HDFC BANK
We understand your world

Board of Directors

Mr. Jagdish Capoor, *Chairman*
Mr. Aditya Puri, *Managing Director*
Mr. Keki Mistry
Mr. Vineet Jain
Mrs. Renu Karnad
Mr. Arvind Pande
Mr. Ashim Samanta
Mr. C. M. Vasudev
(Appointed as Additional Director w.e.f. 17.10.2006)
Mr. Gautam Divan
(Appointed as Additional Director w.e.f. 17.10.2006)
Mr. Bobby Parikh
(Resigned w.e.f. 17.10.2006)
Dr. Venkat Rao Gadwal
(Relinquished Office w.e.f. 14.3.2007)
Dr. Pandit Palande
(Appointed as Additional Director w.e.f. 24.04.2007)

Senior Management Team

Mr. A Parthasarthy
Mr. A. Rajan
Mr. Abhay Aima
Mr. Bharat Shah
Mr. C. N. Ram
Mr. G. Subramanian
Mr. Harish Engineer
Mr. Kaizad Bharucha
Mrs. Mandeep Maitra
Mr. Paresh Sukthankar
Mr. Pralay Mondal
Mr. Sudhir M. Joshi
Mr. Vinod G. Yennemadi

Executive Vice President (Legal) & Company Secretary

Mr. Sanjay Dongre

Auditors

M/s. Haribhakti & Co.,
Chartered Accountants

Registered Office

HDFC Bank House,
Senapati Bapat Marg,
Lower Parel,
Mumbai 400 013.
Tel: 5652 1000
Fax: 2496 0737
Website : www.hdfcbank.com

Registrars & Transfer Agents

Datamatics Financial Services Ltd
Plot No. A. 16 & 17,
Part B Crosslane, MIDC, Marol,
Andheri (East),
Mumbai 400093
Tel: 66712151-56
(Extn Nos. 207, 264 and 220)
Fax: 28213404;
E-mail: hdinvestors@dfssl.com

Financial Highlights

	1997-1998	1998-1999	1999-2000
Interest Income	240,80	376,08	679,87
Interest Expense	137,55	229,18	374,28
Net Interest Income	**103,25**	**146,90**	**305,59**
Other Income	6,1,05	67,13	119,54
Net Revenues	**164,30**	**214,03**	**425,13**
Operating costs	6,2,71	88,79	171,39
Operating Result	**101,59**	**125,24**	**253,74**
Provisions and Contingencies	7,24	8,39	58,89
Loan Loss Provisions	7,22	7,58	53,60
Amortisation on investments	-	-	-
Others	2	81	5,29
Profit before tax	**94,35**	**116,85**	**194,85**
Provision for taxation	31,20	34,45	74,81
Profit after tax	**63,15**	**82,40**	**120,04**
Funds :			
Deposits	2,191,74	2,915,11	8,427,72
Subordinated debt	100,00	135,00	150,00
Stockholders' Equity	285,13	338,93	751,52
Working Funds	2,829,98	4,349,96	11,731,03
Loans	841,98	1,400,56	3,462,34
Investments	1,121,33	1,903,80	5,748,28
Key Ratios :			
Earnings per share (Rs)	3.16	4.12	5.93
Return on Average Networth	23.87%	26.41%	29.00%
Tier 1 Capital Ratio	10.21%	8.34%	9.56%
Total Capital Ratio	13.92%	11.86%	12.19%
Dividend per share (Rs)	1.00	1.30	1.60
Dividend payout ratio	34.84%	34.71%	29.96%
Book value per share as at March 31 (Rs)	14.30	16.90	30.90
Market price per share as at March 31 (Rs)*	70.80	69.15	257.20
Price to Earnings Ratio	22.42	16.78	43.37

Rs. 10 Lac = Rs. 1 Million   Rs. 1 Crore = Rs. 10 Million   **Proposed   *Source : NSE

HDFC BANK
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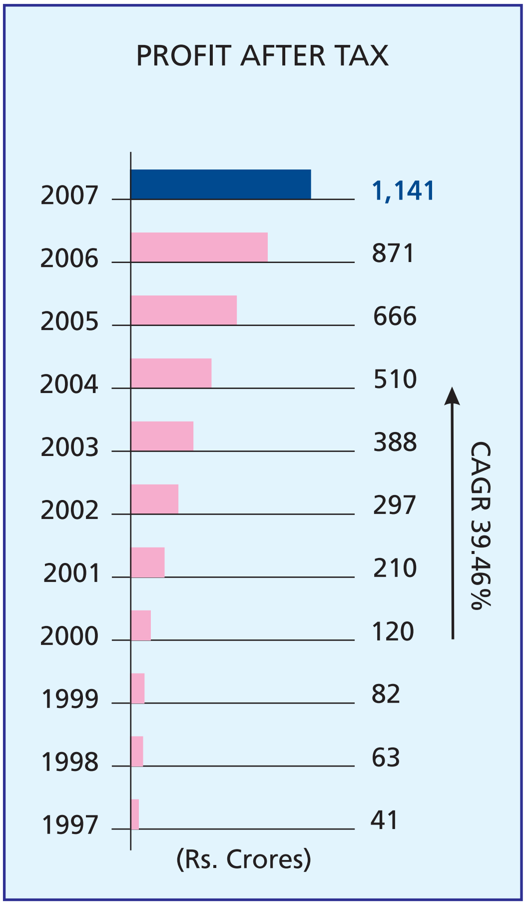
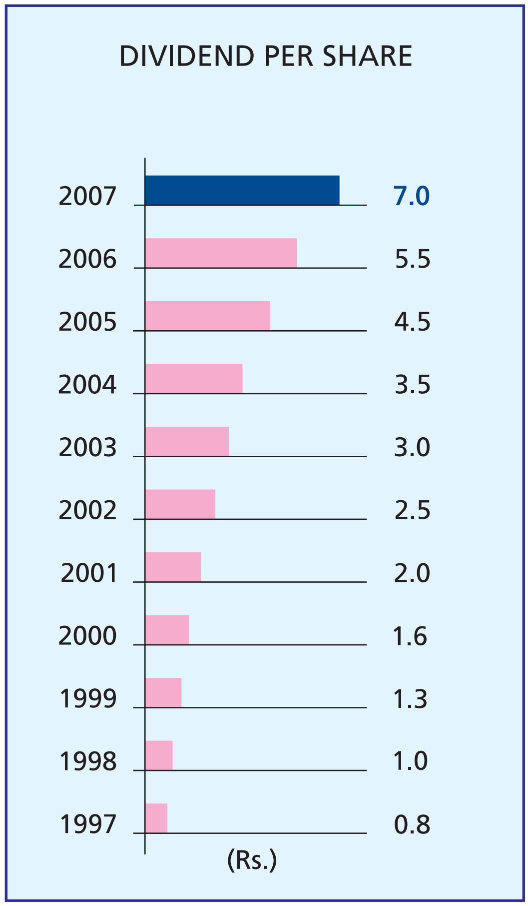
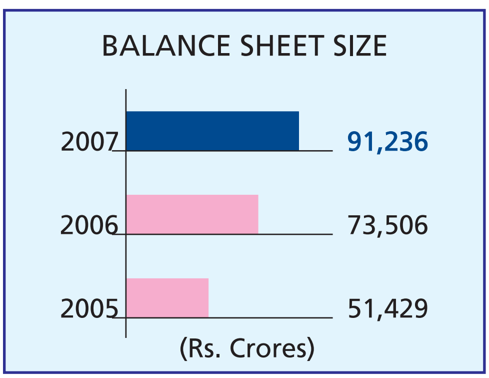
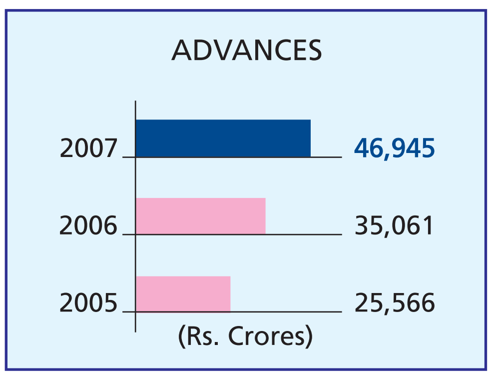
(Rs. lacs)

