



## Federal Bank Q1 FY16 Quarterly Update

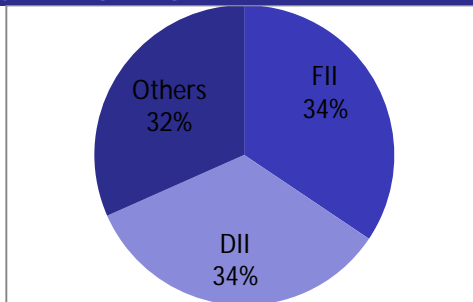
### MARKET DATA

Networth (Rs. Cr)	7,890
P/BV Ratio (FY16E) (x)	1.4
EPS (FY16E) (Rs.)	5.5
Market Price (17/07/2015) (Rs.)	68
P/E Ratio (FY16E) (x)	12.4
52 Week High (14/07/2015)(Rs.)	80
52 Week Low (11/08/2014) (Rs.)	55
Market Capitalisation (Rs. Cr)	11,720

### AVERAGE MONTHLY VOLUME ('000)

BSE	601
NSE	5,680

### SHARE HOLDING PATTERN



RETURN	3M	6M	12M
Federal Bank	5%	-5%	15%
Sensex	1%	-7%	6%

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In Q1 FY16, increase in NPA provisions by 285% QoQ (593% YoY) led by deterioration in asset quality and treasury provisions due to higher bond yields resulted in profits declining by 50% QoQ (36% YoY) to ₹ 141 cr. Net interest income de-grew by 3% QoQ (up 7% YoY) mainly due to decline in NIMs.

#### ■ Loan book de-grew QoQ; however guidance remains strong

Loan book de-grew by 3% QoQ (up 10% YoY) to ₹.50,335 cr led by de-growth of corporate book by 9% QoQ (up 3% YoY). Also, Agri book de-grew by 2% QoQ (up 17% YoY) and Retail book de-grew by 1% QoQ (up 11% YoY). However, SME portfolio grew by 1% QoQ (16% YoY). With focus on Agri, SME and Retail portfolio, share of these has increased to 12%, 32% and 26% respectively as against decline in share of corporate portfolio to 30%. Gold loan book remain a drag on retail book as it de-grew by 9% QoQ (13% YoY). Management is targeting 20% growth in SME, retail and Agri segment to achieve higher than industry growth rate. Corporate book is expected to grow at low teens due to weak capex cycle while retail growth will be stronger (20% YoY) with increase in focus on personal loan category.

#### ■ NIMs declined led by interest reversals

NIMs declined by 19bps QoQ (18bps YoY) to 3.12% led by a) interest reversals (₹.16 cr) due to high fresh slippages and b) Investment grew by 11% QoQ in G-sec securities due to low credit demand. Management guided for 3.2% NIMs for FY16. CASA ratio improved by 83bps QoQ (46bps YoY) to 31.3% in Q1 FY16 as CASA deposits grew by 5% QoQ (19% YoY) as against 2% QoQ (17% YoY) total deposits growth.

#### ■ Asset quality surprised negatively led by corporate account; Strong PCR

Large corporate account of ₹.134 cr slipped from restructured account resulted in increase in fresh slippages by 76% QoQ (73% YoY) to ₹.317 cr. SME portfolio had a slippage of ₹.109 cr (₹.95 cr Q4FY15). GNPA % increased by 55bps QoQ (39bps YoY) to 2.6% and in absolute terms increased by 23% QoQ (28% YoY). PCR continues be strong at 80.5%, though declined 340bps QoQ (437bps YoY), as NNPA % increased by 25bps QoQ (28bps YoY). Bank restructured loan of ₹.77 cr during Q1 FY16 (₹.130 cr QoQ) and outstanding restructured standard loan portfolio stood at ₹.2,583 cr (5.2% of overall loans). According to management, corporate book under watch list for stress sign stands at ₹.170 cr.

