

Federal Bank

BUY

High margin products to be the focus area

Summary

We attended Analyst Day hosted by Federal bank which highlighted the journey of last 3 years (Dec'19- 22) and how the bank has successfully navigated through the Covid'19. Further, future business path to be among the top 5 private banks as well as the most admired bank in the country. Management highlighted that the focus ahead shall be on the higher margin products (Credit Cards, Personal Loans, MSME Loans etc.) by leveraging on its digital, analytical and branch lite partnership based model. The bank is strengthening its presence outside Kerala (such as TN) both through opening new branches as well as building relationships with key stakeholder. Going forward, the bank expects to operate through Branch Lite Distribution Heavy mode. We re-iterate BUY rating with the target price of Rs.175 based on P/BV of 1.4x FY25E.

Key Highlights of Analyst Meet:

- Successfully Navigated through Covid'19:** The bank has successfully navigated through the Covid'19 challenges and emerged out much stronger, delivered strong business growth, improved profitability margin and maintained pristine asset quality. The Bank has witnessed its highest ever quarterly PAT consistently for last three quarters (Rs.8.04bn Q3FY23) while RoA has improved by 29bps and stood at around 1.3% Q3FY23 (vs. 1.0% Q3FY20). Consecutively, RoE improved by 341bps to 15.9% Q3FY23 (12.5% Q3FY20).
- Change in Credit Book Mix:** The credit book mix of the bank has also witnessed significant change in its post Covid era. The book which was majorly led by wholesale loan in pre covid (around 53% in Q4FY19), has now shifted towards retail loan book. The current credit book mix stands as Retail: Wholesale at 54:46 (as compared to Retail: Wholesale at 47:53 in Q4FY19). This has supported bank to granulize its advances book.

TP	Rs.175			Key Stock Data	
CMP	Rs.129			Bloomberg / Reuters FB IN / FED.BO	
Potential upside/downside	36%				Sector
Previous Rating	BUY		Banking		Shares o/s (mn)
			2,116		Market cap. (Rs mn)
			273,149		3-m daily avg trd value (Rs mn)
	71.5		52-week high / low		Rs143 / 83
			Sensex / Nifty		58,962 / 17,304

Price Performance (%)				Shareholding Pattern (%)	
	-1m	-3m	-12m	Promoters	0.0
Absolute	(2.2)	(3.5)	33.2	FII	27.7
Rel to Sensex	(1.6)	2.2	28.3	DII	40.7
				Public	31.6

Financial snapshot (Rs mn)					
Year	FY2021	FY2022	FY2023E	FY2024E	FY2025E
NII	55,337	59,620	71,983	82,749	94,205
Change (yoY, %)	19%	8%	21%	15%	14%
Net Profit	15,903	18,898	28,825	34,165	39,877
Change (yoY, %)	3%	19%	53%	19%	17%
EPS (Rs)	8.0	9.0	13.7	16.2	19.0
Change (yoY, %)	3%	13%	53%	19%	17%
ABV (Rs)	74.9	84.4	96.7	109.4	123.8
PER (x)	16.2	14.4	9.4	7.9	6.8
P/ABV (x)	1.7	1.5	1.3	1.2	1.0
ROE (%)	10.4	10.8	14.4	15.0	15.3
ROA (%)	0.8	0.9	1.2	1.3	1.3
GNPA (%)	3.4	2.8	2.5	2.6	2.7
NNPA (%)	1.2	1.0	0.7	0.9	1.1
CAR (%)	14.6	15.8	15.1	14.8	14.8

Source: IDBI Capital Research

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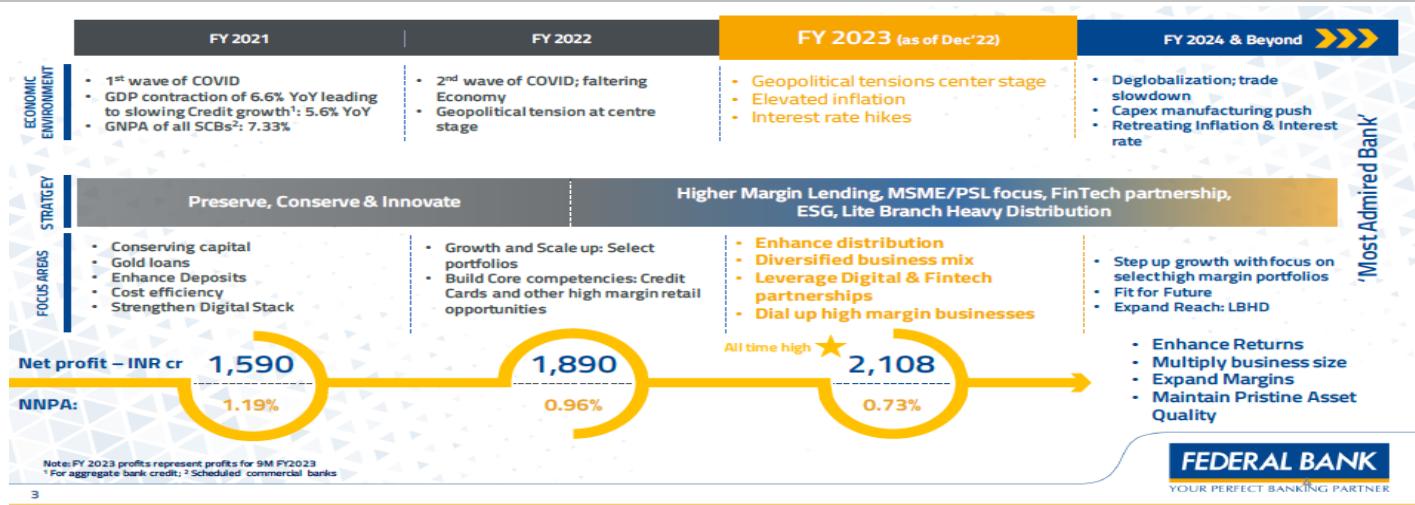
- **Focus towards High Margin Products:** In the retail asset segment, Management has highlighted that going forward; the key focus of the bank would be towards higher margin products such as Personal Loan, Credit Card, MSME Loans etc. These products are expected to help bank scale up its fee income and would be one of the levers of RoA improvement. The bank has increased its portion of unsecured lending to 7% in FY23 (YTD Dec'22) as compared to around 3% in FY19. The bank is increasing its penetration across key product segment such as Home Loan to bring down the cost and gain market share in chosen geographies. The bank aspires to be among the top 7 players in the Credit Card space over next 2 years and in line with the same is expected to roll out NTB as well as assisted journey for its customers in credit card space. The bank also expects to double its personal loan portfolio over next 2 years by leveraging on building digital end to end experiences for NTB customers (earlier was only for ETB customers).
- **Digital and Analytical Initiatives:** The bank is leveraging on continuous innovations across its digital as well as analytical capabilities to enhance and enrich the overall experience of the customer and help the bank make improved business decision based on the output of the models. The success of the digital initiatives can be witnessed in strong performances across all key parameters. The bank is launched various digital initiatives such as easy access to credit for farmers through Digital Kisan Credit Cards, first bank to enable cross border bill payments as well digital first credit card in 3 clicks. Through analytics, the bank is improving its decision making across customer engagement, relationship management, asset underwriting, delinquency management, fraud risk as well as process optimization.
- **Wholesale Banking and Government Business:** In wholesale banking, the bank is emphasizing more towards commercial banking. The bank has opened around 14 client servicing points to serve its wholesale clients and has shifted from focusing on wallet share to focusing towards mind share. The bank has setup a center of excellence which guides clients in trade as well as their regulatory issues. Going forward, the bank would target initiatives such as correspondent banking and MNC vertical. In the Government business space, the bank targets for a market share of around 3% by FY25 which would benefit the bank in terms of CASA deposit, Fee Income as well as customer retention. The bank expects to deliver 2x business over next 2 years.

