Federal Bank – BUY

24 February 2025

Analyst day takeaways

Risk-reward favourable; upgrade to BUY

We attended Federal Bank's (FB) analyst day, where K.V.S Manian, the recently appointed CEO, presented new medium-term strategy. In its pursuit to become a universal bank, FB intends to launch new businesses, open 400-450 new branches (> additions since FY14), and laid out aggressive FY28 targets – ROA/ROE improvement by 75/120bps. We tweak our est. (still conservative), and raise SOTP based TP to Rs218 (21% upside). Post 17% correction in stock price, risk-reward is favourable, and we upgrade our rating to BUY.

Aspires to become a PAN India and truly universal bank: In its pursuit to become a universal bank, FB intends to organically and/or inorganically build MFI, asset and wealth management, affordable housing, capital/ securities market businesses. FB intends to mainly focus on the four pillars: a) Expand NR deposit franchise (where it is already dominant) outside of Kerala and GCC, b) Expand mass affluent banking, c) Become SME bank of choice, and d) Focus on profitable mid-corporate banking. The CEO shared 12 themes (Fig. 6) that FB will be focusing on, and various business initiatives identified (Fig. 9) to help accomplish the strategy.

Focus on profitability over growth; aggressive targets laid out … FB aspires for 70-80bps RoA improvement by FY28 led by higher NII (better CASA, lower COF, higher loan yield) and fee income growth (higher cross sell, more transaction banking fees), stable cost ratios (productivity gains), but partly offset by a rise in credit costs. With FB's Top 3 priorities being CASA, NIM and fee income, there is a clear focus on improving profitability over growth. Our est. are fairly conservative vis-à-vis the management guidance (Fig. 1), and we expect ROA improvement to be only gradual.

… but even a partial delivery should suffice for stock re-rating: We like the FB's strategy but believe the ROA improvement target of 70-80bps by FY28E is ambitious. Having said that, even if FB is able to deliver only 20-30bps ROA improvement and reach 1.4-1.5% ROA and 14-14.5% ROE, the stock can potentially re-rate by 20-30% to 1.4-1.5x P/B vs. current 1YF core P/B of 1.14x. We tweak FY26/27 est. by -1%/+4%, and raise our SOTP based TP to Rs218 based on target P/B of 1.25x and subs value of Rs9/share. Post 17% correction in stock price from the peak, risk-reward is favourable, and we **upgrade our rating to BUY**.

Company update

CMP	**Rs180**
12-mth TP (Rs)	**218 (21%)**
Market cap (US$m)	**4,390**
Bloomberg	**FB IN**
Sector	**Banking & Fin**

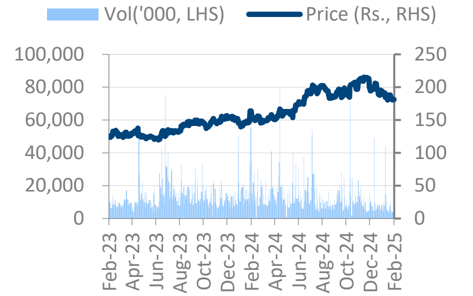
Shareholding pattern (%)

Promoters	0.0
Pledged (as % of promoter share)	0.0
FII	28.6
DII	45.4
52Wk High/Low (Rs)	215/145
Shares o/s (m)	2454
Del Value 3mth avg (US$ m)	9.3
Dividend yield FY26ii (%)	1.1
Free float (%)	100.0

Price performance (%)

	1M	3M	1Y
Absolute (Rs)	-6.5	-14.6	18.0
Absolute (US$)	-6.6	-16.8	12.9
Relative Perf.	0.0	-6.0	15.3
Cagr (%)		**3 yrs**	**5 yrs**
EPS (Rs)		26.7	20.9

Stock performance



Financial summary (Rs bn)

Y/e 31 Mar, Parent	FY23A	FY24A	FY25ii	FY26ii	FY27ii
NII	72	83	96	107	125
PPOP	48	52	62	68	83
Reported PAT	**30**	**37**	**40**	**43**	**52**
EPS (Rs)	14.3	16.2	16.8	17.6	21.3
Growth (%)	54.8	13.8	3.5	5.0	20.9
IIFL vs consensus (%)			1.4	(7.9)	(5.2)
Core PER (x)	12.3	11.3	10.6	9.7	8.0
Book value (Rs)	102	127	134	150	169
Core PB (x)	**1.8**	**1.5**	**1.3**	**1.2**	**1.0**
CAR (%)	14.8	16.1	15.1	14.9	15.0
ROA (%)	1.3	1.3	1.2	1.2	1.3
ROE (%)	**14.9**	**14.7**	**12.9**	**12.4**	**13.4**

Source: Company, IIFL Research. Priced as on 21 February 2025

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Key takeaways from the analyst day

- **Aspires for the Top 5 Private bank bracket with PAN India presence:** K.V.S. Manian, the recently appointed CEO, and the senior management team articulated the new strategy for the Federal Bank (FB). Under Breakthrough 4.0 journey, the bank intends to build onto its strength, modernize and become a truly national universal bank. In its pursuit of becoming a universal bank, FB intends to organically and/or inorganically build MFI, asset and wealth management, affordable housing, securities/capital market services and investment banking businesses. FB intends to mainly focus on the four pillars viz. a) Expand NR deposit franchise (where it is already dominant) outside of Kerala and GCC, b) Win in mass affluent banking by offering wealth management, capital markets and premium savings solution, c) Become SME bank of choice and d) Focus on mid-corporate banking. FB intends to focus on profitable and capital efficient growth, take optimum risks and deliver superior earnings quality.

- **Improvement in the liability franchise to do heavy lifting of margins …** FB expects to improve NIMs by 70-80bps, mainly led by liability led initiatives (~45-50bps) rather than aggressive foray into higher yielding loan segments (~25-30bps). It has guided CASA ratio to improve 6ppt (+4ppt led by CA) to 36%, led by strengthening non-resident (NR) proposition beyond GCC and Kerala diaspora, expand CA offering (IPO, ASBA, PACB) and expand RM coverage (specifically for corporate salary). We concur with the management's strategy of driving structural improvement by working on liability franchise rather than taking undue lending risks. However, given the competitive deposit landscape, relatively older customer cohort (which may result in slower take-off of capital market offerings, and hence the resultant fees and float), stiff competition and low brand awareness outside the home market (FB may have a better right-to-win in Tier2 and beyond markets vs. metros) and inherent difficulty in mobilizing low-cost CASA, we think the benefits may manifest only over the longer-term. We forecast a flat CASA ratio of 30% until FY27, and thus a better than expected execution can drive an upside to our margins forecast.

- **… and further aided by increase in share of medium-yield loans and calibrated deepening of high-yield loans.** FB does not see the current environment fit for growth in very high yielding segments (expects to raise the share by 1ppt to 3%) and instead wants to focus more on medium yielding loans (expects to raise the share by 3ppt to 34%), thereby bringing down share of low yielding loans by 6ppt to 58%. The focus will also be on mid-market corporate lending vs. large corporates for better profitability. It expects the change in loan mix to drive loan yields higher by 25-30bps. With a higher share of floating rate loans (~70%, of which repo-linked is 50%) amid the rate-cuts and a slower growth in very high yielding loan segments, we forecast NIMs to decline 6bps yoy in FY26 and start improving only from FY27 onwards (+5bps yoy). Our NIM forecast is thus quite conservative vs. the management guidance.

