

## Analyst Meet - Merger pangs to drag near-term performance

HDFC Bank, at its Analyst Day, [disclosed details](#) regarding the opening balance sheet of the merged entity along with other details on the merged financials. The incoming networth of HDFC Ltd will stand at INR1.11tn (against INR1.34tn as of Mar-23 i.e. lower by 16%) led by impact of multiple factors: a) provisions b) IGAAP alignment c) tax-related adjustments and d) dividend payout. In addition, given the large excess liquidity build-up in the run up to the merger, the incoming NIM of HDFC Ltd stood at 2% (vs 2.7% for 1QFY24) and this could drag down the merged entity's margins by 25-30bps in the near-term and will recover gradually over the next 2-3 quarters. Additionally, merged entity on an opening basis will see 20bps increase in GNPL given that HDFC's wholesale portfolio has seen asset quality deterioration (GNPL at 6.7% vs 2.9% in Mar-23) as per bank's review. Provisioning alignment also entails the bank raising PCR on GNPLs from 42% to 74% on GNPLs which has been adjusted through the opening networth of the merged entity. As we incorporate these details into our estimates, our "below consensus" FY24/FY25e EPS have been slightly tweaked (1-2% change) while we adjust our BVPS expectations lower given the lower opening networth of HDFC Ltd. Maintain BUY with a target price of INR1850 (values the bank at 2.5x FY25e P/BV).

- HDFC's incoming networth to be lower by 16% over Mar-23:** As per the mgmt., HDFC's opening networth will see impact of multiple factors which include a) harmonization of provisioning policy b) tax-related adjustments c) accounting alignment and d) dividend payout. As a result, HDFC Ltd's opening networth will be lower by ~16% over Mar-23 levels. Standalone BVPS of HDFC Bank will stand at INR519 post-merger vs INR525 pre-merger as on 1st July 2023. The provisioning alignment is an outcome of increased GNPLs in HDFC Ltd's wholesale book (primarily from stage-2 assets) and HDFC Bank choosing to raise coverage on GNPLs to 74% (same as bank vs 42% for erstwhile HDFC). GNPLs of the merged entity will stand at 1.4% (vs 1.2% for the bank earlier).
- Lower NIMs near-term; to improve gradually:** Given the large liquidity build-up in run up to the merger, incoming NIMs of HDFC Ltd stood at 2% (vs 2.7% reported for 1QFY24 by HDFC). The combined entity began the journey with LCR of 125% (vs HDFC's <115% level in a BAU basis). Mgmt indicated that it will take 2-3 quarters to run down the excess liquidity and NIMs will recover gradually from the depressed levels. We expect HDFC Bank's NIM to dip to ~3.6% in 2QFY24 given impact of excess liquidity and I-CRR. Mgmt indicated that they continue to focus on retail deposit build up at the right price and expect to see traction ahead. Cost-income ratio of the merged entity is expected at ~40% (we had pencilled similar estimates earlier).
- Valuations and view:** Given the adjustments to cost ratios and lower NIMs, we tweak our below consensus EPS estimates slightly (we had already built in higher opex). However given changes to the incoming networth, our BVPS estimates are reduced by ~3-4%. Maintain BUY with revised TP of INR1850.

Financial Summary					(INR mn)
Y/E March	FY21A	FY22A	FY23E	FY24E	FY25E
Net Profit	311,165	369,614	441,087	595,642	759,918
Net Profit (YoY) (%)	18.5%	18.8%	19.3%	35.0%	27.6%
Assets (YoY) (%)	14.1%	18.4%	19.2%	47.8%	19.7%
ROA (%)	1.9%	1.9%	1.9%	1.9%	1.9%
ROE (%)	16.6%	16.7%	17.0%	16.7%	16.4%
EPS	56.4	66.7	79.1	79.5	101.5
EPS (YoY) (%)	17.9%	18.1%	18.6%	0.6%	27.6%
<b>PE (x)</b>	<b>28.9</b>	<b>24.4</b>	<b>20.6</b>	<b>20.5</b>	<b>16.1</b>
BV	370	433	502	578	661
BV (YoY) (%)	18.5%	17.2%	16.0%	15.1%	14.4%
<b>P/BV (x)</b>	<b>4.41</b>	<b>3.76</b>	<b>3.24</b>	<b>2.82</b>	<b>2.46</b>

Source: Company data, JM Financial. Note: Valuations as of 18/Sep/2023

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### Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	1,850
Upside/(Downside)	13.6%
Previous Price Target	1,900
Change	-2.6%

