

HDFC Bank

Rs 485

All around strong performance

HOLD

KRChoksey
 INTEGRATED FINANCIAL SOLUTIONS

HDFC Bank reported robust PAT of Rs1,430 crore growing 31.4% y-o-y and 19.2% q-o-q, in line with our expectation and market consensus. NII growth moderated to 12.2% y-o-y & 5.8% q-o-q led by loan growth 22.1% y-o-y and steady NIMs. Fee income saw good traction, up 19.6% y-o-y and 14.1% q-o-q. Cost to income ratio declined 128bps q-o-q to 47.6% due to improvement in operating efficiency. Provisions were down 10.1% q-o-q to Rs329 crore boosted the bottom-line. Broad asset quality remained strong as absolute gross NPAs went up only 6.6% q-o-q with provision coverage of 80.3% in a challenging macro environment. Loan book growth and deposit growth were 3.1% q-o-q and 0.80% q-o-q, resulted into 185bps increase in CD ratio positively impacted NIMs. CASA ratio remained at healthy levels of 47.7% (37bps up q-o-q). Maintain HOLD.

Moderate NII growth: NII growth slowed down to 12.2% y-o-y & 5.8% q-o-q led by led by asset growth and steady NIMs at 4.1%. On sequential basis, contraction in corporate loan book, higher growth in high yield retail loan book led to 34bps improvement in loan yields while cost of funds increased slower pace by 20bps q-o-q to 6.41%. NIM remained stable q-o-q to 4.1% reflecting improvement competitive landscape. We expect NII to grow 20.5% over FY11-FY13e driven by 23.5% CAGR in loan book and steady NIMs.

Strong momentum in core fee & forex income: Non-interest income accelerated 25.9% y-o-y & 17.2% q-o-q to Rs 1,420 crore against Rs 1,128 crore a year ago. Healthy fee income growth and strong forex income continued to drive non-interest income contributing 33% of operating income. Fee income grew 19.6% y-o-y and 14.1% q-o-q driven by retail businesses. The bank incurred a trading loss of Rs 82 crore against Rs 31 crore trading loss a year ago, dented the profitability.

Asset quality remains fairly strong – Broad asset quality continued to be fairly strong as gross NPA increased 6.6% q-o-q basis to Rs 2,021 crore which is equivalent to 1.0% of gross advances. Net NPAs stood at 0.2% with superior coverage ratio of 80.3%. Quarterly trend suggests that credit costs are lower than normalized levels due to better than expected portfolio behavior, so we believe credit cost is likely to revert back to normalized levels medium term. We are building in 65bps & 80bps credit costs in FY12 and FY13 respectively against 53bps in FY11.

Valuation & Recommendation

HDFC Bank reported excellent operating performance in tough macro environment. Strong core earnings growth, robust fee income growth, steady margins, lower provisions, strong asset quality and stable CASA ratio were key positives from the numbers. Strong growth in retail loan book (largely fixed rate loan book) in last few quarters coupled with beginning of rate easing cycle would augur well for NIMs and NII growth – key catalyst going forward. We expect HDFC Bank to deliver 26.9% CAGR in net earnings over FY11-13e, aided by NII growth, steady fee income growth. At Rs 485 the stock is trading at 3.4x FY13e book and 17.8x FY13e earnings, reflecting strong fundamentals. We have revised upward earnings estimate by 1.6% & 5.6% in FY12 and FY13 respectively factoring higher fee income growth and lower credit costs. **We maintain our HOLD rating on the stock with revised target price of Rs540.**

Key Financials

Rs in crore	FY10	FY11	FY12E	FY13E
Net Interest Income	8,387	10,543	12,211	15,320
Pre Provision Profit	6,605	7,725	8,988	11,309
Net Profit	3,124	3,926	5,180	6,320
EPS	13.7	16.9	22.3	27.2
BVPS	94	109	126	147
ABVPS	92	108	124	144
P/E	35.5	28.7	21.8	17.8
P/ABV	5.3	4.5	3.9	3.4

