June 13, 2016

SECTOR REPORT

# Housing Finance Companies

***The outlook stays bright***


## Summary

**The demographic drivers for housing demand in India have remained fairly unchanged, particularly the favourable demographics (favourable risk profile for mortgages due to young population) and rising prosperity (sustained move towards becoming a middle income country). While housing finance has been a rare growth driver for both banks and HFCs in an otherwise tepid growth scenario, it looks to sustain a stronger trend as some of the new structural changes begin to take effect over the medium term. Prominent amongst these are the PMAY-G & U, Real Estate Regulation Act as well as the innovative changes being ushered in by various state governments for acquiring land for housing projects. These changes are likely to provide a strong foundation for housing demand over medium term.**

**We initiate coverage on HDFC (BUY, TP Rs1,429), LICHF (BUY, TP Rs560), and Repco Home Finance (ACCUMULATE, TP Rs820). HDFC and LICHF are firmly entrenched HFCs with strong operating history while Repco Home Finance, though relatively younger has created a niche for itself by focusing on the low income as well as self-employed category. We believe these companies are a strong play on the dominant themes in housing finance – urbanization, rising prosperity, and affordable housing.**


## Investment rationale and outlook

- **Mortgage penetration higher in urban areas**

  RBI's data on commercial bank credit for housing shows a higher distribution in urban areas and therefore a higher concentration in states which have a higher urban population. Rising urbanization, as seen in the decadal population trends alongwith low ownership in the urban areas forms a strong theme for housing finance demand in India. Secondly, with a significant quantum of existing housing stock in single, two room accommodations, demand based on aspiration for ownership of bigger homes can be strong going forward. We also look at other structural drivers – smart cities, RERA, rural and urban housing schemes of GoI.

- **HFCs doing well in a tough game**

  Over the last few years, commercial banks have focused on getting a slice of the housing finance market. The aggressively played pricing game saw banks offering rates close or at par to their base rates. HFCs differentiated by making the difference in their lending rates vis-à-vis banks' rates less meaningful and concentrating on delivering their product faster. This gave the HFCs edge to compete strongly with banks and we believe they could in fact have increased their market share.

- **Initiating coverage on HDFC, LICHF, REPCO**

  Broadly, we see a) strong growth rates, b) sustainable spreads, c) supported by low delinquency levels as key financial theme for the housing finance sector. The medium term outlook offers strong growth opportunities if recent regulatory changes go through and we find HFCs well placed to exploit this opportunity.

**Table: Standalone financial projections**

| Particulars | Operating Income (Rs mn) | | | Operating Profit (Rs mn) | | | Adjusted PAT (Rs mn) | | | EPS (Rs) | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | FY16 | FY17E | FY18E | FY16 | FY17E | FY18E | FY16 | FY17E | FY18E | FY16 | FY17E | FY18E |
| HDFC | 111,321 | 116,051 | 129,768 | 103,731 | 108,026 | 121,182 | 70,931 | 73,505 | 81,543 | 44.9 | 46.5 | 51.6 |
| LICHF | 31,787 | 35,834 | 41,179 | 27,100 | 30,374 | 34,778 | 16,608 | 18,708 | 21,423 | 32.9 | 37.0 | 42.4 |
| REPCO | 3,335 | 4,188 | 5,216 | 2,692 | 3,439 | 4,344 | 1,501 | 1,951 | 2,449 | 24.1 | 31.3 | 39.3 |

*Source: Company; IDBI Capital Research*

**Table: Valuation**

| Particulars | CMP (Rs) | Target Price (Rs) | Reco | P/ABV (x)* | | | RoE (%) | | | RoA (%) | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | FY16 | FY17E | FY18E | FY16 | FY17E | FY18E | FY16 | FY17E | FY18E |
| HDFC | 1,231 | 1,429 | **BUY** | 5.7 | 5.1 | 4.6 | 21.8 | 20.3 | 20.1 | 2.6 | 2.4 | 2.3 |
| LICHF | 473 | 560 | **BUY** | 2.7 | 2.3 | 2.0 | 19.6 | 18.9 | 18.7 | 1.4 | 1.3 | 1.2 |
| REPCO | 740 | 820 | **ACCUMULATE** | 4.8 | 4.1 | 3.4 | 17.0 | 18.7 | 19.7 | 2.2 | 2.2 | 2.1 |

**P/BV for HDFC*

*Source: Company; IDBI Capital Research*

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## Valuation and recommendation

- **HDFC Ltd. (TP – Rs1,429; 16% upside; BUY)**

  Though HDFC shall continue to be identified with retail housing finance, given it's pioneering foray into a segment when it did not exist, the company has over the years grown into a valuable financial conglomerate. Our SOTP value for HDFC finds ~40% value accruing from it's associates and subsidiary companies, which are leaders in their respective businesses. HDFC's ~24% capital is leveraged for associate/subsidiary company business and value accretion in these businesses has been significant even as housing finance business continues to grow steadily. We believe HDFC shall continue to deliver value as it's strong franchise across businesses keeps it anchored as a leading financial conglomerate.

  Our **BUY** rating and price target of Rs1,429 is based on SOTP valuation.

- **LIC Housing Finance Ltd. (TP – Rs560; 18% upside; BUY)**

  The introduction of a new loan product in LAP category has boosted LICHF's earnings momentum while supporting growth, which though robust, had remained concentrated in the traditional housing finance segment. LIC Housing Finance Ltd. (LICHF)'s loan mix had suffered adversely when it's corporate loan book kept unwinding (declining from ~9% in FY11 to ~2% in FY14) and an asset quality event made the company go slow in the non-individual space. This alongwith pricing competition from aggressive banks kept up the pressure on spreads.

  We expect LICHF to remain in a healthy earnings trajectory supported by a benign funding environment and strong growth in high yield LAP segment. Initiate with **BUY** and price target of Rs560.

- **Repco Home Finance Ltd. (TP – Rs820; 11% upside; ACCUMULATE)**

  Repco's niche since inception has been it's focus on self-employed segment of housing finance. As housing finance gained acceptability amongst lenders, it evolved around the salaried customer while the potentially creditworthy but difficult to assess self-employed class remained out of the ambit of lenders. Repco has over the years exploited this niche and established itself firmly in the self-employed segment while continuing to generate equal quantum of growth in the traditional salaried segment. The company's recent, aggressive focus on LAP has given added momentum to earnings. Initiate coverage with **ACCUMULATE** recommendation and a 1-year price target of Rs818 valuing Repco at 21x FY18E EPS Rs39.3 and 3.9x FY18E ABV Rs209.6.

# Trends and drivers of housing demand growth

The demographic drivers for housing demand in India have remained fairly unchanged, particularly the favourable demographics (favourable risk profile for mortgages due to young population) and rising prosperity (sustained move towards becoming a middle income country).

We believe these factors shall continue to remain key structural drivers for housing demand. While demand side has been robust, the constraints have traditionally been observed on the supply side, particularly the LIG (low income group) segment.

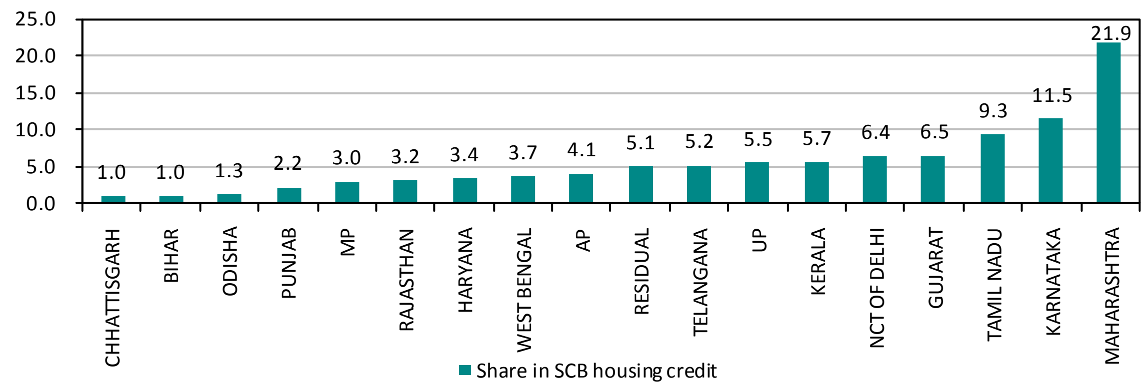
The other structural factors, notably the PMAY-G, Real Estate Regulation Act etc are likely to provide a strong structural framework to housing demand over medium term.

- **Mortgage penetration higher in urban areas**

  RBI's data on commercial bank credit for housing shows a higher distribution in urban areas and therefore a higher concentration in states which have a higher urban population. Thus, the housing mortgage to GSDP (gross state domestic product) is highest for Maharashtra and Karnataka (amongst most urbanized and prosperous states) and lowest for Bihar (amongst least urbanized), based on data for FY15 (RBI publishes data with a one year lag). We consider Chandigarh and NCT of Delhi as outliers (15.8% and 8.3% respectively) given these are city governments / states with mostly urban population.

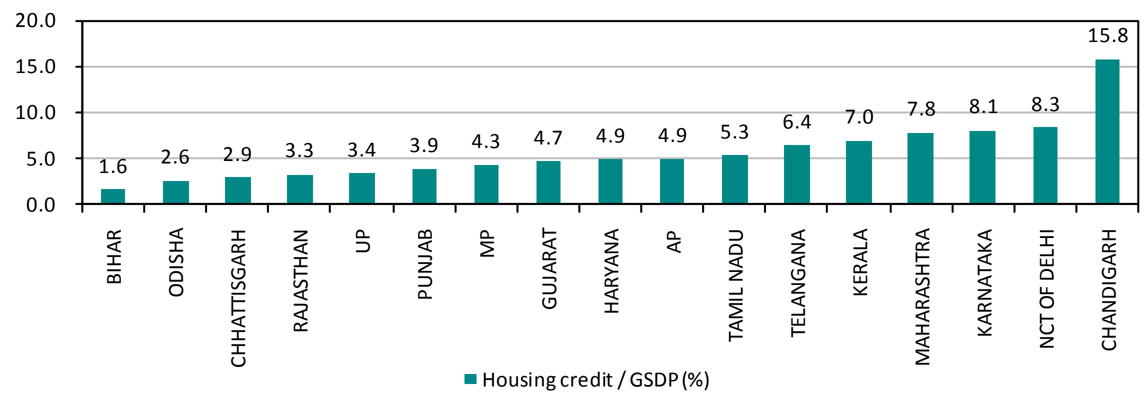
  A similar state-wise dataset for HFCs is not available from NHB (National Housing Bank – regulator for housing finance). However, penetration patterns based on geographic area (metro, urban, semi-urban, and rural) exhibit similar distribution pattern.

**Figure: Mortgage penetration amongst India's states (SCB data)**




*Source: RBI; IDBI Capital Research*

**Figure: Mortgages as % of GSDP: States with high urbanization show higher penetration (SCB data)**




*Source: RBI; IDBI Capital Research*

In terms of mortgage penetration, states like Bihar, Chattisgarh, Odisha, and Rajasthan are at a stage where India was in early 90s whereas states with relatively higher penetration have a still stronger scope for penetration if compared with middle income SE Asian economies.

- **India is steadily urbanising**

Except the first two census decades post-independence, the trend in India's urbanization has been steady with the latest census decade (2001-2011) showing a faster pick-up in urbanization trend (refer to the tables below) even as decadal population growth slowed. By urbanization, we refer to the phenomenon of rising urban population, as identified in the census of India.

**Table: Rural-urban differential in population growth**

| Period | Avg. annual population growth (%) | | |
|---|---|---|---|
| | Rural | Urban | Total |
| 1951-1961 | 2.06 | 2.64 | 2.16 |
| 1961-1971 | 2.19 | 3.82 | 2.48 |
| 1971-1981 | 1.93 | 4.61 | 2.47 |
| 1981-1991 | 2.00 | 3.64 | 2.38 |
| 1991-2001 | 1.81 | 3.15 | 2.15 |
| 2001-2011 | 1.22 | 3.18 | 1.76 |

**Table: Trend in urbanization in India**

| Year | Ur.pop.*# | Change# |
|---|---|---|
| 1951 | 17.30 | |
| 1961 | 18.00 | 0.70 |
| 1971 | 19.90 | 1.90 |
| 1981 | 23.30 | 3.40 |
| 1991 | 25.70 | 2.40 |
| 2001 | 27.80 | 2.10 |
| 2011 | 31.20 | 3.40 |

* Urban population as % of total population, # Values in percentage

*Source: Registrar General of India, Socio Economic Statistics of India, 2011*

The steady pick-up in urbanization post-1971 also coincides with the launch of new cities (post completion of basic infrastructure), prominent examples being Chandigarh (Union Territory, 1966), Gandhinagar (Gujarat, 1970), Pimpri-Chinchwad New Township (1972) and Navi Mumbai (1979) (both in Maharashtra) etc. This is not to argue the pick-up in urbanization was because of creation of new cities, which were far fewer and cumulatively still constitute a small portion of India's overall urban population. Nevertheless, decadal trends do confirm urbanization is here to stay and new cities – greenfield or satellite townships (extensions to existing urban agglomerations) shall have no dearth of demand for housing.

- **Size of households in urbanizing India slowly shrinking…**

…or in other words, number of households in India is rising even as population growth slows. We believe rising urbanization caused by migration of labour (skilled and unskilled) as well as shrinking size of families due to nuclearisation is driving the demand for housing in India.

**Table: Size of rural and urban households has shrunk faster than slowdown in population growth rate**

| Year | Average size of household | | | Avg. no. of persons / dwelling | | |
|---|---|---|---|---|---|---|
| | Rural | Urban | Total | Rural | Urban | Total |
| | | | | | | |
| 1961 | 5.2 | 5.1 | 5.2 | 5.5 | 5.7 | 5.5 |
| 1971 | 5.5 | 5.2 | 5.5 | 6.0 | 6.0 | 6.0 |
| 1981 | 5.6 | 5.5 | 5.6 | 5.9 | 5.7 | 5.8 |
| 1991 | 5.6 | 5.3 | 5.5 | 5.8 | 5.5 | 5.7 |
| 2001 | 5.4 | 5.1 | 5.3 | 4.9 | 5.1 | 5.1 |
| 2011 | 4.9 | 4.6 | 4.8 | n.a. | n.a. | n.a. |

*Source: Registrar General, India; Census of India 2011; IDBI Capital Research*

The urbanization trend is therefore leading to villages on the periphery of expanding cities getting subsumed into urban areas (becoming part of urban local bodies). In the latter case, such subsuming typically leads to better civic infrastructure – most importantly in terms of access roads and electricity. This usually creates new urban growth centres. A typical example of such an expansion is the Shil Phata area near Dombivli (Dombivli-Navi Mumbai), which in the last 8 years has added significant housing stock.

