

## Federal Bank

Buy

Choice

Solid Business Growth Continues, Profitability Impacted by Elevated Costs

Federal Bank delivered a quarter marked by strong loan growth and continued expansion in key business segments, driven by retail, commercial banking, and microfinance. Advances grew substantially by 19% YoY, and deposits continued to show healthy momentum, up 16% YoY. However, the quarter was not without challenges, as profitability came under pressure due to rising operating costs and a marginal dip in Net Interest Margin (NIM). The Cost-to-Income ratio saw an uptick, driven by continued investments in branch expansions and technology upgrades, as well as a rise in pension-related expenses. Despite these pressures, Federal Bank's asset quality improved, with a reduction in both Gross and Net NPA ratios. Looking forward, the bank remains well-positioned for robust business growth with stable asset quality, and management is optimistic about reducing cost pressures and further improving profitability in FY25.

- **Advances Surging Across Segments** - Advances grew by 19% YoY and 4.3% QoQ, reaching ₹2,690 billion. This was supported by robust growth in the retail segment (22% YoY) and commercial vehicle/construction equipment (CV/CE) loans, which saw a notable increase of 43.83% YoY. Additionally, the microfinance book expanded by 75.83% YoY, underscoring the bank's focus on high-growth, high-margin segments. Deposits rose by 16% YoY and 1% QoQ, with the CASA ratio at 30.07%, reflecting a minor dip due to the increasing preference for term deposits. We expect continued traction in loan growth at a CAGR of 17.2% over FY24-26, supported by the retail and commercial banking portfolios.
- **Profitability Under Pressure, NIM Remains Stable**- Net Interest Income (NII) grew by 15% YoY and 3% QoQ, reaching ₹23.67 billion, driven by healthy loan growth. The Net Interest Margin (NIM) stood at 3.12%, reflecting a marginal decline of 9 bps YoY due to higher funding costs. Pre-provision Operating Profit (PPOP) was ₹15.65 billion, growing by 4% QoQ, but profitability was impacted by elevated operating expenses. The Cost-to-Income (C/I) ratio increased to 53.01%, compared to 52.47% in Q2 FY24, though management expects improvements in FY25 as cost pressures ease.
- **Asset Quality Remains Stable**: Asset quality improved, with the Gross NPA ratio reducing to 2.09%, down 17 bps YoY, and the Net NPA ratio improving to 0.57%. Recoveries were strong at ₹2.72 billion, higher than in previous quarters. The provision coverage ratio (PCR) excluding technical write-offs improved to 71.82%. Credit cost stood at 0.30% for the quarter, with expectations for it to remain stable at around 30 bps in FY25. Management remains confident in maintaining healthy asset quality, given strong collection efficiencies and recovery momentum.
- **PAT Marginally Misses Estimates**: Net profit grew by 11% YoY and 5% QoQ, reaching an all-time high of ₹10.57 billion, driven by core income growth and better asset quality. However, PAT was slightly below estimates due to higher operating costs. We expect net profit to grow at a CAGR of 30% over FY24-26, supported by steady business growth, improving cost efficiency, and stable asset quality. Return on Assets (RoA) improved marginally to 1.28% in Q2 FY25, with expectations for it to increase by 12-15 bps annually.

**View & Valuation:** Federal Bank is poised for strong growth, driven by its focus on retail and high-margin segments, along with efforts to improve operational efficiency. The Cost-to-Income ratio is expected to decline in FY25, further boosting profitability. Asset quality remains stable, and credit costs are well-controlled. We anticipate a 30% CAGR in PAT over FY24-26, with RoA improving to 1.6% by FY26. Based on solid growth prospects and improving profitability, we maintain a 'BUY' rating with a target price of ₹222, valuing the bank at 1.47x P/ABV FY26E..

