Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Housing Development Finance Corporation

Riding on multiple growth triggers

NBFC	Sharekhan code: HDFC

Reco/View: Buy	↔	CMP: **Rs. 2,844**	Price Target: **Rs. 3,589**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 19.19

Updated Nov 08, 2021

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

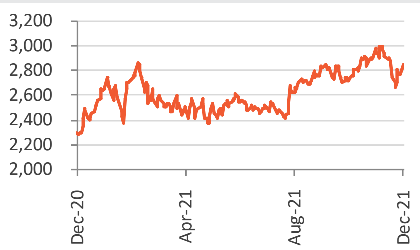
Company details

Market cap:	Rs. 514,396 cr
52-week high/low:	Rs. 3,021/2,267
NSE volume: (No of shares)	14.9 lakh
BSE code:	500010
NSE code:	HDFC
Free float: (No of shares)	180.8 cr

Shareholding (%)

Promoters	-
FII	72.0
DII	16.9
Others	11.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.3	-0.1	11.8	23.4
Relative to Sensex	-0.3	-1.0	-1.1	-3.9

Sharekhan Research, Bloomberg

Summary

- We believe HDFC is the strongest player in housing finance space and better-placed among all its peers with a robust liability franchise, healthy balance sheet with growth levers.
- HDFC has consistently performed well as compared to its peers across business cycles. Better affordability and a change in housing needs post the pandemic, make HDFC a key beneficiary of changing sector dynamics.
- We expect the company's loan book to witness strong growth going ahead with individual loan book to remain healthy for the company; on the asset quality front, HDFC has been able to maintain its GNPAs better than its peers (September GNPAs were at 2% with restructured loans constituting 1.4% of loan book).
- We re-iterate a Buy on HFDC with a SOTP based PT of Rs. 3,589. At CMP, HDFC trades at 3.9x of FY23E P/BV. The stock has corrected by 14% from the highs and touched a low of Rs. 2,656.

We believe that the housing finance sector is set to grow exponentially going ahead driven by lower penetration in India as compared to other developed and developing countries. Additionally, better affordability, record low interest rates and discounts from real estate companies coupled by supportive government initiatives is likely to boost the demand for housing. Government initiatives such as the Pradhan Mantri Awas Yojana (PMAY) and Smart Cities Mission would boost housing demand in India. Nearly 66% of India's population is aged below 35 and ~32% of the population resides in cities; this is estimated to be 50% by 2030. Hence, considering the above factors and opportunities present in the housing sector, we believe that HDFC stands to benefit going forward, being the largest and dominant player in the housing finance segment. The company has demonstrated AUM growth at a CAGR of 14% over FY17 through FY21. Its AUM rose by 11% y-o-y in Q2FY22 and disbursements in October 2021 was the second highest with 44% y-o-y growth. The management expects a positive loan book growth in FY22.

- **Gaining from favourable demand trends:** Driven by favourable sector dynamics, HDFC is poised to witnessed a strong growth going ahead. The real estate market has picked up steadily after the slowdown due to pandemic with demand back on track in the metros and lending rates are at all-time lows. With an increase in the affordability and rise in the income levels, it is opportune time for the HFCs to cater to financing needs. We expect the company to deliver an AUM growth of 13% over FY22E to FY23E.
- **Asset quality remains stable:** The company's asset quality remained stable and stands better as compared to its peers. Its retail/individual loans NPAs have remained at less than 1% over the years, except for 1.37% in Q1FY22. With respect to non-individual NPAs, it appears to have peaked out in Q1FY22 (4.87%). The collection efficiency (CE) has improved over the quarter and for individual loans, the CE was at 98% in Q2FY22. Hence with the improvement in the collections, we expect asset quality to remain stable going ahead.
- **Strong capital position:** With capital adequacy at 22.4% as on September 21, the company is well capitalised to reap the benefits of potential growth opportunities housing finance space.

