

January 22, 2008

**ACCUMULATE**

Price **Rs1,518** Target Price **Rs1,700**

Sensex **17,605**

**Price Performance**

| (%)            | 1M  | 3M | 6M | 12M |
|----------------|-----|----|----|-----|
| Absolute       | (8) | 12 | 24 | 42  |
| Rel. to Sensex | 0   | 12 | 11 | 15  |

Source: Capitaline

**Stock Details**

|                                 |                     |
|---------------------------------|---------------------|
| Sector                          | Banks               |
| Reuters                         | HDBK.BO             |
| Bloomberg                       | HDFCB@IN            |
| Equity Capital (Rs mn)          | 3541                |
| Face Value                      | 10                  |
| 52 Week H/L                     | 1825/890            |
| Market Cap                      | Rs537.3bn/USD13.4bn |
| Daily Avg Volume (No of shares) | 6,99,262            |
| Daily Avg Turnover (US\$)       | 29.2mn              |

**Shareholding Pattern (%)**

| (31 <sup>st</sup> Dec.'07) |      |
|----------------------------|------|
| Promoters                  | 23.3 |
| FII                        | 50.3 |
| Institutions               | 6.2  |
| Private Corp.              | 8.1  |
| Public                     | 12.1 |

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**HDFC Bank**Result  
Update**Superb earnings once again**

HDFC Bank's Q3FY08 result was much ahead of our expectations. The NII grew 65.6% yoy driven by robust advances growth and better than expected NIMs. The operating profit grew by 67.5% yoy to Rs10.6bn driven by higher fee income and treasury gains which compensated for higher Opex. However net profit grew by only 42.2%, as the bank's made a higher provisioning of Rs4.2bn in the quarter as compared to Rs2.1bn in the corresponding quarter last year

We continue to like robust business model of HDFC Bank and robust quality of its earnings as well as assets. We have revised our earnings estimates for FY08-10E by 1-15%. At the current valuations of 20.7x its FY2010E EPS and 3.4x FY2010E P/ABV, the stock seems quite attractive. We retain Accumulate rating on the stock with a revised 12m price target of Rs1,700.

**NII jumps 65.6%yoy led by NIM's expansion**

HDFC Bank's NII (net of amortisation expenses) grew by 65.6% yoy to Rs14.4bn driven by 39.1% yoy growth in core customer assets to Rs750bn and NIM expansion of 50bps on yoy basis.

**NII reports strong growth**

|                       | Q3FY08   | Q3FY07  | Q2FY08   | % yoy chg | % qoq chg |
|-----------------------|----------|---------|----------|-----------|-----------|
| Reported NII          | 14,375.8 | 8,682.5 | 11,626.8 | 65.6      | 23.6      |
| Add: Amortisation exp | 719.0    | 603.8   | 588.0    |           |           |
| Adjusted NII          | 15,094.8 | 9,286.3 | 12,214.8 | 62.5      | 23.6      |

**Higher investment yield and lower deposits costs drive margins**

The strong expansion in margins was driven by higher investment yields as the SLR bonds in portfolio witnessed a repricing during the current quarter even as, the deposit cost also started easing. The cost of deposits declined by 10bps sequentially during the quarter.

**NIM analysis**

| (%)                   | Q3FY08 | Q3FY07 | Q2FY08 | Change in bps yoy | Change in bps qoq |
|-----------------------|--------|--------|--------|-------------------|-------------------|
| Yield on advances*    | 11.1   | 9.8    | 11.2   | 135.9             | -9.6              |
| Yield on investments* | 7.5    | 6.9    | 7.0    | 61.1              | 47.4              |
| Yield on assets*      | 8.6    | 7.8    | 8.3    | 81.1              | 30.5              |
| Cost of funds*        | 4.1    | 3.8    | 4.2    | 25.7              | -14.8             |
| NIM*                  | 4.5    | 4.0    | 4.1    | 55.3              | 45.3              |
| NIM (adj for amort)*  | 4.8    | 4.3    | 4.3    | 50.3              | 47.3              |
| Core NIM (reported)   | 4.3    | 4.0    | 4.0    | 30.0              | 30.0              |

