

Execution on track; marching toward steady growth and profitability

NIMs to revive gradually

We met the top management team of HDFC Bank (HDFCB) represented by Mr. Sashi Jagdishan, CEO; Mr. Srinivasan V, CFO; and Mr. Bhavin Lakhpatwala, Head IR & Strategy, to discuss the bank's growth, margin outlook and post-merger progress. Here are the key takeaways from the discussion:

Loan growth momentum to sustain; aims to double balance sheet in 4-5 years

Loan growth is likely to remain healthy, and the bank expects to double its balance sheet in the next ~4-5 years, which implies growth to remain closer to its historical run rate. Growth momentum in the mortgage business remains strong. About 70% of HDFC customers were new to the bank (NTB), of which 40% have already opened savings account with the bank. Asset quality in the unsecured book remains pristine, and with improved competitive intensity and pricing environment after the recent RBI measures, the bank remains confident of reporting stronger growth in the unsecured space as well. Strong growth in the mortgage business and its focus on cross-sell of other secured/unsecured retail products will enable healthy growth. The outlook on corporate borrowings is turning better and the bank expects to benefit from the potential revival in the capex cycle after the upcoming general elections. **We estimate HDFCB to sustain a ~17% CAGR in loans over FY24-26.**

Strategic branch expansion driving deposit growth and productivity

HDFCB plans to continue with its aggressive branch expansion run rate of 1,400-1,500 branches in FY24 and aims to increase its total branch count to 13k-14k to sustain its growth trajectory over the medium term. The bank's credit-deposit ratio stands elevated at 107% amid merger, hence it focuses on deposit mobilization, which remains its key source of funding. The branch expansion decisions are taken after analytically mapping all the pin codes and assessing competition, deposit potential, existing presence and potential to become the top liability-sourcing bank in the region. The consistent pace of branch expansion and continued investments affirm the bank's commitment to deliver a sustainable growth over the long term.

Focus on robust liability franchise; aiming for a CASA mix of ~39-40% within 18-24 months

Granular and high-quality liability franchise remains a key priority for the bank even as it does not want to compete on rates in the market. Despite the rate-sensitive nature of wholesale deposits (>INR50m), a majority of its deposits come from retail sources (~80-85%). Though the CASA mix has declined to 38% in 2QFY24, the bank has noted its overall market share in incremental CASA flows remains higher than the outstanding deposit market share. While we remain watchful on the CASA mix over the near term due to widened SA and TD rates, the bank indicated that it aims to sustain a CASA mix of 39-40% over the next 18-24 months. The improving vintage of branch network will enable a steady rise in deposit productivity over time, and the bank notes that more than 10-year old branches are able to garner 10-75x more deposits than less than 5-year old branches. **We estimate a ~20% CAGR in the bank's deposit base over FY24-26.**

HDFC Bank



Mr. Sashidhar Jagdishan,
HDFC Bank

Mr. Jagdishan joined HDFCB as a manager in the finance department in 1996 and became Business Head – Finance in 1999. He became CFO of the bank in 2008 and took charge as the CEO in Oct'20. He has overall experience of over 30 years and is a qualified CA. He holds a Master's degree in Economics from the University of Sheffield, UK

NIM recovery to be gradual; Opex and credit cost remain twin levers to drive RoA to steady ~2%

HDFCB indicated that NIM recovery is likely to be gradual as deposit rates and competitive intensity in the industry remain high. Though, the bank said that margins are currently at the lower end of the spectrum and should recover to 3.7% in 18-24 months while recovery to ~4.1% will take further 2-3 years. Operating costs are likely to remain under control, while a well-diversified loan bank will keep credit costs under control over the coming years. Together these two levers will help the bank to sustainably achieve RoA of ~2% over the coming years. The consistent improvement in cost ratios (bank reaffirmed its guidance to reduce C/I ratio to ~30% over the long term) and a long-term recovery in margins increase the prospect of RoA sustainably surpassing the 2% mark over the long term.

