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Company update and
earnings revision

Financials

Target price Rs2,423

Earnings revision

(%)	FY21E	F22E
NII	↑ 0.3	↑ 3.4
PPP	↑ 1.9	↑ 1.7
PAT	↑ 15.2	↑ 5.8

Target price revision

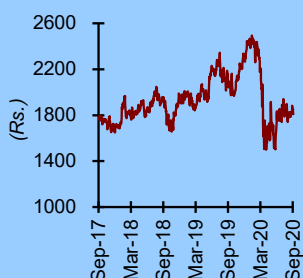
Rs2,423 from Rs2,345

Shareholding pattern

	Dec '19	Mar '20	Jun '20
Promoters	0.0	0.0	0.0
Institutional investors	89.2	88.7	88.5
MFs and other	9.0	9.5	9.4
FIs/Banks	0.0	0.1	0.1
Insurance	7.3	8.1	8.6
FII	72.9	71.1	70.4
Others	10.8	11.3	11.5

Source: NSE

Price chart



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INDIA

ICICI Securities

HDFC Limited

BUY

Maintain

Rs1,770

More than adequate buffers to navigate the cycle

HDFC has strengthened its balance sheet further with recent capital raise (shoring up tier-1 to 19.5%) over and above provisioning buffer of 2.64% of AUM and excess liquidity (at >5% of balance sheet). While movement from Morat 1.0 to Morat 2.0 has not been overwhelming (higher print at 16.6% for retail and 39% for non-retail) due to request-based disclosure approach (not collection efficiency), flow into restructuring will still be restricted. Similar to actions in Q4FY20, HDFC might proactively prefer recognising non-Covid stress upfront (rather than restructuring). Disbursement trends MoM (>80% in July) suggest normalisation in a couple of months and start of growth phase post Q3FY21. Factoring-in the recent capital raise, we revise our EPS and BV upwards by 10%/1% and 12.7%/13.4% respectively for FY21E/FY22E. We maintain our stance of excess buffers (credit cost, liquidity, capital) and superior profile to support earnings traction and help consolidate HDFC's positioning amidst adversity. Maintain BUY with a revised SoTP-based target price of Rs2,423 (earlier: Rs2,345).

- **Dissecting moratorium across sub-segments:** The movement from Morat 1.0 (27% of overall AUM) to Morat 2.0 (22.4% as of July – combination of 12.3% individual and 10.1% non-individual) has not been overwhelming. Moratorium within individual loans was down to 16.6% from 22.6%. Of the non-retail portfolio constituting 26% of AUM, 39% is under moratorium. Within non-retail sub-segments, almost 70% of developer loans, ~20% of corporate loans and 15% of LRD was under moratorium. As the company is disclosing proportion of moratorium requests and not actual collection efficiency, we are not expecting any significant change in trend from July (disclosed numbers) to August.
- **How much of moratorium can flow into restructuring:** Based on customer feedback, of the retail moratorium customers, <15% have faced job losses or business closures with the balance merely conserving cash. Also, in non-retail, >70% have made part/full payment of interest during moratorium. Key monitorable would be the balance 30% (10% of non-retail representing 2.8% of AUM) who have not made any payment at all. Of this, one-third are corporate customers and 2/3rd developers. Even in the worst case, assuming 15% of retail moratorium and 40% of non-retail moratorium customers seeking restructuring, the restructured pool would translate to ~6.5% of AUM, calling for an additional 65bps of provisioning.
- **Adequate provisioning buffer to cushion earnings volatility:** HDFC has been utilising 30% of any windfall gains (from stake sale of its investments) in building a contingency buffer. Thereby, it now has Rs122bn of provisioning reserves (equivalent to 2.64% of the portfolio) and >50% of it is towards the unrecognised stress pool. With this buffer, incremental provisioning requirement will be capped at 1.2%/0.8% over FY21E/FY22E.