Source: Company, Emkay Research \* Calculated on basis of average quarterly balances

**Selective, but strong growth in retail assets**

The business growth remained strong with the advances growing by 48.7% yoy and the deposits having grown by 48.9% yoy. The trend in the various segments of the retail assets remained steady over preceding quarters. The growth in the retail assets was led by personal loans, business banking loans and auto loans. Credit cards business has also seen significant expansion. However, 2-wheeler loans have seen a decline of 3.8% as the bank has stayed away from the segment due to increasing instances of delinquencies. The commercial vehicle segment has also seen a slower growth of 18.1% due to similar kind of problems.

**Retail loan portfolio mix**

|                         | Rs mn          | % yoy<br>change | Proportion<br>(%) | Change in bps |      |
|-------------------------|----------------|-----------------|-------------------|---------------|------|
|                         |                |                 |                   | yoy           | qoq  |
| Auto Loans              | 103,500        | 69.7            | 27.4              | 301           | -100 |
| Personal Loans          | 61,000         | 52.5            | 16.1              | 16            | -37  |
| CVs                     | 55,500         | 18.1            | 14.7              | -408          | -52  |
| Loan Against Securities | 12,500         | -3.8            | 3.3               | -188          | -2   |
| 2-Wheelers              | 17,500         | -10.3           | 4.6               | -316          | -29  |
| Business Banking        | 77,000         | 75.0            | 20.3              | 279           | 82   |
| Credit Cards            | 28,000         | 55.6            | 7.4               | 22            | 60   |
| Others                  | 23,400         | 187.3           | 6.2               | 293           | 78   |
| <b>Total</b>            | <b>378,400</b> | <b>51.0</b>     |                   |               |      |

Source: Company, Emkay Research

**Average quarterly CASA remains stable**

Although on point to point basis the CASA float declined by 400bps over last year, the average quarterly balance in the CASA accounts remained stable during the quarter. Also in the same quarter last year, HDFC Bank had large IPO floats at the end of the quarter, thereby creating a high base

|                | Rs bn | % yoy<br>change | Proportion<br>(%) | Change in bps |      |
|----------------|-------|-----------------|-------------------|---------------|------|
|                |       |                 |                   | yoy           | qoq  |
| Total Deposits | 993.9 | 667.5           | 910.7             | 48.9          | 9.1  |
| Savings        | 249.6 | 192.4           | 223.7             | 29.7          | 11.6 |
| % of total     | 25.1  | 28.8            | 24.6              |               |      |
| Current        | 256.0 | 174.3           | 254.6             | 46.9          | 0.6  |
| % of total     | 25.8  | 26.1            | 28.0              |               |      |
| Total CASA     | 505.6 | 366.7           | 478.3             | 37.9          | 5.7  |
| % of total     | 50.9  | 54.9            | 52.5              |               |      |

Source: Company, Emkay Research

**Opex slightly higher due to distribution business**

During the quarter, the operating expenses have grown by 73.6% yoy (28.3% sequentially) to Rs10.5bn. While the employee expenses grew by just 10% sequentially, the other Opex with 40% sequential jump was the main contributor to the higher Opex. The higher other Opex was attributable to the IPO business (where it operates escrow account for clients). The expenses on this business formed a major chunk of the incremental Opex. However, the same also gives a high CASA float.

**Provisioning higher however asset quality remains robust**

The provisioning requirement during the quarter has gone up substantially driven by Non Performing Assets and standard asset provisioning. However, the bank continues to enjoy robust asset quality as the GNPA as well as NNPA remained 1.2% and 0.4% respectively, same as last year. However the bank made a higher provisioning of Rs4.2bn in Q3FY08 as compare to Rs2060mn in the corresponding quarter last year.

