

LIC Housing Finance

Not Rated / Rs 212

Manish Agarwalla (*manish.agarwalla@mfglobal.in*) +91 22 6667 9962
Shubhangi Agrawal (*Research Associate*)

Tough times ahead

- HFCs (housing finance companies) will face challenges in the short term, given the housing stimulus package announced by PSU banks. Banks offered to provide home loans (between Rs 5-Rs 20lakh) at a rate of 9.25% for a maximum period of 20 years with a margin of 15%, applicable up to 30 June '09.
- This scheme is expected to distort the competitiveness of LIC HF as the cost of their funds itself is over 10% and they lend it at 12%. In order to provide some relief to the funding crisis at HFCs, the regulator has granted Rs 40bn amount of refinance through NHB (National Housing Board). LIC HF is expected to get Rs10bn, as refinance, through NHB, at a cost of 8.5%. Moreover, the declining interest rate will enable HFCs to reduce its cost of funds, thus compensating, to some extent, the decline in the spread.
- We believe that the housing stimulus package, if implemented to the fullest, will either affect the disbursement of HFCs or narrow down the spread in the short term.
- We expect the disbursement growth in Q4FY09 to decline due to an unfavourable environment, thus settling the full-year disbursement growth at 12% YoY and we expect FY10 disbursements to grow at 15%. This will bring down its spread from the current level of 1.75% to 1.54% by the end of Q1FY10. We expect the spread to remain at this level for FY10, provided the stimulus package on housing for banks is not extended beyond 30 June '09.
- We also believe that the change in product mix (increasing weightage towards builder's loans) would not translate to a fruitful result as the banks have become more competitive in this segment due to relaxation of certain norms like risk weightage (reduced from 150% to 100%), provisioning requirement (reduced from 2% to 0.4%) and restructuring of assets (asset classification to remain the same after restructuring of standard assets).
- The asset quality to remain stable with GNPA expected to be around 1.7% in FY09. The exposure towards builder's loans, which is currently 8%, does not put stress on the portfolio as the loan to value ratio in this segment is as low as 30%.
- The change in the business environment will moderate the earnings growth of the company to 13.6% in FY09 and 8.7% in FY10, translating into a decline in ROE to 20.4% from the level of 23% in FY08, assuming the leverage ratio to remain constant at 11x. At the CMP of Rs 212, the stock is valued at 0.9x FY09 ABV of Rs 232 and 0.8x FY10 ABV of Rs 268.

This note should be read for

- **Company update and background**

Bloomberg code: LICHF IN
 Reuters code: LICH.BO
 www.lichousing.com

BSE Sensex: 10076
 NSE Nifty: 3061

Company data

| | |
|-------------------------|-----------|
| O/S shares: | 85mn |
| Market cap (Rs): | 18bn |
| Market cap (USD): | 382mn |
| 52 - wk Hi/Lo (Rs): | 391 / 151 |
| Avg. daily vol. (3mth): | 1.1mn |
| Face Value (Rs): | 10 |

Share holding pattern, %

| | |
|------------------------------|------|
| Promoters: | 40.8 |
| FII / NRI: | 33.2 |
| FI / MF: | 7.9 |
| Non Promoter Corp. Holdings: | 5.6 |
| Public & Others: | 12.5 |

Price performance, %

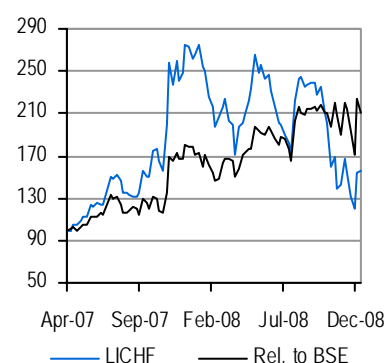
| | 1mth | 3mth | 1yr |
|------------|-------|-------|-------|
| Abs | -12.1 | -32.9 | -40.3 |
| Rel to BSE | -0.6 | -8.6 | 6.9 |

Valuation summary

| Y/E Mar, Rs mn | FY 06 | FY 07 | FY 08 | FY 09E | FY 10E |
|------------------|-------|-------|-------|--------|--------|
| Pre-prov ROE (%) | 25.0 | 25.4 | 32.4 | 31.2 | 29.1 |
| Pre-prov ROA (%) | 2.2 | 2.1 | 2.6 | 2.5 | 2.3 |
| Net Profit | 2,086 | 2,791 | 3,872 | 4,397 | 4,778 |
| % growth | 45.1 | 33.8 | 38.7 | 13.6 | 8.7 |
| EPS (Rs) | 24.5 | 32.8 | 45.6 | 51.7 | 56.2 |
| Adj BVPS (Rs) | 126.7 | 155.7 | 198.9 | 232.8 | 268.5 |
| ROE (%) | 16.6 | 19.3 | 22.9 | 22.0 | 20.4 |
| P/E (x) | 8.6 | 6.5 | 4.7 | 4.1 | 3.8 |
| Adj. P/BV (x) | 1.7 | 1.4 | 1.1 | 0.9 | 0.8 |

