HDFC Bank

October 18, 2020

DALAL & BROACHA
STOCK BROKING PVT. LTD.

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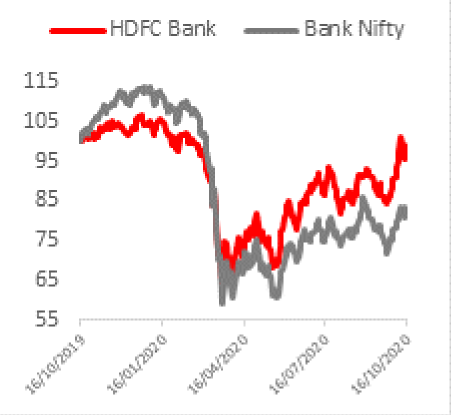
Q2 FY21 Result Update@ Dalal & Broacha

ACCUMULATE	
Current Price (Rs)	1199
52 Week Range	739/1304
Target Price (Rs)	1365
Upside (%)	14

Key Share Data	
Market Cap (Rs.bn)	6599
Market Cap (US$ mn)	89855
No of o/s shares (Cr)	5504
Face Value	1
BSE Code	500180
NSE Code	HDFCBANK
Bloomberg	HDFCB:IN

Price performance



% Shareholding	Sep-20	Jun-20
Promoters	26.02	26.10
FII	37.43	37.04
DII	22.91	21.54
Others	13.65	14.76
Total	100	100

HDFC Bank (HDFCB) reported its Q2FY21 performance which beat our estimates on the profitability front.

- NII came in at INR 157.8 Bn, 0.7% QoQ / 16.7% YoY and 1% below our est.
- Net Income came in at INR 218.7 Bn, 10.8% QoQ/14.5% YoY & 1% below our est.
- PPOP came in at INR 138.1 Bn, 7.7% QoQ / 18.1% YoY and 0.1% above our est.
- Provisions came in at INR 37.0 Bn, -4.8% QoQ/37.1% YoY and 11% below our est.
- PAT came in at INR 75.1 Bn, 12.8% QoQ / 18.4% YoY and 4% above our est.
- EPS stood at INR 13.7 vs INR 12.1 / INR 11.6 in Q1FY21 / Q2FY20 respectively.

Financial Highlights

- Despite the macro headwinds driven by COVID-19, HDFCB has shown healthy credit growth of 15.8% YoY in Q2FY21. Out of which, domestic advances grew by 15.4% YoY, mainly driven by wholesale loan growth of 26.5% YoY, while retail loans grew slower at 5.3% 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 4.4. Considering the management commentary, we expect the bank to sustain above-industry loan growth in the near to medium term.
- On liabilities, Deposits grew by 20.3% YoY/3.4% QoQ in Q2FY21 led by CASA growth of 27.5% YoY/7.1% QoQ taking CASA ratio at 41.6% (Vs 39.3% YoY). Continued focus on strong deposits franchise helped the bank in the maintaining LCR of 153%, well above the regulatory requirement. Bank's capital adequacy ratio stood at 19.1% (vs 17.5% YoY/ 18.9% QoQ), of which Tier I capital was 17.7% (vs 16.2% YoY/ 17.5% QoQ). With strong liability franchise and fixed rate nature of the book, we believe the bank could maintain profitability despite near-term pressure on margins as it maintains a high liquidity ratio to sail through the crisis.
- Bank's asset quality improved during the quarter, with GNPAs sequentially down by 28 bps at 1.08% and NNPAs down by 16 bps to 0.17% on account of standstill levied by the Supreme Court. Excluding the same, GNPAs would have been 1.37% and NNPA would have been 0.35% as per the proforma approach (recognition of NPA using analytical models). Bank held floating provisions of Rs 14.51 Bn and contingent provisions of Rs 63.04 Bn as on Sep 30, 2020. With strong underwriting standards coupled with top quality customer pool and adequate provisioning buffers, we believe the bank is relatively in a better position when compared to peers in terms of NPA additions and credit costs.
- The bank's operational efficiency remained strong, with cost to income ratio falling by 193 bps YoY to 36.8%, backed by higher net income (NII + other income) growth of 14.5% vs opex growth of 8.8% in Q1FY21. We believe this ratio is not sustainable at the current level and expected it (CIR) to be around 38% in the near to medium term. Operating expenses were lower primarily due to lower loan origination & sales volumes. Fess income was also adversely impacted by lower retail loan origination, use of debit and credit cards by customers, efficiency in collection efforts and waivers of certain fees.

