

HDFC BANK ACCUMULATE

21-Dec-17

INDUSTRY - **BANKING**
BLOOMBERG **HDFCB IN**
BSE Code - **500180**
NSE Code - **HDFCBANK**
NIFTY - **10444**

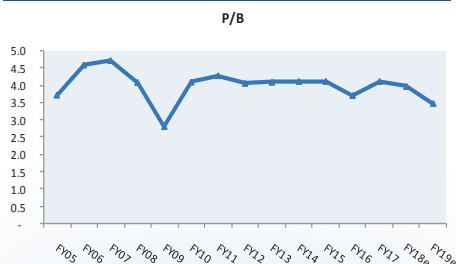
Company Data

CMP	1868
Target Price	2057
Previous Target Price	1989
Upside	10%
Change from Previous	3%
52wk Range H/L	1905/1169
Mkt Capital (Rs Cr)	483463
Av. Volume (.000)	442

Share Holding Pattern %

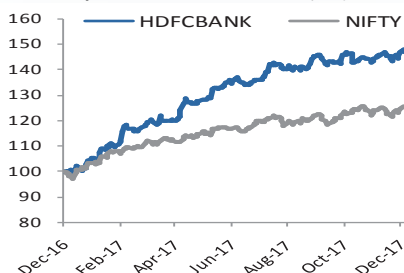
	2QFY18	1QFY18	4QFY17
Promoters	25.7	25.9	26.0
DII	14.1	13.4	12.9
FII	41.5	42.0	42.1
Others	18.7	18.7	18.9

At FY19 B/V, HDFCBANK is trading at par with its historical trend.



Stock Performance %

	1Mn	3Mn	1Yr
Absolute	1.2	1.0	58.3
Rel. to Nifty	0.2	(2.0)	30.0



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Strong Capital Base ensures healthy growth momentum to continue going ahead.

- ✓ In a latest development, HDFC BANK proposes to raise equity capital to the tune of Rs 24000 Cr through various routes. Its promoter HDFC will infuse Rs 8500 Cr via preferential allotment. We expect tier 1 capital to improve to 16% in FY18.
- ✓ This massive capital infusion will support the HDFC Bank to maintain its strong loan book growth momentum going ahead. We expect the bank to register loan book CAGR of 20% over FY17 to FY20.
- ✓ Due to divergence related issue in one account, assets quality may take some blip in 3Q FY18 result. During the 2Q FY18 earning concall management has signaled one standard account to be classified as NPA after regulatory advice. However we don't expect credit cost to shoot up significantly as the management has proactively provided adequate provisions on this account during 2Q FY18.

We increase our target price from Rs 1989 to Rs 2057 at 3.85x BV FY19e and recommend to ACCUMULATE.

Financials/Valuation	FY15	FY16	FY17	FY18E	FY19E
NII	22396	27592	33139	39890	48199
PPP	17404	21364	25732	32071	38541
PAT	10216	12296	14550	17278	22112
NIM %	4.5	4.5	4.4	4.5	4.5
EPS (Rs)	40.8	48.6	56.8	66.9	85.6
EPS growth (%)	15.3	19.3	16.7	17.8	28.0
ROE (%)	19.4	18.3	17.9	17.9	19.7
ROA (%)	2.0	2.0	1.9	1.9	2.0
BV	245	285	347	399	468
P/B (X)	4.2	3.8	4.2	4.7	4.0
✓ P/E (x)	25.1	22.0	25.4	27.9	21.8

Key Highlights of 2Q FY18 Result Update

- ✓ During the quarter management provided Rs 700 Cr of contingent provisions (Rs 300 Cr withdrawn from floating provisions) on one term loan account which is under regulator observance of JLF- flexible restructuring. Management has provided sufficient provisions required related to this account.
- ✓ Advances continues to be robust registering a growth of 22% YoY backed healthy retail advances growth and gain in market share of corporate loans.
- ✓ CASA ratio fell to 43% after it rose to 48% during demonetization period. However this is the normal level of CASA for HDFC Bank.
- ✓ GNPA was flat at 1.26%

Quarterly Performance

Stellar operating profit performance backed by healthy topline and cost control.

