# Can Fin Homes Ltd.

23rd November 2022

## Growth to sustain with Best-in-class Asset Quality

**Can Fin Homes Ltd. (CFHL) was incorporated by Canara Bank in association with HDFC and UTI. The Company focuses on low & middle-income group individuals, and first-time home buyers, with an average ticket size of Rs 2.1 Mn in FY22. The Company has grown its AUM base at 26% CAGR from Rs. ~27 Bn in FY12 to Rs. ~270 Bn in FY22 while maintaining pristine asset quality. Apart from this, CHFL has demonstrated exemplary performance on all operating parameters, irrespective of the phases of the industry cycle. We believe the Company will maintain 18-20% growth in AUM by opening 12-15 new branches yearly in low-competitive cities. Also, the Company has forayed into cross-selling insurance policies, for which it has partnered with three companies. Given its ability to grow in the future while maintaining strong asset quality, we initiate coverage on Can Fin Homes Ltd. with a BUY rating and a target price of Rs. 670 (2.2x FY24E Adj. Book Value).**

### Stable growth in Advances to continue

The Company has shown exemplary AUM growth over the previous decade (FY12-22) and has grown its AUM ten-fold from Rs. ~27 Bn to Rs. ~270 Bn. We believe CFHL can maintain a robust growth rate of 18-20% for the foreseeable future. The Company plans to establish 12-15 branches per annum to achieve this target. The locations of these branches will be meticulously selected to avoid competition from banks. Apart from this, increased focus will be on lower tier cities and ticket sizes, which will help the Company to maintain pricing power over its customers.

### Best in Class Asset Quality to be maintained

The Company has maintained a remarkable asset quality by keeping GNPA ratio below 1% since FY16. For FY22, the Company reported a GNPA ratio of 0.6%, the lowest in the industry. To have exceptional asset quality, the Company has maintained a strict credit policy that allows lending only to low-risk and safe customers, like salaried or self-employed.  Between the two, salaried borrowers induce more certainty to cashflows, thereby substantially reducing Portfolio At Risk (PAR). To ensure this, the Company has guided to maintain 70% AUM in favor of salaried borrowers.

### View and Valuation

The Company has a strong growth history and best-in-class asset quality across various industry phases driven by excellent risk management techniques. We believe that CFHL will grow its loan book at 18-20% in the foreseeable future and maintain its robust asset quality. Given the strong business outlook, we ascribe an adjusted P/B multiple of 2.2x to FY24E adjusted Book Value resulting in a target price of Rs. 670 and an upside of ~27% from the CMP.

## BUY

CMP Rs. 525.7

TARGET Rs. 670 (27.4%)

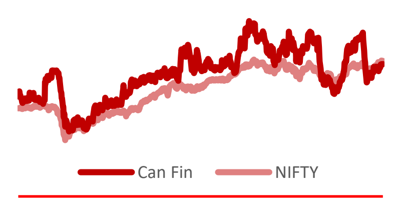
### Company Data

| | |
|---|---|
| MCAP (Rs. Mn) | 69,918 |
| O/S Shares (Mn) | 133 |
| 52w High/Low | 685 / 407 |
| Face Value (in Rs.) | 2 |
| Liquidity (3M) (Rs. Mn) | 910 |

### Shareholding Pattern %

| | Sept 22 | Jun 22 | Mar 22 |
|---|---|---|---|
| Promoters | 30.0 | 30.0 | 30.0 |
| FIIs | 9.3 | 0.0 | 0.0 |
| DIIs | 23.3 | 24.8 | 24.7 |
| Non-Institutional | 37.4 | 45.2 | 45.3 |

### Can Fin Homes vs. Nifty




*Source: Keynote Capitals Ltd.*

### Key Financial Data

| (Rs Mn) | FY22 | FY23E | FY24E |
|---|---|---|---|
| NII | 8,280 | 10,156 | 11,041 |
| PPOP | 6,820 | 8,347 | 9,289 |
| Net Profit | 4,739 | 5,781 | 6,553 |
| Networth | 30,666 | 35,985 | 42,014 |
| ROA (%) | 1.7% | 1.7% | 1.7% |
| ROE (%) | 15.5% | 16.1% | 15.6% |

*Source: Company, Keynote Capitals Ltd.*

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## Regulations and events that shaped the housing sector over the previous few years

**Demonetization** – Before demonetization, most real estate transactions were made in cash and entailed illicit laundering of funds. Consequently, the actual demand for homes could not be assessed. According to Anarock, the demonetization process reduced black money volume in Indian households by 75–80% and revealed the country's actual housing demand. Moreover, post-demonetization, housing sales outpaced new supply in India's top 7 cities.