Source: Company, KRChoksey Research

Target Price (Rs): 540

Potential Upside : 11.3%

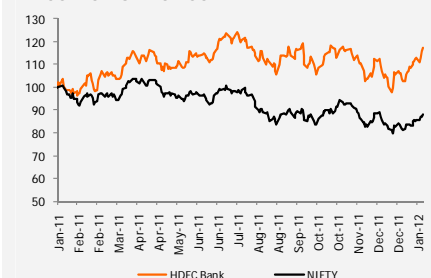
Previous TP (Rs): 510

Market Data	
Eq. sh. O/S (Cr)	234.1
MCAP (Rs crs)	1.13,975
52 Wk H/L (Rs)	519/396
Avg Vol (3m avg)	33,65,259
Fee float (%)	76.8%
Face Value (Rs)	2
Bloomberg Code	HDFCB IN

Market Info:

SENSEX	16,664
NIFTY	5,018

Price Performance



Share Holding pattern (%)

Particulars	Dec-11	Sep-11	Chg (%)
Promoters	23.2	23.2	0.0
FIIs	29.7	29.3	0.4
Institutions	11.0	11.0	0.0
Others	36.5	36.5	0.0
Total	100	100	

Source: BSE

Analysts

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Moderate NII growth

Net interest income slowed down 12.2% y-o-y & 5.8% q-o-q to Rs3,116 led by loan book growth 22% y-o-y and steady NIMs. Net interest margin (calc) saw uptick of 4bps q-o-q due to outpacing asset yields to cost of funds. Contraction in corporate loan book, higher growth in retail assets and improvement in CD ratio led to 34bps increase in loan yields. Cost of funds increased slower pace 20bps q-o-q due to run down of wholesale deposits. NIM remained stable q-o-q to 4.1% reflecting improvement competitive landscape. We expect NII to grow 20.5% over FY11-FY13e driven by 23.5% CAGR in loan book and steady NIMs.

Exhibit : 1 Loan and NII growth Trend

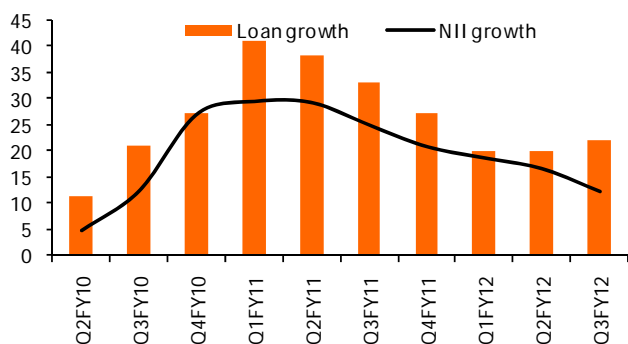
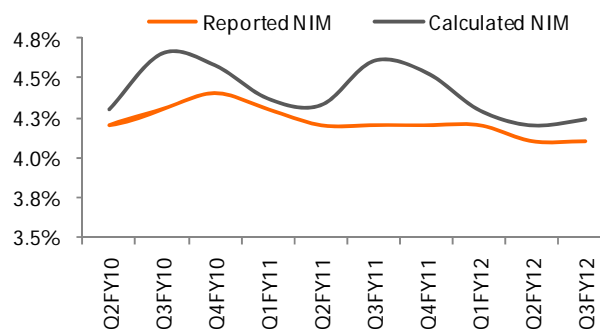


