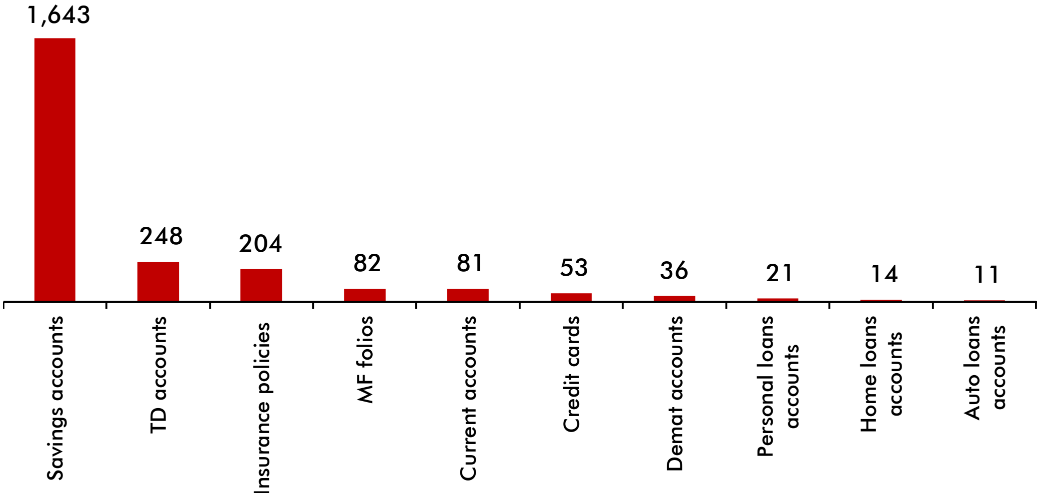
Exhibit 11: …increasing credit to debit card ratio for private sector banks



Source: RBI, Ambit Capital research Note: For top-10 private banks according to outstanding credit cards

Even comparing with other financial products, the penetration of credit cards look lower compared to other products.

Exhibit 12: Outstanding number of various financial products (FY19) (mn)

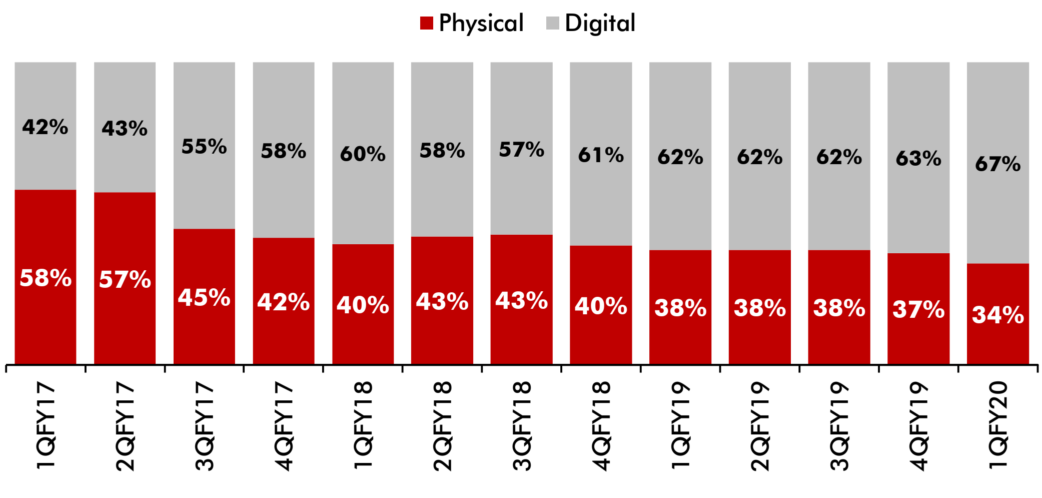


Source: RBI, SEBI, AMFI, IRDA, CRISIL, Ambit Capital research Note: 1HFY20 numbers for credit cards, personal, auto and home loans

Questions for management

- Our back-of-the-envelope calculations (assuming credit card/debit card ratio improving by 70bps every year) show ~21% CAGR outstanding credit cards in India. What according to you is the potential size of Indian credit card market and hence what should be the expected growth rate of the industry for next 5 years?
- The share of digital transaction in volume terms is increasing in the system (from 42% in 1QFY17 to 67% in 1QFY20). Do you expect the trend to be like this going forward? What can be the **steady state mix** of physical and digital transactions after 5 years down the line?

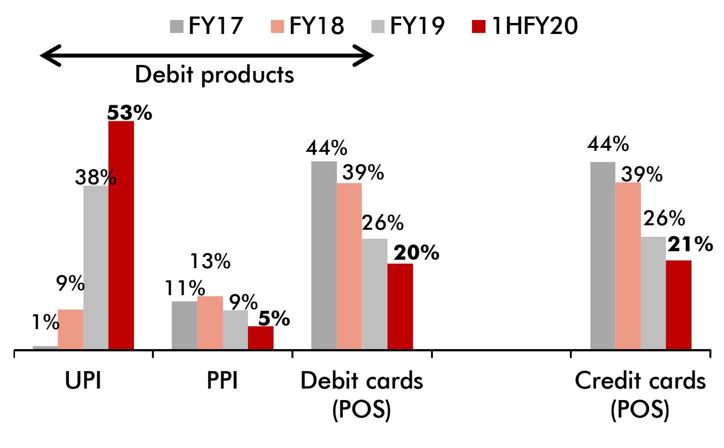
Exhibit 13: Share of digital transaction in volume terms is increasing in the system



Source: RBI, Ambit Capital research Note: Physical transactions include ATM and cheques/paper clearing while digital transactions include RTGS/ECS/NEFT/NACH/IMPS/Credit cards/Debit cards/Prepaid payment instruments

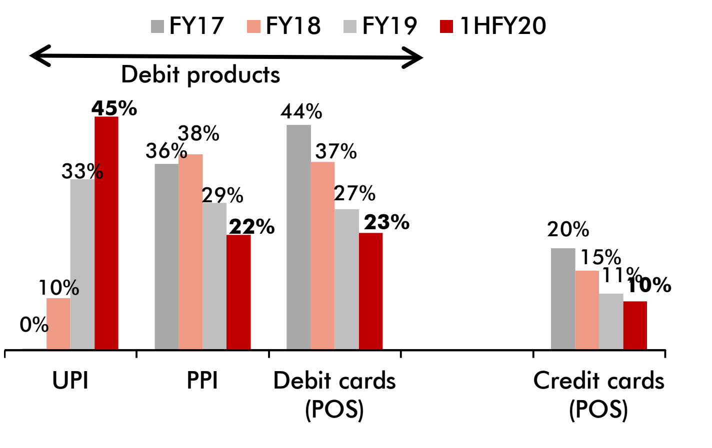
- If we look at the composition of digital transaction over the years, the share of debit products (UPI, PPI and debit cards) have gone up due to the advent of UPI at the expense of credit card products. The share of credit card in volume/value terms have come down to 20%/44% in FY17 to 10%/21% in 1HFY20. Do you think this falling share of credit cards due to arrival of UPI will impact your business materially?

Exhibit 14: Falling share of credit card share (value wise) as UPI becomes a major force



Source: RBI, Company, Ambit Capital research

Exhibit 15: Falling share of credit card volume wise as well

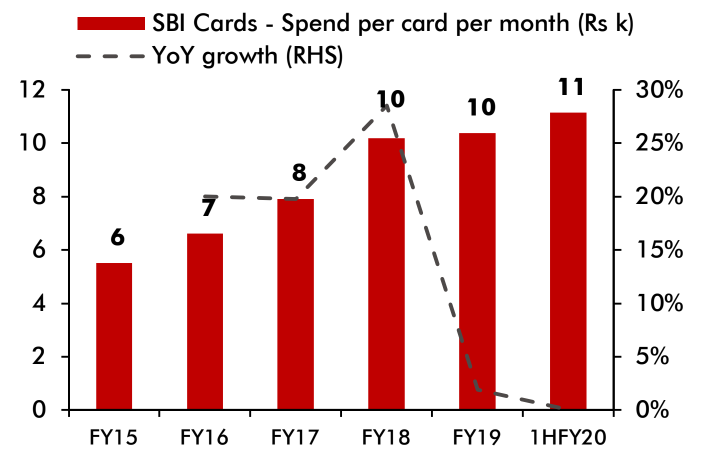


Source: RBI, Company, Ambit Capital research

Stagnating per card spends

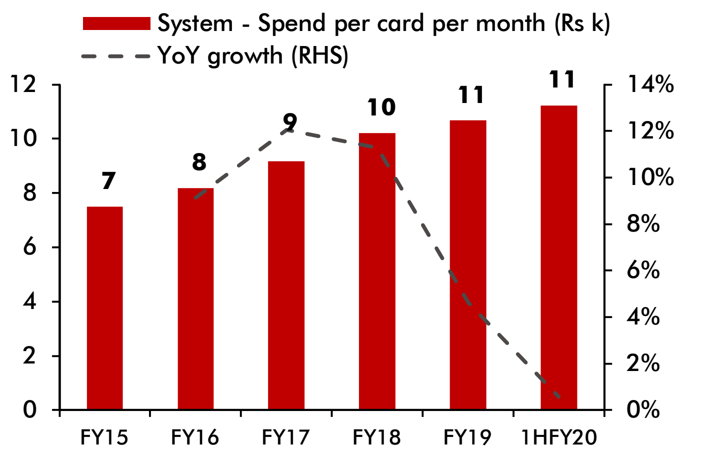
- After growing at a CAGR of 23% over FY15-18, per card spend seems to have stagnated between FY18 and 1HFY20 for SBI. Similar trends have been observed at the industry level where per card spends have stagnated in recent times. What's the reason behind stagnating per card spends? Is it because of incremental growth in cards coming from younger customers/Tier-3-4 cities where spending power is lower? What should be sustainable per card spend growth going forward?

Exhibit 16: SBI Cards - Per card spends have broadly remained at similar level post FY18



Source: RBI, Company, Ambit Capital research

Exhibit 17: Per card spends has broadly remained at similar level for industry as well post FY18

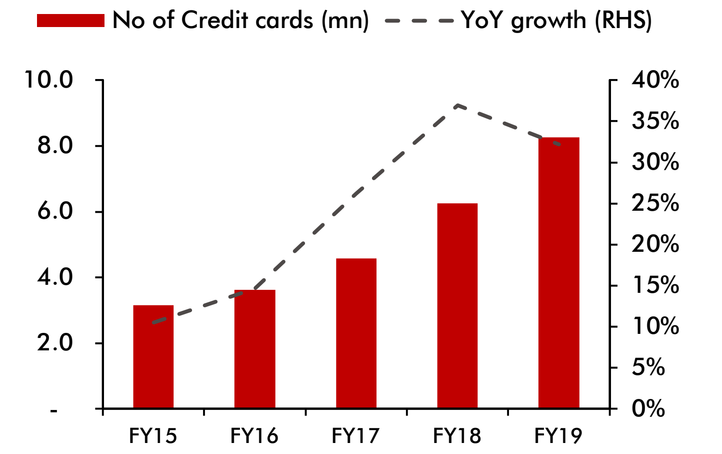


Source: RBI, Company, Ambit Capital research

Increasing market share, how much more it can go up?

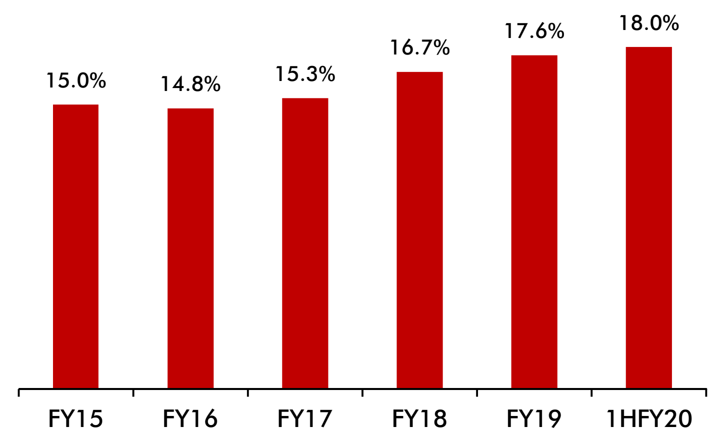
Number of credit cards outstanding has grown at 28% CAGR for SBI Cards over FY15-1HFY20 with market share increasing from 15% at FY15 to 18% at 1HFY20.

