

May 08, 2013

|                         |                      |
|-------------------------|----------------------|
| <b>Rating</b>           | <b>Previous Reco</b> |
| Reduce                  | Reduce               |
| <b>CMP</b>              | <b>Target Price</b>  |
| Rs886                   | Rs760                |
| EPS Chg FY13E/FY14E (%) | NA                   |
| Target Price change (%) | NA                   |
| Nifty                   | 6,069                |
| Sensex                  | 19,990               |

**Price Performance**

|               |    |    |    |     |
|---------------|----|----|----|-----|
| (%)           | 1M | 3M | 6M | 12M |
| Absolute      | 11 | 5  | 7  | 29  |
| Rel. to Nifty | 3  | 4  | 1  | 9   |

Source: Bloomberg

**Relative price chart**



Source: Bloomberg

**Stock Details**

|                             |                              |
|-----------------------------|------------------------------|
| Sector                      | Banking & Financial Services |
| Bloomberg                   | HDFC IB                      |
| Equity Capital (Rs mn)      | 3,093                        |
| Face Value(Rs)              | 2                            |
| No of shares o/s (mn)       | 1,546                        |
| 52 Week H/L                 | 885/ 611                     |
| Market Cap (Rs bn/USD mn)   | 1,320/ 24,384                |
| Daily Avg Volume (No of sh) | 2,666,494                    |
| Daily Avg Turnover (US\$m)  | 39.7                         |

**Shareholding Pattern (%)**

|              |        |        |        |
|--------------|--------|--------|--------|
|              | Mar'13 | Dec'12 | Sep'12 |
| Promoters    | N/A    | N/A    | N/A    |
| FII/NRI      | 73.7   | 73.2   | 68.7   |
| Institutions | 13.2   | 13.8   | 18.0   |
| Private Corp | 2.9    | 3.1    | 3.1    |
| Public       | 10.2   | 9.9    | 10.1   |

Source: Bloomberg

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- **HDFC Q4FY13 NII at Rs18.9bn (+13% yoy) driven by higher than expected decline in cost of IBL\*. Also with steep rise in fee income and modest expenses, PAT came in at Rs15.5bn**
- **Growth in interest income has eased to 16% yoy vs 30% yoy for past 8-quarters, reflecting pricing pressure. The same however is off-set by over 77bps decline in IBL over H2FY13**
- **Loan growth remains buoyant at 21% yoy and is driven by 25% yoy growth in individual loans. Disbursements grew 16% yoy. Continue to build in margin contraction over FY13-15E**
- **In the back-drop of easing core-mortgage RoE profile, we expect valuation multiple to ease. Additional with impending risk to earnings, we retain Reduce with a tp of Rs760**

\* Interest bearing liabilities

**Results aided by higher non-interest income and cost benefits**

HDFC Q4FY13 NII at Rs18.9bn (+13% yoy) beat our estimates of Rs18.3bn and was driven by yet another quarter of higher than expected decline in cost of funds. Cost of interest bearing liabilities have declined by 77bps in H2FY13 (owing to change in borrowing mix and easing interest rate regime) and has thereby enabled improvement in spreads (calc) to 3% for Q4FY13. However, growth in interest income has moderated to 16% yoy for Q4FY13 vs 20% in Q3 and higher 25%+yoy for past 4-quarters, clearly reflecting pricing pressures. Non-interest income too came in as surprise (especially fee income which grew 47% yoy) and with mere 9% yoy growth in operating expenses, net profit at Rs15.5bn grew 17% yoy. Asset quality continues to remain stable with GNPA at 0.7% and provisioning at Rs17.9bn (1.1% of loans).

**On the balance sheet side:** Loan portfolio (including sell-down to HDFC Bank) grew by a healthy 24% yoy. On a net-basis, the run-rate stood at 21% yoy and was aided by 25% yoy growth in individual loans. Non-retail loans (ie corporates + others) grew 12% yoy / 5% qoq. Disbursements during Q4 grew 8% yoy / 14% qoq. For FY13, disbursements were up 16% yoy.

