

## Institutional Equity Research

**HDFC**

NBFC | India

1QFY18 Result Update | July 28, 2017

CMP* (Rs)	1,785
Upside/ (Downside) (%)	12
Bloomberg Ticker	HDFC IN
Market Cap. (Rs bn)	2,836
Free Float (%)	100
Shares O/S (mn)	1,589

**BUY** 

Target Price: Rs1,995

**Strong Disbursement Growth; Maintain BUY**

HDFC has reported a strong 20% YoY growth in loan disbursement during 1QFY18 led by robust growth in both individual and non-individual segments. Its overall loan book remained healthy at 18% YoY led by continued pick-up in non-individual loans book (+22.4% YoY and +6.9% QoQ) owing to strong pick-up in lease rental discounting and construction finance. Sustained pick-up in growth of high-margin non-individual loan is encouraging, as the share of corporate loan in overall loan book increased to 29.9% in Jun'17 from 28% in Sept'16. However, HDFC's reported PAT declined by 27% YoY and 23.9% QoQ to Rs15.6bn due to lower investment gains and fee income along with higher tax rate. Drop in investment gains and higher tax rate was primarily due to booking of large capital gains from sale of stake in HDFC Ergo in the year ago quarter. Adjusted for the same, its PAT grew by a healthy 15% YoY in 1QFY18.

**Key Management Commentary**

- ▶ Gross NPA in non-individual segment increased substantially in 1QFY18 as the company recognised loan worth Rs9.1bn to one of the accounts referred to NCLT/IBC by the RBI. The Company has adequately provided for on same and does not foresee any further hit in profitability from the aforementioned account.
- ▶ Individual disbursement growth trajectory began normalizing in 1QFY18 after sharp decline in 2HFY17 due to demonetisation, which the Management expects to improve further in FY18.
- ▶ Non-individual loan contributed 36.1% to incremental growth in HDFC's loan book in 1QFY18 compared to 28.7% in 4QFY17 and 12% in 1QFY17.
- ▶ Individual loan book – before adjusting for loans sold in preceding 12 months – stood at 23% in 1QFY18 (16% net loans sold).
- ▶ Retail spread declined by 9bps QoQ to 1.9% due to decline in BPLR, while the corporate spreads sequentially improved to 3.18% during the quarter compared to 3.09% in 4QFY17.
- ▶ The Management expects decline in standard assets provision norms for individual loan by NHB as the RBI has reduced it for banks to 25bps from earlier 40bps.
- ▶ Its life insurance subsidiary has reinitiated the process of IPO after it fails to get the IRDA nod for merger with Max Life. As the Company expects to launch the IPO in current calendar year, it has guided for lower effective tax rate due to lower capital gain.

**Outlook & Valuation**

Visible sign of pick-up in demand for mortgage loan led by improving affordability, attractive incentive from PMAY scheme and introduction of RERA augur well for sustained growth in loan book for HDFC over next 3-5 years. Looking ahead, we expect further improvement in operating performance on the back of healthy loan book and NII growth. Further, the performance of its various financial business subsidiaries/associates has improved substantially over the last few quarters. **We reiterate our BUY recommendation on the stock with an upwardly revised Target Price of Rs1,995 (from Rs1,786 earlier) primarily due to higher valuation of subsidiaries/associates.**

Key Financials (Rs mn)	FY16	FY17	FY18E	FY19E
NII	87,617	98,558	111,054	125,020
Other Inc.	28,203	24,076	25,279	26,796
PPP	108,231	114,266	126,467	140,686
Net Profit	74,721	78,742	86,116	96,130
EPS (Rs)	44.9	46.8	54.2	60.5
P/E (x)	39.8	38.1	32.9	29.5
BV (Rs)	215.7	249.2	285.3	326.5
P/ABV (x)	8.7	7.5	6.6	5.8
GNPA (%)	0.7	0.7	0.8	0.8
Avg. ROA (%)	2.2	2.2	2.4	2.6
Avg. ROE (%)	17.6	17.4	18.9	19.8

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	8.1	14.0	28.7
Relative to Nifty	2.8	6.8	12.4

Shareholding Pattern (%)	Dec'16	Mar'17
Promoter	-	-
Mutual Funds	3.2	4.1
Insurance Companies	6.1	7.2
Foreign Portfolio Investors	77.3	77.6
Others	13.5	11.2
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

**1 Year Stock Price Performance**

Note: \* CMP as on July 28, 2017

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**Exhibit 1: SOTP Valuations**

Particulars	Basis	Multiple (x)	Stake (%)	Value (Rs)
Value of Standalone Business	BV	3.3	100	1,078
Other Subsidiaries				
HDFC Bank	Market Cap basis		22	733
Gruh Finance	Market Cap basis		60	56
HDFC Standard Life Insurance	EV	3	61.6	200
HDFC Ergo General Insurance	NW		51.3	16
HDFC AMC	AUM		60	57
Other Busineszs				17
Value of Subsideries				1,079
Holding Company Discount	15%			(162)
Total Value of HDFC Ltd.				1,995

Source: RSec Research

**Risks to view**

- ▶ Aggressive competition among the housing finance companies may impact HDFC's operational performance.
- ▶ Unstable interest rate environment may adversely impact its cost of fund.
- ▶ Adverse change in regulatory and policy environment.

