

India

HOLD (no change)

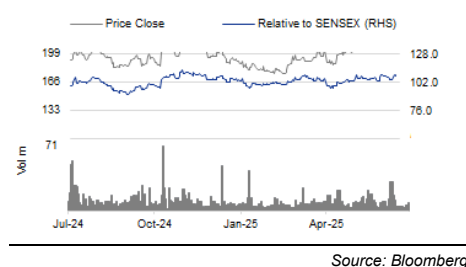
Consensus ratings*: Buy 35 Hold 8 Sell 1

Current price:	Rs196
Target price:	Rs210
Previous target:	Rs220
Up/downside:	7.1%
InCred Research / Consensus:	-8.9%
Reuters:	FED.NS
Bloomberg:	FB IN
Market cap:	US\$5,503m
	Rs481,671m
Average daily turnover:	US\$19.1m
	Rs1669.2m
Current shares o/s:	192.3m
Free float:	100.0%

*Source: Bloomberg

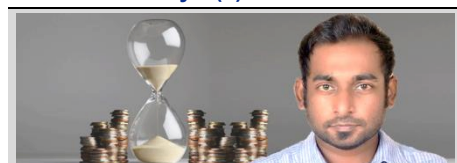
Key changes in this note

- Revise our margin/credit cost assumptions for FY26F-28F based on 1QFY26 results.
- We also tweak our sustainable RoE assumptions and revisit valuations of subs.



Price performance	1M	3M	12M
Absolute (%)	(10.4)	(0.3)	(2.3)
Relative (%)	(7.2)	(0.4)	(1.9)

Major shareholders	% held
HDFC MF	7.1
IFC	3.9
LIC	3.6

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Federal Bank

Core PPOp beat; credit costs rise

- Key negatives are a rise in credit costs and a weaker-than-expected margin progression. The positives are strong fee income and contained costs.
- The transformation journey is one of the steps in right direction, but the current valuation is reasonable, leaving little room to disappoint on the execution front.
- We value the core bank at 1.2x FY27F BV and assign subsidiaries' value (Rs18/share) to arrive at a new TP of Rs210 (7% upside). Retain HOLD rating.

Core PPOp beat; strong treasury gains offset higher provisioning

Federal Bank posted 1QFY26 PAT of Rs8.6bn (annualized RoA of 1%), which was above our estimate. This was mainly owing to a better-than-expected core performance and strong non-core income, which helped offset the QoQ rise in credit costs (67bp vs. our estimate of 50bp). The non-core income includes treasury gains (of Rs1.3bn; 14bp of avg. assets) and recovery from written-off accounts (Rs2bn; 23bp). The core performance was aided by strong core fee income (21% YoY) & contained opex (11% YoY; 3% below our estimate) while NII was broadly in line (up 2% YoY; down 2% QoQ). Margin dipped by 18bp QoQ to 2.94% (above street estimate). The uptick in credit costs was mainly because of stress in microfinance or MFI & agri segments, excluding which, the asset quality was stable across segments. The bank gave full-year credit cost guidance of 55bp for F26F. Management indicated a marginal rise in stress in the lower bucket of business banking & CV/CE segments but is not at all worried and plans to grow in line with its articulated strategy. Loans grew by 9% YoY (+3% QoQ) and the bank gave guidance of growing at 1.2x nominal GDP in the near- to medium- term. Deposits grew by 8% YoY (1% QoQ), of which the average CASA grew by 12% YoY (2% QoQ) and the ratio improved by 12bp QoQ /108bp YoY to 30.35%. The CET-1 ratio remains healthy at 14.7%.

Margin to trough 5-10bp lower in 2Q; full-year average will be ~2.9%

Margin fell by 18bp QoQ to 2.94%, mainly led by loan yields (down 27bp QoQ; includes 5bp owing to higher interest reversals), partly offset by lower deposit costs (down 20bp QoQ). A part of the repo rate cut impact is yet to flow through (particularly two-thirds of ~50bp cut in early-Jun 2025; pass-through is on a T+1 basis) and will reflect in 2QFY26F. This will be offset by residual benefit from savings account rate cuts and some repricing of time liabilities (term deposits & wholesale borrowings).

