Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

LIC Housing Finance

Improving demand outlook, strong fundamentals

Banks & Finance | Sharekhan code: LICHSGFIN | Company Update

Stock Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 371**	
Price Target: **Rs. 440**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 18,700 cr
52-week high/low:	Rs. 486/186
NSE volume: (No of shares)	58.8 lakh
BSE code:	500253
NSE code:	LICHSGFIN
Free float: (No of shares)	30.1 cr

Shareholding (%)

Promoters	40.3
FII	35.0
DII	12.7
Others	12.1

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-1.5	7.0	13.8	-25.8
Relative to Sensex	-1.5	-5.3	-11.7	-30.4

Sharekhan Research, Bloomberg

Summary

- LIC Housing Finance (LICHF) is an attractive player in the housing mortgage market, with high credit ratings (margin support), improving disbursements and better collections efficiency.
- Home loan disbursements are improving, recovered to normalized levels during Q2, and the recent healthy demand augurs well for the home finance market as well.
- We have fine-tuned our estimates and believe the outlook for LICHF has improved; valuations at 1.05x/0.91x its FY2022E and FY2023E BVPS are reasonable considering its high return ratios and stable asset quality.
- We maintain our Buy rating on the stock with a revised PT of Rs. 440.

LIC Housing Finance (LICHF) is an attractive player in the housing mortgage market, with positives such as high credit ratings (results in lower borrowing costs), improving disbursements, and better collections efficiency in its favour. Home loan disbursements recovered to normalised levels during the last quarter, and the recent healthy offtake in the housing sector (seen in November) augurs well for the home finance market as well. The company had recorded 22% and 38% y-o-y growth in home loan disbursements in September and October, respectively, which we believe is encouraging and demand outlook is improving. Further, collection efficiency of 96% in September 2020 is reassuring as well. Historically, home mortgages have been a resilient segment in terms of asset quality; and the developer segment at <8% of book we believe is manageable. The share of retail home loans was flat sequentially at ~76.5%, while the share of developer finance inched up to 7.2% on disbursement of sanctioned loans. The HFC has kept the loan mix stable over the past six quarters – a positive in this environment. LICHF indicated confidence of business traction in the coming quarters. Moreover, recovery/resolution in H2 of some exposures (were at advanced stages) will help further bring down the provision burden. LICHF has strengths in its borrowing profile and has been able to bring down its cost of funds, helped by its strong parent profile.

The recent fall in borrowing costs, which was steep for high-rated NBFCs, is another positive in its favour. We expect repricing benefit (H2 Rs. 16,500 crore at present coupon of ~8.5%; FY2022E Rs. 26,000 crore at present coupon of 8.2%) which will lower Cost of Funds, due to which we expect NIMs to be stable (with a positive bias) going forward. We believe conservative LTVs and inexpensive valuations make risk return favourable. LICHF may have to raise capital to be able to attain the first benchmark of minimum ~15% capital adequacy. However, as per an exception provided by the RBI, the company could pay dividends if it raises capital during the current year. We believe capital raising will help augment the HFC's balance sheet. We have fine-tuned our estimates and believe the outlook for LICHF has improved. At present, LICHF is at 1.05x/0.91x its FY2022E and FY2023E ABVPS, which we believe is reasonable. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 440.

Our Call

We believe valuations at 1.05x/0.91x its FY2022E and FY2023E ABVPS are reasonable considering its high return ratios and stable asset quality. LICHF has comfortable access to liquidity and enjoys high credit ratings and is well placed to manage the expected competitive intensity in the home loan segment and is likely to be able to keep margins steady (with a positive bias). The pall of the pandemic is lifting and healthy traction is encouraging. Asset-quality outlook (aided by conservative LTV ratios) along with normalising business traction (improving faster than earlier envisaged) improves the company's overall outlook. LICHF has strengths in its borrowing profile and has been able to bring down its cost of funds, helped by its strong parent profile. We believe conservative LTVs and inexpensive valuations make it a reasonably attractive investment. We have fine-tuned our estimates and believe the outlook for LICHF has improved. The stock is still down ~24% from its highs and we believe risk reward is favourable for long-term investors. We maintain our Buy rating on the stock with a revised PT of Rs. 440.

