

July 11, 2012

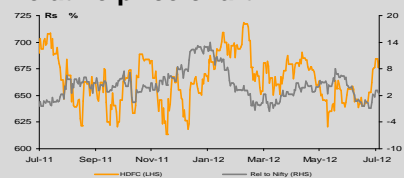
| Rating | Previous Reco |
|-------------------------|---------------|
| Hold | Hold |
| CMP | Target Price |
| Rs679 | Rs700 |
| EPS Chg FY13E/FY14E (%) | NA |
| Target Price change (%) | NA |
| Nifty | 5,306 |
| Sensex | 17,489 |

Price Performance

| (%) | 1M | 3M | 6M | 12M |
|---------------|----|----|----|-----|
| Absolute | 3 | 1 | 0 | -4 |
| Rel. to Nifty | -1 | -1 | -8 | 2 |

Source: Bloomberg

Relative price chart



Source: Bloomberg

Stock Details

| | |
|-----------------------------|------------------------------|
| Sector | Banking & Financial Services |
| Bloomberg | HDFC IB |
| Equity Capital (Rs mn) | 2,979 |
| Face Value(Rs) | 2 |
| No of shares o/s (mn) | 1,489 |
| 52 Week H/L | 726/ 600 |
| Market Cap (Rs bn/USD mn) | 1,011/ 18,248 |
| Daily Avg Volume (No of sh) | 2,490,443 |
| Daily Avg Turnover (US\$mn) | 29.5 |

Shareholding Pattern (%)

| | Mar12 | Dec11 | Sep11 |
|--------------|-------|-------|-------|
| Promoters | N/A | N/A | N/A |
| FII/NRI | 65.8 | 59.0 | 58.2 |
| Institutions | 20.1 | 28.7 | 29.1 |
| Private Corp | 2.9 | 1.7 | 1.8 |
| Public | 11.1 | 10.6 | 11.0 |

Source: Bloomberg

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- HDFC Q1FY13 NII at Rs12.6bn / rep. PAT – Rs10bn - inline with our estimates. Individual loan portfolio grew 22.5% yoy and have alleviated fears of intensifying competition
- Lower share of corporate loans was off-set by upward re-pricing of teaser loan portfolio, thereby protecting spreads at 2.27% levels. Borrowings largely in nature of bonds / deposits
- Minimal concerns on NPA; cumulative provisioning at 1.2% of loans. With stringent credit appraisal system factoring sub-10bps of credit cost. Adequately capitalized for growth
- Steady loan growth, stable margins and lower credit cost to ensure RoA in excess of 2.5%. Current valuations leave limited room for upside. Maintain HOLD with tp of Rs700

No negative surprises on P&L; Forex translation hit by INR depreciation

HDFC Q1FY13 NII at Rs12.6bn and reported PAT – Rs10bn was largely inline with our estimates. However, adjusting for cross currency foreign translation loss of Rs4.5bn, NII growth would have remained flat yoy. Key highlights from the quarter were a) healthy 19.4% yoy growth in loan portfolio aided by 22.5% yoy growth in individual loans b) spreads at 2.27% sequentially and c) stable asset quality with adequate provisioning coverage. Operating profit at Rs14bn was up 19% yoy. With volatile capital market activities, profit on sale of investment stood at Rs200mn vs Rs869mn in Q1FY12. Asset quality continues to remain stable with GNPA at 0.79% and cumulative provisioning at Rs17.1bn (1.2% of loans).

Loan growth at 19.4% yoy (5.2% qoq) was largely driven by 22.5% yoy (7.5% qoq) growth in individual loans. Growth in sanctions / disbursements too remained healthy at 17% yoy / 19.5% yoy respectively. On the liabilities front, the corporation has resorted to bonds and retail deposits to meet its borrowing requirement.

Yield Analysis

| % | Q1FY12 | Q2FY12 | Q3FY12 | Q4FY12 | Q1FY13 | YoY bps | QoQ bps |
|------------------------|--------|--------|--------|--------|--------|---------|---------|
| Yield on advances | 11.6 | 12.3 | 12.9 | 13.5 | 12.9 | 121 | -68 |
| Yield on total assets | 10.4 | 10.9 | 11.6 | 12.4 | 11.7 | 135 | -63 |
| Yield on earning funds | 9.8 | 10.3 | 11.0 | 11.5 | 10.9 | 109 | -64 |
| Cost of borrowings | 8.2 | 8.6 | 9.6 | 8.6 | 9.4 | 120 | 85 |
| Cost of funds | 7.0 | 7.2 | 7.9 | 7.3 | 7.9 | 92 | 61 |
| Spread | 2.0 | 2.2 | 2.0 | 3.5 | 2.2 | 20 | -138 |
| Spread (reported) | 2.3 | 2.3 | 2.3 | 2.3 | 2.3 | -3 | 0 |
| NIM | 2.8 | 3.1 | 3.0 | 4.2 | 2.9 | 17 | -124 |

Source: Company, Emkay Research.

