

## Balancing Transition, Strategy & Execution key

23 February 2025

Federal Bank (FB IN) hosted an analyst meet recently, which outlined a strategy blueprint under the aegis of new MD & CEO KVS Manian. While we found the blueprint to be detailed, it seemed to lag on quantification to benchmark the progress. The intent, team and resources seem to be in place, but execution needs a watch, especially as anecdotally these transitions have been difficult. The roadmap suggests the bank is likely to undertake the transition on both sides of the balance sheet (loan and deposit construct), which we believe takes time and may have near-term dislocation, even as it may lead to longer-term gains. Also, the requirement of upfronted cost allocation will have a near-term impact. Not to mention, sectoral headwinds on NIM and variables at play on deposits would add to transition variabilities and may feed into near-term soft core performance. Amid the transition, sectoral headwinds and peer valuation (few frontline private banks are trading at similar and/or lower levels), near-term outperformance is likely to be limited with longer-term benefits. We reiterate **Buy** with a TP of INR 220 based on 1.3x September 2026E P/BV.

**Making the right moves but the road to success is lined with execution:** The bank outlined a strategic blueprint with underlying aspirations of: 1) becoming the Top 5 private banks, 2) building a universal bank by augmenting other value added service, and 3) building a national franchise by strengthening brand presence & augmenting scale of operations. The bank aims to focus on 1) NIM (this will need balance sheet changes), 2) fee income, and 3) offering other services (open to inorganic routes). The intent seems right, but execution will be crucial, which entails challenges.

**Undertaking transition on 12 key themes:** The bank has outlined 12 key themes detailing crucial success factors. **Theme 1:** NIM improvement: driven by focus on CASA with heavy lifting by CA focus while scaling up medium-yield assets (not in favor of dumbbell strategy), 2) **Theme 2:** expanding product portfolio: used vehicle, micro LAP and tractor finance, 3) **Theme 3:** Fee enhancement: tougher one per management, 4) **Theme 4:** branch strategy for scalable growth: aims to add 400-450 branches until FY28 (1,550 currently), 5) **Theme 5:** branch transformation: focus on efficiency, 6) **Theme 6:** brand transformation, 7) **Theme 7:** digital augmentation, 8) **Theme 8:** renewed digital distribution strategy, 9) **Theme 9:** people & culture, 10) **Theme 10:** cost optimization – leverage Fedserv, 11) **Theme 11:** strengthening assurance functions, and 12) **Theme 12:** evolution towards a universal bank open to inorganic opportunities.

**Reiterate Buy with a TP of INR 220:** FB has been delivering steady earnings in an otherwise difficult operating environment, but the current transition will lead to variabilities in the near term even as longer-term benefits will accrue. The bank has strengthened its underlying in the past few years, which will help it deliver a ROA and a ROE of 1.2% and 12-13%, respectively, by FY27E. It seems to be focused on making the right moves but transition will have its challenges, feeding into near-term vulnerabilities. We retain Buy with a TP of INR 220 on 1.3x September 2026E P/BV.

### Key financials

YE March	FY23	FY24	FY25E	FY26E	FY27E
PPoP (INR bn)	48	52	62	69	81
YoY (%)	27.6	7.9	19.0	12.7	17.5
NP (INR bn)	30	37	40	41	47
YoY (%)	59.3	23.6	7.1	3.9	13.2
EPS (INR)	14	15	16	17	19
YoY (%)	58.3	7.4	7.1	3.9	13.2
P/PPoP (x)	9.4	8.7	7.3	6.5	5.5
RoAE (%)	14.9	14.7	12.9	11.9	12.0
RoAA (%)	1.3	1.4	1.3	1.2	1.2
P/E (x)	12.9	12.0	11.2	10.8	9.5
P/ABV (x)	1.9	1.6	1.4	1.2	1.1

Note: Pricing as on 21 February 2025; Source: Company, Elara Securities Estimate

Rating: **Buy**

Target Price: **INR 220**

Upside: **22%**

CMP: **INR 180**

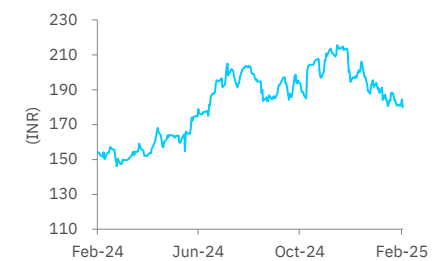
As on 21 February 2025

### Key data

Bloomberg	FB IN
Reuters Code	FED.NS
Shares outstanding (mn)	2454
Market cap (INR bn/USD mn)	441/5092
Enterprise Value (INR bn/USD mn)	0/0
Avg daily volume 3M (INR mn/USD mn)	2070/24
52 week high/low	217/140
Free float (%)	100