Risk-reward appears balanced at valuation of 1.2x 1-yr fwd core P/BV

At the current valuation, the stock appears fairly priced for ~13-14% RoE over FY27F-28F and leaves limited room to disappoint on the execution front. We cut our target price to Rs210 (Rs220 earlier) as we tweak sustainable RoE to account for higher credit costs. We value the core bank at 1.2x FY27F BV and assign subsidiaries' value (at Rs18/share) to arrive at a lower target price of Rs210 (7% upside), from Rs220 earlier. Upside risks: Stronger-than-expected growth & margin progression. Downside risks: Slower-than-expected volume growth, higher credit costs, and weak margin outcome.

Financial Summary	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Net Interest Income (Rsm)	82,935	94,680	97,928	119,209	146,164
Total Non-Interest Income (Rsm)	30,793	38,013	43,710	50,809	63,973
Operating Revenue (Rsm)	113,728	132,692	141,638	170,018	210,137
Total Provision Charges (Rsm)	(1,961)	(7,331)	(15,510)	(16,328)	(19,185)
Net Profit (Rsm)	37,206	40,519	34,365	46,019	63,550
Core EPS (Rs)	15.28	16.50	14.00	18.75	25.89
Core EPS Growth	7%	8%	(15%)	34%	38%
FD Core P/E (x)	12.83	11.88	14.01	10.46	7.57
DPS (Rs)	1.20	1.20	1.05	1.41	1.94
Dividend Yield	0.61%	0.61%	0.54%	0.72%	0.99%
BVPS (Rs)	119.5	136.1	150.7	168.4	192.9
P/BV (x)	1.64	1.44	1.30	1.16	1.02
ROE	14.7%	13.0%	9.8%	11.7%	14.3%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 1: Quarterly earnings summary

Rs Mn	1QFY25	4QFY25	1QFY26	YoY (%)	QoQ (%)
Net Interest Income	22,920	23,774	23,368	2%	-2%
Other Income	9,152	10,060	11,130	22%	11%
--Core Fee	6,080	7,510	7,350	21%	-2%
--Treasury Income	350	460	1,270	263%	176%
--Misc. Income	2,722	2,090	2,510	-8%	20%
-----o/w Recovery from w/off	2,270	1,590	1,990	-12%	25%
Total income	32,072	33,834	34,498	8%	2%
--Core Revenues	29,000	31,284	30,718	6%	-2%
Operating Expenses	17,063	19,180	18,935	11%	-1%
--Staff Expenses	7,380	7,838	7,976	8%	2%
--Other Operating Expenses	9,682	11,342	10,959	13%	-3%
Operating Profit	15,009	14,654	15,563	4%	6%
--Core PPOp	11,937	12,104	11,783	-1%	-3%
Provisions	1,443	1,381	4,002	177%	190%
PBT	13,566	13,273	11,561	-15%	-13%
Tax	3,471	2,971	2,944	-15%	-1%
PAT	10,095	10,302	8,617	-15%	-16%
EPS	17	17	14		
Advances	2,208,070	2,348,364	2,412,040	9%	3%
Deposits	2,660,650	2,836,475	2,874,360	8%	1%
LD Ratio	83%	83%	84%		
CASA Ratio	29%	30%	30%		
Margins (%)	3.16	3.12	2.94	-0.22	-0.18
Overall provisions (in bps)	27	24	67		
---Credit cost (in bps)	27	25	67		
-----NPA provisions	27	25	64		
GNPA	47,384	43,755	46,697	-1%	7%
GNPA Ratio (%)	2.11	1.84	1.91		
NNPA	13,304	10,404	11,576	-13%	11%
NNPA Ratio (%)	0.60	0.44	0.48		
PCR	34,079	33,352	35,120	3%	5%
PCR Ratio (%)	72%	76%	75%		
Slippages	4,240	4,920	6,610	56%	34%
--% of trailing loans	0.9%	0.9%	1.2%		
CET-1 Ratio (%)	14.7%	15.0%	14.7%		
RoA	1.3%	1.2%	1.0%		
RoE	13.6%	12.8%	10.3%		

