

HDFC Ltd. (HDFC IN)

OUTPERFORMER
Consistent performance
Rs673
Mkt Cap: Rs988bn; US\$20.2bn

Q2FY12 result highlights

Quarterly performance: HDFC Ltd. reported PAT of Rs9.71bn in Q2FY12 (up 20% yoy), in line with our estimate of Rs9.66bn. NII (inclusive of dividends) came in at Rs13.1bn (18% yoy rise) led by stable NIMs and healthy advances growth of 20% yoy. The company reported other income of Rs2.5bn on the back of treasury income of Rs869m.

Key positives: Despite higher funding costs, margins (4.3%) and spreads (2.3%) remained stable yoy. Disbursements grew by a healthy 18% yoy resulting in loan growth of 20% yoy. The lender sold off loans worth Rs18.7bn during the quarter and credit growth, including loans sold, came in at 24% yoy. Fee and other charges witnessed traction during the quarter, coming in at Rs789m, vs. Rs681m in Q2FY11. HDFC's asset quality remained firm with nil net NPAs.

Key negatives: Loan approvals moderated to 13.3% yoy from 28% yoy in Q2FY11.

Impact on financials

We expect HDFC's loan book to increase by a healthy 19% CAGR over FY11-13. Active spread management and strong pricing power in corporate loans would enable HDFC to maintain margins despite higher borrowing costs. We maintain our earnings estimates and expect steady margins and negligible credit costs to drive an 18% CAGR in earnings over FY11-13E, with an average RoE of 23% over the period.

Valuations & view

HDFC currently trades at 3.5x FY12E and 3x FY13E BV (excluding the value of its subsidiaries). Given its strong track record and sustainable high core RoEs, we expect HDFC to sustain its premium valuations. Valuing the core business at 4.4x FY12E book (3.8x FY13E) and building in a value of Rs205 per share for the subsidiaries, we assign a 12-month price target of Rs800 to the stock. Reiterate Outperformer.

Key financials (quarterly)

(Rs m)	Q2FY11	Q1FY12	Q2FY12	% ch % chg % var		
				qoq	yoy	from est
NII (gross of dividends)	11,073	12,271	13,064	(14)	16	(2)
Other income	2,103	1,762	2,521	(40)	163	20
Operating expenses	1,041	1,132	1,239	49	12	8
Operating profit	11,485	11,935	13,547	(24)	22	1
Provisions	150	180	170	(28)	20	13
Profit before tax	11,335	11,755	13,377	(24)	22	0
Net profit	8,075	8,445	9,707	(26)	22	1
Loan Book (Rs bn)	1062.9	1241.7	1269.9	6.0	22.2	
Sanctions (Rs bn)	207.2	194.4	234.7	(12.2)	22.0	
Disbursements (Rs bn)	166.5	140.7	196.9	(23.5)	20.0	

Key valuation metrics

	FY10	FY11	FY12E	FY13E
Net profit (Rs m)	28,265	35,350	41,641	49,548
yoy growth (%)	23.8	25.1	17.8	19.0
Shares in issue (m)	1,436	1,467	1,467	1,467
EPS (Rs)	19.7	24.1	28.4	33.8
EPS growth (%)	22.7	22.4	17.8	19.0
PE (x)	34.2	27.9	23.7	19.9
Book value (Rs/share)	106	118	134	154
P/ BV (x)	6.4	5.7	5.0	4.4
RONW (%)	20.0	21.7	22.5	23.4

SOTP valuation

Value per share (FY13E)

Core business	595
Subsidiary valuation	
Life insurance	49
HDFC Bank	138
Others*	18
Total subsidiary valuation	205
Total SOTP value	800