Note: as on 21 February 2025; Source: Bloomberg

### Price chart



Source: Bloomberg

Shareholding (%)	Q4 FY24	Q1 FY25	Q2 FY25	Q3 FY25
Promoter	0.0	0.0	0.0	0.0
% Pledged	0.0	0.0	0.0	0.0
FII	29.3	29.4	27.4	26.32
DII	46.2	44.9	47.1	48.9
Others	24.5	25.7	25.5	24.8

Source: Bloomberg

Price performance (%)	3M	6M	12M
Nifty	(2.4)	(8.0)	3.4
Federal Bank	(14.7)	(11.5)	17.0
NSE Midcap	(7.2)	(13.6)	3.8
NSE Smallcap	(11.1)	(18.0)	(2.3)

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## Financials (YE March)

Income statement (INR mn)	FY23	FY24	FY25E	FY26E	FY27E
<b>Net interest income</b>	<b>72,322</b>	<b>82,935</b>	<b>95,404</b>	<b>108,152</b>	<b>124,044</b>
YoY growth (%)	21.3	14.7	15.0	13.4	14.7
Fee income	19,137	22,422	25,879	29,673	34,275
Trading profits	2,650	2,470	2,600	1,700	2,000
Non-interest income	23,300	30,793	36,880	39,993	45,896
Net operating revenue	95,622	113,728	132,284	148,146	169,940
YoY growth (%)	18.8	18.9	16.3	12.0	14.7
Operating expenses	47,678	61,983	70,733	78,800	88,454
YoY growth (%)	11.1	30.0	14.1	11.4	12.3
<b>Pre-provisioning operating profit</b>	<b>47,944</b>	<b>51,745</b>	<b>61,551</b>	<b>69,346</b>	<b>81,486</b>
YoY growth (%)	27.6	7.9	19.0	12.7	17.5
Provisions for bad debts	5,499	1,661	7,789	13,491	18,326
Other provisions	2,000	300	500	500	500
Profit before tax	40,445	49,784	53,262	55,354	62,660
Tax	10,339	12,578	13,422	13,949	15,790
<b>Profit after tax</b>	<b>30,106</b>	<b>37,206</b>	<b>39,840</b>	<b>41,405</b>	<b>46,870</b>
YoY growth (%)	59.3	23.6	7.1	3.9	13.2
<b>Balance sheet (INR mn)</b>	<b>FY23</b>	<b>FY24</b>	<b>FY25E</b>	<b>FY26E</b>	<b>FY27E</b>
Customer loans	1,744,469	2,094,033	2,391,386	2,726,180	3,151,464
YoY growth (%)	20.4	20.0	14.2	14.0	15.6
Investments	489,834	608,595	680,821	745,830	859,640
Cash & bank balances	176,887	189,629	233,919	249,472	287,354
Fixed assets	9,290	10,151	10,423	10,546	10,521
Other assets	182,890	180,660	162,494	168,473	175,581
<b>Total Assets</b>	<b>2,603,368</b>	<b>3,083,068</b>	<b>3,479,042</b>	<b>3,900,500</b>	<b>4,484,560</b>
