

HDFC Bank BUY

Second Covid wave led deterioration in asset quality

Summary
HDFC Bank's asset quality deteriorated due to second Covid-19 wave as GNPA stood at 1.47% vs 1.36% YoY (1.32% QoQ) while NNPA at 0.5% vs 0.3% YoY (0.4% QoQ). Annualized slippage ratio increased to 2.54% vs 1.2% YoY (1.66% QoQ). Restructured assets stood at 80bps of advances as of Q1FY22; led by retail portfolio. However, 2/3rd of this constitutes unsecured assets. Collections were impacted in April and May however picked up in June. Advances growth remains stable at 14.4% YoY vs 14.0% YoY in Q4FY21 led by wholesale loans (10.2% growth) and retail loan growth of 9.3%. Deposits growth slowdown to 13% YoY (16% YoY in Q4FY21) while, CASA growth remain robust at 28%. NII grew slowly by 9% YoY due to decline in NIMs. PPOp grew by 18% YoY as cost to income ratio remains stable at 35%; fee income grew by 74% YoY and sequentially down by 23%. Provision grew by 24% YoY resulted into high credit cost at 1.5% vs 1.1% YoY. Thus, lower PAT growth at 16% YoY. As overall economy expected to improve in H2FY22, we believe that HDFCB would see the best revival in growth within the sector. We have largely retained our estimates and have BUY rating with the new target price of Rs.1,790 (earlier 1,740) based on P/Bv of 3.6x FY23.

Key Highlights and Investment Rationale

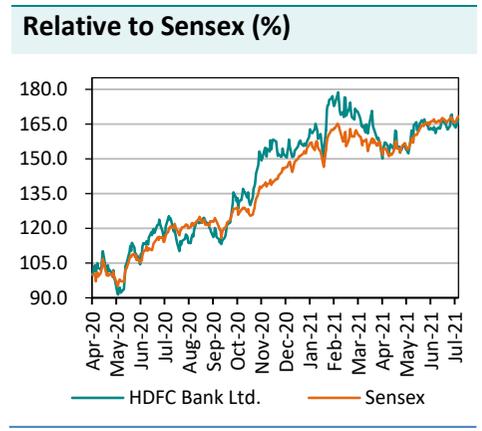
- Moderate Credit as well as deposit growth; sequentially lowers:** HDFCB reported stable credit growth of 14.4% YoY (1% QoQ) vs 14% YoY FY21. Domestic Corporate book slow down to 10% (22% in Q4FY21) and retail book improves to 9% vs 7% YoY (Q4FY21). Post lockdown, Bank witnessed a sharp bounce back in the demand for most of key products; gold loans continue to saw strong growth of 30% (7% in Q1FY21). In mortgages, home and LAP businesses, The first 15 days trends of July'21 suggest ~100% of pre-COVID levels on the disbursement and expects in Q2FY22 will scale up. Deposits growth slowdown to 13% YoY (1% QoQ) vs 16% YoY (5% QoQ) in Q4FY21; CASA deposits grew by 28% resulted CASA ratio at 45.5% vs 40.1% YoY.
- Asset quality deteriorates; restructuring at 80bps:** Bank Asset quality deteriorated with GNPA at 1.47% vs 1.36% YoY (1.32% QoQ); NNPA remain at 0.5% vs 0.3% YoY. Core Credit cost comes in at 1.5% vs 1.1% QoQ (1.1% YoY). Bank annualized slippages stood at 2.54% vs 1.2% YoY (1.66% QoQ). Restructuring advances stands at 80bps (2/3rd from unsecured assets) vs 60bps earlier. However, Bank expects some addition in Q2FY22.
- Outlook:** HDFC Bank continues to command highest market share amongst private banks. We believe HDFCB to traverse through these tough times and will gain market share led by strong leadership position across segments, large distribution, digital focus and strong capital adequacy. We remain structurally positive on HDFCB given its superior credit underwriting, structurally better NIM and the ability to maintain higher RoA among its peers.

