Q1FY13 Result Update

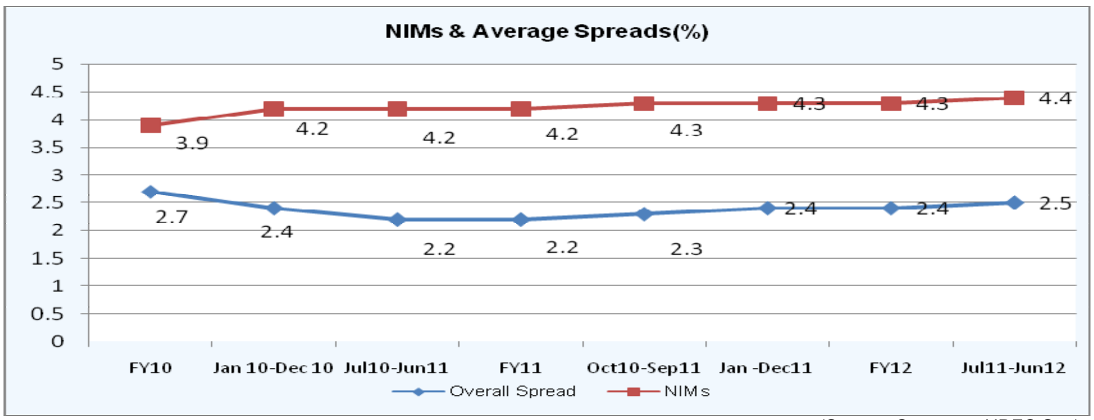
August 23, 2012

HDFC Scrip Code	Industry	CMP	Recommended Action	Time Horizon
IDFLTDEQNR	Finance	142.10	Buy the stock at CMP and add on dips of Rs 128-Rs 132 for a target price of Rs 151	1 quarter

For Q1FY13, IDFC remained on a healthy growth trajectory with strong asset growth (33.7% y-o-y loan growth to Rs 50,157 cr) along with improved NIMs (4.4%), interest spreads (2.5%) and asset quality (NNPAs at 0.14%). NII grew 30.2% y-o-y and 7.3% q-o-q to Rs 629 cr. Non-interest income has gone up 24.5% y-o-y and 2.2% q-o-q to Rs 137 cr driven by higher fee income. Pre Provisioning profits have grown 33.6% y-o-y and 14.1% q-o-q to Rs 656 cr. Gross NPAs and Net NPAs remain negligible and were stable at 0.30% and 0.14% respectively. Provisions were comparatively higher at Rs 103 cr on account of a one- time provisioning of Rs 64 cr related to investment diminution. Reported PAT has gone up 21.1% y-o-y and 13.3% q-o-q to Rs 380 cr.

Robust NII growth accompanied by improved NIMs and Interest Spread

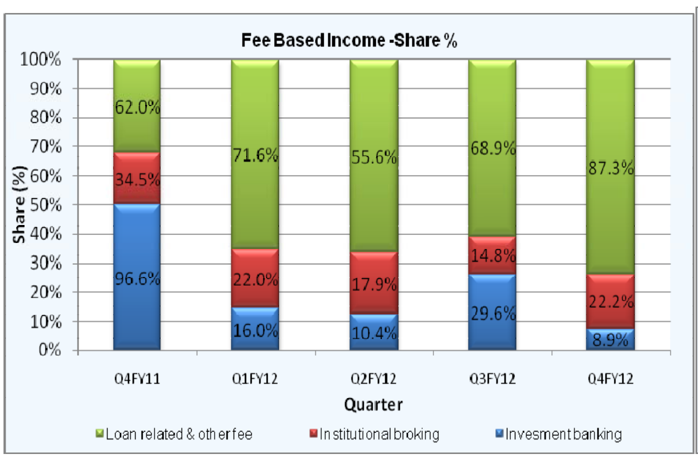
Net Interest Income (NII) during Q1FY13 grew at a robust pace of 30.2% y-o-y and 7.3% q-o-q to Rs 629 cr. While Infra continues to contribute more to the company's revenues, higher growth this quarter came in from treasury income up 34.5% y-o-y and 60.9% q-o-q to Rs 74 cr (though on a low base). Infra segment too performed well with a growth rate of 29.7% y-o-y and 2.8% q-o-q to Rs 555 cr. Over last year, NIMs and Interest Spread have improved to 4.4% (from 4.2%) and 2.5 % (2.2%) respectively. The improvement in spreads is contributed by both improving yields and lowering borrowing costs. The management aims to maintain spreads in the regions of 2.25-2.45% on a sustainable basis.