Exhibit 1: Business Performance Pre Covid vs. Post Covid



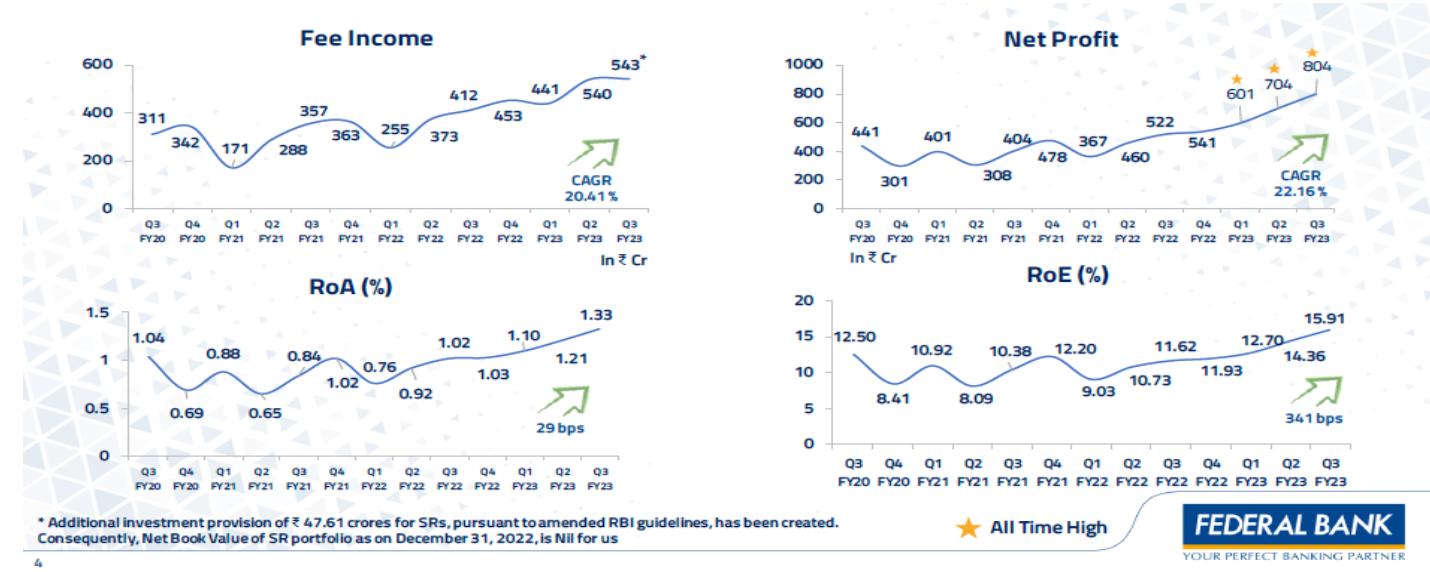
Source: Company; IDBI Capital Research

Exhibit 2: Delivering consistent performance during Covid as well as post Covid



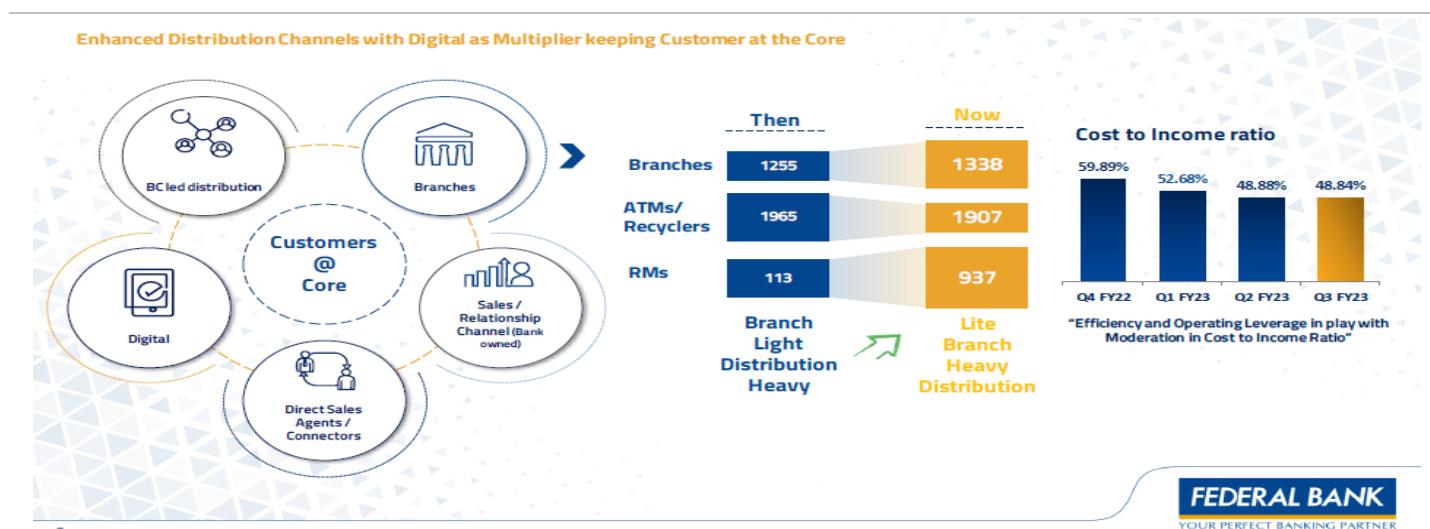
Source: Company; IDBI Capital Research

Exhibit 3: Consistent performance translating into strong business performance



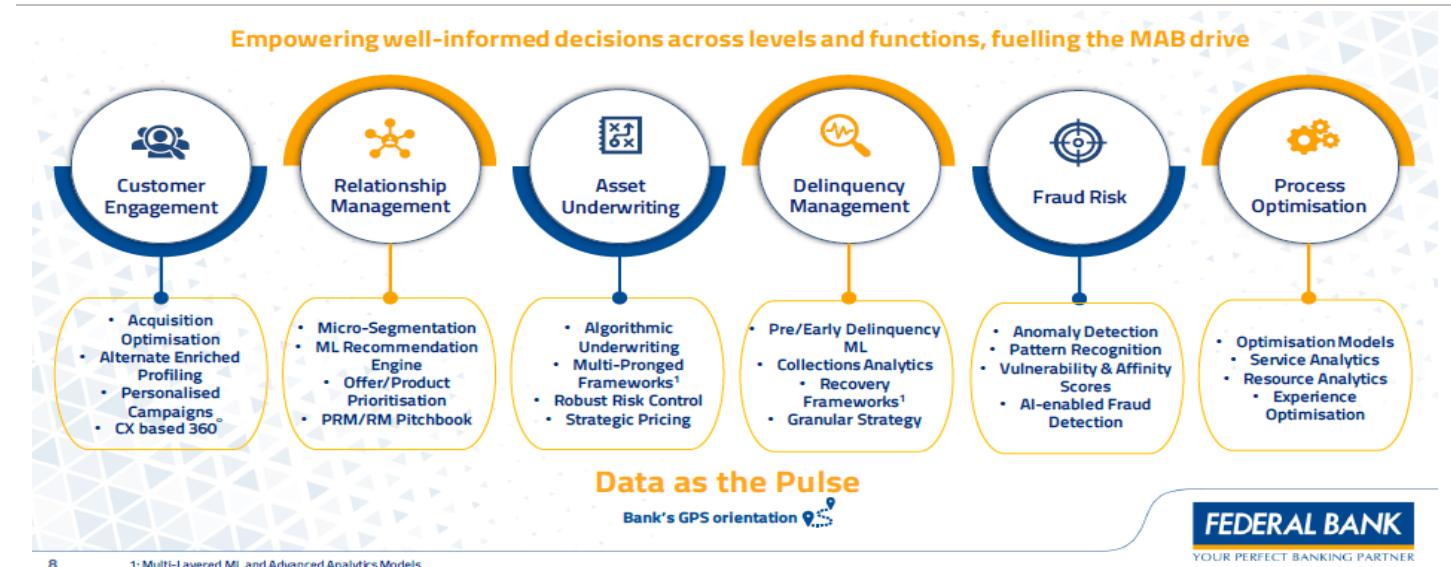
Source: Company; IDBI Capital Research

Exhibit 4: Business model changed from Branch Lite Distribution Heavy to Lite Branch Heavy Distribution



Source: Company; IDBI Capital Research

Exhibit 5: Analytics serving as the backing of Business Decisions



Source: Company; IDBI Capital Research

Exhibit 6: Levers for Growth



Source: Company; IDBI Capital Research

Exhibit 7: Retail banking delivering strong progress since Dec'19

	Then (Dec-19 / Q3 FY20)	Now (Dec-22 / Q3 FY23)	CAGR	11.38 %