Key Risks

Increased delinquencies in the developer book may worsen asset quality and affect profitability.

Valuation Rs cr

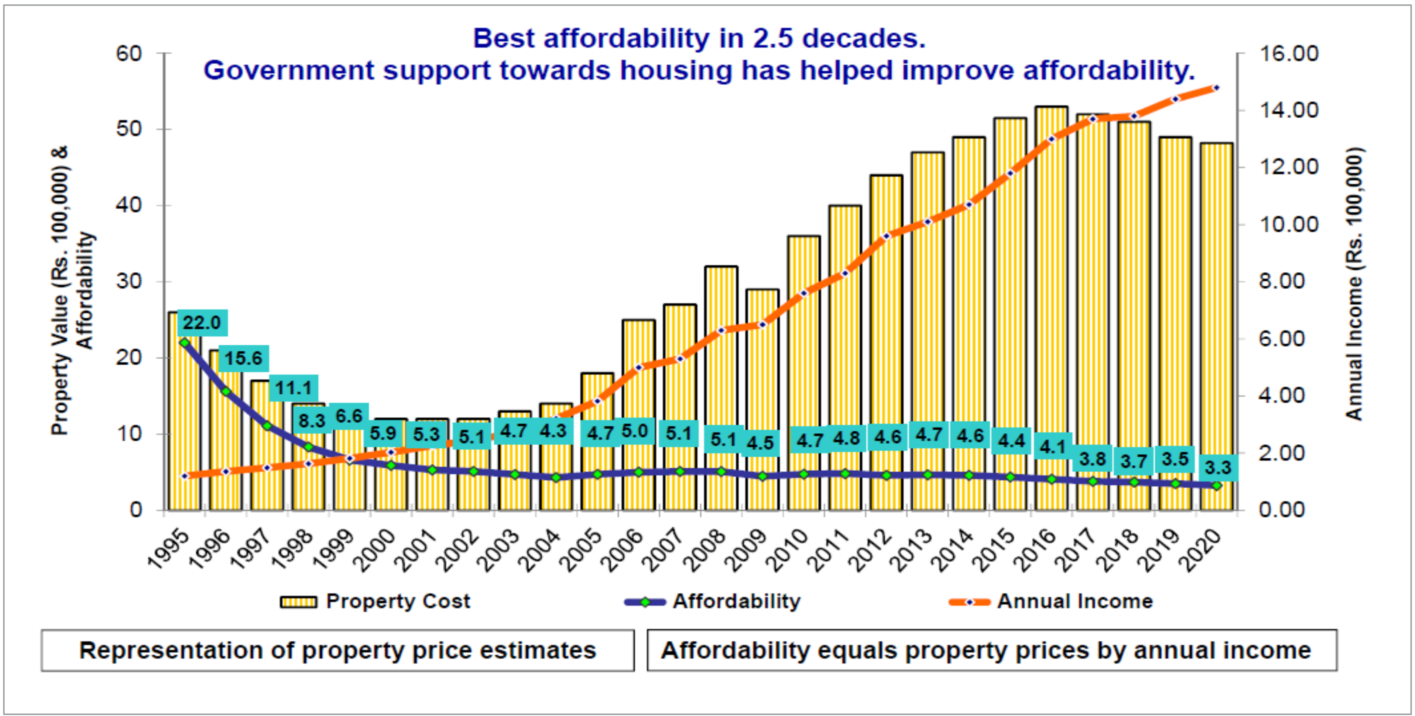
Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net interest income	4,349.9	4,689.0	5,786.8	6,569.1	7,186.6
Net profit	2,431.0	2,401.8	3,098.9	3,527.8	3,704.1
EPS (Rs.)	48.1	47.6	61.4	69.9	73.4
P/E (x)	7.7	7.8	6.0	5.3	5.0
Adj. book value (Rs./share)	315.8	302.0	351.1	407.0	465.7
P/ABV (x)	1.17	1.23	1.05	0.91	0.79
RoAE (%)	16.8	15.9	17.2	17.0	15.6
RoAA (%)	1.46	1.38	1.66	1.66	1.48

