Business Standard

SBI Cards good bet, ticks right boxes

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SBI Cards good bet, ticks right boxes

Stellar returns, growth profile pack a punch; improving asset quality will be key

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Following robust returns by SBI Life Insurance within three years of its listing, the market is quite positive on SBI Cards and Payment Services (SBI Cards). Strong fundamentals, a healthy growth potential, and an attractive return profile makes the IPO —opening on March 2 — a good bet despite its premium valuation.

At 45-46x price-to-earnings and 15x price-to-book value (based on annualised numbers of April-December 2019), the valuation is way higher than global credit card peers and at a premium to domestic well-established lenders.

Rohan Mandora, vice-president at Equirus Securities, however, says: "SBI Cards' unique business model, strong growth visibility and healthy return ratios justify the premium valuation." Analysts at Narnolia Financial Advisors, who have 'subscribe' rating, believe SBI Cards' higher earnings growth as compared to global peers should command a higher premium.

SBI Cards has an 18 per cent market share in terms of outstanding number of cards, as of November 2019 (second to HDFC Bank at 27 per cent). Its strong 27 per cent CAGR or compound annual growth rate in credit cards from FY15-19 has helped it clock a 300-basis-point increase in market share.

Strong traction in total credit card spends, higher sourcing of customers from its parent (SBI), and cost efficiency (cost-to-income ratio declined by 204 bps over FY17-19) have helped drive up its financials. Total operating income and earnings expanded at a CAGR of 41-45 per cent during FY17-19 and by 35 per cent and 84 per cent year-on-year, respectively, in 9MFY20.

During 9MFY20, revenue from operations stood at ₹6,843 crore (up 35 per cent YoY), a tad lower than ₹6,999 crore for the entire FY19, and profit before tax at ₹1,619 crore (up 71 per cent YoY), visibly higher than FY19's ₹1,332 crore. Over two years, return on assets rose 80 bps to 5 per cent in FY19.

The trend of strong growth and healthy return ratios is expected to continue. Lower card penetration (3-4 cards per 100 people in India versus over 30 per 100 people in developed countries), expected sturdy retail credit growth, and digitation augur well for the credit card industry.

HOUSE OF CARDS

	Return on assets (%)	2-yr loans CAGR (%)**	2-yr earnings CAGR (%)**	Price to book (x)	Price to earnings (x)
American Express (US)	3.5	10.0	17.7	4.1	13.4
Capital One Financial Corp (US)	1.3	2.1	22.6	0.7	7.8
HDFC Bank	2.0	22.0	18.1	3.9	24.4
Bajaj Finance	4.2	41.9	42.9	9.0	47.3
SBI Cards*	6.9	33.9	40.9	15.0	45-46

CAGR: Compound annual growth rate; Return on assets, price-to-book, and price-to-earnings are FY20 estimates; *For SBI Cards, numbers as of April-December 2019; profit after tax is annualised
** For FY17-19
Source: Bloomberg, brokerage reports, companies, BS Research Bureau

Credit Card spends, which witnessed a CAGR of 32 per cent over FY15-19 to ₹6 trillion, are expected to reach ₹15 trillion by FY24 (CAGR of 20 per cent), according to CRISIL Research.

Besides supportive macros, focus on tier-2/tier-3 areas, strong reach, its co-branding strategy and an untapped customer base of SBI should support future growth. "We started a relationship with SBI in 2017 in terms of looking at their data base in an organised way. This relationship is coming up now and there is a strong possibility that SBI Cards will generate higher numbers with SBI," says MD and CEO Hardayal Prasad.

While there are many growth opportunities, there are potential risks too, including competition from other digital channels like UPI.

However, Anil Gupta, sector head (financial sector ratings), ICRA, says the credit cards market is unlikely to get affected by other digital channels, given that these are typically used for small-ticket transactions unlike credit cards, which can be used for relatively higher amount as well.

Credit cards also offer limited free-credit to customers besides, incentives like reward points and cash backs. The jury, however is out on this.

Investors should keep an eye out for asset quality. Anand Dama and Neelam Bhatia of Emkay Global, say: "Asset quality risk is on the rise too, given the weakening economic and employment trends. Therefore, SBI Cards, with its already higher delinquency levels and a gross NPA ratio of 2.47 per cent versus 2.3 per cent in Q2 (industry average of 2 per cent), needs to be more vigilant."

Higher share of salaried customers (over 85 per cent) provides some comfort. Overall, the issue looks good for investors with long-term horizon.