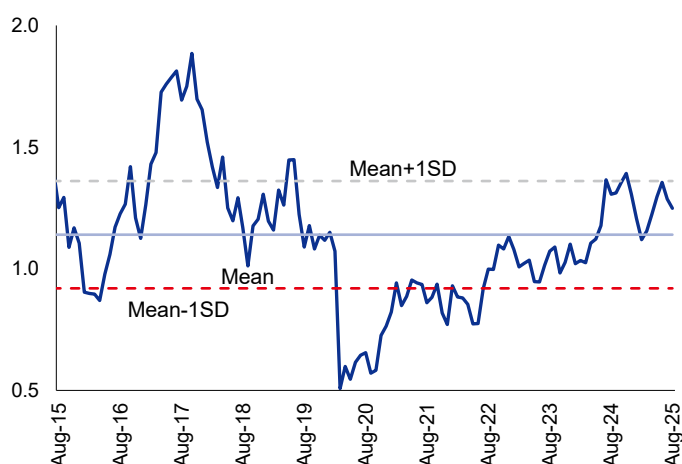
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Our revised earnings estimates

Rs bn	New Estimates				Old Estimates			Change		
	FY25	FY26F	FY27F	FY28F	FY26F	FY27F	FY28F	FY26F	FY27F	FY28F
Net Interest Income	95	98	119	146	103	124	149	-5%	-4%	-2%
--Growth YoY	14%	3%	22%	23%	9%	21%	20%			
Non-Interest Income	38	44	51	64	43	52	66	2%	-2%	-2%
--Growth YoY	23%	15%	16%	26%	12%	22%	26%			
Total Income	133	142	170	210	146	176	214	-3%	-3%	-2%
--Growth YoY	17%	7%	20%	24%	10%	21%	22%			
Opex	72	80	92	106	82	95	109	-3%	-3%	-3%
--Growth YoY	16%	12%	15%	15%	15%	15%	15%			
PPOP	61	61	78	104	63	81	105	-3%	-4%	-1%
--Growth YoY	18%	1%	27%	34%	3%	29%	30%			
Provision	7	16	16	19	13	15	18	20%	8%	8%
--as a % of avg. loans	33	61	56	56	51	51	51			
PBT	54	46	62	85	50	66	87	-8%	-7%	-3%
Tax	13	12	16	21	13	17	22	9%	7%	3%
PAT	41	34	46	64	38	49	65	-8%	-7%	-3%
--Growth YoY	9%	-15%	34%	38%	-7%	31%	32%			
Advances	2,348	2,701	3,173	3,729	2,759	3,242	3,810	-2%	-2%	-2%
--Growth YoY	12%	15%	18%	18%	18%	18%	18%			
Deposits	2,836	3,262	3,784	4,389	3,290	3,817	4,427	-1%	-1%	-1%
--Growth YoY	12%	15%	16%	16%	16%	16%	16%			
Book Value	136	151	168	193	151	170	195	0%	-1%	-1%
--Growth YoY	14%	11%	12%	15%	11%	13%	15%			
EPS	17	14	19	26	15	20	27	-8%	-7%	-3%
--Growth YoY	3%	-16%	34%	38%	-8%	31%	32%			
ROA	1.2%	0.9%	1.1%	1.3%	1.0%	1.1%	1.3%	-8	-6	-2
ROE	13.0%	9.8%	11.7%	14.3%	10.6%	12.5%	14.5%	-87	-73	-20

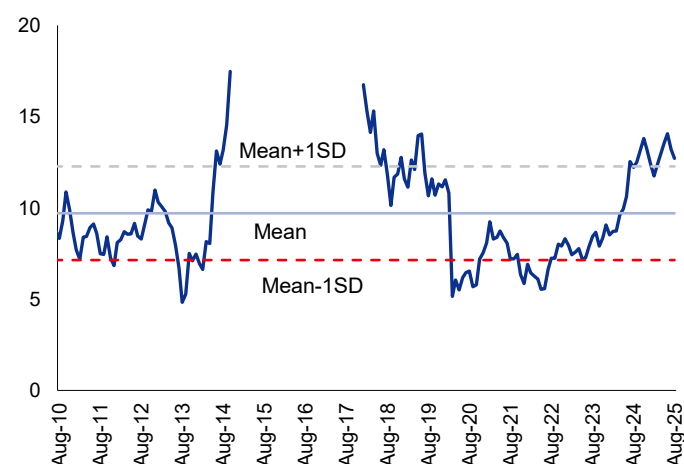
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 3: One-year forward P/BV