**Exhibit 1: Yield analysis**

| %                         | Q4FY12 | Q1FY13 | Q2FY13 | Q3FY13 | Q4FY13 | YoY | QoQ |
|---------------------------|--------|--------|--------|--------|--------|-----|-----|
|                           |        |        |        |        |        | bps | bps |
| Yield on advances         | 13.6   | 12.9   | 12.8   | 12.6   | 12.9   | -63 | 28  |
| Yield on earning funds    | 12.4   | 11.8   | 11.6   | 11.6   | 11.9   | -48 | 34  |
| Yield on total assets     | 11.5   | 10.9   | 10.9   | 11.0   | 11.3   | -24 | 29  |
| Cost of int bearing liab. | 8.8    | 9.6    | 9.7    | 9.5    | 8.9    | 11  | -55 |
| Cost of funds             | 7.3    | 7.9    | 8.0    | 7.7    | 7.3    | -6  | -48 |
| Spread                    | 3.6    | 2.2    | 1.9    | 2.1    | 3.0    | -59 | 90  |
| Spread (reported)         | 2.3    | 2.3    | 2.3    | 2.3    | 2.3    | 3   | 2   |
| NIM (calc)                | 4.2    | 2.9    | 2.9    | 3.2    | 4.0    | -18 | 77  |

Source: Company, Emkay Research

**Financial Snapshot (Standalone)**

(Rsmn)

| Y/E   | Net    | Net    | EPS  | ABV   | RoA | RoE  | PE   | P/ABV |
|-------|--------|--------|------|-------|-----|------|------|-------|
| Mar   | Income | Profit | (Rs) | (Rs)  | (%) | (%)  | (x)  | (x)   |
| FY12A | 59,273 | 41,226 | 26.6 | 127.2 | 2.6 | 21.6 | 33.3 | 7.0   |
| FY13A | 69,412 | 48,483 | 29.8 | 159.8 | 2.6 | 21.0 | 29.7 | 5.5   |
| FY14E | 81,441 | 56,519 | 34.6 | 180.6 | 2.6 | 20.1 | 25.5 | 4.9   |
| FY15E | 93,414 | 64,249 | 39.6 | 202.2 | 2.6 | 20.4 | 22.3 | 4.4   |

**Exhibit 2: Key financials- Quarterly**

| Rs mn                     | Q4FY12 | Q1FY13 | Q2FY13 | Q3FY13 | Q4FY13 | YoY (%) | QoQ (%) | YTD'13 | YTD'12 | YoY (%) |
|---------------------------|--------|--------|--------|--------|--------|---------|---------|--------|--------|---------|
| Net Interest Income       | 16,808 | 12,582 | 12,941 | 14,757 | 18,994 | 13.0    | 28.7    | 59,275 | 49,983 | 18.6    |
| Other Income              | 1,922  | 2,756  | 3,476  | 1,569  | 2,336  | 21.5    | 48.9    | 10,137 | 9,290  | 9.1     |
| Net Income                | 18,730 | 15,339 | 16,417 | 16,326 | 21,330 | 13.9    | 30.6    | 69,412 | 59,273 | 17.1    |
| Total Operating Exp       | 971    | 1,294  | 1,421  | 1,380  | 1,059  | 9.0     | -23.3   | 5,153  | 4,313  | 19.5    |
| <i>As % Of Net Income</i> | 5.2    | 8.4    | 8.7    | 8.5    | 5.0    |         |         | 7.4    | 7.3    |         |
| Employee Expenses         | 497    | 609    | 621    | 642    | 590    | 18.9    | -8.0    | 2,462  | 2,058  | 19.6    |
| <i>As % Of Net Income</i> | 2.7    | 4.0    | 3.8    | 3.9    | 2.8    |         |         | 3.5    | 3.5    |         |
| Other Expenses            | 365    | 510    | 555    | 584    | 286    | -21.7   | -51.1   | 1,934  | 1,730  | 11.8    |
| <i>As % Of Net Income</i> | 1.9    | 3.3    | 3.4    | 3.6    | 1.3    |         |         | 2.8    | 2.9    |         |
| Operating Profit          | 17,701 | 13,997 | 14,940 | 14,888 | 20,198 | 14.1    | 35.7    | 64,023 | 54,754 | 16.9    |
| <i>As % Of Net Income</i> | 94.5   | 91.3   | 91.0   | 91.2   | 94.7   |         |         | 92.2   | 92.4   |         |
| Provisions                | 250    | 400    | 400    | 400    | 250    | 0.0     | -37.5   | 1,450  | 800    | 81.3    |
| PBT                       | 18,241 | 13,799 | 15,481 | 15,451 | 20,997 | 15.1    | 35.9    | 65,728 | 56,656 | 16.0    |
| Total Tax                 | 4,980  | 3,780  | 3,970  | 4,050  | 5,445  | 9.3     | 34.4    | 17,245 | 15,430 | 11.8    |
| Adjusted PAT              | 12,687 | 9,872  | 10,811 | 10,690 | 14,775 | 16.5    | 38.2    | 46,149 | 39,254 | 17.6    |
| Extra Ordinary Items      | -791   | -202   | -941   | -963   | -1,049 | 32.7    | 8.9     | -3,156 | -2,702 |         |
| Reported PAT              | 13,261 | 10,019 | 11,511 | 11,401 | 15,552 | 17.3    | 36.4    | 48,483 | 41,226 | 17.6    |
| Reported EPS              | 8.6    | 6.7    | 7.0    | 6.9    | 9.6    | 11.0    | 37.7    | 30.2   | 26.7   | 13.4    |

