

## Q2FY13-Decent growth, H2 Earnings to pick up

**CMP:** Rs. 483  
**Target Price:** Rs. 533  
**Recommendation:** BUY

**The Q2 Earnings of Federal bank, though not very impressive, were largely supported by lower credit costs and non-interest income performance. However, the top-line stood not very healthy and the opex stood on the higher side.**

### Stock Info

BSE Group	A
BSE Code	500469
NSE Symbol	FEDERALBNK
Bloomberg	FB IN
Reuters	FED.BO
BSE Sensex	18505.4
NSE Nifty	5619.7

### Market Info

Market Capital	8308cr
Equity Capital	171cr
Avg. Trading Vol. (NSE Qtly-'000)	363
52 Wk High/ Low	495/322
Face Value	10

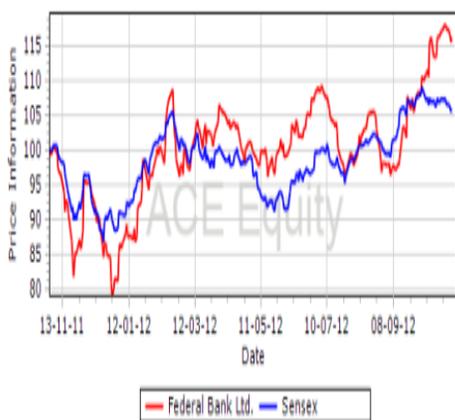
### Shareholding Pattern (%) (30<sup>th</sup> Sep 2012)

Promoters	-
Domestic Institutions	22.5
Foreign Institutions	39.9
Public & Others	37.7

**Top-line disappoints, H2FY13 expected to be better:** The bank disappointed on top-line performance with poor net interest income for the second quarter in a row that was recorded at Rs 506 crs with mere 7% YoY growth and 3% growth on sequential basis for the quarter. But, the other income show was strong at Rs 139 crs that witnessed 19% growth YoY. This combined with lower credit costs that fell above 50% levels both on YoY and QoQ basis, boosted the profitability that recorded 13% growth both YoY and QoQ. However, with the business momentum picking up in the second half of the fiscal year, we expect 20% CAGR growth in Net interest income for the bank driven by credible loan growth and strengthening liability franchise. The first quarter tends to be subdued wrt business, but going ahead we expect the bank to maintain RoEs in the range of 15-16% and RoAs at 1.4% for FY13-14.

**NPLs inched upwards, no major concern:** The quarter witnessed rise in GNPLs to Rs 1435 crs from 1250 crs a year ago. The slippages in certain pockets; particularly; SME have gone up for the quarter. Also, the restructured book needs to have a closer look given the bank's exposure to SEBs and certain shaky infrastructure accounts. However, the provision cushion with coverage ratio at 82% levels provides relief. Moreover, the credit costs for the quarter at 0.21% stood on the lower side and have been consistently improving each quarter. Though we model in higher NPLs for the bank, the bank still stands to report healthy return ratios in tough environs which make us positive on the stock.

**Investment Outlook:** We continue to remain confident wrt fundamentals of the bank and given the inherent balance sheet strength, provision cushion, healthy capital cushion, adequacy and good return ratios, we Maintain BUY. We derive comfort on the asset quality front of the bank due to signs of marked improvement and hence reduce the credit costs estimates marginally for FY14; thereby boosting the profitability of the bank. Hence, we revise the target price upwards to Rs 533 (earlier Rs 480) valuing the bank at 1.3X P/ABV FY14E and reckon that Federal Bank stands as a strong fundamental bet with comfortable valuations and continues to maintain healthy balance sheet proving to be one of the best managed banks particularly amongst the small private sector space.



(Rs Cr)	FY11	FY12	FY13E	FY14E
Net interest income	1747	1953	2296	2809
Operating Profit	1430	1506	1807	2258
PAT	590	776	937	1137
EPS (Rs)	34.3	45.4	54.8	66.5
EPS Growth (%)	26.4%	32.3%	20.6%	21.3%
RoE (%)	12.0	14.4	15.4	16.4
P/E (x)	14.1	10.6	8.8	7.3
PABV (x)	1.6	1.4	1.3	1.2

Oct 31, 2012



**Table 1:- Q2FY13 Earnings Snapshot**

Particulars (Rs in Cr)	Q2FY13	Q2FY12	YoY%	Q1FY13	QoQ %	Comments
Interest Earned	1,526	1,368	11.5	1,537	-0.7	
Interest Expended	1,020	893	14.1	1,045	-2.4	
<b>Net Interest Income</b>	<b>506</b>	<b>474</b>	<b>6.6</b>	<b>492</b>	<b>2.9</b>	NII performance disappoints
Other Income	139	117	19.2	124	12.1	Other income YoY basis showed decent performance
<i>Other income / Net Income (%)</i>	22	20		20		
<b>Total income</b>	<b>645</b>	<b>591</b>	<b>9.1</b>	<b>616</b>	<b>4.8</b>	
Employee Expenses	159	128	24.3	152	4.6	
Non-Employee expenses	136	102	33.8	117	16.4	
<b>Operating Expenses</b>	<b>296</b>	<b>230</b>	<b>28.5</b>	<b>269</b>	<b>9.7</b>	YoY opex stood on the higher side
<i>Cost-income Ratio (%)</i>	46	39		44		As a result, C/I ratio stood on the higher side
<b>Pre-Prov Profits</b>	<b>350</b>	<b>361</b>	<b>-3.2</b>	<b>347</b>	<b>0.9</b>	
Provisions & Contingencies	30	72	-57.8	63	-51.5	Credit costs moved down dramatically
<b>PBT</b>	<b>319</b>	<b>289</b>	<b>10.4</b>	<b>284</b>	<b>12.5</b>	
Provisions for Tax	104	98	6.3	93	11.5	
<i>Effective Tax Rate (%)</i>	33	34		33		
<b>PAT (reported)</b>	<b>215</b>	<b>191</b>	<b>12.5</b>	<b>190</b>	<b>13.0</b>	<b>Bottom-line growth supported by lower credit costs and other income growth</b>
EPS Basic	50.3	44.7		44.5		
EPS Diluted	50.3	44.7		44.5		
GNPA	1435	1250		1409		NPLs stood on the higher side, sequential though not very high, slippages in certain pockets have moved up for the quarter
NNPA	245	196		236		
GNPA (%)	3.8	3.6		3.6		
NNPA (%)	0.7	0.6		0.6		
Total CAR (%)	15.8	15.1		15.5		