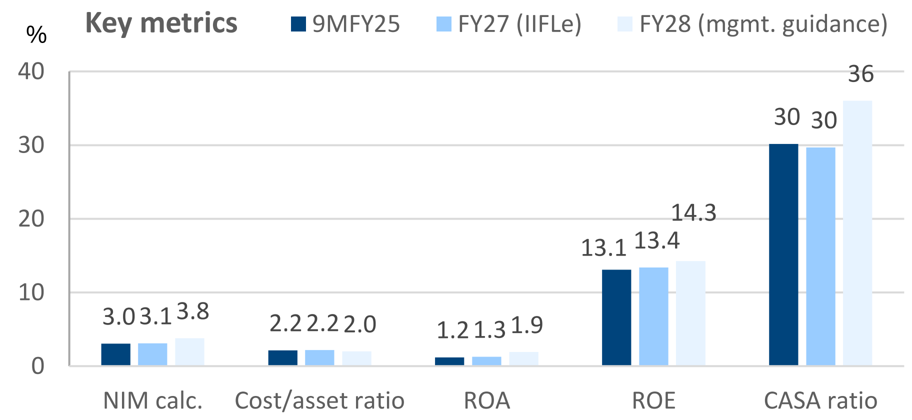
- **Expanding product portfolio and improving fee income growth to be key earning levers:** Bank plans to scale up share in its used vehicle business which shall be yield accretive. It also plans to add new products like – Micro LAP, tractor, unsecured business loans (mainly a cross-sell product for ETB customers), affordable housing and real estate financing, which should improve yields over medium term. The management acknowledged slower fee income growth and is looking to shore it up by looking for opportunities across 1) trade and forex, 2) wealth management and bancassurance, 3) credit card and 4) Cash Management Services via product co-origination or cross-selling. FB expects to improve fee income to avg. asset ratio by ~45 bps from 0.9% as on 9MFY25. We have built a fee income/avg. asset ratio of only 1% in FY27E.

- **Open more branches in the next 3-years than the cumulative addition in last decade; coupled with branch transformation:** FB intends to open 400-450 new branches till FY28 vis-à-vis 375 net branch addition from FY14, which will take it to ~2,000 branches by FY28 (i.e. like Kotak Bank currently). The bulk of these additions are going to happen outside Kerala, with a focus on tier-2 cities within high GDP states and a pin-code level strategy in metros. Bank intends to "free the branch" by centralizing tasks to remove redundancies, deployment of specialized teams to expand sales and distribution capacity and making the branch managers accountable for business growth, customer engagement and market expansion. The Bank has identified / hired a key person to head this role.

- **Focus on digital distribution to improve organic sourcing; cost optimization to be far more gradual:** FB plans to focus more on organic sourcing and reduce its dependency on partners especially for digital saving deposits (from 2% organic to 25%) and credit cards (from 30 to 45%). Although this shall entail higher costs in the near-term, the bank expects to reap benefits in the long run. FB intends to optimize cost by enhancing productivity (new scorecards), introducing centralized processing and leveraging its subsidiary Fedserv to reduce the cost of operations. As the bank continues to invest in the franchise (launch new businesses, open more branches, revamp the mobile app and in-source tech), we do not build any cost benefits – our FY27E cost/avg. asset ratio is flat vs. the management guidance of ~15bps improvement until FY28E.

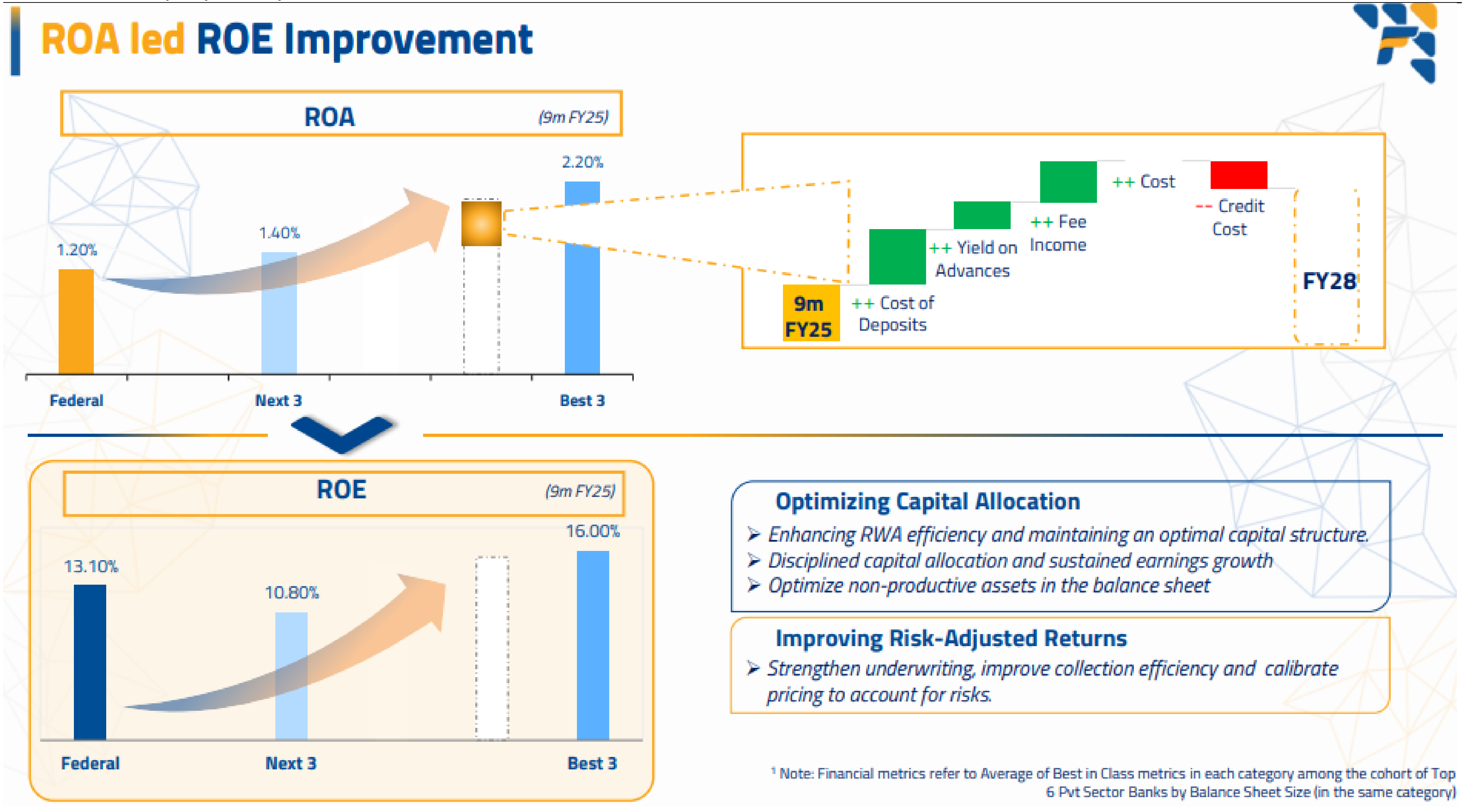
- **RoA improvement of 70-80bps till FY28E too ambitious, but even a partial delivery should suffice for stock price re-rating:** The bank aspires for 70-80bps RoA improvement in next three years led by the strategy of higher NII (higher CASA, lower COF and better yields) and fee income growth (higher cross sell and more transaction banking related income), partly offset by a rise in credit costs. Banks Top three priorities include CASA, NIM and fee income. We like the banks' strategy but believe the ROA target of 70-80bps improvement (to 1.8-1.9%) in the next three years is too ambitious. We think that FB could potentially look to raise capital in the next 12-24 months, given that Tier1 ratio (after including 9MFY25 profits) is ~15.3%. Having said that, even if FB is able to deliver only 20-30bps ROA improvement from current levels and reach 1.4-1.5% ROA and 14-14.5% ROE, the stock could potentially get re-rated by 20-30% to 1.4-1.5x P/B vs. current 1-year core forward P/B of 1.14x. Our SOTP based TP of Rs218 (implying 21% upside) is based on core target P/B multiple of 1.25x (vs. 1-year forward P/B of 1.14x) and subs valued at Rs9/share.

Figure 1: IIFL forecasts are quite conservative vs. management target (we think it is too ambitious) for key financial metrics, and thus the stock price may offer additional upside if the management is able to deliver on its targets



Source: Company, IIFL Research. Note: FY28 management guidance shown in the above chart is based on some approximations based on the analyst presentation.

