

Retail credit growth trending well



Federal Bank reported its Q4FY21 performance which was well above our estimates on the profitability front due to lower Provisions. However, operating performance was lower than expected on account of higher operating expenses and lower than expected growth in net interest income.

- NII came in at INR 14.20 Bn, 16.8% YoY/-1.2% QoQ.
- Other Income came in at INR 4.65 Bn, -34.6% YoY/-3.4% QoQ.
- PPOP came in at INR 8.85 Bn, -7.7% YoY/-8.1% QoQ.
- Provisions came in at INR 2.42 Bn, -57.3% YoY/-42.4% QoQ.
- PAT came in at INR 4.78 Bn, 58.6% YoY/18.2% QoQ.
- EPS stood at INR 2.4 vs INR 1.5 YoY/ INR 2.03 QoQ.

Financial Highlights

- Bank has shown credit growth of 8.6% YoY/5.2% QoQ in Q4FY21, led by Agri (up 23.2% YoY/2.6% QoQ) and Retail (up 18.6% YoY/6.3% QoQ). Wholesale loans declined by 1.1% YoY (up 5.8% QoQ). Given the current focus on gold loans, the segment witnessed robust growth (up 70% YoY). Wholesale constitutes 46% of the overall book (down 453bps YoY) and is likely to drop going ahead. The bank's retail to wholesale mix (54:46) is closer to management's vision of 55:45 mix.
- Bank's asset quality numbers were largely stable, with GNPA & NNPA stood at 3.41% & 1.19% vs 3.38% & 1.14% on a proforma basis in Q3FY21. PCR stood at 65.9% vs 54.5% YoY. The overall Covid related restructured book stood at Rs14.09bn, which is way lower than the Rs15-16bn management had earlier guided to. While collection efficiency for March 2021 remained stable at 95%, it came down to around 90-91% in April 2021 and 88-89% in the first half of May 2021.
- The bank remains optimistic on its ability to improve collections given its favourable asset mix – 76% corporate book (36% of advances) rated A & above, ~12% gold loans and ~15% home loans.

Financial Summary

Y/E Mar (Rs Bn)	FY20	FY21E	FY22E	FY23E
NII	46.5	55.3	63.1	74.3
Adjusted net profit	15.4	15.9	19.3	26.0
Net worth	145	161	176	197
Adj BVPS	65	73	79	89
EPS (Rs)	7.7	8.0	9.7	13.0
P/ABV (x)	1.2	1.1	1.0	0.9
P/E (x)	10.0	9.7	8.0	5.9
C/D Ratio	80	76	77	78
RoA (%)	0.9	0.8	0.9	1.0
RoE (%)	11.1	10.4	11.5	14.0

Source: Company

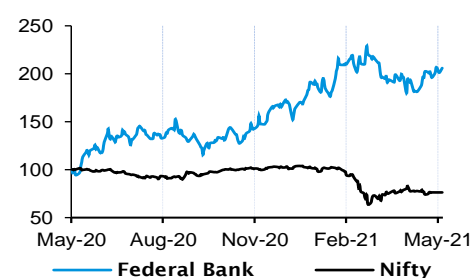
Rating	TP (Rs)	Up/Dn (%)
BUY ON DIPS	89	9

Market data

Current price	Rs	82
Market Cap (Rs.Bn)	(Rs Bn)	162.91
Market Cap (US\$ Mn)	(US\$ Mn)	2225
Face Value	Rs	2
52 Weeks High/Low	Rs	92/37
Average Daily Volume	('000)	29571
BSE Code		500469

Bloomberg FB:IN
Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Mar-21	Dec-20
Promoters	0.00	0.00
FII	24.51	21.69
DII	43.29	44.59
Others	32.20	33.71
Total	100	100

Source: BSE

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- Margin expanded 19bps YoY to 3.23% despite interest reversals. Margin expansion was largely driven by A) increase focus on high-yielding products like gold loan and calibrated growth in lower-yielding products like large corporate, etc. and B) reduced cost of deposit fell 17bps QoQ to 4.70%.