## Financial Snapshot (Rs bn)

Year end: March	FY22	FY23	FY24	FY25E	FY26E
NII	60	72	83	107	136
Gr. (%)	7.7	21.3	14.7	29.5	27.0
NIM (%)	3.16	3.31	3.21	3.60	3.89
PPOP	38	48	52	72	92
A.PAT	19	30	37	49	63
Eq./As. (%)	8.5	8.3	9.4	9.4	9.3
RoE (%)	11.8	17.7	14.1	15.4	17.0
CASA(%)	36.9	32.7	29.4	29.6	27.0
GNPA (%)	2.8	2.4	2.1	2.04	2.08
P/ABV (x)	2.2	1.9	1.6	1.4	1.2

Source: Company, CEBPL

Oct 29, 2024

CMP (Rs)	184.70
Target Price (Rs)	222
Potential Upside (%)	20.3%

\*CMP as on 28<sup>th</sup> 2024

## Company Info

BB Code	FB IN EQUITY
ISIN	INE171A01029
Face Value (Rs)	2
52 Week High (Rs)	206
52 Week Low (Rs)	137
Mkt Cap (Rs bn)	452.81
Mkt Cap (\$ bn)	5.39
Shares o/s (bn)	2.4
FY25E ABVPS (Rs)	132.8
FY26E ABVPS (Rs)	155.8

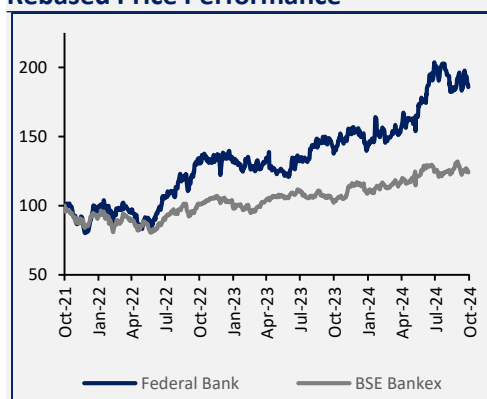
## Shareholding Pattern (%)

	Sep-24	Jun-24	Mar-24
Promoters	-	-	-
FPIs	27.7	28.6	28.6
DIIs	47.2	45.2	45.4
Public	25.1	26.2	26.0

## Relative Performance (%)

YTD	1Y	2Y	3Y
Federal Bank	31.6	39.0	85.8
BSE BANKEX	20.3	23.0	24.1

## Rebased Price Performance



## Quarterly Snapshot (Q2 FY25)

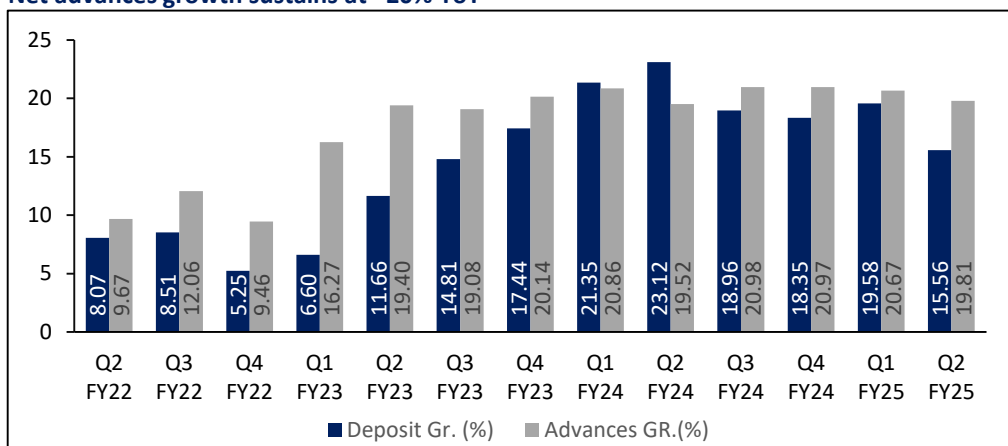
Particulars	(Rs bn)	YoY (%)	QoQ (%)
NII	24	15.1	3.3
NIM (%)	3.12	-10 bps	-4 bps
Fee income	8	18.8	20.2
Opex	18	20.7	3.5
PPOP	16	18.2	4.3
PAT	11	10.8	4.7
Advances	2348	19.8	4.3
Deposits	2691	15.6	1.1
GNPA	49	10.1	3.1
Slippages	13	7.5	-0.6

