

- Loan growth inline with our estimates.
- FY10E EPS 9% lower than the Street on more muted loan growth assumptions.
- No change in our previous estimates as yet; awaiting detailed financials and management discussion.

Net Profit 09 INR22.3b
..... (Unchanged)

Diff from Consensus..(6.7%)
Consensus (mean) INR23.9b
Consensus (momentum) ↓

Target Price . INR2,250.00
..... (Unchanged)

Diff from Consensus ..13.1%
Consensus (median) .INR1,990.00
Consensus (momentum)..... ↓

Current Price INR1,373.55
Upside/ (Downside).....63.8%

BUY
(Unchanged)

Recs in the Market

Positive **21**
Neutral **3**
Negative **1**
Consensus (momentum)..... ↓

Sources: Thomson One Analytics; Bloomberg; BNP Paribas estimates

- **3QFY09 results beat our EPS estimates by 17% and income estimates by 16%.**
- **HDFC maintains spreads even after shifting borrowing mix toward high cost deposits.**
- **Gross NPL ratio continues downward trend (1.01% Q3, 1.04% Q2, 1.09% Q1), tier-1 boosted by relaxed risk weights.**

3QFY09 : EPS beat, thesis on track

HDFC reported 3QFY09 results on 21 January 2009. We present the key takeaways below. We are in the process of assessing the impact of these results on our estimates. We may revise our estimates and price target after discussions with management. A detailed comparison is given in Exhibit 1.

Core segment shows sustained growth, credit costs in check, rising opex the only dampener

- Loan disbursements showed sustained growth (22% growth in cumulative ytd disbursements) while loan approvals became stringent (incremental approvals in the quarter was 8% lower than 3QFY08). More importantly, y-y growth in cumulative ytd approval for individual loans was still at 21% indicating that HDFC is cutting down on exposure to riskier loans like developer financing and real estate.
- The company continued to move its borrowing mix toward deposits (now accounting for 22% of borrowing compared to 18% in 3QFY08) reporting a y-y growth of 57% in deposit base. Interest income maintained a sequential growth of 13%, highlighting HDFC's ability to pass on its higher deposit costs to customers. NII was up 5% q-q.
- Non-interest operating income streams maintained their robust growth with fee, cash management income and lease income posting a combined sequential growth of 28%.
- Gross NPL ratio dropped sequentially to 1.01% from 1.04% while the provision buffer ensured a nominal provision charge of INR120m in the P&L. RBI's relaxation in risk weights also pushed up tier-1 ratio to 14.1% from 13.4% in the previous quarter.
- HDFC's cost-to-income ratio continued over the 12% mark, up from 9.3% last year.

Valuation

Our current target price for HDFC is INR2,250. Our TP consists of INR1,700 for the core mortgage business (based on a three-stage residual income model) and INR550 for the subsidiary value. At our TP for core business, HDFC trades at 3.3x our FY10E BV.

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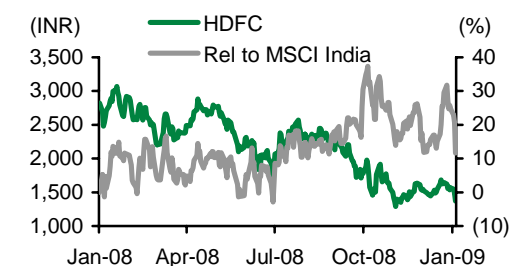
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Earnings Estimates And Valuation Ratios

YE Mar (INR m)	2008	2009E	2010E	2011E
Operating profit	27,372	31,146	37,139	46,283
Reported net profit	24,363	22,282	26,710	33,294
Recurring net profit	18,000	22,282	26,710	33,294
Previous rec net profit	18,000	22,282	26,710	33,294
Chg from previous (%)	—	—	—	—
Recurring EPS (INR)	63.01	76.74	91.99	114.67
Prev rec EPS (INR)	63.01	76.74	91.99	114.67
Rec EPS growth (%)	10.5	21.8	19.9	24.6
Recurring P/E (x)	21.8	17.9	14.9	12.0
Dividend yield (%)	1.8	2.0	2.4	3.0
Price/book (x)	3.3	3.0	2.7	2.4
Price/tangible book (x)	3.3	3.0	2.7	2.4
ROA (%)	2.40	2.43	2.48	2.66
ROE (%)	20.6	17.7	19.2	21.3