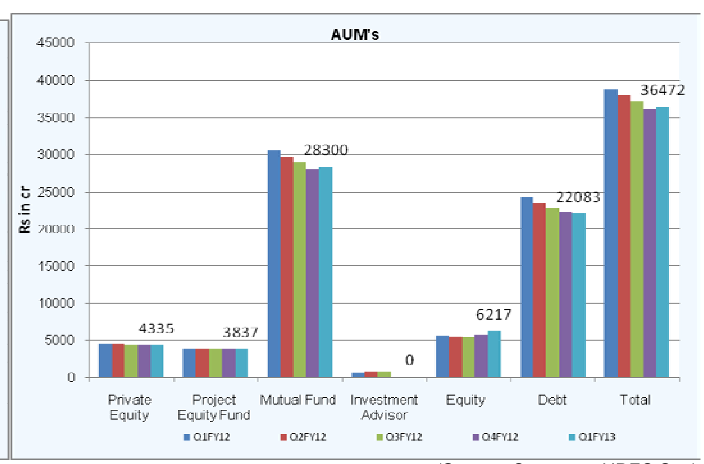


(Source: Company, HDFC Sec)

Higher Non Interest Income led by higher fee income

Non-interest income which comprises of Principal investment, Asset Management and Fee Income has gone up 24.5% y-o-y and 2.2% q-o-q to Rs 137 cr. Loan related and other fees came in at Rs 62 cr, up 77.1% y-o-y and more than double compared to Q4FY12. The increase in fee income was mainly on account of strong pickup in sanctions and closure of a few structured deals. Income from asset management business remained stable with growth of 3.2% y-o-y and 6.7% q-o-q at Rs 64 cr. Income from institutional broking and investment banking businesses have declined q-o-q and y-o-y. Income from principal investments during the quarter was just Rs 2 cr compared to Rs 29 cr in Q4FY12.





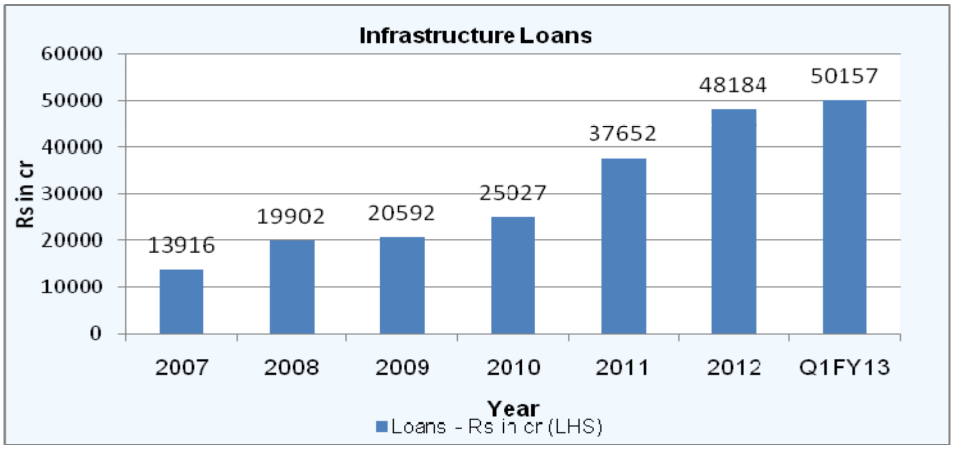
(Source: Company, HDFC Sec)