Financial Snapshot (Standalone)

(Rsmn)

| Y/E | Net Income | Net Profit | EPS (Rs) | ABV (Rs) | RoA (%) | RoE (%) | PE (x) | P/ABV (x) |
|-------|------------|------------|----------|----------|---------|---------|--------|-----------|
| Mar | | | | | | | | |
| FY11A | 49,584 | 35,350 | 24.1 | 116.8 | 2.8 | 21.7 | 28.2 | 5.8 |
| FY12A | 59,273 | 41,226 | 27.9 | 127.2 | 2.7 | 22.7 | 24.3 | 5.3 |
| FY13E | 69,617 | 47,565 | 31.3 | 176.1 | 2.6 | 20.6 | 21.7 | 3.9 |
| FY14E | 81,386 | 55,391 | 36.4 | 187.6 | 2.6 | 19.8 | 18.7 | 3.6 |

Exhibit 1: Key financials – Quarterly

| Rs mn | Q1FY12 | Q2FY12 | Q3FY12 | Q4FY12 | Q1FY13 | YoY (%) | QoQ (%) |
|----------------------|--------|--------|--------|--------|--------|---------|---------|
| Net Interest Income | 9,982 | 11,636 | 11,557 | 16,808 | 12,582 | 26.0 | -25.1 |
| Other Income | 2,922 | 2,282 | 2,164 | 1,922 | 2,756 | -5.7 | 43.4 |
| Net Income | 12,904 | 13,917 | 13,721 | 18,730 | 15,339 | 18.9 | -18.1 |
| Total Operating Exp | 1,087 | 1,191 | 1,065 | 971 | 1,294 | 19.1 | 33.3 |
| As % Of Net Income | 8.4 | 8.6 | 7.8 | 5.2 | 8.4 | | |
| Employee Expenses | 528 | 526 | 508 | 497 | 609 | 15.4 | 22.6 |
| As % Of Net Income | 4.1 | 3.8 | 3.7 | 2.7 | 4.0 | | |
| Other Expenses | 412 | 529 | 424 | 365 | 510 | 23.7 | 39.7 |
| As % Of Net Income | 3.2 | 3.8 | 3.1 | 1.9 | 3.3 | | |
| Operating Profit | 11,773 | 12,678 | 12,603 | 17,701 | 13,997 | 18.9 | -20.9 |
| As % Of Net Income | 91.2 | 91.1 | 91.8 | 94.5 | 91.3 | | |
| Provisions | 180 | 170 | 200 | 250 | 400 | NA | 60.0 |
| PBT | 11,755 | 13,377 | 13,283 | 18,241 | 13,797 | 17.4 | -24.4 |
| Total Tax | 3,310 | 3,670 | 3,470 | 4,980 | 3,780 | 14.2 | -24.1 |
| Adjusted PAT | 8,328 | 9,077 | 9,162 | 12,687 | 9,871 | 18.5 | -22.2 |
| Extra Ordinary Items | -163 | -869 | -880 | -791 | -200 | | |
| Reported PAT | 8,445 | 9,707 | 9,813 | 13,261 | 10,017 | 18.6 | -24.5 |
| Reported EPS | 5.7 | 6.2 | 6.2 | 8.6 | 6.7 | 18.2 | -22.2 |

Source: Company, Emkay Research

NII growth adjusted for forex translation was lower at 2% yoy

While reported NII / net profit at Rs12.6bn and Rs10.0bn were up 26% yoy / 18.6% yoy respectively, adjusted for cross currency forex translation growth was actually lower.