RETAIL DEPOSITS	1,31,530	1,81,714		
COST OF DEPOSIT	5.84	4.57		
CASA RATIO	30.81%	34.24%		
RETAIL ASSETS	36,551	53,936	CAGR	13.85 %
MARKET SHARE OF DEPOSITS	1.09 %	1.12 %		
MARKET SHARE OF ASSETS	1.18 %	1.26 %		
CREDIT COST	0.82	0.38		

In ₹ Cr

FEDERAL BANK
YOUR PERFECT BANKING PARTNER

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Source: Company; IDBI Capital Research

Exhibit 8: New Campaign- “RISHTA AAP SE HAI, SIRF APP SE NAHI”



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Source: Company; IDBI Capital Research

Exhibit 9: 4-D Mantra leveraging the success of Federal Bank



Source: Company; IDBI Capital Research

Exhibit 10: Digitization-Enabling smoother and efficient business progress



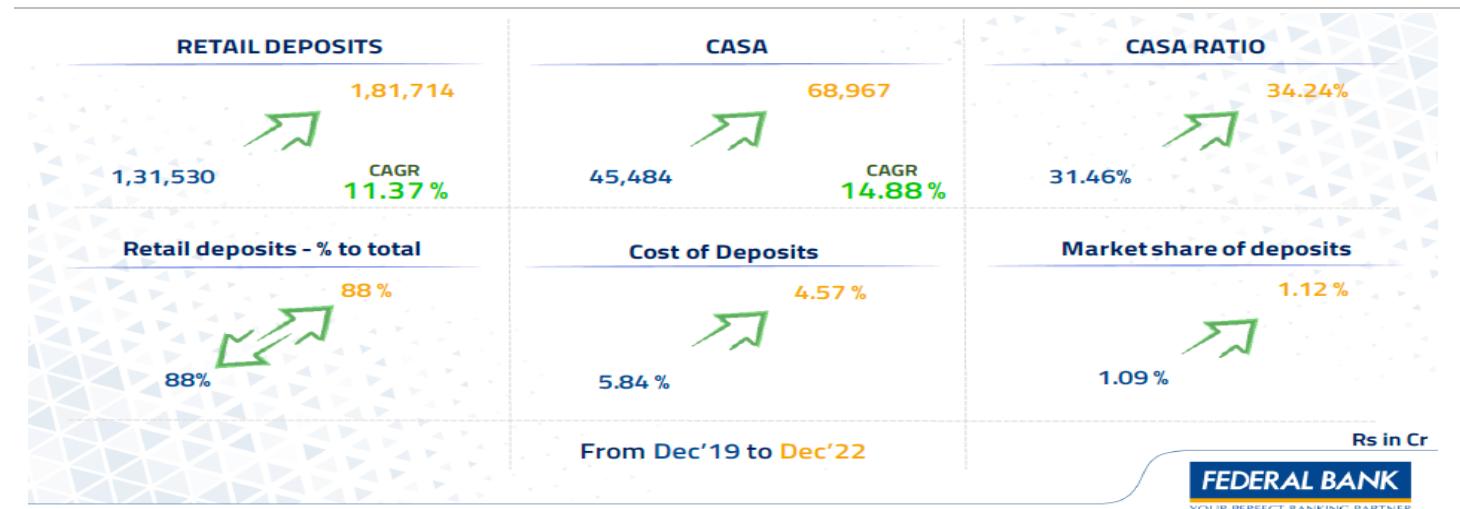
Source: Company; IDBI Capital Research

Exhibit 11: Credit Card: Aspiring to be among the top 7 Credit Card Players by 2024



