RESEARCH

[SECTOR REPORT] BUILDING MATERIALS

Strong foundations

HDFC BANK | TARGET: Rs 1,896 | +23% | BUY

Margin pressure dampens performance

SUMMARY

[SECTOR REPORT] BUILDING MATERIALS

- India's building materials industry is on a strong footing given the anticipated revival in real estate cycle and rising organised share
- Valuations price in the positives for most building material stocks, capping upside potential
- We initiate on 3 stocks (APOLP, HINDWARE, PRINCPIP) and assume coverage on 10; HINDWARE, SOMC and MTLM are our only BUYs

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HDFC BANK

- Operationally weak December quarter due to elevated cost of funds and increased provisions
- Reported NIM flat QoQ at 3.6% and PAT up only 2.5% QoQ to Rs 164bn; asset quality stable
- Maintain BUY with TP revised to Rs 1,896 (vs. Rs 1,929) as we adjust FY24/ FY25 PAT estimates by -6%/+1% and roll valuations over

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Daily macro indicators

Indicator	15-Jan	16-Jan	Chg (%)
US 10Y yield (%)	3.94	4.06	12bps
India 10Y yield (%)	7.15	7.15	0bps
USD/INR	82.89	83.08	(0.2)
Brent Crude (US$/bbl)	78.2	78.3	0.2
Dow	37,593	37,361	(0.6)
Hang Seng	16,216	15,866	(2.2)
Sensex	73,328	73,129	(0.3)
India FII (US$ mn)	**12-Jan**	**15-Jan**	**Chg ($ mn)**
FII-D	314.8	77.7	(237.2)
FII-E	(51.9)	243.2	295.1

Source: Bank of Baroda Economics Research

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BUILDING MATERIALS

17 January 2024

Strong foundations

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- **We initiate on 3 stocks (APOLP, HINDWARE, PRINCPIP) and assume coverage on 10; HINDWARE, SOMC and MTLM are our only BUYs**

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Positive on industry growth, cautious on valuations: We assume coverage on India's building materials sector with a positive outlook in anticipation of a broad-based revival in the domestic real estate market and a gradual formalisation of the materials sector. Even so, we are cautious on most building material stocks as their valuations look full – our universe is trading at 41x on 1Y forward P/E vs. the 5Y average of 31.7x. We prefer only a few select names, viz. HINDWARE, SOMC and MTLM, where we see strong earnings potential alongside reasonable valuations.

Plastic Pipes – fastest growing segment: We are positive on this space as it is the fastest growing segment in the building materials industry and has lower risk of MTM inventory loss from Q4FY24 onward as global PVC resin prices are trading well below the 20Y avg. However, we have HOLD ratings on the top 5 names – SI (TP Rs 4,300), ASTRA (Rs 2,000), FNXP (Rs 230), PRINCPIP (Rs 800) and APOLP (Rs 650) – on high valuations. Our pipe universe trades at 44.4x 1Y fwd P/E vs. the 5Y avg of 34.1x.

Tiles – a play on rising per capita income: We assume coverage on SOMC (TP Rs 900) with a BUY given expectations of a strong 36.6% earnings CAGR over FY23-FY26 as capacity expansion likely propels volumes and margins improve on a better mix. Valuations too look reasonable at 23.5x 1Y fwd P/E – in line with the 5Y mean. For peer KJC (Rs 1,450), we recommend HOLD as valuations appear high.

Bathware – a premiumisation play: We assign a BUY to HINDWARE (TP Rs 700) as it has successfully arrested its market share decline in bathware, diversified into pipes and small kitchen appliances, and offers a robust 56% EPS CAGR over FY23-FY26E along with reasonable valuations at 28.1x 1Y fwd P/E. For CRS (Rs 8,100), we ascribe a HOLD rating as it lacks growth catalysts amid rising competition and looks richly valued.

Wood Panels – MDF to lead growth but faces supply glut: We assume coverage on MTLM (TP Rs 300) with BUY given likely market share gains in plywood from enhanced capacity, entry into MDF and architectural fittings, and strong execution in an oversupplied MDF industry. CPBI (Rs 800), GREENP (Rs 400) and GRLM (Rs 600) are all rated HOLD given a supply overhang in MDF and particleboard coupled with lofty valuations.