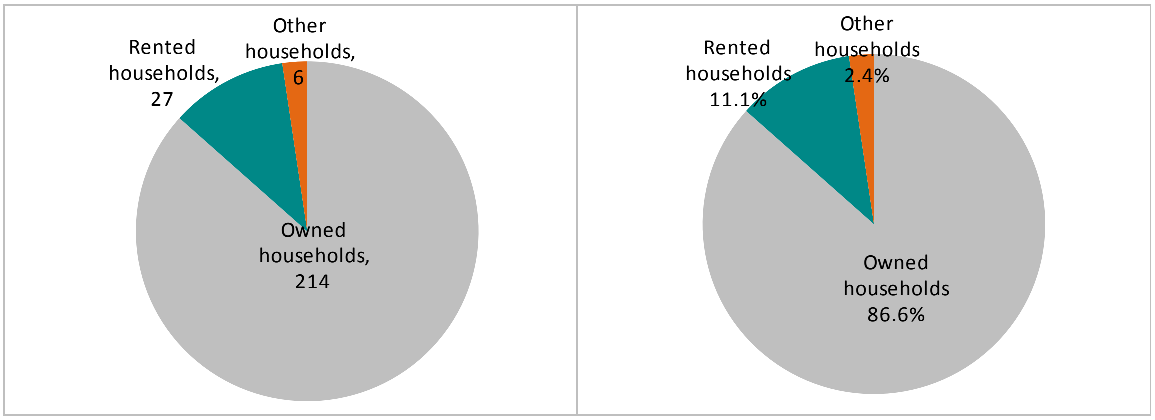
- **The urban housing paradox: high mortgage penetration but low home ownership in urban areas**

Our analysis shows urban areas check all boxes for a high home ownership rate. However, the census data actually presents a paradox. The driving factors of mortgage penetration – urbanization, falling home ownership age – are not necessarily leading to high ownership rates though ownership overall is indeed rising. In other words, while mortgage penetration continues to rise in urban areas, home ownership is not rising at the same pace.

The latest Census of India (2011) data throws up some interesting data points on the supply and type of housing in India. The census data shows a significant 86.6% housing stock is owned with a high, 94.7% ownership in rural areas and a low 69.2% ownership in urban areas. This also explains the challenge of low cost affordable housing in urban areas, which remain major centres of growth and new employment.

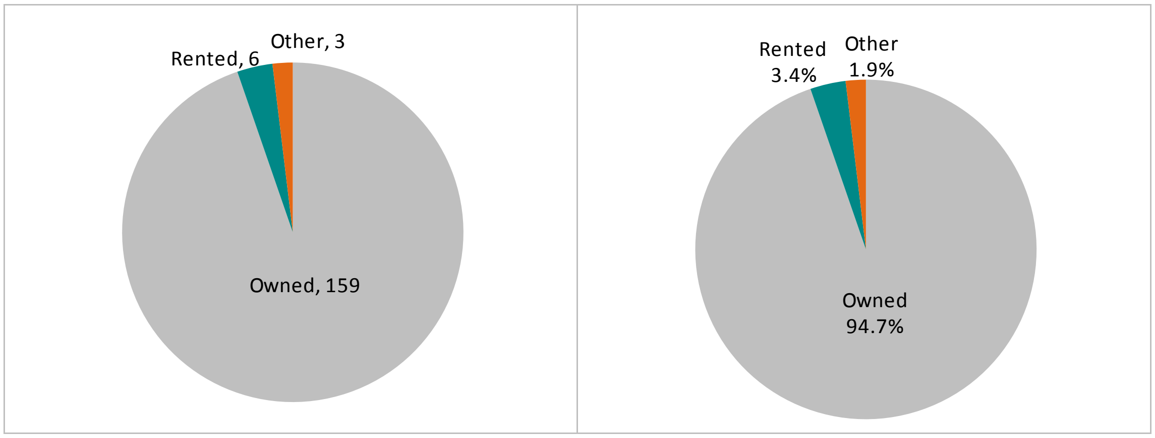
One reason for low ownership in urban areas is likely to be prevalence of slums which are often illegal structures. Other reason could be demand for rental housing by migrants who may take time to create equity before making a house purchase. This is likely to be true in places like Mumbai which typically see significant migration from other parts of the country.

**Figure: Home ownership in India**



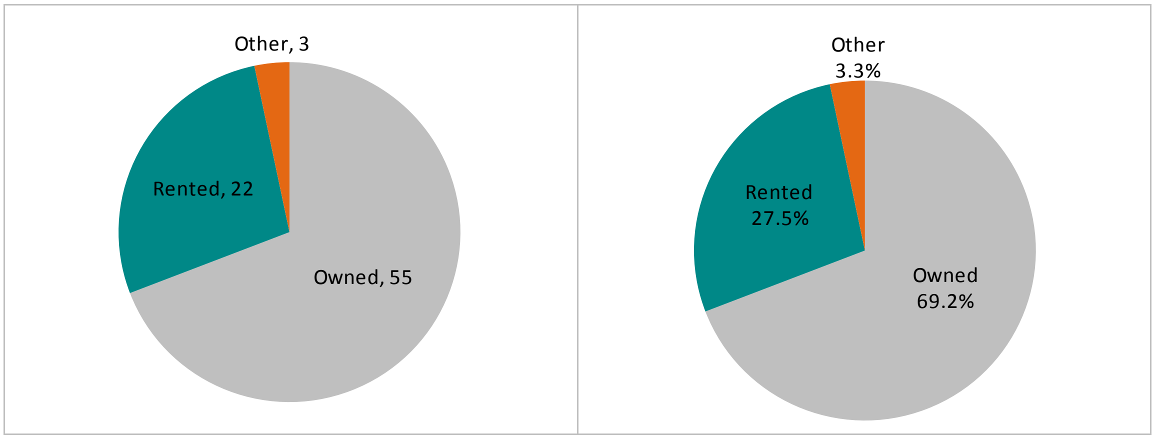

*Source: Census of India 2011; IDBI Capital Research*

**Figure: Home ownership in rural areas**




*Source: Census of India 2011; IDBI Capital Research*

**Figure: Home ownership in urban areas**




*Source: Census of India 2011; IDBI Capital Research*

# Structural drivers for medium term: Smart Cities, Rural Housing, Real Estate Law

## Role of New Townships and Smart Cities

Independent India has seen creation of new, planned cities that today count amongst prominent cities offering good quality of life. Most of these cities have been created out of erstwhile scattered villages which have now become seamlessly connected with a rise in population. Some of these cities are summarized below.

**Table: Greenfield cities created in post-independent India**

| City | Created By | Year founded# | Area (sq.km.) | Population in inception year | Population in latest census |
|---|---|---|---|---|---|
| Chandigarh | Govt. of India | 1966 | 114 sq.km. | 0.02mn | 1.05mn |
| Navi Mumbai | Govt. of Maharashtra | 1979 | 344 sq.km. | 0.16mn | 1.12mn |
| Pimpri Chinchwad New Township | Govt. of Maharashtra | 1972 | 43 sq.km. | n.a. | 0.50mn |
| New Town Kolkata | Govt. of West Bengal | 2007 | 28 sq.km. | n.a. | 0.40mn |
| Gandhinagar | Govt. of Gujarat | 1970 | 177 sq.km. | n.a. | 0.29mn |
| Lavasa^ | HCC | n.a. | 100 sq.km. | n.a. | 0.20mn* |

# Year when planned basic infrastructure was ready, *on completion, ^Lavasa is a hill town

*Source: Respective city websites; IDBI Capital Research*

The number of metropolitan cities with a population of 1mn and above increased from 35 in 2001 census to 50 in 2011 and is estimated to further increase to 87 by 2031 (NHB). This therefore brings into focus the need to add capacity – modern urban infrastructure – to cities that shall expand future metropolises. The planned 100 smart cities – a mission mode plan to turn India's mega cities into world class cities by rejuvenating their infrastructure is a promising intervention. The initial outlay of USD15bn is likely to see further investments by the government to modernize basic infrastructure of these cities. A total 33 cities have been currently shortlisted through a Smart City Challenge to receive direct Government of India funding under the Smart Cities Mission through SPV route.

## Significant shortfall in affordable housing

Affordable housing has been talked about for a long time now. Most of the shortfall in housing supply, variously estimated at 62.5mn homes (MHUPA, NHB), is in the affordable housing category. The Government of India defines affordable housing both in terms of value of home / dwelling unit as well as the carpet area. The following table compares two prevalent definitions:

**Table: Affordable housing definitions**

| Parameter | RBI (for purposes of ECB) | Government of India (PMAY-G)* |
|---|---|---|
| Housing project | Min 60% FSI for affordable housing | - |
| Unit area (sq.ft.) | Max 60 sq.m. carpet (645 sq.ft.) | Max 25 sq.m. |
| Value of home (for purpose of housing loan) | Max Rs3mn | - |
| Max permissible home loan | Rs2.5mn | - |
| Other parameters | - | a) Direct government assistance between Rs120,000 to Rs130,000,<br>b) Government facilitation for home loan up to Rs70,000. |

* Prime Minister Awaas Yojana - Gramin (Prime Minister Housing Scheme - Rural)

*Source: RBI; GoI; IDBI Capital Research*

## Will housing demand pick up more strongly?

So far, trends analysed above show a clear correlation between urbanization and housing demand with higher mortgage penetration rates in more urbanized states. Secondly, census data, as analysed earlier, also shows a high home ownership rate (94.5%) in rural areas. This is not surprising given the high prevalence of land ownership, howsoever marginal, in the rural areas. Still, the ~6.5% non-ownership does present a significant rural housing opportunity, given the still high rural population.

Secondly, the quality of housing differs and this is also an area where the government's rural housing scheme shall look to make a difference. The new housing scheme is meant for all the homeless as well as home owners with dilapidated homes.

Assuming all the beneficiaries of PMAY-G (target of 10mn houses) are fully entitled to the government facilitated loan of Rs70,000 per beneficiary, it could open up a lending opportunity of up to Rs700bn in rural housing over the implementation period (FY17E-FY19E).

**Table: Progress under PMAY (as of mid-May'16)**

| Name of the State | Cities (nos.) | Projects (nos.) | EWS Houses (nos.) | GoI Assis. (Rs.bn.) | Assis. Rel. (Rs.bn.) |
|---|---|---|---|---|---|
| Andhra Pradesh | 59 | 110 | 193,147 | 29 | 3 |
| Bihar | 85 | 85 | 30,216 | 5 | 1 |
| Chhattisgarh | 9 | 11 | 12,670 | 2 | 1 |
| Gujarat | 12 | 77 | 66,983 | 9 | 3 |
| Himachal Pradesh | 9 | 9 | 1,077 | 0 | 0 |
| Jammu & Kashmir | 2 | 2 | 224 | 0 | 0 |
| Jharkhand | 38 | 38 | 20,239 | 3 | 1 |
| Karnataka | 15 | 21 | 16,522 | 2 | 0 |
| Madhya Pradesh | 37 | 45 | 43,393 | 6 | 2 |
| Maharashtra | 10 | 17 | 71,701 | 11 | 0 |
| Mizoram | 8 | 8 | 10,286 | 2 | 0 |
| Orissa | 2 | 6 | 11,548 | 1 | 0 |
| Punjab | 1 | 1 | 1,280 | 0 | 0 |
| Rajasthan | 19 | 23 | 12,307 | 2 | 0 |
| TamilNadu | 175 | 197 | 34,013 | 5 | 0 |
| Telangana | 63 | 144 | 80,481 | 12 | 3 |
| Uttrakhand | 19 | 21 | 2,757 | 0 | 0 |
| West Bengal | 108 | 108 | 74,880 | 11 | 1 |
| **TOTAL** | **671** | **923** | **683,724** | **100** | **16** |

*Source: MHUPA, GoI; IDBI Capital Research*

## New Real Estate Regulation Act can be a game changer

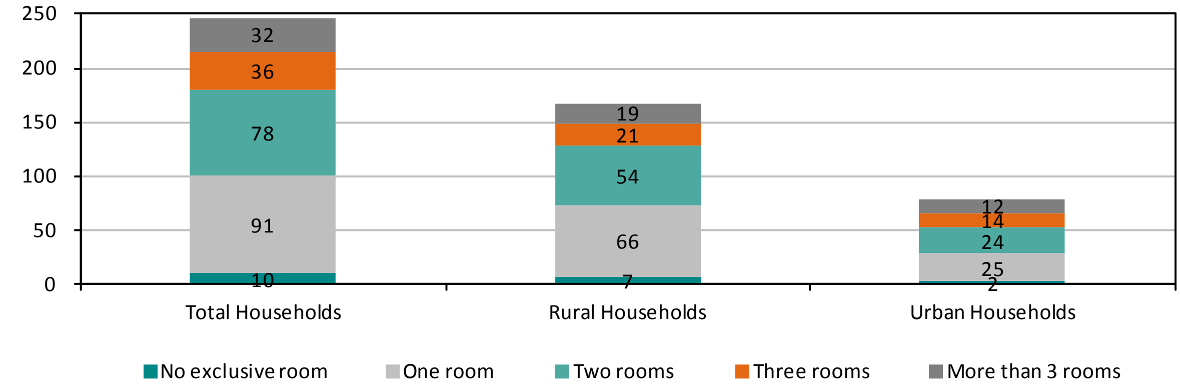
The new Real Estate Regulation Law seeks to set right many shortcomings that currently plague the housing segment in India. Prominent amongst these are 1) inordinate delays in delivering homes to owners, often caused by diversion of funds to other projects / purchasing land banks, 2) illegally constructing and selling flats, the plans for which are not approved by concerned competent authority.

The new law seeks to pin responsibility on developer to deliver the homes on time. This is expected to push non-serious players / speculators out of the arena and bring in transparency as well as confidence in the housing market. Our interaction with sector participants suggests the new law should a) provide a fillip to residential sales, b) attract more FDI into Indian realty, and c) cut down speculator participation. On the flip side, it could slow down number of new project launches initially.

## An upgrade in size? Large proportion of homes are single room tenements

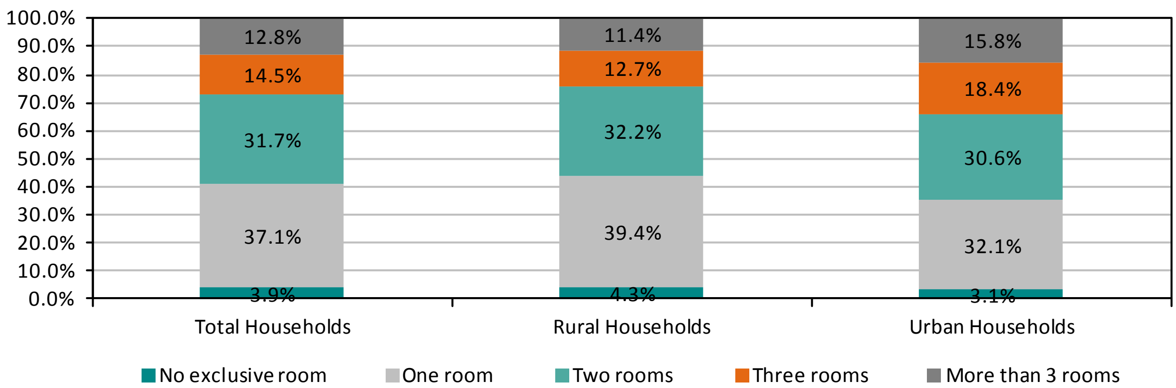
Another element which could be a structural driver for housing can be the size (in terms of area) of homes. The quality of housing differs significantly with accommodations with no exclusive room or one room constituting 41% of total households. These could be slums (legal or illegal) or apartment blocks (1RK flats) that could come up for rehabilitation / redevelopment. This typically should lead to higher housing stock though it has it's own set of challenges – the Dharavi redevelopment in Mumbai being a case in point. Nevertheless, registered co-operative housing societies continue to get redeveloped with existing owners typically getting higher carpet area in the new redeveloped buildings.

