

January 25, 2016

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Rating	BUY
Price	Rs1,041
Target Price	Rs1,300
Implied Upside	24.9%
Sensex	24,486
Nifty	7,436

(Prices as on January 25, 2016)
Trading data

Market Cap. (Rs bn)	2,609.6
Shares o/s (m)	2,506.5
3M Avg. Daily value (Rs m)	1386.3

Major shareholders

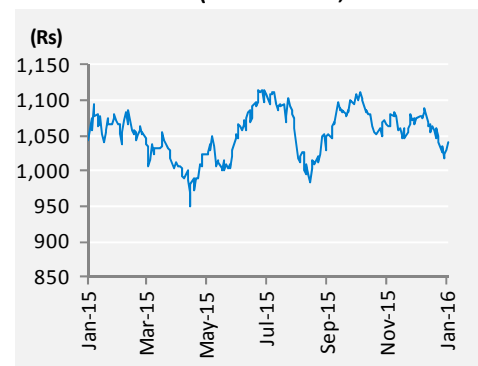
Promoters	21.60%
Foreign	39.78%
Domestic Inst.	13.73%
Public & Other	25.08%

Stock Performance

(%)	1M	6M	12M
Absolute	(3.1)	(6.0)	(0.2)
Relative	2.2	6.9	16.2

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2017	60.2	61.4	-1.9
2018	75.2	76.3	-1.4

Price Performance (RIC:HDBK.BO, BB:HDFCB IN)


Source: Bloomberg

HDFCB reported steady quarter as loan growth continues to report healthy traction while net earnings grew 20% YoY on expected lines. Revenue growth was broadly in-line though margin expansion by 10bp QoQ surprised positively, despite bank cutting base rate sharply (40bp in past four months). GNPL/NNPL increased by 11%/21% QoQ to Rs42.5 bn and Rs12.6bn respectively however there are no pending accounts to take care of as part of RBI's balance sheet clean up drive. HDFCB remains one of the top-picks for us and we maintain 'BUY' with a revised PT of Rs1,300 (from Rs1,200) based on 3.8x Sep-2017E ABV.

- Revenue growth broadly in-line:** HDFCB delivered ~21% YoY growth in total revenues at Rs99.4 bn (PLe: Rs100.7 bn) led by steady 24% YoY growth in NII though other income growth remains slightly tepid (weaker third-party income) at 13% YoY. Core other income also grew similar 21% YoY. NII growth was boosted by 10bp QoQ expansion in margins despite bank base rate cut. HDFCB opened 54 branches and added 1,203 employees during the quarter. Over past one year HDFCB has added ~8,400 employees yet commendably the cost-ratios remain stable over 9MFY16 (down 310bp QoQ for 3QFY16).
- Loan growth remains healthy; wholesale – retail mix remains stable:** Overall loan growth stood at ~26% YoY (4.3% QoQ) led by healthy growth in both retail and wholesale portfolio. Within wholesale, growth was largely on account of working capital loans while growth in the retail portfolio was led by strong traction in CV loans, personal loans, two-wheeler, credit cards and other retail segment. The mix of retail increased marginally to 49.2%. HDFCB indicated healthy growth trends on underlying improvement in product segments where it is gaining market share and benefitting from increased distribution presence.
- Asset quality deteriorates a little; outlook stable:** Asset quality reported slight blip with GNPL/NNPL increasing by 11%/21% QoQ to Rs42.5 bn and Rs12.6bn respectively however there are no pending accounts to take care of as part of RBI's balance sheet clean up drive. Coverage ratio also thus declined by 250bp QoQ though floating provisions remain stable at ~Rs16bn. O/s restructured assets remain tiny at 0.1% of total loans. HDFCB remains one of our top-picks and we revise PT to Rs1,300 (from Rs1,200) based on 3.8x Sep-2017E ABV.