Our Call

Valuation: We re-iterate Buy on HFDC with a SOTP based PT of Rs. 3,589. At CMP, HDFC trades at 3.9x of FY23E P/BV. HDFC has weathered and emerged as the strongest player among all large HFCs, especially during the pandemic. The management was optimistic in terms of improving CE and asset quality. Individual non-performing loans seem to be restrained at 1%, barring Q1FY2022, which saw NPA at 1.37%. While non-individual loans are likely to take some more time to recover. On the disbursement front, the individual segment witnessed the highest-ever disbursals, while management indicated a healthy pipeline for the non individual segment. We believe that the company would emerge as the key beneficiary of the favourable macro factors play - low interest rate regime, improved affordability, revival of demand for housing and stable property prices.

Key Risks

Any prolonged economic slowdown may impact its growth and asset quality.

Valuation Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
PAT	12,027	14,697	16,433	18,050
EPS (Rs.)	59.8	73.5	82.2	90.3
BVPS (Rs.)	603.0	661.8	726.9	798.9
P/E (x)	47.5	38.6	34.5	31.4
P/BVPS (x)	4.7	4.3	3.9	3.6
ROE (%)	12.3	12.9	13.1	13.4
ROA (%)	2.2	2.4	2.4	2.3

Source: Company; Sharekhan estimates

SOTP Valuation

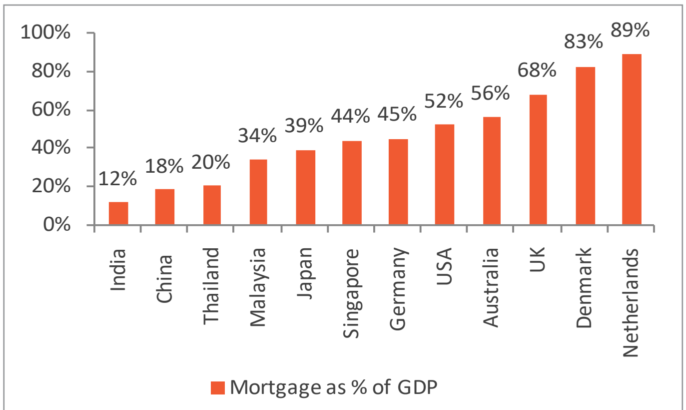
Subsidiary/Associate/JV	% stake	Basis	Per share value
HDFC Bank	21.1%	Target Price	997
HDFC Life	50.0%	Target Price	380
HDFC ERGO General Insurance	45.0%	Book Value	21
HDFC AMC	52.7%	BBG consensus TP with holdco discount	216
Bandhan Bank	9.9%	BBG consensus TP with holdco discount	27
HDFC Credila	100.0%	Book Value	10
Value of subs (post holdco discount)			1641
Core Mortgage Business		2.7x Book Value	1948
Total SOTP Valuation (Rs)			**3,589**

Source: Company; Sharekhan Research

Favourable growth drivers in housing finance space

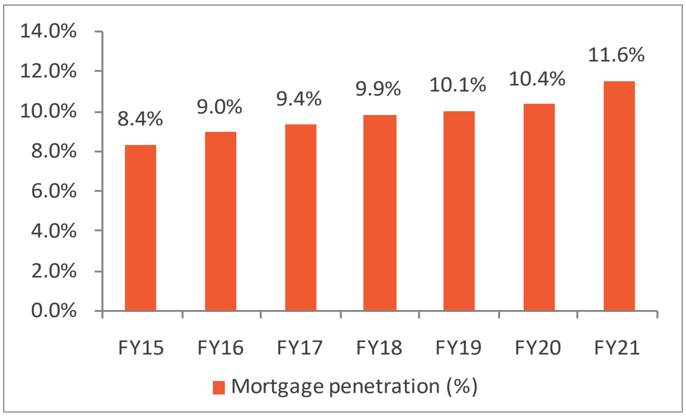
We believe that HFCs stand to benefit from the opportunities in housing sector as they are well equipped with competitive product offerings and product pricing. As per the Ministry of Housing and Urban Affairs, the demand for affordable housing has been pegged at ~11.22 million houses. With the adaption of Pradhan Mantri Awas Yojana (PMAY) in 2015, the government had targeted to meet the demand for 11.22 mn houses. Under this programme, 11.4 million houses have been sanctioned and out which 5.3 mn have been completed till date. This growing need for housing in the urban India has thrown large opportunities with many developers seeking to exploit this opportunity. The residential housing market has demonstrated robust performance in Q2FY22 with residential unit sales and new launches of residential projects growing robustly since the outbreak of pandemic. Housing sales increased by 65% q-o-q to 32,358 apartment units in Q2FY22. With respect to launches, the sector also saw new launches of approximately 32,860 units, an increase of 21% q-o-q. Apart from this, there were significant launches in the mid-market and affordable housing categories, accounting to 73% in FY21. On the pricing front, the prices remained largely stable across all the seven cities during September 2021 and developers are expected to offer incentives to attract the prospective home buyers. We believe HFCs would be the biggest beneficiaries of the housing cycle uptick with competitive product offerings with competitive prices supported by stable property houses over the years and government measures.

