Can Fin Homes

BSE SENSEX	S&P CNX
59,845	17,807

Stock Info

Bloomberg	CANF IN
Equity Shares (m)	133
M.Cap.(INRb)/(USDb)	65.1 / 0.8
52-Week Range (INR)	685 / 408
1, 6, 12 Rel. Per (%)	-4/0/-16
12M Avg Val (INR M)	618
Free float (%)	70.0

Financials Snapshot (INR b)

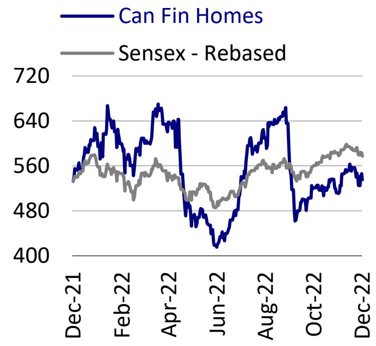
Y/E March	FY22	FY23E	FY24E	FY25E
NII	8.2	10.1	11.4	13.3
PPP	6.8	8.5	9.6	11.3
PAT	4.7	5.9	6.7	7.8
EPS (INR)	35.4	44.2	50.4	58.9
EPS Growth (%)	3.3	25.1	13.9	16.9
BVPS (INR)	230	272	320	377
Ratios (%)				
NIM	3.4	3.5	3.3	3.4
C/I ratio	18.3	17.0	17.1	16.4
RoAA	1.9	1.9	1.9	1.9
RoE	16.6	17.6	17.0	16.9
Payout	5.7	5.0	5.0	4.2
Valuation				
P/E (x)	14.0	11.2	9.8	8.4
P/BV (x)	2.1	1.8	1.5	1.3
Div. Yield (%)	0.4	0.4	0.5	0.5

Shareholding pattern (%)

As On	Sep-22	Jun-22	Sep-21
Promoter	30.0	30.0	30.0
DII	23.3	24.8	21.7
FII	9.3	0.0	0.0
Others	37.4	45.2	48.4

FII Includes depository receipts

Stock Performance (1-year)



CMP: INR489 TP: INR630 (+29%) Buy

In the pink of health - Growth trajectory to remain intact

Re-rating still contingent on CANF's ability to identify a successor

- CANF, in our view, is a franchise which has proven its astute underwriting, strong risk management, and inclination to deliver industry-leading loan growth in the mortgage sector at least (if not more) over the last decade. This report is expected to draw references from our recent interaction with the senior management of CANF in their corporate office at Bangalore, India.
- What we want to highlight through this report is that despite the vacant MD/CEO position at CANF for over a month, the business momentum under the interim leadership of DMD Amitabh Chatterjee and CFO Prashanth Joishy has remained strong. CANF has long demonstrated that it is a processes-driven organization and that it will continue to demonstrate the same ethos and trajectory even under the leadership of the successor to ex-MD Girish Kousgi.
- Management shared that the Board of Directors (BoD) at CANF is keen to onboard a new MD/CEO from the mortgage sector itself (potentially from the private sector, in our view) by offering a compensation in line with the markets (even though the pay-scale at CANF, which is a subsidiary of public sector Canara Bank, is otherwise lower).
- We believe that the intimation to the exchanges would only come (and appropriately so) when the successor formally joins CANF. While identification of the new CEO is in very advanced stages, it is difficult to put a timeline to when the new candidate's name will be announced.
- While there could be near-term transitory compression in margins because of the delay in transmitting higher borrowing costs to the customers, we believe it can sustain NIM of ~3.3-3.4% in the medium term. We model a Loan Book/PAT CAGR of 17%/~19%, respectively, over FY22-FY25E. CANF is a franchise with moats on the liability side and has always exhibited superior asset quality. For a RoA/RoE of 1.9%/17% in FY24E and triggers for valuation re-rating if the new management team (of MD&CEO/CFO/CRO) can gain investor confidence, we reiterate **our BUY rating with a TP of INR630 premised on 1.8x Sep'24 P/BV.**
- Key downside risks are a) inability to attract good talent for senior leadership positions and b) change in parentage (if at all) which could pose a risk to its credit rating and ability to borrow at such low interest rates

Robust franchise; processes orientation has served it well

- Unlike many of its other peers, CANF does not have corporate/builder loans in its loan mix. It has very consistently maintained the share of Home loans in its loan mix at around 90% for the last decade and has consciously stayed away from increasing the proportion of LAP despite the obvious benefits of better spreads/margins. Management in the past has shared that it plans to increase the proportion of LAP over the medium-to-long term.
- What has served CANF really well, in our view, over the last many years, is its process orientation and very little subjectivity/deviations in its credit decisions, which will enable it to flourish even under the leadership of the new MD/CEO.