Financials	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY %	QoQ %	FY16	FY17	YoY %
Interest Inc.	17,070	17,606	18,114	18,669	19,670	15.2%	5.4%	60,221	69,306	15.1%
Interest Exp.	9,076	9,297	9,059	9,298	9,918	9.3%	6.7%	32,630	36,167	10.8%
NII	7,994	8,309	9,055	9,371	9,752	22.0%	4.1%	27,592	33,139	20.1%
Other Income	2,901	3,143	3,446	3,517	3,606	24.3%	2.5%	10,752	12,296	14.4%
Total Income	10,895	11,452	12,501	12,887	13,358	22.6%	3.7%	38,343	45,436	18.5%
Ope Exp.	4,870	4,843	5,222	5,367	5,540	13.8%	3.2%	16,980	19,703	16.0%
PPP	6,025	6,609	7,279	7,520	7,818	29.8%	4.0%	21,364	25,732	20.4%
Provisions	749	716	1,262	1,559	1,476	97.1%	-5.3%	2,726	3,593	31.8%
PBT	5,276	5,893	6,018	5,961	6,342	20.2%	6.4%	18,638	22,139	18.8%
Tax	1,820	2,028	2,028	2,067	2,191	20.4%	6.0%	6,342	7,589	19.7%
Net Profit	3,455	3,865	3,990	3,894	4,151	20.1%	6.6%	12,296	14,550	18.3%

Healthy Operating Performance.

- ✓ HDFC BANK 2Q FY17 result was in line with our expectation. NII grew with a robust rate of 22% backed by strong loan growth 22% YoY.
- ✓ Other income grew by 24% YoY led by pick up in fee income which grew by 25% YoY.
- ✓ On the back of controlled opex operating profit grew by a robust rate of 30% YoY. However higher provisioning during the quarter led the PAT to grow by 20% YoY.
- ✓ C/I ratio declined by more than 323 bpsYoY to 41.5%. Total operating expenses grew by 14% YoY due to lower employee expenses which grew by 4% YoY. Employee base increased by 2700 sequentially. However intensive digitalization has helped to improve productivity.
- ✓ Provisions increased by 97% YoY/-5% QoQ to Rs 1476 Cr of which Rs 1079 Cr were provided for loan loss provisions. During the quarter management provided Rs 700 Cr of contingent provision for one term loan account under JLF route. Out of this Rs 700 Cr around Rs 300 Cr were utilized from floating provisions.

C/I Ratio declined due to improved productivity.

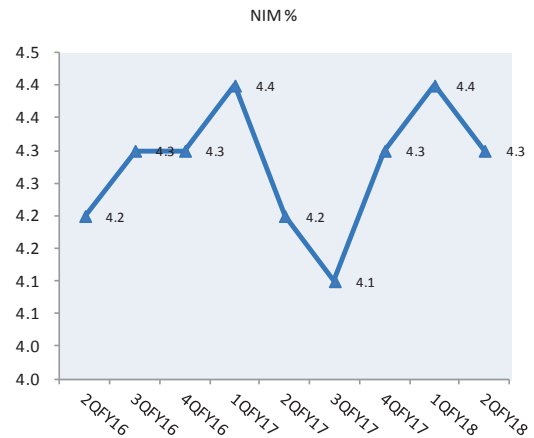
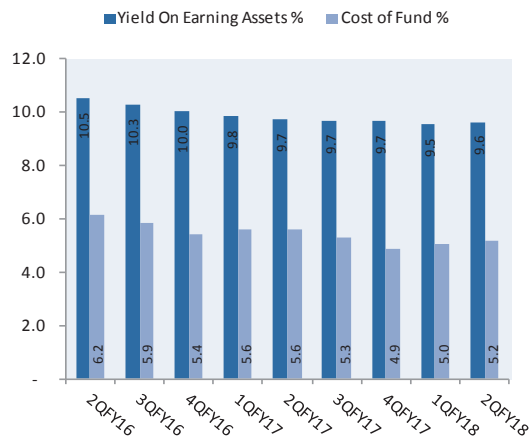
Profitability Metrix	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY(+/-)	QoQ(+/-)	FY16	FY17	YoY %
C/I Ratio %	44.7	42.3	41.8	41.6	41.5	-3.23	-0.18	46.4	45.6	-0.83
Empl. Cost/ Tot. Exp. %	34.0	34.9	29.7	30.9	31.0	-3.06	0.09	33.6	32.9	-0.68
Other Exp/Tot. Exp. %	66.0	65.1	70.3	69.1	69.0	3.06	-0.09	66.4	67.1	0.68
Provision/PPP %	12.4	10.8	17.3	20.7	18.9	6.45	-1.85	12.8	14.0	1.21
Provision/Avg. Advances	0.6	0.6	1.0	1.1	1.0	0.37	-0.10	0.7	0.7	0.05
Tax Rate %	34.5	34.4	33.7	34.7	34.5	0.04	-0.14	34.0	34.3	0.25
Int Exp./Int Inc. (%)	53.2	52.8	50.0	49.8	50.4	-2.75	0.62	54.2	52.2	-2.00
Other Inc./Net Inc. %	26.6	27.4	27.6	27.3	27.0	0.37	-0.29	28.0	27.1	-0.98
PAT/ Net Income %	31.7	33.8	31.9	30.2	31.1	-0.64	0.86	32.1	32.0	-0.05
PAT Growth %	20.4	15.1	18.3	20.2	20.1	-0.28	-0.09	20.4	18.3	-2.04
NII Growth % (YoY)	19.6	17.6	21.5	20.4	22.0	2.35	1.57	23.2	20.1	-3.09
Operating Profit Growth	19.5	15.2	26.9	29.2	29.8	10.30	0.54	22.7	20.4	-2.30
RoE %	17.6	18.7	18.3	17.0	17.5	-0.16	0.50	18.3	17.9	-0.31
RoA %	1.8	1.9	1.9	1.8	1.8	0.02	0.04	2.0	1.9	-0.04

