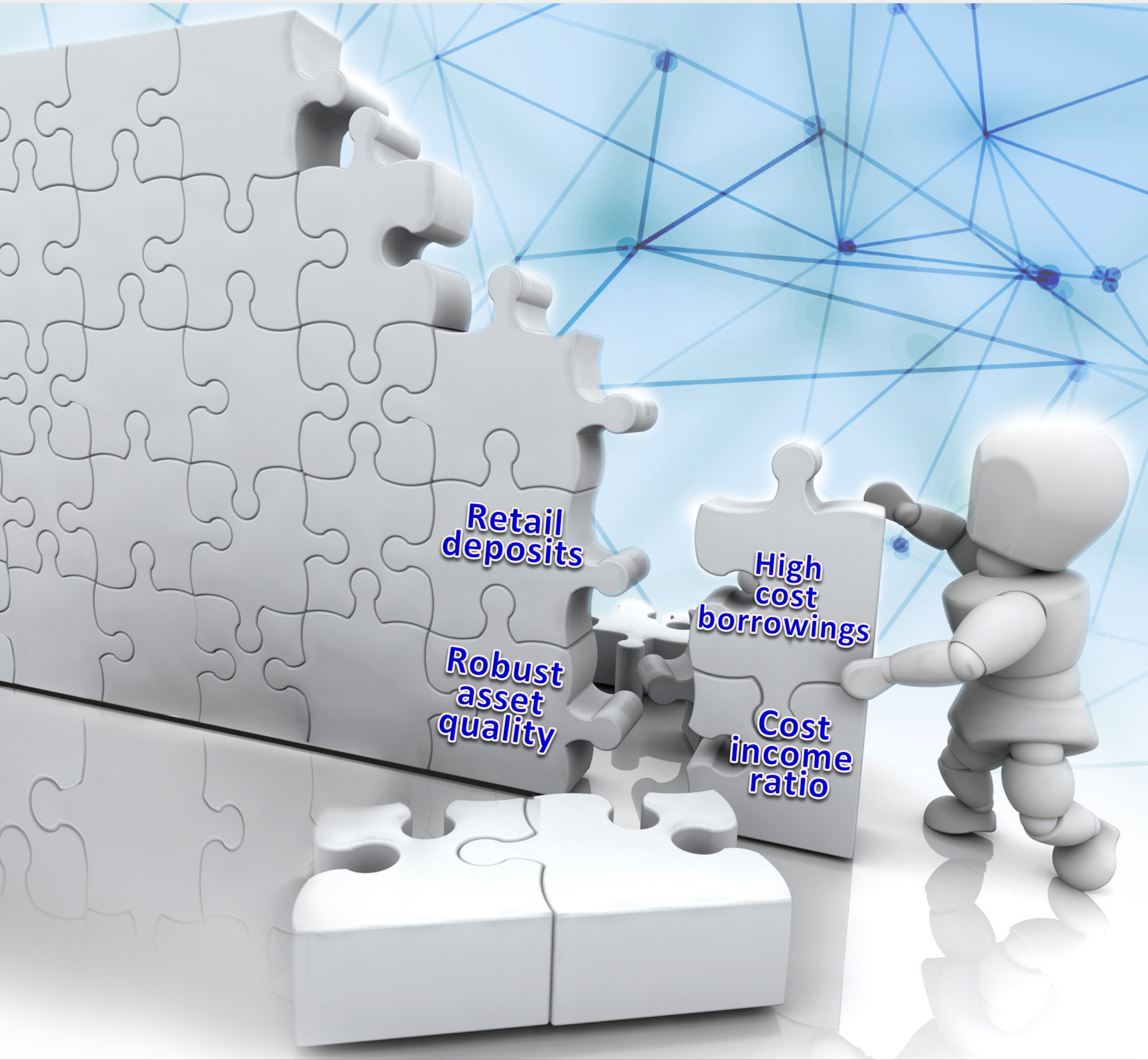
October 2022

Initiating Coverage | Sector: Financials

IDFC First Bank



A better tomorrow!

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IDFC First Bank: A better tomorrow!

MOTILAL OSWAL

IDFC First Bank

BSE SENSEX	S&P CNX
57,920	17,186

Bloomberg	IDFCFB IN
Equity Shares (m)	6219
M.Cap.(INRb)/(USDb)	337.5 / 4.1
52-Week Range (INR)	56 / 29
1, 6, 12 Rel. Per (%)	11/32/15
12M Avg Val (INR M)	1583
Free float (%)	63.5

Financials & Valuations (INR b)

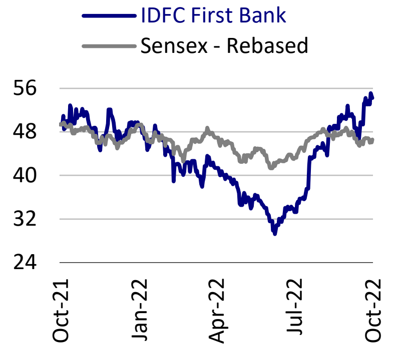
Y/E MARCH	FY23E	FY24E	FY25E
NII	120.2	144.0	176.8
OP	45.3	59.0	80.8
NP	22.1	30.1	39.1
NIM (%)	6.4	6.4	6.5
EPS (INR)	3.6	4.8	6.3
EPS Gr. (%)	NM	35.8	29.9
BV/Sh. (INR)	37.3	42.1	48.4
Ratios			
RoE (%)	10.0	12.2	13.9
RoA (%)	1.1	1.2	1.3
Valuations			
P/E(X)	15.2	11.2	8.6
P/BV (X)	1.5	1.3	1.1
P/ABV (X)	1.6	1.4	1.2

Shareholding pattern (%)

As On	Jun-22	Mar-22	Jun-21
Promoter	36.5	36.5	36.6
DII	14.4	13.8	16.1
FII	11.0	13.5	15.1
Others	38.1	36.2	32.2

FII Includes depository receipts

Stock's performance (one-year)



CMP: INR54 TP: INR70 (+29%) Buy

A better tomorrow!

Liability re-pricing and operational efficiency to drive RoE

- **IDFC First Bank (IDFCFB) has strengthened its balance sheet over the past few years as it consciously increased the mix of retail business. The bank reported 5x growth in retail deposits over the past three years and simultaneously improved CASA mix to 50%. Further, the retail loan book posted an impressive 31% CAGR over FY19-22.**
- **IDFCFB is well positioned to benefit from gradual run-down of its high-cost legacy borrowings over FY23-26E (INR224b at 8-9% cost) and replace them with deposits (at ~5.5% cost). ~77% of such bonds will be refinanced by FY25E. This will potentially add ~INR7.5-8.0b to NII (FY22 NII: INR97b) in due course.**
- **IDFCFB has made substantial investments in building the franchise, which has resulted in sub-optimal cost metrics. However, we expect the operating leverage to improve (C/I ratio at 66% by FY25 vs 75% in FY22) thereby aiding earnings.**
- **The bank is entering a phase of strong loan growth as the drag from wholesale book moderates. This will be aided by a strong growth in profitability due to replacement of high-cost borrowings, better cost trends and controlled credit costs (1.3-1.5%).**
- **We estimate return ratios to improve sharply with RoA/RoE reaching 1.3%/ 13.9% in FY25E, respectively. We initiate coverage with a 'BUY' rating and a TP of INR70 (premised on 1.5x Sep'24E BV). A key near term event would be the merger of IDFC Ltd and IDFCFIRST. IDFC owns 36.5% stake and both entities have accorded in-principle approval towards the merger (link1/link2).**

Loan book retailization on track; estimate 21% loan CAGR over FY22-25

IDFCFB's strategy since the time of the merger with Capital First has revolved around building a loan book with a primary focus on retail assets. The share of retail assets thus rose to 74% in 1QFY23 from 38% in FY19 – well ahead of the timelines the bank had set for itself at the time of the merger. Over the past three years, overall funded assets reported a modest 6% CAGR as the wholesale book declined 46% due to run-down of legacy infra book while retail and commercial loans posted 31% CAGR. Thus, the share of wholesale book/ legacy (infra) reduced dramatically to 26%/5% in FY22 from 62%/19% in FY19, respectively. We now estimate total loans to clock 21% CAGR over FY22-25E as the drag from wholesale book moderates.

Well-diversified retail asset base with balanced share of all segments

IDFCFB has scaled up its retail and commercial loan book at a robust pace of 31% CAGR over FY19-22. Within this, the share of different segments such as consumer loans, home loans, LAP, rural finance, wheels and commerical loans is fairly well balanced with mortgage (including LAP) accounting for 37% of total loan book. Credit card has a low share in the mix (2%) as it is a recently launched product and is in a scale-up phase.

Deposit franchise scaling up rapidly; CASA mix improves to 50%

The bank has progressed fairly well on the liabilites front and scaled up retail liabilities at an impressive 73% CAGR during FY19-22. Thus, the share of retail deposits has increased to 67% in 1QFY23 from 19% in FY19.

Since the merger, IDFCFB has consistently expanded its footprint by opening 445 branches and 695 new ATMs. This has played a critical role in deposit mobilization and boosted CASA ratio to 50% in 1QFY23 from a mere 11% in FY19. Simultaneously, IDFCFB has also invested in digital platforms and capabilities. A strong brand, quality service levels, transparency and customer friendly products have enabled IDFCFB to maintain its strong deposit momentum.

Funding mix becoming stable; maturity of high-cost borrowings to aid NII

Over the past three years, the bank has diversified its funding mix in favor of low-cost customer deposits owing to its continuous efforts to build a solid retail franchise. The share of retail deposits has increased to 67% in 1QFY23 from 19% in FY19. This has made the funding structure more stable and granular. IDFCFB also continues to run-down high-cost legacy borrowings (Total: INR224b, 8-9% cost) and replace them with deposits at an average cost of ~5.5%. ~77% of such bonds will be refinanced by FY25E and will thus result in interest savings of ~INR7.5-8.0b, which in turn will boost the bank's NII and profitability in due course.

Cost ratios have peaked; operating leverage to improve gradually

To fortify its presence as a retail franchise, the bank has made investments in expanding its branch network and digital capabilities, and widen product offerings as well as increase in employee count. However, this has led to a significant increase in opex and hence its cost metrics were elevated and not comparable with peers. However, as some of these challenges ebb over the next few years, we expect the cost-income ratio to trend down gradually. Repayment of high-cost legacy borrowings will also benefit the same. Branch productivity trends are mixed v/s similar mid-sized banks and thus, there is a significant scope for improvement as the bank gains further scale.

Asset quality – legacy issues in wholesale book behind; credit cost in control

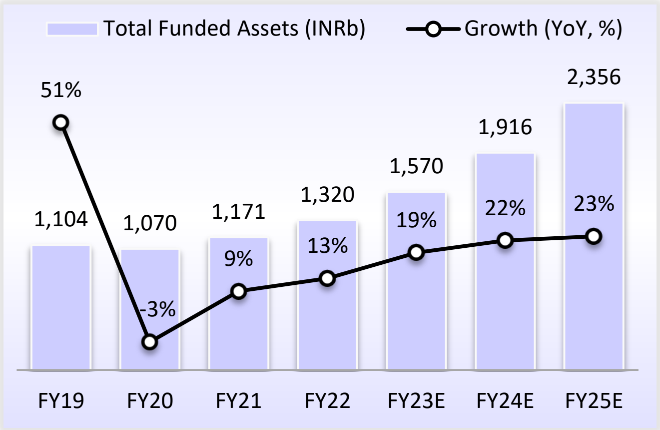
The worst of the asset quality pain is behind as retail portfolio has been reasonably stress tested during COVID-19, while all possible stressed assets in wholesale have been recognized and well provided for (PCR of 97% in the corporate segment). IDFCFB's asset quality is likely to be robust with its incremental focus on building a granular, retail portfolio where it has sharp underwriting expertise. It is gradually heading back towards its long-term trend of ~2% GNPA and 1% NNPA in retail and commercial finance book (74% of overall loans). The restructured book stands controlled at 1.3% in 1QFY23.

Valuation & View: Growth levers in place; Initiate coverage with BUY

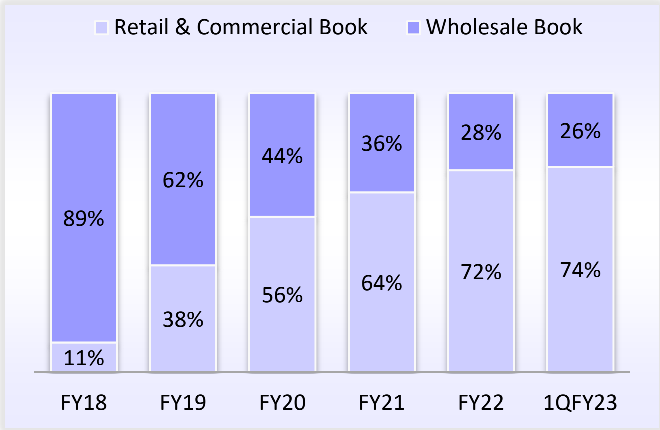
IDFCFB is entering a phase of strong loan growth as the drag from wholesale book moderates and we estimate loans to report 21% CAGR during FY22-25E. The bank has scaled up retail deposits (CASA/retail TD) at a robust 73% CAGR over FY19-22 with solid CASA mix of 50%. It has invested well in digital capabilities, branch and product expansion and has presence across retail products. Cost ratios are elevated but will moderate as scale benefits come into effect, while retirement of high-cost borrowings will aid NII growth. We estimate 35% CAGR in PPoP during FY22-25E while controlled credit costs will drive 199% CAGR in PAT over the similar period. We thus estimate RoA/RoE to reach 1.3%/13.9% in FY25E, respectively. **We initiate coverage with a 'BUY' rating and a TP of INR70 (premised on 1.5x Sep'24E BV).** **Key risks:** a) slowdown in deposit growth momentum, b) higher cost-to-income ratio, and c) headwinds in retail asset quality.