Key financials (Y/e March)	2015	2016E	2017E	2018E
Net interest income	223,957	273,105	332,998	402,477
Growth (%)	21.2	21.9	21.9	20.9
Operating profit	174,045	210,469	262,597	328,323
PAT	102,159	122,744	150,814	188,497
EPS (Rs)	41.7	49.0	60.2	75.2
Growth (%)	17.4	17.6	22.9	25.0
Net DPS (Rs)	8.0	9.0	10.5	12.0

Profitability & Valuation	2015	2016E	2017E	2018E
NIM (%)	4.14	4.18	4.19	4.15
RoAE (%)	19.4	18.4	19.5	20.7
RoAA (%)	1.89	1.88	1.90	1.95
P / BV (x)	4.2	3.6	3.1	2.6
P / ABV (x)	4.5	3.9	3.3	2.8
PE (x)	25.0	21.3	17.3	13.8
Net dividend yield (%)	0.8	0.9	1.0	1.2

Source: Company Data; PL Research

Exhibit 1: Q3FY16 Results – Display of strong performance continues

(Rs m)	Q3FY16	Q3FY15	YoY gr. (%)	Q2FY16	QoQ gr. (%)
Interest income	154,111	123,958	24.3	147,725	4.3
Interest Expended	83,426	66,959	24.6	80,916	3.1
Net interest income (NII)	70,685	56,999	24.0	66,809	5.8
- Treasury income	3,279	2,655	23.5	1,624	101.9
Other income	28,722	25,349	13.3	25,518	12.6
Total income	99,407	82,348	20.7	92,327	7.7
Operating expenses	42,048	34,563	21.7	41,898	0.4
-Staff expenses	14,313	11,325	26.4	14,140	1.2
-Other expenses	27,736	23,238	19.4	27,758	(0.1)
Operating profit	57,359	47,786	20.0	50,429	13.7
Core operating profit	54,080	45,131	19.8	48,805	10.8
Total provisions	6,539	5,604	16.7	6,813	(4.0)
Profit before tax	50,820	42,181	20.5	43,616	16.5
Tax	17,251	14,236	21.2	14,922	15.6
Profit after tax	33,568	27,945	20.1	28,695	17.0
Balance sheet (Rs m)					
Deposits	5,239,968	4,141,283	26.5	5,069,087	3.4
Advances	4,363,644	3,470,880	25.7	4,185,410	4.3
Gross NPL (Rs m)	42,552	34,679	22.7	38,278	11.2
Net NPL (Rs m)	12,606	9,037	39.5	10,377	21.5
Restructured Assets (Rs m)	4,406	3,506	25.7	4,224	4.3
Profitability ratios					
Yield on Advances	10.7	11.3	(58)	11.2	(43)
Cost of Funds	5.8	6.1	(23)	6.1	(30)
NIM	4.3	4.4	(10)	4.2	10
RoaA	2.0	2.1	(15)	1.8	16
RoaE	19.1	22.3	(313)	17.6	152
Asset Quality					
Gross NPL ratio	1.0	1.0	(3)	0.9	6
Net NPL ratio	0.3	0.3	(1)	0.3	4
Coverage ratio	70.4	73.9	(357)	72.9	(252)
Rest. assets/ Total adv.	0.1	0.1	(0)	0.1	0
Business & Other Ratios					
Low-cost deposit mix	40.0	40.9	(90)	40.0	-
Cost-income ratio	42.3	42.0	33	45.4	(308)
Non int. inc / total income	28.9	30.8	(189)	27.6	125
Credit deposit ratio	83.3	83.8	(54)	82.6	71
CAR	15.9	15.7	20	15.5	40
Tier-I	13.2	12.0	123	12.8	40

Source: Company Data, PL Research

Key Q3FY16 Concall Highlights:

Balance sheet & Outlook

- **Loan book** – Urban market continues to see higher competition & pricing pressure in urban markets than SU-RU markets. **Overseas operations** – Currently of the total loans book, 7.5% is overseas loans.
- **Retail loans** – Higher focus on retail by competitors has put pressure on pricing but better brand & reach has helped gained market share among products. Volume growth has picked in 2W, CV (as were slow growing in in FY15), also have seen other products continuing to do well as well. **Home loans** – Have bought over Rs12bn of home loans which also include non-originated, this could be higher going ahead as historically have been buying back PSL related loans. **Car loans** – 80% mix of new vehicle is the trend in origination of car loans.
- **Corporate loans** – Loan growth pre-dominantly are on back of short term working capital requirement and lower of term loans. Have seen some re-financing deals during the quarter.

Margins

- Margins have been in the range of 4-4.3% and likely to continue remain the same going ahead. Transition on MCLR will be easy for the bank with minor issues, but will be difficult to assess the MCLR impact currently as rates will be based on tenor based linking.

Fee income/other income

- Fee growth was sluggish on some slowdown in TPD fees on mix change in products & some regulatory changes like commission up-fronting. Also, due to festive season certain fees were waived off which also impacted fee growth.