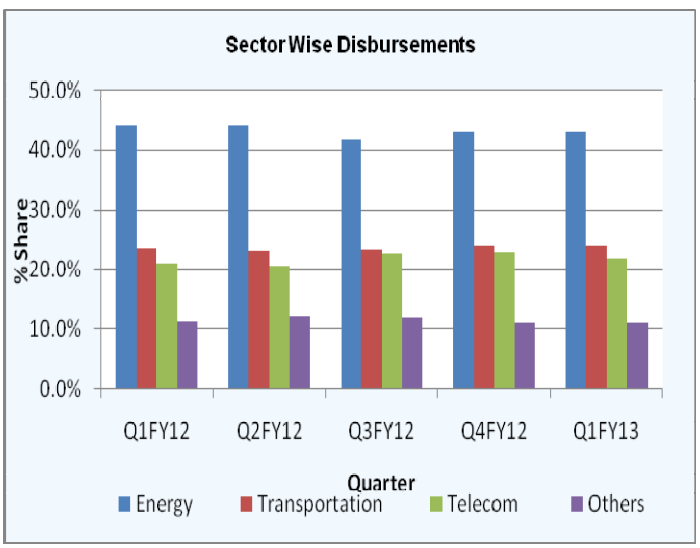
Loan growth driven by refinancing; Power sector exposure at 41%

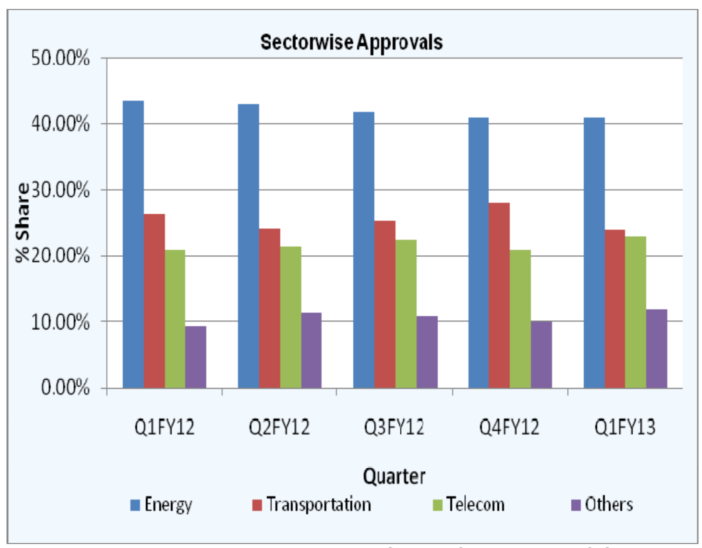
Outstanding loans grew 33.7% y-o-y and 4.1% q-o-q to Rs 50,157 cr driven mainly by refinancing activity. Going forward too, the management expects 30-40% of the incremental business to come through refinancing. Cumulative outstanding approvals have gone up 23.9% y-o-y and 9.6% q-o-q to Rs 76,412 cr. Exposure to the Energy sector has come down to 41% from 43% last year. Exposure to telecom has gone up to 23% from 21% last year but management has cited that the exposure is only towards the top three-four players and they are capitalizing on refinancing opportunities in the segment.

Refinance opportunities exist in operational assets in the roads, renewable power and telecom sectors. Loans to operating assets currently constitute 67% of the total loan book.

Total Outstanding disbursements have grown 30.2% y-o-y and 3.5% q-o-q to Rs 55,413 cr. Power segment has a significant share of 43% followed by transportation (24%) and telecom (22%).



