MORNING INSIGHT

kotak Kotak Securities

PRIVATE CLIENT RESEARCH

FEBRUARY 22, 2011

Economy News

- The government is likely to announce in the Budget a timeline for allowing 51 per cent foreign direct investment (FDI) in multi-brand retail. To show the government's commitment to reforms, Finance Minister Pranab Mukherjee may make an announcement as a major reform process on March 16 and give the proposal a fresh lease of life to build investors' confidence. (BS)
- The Gross Budgetary Support (GBS) for 2012-13 may touch Rs 5.2 lakh crore, with an increase of more than 18 per cent over the current fiscal year. This includes both Central assistance to the States and allocation to various Central Ministries. (BL)
- Consumer Price Index (CPI)-based inflation, announced for the first time on Tuesday, stood at 7.65 per cent in January year on year. The rate of price rise was a bit higher in urban areas (8.25 per cent) than in rural (7.38 per cent). (BS)
- After the prime minister's office (PMO) nudged Coal India Ltd to meet the coal requirement of power plants, heads of India's most powerful corporates have shifted their focus to modalities.At its first follow-up meeting with the committee of secretaries (CoS) headed by Prime Minister Manmohan Singh's Principal Secretary Pulok Chatterjee, a delegation of tycoons is going to push for price pooling of imported coal. (BS)

Corporate News

- **Sesa Goa** is set to merge with Sterlite industries, creating a Rs 400 bn metals giant. As part of the grand restructuring initiated by Anil Agarwal, even Cairn India may get realigned with the new entity. According to independent sources aware of the ongoing plan, a share swap in the ratio of 2:3 is being talked about. (BS)
- **GTL Infra** may get about Rs 10 bn from Aircel since it will not be able to deliver on its promise to rent 20,000 additional towers by mid-2013. (ET)
- **Lanco Infratech** is known to be in talks with international energy majors like AES of United States and Gaz de France to sell a part of its power business. The company had recently said it planned to sell a minority stake in its power business and raise $600-$750 million (Rs 29.40- Rs 36.75 bn). (BS)
- **Reliance Industries (RIL)** and Russian rubber giant Sibur, Eastern Europe's largest maker of petrochemicals, announced the formation of a joint venture company called Reliance Sibur Elastomers that aims to become the fourth largest supplier of butyl rubber - an input for tyres - in the world. "In the first year of production the company could target a turnover of 25 bn. (ET)
- **Tata Motors** will double investments in its Jaguar Land Rover brands to pound 1.5 billion a year, even as it warned that it will be a challenge to sustain high margins at its key profit generator. (BS)
- Debt-crippled **Kingfisher Airlines** said it had allotted equity shares against optionally convertible debentures (OCDs), a development that would help the country's third-biggest carrier by market share save interest outflow on such instruments. (BS)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

Equity

		% Chg		
	21 Feb 12	1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	18,429	0.8	10.1	12.6
NIFTY Index	5,607	0.8	11.1	14.3
BANKEX Index	12,839	0.8	17.7	26.4
BSET Index	6,257	(0.2)	13.8	11.4
BSETCG INDEX	11,204	0.9	14.2	17.3
BSEOIL INDEX	8,842	2.3	6.2	6.5
CNXMcap Index	7,981	0.7	17.3	20.2
BSESMCAP INDEX	7,202	1.2	14.7	16.5
World Indices				
Dow Jones	12,966	0.1	1.9	9.9
Nasdaq	2,949	(0.1)	5.8	14.6
FTSE	5,928	(0.3)	3.5	13.5
NIKKEI	9,463	(0.2)	8.1	14.0
HANGSENG	21,479	0.3	6.2	17.0

Value traded (Rs cr)

	21 Feb 12	% Chg - Day
Cash BSE	3,429	(21.1)
Cash NSE	15,880	(23.3)
Derivatives	153,479	(15.1)

Net inflows (Rs cr)

	17 Feb 12	% Chg	MTD	YTD
FII	595	(72.8)	13,817	24,906
Mutual Fund	(14)	(96.7)	(1,344)	(3,191)

FII open interest (Rs cr)