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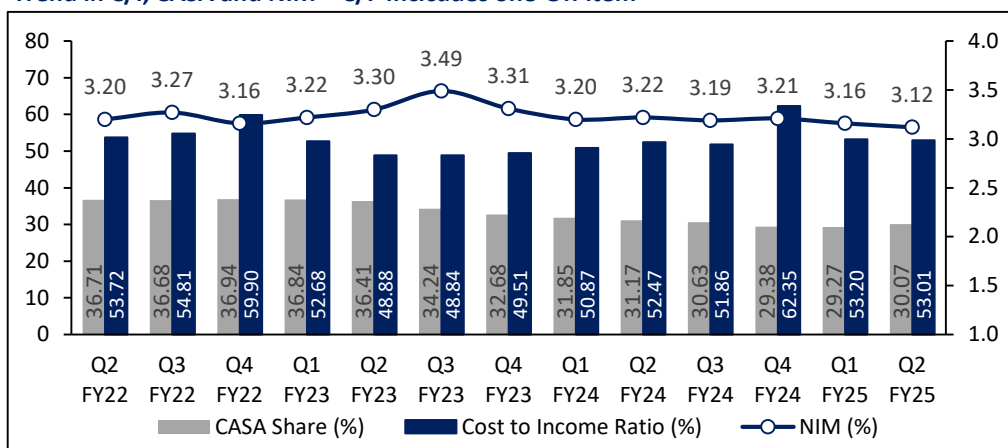
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**Net advances growth sustains at ~20% YoY**



