



Federal Bank Q2 FY16 Quarterly Update

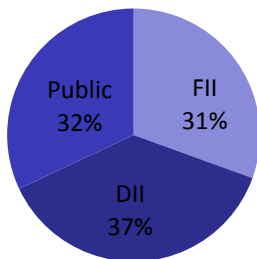
MARKET DATA

Networth (Rs. Crs)	8,245
P/BV Ratio (FY16E) (x)	1.1
EPS (FY16E) (Rs.)	5.5
Market Price (Rs.)	54
P/E Ratio (FY16E) (x)	12.5
52 Week High(3/7/2015)(Rs)	80
52 Week Low (2/11/2015)(Rs)	52
Market Capitalisation (Rs. crs)	9,528

AVERAGE MONTHLY VOLUME ('000)

BSE	601
NSE	5,680

SHARE HOLDING PATTERN



RETURN	3M	6M	12M
Federal Bank	-7%	-19%	-21%
Sensex	-1%	-6%	-9%

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In Q2 FY16, Federal Bank reported moderate loan growth (3% q-o-q); increase in GNPA 2.9% (31bps q-o-q); stable NIMs (3.11% vs 3.12% q-o-q) and a healthy CASA ratio (32% vs 31% q-o-q). Increase in opex cost by 5% q-o-q (16% y-o-y) and decrease in provisions by 43% q-o-q (67% y-o-y) resulted in an increase in PAT by 14% q-o-q (down 33% y-o-y) to Rs. 161 crs.

■ Loan book grew q-o-q; guidance remains strong

Gross advances grew by 3% q-o-q (5% y-o-y) to Rs. 51,677 crs led by growth of SME book by 7% q-o-q (17% y-o-y). Also, Retail book grew by 2% q-o-q (6% y-o-y); corporate book grew by 1% q-o-q (down 5% y-o-y) and agri book's growth was flat q-o-q (up 7% y-o-y). Credit book is well diversified with Retail, SME, Agri & Corporate exposure of 32%, 27%, 12% and 30% respectively. Gold loan book continues to drag the retail book as it de-grew by 11% q-o-q (28% y-o-y) whereas mortgage & housing grew by 9% & 4% q-o-q (33% & 16% y-o-y) respectively. We expect corporate book growth to pick up with a sanctioned pipeline of Rs. 3,000 crs and an appointment of a new Executive Director, with special focus on corporate loans.

■ Stable NIMs; Increase in Cost to Income ratio

NIMs declined by 1bp q-o-q (24bps y-o-y) to 3.11%. We believe the new RBI regulations (marginal cost of funds) and the banks focus on low yielding corporate deposits would lower the NIMs going forward. Management guided for 3.15% NIMs for FY16. In Q2 FY16, CASA ratio improved by 64bps q-o-q (134bps y-o-y) to 31.9%. Opex to loan book grew by 9bps q-o-q (34 bps y-o-y) to 3.57%. Cost to income ratio increased by 339bps q-o-q (853 bps y-o-y) to 57.42. Other income de-grew by 6% q-o-q (7% y-o-y). Also, fee income including forex grew by 1% q-o-q (8% y-o-y).

■ Asset quality negatively surprised led by corporate & SME account

Fresh slippages were at Rs. 405crs (Rs. 317crs in Q1 FY16; Rs. 176crs in Q2 FY15) led by ~Rs. 174 crs from the corporate segment and ~Rs. 155crs from the SME segment. GNPA % increased by 31bps q-o-q (80bps y-o-y) to 2.9% and in absolute terms increased by 15% q-o-q (45% y-o-y). We draw comfort with PCR at 76.6% providing cushion to credit cost, though declined by 395bps q-o-q (855bps y-o-y), as NNPA % increased by 32bps q-o-q (64bps y-o-y). Fresh restructuring stood at Rs. 80 lacs and outstanding restructured standard loan portfolio stood at Rs. 2,445crs (4.8% of overall loans). Out of the total slippages Rs. 120crs are from the restructured accounts, Rs. 102crs from corporates and Rs. 18crs from SME.

