



LIC Housing Finance

 Relative to sector: **Outperformer**
Praveen Agarwal

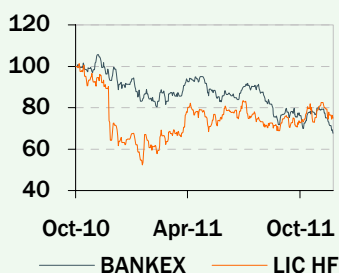
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Relative Performance


Source: Bloomberg, ENAM Research

Stock data

No. of shares	: 475 mn
Market cap	: Rs 103.9 bn
52 week high/low	: Rs 245/Rs 130
Avg. daily vol. (6mth)	: 4.3 mn shares
Bloomberg code	: LICHF IB
Reuters code	: LICH.BO

Shareholding (%) Sep-11 QoQ chg

Promoters	: 36.5	0.0
FIs	: 37.8	(2.1)
MFs / UTI	: 5.5	1.3
Banks / FIs	: 3.4	(0.1)
Others	: 16.8	0.9

Financial summary

Y/E Mar	PAT (Rs mn)	EPS (Rs)	EPS chg (%)	P/E (x)	P/E (x)*	Adj. BV (Rs.)	P/Adj. BV (x)	P/Adj. BV (x)*	RoE (%)	RoA (%)	Net NPA (%)
2010	6,622	13.9	11.5	15.7	15.6	71	3.1	3.1	23.6	1.9	0.1
2011	9,745	20.5	47.2	10.7	10.6	88	2.5	2.5	25.8	2.1	0.0
2012E	9,781	20.6	0.4	10.6	10.5	105	2.1	2.1	21.5	1.6	(0.1)
2013E	13,292	26.7	29.7	8.2	8.1	137	1.6	1.6	22.2	1.8	(0.1)

Source: Company, ENAM Research. *P/Adj. BV and P/E calculated after deducting value of investment from price and cost of investment from BV. # Assumed equity dilution of Rs10bn in FY13E

CONSISTENT PERFORMANCE DESPITE ECONOMIC HEADWINDS

We recently met with the management of LIC Housing Finance (LICHF), primarily to understand their views on: (a) factors which will contribute to margin improvement, (b) write-back of provisions, and (c) visibility of advances growth.

Post our interaction, we continue to believe that LICHF remains a secular play on India's retail growth story and is likely to benefit from: (a) improving margins backed by improvement in yields, (b) higher proportion of Developer loans, (c) easing pressure on funding costs, (d) continuous improvement in asset quality and (e) strong momentum in demand for retail mortgages.

Management meet highlights:

- NIMs are expected to improve to 2.7% led by an increase in proportion of developer loans and rise in lending rates.
- LICHF would write-back ~Rs 1 bn of NPA provisions in H2FY12, post approval of the same by Board of Directors.
- Retail advances are expected to grow by ~25% for FY12E in spite of an overall slowdown in the economy.

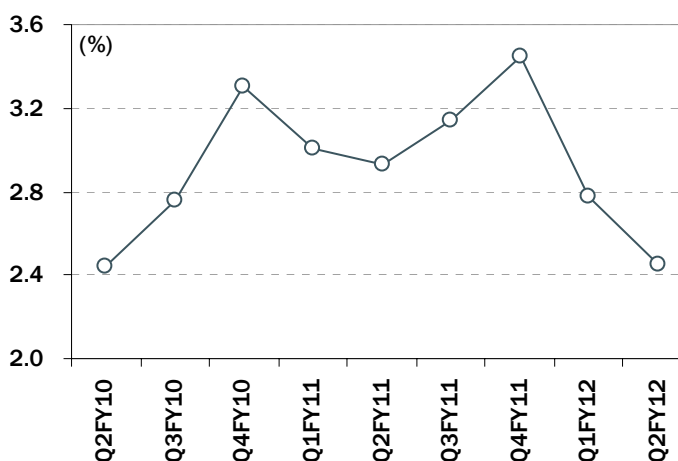
Valuations attractive; Recommend BUY

LICHF will be one of the biggest beneficiaries of the structural demand for mortgages backed by strong domain expertise, relatively lower cost of funds and lower credit costs. The above factors, coupled with fund raising plans (book accretive dilution), make LICHF an attractive **BUY** at current levels. At **CMP of Rs 219**, LICHF is trading at 1.6x FY13E ABV of Rs 137. We recommend **BUY rating** on the stock with a TP of Rs 250 – upside of 14% from CMP.

