Wage settlement impact on banks

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New wage settlement – highest impact on SBI, lowest on BoB

- The Indian Banks' Association (IBA) and bank unions have agreed to a 17% wage hike for public sector banks. The wage revision will be effective from November 1, 2022, for a period of five years
- Banks have provided 14-15% towards the settlement and will now have to bridge the gap in pension and wages.
- The biggest bank wise impact from catch-up provisions on book value for FY25E would be for SBI at 2.5% while BoB would be the least impacted at below 1%.
- Unlike in previous settlements, banks have made provisions this time around. Furthermore, wage negotiations were concluded within 12 months of the old settlement ending, which is the fastest so far.
- In FY25E, total employee expenses would be flattish to marginally down given the catch-up provisions in the base of FY24.
- The increase in the salary bill over the next four years shall be 5–8% depending upon CPI.
- The Ministry of Finance (MoF) is yet to approve the agreement. It will become effective only after that, but banks would make provisions in H2FY24 towards the gap.

New wage settlement – Details

- The Indian Banks' Association (IBA) and bank unions have agreed to a 17% wage increase for public sector banks. The wage revision would be effective from November 1, 2022, for a period of five years and would be the Twelfth bipartite settlement.
- Banks have provided 14–15% towards the settlement and will now have to bridge the gap in pension and wages.
- Unlike in the previous settlements, banks have made reasonably large provisions this time around. Furthermore, the wage negotiations were concluded within 12 months of the old settlement ending, which is the fastest so far.
- The employee unions and the IBA have concluded their negotiations. However, the settlement would become effective only once the MoF cleared it.
- In addition to state-owned banks, Federal Bank is the only private bank we cover, which would be impacted by this agreement

Details of basic pay and DA

New basic pay: Entire dearness allowance (DA) of Oct-22 (8088 points) has been merged with basic. Hence, DA is zero as of Nov-22. On the new basic, employees will get a hike of 17%.

DA is linked to inflation and depending on the inflation rate, gets adjusted upward every quarter.

While the DA is zero as on November 1, 2022, there has been additional DA from November 1, 2022 to date of around 1000 points, which becomes the new DA. The DA between Nov-22 and Jan-24 of 1000 points amounts to 10% of old basic and around 7% of new basic. There would be increments to DA every quarter depending on inflation. The increase in DA would be applied on the new (merged) basic.

By the end of the settlement, DA would likely move up to at least 40–50% depending on inflation. There have been years when DA has touched as high as 80% of basic due to inflation and at times (2016) it has also been above 100%.

Details of basic pay and DA – An illustration

If basic on October 31, 2022 is INR100 and DA is INR40, the new base as of Nov-22 would be INR140. Banks would provide an increase of 17% on INR140, which would be around INR164. Hence, the new basic salary bill shall be INR164. The DA during Nov-22 to date, which has not been merged because the cutoff date was November 1, 2022, would become the new DA. This new DA would roughly be 7% of new basic or INR11.5. In the next year, assuming 5% inflation the new salary bill would be INR183 (INR164 + 164*0.05+11.5). This would translate to an increase of 4.7% YoY in the salary bill ex-pensions for FY25.

Exhibit 1: Illustration of the current wage hike

Basic as on Oct 31, 2022	100
DA as on	40
Merged basic as on Nov-1, 2022	140
New basic on Nov-1,22 after 17% hike	164
New DA= DA from Nov1-date @7% of new basic	11.466
Total salary as on Nov-1, 2022 to Nov-25	175
Assuming 5% inflation in FY25, new DA	19.656
New salary in FY25	183
% increase	4.7%

Source: Nuvama Research

Existing provisions made by banks

- Most banks have provided for the wage settlement for 11 months from Nov-22 to Sep-23 assuming a hike of 15%.
- SBI and PNB have provided for 14%.
- Canara Bank has provided 10% for five months and 15% for six months while other banks have provided at a consistent rate for all 11 months.
- In addition to salaries, banks will also have to provide for a hike in pensions.
- Banks plan to absorb the entire shortfall on both wages and pensions equally over Q3FY24 and Q4FY24.

Exhibit 2: Current provisioning

INR bn	Cumulative provisions as of Sep-2023	Existing provision per month
Bank of India	6.43	0.61
Canara Bank	10.74	0.98
Union Bank	12.10	1.10
Indian Bank	6.89	0.63
State Bank of India	88.95	8.09
Bank of Baroda	13.20	1.20
Punjab National Bank	14.38	1.31

Source : Company, Nuvama Research

Feedback on additional wage provisions

- Most banks have provided feedback on additional provisions. However, other than SBI and Canara no bank has provided feedback on the pension shortfall.
- Given that the wage bills of Canara, Union, BoI and BoB are similar, the impact on pensions could also be similar.
- SBI would be the most impacted by these provisions at 2.6% while BoB would be the least impacted.
- In terms of QoQ increase in the total employee cost in Q3FY24, SBI, BoB and PNB would be lower than others because of one-off provisions in the base quarter (Q2FY24).