	17 Feb 12	% Chg
FII Index Futures	17,252	2.3
FII Index Options	48,927	6.7
FII Stock Futures	32,911	(0.7)
FII Stock Options	1,898	1.0

Advances / Declines (BSE)

21 Feb 12	A	B	T	Total	% total
Advances	135	1,163	376	1,674	54
Declines	69	903	328	1,300	42
Unchanged	1	69	41	111	4

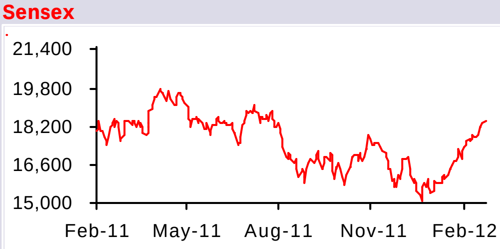
Commodity

		% Chg		
	21 Feb 12	1 Day	1 Mth	3 Mths
Crude (NYMEX) (US$/BBL)	105.8	(0.4)	7.5	8.0
Gold (US$/OZ)	1,752.0	1.0	5.5	3.1
Silver (US$/OZ)	34.1	1.7	8.5	3.8

Debt / forex market

	21 Feb 12	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	8.17	8.19	8.18	8.84
Re/US$	49.2	49.3	50.1	52.1

Sensex



COMPANY UPDATE

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STATE BANK OF INDIA (SBI)

PRICE: RS.2451 **RECOMMENDATION: ACCUMULATE**
TARGET PRICE: RS.2381 **FY13E P/E: 11.9X; P/ABV: 2.7X**

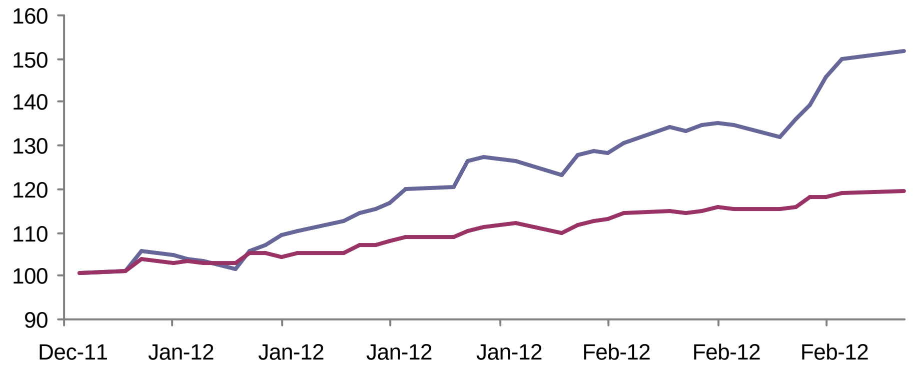
Too fast too quick; stock has risen ~15% during last one week, belying the risk associated with its asset quality. Downgrade to ACCUMULATE from BUY earlier...

- **SBI has moved up sharply during last one week (15.2%) as against 3.7% rise in Sensex, despite unsatisfactory performance on the asset quality. Even YTD (CY12), SBI has outperformed the benchmark Sensex by 32% on back of expectations of some monetary easing by the RBI. This has happened despite the biggest disappointment on the slippage front (Rs.81.6 bn; 4.2% on annualized basis) which continued to remain at elevated levels - run rate at 4%+ during last two quarters, is clearly negative in our view.**
- **Management had earlier indicated that worst is over but the health of SMEs and mid-corporate book is more likely to be dependent on the overall economic recovery. On agri book, management has enthused confidence with the recovery done during last one and half months; they also indicated that NPA has peaked for this segment. However, we believe NPA in agri segment is higher (9.5% at the end of Q3FY12) due to moral hazards as farmers are delaying the payments with an expectation that they might get another Debt waiver scheme of 2008 kind.**
- **New management can clearly pat their back for consistently delivering robust NIM during last couple of quarters. NIM of the bank bottomed out in Q1FY10 and since then it has been witnessing consistent improvement. It has improved to 4.05% in Q3FY12 as against 3.62% in Q1FY12 and 3.79% in Q2FY12. Its ~9% loan book is under stress (gross NPA: 4.6%; restructured book: 4.3%) which could be the potential risk, going forward.**
- **Bank has received a notification from the GOI to infuse capital worth Rs.79 bn during FY12. This is definitely positive for the stock, as it was one of the reasons for its recent downgrade, by one of the rating agency. Management has guided that this would lead to improvement in its Tier-I capital from 7.59% at the end of Q3FY12 to ~9% at the end of FY12 with ploughing back of 12M profits along with this capital infusion.**
- **At the CMP of Rs.2451, stock is trading at 1.7x its FY13E adjusted book value and 7.5x its FY13E earnings, after stripping the value of its subsidiaries. We maintain our earnings estimate for FY12-13E but downgrade the stock to ACCUMULATE from BUY earlier with unchanged TP of Rs.2391, as stock has witnessed sharp run-up (~15%) during last one week, belying the risk associated with its asset quality.**

