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Loan growth of 20.7%, skewed towards retail

Quick Note

May 8, 2013

Rating Remains	**Neutral**
Target price Remains	INR 780
Closing price May 8, 2013	INR 885

HDFC reported 4QFY13 earnings that were in line with our expectations, with PAT of INR15.5bn vs our INR15.5bn estimate (Street at INR14.8bn) - a y-y growth rate of 17.3%. Loan growth was 20.7% y-y with net interest spread of 2.3%. The in-line PAT vs our estimate was driven by lower net interest income, higher non-interest income, lower costs and lower provisions.

Key highlights from 4QFY13 were:

- Overall loan growth of 20.7% y-y was driven by 25.4% y-y growth in retail loans and 13.5% growth in corporate loans. HDFC sold loans to the tune of INR16.4bn during the quarter and gross of this sell-down, retail loan growth would be 31% y-y and overall loan growth of 24% y-y.
- Net interest income of INR19.2bn (y-y growth of 13.3%) was driven by spreads of 2.3% (2.28% in 3QFY13 respectively). Spreads on individual loans for FY13 stand at 1.96% and corporate loans at 2.94% (1.95% and 2.79% respectively in 9MFY13). Non-interest income of INR3.4bn (y-y growth of 24.8%), vs our estimate of INR2.9bn was higher on account of strong growth in core fee income, treasury income and dividend income.
- Total provisions came in at INR250mn versus our expected INR400mn (flat y-y). GNPL ratio declined 5bps to 0.7% (0.75% in 3QFY13). GNPL ratio for individual loans stands at 0.58% and corporate loans stands at 0.91%.
- Total CAR was 16.2% - with tier-1 at 13.8%.
- Prepayment/repayment as a % of 12-month loan book increased marginally. Our analysis detailed in Fig. 6 indicates that while prepayments / repayments (excluding loans sold down) were relatively high at 40.9% (on a 12m lagged loan book) in June 2010, the ratio trended down gradually to reach the 34.1% level in March 2013.
- Loans sold as a proportion of the loan book which has been in the 9.4-10.5% range for the past few quarters, closed at 10% in 4QFY13 (flat q/q).
- HDFC has reduced the zero coupon bond borrowing from INR80bn at the beginning of FY13 to INR50bn by the end of the year by using the proceeds from the warrant conversion. The company has increased the proportion of bonds in its funding mix through FY13 at the cost of bank loans due to more favorable market borrowing costs.
- HDFC is carrying INR17.92bn as provisions on its book as against a regulatory requirement of INR15.06bn. The provisions break-up is as follows - standard provisions of INR8.49bn, provisions against dual rate loans of INR2.7bn, specific provisions of INR3.87bn and excess provisions of INR2.86bn.
- Loan growth guidance for FY14F continues to be 20% and the incremental mix between retail & developer loans will evolve depending on market conditions.

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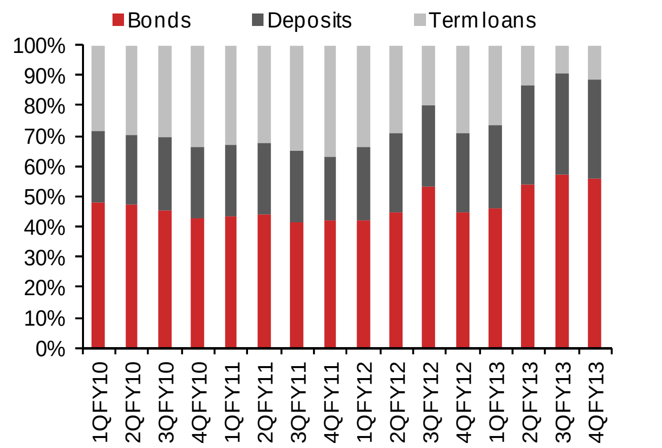
See Appendix A-1 for analyst certification, important disclosures and the status of non-US analysts.