### Key Data – HDFCB IN

Current Market Price	INR1,629
Market cap (bn)	INR12,341.0/US\$148.2
Free Float	93%
Shares in issue (mn)	5,512.8
Diluted share (mn)	
3-mon avg daily val (mn)	INR34,785.2/US\$417.7
52-week range	1,758/1,365
Sensex/Nifty	67,597/20,133
INR/US\$	83.3

### Price Performance

%	1M	6M	12M
Absolute	2.4	3.6	8.4
Relative*	-1.6	-11.1	-5.1

\* To the BSE Sensex

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Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

## Exhibit 1. HDFC Bank: Key ratios after merger

## Key Ratios: Merged HDFC Bank



Financials	HDFCB Standalone		Proforma Merged HDFCB Q1FY24
	FY23	Q1FY24	
NIM (interest bearing assets)	4.3%	4.3%	3.9% - 4.0%
NIM (total assets)	4.1%	4.1%	3.7% - 3.8%
Cost to income	40%	43%	~40%
Credit costs as a % of advances	0.7%	0.7%	~0.6%
RoA	2.1%	2.1%	1.9% - 2.0%
RoE	17.4%	17.3%	~16%
EPS – standalone	79	21	20
EPS – consolidated	83	22	22
BVPS – standalone	502	525	519
BVPS – consolidated	519	543	536
Capital adequacy ratio	19.3%	18.9%	19.2%

Source: Company

Exhibit 2. HDFC Bank: Merged Balance Sheet (As of 1<sup>st</sup> July, 2023)Merged summarised balance sheet – 1<sup>st</sup> July 2023

₹ Bn.	HDFCB 30-Jun-23	HDFCB Merged Opening
Share capital & reserves	2,938	3,914
Deposits	19,131	20,638
Borrowings	2,094	6,869
Other liabilities	854	1,125
<b>Total</b>	<b>25,017</b>	<b>32,546</b>
Loans and advances	16,157	22,210
Cash & equivalent	1,607	1,610
Investments	5,658	6,984
Fixed and other assets	1,595	1,742
<b>Total</b>	<b>25,017</b>	<b>32,546</b>

Source: Company

Exhibit 3. HDFC Bank: Asset Quality after merger (As of 1<sup>st</sup> July, 2023)

## Asset quality



Particulars	Mar-23 HDFCB	Jun-23 HDFCB	1 <sup>st</sup> Jul-23 HDFCB Merged
<b>Gross NPA (%)</b>	<b>1.1%</b>	<b>1.2%</b>	<b>1.4%</b>
Retail GNPA (%)	1.0%	0.9%	0.9%
CRB GNPA (%)	1.6%	1.8%	1.8%
CRB ex-Agri GNPA (%)	1.1%	1.2%	1.2%
Wholesale GNPA (%)	0.5%	0.4%	0.4%
e-HDFCL Individual GNPA (%)			1.0%
e-HDFCL Non-Individual GNPA (%)			6.7%
<b>Net NPA</b>	<b>0.3%</b>	<b>0.3%</b>	<b>0.4%</b>
Specific provision coverage (%)	76%	75%	74%
Contingent and floating provisions as a % of advances	0.7%	0.7%	0.7%
Total provisions as a % of advances	2.0%	2.0%	2.2%
Total provisions (ex-specific) as a % of advances	1.1%	1.1%	1.1%

