

CMP: Rs 100

Rating: Buy

Target Price: Rs 126

Stock Info

| | |
|--------------------------|------------|
| INDEX | |
| BSE | 500469 |
| NSE | FEDERALBNK |
| Bloomberg | FB IN |
| Reuters | FED.BO |
| Sector | Banks |
| Face Value (Rs) | 2 |
| Equity Capital (Rs cr.) | 397 |
| Mkt Cap (Rs cr.) | 19,407 |
| 52w H/L (Rs) | 105/67 |
| Weekly Avg Vol (BSE+NSE) | 12,024,350 |

Shareholding Pattern

| (As on March, 2019) | % |
|---------------------|------|
| Promoters | Nil |
| FII | 37.3 |
| DII | 29.7 |
| Public & Others | 33.0 |

Source: NSE, Arihant Research

Stock Performance (%)

| | 3m | 6m | 12m |
|--------------|------|------|------|
| Federal Bank | 13.6 | 18.7 | 0.0 |
| Sensex | 6.6 | 11.3 | 10.8 |

Source: ACE Equity, Arihant Research

Federal Bank v/s Sensex



Source: ACE Equity, Arihant Research

Federal Bank reported a strong performance during Q4FY19 with 18% YoY growth in advances leading to 17.5% YoY growth in NII. Earnings growth for the quarter was higher at 163% YoY to Rs 382 cr, largely due to sharp decline in provisions. Moderate increase in OPEX and 21% rise in total income, led to 28% jump in operating profit. Due to sharp decline in slippages, GNPA/NNPA witnessed an improvement of 22bps/24 bps on QoQ basis. NIM was stable at 3.20% an expected to remain in the same range going forward. OPEX grew by 14% YoY with CI ratio improving by ~280 bps to 50%. RoA for the quarter came in at 1.02% as per the management target. Given by, improvement in operating performance and compelling valuation we maintain our Buy rating with a revised target price of Rs 126.

Q4FY19 Highlights:

- Total Advances grew by 18% YoY/4% QoQ to Rs 110223 cr, leading to 18% jump in NII to Rs 1097 cr. PPOP grew by 28% YoY to Rs 755 cr. Other income for the quarter grew by 31% YoY to Rs 412 cr, supported by 21% growth in fee income. Margins remained flat sequentially at 3.17% as yields and CoF both moved up alongside each other.
- Overall Retail book achieved a strong momentum with a 23% YoY growth whereas Corporate loan book grew by 18%. Currently, the share of retail & wholesale book stood at 47% & 53% respectively which is targeted to be 50:50 going forward. Deposit for the quarter grew by 29% YoY to Rs 134,955 cr, driven by 17% YoY growth in retail deposits.
- Slippages declined by 40% QoQ to Rs 256 cr, driven by meaningful decline in SME slippages and NIL slippages in corporate segment. SME slippages fell from Rs 192 cr to Rs 97 cr QoQ. GNPA/NNPAs declined both in absolute and percentage terms to 2.92%/1.48% from 3.14%/1.72% QoQ.

Management commentary

- IL&FS update:** Bank has exposure of Rs 270 cr towards 3 entities, out of which one large exposure of Rs 210 cr is under Amber category which is fully operational. The remaining 2 entities (Rs. 30 Cr exposure each) are also operational on which the bank has provisioned an amount of Rs 22 Cr. The repayment scheduled in April had been executed by these entities.
- Federal bank does not have direct exposure in stressed companies like Rcom, Essel group, Jet airways and Reliance infrastructure. The bank has a small exposure to Reliance Home Finance and to Reliance Capital (both amounts are in double digits).
- The bank achieved FY19 ROA of 0.88% and Q4FY19 ROA of 1.02%. Management targets 10-12 bps improvement in RoA each year led by decline in credit costs and cost/income.
- NIMs were stable on QoQ basis at 3.17%. Management expects NIMs to be in the same range going forward. (FY20 target: 3.2%)
- Credit cost at 0.51% should remain soft and there was no one off benefit during the quarter (QoQ 0.68%, YoY 1.23%). Guidance for FY20 stands at 55-56 bps.
- No capital infusion plan for the next 12-18 months.