Source: Company; Sharekhan estimates

Long-term structural tailwinds present for the Indian home mortgage sector

The Indian housing mortgage industry has long-term structural tailwinds to support its growth. Housing has become increasingly affordable over the years due to rising per capita income, as well as increasing affordability due to low interest rates. Moreover, easy availability of mortgage products and a young demography are positive growth drivers.

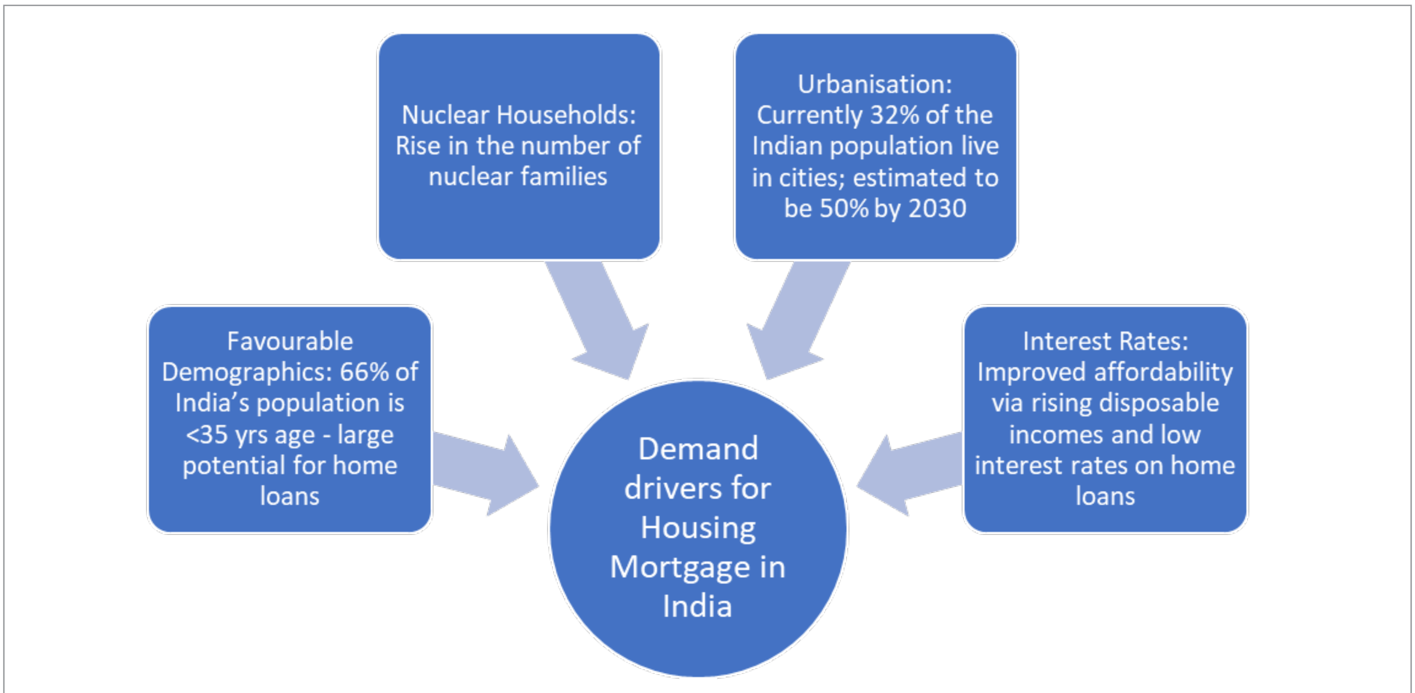
Improved affordability – Falling property costs versus rising incomes



Source: Company

In the past few years, property prices in India have generally not gone up, which we believe will in turn fuel demand for home loans. Income levels have gone up and, therefore, the cost of a house as a multiple of annual income of a customer has declined making it more affordable.