Source: Company; IDBI Capital Research

Exhibit 12: Strong growth traction delivered across Retail Deposit Products



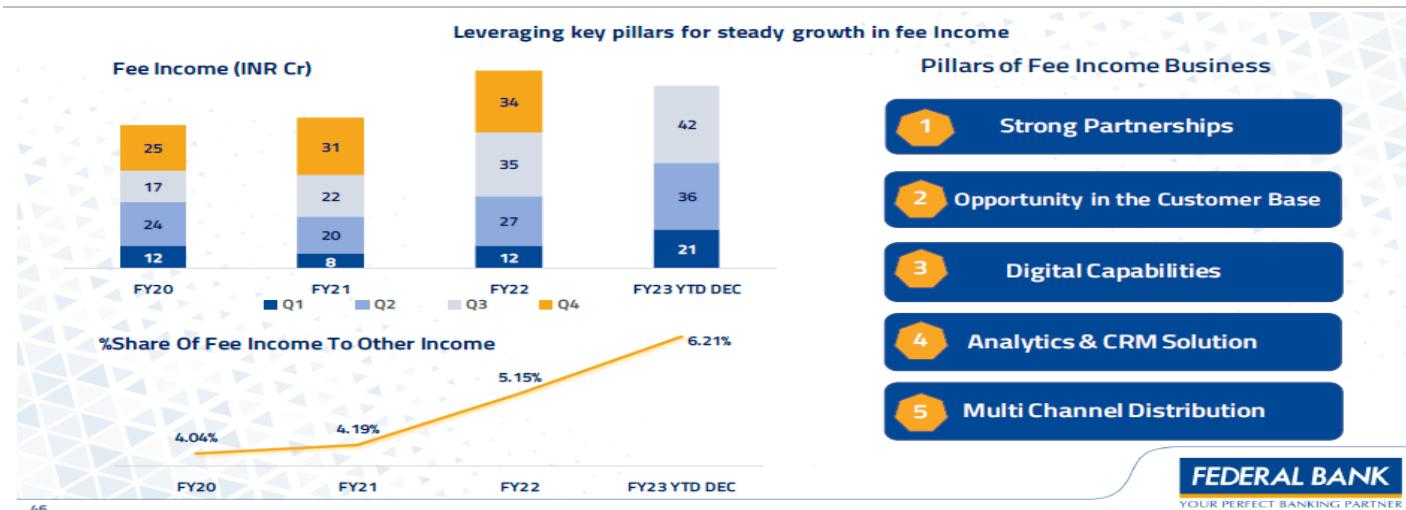
Source: Company; IDBI Capital Research

Exhibit 13: NR Deposit: Outperforming the industry growth trend



Source: Company; IDBI Capital Research

Exhibit 14: Fee Income to be one of the important growth aspects of the Bank



Source: Company; IDBI Capital Research

Exhibit 15: Expecting the Gold Loan portfolio to get double over next 3 year



Exhibit 16: Key Focus areas for Business Banking

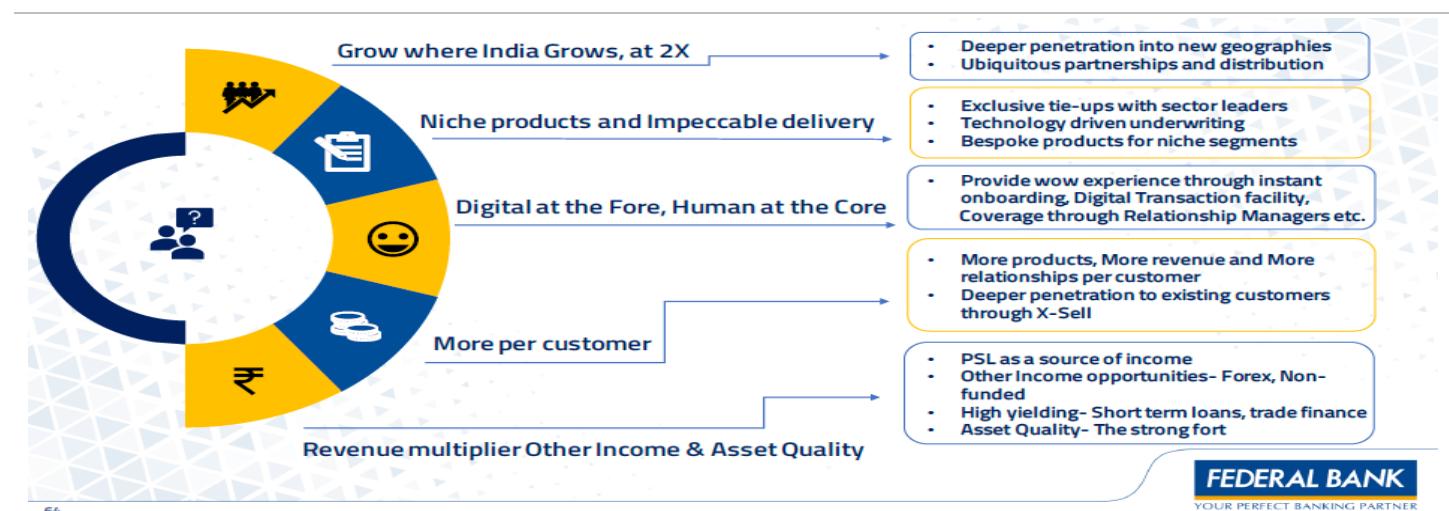
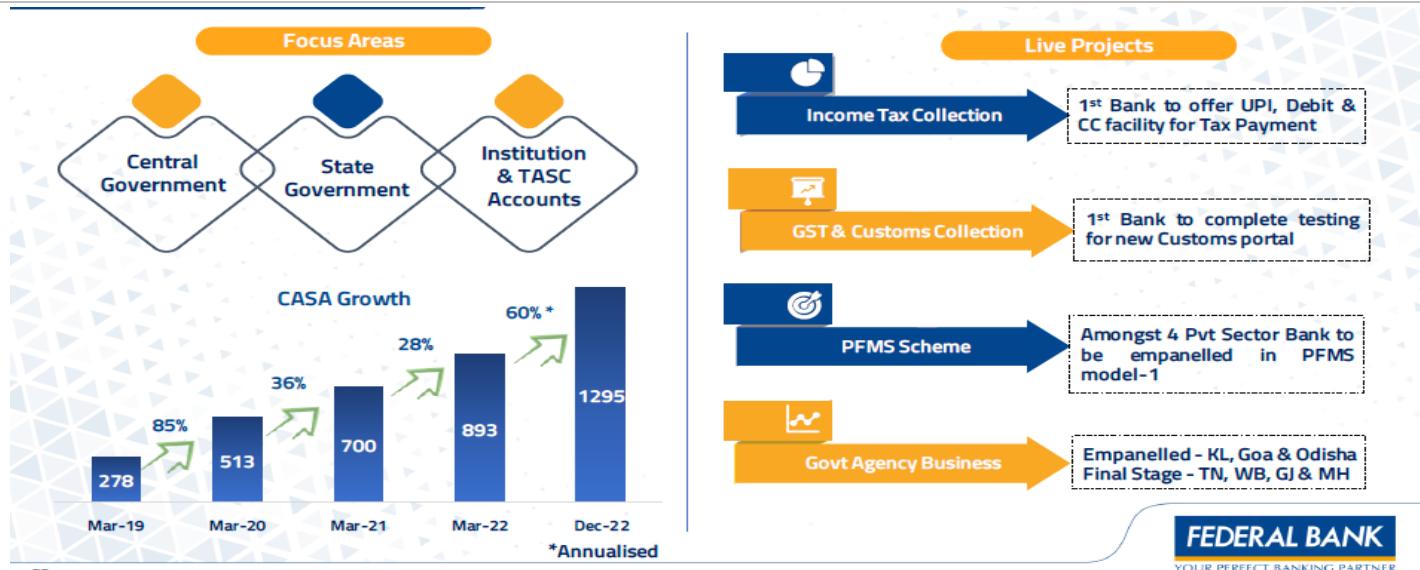


Exhibit 17: Wholesale Banking continuing to deliver robust business performance with pristine asset quality



