Sharekhan by BNP PARIBAS

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HDFC Bank

Decent outcome considering transition period

Banks	Sharekhan code: HDFCBANK

Reco/View: Buy	↔	CMP: Rs. 1,531	Price Target: Rs. 1,900	↔

↑ 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		↔	

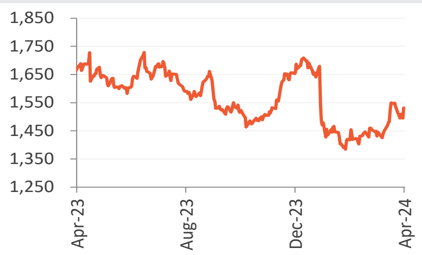
Company details

Market cap:	Rs. 11,63,315 cr
52-week high/low:	Rs. 1,758/1,363
NSE volume: (No of shares)	208.9 lakh
BSE code:	500180
NSE code:	HDFCBANK
Free float: (No of shares)	752 .1 cr

Shareholding (%)

Promoters	-
FII	47.8
DII	33.6
Others	18.6

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.0	3.5	0.5	-8.4
Relative to Sensex	6.4	1.3	-9.5	-30.4

Sharekhan Research, Bloomberg

Summary

- Results were broadly in line with expectations. The bank chose to set aside floating provisions against a large stake sale gain from HDFC Credila.
- Despite tight liquidity, the outcome on NIMs and deposit mobilisation were excellent.
- Asset growth has been recalibrated while managing the LCR and LDR. We believe this is a decent outcome considering the transition period.
- Stock trades at 2.0x/1.8x its FY2025E/FY2026E core BV estimates. We maintain Buy with an unchanged PT of Rs. 1,900. We remain assertive from medium to long term.

HDFC Bank reported broadly in-line performance in Q4FY24. Numbers on a y-o-y numbers are not comparable as this is the third quarter reported after the merger. NII at Rs. 29,077 crore (up 2% q-o-q) was in line with expectations driven by stable NIM of 3.4% (marginally improved by 4 bps q-o-q) and net loan growth of 1.6% q-o-q. Yields improved by 4 bps, while the cost of funds remained stable q-o-q. Core fee income was robust, up 15% q-o-q. Other income was higher at Rs. 10,176 crore as the bank sold its stake in HDFC Credila. Operating expenses rose by 13% q-o-q mainly due to one-time non-recurring item. Ex gratia of Rs. 1,500 crore was paid to employees to ensure attrition remains low. Cost to income ratio (ex. one off and stake sale gain) stood at 41.3% vs 40.3% q-o-q. PPoP was at Rs. 29,274 crore marginally above estimates, up 24% q-o-q. Core PPoP (Ex. one-offs & other income) was at Rs. 17,598 crore, up 6% q-o-q. Provision increased to Rs 13,512 crore (led by higher floating provisions) leading to PBT of Rs 15,763 crore (down 19% qoq), but due to tax reversal provisions, PAT growth was 1% q-o-q at Rs 16,512 crore, below our expectation of Rs 19,185 crore mainly led by higher floating provisions. The bank made a floating provision of Rs 10,900 crore. Core credit cost continued to remain lower at 42 bps vs 49 bps q-o-q. Gross advances grew by 2% q-o-q led by Commercial & rural banking (up 4% q-o-q). Retail loans grew by 3% q-o-q mainly driven by home loans. Corporate loans (ex. non-individual loans of erstwhile HDFC Ltd.) declined by ~2% q-o-q. Non-individual loans of erstwhile HDFC Ltd declined by 18% q-o-q. Deposit outpaced loan growth resulting into decrease in LDR to 104%. Deposit witnessed growth of 7.5% q-o-q, within which retail deposits grew by 6.9% and wholesale deposit grew by 10.9%. Liquidity coverage ratio was at 115% Vs 110% in Q3. GNPA was at 1.24% (-2 bps q-o-q) and NNPA at 0.33% (+2bps q-o-q). PCR at 74% vs 75% in Q3 Annualised slippage was 1.32% vs 1.27% q-o-q. Floating provisions & contingent provisions now are at 50 bps & 59 bps, respectively.

