

FEDERAL BANK

BANKING

Q3FY17: Strong loan book growth continues with stable asset quality

Federal Bank (FB) reported strong earnings at Rs 206 cr which grew by 26% YoY (up 2% QoQ). These strong earnings were mainly on account of strong loan growth and improvement in margins. Loan growth improved to 32% YoY (8% QoQ) from 27% in Q2FY17 on the back of increase in corporate loan (up 53% YoY) and Retail +Agri loan book (up 23% YoY). With a new corporate banking team, the bank's presence in GIFT city, targeted corporate coverage and focused and effective digital and digitization strategy underway, management guided for strong momentum to continue in quarters ahead.

Outlook

We expect advance growth to improve to 20% (earlier 17%) for FY17E led by growth in Corporate, SME and Retail portfolio. Going forward, management's focus would be on containing slippages from its corporate book, reduce its cost of borrowing and also increase lending towards retail and SME. Management have identified and addressed all stressed accounts and guided for few restructured accounts of Rs.257 cr under watch list. We value FB at FY18E P/ABV multiple of 1.9x to arrive at target price of Rs 96/share and retain **BUY** rating on the stock.

BUY

Target Price: Rs 96

 CMP : Rs 78
 Potential Upside : 23%

MARKET DATA

No. of Shares	: 172.2cr
FV (Rs)	: 2
Market Cap	: Rs 12,860 cr
52-week High / Low	: Rs 86 / Rs 41
Avg. Daily vol. (6mth)	: 34,15,928 shares
Bloomberg Code	: FB IN
Reuters Code	: FED.BO
BSE Code	: 500469
NSE Code	: FEDERAL BNK

Key Highlights

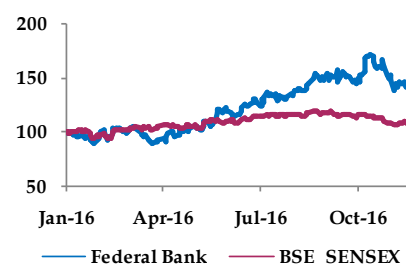
- **Stable asset quality:** Bank's slippage ratio declined from 2.1% in Q2FY17 to 1.6% in Q3FY17 led by slippage of Rs 55 cr (42 cr in Q2 FY17) in corporate accounts and Rs. 119 cr (135 cr in Q2 FY17) from SME accounts. GNPA ratio remained flat at 2.77% vs 2.78% in Q2FY17 due to lower write offs. In bank's restructured book one account of Rs 200 cr came out of moratorium in Q2FY17 but may show stress in future. Management expects credit cost to remain stable at H1 FY17 level of 70-75bps in FY17.
- **CASA ratio improved led by demonetization:** Deposit growth strong at 23% YoY led by higher CASA growth (33% YoY) due to demonetization. Bank's overall CASA growth was healthy at ~33% YoY and CASA ratio increased by 257bp YoY and 362bps QoQ to 34.66% due to high savings growth. Management expects 1/3rd of the incremental CASA flow to remain sticky.
- **Credit growth picks up further:** FB's advances during the quarter grew by 32% YoY (vs 27% in Q2 FY17) led by traction in Corporate, SME and Retail (incl. Agri) loan book which was up by 53%,16%, 23% YoY respectively. The management has guided that in FY17 its strong loan book growth to continue. We expect loan CAGR of 18% over FY15-18E.
- **NIMs improved YoY:** FB's Q3FY17 NIM stood at 3.32% (up 1bp QoQ & up 28bps YoY). Risk-adjusted NIMs clocked in at 2.88% up 1bp QoQ as it has benefited from having calibrated its loan mix towards better-rated large and SME corporates. Management maintained the NIMs guidance to be in the range of 3.25-3.30%.

FINANCIAL SUMMARY

Y/E	NII	PAT	EPS	EPS	BVPS	P/E	P/BV	Net	Adj BV	P/Adj.BV	RoE	RoA
Mar	(Rs Cr)	(Rs. Cr)	(Rs.)	Change	(Rs)	(x)	(x)	NPA (%)	(Rs.)	(x)	(%)	(%)
FY15	2380.4	1005.8	5.9	0.0	45.2	13.9	1.8	0.7	43.2	1.9	13.7	1.3
FY16	2504.2	475.7	2.8	-53%	47.8	29.5	1.7	1.1	41.5	2.0	6.1	0.5
FY17E	2785.6	791.7	4.6	66%	50.4	17.8	1.6	1.1	45.8	1.8	8.7	0.8
FY18E	3408.8	994.7	5.8	26%	54.8	14.1	1.5	1.0	49.5	1.7	9.7	0.9