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Research Analyst: Nitin Aggarwal (Nitin.Aggarwal@MotilalOswal.com) | **Parth Bhavesh Desai** (parth.desai@motilaloswal.com)

Biggest moat is CANF's business model is its superior liability franchise

- Mortgage, particularly the product and customer segments that CANF caters to, has become more of a commodity with very little to differentiate in terms of product/service offerings. One of CANF's biggest moats is its low cost of borrowings. Over the last four years, its average cost of funds stood at 6.4% - which was in line with (and perhaps ever lower) even the likes of LICHF and HDFC Ltd. This in turn is anchored on its strong PSU Bank parentage of Canara Bank as well as its superior asset quality track record over the last decade.
- Understandably, the higher proportion of CP in the borrowing mix (in sharp contrast to all other affordable and low-ticket HFCs) is not viewed very favorably by investors and in a tough external environment can lead to ALM risks and/or sharp increase in borrowing costs. However, CANF has always emphasized that it does not use CPs for lending but instead only as an instrument for cost-arbitrage against the undrawn sanctioned lines from banks.
- The company has managed its liabilities very well – extensively leveraging debt markets pre-IL&FS and rapidly transitioning to bank borrowings (from market borrowing) post that. Unarguably, CANF benefits from >20% of its borrowings mix from the NHB and has a higher dependence on Bank borrowings (v/s a more diversified borrowing mix for peers), it still has been able to consistently deliver very healthy spreads of 2.5%-3.0% over the last five-six years. **We model spreads of 2.8%-3.1% and NIM of 3.3%-3.5% over FY23-FY25.**

Stringent cost-control measures aid in low opex ratios

- Focused on maximizing the productivity by controlling its operating expenses, CANF has maintained a frugal operational structure. The company also extensively leverages the DSA network with ~79% of its sourcing done through the network and the remaining through branches.
- With cost-to-income ratio (CIR) of 16%-17% and opex-to-average loans of 0.6% for the last five-six years, it has exercised stringent cost controls to build this cost-efficient franchise. We continue to model similar cost-ratios of 60bp over FY23-FY25E.

Superior asset quality translates into benign credit costs

- Given its product and customer positioning, CANF has exhibited superior asset quality over time. Its slippage ratio has historically been less than ~0.4%, GS3 ratio has been sub-1%, while the average credit costs over the last five years was ~0.2% (despite the impact of COVID). Stage 2, which peaked to 6% in FY20, has now moderated back to ~3.6% (as on Sep'22).
- CANF's 2QFY23 results reiterated that all the noise around asset quality/fraudulent accounts over the last two quarters have been addressed and there will be no unpleasant surprises after the exit of ex-MD/CEO Mr. Kousgi
- We do not expect any new negative developments in asset quality and estimate FY23-FY25 credit costs of ~15-20bp (in line with historical credit costs).

Parentage allows it to highly lever the balance sheet

- Like LICHF, CANF is able to highly lever its balance sheet, aided by the underlying parentage of Canara Bank. While the average leverage has steadily declined, it has been hovering between 8.8x-10.1x over the last three years, thereby, allowing it to deliver consistently healthy RoEs.

- CANF has an enabling resolution to raise equity capital up to INR10b, which in our view could potentially be in the form of a rights issue. Although we expect CANF to complete this primary equity raise in FY24, we have not factored it in our estimates because this raise could get further postponed since CANF already has a strong CRAR of ~24%.

What are the key risks to the investment thesis in CANF?

- The biggest risk (not that it is imminent) is the change in parentage for CANF. This is especially relevant since the government has been asking state-run banks to review their non-core businesses (link). Without the parentage of a large group or a PSU undertaking, it will be difficult for CANF to maintain high leverage on its balance sheet.
- Another risk is the company's inability to identify a credible successor (MD/ CFO). In the worst case, the parent Canara Bank might have to depute someone from the Bank to lead CANF. While the probability of this is very low, we do not see this event to have any significant impact on our investment thesis at CANF.

Moats on the liability side and superior asset quality; reiterate BUY

- We model a Loan Book/PAT CAGR of 17%/~19%, respectively, over FY22-FY25E.
- For a RoA/RoE of 1.9%/17% in FY24E and triggers for valuation re-rating if the new management team (of MD&CEO/CFO/CRO) can gain investor confidence, we **reiterate our BUY rating with a TP of INR630 (based on 1.8x Sep'24 P/BV).**

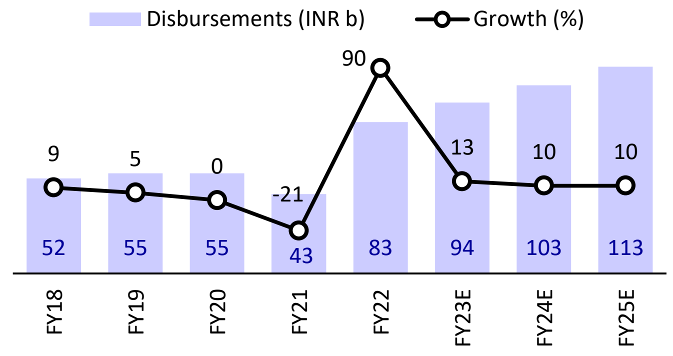
Exhibit 1: Peer valuation matrix

Peers	CMP	Mkt. Cap	BV		P/BV		EPS		P/E		RoA (%)		RoE (%)	
	(INR)	(Rs b)	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Canfin	494	66	272	320	1.8	1.5	44	50	11	10	1.9	1.9	17.6	17.0
Homefirst	696	61	204	235	3.4	3.0	25	31	28	22	3.8	3.7	13.2	14.2
Aavas	1,872	148	410	479	4.6	3.9	54	69	35	27	3.5	3.7	14.1	15.6
Aptus*	275	137	68	79	4.0	3.5	10	11	29	24	7.2	6.8	15.0	15.6
Repco	212	13	397	446	0.5	0.5	42	52	5	4	2.1	2.4	11.3	12.4