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 4: One-year forward P/E



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Earnings highlights

- Gross slippage increased to Rs6.6bn (1.2% annualized) vs. Rs4.9bn (0.9%) last quarter. This was mainly owing to the slippage from MFI & agri segments. Excluding this, slippage was broadly steady across other segments. Management indicated that MFI collection efficiency and SMA flows have improved in Jun/Jul vs. May 2025. Moreover, there was marginal increase in stress in the lower bucket of business banking and CV/CE segments but is not a cause of worry currently. Recovery/upgrades were lower (Rs1.6bn vs. 4.3bn; partly seasonal) and write-offs also declined QoQ (Rs2.1bn vs. Rs2.4bn). This led to a rise in gross non-performing assets or GNPA's by 7% QoQ to Rs46.7bn. The GNPA ratio inched up by 7bp QoQ to 1.91%. The PCR ratio moderated QoQ (75.2% vs. 76.2%). The net NPA ratio inched up to 0.48%.
- Loan growth (pre-IBPC) was 9% YoY vs. 13% YoY last quarter. Sequentially, growth was 1% vs. 2% last quarter. Growth was mainly contributed by gold loans (14% YoY; 2% QoQ), CV/CE segments (30% YoY; 5% QoQ) and commercial banking (27% YoY; 6% QoQ). The retail loan book grew by 6% YoY (flat QoQ). The MFI book grew by 5% YoY (down 4% QoQ).

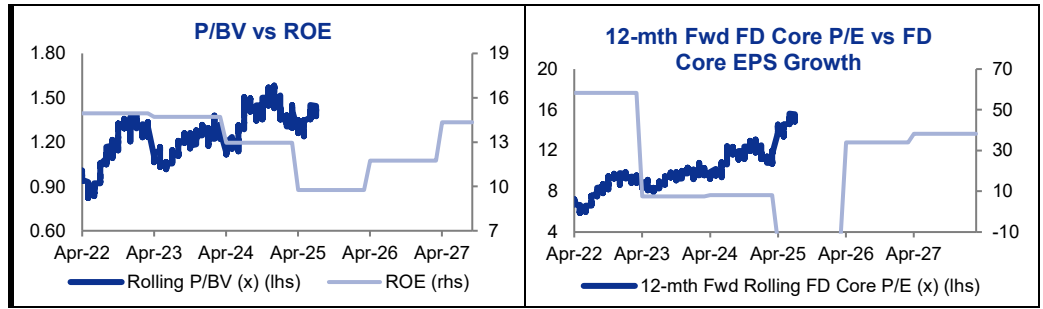
- Opex growth was contained at 11% YoY (down 1% QoQ). Management gave guidance of an elevated cost-to-income ratio at mid-50s in the near- to medium- term as the bank continues to invest in people/processes, digital initiatives, network expansion, and distribution.
- The bank clocked an annualized RoA of 1% in 1QFY26 and indicated that structural RoA drivers are well in place. These include a) improving fee income to assets (led by wealth product offerings, trade/fx and credit cards, b) improving low-cost liability franchise (particularly current accounts) and c) improving yields by changing the lending mix towards better-yield segments (and not by increasing the inherent portfolio risk).