Opex/Branches/Capacity

- Other opex has been seeing higher growth **(1)** higher branch additions especially in metro which are expensive than SU-RU. Employee count additions have been higher on higher product introduction in newer branches which requires higher customer facing activity.
- **Outlook** – Would likely see some moderation in branch additions going ahead and would likely not see the rate of additions seen in last few quarters.

Asset Quality

- **Slippages** – Bank witnessed slippages of Rs15.5bn (net slippage: Rs 0.42bn). Have seen slippages from some pockets of Agri & SME. Also, some slippages were seen from credit card receivables as it has under gone some regulatory changes on recognition
- **Currently holding Rs16bn as floating provisions (unchanged from last quarter).** Also, currently do not have any SDR asset or 5/25 refinancing
- **Outlook** – Do not any see any corporate falling into NPA in near term.

Others

- **Capital consumption** – Have seen increase of one-off release of provisions by 40bps in CAR on revised regulatory guidelines on affordable housing and capital released on securitization assets. Bank will be likely facing 50-60bps burn of capital burn per annum.

Overall loan growth of 26% continues to be strong mainly from retail book.

Retail loan book growth was led by high growth in Car loans, 2W which witnessed high volume especially in back ground of festive season, while regular retail segments like personal loans & credit card continue to lead growth

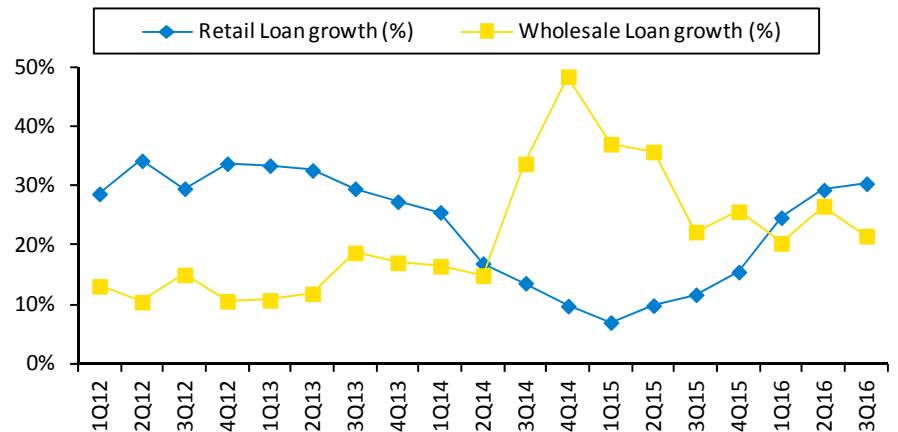
Trends in CV loans soften slightly; SME segment saw some decline in growth

Exhibit 2: Retail loan book leads growth; share of retail to wholesale in total loans now close to 50:50

Loan Composition (Rs m)	Q3FY16	Q3FY15	YoY gr. (%)	Q2FY16	QoQ gr. (%)
Car Loans	497,550	400,140	24.3	460,090	8.1
CV loans	149,500	132,120	13.2	147,990	1.0
2 wheeler loans	52,130	39,590	31.7	47,300	10.2
Sub-total - Auto Loans	699,180	571,850	22.3	655,380	6.7
Personal loans	350,710	248,040	41.4	318,810	10.0
Business banking	269,360	213,400	26.2	272,880	(1.3)
Loan against shares	11,290	11,940	(5.4)	10,780	4.7
Credit Cards	196,890	153,640	28.2	180,000	9.4
Home loans	284,190	199,770	42.3	284,380	(0.1)
Gold Loans	43,610	39,010	11.8	43,090	1.2
Other Retail	293,490	210,690	39.3	278,780	5.3
Retail Loans	2,148,720	1,648,340	30.4	2,044,100	5.1
Non Retail Loans	2,214,924	1,822,540	21.5	2,141,310	3.4
Total Advances	4,363,644	3,470,880	25.7	4,185,410	4.3