Exhibit 18: SBI Cards - Outstanding credit cards have been increasing...



Source: Company, Ambit Capital research

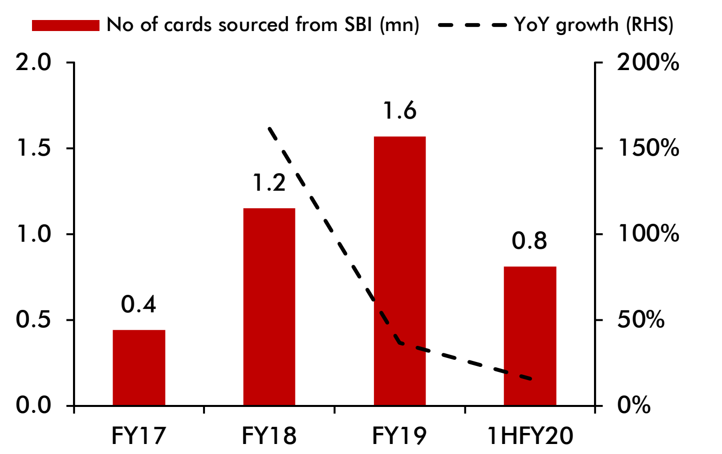
Exhibit 19: ...and market share as well



Source: Company, Ambit Capital research

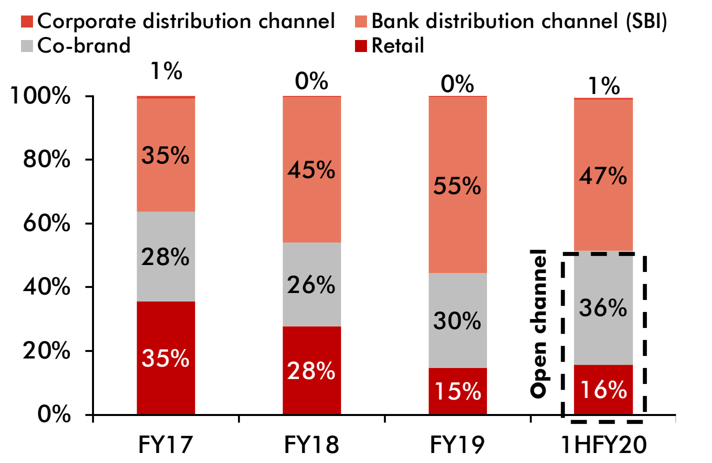
A major driver of increase in credit card growth and increase in market share for SBI Cards has been increased sourcing from its parent. New credit card sourced from SBI has grown at 60% CAGR in FY17-1HFY20 vs just 42% CAGR from other sources.

Exhibit 20: Number of cards sourced from SBI Bank distribution network has been increasing...



Source: Company, Ambit Capital research

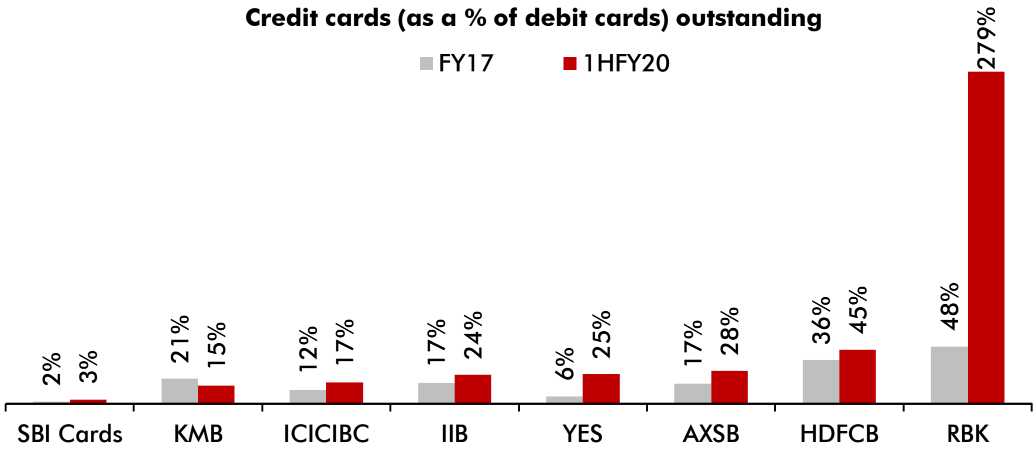
Exhibit 21: ...and market share of bank distribution channel as well



Source: Company, Ambit Capital research

Data shows that outstanding credit cards of SBI Cards are only 3% of debit cards outstanding of SBI vs ~31% for private sector banks. This, we believe, is a very good proxy for potential available with SBI Cards to penetrate SBI customer base.

Exhibit 22: Lowest share of credit cards over debit cards for SBI Cards vs peers implies strong growth potential from SBI customers



Source: RBI, Ambit Capital research

Questions for Management

- What percentage of SBI liability-side customer base could be penetrated for credit cards? What are the strategies the company is employing to penetrate deeper into SBI customer base? Do you have any dedicated sales force to tap SBI savings account customers?
- Co-branded credit cards has been another area of high growth for SBI Cards where new origination of co-branded credit cards CAGR was 70% over FY17-1HFY20, with share of co-branded credit cards in new originations increasing from 28% in FY17 to 36% in 1HFY20. What are the key factors which attract companies like Ola, Air India, BPCL, Yatra, etc. to tie up with you rather than your competitors? How easy it is for your co-branded partners to switch to your competitors?

Net interest Income could be the biggest driver of future earnings

Net interest income is the biggest component of net revenues for SBI Cards followed by interchange fee on card transactions.

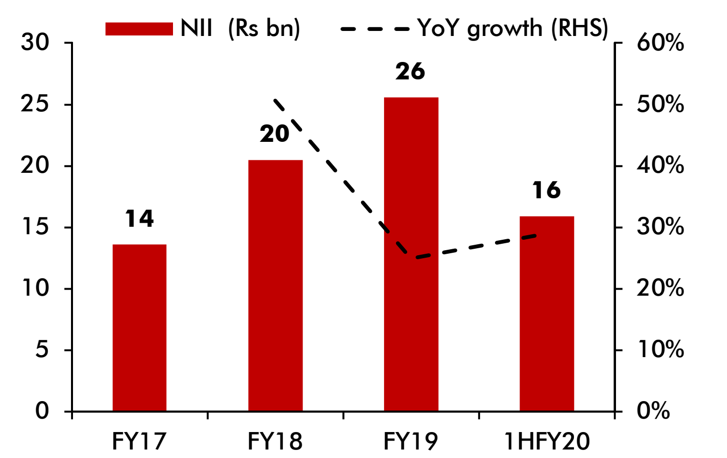
Exhibit 23: NII and spend-based fee income are key components of net revenues

Revenue stream	% of total Income (1HFY20)	Comments
Net Interest Income (NII)	39%	Interest income on credit card receivables net of interest expenses
Spends-based fees	25%	Interchange fees for the transactions carried out using credit cards. Also, includes foreign exchange mark-up income on international transactions using our credit cards.
Instance-based fees	16%	Late/reward redemption/cash withdrawal/over limit/payment dishonour/processing/statement retrieval fees or service charges for various cross-sell or value-added products
Subscription-based fees	7%	Credit card membership and annual fees
Business development income	4%	Contractual business development incentives from payment networks under long-term contracts. Based on increases in total credit card spends, total credit cards outstanding and new product launches, etc.
Service Charges	1%	Commission from selling of third-party products (like card protection plans), share of accelerated reward points cost recovered from partners, brand association fee charged to partners, transaction revenue from aggregators.
Others	8%	Recovery from bad debts written off, income from investments/fixed deposits and liabilities and provisions written back and tax refunds

Source: Company, Ambit Capital research

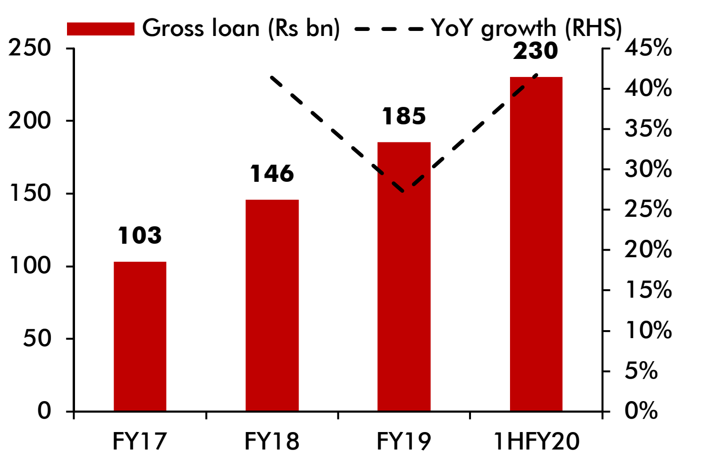
Net interest income forms 39% of net revenues of SBI Cards in 1HFY20 (down from 46% in FY17). The company earns interest income on credit card receivables. Net Interest Income witnessed CAGR of 34% over FY17-1HFY20, broadly in line with 37% CAGR in gross loan portfolio.

Exhibit 24: Net interest income rose...



Source: Company, Ambit Capital research

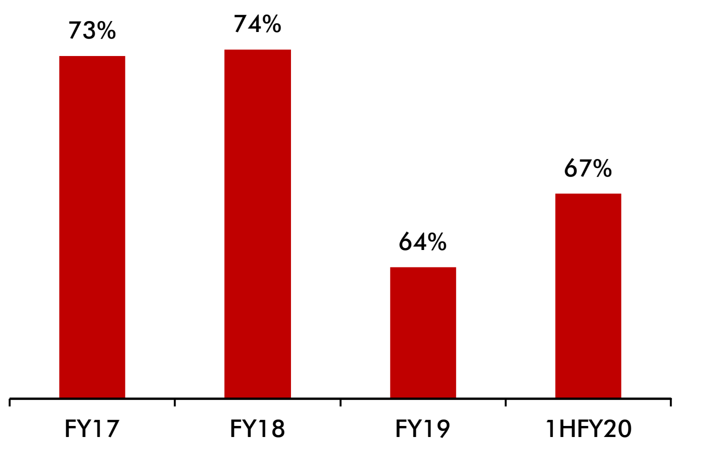
Exhibit 25: ...as gross loan portfolio increased



Source: Company, Ambit Capital research

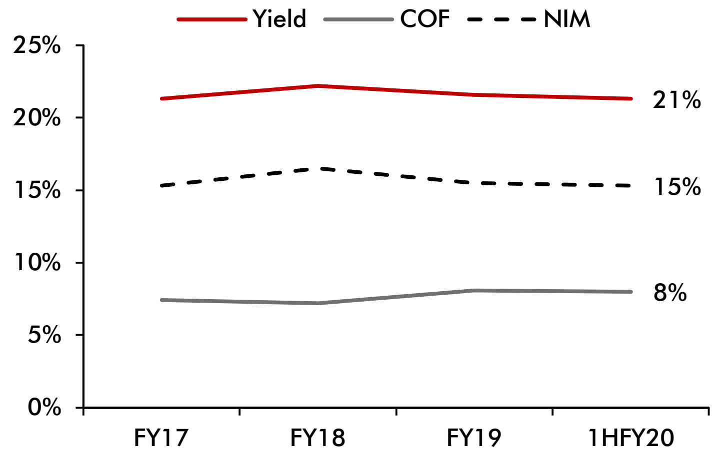
Gross loan portfolio is broadly driven by credit card spends and has ranged over 18-36% of spends in FY17-1HFY20. NIMs for the company have been broadly stable at 15.3% to 16.5% with lending yields being in the range of 21.3% to 22.2%. However, there has been increase in cost of funds for the company over the last 18 months with cost of funds increasing to ~8.0% in 1HFY20 from ~7.2% in FY18.