	2000-2001	2001-2002	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007
	1,259,46	1,702,99	2,013,61	2,548,93	3,093,49	4,475,34	6,889,02
	753,75	1,073,74	1,191,96	1,211,05	1,315,56	1,929,50	3,179,45
	505,71	**629,25**	**821,65**	**1,337,88**	**1,777,93**	**2,545,84**	**3,709,57**
	176,57	335,90	465,55	480,03	651,34	1,123,98	1,516,23
	682,28	**965,15**	**1,287,20**	**1,817,91**	**2,429,27**	**3,669,82**	**5,225,80**
	309,59	417,95	577,05	810,00	1,085,40	1,691,09	2,420,80
	372,69	**547,20**	**710,15**	**1,007,91**	**1,343,87**	**1,978,73**	**2,805,00**
	57,63	121,82	139,30	288,95	364,93	725,22	1,166,25
	52,96	85,77	88,39	178,28	176,22	479,76	861,01
	4,42	21,81	50,44	93,22	188,06	245,16	241,09
	25	14,24	47	17,45	65	30	64,15
	315,06	**425,38**	**570,85**	**718,96**	**978,94**	**1,253,51**	**1,638,75**
	104,94	128,34	183,25	209,46	313,38	382,73	497,30
	210,12	**297,04**	**387,60**	**509,50**	**665,56**	**870,78**	**1,141,45**
	11,658,11	17,653,81	22,376,07	30,408,86	36,354,25	55,796,82	68,297,94
	200,00	200,00	200,00	600,00	500,00	1,702,00	3,282,60
	913,09	1,942,28	2,244,83	2,691,88	4,519,85	5,299,53	6,433,15
	15,617,33	23,787,38	30,424,08	42,306,99	51,429,00	73,506,39	91,235,61
	4,636,66	6,813,72	11,754,86	17,744,51	25,566,30	35,061,26	46,944,78
	7,145,14	12,004,02	13,388,08	19,256,79	19,349,81	28,393,96	30,564,80
	8.64	11.01	13.75	17.95	22.92	27.92	36.29
	24.53%	18.30%	18.10%	20.14%	20.44%	17.47%	19.40%
	8.69%	10.81%	9.49%	8.03%	9.60%	8.55%	8.58%
	11.09%	13.93%	11.12%	11.66%	12.16%	11.41%	13.08%
	2.00	2.50	3.00	3.50	4.50	5.50	7.00**
	25.55%	23.68%	24.72%	22.15%	24.00%	22.55%	22.92%
	37.50	69.00	79.60	94.52	145.86	169.24	201.42
	228.35	236.60	234.55	378.75	573.64	774.25	954.15
	26.43	21.50	17.06	21.10	25.03	27.74	26.29

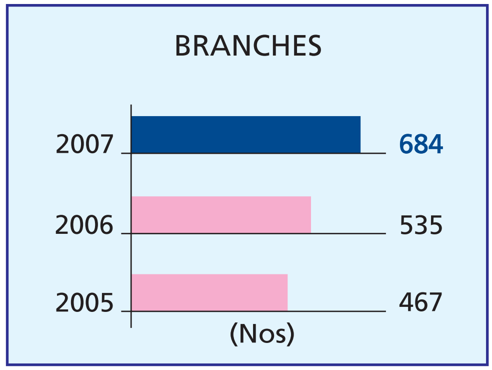

PROFIT AFTER TAX
2007
1,141
2006
871
2005
666
2004
510
2003
388
2002
297
2001
210
2000
120
1999
82
1998
63
1997
41
CAGR 39.46%
(Rs. Crores)

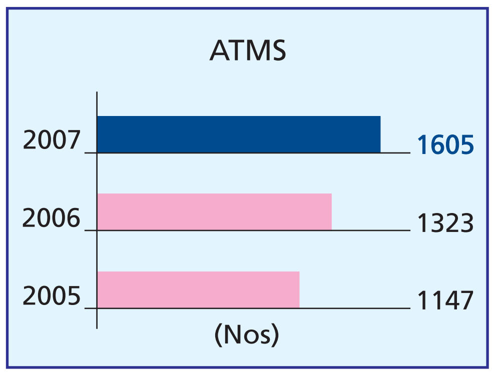

DIVIDEND PER SHARE
2007
7.0
2006
5.5
2005
4.5
2004
3.5
2003
3.0
2002
2.5
2001
2.0
2000
1.6
1999
1.3
1998
1.0
1997
0.8
(Rs.)

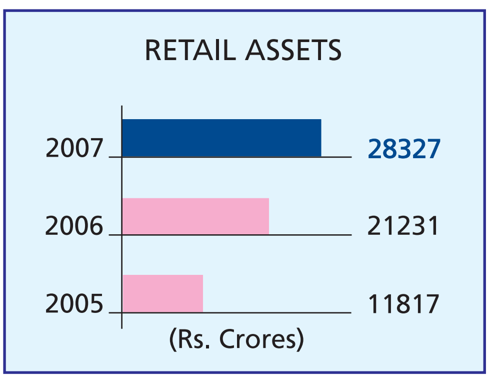

BALANCE SHEET SIZE
2007
91,236
2006
73,506
2005
51,429
(Rs. Crores)

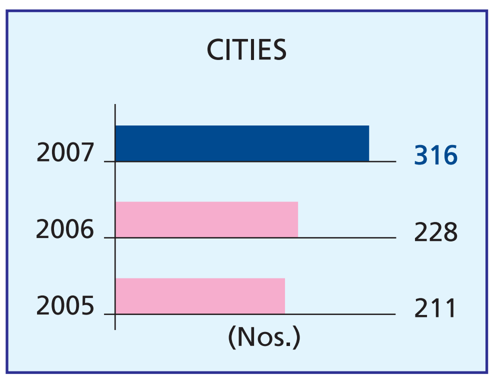

ADVANCES
2007
46,945
2006
35,061
2005
25,566
(Rs. Crores)

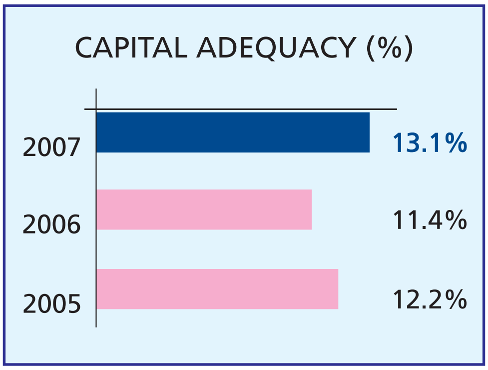

EARNING PER SHARE
2007
36.29
2006
27.92
2005
22.92
2004
17.95
2003
13.75
2002
11.01
2001
8.64
2000
5.93
1999
4.12
1998
3.16
1997
2.03
(Rs.)

