

LIC Housing Finance

BSE SENSEX 25,765
S&P CNX 7,929

CMP: INR501 TP: INR716(+43%) Buy



Stock Info

Bloomberg	LICHF IN
Equity Shares (m)	505.0
52-Week Range (INR)	624 / 389
1, 6, 12 Rel. Per (%)	-8/13/8
M.Cap. (INR b)	253.0
M.Cap. (USD b)	3.8
12M Avg Val (INR M)	1121
Free float (%)	59.7

Financials Snapshot (INR b)

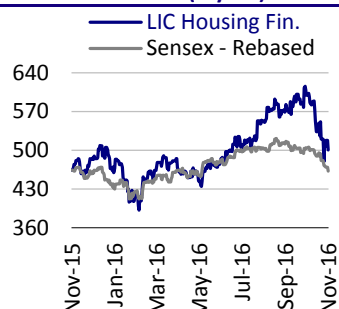
Y/E March	2016	2017E	2018E
NII	29.4	36.4	42.6
PPP	27.1	33.2	38.7
Adj. PAT	16.6	19.9	24.3
Adj. EPS(INR)	32.9	39.4	48.1
EPS Gr. (%)	23.3	19.7	22.3
BV/Sh (INR)	181.1	212.8	251.4
RoAA (%)	1.5	1.5	1.5
RoE (%)	19.6	20.0	20.7
Payout (%)	19.4	20.3	20.3
Valuations			
P/E (x)	15.2	12.7	10.4
P/BV (x)	2.8	2.3	2.0
Div. Yield (%)	1.1	1.4	1.7

Shareholding pattern (%)

As On	Sep-16	Jun-16	Sep-15
Promoter	40.3	40.3	40.3
DII	37.6	6.1	7.3
FII	0.0	27.5	37.4
Others	22.1	26.0	15.1

FII Includes depository receipts

Stock Performance (1-year)



Significant benefits from demonetization

Medium-term pick-up likely, no issues on asset quality

- Following the government's demonetization drive, property prices are expected to correct in the medium term. Thus, volumes may pick up impressively and thus drive strong loan growth.
- LICHF's customers are predominantly salaried professionals (~85%) and thus not affected by demonetization. Also, as ~50% of borrowers are government employees, the company expects significant growth as a result of 7th Pay Commission disbursement.
- Its LAP book, which grew rapidly over the past six quarters, has features that are very different from competitors. Average ticket size is only INR1.2m with average LTV of 25%. Hence, it is well insulated from any adverse impact of property price correction.
- G-sec yields have fallen below 6.5%. With greater liquidity (CASA deposits) in the system, we expect yields to fall further. LICHF will be the biggest beneficiary of falling yields as ~85% of its borrowings are from market.

Boost to growth over medium term

Demonetization should benefit LICHF in the following ways. a) Property prices should correct and thus houses will be more affordable for the salaried class. b) Unorganized financing sector will get wiped out gradually. Some pressure may however be felt over next six months as pace of home purchase comes down. While builders are busy with their back-office operations, buyers are in a 'wait-and-watch' mode, expecting property prices to correct over next 3-6 months. In addition, as around 50% of borrowers are government employees, the company expects significant growth as a result of the 7th Pay Commission disbursement.

No concerns around LAP portfolio

In our view, investors are primarily concerned about LICHF's LAP book, which has grown rapidly over past 5-6 quarters and is mostly unseasoned. Investors are worried that as a result of demonetization, asset quality in LAP would be severely stressed. While we acknowledge some transitory impact, there should not be any net credit losses due to the company's conservative underwriting philosophy (average ticket size: INR1.2m; average LTV: 25%), in our view.

LICHF benefits from falling G-sec yields

LICHF borrows ~85% from capital markets. It stands to benefit the most from falling G-sec yields. Over past three quarters, 10-year G-sec yield has declined more than 130bp from 7.8% to 6.5%. LICHF has more than INR150b worth of NCDs (with interest rate of 9.1-9.3%) maturing in next four quarters. If G-sec yields sustain at these levels going forward, we believe LICHF will be able to raise bonds at 7.2-7.4% given its AAA rating. We expect significant refinancing savings over next few quarters.