**Real Estate Regulation Act (RERA)** – From May'16, all real estate projects were required to be RERA-certified, and builders were required to inform buyers about the project's status on time to avoid penalties. As a result, RERA accreditation became a vital information for customers before purchasing a property. This impacted market demand in the short run.

**IL&FS Crisis** – The IL&FS crisis significantly impacted NBFCs' credit risk, making it challenging to source funds from the debt markets. Investors demanded higher interest rates amidst a lack of trust in NBFCs. As a result, HFCs had a two-year-long liquidity crisis. Only the HFCs with the most robust balance sheets could make their way out of this. As a result, the stronger players gained market share.

**COVID-19** – HFCs had severe problems when banks dropped their interest rates at the beginning of the pandemic as their advances to customers were revalued downwards immediately, but their borrowings from banks were revalued according to their yearly maturity.

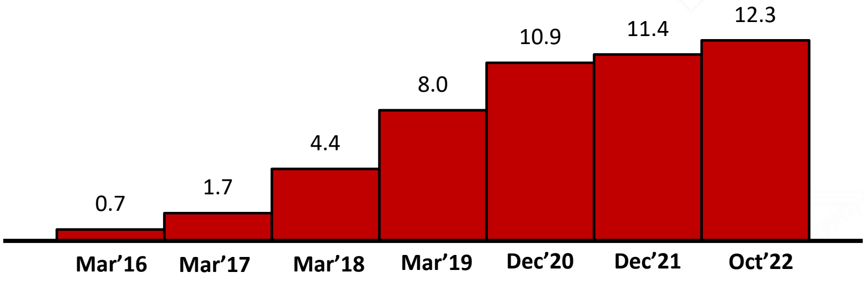
Except for IL&FS and COVID'19, all incidents caused only short-term turbulence in the home loan market. Furthermore, it was for the mass market that was neither regulated nor accounted for. Nevertheless, all measures were taken to improve the real estate sector and promote transparency between all parties, particularly among the builder and the buyer.

## Industry Trends

### Housing Demand

India, which had 1.25 Bn citizens in 2011, reported that 15% of its population was homeless. The Pradhan Mantri Aawas Yojna (PMAY), a program of the Government of India (GOI), started in 2015, verified a startling demand for more than 11 Mn homes. Given the magnitude of the nation's population, PMAY is one of the most significant housing initiatives in the world, aiming to provide a home for every citizen by 2024. As of October 2022, 12.3 million houses have been sanctioned, of which 6.4 million houses have been completed.

Cumulative Houses Sanctioned (units in Mn)

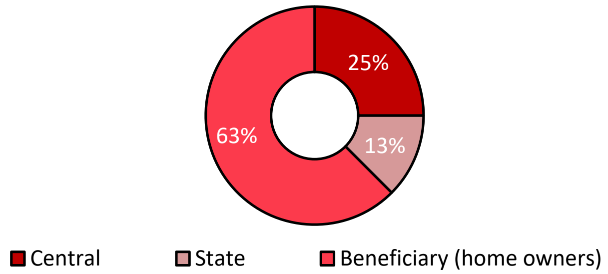



*Source: MoHUA Annual Report, PMAY(U) Updates, Keynote Capitals Ltd.*

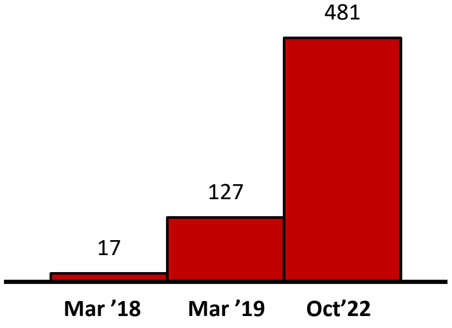
A total of Rs. 8 Trn has been committed to building 12 Mn homes. Of this, Rs. 2 Trn will come from the central government, Rs. 1 Trn from state governments, and the remaining Rs. 5 Trn will come from the recipients (homeowners). This suggests that the government intends to cut the buying expenses for homeowners by 37.5%.

Under PMAY(Urban), the program offers Credit Linked Subsidy Scheme (CLSS), where the subsidy is credited upfront to loan accounts by the government. By far, the CLSS interest subsidy sanctioned up to October 2022 is Rs. 590 Bn (Rs. 480 Bn released, Rs. 110 Bn pending).

