RETAIL EQUITY RESEARCH

HDFC Bank

Banking

BSE CODE: 500180 **NSE CODE:** HDFCBANK
Bloomberg CODE: HDFCB:IN **SENSEX:** 30,126

BUY

Rating as per Largecap 12months investment period

CMP Rs1535 **TARGET** Rs1681 **RETURN 10%**

04th May, 2017

Stellar Performance continues…

HDFC Bank is the second largest private sector bank in India. The Bank has a nationwide distribution network of 4,715 branches and 12,260 ATM's in 2,657 cities/towns.

- **Net interest income (NII)/net profit increased by 22%/19% YoY (in line with our expectation) on the back of strong loan growth and higher NIM.**
- **Advances grew at a healthy pace of 19.4% YoY led by strong growth in domestic advances (↑23.7% YoY).**
- **Asset quality remained broadly stable with Gross non-performing assets (GNPA) ratio at 1.1% and Net NPA (NNPA) ratio at 0.3%.**
- **We expect NII and net profit to increase at a healthy CAGR of 19% and 21%, respectively over FY17-19E supported by 20% CAGR in advances.**
- **HDFC Bank is best placed among peers given its higher than system credit growth coupled with superior return ratios and stable asset quality. We maintain BUY rating on the stock with a TP of Rs1,681 (3.8x FY19E P/ABV).**

Business growth intact

Advances continued to increase at a strong pace of 19.4% YoY led by strong growth in domestic loan book (↑23.7% YoY). The domestic retail and wholesale loans grew by 26.6% YoY and 20.7% YoY, respectively (domestic loan mix between Retail and Wholesale stood at 53:47). The strong growth in both the segments was driven by a sustained geographical expansion, a differentiated product range, digital initiatives and improved turnaround times. On liabilities side, CASA ratio improved to 48% (↑479 bps YoY) supported by 31% YoY growth in CASA deposits. Going forward, we expect the bank to continue to outpace the industry growth rate (8-9%) and factor 20%/15% CAGR in advances/deposits over FY17-19E supported by the bank's robust retail franchise.

Strong operating performance

HDFC Bank's net interest income (NII) increased at a robust pace of 22% YoY (in line with our expectation) on the back of strong loan growth and expansion in NIM by 5 bps YoY to 4.8%. Increase in NIM was driven by higher credit/deposit (c/d) ratio coupled with higher share of CASA deposits. Although reported provisions increased by 91% YoY, it would have increased by just 31% YoY if we adjust it with the benefit of floating provision availed (~Rs300cr) in Q4FY16 by the bank. Hence, net profit increased at a slower pace of 18% YoY. We expect NII and net profit to grow at a healthy CAGR of 19% and 21%, respectively over FY17-19E supported by stable NIM of 4.6% and moderate credit cost of 0.6%.

Best in class asset quality

Asset quality continued to remain stable as Gross and Net non-performing asset (NPA) ratios stood at 1.1% (no change QoQ) and 0.3% (↑1 bp QoQ), respectively. Notably, there was no asset quality related discrepancy reported by the RBI for FY16 under IRACP (Income Recognition, Asset Classification and Provisioning) norms. Overall, the bank has maintained robust asset quality over the last ten years. Further, negligible pool under stressed assets coupled with Rs1,250cr of floating provisions lend more comfort. Hence, we don't expect any negative surprises on asset quality front over near to medium term.

Outlook & Valuation

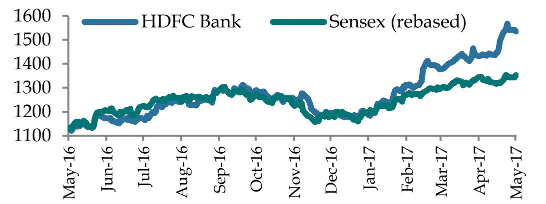
Given the bank's higher credit growth (20% CAGR over FY17-19E), best in-class asset quality (Gross NPA of 1.1% by FY19E) and superior return ratios (RoE of 19.5% and RoA of 2.1%), we expect the bank to continue to command premium valuation over its peers. Further, the bank is well-capitalised with a capital adequacy of 14.6% as of FY17 (tier 1 capital of 12.8%). Hence, we maintain a BUY rating on the stock with revised target price of Rs1,681 (3.8x FY19E P/ABV).