*Asset management + general insurance

Quarterly results: Detailed

(Rs m)	Q2FY11	Q1FY12	Q2FY12	FY11	FY12E	FY13E	Comments
Interest income (incl dividend)	28,249	37,420	39,969	122,498	160,878	189,097	
Interest expense	17,176	25,149	26,905	75,599	104,519	121,441	
NII (excluding dividends)	10,845	10,948	12,435	44,646	53,708	64,365	
yoy growth (%)	38.3	17.1	14.7	24.8	20.3	19.8	
NII (gross of dividends)	11,073	12,271	13,064	46,898	56,358	67,656	Stable NIMs and healthy advances growth drives NII growth
yoy growth (%)	26.3	16.5	18.0	23.1	20.2	20.0	
Other income	2,103	1,762	2,521	6,032	5,730	6,118	Treasury income of Rs869m booked during the quarter
Operating expenses	1,041	1,132	1,239	3,812	4,403	5,182	
yoy growth (%)	20.0	12.3	19.0	17.7	15.5	17.7	
Operating profit	11,485	11,935	13,547	49,370	58,085	68,992	
yoy growth (%)	23.9	21.6	17.9	24.2	17.7	18.8	
Provision for contingencies	150	180	170	700	650	650	
Profit before tax	11,335	11,755	13,377	48,670	57,435	68,342	
yoy growth (%)	24.2	21.6	18.0	24.3	18.0	19.0	
Net profit	8,075	8,445	9,707	35,350	41,641	49,548	In-line with estimates
yoy growth (%)	21.6	21.6	20.2	25.1	17.8	19.0	
Ratios (%)							
Net interest margin	3.5	3.5	3.6	3.7	3.7	3.8	Loan spreads and margins stable yoy as well as qoq
Fees/avg assets	0.22	0.16	0.22	0.2	0.2	0.2	
Other income /Avg assets	0.7	0.5	0.7	0.5	0.4	0.3	
Expenses/Avg assets	0.3	0.3	0.3	0.3	0.3	0.3	
Cost/Income	7.9	8.1	8.0	7.2	7.1	7.0	
Provisions/Avg assets	0.0	0.1	0.0	0.1	0.0	0.0	
PBT/Avg assets	3.6	3.3	3.7	3.8	3.8	3.8	
RoA	2.6	2.4	2.7	2.8	2.7	2.8	
Tax/PBT	28.8	28.2	27.4	27.4	27.5	27.5	
Balance Sheet (Rs bn)							
Loan Book	1062.9	1241.7	1269.9				Loans to individual and corporate segments up 18% and 24% yoy respectively
yoy growth (%)	18.7	22.2	19.5				
Total Assets (incl current assets)	1310.2	1415.9	1506.1				
yoy growth (%)	20.7	16.7	14.9				
Sanctions	207.2	194.4	234.7				
yoy growth (%)	28.2	22.0	13.3				
Disbursements	166.5	140.7	196.9				
yoy growth (%)	21.9	20.0	18.3				

Other Highlights

- **Healthy NII performance:** NII (ex-dividends) grew by 15% yoy to Rs12.4bn. Including higher dividend income of Rs629m witnessed during the quarter (Rs229m in Q2FY11), NII stood at Rs13.1bn (up 18% yoy). Despite rising cost of funds, HDFC's spreads remained stable yoy as well as qoq at 2.3% in Q2FY12. NIMs were stable at ~4.3% in H1FY12. (Exhibit 1)
- **Robust business volume growth:** The loan book increased by 20% yoy and 2% qoq to Rs1270bn. Advances to the individual and corporate segments increased by 18% and 24% yoy respectively. Business volumes remained strong as disbursements grew by 18% yoy to Rs197bn in Q2FY12. Loan approvals grew by 13% yoy to Rs235bn. The lender sold off loans of Rs18.7bn during the quarter. (Exhibit 4)
- **Other income - traction in fee and other charges:** Total other income grew from Rs2.1bn in Q2FY11 to Rs2.5bn in Q2FY12, aided by treasury profits and strong fee income. Fees and other charges came in at Rs789m, up 16% yoy. HDFC booked treasury income of Rs869m during the quarter as against Rs590m in Q2FY11.
- **Steady asset quality:** HDFC continued to demonstrate resilience with strong asset quality. Gross NPA on 90dpd basis came in at 0.82% in Q2FY12 vs. 0.86% a year ago. On an absolute basis, gross NPA increased by ~Rs250m qoq. HDFC has nil net NPAs as the provision for contingencies exceeded gross NPAs. Provision expenses stood at a low 0.05% of assets in Q2FY12 – Rs170m in absolute terms.
- **Funding base remains well diversified:** HDFC continues to benefit from a diversified funding base. In Q2FY12, term loans declined by 8% yoy, while bonds, debentures and CPs were up 29% yoy. The proportion remained stable yoy with – term loans at ~26%; bonds, debentures and CPs at ~49%; and deposits at ~25%.
- The lender utilized Rs2.6bn (net of deferred tax) during the quarter from the additional reserve to meet the additional provision consequent to changes in provisioning norms on standard assets.

