

THE FEDERAL BANK LIMITED | Banking

Asset quality in check; Strong growth guidance for FY23

LKP

Price Analysis

Federal Bank has reported 4QFY22 earnings in line with our expectations and the positive pointers are a) lower slippages (₹3.6bn v/s ₹4.4bn in 3QFY22) resulted in GNPA and NNPA reduction in absolute term as well as the ratio, b) restructuring pool flat with 21% coverage, c) reduction in provisioning expenses with stable PCR, d) Credit growth was at par of 10% YoY and 3% QoQ led by SME book, and e) quarterly profit reached ₹5bn for the second time with ROA above 1%. However, the disappointments are 1) below par NII growth (7.4% YoY) with NIMs compression of 16bps, and 2) Operating expenses higher because of staff cost. The bank's credit quality is in check with no major hiccups. However, the business growth will be key monitor-able as management guided 15% credit growth for FY23. A consistent growth may drive stock re-rating with higher valuation than 1.0x of book value

Lower slippages led to GNPA reduction; restructuring improved: Reported fresh slippages were down sequentially to ₹3.6bn v/s ₹4.4bn reported in the previous quarter. SME book (BuB + CuB) contributed 35% of the fresh slippages where Agriculture book contributed 42% of total slippages. The retail slippages down at ₹0.86bn against ₹0.95bn in 4QFY22. The bank's up-gradation and recoveries moderated sequentially at ₹4.1bn v/s ₹5bn in previous quarter. Moreover, write-offs are at higher side of ₹2.5bn. A lower slippage and higher write-offs had resulted in reduction in GNPA ratio. The bank's GNPA/NNPA/PCR stood at 2.8%/0.96%/66% v/s 3.06%/1.05%/66% in the previous quarter. The absolute GNPA down sequentially by 6%. The total standard restructuring reported worth ₹35.4bn (2.4% of book); decreased sequentially from ₹37.2bn (2.65% of book). The restructuring amount is line with the expectations. Retail restructuring contributes ~60% of total amount. The management expects a relapse rate of ~30% from the pool in 2-3 years and would maintain a 65% PCR on the same as prudent measure.

Key Financials (₹ mn)	FY20	FY21	FY22	FY23E	FY24E
NII	46,489	55,337	59,620	72,222	86,422
Operating Profit	32,047	37,869	37,125	45,221	54,974
Reported Profits	15,428	15,903	18,444	26,415	32,578
Net Worth	1,45,126	1,61,186	1,87,888	2,14,303	2,46,881
Loan & Advances	12,22,679	13,18,786	14,49,283	16,66,676	19,33,344
Int. Bearing Liabilities	16,26,625	18,17,130	19,70,937	22,46,117	25,83,107

Key Ratios (%)	FY20	FY21	FY22	FY23E	FY24E
NIM's	2.9	3.1	3.0	3.3	3.4
C/I	51.3	49.4	53.6	52.6	51.4
Gross NPA	2.8	3.4	2.8	2.5	2.0
Tier 1	13.8	14.4	15.5	15.4	15.4
Adj. RoA	0.9	0.8	0.9	1.1	1.2
Adj. RoE	11.1	10.4	10.6	13.1	14.1

Rating	BUY
Current Market Price (₹)	91
12 M Price Target (₹)	116
Potential upside (%)	27

Stock Data

FV (₹) :	2
Market Cap Full (₹ bn) :	193
Market Cap Free Float (₹ bn) :	182
52-Week High / Low (₹) :	108 / 77
2-Year High / Low (₹) :	108 / 37
1 Yr Avg. Dly Traded Volume (in lakh)	197
BSE Code / NSE Symbol	500469 / FEDERALBNK
Bloomberg :	FB IN

Shareholding Pattern

(%)	Mar-22	Dec-21	Sep-21	Jun-21
FPIs	26.01	25.23	25.92	24.05
MFs	33.61	32.58	32.72	32.59
AIF's	1.40	0.52	0.46	0.45
Insurance	8.23	8.55	9.34	10.83
Others	30.75	33.12	31.56	32.08

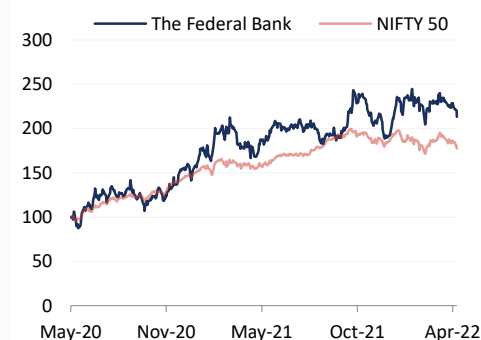
Source: BSE

Price Performance (%)

(%)	1M	3M	6M	1YR
Federal Bank	-8.3%	-7.9%	-9.9%	15.9%
Nifty 50	-7.8%	-6.3%	-8.4%	11.5%