Net worth	215,012	290,894	328,753	368,176	413,065
Deposits	2,133,860	2,525,340	2,780,400	3,183,557	3,661,091
YoY growth (%)	17.4	18.3	10.1	14.5	15.0
Borrowings	193,193	180,264	253,444	225,744	272,488
Other liabilities	61,303	86,570	116,446	123,022	137,916
<b>Total Liabilities</b>	<b>2,603,368</b>	<b>3,083,068</b>	<b>3,479,042</b>	<b>3,900,500</b>	<b>4,484,560</b>
<b>Key operating ratios (%)</b>	<b>FY23</b>	<b>FY24</b>	<b>FY25E</b>	<b>FY26E</b>	<b>FY27E</b>
Lending yield	8.4	9.2	9.2	8.9	8.8
Cost of Funds	4.3	5.4	5.4	5.2	5.2
Spreads	3.2	3.0	2.9	2.8	2.8
Net interest margin	3.2	3.1	3.1	3.1	3.1
CASA Ratio	32.7	29.4	30.3	30.4	30.5
Non-interest income / operating income	24.4	27.1	27.9	27.0	27.0
Cost/income	49.9	54.5	53.5	53.2	52.1
Operating expense/avg assets	2.0	2.2	2.2	2.1	2.1
Credit costs / avg loans	0.3	0.1	0.3	0.5	0.6
Effective tax rate	25.6	25.3	25.2	25.2	25.2
Loan deposit ratio	81.8	82.9	86.0	85.6	86.1
<b>ROA decomposition (%)</b>	<b>FY23</b>	<b>FY24</b>	<b>FY25E</b>	<b>FY26E</b>	<b>FY27E</b>
NII /Assets	3.2	3.1	3.1	3.1	3.1
Fees/Assets	0.9	1.1	1.1	1.1	1.1
Invst profits/Assets	0.1	0.1	0.1	0.0	0.0
Net revenues/Assets	4.3	4.3	4.3	4.2	4.2
Opex /Assets	(2.1)	(2.3)	(2.3)	(2.2)	(2.2)
Provisions/Assets	(0.3)	(0.1)	(0.3)	(0.4)	(0.5)
Taxes/Assets	(0.5)	(0.5)	(0.4)	(0.4)	(0.4)
Total costs/Assets	(2.9)	(2.9)	(3.0)	(3.0)	(3.1)
ROA	1.3	1.4	1.3	1.2	1.2
Equity/Assets	9.0	9.5	10.0	9.9	9.7
ROAE -RHS	14.9	14.7	12.9	11.9	12.0
<b>Key financial ratios (%)</b>	<b>FY23</b>	<b>FY24</b>	<b>FY25E</b>	<b>FY26E</b>	<b>FY27E</b>
Tier I Capital adequacy	13.0	14.6	14.4	14.0	13.7
Gross NPL	2.4	2.1	1.9	2.0	2.1
Net NPL	0.7	0.6	0.5	0.6	0.6
Slippage ratio	1.1	1.0	0.9	1.2	1.3
Assets / equity (x)	12.1	10.6	10.6	10.6	10.9
<b>Per share data</b>					
EPS (INR)	14	15	16	17	19
YoY growth (%)	58	7	7	4	13
BVPS (INR)	102	119	135	151	170
Adj BVPS (INR)	98	116	132	147	164
Dividend yield (%)	0.7	0.9	1.0	1.0	1.0
<b>Valuation (x)</b>					
P/BV	1.80	1.53	1.36	1.21	1.08
P/ABV	1.88	1.58	1.39	1.25	1.12
P/E	12.88	12.00	11.20	10.78	9.52