Source: Company, Emkay Research

## Key highlights

- Incremental loan mix in favor of non-retail loans:** Q4FY13 loan growth at 5.4% qoq was led by healthy growth on both retail (+6% qoq) and non-retail front (+5% qoq). However, on an incremental basis, the growth was largely in nature of non-retail loans which comprised 19% of total loans vs 15% for Q3FY13. Management guided for improved outlook on disbursements across all segments. We have thereby factored in 18% CAGR in disbursements over FY13-15E.
- ... steep rise in fee income is unexplainable:** Unlike previous two quarters of qoq decline in fee income due to withdrawal of pre-payment penalty charges and lower disbursements, Q4FY13 fee income at Rs879mn (+47% yoy) came in as surprise. While management guided for such higher levels of fee income to incremental disbursements in Q4FY13 towards non-retail loans, we fail to understand the same as on a qoq basis, disbursements are up mere 14%. Non-interest income was also aided by higher than expected dividend income from subsidiaries.
- Our contention on margin maintenance continues:** Change in borrowing mix towards bonds / debentures (since Q2FY13) and the soft interest regime (especially in H2FY13) enabled HDFC witness margin improvement in H2FY13. However, growth in core operational line item ie interest income has moderated to 16% yoy for Q4FY13 vs 20% yoy for Q3FY13 and 25%+ yoy for past 4-quarters, clearly reflecting pricing pressures. We believe that even as liability re-pricing benefits would persists, lending yields are set to ease further in CY13 due to a) increasing competition in the individual mortgage space and b) declining appetite towards high yielding corporate loans. We thereby expect NIM to ease to 3.2% over FY13-15E
- Asset quality concerns remains low; cumulative provisioning at 1.1% of loans:** Asset quality remains comfortable with overall GNPA at 0.7%. GNPA in the retail space have declined to 0.58% vs 0.61% in Q3FY13, while GNPA in non-individuals segment have remained constant at 0.91% qoq. Cumulative provisioning stood at Rs17.9bn (1.1% of loans) including NPA provisioning of Rs5.0bn and balance towards contingencies and teaser loan provisioning.