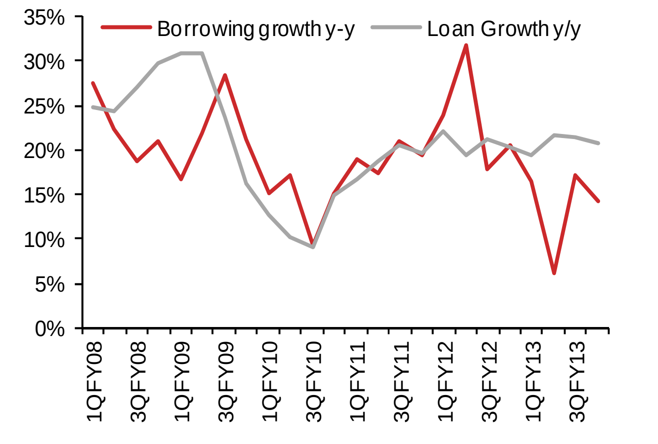
Valuation: HDFC currently trades at 3.7x our FY14F ABV of INR180.7and 19.9x our FY14F EPS of INR33.6

Fig. 1: Funding mix



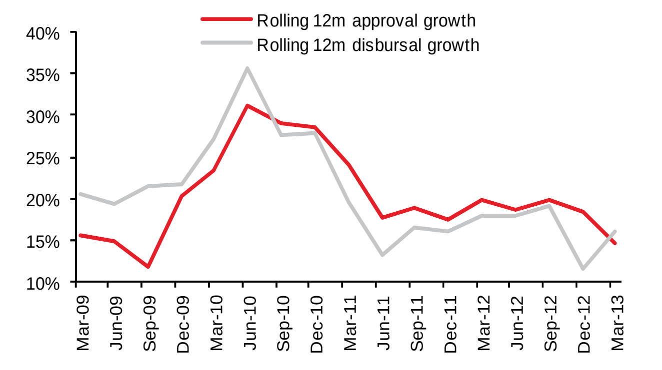
Source: Company data, Nomura research

Fig. 2: Loan growth vs borrowing growth



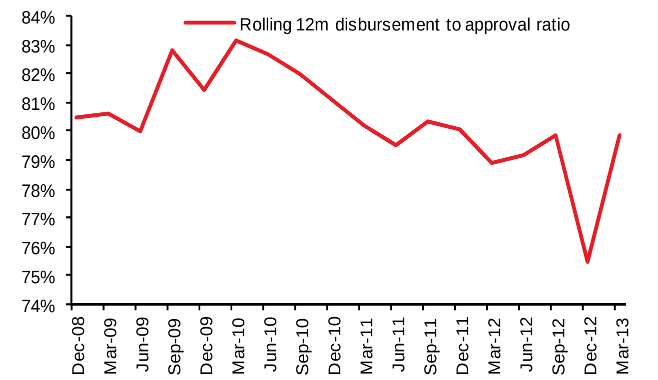
Source: RBI, Company data, Nomura research