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Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

2%+ spreads to sustain despite stable share of LAP

Over past six quarters, LICHF has grown its LAP book rapidly. The share of LAP increased from 4.6% in 4QFY15 to 9.7% in 2QFY17. On incremental loans basis, the share of LAP rose from 17% in 1QFY16 to 37% in 1QFY17, but moderated to 24% in 2QFY17. Incremental spread increased from 1.74% to 2.18% over this period. This has helped shore up NIM to 2.6-2.7%. However, management indicated that it would not increase the share of LAP any further. While this would put pressure on incremental yields, LICHF would benefit from lower incremental cost of borrowings due to falling G-sec yields (**10-year G-sec yields below 6.5%**). We believe LICHF would maintain incremental spread above 2%. **In our view, consistently achieving 2% incremental spread over next few quarters would be a trigger for the stock to re-rate in line with peers.**

Spreads of AAA yields over G-sec yields narrow significantly

Another big impact of the RBI's OMOs has been that AAA bond spreads over GSec yields have narrowed significantly. While average spread has been ~80bp over the past year, it increased to 1.5% in March 2016 due to liquidity deficit. However, since then, spreads have come off significantly (mostly in August–September) to around 35bp now (refer Exhibit 5). Given current liquidity situation, we expect spreads to sustain at these levels.

Loan pricing competitive

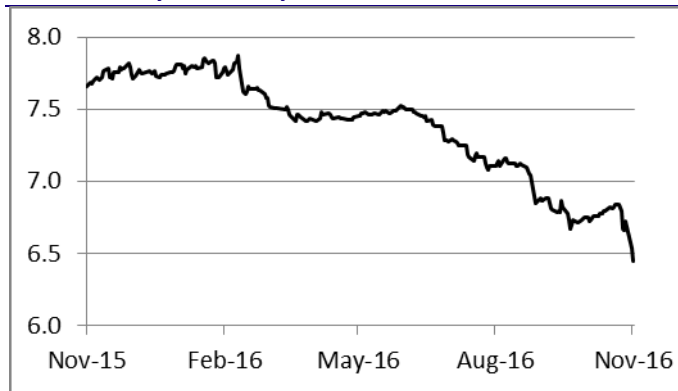
LICHF is originating pure floating rate loans at ~9.4% and other home loans at ~10%. Banks are also originating loans at 9.2-9.5%. We believe banks would be averse to reducing home loan rates further as they would have to reduce MCLR, as a result of which the whole loan book would get re-priced. Hence, we believe LICHF would not need to reduce rates substantially to remain competitive. We only see re-pricing risk of old fixed-to-floating rate loans upon conversion.

Re-rating on the cards; Buy

LICHF stands to benefit significantly from growing demand for mortgages and falling interest rates. Over past few quarters, change in loan mix has led to 2%+ incremental spread. **We expect 2%+ incremental spread to continue, and believe that the stock price does not factor in sustained spread improvement due to falling G-sec yields and narrowing AAA spreads.** We marginally cut EPS estimates by 2-3% to factor in temporary impact of demonetization. Yet, we expect 21% PAT CAGR over FY16-19. RoE is set to cross 20% in FY18, which would drive further re-rating. The stock trades at 2.0x FY18E BV, a discount to peers. We use RI model to value the stock, with Rf: 7.25%, CoE: 13.3% and terminal growth rate: 5%. **Buy** with a target price of INR716 (2.6x Sep 2018E BV).