TP	Rs1,790	
CMP	Rs1,522	
Potential upside / downside	18%	
V/s Consensus		
EPS (Rs)	FY22E	FY23E
IDBI Capital	66.7	80.6
Consensus	67.7	81.0
% difference	(1.4)	(0.6)

Shareholding Pattern (%)	
Promoters	26.0
FII	39.8
DII	16.6
Public	17.6

Price Performance (%)			
	-1m	-3m	-12m
Absolute	3.8	6.5	38.4
Rel to Sensex	2.2	(2.3)	(5.2)

Key Stock Data	
Bloomberg / Reuters	HDFCB IN/HDBK.BO
Sector	Bank
Shares o/s (mn)	5,527
Market cap. (Rs mn)	8,410,008
Market cap. (US\$ mn)	112,205
3-m daily avgTrd value (Rs mn)	--
52-week high / low	Rs1,650/994
Sensex / Nifty	53,140 / 15,923



Financial snapshot					(Rs mn)
Year	FY2019	FY2020	FY2021	FY2022E	FY2023E
NII	482,431	561,862	648,796	743,693	866,467
Net Profit	210,780	262,573	311,165	367,958	444,110
EPS (Rs)	38.7	47.9	56.4	66.7	80.6
ABV (Rs)	270.7	308.0	363.9	433.2	496.7
PER (x)	39.3	31.8	27.0	22.8	18.9
P/ABV (x)	5.6	4.9	4.2	3.5	3.1
ROE (%)	16.5	16.4	16.6	16.6	17.2
ROA (%)	1.8	1.9	1.9	2.0	2.1
GNPA (%)	1.4	1.3	1.3	1.4	1.3
NNPA (%)	0.4	0.4	0.4	0.2	0.3
CAR (%)	17.1	18.5	18.8	19.4	19.0

Source: Company; IDBI Capital Research

Conference Call Highlights

Digital and Card business

- UPI transaction (by count), P2P and P2M have sequentially grown by 5% to 0.65bn as against 2.4x in prior years and by value it grew by 11% (sequentially) to 1,650bn. UPI (value terms), P2P market share at 10% and P2M market share at 14%
- Transaction count seen growth of 103% yoy in mobile banking and 39% in net banking.
- Bank has 14.9mn cards (June end) with market share 23.8% (May'21). Spends per active cards for bank was at 1.4x higher than industry and average ticket size is 1.2x higher than industry.
- Bank share in fee based stands at 56% and market share in issuing cards stands at 28.5% (May'21). 1/3rd or 1/4th of the fee income constitute from card.
- Card balances were Rs600bn as against Rs640bn (Q4FY21). Revolving balances are down due to credit and a lower card spends while bank is cautious on extending credit. 3/4th banks credit card customer hold deposit with bank with aggregate balances amounting to 5x of card outstanding.
- As per RBI data, Bank acquiring market share stands at 50.5% (April'21) vs 44% (April'20).

Asset quality

- The annualized slippage ratio for the quarter stood at 2.54% as against 1.66% qoq and 1.2% yoy. Excluding slippages in the agricultural segment, the slippage was at 2.2% against 1.1% qoq and 1.17% yoy.
- Sale of NPAs was at Rs18bn in the quarter. Slippages were Rs70bn within that agri. Stood at Rs9bn. Write off stood at Rs31bn (1.05%) for the quarter as against Rs15bn (Q1FY21).
- Recoveries account to 14bps of gross advances (Q1FY22) vs 26bps qoq and 9bps yoy. Recoveries in June were better than April and May while is not back to pre-covid level but back to March level.
- 0 dpd reverted back to pre-covid level. Overall bounce rate not back to pre-covid level but good recovery in June and in July there is further recovery. According to NACH data, Bank had 50% better bounce rate.
- Demand resolution in early bucket impacted in April and May.

Restructuring

- Restructuring stands at 70 bps (June'21) vs 60bps earlier and together restructuring 1.0 and 2.0 it stands at 80bps. Expect some addition in Q2FY22.
- 2/3rd constitutes unsecured assets and 1/3rd is from secured assets. Bulk would be from retail.

Collection and Bureau data

- Collections were picked up in March but momentum stalled in April and May. Collection resolutions were hampered but recoveries were quite sharp.
- Bureau enquiry going up in faster pace for bank but quality of this enquiry is at 760-767 kind of bureau score. Every single product bank has 33% 40% 50% better penetration into the higher scores.