**Figure: Significant households are single room tenements**




*Source: Census of India 2011; IDBI Capital Research*

**Figure: ~41% homes on all India basis are without an exclusive room or have one room**




*Source: Census of India 2011; IDBI Capital Research*

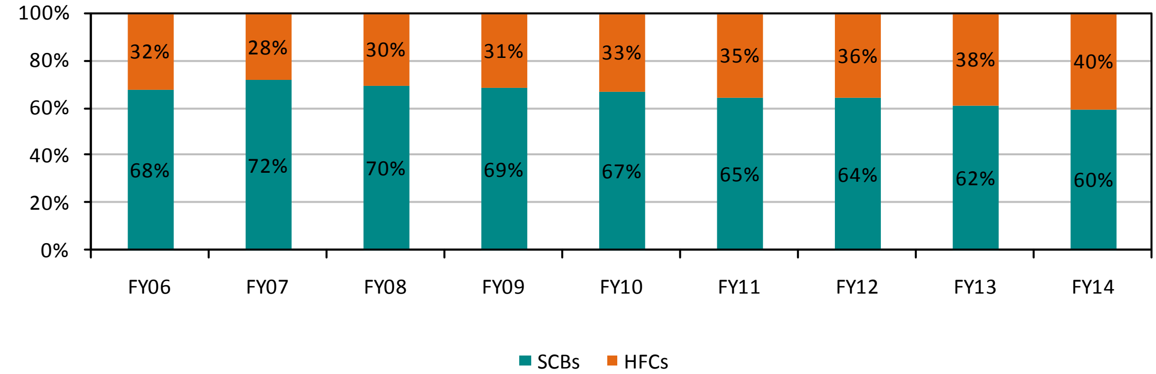
## Business Scenario: It's a tough game and HFCs are doing well

### HFCs market share creeping up

Despite the stiff pricing competition from SCBs, HFCs market share in retail housing loans has seen a steady improvement from FY08. A comparison of housing loan growth rates for SCBs (housing loans data from RBI) and HFCs (housing loan data from NHB) shows HFCs improved their share in housing loans by ~10% FY08-FY14 (NHB releases annual housing report with one year lag, FY16 yet to be released). While aggregating SCB and NHB housing data for this comparison, we presume bank financing to HFCs is reported/classified separately in the NBFC category by RBI/Banks. But assuming bank lending to NBFCs adds up in the housing loan data, it could mean HFCs have a better market share compared to banks.

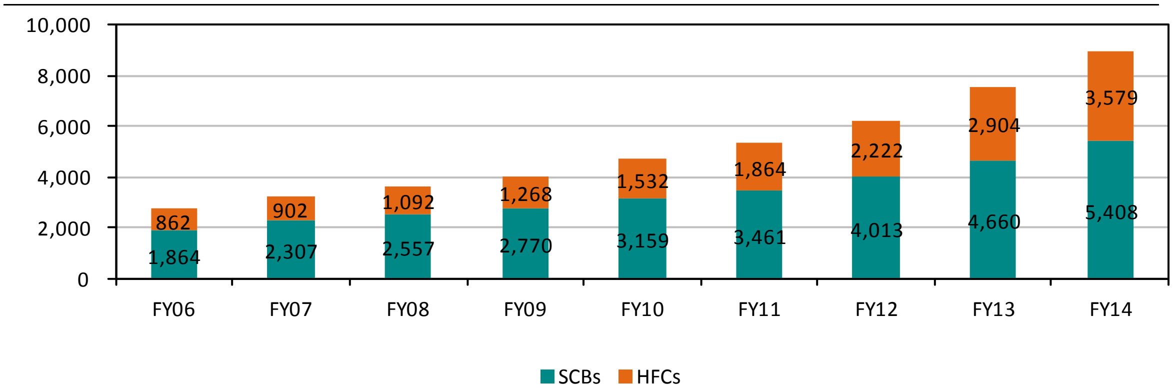
The rising market share of HFCs in our opinion confirms few key fundamental growth drivers for HFCs: a) the service proposition of fast turnaround time remains a key consideration for borrowers, b) pricing difference between SCBs and HFCs has narrowed enough to make the borrower price agnostic.

**Figure: Rising share of HFCs in housing loans**




*Source: NHB; RBI; IDBI Capital Research*

**Figure: Rising share of HFCs in housing loans**

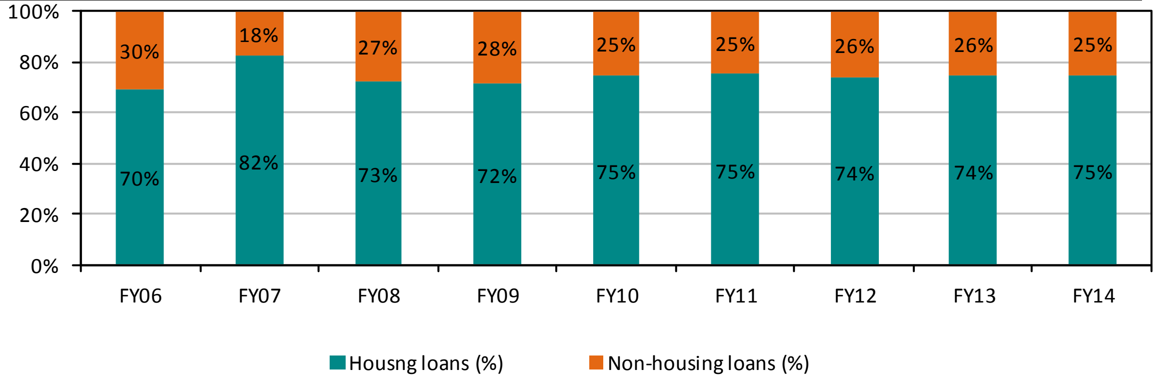



*Source: NHB; RBI; IDBI Capital Research*

### Mix of HFCs' portfolio between housing and non-housing loans steady

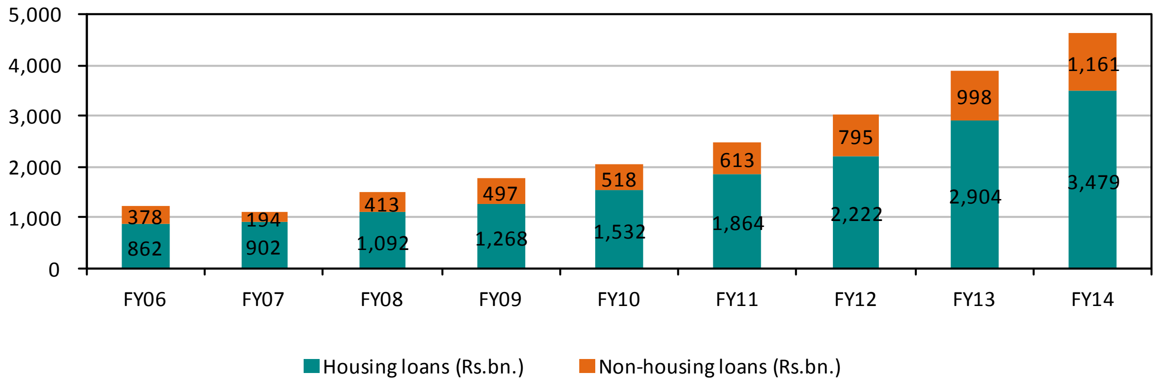
Though HFCs have recently focused aggressively on growing the non-individual as well as individual non-housing (typically LAP, LRD, developer loans) piece, the growth nevertheless has held strong in the core housing loans business too. While growth in non-individual piece did accelerate for some HFCs, it's overall proportion in the loan book remains below the decadal peak of 30% observed in FY06. We see this as strength of momentum in HFCs' core business of housing finance. Since latest aggregated data for HFCs is not available, a look at the portfolios of top 4 HFCs, which constitute a lion's share of HFC loans suggests the share of non-individual loans has remained fairly steady since FY10.

**Figure: Share of non-housing loans steady…**




*Source: NHB; IDBI Capital Research*

**Figure: Rising share of HFCs in housing loans**

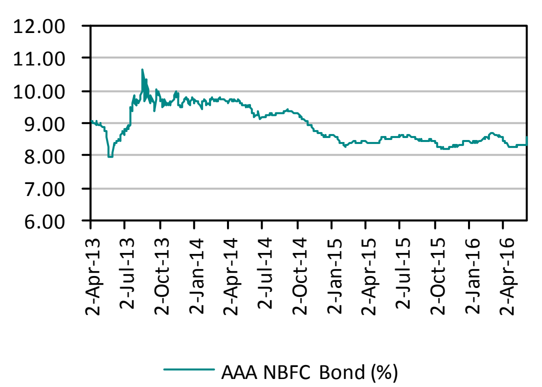



*Source: NHB; IDBI Capital Research*

- **Borrowing costs are softening**

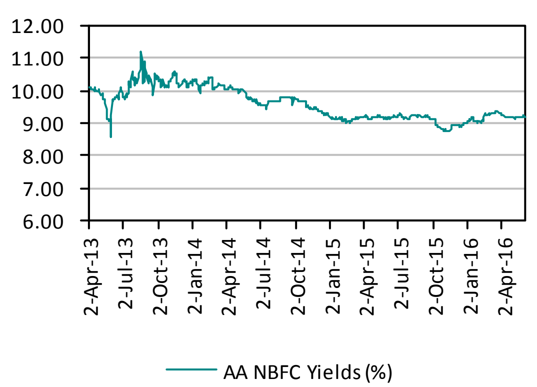
Borrowing costs have softened for HFCs over the course of last two years. The softening has however been higher for AAA compared to AA borrowers (see charts below). Nevertheless, the relatively stable spreads shows the HFCs have been able to manage the pricing pressure on lending side well. Also, the strengthening of spreads in some cases like LICHF is also a combination of changing product mix as well as softening borrowing costs. HFCs have a spread improvement opportunity. We believe spread improvement opportunity purely due to softening borrowing costs could be limited unless HFCs are running a mismatched ALM (that can hurt when rates turn).

**Figure: AAA NBFC bond yields averaged 8.34% in Q1FY17 vs. 9.5% in Q1FY15**




*Source: Bloomberg; IDBI Capital Research*

**Figure: AA NBFC bond yields averaged 9.2% in Q1FY17 vs. 9.9% in Q1FY15**

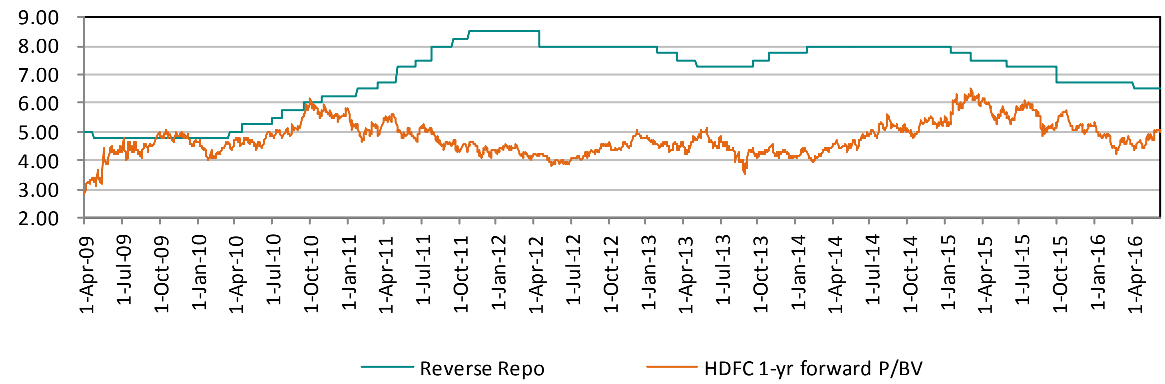



*Source: Bloomberg; IDBI Capital Research*

- **Do HFC valuations improve in a softer rate scenario? The correlation is weak…**

…and in fact over the cycles, the 1-year forward P/BV shows almost nil correlation to the RBI Repo cycle. Nevertheless, if observed closely, the charts below do tell a story. The valuations appear to improve in the initial tightening phase of monetary cycle but discontinue and begin to de-rate after a period if tightening continues. Similarly, valuations begin improving as monetary easing begins and stay stable till initial phase of next tightening. However, in the last one year, HDFC's valuations have weakened even as monetary easing has continued!

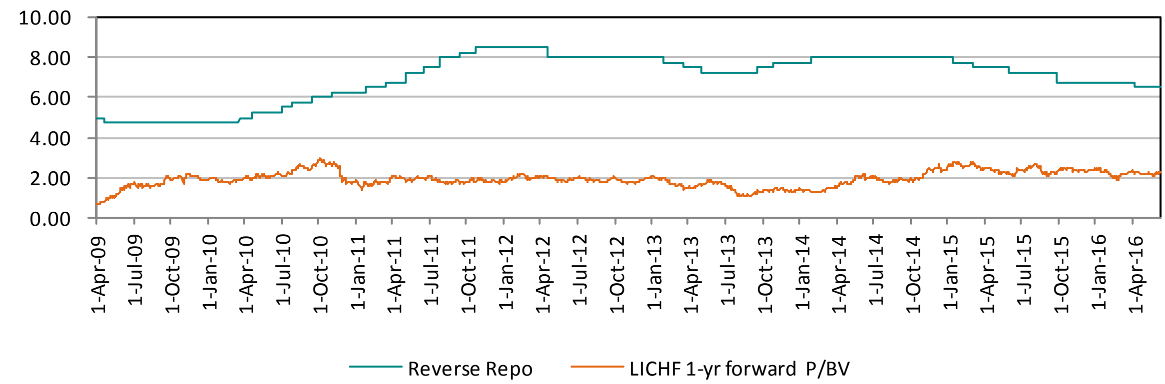
**Figure: HDFC 1-yr fwd P/BV valuation and RBI Repo rate over rate cycles – nil statistical correlation**




*Source: NHB; IDBI Capital Research*

LICHF's valuation trends appear more agnostic to Repo movement (flattish graph) though the correlation is similar to that of HDFC exhibiting close to nil correlation.

**Figure: LICHF 1-yr fwd P/BV valuation and RBI Repo rate over rate cycles – nil statistical correlation**




*Source: NHB; IDBI Capital Research*

We haven't plotted Repco since it's public listing history is a short (just over three years). Secondly, it has seen a strong and sustained valuation improvement, the reasons for which we believe are less correlated to RBI's actions and more geared to it's business segment.

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# Company Section

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June 13, 2016

COMPANY REPORT

# HDFC Ltd.

***Housing finance + much more*** 

BUY

**Nifty: 8,170; Sensex: 26,636**

| | |
|---|---|
| **CMP** | **Rs1,231** |
| **Target Price** | **Rs1,429** |
| **Potential Upside/Downside** | **+16%** |

**Key Stock Data**

| | |
|---|---|
| Sector | Housing Finance |
| Bloomberg / Reuters | HDFC IN / HDFC.BO |
| Shares o/s (mn) | 1,580 |
| Market cap. (Rs mn) | 1,944,664 |
| Market cap. (US$ mn) | 29,129 |
| 3-m daily average vol. | 168,245 |

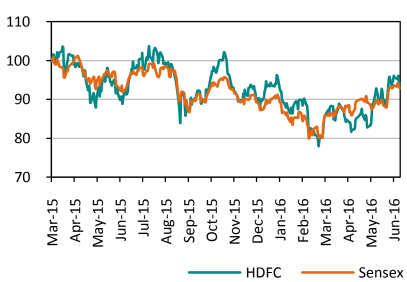
**Price Performance**

| | | | |
|---|---|---|---|
| 52-week high/low | | Rs1,371/1,012 | |
| | -1m | -3m | -12m |
| Absolute (%) | 1 | 7 | 3 |
| Rel to Sensex (%) | (2) | (1) | 4 |

**Shareholding Pattern (%)**

| | |
|---|---|
| FIIs/NRIs/OCBs/GDR | 77.39 |
| MFs/Banks/FIs | 10.39 |
| Govt. | 0.08 |
| Public & Others | 12.13 |

**Relative to Sensex**




*Source: Capitaline*

## Summary


**Though HDFC shall continue to be identified with retail housing finance, given it's pioneering foray into a segment when it did not exist, the company has over the years grown into a valuable financial conglomerate. Our SOTP value for HDFC finds ~40% value accruing from it's associates and subsidiary companies, which are leaders in their respective businesses. HDFC's ~24% capital is leveraged for associate/subsidiary company business and value accretion in these businesses has been significant even as housing finance business continues to grow steadily. We believe HDFC shall continue to deliver value as it's strong franchise across businesses keeps it anchored as a leading financial conglomerate. Our BUY rating and price target of Rs1,429 is based on SOTP valuation.**


## Outlook and Investment Rationale

- **Healthy loan growth rate despite higher sell-downs**

  The overall pace remains in HDFC's loan book remains healthy with the changing loan book composition reflecting the some of the slowdown in real estate sector. The non-housing piece has declined from ~36% in FY12 to ~29% in FY16. We expect HDFC's loan book to show steady momentum and grow at ~17% CAGR FY16-FY18E with a likelihood of non-individual business picking up in near future.