**Comfortable capital adequacy**

The bank had Capital adequacy of 13.8% and tier I CAR at 10.5% at the end of Q3FY08. The bank has raised fresh equity capital of Rs42.0bn during the current year via preferential allotment to its promoter and ADS.

**Valuations and view**

We continue to like robust business model of HDFC Bank and robust quality of its earnings as well as assets. We have revised our earnings estimates for FY08-10E by 1-15%. At the current valuations of 20.7x its FY2010E EPS and 3.4x FY2010E P/ABV, the stock seems quite attractive. We retain Accumulate rating on the stock with a revised 12m price target of Rs1,700.

## Quarterly results

|                            | 9MFY08   | 9MFY07   | % yoy chg | Q3FY08   | Q3FY07   | Q2FY08   | % yoy chg | % qoq chg |
|----------------------------|----------|----------|-----------|----------|----------|----------|-----------|-----------|
| Net interest income        | 35,857.8 | 24,139.9 | 48.5      | 14,375.8 | 8,682.5  | 11,626.8 | 65.6      | 23.6      |
| Other Income               | 17,338.1 | 11,218.0 | 54.6      | 6,788.9  | 3,733.0  | 4,823.8  | 81.9      | 40.7      |
| <i>Fee income</i>          | 12,242.0 | 9,428.0  | 29.8      | 4,601.0  | 3,314.0  | 3,919.0  | 38.8      | 17.4      |
| <i>Other</i>               | 5,096.1  | 1,790.0  | 184.7     | 2,187.9  | 419.0    | 0.0      | 422.2     | -         |
| Net Income                 | 53,195.9 | 35,357.9 | 50.4      | 21,164.7 | 12,415.5 | 16,450.6 | 70.5      | 28.7      |
| Operating Expenses         | 26,428.8 | 17,368.7 | 52.2      | 10,501.2 | 6,050.2  | 8,183.8  | 73.6      | 28.3      |
| Operating Profit           | 26,767.1 | 17,989.2 | 48.8      | 10,663.5 | 6,365.3  | 8,266.8  | 67.5      | 29.0      |
| Provisions & Contingencies | 10,196.4 | 6,581.0  | 54.9      | 4,231.3  | 2,060.1  | 2,893.9  | 105.4     | 46.2      |
| <i>Loan loss provision</i> | 8,630.6  | 5,711.9  | 51.1      | 3,501.0  | 1,929.0  | 2,732.0  | 81.5      | 28.1      |
| Profit before tax          | 16,570.7 | 11,408.2 | 45.3      | 6,432.2  | 4,305.2  | 5,372.9  | 49.4      | 19.7      |
| Provision for Taxes        | 5,380.0  | 3,429.4  | 56.9      | 2,138.6  | 1,348.8  | 1,688.1  | 58.6      | 26.7      |
| Net Profit                 | 11,190.7 | 7,978.8  | 40.3      | 4,293.6  | 2,956.4  | 3,684.8  | 45.2      | 16.5      |

## Valuation table

| Y/E March 31 | Net<br>income | Net<br>profit | EPS<br>(Rs) | ABV<br>(Rs) | RoA<br>(%) | RoE<br>(%) | PE<br>(x) | P/ABV<br>(x) |
|--------------|---------------|---------------|-------------|-------------|------------|------------|-----------|--------------|
| FY2007       | 52,258        | 11,419        | 35.8        | 187.3       | 1.4        | 19.5       | 50.5      | 8.4          |
| FY2008E      | 68,668        | 15,404        | 42.8        | 318.8       | 1.5        | 16.8       | 36.9      | 5.0          |
| FY2009E      | 87,887        | 20,653        | 56.2        | 366.7       | 1.5        | 16.0       | 26.3      | 4.2          |
| FY2010E      | 109,293       | 24,402        | 66.4        | 435.7       | 1.4        | 16.1       | 20.5      | 3.4          |

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