■ Valuation

At CMP of Rs.54, Federal Bank is trading at P/B multiple of 1.1x its FY16E BV of Rs.48 and 1.0x its FY17E BV of Rs.53. We maintain BUY rating with a target price Rs. 68 (1.4x FY17E Adj.BV of Rs.49 after providing for 70% provisioning shortfall on GNPA & 50% on restructured assets excluding assets from SEB & Aviation sector).

Quarterly Performance:

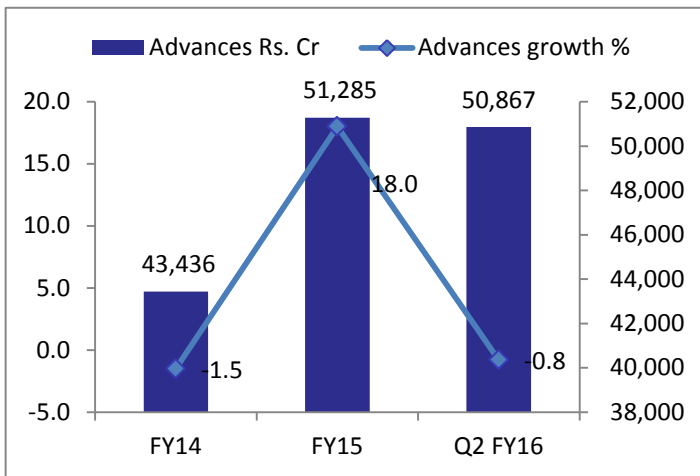
Particulars Rs. Cr	Q2 FY16	Q2 FY15	% y-o-y	Q1 FY16	% q-o-q	FY15	FY14	% y-o-y
Net Interest Income	608	606	0%	605	1%	2,380	2,229	7%
Other Income	182	196	-7%	194	-6%	878	694	27%
Total Income	791	802	-1%	799	-1%	3,259	2,923	12%
Operating Expenses	454	392	16%	431	5%	1,631	1,442	13%
PPOP*	337	410	-18%	367	-8%	1,628	1,481	10%
Total Provisions	87	46	91%	153	-43%	107	268	-60%
PBT	249	364	-31%	214	16%	1,521	1,212	25%
Taxes	88	124	-29%	73	21%	515	373	38%
PAT	161	240	-33%	141	14%	1,006	839	20%