NIM stable, benefitting from declining cost

- ✓ NIM declined sequentially by 10 bps to 4.3%, however it increased by 10 bps YoY.
- ✓ HDFCBANK has been reporting superior net interest income among its peers on the back of healthier CASA level and higher yield assets mix. Superior assets quality has provided cushion to its margins.
- ✓ Going forward we expect margin to sustain at current level due to increase in higher yield assets mix and healthy CASA level despite reduction in yields due to MCLR.

Margin Performance

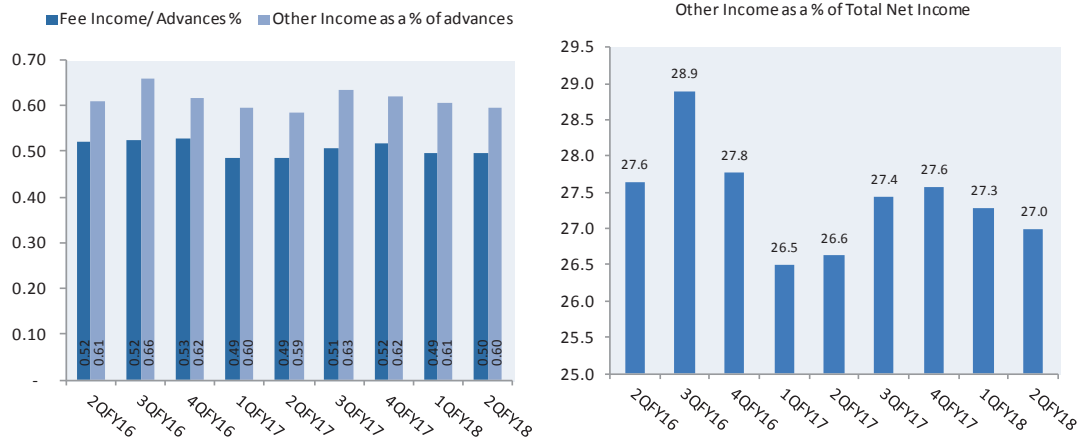
Margin %	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY(+/-)	QoQ(+/-)	FY16	FY17	YoY %
Yield (Total Assets)	9.7	9.7	9.7	9.5	9.6	-0.10	0.10	9.7	9.2	-0.47
Cost Of Funds	5.6	5.3	4.9	5.0	5.2	-0.40	0.17	5.6	5.2	-0.44
NIM	4.2	4.1	4.3	4.4	4.3	0.10	-0.10	4.5	4.4	-0.03



Pick up in fee income.

- ✓ Profit on sale of investments grew by 26% YoY while recovery income also saw robust growth of 15% YoY.
- ✓ Other income grew by 24% YoY on the back of robust fee income growth of 25% YoY.
- ✓ Fee income growth has been strong since last two quarters on the back of increased third party distribution and processing fee from retail loan. Forex income grew by 30% YoY.