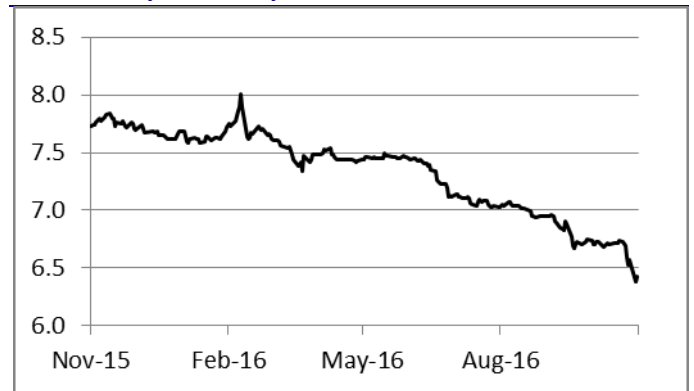
Story in charts

Exhibit 1: 10-year G-Sec yield at 6.5%



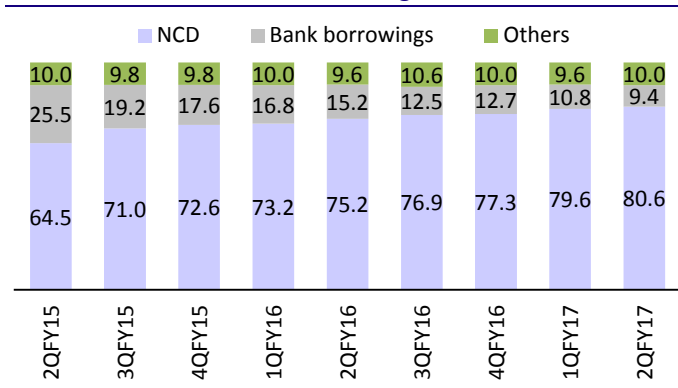
Source: MOSL, Company

Exhibit 2: 5-year G-Sec yield at 6.4%



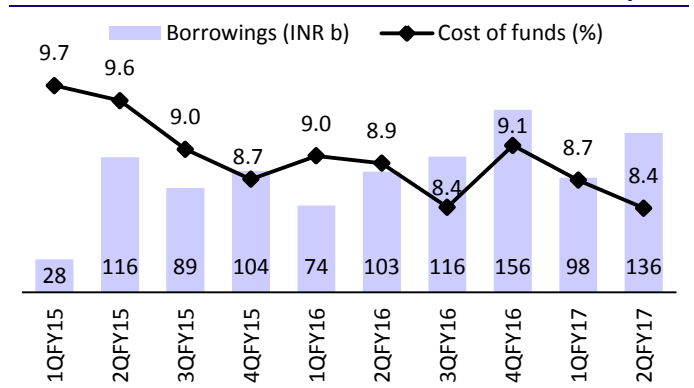
Source: MOSL, Company

Exhibit 3: Gradual shift in borrowing mix



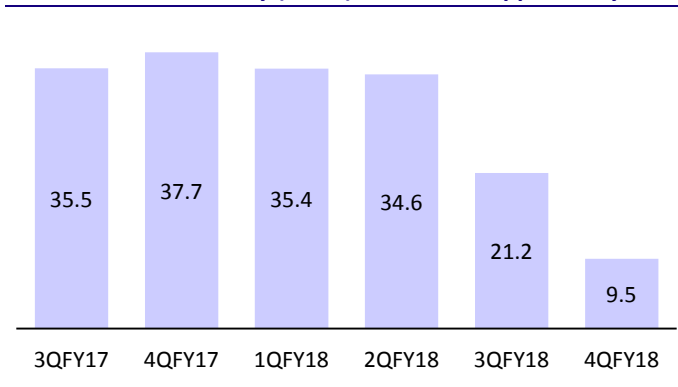
Source: MOSL, Company

Exhibit 4: Incremental cost of funds has fallen drastically



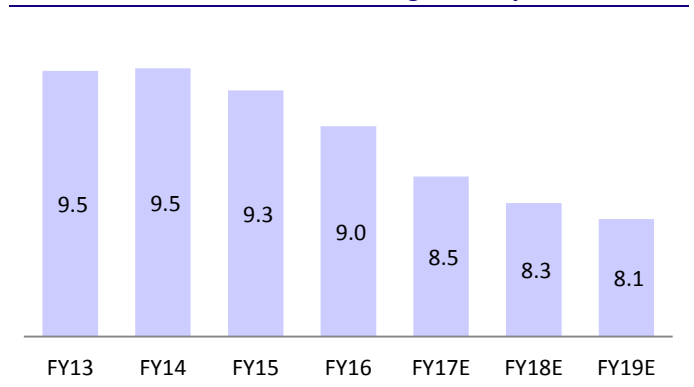
Source: MOSL, Company

Exhibit 5: NCD maturity (INR b) – Good refi opportunity



Source: MOSL, Company

Exhibit 6: Cost of funds to decline significantly



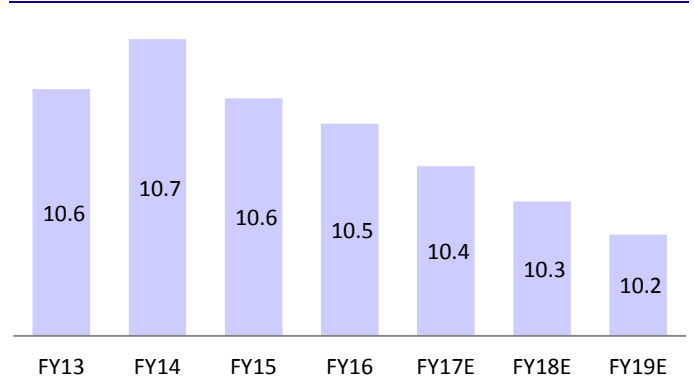
Source: MOSL, Company

Exhibit 7: Home loan rates are at marginal premium to MCLR

	1-yr MCLR (%)	Home loan rate (%)
HDFCB	8.90	9.25
ICICIBC	8.95	9.20
AXSB	9.15	9.35
SBIN	8.90	9.10
BOB	9.25	9.55