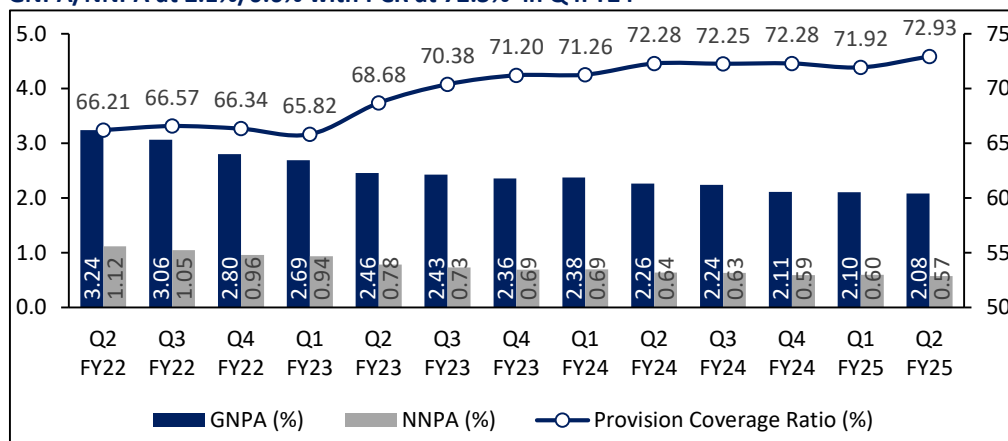
Source: Company, CEBPL

**Trend in C/I, CASA and NIM – C/I Includes one-Off item**



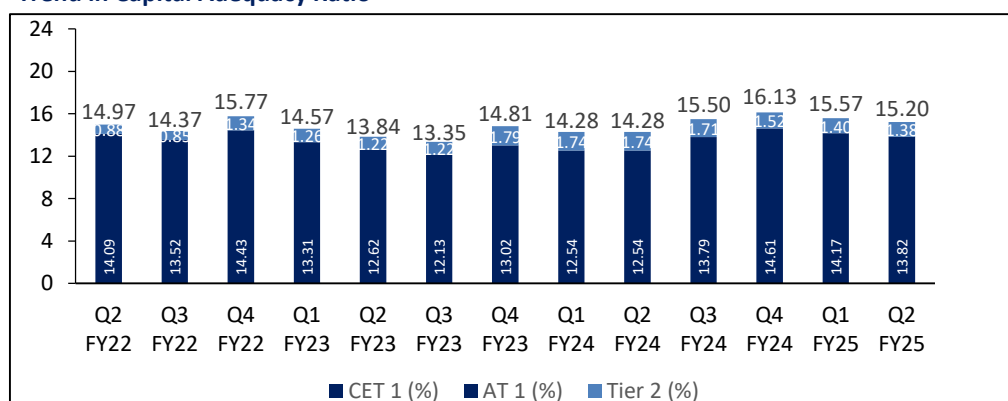
Source: Company, CEBPL

**GNPA/NNPA at 2.1%/0.6% with PCR at 72.3% in Q4FY24**



Source: Company, CEBPL

**Trend in Capital Adequacy Ratio**



Source: Company, CEBPL

## Sequential Quarterly Performance

Particulars (Rs bn)	Q2 FY24	Q3 FY24	Q4 FY24	Q1 FY25	Q2 FY25	YoY (%)	QoQ (%)
Interest Earned	55	57	60	63	66	20.6	3.9
Interest Expended	34	36	38	40	42	23.9	4.2
<b>NII</b>	<b>21</b>	<b>21</b>	<b>22</b>	<b>23</b>	<b>24</b>	<b>15.1</b>	<b>3.3</b>
Other Income	7	9	8	9	10	32.0	5.3
Fees & commissions	7	6	6	7	8	18.8	20.2
Total Income	62	66	67	72	75	21.9	4.1
OPEX	15	15	18	17	18	20.7	3.5
<b>PPOP</b>	<b>13</b>	<b>14</b>	<b>11</b>	<b>15</b>	<b>16</b>	<b>18.2</b>	<b>4.3</b>
P&C (incl NPA)	0	1	-1	1	2	260.7	9.7
PBT	13	13	12	14	14	9.9	3.7
Tax	3	3	3	3	4	7.2	0.9
<b>Net Profit</b>	<b>10</b>	<b>10</b>	<b>9</b>	<b>10</b>	<b>11</b>	<b>10.8</b>	<b>4.7</b>
Outstanding Shares	2	2	2	2	2	4.4	0.1
Dil. EPS (Rs)	4	4	4	4	4	6.2	4.6
<b>Balance Sheet items/ratios (Rs bn)</b>							
Deposits	2,329	2,396	2,525	2,661	2,691	15.6	1.1
CA Deposits	157	153	152	164	174	10.6	5.8
SB Deposits	569	581	590	615	635	11.7	3.4
CASA	726	734	742	779	809	11.5	3.9
Term Deposits	1,603	1,662	1,783	1,882	1,882	17.4	0.0
Advances	1,960	2,069	2,146	2,252	2,348	19.8	4.3
CD (%)	84.2	86.4	85.0	84.6	87.2	309 bps	262 bps
CASA Share (%)	31.2	30.6	29.4	29.3	30.1	-110 bps	80 bps
CAR(%)	14.3	15.5	16.1	15.6	15.2	92 bps	-37 bps
Tier 1 (%)	12.5	13.8	14.6	14.2	13.8	128 bps	-35 bps
CET 1 (%)	0.0	0.0	0.0	0.0	0.0	0 bps	0 bps
<b>Operating ratios (%)</b>							
Credit cost (Annualized)	0.07	0.14	-0.14	0.20	0.21	14 bps	1 bps
CoD	5.52	5.73	5.90	5.84	5.86	34 bps	2 bps
YoA	9.35	9.37	9.48	9.43	9.35	0 bps	-8 bps
NIM	3.22	3.19	3.21	3.16	3.12	-10 bps	-4 bps
YoI	7.35	7.32	7.65	7.77	7.74	39 bps	-3 bps
Cost-Income (C/I) Ratio	52.47	51.86	62.35	53.20	53.01	53 bps	-19 bps
<b>Assets Quality</b>							
Gross NPAs	44	46	45	47	49	10.1	3.1
Net NPAs	12	13	13	13	13	7.5	-0.6
GNPA (%)	2.26	2.24	2.11	2.10	2.08	-18 bps	-2 bps
NNPA (%)	0.64	0.63	0.59	0.60	0.57	-7 bps	-3 bps
Coverage Ratio(%)	72.28	72.25	72.28	71.92	72.93	65 bps	101 bps
RoA(%) (average) - annualized	1.51	1.53	1.31	1.38	1.40	-10 bps	3 bps
<b>Slippages</b>							
Gross slippages	4	5	4	4	4	17.3	2.6
R&U	4	3	5	2	3	-24.2	32.0
Write-offs	0	0	0	0	0	23.1	77.8
Slippages (Net Addition to GNPA)	4	5	4	4	4	16.4	2.4
Slippages (%)	0.98	0.26	0.19	0.20	0.20	-0.79	-0.01
<b>Advances Break-Out</b>							
Gross Advances	1,960	2,069	2,146	2,252	2,348	19.8	4.3
Wholesale Advances	878	928	951	993	1,024	16.7	3.2
Retail Advances	1,082	1,142	1,195	1,259	1,323	22.3	5.1
<b>Network (in num)</b>							
Branches	1,389	1,418	1,504	1,518	1,533		
Total CRMs and ATMs	1937	1962	2015	2041	2052		

