

## Federal Bank

### Performance Highlights

Particulars (₹ cr)	3QFY16	2QFY16	% chg (qoq)	3QFY15	% chg (yoy)
NII	605	608	(0.5)	587	3.1
Pre-prov. profit	325	337	(3.3)	397	(18.1)
PAT	163	161	0.9	265	(38.5)

Source: Company, Angel Research

Federal Bank reported a weak set of numbers for 3QFY2016. Its NII grew 3.1% yoy while profit declined on a yoy basis on account of decrease in non-interest income as well as higher provisions.

### Slippages at peak; NIM falls qoq

During 3QFY2016, the bank witnessed a loan growth of 9.8% yoy, while deposits grew by 14.1% yoy. Growth in advances was led by the Corporate and SME books, which grew by 19.4% and 17.1% yoy, respectively, while the growth in the retail loan book was lower at 6.9% yoy. CASA deposits, with a growth of 20.1% yoy, outpaced deposit growth, led by growth in both the current and savings deposits. As a result, the CASA ratio improved by 161bp yoy to 32.1%. The Reported NIM fell by 7bp qoq to 3.04%, due to interest reversal on account of higher slippages and base rate cut by the bank. Other income (excluding treasury) growth was moderate as the quarter saw some softness in forex income, while core fee income remained stable. Treasury gains during the quarter came in much lower at ₹23cr as against ₹77cr in 3QFY2015.

On the asset quality front, the annualized slippage ratio was higher at 4.5% as compared to 3.2% in 2QFY2016 and 2.2% in 3QFY2015. During the quarter, the bank registered the highest ever slippages of ₹571cr. 3 of the bank's accounts amounting to ₹225cr were sold to ARCs (1 account in the shipping industry [₹109cr] and 2 accounts falling in the metals segment). There is no pending stress on these lines as far as the list from the RBI is concerned. Recoveries and upgrades were higher at ₹108cr during the quarter, partially offsetting the impact of higher slippages in terms of absolute Gross NPAs which rose by 12.3% qoq to ₹1,684cr. Higher slippages led to an increase in the Gross NPA ratio by 25bp qoq to 3.15%, whereas the Net NPA ratio increased by 33bps qoq to 1.66%. The provision coverage ratio fell by 1,331bp yoy and 493bp qoq to 71.7% as of 3QFY2016.

**Outlook and valuation:** Earnings were affected due to decline in non-interest income, higher cost-income ratio and poor asset quality. Given the increasing uncertainty in the corporate books in the industry as a whole, we remain watchful of the bank's near-term performance on the asset quality front. At the current market price, the stock trades at 0.9x FY2017E ABV. **We maintain our Neutral rating on the stock.**

### Key financials

Y/E March (₹ cr)	FY2014	FY2015	FY2016E	FY2017E
NII	2,229	2,380	2,457	2,861
% chg	12.9	6.8	3.2	16.4
Net profit	839	1,006	675	948
% chg	0.1	19.9	(32.9)	40.4
NIM (%)	3.2	3.1	2.8	2.9
EPS (₹)	4.9	5.9	3.9	5.5
P/E (x)	10.2	8.5	12.7	9.0
P/ABV (x)	0.6	0.6	1.0	0.9
RoA (%)	1.2	1.3	0.8	0.9
RoE (%)	12.6	13.7	8.4	10.8

Source: Company, Angel Research; Note: CMP as of January 13, 2016

## NEUTRAL

CMP	₹50
Target Price	-
Investment Period	-

### Stock Info

Sector	Banking
Market Cap (₹ cr)	8,587
Beta	1.1
52 Week High / Low	79.7/47.4
Avg. Daily Volume	46,42,224
Face Value (₹)	2
BSE Sensex	24,854
Nifty	7,562
Reuters Code	FED.BO
Bloomberg Code	FB:IN

### Shareholding Pattern (%)

Promoters	0.0
MF / Banks / Indian Fls	30.6
FII / NRIs / OCBs	37.5
Indian Public / Others	32.0

Abs. (%)	3m	1yr	3yr
Sensex	(7.2)	(9.1)	24.9
FB	(22.2)	(32.5)	(3.8)

### 3-year price chart



Source: Company, Angel Research

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**Exhibit 1: 3QFY2016 performance**