Deposit

- Retail constituted about 82% of total deposits and incrementally contributed Rs370bn+ in Q1FY22.
- Current account increased by 24% yoy, however, it declined by Rs260bn in Q1FY22 because of wholesale segment. Savings account grew by 30% yoy (Rs980bn+) and sequentially grew by 5.6% (Rs220bn). Retail constituted about 88% of CASA deposits.
- Time deposits in the retail segments grew by 6.6% yoy and 3.7% sequentially. Time deposits in the wholesale segment decreased by 7% yoy and decreased 3% sequentially.
- New portfolios are holding up and have better quality than historic portfolio.

Retail Banking

- Bureau data at an industry level and demand for retail loans in the month of June'21 stands at 80% of Q4FY21.
- Bank witnessed a sharp bounce back in the demand for most of key products like auto loans, unsecured loans, LAP and home loans.
- Bank plan to focus a little more aggressively on certain segments like the government segment and have gain decent market share in 4W. In Auto loans and 2W bank have gained substantial market share.
- In mortgages, home and LAP businesses Bank are originating and growing faster yoy. The first 15 days trends of July'21 Bank is adding almost 100% of pre-COVID levels on the disbursement and further in Q2FY22 will scale up to growth rate.

SME Portfolio

- Every single bucket (7, 15, 30 and 60 PA bucket) the delinquency numbers are improving qoq.
- Average utilization remains range bound in a 70% to 75% of the limit sanctioned bracket.
- Incremental NPAs for the quarter have lower than those of the previous quarter and gross NPA levels also remain very range bound. However, Collateralization of the portfolio is in range of 67-72% and as high as mid 80%.

Corporate Portfolio

- Internal rating is in range of 4.3-4.4. The unsecured wholesale portfolio on an average rated at 3.5. AAA and AA portfolio stand at 80% of the book and at least 50% of book is on an HTB1 related scales.
- Pay down increased due to corporate deleverage and bank continues to gain market share. Wholesale credit growth largely coming from PSU and continue to provide liquidity quality NBFCs for onlending and PSL.

Commercial and Rural Banking

- CRB (mid-market segment) growth stood at 25% yoy and 8% qoq. Emerging enterprises group (Retail SME business) saw asset growth of 52% yoy and 9% qoq.
- Transportation finance business remained flat qoq, and up about 8% yoy. Under CV & CE and tractors, Bank increased volumes by 160% led to market share in June in MSPV was 29%.
- Business remains on track to expand its footprint over 100 cities by the end of the year.
- Bank saw credit offtake across a wide spectrum of industries, such as metals and mining, manufacturing and engineering, auto and ancillaries agri. food, beverages etc, growth was from both existing and NTB.
- Bank see growth and CapEx demand in sectors such as steel, textiles, chemicals, durables, paper and packaging, food processing, tractors, et cetera.
- New NPA Remained at a flat run rate to last year and 50% lower than two years ago. Overdraft utilizations were at 20% while exiting June. Collections of last 3 half yearly cycles were impacted in early part of the quarter but are accumulated and collected.

HDB Financial

- NPA stood at 7.75% vs 3.89% qoq. Adequate Capitalize and capital ratio stands at 20%.
- Collection activity were postpone incl. auction while not done any assets sale and restructuring in Q1FY22. Restructured book stood at Rs36.5bn (Mar'21) within that Rs1.20bn impacted.

Other highlights-

- Bank activities were impacted for almost 2/3rd of the quarter.
- **Healthcare initiative-** Bank is extending loan as per RBI guidelines and also activated patient EMI and Debit and credit card programme with 200+ hospitals.
- **Net interest income-** NII got impacted due to lower yielding asset mix, including lower card yield and revolver balances, higher interest reversal due to delinquencies and higher mandatory cash reserve ratio.
- **Cost to income-** C/I remains stable at 35%. Expect to increase as activity in retail front pick up and will revert back to 38-39% as in short term.
- **ECLGS-** ECLGS 1.0 was at Rs300bn, ECLGS 2.0 and 3.0 stands at Rs25-30bn.
- During the quarter, 1.64mn (increase of 40% Q1FY21) liability relationships were opened. Added 45 branches and has 150 branches in various stages of readiness to be opened soon as situation improves.
- Bank already submitted auditor report and Awaiting response from RBI.