Figure 2: Federal Bank is targeting RoA improvement of nearly 70-80bps over the next 3 years driven by improvement in Cost of deposits, yield on advances and fee income, stable cost ratios, which will be partly offset by some rise in credit cost



Source: Company, IIFL Research

Figure 3: DuPont analysis and key metrics

DuPont analysis (% of avg. assets)	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24	FY25ii	FY26ii	FY27ii
Interest income	8.9	8.4	7.7	7.7	7.8	7.2	6.5	7.0	7.8	8.2	8.0	7.9
Interest expense	6.0	5.5	4.9	4.9	5.0	4.3	3.6	4.0	4.9	5.2	5.1	4.9
Net interest income	**2.9**	**3.0**	**2.8**	**2.8**	**2.7**	**2.9**	**2.8**	**3.0**	**2.9**	**2.9**	**2.9**	**3.0**
Fee Income	0.6	0.7	0.6	0.7	0.7	0.6	0.7	0.9	0.9	0.9	0.9	1.0
Trading Profits	0.1	0.3	0.2	0.2	0.4	0.3	0.2	0.0	0.1	0.1	0.1	0.1
Other income	0.1	0.1	0.1	0.1	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Total non-interest income	0.9	1.0	0.9	0.9	1.1	1.0	1.0	1.0	1.1	1.1	1.1	1.2
Total revenue	**3.8**	**4.0**	**3.7**	**3.7**	**3.9**	**3.9**	**3.8**	**4.0**	**4.0**	**4.1**	**4.1**	**4.2**
Employee expense	1.2	1.1	1.0	0.9	1.0	1.1	1.1	0.9	1.0	1.0	0.9	0.9
Other expense	0.9	1.0	1.0	0.9	0.9	0.9	0.9	1.1	1.2	1.2	1.3	1.2
Total expenses	**2.2**	**2.1**	**1.9**	**1.9**	**2.0**	**1.9**	**2.0**	**2.0**	**2.2**	**2.2**	**2.2**	**2.2**
Pre-provision operating profit	**1.6**	**1.9**	**1.8**	**1.9**	**1.9**	**2.0**	**1.8**	**2.0**	**1.8**	**1.9**	**1.9**	**2.0**
Provisions	0.8	0.6	0.7	0.6	0.7	0.8	0.6	0.3	0.1	0.3	0.3	0.3
Profit before tax	0.8	1.3	1.1	1.3	1.2	1.1	1.2	1.7	1.8	1.6	1.6	1.7
Taxes	0.3	0.5	0.4	0.4	0.3	0.3	0.3	0.4	0.4	0.4	0.4	0.4
ROA	**0.5**	**0.8**	**0.7**	**0.8**	**0.9**	**0.8**	**0.9**	**1.3**	**1.3**	**1.2**	**1.2**	**1.3**
Leverage	11.0	12.1	12.0	11.7	12.2	12.5	12.1	11.9	11.2	10.5	10.5	10.7
ROE	**6.0**	**9.8**	**8.3**	**9.8**	**11.1**	**10.4**	**10.8**	**14.9**	**14.7**	**12.9**	**12.4**	**13.4**

Key metrics												
Loan growth	13	26	25	20	11	8	10	20	20	13	15	15
Deposit growth	12	23	15	21	13	13	5	17	18	8	14	14
Credit-deposit ratio	73	75	82	82	80	76	80	82	83	87	87	88
Yield on IEA	9.5	8.9	8.1	8.0	8.2	7.7	6.9	7.5	8.4	8.6	8.3	8.1
Cost of funds	6.8	6.1	5.4	5.4	5.6	4.8	4.1	4.5	5.5	6.0	5.8	5.6
NIM	**3.1**	**3.1**	**3.0**	**2.9**	**2.9**	**3.1**	**3.0**	**3.2**	**3.1**	**3.1**	**3.0**	**3.1**
Cost-to-income ratio	56.9	53.1	51.7	50.0	51.3	49.7	53.3	49.9	54.5	53.7	54.3	52.2
GNPA ratio	2.8	2.3	3.0	2.9	2.8	3.4	2.8	2.4	2.1	1.8	1.9	2.0
NNPA ratio	1.6	1.3	1.7	1.5	1.3	1.2	1.0	0.7	0.6	0.4	0.5	0.5
Credit cost	**1.3**	**0.9**	**1.1**	**0.8**	**1.0**	**1.3**	**0.9**	**0.5**	**0.1**	**0.4**	**0.4**	**0.4**
CET1 ratio	**13.4**	**11.8**	**14.2**	**13.4**	**13.3**	**13.8**	**14.4**	**13.0**	**14.6**	**13.9**	**13.7**	**13.8**
PAT growth	-52.7	74.7	5.8	41.5	24.0	3.1	18.8	59.3	23.6	7.2	8.6	20.9

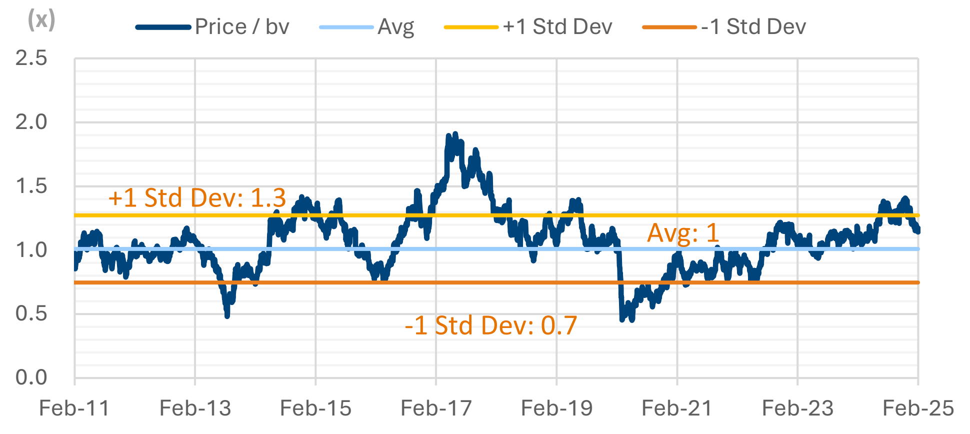
Source: Company, IIFL Research

Figure 4: Federal Bank SOTP – FY27 based

Particular	Stake	Value (INR bn)	Value (USD bn)	Value/ Sh. (INR)	% of total	Target Multiple (x)	Rationale
Federal Bank*		**510**	**6.1**	**210**	**96**	**1.3**	**PABV**
Key Ventures							
Feedback financial services	61.2	26	0.3	11	5.0	1.4	PBV
Total Value of Ventures		**26**	**0.3**	**11**	**5.0**		
Less: 20% holding discount		5	0.1	2	1.0		
Value of Key Ventures		**21**	**0.3**	**9**	**4.0**		
SOTP		**532**	**6.4**	**218**	**100**		
CMP				180			
Upside - %				**21**			

Source: IIFL Research. Note: *BV adjusted for investment in subsidiaries

Figure 5: Federal Bank is trading at 1.14x 1FY core P/B (13% above its LTA)



Source: Bloomberg, IIFL Research

Figure 6: Summary of Federal Bank's Project breakthrough 4.0 plan with detailed synopsis of 12 themes envisaged in the analyst meet