Investment Approved towards Houses



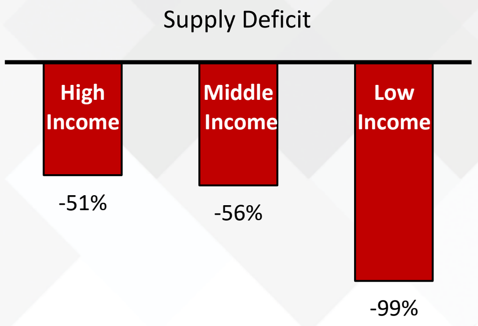

Cumulative CLSS Subsidy Released (Rs Bn)



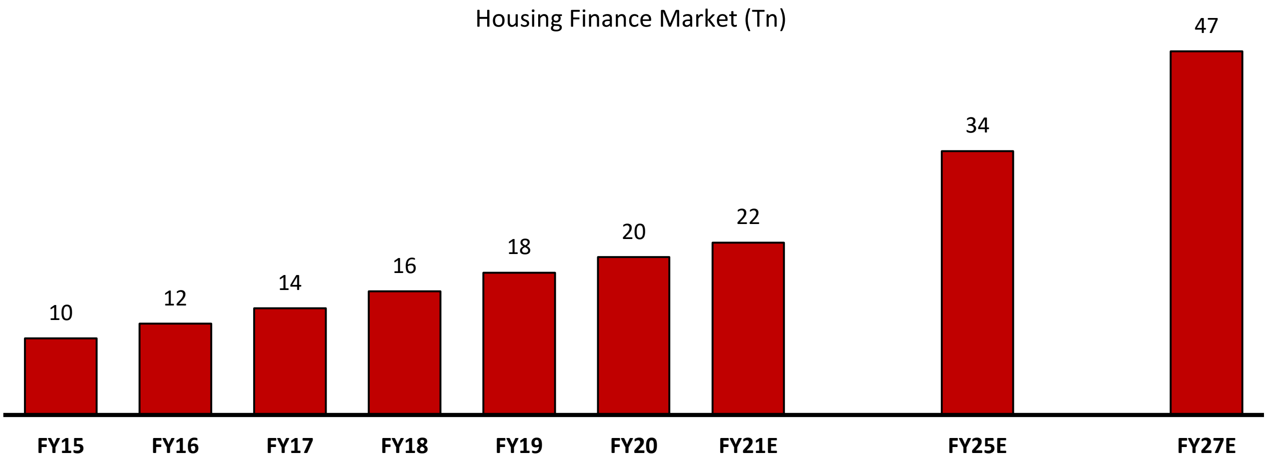

*Source: MoHUA Annual Reports, PMAY(U) Updates, Keynote Capitals Ltd.*

Between 2016 and 2020, when the nation was being benefitted from the PMAY, there was still a housing shortage. The accompanying graph demonstrates that the top 8 cities, which account for ~45% of the nation's housing loans, recorded enormous supply shortfalls in all categories in the corresponding period.

Further, in 2019, the RBI predicted that there would be a shortage of houses in the range of 100 Mn units by 2022, with 95% of those units deriving from the Economically Weaker Sections (EWS) and Low-Income Group (LIG) sectors and only 5% coming from the middle- and upper-income groups. On these grounds, it is anticipated that total outstanding home loans, which were at Rs. 22 Trn in FY21, are expected to grow at 16% CAGR and reach Rs. 47 Trn by FY27.




*Source: Statista, Keynote Capitals Ltd.*

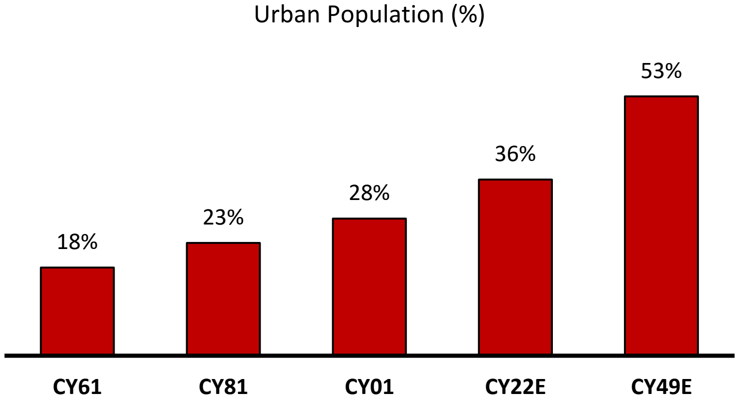



*Source: CRISIL, Keynote Capitals Ltd.*

In addition to the housing scarcity, increased home demand will also uplift the market for the reasons listed below.