- **Softening spreads to stabilise**

  HDFC's conservative ALM management – near neutral liquidity risk and hedging of interest rate risk has kept volatility out of it's spreads. Nevertheless, changing loan book composition has brought in some softness that is likely to persist in the current interest rate scenario. We estimate (calculated) spreads to average 3% going forward.

- **Profit to grow at ~7% CAGR FY16-FY18E**

  We are currently not factoring any value unlocking from HDFC's life insurance subsidiaries in our estimates. Hence, while NII should show a double-digit momentum, the overall profit growth should be lower. We don't expect asset quality or operating costs to disturb earnings momentum and estimate net profit to grow at ~7% CAGR FY16-FY18E.

- **A valuable franchise to own, initiate with BUY**

  Our call is based on SOTP valuation of HDFC and it's associate/subsidiary companies. We value HDFC's standalone equity by stripping it's core equity investments. We find HDFC generates a significant, +20% RoE on the portion of capital leveraged for housing finance business. **BUY** to our price target of Rs1,429.

**Table: Financial snapshot**

| Y/E: March | NII (Rs mn) | PAT (Rs mn) | EPS (Rs) | BV (Rs) | PE (x) | P/BV (x) | ROE (%) | ROA (%) | GNPA (%) | CAR (%) |
|---|---|---|---|---|---|---|---|---|---|---|
| FY15 | 76,305 | 59,901 | 38.0 | 196.7 | 19.2 | 6.3 | 20.3 | 2.5 | 0.8 | 17.9 |
| FY16 | 83,875 | 70,931 | 44.9 | 216.0 | 16.3 | 5.7 | 21.8 | 2.6 | 0.7 | 16.6 |
| FY17E | 93,261 | 73,505 | 46.5 | 242.1 | 15.7 | 5.1 | 20.3 | 2.4 | 0.7 | 13.1 |
| FY18E | 102,929 | 81,543 | 51.6 | 271.2 | 24.0 | 4.6 | 20.1 | 2.3 | 0.8 | 12.5 |

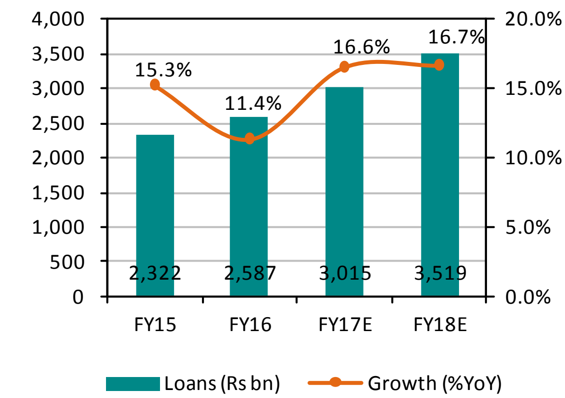
*Source: Company; IDBI Capital Research*

# Investment Rationale

## Steady momentum in loan growth

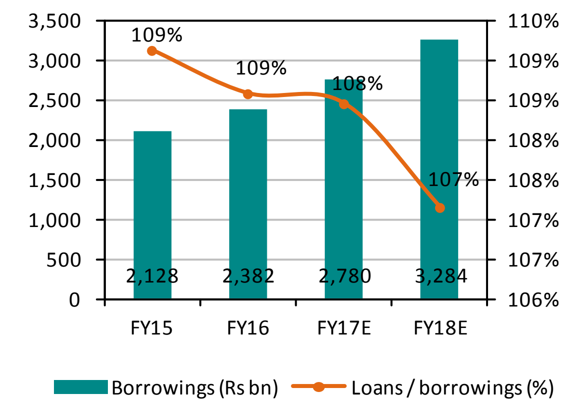
We expect HDFC's loan momentum to stay healthy at mid-teens despite HDFC Bank recently beginning to retain a higher portion of loans it originates. We see the decline in non-housing piece from ~36% in FY12 to ~29% in FY16 as reflective of the slowdown in real estate sector. However, there is a likelihood of the same picking up momentum in near future. We expect HDFC's loan book to show steady momentum and grow at ~17% CAGR FY16-FY18E with a likelihood of non-individual business picking up in near future.

**Figure: Loan growth to stay in mid \teens**




*Source: Company; IDBI Capital Research*

**Figure: Loan / borrowings could slightly moderate**

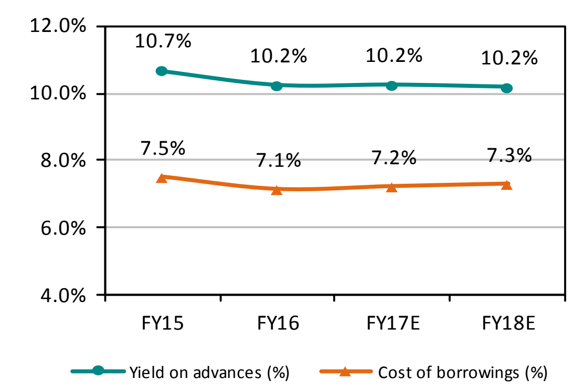



*Source: Company; IDBI Capital Research*

## Spreads could have a slight downward bias

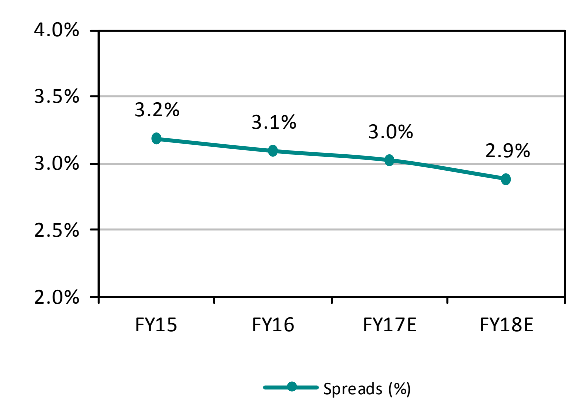
HDFC's conservative ALM management – near neutral liquidity risk and hedging of interest rate risk has kept volatility out of it's spreads. Nevertheless, changing loan book composition has brought in some softness that is likely to persist in the current interest rate scenario. Past experience shows HDFC manages to maintain spreads at +2.2% levels across rate cycles (reported, corresponds to ~3% calculated in FY16). We expect stability in spreads around and estimate the calculated spreads at ~3% going forward.

**Figure: Estimate slight hardening in borrowing costs**




*Source: Company; IDBI Capital Research*

**Figure: …but should not affect spreads…**

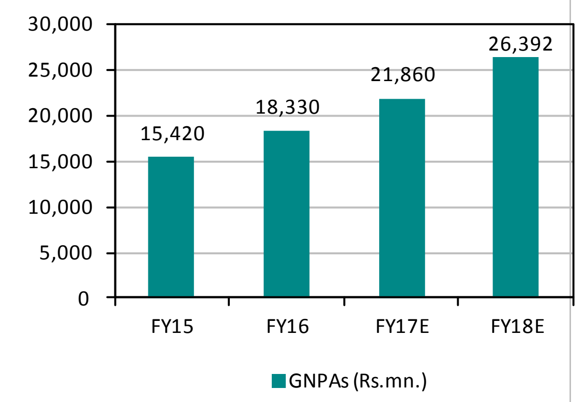



*Source: Company; IDBI Capital Research*

## Stable asset quality

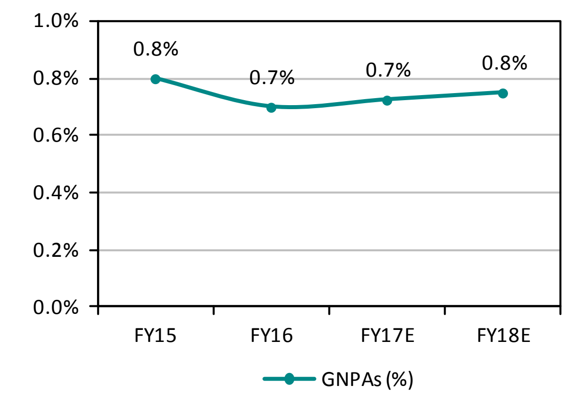
Housing finance companies in general exhibit strong asset quality and HDFC's track record has been extremely sound on asset quality. The costs too have stayed steady over cycles. The rising absolute level of GNPAs should be in line with the increasing book size though the ratio should not exceed recently observed patterns of 70-80bps.

**Figure: GNPAs in absolute terms to rise…**




*Source: Company; IDBI Capital Research*

**Figure: …but stay stable in ratio terms**

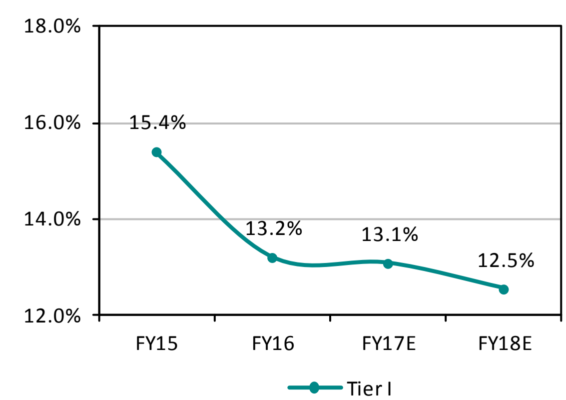



*Source: Company; IDBI Capital Research*

## Capitalisation to stay healthy

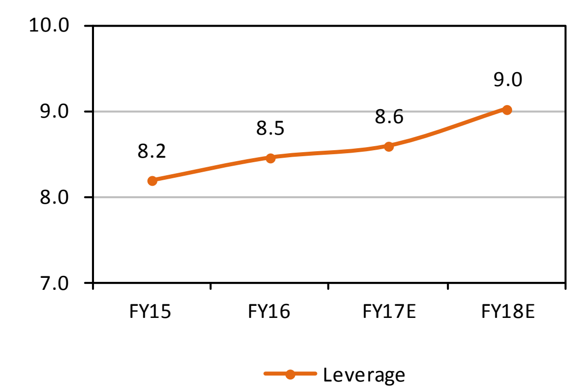
HDFC could likely unlock value in HDFC Life through an IPO during FY17E. The company realized Rs14bn through sale of 9% stake in HDFC Life in FY16. The IPO could see the company realizing some of the value of it's investment in the leading life insurance company. Our capital estimate does not include the profit on sale of investment.

**Figure: Tier 1 capital should stay healthy at ~12.5%**



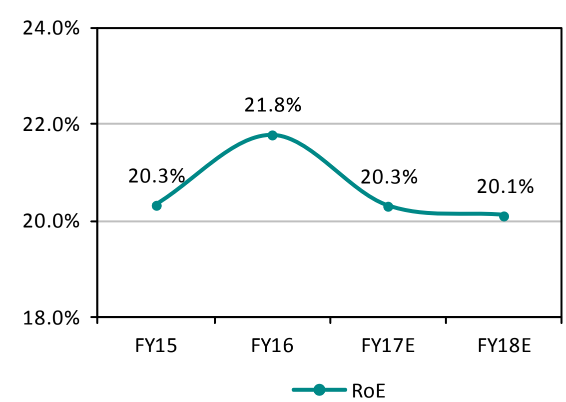

*Source: Company; IDBI Capital Research*

**Figure: Leverage to expand…**



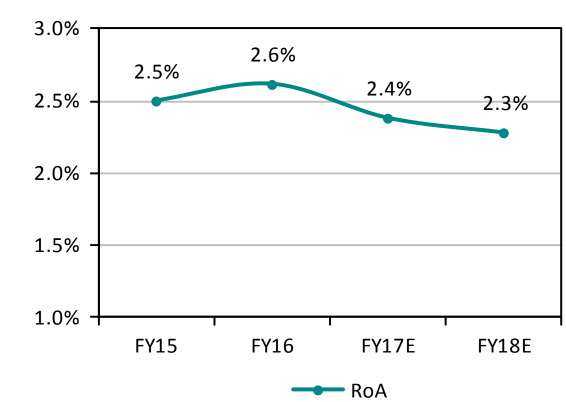

*Source: Company; IDBI Capital Research*

**Figure: RoE to stay robust at ~20%**




*Source: Company; IDBI Capital Research*

**Figure: RoA to average 2.4%**




*Source: Company; IDBI Capital Research*

## Valuation and Recommendation

- **Business leadership and consistent earnings performance keeps SOTP valuation at a premium**

  Given HDFC's financial strength and leadership, it commands a valuation premium to its peers. As stated at outset, HDFC's associate/subsidiaries contribute ~40% to the SOTP value with the rest being generated by the mortgage business. We value the company using SOTP method, assigning housing finance company 4x FY18E ABV. We have chosen to value life insurance business based on recent transactions, asset management business is valued at 5% of the average AUM and bank is valued at fair value – giving us Rs553 per share of HDFC for the investments in subsidiaries/associates. The SOTP target price of Rs1,429 gives us a potential upside of +16% from CMP.

