

Federal Bank (FB)

Banking | Analyst Meet Update

BUY
CMP: Rs180 | Target Price (TP): Rs226 | Upside: 26%
February 23, 2025

Well charted out strategy; All eyes on execution ahead

Key Points

- Federal Bank held an analyst meet represented by Mr. K V S Manian, MD & CEO; Ms. Shalini Warriar, ED and head of retail banking; Mr. Harsh Dugar, ED and head of wholesale banking; Mr. Venkatraman Venkateswaran, Group president and CFO; Mr. Souvik Roy, Head - Investor Relations.
- The bank unveiled its new strategy and discussed its roadmap for the next 3 years up to FY28. It has identified twelve key themes under its new strategy, where it is benchmarking itself with top 6 private sector banks and aims to position itself in between the best 3 private banks and the next 3 private banks on various parameters.
- Some of the key focus areas for the bank include: (1) NIM improvement through focus on CASA and retail term deposits and increasing the share of medium yield / high yield assets, (2) Focus on becoming SME bank of choice and on the wholesale side focus is on mid-market borrowers; (3) Fee enhancement, (4) Selective geographic expansion through addition of 400-450 branches by FY28; the branches will be made more liability centric, (5) Streamlining processes at branches to free up time for customer acquisition, servicing and engagement, (6) The Brand and branches to be redesigned and brand ambassador to be appointed, (7) Further digitalization to reduce TAT, (8) Achieve a balance between partner led sourcing and own sourcing for credit cards, PL and savings accounts, (9) Foster culture of collective focus on P&L, (10) Expansion of NRI clients beyond GCC nations (11) Cost optimization by improving productivity, leveraging tech subsidiary Fedserv and the use of AI and other technology, (12) Expand organically or inorganically in microfinance, insurance, wealth management, AMC and broking.
- In our view, the bank has come out with a well-crafted strategy of focusing on leveraging its existing strengths and taking it forward from here by aiming to close the gaps in terms of products, new businesses, customer segments and geographies. However, execution will be key here. We continue to maintain 'BUY' on Federal Bank with an unchanged target price (TP) of Rs226 (valued at 1.4x December 2026E ABV plus subsidiary value per share of Rs8.6). Our target multiple of 1.4x is at a 37% premium to the past 5-year average multiple of 1x ABV, which adequately captures our loan/earnings CAGR estimates of 14.6%/13.7% over FY24-FY27E, which will lead to 1.3% RoA in FY27E.

Est Change	Unchanged
TP Change	Unchanged
Rating	Unchanged

Company Data and Valuation Summary

Reuters	FED.BO
Bloomberg	FB IN Equity
Mkt Cap (Rsbn/US\$bn)	441.6 / 5.1
52 Wk H / L (Rs)	217 / 140
ADTV-3M (mn) (Rs/US\$)	1,567.6 / 18.3
Stock performance (%) 1M/6M/1yr	(6.5) / (11.5) / 17.0
Nifty 50 performance (%) 1M/6M/1yr	(1.6) / (4.7) / 2.6

Shareholding	1QFY25	2QFY25	3QFY25
Promoters	0.0	0.0	0.0
DIs	45.0	47.0	48.7
FIs	28.6	27.7	26.3
Others	26.4	25.3	25.0
Pro pledge	0.0	0.0	0.0

Financial and Valuation Summary

Particulars (Rsmn)	FY24E	FY25E	FY26E	FY27E
NII	82,935	95,216	1,05,067	1,24,299
% growth	14.7	14.8	10.3	18.3
NIM %	3.1	3.1	3.0	3.1
C/I Ratio %	54.5	53.9	52.1	50.3
Operating Profit	51,745	58,278	70,167	85,166
% growth	7.9	17.3	15.6	21.4
Adjusted PAT	37,206	37,266	45,909	54,751
% growth	23.6	6.7	15.7	19.3
ABVPS (Rs /share)	118	131	146	163
P/ABV	1.5	1.4	1.2	1.1
RoA (%)	1.3	1.2	1.3	1.3
Leverage (x)	11.2	10.6	10.7	10.9
RoE (%)	14.7	12.9	13.4	14.3

Source: Bloomberg, Company, Nirmal Bang Institutional Equities Research

[Key Links-3QFY25 presentation](#)

Please refer to the disclaimer towards the end of the document.