### Rise in Urbanization

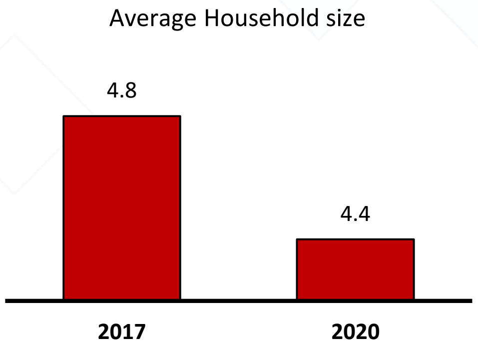
The Ministry of Housing and Urban Affairs predicts that by 2050, more than 50% of Indians will live in urban areas, creating a massive need for homes.




*Source: World Bank and Home First Finance Company Ltd, Keynote Capitals Ltd.*

### Increase in Nuclearization

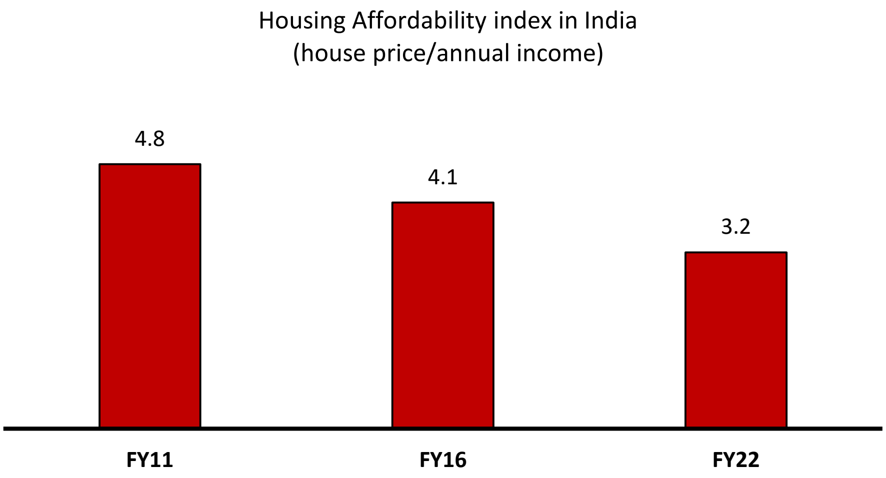
India's average household size is shrinking over time, following China's pattern, where the average family size decreased from 3.2 in 2017 to 2.6 in 2020. In India’s case, the average household size shrunk from 4.8 in 2017 to 4.4 in 2020.




*Source: Company, Keynote Capitals Ltd.*

### Improved Housing Affordability (house price/annual income)

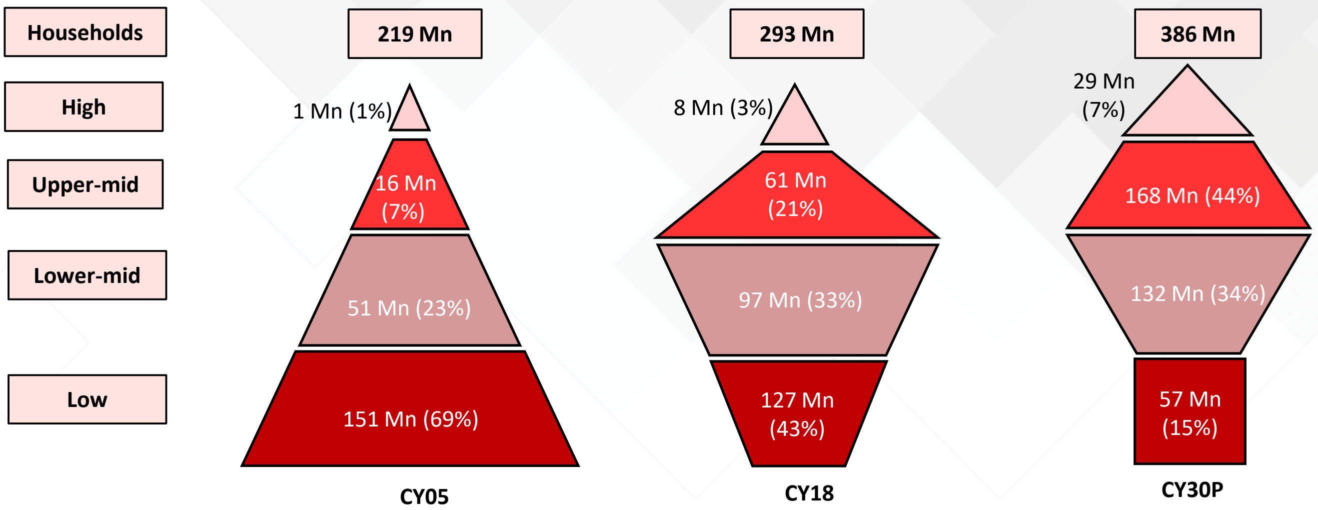
This metric displays the number of years a person will take to purchase a home, given his annual income level. Housing affordability has a three-way impact. First, according to an article in Mint, since 2013, home prices have increased by 1-2% yearly. Two, this rise is slower than the growth in income levels. And finally, interest rates have decreased over time. According to studies, a 1% decrease in interest rate results in a 5% drop in home prices, which implies lower cash outflows.