*PPOP – Pre Provisioning Operating Profit

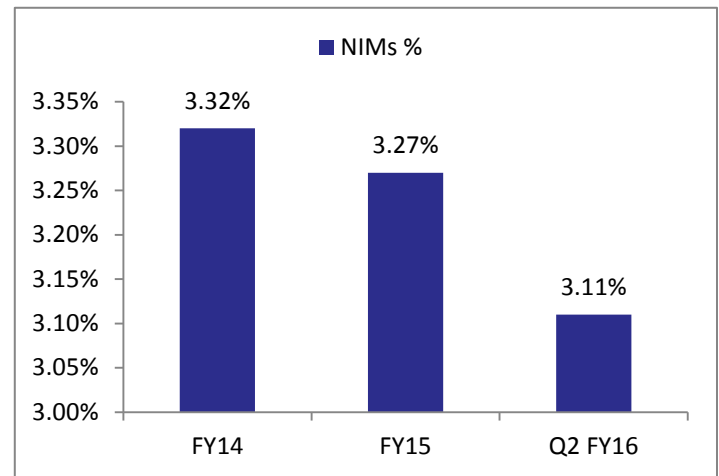


Graphs for important parameters

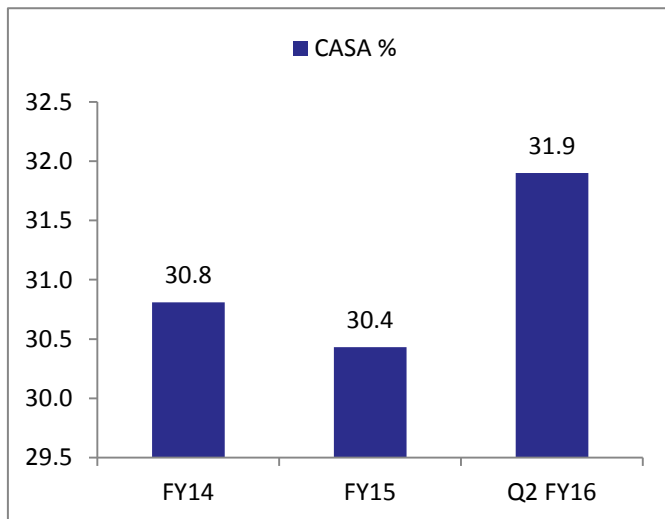
Steady improvement in loan book



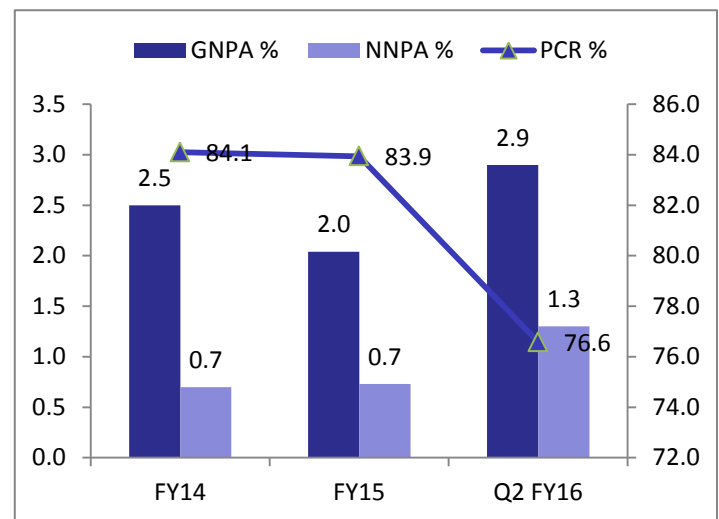
NIMs declined due to pressure on yields



Improving CASA Ratio



Asset Quality deteriorated



Q2 FY16 CONFERENCE CALL HIGHLIGHTS: -

- SME book is mostly collateralised and is expected to improve going forward. Focus would be largely on the recovery front.
- Bank has sold one shipping account (standard asset) in Q3FY15 of Rs. 140 crs. Of the sale ~80% will be in form of SRs and balance in cash. The impact of loss on sale of assets will be ~ Rs. 25 crs which will be amortized across 8 quarters.
- Fresh restructuring for the quarter was Rs. 0.8 crs. No restructuring pipeline in place. 5:25 scheme was not used during the quarter.
- Of the total ~ Rs. 2,445 crs of standard restructured, ~ Rs. 900 crs is from SEBs, Rs. 273 crs from aviation (Air India), Rs. 430 crs from Iron & Steel sector.
- NRE deposits – Rs. 27,217 crs; NRE savings – Rs. 8,142 crs; NRO – Rs. 988crs.
- Exposure of corporate book towards power sector (10%), basic metals (8%) of the overall corporate portfolio.



QUARTERLY PERFORMANCE:

Particulars (amt in crs)	Sept-15	Sept-14	% y-o-y	Jun-15	% q-o-q	FY15	FY14	% y-o-y
Interest Income	1,902	1,870	2%	1,913	-1%	7,420	6,946	7%
Interest Expenses	1,294	1,264	2%	1,308	-1%	5,039	4,718	7%
Net Interest Income	608	606	0%	605	1%	2,380	2,229	7%
Other Income	182	196	-7%	194	-6%	878	694	27%
Fee Income (including Forex)	137	136	1%	127	8%	523	465	12%
Total Income	791	802	-1%	799	-1%	3,259	2,923	12%
Operating Expenses	454	392	16%	431	5%	1,631	1,442	13%
Employee	249	204	22%	252	-1%	892	772	16%
Others	205	188	9%	179	14%	739	671	10%
Operating Profits before provisions	337	410	-18%	367	-8%	1,628	1,481	10%
Exceptional Items	-	-	-	-	-	-	-	-
Total Provisions	87	46	91%	153	-43%	107	268	-60%
PBT	249	364	-31%	214	16%	1,521	1,212	25%
Taxes	88	124	-29%	73	21%	515	373	38%
PAT	161	240	-33%	141	14%	1,006	839	20%
EPS	0.9	2.8	-67%	1.7	-43%	12	5	139%
Asset Quality								
GNPA Rs. crs	1,499	1,031	45%	1,305	15%	1,058	1,087	-3%
NNPA Rs. crs	675	319	112%	484	39%	373	322	16%
GNPA %	2.9	2.1	80	2.59	31	2.04	2.50	-46
NNPA %	1.3	0.7	64	0.98	32	0.73	0.7	3
PCR % Calculated	54.97	69.11	-1413	62.86	-789	64.71	70.42	-572
PCR % Reported	76.58	85.13	-855	80.53	-395	83.94	84.1	-16
Slippages	405	176	130%	317	28%	773	795	-3%
Slippage Ratio %	3.18	1.45	173	2.56	63	1.51	1.83	-32
Restructured Assets	2,445	2,456	0%	2,583	-5%	-	-	-
Credit Cost %	0.69	0.38	31	1.24	-55	0.21	0.62	-41
Ratios %								
Fees to Advances	1.08	1.12	-5	1.03	5	1.02	1.07	-5
Cost to Income ratio	57.42	48.89	853	54.02	339	50.05	49.34	71
Tax Rate	35.28	33.99	129	33.96	132	33.88	30.78	310
CASA %	31.9	30.56	134	31.26	64	30.43	30.8	-37
RoA %	0.78	1.26	-48	0.7	8	1.32	1.2	12
RoE %	8.09	13.18	-509	7.25	84	13.75	12.8	95
CAR (Basel III) %	14.71	14.45	26	15.07	-36	15.46	15.14	32
Tier I %	14.06	13.85	21	14.4	-34	14.81	14.59	22
Opex to Loan book	3.57	3.23	34	3.48	9	3.18	3.32	-14
Quarterly NIMs	3.11	3.35	-24	3.12	-1	3.27	3.3	-3
Balance sheet								
Capital	344	171	101%	171	100%	171	342	-50%
Net Worth	8,058	7,411	9%	7,889	2%	7,758	6,951	12%
FV	2	2	2	2	2	2	2	2
Deposits	73,783	64,564	14%	72,140	2%	70,825	59,731	19%
Investments	23,199	22,712	2%	27,041	-14%	24,409	24,118	1%
Loans	50,867	48,466	5%	49,552	3%	51,285	43,436	18%
BV-Calculated	47	87	-46%	92	-49%	91	41	123%
Adj. Network	7,383	7,092	4%	7,405	0%	7,385	6,629	11%
Adj. BV	43	83	-48%	86	-50%	86	39	123%

* Adj. Network = Reported Network – NNPA

Source: Company, Dimensional Securities



ROA TREE:

Particulars	Sep-15	Jun-15	Mar-15	Dec-14	Sep-14	FY15	FY14
Interest Income	9.2%	9.6%	9.7%	9.7%	10.0%	9.4%	9.5%
Interest Expenses	6.3%	6.5%	6.5%	6.7%	6.8%	6.4%	6.5%
Net Interest Income	3.0%	3.0%	3.2%	3.1%	3.2%	3.0%	3.1%
Other Income	0.9%	1.0%	1.6%	1.1%	1.0%	1.1%	1.0%
Fee Income	0.7%	0.6%	0.7%	0.6%	0.7%	0.6%	0.6%
Total Income	3.8%	4.0%	4.7%	4.2%	4.3%	4.1%	4.0%
Operating Expenses	2.2%	2.2%	2.3%	2.1%	2.1%	2.1%	2.0%
Employee	1.2%	1.3%	1.3%	1.2%	1.1%	1.1%	1.1%
Others	1.0%	0.9%	1.1%	0.9%	1.0%	0.9%	0.9%
Operating Profits before provisions	1.6%	1.8%	2.4%	2.1%	2.2%	2.1%	2.0%
Total Provisions	0.4%	0.8%	0.2%	0.0%	0.2%	0.1%	0.4%
PBT	1.2%	1.1%	2.2%	2.1%	1.9%	1.9%	1.7%
Taxes	0.4%	0.4%	0.8%	0.7%	0.7%	0.7%	0.5%
PAT (RoA)	0.8%	0.7%	1.4%	1.4%	1.3%	1.3%	1.2%
Average Assets/Average Equity	10.64	10.64	10.70	10.57	10.61	10.70	10.94
RoE	8.3%	7.5%	15.3%	14.6%	13.6%	13.7%	12.6%