Focused charts

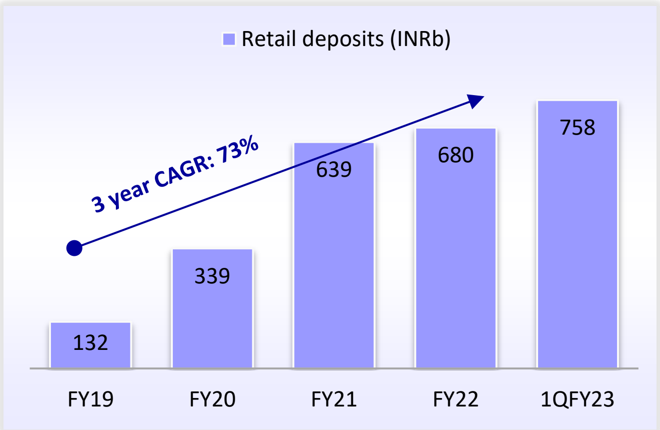
Total funded assets posted 6% CAGR during FY19-22; expect 21% CAGR over FY22-25E led by momentum in retail assets



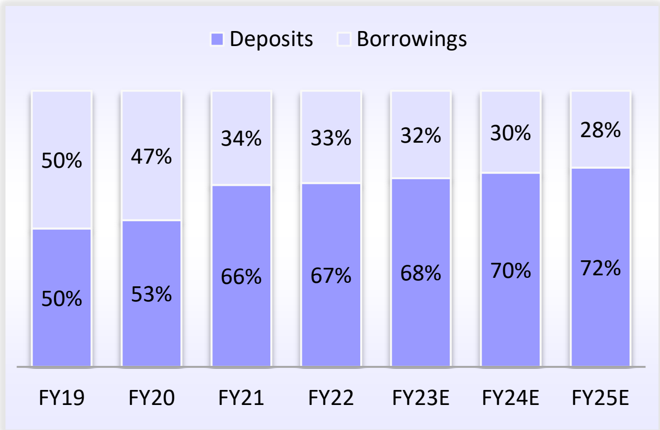
Retail portfolio has scaled up to 74% of loans due to robust traction and intentional run-down of infra (legacy) segment



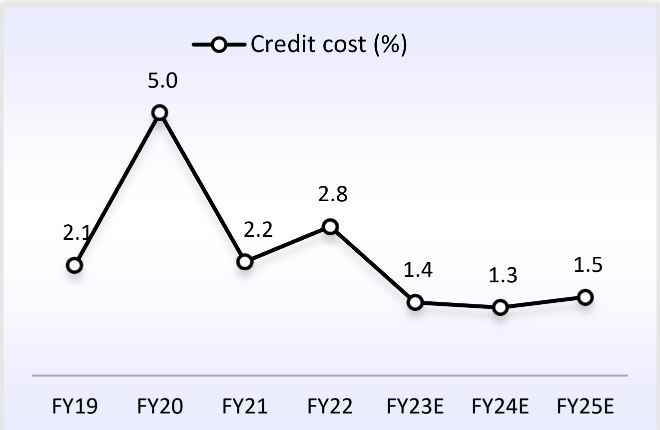
Impressive scale-up of retail deposits at 73% CAGR over FY19-22



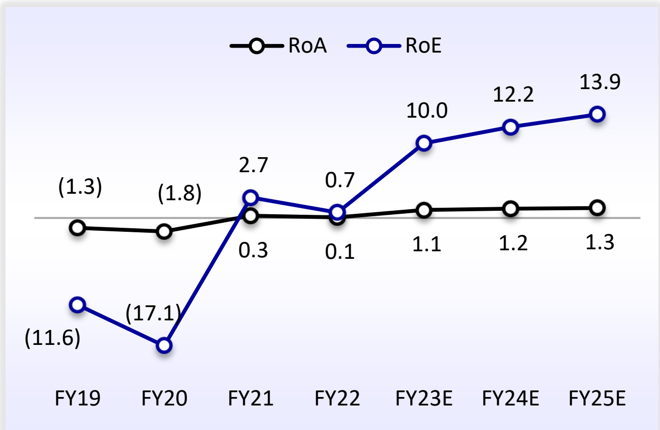
Share of deposits to rise gradually to 72% led by robust traction in deposits and retirement of high cost borrowings



Credit cost has stabilized in a narrow range between 1.3-1.5%, henceforth



Healthy NII growth, improving cost metrics and controlled credit costs to lead recovery in return ratios



Source: Company, MOFSL

Story in charts

Background of IDFC FIRST Bank

- **1997** – IDFC incorporated in Chennai on the recommendation of the Expert Group on commercialization of Infrastructure Projects
- **2005** – IDFC lists on both NSE & BSE. Raises INR13.72b of equity capital
- **2008** – Acquired AMC business of Standard Chartered Bank.
- **2011** – IDFC Mutual Fund ranked 10th by AUM
- **2012** – IDFC completes 15 years. Recognized as the best NBFC for Infrastructure Financing.
- **2014** – Secured license from RBI
- **2015** – Incorporation of IDFC Bank
- **2018** – IDFC FIRST Bank was created by the merger of Erstwhile IDFC Bank and Erstwhile Capital First
- **2019** – Journey of retailization began
- **2022** – Crossed INR500b worth of CASA deposits. Customer deposits as well as Retail & Commercial finance portfolio crossed INR1t. RoA touches ~1% in 1QFY23

Product & Digital Innovations

India's FIRST FASTAG with Triple Benefits – Toll, Fuel and Parking!

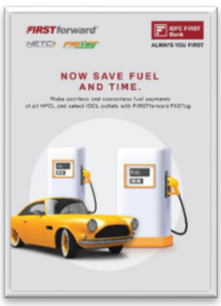
85,00,000 + Number of FASTag issued

30% Market Share
(Average Daily Toll Value Paid in June 2022)

432 Toll Plaza Merchants

39% Market Share
(Average Daily Toll Value Acquired in June 2022)

19,000 Fuel Merchants



Largest Fuel Acquirer

22 Parking Merchants

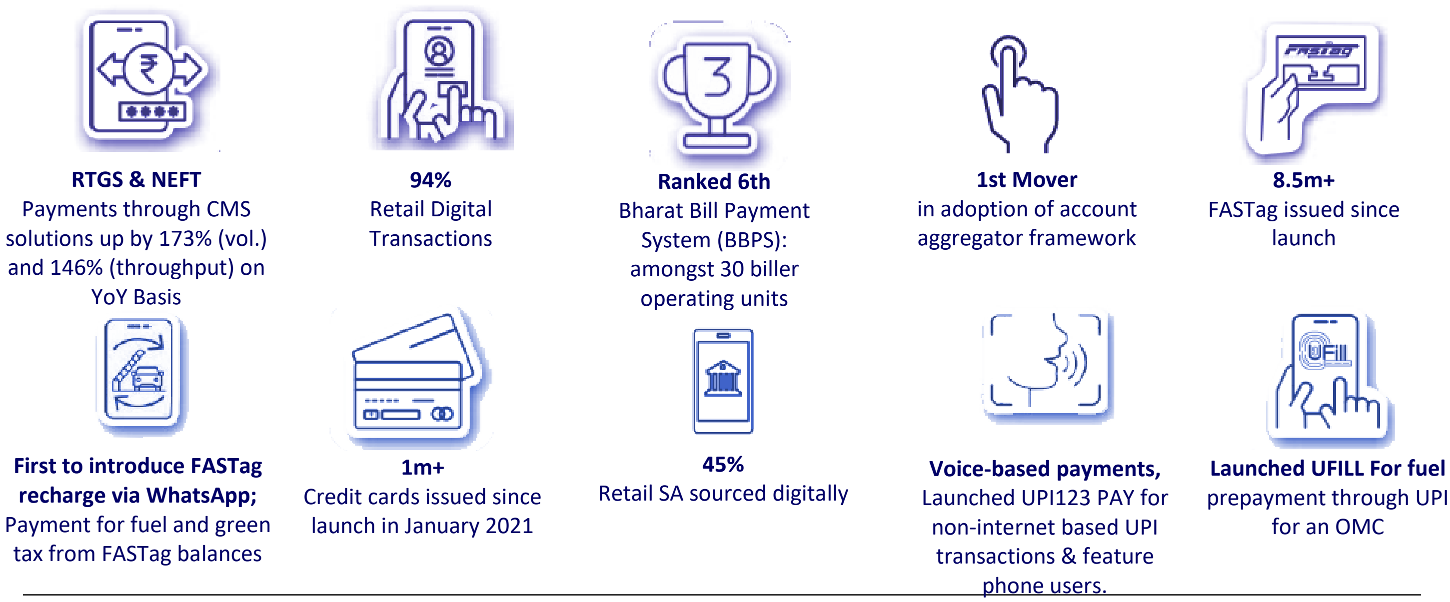
Largest Parking Acquirer

Product & Digital Innovations

The Bank has a wide bouquet of fund based and non-fund based products across urban and rural consumer, MSMEs and Corporates

The Bank has a wide range of Current and Savings Account Offerings

IDFCFB's Digital Initiatives: Significant traction on electronic platforms



Loan mix evolving into a diversified book

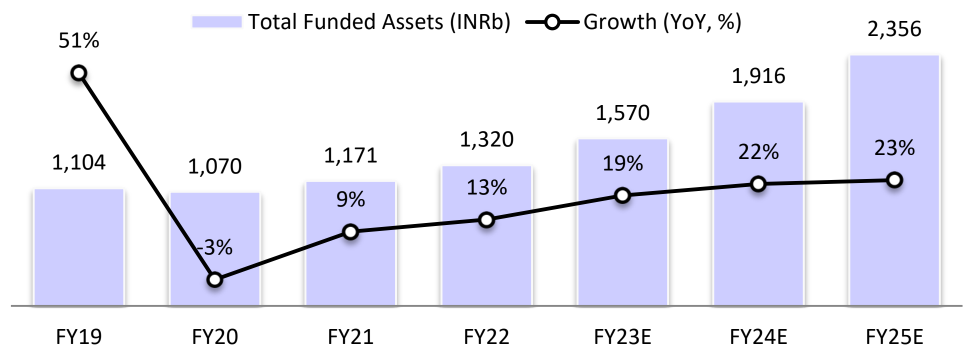
Focus on building a granular balance sheet

- IDFCFB has undergone a dramatic shift in loan book since the time of merger in Dec'18. In FY19, wholesale book formed 62% of its overall loan book while the residual 38% comprised retail loans (inherited from Erstwhile Capital First). As of FY22, the bank, however, has a much stronger retail portfolio with 72% share in overall loan book.

Dramatic shift in loan mix in favor of granular, retail assets over the last three years

- Realization of emerging risks in the lumpy infrastructure financing business and a massive opportunity in consumer finance business caused this radical shift towards retail loans.
- However, CASA/retail deposit was a key gap that needed to be plugged in for retail franchise growth and to enable IDFCFB to compete effectively with established players. Thus, the bank calibrated growth in loan book (including advances and credit investments) at a three-year CAGR (FY19-22) of only 6% as it wanted to build a strong liability franchise first. In 1QFY23, it saw a loan growth of 21% YoY.
- We estimate the loan portfolio to post 21% CAGR over the next three years as we believe that incremental loan growth can be funded through deposit mobilization. Further, retail portfolio has sustained the traction observed over the past few years and we expect it to continue.

Exhibit 1: Total funded assets posted a 6% CAGR during FY19-22; expect 21% CAGR over FY22-25E led by sustained momentum in retail assets

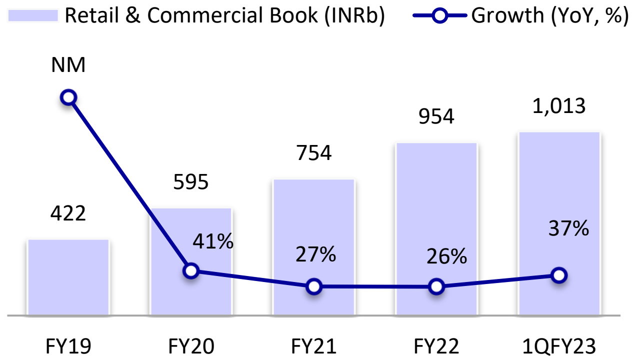


Source: MOFSL, Company

Overall loans to grow at a healthy pace led by retail as drag from wholesale reduces further

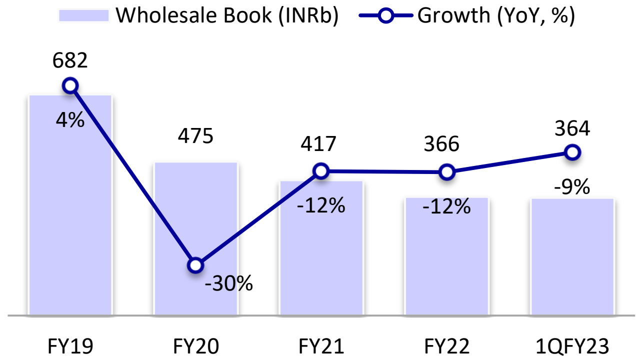
- Retail and commercial book recorded 31% CAGR during FY19-22 to reach INR954b in FY22 led by traction in segments such as home loans, consumer loans and digital and gold loans. In 1QFY23, the book grew 37% YoY to INR1.0t. This reflects the strong intent of the management in growing the retail franchise of the bank.
- While retail portfolio grew at a robust pace, wholesale book witnessed significant moderation (46% in the last three years) due to run-down of legacy infrastructure financing book and conservative stance on corporate segment. In 1QFY23, the wholesale book further declined 9% YoY to INR364b.

Exhibit 2: Retail loan book posted an impressive 31% CAGR over FY19-22 but is offset by…



Source: MOFSL, Company

Exhibit 3: …run-down of infra financing (legacy) loan book, leading to a reduction in wholesale book

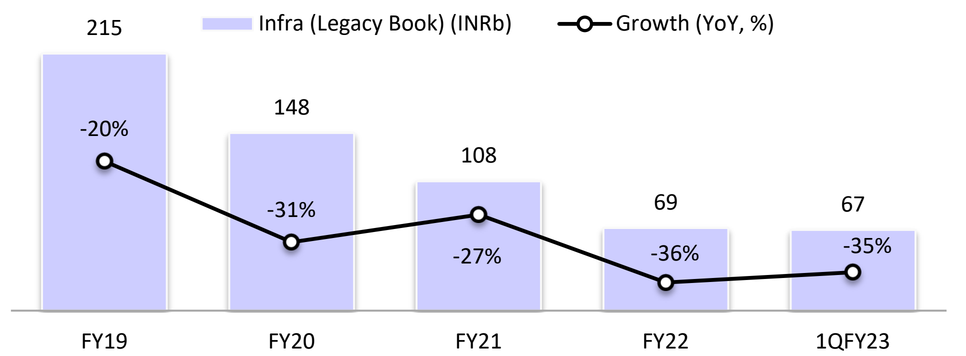


Source: MOFSL, Company

Share of infra (legacy) book down to a mere 5% of business mix

- Over the past three years, since the merger, the bank has reduced legacy infrastructure financing book by 68% to INR69b. In 1QFY23, this book moderated 2% QoQ to INR67b. As a result, the share of this segment in overall loan book has also fallen to 5% in 1QFY23 from 19% in FY19.
- This step was driven by prudent risk management, considering the emerging risk in this space coupled with the desire to diversify to a more granular-focused retail lending portfolio.

Exhibit 4: Consistent reduction in legacy, large-ticket and long-tenure infrastructure financing assets; now stands at 5% of mix v/s 22% at the time of merger



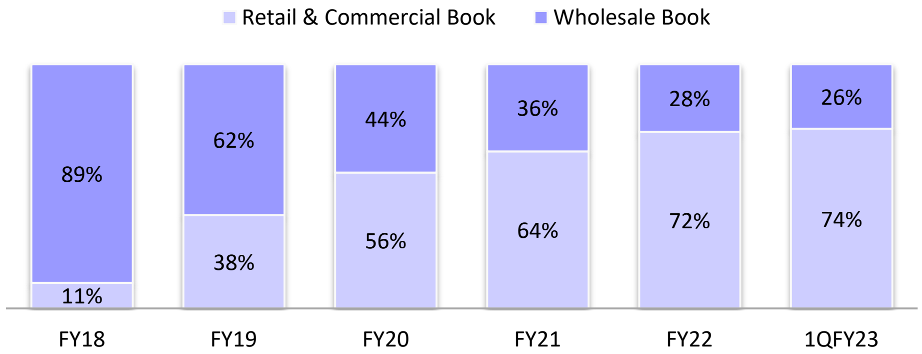
Source: MOFSL, Company

Impressive scale-up of retail portfolio at 31% CAGR over FY19-22

- Due to the combination of growing retail loans and reducing wholesale exposures, the share of retail portfolio in overall portfolio increased to 72% in FY22 from 38% in FY19.
- Within the retail and commercial portfolio, retail has reported a strong 33% CAGR over FY19-22, while commercial witnessed 22% growth during the same period.