Key positives

- Retail deposit mobilisation was strong (up 7.5% q-o-q)
- Lower core credit cost sustained (~42 bps).
- Strong buffers - Floating provisions & contingent provisions now stands at 50 bps & 59 bps respectively.

Key negatives

- The bank is likely to have shortfall in meeting the PSL requirement on HDFC Ltd share of loans in Oct 2024 and thus it would have to ride inorganic path. This would result in additional cost, but it was not quantified by management.

Management Commentary

- The bank's key focus remains higher retail deposit mobilisation. The bank believes it can garner 15-20% incremental share in deposits without being aggressive on rates. Focus would be on customer service and product offerings.
- Run-down of high cost borrowings of HDFC Ltd is likely to happen from FY25 onwards.
- Incremental LDR would continue to be lower going forward and it endeavours to maintain NIMs at the current levels in near term and gradually improve over the medium term.

Our Call

Valuation: We maintain our Buy rating on the stock with an unchanged TP of Rs. 1,900: The stock trades at 2.0x/1.8x its FY2025E/FY2026E core BV estimates. We believe loan growth is expected to be in low mid-teens in the near term and deposit growth should outpace loan growth, which should bring the CD ratio to a normalised level gradually. FY25 would be yet another period of transition. The bank is confident of regaining its higher growth trajectory and NIMs once this transition period is completed. We retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 1,900 as downside risk appears to be minimal from hereon. Key monitorable: NIM progression and retail deposit mobilisation.

Key Risks

Slower retail deposit mobilisation; economic slowdown; tech outage

Valuation Rs cr

Particulars	FY22	FY23	FY24	FY25E	FY26E
Net Interest Income	72,010	86,842	1,08,532	1,33,174	1,50,289
Net profit	36,962	44,109	60,812	69,160	77,383
EPS (Rs.)	66.3	78.9	85.4	89.9	100.5
P/E (x)	20.2	17.0	15.7	14.9	13.3
P/BV (x)	3.1	2.7	2.3	2.0	1.8
RoE	16.7	17.0	16.9	14.6	14.2
RoA	1.9	1.9	2.0	1.8	1.8

Source: Company; Sharekhan estimates

Key result highlights

NIMs stable: NII at Rs. 29,077 crore (+2% q-o-q) was in line with expectations driven by stable NIM of 3.4% (marginally improved by 4bps q-o-q) and net loan growth of 1.6% q-o-q. Yields improved by 4 bps while cost of funds remained stable q-o-q. Yields are expected to remain stable if COF funds remain stable thus bank endeavors to maintain NIMs at the current levels in near term and gradually improve to 3.7% over the next 2 years. Margins are expected to improve gradually as high-cost wholesale funding of HDFC Ltd gets replaced with retail funding (CASA and retail deposits) and improving loan mix towards other retail high-yielding segments.

Asset quality remains pristine: Asset quality remained stable q-o-q with GNPA/NNPA ratios at 1.24%/0.33% vs. 1.26%/0.31% q-o-q. PCR stood at 74% vs. 75% q-o-q. Net slippages were at Rs. 2,800 crore vs. Rs. 2,500 crore q-o-q. The bank does not foresee any incremental pressure on asset quality. Core credit costs stood at 42 bps vs 49 bps q-o-q. Floating provisions & contingent provisions now stands at 50 bps and 59 bps of loans respectively. Additional floating provisions were created to bring more resiliency in the balance sheet.

