

**BUY**

TP: Rs 1,200 | ▲ 32%

**HDFC BANK**

| Banking

| 18 April 2020

## Turning to wholesale for growth

**HDFC Bank's (HDFCB) Q4FY20 PAT at Rs 69bn (+18% YoY) was lower estimates as the bank created Rs 15.5bn Covid-related contingent provisions. The lockdown hit loan origination, product distribution and collections. The bank saw a low proportion of moratorium accounts, with ~95% of these not in default. Excluding the impact of forbearance, GNPA/NNPA would have been 10bps/6bps higher. Wholesale loan growth held strong while retail growth could be tepid in the next few quarters. Maintain BUY, Mar'21 TP Rs 1,200.**

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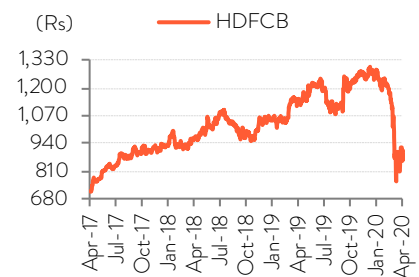
**Covid-related impact manageable in Q4:** Management highlighted that the share of retail customers applying for moratorium was in the low single digits, with 95-98% of these customers not being in default but applying for the reprieve as a conservative measure. GNPA/NNPA/slippage ratios stood at 1.3%/0.4%/1.2% in Q4 and had 10bps/6bps/40bps of forbearance impact.

Ticker/Price	HDFCB IN/Rs 910
Market cap	US\$ 32.5bn
Shares o/s	2,733mn
3M ADV	US\$ 193.2mn
52wk high/low	Rs 1,306/Rs 739
Promoter/FPI/DII	27%/39%/34%

Source: NSE

**Built contingent provisions to strengthen balance sheet:** HDFCB built in Covid-19-related contingent provisions worth Rs 15.5bn in Q4 and believes this is higher than that mandated by RBI. Excess liquidity on the balance sheet had a 10bps negative impact on NIM which stood at 4.3%. Card spends in the second half of Mar'20 were 35% lower than the similar periods in Jan/Feb'20.

## STOCK PERFORMANCE



Source: NSE

**Market share gains continue:** HDFCB's wholesale portfolio grew 29% YoY given demand for working capital, capex and NCLT-related purchases from PSUs, nodal agencies, private corporates and MNC entities operating in the power, power infrastructure, agriculture and allied sectors. The bank's wholesale book is fairly diversified across sectors and geographies with 75-80% of the book rated AA & above. Retail loan growth is expected to be tepid over the next few quarters. About 80% of the unsecured portfolio is to salaried clients, 67% of which are employed with AA- &-above, government or MNC entities.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20A	FY21E	FY22E
Net interest income	400,949	482,432	561,863	685,104	776,833
NII growth (%)	21.0	20.3	16.5	21.9	13.4
Adj. net profit (Rs mn)	174,867	210,782	262,573	300,015	333,709
EPS (Rs)	33.9	39.6	48.0	54.7	60.9
P/E (x)	26.8	23.0	18.9	16.6	15.0
P/BV (x)	4.4	3.3	2.9	2.5	2.2
ROA (%)	1.8	1.8	1.9	1.8	1.7
ROE (%)	17.9	16.5	16.4	16.2	15.8