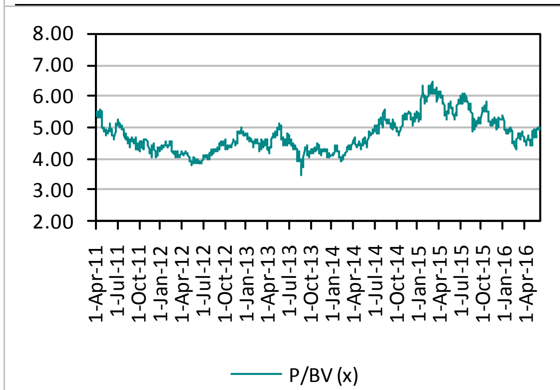
**Table: Sum of the parts valuation for HDFC and its subsidiaries, associates**

| HDFC & HDFC Subsidiaries | Metho-dology | Inv. (BV) Rs.mn. | Val. (x) | Val. Rs.mn. | Eq. stake (%) | Attributable Val. (Rs.) | Value/share Rs. |
|---|---|---|---|---|---|---|---|
| HDFC Ltd. (core mortgage business) | P/ABV | 346,542 | 4.0 | 1,386,168 | 100.0 | 1,386,168 | 877 |
| **Listed subs. / asso.** | | | | | | | |
| HDFC Bank Ltd. | Value at TP (Rs1,224) | 55,497 | 3.5 | 3,094,517 | 19.6 | 606,525 | 384 |
| Gruh Finance Ltd. | CMP | 607 | - | 103,667 | 58.6 | 60,739 | 38 |
| **Value of listed subsidiaries / associate cos.** | | | | | | | **422** |
| **Unlisted subsidiaries / associate companies** | | | | | | | |
| HDFC Asset Management Co. Ltd. | Avg. AUM (FY18E) | 2,359 | 5% | 93,708 | 60.0 | 56,225 | 36 |
| HDFC Standard Life Insurance Co. Ltd. | Latest transaction | 13,162 | - | 188,889 | 61.6 | 116,412 | 74 |
| HDFC Ergo General Insurance Co. Ltd. | Latest transaction | 4,444 | - | 49,001 | 50.7 | 24,858 | 16 |
| Residual equity investment | P/BV | 5,818 | 1.5 | 8,727 | 100.0 | 8,727 | 6 |
| **Value of unlisted subs. / asso.** | | | | | | | **131** |
| **Total equity investment in subs. / asso.** | | **81,887** | | | | | |
| **SOTP valuation / share (Rs.)** | | | | | | | **1,429** |

*Source: Company, IDBI Capital Researche*

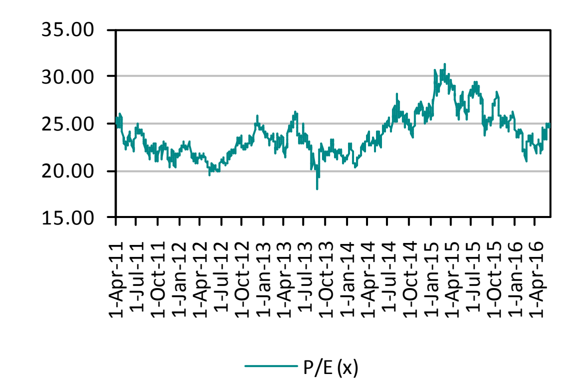
We do not attribute any holding company discount to the value of unlisted subsidiaries of HDFC Ltd. Holding company discount is typically applied for either a) lack of control over subsidiary company, b) poor marketability of subsidiary company securities including likely difficulties in raising capital. We believe neither of these conditions apply to HDFC's subsidiaries and certainly not to HDFCB. We also believe the discount applicable to HDFC Life shall also dilute as the company gears for listing. We therefore do not apply holding company discount to HDFC's stake in HDFCB and HDFC Life.

**Figure: HDFC trades at 5x 1-yr forward P/BV…**




*Source: Company; IDBI Capital Research*

**Figure: …and 25x P/E**




*Source: Company; IDBI Capital Research*

## About the Company

Housing Development Finance Corporation Ltd (HDFC Ltd) was founded in 1977 by Mr. H T Parekh with the primary objective of encouraging home ownership by providing long-term finance to households. It was a pioneering foray in a segment that was considered risky and where lending precedence did not exist. HDFC became a leading retail mortgage financier eventually spawning into a diversified financial conglomerate. The company has its presence in ~2,400 towns and cities across the country with a network of 304 branches. It also has offices in Dubai, London and Singapore and service associates in the Middle-East region, to provide housing loans and property advisory services to Non-Resident Indians (NRIs) and Persons of Indian Origin (PIOs).

**Table: Subsidiary And Associate Companies**

| | Ownership % | Shares owned mn. | BV of equity* Rs.mn. |
|---|---|---|---|
| **Subsidiary Companies** | | | |
| GRUH Finance Ltd. | 58.6 | 213 | 607 |
| HDFC Asset Management Co. Ltd. | 59.8 | 15 | 2,359 |
| HDFC Standard Life Insurance Co. Ltd.* | 70.7 | 1,409 | 15,088 |
| HDFC ERGO General Insurance Co. Ltd.* | 73.6 | 397 | 6,450 |
| HDFC Property Ventures Ltd. | 80.5 | 1 | 10 |
| HDFC Venture Capital Ltd. | 80.5 | 0 | 4 |
| Credila Financial Services Pvt. Ltd. | 89.5 | 42 | 480 |
| HDFC Developers Ltd. | 100.0 | 3 | 31 |
| HDFC Education and Development Services Pvt. Ltd. | 100.0 | 15 | 151 |
| HDFC Holdings Ltd. | 100.0 | 2 | 1,024 |
| HDFC Investments Ltd. | 100.0 | 27 | 662 |
| HDFC Realty Ltd. | 100.0 | 8 | 73 |
| HDFC Sales Pvt. Ltd. | 100.0 | 4 | 40 |
| HDFC Trustee Co. Ltd. | 100.0 | 0 | 1 |
| HDFC Ventures Trustee Co. Ltd. | 100.0 | 0 | 1 |
| **Associate Companies** | | | |
| HDFC Bank Ltd. | 21.7 | 393 | 55,497 |
| India Value Fund Advisors Pvt. Ltd. | 21.5 | 1 | 0 |
| RuralShores Business Services Pvt. Ltd. | 27.5 | 0 | 25 |
| **TotalL*** | | | **82,502** |

** Based on FY15 annual report. HDFC's stake in HDFC Life Insurance has since declined to 61.6% and that in HDFC ERGO General Insurance to 50.7%. The book value of equity investments in associates and subsidiaries stood at Rs81,887mn in FY16. These changes are factored in our SOTP valuation.*

*Source: Company, IDBI Capital Research*

# Financial Summary

### Profit & Loss Account (Rs mn)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Interest income | 256,056 | 277,620 | 316,344 | 364,008 |
| Interest expense | 179,751 | 193,745 | 223,083 | 261,079 |
| **Net interest income** | **76,305** | **83,875** | **93,261** | **102,929** |
| *Growth (% YoY)* | *14.5* | *9.9* | *11.2* | *10.4* |
| **Other income** | **18,653** | **27,446** | **22,789** | **26,839** |
| **Operating income** | **94,958** | **111,321** | **116,051** | **129,768** |
| *Growth (% YoY)* | *16.3* | *17.2* | *4.2* | *11.8* |
| Staff cost | 3,285 | 3,491 | 3,491 | 3,491 |
| Other operating expenses | 3,782 | 4,099 | 4,534 | 5,095 |
| Total operating expenses | 7,066 | 7,590 | 8,025 | 8,586 |
| *Growth (% YoY)* | *12.5* | *7.4* | *5.7* | *7.0* |
| **Operating profit** | **87,891** | **103,731** | **108,026** | **121,182** |
| *Growth (% YoY)* | *16.6* | *18.0* | *4.1* | *12.2* |
| Non-tax provisions | 1,650 | 2,650 | 3,019 | 4,692 |
| **Profit before tax** | **86,241** | **101,081** | **105,007** | **116,490** |
| *Growth (% YoY)* | *15.9* | *17.2* | *3.9* | *10.9* |
| Taxes | 26,340 | 30,150 | 31,502 | 34,947 |
| *Tax rate (%)* | *30.5* | *29.8* | *30.0* | *30.0* |
| **Profit after tax** | **59,901** | **70,931** | **73,505** | **81,543** |
| *Growth (% YoY)* | *10.1* | *18.4* | *3.6* | *10.9* |

### Balance Sheet (Rs mn)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Equity | 3,149 | 3,160 | 3,160 | 3,160 |
| Reserves | 306,550 | 338,051 | 381,547 | 431,404 |
| Networth | 309,700 | 341,211 | 384,706 | 434,564 |
| Borrowings | 2,127,874 | 2,381,930 | 2,792,889 | 3,290,667 |
| Current liabilities | 101,943 | 164,388 | 129,629 | 158,874 |
| **Total liabilities** | **2,539,516** | **2,887,528** | **3,307,224** | **3,884,105** |
| Loans | 2,322,311 | 2,586,580 | 3,028,211 | 3,525,754 |
| Investments | 142,943 | 153,454 | 153,454 | 153,454 |
| Current assets | 67,496 | 140,849 | 118,846 | 197,849 |
| Fixed assets | 6,766 | 6,645 | 6,712 | 7,047 |
| **Total assets** | **2,539,516** | **2,887,528** | **3,307,224** | **3,884,105** |

### Growth (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Total assets | 12.7 | 13.7 | 13.9 | 17.6 |
| Housing loans | 15.3 | 11.4 | 16.6 | 16.7 |
| Borrowings | 14.7 | 11.9 | 16.7 | 18.1 |

### Earnings Ratios (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Average yield on funds | 10.7 | 10.2 | 10.2 | 10.2 |
| Average cost of funds | 7.5 | 7.1 | 7.2 | 7.3 |
| Spread | 3.2 | 3.1 | 3.0 | 2.9 |
| RoE | 20.3 | 21.8 | 20.3 | 20.1 |
| RoA | 2.5 | 2.6 | 2.4 | 2.3 |

### Cost Ratios (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Op. exps. / avg. assets | 0.3 | 0.3 | 0.3 | 0.2 |
| Op. exps / income | 7.4 | 6.8 | 6.9 | 6.6 |

### Asset Quality (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Gross NPAs (Rs.mn.) | 15,420 | 18,330 | 21,860 | 26,392 |
| Gross NPAs (%) | 0.8 | 0.7 | 0.7 | 0.8 |

### Capital Adequacy (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Capital adequacy | 17.9 | 16.6 | 13.1 | 12.5 |
| Tier I | 15.4 | 13.2 | 13.1 | 12.5 |
| Leverage (x) | 8.2 | 8.5 | 8.6 | 9.0 |

### Valuation

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| EPS (Rs.) | 38.0 | 44.9 | 46.5 | 51.6 |
| Adjusted book value (Rs.) | 196.7 | 216.0 | 242.1 | 271.2 |
| P / E | 19.2 | 16.3 | 15.7 | 24.0 |
| P / BV | 6.3 | 5.7 | 5.1 | 4.6 |
| Div. payout (%) | 39.4 | 37.9 | 37.5 | 37.5 |

*Source: Company; IDBI Capital Research*

## RoAA decomposition

(%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Interest earned | 10.68 | 10.23 | 10.24 | 10.15 |
| Interest expended | 7.50 | 7.14 | 7.05 | 7.01 |
| Net interest income | 3.18 | 3.09 | 3.19 | 3.14 |
| Other income | 0.78 | 1.01 | 0.74 | 0.75 |
| Operating income | 3.96 | 4.10 | 3.92 | 3.89 |
| Operating expenses | 0.29 | 0.28 | 0.26 | 0.24 |
| Pre-provision profits (PPP) | 3.67 | 3.82 | 3.66 | 3.65 |
| Provisions | 0.07 | 0.10 | 0.10 | 0.13 |
| Profit before taxes | 3.60 | 3.73 | 3.57 | 3.52 |
| Taxes | 1.10 | 1.11 | 1.07 | 1.06 |
| Profit after taxes | 2.50 | 2.61 | 2.50 | 2.46 |

*Source: Company; IDBI Capital Research*

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June 13, 2016

IDBI capital

COMPANY REPORT

# LIC Housing Finance

***Reverting to stronger earnings***

BUY

**Nifty: 8,170; Sensex: 26,636**

| | |
|---|---|
| **CMP** | **Rs473** |
| **Target Price** | **Rs560** |
| **Potential Upside/Downside** | **+18%** |

### Key Stock Data

| | |
|---|---|
| Sector | Housing Finance |
| Bloomberg / Reuters | LICHF IN / LIC.BO |
| Shares o/s (mn) | 505 |
| Market cap. (Rs mn) | 239,042 |
| Market cap. (US$ mn) | 3,581 |
| 3-m daily average vol. | 151,321 |

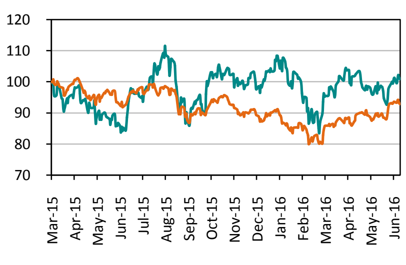
### Price Performance

| | | | |
|---|---|---|---|
| 52-week high/low | | | Rs526/389 |
| | -1m | -3m | -12m |
| Absolute (%) | 3 | 3 | 18 |
| Rel to Sensex (%) | (1) | (5) | 19 |

### Shareholding Pattern (%)

| | |
|---|---|
| Promoters | 40.31 |
| FIIs/NRIs/OCBs/GDR | 27.84 |
| MFs/Banks/FIs | 4.67 |
| Govt. | 1.46 |
| Public & Others | 25.72 |

### Relative to Sensex




*Source: Capitaline*

## Summary

**The introduction of a new loan product in LAP category has boosted LICHF's earnings momentum while supporting growth, which though robust, had remained concentrated in the traditional housing finance segment. LICHF's loan mix had suffered adversely when it's corporate loan book kept unwinding (declining from ~9% in FY11 to ~2% in FY14) and an asset quality event made the company go slow in the non-individual space. This alongwith pricing competition from aggressive banks kept up the pressure on spreads.**

**We expect LICHF to remain in a healthy earnings trajectory supported by a benign funding environment and strong growth in high yield LAP segment. Initiate with BUY and price target of Rs560.**

## Outlook and Investment Rationale

- **Pick up in high yield loan product**

  LICHF introduced LAP product in FY14 and has since seen a strong pick up in it's disbursals, adding ~100%YoY in FY16. This product, which is typically sold to salaried segment, belongs to high yield segment of +12% and has provided a strong fillip to LICHF's earnings, replacing the yet tepid developer portfolio. We expect LAP proportion to move to ~12% of LICHF portfolio FY16-FY18E taking a strong share in incremental loan growth.

- **Strong asset quality**

  LICHF has maintained a strong asset quality, with GNPAs at just 60bps thus comparing at par with HDFC. While the new LAP product may appear as a high risk product, it's relatively conservative LTV of ~60% at origination as well as the fact that it is sold to past, salaried customers builds risk mitigation buffers at origination itself.

- **Estimate net profit CAGR ~14%/RoE ~19% FY16-FY18E**

  We expect LICHF to benefit from softening cost of funds as well as an expanding high yield LAP portfolio with origination and overall operating costs staying muted. This should provide a healthy upside to the profit growth going forward, which we expect to stay at +14% CAGR FY16-FY18E and generate a RoE of ~19% FY16-FY18E.

- **Valuations to stay strong on back of robust earnings**

  We initiate coverage on LICHF with a **BUY** rating and a price target of Rs560. We believe LICHF's valuations shall improve to cyclically stronger levels given the RoE outlook supported by a changing asset mix. We value LICHF at 2.4x FY18E ABV Rs235.5.

**Table: Financial snapshot**

| Y/E: March | Op. inc. (Rs mn) | PAT (Rs mn) | EPS (Rs) | BV (Rs) | PE (x) | P/BV (x) | ROE (%) | ROA (%) | GNPA (%) | NNPA (%) |
|---|---|---|---|---|---|---|---|---|---|---|
| FY15 | 24,884 | 13,862 | 27.5 | 149.7 | 17.2 | 3.2 | 18.1 | 1.3 | 0.6 | 16.5 |
| FY16 | 31,787 | 16,608 | 32.9 | 175.2 | 14.4 | 2.7 | 19.6 | 1.4 | 0.6 | 15.5 |
| FY17E | 35,834 | 18,708 | 37.0 | 202.6 | 12.8 | 2.3 | 18.9 | 1.3 | 0.6 | 14.8 |
| FY18E | 41,179 | 21,423 | 42.4 | 235.5 | 11.2 | 2.0 | 18.7 | 1.3 | 0.6 | 14.0 |

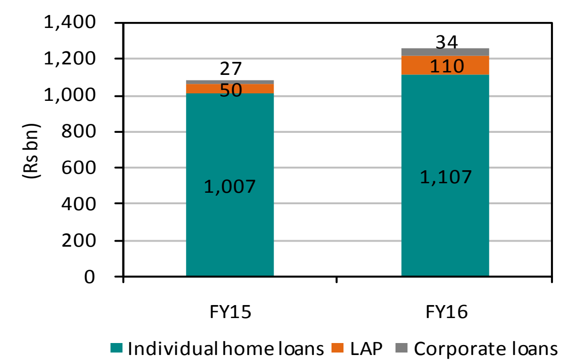
*Source: Company; IDBI Capital Research*

# Investment Rationale

- **New individual LAP product driving growth**

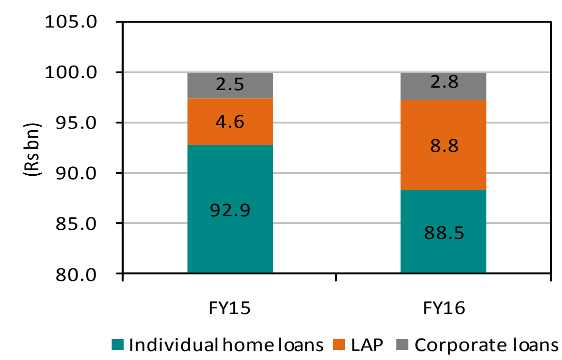
  Based on net outstanding advances, LICHF has derived a strong 50% and 60% incremental growth from LAP in FY15 and FY16 respectively. The proportion of LAP loans increased significantly from close to nil in FY14 to 4.5% in FY15 and 8.7% in FY16 in the overall loan mix. The company expects proportion of LAP to further increase to ~12% in FY17E and stabilize around those levels.