Sr. No.	Theme	Action Plan	Financial target
1	NIM Improvement	**Part I: Liabilities/Deposits** a) Reorient Branch Strategy towards CASA & Deposit b) Strengthening CA Portfolio c) Enhance engagement with capital markets d) Enhance NR Beyond the GCC and Kerala e) Segmental propositions to enhance engagement f) Granular focus **Part II: Advances/ Assets** a) Scaling up Medium-Yield Assets b) Mid-Market Corporate Lending for Better Profitability c) Leveraging Priority Sector Lending (PSL) Strategy d) Deepening High-Yield Assets e) Optimized Risk-Based Pricing Strategy	**Part I: Liabilities/Deposits** a) Improving CASA ratio from 30% in FY25E to 36% by FY28E b) Improving CA as % of total deposit share from 6% in FY25E to 10% by FY28E c) Reducing Interest exp to avg. earning assets by 45-50bps from 5.6% as on 9MFY25 **Part II: Advances/ Assets** a) Changing advances mix - i) decreasing share of low yielding advances from 64% to 58%, ii) increasing share of medium yielding advances from 31% to 34%, iii) increasing share of high yielding advances from 3% to 5% and iv) increasing share of very high yielding advances from 2% to 3% b) Increasing Interest inc to avg. earning assets by 25-30bps from 8.74% as on 9MFY25 **Consequentially bank expects NIM to improve by 70-80bps from 3.13% as on 9MFY25**
2	Expanding Product Portfolio	Bank plans to expand current and also enter new products namely: a) investment products: Wealth Management, 3 in 1 account, Bespoke solutions to NR b) Scale-up Used Vehicle Finance – CV/CE , Car Loans c) Expand offerings for Micro-LAP Products d) Tractor Finance e) EMI-Based Unsecured Biz Loans f) Affordable Housing Loans g) Real Estate Finance h) Sustainable Finance i) Correspondent Banking j) Syndication & Investment Banking k) Capital Market Services Business	

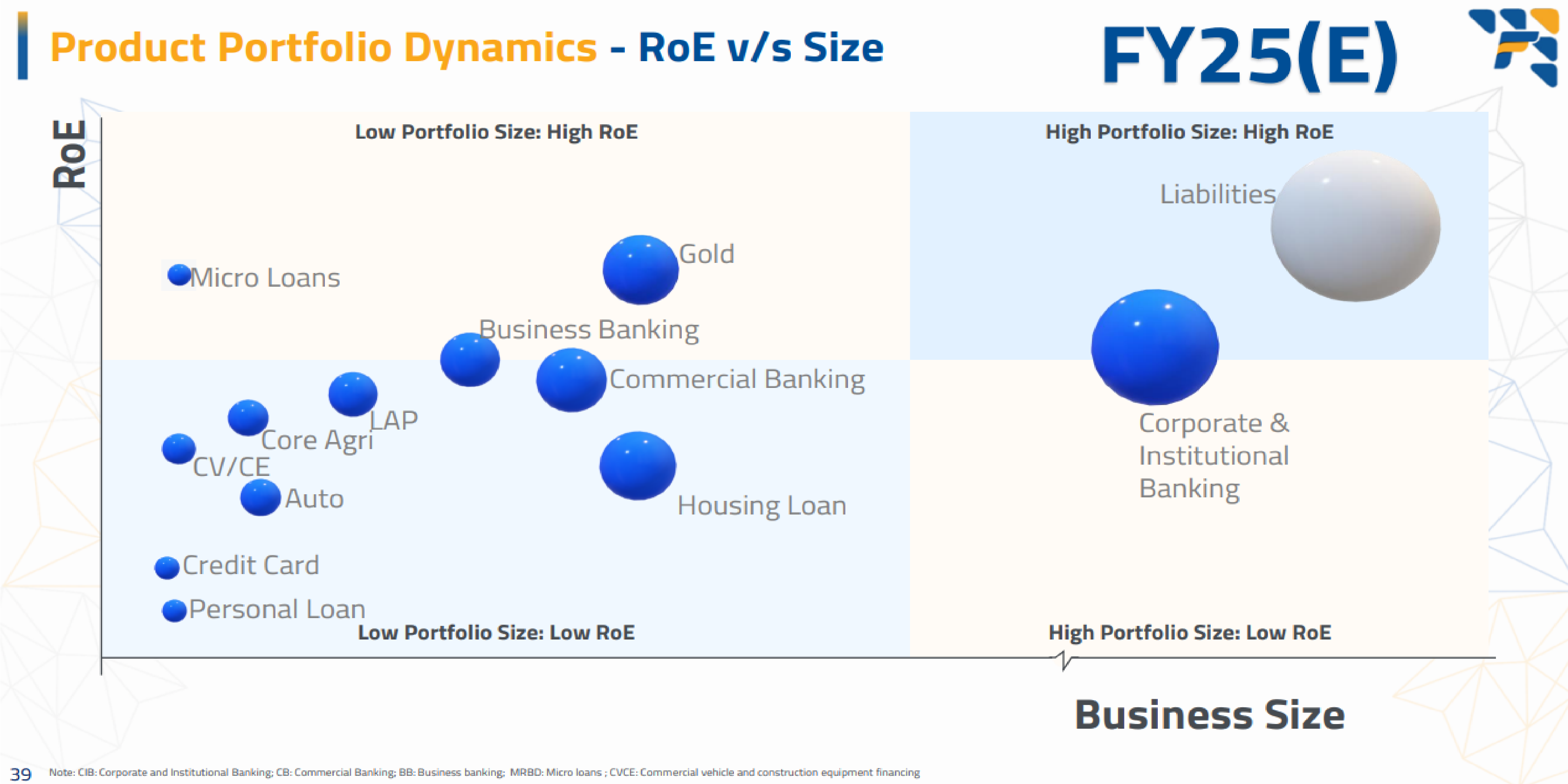
Sr. No.	Theme	Action Plan	Financial target
3	Fee Enhancement	Key Opportunities for fee enhancement are: a) Trade and Forex Income, b) Wealth Management & Bancassurance, c) Credit Cards & Acquiring Businesses and d) Cash Management Services mainly through a) Product Co-origination and b) Cross selling	Increasing other income to avg. assets ratio by ~45bps from current 1.1% as on 9MFY25
4	Branch Strategy for Scalable Growth	Bank plans to expand the network outside the legacy states using the following strategy: a) Selective State level expansion, b) Focus on top 10 high GSDP states, c) Focus on tier-2 cities and d) Pin code level strategies in Metros	Adding 400-450 branches till FY28 from current 1,550 branches as on 9MFY25 which shall take it closer to scale of next 3 best banks after best 3 banks
5	Branch Transformation	**I) "FREE The Branch" Initiative using -** a) Modernized Branch Formats, b) Expanding Sales & Distribution Capacity, c) Elevating the Branch Manager's Role and d) Digitization **II) Strategic Framework for Operational Efficiency by** a) Removing inefficiencies, b) Leveraging digital tools, c) Shifting routine tasks to centralized hubs, d) Structuring regional support for agility and market alignment and e) creating centres of excellence to harness expertise and innovation	
6	Brand Transformation	Transforming the brand via - a) Brand Ambassador & ATL Campaign, b) Redesign the Brand & Branches, c) Reinforce Loyalty in Home Market, d) Put in place a full NPS System, e) Contemporize for new gen clients, f) Redefine Legacy Perceptions, g) Brand Salience Outside Home Market and h) Positioning to Small Biz. & Mass Affluent Segments	

