

SD/LODR/277/2024-25

October 22,2024

<p>The Manager Listing Department The National Stock Exchange of India Limited Exchange Plaza, Bandra-Kurla Complex, Bandra (E), Mumbai – 400 051</p>	<p>The Manager Department of Corporate Services BSE Limited Phiroze Jeejeebhoy Towers, Floor 25, Dalal Street, Mumbai – 400 001</p>
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Re: Scrip Symbol: FEDERALBNK/Scrip Code: 500469

Sub: Intimation regarding affirmation and Assignment of Credit Rating

Dear Sir/Madam,

Pursuant to Regulation 30 of the Listing Regulations, we wish to inform you that India Ratings and Research (Ind-Ra) has affirmed and assigned credit rating to the Tier-II Bonds and infrastructure Bonds of the Bank as mentioned below.

Instrument Description	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating Assigned along with Outlook/Watch	Rating Action
Basel III Tier 2 debt	-	-	-	INR17 (reduced from INR20)	IND AA+/Stable	Affirmed
Infrastructure bond	-	-	-	INR15	IND AA+/Stable	Assigned

Detailed press-release of the aforesaid affirmation and assignment of Credit Rating is enclosed herewith.

Kindly take the above information on record.

Thanking you,

Yours faithfully,

For The Federal Bank Limited

Samir P Rajdev
Company Secretary

India Ratings Affirms The Federal Bank's Bank's Basel III Tier 2 Bonds at 'IND AA+/ Stable'; Rates Infrastructure Bonds

Oct 21, 2024 | Private Sector Bank

India Ratings and Research (Ind-Ra) has taken the following rating actions on The Federal Bank Limited's (FBL) debt instruments:

Details of Instruments

Instrument Description	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating Assigned along with Outlook/Watch	Rating Action
Basel III Tier 2 debt*	-	-	-	INR17 (reduced from INR20)	IND AA+/Stable	Affirmed
Infrastructure bond#	-	-	-	INR15	IND AA+/Stable	Assigned

*Details in annexure

Unutilised

Analytical Approach

Ind-Ra continues to take a standalone view of FBL for the rating review.

Detailed Rationale of the Rating Action

The affirmation reflects the consistent strengthening of FBL's credit profile as reflected in scaling up of franchise, stable liability franchise, improving diversification of its loan portfolio outside the home state (Kerala), a reasonably well-managed asset quality and improved profitability buffers.

List of Key Rating Drivers

Strengths

- Sizeable franchise with reducing concentration in home state
- Strengthened management team
- Stable and adequately provided asset quality
- Incremental improvement in profitability to be driven by focus on growing high yielding book
- Adequate capital buffers

Weaknesses

- Developing funding profile

Detailed Description of Key Rating Drivers

Sizeable Franchise with Reducing Concentration in Home State: FBL continues to have a large presence in the southern states of the country with a huge asset and liability franchise. The bank is diversifying away from Kerala, where its share in the overall advances moderated to 30.57% in 1QFY25 (FY15: 42.6%), while the share of Tamil Nadu and

Karnataka rose to 13.19% (11.2%) and 9.27(6.5%), respectively. As of 1QFY25, the bank's loan portfolio was INR2,208 billion (of which 53.03% originated in Kerala, Tamil Nadu and Karnataka) and it had a deposit base of INR2,660 billion (56.5%% in Kerala). Also, the bank's incremental efforts are on increasing its share in Maharashtra, whose advance share has increased to 21.24% in 1QFY25 (FY15: 19.7%) and deposits share to 13.75% (8.1%).

Furthermore, the bank has a well-diversified advances portfolio across segments, comprising corporates (1QFY25: 34.0%; FY24:34.3; FY23: 36.8%), retail (1QFY25: 31.1%; FY24:31.4%; FY23: 31.5%), small and medium-sized enterprises (SMEs; 1QFY25: 19.8%; FY24:19.6%; FY23: 18.6%) and agriculture (1QFY25: 13.4%; FY24:13.1%; FY23: 12.3%,). The retail loan book grew 25% yoy in 1QFY25, against the overall gross loan growth of 20.3% yoy. The gold loan book grew 31.1% yoy to INR274.3 billion in 1QFY25, accounting for 12.2% of the overall gross loan book.

Strengthened Management Team: The bank has had a substantial number of lateral hires across key verticals, who bring in significant amount of experience and knowledge with them, thus enhancing management capabilities. Mr. KVS Manian was appointed as the managing director and chief executive officer of FBL by the Reserve Bank of India for a term of three years from September 2024. The bank has established a second-layer team under each business vertical head to adapt to any transition at the senior level.

As part of its strategy, the management continues to focus on retailisation of the loan book with controlled risk underwriting, adoption of digitisation to improve branch-level productivity and increasing the wallet share with customers. The management has stated that the unsecured lending would be capped at 10% of the overall assets under management, which could be achieved over the course of the next two financial years. Under large corporates, the bank aims to lend to higher-rated entities while focusing on driving growth through mid-corporate segment in the medium-to-long term.