Exhibit 1: Margins and spreads

%	Q2FY11	Q1FY12	Q2FY12	yoy change (bps)	qoq change (bps)
Interest income (less dividends)/Avg assets	8.9	10.3	10.8	189	50
Interest income (less dividends)/Avg interest earning assets : A	9.3	10.7	11.1	177	42
Interest income(gross dividends)/Avg interest earning assets	9.4	11.1	11.3	187	21
Yield on advances : C	10.1	11.0	11.7	163	65
Yield on Investments	5.2	11.3	8.1	288	(320)
Interest expenses/Avg interest bearing liabilities : B	6.6	8.4	8.7	208	24
Spread : (A-B)	2.8	2.3	2.4	(31)	19
Spread on loans : (C-B)	3.5	2.6	3.0	(45)	41
NIMs	3.4	3.1	3.4	(3)	29
NIM (gross dividends)/avg assets	3.5	3.5	3.6	7	8

Exhibit 2: Break-up of loan portfolio

(Rs mn)	Q2FY11	Q1FY12	Q2FY12	yoy growth (%)	% of total
Individuals	683	779	803	17.6	63.2
Corporates	365	448	451	23.6	35.5
Others	15	15	16	5.3	1.2
Loan book - reported	1063	1242	1270	19.5	100.0

Exhibit 3: Disbursements and approvals

Rs m	Q2FY11	Q1FY12	Q2FY12
Approvals	207,225	194,428	234,742
yoy growth (%)	28.2	22.0	13.3
Disbursements	166,455	140,746	196,909
yoy growth (%)	21.9	20.0	18.3

Exhibit 4: Break-up on non-fund revenues

Rs m	Q2	Q1	Q2	growth (%)	
	FY11	FY12	FY12	yoy	qoq
Fees and other charges	681	573	789	15.9	37.7
Profit on sale of investments	590	163	869	47.4	434.3
Lease income	136	14	12	(91.3)	(13.9)
Other non-fund income	47	47	52	10.4	11.6
Non-fund income	1,453	796	1,722	18.5	116.3

Exhibit 5: Funding Mix

Rs bn	Q2	Q1	Q2	(%/bp)	
	FY11	FY12	FY12	yoy	qoq
Break-up of borrowings					
Term Loans	350	414	323	(7.7)	(22.0)
Bonds, Debentures, FRN and CPs	473	516	611	29.1	18.3
Deposits	269	305	317	18.0	4.0
% of total					
Term Loans	32.1	33.5	25.8	(622)	(770)
Bonds, Debentures, FRN and CPs	43.3	41.8	48.8	548	703
Deposits	24.6	24.7	25.4	74	67

Exhibit 6: Stable asset quality

	Q2FY11	Q1FY12	Q2FY12	yoy chg		qoq chg	
				(%/bps)	(%/bps)	(%/bps)	(%/bps)
NPLs (180 DPD)	0.53	0.55	0.53	-	(2)		
Gross NPLS (Rs m)	9,393	10,382	10,630	13	2		