Source: MOFSL, Company, Note: Data for Aptus based on consensus estimates

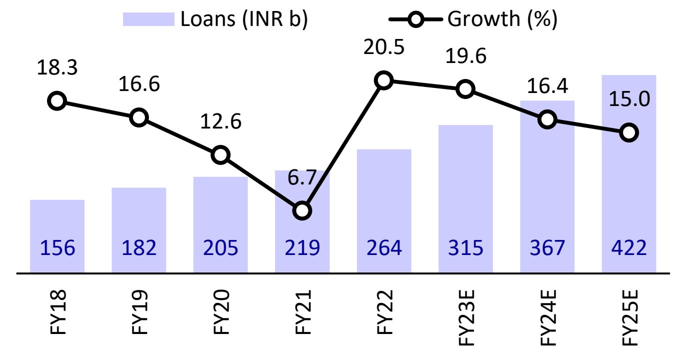
Story in charts

Exhibit 2: Estimate disbursement CAGR of ~11% over FY22-25…



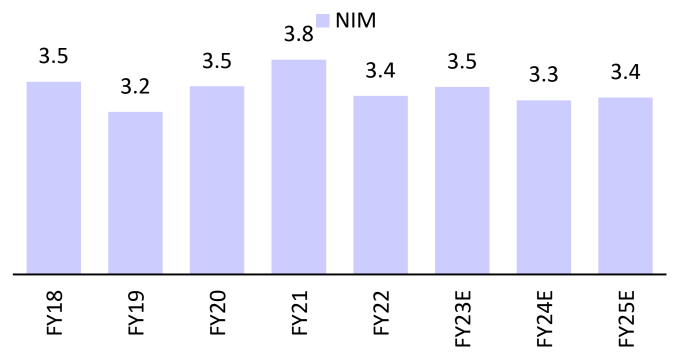
Source: MOFSL, Company

Exhibit 3: …leading to an AUM CAGR of ~17% over this period



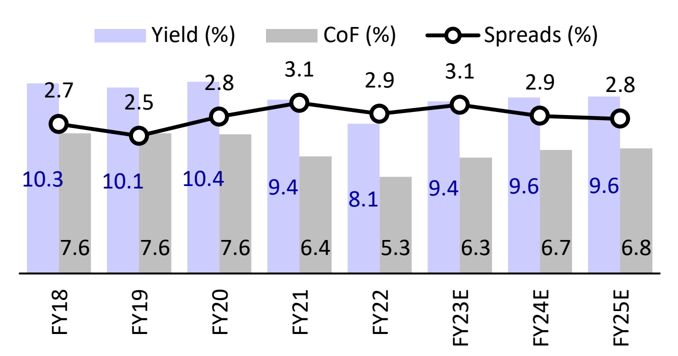
Source: MOFSL, Company

Exhibit 4: Margin likely to moderate to ~3.3% in FY24



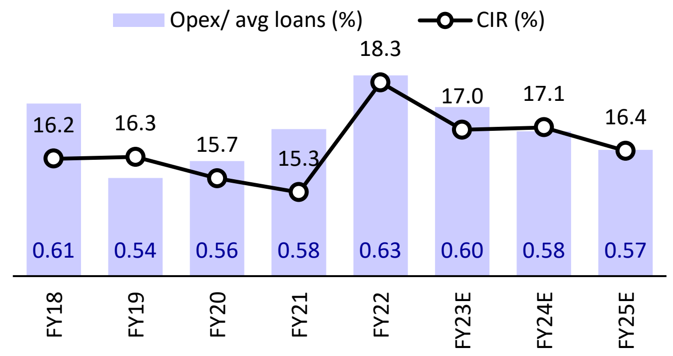
Source: MOFSL, Company

Exhibit 5: Estimate spreads to decline over FY24-FY25



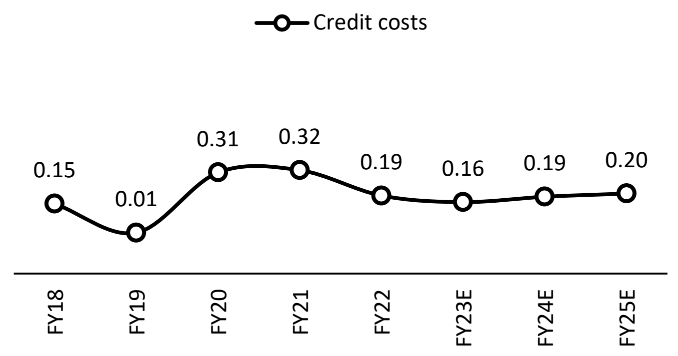
Source: MOFSL, Company

Exhibit 6: Opex to AUM to remain at similar levels of ~60bp



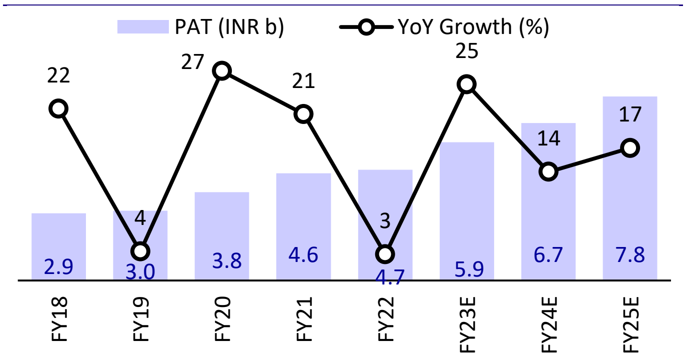
Source: MOFSL, Company

Exhibit 7: Credit costs would normalize to levels of ~20bp



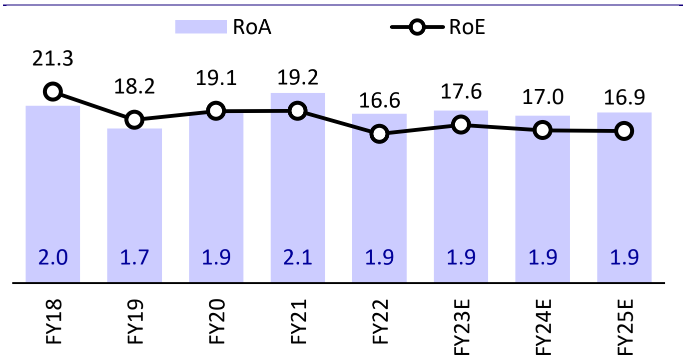
Source: MOFSL, Company

Exhibit 8: Estimate PAT CAGR of ~19% over FY22–25…



Source: MOFSL, Company

Exhibit 9: …while RoE will be healthy at ~17% over FY24-FY25



Source: MOFSL, Company

Robust franchise; processes orientation has served it well

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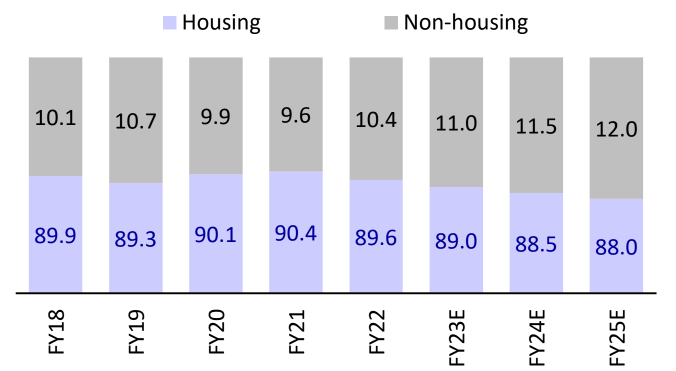
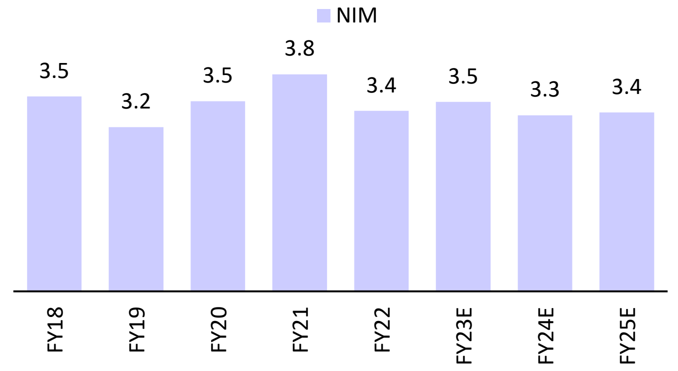
- What has served CANF really well, in our view, over the last many years, is its process orientation and very little subjectivity/deviations in its credit decisioning. This will enable it to continue to flourish even under the leadership of the new MD/CEO.

