

**BUY**

TP: Rs 1,400 | ▲ 17%

**HDFC BANK**

| Banking

| 17 October 2020

## Resilient quarter; confident commentary

HDFC Bank reported a commendable Q2FY21 with 18% YoY growth in operating profit and PAT. Management is confident of growth opportunities and portfolio quality despite challenges. Headline NPAs declined due to the court's interim stay on loan classification but HDFCB indicated that even using its analytical models to accelerate recognition, GNPA would have been stable at ~1.4%. Demand resolution for the retail moratorium portfolio is expected to reach 97% in Oct'20. We raise FY21-FY23 EPS 2-8% and revise our Sep'21 TP to Rs 1,400 (vs. Rs 1,275).

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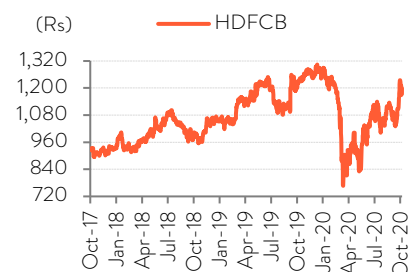
**Asset quality shows buoyant trends:** HDFCB's GNPA ratio declined to ~1.1% (~1.4% in Q1) due to the Supreme Court's interim stay on NPA classification. Per the bank, had it used its analytical models and recognised those accounts on a prudent basis coupled with accelerated recognition, GNPA would have still been flat at ~1.4%. Demand resolution for the retail moratorium portfolio stood at 95% in Sep'20 and is expected to reach 97% in Oct'20 and revert to pre-Covid levels of 99% over the next couple of months. Management did not put a number on the potential restructured book but said they remain conservative.

Ticker/Price	HDFCB IN/Rs 1,199
Market cap	US\$ 89.8bn
Shares o/s	5,490mn
3M ADV	US\$ 190.3mn
52wk high/low	Rs 1,306/Rs 739
Promoter/FPI/DII	26%/37%/37%

Source: NSE

**Wholesale continues to spur loan growth:** Advances increased ~16% YoY led by ~27% growth in the wholesale portfolio. The bank continued to expand this business without diluting its credit standards, as much of the incremental growth was from AA-rated corporates. Retail advances grew at a subdued 5% YoY but early trends are positive with disbursements up 80-85% YoY and 2.5x QoQ. Excess liquidity shaved 15bps off NIM which declined to 4.1% (4.3% in Q1).

## STOCK PERFORMANCE



Source: NSE

**Reiterate BUY:** We increase our FY21-FY23 EPS estimates by 2-8% to adjust for lower operating expense and credit cost assumptions, while now valuing the core book at 3.2x Sep'22E P/BV (vs. 2.8x earlier) – this yields a higher SOTP-based TP of Rs 1,400 (vs. Rs 1,275 earlier).

## KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Net interest income	482,432	561,863	649,511	760,941	900,462
NII growth (%)	20.3	16.5	15.6	17.2	18.3
Adj. net profit (Rs mn)	210,782	262,573	296,368	337,300	401,074
EPS (Rs)	39.6	48.0	54.0	61.5	73.1
P/E (x)	30.3	25.0	22.2	19.5	16.4
P/BV (x)	4.4	3.8	3.4	3.0	2.6
ROA (%)	1.8	1.9	1.8	1.8	1.8
ROE (%)	16.5	16.4	16.3	16.3	17.1