Low penetration, opportunity for mortgage finance companies



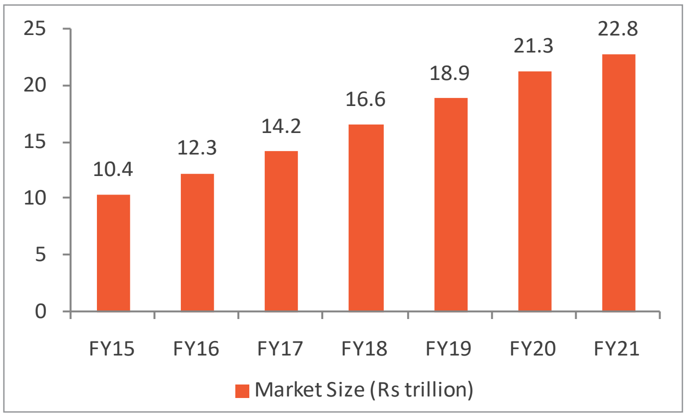
Source: Company (HDFC Ltd); Sharekhan Research

Mortgage Penetration India over the years (%)



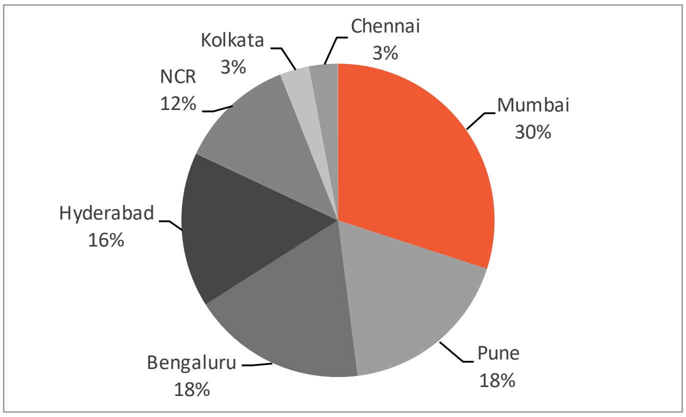
Source: Company (Aavas); Sharekhan Research

Housing market size - India



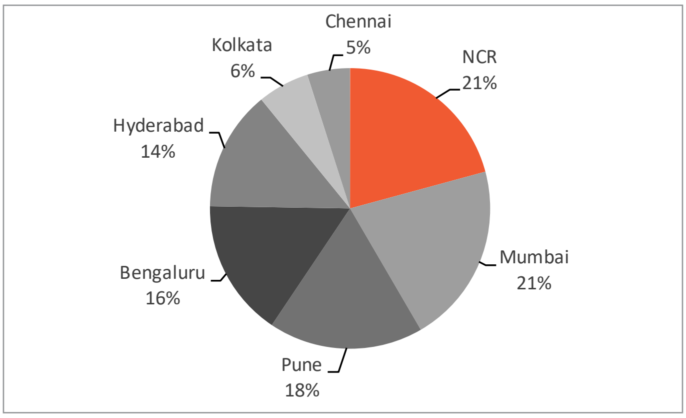
Source: Company (Aavas); Sharekhan Research