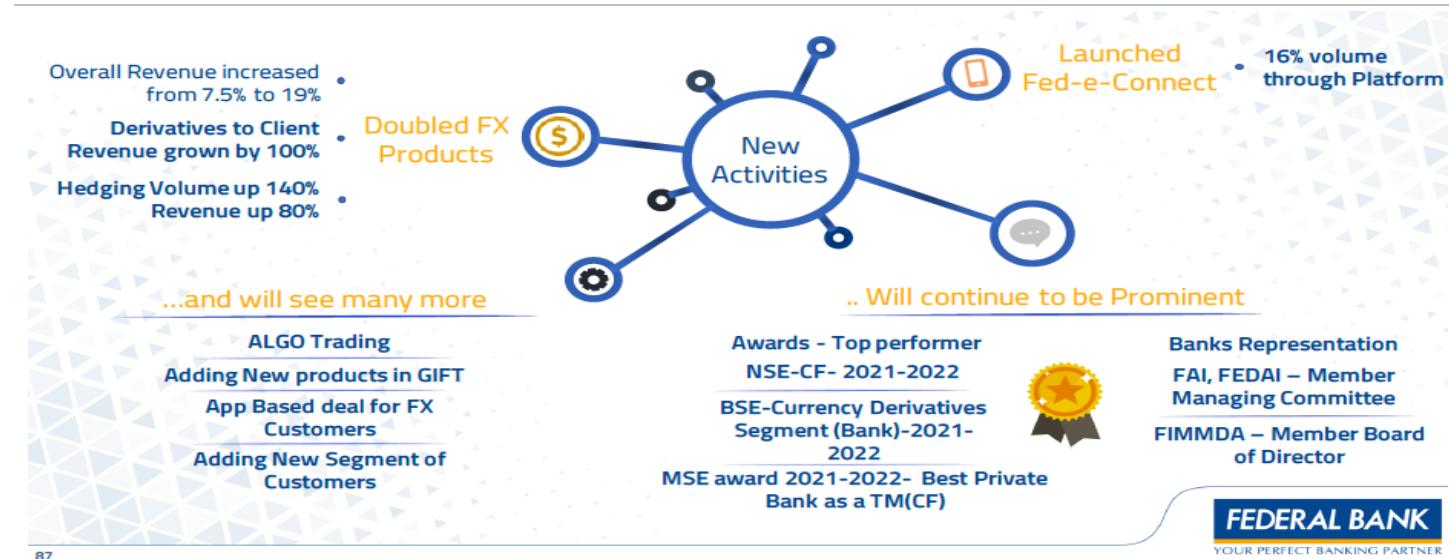
Source: Company; IDBI Capital Research

Exhibit 18: Encashing the expertise in Government Business to deliver strong business growth



Source: Company; IDBI Capital Research

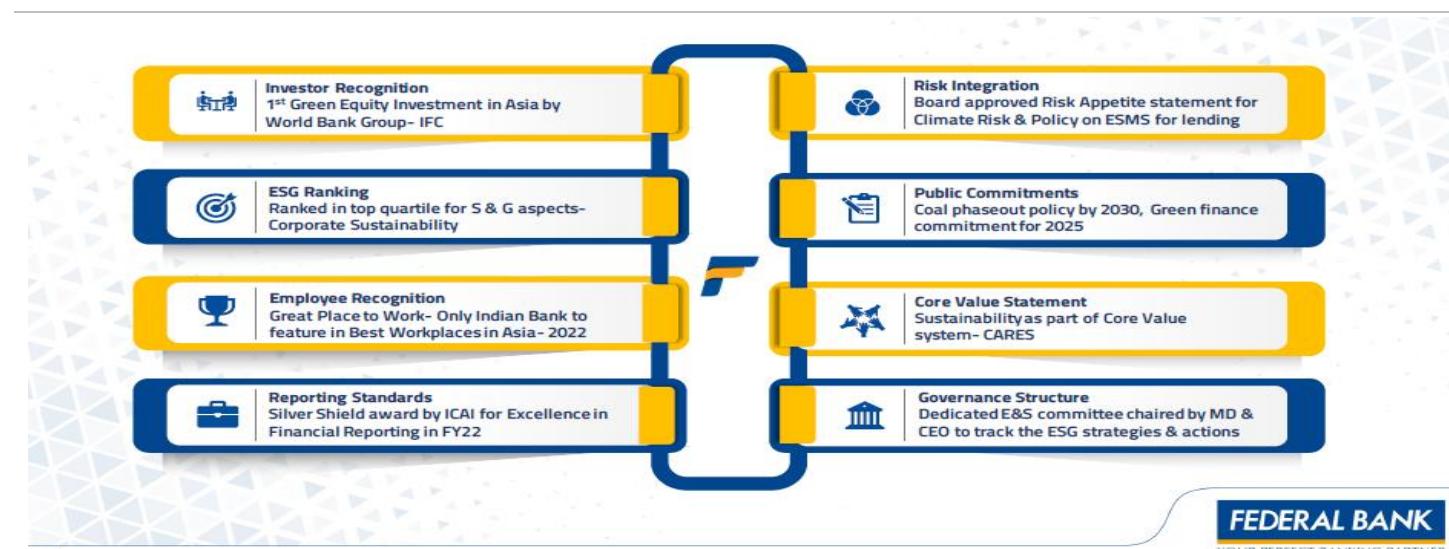
Exhibit 19: Snapshot of treasury operations of the Bank



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Source: Company; IDBI Capital Research

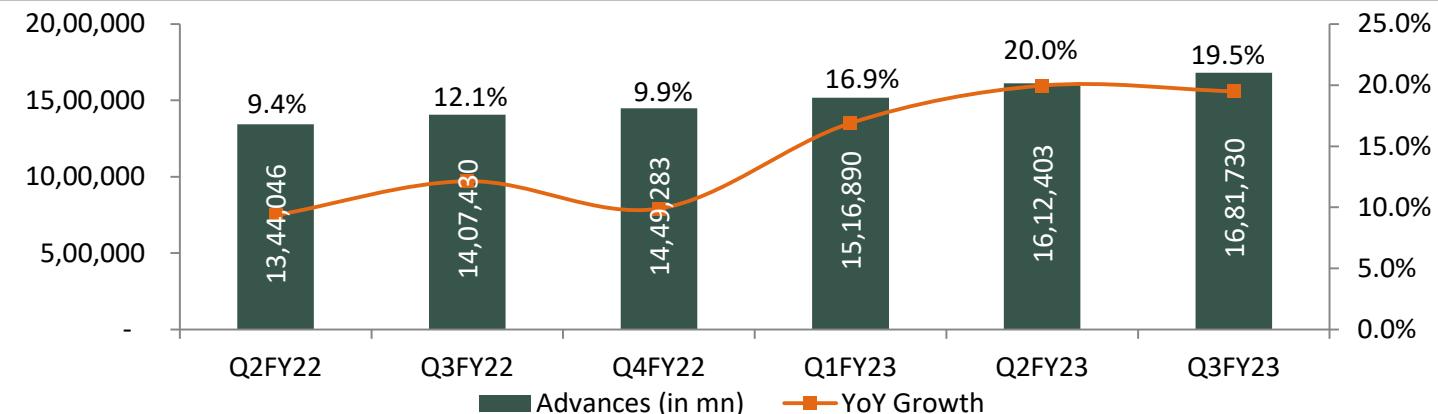
Exhibit 20: ESG-One of the core areas of focus for the bank



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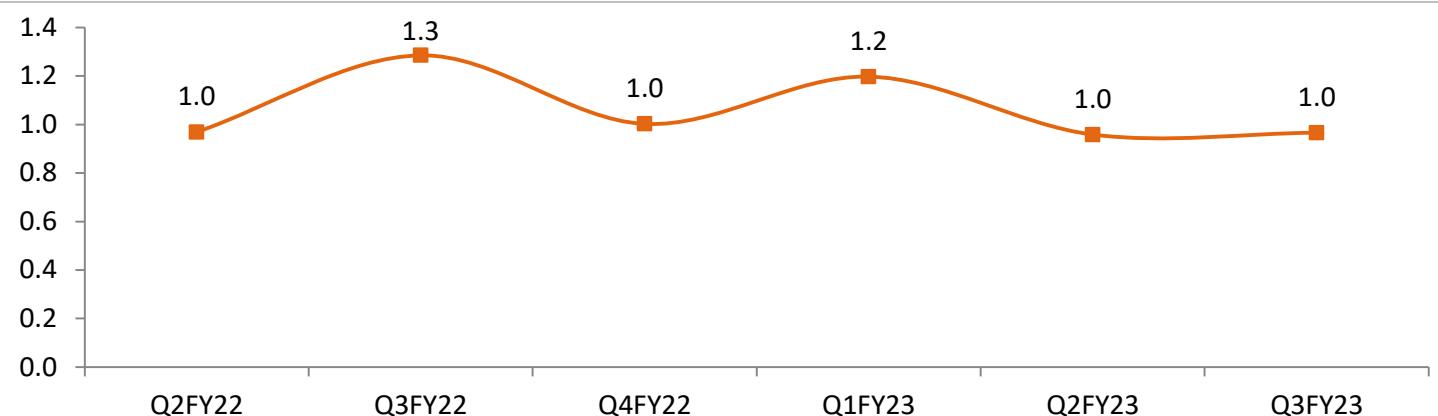
Source: Company; IDBI Capital Research