Exhibit : 2 Strong & stable Net interest margin



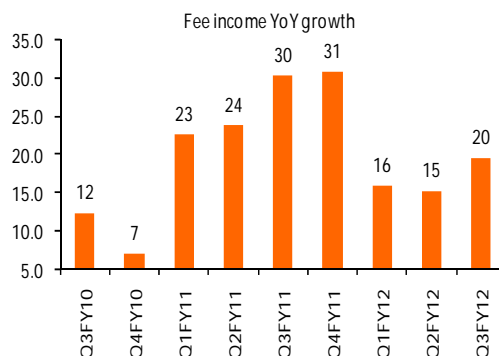
Source: Company, KRChoksey Research

Strong momentum in core fee & forex income

Non- interest income accelerated 25.9% y-o-y & 17.2% q-o-q to Rs 1,420 crore against Rs 1128 crore a year ago. Stronger fee income growth and Robust in forex profits continued to drive non-interest income contributing 33% of operating income. Fee income grew 19.6% y-o-y and 14.1% q-o-q driven by retail and corporate businesses. Retail and corporate businesses contribute 80% & 20% respectively to total core fee income. Third party distribution fee growth was negative due to lower commission on incremental financial products sales. However, there has been strong traction in LC, guarantee and business banking driven fee income during the quarter. The bank incurred a trading loss of only Rs 81 crore against Rs 31 crore trading loss a year ago largely attributable MTM hit on bond portfolio, dented core earnings growth during the quarter. We are factoring in 18.0% CAGR in fee income over FY11-FY13.

Exhibit : 3 Non- interest income growth

(Rs crore)	Q3FY12	Q2FY12	Q3FY11	q-o-q	y-o-y
Fee income	1128	988	943	14.1%	19.6%
Treasury Income	-82	-1	-31	-	-
Forex Trans	366	218	217	67.7%	68.6%
Non- Interest Income	1420	1212	1128	17.2%	25.9%

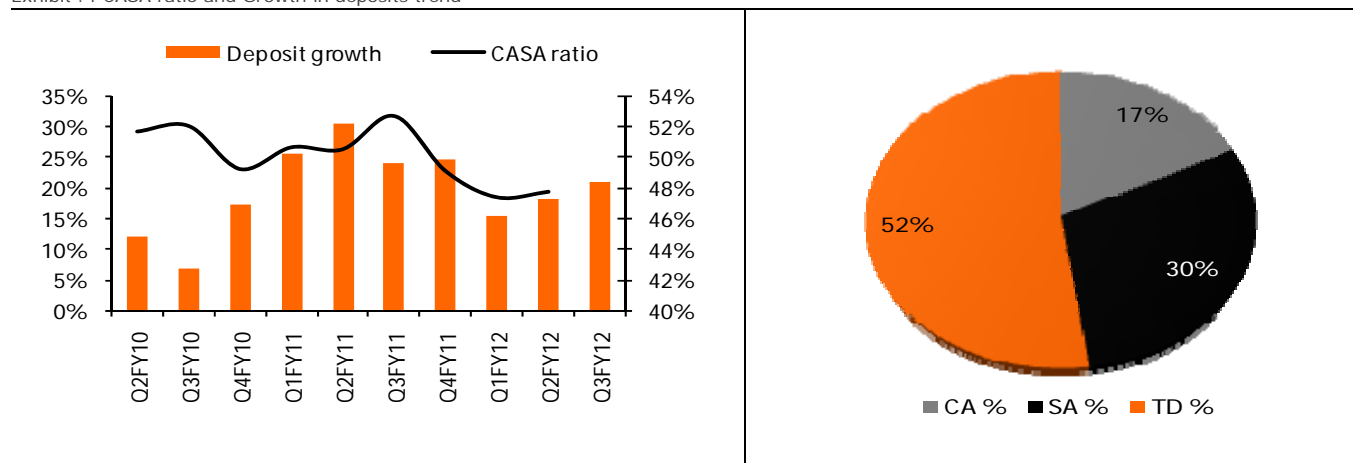


Source: Company, KRChoksey Research

Tepid deposit growth due to run down of wholesale deposits

Deposits grew at 21.0% y-o-y and 0.8% on q-o-q basis to Rs 2,32,508 crore. Normalized Current account deposits (excluding one off floats) up by 1.0% q-o-q against decline in current deposits at industry level. Savings deposits continued to show healthy momentum, up 15.2% y-o-y and 1.9% q-o-q despite of contraction in demand deposits at system level and de-regulation of saving bank deposits. Saving customer acquisition run rate remained stable q-o-q reflecting superior saving bank deposit franchise. The bank cautiously decided run down of wholesale deposits and corporate loan book due to unfavorable pricing and higher risk levels. Wholesale deposits and corporate loan book down by Rs6000 crore and Rs1668 crore respectively. The deposit mix between wholesale and retail deposits remained stable at 30% & 70% respectively. We expect newly open branches and seasonal factors will start contribute to mobilize higher CASA deposits in Q4FY12. We expect deposits to grow 23.0% CAGR over FY11-FY13