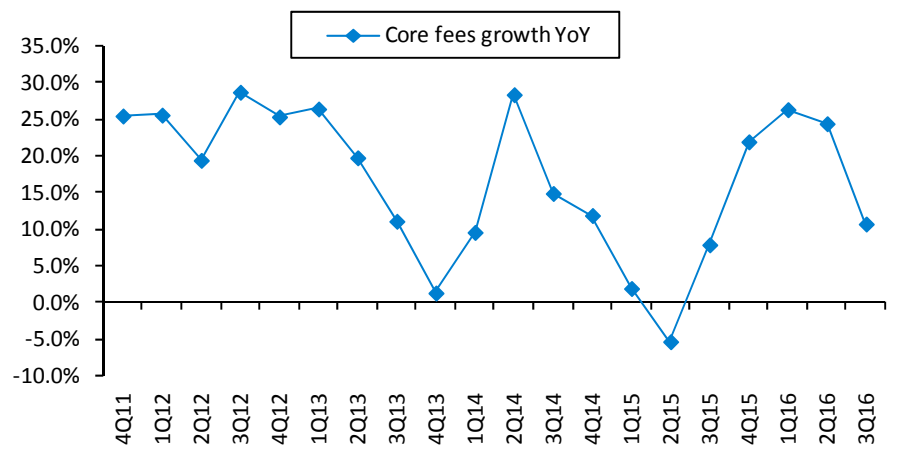
Source: Company Data, PL Research

Exhibit 3: Retail loans growth have been outpacing wholesale loans from past few quarters



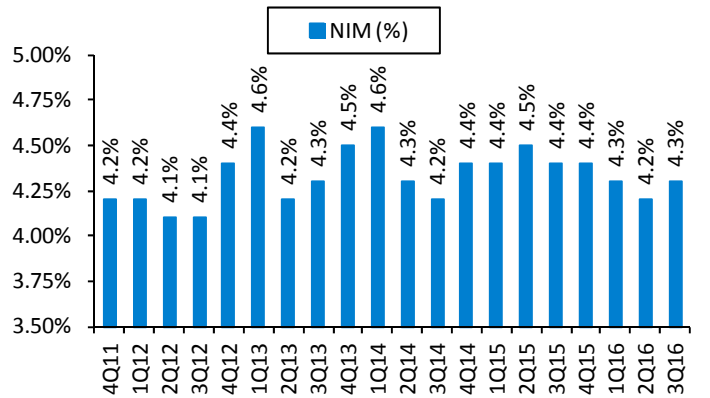
Source: Company Data, PL Research

Exhibit 4: Core fees growth was sluggish on some weakness in TPD fees



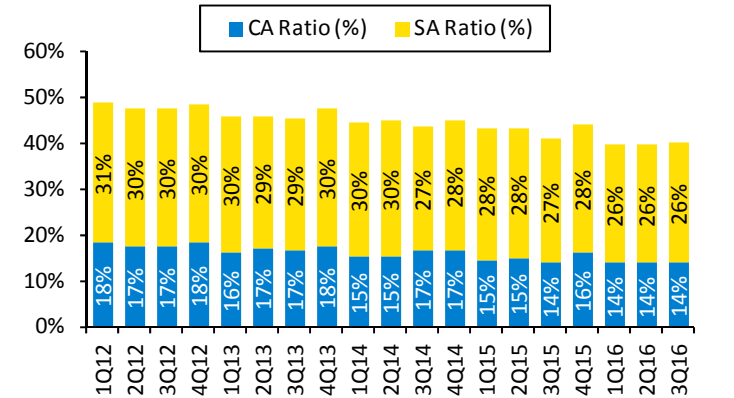
Source: Company Data, PL Research

Exhibit 5: Margins improve sequentially as short term loans re-price on sharp base rate cut seen in Q1FY16 quarter