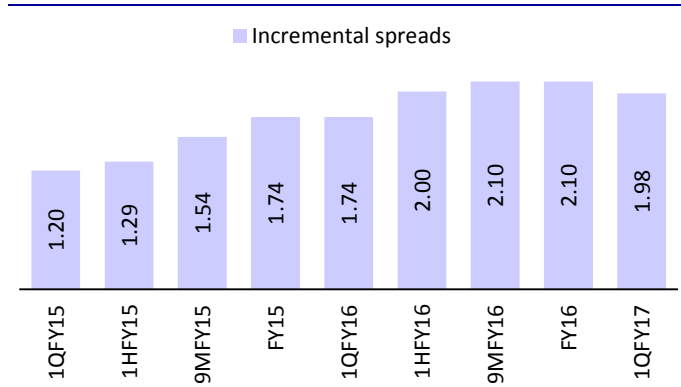
Source: MOSL, Company

Exhibit 8: Loan yields too trending down



Source: MOSL, Company

Exhibit 9: Incremental spreads (reported)



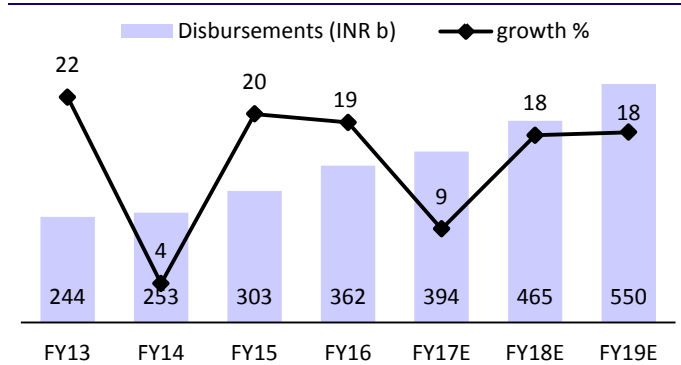
Source: MOSL, Company

Exhibit 10: Incremental spreads will sustain at ~2.0%

	Home loan	Non-retail
Yield (Incremental)	9.7%	12.0%
Share of disbursements	88.0%	12.0%
Incremental CoF	7.8%	7.8%
Weighted Avg Yield	10.0%	
Incremental Spreads	2.2%	

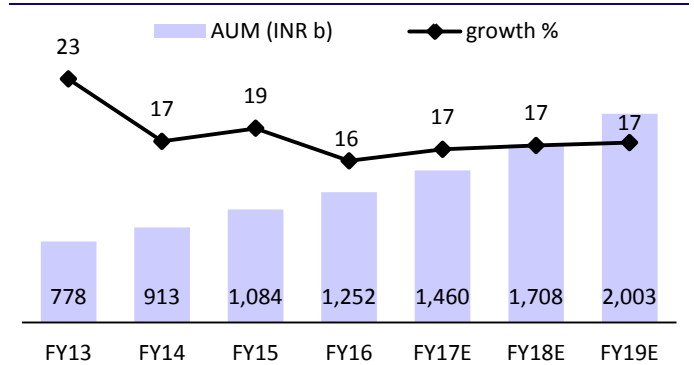
Source: MOSL, Company

Exhibit 11: Disbursement growth will remain robust



Source: MOSL, Company

Exhibit 12: Consistent AUM growth over the medium term



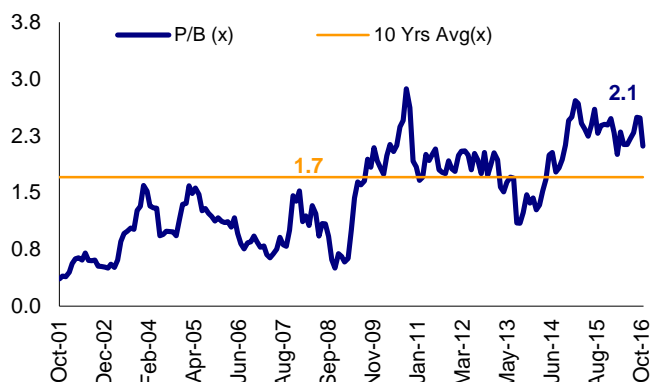
Source: MOSL, Company

Exhibit 13: DuPont analysis

LIC Housing Finance	FY15	FY16	FY17E	FY18E	FY19E
Interest Income	10.9	10.9	10.6	10.3	10.2
Interest Expenses	8.6	8.3	7.9	7.6	7.5
Net Interest Income	2.3	2.6	2.7	2.7	2.7
Non-interest Income	0.3	0.2	0.2	0.2	0.2
Fee Income	0.1	0.1	0.1	0.1	0.1
Treasury Income	0.1	0.1	0.1	0.1	0.0
Other Income	0.0	0.0	0.0	0.0	0.0
Net Income	2.6	2.8	2.9	2.9	2.9
Operating Expenses	0.4	0.4	0.4	0.4	0.4
Cost to income (%)	15.2	14.7	14.8	15.1	15.1
Employees	0.1	0.1	0.2	0.2	0.2
Others	0.3	0.3	0.3	0.3	0.3
Operating Profits	2.2	2.4	2.5	2.5	2.5
Provisions/write offs	0.0	0.1	0.2	0.1	0.1
PBT	2.2	2.3	2.3	2.4	2.4
Tax	0.7	0.8	0.8	0.8	0.8
Tax Rate (%)	34.1	35.2	35.0	34.0	34.0
PAT	1.4	1.5	1.5	1.6	1.6
Leverage (x)	12.6	13.2	13.3	13.4	13.3
RoE	17.5	19.6	20.0	20.7	20.9

