DALAL & BROACHA
STOCK BROKING PVT. LTD.

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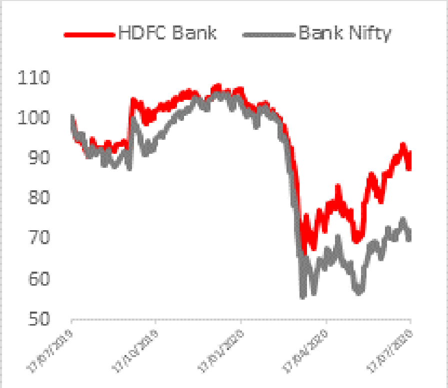
Q1FY21 Result update@ Dalal & Broacha

ACCUMULATE	
Current Price	1099
52 Week Range	739/1304
Target Price	1215
Upside (%)	11

Key Share Data	
Market Cap (Rs.bn)	6034.64
Market Cap (US$ bn)	80.54
No of o/s shares (Mn)	5490.28
Face Value	1
BSE Code	500180
NSE Code	HDFCBANK
Bloomberg	HDFCB

Price performance



% Shareholding	Jun-20	Mar-20
Promoters	26.10	26.14
Public	73.90	73.86
Others	0.00	0.00
Total	100	100

Despite the macro headwinds driven by COVID-19, HDFC Bank (HDFCB) has reported a stable set of numbers for the quarter ended June 30, 2020. Bank's numbers were below our estimates on the profitability front due to higher provisions, though operating performance was better than our estimates.

- NII came in at INR 156.7 Bn, +3% QoQ / +17.8% YoY and 2% above our est.
- Net Income came in at INR 197.4 Bn, -7.0% QoQ / +8.1% YoY and 5% below our est.
- PPOP came in at INR 128.3 Bn, -1.0% QoQ / +15.1% YoY and 3% above our est.
- Provisions came in at INR 38.9 Bn, +2.8% QoQ / +48.9% YoY and 21% above our est.
- PAT came in at INR 66.6 Bn, -3.9% QoQ / +19.6% YoY and 4% below our est.
- EPS stood at INR 12.1 vs INR 12.6 / INR 10.2 in Q4FY20 / Q1FY20 respectively.

Financial Highlights

- **HDFCB has shown healthy credit growth of 20.9% YoY in Q1FY20. Out of which, domestic advances grew by 21% YoY, mainly driven by wholesale loan growth of 37.6% YoY, while retail loans grew slower at 7.2% YoY.** Management highlighted that the weighted average rating of the book on an internal scale (ranges from 1-10 with 1 being highest rated corporates and 7 corresponding to an external 'A' rating) is currently at 4.3, which is an improvement of 30 bps YoY.
- On liabilities, **Deposits growth was also strong at 24.6% YoY/3.7% QoQ with CASA mix stood at 40%.** Bank's continued focus on deposits helped in the maintenance of a healthy liquidity coverage ratio at 140%, well above the regulatory requirement.
- **Bank's asset quality remains stable, with GNPAs sequentially up by 10 bps at 1.36% and NNPAs down by 3 bps to 0.33% in Q1FY21.** Bank's PCR improved by 419 bps sequentially to 76.2% in Q1FY21. Core Credit Cost ratio stood at 1.08%, as compared to 0.77% QoQ and 1.07% YoY. Bank held floating provisions of Rs 14.51 Bn and contingent provisions of Rs 40.02 Bn as on June 30, 2020. **We believe the bank's discretionary provisions are more than adequate for even the 'stress case' scenario that it currently anticipates.**
- **The bank's operational efficiency remained strong, with cost to income ratio falling by 396 bps YoY to 35%, backed by higher net income (NII + other income) growth of 18% vs opex de-growth of 2.9% in Q1FY21.** Operating expenses were lower primarily due to lower loan origination & sales volumes. The continued slowdown in economic activity has led to a decrease in retail loan origination, sale of third party products, efficiency in collection efforts and waivers of certain fees. As a result, fees/other income were lower by ~ Rs 2,000 Cr. Retail constitutes ~ 89% and wholesale constitutes 11% of fees & commission.
- **Bank's capital adequacy ratio stood at 18.9% (vs 16.9% YoY/ 18.5% QoQ), of which Tier I capital was 17.5% (vs 15.6% YoY/ 17.2% QoQ).** During the quarter, the bank generated slightly above 60 bps of capital, mainly driven by earnings, while the consumption was about 3 bps. Therefore, the net capital generated in the quarter is about 30 bps, which is reflected in the increase in the total capital ratio to 18.85%.