Demand drivers in place

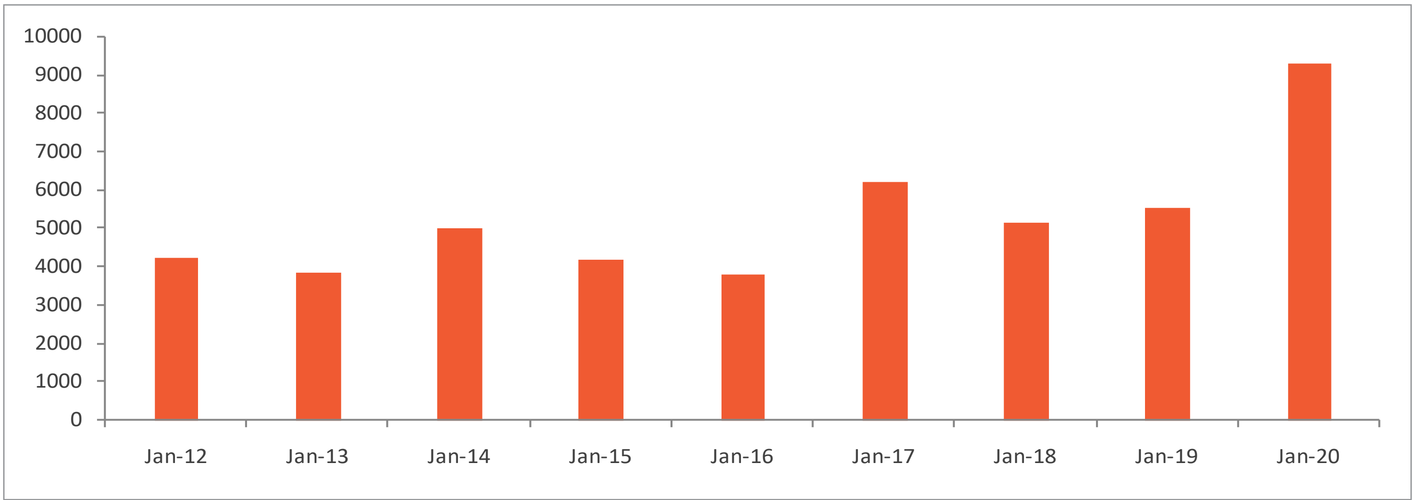


Source: Company, Sharekhan Research

Healthy pickup in home sales augurs well for Housing Mortgage sector

Post the severe decline in Q1FY2021, the housing segment has witnessed a sharp recovery in Q2FY2021. Sales across the top eight cities of India rebounded in Q2, indicating some green shoots of normalisation. At 9,301 units registered in November 2020, the residential sector of Mumbai recorded the highest-ever registrations in November over the past 9 years.

