

### Mixed bag results !!!

Federal Bank reported Q2FY24 numbers – PAT came in at INR 9.5 bn, up by 35.5% yoy and 11.7% qoq. NII growth was slightly on lower end at 16.7% yoy due to higher interest outgo. Asset growth was healthy at 19.6% yoy and 5% qoq. While on liabilities side, core deposits growth (excluding bulk deposits) was lower at 9.6% and also, share of CASA deposits has come down by 520 bps yoy to 31.2% levels. While margins were maintained on qoq basis at 3.16% levels (down by 15 bps yoy). Asset quality performance of the bank was stable. Management reiterated that ROA of 1.4% by FY25 period. In our view, we do not see any meaningful upside in the stock going forward. Maintain Accumulate rating with TP of INR 166, upside of 12% from the current levels.

#### Outlook

- Margins in FY24 is expected to be at 3.25% levels vs. 3.16% levels seen in Q2FY24
- Credit cost for the full year FY24 is expected to be at 35-40 bps vs. 11 bps seen in H1FY24.
- Cost/Income is expected to come down to 50% levels by FY25 vs. 52.5% as in Q2FY24.
- Management aims for ROA of 1.4% levels by FY25 vs. >1.3% levels seen in H1FY24.
- Current run-rate of fee income growth will continue.
- Credit growth in high-teens in FY24 (in-line with our estimate of 19%).

#### Valuations

Going forward, we expect PAT growth to slow down to 12.6% CAGR over the next 2 years i.e. FY23-25e mainly due to higher cost ratios and muted margins. At current CMP, it is trading at 1.3x/1.2x FY24e/FY25e ABV on ROE/ROA of ~13-14%/1.2%. Given slower trajectory of profitability, **we assign ACCUMULATE rating to the stock with TP of INR 166, upside of 12%** from current levels and discounting its FY25e ABV by 1.35x. Although we have ACCUMULATE rating on the stock; it is not one of our top picks.

#### Financial Summary

Y/E Mar (Rs Bn)	FY20	FY21	FY22	FY23E	FY24E	FY25E
NII	46.5	55.3	59.6	72.3	82.9	94.2
Net profit	15.7	15.8	18.9	30.1	34.3	38.2
Networth	145	161	188	215	276	310
Adj BVPS	65	73	83	94	110	123
EPS (Rs)	2.0	7.9	9.0	14.2	14.6	16.2
P/ABV (x)	2.3	2.0	1.8	1.6	1.3	1.2
P/E (x)	74.0	18.7	16.5	10.4	10.2	9.1

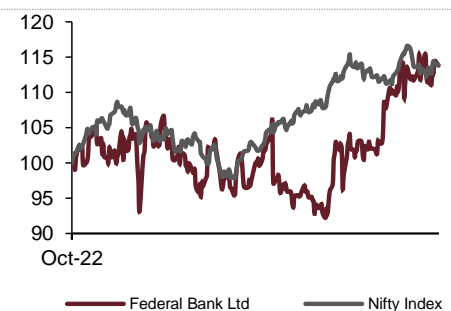
Source: Dalal & Broacha Research, Company

Rating	TP (Rs)	Up/Dn (%)
<b>ACCUMULATE</b>	<b>166</b>	<b>12</b>

#### Market data

Current price	Rs	149
Market Cap (Rs.Bn)	(Rs Bn)	349
Market Cap (US\$ Mn)	(US\$ Mn)	4,195
Face Value	Rs	2
52 Weeks High/Low	Rs	153 / 121
Average Daily Volume	('000)	16,441
BSE Code		500469
Bloomberg		FB.IN
Source: Bloomberg		

#### One Year Performance



Source: Bloomberg

% Shareholding	Mar-23	Dec-22
Promoters	25	25
Public	75	75
Others		
<b>Total</b>	<b>100</b>	<b>100</b>