Sr. No.	Theme	Action Plan	Financial target
7	Digital At The Fore, Human At The Core	**Part I: Enhance User experience with the following** a) Mobile Revamp and Omni-Channel Experience, b) Gen AI Chatbots, c) Wealth Management Solutions and d) Corporate/ SME Portal Services **Part II: Employee enablement via** a) Enhanced Branch Interface, b) Regulatory & Compliance bots, c) HRMS Solution (Cloud), d) Unified Account Opening, e) Loan Origination System, f) AI-Assisted Decision Support, g) Virtual Agent Assist, h) Process Digitization & Workflow Automation and i) Learning & Development via Digital Platforms	
8	Renewed Digital Distribution Strategy	**I) Credit Cards:** a) Focus on faster growth of organic credit cards through our own digital channels, b) Rationalize commercials with co-branded partners and c) Establish Bank primacy in ownership of brand **II) Personal Loans:** a) Multiple partnerships to diversify sourcing, b) Enhance own digital distribution capabilities, c) Refine the digital workflows to enable plug and play and d) Revise partnership commercials to restrict to distribution model **III) Savings account:** Focus on Gen Z growth through scaling up our own digital acquisition as well as through strategic partnerships, driving higher AMB, enhanced cross-sell and optimized commercial arrangements	I) Reduce the share of partner sourced credit cards from 70% as on FY24 to 55% by FY28E II) Increase the share of partner sourced in PL from 40% in FY24 to 50% by FY28E III) Reduce the share of partner sourced savings accounts from 95% as on FY24 to 75% by FY28E
9	People & Culture	Bank wants to empower leadership via: a) Vertical Heads as CEOs, b) Fostering alertness, agility, and astuteness at all levels, c) Enhance Sales Culture, d) Setting up an Alternate Low-Cost Channel, e) Collective focus on P/L, f) Making the BM role attractive, g) Generalists V/s Specialists and h) Identify Talent Gaps to improve capabilities	
10	Cost Optimization	Bank aims to achieve cost optimisation by: a) Enhancing Productivity b) Introducing a low-cost sales channel c) Leveraging its subsidiary Fedserv d) Centralizing/Regionalizing Processes e) using AI and Automation f) Cost Rationalization	a) Improving cost to avg assets by ~15bps from 2.15% as on 9MFY25 b) Improving cost to income ratio by 2-3ppt from 53.11% as on 9MFY25

Sr. No.	Theme	Action Plan	Financial target
11	Strengthening Assurance Functions	**a) Compliance -** Optimize SAS Continuous Compliance Monitoring, AI Driven Validation of Policies for Regulatory Edits and Digitize Enterprise Risk Management **b) Risk Management -** Institute a better RAROC based pricing mode and robust transfer pricing methodology, Using AI, ML, and Analytics for Better Risk Management and Smooth Transition to ECL-Based Provisioning **c) Audit -** Maximize Process Automation, Integrated Zonal Audit, Continuous Control Monitoring (CCM) and Develop In-House IS Auditing Capability	
12	Journey towards a Universal Bank	Diversifying Financial Services for Creating a Holistic Franchise: Growth either organically or inorganically for - a) Microfinance, b) Asset Management, c) Wealth Management, d) Affordable housing, e) Securities & Capital Market Services and f) Investment banking	

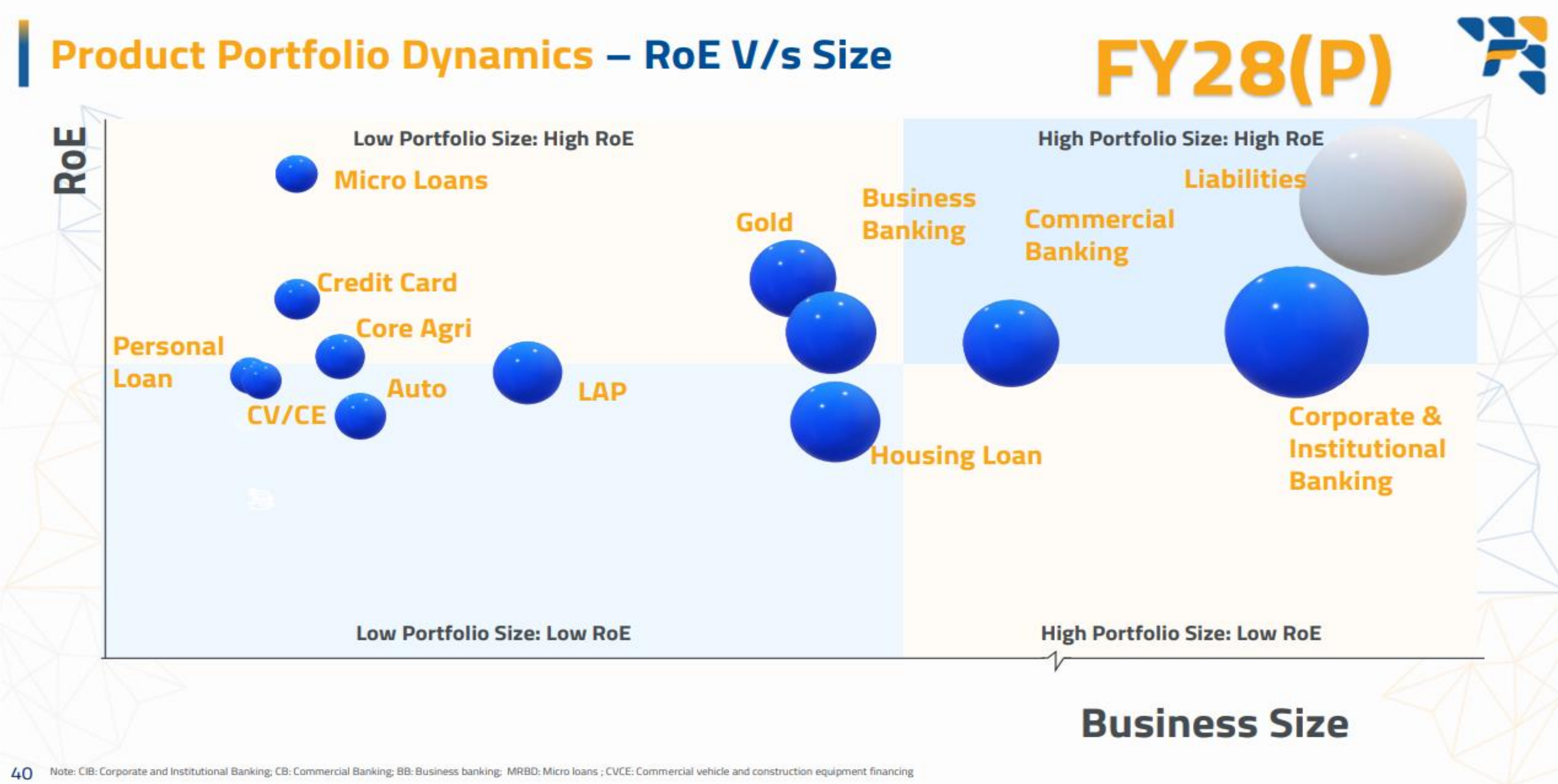
Source: Company, IIFL Research

Figure 7: Federal Bank current portfolio dynamics



Source: Company, IIFL Research

Figure 8: Federal Bank expected portfolio dynamics



Source: Company, IIFL Research

Figure 9: Detailed review of key business segments, expansion levers, enhancement areas and key initiatives to be undertaken by Federal Bank

Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Branch Banking		• Strong brand presence in home market • Customer-centric service culture ensuring high retention • Diverse product suite catering to retail banking needs • High employee engagement and growth-oriented culture	• Geographic expansion into high-GSDP states and Tier-2 cities • Pin-code based strategies for metros • Unlocking potential within the existing client base • Enhancing fee income through Forex and Wealth Management	• Expanding liability business share in ex-home markets • Introducing dedicated sales teams at branches to enhance business acquisition • Accelerating branch transformation into sales and service hubs with digital integration	• Free the Branch Centralize and Regionalize • Transform Operations Sales & Service architecture • Enhance people capabilities Pervasive growth-oriented culture
Deposits	Business size – Rs 2,658 Bn Customer count – 17.3+ mn	• Strong relationship-driven approach fostering customer loyalty • Low employee attrition, ensuring service continuity • Market prominence in NR (home market) and cross-border remittances • Robust onboarding and servicing framework through digital channels	• Growth opportunities in mass affluent segment • Enhancing digital onboarding to increase penetration • Customized solutions to cater to diverse customer segments • Opportunity to expand Govt & retail institutional CASA • Distribution expansion through branches and alternate channels	• Strengthening integration with capital markets and investment offerings • Enhancing RM-to-customer coverage for improved engagement • Expanding Feet-on-Street efforts to drive CASA growth • Enhancing brand visibility in emerging and non-core market	• Strengthen NR proposition • Increase share of digital on-boarding • Develop co-origination • Expand CA offerings • Improve and expand RM coverage • Leverage Analytics for Growth
Wealth & Insurance Distribution		• Robust partner ecosystem and streamlined processes for insurance distribution • Extensive coverage with a skilled sales force certified in insurance advisory	• Large untapped customer base • Enhancing digital penetration in Banca sourcing • Increasing customer stickiness and driving SA balance growth through SIPs, 3-in-1 accounts, and NPS integrations	• Enhancing digital platforms for Wealth Management Services and 3-in-1 (e-Trade) accounts • Strengthening in-house wealth management capabilities	• Enhance Product co-origination and cross-sell • Accelerate 3-in-1 Account & Investment Growth • Enhance Wealth Management Proposition for Affluent • Optimize RM coverage and capabilities • Expand Digital Wealth Offerings for Mass Affluent

Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Credit Card	Business size – Rs 36 Bn Customer count - 1.1+ mn	• Superior digital onboarding experience • Differentiated product suite tailored to diverse customer segments	• Enhanced opportunities for co-origination and cross-selling • Enhanced digital origination organically and through partners	• Opportunity to scale in a competitive market • Expanding expertise in unsecured lending (advanced analytics, precision underwriting and optimized collections) • Refining customer ownership framework under fintech partnerships	• Expand Distribution & Market Reach • Increase share of digital on-boarding • Drive Income Growth Through Optimized Spend Strategies • Leverage AI & Analytics for Smarter Decision Making • Enhance Product Suite & Customer Retention • Deploy Data-Led Profile-Based Sourcing Models
Personal Loans	Business size – Rs 38 Bn Customer count - 0.2+ mn	• Fully digital customer onboarding process • Strong liability customer base providing opportunities for preapproved offers	• Well-established branch network and RM channel to drive growth • Opportunity to leverage Credit Line on UPI for expansion • Leverage digital channels for on-boarding organically and through partners	• Opportunity to enhance sourcing from NTB customers • Scope to scale up pre-approved PL base • Potential to establish a dedicated sourcing team	• Broaden partnerships • Leverage Branch relationship / RM network • Launch Credit on UPI • Develop co-origination journeys
Auto Loans	Business size – Rs 85 Bn Customer count - 83,600+	• Industry-leading delinquency levels, ensuring strong asset quality • Sustained 25%+ YoY portfolio growth, demonstrating robust demand • Dedicated sourcing team and DSA network for effective distribution • Straight Through Processing for seamless new car loan approvals	• Rising income and urbanization driving fresh demand • Increasing market for used car financing • Growth potential in refinance and loan-against-car segments • Emerging opportunity in green auto loans	• Opportunity to reduce branch dependency and optimize operational costs • Scope to expand geographic presence in underpenetrated markets • Scaling used car financing to capture a larger market share	• Scale-up used car financing • Expand Loan Against Car product • Increase Co-Origination of Credit Card & Savings account • Expand distribution • Enhance digitization & STP adoption • Centralize underwriting and collections • Develop sustainable finance

Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Loan Against Property	Business size – Rs 137 Bn Customer count - 33,000+	• Secured lending offering an optimal risk-reward balance • Dedicated sourcing team and established DSA channel for efficient acquisition	• Growth potential in markets beyond the existing footprint • Opportunity to upsell to existing home loan customers, optimizing acquisition costs • Self-employed segment - use case for leveraging property for business expansion or asset creation	• Digitize credit assessment processes for enhanced efficiency • Expand distribution capacity and capabilities through alternate channels • Leveraging cross-sell opportunities to enhance profitability	• Digitized customer journeys • Enhance Sales Structure in ex-home markets • Strengthen Fee Based Income Opportunities • Recalibrate distribution strategy • Scaling up Retail Loan Service Centers • Develop alternate/surrogate credit assessment frameworks • Optimize collection strategies
Housing Loans	Business size – Rs 295 Bn Customer count - 85,000+	• Low credit cost and capital consumption, ensuring profitability • Dedicated and structured sourcing team for efficient acquisition • High-retention product with strong potential customer profitability	• Urbanization trends driving sustained housing demand • Long-term customer relationships enabling higher cross-sell potential • Strengthening cross-sell initiatives to enhance customer lifetime value	• Opportunity to expand presence in underpenetrated geographies • Scope to optimize operational efficiency and reduce branch dependency • Diversifying sourcing channels beyond the DSA model for cost efficiency • Strategic focus on optimizing liquidity impact from long-tenure, lowyield loans	• Explore affordable housing • Implement end-to-end digitization • Increase Co-Origination of Credit Card & Savings account • Expand Retail Loan Service Centers • Strengthen direct sourcing through builder channel • Enhance self-employed and NRI offerings • Scale up Sales team pan India

Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Business Banking	Business size – Rs 189 Bn Customer count - 26,000+	• Granular portfolio with an average ticket size of ₹1 Cr, highly collateralized and PSL-oriented • Optimal working capital mix ensuring portfolio stability • Prudent underwriting with low credit costs.	• Opportunities in higher-yielding segments with managed risk • Customized solutions for key industry sectors • Introduction of Business Installment Loans • Geographic expansion to untapped markets	• Scope to optimize TAT to align with industry benchmarks • Opportunity to improve trade & forex revenues • Enhancing digital capabilities to improve efficiency and customer experience • Improving CA-to-asset ratio • Strengthening small-value loan disbursement, given its high ROE	• Better-Yield Lending for Profitable Growth • Digital Lending for Scale & Speed • Proactive Risk Mitigation with Advanced Collections • Forex & Trade Finance Optimization for Revenue Growth • Distribution enhancement through dedicated business banking RMs • Sectoral Diversification to Future-Proof Growth • TAT Optimization with Process Automation & AI
Corporate & Institutional Banking	Business size – Rs 824 Bn Customer count - 1,500+	• Comprehensive product suite catering to diverse corporate needs • Expanding market presence, reinforcing industry positioning • Strong asset quality, ensuring portfolio resilience • Presence in GIFT City, unlocking international business opportunities	• Enhancing Digital offerings for Trade, Transaction & Supply Chain • Improving CA mix in overall Liability book • Increase wallet share across Trade, Transaction & Treasury • Sectoral focus approach	• Enhancing NFB to FB ratio with increased Trade focus • Strengthening Self-funding and focus on Liability sourcing • Scaling presence in Capital Markets • Expanding Syndication and Debt Capital Market capabilities • Thrust on corporate salary sourcing from large corporates	• Accelerate Digital Banking • Expand Capital Market Business • MNC & Correspondent Banking • Mid-Market Focus • Source & Down sell Model for Revenue Growth • Bespoke Corporate Banking Solutions

Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Commercial Banking	Business size – Rs 263 Bn Customer count - 3,000+	• Granular asset book supporting portfolio stability • Sole Banking relationships with ~67% of clients • Extensive geographic penetration - enabling wider market reach • Consistently improving asset quality & strengthening risk metrics	• Significant market potential in deeper geographies. • PSL growth opportunities with a focused approach on SME • Ecosystem Banking expansion (including SCM opportunities) • Wholesale liability team for increased deposit mobilization	• Enhancing wallet share in Trade, Transaction & Treasury products • Optimizing onboarding processes to improve turnaround time • Comprehensive & Customized Digital solutions for Clients • Use of Analytics for deepening and widening of product base	• Deeper Geography Penetration • Enhance Credit Delivery & Risk Management • Self-Funding & Liquidity • Accelerate Digital Transformation • Scale Supply Chain Finance • Expand Client Servicing Centers
Treasury		• Strong presence with Exchange Houses, CSGL and Arbitrage products • Market leader in Exchange traded volumes, reinforcing competitive positioning • Advanced analytics-driven approach, enhancing decision-making & risk management • Handle significant FX volume in Personal Inward remittances	• New product development – Structured options, IRO hedging etc. • Expanding proprietary trading – Options/swaps, MIFOR book running • Leveraging analytics driven trading strategies • Deepening products & revenue with Wholesale clients	• Expanding investment offerings across wealth clients • Broaden Wholesale client base by expanding product offer & Wallet share • Strengthening Retail Trade & Forex solutions to capture untapped demand	• Expanding GIFT Capabilities • Strengthening Retail Trade & Forex • Expand Product & Trading Strategies • Diversified Resource Mobilization • Optimizing NSLR Debt Strategy • Advancing Correspondent Banking
Government & Institutional Business	Business size – Rs 122 Bn	• Strong technological capabilities to support digital integrations and rollouts • Synergy with branches and expanding network for deeper penetration • Established reputation, brand and trust	• Rising government expenditure driving new business opportunities • Empaneled with CBDT & CBEC for Tax collection • Empaneled for Agency business with various states • Non agency business with Central and State Government.	• Sharpen focus on Institutions / TASC accounts • Developing bespoke solutions and tailored financial products for government entities • Building expertise in niche government segments to drive specialized offerings	• Expand State Government Agency Business • Focus on Local Authorities • Enhance e-Treasury Integration • Customised Digital Products • Enhance Government Partnerships • Centralised Fund Management