Exhibit 10: AUM mix basis product type (%)



Source: MOFSL, Company

Exhibit 11: NIMs expected to moderate by ~20bp in FY24



Source: MOFSL, Company

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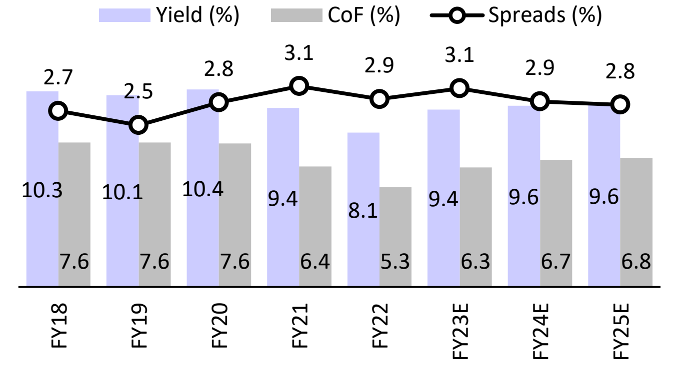
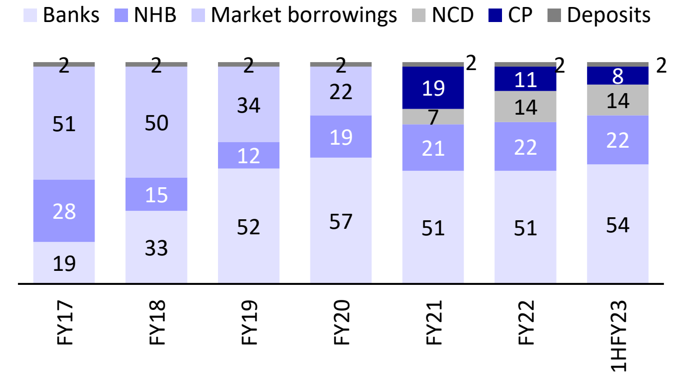
- Mortgage, particularly the product and customer segments that CANF caters to, has become more of a commodity with very little to differentiate in terms of product/service offerings. One of CANF's biggest moats is its low cost of borrowings.
- Over the last four years, its average cost of funds stood at 6.4%, which was in-line with (and perhaps ever lower) the likes of LICHF and HDFC Ltd. This in turn is anchored on its strong PSU Bank parentage of Canara Bank as well its superior asset quality track record over the last decade.
- CANF has always emphasized that it does not use CPs for lending but instead only as an instrument for cost-arbitrage against the undrawn sanctioned lines from banks.
- Unarguably, CANF benefits from >20% of its borrowings mix from the NHB and has a higher dependence on Bank borrowings (v/s a more diversified borrowing mix for peers), it still has been able to consistently deliver healthy spreads of 2.5%-3.0% over the last five-six years. We model spreads of 2.8%-3.1% and NIM of 3.3%-3.5% over FY23-FY25.