Fig. 3: Rolling 12mn disbursement growth lower than approval growth



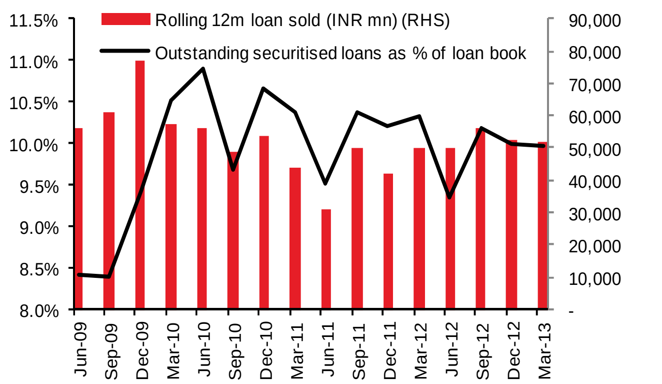
Source: Company data, Nomura research

Fig. 4: Rolling 12m disbursement to approval ratio



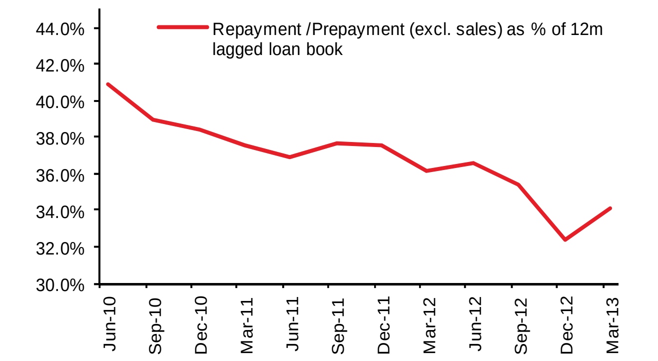
Source: Company data, Nomura research

Fig. 5: Rolling 12m loans sold vs securitised loans as % of loan book



Source: Company data, Nomura research

Fig. 6: Repayment / prepayment (excl. sales) as % of 12m lagged loan book



Source: Company data, Nomura research

Fig. 7: Earnings summary

Earnings summary (INR mn)	4QFY13	3QFY13	4QFY12	%y/y	%q/q	4QFY13F	Variance %
Interest Earned	53,392.3	49,971.6	46,197.6	15.6	6.8	56,012.4	(4.7)
Interest on loans	50,984.9	48,432.5	44,593.5	14.3	5.3	54,586.8	(6.6)
Interest from treasury	2,407.4	1,539.1	1,604.1	50.1	56.4	1,425.5	68.9
Interest expended	34,174.0	34,987.9	29,228.7	16.9	(2.3)	35,401.2	(3.5)
Net interest income	19,218.3	14,983.7	16,968.9	13.3	28.3	20,611.1	(6.8)
Non-interest income	3,384.8	2,532.4	2,712.6	24.8	33.7	2,881.1	17.5
Fee income	879.4	391.3	600.1	46.5	124.7	461.6	90.5
Surplus from deployment in Cash mgmt schemes	513.5	632.1	625.7	(17.9)	(18.8)	725.3	(29.2)
Treasury income	1,048.8	963.2	790.6	32.7	8.9	925.9	13.3
Dividend income	814.3	451.8	615.1	32.4	80.2	585.1	39.2
Total Net income	22,603.1	17,516.1	19,681.5	14.8	29.0	23,492.2	(3.8)
Operating expense	1,356.0	1,665.1	1,190.2	13.9	(18.6)	1,639.9	(17.3)
Employee cost	590.4	642.0	496.5	18.9	(8.0)	681.3	(13.3)
Other Finance Charges	224.3	226.6	160.6	39.7	(1.0)	194.7	15.2
Operating & Administrative costs	468.3	737.6	474.4	(1.3)	(36.5)	704.8	(33.6)
Depreciation	73.0	58.9	58.7	24.4	23.9	59.2	23.4
Pre-prov operating profit	21,247.1	15,851.0	18,491.3	14.9	34.0	21,852.3	(2.8)
Provisions & Contingencies	250.0	400.0	250.0	-	(37.5)	400.1	(37.5)
PBT	20,997.1	15,451.0	18,241.3	15.1	35.9	21,452.2	(2.1)
Tax Provisions	5,445.0	4,050.0	4,980.0	9.3	34.4	5,899.4	(7.7)
Adjusted net profit	15,552.1	11,401.0	13,261.3	17.3	36.4	15,552.9	(0.0)
EPS	10.0	7.3	8.8	12.6	36.5	9.9	0.1

Source: Company data, Nomura estimates

Fig. 8: Loan book breakdown

Loan Break-up (INR mn)	4QFY13	3QFY13	4QFY12	%y/y	%q/q
Individuals	1,113,210.0	1,052,372.4	887,778.5	25.4	5.8
Corporate Bodies	569,550.0	539,348.7	501,896.0	13.5	5.6
Others	17,700.0	17,692.0	19,071.3	(7.2)	0.0
Total Loans	1,700,460.0	1,604,343.1	1,408,745.8	20.7	6.0
Approvals	292,600.0	229,557.0	270,460.4	8.2	27.5
Disbursements	274,520.0	141,437.9	212,415.9	29.2	94.1