Stock had a sharp run-up during last one week (~15%), belying the risk associated with its asset quality

SBI has moved up sharply during last one week (15.2%) as against 3.7% rise in Sensex, despite unsatisfactory performance on the asset quality. Even YTD (CY12), SBI has outperformed the benchmark Sensex by 32% on back of expectations of some monetary easing by the RBI.

SBI performance vis-à-vis SENSEX



Source: Company

This has happened despite the biggest disappointment on the slippage front (Rs.81.6 bn; 4.2% on annualized basis) which continued to remain at elevated levels - run rate at 4%+ during last two quarters, is clearly negative in our view.

In absolute terms, bank's gross and net NPAs rose 18.1% and 16.6%, respectively. Management had indicated that sectors like aviation, metals, sugar and companies which are dependent on state utilities have contributed to this kind of rise in NPA. Slippages were higher in SMEs and Mid-corporate segments.

NPA Movement

(Rs bn)	Q3FY12	Q2FY12	Q1FY12	FY11
Opening Balance	339.5	277.7	253.3	195.4
Slippage	81.6	80.2	61.8	181.5
Reduction	20.1	18.4	37.4	123.5
Upgradation + Cash Recovery	19.7	17.7	30.8	83.5
Write Off	0.4	0.7	6.6	40.1
Closing NPA	**401.0**	**339.5**	**277.7**	**253.3**
Inc in GNPA	61.5	61.8	24.4	57.9
Slippage ratio (%)	**4.23**	**4.15**	**3.20**	**2.83**

Source: Company

Slippage

(Rs. bn)	Q3FY12	Q2FY12
Corporate	39.5	24.5
International	6.1	1.4
SMEs	20.8	22.4
Agriculture	11.3	20.1
Retail	4.0	11.7
Total slippage	**81.6**	**80.2**

Source: Company

Management had earlier indicated that worst is over but the health of SMEs and mid-corporate book is more likely to be dependent on the overall economic recovery. On agri book, management has enthused confidence with the recovery done during last one and half months; they also indicated that NPA has peaked for this segment.

However, we believe NPA in agri segment is higher (9.5% at the end of Q3FY12) due to moral hazards as farmers are delaying the payments with an expectation that they might get another Debt waiver scheme of 2008 kind.

Robust NIM on back conscious strategy; however, ~9% of loan book under stress could be the potential risk

New management can clearly pat their back for consistently delivering robust NIM during last couple of quarters. NIM of the bank bottomed out in Q1FY10 and since then it has been witnessing consistent improvement. It has improved to 4.05% in Q3FY12 as against 3.62% in Q1FY12 and 3.79% in Q2FY12. We believe strong NIM provides some kind of cushion to absorb its current high credit costs. We are conservative enough to model NIM at 3.75% during FY12E (3.82% during 9MFY12) and 3.45% during FY13E.

Its ~9% loan book is under stress (gross NPA: 4.6%; restructured book: 4.3%) which could be the potential risk, going forward. During Q3FY12, bank restructured accounts worth Rs.21.9 bn, taking total cumulative restructured book to Rs.376.1 bn (4.3% of advances). Till date, Rs.96.8 bn has slipped into NPA, constituting 25.7% of total restructured account. Its PCR also dropped to 62.5% at the end of Q3FY12 as compared to 63.5% in the previous quarter, negative in terms of balance sheet quality.