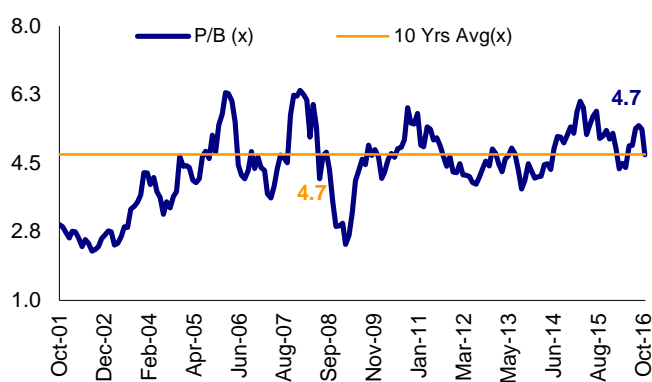
Source: MOSL, Company

Exhibit 14: LICHF P/B



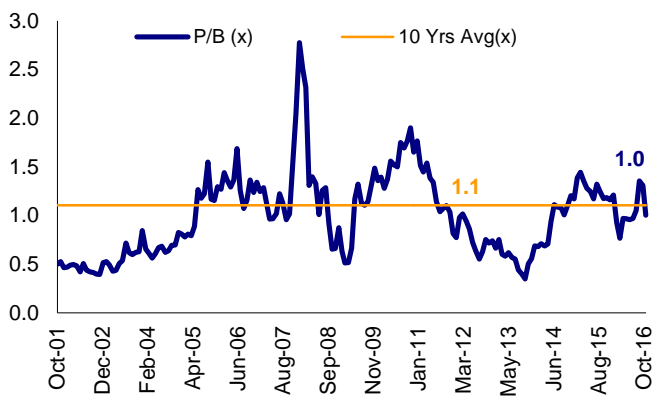
Source: MOSL, Company

Exhibit 15: HDFC P/B



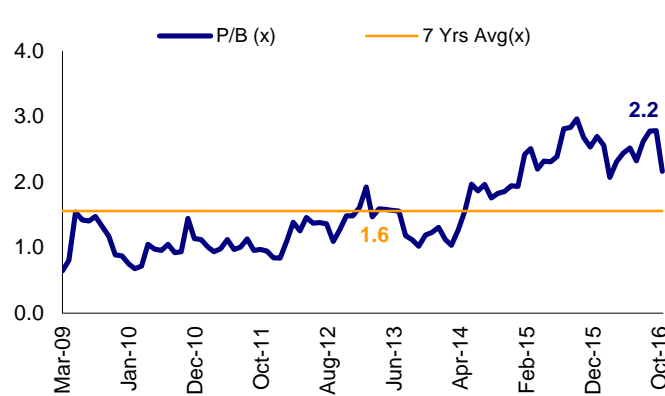
Source: MOSL, Company

Exhibit 16: DEWH P/B



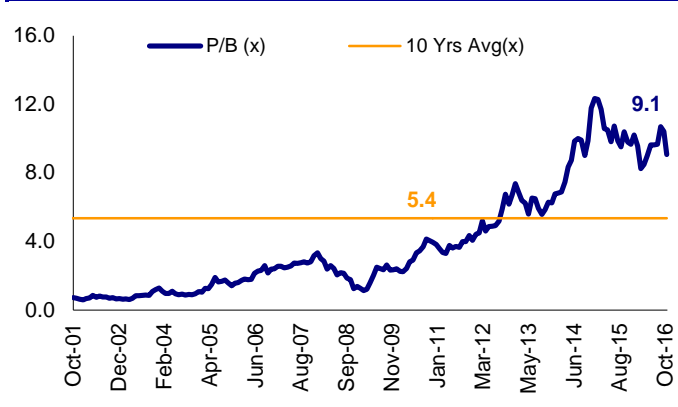
Source: MOSL, Company

Exhibit 17: IHFL P/B



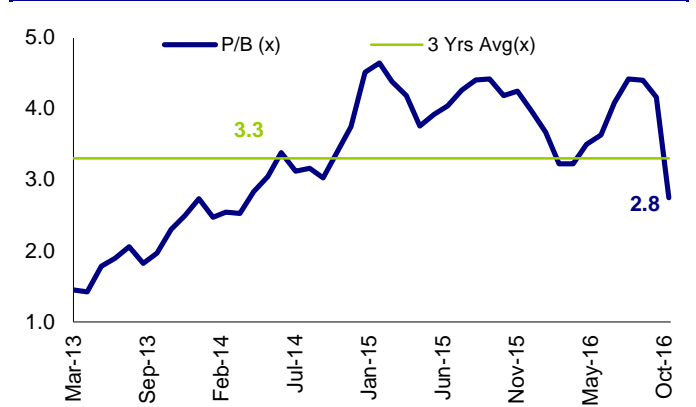
Source: MOSL, Company

Exhibit 18: GRUH P/B



Source: MOSL, Company

Exhibit 19: REPCO P/B



Source: MOSL, Company

Valuation matrix

Financials: Valuation metrics

	Rating	CMP	Mcap	EPS (INR)		P/E (x)		BV (INR)		P/BV (x)		RoA (%)		RoE (%)	
		(INR)	(USDb)	FY17	FY18	FY17	FY18	FY17	FY18	FY17	FY18	FY17	FY18	FY17	FY18
ICICIBC*	Buy	262	23.0	17.2	18.2	11.9	9.9	145	158	1.32	1.14	1.12	1.05	10.4	10.1
HDFCB	Buy	1,199	45.9	58.5	70.3	20.5	17.1	332	386	3.61	3.10	1.92	1.94	18.9	19.6
AXSB	Neutral	466	16.8	13.4	23.7	34.7	19.6	230	250	2.02	1.86	0.56	0.84	6.0	9.9
KMB*	Buy	763	21.2	26.7	33.1	28.6	23.1	208	239	3.67	3.19	1.63	1.81	14.2	15.4
YES	Buy	1,113	7.1	77.4	100.0	14.4	11.1	389	469	2.86	2.37	1.77	1.84	21.6	23.3
IIB	Buy	1,058	9.5	48.4	60.9	21.9	17.4	333	385	3.18	2.75	1.83	1.85	15.5	17.0
IDFC Bk	Neutral	68	3.5	3.2	4.1	21.2	16.6	43	46	1.60	1.49	1.18	1.11	7.8	9.3
FB	Buy	67	1.7	4.6	5.6	14.5	12.0	51	55	1.32	1.22	0.79	0.80	9.4	10.6
DCBB	Neutral	106	0.5	7.2	8.7	14.8	12.2	69	77	1.55	1.37	0.95	0.93	11.0	11.9
JKBK	Neutral	58	0.4	-1.8	5.6	-32.8	10.5	130	136	0.45	0.43	-0.10	0.28	-1.4	4.2
SIB	Buy	21	0.4	3.0	3.6	7.1	5.8	30	33	0.70	0.64	0.59	0.62	10.3	11.7
Private Aggregate			130.2			21.7	17.6			2.56	2.30				
SBIN (cons)*	Buy	258	30.3	14.2	24.6	18.1	10.5	234	253	1.19	1.08	0.46	0.56	7.7	9.8
PNB	Buy	137	4.4	11.4	13.6	12.0	10.0	186	197	0.73	0.69	0.35	0.39	6.4	7.1