Sources: HDFC; BNP Paribas estimates

Share Price Daily vs MSCI India



Next results/event	June 2009
Market cap (USD m)	8.638
12m avg daily turnover (USD m)	67.3
Free float (%)	94
Major shareholder	Citi Str Hldg Mauritius (9%)
12m high/low (INR)	3,070.05/1,287.10
ADR (USD)	Nil
Avg daily turnover (USD m)	Nil
Discount/premium (%)	Nil
Disc/premium vs 52-wk avg (%)	Nil

Source: Datastream

Exhibit 1: 3QFY09 Result Variance Analysis

	3Q09 (INR m)	vs BNPP (%)	Chg (q-q %)	Chg (y-y %)	Comments
Income statement					
Interest earned	28,280.5	15	13	43	Interest income beat primarily from higher loan yield – volumes in line
Interest expended	20,220.0	14	16	54	
Interest on deposits	4,029.4	31	16	52	Deposit costs pushing up interest expenses
Interest on loans	6,250.4	(7)	17	33	Change in funding mix from term loans to deposits - a positive in our view
Interest on bonds/debentures	9,940.2	25	16	73	
Net interest income	8,060.5	17	5	20	5% q-q NII growth on 2% q-q loan growth- ability to maintain spreads
Non interest income	967.9	16	(17)	(44)	Operating income up 28% q-q, impact of lower treasury gains
Fee & other operating income	169.7	23	(5)	54	Fee & Cash management income streams continue strong trends
Surplus from cash mgmt deployment	307.6	34	25	(31)	
Treasury income	54.1	(82)	(76)	(95)	
Dividend income	332.9	326	(32)	464	Huge positive surprise driven by dividend income
Total income	9,028.4	17	2	7	Beat on higher NII and strong growth in non interest operating income
Employee cost	379.9	41	7	41	Opex much higher than expected
Operating & administrative costs	667.3	36	1	40	Cost to income ratio continues to remain above 12% compared to 9% LY
Depreciation	45.4	17	6	3	
Pre-prov operating profit	7,935.8	15	2	4	
Provisions & contingencies	120.0	(64)	(25)	100	Nominal provision flow through P&L owing to high provision buffer
PBT	7,815.8	19	3	3	
Tax provisions	2,347.5	27	4	1	
PAT	5,468.3	16	2	4	
PAT after extraordinary income	5,468.3	16	2	(27)	3QFY08 had extraordinary income of INR 1.2b
Basic EPS	19.2	16	2	2	
Pro forma diluted EPS	18.9	16	3	3	EPS Beat
Balance sheet					
Liabilities	951,118.7	4	6	26	
Share capital	2,844.4	0	0	1	
Reserves and surplus	131,968.6	3	5	15	
Borrowings	816,305.7	4	6	29	
Term loans	225,305.4	(4)	5	12	Reduced dependence on term loans
Bond/debenture/FCCB/CP	415,487.6	2	2	29	
Deposits	951,118.7	4	6	26	Increased reliance on customer deposits – 22% of total borrowing
Assets	896,700.0	2	5	23	
Investments	105,250.8	46	62	27	Parked INR39bn in liquid funds this quarter
Advances	828,956.7	(1)	2	34	Loan book in line with our estimates
Calculated book value	474.0	3	5	14	
	3Q09	BNPP est	2Q09	3Q08	
	(INR m)	(%)	(%)	(%)	
Capital Adequacy Ratio (CRAR) (%)	16.0	15.8	16.1	17.6	
CRAR - Tier 1 (%)	14.1	13.1	13.4	15.3	RBI relaxation of risk weights boosts tier-1 ratio sequentially
Provision for contingencies	4,975.1	(21)	3	(39)	
Gross NPL Ratio (%)	1.01	1.15	1.04	1.12	Sequential decline in gross NPL ratio continues