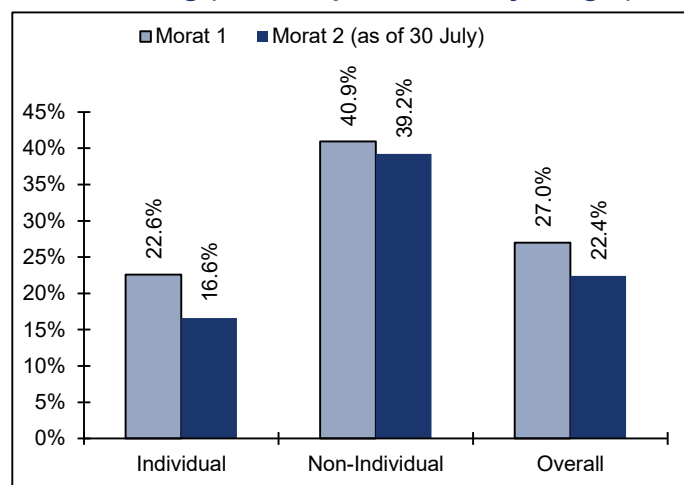
Market Cap	Rs3173bn/US\$43.3bn
Reuters/Bloomberg	HDFC.BO/ HDFC IN
Shares Outstanding (mn)	1,732.0
52-week Range (Rs)	2499/1,473
Free Float (%)	100.0
FII (%)	70.4
Daily Volume (US\$/'000)	1,65,036
Absolute Return 3m (%)	0.3
Absolute Return 12m (%)	15.7
Sensex Return 3m (%)	13.5
Sensex Return 12m (%)	5.6

Year to March	FY19	FY20	FY21E	FY22E
NII (Rs mn)	114,026	127,480	138,414	157,307
Net Income (Rs mn)	96,325	179,951	99,469	124,447
EPS (Rs)	42.5	40.5	35.8	49.3
% Chg YoY	-16.9	85.7	-47.1	25.1
P/E (x)	16.6	17.4	19.7	14.3
P/BV (x)	2.0	1.8	1.5	1.4
Net NPA (%)	0.8	1.3	2.2	1.7
Dividend Yield (%)	1.2	1.2	0.8	1.1
RoA (%)	2.2	3.7	1.8	2.0
RoE (%)	13.5	22.0	10.4	11.4

Please refer to important disclosures at the end of this report

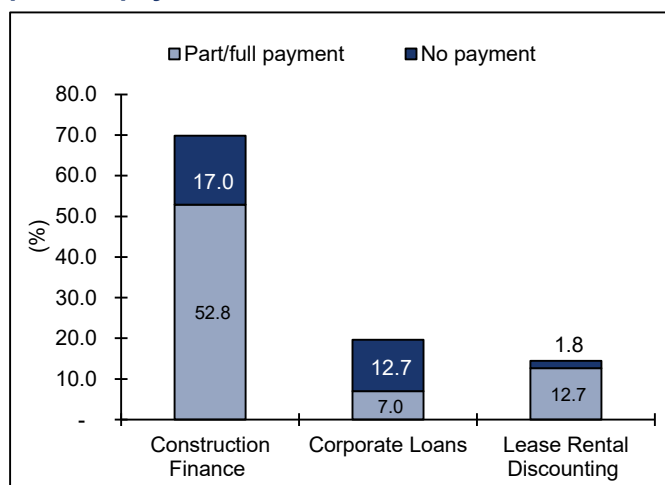
- **Disbursements normalising to a large extent and will pick pace soon:** There has been consistent MoM improvement in retail disbursements (June run-rate at 68% of last year, July at 81%). Normalisation would take another couple of months and the company should report YoY growth post Q3FY21. On the non-retail side, HDFC is focused on lending to select 'AAA' rated corporates. In the interim, for a quarter or so, traction gained MoM will be offset by improved repayment run-rate post Morat 2.0. We are building-in loan growth of 9% (11% for retail loans) by FY21-end and 14% (16% retail) for FY22.
- **Factoring recent capital raise into our estimates:** HDFC has recently raised Rs140bn via QIP through a combination of equity shares + NCD/warrants structure issuing 56.8mn shares at Rs1,760/sh and 17mn warrants (convertible into equity in three years at Rs2,175). This has shored up its tier-1 capital by >320bps to 19.5%. Factoring this, we revise our EPS and BV upwards by 10%/1% and 12.7%/13.4% respectively for FY21E/FY22E.