Exhibit 26: Loan portfolio as a percentage of 3-month spends



Source: Company, Ambit Capital research

Exhibit 27: NIMs are broadly stable



Source: Company, Ambit Capital research

However, the entire gross loan portfolio of the bank is not interest earning portfolio. The gross loans (credit card receivables) portfolio is divided into three parts depending upon the interest earning capability:

- **"Transactor" receivables:** Dues which are paid within the due date of payment and thus company does not earn any interest. As per our estimate, ~33% of the portfolio should be transactor portfolio in 1HFY20.
- **"Term loan" receivables:** Dues are converted in equal monthly payments (EMI) by the customers and thus earn interest income for the company. Term loan usually carries lower interest rate as compared to the Revolver receivables. As per SBI Cards website, the interest on EMI loans is in the range of 14-15%. As per company filings, ~30% of the portfolio is term loan portfolio in 1HFY20 and has been at similar levels in past.
- **"Revolver" receivables:** Dues which are revolved from current month to next month, earn interest income for the company. As per SBI, the company earns yield in the range of 36-48% on this portfolio (highest interest rate among the three kinds of receivables). As per our estimate, ~38% of the portfolio should be revolver portfolio in 1HFY20.

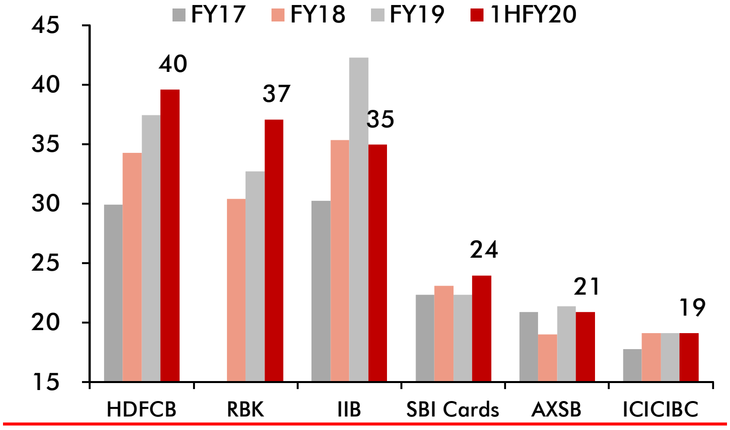
Exhibit 28: Portfolio mix: "Revolver" receivable has the highest interest rate

Segments of portfolio	% of portfolio (1HFY20)	Interest rate (%)
"Transactor" receivables	32.6%	No Interest
"Revolver" receivables	37.6%	36%-48%
"Term loan" receivables	29.8%	14%-15%

Source: Company, Ambit Capital research Note: We have estimated the portfolio mix using the data available in DRHP (proportion of term loan in total credit card receivable & total yield) and interest rate charged on revolver/term loan receivables available on the SBI Cards website

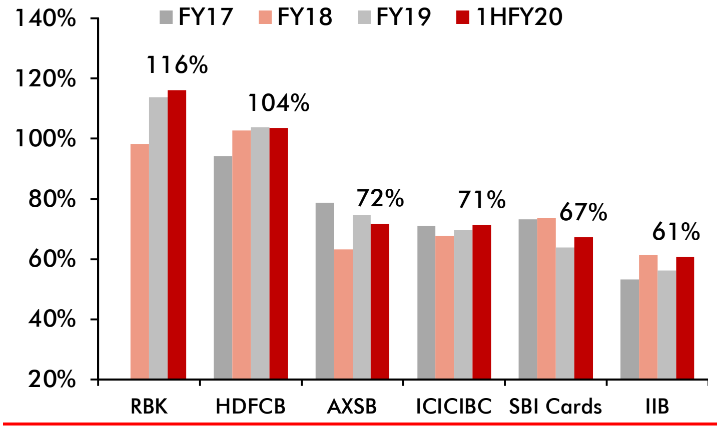
However, loan book size of SBI Cards is relatively smaller compared to its size in number of outstanding cards and number of transactions. Hence, per card loan portfolio of SBI Cards is smaller compared to peers like HDFC Bank and RBL Bank. This trend is also visible in terms loan book as a percentage of trailing three-month spends being lower for SBI Cards vs HDFC Bank and RBL Bank.

Exhibit 29: Per card loan book (₹ k) for SBI Cards has been lower compared to peers



Source: Company, Ambit Capital research

Exhibit 30: Rollover rate (loan as % of 3-month spends) for SBI Cards is lower than peers



Source: Company, Ambit Capital research

Hence, loan book and specially interest earning loan book of the company could grow at much faster rate than growth in number of cards/number of transactions. E.g. assuming 20% CAGR in number of cards and 5% CAGR in spends per card, the loan portfolio of SBI Cards can grow at 41% CAGR with interest earnings portfolio growing at even faster pace at 46% CAGR if the rollover rate of SBI Cards converges with likes of HDFC Bank and RBL Bank.

Exhibit 31: Interest earning portion of the loan book can grow at faster pace

	FY15	FY16	FY17	FY18	FY19	FY19-24E CAGR
No of Credit cards (mn)	3.2	3.6	4.6	6.3	8.3	20.6
YoY growth (RHS)	*10%*	*15%*	*26%*	*37%*	*32%*	*20%*
Total spend (₹ mn)	208,863	287,272	434,355	764,702	1,029,702	3,270,125
YoY growth		*38%*	*51%*	*76%*	*35%*	*26%*
Spend per card (₹)	66,137	79,356	95,065	122,189	124,489	158,883
YoY growth		*20%*	*20%*	*29%*	*2%*	*5%*
Loans			99,829	140,455	179,087	981,038
YoY growth				*41%*	*28%*	*41%*
12m -rollover rate			23%	18%	17%	30%
Interest earnings loans (₹ mn)			66,557	92,901	120,054	793,561
YoY growth				*40%*	*29%*	*46%*
Interest earnings loans (%)			**67%**	**66%**	**67%**	**81%**

Source: Company, Ambit Capital research

Questions for management

- What is the rationale behind lower loans per card and lower loans as a percentage of transactions? Is it a conscious strategy to be cautious on offering EMI conversions and/or minimizing rollovers or better quality of customers is leading to lower rollover rate and lower EMI conversion?
- Does the company have any plans to increase EMI-based loans/revolvers and what is the strategy to execute this without taking too much balance sheet risk?
- What is the reason behind changing liability mix towards debt securities compared to bank borrowings given that it is relatively difficult to get money from bond market than from banks post-liquidity crisis?

Exhibit 32: Liability mix is shifting towards debt securities

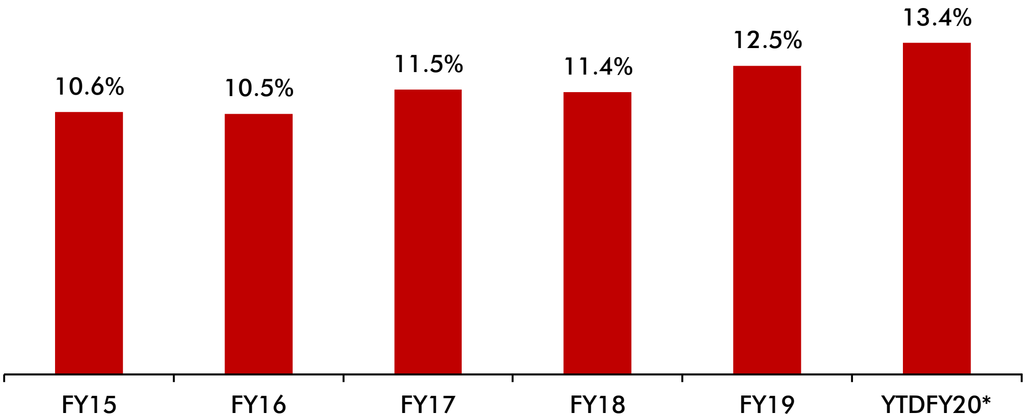
Liability mix	FY18	FY19	1HFY20	Comments
Borrowings	72%	67%	60%	Cost of borrowing - 7.80-8.30%
Debt Securities	28%	33%	40%	Cost of borrowing - 5.75-9.65%

Source: Company, Ambit Capital research

- DRHP shows that your borrowing cost from your parent SBI is at ~7.80%, lower than other banks at ~8.30% with ~87% of the bank borrowings coming from SBI in 1HFY20. Back-of-the-envelope calculations show that if replacing borrowing from the SBI to other banks could impact your RoA by ~15-20bps. Do you get preferential rates from SBI on your borrowings? How much is the headroom to borrow more from SBI?

Credit card loans in India compete with personal loans in India which is visible in credit card loans being just ~4% of total unsecured loans in India. Is there a possibility that with increasing credit card limits/EMI options on large purchases, credit card loans can replace unsecured personal loans in India? Are you seeing any changing consumer preference in this regard?

Exhibit 33: Share of credit cards in unsecured loans is increasing



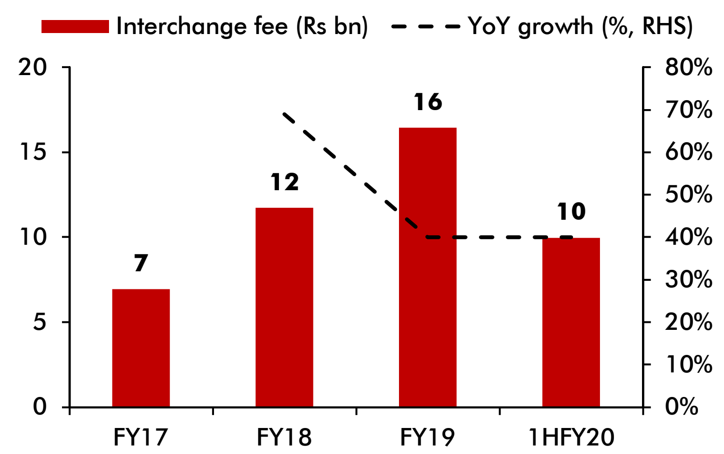
*Source: RBI, Ambit Capital research *as of end-October 2019*

Is fee income sustainable?

Risk of cap on transaction-based fee

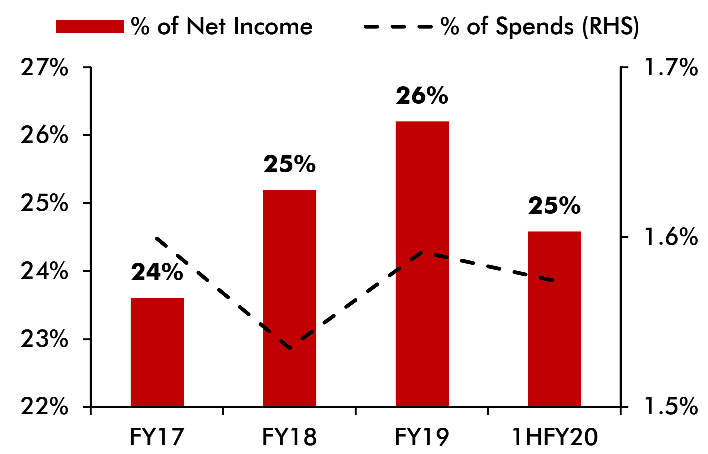
Interchange fees for the transactions carried out using credit cards form ~25% of the net income for SBI Cards. This income stream has grown at a CAGR of 49% over FY17-1HFY20. Interchange fee is part of merchant discount rate (MDR) which merchant pays on value of transaction. MDR in India is ~2-3% out of which ~1-2% goes to issuing bank (SBI Cards in this case) in the form of interchange fee. Remaining ~1-2% is split between payment Gateway (Visa, MasterCard, etc.) and the bank which owns POS terminal at merchant location.

Exhibit 34: Interchange fee has been growing robustly



Source: Company, Ambit Capital research

Exhibit 35: Interchange fee as a % of net income & as % of spends



Source: Company, Ambit Capital research

Interchange and MDR charges, currently at ~1-3%, on credit card transactions in India are relatively higher than some other countries.

Exhibit 36: Cap on Interchange fee in various countries/regions is lower than India

Country/Region	Cap on Interchange fee- Credit cards
Canada	1.50%
China	0.45%
Australia	0.50%
EU	0.30%

Source: RBI, Ambit Capital research

Over the years, RBI has been bringing down transaction charges on digital transactions to promote digital transactions in India. Over the years, RBI has brought down MDR charges on debit cards to 0.3-0.9%. There has also been cut in transaction charges for other digital payments in recent years.