Source: Bloomberg

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## Key Financial Highlights

- PAT reported healthy growth of 35.5% yoy and 11.7% qoq to INR 9.5 bn. During the quarter, interest expenses growth was higher at 50% vs. interest income growth of 35.7% that led by moderated NII growth of 16.7% yoy to INR 2 bn
- **Asset growth was healthy** – Credit growth was strong at 19.6% yoy (5.1% qoq) to INR 1928 bn. Loan growth was good across segments – retail loans (31.6% share) showed 18.2% yoy growth, agri loans (12.8% share) 23.6% yoy, corporate loans (10.1% share) 23.8% yoy and commercial banking (34.7% share) grew by 14.9% yoy basis.
- **Within retail loans**, growth in the unsecured loans was much higher than secured loans. Credit cards reported growth of 183% yoy and personal loans 76.4% yoy; while share of both these segments has grown to 9% vs. 5% a year ago. Home loans (43% share) grew by 13.9% yoy and LAP (17.6% share) 18.7% share.
- MFI business of the bank crossed INR 23.3 bn which is growing by 206% yoy and currently forms 1.2% share in total loans
- **CASA growth muted; bulk TDs drive deposit growth** – CASA showed a muted growth of 4% yoy to INR 696 bn; this resulted in fall in the CASA ratio from 36.4% year ago to 31.2% currently. While the growth was relatively better in retail term deposits at 9.6% yoy. Bulk TDs (19% share in total deposits) grew by ~>1.5x over the last one year time to INR 442 bn. This resulted in bulk deposits share in total deposits increasing to 19% in Q2 from 9% in Q1FY23. This drive the overall deposits growth to 23% yoy levels to INR 2328.7 bn
- **Margins came were stable on qoq basis** – Reported margins were stable at 3.16% levels on qoq basis while it was down by 15 bps on yoy basis. There was impact of 3-4 bps due to ICRR (Incremental Cash Reserve Ratio) and the same was set off against capital raising that bank had done in Q2. Going forward, the bank expects FY24 margins would be maintained at 3.25% levels. Lower CASA growth and higher growth in bulk deposits (INR >2 cr) is one of the reasons that is resulting in ~120 bps increase in the cost of deposits on yoy basis.
- Core fee income growth was healthy at 22% yoy and 23% qoq to INR 6.6 bn led by good loan processing fees, cards & para banking fees. While there was profit on sale on investments income was lower at INR 18 cr in Q2 vs. INR 33 cr in Q1 last quarter.
- **Credit cost (calculated) was much lower at 2.3 bps (INR 0.4 bn) vs. 9 bps in Q1FY24 (INR 1.6 bn).** Cumulative credit cost for the H1FY24 was at 11 bps. Incremental slippages for the quarter were at INR 3.7 bn vs. INR 5 bn in Q1FY24 which was largely led by lower slippages from retail portfolio. GNPA/NNPA ratio stood at 2.26%/0.64% in Q2FY24 vs. 2.38%/0.69% in Q1FY24
- Cost to income ratio was on higher end at 52.5% in Q2FY24 vs. 50.9% in Q1FY24 (Opex growth was on higher end at 26.2%). Management expects cost ratios to stabilise to 50% levels by FY25 as it is currently investing in the new businesses like personal loans, credit cards, MFI businesses which are likely to generate higher revenues in times to come. Also, there is higher opex is incurred due to branch expansion and increase in marketing spends

## Concall Highlights

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## Valuations

Going forward, we expect PAT growth to slow down to 12.6% CAGR over the next 2 years i.e. FY23-25e mainly due to higher cost ratios and muted margins. At current CMP, it is trading at 1.3x/1.2x FY24e/FY25e ABV on ROE/ROA of ~13-14%/1.2%. Given slower trajectory of profitability, **we assign ACCUMULATE rating to the stock with TP of INR 166, upside of 12% from current levels** and discounting its FY25e ABV by 1.35x. Although we have ACCUMULATE rating on the stock; it is not one of our top picks.