Exhibit 2: Reported / adjusted NII and net profit

| Rs mn | Q1FY13 | Q4FY12 | Q1FY12 | % yoy |
|--------------------------------------|--------------|---------------|--------|-------|
| Other non-current assets | 3,008 | 1,404 | | |
| Other current assets (tax benefits) | 1,445 | 659 | | |
| Total | 4,452 | 2,062 | | |
| Increase in Other non-current assets | 1,604 | -1,402 | | |
| Increase in Other current assets | 786 | -682 | | |
| Increase in total | 2,390 | -2,084 | | |
| Reported NII | 12,582 | 16,808 | 9,982 | 26.0 |
| Adjusted NII | 10,192 | 18,892 | 9,982 | 2.1 |
| Reported PAT | 10,017 | 13,261 | 8,445 | 18.6 |
| Adjusted PAT | 8,413 | 14,664 | 8,445 | -0.4 |

Source: Emkay Research

Loan growth aided by individual segment; factoring 19% CAGR

Wide spread reach via penetration into smaller cities, customer friendly product portfolio including introduction of innovative schemes and easing competitive scenario vis-à-vis banks has clearly enabled HDFC score on the individual loans front. Q1FY13 loan growth at 19.4% yoy was largely aided by 22.5% yoy growth in individuals. The strong individual loan growth has partially alleviated fears of intensifying competition. The management hinted for increasing traction across tier-II to tier-IV cities. Metropolitan cities continue to report muted to marginally positive growth. Corporate loan portfolio grew 13.5% yoy, lowest in past several quarters. We believe this is one-off and unlikely to continue in coming quarters. We have factored 19% CAGR in disbursements / loans over FY12-14E. Repayment rate at sub-10% also provides comfort in terms of lower pre-payment by the customers.

... dual rate loan re-pricing + increasing corporate share to cushion margins

Q1FY13 NIM at 2.9% (up 17bps yoy) was aided by improved yields on advances and interest on liquid funds. We expect margins to inch upwards aided by re-pricing of dual rate loan portfolio and higher share of corporate loans.

Exhibit 3: Loan mix – 23% yoy growth in individual loans has alleviated fears of intensifying competition

| Rs mn | Q1FY12 | Q2FY12 | Q3FY12 | Q4FY12 | Q1FY13 | YoY (%) | QoQ (%) |
|-----------------------|------------------|------------------|------------------|------------------|------------------|-------------|------------|
| Loan portfolio | 1,241,677 | 1,269,924 | 1,322,079 | 1,408,746 | 1,482,623 | 19.4 | 5.2 |
| - Individuals | 778,860 | 802,680 | 842,999 | 887,779 | 954,129 | 22.5 | 7.5 |
| - Corporate | 448,233 | 451,442 | 461,609 | 501,896 | 509,977 | 13.8 | 1.6 |
| - Others | 14,585 | 15,802 | 17,472 | 19,071 | 18,517 | 27.0 | -2.9 |
| % of total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | | |
| - Individuals | 62.7 | 63.2 | 63.8 | 63.0 | 64.4 | | |
| - Corporate | 36.1 | 35.5 | 34.9 | 35.6 | 34.4 | | |
| - Others | 1.2 | 1.2 | 1.3 | 1.4 | 1.2 | | |

Source: Company, Emkay Research

Borrowings increasing in nature of bonds / retail deposits

HDFC had resorted for higher share of term loan from banks in Q4FY12. However, with competitive bond rates, the management increased the share of bonds, debenture and deposits to 74% of total borrowings vs 71% in Mar'12 and 66% in June'11. As at Mar'12, 84% of assets and 75% of liabilities were on floating rate basis. Capital infusion in Q2FY13 via conversion of warrants, will enable HDFC retire high cost borrowings.

Exhibit 4: Borrowing mix – Increasing reliance on bonds / deposit window

| Rs mn | Q1FY12 | Q2FY12 | Q3FY12 | Q4FY12 | Q1FY13 | YoY (%) | QoQ (%) |
|---------------------------------|------------------|------------------|------------------|------------------|------------------|-------------|------------|
| Borrowings | 1,235,187 | 1,251,027 | 1,270,962 | 1,391,275 | 1,438,116 | 16.4 | 3.4 |
| - Term loans | 414,279 | 323,243 | 249,829 | 406,966 | 374,844 | -9.5 | -7.9 |
| - Bonds, debentures, FCCB & CPs | 515,905 | 610,505 | 673,681 | 621,381 | 663,838 | 28.7 | 6.8 |
| - Deposits | 305,004 | 317,280 | 347,451 | 362,928 | 399,434 | 31.0 | 10.1 |
| % of total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | | |
| - Term loans | 33.5 | 25.8 | 19.7 | 29.3 | 26.1 | | |
| - Bonds, debentures, FCCB & CPs | 41.8 | 48.8 | 53.0 | 44.7 | 46.2 | | |
| - Deposits | 24.7 | 25.4 | 27.3 | 26.1 | 27.8 | | |

Source: Company, Emkay Research

Other key highlights from the quarter:

- Q1FY13 investment portfolio at Rs152bn was up 24% sequential with large part of incremental investments in nature of properties, government securities and liquid funds.
- Following AS11 requirement, HDFC has carried forward Rs4.4bn towards foreign exchange monetary translation. This amount will be amortized over the period of seven years.