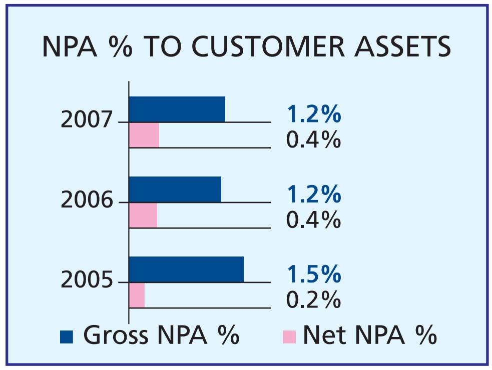

BRANCHES
2007
684
2006
535
2005
467
(Nos)

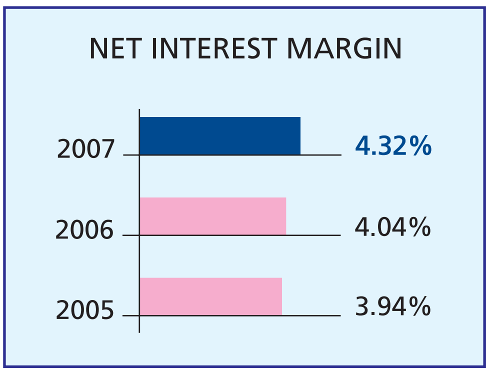

ATMS
2007
1605
2006
1323
2005
1147
(Nos)

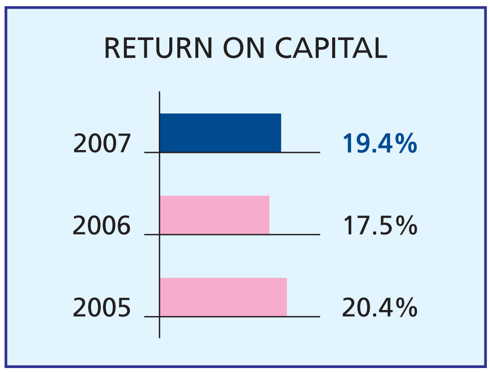

RETAIL ASSETS
2007
28327
2006
21231
2005
11817
(Rs. Crores)

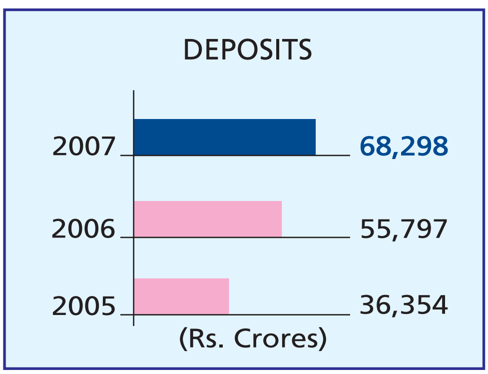

CITIES
2007
316
2006
228
2005
211
(Nos.)

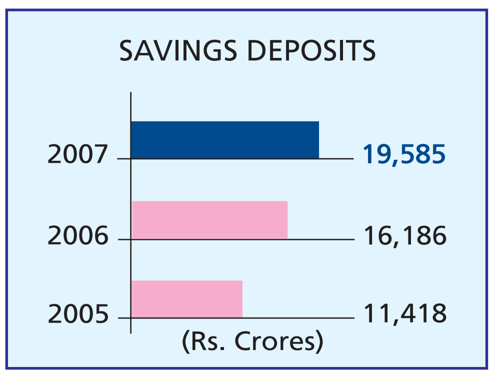

CAPITAL ADEQUACY (%)
2007
13.1%
2006
11.4%
2005
12.2%

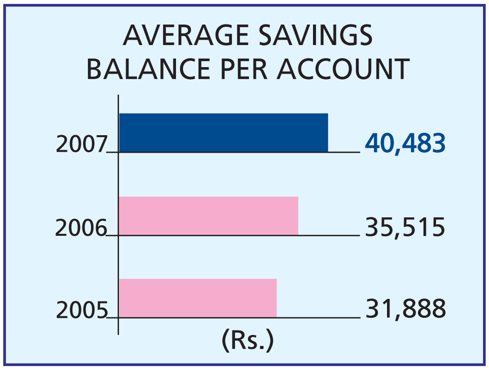

NPA % TO CUSTOMER ASSETS
2007
1.2%
0.4%
2006
1.2%
0.4%
2005
1.5%
0.2%
Gross NPA %
Net NPA %

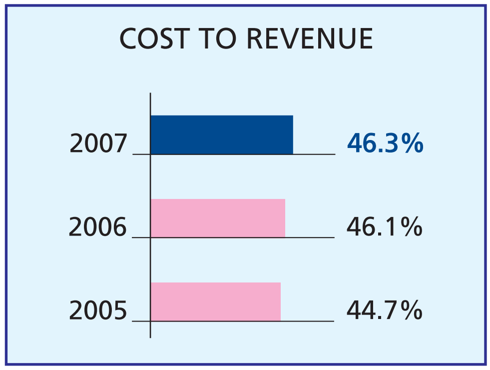

NET INTEREST MARGIN
2007
4.32%
2006
4.04%
2005
3.94%

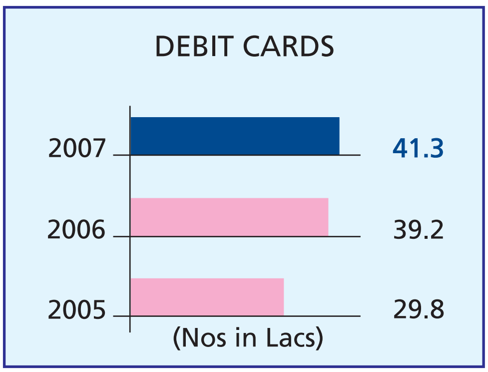

RETURN ON CAPITAL
2007
19.4%
2006
17.5%
2005
20.4%

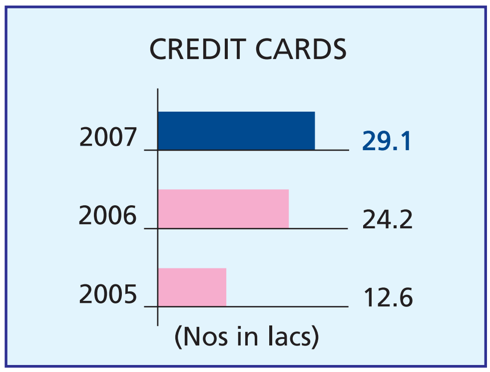

DEPOSITS
2007
68,298
2006
55,797
2005
36,354
(Rs. Crores)


SAVINGS DEPOSITS
2007
19,585
2006
16,186
2005
11,418
(Rs. Crores)

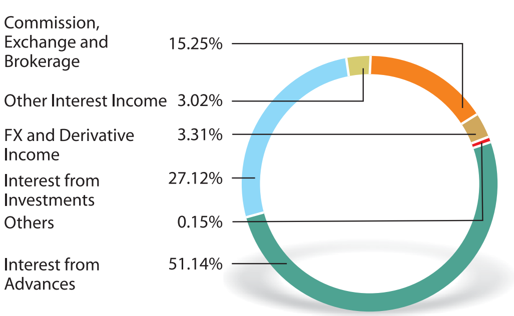




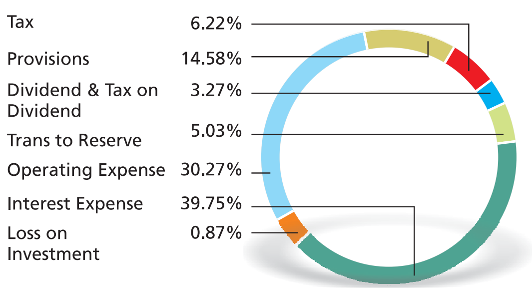




RUPEE EARNED



RUPEE SPENT



Directors' Report

To the Members,

Your Directors have great pleasure in presenting the Thirteenth Annual Report on the business and operations of your Bank together with the audited accounts for the year ended March 31, 2007.