#### ■ Other Highlights

Non - interest income de-grew by 37% QoQ (up 24% YoY) led by lower trading gains and recoveries. Also, fee income de-grew by 20% QoQ (up 19% YoY). Cost to Income increased by 450 bps QoQ (280bps YoY) to 54% due to extra provisions on wage revisions of ₹.36 cr.

#### ■ Valuation

At CMP of ₹.69 Federal Bank is trading at P/B multiple of 1.4x its FY16E BV of ₹.49 and 1.3x its FY17E BV of ₹.54. We recommend a BUY rating with a target of ₹.82, calculated based on Justified P/BV multiple method, by March 2016 and an upside potential of 19%.

### Quarterly Performance:

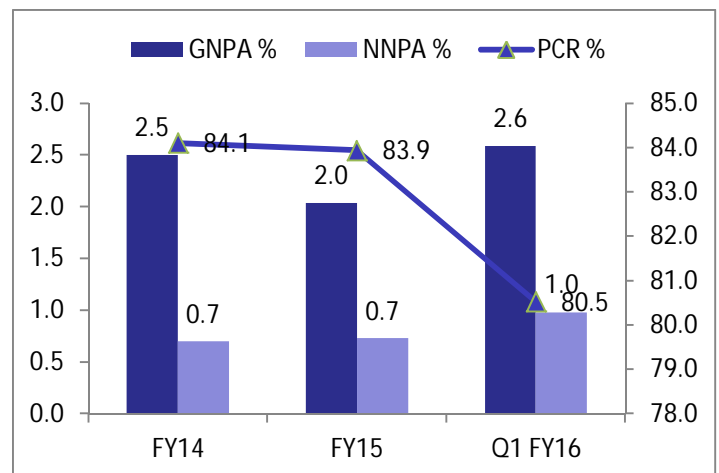
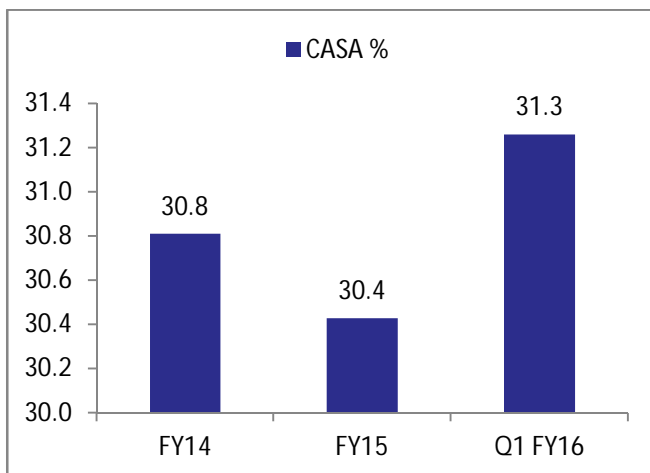
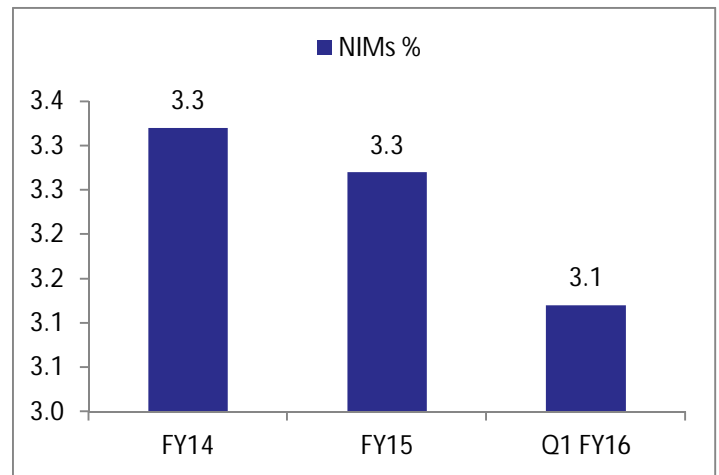
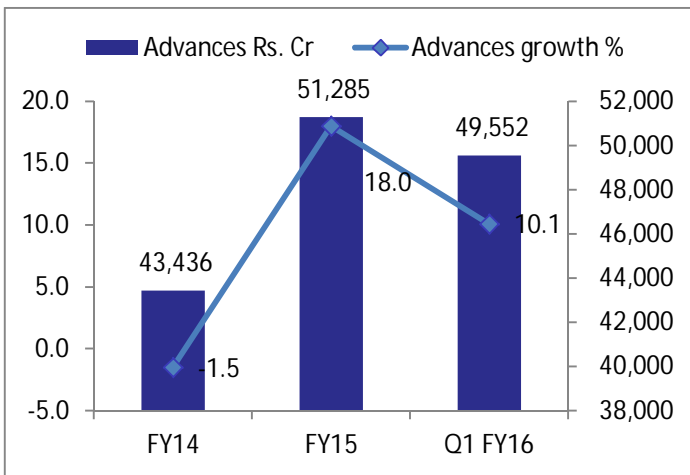
Particulars Rs. Cr	Q1 FY16	Q1 FY15	% YoY	Q4 FY15	%QoQ	FY15	FY14	% YoY
Net Interest Income	605	564	7%	623	-3%	2,380	2,229	7%
Other Income	194	157	24%	306	-37%	878	694	27%
Total Income	799	721	11%	929	-14%	3,259	2,923	12%
Operating Expenses	431	369	17%	460	-6%	1,631	1,442	13%
PPOP	367	352	4%	469	-22%	1,628	1,481	10%
Total Provisions	153	22	593%	40	285%	107	268	-60%
PBT	214	329	-35%	429	-50%	1,521	1,212	25%
Taxes	73	109	-33%	149	-51%	515	373	38%
PAT	141	220	-36%	281	-50%	1,006	839	20%