Exhibit : 4 CASA ratio and Growth in deposits trend



Source: Company, KRChoksey Research

Healthy loan book growth at 22.1% y-o-y & 3.1% q-o-q led by retail loan book

Loan book grew 22.1% y-o-y and 3.1% q-o-q driven by retail loan book which grew 29.5% y-o-y & 8.0% q-o-q. CD ratio improved 185bps q-o-q to 83.6% positively impacted NIMs. The bank witnessed strong growth in Personal loan (9.2% q-o-q), Commercial vehicles loans (11.1% q-o-q), two wheelers (10.7% q-o-q) and credit cards (10.3% q-o-q), resulted into strong growth in retail loan book during the quarter. In terms loan mix, Retail loan book and corporate loan book stood at 52% & 48% respectively. The management expects retail loan will continue to grow faster than wholesale loan book and uptick in wholesale loans is largely depend on improvement in pricing environment and risk levels. We expect loan book to grow at 23.5% CAGR over FY11-FY13.

Exhibit : 5 Advances growth Trend

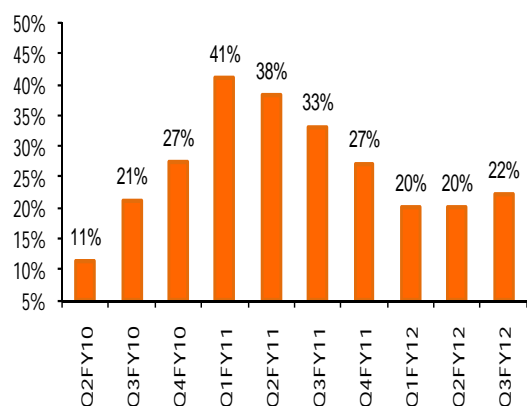


Exhibit 6: Advances growth Trend

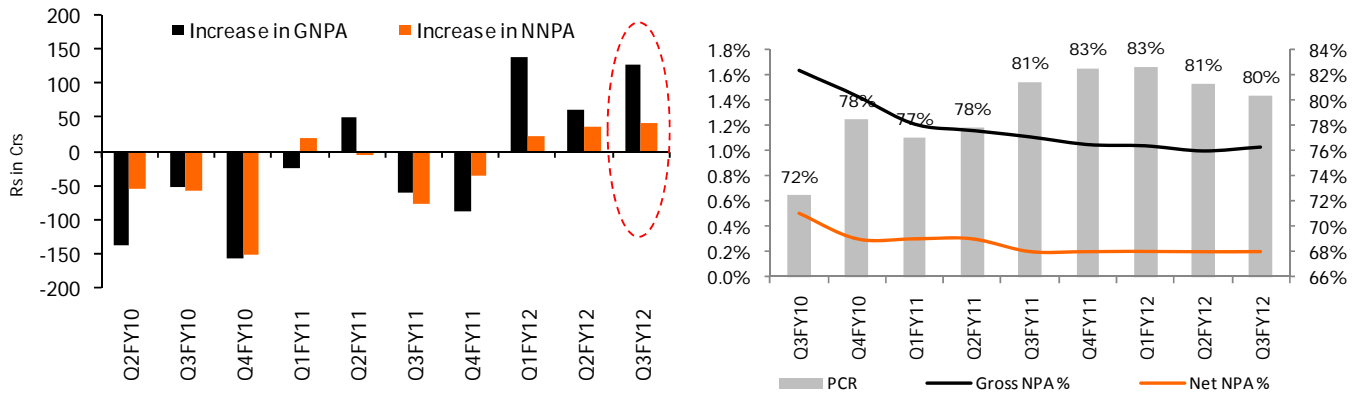
Rs in crore	Q3FY12	Q2FY12	Q3FY11	q-o-q	y-o-y
Auto Loans	25762	24606	22200	4.7%	16.0%
Personal Loans	13112	12004	9800	9.2%	33.8%
CVs	12604	11348	8700	11.1%	44.9%
Loans against securities	1034	980	1200	5.5%	-13.8%
2- wheelers	2405	2173	1900	10.7%	26.6%
Business banking	17358	16847	13400	3.0%	29.5%
Credit cards	6459	5855	4600	10.3%	40.4%
Home loans	13128	12344	10950	6.4%	19.9%
Others**	8485	6721	4750	26.2%	78.6%
Total	100347	92878	77500	8.0%	29.5%