Exhibit 5: Retail and commercial book has scaled up to 74% of total funded assets in 1QFY23 v/s 35% at the time of merger in Dec'18

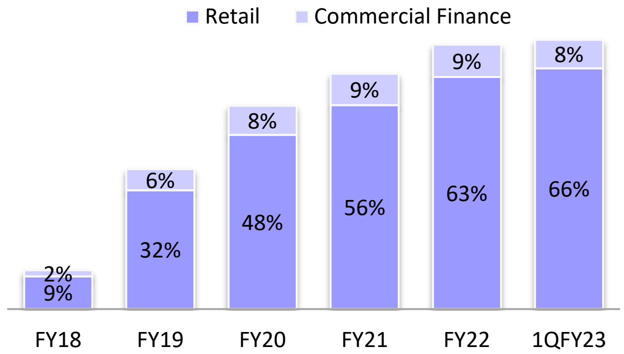
Well-diversified and balanced retail loan book now commands 74% share of overall loans



Source: MOFSL, Company

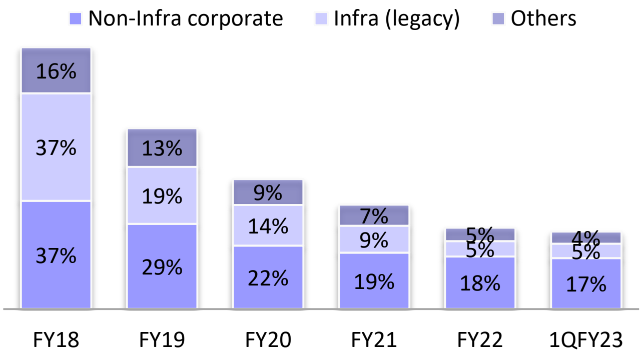
- The retail book is well diversified with a fairly balanced mix across different products such as home loans, LAP, consumer loans, wheels, rural and digital/gold loans. Commercial finance includes business loans, CV loans and trade advances.
- The growth in retail as well as commercial finance is significantly higher than the muted 6% CAGR during FY19-22 for the bank.
- The share of wholesale assets has come-off across all sub-segments. The most profound impact has been in infra (legacy) portfolio, which now forms 5% of mix.

Exhibit 6: Home loans, LAP and consumer loans formed 59% of retail portfolio (ex. commercial finance)



Source: MOFSL, Company

Exhibit 7: Share of wholesale segment has come-off due to focus on building a granular, retail portfolio



Source: MOFSL, Company

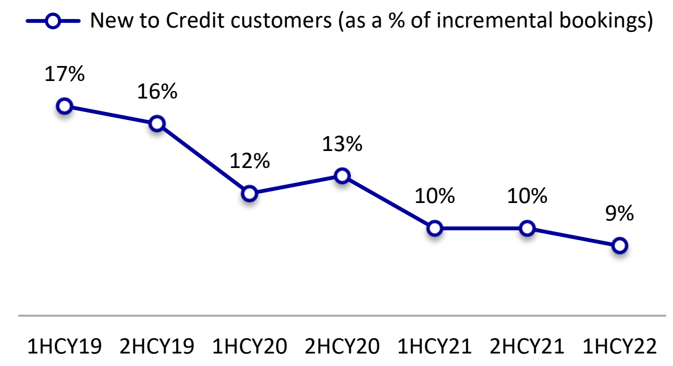
Building a high quality retail and commercial loan book

Strong growth in retail portfolio backed by deep underwriting capabilities

- Leveraging on strong underwriting capabilities of the Erstwhile Capital First team, IDFCFB has built a quality retail and commercial finance portfolio over the past few years.
- As cost of funds has come down, the bank has increased its focus on lending to safer customer segments (with a higher credit score) while maintaining similar margins.
- Out of the total loan bookings, the share of 'new to credit' customers has come down to 9% in 1HCY22 from 17% in FY19 because of stricter underwriting process. Of the credit-tested customers, the share of customers with a credit score in excess of 700 has improved to 84% in 1HCY22 from 61% in FY19.

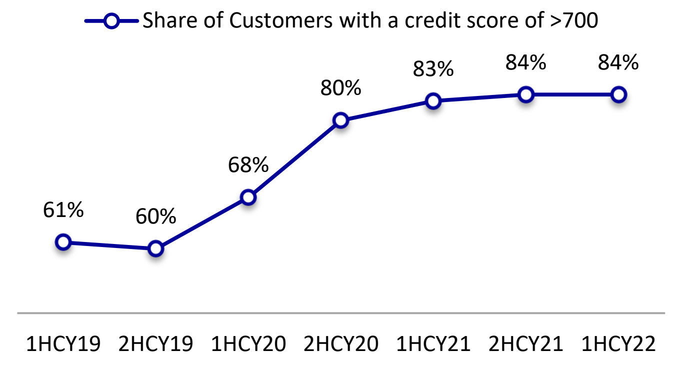
- This indicates improved borrower profile and will lead to better asset quality outcomes in future.

Exhibit 8: Lower CoF enabled migration to safer customer segments; 9% NTC in 1HCY22 v/s 17% three years ago



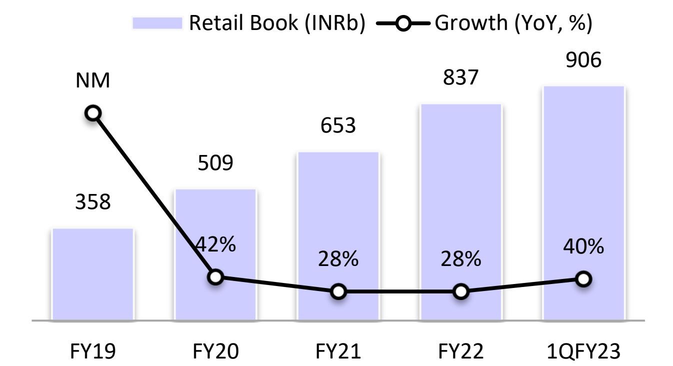
Source: MOFSL, Company

Exhibit 9: Quality of sourcing has improved with 84% customers having a credit score of >700



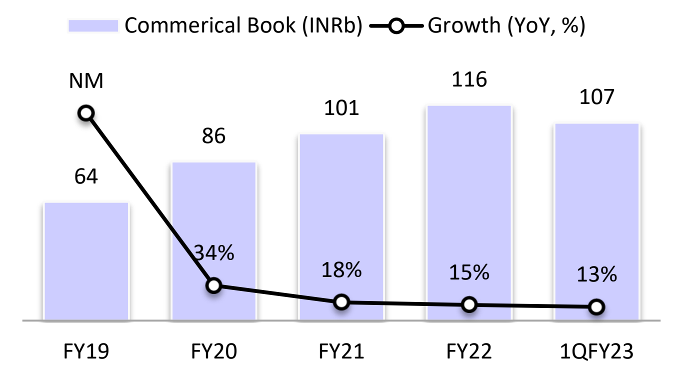
Source: MOFSL, Company

Exhibit 10: Superior growth at 33% CAGR over FY19-22 in retail portfolio backed by deep underwriting capabilities



Source: MOFSL, Company

Exhibit 11: Growth at 22% CAGR during the same period was lower than retail but notably higher than the overall bank



Source: MOFSL, Company

Extensive product offering catering to diverse needs of retail customers

- Within retail, IDFCFB has a fairly well-diversified mix across different segments such as home loans, LAP, consumer loans, wheels, rural and digital/gold loans. The retail loan book formed 74% of total funded assets in 1QFY23.

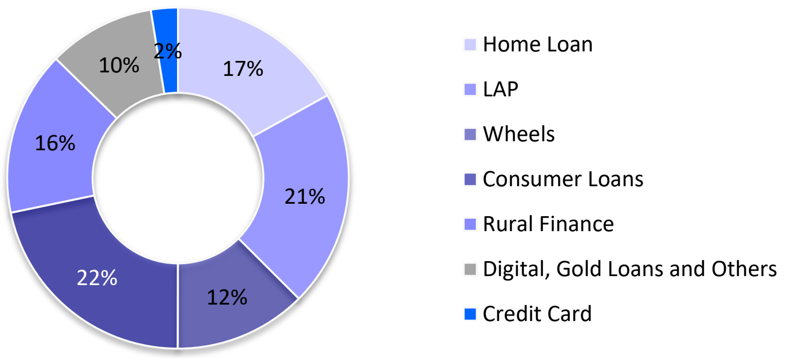
Wide array of products to appeal to one and all

- The growth in FY22 retail loan book was driven by a strong 52% YoY growth in home loans to INR141.1b. The focus of the bank has been to grow its affordable home loans in rural and prime home loans in urban areas. IDFCFB is carrying out significant digital investments in this segment to make the customer journey and interaction simpler and more convenient.
  - Contribution of the salaried segment in home loans portfolio increased to 60% in FY22 from 38% in FY21. This again reflects the migration to safer customer segments in lending.
- In consumer durable financing, the bank has built strong capabilities as it has a long standing experience through erstwhile Capital First. IDFCFB continues to deliver robust performance in this segment and intends to build it further considering its immense opportunity.

Fairly well-balanced mix of individual sub-segments within retail

- Within wheels, the bank has a higher focus on two-wheeler and pre-owned car loans. The aspiration is to build this segment gradually with a tightened underwriting process. Recently, IDFCFB has also partnered with leading digital marketplaces for pre-owned car loans along with financing of new cars from branches. It is also trying to get into pre-owned two wheelers. Broadly, the vehicle segment is a big opportunity and the bank is leaving no stone unturned to capture and benefit from the same.
- In rural banking, IDFCFB endeavors in developing deep relationships across small towns and villages. The team conducts frequent workshops on personal finance, credit scores, weekend camps etc. Over 70% of middle and senior leadership teams from this segment comprise home grown talent for better connect. This portfolio usually includes agri loans, JLG loans – microfinance and some other secured loans.

Exhibit 12: Well-diversified retail book with a balanced mix of home loans, LAP, wheels, consumer loans as of 1QFY23; Credit card is a recent addition and hence share is low at 2%



Source: MOFSL, Company

- The bank also launched new products such as gold loans, especially for the rural customers as the rural economy is recovering strongly.
- Credit card is a recent introduction and hence its share remains low. The bank has issued slightly more than 1m cards since Jan'21. IDFCFB is gradually growing the business as all originations are in-house, assisted by technological capabilities. Though the bank is a marginal player in this segment, prospects look bullish led by marked under-penetration and rising adoption of cashless payments.

In addition to retail, IDFCFB provides several products for small businesses

- Commercial finance includes business loans, CV loans and trade advances. IDFCFB has built an attractive proposition to provide secured working capital loans to small entrepreneurs. It is also extensively using technological capabilities to grow this book in future.
- CV loans segment was a new one for the bank and hence disbursements were strong. About 70% of lending in this segment qualifies as priority sector lending and thus is an added advantage.

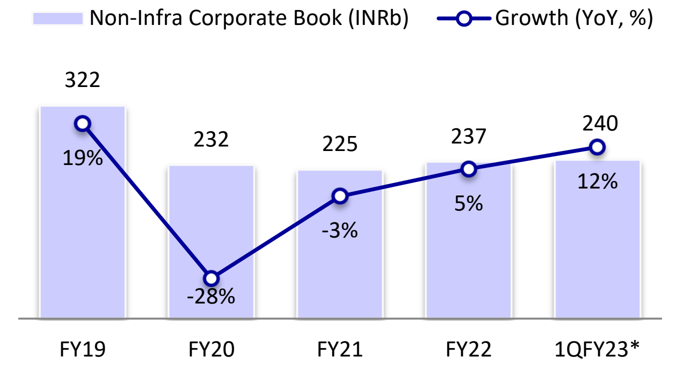
Cautiously growing the non-infra corporate book

- Corporate Banking is an important area for Indian banks with a current market size of INR65t. Thus, all banks look to tap this segment for higher growth opportunity. However, other than direct lending, there are several other fee-related activities which a bank can do with strong relationships with Corporates.

Selectively growing corporate book after extensive due diligence

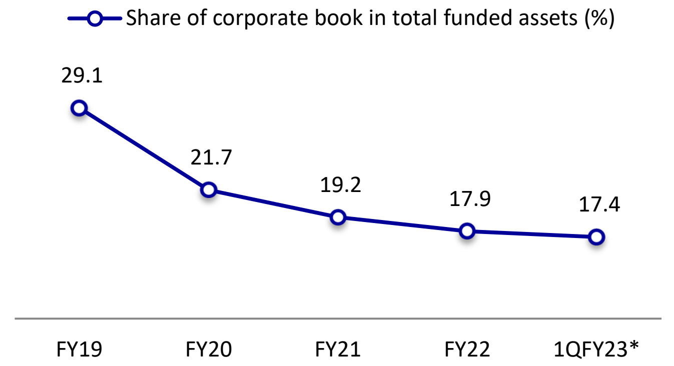
- While IDFCFB has consistently lowered its exposure to the infrastructure financing portfolio, it is seeking to build the non-infra corporate book moderately and opportunistically with a strong credit evaluation process.
- The offerings under Corporate Banking cover the entire gamut of services ranging from term loans and working capital loans to treasury solutions. In addition, IDFCFB also provides several powerful digital solutions to render a superior customer service.
- Over the past three years, the bank has disbursed INR110b worth of loans (out of total sanctions of INR180b). A pristine asset quality performance (GNPA/ NNPA of 2.75%/0.31% in FY22) of this portfolio reflects strong underwriting capabilities of IDFCFB along with careful selection of industries and customers with an aim to reduce concentration risk.

Exhibit 13: Careful build-up of non-infra corporate loan book…



Source: Company, MOFSL

Exhibit 14: …with share declining to 17% of loans in FY22

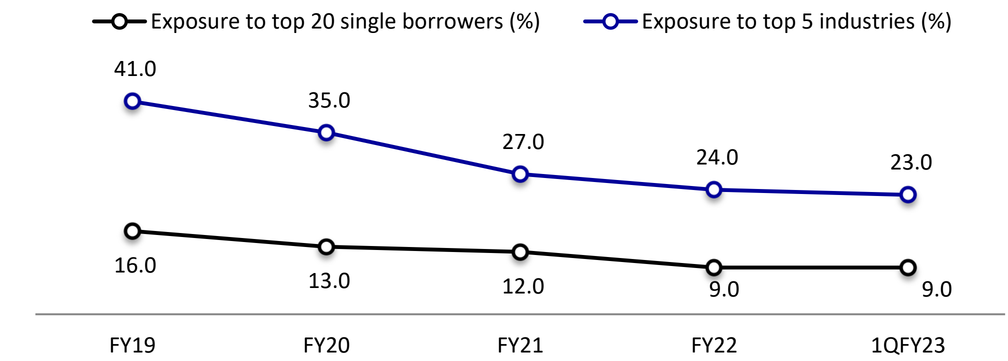


Source: Company, MOFSL

Significantly reduced concentration risk is heartening

- As part of the bank's retailization agenda, it has lowered concentration risk by successfully reducing: a) the wholesale exposure levels across all key parameters and b) the share of top 20 borrowers/top 5 industries in overall loan book.

