

PNB Housing Finance



In the Big League

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PNB Housing Finance

BSE Sensex

31,160

S&P CNX

9,736

CMP: INR1,412

TP: INR1,675 (+19%)

Buy



Ghar Ki Baat

Stock Info

Bloomberg	PNBHF IN
Equity Shares (m)	165.6
52-Week Range (INR)	1715 / 789
1, 6, 12 Rel. Per (%)	-7/19/-
M.Cap. (INR b)	233.9
M.Cap. (USD b)	3.7
12M Avg. Val (INR M)	690
Free float (%)	61.1

Financial Snapshot (INR b)

Y/E Mar	2018E	2019E	2020E
NII	14.8	19.9	26.4
PPP	14.4	19.3	25.9
PAT	8.0	10.8	14.4
EPS (INR)	48.1	65.1	87.2
BV/Sh. (INR)	367.6	419.1	488.1
RoAA (%)	1.5	1.5	1.5
RoE (%)	13.8	16.6	19.2
Payout (%)	20.9	20.9	20.9
P/E (x)	29.3	21.7	16.2
P/BV (x)	3.8	3.4	2.9

Shareholding pattern (%)

As On	Jun-17	Mar-17	Dec-16
Promoter	38.9	39.1	39.1
DII	4.5	4.1	4.0
FII	14.5	15.4	15.9
Others	42.1	41.5	41.0

FII Includes depository receipts

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In the Big League

A perfect blend of growth with quality

- PNB Housing Finance (PNBHF) is a classic turnaround story. While the company was incorporated in 1988 as a wholly-owned subsidiary of Punjab National Bank, the turnaround started two decades later in FY10. This was effected by a change in shareholding (Destimoney Enterprises, a subsidiary of the Carlyle Group, purchased 26% stake in PNBHF) as well as a change in management.
- Over FY10-15, the company invested in technology, re-jigged its operations and processes, diversified its loan book, and expanded in new geographies. Consequently, over FY12-17, PNBHF's loan book grew from INR40b to INR400b+, and PAT increased from INR0.8b to INR5.2b.
- PNBHF has effectively leveraged on a unique hub-and-spoke model, where customer acquisition happens at the branch level while underwriting takes place at a hub. The company has incurred significant technology and branch infrastructure costs over the past few years and we expect operating leverage benefits to accrue with strong growth, resulting in a 600bp reduction in the C/I ratio to 22% over FY17-20.
- PNBHF's asset quality has been one of the best among peers, with a GNPL ratio (2-year lag basis) of 0.5% as of FY17. However, as the loan book gets more seasoned and on account of increasing corporate exposure, we expect a modest increase in GNPA and credit costs. Yet, we expect RoA to remain largely stable at ~1.5%. With increasing leverage over time, RoE should cross 19% by FY20. We initiate coverage on PNBHF with a Buy rating and a target price of INR1,675 (22x Sep 2019E EPS), implying 3.7x Sep2019E BVPS.

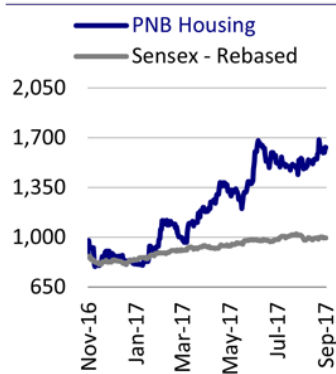
Growth potential unlocked with unique business model

Commencing a turnaround in 2011, PNBHF registered strong loan growth across segments with a loan book CAGR of 60% over FY12-17, driven by increased market penetration and expansion into new territories. Consequently, its market share increased from ~0.5% to 2%+, making it the fifth largest HFC in India. With a hub-and-spoke model and a central processing center (CPC), the company has ensured that branches focus only on loan sourcing, hubs focus solely on underwriting and the CPC focuses only on file processing. Unlike other HFCs which are now focusing more on the affordable housing segment, PNBHF caters largely to the middle and upper-middle class segment. Its average ticket size of INR3.2m in home loans is ~30% higher than that of HDFC and IHFL. The company now has 66 branches in 40 cities, and aspires to achieve at least 8-10% market share (among HFCs) in every city where it operates. We believe the company has built the foundation to drive 37% AUM CAGR over FY17-20.

Loan mix reached targeted level of 60:40 (Retail and Non retail)

PNBHF has built capabilities in appraising LAP, builder loans and other non-core loans. With a strong & well-qualified team (60-65% of its underwriters are Chartered Accountants), the company has developed capabilities to underwrite

Stock Performance (1-year)



skillfully based on cash-flow analysis. The non-housing loan book now accounts for 41% of the total loan book, as compared to 25% in FY13. Shift in the loan mix has helped the company to a) be competitive in the retail segment without impact on overall company margins b) absorb high opex without denting profitability. Loan mix has reached targeted level and upside to ROA will be realized by operating leverage rather than margins.

Asset quality pristine; Factor in high credit cost conservatively

GNPL/NNPL ratio stood at 0.22%/0.15% as of end-FY17, the lowest among peers. Even on a two-year lag basis, the GNPL ratio stands at ~0.5%. In the construction finance loan book, the NPA is nil. In fact, 88% of projects funded have witnessed sales velocity in excess of the company's assumptions. While the company has stringent underwriting processes in place, we believe that the loan book is still largely unseasoned, and thus, the GNPL ratio could increase. PNBHF has a large corporate loan book (~16% of total loans) and LAP book (~16%). Additionally, nearly 40% of the loan book is from north India, where the real estate market has been subdued for the past 2-3 years. While the company maintains adequate collateral cover on its loans (LAP LTV capped at 70% at origination; construction finance loan cover of 2x), we believe GNPLs should rise to 40-50bp over the next 2-3 years. Consequently, credit costs (including standard asset provisions) are expected to rise from 30bp in FY17 to 40-45bp over the medium term. However, the company has already built a contingency provision buffer of INR395m.

Growth, asset quality & improving RoE justify valuation premium

We believe PNBHF is at an inflection point. Increasing geographical spread and new branch openings (110 branches in FY20E v/s 66 in FY17) are expected to result in the loan book growing to ~INR1t by FY20 (37% CAGR). With the pace of investments slowing down, coupled with operating leverage benefits kicking in, the expense ratio is set to decline meaningfully. Credit costs, however, are expected to inch up marginally on account of portfolio seasoning. All these factors put together are expected to drive 40% PAT CAGR over FY17-20E, in our view. While RoA is likely to remain largely stable at ~1.5%, RoE should improve from 14% in FY17 to 19% in FY20 on account of higher leverage. While we expect the company to raise capital in FY19 or FY20, we have not built in any capital raise assumptions in our numbers. We use RI model with Rf of 7%, CoE of 13.5% and terminal growth rate of 5% to arrive at a target price of INR1,675 (22x Sep 2019E EPS), implying 3.7x Sep2019E BVPS. We initiate coverage with a **Buy** rating.

Exhibit 1: Valuation comparison

	AUM (INR b)	Price (INR)	Market Cap (INR b)	AUM CAGR (FY17-20E) %	PAT CAGR (FY17-20E) %	RoA (%)		RoE (%)		P/B		P/E	
						FY18E	FY19E	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
HDFC	3,550	1,719	2,750	16	14	1.9	1.9	19.3	18.4	4.3	3.1	23.8	18.7
LICHF	1,471	607	307	14	14	1.4	1.5	18.2	18.5	2.5	2.1	14.6	12.4
IHFL	945	1,223	521	29	25	3.3	3.2	28.2	31.3	3.8	3.3	14.2	11.3
DHFL	882	526	167	21	24	1.2	1.3	14.1	15.6	1.9	1.6	13.9	11.2
PNBHF	468	1,412	234	37	40	1.5	1.5	13.8	16.6	3.8	3.4	29.3	21.7
Can Fin	138	2,597	69	NA	NA	2.0	2.0	23.2	22.6	4.6	3.7	23.1	18.1
GRUH	137	520	191	22	23	2.4	2.4	33.0	32.8	15.7	12.9	52.3	43.1
REPCO	90	601	37	19	17	2.2	2.2	17.5	17.0	2.8	2.4	17.4	15.3

Source: Company, MOSL; Note: Can Fin Homes numbers are BBG estimates

Consistently gaining market share from peers

Turnaround led by change in ownership and management

- With a change in management in 2011, PNBHF witnessed an impressive turnaround, with a robust loan CAGR of 60% over FY12-17. This was driven by a higher branch count, coupled with increasing branch productivity.
- The company has created a niche for itself by targeting the self-employed segment in the urban areas. With low cost of funds driven by a superior liability profile, it is able to price its loans at par with the best players in the industry.
- Branch count grew from 32 in FY14 to 63 in FY17. Management plans to open 23 new branches in FY18, and we estimate another 25 branches over FY18-20. New branch openings, coupled with improving productivity, should drive 37% AUM CAGR over FY17-20, in our view.

Unlike most state-owned enterprises, management does not have a fixed tenure

Change in ownership and management key to turnaround

PNBHF was incorporated in 1988 as a wholly owned subsidiary of Punjab National Bank. Subsequently, the company registered as a housing finance company (HFC) with the National Housing Bank (NHB) in 2001. In 2009, PNB sold 26% stake in the company to Destimoney Enterprises (DEPL). Further, in 2012, DEPL's stake increased to 49% upon conversion of the CCDs issued to it in 2009. DEPL is now owned by Carlyle Group's Quality Investments Holdings. Post the stake sale to DEPL, new management was inducted into the company.



Mr Sanjaya Gupta - Managing Director

- Joined the company in 2010 as Managing Director.
- Previously served as the Country Head and CEO of the Prospective Mortgage Guaranty Business in India at AIG United Guarantee
- Worked with HDFC Ltd. for 16 years, with his last assignment as Head of Business Development & Distribution. Was also responsible for establishing the international housing finance branch operations for HDFC Ltd.



Mr Jayesh Jain - Chief Financial Officer

- Joined PNBHF in August 2014.
- Previously served as the CFO of GRUH Finance Limited and has over 15 years of experience in the housing finance industry.
- He holds a BCom and is a CA. He is a Fellow Member of the ICAI, and a Certified Information Systems Auditor and a Certified Information Security Manager from the Information Systems Audit and Control Association, USA.