Macro Commentary and Banking Industry Trends: India's FY25 GDP forecast by various institutions including CMIE, MOSPI, IMF, ADB, S&P Global and OECD has been in between 6.3-6.8%. RBI projects GDP growth at 6.7% for FY26. The bank follows the RBI forecast for its internal projections on business growth. Industrial growth has strengthened with rising steel and cement output, while auto sales have seen moderate growth amid weak demand year on year. Services exports and imports saw strong growth.

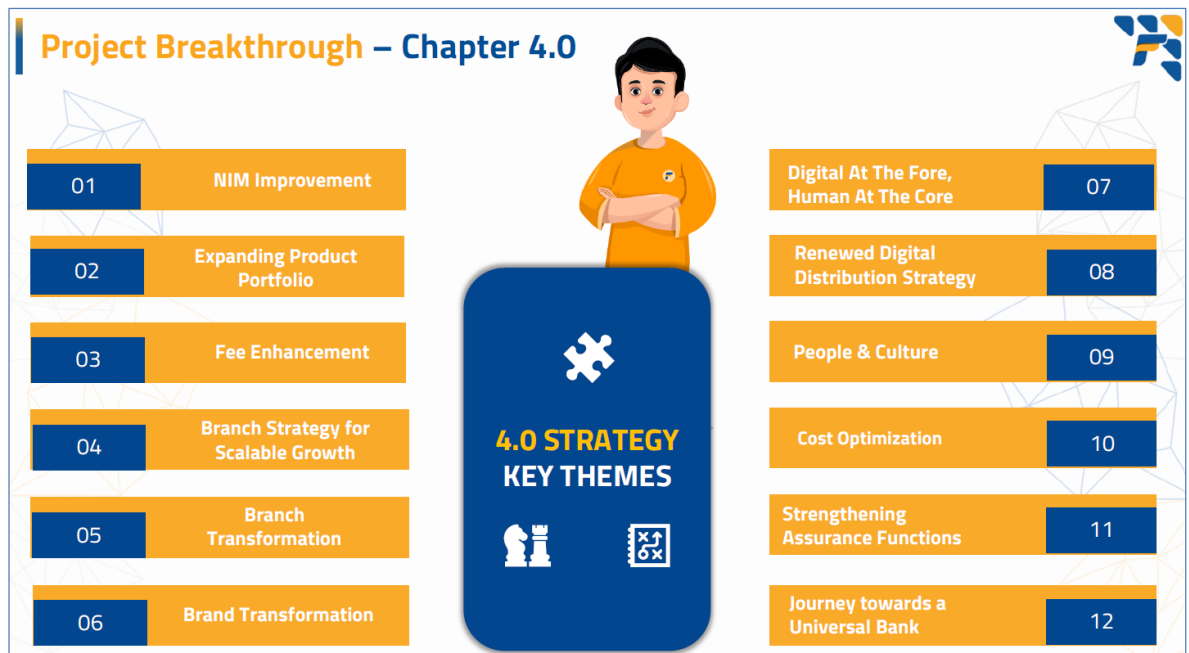
Credit growth of 36 banks slowed down to 12% YoY during 9MFY25, with YoY growth in different segments as follows: retail (14%), agriculture (12%), MSME (15%) and corporate (9%). C/D ratio stood at 82%, indicating potential stress in funding availability going forward. Deposits grew by 11% YoY in 9MFY25. Industry CASA ratio stood at 37%. YoY growth in CASA was 6% and TD was 15%. The Cost to income ratio improved by 140bps to 48.3% for the industry. All banks have CRAR >13%. Private banks reported 12% YoY growth in PAT, driven by controlled growth in operating expenses. SFB PAT declined by 13% amid rising credit costs. From March 2023 onwards, while the average banking system lending rate has remained stable at 9.3%, the average cost of deposits increased from 6.2% in March 2023 to 7% in November 2024.