Chart 1: Movement from morat 1.0 to morat 2.0 not overwhelming (as its requests actually sought)



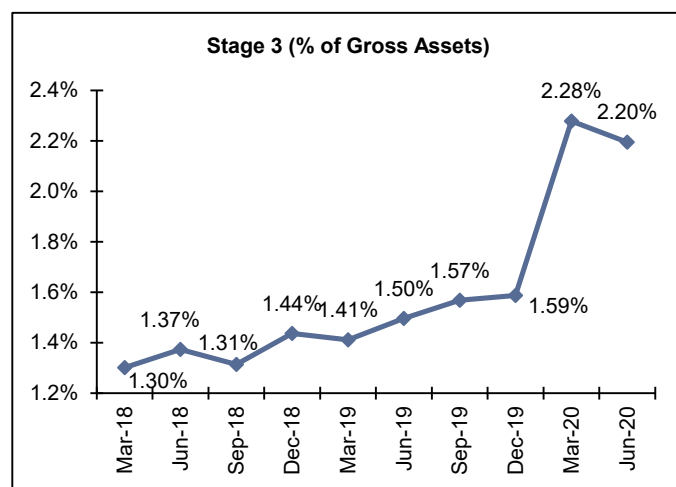
Source: Company data, I-Sec research

Chart 2: Of non-retail loans, ~70% have made part/full payment of interest



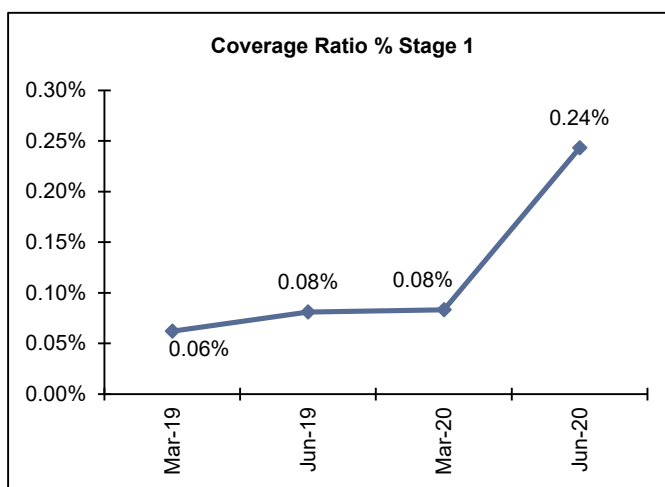
Source: Company data, I-Sec research