Source: Company and Axis Securities

PRICE PERFORMANCE


 Bunty Chawla
bunty.chawla@axissecurities.in

Results Update

Federal Bank	Quarterly					Yearly				
	Fig in Rs. Cr	Q3FY17	Q3FY16	Y-o-Y Ch (%)	Q2FY17	Q-o-Q Ch (%)	FY15	FY16E	FY17E	FY18E
Interest income	2281.4	1902.8	19.9	2066.3	10.4	7419.5	7744.7	8678.8	10237.1	15.0
Interest expended	1490.0	1297.6	14.8	1340.1	11.2	5039.1	5240.5	5893.2	6828.3	14.1
Net interest income	791.4	605.2	30.8	726.2	9.0	2380.4	2504.2	2785.6	3408.8	16.7
NII as a % of Net income	75.0	76.8	-2.2	73.5	2.1	73.0	76.1	77.1	79.7	2.4
Other income	263.3	183.3	43.7	261.5	0.7	878.3	786.4	825.7	867.0	5.0
Total income	2544.8	2086.1	22.0	2327.8	9.3	8297.8	8531.1	9504.5	11104.1	14.1
Net total income (3+4)	1054.7	788.5	33.8	987.7	6.8	3258.7	3290.6	3611.3	4275.8	14.0
Operating expenses	579.8	463.0	25.2	512.8	13.1	1630.9	1866.8	1877.9	2137.9	7.0
Personnel exp	319.7	258.6	23.6	291.6	9.6	892.0	1052.9	1070.4	1175.8	5.7
Other exp	260.1	204.4	27.2	221.2	17.6	739.0	814.0	807.5	962.1	8.7
Profit before tax & prov.	474.9	325.5	45.9	474.9	0.0	1627.8	1423.8	1733.4	2137.9	22.5
Provisions & contingencies	158.8	75.1	111.4	168.4	-5.7	106.8	704.1	522.8	616.9	-6.4
PBT	316.1	250.4	26.2	306.5	3.1	1521.0	719.7	1210.6	1521.0	45.4
Tax	110.4	87.7	26.0	105.3	4.9	515.3	244.0	418.9	526.3	46.9
Tax as % of PBT	34.9	35.0	-0.2	34.3	1.7	33.9	33.9	34.6	34.6	1.0
Profit after tax	205.7	162.7	26.4	201.2	2.2	1005.8	475.7	791.7	994.7	44.6
Extra ordinary Item	0.0	0.0		0.0		0.0	0.0	0.0	0.0	#DIV/0!
Reported PAT	205.7	162.7	26.4	201.2	2.2	1005.8	475.7	791.7	994.7	44.6
Equity	344.4	343.7		344.1		171.0	343.7	343.7	343.7	0.0
Cap. adequacy ratio (Basel-II)	12.28	14.32	-	12.85	-	15.46	13.93	13.80	13.10	-
EPS (Rs)	1.2	3.8	-68.9	1.2	2.6	5.8	2.8	4.6	5.8	45.2
BVPS (Rs)	49.9	47.9	4.3	48.6	2.7	45.2	47.8	50.4	54.8	7.1
NIMs (%)	3.32	3.04	-	3.31	-	3.1	2.9	3.0	3.1	-
CASA (%)	34.66	32.10	-	31.04	-	30.4	32.2	33.7	34.7	-
RoE (%)	9.62	8.00	-	9.78	-	13.7	8.6	9.5	11.0	-
RoA (%)	0.78	0.77	-	0.88	-	1.4	0.8	0.8	0.9	-
Gross NPA (%)	2.77	3.15	-	2.78	-	2.0	3.1	2.9	2.7	-
Net NPA (%)	1.58	1.66	-	1.61	-	0.7	1.1	1.1	1.0	-
Provisional Coverage (%)	71.0	71.7	-	71.70	-	83.9	77.4	70.2	70.0	-
Credit cost (%)	0.64	0.30	-	0.65	-	0.2	1.2	0.8	0.7	-
NII/ Operating expenses	1.4	1.3	-	1.4	-	1.6	1.3	1.5	1.6	-

Source: Company and Axis Securities

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Ratings	Expected absolute returns over 12-18 months
BUY	More than 10%
HOLD	Between 10% and -10%
SELL	Less than -10%

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