

HDFC BANK

Rate rise to slow retail loan growth

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HDFC Bank reported a 32.9% year-on-year growth in net profit for the December 2010 quarter on the back of high loan book growth, better asset quality and higher fee income growth. This should cheer investors, as high profits lower the stock's price-to-earnings ratio, making expensive valuations reasonable.

The bank's high profits were mainly due to a 32.7% YoY growth in advances, driven by its retail book, which grew faster than its corporate loan book. The lower corporate loan book growth was mainly due to one-off loans of six to nine months maturity lent to companies during the first quarter of FY11. Within the retail book, secured loans, such as auto and home loans, have shown growth. Higher secured lending also improves a bank's asset quality.

Profits were also boosted by the bank's other income, mainly due to a 22.5% YoY growth in fees and commissions and foreign exchange and derivative revenues of ₹216 crore (₹154 crore a year ago). Profits would have been higher but for a loss of ₹30 crore on the sale of investments.

HDFC Bank has maintained its net interest margin, or NIM, at 4.2% over the past three quarters. This is because almost half of its deposit base consists of low-cost current and savings account balances. This helps in restricting costs when interest rates rise.

The management has indicated that re-pricing of assets and liabilities will not have much of an impact on the bank's NIM. This is because 25% of its total deposit base is from fixed deposits that get re-priced every year. As against this, 80-85% of the loans in the corporate and retail books have a maturity of less than three years with majority of the corporate loans getting re-priced every year.

HDFC Bank's asset quality is one of the best in the industry. Net non-performing assets fell to a 11-quarter low of 0.2% of net advances for the quarter to December. Restructured assets formed only 0.3% of its total assets and have been at this level for four quarters. This also supports profit growth, as provisions will be lower. There are concerns over retail loan demand, which may slow down due to rising interest rate. In the retail loan book of ₹89,000 crore, auto loans are worth ₹24,000 crore. This segment is sensitive to interest rate changes.

Unlike its peers, the bank has maintained its NIM at over 4% for over 20 quarters. But, going forward, NIM may come under pressure due to rising interest rates, tempering of loan growth and higher pricing of deposits.

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