

Federal Bank's numbers were above our estimates on the profitability front mainly due to lower provisions, though the operating performance was below our expectations, mainly due to higher operating expenses. Bank's asset quality improved during the quarter, with GNPA's sequentially down by 26 bps at 3.24% and NNPA's down by 11 bps to 1.12%. PCR stood at 66.2% vs 65.7% QoQ.

- **NII came in at INR 14.79 Bn, +7.2% YoY / +4.3% QoQ**
- **Other Income came in at INR 4.44 Bn, -1.1% YoY / -19.6% QoQ**
- **PPOP came in at INR 8.65 Bn, -8.7% YoY / -16.6% QoQ**
- **Provisions came in at INR 2.45 Bn, -53.9% YoY / -54.9% QoQ**
- **PAT came in at INR 4.60 Bn, 49.6% YoY/25.3% QoQ**
- **EPS stood at INR 2.22 vs INR 1.84 / INR 1.54 in Q2FY21 / Q1FY22 respectively**

Financial Highlights

- Bank has shown credit growth of 9.4% YoY/ 3.6% QoQ in Q2FY22. Out of which, retail advances grew by 12% YoY, agri business by 20% YoY and business banking by 10%, while wholesale book up by 5.5% YoY.
- Deposits grew by 9.7% YoY/1.5% QoQ in Q2FY22 led by CASA growth of 17.8% YoY/5.5% QoQ taking CASA ratio to 36.2% (all time high level) Vs 33.7% YoY. Digital channel adoption and CASA enabling products (Trade & Transaction products) helped Avg CASA grow by 41% YoY in CIB (Corporate Banking) and 21% YoY in CoB (Commercial Banking).
- The bank's deposit franchise is among the most granular with >94% retail deposits, driving cost of deposits at 4.7% in Q2FY22 (lower by ~13bps YoY).
- Opex stood at Rs. 10.59 Bn, is up by 20% YoY and 13.5% QoQ. The YoY increase in opex is driven by 17.3% YoY increase in employee expenses & increase of 23.2% YoY in other expenses. Consequently, Bank's cost to income ratio stood at 55.05%, up by 680 bps YoY.
- Despite being a branch-light business model, the bank's opex ratios remain elevated due to lower revenues (mainly NIMs) and sticky costs. The bank has started diversifying its loan book into higher-margin CV, MFI and Credit Card businesses, which will support NIMs and drive up RoA in the medium to long term.

Financial Summary

Y/E Mar (Rs Bn)	FY20	FY21E	FY22E	FY23E
NII	46.5	55.3	62.5	73.8
Adjusted net profit	15.4	15.9	19.8	25.3
Networth	145	161	188	210
Adj BVPS	65	73	81	91
EPS (Rs)	7.7	8.0	9.4	12.0
P/ABV (x)	1.6	1.4	1.3	1.1
P/E (x)	13.4	13.1	11.0	8.6
RoA (%)	0.9	0.8	0.9	1.0
RoE (%)	11.1	10.4	11.3	12.7

Source: Dalal & Broacha Research, Company

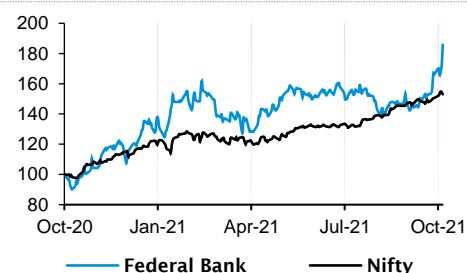
Rating	TP (Rs)	Up/Dn (%)
BUY ON DIPS	118	13

Market data

Current price	Rs	104
Market Cap (Rs.Bn)	(Rs Bn)	219
Market Cap (US\$ Mn)	(US\$ Mn)	2918
Face Value	Rs	2
52 Weeks High/Low	Rs	106/50
Average Daily Volume	('000)	26328
BSE Code		500469
Bloomberg		FB:IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Sep-21	Jun-21
FII	25.9	24.1
DII	42.5	43.9
Others	31.6	32.1
Total	100	100

Source: BSE

Avinash Tanawade
(022) 67141449
avinash.tanawade@dalal-broacha.com

- Covid specific restructuring as on Q2 FY22 stood at 2.49% of loans (vs ~1% of loans in FY21). The bank's gross stressed assets (GNPA+Rstd) increased to 5.8% vs 5.4% QoQ.
- We expect LGDs to remain low for restructuring book, as 80% of the restructured book has >75% security coverage, while 73% of this has >100% security cover.
- Collection efficiency has also improved to 96%, boding well for asset quality trends.
- Credit cost for the quarter stood at 0.7% vs 1.7% QoQ. As per latest changes in accounting policies, the recoveries are now netted off from provisions instead of being included in other income, which helps lower provisions during Q2FY22.
- Employee costs are up due to pension costs plus DA.
- Bank saw strong traction in core fee income at Rs 3.73 Bn, up by 29% YoY/46% QoQ.
- Meanwhile, the bank guided that it should cross 1% mark by Q4FY22 and 1.2% by end of FY24. All line items will contribute towards improving ROA.