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q4FY20	Q3FY20	Q4FY19	YoY (%)	QoQ (%)	FY20	FY19	YoY (%)
<b>Income Statement</b>								
<b>Interest income</b>	<b>298,851</b>	<b>293,697</b>	<b>263,333</b>	<b>13.5</b>	<b>1.8</b>	<b>1,148,127</b>	<b>989,721</b>	<b>16.0</b>
Interest expense	146,810	151,968	132,438	10.9	(3.4)	586,264	507,288	15.6
Net interest income	152,041	141,729	130,895	16.2	7.3	561,863	482,432	16.5
Non-interest income	60,326	66,693	48,712	23.8	(9.5)	232,608	176,259	32.0
<b>Net total income</b>	<b>212,366</b>	<b>208,422</b>	<b>179,607</b>	<b>18.2</b>	<b>1.9</b>	<b>794,471</b>	<b>658,691</b>	<b>20.6</b>
Staff expenses	24,983	24,550	20,744	20.4	1.8	95,257	77,618	22.7
Other operating expenses	57,796	54,418	50,427	14.6	6.2	211,719	183,576	15.3
Operating expenses	82,778	78,968	71,171	16.3	4.8	306,975	261,194	17.5
Pre-provisioning profit	129,588	129,454	108,436	19.5	0.1	487,496	397,497	22.6
<b>Total provisions</b>	<b>37,845</b>	<b>30,436</b>	<b>18,892</b>	<b>100.3</b>	<b>24.3</b>	<b>121,424</b>	<b>75,501</b>	<b>60.8</b>
<b>Profit before tax</b>	<b>91,743</b>	<b>99,019</b>	<b>89,544</b>	<b>2.5</b>	<b>(7.3)</b>	<b>366,072</b>	<b>321,996</b>	<b>13.7</b>
Tax	22,466	24,854	30,693	(26.8)	(9.6)	103,498	111,215	(6.9)
<b>Profit after tax</b>	<b>69,277</b>	<b>74,165</b>	<b>58,851</b>	<b>17.7</b>	<b>(6.6)</b>	<b>262,573</b>	<b>210,781</b>	<b>24.6</b>
<b>Balance Sheet</b>								
Advances	9,937,029	9,360,295	8,194,012	21.3	6.2	9,937,029	8,194,012	21.3
Deposits	11,475,023	10,674,335	9,231,409	24.3	7.5	11,475,023	9,231,409	24.3
CASA ratio (%)	42.2	39.5	42.4	(14bps)	272bps	42.2	42.4	(14bps)
<b>Yields and margins (%)</b>								
Net interest margin	4.3	4.2	4.4	(10bps)	10bps	-	-	-
Yield on advances	10.0	10.2	10.5	(54bps)	(26bps)	-	-	-
Cost of funds	4.7	5.3	5.3	(51bps)	(55bps)	-	-	-
<b>Key ratios (%)</b>								
Cost/Income	39.0	37.9	39.6	(65bps)	109bps	38.6	39.7	(101bps)
Tax rate	24.5	25.1	34.3	(979bps)	(61bps)	28.3	34.5	(627bps)
Loan to Deposit ratio	86.6	87.7	88.8	(217bps)	(109bps)	86.6	88.8	(217bps)
<b>Capital adequacy ratios (%)</b>								
Tier 1	17.2	17.1	15.8	140bps	10bps	17.2	15.8	140bps
Total CAR	18.5	18.5	17.1	140bps	0bps	18.5	17.1	140bps
<b>Asset quality (Rs mn)</b>								
Gross NPAs	12,649,970	13,427,250	11,224,160	12.7	(5.8)	12,649,970	11,224,160	12.7
Net NPAs	3,542,360	4,468,350	3,214,520	10.2	(20.7)	3,542,360	3,214,520	10.2
Gross NPA ratio (%)	1.3	1.4	1.4	(10bps)	(16bps)	1.3	1.4	(10bps)
Net NPA ratio (%)	0.4	0.5	0.4	(3bps)	(12bps)	0.4	0.4	(3bps)
Coverage ratio (%)	72.0	66.7	71.4	64bps	528bps	72.0	71.4	64bps

Source: Company, BOBCAPS Research

## Valuation methodology

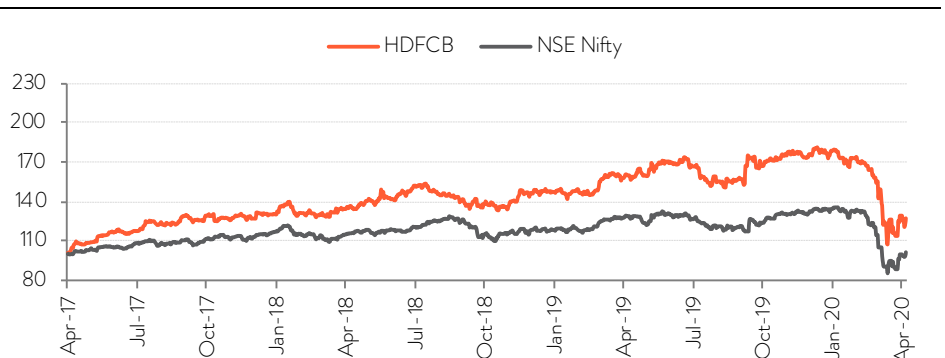
We like HDFCB for its strong processes, risk management practices and stable asset quality – maintain BUY with an unchanged Mar'21 target price of Rs 1,200. Our target price is derived using the SOTP method. The core book has been adjusted for investment in subsidiaries and valued at 2.8x FY22E P/BV – this is based on a two-stage Gordon Growth Model given that we expect the business to continue growing much faster than the industry for the next few years. Our SOTP model also includes the value of the bank's NBFC and broking businesses.