Exhibit 21: Advances growth continued to witness strong growth momentum on YoY basis



Source: Company; IDBI Capital Research

Exhibit 22: Slippage ratio remained stable sequentially



Source: Company; IDBI Capital Research

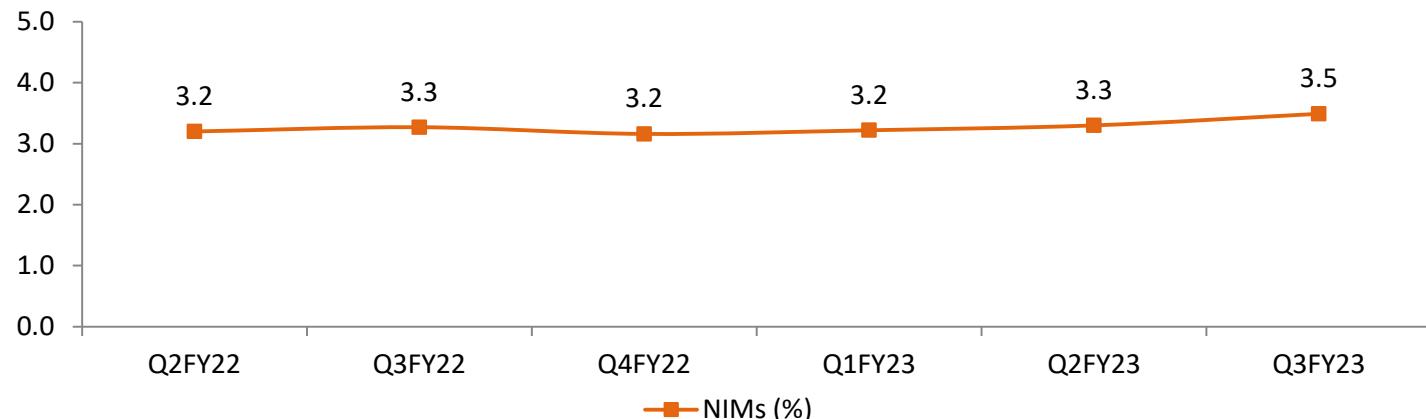
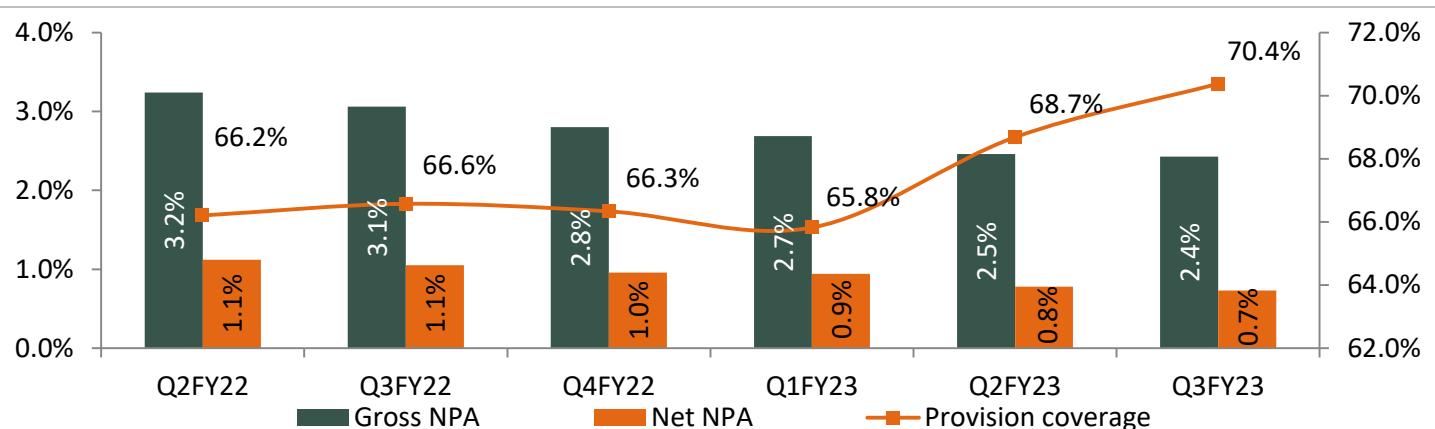
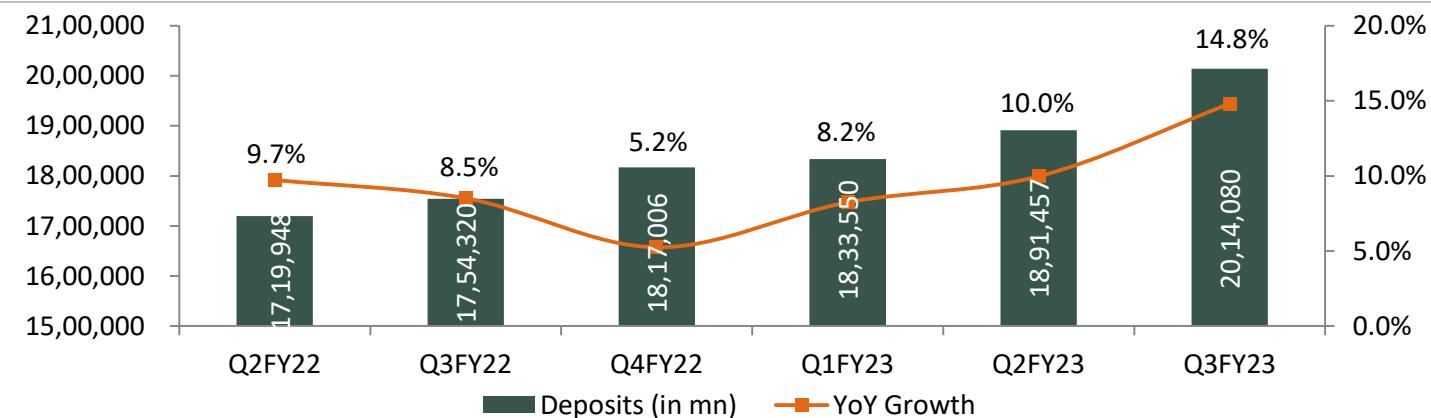
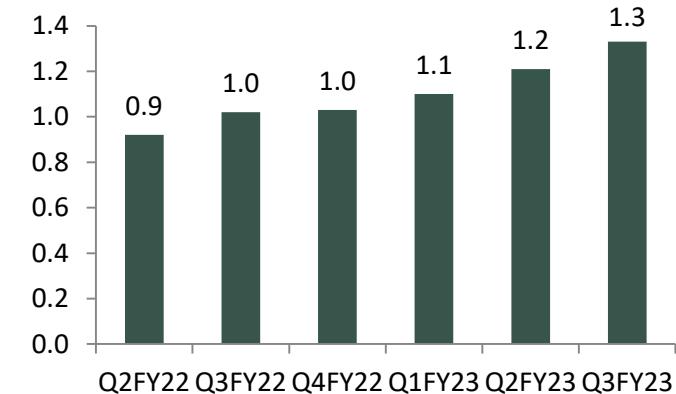
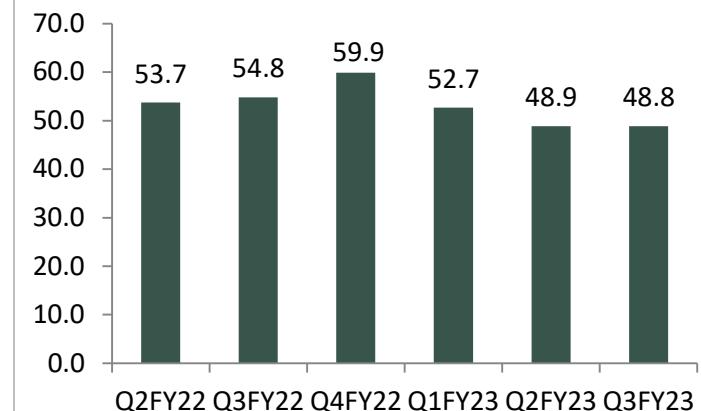
Exhibit 23: Net Interest margins continued to improve QoQ