**Exhibit 2: Standalone Quarterly Performance**

(Rs mn)	1QFY18	1QFY17	%yoy	4QFY17	%qoq	FY 2017	FY 2016	%yoy
Operating Income	82,377	75,461	9.2	83,606	(1.5)	317,044	288,926	9.7
Interest expenses	54,444	51,262	6.2	52,379	3.9	208,962	193,745	7.9
<b>Net Interest Income</b>	<b>27,933</b>	<b>24,200</b>	<b>15.4</b>	<b>31,226</b>	<b>(10.5)</b>	<b>108,082</b>	<b>95,181</b>	<b>13.6</b>
Non-Interest Income	745	9,841	(92.4)	2,839	(73.8)	19,576	25,061	(21.9)
<b>Total Income</b>	<b>26,974</b>	<b>32,672</b>	<b>(17.4)</b>	<b>32,766</b>	<b>(17.7)</b>	<b>122,634</b>	<b>115,821</b>	<b>5.9</b>
Operating expenses	2,536	2,274	11.5	1,904	33.2	8,368	7,590	10.3
<b>Pre Provision Profits</b>	<b>24,437</b>	<b>30,397</b>	<b>(19.6)</b>	<b>30,862</b>	<b>(20.8)</b>	<b>114,266</b>	<b>108,231</b>	<b>5.6</b>
Provisions	850	650	30.8	1,480	(42.6)	7,000	7,150	(2.1)
<b>Profit Before Tax</b>	<b>23,587</b>	<b>29,747</b>	<b>(20.7)</b>	<b>29,382</b>	<b>(19.7)</b>	<b>107,266</b>	<b>101,081</b>	<b>6.1</b>
Income tax	6,980	7,394	(5.6)	7,632	(8.5)	28,524	26,360	8.2
DTL Provision	1,050	896	17.1	1,308	(19.7)	4,316	3,790	13.9
<b>Net Profit</b>	<b>15,557</b>	<b>21,457</b>	<b>(27.5)</b>	<b>20,442</b>	<b>(23.9)</b>	<b>74,426</b>	<b>70,931</b>	<b>4.9</b>

Source: Company, RSec Research

**Exhibit 3: Non-Interest Income**

(Rs mn)	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	QoQ%	YoY %
Profit from sale of Investment	9,216	281	34	486	21	(96)	(100)
Dividend Income	515	4,560	1,788	2,228	599	(73)	16
Others	111	118	114	125	125	(0)	13
<b>Total Other Income</b>	<b>9,841</b>	<b>4,960</b>	<b>1,936</b>	<b>2,839</b>	<b>745</b>	<b>(74)</b>	<b>(92)</b>

Source: Company, RSec Research

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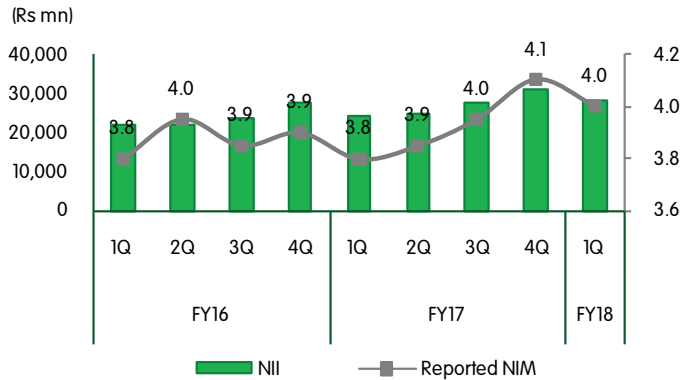
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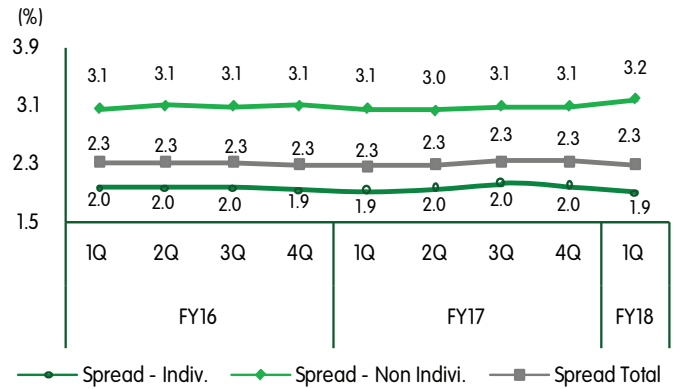
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**Exhibit 4: NII growth was led by healthy growth in loan book and stable spread**