Particulars (₹ cr)	3QFY16	2QFY16	% chg (qoq)	3QFY15	% chg (yoy)	FY2015	FY2014	% chg
<b>Interest earned</b>	<b>1,903</b>	<b>1,902</b>	<b>0.0</b>	<b>1,870</b>	<b>1.7</b>	<b>7,419</b>	<b>6,946</b>	<b>6.8</b>
- on Advances / Bills	1,386	1,400	(1.0)	1,399	(1.0)	5,447	5,011	8.7
- on investments	446	424	5.3	449	(0.7)	1,836	1,777	3.3
- on balance with RBI & others	17	19	(13.0)	21	(19.6)	62	52	19.1
- on others	55	60	(8.1)	1	3,650.7	74	106	(29.7)
<b>Interest Expended</b>	<b>1,298</b>	<b>1,294</b>	<b>0.3</b>	<b>1,283</b>	<b>1.1</b>	<b>5,039</b>	<b>4,717</b>	<b>6.8</b>
<b>Net Interest Income</b>	<b>605</b>	<b>608</b>	<b>(0.5)</b>	<b>587</b>	<b>3.1</b>	<b>2,380</b>	<b>2,229</b>	<b>6.8</b>
<b>Other income</b>	<b>183</b>	<b>182</b>	<b>0.6</b>	<b>220</b>	<b>(16.6)</b>	<b>878</b>	<b>694</b>	<b>26.6</b>
- Other income excl. treasury	160	156	2.6	142	12.5	623	540	15.3
- Treasury Income	23	26	(11.5)	77	(70.3)	256	154	66.1
<b>Operating income</b>	<b>789</b>	<b>791</b>	<b>(0.3)</b>	<b>807</b>	<b>(2.3)</b>	<b>3,259</b>	<b>2,922</b>	<b>11.5</b>
<b>Operating expenses</b>	<b>463</b>	<b>454</b>	<b>2.0</b>	<b>410</b>	<b>13.0</b>	<b>1,631</b>	<b>1,392</b>	<b>17.2</b>
- Employee expenses	259	249	3.9	235	10.0	892	722	23.6
- Other Opex	204	205	(0.3)	175	17.1	739	671	10.2
<b>Pre-provision Profit</b>	<b>325</b>	<b>337</b>	<b>(3.3)</b>	<b>397</b>	<b>(18.1)</b>	<b>1,628</b>	<b>1,530</b>	<b>6.4</b>
<b>Provisions &amp; Contingencies</b>	<b>75</b>	<b>87</b>	<b>(13.9)</b>	<b>(1)</b>	<b>(9,259.8)</b>	<b>107</b>	<b>318</b>	<b>(66.5)</b>
- Provisions for NPAs	-	127	(100.0)	56	(100.0)	204	228	(10.8)
- Provisions for Investments	-	(26)	(100.0)	(59)	(100.0)	(80)	112	(171.4)
- Other Provisions	75	(14)	(647.4)	2	3,345.4	(41)	(35)	16.1
<b>PBT</b>	<b>250</b>	<b>249</b>	<b>0.4</b>	<b>398</b>	<b>(37.1)</b>	<b>1,521</b>	<b>1,212</b>	<b>25.5</b>
Provision for Tax	88	88	(0.4)	133	(34.3)	515	373	38.1
<b>PAT</b>	<b>163</b>	<b>161</b>	<b>0.9</b>	<b>265</b>	<b>(38.5)</b>	<b>1,006</b>	<b>839</b>	<b>19.9</b>
Effective Tax Rate (%)	35.0	35.3	(30)bp	33.5	148bp	33.9	30.8	309bp

Source: Company, Angel Research

**Exhibit 2: 3QFY2016 performance**

Particulars	3QFY16	2QFY16	% chg (qoq)	3QFY15	% chg (yoy)
<b>Balance sheet</b>					
Advances (₹cr)	52,753	50,867	3.7	48,026	9.8
Deposits (₹ cr)	74,792	73,783	1.4	65,550	14.1
Credit-to-Deposit Ratio (%)	70.5	68.9	159bp	73.3	(273)bp
Current deposits (₹ cr)	3,877	4,178	(7.2)	3,194	21.4
Saving deposits (₹ cr)	20,128	19,335	4.1	16,791	19.9
CASA deposits (₹ cr)	24,005	23,513	2.1	19,985	20.1
CASA ratio (%)	32.1	31.9	23bp	30.49	161bp
CAR (%)	14.3	14.7	(39)bp	14.5	(19)bp
<b>Profitability Ratios (%)</b>					
Reported NIM	3.0	3.1	(7)bp	3.2	(16)bp
Cost-to-income ratio	58.7	57.4	129bp	50.8	796bp
<b>Asset quality</b>					
Gross NPAs (₹ cr)	1,684	1,499	12.3	1,067	57.9
Gross NPAs (%)	3.15	2.9	25bp	2.2	96bp
Net NPAs (₹ cr)	876	675	29.8	333	163.1
Net NPAs (%)	1.7	1.3	33bp	0.7	97bp
Provision Coverage Ratio (%)	71.7	76.6	(493)bp	85.0	(1331)bp
Slippage ratio (%)	4.5	3.2	129bp	2.2	230bp