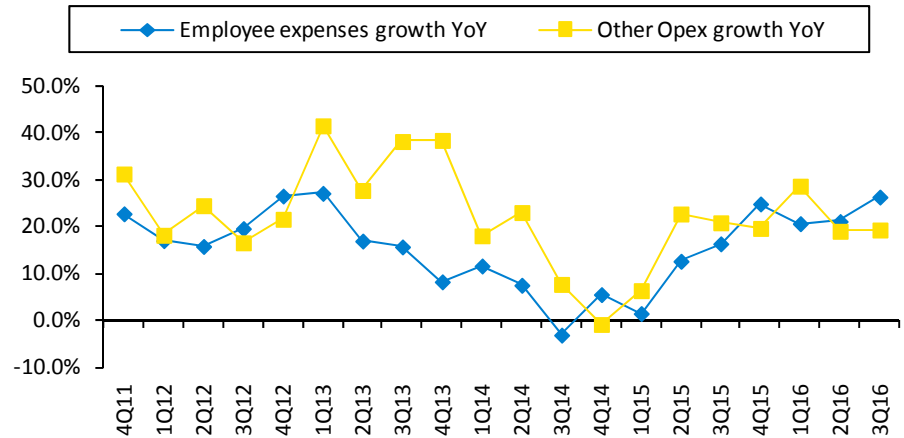


Source: Company Data, PL Research

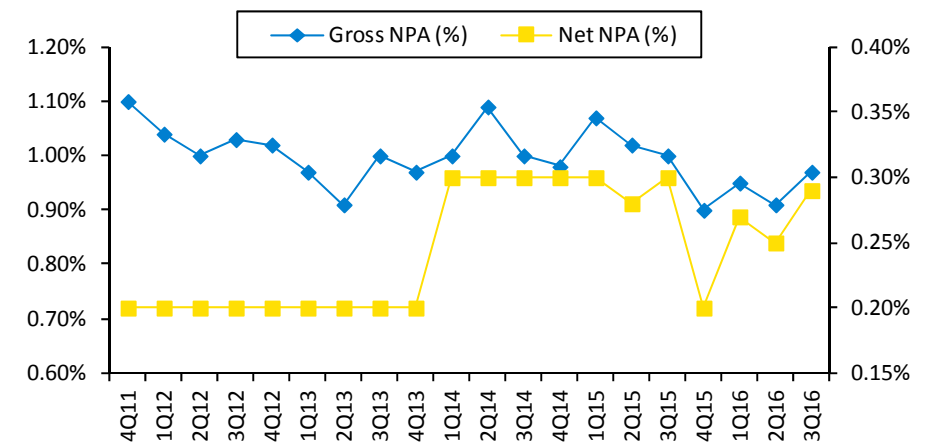
Exhibit 6: CASA ratio continues to remain stable at 40%; CA profile sees robust growth in the quarter



Source: Company Data, PL Research

Exhibit 7: Opex growth continues to remain high as bank continues to add high employee count and open branches in metro areas


Source: Company Data, PL Research

Exhibit 8: Asset quality some slippages from Agri & SME but overall ratios remain robust


Source: Company Data, PL Research

Exhibit 9: Change in earnings estimates table – We adjust our business growth, fees and opex assumptions leading to slight cut in earnings

Rs (mn)	Old estimates		Revised estimates		% change		New
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E	
Net interest income	270,554	329,540	273,105	332,998	0.9	1.0	402,477
Operating profit	214,436	266,674	210,469	262,597	(1.8)	(1.5)	328,323
Net profit	125,431	155,802	122,744	150,814	(2.1)	(3.2)	188,498
EPS, Rs.	50.0	62.2	49.0	60.2	(2.1)	(3.2)	75.2
ABVPS, Rs.	271.2	317.4	268.3	313.8	(1.1)	(1.1)	370.2
Price target, Rs.	1,200		1,300				
Recommendation	BUY		BUY				

Source: Company Data, PL Research

Exhibit 10: We increase HDFCB TP to Rs1,300 (from Rs1,200) as we roll our valuations to Sep-17 with a multiple of 3.8x and retain as our top pick in the sector

PT calculation and upside	
Fair price – EVA	1,283
Fair price - P/ABV	1,316
Average of the two	1,300
Target P/ABV	3.8
Target P/E	19.2
Current price, Rs	1041
Upside (%)	24.8%
Dividend yield (%)	1.0%
Total return (%)	25.9%