Note: Pricing as on 21 February 2025; Source: Company, Elara Securities Estimate

## Opening remarks by MD&CEO KVS Manian

- ▶ In the initial 100 days, to understand the DNA of the bank – MD & CEO travelled across 15 locations including foreign locations meeting ~2,000 people
- ▶ Profitability: FB aims to enhance profitability while sustaining growth momentum and make a pivotal shift from affordability-driven bank to value-driven
- ▶ Expansion of branches: expand outside Kerala while leveraging home-turf strength
- ▶ Branch banking: FB currently is working to refine branch banking model, thereby garnering asset and liability business through sustainable sales mechanism
- ▶ Brand creation: It aims to attract younger generation for their banking needs
- ▶ HR, talent and culture: With the lowest attrition rate among peers, bank wants to leverage the same for maintaining a healthy and conducive working environment.

The bank aims to be a part of the Top 5 large private banks in the next 3-5 years. In order this, it has identified the following focus areas:

NR franchise: FB aims to strengthen its non-resident(NR) franchise. With 20% of remittance volume taking place through the bank due to Kerala GCC, it wants to expand beyond Kerala GCC. The bank is relatively focused on this franchise and aims to build further on this segment with low focus on FCNR-B deposits

- Affluent banking: The bank has loan products in this segment; however, the wealth management segment is absent. It aims to add capital market and wealth management propositions to excel in this segment
  - SME lending: FB aims to improve this segment by generating fees through cash management fees, transactions flows and trade & forex services
  - Corporate banking: It aims to be profitable by serving the mid-corporate segment where the scope of garnering various business is higher
  - Cards business: The bank is currently sourcing 70% of cards through partners, which limits upside as well as the risk. It wants to make a strategic shift to acquire cards through the organic route, thereby resulting in higher acquisition cost initially but larger rewards in the future
- ▶ Pivotal Bank has identified 12 key themes for the next half-decadal horizon

### Theme 1: NIM improvement

#### Liability side

- ▶ With current interest expense to average earning assets ratio at 5.6% on a 9MFY25 basis, FB aims to move directionally toward 5.2% (the next three large private banks) and ~4.6% (the Top 3 large private banks), respectively
- ▶ Strengthening the CA portfolio: the bank aims to take total deposits from the current levels of 6% to 10-12%, thereby leading to improved cost of funds. It aims to build a granular CASA portfolio and take it from 30% to 36% in the next three years
- ▶ Enhance engagement with capital markets to garner liability business and better fee & float
- ▶ Enhance NR beyond the GCC and Kerala: Diversifying base by tapping high CASA-potential markets beyond the Gulf and the Kerala corridor

#### Asset side

- ▶ FB aims to scale-up medium yield assets. With current environment remaining tough for the unsecured segments, it aims to focus on medium yield segments
- ▶ Corporate banking is set to target mid-market corporate lending for better profitability
- ▶ Bank aims to leverage priority sector lending (PSL) strategy in the MSME business segment

- ▶ It has an optimized risk adjusted return on capital (RAROC)-based pricing mechanism, which is implemented to manage risk framework
- ▶ Low yield asset is likely to be brought down from current 64% to 58%. FB expects to execute it in a phased manner

#### Theme 2: Expanding product portfolio

- ▶ The bank aims to offer investment products – wealth management, 3-IN-1 product
- ▶ Scaling-up used vehicle finance (CV, CE and car loans) as it provides better yield. These businesses are small and it aims to scale up
- ▶ It wants to expand offerings for micro-LAP products
- ▶ FB aims to launch EMI-based unsecured business loans: This will focus on existing customers
- ▶ Regulatory changes in real estate finance on the corporate side has made this segment safer: FB plans to explore in this segment
- ▶ Sustainable finance: EV financing and green products are the sunrise segments, and it will venture into this space
- ▶ Wholesale banking: correspondent banking, syndication and investment banking and capital market services

#### Theme 3: Fee enhancement

- ▶ Wealth management and bancassurance business: FB has robust bancassurance policies and is fully compliant
- ▶ Cash management services are set to garner liability business
- ▶ Trade and forex income: Affluent & NR banking and segment offerings for MSME and mid-market business are expected to drive this segment. It aims to add talent in these pools and reskilling current employees

#### Theme 4: Branch strategy

- ▶ The bank aims to do a phased expansion in Tier-2 geographies. Strategy is to have selective state level expansion with focus on Top 10 high GSDP States
- ▶ With FB's current strategy to improve productivity metrics from current branches, it aims to add 400-450 branches until FY28 with continued monitoring of cost-to-income levels

#### Theme 5: Branch transformation

- ▶ FB aims to modernize the branch format, expanding sales & distribution capacity and automation of some activities
- ▶ It is working to centralize task and structure regional support for operational efficiency

#### Theme 6: Brand transformation

- ▶ The bank aims to improve brand recognition apart from home-turf and attract younger generation. In Kerala, it has "Out of chart" numbers and aims to replicate them in other States

#### Theme 7: Technology (digital at the fore, human at the core)

- ▶ FB aims to enhance user experience by improving omni-channel experience, introducing Gen AI chatbots, adding wealth management solutions and offering comprehensive digital offerings for corporate & SME segments

**Theme 8: Improve digital distribution**

- ▶ Improve digital distribution: a large part of digital distribution has been partner-led. FB aims to create its own digital capabilities to reduce reliance on partners
- ▶ In the credit card portfolio, partner sourcing is ~70% and aims to lower it to 55% by FY28. In personal loans, current partner sourcing is at 40% and the bank aims to take it to 50%
- ▶ With respect to savings account, partner sourcing is 95% and it wants to cut it to 75%