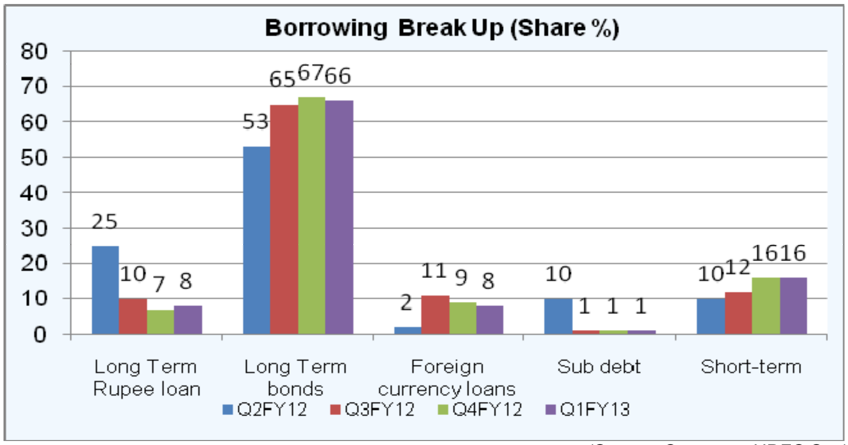




(Source: Company, HDFC Sec)

Incremental Borrowings higher compared to incremental loan growth

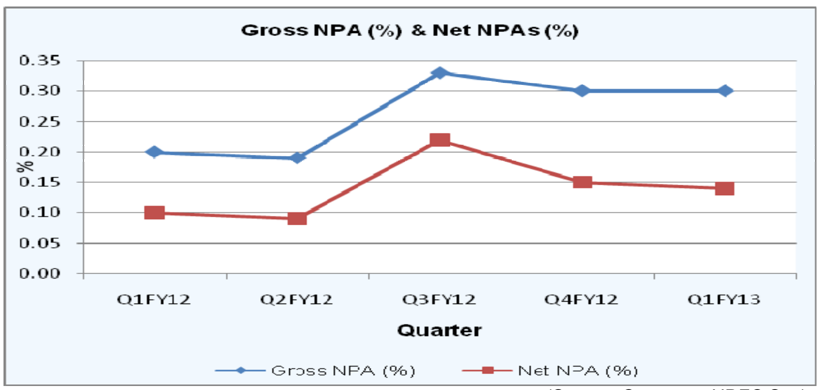
Borrowings as on June 2012 have grown 29.3% y-o-y and 7.7% q-o-q to Rs 50,012 cr of which 66% were from long term bonds while rupee loans were 8%. In Q1FY13, Incremental loans stood at Rs 1,973 cr q-o-q while incremental borrowings have grown at faster rate of Rs 3,576 cr q-o-q. As a result, IDFC has built excess liquidity on balance sheet, leading to 24.8% q-o-q increase in treasury assets. IDFC has increased the share of short-term borrowings (from 12% in Q3FY12 to 16% in Q1FY13) that is driven by rise in share of refinancing and expectation of correction in long term interest rates, especially in near term.



(Source: Company, HDFC Sec)

GNPAs and NNPAs remain stable; Provisioning rises on one-offs

Gross NPAs and Net NPAs sequentially have gone up just 1.3% and 1.7% to Rs 150.3 cr and Rs 72.7 cr respectively. Gross NPAs as a percentage has been maintained at 0.30% in Q1FY13 as in Q4FY12 (0.20% in Q1FY12). Net NPAs stood at 0.14% compared to 0.10% in Q1FY12 and 0.15% in Q4FY12. Provisioning was higher at Rs 102.6 cr, a steep increase from Rs 39.9 cr in Q1FY12 and Rs 83.8 cr in Q4FY12 mainly on account of Rs 64 cr worth provisions on permanent diminution in value of investments (mainly a Commercial paper default). The loan loss ratio (on a rolling 12-month basis) stood at 1.6% of standard loans v/s 1.5% in Q4FY12. Current restructured book is under 2% and the company has so far not taken any NPV hit on the accounts restructured.



(Source: Company, HDFC Sec)

Cost to income ratio has come down to 15.1% in Q1FY13 compared to 18.8% in Q1FY12 and 20.7% in Q4FY12 primarily on account of lower staff costs which has fallen by 26.7% q-o-q and has gone up only 1.5% y-o-y to Rs 66 cr.

PBT grew 22.6% y-o-y and 12.7% q-o-q to Rs 553 cr. Tax rate during the quarter at ~31% was higher than the historical run rate of 25%-27%. The management is guiding for a tax rate of around 28% for the year. Reported PAT was up 21.1% y-o-y and 13.3% q-o-q to Rs 380 cr.

