

HDFC Ltd.

20 February 2023

Reuters: HDFC.BO; Bloomberg: HDFC IN

Management meet note

We recently hosted the management of HDFC Ltd., represented by Mr. Conrad D'souza, Member of the Executive Management & Chief Investor Relations Officer as a part of our week long investors' conference. The management indicated that the overall business environment continues to remain healthy, driven by both Retail as well as Wholesale segments. Within the Non-retail segment (excluding the run-down portfolio), growth remains healthy. On the margin front, the management stated that the same has largely bottomed out as the lead-lag effect of the rate hikes is over and expects margins to normalize going forward. The company has some exposure to a large conglomerate, largely towards their residential projects and does not expect any asset quality issues from the same. We continue to remain positive on HDFC on the back of its stable market share in a growing Housing Finance sector and its ability to deliver 2%+ ROAs. We maintain our BUY rating on HDFC with a target price (TP) of Rs3,159 (SOTP-based).

Management Meet Key takeaways

On exposure to Adani Group

- The management indicated that they don't have any major exposure to Adani Group companies. They have some marginal exposure to a few residential projects of Adani Group, but none to any of its major listed entities that may be of big concern.

On business environment

- The overall business environment stands healthy, with Retail loans growing strongly. However, the Wholesale book has contracted partially because of heightened competitive intensity and run-down of the non-compliant book, as per banking norms.
- The management indicated that run-away growth is not visible as of now and it is normalizing around historical range of 15-18%.
- Within the Non-individual book, there has been a decline as the company has been running down the book not eligible under banking norms. Stripping this away, the management indicated that growth has been healthy. The pending amount in the run-down book stands at ~Rs70bn. Moreover, the company has requested for the RBI's approval for loans with near term maturity to be kept in the merged entity's book.
- The Affordable Housing segment has witnessed some slowdown for the past one year, but volume is returning to normalcy now.
- The relative weakness in housing loans has been on account of the festive season in Oct-Nov'22. However, the momentum from Dec'22 has been healthy.
- Geographically, the company hasn't witnessed any pullback from any specific region. Following the merger, loans will be sourced from more geographies, which is likely to aid growth.
- Asset quality has been improving along with strong Collection Efficiency (CE).

On margins

- There has been some downward pressure on NIM for the last two quarters as the rate hikes have been rapid while loan re-pricing has happened with a lag.
- The management indicated that all the rate hikes have now been passed on and another hike pass-through is likely to be announced w.e.f 1st March, 2023.
- The company is witnessing normalcy 3QFY23 onwards and expects NIMs to broadly bottom out around the current levels.
- On the funding side, interest rates have spiked significantly over the past year. But, from a mid-term perspective, they are only 60bps above pre-covid levels.
- Mortgages have historically been in the range of 8-10%. Additionally, the management does not expect any major impact from rate hikes as interest rate are an important factor but not the only factor for customers to opt for a housing loan.
- Also, the company hasn't witnessed any drop in loan application inflow post the rate hikes.

Merger

- The management does not expect any significant challenges in the process of integration with the bank as over the years the regulatory environment for banks and NBFCs has been converging, which makes the merger now all the more sensible.
- Post-merger, the existing deposit book will be held till maturity; thereafter, funding will depend on the bank's requirements.
- Additionally, the bank will be able to control BT-out better. Pre-payments currently are ~11%, of which ~3% is BT-out. However, BT-in rate is also similar.
- NCLT hearing for the merger is scheduled on 27th Feb, 2023. The merger is expected to be finalized by 2QFY24-end.

BUY

Sector: NBFC

CMP: Rs2,654

Target Price: Rs3,159

Upside: 19%

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Key Data

Current Shares O/S (mn)	1,829.2
Mkt Cap (Rsbn/US\$bn)	4,857.7/58.7
52 Wk H / L (Rs)	2,934/2,026
Daily Vol. (3M NSE Avg.)	2,699,071

Price Performance (%)