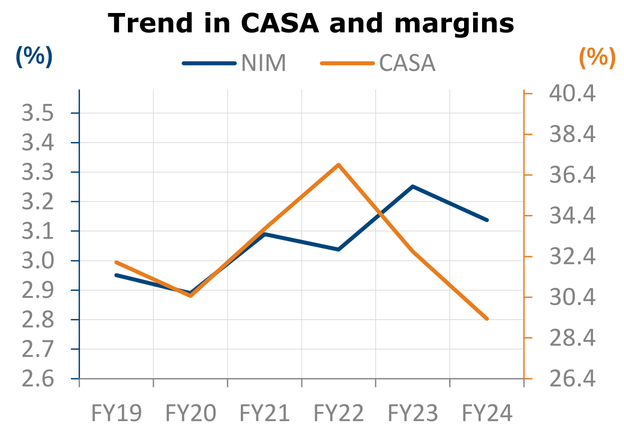
Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Gold Business	Business size – Rs 314 Bn Gold Tonnage - 65+ tonnes	• Largest gold loan portfolio amongst private sector banks • High ROE Business with high fee income & profitability. • Extensive branch expertise driving strong execution capabilities • Low RWA, ensuring optimal capital utilization	• Branch network expansion into high-potential gold loan markets • Formalization trend shifting customers from unorganized to organized lenders. • Innovative product offerings to cater to evolving customer needs • Thrust on cross-sell and upsell.	• Enhancing operational efficiency through digitization and lean processes. • Diversifying acquisition channels beyond branch-led sourcing to drive scale • Use of Analytics for deeper and wider customer penetration	• Innovation Cell • Gold Loan 3.0 Implementation • Market Expansion • Fee Focus • Streamline Operations • Branding and Marketing
Inclusive Finance	Business size – Rs 41 Bn	• 20+ BC Partners, 900+ BC branches across 20 states & 2 UTs, ensuring deep market penetration • 1.35M+ customer base with strong growth potential (~98% Women and ~66% Rural) • High-yielding portfolio with high risk adjusted return	• Untapped liability business presenting growth opportunities • 12Tn+ addressable market across SHG, Micro & AFHL segments • MFI lending recalibration towards individual lending models • Emergence of a Unified Lending Interface for seamless integration & customer experience	• Optimizing cost structure to enhance operational efficiency • Strengthening provisioning norms to realign to business cyclicality • Reducing dependency on Agency channels by expanding direct sourcing models – SHG/ Individual loans • Increase digital collections to lower cash-handling risks	• Digital Transformation • BC Outlets Expansion • Product Innovation • Customer Journey & Growth • Diversification Strategy • Full Product Suite

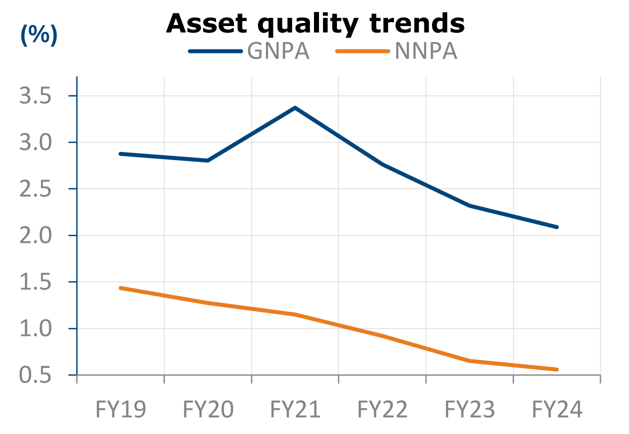
Product	Business size and customers	Strategic Advantages	Expansion Levers	Enhancement Areas	Initiatives
Agri Business	Business size – Rs 81 Bn	• 80% PSL portfolio • Expanding customer base- 1 lac+ unique customers • Robust digital platform facilitating small-ticket Agri loans • Wide distribution through branch network & partnerships	• Scaling digital platforms & product innovation for broader market reach • Strengthening partnerships to enhance distribution and scale. • Leveraging the Unified Agri Lending Stack for seamless credit delivery • Enhancing ETB/NTB borrower engagement to drive higher PPC	• Portfolio optimization strategies to improve repayment trends in legacy accounts • Developing region-specific Agri solutions to align with diverse market needs • More comprehensive product offer – ENWR & Post harvest financing option • Leverage Priority Sector opportunities	• Accelerate Digital Transformation & Automation • Expand Market Reach & Distribution • Unified Lending Interface • Product Customization • Expand Agri Supply Chain & Ecosystem
CV/CE	Business size – Rs 42 Bn	• Strong brand & leveraging existing customer base • Robust distribution Through RMs, Branches and DSAs • PSL opportunities - ~80% qualifies as PSL • PAN India presence	• Focus on used CV/ CE • Distribution – Deeper Geography penetration – T2 & T3 • Deeper Penetration of existing customer base • Line of Credit to Strategic & Corporate Clients	• Rollout Tractor Financing • New Product rollouts – Green / Balance Transfer • Expand distribution through CLM • Thrust on Cross Sell/ Upsell – Working Capital, Liability & Insurance products	• Expand Distribution & Market Penetration • Optimize Credit Delivery & Risk Management • Scale ETB & NTB Client Base • Drive Yield Optimization & Profitability • Strengthen Branding & Market Positioning

Background: Federal Bank Limited is a major Indian commercial bank in the private sector headquartered at Aluva, Kerala having >15,000 employees, spread over 1,504 branches as of FY24. The history of Federal Bank dates back to the pre-independence era. It was initially known as the Travancore Federal Bank, later gradually transformed into a full-fledged bank under the able leadership of its Founder, Mr. K P Hormis. The name Federal Bank Limited was officially announced in the year 1947 with its headquarters nestled on the banks of the river Periyar. As at the end of FY24, bank had a balance sheet of Rs 3.1tn, with advances of Rs2.1tn.

