21 May 2024

India | Equity Research | Company Update

IDFC FIRST Bank

Banking

Industry leading deposits and PAT growth to drive re-rating

We upgrade IDFC First Bank (IDFCFB) to **BUY** (from Hold) as we see the near-term (H1FY25) stagnation in the cost-income ratio/rise in credit costs likely being outweighed by industry-leading deposits/loan/PAT growth. For FY24-26, we see deposits growth (~13-14% CAGR) and PAT growth (mid-teen CAGR) as key challenges for the banking system. That said, we believe IDFCFB with industry leading deposits growth (26% CAGR over FY24-26; double of industry) and PAT growth (~30% CAGR; double of industry) look exciting. The bank is also likely to be least impacted by the RBI's *Projects Under Implementation* draft guidelines. Merger consummation within a quarter, or so, should lift FY25E/26E BVPS by 3–4% (not in our estimates yet) on reduced share-count. We broadly maintain our PAT estimates (upgrade of ~1%). We raise our TP to INR 95 (from INR 85), valuing the stock at ~1.7x FY26E ABV.

Upgrade to Buy on sustaining industry leading deposits growth and PAT growth over FY24-26E

In Jan'24, we downgraded IDFCB to *Hold* (from *Add*), envisaging a moderation in loan growth and an ensuing consolidation in operating ratios. The stock has since underperformed BANK NIFTY by ~15%. While we broadly maintain our RoA assumptions (PAT upgrade of ~1%) and envisage stagnant cost-income in the near term (1HFY25), we believe steep changes in the banking sector's operating environment warrant a constructive view on the stock. For FY24–26E, we see deposits growth (~13-14% CAGR) and PAT growth (mid-teen CAGR) as the key challenges for the banking system. That said, IDFCFB's industry-leading growth (double of industry) in deposits (26% CAGR) and PAT (~30% CAGR) looks exciting. We believe the near-term stagnation in the cost-income ratio and inch-up in credit costs will likely be outweighed by industry-leading deposits, loan and PAT growth.

IDFCB is also least likely to be impacted by RBI's draft guidelines on *Projects Under Implementation* (link). Merger consummation (link) within a quarter or so, should also help improve FY25E/26E BVPS by 3–4% (not in estimates yet). Other strong positives in the form of likely longevity of MD&CEO and strong incremental unit economics remain unchanged. We raise our TP from INR 85 to INR 95, valuing the stock at ~1.7x FY26E (earlier ~1.7x on FY25 ABV). Key risks are higher than expected rise in stress impacting growth and profitability.

Financial Summary

Y/E March	FY23A	FY24A	FY25E	FY26E
NII (INR bn)	126.4	164.5	202.2	243.2
Op. profit (INR bn)	49.3	62.4	84.0	109.6
Net Profit (INR bn)	24.4	29.6	36.9	50.6
EPS (INR)	3.7	4.2	5.2	7.2
EPS % change YoY	1,501.1	13.6	24.7	37.1
ABV (INR)	37.4	44.3	49.4	56.3
P/BV (x)	2.0	1.7	1.5	1.3
P/ABV (x)	2.1	1.7	1.6	1.4
Return on Assets (%)	1.1	1.1	1.1	1.3
Return on Equity (%)	10.4	10.2	10.8	13.2

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Market Data

Market Cap (INR)	546bn
Market Cap (USD)	6,553mn
Bloomberg Code	IDFCFB IN
Reuters Code	IDFB BO
52-week Range (INR)	101 /66
Free Float (%)	55.0
ADTV-3M (mn) (USD)	45.0

Price Performance (%)	3m	6m	12m
Absolute	(6.8)	(9.3)	15.3
Relative to Sensex	(8.9)	(21.6)	(4.8)

Earnings Revisions (%)	FY25E	FY26E
PAT	1	1

Previous Reports

22-04-2024: Q4FY24 results review
22-01-2024: Q3FY24 results review

Deposits growth to sustain at >2x industry growth

IDFCFB has delivered industry-leading deposits growth in FY24 and is likely to sustain its leadership over FY24-26E. The bank delivered a staggering 63% CAGR in retail deposits, since merger. For FY24, it delivered industry-leading overall deposits growth of ~39% YoY (almost double of the top four private banks). Growth has also been fairly consistent with ~8% QoQ run-rate (7-10% QoQ range) for the last few quarters. The bank has mobilized ~INR 550bn YoY in FY24 and targets ~INR 600 bn for FY25 (~30% YoY growth) with expanded distribution.

Importantly, we note that IDFCFB has seen amongst the lowest rise in calculated cost of funds YoY in FY24, partly aided by re-payment of high-cost borrowings (which should continue in FY25 as well) suggesting an improved funding profile.

The LDR has improved to 97% in FY24, from 105% YoY and is likely to improve further. Higher deposits growth should also enable the bank to run-down higher-yielding legacy borrowings as well. We believe that strong deposits growth should help create sizeable option value in broadening its asset mix and bettering cross-sell opportunities.

Loan growth to stay industry-leading at ~20% CAGR over FY24-26

The bank has delivered ~25% YoY growth in total gross loans and advances in FY24. It aims for strong ~20% CAGR for the same over FY24–29E. We build ~23/20% YoY growth in loans for FY25E/26E. While there is deceleration in loan growth vs. FY24, we reckon that growth (in FY25/26) should still be industry-leading. We also believe that slight moderation in growth should also entail relatively lower risks and enable a broad-based loan mix.

Cost-to-income to improve H2FY25 onwards

The bank saw more than 500bps of YoY improvement in its core cost-to-income ratio in FY23 though it was flattish (deterioration of 40bps YoY) in FY24. Cost-to-income ratio seems to be stabilising for the banks' retail, rural and SME businesses (at ~55% in FY24). Cost-to-income ratio for the credit card segment has seen massive improvement from 165% in FY23 to 116% in FY24 and is likely to break-even by FY25. Cost-to-income ratio in branch banking (liabilities) continues to remain elevated at 186% in FY24 (vs. 174% YoY) on expanding distribution/resources, which should improve as scale-kicks in. On an overall basis, Cost-to-income ratio is likely to remain flattish in H1FY25, partly on continued investments. The FLDG costs should come-in base from Q3FY25. The bank should see visible improvement by H2FY25, aided by break-even in the credit card business and redemption of high-cost legacy borrowings. We recon that, of all the metrices under guidance shared earlier, the progress on cost-to-income has been bit slower, partly impacted by external factors as well. We build in cost-to-income improving from 72% in FY24 to 70%/67% by FY25E/26E.