Other Income Break Up	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY(+/-)	QoQ(+/-)	FY16	FY17	YoY(+/-)
Fees & Commissions	2,104	2,207	2,523	2,578	2,614	24.2%	1.4%	7,759	8,812	13.6%
FX & Derivatives	295	297	357	297	384	30.2%	29.4%	1,228	1,263	2.9%
Profit / (loss) on	284	399	180	331	356	25.5%	7.4%	732	1,139	55.7%
Miscellaneous Income	219	240	386	310	252	15.3%	-18.8%	1,033	1,082	4.7%
Other Income	2,901	3,143	3,446	3,517	3,606	24.3%	2.5%	10,752	12,297	14.4%



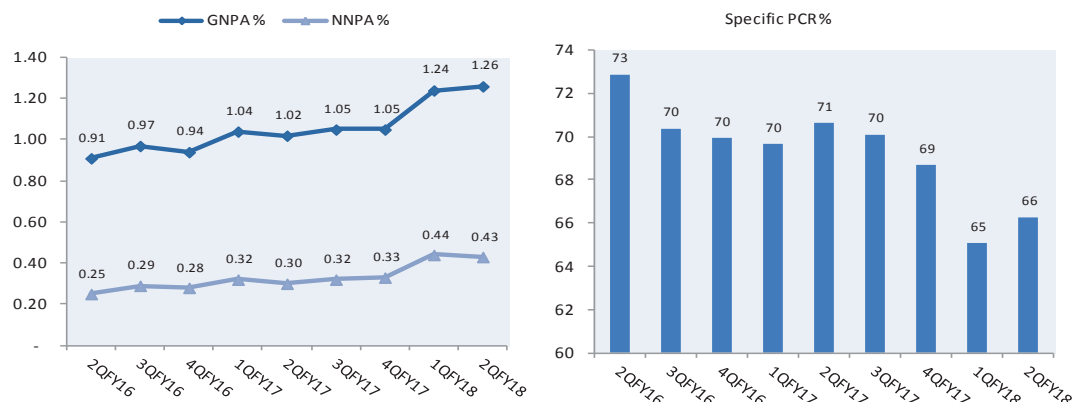
Healthy Balance sheet growth

- ✓ Advances continues to be robust registering a growth of 22% YoY backed healthy retail advances growth and gain in market share of corporate loans.
- ✓ Domestic advances grew by 27% YoY where as overseas portfolio declined by 37% YoY mainly in account of FCNR linked loan repayment. Domestic corporate loan grew by 24% YoY. Management indicated that the demand was generally led by short term loan by mid corporate segment.
- ✓ Domestic retail advances as per regulatory classification grew by 29% YoY and retail mix increased to 55% against 54% a year back.
- ✓ Under the retail loan segment, vehicle loan grew by 22% YoY, housing loan grew by 19% YoY and unsecured loan grew by 39% YoY.
- ✓ Under the vehicle loan auto, CV and two wheelers grew by 22%, 22% and 18% YoY respectively.
- ✓ Business banking grew by a robust rate of 44% YoY. Unsecured loan retail loan (PL+ Card) increased to 15.1% from 13.4% a year ago.
- ✓ As per the regulatory norm retail and wholesale mix stands at 55:45 of domestic advances.
- ✓ Total business of HDFCBANK grew by a healthy rate of 19% YoY to reach the mark of Rs 12.9 Lakh Deposits grew by 16% YoY led by strong growth in CASA which grew by 24% YoY. Both saving as well as current deposit grew by 24% YoY however current account saw decline of 4% on sequential CASA ratio fell to 43% after it rose to 48% during demonetization period. However this is the normal level of CASA for HDFC Bank and we expect it to sustain at this level.

Assets Quality remained flat, provisioning increased due to one-off.

- ✓ After the blip in 1Q FY18 due to loan waiver sentiment and demonetization, assets quality was flat sequentially. Slippages were Rs 2470 Cr against Rs 3100 in 1Q FY18.
- ✓ GNPA was flat at 1.26% and NNPA 0.43%.
- ✓ During the quarter management provided Rs 700 Cr of contingent provisions (Rs 300 Cr withdrawn from floating provisions) on one term loan account which is under regulator observance of JLF- flexible restructuring. Management has provided sufficient provisions required related to this account.
- ✓ Provision coverage remained healthy at 66% against 65% sequentially.
- ✓ Going forward in short term there may be some blip in assets quality due to GST implementation and loan waiver sentiments; however in long run we expect assets quality to remain intact. Assets quality of HDFC Bank remains one of the best in the industry.