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q2FY21	Q2FY20	Q1FY21	YoY (%)	QoQ (%)	6MFY21	6MFY20	YoY (%)
<b>Income Statement</b>								
Interest income	299,770	281,663	303,780	6.4	(1.3)	603,549	555,579	8.6
Interest expense	142,006	146,512	147,126	(3.1)	(3.5)	289,131	287,486	0.6
<b>Net interest income</b>	<b>157,764</b>	<b>135,150</b>	<b>156,654</b>	<b>16.7</b>	<b>0.7</b>	<b>314,418</b>	<b>268,093</b>	<b>17.3</b>
Non-interest income	60,925	55,887	40,753	9.0	49.5	101,678	105,590	(3.7)
<b>Net total income</b>	<b>218,688</b>	<b>191,038</b>	<b>197,407</b>	<b>14.5</b>	<b>10.8</b>	<b>416,096</b>	<b>373,683</b>	<b>11.4</b>
Staff expenses	25,424	23,551	25,134	8.0	1.2	50,558	45,725	10.6
Other operating expenses	55,127	50,506	43,980	9.1	25.3	99,107	99,505	(0.4)
Operating expenses	80,551	74,057	69,115	8.8	16.5	149,665	145,229	3.1
<b>Pre-provisioning profit</b>	<b>138,138</b>	<b>116,981</b>	<b>128,293</b>	<b>18.1</b>	<b>7.7</b>	<b>266,431</b>	<b>228,453</b>	<b>16.6</b>
Total provisions	37,035	27,007	38,915	37.1	(4.8)	75,950	53,143	42.9
Profit before tax	101,103	89,974	89,378	12.4	13.1	190,480	175,310	8.7
Tax	25,972	26,524	22,791	(2.1)	14.0	48,763	56,178	(13.2)
<b>Profit after tax</b>	<b>75,131</b>	<b>63,450</b>	<b>66,586</b>	<b>18.4</b>	<b>12.8</b>	<b>141,717</b>	<b>119,132</b>	<b>19.0</b>
<b>Balance Sheet</b>								
Advances	10,383,351	8,969,838	10,032,989	15.8	3.5	10,383,351	8,969,838	15.8
Deposits	12,293,104	10,216,149	11,893,873	20.3	3.4	12,293,104	10,216,149	20.3
CASA ratio (%)	41.6	39.3	40.1	233bps	146bps	41.6	39.3	233bps
<b>Yields and margins (%)</b>								
Net interest margin	4.1	4.2	4.3	(10bps)	(20bps)	-	-	-
Yield on advances	9.2	10.4	9.6	(126bps)	(46bps)	-	-	-
Cost of funds	4.3	5.4	4.5	(114bps)	(27bps)	-	-	-
<b>Key ratios (%)</b>								
Cost/Income	36.8	38.8	35.0	(193bps)	182bps	36.0	38.9	(290bps)
Tax rate	25.7	29.5	25.5	(379bps)	19bps	25.6	32.0	(645bps)
Loan to Deposit ratio	84.5	87.8	84.4	(334bps)	11bps	84.5	87.8	(334bps)
<b>Capital adequacy ratios (%)</b>								
Tier 1	17.7	16.2	17.5	150bps	20bps	17.7	16.2	150bps
Total CAR	19.1	17.5	18.9	160bps	20bps	19.1	17.5	160bps
<b>Asset quality (Rs mn)</b>								
Gross NPAs	113,046	125,082	137,735	(9.6)	(17.9)	113,046	125,082	(9.6)
Net NPAs	17,561	37,910	32,800	(53.7)	(46.5)	17,561	37,910	(53.7)
Gross NPA ratio (%)	1.1	1.4	1.4	(30bps)	(28bps)	1.1	1.4	(30bps)
Net NPA ratio (%)	0.2	0.4	0.3	(25bps)	(16bps)	0.2	0.4	(25bps)
Coverage ratio (%)	84.5	69.7	76.2	1,477bps	828bps	84.5	69.7	1,477bps

Source: Company, BOBCAPS Research

## Valuation methodology

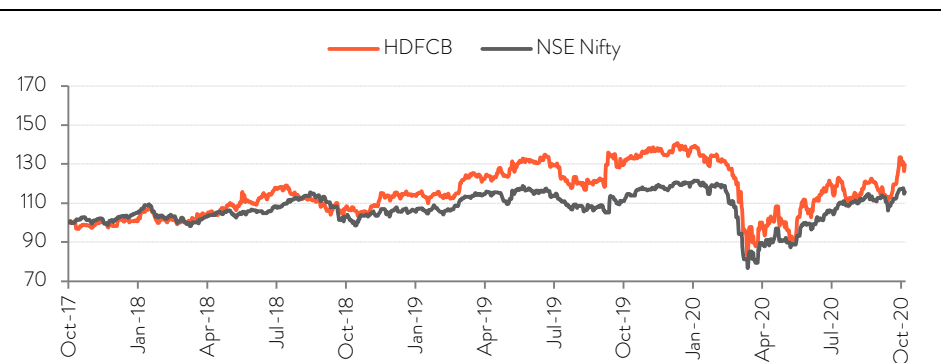
We like HDFCB for its adequate provisioning buffers and strong stress management capability. In our view, the bank deserves to trade at a premium to peers given its superior profitability. We increase our FY21-FY23 EPS estimates by 2-8% to adjust for lower operating expense and credit cost assumptions, while now valuing the core book at 3.2x Sep'22E P/BV (from 2.8x) – this yields a higher SOTP- based target price of Rs 1,400 (from Rs 1,275). Our SOTP model also includes the value of the bank's NBFC and broking businesses. Maintain BUY.