BOI	Neutral	117	1.7	-10.8	21.6	-10.9	5.4	239	255	0.49	0.46	-0.16	0.29	-4.6	8.7
BOB	Buy	161	5.7	14.1	20.0	11.4	8.1	157	173	1.03	0.94	0.47	0.60	9.3	12.1
CBK	Neutral	307	2.5	28.3	37.5	10.9	8.2	500	528	0.61	0.58	0.27	0.32	5.8	7.3
UNBK	Buy	149	1.6	15.9	32.0	9.4	4.6	308	336	0.48	0.44	0.26	0.48	5.3	9.9
OBC	Neutral	116	0.6	20.2	21.6	5.7	5.4	412	429	0.28	0.27	0.29	0.28	5.1	5.1
INBK	Buy	250	1.8	30.9	32.8	8.1	7.6	304	330	0.82	0.76	0.70	0.68	10.6	10.3
ANDB	Buy	52	1.6	1.5	6.4	34.0	8.1	109	114	0.48	0.46	0.08	0.31	1.4	5.8
Public Aggregate			50.2			15.9	10.2			0.79	0.75				
Banks Aggregate			180.4			19.7	14.6			1.58	1.46				
HDFC*	Buy	1,225	29.3	34.5	37.8	23.4	18.0	194	217	3.51	2.82	1.84	1.82	19.4	19.0
LICHF	Buy	501	3.8	39.9	49.6	12.5	10.1	213	253	2.35	1.98	1.51	1.55	20.3	21.3
IHFL	Buy	651	4.2	69.5	87.7	9.4	7.4	281	317	2.32	2.05	3.69	3.76	26.0	29.3
GRHF	Neutral	287	1.6	8.0	10.1	35.9	28.4	28	35	10.19	8.27	2.25	2.26	31.3	32.1
REPCO	Buy	594	0.6	30.2	39.8	19.7	14.9	179	215	3.31	2.77	2.14	2.21	18.2	20.2
DEWH	Buy	219	1.0	31.4	38.8	7.0	5.7	202	231	1.08	0.95	1.27	1.31	17.0	17.9
Housing Finance			40.5			19.1	16.0			3.84	3.38				
RECL	Neutral	126	3.8	29.4	33.4	4.3	3.8	168	194	0.75	0.65	2.63	2.54	18.8	18.5
POWF	Neutral	119	4.7	24.0	25.5	5.0	4.6	149	167	0.80	0.71	2.37	2.12	16.8	16.2
Infra Finance			8.5			4.6	4.2			0.78	0.69				
SHTF	Buy	828	2.8	66.9	90.2	12.4	9.2	502	573	1.65	1.44	2.30	2.65	14.1	16.7
MMFS	Buy	265	2.3	14.3	17.4	18.6	15.3	118	131	2.25	2.03	1.97	2.10	12.6	14.0
BAF	Buy	833	1.4	34.9	44.9	23.9	18.6	167	205	5.00	4.07	3.51	3.43	23.0	24.2
MUTH	Buy	289	1.7	28.0	33.6	10.3	8.6	159	180	1.82	1.60	3.66	3.57	18.7	19.9
Asset Finance			9.6			10.6	8.6			1.74	1.54				
NBFC Aggregate			58.6			12.0	10.3			2.17	1.91				
Financials			239.0			17.0	13.3			1.69	1.55				