Mr Shaji Varghese – Executive Director, Business Development

- Joined PNBHF in February 2012.
- Previously served as Senior VP at IndusInd Bank. He has more than 17 years of experience in retail assets, liabilities and wealth management.
- He holds a Bachelor's Degree in Law from the Bharati Vidyapeeth New Law College, University of Pune. He also holds a Diploma in Business Management from the Bharati Institute of Management, University of Pune. He holds a Master's Degree in Management Science from the University of Pune.

Management initiated a thorough business restructuring program in FY11, which concluded in FY16. This included:

PNBHF undertook an exhaustive restructuring exercise over FY11-16, resulting in significantly improved performance

- Improvement, centralization and standardization of business processes, payments and credit policies; changes in origination/sourcing strategy and in product composition/target customer segments.
- Changes to the organizational structure, which involved significant changes in credit underwriting and monitoring functions, and the hiring of in-house sales teams, fraud prevention specialists, collection experts and in-house legal, technical and property valuation experts.
- Creation and implementation of a new hub-and-spoke model, wherein the branches were positioned to act as the primary points of sale and collections, while the processing hubs were positioned to provide loan processing, credit appraisal and monitoring functions.
- Development of a new IT platform, which improved the efficiency of operations. PNBHF also undertook a marketing program to reposition the 'PNB Housing' brand and create a new logo and tagline.

This exercise was instrumental in driving a CAGR of 60% in the loan book (3x of industry growth) and ~50% in PAT over FY12-17. The company is now the fifth largest HFC in India. It also has the second largest public deposit base after HDFC among HFCs. However, the company has higher share of bulk deposit base, with the top 20 depositors accounting for 35% of all deposits. More than half of the deposits come from non-retail sources.

Exhibit 2: 60% AUM CAGR over FY12-17

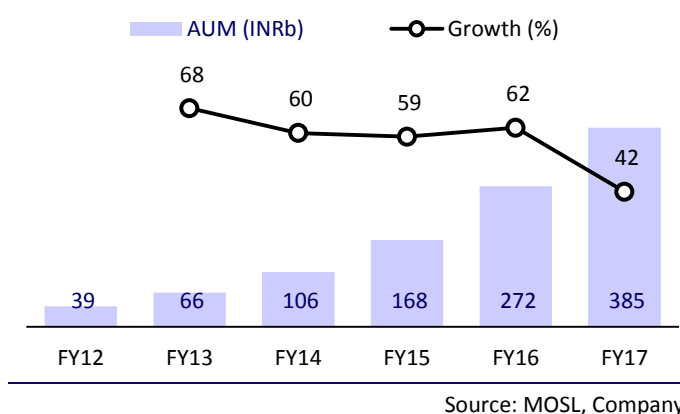


Exhibit 3: 48% PAT CAGR over FY12-17

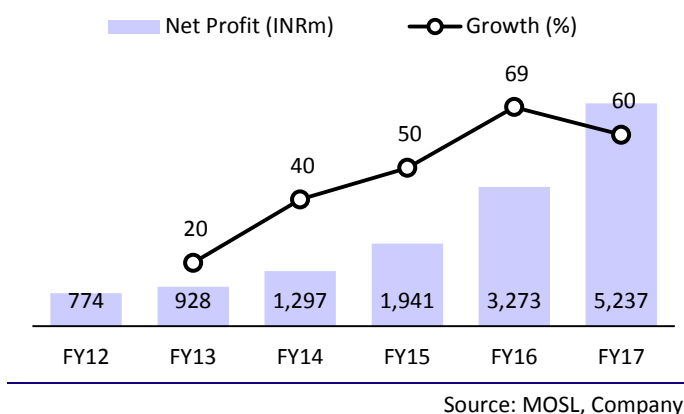


Exhibit 4: Key milestones

Year	Details
1988	Incorporation of the Company
2003	Company notified under the SARFAESI Act
2009	PNB sold 26% of its stake in the total issued, subscribed and paid-up share capital of the Company to DEPL
2010	Launched the business process re-engineering project, "Kshitij"
2012	DEPL increased its shareholding to 49% in the Company, pursuant to the conversion of CCDs issued to DEPL in 2009
2015	Implemented end-to-end Enterprise System Solution

Source: MOSL, Company

Loan sourcing done by an in-house sales team, off-roll DST team and DSAs

Well-diversified loan book with hub-and-spoke underwriting

PNBHF caters to both the salaried and self-employed customer segments, but with a greater focus on the urban self-employed segment. It offers retail home loans, and non-housing loans in the form of construction finance, loans against property (LAP), lease rental discounting loans (LRD), non-residential property (NRP) and corporate term loans (CTL). PNBHF conducts its operations via 66 branches, 18 processing hubs and a central processing center (CPC) in NCR. The biggest advantage of this model is that the branch focuses exclusively on loan sourcing, the hub focuses solely on loan underwriting and the CPC focuses solely on file processing and other back-end operations. Apart from an in-house sales team, the company has a team of DSTs (off-roll employees who source loans exclusively for PNBHF) and also relies on DSAs for loan sourcing.

Exhibit 5: Interesting facts about their hub-and-spoke model

What?	Description
Number of branches associated to a hub	❖ 4-5
Number of underwriters in a hub	❖ 9-10
Number of sales managers per branch	❖ 3-6
Number of DST managers per branch	❖ 20-25
Home loan approval rate	❖ 75-80%
LAP approval rate	❖ 60-65%
Collection mechanism	❖ Completely in-sourced; 2-3 collection guys per branch

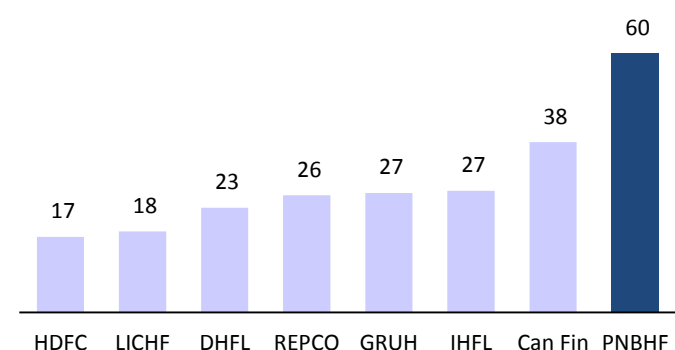
Source: MOSL, Company

Fastest AUM CAGR over the past 5 years compared to peers

Gaining market share from peers

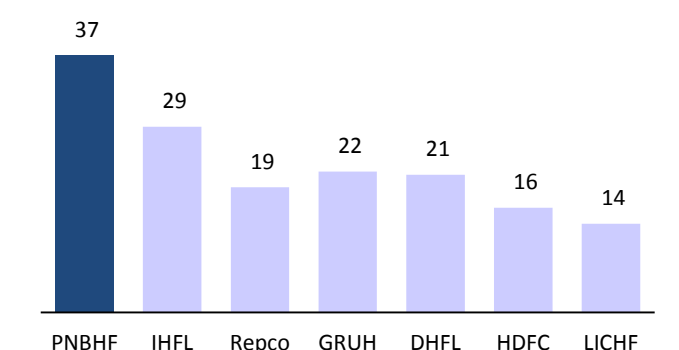
On account of a low base, coupled with the impact of business re-engineering, PNBHF registered loan growth significantly better than peers over FY12-17. While the home loan industry grew at an 18% CAGR over the same time frame, PNBHF registered 60% growth. As a result, its home loan market share improved from 0.5% in FY12 to 2%+ in FY17. The company has a target to achieve 8-10% market share (among HFCs) in every market that it operates in.

Exhibit 6: FY12-17 loan book CAGR (%) – best among peers



Source: MOSL, Company; Note: DHFL loan book CAGR over FY13-17

Exhibit 7: FY17-20E loan book CAGR (%) – best among peers

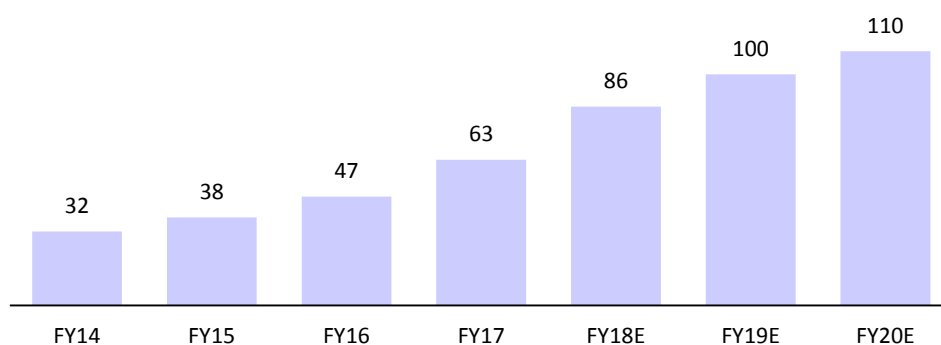


Source: MOSL, Company

With falling interest rates, largely stable real estate prices and boost from government schemes, the housing finance sector remains in a sweet spot over the foreseeable future. We expect PNBHF to continue with its robust growth trajectory with expansion into newer geographies, and build in 37% AUM CAGR over FY17-20E.