Moderation in business growth continues; new management has been focusing more on profitable growth rather than earlier strategy of gaining market share, even if it involves at some margin sacrifice.

SBI has delivered sub-20% loan growth during last three quarters, which indicates moderation in overall business growth. This is in line with the new management's strategy which has a focus on margins as against earlier strategy of garnering market share, even if it came at some margin sacrifice.

We have modeled balance sheet growth at 14.2% CAGR during FY11-13E. We are also maintaining our loan growth assumption of ~16% (11.8% YTD) during FY12E and ~17% during FY13E.

On liability side, bank has a conscious strategy of reducing dependence on bulk deposits. Its CASA mix has remained healthy at 47.5% at the end of Q3FY12; however, in case of a competitive rise in interest rates on SB deposits, it could negatively impact its NIM.

Government infusion of Rs.79 bn; management guided Tier-I capital to improve to ~9% with ploughing back of 12M profits along with this capital infusion

Bank has received a notification from the GOI to infuse capital worth Rs.79 bn during FY12. This is definitely positive for the stock, as it was one of the reasons for its recent downgrade, by one of the rating agency.

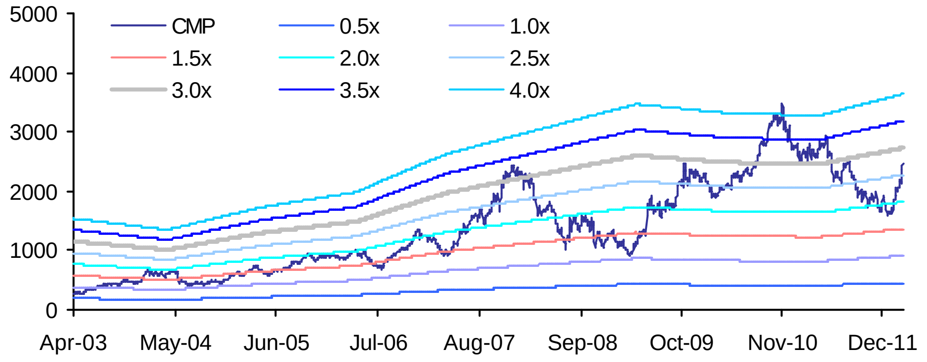
Management has guided that this would lead to improvement in its Tier-I capital from 7.59% at the end of Q3FY12 to ~9% at the end of FY12 with ploughing back of 12M profits along with this capital infusion.

Valuation & Recommendation

At the CMP of Rs.2451, stock is trading at 1.7x its FY13E adjusted book value and 7.5x its FY13E earnings, after stripping the value of its subsidiaries. We maintain our earnings estimate for FY12-13E but downgrade the stock to **ACCUMULATE** from BUY earlier as stock has witnessed sharp run-up (~15%) during last one week, belying the risk associated with its asset quality.

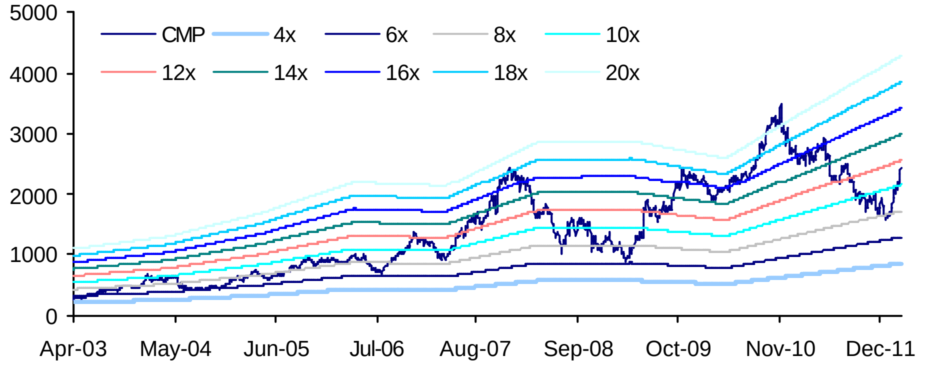
We expect net profit for FY12E and FY13E to be Rs.110.7 bn and 131.3 bn, respectively. This would result into an EPS of Rs.174.4 and Rs.206.8 for FY12E and FY13E, respectively. Adjusted book value is estimated to be at Rs.819.8 and Rs.922.2, respectively.