FINANCIAL PERFORMANCE

(Rs. in crores)
For the year ended

	March 31, 2007	March 31, 2006
Deposits and other borrowings	71,113.3	58,655.3
Advances	46,944.8	35,061.3
Total income	8,405.3	5,599.3
Profit before depreciation and tax	1,858.4	1,432.1
Net profit	1,141.5	870.8
Profit brought forward	1,455.0	602.3
Transfer from Investment Fluctuation Reserve	-	484.2
Total profit available for appropriation	2,596.5	1,957.3
Appropriations:		
Transfer to statutory reserve	285.4	217.7
Transfer to general reserve	114.1	87.1
Transfer to capital reserve	0.0	1.1
Transfer to investment reserve account	3.0	-
Proposed dividend	223.6	172.2
Tax including surcharge and education cess on dividend	38.0	24.2
Dividend paid for prior year	0.4	-
Balance carried over to Balance Sheet	1,932.0	1,455.0

The Bank posted total income and net profit of Rs. 8,405.3 crores and Rs. 1,141.5 crores respectively for the financial year 2006-07 as against Rs. 5,599.3 crores and Rs. 870.8 crores respectively in the previous year. Appropriations from the net profit have been effected as per the table given above.

Dividend

Your Bank has had a track record of moderate but steady increases in dividend declarations for the last 10 years and the dividend payout ratio in the last few years has been in the range of

20-25%. Your Bank's dividend policy is based on the need to balance the twin objectives of appropriately rewarding shareholders with cash dividends and of retaining capital to maintain a healthy capital adequacy ratio to support future growth. In line with this policy and in recognition of the healthy performance during 2006-07, your directors are pleased to recommend a dividend of 70% for the year ended March 31, 2007 as against 55% for the year ended March 31, 2006. This dividend shall be subject to dividend distribution tax to be paid by the Bank but will be tax-free in the hands of the members.

Awards

Your Bank continued to receive awards and gain recognition from various leading domestic and international publications during the fiscal 2006-07. The Bank was selected as the"Best Bank in India" by the Business Today magazine for the fourth consecutive year. Forbes magazine named the Bank as 'One of Asia Pacific's Best 50 companies'. The Bank was named as the 'Best Listed Bank of India' by the Businessworld magazine. The Bank was selected as the 'Best Domestic Bank' at The Asset Magazine's Triple A Country Awards. The Bank was named as the 'Best Local Cash Management Bank in Large and Medium Segments' at the Asiamoney Awards and as the 'Best Bank in India' at the Euromoney awards. The Bank was also named as one of the best companies in terms of corporate governance in India by the The Asset magazine. The Managing Director of your Bank, Mr Aditya Puri, was awarded the Asian Banker Leadership Achievement Award 2006 for India.

Ratings

The Bank has its deposit programs rated by two rating agencies - Credit Analysis & Research Limited (CARE) and Fitch Ratings India Private Limited. The Bank's Fixed Deposit programme has been rated 'CARE AAA (FD)' [Triple A] by CARE, which represents instruments considered to be "of the best quality, carrying negligible investment risk". CARE has also rated the bank's Certificate of Deposit (CD) programme "PR 1+" which represents "superior capacity for repayment of short term promissory obligations". Fitch Ratings India Pvt. Ltd. (100% subsidiary of Fitch Inc.) has assigned the "tAAA (ind)" rating to the Bank's deposit programme, with the outlook on the rating as "stable". This rating indicates "highest credit quality" where "protection factors are very high".

The Bank also has its long term unsecured, subordinated (Tier II) Bonds rated by CARE and Fitch Ratings India Private Limited and its Tier I perpetual Bonds and Upper Tier II Bonds rated by CARE and CRISIL Ltd. CARE has assigned the rating of "CARE AAA" for the subordinated Tier II Bonds while Fitch Ratings India Pvt. Ltd. has assigned the rating "AAA (ind)" with the outlook on the rating as "stable". CARE has also assigned "CARE AAA [Triple A] for the Banks Perpetual bond and Upper Tier II bond issues. CRISIL has assigned the rating "AAA / Stable" for the Bank's Perpetual Debt programme and Upper Tier II Bond issue. In each of the cases referred to above, the ratings awarded were the highest assigned by the rating agency for those instruments.

Additional Capital

During the year under review, 62.5 lac shares were allotted to the employees of the Bank pursuant to the exercise of options under the Employee Stock Option Scheme of the Bank.

The Bank raised Rs. 635.90 crores during the year at an annualized coupon ranging between 8.80% to 9.20% p.a. and also raised foreign currency borrowing of USD 100 million at an annualized coupon rate of 6-month LIBOR plus 120 bps as Upper Tier II capital. The bank raised Rs. 410 crores as Lower Tier II capital at an annualized coupon ranging between 8.45% to 9.10% p.a. The debts are subordinated to present and future senior indebtedness of the Bank and qualifies as Tier II capital under RBI's guidelines for assessing capital adequacy. The Bank also raised Rs.200 crores as unsecured non-convertible subordinated perpetual bonds in the nature of debentures for inclusion as Tier I capital at an annualized coupon 9.92% p.a. payable semi-annually.

The Bank has grown rapidly over the last several years. Given the market opportunity in light of continued economic growth and the Bank's strong positioning in each of its major franchises, it is important that your Bank has adequate capital to support its growth plans. Further, incremental capital would also facilitate meeting the changing regulatory requirements such as the proposed capital adequacy framework (based on Basel II Accord) and the new capital market exposure norms. Your Bank thus proposes to raise additional equity capital equivalent to US$ 1 billion (approximately Rs 4200 crores).

The above proposed equity issue will result in the reduction of the present shareholding of the promoter viz HDFC Group which is currently at 21.56%. With a view to maintain the shareholding of the promoter group at around 23% of the enhanced capital base, it is proposed to offer 1,35,82,000 equity shares of Rs. 10 each at an issue price to be determined in accordance with a specified formula in respect of each share, as per SEBI (Disclosure and Investor Protection) Guidelines, 2000. The balance amount of the proposed equity capital may be raised either as domestic public offering or an international offering.

Employee Stock Options

The information pertaining to Employee Stock Options is given in an annexure to this report.

Capital Adequacy Ratio

As of March 31, 2007 your Bank's total Capital Adequacy Ratio (CAR) stood at 13.1%, well above the regulatory minimum of 9.0%. Of this, Tier I CAR was 8.6%.

SUBSIDIARY COMPANY

In terms of the approval granted by the Government of India, the provisions contained under Section 212(1) of the Companies Act, 1956 shall not apply in respect of the Bank's subsidiary namely, HDFC Securities Limited (HSL). Accordingly, a copy of the balance sheet, profit and loss account, report of the Board of Directors and Report of the Auditors of HSL have not been attached to the accounts of the Bank for the year ended March 31, 2007.