Chart 3: Proactively recognised stress in Q4FY20



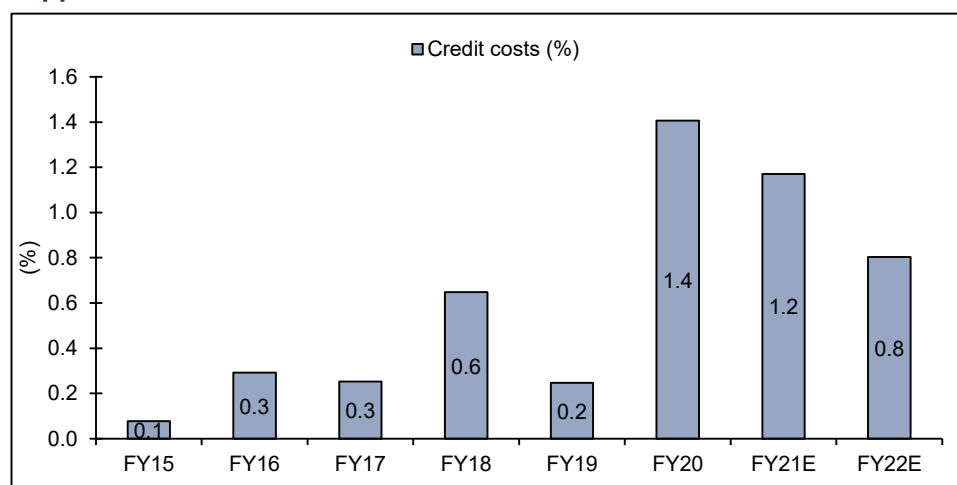
Source: Company data, I-Sec research

Chart 4: Accelerated Stage 1 provisioning in Q1FY21



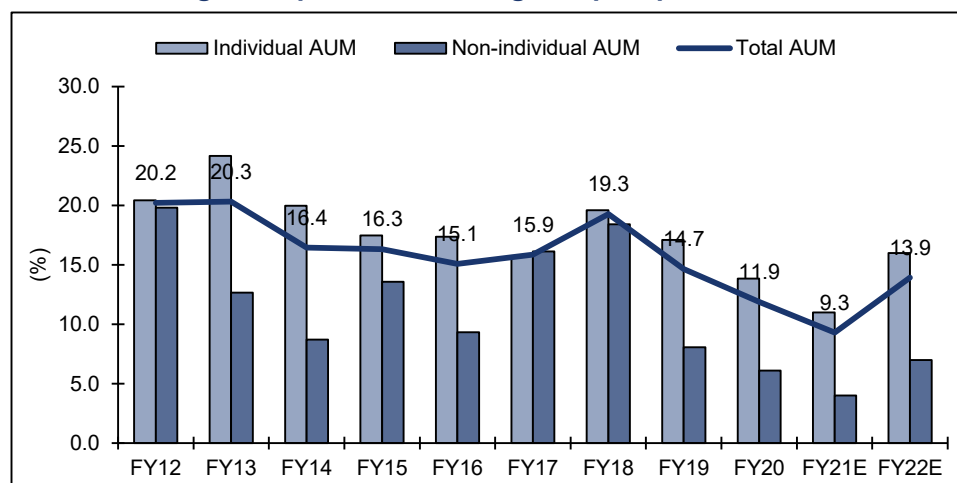
Source: Company data, I-Sec research

Chart 5: Utilising windfall gains to build buffer; incremental provisioning capped at 1.2%/0.8% for FY21E/FY22E