Source: Company, Angel Research, Note: \*Basel III

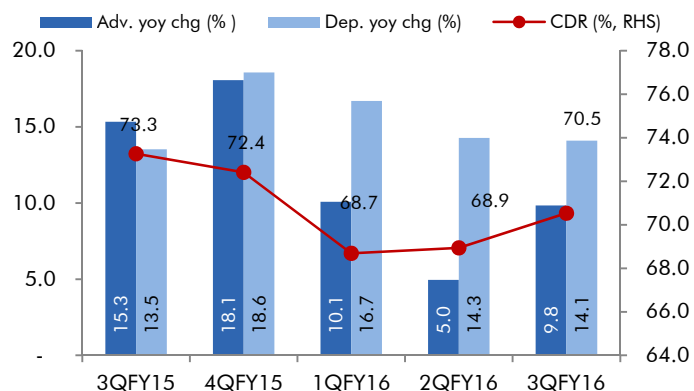
**Balance sheet growth moderate; NIM falls**

During 3QFY2016, the bank witnessed a loan growth of 9.8% yoy, while deposits grew by 14.1% yoy. Growth in advances was led by the Corporate and SME books, which grew by 19.4% and 17.1% yoy, respectively, while the growth in the retail loan book was lower at 6.9% yoy.

Deposits profile continues to be better with CASA inching higher to 32% of deposits, while credit growth has been mainly from credit substitutes in the corporate book. 82% of the incremental corporate advances were to the highly rated corporates with a rating of A and above.

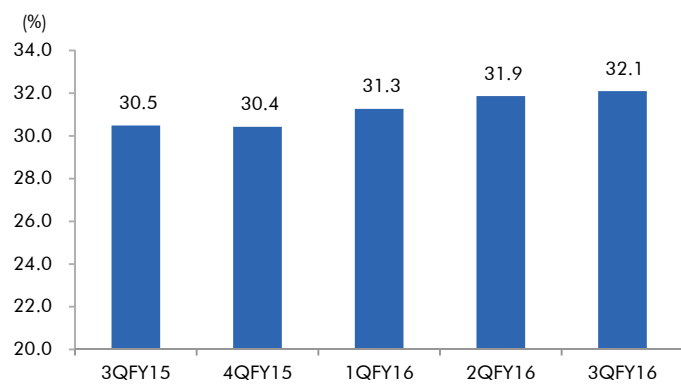
CASA deposits, with a growth of 20.1% yoy, outpaced deposit growth, led by growth in both the current and savings deposits. As a result, the CASA ratio improved by 161bp yoy to 32.1%.

**Exhibit 3: Business growth moderate in 3QFY2016**



Source: Company, Angel Research

**Exhibit 4: CASA ratio improves**

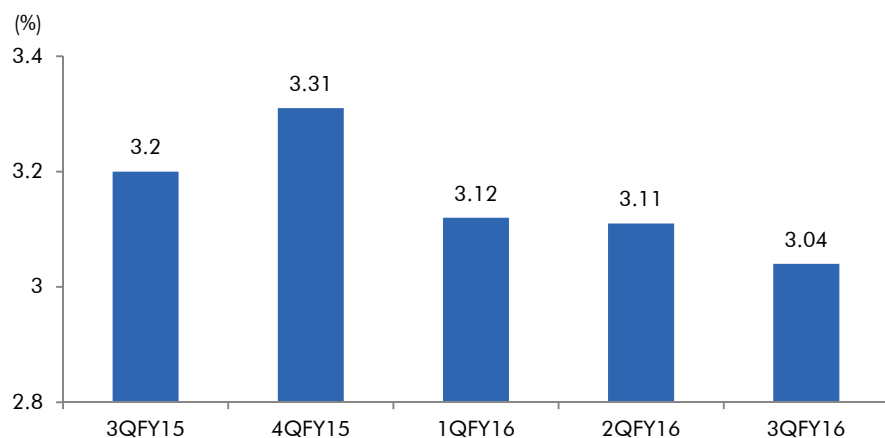


Source: Company, Angel Research

The Reported NIM fell by 7bp qoq to 3.04%, due to interest reversal on account of higher slippages and base rate cut by the bank.