* To date / current date : May 6, 2022

Federal Bank vs Nifty 50



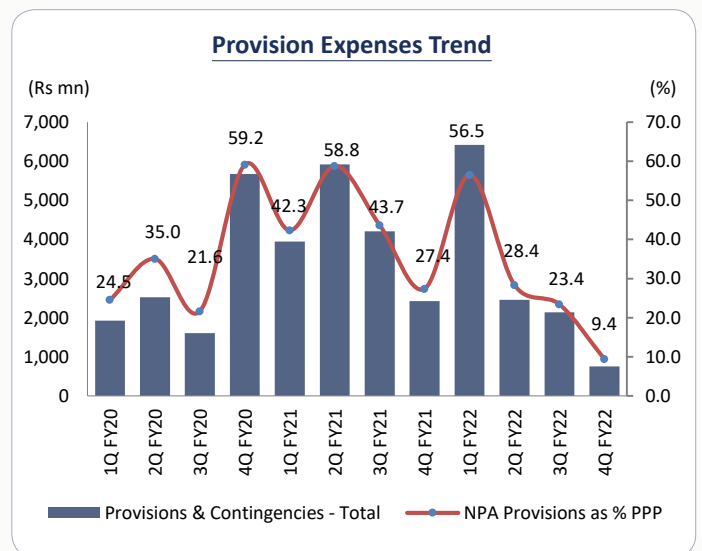
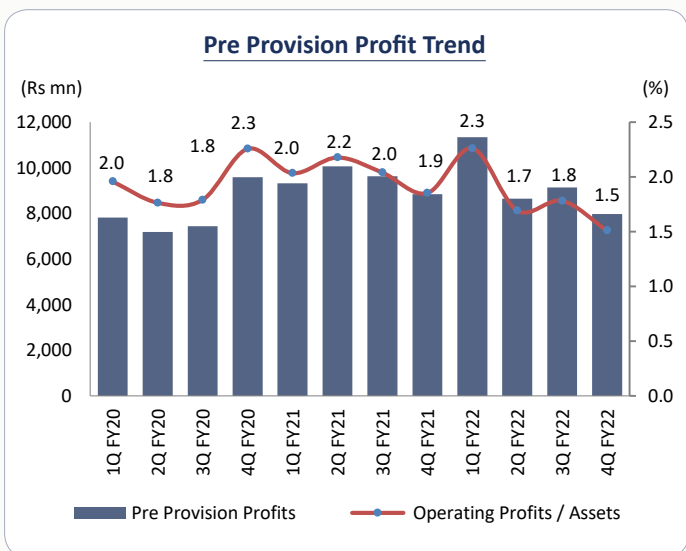
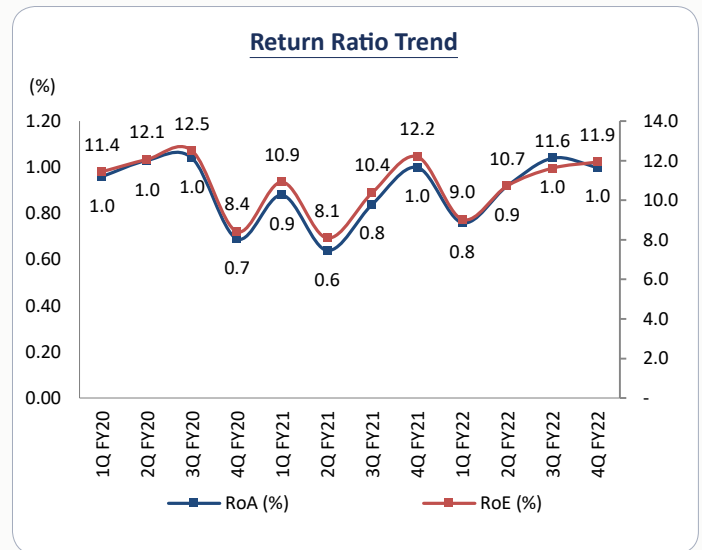
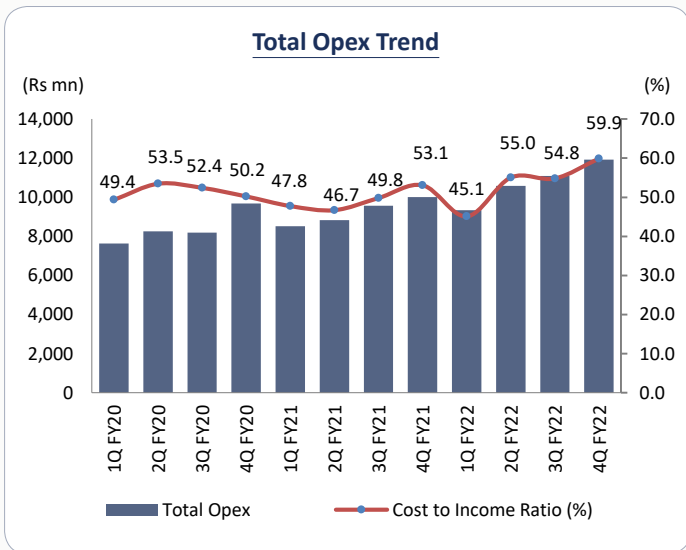
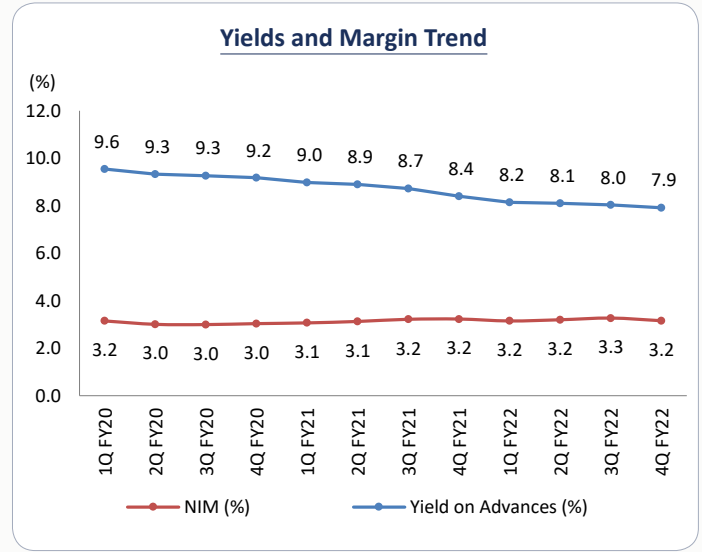
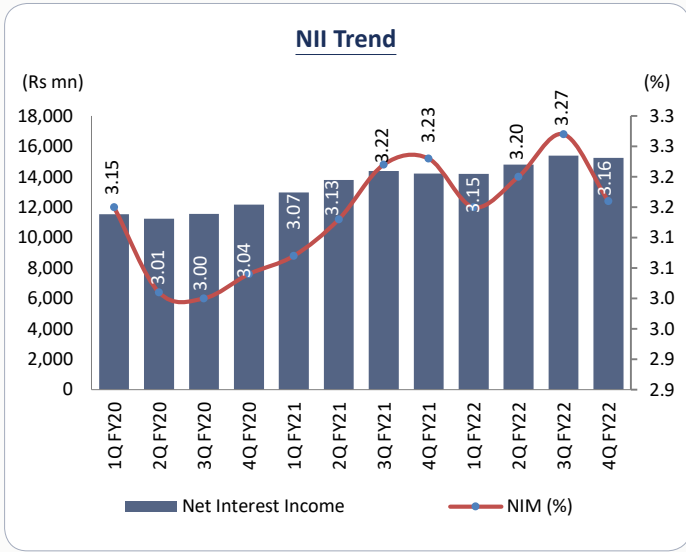
Sequential Profit growth owing to provision write-back: The bank has made provisioning of ₹0.8bn v/s ₹2.4bn in 3QFY22. The loan loss provisions stood at ₹0.95bn. The bank wrote back ₹0.4bn from standard account provision. Hence the quarterly provision are on lower side. The bank's NII stood at ₹15.2bn; grew by 7.4% YoY and de-grew 1% sequentially. NIM squeezed sequentially 11bps to 3.16% driven by 1bps increase in CoD at 4.28%. The bank's yields on advances declined by 12bps to 7.92%. Management estimates NIMs range of 3.2%-3.3% for FY23. Non-interest income has witnessed de-growth of 4% QoQ driven lower treasury income. C/I ratio was at higher side and stood at 60%. Employee expenses to remain high for next few quarters due to pension costs going up because of regulations related to purchasing annuity. ₹1.77bn family pension impact will amortize over 5 years with incremental impact per quarter of about ₹250mn. Therefore, the employee cost is likely to be on higher side. Owing to sequentially lower NII, other income and higher operating expenses, the bank's PPOP de-grew by 12.7% QoQ. Provisioning expenses are on lower side (₹0.8bn v/s 2.1bn in the last quarter) on the back of provision write-back. Thus, it resulted in PAT stability at ₹5.4bn; grew by 13% YoY and 3.6% sequentially. The bank's ROA/ROE stood at 1.0%/11.9%. The management targets ROA of 1.1% in FY23E.