Property sales (in Mumbai, November) – Highest in 9 years

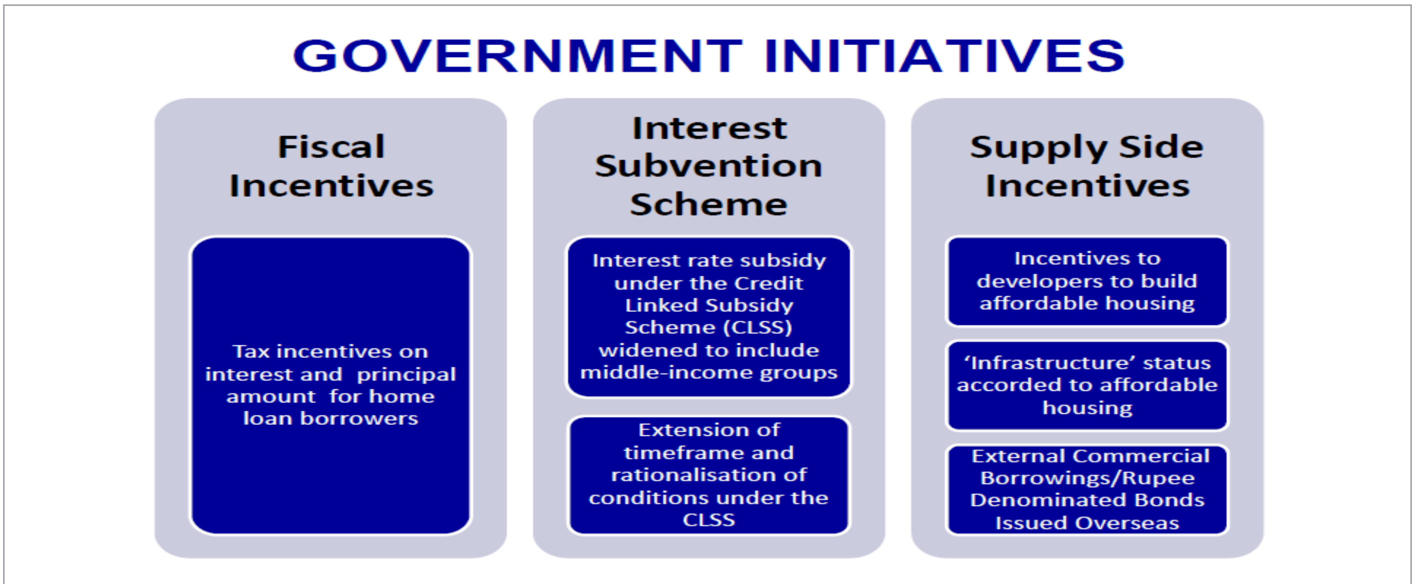


Source: Media reports, Sharekhan Research

The recent improvement was primarily driven by the gradual unlocking of the economy, pent-up demand, and improved affordability because of reduced home loan rates and attractive payment schemes/discounts. The uptick in absorption levels during Q2FY2021 has also been driven by the affordable and mid/upper-mid segments, indicating the higher resilience of these segments to demand headwinds currently prevailing in the residential realty market.

Moreover, supportive factors such as stamp duty cut (in Maharashtra) and government's measures allowing for increasing the differential between agreement value and circle rate from 10% to 20% have helped improve housing demand.

Supportive government measures for the housing mortgage sector

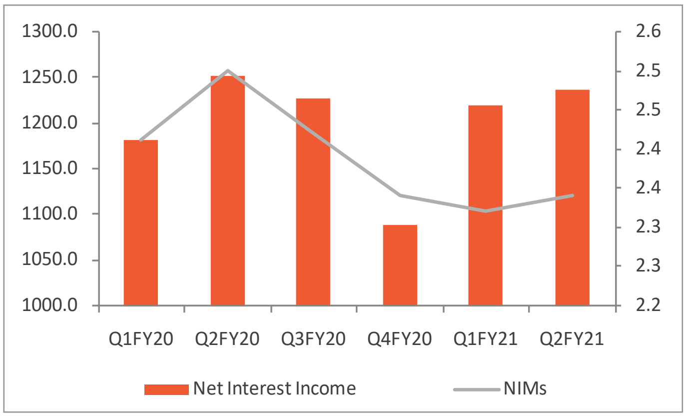


Source: Company, Sharekhan Research

Post the announcement of increasing the differential between agreement value and circle rate from 10% to 20%, the industry has reacted quite positively towards it, as the discounts being offered by developers were inching closer to 20% in many geographies. However, this benefit is only available till June 30, 2021, and it is only applicable for the primary sale of residential units of value up to Rs. 2 crore.