Phases Federal Bank has gone through and beginning of Chapter 4: (1) Nascent Era, Chapter 1 (1945 – 1979): During this time the bank became a household name in its home market. (2) Chequered Era, Chapter 2 (1979 – 2010): This phase was marked by a low penetration outside home market, asset quality issues, lower paced growth, employee productivity issues and amalgamation of 'The Ganesh Bank of Kurundwad Ltd with itself in 2006. (3) Resurgence Era, Chapter 3 (2010-2024): During this phase asset quality improved, it increased penetration outside Kerala, there was verticalization and introduction of new business segments, the brand went through an overhaul and the bank got attention from capital markets and institutional investors. (4) Breakthrough Era, Chapter 4 (present phase): From here the management plans to modernize the bank and make the franchise truly national. It aims to move closer to the top private sector banks in terms of various parameters and create a universal bank.

Key focus areas: The bank has unveiled its new strategy with a focus on the following areas: (1) Becoming the SME bank of choice by establishing best in class SME banking ecosystem with a differentiated value proposition. (2) On the corporate and institutional banking side, the focus is on high growth mid-market businesses. (3) It is expanding offerings in wealth management, capital markets and premium savings solutions for both NR and domestic clients. (4) NRI business is a moat that the bank has created over a long period of time. 20% of the remittances into the country happen through Federal Bank. Going ahead, it is aiming to unlock NR growth beyond Kerala and GCC nations and enhance it by wealth offerings. (5) Instill P&L culture in the bank's business heads. (6) Aiming to move from affordability driven to value driven banking. (7) Expand nationally while leveraging Kerala's strengths. (8) Making the branch model liability centric. (9) Focusing on mass affluent, MSME and next-gen customers to deepen relationships and enhance value. (10) Leveraging AI and automation to enhance efficiency, streamline operations and boost customer experience. (11) Strengthening governance, risk and compliance to ensure stability while scaling new heights.

Twelve Key themes of Strategy 4.0: The bank has identified twelve key themes under its new strategy, where it is benchmarking itself with top 6 private sector banks and aims to position itself in between the best 3 private banks and the next 3 private banks.

Exhibit 1: Key themes of Strategy 4.0



Source: Company, Nirmal Bang Institutional Equities Research

Theme 1 – NIM Improvement: For NIM improvement the bank is giving equal weightage to liabilities, rather than just depending on growing higher yielding assets. It wants the branches to focus on growing CASA and retail term deposits. It plans to increase the CASA ratio from 30% at present to 36% by FY28. Of this 4% will be driven by CA deposit mobilization through strategic product innovation and market penetration. The bank also plans to deepen relationships with capital markets for better fee and float. For NR deposits it wants to diversify its base by tapping high CASA potential markets beyond the gulf and Kerala. Overall, there will be a granular focus on CASA and TD to ensure deposit stability, LCR efficiency and cost of funds.

On the asset side, it will be looking at increasing the proportion of medium yield assets (LAP, SME, business banking and commercial banking) from 31% at present to 34% by FY28 and the share of higher yielding assets from 5% to 8% during the same period. It will target mid-market corporate borrowers to improve spreads and asset quality. The PSL portfolio will be aligned with profitability and compliance objectives. As the market conditions improve, it will expand higher yielding unsecured loans to optimize portfolio returns. The bank will apply RAROC and tenor-based pricing methodologies to enhance lending margins.

