# Investor's Delight – HDFC Bank Ltd. (SIL) – Q1FY14 result update, "BUY"

## "Gigantic scale yet to be achieved, journey on right track…"

| Date | July 18, 2013 |
|---|---|
| BSE Code/NSE Code | 500180/HDFCBANK |
| Bloomberg/Reuters Code | HDFCB:IN/HDBK.BO |
| Industry | Banking |
| FV | Rs. 2 |
| Equity Share Capital | Rs. 4.77 bn |
| Market Capitalization | Rs. 1634 bn |
| ROAE | 20.3% |
| ROAA | 1.8% |
| 52 week high/low | Rs. 727.3 (30th May, 2013)/Rs. 505.05 (5th Oct, 2012) |
| CMP | Rs. 684 |
| Recommendation | "BUY" |
| Target/Upside (%) | Rs. 740/Upside: 8 % |

### Ajcon's view

We believe HDFC Bank is at an inception point where in the best performance of the bank is yet to be witnessed. In addition, we are of the view that it is one of the unique bank in the Indian Banking industry and will become one of the giants similar to SBI. Going back to value investing basics and replicating value investing methodology of Mr. Warren Buffet, HDFC enjoys all the features of being a "Good" company which are as follows:

a) Nature of business is subject to moderate changes like to deal with RBI measures such as CRR, repo rates etc.
b) It enjoys steady competitive advantage
c) Brilliant management quality with good corporate governance
d) Business growth above industry benchmark
e) Stable and attractive ROE of 23%

Buffet calls this the "put-up more-to earn-more" phenomenon, which is true of most companies across countries. Good companies grow at healthy rates, but need large increase in capital to sustain growth.

On lending front, the pace of retail credit expansion will be higher than loans to companies. In an election year, we are likely to see some pick-up in domestic consumption. A good monsoon too is a positive trigger for the economy. We do not see much of a scope for any base rate reduction as the bank cannot reduce its deposit rates. HDFC Bank's conservative lending strategies have helped it maintain consistently strong growth and outperform local peers struggling with an increase in bad loans. Historically, Bank has managed well in terms of maintaining its margins in interest rate cyclical environment along with a high CASA ratio with stable NPAs in the past, high provision coverage ratio of 74.7 percent, and robust quality franchise as compared to peer banks, which deserves a premium. It has proved that it is one of the safe heavens in the Banking sector as well and has a long journey ahead in years to come and achieve a gigantic scale. HDFC Bank is expected to deliver earnings CAGR of 25 %+ over FY13-FY15E. We recommend a "Buy" with a target price of Rs. 740 for investors with 9-12 months horizon and believe that this stock offers Wealth Creation Opportunity for investors having a view of more than 10 years.


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Business Growth - HDFC Bank's first quarter Q1FY14 results earnings witnessed consistency in growth. It continued to outperform the banking industry growth rate in both advances and deposits. Savings accounts deposits clocked yoy growth of 16.7 percent to touch Rs. 89,480 crores and current account deposits grew by 10.5 percent to touch Rs. 46,0781 crores. CASA stood at an impressive 44.7%. The Bank's network registered a growth of yoy growth of 22 percent in branches to reach 3,119 Branches and yoy growth of 12.4 percent to touch11,088 ATMs as on Q1FY14. 54 percent is of network is accounted by semi urban, rural areas. They are planning to open further 250-300 branches. Advances clocked yoy growth of 21.2 percent to touch Rs. 2,58,589 crores in Q1FY14. This loan growth was contributed by both segments of the Bank loan portfolio, with retail loans growing by 25.5 percent and wholesale loans by 16.5 percent resulting in a retail:wholesale loan mix of 54:46. Wholesale book mainly comprises of Working Capital, Medium Term Loans, and Refinancing of corporate debts. On the other hand, The Retail Portfolio comprises of Auto Loan, CV, Business Banking, Home Loans, Personal Loans, Gold Loans. Proportion of unsecured loan in retail book is 21% (No change in mix). In addition, the bank was successful in meeting with the 40% priority sector lending target and is also complying with meeting the sub targets.