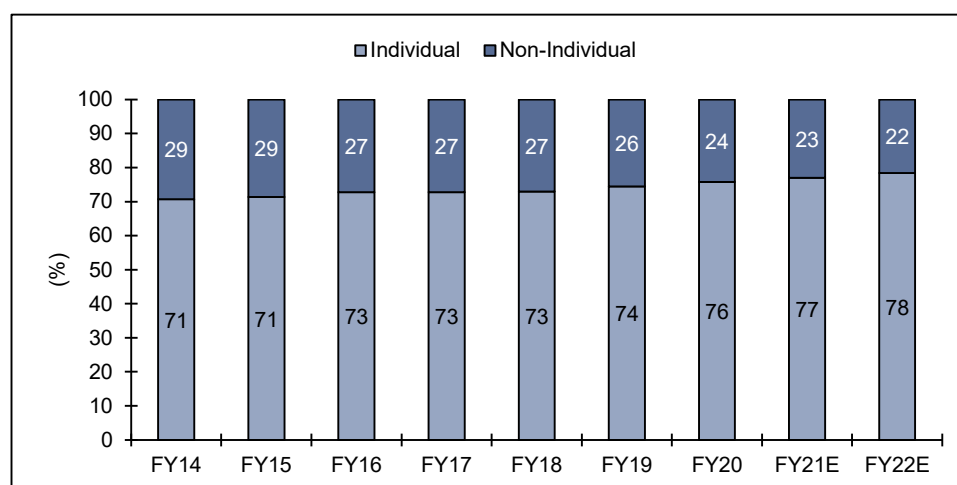
Source: Company data, I-Sec research

Chart 6: AUM growth pace normalising and pick pace soon

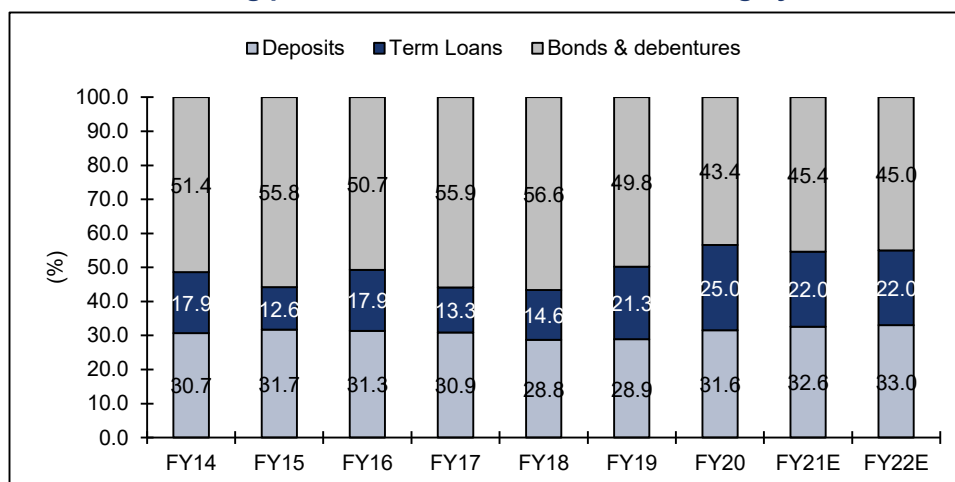


Source: Company data, I-Sec research

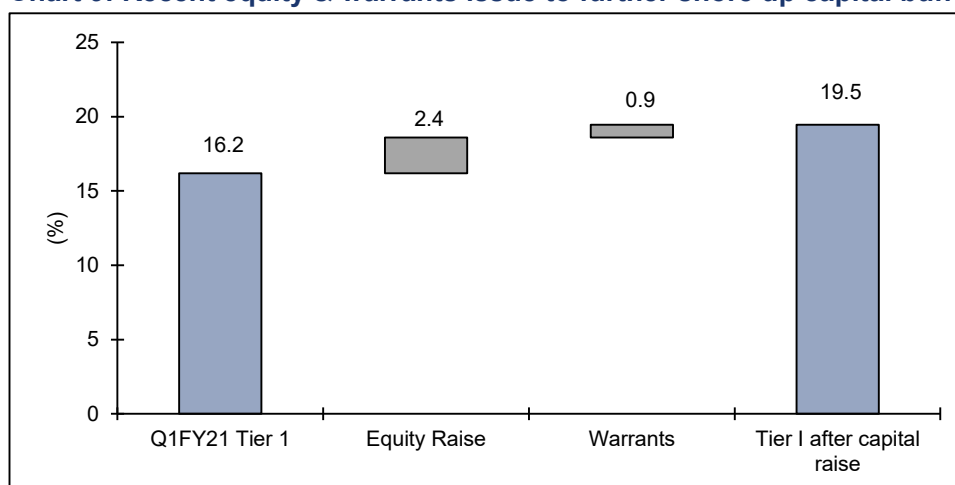
Chart 7: Portfolio mix to remain tilted towards individual loans