Figure 5: Financial summary

Federal Bank					Per Share Data and Valuations				
Profit and Loss Statement									
Rs Mn (Year-end March)	FY25	FY26F	FY27F	FY28F	Rs Mn (Year-end March)	FY25	FY26F	FY27F	FY28F
Interest Income	263,652	279,981	327,072	384,482	EPS	16.6	14.0	18.7	25.9
Interest Expense	168,973	182,053	207,863	238,318	Book Value	136.1	150.7	168.4	192.9
Net Interest Income	94,680	97,928	119,209	146,164	Book Value (Core)	133.9	147.9	165.7	190.1
—Fee Income	27,970	33,618	42,023	54,629	Core Op. Profit	20.8	20.9	28.1	38.6
—Capital Gains	2,650	2,770	2,000	2,000	DPS	1.2	1.0	1.4	1.9
—Miscellaneous Inc.	5,443	5,000	4,000	4,000					
Total Non Interest Income	38,013	43,710	50,809	63,973	Valuations				
Total Operating Income	132,692	141,638	170,018	210,137	P/E	11.8	14.0	10.4	7.6
—Employee Exp	30,827	33,848	38,925	44,764	P/E (Core)	10.7	12.7	9.5	6.9
—Other Expenses	40,854	46,297	53,242	61,228	Price to Book	1.4	1.3	1.2	1.0
Total Operating Expenses	71,681	80,145	92,167	105,992	Price to Book (Core)	1.3	1.2	1.1	0.9
Operating Profit	61,011	61,493	77,851	104,145	Price to Core PPOP	9.4	9.3	7.0	5.1
—Prov. For Investment Dep.	-150	-10	0	0	Core Price to Core PPOP	8.5	8.5	6.3	4.6
—Loan Loss Provisions	8,030	14,329	14,674	17,242	Dividend Yield	0.6%	0.5%	0.7%	1.0%
Total provisions	7,331	15,510	16,328	19,185					
Profit Before Tax	53,681	45,982	61,523	84,960	Ratio Analysis				
Provision for Tax	13,162	11,618	15,504	21,410	Rs Mn (Year-end March)	FY25	FY26F	FY27F	FY28F
Net Profit	40,519	34,365	46,019	63,550	Spread Analysis				
					Average yield on assets	8.5%	7.8%	7.9%	8.1%
					Cost of earning assets	5.4%	5.1%	5.0%	5.0%
					Net Interest Margin (Reported)	3.13%	2.93%	3.09%	3.30%
					Growth Ratios				
					Net Interest Income	14%	3%	22%	23%
					Non Interest Income	23%	15%	16%	26%
					Operating expenses	16%	12%	15%	15%
					Core PPOP	18%	1%	34%	37%
					Operating Profit	18%	1%	27%	34%
					Net Profit	9%	-15%	34%	38%
					EPS	3%	-16%	34%	38%
					Deposits	12%	15%	16%	16%
					Advances	12%	15%	18%	18%
					Total Assets	13%	15%	15%	15%
					Profitability Ratios				
					Return On Equity	13.0%	9.8%	11.7%	14.3%
					Return On Equity (Core)	13.2%	9.9%	12.0%	14.6%
					Return on Assets	1.2%	0.9%	1.1%	1.3%
					Core PPOP/Avg Loans	2.3%	2.0%	2.4%	2.7%
					Efficiency Ratios				
					Cost Income Ratio	54.0%	56.6%	54.2%	50.4%
					Expenses/Avg Assets	2.2%	2.1%	2.1%	2.1%
					Capital Ratios				
					CET 1 Ratio	15.0%	13.9%	13.6%	13.6%
					Tier 1 Ratio	15.0%	13.9%	13.6%	13.6%
					Tier 2 Ratio	1.4%	1.3%	1.2%	1.2%
					Capital Adequacy Ratio	16.4%	15.2%	14.9%	14.9%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS



Profit & Loss

(Rsm)	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Net Interest Income	82,935	94,680	97,928	119,209	146,164
Total Non-Interest Income	30,793	38,013	43,710	50,809	63,973
Operating Revenue	113,728	132,692	141,638	170,018	210,137
Total Non-Interest Expenses	(61,983)	(71,681)	(80,145)	(92,167)	(105,992)
Pre-provision Operating Profit	51,745	61,011	61,493	77,851	104,145
Total Provision Charges	(1,961)	(7,331)	(15,510)	(16,328)	(19,185)
Operating Profit After Provisions	49,784	53,681	45,982	61,523	84,960
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	49,784	53,681	45,982	61,523	84,960
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	49,784	53,681	45,982	61,523	84,960
Exceptional Items					
Pre-tax Profit	49,784	53,681	45,982	61,523	84,960
Taxation	(12,578)	(13,162)	(11,618)	(15,504)	(21,410)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	37,206	40,519	34,365	46,019	63,550
Minority Interests					
Pref. & Special Div					
FX And Other Adj.					
Net Profit	37,206	40,519	34,365	46,019	63,550
Recurring Net Profit					