**Theme 9: People and culture**

- ▶ The bank has vertical heads and enhanced sales culture, which foster alertness, agility, and astuteness

**Theme 10: Cost optimization**

- ▶ FB is working on scorecard-based approach to optimize outcomes rather than focusing on cost
- ▶ The bank aims to leverage Fedserv (100% subsidiary for operations) to reduce cost of operations
- ▶ Downtrend on cost might not be visible initially, it will improve in the longer run

**Theme 11: Strengthening assurance functions**

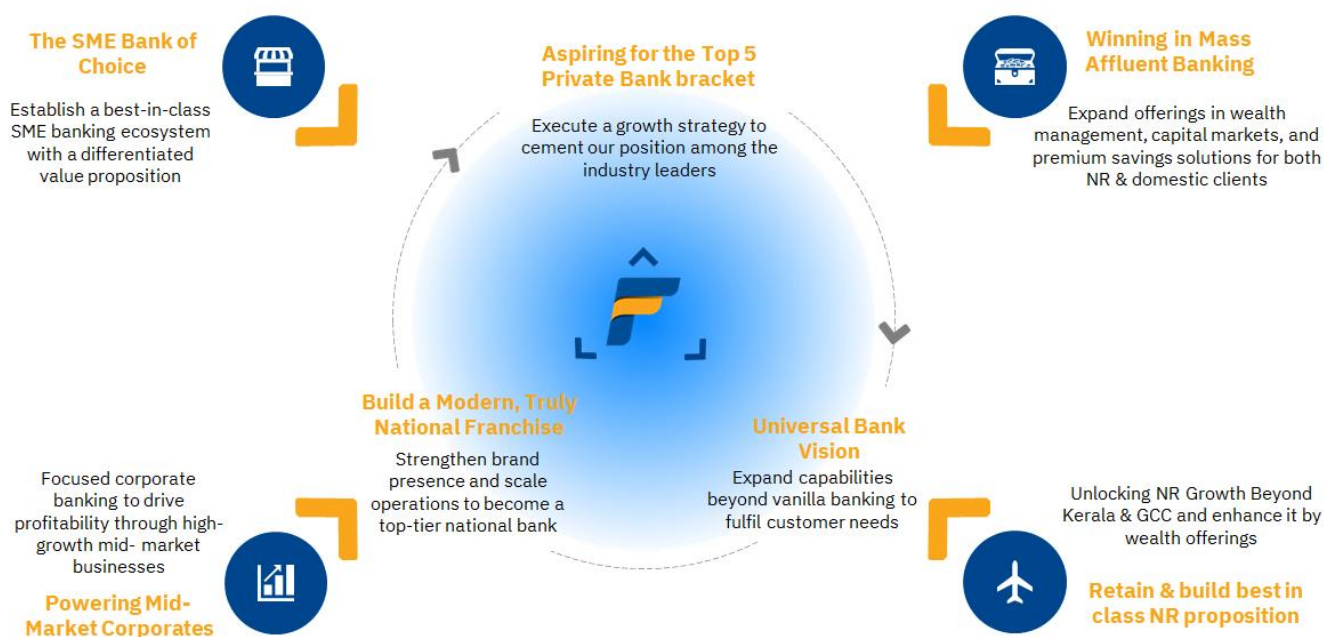
- ▶ Compliance: FB wants to optimize (SAS) and digitize enterprise risk management through compliance management system
- ▶ Institute better RAROC-based pricing to manage risk in a better manner

**Theme 12: Evolution toward a universal bank**

- ▶ With goal to become the most admired bank, FB will diversify into financial services, either organically or inorganically by creating a holistic franchise

**Exhibit 1: Key focus areas**

**Charting the Future: Strengthening Our Foundation & Expanding Horizons**



Source: Company presentation, Elara Securities Research

Exhibit 2: Key drivers to achieve these goals

Breakthrough – Chapter 4.0

Profitable Growth

Prioritizing sustainable, high-quality earnings aligned with long-term profitability.

Scaling Up, Smartly

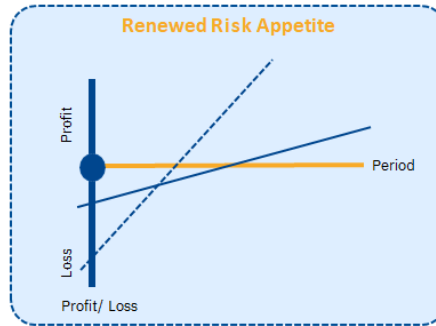
Expanding footprint, optimizing capital, and leveraging tech for cost-effective growth.