Source: Company, CEBPL

## Key Highlights – Q2FY25

**NII growth remained healthy at 15.1%**

**Core fee remained robust on sequential basis.**

**Net Advances grew by 19.8% YoY driven by the retail segments**

**CASA share increases to 30.1% due to strong CASA deposits v/s TD growth.**

**NIM declined by 4 bps QoQ and 10 bps YoY to 3.12% as CoD increased.**

**GNPA dropped by 18 bps YoY and 2 BPS QoQ.**

**Gross advances growth remained healthy at 19.8% Y, driven by Retail**

**Management expressed robust advances and deposits growth for FY25 and FY26**

## CEBPL Estimates vs Actual for Q3FY24

India - Banking: FB IN

Result Snapshot (Rs bn)	Q2 FY25	Q2 FY24	YoY (%)	Q1 FY25	QoQ (%)	EST.	Dev. (%)
NII	24	21	15.11	23	3.28	22	7.6
NIM (%)	3.12	3.22	-10 bps	3.16	-4 bps	3.14	2 bps
Other Income	10	7	31.98	9	5.33	10	-3.6
Total Income	75	62	21.91	72	4.07	73	3.3
OPEX	18	15	20.75	17	3.49	19	-4.6
PPOP	16	13	18.18	15	4.29	16	1.0
P&C	2	0	260.71	1	9.74	1	13.1

Source: Company, CEBPL

## Change in estimates

(Rs bn)	Old		Revised		Change (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
NII	105	133	107	136	2.3	2.6
Other Income	29	40	31	41	6.2	2.2
OPEX	74	96	76	94	3.3	-2.5
P&C	6	8	7	8	13.6	12.3
PAT	47	61	49	63	3.5	3.0
Adj. BVPS (Rs/sh)	132	152	133	156	0.6	2.5
Deposits	2,879	3,349	2,947	3,455	2.4	3.2
Advances	2,459	2,941	2,555	2,949	3.9	0.3
GNPA	54	72	53	68	-1.7	-6.0

Source: Company, CEBPL

## Management Call - Highlights

### Business Growth

- Total Advances: Net advances grew by 4.3% QoQ and 19% YoY to ₹2.69 lakh crore.
- Retail Book: Retail advances up 22% YoY, driven by a 43.83% YoY growth in Commercial Vehicle/Construction Equipment (CV/CE) loans.
- Gold Loans: Gold loan book increased by 31% YoY, reaching ₹29,722 crore.
- MFI and CV/CE: Microfinance book grew by 75.83% YoY, while CV/CE book grew by 44% YoY.
- Deposits: Total deposits grew 16% YoY to ₹2.69 lakh crore, with CASA growing 3.91% QoQ. CASA ratio stood at 30.07%.