Exhibit 15: Successfully reduced concentration risk by lowering exposure towards top 20 single borrowers and top 5 industries



Source: MOFSL, Company

Rapid scale-up of retail deposits

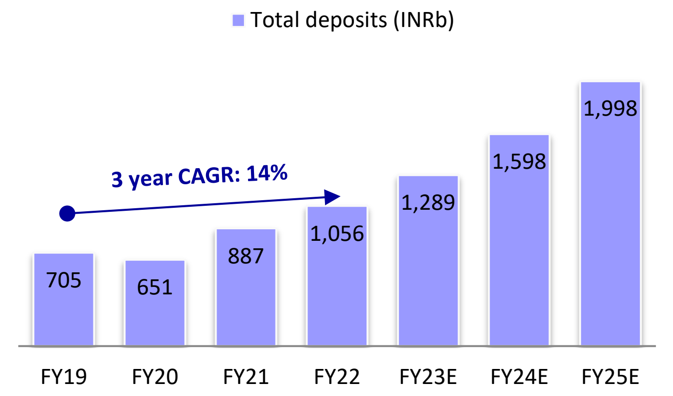
Funding mix getting steadier with focus on CASA + retail term deposits

- Over the last three years, the bank has focused on building a strong retail deposit platform. While the loan book at INR1.0t was fairly large, at the time of merger (Dec'19), the share of retail deposits was quite low at INR0.1t. This dichotomy required corrections and thus the bank focused on building a solid franchise to attract retail liabilities.

Retail deposits up 5x in past 3 years

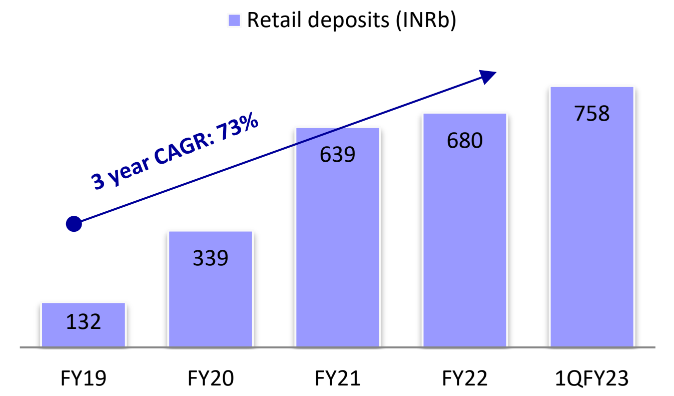
- As a result, IDFCFB grew its retail deposits at a rapid pace (73% CAGR over the past three years) and intentionally slowed down overall loan growth (6% CAGR between FY19 and FY22) to correct the deposit/asset mix.
- In these three years, the bank has demonstrated its ability to raise deposits. **It is even more encouraging to note that IDFCFB sustained traction on deposits and increased CASA deposits despite reducing interest rates in the previous financial year.** Thus, we feel the bank is now well positioned on the deposits front and can successfully fund incremental loan growth from deposits.
- IDFCFB has also achieved all deposit-related guidance such as CASA ratio of 30% by FY24E, CASA + Term deposits <INR50m (% of customer deposits) at 85% and CD < 10% given at the time of merger, a couple of years before the timelines.
- We estimate CASA deposits to post 24% CAGR over FY22-25E, led by sustained momentum in SA deposits. However, as interest rates are rising and the whole sector is looking to raise deposits to fund the improving loan growth, IDFCFB would have to focus on sustaining this momentum.

Exhibit 16: Total deposits posted 14% CAGR over FY19-22 led purely by retail; expect 24% CAGR during FY22-25E



Source: MOFSL, Company

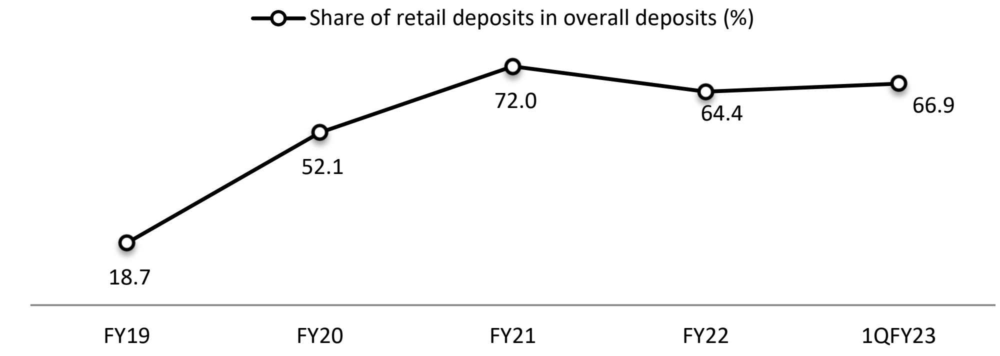
Exhibit 17: Impressive scale-up of retail deposits at 73% CAGR over FY19-22



Source: MOFSL, Company

Share of retail deposits moderated but still stood at a solid 67%

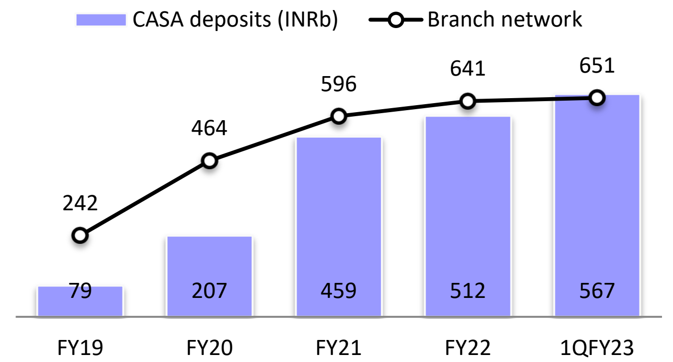
Exhibit 18: Thus, the share of retail deposits (retail CASA + retail TD) in overall deposits increased to 67% in 1QFY23 from 19% in FY19



Source: MOFSL, Company

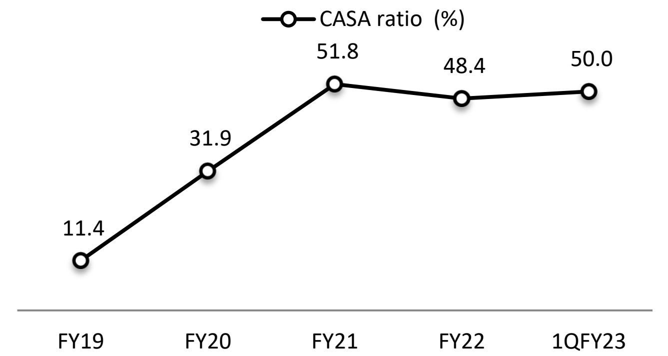
- The bank has raised CASA deposits at a robust pace at 86% CAGR during FY19-22. This has enabled a sharp expansion in CASA ratio to 50.0% in 1QFY23 from 31.9% in FY19. IDFCFB has successfully demonstrated its ability to grow deposits and fund incremental asset growth through the same.
- Since merger, the bank has consistently increased its footprint by opening 445 branches and 695 new ATMs. This has expanded the branch/ATM count to 651/807 as of 1QFY23, respectively, and played a critical role in deposit mobilization. Simultaneously, it has also invested in digital platforms and capabilities to originate and service liability customers.
- We are enthused that despite reducing interest rates in the past year, the bank has successfully raised CASA deposits and ratio. A strong brand, quality service levels, transparency and customer friendly products have allowed the bank to maintain its growth momentum.

Exhibit 19: Robust growth in CASA deposits at 86% CAGR during FY19-22



Source: MOFSL, Company

Exhibit 20: Despite reduction in SA interest, CASA ratio remained robust at 50%



Source: MOFSL, Company

- At end-FY21, the bank was sitting on a very high LCR of 153%. It was also attracting high inflow of deposits due to attractive interest rates. This led to an adverse impact on P&L due to negative carry.
- Thus, the bank reduced interest rate offered on deposits to slow down the inflow of deposits and moderated LCR to reduce the adverse impact of excess liquidity on the balance sheet. This strategy helped it to reduce the Average LCR to 136% in 4QFY22 from 166% in 1QFY22.

- In the table below, we compare the interest rates offered on savings account deposits by IDFCFB and its peers of a similar size. Barring a couple of pockets, IDFCFB offers the lowest interest rate across peers.
- Thus, the bank is relying on factors such as brand, reach and service level rather than pricing to maintain the pace of deposit growth going forward.

Despite lower interest rates v/s peers, momentum in deposits remains strong

Exhibit 21: Savings account interest rate of IDFCFB across slabs are lower than peers

Saving Account Balance	IDFCFB	BANDHAN	AUBANK*	UJJIVAN	EQUITAS
upto 0.1m	4.00	3.00	3.50	3.50	3.50
0.1m to 0.5m	4.00	6.00	5.00	6.00	5.50
0.5m to 1.0m	4.00	6.00	5.00	7.00	7.00
1m to 20m	6.25	6.25	6.0/6.5/7.0	7.00	7.00
20m to 50m	6.25	6.25	6.25	7.00	7.00
50m to 100m	6.25	6.25	6.00	6.75	5.50
100m to 250m	6.25	6.50	Custom**	6.75	5.00
250m to 500m	6.25	6.50	Custom**	6.75	5.00
500m to 1.0b	5.00	Custom**	Custom**	6.75	5.00
1.0b to 2.0b	4.50	Custom**	Custom**	6.75	5.00
>2.0b	3.50	Custom**	Custom**	6.75	5.00

Source: MOFSL, Company

*For AUBANK, 7.0% for balances between INR2.5m-10m and 6.5% between INR10m-20m

**To be decided on a case to case basis

Retirement of high-cost borrowings to aid NII growth

Estimate mix of deposit in total funds to increase to 72% by FY25E

Replacement of high-cost borrowings to add INR7.5-8.0b to NII on an annual basis

- The bank continues to run-down high-cost legacy borrowings (~8.8%) as it replaces them with low-cost deposits (~5.5% cost). As these liabilities get paid off, IDFCFB is likely to save INR7.5-8.0b p.a. in interest expense. This in turn will boost NII and profitability.
- This will reduce the cost of funds and thus enable the bank to further migrate to safer customer profiles and segments, a step it has already embarked upon. Further, this will improve the risk profile and lead to controlled credit costs.

Exhibit 22: About 77% of high-cost legacy bonds will be refinanced with low-cost deposits by FY25E

INR b	O/S Balance	RoI (%)	Maturity in				
			FY23	FY24	FY25	FY26	Beyond FY26
Infra bonds	79.6	8.9	4.8	10.9	55.0	8.9	-
Long term legacy bonds	66.2	9.0	-	16.6	13.1	36.6	-
Other bonds	29.6	8.8	13.5	7.7	1.5	3.3	3.6
Refinance	48.7	8.1	20.6	18.8	9.3	-	-
Total	**224.1**	**8.8**	**38.9**	**54.0**	**78.8**	**48.8**	**3.6**

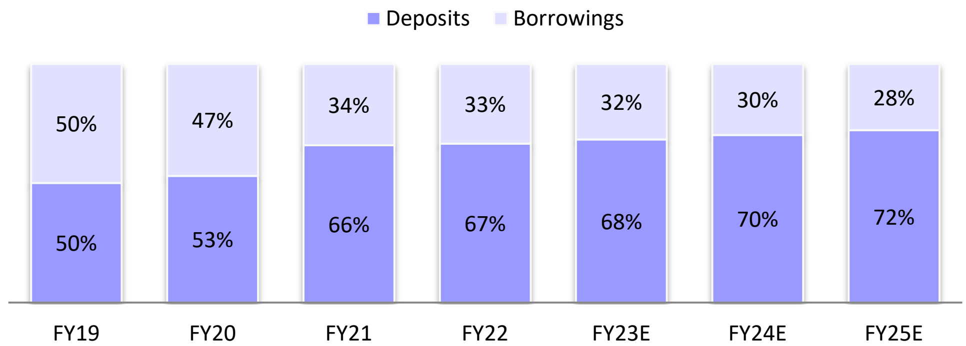
Source: MOFSL, Company

Funding mix becoming steadier with a higher share of retail deposits

Greater proportion of retail deposits in funding mix makes it more stable and favorable

- IDFCFB was in a peculiar position at the time of merger (with erstwhile Capital First) as it had a large loan book comprising infrastructure financing business of erstwhile IDFC Ltd with limited deposits. Thus, reliance was high on borrowings and wholesale deposits, together at 71% of total liabilities.
- Over the past three years, however, the bank has diversified the mix in favor of lower-cost customer deposits led by continuous efforts to build a solid retail franchise. Thus, the share of customer deposits increased to 61% in 1QFY23 from 29% in FY19. This has made the funding structure more stable and granular.
- In recent past, the bank has raised borrowings through refinance at competitive rates for medium-term (4-5 years) with an objective to reduce the cost of funds. These funds have been mobilized at rates lower than even the cost of deposits.
- IDFCFB's funding structure currently is far more optimal with a relatively higher share of customer deposits. It introduces flexibility to take advantage of competitive rates on borrowings, as and when possible.

Exhibit 23: Deposits will continue to have a higher share in funding mix; expect it to form 72% of funding mix by FY25



Source: MOFSL, Company

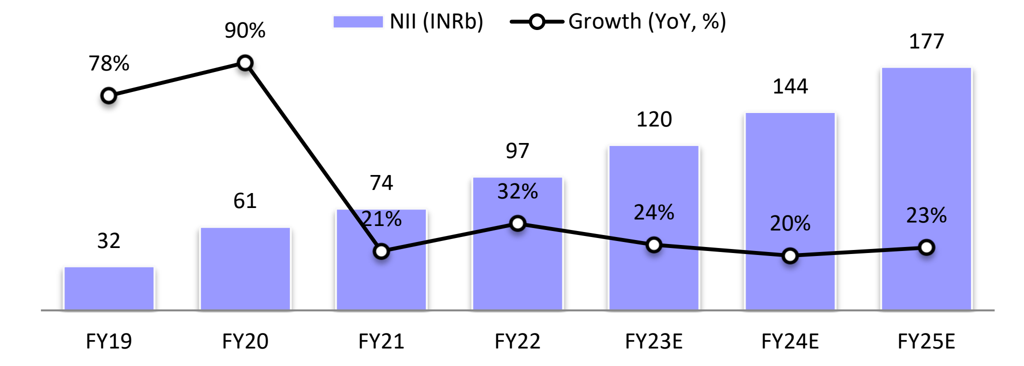
NIM trajectory remains robust

Estimate NII to clock 22% CAGR over FY22-25E

- At the time of merger, IDFCFB had guided for a target NIM of 5.0-5.5% by FY24/25E. It has surpassed the target ahead of time with NIM (reported) of 5.96% in FY22.
- NIM has expanded every quarter since the merger due to a shift of business mix in favor of retail in assets as well as liabilities. This has resulted in higher yields and lower cost of funds.
- We expect growth in NII to be driven by strong 21% loan CAGR over FY22-25 along with ~42bp expansion in margin to 6.5%.