### Valuations and view

Easing interest rate regime coupled with change in borrowing mix towards bonds / debentures have enabled margin improvement even as growth in interest income has moderated to 16% yoy vs 30% yoy for past 8-quarters. Going forward, even as cost benefits due to re-pricing of liabilities would persist, margin maintenance would be a challenge given pressure on asset re-pricing. We have retained our earnings largely intact and are now factoring in 15% CAGR in each NII / PAT over FY13-15E. Core-mortgage RoE has averaged 35% over the past 5-years and is thereby reflected in 1-year forward PB (5-year avg) at 4.5x for the same period. However, in the backdrop of easing RoE profile, we expect valuation multiple to ease lower.

With impending risk to earnings growth and increasing competition, we continue to retain our REDUCE rating with target price of Rs 760. However, within the BFSI space, mortgage companies remain the safe bet given their strong earnings visibility, limited NPA and reasonable valuations vis-à-vis PSU / private banks currently grappling with concerns over asset quality, capital requirement or regulatory requirements.

**Exhibit 3: Loan mix – growth witnessed across all segments**

| Rs mn                 | Q4FY12           | Q1FY13           | Q2FY13           | Q3FY13           | Q4FY13           | YoY (%)     | QoQ (%)    |
|-----------------------|------------------|------------------|------------------|------------------|------------------|-------------|------------|
| <b>Loan portfolio</b> | <b>1,404,216</b> | <b>1,482,623</b> | <b>1,551,270</b> | <b>1,609,410</b> | <b>1,695,710</b> | <b>20.8</b> | <b>5.4</b> |
| - Individuals         | 887,779          | 954,129          | 994,010          | 1,052,370        | 1,113,210        | 25.4        | 5.8        |
| - Corporate           | 501,896          | 509,977          | 537,630          | 539,350          | 569,550          | 13.5        | 5.6        |
| - Others              | 19,071           | 18,517           | 19,630           | 17,690           | 12,950           | -32.1       | -26.8      |
| <b>% of total</b>     | <b>100.3</b>     | <b>100.0</b>     | <b>100.0</b>     | <b>100.0</b>     | <b>100.0</b>     |             |            |
| - Individuals         | 63.2             | 64.4             | 64.1             | 65.4             | 65.6             |             |            |
| - Corporate           | 35.7             | 34.4             | 34.7             | 33.5             | 33.6             |             |            |
| - Others              | 1.4              | 1.2              | 1.3              | 1.1              | 0.8              |             |            |

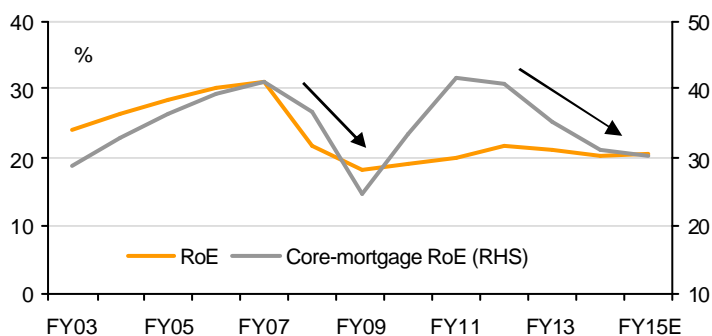
Source: Company, Emkay Research

**Exhibit 4: Borrowing profile.**

| Rs mn                           | Q4FY12           | Q1FY13           | Q2FY13           | Q3FY13           | Q4FY13           | YoY (%)     | QoQ (%)    |
|---------------------------------|------------------|------------------|------------------|------------------|------------------|-------------|------------|
| <b>Borrowings</b>               | <b>1,391,275</b> | <b>1,438,116</b> | <b>1,477,900</b> | <b>1,488,700</b> | <b>1,588,280</b> | <b>14.2</b> | <b>6.7</b> |
| - Term loans                    | 406,966          | 374,844          | 197,240          | 136,400          | 178,240          | -56.2       | 30.7       |
| - Bonds, debentures, FCCB & CPs | 621,381          | 663,838          | 798,040          | 854,670          | 890,710          | 43.3        | 4.2        |
| - Deposits                      | 362,928          | 399,434          | 482,620          | 497,630          | 519,330          | 43.1        | 4.4        |
| <b>% of total</b>               | <b>100.0</b>     | <b>100.0</b>     | <b>100.0</b>     | <b>100.0</b>     | <b>100.0</b>     |             |            |
| - Term loans                    | 29.3             | 26.1             | 13.3             | 9.2              | 11.2             |             |            |
| - Bonds, debentures, FCCB & CPs | 44.7             | 46.2             | 54.0             | 57.4             | 56.1             |             |            |
| - Deposits                      | 26.1             | 27.8             | 32.7             | 33.4             | 32.7             |             |            |