Growth on track: The bank's net advances stood at ₹1.45tn; grew by 10% YoY and 3% QOQ. Retail book (32% of book) grew at 4.5% QoQ. Agriculture book (13% of book), SME (BuB+cuB) book (19% of book) and corporate book (35.0%) grew by 4.4% QoQ, 4.5% QoQ and -0.2% QoQ respectively. The bank has been focusing on gold loans since the lockdown started and currently stood at ₹173bn (9% YoY) with a LTV 69%. The management guided for loan growth of 15% for FY23. Loan growth was soft in FY22 because of slower gold loan growth in 9MFY22. Furthermore, competition has intensified across segments – retail, SME, corporate. Deposits grew by 5.2% YOY and grew 3.6% QOQ; CASA stood at 36.9% vs. 36.7% in last quarter.

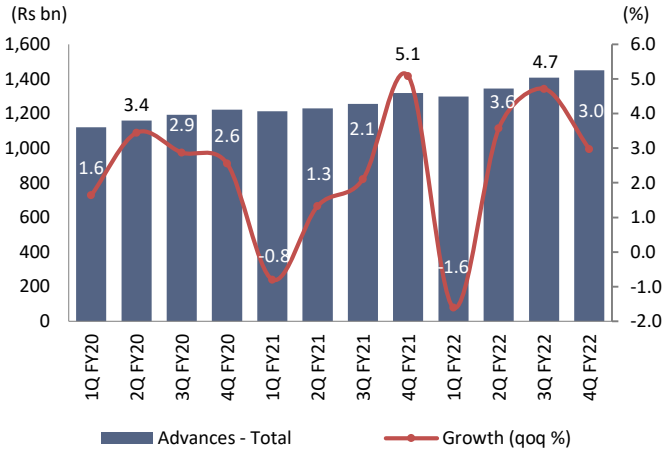
Outlook & Valuation

We believe the asset quality is likely to stay stable with gradual improvement in profitability. We have incorporated steady provision requirements along with stable growth in the balance sheet and thus expect it to deliver RoA/ RoE of 1.1%/13% by FY23E. We reiterate BUY on Federal Bank with target price of ₹116 (based on 1.2x FY23E Adj. BVPS); a potential upside of 27%.