Growth in NII to be largely led by loan growth henceforth

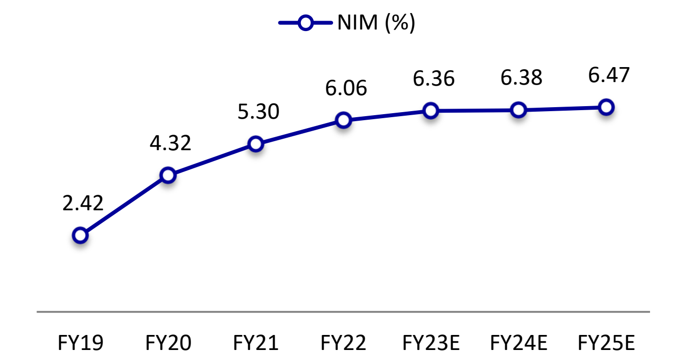
Exhibit 24: NII witnessed robust 45% CAGR over FY19-22; expect 22% CAGR over FY22-25E



Source: MOFSL, Company

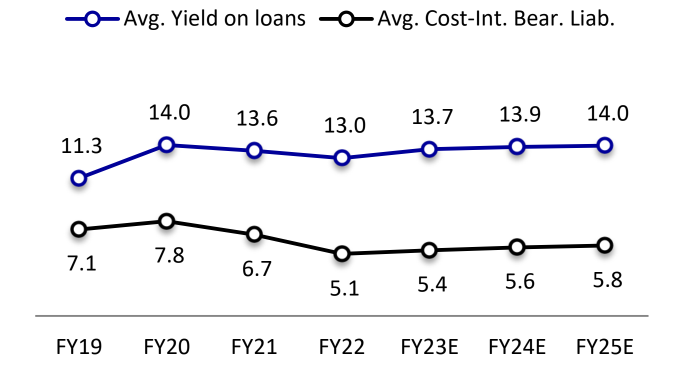
- NIM expansion is driven by higher yields, partially offset by a lower increase in cost of funds. Rising share of deposits, refinance at competitive rates and gradual reduction in high-cost legacy bonds will keep cost of funds in check.

Exhibit 25: Consistent rise in NIM, driven by increasing share of retail in business; marginal expansion henceforth as…



Source: MOFSL, Company

Exhibit 26: … improvement in yield is partially offset by increase in cost of funds



Source: MOFSL, Company

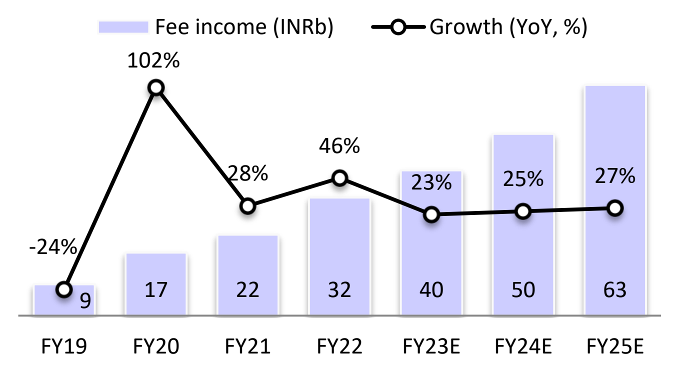
Non-interest income witnessing robust growth

- Fee income has recorded 56% CAGR over FY19-22, driven largely by growth in core fee income. Fee income growth was fueled primarily by the fees related to loan sourcing, higher transaction fees and distribution and wealth management fees. The bank has successfully built a granular fee income base, which is also a reflection of the growing share of retail in all its business aspects.

More than 90% of fee income is generated from retail banking operations; thus it is granular and sustainable in nature

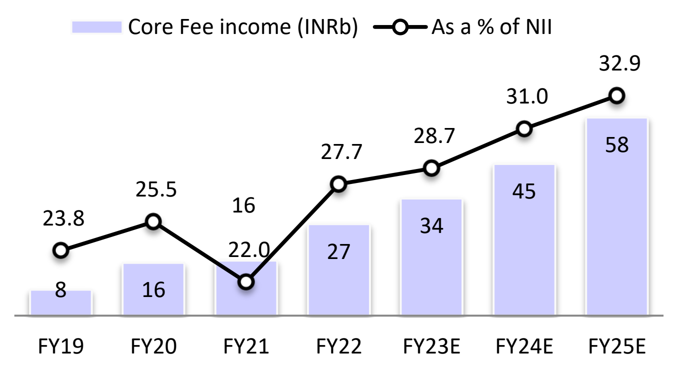
- Wealth management AUM has expanded significantly in recent years to reach INR65.4b in FY22. With large under-penetration, this holds potential to generate significant distribution income for IDFCFB in future. The bank is also a major player in the FASTag and Toll business.
- We expect the fee income momentum to continue despite pressure on treasury performance due to rising bond yields. We forecast fee income to report 25% CAGR during FY22-25E.

Exhibit 27: Fee income clocked 56% CAGR over FY19-22; expect healthy momentum to continue



Source: MOFSL, Company

Exhibit 28: Robust growth in core fee income; rising contribution in total income of the bank



Source: MOFSL, Company

Cost ratios peaking out; operating leverage to improve

Expect C/I ratio to moderate to 66% by FY25E v/s 75% in FY22

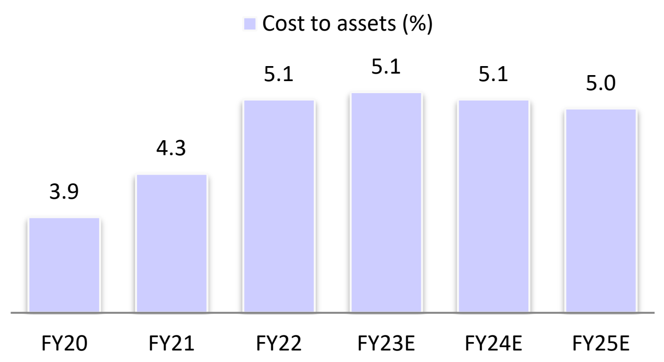
Need to build a retail franchise for deposit mobilization led to an elevated C/I ratio

- At the time of the merger, IDFCFB had a large wholesale asset book, while retail liabilities were a fraction of it. The need to build a large retail franchise (to correct this gap) required upfront investments, and hence cost metrics were sub-optimal.
- These upfront investments included setting up of branches, ATMs, expansion of the workforce, and building banking capabilities to handle a large number of transactions. All of this led to an increase in operating expenditure. As a result, IDFCFB's cost ratios were not comparable to its peers that have been in existing for a much longer period of time.
- Another reason for the elevated C/I ratio is the continuous launch of new product lines – the latest being Credit Cards. As the bank aims to build a solid retail franchise, it is imperative to have a wide product portfolio catering to the diverse needs of retail customers.
- Of the 651 branches in Jun'22, most would have an average life of 1.5-2 years. As these scale up over the medium term, cost metrics would naturally trend down.

We expect operating leverage benefits to start flowing in as the bank continues to gain scale

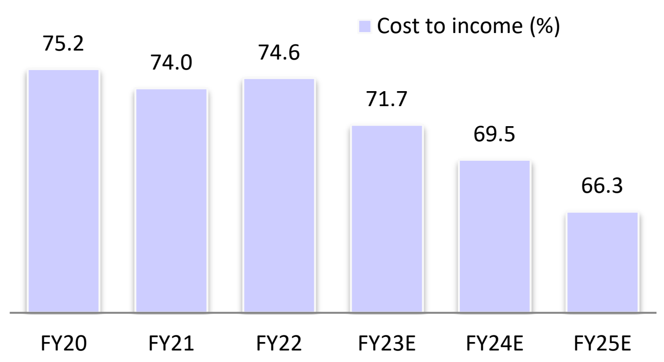
- As some of these challenges settle down over the next few years, we expect the C/I ratio to trend down to more normalized and peer-like levels. Repayment of high cost legacy borrowings would also benefit the same.
- While the bank has already met its guidance on most metrics a couple of years ahead of the timelines, there is significant scope for improvement on the cost front. The management has guided at a C/I ratio of 55% by FY24/FY25 v/s 74.6% at the end of FY22. We expect the C/I ratio to improve to 66% as the bank benefits from economies of scale.

Exhibit 29: Significant investments made in the past would start to yield results



Source: MOFSL, Company

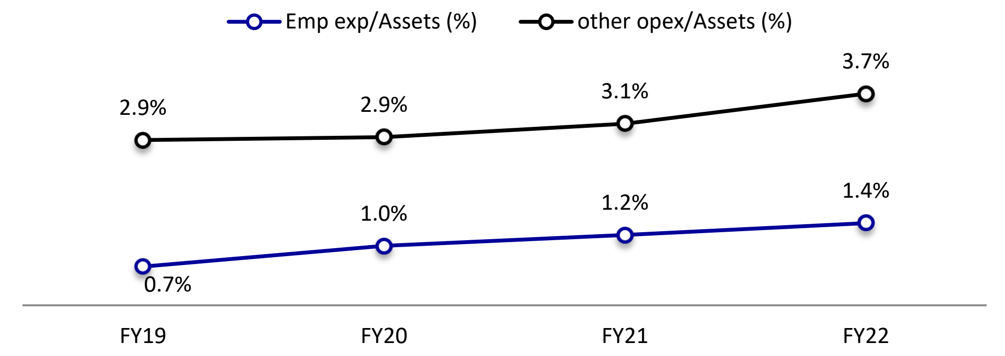
Exhibit 30: Thus, cost-to-assets ratio and C/I ratio should improve gradually



Source: MOFSL, Company

Exhibit 31: Breakup of cost-to-assets ratio: Other OPEX sees a significant rise over FY22

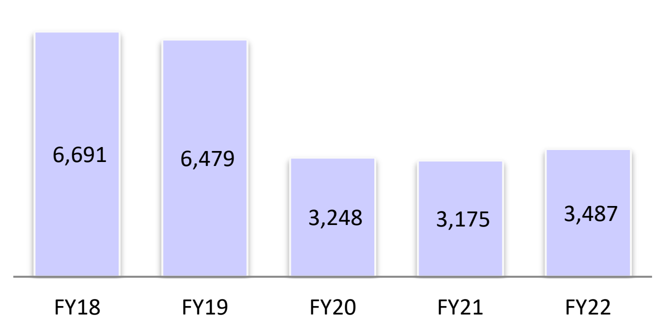
Rise in other opex is due to investments in building the brand, branch expansion and roll out of new products



Source: MOFSL, Company

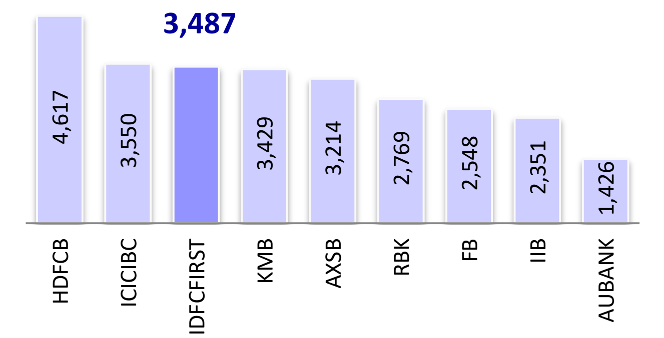
- Over the past few years, business per branch for IDFCFB has been broadly stable in the INR3.2-3.5b range. The same stands higher than mid-size peers and is in line with the larger banks. However, business per employee stands among the lowest at INR80m, providing ample scope for an improvement in efficiency ratios. SA per branch for IDFCFB has improved significantly to INR652m in FY22 v/s INR236m in FY18 and stands closer to the large banks, but much higher than mid-size banks. This underscores the bank's ability to garner retail deposits, which can be built upon further.

Exhibit 32: Business/branch (INR m) witnessed a gradual increase in FY22



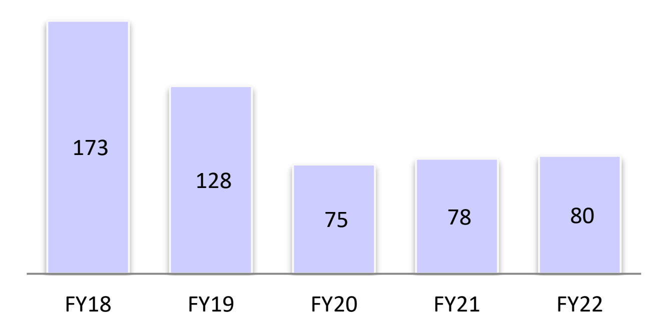
Source: MOFSL, Company

Exhibit 33: Business/branch (INR m) stands among the top tier v/s its peers



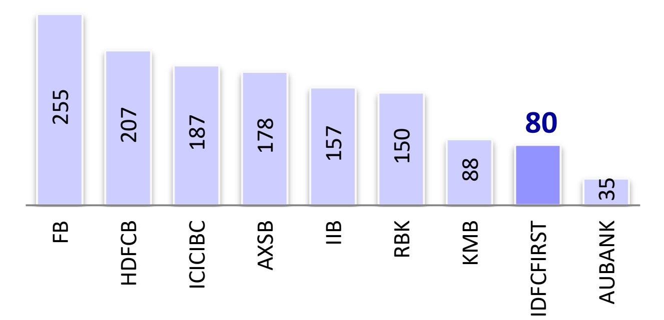
Source: MOFSL, Company

Exhibit 34: Business/employee (INR m) is on an improving trajectory



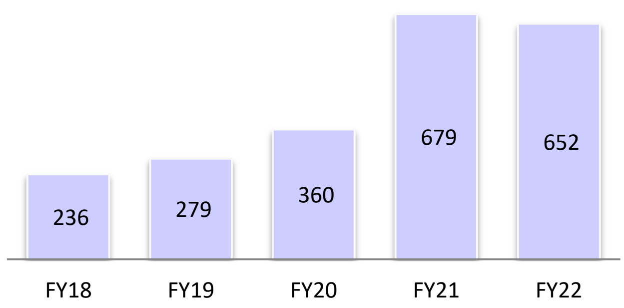
Source: MOFSL, Company

Exhibit 35: Business/employee (INR m) stands among the lowest and thus, ample scope for improvement exists



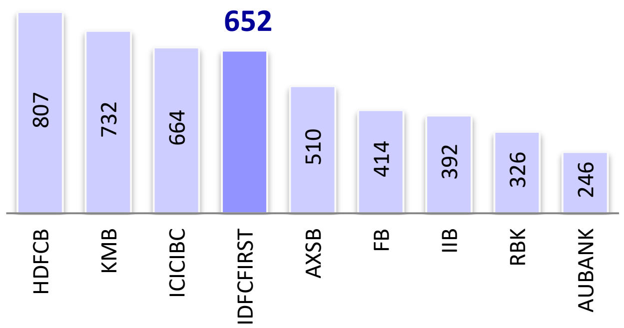
Source: MOFSL, Company

Exhibit 36: SA per branch (INR m) healthy at ~INR652m as of FY22



Source: MOFSL, Company

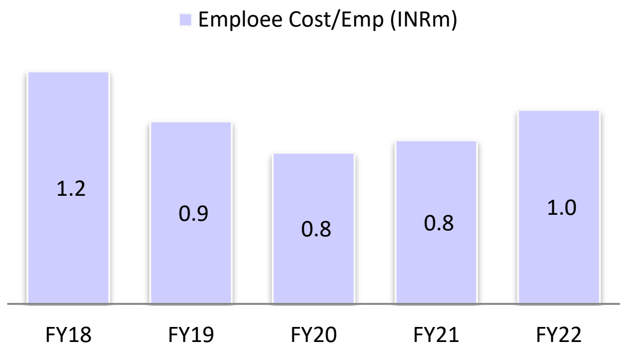
Exhibit 37: SA/branch (INR m) among the top tier in comparison to its peers



Source: MOFSL, Company

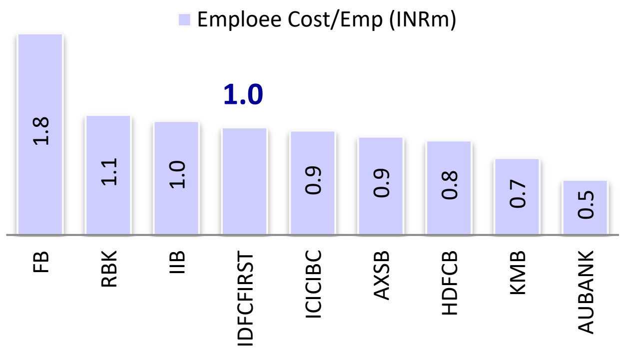
- While employee cost per employee for IDFCFB has been broadly in line with peers, total OPEX per branch remains significantly high as bank has been focusing on building its capacity. As a result, total OPEX per branch stands at INR150m, which is 2-5x that of other peers. As branches mature, operating leverage is likely to kick in, which would further aid operating profitability.