Recommendation snapshot

Ticker	Price	Target	Rating
APOLP IN	694	650	HOLD
ASTRA IN	1,794	2,000	HOLD
CPBI IN	778	800	HOLD
CRS IN	8,056	8,100	HOLD
FNXP IN	236	230	HOLD
GREENP IN	410	400	HOLD
GRLM IN	524	600	HOLD
HINDWARE IN	501	700	BUY
KJC IN	1,399	1,450	HOLD
MTLM IN	243	300	BUY
PRINCPIP IN	712	800	HOLD
SI IN	4,163	4,300	HOLD
SOMC IN	705	900	BUY

Price & Target in Rupees | Price as of 16 Jan 2024

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

BUY
TP: Rs 1,896 | ⮝ 23%

HDFC BANK | Banking | 17 January 2024

Margin pressure dampens performance

- **Operationally weak December quarter due to elevated cost of funds and increased provisions**
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Deposit mobilisation sluggish: HDFCB is facing challenges in mobilising low-cost CASA deposits even as term deposit rates continue to rise, which limited its deposit growth to just 1.9% QoQ in Q3FY24. However, the loan book grew at a healthy 4.9% QoQ supported by the retail segments. The retail book increased only 3.3% QoQ and wholesale loans were muted at 1.9%, whereas CRB posted healthy growth of 6.7%. The bank's CD ratio reached an all-time high of 110% while LCR at 110% was at the lower end, which leaves few margin levers.

NIM flat QoQ: Reported NIM was flat sequentially at 3.6% due to a high cost of funds, despite management's stated focus on raising margins post-merger with HDFC. Although HDFCB is hopeful of a rising share of CASA (currently at 37.9% of deposits) and favourable changes in the borrowing mix (e.g. infrastructure bonds), we believe this would be a gradual process. Challenges to margins may compel the bank to focus on high-yielding retail loans (ex-mortgage), which contribute 19% of advances post-merger vs. 27% pre-merger.

Credit cost rises, asset quality stable: Though the C/I ratio declined 13bps QoQ in Q3, the bank's prudent provisioning of Rs 12.2bn towards AIFs increased credit costs for the quarter. Ex-contingent provisions, credit cost was flat QoQ. Cumulative provisioning stood at 159% of GNPA vs. 171% in Q2. Asset quality was stable with GNPA/NNPA of 1.26%/0.31% vs. 1.34%/0.35% in Q2FY24. Further, a tax writeback of Rs 15bn supported PAT growth of 33.5% YoY (+2.5% QoQ).

Maintain BUY: We revise our FY24/FY25 PAT estimates by -6%/+1% to bake in the results, besides introducing FY26 forecasts and rolling valuations forward to Mar'26E. This yields a revised SOTP-based TP of Rs 1,896 (vs. Rs 1929), where we value the core business at 2.4x FY26E ABV (vs. 2.9x FY25E ABV) based on the Gordon Growth Model and include Rs 223/sh for subsidiaries. Although the bank's growth outlook remains healthy, margin improvement would be key to watch.

Key changes

Target	Rating
▼	◄ ►

Ticker/Price	HDFCB IN/Rs 1,538
Market cap	US$ 141.0bn
Free float	100%
3M ADV	US$ 317.3mn
52wk high/low	Rs 1,758/Rs 1,460
Promoter/FPI/DII	0%/52%/31%

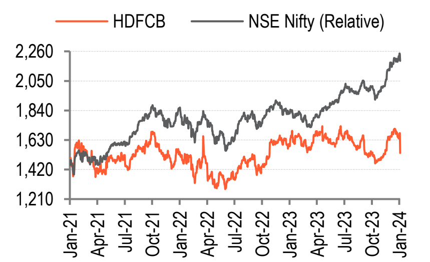
Source: NSE | Price as of 17 Jan 2024

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Net interest income	868,422	1,074,938	1,420,161
NII growth (%)	20.6	23.8	32.1
Adj. net profit (Rs mn)	441,087	557,489	757,275
EPS (Rs)	79.3	84.6	99.7
Consensus EPS (Rs)	79.3	92.0	106.0
P/E (x)	19.4	18.2	15.4
P/BV (x)	3.1	2.8	2.4
ROA (%)	1.9	1.8	2.0
ROE (%)	17.0	15.9	16.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

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