

RETAIL EQUITY RESEARCH

HDFC Ltd.

NBFC

BSE CODE: 500010

NSE CODE: HDFC

Bloomberg CODE: HDFC:IN SENSEX: 26,878

BUY

Rating as per Large cap

12months investment period

CMP Rs1217 TARGET Rs1400 RETURN 15%

06th January 2017

Better placed among housing finance companies (HFCs)

HDFC is a leading provider of Housing Finance in India with a network of 285 offices catering to over 2,400 towns & cities spread across the country.

- HDFC has consistently maintained healthy performance and low delinquencies over past couple of years despite slowdown in the economy.
- Loan growth was healthy at 15.7% YoY in H1FY17 on the back of strong business performance in the individual loan segment (↑18% YoY).
- Asset quality remained stable as Gross NPA increased only 1bp sequentially to 0.8% in H1FY17.
- We expect adjusted net profit (excluding one-off income) to increase at a CAGR of 14.2% over FY16-18E backed by healthy NII growth (↑12.2% CAGR).
- While the pace of loan growth will moderate in H2FY17, the long-term growth prospects of HDFC remains intact given its leadership position.
- HDFC is the best placed in the housing finance space given its competitive edge over its peers through strong business growth, stable margin and well-managed asset quality. Hence, we assign BUY rating on the stock with a TP of Rs1,400 based on SOTP valuation.

AUM to grow at a moderate pace post demonetization

HDFC reported healthy assets under management (AUM) growth of 16.5% YoY in H1FY17 on the back of strong business performance in the individual loan segment with 18% YoY AUM growth. Loan mix continues to favour retail mortgages which now constitutes 74% of overall loans. However, growth in corporate loan book was slower at 13% YoY due to persistent slowdown in real estate sector and heavy inventory built up, especially in Tier I and metro cities. We expect AUM to grow at a moderate pace of ~13.9% CAGR for FY16-18E led by individual loan book (↑15%). Further, HDFC will have limited impact of expected fall in real estate prices post demonetization given its limited exposure to loan against property (LAP) segment (<5% of loan book).

Healthy operating matrices

Net Interest Income (NII) grew 10.8% YoY in H1FY17 mainly driven by 17% YoY growth in individual loan segment. However, net interest margin (NIM) declined 7 bps YoY to 3.1% mainly due to increased competition and reduction in the proportional contribution of higher yielding corporate loan book. With rising share of individual loans, we expect NIM to remain around current level over FY16-18E. The company reported adjusted net profit growth of 9.3% YoY to Rs3,242cr. We expect adjusted net profit (excluding one-off income) to increase at a healthy CAGR of 14.2% over FY16-18E backed by higher NII and lower operating expenses.

Stable asset quality

HDFC reported a stable trend in asset quality as gross non-performing assets (NPA) increased only 1bp sequentially to 0.8%. Gross NPA in the individual loan segment increased marginally by 2 bps QoQ to 0.61% while gross NPA in non-individual loan segment was stable at 1.11%. Further, the company maintained 100%+ provision coverage ratio. Hence, we remain relatively comfortable towards overall asset quality profile and expect it to remain broadly stable (Gross NPA <1.0%) over FY16-18E.

Outlook & Valuation

While the housing finance sector may see some near-term pain, the long-term prospects of HDFC remain intact given its competitive edge over its peers through strong growth in business, stable margin and well-managed asset quality. Further, other key components i.e. HDFC bank, Gruh finance, Insurance and Asset management businesses too will continue to strongly contribute to the parent's valuation. Hence, we assign BUY rating on the stock with a TP of Rs1,400 based on sum of the parts (SOTP) methodology where we value its standalone business at Rs814 (P/ABV of 3.0x for FY18E) and subsidiaries at Rs586.

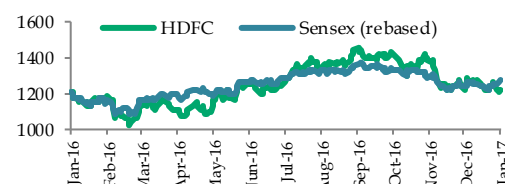
Company Data

Market Cap (Rs cr)	192,833
Outstanding Shares (cr)	158.4
Free Float	100%
Dividend Yield	1.4%
52 week high	Rs1,463
52 week low	Rs1,012
6m average volume (cr)	0.3
Beta	1.3
Face value	Rs2

Shareholding %	Q4 FY16	Q1 FY17	Q2 FY17
Promoters	0.0	0.0	0.0
FII's	77.4	76.9	77.3
MFs/Insti	10.4	11.3	11.3
Public & Others	12.2	11.8	11.5
Total	100.0	100.0	100.0

