

# SBI Card – An exciting consumer play for the long term

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**Overview:** SBI card is India's second largest credit card player (both in terms of credit card issued and spends as well) as of 2019. The company is a pure play credit card issuer in India. The company had 17.6% and 18.1% share of the total credit card issued till date as of March 2019 and November 2019 respectively and a 17.1% and 17.9% market share of the Indian credit card market in terms of total credit card spends in fiscal 2019 and in the eight months ended November 30, 2019, respectively, according to RBI. It's a subsidiary of India's largest public sector bank, SBI. The company began operations in 1998 with GE Capital and SBI being its promoters. GE Capital exited with the entry of Carlyle Group, a well known PE firm with assets under management to the tune of 224 billion dollars. SBI card offers an extensive range of credit cards to all types of corporates and individual income earners of all profiles and lifestyles.

**Industry:** There are 74 credit card issuers in India, including the top-three Indian private banks (HDFC Bank, Axis Bank and ICICI Bank) and SBI Card – the leading pure-play credit card issuer – according to CRISIL Report. Credit card spends have registered robust growth, growing at a CAGR of 32.0% from fiscal 2015 to fiscal 2019, and growth is expected to continue to reach ₹ 15.0 trillion in total credit card spends for fiscal 2024, according to CRISIL Report. The Government's vision of a cash-less society, digitalization, developments in e-commerce, and growth in POS infrastructure have encouraged the use of credit cards. SBI card should eventually become the market leader due to its high growth rate and marketing infrastructure. From March 31, 2017 to March 31, 2019 SBI card's total credit card spends grew at a 54.2% CAGR (as compared to a 35.6% CAGR for the overall credit card industry, according to the RBI) and the number of SBI card credit cards outstanding grew at a 34.5% CAGR (as compared to a 25.6% CAGR for the overall credit card industry, according to the RBI). SBI Card currently has 9.83 million cards outstanding as of November 2019. Credit card spends stood at 1,032.65 billion rupees for fiscal 2019. Credit card market in India continues to remain under penetrated as compared to other developed and developing economies like the US, China, Singapore, Brazil, etc. The average number of cards per 100 people stands at an abysmal low of 3% in India while in the US it stands at 320%, China at 42% which suggests that the sector is highly under penetrated in India. The factors leading the growth mainly include, the younger upcoming generation which is more likely to take debt, rising penetration of smartphones and the rise in consumption. Availability of POS (point of sale) terminals has also increased in recent years (from 1.1 million in

2014 to 3.4 million in 2019) but a large room for growth remains.

**Competitive Advantage:** SBI Card's access to SBI's extensive branch network of more than 21,900 branches and a customer base of more than 445 million customers offers a great opportunity for SBI Card to capitalize on. They are also a leader in open market customer acquisition according to CRISIL Report with 32,677 outsourced service personnel operating as of December 31, 2019. The company's increasing focus on non interest income (48.9% as of 2019 versus 43.6% in 2017) in its revenue mix could help in offsetting the interest rate volatility associated with interest income in the revenue mix. The SBI brand is well known in India, which offers people trust and confidence into buying a SBI branded product. Company's pure play status in credit card market offers it the ability to tie up with other banks to push their product as well. The company is the largest issuer of co brand credit cards in India and has a well-diversified product portfolio catering to customers of all segments. Company has already made significant investment in technology infrastructure and does not immediately require any investment in technology infrastructure as the current capacity is underutilized and can handle 3-5 times of current business volumes as per management. Ability to cross sell other financial products acts a bonus for the company.

**Product mix:** SBI Card offers personal cards, corporate cards and white label cards. As of December 2019, personal cards made up 99.5% of the total cards outstanding (9.99 million cards). Corporate cards made up 0.5% of the total cards. Company only offers one white label card. Total spends by personal cards stood at 759 billion rupees while corporate made up 220 billion rupees for the nine months ended December 31, 2019. Personal cards steadily increased their share in total pie from fiscal 2019 by contributing 77% to the total spending in the nine months ended December 31, 2019. Company has 21 co-brand partners as of December 2019 with 3 more soon to become operational.