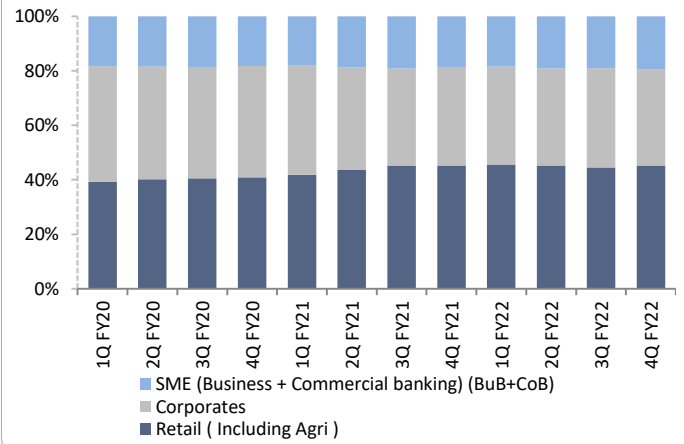
Quarterly story in charts



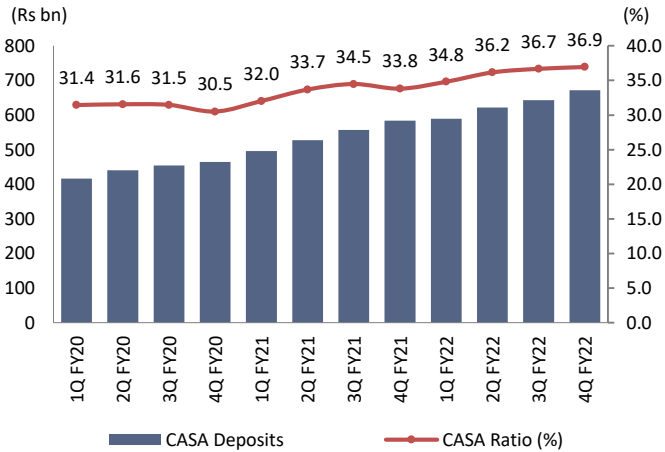
Loan Book Trend



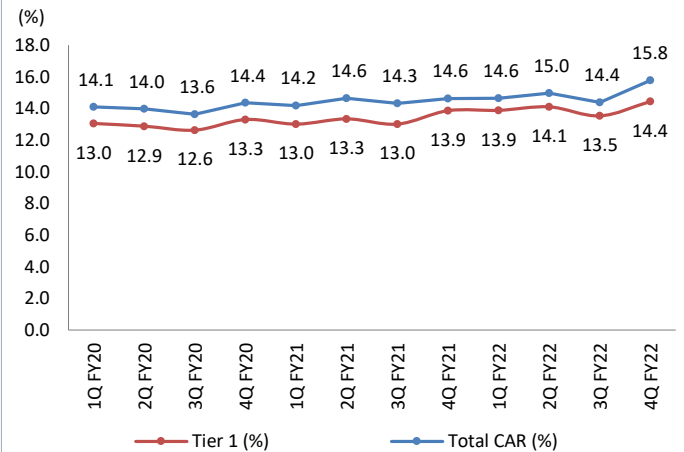
Loan Book Mix



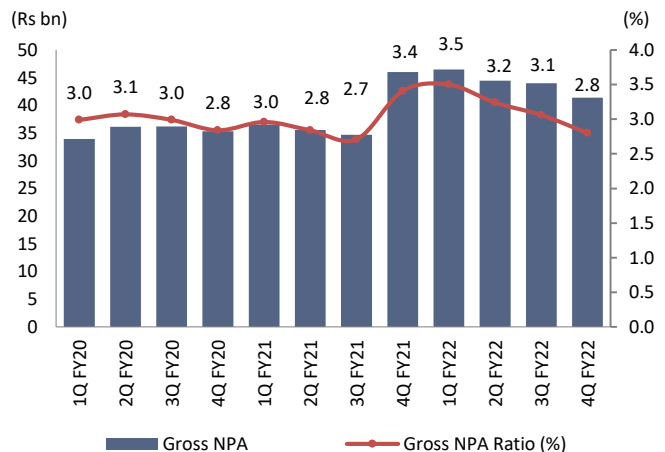
CASA Deposit Trend



CRAR and Tier 1 Trend



Gross NPA Trend



Net NPA Trend

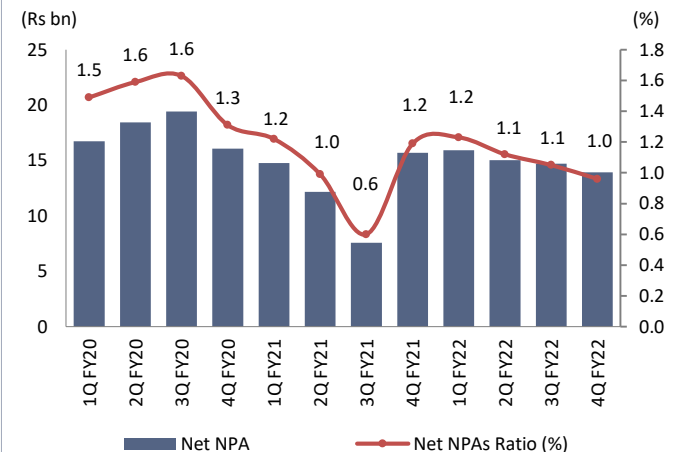


Exhibit 1 : Income Statement Analysis

(₹ mn)	4Q FY22	4Q FY21	% yoy / bps	3Q FY22	% qoq / bps	FY22	FY21	% yoy / bps
Interest Inc.	34,832	33,663	3.5	34,426	1.2	1,36,608	1,37,579	(0.7)
Interest Expenses	19,580	19,460	0.6	19,037	2.9	76,988	82,242	(6.4)
Net Interest Income	15,252	14,204	7.4	15,389	(0.9)	59,620	55,337	7.7
NII to Net Operative Income	76.6	75.3	131	76.1	57	74.5	74.0	48
NIM (%)	3.16	3.2	(7)	3.3	(11)	3.0	-	-
Other Income - Total	4,650	4,654	(0.1)	4,842	(4.0)	20,437	19,449	5.1
Other Inc to Net Oper. Income (%)	23.4	24.7	(131)	23.9	(57)	25.5	26.0	(48)
Net Operating Revenue	19,902	18,858	5.5	20,231	(1.6)	80,057	74,786	7.0
Employee Expenses	6,373	5,252	21.3	5,831	9.3	23,206	20,342	14.1
Other Opex	5,548	4,754	16.7	5,257	5.5	19,727	16,575	19.0
Total Opex	11,920	10,007	19.1	11,088	7.5	42,932	36,917	16.3
Cost to Income Ratio (%)	59.9	53.1	683	54.8	509	53.6	49.4	426
Pre Provision Profits	7,982	8,851	(9.8)	9,143	(12.7)	37,125	37,869	(2.0)
Provisions & Contingencies - Total	752	2,423	(69.0)	2,140	(64.8)	12,218	16,496	(25.9)
NPA Provisions as % PPP	9.4	27.4	(1,795)	23.4	(1,398)	32.9	43.6	(1,065)
Profit Before Tax	7,230	6,428	12.5	7,003	3.2	24,907	21,373	16.5
Tax	1,824	1,650	10.6	1,786	2.2	6,463	5,470	18.2
Effective Tax Rate (%)	25.2	25.7	(43)	25.5	(27)	25.9	25.6	35
Reported Profits	5,405	4,778	13.1	5,217	3.6	18,444	15,903	16.0
RoA (%)	1.0	1.0	-	1.0	(4)	0.9	-	-
RoE (%)	11.9	12.2	(27)	11.6	31	10.6	-	-