Management

Name	Designation
KVS Manian	Managing Director & CEO
Harsh Dugar	Executive Director
Shalini Warrier	Executive Director

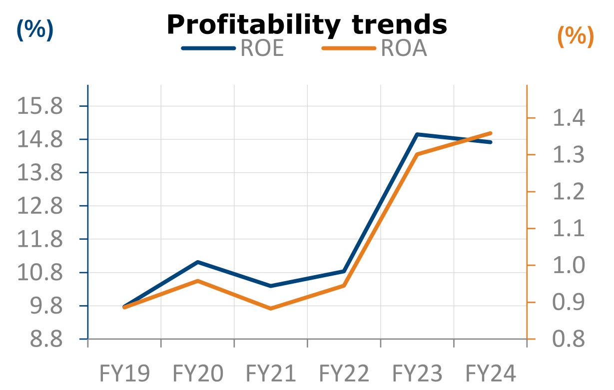


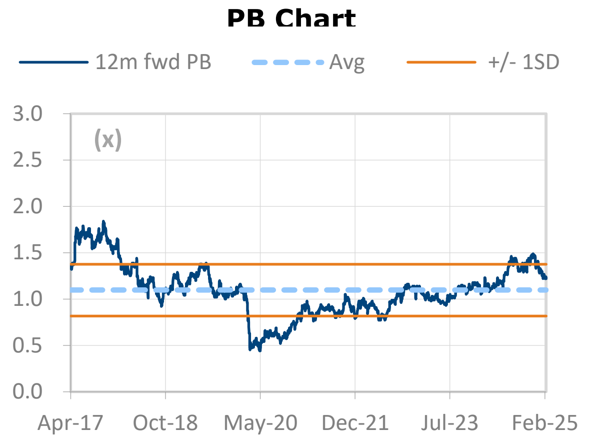


Key earnings drivers

Y/e 31 Mar, Parent	FY23A	FY24A	FY25ii	FY26ii	FY27ii
Loan Growth (%)	20.4	20.0	13.1	14.9	15.0
Net Interest Margin (%)	3.2	3.1	3.1	3.0	3.1
Net int income growth (%)	21.3	14.7	15.7	11.7	16.4
Core fee income growth (%)	39.5	16.9	20.9	16.3	19.0
Non-int inc/total inc (%)	24.4	27.1	27.8	27.8	28.0
Operating costs growth (%)	11.1	30.0	15.2	12.8	12.3
Cost/income ratio (%)	49.9	54.5	53.7	54.3	52.2
Gross NPLs ratio (%)	2.4	2.1	1.8	1.9	2.0
Total Prov/avg loans (%)	0.5	0.1	0.4	0.4	0.4

Source: Company data, IIFL Research





Financial summary

Income statement summary (Rs bn)

Y/e 31 Mar, Parent	FY23A	FY24A	FY25ii	FY26ii	FY27ii
Net interest income	**72**	**83**	**96**	**107**	**125**
Non-interest income	**23**	**31**	**37**	**41**	**49**
Fee Income	21	25	30	35	41
Portfolio gains	1	2	3	2	2
Others	2	4	5	5	5
Total operating income	**96**	**114**	**133**	**148**	**173**
Total operating expenses	48	62	71	81	90
Pre provision operating profit	**48**	**52**	**62**	**68**	**83**
Total provisions	7	2	8	10	13
Profit before tax	**40**	**50**	**53**	**58**	**70**
Taxes	10	13	13	14	17
Net profit-pre exceptional	**30**	**37**	**40**	**43**	**52**
Exceptional items	0	0	0	0	0
Reported net profit	**30**	**37**	**40**	**43**	**52**

Balance sheet summary (Rs bn)

Y/e 31 Mar, Parent	FY23A	FY24A	FY25ii	FY26ii	FY27ii
Net loans & advances	1,744	2,094	2,369	2,721	3,131
Placements to other banks	51	75	82	85	97
Cash & equivalents	126	115	171	187	214
Investments	490	609	662	756	864
Total interest-earning assets	**2,411**	**2,892**	**3,284**	**3,750**	**4,306**
Fixed assets	9	10	15	16	18
Other assets	183	181	127	135	128
Total assets	**2,603**	**3,083**	**3,426**	**3,902**	**4,453**
Customer deposits	2,134	2,525	2,736	3,125	3,574
Borrowings	193	180	243	280	322
Total interest-bearing liabilities	**2,327**	**2,706**	**2,980**	**3,405**	**3,896**
Non-interest-bearing liabilities	61	87	117	129	141
Total liabilities	**2,388**	**2,792**	**3,096**	**3,534**	**4,037**
Total Shareholders' equity	**215**	**291**	**329**	**368**	**415**
Total liabilities & equity	**2,603**	**3,083**	**3,426**	**3,902**	**4,453**

Source: Company data, IIFL Research

Ratio analysis - I

Y/e 31 Mar, Parent	FY23A	FY24A	FY25ii	FY26ii	FY27ii
Balance Sheet Structure Ratios (%)					
Loans / Deposits	81.8	82.9	86.6	87.1	87.6
Loan Growth	20.4	20.0	13.1	14.9	15.0
Deposit Growth	17.4	18.3	8.4	14.2	14.4
Total Assets Growth	17.8	18.4	11.1	13.9	14.1
Profitability Ratios (%)					
Net Interest Margin	3.2	3.1	3.1	3.0	3.1
ROA	1.3	1.3	1.2	1.2	1.3
ROE	14.9	14.7	12.9	12.4	13.4
Non-Int Income as % of Total Income	24.4	27.1	27.8	27.8	28.0
Net Profit Growth	59.3	23.6	7.2	8.6	20.9
FDEPS Growth	54.8	13.8	3.5	5.0	20.9
Efficiency Ratios (%)					
Cost to Income Ratio	49.9	54.5	53.7	54.3	52.2
Salaries as % of Non-Interest costs	45.6	45.5	43.4	42.8	42.4

Ratio analysis - II

Y/e 31 Mar, Parent	FY23A	FY24A	FY25ii	FY26ii	FY27ii
Credit Quality Ratios (%)					
Gross NPLs as % of loans	2.4	2.1	1.8	1.9	2.0
NPL coverage ratio	71.2	72.3	75.0	75.0	75.0
Total prov charges as % avg loans	0.5	0.1	0.4	0.4	0.4
Net NPLs as % of net loans	0.7	0.6	0.4	0.5	0.5
Capital Adequacy Ratios (%)					
Total CAR	14.8	16.1	15.1	14.9	15.0
Tier I capital ratio	13.0	14.6	13.9	13.7	13.8

Source: Company data, IIFL Research

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Key to our recommendation structure
BUY - Stock expected to give a return 10%+ more than average return on a debt instrument over a 1-year horizon.
SELL - Stock expected to give a return 10%+ below the average return on a debt instrument over a 1-year horizon.
Add - Stock expected to give a return 0-10% over the average return on a debt instrument over a 1-year horizon.
Reduce - Stock expected to give a return 0-10% below the average return on a debt instrument over a 1-year horizon.

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Price Target: Unless otherwise stated in the text of this report, target prices in this report are based on either a discounted cash flow valuation or comparison of valuation ratios with companies seen by the analyst as comparable or a combination of the two methods. The result of this fundamental valuation is adjusted to reflect the analyst's views on the likely course of investor sentiment. Whichever valuation method is used there is a significant risk that the target price will not be achieved within the expected timeframe. Risk factors include unforeseen changes in competitive pressures or in the level of demand for the company's products. Such demand variations may result from changes in technology, in the overall level of economic activity or, in some cases, in fashion. Valuations may also be affected by changes in taxation, in exchange rates and, in certain industries, in regulations. Investment in overseas markets and instruments such as ADRs can result in increased risk from factors such as exchange rates, exchange controls, taxation, and political and social conditions. This discussion of valuation methods and risk factors is not comprehensive – further information is available upon request.

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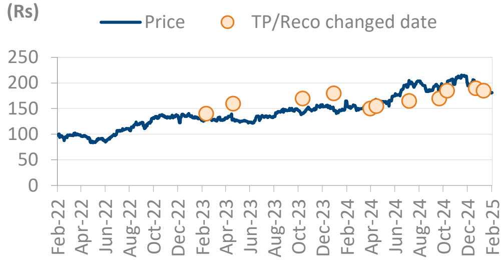
Federal Bank: 3 year price and rating history



Date	Rating	Close price (Rs)	Target price (Rs)	Upside (%)
29 Jan 2025	ADD	184	185	0.5
09 Jan 2025	ADD	195	190	-2.6
29 Oct 2024	ADD	188	185	-1.6
09 Oct 2024	REDUCE	188	170	-9.6
25 Jul 2024	REDUCE	201	165	-17.9
03 May 2024	REDUCE	168	155	-7.7
18 Apr 2024	REDUCE	152	150	-1.3
17 Jan 2024	BUY	150	180	20.0
30 Oct 2023	BUY	138	170	23.2
08 May 2023	BUY	128	160	25.0
01 Mar 2023	BUY	129	140	8.5