Sources: HDFC; BNP Paribas estimates

FINANCIAL STATEMENTS

HDFC

Profit and Loss (INR m)					
Year Ending March	2007A	2008A	2009E	2010E	2011E
Interest income	53,140	77,840	99,279	116,424	135,877
Interest expense	(36,293)	(51,100)	(67,581)	(79,020)	(89,120)
Net interest income	16,848	26,740	31,698	37,404	46,757
Net fees & commission	686	632	510	748	896
Foreign exchange trading income	-	-	-	-	-
Securities trading income	3,311	2,450	1,770	2,510	2,886
Dividend income	1,179	686	1,249	992	1,099
Other income	317	352	362	521	645
Non interest income	5,493	4,121	3,892	4,770	5,527
Total income	22,340	30,861	35,589	42,174	52,284
Staff costs	(913)	(1,178)	(1,405)	(1,635)	(1,985)
Other operating costs	(1,829)	(1,990)	(2,426)	(2,727)	(3,215)
Operating costs	(2,742)	(3,168)	(3,831)	(4,362)	(5,200)
Pre provision operating profit	19,598	27,692	31,759	37,812	47,084
Provisions for bad and doubtful debts	(250)	(320)	(613)	(673)	(801)
Other provisions	-	-	-	-	-
Operating profit	19,348	27,372	31,146	37,139	46,283
Recurring non operating income	-	-	-	-	-
Associates	-	-	-	-	-
Goodwill amortisation	-	-	-	-	-
Non recurring items	330	6,363	-	-	-
Profit before tax	19,678	33,735	31,146	37,139	46,283
Tax	(3,974)	(9,373)	(8,863)	(10,429)	(12,989)
Profit after tax	15,704	24,363	22,282	26,710	33,294
Minority interests	-	-	-	-	-
Preferred dividends	-	-	-	-	-
Other items	-	-	-	-	-
Reported net profit	15,704	24,363	22,282	26,710	33,294
Non recurring items & goodwill (net)	(330)	(6,363)	-	-	-
Recurring net profit	15,374	18,000	22,282	26,710	33,294
Per share (INR)					
Recurring EPS *	57.03	63.01	76.74	91.99	114.67
Reported EPS	62.65	89.86	78.20	93.74	116.85
DPS	22.00	25.00	27.37	32.81	40.90
Growth					
Net interest income (%)	27.7	58.7	18.5	18.0	25.0
Non interest income (%)	22.8	(25.0)	(5.6)	22.6	15.9
Pre provision operating profit (%)	29.4	41.3	14.7	19.1	24.5
Operating profit (%)	29.0	41.5	13.8	19.2	24.6
Reported net profit (%)	24.9	55.1	(8.5)	19.9	24.6
Recurring EPS (%)	23.4	10.5	21.8	19.9	24.6
Reported EPS (%)	24.7	43.4	(13.0)	19.9	24.6
Income breakdown					
Net interest income (%)	75.4	86.6	89.1	88.7	89.4
Net fees & commission (%)	3.1	2.0	1.4	1.8	1.7
Foreign exchange trading income (%)	-	-	-	-	-
Securities trading income (%)	14.8	7.9	5.0	6.0	5.5
Dividend income (%)	5.3	2.2	3.5	2.4	2.1
Other income (%)	1.4	1.1	1.0	1.2	1.2
Operating performance					
Gross interest yield (%)	9.61	11.30	11.86	11.82	11.80
Cost of funds (%)	6.99	8.09	9.02	9.00	8.66
Net interest spread (%)	2.62	3.21	2.84	2.82	3.14
Net interest margin (%)	3.05	3.88	3.79	3.80	4.06
Cost/income (%)	12.3	10.3	10.8	10.3	9.9
Cost/assets (%)	0.46	0.42	0.42	0.41	0.41
Effective tax rate (%)	20.2	27.8	28.5	28.1	28.1
Dividend payout on recurring profit (%)	38.6	39.7	35.7	35.7	35.7
ROE (%)	30.7	20.6	17.7	19.2	21.3
ROE - COE (%)	13.4	3.3	0.5	1.9	4.1
ROA (%)	2.58	2.40	2.43	2.48	2.66
RORWA (%)	8.02	4.51	3.47	3.28	3.36
* Pre exceptional, pre-goodwill and fully diluted					