Exhibit 1: Quarterly Snapshot

(Rs mn)

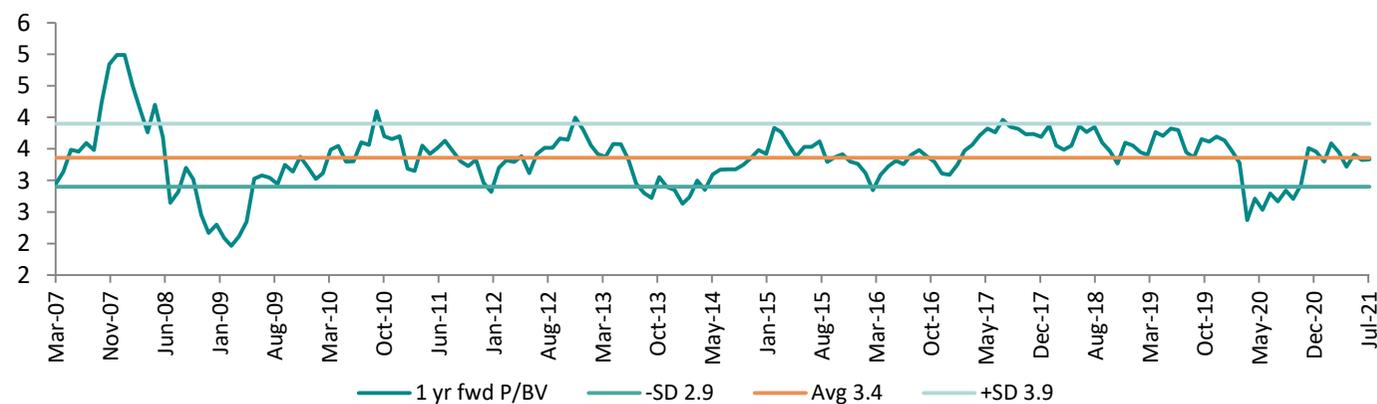
Year-end: March	Q1FY22	Q1FY21	Q4FY21	YoY (%)	QoQ (%)
Interest Income	304,829	303,779	304,236	0.3	0.2
Interest Expenses	134,740	147,126	133,034	(8.4)	1.3
Net Interest Income	170,089	156,653	171,202	8.6	(0.7)
NIM Calc.(%)	4.3	4.5	4.4	(23 bps)	(14 bps)
Non-Interest Income	62,885	40,753	75,939	54.3	(17.2)
Operating Income	232,974	197,406	247,141	18.0	(5.7)
Staff Cost	27,656	25,134	26,789	10.0	3.2
Other Op Exp	53,948	43,980	65,024	22.7	(17.0)
Total Operating Expenses	81,604	69,114	91,813	18.1	(11.1)
<i>Cost to Income (%)</i>	<i>35.0</i>	<i>35.0</i>	<i>37.2</i>	<i>2 bps</i>	<i>(212 bps)</i>
Operating Profit	151,370	128,292	155,328	18.0	(2.5)
Provisions	48,308	38,915	46,937	24.1	2.9
PBT	103,062	89,377	108,391	15.3	(4.9)
Tax	25,766	22,791	26,526	13.1	(2.9)
<i>-effective tax rate</i>	<i>25.0</i>	<i>25.5</i>	<i>24.5</i>	<i>(50 bps)</i>	<i>53 bps</i>
PAT	77,296	66,586	81,865	16.1	(5.6)
EPS (Rs)	28.0	24.3	29.7	15.3	(5.8)
BV (Rs)	768.9	648.3	739.1	18.6	4.0
Deposits	13,458,293	11,893,873	13,350,602	13.2	0.8
Advances	11,476,516	10,032,989	11,328,366	14.4	1.3