Other highlights:

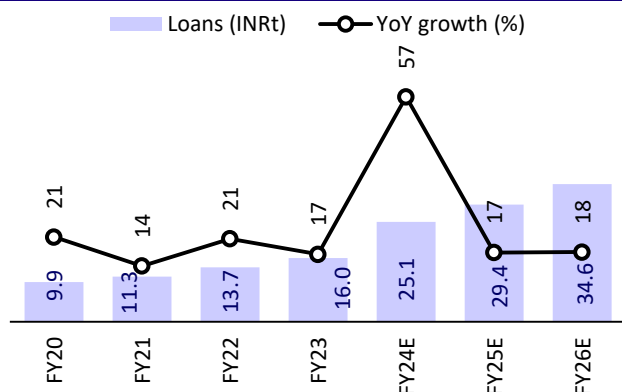
- **Loan related:** The bank has an average ticket size of INR0.5m in personal loans and ~INR4-4.5m in mortgage loans. HDFCB has been focusing on the salaried segment, but after merger it is confident on asset quality of the self-employed segment as well.
- **Turnaround time:** For the salaried segment, the bank has reduced its turnaround time to 2 days from 7 days and has also reduced it significantly for the self-employed segment (from ~14-20 days earlier).
- **Capex cycle:** The bank is well positioned to capitalize on the impending revival in the capex cycle and expects improved corporate demand after May'24 elections.
- **Digital journey and capabilities:** HDFCB has launched separate journeys for savings account, consumer durables and credit card, which helps customers open accounts in just one click. The bank will launch its new app and start offering a 10-second NTB personal loan, credit card and business loan from 15th Dec'23.
- **Others:** HDFCB has lost some share in credit card spending, but those were mainly in unprofitable segments. After watching for two cycles, the bank will look to have partnerships with fintechs and also intends to do small elements of co-lending.

Valuations and view:

HDFCB has everything in place to deliver strong profitability and growth trajectory over the coming years (similar to pre-merger levels) and the management believes that execution remains the most important factor for the bank. HDFCB is confident of sustaining the steady growth momentum and has highlighted that it has been able to maintain its incremental market share of ~16-20% despite an increase in its size. While execution at such a large scale is inherently complex, especially amid intense competition for liabilities and rates staying elevated for longer than initially thought, we expect the bank's operating performance to recover gradually over FY25/FY26. We expect margins to recover to 3.7% by FY26E and expect improvements in cost ratios, which should enable a ~22% CAGR in PPOP over FY24-26E, leading to RoA/RoE of ~2%/17% by FY26E (thus reaching back to pre-merger levels). **We maintain BUY with a TP of INR1,950 (premised on 2.7x FY25E ABV + INR209 from subs).**

