



DALAL & BROACHA
STOCK BROKING PVT. LTD.

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Result update@ Dalal & Broacha

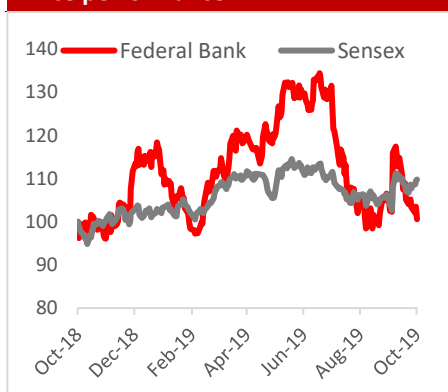
BUY

Current Price	82
52 Week Range	110/76
Target Price	98
Upside (%)	19

Key Share Data

Market Cap (Rs.bn)	163.42
Market Cap (US\$ Mn)	2288
No of o/s shares (Mn)	1986
Face Value	2
BSE Code	500469
NSE Code	FEDERALBNK
Bloomberg	FB:IN

Price performance



% Shareholding	Sep-19	June-19
FII	37.5	37.5
DII	30.5	30.5
Others	32.0	32.0
Total	100	100

Federal Bank (FB) reported a Net profit of Rs 4167 Mn (8% below our estimate) for Q2 FY20, mainly due to elevated provisions (+31% QoQ) and higher operating cost (+8% QoQ). While loan growth (+15% YoY in 2QFY20) was stable, NII were dented (~6% miss) by interest reversals and fall in T-bill. Asset quality of the bank worsen during the quarter, with GNPA's stood at 3.07% in Q2FY20, as against 2.99% QoQ and 3.11% YoY. The comforting factor from the results is that the major slippages are from portfolios identified as stressed.

Business momentum has sustained, and we expect return ratios to gradually improve over the next 2 to 3 quarters, supported by stable loan growth, better margin and higher other income. Bank's RoA and RoE came in at 1.03%/12.06% (annualized) in Q2FY20. Management expects another 10-12 bps improvement in each passing year to reach an RoA of 1.35% by FY22. For FY20, bank targets exit quarter ROA of 1.1%.

Bank's loan growth was driven by retail loans, which grew by 22.6% YoY, whereas corporate and Commercial Banking loans have grown by 8.5% YoY and 8.8% YoY respectively. Strong growth in retail loans was aided by 24% YoY and 29% YoY growth in housing loans and mortgages respectively. Bank is moving closer towards its desired loan mix of a 50:50 retail-wholesale loan book, with the share of retail loans being 49% and corporate loans at 51% in Q2FY20. On liabilities, deposits growth was also strong at 18% YoY/5% QoQ with continued retail deposit traction keeping CASA mix steady at 31.6%.

Asset quality: FEDB's asset quality worsen during the quarter with rise (QoQ) in gross NPA's by 8 bps (7.6% QoQ in absolute term) and net NPA's by 10 bps (12.3% QoQ in absolute term) at 3.07% and 1.59% respectively. Credit cost was restricted at 62 bps (vs 63 bps in Q1FY20/ Rs 64 bps in Q2FY19). Bank is targeting PCR to ultimately be 70% (including tech write off)/50% (Excluding tech write off) over the few quarters. Gross slippages for the quarter rose to Rs 5400 Mn from Rs 4150 Mn in Q1FY20, spread across both corporate and retail loans. Out of total corporate slippages of Rs 1990 mn, Rs 1900 mn came from one large cooperate account, where bank has coverage of 2x. Bank has exposure of about Rs 2100 Mn in a completed IL&FS project, and as of now it is standard asset. Bank is likely to sell this account in Q3FY20. Given the large exposure in Kerala & volatile past performance, we have factored in slippages of 2% in FY20E.

Operating performance: Bank's operating performance deteriorated during the quarter, with cost-to-income ratio increased by 411 bps QoQ/532 bps YoY to 53.5%, mainly due to opex growth of 27.5% vs 14.8% of net income growth. The main driver of higher operating costs was additional provision for wage hike (Rs 280 Mn for 23 months) and pension related exp (Rs 1400 Mn). FEDB's operating profit increased by 3% YoY (down 8.2% QoQ) to Rs 7188 Mn.