Other Highlights

- IDFC's overall capital adequacy stood at 21.83% in Q1FY13 compared to 24.01% in Q1FY12 and 20.79% in Q4FY11.
- As on June 2012, asset-liability management was maintained well with assets having duration of 1.54 years while liabilities were of 1.86 years duration
- During Q1FY13, name of the Company was changed from Infrastructure Development Company Ltd to IDFC Ltd
- In Q1FY13, Dheeru Powergen Ltd has ceased to be a subsidiary and IDFC Private Equity Company Ltd was renamed as IDFC Alternatives Ltd
- During Q1FY13, the Company issued 956,944 equity shares of face value of Rs10 each pursuant to exercise of stock options by employees under the employee stock option scheme.

Concerns

- Inability to raise capital in future could impact growth
- Inherent risks in infrastructure financing
- Significant exposures to certain sectors like power (43% in Q1FY13)
- Foreign currency risk - 8% of loans borrowed are in foreign currency
- Discontinuation of tax benefits could affect profits
- Competitive and profitability pressures in the capital market related businesses

Outlook & Valuation

IDFC has been performing well in the last couple of years reflected in growing loan book size, interest income, disbursements and profits. Besides structural advantage over banks, it is also supported by good management which has expertise in infrastructure lending. This would help in keeping its loan book growth intact given the potential of infrastructure financing in India. A strong return on assets ratio of 2.47% as on June 2012, capital to support loan book growth, superior credit quality and high non-interest income contribution (~18 % of the revenues) are the key positives. IDFC's loan book grew at 27 % CAGR over the period FY07-12. IDFC has a strong asset quality with gross NPA ratio of 30 bps of loans and ROE of 13.2%.

For Q1FY13, IDFC remained on healthy growth trajectory with strong asset growth (33.7% y-o-y loan growth to Rs 50,157 cr) along with improved NIMs (4.4%), interest spreads (2.5%) and asset quality (NNPAs at 0.14%). NII grew 30.2% y-o-y and 7.3% q-o-q to Rs 629 cr. Non-interest income has gone up 24.5% y-o-y and 2.2% q-o-q to Rs 137 cr driven by higher fee income. Pre Provisioning profits have grown 33.6% y-o-y and 14.1% q-o-q to Rs 656 cr. Gross NPAs and Net NPAs remain negligible and were stable at 0.30% and 0.14% respectively. Provisions were comparatively higher at Rs 103 cr on account of a one- time provisioning of Rs 64 cr related to investment diminution. Reported PAT has gone up 21.1% y-o-y and 13.3% q-o-q to Rs 380 cr.

During FY13, management expects ~20% growth in loans with stable spreads. Refinancing is a large opportunity as the number of first generation projects that will look to refinance is high. Fall in cost of funds will help to grow in refinancing business without the sacrifice of spreads. With the definition of infrastructure sector being widened to include healthcare, pipelines etc. IDFC could look into tapping these sectors as well.

We are maintaining our FY13 estimates (though the components of topline may require a change – but the topline could remain the same). NPAs could continue to remain negligible and we don't expect much concern on this front. Exposure to power sector (43% of total) has increased only marginally and given recent positive sector developments, management is confident of earnings risks to be lower.

In our result update on IDFC dated May 18, 2012 we had mentioned, "IDFC could trade in the range of Rs 105-Rs 137 (1.1x – 1.5xFY13E BV) for the next three months". Post the report the stock has touched a low of Rs 115.7 on 21^{h} May 2012 and a high of Rs 144.7 on 21st August 2012.

We feel fresh investors could look to buy the stock at CMP and add the stock on dips of Rs 128-Rs 132 (1.4x-1.45x) for a target price of Rs 151 (1.65x FY13E BV) over the next 1 quarter.