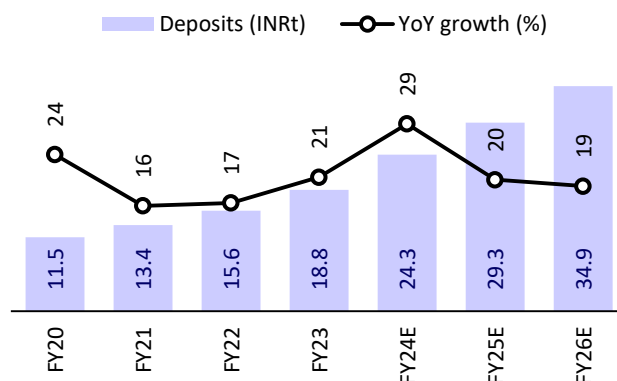
STORY IN CHARTS

Exhibit 1: Advances to see ~17% CAGR over FY24-FY26E



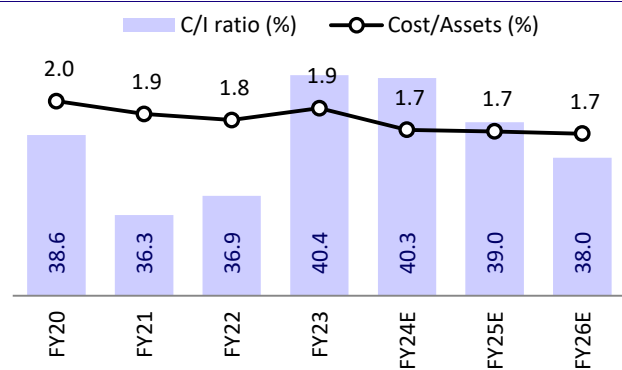
Source: MOFSL, Company

Exhibit 2: Estimate 20% CAGR in deposits over FY24-FY26E



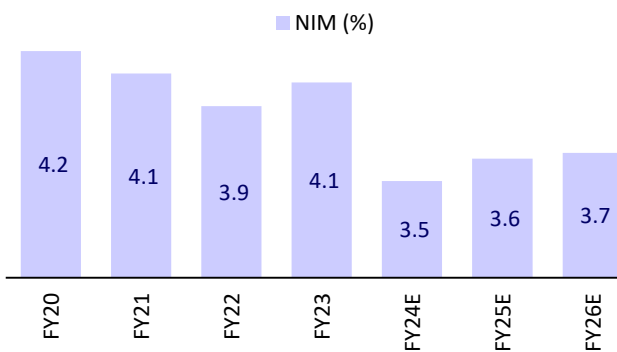
Source: MOFSL, Company

Exhibit 3: Cost-income ratio to moderate to 38% by FY26E



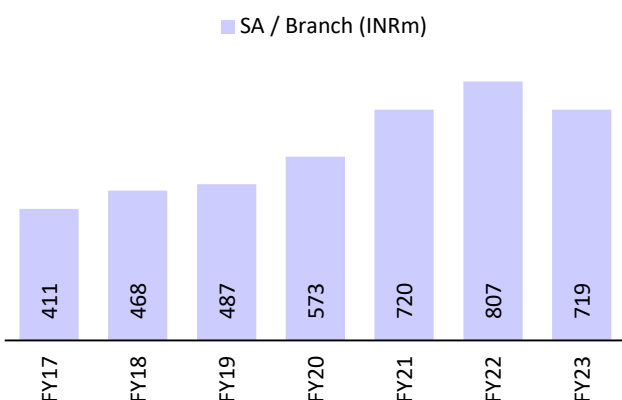
Source: MOFSL, Company

Exhibit 4: NIMs to decline to 3.5% in FY24 and improve gradually



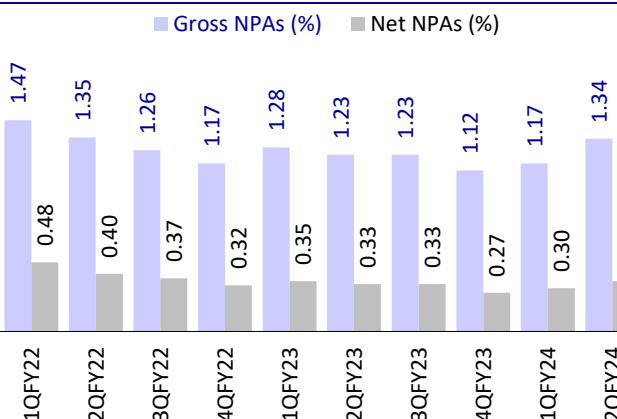
Source: MOFSL, Company

Exhibit 5: We expect SA/Branch of HDFCB to improve further



Source: MOFSL, Company

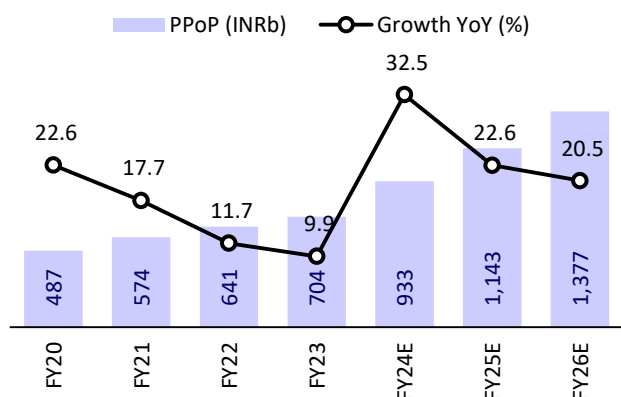
Exhibit 6: GNPA/NNPA ratio stood at 1.34%/0.35% in 2QFY24