**FIG 2 – SOTP VALUATION**

Sum of Parts	Company Value (Rs bn)	Stake in Company (%)	Value for HDFCB (Rs bn)	Per Share (Rs)	Contribution to TP (%)	Comments
Core Business	6,150	100	6,150	1,122	93	Valued at 2.8x Mar'22 P/BV on Gordon Growth Model
HDB Financial	317	96	350	64	5	Valued at 3x FY22E P/BV
HDFC Securities	65	98	80	15	1	Valued at 12x FY22E P/E
<b>Sum of Parts</b>			<b>6,579</b>	<b>1,200</b>	<b>100</b>	

Source: Company, BOBCAPS Research

**FIG 3 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- Economic slowdown:** In our view, HDFCB's loan portfolio broadly imitates India's GDP mix by catering to the consumption theme. If COVID-19 related lockdown extends for a longer duration, our assumptions for loan growth and asset quality may be impacted.
- Leadership risk:** The bank will witness a change at the helm after three decades, with MD & CEO Aditya Puri retiring in Oct'20. While we continue to believe that HDFCB's process-driven business will hold it in good stead, the stock could be negatively affected should there be a slew of senior management exits during the transition phase.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20A	FY21E	FY22E
<b>Net interest income</b>	<b>400,949</b>	<b>482,432</b>	<b>561,863</b>	<b>685,104</b>	<b>776,833</b>
NII growth (%)	21.0	20.3	16.5	21.9	13.4
Non-interest income	152,203	176,259	232,608	247,635	289,093
Total income	553,152	658,691	794,471	932,739	1,065,926
Operating expenses	(226,904)	(261,194)	(306,975)	(356,259)	(418,265)
Operating profit	326,248	397,497	487,496	576,480	647,661
Operating profit growth (%)	26.8	21.8	22.6	18.3	12.3
Provisions	(59,275)	(75,501)	(121,424)	(173,235)	(199,127)
PBT	266,973	321,997	366,072	403,246	448,534
Tax	(92,106)	(111,215)	(103,498)	(103,231)	(114,825)
<b>Reported net profit</b>	<b>174,867</b>	<b>210,782</b>	<b>262,573</b>	<b>300,015</b>	<b>333,709</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>174,867</b>	<b>210,782</b>	<b>262,573</b>	<b>300,015</b>	<b>333,709</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20A	FY21E	FY22E
Equity capital	5,190	5,447	5,483	5,483	5,483
Reserves & surplus	1,057,760	1,486,617	1,704,377	1,979,001	2,234,623
Net worth	1,062,950	1,492,064	1,709,860	1,984,485	2,240,106
Deposits	7,887,706	9,231,409	11,475,023	13,273,235	15,541,363
Borrowings	1,260,946	1,207,248	1,511,281	1,722,358	1,988,836
Other liabilities & provisions	427,741	514,686	608,948	726,795	870,341
<b>Total liabilities and equities</b>	<b>10,639,343</b>	<b>12,445,407</b>	<b>15,305,113</b>	<b>17,706,873</b>	<b>20,640,646</b>
Cash & bank balance	1,229,151	813,476	866,187	885,071	904,963
Investments	2,422,002	2,905,879	3,918,267	4,426,722	5,081,066
Advances	6,583,331	8,194,012	9,937,029	11,427,583	13,255,996
Fixed & Other assets	404,859	532,040	583,630	967,496	1,398,621
<b>Total assets</b>	<b>10,639,343</b>	<b>12,445,407</b>	<b>15,305,113</b>	<b>17,706,873</b>	<b>20,640,646</b>
Deposit growth (%)	22.5	17.0	24.3	15.7	17.1
Advances growth (%)	18.7	24.5	21.3	15.0	16.0

### Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20A	FY21E	FY22E
EPS	33.9	39.6	48.0	54.7	60.9
Dividend per share	0.0	7.4	0.0	10.9	12.2
Book value per share	204.8	273.9	311.8	361.9	408.5