Asset quality to remain stable; credit costs could rise in H1FY25, before improving in H2FY25

IDFCB has consistently maintained comfortable asset quality over the last few years with successive improvement in GNPA, slippages and net NPA ratios. As of FY24, GNPA and net NPA stand at 1.9% and 0.6%, respectively. All retail, rural and SME product segments have <2% GNPA and net NPA at <1%. Slippages for FY24 improved to 2.7% (vs. 3% YoY) while net slippages stood at 1.4% (vs. 1.5% YoY). Credit costs (calculated) also moderated to 1.3% vs. 1.7% YoY. SMA 1+2 pool has been consistently muted at ~0.85%.

We highlight that the bank seems to be the most efficient in pricing the risks, as measured in NIM adjusted for credit costs. While part of the high NIM can be explained by the high-touch opex-intensive sector, nonetheless, we believe the bank could still sustain its edge on credit costs adjusted NIM going ahead.

IDFCB has seen a marginal uptick in its credit costs (calculated) trajectory, from ~1.2% in Q1FY24 to ~1.5% Q4FY24. The bank is guiding for a small upward normalisation in credit costs to ~1.6% for FY25 (vs. 1.3% for FY24 and ~1.5% in Q4FY24), partly as recoveries from the post-pandemic pool is drying out. While the bank is likely to see credit costs inch-up in H1FY25, it estimates that H2FY25 should see moderation – with benefits coming from FLDG agreements. We are building-in gross slippages at ~2.7% for FY25 with ~1.6% credit costs.

RoA to retain rising trajectory; model 30% PAT CAGR over FY24–26E

We believe IDFCFB shall continue delivering industry-leading deposits and loans growth (off low market share of ~1–1.2%), leveraging the under-penetrated retail segment and expanding distribution/customers/product segments. We estimate a broadly stable NIM with a rise in deposits costs/ higher LDR to be offset by redemption of high-cost borrowings. In-line with management's view, we expect stable cost to income and rise in credit costs in H1FY25 but improved H2FY25, led by improving scale and redemption of high-cost legacy borrowings. Overall, we see RoA rising to ~1.1%/1.3% by FY25E/26E and RoE rising to ~11%/13% in the same period. We estimate the bank to deliver amongst the highest PAT CAGR of ~30% over FY24–26E. We reckon that the bank should be able to deliver loan, deposit and PAT CAGR for FY24–26E at ~2x industry levels.

Likely management longevity aids comfort

Management longevity has been a vital ingredient in the superior stock performance of private banks across cycles. Similarly, the frequent change in MD&CEO has spooked investors' confidence in the long-term vision and culture of the bank. Among private banks in India, IDFCFB seems to stand out with management longevity. The incumbent MD&CEO (in mid-50s) has age in his favour. He would complete his second three-year term in Dec'24 and can theoretically lead the bank for another nine years.

Reverse merger to improve BVPS due to reduced number of shares

The board of the bank and IDFC Ltd. have approved a reverse merger. Most of the requisite approvals/NOCs from RBI, SEBI, BSE, NSE and CCI are in place. Overall, it appears that the reverse merger should be effective within the next three–four months. The merger should ideally reduce the number of shares by ~2.4% and there could be small addition to net-worth.

Overall, we believe the reverse merger should lead to a 3–4% rise in book value per share for FY25E/26E. We have NOT incorporated the same in our FY25/26 estimates.

Minimal impact by draft guidelines on *Projects Under Implementation*

RBI has recently come out with draft guidelines (link) on *Projects Under Implementation* (PUI), seeking staggered standard asset provisions up to 500bps on project exposure. Positively, IDFCFB has chosen granular and retail assets as growth drivers. The legacy infrastructure loan book has been a non-focus area and has reduced to ~1% of loans and is likely to run-down in full over the next few years. Thus, the bank should have minimal impact under the proposed guidelines.

Ahead of the curve digital capabilities

IDFCB has scaled various offerings in the last two years, leveraging technology and also driving efficiency and enhanced control. Its mobile banking app ranks higher and favourably across peers highlighting the sharp focus on digital experience. The bank believes that its current systems are scalable and have been designed keeping in mind the likely jump in volumes over the next few years. IDFCB has been investing heavily in technology, which is visible in bulky other miscellaneous expenditure of the bank. Importantly, as against peers, the bank's entire tech stack is newly built as per the extant architecture, and thus, has the least probability of any significant bottlenecks.

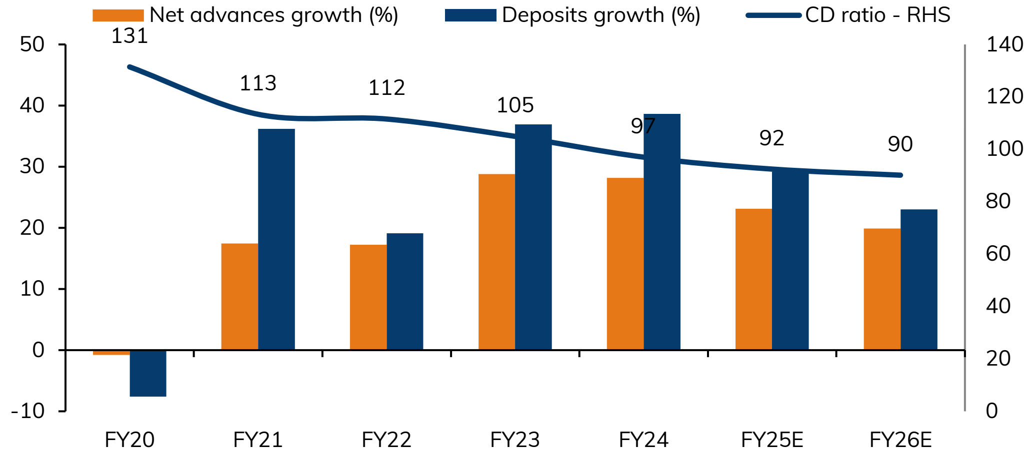
Past capital raises have been book-value accretive and less dilutive

IDFCB has been delivering strong loan growth along with superior risk-adjusted NIM, though RoE has been weighed down by huge upfront investments. Slower growth in net-worth addition coupled with strong growth in assets has resulted in frequent capital raises by the bank.