Theme 2 – Expanding product portfolio: The bank is looking to expand the following segments – scaling up used vehicle finance in CV/CE and car loans; expand offerings for micro-LAP products; tractor finance; EMI-based unsecured business loans to existing customers; affordable housing loans; real estate finance; sustainable finance (renewable energy, EV financing); correspondent banking; syndication and investment banking; capital market services business; and offering investment products like wealth management, 3 in 1 accounts to domestic and NR customers and bespoke solutions to NR customers.

Theme 3 – Fee enhancement: For 9MFY25, Federal Bank’s fee to average assets ratio stood at 1.1% as against 1.7% in the case of best 3 private banks and 1.4% in the case of next 3 private banks. It aims to position itself in between the best 3 and next 3 private banks in terms of fee to average assets ratio. For fee enhancement, key opportunities it will be focusing on include trade and forex income, wealth management and bancassurance, credit cards and acquiring businesses and cash

management services. This will be achieved through product co-origination and cross selling with segmental offerings for mass affluent and NR customers, MSME and mid-market borrowers.

Theme 4 – Branch strategy for scalable growth: Federal Bank's current branch strength is 1550 branches and by FY28 the bank plans to add 400-450 branches. For this, it will target selective state level expansion focusing on top 10 high GSDP states (80-90% new branches to come up in these states) and tier-2 cities. For metros it will adopt pincode level strategies. Besides this expansion, it will focus on improving the productivity of existing branches.

Theme 5 – Branch transformation: Over here, the main focus will be on streamlining processes, reduce manual effort and enhancing efficiency, so that branch staff time is dedicated more towards customer acquisition, engagement and service. There will be different RMs for wealth business, personal banking and business banking, rather than putting one RM to do everything.

Theme 6 – Brand transformation: The positioning will be towards small businesses and mass affluent segments. The brand and branches will be redesigned and a brand ambassador will be appointed. Focus will be on reinforcing loyalty in the home market and increasing brand salience outside the home market.

Theme 7 – Digital at the fore, human at the core: The bank has undertaken a lot of digital initiatives with focus on both customer and employee enablement. It is streamlining and automating end to end loan processes and is looking at fully digitalizing customer onboarding in order to reduce TAT. It has 12-13 LOS for each product which it wants to unify into a similar platform.

Theme 8 – Renewed digital distribution strategy: The bank will focus on faster growth of organic credit cards through its own digital channels while continuing to source through fintech partners. It plans to reduce reliance on partner sourced credit cards from 70% at present to 55% by FY28. In the case of sourcing through partners, the bank has an economic arrangement which limits the initial cost but limits the upside in terms of profits. While doing own sourcing the bank has to take the acquisition cost in the beginning but the upside in terms of profit is higher.

In personal loans, the bank is looking at multiple partnerships to diversify sourcing and increase the proportion of partner sourced PL book from 40% at present to 50% in FY28. In the case of savings accounts the focus will be on gen Z through scaling up own digital acquisition as well as through strategic partnerships. It plans to increase own sourcing of SA accounts from 2% at present to 25% by FY28.

Theme 9 – People and culture: Foster culture of collective focus on P&L. The vertical heads will be encouraged to act as CEOs of their respective domains and the branch manager role will be made more attractive.