Source: MOFSL, Company

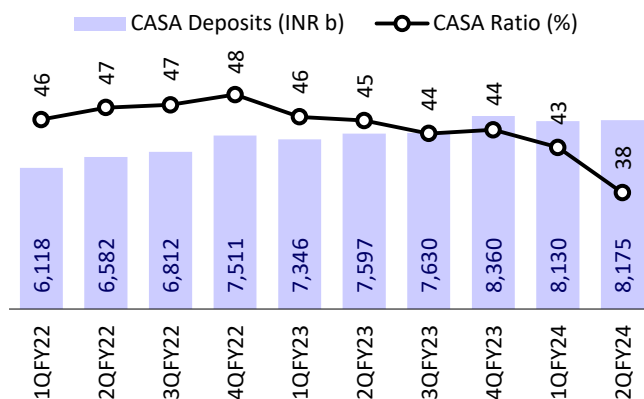
STORY IN CHARTS

Exhibit 7: PPOp to see a growth of ~20.5% YoY by FY26



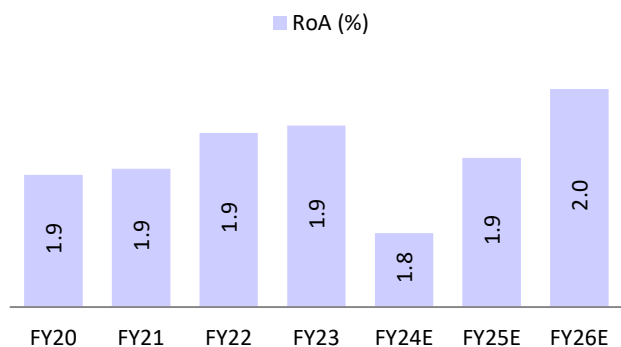
Source: MOFSL, Company

Exhibit 8: CASA ratio moderated to 38% in 2QFY24



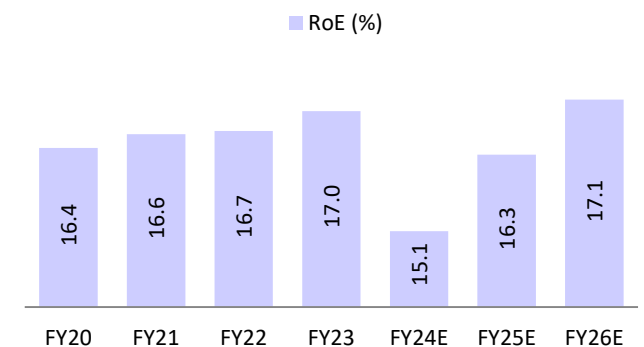
Source: MOFSL, Company

Exhibit 9: ROA to increase to 2.0% by FY26E



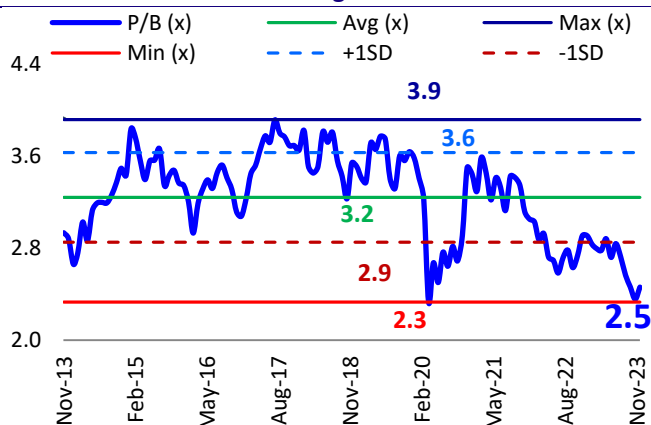
Source: MOFSL, Company

Exhibit 10: ROE to rise to pre-merge levels by FY26E after a dip in FY24E



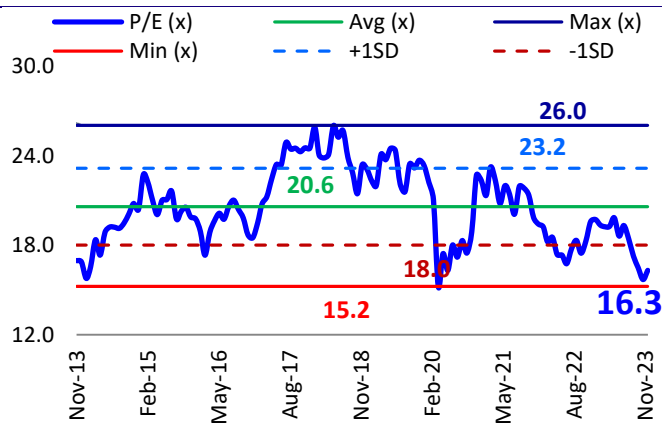
Source: MOFSL, Company

Exhibit 11: HDFCB PB is trading at 2.5x



Source: MOFSL, Company

Exhibit 12: HDFCB PE is at 16.3x in Nov-23



Source: MOFSL, Company

Exhibit 14: SOTP-based pricing

	Stake (%)	Value INRb	Value USD b	Per Share INR	% of Total	Rationale
HDFC Bank		13,102.2	158.8	1,741	89.3	❖ 2.7x FY25E ABV
HDB Financial Ser	94.8	570.8	6.9	76	3.9	❖ 3.5x FY25E Net worth
HDFC Securities	95.5	203.4	2.5	27	1.4	❖ 18x FY25E PAT
HDFC Life Insurance	50.4	788.7	9.6	105	5.4	❖ 2.8x FY25E EV
HDFC Ergo General Insurance	50.5	130.1	1.6	17	0.9	❖ 25x FY25E PAT
HDFC AMC	52.5	244.0	3.0	32	1.7	❖ 26x FY25E PAT
HDFC Credila	10.0	10.1	0.1	1	0.1	❖ 3.5x FY25E BV