Interestingly, for the last four years, we highlight that capital raises have happened at successively higher stock prices; thus, accretive to book value. Similarly, the equity dilution percentage has been successively declining. As of FY24, the bank has CET 1 of 13.36% with total CAR of 16.11%.

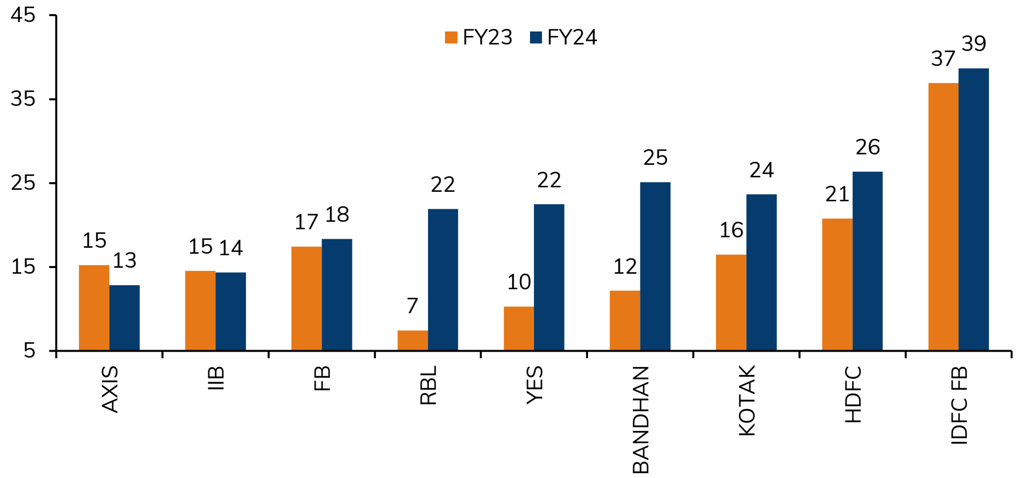
Story in charts

Exhibit 1: Despite slight moderation YoY, IDFCFB should deliver industry-leading deposits growth (~26% CAGR) and loan growth (22% CAGR) over FY24-26E



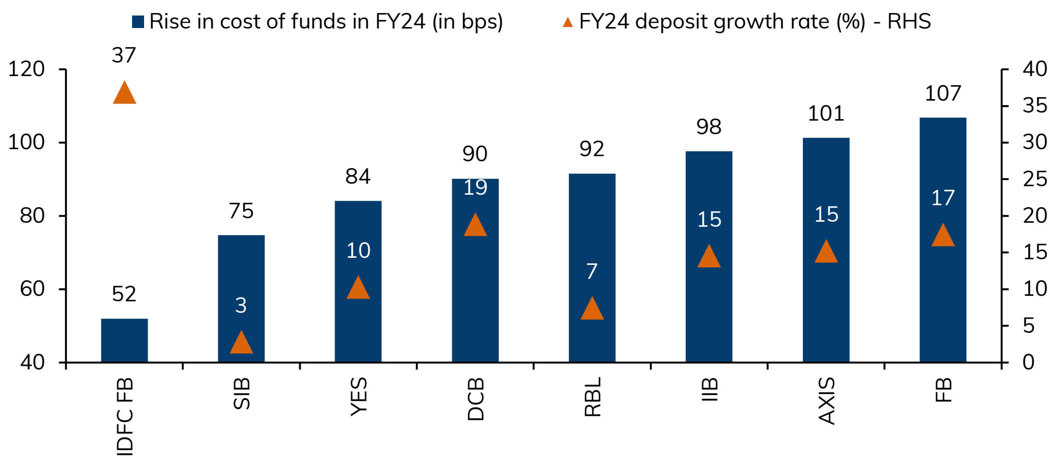
Source: Company data, I-Sec research

Exhibit 2: For FY23/24, IDFCFB delivered deposits growth at 37%/39% YoY, almost 1.5–2x of larger peers



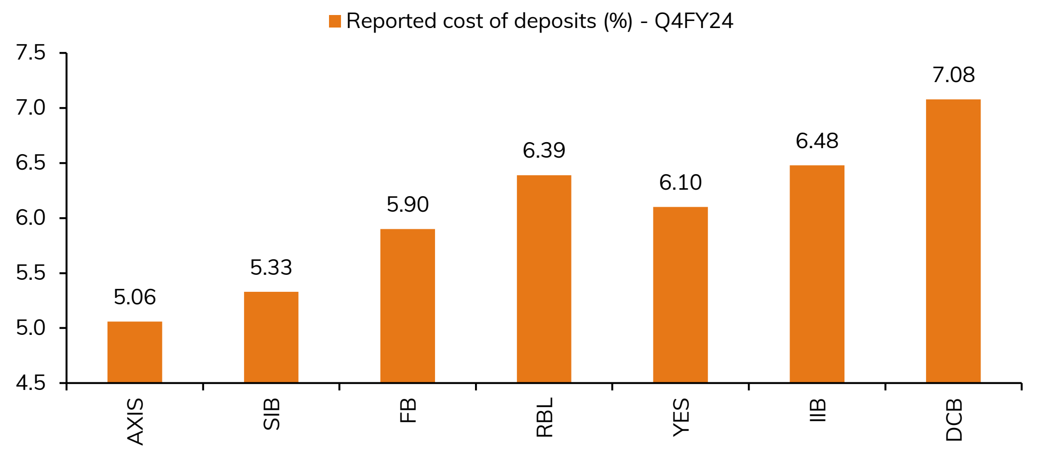
Source: Company data, I-Sec research

Exhibit 3: IDFCFB has seen amongst the lowest rises in cost of funds YoY in FY24, partly aided by redemption of high-cost borrowing but also suggestive of an improving deposits franchise