Source: Company, Dimensional Securities

CHANGE IN ESTIMATE:

	FY16					
	Revised	Old	Change (%)	Revised	Old	Change (%)
Loan Book	56,413	58,978	-4%	64,876	69,594	-7%
NII	2,674	2,689	-1%	3,030	3,072	-1%
PAT	797	940	-15%	1,027	1,174	-13%



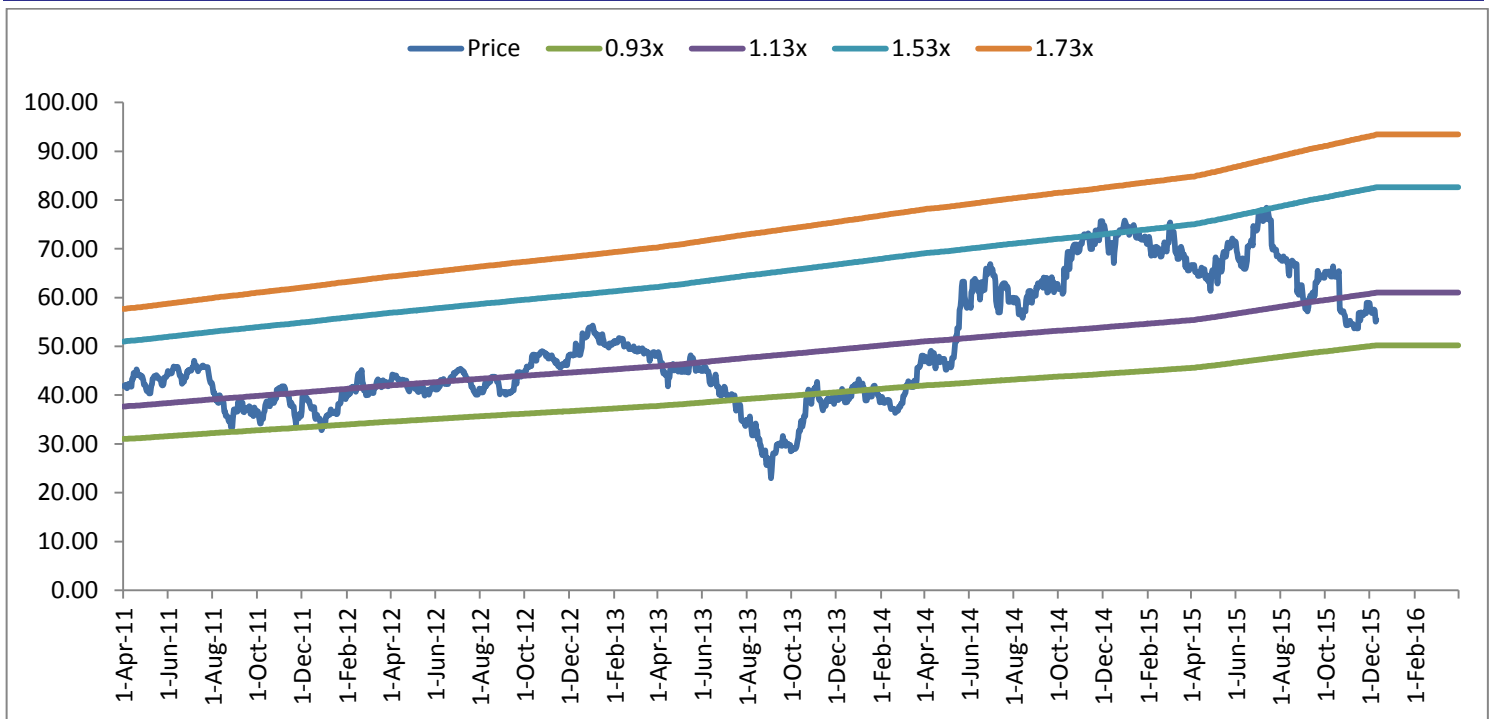
OUTLOOK & VALUATION: -

Federal bank negatively surprised on asset quality front with higher slippages from corporate & SME accounts. However, PCR at 77% provides cushion to credit cost going ahead. Also, Tier I ratio at 14.06% should support high growth going forward as the opportunity arises with improvement in the economic activity.

We expect loan book to grow at 13% CAGR (FY15-17E) with RoA and RoE to improve towards 1% and 12% by FY17E.

At CMP of Rs.54, Federal Bank is trading at P/B multiple of 1.1x its FY16E BV of Rs.48 and 1.0x its FY17E BV of Rs.53. We maintain BUY rating with a target price Rs. 68 (1.4x FY17E Adj.BV of Rs.49 after providing for 70% provisioning shortfall on GNPA & 50% on restructured assets excluding assets from SEB & Aviation sector).

P/BV (Forward)



Source: Company, Dimensional Securities



PROFIT & LOSS STATEMENT:

Particulars (Rs Cr)	FY14	FY15	FY16E	FY17E
Interest Earned	6,946	7,419	8,160	9,137
Interest expended	4,717	5,039	5,486	6,107
Net Interest Income	2,229	2,380	2,674	3,030
Other Income	694	878	834	918
NII+ Other Inc.	2,922	3,259	3,508	3,948
Employees Cost	772	892	1,032	1,098
Other Expenses	671	739	862	955
PPOP*	1,480	1,628	1,614	1,895