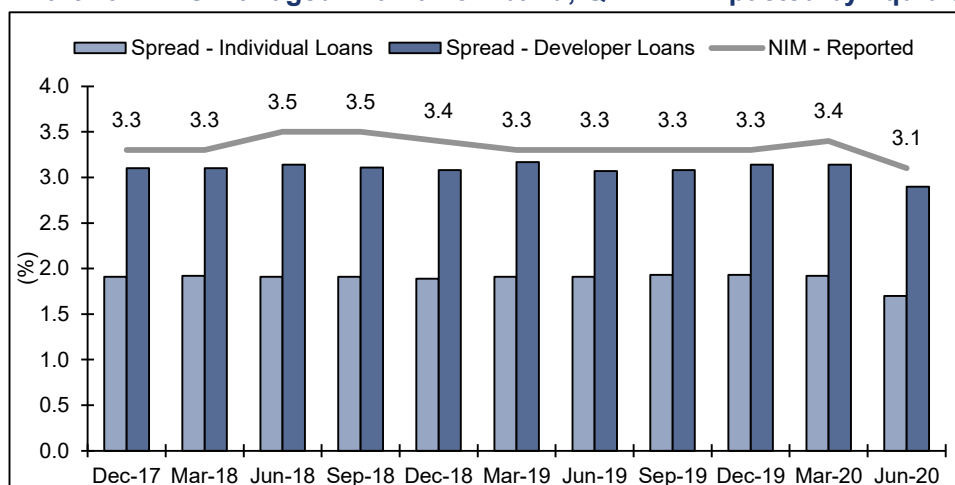
Source: Company data, I-Sec research

Chart 8: Borrowing profile to remain diversified and largely intact

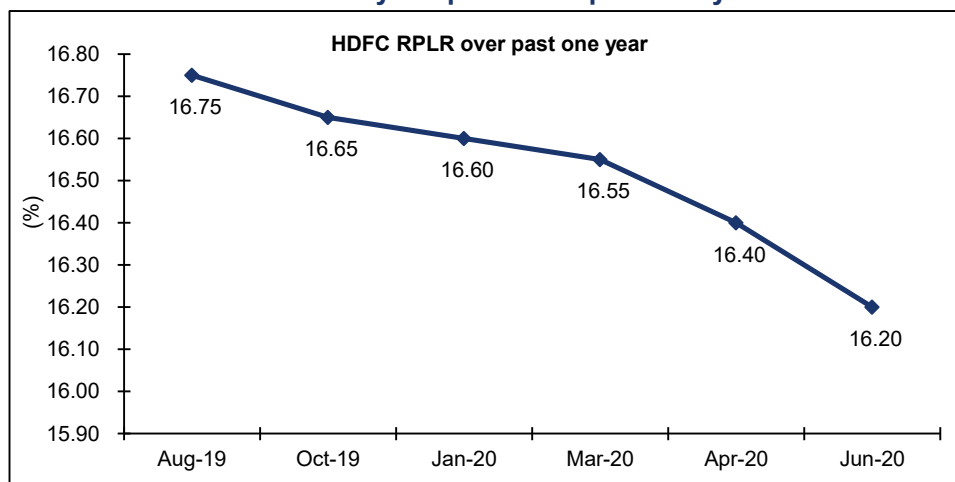
Source: Company data, I-Sec research

Chart 9: Recent equity & warrants issue to further shore up capital buffer

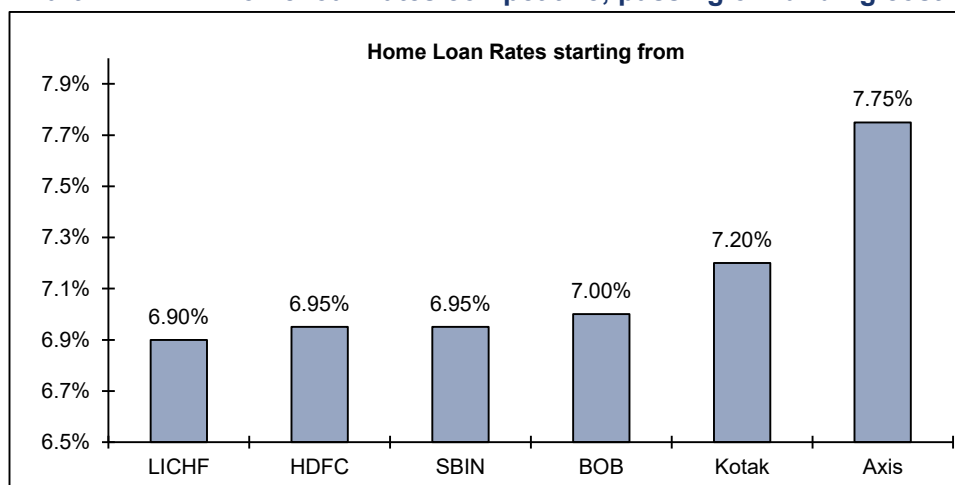
Source: Company data, I-Sec research

Chart 10: NIMs managed in a narrow band; Q1FY21 impacted by liquidity drag

Source: Company data, I-Sec research

Chart 11: RPLR has fallen by 55bp over the past one year for HDFC

Source: Company data, I-Sec research

Chart 12: HDFC home loan rates competitive; passing on funding cost benefit

Source: Company data, I-Sec research

Table 1: Current valuation of core business – SoTP framework

Subsidiary/Associate/JV	% stake	Basis	Multiple/CMP/TP	Total valuation (Rs mn)	Per share value (Rs)	Year
HDFC Bank	19.4%	Fair value	1470.0	11,73,078	649	
	50.1%	Appraisal value	592.0	4,49,511	249	
HDFC Standard Life						
HDFC ERGO General Insurance	50.8%	Book Value	3.0	29,757	16	FY22
HDFC AMC	52.7%	CMP	2615.0	2,20,029	122	FY22
HDFC Venture Capital	80.5%	AUM	10.0%	884	0	FY22
Bandhan Bank	9.9%	Fair value	455	54,401	30	FY22
Value of ancillary business					1066	
CMP					1771	
Value of core business at CMP					705	
BVPS - Core business (FY22)					495	
P/BV - Core business (FY22)					1.4	
Core EPS (FY22)					49.3	
P/E - Core business (FY22)					14.3	

Source: Company data, I-Sec research

Table 2: SoTP-based target price

Subsidiary/Associate/JV	% stake	Basis	Multiple/TP /CMP	Total valuation (Rs mn)	Per share value (Rs)	Year
HDFC Bank	19.4%	Target Price	1470.0	11,73,078	649	
HDFC Standard Life	50.1%	Target Price	592.0	4,49,511	249	
HDFC ERGO General Insurance	50.8%	Book Value	3.0	29,757	16	FY22
HDFC AMC	52.7%	Market value	2615.0	2,20,029	122	FY22
HDFC Venture Capital	80.5%	AUM	10.0%	884	0	FY22