Company Data	
Market Cap (cr)	Rs393,701
Outstanding Shares (cr)	254.6
Free Float	75%
Dividend Yield	0.6
52 week high	Rs1,572
52 week low	Rs1,110
6m average volume (cr)	0.27
Beta	0.5
Face value	Rs2

Shareholding %	Q2FY17	Q3FY17	Q4FY17
Promoters	26.2	26.1	26.0
FII's	39.4	39.2	42.1
MFs/Insti	14.3	15.0	12.9
Public	20.1	19.7	18.9
Others	-	-	-
Total	100.0	100.0	100.0

Price Performance	3mth	6mth	1 Year
Absolute Return	17.1%	23.4%	36.1%
Absolute Sensex	-3.3%	-0.1%	8.6%
Relative Return*	20.3%	23.5%	27.6%

***over or under performance to benchmark index**



Standalone (Rs.cr)	FY17	FY18E	FY19E
Net Interest Income	33,139	39,866	47,082
Growth (%)	*20%*	*20%*	*18%*
NIM (%)	4.7	4.6	4.6
Pre Pro Profit	25,732	31,152	36,869
Growth (%)	*20%*	*21%*	*18%*
Net Profit	14,550	17,748	21,092
Growth (%)	*18%*	*22%*	*19%*
EPS	56.8	69.3	82.3
Growth (%)	*17%*	*22%*	*19%*
P/E	27.0	22.2	18.6
P/BV	4.4	4.0	3.4
P/ABV	4.5	4.1	3.5
RoE (%)	17.9	18.7	19.5
RoA (%)	1.9	2.0	2.1

Quarterly Financials (Standalone)

Profit & Loss Account

(Rs cr)	Q4FY17	Q4FY16	YoY Growth %	Q3FY17	QoQ Growth %
Interest Income	18,114	15,997	13.2	17,606	2.9
Interest on advances	13,507	11,949	13.0	13,176	2.5
Income on Investments	4,268	3,790	12.6	4,049	5.4
Others	339	258	31.4	381	(10.9)
Interest Expense	9,059	8,543	6.0	9,297	(2.6)
Net Interest Income	**9,055**	**7,453**	**21.5**	**8,309**	**9.0**
Non-Interest Income	3,446	2,866	20.3	3,143	9.7
Total Net Income	**12,501**	**10,319**	**21.1**	**11,452**	**9.2**
Operating Expenses	5,222	4,584	13.9	4,843	7.8
Employee Cost	1,553	1,498	3.7	1,689	(8.1)
Other Operating Exp.	3,669	3,086	18.9	3,154	16.3
Total Income	**21,561**	**18,863**	**14.3**	**20,748**	**3.9**
Total Expenditure	**14,281**	**13,128**	**8.8**	**14,139**	**1.0**
Pre-Provisioning profit	**7,279**	**5,735**	**26.9**	**6,609**	**10.1**
Provisions	1,262	662	90.5	716	76.3
Profit Before Tax	**6,018**	**5,072**	**18.6**	**5,893**	**2.1**
Tax	2,028	1,698	19.4	2,028	(0.0)
Net Profit	**3,990**	**3,374**	**18.3**	**3,865**	**3.2**
EPS - Diluted (Rs)	15.6	13.3	16.7	15.1	2.9

Business Performance (Rs cr)	Q4FY17	Q4FY16	YoY Growth %	Q3FY17	QoQ Growth %
Advances	554,568	464,594	19.4	495,043	12.0
Deposits	643,640	546,424	17.8	634,705	1.4
Business	1,198,208	1,011,018	18.5	1,129,748	6.1
Gross NPA	5,886	4,393	34.0	5,232	12.5
Net NPA	1,844	1,320	39.7	1,564	17.9