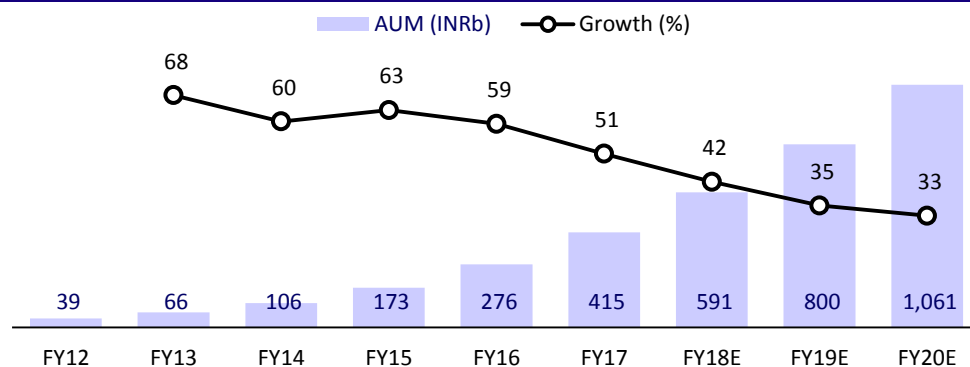
The company has doubled its branch count over FY14-17, leading to strong loan growth

Exhibit 8: Trend in branch network



Source: MOSL, Company

Exhibit 9: Trend in AUM



Source: MOSL, Company

Diverse product offering across retail and corporate

Mix reached to targeted level

- PNBHF is one of the most diversified HFCs, with a mix of retail home loans, LAP, construction finance, LRD, non-residential property and corporate term loans.
- Over the past four years, the company has gradually increased the share of non-housing loans (including construction finance) from 25% to 41%. The share of the non-retail home loan book is highest among its large peers after IHFL. However, in both LAP and CF, the company caters to the lower-risk end of the spectrum.
- We expect PNBHF to continue increasing its share of non-housing loans, albeit at a slower pace than in the past few years.

Greater focus on the self-employed segment, with higher ticket size than peers like HDFC & IHFL in home loans

Increasing share in non-retail loans

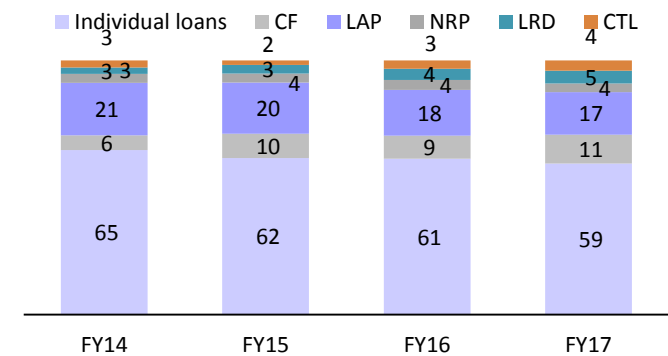
PNBHF caters to both the salaried and self-employed customer segments, but with a greater focus on the urban self-employed segment. It offers retail home loans, and non-housing loans in the form of construction finance, loans against property (LAP), lease rental discounting loans (LRD) and corporate term loans. Construction finance is done to real estate developers for residential projects only. In addition, bulk of the LRD book is retail.

Since PNBHF operates largely in tier I/II cities, its average ticket size in home loans of INR3.2m is almost 30% higher than that of its peers like HDFC and Indiabulls. Also, unlike some of its peers, the company is not focusing a lot on affordable housing finance. However, in LAP, the company chooses to cater to the lower end of the spectrum in terms of ticket size, with average ticket size of INR5m. In construction finance, PNBHF has average ticket size of INR500m, while retail LRD bears average ticket size of INR30-40m. The company follows stringent underwriting standards, with retail housing loans originating at an LTV of 66% and retail non-housing loans (LAP) at an LTV of 46%.

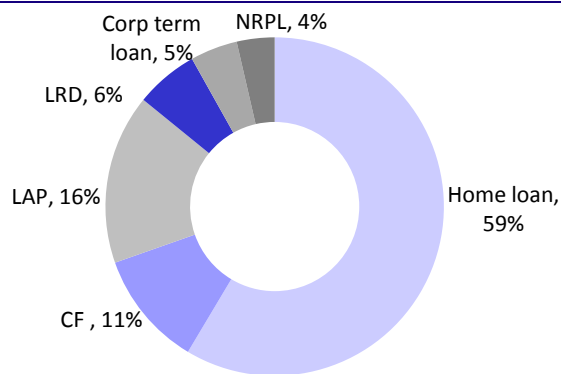
PNBHF has increased the share of its non-retail book over the past four years; however, its CF

Over FY13-17, PNBHF increased the share of its non-housing loans from 25% to 41%. Majority of this increase was on account of construction finance. The share of construction finance now stands at 11% v/s 2% in FY13. This was accompanied by a decline in the share of retail home loans from 75% to 59% over the same time period. As of June 2017, the share of individual home loans/construction finance/other non-housing loans stood at 59%/11%/30% of its total loan portfolio.

Within the construction finance segment, PNBHF caters to the lower-risk end of the spectrum in terms of quality of the developer and the project. This is evident from the incremental yields of <12%, which is lower than what other HFCs make on their construction finance portfolio.

Exhibit 10: Loan mix trend over FY13-17 (%)

Source: MOSL, Company

Exhibit 11: Loan mix with break-up of non-housing loans

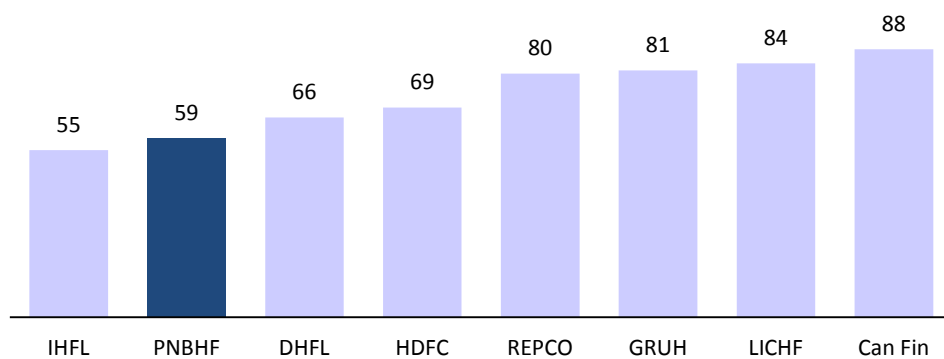
Source: MOSL, Company

Around 66% of incremental loans are sourced in-house

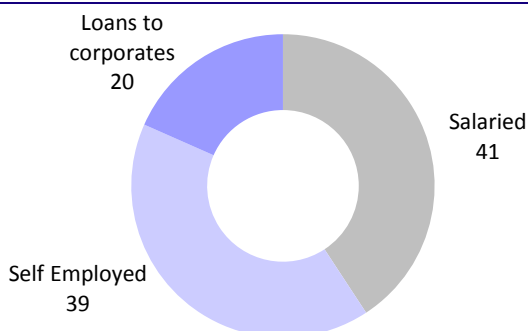
PNBHF has a network of 66 branches across the northern, western and southern regions, through which it sources loans. In addition to its in-house teams, it has a large network of DSAs for loan sourcing (largely for LAP). It also has 18 processing offices and one central support office (CSO). The branches act as the primary point of sale, assisting with the origination of loans, collection processes, sourcing deposits and enhancing customer service, while the processing hubs and zonal offices provide support functions such as loan processing, credit appraisal and monitoring. The CSO supervises operations nationally.

The company has a lower share of retail home loans compared to peers

Within its peer group, PNBHF has a relatively low share of retail home loans (59% as of FY17). It also has a high proportion of loans to self-employed customers, similar to peers like Repco Home Finance, GRUH Finance and DHFL.

Exhibit 12: Share of retail home loans in total loan book (FY17, %)

Source: MOSL, Company

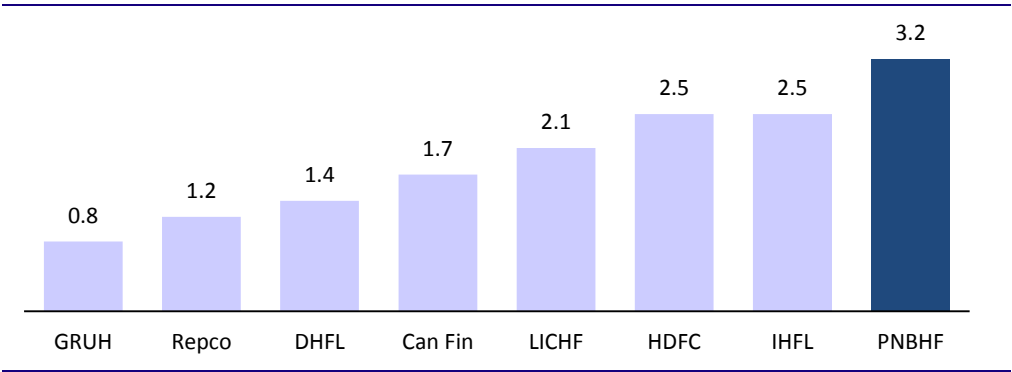
Exhibit 13: Customer segment mix (%)

Source: MOSL, Company

Ticket size at INR3.2m for retail home loans is higher than competitors

PNBHF has the highest average ticket size of INR3.2m in retail home loans in its peer group.

Exhibit 14: Average ticket size (INR m, FY17)



Source: MOSL, Company

Factor in stable margins

Diversified liability profile – an added advantage

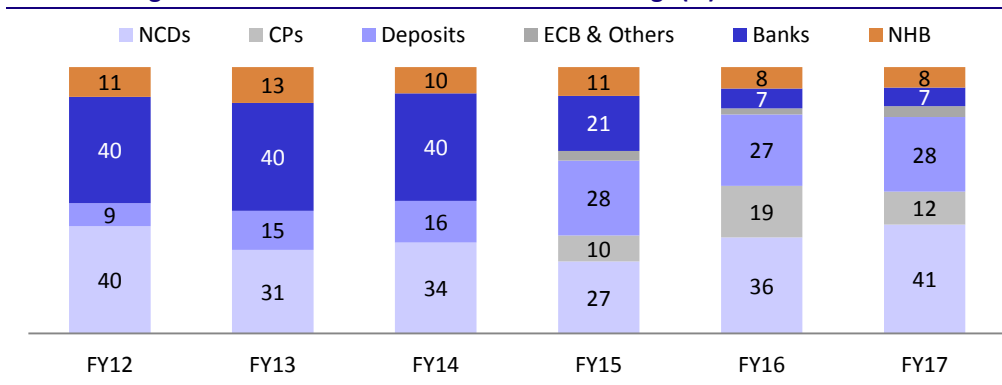
- Among all the companies under our coverage, PNBHF has the one of the most diversified liability profiles. We attribute this to its strong parentage and credit rating.
- The company has a healthy mix of retail and wholesale borrowings. Over FY14-17, PNBHF reduced the share of bank borrowings from 30%+ to 7%. At the same time, it started accessing the CP market, which now accounts for 12% of total borrowings.
- PNBHF is the second largest HFC in terms of public deposits, which account for 28% of total borrowings. However, more than half of its deposits come from non-retail sources.