### Profitability

- Net Profit: Highest-ever quarterly net profit of ₹1,057 crore, up 11% YoY.
- Net Interest Income (NII): NII rose by 15% YoY to ₹2,367 crore.
- Operating Profit: Operating profit reached ₹1,565 crore, reflecting an 18% YoY growth.
- Fee Income: Fee income hit ₹784 crore, growing by 19% YoY.

### Capital and Liquidity

- CRAR: Capital Adequacy Ratio (CRAR) stood at 15.20%, while Common Equity Tier 1 (CET1) was at 13.82%.

### Asset Quality

- Provision Coverage Ratio (PCR): PCR improved to 71.82%, increasing by 103 bps QoQ.
- Credit Cost: Credit cost for Q2 FY25 was at 30 bps.
- GNPA/NNPA: Gross NPA decreased to 2.09%, while Net NPA improved to 0.57%.
- Recovery and Upgrades: Recoveries and upgrades amounted to ₹272 crore for Q2.

### Digital & Innovation

- Loan Growth through Digital: Continued growth in digital loan disbursements, including partnerships in high-margin lending products.
- Fintech Collaborations: Fintech partnerships continue to drive customer acquisition, loan disbursements, and CASA growth.

### Other Key Metrics

- Return on Assets (RoA): RoA remained stable at 1.28%.
- Return on Equity (RoE): RoE was 13.65%.
- Net Interest Margin (NIM): NIM stood at 3.12%, reflecting a marginal decline QoQ.

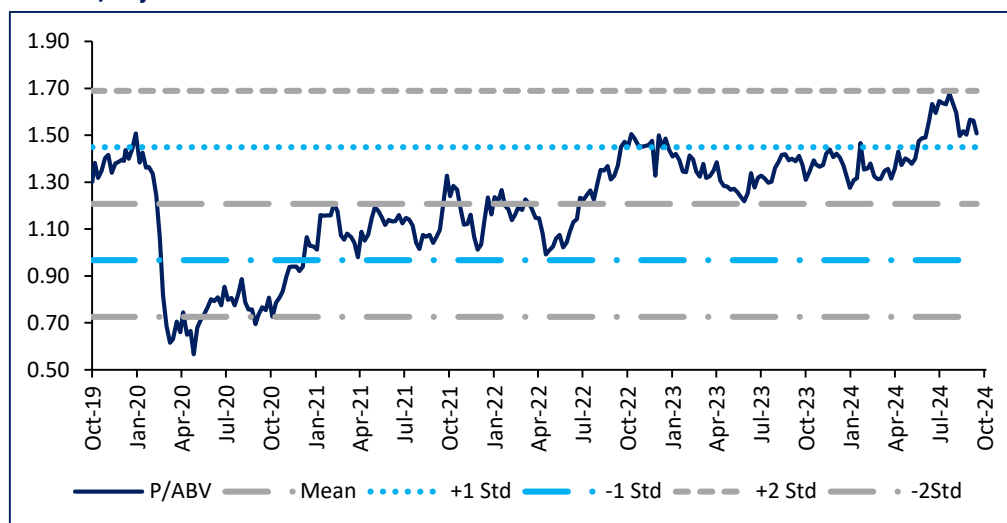
### View & Valuation

: Federal Bank is poised for strong growth, driven by its focus on retail and high-margin segments, along with efforts to improve operational efficiency. The Cost-to-Income ratio is expected to decline in FY25, further boosting profitability. Asset quality remains stable, and credit costs are well-controlled. We anticipate a 30% CAGR in PAT over FY24-26, with RoA improving to 1.6% by FY26. Based on solid growth prospects and improving profitability, we maintain a 'BUY' rating with a target price of ₹222, valuing the bank at 1.47x P/ABV FY26E..