Exhibit 38: Cost/employee ~INR1m in FY22



Source: MOFSL, Company

Exhibit 39: Cost/employee trends across peers



Source: MOFSL, Company

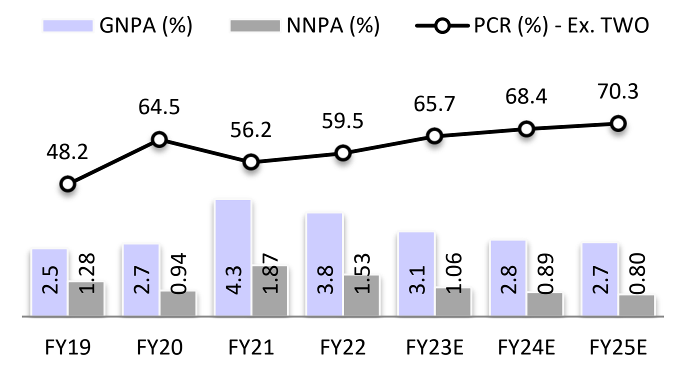
Robust asset quality trends; legacy issues behind

Strong underwriting and safer retail lending to rein in credit costs

Asset quality moving back to long-term mean in retail and commercial finance book

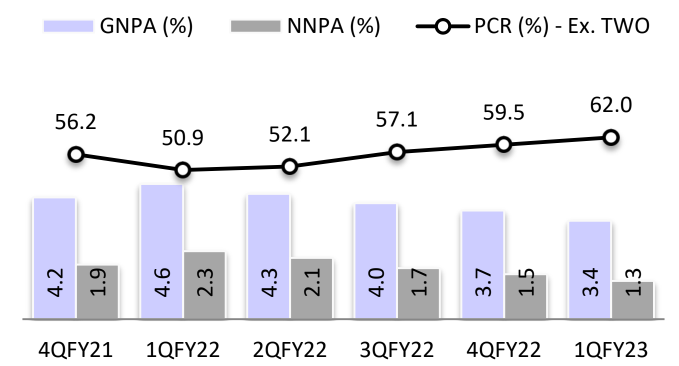
- The worst of the asset quality pain is behind it, with the retail portfolio reasonably stress tested during the pandemic, while all possible wholesale stressed assets have been recognized and well provided for. The bank is entering a period of strong asset quality performance, with an incremental focus on building a granular retail portfolio, where it has a sharp underwriting expertise.
- The bank is gradually heading back towards a long term-trend of GNPA/NNPA level of ~2%/1% in the retail and commercial finance book. This book constitutes 74% as of Jun'22 and is the primary growth driver of the bank's overall loan book.
- Over the past few years, the bank has built a sufficient provision buffer on all stressed wholesale exposures. The Corporate (non-infra) book forms 17% of the overall loan book as of Jun'22 and GNNPA/NNPA stood at 3.67%/0.2% in this segment. Excluding a large retail chain that is fully provided for, GNPA would have been 1.79%. The bank has a robust PCR of 97%.
- The restructured portfolio has further moderated to 1.3% in 1QFY23 as compared to 1.8% in FY22.
- The legacy Infrastructure book constitutes only 5% of the overall loan book and continues to run down. GNPA/NNPA, at 21.7%/11.8%, is elevated due to a decline in the loan book. The management is confident that all possible stress accounts have been already recognized.

Exhibit 40: Asset quality should continue to improve as the bank moves to safer customer segments



Source: MOFSL, Company

Exhibit 41: A consistent decline in GNNPA/NNPA and an increase in PCR in recent quarters



Source: MOFSL, Company

Asset quality to improve led by improved underwriting and a focus on safer customer segments

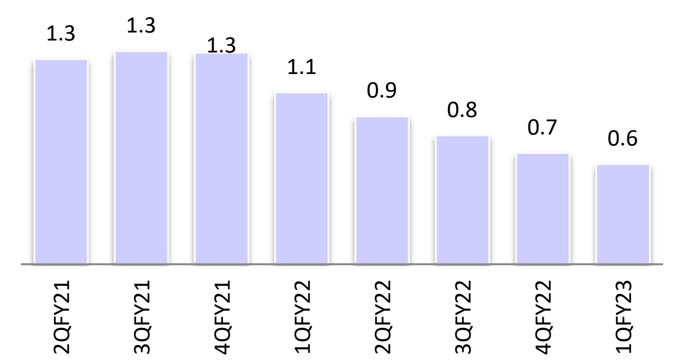
- In Exhibit 8 and 9, we showcase the bank's improving quality of sourcing of retail customers, with a significantly higher proportion of customers with a credit history and credit score in excess of 700 as compared to a few years back.
- The cheque bounce rate is a direct indicator of asset quality and has shown consistent improvement over the past two years. The ratio is better even when compared to the pre-COVID (Dec'19) level by 30%.

- Collection efficiency, another important indicator of asset quality, in early stage bucket for urban retail customers has increased by 50bp to 99.4% v/s the pre-COVID level of 98.9%.

High-level indicators pointing to better asset quality outcomes in future

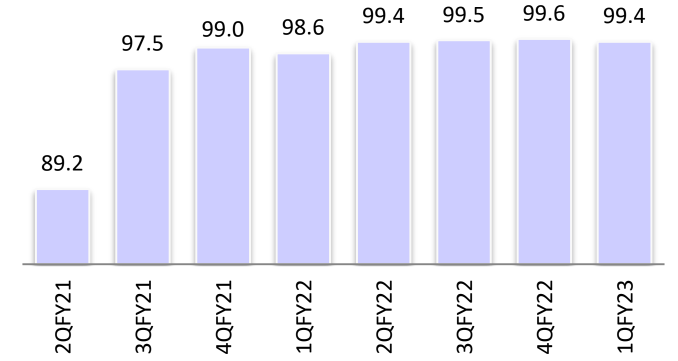
- On the basis of improving trends in factors such as sourcing quality, cheque bounce rate, collection efficiency, and recoveries, we expect NPAs in retail and commercial finance to remain in a narrow range, with a downward bias. This would lead to lower delinquency and thus controlled credit costs.

Exhibit 42: Encouraging outlook on asset quality led by a lower cheque bounce rate as well as…



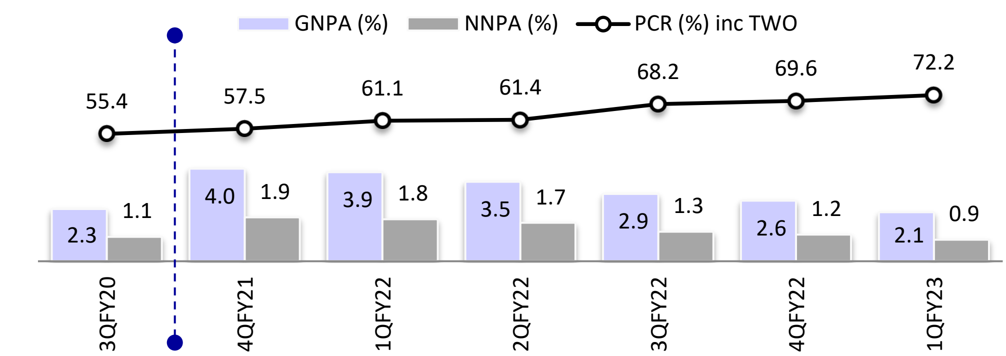
Source: MOFSL, Company

Exhibit 43: …a higher collection efficiency (%) in the early stage bucket for urban retail customers



Source: MOFSL, Company

Exhibit 44: GNPA/NNPA in retail and commercial finance is back to its long-term trend after seeing a spike during the COVID-19 pandemic; PCR improves to 72%



Source: MOFSL, Company

Large-ticket, legacy, and stressed wholesale exposures are well-recognized and provided for

- Since the merger of Capital First with IDFCFB, the management is consistently reducing risk on its Balance Sheet by lowering the concentration risk of its top 20/five borrowers/industries. It has also cut its exposure to the Infrastructure sector to 5% in FY22 from 19% in FY19 (*refer Exhibit 7*).

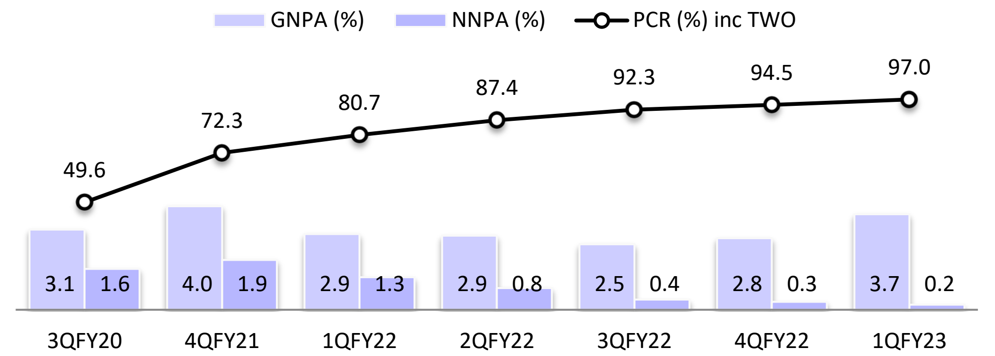
All possible stressed assets in wholesale book are identified and provided for

- The management has tightened its underwriting process, with checks on the industry and company outlook, cash flows, net worth, financial ratios, background references, among others. It looks to build this segment moderately and opportunistically without taking undue risks. While the retail and commercial loan book clocked 31% CAGR over the past three years, the Corporate (non-Infra) segment fell 26% over the same period.

- This reflects a conservative and risk-off approach of the management towards growing this segment and would keep credit costs in check.
- Due to slippage of a large exposure, pertaining to a retail chain, GNPA rose to 3.67%. Excluding this, GNPA would have stood at 1.79%. However, NNPA ratio remains the same as the exposure is fully provided for.

PCR inc. TWO stood at 97% in corporate (non-infra) segment and lends comfort

Exhibit 45: Adequate provision buffers to tackle incremental stress in the Corporate (non-infrastructure) book

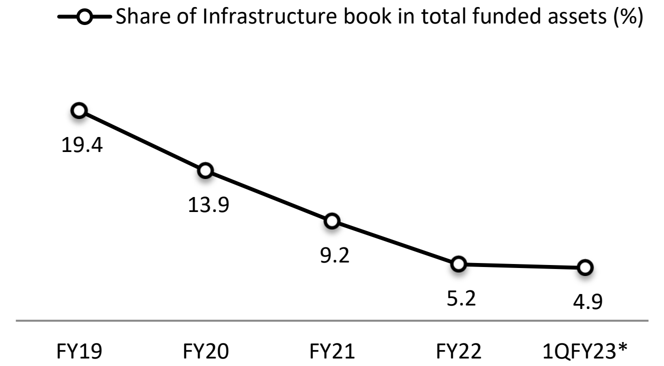


Source: MOFSL, Company

Incremental stress from infra book limited as contribution in mix is a mere 5% now

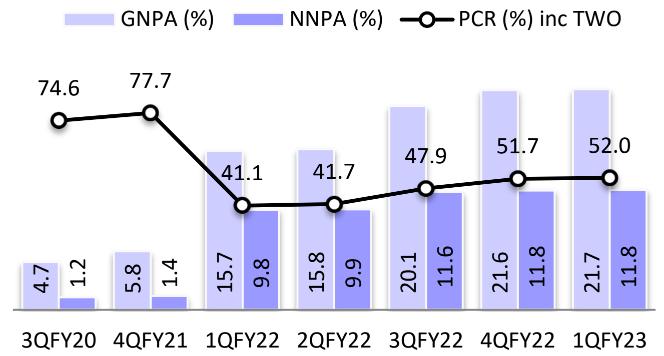
- The bank's legacy Infrastructure book is in a run-down phase and currently constitutes only 5% of the overall loan book as compared to 19% in FY19 and 22% at the time of its merger in Dec'19.
- The GNPA ratio for this segment looks elevated due to a decline in this book. All possible stressed accounts in this segment have been identified and provided for. As this segment now constitutes only 5% of the overall loan book, the incremental stress here would be fairly limited.
- Due to slippage of a large exposure, pertaining to a Mumbai-based toll operator, GNPA/NNPA rose to 21.64%/11.76%. Excluding this, GNPA/NNPA would have been at 9.7%/1.62%. The management is hopeful of a resolution as the toll operator continues to generate revenues.

