

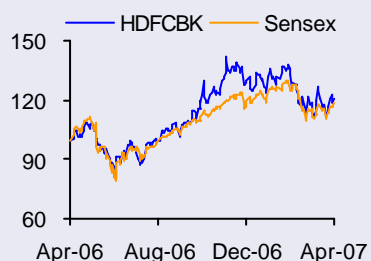
HDFC Bank (Q4 FY07) - Investment Update

Recommendation	SELL
CMP	Rs1,014
Target Price	Rs953
Upside	-6%
Market Cap.	Rs319bn
52 Week H/L	Rs1,160/615
Face Value	Rs10
BSE Code	500180
NSE Code	HDFCBANK
Bloomberg Code	HDFCB@IN
Reuters Code	HDBK.BO
1 Month avg vol.	0.2mn

Share Holding Pattern

Mar'07	(%)
Promoters	21.6
Institutions	6.4
FII	51.3
Public	20.7

Share Price Trend



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Sustained high CASA and lower pressure on resources helped improve margins to 4.5% in Q4 FY07. HDFC Bank reduced its exposure to bulk deposits as liquidity remained comfortable with advances reporting a 2.2% drop qoq. Operating cost continued to remain high as Bank opened 101 new branches during the quarter. Higher general provisions kept provisioning requirement high though profit growth maintained its 30% consistency. We maintain our positive outlook on the Bank's operational performance, though valuations at 4.3x FY08E book offer no upside from a 12 month perspective. We maintain our SELL rating on the stock with a price target of Rs953.

Sustained CASA, lower bulk deposits help improve NIM to 4.5%

Sequentially CASA remained steady at 55% as the Bank reduced its exposure to bulk deposits. This was more due to the slowdown in credit growth, which saw advances dropping by 2.2% sequentially. Lower pressure on resources, coupled with lending rate hikes, helped improve NIM to 4.5% from 4.3% in Q3 FY07.

Retail loan share improved to 56%

Retail loans during the quarter grew by 33.4%, improving its share to 56.9% as against 52% in Q3 FY07. While the retail segment growth has bounced backed well in Q4 FY07, we expect it to witness a slowdown over the next 8-12 months. We estimate a 28% CAGR in retail advances over FY07-09.

Core fee income reported a modest growth of 19.5%

Commission income during Q4 FY07 grew by mere 5.8% to Rs3.6bn, while forex income reported high growth of 118% to Rs1bn. Slower growth in the former segment kept core fee growth modest at 19.5%.

Branch expansion allowing no moderation in operating cost

HDFC Bank opened 101 new branches during Q4 FY07, in addition to 48 branches in Q3 FY07. This kept operating expenses growth (42%) high through increased staff (56%) and administrative cost (36%). Sustained branch expansion albeit at a lower speed would continue to keep operating cost growth high.

We expect provisioning to remain high

RBI's directive on increased general provisioning (Rs1.2bn out of the total Rs3.3bn) on real estate and certain non-collateralized retail loans kept provisioning requirements high. Higher incremental defaults on its non-collateralized retail book would likely keep provisioning high.

Table: Valuation summary

	FY05	FY06	FY07E	FY08E	FY09E
Net Profit (Rs mn)	6,656	8,708	11,415	14,746	18,900
Growth (%)	30.6	30.8	31.1	29.2	28.2
EPS (Rs)	21.5	27.8	36.3	46.9	60.1
ROAA (%)	1.4	1.4	1.4	1.4	1.4
ROE (%)	18.5	17.7	19.8	21.7	23.2
PE (x)	47.2	36.5	27.9	21.6	16.9
P/ Bv (x)	7.0	6.0	5.1	4.3	3.6
P/ Adj Bv (x)	7.0	6.2	5.3	4.5	3.8

Source: Company data, India Infoline Research



Table: Quarterly Financials

(Rs mn)	Q4 FY07 (3)	Q4 FY06 (3)	Growth (%)	Q3 FY07 (3)	Growth (qoq) (%)	FY07 (12)	FY06 (12)	Growth (%)
Interest Earned	19,898	13,785	44.3	17,593	13.1	68,890	44,753	53.9
Interest Expended	(8,721)	(6,391)	36.5	(8,307)	5.0	(31,795)	(19,295)	64.8
Net Interest Income	11,177	7,394	51.2	9,286	20.4	37,096	25,458	45.7
Other Income	3,944	3,042	29.7	3,733	5.7	15,162	11,240	34.9
Net Total Income	15,121	10,436	44.9	13,019	16.1	52,258	36,698	42.4
Operating Expenses	(6,839)	(4,823)	41.8	(6,050)	13.0	(24,208)	(16,911)	43.2
Pre Provisioning Profits	8,282	5,612	47.6	6,969	18.8	28,050	19,787	41.8
Provisions	(3,303)	(1,816)	81.9	(2,664)	24.0	(11,663)	(7,252)	60.8
Profit Before Tax	4,979	3,796	31.2	4,305	15.7	16,388	12,535	30.7
Tax	(1,544)	(1,164)	32.6	(1,349)	14.4	(4,973)	(3,827)	29.9
Profit After Tax	3,436	2,632	30.5	2,956	16.2	11,415	8,708	31.1
Advances (Rs bn)	469	351	34	480	(2.2)	469	351	34
Deposits (Rs bn)	683	558	22	667	2.3	683	558	22
Assets (Rs bn)	912	735	24	896	1.8	912	735	24
Retail Assets (%)	57	61		53		57	61	
CASA (%)	55	55		55		55	55	
NIM (%)	4.5	4.2		4.3		4.5	4.2	
GNPA (%)	1.2	1.2		1.2		1.2	1.2	
NNPA (%)	0.4	0.4		0.4		0.4	0.4	
CAR (%)	13.1	11.4		12.8		13.1	11.4	
Tier I (%)	8.6	8.6		8.4		8.6	8.6	
Branches	684	535		583		684	535	
ATMs	1,605	1,323		1,471		1,605	1,323	

Source: Company data, India Infoline Research



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