Source: Company, KRChoksey Research ** Includes Gold loans, Kishan Retail Agri loans, tractor loan and retail OD against FD

Asset quality remains fairly strong

Broad asset quality continued to be fairly strong as gross NPA increased 6.6% q-o-q basis to Rs 2,021 crore which is equivalent to 1.0% of gross advances. Net NPAs stood at 0.2% with superior coverage ratio of 80.3%. Restructured assets stood at 0.40% of total advances, out of that 0.3% were NPAs. Quarterly trend suggests that credit costs are lower than normalized levels due to better than expected portfolio behavior, so we believe credit cost is likely to revert back to normalized levels medium term. The management expects slowdown in up gradation and recoveries which may translate into higher gross NPAs in coming quarters. We are building in 65bps & 80bps credit costs in FY12 and FY13 respectively against 53bps in FY11.

Exhibit : 7 Gross NPA and Net NPA Trend

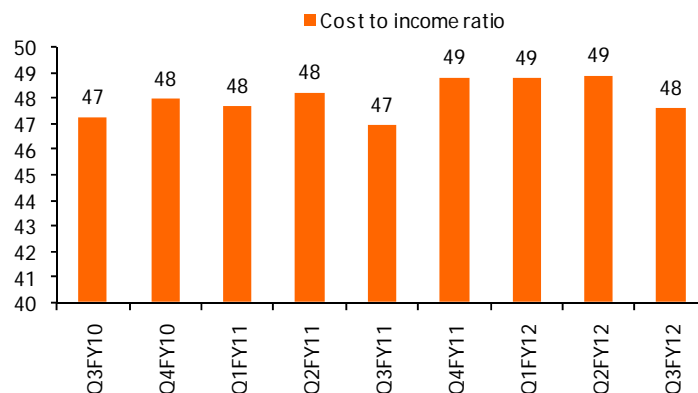


Source: Company, KRChoksey Research

Improving operating efficiency led to decline in cost to income ratio

Other operating expenses increased by 16.6% y-o-y & 6.9% q-o-q to Rs 1,291 crore as the bank continued to invest in network expansion. It added 51 new branches and 590 ATMs during the quarter. The increase in employee cost was 5.4% q-o-q to Rs 867.4 crore, in line with quarterly run rate. Strong net operating revenues and better operating efficiency resulted into improvement in cost to income by 128bps to 47.6%. The bank continues to add branches and ATMs in new geographic, so we believe cost to income ratio to remain in the range of 47-48%.

Exhibit : 8 Cost to income ratio



Source: Company, KRChoksey Research

Other key highlights

- Total specific and general provision went down by 10.1% q-o-q to Rs329 crore. The bank provided Rs289 crore towards loan loss provisioning and balance Rs30 crore towards contingent liabilities. Out of total loan loss provisioning, general and specific provisions contributed 45% and 55% respectively. Specific LLP was down 20% q-o-q due to stable asset quality. On YTD basis, Total specific provisioning stood Rs600 crore.
- Risk weighted assets stood at Rs2,33,000 which is 69.5% of total assets.
- Capital adequacy stood at 16.3% while tier I stood at 11.2%, well capitalized for asset growth in medium term.

Earnings Revision

(Rs in crore)	FY12e		Change (%)	FY13		Change (%)
	Old	New		Old	New	
Net Interest Income	12544	12211	-2.7%	15391	15320	-0.5%
Pre Provision Profit	9497	8988	-5.4%	11722	11309	-3.5%
Net Profit	5098	5180	1.6%	5985	6320	5.6%