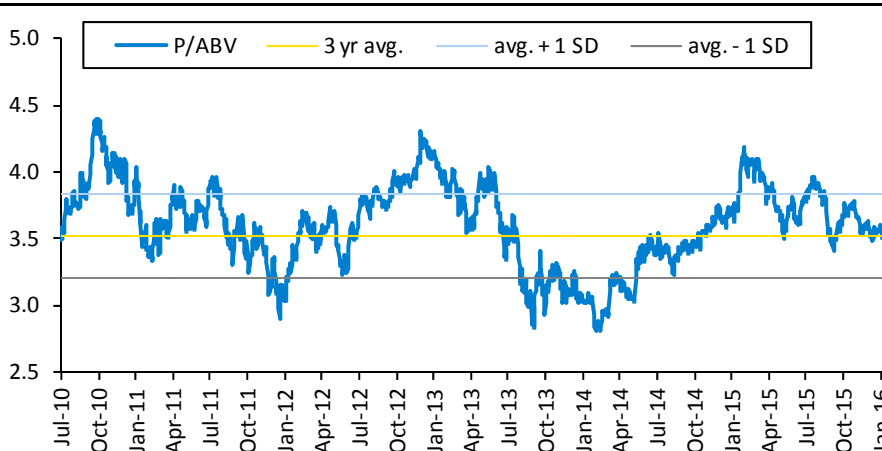
Source: Company Data, PL Research

Exhibit 11: Return ratios to improve on high loan growth with increasing market share, controlled credit cost and likely waning of opex cost

RoA decomposition	FY12	FY13	FY14	FY15	FY16E	FY17E	FY18E
Interest income	9.06	9.50	9.22	8.96	9.07	8.95	8.89
Interest expenses	4.87	5.22	5.08	4.82	4.87	4.73	4.68
Net interest income	4.19	4.28	4.14	4.14	4.19	4.22	4.21
Treasury income	0.38	0.28	0.32	0.29	0.32	0.32	0.33
Other Inc. from operations	1.50	1.57	1.46	1.38	1.28	1.24	1.18
Total income	6.07	6.14	5.92	5.80	5.80	5.78	5.71
Employee expenses	1.11	1.07	0.94	0.88	0.82	0.77	0.68
Other operating expenses	1.91	1.97	1.76	1.71	1.65	1.60	1.51
Operating profit	3.05	3.10	3.22	3.22	3.32	3.41	3.52
Tax	0.76	0.82	0.96	0.94	0.96	0.98	1.01
Loan loss provisions	0.61	0.45	0.36	0.38	0.42	0.44	0.45
Net profit	1.68	1.82	1.90	1.89	1.94	1.99	2.06

Source: Company Data, PL Research

Exhibit 12: HDFCB historical 1 year forward P/ABV trend



Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2015	2016E	2017E	2018E
Int. Earned from Adv.	371,808	452,558	550,842	666,788
Int. Earned from Inv.	107,056	133,556	152,146	181,623
Others	5,835	5,762	7,530	9,245
Total Interest Income	484,699	591,876	710,518	857,656
Interest expense	260,742	318,772	377,520	455,180
NII	223,957	273,105	332,998	402,477
Growth (%)	21.2	21.9	21.9	20.9
Treasury Income	5,260	—	—	—
NTNII	84,704	104,538	123,354	145,558
Non Interest Income	89,964	104,538	123,354	145,558
Total Income	574,663	696,414	833,872	1,003,214
Growth (%)	17.1	21.2	19.7	20.3
Operating Expense	139,875	167,173	193,755	219,712
Operating Profit	174,045	210,469	262,597	328,323
Growth (%)	21.2	20.9	24.8	25.0
NPA Provisions	17,236	22,832	30,046	37,927
Investment Provisions	(38)	(34)	(31)	(28)
Total Provisions	20,758	24,494	34,091	42,720
PBT	153,287	185,975	228,506	285,603
Tax Provisions	51,128	63,232	77,692	97,106
Effective Tax Rate (%)	33.4	34.0	34.0	34.0
PAT	102,159	122,744	150,814	188,497
Growth (%)	20.5	20.1	22.9	25.0

Balance Sheet (Rs m)

Y/e March	2015	2016E	2017E	2018E
Par Value	2	2	2	2
No. of equity shares	2,506	2,506	2,506	2,506
Equity	5,013	5,013	5,013	5,013
Networth	620,094	715,687	834,825	987,122
Adj. Networth	611,131	702,957	823,451	972,402
Deposits	4,507,956	5,504,215	6,786,697	8,306,917
Growth (%)	22.7	22.1	23.3	22.4
Low Cost deposits	1,984,921	2,520,930	3,162,601	3,912,558
% of total deposits	44.0	45.8	46.6	47.1
Total Liabilities	5,905,031	7,154,513	8,742,533	10,636,486
Net Advances	3,654,950	4,499,244	5,516,073	6,718,577
Growth (%)	20.6	23.1	22.6	21.8
Investments	1,664,599	1,820,904	2,201,301	2,663,361
Total Assets	5,905,031	7,154,513	8,742,533	10,636,486

Source: Company Data, PL Research.