Analyst	Sector/Industry/Coverage	E-mail	Tel. +91-22-6622 2600
Pathik Gandotra	Head of Equities; Financials	pathik.gandotra@idfc.com	91-22-662 22525
Shirish Rane	Co-Head of Research; Construction, Power, Cement	shirish.rane@idfc.com	91-22-662 22575
Nikhil Vora	Co-Head of Research; Strategy, FMCG, Media, Education, Exchanges, Mid Caps	nikhil.vora@idfc.com	91-22-662 22567
Nitin Agarwal	Pharmaceuticals, Real Estate, Agri-inputs	nitin.agarwal@idfc.com	91-22-662 22568
Chirag Shah	Metals & Mining, Telecom, Pipes	chirag.shah@idfc.com	91-22-662 22564
Bhoomika Nair	Logistics, Engineering	bhoomika.nair@idfc.com	91-22-662 22561
Hitesh Shah, CFA	IT Services	hitesh.shah@idfc.com	91-22-662 22565
Bhushan Gajaria	Automobiles, Auto ancillaries, Retailing	bhushan.gajaria@idfc.com	91-22-662 22562
Salil Desai	Construction, Power, Cement	salil.desai@idfc.com	91-22-662 22573
Ashish Shah	Construction, Power, Cement	ashish.shah@idfc.com	91-22-662 22560
Probal Sen	Oil & Gas	probal.sen@idfc.com	91-22-662 22569
Chinmaya Garg	Financials	chinmaya.garg@idfc.com	91-22-662 22563
Abhishek Gupta	Telecom, Metals & Mining	abhishek.gupta@idfc.com	91-22-662 22661
Saumil Mehta	Metals, Pipes	saumil.mehta@idfc.com	91-22-662 22578
Vineet Chandak	Real Estate, Pharmaceuticals, Agri-inputs	vineet.chandak@idfc.com	91-22-662 22579
Anamika Sharma	IT Services	anamika.sharma@idfc.com	91-22-662 22680
Varun Kejriwal	FMCG, Mid Caps, Shipping, Aviation	varun.kejriwal@idfc.com	91-22-662 22685
Swati Nangalia	Media, Education, Exchanges, Midcaps	swati.nangalia@idfc.com	91-22-662 22576
Nikhil Salvi	Construction, Power, Cement	nikhil.salvi@idfc.com	91-22-662 22566
Kavitha Rajan	Strategy, Financials	kavitha.rajan@idfc.com	91-22-662 22697
Dharmendra Sahu	Database Analyst	dharmendra.sahu@idfc.com	91-22-662 22580
Rupesh Sonawale	Database Analyst	rupesh.sonawale@idfc.com	91-22-662 22572
Dharmesh R Bhatt, CMT	Technical Analyst	dharmesh.bhatt@idfc.com	91-22-662 22534
Equity Sales/Dealing	Designation	E-mail	Tel. +91-22-6622 2500
Naishadh Paleja	Co-Group CEO	naishadh.paleja@idfc.com	91-22-6622 2522
Paresh Shah	MD, Dealing	paresh.shah@idfc.com	91-22-6622 2508
Vishal Purohit	MD, Co-Head of Sales	vishal.purohit@idfc.com	91-22-6622 2533
Nikhil Gholani	MD, Co-Head of Sales	nikhil.gholani@idfc.com	91-22-6622 2529
Sanjay Panicker	Director, Sales	sanjay.panicker@idfc.com	91-22-6622 2530
Rajesh Makharia	Director, Sales	rajesh.makharia@idfc.com	91-22-6622 2528
Kalpesh Parekh	Director, Sales	kalpesh.parekh@idfc.com	91-22-6622 2696
Pradip Seth	SVP, Sales	pradip.seth@idfc.com	91-22-6622 2595
Varun Saboo	AVP, Sales	varun.saboo@idfc.com	91-22-6622 2558
Pawan Sharma	MD, Derivatives	pawan.sharma@idfc.com	91-22-6622 2539
Dipesh Shah	Director, Derivatives	dipesh.shah@idfc.com	91-22-6622 2693
Jignesh Shah	AVP, Derivatives	jignesh.shah@idfc.com	91-22-6622 2536
Sunil Pandit	Director, Sales trading	sunil.pandit@idfc.com	91-22-6622 2524
Mukesh Chaturvedi	SVP, Sales trading	mukesh.chaturvedi@idfc.com	91-22-6622 2512
Viren Sompura	SVP, Sales trading	viren.sompura@idfc.com	91-22-6622 2527
Rajashekhar Hiremath	VP, Sales trading	rajashekhar.hiremath@idfc.com	91-22-6622 2516

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- | | |
|-------------------|---|
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Naman Chambers, C-32,
G- Block, Bandra-Kurla Complex,
Bandra (East), Mumbai 400 051

Tel: 91-22-6622 2600
Fax: 91-22-6622 2501