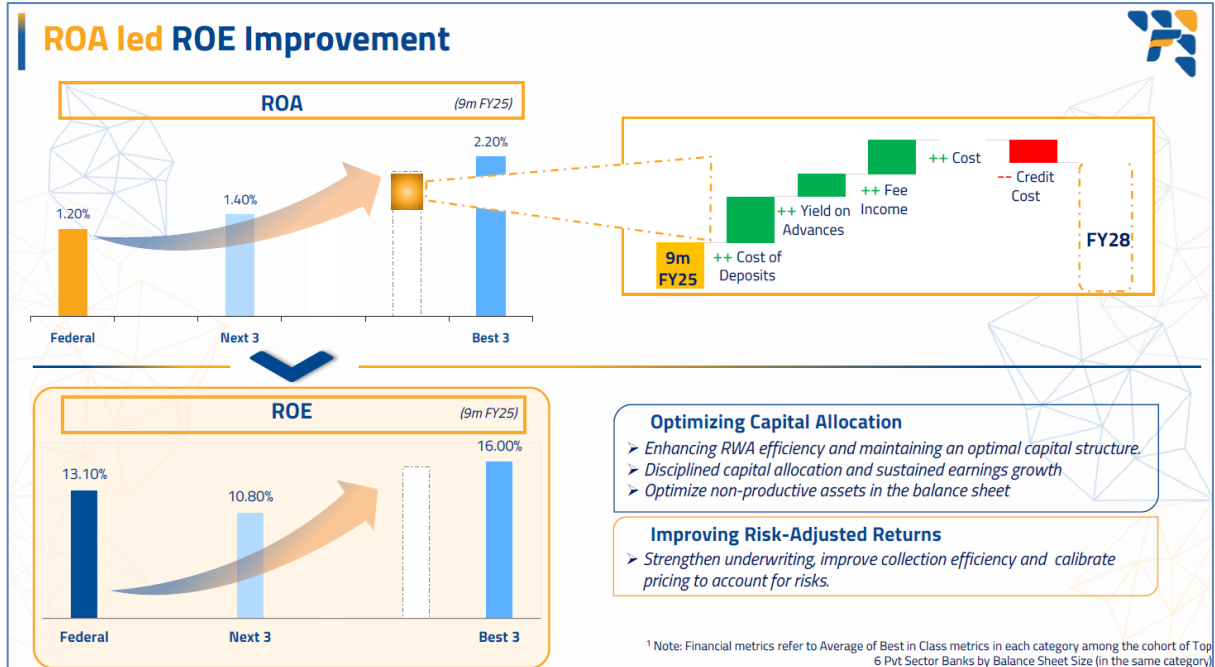
Theme 10 – Cost optimization: Cost optimization will be achieved through enhancing productivity; leveraging subsidiary Fedserv to reduce cost of operations through its call centers and back office; centralize and regionalize processes through removal of non-sales non-service operations out of the branch environment; leverage AI and automate technology to streamline operations; cost rationalization through targeted initiatives to identify and control major costs. The cost to average asset ratio of Federal bank was at 2.15% in 9MFY25 and it aims to bring it down to between that of the best 3 private banks (1.54%) and the next 3 private banks (2.14%).

Theme 11 – Strengthening assurance functions: Over there the focus will be on compliance, risk management and audit.

Theme 12 – Evolution towards a universal bank: Federal Bank at present has an NBFC subsidiary and a life insurance company as an associate. In future it plans to organically or inorganically diversify into microfinance, asset management, wealth management, affordable housing, securities and capital market services and investment banking.

Ingredients of RoA improvement in future: Federal Bank's RoA in 9MFY25 was 1.2% and by FY28 it aims to position itself in between the best 3 private banks (2.2%) and the next 3 private banks (1.4%) through lowering cost of deposits, improving yield on advances and fee income. However, the credit cost is expected to see some upward normalization during the same period. It will target improving risk adjusted returns by strengthening underwriting, improving collection efficiency and calibrate pricing to account for risks.

Exhibit 2: Ingredients of RoA improvement



Source: Company, Nirmal Bang Institutional Equities Research

Other Highlights:

- Federal Bank is targeting loan growth of 1.5x nominal GDP.
- There will be short term pressures on margins as the repo rate falls and deposits reprice downwards slower than loans. But in the long term, the bank would like to position itself between the best 3 private banks and next 3 private banks.
- The bank believes that it has not exploited the CA opportunity within its existing network. In Kerala itself the CA opportunity is more than it has exploited. There is CA potential on the SME side, commercial banking and business banking side.
- RoA expansion will be driven more by the liability side followed by the fee side and then by yield on assets.
- As the CRAR is 16.5% including profits, there is no requirement of raising capital.
- Just like it happened in home loans, there is some irrational pricing in the SME segment. But the wallet share from this business can be very good and if a bank chooses its customers properly and has a focused strategy, this segment can be RoE accretive.
- In the NRI segment, the bank's largest market share comes out of the bank's NRE deposits, followed by NRO deposits and then followed by FCNR (B) deposits. FCNR (B) is quite irrationally priced and the bank has never been a large player here.
- Despite the metro markets being highly competitive for deposits, the top 10 markets still remain large. The bank will be following a pin code level strategy in metros.
- Federal bank will prefer building its currency well, before going in for inorganic expansion in 3-5 years.
- By co-origination the bank means it will be sourcing more products from one customer and improving product per customer.
- The short-term environment is not very friendly for adding higher yield products now. The bank would wait to get air cleared about the credit costs on those kinds of products.
- The bank would like to focus on improving the productivity of existing branches before getting aggressive on branch expansion.
- In line with the top 4-5 universal banks, the bank would build the insurance, capital markets, AMC and broking businesses in next few years through organic or inorganic route.
- On the issue of investments in subsidiary in similar line of business, the bank has made its representation to the regulator and is waiting for final response on the same.
- The bank has re-started issuing cards with Scapia. As the other partners fall in line with the regulatory requirements, it will restart issuing cards through them.
- Not looking at rate reductions in savings accounts. The bank does have a sweep product.
- The bank's ratio of non-fund based to fund-based products is lower. It will be expanding the non-fund-based product portfolio as per its risk appetite.

Exhibit 3: Financial summary

Y/E March (Rsmn)	FY23	FY24	FY25E	FY26E	FY27E
Net interest income	72,322	82,935	95,216	1,05,067	1,24,299
Operating profit	47,944	51,745	58,278	70,167	85,166
PAT	30,106	37,206	37,266	45,909	54,751
EPS (Rs)	14	15	16	19	22
BV (Rs)	102	119	132	147	165
P/E (x)	12.6	11.8	11.1	9.6	8.1
P/BV (x)	1.8	1.5	1.4	1.2	1.1
GNPAs (%)	2.4	2.1	2.0	2.0	2.0
NNPAs (%)	0.7	0.6	0.5	0.5	0.5
RoA (%)	1.3	1.3	1.2	1.3	1.3
RoE (%)	14.9	14.7	12.9	13.4	14.3

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: SOTP Valuation

Company Name	Stake (%)	Financial Parameter	Multiple (x)	Value per Share (Rs)
Federal Bank		Dec 2026E ABV (Rs)	155.3	
Fedbank Financial Services Limited	61.0%	Current Mcap (Rs mn)	34,248.2	8.5
Federal Operations and Services Limited	100.0%	FY24 PAT (Rs mn)	60	0.1
Ageas Federal Life Insurance Company Limited	26.0%	March 2024 Networth	11,758	1.2
Equirus Capital Private Limited	19.6%	FY24 PAT (Rs mn)	440	0.3
<i>Holding Company Discount (%)</i>				15
Target Price (Rs)				226.1
Upside (%)				23.3

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: One-year forward P/ABV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 6: Income statement

Y/E March (Rsmn)	FY23	FY24	FY25E	FY26E	FY27E
Interest Income	1,68,036	2,21,883	2,65,973	2,93,951	3,43,194
Interest expense	95,715	1,38,948	1,70,757	1,88,885	2,18,895
Net interest income	72,322	82,935	95,216	1,05,067	1,24,299
Non-interest income	23,300	30,793	36,494	41,496	47,163
Net Revenue	95,622	1,13,728	1,31,709	1,46,563	1,71,462
Operating Expense	47,678	61,983	73,432	76,396	86,296
-Employee Exp	21,730	28,231	31,055	32,370	35,775
-Other Exp	25,948	33,752	42,377	44,027	50,521
Operating profit	47,944	51,745	58,278	70,167	85,166
Provisions	7,499	1,961	8,086	12,093	14,638
PBT	40,445	49,784	50,192	58,074	70,528
Taxes	10,339	12,578	12,926	12,164	15,777
PAT	30,106	37,206	37,266	45,909	54,751

