

Federal Bank Ltd.

14th July 2023

Promising Growth Ahead

Federal Bank Ltd. (FBL) loan book stood at Rs. 1.9 Trn, which grew by 21% on YoY and 5% on QoQ basis. NII reached Rs. 19 Bn, with ~20% YoY growth and muted QoQ growth, registering a lower NIM at 3.15% compared to 3.31% in Q4 FY23 and 3.22% in Q1 FY23. However, with the entire book almost repriced, the management expects margin expansion to begin from Q2 FY24. The Bank reported 42% YoY growth and a 5% QoQ degrowth in earnings at Rs. 8.8 Bn. The Bank maintained its loan book mix between retail and wholesale at 54:46, on the back of 20% and 22% YoY growth and 6% and 5% QoQ growth, respectively. During the quarter, the Bank expanded its branch network by adding 12 new branches, bringing the total count to 1,366 branches, continuing to hold a dominant market share of 52% in rural areas.

Strong growth in loan book

FBL registered a ~21% YoY growth and a 5% QoQ growth to close the book at Rs. 1,866 Bn in Q1 FY24. While the retail and wholesale mix was maintained at 54:46, segments like retail others (56% YoY, 38% QoQ), auto (30% YoY, 6% QoQ), personal (62% YoY, 17% QoQ), and CV/CE (72% YoY, 12% QoQ) exceeded the loan book growth. The management has guided that the book is expected to grow at 18-20% in FY24.

Fintech partnerships thriving

Fintech partnerships have increased their contribution to their business with FBL. The contribution of fintech in the incremental savings bank account increased from 33% in FY23 to 61% during the quarter. The share of fintech in personal loan disbursement increased from 24% in FY23 to 53% in Q1 FY24. However, despite the contribution in the number of credit cards issued by fintech dipped from 81% in FY23 to 77% in Q1 FY24, the number of cards issued by the Company and fintech partners has increased up 5x, and their spending has soared by ~12 times YoY.

View & Valuation

We believe that the Bank will be able to achieve 18-20% growth in the loan book and revert to 3.3% NIM which will lead to an improvement in ROA by 5-10 basis points. On the back of these rationales, we revise our estimates and maintain a BUY rating on FBL with a target price of Rs. 169 on 1.5x FY24E Adj. book value, indicating a 30% upside.

BUY

CMP Rs. 130

TARGET Rs. 169 (+30%)

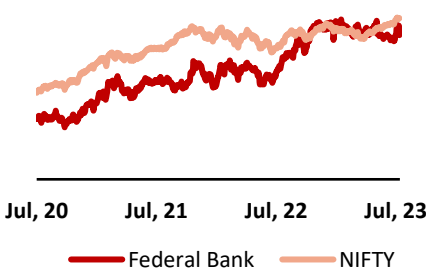
Company Data

MCAP (Rs. Mn)	2,74,749
O/S Shares (Mn)	2,118
52w High/Low	143 / 96
Face Value (Rs.)	2
Liquidity (3M) (Rs. Mn)	1,725

Shareholding Pattern %

	Jun 23	Mar 23	Dec 22
Promoters	0	0	0
FIIIs	26.94	26.94	27.72
DIIIs	43.78	43.78	42.33
Non-Institutional	29.28	29.28	29.97

Federal Bank vs Nifty



Source: Keynote Capitals Ltd.

Key Financial Data

(Rs Bn)	FY23	FY24E	FY25E
NII	78	81	95
PPOP	51	53	63
Net Profit	32	34	41
Advances	1,820	2,129	2,512
ROE (%)	14%	13%	14%
ROA (%)	1.2%	1.1%	1.2%

Source: Company, Keynote Capitals Ltd. estimates

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Federal Bank Ltd. | Quarterly Update

Q1 FY24 result update

Result Highlight (Rs. Mn)

