

Q3FY13-Tough quarter, yet geared for next growth level

CMP: Rs. 501
Target Price: Rs. 576
Recommendation: BUY

Stock Info

BSE Group	A
BSE Code	500469
NSE Symbol	FEDERALBNK
Bloomberg	FB IN
Reuters	FED.BO
BSE Sensex	19981.6
NSE Nifty	6048.5

Market Info

Market Capital	8508cr
Equity Capital	171cr
Avg. Trading Vol. (NSE Qtly-'000)	398
52 Wk High/ Low	551/335
Face Value	10

Shareholding Pattern (%) (31th Dec 2012)

Promoters	-
Domestic Institutions	23.4
Foreign Institutions	43.6
Public & Others	33.1

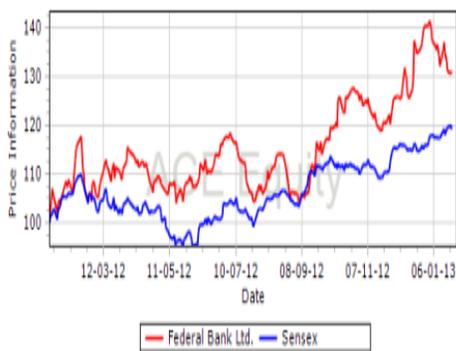
The Q3 Earnings of Federal bank, though not very impressive, were largely supported by lower credit costs and non-interest income performance. The top-line looked strained and the opex stood on the higher side. The fact that the bank is investing in people and processes and gearing up for next levels of growth, we are confident that these efforts would yield returns sooner than later.

Top-line disappoints, long term outlook positive: The bank disappointed on top-line performance with poor net interest income for the second quarter in a row that was recorded at Rs 497 crs that was down 6% YoY; largely on account of choppy corporate loan book. That said, the other income show was strong at Rs 204 crs that witnessed robust 48% growth YoY and 46% QoQ that came on account of one-off transactions wrt stake sale in CARE. Though such high momentum seems unsustainable, bank is on track to report decent core income growth going ahead.

Though YoY lower credit costs boosted profitability, sequential provisions were dramatically high with the bank providing for the painful NAFED account and provisions made for restructured assets. That said, the credit costs seem to be apparently bottomed-out and may not be a profitability dragger going ahead. Moreover, with the bank keenly investing in people and processes that are expected to yield returns in near future and de-bulking the corporate loan book and focusing on retail and SME coupled with strengthening liability franchise, we expect 20% CAGR growth in Net interest income for the bank. Margins that remained pressurized (on account of FITL provisions) are expected to settle in the range of 355bps – 360bps by year end. While the earnings also expected to deliver 20%+ CAGR, we expect the RoEs to trend in the range of 15-16% and RoAs at 1.4% for FY13-14.

NPLs inched upwards, no major concern: The quarter witnessed rise in GNPLs to Rs 1564crs from 1363crs a year ago. The slippages for the quarter stood higher due to fresh additions from corporate (couple of accounts ~Rs 100-150crs) and SME portfolio. The restructured book needs to have a closer look given the bank's exposure to SEBs and certain shaky infrastructure accounts. However, the provision cushion with coverage ratio at 75% levels provides relief.

Investment Outlook: Upturn in NR deposits, expanding retail loan portfolio (gold loan also showing up traction with in-line credit growth, improving SA traction, de-bulking of corporate loan book and), expanding footprint across pan-India makes us positive on the stock. Hence, we revise the target price upwards to Rs 576 (earlier Rs 533) valuing the bank at 1.4X P/ABV FY14E on an 8-12 month horizon. Expect mid-term jitters as the stock has already rallied, but long term stay invested.



(Rs Cr)	FY11	FY12	FY13E	FY14E
Net interest income	1747	1953	2217	2757
Operating Profit	1430	1506	1725	2188
PAT	590	776	895	1128
EPS (Rs)	34.3	45.4	52.3	66.0
RoE (%)	12.0	14.4	14.8	16.3
P/E (x)	14.1	11.0	9.6	7.6
PABV (x)	1.6	1.5	1.4	1.2

January 23, 2013

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Q3FY13 Earnings Snapshot

Particulars (Rs in Cr)	Q3FY13	Q3FY12	YoY%	Q2FY13	QoQ %	Comments
Interest Earned	1,522	1,467	3.7	1,526	-0.3	
Interest Expended	1,024	939	9.1	1,020	0.5	
Net Interest Income	497	528	-5.8	506	-1.7	NII performance disappoints
Other Income	204	138	47.8	139	46.2	Other income YoY basis showed healthy performance both YoY and QoQ basis
Total income	701	666	5.3	645	8.7	
Employee Expenses	163	138	18.1	159	2.5	
Non-Employee expenses	144	109	32.2	136	5.5	
Operating Expenses	307	247	24.3	296	3.9	YoY opex stood on the higher side with the bank investing in people and process
Cost-income Ratio (%)	44	37		46		As a result, C/I ratio stood on the higher side
Pre-Prov Profits	394	419	-5.9	350	12.7	
Provisions & Contingencies	74	115	-35.5	30	144.3	Credit costs moved down YoY, but increased dramatically QoQ (NAFED, restructured ac/s)
PBT	320	303	5.3	319	0.1	
Provisions for Tax	109	102	7.1	104	4.5	
Effective Tax Rate (%)	34	33		33		
PAT (reported)	211	202	4.4	215	-2.0	Bottom-line growth supported by lower credit costs and other income growth
EPS Basic	49.3	47.2		50.3		
EPS Diluted	49.3	47.2		50.3		
GNPA	1564	1363		1435		NPLs stood on the higher side, slippages in certain large corporate pockets have moved up for the quarter
NNPA	362	244		245		
GNPA (%)	3.9	4.0		3.8		GNPAs moved tad down, yet not satisfactory
NNPA (%)	0.9	0.7		0.7		NNPAs spiked up
Total CAR (%)	14.9	15.9		15.8		CAR stands at healthy levels