We expect LGDs to remain low for restructuring book, as 80% of the restructured book has >75% security coverage, while 73% of this has >100% security cover.

Bank saw strong traction in core fee income at Rs 3.73 Bn, up by 29% YoY/46% QoQ.

Bank guided that it should cross 1% mark by Q4FY22 and 1.2% by end of FY24. All line items will contribute towards improving ROA.

Valuation and outlook

We like Federal bank for its healthy liability franchise (94% retail Deposit), increasing retail focus, strong fee income, and prudent provisioning. Even though Asset Quality is likely to remain under pressure in the near term, we take comfort from its tier-1 capital ratio (14.09%) and improvement in core operating performance, which provide an additional buffer to cushion any adverse effect of sudden spikes in slippages. We expect the bank's RoA/RoE to be around 0.9%/11.3% in FY22 and recover back to 1%/12.7% in FY23. At CMP the stock trades at 1.3x its FY22E ABV and 1.1x its FY23E ABV. We assign a BUY ON DIPS rating with a Target Price of Rs 118/share, valuing the stock at a target multiple of 1.3x FY23E ABV.

Financials

Rs Mn	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY23
Interest Earned	33,968	34,442	34,879	34,595	33,663	33,557	33,793
Interest Expended	21,808	21,477	21,081	20,225	19,460	19,373	18,998
NII	12,160	12,964	13,799	14,370	14,204	14,184	14,794
Other Income	7,111	4,884	4,494	4,818	4,654	5,518	4,444
Net Income	19,271	17,848	18,292	19,189	18,858	19,702	19,238
Opex	9,678	8,524	8,827	9,560	10,007	9,334	10,590
PPOP	9,593	9,324	9,466	9,629	8,851	10,368	8,648
Provisions	5,675	3,946	5,321	4,206	2,423	5,435	2,453
PBT	3,918	5,378	4,145	5,423	6,428	4,934	6,195
Tax	906	1,370	1,069	1,382	1,650	1,261	1,592
PAT	3,012	4,008	3,076	4,041	4,778	3,673	4,603
Balance Sheet							
Net-worth	1,45,176	1,49,225	1,52,353	1,56,450	1,61,236	1,64,880	1,77,270
Deposits	15,22,901	15,49,380	15,67,474	16,16,700	17,26,445	16,93,930	17,19,948
Advances	12,22,679	12,12,970	12,29,120	12,55,050	13,18,786	12,97,650	13,44,046
Growth (%)							
NII	10.9	12.3	22.8	24.4	16.8	9.4	7.2
PPOP	27.1	19.1	31.7	29.5	-7.7	11.2	-8.6
PAT	-21.0	4.3	-26.2	-8.3	58.6	-8.4	49.6
Deposits	12.8	16.9	12.3	11.8	13.4	9.3	9.7
Advances	10.9	8.3	6.1	5.3	7.9	7.0	9.4
Efficiency (%)							
GNPA	2.8	3.0	2.8	2.7	3.4	3.5	3.2
NNPA	1.3	1.2	1.0	0.6	1.2	1.2	1.1
PCR	54.5	59.6	65.7	78.2	65.9	65.7	66.2
Credit Cost (annualized)	1.9	1.3	1.7	1.3	0.7	1.7	0.7
C/I Ratio	50.2	47.8	48.3	49.8	53.1	47.4	55.0
CASA	30.5	32.0	33.7	34.5	33.8	34.8	36.2
NPA Composition							
Retail	20	19	19	19	27	28	27
Agri	16	16	16	15	16	18	19
Business banking	39	37	37	37	18	20	20
Wholesale	25	28	29	29	40	34	34

Source: Dalal & Broacha Research, Company

Financial

P&L (Rs Bn)	FY20	FY21	FY22	FY23
Interest income	132.1	137.6	158.0	195.5
Interest expense	85.6	82.2	95.5	121.7
NII	46.5	55.3	62.5	73.8
Non-interest income	19.3	19.4	21.8	25.8
Net revenues	65.8	74.8	84.3	99.6
Operating expenses	33.8	36.9	42.7	48.8
PPOP	32.0	37.9	41.6	50.7
Provisions	11.7	16.5	15.1	16.9
PBT	20.3	21.4	26.5	33.8
Tax	4.9	5.5	6.7	8.5
PAT	15.4	15.9	19.8	25.3

Balance sheet	FY20	FY21	FY22	FY23
Share capital	3.99	3.99	4.20	4.20
Reserves & surplus	141.2	157.2	184.0	206.3
Net worth	145.2	161.2	188.2	210.5
Deposits	1,522.9	1,726.4	2,020.4	2,396.5
Borrowings	103.7	90.7	91.8	96.6
Other liability	34.6	35.3	37.6	42.0
Total liabilities	1,806.4	2,013.7	2,338.0	2,745.6

Fixed assets	4.8	4.9	5.1	5.2
Investments	358.9	371.9	455.0	561.6
Loans	1222.7	1318.8	1544.7	1835.6
Cash	125.7	195.9	223.9	228.5
Other assets	94.2	122.2	109.3	114.7
Total assets	1806.4	2013.7	2338.0	2745.6