Growth in non-interest income remains muted; C/Income still in low-10%

Non-int income at Rs2.8bn was down 6% yoy and was dragged by lower trading gains. Growth in fee income too remains lower at 8% yoy. With volatile capital market activities, profit on sale of investment stood at Rs200mn vs Rs869mn in Q1FY12. Cost-income continues to remain at healthy sub-10% levels.

Minimal NPA concerns; adequate capital for growth

Housing finance companies have scored over its peers ie banks on their stringent credit appraisal systems and collection process. HDFC Q1FY13 results provided comfort in terms stable NPA/ This is commendable given HDFC's higher exposure to risky asset class of corporate loans and fears over rising delinquencies in individual home loans. Q1FY13 GNPA at Rs11.9bn was up 11% qoq. However, the cumulative provisioning stood at Rs17.1bn (1.4% of NPA). As per the recent NHB directive, the teaser loan provision of ~Rs4.5bn will be reversed beginning Q1FY14. With effective asset quality checks we expect credit cost to remain lower at sub-10bps over FY13-14E. On the capital front, CAR at 14.6% including tier-I CAR at 11.8% provides room for growth.

Valuations and view

We continue to prefer housing finance space over banks in the mortgage business given their edge on sector expertise, asset quality controls and pricing power. HDFC has delivered another steady quarter with healthy 20% disbursement growth and robust 23% yoy growth in individual loans. Asset quality too remains comfortable with adequate provisioning. We expect the mortgage giant to report 19% CAGR in loan portfolio over FY12-14E. Margins are likely to remain stable at 3.2% range and would off-set credit cost requirement over FY13-14E thereby ensuring RoA in excess of 2.5%. We roll our estimates to FY14. However, current valuations leave limited room for upside. Maintain HOLD with target price of Rs700.

Exhibit 5: SOTP valuation

| | Basis | Period | Rs m | Multiple (x) | Stake (%) | % in total | Value/sh (Rs) |
|---|---------|--------|-----------|--------------|-----------|------------|---------------|
| Standalone | BV | FY14ii | 198,694 | 3.00 | 100.0 | 55.7 | 392 |
| HDFC Bank stake (80% holding co discount) | BV | FY14ii | 414,475 | 2.64 | 23.4 | 23.9 | 168 |
| HDFC Standard Life | EV+NBAP | FY14ii | 119,840 | 12.0 | 72.4 | 8.1 | 57 |
| HDFC General Ins | PAT | FY13ii | 604 | 10.00 | 74.0 | 0.4 | 3 |
| HDFC AMC | AUM | FY13ii | 1,160,395 | 5.0 | 60.0 | 3.3 | 23 |
| HDFC Venture Cap | AUM | FY13ii | 19,367 | 10.00 | 80.5 | 0.1 | 1 |
| Gruh Finance (40% discount) | Mkt val | | 28,230 | 0.60 | 60.6 | 1.0 | 7 |
| Unrealised gains - Others | Mkt val | | 80,000 | 1.00 | | 7.5 | 53 |
| Total | | | | | | 100 | 700 |

Source: Emkay Research

Key Financials

Income Statement

| Y/E Mar (Rsmn) | FY11A | FY12A | FY13E | FY14E |
|----------------------------|---------------|---------------|---------------|---------------|
| Net interest income | 42,471 | 49,983 | 58,068 | 67,859 |
| Other income | 7,113 | 9,290 | 11,549 | 13,527 |
| Net income | 49,584 | 59,273 | 69,617 | 81,386 |
| Operating expenses | 3,812 | 4,519 | 5,608 | 6,533 |
| Pre provision profit | 45,772 | 54,754 | 64,009 | 74,853 |
| PPP excl treasury | 0 | 0 | 0 | 0 |
| Provisions | 700 | 800 | 1,402 | 1,451 |
| Profit before tax | 45,072 | 53,954 | 62,607 | 73,402 |
| Tax | 13,320 | 15,430 | 18,042 | 21,010 |
| Tax rate | 29.6 | 28.6 | 28.8 | 28.6 |
| Profit after tax | 35,350 | 41,226 | 47,565 | 55,391 |

