

INDUSTRY	BANKS
CMP (as on 20 Sep 2013)	Rs 305
Target Price	Rs 409
Nifty	6,012
Sensex	20,264

KEY STOCK DATA	
Bloomberg/Reuters	FB IN/FED.BO
No. of Shares (mn)	171
MCap (Rs bn) / (\$ mn)	52 / 838
6m avg traded value (Rs mn)	225

STOCK PERFORMANCE (%)			
52 Week high / low	Rs 571 / 221		
	3M	6M	12M
Absolute (%)	(26.6)	(36.7)	(31.6)
Relative (%)	(34.6)	(44.9)	(39.7)

SHAREHOLDING PATTERN (%)	
Promoters	-
FIs & Local MFs	20.80
FIIIs	44.42
Public & Others	34.78

Source : BSE

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Concerns persist, priced in

Federal Bank (FB) corrected 28% in the last 3 months on increasingly tough macro environment. We met Shyam Srinivasan, MD & CEO, recently. Key takeaways are (a) Large corp assets of Rs 3-4bn remain under stress, while slippages in retail and SME segment are under check. Restructured assets additions can be ~Rs 2bn in 2QFY14 (b) Loan growth in retail and SME is strong (c) NIMs guidance for FY14 was kept at 3.20-3.25% (d) MTM losses of Rs 200-400mn foreseeable in 2QFY14. Our earnings estimates fall by ~11/9% for FY14/15E given marginal NIM compression, lower growth and higher slippages, credit cost. Maintain BUY with a revised TP of Rs 409 (1x FY15E ABV) vs. Rs 506 (1.2x FY15E ABV) earlier.

- **Stress in corp segment** : FB maintained that its corporate book contains stressed assets of Rs 3-4bn (in 7-8 accounts). On a positive note, management guided for controlled slippages in the retail and SME segments. **We have revised our slippages estimates to 2.2% for FY14/15E vs. 2%**. Restructuring is expected at Rs 2bn, during 2QFY14. As at Jun-13, restructured book stood at Rs 19.6bn (SEB and AI : ~Rs 10bn).
- **Retail, SME segments drive loan growth** : FB continues to witness strong growth of ~22-25% in the retail and SME segments. Large corp segment is expected to report muted QoQ growth. FB expects CASA to touch 30%+ in 2QFY14 (vs. 29% in 1QFY14), with strong growth in SB (especially NR). Retail deposits are expected to improve to ~93% of total deposits (vs. 89% in 1QFY14).

- **NIMs to be stable** : Management maintained its NIM guidance of 3.20-3.25% for FY14 with better traction in retail business, CASA improvement and lower interest reversals. For 2QFY14, management maintained NIMs guidance at 8-10bps improvement to 3.2%+. We have factored in NIMs of 3.1% (3.2% earlier) for FY14/15E.
- **MTM hit on investment book** : FB expects MTM hit of Rs 200-400mn for 2QFY14. FB's AFS book stood at Rs 30bn with duration of ~2years. It is insulated upto yields of 7.70%.
- **Other highlights** : Fee income growth target was maintained at ~20% for FY14. Wage provisions of Rs 100mn (vs. Rs 80-100mn in 1QFY14) expected in 2QFY14. C/I ratio to stabilize at 42-44%. Target RoA by FY15 : 1.3%.
- **Despite the slips on asset quality, FB's calibrated growth approach, high CRAR, superior PCR of ~83% and attractive valuations make us positive on the stock. At CMP, FB trades at 0.75x FY15E ABV. Maintain BUY.**

FINANCIAL SUMMARY

YE Mar (Rs mn)	FY12	FY13	FY14E	FY15E
Net interest income	19,534	19,747	22,063	25,195
PPP	15,065	14,596	15,988	17,725
PAT	7,768	8,382	7,164	8,961
EPS	45.4	49.0	41.9	52.4
EPS growth (%)	32.3	7.9	(14.5)	25.1
RoAE (%)	14.4	13.9	10.8	12.3
RoAA	1.39	1.27	0.94	1.03
Adj BV	321.3	346.2	373.1	409.1
P/E (x)	6.7	6.2	7.3	5.8
P / Adj BV	0.95	0.88	0.82	0.75

Source: Company, HDFC sec Inst Research

CHANGE IN ESTIMATES

(Rs mn)	FY14E			FY15E		
	Old	New	Change	Old	New	Change
NII	23,012	22,063	-4.1%	26,276	25,195	-4.1%
PPOP	16,855	15,988	-5.1%	18,397	17,725	-3.6%
PAT	8,027	7,164	-10.7%	9,859	8,961	-9.1%
Adj. BVPS (Rs)	381	373.1	-2.0%	422.2	409.1	-3.1%

Source : HDFC sec Inst Research

INCOME STATEMENT

(Rs mn)	FY11	FY12	FY13	FY14E	FY15E
Interest Earned	40,520	55,584	61,676	71,490	81,156
Interest Expended	23,054	36,050	41,929	49,427	55,960
Net Interest Income	17,466	19,534	19,747	22,063	25,195
Other Income	5,168	5,323	6,644	7,387	7,755
<i>Fee Income (CEB)</i>	<i>1,144</i>	<i>2,516</i>	<i>3,047</i>	<i>3,550</i>	<i>4,177</i>
<i>Treasury Income</i>	<i>458</i>	<i>821</i>	<i>2,058</i>	<i>2,000</i>	<i>1,450</i>
Total Income	22,634	24,857	26,391	29,450	32,951
Total Operating Exp	8,361	9,793	11,795	13,462	15,225
<i>Employee Expense</i>	<i>4,804</i>	<i>5,439</i>	<i>6,265</i>	<i>7,227</i>	<i>8,361</i>
PPOP	14,273	15,065	14,596	15,988	17,725
Provisions & Contingencies	5,254	3,370	2,658	5,753	4,924
<i>Prov. for NPAs (incl. std prov.)</i>	<i>5,032</i>	<i>2,582</i>	<i>2,386</i>	<i>4,774</i>	<i>5,127</i>
PBT	9,018	11,695	11,938	10,234	12,801
Provision for Tax	3,147	3,927	3,556	3,070	3,840
PAT	5,871	7,768	8,382	7,164	8,961