Source: Company; IDBI Capital Research
Exhibit 24: Asset quality remained stable

Source: Company; IDBI Capital Research

Exhibit 25: Deposits growth continued to witness strong growth uptick


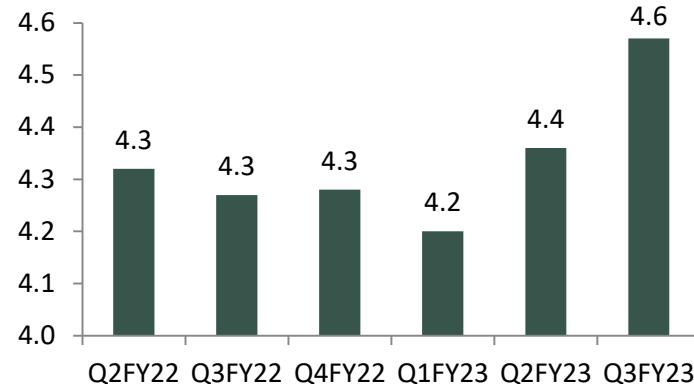
Source: Company; IDBI Capital Research

Exhibit 26: RoA continued witnessing up tick QoQ


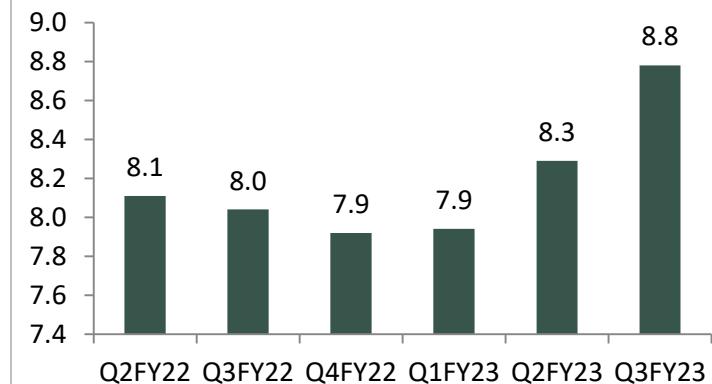
Source: Company; IDBI Capital Research

Exhibit 27: Cost to Income Ratio remained stable sequentially


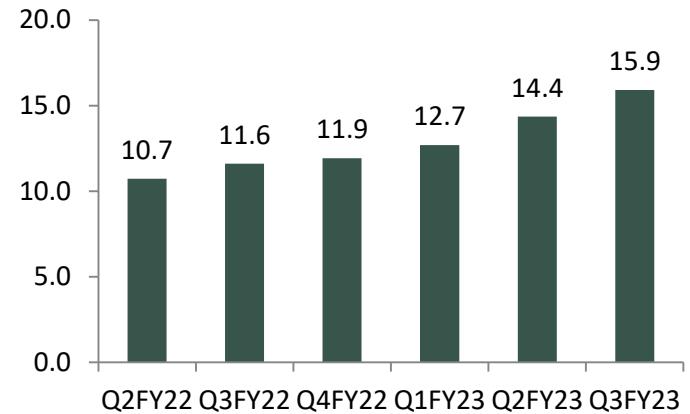
Source: Company; IDBI Capital Research

Exhibit 28: Cost of Deposits inched up sequentially

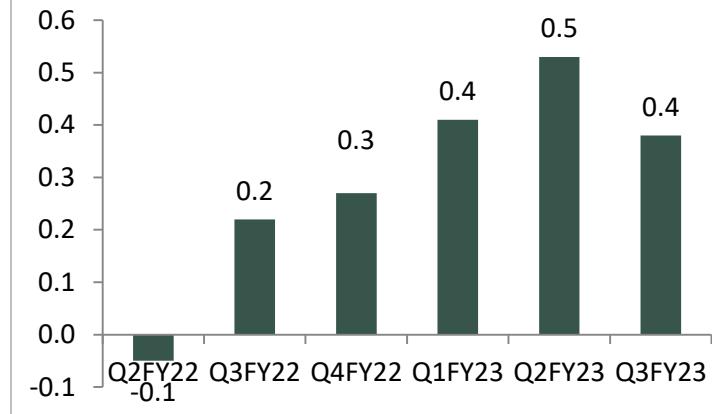
Source: Company; IDBI Capital Research

Exhibit 29: Yield on Advances witnessed sharp up tick QoQ

Source: Company; IDBI Capital Research

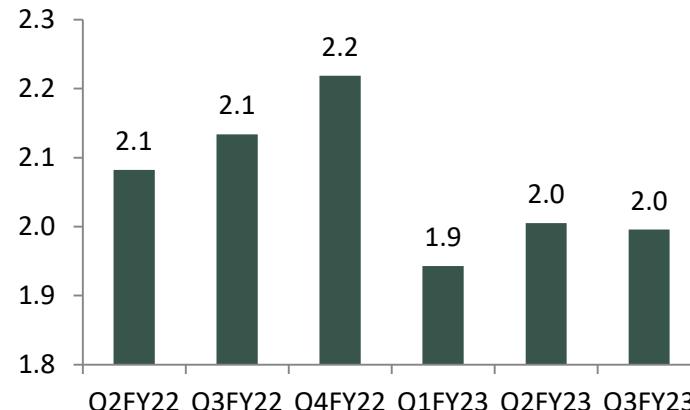
Exhibit 30: Return on Equity continued to trend upward