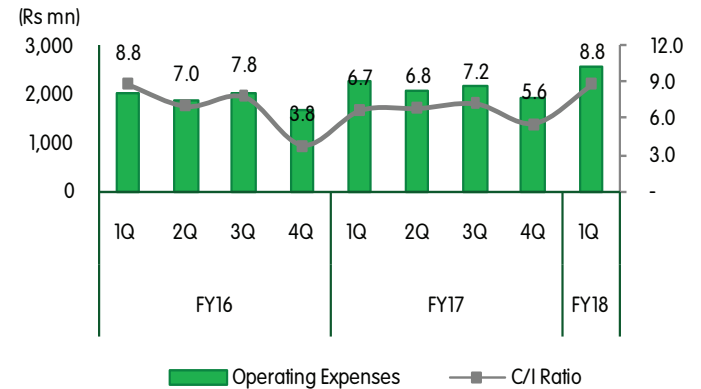
Source: Company, RSec Research

**Exhibit 5: Spread remained stable due to strong growth in high-yielding non-individual segments**


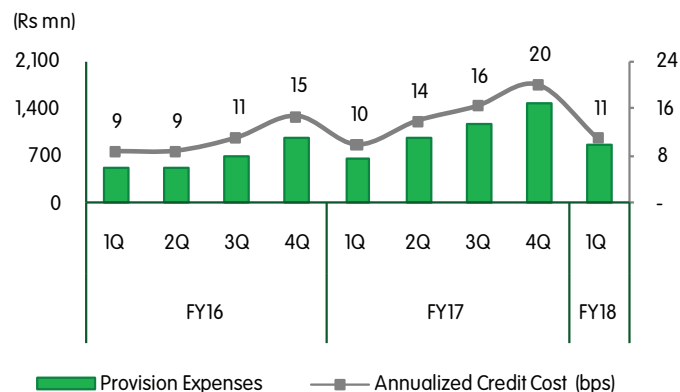
Source: Company, RSec Research

**Exhibit 6: Other income growth was lower due to lower fee and dividend income**

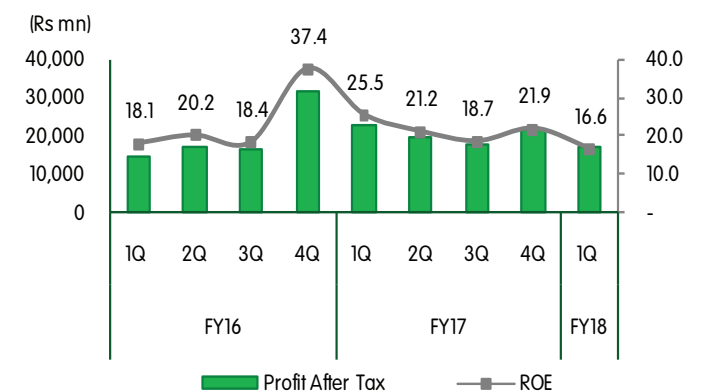

Source: Company, RSec Research

**Exhibit 7: C/I ratio increased sequentially due to sequential rise in operating expenses**


Source: Company, RSec Research

**Exhibit 8: Provisioning expenses declined sequentially despite slippages in corporate portfolio**


Source: Company, RSec Research

**Exhibit 9: PAT growth declined due to lower investment gains and fee income along with higher tax rate**


Source: Company, RSec Research

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**Exhibit 10: Loan break-up**

(Rs bn)	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	QoQ%	YoY %
Individuals	1,853	1,935	1,993	2,044	2,147	5.0	15.9
Corporate	763	771	832	874	934	6.9	22.4
Others	41	47	43	47	48	3.6	16.7
<b>Total Loans</b>	<b>2,657</b>	<b>2,754</b>	<b>2,869</b>	<b>2,965</b>	<b>3,130</b>	<b>5.6</b>	<b>17.8</b>

Source: Company, RSec Research

**Exhibit 11: Loan Mix (%)**

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	QoQ bps	YoY bps
Individuals	69.7	70.3	69.5	69.0	68.6	(35)	(112)
Corporate	28.7	28.0	29.0	29.5	29.9	38	113
Others	1.6	1.7	1.5	1.6	1.5	(3)	(1)
<b>Total Loans</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>(0)</b>	<b>(0)</b>