The Annual Report of the Bank, the annual accounts and the related documents of HSL are posted on the website of the Bank, www.hdfcbank.com. Investors who wish to have a copy of the annual accounts and detailed information on HSL may download the same from the website or alternatively write to the Bank for the same. Further, the said documents shall be available for inspection by the investors at the registered office of the Bank and HSL.

MANAGEMENT'S DISCUSSIONS AND ANALYSIS

Macro-economic and Industry Developments

The average growth rate of the Indian economy over a period of 25 years since 1980-81 (financial year beginning April) has been about 6.0% p.a., with the growth rate averaging 9.1% p.a. during the last two years.

The strengthening of economic activity in the recent years has been supported by a persistent increase in the domestic investment rate from 22.9% of GDP in 2001-02 to 33.8% in 2005-06 coupled with more efficient use of capital. Domestic saving rate improved from 23.5% to 32.4% of GDP during the same period. The services sector continues to be the driver of growth with a share of around 60% in the overall GDP and contributing almost three-fourth to overall growth. The manufacturing sector has shown good growth supported by domestic as well export demand. The Real GDP Growth for 2006-07 is expected to be 8.5-9.0%.

India's merchandise exports recorded a growth rate of 22% during April-December 2006 as compared with 22.9% in the corresponding period of 2005. Imports rose by 24.8% as compared with 37.8% a year ago. While petroleum, oil and lubricants imports rose by 39.2% during April-December 2006 as compared to 46.9% a year ago, non-oil imports showed a lower growth of 18.7% from as against a growth of 34.3% in the previous financial year.

Exports have been growing at an average rate of around 25% during the last three years. Sustained growth in export of services and remittances continued to provide buoyancy to the surplus in the invisible account which enabled financing a large part of trade deficit. There was a significant strengthening in the capital account with the foreign exchange reserves crossing US $ 200 billion, The reserves currently exceed the country's external debt of about US $ 140 billion as on September 2006.

During 2006-07, non-food credit expanded by 31.2% compared to 25.2% a year ago. The Y-o-Y growth in aggregate deposits at 22.5% was higher than that of 17.2% a year ago and was also the highest since 1993-94 on a comparable basis. Bank deposit rates increased by 100 - 300 basis points during the year across various maturities on account of tighter liquidity conditions coupled with high credit growth.

The financial year 2006-2007 started with the banking system remaining surplus in liquidity till mid of December 2006. However, thereafter due to the tightening of monetary policy by way of increase in CRR and advance tax outflows, the banking system remained net borrowers of funds from RBI for most part of the January - March 07 quarter. Tight liquidity coupled with high credit growth led to an increase in rates offered on deposits by the banks. During the financial year, the benchmark reverse repo rate was revised upwards by 50 basis points to 6.00% presently. Similarly the repo rate was revised upwards by 125 basis points to 7.75%. The Cash Reserve Ratio was also increased from 5% to 6% during the financial year 2006-07.

The one year Government Securities (G Sec) yields which reflects the liquidity condition in the economy climbed from 6.54% in March 2006 to 7.31% in March 2007, an increase of approximately 77 basis points through the year. The 10 year G Sec yield showed a smaller year-on-year movement of 42 basis points to 7.94% at the end of the year.

The capital markets remained buoyant in the last fiscal with the stock indices touching their all time highs in the recent months. During 2006-07, the Assets Under Management (AUM) of mutual funds have grown by Rs. 95,283 crores, an increase of 41.2% over the previous year's AUM.

(Sources: Ministry of Finance, RBI, CSO)

Mission and Business Strategy

Our mission is to be "a World Class Indian Bank", benchmarking ourselves against international standards and best practices in terms of product offerings, technology, service levels, risk management and audit & compliance. The objective is to build sound customer franchises across distinct businesses so as to be a preferred provider of banking services for target retail and wholesale customer segments, and to achieve a healthy growth in profitability, consistent with the Bank's risk appetite. We are committed to do this while ensuring the highest levels of ethical standards, professional integrity, corporate governance and regulatory compliance.

Our business strategy emphasizes the following:

- Increase our market share in India's expanding banking and financial services industry by following a disciplined growth strategy focusing on balancing quality and volume growth while delivering high quality customer service;
- Leverage our technology platform and open scaleable systems to deliver more products to more customers and to control operating costs;
- Maintain high standards for asset quality through disciplined credit risk management;
- Develop innovative products and services that attract our targeted customers and address inefficiencies in the Indian financial sector;
- Continue to develop products and services that reduce our cost of funds; and
- Focus on healthy earnings growth with low volatility.

Financial Performance:

The financial performance during the fiscal year 2006-07 remained healthy with total net revenues (net interest income plus other income) increasing by 42.4% to Rs. 5225.8 crores from Rs.3669.8 crores in 2005-06. The revenue growth was driven principally by an increase in net interest income. Net interest income grew by 45.7% primarily due to an increase in the average balance sheet size by 36.6% and an increase in net interest margin from 4.0% to 4.3%. The increase in net interest margin was due to better mix of deposits with a higher proportion of current accounts (arising out of an increase in our transaction banking business) and an increase in lending rates which was only partially offset by higher costs of deposits and costs of borrowings. The Bank increased its Benchmark Prime Lending Rate (BPLR) thrice during the year as a result of increase in interest rates in the banking system due to tight liquidity conditions. Average cost of time (fixed) deposits increased by over 100 basis points on a year-on-year basis.

The other income (non-interest revenue) increased by 34.9% to Rs. 1516.2 crores primarily due to fees and commissions and income from foreign exchange and derivatives. In 2006-07, commission income increased by 23.7% to Rs. 1292.4 crores with the main drivers being commission from distribution of third party mutual funds and insurance, fees on debit/credit cards and transactional charges/fees. The Bank incurred net losses on sale /revaluation of investments of Rs. 68.4 crores (primarily on non-SLR investments) as a result of the sharp increase in short term yields in the debt markets in March 2007. A large portion of the non-SLR investments were bonds in which the Bank had invested in previous years for meeting priority sector lending requirements. Foreign exchange and derivatives revenues grew from Rs. 118.6 crores to Rs. 280.3 crores which largely related to higher customer transaction volumes.

Operating (non-interest) expenses increased from Rs.1691.1 crores in 2005-06 to Rs. 2420.8 crores in 2006-07, due to significant expansion in new branch infrastructure, retail loan products and the credit card business. The ratio of operating cost to net revenues however, remained more or less stable at 46.3% as against 46.1% in the corresponding year. Staff expenses accounted for 32.1% of non-interest expenses in 2006-07 as against 28.8% in 2005-06, due to an increase in staff strength from 14878 to 21477 and also due to increase in salary levels. Specific loan loss provisions for NPAs and general provisions for standard assets increased from Rs.479.8 crores to Rs. 861.0 crores in 2006-07. In May 2006 and January 2007 the Reserve Bank of India increased the general provision requirement for certain standard assets such as personal loans, credit card receivables, capital market exposures and real estate exposures resulting in an extraordinary one-time general provision of Rs 158 crores for 2006-07. Provision for amortisation of investments was Rs. 241.09 crores, principally due to the amortisation of the premium of SLR investments in the 'Held to Maturity' category.