Income Statement				
Year to 31st March (Rs.Cr)	FY11	FY12	FY13E	FY14E
Interest Income	4052	5558	6492	7814
Interest Expenses	2305	3605	4274	5057
Net Interest Income	1747	1953	2217	2757
- growth %	24	12	14	24
Non-interest Income	520	532	643	767
Operating Income	2266	2485	2861	3524
- growth %	17	10	15	23
Operating Expenses	836	979	1136	1336
- Staff Cost	480	544	617	706
- Other Operating Exp.	356	435	519	630
Gross Profits	1430	1506	1725	2188
- growth %	13	5	15	27
Provisions	525	337	369	504
Profit Before Taxes	905	1169	1356	1684
Taxes	315	393	461	556
Profit After Taxes	590	776	895	1128
- growth %	27	32	15	26

Balance sheet				
As on 31st March (Rs. Cr)	FY11	FY12	FY13E	FY14E
LIABILITIES				
Capital	171	171	171	171
Reserves & Surplus	4,938	5,535	6,260	7,219
Deposits	43,014	48,937	57,746	68,140
- growth %	19	14	18	18
Borrowings	1,888	4,241	6,600	8,310
Other liabilities & provisions	1,445	1,742	3,235	6,066
TOTAL LIABILITIES	51,456	60,627	74,012	89,906
ASSETS				
Cash, Inter-bank, etc	2,936	2,424	4,039	4,760
Money at call and short notice	813	1,108	1,161	1,394
Advances	31,953	37,756	45,685	56,649
- growth %	19	18	21	24
Investments	14,538	17,402	20,872	24,296
Fixed assets	290	326	420	517
Other assets	926	1,610	1,835	2,290
TOTAL ASSETS	51,456	60,627	74,012	89,906

Ratio Analysis				
	FY11	FY12	FY13E	FY14E
Basic Ratio (Rs.)				
EPS	34.3	45.4	52.3	66.0
Book Value per share	298.4	333.3	375.7	431.7
70% Adjusted Book Value	307.3	341.8	366.8	409.1
Dividend per share	8.5	9.0	8.5	8.5
Asset Quality (%)				
Gross NPAs	3.6	3.4	3.8	4.0
Net NPAs	0.6	0.7	1.5	1.9
NPA Coverage	83.4	81.1	61.3	52.9
Profitability ratios (%)				
RoAE	12.0	14.4	14.8	16.3
RoAA	1.2	1.4	1.3	1.4
NIM	4.0	3.8	3.6	3.7
Operating Profit Margin	31.2	24.7	24.2	25.5
Net Profit Margin	12.8	12.8	12.5	13.1
Cost to Income	36.9	39.4	39.7	37.9

	FY11	FY12	FY13E	FY14E
Spread analysis (%)				
Yield on advances	10.8	12.0	12.1	12.0
Yield on investments	6.3	8.2	7.3	7.2
Yield on interest-earning assets	8.7	10.0	9.7	9.6
Cost of deposits	5.5	7.2	7.5	7.6
Cost of funds	5.1	6.8	6.6	6.6
Spread	3.5	3.2	3.1	3.0
Net Interest Income to AWF	3.8	3.6	3.4	3.5
Non Interest Income to AWF	1.1	1.0	1.0	1.0
Operating Profit to AWF	3.1	2.8	2.7	2.8
Net Profit to AWF	1.3	1.4	1.4	1.5

Valuation ratios (x)				
	FY11	FY12	FY13E	FY14E
P/E	14.6	11.0	9.6	7.6
P/BV	1.6	1.4	1.3	1.2
P/ABV	1.6	1.4	1.4	1.2



Arihant Research Desk

E. research@arihantcapital.com
T. 022-42254834

Head Office **Registered Office**

3rd Floor, Krishna Bhavan,
67 Nehru Road, Vile Parle (East),
Mumbai - 400057
Tel: (91-22) 42254800
Fax: (91-22) 42254880

E-5 Ratlam Kothi
Indore - 452003, (M.P.)
Tel: (91-731) 3016100
Fax: (91-731) 3016199

Stock Rating Scale

	Absolute Return
BUY	>20
ACCUMULATE	12-20
HOLD	5-12
REDUCE	<5

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