Balance Sheet Employment

(Rsm)	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Gross Loans/Cust Deposits					
Avg Loans/Avg Deposits	82.4%	82.9%	82.8%	83.4%	84.4%
Avg Liquid Assets/Avg Assets	93.3%	94.5%	95.4%	95.7%	95.8%
Avg Liquid Assets/Avg IEAs	107.4%	108.7%	110.4%	110.7%	111.0%
Net Cust Loans/Assets					
Net Cust Loans/Broad Deposits					
Equity & Provns/Gross Cust Loans					
Asset Risk Weighting					
Provision Charge/Avg Cust Loans	0.10%	0.33%	0.61%	0.56%	0.56%
Provision Charge/Avg Assets	0.07%	0.22%	0.41%	0.38%	0.39%
Total Write Offs/Average Assets					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet

(Rsm)	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Total Gross Loans	2,094,033	2,348,364	2,700,619	3,173,227	3,728,542
Liquid Assets & Invst. (Current)	608,595	662,456	767,663	802,539	842,303
Other Int. Earning Assets					
Total Gross Int. Earning Assets	2,702,629	3,010,820	3,468,282	3,975,766	4,570,845
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets	2,702,629	3,010,820	3,468,282	3,975,766	4,570,845
Intangible Assets					
Other Non-Interest Earning Assets	180,660	155,853	155,853	179,231	206,115
Total Non-Interest Earning Assets	190,860	170,636	171,744	196,314	224,480
Cash And Marketable Securities	189,629	308,592	364,139	429,684	507,027
Long-term Investments					
Total Assets	3,083,118	3,490,048	4,004,165	4,601,764	5,302,352
Customer Interest-Bearing Liabilities	2,525,340	2,836,475	3,261,946	3,783,857	4,389,275
Bank Deposits					
Interest Bearing Liabilities: Others					
Total Interest-Bearing Liabilities	2,705,604	3,073,738	3,511,072	4,052,914	4,679,855
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	86,570	82,104	123,156	135,472	149,019
Total Liabilities	2,792,174	3,155,842	3,634,228	4,188,385	4,828,874
Shareholders Equity	290,944	334,206	369,937	413,379	473,478
Minority Interests					
Total Equity	290,944	334,206	369,937	413,379	473,478

Key Ratios

	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Total Income Growth	14.7%	14.2%	3.4%	21.7%	22.6%
Operating Profit Growth	7.9%	17.9%	0.8%	26.6%	33.8%
Pretax Profit Growth	23%	8%	(14%)	34%	38%
Net Interest To Total Income	72.9%	71.4%	69.1%	70.1%	69.6%
Cost Of Funds	5.52%	5.85%	5.53%	5.50%	5.46%
Return On Interest Earning Assets	9.0%	9.2%	8.6%	8.8%	9.0%
Net Interest Spread	3.47%	3.38%	3.11%	3.29%	3.54%
Net Interest Margin (Avg Deposits)	3.56%	3.53%	3.21%	3.38%	3.58%
Net Interest Margin (Avg RWA)					
Provisions to Pre Prov. Operating Profit	4%	12%	25%	21%	18%
Interest Return On Average Assets	2.92%	2.88%	2.61%	2.77%	2.95%
Effective Tax Rate	25.3%	24.5%	25.3%	25.2%	25.2%
Net Dividend Payout Ratio	7.4%	7.2%	7.5%	7.5%	7.5%
Return On Average Assets	1.31%	1.23%	0.92%	1.07%	1.28%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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Recommendation Framework

Stock Ratings

Definition:

- Add** The stock's total return is expected to exceed 10% over the next 12 months.
- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
- Reduce** The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

- Overweight** An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

- Overweight** An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral** A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight** An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.