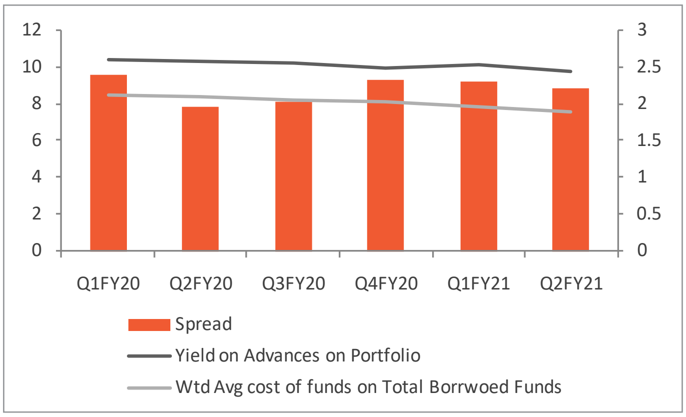
Financials in charts

NII, NIMs



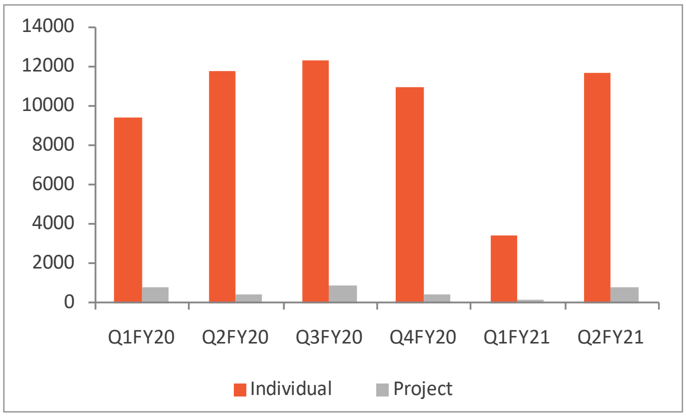
Source: Company, Sharekhan Research

Yeilds, Costs and Spreads



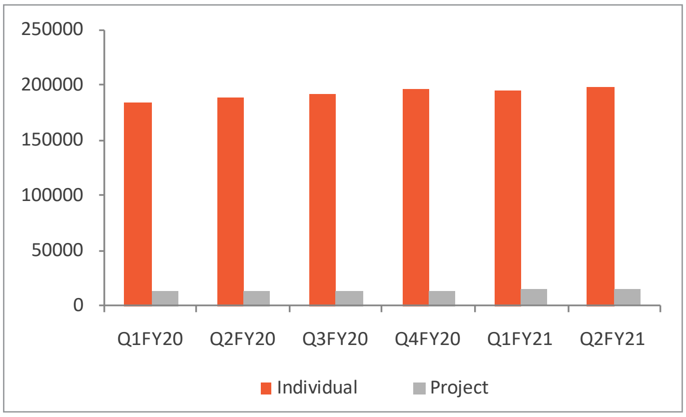
Source: Company, Sharekhan Research

Disbursemnts trend



Source: Company, Sharekhan Research

Loan Book mix

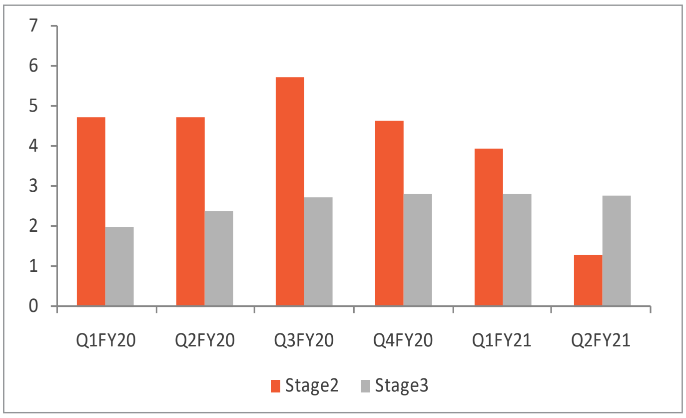


Source: Company, Sharekhan Research

Return Ratios

Source: Company, Sharekhan Research

Asset Quality



Source: Company, Sharekhan Research

Outlook and Valuation

Sector view - Outlook improves for NBFCs in general and HFCs in particular

Long-term structural indicators remain strong for housing and mortgages in India. Ruling interest rates are low and several states have given incentive for home buying, which is likely to prop up demand. With the recent fall in borrowing costs, which was steep for high-rated NBFCs, is another positive in its favour. Moreover, rising affordability and softening pricing (helped by tax incentives) are positive for demand offtake and LTV outlook for HFCs. India has a young population and government schemes such as CLSS etc., which will facilitate even the affordable housing segments, are also enablers