Particulars	Q1FY24	Q1FY23	Change % (Y-o-Y)	Q4FY23	Change % (Q-o-Q)	FY23
Net Interest Income	20,953	17,393	20%	20,747	1%	78,365
Other Income	7,413	4,751	56%	7,684	-4%	24,362
Net Income	28,366	22,144	28%	28,431	0%	1,02,728
Operating Expense	14,694	11,758	25%	14,492	1%	52,112
Pre-provision Operating Profit	13,671	10,386	32%	13,940	-2%	50,616
Provisions	1,647	1,752	-6%	1,253	31%	7,986
PBT	12,024	8,634	39%	12,687	-5%	42,629
Tax	3,107	2,204	41%	3,292	-6%	10,872
Minority Interest	138	110	25%	96	43%	451
Share of Associate	22	23	-5%	240	-91%	341
PAT	8,801	6,342	39%	9,539	-8%	31,647
EPS	4.1	3.0	37%	4.5	-8%	14.8

Source: Company, Keynote Capitals Ltd.

Loan Book mix

Particulars	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Growth Y-o-Y (%)	Growth Q-o-Q (%)
Retail Advances	54%	54%	54%	54%	54%	20%	6%
Retail	32%	32%	32%	32%	31%	17%	4%
Housing	15%	15%	15%	15%	14%	8%	-5.5%
Gold	3%	3%	3%	2%	2%	-15%	2%
LAP	6%	6%	6%	6%	6%	19%	4.1%
Others	4%	4%	4%	4%	5%	56%	38%
Auto	3%	3%	3%	3%	3%	30%	6%
Personal	1%	1%	1%	1%	2%	62%	17%
Agri	13%	13%	13%	13%	13%	26%	8%
Business Banking	8%	8%	8%	8%	8%	18%	7%
CV / CE	1%	1%	1%	1%	1%	72%	12%
Wholesale Advances	46%	46%	46%	46%	46%	22%	5%
Commercial	10%	10%	10%	10%	10%	20%	6%
CIB	36%	36%	36%	36%	36%	22%	4%
Total Funded Assets (Rs. Bn)	1,544	1,640	1,710	1,774	1,866	21%	5%

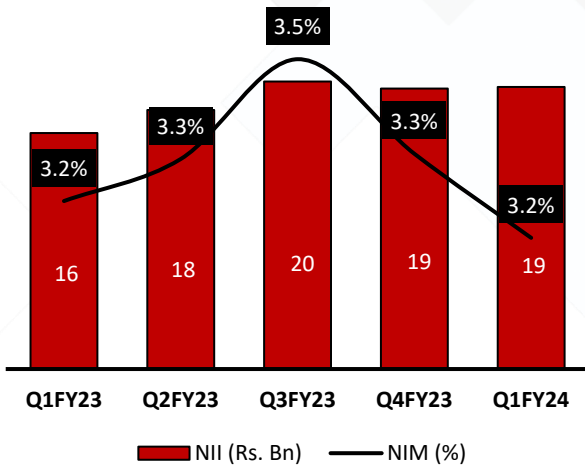
Source: Company, Keynote Capitals Ltd.

Deposits mix

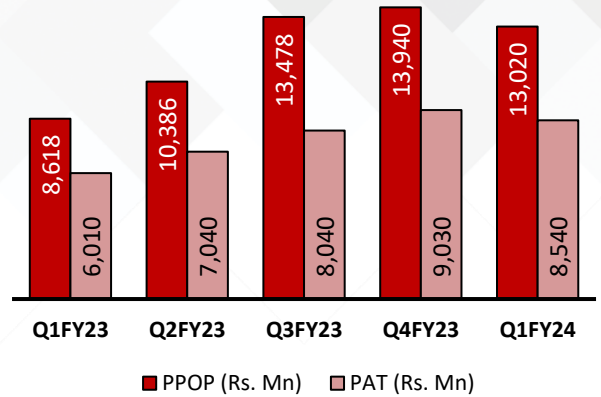
Particulars	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Growth Y-o-Y (%)	Growth Q-o-Q (%)
CASA Ratio	37%	36%	34%	33%	32%	5%	2%
NRE Deposit	37%	36%	34%	33%	32%	5%	0%
Term Deposit	26%	28%	32%	34%	36%	68%	11%
Total Deposits (Rs. Bn)	9,277	10,563	11,335	13,303	14,464	21%	4%

Source: Company, Keynote Capitals Ltd.