Source: Company, KRChoksey Research

Q3FY12: Quarterly Result Analysis

	Q3FY12	Q2FY12	Q3FY11	q-o-q	y-o-y
Income Statement					
Interest income	7203	6718	5230	7.2%	37.7%
Interest expense	4087	3773	2453	8.3%	66.6%
Net interest income	3116	2945	2777	5.8%	12.2%
Non interest income	1420	1212	1128	17.2%	25.9%
-- Core fee income	1128	988	943	14.1%	19.6%
-- Trading gains	-82	-1	-31	-	-
Operating income	4536	4156	3905	9.1%	16.2%
- Employee costs	867	823	725	5.4%	19.6%
- Other operating expenses	1291	1207	1107	6.9%	16.6%
Operating expenses	2158	2030	1832	6.3%	17.8%
Pre-provision profits	2378	2126	2073	11.9%	14.7%
Provisions	329	366	466	-10.1%	-29.3%
Profit before tax	2049	1760	1607	16.4%	27.5%
Tax expense	619	560	519	10.5%	19.3%
Net profit	1430	1199	1088	19.2%	31.4%
Balance Sheet summary					
Net worth	29490	27972	25050	5.4%	17.7%
Deposits	232508	230676	192202	0.8%	21.0%
Borrowings	24426	22344	13436	9.3%	81.8%
Other Liabilities & Provisions	49064	34751	19130	41.2%	156.5%
Total Liabilities	335487	315746	249820	6.3%	34.3%
Investments	80214	78647	63014	2.0%	27.3%
Advances	194303	188502	159184	3.1%	22.1%
Total Assets	335487	315746	249820	6.3%	34.3%
Key ratios					
Spread Analysis					
Yield on avg advances	11.32%	10.98%	9.99%	34 bps	133 bps
Yield on avg investments	8.80%	8.54%	7.74%	26 bps	106 bps
Yield on avg int. bearing assets	9.80%	9.59%	8.67%	21 bps	113 bps
Cost of funds	6.41%	6.21%	4.74%	20 bps	167 bps
Net interest margins	4.24%	4.20%	4.60%	4 bps	-36 bps
Reported NIM	4.10%	4.10%	4.20%	0 bps	-10 bps
Other ratios					
CD ratio	83.6%	81.7%	82.8%	185 bps	75 bps
CASA ratio	48.6%	47.3%	50.5%	123 bps	-193 bps
Gross NPAs	2021	1895	1782	6.6%	13.4%
Net NPAs	398	355	331	12%	20.3%
GNPA ratio	1.03%	1.00%	1.11%	3 bps	-8 bps
NNPA ratio	0.20%	0.20%	0.20%	0 bps	0 bps
Provision coverage ratio	80.3%	81.3%	81.4%	-95 bps	-114 bps
Cost to income ratio	47.6%	48.9%	46.9%	-128 bps	66 bps
Provisions / Avg assets	0.40%	0.49%	0.75%	-8 bps	-34 bps
Capital Adequacy ratio					
Tier I	11.2%	11.4%	12.1%	-20 bps	-90 bps
Tier II	5.1%	5.1%	4.2%	0 bps	90 bps
CAR	16.3%	16.5%	16.3%	-20 bps	0 bps

Source: Company, KRChoksey Research

NII grew 12.2% y-o-y driven by volume growth and resilient margin of 4.1%

Healthy fee income growth coupled with strong traction in forex profits boosted non-interest income

Provisioning expenses were down 10.1% q-o-q due to lower loan loss provisioning

Advances grew by 22.1% y-o-y while deposits grew by 21.0% y-o-y as a result CD Ratio improved to 83.6%

Asset quality remained fairly strong

Cost to income ratio improved q-o-q

Well capitalized with tier I ratio 11.2% excluding Q3FY12 profits

Financials

Income Statement

Rs in crore	FY10	FY11	FY12E	FY13E
Interest income	16173	19928	27347	32675
Interest expense	7786	9385	15135	17355
Net Interest Income	8387	10543	12211	15320
-- Core fee Income	3616	4518	5359	6294
Non-interest income	3983	4335	5259	6494
Operating income	12370	14878	17470	21814
Operating expenses	5764	7153	8482	10505
-Employee cost	2289	2836	3361	4039
-Other operating expenses	3475	4317	5120	6467
Pre-provision profits	6605	7725	8988	11309
Provisions	2140	1906	1480	2149
PBT	4465	5819	7508	9160
Provision for taxes	1341	1893	2327	2840
Net profit	3124	3926	5180	6320
Dividend (Inc. tax)	641	892	1204	1506