Source: Company; IDBI Capital Research

Exhibit 2: ROE Decomposition

(%)	FY19	FY20	FY21	FY22E	FY23E
NII	4.18	4.05	3.96	3.99	4.03
Fees	1.49	1.54	1.30	1.31	1.32
Other Income	0.03	0.14	0.24	0.23	0.22
Net Revenue	5.71	5.73	5.50	5.52	5.58
Op.Exp	2.26	2.21	2.00	2.04	2.11
Op.Profit	3.44	3.51	3.50	3.48	3.47
Provisions	0.65	0.88	0.96	0.84	0.70
PBT	2.79	2.64	2.54	2.64	2.76
Tax	0.96	0.75	0.64	0.66	0.70
ROA	1.83	1.89	1.90	1.97	2.07
Leverage (x)	9.04	8.67	8.75	8.40	8.31
ROE	16.50	16.40	16.61	16.57	17.19

Source: Company; IDBI Capital Research

Exhibit 3: One-year forward P/ABV


Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Net interest income	561,862	648,796	743,693	866,467
Fee Income	213,006	212,894	243,560	284,002
Treasury Gains	19,602	39,154	42,533	47,769
Operating Income	794,470	900,844	1,029,786	1,198,238
Operating expenses	(306,975)	(327,226)	(380,822)	(453,627)
Employee expenses	(95,257)	(103,648)	(112,907)	(127,025)
Other expenses	(211,718)	(223,578)	(267,916)	(326,602)
Pre-Provision Profit	487,495	573,618	648,963	744,611
Provision	(121,424)	(157,028)	(157,238)	(151,120)
Loan loss Provisions	(90,833)	(114,502)	(146,136)	(142,001)
Other Provisions	(30,591)	(42,526)	(11,102)	(9,119)
PBT	366,071	416,590	491,726	593,491
Taxes	(103,498)	(105,425)	(123,767)	(149,382)
Net profit	262,573	311,165	367,958	444,110

Balance Sheet

(Rsmn)

Year-end: March	FY20	FY21	FY22E	FY23E
Capital	5,483	5,513	5,513	5,513
Reserves	1,704,377	2,031,696	2,399,654	2,757,421
Networth	1,709,860	2,037,209	2,405,167	2,762,934
Deposits	11,475,023	13,350,602	15,219,782	17,564,754
Borrowings	1,446,286	1,354,873	1,466,153	1,808,569
Total Liab. & Equity	15,305,113	17,468,705	19,851,349	23,114,998
Cash & Bank with RBI	866,187	1,194,705	1,205,055	1,421,965
Investments	3,918,267	4,437,282	5,014,542	5,600,785
Advances	9,937,029	11,328,366	13,027,621	15,372,593
Other Assets	539,311	459,259	551,111	661,333
Total assets	15,305,113	17,468,705	19,851,349	23,114,998

Growth

(%)

Year-end: March	FY20	FY21	FY22E	FY23E
Growth				
Deposits	24.3	16.3	14.0	15.4
Advances	21.3	14.0	15.0	18.0
NII	16.5	15.5	14.6	16.5
Pre-Provision Profit	22.6	17.7	13.1	14.7
Net Profit	24.6	18.5	18.3	20.7
Spreads				
Yield on Assets	9.0	7.9	7.9	7.9
Cost of Funds	5.0	4.1	4.1	4.0
NIM	4.4	4.3	4.3	4.3
CASA	42.2	46.1	46.0	47.0
Operating Efficiency				
Cost-to-Income	38.6	36.3	37.0	37.9
Cost-to-Assets	2.2	2.0	2.0	2.1
Asset Quality				
GNPA	1.3	1.3	1.4	1.3
NNPA	0.4	0.4	0.2	0.3
Provision Coverage	72.0	69.8	82.5	81.0
Credit Cost	1.0	1.1	1.2	1.0
Capital Adequacy				
CAR	18.5	18.8	19.4	19.0
Tier I	17.2	17.6	18.0	17.5
Valuation				
EPS	47.9	56.4	66.7	80.6
ABV	308.0	363.9	433.2	496.7
P/E	31.8	27.0	22.8	18.9
P/ABV	4.9	4.2	3.5	3.1
ROE	16.4	16.6	16.6	17.2
ROA	1.9	1.9	2.0	2.1
RORWA	2.7	2.9	2.8	2.7

Source: Company; IDBI Capital Research



Notes

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Key to Ratings Stocks:
BUY: 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.

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