Source: Bank, HDFC sec Inst Research

BALANCE SHEET

(Rs mn)	FY11	FY12	FY13	FY14E	FY15E
SOURCES OF FUNDS					
Share Capital	1,710	1,710	1,711	1,711	1,711
Reserves	49,376	55,353	61,936	67,556	74,588
Shareholder's Funds	51,087	57,063	63,647	69,267	76,299
Savings	91,483	109,299	127,432	149,731	172,189
Current	24,058	25,459	29,089	32,580	35,838
Term Deposit	314,607	354,613	419,627	482,571	559,783
Total Deposits	430,148	489,371	576,149	664,882	767,810
Borrowings	18,884	42,410	51,870	58,735	66,569
Other Liabilities & Provisions	14,446	17,423	18,831	19,692	20,594
Total Liabilities	514,564	606,268	710,496	812,576	931,271
APPLICATION OF FUNDS					
Cash & Bank Balance	37,483	35,326	37,200	37,968	44,150
Investments	145,377	174,025	211,546	245,998	276,660
<i>G-Secs</i>	<i>99,645</i>	<i>115,312</i>	<i>145,751</i>	<i>176,194</i>	<i>201,550</i>
Advances	319,532	377,560	440,967	507,112	588,250
Fixed Assets	2,898	3,261	3,975	4,139	4,279
Other Assets	9,273	16,096	16,808	17,359	17,932
Total Assets	514,564	606,268	710,496	812,576	931,271

Source: Bank, HDFC sec Inst Research

KEY RATIOS

	FY11	FY12	FY13	FY14E	FY15E
Valuation Ratios					
EPS	34.3	45.4	49.0	41.9	52.4
Earnings Growth (%)	26.4	32.3	7.9	(14.5)	25.1
BVPS (ex reval.)	298.3	333.3	371.8	404.6	445.7
Adj. BVPS (ex reval. & 100% cover)	286.9	321.3	346.2	373.1	409.1
ROAA (%)	1.2	1.4	1.3	0.94	1.03
ROAE (%)	12.0	14.4	13.9	10.8	12.3
ROAE (%) (ex revaluations)	12.0	14.4	13.9	10.8	12.3
P/E (x)	8.9	6.7	6.2	7.3	5.8
P/ABV (x)	1.1	0.95	0.88	0.82	0.75
P/PPOP (x)	3.7	3.5	3.6	3.3	2.9
Dividend Yield (%)	2.8	3.0	3.0	2.6	3.3
Profitability					
Yield on Advances (%)	10.8	12.0	11.3	11.3	11.1
Yield on Investment (%)	6.3	8.2	7.6	7.6	7.6
Cost of Funds (%)	5.6	7.4	7.2	7.3	7.2
Cost of Deposits (%)	5.5	7.2	7.2	7.3	7.2
Core Spread (%)	5.2	4.7	4.1	4.0	3.9
NIM (%)	4.0	3.8	3.2	3.1	3.1
Operating Efficiency					
Cost/Avg. Asset Ratio (%)	1.8	1.7	1.8	1.8	1.7
Cost-Income Ratio (Excl Treasury)	37.7	40.7	48.5	49.0	48.3
Balance Sheet Structure Ratios					
Loan Growth (%)	18.6	18.2	16.8	15.0	16.0
Deposit Growth (%)	19.3	13.8	17.7	15.4	15.5
C/D Ratio (%)	74.3	77.2	76.5	76.3	76.6
Equity/Assets (%)	9.9	9.4	9.0	8.5	8.2
Equity/Loans (%)	16.0	15.1	14.4	13.7	13.0
CASA (%)	26.9	27.5	27.2	27.4	27.1
Total Capital Adequacy Ratio (CAR)	16.8	16.6	14.7	14.5	13.9
Tier I CAR	15.6	15.9	14.1	13.8	13.3

	FY11	FY12	FY13	FY14E	FY15E
Asset Quality					
Gross NPLs (Rsm)	11,483	13,008	15,540	18,110	20,638
Net NPLs (Rsm)	1,907	1,990	4,319	5,333	6,212
Gross NPLs (%)	3.5	3.4	3.4	3.6	3.5
Net NPLs (%)	0.6	0.5	1.0	1.1	1.1
Coverage Ratio (%)	83.4	84.7	72.2	70.6	69.9
Provision/Avg. Loans (%)	1.7	0.64	0.46	0.96	0.88
RoAA Tree					
Net Interest Income	3.67%	3.49%	3.00%	2.90%	2.89%
Non Interest Income	1.09%	0.95%	1.01%	0.97%	0.89%
Treasury Income	0.10%	0.15%	0.31%	0.26%	0.17%
Operating Cost	1.76%	1.75%	1.79%	1.77%	1.75%
Provisions	1.10%	0.60%	0.40%	0.76%	0.56%
Provisions for NPAs	1.03%	0.40%	0.29%	0.60%	0.56%
Tax	0.66%	0.70%	0.54%	0.40%	0.44%
ROAA	1.23%	1.39%	1.27%	0.94%	1.03%
Leverage (x)	10.07	10.62	11.16	11.73	12.21
ROAE	12.43%	14.73%	14.21%	11.04%	12.54%

Source: Bank, HDFC sec Inst Research

Rating Definitions

BUY	:	Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL	:	Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL	:	Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

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