Spread Analysis

	FY10	FY11	FY12E	FY13E
Yield On Advances	10.8%	8.7%	8.9%	8.9%
Yield On Investments	6.8%	7.1%	7.0%	7.0%
Avg Yield On IBA	8.0%	8.0%	8.2%	8.2%
Avg Cost Of Deposits	4.5%	4.4%	4.6%	4.7%
Avg Cost of Funds	4.6%	4.6%	4.7%	4.8%
Spread	3.4%	3.4%	3.5%	3.4%
NIM	4.3%	4.4%	4.2%	4.3%

Asset Quality Profile

	FY10	FY11	FY12E	FY13E
Gross NPA	1,817	1,694	2,183	2,706
Net NPA	392	296	546	677
Gross NPA %	1.4%	1.1%	1.1%	1.1%
Net NPA %	0.3%	0.2%	0.3%	0.3%
Credit Costs	1.7%	0.53%	0.65%	0.80%

Per Share Data

(Rs)	FY10	FY11	FY12E	FY13E
EPS	13.7	16.9	22.3	27.2
DPS	2.8	3.8	5.2	6.5
BVPS	94.0	109.1	126.2	146.9
ABVPS	92.3	107.8	123.8	144.0
P/E	35.5	28.7	21.8	17.8
P/ABV	5.3	4.5	3.9	3.4
Dividend Yield	0.6%	0.8%	1.1%	1.3%

Balance Sheet

Rs in crore	FY10	FY11	FY12E	FY13E
Equity capital	458	465	465	465
Reserve and Surplus	21062	24911	28887	33702
Net worth	21520	25376	29353	34167
Deposits	167404	208586	254475	315550
Borrowings	12916	14394	16553	19036
CL and provisions	20616	28993	37053	46575
Total	222459	277353	337437	415331
Cash and Bal. with RBI	15483	25101	23099	28044
Balances with RBI	14459	4568	10182	13210
Investments	58608	70929	86522	104131
Advances	125831	159983	196779	244006
Fixed assets	2123	2171	2605	3126
Other assets	5955	14601	18251	22814
Total	222459	277353	337437	415331

DuPont Analysis

	FY10	FY11	FY12E	FY13E
NII	4.1%	4.2%	4.0%	4.1%
Fee Income	1.8%	1.8%	1.7%	1.7%
Treasury Income	0.2%	0.0%	0.0%	0.0%
Employee Cost	1.1%	1.1%	0.9%	0.9%
Operating Costs	2.8%	2.9%	2.8%	2.8%
Provisions	1.1%	0.8%	0.5%	0.6%
Tax	0.7%	0.8%	0.8%	0.8%
ROAA	1.5%	1.6%	1.7%	1.7%
RoAE	17.3%	16.7%	18.9%	19.9%

Business Profile

	FY10	FY11	FY12E	FY13E
Advances	125831	159983	196779	244006
CD ratio	75%	77%	77%	77%
Deposits	167404	208586	254475	315550
CASA Deposits	87104	109908	120876	146731
CASA Ratio	52.0%	52.7%	47.5%	46.5%

Growth ratios

	FY10	FY11	FY12E	FY13E
Net interest income	13%	26%	16%	25%
Fee income	18%	25%	19%	17%
Pre-provision Profits	28%	17%	16%	26%
Net Profits	39%	26%	32%	22%
Advances	27%	27%	23%	24%
Deposits	17%	25%	22%	24%
Total Assets	21%	25%	22%	23%

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HDFC Bank			
Date	Recom	CMP	Target
20-Jan-12	HOLD	485	540
5-Jan-12	HOLD	458	510
19-Oct-11	HOLD	491	530
4-Oct-11	BUY	458	530
23-Sept-11	BUY	460	530
20-July-11	HOLD	519	565
19-Apr-11	BUY	463	534
28-Jan-11	BUY	410	493

Rating Legend	
Our Rating	Upside
Buy	More 15%
Hold	5% - 15%
Reduce	0% – 5%
Sell	Less than 0%

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