*Source: Statista, Keynote Capitals Ltd.*

### Share of Premium Homes to Increase

The housing industry is seeing substantial development in the upper-end segment, much like premiumization in different sectors in India, which is banking on the growing income levels of the population. In India, these homes made up 25% of all homes in 2018, and by 2030, it is expected that they will make up 50% of all homes.

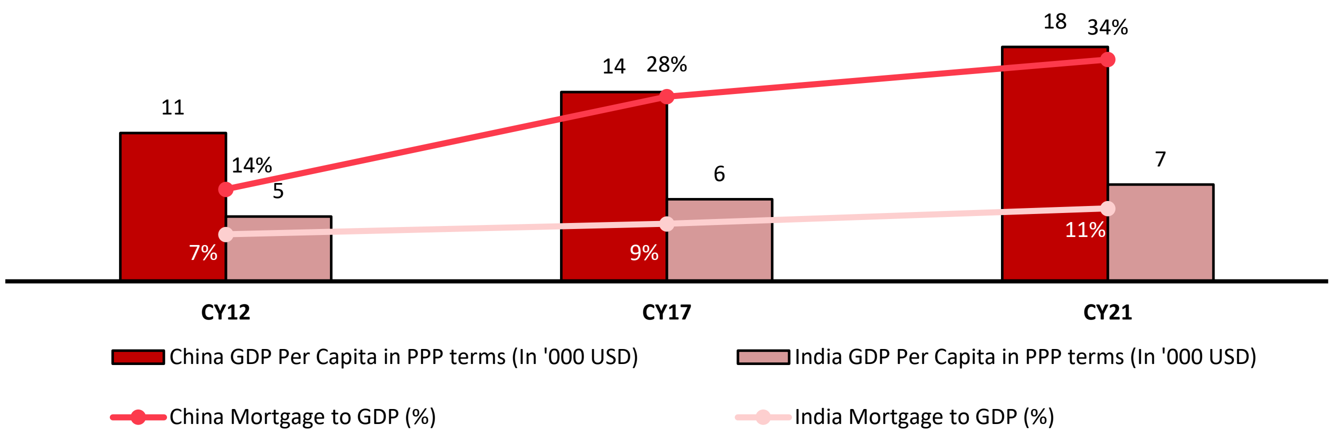



*Source: Home First Finance Company Ltd Annual Report, Keynote Capitals Ltd.*

### Increase in Mortgage Penetration

The average ratio of mortgages to GDP in India is ~ 11%, compared to 20% to 30% in other Asian nations. This opens a wide runway for the industry. Furthermore, as the GDP per capita rises, discretionary expenditure also rises, which includes buying bigger homes. Consequently, mortgage penetration rises. It is anticipated that this domino effect, which has already occurred in nations like the USA and China, will also happen in India.