Rolling 1-year forward P/ABV band



Source: Company, Kotak Securities - Private Client Research

Rolling 1-year forward P/E band



Source: Company, Kotak Securities - Private Client Research

We recommend ACCUMULATE on SBI with a price target of Rs.2381

Our fair value estimate is based on SOTP methodology where core business is valued at Rs.1476 (1.6x FY13E ABV) and subsidiaries are valued at Rs.905 (after giving 20% holding company discount). We advise our clients to **ACCUMULATE** this stock with every decline...

Sum of Parts Valuation

	Basis	Multiple	Year	Value/Share
Core Banking Business (standalone)	ABV	1.60	FY13	1,476
Associate Banks	ABV	1.50	FY13	727
Life Insurance Business	NBAP	15	FY13	246
SBI Capital Market	P/E	10	FY13	68
Asset Management	AUM	5%	FY13	26
SBI DFHI	P/E	6	FY13	14
SBI Factors	P/E	10	FY13	9
SBI Cards & Payment services	P/E	10	FY13	3
Other Investments (UTI MF, NSE, GTF etc)				
Total Value of subsidiaries				**1,131**
After 20% Holding company discount				905
Total Value				**2,381**

Source: Kotak Securities - Private Client Research

Key data

Key data, Rs bn	2010	2011	2012E	2013E
Interest income	709.9	813.9	1,069.5	1,203.3
Interest expense	473.2	488.7	641.4	755.6
Net interest income	**236.7**	**325.3**	**428.1**	**447.7**
Growth (%)	13.4%	37.4%	31.6%	4.6%
Other income	149.7	158.2	129.3	169.9
Gross profit	183.2	253.4	300.1	323.5
Net profit	**91.7**	**82.6**	**110.7**	**131.3**
Growth (%)	0.5%	-9.8%	34.0%	18.6%
Gross NPA (%)	3.1	3.3	4.6	4.8
Net NPA (%)	1.7	1.6	2.4	2.4
Net interest margin (%)	2.7	3.3	3.8	3.4
CAR (%)	13.4	12.0	12.5	12.5
RoE (%)	14.8	12.6	16.0	16.7
RoAA (%)	0.9	0.7	0.8	0.9
Dividend per share (Rs)	30.0	30.0	35.0	40.0
EPS (Rs)	**144.4**	**130.2**	**174.4**	**206.8**
Adjusted BVPS (Rs)	**867.5**	**829.0**	**819.8**	**922.5**
P/E (x)	**17.0**	**18.8**	**14.1**	**11.9**
P/ABV (x)	2.8	3.0	3.0	2.7

