

SBI reports lower bad loans and slippages, but sustainability will be key

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The trend in slippages and core net interest income has been bumpy over the past year

At a time when concerns over the stability and risks in the banking system have intensified, SBI---the country's largest bank---checking nearly all boxes on key performance metrics in the latest September quarter--- is sure to calm ruffled nerves. But whether the performance justifies the exuberance in the market---the stock rallied by a tidy 7 per cent post the results ---is another matter.

True, SBI has reported a sharp fall in slippages in the September quarter, decrease in SMA (special mention accounts) book and significant improvement in core net interest income. But given that trend in these metrics have been bumpy over the past year, how far the bank is able to sustain the performance in

the coming quarters, will be critical. Importantly, even if fresh slippages continue to moderate, the stock of bad loan problem needs to be addressed quickly, if lenders such as SBI have to see significant improvement in earnings.

Despite the reduction in the September quarter, SBI's bad loan book is still a large Rs 1.61 lakh crore. SBI has about ₹25,000 crore exposure to accounts under the RBI's first and second list (referred to IBC). The bank has made ₹22,399 crore or 89.6 per cent provisioning against them. The bank's exposure to all cases under NCLT (including cases beyond the two lists) is over ₹1.16 lakh crore. Unlocking of capital by way of write-backs will be critical to ramp up credit growth.

SBI has also not moved to the new corporate tax rate regime. Hence the deferred tax asset (DTA) adjustment is pending, which can impact earnings in the coming quarters.

Why the exuberance

For SBI, after it reported steep slippages of Rs 33,670 crore in the March 2018 quarter, quarterly additions to bad loans have been under focus. While slippages had moderated in FY19—from about Rs 10,000 crore quarterly slippages in the first half to Rs 4,000-7,000 crore in the second half----they had shot up again to Rs 16,212 crore in the previous June quarter.

In the September quarter, slippages have nearly halved to Rs 8,805 crore, which is comforting. As a result, bad loan book has declined to Rs 1.61 lakh crore from Rs 1.68 lakh crore in the June quarter.

The other key concern in the June quarter was the sharp rise SBI's SMA1 (where payments are overdue by 31-60 days) and SMA2 (overdue by 61-90 days) book-- to Rs 10,289 crore in the June quarter from Rs 7,762 crore in the March quarter. The SMA1 and SMA 2 book has declined to Rs 9,312 crore in the latest September quarter, which is also a positive trend.

Aside from improvement in asset quality, SBI's core performance has also picked up significantly in the September quarter, beating most expectations. After a subdued 5 per cent growth in core net interest income (NII), the bank delivered a strong 17.7 per cent growth in NII in the September quarter, cheering the market.

What needs a watch?

While sharp fall in slippages is a key positive, it needs to be seen if the trend continues. In the past 4-6 quarters, slippages have fallen and risen sharply, making it difficult to gauge the broad trend. For instance, after slippages fell sharply to about Rs 4,500 crore in the December 2018 quarter (from Rs 10,700 crore in the June 2018 quarter), they had again spiked to Rs 16,000 crore levels in the previous June quarter. Given the persisting unfavourable credit risk environment, spikes in slippages in the ensuing quarters cannot be ruled out.

Also, after the one-off recovery in the June quarter last year, recoveries have not been significant. Much of the reduction in bad loans has come from write-offs in the past few quarters. In the September quarter too write-offs stood at a substantial Rs 12,000 crore (reduction in bad loans less recovery). Write-offs mean that banks fully provide for bad loans (taking a knock on profits) and take them off the books.

While SBI's SMA book has reduced in the September quarter, at a little over Rs 9,300 crore it is still a significant amount. Also, post RBI's June circular (revised framework for resolution of stressed accounts), in 15 standard accounts of SBI, inter-creditor agreement (ICA) has been signed or likely to be signed. On a default, banks have to decide on the resolution plan, which requires all lenders to enter into an ICA. These accounts amount to Rs 16,822 crore and carry about 13 per cent provision. A substantial stressed assets pool leaves open the possibility of notable slippages.

SBI has Rs 35,735 crore exposure to the telecom sector as of September 2019. The Supreme Court's recent verdict on adjusted gross revenue, is expected to hurt telecom operators and their debt repayment ability. How this impacts banks

such as SBI needs to be seen.

NII rise, a positive

On the core business front, while the notable rise in NII in the September quarter is a positive, how far the bank is able to maintain its net interest margin (NIM)--- post the launch of repo-linked loans----needs to be seen. While increase in yields and fall in cost of deposits has aided NIM this time around, the notable pick up in NII has also been due to lower interest reversal in the September quarter. In the September quarter last year, the bank had seen slippages rise sharply owing to which NII growth was subdued.

As such SBI's domestic loan growth of 8 per cent in the September quarter lags that of leading private banks. HDFC Bank's domestic loans grew by 20 per cent in the latest September quarter. However, SBI's retail loan growth was a healthy 19 per cent, led by home loans.

Finally, for SBI's earnings to see a significant jump, provisions will have to moderate substantially. SBI's provisioning for bad loans remained elevated at Rs 11,000 crore in the September quarter, owing to its large bad loan book. Unless there is sharp decline in bad loans, led by recoveries (rather than write-offs), earnings may not see a sustainable revival.

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