Over the past four years, the company significantly diversified its liability mix, maintaining stable margins despite yield pressure

Strong liability franchise makes PNBHF a 'low-cost producer'

One of PNBHF's biggest strengths is its well-diversified liability franchise, which makes its cost of funds competitive versus the largest players in the industry. The company significantly reduced the share of bank borrowings from 34% in FY14 to 7% in FY17. It is a deposit-accepting HFC, with deposits comprising ~30% of its total borrowings. However, ~35% of its deposits come from the top 20 accounts. With the reduction in the share of bank borrowings and the corresponding increase in the share of market borrowings, the company has managed to reduce its cost of funds significantly.

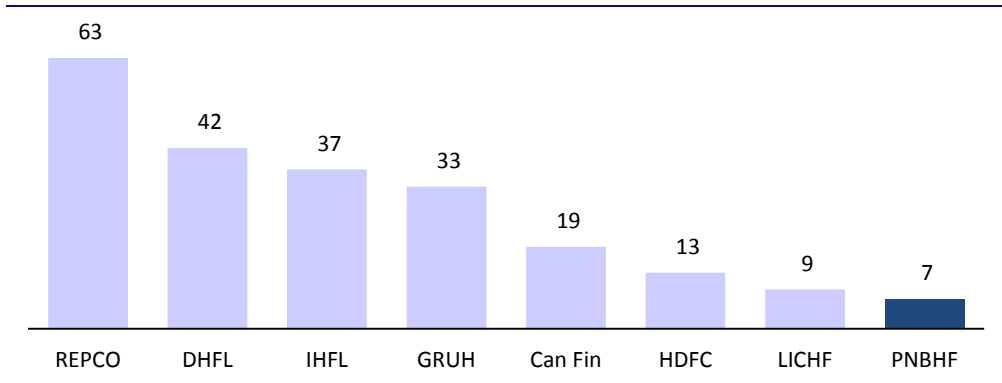
Exhibit 15: Significant reduction in share of bank borrowings (%)



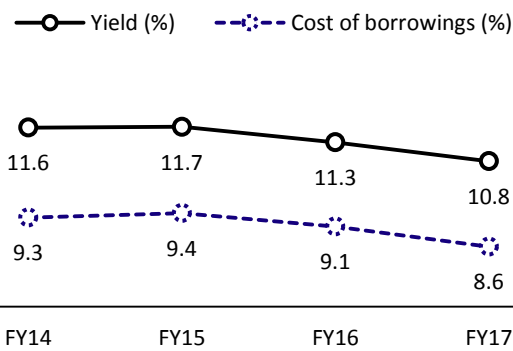
Source: Company, MOSL

PNBHF has the lowest share of bank borrowings versus peers, which gives it an edge on cost of funds

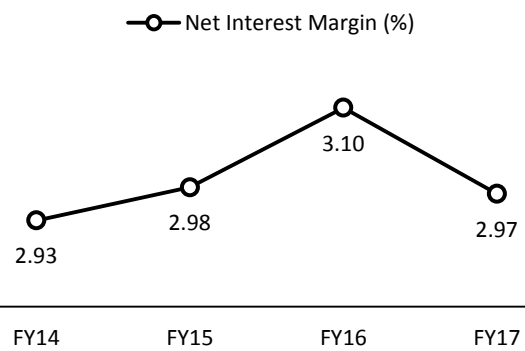
Exhibit 16: Share of bank borrowings versus peers (FY17, %)



Source: Company, MOSL

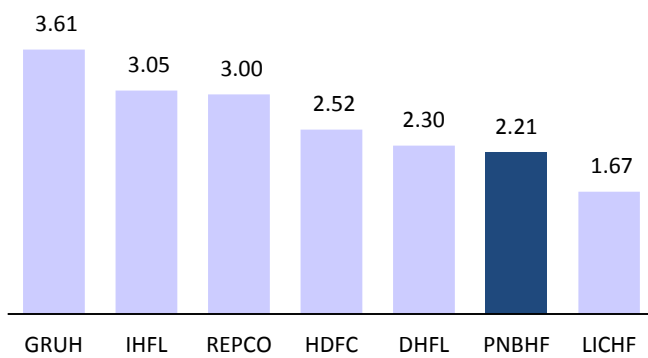
Exhibit 17: Both yields and CoF trending lower

Source: MOSL, Company

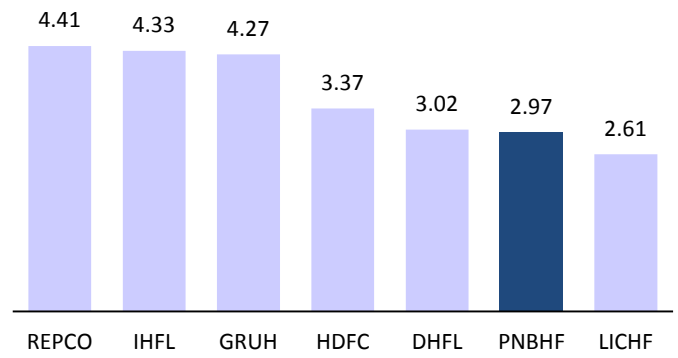
Exhibit 18: NIM has ranged close to 3%

Source: MOSL, Company

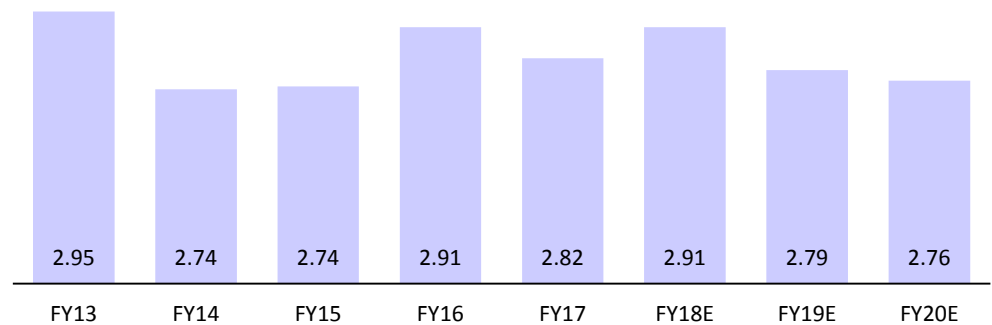
PNBHf lies in the middle of the range in terms of spreads vis-à-vis competitors.

Exhibit 19: Spread v/s peers – FY17 (%)

Source: MOSL, Company

Exhibit 20: Margins v/s peers – FY17 (%)

Source: MOSL, Company

Exhibit 21: Trend in margins (%)

Source: MOSL, Company

Operating leverage benefits to play out gradually

Over 20bp benefit in expense ratio expected over FY17-20

- Over the tenure of the business restructuring program, operating expenses remained elevated as PNBHF incurred several set-up costs, especially on the technology front.
- The benefits of the hub-and-spoke model have started to accrue, as is being driven largely by addition of spokes, with growth in the number of hubs slowing down.
- While the expense ratio declined from 120bp in FY15 to 98bp in FY17, we expect it to fall further to 75bp by FY20, largely driven by operating leverage benefits.

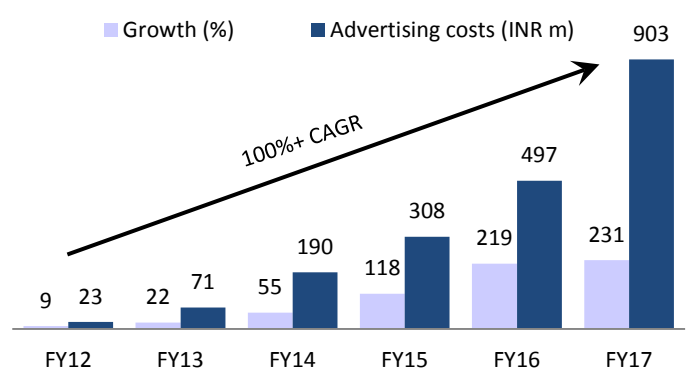
Loan acquisition cost is the key component of opex, amounting to 25% of total opex in FY17

High opex driven by loan acquisition costs

Over FY12-16, PNBHF incurred an opex CAGR of 65%, largely in line with the loan book CAGR. The company had invested significantly in setting up the front-end and back-end infrastructure. It also deployed 55 people and incurred INR550m in IT costs over the past few years. The company still has a long way to go in terms of efficiency improvement. The cost-to-income ratio (calculated) is elevated at 28%, higher than most peers. The key component of opex has been loan acquisition cost, which accounted for 25% of the company's total opex in FY17.

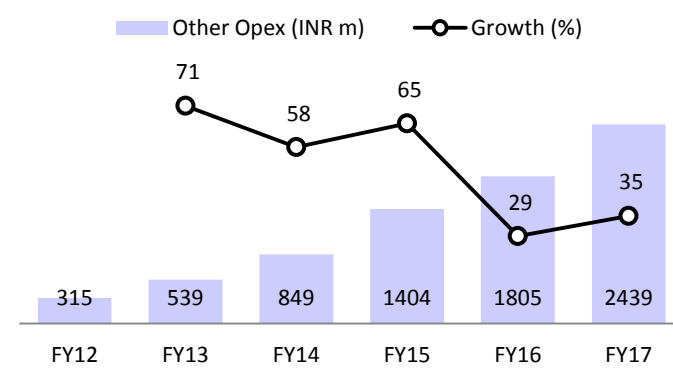
However, the company has been focusing on curbing other operating expenses and improving branch productivity. This is evident from the fact that growth in opex, excluding advertising and loan acquisition, has slowed down meaningfully over the past two years. In addition, branch productivity has improved, with AUM/branch doubling from INR3.3b in FY14 to INR6.6b in FY17. Due to this, there has been some improvement in the expense and C/I ratios over the past few years. We expect PNBHF to continue improving its cost structure as the benefits of operating leverage kick in with strong growth.