Net profit increased by 31.1% from Rs. 870.8 crores in 2005-06 to Rs. 1141.5 crores in 2006-07. Return on average net worth was higher at 19.4% from the previous year figure of 17.5%. The Bank's basic earning per share increased from Rs. 27.92 to Rs. 36.29 per equity share. The diluted earnings was Rs.26.33 per equity share in 2005-06 and for the current year is Rs. 36.06.

During 2006-07, the Bank's total balance sheet size increased by 24.1% to Rs. 91236 crores. Total Deposits increased from Rs. 55797 crores (as of March 31, 2006) to Rs. 68298 crores (as of March 31, 2007) with savings account deposits at Rs. 19585 crores and current account deposits at Rs. 19812 crores. In the January to March 2007 quarter time (fixed) deposit rates in the banking system increased sharply to levels which the Bank considered unattractive and unsustainable. The Bank, therefore, allowed some of its wholesale deposits to run-off, without affecting its liquidity position. As a result, demand (CASA) deposits were around 57.7% of total deposits as of March 31, 2007. During 2006-07, gross advances grew by 29.6 % to Rs. 49780 crores. This was driven by a growth of 33.4% in retail advances to Rs. 28327 crores, and an increase of 24.9% in wholesale advances to Rs. 21452 crores.

Business Segment Update:

The bank has been able to achieve healthy growth across various operating and financial parameters. This performance reflects the strength and diversity of the bank's three primary business franchises – retail banking, wholesale banking and treasury, as well as a disciplined approach to risk-reward management.

The retail banking business continued its growth in 2006-07. In this business, the Bank has positioned itself as a one-stop-shop financial services provider, catering primarily to the middle class, mass affluent and high networth segments. The Bank's range of retail financial products and services is fairly exhaustive including various deposit products, loans, credit cards, debit cards, depository (custody) services, investment advice, bill payments and various transactional services. Apart from its own products, the Bank sells third party financial products like mutual funds and insurance to its retail customers. To provide its customers greater flexibility and convenience as well as to reduce servicing costs, the Bank has invested in multiple channels – branches, ATMs, phone banking, internet banking and mobile banking. The success of the Bank's multi-channel strategy is evidenced in the fact that almost 78% of customer initiated transactions are serviced through non-branch channels. The Bank's data warehouse and Customer Relationship Management (CRM) solutions have helped it to target its customers more effectively and offer appropriate products depending on customer profiles, thus reducing costs of acquisition and deepening customer relationships.

The Bank's total customer base increased from 96.0 lacs in March 2006 to 100.1 lacs in March 2007. On receiving regulatory approvals in the third quarter of the financial year, the Bank could resume its branch expansion efforts and opened 149 branches by March 2007. The distribution network was thus expanded with the number of branches increasing from 535 (in 228 cities) in March 2006 to 684 (in 316 cities) in March 2007 and the number of ATMs from 1323 to 1605 over the same period. The Bank's focus on semi-urban and under-banked markets continued, with about 62% of the Bank's branches now outside the top nine cities. Savings account deposits, which reflect the strength of the retail liability franchise, grew by 21% to Rs.19585 crores in 2006-07. The retail gross loan portfolio increased from Rs. 21231 crores as of March 31, 2006 to Rs. 28327 crores as of March 31, 2007, an increase of 33.4%. The Bank also extends almost half of its retail loans in non-metro markets (outside top nine cities).

The Bank's credit card business strategy in 2006-07 was to focus on quality customer acquisitions and improve processes to reduce cycle times and bring in cost efficiencies. The total number of cards in force has crossed the 2.9 million mark. The Bank has a significant presence in the "merchant acquiring" business with the total number of point-of-sale (POS) terminals installed by the Bank at over 51000. The Bank's third party distribution business continued to be a key revenue earner with income from sales of mutual funds and life insurance policies contributing over 18% of retail fees and commission. On the Bank's housing loan business, the origination of the HDFC home loan product increased to around Rs. 450 crores per month.

The wholesale banking business too registered a healthy growth in 2006-07. In this business, the Bank provides its corporate and institutional clients a wide range of commercial and transactional banking products, backed by high quality service and relationship management. The Bank's commercial banking business covers not only the top end of the corporate sector but also the growing Emerging Corporate and Small and Medium Enterprise (SME) segments. The Bank now has four business groups catering to various SME customers extending a wide range of banking services including working captial and term finance, cash management services, foreign exchange products and electronic banking.

During the financial year 2006-07, growth in the wholesale banking business continued to be driven by new customer acquisition and higher cross sell with a focus on optimising yields and increasing product penetration. The Bank's cash management and vendor & distributor finance products continued to be an important contributor to growth in the corporate banking business. The Bank further consolidated its position as a leading player in the cash management business (covering all outstation collection, disbursement and electronic fund transfer products across the Bank's various customer segments) with volumes growing from about Rs.1000000 crores in FY 2005-06 to over Rs.1300000 crores in FY 2006-07. The Bank also strengthened its market leadership in cash settlement services for major stock exchanges and commodity exchanges in the country. The Bank's capital market exposure has been within the regulatory limits and the current account floats from this business showed moderate growth. Yet again, the Bank met the overall priority sector lending requirement of 40% of net bank credit.

The Bank also achieved healthy growth in its agriculture and micro finance portfolios. With products including the Kisan Gold Card, rural supply chain initiatives and commodity finance covering the entire agriculture financing cycle, the Bank's direct agriculture lending increased by over 40% during the year. The Bank has targeted potential outreach locations within a certain radius of its semi-urban and rural branches, distributing a set of products that includes savings accounts, fixed deposits, two wheeler and auto loans, kisan card loans , tractor loans and warehouse receipt loans. The Bank has also rolled out special rural fixed deposit and savings account products. The Bank also has specialised Agri Desks at certain branches across the country which work as single point contacts for farmers.

The Bank has relationships with over 70 micro finance institutions and has provided financing where the ultimate beneficiaries exceed 600000 households. The Bank has successfully commenced direct lending to Self Help Groups (SHG). The Bank opened a dedicated branch for lending to SHGs, in Thudiyalur village (Tamil Nadu). With this successful pilot, the Bank plans to open more such branches which are also involved in promoting financial literacy in the rural and tribal areas.

The treasury group manages the Bank's balance sheet and is responsible for compliance with reserve requirements and management of market and liquidity risk. On the foreign exchange and derivatives front, the revenues are driven primarily by spreads on customer transactions based on their trade flows and hedging needs. In addition, the treasury group seeks to optimise profits from proprietary trading within established limits. During 2006-07, revenues from foreign exchange and derivative transactions grew by 136.3% to Rs 280 crores with the revenue streams well diversified across large corporate, retail and SME segments. Given the regulatory requirement of holding government securities to meet the statutory liquidity ratio (SLR) requirement, the Bank has to necessarily maintain a large portfolio of government securities. This enables the Bank to realise gains in a declining interest rate environment but exposes the Bank to losses or depreciation in value of investments when bond yields rise. To reduce this volatility as of March 2007, around 85% of the SLR book was held in the 'Held to Maturity' (HTM) category. The SLR securities now in the 'Available for Sale' (AFS) category are primarily floating rate bonds where the interest rate risk is low. The Bank, therefore remains exposed to market risk primarily on the non-SLR investment portfolio in the AFS category as the regulations do not allow new non-SLR investments to be classified in the HTM category.