**FIG 2 – REVISED ESTIMATES**

Particulars (Rs mn)	New			Old			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Net interest income	649,511	760,941	900,462	664,364	765,687	886,619	(2.2)	(0.6)	1.6
Pre-provisioning profit	560,896	640,145	754,901	560,488	627,615	727,872	0.1	2.0	3.7
Net Profit	296,368	337,300	401,074	292,091	318,795	370,239	1.5	5.8	8.3
EPS (Rs)	54	62	73	53	58	68	1.5	5.8	8.3

Source: BOBCAPS Research

**FIG 3 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- Prolonged Covid-related disruptions will affect our loan growth and margin assumptions.
- HDFCB's exposure in unsecured retail and SME credit may pose risks to asset quality in a tough macroeconomic environment.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Net interest income</b>	<b>482,432</b>	<b>561,863</b>	<b>649,511</b>	<b>760,941</b>	<b>900,462</b>
NII growth (%)	20.3	16.5	15.6	17.2	18.3
Non-interest income	176,259	232,608	239,787	266,356	305,153
Total income	658,691	794,471	889,299	1,027,297	1,205,615
Operating expenses	(261,194)	(306,975)	(328,403)	(387,152)	(450,714)
Operating profit	397,497	487,495	560,896	640,145	754,901
Operating profit growth (%)	21.8	22.6	15.1	14.1	17.9
Provisions	(75,501)	(121,424)	(162,552)	(186,785)	(215,823)
PBT	321,997	366,072	398,344	453,360	539,078
Tax	(111,215)	(103,498)	(101,976)	(116,060)	(138,004)
<b>Reported net profit</b>	<b>210,782</b>	<b>262,573</b>	<b>296,368</b>	<b>337,300</b>	<b>401,074</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>210,782</b>	<b>262,573</b>	<b>296,368</b>	<b>337,300</b>	<b>401,074</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Equity capital	5,447	5,483	5,483	5,483	5,483
Reserves & surplus	1,486,617	1,704,377	1,931,395	2,189,766	2,496,989
Net worth	1,492,064	1,709,860	1,936,878	2,195,250	2,502,472
Deposits	9,231,409	11,475,023	13,269,732	15,532,653	18,182,576
Borrowings	1,207,248	1,490,664	1,723,989	1,984,276	2,286,382
Other liabilities & provisions	514,686	629,565	680,383	776,168	890,027
<b>Total liabilities and equities</b>	<b>12,445,407</b>	<b>15,305,113</b>	<b>17,610,982</b>	<b>20,488,347</b>	<b>23,861,457</b>
Cash & bank balance	813,476	866,187	890,194	915,632	942,612
Investments	2,905,879	3,918,267	4,422,821	5,068,841	5,814,049
Advances	8,194,012	9,937,029	11,427,583	13,255,996	15,575,796
Fixed & Other assets	532,040	583,630	870,385	1,247,878	1,529,000
<b>Total assets</b>	<b>12,445,407</b>	<b>15,305,113</b>	<b>17,610,982</b>	<b>20,488,347</b>	<b>23,861,457</b>
Deposit growth (%)	17.0	24.3	15.6	17.1	17.1
Advances growth (%)	24.5	21.3	15.0	16.0	17.5

### Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
EPS	39.6	48.0	54.0	61.5	73.1
Dividend per share	7.4	11.9	10.8	12.3	14.6
Book value per share	273.9	311.8	353.2	400.4	456.4

Source: Company, BOBCAPS Research

**Valuations Ratios**

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
P/E	30.3	25.0	22.2	19.5	16.4
P/BV	4.4	3.8	3.4	3.0	2.6
Dividend yield (%)	0.6	1.0	0.9	1.0	1.2