Valuation and outlook

With better capital adequacy and healthy provisioning buffer, HDFC Bank is in better position to withstand upcoming economic storm. The bank is sitting on excess liquidity led by strong deposit growth, a stance that the bank has adopted since 2018 (which was then criticized) as it believes that systemic liquidity risks still remain high. Besides, we believe its loan book quality across segments is significantly stronger than the rest of the industry, which should hold it in comparatively better stead.

However, selection of the new MD continues to remain an overhang on the stock. **The stock has rallied strongly in the past two months ~ 30% up move. Thus, while we remain broadly positive on stock from a business perspective, valuations remain a constraining factor. Hence, we revise rating to "Accumulate" from "BUY" earlier. At CMP, stock trades at 3.2x its FY21E ABV and 2.8x its FY22E ABV. We value HDFCB at FY22E P/ABV multiple of 3.1x to arrive at target price of Rs 1215/ share.**

Key Financials (Rs /Bn)

Year	NII	PPOP	PAT	ROA	Adj.BVPS	P/ABVPS
FY20	562	487	263	1.9	305	3.6
FY21E	632	551	298	1.8	343	3.2
FY22E	737	648	358	1.9	392	2.8

Key takeaways from HDFC Bank's Q1FY21 earnings call

Economic activates:

- Economy appears to recover sharply from April, with a whole range of high-frequency indicators ranging from oil consumption and electricity consumption, to e-way Bill / toll collections and the purchase managers' index marked sharp improvement in May that sustained in June.
- Anecdotal evidence on capacity utilization of some of the companies like auto, steel, FMCG seems to corroborate this conclusion. The pickup in tractor 2-wheeler and small car sales as well as the nature of FMCG items that have shown robust growth point to a rural bias in the recovery and are consistent with 2 themes.
- The rural economy seems to have been relatively isolated from the virus. The robust rabi or winter crop of the previous cycle and the satisfactory progress of this season's summer or kharif crop has manifested in a healthy income in the hands of the farm sector as well as expectations of income boost going forward as the summer crop is harvested.
- However, the steady rise in infections and the greater dispersion across the country means that containment remains a policy challenge and partial lockdowns that are being imposed in different pockets could hinder a full-grown recovery.

Banking Industry

- The transmission of 150 bps rate cuts from February and the presence of a large surplus liquidity of 6.5 lakh Cr currently has led to a sharp decline in yields and borrowing costs for other tenures.
- Duration risk and the large supply of central and state government paper have set a floor to longer-tenured loans and debt paper.
- Bank expect another 25 - 50 bps cut in the policy rate over the near term and yield management operations such LTROS and conventional open-market operation to pick up in H2FY20.

Operation activates

- 2/3 of bank's employees outside of the branches are working from home. Certain branch staff come in to service customers on a rotational basis.
- On an average, the bank had customer interactions of 2.25 lakh per day, totaling to 68 lakh customer interactions in the month.
- Bank has acquired 1.2 Mn liability customers, ~13,000 accounts a day (~ 80% of Q1FY20).
- ~95% of the branches and ~13,000 ATMs across the country are operational.
- Bank has added 72 branches & 1,002 BCS during the quarter. In addition, ~ 200 branches are in various stages of readiness to open in a short time.
- Lower costs in various sales channels, promotional activities & discretionary spend contributed to a better Cost to income ratio than recent trends.

Payment Business

- Payment business volumes, both acquiring & issuance, in June '20 saw a bounce back to ~ 70% of January '20 levels.
- Strong tractions are seen on the categories such as daily essentials, medical expenses, food home delivery etc. Since these are low-ticket spends with high frequency, it led to higher engagement levels with customers on payment instruments.
- While travel & hospitality spends have been muted, spends have increased in segments such as online education, video subscription services etc

Balance Sheet strength

- Bank has improved the risk rating of its balance sheet by 30 bps to 4.3%.
- Almost all of the QoQ attrition in the book came from top half of a 10-point internal rating scale, which has served the bank well over the years.
- Bank has achieved 100% self-funding for the BBG portfolio in May, and closed in June at 103%.
- Weighted Avg rating on the unsecured book stood at a 3.45, vs Avg portfolio rating of 4.43 and Avg secured portfolio of 4.81. The historical trends of delinquency suggest, there is a 55% lower probability of default in the unsecured wholesale book than there is in the secured wholesale book.