Service Quality Initiatives

In January 2006, the Bank had launched a new Quality Initiative – Lean Sigma Project Management. Through this initiative more than 500 projects have been executed to reduce transaction turnaround times and improve business cycle efficiencies.

The Service Quality Initiative was upgraded during the year to measure and improve the customer service experience across all touch points. The Bank plans to re-engineer key processes in the coming year using technology, Six Sigma and Five S (a technique used for workplace transformation) to further improve customer experience.

Risk Management & Portfolio Quality

The Bank's risk philosophy involves developing and maintaining a healthy porfolio within its risk appetite and the regulatory framework. While the Bank is exposed to various types of risks, the most important among them are credit risk, market risk (which includes liquidity risk and price risk) and operational risk. The measurement, monitoring and management of risks remains a key focus areas for the Bank. For credit risk, distinct policies and processes are in place, separately for wholesale and retail credit exposures. For wholesale credits, management of credit risk is carried out through target market definition, portfolio diversification, appraisal and approval processes, post sanction monitoring and remedial management procedures. In the retail asset businesses, the credit cycle is managed through credit policy definition, appropriate front-end credit buying, operations, fraud control and collection processes. For each product, programs defining customer segments, underwriting standards, security structures, etc are specified to ensure consistency of credit buying patterns. Given the granularity of individual exposures, retail credit risk is managed largely on a portfolio basis, across various products and customer segments.

The Risk Monitoring Committee of the Board monitors the Bank's risk management policies and procedures, vets treasury risk limits before they are considered by the Board, and reviews portfolio composition and impaired credits. From an industry concentration perspective (excluding the retail loan portfolio), as of March 31, 2007, the following table gives industry wise classification of the Loans and Investments outstanding (excluding SLR investments, equity shares and mutual funds).

	(Rs. Crores) Funded exposure	% to total exposure
Transportation	6187	10.74%
Banks and Financial Institutions	3175	5.51%
Trade	2606	4.52%
Automobiles and Auto Ancillaries	2573	4.47%
Other Financial Intermediaries	1657	2.88%
Food Processing	1342	2.33%
Engineering	1235	2.14%
Fertilisers and Pesticides	1216	2.11%
Other industries < 2% each of Loans and Investments outstanding (38 sectors))	12210	21.20%
Retail – Except where otherwise classified	25399	44.10%
Total	57600	100.00%

As of March 31, 2007, the Bank's ratio of gross non-performing assets (NPAs) to total customer assets was 1.2%, about the same as of March 31, 2006. Increases in NPAs during the year were mainly related to delinquencies in various retail loan products. These delinquencies and NPAs remained largely within the product parameters for various retail asset products. Net non-performing assets (gross non-performing assets less specific loan loss provisions, interest in suspense and ECGC claims received) were 0.4% of customer assets as of March 31, 2007, again about the same level as last year. The specific loan loss provisions that the Bank has made for its non performing assets continue to be more conservative than the regulatory requirement. In May 2006 and January 2007, the Reserve Bank of India increased the general provision requirements for certain standard assets such as personal loans, credit card receivables, capital market exposures and real estate exposures, resulting in a one-time general provision of Rs.158 crores during the year.

The Basel Committee on Banking Supervision (BCBS) released the International Convergence of Capital Measurement & Capital Standards in June 2004, providing the new framework for Capital Adequacy (Basel II). Pursuant to this Accord, Reserve Bank of India came out with its draft guidelines for implementation of the New Capital Adequacy Framework in February 2005, following it up with the revised final guidelines in March 2007 and final guidelines in April 2007. In terms of the guidelines of Reserve Bank of India, Indian banks having operational presence outside India will have to migrate to the selected approaches (Standardised Approach for credit risk and Basic Indicator Approach for operational risk) with effect from March 31, 2008. All other scheduled commercial banks are required to migrate to these approaches no later than March 31, 2009. The Bank views the implementation of the Basel II framework as synchronous with its objective of adopting international best practices in risk management. The Bank has assessed the key requirements of the New Framework as released by BCBS and as they evolve under the Reserve Bank of India guidelines. Based on this assessment, the Bank has progressed on various initiatives to enhance its risk management systems in terms of architecture, capabilities, technology, etc., in areas such as ratings systems, borrower segmentation, exposure consolidation, risk mapping, risk estimation, capital computation, etc. While the Bank, to start with, will migrate to the above approaches defined in the Reserve Bank of India guidelines, the initiatives undertaken are geared towards enabling the Bank comply with the standards set out for the more advanced capital measurement approaches in the BCBS accord.

INTERNAL AUDIT & COMPLIANCE

The Bank has an Internal Audit & Compliance department, which is responsible for independently evaluating the adequacy of all internal controls and ensuring operating and business units adhere to internal processes and procedures as well as to regulatory and legal requirements. The department also pro-actively recommends improvements in operational processes and service quality. To ensure independence, the Audit & Compliance department has a reporting line to the Chairman of the Board of Directors and the Audit & Compliance Committee of the Board and only indirectly to the Managing Director. To mitigate operational risks, the Bank has put in place extensive internal controls including restricted access to the Bank's computer systems, appropriate segregation of front and back office operations and strong audit trails. The Audit & Compliance Committee of the Board also reviews the performance of the Audit & Compliance department and reviews the effectiveness of controls and compliance with regulatory guidelines.

During the year, Securities and Exchange Board of India (SEBI) in the course of its investigations into the irregularities identified in regard to the applications tendered for the IPO offerings made by companies during the period 2003-05, observed that several Depository Participants (DPs) including HDFC Bank Ltd. prima facie, had appeared to have grossly failed in adhering to the Know Your Client norms as laid down by SEBI and thereby facilitated opening of demat accounts in ficticious / benami names. Consequently, SEBI passed an ex- parte interim order directing certain DPs not to open fresh demat accounts till further directions, and initiated enquiry proceedings. Simultaneously, SEBI also passed an order for disgorgement amounting to Rs. 1.64 crores. The Bank in its response to the ex-parte order submitted that the prescribed Know Your Client norms were followed by the Bank and that the Bank had obtained all the prescribed documentation as prescribed by SEBI at the relevant points of time. The Bank, has been allowed to open fresh demat accounts since November 2006. The Bank has also submitted its response to the Enquiry Notice and is awaiting the response from SEBI. The Bank preferred an appeal against the disgorgement order with the Securities Appellate Tribunal. The Securities Appellate Tribunal has passed an interim order staying the operations of the disgorgement order.

SOCIAL INITIATIVES

Pursuing a vision towards the socio-economic empowerment of underprivileged and marginalised sections of society the Bank supports social initiatives with special focus on education and livelihood support. This supplements the Bank's support and lending to self-help groups as part of its Microfinance activities.

In addition to the continued support to the 'ensuring children learn' and the 'girl child' projects, the bank has assisted in setting up a learning resource center 'LRC' at a shelter home for street boys. The LRC houses a bank of materials, books, teaching and learning aids and aims to help expand the skill sets of underprivileged students.

The Bank supports a day care center for the children of construction laborers. The center offers a comprehensive day care program which facilitates the holistic development and education of the children through its crèche, kindergarten and non-formal/ "bridge" schools. The bank also supports a program, which reaches out to the developmentally challenged to equip them with skills so as to enable them to lead a a self reliant and productive life. The program offers a vocational course that taps and fosters their skills in various fields such as art and crafts, catering and hospitality services, office skills etc.