Exhibit 3: Current provisioning versus actual impact (INR bn)

INR bn	Cumulative provisions as of Sep-2023	Existing provision per month	New provision per month	Pension
Bank of India	6.43	0.61	0.69	NA
Canara Bank	10.74	0.98	1.11	NA
Union Bank	12.10	1.10	1.25	NA
Indian Bank	6.89	0.63	0.71	NA
State Bank of India	88.95	8.09	9.82	Provided upto Sep-23
Bank of Baroda	13.20	1.20	1.36	Provided @ 12%
Punjab National Bank	14.38	1.31	1.48	Provided upto Sep-23

Source : Company, Nuvama Research

Exhibit 4: Mapping bank wise feedback on wage impact

INR mn	Backlog provisions for wages	Provision for quarter	Total provision	Provision for pension due to new wage agreement
Bank of India	2,970	2,100	5,070	NA
Canara Bank	1,533	3,910	5,443	7,500
Union Bank	1,613	3,738	5,351	NA
Indian Bank	NA	NA	NA	NA
State Bank of India	51,000	-	51,000	49,000
Bank of Baroda	-730	3,400	2,670	NA
Punjab National Bank	3,064	4,740	7,804	1,650

Source : Company, Nuvama Research

Exhibit 5: Our estimate of total provisions based on our calculation of pension liability

INR mn	Wages	Pension	Total
Bank of India	5,070	7,000	12,070
Canara Bank	5,443	7,500	12,943
Union Bank	5,531	7,300	12,651
Indian Bank	NA	NA	NA
State Bank of India	51,000	49,000	1,00,000
Bank of Baroda	2,670	2,500	5,170
Punjab National Bank	7,804	1,650	9,454

Source : Company, Nuvama Research

Exhibit 6: Percentage QoQ increase in wages and percentage impact on PPOP

INR mn	Q3FY24 wages assuming two quarter charge	Reported wages for Q2FY24	One-time provision in Q2FY24	% change QoQ in wages	% impact on Q2 PPOP
Bank of India	6,035	21,783	0	28%	16%
Canara Bank	6,472	39,568	0	16%	8%
Union Bank	6,326	30,853	0	21%	9%
Indian Bank	NA	21,769	0	NA	NA
State Bank of India	50,000	1,89,264	34,000	26%	26%
Bank of Baroda	5,170	37,064	1,000	14%	6%
Punjab National Bank	4,727	42,001	3,040	11%	8%

Source : Company, Nuvama Research Note: For BoB we have assumed that the entire impact will be in Q3FY24, for others we have spread it over two quarters

Exhibit 7: Percentage of book value

	BV FY25E	Total wage impact	% of BV
Bank of India	6,54,689	12,070	1.38%
Canara Bank	9,27,061	12,943	1.05%
Union Bank	10,05,221	12,651	0.94%
Indian Bank	6,13,487	NA	NA
State Bank of India	40,62,335	1,00,000	1.85%
Bank of Baroda	12,44,877	5,170	0.31%
Punjab National Bank	8,10,494	9,454	0.87%

Source : Company, Nuvama Research

Valuation

- PSU bank stocks have outperformed private banks in CY23, driven by a pick-up in loan growth and improvement in asset quality.
- As long as they can deliver core RoA of 1% or above, which would require a benign credit environment and strong loan growth to sustain, we believe the outperformance can endure.
- The book values are adjusted for revaluation reserves (55%) and DTA for PNB.
- PNB now looks more richly valued compared to other state banks.
- SBI's earnings have been strong. We retain BUY though capital adequacy remains a challenge.
- BoB offers good risk-reward and a low base of earnings.
- Other mid-sized banks offer better risk-reward.

Exhibit 8: Valuation

	PBV, FY25E	PE, FY25E	RoA, %
Bank of India	0.8	6.3	0.89%
Canara Bank	0.9	5.3	0.98%
Union Bank	0.9	6.3	1.00%
Indian Bank	1.0	7.3	1.03%
State Bank of India	1.0	8.4	1.04%
Bank of Baroda	0.9	6.2	1.08%
Punjab National Bank	1.2	11.2	0.54%

Source : Company, Nuvama Research, Bloomberg Consensus   Note: We have not factored in subsidiary value for Canara

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