**Financials:** SBI Card has performed very well in terms of financials. The company has delivered an average ROE of 28%. The company presently stands adequately capitalized with capital adequacy ratio at 19.2% as of December, 2019 as per Value Research. SBI Card has undertaken lot of equity dilution but that can be attributed to the promoters subscribing to the rights issue at 90 rupees per share last financial year and amalgamation of SBIBPMSL. These transactions suggest that further equity dilution going forward will be more controlled and will face more market scrutiny. Promoters stand to make 660 rupees per share in one year by doing the IPO. Company is mainly reliant on debt which provides further comfort in terms of equity dilution. High growth rate of the company may demand equity issuance but at a higher price thus supporting return on equity with the ability to take more

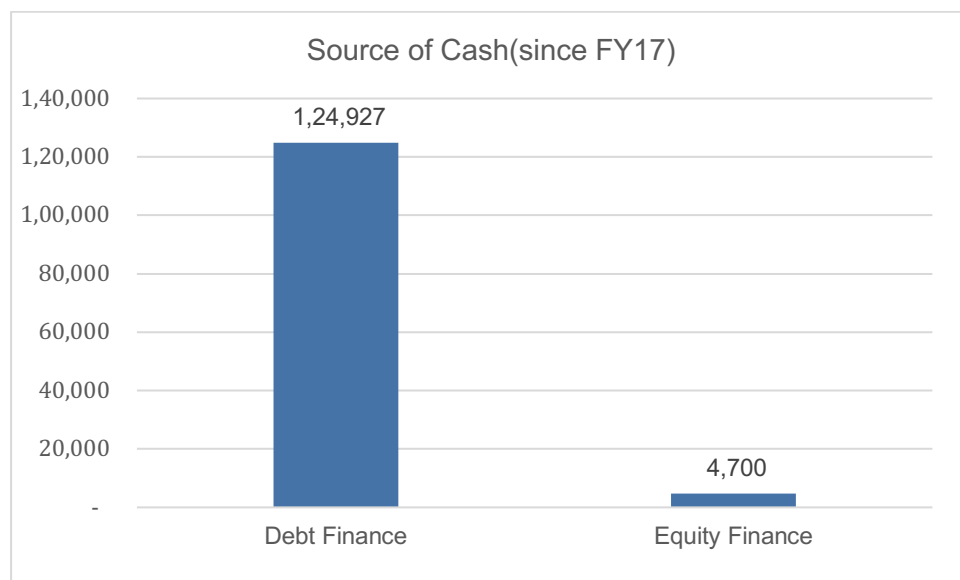
debt. Company has diluted more than 18% since FY17. The cost component of the company has reduced with an increase in net profit margin from 10% to 16% from FY17 to FY19, mainly due to reduction in operating and other expenses. Total costs fell from 86% to 82% of the total revenue excluding other income. Net interest margin stand at 15.6% as per Value Research. The loan book has grown at 37% from FY17 till December, 2019 as per Value Research.

Source: SBI card RHP

Ratios	FY17	FY18	FY19	9MFY20
Debt/Equity	5.91	5.12	4.08	4.08
Interest Coverage	2.08	2.29	2.47	2.75
Debt/EBITDA	7.74	7.28	6.30	7.41
Net profit margin	10.74	11.19	11.84	16.04
Gross NPA	2.34%	2.83%	2.44%	2.47%
Net NPA	0.76%	0.94%	0.83%	0.83%

Financing	FY17	FY18	FY19	9MFY20
Equity	-	-	4,700	-
Debt	23,431	30,435	23,060	47,999
No of new shares issued	-	-	52.22	95.11
No of shares outstanding	785.00	785.00	837.22	932.33
Total Dilution since FY17 pre IPO	-	-	-	18.77

Note: all the numbers are in millions.