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Valuation and outlook

Given the bank's strong liability franchise, better capitalization, and higher secure portfolio, Federal Bank is better placed to withstand Covid'19-related stresses than some of its regional peers. Bank maintains a cautious approach for corporate banking while its Gold loans book continues to strengthen at Rs 158bn. Bank is also investing in ramping up its high-margin retail lending segments (CVs, MFI, and credit cards), which will support its margin expansion over the medium to long term. However with the drop in collection efficiency in April & May, we expect Bank's earnings and asset quality could remain under pressure in the near term though expected to improve sequentially depending on economic impact of pandemic second wave. At CMP, the bank trades at 1x FY22 Adj BV and 0.9x FY23 Adj BV. We recommend investors to follow buy on dips strategy, with a price target of Rs 89, valuing the stock at 1x FY23E Adj BV.

Rs Mn	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q3FY22
NII	10965	11542	11238	11549	12160	12964	13799	14370	14204
YoY %	17	18	10	7	11	12	23	24	17
QoQ %	2	5	-3	3	5	7	6	4	-1
Other Income	4117	3915	4209	4079	7111	4884	5093	4818	4654
YoY %	31.1	44.5	30.4	18.0	72.7	24.7	21.0	18.1	-34.6
QoQ %	19.1	-4.9	7.5	-3.1	74.4	-31.3	4.3	-5.4	-3.4
PPOP	7548	7828	7188	7438	9593	9324	10065	9629	8851
YoY %	28	30	3	5	27	19	40	29	-8
QoQ %	7	4	-8	3	29	-3	8	-4	-8
PAT	3815	3842	4167	4406	3012	4008	3076	4041	4778
YoY %	163	46	57	32	-21	4	-26	-8	59
QoQ %	14	1	8	6	-32	33	-23	31	18
Cost Structure									
Operating expenses	7535	7629	8259	8190	9678	8524	8827	9560	10007
YoY %	14	18	28	15	28	12	7	17	3
QoQ %	5	1	8	-1	18	-12	4	8	5
C/I Ratio %	50	49	53	52	50	48	47	50	53
Provisions	1778	1920	2518	1609	5675	3946	5921	4206	2423
YoY %	-52	-4	-13	-15	219	105	135	161	-57
QoQ %	-7	8	31	-36	253	-30	50	-29	-42
As % of advances	0.2	0.2	0.2	0.1	0.5	0.3	0.5	0.3	0.2
Asset Quality									
GNPA	2.9	3.0	3.1	3.0	2.8	3.0	2.8	2.7	3.4
NNPA	1.5	1.5	1.6	1.6	1.3	1.2	1.0	0.6	1.2
PCR	50.1	50.7	48.6	46.4	54.5	59.6	65.7	78.2	65.9

Source: Dalal & Broacha Research, Company

Highlights of the Conference Call

Asset Quality

- FY21 the slippages at Rs 18.74 Bn were in line with the slippages in FY20 (Rs 18.32 Bn).
- Collection efficiency for March 2021 stood at 95%, which came down to around 90-91% in April 2021. Collection efficiency in the first half of May stood at around 88-89%. Management expects this could improve in June 2021.
- SMA book (including SMA0, SMA1 and SMA2) stood at 4.64% of total advances (Sub 5% QoQ).
- Credit costs in FY22 could be lower than FY21 if the Covid situation did not accelerate from here.

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Elevated PCR; utilized most of its Covid related provisions

- Bank has utilized most of its Covid related provisions, and carrying ~ 10% provision cover on the restructured book.
- Overall, PCR increased from 53.4% to 65.14% on a YoY basis. Management expects this provisioning coverage to be adequate, given the large part of the book is secured and LGD expectations are lower, even post-pandemic.
- The bank used to hold ~10% excess provision over LGD during the normal business conditions (pre Covid).

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Restructured book

- Bank's Covid-19 restructured book stood at Rs 14.09 bn; out of which ~70% is secured, mostly with mortgage security. Historically, LGD for mortgage-backed loans was very low (sometimes in single digit).
- Around 30-40% of the restructured book could slip into NPAs.