## Quarterly Financials (Q4FY23)

(in cr)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	H2FY24	H2FY23	YoY (%)
Interest earned	5455.3	4020.8	35.7	5024.5	8.6	10479.8	7649.6	37.0
Interest expenses	3398.9	2259.0	50.5	3105.9	9.4	6504.8	4283.3	51.9
<b>Net Interest Income (NII)</b>	<b>2056.4</b>	<b>1761.8</b>	<b>16.7</b>	<b>1918.6</b>	<b>7.2</b>	<b>3975.0</b>	<b>3366.3</b>	<b>18.1</b>
Other Income	730.4	609.5	19.8	732.4	-0.3	1462.8	1062.1	37.7
<b>Total income</b>	<b>2786.8</b>	<b>2371.4</b>	<b>17.5</b>	<b>2651.0</b>	<b>5.1</b>	<b>5437.8</b>	<b>4428.5</b>	<b>22.8</b>
Operating expenses	1462.4	1159.1	26.2	1348.7	8.4	2811.0	2242.9	25.3
<b>Operating profit</b>	<b>1324.5</b>	<b>1212.2</b>	<b>9.3</b>	<b>1302.4</b>	<b>1.7</b>	<b>2626.8</b>	<b>2185.6</b>	<b>20.2</b>
Provision for contingencies	43.9	267.9	-83.6	155.6	-71.8	199.5	434.5	-54.1
<b>PBT</b>	<b>1280.6</b>	<b>944.4</b>	<b>35.6</b>	<b>1146.8</b>	<b>11.7</b>	<b>2427.3</b>	<b>1751.1</b>	<b>38.6</b>
Provision for taxes	326.7	240.7	35.8	293.0	11.5	619.8	446.7	38.7
<b>Net profit</b>	<b>953.8</b>	<b>703.7</b>	<b>35.5</b>	<b>853.7</b>	<b>11.7</b>	<b>1807.6</b>	<b>1304.4</b>	<b>38.6</b>
Equity	470.3	421.9	11.5	423.6	11.0	470.3	421.9	11.5
EPS	4.17	3.34	24.9	4.03	3.5	38.43	30.92	24.3
<b>Ratios (%)</b>								
Int. exp/Int earned (%)	62.3	56.2	-	61.8	-	62.1	56.0	-
Cost/Income ratio (%)	52.5	48.9	-	50.9	-	51.7	50.6	-
Gross NPAs (Rs)	4436.1	4031.1	10.0	4434.8	0.0	4436.1	4031.1	10.0
Net NPAs (Rs)	1229.8	1262.4	-2.6	1274.6	-3.5	1229.8	1262.4	-2.6
Gross NPAs (%)	2.26	2.46	-	2.38	-	2.3	2.5	-
Net NPAs (%)	0.64	0.8	-	0.69	-	0.6	0.8	-
ROA (%)	0.3	0.3	-	0.3	-	1.5	1.5	-
CAR (%)	15.5	13.8	-	14.3	-	15.5	13.8	-
<b>Balance Sheet (Rs.cr)</b>								
Deposits	2,32,868	1,89,146	23.1	2,22,496	4.7	2,32,868	1,89,146	23.1
Advances	1,92,817	1,61,240	19.6	1,83,487	5.1	1,92,817	1,61,240	19.6