Loan growth driven by retail and commercial banking: Gross advances grew by 2% q-o-q led by Commercial & rural banking (up 4% q-o-q). Retail loans grew by 3% q-o-q mainly driven by home loans. Corporate loans (ex. non-individual loans of erstwhile HDFC Ltd.) declined by ~2% q-o-q. Non-individual loans of the erstwhile HDFC Ltd declined by 18% q-o-q. Asset growth has been adjusted while managing liquidity and CD ratio. Also yields in corporate segment were lower than internal risk based threshold limit thus bank did not participate in Corporate loans. Deposits outpaced loan growth resulting in a decrease in LDR to 104%. Incremental LDR would continue to be lower going forward. LCR during the quarter was 115% versus 110% in the last quarter.

Strong deposit mobilisation: Deposits outpaced loan growth, rising 7.5% q-o-q, within which retail deposit grew by 6.9% and wholesale deposit grew by 10.9%. Retail deposits accounted for 84%. CASA ratio marginally improved to 38.2% versus 37.9% q-o-q. The bank's key focus remains higher retail deposit mobilisation. The bank believes it can garner 15-20% incremental share in deposits without being aggressive on rates. Focus would be on customer service and product offerings.

Branch expansion: The bank highlighted that its endeavor is to increase the distribution network but at the same time the focus would be on achieving increased productivity.

PSLC requirement: In connection with PSLC requirement, earlier RBI had allowed the bank to consider only one third of the outstanding HDFC Ltd loans in the first year of the merger. The remaining two-thirds of the portfolio of HDFC LTD was to be considered over the next two years equally. The bank is scaling up the Small/marginal farmer & weaker section segment gradually through rural banking, but there would be shortfall and threshold limit would not be met by organic means as ticket sizes are lower. Bank would also have to ride inorganic route in meeting the regulatory requirement. The impact cost of this was not quantified by the bank.

Results Rs cr

Particulars	Q4FY24	Q4FY23	Q3FY24	Y-o-Y %	Q-o-Q %
Interest Inc.	71,473	45,119	70,583	58.4%	1.3%
Interest Expenses	42,396	21,768	42,111	94.8%	0.7%
Net Interest Income	**29,077**	**23,352**	**28,471**	**24.5%**	**2.1%**
NIM (%)	3.44	4.30	3.40	-86 bps	4 bps
Core Fee Income	7,990	6,630	6,940	20.5%	15.1%
Other Income	10,176	2,101	4,197	384.3%	142.5%
Net Income	**47,243**	**32,083**	**39,608**	**47.3%**	**19.3%**
Employee Expenses	6,936	4,362	5,352	59.0%	29.6%
Other Opex	11,033	9,100	10,609	21.2%	4.0%
Total Opex	**17,969**	**13,462**	**15,961**	**33.5%**	**12.6%**
Cost to Income Ratio	38.0%	42.0%	40.3%		
Pre-Provision Profit	**29,274**	**18,621**	**23,647**	**57.2%**	**23.8%**
Provisions & Contingencies – Total	13,512	2,685	4,217	403.2%	220.4%
Profit Before Tax	**15,763**	**15,936**	**19,431**	**-1.1%**	**-18.9%**
Tax	-749	3,888	3,058	NM	NM
Effective Tax Rate	-5%	24%	16%		
Reported Profit	**16,512**	**12,047**	**16,373**	**37.1%**	**0.9%**
Basic EPS (Rs.)	21.7	21.6	21.6	0.6%	0.7%
Diluted EPS (Rs.)	21.7	21.5	21.5	0.8%	0.8%
RoA (%)	2.0	2.1	2.0		
Advances	24,84,862	16,00,586	24,46,076	55.2%	1.6%
Deposits	23,79,786	18,83,395	22,13,977	26.4%	7.5%
Gross NPA	31,173	18,019	31,012	73.0%	0.5%
Gross NPA Ratio (%)	1.24	1.12	1.26		
Net NPA	8,092	4,368	7,664	85.2%	5.6%
Net NPAs Ratio (%)	0.33	0.27	0.31		
PCR - Calculated	74.0%	75.8%	75.3%		