Percentage increase in sales in Q1FY22



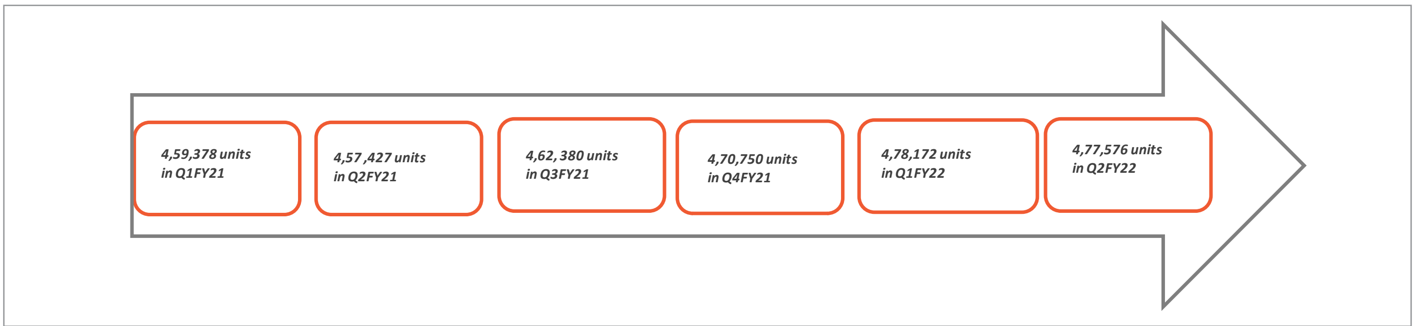
Source: Industry; Sharekhan Research

Percentage increase in sales in Q2FY22



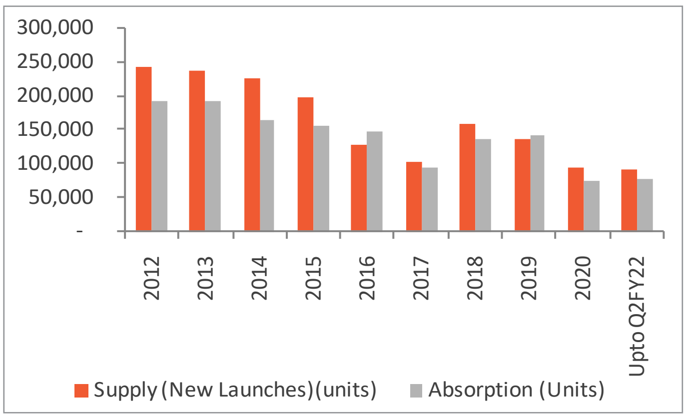
Source: Industry; Sharekhan Research

Unsold Inventory (in nos)



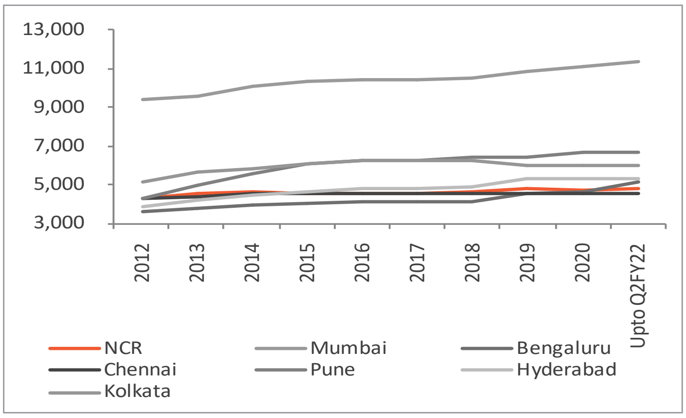
Source: Industry; Sharekhan Research

Residential supply & absorption (in units)



Source: Industry; Sharekhan Research

Value trend (Rs. per sq ft)

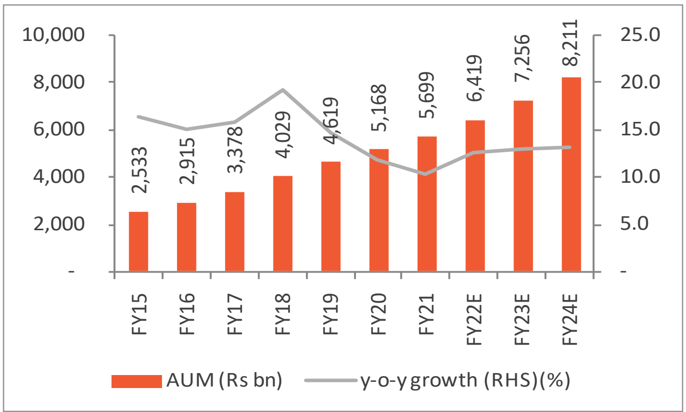


Source: Industry; Sharekhan Research

HFDC is likely to be a key beneficiary on favourable demand trends:

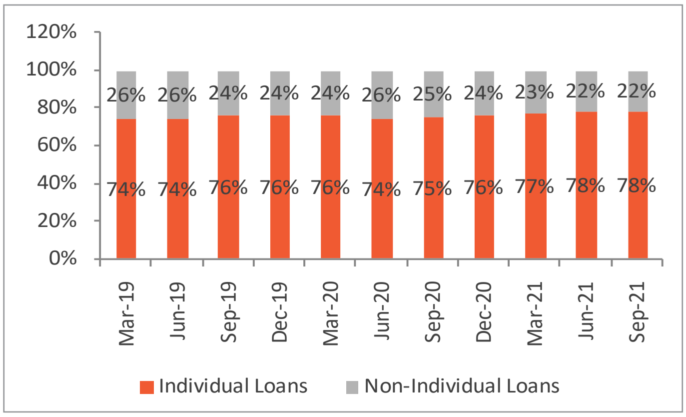
HDFC is a dominant player in the housing finance space and is expected to benefit from the revival of the economy. We expect its AUM to witness robust growth at a CAGR of 13% over FY22E through FY24E. With the improvement in the macro/ sector dynamics such as recovery in the real estate sector, benign interest rates, stable property prices and improvement in the affordability, HDFC is expected to be a key beneficiary being the largest player in the housing space. For Q2FY22, the company recorded highest disbursements. Individual loan book is expected to witness higher growth going ahead supported by favorable demand trends, while the non-individual segment is likely to grow in single digits going ahead. This segment's growth was subdued in Q2FY22 on account of pre payments on REIT issuance in Q1FY22. Nonetheless, trends are looking positive with the company expecting a positive growth to close FY22. It also expects overall housing emand to remain strong for affordable and luxury segments coupled with new project launches going ahead.

AUM growth (%)



Source: Company; Sharekhan Research

AUM mix (%)

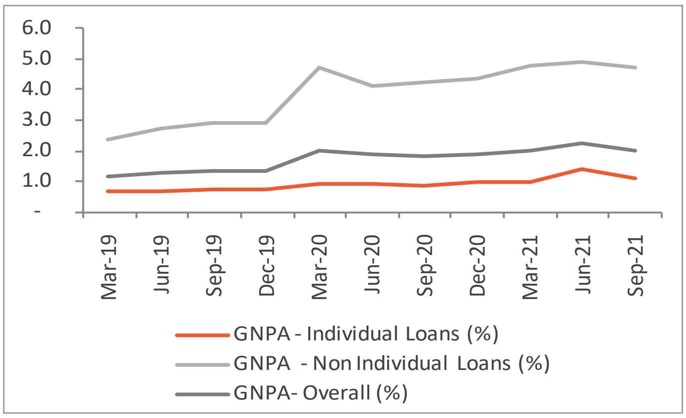


Source: Company; Sharekhan Research

Asset quality remains stable

HDFC's asset quality remained stable and stands better as compared to its peers. Its retail/individual loans NPAs have remained at less than 1% over the years, except for 1.37% in Q1FY22. With respect to non-individual NPAs, it appears to be peaked out in Q1FY22 (4.87%). Collection efficiency (CE) has improved over the quarter and for individual loans the CE was at 98% in Q2FY22. As of September 2021, restructuring book under OTR 1 and 2 was 1.4% of the book as compared 0.9% in June 2021. Of the total restructured book, 63% are individual loans, while the rest are non-individual loans. Resolution of a key account is expected to result in a meaningful reduction in restructured assets. Within restructured loans for individual book, 65% were from self-employed segment. We believe that, the company has adequately provided for the stress in the assets. As of September 2021, the company carries a provision for NPAs stands at Rs 13,340 cr vs. the required Rs 6,605 crore under the expected credit loss (ECL) model.