along with low penetration levels of mortgages in India (at 10% of GDP, against 18% in China and 56% in the US). We believe economic recovery is also gaining momentum and stimulus/supportive measures by the government and the Reserve Bank of India (RBI) will further aid to the same. We believe the outlook has turned positive on the NBFC sector in general and HFCs in particular.

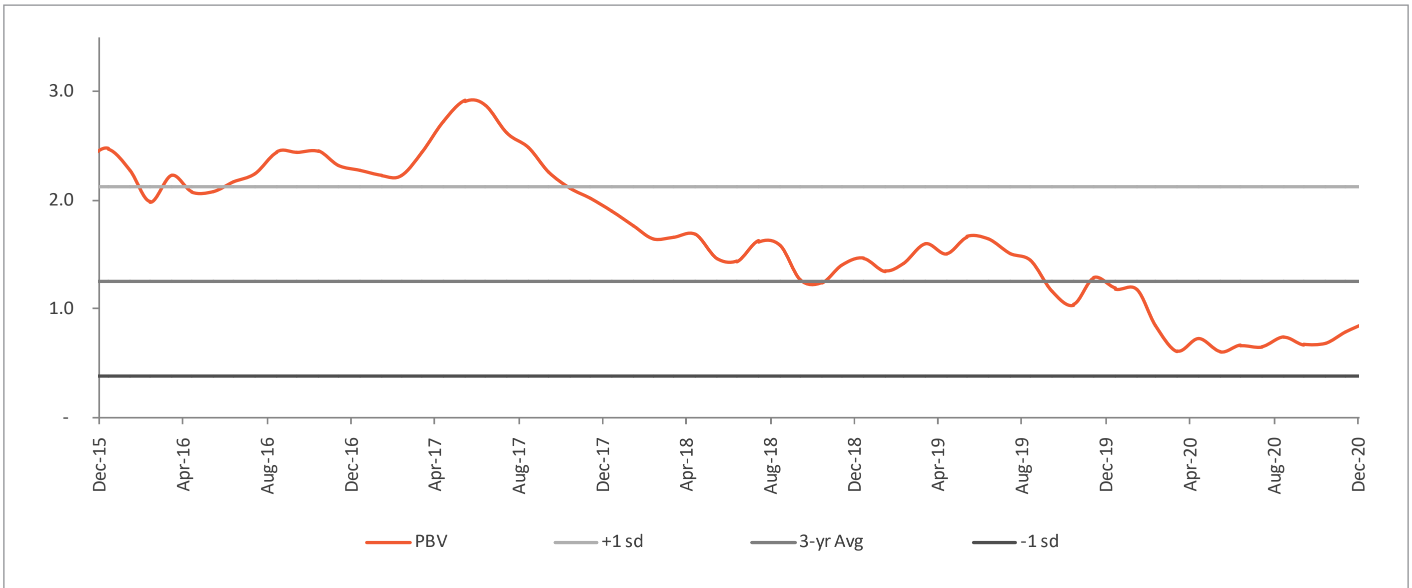
Company outlook - Strong fundamentals, with improving growth outlook, resilient margins

During the quarter, LICHF witnessed improved loan disbursement and stable NIM, indicating a recovering traction post the lockdown and slower economic activity due to Covid-19 pandemic. LICHF is well placed in terms of liquidity management and falling interest would certainly augur well for the company in the coming quarters. LICHF has comfortable access to liquidity and enjoys high credit ratings. Even though, we believe competitive intensity may increase in the home loan segment, we expect margin outlook to be stable (with a positive bias) due to its declining cost of funds and improving disbursement traction. We believe asset-quality outlook and well-managed costs of borrowings are positives in favour.