Valuation and Outlook; Maintain Buy

Federal bank reported strong performance during Q4FY19 across parameters and it continues enjoying a strong retail liability franchise with high share of retail deposits. Improvement in core metrics like CI ratio, Asset quality, decline in credit cost and sustainable margins will be a key to deliver 1% RoA. We expect current growth trajectory to continue and have valued the stock on P/ABV of 1.7(x) to its FY21E ABV and arrived at a fair value of Rs 126 per share, giving a potential upside of 26%.

Q4FY19 Financial Snapshot:

| Particulars (Rs in Cr) | Q4 FY19 | Q4 FY18 | YoY% | Q3 FY19 | QoQ % |
|--------------------------------------|--------------|-------------|--------------|--------------|-------------|
| Interest Earned | 3,032 | 2,548 | 19.0 | 2,954 | 2.6 |
| Interest Expended | 1,936 | 1,615 | 19.9 | 1,877 | 3.1 |
| Net Interest Income | 1,097 | 933 | 17.50 | 1,077 | 1.8 |
| Other Income | 412 | 314 | 31.1 | 346 | 19.1 |
| <i>Other income / Net Income (%)</i> | 27 | 25 | | 24 | |
| Total income | 1508 | 1247 | 20.9 | 1423 | 6.0 |
| Employee Expenses | 370 | 331 | 11.9 | 354 | 4.7 |
| Non-Employee expenses | 383 | 328 | 16.9 | 361 | 6.1 |
| Operating Expenses | 754 | 659 | 14.4 | 715 | 5.4 |
| <i>Cost-income Ratio (%)</i> | 50.0 | 52.8 | | 50.3 | |
| Pre-Prov Profits | 755 | 589 | 28.2 | 708 | 6.6 |
| Provisions & Contingencies | 178 | 372 | -52.2 | 190 | -6.5 |
| PBT | 577 | 217 | 165.8 | 518 | 11.5 |
| Provisions for Tax | 195 | 72 | 171.3 | 184 | 6.2 |
| <i>Effective Tax Rate (%)</i> | 34 | 33 | | 36 | |
| PAT (reported) | 382 | 145 | 163.1 | 334 | 14.4 |
| EPS | 1.9 | 0.7 | 159.8 | 1.7 | 14.4 |
| GNPA | 3261 | 2796 | 16.6 | 3361 | -3.0 |
| NNPA | 1626 | 1552 | 4.8 | 1817 | -10.5 |
| GNPA (%) | 2.92 | 3.00 | | 3.14 | |
| NNPA (%) | 1.48 | 1.69 | | 1.72 | |
| Provision Coverage (%) | 67.0 | 65.0 | | 64.2 | |
| Total CAR (%) | 14.1 | 14.7 | | 13.0 | |
| NIM (%) | 3.17 | 3.11 | | 3.17 | |
| Advances | 110223 | 93173 | 18.3 | 105550 | 4.4 |
| Deposits | 134955 | 104928 | 28.6 | 123457 | 9.3 |

| Income Statement | | | |
|----------------------------|--------------|--------------|--------------|
| Particulars (Rs. cr) | FY19 | FY20E | FY21E |
| Interest Income | 11,419 | 13,448 | 15,816 |
| Interest Expenses | 7,243 | 8,555 | 10,014 |
| Net Interest Income | 4,176 | 4,894 | 5,802 |
| - growth % | 17 | 17 | 19 |
| Other Income | 1,351 | 1,621 | 1,864 |
| Operating Income | 5,527 | 6,515 | 7,666 |
| Operating Expenses | 2,764 | 3,144 | 3,795 |
| - Staff Cost | 1,378 | 1,591 | 1,854 |
| - Other Operating Exp. | 1,387 | 1,553 | 1,941 |
| Gross Profits | 2,763 | 3,372 | 3,871 |
| Provisions | 856 | 941 | 989 |
| Profit Before Taxes | 1907 | 2430 | 2882 |
| Taxes | 663 | 845 | 1,003 |
| Profit After Taxes | 1244 | 1585 | 1880 |