Balance Sheet

| Y/E Mar (Rsmn) | FY11A | FY12A | FY13E | FY14E |
|---------------------|-----------|-----------|-----------|-----------|
| Liabilities | | | | |
| Equity | 2,934 | 2,954 | 3,044 | 3,044 |
| Reserves | 170,231 | 187,222 | 267,843 | 285,981 |
| Net worth | 173,165 | 190,176 | 270,887 | 289,025 |
| Deposits | 1,151,123 | 1,391,275 | 1,593,010 | 1,863,822 |
| Current Lia. & Prov | 66,894 | 93,749 | 94,455 | 94,455 |
| Total liabilities | 1,391,183 | 1,675,199 | 1,958,351 | 2,247,302 |
| Assets | | | | |
| Cash and bank | 82,838 | 124,910 | 118,665 | 112,732 |
| Investments | 118,324 | 122,070 | 131,306 | 136,948 |
| Customer assets | 1,171,266 | 1,408,746 | 1,689,092 | 1,979,301 |
| Others | 18,719 | 19,474 | 19,289 | 18,321 |
| Total assets | 1,391,183 | 1,675,199 | 1,958,351 | 2,247,302 |

Key Ratio (%)

| Y/E Mar (Rsmn) | FY11A | FY12A | FY13E | FY14E |
|-----------------------|-------|-------|-------|-------|
| NIM | 3.3 | 3.3 | 3.2 | 3.2 |
| Non-ll/avg assets | 0.6 | 0.6 | 0.6 | 0.6 |
| 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 | 3.8 | 3.7 | 3.6 | 3.6 |
| Tax/avg assets | 1.0 | 1.0 | 1.0 | 1.0 |
| RoA | 2.8 | 2.7 | 2.6 | 2.6 |
| RoAE | 19.9 | 21.6 | 19.7 | 19.0 |
| GNPA (%) | 0.8 | 0.8 | 0.9 | 0.9 |
| NNPA (%) | 0.2 | 0.2 | 0.2 | 0.2 |

Valuation Table

| Y/E Mar | FY11A | FY12A | FY13E | FY14E |
|----------------------|--------|--------|--------|--------|
| Net profit (Rs mn) | 35,350 | 41,226 | 47,565 | 55,391 |
| Shares in issue (mn) | 1,467 | 1,477 | 1,522 | 1,522 |
| EPS (Rs) | 24.1 | 27.9 | 31.3 | 36.4 |
| PER (x) | 28.2 | 24.3 | 21.7 | 18.7 |
| FDEPS(Rs) | 22.0 | 26.6 | 29.8 | 35.0 |
| FDPER (x) | 30.8 | 25.5 | 22.7 | 19.4 |
| Book value (Rs) | 118.1 | 128.8 | 178.0 | 189.9 |
| P/BV (x) | 5.8 | 5.3 | 3.8 | 3.6 |
| Adj book value (Rs) | 116.8 | 127.2 | 176.1 | 187.6 |
| P/ABV (x) | 5.8 | 5.3 | 3.9 | 3.6 |
| P/PPP (x) | 0.0 | 0.0 | 0.0 | 0.0 |
| Dividend yield (%) | 1.3 | 1.6 | 1.6 | 1.6 |

Recommendation History: HDFC Ltd. – HDFC IN

| Date | Reports | Reco | CMP | Target |
|------------|---|------|-----|--------|
| 07/05/2012 | HDFC Q4FY12 Result Update | Hold | 664 | 700 |
| 12/01/2012 | HDFC Q3FY12 Result Update | Hold | 688 | 700 |
| 06/01/2012 | India - Housing Finance Sector Report | Hold | 665 | 700 |

Recent Research Reports

| Date | Reports | Reco | CMP | Target |
|------------|---|------------|-------|--------|
| 04/06/2012 | CRISIL Event Update | Accumulate | 1,050 | 1,240 |
| 22/05/2012 | Manappuram Finance Q4FY12 Result Update | Hold | 24 | 25 |
| 21/05/2012 | State Bank of India Q4FY12 Result Update | Reduce | 1,942 | 1,900 |
| 14/05/2012 | United Bank of India Q4FY12 Result Update | Buy | 57 | 75 |

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