Exhibit 37: Regulatory changes over the years – Reducing MDR charges on debit card transactions

Year	Comments
2012	Introduction of MDR cap for debit card (upto 0.75% for value upto ₹2,000, upto 1% for value above ₹2,000)
2016	Revision in MDR cap (upto 0.25% for value upto ₹1,000, upto 0.50% for value above ₹1,000 and upto ₹2,000)
2017	**Revision in MDR cap:** ▪ For merchants with turnover <=₹2mn: 0.4% for physical POS infrastructure (including online card transactions) & 0.3% for QR code based transactions, up to a max of ₹200 ▪ For merchants with turnover >₹2mn: 0.9% for physical POS infrastructure including online card transactions & 0.8% for QR code based transactions, up to a max of ₹1,000
2019	In Budget speech in July 2019, The FM announced that no MDR will be charged from 1st November 2019 for establishments with annual turnover of ₹0.5bn and above

Source: Company, Ambit Capital research

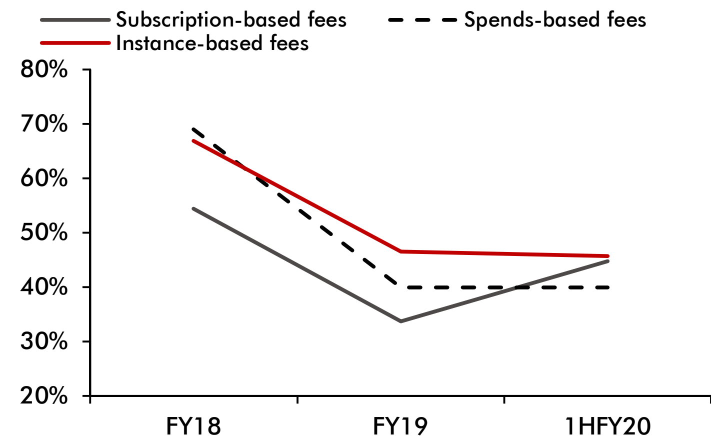
A committee set up by the RBI and headed by Mr. Nandan Nilekani to promote digital payments in India has proposed to decrease Interchange fee by 15bps on credit card transactions as well. This could have **decreased net revenue by ~2% and PAT by ~9%.** In this context, management should be asked:

- What is the probability of MDR/Interchange charges being brought down on credit cards and what would be the impact on financials if done?
- With charges on other modes of payments being lower for merchants, why can't merchants incentivize customers to pay through other digital modes like credit cards/UPI?

Increasing instance-based fee

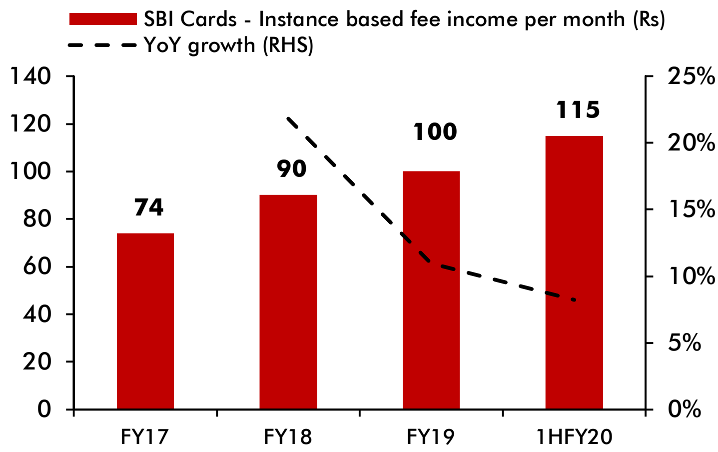
Instance-based fee which mostly comprises late payment fee, ATM cash withdrawal fee is 34% of the fee income and 16% of net income of the company in 1HFY20. This is the fastest growing fee income stream for the company with 53% CAGR over FY17-1HFY20 vs 49% for total fee income. This fee item per card per month has increased at 14% CAGR from ₹74 in FY17 to ₹115 in 1HFY20.

Exhibit 38: Fee income (YoY) growth – Instance-based fee is growing fastest among all



Source: Company, Ambit Capital research

Exhibit 39: Per card instance-based fee has increased by 14% CAGR



Source: Company, Ambit Capital research

Question for management

- What is driving per higher growth in instance-based fee growth? With improving payment infrastructure, can it lead to timely payments resulting in decrease in this fee line item?

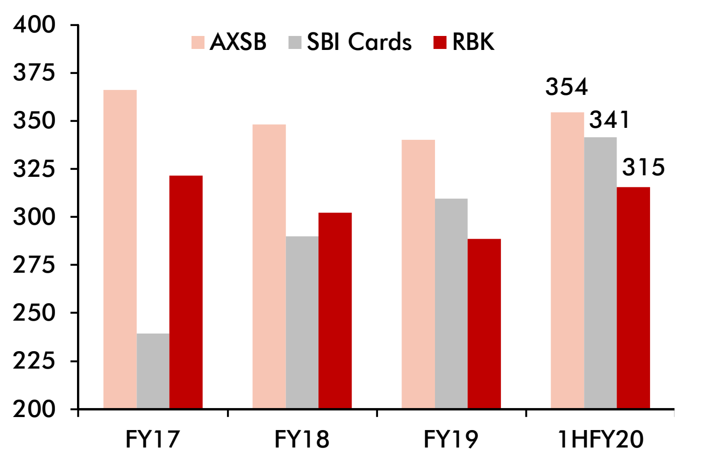
Lower fee income as % spends vs Axis and RBL

Few of the banks (Axis and RBL Bank) give fee income from credit card business. We have compared the fee income per card and fee income as percentage of spends for those banks with SBI Cards. If we look at the fee income per card, all three (Axis, RBL and SBI Cards) have broadly comparable fee income per card per month at ~₹315-354. However, if we look at the fee income as percentage of spends, it is the lowest amongst the three.

Question for management

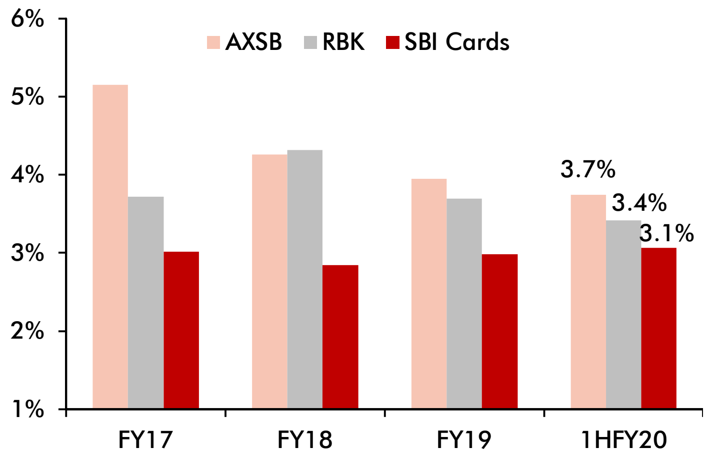
- Why fee income as percentage of spends is low for SBI Cards at ~3% vs ~4% for others? Why has this number remained stagnant at ~3% since FY17?

Exhibit 40: Fee income per card per month (₹) is comparable...



Source: Company, Ambit Capital research

Exhibit 41: ...but fee income as % of spends is lowest among peers

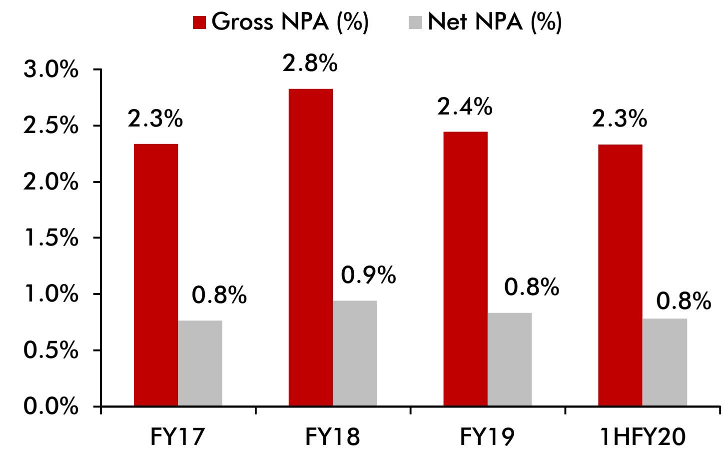


Source: Company, Ambit Capital research

Asset quality broadly stable, but is it sustainable?

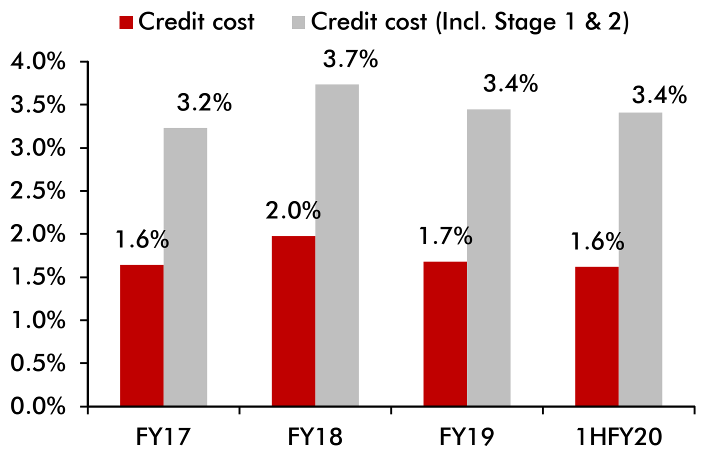
Asset quality trends have been broadly stable for the bank with gross NPA ratio being in the narrow range of 2.3%-2.8% and credit cost (provision expense as a % average loan book) being in the narrow range of 3.2% to 3.7%.

Exhibit 42: NPA ratio and...



Source: Company, Ambit Capital research

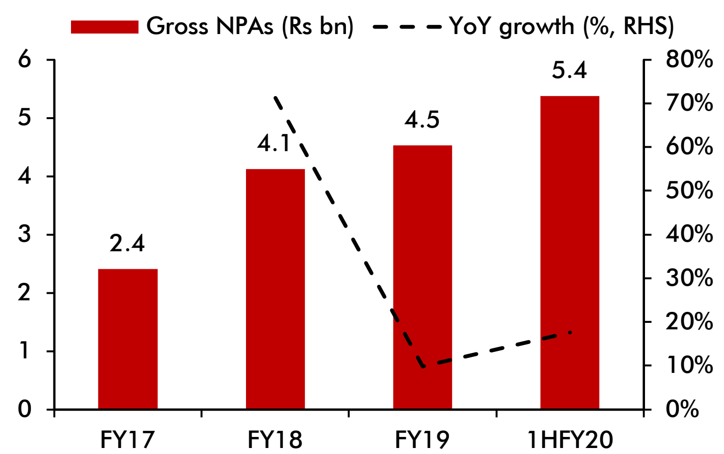
Exhibit 43: ...and credit cost are broadly stable



Source: Company, Ambit Capital research

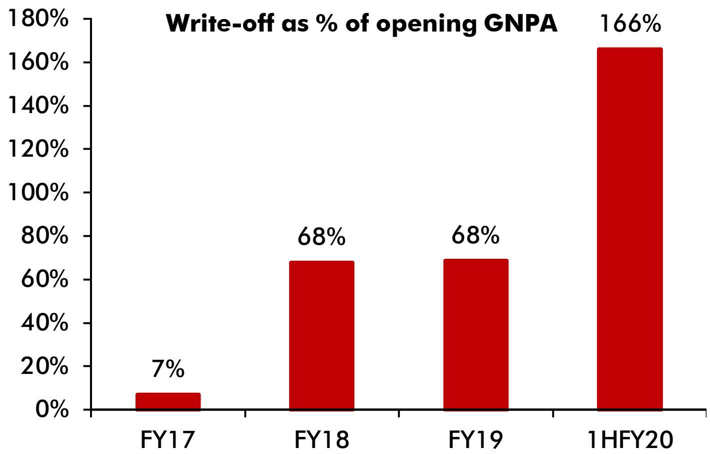
However, in absolute term there has been ~20% increase in gross NPAs between Mar'19 and Sep'19. Moreover, write-offs as a % of opening gross NPAs have also jumped in 1HFY20 vs earlier years.