Bandhan Bank	5.0	20.1	0.2	3	0.1	❖ 1.6x FY25E BV
Total Value of Subs		1,967.2	23.8	261	13.4	
Less: 20% holding Disc		393.4	4.8	52	2.7	
Value of Subs (Post Holding Disc)		1,573.7	19.1	209	10.7	
Target Price		14,675.9	177.9	1,950		

Exhibit 14: DuPont Analysis: Return ratios to remain healthy

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Net Interest Income	4.05	3.96	3.77	3.83	3.31	3.40	3.42
Core Fee Income	1.38	1.15	1.22	1.24	1.10	1.13	1.15
Trading and others	0.30	0.39	0.33	0.13	0.14	0.16	0.16
Non-Interest income	1.68	1.54	1.55	1.38	1.24	1.28	1.32
Total Income	5.73	5.50	5.32	5.21	4.55	4.69	4.74
Operating Expenses	2.21	2.00	1.96	2.10	1.83	1.83	1.80
Employee cost	0.69	0.63	0.63	0.68	0.58	0.59	0.58
Others	1.53	1.36	1.33	1.42	1.25	1.24	1.22
Operating Profits	3.51	3.50	3.36	3.11	2.71	2.86	2.94
Core operating Profits	3.22	3.11	3.03	2.97	2.58	2.70	2.78
Provisions	0.88	0.96	0.79	0.53	0.34	0.34	0.35
PBT	2.64	2.54	2.57	2.58	2.38	2.52	2.59
Tax	0.75	0.64	0.63	0.63	0.55	0.62	0.63
RoA	1.89	1.90	1.94	1.95	1.83	1.90	1.95
Leverage (x)	8.7	8.7	8.6	8.7	8.3	8.6	8.8
RoE	16.4	16.6	16.7	17.0	15.1	16.3	17.1

Financials and valuations

Income Statement

(INRb)