UR=Under Review*Multiples adj. for value of key ventures/Investments; For ICICI Bank and HDFC Ltd BV is adjusted for investments in subsidiaries

Financials and valuations

Income Statement								(INR Million)
Y/E March	2012	2013	2014	2015	2016	2017E	2018E	2019E
Interest Income	59,827	74,591	90,733	105,467	122,509	140,649	162,770	188,967
Interest Expense	45,911	59,246	71,744	83,102	93,068	104,225	120,211	138,255
Net Interest Income	13,916	15,345	18,990	22,364	29,441	36,425	42,559	50,712
Change (%)	1.4	10.3	23.8	17.8	31.6	23.7	16.8	19.2
Fee Income	1,322	1,549	1,080	1,227	1,453	1,576	1,975	2,336
Income from Investments	804	617	1,083	815	609	709	809	909
Other Income	198	-168	450	343	285	285	285	285
Net Income	16,240	17,343	21,603	24,749	31,787	38,994	45,627	54,241
Change (%)	-8.3	6.8	24.6	14.6	28.4	22.7	17.0	18.9
Operating Expenses	2,371	2,819	3,133	3,885	4,687	5,784	6,887	8,201
Operating Income	13,870	14,524	18,470	20,864	27,100	33,210	38,740	46,040
Change (%)	-10.8	4.7	27.2	13.0	29.9	22.5	16.7	18.8
Provisions/write offs	1,561	789	215	-20	1,465	2,300	1,588	1,870
PBT	12,309	13,736	18,255	20,884	25,636	30,910	37,152	44,170
Tax	3,167	3,504	5,083	7,158	9,028	10,819	12,632	15,018
Tax Rate (%)	25.7	25.5	27.8	34.3	35.2	35.0	34.0	34.0
PAT	9,142	10,232	13,172	13,727	16,608	20,092	24,521	29,152
Change (%)	-6.2	11.9	28.7	4.2	21.0	21.0	22.0	18.9
Adjusted PAT	10,011	10,232	12,017	13,466	16,608	19,884	24,309	28,941
Change (%)	-2.7	2.2	17.4	12.1	23.3	19.7	22.3	19.1
Proposed Dividend	2,112	2,244	2,657	3,022	3,333	4,096	4,999	5,943