Exhibit 22: Advertising and loan acquisition cost trend



Source: MOSL, Company

Exhibit 23: Trend in other opex



Source: MOSL, Company; Other opex includes total opex less advertising and loan acquisition expenses

Cost structure elevated
compared to most peers

Exhibit 24: Cost-to-income ratio (calculated, FY17) is elevated compared to peers

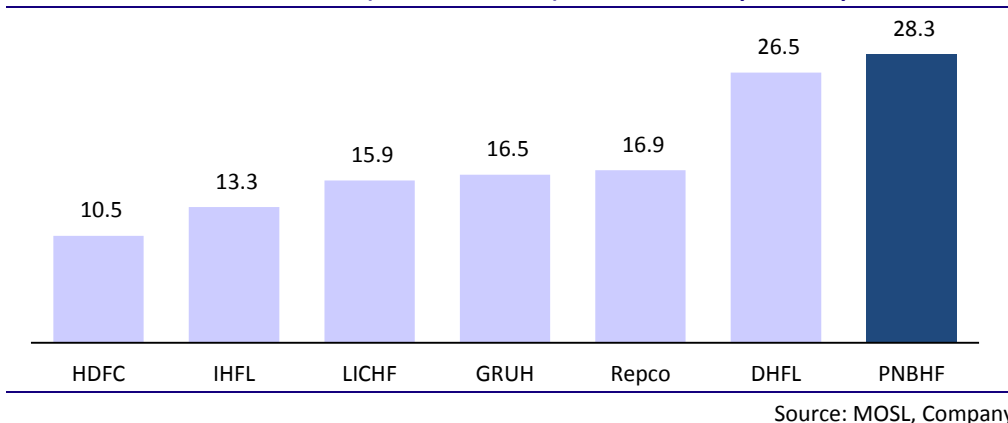
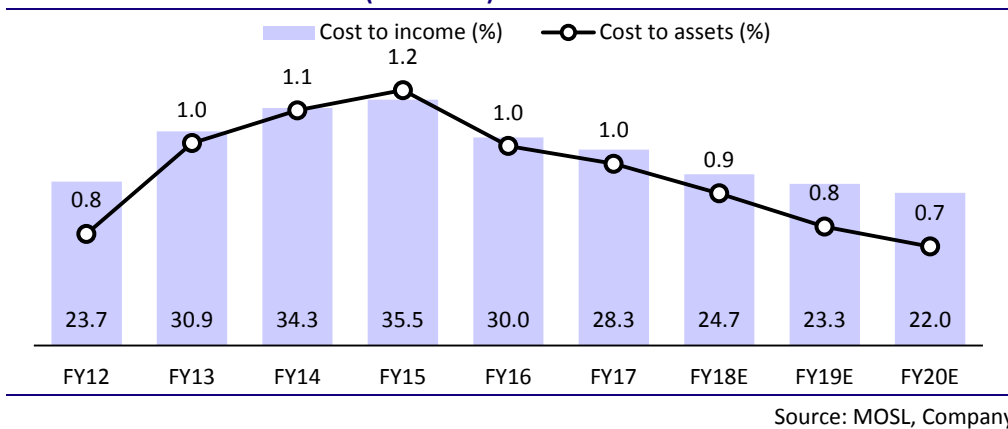


Exhibit 25: Cost-to-income ratio (calculated) to continue to decline



Pristine asset quality, Returns ratios to improve

RoE to reach 19% by FY20

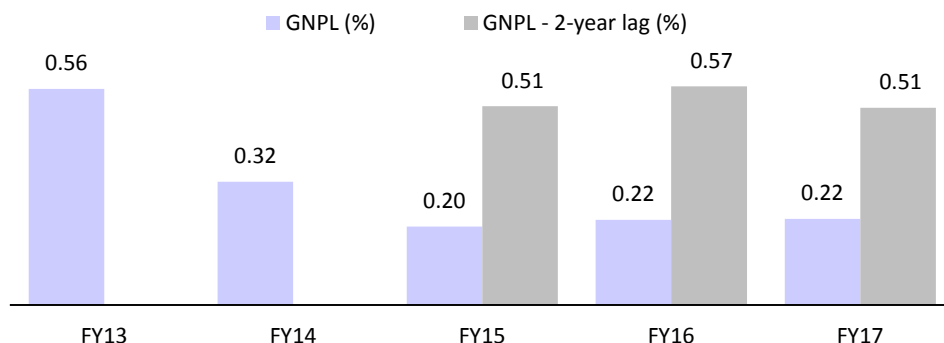
- Despite strong growth witnessed in the past five years, PNBHF has not been faced with any asset quality issues.
- The strength of its underwriting practices is evident from the fact that its GNPL in the corporate segment is nil. The company prefers to sacrifice yield (its incremental yield in the project finance segments is ~12%), but does not compromise on asset quality.
- While we expect the GNPL ratio to inch up marginally as the loan book seasons, we believe it will not have any material impact on the financials.
- We expect strong loan growth, stable margins/asset quality and operating leverage benefits to drive an improvement in the return ratios. We forecast 40% PAT CAGR over FY17-20, with RoA/RoE of 1.5%/19% in FY20.

With GNPA of 0.4% on a two-year lag basis, PNBHF's asset quality is best-in-class

Asset quality pristine; credit costs low

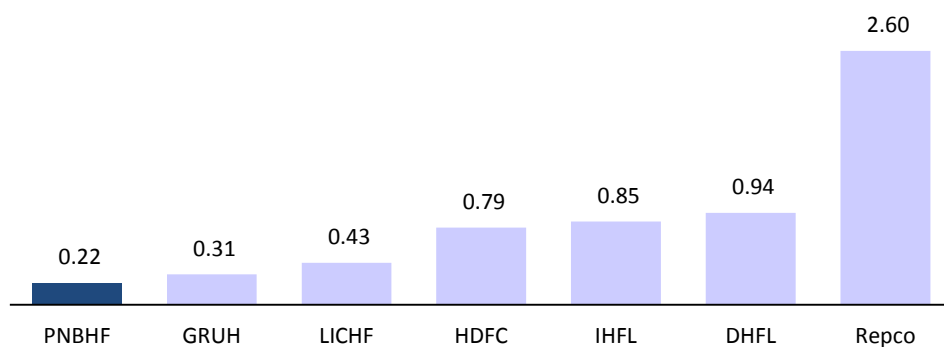
With the implementation of the business restructuring program, PNBHF has delivered superior loan growth relative to peers. Yet, it has not compromised on the underwriting standards. As a result, with a stable GNPA of 0.2% (FY17), its asset quality is best-in-class and comparable with private sector peers. However, since the portfolio has grown at a robust pace over the past few years, there could be a modest rise in delinquencies as the loan book seasons.

Exhibit 26: Pristine asset quality

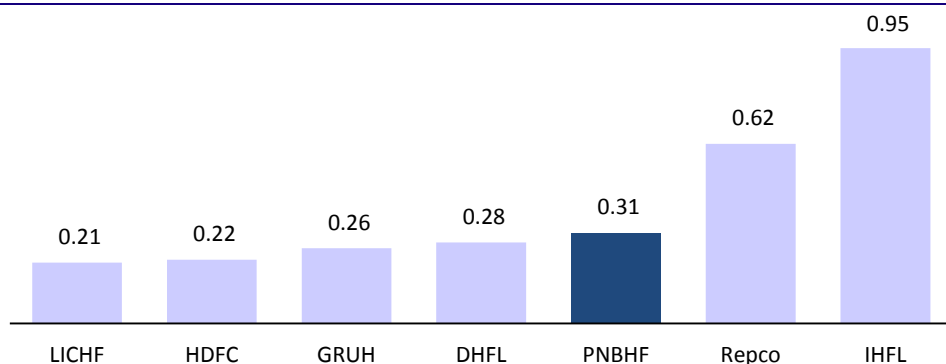


Source: MOSL, Company

Exhibit 27: GNPA as of FY17 (%) – Best-in-class asset quality



Source: MOSL, Company

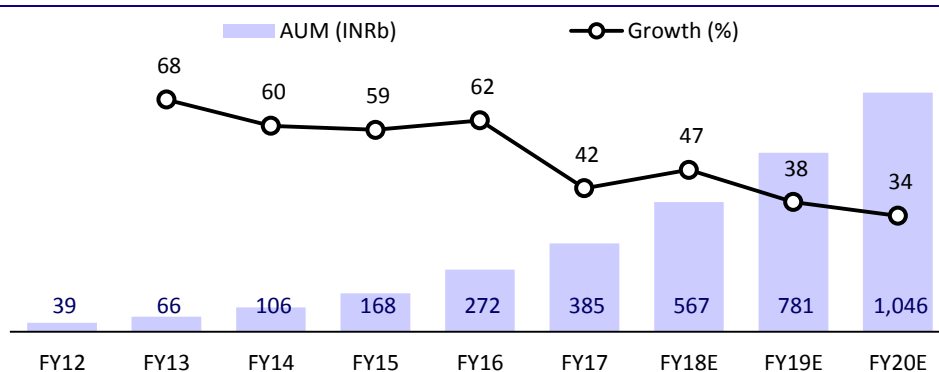
Exhibit 28: FY17 credit costs – comparison v/s peers

Source: MOSL, Company

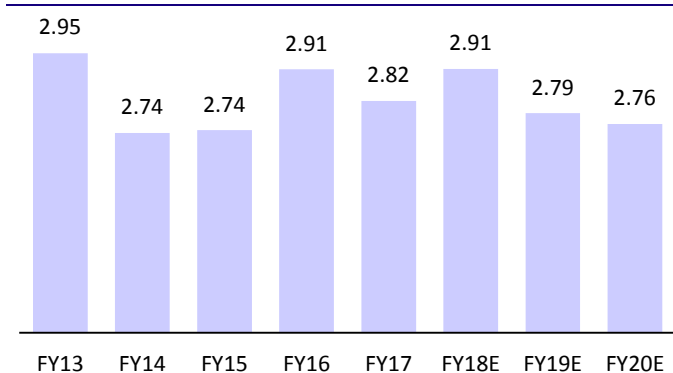
Reduction in expense ratio
to drive improvement in
return ratios

Triggers in place for improving return ratios

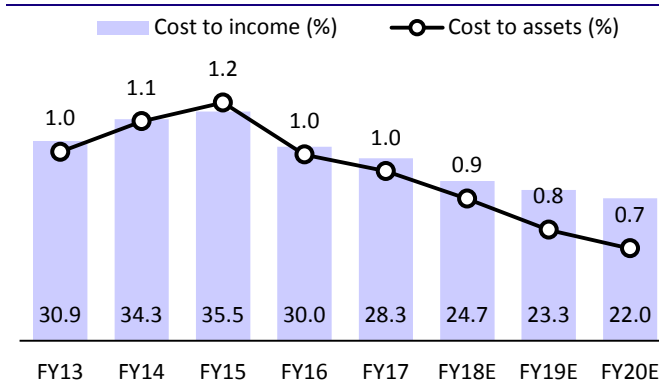
Over FY13-16, PNBHF generated consistent RoA of 1.3-1.5% and RoE of 16-18%. In FY17, however, RoE declined to 14% due to large capital infusion. With the benefits of operating leverage kicking in, coupled with higher financial leverage, we expect RoE to return to pre-IPO levels in the next 2-3 years. We forecast RoA/RoE of 1.5%/19% by FY20. Given the strong growth outlook, we believe the company would look to raise capital in FY19 or FY20. However, our estimates do not include the impact of any capital raise.

