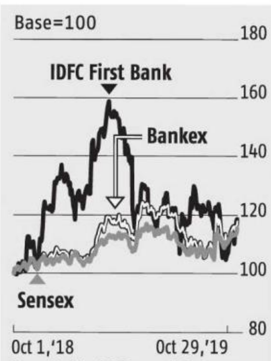
IDFC First Bank progressing on its promises

Valuation of 1.1x its FY21 book makes it an attractive bet



Compiled by BS Research Bureau

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After a prolonged period of underperformance operationally and on the bourses, things seem to be getting better for IDFC First Bank. The September quarter (Q2FY20) results highlight the same, especially three metrics — improved mix of retail assets, sharp rise in deposits, and an increase in profitability.

The share of wholesale loans fell from 87 per cent last year to 55 per cent in Q2, with the segment's exposure down by about ₹10,000 crore.

The share of retail loans, which came from the merger with Capital First, rose to 45 per cent in Q2, from 10 per cent a year ago, which was prior to the merger. While the loan book at ₹1 trillion may have shrunk following the bank's move to rationalise its wholesale loans, retail loans grew 7.7 per cent sequentially (in line with the industry trend). This suggests the composition of assets is moving in favour of retail loans.

A similar impact was felt on liabilities as well, with the share of low-cost current account savings account (CASA) deposits increasing to 18.7 per cent in Q2, from 8 per cent last year.

While the bank has to go a long way to reach the 30 per cent-mark that many private banks maintain, the Q2 numbers show it is in the right direction. The 34 per cent increase in share of retail deposits (CASA plus retail term deposits) to overall liabilities in Q2, is also a positive.

Given that retail banking is now a significant component, profitability also improved sharply from 1.6 per cent a year ago to 3.4 per cent in Q2. At these levels, the net interest margin (NIM) of IDFC First Bank matches the average of the top private banks. Asset quality was stable, but one needs to keep a tab on the ₹5,400-crore exposure, including non-funded exposure (5 per cent of gross loans), which the bank has to the telecom sector. As this was the first quarter in which the bank recorded profit before tax, it instils some confidence that the merger is yielding results. Whether the bank can touch the 13-15 per cent projected return on equity by 2023-24 needs to be seen.

Analysts at Prabhudas Lilladher say the continued retailisation of loans, traction in liabilities, an upward NIM trajectory, and steady asset quality provide comfort in the medium-to-long term.

Valuations at 1.1 times its 2020-21 estimated book, which is also the lowest among private banks, makes for an attractive bet.