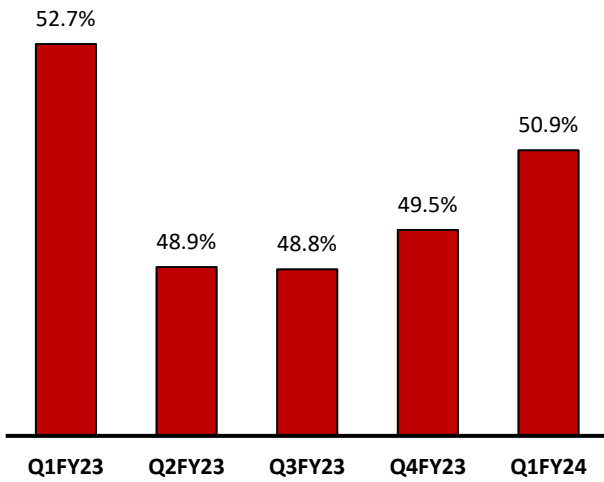
NII remained flat and NIM declined



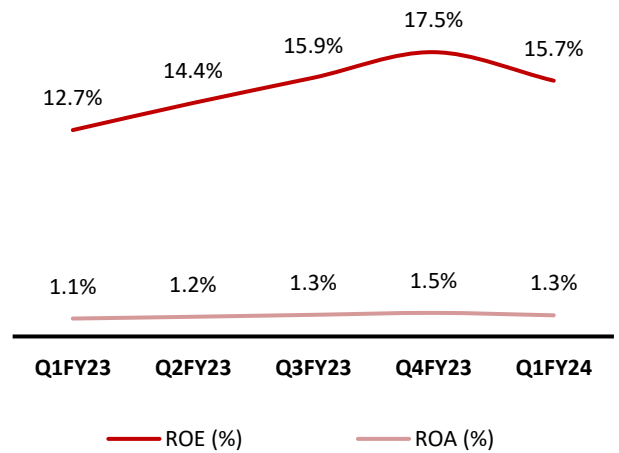
PPOP and PAT declined 7% and 5% on QoQ basis respectively



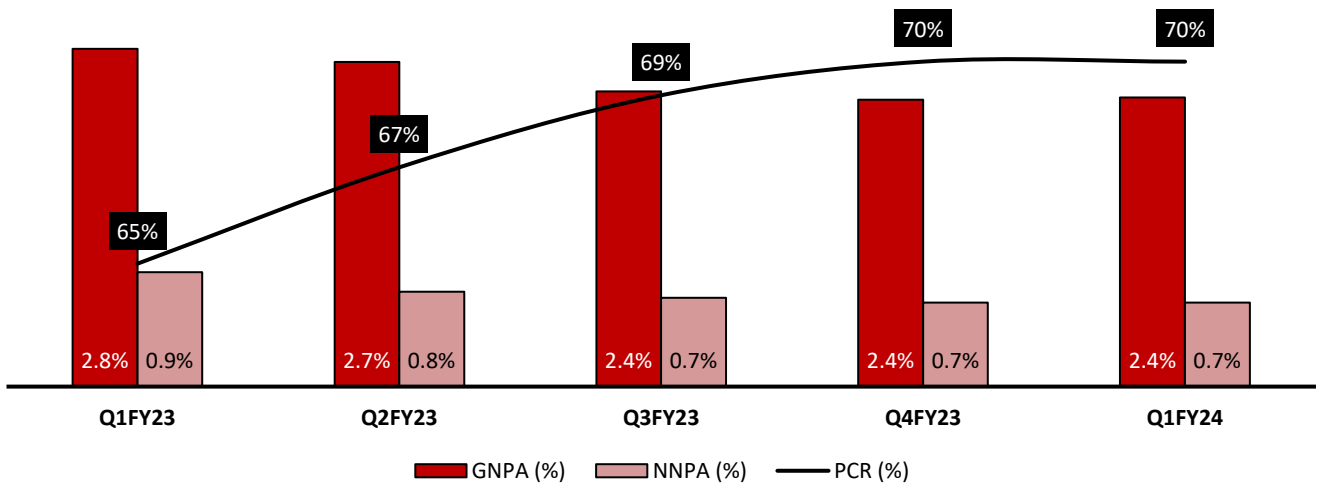
Cost to Income ratio (%)