Exhibit 46: As infrastructure book is in a run-down phase, the scope for incremental stress is limited



Source: MOFSL, Company; *net of IBPC

Exhibit 47: GNPA elevated in recent quarters due to a decline in the book size of the Infrastructure segment



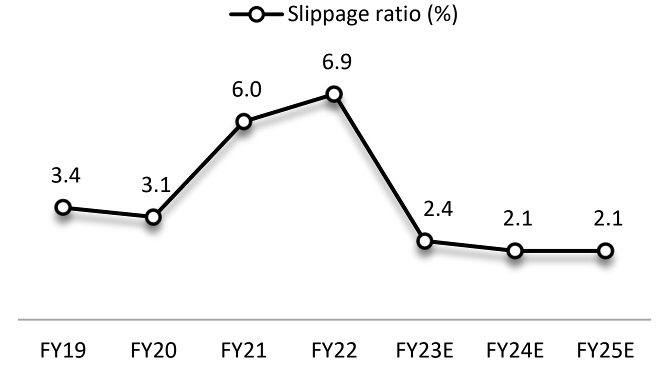
Source: MOFSL, Company

Estimate credit cost to be in the 1.3-1.5% range

Expect slippages and credit cost to stabilize in a narrow range henceforth

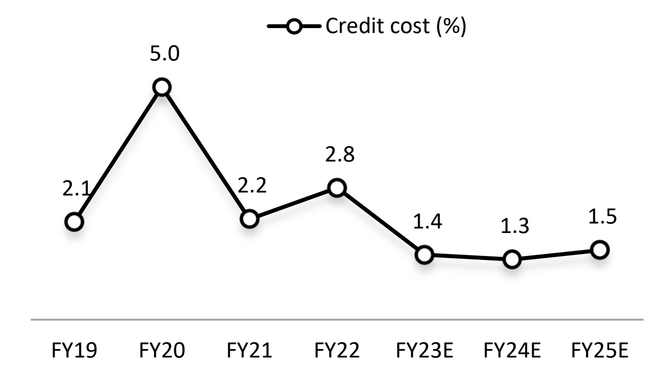
- Over FY19-20, the bank made significant provisions towards its stressed legacy Infrastructure and Corporate accounts. While this led to a hit to its P&L, it laid the foundation for a strong provision buffer.
- With a comfortable PCR (including TWO), at 73.1% in Jun'22, and in the backdrop of an improving asset quality cycle, the bank is well-placed to ride the cycle with controlled credit costs.
- The current buffer allows the bank to navigate any incremental stress in the future without dampening the Balance Sheet or return ratios.
- While credit cost on an average was 3% over FY19-22, we expect it to improve in coming years.

Exhibit 48: Transition to safer customer segments within retail to drive lower slippages



Source: MOFSL, Company

Exhibit 49: Credit cost (%) to improve led by stronger underwriting and adequate provisioning buffers



Source: MOFSL, Company

Return ratios to steadily improve

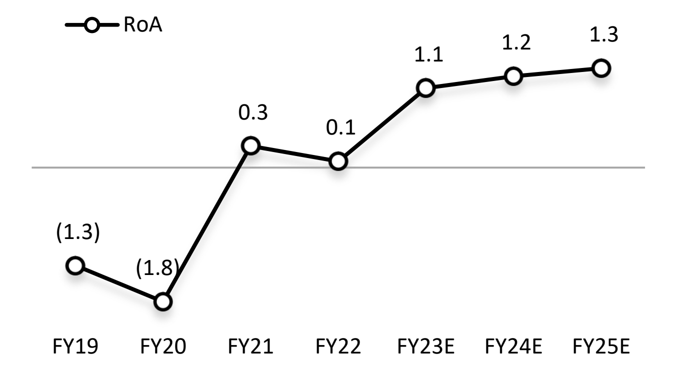
Expect RoE to improve to 12.2%/13.9% in FY24/FY25E

- At the time of its merger, the management had guided at a FY24-25 RoA/RoE of 1.4-1.6%/13-15%. While the bank is currently far away from these guided levels, its return ratio trajectory has improved considerably.
- Based on the reducing drag of legacy high-cost liabilities, investment in building a retail franchise, and setup of the Credit Card segment, profitability of the bank is set to improve.

Return ratios are set to move north from here as drag from wholesale exposure and legacy borrowings reduce

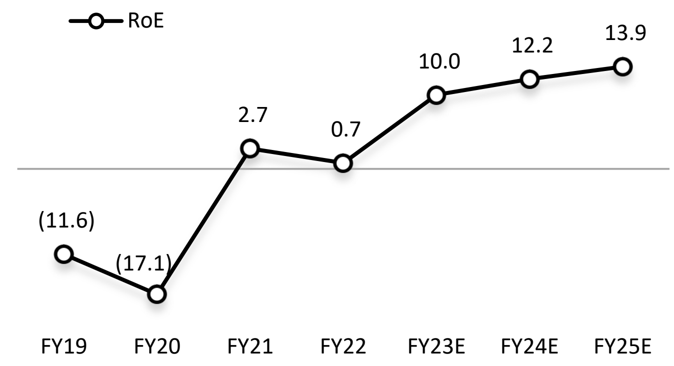
- Credit costs should be controlled as the share of the Infra financing book has fallen to 5%, all possible stressed corporate accounts have been identified and well provided for, and asset quality in the retail book is back to its long-term trend after a spike during the COVID-led lockdown.
- While we are confident about the sustainability of the rising trajectory in profitability and return ratios, we feel the guided levels may take a couple of years more than envisioned.

Exhibit 50: Improving profitability profile would result in a strong RoA for the bank at 1.3%...



Source: MOFSL, Company

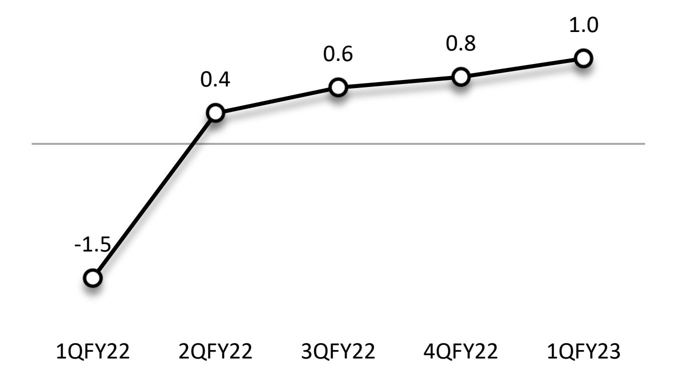
Exhibit 51: ...as well as a healthy RoE at 13.9% by FY25E (%)



Source: MOFSL, Company

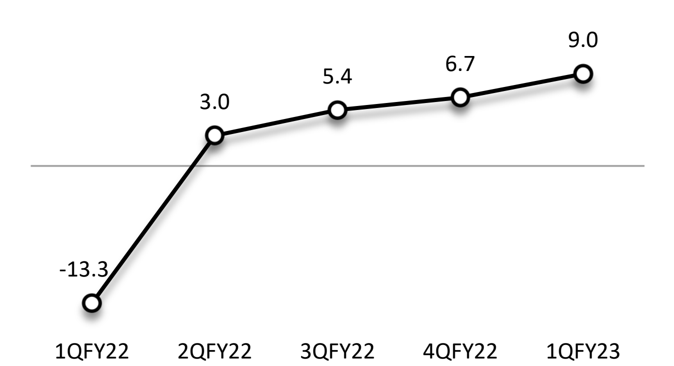
- RoE has been gradually and consistently inching up, suggesting incremental business has a higher unit economics as compared to the whole stock.

Exhibit 52: Superior incremental unit economics as reflected in an improving annualized RoA trajectory (%)...



Source: MOFSL, Company

Exhibit 53: ...as well as RoE; annualized RoE stood at 9% in 1QFY23 (%)



Source: MOFSL, Company

Experienced management team, with a proven track record

Mr. V. Vaidyanathan, Managing Director & CEO

Mr. Vaidyanathan has over two decades of experience in Financial Services in India and was instrumental in building ICICIBC's Retail Banking network from CY00 to CY09. He was MD & CEO of IPRU for a brief period. In CY10, he turned entrepreneur with Capital First, a retail-focused NBFC, specializing in lending to consumers and small businesses. Between CY10 and CY18, he grew the loan book to INR296b, with pristine asset quality, from a nascent state. In CY18, he played a pivotal role in the merger of Capital First with IDFCFB and took over as MD and CEO of the merged entity.

Mr. Sudhanshu Jain, CFO & Head – Corporate Centre

Mr. Jain has been associated with the bank since Mar'20. He is a qualified Chartered Accountant and Company Secretary with 19 years of experience in the finance domain. Prior to joining the bank, he was the Deputy CFO of Paytm E-Commerce and CFO of Paytm Payments Bank for a couple of years. He has also worked for ~14 years at ICICIBC in the areas of audit and financial planning.

Mr. Pradeep Natarajan, Head – Retail Banking

He has been associated with Capital First since Nov'10. Post the merger of Capital First with IDFCFB in Dec'18, he used to head the bank's retail assets. Since Apr'22, he has been the Head of Retail Banking. Prior to joining Capital First, he was associated with Macquarie Private Wealth as Director – Sales & Marketing. He has also spent eight years with Standard Chartered as Business Head of Personal Loans. Mr. Natarajan holds a Master's Degree from Sydenham Institute of Management Studies.

Mr. Sumit Madan, Head – Retail Liabilities & Branch Banking

Mr. Madan has been associated with IDFCFB for over three years. He heads the retail liabilities division, along with Branch Banking. Prior to joining IDFCFB, he was the Chief of Branch Banking for AUBANK. He has worked for over 12 years at Citibank in various capacities and left as Regional Head for its North Indian operations. He has a Master's degree from Lal Bahadur Shastri Institute of Management.

SWOT analysis

Strength

- Its strong underwriting experience in retail, given the robust scale-up in Capital First retail portfolio, with pristine asset quality
- With significant investments in building its digital capabilities, the bank believes that its digital footprint is a key strength
- Over the past few years, the bank has recognized and provided for all possible stressed assets. Thus, the bank is well-placed to absorb any pressure in the future

Weakness

- While the cost of funds has declined over the past few years, the bank still has a fair share of high-cost legacy borrowings
- As it still is a relatively new bank, it has to make significant investments in brand and infrastructure (branches and employees), thus keeping its C/I ratio elevated

Opportunity

- The bank recently launched Credit Cards, which offers an exciting opportunity to build a high RoA product that is significantly underpenetrated in India
- As the bank widens its Retail product portfolio, it can gain further traction in overall growth
- Careful underwriting in Corporate Banking will boost NII and result in healthy fee income

Threat

- Stiff competition from large and mid-size Banks on retail deposits as they increase focus on mobilizing the same
- Aggressive lending of unsecured retail products can impact asset quality in the event of a global domestic economic slowdown

Bull and Bear case

Bull case

- ☑ In our Bull case, we assume strong loan growth (28% CAGR v/s 21% in the Base case) over FY22-25E. The strong economic outlook can result in higher than expected retail growth and improve wholesale lending opportunities for the bank as corporates embark on a capital cycle.
- ☑ We expect 28% deposit CAGR (v/s 24% in our Base case) over FY22-25E, led by strong growth in retail deposits. We expect the CASA ratio to touch 51% (v/s 49% in our Base case).
- ☑ While our Base case on NIM stands at 6.5%, a higher than anticipated growth in the retail segments and stronger growth in low-cost liabilities can lead to a NIM of 6.8%.
- ☑ Asset quality would be slightly better, with GNPA at 2.5% by FY25E (v/s 2.7% in our Base case).
- ☑ We expect a RoA/RoE of 1.7%/17.9% in FY25E (v/s 1.3%/13.9% in our Base case).
- ☑ Based on the above assumptions, we value IDFCB at INR95 (2x Sep-24E BV) – an upside of 75%.

Bear case

- ☑ In our Bear case, we assume a 12% loan CAGR (v/s 21% in our Base case) over FY22-25E due to a calibrated growth in retail and a reduction in wholesale exposure.
- ☑ Due to the strong competitive intensity in deposits, the bank may be able to grow its deposits at 14% CAGR (v/s 24% in our Base case) over FY22-25E.
- ☑ We expect margin to decline to 6.2% in FY24 (v/s 6.5% in our Base case) due to a slowdown in loan growth and CASA deposits.
- ☑ Any economic slowdown in retail can impact asset quality, with GNPA at 3.0% in FY24E (v/s 2.7% in our Base case).
- ☑ We expect a RoA/RoE of 0.9%/8.8% in FY25E (v/s 1.3%/13.9% in our Base case).
- ☑ Based on the above assumptions, we value IDFCB at INR37 (0.9x Sep-24E BV) – a downside of 32%.

Exhibit 54: Scenario analysis – Bull case

Bull Case	FY22	FY23E	FY24E	FY25E
NII	97,062	1,25,239	1,63,152	2,08,929
OPEX	96,444	1,15,090	1,37,056	1,63,637
Provisions	31,086	16,836	21,728	33,173
PBT	1,752	32,943	53,114	72,076
PAT	1,455	24,642	39,729	53,913
NIM (%)	6.1	6.4	6.6	6.8
RoA (%)	0.1	1.2	1.5	1.7
RoE (%)	0.7	11.1	15.6	17.9
EPS	0.2	4.0	6.4	8.7
BV	33.8	37.7	44.1	52.8
Target multiple (P/BV)				**2.0**
TP (INR)				**95**
Upside (%)				**75**

Source: Company, MOFSL

Exhibit 55: Scenario analysis – Bear Case

Bear case	FY22	FY23E	FY24E	FY25E
NII	97,062	1,15,238	1,29,249	1,50,438
OPEX	96,444	1,14,282	1,33,898	1,59,863
Provisions	31,086	15,021	16,524	22,194
PBT	1,752	25,566	28,365	30,799
PAT	1,455	19,123	21,217	23,038
NIM (%)	6.1	6.2	6.1	6.2
RoA (%)	0.1	0.9	0.9	0.9
RoE (%)	0.7	8.7	8.9	8.8
EPS	0.2	3.1	3.4	3.7
BV	33.8	36.8	40.2	43.9
Target multiple (P/BV)				**0.9**
TP (INR)				**37**
Downside (%)				**-32**

Source: Company, MOFSL

Integrated approach to maintaining high ESG standards

- While the bank has successfully transformed most of its key operating and financial parameters over the past three years, it is continuously reimagining its approach to ESG. This is to create more value for customers, communities, and all other stakeholders.
- ESG has always been a key element of the bank's culture. It has also embedded good ESG practices in its vision statement.
- The bank is mindful of the broader impact its activities can have and thus inculcates ESG considerations in its decision-making across the organization. This would eventually lead to economic value for all shareholders and other stakeholders, and create a positive impact on the economy.

Environment

- The bank is conscious of its responsibility towards the environment and thus created energy efficient solutions in a new corporate office. It has received an Indian Green Building Council (ICBC) certificate for the same property.
- To reduce the consumption of paper, the bank has adopted digitization and automation. It has lowered dependence on paper by regularly sharing e-statements and e-receipts with its customers.
- It has empaneled certified vendors for managing e-waste and also adopted separate waste segregation methods for dry and wet waste.

Social

- The bank is driven towards the theme of financial inclusion by serving more than 6m customers across 70k villages and towns. Women constitute ~75% of the rural population served by the bank.
- Over FY21-22, it undertook several initiatives (like Insurance, medical assistance, salary credit to the nominee, relocation assistance, and advance salary) to improve the well-being of its employees impacted by the COVID-19 pandemic.
- It is dedicated to improving the experience of its customers and introduced a platform to motivate employees to deliver the same. Employees are rewarded for creating an environment of customer delight.