Quick Estimates

Particulars (Rs in cr)	FY07	FY08	FY09	FY10	FY11	FY12A	FY13E
NII	429	694	922	1117	1645	2113	2493
Non- interest income	267	618	612	949	875	844	861
Operating expenses	82	254	367	549	533	523	570
Cost-Income (%)	11.8%	19.4%	23.9%	26.6%	21.2%	17.7%	17.0%
Pre Provisioning Profit	634	1070	1187	1557	2013	2434	2784
Provisions	17	70	153	130	235	285	306
PBT	617	1000	1034	1427	1778	2149	2478
PAT (after MI & Ass. Profit)	505	742	750	1062	1282	1544	1785
EPS	3.3	4.9	5.0	7.0	8.5	10.2	11.8
BV	26.2	43.2	47.7	53.9	74.6	81.2	91.3
P/BV	5.5	3.3	3.0	2.7	1.9	1.8	1.6
P/E	43.3	29.4	29.1	20.6	17.0	14.1	12.2
Equity	1126	1294	1295	1301	1509	1512	1513

*Adj BV is not separately mentioned as the difference is nominal due to very low NPAs
(E: Estimates, OE: Original Estimates, RE: Revised Estimates; Source: Capitalline, HDFC Sec Estimates)

Quarterly (Consolidated)

Particulars	Q1FY13	Q1FY12	% Chg	Q4FY12	% Chg	FY12	FY11	% Chg
(A)Net Interest Income	**629**	**483**	**30.2%**	**586**	**7.3%**	**2113.0**	**1645.0**	**28.4%**
1.NII-Infrastructure	555	428	**29.7%**	540	**2.8%**	1880	1501	**25.2%**
2.NII-Treasury	74	55	**34.5%**	46	**60.9%**	233	144	**61.8%**
(B)Non Interest Income	**137**	**110**	**24.5%**	**134**	**2.2%**	**876.0**	**845.0**	**3.7%**

1.Principal investment	2	-2	-200.0%	29	-93.1%	191	350	-45.4%
2.Asset management	64	62	3.2%	60	6.7%	292.0	281.0	3.9%
a)Mutual Funds	35	33	6.1%	29	20.7%	110	122	-9.8%
b)Alternative assets/Fees	29	29	0.0%	29	0.0%	139	120	15.8%
c)Capital gains & carry	0	0	NC	2	-100.0%	43	39	10.3%
3.Fee income	71	50	42.0%	45	57.8%	393.0	214.0	83.6%
a)Investment banking	3	4	-25.0%	4	-25.0%	146	34	329.4%
b)Institutional broking	6	11	-45.5%	10	-40.0%	53	41	29.3%
c)Loan related & other fee	62	35	77.1%	31	100.0%	194	139	39.6%
(C)Other Income	7	12	-41.7%	6	16.7%	26	23	13.0%
Net income (A+B+C)	773	605	27.8%	725	6.6%	2979	2546	17.0%
Operating expenses (incl Depr)	117	114	2.6%	150	-22.0%	522	532	-2.0%
Staff	66	65	1.5%	90	-26.7%	305	296	3.0%
Other Operating expenses	51	49	4.1%	60	-15.0%	217	236	-8.1%
Pre-Provisioning Profits	656	491	33.6%	575	14.1%	2457	2013	22.0%
Provisions	103	40	157.5%	84	22.6%	285	235	21.3%
PBT	553	451	22.6%	491	12.6%	2173	1779	22.1%
Tax	171	138	24.4%	159	7.8%	622	500	24.4%
PAT	382	313	21.9%	332	14.9%	1551	1279	21.2%
MI	2	0	3975.0%	-2	-170.6%	-1	0	291.2%
Share of profit from associate	0	1	-155.8%	1	-143.9%	2	2	-16.1%
Reported PAT	380	314	21.1%	335	13.3%	1554	1282	21.2%
EPS	2.5	2.1	21.1%	2.2	13.3%	10.3	8.5	21.2%
CAR	21.83	24.01		20.79		20.79	24.48	
Gross NPA	150.26	77.9	92.9%	148.32	1.3%	148.32	79.73	86.0%
Net NPA	72.68	36.5	99.1%	71.43	1.7%	71.43	38.91	83.6%
% of Gross NPA	0.30	0.20		0.30		0.30	0.21	
% of Net NPA	0.14	0.10		0.15		0.15	0.10	

(Source: Company, HDFC Sec)

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