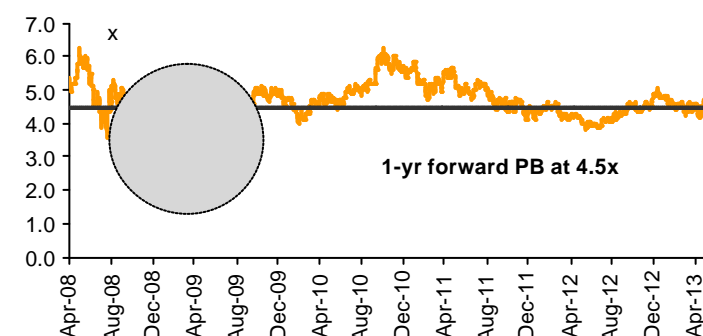
Source: Company, Emkay Research

**Exhibit 5: Trend in RoE and core-mortgage RoE**



Source: Company, Emkay Research

**Exhibit 6: 1-yr forward PB averaged 4.5x for past 5-years**



Source: Company, Emkay Research

**Exhibit 7: SOTP valuation**

|  | <b>Basis</b> | <b>Period</b> | <b>Rs m</b> | <b>Multiple (x)</b> | <b>Stake (%)</b> | <b>% in total</b> | <b>Value/sh (Rs)</b> |
|--|--------------|---------------|-------------|---------------------|------------------|-------------------|----------------------|
| Standalone                                   | BV           | FY15ii        | 224,884     | 3.0                 | 100.0            | 57.4              | 438                  |
| HDFC Bank stake<br>(20% holding co discount) | BV           | FY15ii        | 535,770     | 2.8                 | 23.4             | 29.9              | 228                  |
| HDFC Standard Life                           | EV+NBAP      | FY13ii        | 119,840     | 12.0                | 72.4             | 7.4               | 56                   |
| HDFC General Ins                             | PAT          | FY13ii        | 604         | 10.0                | 74.0             | 0.4               | 3                    |
| HDFC AMC                                     | AUM          | FY13          | 1,021,420   | 5.0                 | 60.0             | 2.6               | 20                   |
| HDFC Venture Cap                             | AUM          | FY13ii        | 19,367      | 10.0                | 80.5             | 0.1               | 1                    |
| Gruh Finance (20% discount)                  | Mkt val      |               | 38,620      | 0.8                 | 60.6             | 1.6               | 12                   |
| Unrealised gains - Others                    | Mkt val      |               | 8,000       | 1.0                 |                  | 0.7               | 5                    |
| <b>Total</b>                                 |              |               |             |                     |                  | <b>100</b>        | <b>760</b>           |

Source: Emkay Research

## Key Financials

## Income Statement

| Y/E Mar (Rsmn)             | FY12A         | FY13P         | FY14E         | FY15E         |
|----------------------------|---------------|---------------|---------------|---------------|
| <b>Net interest income</b> | <b>49,983</b> | <b>59,275</b> | <b>67,660</b> | <b>77,722</b> |
| Other income               | 9,290         | 10,137        | 13,781        | 15,691        |
| Net income                 | 59,273        | 69,412        | 81,441        | 93,414        |
| Operating expenses         | 4,519         | 5,389         | 6,447         | 7,485         |
| Pre provision profit       | 54,754        | 64,023        | 74,994        | 85,929        |
| PPP excl treasury          | 54,754        | 64,023        | 74,994        | 85,929        |
| Provisions                 | 800           | 1,450         | 2,372         | 2,827         |
| <b>Profit before tax</b>   | <b>56,656</b> | <b>65,728</b> | <b>76,622</b> | <b>87,102</b> |
| Tax                        | 15,430        | 17,245        | 20,103        | 22,853        |
| Tax rate                   | 28.6          | 27.6          | 27.7          | 27.5          |
| Profit after tax           | 41,226        | 48,483        | 56,519        | 64,249        |