Exhibit 12: Model moderation in spreads over FY24-FY25



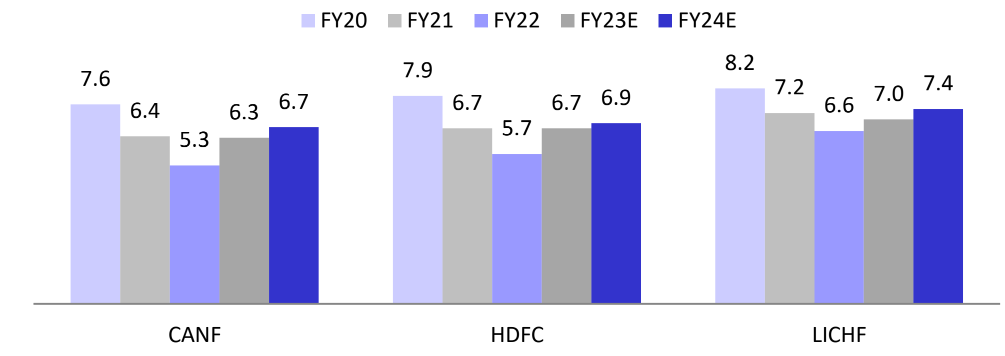
Source: MOFSL, Company

Exhibit 13: CP forms 8% of the borrowing mix (%)



Source: MOFSL, Company

Exhibit 14: CanFin has the lowest CoF among peers

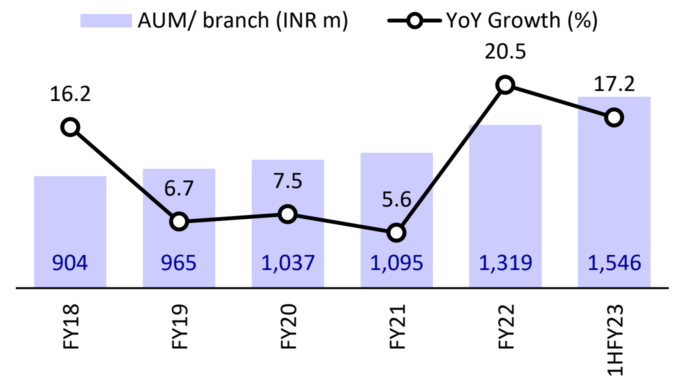


Source: MOFSL, Company

Stringent cost-control measures aid in low opex ratios

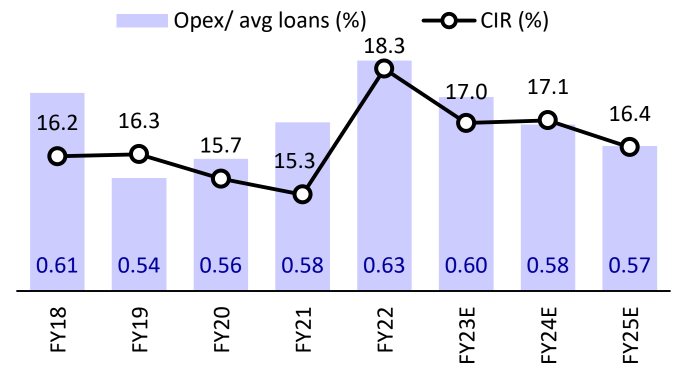
- Focused on maximizing the productivity by controlling the operating expenses, CANF has maintained a frugal operational structure. The company also extensively leverages the DSA network with ~79% of its sourcing done through the network.
- With cost-to-income ratio (CIR) of 16%-17% and opex-to-average loans of 0.6% for the last five-six years, it has exercised stringent cost control measures to build this cost-efficient franchise. We continue to model similar cost-ratios of 60bp over FY23-FY25E.