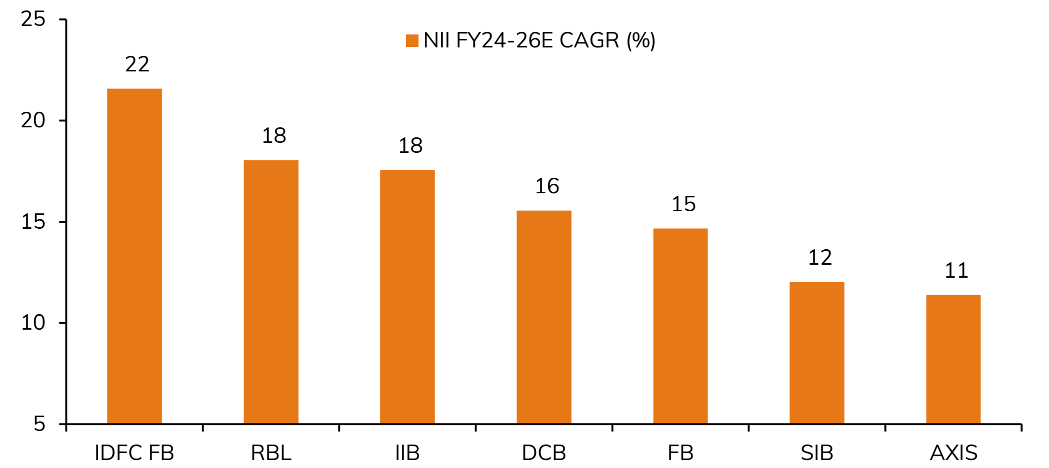
Source: Company data, I-Sec research

Exhibit 4: The bank has reported cost of deposits ~120bps higher than larger peers, but lower than IIB/RBL



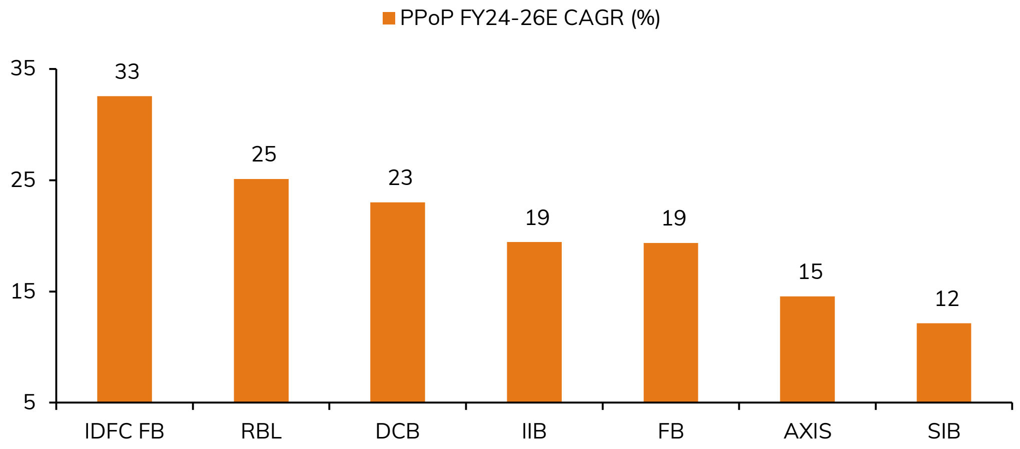
Source: Company data, I-Sec research

Exhibit 5: We estimate IDFCFB to deliver superior NII CAGR over FY24–26, driven by strong growth and stable NIM



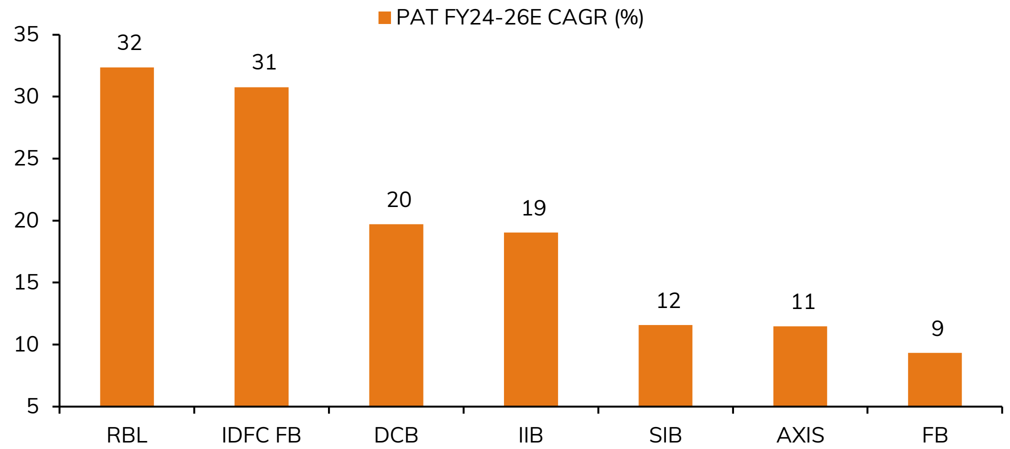
Source: Company data, I-Sec research

Exhibit 6: We estimate IDFCFB to lead the pack on PPOP CAGR for FY24-26E



Source: Company data, I-Sec research

Exhibit 7: Overall, we see IDFCFB delivering >30% CAGR in PAT over FY24-26, amongst the highest across peers



Source: Company data, I-Sec research

Exhibit 8: IDFCFB's mobile app ranks around highest vs. peers across Android and IOS

Name of the Bank	App Name	Mobile app rating		Latest net adv. (INR bn)
		Android	Apple	
AXIS	Axis Mobile	4.6	4.8	9,651
BANDHAN	mBandhan	3.4	2.2	1,102
FB	FedMobile	4.4	3.5	2,094
HDFC	HDFC Bank MobileBanking	3.8	3.3	24,849
IDFC FB	**IDFC First Bank MobileBanking**	**4.8**	**4.7**	**1,946**
IIB	IndusMobile	4.2	4.5	3,433
KOTAK	Kotak Mobile	4.1	4.8	3,761
RBL	MoBank	4.0	4.0	840
SBI	YONO	4.2	3.7	35,195
YES	iris by YES Bank	2.3	3.9	2,278