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	1,148.1	1,208.6	1,277.5	1,615.9	2,590.4	3,074.1	3,560.0
Interest Expense	586.3	559.8	557.4	747.4	1,453.1	1,713.3	1,955.8
Net Interest Income	561.9	648.8	720.1	868.4	1,137.3	1,360.9	1,604.1
Growth (%)	16.5	15.5	11.0	20.6	31.0	19.7	17.9
Non Interest Income	232.6	252.0	295.1	312.1	424.5	513.7	616.4
Total Income	794.5	900.8	1,015.2	1,180.6	1,561.8	1,874.5	2,220.5
Growth (%)	20.6	13.4	12.7	16.3	32.3	20.0	18.5
Operating Expenses	307.0	327.2	374.4	476.5	629.1	731.1	843.3
Pre Provision Profits	487.5	573.6	640.8	704.0	932.6	1,143.4	1,377.3
Growth (%)	22.6	17.7	11.7	9.9	32.5	22.6	20.5
Core PPP	465.9	549.2	601.7	663.2	873.7	1,067.8	1,287.5
Growth (%)	22.5	17.9	9.6	10.2	31.7	22.2	20.6
Provisions (excl tax)	121.4	157.0	150.6	119.2	116.2	137.5	165.0
PBT	366.1	416.6	490.2	584.9	816.4	1,005.9	1,212.3
Tax	103.5	105.4	120.5	143.8	187.8	246.5	297.0
Tax Rate (%)	28.3	25.3	24.6	24.6	23.0	24.5	24.5
PAT	262.6	311.2	369.6	441.1	628.6	759.5	915.3
Growth (%)	24.6	18.5	18.8	19.3	42.5	20.8	20.5

Balance Sheet

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Equity Share Capital	5.5	5.5	5.5	5.6	7.5	7.5	7.5
Reserves & Surplus	1,704.4	2,031.7	2,395.4	2,796.4	4,348.1	4,957.0	5,714.3
Net Worth	1,709.9	2,037.2	2,400.9	2,802.0	4,355.6	4,964.6	5,721.8
Deposits	11,475.0	13,350.6	15,592.2	18,833.9	24,310.2	29,269.5	34,947.7
Growth (%)	24.3	16.3	16.8	20.8	29.1	20.4	19.4
of which CASA Dep	4,846.3	6,156.8	7,510.5	8,359.9	8,873.2	10,946.8	13,594.7
Growth (%)	23.9	27.0	22.0	11.3	6.1	23.4	24.2
Borrowings	1,446.3	1,354.9	1,848.2	2,067.7	6,851.5	7,503.3	8,209.0
Other Liabilities & Prov.	673.9	726.0	844.1	957.2	1,273.8	1,439.4	1,640.9
Total Liabilities	15,305.1	17,468.7	20,685.4	24,660.8	36,791.1	43,176.7	50,519.4
Current Assets	866.2	1,194.7	1,523.3	1,937.7	2,068.8	2,279.9	2,567.8
Investments	3,918.3	4,437.3	4,555.4	5,170.0	7,362.1	8,613.7	9,991.9
Growth (%)	33.7	13.2	2.7	13.5	42.4	17.0	16.0
Loans	9,937.0	11,328.4	13,688.2	16,005.9	25,050.6	29,409.4	34,556.0
Growth (%)	21.3	14.0	20.8	16.9	56.5	17.4	17.5
Fixed Assets	44.3	49.1	60.8	80.2	136.7	147.3	172.3
Other Assets	539.3	459.3	857.7	1,467.1	2,172.9	2,726.5	3,231.4
Total Assets	15,305.1	17,468.7	20,685.4	24,660.8	36,791.1	43,176.7	50,519.4