Exhibit 15: Focus on maximizing productivity…



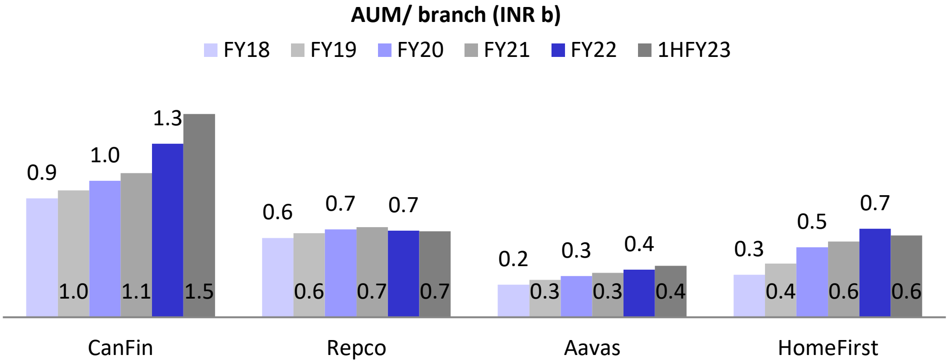
Source: Company, MOFSL

Exhibit 16: … to deliver economies of scale and drive cost efficiencies



Source: Company, MOFSL

Exhibit 17: CanFin has the highest branch productivity among peers

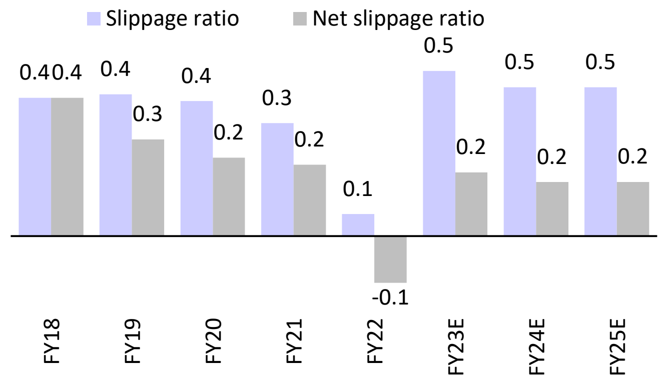


Source: MOFSL, Company

Superior Asset quality translates into very benign credit costs

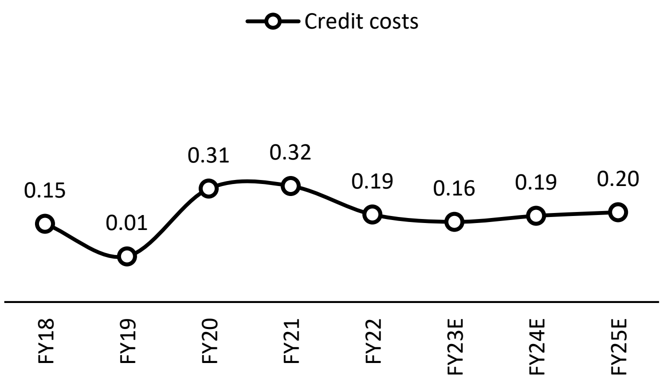
- Given its product and customer positioning, CANF has exhibited superior asset quality over time. Its slippage ratio has historically been less than ~0.4%, GS3 ratio has been sub-1%, while the average credit costs over the last five years was ~0.2% (despite the impact of COVID). **Stage 2, which peaked to 6% in FY20, has now moderated back to ~3.6% (as on Sep'22).**
- CANF's 2QFY23 results reiterated that all the noise around asset quality/fraudulent accounts over the last two quarters have been addressed and there will be no unpleasant surprises after the exit of ex-MD/CEO Mr. Kousgi.
- We do not expect any new negative developments in asset quality and estimate FY23-FY25 credit costs of ~15-20bp (in line with historical credit costs).

Exhibit 18: Slippage ratio has historically been largely stable



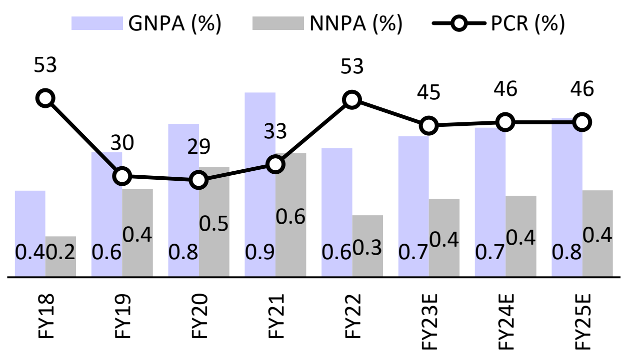
Source: MOFSL, Company

Exhibit 19: Expect credit costs to moderate to ~20bp (%)



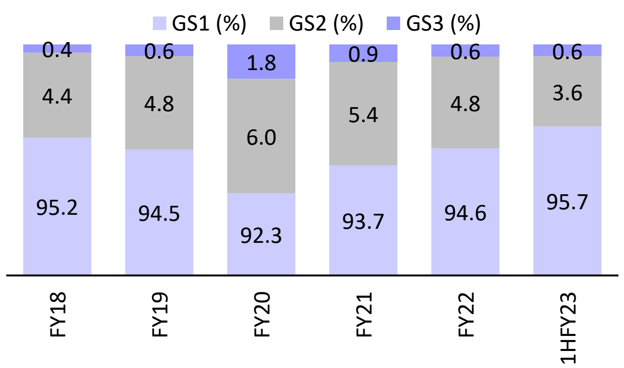
Source: MOFSL, Company

Exhibit 20: NNPA sub 0.5%



Source: MOFSL, Company

Exhibit 21: Gradual improvement in Stage 2

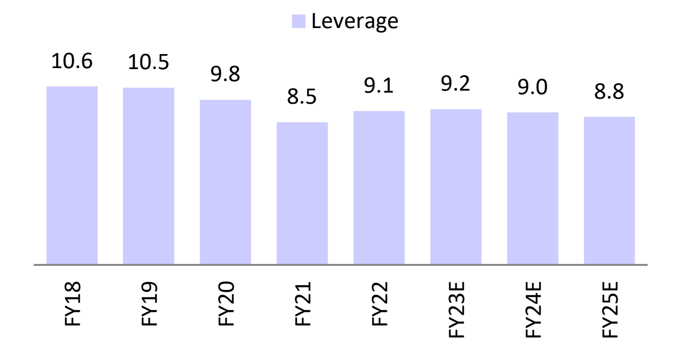


Source: MOFSL, Company

Parentage allows it to highly lever the balance sheet

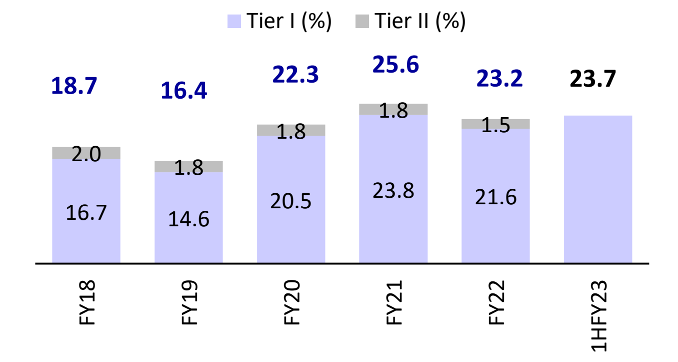
- Like LICHF, CANF is able to highly lever its balance sheet, aided by the underlying parentage of Canara Bank.
- While the average leverage has steadily declined, it has been hovering around 8.8x-10.1x over the last three years, which in turn has allowed it to consistently deliver healthy RoEs.