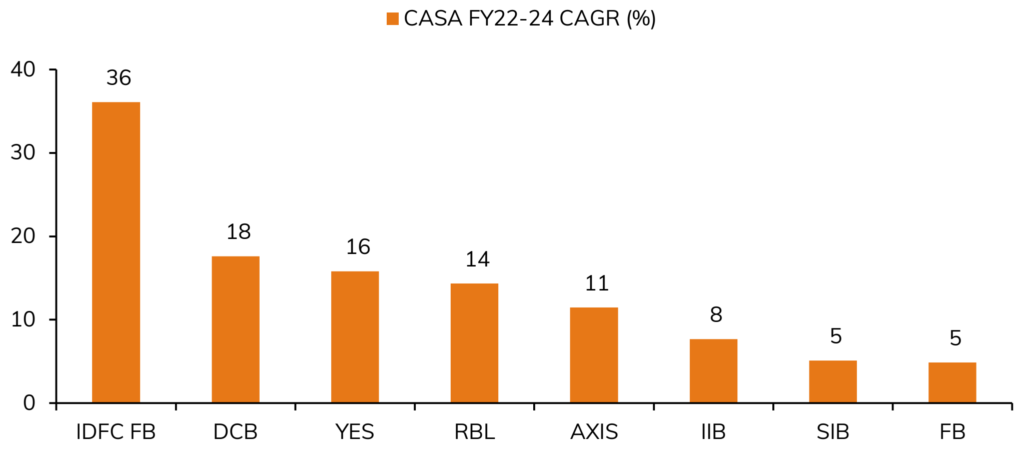
Source: Company data, I-Sec research

Exhibit 9: Capital raises have been regular, though dilution has been lower successively

Fiscal Year	Month	Mode	Capital Raise (INR bn)	Price	Dilution (post money)
FY21	Jun;20	Preferential	20.0	23	15.2%
FY22	Apr'21	QIP	30.0	57	8.4%
FY23	Mar'23	Preferential	22.0	58	5.7%
FY24	Oct'23	QIP	30.0	90	4.7%

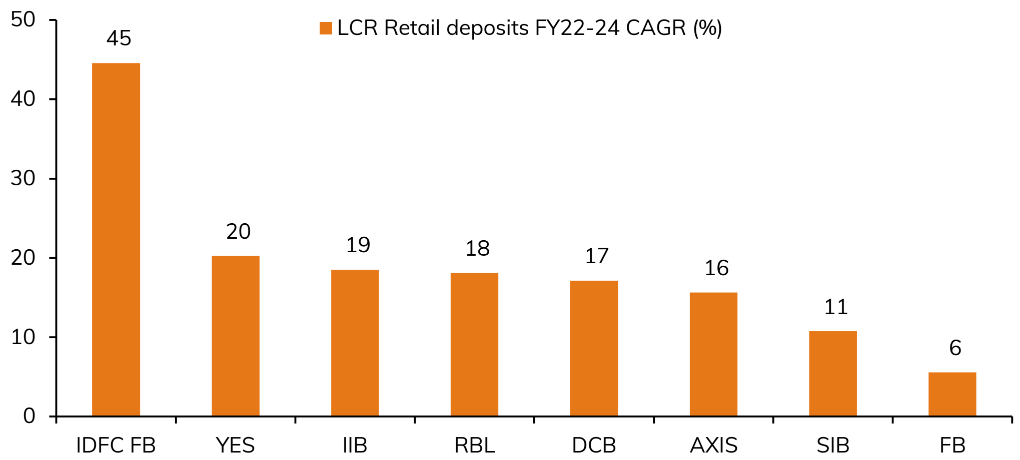
Source: Company data, I-Sec research

Exhibit 10: The bank's CASA CAGR over FY22-24 has been amongst the highest versus peers



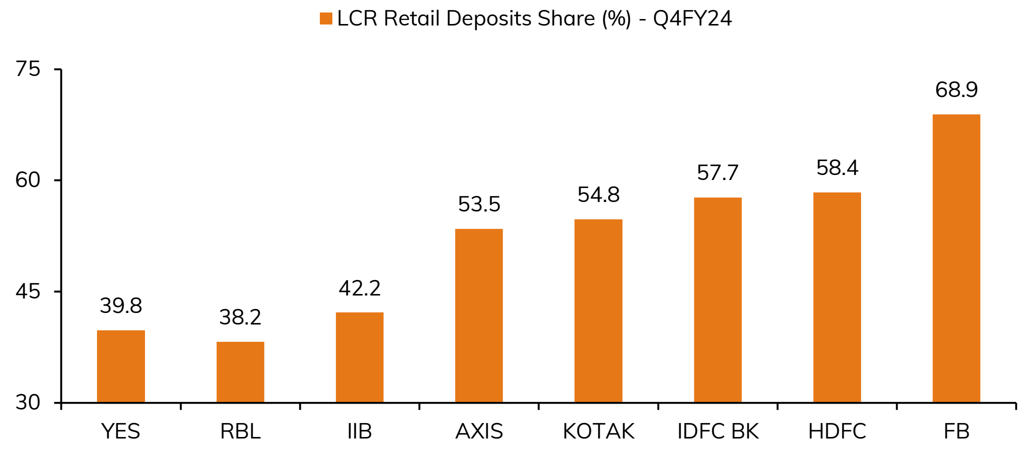
Source: Company data, I-Sec research

Exhibit 11: Retail deposits growth has been head and shoulder above others, creating strong option value for coming years



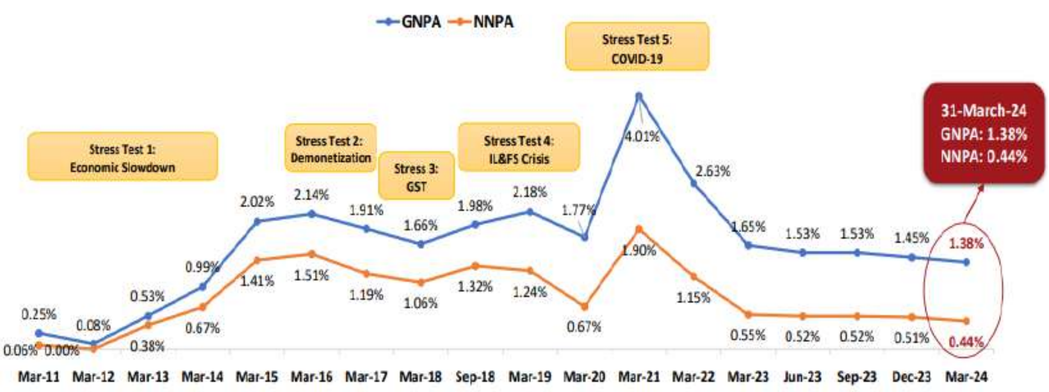
Source: Company data, I-Sec research

Exhibit 12: Retail LCR deposits share is comparable to large peers



Source: Company data, I-Sec research

Exhibit 13: Maintained high retail asset quality GNPA of ~2% and NNPA of ~1% for a decade, across cycles