Asset Quality

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
GNPA	126.5	150.9	161.4	180.2	320.4	328.4	381.7
NNPA	35.4	45.5	44.1	43.7	85.3	89.3	99.5
Slippages		160.4	268.6	245.4	328.5	408.4	463.7
GNPA Ratio	1.3	1.3	1.2	1.1	1.3	1.1	1.1
NNPA Ratio	0.4	0.4	0.3	0.3	0.3	0.3	0.3
Slippage Ratio	1.9	1.5	2.1	1.7	1.6	1.5	1.5
Credit Cost	1.3	1.5	1.2	0.8	0.5	0.5	0.5
PCR (Excl Tech. write off)	72.0	69.8	72.7	75.8	73.4	72.8	73.9

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Yield & Cost Ratios (%)							
Avg. Yield-Earning Assets	9.0	8.1	7.4	8.0	8.4	8.6	8.5
Avg. Yield on loans	10.1	8.9	7.9	8.6	8.9	9.1	9.0
Avg. Yield on Inv't	6.1	5.6	5.8	6.5	6.8	6.9	6.9
Avg. Cost-Int. Bear. Liab.	5.0	4.1	3.5	3.9	5.0	5.0	4.9
Avg. Cost of Deposits	4.9	4.0	3.4	3.6	4.6	4.7	4.6
Interest Spread	4.0	4.0	3.9	4.1	3.3	3.5	3.6
Net Interest Margin	4.2	4.1	3.9	4.1	3.5	3.6	3.7
Capitalisation Ratios (%)							
CAR	18.3	18.5	18.7	19.3	19.3	18.4	17.8
Tier I	17.0	17.3	17.7	17.1	17.8	17.2	16.7
Tier II	1.2	1.2	1.0	2.1	1.5	1.3	1.1
CET-1		16.9	16.7	16.4			
Business and Efficiency Ratios (%)							
Loans/Deposit	86.6	84.9	87.8	85.0	103.0	100.5	98.9
CASA Ratio	42.2	46.1	48.2	44.4	36.5	37.4	38.9
Cost/Assets	2.0	1.9	1.8	1.9	1.7	1.7	1.7
Cost/Total Income	38.6	36.3	36.9	40.4	40.3	39.0	38.0
Cost/Core Income	39.7	37.3	38.4	41.8	41.9	40.6	39.6
Int. Expense/Int. Income	51.1	46.3	43.6	46.3	56.1	55.7	54.9
Fee Income/Total Income	24.1	20.9	22.9	23.9	24.1	24.0	24.3
Non Int. Inc./Total Income	29.3	28.0	29.1	26.4	27.2	27.4	27.8
Empl. Cost/Total Expense	31.0	31.7	32.1	32.6	31.6	32.0	32.2
Business per Employee (INR m)	197.7	205.5	206.8	201.1	241.5	241.2	238.1
Profit per Employee (INR m)	2.5	2.6	2.6	2.5	3.1	3.1	3.1
Investment/Deposit Ratio	34.1	33.2	29.2	27.5	30.3	29.4	28.6
G-Sec/Investment Ratio	81.2	79.3	80.5	84.6	84.6	84.6	84.6

Valuation

RoE	16.4	16.6	16.7	17.0	15.1	16.3	17.1
RoA	1.9	1.9	1.9	1.9	1.8	1.9	2.0
RoRWA	2.6	2.8	2.8	2.9	2.8	2.9	3.0
Book Value (INR)	312	370	433	502	579	660	760
Growth (%)	13.8	18.5	17.2	16.0	15.3	14.0	15.3
Price-BV (x)	5.3	4.5	3.8	3.3	2.9	2.5	2.2
Adjusted BV (INR)	300	357	420	490	564	643	741
Price-ABV (x)	5.5	4.6	3.9	3.4	2.9	2.6	2.2
EPS (INR)	48.0	56.6	66.8	79.3	83.5	100.9	121.6
Growth (%)	21.2	17.8	18.1	18.6	5.3	20.8	20.5
Price-Earnings (x)	34.4	29.2	24.7	20.8	19.8	16.4	13.6
Dividend Per Sh (INR)	11.9	6.5	15.5	19.0	19.0	20.0	21.0
Dividend Yield (%)	0.7	0.4	0.9	1.1	1.1	1.2	1.3

E: MOFSL Estimates

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NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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