Key Ratios (%)	Q4FY17	Q4FY16	YoY bps	Q3FY17	QoQ bps
Net Interest Margin	4.8	4.8	5	4.6	19
Cost of Funds	5.1	5.8	(69)	5.4	(32)
Yield on Advances	10.3	10.6	(31)	10.7	(36)
Yield on Investments	7.6	8.8	(118)	7.3	26
Yield on Funds	9.7	10.3	(60)	9.8	(17)
Cost to Income	41.8	44.4	(265)	42.3	(52)
Credit to Deposit	86.2	85.0	114	78.0	817
CASA	48.0	43.2	479	45.4	268
Capital Adequacy	14.6	15.5	(90)	15.9	(130)
Tier I Capital	12.8	13.2	(40)	13.8	(100)
Gross NPA	1.1	0.9	11	1.1	0
Net NPA	0.3	0.3	5	0.3	1
Provision Coverage	68.6	70.2	(164)	69.5	(95)
Credit Cost	0.9	0.6	34	0.6	33
RoE (Ann.)	18.3	18.7	(36)	18.7	(38)
RoA (Ann.)	1.9	1.9	(5)	1.9	(3)

Change in estimates

	Old estimates		New estimates		*Change %*	
Year / Rs cr	**FY18E**	**FY19E**	**FY18E**	**FY19E**	**FY18E**	**FY19E**
Net Interest Income	38,838	45,566	39,866	47,082	*2.6*	*3.3*
Pre-Provisioning Profit	30,025	35,608	31,152	36,869	*3.8*	*3.5*
Net Profit	17,341	20,529	17,748	21,092	*2.3*	*2.7*
EPS (Rs)	67.9	80.3	69.3	82.3	*2.0*	*2.5*

Source: Company, Geojit Research

Standalone Financials

Profit & Loss Account

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Interest Income	48,470	60,221	69,306	81,833	95,152
Interest Expense	26,074	32,630	36,167	41,967	48,070
Net Interest Income	**22,396**	**27,592**	**33,139**	**39,866**	**47,082**
% Change	*21.2*	*23.2*	*20.1*	*20.3*	*18.1*
Non-Interest Income	8,996	10,752	12,296	14,013	15,714
Net Income	**31,392**	**38,343**	**45,436**	**53,880**	**62,796**
Operating Expenses	13,988	16,980	19,703	22,728	25,928
Total Income	**57,466**	**70,973**	**81,602**	**95,846**	**110,867**
Total Expenditure	**40,062**	**49,610**	**55,870**	**64,694**	**73,998**
Pre-Provisioning Profit	**17,404**	**21,364**	**25,732**	**31,152**	**36,869**
% Change	*21.2*	*22.7*	*20.4*	*21.1*	*18.4*
Provisions	2,076	2,726	3,593	4,146	4,775
Profit Before Tax	**15,329**	**18,638**	**22,139**	**27,006**	**32,093**
Tax	5,113	6,342	7,589	9,258	11,002
Tax Rate (%)	*33*	*34*	*34*	*34*	*34*
Net Profit	**10,216**	**12,296**	**14,550**	**17,748**	**21,092**
% Change	*20.5*	*20.4*	*18.3*	*22.0*	*18.8*
No. of Shares (cr)	251	253	256	256	256
EPS (Rs)	40.8	48.6	56.8	69.3	82.3
% Change	*15.3*	*19.3*	*16.7*	*22.0*	*18.8*