Technology & Innovation at the Core

Leveraging AI and automation to enhance efficiency, streamline operations, and boost customer experience.

Culture of High Performance

Fostering ownership, agility, and accountability to drive collective success.



Winning the Right Customers

Focusing on Mass Affluent, MSME, and next-gen customers to deepen relationships and enhance value.

Repositioning for the Future

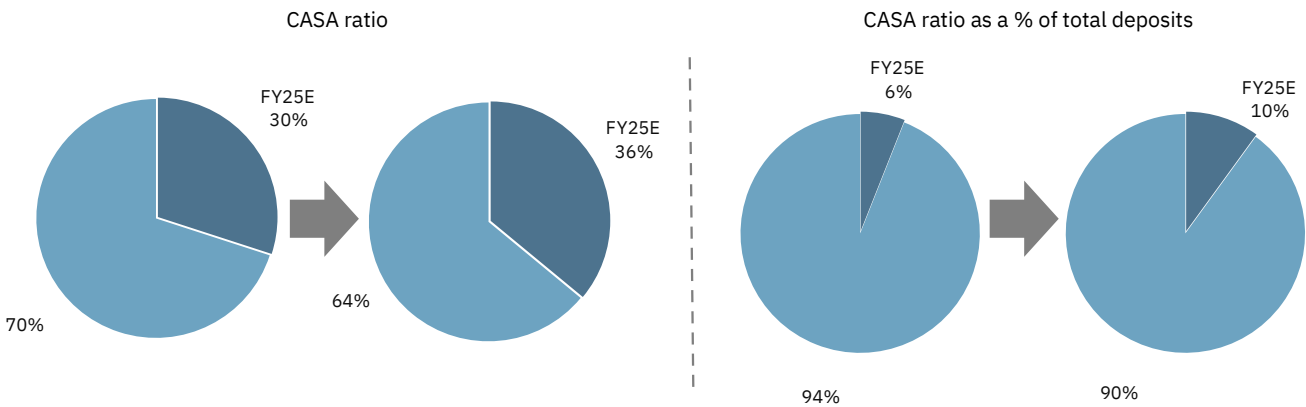
Evolving beyond legacy perceptions to establish Federal Bank as a future-ready powerhouse.

Uncompromising Risk & Compliance Standards

Strengthening governance, risk, and compliance to ensure stability while scaling new heights.

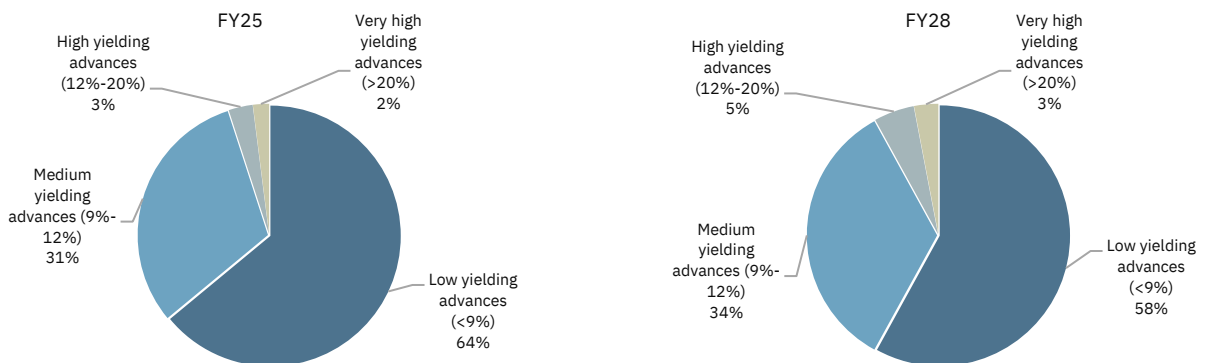
Source: Company presentation, Elara Securities Research

Exhibit 3: Bank aims to improve the CASA ratio with increased contribution from CA