Source: Company, LKP Research

Exhibit 2 : Balance Sheet Analysis

(₹ mn)	3Q FY21	4Q FY21	1Q FY22	2Q FY22	3Q FY22	4Q FY22	QoQ % / bps	YoY % / bps
Net Worth	1,56,452	1,61,236	1,64,883	1,77,270	1,82,524	1,87,938	3.0	16.6
RoE (%)	10.4	12.2	9.0	10.7	11.6	11.9	31	(27)
Tier 1 (%)	13.0	13.9	13.9	14.1	13.5	14.4	91	58
Total CAR (%)	14.3	14.6	14.6	15.0	14.4	15.8	140	115
RWA - Total	10,77,510	11,16,210	11,03,370	11,39,480	11,89,040	12,22,600	2.8	9.5
Advances - Total	12,55,050	13,18,786	12,97,650	13,44,046	14,07,430	14,49,283	3.0	9.9
Investments	3,43,890	3,71,862	3,73,910	3,69,767	3,74,950	3,91,795	4.5	5.4
Total Assets	19,68,472	20,13,674	20,00,383	20,68,743	20,88,774	22,09,463	5.8	9.7
RoA (%)	0.84	1.00	0.76	0.92	1.04	1.00	(4)	-
Deposits	16,16,700	17,26,445	16,93,930	17,19,948	17,54,320	18,17,006	3.6	5.2
CASA Deposits	5,57,400	5,83,700	5,89,590	6,21,910	6,43,440	6,71,220	4.3	15.0
CASA Ratio (%)	34.5	33.8	34.8	36.2	36.7	36.9	26	313
Interest Bearing Liabilities - Total	17,41,440	18,17,130	17,87,430	18,27,788	18,35,820	19,70,937	7.4	8.5

Source: Company, LKP Research

Exhibit 3: Funding Profile Analysis

(₹ mn)	3Q FY21	4Q FY21	1Q FY22	2Q FY22	3Q FY22	4Q FY22	QoQ % / bps	YoY % / bps
Interest Bearing Liabilities - Total	17,41,440	18,17,130	17,87,430	18,27,788	18,35,820	19,70,937	7.4	8.5
Deposits	16,16,700	17,26,445	16,93,930	17,19,948	17,54,320	18,17,006	3.6	5.2
CASA Deposits	5,57,400	5,83,700	5,89,590	6,21,910	6,43,440	6,71,220	4.3	15.0
Saving Deposit	4,65,820	4,76,860	89,630	1,08,100	5,30,140	5,45,100	2.8	14.3
Current Deposit	91,580	1,06,840	4,99,960	5,13,810	1,13,300	1,26,120	11.3	18.0
Term Deposits	10,59,300	11,42,745	11,04,340	10,98,038	11,10,880	11,45,786	3.1	0.3
Borrowings	1,24,740	90,685	93,500	1,07,841	81,500	1,53,931	88.9	69.7

Source: Company, LKP Research

Exhibit 4: Assets Quality Analysis

(₹ mn)	3Q FY21	4Q FY21	1Q FY22	2Q FY22	3Q FY22	4Q FY22	QoQ % / bps	YoY % / bps
Total Slippages	340	16,850	6,890	3,390	4,530	3,990	(11.9)	(76.3)
Slippages Ratio (%)	0.03	1.38	0.52	0.26	0.34	0.30	(4)	(108)
Gross NPA	34,702	46,024	46,493	44,458	44,013	41,367	(6.0)	(10.1)
Gross NPAs Ratio (%)	2.71	3.41	3.50	3.24	3.06	2.80	(26)	(61)
PCR - Calculated (%)	78.2	65.9	65.7	66.2	66.6	66.3	(24)	43
Net NPA	7,572	15,693	15,932	15,024	14,712	13,926	(5.3)	(11.3)
Net NPAs Ratio (%)	0.60	1.19	1.23	1.12	1.05	0.96	(9)	(23)
Standard Restructured	11,290	16,180	24,140	35,530	37,230	35,360	(5.0)	118.5
Std. Rest. Adv. as % of Advances	0.9	1.2	1.86	2.64	2.65	2.44	(21)	121