Provisions	268	107	395	324
PBT	1,212	1,521	1,219	1,570
Provision for Tax	373	515	422	543
PAT	839	1,006	797	1,027

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	7,952	8,678
Deposits	59,731	70,825	81,449	95,295
Borrowings	5,688	2,308	3,385	3,893
Other Liabilities	2,224	1,979	2,374	2,698
TOTAL LIABILITIES	74,594	82,850	95,502	110,907
Application of Funds :				
Cash & Bank Balances	4,529	4,780	9,473	12,211
Investments	24,118	24,409	26,850	30,609
Advances	43,436	51,285	56,413	64,876
Fixed Assets	425	467	553	642
Other Assets	2,086	1,910	2,213	2,569
TOTAL ASSETS	74,594	82,850	95,502	110,907

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%	3.0%
Profitability Ratio				
RoE, %	12.6%	13.7%	9.9%	11.9%
RoA, %	1.2%	1.3%	0.9%	1.0%
Interest Expense/ Interest Income	67.9%	67.9%	67.2%	66.8%
Non-Interest Income/ Total Income	23.7%	27.0%	23.8%	23.3%
Efficiency Ratio				
Cost/Income	49.3%	50.0%	54.0%	52.0%
Employee Cost/ Operating Expenses	53.5%	54.7%	54.5%	53.5%
Asset Liability Ratio				
Credit/Deposit	72.7%	72.4%	69.3%	68.1%
CASA/Deposit	30.8%	30.4%	30.3%	30.3%
Investment/ Deposits	40.4%	34.5%	33.0%	32.1%
Asset Quality				
GNPA (%)	2.49	2.05	2.70	2.60
NNPA (%)	0.74	0.73	0.96	1.00
Valuation Ratio				
Book Value, Rs.	40.6	45.2	48.4	52.7
EPS, Rs.	4.9	5.9	4.7	6.0
Dividend, Rs.	1.0	1.1	1.2	1.5
P/BV(x)	1.2	1.5	1.1	1.0
P/E(x)	9.7	11.2	11.7	9.1

Source: Company, Dimensional Securities



ANALYST CERTIFICATION

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