Exhibit 29: AUM growth to continue remaining strong over the medium term

Source: MOSL, Company

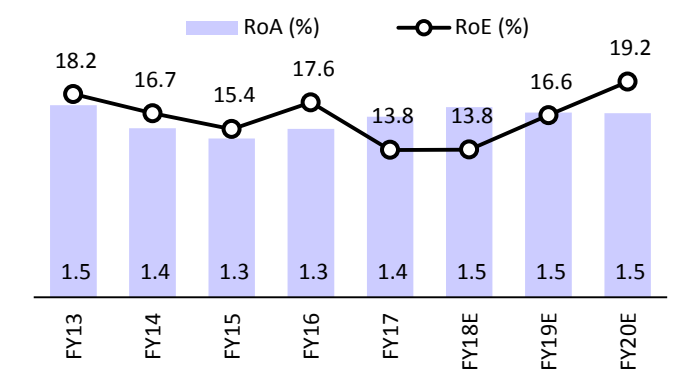
Exhibit 30: Margins to remain stable (%)

Source: MOSL, Company

Exhibit 31: Opex benefits to accrue

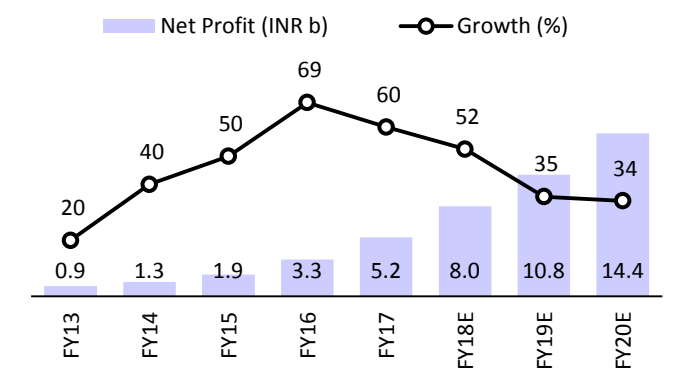
Source: MOSL, Company

Exhibit 32: Return ratios poised to pick up



Source: MOSL, Company

Exhibit 33: 40% PAT CAGR over FY17-20E



Source: MOSL, Company

Exhibit 34: DuPont Analysis

	2013	2014	2015	2016	2017	2018E	2019E	2020E
Interest Income	10.50	11.00	10.93	10.46	10.03	9.41	9.41	9.49
Interest Expended	7.64	8.35	8.28	7.64	7.29	6.57	6.69	6.80
Net Interest Income	2.86	2.65	2.66	2.82	2.75	2.83	2.72	2.69
Other Income	0.52	0.67	0.72	0.63	0.74	0.81	0.73	0.70
Net Income	3.38	3.32	3.37	3.45	3.48	3.64	3.44	3.38
Operating Expenses	1.04	1.14	1.20	1.04	0.98	0.90	0.80	0.75
Operating Profit	2.34	2.18	2.18	2.41	2.50	2.74	2.64	2.64
Provisions/write offs	0.21	0.32	0.25	0.34	0.28	0.40	0.37	0.37
PBT	2.13	1.86	1.93	2.07	2.22	2.34	2.27	2.27
Tax	0.59	0.51	0.66	0.73	0.77	0.82	0.79	0.79
Reported PAT	1.54	1.35	1.27	1.35	1.44	1.52	1.48	1.47
Leverage	11.88	12.37	12.16	13.07	9.54	9.08	11.22	13.06
RoE	18.24	16.71	15.45	17.58	13.78	13.81	16.56	19.22

Source: MOSL, Company

Exhibit 35: DuPont Analysis (FY16) – Higher cost structure a drag on profitability

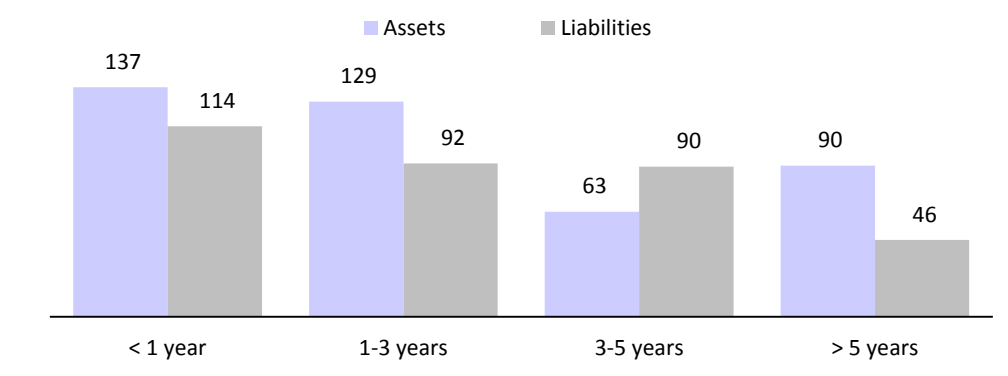
	PNBHF	IHFL	GRUH	LICHFC	Repco	DHFL	HDFC
Interest Income	10.03	12.28	11.91	10.79	12.07	10.51	9.87
Interest Expended	7.29	7.57	7.61	7.96	7.69	8.57	6.69
Net Interest Income	2.75	4.71	4.31	2.84	4.38	1.94	3.18
Non interest Income	0.74	1.54	0.39	0.16	0.38	0.90	0.61
Net Income	3.48	6.25	4.69	2.99	4.76	2.84	3.79
Operating Expenses	0.98	0.90	0.77	0.48	0.80	0.75	0.43
Cost to income (%)	28.26	14.35	16.48	15.89	16.91	26.47	11.30
Operating Profits	2.50	5.35	3.92	2.52	3.95	2.09	3.36
Provisions/write offs	0.28	0.90	0.27	0.22	0.62	0.28	0.14
PBT	2.22	4.45	3.65	2.30	3.33	1.81	3.23
Tax	0.77	1.02	1.20	0.80	1.17	0.61	1.05
Tax rate	34.86	22.88	32.91	34.67	34.95	14.10	32.56
PAT	1.44	3.44	2.45	1.50	2.17	1.19	2.18
Leverage	9.54	7.42	13.24	12.95	8.03	12.03	8.82
RoE	13.78	25.50	32.46	19.45	17.42	14.37	21.00

Source: MOSL, Company

Asset-liability management

The company is conservative in maintaining its ALM, with assets exceeding liabilities comfortably in its 0-3 year bucket. This would help the company maintain operations smoothly in times of liquidity tightening.

Conservative ALM

Exhibit 36: Maturity pattern of assets and liabilities (INR b)

Source: MOSL, Company

SWOT analysis



Bull & Bear case



Bull Case

- ✓ In our bull case, we assume strong AUM CAGR of 41% (v/s base case of 37%). We believe the CF and LAP segments could surprise on the upside.
- ✓ We expect margins to increase modestly to 3%.
- ✓ We expect significant cost control, with cost-to-income ratio declining to 19% by FY20 (v/s 22% in base case).
- ✓ Asset quality would be slightly better with GNPA of 0.4% by FY20 (v/s 0.5% in base case).
- ✓ This results in PAT CAGR of 50% (vs. 40% in base case) over FY17-20, with RoA/RoE in FY20 equal to 1.7%/23%.
- ✓ Based on the above assumptions, our bull case target multiple is 5x FY19 BV, implying an upside of 52%.



Bear Case

- ✓ In our bear case, we assume AUM CAGR of 27% (vs. base case of 37%). Slowdown in the non-core segments could lead to such a scenario.
- ✓ We expect margins to remain stable at 2.8%.
- ✓ We expect no cost control, with cost-to-income ratio remaining largely stable at ~27-28% over FY17-20 (v/s 22% by FY20 in base case).
- ✓ Asset quality would worsen, with GNPA of 1.2% by FY20 (v/s 0.5% in base case).
- ✓ This results in PAT CAGR of 27% (vs. 40% in base case) over FY17-20, with RoA/RoE in FY20 equal to 1.3%/15%.
- ✓ Based on the above assumptions, our bear case target multiple is 3x FY19E BV, implying a downside of 14%.