Source: Company; IDBI Capital Research

Exhibit 31: Credit Cost declined sequentially led by better asset quality

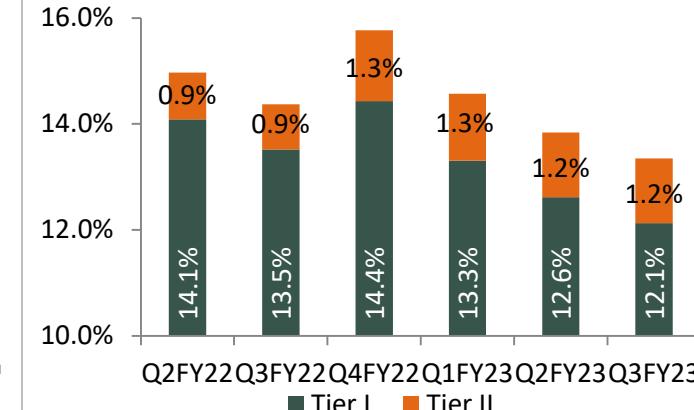
Source: Company; IDBI Capital Research

Exhibit 32: Cost to Assets remained stable QoQ



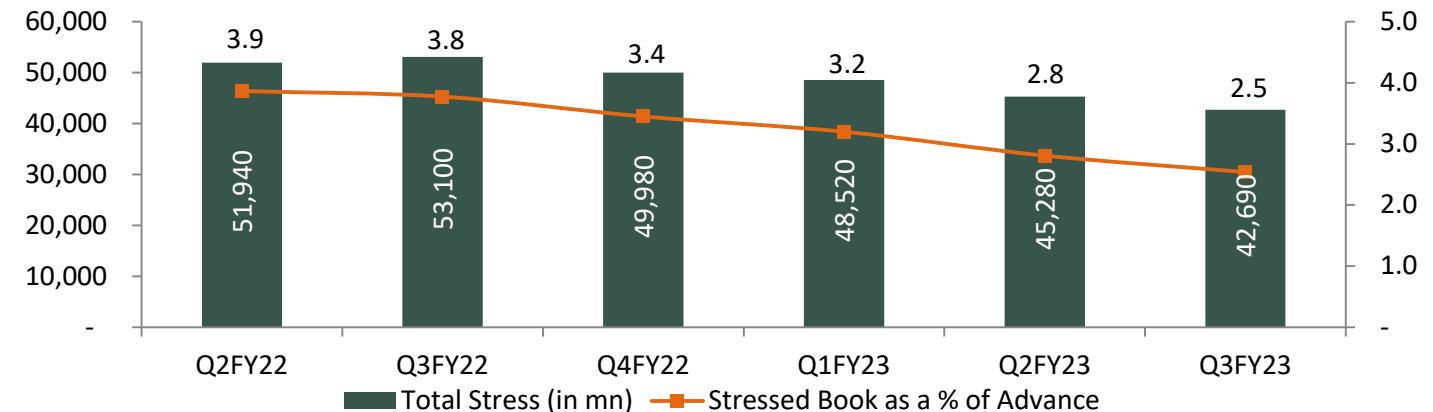
Source: Company; IDBI Capital Research

Exhibit 33: CAR remains comfortable



Source: Company; IDBI Capital Research

Exhibit 34: Stress Book continuing to witness improvement on a sequential basis



Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

	(Rs mn)					
Year-end: March	FY20	FY21	FY22	FY23E	FY24E	FY25E
Net interest income	46,489	55,337	59,620	71,983	82,749	94,205
<i>Change (yoY, %)</i>	11%	19%	8%	21%	15%	14%
Fees	13,183	13,343	17,809	20,536	20,223	23,256
Other Income	6,131	6,244	3,082	1,704	4,736	5,224
Net Revenue	65,803	74,924	80,510	94,223	1,07,708	1,22,685
Operating expenses	33,756	36,917	42,932	47,034	52,001	57,838
Employee expenses	17,724	20,342	23,206	21,758	26,263	28,240
Other expenses	16,032	16,575	19,726	25,275	25,738	29,598
Pre-Provision Profit	32,047	38,007	37,579	47,190	55,707	64,847
<i>Change (yoY, %)</i>	16%	19%	-1%	26%	18%	16%
Provision	11,722	16,634	12,218	8,669	10,049	11,557
PBT	20,325	21,373	25,361	38,520	45,657	53,290
Taxes	4,897	5,470	6,463	9,696	11,492	13,413
<i>Effective tax rate (%)</i>	24%	26%	25%	25%	25%	25%
Net profit	15,428	15,903	18,898	28,825	34,165	39,877
<i>Change (yoY, %)</i>	24%	3%	19%	53%	19%	17%
EPS	7.7	8.0	9.0	13.7	16.2	19.0
Return on Equity (%)	11.1	10.4	10.8	14.4	15.0	15.3
Return on Assets (%)	0.9	0.8	0.9	1.2	1.3	1.3

Balance Sheet

(Rs mn)

Year-end: March	FY20	FY21	FY22	FY23E	FY24E	FY25E
Capital	3,985	3,992	4,205	4,205	4,205	4,205
Reserves	1,41,191	1,57,252	1,83,733	2,08,352	2,38,313	2,73,984
Networth	1,45,176	1,61,244	1,87,938	2,12,558	2,42,518	2,78,190
Deposits	15,22,901	17,26,445	18,17,006	20,90,920	23,98,748	27,52,750
Current deposits	82,398	1,18,603	1,43,883	1,46,364	1,67,912	1,92,693
Saving deposits	3,85,344	4,68,523	5,30,827	6,06,367	6,95,637	7,98,298
Term deposit	10,55,159	11,39,319	11,42,296	13,38,189	15,35,199	17,61,760
Borrowings	1,03,724	90,685	1,53,931	1,72,428	1,71,189	2,09,020
Other liabilities	34,580	35,299	50,588	47,265	46,656	44,530
Total Liab. & Equity	18,06,381	20,13,673	22,09,463	25,23,171	28,59,111	32,84,490
Cash	1,25,746	1,95,913	2,10,103	1,71,015	1,96,668	2,26,168
Advances	12,22,679	13,18,786	14,49,283	17,10,154	19,66,677	22,61,679
Investments	3,58,927	3,71,862	3,91,795	4,60,041	4,87,234	5,57,590
Fixed Assets	4,800	4,911	6,339	7,227	7,588	7,968
Other Assets	94,229	1,22,201	1,51,942	1,74,734	2,00,944	2,31,085
Total assets	18,06,381	20,13,673	22,09,463	25,23,171	28,59,111	32,84,490

Financial Ratios (%)						
Year-end: March	FY20	FY21	FY22	FY23E	FY24E	FY25E
Growth						
Deposits	12.8	13.4	5.2	15.1	14.7	14.8
Advances	10.9	7.9	9.9	18.0	15.0	15.0
NII	11.3	19.0	7.7	20.7	15.0	13.8
Pre-Provision Profit	16.0	18.6	(1.1)	25.6	18.0	16.4
Net Profit	24.0	3.1	18.8	52.5	18.5	16.7
Spreads						
Yield on Assets	8.6	8.0	7.2	7.9	8.0	8.0
Cost of Funds	5.6	4.8	4.1	4.5	4.5	4.5
NIM	3.0	3.2	3.2	3.4	3.4	3.4
CASA	30.7	34.0	37.1	36.0	36.0	36.0
Operating Efficiency						
Cost-to-Income	51.3	49.3	53.3	49.9	48.3	47.1
Cost-to-Assets	2.0	1.9	2.0	2.0	1.9	1.9
Asset Quality						
GNPA	2.8	3.4	2.8	2.5	2.6	2.7
NNPA	1.3	1.2	1.0	0.7	0.9	1.1
Provision Coverage	54.5	65.9	66.4	72.3	67.5	61.6
Credit Cost	1.0	1.3	0.9	0.5	0.5	0.5
Capital Adequacy						
CAR	14.4	14.6	15.8	15.1	14.8	14.8
Tier I	13.3	13.9	14.4	13.9	13.7	13.7
Valuation						
EPS	8	8	9	14	16	19
ABV	67	75	84	97	109	124
P/E	16.7	16.2	14.4	9.4	7.9	6.8
P/ABV	1.9	1.7	1.5	1.3	1.2	1.0
ROE	11.1	10.4	10.8	14.4	15.0	15.3
ROA	0.9	0.8	0.9	1.2	1.3	1.3
RORWA	1.5	1.5	1.6	2.1	2.1	2.2

Source: Company; IDBI Capital Research



Notes

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