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Stock Idea
July 16, 2014

Capital First Ltd.

Current	Previous
CMP : Rs.223	
Rating : BUY	Rating : NR
Target : Rs.257	Target : NR

(NR-Not Rated)

STOCK INFO	
BSE	532938
NSE	CAPF
Bloomberg	CAFL IN
Reuters	CAPF.BO
Sector	NBFC
Face Value (Rs)	10
Equity Capital (Rs Mn)	826
Mkt Cap (Rs Mn)	17,765
52w H/L (Rs)	240/111
Avg Daily Vol (BSE+NSE)	135,131

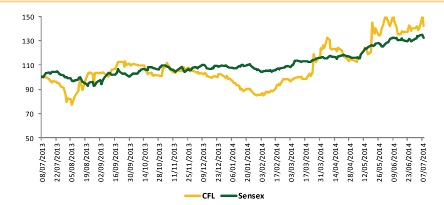
SHAREHOLDING PATTERN	%
(as on 31st Mar. 2014)	
Promoters	72.0
FIIs	0.8
DIIs	4.1
Public & Others	23.1

Source: BSE

STOCK PERFORMANCE (%)	1m	3m	12m
CFL	0	7	42
Sensex	1	14	32

Source: Capitaline, IndiaNivesh Research

CFL v/s SENSEX



Source: Capitaline, IndiaNivesh Research

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Company Background

Capital First Ltd (CFL) is the leading Non Banking Financing Company (NBFC) providing finance to Retail (SME) and Wholesale businesses. In Retail Financing it offers Consumer Durable Loans, Two wheeler Loans, Loan against Property, Mortgage, Gold Loans and Small Business Loans while in Wholesale business it provides loans majorly to real estate developers. CFL has a total AUM of Rs 97 bn with distribution network of 164 branches and 1,089 employees spread across 40 cities.

Investment Rationale

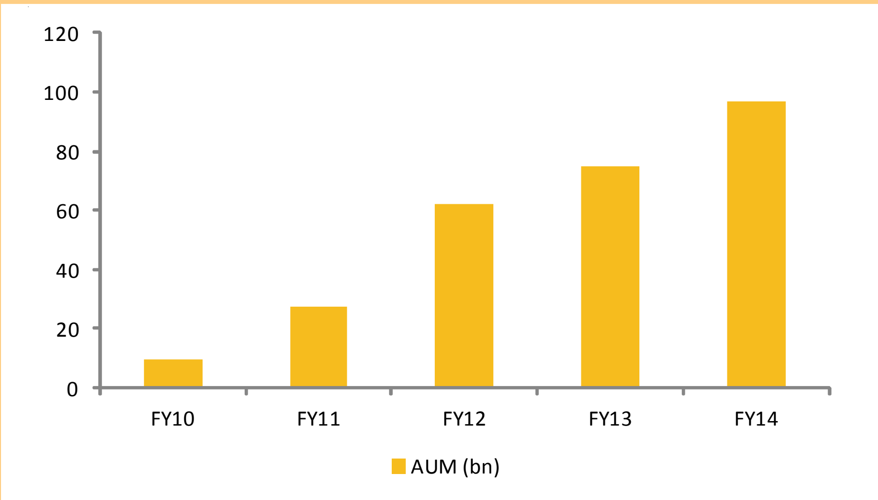
AUM growth much ahead of industry:

Asset Under Management (AUM) of CFL has grown at 79% CAGR over FY10-14 led by low base. As a strategy to focus on retail segment (which includes Consumer Durable Loans, Two wheeler Loans, Loan against Property, Mortgage, Gold Loans and Small Business Loans), AUM of CFL has gradually moved towards retail from 10% in FY10 to 81% in FY14. As a result wholesale loan book (which includes loans to real estate developers) has come down to 19% from 90% over the same period. We believe CFL is well poised to grow at 25% CAGR over FY14-16E with more focus on retail segment.

Particulars (Rs mn)	FY11	FY12	FY13	FY14	FY15E	FY16E
AUM	**27,510**	**61,860**	**75,100**	**96,790**	**120,988**	**151,234**
% Y-o-Y		*124.9*	*21.4*	*28.9*	*25.0*	*25.0*
Wholesale Credit Assets	19,807	27,218	19,526	17,955	20,439	22,814
% of total AUM	*72.0*	*44.0*	*26.0*	*18.6*	*16.9*	*15.1*
Retail Credit Assets	7,703	34,642	55,574	78,835	100,549	128,421
% of total AUM	*28.0*	*56.0*	*74.0*	*81.5*	*83.1*	*84.9*

Source: Company, IndiaNivesh Research

AUM (bn) and YoY Growth (%)



Source: Company, IndiaNivesh Research

Borrowings skewed towards bank loans:

Significant portion of CFL's borrowings forms the term loans from banks which are raised at close to base rate. After the change in management in FY10, Credit rating of CFL has improved materially from A+ in FY11 to AA+ in FY13 which is indication of safety in terms of servicing and also one of the highest ratings in financial services industry. Currently bank borrowings constitute 75% of the total borrowings followed by NCDs (7%) and Sub-ordinated debts (5%). As per the management, borrowing mix is likely to remain at current level with more focus on long term borrowings.