Exhibit 44: NPAs have increased between Mar'19 and Sep'19...



Source: Company, Ambit Capital research

Exhibit 45: ...so have the write-offs



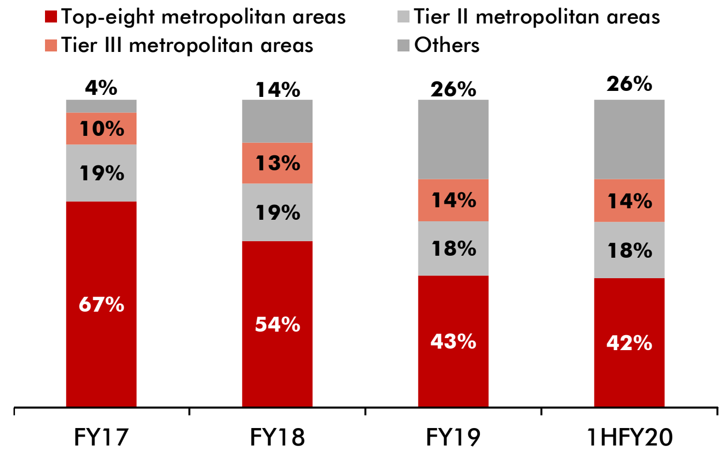
Source: Company, Ambit Capital research

Question for management:

- How should we read the jump in both absolute NPAs and write-offs in 1HFY20? How has been the asset quality trend on a static pool basis as gross NPA ratio could be misleading in a high growth company?
- The write-off in 1HFY20 has increased to 166% of opening GNPA from 68% in FY19. As per DRHP, this is due to the stress in one corporate account which resulted in write-off of ₹921mn. What did go wrong here? What is the current status of the account? Are there anymore accounts which might slip into stress going forward?

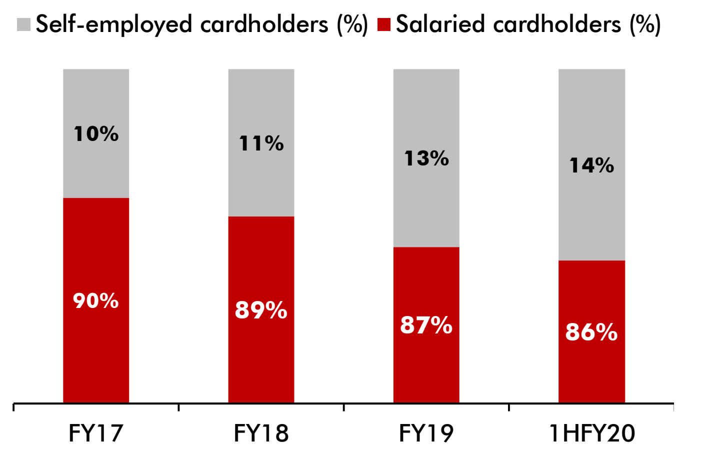
- Data shows that share of new accounts opened in non-metros and share of self-employed cardholders is inching up for you. Don't you think that the change in profile of the customer should lead to higher NPAs/credit cost for you going forward vs historical trends?

Exhibit 46: Proportion of new accounts opened in non-metros and...



Source: Company, Ambit Capital research

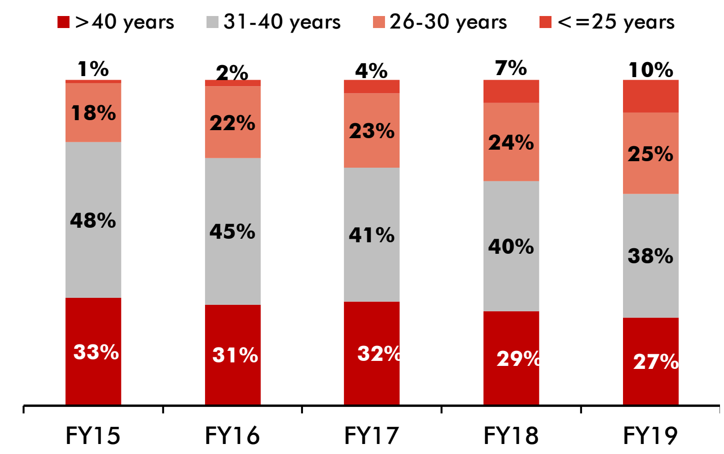
Exhibit 47: ...self-employed cardholders for SBI Cards is increasing



Source: Company, Ambit Capital research

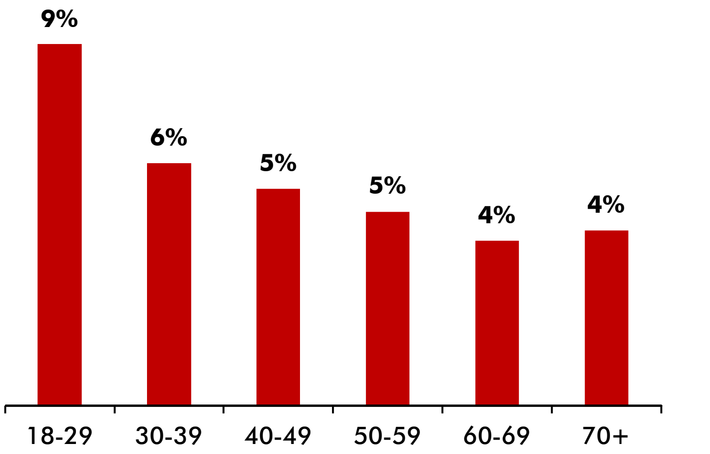
- In overall credit card Industry, there is an increase in share of younger people (<30 years) in originations. However, evidence from US Credit card Industry shows that 90+ dpd delinquencies is the highest for the younger population across cycles. Don't you think that the change in demographic profile of the customer should lead to higher NPAs/credit cost for you and Industry as whole?

Exhibit 48: Indian credit cards Industry – Increasing proportion of credit card originations among millennials (persons below 30 years)



Source: Company, Ambit Capital research

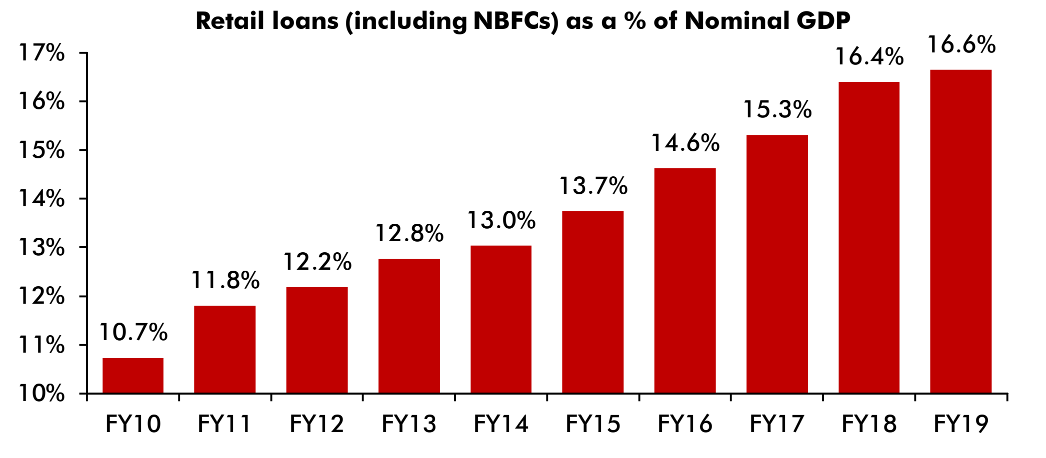
Exhibit 49: US credit cards Industry – Highest delinquency levels (90+ dpd) for younger population (1HFY20)



Source: New York Fed Consumer Credit Panel/Equifax, Ambit Capital research

- As per our analysis, consumer credit as a % of nominal GDP has increased from 14% in FY15 to 17% in FY19. There were huge losses for banking industry in credit card/personal loan portfolios in FY109-10 post Lehman crisis when consumer leverage was just 50% vs current levels. With higher consumer leverage compared to the past amidst slowing economy and slowing job growth/salary hikes, what comfort can you provide on future asset quality trends of the company?

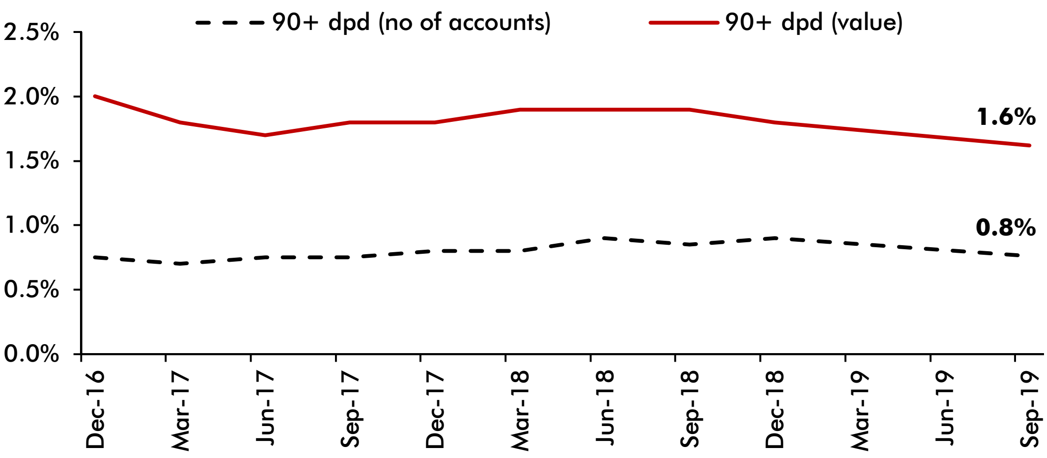
Exhibit 50: Consumer leverage is increasing in the economy



Source: RBI, Ambit Capital research

The delinquency levels in credit cards industry have remained under control recently. The 90+ dpd delinquency levels on the basis of value/no. of accounts have come at 1.6%/0.8% in 1HFY20 vs 1.8%/0.8% in 1HFY18.

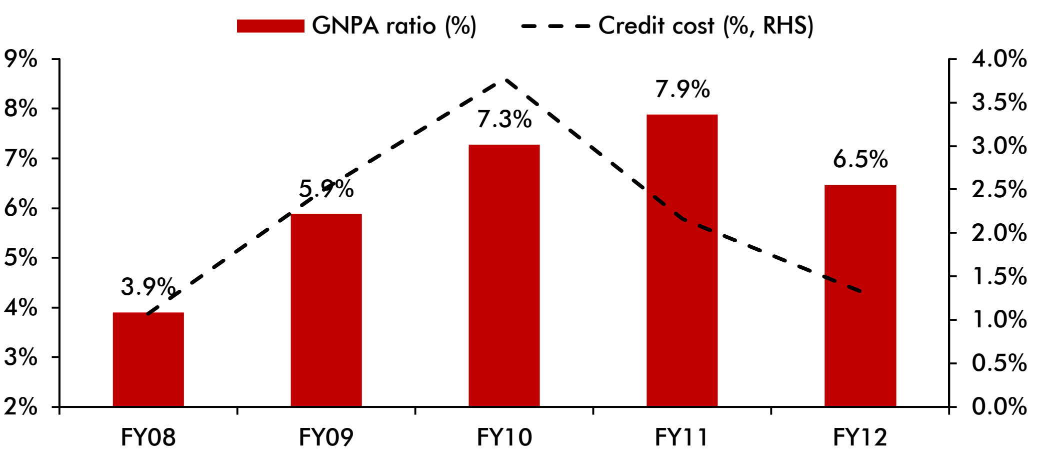
Exhibit 51: Delinquency level is under control for the Indian credit card industry



Source: CIBIL, Ambit Capital research

However, we have seen that credit card NPAs have risen sharply in FY08-11 for Indian banks post Lehman crisis. This is visible in credit card NPAs of ICICI Bank during those years. Why do you think that FY08-11 won't be repeated?