Cost of deposits fell to 6.90% as against 6.98% in 2QFY2016 and is expected to trend lower going ahead. The Management expects NIM to be in the range of 3.10-3.15% in FY2017.

**Exhibit 5: NIM fell by 7bp qoq; 16bp yoy**



Source: Company, Angel Research

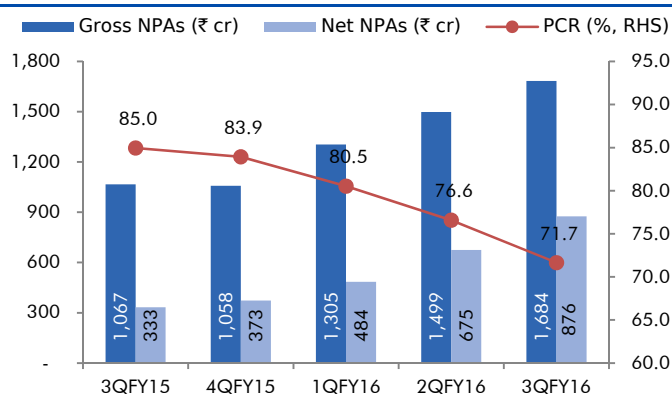
**Moderate performance in Non-interest income (excluding treasury)**

During the quarter, other income (excluding treasury) growth was moderate as the quarter saw some softness in forex income, while core fee income remained stable. Treasury gains during the quarter came in much lower at ₹23cr as against ₹77cr in 3QFY2015. The overall other income for the bank de-grew by 16.6% yoy.

### Asset quality woes worsen, Slippages at the peak

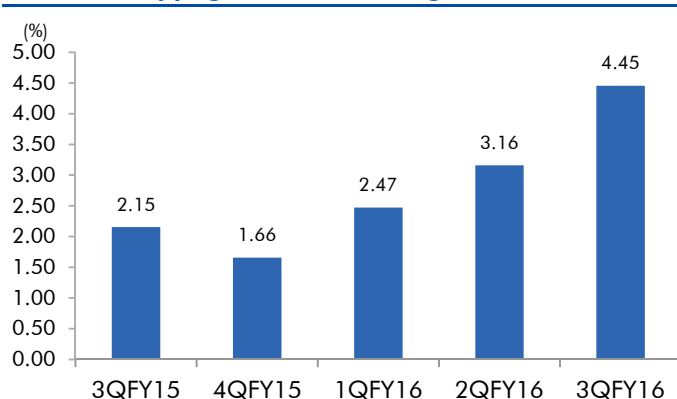
On the asset quality front, the annualized slippage ratio was higher at 4.5% as compared to 3.2% in 2QFY2016 and 2.2% in 3QFY2015. During the quarter, the bank registered the highest ever slippages of ₹571cr. 3 of the bank's accounts amounting to ₹225cr were sold to ARCs (1 account in the shipping industry [₹109cr] and 2 accounts falling in the metals segment). There is no pending stress on these lines as far as the list from the RBI is concerned. Recoveries and upgrades were higher at ₹108cr during the quarter, partially offsetting the impact of higher slippages in terms of absolute Gross NPAs which rose by 12.3% qoq to ₹1,684cr. Higher slippages led to an increase in the Gross NPA ratio by 25bp qoq to 3.15%, whereas the Net NPA ratio increased by 33bps qoq to 1.66%. The provision coverage ratio fell by 1,331bp yoy and 493bp qoq to 71.7% as of 3QFY2016. The bank has not undertaken any refinancing in 5/25 scheme nor participated in SDR during this quarter.