**DuPont Analysis**

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Net interest income	4.2	4.0	3.9	4.0	4.1
Non-interest income	1.5	1.7	1.5	1.4	1.4
Operating expenses	2.3	2.2	2.0	2.0	2.0
Pre-provisioning profit	3.4	3.5	3.4	3.4	3.4
Provisions	0.7	0.9	1.0	1.0	1.0
PBT	2.8	2.6	2.4	2.4	2.4
Tax	1.0	0.7	0.6	0.6	0.6
ROA	1.8	1.9	1.8	1.8	1.8
Leverage (x)	9.0	8.7	9.0	9.2	9.4
ROE	16.5	16.4	16.3	16.3	17.1

**Ratio Analysis**

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
<b>YoY growth (%)</b>					
Net interest income	20.3	16.5	15.6	17.2	18.3
Pre-provisioning profit	21.8	22.6	15.1	14.1	17.9
EPS	16.9	21.2	12.5	13.8	18.9
<b>Profitability &amp; Return ratios (%)</b>					
Net interest margin	4.4	4.2	4.1	4.2	4.3
Fees / Avg. assets	1.2	1.2	1.0	1.0	1.0
Cost-Income	39.7	38.6	36.9	37.7	37.4
ROE	16.5	16.4	16.3	16.3	17.1
ROA	1.8	1.9	1.8	1.8	1.8
<b>Asset quality (%)</b>					
GNPA	1.4	1.3	1.9	1.8	1.8
NNPA	0.4	0.4	0.5	0.5	0.5
Provision coverage	71.4	72.0	72.1	72.4	70.1
<b>Ratios (%)</b>					
Credit-Deposit	88.8	86.6	86.1	85.3	85.7
Investment-Deposit	31.5	34.1	33.3	32.6	32.0
CAR	17.1	18.5	18.4	18.1	17.6
Tier-1	15.8	17.2	17.2	17.0	16.6

Source: Company, BOBCAPS Research

## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

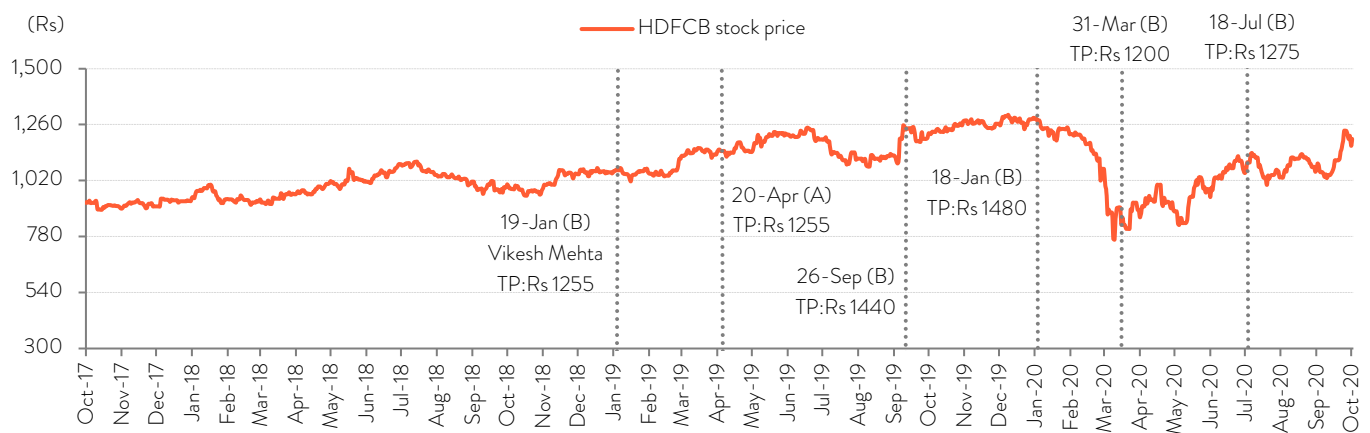
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### RATINGS AND TARGET PRICE (3-YEAR HISTORY): HDFC BANK (HDFCB IN)



B – Buy, A – Add, R – Reduce, S – Sell

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