Segment- wise GNPAs (%)

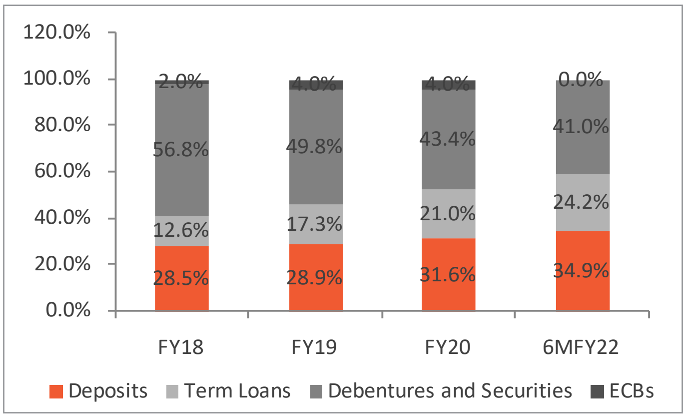


Source: Company; Sharekhan Research

Strong capital position

HDFC has one of the best liabilities franchise among all HFCs. It is adequately capitalised with capital adequacy at 22.4% with Tier-1 Capital ratio at 21.6% as of September 2021. Being a reputed brand name and having favourable credit rating, the company can raise funds at competitive rates. It has a diversified borrowings profile with deposits constituting 35% of borrowings.

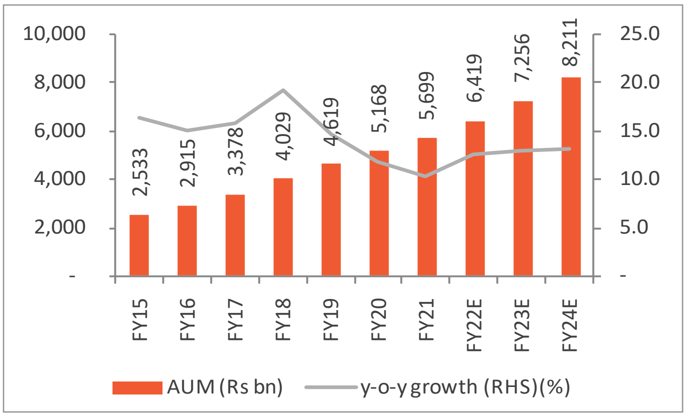
Diversified borrowing mix (%)



Source: Company; Sharekhan Research

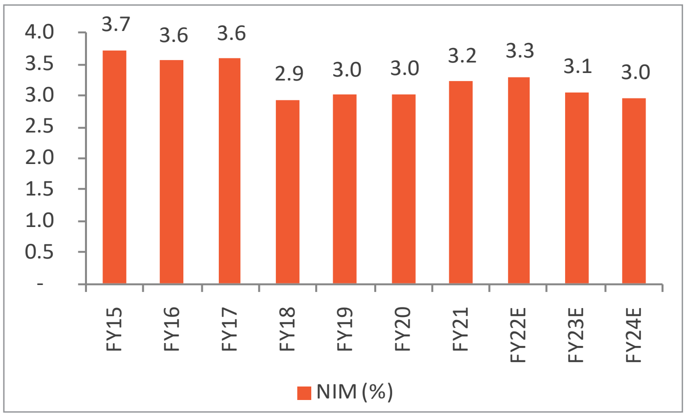
Financials in charts

AUM growth (%)



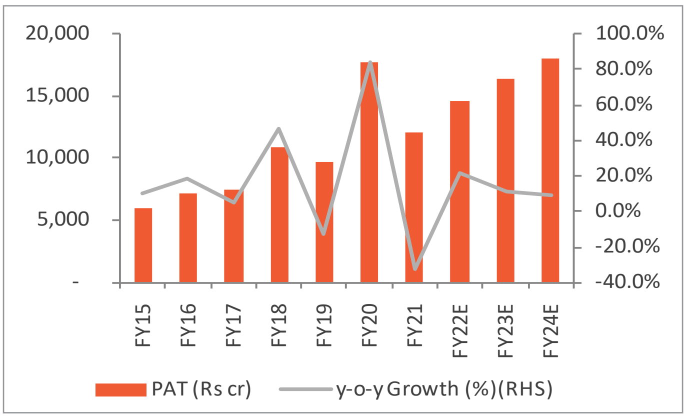
Source: Company; Sharekhan Research

NIM on average AUM (%)



Source: Company; Sharekhan Research

PAT trend



Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view - Housing demand to grow exponentially amid favourable macros, better affordability and low interest rates