Source: Company, Dalal & Broacha Research

## Financials

P&L (Rs Bn)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Interest income	132.1	137.6	136.6	168.0	202.6	242.6
Interest expense	85.6	82.2	77.0	95.7	119.7	148.3
<b>NII</b>	<b>46.5</b>	<b>55.3</b>	<b>59.6</b>	<b>72.3</b>	<b>82.9</b>	<b>94.2</b>
Non-interest income	19.6	19.4	20.9	23.3	26.8	31.4
<b>Net revenues</b>	<b>66.1</b>	<b>74.8</b>	<b>80.5</b>	<b>95.6</b>	<b>109.7</b>	<b>125.6</b>
Operating expenses	33.8	36.9	42.9	47.7	55.0	63.0
<b>PPOP</b>	<b>32.3</b>	<b>37.9</b>	<b>37.6</b>	<b>48.0</b>	<b>54.7</b>	<b>62.6</b>
Provisions	11.7	16.6	12.2	7.5	8.6	11.3
<b>PBT</b>	<b>20.6</b>	<b>21.2</b>	<b>25.4</b>	<b>40.5</b>	<b>46.1</b>	<b>51.3</b>
Tax	4.9	5.5	6.5	10.3	11.8	13.1
<b>PAT</b>	<b>15.7</b>	<b>15.8</b>	<b>18.9</b>	<b>30.1</b>	<b>34.3</b>	<b>38.2</b>
<b>Growth (y-o-y)</b>		<b>0.6</b>	<b>19.8</b>	<b>59.4</b>	<b>13.9</b>	<b>11.3</b>

Balance sheet (Rs.bn)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Share capital	3.99	3.99	4.21	4.23	4.71	4.71
Reserves & surplus	141	157	184	211	271	305
<b>Net worth</b>	<b>145</b>	<b>161</b>	<b>188</b>	<b>215</b>	<b>276</b>	<b>310</b>
Deposits	1,523	1,726	1,817	2,134	2,496	2,895
Borrowings	104	91	154	193	228	269
Other liability	35	35	51	61	71	82
<b>Total liabilities</b>	<b>1,806</b>	<b>2,014</b>	<b>2,209</b>	<b>2,603</b>	<b>3,071</b>	<b>3,556</b>
Fixed assets	4.8	4.9	6.3	9.3	9.7	10.0
Investments	359	372	392	490	571	662
Loans	1,223	1,319	1,449	1,744	2,076	2,450
Cash	126	196	210	177	228	244
Other assets	94	122	152	183	187	190
<b>Total assets</b>	<b>1,806</b>	<b>2,014</b>	<b>2,209</b>	<b>2,603</b>	<b>3,071</b>	<b>3,556</b>

Ratios	FY20	FY21	FY22	FY23e	FY24e	FY25e
<b>Growth (%)</b>						
NII	11.3	19.0	7.7	21.3	14.7	13.6
PPOP	14.2	17.3	-0.8	27.6	14.0	14.5
PAT	19.8	0.6	19.8	59.4	13.9	11.3
Advances	10.9	7.9	9.9	20.0	19.0	18.0
Deposits	12.8	13.4	5.2	17.4	17.0	16.0
<b>Spread (%)</b>						
Yield on Funds	8.2	7.7	6.9	7.5	7.7	7.8
Cost of Funds	5.6	4.8	4.1	4.5	4.7	5.0
Spread	2.6	2.9	2.9	3.1	2.9	2.7
NIM	2.9	3.1	3.0	3.24	3.14	3.03
<b>Asset quality (%)</b>						
Gross NPAs	2.8	3.4	2.8	2.4	2.3	2.3
Net NPAs	1.3	1.2	1.0	0.9	0.9	0.8
Provisions	53	66	66	65	63	63
<b>Return ratios (%)</b>						
RoE	11.3	10.3	10.8	14.9	14.0	13.0
RoA	0.9	0.8	0.9	1.3	1.2	1.2
<b>Per share (Rs)</b>						
EPS	2	8	9	14	15	16
BV	73	81	89	102	117	132
ABV	65	73	83	94	110	123
<b>Valuation (x)</b>						
P/E	75.0	19.0	16.7	10.5	10.3	9.2
P/BV	2.1	1.9	1.7	1.5	1.3	1.1
P/ABV	2.3	2.1	1.8	1.6	1.4	1.2
<b>Other Ratios (%)</b>						
Cost/Income	51.1	49.4	53.3	49.9	50.2	50.2
CD ratio	80.3	76.4	79.8	81.8	83.2	84.6
CASA ratio	30.7	34.0	37.1	32.7	29.8	27.4
CAR	14.3	14.6	15.8	15.0	16.1	15.4

Source: Dalal &amp; Broacha Research, Company

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