HUMAN RESOURCES

The Bank's staffing needs continued to increase during the year particularly in the retail banking businesses in line with the business growth. Total number of employees increased from 14878 as of March 31, 2006 to 21477 as of March 31, 2007. The Bank continues to focus on training its employees on a continuing basis, both on the job and through training programs conducted by internal and external faculty. The Bank has consistently believed that broader employee ownership of its shares has a positive impact on its performance and employee motivation. The Bank's employee stock option scheme so far covers around 9000 employees.

STATUTORY DISCLOSURES

The information required under Section 217(2A) of the Companies Act, 1956 and the rules made there under, are given in the annexure appended hereto and forms part of this report. In terms of section 219(1)(iv) of the Act, the Report and Accounts are being sent to the shareholders excluding the aforesaid annexure. Any shareholder interested in obtaining a copy of the said annexure may write to the Company Secretary at the Registered Office of the Bank. The Bank had 21477 employees as on March 31, 2007. One hundred seventy one employees employed throughout the year were in receipt of remuneration of Rs. 24.0 lacs per annum and twenty three employees employed for part of the year were in receipt of remuneration of more than Rs. 2.0 lacs per month.

The provisions of Section 217(1)(e) of the Act relating to conservation of energy and technology absorption do not apply to your Bank. The Bank has, however, used information technology extensively in its operations.

The report on the Corporate Governance is annexed herewith and forms part of this report.

RESPONSIBILITY STATEMENT

The Board of Directors hereby state that

i) in the preparation of the annual accounts, the applicable accounting standards have been followed along with proper explanation relating to material departures;

ii) we have selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the Bank as on March 31, 2007 and of the profit of the Bank for the year ended on that date;

iii) we have taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of the Companies Act, 1956 for safeguarding the assets of the Bank and for preventing and detecting the fraud and other irregularities;

iv) we have prepared the annual accounts on a going concern basis.

DIRECTORS

Mr. Arvind Pande and Mr. Ashim Samanta will retire by rotation at the ensuing Annual General Meeting and are eligible for re-appointment.

Mr. Bobby Parikh has resigned from the Board w.e.f. October 17, 2006 and Dr. V. R. Gadwal relinquished his office of Director with effect from March 14, 2007. Your directors wish to place on record their sincere appreciation for the contribution made by Mr. Bobby Parikh and Dr. V. R. Gadwal during their tenure as Directors.

The Board at its meeting held on October 17, 2006, appointed Mr. C. M. Vasudev and Mr. Gautam Divan as Additional Directors. The Bank has received notices in writing under Section 257 of the Act, proposing candidatures of Mr. Vasudev and Mr. Divan for the office of Directors of the Bank.

The term of office of Mr. Jagdish Capoor as part-time Chairman of the Bank comes to an end by flux of time on 5th July, 2007. It is proposed to renew the term of Mr. Capoor seeking approval of the members. Resolution to this effect has been included in the notice convening the ensuing Annual General Meeting.

The brief resume/details relating to Directors who are to be appointed/re-appointed are furnished in the report on Corporate Governance.

AUDITORS

The Auditors M/s. Haribhakti & Co., Chartered Accountants will retire at the conclusion of the forthcoming Annual General Meeting and are eligible for re-appointment. Members are requested to consider their re-appointment on remuneration to be decided by the Audit and Compliance Committee of the Board.

ACKNOWLEDGEMENT

Your Directors would like to place on record their gratitude for all the guidance and co-operation received from the Reserve Bank of India and other government and regulatory agencies. Your Directors would also like to take this opportunity to express their appreciation for the hard work and dedicated efforts put in by the Bank's employees and look forward to their continued contribution in building a world class Indian bank.

On behalf of the Board of Directors

Jagdish Capoor
Chairman

Mumbai, May 17, 2007

Annexure to Directors' Report for the year ended March 31, 2007

EMPLOYEES' STOCK OPTIONS

Details of the stock options granted, vested, exercise and lapsed during the year under review are as under:

Scheme(s)	Exercise Price (Rs.)	Options Granted	Options Vested	Options Exercised	Options Lapsed	Total Options in Force As on March 31,2007
ESOP I	131.33	-	-	21000	2100	0
ESOP II	225.43	-	-	128200	17800	1500
ESOP III	226.96	-	-	74400	15300	7600
ESOP IV	358.60	-	2564400	2795900	175300	413600
ESOP V	366.30	-	967700	1385900	75600	194400
ESOP VI	362.90	-	600300	672600	108900	205600
ESOP VII	630.60	-	2611700	1169200	1610700	4526100
ESOP VIII	994.85	3586500	-	-	432900	3153600
ESOP IX	994.85	3046800	-	-	227600	2819200
Total		6633300	6744100	6247200	2666200	11321600

Note : One (1) share would arise on exercise of one (1) stock option.

Other details are as under:

Money realized by exercise of options	The Bank received Rs. 6,24,72,000 towards share capital and Rs. 2,47,77,20,850/- towards share premium on account of 62,47,200 stock options exercised and allotted during the year under review.
Pricing Formula	**ESOS VIII** : Closing market price on the stock exchange where there is highest trading volume during the preceding 2 weeks from the date of grant. **ESOS IX** : Closing market price on the stock exchange where there is highest trading volume on the preceding date of grant.
Details of options granted to:	
i. Senior managerial personnel	Nil
ii. Other employee who receives a grant in any one year of option amounting to 5% or more of option granted during that year	Nil
iii. Identified employees who were granted option, during any one year, equal to or exceeding 1% of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant	Nil
Diluted Earnings Per Share (EPS) pursuant to issue of shares on exercise of option calculated in accordance with Accounting Standard (AS) - 20 (Earnings Per Share).	The Diluted EPS of the Bank calculated after considering the effect of potential equity shares arising on account of exercise of options is Rs. 36.06.
Where the company has calculated the employee compensation cost using the intrinsic value of the stock options, the difference between the employee compensation cost so computed and the employee compensation cost that shall have	Had the Bank followed fair value method for accounting the stock option compensation expense would have been higher by Rs. 134.89 crores. Consequently profit after tax would have been lower by Rs. 89.5 crores and the basic EPS of the Bank would have been Rs. 33.44 per share (lower

Other details are as under:

been recognized if it had used the fair value of the options, shall be disclosed. The impact of this difference on profits and on EPS of the company shall also be disclosed.	by Rs. 2.85 per share) and the Diluted EPS would have been Rs. 33.23 per share (lower by Rs. 2.83)
Weighted-average exercise prices and weighted-average fair values of options shall be disclosed separately for options whose exercise price either equals or exceeds or is less than the market price of the stock options.	The weighted average price of the stock options exercised is Rs. 406.61 and the weighted average fair value is Rs. 595.10.
A description of the method and significant assumptions used during the year to estimate the fair values of options, including the following weighted-average information:	The Securities Exchange Board of India (SEBI) has prescribed two methods to account for stock grants; (i) the intrinsic value method; (ii) the fair value method. The Bank adopts the intrinsic value method to account for the stock options it grants to the employees. The Bank also calculates the fair value of options at the time of grant, using internally developed and tested model with the following assumptions:
i. Risk-free interest rate,	It will remain between 7.8% to 7.9%.
ii. Expected life,	3 (three) years.
iii. Expected volatility,	It will be around 31.75%.
iv. Expected dividends, and	Around Rs. 5.50 per share during the tenor of the ESOSs.
v. The price of the underlying share in market at the time of option grant	The per share market price was Rs. 994.85 at the time of grant of options.