**Figure: LAP showing strong growth…**




*Source: Company; IDBI Capital Research*

**Figure: LAP share almost doubled in FY16**

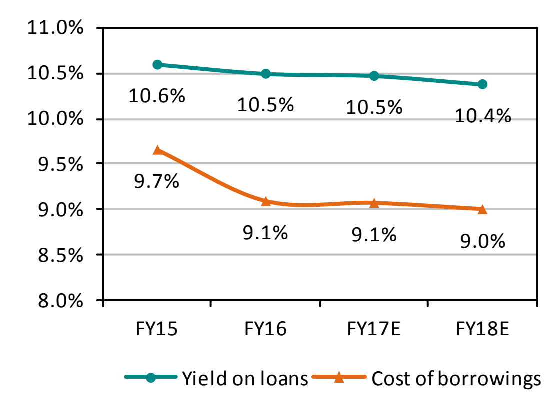



*Source: Company; IDBI Capital Research*

- **Better margins led by yield improvement**

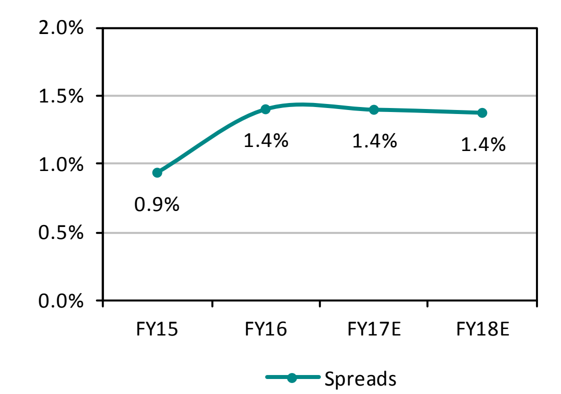
  LICHF went through long period of relatively weaker spread post FY12 as it's non-individual portfolio shrank pulling down overall earnings yield. The subdued phase got over as growth returned in the non-individual loan segment from FY14. As the company continues to build non-individual loan portfolio, we expect LICHF to report stable to improving spreads going forward.

**Figure: Loan yields to remain stable**




*Source: Company; IDBI Capital Research*

**Figure: and reflect in stable spreads**




*Source: Company; IDBI Capital Research*

- **Asset quality in a stable trajectory**

  LICHF has maintained stable asset quality for almost a decade now. It achieved a major turnaround in asset quality post FY07. Prior to 2007, internal risk management had been a weak link creating asset quality troubles. Its GNPAs kept increasing during F00-F05 and peaked at 4.4% in FY05. The NPAs began declining thereafter and have averaged 54bps FY09-FY16.

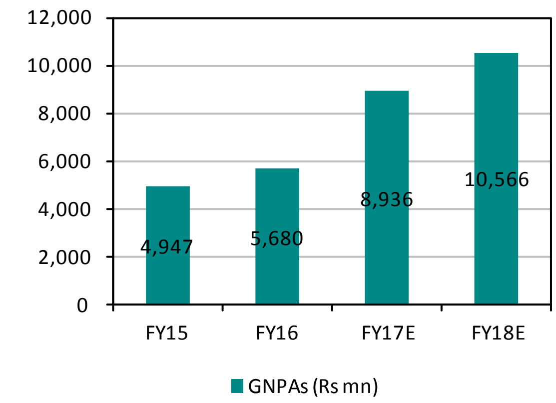
  LICHF improved its asset quality in a two pronged manner:

  1) It initiated and implemented stringent credit appraisal system. The automation of the whole loan sanction procedure, separation of various departments as marketing and appraisals along with introduction of credit scorecards were some of the key initiatives taken in this regard.

2) It vigorously pursued recovery efforts in non-performing accounts.

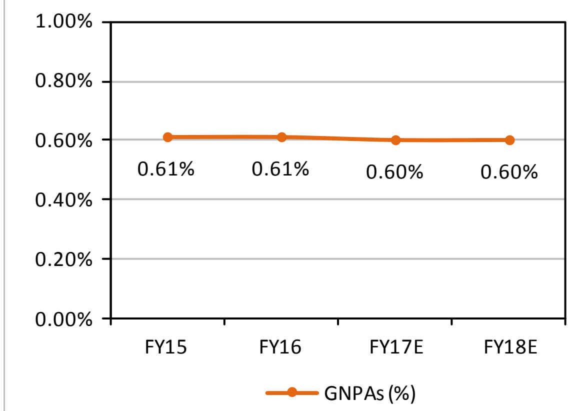
LICHF continues to maintain prudent lending practices with a low incremental LTV of 46.6%. The LAP product also has a modest 60% LTV with significant borrowers from salaried class. We therefore believe LICHF's asset quality is likely to stay stable going forward.

**Figure: GNPAs to rise…**




*Source: Company; IDBI Capital Research*

**Figure: …but ratio should stay flat**

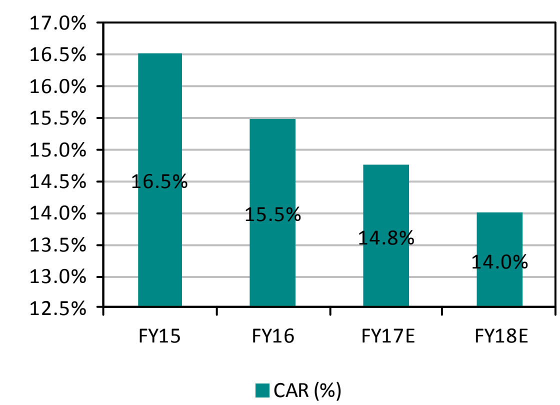



*Source: Company; IDBI Capital Research*

- **Highest leverage amongst peers but comfortable capital**

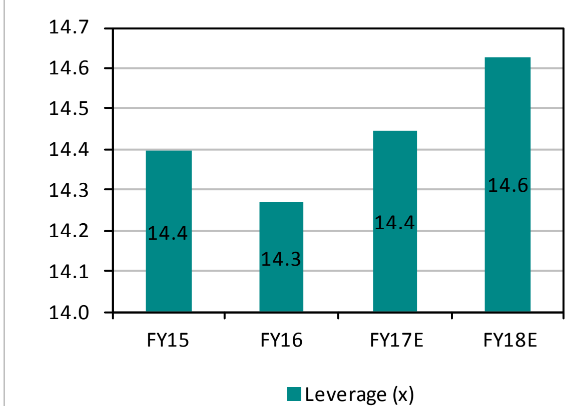
The high leverage-high capital adequacy (including DTL) is on account of continuing low ticket size of loans – Rs1.2mn size of legacy loans and Rs2mn on incremental loans, thereby keeping the risk weights low and freeing up capital to book higher volume of business. The continuing healthy RoEs ensure LIC continues to add sufficient incremental equity to keep Tier 1 at healthy levels.

**Fig.: Tier 1 capital should stay healthy at ~14%**




*Source: Company; IDBI Capital Research*

**Fig.: Leverage likely to stay around 14x**

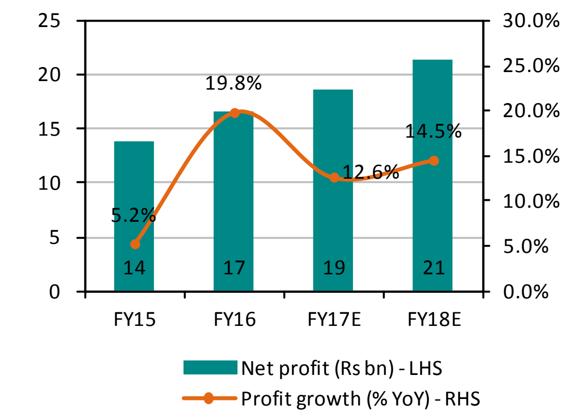



*Source: Company; IDBI Capital Research*

- **Estimate net profit CAGR of ~14% FY16-FY18E**

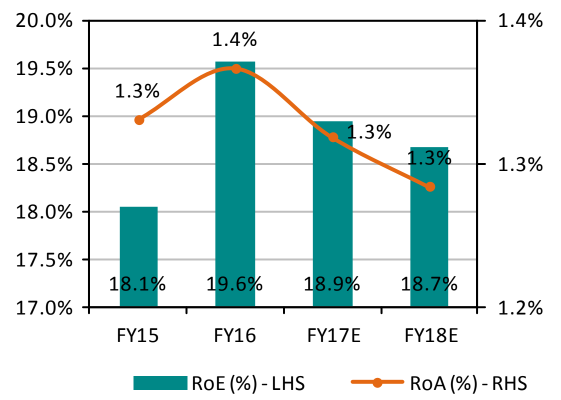
Compared to the ~12% CAGR FY14-FY16, we expect LICHF net profit to improve to ~14% CAGR FY16-FY18E while the RoE should stay stable at 18.8% FY17E-FY18E. LICHF's changing loan mix and stable asset quality provide strong support to it's earnings which can improve with stronger portfolio growth momentum. Our assumption of absolutely stable asset quality also remains key earnings risk in our estimates.

**Figure: Profit to touch Rs21bn in FY18E**




*Source: Company; IDBI Capital Research*

**Figure: RoEs to stay in high teens**




*Source: Company; IDBI Capital Research*

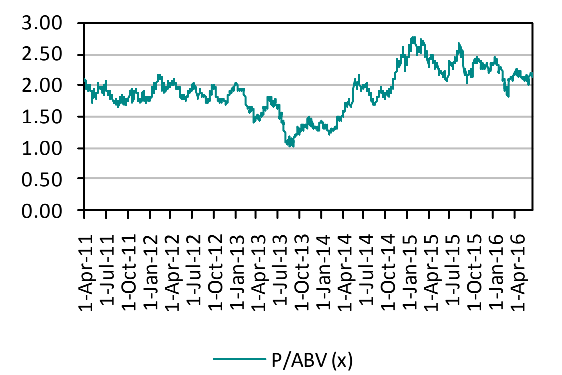
# Valuation and Recommendation

- **Valuations improving on back of better earnings, initiate with BUY**

  Despite a higher current tax rate, LICHF has been able to improve it's profitability driven by a robust core income growth. This has pulled up the RoE from mid-teens to high-teens between FY12-FY16 even as the corporate tax rate, due to a regulatory requirement, went up from 27% to 34%. LICHF's valuations have begun reflecting this positive trend.

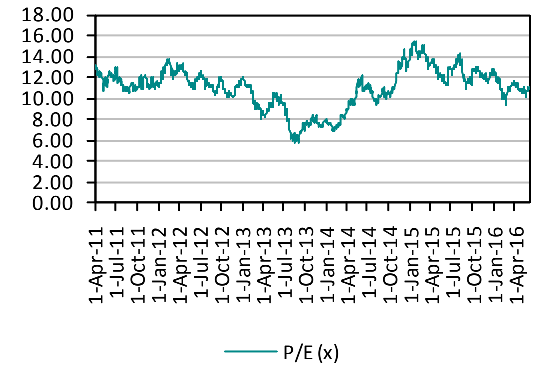
  We initiate coverage on LICHF with a **BUY** recommendation and price target of Rs560 based on 2.4x FY18E ABV while our FY18E EPS Rs42.4 discounts the target price 13.2x. We don't anticipate any dilution in BV / EPS due to equity dilution (which is unlikely to happen given the robust capitalization and healthy earnings).

**Fig.: LICHF trading at 1Y forward P/ABV**




*Source: Company; NSE, IDBI Capital Research*

**Fig.: LICHF trading at 1Y forward P/E**




*Source: Company; NSE, IDBI Capital Research*

## About the Company

Promoted by Life Insurance Corporation in 1989, LIC Housing Finance Ltd (LIC HF) is among the top-3 housing finance companies in India. It went public in 1994 and launched its maiden GDR issue in 2004, which is listed on the Luxembourg Stock Exchange.

LICHF's core area of operations is long term finance to individuals for purchase / construction / repair and renovation of new / existing flats / houses. It also provides finance on existing property for business / personal needs and gives loans to professionals for purchase / construction of clinics / nursing homes / diagnostic centres / office space and purchase of equipments.

The company had a network of 234 marketing offices across India in addition to several hundred direct sales agents (DSAs), a few thousand home loan agents (HLAs) and customer relationship associates (CRAs) to extend its marketing reach. The company has a representative office in Dubai and Kuwait to cater to the NRI in the GCC countries

### Subsidiaries

- **LICHFL Care Homes Ltd.:** Incorporated on September 11, 2001, the company aims to address the gap in housing for the senior citizens of the country.
- **LICHFL Financial Services Ltd.:** Founded on October 31, 2007, LICHFL Financial Services Ltd undertakes non-fund based activities like marketing of housing loans, insurance products, credit card, mutual fund and personal loan. It became operational in 2008-09.
- **LICHFL Trustee Company Private Ltd.:** The company was established on March 5, 2008 to foray into the business of trustees of venture capital funds in India and offshore fund. The company acts as trustee of the fund raised through private placement and public offer.
- **LICHFL Asset Management Company Private Ltd.:** The company was incorporated on February 14, 2008 for undertaking the business of managing, advising, administering venture funds, unit trust and investment trust in India and abroad.