Exhibit 52: GNPA and credit cost for consumer loans & credit cards spiked for ICICI Bank over FY08-11…

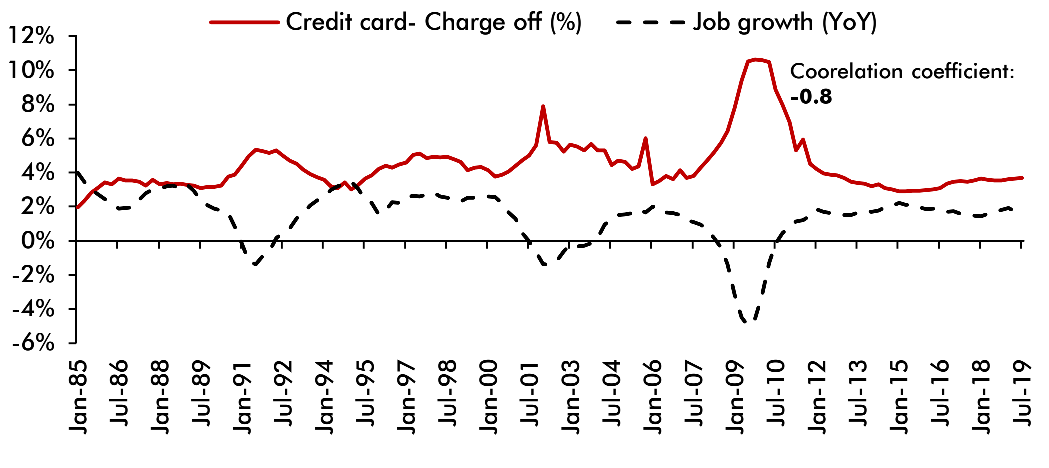


Source: Company, Ambit Capital research Note: Data for consumer loans and credit cards which also includes home, auto and personal loans.

Also, the Indian credit card market is still evolving and to project the current level of low delinquency being same going forward is not prudent. The delinquency levels in an economy depend upon many factors like GDP growth, GDP per capita growth, employments generation, etc. To gauge the impact of these factors on delinquency levels, we have studied the US Credit card market which has matured over the years.

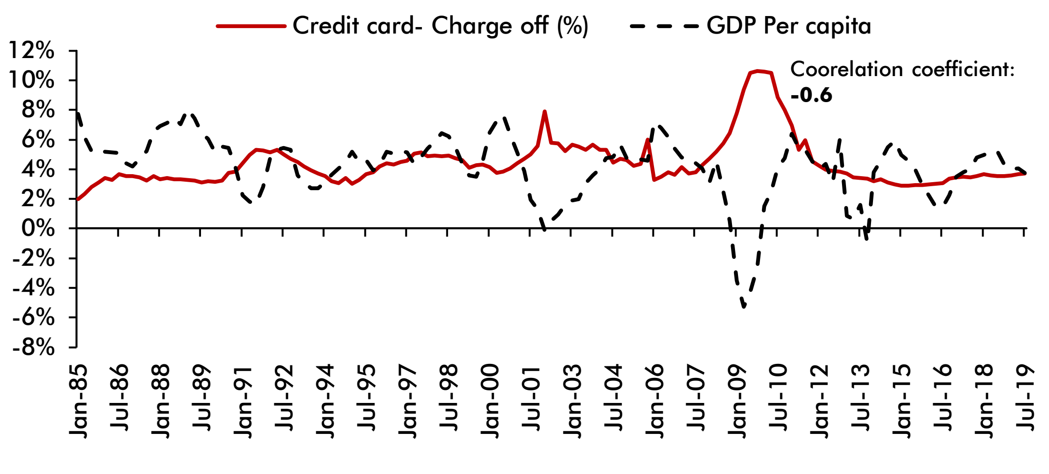
If we look at the credit cost in US credit card market, it has gone as high as ~11% in 2009. The credit cost is highly inversely correlated with GDP per capita and employment generation. As the Indian credit card market gets matured, the same kind of pattern observation cannot be entirely ruled out. Given the current slowdown in economy and its adverse impact on employment generation, don't you think the delinquency levels may increase in coming years?

Exhibit 53: US Credit card market: Credit cost is inversely related to job growth



Source: FED website, Ambit Capital research

Exhibit 54: US Credit card market: Credit cost is inversely related to GDP per capita

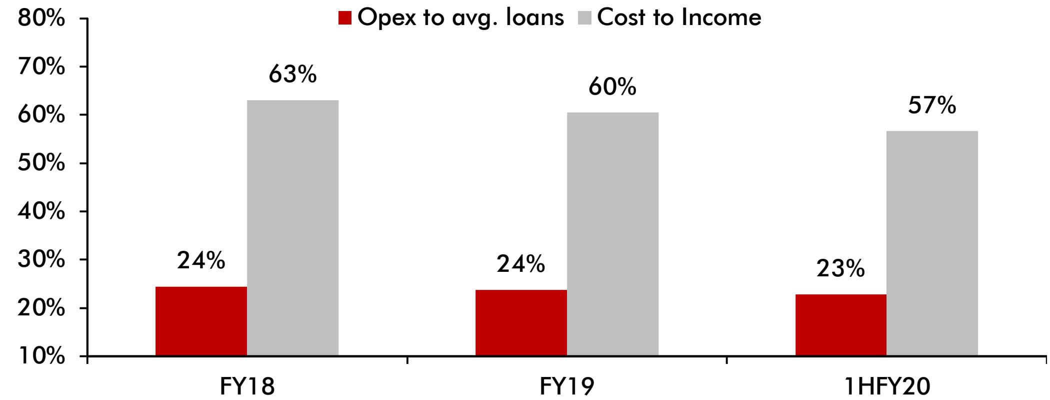


Source: FED website, Ambit Capital research

Improving operational efficiency

Operating efficiency is improving for SBI Cards over the last two years with cost-to-income ratio improving from 63% in FY18 to 57% in 1HFY20. Cost to average loan book has also decreased from 24.5% in FY18 to 22.8% in 1HFY20.

Exhibit 55: Cost-to-income ratio has been falling



Source: Company, Ambit Capital research

Sales and promotion cost is the biggest cost item, comprising around 46% of the company's total expenses followed by reward point redemption being around 11% of the expenses.

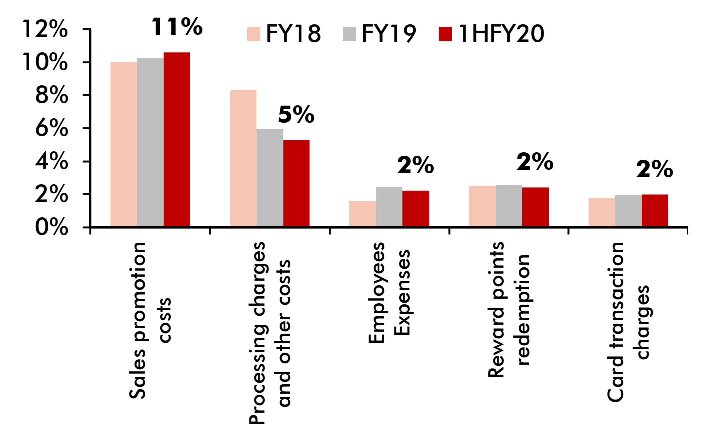
Exhibit 56: Operating expense - Types

Opex items	% of total Income (1HFY20)	Comments
Sales promotion costs	46%	Acquisition cost for sourcing new accounts, cost of value propositions/promotional/cashback/pass back/other benefits to cardholders
Reward points redemption	11%	Cost of reward points already redeemed/estimated cost of future reward redemptions based on an actuarial valuation
Employee expenses	9%	For 3,701 employees of SBI Cards and 37,951 outsourced workforce
Card transaction charges	9%	Charges and levies paid to payment networks for transaction charges and other services
Processing charges & Others	25%	Communication/collection/power and fuel/printing, postage/stationery/professional and consulting/advertising/data processing/short and variable lease, etc.

Source: Company, Ambit Capital research

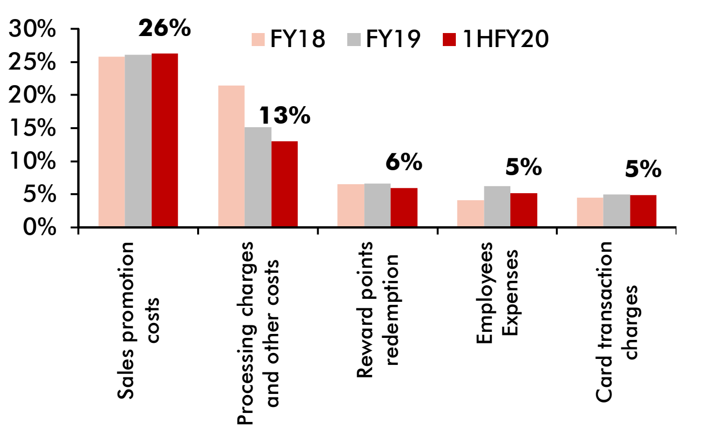
The biggest driver of improvement in operating efficiency has been "processing and other charges" which decreased from 8.3% of average loan book in FY18 to 5.3% in 1HFY20 and from 26% of net income in FY17 to 13% of net income in 1HFY20. All other expenses items have broadly remain stable as a percentage of average loan book and net income

Exhibit 57: Expense items as a percentage of average loans: Processing and other charges are reducing



Source: RBI, Company, Ambit Capital research

Exhibit 58: Expense items as a percentage of net income: Other expenses items broadly remain stable



Source: RBI, Company, Ambit Capital research

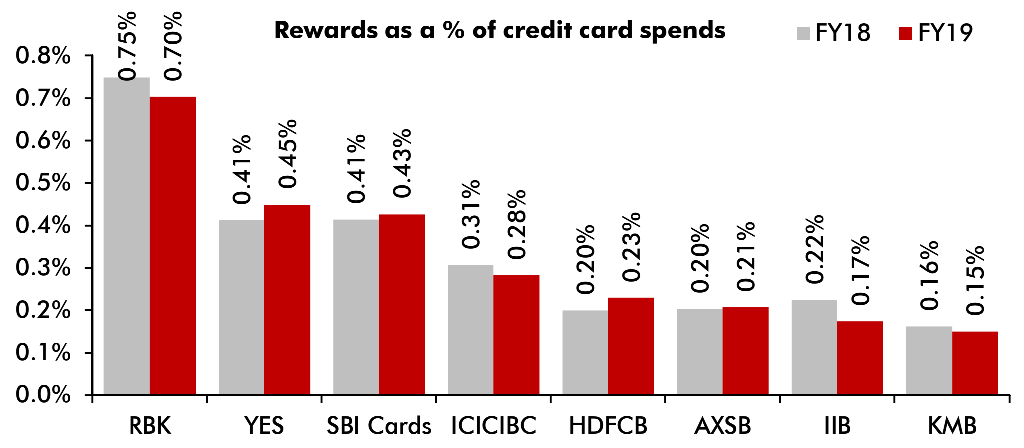
Questions for Management

Data suggest that most of the expense items are broadly variable in nature moving broadly in line with net income and loan book. How much more scope left for further improvement in cost-to-income/cost-to-average loan book ratio?

Rewards programme – Higher vs peers

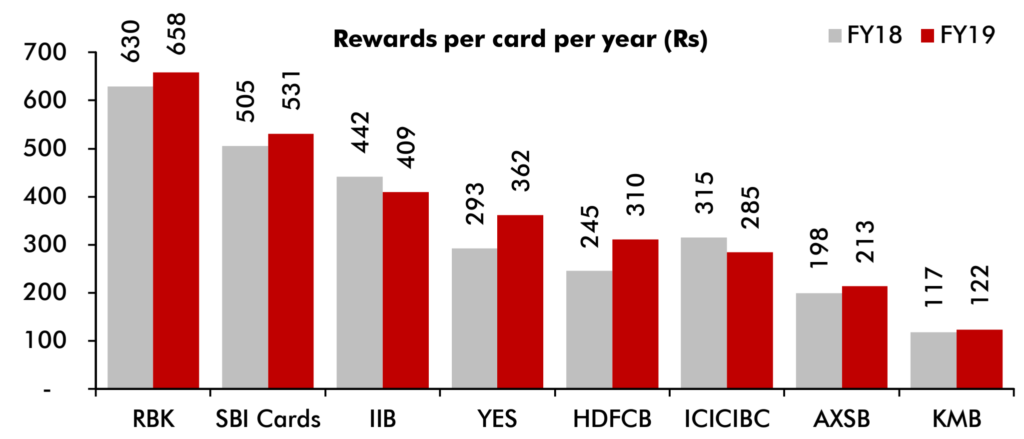
Rewards programme is one such avenue where the credit card providers fight intensely to attract and retain the customers. Analysis of provision for rewards disclosed by all large banks in their annual report suggests that SBI Cards' rewards per card is ~₹531 in FY19, only lower than that of RBL Bank, but higher than the category average of ~₹361. Also, rewards as a percentage of credit card spends for SBI Cards are 0.43%, only lower than RBL Bank and Yes Bank.