**Exhibit 6: Trends in Gross and Net NPA levels**



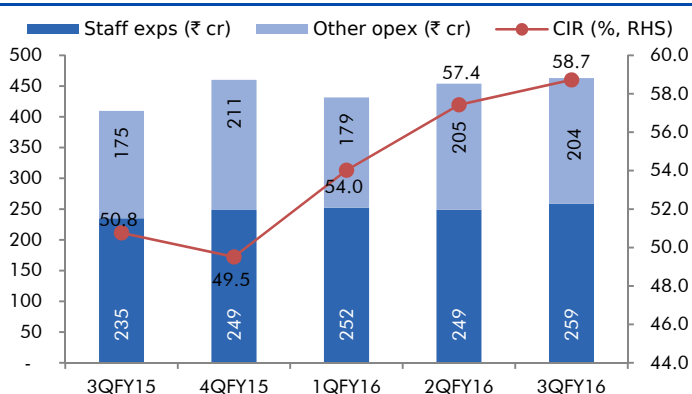
Source: Company, Angel Research

**Exhibit 7: Slippages at 4.5% during 3QFY2016**



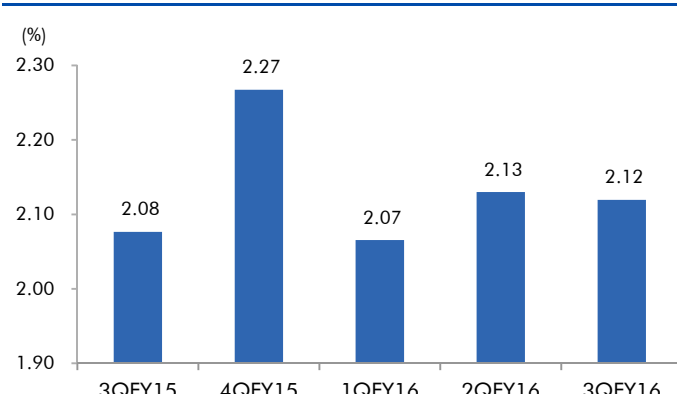
Source: Company, Angel Research

**Exhibit 8: Opex trends**



Source: Company, Angel Research

**Exhibit 9: Opex-to-avg. assets trend**



Source: Company, Angel Research

## Outlook and valuation

Earnings were affected due to decline in non-interest income, higher cost-income ratio and poor asset quality. Given the increasing uncertainty in the corporate books in the industry as a whole, we remain watchful of the bank's near-term performance on the asset quality front. At the current market price, the stock trades at 0.9x FY2017E ABV. **We maintain our Neutral rating on the stock.**

### Exhibit 10: Recommendation summary

Company	Reco.	CMP (₹)	Tgt. Price (₹)	Upside (%)	FY2017E P/ABV (x)	FY2017E Tgt. P/ABV (x)	FY2017E P/E (x)	FY15-17E EPS CAGR (%)	FY2017E RoA (%)	FY2017E RoE (%)
HDFCBk	Buy	1,059	1,262	19.2	3.2	3.8	17.4	22.4	1.9	19.7
ICICIBk*	Buy	239	304	27.3	1.6	1.7	9.8	13.5	1.6	14.7
YesBk	Buy	683	825	20.8	1.8	2.2	9.8	20.5	1.6	19.6
AxisBk	Buy	406	531	30.6	1.6	2.2	9.3	18.4	1.8	18.9
SBI*	Buy	201	237	17.7	1.0	1.0	8.2	17.8	0.7	12.8
<b>FedBk</b>	<b>Neutral</b>	<b>50</b>	<b>-</b>	<b>-</b>	<b>0.9</b>	<b>1.0</b>	<b>9.0</b>	<b>(2.9)</b>	<b>0.9</b>	<b>10.8</b>
SIB	Neutral	19	-	-	0.7	0.7	5.8	21.6	0.7	11.6
BOB	Neutral	132	-	-	0.7	0.7	6.2	17.5	0.6	10.6
PNB	Neutral	98	-	-	0.5	0.5	3.6	28.5	0.7	12.0
BOI	Neutral	100	-	-	0.3	0.8	3.0	14.0	0.3	7.6
IndBk	Neutral	99	-	-	0.3	0.3	3.3	19.4	0.6	8.6
Vijaya Bank	Neutral	32	-	-	0.4	0.4	4.8	14.1	0.4	8.8
OBC	Neutral	116	-	-	0.2	0.3	2.6	65.5	0.5	9.4
Allahabad Bank	Neutral	60	-	-	0.3	0.3	2.2	56.2	0.6	11.9
UnionBk	Neutral	128	-	-	0.4	0.4	3.3	18.1	0.6	11.4
CanBk	Neutral	199	-	-	0.3	0.3	2.8	12.0	0.6	11.2
AllBk	Neutral	60	-	-	0.3	0.4	2.2	56.2	0.6	11.9
IDBI#	Neutral	70	-	-	0.5	0.5	4.9	61.6	0.6	9.3