Asset Growth

- The bank continued to diversify its book and reduce concentration. Its next 100 programs contributed to approximately 1/3 of the Y-o-Y asset book attrition.
- ~ 70 - 78% of the Q-o-Q and the Y-o-Y gross disbursements, including rollovers, were assets with less than 1-year tenure maturity.
- Retail originations fell by 70% during the quarter, largely due to tightening of credit standards as well as some amount of pessimism in the borrowers.
- The personal loan book saw severe impact, a drop of 86% in origination, a reflection not just of the lockdown but also the bank's own prudence and tightening of credit standards in an otherwise uncertain environment.
- Credit cards sourcing dropped by 87%, with spends fell by 40% and leading to a book contracting by 4.5%.
- SME assets were on a declining trend but received a partial offset QoQ due to credit guarantee scheme.

Asset quality

- The moratorium granted as on June 30, 2020, is about 9% of the bank's loan book. Out of which, 90% of them have come in from moratorium 1.
- Bank has used analytical models in determining the slippages instead of waiting for purely on the roles. The annualized slippage in Q1 was 1.2%.
- Of the Rs 2,740 Cr specific loan loss provisions for Q1, approximately 2/3 of this is due to the accelerated recognition using analytical models.
- The core credit cost ratio stood at 1.08% of advances, as against 1.07% YoY and 0.77% QoQ.
- ~ 86% of the externally rated portfolio is either AAA or AA.
- The personal loan is entirely salaried individuals (98% of them continue to receive salary credits), mostly comes from private enterprises that are very highly rated and of a high quality themselves.
- ~ 97% of personal loan customers in moratorium portfolio today are 0 DPD customers.