The Bank's net interest margin (NIM) should be in the range of 4.1-4.6 range. The impact of RBI's liquidity measures on HDFC Bank in case of the tighter liquidity situation will only affect the lender's bond portfolio especially in two categories available for sales (AFS) and available for trading (AFT). It is mostly deposit funded. Bond yields have risen sharply. In those categories, impact will be booked on mark-to-market (M-to-M) basis. These bonds are roughly about 20-25 percent of its SLR portfolio. HDFC Bank's total deposits stood at Rs. 3.03 lakh crore. Currently, the statutory liquidity ratio is at 23 percent as mandated by the RBI. Hence, the bank maintains an investment worth of Rs. 69,762 crore (approx.) in the government securities under the SLR obligation. Accordingly, AFS and AFT portfolios come to around Rs. 17,440 crore (25 percent).

P&L performance - Total income of the Bank witnessed yoy growth of 17.9 percent to touch Rs. 11,588.6 crores as on Q1FY14. Net interest income which accounts for 69.6 percent of net revenues grew by 21 percent to Rs. 4,419 crores. The bank has a steady NIM of 4.6% owing to reduction of funding cost by 10basis points, the FD rates were also less, which was offset by lower yields on loan growth. Fee income became less due top third party commission. There will be no impact on Forex Revenues due to proprietary trading. Other income was up by 30.4 percent to touch Rs. 1,925.6 crores blostered by four components a) Fees & Commissions of Rs. 1,284.5 crores, b) Foreign Exchange and Derivative revenue of Rs. 314.3 crores, c) Gain on revaluation/sale of investments of Rs. 199.5 crores (Rs. 66.5 crores in Q1FY13) and d) miscellaneous income including recoveries of Rs. 127.3 crores as against Rs. 117.6 crores for the corresponding quarter of the previous year. Cost to Income ratio witnessed a decline of 160 bps to 47.9 percent in Q1FY14. The profit before tax stood at Rs. 2,779 crores, an increase of 32.7 percent on yoy basis. PAT clocked yoy growth of commendable 30.1 percent to earn Rs. 1,843.9 crores.

Asset Quality - Grosss non – performing assets (GNPAs) stood at 1 percent of gross advances as on Q1FY14. Net non – performing assets stood at 1 percent of gross advances as on June 30, 2012. Net NPAs were at 0.3 percent of net advances as on Q1FY14. Total restructured loans (including applications received and under process for restructuring) were at 0.2 percent of gross advances as of June 30, 2013 as against 0.3 percent in the previous year. Total floating provisions stood at Rs. 1,865 crores as on Q1FY14, as against Rs. 1,680 crores in Q1FY13. A marginal rise of 10 basis points in the bank's net non-performing asset ratio, which stood at 0.30 percent as against a static level 0.20 percent recorded for last so many quarters. One may call it a flippant reaction or whatsoever; investors discounted one of the banking elites on this crucial deviation. The bank expanded its loan book by more than 21 percent y-o-y to about Rs 2.59 lakh crores. In absolute term, the net NPAs would come around Rs 700 crore. Going forward, we do not see it as a trend. It should stabilize at around the current levels of gross and net NPA ratios (1 percent and 0.30 percent).The rise on net NPAs came from retail and corporate segments equally. Some loans in the commercial vehicle and construction equipments added to it while individual corporate loans from two-three different sectors, contributed as well. In terms of total book size, NPAs are not significant.

**Slippages**
Retail contributed to 43 percent in slippages mainly in CV, CE .Corporates contributed less than half. Gross slippages in quarter 1.04 percent i.e. Rs. 380 crores.

**Provisions and Contingencies** stood at Rs. 527.1 crores (consisting of specific loan loss, general and floating provisions) for Q1FY14 as against Rs. 581.6 crores in Q1FY13.