**Q1 FY16 CONFERENCE CALL HIGHLIGHTS: -**

- SME, Agri and Retail are the focus area for the bank
- Shipping account of Rs.100 cr showing signs of stress and will be dealt in Q2 FY16
- Loan book growth guidance – SME, Agri and Retail book to grow 20%
- In FY16, recoveries and up gradations expected to be same as FY15
- Credit cost guidance FY16 – 55-60bps; PCR – sustainable at 80% & Cost to Income FY16 – 51%
- Gold loan book – growth remains a challenge, however no credit risk is seen
- PSL as % of loan portfolio – 39.5%
- SEB Exposure – Rs.13,00 cr

**Graphs for important parameters**





**QUARTERLY PERFORMANCE:**

Particulars	Jun-15	Jun-14	% YoY	Mar-15	%QoQ	FY15	FY14	% YoY
Interest Income	1,913	1,772	8%	1,908	0%	7,420	6,946	7%
Interest Expenses	1,308	1,207	8%	1,285	2%	5,039	4,718	7%
Net Interest Income	605	564	7%	623	-3%	2,380	2,229	7%
Other Income	194	157	24%	306	-37%	878	694	27%
Fee Income	127	107	19%	133	-5%	498	465	7%
Total Income	799	721	11%	929	-14%	3,259	2,923	12%
Operating Expenses	431	369	17%	460	-6%	1,631	1,442	13%
Employee	252	204	23%	249	1%	892	772	16%
Others	179	165	9%	211	-15%	739	671	10%
Operating Profits before provisions	367	352	4%	469	-22%	1,628	1,481	10%
Total Provisions	153	22	593%	40	285%	107	268	-60%
PBT	214	329	-35%	429	-50%	1,521	1,212	25%
Taxes	73	109	-33%	149	-51%	515	373	38%
PAT	141	220	-36%	281	-50%	1,006	839	20%
EPS	0.8	1.3	-36%	1.6	-50%	6	5	20%
<b>Asset Quality</b>								
GNPA Rs. Cr	1,305	1,016	28%	1,058	23%	1,058	1,087	-3%
NNPA Rs. Cr	484	304	59%	373	30%	373	322	16%
GNPA %	2.59	2.2	39	2.04	55	2.04	2.50	-46
NNPA %	0.98	0.7	28	0.73	25	0.73	0.7	3
PCR % Calculated	62.86	70.10	-724	64.71	-184	64.71	70.42	-572
PCR % Reported	80.53	84.9	-437	83.94	-341	83.94	84.1	-16
Slippages	317	183	73%	180	76%	773	795	-3%
Slippage Ratio %	2.56	1.63	93	1.40	116	1.51	1.83	-32
Credit Cost %	1.24	0.20	104	0.31	93	0.21	0.62	-41
<b>Ratios %</b>								
Fees to Advances	1.03	0.95	7	1.04	-1	0.97	1.07	-10
Cost to Income ratio	54.02	51.23	280	49.52	451	50.05	49.34	71
Tax Rate	33.96	33.15	81	34.66	-70	33.88	30.78	310
Loan/Deposit	68.69	72.82	-413	72.41	-372	72.41	72.72	-31
CASA %	31.26	30.8	46	30.43	83	30.43	30.8	-37