	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY(+/-)	QoQ(+/-)	FY16	FY17	YoY %
GNPA (Rs)	5,069	5,232	5,886	7,243	7,703	52.0%	6.3%	4,393	5,886	34.0%
GNPA %	1.0	1.1	1.1	1.2	1.3	0.24	0.02	0.9	1.1	0.11
NNPA (Rs)	1,489	1,564	1,844	2,528	2,597	74.4%	2.7%	1,320	1,844	39.7%
NNPA %	0.3	0.3	0.3	0.4	0.4	0.13	-0.01	0.3	0.3	0.05
Slippages (Rs)	1,440	1,700	2,100	3,100	2,473	71.7%	-20.2%	5,941	7,001	17.8%
Specific PCR %	70.6	70.1	68.7	65.1	66.3	-4.34	1.19	70.6	66.3	-4.34



Concall Highlights

- ✓ During the quarter HDFC Bank was announced as Domestically Systematically Important Bank and hence required to maintain 15 bps and 20 bps more capital above regulatory requirement on April 2018 and April 2019 respectively.
 - ✓ Bank has been catering to Government saving deposits and has been under focus.
 - ✓ Management has provided Rs 700 Cr of provisions on one term loan project on account of regulatory observances for JLF flexible restructuring. Out of Rs 700 Cr, management provided Rs 300 Cr from floating provision.
 - ✓ Stock of floating provision now stands at Rs 1000 Cr.
 - ✓ Endeavour is to outpace expenses growth by revenue growth so that cost to income ratio tend to
 - ✓ 2700 employee were added sequentially.
- There is intense competition on mid-corporate and emerging corporate loan account.
Overseas loan is at Rs 21000 Cr.

View and Valuation

We continue to like HDFC Bank given its strong fundamentals, steady loan growth, adequate capital, best in assets quality, strong branch network and intensive digitalization initiatives. With all levers set, HDFCBANK is poised for strong business growth from the expected upturn in economy. Continuation of strong loan growth has resulted in gain of market share from its peers.

Historically HDFC Bank has grown in line with the Indian Economy growth. Now with the expectation of improved economy growth, gaining market share from its peers and increase in demand of working capital loan, we expect HDFC Bank loan book to register 20% CAGR over FY17 to FY20. Recent proposal to raise Rs 24000 Cr will boost the Tier I ratio significantly. This capital raise will ensure the momentum of strong loan growth to continue going ahead. Assets quality remains best in the industry but recently it got impacted by demonetization and loan waiver sentiment. There might be some divergence related account which will have impact in near term. Although it is temporary issue but we remain cautious and expect credit cost to remain at higher levels in FY18.

Due to intensive investment in digitalization and slow down in branch expansion, operating expense has shown a modest growth in last three quarters which we expect to continue further due to improved productivity.

Recent hardening of bond yield has resisted the scope of NIM improvement. However healthy CASA ratio in the range of 43%, higher yield assets mix and massive capital infusion will provide cushion to NIM in near term.

Post capital dilution, we expect HDFC Bank to report RoE/RoA in the range of 16.5% and 2.1% in FY19. On the back of increased book value, we increase our target price from Rs 1989 to Rs 2057 at 3.85x BV FY19e and recommend to **ACCUMULATE**.

Performance Story in Charts and Graphs

Advances Performance

	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18
Net Advances (Rs in Cr)	4,18,541	4,36,364	4,64,594	4,70,622	4,94,418	4,95,043	5,54,568	5,80,976	6,04,867
Adv. Growth YoY %	27.9	25.7	27.1	23.2	18.1	13.4	19.4	23.4	22.3
>> Growth QoQ %	9.6	4.3	6.5	1.3	5.1	0.1	12.0	4.8	4.1

Advances Breakup %(as per regulatory)

Retail Advances	48.8	49.2	48.2	49.5	51.1	52.7	51.2	52.1	53.6
Corporate Dom. Adv.	43.7	43.9	45.8	43.9	42.2	43.7	46.0	44.4	43.9
Overseas Loan	7.5	6.9	6.0	6.6	6.7	3.6	2.9	3.5	2.5