	1 M	6 M	1 Yr
HDFC Ltd	(2.2)	7.6	8.8
Nifty Index	(1.0)	0.5	3.3

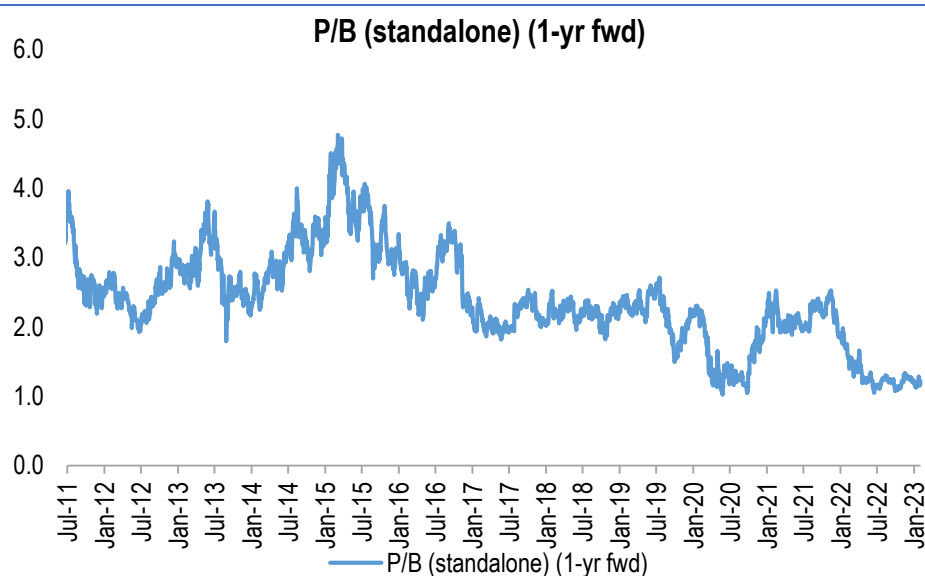
Source: Bloomberg

Exhibit 1: Financial summary

(Rsmn)	FY21	FY22	FY23E	FY24E	FY25E
Net Interest Income	163,620	180,755	200,991	244,539	283,141
Operating profit	177,631	191,783	213,044	245,538	282,443
PAT	120,273	137,422	168,980	179,197	213,088
EPS (Rs)	67	76	93	99	117
BV (Rs)	603	663	707	771	847
P/E (x)	16.5	14.5	11.8	11.2	9.4
P/BV (consol.)	2.9	2.6	2.4	2.1	1.9
ROA (%)	2.2	2.3	2.5	2.3	2.4
ROE (%)	12.2	12.1	13.6	13.8	15.0
Gross stage 3	2.3	2.3	1.5	1.8	1.8
Net stage 3	1.2	1.1	0.7	0.9	0.9

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: One-year forward P/BV (standalone)



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 3: Income statement

Y/E March (RsMn)	FY21	FY22	FY23E	FY24E	FY25E
Interest Income	449,768	448,147	547,987	634,421	732,277
Interest Expense	286,148	267,392	346,996	389,882	449,136
Net Interest Income	163,620	180,755	200,991	244,539	283,141
Non-Interest Income	31,991	31,755	35,605	27,030	28,030
Net Revenue	195,611	212,510	236,596	271,569	311,171
Operating expenses	17,980	20,727	23,553	26,031	28,728
Operating profit	177,631	191,783	213,044	245,538	282,443
Provisions	29,480	19,320	3,415	21,821	16,416
PBT	148,151	172,463	209,629	223,717	266,027
Tax	27,878	35,041	40,649	44,520	52,939
PAT	120,273	137,422	168,980	179,197	213,088

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Balance sheet

Y/E March (RsMn)	FY21	FY22	FY23E	FY24E	FY25E
Share capital	3,608	3,626	3,635	3,635	3,635
Reserves & surplus	1,084,219	1,198,884	1,280,434	1,396,913	1,535,420
Shareholders' funds	1,087,826	1,202,510	1,284,069	1,400,547	1,539,054
Borrowings	4,413,650	4,996,810	5,762,838	6,727,868	7,727,469
Other liability & provisions	174,510	209,303	246,230	280,243	320,213
Total liabilities	5,675,986	6,408,623	7,293,137	8,408,658	9,586,736
Investments	686,368	685,922	806,797	941,902	1,043,208
Loans	4,852,730	5,548,570	6,305,469	7,258,145	8,305,783
Other assets	136,889	174,131	180,871	208,611	237,745
Total assets	5,675,986	6,408,623	7,293,137	8,408,658	9,586,736