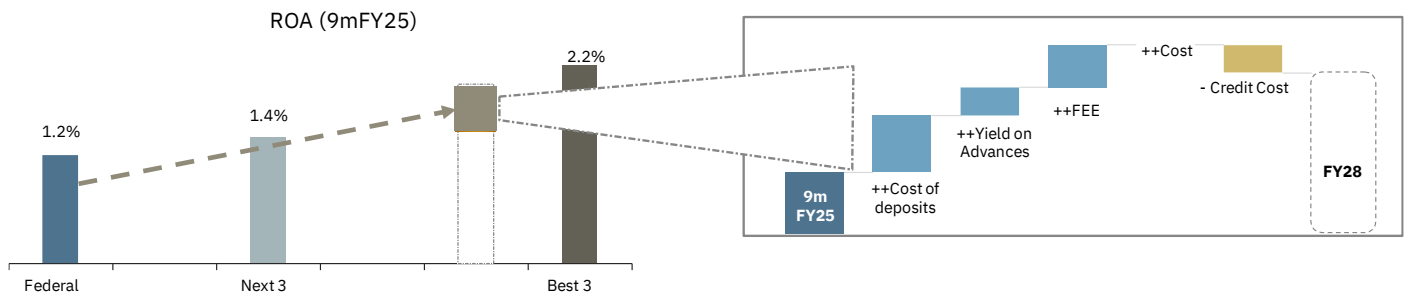
Source: Company, Elara Securities Research

Exhibit 4: Reshaping advance mix target



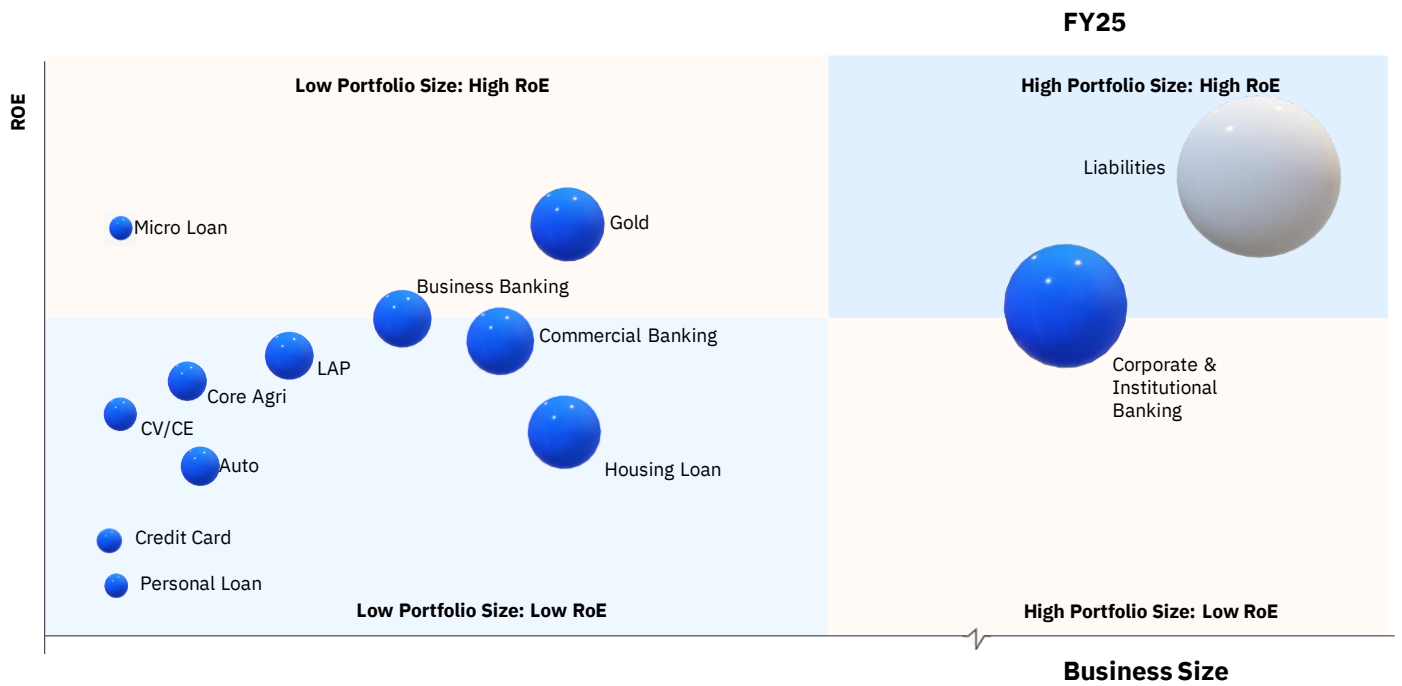
Source: Company, Elara Securities Research