Total Income CAGR of 17% from FY08 to FY10

Recurring PAT CAGR of 22% from FY08 to FY10

Sector leading cost to income ratio of about 10%

Sources: HDFC; BNP Paribas estimates

Balance Sheet (INR m)					
Year Ending March	2007A	2008A	2009E	2010E	2011E
Gross customer loans	565,124	729,979	866,626	1,016,238	1,195,442
Total provisions	(0)	(0)	(0)	(0)	(0)
Interest in suspense	-	-	-	-	-
Net customer loans	565,124	729,979	866,626	1,016,238	1,195,442
Bank loans	-	-	-	-	-
Government securities	9,389	9,054	12,405	13,893	15,283
Trading securities	-	-	-	-	-
Investment securities	27,273	60,096	61,738	69,396	77,703
Cash & equivalents	13,733	7,777	7,460	9,520	9,535
Other interest earning assets	23,753	20,614	22,534	22,534	22,534
Tangible fixed assets	2,131	2,085	2,042	1,975	1,905
Associates	-	-	-	-	-
Goodwill	-	-	-	-	-
Other intangible assets	-	-	-	-	-
Other assets	14,310	14,600	20,559	23,529	27,214
Total assets	655,713	844,205	993,364	1,157,085	1,349,617
Customer deposits	0	0	0	0	0
Bank deposits	-	-	-	-	-
Other interest bearing liabilities	571,930	691,512	807,528	947,528	1,110,028
Non interest bearing liabilities	28,269	33,220	54,194	62,900	74,173
Hybrid capital	-	-	-	-	-
Total liabilities	600,199	724,732	861,722	1,010,428	1,184,201
Share capital	2,530	2,840	2,842	2,842	2,842
Reserves	52,984	116,633	128,800	143,815	162,574
Total equity	55,514	119,473	131,642	146,658	165,416
Minority interests	-	-	-	-	-
Total liabilities & equity	655,713	844,205	993,364	1,157,085	1,349,617
Supplementary items					
Risk weighted assets (RWA)	244,906	552,500	732,553	897,232	1,084,127
Average interest earning assets	552,953	688,786	837,405	984,692	1,151,465
Average interest bearing liabilities	519,480	631,721	749,520	877,528	1,028,778
Tier 1 capital	18,613	80,665	91,973	101,771	114,022
Total capital	31,593	92,820	110,723	140,521	170,272
Gross non performing loans (NPL)	5,335	6,210	8,527	9,941	11,664
Per share (INR)					
Book value per share	219.42	420.62	462.03	514.73	580.57
Tangible book value per share	219.42	420.62	462.03	514.73	580.57
Growth					
Gross customer loans (%)	25.6	29.2	18.7	17.3	17.6
Average interest earning assets (%)	24.9	24.6	21.6	17.6	16.9
Total assets (%)	22.7	28.7	17.7	16.5	16.6
Risk weighted assets (%)	76.9	125.6	32.6	22.5	20.8
Customer deposits (%)	-	-	-	-	-
Leverage & capital measures					
Customer loans/deposits (%)	-	-	-	-	-
Equity/assets (%)	8.5	14.2	13.3	12.7	12.3
Tangible equity/assets (%)	8.5	14.2	13.3	12.7	12.3
RWA/assets (%)	37.3	65.4	73.7	77.5	80.3
Tier 1 CAR (%)	7.6	14.6	12.6	11.3	10.5
Total CAR (%)	12.9	16.8	15.1	15.7	15.7
Asset quality					
Change in NPL (%)	18.2	16.4	37.3	16.6	17.3
NPL/gross loans (%)	0.9	0.9	1.0	1.0	1.0
Total provisions/gross loans (%)	0.0	0.0	0.0	0.0	0.0
Total provisions/NPL (%)	0.0	0.0	0.0	0.0	0.0
Valuation					
Recurring P/E (x) *	24.1	21.8	17.9	14.9	12.0
Recurring P/E @ target price (x) *	39.5	35.7	29.3	24.5	19.6
Reported P/E (x)	21.9	15.3	17.6	14.7	11.8
Dividend yield (%)	1.6	1.8	2.0	2.4	3.0
Price/book (x)	6.3	3.3	3.0	2.7	2.4
Price/tangible book (x)	6.3	3.3	3.0	2.7	2.4
Price/tangible book @ target price (x)	10.3	5.3	4.9	4.4	3.9

Loan CAGR of 18%
from FY08 to FY10

Sufficiently capitalized
for growth over next few
years

NPL ratio to remain
around 1% level

Sources: HDFC; BNP Paribas estimates

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All share prices are as at market close on 21 January 2008 unless otherwise stated. Stock recommendations are based on absolute upside (downside), which we define as $(\text{target price} - \text{current price}) / \text{current price}$. If the upside is 10% or more, the recommendation is BUY. If the downside is 10% or more, the recommendation is REDUCE. For stocks where the upside or downside is less than 10%, the recommendation is HOLD. In addition, we have key buy and key sell lists in each market, which are our most commercial and/or actionable BUY and REDUCE calls and are limited to at most five key buys and five key sells in each market at any point in time.

Unless otherwise specified, these recommendations are set with a 12-month horizon. Thus, it is possible that future price volatility may cause a temporary mismatch between upside/downside for a stock based on market price and the formal recommendation.

*In most cases, the target price will equal the analyst's assessment of the current fair value of the stock. However, if the analyst doesn't think the market will reassess the stock over the specified time horizon due to a lack of events or catalysts, then the target price may differ from fair value. In most cases, therefore, our recommendation is an assessment of the mismatch between current market price and our assessment of current fair value.

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