Source: - Company, Arihant Research



Income Statement				
Year to 31st March (Rs.Cr)	FY11	FY12	FY13E	FY14E
Interest Income	4052	5558	6499	7763
Interest Expenses	2305	3605	4203	4954
<b>Net Interest Income</b>	<b>1747</b>	<b>1953</b>	<b>2296</b>	<b>2809</b>
- growth %	24	12	18	22
Non-interest Income	520	532	643	767
<b>Operating Income</b>	<b>2266</b>	<b>2485</b>	<b>2940</b>	<b>3576</b>
- growth %	17	10	18	22
Operating Expenses	836	979	1132	1318
- Staff Cost	480	544	617	706
- Other Operating Exp.	356	435	515	612
<b>Gross Profits</b>	<b>1430</b>	<b>1506</b>	<b>1807</b>	<b>2258</b>
- growth %	13	5	20	25
Provisions	525	337	408	535
<b>Profit Before Taxes</b>	<b>905</b>	<b>1169</b>	<b>1399</b>	<b>1723</b>
Taxes	315	393	462	586
<b>Profit After Taxes</b>	<b>590</b>	<b>776</b>	<b>937</b>	<b>1137</b>
- growth %	27	32	21	21

Balance sheet				
As on 31st March (Rs. Cr)	FY11	FY12	FY13E	FY14E
<b>LIABILITIES</b>				
Capital	171	171	171	171
Reserves & Surplus	4,938	5,535	6,302	7,269
Deposits	43,014	48,937	57,256	67,563
- growth %	19	14	17	18
Borrowings	1,888	4,241	6,535	7,744
Other liabilities & provisions	1,445	1,742	3,217	4,567
<b>TOTAL LIABILITIES</b>	<b>51,456</b>	<b>60,627</b>	<b>73,482</b>	<b>87,315</b>
<b>ASSETS</b>				
Cash, Inter-bank, etc	2,936	2,424	4,008	4,696
Money at call and short notice	813	1,108	1,161	1,394
Advances	31,953	37,756	45,307	54,369
- growth %	19	18	20	20
Investments	14,538	17,402	20,750	24,052
Fixed assets	290	326	403	496
Other assets	926	1,610	1,853	2,308
<b>TOTAL ASSETS</b>	<b>51,456</b>	<b>60,627</b>	<b>73,482</b>	<b>87,314</b>

Ratio Analysis				
	FY11	FY12	FY13E	FY14E
<b>Basic Ratio (Rs.)</b>				
EPS	34.3	45.4	54.8	66.5
Book Value per share	298.4	333.3	378.1	434.7
70% Adjusted Book Value	307.3	341.8	371.4	418.7
Dividend per share	8.5	9.0	8.5	8.5
<b>Asset Quality (%)</b>				
Gross NPAs	3.6	3.4	3.8	4.1
Net NPAs	0.6	0.7	1.4	1.8
NPA Coverage	83.4	81.1	63.4	57.6
<b>Profitability ratios (%)</b>				
RoAE	12.0	14.4	15.4	16.4
RoAA	1.2	1.4	1.4	1.4
NIM	4.0	3.8	3.8	3.9
Operating Profit Margin	31.2	24.7	25.3	26.5
Net Profit Margin	12.8	12.8	13.1	13.3
Cost to Income	36.9	39.4	38.5	36.9

	FY11	FY12	FY13E	FY14E
<b>Spread analysis (%)</b>				
Yield on advances	10.8	12.0	12.2	12.2
Yield on investments	6.3	8.2	7.3	7.3
Yield on interest-earning assets	8.7	10.0	9.8	9.8
Cost of deposits	5.5	7.2	7.4	7.5
Cost of funds	5.1	6.8	6.6	6.5
Spread	3.5	3.2	3.2	3.3
Net Interest Income to AWF	3.8	3.6	3.5	3.7
Non Interest Income to AWF	1.1	1.0	1.0	1.0
Operating Profit to AWF	3.1	2.8	2.8	2.9
Net Profit to AWF	1.3	1.4	1.4	1.5

	FY11	FY12	FY13E	FY14E
<b>Valuation ratios (x)</b>				
P/E	14.1	10.6	8.8	7.3
P/BV	1.6	1.4	1.3	1.1
P/ABV	1.6	1.4	1.3	1.2



**Arihant Research Desk**

E. research@arihantcapital.com  
T. 022-42254834

**Head Office**

3<sup>rd</sup> Floor, Krishna Bhavan,  
67 Nehru Road, Vile Parle (East),  
Mumbai - 400057  
Tel: (91-22) 42254800  
Fax: (91-22) 42254880

**Registered Office**

E-5 Ratlam Kothi  
Indore - 452003, (M.P.)  
Tel: (91-731) 3016100  
Fax: (91-731) 3016199

**Stock Rating Scale**

	<b>Absolute Return</b>
BUY	>20
ACCUMULATE	12-20
HOLD	5-12
REDUCE	<5

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