## Balance Sheet

| Y/E Mar (Rsmn)      | FY12A     | FY13P     | FY14E     | FY15E     |
|---------------------|-----------|-----------|-----------|-----------|
| <b>Liabilities</b>  |           |           |           |           |
| Equity              | 2,954     | 3,093     | 3,093     | 3,093     |
| Reserves            | 187,222   | 246,907   | 279,656   | 313,826   |
| Net worth           | 190,176   | 250,000   | 282,749   | 316,919   |
| Borrowings          | 1,391,275 | 1,588,280 | 1,834,463 | 2,146,322 |
| Current liabilities | 93,749    | 97,543    | 108,060   | 117,689   |
| Total liabilities   | 1,675,199 | 1,935,823 | 2,225,272 | 2,580,930 |
| <b>Assets</b>       |           |           |           |           |
| Cash and bank       | 124,910   | 84,689    | 84,463    | 84,248    |
| Investments         | 122,070   | 136,135   | 130,287   | 133,678   |
| Customer assets     | 1,408,746 | 1,695,710 | 1,992,200 | 2,345,554 |
| Others              | 19,474    | 19,289    | 18,321    | 17,450    |
| Total assets        | 1,675,199 | 1,935,823 | 2,225,272 | 2,580,930 |

## Key Ratio (%)

| Y/E Mar (Rsmn)        | FY12A | FY13P | FY14E | FY15E |
|-----------------------|-------|-------|-------|-------|
| NIM                   | 3.3   | 3.3   | 3.3   | 3.2   |
| Non-Il/avg assets     | 0.6   | 0.6   | 0.7   | 0.7   |
| Fee income/avg assets | 0.0   | 0.0   | 0.0   | 0.0   |
| Opex/avg assets       | 0.3   | 0.3   | 0.3   | 0.3   |
| Provisions/avg assets | 0.1   | 0.1   | 0.1   | 0.1   |
| PBT/avg assets        | 3.7   | 3.6   | 3.7   | 3.6   |
| Tax/avg assets        | 1.0   | 1.0   | 1.0   | 1.0   |
| RoA                   | 2.6   | 2.6   | 2.6   | 2.6   |
| RoAE                  | 21.6  | 21.0  | 20.1  | 20.4  |
| GNPA (%)              | 0.8   | 0.9   | 0.9   | 0.9   |
| NNPA (%)              | 0.2   | 0.2   | 0.2   | 0.2   |

## Valuation Table

| Y/E Mar               | FY12A  | FY13P  | FY14E  | FY15E  |
|-----------------------|--------|--------|--------|--------|
| Net profit (Rs mn)    | 41,226 | 48,483 | 56,519 | 64,249 |
| Shares in issue (mn)  | 1,477  | 1,546  | 1,546  | 1,546  |
| EPS (Rs)              | 26.6   | 29.8   | 34.6   | 39.6   |
| PER (x)               | 33.3   | 29.7   | 25.5   | 22.3   |
| FDEPS(Rs)             | 26.6   | 29.8   | 34.6   | 39.6   |
| FDPER (x)             | 33.3   | 29.7   | 25.5   | 22.3   |
| Book value (Rs)       | 128.8  | 161.7  | 182.8  | 204.9  |
| P/BV (x)              | 6.9    | 5.5    | 4.8    | 4.3    |
| Adj book value (Rs)   | 127.2  | 159.8  | 180.6  | 202.2  |
| P/ABV (x)             | 7.0    | 5.5    | 4.9    | 4.4    |
| Core mortgage RoE (%) | 40.8   | 35.1   | 31.0   | 30.2   |
| Dividend yield (%)    | 1.2    | 1.4    | 1.5    | 1.6    |

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