Source: Company

## Financial Tables (Standalone)

Profit & Loss						(INR mn)
Y/E March	FY21A	FY22A	FY23E	FY24E	FY25E	
Net Interest Income	648,796	720,096	868,422	1,133,288	1,464,272	
Profit on Investments	38,670	22,826	-11,312	10,000	10,000	
Exchange Income	24,384	39,079	40,819	51,023	62,248	
Fee & Other Income	188,995	233,193	282,641	336,771	405,286	
<b>Non-Interest Income</b>	<b>252,049</b>	<b>295,099</b>	<b>312,148</b>	<b>397,794</b>	<b>477,534</b>	
<b>Total Income</b>	<b>900,845</b>	<b>1,015,195</b>	<b>1,180,570</b>	<b>1,531,082</b>	<b>1,941,806</b>	
Operating Expenses	327,226	374,422	476,521	613,829	762,632	
<b>Pre-provisioning Profits</b>	<b>573,618</b>	<b>640,773</b>	<b>704,050</b>	<b>917,254</b>	<b>1,179,174</b>	
Loan-Loss Provisions	123,168	113,772	122,060	122,708	164,696	
Provisions on Investments	-168	-145	41	0	0	
Others Provisions	34,029	36,991	-2,904	-2,904	-2,904	
<b>Total Provisions</b>	<b>157,029</b>	<b>150,618</b>	<b>119,197</b>	<b>119,804</b>	<b>161,792</b>	
<b>PBT</b>	<b>416,590</b>	<b>490,155</b>	<b>584,853</b>	<b>797,450</b>	<b>1,017,383</b>	
Tax	105,425	120,541	143,766	201,807	257,465	
<b>PAT (Pre-Extraordinaries)</b>	<b>311,165</b>	<b>369,614</b>	<b>441,087</b>	<b>595,642</b>	<b>759,918</b>	
Extra ordinaries (Net of Tax)	0	0	0	0	0	
<b>Reported Profits</b>	<b>311,165</b>	<b>369,614</b>	<b>441,087</b>	<b>595,642</b>	<b>759,918</b>	
Dividend paid	35,924	86,045	106,015	127,325	134,815	
<b>Retained Profits</b>	<b>275,241</b>	<b>283,568</b>	<b>335,072</b>	<b>468,318</b>	<b>625,103</b>	

Source: Company, JM Financial

Key Ratios					
Y/E March	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Growth (YoY) (%)</b>					
Deposits	16.3%	16.8%	20.8%	26.0%	22.0%
Advances	14.0%	20.8%	16.9%	56.8%	17.0%
Total Assets	14.1%	18.4%	19.2%	47.8%	19.7%
NII	15.5%	11.0%	20.6%	30.5%	29.2%
Non-interest Income	8.4%	17.1%	5.8%	27.4%	20.0%
Operating Expenses	6.6%	14.4%	27.3%	28.8%	24.2%
Operating Profits	17.7%	11.7%	9.9%	30.3%	28.6%
Core Operating profit	14.3%	15.5%	15.8%	26.8%	28.9%
Provisions	29.3%	-4.1%	-20.9%	0.5%	35.0%
Reported PAT	18.5%	18.8%	19.3%	35.0%	27.6%
<b>Yields / Margins (%)</b>					
Interest Spread	3.58%	3.49%	3.64%	3.46%	3.43%
NIM	4.10%	3.92%	4.05%	3.94%	3.90%
<b>Profitability (%)</b>					
Non-IR to Income	28.0%	29.1%	26.4%	26.0%	24.6%
Cost to Income	36.3%	36.9%	40.4%	40.1%	39.3%
ROA	1.90%	1.94%	1.95%	1.95%	1.90%
ROE	16.6%	16.7%	17.0%	16.7%	16.4%
<b>Assets Quality (%)</b>					
Slippages	1.62%	2.38%	1.80%	1.00%	1.10%
Gross NPA	1.32%	1.17%	1.12%	0.63%	0.77%
Net NPAs	0.40%	0.32%	0.27%	0.16%	0.19%
Provision Coverage	69.8%	72.7%	75.8%	74.0%	75.0%
Specific LLP	1.08%	0.81%	0.79%	0.48%	0.55%
Net NPAs / Networth	2.2%	1.8%	1.6%	1.0%	1.2%
<b>Capital Adequacy (%)</b>					
Tier I	17.56%	17.87%	17.13%	18.10%	17.35%
CAR	18.79%	18.90%	19.26%	19.59%	18.63%

Source: Company, JM Financial

Balance Sheet						(INR mn)
Y/E March	FY21A	FY22A	FY23E	FY24E	FY25E	
Equity Capital	5,513	5,546	5,580	7,490	7,490	
Reserves & Surplus	2,031,696	2,395,384	2,796,410	4,320,510	4,945,614	
Deposits	13,350,602	15,592,174	18,833,946	23,733,700	28,955,114	
Borrowings	1,354,873	1,848,172	2,067,656	6,896,495	8,020,853	
Other Liabilities	726,022	844,075	957,222	1,489,296	1,697,797	
<b>Total Liabilities</b>	<b>17,468,705</b>	<b>20,685,351</b>	<b>24,660,815</b>	<b>36,447,490</b>	<b>43,626,868</b>	
Investments	4,437,283	4,555,357	5,170,014	6,724,185	8,223,810	
Net Advances	11,328,366	13,688,209	16,005,859	25,097,300	29,363,841	
Cash & Equivalents	1,194,704	1,523,269	1,937,651	2,646,852	3,104,050	
Fixed Assets	49,093	60,837	80,165	156,745	161,419	
Other Assets	459,259	857,678	1,467,125	1,822,408	2,773,747	
<b>Total Assets</b>	<b>17,468,705</b>	<b>20,685,351</b>	<b>24,660,815</b>	<b>36,447,490</b>	<b>43,626,868</b>	