Mortgage to GDP and GDP Per Capita




*Source: Home First Finance Company Ltd, World Bank, Keynote Capitals Ltd.*

*PPP – Purchasing Power Parity*

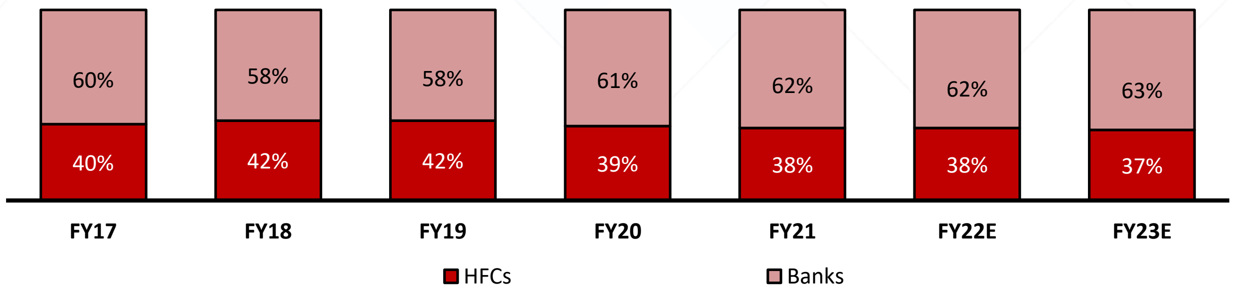
### Favorable Demographics

Currently, 65% of the Indian population is under 35, and it is predicted that the working-class population will increase by 10 Mn between 2021 and 2031. This will induce demand for more homes from the working section of the country.

## Housing Financiers

HFCs spearheaded the home loan market with a 70% market share in 1998, which came down to 30% by 2010. Following this, HFCs regained market share from banks and captured 42% of the market until the IL&FS crisis struck NBFCs in 2018. Currently, HFCs hold a 38% market share, which is expected to go down further as they can't raise low-cost deposits, unlike banks.

Market Share in Outstanding home loans




*Source: CRISIL, Keynote Capitals Ltd.*

## The loss of share

Banks have long been taking away market share from HFCs. However, the latest share shift was caused due to Indiabulls Housing Finance, DHFL, and Gruh Finance. Indiabulls' loan book decreased 30% from Rs. 1 Trn in FY17 to Rs. 0.72 Trn in FY22. Additionally, DHFL's loan assets decreased by around 30% from Rs. 0.9 Trn in FY17 to Rs. 0.65 Trn in Q1FY21. Furthermore, in FY17, Bandhan Bank acquired Gruh Finance, which had a loan book of Rs. 0.13 Trn. As a result of all these market activities, Rs. 0.56 Trn, or 2.5% of the entire loan outstanding for FY22, got shifted to banks.

In summary, only HFCs with strong balance sheets and prudent asset-liability management can sustain against the banks. HFCs like Housing Development Finance Corporation Ltd., LIC Housing Finance Ltd, Can Fin Homes Ltd, and a few others have historically been exhibiting their strength.

## Outlook

Several factors will drive the future of the housing market. High-end houses are expected to dictate the market share with a 50% share (70 Mn units) in 2030 from a 25% share (16 Mn units) in 2018.

CLSS and RERA, revolutionary for housing demand, have been well-equipped on the demand side. With CLSS, the central and state governments will contribute 25% and 13% of the cost, respectively, lowering the load on home buyers by 37.5%. On the other side, the RERA accreditation forces developers to act fast, inform customers of the project's status, and deliver houses on schedule. The demand for homes in India will continue to rise as the per-capita GDP rises and mortgage penetration increases.

The home loan market is expected to create an opportunity of Rs. ~26 Trn in the next six years as the market is expected to grow from Rs. 21 Trn in FY21 to Rs. 47 Trn in FY27.

## About Can Fin Homes

Can Fin Homes Ltd (CFHL), one of the leading medium-sized housing finance companies, was established in 1987. The Company has total loans outstanding at Rs. 288 Bn as of September 2022. Canara Bank incorporated CFHL in association with HDFC and UTI. As of Sep 2022, Canara Bank holds 30% of the Company.

Although the Company has 204 branches across India, 60% are based in Southern India, and 43% of its loans come only from two states, Telangana and Karnataka.

As of FY22, housing loans account for 81% of its loan book. The remaining loans are for purposes besides housing. The average ticket size for the former is Rs. 2.1 Mn, and Rs. 0.9 Mn for the latter.

The Company has created about 24 products, including Individual Housing Loans, Site Loans, Composite Loans (Purchase of Site and Construction), Personal Loans, Mortgage Loans, Loans against Rent Receivables (LRR), Loans for Commercial Properties (LCP), Flexi LAP, Commercial Housing Loan, Loan on Deposit, Special Urban Housing Refinance Scheme (Direct, Indirect), Top Up Loan, Loan for Pensioners (Nishchint), Flats under construction, etc.