Source: Company data, I-Sec research

Exhibit 14: All of IDFCFB's products have low GNPA and NNPA

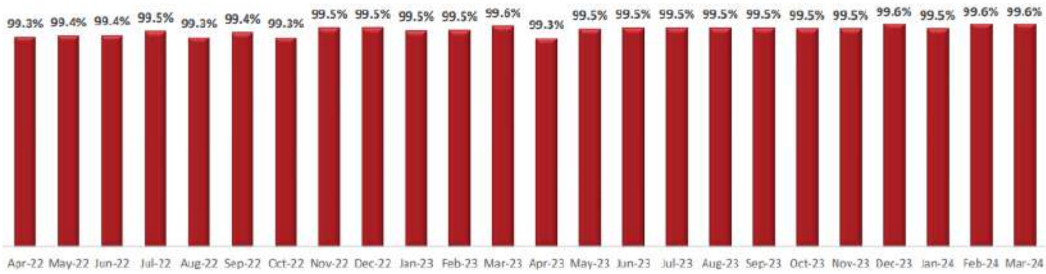
Segment	Gross Advances Breakup (Rs. Crore)	Gross NPA	Net NPA
Home Loan	22,325	0.75%	0.33%
Loan Against Property	24,247	1.59%	0.67%
Vehicles	20,827	1.52%	0.59%
Consumer Loans	28,659	1.72%	0.52%
Rural Finance	23,882	1.01%	0.20%
Digital, Gold & Others	17,527	1.80%	0.41%
Credit Cards	5,546	1.76%	0.39%
SME Finance	23,591	1.20%	0.38%
Corporate (Non-Infra)	28,213	2.55%	0.26%
Infrastructure Finance	2,643	26.45%	15.55%
Overall Bank	1,97,459	1.88%	0.60%
Bank (Excluding Infra)	1,94,816	1.55%	0.42%

Source: Company data, I-Sec research

Exhibit 15: Collection efficiency is strong and steady

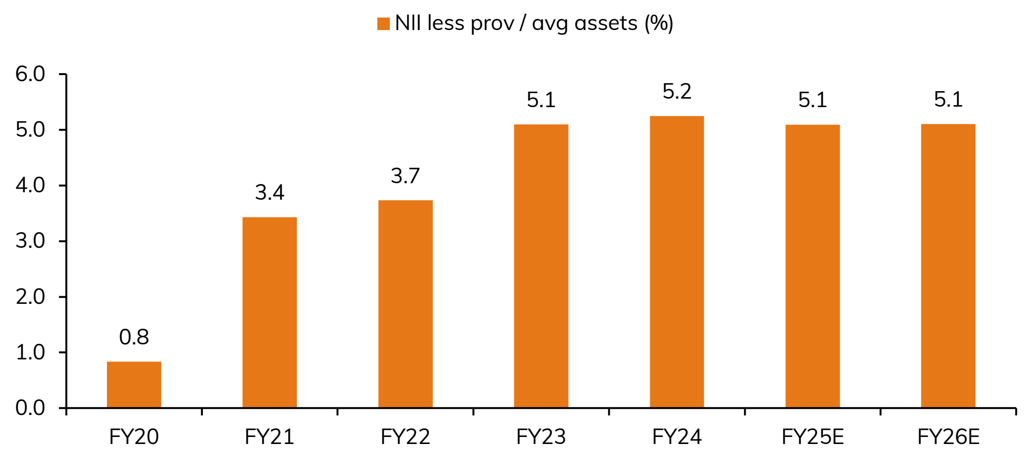
Definition:
Collection Efficiency % = (Pos of EMI Collected for the Month)/(Pos of EMI Due for the month)* 100

Note: Collections does not include any arrear collections, or prepayment collections in these calculations, and hence represents the true picture of collections efficiency.



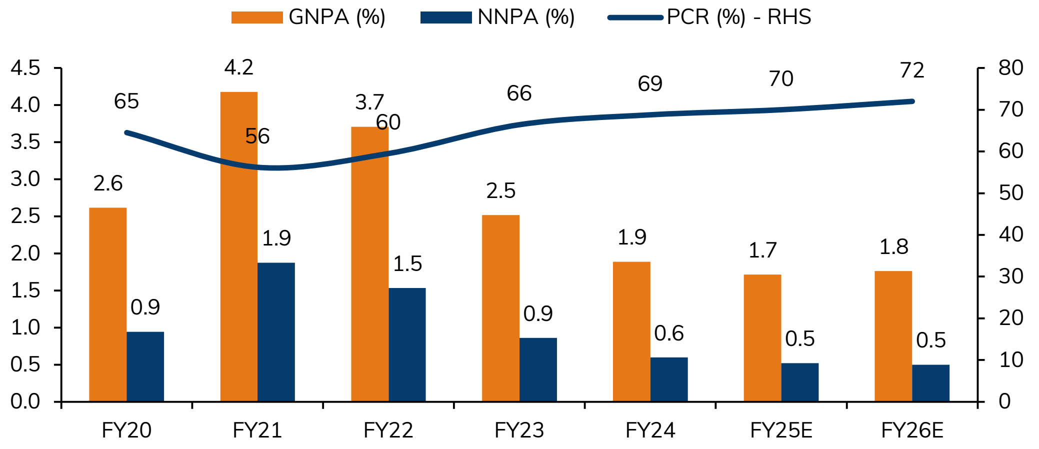
Source: Company data, I-Sec research

Exhibit 16: While higher NII (as % of assets) is partly due to higher opex segment, we believe IDFCFB has managed to price risk much better vs. peers