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY23	FY24	FY25E	FY26E	FY27E
Share capital	4,232	4,871	4,910	4,910	4,910
Reserves & Surplus	2,10,830	2,86,073	3,19,712	3,56,440	4,00,240
Shareholder's Funds	2,15,062	2,90,944	3,24,622	3,61,350	4,05,150
Deposits	21,33,860	25,25,340	27,70,300	31,31,070	35,38,823
Borrowings	1,93,193	1,80,264	3,05,549	3,48,646	3,97,822
Other liabilities	61,303	86,570	15,897	57,734	1,09,699
Total liabilities	26,03,418	30,83,118	34,16,368	38,98,800	44,51,495
Cash/Equivalent	1,76,887	1,89,629	2,21,624	2,50,486	2,83,106
Advances	17,44,469	20,94,033	23,72,811	27,34,661	31,51,692
Investments	4,89,833	6,08,595	6,51,021	7,35,802	8,31,623
Fixed Assets	9,340	10,201	14,776	15,376	16,001
Other assets	1,82,889	1,80,660	1,56,136	1,62,476	1,69,073
Total assets	26,03,418	30,83,118	34,16,368	38,98,800	44,51,495

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Key ratios

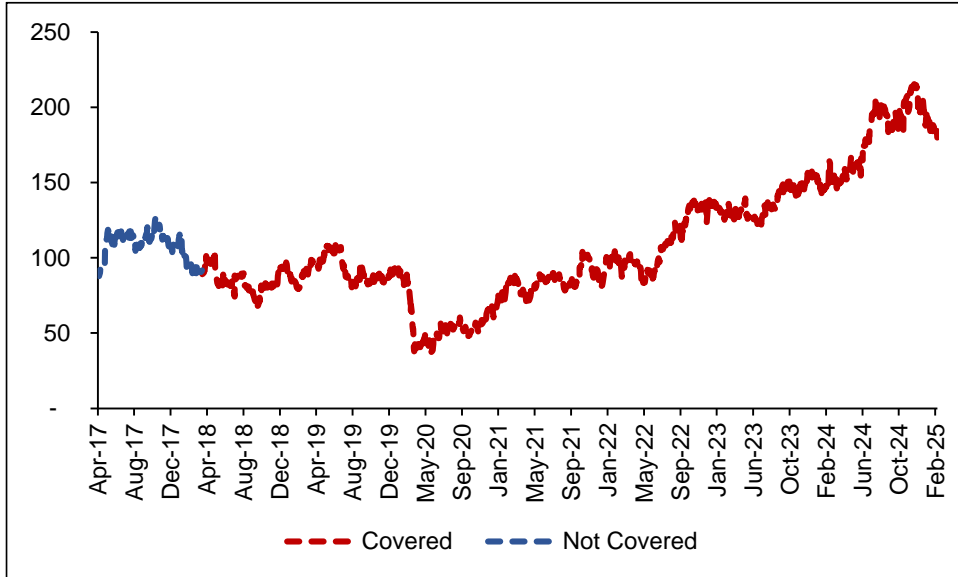
Y/E March	FY23	FY24	FY25E	FY26E	FY27E
Growth (%)					
NII growth	21.3	14.7	14.8	10.3	18.3
Pre-provision profit growth	27.6	7.9	17.3	15.6	21.4
PAT growth	59.3	23.6	6.7	15.7	19.3
Business (%)					
Deposit growth	17.4	18.3	9.7	13.0	13.0
Advance growth	20.4	20.0	13.3	15.2	15.2
CD	81.8	82.9	85.7	87.3	89.1
CASA	32.9	29.6	30.3	30.7	31.1
Operating efficiency (%)					
Cost-to-income	49.9	54.5	53.9	52.1	50.3
Cost-to-assets	2.0	2.2	2.2	2.1	2.1
Spreads (%)					
Yield on advances	8.4	9.2	9.5	9.3	9.4
Yield on investments	6.3	6.7	7.2	6.7	6.8
Cost of deposits	4.4	5.5	4.5	4.5	4.5
Yield on assets	7.6	8.4	8.7	8.5	8.6
Cost of funds	4.5	5.5	5.9	5.8	5.9
NIMs	3.3	3.1	3.1	3.0	3.1
Capital adequacy (%)					
Tier I	13.0	14.6	15.1	14.5	14.2
Tier II	1.8	1.5	1.3	1.2	1.0
Total CAR	14.8	16.1	16.4	15.6	15.2
Asset Quality (%)					
Gross NPA	2.4	2.1	2.0	2.0	2.0
Net NPA	0.7	0.6	0.5	0.5	0.5
Provision coverage	71.2	72.3	75.2	75.2	75.2
Slippage	1.0	0.8	0.8	1.0	0.9
Credit-cost	0.5	0.1	0.4	0.5	0.5
Return (%)					
ROE	14.9	14.7	12.9	13.4	14.3
ROA	1.3	1.3	1.2	1.3	1.3
RORWA	2.2	2.1	1.8	2.0	2.0
Per share					
EPS	14	15	16	19	22
BV	102	119	132	147	165
ABV	100	118	131	146	163
Valuation					
P/E	12.6	11.8	11.1	9.6	8.1
P/BV	1.8	1.5	1.4	1.2	1.1
P/ABV	1.8	1.5	1.4	1.2	1.1