CAR (Basel III) %	15.07	15.16	-9	15.46	-39	15.46	15.14	32
Tier I %	14.40	14.56	-16	14.81	-41	14.81	14.59	22
Quarterly NIMs	3.12	3.3	-18	3.31	-19	3.27	3.3	-3
Opex to Loan book	3.48	3.28	20	3.59	-11	3.18	3.32	-14
<b>Balance Sheet</b>								
Capital	344	342	1%	342	1%	342	342	0%
Net Worth	7,890	7,171	10%	7,758	2%	7,758	6,951	12%
FV	2	2		2		2	2	
Deposits	72,140	61,815	17%	70,825	2%	70,825	59,731	19%
Investments	27,041	23,564	15%	24,409	11%	24,409	24,118	1%
Loans	49,552	45,012	10%	51,285	-3%	51,285	43,436	18%
BV-Calculated Rs.	46	42	9%	45	1%	45	41	12%
Adjusted Network*	7,406	6,867	8%	7,385	0%	7,385	6,629	11%
Adj. BV Rs.	43	40	7%	43	0%	43	39	11%

\* Adj. Network = Reported Network - NNPA

Source: Company, Dimensional Securities



## ROA TREE ANALYSIS

Particulars	Jun-15	Mar-15	Dec-14	Sep-14	Jun-14	FY15	FY14
Interest Income	9.6%	9.7%	9.7%	10.0%	9.6%	9.4%	9.5%
Interest Expenses	6.5%	6.5%	6.7%	6.8%	6.5%	6.4%	6.5%
Net Interest Income	3.0%	3.2%	3.1%	3.2%	3.1%	3.0%	3.1%
Other Income	1.0%	1.6%	1.1%	1.0%	0.8%	1.1%	1.0%
Fee Income	0.6%	0.7%	0.6%	0.7%	0.6%	0.6%	0.6%
Total Income	4.0%	4.7%	4.2%	4.3%	3.9%	4.1%	4.0%
Operating Expenses	2.2%	2.3%	2.1%	2.1%	2.0%	2.1%	2.0%
Employee	1.3%	1.3%	1.2%	1.1%	1.1%	1.1%	1.1%
Others	0.9%	1.1%	0.9%	1.0%	0.9%	0.9%	0.9%
Operating Profits before provisions	1.8%	2.4%	2.1%	2.2%	1.9%	2.1%	2.0%
Total Provisions	0.8%	0.2%	0.0%	0.2%	0.1%	0.1%	0.4%
PBT	1.1%	2.2%	2.1%	1.9%	1.8%	1.9%	1.7%
Taxes	0.4%	0.8%	0.7%	0.7%	0.6%	0.7%	0.5%
PAT (RoA)	0.7%	1.4%	1.4%	1.3%	1.2%	1.3%	1.2%
Average Assets/Average Equity	10.64	10.70	10.57	10.61	10.85	10.70	10.94
RoE	7.5%	15.3%	14.6%	13.6%	12.9%	13.7%	12.6%

Source: Company, Dimensional Securities



### OUTLOOK & VALUATION: -

Federal bank surprised negatively on asset quality front with higher slippages from corporate accounts which impacted profitability due to higher provisions (provided 50% of corporate slippage during the quarter). However, with PCR at 80% provides cushion to credit cost going ahead with stable asset quality. Also, Tier I ratio at 14.4% should support high growth going forward as the opportunity arises with improvement in economic activity.