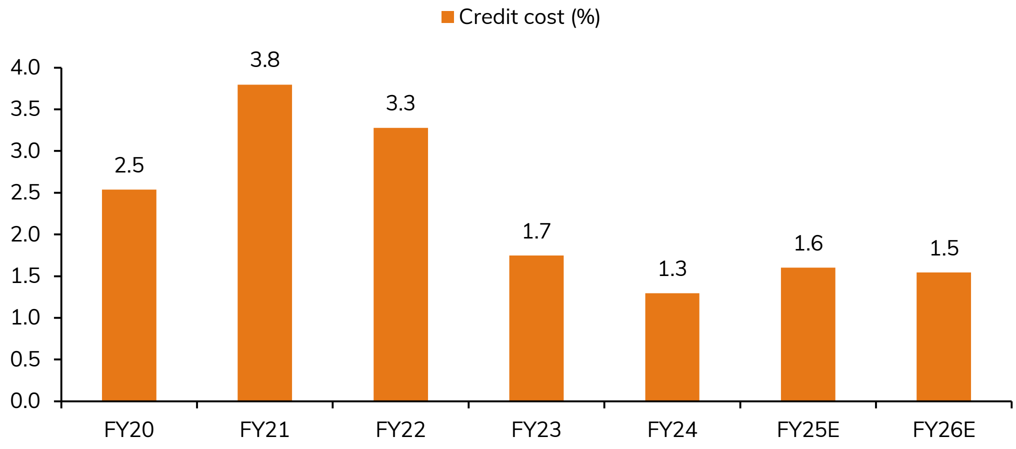
Source: Company data, I-Sec research

Exhibit 17: Headline GNPA and NNPA have improved over the years and are likely to remain stable going ahead



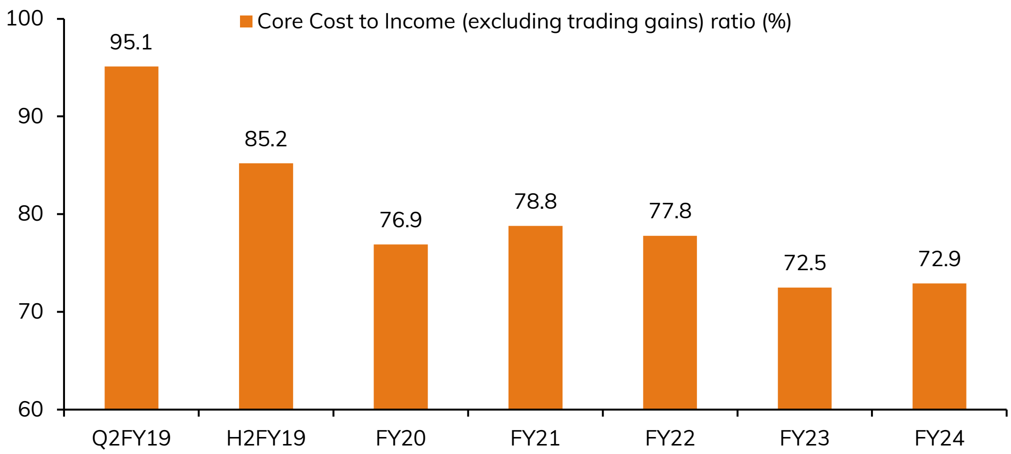
Source: Company data, I-Sec research

Exhibit 18: Credit costs are likely to normalise upwards in FY25E/26E



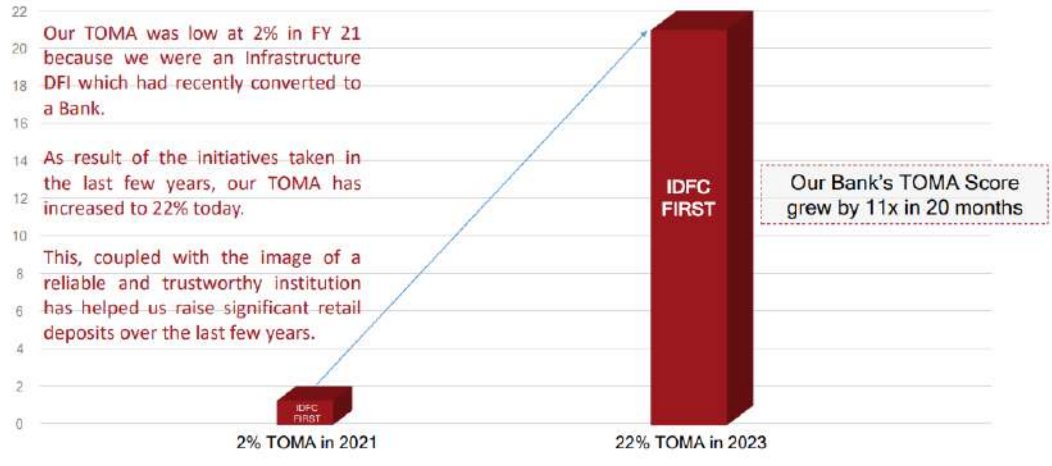
Source: Company data, I-Sec research

Exhibit 19: Cost-to-income ratio flattish in FY24; likely to improve in H2FY25



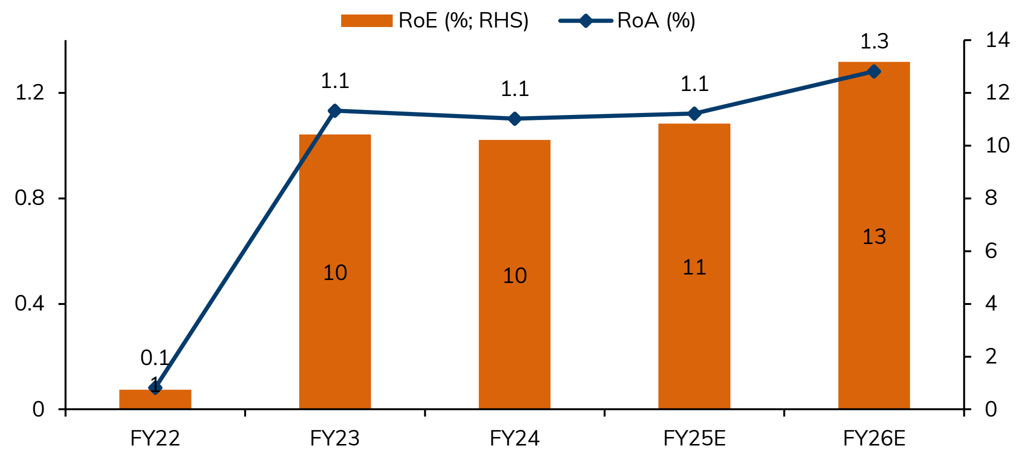
Source: Company data, I-Sec research

Exhibit 20: The bank has significantly increased 'top of mind awareness' score



Source: Company data, I-Sec research

Exhibit 21: RoA/RoE to rise to ~1.1%/1.3% and ~11/13% by FY25E/26E



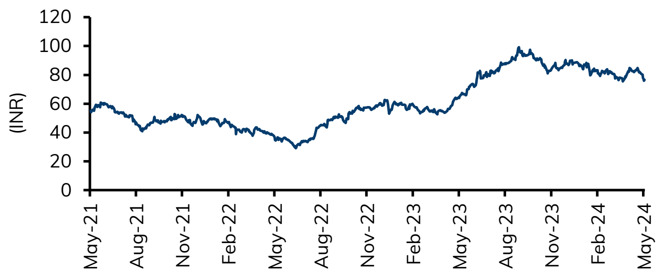
Source: Company data, I-Sec research

Exhibit 22: Shareholding pattern

%	Sep'23	Dec'24	Mar'24
Promoters	39.4	37.5	37.4
Institutional investors	30.1	30.9	30.5
MFs and other	2.7	3.4	2.7
FIs/ Banks	0.0	0.1	0.0
Insurance Cos.	2.2	2.5	3.6
FIIs	25.2	24.9	24.2
Others	30.5	31.6	32.1