Bandhan Bank	9.9%	Target Price basis	455	54,401	30	FY22
Value of subs (post holdco discount)					1066	
Core Mortgage Business		Book Value	2.7	24,57,391	1358	FY22
Total SOTP Valuation (Rs)				43,85,052	2,423	

Source: Company data, I-Sec research

Financial summary

Table 3: Profit and loss statement

(Rs mn, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Interest earned	3,31,188	3,92,402	4,37,493	4,64,757	5,30,579
Interest expended	2,34,980	2,78,377	3,10,014	3,26,342	3,73,272
Net interest income	96,208	1,14,026	1,27,480	1,38,414	1,57,307
Other income	75,887	41,378	1,50,140	54,020	57,759
Operating expenses	4,831	5,457	5,455	7,543	8,184
Employee costs	4,255	5,054	5,793	6,297	7,053
Depreciation	492	665	1,477	1,471	1,720
Pre-provisioning op profit	1,53,046	1,40,538	2,64,894	1,77,124	1,98,109
Provisions & contingencies	21,150	9,350	59,131	54,863	42,550
Profit before tax	1,31,896	1,31,188	2,05,763	1,22,261	1,55,559
Income taxes	22,303	34,863	25,813	22,792	31,112
Net profit	1,09,593	96,325	1,79,951	99,469	1,24,447

Source: Company data, I-Sec research

Table 4: Balance sheet

(Rs mn, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Share Capital	3,352	3,443	3,464	3,618	3,618
ESOPs					
Reserves and surplus	6,49,297	7,70,112	8,58,117	10,51,167	11,32,201
Minority Interest					
Borrowings	31,97,160	36,52,660	41,91,020	46,49,918	53,44,777
Current liabilities & provisions	1,39,287	1,61,561	1,88,335	2,40,690	2,92,560
Total liabilities & stockholders' equity	39,89,096	45,87,776	52,40,936	59,45,392	67,73,155
Loans & advances	35,73,800	40,07,600	43,99,430	49,70,851	56,24,631
Fixed assets	6,445	6,442	9,861	10,110	12,288
Investments	3,11,119	4,65,617	6,49,444	8,40,161	10,21,221
Cash and Balance	14,851	15,963	34,257	38,655	31,484
Current assets	70,087	83,845	1,32,265	72,796	76,156
Deferred tax assets	12,795	8,309	15,679	12,819	7,375
Total assets	39,89,096	45,87,776	52,40,936	59,45,392	67,73,155