Source: Company, MF Global India Research Estimates

Price vs. Sensex



Source: Bloomberg, MF Global India Research

Background

LIC HF contributes 6.3% to the total housing finance business. It is the second largest player, after HDFC. LIC HF provides long-term finance to individuals for purchase, construction, repair and renovation of new and existing houses. The company also lends to corporate bodies and companies under different schemes for purchase or construction of office premises. The incremental ticket size stands at ~Rs 11lakh, whereas the average ticket size is more than Rs 6lakh, the prepayment rate is ~8% and the average duration of the loan is 7-8 years. The loan to value ratio stands at 60% with the tenure of the loan at 15 years. The asset quality has shown an improvement over a period with GNPA of 1.85% and NNPA of 0.87% as on Sep'08. LIC HF's funds are sourced from term loans from banks, bonds and debentures constituting 80% of borrowing and term loans from LIC, which constitute 15% of total borrowings and the remaining 5% in the form of refinance from NHB and others. On the asset front, 92% of outstanding loans is in the individual segment, yielding 11.5% and the balance is towards corporate and other loans (builder loans), yielding 15%-16%. Around 65% of liabilities are floating in nature whereas 96% of the assets are floating. The company resort to swap to manage its asset-liability mismatch.

FINANCIALS

Income Statement

| Profit and Loss Account | FY 06 | FY 07 | FY 08 | FY09E | FY10E |
|----------------------------|--------|--------|--------|--------|--------|
| Interest on Loans | 11,897 | 14,990 | 20,368 | 26,478 | 29,656 |
| Others | 48 | 64 | 198 | 100 | 100 |
| Total Interest Earned | 11,945 | 15,054 | 20,566 | 26,578 | 29,756 |
| Total Interest Expended | 8,594 | 11,079 | 14,943 | 19,829 | 22,208 |
| Net Interest Income | 3,350 | 3,975 | 5,624 | 6,749 | 7,547 |
| Total non interest income | 768 | 745 | 1,176 | 915 | 837 |
| Total Income | 4,118 | 4,720 | 6,800 | 7,664 | 8,385 |
| Personnel Expenses | 251 | 268 | 346 | 374 | 404 |
| Other Expenses | 688 | 777 | 992 | 1,068 | 1,173 |
| Total Op expenses | 938 | 1,044 | 1,338 | 1,441 | 1,577 |
| Net Inc (Loss) before prov | 3,180 | 3,676 | 5,461 | 6,223 | 6,808 |
| Provision for NPAs | 563 | 157 | 243 | 200 | 263 |
| Net Inc (Loss) before tax | 2,639 | 3,539 | 5,324 | 6,023 | 6,545 |
| Provision for Income Tax | 532 | 746 | 1,451 | 1,626 | 1,767 |
| Net Profit | 2,086 | 2,791 | 3,872 | 4,397 | 4,778 |

Source: Company, MF Global India Research Estimates

Balance Sheet

| Rs mn | FY 06 | FY 07 | FY 08 | FY09E | FY10E |
|--|---------|---------|---------|---------|---------|
| Assets | | | | | |
| Cash & Cash Equivalents | 4,800 | 7,790 | 3,617 | 4,277 | 3,891 |
| Advances | 148,672 | 175,634 | 219,364 | 263,048 | 307,230 |
| Investments | 3,514 | 2,414 | 7,993 | 8,688 | 8,765 |
| Fixed Assets (Net) | 245 | 236 | 300 | 306 | 312 |
| Current Assets, Loans & Advances | 1,283 | 1,284 | 1,597 | 1,634 | 1,097 |
| Deferred Tax Assets | 835 | 834 | 929 | 860 | 870 |
| Total Assets | 159,349 | 188,193 | 233,800 | 278,813 | 322,165 |
| Liabilities | | | | | |
| Share capital | 850 | 850 | 850 | 850 | 850 |
| Reserves and Surplus | 12,605 | 14,588 | 17,467 | 20,769 | 24,354 |
| Debt | 5,000 | 5,000 | 5,000 | 7,000 | 8,000 |
| Total borrowing | 132,804 | 158,326 | 198,444 | 236,149 | 273,932 |
| Other non-interest bearing liabilities | 5,922 | 7,444 | 10,436 | 10,645 | 10,858 |
| Provisions for contingencies | 1,795 | 1,632 | 1,355 | 3,040 | 3,800 |
| Provision for diminution in value of investments | 374 | 353 | 248 | 360 | 370 |
| Total Liabilities | 159,350 | 188,193 | 233,800 | 278,813 | 322,165 |