Exhibit 59: Peer comparison - Rewards as a percentage of spends



Source: RBI, Company, Ambit Capital research

Exhibit 60: Reward per card is high for SBI Cards after RBL Bank



Source: RBI, Company, Ambit Capital research

Questions for management

Are high rewards per card and rewards as a percentage of spends the key drivers for you to grow faster than your peers in recent times given that RBK which has highest reward points per card has grown fastest in the segment? Does it mean that competitors can take away market share from you offering higher reward points?

Valuation – Is the premium justifiable?

The valuation benchmarking for SBI Cards becomes difficult due to lack of strict comparable players (pure play listed credit card players). The credit card business comes under the normal operations for most of the banks. Therefore, we have taken example from US Credit card industry to benchmark the valuation.

American express Co., a leading credit card player in the US trades at ~4.6 FY20E PB, 156% premium to the expected valuation of SBI Cards despite having similar level of RoE. The premium can be justified by looking at the earnings growth of 41% in last two years for SBI Cards vs only 19% for American Express.

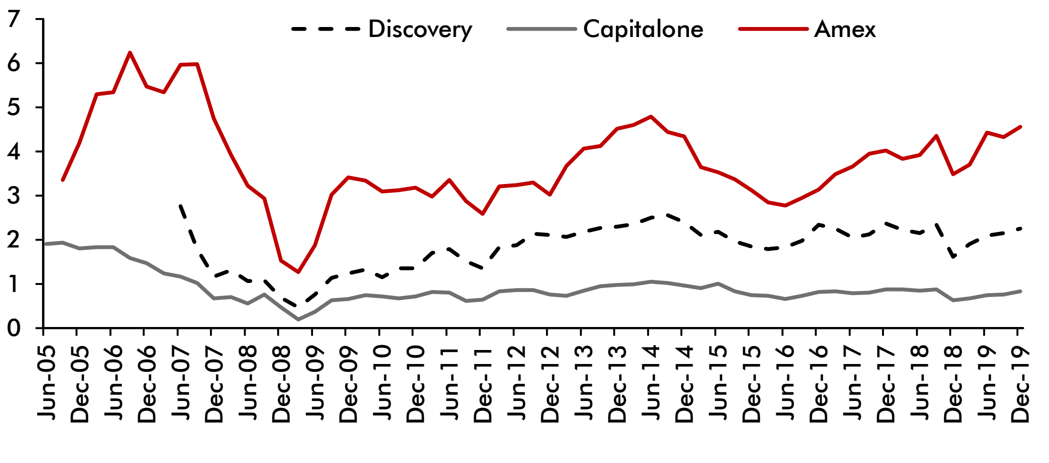
Exhibit 61: Speculated post money valuation is likely to be at ~83% premium to high RoE business due to expected higher growth

Company	Country	M-Cap (USDbn)	Forward P/E(x)		EPS growth	PEG (x)	Fwd P/B(x)		ROE (x)		ROA (x)	
			FY20E	FY21E	2-yr CAGR		FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Pure-play credit card business												
American Express Co	US	101.9	15.3	13.8	19%	0.74	4.6	4.1	30.4%	30.9%	3.4%	3.5%
Capital One Financial Corp.	US	47.9	9.0	8.6	31%	0.28	0.8	0.8	10.0%	9.3%	1.5%	1.4%
Discover Financial Services	US	26.8	9.4	8.9	16%	0.55	2.3	2.1	25.5%	25.3%	2.6%	2.5%
Average			**11.2**	**10.5**	**22%**	**0.52**	**2.6**	**2.3**	**22.0%**	**21.8%**	**2.5%**	**2.5%**
High ROE business in India												
HDFC Bank	India	100.2	26.6	21.6	17%	1.25	4.2	3.6	16.6%	18.0%	2.0%	2.0%
Bajaj Finance	India	35.2	41.5	31.0	41%	0.76	8.6	6.6	24.8%	24.9%	4.2%	4.5%
Bandhan Bank	India	11.4	23.2	20.9	27%	0.77	5.6	4.7	27.3%	24.5%	4.3%	3.3%
Aavas Financiers	India	2.1	56.4	45.4	49%	0.93	7.0	6.1	13.1%	14.1%	4.1%	3.9%
Average			**36.9**	**29.7**	**33%**	**0.93**	**6.4**	**5.2**	**20.4%**	**20.4%**	**3.6%**	**3.4%**
SBI Cards*	**India**	**9.2**	**45.1**	**NA**	**41%**	**NA**	**11.7**	**NA**	**31.6%**	**NA**	**NA**	**NA**

*Source: Bloomberg, Ambit Capital research *Net profit for FY20E is annualized. Networth/BVPS for FY20E are calculated by adding 1HFY20 PAT to 1HFY20 networth. For US Companies, the data refers to FY19E and FY20E. Our estimates for Bandhan Bank.*

Due to the relatively low growth experienced in the US Credit card industry, the credit card companies have never traded beyond ~6.2x one-year forward PB.

Exhibit 62: The US credit card companies have maximum traded at ~6.2x one-year forward PB since inception



Source: Bloomberg, Company, Ambit Capital research

The expected valuation of SBI Cards is also ~83% premium to average valuation of high growth and/or high RoE lenders like HDFC Bank, Bajaj Finance, Bandhan Bank, AU Finance and Aavas Financiers. However, unlike these other lenders, SBI Cards is a mono-line business with no optionality to get into other businesses given parent SBI's presence in other businesses. This lack of optionality means that the company is exposed to vagaries of credit card business compared to other lenders and hence RoE and growth should not be the only parameter to determine valuations.

Compared to some of these high-growth/high-RoE Indian lenders, SBI scores high on most parameters barring asset quality risk and concentration in a single business.

Exhibit 63: SBI Cards scores over high-growth/high-RoE lenders in most of the parameters

Metric	HDFC Bank	Bajaj Finance	Bandhan Bank	Aavas Financiers	SBI Cards
Growth Potential	◑	◑	◕	◕	◕
Cross Cycle ROE of core business	◑	◕	◑	◑	◕
Asset quality risk	◕	◑	◔	◑	◔
Diversified loan book	◕	◑	◔	◔	◔
Distribution Prowess	◕	◑	◔	◔	◕
Cost of funds	◕	◑	◑	◑	◑

Source: Company, Ambit Capital research Note: ● - Highest; ◕ - Relatively more; ◑ - Average; ◔ - Less

Annexures

Exhibit 64: SBI Cards - Board composition

Name	Age	Designation	Profile
Mr. Rajnish Kumar	61	Non-executive Chairman (Nominee of SBI)	Currently, he is the chairman of SBI. Earlier, he has also served as the MD in SBI, Chief general manager of the north-eastern circle of SBI and MD & CEO of SBICAP. He holds master's degree in physics from the Meerut University
Mr. Dinesh Kumar Khara	58	Non-executive (Nominee of SBI)	Currently, he is the MD of SBI. Earlier, he has also served as the MD & CEO of SBI Funds. He holds a bachelor's and a master's degree in commerce and a master's degree in business administration from the University of Delhi
Mr. Hardayal Prasad	59	Managing Director and Chief Executive Officer (Nominee of SBI)	He holds a master's degree in chemistry from Agra College. He is also a certified associate of Indian Institute of Bankers.
Mr. Shree Prakash Singh	59	Non-executive (Nominee of SBI)	Currently, he is the chief general manager in SBI, looking after non-banking domestic subsidiaries and regional rural banks. He holds a bachelor's and a master's degree in physics from Patna University. He is also an associate of Indian Institute of Bankers.
Mr. Sunil Kaul	59	Non-executive (Nominee of CA Rover)	Currently, he is the MD and head of the financial services industry of Carlyle Asia Partners and concurrently heads the south-east Asia business of the Carlyle Group. He holds a bachelor's degree in technology from IIT Bombay and a postgraduate diploma in management from the IIM, Bangalore.
Dr. Tejendra Mohan Bhasin	63	Independent Director	He holds a bachelor's degree in law and a master's degree in business administration from the University of Delhi. He is a doctor of philosophy from the Faculty of Management Sciences, University of Madras. He is also an associate of the Indian Institute of Bankers.
Mr. Nilesh Shivji Vikamsey	55	Independent Director	Currently, He is serving as a senior partner since 1985 at Khimji Kunverji & Co LLP. He holds a bachelor's degree in commerce from R. A. Podar College of Commerce & Economics, Mumbai University. He is a qualified chartered accountant from the Institute of Chartered Accountants of India and holds a post qualification course in information system audit.
Mr. Rajendra Kumar Saraf	65	Independent Director	He holds a bachelor's degree in science from Birla Institute of Technology and Science and a master's degree in science from IIT, Kanpur. He is an associate of the Indian Institute of Bankers and a fellow of Insurance Institute of India.
Mr. Dinesh Kumar Mehrotra	66	Independent Director	Earlier in his career, he has served as the chairman and the managing director of Life Insurance Corporation of India ("LIC"). He holds a bachelor's degree in science (honours) from the University of Patna.
Ms. Anuradha Shripad Nadkarni	57	Independent Director	Currently she is working with Svakarma Finance Private Limited as a founding member and the whole-time director. Earlier in her career, she has worked as head of financial institutions group at Standard Chartered Bank. She holds a bachelor's degree in commerce from the University of Poona. She holds a post-graduate diploma in management from IIM Bangalore and is a member of the Council of Chartered Financial Analysts.