Valuation and Outlook

We expect the bank's business to register a 19% CAGR over FY19-21E, with advances and deposits CAGR of 18% and 19%, respectively. We believe, return ratios are on track to improve with moderate risk on asset quality but valuation remains reasonable, hence we retain BUY with revised TP of Rs 98 (from 130) based on 1.4x Mar-21 ABV

Key Financials (Rs Mn)

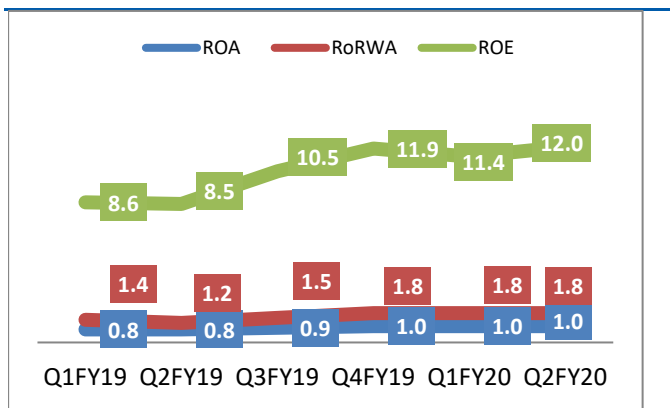
Year	NII	Growth (%)	PPOP	Growth (%)	PAT	Growth (%)	BVPS	PB (X)	ROE
FY19	41764	17	27631	21	12439	42	67	1.2	9.8
FY20E	49372	18	32651	18	15905	28	73	1.1	11.4
FY21E	58643	19	39196	20	20084	26	81	1.0	13.1



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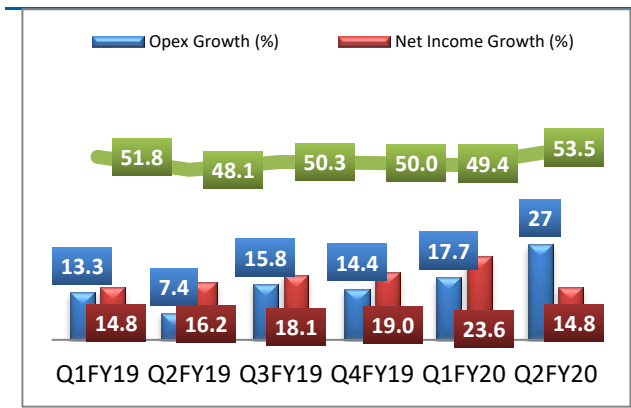
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Exhibit 1: sustainability in return ratios