Exhibit 22: Parentage allows for such high leverage



Source: Company, MOFSL

Exhibit 23: Healthy capital adequacy levels

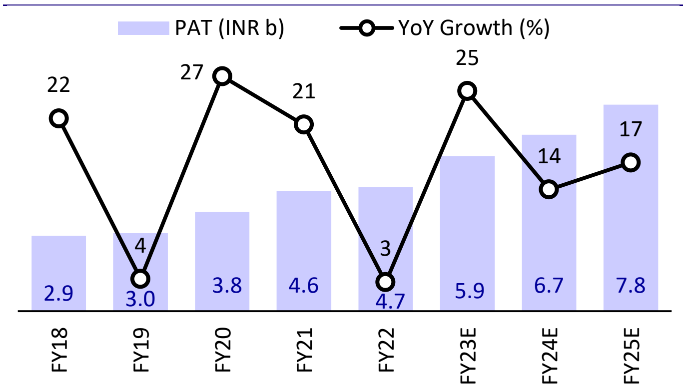


Source: Company, MOFSL

Moats on the liability side and superior asset quality; reiterate BUY

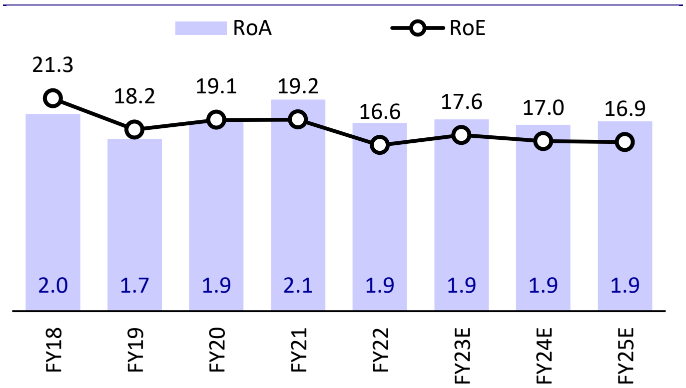
- We model a Loan Book/PAT CAGR of 17%/~19%, respectively, over FY22-FY25E.
- For a RoA/RoE of 1.9%/17% in FY24E and triggers for valuation re-rating if the new management team (of MD&CEO/CFO/CRO) can gain investor confidence, we **reiterate our BUY rating with a TP of INR630 (premised on 1.8x Sep'24 P/BV).**

Exhibit 24: Expect PAT CAGR of ~19% over FY22–25…



Source: MOFSL, Company

Exhibit 25: …leading to a healthy RoE of ~17% over FY24-FY25



Source: MOFSL, Company

Exhibit 26: Increase our FY24 EPS by ~2% to factor in lower credit costs

INR b	Old Est.		New Est.		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
NII	10.0	11.3	10.1	11.4	0.2	0.6
Other Income	0.2	0.3	0.2	0.3	0.0	0.0
Total Income	**10.3**	**11.6**	**10.3**	**11.6**	**0.2**	**0.6**
Operating Expenses	1.8	2.0	1.8	2.0	0.0	0.0
Operating Profits	**8.5**	**9.6**	**8.5**	**9.6**	**0.2**	**0.7**
Provisions	0.5	0.7	0.5	0.6	0.0	-13.4
PBT	**8.1**	**8.8**	**8.1**	**9.0**	**0.2**	**1.9**
Tax	2.2	2.3	2.2	2.3	0.2	1.9
PAT	**5.9**	**6.6**	**5.9**	**6.7**	**0.2**	**1.9**
AUM	318	369	318	370	0.0	0.5
Borrowings	294	339	295	339	0.4	0.0
NIM (%)	3.5	3.3	3.5	3.3		
ROA (%)	1.9	1.8	1.9	1.9		
RoE (%)	17.6	16.7	17.6	17.0		