# Financial Summary

### Profit & Loss Account (Rs mn)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Interest income | 105,761 | 122,509 | 143,296 | 168,225 |
| Interest expense | 83,102 | 93,068 | 110,169 | 130,178 |
| **Net interest income** | **22,658** | **29,441** | **33,128** | **38,047** |
| *Growth (% YoY)* | *18.3* | *29.9* | *12.5* | *14.8* |
| Other income | 2,226 | 2,346 | 2,706 | 3,132 |
| **Operating income** | **24,884** | **31,787** | **35,834** | **41,179** |
| *Growth (% YoY)* | *15.2* | *27.7* | *12.7* | *14.9* |
| Staff cost | 1,293 | 1,503 | 1,967 | 2,310 |
| Other operating expenses | 2,499 | 3,183 | 3,493 | 4,091 |
| Operating expenses | 3,792 | 4,687 | 5,460 | 6,401 |
| *Growth (% YoY)* | *20.0* | *23.6* | *16.5* | *17.2* |
| **Operating profit** | **21,092** | **27,100** | **30,374** | **34,778** |
| *Growth (% YoY)* | *14.4* | *28.5* | *12.1* | *14.5* |
| Non-tax provisions | 73 | 1,465 | 2,029 | 2,319 |
| **Profit before tax** | **21,019** | **25,636** | **28,345** | **32,459** |
| *Growth (% YoY)* | *15.1* | *22.0* | *10.6* | *14.5* |
| **Taxes** | 7,158 | 9,028 | 9,637 | 11,036 |
| *Tax rate (%)* | *34.1* | *35.2* | *34.0* | *34.0* |
| **Profit after tax** | **13,862** | **16,608** | **18,708** | **21,423** |
| *Growth (% YoY)* | *5.2* | *19.8* | *12.6* | *14.5* |

### Balance Sheet (Rs mn)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Equity | 1,010 | 1,010 | 1,010 | 1,010 |
| Reserves | 77,174 | 90,450 | 105,038 | 122,342 |
| Networth | 78,184 | 91,460 | 106,048 | 123,352 |
| Borrowings | 965,319 | 1,109,360 | 1,319,851 | 1,572,818 |
| Current liabilties | 81,947 | 104,158 | 106,199 | 108,272 |
| **Total liabilities** | **1,125,450** | **1,304,978** | **1,532,098** | **1,804,442** |
| | | | | |
| Loans | 1,083,607 | 1,251,732 | 1,485,963 | 1,756,642 |
| Investments | 2,371 | 2,718 | 2,718 | 2,718 |
| Fixed assets | 797 | 920 | 1,104 | 1,325 |
| Current assets | 38,675 | 49,607 | 42,313 | 43,757 |
| **Total assets** | **1,125,450** | **1,304,978** | **1,532,098** | **1,804,442** |

*Source: Company; IDBI Capital Research*

### Growth (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Total assets | 17.5 | 16.0 | 17.4 | 17.8 |
| Loans | 18.6 | 15.5 | 18.7 | 18.2 |
| Borrowings | 17.7 | 14.9 | 19.0 | 19.2 |

### Earnings ratios (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Average yield on funds | 10.6 | 10.5 | 10.5 | 10.4 |
| Average cost of funds | 9.7 | 9.1 | 9.1 | 9.0 |
| Spread | 0.9 | 1.4 | 1.4 | 1.4 |
| NIM | 2.3 | 2.5 | 2.4 | 2.3 |
| RoE | 18.1 | 19.6 | 18.9 | 18.7 |
| RoA | 1.3 | 1.4 | 1.3 | 1.3 |

### Operating ratios (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Op. exps / income | 15.2 | 14.7 | 15.2 | 15.5 |
| Op. exps. / avg. assets | 0.4 | 0.4 | 0.4 | 0.4 |

### Asset quality (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Gross NPAs (Rs.mn.) | 4,947 | 5,680 | 8,936 | 10,566 |
| Gross NPAs (%) | 0.6 | 0.6 | 0.6 | 0.6 |

### Capital adequacy (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Capital adequacy | 16.5 | 15.5 | 14.8 | 14.0 |
| Tier I | 12.5 | 12.5 | 12.3 | 12.0 |
| Leverage (x) | 14.4 | 14.3 | 14.4 | 14.6 |

### Valuations

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| EPS | 27.5 | 32.9 | 37.0 | 42.4 |
| Adjusted book value | 149.7 | 175.2 | 202.6 | 235.5 |
| P / E | 17.2 | 14.4 | 12.8 | 11.2 |
| P / ABV | 3.2 | 2.7 | 2.3 | 2.0 |
| Div. payout (%) | 18.2 | 20.1 | 18.9 | 16.5 |

## RoAA decomposition

(%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Interest earned | 10.2 | 10.1 | 10.1 | 10.1 |
| Interest expended | 8.0 | 7.7 | 7.8 | 7.8 |
| Net interest income | 2.2 | 2.4 | 2.3 | 2.3 |
| Other income | 0.2 | 0.2 | 0.2 | 0.2 |
| Operating income | 2.4 | 2.6 | 2.5 | 2.5 |
| Operating expenses | 0.4 | 0.4 | 0.4 | 0.4 |
| Pre-provision profits (PPP) | 2.0 | 2.2 | 2.1 | 2.1 |
| Provisions | 0.0 | 0.1 | 0.1 | 0.1 |
| Profit before taxes | 2.0 | 2.1 | 2.0 | 1.9 |
| Taxes | 0.7 | 0.7 | 0.7 | 0.7 |
| Profit after taxes | 1.3 | 1.4 | 1.3 | 1.3 |

*Source: Company; IDBI Capital Research*

COMPANY REPORT

June 13, 2016

# Repco Home Finance

***Strong play on affordable housing***

ACCUMULATE

**Nifty: 8,170; Sensex: 26,636**

| | |
|---|---|
| **CMP** | **Rs740** |
| **Target Price** | **Rs820** |
| **Potential Upside/Downside** | **+11%** |

**Key Stock Data**

| | |
|---|---|
| Sector | Housing Finance |
| Bloomberg / Reuters | REPCO IN / RHFL.BO |
| Shares o/s (mn) | 63 |
| Market cap. (Rs mn) | 46,708 |
| Market cap. (US$ mn) | 700 |
| 3-m daily average vol. | 15,911 |

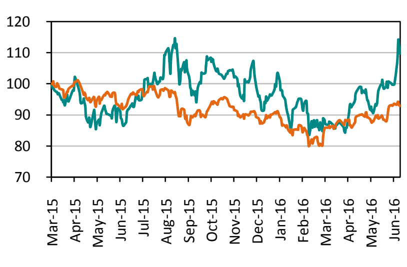
**Price Performance**

| | | | |
|---|---|---|---|
| 52-week high/low | | | Rs794/552 |
| | -1m | -3m | -12m |
| Absolute (%) | 18 | 25 | 24 |
| Rel to Sensex (%) | 15 | 17 | 25 |

**Shareholding Pattern (%)**

| | |
|---|---|
| Promoters | 37.1 |
| FIIs/NRIs/OCBs/GDR | 29.7 |
| MFs/Banks/FIs | 19.2 |
| Non Promoter Corporate | 2.8 |
| Public & Others | 11.2 |

**Relative to Sensex**




*Source: Capitaline*


## Summary

**Repco's niche since inception has been it's focus on self-employed segment of housing finance. As housing finance gained acceptability amongst lenders, it evolved around the salaried customer while the potentially creditworthy but difficult to assess self-employed class remained out of the ambit of lenders. Repco has over the years exploited this niche and established itself firmly in the self-employed segment while continuing to generate equal quantum of growth in the traditional salaried segment. The company's recent, aggressive focus on LAP has given added momentum to earnings. We expect Repco to improve RoE to ~20% in FY18E as leverage expands and spreads stay stable with positive bias.**

**Initiate coverage with ACCUMULATE recommendation and a 1-year price target of Rs820 valuing Repco at 21x FY18E EPS Rs39.3 and 3.9x FY18E ABV Rs209.6.**


## Outlook and Investment Rationale

- **Net advances to grow at ~30% CAGR FY16-FY18E**

  Repco's has achieved a healthy mix between it's consumer segments and product mix which should help the company stay in a strong growth trajectory going forward. With a sanctions growth rate of over 30% and disbursals staying a strong +92% of incremental sanctions, we believe Repco can touch a loan growth CAGR of ~30% FY16-FY18E.

- **Asset quality should stay healthy**

  Repco's NPAs normalize following seasonal spike, typically in first and third quarter, every year. However, in proportion terms, NPAs have actually shown a declining trend in the last few years with Repco utilizing earnings to improve coverage ratio. Repco's cumulative write-offs of just Rs50mn since inception (0.04% of cumulative disbursements) points to underlying robustness of it's origination and monitoring processes.

- **Estimate net profit CAGR ~29% FY16-FY18E**

  Our profit estimate trends in-line with our key assumptions of a strong 30% loan CAGR FY16-FY18E and expectations of softer cost of funds leading to a strong profit growth over estimate period. We expect Repco's RoE (calculated) to touch ~20% in FY18E from 17% in FY16.

- **Initiate with ACCUMULATE**

  We believe the re-rating in Repco's valuation multiples has been driven by a) it's sustained high loan growth post IPO b) matched by equally robust earnings growth. The earnings strength also derives from rising share of high yielding products which has provided the company both diversification as well as hedge for it's spreads. This we believe has led to the valuation re-rating we have seen in Repco. We initiate coverage with an **ACCUMULATE** recommendation and 1-yr price target of Rs820 based on a fair value P/E multiple of 21x FY18E EPS Rs39.3.

**Table: Financial snapshot**

| Y/E: March | NII (Rs mn) | PAT (Rs mn) | EPS (Rs) | BV (Rs) | PE (x) | P/BV (x) | ROE (%) | ROA (%) | GNPA (%) | CAR (%) |
|---|---|---|---|---|---|---|---|---|---|---|
| FY15 | 2,375 | 1,231 | 19.7 | 130.2 | 37.5 | 5.7 | 15.9 | 2.3 | 1.3 | 20.3 |
| FY16 | 3,034 | 1,501 | 24.1 | 153.1 | 30.7 | 4.8 | 17.0 | 2.2 | 1.3 | 20.7 |
| FY17E | 3,798 | 1,951 | 31.3 | 180.8 | 23.6 | 4.1 | 18.7 | 2.2 | 1.4 | 20.2 |
| FY18E | 4,717 | 2,449 | 39.3 | 217.8 | 18.8 | 3.4 | 19.7 | 2.1 | 1.4 | 19.2 |

*Source: Company; IDBI Capital Research*

## Investment Rationale

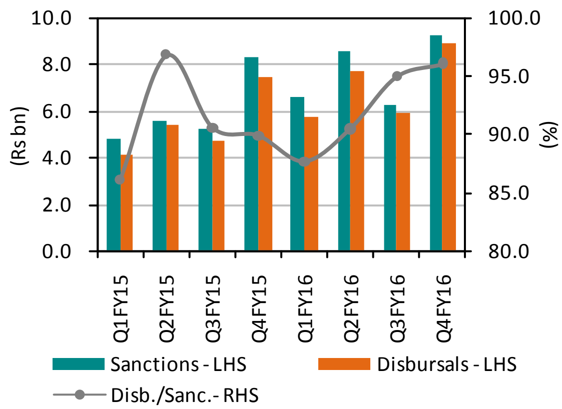
- **Net advances to grow at ~30% CAGR FY16-FY18E**

As discussed in the industry section, there exists a strong growth opportunity in the low cost housing segment, typically the sub Rs3mn category. While Repco has never bound itself with loan sizes, having lent even in higher ticket size segment (+Rs3mn), those remain outliers based on specific cases. Repco's overwhelming business continues to accrue from the affordable segment.

We believe Repco's niche in lending to non-salaried segment should help the company stay in a strong growth trajectory going forward. Repco's net advances grew at a 42% CAGR FY05-FY16. The growth rate has moderated but nevertheless steady at ~30% CAGR in the post-listing period (FY13-FY16). With a sanctions growth rate of over 30% and disbursals staying a strong +90% of incremental sanctions, we expect Repco's loan growth to stay comfortably high at ~30% FY16-FY18E.

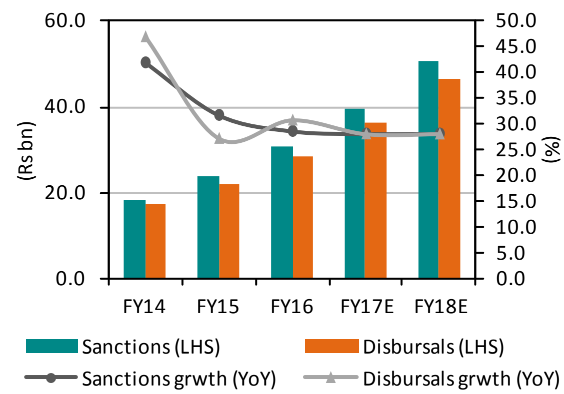
We also expect Repco to continue maintaining a mix of 80/20 between housing and LAP products. Within housing, the company believes it shall be able to maintain the current mix of 55/45 between non-salaried and salaried segments. Our earnings estimates are based on these assumptions.

**Figure: Steadily rising disbursals…**



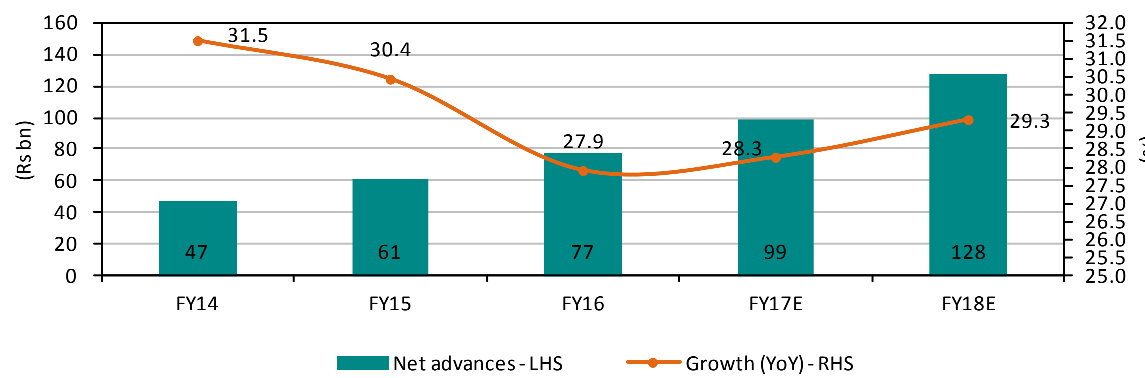

*Source: Company; IDBI Capital Research*

**Figure: …should keep loan growth strong**




*Source: Company; IDBI Capital Research*

**Figure: Net loans to grow at ~29% CAGR FY16-FY18E**




*Source: Company; IDBI Capital Research*

- **LAP giving steady momentum to loan growth**

Repco gave a steady push to the LAP product taking it to constitute ~20% of the overall loan portfolio in FY14 compared to ~14% in FY10. The loan mix has been kept steady over past two years and is likely to stay so going forward. Thus, while FY10-FY14 saw an outsized and rising share of LAP in the incremental loan mix, it has stayed steady over FY15-FY16 in the incremental loan mix. Given Repco's competitive pricing in LAP, which is comparable to SCBs (~15% yield), we believe this product easily offers Repco strong growth opportunity.

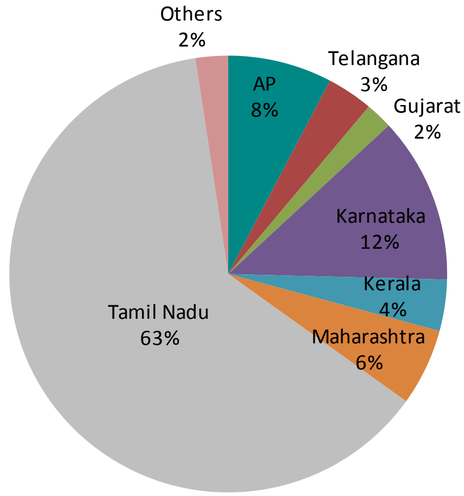
- **Steady network expansion to help maintain momentum**

Repco has been expanding footprint in newer areas, specifically, contiguous states. The company scouts new geographies with a 'satellite office', typically a small branch which over a 18-24 month period gets upgraded to a full fledged branch.

Repco has been expanding it's network by 5-6 outlets every year. The branch additions are typically upgradation of existing satellite branches with greenfield expansion happening in the form of new satellite branches. In states like Maharashtra, Repco is present in fringes of metropolitan areas like Pimpri-Chinchwad (Pune), Dombivali (Thane-Mumbai-Navi Mumbai). These fringes are strong catchment areas for attracting it's target customers.