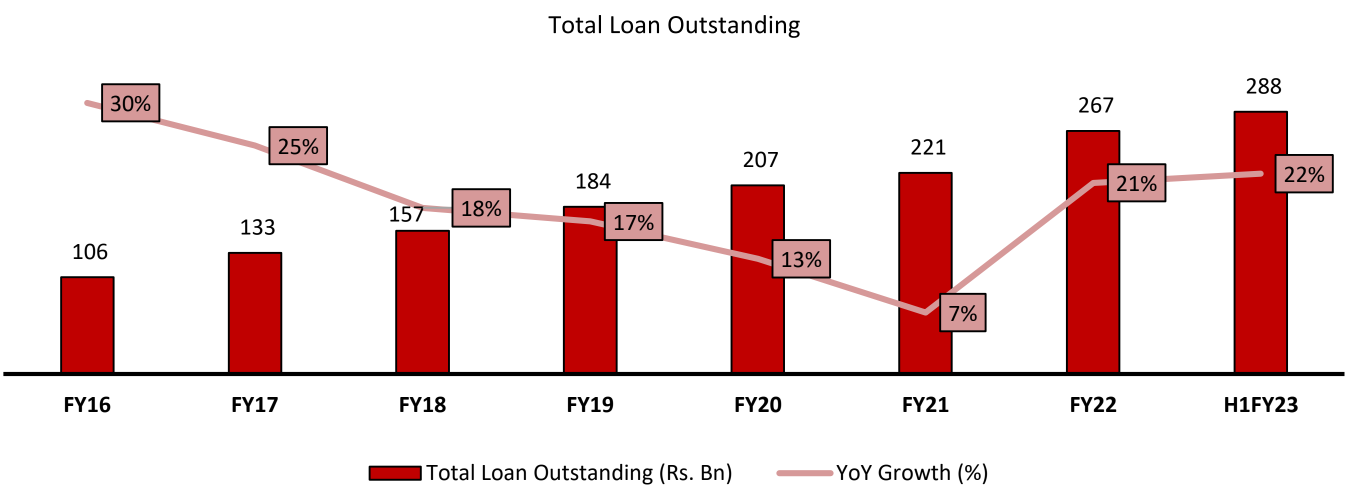
The Company's target market, LIG, MIG I, and MIG II, is the same as PMAY's. A typical borrower of CFHL falls in the 35-year-old bracket, and 74% of its AUM belongs to salaried customers, while the rest is with self-employed customers.

CFHL qualifies among the few HFCs that the RBI and National Housing Bank (NHB) have approved to accept public deposits.

### Operating Metrics Analysis

#### Total Loan Outstanding

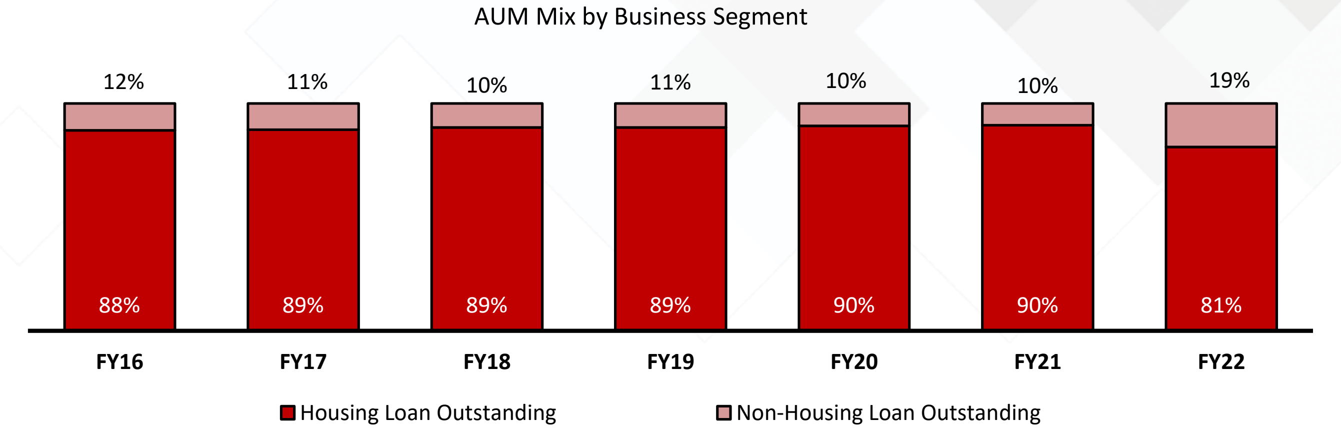
Between 2016 and 2022, the total loan outstanding for the Company grew at a 16% CAGR, which is in line with the industry. From Rs. ~100 Bn in FY16 to Rs. ~300 Bn by H1FY23, the AUM increased to ~3x. In the future, the management has guided to grow its loan book by 18-20%.