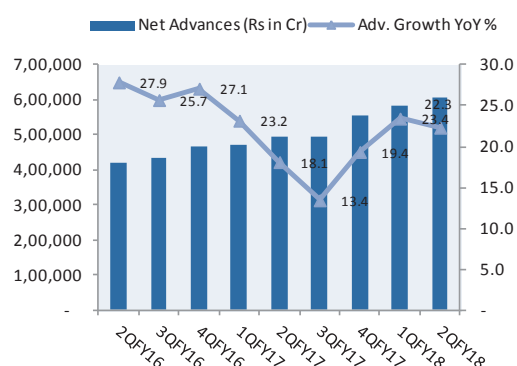
Break-up of Domestic Retail Advances % (As per regulatory segment reporting)

Auto	22.5	23.2	22.4	22.4	22.4	22.4	21.9	21.8	21.3
Personal Loans	15.6	16.3	16.6	17.4	17.7	17.8	17.6	18.3	18.7
Home Loans	13.9	13.2	14.2	14.4	13.3	13.6	13.5	12.8	12.3
Business Banking	13.3	12.5	11.3	11.0	12.5	12.3	12.8	13.4	14.0
Kisan Gold Card	9.4	9.2	10.0	9.4	9.7	9.0	9.2	9.1	9.6
Credit Cards	8.8	9.2	9.2	9.1	8.5	9.1	9.2	9.6	9.5
CV/CE	7.2	7.0	6.6	6.6	6.6	6.7	6.8	6.5	6.2
Others	4.2	4.5	4.8	4.8	4.6	4.5	4.6	4.2	4.1
Two Wheelers	2.3	2.4	2.4	2.4	2.3	2.3	2.2	2.2	2.1
Gold Loans	2.1	2.0	2.0	2.1	2.0	1.8	1.7	1.6	1.6
Loans against securities	0.5	0.5	0.6	0.5	0.5	0.5	0.5	0.5	0.5

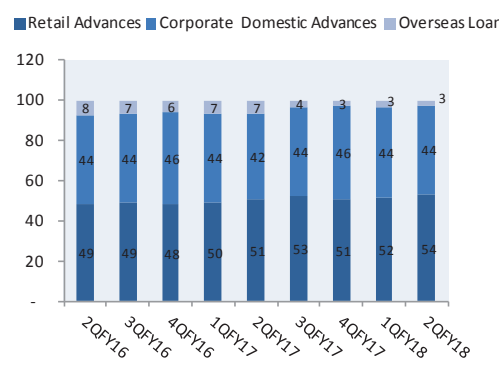
Deposits Performance

	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18
Deposits (Rs in Cr)	5,06,909	5,23,997	5,46,424	5,73,755	5,91,731	6,34,705	6,43,640	6,71,376	6,89,346
Growth YoY %	29.7	26.5	21.2	18.5	16.7	21.1	17.8	17.0	16.5
>> Growth QoQ %	4.7	3.4	4.3	5.0	3.1	7.3	1.4	4.3	2.7
CA % (of Deposits)	14	14	16	13	13	16	18	15	14
SA % (of Deposits)	25.9	25.8	27.1	26.6	27.0	29.4	30.1	28.8	28.7
CASA %	39.7	40.0	43.2	39.9	40.4	45.4	48.0	44.0	42.9
CASA Growth YoY %	19.4	23.7	19.1	19.2	18.8	37.4	30.8	29.0	6.1
>> Growth QoQ %	4.9	4.0	12.8	(3.2)	4.5	20.4	7.4	(4.5)	(2.5)
Credit Deposit Ratio	82.6	83.3	85.0	82.0	83.6	78.0	86.2	83.5	87.7