While the company continues to derive significant business from Tamil Nadu with ~62.5% of the portfolio exposure, it is not surprising given the company's decade and half existence in the state. Secondly, new expansion is evenly split between TN and non-TN geographies keeping the incremental portfolio exposure unchanged. Newer geographies are slowly catching up and should provide strong growth opportunities as the network expands and matures.

**Figure: Statewise portfolio exposure (FY16)**



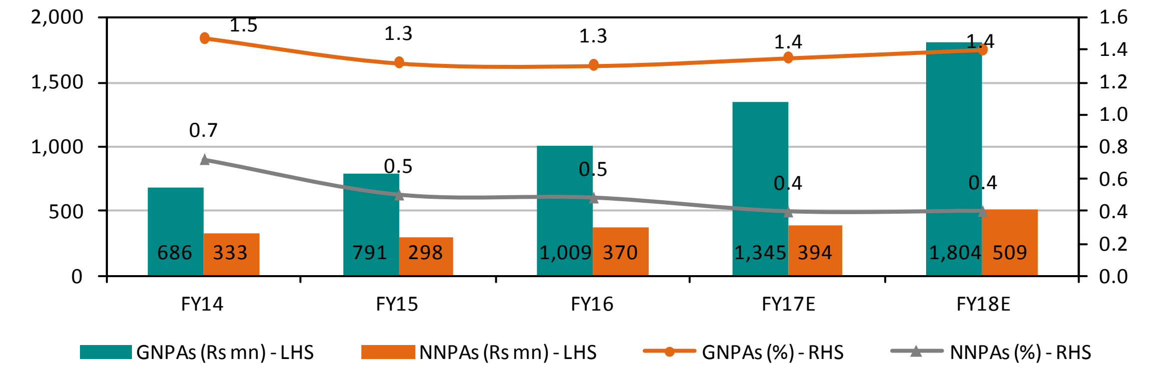

*Source: Company; IDBI Capital Research*

## Asset quality has stayed robust

- **Seasonality in asset quality lasts one quarter**

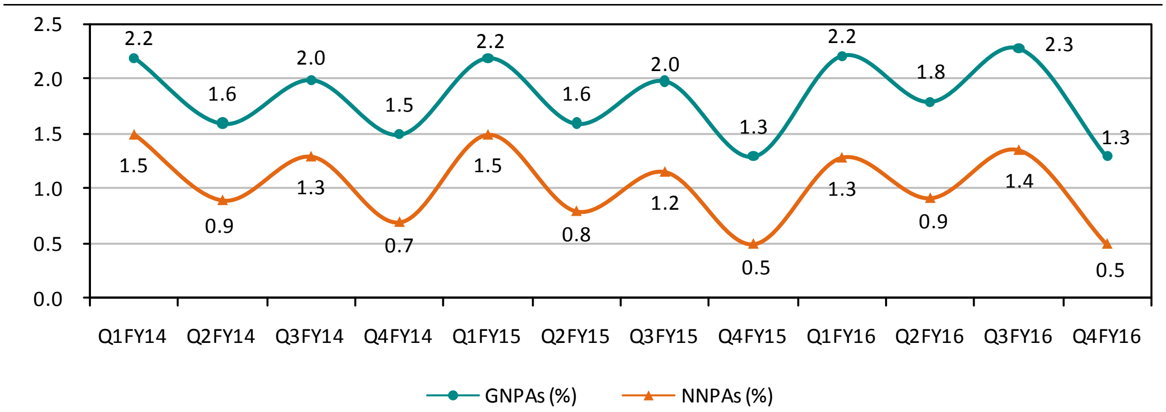
  Repco's NPAs typically spike in the first and third quarter of every financial year and are resolved in the subsequent quarter. This short seasonality is caused by the typical cash flow issues faced by low income segment due to personal expenses – typically education related (start of new academic year) or religious celebrations (period of major religious festivals). Repco's NPAs normalize following spike every year and in proportion terms, have actually shown a declining trend in the last few years. Repco's cumulative write-offs of just Rs50mn since inception (0.04% of cumulative disbursements) points to underlying robustness of it's asset quality.

**Figure: GNPAs have stayed stable, PCR improving**




*Source: Company; IDBI Capital Research*

**Figure: Asset quality getting incrementally better though seasonality persists**




*Source: Company; IDBI Capital Research*

- **Estimate net profit CAGR ~29% FY16-FY18E**

  We expect Repco's net profit to increase at ~29% CAGR FY16-FY18E compared to a softer 23% CAGR FY13-FY16. We estimate Repco's net profit at Rs2,481mn in FY18E compared to Rs1,501mn in FY16. A key earnings risk in our estimates shall be asset quality, which we have estimated to stay steady over FY16-FY18E period. We estimate GNPA at 1.4% over FY17E-FY18E compared to average 1.3% FY15-FY16 (the recent NPA peak was in FY13 at 1.5%).

## Valuation and Recommendation

- **Valuations have steadily re-rated**

Repco's valuations have steadily re-rated and risen since it's listing in April 2013. The following tables summarise Repco's valuations at the time of it's IPO and since listing.

**Table: Repco forward valuations at IPO offer price of Rs172/share**

| Metric | FY14 | FY15 |
|---|---|---|
| EPS (Rs) | 14.1 | 15.8 |
| P/E (x) | 12.2 | 10.9 |
| ABV (Rs) | 91.6 | 105.2 |
| P/ABV (x) | 1.9 | 1.6 |

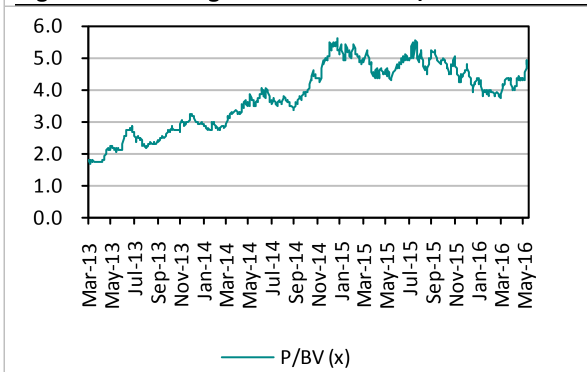
*Source: Bloomberg; IDBI Capital Research*

**Table: Repco one year forward valuations since listing**

| Metric | P/E (x) | P/ABV (x) |
|---|---|---|
| Median since listing | 20.4 | 3.4 |
| Max since listing | 30.7 | 5.0 |

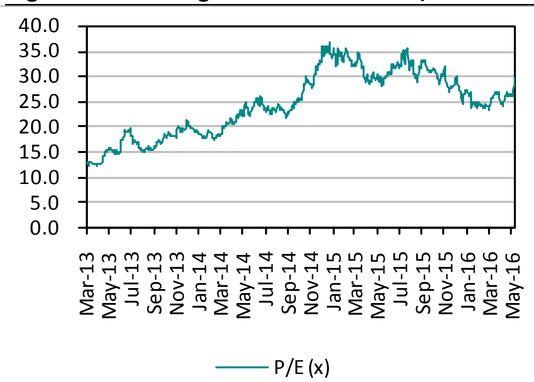
*Source: Bloomberg; IDBI Capital Research*

**Fig.: REPCO trading at 5x 1Y forward P/ABV**




*Source: Company; NSE, IDBI Capital Research*

**Fig.: REPCO trading at 25x 1Y forward P/E**




*Source: Company; NSE, IDBI Capital Research*

We believe the re-rating in Repco's valuation multiples has been driven by a) it's sustained, high loan growth post IPO, b) matched by strong earnings, also a result of improving mix of LAP product. While LAP as a product did exist, it picked up strong momentum post IPO.

- **Initiate with ACCUMULATE, price target Rs820**

Our price target is based on a P/E of 21x FY18E EPS Rs39.3 and our fair value P/E multiple is also Repco's median P/E ratio since listing. Our FY18E ABV Rs209.6 discounts the target price 3.9x. While we don't foresee further re-rating, we do believe Repco shall continue to exhibit strong earnings growth going forward and hence, continue to trade at premium multiples.

## About the Company

Repco Home Finance was founded in FY01 as a 100% owned housing finance subsidiary of The Repatriates Co-operative Bank Ltd or Repco Bank, a special purpose co-operative banking institution founded in 1969 for rehabilitation and financial upliftment of refugees from Myanmar and Sri Lanka. The first major non-promoter investment in Repco Home Finance came in 2007 with the induction of Carlyle PE on Repco Board following it's equity investment. In Mar-Apr'13, Repco concluded it's IPO and listed on BSE and NSE.

**Table: Shareholding Pattern (Mar'16)**

| Share holder | Shareholding (%) |
|---|---|
| Repco Bank (Promoter) | 37.1 |
| FIIs | 28.4 |
| MFs | 18.8 |
| Others | 15.7 |
| **Total** | **100.0** |

*Source: Company; IDBI Capital Research*

Repco first crossed Rs1 bn loan booking FY04 and has grown at a 42% CAGR between FY04 FY16. The growth rate though moderating has continued to stay strong at 29% CAGR post listing (FY13-FY16). Repco Home overtook it's parents overall loan book size and profitability in FY14 and since then continues to lead.

- **Management Overview**

  Repco top management comprises of career bankers with extensive experience with PSBs as well as the housing regulator NHB. Most of Repco's current top management has been with the company for a fairly longtime. Repco MD Mr. Varadarajan has been associated with the parent Repco Bank since the year 2001.

| Name | Designation | With Repco since |
|---|---|---|
| T S Krishnamurthy | Non-Exec. Chairman | Sep'11 |
| R Varadarajan | MD | Oct'10 |
| T Karunakaran | CFO | Jul'04 |
| K Prabhu | CS | Dec'08 |
| P Natarajan | ED | Aug'12 |
| V Raghu | ED | Nov'12 |
| K Ashok | CGM | Dec'05 |
| Poonam Sen | GM | Oct'06 |
| K S Madhukar | GM | Apr'08 |

# Financial Summary

### Profit & Loss Account (Rs mn)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Interest income | 6,693 | 8,521 | 10,868 | 13,892 |
| Interest expense | 4,318 | 5,487 | 7,070 | 9,175 |
| **Net interest income** | **2,375** | **3,034** | **3,798** | **4,717** |
| *Growth (% YoY)* | *24.0* | *27.7* | *25.2* | *24.2* |
| Other income | 237 | 301 | 390 | 499 |
| **Operating income** | **2,613** | **3,335** | **4,188** | **5,216** |
| *Growth (% YoY)* | *24.1* | *27.7* | *25.6* | *24.5* |
| Staff cost | 335 | 399 | 473 | 559 |
| Other operating expenses | 212 | 244 | 277 | 312 |
| Operating expenses | 547 | 643 | 750 | 872 |
| *Growth (% YoY)* | *41.1* | *17.5* | *16.6* | *16.3* |
| **Operating profit** | **2,065** | **2,692** | **3,439** | **4,344** |
| *Growth (% YoY)* | *20.2* | *30.4* | *27.7* | *26.3* |
| Non-tax provisions | 203 | 392 | 483 | 634 |
| **Profit before tax** | **1,862** | **2,300** | **2,956** | **3,710** |
| *Growth (% YoY)* | *24.9* | *23.5* | *28.5* | *25.5* |
| Taxes | 631 | 799 | 1,005 | 1,261 |
| *Tax rate (%)* | *33.9* | *34.8* | *34.0* | *34.0* |
| **Profit after tax** | **1,231** | **1,501** | **1,951** | **2,449** |
| *Growth (% YoY)* | *11.8* | *21.9* | *30.0* | *25.5* |

### Balance Sheet (Rs mn)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Equity | 624 | 624 | 624 | 624 |
| Reserves | 7,497 | 8,925 | 10,653 | 12,957 |
| Networth | 8,121 | 9,548 | 11,277 | 13,581 |
| Borrowings | 51,044 | 65,379 | 86,003 | 112,101 |
| Current liabilties | 1,592 | 2,706 | 2,591 | 3,579 |
| **Total liabilities** | **60,757** | **77,633** | **99,871** | **129,261** |
| | | | | |
| Loans | 60,129 | 76,912 | 98,662 | 127,592 |
| Investments | 124 | 124 | 124 | 124 |
| Fixed assets | 89 | 107 | 126 | 147 |
| Current assets | 414 | 490 | 959 | 1,398 |
| **Total assets** | **60,757** | **77,633** | **99,871** | **129,261** |

*Source: Company; IDBI Capital Research*

### Growth (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Total assets | 28.3 | 27.8 | 28.6 | 29.4 |
| Housing loans | 29.0 | 27.9 | 28.3 | 29.3 |
| Borrowings (sec+unsc.) | 30.8 | 28.1 | 31.5 | 30.3 |

### Earnings ratios (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Average yield on funds | 12.4 | 12.4 | 12.3 | 12.2 |
| Average cost of funds | 9.6 | 9.4 | 9.3 | 9.3 |
| Spread | 2.8 | 3.0 | 3.0 | 2.9 |
| NIM | 4.4 | 4.4 | 4.3 | 4.2 |
| RoE | 15.9 | 17.0 | 18.7 | 19.7 |
| RoA | 2.3 | 2.2 | 2.2 | 2.1 |

### Cost ratios (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Op. exps / income | 21.0 | 19.3 | 17.9 | 16.7 |
| Op. exps. / avg. assets | 1.0 | 0.9 | 0.8 | 0.8 |

### Asset quality (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Gross NPAs (Rs.mn.) | 791 | 1,001 | 1,345 | 1,804 |
| Gross NPAs (%) | 1.3 | 1.3 | 1.4 | 1.4 |

### Capital adequacy ratio (%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Capital adequacy | 20.3 | 20.7 | 20.2 | 19.2 |
| Tier I | 20.3 | 20.7 | 20.2 | 19.2 |
| Leverage (x) | 7.5 | 8.1 | 8.9 | 9.5 |

### Valuations (x)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| EPS | 19.7 | 24.1 | 31.3 | 39.3 |
| Book value | 125.5 | 148.2 | 174.5 | 209.6 |
| P / E | 37.5 | 30.7 | 23.6 | 18.8 |
| P / ABV | 5.9 | 5.0 | 4.2 | 3.5 |
| Div. payout (%) | 7.6 | 7.5 | 5.6 | 5.1 |

## RoAA decomposition

(%)

| Year-end: March | FY15 | FY16 | FY17E | FY18E |
|---|---|---|---|---|
| Interest earned | 12.38 | 12.31 | 12.25 | 12.13 |
| Interest expended | 7.99 | 7.93 | 7.97 | 8.01 |
| Net interest income | 4.39 | 4.38 | 4.28 | 4.12 |
| Other income | 0.44 | 0.44 | 0.44 | 0.44 |
| Operating income | 4.83 | 4.82 | 4.72 | 4.55 |
| Operating expenses | 1.01 | 0.93 | 0.84 | 0.76 |
| Pre-provision profits (PPP) | 3.82 | 3.89 | 3.87 | 3.79 |
| Provisions | 0.38 | 0.57 | 0.54 | 0.55 |
| Profit before taxes | 3.44 | 3.32 | 3.33 | 3.24 |
| Taxes | 1.17 | 1.16 | 1.13 | 1.10 |
| Profit after taxes | 2.28 | 2.17 | 2.20 | 2.14 |

*Source: Company; IDBI Capital Research*

# Notes

| | | |
|---|---|---|
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**Stocks:**

**BUY:** Absolute return of 15% and above; **ACCUMULATE:** 5% to 15%; **HOLD:** Upto ±5%; **REDUCE:** -5% to -15%; **SELL:** -15% and below.

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