We expect loan book to grow better than industry at 18% CAGR (FY15-18E) with RoA and RoE to improve towards 1.2% and 14% by FY18E.

At CMP of Rs.69 Federal Bank is trading at P/B multiple of 1.4x its FY16E BV of Rs.49 and 1.3x its FY17E BV of Rs.54. We recommend a BUY rating with a target of Rs.82 calculated based on Justified P/BV multiple by March 2016 and an upside potential of 19%.

#### P/BV (Forward)





**PROFIT & LOSS STATEMENT:**

Particulars (Rs Cr)	FY14	FY15	FY16E	FY17E
Interest Earned	6,946	7,419	8,179	9,192
Interest expended	4,717	5,039	5,490	6,120
Net Interest Income	2,229	2,380	2,689	3,072
Other Income	694	878	966	1,130
NII+ Other Inc.	2,922	3,259	3,656	4,202
Employees Cost	772	892	997	1,102
Other Expenses	671	739	867	958
PPOP*	1,480	1,628	1,791	2,143
Provisions	268	107	354	348
PBT	1,212	1,521	1,437	1,795
Provision for Tax	373	515	497	621
PAT	839	1,006	940	1,174

Source: Company, Dimensional Securities

**BALANCE SHEET STATEMENT:**

Particulars (Rs Cr)	FY14	FY15	FY16E	FY17E
Sources of Funds :				
Capital	342	343	343	343
Reserves	6,608	7,395	8,095	8,968
Deposits	59,731	70,825	81,449	95,295
Borrowings	5,688	2,308	3,539	4,176
Other Liabilities	2,224	1,979	2,333	2,681
<b>TOTAL LIABILITIES</b>	<b>74,594</b>	<b>82,850</b>	<b>95,758</b>	<b>111,463</b>
Application of Funds :				
Cash & Bank Balances	4,529	4,780	5,931	6,634
Investments	24,118	24,409	28,071	32,000
Advances	43,436	51,285	58,978	69,594
Fixed Assets	425	467	556	647
Other Assets	2,086	1,910	2,223	2,588
<b>TOTAL ASSETS</b>	<b>74,594</b>	<b>82,850</b>	<b>95,758</b>	<b>111,463</b>

Source: Company, Dimensional Securities

**RATIO Analysis:**

Particulars	FY14	FY15	FY16E	FY17E
Spread Analysis				
Yield on Earning Assets	9.9%	9.8%	9.5%	9.2%
Cost of Funds	7.1%	7.1%	6.8%	6.5%
Net Interest Margin	3.2%	3.1%	3.1%	3.1%
Profitability Ratio				
RoE, %	12.6%	13.7%	11.6%	13.2%
RoA, %	1.2%	1.3%	1.1%	1.1%
Interest Expense/ Interest Income	67.9%	67.9%	67.1%	66.6%
Non-Interest Income/ Total Income	23.7%	27.0%	26.4%	26.9%
Efficiency Ratio				
Cost/Income	49.3%	50.0%	51.0%	49.0%
Employee Cost/ Operating Expenses	53.5%	54.7%	53.5%	53.5%
Asset Liability Ratio				
Credit/Deposit	72.7%	72.4%	72.4%	73.0%
CASA/Deposit	30.8%	30.4%	30.3%	30.3%
Investment/ Deposits	40.4%	34.5%	34.5%	33.6%
Valuation Ratio				
Book Value, Rs.	40.6	45.2	49.2	54.3
EPS, Rs.	4.9	5.9	5.5	6.9
Dividend, Rs.	1.0	1.1	1.2	1.5
P/BV(x)	1.2	1.5	1.4	1.3
P/E(x)	9.7	11.2	12.7	10.2

Source: Company, Dimensional Securities



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