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Gold loans reported a growth of 70% YoY

- Gold loan book stood at ~Rs 158.16bn (11.85% of total advances). Out of which, 1/3 is retail gold loans, while the rest is agri and MSME gold loans.
- Even though there would be some negative impact from the expiry of higher LTV of 90% in March-end, Bank is still targeting 30-40% growth for this book in the current financial year.

CV book stood at ~ Rs 10bn and has been grown completely organically, while microfinance book stood at Rs 3 Bn. Bank is looking for inorganic opportunities in microfinance segment.

CV finance & Microfinance

- CV book stood at ~ Rs 10bn and has been grown completely organically, while microfinance book stood at Rs 3 Bn. Bank is looking for inorganic opportunities in microfinance segment.
- Bank has higher expectation for these segments in FY22 & FY23 though will remain cautious over next one or two quarters.

Out of total loan portfolio, ~32% linked to EBLR, ~28% linked to MCLR and ~32% loans were on fixed rate

Segmental yields for the quarter

- Retail loans ~ 9% plus
- Agri loans ~10%
- business banking loans ~10%
- Commercial banking loans ~9%
- corporate loans ~7%

Exhibit 1:

P&L (Rs Bn)	FY20	FY21	FY22	FY23
Interest income	132.1	137.6	160.1	195.2
Interest expense	85.6	82.2	97.0	120.9
NII	46.5	55.3	63.1	74.3
Non-interest income	19.3	19.4	21.7	25.4
Net revenues	65.8	74.8	84.8	99.7
Operating expenses	33.8	36.9	41.1	48.1
PPOP	32.0	37.9	43.7	51.6
Provisions	11.7	16.5	17.8	16.8
PBT	20.3	21.4	25.9	34.8
Tax	4.9	5.5	6.5	8.8
PAT	15.4	15.9	19.3	26.0
Balance sheet	FY20	FY21	FY22	FY23
Share capital	4.0	4.0	4.0	4.0
Reserves & surplus	141.2	157.2	172.5	192.7
Net worth	145.2	161.2	176.5	196.7
Deposits	1522.9	1726.4	1999.1	2349.8
Borrowings	103.7	90.7	91.8	102.2
Other liability	34.6	35.3	37.6	42.0
Total liabilities	1806.4	2013.7	2305.0	2690.6
Fixed assets	4.8	4.9	5.1	5.2
Investments	358.9	371.9	450.2	550.6
Loans	1222.7	1318.8	1544.5	1836.6
Cash	125.7	195.9	195.9	183.4
Other assets	94.2	122.2	109.3	114.7
Total assets	1806.4	2013.7	2305.0	2690.6

Source: Dalal & Broacha Research, Company

Exhibit 2:

Ratios	FY20	FY21	FY22	FY23
Growth (%)				
NII	11.3	19.0	14.0	17.8
PPOP	16.0	18.2	15.3	18.2
PAT	24.0	3.1	21.7	34.5
Advances	10.9	7.9	17.1	18.9
Deposits	12.8	13.4	15.8	17.5
Spread (%)				
Yield on Funds	8.2	7.7	7.9	8.2
Cost of Funds	5.6	4.8	5.0	5.3
Spread	2.6	2.9	2.9	2.9
NIM	2.9	3.1	3.1	3.1
Asset quality (%)				
Gross NPAs	2.8	3.4	3.1	2.8
Net NPAs	1.3	1.2	1.2	1.1
Provisions	53	66	63	62
Return ratios (%)				
RoE	11.1	10.4	11.5	14.0
RoA	0.9	0.8	0.9	1.0
Per share (Rs)				
EPS	8	8	10	13
BV	73	81	88	99
ABV	65	73	79	89
Valuation (x)				
P/E	10.5	10.2	8.4	6.3
P/BV	1.1	1.0	0.9	0.8
P/ABV	1.3	1.1	1.0	0.9

Source: Dalal & Broacha Research, Company

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