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. On the asset quality front, slippages are likely to pick up during 2HFY21 due to the COVID-19 disruption, which could keep credit costs elevated. However, 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. **At CMP the stock trades at 3.5x its FY21E ABV and 3.1x its FY22E ABV. We have maintained a 'Accumulate' rating on HDFC Bank with a price target of Rs 1365, valuing the stock at 3.5x FY22E P/ABV.**

Key Financials (Rs Mn)

Year	NII	PPOP	PAT	ROE	Adj BVPS	P/ABVPS
FY20	563	488	263	16.5	304	3.9
FY21	634	554	295	16.2	339	3.5
FY22	737	648	359	17.3	390	3.1

Highlights of the Conference Call

Asset Quality

- Although as per Supreme Court's order banks can't classifying accounts that are standard as of Aug 31 as NPAs, HDFC Bank using its analytical models recognized some early NPAs (on proforma basis).
- Slippage ratio stood at 0.8% (would have been 1.98% as per analytical models).
- Net recovery for the quarter stood at 22 bps of the advances. Collection was impacted by local lockdowns and overall impact of the same on recoveries was Rs 100 Cr.
- Bank's collection efficiency on the non-morat book stood at 99%, while on the morat book stood at 95% (expects 97% by October end).
- The bank made contingent provisions of Rs 23.04 bn (including Rs 11.3bn for specific accounts and Rs11.73bn to strengthen the balance sheet).
- SMA and overdue accounts where moratorium or deferment were announced stood at Rs 157.4 Bn. Amount where asset classification benefit has been extended stood at Rs 46.39 Bn.
- Unsecured exposure rated at 3.5 avg on internal rating scale; very safe and much lower risky than aggregate secured

Business segments

- The bank's disbursements in Q2FY21 have been at 80-85% level of last year. Retail assets showing first signs of recovery, disbursals 2.5x of Q1FY21, recovery is stronger.
- In wholesale SME, the bank added 1,550 new customers which is 3x of Q1.
- The bank is posting double digit growth in government business and rural and semi-urban in both secured and unsecured segments.
- According to management, the bank has achieved growth in wholesale banking without dilution in rating standards. The weighted average rating of the book on an internal scale is currently at 4.4, while incremental lending is also at a rating of 4.4. Besides, 75% of the externally rated book is AA & above rated and 93% is A rated & above.
- Bank remains cautious and prudent on MFI segment, expect recovery in 90 days.
- Merchant acquiring as well as card issuances have picked up, hitting 97% level of last year.

Economic activity

- The bank's rural checks suggest strong rural demand (tractor sales, good monsoon, good water storage levels etc; rural growth story is intact).
- As per payroll account data, Bank didn't saw steep job losses, though there are some job losses in select sectors at limited level.
- Bank seeing good OD utilization for inventory buildup ahead of festive season

Other Highlights

- Bank's continuous focus on strong deposits franchise helped in the maintenance of a healthy liquidity coverage ratio at 153%, well above the regulatory requirement. This excess liquidity has impacted NIM by ~15 bps. This drag was partly offset by monetizing some of the investment in form of trading gains.
- Fess income was adversely impacted by lower retail loan origination, use of debit and credit cards by customers, efficiency in collection efforts and waivers of certain fees.
- During the quarter, Bank has added 104 branches and~ 1000 employees. Furthermore, the bank is in the process to open ~100 mor e branches in coming quarters.
- Bank is looking to introduce a digital platform for auto loans in the next 90 days.