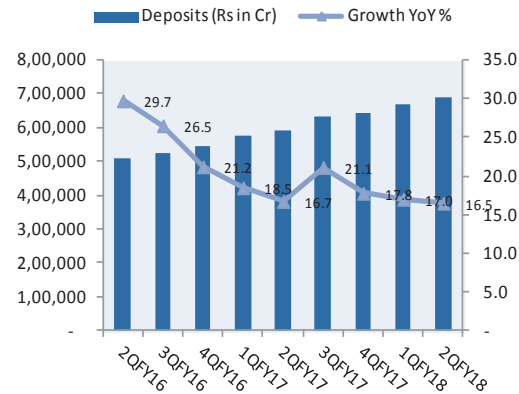
Advances Growth remained healthy



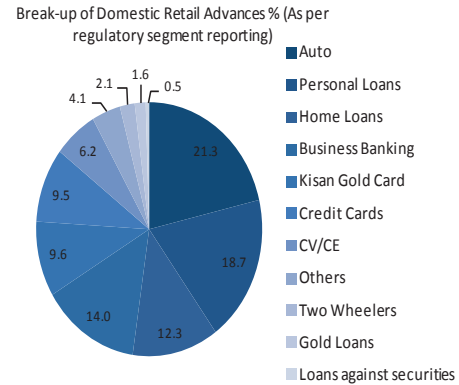
Loan Mix remained Stable



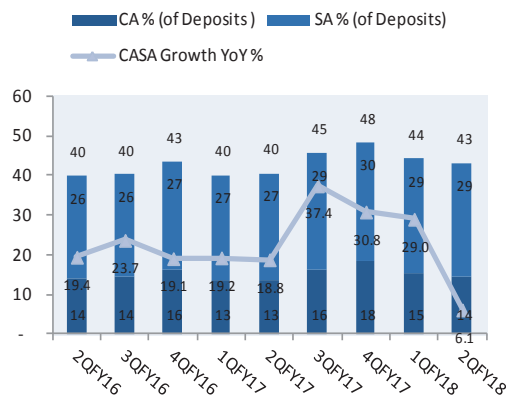
Deposit growth trend



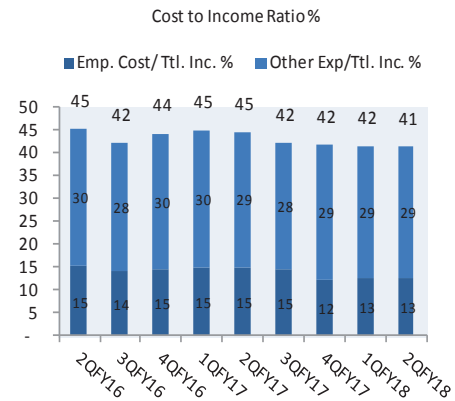
Diversified Retail Assets



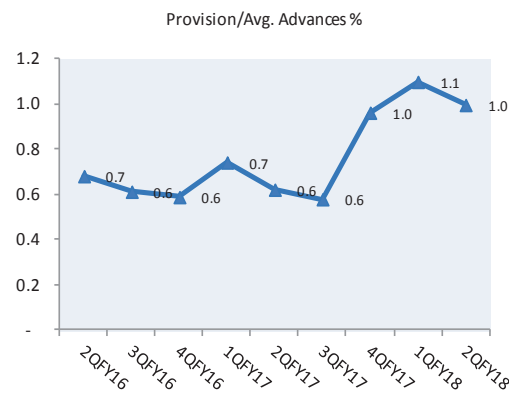
CASA spiked led by demonetization



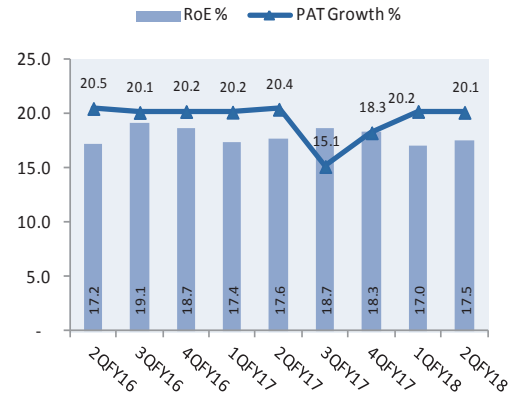
Stringent control on C/I ratio



PL Provisioning Trend



Healthy RoE and PAT growth



Financials Snap Shot

Balance Sheet

Rs in Crores

Y/E March	FY17	FY18E	FY19E	FY20E
Share Capital	513	542	542	542
>> <i>Equity Capital</i>	513	542	542	542
>> <i>Preference Capital</i>	-	-	-	-
Reserves & Surplus	88,950	1,26,519	1,44,313	1,66,410
Networth	89,462	1,27,061	1,44,856	1,66,952
Deposits	6,43,640	7,47,247	8,96,696	10,64,697
Change (%)	17.8	16.1	20.0	18.7
>> <i>CASA Deposits</i>	3,09,153	3,21,316	3,90,063	4,68,467
Change (%)	30.8	3.9	21.4	20.1
Borrowings	74,029	1,00,938	1,09,935	1,30,745
Other Liabilities & Provision:	56,709	56,791	63,296	76,658
Total Liabilities	8,63,840	10,32,037	12,14,783	14,39,052
Cash & Bank	48,952	61,035	59,251	71,142
Investments	2,14,463	2,46,591	2,94,116	3,49,221
Change (%)	9.5	15.0	19.3	18.7
Advances	5,54,568	6,71,028	8,05,233	9,58,227
Change (%)	19.4	21.0	20.0	19.0
Fixed Assets	3,627	3,881	4,152	4,443
Other Assets	42,230	49,502	52,030	56,019
Total Assets	8,63,840	10,32,037	12,14,783	14,39,052