Stable and Adequately Provided Asset Quality: The bank's gross non-performing assets moderated to 2.11% in 1QFY25 (FY24: 2.13%; FY23: 2.36%; FY22: 2.8%), with improved recoveries and upgradation. FBL's provision coverage ratio improved to 70.79% in 1QFY25 (FY24: 71.08%, FY23: 70.23%). However, the absence of any large, stressed exposure will contain the impact on credit cost and normalise the same in the medium term. The concentration risk, in terms of the top 20 group exposures to the total advances, remained at 7.73% in FY24 (FY23: 8.03%).

FBL's total stressed book (net non-performing assets + standard restructured assets + net security receipts) stood at 1.43% of the loan book at 1QFY25 (FY24: 1.57%, FY23: 2.31%), and net stressed asset/net worth stood at 10.3% (11.3%; 18.8%). Ind-Ra expects the impaired book to stabilise in the medium term, along with incremental loan growth in better-rated borrowers and increased focus on retail growth.

Incremental Improvement in Profitability to be Driven by Focus on Growing High Yielding Book: FBL's net interest margin declined 4bp yoy to 3.16% in 1QFY25 (FY24:3.20%; FY23: 3.37%), largely because of higher flows towards term deposits and lower current account savings account ratio. However, the overall deposits profile was supported by its strong low-cost retail liability franchise, a shift in loan mix towards high-yielding retail loans and the increase in gold loan proportion in the overall book. FBL's profitability remains adequate on risk-adjusted basis; where profit after tax to risk weighted assets stood at 2.05% for 1QFY25 (FY24: 1.96%; FY23: 1.92%), largely due to the lower credit cost and improved loan book growth, which stands comparable with peers'.

Furthermore, while the bank expects the retail/wholesale share to remain intact at 56:44, the share of higher yielding book (excluding gold loans), which includes credit cards, personal loans, Micro, Small and Medium Enterprises (business loan + commercial banking; 18.2%), commercial vehicle/commercial equipment and microfinance is improving and stood at about 24.8% in 1QFY25 (1QFY24: 22.7%). The share of these segments in the bank's interest income increased to 28.0% from 25.3% during the same period.

The bank's pre-provision operating profit buffer (FY24: 1.84% of average assets; FY23: 1.99%; FY22: 1.79%) has largely remained stable. However, the pre-provision operating profit buffer stands lower than that of higher rated banks. The bank's pensionable employees share in the total employees has been moderating. Management expects the share of

pensionable employees would further moderate in the medium term with increased seasoning, thereby moderating the volatility in employee cost with movements in interest rates. The bank has guided to maintain a cost/income ratio of around 50% in the medium term.

Adequate Capital Buffers: FBL's capitalisation (1QFY25 Tier 1 ratio: 14.2%, FY24: 14.6%, FY23: 13.0%) increased due to higher internal accruals and capital raise of INR9.59 billion in July 2023 from International Finance Corporation and INR30.40 billion from a qualified institutional placement. The bank also has a material stake in its subsidiaries, which can be liquidated in the event of stress. According to Ind-Ra's stress test, FBL is likely to maintain a common equity tier-1 (CET1) ratio above the regulatory minimum and system average, and the management has guided it will maintain the floor threshold of CET1 ratio at 12%.

Developing Funding Profile: FBL has a well-diversified granular deposit profile with a low reliance on bulk deposits. Its granular deposits (deposits lower than INR30 million) constituted 80% of the total deposits as of 1QFY25 with the overall current accounts and savings accounts constituting 29.3% of the total deposits. Kerala is a home town for non-resident Indians (NRIs) where all accounts reside. The origination of deposits takes place outside India and across various states in India, thereby moderating the geographical concentration risk. Non-resident external deposits stood at 28.9% of the total deposits in 1QFY25 (FY24: 31.8%, FY23: 30.1%) and has moderated over the years. Further, the bank has maintained its NRI deposits share/total deposits and its share in NRI remittances was 18.75% as of FY24 (FY23: 19.3%; FY22: 21.06%; FY21: 18.20%). This large granular funding is helping FBL to maintain lower funding costs than that of its large peers. The bank has shown stability in maintaining and gaining the share of NRI remittances in Kerala. However, rising competition and impact of inflation across capital flows could slowdown accretion of NRI deposits, which remains a rating monitorable.

The bank is using its relationships on the wholesale side to bring in corporate salary customers and open current account deposits. The bank has a tie-up with Jupiter and Epifi on the liability side, and it plans to tap the customer base of these fintechs for credit cards and personal loan products. The product per customer is still below two, which has the potential to further increase.