Quarterly Financials (Rs m)

Y/e March	Q4FY15	Q1FY16	Q2FY16	Q3FY16
Interest Income	130,064	140,411	147,725	154,111
Interest Expense	69,932	76,523	80,916	83,426
Net Interest Income	60,132	63,888	66,809	70,685
Non Interest Income	25,638	24,619	25,518	28,722
CEB	18,348	17,130	18,689	20,048
Treasury	1,961	1,259	1,624	3,279
Net Total Income	85,769	88,507	92,327	99,407
Operating Expenses	38,550	40,008	41,898	42,048
Employee Expenses	13,256	13,590	14,140	14,313
Other Expenses	25,294	26,418	27,758	27,736
Operating Profit	47,220	48,499	50,429	57,359
Core Operating Profit	45,259	47,240	48,805	54,080
Provisions	5,767	7,280	6,813	6,539
Loan loss provisions	4,248	5,575	4,844	6,015
Investment Depreciation	—	—	—	—
Profit before tax	41,453	41,219	43,616	50,820
Tax	13,384	14,262	14,922	17,251
PAT before EO	28,069	26,957	28,695	33,568
Extraordinary item	—	—	—	—
PAT	28,069	26,957	28,695	33,568

Key Ratios

Y/e March	2015	2016E	2017E	2018E
CMP (Rs)	1,041	1,041	1,041	1,041
Equity Shrs. Os. (m)	2,506	2,506	2,506	2,506
Market Cap (Rs m)	2,609,638	2,609,638	2,609,638	2,609,638
M/Cap to AUM (%)	44.2	36.5	29.8	24.5
EPS (Rs)	41.7	49.0	60.2	75.2
Book Value (Rs)	247	286	333	394
Adj. BV (100%) (Rs)	233	268	314	370
P/E (x)	25.0	21.3	17.3	13.8
P/BV (x)	4.2	3.6	3.1	2.6
P/ABV (x)	4.5	3.9	3.3	2.8
DPS (Rs)	8.0	9.0	10.5	12.0
Dividend Yield (%)	0.8	0.9	1.0	1.2

Profitability (%)

Y/e March	2015	2016E	2017E	2018E
NIM	4.1	4.2	4.2	4.2
RoAA	1.9	1.9	1.9	1.9
RoAE	19.4	18.4	19.5	20.7

Efficiency

Y/e March	2015	2016E	2017E	2018E
Cost-Income Ratio (%)	44.6	44.3	42.5	40.1
C-D Ratio (%)	81.1	81.7	81.3	80.9
Business per Emp. (Rs m)	112	128	143	159
Profit per Emp. (Rs lacs)	14.0	15.7	17.6	20.0
Business per Branch (Rs m)	659	721	807	895
Profit per Branch (Rs m)	8	9	10	11

Asset Quality

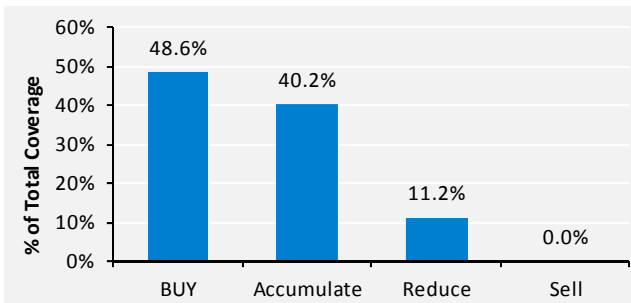
Y/e March	2015	2016E	2017E	2018E
Gross NPAs (Rs m)	34,384	42,565	48,825	59,995
Net NPAs (Rs m)	8,963	12,730	11,373	14,720
Gr. NPAs to Gross Adv. (%)	0.9	0.9	0.9	0.9
Net NPAs to Net Adv. (%)	0.2	0.3	0.2	0.2
NPA Coverage (%)	73.9	70.1	76.7	75.5

Source: Company Data, PL Research.

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BUY	:	Over 15% Outperformance to Sensex over 12-months
Accumulate	:	Outperformance to Sensex over 12-months
Reduce	:	Underperformance to Sensex over 12-months
Sell	:	Over 15% underperformance to Sensex over 12-months
Trading Buy	:	Over 10% absolute upside in 1-month
Trading Sell	:	Over 10% absolute decline in 1-month
Not Rated (NR)	:	No specific call on the stock
Under Review (UR)	:	Rating likely to change shortly

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