Following are the key takeaways from our interaction with the mgmt:

- **Net interest margins to improve:**
 - ▶ Management has guided for an NIM of ~2.7% for FY12E (2.45% in Q2FY12) driven by increased disbursements to Developers (plans to disburse Rs 10 bn per quarter over H2FY12 and end the year with ~9-10% of total advances) which enjoy better yields (~15%).
 - ▶ Further, the company has raised PLR by 40 bps to 14.4% on Retail loans (58% of retail advances are floating in nature) effective 1st October and the entire impact of this would be seen on the yield on advances in the current quarter.
 - ▶ Rs 30 bn (Rs 60 bn in FY13E) of advances under the “Fix-o-Floaty” scheme would become floating in nature in Q1FY13E which will further aid in improving NIMs.

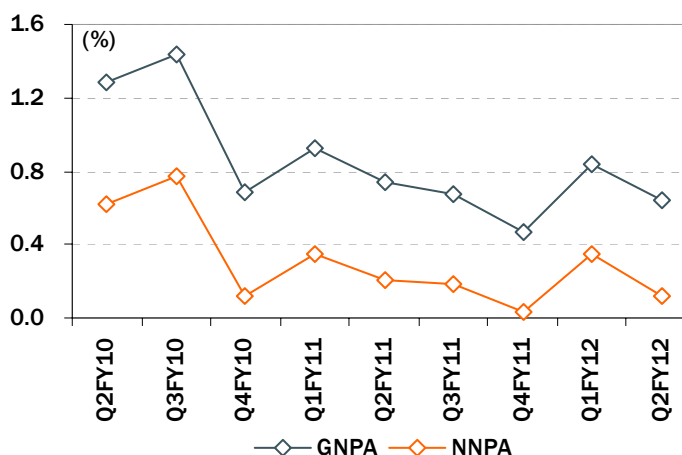
Net Interest margins – expected to increase going forward



Source: Company, ENAM Research

- **Asset quality continues to improve:**
 - ▶ GNPA % declined by 20 bps QoQ to 0.64% in Q2FY12.
 - ▶ Management has guided that the year-end Absolute GNPA's would decline to ~Rs 3 bn (from Rs 3.59 bn in Q2FY12) as recoveries are expected to improve in H2FY12.
 - ▶ NNPA % declined 23 bps to 0.12% in Q2FY12 due to the aggressive provisions done by LICHF during the quarter.

Asset quality – showing continuous improvement



Source: Company, ENAM Research

□ Reversal of provisions:

- ▶ LICHF has made a provision of Rs 2.05 bn in Q2FY12 – Rs 1.6 bn as standard asset provision on portfolio of Rs 400 bn @ 0.4% (adjusted for Fix-o-Floaty products) + Rs 450 mn relating to increased provisioning for NPAs (due to increased provisioning requirement in bucket above 52 months from 65% to 100%).
- ▶ LICHF was already carrying a provision of Rs 4.84 bn as on March 2011.
- ▶ The cumulative provision now stands at Rs 7.24 bn, whereas the regulatory requirement is of ~Rs 6.25 bn. This essentially means that an excess provision of Rs 1 bn will be reversed post the approval by Board of Directors in H2FY12. This reversal will be routed through P&L account.
- ▶ LICHF has not made any provisions on 'Advantage 5' products. According to the management, NHB has made it clear that 'New Advantage 5' & 'Super 6' products are not classified as Teaser products and hence no provision requirements are needed. However, there is no clarity on earlier products and hence LICHF continues to be in a discussion with the regulator on the same.