Valuation - We maintain a Buy rating on the stock with a revised PT of Rs. 440

Valuations at 1.05x/0.91x its FY2022E and FY2023E ABVPS are reasonable considering its high return ratios and stable asset quality. LICHF has comfortable access to liquidity and enjoys high credit ratings and is well placed to manage the expected competitive intensity in the home loan segment and is likely to be able to keep margins steady (with a positive bias). The pall of the pandemic is lifting and healthy traction is encouraging. The asset-quality outlook (aided by conservative LTV ratios) along with normalising business traction (improving faster than earlier envisaged) improves the overall outlook for the company. LICHF has strengths in its borrowing profile and has been able to bring down its cost of funds, helped by its strong parent profile. We believe conservative LTVs and inexpensive valuations make it a reasonably attractive investment. We have fine-tuned our estimates and believe the outlook for LICHF has improved. The stock is still down ~24% from its highs and we believe risk reward is favourable for long-term investors. We maintain our Buy rating on the stock with a revised PT of Rs. 440.

One-year forward P/BV (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs.)	P/BV (x)		P/E (x)		RoA (%)		RoE (%)	
		FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
LIC Housing Finance	371	1.1	0.9	6.0	5.3	1.7	1.7	17.2	17.0
Can Fin Homes	491	2.6	2.2	15.5	13.2	1.9	2.1	17.8	17.8
PNB Housing Finance	366	8.7	7.2	8.7	7.2	0.9	1.2	8.3	10.1

Source: Bloomberg, Sharekhan Research

About company

LICHF is one of the largest HFCs in India having one of the widest networks of offices across the country and representative offices in Dubai and Kuwait. In addition, the company distributes its products through branches of its subsidiary. LICHF is promoted by Life Insurance Corporation in which it currently holds 40.31% shares in HFC. LICHF enjoys high rating from CRISIL and CARE, indicating the highest safety about the ability to service interest and repay principal, which to some degree can be attributed to having a strong parent.

Investment theme

LICHF has seen steady loan book growth, but performance of the high-yield (but also high delinquency) developer loan book portion such as LAP/Developer is a key monitorable. Backed by a strong parent, the rating of LICHF has been strong; and it has been able to see off most of the liquidity pressure that had impacted most NBFCs/HFCs of late. However, high ratings are a key positive support to its margins and allows it to wean off high liquidity faster than peers. Even though we believe competitive intensity may increase in the home loan segment, we expect margin outlook to be stable (with a positive bias) due to its declining cost of funds and improving disbursement traction. We believe asset-quality outlook, pickup in economic activities, and well-managed costs of borrowings are positives in favour.

Key Risks

Increased delinquencies in the developer book may worsen asset quality and affect profitability.

Additional Data

Key management personnel

Mr. Siddhartha Mohanty	Managing Director and CEO
Mr. Sudipto Sil	CFO/Manager:Investor Relation
Mr. Nitin K. Jage	General Manager (Taxation) & Company Secretary
Ms. Purti Samant	Chief Risk Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	FIDELITY INV TRUST FIDELIT	9.35
2	ICICI Prudential Asset Management	3.37
3	FMR LLC	2.54
4	Bank Muscat SAOG	2.28
5	Norges Bank	2.23
6	NPS TRUST	2.21
7	GOVERNMENT PENSION FUND - GLOBAL	2.01
8	HDFC Life Insurance Co Ltd	1.87
9	Vanguard Group Inc/The	1.84
10	BlackRock Inc	1.47

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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