### Risks to investment

- Concertation Risk
- Margin risk

### 12MF P/Adjusted Book Value



Source: Company, CEBPL

## Financial Summary (Standalone in INR Mn.)

## Profit And Loss Statement

Income Statement	FY22	FY23	FY24	FY25E	FY26E
Interest Earned	137	168	222	274	316
Growth (%)	34.2	39.1	36.9	23.3	15.7
Interest Expended	77	96	139	166	180
Growth (%)	34.1	41.6	37.4	19.5	8.3
Net Interest Income	60	72	83	107	136
Net Interest Margin (%)	3.16	3.31	3.21	3.60	3.89
Other Income	21	23	31	41	49
% of Interest Income	13.3	12.2	12.2	14.9	15.6
Total Income	158	191	253	314	366
Growth (%)	33.5	39.9	36.3	24.4	16.4
Operating & Other expenses	43	48	62	76	94
PPOP	38	48	52	72	92
P&C	12	8	2	7	8
P&C % of Advances	0.8	0.4	0.1	0.3	0.3
Operating Profit before Tax	25	40	50	65	84
Growth (%)	39.9	43.1	31.9	30.6	29.0
Pre-tax Margin %	16.1	21.1	19.7	20.7	22.9
Tax	6	10	13	16	21
% of PBT	25.5	25.6	25.3	25.2	25.1
Reported PAT	19	30	37	49	63
Net Profit Margin %	12.0	15.7	14.7	15.5	17.2
Extraordinary Income	0	0	0	0	0
Adjusted PAT	19	30	37	49	63
Growth (%)	18.9	59.3	23.6	30.8	29.2

## Balance Sheet

Balance Sheet	FY22	FY23	FY24	FY25E	FY26E
Cash with RBI and Banks	100	126	115	127	220
Investments	392	490	609	707	811
Advances	1,449	1,744	2,094	2,555	2,949
Fixed assets	6	9	10	9	9
Other assets	152	183	181	235	277
<b>TOTAL ASSETS</b>	<b>2,209</b>	<b>2,603</b>	<b>3,083</b>	<b>3,633</b>	<b>4,267</b>
Capital	4	4	5	5	5
Reserves and Surplus	184	211	286	335	393
Deposits	1,817	2,134	2,525	2,947	3,455
Borrowings	154	193	180	234	270
Other liabilities and provisions	51	61	87	112	145
<b>TOTAL CAPITAL AND LIABILITIES</b>	<b>2,209</b>	<b>2,603</b>	<b>3,083</b>	<b>3,633</b>	<b>4,267</b>