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 March 2018	Buy	91	112
10 May 2018	Buy	101	116
18 July 2018	Buy	88	119
9 October 2018	Buy	70	115
17 October 2018	Buy	82	117
18 January 2019	Buy	89	122
8 April 2019	Buy	99	123
6 May 2019	Buy	98	134
8 July 2019	Buy	107	134
17 July 2019	Buy	107	135
7 October 2019	Buy	86	124
17 October 2019	Buy	82	115
8 January 2020	Buy	87	111
21 January 2020	Buy	94	109
27 March 2020	Buy	43	59
9 April 2020	Buy	41	59
29 May 2020	Buy	43	57
9 July 2020	Buy	54	65
16 July 2020	Accumulate	51	57
23 September 2020	Accumulate	49	55
7 October 2020	Accumulate	52	54
19 October 2020	Buy	52	63
26 November 2020	Buy	59	72
8 January 2021	Buy	76	89
21 January 2021	Buy	77	91
21 February 2021	Buy	83	111
17 May 2021	Buy	82	112
25 July 2021	Buy	85	111
26 September 2021	Buy	81	119
24 October 2021	Buy	103	124
26 January 2022	Buy	96	127
07 May 2022	Buy	92	120
17 July 2022	Buy	99	119
19 September 2022	Buy	122	149
16 October 2022	Buy	130	150
16 January 2023	Buy	140	166
1 March 2023	Buy	129	166
22 March 2023	Buy	129	176
7 May 2023	Buy	128	178
14 July 2023	Buy	127	184
17 October 2023	Buy	148	176
17 December 2023	Buy	157	182
17 January 2024	Buy	150	178
03 May 2024	Buy	168	204
07 July 2024	Buy	186	218
25 July 2024	Buy	201	235
10 October 2024	Buy	186	236
29 October 2024	Buy	185	231
6 December 2024	Buy	215	254
10 January 2025	Buy	189	235
28 January 2025	Buy	184	226
23 February 2025	Buy	180	226

Rating track graph



DISCLOSURES

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Stock Ratings Absolute Returns

BUY > 15%

HOLD -5% to 14%

SELL < -5%

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