Source: Dalal & Broacha Research, Company

Ratios	FY20	FY21	FY22	FY23
Growth (%)				
NII	11.3	19.0	12.9	18.1
PPOP	16.0	18.2	9.9	21.9
PAT	24.0	3.1	24.6	27.6
Advances	10.9	7.9	17.1	18.8
Deposits	12.8	13.4	17.0	18.6
Spread (%)				
Yield on Funds	8.2	7.7	7.7	8.1
Cost of Funds	5.6	4.8	4.9	5.3
Spread	2.6	2.9	2.8	2.8
NIM	2.9	3.1	3.0	3.0
Asset quality (%)				
Gross NPAs	2.8	3.4	3.3	2.9
Net NPAs	1.3	1.2	1.1	1.1
Provisions	53	66	66	62
Return ratios (%)				
RoE	11.1	10.4	11.3	12.7
RoA	0.9	0.8	0.9	1.0
Per share (Rs)				
EPS	8	8	9	12
BV	73	81	90	100
ABV	65	73	81	91
Valuation (x)				
P/E	13.4	13.1	11.0	8.6
P/BV	1.4	1.3	1.2	1.0
P/ABV	1.6	1.4	1.3	1.1

Disclaimer

Dalal & Broacha Stock Broking Pvt Ltd, hereinafter referred to as D&B (CINU67120MH1997PTC111186) was established in 1997 and is an integrated financial services player offering an extensive range of financial solutions and services to a wide spectrum of customers with varied needs ranging from equities to mutual funds to depository services.

D&B is a corporate trading member of Bombay Stock Exchange Limited (BSE), National Stock Exchange of India Limited (NSE). D&B along with its affiliates offers the most comprehensive avenues for investments and is engaged in the securities businesses including stock broking (Institutional and retail), depository participant, portfolio management and services rendered in connection with distribution of primary market issues and financial products like mutual funds, fixed deposits. Details of associates are available on our website i.e. www.dalal-broacha.com

D&B is registered as Research Analyst with SEBI bearing registration Number INH000001246 as per SEBI (Research Analysts) Regulations, 2014.

D&B hereby declares that it has not defaulted with any stock exchange nor its activities were suspended by any stock exchange with whom it is registered in any time in the past. It has not been debarred from doing business by any Stock Exchange / SEBI or any other authorities; nor has its certificate of registration been cancelled by SEBI at any point of time.

SEBI and Stock Exchanges have conducted the routine inspection and based on their observations have issued advice letters or levied minor penalty on D&B for certain operational deviations in routine course of business.

D&B offers research services to clients as well as prospects. The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

Other disclosures by D&B (Research Entity) and its Research Analyst under SEBI (Research Analyst) Regulations, 2014 with reference to the subject company(s) covered in this report:-

D&B or its associates may have financial interest in the subject company.

D&B or its associates do not have any material conflict of interest in the subject company.

The Research Analyst or Research Entity (D&B) has not been engaged in market making activity for the subject company.

D&B or its associates may have actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of Research Report.

Disclosures in respect of Research Analyst:

Whether Research Analyst or his/her relatives have actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of Research Report:	No
Whether the Research Analyst or his/her relative's financial interest in the subject company.	No
Whether the research Analyst has served as officer, director or employee of the subject company	No
Whether the Research Analyst has received any compensation from the subject company in the past twelve months	No
Whether the Research Analyst has managed or co-managed public offering of securities for the subject company in the past twelve months	No
Whether the Research Analyst has received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
Whether the Research Analyst has received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
Whether the Research Analyst has received any compensation or other benefits from the subject company or third party in connection with the research report	No

D&B and/or its affiliates may seek investment banking or other business from the company or companies that are the subject of this material. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that may be inconsistent with the recommendations expressed herein.

In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest including but not limited to those stated herein. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein. This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject D&B or its group companies to any registration or licensing requirement within such jurisdiction. Specifically, this document does not constitute an offer to or solicitation to any U.S. person for the purchase or sale of any financial instrument or as an official confirmation of any transaction to any U.S. person. Unless otherwise stated, this message should not be construed as official confirmation of any transaction. No part of this document may be distributed in Canada or used by private customers in United Kingdom. All material presented in this report, unless specifically indicated otherwise, is under copyright to D&B. None of the material, nor its content, nor any

copy of it, may be altered in any way, transmitted to, copied or distributed to any other party, without the prior express written permission of D&B . All trademarks, service marks and logos used in this report are trademarks or registered trademarks of D&B or its Group Companies. The information contained herein is not intended for publication or distribution or circulation in any manner whatsoever and any unauthorized reading, dissemination, distribution or copying of this communication is prohibited unless otherwise expressly authorized. Please ensure that you have read "Risk Disclosure Document for Capital Market and Derivatives Segments" as prescribed by Securities and Exchange Board of India before investing in Indian Securities Market. In so far as this report includes current or historic information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

Address: - 508, Maker Chambers V, 221 Nariman Point, Mumbai 400 021 .

Tel: 91-22- 2282 2992 | E-mail: equity.research@dalal-broacha.com
