

Company Flash

11 March 2008 | 7 pages

HDFC Bank (HDBK.BO)

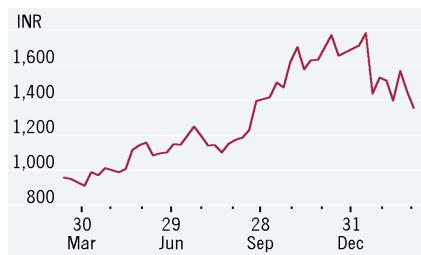
 Meeting with management
 Conference

Citi India Conference 2008: Day 1 Takeaways

- **Conference takeaways** — HDFC Bank spoke with investors at the Citi India Investor Conference 2008. Here are some of the highlights of that presentation.
- **Integration of CBOP merger** — The merger will be put up for shareholders approval of both banks before end Mar 08. It expects legal approvals (from RBI) to be in place by Jul 08. The integration process would, however, take an additional 12-15 months. Key near-term benefits from the merger would be increases in operational efficiencies, resulting in lower costs and higher CASA ratio.
- **Asset growth on track** — Management reiterated asset growth remained strong and well balanced. Growth is well diversified between retail (55% of book) and corporate, across credit and deposit products and across products and customer segments.
- **Asset quality – no signs of strain** — Despite the strong growth outlook, management is not seeing any significant deterioration in quality of assets in the retail segment, and provisioning is in-line with its evolving asset mix. Also, there is no impact of the farm loan waiver to HDBK's loan portfolio.
- **Fee income – sustained growth** — Management seemed confident of sustaining strong growth in fees as its dependence on trading income remains low. The fee base remains well balanced across products, though growth might slow down a bit due to relatively slower growth in treasury-linked product sales (strong area of growth last year).

Hold/Low Risk	2L
Price (11 Mar 08)	Rs1,331.95
Target price	Rs1,565.00
Expected share price return	17.5%
Expected dividend yield	0.6%
Expected total return	18.1%
Market Cap	Rs472,087M
	US\$11,685M

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



Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2006A	8,709	27.28	25.1	48.8	7.9	17.7	0.4
2007A	11,414	35.23	29.1	37.8	6.6	19.5	0.5
2008E	16,374	47.40	34.5	28.1	4.0	17.8	0.6
2009E	21,375	58.76	24.0	22.7	3.4	16.6	0.6
2010E	28,501	78.35	33.3	17.0	2.9	19.0	0.8

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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HDFC Bank

Company description

HDFC Bank, which began operations in 1994, is 24%-owned by HDFC - India's premier mortgage-finance institution. In 2000 HDFC Bank took over private-sector Times Bank. HDFC Bank is headquartered in Mumbai and has a network of more than 734 branches spread across 263 cities. The bank has a network of more than 1,471 ATMs. HDFC Bank entered into an arrangement with its parent FY04 through which HDFC Bank sources mortgages for the parent. HDFC Bank pays HDFC for credit appraisal and operations and receives a fee for sourcing. In addition, HDFC Bank buys back 70% of mortgages at a price of 125bps lower than the yield of the mortgages. HDFC Bank has had strong and steady growth over the past 10 years and continues to grow at more than 30%.

Investment strategy

We rate HDFC Bank as Hold/Low Risk (2L) with a 12-month target price of Rs1,565. We believe HDFC Bank should be able to generate a premium to its current trading level as it sustains asset growth, consolidates its distribution, leverages off new capital and stabilizes its business mix with increased retail returns. HDFC Bank should also enjoy increased growth and stability in its fee franchise due to its consistently widening distribution platform. While we expect HDFC Bank to trade in the 3-4x P/BV band over the longer term, we see it trading at the upper end of its trading band, as its raises ROE's on capital that it has recently raised. We remain positive on the bank's prospects and management's ability to deliver, but in the near term the stock's performance could be moderated by high valuations relative to ROE and peers, uncertainty on interest rates, and competitive pricing environment.

Valuation

Our valuation is based on our EVA-based methodology, which values HDFC Bank at Rs1,565. Our EVA value is based on an 8% risk-free rate, higher-than-industry margins and higher capital ratio (6.75% vs. 6% average).

Our target price is also benchmarked off a 4x FY09E P/BV of Rs1,545. The basis for our target multiple - a distinct premium to all other Indian commercial banks - is HDBK's structurally higher margin, de-risked earnings and balance sheet mix, and gains in the consumer-lending franchise. We believe a re-rating from current levels would be difficult.

We prefer using an EVA-based valuation benchmark to P/BV because EVA concentrates on the economic value creation of the bank.

Risks

We rate HDFC Bank as Low Risk based on our quantitative risk-rating system, which tracks 260-day historical share-price volatility. The downside and upside risks to our target price lie in: (1) any negative/positive news on asset quality; (2) management changes; (3) emergence of high quality and scale competitors; and (4) the HDFC Bank-HDFC agreement. If any of these factors has a greater impact than we expect, the stock could have difficulty achieving our target price.

Appendix A-1

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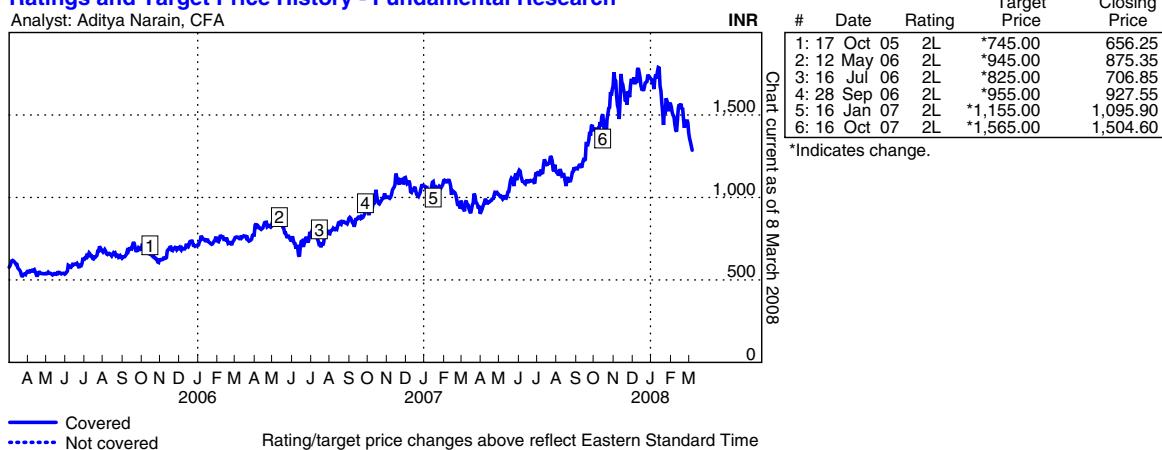
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HDFC Bank (HDBK.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Aditya Narain, CFA



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