Exhibit 37: Scenario Analysis – Bull Case

Bull Case	FY18E	FY19E	FY20E
NII	15,281	22,074	30,261
Opex	4,715	5,737	6,982
Provisions	1,934	2,476	3,473
PBT	12,987	19,519	27,233
PAT	8,441	12,687	17,702
NIM (%)	3.0	3.0	2.9
Cost to assets (%)	0.9	0.8	0.7
RoA (%)	1.6	1.7	1.7
RoE (%)	14.6	19.1	22.6
EPS	51	77	107
BV	370	430	515
Target multiple	5		
Target price (INR)	2,152		
Upside	52%		

Source: Company, MOSL

Exhibit 38: Scenario Analysis – Bear Case

Bear Case	FY17E	FY18E	FY19E
NII	14,140	17,652	22,097
Opex	4,715	6,033	7,725
Provisions	2,271	2,987	3,781
PBT	11,007	13,284	16,339
PAT	7,155	8,635	10,620
NIM (%)	2.9	2.8	2.8
Cost to assets (%)	0.9	0.9	0.9
RoA (%)	1.4	1.3	1.3
RoE (%)	12.5	13.6	14.9
EPS	43	52	64
BV	364	405	456
Target multiple	3		
Target price (INR)	1,215		
Upside	-14%		

Source: Company, MOSL

Valuation and view

Superior execution + Strong growth + Healthy return ratio = Premium Valuations

- Over the past six years, PNBHF has scripted an enviable turnaround, positioning itself to become the fifth largest player in the HFC segment. Strong underwriting and execution skills have ensured that growth has not come at the cost of asset quality.
- The company has been able to offset the pressure on yields and high opex with superior liability management and asset mix.
- Strong loan growth, stable margins and moderating expense ratio should drive 40% PAT CAGR over FY17-20. RoE is expected to improve from 13.6% in FY17 to 19% in FY20.
- Stock trades at 3.4x FY19E P/B and 21.7x FY19E P/E. With strong macro factors supporting and geographical diversification, we expect strong AUM CAGR of 40% over FY17-20. Strong operating leverage will negate the expected rise in credit cost. Overall we expect stable ROAs and improving RoEs will rising financial leverage. Superior execution, strong EPS growth and healthy return ratios/asset quality will ensure premium valuations to sustain. We thus initiate coverage on the company with a Buy rating and a target price of INR1,675 (22x Sep 2019E EPS), implying 3.7x Sep2019E BVPS.

Over the past six years, PNBHF has scripted an enviable turnaround. The company has registered strong loan growth across segments. Loan book CAGR over FY12-17 was 60%, driven by increased market penetration and expansion into new territories. Consequently, its market share increased from ~0.5% to 2%+ over the same time period, making it the fifth largest HFC in India.

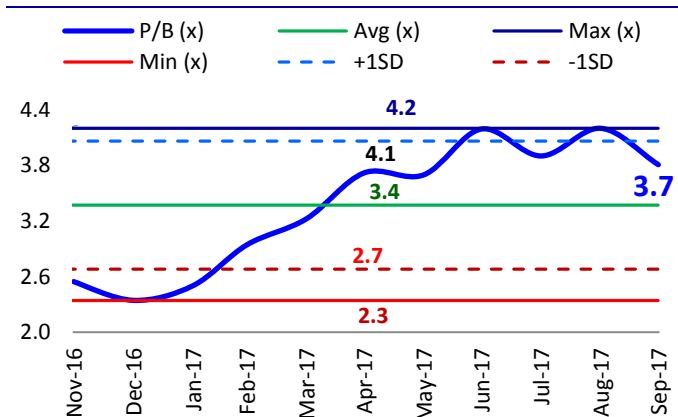
Strong growth, diversified liability franchise and best-in-class asset quality are some of the key strengths of the company

With a diversified liability franchise and minimal dependence on bank borrowings, the company has been able to offset intense yield pressure and maintain spreads. Over the past few years, the company has invested significantly in upgrading its technology. In addition, the company uses a unique hub-and-spoke model, with which it will be able to deliver strong loan growth with lower opex growth. As a result, we expect operating leverage benefits to accrue over the medium term. We expect opex/average assets to decline from 98bp in FY17 to 75bp in FY20.

PNBHF has best-in-class asset quality with GNPL ratio of 0.2% in FY17 (0.5% on a 2-year lag basis). It has the distinction of being the only HFC with nil NPL in the construction finance book. Additionally, 88% of projects funded by the company have witnessed sales velocity in excess of the company's assumptions.

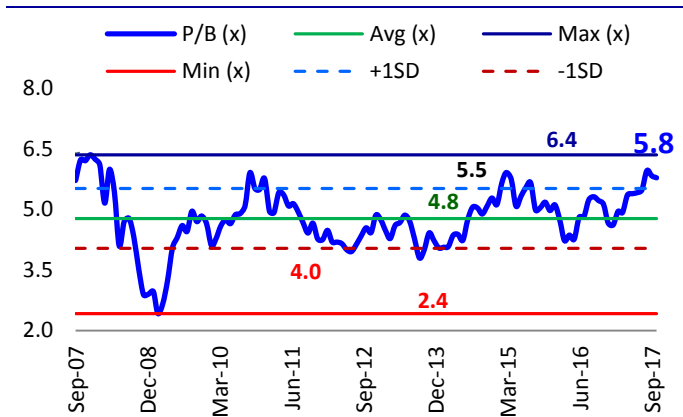
Strong loan growth, stable margins and moderating expense ratio should drive 40% PAT CAGR over FY17-20, in our view. RoE is expected to improve from 13.6% in FY17 to 19% in FY20. While the stock trades at a premium valuation of 3.4x FY19E P/B and 21.7x FY19E P/E, we believe this is justified, given its strong earnings growth over the foreseeable future. We use RI model to value to company, with Rf of 7%, CoE of 13.5% and terminal growth rate of 5%. We initiate coverage with a Buy rating, valuing the stock at INR1,675 (22x Sep 2019E EPS), implying 3.7x Sep2019E BVPS.

Exhibit 39: PNBHF P/B chart



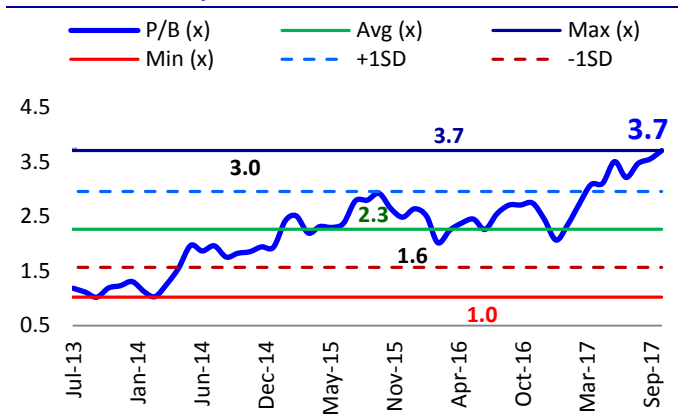
Source: MOSL, Company

Exhibit 40: HDFC P/B chart



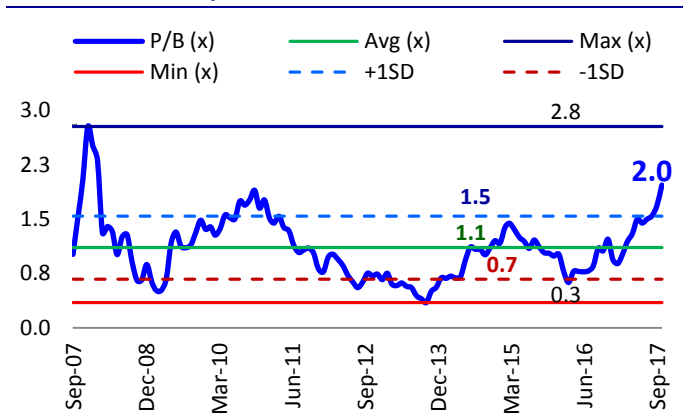
Source: MOSL, Company

Exhibit 41: IHFL P/B chart



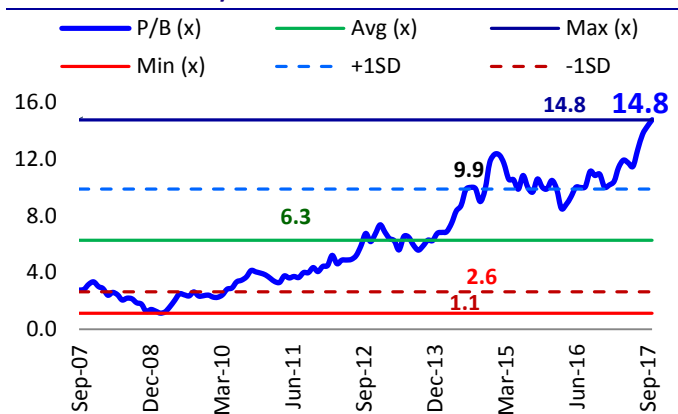
Source: MOSL, Company

Exhibit 42: DHFL P/B chart



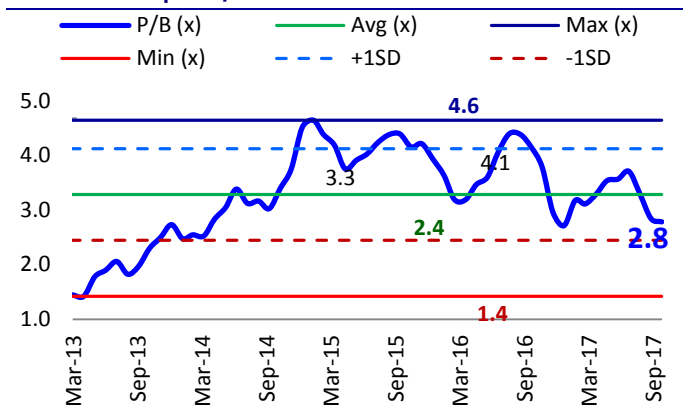
Source: MOSL, Company

Exhibit 43: GRUH P/B chart



Source: MOSL, Company

Exhibit 44: Repco P/B chart



Source: MOSL, Company

Key risks

Increasing share of commercial real estate exposure

As per disclosures in the FY17 Annual Report, the exposure to commercial real estate increased multi-fold from INR46b in FY16 to INR114b in FY17. However, as per management, this is due to reclassification of construction finance from residential exposure in FY16 to commercial exposure in FY17. Yet, we believe that this could pose asset quality issues in the future, especially if the commercial real estate environment remains subdued.

Operating leverage may not play out with network expansion

Currently, PNBHF operates in the larger towns and cities. However, as it migrates more into semi-urban areas, the average ticket size is expected to decline. As a result, to maintain growth, volumes will have to be stronger and in order to support volumes, there would have to be more investments. Hence, it is possible that operating leverage does not play out.