□ Visibility of advances growth:

- ▶ Management sounded confident of achieving ~25% advances growth for FY12E.
- ▶ Demand continues to be strong on a Pan-India basis for retail mortgages. Of the total retail loans, ~85% are to salaried class (of which ~50% are Government employees).
- ▶ LICHF would start focusing on Developer loans and plans to disburse ~Rs 10 bn per quarter in H2FY12. The mgmt plans to have ~10% of advances to Developers by end of FY12E (7% in Q2FY12).

Borrower Segment

Nature of advances	Average Yields (%)	Incremental tenure (Years)	Ticket size (Rs mn)
Retail	~11.5-12	~ 15	~ 1.6
Developer	~15-16	~ 3	~500

Source: Company; ENAM Research

□ **Funding Book:**

- ▶ LICHF has been replacing bank loans with NCDs due to the recent base rate hikes taken by banks which have made bank loans expensive (NCDs are cheaper than Bank loans by almost ~75 bps currently).
- ▶ ~50% of total Liabilities for LICHF are floating in nature which will be re-priced as and when interest rates start to trend downward.

Borrowings profile

Nature of Liabilities	% of Total borrowings	Duration
Bank Loans	30	7-8 years (floating with prepayment option without penalty)
NCDs	57	Fixed
NHB	4	Fixed as well as floating
others (Including Retail)	9	NA

Source: Company; ENAM Research

□ **Housing loan portfolio of LIC employees:**

- ▶ LICHF had entered into an agreement with LIC under which the former was required to takeover housing loan portfolio of LIC employees worth Rs 12.4 bn.
- ▶ The agreement is structured in such a way that LICHF is required to collect the EMIs (Principal + Interest) from employees of LIC and is required to pay only the Principal back to LIC.
- ▶ This essentially implies that LICHF get to book interest income on the portfolio whereas there are no interest expenses to be paid on the same. Outstanding portfolio in Q2FY12 stood at ~Rs 8 bn which LICHF is required to pay-back over the next few qtrs (no fixed time-line).

□ **NHB's circular: Same interest rates to be charged from both old & new borrowers:**

- ▶ The circular issued is advisory in nature and HFCs would wait for Banks to implement the same.
- ▶ However, the difference between old & new customers for LICHF is not very significant and as a result, the management does not expect any large impact if the circular is implemented.

- **Other key highlights:**
 - ▶ LICHF has not securitized any loans during H1FY12 as the securitization route has become unattractive post the implementation of base rates by banks.
 - ▶ 4% of total borrowings are through swap transactions. However, LICHF has not used swap transactions in H1FY12 and believes these transactions are not viable in a high interest rate scenario.
 - ▶ Competitive intensity has reduced in mortgage segments with Banks becoming less aggressive and teaser rate products moving out of the markets.
 - ▶ Origination of all loans is done in-house (through the financial services subsidiary) which results in lower asset quality risks & better evaluation of applications.
 - ▶ The entire interest expenses on zero coupon bonds have been routed through the P&L account on a regular basis and completely provided for till date.
 - ▶ LICHF plans to raise equity capital in near term and also has cushion of Rs 10 bn in Tier II to fund its future growth plans. (Current CAR stands at 14.56% with Tier I of 8.73%). We have assumed Rs 10 bn of equity dilution in FY13E.
 - ▶ The company is eligible for a banking license as they are not considered as a Government owned entity and are awaiting final guidelines on the same.

- **Management guidance:**
 - ▶ Credit growth target: **24-25%**
 - ▶ NIMs: **~2.7%**
 - ▶ Absolute GNPA: **Rs 3 bn**
 - ▶ Targeting incremental spread of 150 bps (current incremental spread at ~100 bps)

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2. Firm ownership of the stock	No
3. Directors ownership of the stock	No
4. Investment Banking mandate	No
5. Broking relationship	No

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