Source: Company, LKP Research

Annual Projections

Exhibit 5: Profit and Loss Statement

(₹ mn)	FY20	FY21	FY22	FY23E	FY24E
Int. Income	1,32,108	1,37,579	1,36,608	1,57,042	1,83,611
Interest Expenses	85,618	82,242	76,988	84,820	97,189
Net Interest Income	46,489	55,337	59,620	72,222	86,422
<i>NIM (%)</i>	<i>2.88</i>	<i>3.08</i>	<i>3.03</i>	<i>3.29</i>	<i>3.43</i>
Other Income - Total	19,314	19,449	20,437	23,160	26,643
Net Operating Revenue	65,803	74,786	80,057	95,382	1,13,064
Employee Exp.	17,724	20,342	23,206	26,686	30,156
Other Opex	16,033	16,575	19,727	23,475	27,935
Total Opex	33,756	36,917	42,932	50,161	58,090
<i>C/I Ratio (%)</i>	<i>51.30</i>	<i>49.36</i>	<i>53.63</i>	<i>52.59</i>	<i>51.38</i>
Pre Provision Profits	32,047	37,869	37,125	45,221	54,974
<i>PPP Growth (yoy %)</i>	<i>16.0</i>	<i>18.2</i>	<i>(2.0)</i>	<i>21.8</i>	<i>21.6</i>
Provisions & Contingencies - Total	11,722	16,496	12,218	9,551	10,981
<i>Credit Cost (As % of Op. AUM)</i>	<i>1.01</i>	<i>1.34</i>	<i>0.92</i>	<i>0.65</i>	<i>0.65</i>
Profit Before Tax	20,325	21,373	24,907	35,670	43,993
Tax	4,898	5,470	6,463	9,255	11,415
<i>Effective Tax Rate (%)</i>	<i>24.1</i>	<i>25.6</i>	<i>25.9</i>	<i>25.9</i>	<i>25.9</i>
Reported Profits	15,428	15,903	18,444	26,415	32,578
<i>PAT Growth (yoy %)</i>	<i>24.0</i>	<i>3.1</i>	<i>16.0</i>	<i>43.2</i>	<i>23.3</i>

Source: Company, LKP Research

Exhibit 6: Balance Sheet

(₹ mn)	FY20	FY21	FY22	FY23E	FY24E
Equity Share Capital	3,985	3,992	4,205	4,205	4,205
Reserves (ex Revel. Reserve)	1,41,141	1,57,194	1,83,683	2,10,098	2,42,676
Net Worth - Ex Revaluation	1,45,126	1,61,186	1,87,888	2,14,303	2,46,881
Deposits	15,22,901	17,26,445	18,17,006	20,70,694	23,81,365
Borrowings	1,03,724	90,685	1,53,931	1,75,423	2,01,742
Interest Bearing Liabilities (₹ mn)	16,26,625	18,17,130	19,70,937	22,46,117	25,83,107
Other Lia. & Prov.	34,579	35,308	50,588	59,174	66,019
Total Liabilities	18,06,380	20,13,674	22,09,463	25,19,657	28,96,071
Assets					
Cash & Cash Equivalent	1,25,746	1,95,914	2,10,104	2,40,089	2,76,811
Investments	3,58,927	3,71,862	3,91,795	4,37,160	4,92,271
Loan & Advances (₹ mn)	12,22,679	13,18,786	14,49,283	16,66,676	19,33,344
Growth (yoy %)	10.9	7.9	9.9	15.0	16.0
Fixed Assets	4,800	4,911	6,339	7,076	8,124
Other Assets	94,229	1,22,201	1,51,942	1,68,656	1,85,522
Total Assets	18,06,380	20,13,674	22,09,463	25,19,657	28,96,071

Source: Company, LKP Research

Exhibit 7: Per share data

Y/E Mar	FY20	FY21	FY22	FY23E	FY24E
Face Value (₹)	2	2	2	2	2
Adjusted Share O/S (mn)	1,993	1,996	2,103	2,103	2,103
Earnings Per Share (₹)	7.7	8.0	8.8	12.6	15.5
EPS (% YoY)	23.6	2.9	10.1	43.2	23.3
P/E (x)	11.7	11.4	10.3	7.2	5.9
Book Value (₹)	72.8	80.7	89.4	101.9	117.4
BVPS (% YoY)	9.0	10.9	10.7	14.1	15.2
P/BV (x)	1.2	1.1	1.0	0.9	0.8
Adj. BV (₹)	68.8	75.0	84.5	97.1	112.6
Adj. BV (% YoY)	9.6	9.0	12.7	14.9	16.0
P/ABV (x)	1.3	1.2	1.1	0.9	0.8

Source: Company, LKP Research

Exhibit 8: Detail RoA Tree Analysis (%)