Borrowing Composition *(in terms of %)*	FY12	FY13	FY14
Bank Borrowing	68	72	75
NCDs	10	14	7
Sub-Debt	0	0	5
Perpetual Debt	0	0	2
Short Term Borrowing	7	0	0
Equity	15	14	12
Total	**100**	**100**	**100**

Source: Company, IndiaNivesh Research

Margin to remain stable:

Net Interest Margin (Calc) of CFL has remained stable at 4.5-4.7% in last 2 years. With stable borrowing profile and company's increasing presence in high yielding segments (i.e. two wheeler, gold, consumer durable loans), margins are likely to improve marginally going forward. Currently CFL enjoys the IIR (internal rate of return) of ~27% in Consumer Durable whereas it enjoys ~24% of yield in two wheeler which constitutes 8.4% of the total AUM, ~18% of yield in Gold Loans (6% of the AUM) and ~13% of yield in LAP. Further Average Ticket Size (ATS) in Consumer durables is ~Rs 28000/-, two wheelers is ~Rs 35000/-, Gold loans is ~Rs 120000/- while in LAP it is higher at ~Rs 100 mn. While the management remains confident of improving its NIMs over next 2 to 3 years, we remain conservative and expect it to remain broadly stable at 5.0%.

Asset quality maintained:

CFL was successful in maintaining its asset quality with lowest Gross and Net NPAs in the industry at 0.5% and 0.1% respectively. This is based on the fact that asset mix has shifted towards comparatively safer segments like LAP, Mortgage, two wheelers and Consumer Durables than riskier segments of developer loans. We drive more comfort from stringent provisioning norms of CFL where in it starts providing once the assets cross 90 days overdue which is ahead of regulatory requirement of 180 days. While retail segment is low LTV and ATS business which remains least affected from downturn in the economy, we don't expect any significant deterioration in asset quality and expect it to remain stable.

in terms of %	FY11	FY12	FY13	FY14
GNPA	0.25	0.04	0.11	0.45
NNPA	0.06	0.00	0.01	0.08

Source: Company, IndiaNivesh Research

Healthy Capital Adequacy:

Capital adequacy of CFL remains strong and ahead of regulatory requirement at 22% with tier I capital of 16%. Recent capital infusion from promoter and HDFC (Rs 1.3 bn and Rs 0.5 bn respectively) has boosted Capital adequacy making it one of the best amongst peers.

Returns profile to improve significantly:

ROE of CFL is lower because of the fact that company has changed its accounting policy of amortizing processing fees over the tenure of the loan as against earlier policy of booking the said fees at upfront. Another reason is company's conscious decision of higher provisioning than the regulatory requirements and recent capital infusion. We expect provisioning expense (credit cost) is likely to remain stable going forward. This along with improving efficiency in terms of lower cost to income (expense) ratio is likely to help strong bottom line growth of 98% (due to low base of FY14) over FY14-16E. Consequently ROEs / ROAs (calc) are likely to improve to 10.0% / 1.1% from 3.3% / 0.4% in FY14.

Valuation:

CFL's management has delivered the promises of changing the business strategy which has yielded positive results despite struggling environment for financial services industry. Business mix has completely moved towards safer segments in retail after the new management has taken the charge in FY10 along with significant improvement in credit rating. Further CFL's strategy of 1) moving out of non profitable business like securities and commodity broking, 2) focus on core business of SME financing and 3) best in class asset quality with higher provisioning than regulatory requirement drives more comfort. We believe company is well positioned to deliver the consistent growth of over 25% in next 2-3 years given its strong business model and increasing penetration.

Though return profile of CFL is lower than its closest peer but we believe ROEs are likely improve to double digit by FY16E from current low single digit. Most of the NBFCs are trading at 2.0-2.4x for FY16 ABV and CFL is trading at P/ABV of 1.5x and 1.3x for FY15E and FY16E respectively. Though discount of CFL (currently at an average of ~40%) compared to other NBFCs is likely to narrow down on back of improving return profile yet we are not increasing the targeted multiple and rolling over FY15E multiple to FY16E. Hence we recommend buy on the stock with target price of Rs 257, valuing it at 1.5x FY16E ABV which is much lower than peers valuation of 2.0-2.3x for FY16. Significant deterioration in asset quality, lower asset growth than anticipated and significant correction in property/gold prices remain the risk to our estimates. We intend to come up with detailed initiating coverage on CFL.

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