Source Company data, Nomura research

Fig. 9: Key ratios

Key Ratios	4QFY13	3QFY13	4QFY12	y/y bps	q/q bps
Reported spread, %	2.30	2.28	2.27	3	2
Total CAR, %	16.2	17.5	14.6	160	(130)
Tier I, %	13.8	14.9	11.7	210	(110)
Cost-income ratio, %	6.0	9.5	6.0	(5)	(351)
Cost-asset ratio, %	0.30	0.39	0.31	(1)	(9)
Gross NPA, %	0.70	0.75	0.75	(5)	(6)

Source: Company data, Nomura research

Appendix A-1

Analyst Certification

We, Vijay Sarathi, Abhishek Bhattacharya and Amit Nanavati, hereby certify (1) that the views expressed in this Research report accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Research report, (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Research report and (3) no part of our compensation is tied to any specific investment banking transactions performed by Nomura Securities International, Inc., Nomura International plc or any other Nomura Group company.

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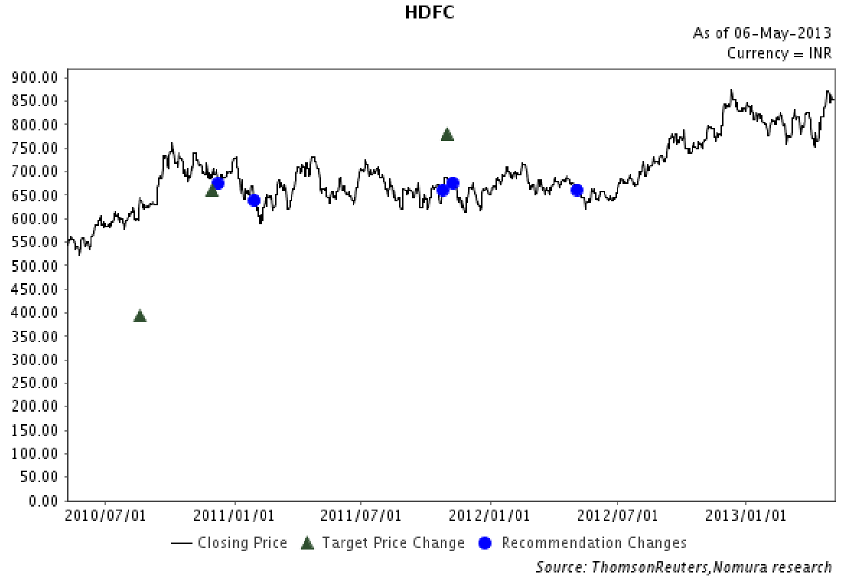
Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
HDFC	HDFC IN	INR 885	08-May-2013	Neutral	Not rated	A6,A13

A6 The Nomura Group expects to receive or intends to seek compensation for investment banking services from the issuer in the next three months.

A13 The Nomura Group has a significant financial interest (non-equity) in the issuer.

HDFC (HDFC IN) **INR 885 (08-May-2013)** Neutral (Sector rating: Not rated)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
26-Apr-12	Neutral		674.10
31-Oct-11	Buy		688.85
31-Oct-11		780.00	688.85
17-Oct-11	Not Rated		673.45
21-Jan-11	Suspended		651.20
30-Nov-10	Neutral		686.65
30-Nov-10		660.00	686.65
19-Aug-10		394.00	645.05

For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value HDFC's core mortgage business at INR555 and its subsidiaries at INR225 to arrive at our SOTP-based TP of INR780. At our TP, HDFC would trade at 3.1x our FY14F ABV of INR180.7 and 16.5x our FY14F EPS of INR33.6.

Risks that may impede the achievement of the target price Accelerated monetary policy easing, higher than expected domestic economic growth and value unlocking in the life insurance subsidiary are key upside catalysts. The potential downside risks are a relative tight money policy, regulatory uncertainty and heightened global macro risks.

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