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Profit & Loss Account											
Rs Bn	Q4FY20	YOY	QOQ	Q4FY20	Q3FY20	Q2FY20	Q1FY20	Q4FY19	Q3FY19	Q2FY19	Q1FY19
Interest Earned	304	11%	2%	299	294	282	274	263	259	242	225
Interest Expended	147	4%	0%	147	152	147	141	132	133	124	117
NII	**157**	**18%**	**3%**	**152**	**142**	**135**	**133**	**131**	**126**	**118**	**108**
Other Income	41	-18%	-32%	60	67	56	50	49	49	40	38
Net Income	**197**	**8%**	**-7%**	**212**	**208**	**191**	**183**	**180**	**175**	**158**	**146**
Operating expenses	69	-3%	-17%	83	79	74	71	71	67	63	60
PPoP	**128**	**15%**	**-1%**	**130**	**129**	**117**	**111**	**108**	**108**	**95**	**86**
Provisions	39	49%	3%	38	30	27	26	19	22	18	16
Profit Before Tax	**89**	**5%**	**-3%**	**92**	**99**	**90**	**85**	**90**	**86**	**77**	**70**
Tax	23	-23%	1%	22	25	27	30	31	30	27	24
Net Profit	**67**	**20%**	**-4%**	**69**	**74**	**63**	**56**	**59**	**56**	**50**	**46**
Balance Sheet											
Net worth	1780	14%	4%	1710	1636	1558	1556	1492	1430	1372	1077
Deposits	11894	25%	4%	11475	10674	10216	9546	9231	8525	8334	8058
Borrowings	1164	15%	-20%	1446	1133	922	1009	1171	1235	1427	1210
Other liabilities	614	13%	-9%	674	510	555	542	551	496	566	459
Total liabilities	**15451**	**22%**	**1%**	**15305**	**13953**	**13251**	**12653**	**12445**	**11686**	**11699**	**10804**
Cash & Balances	1096	30%	27%	866	1024	735	842	813	567	645	515
Investments	3794	27%	-3%	3918	3113	3071	2985	2906	2798	3001	2757
Advances	10033	21%	1%	9937	9360	8970	8297	8194	7810	7508	7086
Fixed Assets	45	11%	1%	44	43	41	40	40	39	38	36
Other Assets	483	-1%	-10%	539	413	433	488	492	473	507	410
Total Assets	**15451**	**22%**	**1%**	**15305**	**13953**	**13251**	**12653**	**12445**	**11686**	**11699**	**10804**
Important ratios (%)											
Gross NPAs	1.4	10 bps	(5 bps)	1.3	1.4	1.4	1.4	1.4	1.4	1.3	1.3
Net NPAs	0.3	(3 bps)	(10 bps)	0.4	0.5	0.4	0.4	0.4	0.4	0.4	0.4
PCR	76.2	419 bps	650 bps	72.0	66.7	69.7	69.7	71.4	69.7	70.0	69.5
Cost to income ratio	35.0	(397 bps)	(396 bps)	39.0	37.9	38.8	39.0	39.6	38.4	39.9	40.9
CASA	40.1	(209 bps)	44 bps	42.2	39.5	39.3	39.7	42.4	40.7	42.0	41.7
CAR	18.9	40bps	200 bps	18.5	18.5	17.5	16.9	17.1	17.3	17.1	14.6
Break-up of Domestic Retail Advances											
Auto	811	-1%	-3%	839	836	808	819	807	830	803	777
Personal Loans	1,116	15%	-3%	1,156	1,095	1,021	971	930	888	834	779
Home Loans	627	12%	-1%	634	617	600	558	514	518	479	440
Business Banking	606	5%	-6%	641	633	627	577	570	557	542	521
Kisan Gold Card	400	9%	-8%	433	390	391	367	387	351	361	331
Credit Cards	547	10%	-5%	576	577	520	495	466	448	405	385
CV/CE	278	-5%	-4%	290	281	285	292	287	272	255	249
Others	199	10%	-2%	203	200	184	181	181	174	169	163
Two Wheelers	96	-5%	-3%	99	101	99	101	100	101	97	92
Gold Loans	56	6%	3%	54	53	53	52	52	52	52	51
Loans against sec	15	-16%	-17%	18	18	18	18	19	18	18	17
Total	**4,750**	**7%**	**-4%**	**4,944**	**4,801**	**4,606**	**4,432**	**4,314**	**4,209**	**4,015**	**3,805**

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Profit & Loss Account				
Rs Bn	FY19	FY20	FY21E	FY22E
Interest Earned	990	1148	1323	1536
Interest Expended	507	586	691	799
NII	**482**	**562**	**632**	**737**
Other Income	176	233	259	304
Net Income	**659**	**794**	**891**	**1041**
Operating expenses	261	307	339	393
PPoP	**397**	**487**	**551**	**648**
Provisions	76	121	152	169
Profit Before Tax	**322**	**366**	**399**	**479**
Tax	111	103	101	121
Net Profit	**211**	**263**	**298**	**358**

Balance Sheet				
Rs Bn	FY19	FY20	FY21E	FY22E
Net worth	1492	1710	1939	2213
Deposits	9231	11475	13140	15443
Borrowings	1171	1446	1504	1579
Other liabilities	551	674	753	841
Total liabilities	**12445**	**15305**	**17336**	**20077**
Cash & Balances	813	866	1068	1028
Investments	2931	3918	4369	5057
Advances	8194	9937	11291	13356
Fixed Assets	41	45	48	52
Other Assets	466	539	560	584
Total Assets	**12445**	**15305**	**17336**	**20077**

Important ratios				
(%)	FY19	FY20	FY21E	FY22E
Gross NPAs	1.3	1.2	1.9	1.6
Net NPAs	0.4	0.4	0.5	0.5
PCR	71.4	72.0	73.1	70.6
Cost to income ratio	39.7	38.6	38.1	37.7
CASA	42.4	42.2	42.0	41.8
CAR	17.1	18.5	17.7	16.9
Loan to Deposit Ratio	88.8	86.6	85.9	86.5

Important ratios (%)				
(%)	FY19	FY20	FY21E	FY22E
ROA	1.8	1.9	1.8	1.9
ROE	16	16	16	17
Per share (Rs)				
EPS	39	48	54	65
ABVPS	268	305	343	392
P/E	28	23	20	17
P/ABVPS	4.1	3.6	3.2	2.8

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