Source: Company data, I-Sec research

Table 5: Key ratios*(Year ending March 31)*

	FY18	FY19	FY20	FY21E	FY22E
Growth:					
AUM	19.3	14.7	11.9	9.3	13.9
Net Interest Income	-3.4	18.5	11.8	8.6	13.6
Total Non-Interest Expenses	127.6	-22.0	-14.4	20.3	10.8
Pre provisioning operating profits	33.9	-8.2	88.5	-33.1	11.8
PAT	47.3	-12.1	86.8	-44.7	25.1
EPS	43.7	-16.9	85.7	-47.1	25.1
Yields, interest costs and spreads (%)					
NIM on AUM	2.9	3.0	3.0	3.0	3.0
Yield on loan assets	9.7	9.8	9.9	9.4	9.4
Average cost of funds	7.8	8.1	7.9	7.4	7.5
Interest Spread on loan assets	1.9	1.7	2.0	2.0	1.9
Operating efficiencies					
Non interest income as % of total income	18.6	9.5	25.5	10.4	9.8
Cost to income ratio (%)	19.8	13.0	10.0	11.1	10.8
Op.costs/avg AUM (%)	0.5	0.3	0.3	0.3	0.3
No of employees (estimate)	2,575	2,745	2,915	3,085	3,255
No of branches	326	341	356	371	386
Average annual salary (Rs)	16,52,311	18,41,275	19,87,238	20,41,254	21,66,803
Annual inflation in average salary(%)	-2.0	11.4	7.9	2.7	6.2
Salaries as % of non-int.costs (%)	22.3	34.0	45.5	41.1	41.6
NII /employee (Rs mn)	3,736	4,154	4,373	4,487	4,833
AUM/employee(Rs mn)	1,565	1,683	1,773	1,831	1,977
AUM/ branch (Rs mn)	12,358	13,546	14,516	15,226	16,672
Capital Structure					
Debt-Equity ratio	4.9	4.7	4.9	4.4	4.7
Leverage (x)	6.1	5.9	6.1	5.6	6.0
CAR (%) –standalone	19.2	19.2	17.7	21.4	20.7
Tier 1 CAR (%) –standalone	17.3	17.6	16.6	20.2	19.5
Tier 2 CAR (%) – standalone	1.9	1.6	1.1	1.2	1.2
Asset quality and provisioning					
GNPA (%)	1.3	1.4	2.3	4.0	3.0
NNPA (%)	0.8	0.8	1.3	2.2	1.7
GNPA	47,170	57,430	1,00,307	1,98,834	1,68,739
NNPA	27,470	32,440	55,169	1,09,359	92,806
Coverage ratio (%)	41.8	43.5	45.0	45.0	45.0
Return ratios & capital management					
RoAA (%)	3.0	2.2	3.7	1.8	2.0
RoAE (%)	20.9	13.5	22.0	10.4	11.4
Payout ratio (%)	20.8	33.3	12.5	24.3	29.1
Valuation Ratios					
Reported EPS	65.4	56.0	103.9	55.0	68.8
Adjusted EPS	32.9	42.5	40.5	35.8	49.3
Reported BV	389.4	449.4	497.4	583.1	627.9
Adjusted BV	303.7	351.4	387.1	463.6	494.6
P/E	21.5	16.6	17.4	19.7	14.3
P/B	2.3	2.0	1.8	1.5	1.4

Source: Company data, I-Sec research

Table 6: DuPont analysis*(Rs mn, year ending March 31)*

	FY18	FY19	FY20	FY21E	FY22E
Interest earned	10.1	10.4	10.4	9.9	10.0
Interest expended	7.2	7.3	7.4	7.0	7.0
Gross Interest Spread	2.9	3.0	3.0	3.0	3.0
Provisioning for NPAs	0.6	0.2	1.4	1.2	0.8
Net Interest Spread	2.3	2.8	1.6	1.8	2.2
Operating cost	0.6	0.4	0.3	0.3	0.3
Lending spread	1.7	2.4	1.3	1.5	1.8
Non-interest income	2.3	1.1	3.6	1.2	1.1
Operating spread	4.0	3.5	4.9	2.6	2.9
Tax	0.7	0.9	0.6	0.5	0.6
Return on average loan assets	3.4	2.5	4.3	2.1	2.3
Effective leverage (average loan assets/ average equity)(x)	6.2	5.3	5.1	4.9	4.8
RoAE	20.9	13.5	22.0	10.4	11.4

Source: Company data, I-Sec research

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