Source: Company, MF Global India Research Estimates

Profitability, Productivity, Liquidity and Valuation Ratios

| | FY06 | FY07 | FY08 | FY09E | FY10E |
|--------------------------------------|------------|------------|------------|------------|------------|
| Earnings and Valuation Ratios | | | | | |
| Pre-provision Operating RoAE (%) | 25.0 | 25.4 | 32.4 | 31.2 | 29.1 |
| RoAE (%) | 16.6 | 19.3 | 22.9 | 22.0 | 20.4 |
| Pre-provision Operating ROA (%) | 2.2 | 2.1 | 2.6 | 2.4 | 2.3 |
| RoAA (%) | 1.5 | 1.6 | 1.9 | 1.7 | 1.6 |
| EPS (Rs.) | 24.5 | 32.8 | 45.6 | 51.7 | 56.2 |
| Dividend per share (Rs.) | 6.0 | 3.0 | 10.0 | 11.0 | 12.0 |
| Book Value (Rs.) | 158.3 | 181.6 | 215.5 | 254.4 | 296.5 |
| Adj BV (Rs.) | 126.7 | 155.7 | 198.9 | 232.8 | 268.5 |
| Revenue Analysis | | | | | |
| Interest income on IBA (%) | 8.4 | 8.8 | 9.9 | 10.5 | 10.0 |
| Interest cost on IBL (%) | 6.9 | 7.4 | 8.1 | 8.9 | 8.5 |
| NIM on IBA / AWF (%) | 2.4 | 2.3 | 2.7 | 2.7 | 2.5 |
| Spread (%) | 1.5 | 1.4 | 1.7 | 1.6 | 1.5 |
| Core fee Inc / AWF (%) | 0.3 | 0.3 | 0.3 | 0.2 | 0.2 |
| Portfolio gains / Total Inc (%) | 4.7 | 5.2 | 9.5 | 2.7 | 2.4 |
| Op.Exp / TI (%) | 23.9 | 23.3 | 21.6 | 19.3 | 19.3 |
| Op.Exp / AWF (%) | 0.7 | 0.6 | 0.6 | 0.6 | 0.5 |
| Employee exps / Op exps (%) | 26.7 | 25.7 | 25.8 | 25.9 | 25.6 |
| Tax / Pre-tax earnings (%) | 20.2 | 21.1 | 27.3 | 27.0 | 27.0 |
| Asset Quality | | | | | |
| GNPAs / Gr Adv (%) | 3.4 | 2.6 | 1.7 | 1.7 | 1.7 |
| NNPAs / Net Adv (%) | 1.8 | 1.3 | 0.6 | 0.7 | 0.8 |
| Growth Ratio | | | | | |
| Loans (%) | 19.7 | 18.1 | 24.9 | 19.9 | 16.8 |
| Investments (%) | 203.9 | (31.3) | 231.1 | 8.7 | 0.9 |
| Deposits (%) | 20.2 | 19.2 | 25.3 | 19.0 | 16.0 |
| Net worth (%) | 12.6 | 14.7 | 18.6 | 18.0 | 16.6 |
| Net Int Income (%) | 11.4 | 18.7 | 41.5 | 20.0 | 11.8 |
| Non-fund based income (%) | 15.3 | (12.4) | 14.2 | 22.6 | (10.9) |
| Non-Int Exp (%) | 8.8 | 11.3 | 28.1 | 7.7 | 9.4 |
| Profit Before Tax (%) | 29.1 | 34.1 | 50.4 | 13.1 | 8.7 |
| Net profit (%) | 45.1 | 33.8 | 38.7 | 13.6 | 8.7 |
| Capital Adequacy Ratio | | | | | |
| Tier I (%) | 14.1 | 12.9 | 12.7 | 13.1 | 13.2 |
| Internal Capital Generation rate (%) | 13.2 | 18.9 | 19.6 | 18.9 | 17.4 |
| NNPAs to Equity (%) | 19.9 | 14.3 | 7.7 | 8.5 | 9.4 |

Source: Company, MF Global India Research Estimates

Vineet Bhatnagar
James Rowsell
Sajid Khalid
Jignesh Shah

Managing Director
Global Head – Institutional Equities & Derivatives
Head – Institutional Cash Equities
Head – Equity Derivatives