Source: Company, BOBCAPS Research

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20A	FY21E	FY22E
P/E	26.8	23.0	18.9	16.6	15.0
P/BV	4.4	3.3	2.9	2.5	2.2
Dividend yield (%)	0.0	0.8	0.0	1.2	1.3

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20A	FY21E	FY22E
Net interest income	4.2	4.2	4.0	4.2	4.1
Non-interest income	1.6	1.5	1.7	1.5	1.5
Operating expenses	2.4	2.3	2.2	2.2	2.2
Pre-provisioning profit	3.4	3.4	3.5	3.5	3.4
Provisions	0.6	0.7	0.9	1.0	1.0
PBT	2.8	2.8	2.6	2.4	2.3
Tax	1.0	1.0	0.7	0.6	0.6
ROA	1.8	1.8	1.9	1.8	1.7
Leverage (x)	9.8	9.0	8.7	8.9	9.1
ROE	17.9	16.5	16.4	16.2	15.8

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20A	FY21E	FY22E
<b>YoY growth (%)</b>					
Net interest income	21.0	20.3	16.5	21.9	13.4
Pre-provisioning profit	26.8	21.8	22.6	18.3	12.3
EPS	18.6	16.9	21.2	13.9	11.2
<b>Profitability &amp; Return ratios (%)</b>					
Net interest margin	4.4	4.4	4.2	4.4	4.3
Fees / Avg. assets	1.2	1.2	1.2	1.1	1.1
Cost-Income	41.0	39.7	38.6	38.2	39.2
ROE	17.9	16.5	16.4	16.2	15.8
ROA	1.8	1.8	1.9	1.8	1.7
<b>Asset quality (%)</b>					
GNPA	1.3	1.4	1.3	1.8	1.9
NNPA	0.4	0.4	0.4	0.5	0.5
Provision coverage	69.8	71.4	72.0	72.3	72.9
<b>Ratios (%)</b>					
Credit-Deposit	83.5	88.8	86.6	86.1	85.3
Investment-Deposit	30.7	31.5	34.1	33.4	32.7
CAR	14.8	17.1	19.1	18.7	18.3
Tier-1	13.2	15.8	17.8	17.5	17.2

Source: Company, BOBCAPS Research

## Disclaimer

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

**BUY** – Expected return >+15%

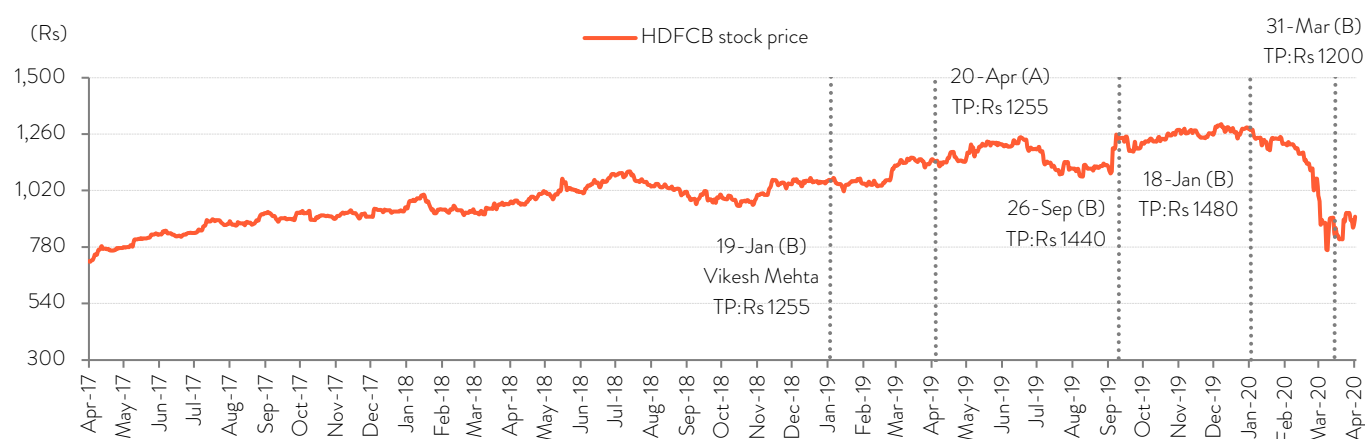
**ADD** – Expected return from >+5% to +15%

**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)

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

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