Source: Company, Sharekhan Research; Note: y-o-y numbers are not comparable

Outlook and Valuation

■ **Sector view - Deposit mobilisation to be in focus; banks with a superior liability franchise placed better:**

System-level credit offtake (Ex. HDFC Ltd) grew by ~16% y-o-y in the fortnight ending March 22, 2024, indicating loan growth has been strong and sustaining given distinct signs of improved macros, revival of private capex, and healthy demand. On the other hand, deposits rose by ~13%. The gap between advances and deposits growth has started to narrow. We are seeing strong traction in loan growth and overall deposit growth is also picking up. Margins are expected to remain under pressure due to lower CASA, higher deposits rates and inability to pass on rates on asset book. Overall asset-quality outlook is stable to positive for the sector. We believe banks with a robust capital base and strong retail deposit franchises are well-placed to capture growth opportunities.

■ **Company outlook - Strong execution track record**

Improvement in NIMs, strong retail deposit mobilisation resulting in the normalisation of CD ratio in turn leading to a sustainable loan growth path, building strong distribution, broadening customer base and enabling technology remain key monitorables in near to medium term. The bank has a good track record of strong execution capabilities, has consistently delivered superior performance, and its track record is unmatched across the sector. FY25 would be another period of transition and once this transition period is completed, growth and profitability trajectory should catch up with peers.

■ **Valuation - We maintain our Buy rating on the stock with an unchanged TP of Rs. 1,900**

The stock trades at 2.0x/1.8x its FY2025E/FY2026E core BV estimates. We believe loan growth is expected to be in low mid-teens in the near term and deposit growth should outpace loan growth, which should bring the CD ratio to a normalised level gradually. FY25 would be yet another period of transition. The bank is confident of regaining its higher growth trajectory and NIMs once this transition period is completed. We retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 1,900 as downside risk appears to be minimal from hereon. Key monitorable: NIM progression and retail deposit mobilisation.

Peer Comparison

Companies	CMP (Rs/Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY25E	FY26E	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
HDFC Bank	1,531	11,63,315	14.9	13.3	2.0	1.8	14.6	14.2	1.8	1.8
ICICI Bank	1,066	7,49,024	14.5	13.0	2.2	1.9	16.6	15.8	2.2	2.2
Axis Bank	1,030	3,17,796	11.4	10.2	1.7	1.5	16.1	15.4	1.8	1.8

Source: Company; Sharekhan Research

About company

HDFC Bank is the largest private sector bank with a pan-India presence. The bank has been designated by the Reserve Bank of India (RBI) as a domestic systemically important bank (D-SIB), underlining its importance in the financial system. The bank's loan book is well balanced between retail and wholesale loans. As a business entity, HDFC Bank continues to deliver steady performance with well-maintained margins and conservative asset-quality performance. HDFC Bank and HDFC Limited have successfully completed one of India's largest financial services mergers.

Investment theme

The merged entity is going through a transition period. The bank in past, has consistently reported healthy return ratios and earnings growth over the years across various credit/interest rate cycles and has been able to maintain its asset quality, which is indicative of its strong business franchise strength and leadership qualities. The merged entity is looking to work through the opportunities. The bank is confident of regaining its higher growth trajectory and NIMs once this transition period is completed.

Key Risks

Slower deposit mobilisation; economic slowdown; tech outage

Additional Data

Key management personnel

Sashidhar Jagdishan	Managing Director and CEO
Kaizad Bharucha	Deputy MD
Srinivasan Vaidyanathan	Chief Financial Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Funds Management Ltd	4.84
2	Life Insurance Corp of India	4.54
3	Vanguard Group Inc/The	3.10
4	FMR LLC	2.25
5	HDFC Asset Management Co Ltd	2.25
6	ICICI Prudential Asset Management	2.18
7	Republic of Singapore	2.03
8	BlackRock Inc	1.77
9	Capital Group Cos Inc/The	1.69
10	UTI Asset Management Co Ltd	1.68

Source: Bloomberg

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

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