Source: Company, RSec Research

**Exhibit 12: Ratios**

(%)	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	QoQ%	YoY %
Spread - Individual Loans	1.94	1.92	2.02	1.99	1.90	(9)	(4)
Spread - Non Individual loans	3.10	3.06	3.09	3.09	3.18	9	8
Combined Spread on Loans	2.32	2.26	2.34	2.33	2.29	(4)	(3)
NIM	4.00	3.80	3.95	4.10	4.00	(10)	-
Other Income As % Opr Income	30.1	17.4	6.8	8.7	2.8	(590)	(2,736)
C/I Ratio	7.0	7.2	7.5	5.8	9.4	359	244
Provision as % of Op Profit	11.2	3.6	4.4	4.8	3.5	(132)	(771)
Tax Rate (Exc. DTL)	27.4	24.5	28.5	26.0	29.6	362	221
Tax Rate (Inc. DTL)	30.7	28.6	32.8	30.4	34.0	362	334
Total CAR	16.6	16.5	16.4	14.5	14.7	20	(190)
Tier I	13.2	13.1	13.4	11.8	12.1	30	(110)
Tier II	3.4	3.4	3.0	2.7	2.6	(10)	(80)
GNPA - Individual Loans	0.70	0.75	0.81	0.79	0.65	(14)	(5)
GNPA - Non Individual Loans	0.5	0.6	0.7	0.6	2.1	148	158
GNPA Ratio (Combined)	1.1	1.1	1.2	1.2	1.1	(4)	-

Source: Company, RSec Research

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**Profit & Loss**

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Interest income	285,784	312,544	347,569	391,894
Interest expenses	198,167	213,986	236,515	266,874
<b>Net interest income</b>	<b>87,617</b>	<b>98,558</b>	<b>111,054</b>	<b>125,020</b>
Noninterest income	28,203	24,076	25,279	26,796
<b>Total income</b>	<b>115,821</b>	<b>122,634</b>	<b>136,334</b>	<b>151,816</b>
Operating expenses	7,590	8,368	9,867	11,131
<b>Pre provision profits</b>	<b>108,231</b>	<b>114,266</b>	<b>126,467</b>	<b>140,686</b>
Provisions	7,150	7,000	8,500	9,000
Profit before tax	101,081	107,266	117,967	131,686
Income tax	26,360	28,524	31,851	35,555
<b>Net profit</b>	<b>74,721</b>	<b>78,742</b>	<b>86,116</b>	<b>96,130</b>

**Balance sheet**

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Current assets	136,427	188,334	167,288	181,750
Investments (net)	153,454	204,101	152,708	155,487
Loans	2,592,240	2,964,720	3,440,433	3,990,829
Fixed assets	6,645	6,423	7,136	7,368
<b>Total assets</b>	<b>2,888,766</b>	<b>3,363,579</b>	<b>3,767,565</b>	<b>4,335,433</b>
Total deposits	746,700	865,740	970,357	1,103,320
Total borrowings	1,636,470	1,939,600	2,253,421	2,605,318
Other liabilities	164,897	162,296	119,411	138,635
Total liabilities	25,480,666	29,676,361	33,431,890	38,472,717
Shareholders' equity	340,700	395,943	453,217	518,755
<b>Total liabilities &amp; equity</b>	<b>2,888,766</b>	<b>3,363,579</b>	<b>3,767,565</b>	<b>4,335,433</b>

**Key Ratios**

Y/E March	FY16	FY17	FY18E	FY19E
Asset Quality Ratios (%)				
Gross NPA	0.7	0.7	0.8	0.8
Growth Ratios (%)				
Advances growth	13.6	14.4	16.0	16.0
Net interest income	10.6	12.5	12.7	12.6
Fee income	79.2	-14.6	5.0	6.0
Core earnings growth	22.0	5.9	11.2	11.4
Pre-provision profits	23.1	5.6	10.7	11.2
Net profit	17.6	5.4	9.4	11.6
Total assets	13.8	16.4	12.0	15.1
NIM (%) – calculated	3.6	3.6	3.7	3.9
ROE (%)	17.6	17.4	18.9	19.8
ROA (%)	2.2	2.2	2.4	2.6
Cost-to-income (%)	6.6	6.8	7.2	7.3
Capital Adequacy Ratio (%)				
Tier 1	13.2	11.8	11.4	11.1
Tier 2	3.4	2.7	2.6	2.5
Total	16.6	14.5	14.1	13.6
Per Share Data (Rs)				
EPS	44.9	46.8	54.2	60.5
DPS	14.0	0.0	15.1	16.0
Dividend yield (%)	0.8	0.0	0.8	0.9
BVPS	215.7	249.2	285.3	326.5
P/E (x)	39.8	38.1	32.9	29.5
P/BV (x)	8.7	7.5	6.6	5.8

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**Rating Guides**

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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