Y/E Mar	FY20	FY21	FY22	FY23E	FY24E
Yields / Margins					
<i>Yield on Advance</i>	9.2	8.5	7.8	8.1	8.2
<i>Yield on Funds</i>	8.2	7.7	6.9	7.1	7.3
<i>Cost of Funds (CoF)</i>	5.6	4.8	4.1	4.0	4.0
<i>Interest Spread</i>	2.6	2.9	2.9	3.1	3.3
<i>NIM's</i>	2.9	3.1	3.0	3.3	3.4
<i>Interest Income / Assets</i>	7.8	7.2	6.5	6.6	6.8
<i>Interest Exp. / Assets</i>	5.0	4.3	3.6	3.6	3.6
<i>NII / Assets</i>	2.7	2.9	2.8	3.1	3.2
<i>Fee Income / Assets</i>	0.6	0.5	0.6	0.6	0.6
<i>Other Non Core Income / Assets</i>	0.4	0.3	0.2	0.2	0.2
<i>Other Income / Assets</i>	1.1	1.0	1.0	1.0	1.0
<i>Net Operating Income / Assets</i>	3.9	3.9	3.8	4.0	4.2
Operating Ratios					
<i>NII to Net Operative Income</i>	70.6	74.0	74.5	75.7	76.4
<i>Other Income to Net Operative Income</i>	29.4	26.0	25.5	24.3	23.6
<i>Empl. Cost/Oper. Exps.</i>	52.5	55.1	54.1	53.2	51.9
<i>Other Op. Exps./Oper. Exps.</i>	47.5	44.9	45.9	46.8	48.1
<i>C/I Ratio (%)</i>	51.3	49.4	53.6	52.6	51.4
<i>Provisions as % PPP</i>	17.8	22.1	15.3	10.0	9.7
<i>Credit Cost (As % of Op. AUM)</i>	1.0	1.3	0.9	0.7	0.7
<i>Effective Tax Rate (%)</i>	24.1	25.6	25.9	25.9	25.9
<i>Employee Exp. / Assets</i>	1.0	1.1	1.1	1.1	1.1
<i>Other Opex/ Assets</i>	0.9	0.9	0.9	1.0	1.0
<i>Total Opex / Assets</i>	2.0	1.9	2.0	2.1	2.1
<i>Operating Profits / Assets</i>	1.9	2.0	1.8	1.9	2.0
<i>Op Profit ex Except Items / Assets</i>	1.9	2.0	1.8	1.9	2.0
<i>Provisions / Assets</i>	0.7	0.9	0.6	0.4	0.4
<i>Profit Before Tax / Assets</i>	1.2	1.1	1.2	1.5	1.6
<i>Tax Expenses / Assets</i>	0.3	0.3	0.3	0.4	0.4
<i>RoA</i>	0.9	0.8	0.9	1.1	1.2
<i>Leverage (x)</i>	12.4	12.5	11.8	11.8	11.7
<i>RoE</i>	11.1	10.4	10.6	13.1	14.1

Source: Company, LKP Research

Exhibit 9: Balance Sheet Ratios

Y/E Mar	FY20	FY21	FY22	FY23E	FY24E
Credit / Deposit Ratio	80.3	76.4	79.8	80.5	81.2
Incremental C/D Ratio	69.5	47.2	144.1	85.7	85.8
Investment Deposit Ratio	23.6	21.5	21.6	21.1	20.7
Dom. SLR Investment / Deposits	20.9	19.0	19.0	18.8	18.7
CASA Ratio	29.0	34.0	36.9	36.1	36.1

Source: Company, LKP Research

Exhibit 10: Credit Quality

Y/E Mar	FY20	FY21	FY22	FY23E	FY24E
Slippage Ratio (%)	1.7	1.6	1.4	1.2	1.2
Gross NPA	35,308	46,024	41,367	42,092	38,862
Gross NPAs Ratio (%)	2.8	3.4	2.8	2.5	2.0
PCR (%)	54.5	65.9	66.3	65.9	64.9
Net NPA	16,072	15,693	13,926	14,354	13,650
Net NPAs Ratio (%)	1.3	1.2	1.0	0.9	0.7
Total Impaired Loans	35,308	46,024	41,367	42,092	38,862
Impaired Loan as % of Loan / AUM	2.8	3.4	2.8	2.5	2.0
Total Risk Reserves	20,056	31,150	27,441	27,738	25,212
Total Risk As % of Loan Book	1.6	2.3	1.8	1.6	1.3

Source: Company, LKP Research

Exhibit 11: Key Assumptions & Forecasts

Y/E Mar	FY20	FY21	FY22	FY23E	FY24E
Loan & Advances (₹ mn)	12,22,679	13,18,786	14,49,283	16,66,676	19,33,344
Growth (yoy %)		7.9	9.9	15.0	16.0
Interest Bearing Liabilities (₹ mn)	16,26,625	18,17,130	19,70,937	22,46,117	25,83,107
Growth (yoy %)		11.7	8.5	14.0	15.0
Yield on Funds	8.2	7.7	6.9	7.1	7.3
Cost of Funds (CoF)	5.6	4.8	4.1	4.0	4.0
Interest Spread	2.6	2.9	2.9	3.1	3.3
NIM's	2.9	3.1	3.0	3.3	3.4
Other Income Growth	43.0	0.7	5.1	13.3	15.0
C/I Ratio (%)	51.3	49.4	53.6	52.6	51.4
Effective Tax Rate (%)	24.1	25.6	25.9	25.9	25.9
Return Ratios					
Adj. RoA	0.9	0.8	0.9	1.1	1.2
Adj. RoE	11.1	10.4	10.6	13.1	14.1
Asset Quality Metrics					
Credit Cost (As % of Op. AUM)	1.0	1.3	0.9	0.7	0.7
Gross NPAs Ratio (%)	2.8	3.4	2.8	2.5	2.0
Net NPAs Ratio (%)	1.3	1.2	1.0	0.9	0.7

Source: Company, LKP Research

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