**Capital Adequacy**
The Bank's total Capital Adequacy ratio (CAR) as onQ1FY14 (computed as per Basel III guidelines) stood at 15.5 percent as against a regulatory requirement of 9 percent. Of this, Tier-I CAR was 10.5%. Computed as per Basel II guidelines, total CAR was 16 percent and Tier I CAR was 10.6 percent.

**Financial Summary (Rs. cr)**

| Particulars (Rs in Crore) | Q1FY14 | Q4FY13 | QoQ (%) | Q1FY13 | YoY (%) |
|---|---|---|---|---|---|
| **Interest Earned (A)** | **9663** | 9324 | 3.6 | 8176 | 18.2 |
| a) Interest-Discount on Advances/ Bills | **7325** | 7087 | 3.4 | 6232 | 17.5 |
| b) Income on Investments | **2218** | 2096 | 5.8 | 1879 | 18.1 |
| c) Interest on Balances with RBI and other inter bank funds | **110** | 78 | 41.7 | 51 | 115.8 |
| d) Others | **10** | 64 | (84.1) | 14 | (28.7) |
| **Other Income (B)** | **1926** | 1804 | 6.8 | 1649 | 16.7 |
| **Total Income (A+B)** | **11589** | 11128 | 4.1 | 9825 | 17.9 |
| Interest Expended | **5244** | 5029 | 4.3 | 4523 | 15.9 |
| **Net Interest Income** | **4419** | 4295 | 2.9 | 3652 | 21.0 |
| Operating Expenses | **3038** | 3136 | (3.1) | 2627 | 15.7 |
| Employee Cost | **1109** | 1005 | 10.3 | 993 | 11.7 |
| Other Operating Expenses | **1929** | 2131 | (9.5) | 1633 | 18.1 |
| Total Expenditure | **8282** | 8165 | 1.4 | 7150 | 15.8 |
| **Operating Profit** | **3306** | 2963 | 11.6 | 2675 | 23.6 |
| **Provisions(other than tax) and contingencies** | **527** | **301** | **75.4** | **582** | **(9.4)** |
| Profit and Loss from Ordinary Activities before tax | **2779** | 2662 | 4.4 | 2094 | 32.7 |
| Tax Expenses | **935** | 772 | 21.1 | 676 | 0.0 |
| Net Profit/Loss from Ordinary Activities after tax | **1844** | 1890 | (2.4) | 1417 | 30.1 |
| **Net Profit for the period** | **1844** | 1890 | (2.4) | 1417 | 30.1 |
| No. of Shares | **238.88** | 237.94 | 0.4 | 235.59 | 1.4 |
| EPS Rs. | **7.72** | 7.94 | (2.8) | 6.02 | 28.3 |
| **Key Financial Indicators** | | | | | |
| Advances (Rs. cr) | 258589.4 | 296247 | (12.7) | 213338.3 | 21.2 |
| Deposits (Rs. cr) | 303315.0 | 239721 | 26.5 | 257531.0 | 17.8 |
| Cost/Income % | 47.9 | 51.4 | (6.9) | 49.5 | (3.3) |
| Net Interest Margin (%) | 4.5 | 4.40 | 2.3 | | |
| Net NPA (%) | 0.3 | 0.20 | 50.0 | | |

| | | | | | |
|---|---|---|---|---|---|
| Net Worth (Rs. Cr) | 37980.0 | 36214 | 4.9 | 31603.98 | 20.2 |
| Book Value per share (Rs.) | 159 | 152 | 4.5 | 134 | 18.5 |
| Gross NPA (Rs. Cr) | 2719 | 2334.64 | 16.5 | 2086.32 | 30.3 |
| Net NPA (Rs. Cr) | 689 | 468.95 | 46.9 | 396.02 | 74.0 |
| % of Gross NPA | 1.0 | 0.97 | 3.1 | 1.00 | 0.0 |
| % of Net NPA | 0.3 | 0.20 | 50 | 0.20 | 50.0 |
| Restructured Advances % | 0.2 | 0.20 | 0.0 | 0.30 | (33.3) |

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