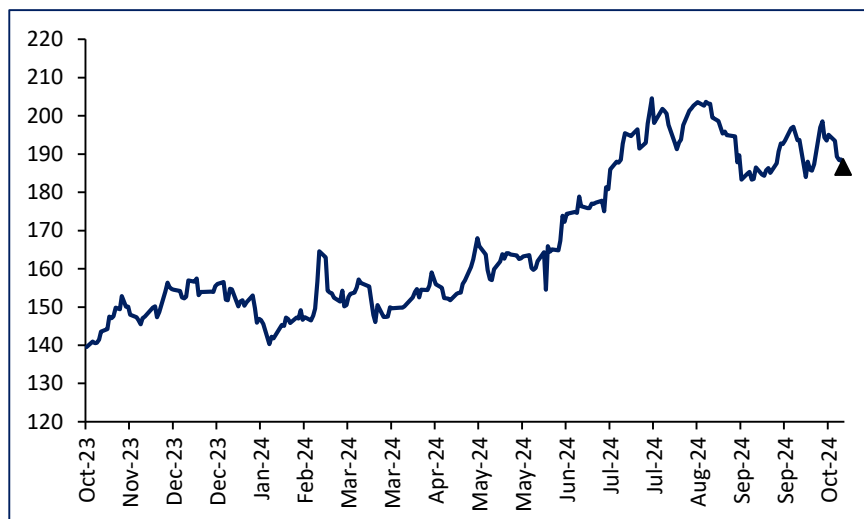
Source: Company, CEBPL

## Financial Ratios

Financial Ratios	FY22	FY23	FY24	FY25E	FY26E
<b>Return / Profitability Ratios (%)</b>					
Net interest margin (NIM)	3.2	3.3	3.2	3.6	3.9
Yield on Advances	8.1	8.5	9.4	9.6	9.4
Yield on Investments	6.8	7.0	7.7	7.5	7.8
EPS (Diluted) (Rs)	9.0	14.2	15.3	19.8	25.6
RoA	0.9	1.3	1.3	1.4	1.6
RoE	10.8	14.9	14.7	15.4	17.0
Cost of Deposits	4.3	5.1	5.9	5.8	5.3
<b>Operating ratios (%)</b>					
Credit to Deposit (C/D)	79.8	81.8	82.9	86.7	85.4
Cost to Income (C/I)	53.3	49.9	54.5	51.6	50.3
CASA Share	36.9	32.7	29.4	29.6	27.0
Investment / Deposit	21.6	23.0	24.1	24.0	23.5
Non Interest Income / Total Income	13.3	12.2	12.2	13.0	13.5
<b>Capital adequacy (%)</b>					
Tier-1	0.0	0.0	0.0	0.0	0.0
Tier-2	14.4	13.0	14.6	14.4	14.6
CAR (BASEL III)	15.8	14.8	16.1	15.8	16.0
Equity / Assets	8.5	8.3	9.4	9.4	9.3
Loans / Assets	65.6	67.0	67.9	70.3	69.1
Investments / Assets	17.7	18.8	19.7	19.4	19.0
Dividend payout	20.0	7.0	10.5	9.6	11.7
<b>Asset Quality ratios (%)</b>					
Gross NPA	2.8	2.4	2.1	2.0	2.1
Net NPA	1.0	0.7	0.6	0.5	0.5
Coverage Ratio	66.3	71.2	72.3	73.3	74.6
Slippage Ratio	1.3	1.0	0.9	1.1	1.5
Credit cost	0.8	0.4	0.1	0.3	0.3
<b>Per Share Data (Rs)</b>					
EPS (Diluted)	9.0	14.2	15.3	19.8	25.6
DPS	1.8	1.0	1.6	1.9	3.0
BVPS	89.3	101.7	119.5	138.6	162.2
Adjusted BVPS	82.7	96.0	114.3	132.8	155.8
<b>Valuation ratios (x)</b>					
P/E (x)	21.7	13.7	12.8	9.8	7.6
P/BV (x)	2.2	1.9	1.6	1.4	1.2
P/ABV (x)	2.4	2.0	1.7	1.5	1.3
<b>Growth ratios (%)</b>					
Advances	9.9	20.4	20.0	22.0	15.4
Deposits	5.2	17.4	18.3	16.7	17.2
Net Interest Income (NII)	7.7	21.3	14.7	29.5	27.0
Interest Earned	-0.7	23.0	32.0	23.3	15.7
PAT	18.9	59.3	23.6	30.8	29.2

Source: Company, CEBPL

## Historical recommendations and target price: FB IN



### FB IN Bank

Date	Rating	CMP	Target Price
21-Apr-23	OUTPERFORM	131	166
07-May-23	OUTPERFORM	128	166
14-Jul-23	OUTPERFORM	129	168
17-Jan-24	Neutral	149.7	144.3
03-May-24	Buy	191.0	244
29-Oct-24	Buy	184.7	222

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