Income Statement

Rs in Crores

Y/E March	FY17	FY18E	FY19E	FY20E
Interest income	69,306	79,976	94,834	1,12,563
Interest expended	36,167	39,581	46,023	55,033
Net Interest Income	33,139	40,395	48,811	57,530
Change (%)	20.1	21.9	20.8	17.9
Other Income	12,296	14,863	17,235	20,464
Change (%)	14.3676547	20.9	16.0	18.7
>> <i>Core Fee Income</i>	10,075	12,364	14,343	17,069
>> <i>Treasury Income</i>	1,139	1,384	1,551	1,842
>> <i>Others</i>	1,082	1,114	1,341	1,553
Total Net Income	45,436	55,258	66,046	77,994
Operating Expenses	19,703	22,848	27,144	31,725
Change (%)	16.0	16.0	18.8	16.9
>> <i>Employee Expenses</i>	6,484	7,045	8,333	9,803
Pre-provisioning Profit	25,732	32,410	38,902	46,269
Change (%)	20.4500198	25.9	20.0	18.9
Provisions	3,593	5,928	4,880	4,954
Change (%)	31.8	65.0	(17.7)	1.5
PBT	22,139	26,482	34,023	41,315
Tax	7,589	9,084	11,672	14,175
Profit After Tax	14,550	17,398	22,350	27,140
Change (%)	18.3	19.6	28.5	21.4

Key Ratios & Assumptions

Y/E March	FY17	FY18E	FY19E	FY20E
Balance Sheet Metrics				
Loan Growth (%)	19.4	21.0	20.0	19.0
Deposit Growth (%)	17.8	16.1	20.0	18.7
C/D Ratio (%)	86.2	89.8	89.8	90.0
CASA (%)	48.0	43.0	43.5	44.0
Investment/Deposit (%)	33.3	33.0	32.8	32.8
CRAR (%)	14.6	18.1	17.5	17.1
>> <i>Tier 1 (%)</i>	12.8	16.1	15.6	15.3
>> <i>Tier 2 (%)</i>	1.8	2.0	1.8	1.8

Assets Quality Metrics

Gross NPA	5,886	11,170	12,688	14,446
Gross NAP (%)	1.05	1.65	1.56	1.50
Net NPA	1,844	3,574	3,806	4,334
Net NPA (%)	0.33	0.53	0.47	0.45
Slippages (%)	1.51	2.65	1.52	1.47
Provision Coverage (%)	68.7	68.0	70.0	70.0
Provision/Average Advance	0.71	0.97	0.66	0.56

Margin Metrics

Yield On Advances (%)	10.2	10.1	10.0	9.9
Yield On Investment (%)	7.8	7.2	7.4	7.4
Yield on Earning Assets (%)	9.2	9.0	9.0	9.0
Cost Of Deposits (%)	5.3	4.9	4.8	4.8
Cost Of Funds (%)	5.2	4.9	4.8	4.8
Spread (%)	4.1	4.2	4.2	4.1
NIM (%)	4.4	4.6	4.6	4.6

Profitability & Efficiency Metrics

Int. Expense/Int. Income (%)	52.2	49.5	48.5	48.9
Fee Income/NII (%)	30.4	30.6	29.4	29.7
Cost to Income (%)	45.6	43.3	43.0	42.5
Cost on Average Assets (%)	2.6	2.6	2.6	2.5
Tax Rate (%)	34.3	34.3	34.3	34.3

Valuation Ratio Metrics

EPS (Rs)	56.8	64.2	82.4	100.1
Change (%)	16.7	13.0	28.5	21.4
ROAE (%)	17.9	16.1	16.4	17.4
ROAA (%)	1.9	2.0	2.1	2.2
Dividend Payout (%)	19.4	19.5	17.0	15.5
Dividend yield (%)	0.8	0.7	0.7	0.8
Book Value (Rs)	349	469	534	616
Change (%)	21.4	34.2	14.0	15.3
P/B (X)	4.13	3.99	3.50	3.03
P/E (X)	25.40	29.12	22.66	18.66