Liquidity

Adequate: FBL maintained a cumulative funding deficit of 11.0% in the cumulative one-year bucket as a percentage of the total assets at end-1QFY25. FBL also maintains 16.9% of its total assets in government securities and balances with the Reserve Bank of India. More than adequate liquidity buffers are maintained to meet its short-term funding requirements. The bank also had a comfortable consolidated quarterly average liquidity coverage ratio of 112.61% in 1QFY25, higher above the regulatory requirement of 100%.

Rating Sensitivities

Positive: FBL's improved visibility on the diversification of asset profile outside its core geographies, sustained market share gains on both assets and liabilities, traction in the new retail products with adequate seasoning, build-up of other non-interest revenue streams, along with a sustained diversification in operating geographies comparable to peers will lead to a positive rating action.

Negative: Events that could, individually or collectively, lead to a negative rating action are:

- deterioration in the funding profile due a fall in low-cost deposits, a rise in operating expenses, a prolonged decline in the profitability buffers driven by asset quality pressures and any deviation from the aforementioned positive rating sensitivities above Ind-Ra's expectations,
- any material impact on Tier I capitalisation levels with CET1 capital falling below 12% on a sustained basis,
- a significant increase in net non-performing assets or a decline in CET1,
- a significant erosion of the franchise (sustained reduction of market share in advances or deposits),
- a weakening of the bank's competitiveness in the industry.

ESG Issues

ESG Factors Minimally Relevant to Rating: Unless otherwise disclosed in this section, the ESG issues are credit neutral or have only a minimal credit impact on FBL, due to either their nature or the way in which they are being managed by the entity. For more information on Ind-Ra's ESG Relevance Disclosures, please click [here](#). For answers to frequently asked questions regarding ESG Relevance Disclosures and their impact on ratings, please click [here](#).

About the Company

FBL was established in 1931 in Aluva (Kerala), and is classified as an old private sector bank by the Reserve Bank of India. FBL is the second-largest bank and the largest private sector bank in Kerala, with nearly 42% of its 1,518 Banking Outlets located in the state. The bank has a strong retail funding franchise, including a stable base of NRI deposits, largely contributed by remittances from the expatriate Indian community in the Middle East.

Key Financial Indicators

Particulars	FY24	FY23
Total assets (INR billion)	3,083.1	2,603.4
Total net worth (INR billion)	290.9	214.2
Net profit (INR billion)	37.2	30.1
Return on assets (%)	1.32	1.28
Tier 1 ratio (%)	14.6	13.0
Capital adequacy ratio (%)	16.1	14.8
Gross non-performing asset ratio (%)	2.13	2.36
Impaired asset (net non-performing assets + standard restructured assets + net SR) as percentage of advances (%)	1.57	2.31
Source: Federal Bank, Ind-Ra		

Status of Non-Cooperation with previous rating agency

Not applicable

Rating History

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook			
	Rating Type	Rated Limits (billion)	Rating	9 February 2024	27 February 2023	8 July 2022	14 September 2021
Basel III Tier 2 debt	Long-term	INR17	IND AA+/Stable	IND AA+/Stable	IND AA/Positive	IND AA/Positive	IND AA/Stable
Infrastructure bond	Long-term	INR15	IND AA+/Stable	-	-	-	-

Complexity Level of the Instruments

Instrument Type	Complexity Indicator
Basel III Tier 2 debt	Medium
Infrastructure bond	Low

For details on the complexity level of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

Annexure

Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook
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Basel III Tier 2 debt	INE171A08024	20 June 2019	9.75	20 June 2029	INR3	WD (paid in full)
Basel III Tier 2 debt	INE171A08032	20 January 2022	8.20	20 January 2032	INR7	IND AA+/Stable
Basel III Tier 2 debt	INE171A08040	29 March 2023	8.84	29 March 2033	INR9.95	IND AA+/Stable
				Total utilised	INR16.95	
				Total unutilised	INR0.05	

Source : NSDL , Federal Bank

Contact

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About India Ratings and Research: India Ratings and Research (Ind-Ra) is committed to providing India's credit markets accurate, timely and prospective credit opinions. Built on a foundation of independent thinking, rigorous analytics, and an open and balanced approach towards credit research, Ind-Ra has grown rapidly during the past decade, gaining significant market presence in India's fixed income market.

Ind-Ra currently maintains coverage of corporate issuers, financial institutions (including banks and insurance companies), finance and leasing companies, managed funds, urban local bodies and project finance companies.

Headquartered in Mumbai, Ind-Ra has seven branch offices located in Ahmedabad, Bengaluru, Chennai, Delhi, Hyderabad, Kolkata and Pune. Ind-Ra is recognised by the Securities and Exchange Board of India, the Reserve Bank of India and National Housing Bank.

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For more information, visit www.indiaratings.co.in.

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APPLICABLE CRITERIA AND POLICIES

Rating Bank Subordinated and Hybrid Securities

Evaluating Corporate Governance

Financial Institutions Rating Criteria

The Rating Process

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