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY21A	FY22A	FY23E	FY24E	FY25E
NII / Assets	3.96%	3.77%	3.83%	3.71%	3.66%
Other Income / Assets	1.54%	1.55%	1.38%	1.30%	1.19%
Total Income / Assets	5.50%	5.32%	5.21%	5.01%	4.85%
Cost / Assets	2.00%	1.96%	2.10%	2.01%	1.90%
PBP / Assets	3.50%	3.36%	3.11%	3.00%	2.95%
Provisions / Assets	0.96%	0.79%	0.53%	0.39%	0.40%
PBT / Assets	2.54%	2.57%	2.58%	2.61%	2.54%
Tax rate	25.3%	24.6%	24.6%	25.3%	25.3%
ROA	1.90%	1.94%	1.95%	1.95%	1.90%
RoRWAs	2.93%	2.98%	3.00%	3.03%	2.95%
Leverage	8.6	8.6	8.8	8.4	8.8
ROE	16.6%	16.7%	17.0%	16.7%	16.4%

Source: Company, JM Financial

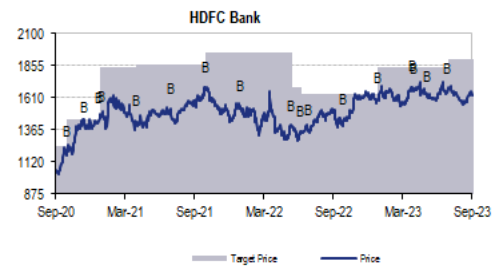
Valuations					
Y/E March	FY21A	FY22A	FY23E	FY24E	FY25E
Shares in Issue	5,512.8	5,545.5	5,579.7	7,489.7	7,489.7
EPS (INR)	56.4	66.7	79.1	79.5	101.5
EPS (YoY) (%)	17.9%	18.1%	18.6%	0.6%	27.6%
PER (x)	28.9	24.4	20.6	20.5	16.1
BV (INR)	370	433	502	578	661
BV (YoY) (%)	18.5%	17.2%	16.0%	15.1%	14.4%
ABV (INR)	369	433	502	578	661
ABV (YoY) (%)	18.5%	17.2%	16.0%	15.1%	14.4%
P/BV (x)	4.41	3.76	3.24	2.82	2.46
P/ABV (x)	4.41	3.76	3.24	2.82	2.46
DPS (INR)	6.5	15.5	19.0	17.0	18.0
Div. yield (%)	0.4%	1.0%	1.2%	1.0%	1.1%

Source: Company, JM Financial

## History of Recommendation and Target Price

Date	Recommendation	Target Price	% Chg.
19-Jul-20	Buy	1,240	
25-Aug-20	Buy	1,240	0.0
18-Oct-20	Buy	1,440	16.1
4-Dec-20	Buy	1,440	0.0
11-Jan-21	Buy	1,840	27.8
16-Jan-21	Buy	1,840	0.0
18-Apr-21	Buy	1,860	1.1
18-Jul-21	Buy	1,860	0.0
17-Oct-21	Buy	1,950	4.8
16-Jan-22	Buy	1,950	0.0
1-Jun-22	Buy	1,690	-13.3
24-Jun-22	Buy	1,640	-3.0
17-Jul-22	Buy	1,640	0.0
16-Oct-22	Buy	1,640	0.0
14-Jan-23	Buy	1,840	12.2
15-Apr-23	Buy	1,840	0.0
21-Apr-23	Buy	1,840	0.0
24-May-23	Buy	1,840	0.0
17-Jul-23	Buy	1,900	3.3
19-Sep-23	Buy	1,850	-2.6

## Recommendation History



## APPENDIX I

## JM Financial Institutional Securities Limited

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Hold	Price expected to move in the range of 10% downside to 10% upside from the current market price for stocks with market capitalisation in excess of INR 200 billion and REITs* and in the range of 10% downside to 15% upside from the current market price for all other stocks, over the next twelve months.
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