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Rs Bn	Q4FY20	YOY	QOQ	Q1FY21	Q4FY20	Q3FY20	Q2FY20	Q1FY20	Q4FY19
Profit & Loss Account									
Interest Earned	300	6%	-1%	304	299	294	282	274	263
Interest Expended	142	-3%	-3%	147	147	152	147	141	132
NII	**158**	**17%**	**1%**	**157**	**152**	**142**	**135**	**133**	**131**
Other Income	61	9%	49%	41	60	67	56	50	49
Net Income	**219**	**14%**	**11%**	**197**	**212**	**208**	**191**	**183**	**180**
Operating expenses	81	9%	17%	69	83	79	74	71	71
PPoP	**138**	**18%**	**8%**	**128**	**130**	**129**	**117**	**111**	**108**
Provisions	37	37%	-5%	39	38	30	27	26	19
Profit Before Tax	**101**	**12%**	**13%**	**89**	**92**	**99**	**90**	**85**	**90**
Tax	26	-2%	14%	23	22	25	27	30	31
Net Profit	**75**	**18%**	**13%**	**67**	**69**	**74**	**63**	**56**	**59**
Balance Sheet									
Net worth	1861	19%	5%	1780	1710	1636	1558	1556	1492
Deposits	12293	20%	3%	11894	11475	10674	10216	9546	9231
Borrowings	1326	44%	14%	1164	1446	1133	922	1009	1171
Other liabilities	614	11%	0%	614	674	510	555	542	551
Total liabilities	**16094**	**21%**	**4%**	**15451**	**15305**	**13953**	**13251**	**12653**	**12445**
Cash & Balances	1080	47%	-1%	1096	866	1024	735	842	813
Investments	4140	35%	9%	3794	3918	3113	3071	2985	2906
Advances	10383	16%	3%	10033	9937	9360	8970	8297	8194
Fixed Assets	46	11%	2%	45	44	43	41	40	40
Other Assets	445	3%	-8%	483	539	413	433	488	492
Total Assets	**16094**	**21%**	**4%**	**15451**	**15305**	**13953**	**13251**	**12653**	**12445**
Important ratios (%)									
Gross NPAs	1.08	(28 bps)	(30 bps)	1.4	1.3	1.4	1.4	1.4	1.4
Net NPAs	0.2	(16 bps)	(25 bps)	0.3	0.4	0.5	0.4	0.4	0.4
PCR	84.5	828 bps	1477 bps	76.2	72.0	66.7	69.7	69.7	71.4
Cost to income ratio	36.8	182 bps	(193 bps)	35.0	39.0	37.9	38.8	39.0	39.6
CASA	41.6	146 bps	233 bps	40.1	42.2	39.5	39.3	39.7	42.4
CAR	19.1	20 bps	160 bps	18.9	18.5	18.5	17.5	16.9	17.1
Break-up of Domestic Retail Advances									
Auto	797	-1.4%	-1.7%	811	839	836	808	819	807
Personal Loans	1,124	10.2%	0.8%	1,116	1,156	1,095	1,021	971	930
Home Loans	628	4.7%	0.3%	627	634	617	600	558	514
Business Banking	635	1.3%	4.8%	606	641	633	627	577	570
Kisan Gold Card	435	11.4%	8.8%	400	433	390	391	367	387
Credit Cards	581	11.7%	6.3%	547	576	577	520	495	466
CV/CE	270	-5.3%	-3.0%	278	290	281	285	292	287
Others	208	12.6%	4.1%	199	203	200	184	181	181
Two Wheelers	95	-3.6%	-0.8%	96	99	101	99	101	100
Gold Loans	60	13.5%	8.4%	56	54	53	53	52	52
Loans against sec	16	-13.8%	5.0%	15	18	18	18	18	19
Total	**4,850**	**5.3%**	**2.1%**	**4,750**	**4,944**	**4,801**	**4,606**	**4,432**	**4,314**

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Profit & Loss Account				
Rs Bn	FY19	FY20	FY21E	FY22E
Interest Earned	990	1149	1322	1533
Interest Expended	507	586	688	796
NII	**482**	**563**	**634**	**737**
Other Income	176	233	259	304
Net Income	**659**	**795**	**893**	**1041**
Operating expenses	261	307	339	393
PPoP	**397**	**488**	**554**	**648**
Provisions	76	121	159	169
Profit Before Tax	**322**	**367**	**394**	**479**
Tax	111	103	99	121
Net Profit	**211**	**263**	**295**	**359**

Balance Sheet				
Rs Bn	FY19	FY20	FY21E	FY22E
Net worth	1492	1710	1936	2211
Deposits	9231	11475	13140	15443
Borrowings	1171	1326	1379	1448
Other liabilities	551	614	697	785
Total liabilities	**12445**	**15125**	**17152**	**19887**
Cash & Balances	813	808	886	838
Investments	2931	3918	4369	5057
Advances	8194	9937	11291	13356
Fixed Assets	41	45	48	52
Other Assets	466	539	558	584
Total Assets	**12445**	**15247**	**17152**	**19887**

Important ratios				
(%)	FY19	FY20	FY21E	FY22E
Gross NPAs	1.3	1.2	1.9	1.6
Net NPAs	0.4	0.4	0.6	0.5
PCR	71.4	72.0	67.6	70.4
Cost to income ratio	39.7	38.6	38.0	37.7
CASA	42.4	42.2	42.0	41.8
CAR	17.1	19.9	19.0	18.0
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	304	339	390
P/E	31	25	22	18
P/ABVPS	4.5	3.9	3.5	3.1

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