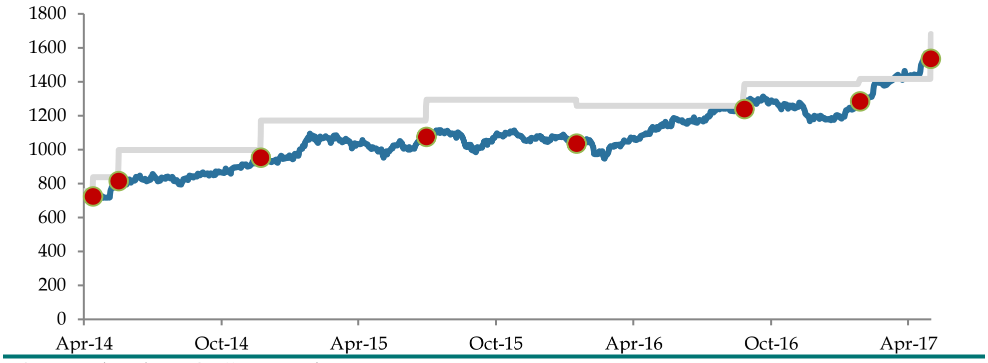
Balance Sheet

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Liabilities					
Capital	501	506	513	513	513
Reserves & Surplus	61,508	72,172	88,950	97,424	115,287
Deposits	450,796	546,424	643,640	740,186	851,213
Borrowings	45,214	53,018	74,029	98,817	126,566
Other Liabilities & Provisions	32,557	36,725	56,709	49,555	57,987
Total Liabilities	**590,576**	**708,846**	**863,840**	**986,494**	**1,151,566**
Assets					
Cash & Balances	36,331	38,919	48,952	59,215	62,990
Investments	166,460	163,886	214,463	222,056	255,364
Advances	365,495	464,594	554,568	665,482	798,578
Fixed Assets	3,122	3,343	3,627	3,934	3,934
Other Assets	19,168	38,104	42,230	35,807	30,699
Total Assets	**590,576**	**708,846**	**863,840**	**986,494**	**1,151,566**

Ratios

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
EPS	40.8	48.6	56.8	69.3	82.3
DPS	8.0	9.5	9.5	10.0	10.5
BV	247.4	287.5	349.1	382.2	451.9
ABV	243.8	282.2	341.9	373.6	440.7
Valuation (%)					
P/E	37.7	31.6	27.0	22.2	18.6
P/BV	6.2	5.3	4.4	4.0	3.4
P/ABV	6.3	5.4	4.5	4.1	3.5
Div. Yield	0.5	0.6	0.6	0.7	0.7
Spreads (%)					
Yield on Advances	11.1	10.8	10.2	10.1	10.1
Yield on Investments	7.2	8.5	8.4	8.3	8.3
Yield on Funds	10.1	10.4	9.9	9.9	9.8
Cost of Funds	5.8	6.0	5.5	5.4	5.3
Capital (%)					
CAR	16.8	15.5	14.6	15.1	15.1
Tier I	13.7	13.2	12.8	13.4	13.6
Tier II	3.1	2.3	1.8	1.7	1.5
Asset (%)					
GNPA	0.9	0.9	1.1	1.0	1.1
NNPA	0.2	0.3	0.3	0.3	0.4
PCR	72.8	69.9	68.7	65.5	67.2
Management (%)					
Credit/ Deposit	81.1	85.0	86.2	89.9	93.8
Cost/ Income	44.6	44.3	43.4	42.2	41.3
CASA	44.0	43.2	48.0	48.0	48.0
Earnings (%)					
NIM	4.7	4.8	4.7	4.6	4.6
ROE	19.4	18.3	17.9	18.7	19.5
ROA	1.9	1.9	1.9	2.0	2.1

Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
16 April 2014	BUY	837
20 May 2014	BUY	997
25 November 2014	BUY	1171
03 July 2015	BUY	1294
19 January 2016	BUY	1259
29 August 2016	BUY	1387
30 January 2017	BUY	1417
04 May 2017	BUY	1681

*Initiating Coverage

Investment Rating Criteria

Large Cap Stocks;

Buy	-	**Upside is 10% or more.**
Hold	-	**Upside or downside is less than 10%.**
Reduce	-	**Downside is 10% or more.**

Mid Cap and Small Cap;

Buy	-	**Upside is 15% or more.**
Accumulate*	-	**Upside between 10% - 15%.**
Hold	-	**Absolute returns between 0% - 10%.**
Reduce/Sell	-	**Absolute returns less than 0%.**

To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.

The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating.
* For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

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KAUSHAL KANUBHAI PATEL

Digitally signed by KAUSHAL KANUBHAI PATEL
Date: 2017.05.04 16:09:51 +05'30'