Source: MOFSL, Company

Financials and valuation

Income statement — **INR m**

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Interest Income	10,444	13,060	14,906	17,134	20,189	20,064	19,697	27,137	32,648	37,935
Interest Expended	7,435	8,840	9,810	11,693	13,442	12,083	11,535	17,072	21,269	24,663
Net Interest Income	**3,009**	**4,220**	**5,096**	**5,441**	**6,747**	**7,980**	**8,162**	**10,065**	**11,379**	**13,272**
Change (%)	69.4	40.2	20.8	6.8	24.0	18.3	2.3	23.3	13.1	16.6
Other Income	391	471	314	179	115	121	188	225	257	295
Net Income	**3,401**	**4,691**	**5,410**	**5,621**	**6,862**	**8,101**	**8,350**	**10,290**	**11,636**	**13,568**
Change (%)	64.5	37.9	15.3	3.9	22.1	18.0	3.1	23.2	13.1	16.6
Operating Expenses	668	807	878	915	1,076	1,240	1,530	1,752	1,988	2,231
Operating Income	**2,733**	**3,884**	**4,532**	**4,706**	**5,786**	**6,861**	**6,820**	**8,538**	**9,648**	**11,337**
Change (%)	80.1	42.1	16.7	3.8	23.0	18.6	-0.6	25.2	13.0	17.5
Provisions/write offs	194	188	221	11	603	685	469	467	643	808
PBT	**2,539**	**3,696**	**4,311**	**4,695**	**5,183**	**6,176**	**6,351**	**8,071**	**9,005**	**10,529**
Tax	968	1,349	1,449	1,728	1,422	1,615	1,640	2,179	2,296	2,685
Tax Rate (%)	38.1	36.5	33.6	36.8	27.4	26.2	25.8	27.0	25.5	25.5
Reported PAT	**1,571**	**2,347**	**2,862**	**2,967**	**3,761**	**4,561**	**4,711**	**5,892**	**6,708**	**7,844**
Change (%)	82.2	49.4	22.0	3.7	26.8	21.3	3.3	25.1	13.9	16.9
Proposed Dividend (incl. tax)	321	321	321	321	321	266	266	293	333	333

Balance sheet

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Capital	266	266	266	266	266	266	266	266	266	266
Reserves & Surplus	8,514	11,771	14,604	17,556	21,234	25,832	30,400	35,999	42,374	49,885
Net Worth	**8,780**	**12,037**	**14,870**	**17,822**	**21,501**	**26,098**	**30,666**	**36,265**	**42,640**	**50,151**
Borrowings	90,740	1,18,675	1,39,210	1,67,974	1,87,484	1,92,929	2,46,477	2,95,491	3,39,411	3,85,963
Change (%)	23.0	30.8	17.3	20.7	11.6	2.9	27.8	19.9	14.9	13.7
Other liabilities	8,040	2,168	3,215	1,500	1,451	1,710	2,300	2,761	3,313	3,975
Total Liabilities	**1,07,560**	**1,32,880**	**1,57,295**	**1,87,295**	**2,10,436**	**2,20,737**	**2,79,443**	**3,34,516**	**3,85,364**	**4,40,090**
Loans	**1,07,146**	**1,32,241**	**1,56,440**	**1,82,342**	**2,05,257**	**2,18,915**	**2,63,781**	**3,15,358**	**3,66,931**	**4,21,818**
Change (%)	29.1	23.4	18.3	16.6	12.6	6.7	20.5	19.6	16.4	15.0
Investments	149	160	160	163	243	496	11,260	12,949	14,891	17,125
Change (%)	0.0	7.1	0.0	1.9	49.1	104.1	2,169.9	15.0	15.0	15.0
Net Fixed Assets	89	102	96	99	379	378	346	317	290	265
Other assets	175	377	600	4,692	4,557	948	4,057	5,892	3,252	882
Total Assets	**1,07,560**	**1,32,880**	**1,57,295**	**1,87,295**	**2,10,436**	**2,20,737**	**2,79,443**	**3,34,516**	**3,85,364**	**4,40,090**

E: MOFSL Estimates -

Financials and valuation

Ratios										(%)
Y/E March	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23E**	**FY24E**	**FY25E**
Yield on loans	11.0	10.9	10.3	10.1	10.4	9.44	8.14	9.4	9.6	9.6
Cost of funds	9.0	8.4	7.6	7.6	7.6	6.35	5.25	6.3	6.7	6.8
Spread	1.9	2.5	2.7	2.5	2.8	3.1	2.9	3.1	2.9	2.8
Net Interest Margin	3.2	3.5	3.5	3.2	3.5	3.8	3.4	3.5	3.3	3.4
Profitability Ratios (%)										
RoE	19.0	22.5	21.3	18.2	19.1	19.2	16.6	17.6	17.0	16.9
RoA	1.6	2.0	2.0	1.7	1.9	2.1	1.9	1.9	1.9	1.9
C/I ratio	19.6	17.2	16.2	16.3	15.7	15.3	18.3	17.0	17.1	16.4
Asset Quality (%)										
Gross NPAs	198	279	675	1,135	1,571	2,019	1,706	2,220	2,740	3,349
Gross NPAs to Adv.	0.2	0.2	0.4	0.6	0.8	0.9	0.6	0.7	0.7	0.8
Net NPAs	0	0	316	795	1,118	1,343	807	1,221	1,480	1,809
Net NPAs to Adv.	0.0	0.0	0.2	0.4	0.5	0.6	0.3	0.4	0.4	0.4
PCR	100.0	100.0	53.2	30.0	28.8	33.5	52.7	45.0	46.0	46.0
VALUATION										
Book Value (INR)	66	90	112	134	161	196	230	272	320	377
Price-BV (x)	**7.5**	**5.5**	**4.4**	**3.7**	**3.1**	**2.5**	**2.1**	**1.8**	**1.5**	**1.3**
EPS (INR)	11.8	17.6	21.5	22.3	28.2	34.2	35.4	44.2	50.4	58.9
EPS Growth YoY	82.2	49.4	21.9	3.7	26.8	21.3	3.3	25.1	13.9	16.9
Price-Earnings (x)	**41.9**	**28.0**	**23.0**	**22.2**	**17.5**	**14.4**	**14.0**	**11.2**	**9.8**	**8.4**
Dividend per share (INR)	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.2	2.5	2.5
Dividend yield (%)	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.5**	**0.5**

E: MOFSL Estimates

NOTES

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Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
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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