Source: Company, Angel Research; Note: \*Target multiples=SOTP target price/ABV (including subsidiaries); # Without adjusting for SASF

**Income statement**

Y/E March (₹ cr)	FY11	FY12	FY13	FY14	FY15	FY16E	FY17E
<b>Nil</b>	<b>1,747</b>	<b>1,953</b>	<b>1,975</b>	<b>2,229</b>	<b>2,380</b>	<b>2,457</b>	<b>2,861</b>
- YoY growth (%)	23.8	11.8	1.1	12.9	6.8	3.2	16.4
<b>Other income</b>	<b>517</b>	<b>532</b>	<b>664</b>	<b>694</b>	<b>878</b>	<b>821</b>	<b>927</b>
- YoY growth (%)	(2.7)	3.0	24.8	4.4	26.6	(6.5)	12.8
<b>Operating income</b>	<b>2,263</b>	<b>2,486</b>	<b>2,639</b>	<b>2,922</b>	<b>3,259</b>	<b>3,279</b>	<b>3,787</b>
- YoY growth (%)	16.6	9.8	6.2	10.7	11.5	0.6	15.5
<b>Operating expenses</b>	<b>836</b>	<b>979</b>	<b>1,180</b>	<b>1,442</b>	<b>1,631</b>	<b>1,861</b>	<b>2,073</b>
- YoY growth (%)	23.5	17.1	20.5	22.3	13.1	14.1	11.4
<b>Pre-prov. profit</b>	<b>1,427</b>	<b>1,506</b>	<b>1,460</b>	<b>1,480</b>	<b>1,628</b>	<b>1,418</b>	<b>1,714</b>
- YoY growth (%)	12.8	5.6	(3.1)	1.4	9.9	(12.9)	20.9
<b>Prov. &amp; cont.</b>	<b>525</b>	<b>337</b>	<b>266</b>	<b>268</b>	<b>106.7</b>	<b>385</b>	<b>265</b>
- YoY growth (%)	29.6	(35.9)	(21.1)	1.0	(60.2)	261.0	(31.3)
<b>PBT</b>	<b>902</b>	<b>1,170</b>	<b>1,194</b>	<b>1,212</b>	<b>1,521</b>	<b>1,032</b>	<b>1,449</b>
- YoY growth (%)	4.9	29.7	2.1	1.5	25.5	(32.1)	40.4
<b>Prov. for taxation</b>	<b>315</b>	<b>393</b>	<b>356</b>	<b>373</b>	<b>515</b>	<b>357</b>	<b>502</b>
- as a % of PBT	34.9	33.6	29.8	30.8	33.9	34.6	34.6
<b>PAT</b>	<b>587</b>	<b>777</b>	<b>838</b>	<b>839</b>	<b>1,006</b>	<b>675</b>	<b>948</b>
- YoY growth (%)	26.4	32.3	7.9	0.1	19.9	(32.9)	40.4

**Balance sheet**

Y/E March (₹ cr)	FY11	FY12	FY13	FY14	FY15	FY16E	FY17E
Share Capital	171	171	171	171	171	343	343
Reserves & Surplus	4,938	5,535	6,194	6,780	7,566	8,082	8,811
Deposits	43,015	48,937	57,615	59,731	70,825	80,741	93,659
- Growth (%)	19.3	13.8	17.7	3.7	18.6	14.0	16.0
Borrowings	1,582	3,935	4,957	5,458	2,084	4,071	4,402
Tier 2 Capital	306	306	230	230	224	219	213
Other Liab. & Prov.	1,445	1,742	1,883	2,224	1,980	2,323	2,630
<b>Total Liabilities</b>	<b>51,456</b>	<b>60,627</b>	<b>71,050</b>	<b>74,594</b>	<b>82,851</b>	<b>95,778</b>	<b>1,10,058</b>
Cash Balances	2,935	2,424	2,743	3,104	3,380	4,037	4,683
Bank Balances	813	1,108	977	1,425	1,401	1,619	1,860
Investments	14,538	17,402	21,155	24,118	24,409	29,951	33,765
Advances	31,953	37,756	44,097	43,436	51,285	57,439	66,629
- Growth (%)	18.6	18.2	16.8	-1.5	18.1	12.0	16.0
Fixed Assets	290	326	397	425	467	523	583
Other Assets	927	1,610	1,681	2,086	1,910	2,208	2,537
<b>Total Assets</b>	<b>51,456</b>	<b>60,627</b>	<b>71,050</b>	<b>74,594</b>	<b>82,851</b>	<b>95,778</b>	<b>1,10,058</b>
- Growth (%)	17.8	17.8	17.2	5.0	11.1	15.6	14.9