91-22-6667 9972
91-22-6667 9735

vineet.bhatnagar@mfglobal.in
jrowsell@mfglobal.com
sajid.khalid@mfglobal.in
jignesh.shah@mfglobal.in

Equity Research

| | | | |
|-------------------|-------------------------------------|-----------------|-------------------------------|
| Amrish Mishra | Automobiles & Auto Component | 91-22-6667 9758 | amrish.mishra@mfglobal.in |
| Amit Mahawar | Engineering & Capital Goods / Power | 91-22-6667 9759 | amit.mahawar@mfglobal.in |
| Anjali Verma | Economist | 91-22-6667 9969 | anjali.verma@mfglobal.in |
| Avishek Agarwal | Logistics & Shipping | 91-22-6667 9986 | avishek.agarwal@mfglobal.in |
| Deepali Gautam | Power | 91-22-6667 9974 | deepali.gautam@mfglobal.in |
| Dipesh Sohani | Real Estate | 91-22-6667 9965 | dipesh.sohani@mfglobal.in |
| Gauri Anand | Oil & Gas / Fertiliser | 91-22-6667 9943 | gauri.anand@mfglobal.in |
| Kapil Bagaria | Midcap | 91-22-6667 9987 | kapil.bagaria@mfglobal.in |
| Kunal Motishaw | Metals | 91-22-6667 9996 | kunal.motishaw@mfglobal.in |
| Manish Agarwalla | Banking | 91-22-6667 9962 | manish.agarwalla@mfglobal.in |
| Naveen Kulkarni | Telecom | 91-22-6667 9947 | naveen.kulkarni@mfglobal.in |
| Nimesh Mistry | IT Services | 91-22-6667 9768 | nimesh.mistry@mfglobal.in |
| Ritwik Rai | Media | 91-22-6667 9766 | ritwik.rai@mfglobal.in |
| Vaibhav Agarwal | Cement | 91-22-6667 9967 | vaibhav.agarwal@mfglobal.in |
| Aravind Manickam | Research Associate | 91-22-6667 9992 | aravind.manickam@mfglobal.in |
| Chaturya Tipnis | Research Associate | 91-22-6667 9764 | chaturya.tipnis@mfglobal.in |
| Deepali Gautam | Research Associate | 91-22-6667 9974 | deepali.gautam@mfglobal.in |
| Shubhangi Agrawal | Research Associate | 91-22-6667 9964 | shubhangi.agrawal@mfglobal.in |
| Shikha Khurana | Quant Analyst | 91-22-6667 9934 | shikha.khurana@mfglobal.in |
| Ganesh Deorukhkar | Production | 91-22-6667 9756 | ganesh.deorukhkar@mfglobal.in |
| Roshni Kallor | Editor | 91-22-6667 9762 | roshni.kallor@mfglobal.in |

Institutional Cash Equity Sales

| | | | |
|-------------------|--------------------|-----------------|-------------------------------|
| Kartik Broker | Equity Sales | 91-22-6667 9934 | kartik.broker@mfglobal.in |
| Kinshuk Tiwari | Equity Sales | 91-22-6667 9944 | kinshuk.tiwari@mfglobal.in |
| Milauni Vibhakar | Equity Sales | 91-22-6667 9991 | milauni.vibhakar@mfglobal.in |
| Priyanka Birmecha | Equity Sales | 91-22-6667 9944 | priyanka.birmecha@mfglobal.in |
| Nasir Mohamed | Equity Sales - UAE | 009714 3325052 | nasir.mohamed@mfglobal.in |

Institutional Cash Equity Sales Trading

| | | | |
|--------------|--------------|-----------------|--------------------------|
| Chetan Savla | Sales Trader | 91-22-6667 9749 | chetan.savla@mfglobal.in |
| Rajesh Ashar | Sales Trader | 91-22-6667 9746 | rajesh.ashar@mfglobal.in |
| Sunil Kamath | Sales Trader | 91-22-6667 9747 | sunil.kamath@mfglobal.in |

Institutional Cash Equity Dealing

| | | | |
|----------------|--------|-----------------|----------------------------|
| Chetan Babaria | Dealer | 91-22-6667 9748 | chetan.babaria@mfglobal.in |
| Mayur Shah | Dealer | 91-22-6677 9748 | mayur.shah@mfglobal.in |
| Sagar Shah | Dealer | 91-22-6677 9748 | sagar.shah@mfglobal.in |

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2nd Floor, C-Block, Modern Centre, Mahalaxmi, Mumbai-400 011