Balance Sheet								(INR Million)
Y/E March	2012	2013	2014	2015	2016	2017E	2018E	2019E
Capital	1,010	1,010	1,010	1,010	1,010	1,010	1,010	1,010
Reserves & Surplus	55,812	63,803	74,319	77,174	90,450	106,445	125,967	149,176
Net Worth	56,822	64,813	75,329	78,184	91,460	107,455	126,977	150,186
Borrowings	560,873	687,641	820,356	965,319	1,109,312	1,343,030	1,571,184	1,842,517
Change (%)	24.2	22.6	19.3	17.7	14.9	21.1	17.0	17.3
Total Liabilities	617,695	752,454	895,685	1,043,503	1,200,771	1,450,485	1,698,161	1,992,702
Investments	13,750	18,673	1,993	2,371	2,768	3,045	3,289	3,519
Change (%)	-2.0	35.8	-89.3	19.0	16.7	10.0	8.0	7.0
Loans	630,802	778,120	913,410	1,083,610	1,251,730	1,459,815	1,707,809	2,002,736
Change (%)	23.5	23.4	17.4	18.6	15.5	16.6	17.0	17.3
Net Fixed Assets	623	624	756	797	920	963	996	1,019
Net Current Assets	-27,481	-44,963	-20,474	-43,275	-54,649	-13,338	-13,933	-14,571
Total Assets	617,695	752,454	895,685	1,043,503	1,200,769	1,450,485	1,698,161	1,992,702

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	2012	2013	2014	2015	2016	2017E	2018E	2019E
Spreads Analysis (%)								
Avg. Yield on loans	10.5	10.6	10.7	10.6	10.5	10.4	10.3	10.2
Avg. Yield on Earning Assets	10.2	10.2	10.5	10.3	10.2	10.0	9.8	9.8
Avg. Cost-Int. Bear. Liab.	9.1	9.5	9.5	9.3	9.0	8.5	8.3	8.1
Int. Spread on Hsg. Loans	1.4	1.1	1.21	1.25	1.52	1.9	2.0	2.1
Net Int. Margin on Hsg. Loans	2.4	2.2	2.25	2.24	2.52	2.69	2.69	2.73
Profitability Ratios (%)								
Adj RoAE	20.3	16.8	17.2	17.5	19.6	20.0	20.7	20.9
Adj RoAA	1.8	1.5	1.5	1.4	1.5	1.5	1.5	1.6
Int. Expended/Int.Earned	76.7	79.4	79.1	78.8	76.0	74.1	73.9	73.2
Other Inc./Net Income	1.2	-1.0	2.1	1.4	0.9	0.7	0.6	0.5
Efficiency Ratios (%)								
Fees/Operating income	2.1	2.0	1.2	1.1	1.2	1.1	1.2	1.2
Op. Exps./Net Income	14.6	16.3	14.5	15.7	14.7	14.8	15.1	15.1
Empl. Cost/Op. Exps.	30.6	32.1	33.1	34.1	32.1	36.4	36.1	35.7
Asset-Liability Profile (%)								
Loans/Borrowings Ratio	112.5	113.2	111.3	112.3	112.8	108.7	108.7	108.7
Debt/Equity (x)	9.9	10.6	10.9	12.3	12.1	12.5	12.4	12.3
Gross NPAs (Rs m)	2,652	4,712	6,090	4,947	5,678	6,304	6,888	7,571
Gross NPAs to Adv.	0.4	0.6	0.7	0.5	0.5	0.4	0.4	0.4
Net NPAs (Rs m)	849	1,953	3,534	2,344	2,705	3,152	3,444	3,786
Net NPAs to Adv.	0.1	0.3	0.4	0.2	0.2	0.2	0.2	0.2
CAR	13.0	12.5	16.4	16.5	15.5	14.5	13.5	10.5

Valuation

Book Value (INR)	112.5	128.3	149.2	154.8	181.1	212.8	251.4	297.4
Growth (%)	28.2	14.1	16.2	3.8	17.0	17.5	18.2	18.3
Price-BV (x)	4.5	3.9	3.4	3.2	2.8	2.4	2.0	1.7
Adjusted BV (INR)	112.1	127.3	147.3	153.6	179.7	211.1	249.6	295.4
Price-ABV (x)	4.5	3.9	3.4	3.2	2.8	2.4	2.0	1.7
EPS (INR)	18.1	20.3	26.1	27.2	32.9	39.8	48.6	57.7
Growth (%)	-11.7	11.9	28.7	4.2	21.0	21.0	22.0	18.9
Price-Earnings (x)	27.7	24.7	19.2	18.4	15.2	12.6	10.3	8.7
Adj. EPS (INR)	19.8	20.3	23.8	26.7	32.9	39.4	48.1	57.3
Growth (%)	-8.4	2.2	17.4	12.1	23.3	19.7	22.3	19.1
Price-Earnings (x)	25.3	24.7	21.1	18.8	15.2	12.7	10.4	8.7
Dividend Per Share	3.6	3.8	4.5	5.0	5.5	7.0	8.5	10.1
Dividend Yield (%)	0.7	0.8	0.9	1.0	1.1	1.4	1.7	2.0

E: MOSL Estimates

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