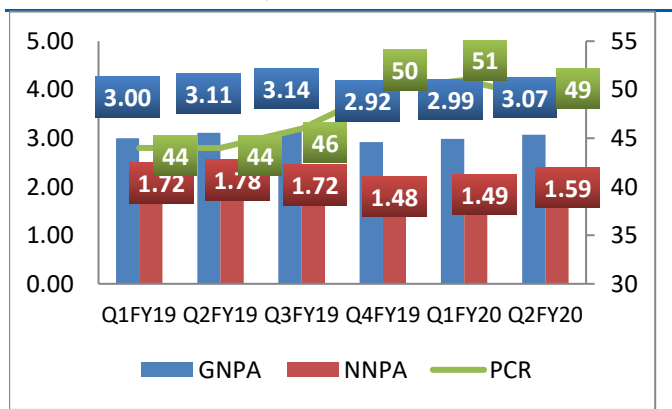
Source: D&B Research, Company

Exhibit 2: Operational Efficiency deteriorated



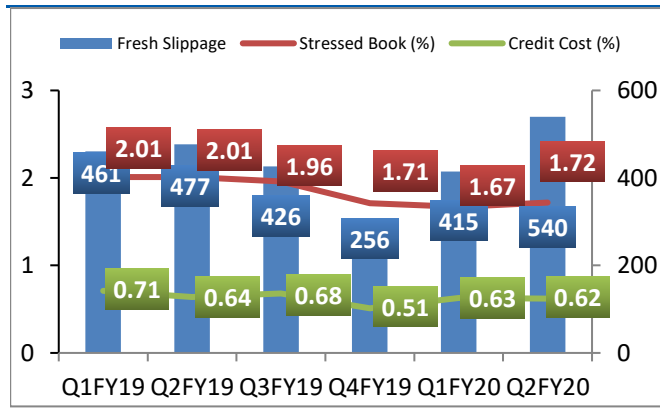
Source: D&B Research, Company

Exhibit 3: Asset Quality worsen



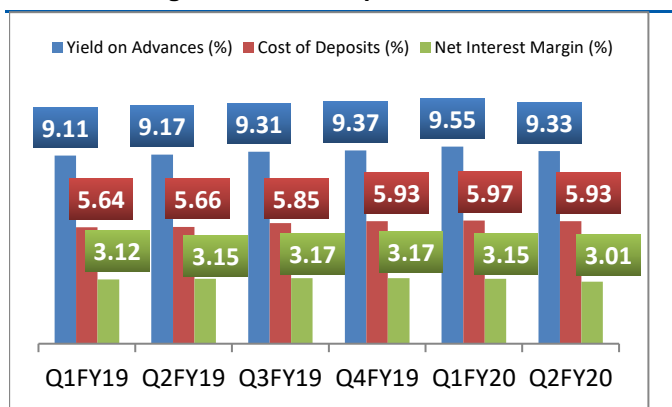
Source: D&B Research, Company

Exhibit 4: Materially reduced stressed book size



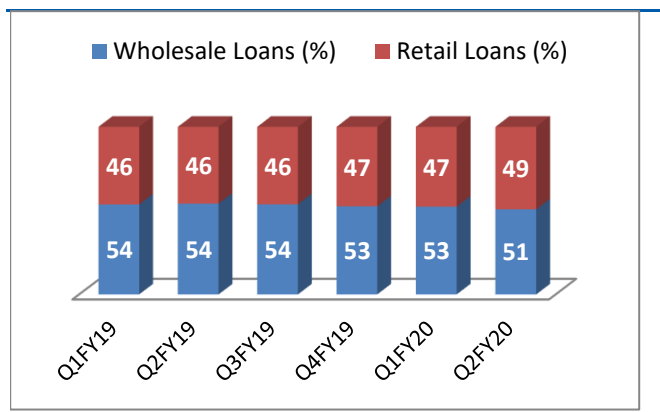
Source: D&B Research, Company

Exhibit 5: Margins came under pressure



Source: D&B Research, Company

Exhibit 6: Loan Book Mix



Source: D&B Research, Company



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<i>P&L (Rs mn)</i>	FY18	FY19	FY20	FY21
Interest Earned	97529	114190	136586	164207
Interest Expended	61701	72427	87214	105565
NII	35828	41764	49372	58643
Other Income	11591	13510	15285	17314
Net Income	47419	55274	64657	75956
Opex	24509	27643	32006	36760
PPOP	22910	27631	32651	39196
Provisions	9472	8559	10499	11224
PBT	13439	19073	22152	27973
Tax	4650	6634	6247	7888
PAT	8788	12439	15905	20084

<i>Ratios (%)</i>	FY18	FY19	FY20	FY21
Growth				
NII	17	17	18	19
Operating profit	19	21	18	20
Net profit	6	42	28	26
Advances	25	20	18	19
Deposits	15	21	18	20
Returns				
ROA	0.7	0.8	0.9	1.0
ROE	8	9.8	11.4	13.1

<i>BS (Rs mn)</i>	FY18	FY19	FY20	FY21
Capital	3944	3970	3970	3970
Reserves	118158	128760	141220	156953
Deposits	1119925	1349543	1596324	1907989
Borrowings	115335	77813	98752	108215
Other Liabilities	25777	33313	43812	55036
Total	1383140	1593400	1884077	2232163
Cash & Bank	92034	100668	165578	201895
Investments	307811	318245	343226	401453
Advances	919575	1102230	1296589	1542941
Fixed Assets	4574	4720	5204	5779
Other Assets	59146	67537	73481	80094
Total	1383140	1593400	1884077	2232163

<i>Ratios (%)</i>	FY18	FY19	FY20	FY21
Asset quality				
GNPA	3.0	2.9	3.1	2.7
NNPA	1.7	1.5	1.7	1.5
PCR	43	50	45	47
Per share (Rs)				
EPS	4.5	6.3	8.0	10.1
ABVPS	54	59	62	70
P/E	18	13	10	8
P/ABVPS	1.5	1.4	1.3	1.2



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