Source: Company, Ambit Capital research

Exhibit 65: SBI Cards' top executives are from banking background

Name	DOJ	Designation	Profile
Mr. Richhpal Singh	01-Apr-18	Chief Operating Officer	Earlier in his career, he worked with Jio Payments Bank Limited and SBI. He holds a bachelor's degree in arts from Maharshi Dayanand University, Rohtak.
Mr. Nalin Negi	01-Dec-18	Executive Vice President, Chief Financial Officer	Earlier in his career, he worked with Nestle India Limited, American Express (India) Private Limited, exl Service.com (India) Private Limited and ITC Limited. He holds a bachelor's degree in commerce (honours course) from the University of Delhi. He is an associate of the Institute of Chartered Accountants of India.
Ms. Aparna Kuppuswamy	01-Apr-09	Executive Vice President and Chief Risk Officer	Earlier in her career, she worked with American Express Financial Advisors, Bank of America and ABN AMRO Bank. She holds a master's degree in finance and control from the University of Delhi.
Mr. Manish Dewan	01-Oct-11	Executive Vice President & Chief Sales Officer	Earlier in his career, he was associated with Standard Chartered Bank and American Express Bank Limited. He holds a bachelor's degree in engineering (mechanical) from Panjab University and a postgraduate diploma in management from Indian Institute of Management Society, Lucknow.
Mr. Girish Budhiraja	01-Nov-12	Executive Vice President and Chief Product and Marketing Officer	Earlier, he was associated with American Express Bank Limited, and ICI India Limited. He holds a bachelor's degree in technology in mining engineering from Indian School of Mines and a post-graduate diploma in management from the IIM, Bangalore.
Ms. Suruchi Nagpal	20-Jun-19	Executive Vice President and Head, Workforce Effectiveness	She holds a degree in master of arts (economics) from Panjab University.
Mr. Naresh Kumar Kapur	18-Sep-17	Executive Vice President and Chief People Officer	He holds a bachelor's degree in science from the Guru Nanak Dev University.
Mr. Rajendra Singh Chauhan	06-Jun-18	Executive Vice President and Head, Internal Audit	He is an associate of the Indian Institute of Bankers.
Ms. Rinku Sharma	01-Nov-12	Executive Vice President and Chief Compliance Officer	Earlier, she was associated with DCM Financial Services. She holds a bachelor's degree in science (honours) from the St. Stephen's College, University of Delhi and a postgraduate diploma in management from the International Management Institute, New Delhi.
Mr. Ugen Tashi Bhutia	02-Jan-12	Executive Vice President and Head, Legal	Earlier, he was associated with Lakshmikumaran & Sridharan Attorneys and Fox Mandal & Co. He holds a bachelor of law degree from the University of Delhi, New Delhi and a bachelor's degree in commerce (honours) from the University of North Bengal.
Mr. Amit Batra	01-Jan-11	Executive Vice President and Head, Operations	He holds a diploma in hotel management from National Council for Hotel Management and Catering Technology, Noida, and has received a certificate for completion of INSEAD leadership program for senior Indian executives from INSEAD.
Mr. Monish Vohra	01-Apr-18	Executive Vice President and Head, Customer Service	Earlier, he was associated with PNB MetLife India Insurance Company Limited. He holds a bachelor's degree in engineering (electrical) from the University of Delhi and a master's degree in business administration from the University of Delhi.
Mr. Pradeep Khurana	01-Apr-18	Executive Vice President and Chief Information Officer	Earlier, he was associated with IGE India Limited. He holds a bachelor's degree in engineering from the Punjab Technical University, Jalandhar and a diploma in advanced computing from Advanced Computer Training School, Pune.
Ms. Anu Choudhary Gupta	01-Apr-18	Executive Vice President and Head, Collections	Earlier, she was associated with Standard Chartered Bank, India. She holds a bachelor's degree in commerce from the University of Rajasthan, Jaipur and a post graduate diploma in management from Lal Bahadur Shastri Institute of Management, New Delhi.
Ms. Payal Mittal Chhabra	15-Feb-12	Senior Vice President, Company Secretarial	She is an associate of the Institute of Company Secretaries of India. She holds bachelor's degrees in commerce and laws from the University of Delhi. She holds a master's degree in laws from Kurukshetra University.

Source: Company, Ambit Capital research

Summary financials

Balance sheet

Year to March (₹ mn)	FY17	FY18	FY19	1HFY20
Net worth	14,488	23,531	35,817	43,099
Borrowings	77,295	104,148	124,537	161,810
Other Liabilities	15,866	29,182	42,042	39,682
Total Liabilities	**107,650**	**156,860**	**202,396**	**244,591**
Cash & Balances with RBI & Banks	2,829	4,727	7,768	4,927
Investments	0	0	15	15
Advances	99,829	140,455	179,087	222,795
Other Assets	4,992	11,678	15,527	16,855
Total Assets	**107,650**	**156,860**	**202,396**	**244,591**

Source: Company, Ambit Capital research

Income statement

Year to March (₹ mn)	FY17	FY18	FY19	1HFY20
Interest Income	18,882	27,600	35,757	22,116
Interest expenses	5,284	7,115	10,172	6,213
Net Interest Income	**13,597**	**20,485**	**25,585**	**15,902**
Total Non-Interest Income	15,829	26,102	37,111	24,656
Total Income	**29,426**	**46,587**	**62,696**	**40,559**
Total Operating Expenses	18,390	29,393	37,903	22,955
Employees expenses	953	1,931	3,904	2,103
Other Operating Expenses	17,437	27,462	33,999	20,852
Pre Provisioning Profits	**11,036**	**17,194**	**24,793**	**17,604**
Provisions	5,320	8,001	11,477	7,258
PBT	5,716	9,193	13,316	10,346
Tax	1,988	3,182	4,689	3,087
PAT	**3,729**	**6,011**	**8,627**	**7,259**

Source: Company, Ambit Capital research

Key ratios

Year to March	FY17	FY18	FY19	1HFY20
Cost/Income ratio (%)	62.5%	63.1%	60.5%	56.6%
Gross NPA (₹ mn)	2,409	4,125	4,529	5,378
Gross NPA (%)	2.34%	2.83%	2.44%	2.33%
Net NPA (₹ mn)	773	1,348	1,518	1,774
Net NPA (%)	0.76%	0.94%	0.83%	0.78%
Provision coverage (%)	67.9%	67.3%	66.5%	67.0%
Yield on loans (%)	7.4%	7.2%	8.1%	8.0%
Cost of funds	21.3%	22.2%	21.6%	21.3%
NIMs (%)	15.3%	16.5%	15.5%	15.3%
Tier-1 capital ratio (%)	11.3%	12.4%	14.7%	14.8%
CAR (%)	15.7%	18.3%	20.0%	19.0%

Source: Company, Ambit Capital research

Du-pont analysis

Year to March	FY17	FY18	FY19	1HFY20
NII / Assets (%)		15.5%	14.2%	14.2%
Other income / Assets (%)		19.7%	20.7%	22.1%
Total Income / Assets (%)		35.2%	34.9%	36.3%
Cost to Assets (%)		22.2%	21.1%	20.5%
PPP / Assets (%)		13.0%	13.8%	15.8%
Provisions / Assets (%)		6.0%	6.4%	6.5%
PBT / Assets (%)		7.0%	7.4%	9.3%
Tax Rate (%)		2.4%	2.6%	2.8%
RoA (%)		4.5%	4.80%	6.50%
Leverage		7.0	6.1	5.7
RoE (%)		31.6%	29.1%	36.8%

Source: Company, Ambit Capital research

Valuation*

Year to March	FY17	FY18	FY19	1HFY20
EPS - annualized (₹)	4.8	7.4	9.4	15.6
EPS growth (%)		56%	27%	85%
BVPS (₹)	18.5	29.8	39.9	47.0
P/E (x)	146.8	94.2	73.9	44.7
P/B (x)	37.8	23.4	17.5	14.8

*Source: Company, Ambit Capital research; *Assuming an issue price of Rs697*

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Explanation of Investment Rating

Investment Rating	Expected return (over 12-month)
BUY	>10%
SELL	≤10%
NO STANCE	We have forward looking estimates for the stock but we refrain from assigning valuation and recommendation
UNDER REVIEW	We will revisit our recommendation, valuation and estimates on the stock following recent events
NOT RATED	We do not have any forward looking estimates, valuation or recommendation for the stock
POSITIVE	We have a positive view on the sector and most of stocks under our coverage in the sector are BUYs
NEGATIVE	We have a negative view on the sector and most of stocks under our coverage in the sector are SELLs

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AMBIT
Acumen at work

Questions for management

On Indian credit card industry

- Our back-of-the-envelope calculations (assuming credit card/debit card ratio improving by 70bps every year) show ~21% CAGR outstanding credit cards in India. What according to you is the potential size of Indian credit card market and hence what should be the expected growth rate of the industry for next 5 years?
- The share of digital transaction in volume terms is increasing in the system (from 42% in 1QFY17 to 67% in 1QFY20). Do you expect the trend to sustain going forward? What can be the steady state mix of physical and digital transactions after 5 years down the line?
- If we look at the composition of digital transaction over the years, the share of debit products (UPI, PPI and debit cards) have gone up due to the advent of UPI at the expense of credit card products. The share of credit card in volume/value terms have come down to 20%/44% in FY17 to 10%/21% in 1HFY20. Do you think this falling share of credit cards due to arrival of UPI will impact your business materially?
- After growing at a CAGR of 23% over FY15-18, per card spend seems to have stagnated between FY18 and 1HFY20 for SBI. Similar trends have been observed at the industry level where per card spends have stagnated in recent times. What's the reason behind stagnating per card spends? Is it because of incremental growth in cards coming from younger customers/Tier-3-4 cities where spending power is lower? What should be sustainable per card spend growth going forward?
- Credit card loans in India compete with personal loans in India which is visible in credit card loans being just ~4% of total unsecured loans in India. Is there a possibility that with increasing credit card limits/EMI options on large purchases, credit card loans can replace unsecured personal loans in India? Are you seeing any changing consumer preference in this regard?

On SBI Cards growth

- What percentage of SBI liability-side customer base could be penetrated for credit cards? What are the strategies the company is employing to penetrate deeper into SBI customer base?
- Co-branded credit cards have been another area of high growth for SBI Cards where new origination of co-branded credit cards has growth at a CAGR of 70% over FY17-1HFY20 with share of co-branded credit cards in new originations increasing from 28% in FY17 to 36% in 1HFY20. What are the key factors which attract companies like Ola, Air India, BPCL, Yatra, etc. to tie up with you rather than your competitors? How easy it is for your co-branded partners to switch to your competitors?

On SBI Card's assets/labilities

- What is the rationale behind lower loans per card and lower loans as percentage of transactions? Is it a conscious strategy to be cautious on offering EMI conversions and/or minimizing rollovers or better quality of customers is leading to lower rollover rate and lower EMI conversion?
- Does the company have any plans to increase EMI-based loans/revolvers and what is the strategy to execute this without taking too much balance sheet risk?
- What is the reason behind changing liability mix towards debt securities compared to bank borrowings given that it is relatively difficult to get money from bond market than from banks post-liquidity crisis?
- DRHP shows that your borrowing cost from your parent SBI at ~7.80% is lower compared to other banks at ~8.30% with ~87% of the bank borrowings coming from SBI in 1HFY20. Back-of-the-envelope calculations show that if replacing borrowing from the SBI to other banks could impact your RoA by ~15-20bps. Do you get preferential rates from SBI on your borrowings? How much is the headroom to borrow more from SBI?

On Fee Income

- What is the probability of MDR/Interchange charges being brought down on credit cards and what impact it would have on financials of the company if the MDR/Interchange is brought down?
- With charges on other modes of payments being lower for merchants, why can't merchants incentivize customers to pay through other digital modes?
- What is driving per higher growth in instance-based fee growth? With improving payment infrastructure, can it lead to timely payments resulting in decrease in this fee line item?
- Why fee income as percentage of spends is low for SBI Cards at ~3% vs ~4% for others? Why this number has remained stagnant at ~3% since FY17?

On operational efficiency

- Data suggest that most of the expense items are broadly variable in nature moving broadly in line with net income and loan book. How much more scope is left for further improvement in cost to income/cost to average loan book ratio?
- Are high rewards per card and rewards as percentage of spends key drivers for you to grow faster than your peers in recent times given that RBK which has highest reward points per card has grown fastest in the segment? Does it mean that competitors can take away market share from you offering higher reward points?

On Asset quality

- How should we read the jump in both absolute NPAs and write-offs in 1HFY20? How has been the asset quality trend on a static pool basis as gross NPA ratio could be misleading in a high growth company?
- The write-off in 1HFY20 has increased to 166% of opening GNPA from 68% in FY19. As per DRHP, this is due to the stress in one corporate account which resulted in write-off of ₹921mn. What went wrong here? What is the current status of the account? Are there anymore accounts which might slip into stress going forward?
- Data shows that share of new accounts opened in non-metros and share of self-employed cardholders is inching up for you. Don't you think that the change in profile of the customer should lead to higher NPAs/credit cost for you going forward vs historical trends?
- In overall credit card industry, there is an increase in share of younger people (<30 years) in originations. However, evidence from US Credit card industry shows that 90+ dpd delinquencies are the highest for the younger population across cycles. Don't you think that the change in demographic profile of the customer should lead to higher NPAs/credit cost for you and industry as whole?
- As per our analysis, consumer credit as a percentage of nominal GDP has increased from 14% in FY15 to 17% in FY19. There were huge losses for banking industry in credit card/personal loan portfolios in FY109-10 post Lehman crisis when consumer leverage was just 50% vs current levels. With higher consumer leverage compared to the past amidst slowing economy and slowing job growth/salary hikes, what comfort can you provide on future asset quality trends of the company?
- If we look at the credit cost in US credit card market, the credit cost has gone as high as ~11% during 2009. The credit cost is highly inversely correlated with GDP per capita and employment generation. As the Indian credit card market gets matured, the same kind of pattern observation cannot be entirely ruled out. Given the current slowdown in economy and its adverse impact on employment generation, don't you think the delinquency levels may increase in coming years?