Source: Company, Kotak Securities - Private Client Research

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
21-Feb	Agarwal Hold	Vikas Malu	S	100,000	204.0
21-Feb	Dr Agarwals-$	Forrester Securities Pvt Ltd	S	28,267	141.0
21-Feb	Emporis	Aashish Developer	B	142,440	59.5
21-Feb	Emporis	Raajratna Stockholdings Pvt Ltd	S	99,191	59.6
21-Feb	Eveready Inds	American Funds Insurance Series-Global Capitalizat	S	510,793	27.9
21-Feb	GATI	Sura Securities Pvt Ltd	B	771,000	41.6
21-Feb	GFLFIN	Nutshell Commercial Pvt. Ltd.	B	58,570	36.0
21-Feb	GFLFIN	Purotech Merchants Pvt Ltd	B	69,000	36.0
21-Feb	GFLFIN	Rajnee Rajan Gitaye	S	76,000	36.0
21-Feb	GFLFIN	Sonal International Ltd	S	50,000	36.0
21-Feb	GK Consultants	Preeti Agrawal	B	43,001	15.3
21-Feb	GK Consultants	Usha Agarwal	S	45,000	15.3
21-Feb	Golden Tob	Lend Lease Company India Ltd	B	120,000	40.4
21-Feb	Golden Tob	Man Mohan Damani	S	102,137	40.4
21-Feb	Kadamb Constr	Aurangabad Auto Ancilliary Pvt Ltd	B	150,000	10.4
21-Feb	Karma Ind	Moonstar Securities Trading & Fin	B	250,199	57.6
21-Feb	KIC Metaliks	Maryada Barter Pvt Ltd	B	154,513	150.0
21-Feb	KIC Metaliks	Manphool Exports Ltd	S	67,057	150.0
21-Feb	KIC Metaliks	Amrabathi Investra Pvt Ltd	S	47,706	150.0
21-Feb	Krishna Deep	Hotel Polo Towers Pvt Ltd	S	33,855	44.6
21-Feb	Krishna Deep	Money Managers	S	19,505	44.6
21-Feb	Marsons	Elcon Investment	B	212,890	11.9
21-Feb	Pasupati Fin	Rohnil Boradia	B	40,006	36.1
21-Feb	Pasupati Fin	Paresh Ramjibhai Chauhan	S	25,000	36.1
21-Feb	PFL Infotech	Majestic Bottlers P Ltd	B	100,000	36.8
21-Feb	PFL Infotech	Vasanthi Kavur	B	50,000	37.7
21-Feb	PFL Infotech	Sushila Kavur	B	100,000	37.8
21-Feb	PFL Infotech	Rakesh Kumar Chordia	B	39,814	37.5
21-Feb	PFL Infotech	Animesh Kanjibhai Patel	S	93,690	35.8
21-Feb	PFL Infotech	Swarn Projects Ltd	S	40,000	37.8
21-Feb	PFL Infotech	High Value Traders Pvt Ltd	S	60,000	37.8
21-Feb	PFL Infotech	P.R.B.Securities Pvt Ltd	S	60,000	37.8
21-Feb	PFL Infotech	Narayan Tatu Rane	S	46,733	34.3
21-Feb	PFL Infotech	Silver Cross Marketing Pvt. Ltd.	S	40,000	37.8
21-Feb	PG Foils	Inventure Growth & Securities Ltd.	B	131,400	101.5
21-Feb	PG Foils	Inventure Finance Pvt Ltd	S	131,400	101.5
21-Feb	Punjab Comm-$	Aristro Capital Markets Pvt Ltd	S	200,000	199.8
21-Feb	Rander Corp	Sarla Bafna	S	100,000	149.6
21-Feb	Rander Corp	Vimal Kumar Motilal Somani	S	65,000	149.9
21-Feb	Ranklin Sol-$	O Markandeyulu	S	37,751	10.9
21-Feb	Ravinay Trad	Neora Consulting Pvt Ltd	B	35,000	205.7
21-Feb	Raymed Labs	Fastcon Infrastructure Pvt Ltd	B	38,605	25.6
21-Feb	Sanghvi Forging	Jignesh Vaghjibhai Shah	B	81,034	42.5
21-Feb	Sanghvi Forging	Sagar Rajeshbhai Jhaveri	B	203,318	37.9
21-Feb	Scope Ind	Amit S Soni	S	58,334	10.8
21-Feb	Setco Auto	Morgan Stanley Asia (Singapore) Pte	B	300,000	174.0
21-Feb	Shalibhadra Fin	Jigneshkumar Harshvadan Gandhi	B	25,000	62.1
21-Feb	Unisys Soft	Esha Securities Ltd	S	137,363	155.0
21-Feb	Varun Inds	Swati Rajesh Shah	B	150,000	265.1
21-Feb	Westlife Dev	Piyush Prafulchandra Avlani	B	775,000	42.9
21-Feb	Westlife Dev	Decent Enterprises	S	775,000	42.9

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
Reliance Ind	844	3.1	14.1	8.3
ONGC	292	3.8	4.7	6.6
BHEL	318	4.8	3.8	10.8
Losers				
Sterlite Ind	128	(3.6)	(2.2)	17.0
Tata Power	116	(2.7)	(1.7)	7.6
Tata Motors	271	(1.0)	(1.5)	18.3

Source: Bloomberg

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