ROE and ROA declined



Asset Quality Maintained (%)



Source: Company, Keynote Capitals Ltd.

Federal Bank Ltd. | Quarterly Update

Q1 FY24 Conference Call Takeaways

Loan Book

- The margin expansion is expected to happen in Q2 FY24 on the back of the increased cost of lending from 9.21% in Q1 FY24 to 9.27% in Q2 FY24, and the cost of funds is expected to be lower than the rise in the yield on advance. The rate increase on deposits has already happened, and the yield expansion on credit and business mix is beginning to show.
- Within the MSME segment, ~55-60% of the book is working capital, and the remaining 40-45% of the book is term loans.
- The loan mix classified by benchmark stood with 49% repo-linked, 27% fixed rate, 14% MCLR, and ~6% staff loans and ~4% base rate/foreign currency.
- The contribution of high yielding loans in revenue stood at ~30%, despite having ~34% share in the loan book. This is because of certain revenue calculation techniques which consider revenue for some segments on a gross basis while others on a net basis.
- ~69% of the CV/CE book accounts for PSL, which also finances school buses which is not PSL.
- Retail slippages for the quarter stood at 1.92%, which is highest in the last 4 quarters, attributes ~30% of the book to restructured book for Covid'19.
- The home loan segment, operated in 5-6 geographies, is undergoing pricing pressure due to intense competition and is more prone to slippages.
- ~40-45% of the loan book has been outside Kerela for the last two years, whereas the incremental growth outside Kerela has been higher than that in Kerela.

Deposits

- The combined share of CASA and term deposits dropped from 92% in Q1 FY23 to 82% in Q1 FY24. The management has guided to maintain the same at ~85%.
- Rs. 8-10 Bn or 15% of incremental deposits are sourced from the fintech partners
- The incremental cost of term deposits stood at ~6.5%
- The Bank's 70% network is in semi-urban and rural areas.

Federal Bank Ltd. | Quarterly Update

Others

- The other income of ~Rs. 1.6 Bn represented 15% recoveries previously written off, ~9% dividend from subsidiaries, ~7% revaluation of the investment, and 32% against the sale of PSL.
- The core fee income was registered at ~Rs. 5.4 Bn, which is growing at 20-22% YoY.
- Employee costs increased by 24% YoY to account for the impact of yield movements on the pension and traditional Q1 expenses like leave travel. The management does not anticipate an improvement in staff costs going forward. Other operating expenses witnessed a 26% YoY growth, primarily driven by variable costs and the depreciation of projects that became operational last year.

Guidance

- The retail-wholesale mix is guided to be around 55:45, close to the current 54:46.
- The management maintained their guidance of ~18-20% YoY growth on the loan book for FY24.
- The guided NIM for Q2FY24 is ~3.20% (7-8 bps improvement QoQ) FY24 is close to 3.30%.
- The ROA is expected to improve by 5-10 bps in FY24.
- The credit cost is expected to remain ~40 bps, close to the current 41 bps.
- The share of unsecured book shall stay less than 10%.
- No segment shall exceed 15% of the book.