| Ratio Analysis | | | |
|---------------------------------|------|-------|-------|
| Particulars | FY19 | FY20E | FY21E |
| Basic Ratio (Rs.) | | | |
| EPS | 6.3 | 8.0 | 9.5 |
| Book Value per share | 66.9 | 74.9 | 84.3 |
| Adjusted Book Value | 58.7 | 64.9 | 74.2 |
| Dividend per share | 1.0 | 1.0 | 1.0 |
| Asset Quality (%) | | | |
| Gross NPAs | 3.0 | 2.4 | 2.3 |
| Net NPAs | 1.5 | 1.5 | 1.3 |
| PCR | 68.0 | 71.0 | 71.0 |
| Profitability ratios (%) | | | |
| RoAE | 10.7 | 11.8 | 12.6 |
| RoAA | 1.0 | 1.1 | 1.1 |
| NIM | 3.2 | 3.2 | 3.2 |
| Cost to Income | 50.0 | 51.7 | 50.0 |

| Balance Sheet | | | |
|--------------------------------|----------------|----------------|----------------|
| Particulars (Rs. cr) | FY19 | FY20E | FY21E |
| LIABILITIES | | | |
| Capital | 397 | 397 | 397 |
| Reserves & Surplus | 12,876 | 14,461 | 16,341 |
| Deposits | 134,955 | 157,461 | 186,731 |
| Borrowings | 7,781 | 8,845 | 10,069 |
| Other liabilities & provisions | 3,331 | 3,997 | 4,798 |
| Total Liabilities | 159,340 | 185,162 | 218,335 |
| ASSETS | | | |
| Cash on hand & with RBI | 6,419 | 7,203 | 8,123 |
| Money at call and short notice | 3,648 | 4,012 | 4,867 |
| Advances | 110,223 | 132,268 | 158,721 |
| Investments | 31,824 | 33,416 | 36,757 |
| Fixed assets | 472 | 497 | 546 |
| Other assets | 6,754 | 7,767 | 9,321 |
| Total Assets | 159,340 | 185,162 | 218,335 |

| Spread analysis (%) | | | |
|-----------------------------|------|-------|-------|
| | FY19 | FY20E | FY21E |
| Yield on advances | 9.0 | 9.1 | 9.1 |
| Yield on investments | 6.5 | 6.5 | 6.5 |
| Cost of deposits | 5.7 | 6.0 | 6.3 |
| Avg. Cost of funds | 5.1 | 5.1 | 5.1 |
| Spread | 3.0 | 3.0 | 3.0 |
| Interest Income to AWF | 7.8 | 8.0 | 8.0 |
| Net Interest Income to AWF | 2.9 | 2.9 | 2.9 |
| Non Interest Income to AWF | 0.9 | 1.0 | 0.9 |
| Operating Expense to AWF | 1.9 | 1.9 | 1.9 |
| Operating Profit to AWF | 1.9 | 2.0 | 2.0 |
| Net Profit to AWF | 0.9 | 0.9 | 1.0 |
| Valuation ratios (x) | | | |
| P/E | 15.6 | 12.3 | 10.3 |
| P/BV | 1.5 | 1.3 | 1.2 |
| P/ABV | 1.7 | 1.5 | 1.3 |

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Stock Rating Scale

| | Absolute Return |
|------------|------------------------|
| BUY | >20% |
| ACCUMULATE | 12% to 20% |
| HOLD | 5% to 12% |
| NEUTRAL | -5% to 5% |
| REDUCE | <-5% |

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