**Ratio analysis**

Y/E March	FY11	FY12	FY13	FY14	FY15	FY16E	FY17E
<b>Profitability ratios (%)</b>							
NIMs	3.8	3.6	3.1	3.2	3.1	2.8	2.9
Cost to Income Ratio	36.9	39.4	44.7	49.3	50.1	56.8	54.7
RoA	1.2	1.4	1.3	1.2	1.3	0.8	0.9
RoE	12.0	14.4	13.9	12.6	13.7	8.4	10.8
<b>B/S ratios (%)</b>							
CASA Ratio	26.9	27.5	27.2	31.2	29.4	29.3	29.2
Credit/Deposit Ratio	74.3	77.2	76.5	72.7	72.4	71.1	71.1
CAR	16.8	16.6	14.7	15.3	15.6	14.8	14.1
- Tier I	15.6	15.9	14.1	14.6	14.8	14.1	13.5
<b>Asset Quality (%)</b>							
Gross NPAs	3.5	3.3	3.4	2.5	2.0	2.2	2.0
Net NPAs	0.6	0.5	1.0	0.7	0.7	0.7	0.6
Slippages	3.2	2.1	2.1	1.2	1.7	2.1	1.5
Loan Loss Prov./Avg. Assets	1.0	0.4	0.3	0.3	0.3	0.4	0.2
Provision Coverage	83.4	84.7	72.2	70.4	64.8	67.8	68.5
<b>Per Share Data (₹)</b>							
EPS	3.4	4.5	4.9	4.9	5.9	3.9	5.5
ABVPS	59.7	66.7	73.8	80.6	89.0	48.6	52.9
DPS	8.5	9.0	9.0	10.0	11.0	4.0	5.5
<b>Valuation Ratios</b>							
PER (x)	14.6	11.0	10.2	10.2	8.5	12.7	9.0
P/ABVPS (x)	0.8	0.8	0.7	0.6	0.6	1.0	0.9
Dividend Yield	17.0	18.0	18.0	20.0	22.0	8.0	11.0
<b>DuPont Analysis (%)</b>							
NII	3.7	3.5	3.0	3.1	3.0	2.8	2.8
(-) Prov. Exp.	1.1	0.6	0.4	0.4	0.1	0.4	0.3
Adj. NII	2.6	2.9	2.6	2.7	2.9	2.3	2.5
Treasury	0.1	0.1	0.3	0.2	0.3	0.2	0.2
Int. Sens. Inc.	2.7	3.0	2.9	2.9	3.2	2.5	2.7
Other Inc.	1.0	0.8	0.7	0.7	0.8	0.8	0.7
Op. Inc.	3.7	3.8	3.6	3.6	4.0	3.2	3.4
Opex	1.8	1.7	1.8	2.0	2.1	2.1	2.0
PBT	1.9	2.1	1.8	1.7	1.9	1.2	1.4
Taxes	0.7	0.7	0.5	0.5	0.7	0.4	0.5
<b>RoA</b>	<b>1.2</b>	<b>1.4</b>	<b>1.3</b>	<b>1.2</b>	<b>1.3</b>	<b>0.8</b>	<b>0.9</b>
Leverage (x)	9.7	10.4	10.9	10.9	10.7	11.1	11.7
<b>RoE</b>	<b>12.0</b>	<b>14.4</b>	<b>13.9</b>	<b>12.6</b>	<b>13.7</b>	<b>8.4</b>	<b>10.8</b>

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Disclosure of Interest Statement	Federal Bank
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

*Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors*

<b>Ratings (Based on expected returns over 12 months investment period):</b>	Buy (> 15%)	Accumulate (5% to 15%) Reduce (-5% to -15%)	Neutral (-5 to 5%) Sell (< -15)
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