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Equity | India

Flashnote

Financials

NHB waives pre-payment penalty

NHB, the regulator for HFCs has advised companies to stop charging pre-payment penalty on all floating rate loans and also to charge a uniform floating rate to old and new customers. In general, this will impact proftability and create challenges on asset-liability maturity management.

NHB - No pre-payment penalty, uniform floating rate for old and new customers

- NHB (National Housing Bank), the regulator for Housing Finance Companies (HFCs) has issued regulations to 1) not charge any pre-payment penalty in case of floating rate loans (pre-closed through any source including re-finance), 2) not charge any pre-payment penalty in case of fixed rate loans if the loan is pre-closed by the borrower out of their own sources (i.e. penalty can be levied if the loan is being re-financed)
- Further, HFCs have been advised to charge uniform rate of interest to old and new borrowers, with the same credit / risk profile irrespective of the time of entry of the borrowers in the market.

Impact analysis - Spreads and asset-liability maturity management

- We believe the above changes will have the following impact 1) marginally impact earnings due to absence of pre-payment penalty, 2) create challenges on asset-liability maturity management, 3) it seems that this will be applicable only on incremental business as it will be difficult to re-price existing customers as they are on a contractual basis.
- We expect that similar regulations (as above) will be issued by RBI for banks, in the near future.
- HDFC Limited (Buy) does not charge pre-payment penalty (about 2%) in case of pre-payment by the borrower from own sources (ie. if the loan is not re-financed). At this stage, we are unable to assess the financial impact of above regulations. However, we believe, HFCs will price incremental loans at a higher rate to offset the risk of pre-payment.

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Recommendation structure

Absolute performance, short term (trading) recommendation: A Trading Buy recommendation implies upside of 5% or more and a Trading Sell indicates downside of 5% or more. The trading recommendation time horizon is 0-60 days. For Australian coverage, a Trading Buy recommendation implies upside of 5% or more from the suggested entry price range, and a Trading Sell recommendation implies downside of 5% or more from the suggested entry price range. The trading recommendation time horizon is 0-60 days.Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and, except as follows, only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. For UK-based Investment Funds research, the recommendation structure is not based on upside/downside to the target price. Rather it is the subjective view of the analyst based on an assessment of the resources and track record of the fund management company. For research on Australian listed property trusts (LPT) or real estate investment trusts (REIT), the recommendation is based upon total return, ie, the estimated total return of capital gain, dividends and distributions received for any particular stock over the investment horizon.
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Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.
Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Distribution of recommendations

The tables below show the distribution of recommendations (both long term and trading). The first column displays the distribution of recommendations globally and the second column shows the distribution for the region. Numbers in brackets show the percentage for each category where there is an investment banking relationship. These numbers include recommendations produced by third parties with which RBS has joint ventures or strategic alliances.

Long term recommendations (as at 20 Oct 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Buy	867 (11)	567 (3)
Hold	417 (7)	225 (4)
Sell	90 (6)	49 (0)
Total (IB%)	1374 (9)	841 (3)

Source: RBS

Trading recommendations (as at 20 Oct 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Trading Buy	1 (100)	1 (100)
Trading Sell	1 (0)	1 (0)
Total (IB%)	2 (50)	2 (50)

Source: RBS

Valuation and risks to target price

For a discussion of the valuation methodologies used to derive our price targets and the risks that could impede their achievement, please refer to our latest published research on those stocks at http://research.rbsm.com

Regulatory disclosures

None

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