Strong AUM growth – Portfolio seasoning a key risk

The company enjoys a superior GNPL ratio of 0.4%. However, one of the reasons for this is that the portfolio is not fully seasoned. Also, some project loans could be in the moratorium period. With further seasoning of the loan book, there is a possibility that the GNPL ratio increases.

Higher share of bulk deposits in Public deposits

The top 20 depositors constitute 35% of the company's total deposits, implying a large share of chunky deposits. In addition, deposits are a significant source of borrowings for the company, constituting 25% of total borrowings. Any contraction in liquidity in the system could hamper PNBHF's ability to raise money from deposits, and thus, impact growth.

Company Background

PNBHF is the fifth largest housing finance company (HFC) in India in terms of loan book size (INR468b as of June 2017). It has a diverse product suite offering retail home loans, loans against property (LAP), corporate term loans, non-residential property loans, construction finance, and lease rental discounting (LRD). It conducts operations from a network of 66 branches and 18 processing units. PNBHF was incorporated in 1988 as a subsidiary of Punjab National Bank (PNB). In 2009, PNB sold 26% stake to Destimoney Enterprises (now a Carlyle Group entity). In 2012, Destimoney Enterprises increased its stake to 49%.

Management details



Mr Sunil Mehta – Non-Executive Chairman

Mr Sunil Mehta is the MD & CEO of Punjab National Bank. He is a seasoned banker with over 35 years of rich experience in various administrative and functional capacities at branches, zonal offices and also at the head office level. Prior to assuming the position of MD & CEO of Punjab National Bank, he was Executive Director of Corporation Bank. He is a Post Graduate in Agriculture, MBA in Finance and a Certified Associate of Indian Institute of Bankers (CAIIB).



Mr Sanjaya Gupta - Managing Director

Mr Gupta joined the company in 2010 as Managing Director. Previously, he served as the Country Head and CEO of the Prospective Mortgage Guaranty Business in India at AIG United Guaranty; as the National Product Head, Mortgages - Consumer Banking at ABN Amro Bank NV; and as the VP Mortgages at ABN AMRO Central Enterprise Services Private Limited. Mr Gupta worked for 16 years with HDFC Ltd. He holds a BCom and an MBA from Lucknow University.



Mr Jayesh Jain - Chief Financial Officer

Mr Jain has been with PNBHF since August 2014. He holds a BCom and is a CA. He is a Fellow Member of the ICAI, and a Certified Information Systems Auditor and a Certified Information Security Manager from the Information Systems Audit and Control Association, USA. Previously, he served as the CFO of GRUH Finance Limited and has over 15 years of experience in the housing finance industry.



Mr Shaji Varghese – Executive Director, Business Development

Mr Varghese has been with PNBHF since February 2012. He has more than 17 years of experience in retail assets, liabilities and wealth management. Prior to joining PNBHF, he was Senior VP at IndusInd Bank. He holds a Bachelor's Degree in Law from the Bharati Vidyapeeth New Law College, University of Pune. He also holds a Diploma in Business Management from the Bharati Institute of Management, University of Pune. He holds a Master's Degree in Management Science from the University of Pune.

Financials and valuations

Income statement								(INR Million)
Y/E March	2013	2014	2015	2016	2017	2018E	2019E	2020E
Interest Income	6,346	10,559	16,708	25,461	36,401	49,305	68,804	93,066
Interest Expended	4,620	8,016	12,648	18,603	26,437	34,456	48,942	66,703
Net Interest Income	1,727	2,543	4,060	6,858	9,964	14,848	19,863	26,363
Change (%)	33.7	47.3	59.6	68.9	45.3	49.0	33.8	32.7
Other Operating Income	317	644	1,095	1,534	2,678	4,225	5,302	6,827
Net Income	2,044	3,187	5,155	8,393	12,642	19,073	25,165	33,190
Change (%)	39.4	56.0	61.8	62.8	50.6	50.9	31.9	31.9
Operating Expenses	631	1,093	1,830	2,521	3,573	4,715	5,872	7,316
Operating Income	1,412	2,094	3,326	5,872	9,069	14,358	19,292	25,874
Change (%)	26.2	48.3	58.8	76.6	54.5	58.3	34.4	34.1
Provisions/write offs	125	304	381	832	1,029	2,096	2,697	3,654
PBT	1,287	1,790	2,945	5,040	8,040	12,263	16,595	22,220
Tax	359	493	1,004	1,766	2,803	4,292	5,808	7,777
Tax Rate (%)	28	28	34	35	35	35	35	35
Reported PAT	928	1,297	1,941	3,273	5,237	7,971	10,787	14,443
Change (%)	19.9	39.7	49.6	68.7	60.0	52.2	35.3	33.9
Proposed Dividend	120	176	290	486	1,196	1,664	2,252	3,016

Balance sheet								(INR Million)
Y/E March	2013	2014	2015	2016	2017	2018E	2019E	2020E
Capital	500	657	1,038	1,269	1,656	1,656	1,656	1,656
Reserves & Surplus	5,680	8,684	14,749	20,190	52,921	59,227	67,762	79,189
Net Worth	6,180	9,341	15,787	21,459	54,577	60,883	69,418	80,845
Borrowings	45,954	66,577	104,158	116,087	165,561	531,929	739,281	993,274
Borrowings	66,954	101,077	164,808	260,137	354,971	531,929	739,281	993,274
Change (%)	73.5	51.0	63.1	57.8	36.5	49.9	39.0	34.4
Other liabilities	3,417	4,978	9,695	14,809	19,579	26,431	34,360	44,669
Total Liabilities	76,551	115,396	190,290	296,405	429,127	619,243	843,059	1,118,788
Loans	66,008	105,660	168,006	271,813	385,452	567,088	781,481	1,045,552
Change (%)	67.2	60.1	59.0	61.8	41.8	47.1	37.8	33.8
Investments	7,769	6,455	15,860	16,223	32,796	36,075	39,683	43,651
Change (%)	105.4	-16.9	145.7	2.3	102.2	10.0	10.0	10.0
Net Fixed Assets	177	288	577	622	604	619	635	651
Other assets	2,596	2,993	5,847	7,747	10,275	15,460	21,261	28,934
Total Assets	76,551	115,396	190,290	296,405	429,127	619,243	843,059	1,118,788

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	2013	2014	2015	2016	2017	2018E	2019E	2020E
Spreads Analysis (%)								
Avg yield on loans	11.5	11.7	11.7	11.2	10.6	9.9	9.8	9.8
Avg. cost of funds	8.8	9.5	9.5	8.8	8.6	7.8	7.7	7.7
Interest Spread	2.1	1.8	1.8	2.0	1.7	1.9	2.0	2.0
Net Interest Margin	3.0	2.7	2.7	2.9	2.8	2.9	2.8	2.8
Profitability Ratios (%)								
RoE	18.2	16.7	15.4	17.6	13.8	13.8	16.6	19.2
RoA	1.54	1.35	1.27	1.35	1.44	1.52	1.48	1.47
Int. Expended/Int.Earned	72.8	75.9	75.7	73.1	72.6	69.9	71.1	71.7
Other Inc./Net Income	15.5	20.2	21.2	18.3	21.2	22.2	21.1	20.6
Efficiency Ratios (%)								
Op. Exps./Net Income	30.9	34.3	35.5	30.0	28.3	24.7	23.3	22.0
Empl. Cost/Op. Exps.	40.3	37.0	36.6	29.9	28.3	27.5	27.6	27.7
Asset Quality (%)								
Gross NPAs	371	337	341	598	858	1,821	3,239	5,193
Gross NPAs to Adv.	0.6	0.3	0.2	0.2	0.2	0.3	0.4	0.5
Net NPAs	0	164	114	381	590	1,184	2,105	3,375
Net NPAs to Adv.	0.0	0.2	0.1	0.1	0.2	0.2	0.3	0.3

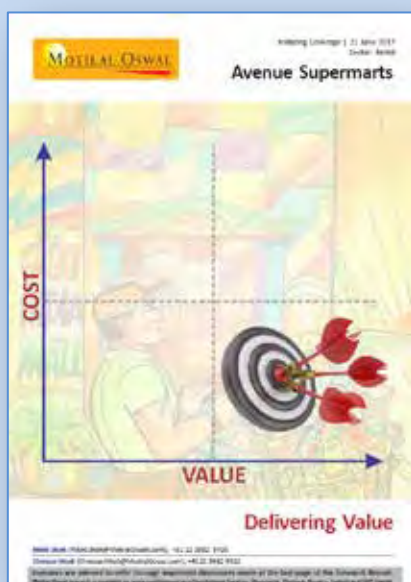
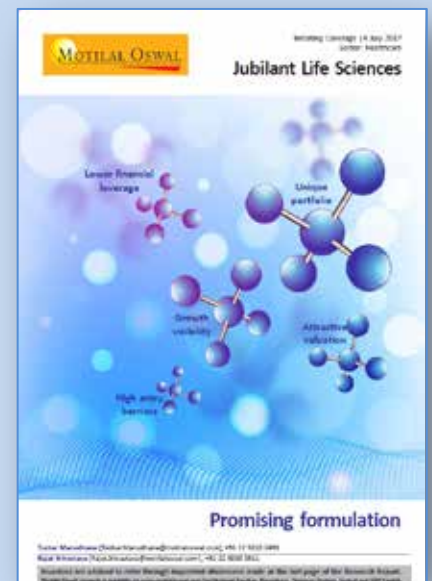
VALUATION

Book Value (INR)	123.6	142.2	152.0	169.1	329.5	367.6	419.1	488.1
Price-BV (x)					4.3	3.8	3.4	2.9
EPS (INR)	18.6	19.7	18.7	25.8	31.6	48.1	65.1	87.2
EPS Growth YoY	-28.1	6.4	-5.3	38.0	22.6	52.2	35.3	33.9
Price-Earnings (x)					44.7	29.3	21.7	16.2
Dividend per share (INR)	2.5	3.0	3.0	3.4	6.0	8.7	11.7	15.7
Dividend yield (%)					0.4	0.6	0.8	1.1

E: MOSL Estimates

REPORT GALLERY

RECENT INITIATING COVERAGE REPORTS



NOTES

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