Price Performance	3mth	6mth	1 Year
Absolute Return	-14.4%	-3.4%	0.6%
Absolute Sensex	-4.8%	-1.1%	5.1%
Relative Return*	-9.6%	-2.3%	-4.5%

*over or under performance to benchmark index



Y.E Mar (Rscr)	FY16	FY17E	FY18E
Net Interest Income	9,076	10,141	11,427
Growth (%)	9%	12%	13%
NIM (%)	3.3	3.3	3.2
Pre Pro Profit	10,823	11,611	12,137
Growth (%)	23%	7%	5%
Net Profit	7,093	7,760	8,281
Growth (%)	18%	9%	7%
EPS	44.9	49.0	52.3
Growth (%)	18%	9%	7%
P/E	27.1	24.8	23.3
P/BV	5.6	5.0	4.5
P/ABV	5.6	5.0	4.5
RoE (%)	21.8	21.4	20.3
RoA (%)	2.6	2.5	2.4



Quarterly Financials (Standalone)

Profit & Loss Account

(Rs cr)	H1FY17	H1FY16	YoY Growth %
Interest Income	15,016	13,875	8.2
Interest Expense	10,372	9,683	7.1
Net Interest Income	4,644	4,192	10.8
Non-Interest Income	1,480	575	157.3
Total Net Income	6,124	4,768	28.5
Operating Expenses	432	390	10.8
Employee Cost	199	174	14.5
Other Operating Exp.	233	216	7.9
Total Income	16,496	14,451	14.2
Total Expenditure	10,804	10,073	7.3
Pre-Provisioning profit	5,692	4,378	30.0
Provisions	435	102	326.5
Profit Before Tax	5,257	4,276	23.0
Tax	1,560	1,310	19.1
Net Profit	3,697	2,966	24.7
EPS - Diluted (Rs)	23.4	18.8	24.2

Business Performance (Rs cr)	H1FY17	H1FY16	YoY Growth %
AUM	311,300	267,100	16.5
Loans	275,400	238,000	15.7
Borrowings	255,500	218,900	16.7

Key Ratios (%)	H1FY17	H1FY16	YoY bps
Net Interest Margin	3.2	3.4	(14)
Cost of Borrowings	8.7	9.4	(61)
Yield on AUM	11.7	12.3	(63)
Cost to Income	7.1	8.2	(112)
Debt to Equity	6.9	6.5	44
Capital Adequacy	16.5	16.1	40
Tier I Capital	13.3	12.8	50
Gross NPA	0.8	0.7	5
Net NPA	0.0	0.1	(8)
Provision Coverage	113.0	89.0	2400
Credit Cost	0.6	0.2	41
ROE (Ann.)	20.8	18.3	251
ROA (Ann.)	2.6	2.4	22

Source: Company, Geojit BNP Paribas Research

Sum of the parts (SOTP) valuation

Particulars	Basis	Multiple	Year	Value/Share
HDFC (standalone)	ABV	3.0x	FY18E	814
HDFC Bank	Target Price		FY18E	475
Gruh Finance	Market Price			40
Life Insurance	Embedded Value	4.0x	FY16	159
General Insurance	Recent Stake Sale			16
Asset Management	5% of AUM		FY18E	43
			20% holding discount to subsidiaries	147
		Target Price		1,400



Standalone Financials

Profit & Loss Account

Y.E March (Rs cr)	FY14	FY15	FY16	FY17E	FY18E
Interest Income	23,338	26,272	28,450	30,788	34,378
Interest Expense	16,029	17,975	19,375	20,646	22,951
Net Interest Income	7,309	8,297	9,076	10,141	11,427
% Change	13.8	13.5	9.4	11.7	12.7
Non-Interest Income	859	1,199	2,506	2,298	1,587
Net Income	8,168	9,496	11,582	12,439	13,014
Operating Expenses	628	707	759	828	878
Total Income	24,198	27,471	30,957	33,086	35,965
Total Expenditure	16,657	18,682	20,133	21,474	23,828
Pre-Prov. Profit	7,540	8,789	10,823	11,611	12,137
% Change	12.2	16.6	23.1	7.3	4.5
Provisions	100	165	715	553	335
Profit Before Tax	7,440	8,624	10,108	11,058	11,802
Tax	2,000	2,634	3,015	3,298	3,520
Tax Rate (%)	27	31	30	30	30
Net Profit	5,440	5,990	7,093	7,760	8,281
% Change	12.2	10.1	18.4	9.4	6.7
No. of Shares (cr)	156	157	158	158	158
EPS (Rs)	34.9	38.0	44.9	49.0	52.3
% Change	11.2	9.1	18.0	9.1	6.7