Source: Bloomberg, I-Sec research

Exhibit 23: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 24: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Interest income	227,275	303,225	370,505	445,036
Interest expense	100,922	138,718	168,351	201,881
Net interest income	**126,353**	**164,508**	**202,153**	**243,155**
Non-interest income	44,670	60,020	73,586	88,815
Operating income	**171,023**	**224,528**	**275,739**	**331,970**
Operating expense	121,704	162,158	191,778	222,388
Staff expense	37,422	48,925	56,753	64,699
Operating profit	**49,320**	**62,370**	**83,962**	**109,582**
Core operating profit	**46,139**	**58,870**	**79,938**	**105,076**
Provisions & Contingencies	16,648	23,817	34,678	41,990
Pre-tax profit	**32,671**	**38,553**	**49,284**	**67,593**
Tax (current + deferred)	8,300	8,988	12,420	17,033
Net Profit	**24,371**	**29,565**	**36,864**	**50,559**
Adjusted net profit	**24,371**	**29,565**	**36,864**	**50,559**

Source Company data, I-Sec research

Exhibit 25: Balance sheet

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Cash and balance with RBI/Banks	138,980	124,802	199,709	237,587
Investments	611,236	747,104	852,924	971,592
Advances	1,517,945	1,945,924	2,395,829	2,873,019
Fixed assets	20,901	26,194	29,727	33,711
Other assets	110,355	117,127	134,680	154,791
Total assets	**2,399,417**	**2,961,151**	**3,612,868**	**4,270,701**
Deposits	1,446,373	2,005,763	2,591,223	3,187,434
Borrowings	572,121	509,356	481,219	467,750
Other liabilities and provisions	123,711	124,419	181,949	206,480
Share capital	66,181	70,699	70,699	70,699
Reserve & surplus	191,030	250,914	287,778	338,338
Total equity & liabilities	**2,399,417**	**2,961,151**	**3,612,868**	**4,270,701**
% Growth	26.2	23.4	22.0	18.2

Source Company data, I-Sec research

Exhibit 26: Growth ratios

(%, year ending March)

	FY23A	FY24A	FY25E	FY26E
Net Interest Income	30.2	30.2	22.9	20.3
Operating profit	50.2	26.5	34.6	30.5
Core operating profit	68.5	27.6	35.8	31.4
Profit after tax	1,575.1	21.3	24.7	37.1
EPS	1,501.1	13.6	24.7	37.1
Advances	28.8	28.2	23.1	19.9
Deposits	36.9	38.7	29.2	23.0
Book value per share	15.1	17.0	11.5	14.1
Adj Book value per share	18.3	18.4	11.6	14.1

Source Company data, I-Sec research

Exhibit 27: Key ratios

(Year ending March)

	FY23A	FY24A	FY25E	FY26E
No. of shares and per share data				
Adjusted EPS	3.7	4.2	5.2	7.2
Book Value per share	39	45	51	58
Adjusted BVPS	37	44	49	56
Valuation ratio				
PER (x)	21.0	18.5	14.8	10.8
Price/ Book (x)	2.0	1.7	1.5	1.3
Price/ Adjusted book (x)	2.1	1.7	1.6	1.4
Dividend Yield (%)	-	-	-	-
Profitability ratios (%)				
Yield on advances	14.2	15.0	14.5	14.4
Yields on Assets	10.6	11.3	11.3	11.3
Cost of deposits	5.0	5.9	5.9	5.8
Cost of funds	4.7	5.2	5.1	5.1
NIMs	6.3	6.5	6.5	6.5
Cost/Income	71.2	72.2	69.6	67.0
Dupont Analysis (as % of Avg Assets)				
Interest Income	10.6	11.3	11.3	11.3
Interest expended	4.7	5.2	5.1	5.1
Net Interest Income	**5.9**	**6.1**	**6.2**	**6.2**
Non-interest income	2.1	2.2	2.2	2.3
Trading gains	0.1	0.1	0.1	0.1
Fee income	1.9	2.1	2.1	2.1
Total Income	**8.0**	**8.4**	**8.4**	**8.4**
Total Cost	**5.7**	**6.1**	**5.8**	**5.6**
Staff costs	1.7	1.8	1.7	1.6
Non-staff costs	3.9	4.2	4.1	4.0
Operating Profit	**2.3**	**2.3**	**2.6**	**2.8**
Core Operating Profit	2.1	2.2	2.4	2.7
Non-tax Provisions	0.8	0.9	1.1	1.1
PBT	**1.5**	**1.4**	**1.5**	**1.7**
Tax Provisions	0.4	0.3	0.4	0.4
Return on Assets (%)	**1.1**	**1.1**	**1.1**	**1.3**
Leverage (x)	9.2	9.3	9.7	10.3
Return on Equity (%)	**10.4**	**10.2**	**10.8**	**13.2**
Asset quality ratios (%)				
Gross NPA	2.5	1.9	1.7	1.8
Net NPA	0.9	0.6	0.5	0.5
PCR	66.4	68.8	70.0	72.0
Gross Slippages	3.9	3.5	3.3	2.7
LLP / Avg loans	1.9	1.7	1.7	1.6
Total provisions / Avg loans	1.2	1.4	1.6	1.6
Net NPA / Networth	5.1	3.6	3.5	3.5
Capitalisation ratios (%)				
Core Equity Tier 1	14.2	13.3	12.5	12.1
Tier 1 cap. adequacy	14.2	13.4	12.5	12.1
Total cap. adequacy	16.8	16.1	15.3	15.0

Source Company data, I-Sec research

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