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Key ratios

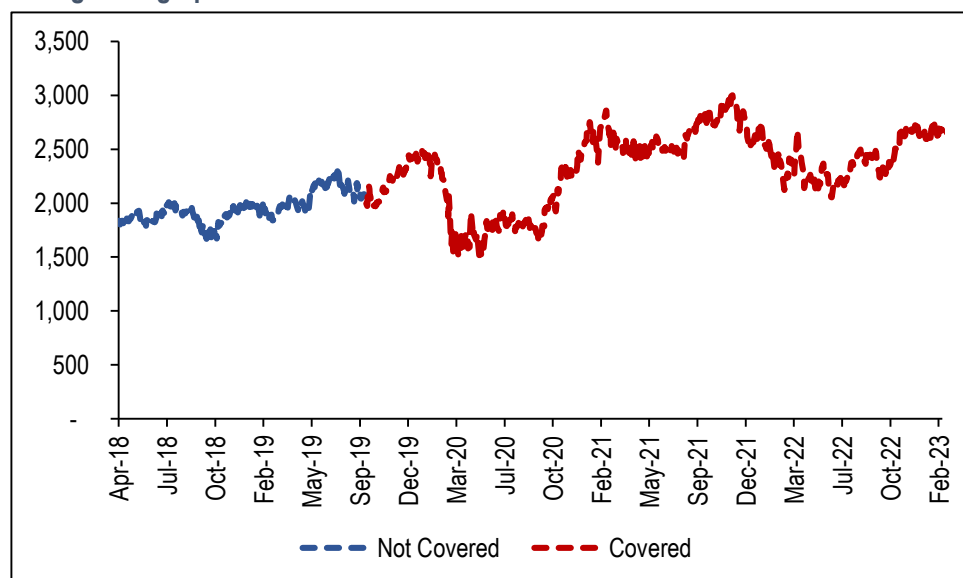
Y/E March- Ratios	FY21	FY22	FY23E	FY24E	FY25E
Growth (%)					
NII	17.9	10.5	11.2	21.7	15.8
Operating profit	-32.4	8.0	11.1	15.3	15.0
Profit after tax	-32.3	14.3	23.0	6.0	18.9
Loans	10.5	14.1	13.1	15.2	14.4
Spreads (%)					
Yield on loans	8.8	7.7	8.6	8.4	8.5
Cost of borrowings	6.7	5.7	6.4	6.2	6.2
NIM	3.0	3.0	3.0	3.1	3.2
Operational efficiency (%)					
Cost/income	9.2	9.8	10.0	9.6	9.2
Cost/AUM	0.3	0.3	0.3	0.3	0.3
CRAR (%)					
Tier I	21.5	22.2	22.9	22.2	21.8
Tier II	0.7	0.6	0.5	0.5	0.5
Total CRAR	22.2	22.8	23.4	22.7	22.3
Asset quality (%)					
Gross stage 3	2.3	2.3	1.5	1.8	1.8
Net stage 3	1.2	1.1	0.7	0.9	0.9
ECL stage 3	52.1	54.3	53.1	50.5	50.4
Credit cost	0.6	0.4	0.1	0.3	0.2
Profitability (%)					
ROA	2.2	2.3	2.5	2.3	2.4
ROE (core business)	12.2	12.1	13.6	13.8	15.0
Per share (Rs)					
EPS	67	76	93	99	117
BVPS	603	663	707	771	847
BV (consol.)	918	1025	1118	1237	1375
ABV (consol.)	887	993	1093	1200	1334
Valuation (x)					
P/E	16.5	14.5	11.8	11.2	9.4
P/BV (consol.)	2.9	2.6	2.4	2.1	1.9
P/ABV (consol.)	3.0	2.7	2.4	2.2	2.0

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
17 September 2019	Buy	1,985	2,527
7 October 2019	Buy	1,978	2,528
5 November 2019	Buy	2,180	2,655
8 January 2020	Buy	2,406	2,760
28 January 2020	Buy	2,396	2,771
27 March 2020	Buy	1,755	2,519
9 April 2020	Buy	1,559	2,519
26 May 2020	Buy	1,515	2,062
9 July 2020	Buy	1,886	2,204
31 July 2020	Buy	1,811	2,101
23 September 2020	Buy	1,676	2,469
7 October 2020	Buy	1,934	2,488
3 November 2020	Buy	2,022	2,483
26 November 2020	Buy	2,190	2,620
08 January 2021	Buy	2,661	3,067
03 February 2021	Buy	2,653	3,128
21 February 2021	Buy	2,745	3,195
7 May 2021	Buy	2,496	3,142
2 August 2021	Buy	2,462	3,120
30 August 2021	Buy	2,718	3,154
26 September 2021	Buy	2,839	3,325
1 November 2021	Buy	2,890	3,379
2 February 2022	Buy	2,611	3,407
21 February 2022	Buy	2,454	3,530
3 May 2022	Buy	2,259	3,410
31 July 2022	Buy	2,389	3,121
19 September 2022	Buy	2,414	3,276
04 November 2022	Buy	2,497	3,225
02 February 2023	Buy	2,613	3,159
20 February 2023	Buy	2,654	3,159

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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