Financial Statement Analysis

Profit & Loss

Y/E Mar, Rs. Mn	FY22	FY23	FY24E	FY25E	FY26E
Net Interest Income	64,222	78,365	80,934	94,724	1,09,048
Other Income	21,209	24,362	24,280	29,365	33,805
Net Income	85,431	1,02,728	1,05,214	1,24,089	1,42,853
Operating Expenses	45,922	52,112	52,607	60,804	69,998
Pre-Provision Operating Profit	39,509	50,616	52,607	63,285	72,855
Provisions	13,047	7,986	7,897	8,818	9,584
Profit Before Tax	26,463	42,629	44,710	54,468	63,272
Tax	6,809	10,872	11,178	13,617	15,818
Profit After Tax	19,654	31,758	33,533	40,851	47,454

Balance Sheet

Y/E Mar, Rs. Mn	FY22	FY23	FY24E	FY25E	FY26E
Share Capital	4,205	4,232	4,232	4,232	4,232
Reserves & Surplus	1,91,403	2,20,511	2,47,338	2,80,018	3,17,981
Total Equity	1,95,608	2,24,744	2,51,570	2,84,250	3,22,213
Deposits	18,16,775	21,29,885	25,34,398	29,55,406	34,87,379
Borrowings	1,95,874	2,58,620	2,32,872	1,71,350	56,969
Other Liabilities & Provisions	54,153	66,792	93,500	99,800	99,800
Total Liabilities	22,62,410	26,80,041	31,12,340	35,10,816	39,66,361
ASSETS					
Cash and Balance	2,11,361	1,78,039	2,24,627	2,79,099	2,74,396
Investments	3,90,652	4,87,022	5,45,081	4,69,122	4,69,122
Advances	14,99,515	18,19,568	21,28,894	25,12,095	29,64,272
Fixed Assets & Others	1,60,883	1,95,401	2,13,738	2,50,490	2,58,571
Total Assets	22,62,410	26,80,041	31,12,340	35,10,816	39,66,361

Ratios

	FY22	FY23	FY24E	FY25E	FY26E
Growth YoY (%)					
Advance Growth (%)	13.7%	21.3%	17.0%	18.0%	18.0%
Deposit Growth (%)	5.2%	17.2%	19.0%	16.6%	18.0%
NII Growth (%)	16.1%	22.0%	3.3%	17.0%	15.1%
PPOP Growth (%)	4.0%	28.1%	3.9%	20.3%	15.1%
Ratios					
NIM (%)	3.2%	3.4%	3.0%	3.1%	3.1%
Cost to Income Ratio	53.8%	50.7%	50.0%	49.0%	49.0%
C/D Ratio	82.5%	85.4%	84.0%	85.0%	85.0%
CASA Ratio (%)	37.1%	32.7%	33.2%	34.0%	34.0%
ROE (%)	10.0%	14.1%	13.3%	14.4%	14.7%
ROA (%)	0.9%	1.2%	1.1%	1.2%	1.2%
Asset Quality					
GNPA	2.9%	2.4%	2.2%	2.0%	2.0%
NNPA	1.0%	0.7%	0.6%	0.5%	0.5%
PCR (%)	63.9%	68.9%	72.7%	75.0%	75.0%
Credit Cost (%)	3.2%	1.5%	1.2%	1.0%	1.0%
Valuation					
P/BV (x)	1.4	1.2	1.1	1.0	0.8
Price-ABV (x)	1.5	1.3	1.1	1.0	0.9

Source: Company, Keynote Capitals Ltd.

KEYNOTE Rating History

Date	Rating	Market Price at Recommendation	Upside/Downside
17 th Apr 2023	BUY	131.3	+24.9%
8 th May 2023	BUY	128.6	+32.2%
14 th July 2023	BUY	130.0	+30.0%

Rating Methodology

Rating	Criteria
BUY	Expected positive return of > 10% over 1-year horizon
NEUTRAL	Expected positive return of > 0% to < 10% over 1-year horizon
REDUCE	Expected return of < 0% to -10% over 1-year horizon
SELL	Expected to fall by >10% over 1-year horizon
NOT RATED (NR)/UNDER REVIEW (UR)/COVERAGE SUSPENDED (CS)	Not covered by Keynote Capitals Ltd/Rating & Fair value under Review/Keynote Capitals Ltd has suspended coverage

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