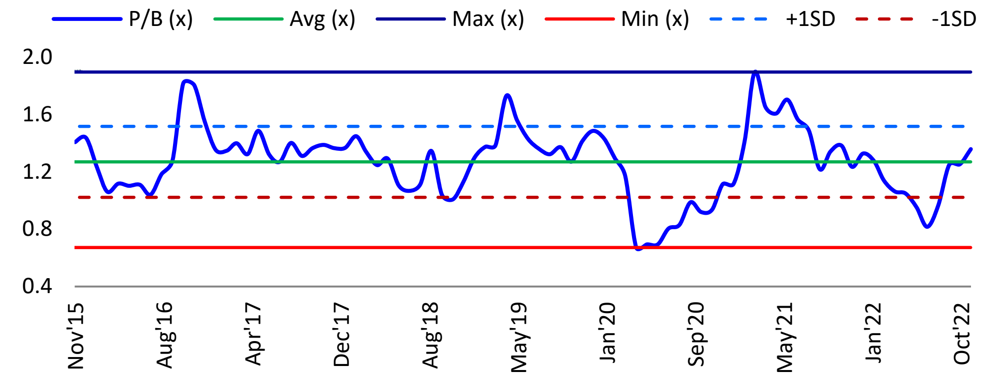
Governance

- The bank has an ESG Management Committee with business leaders across departments to monitor, compare, and enhance performance of the bank on key ESG-related metrics.
- IDFCFB has adopted various policies for rigorous governance. These measures have been supported by investors and other stakeholders of the bank.
- It is compliant with all regulations such as AML regulatory reporting, vigil mechanism, etc. and has won several awards from different agencies as recognition towards the ESG initiatives adopted.

Valuation & View: Growth levers in place; Initiate with BUY

- IDFCFB is entering a phase of strong loan growth as a drag from wholesale exposure falls due to a declining share in the overall mix. While its retail loan portfolio clocked an impressive 31% CAGR over the last three years, overall loan growth was capped at 6% CAGR due to the rundown of its legacy Infrastructure Financing book and cautious stance on its Corporate portfolio. Together, these two segments contributed 62% in FY19 v/s 26% in 1QFY23. We expect 21% loan growth CAGR over FY22-25E.
- The bank has scaled up its retail deposits (CASA/Retail TD) at a robust pace (73% CAGR over FY19-22). While the higher interest rates offered by the bank acted as the initial growth catalyst, attractive service quality, strong brand, and transparency is driving growth at present. As the bank continues to invest in its digital capabilities and branch expansion, the C/I ratio would stay elevated as compared to its peers. We expect 24% CAGR in CASA deposits over the next three years and a marginal improvement in CASA ratio to 49% by FY25E.
- The bank's capital adequacy ratio (CAR) stood at 15.8% as of 1QFY23, to support the traction in loan growth over the next couple of years. This would be augmented by rising profitability.
- We believe the worst of the asset quality pain is over as the bank makes use of the low cost of funds to transition to safer customer segments in lending. The objective is to maintain NIM ~6%, while reducing the risk profile of borrowers. Within wholesale, all possible stressed assets have been recognized and well provided for.
- **Initiate Buy with TP of INR70:** Thus, healthy growth in NII and rising fee income would be partially offset by higher OPEX, leading to a 35% CAGR in PPOP over FY22-25E. Controlled credit costs, led by stable asset quality, would therefore lead to a significantly higher growth in PAT over the same period. We expect return ratios to improve sharply and RoA/RoE to touch 1.3%/13.9% in FY25E. **We initiate coverage with a 'BUY' rating and a TP of INR70 (premised on 1.5x Sep'24E BV).**

Exhibit 56: IDFCFB's one-year forward P/BV ratio chart



Source: MOFSL, Company

Key risks

- **The slowdown in deposit growth momentum:** As all banks start to raise their focus on the mobilization of deposits and increase deposit rates, it may become difficult for IDFCFB to garner CASA/retail deposits in a meaningful manner.
- **Higher C/I ratio:** Sustained investments in building the retail franchise, especially on the liability side, may keep C/I ratio elevated as compared to its peers and the management's own guidance. This, in turn, would affect operating leverage and thus profitability of the bank.
- **A hiccup in retail asset quality:** While asset quality has held up in its retail portfolio so far, a global-led slowdown in domestic economy may hamper economic recovery and hurt income levels of the population at large. This, in turn, may have repercussions on the asset quality behavior of the bank's retail portfolio.

Financials and valuations

Income Statement

(INRm)

Y/E March	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Interest Income	1,19,482	1,63,076	1,59,679	1,71,727	2,13,713	2,61,224	3,22,842
Interest Expense	87,491	1,02,320	85,876	74,665	93,541	1,17,221	1,45,993
Net Interest Income	**31,991**	**60,756**	**73,803**	**97,062**	**1,20,172**	**1,44,003**	**1,76,849**
Growth (%)	77.9	89.9	21.5	31.5	23.8	19.8	22.8
Non Interest Income	8,521	17,222	22,113	32,220	39,631	49,539	62,914
Total Income	**40,512**	**77,977**	**95,916**	**1,29,282**	**1,59,803**	**1,93,542**	**2,39,763**
Growth (%)	38.9	92.5	23.0	34.8	23.6	21.1	23.9
Operating Expenses	58,867	58,610	70,933	96,444	1,14,551	1,34,526	1,58,942
Pre Provision Profits	**-18,356**	**19,367**	**24,983**	**32,837**	**45,252**	**59,015**	**80,821**
Growth (%)	NM	NM	29.0	31.4	37.8	30.4	36.9
Core PPP	**-18,681**	**15,463**	**19,014**	**27,374**	**40,061**	**54,084**	**76,137**
Growth (%)	NM	NM	23.0	44.0	46.3	35.0	40.8
Provisions (excl tax)	14,596	43,153	20,225	31,086	15,669	18,837	28,610
PBT	**-32,952**	**-23,785**	**4,758**	**1,752**	**29,583**	**40,178**	**52,211**
Tax	-13,510	4,857	235	297	7,455	10,125	13,157
Tax Rate (%)	41.0	NM	4.9	16.9	25.2	25.2	25.2
PAT	**-19,442**	**-28,642**	**4,523**	**1,455**	**22,128**	**30,053**	**39,054**
Growth (%)	NM	NM	NM	NM	NM	35.8	29.9

Balance Sheet

Y/E March	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Equity Share Capital	47,817	48,099	56,758	62,177	62,177	62,177	62,177
Reserves & Surplus	1,33,776	1,05,327	1,21,320	1,47,697	1,69,824	1,99,878	2,38,931
Net Worth	**1,81,593**	**1,53,426**	**1,78,079**	**2,09,874**	**2,32,001**	**2,62,055**	**3,01,108**
Deposits	**7,04,790**	**6,51,080**	**8,86,884**	**10,56,344**	**12,88,739**	**15,98,037**	**19,97,546**
Growth (%)	46.2	-7.6	36.2	19.1	22.0	24.0	25.0
of which CASA Dep	**91,139**	**2,09,397**	**4,58,961**	**5,11,704**	**6,46,947**	**7,89,430**	**9,76,800**
Growth (%)	59.6	129.8	119.2	11.5	26.4	22.0	23.7
Borrowings	6,99,834	5,73,972	4,57,861	5,29,626	5,95,702	6,76,112	7,67,779
Other Liabilities & Prov.	85,632	1,13,526	1,08,615	1,05,812	1,11,102	1,16,657	1,22,490
Total Liabilities	**16,71,849**	**14,92,004**	**16,31,439**	**19,01,655**	**22,27,545**	**26,52,860**	**31,88,923**
Current Assets	95,668	41,908	58,279	1,57,579	1,60,178	1,72,835	1,85,277
Investments	**5,84,754**	**4,54,046**	**4,54,117**	**4,61,448**	**5,49,124**	**6,58,948**	**7,90,738**
Growth (%)	-4.5	-22.4	0.0	1.6	19.0	20.0	20.0
Loans	**8,63,023**	**8,55,954**	**10,05,501**	**11,78,578**	**14,02,508**	**17,11,060**	**21,04,603**
Growth (%)	65.4	-0.8	17.5	17.2	19.0	22.0	23.0
Fixed Assets	9,502	10,377	12,664	13,612	14,613	15,630	16,857
Other Assets	1,18,902	1,29,719	1,00,877	90,598	1,01,123	94,387	91,448
Total Assets	**16,71,849**	**14,92,004**	**16,31,439**	**19,01,816**	**22,27,545**	**26,52,860**	**31,88,923**

Asset Quality	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
GNPA (INR m)	21,360	22,796	43,026	44,686	43,485	47,912	56,834
NNPA (INR m)	11,066	8,086	18,826	18,076	14,928	15,158	16,908
GNPA Ratio	2.48	2.66	4.28	3.79	3.10	2.80	2.70
NNPA Ratio	1.28	0.94	1.87	1.53	1.06	0.89	0.80
Slippage Ratio	3.4	3.1	6.0	6.9	2.4	2.1	2.1
Credit Cost	2.1	5.0	2.2	2.8	1.4	1.3	1.5
PCR (Excl Tech. write off)	48.2	64.5	56.2	59.5	65.7	68.4	70.3

Financials and valuations

Ratios

Y/E March	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Yield and Cost Ratios (%)							
Avg. Yield-Earning Assets	**8.8**	**11.3**	**11.1**	**10.4**	**10.9**	**11.2**	**11.5**
Avg. Yield on loans	11.3	14.0	13.6	13.0	13.7	13.9	14.0
Avg. Yield on Investments	6.6	7.6	6.8	5.8	6.6	6.9	7.2
Avg. Cost-Int. Bear. Liab.	**7.1**	**7.8**	**6.7**	**5.1**	**5.4**	**5.6**	**5.8**
Avg. Cost of Deposits	6.6	7.0	6.2	4.4	5.0	5.3	5.6
Interest Spread	**4.7**	**7.1**	**7.4**	**8.6**	**8.7**	**8.6**	**8.4**
Net Interest Margin	**2.4**	**4.3**	**5.3**	**6.1**	**6.4**	**6.4**	**6.5**
Capitalisation Ratios (%)							
CAR	15.5	13.4	13.8	16.7	15.5	14.4	13.4
Tier I	15.3	13.3	13.3	14.9	14.0	13.1	12.4
Tier II	0.2	0.1	0.5	1.9	1.6	1.3	1.0
Business and Efficiency Ratios (%)							
Loans/Deposit Ratio	122.5	131.5	113.4	111.6	108.8	107.1	105.4
CASA Ratio	12.9	32.2	51.7	48.4	50.2	49.4	48.9
Cost/Assets	3.5	3.9	4.3	5.1	5.1	5.1	5.0
Cost/Total Income	145.3	75.2	74.0	74.6	71.7	69.5	66.3
Cost/Core Income	146.5	79.1	78.9	77.9	74.1	71.3	67.6
Int. Expense/Int.Income	73.2	62.7	53.8	43.5	43.8	44.9	45.2
Fee Income/Total Income	20.2	17.1	16.8	20.7	21.6	23.0	24.3
Non Int. Inc./Total Income	21.0	22.1	23.1	24.9	24.8	25.6	26.2
Empl. Cost/Total Expense	19.0	26.1	27.9	28.0	27.5	27.4	27.2
Investment/Deposit Ratio	83.0	69.7	51.2	43.7	42.6	41.2	39.6

Profitability Ratios and Valuation

	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
RoE	-11.6	-17.1	2.7	0.7	10.0	12.2	13.9
RoA	-1.3	-1.8	0.3	0.1	1.1	1.2	1.3
RoRWA	-2.0	-2.6	0.4	0.1	1.5	1.7	1.8
Book Value (INR)	38.0	31.9	31.4	33.8	37.3	42.1	48.4
Growth (%)	-15.3	-16.0	-1.6	7.6	10.5	13.0	14.9
Price-BV (x)	**1.4**	**1.7**	**1.7**	**1.6**	**1.5**	**1.3**	**1.1**
EPS (INR)	-4.8	-6.0	0.9	0.2	3.6	4.8	6.3
Growth (%)	NM	NM	NM	NM	NM	35.8	29.9
Price-Earnings (x)	**NM**	**NM**	**62.9**	**NM**	**15.2**	**11.2**	**8.6**

REPORT GALLERY

RECENT INITIATING COVERAGE REPORTS

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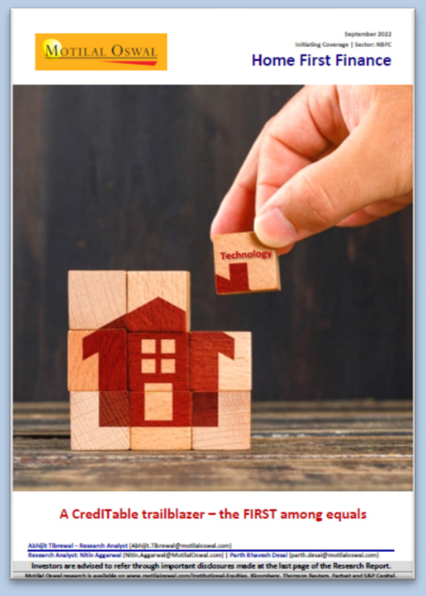

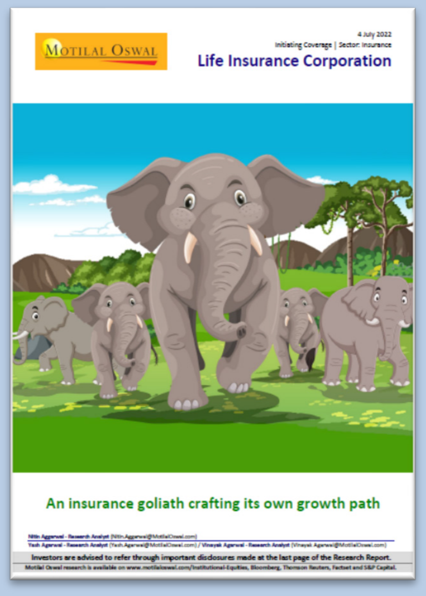

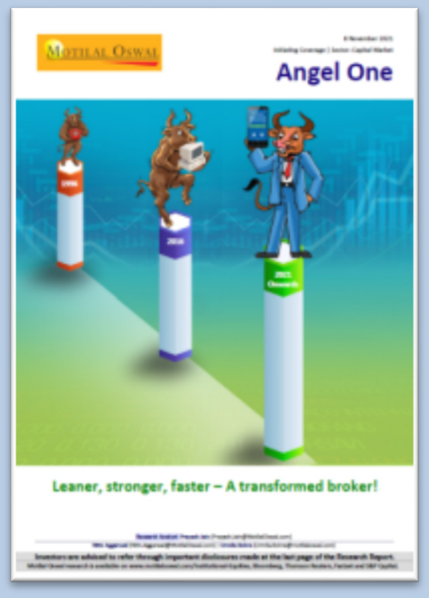

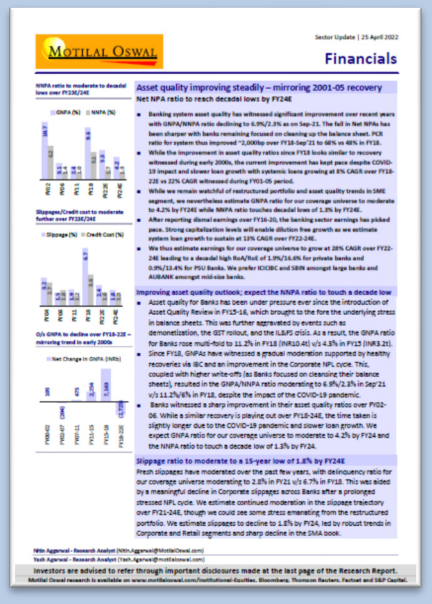

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall be within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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