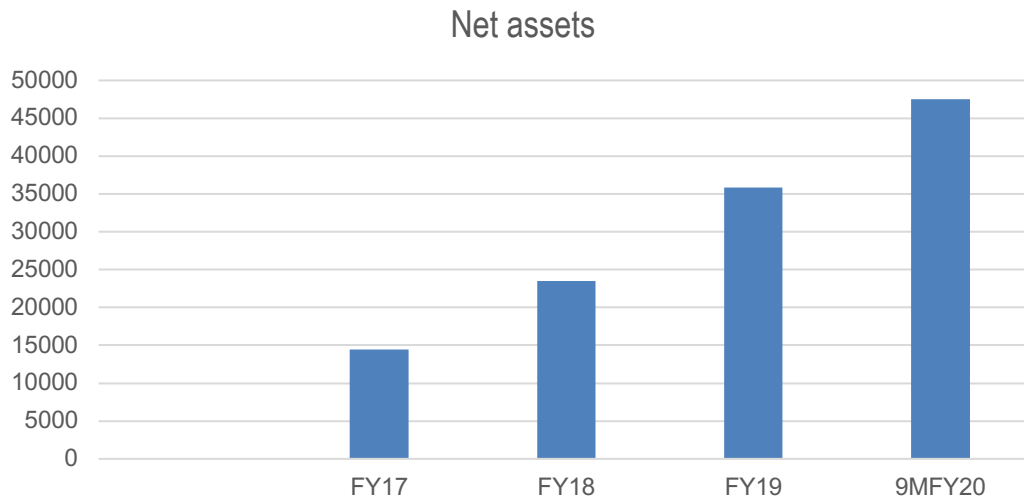


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**Expansion Strategy:** SBI Card is embarking on increasing its physical touch points in tier 2 and tier 3 cities, team up with more co-brand partners and increase the focus towards acquiring accounts from SBI, its parent. The company intends to broaden its product offerings and target new to credit and new to card segments, it will be a key driver with the growth of the Indian economy. Company is already delivering cards digitally which is helping customers use the card even before the physical card has reached their doorstep.

**Downside risks:** The big risk facing the company is the economic cycle and negligence in underwriting process for the issue of new cards to chase growth. The company is growing at a very fast pace which can lead to on boarding of sub prime customers which can lead to deterioration of the credit quality of the credit card receivables portfolio. Plus, the high growth rate can lead to an increase in requirement for equity capital that can lead to dilution of the current shareholders. Also with the changes in technology and the rise of fintech startups, the company faces a material risk of reduction in margins to compete with other players. There can be shareholder interest conflict because SBI will continue to retain about 70% of the company post IPO. SBI will continue to have the main influence on the affairs of the company like appointing managing director and other board members and end up hurting the interests of minority shareholders. Government run enterprises haven't found much love in the Indian market due to the undue influence of government in the affairs of these companies. This could cause share price to command lower premium as compared to other private sector players. SBI Card, being a non-banking finance company, doesn't have access to public funds like savings account and current account. This will further dent its margins and reduce its competitiveness against banks.

**Conclusion:** SBI Card is a great company with great financials. Company can become the no 1 player in credit cards displacing HDFC Bank as the leader. The company needs to continue growing at a very high rate for few years to achieve that milestone. India's highly underpenetrated credit card market presents a tremendous opportunity to investors and SBI Card fits the bill. Equity dilution going forward may go down due to the unusual nature of previous dilutions and improved market coverage of the company after listing.



Note: all numbers are in millions

The company has steadily grown net assets with rights issue contributing 14.2% of the increase in net assets and rest of the increase coming completely from internal generation since FY17. Return on equity will continue to stay at high levels due to the high growth rate. Using PEG ratio and trailing FY19 earnings PE ratio at 79, the valuation seems fair. Even though the company compensates for the high valuation with high growth rate, current market scenario presents a threat to the sustenance of high growth rates as well as the valuation in the short term. When you take a long term view the expected growth of the company more than compensates the investors for high valuation.

**Source:** RHP of SBI Cards and Payments Services, Value Research