Long-term structural indicators remain strong for housing and mortgages in India. Interest rates are low and several states have given incentives for home buying, which is likely to prop up demand. Correction in borrowing costs, which was steep for high-rated NBFCs, is another positive. Moreover, rising affordability and softening pricing (helped by tax incentives) are positive for demand offtake and LTV outlook for HFCs. India has a young population and government schemes such as CLSS, etc., which will facilitate even the affordable housing segments along with low penetration levels of mortgages in India (at 11% of GDP, against 18% in China and 56% in the US). We believe economic recovery is also gaining momentum and stimulus/supportive measures by the government and the Reserve Bank of India (RBI) will further aid to the same. We believe the outlook is resilient for well-run NBFC sector in general and HFCs in particular.

■ Company outlook - Strong triggers to drive growth, with resilient asset quality

Balance sheet strength, consistency, and quality of earnings continue to be the key differentiators for HDFC, which support long-term investments. HDFC is well capitalised and its book with high-quality granular individual loans make it comfortably placed. Given the market dominance of HDFC, we expect the leadership to sustain going forward, even as growth momentum in the housing market is encouraging. HDFC's strong operating metrics, supported by its industry's best credit rating, enable it to attract best rates and, hence, optimum cost of funds, which will be crucial supports for margins.

■ Valuation - We re-iterate Buy on HFDC with a SOTP based PT of Rs. 3,589

At CMP, HDFC trades at 3.9x of FY23E P/BV. HDFC has weathered and emerged as the strongest player among all large HFCs, especially during the pandemic period. Management was optimistic in terms of improving CE and asset quality. Individual non-performing loans seem to be restrained at 1%, barring Q1FY2022, which saw NPA at 1.37%. While non-individual loans are likely to take some more time to recover. On the disbursement front, the individual segment witnessed the highest-ever disbursals, while management indicated for a healthy pipeline for the non individual segment. We believe that the company would emerge as the key beneficiary of the favourable macro factors play- low interest rate regime, improved affordability, revival of demand for housing and stable property prices.

Peer Comparison

Company	CMP (Rs / Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
HDFC Ltd	2,846	514,396	39.5	35.3	2.9	2.7	12.9	13.1	2.4	2.3
LIC Housing Finance	395	21,681	10.8	5.3	1.0	0.8	9.0	17.0	0.8	1.4
Can Fin Homes	609	8,114	16.8	14.1	2.9	2.4	17.7	18.4	2.0	2.0

Source: Bloomberg; Sharekhan Research

About company

HDFC Limited is a major provider of finance for housing in India. The company (via its subsidiaries and group companies) is also present in banking, life and general insurance, asset management, venture capital, realty, education, deposits, and education loans via its formidable subsidiaries. As pioneers in housing mortgages, it is a brand name that has been characterised by trust, solidity, both financial and managerial, and sound principles. Established in 1977, HDFC has been able to maintain and set high standards in the housing finance sector.

Investment theme

HDFC has a strong portfolio of subsidiaries, which are market leaders in their own respective fields, which add to the value of the parent. By virtue of its strong market position, it has been able to withstand most market headwinds in the recent past. We believe balance sheet strength, consistency, and quality of earnings continue to be the key differentiators for HDFC and will help it tide over challenges. We believe HDFC is an attractive business franchise due to its strong retail book, a quality developer finance book (with sufficient cover), opportunity of quality market share gains (AUM growth), access to reasonably priced funds, and superior underwriting practices

Key Risks

Any prolonged economic slowdown may impact its growth and asset quality

Additional Data

Key management personnel

Mr. Deepak S. Parekh	Chairman
Mr. Keki M. Mistry	Vice Chairman & CEO
Ms. Renu S Karnad	Managing Director
Mr V Srinivasa Rangan	Executive Director and CFO
Mr. Mathew Joseph	Chief Risk Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Vanguard Group Inc/The	4.4
2	Invesco Ltd	4.3
3	Life Insurance Corp of India	4.0
4	JPMorgan Chase & Co	3.8
5	BlackRock Inc	3.6
6	SBI Funds Management Pvt Ltd	3.2
7	Republic of Singapore	3.0
8	FMR LLC	2.7
9	Baillie Gifford & Co	1.9
10	T Rowe Price Group LLC	1.6

Source: Bloomberg; as on Nov 2, 2021

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

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