Balance Sheet

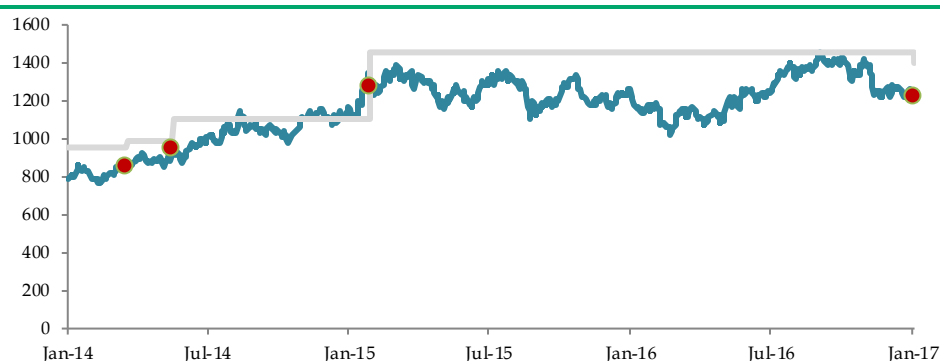
Y.E March (Rs cr)	FY14	FY15	FY16	FY17E	FY18E
Liabilities					
Capital	312	315	316	317	317
Reserves & Surplus	27,643	30,655	33,805	38,117	42,726
Borrowings	183,973	208,599	237,639	267,779	308,799
Provisions	4,054	4,190	4,964	6,134	7,642
Other Liabilities	9,450	10,193	12,028	13,041	14,315
Total Liabilities	225,432	253,952	288,753	325,388	373,799
Assets					
Cash & Bank Balances	7,716	3,365	5,305	4,693	5,610
Investments	13,913	14,294	15,345	16,215	17,289
Advances	201,313	232,231	263,853	299,844	345,775
Fixed Assets	280	677	665	665	665
Other Assets	2,211	3,385	3,585	3,971	4,461
Total Assets	225,432	253,952	288,753	325,388	373,799

Ratios

Y.E March (Rs)	FY14	FY15	FY16	FY17E	FY18E
EPS	34.9	38.0	44.9	49.0	52.3
DPS	14.0	15.0	17.0	18.5	20.0
BV	179.1	196.7	216.0	242.6	271.7
ABV	176.3	195.8	216.0	242.1	271.3
Valuation (%)					
P/E	34.9	32.0	27.1	24.8	23.3
P/BV	6.8	6.2	5.6	5.0	4.5
P/ABV	6.9	6.2	5.6	5.0	4.5
Div. Yield	1.2	1.2	1.4	1.5	1.6
Spreads (%)					
Yield on Funds	11.5	11.2	10.4	9.9	9.7
Cost of Funds	9.4	9.1	8.7	8.2	8.0
Capital (%)					
CAR	14.6	16.1	16.6	16.6	16.2
Tier I	12.1	12.5	13.2	13.2	12.8
Tier II	2.5	3.6	3.4	3.4	3.4
Asset (%)					
GNPA	0.7	0.7	0.7	0.9	0.9
NNPA	0.0	0.1	0.0	0.1	0.1
PCR	0.7	0.7	0.7	0.9	0.9
Management (%)					
Debt/Equity	6.6	6.7	7.0	7.0	7.2
Cost/Income	7.7	7.4	6.6	6.7	6.7
Earnings (%)					
NIM	3.6	3.5	3.3	3.3	3.2
ROE	20.6	20.3	21.8	21.4	20.3
ROA	2.6	2.5	2.6	2.5	2.4



Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit BNP Paribas Research

Dates	Rating	Target
21 April 2014	BUY	988
20 May 2014	BUY	1,106
30 January 2015	BUY	1,455
06 January 2017	BUY	1,400

Investment Rating Criteria

Large Cap Stocks;

Buy	-	Upside is 10% or more.
Hold	-	Upside or downside is less than 10%.
Reduce	-	Downside is 10% or more.

Mid Cap and Small Cap;

Buy	-	Upside is 15% or more.
Accumulate*	-	Upside between 10% - 15%.
Hold	-	Absolute returns between 0% - 10%.
Reduce/Sell	-	Absolute returns less than 0%.
To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.		

The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/ negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating.

* For reasons of valuations/return/ lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

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