**Exhibit 5: ROA improvement contributors**



Source: Company presentation, Elara Securities Research

**Exhibit 6: Product portfolio dynamics**



Note: CIB: Corporate and Institutional Banking; CB: Commercial Banking; BB: Business banking; MRBD: Micro loans ; CVCE: Commercial vehicle and construction equipment financing  
 Source: Company presentation, Elara Securities Research

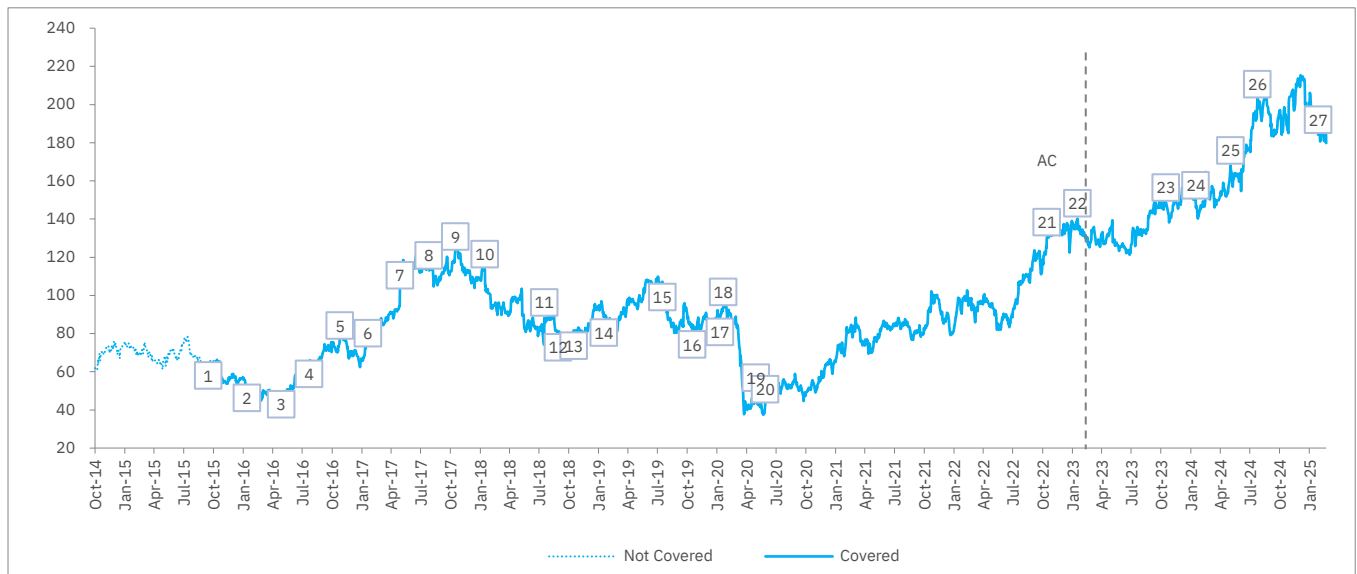
**Exhibit 7: Valuation summary**

Particulars	INR
BVPS on Sep ,2026	160
Target multiple (x)	1.3
Value of core bank	220
CMP	180
Upside (%)	22

Source: Elara Securities Estimate



## Coverage History



	Date	Rating	Target Price	Closing Price
22	16-Jan-2023	Buy	INR 168	INR 140
23	16-Oct-2023	Buy	INR 175	INR 149
24	16-Jan-2024	Buy	INR 189	INR 149
25	2-May-2024	Buy	INR 207	INR 168
26	24-Jul-2024	Buy	INR 240	INR 201
27	28-Jan-2025	Buy	INR 220	INR 184

## Guide to Research Rating

<b>BUY</b>	Absolute Return >+20%
<b>ACCUMULATE</b>	Absolute Return +5% to +20%
<b>REDUCE</b>	Absolute Return -5% to +5%
<b>SELL</b>	Absolute Return < -5%



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