*Source: Company, Keynote Capitals Ltd.*

**Business Segments**

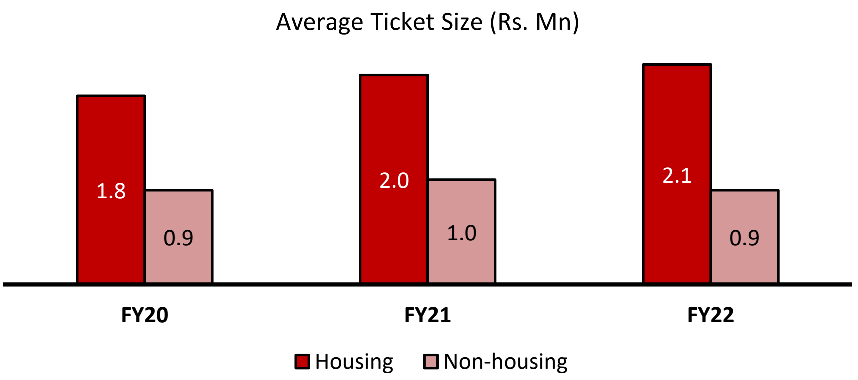
CFHL is a housing-focused NBFC, with more than 80% of the AUM directed to housing.




*Source: Company, Keynote Capitals Ltd.*

**Average Ticket Size**

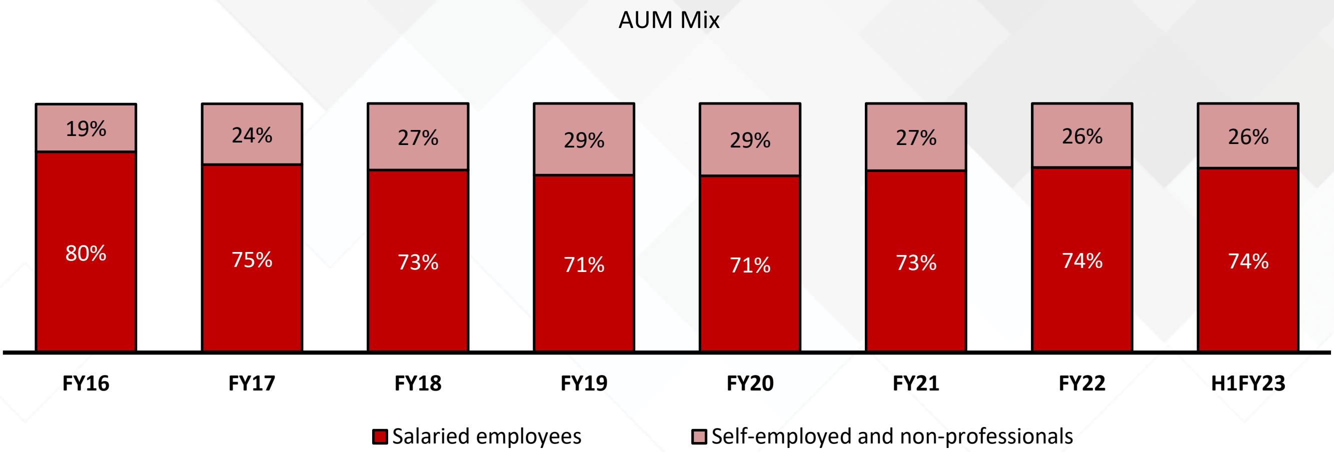
Ticket size in the housing segment has gone up from Rs. 1.8 Mn to Rs. 2.1 Mn, while the ticket size in the non-housing segment has remained at Rs. 0.9 Mn.




*Source: Company, Keynote Capitals Ltd.*

**AUM Mix by Borrower Type**

The Company has lent the bulk of its AUM to salaried customers as they offer cash flow certainty. Salaried customers form 74% of the total outstanding AUM of the Company as of H1FY23. Due to the COVID'19 pandemic, the Company discontinued lending to builders in FY20, which had previously contributed 0.1% of AUM. By FY26, the Company anticipates the builder loan book to form 0.5% of AUM while maintaining the salaried segment AUM at 70%.

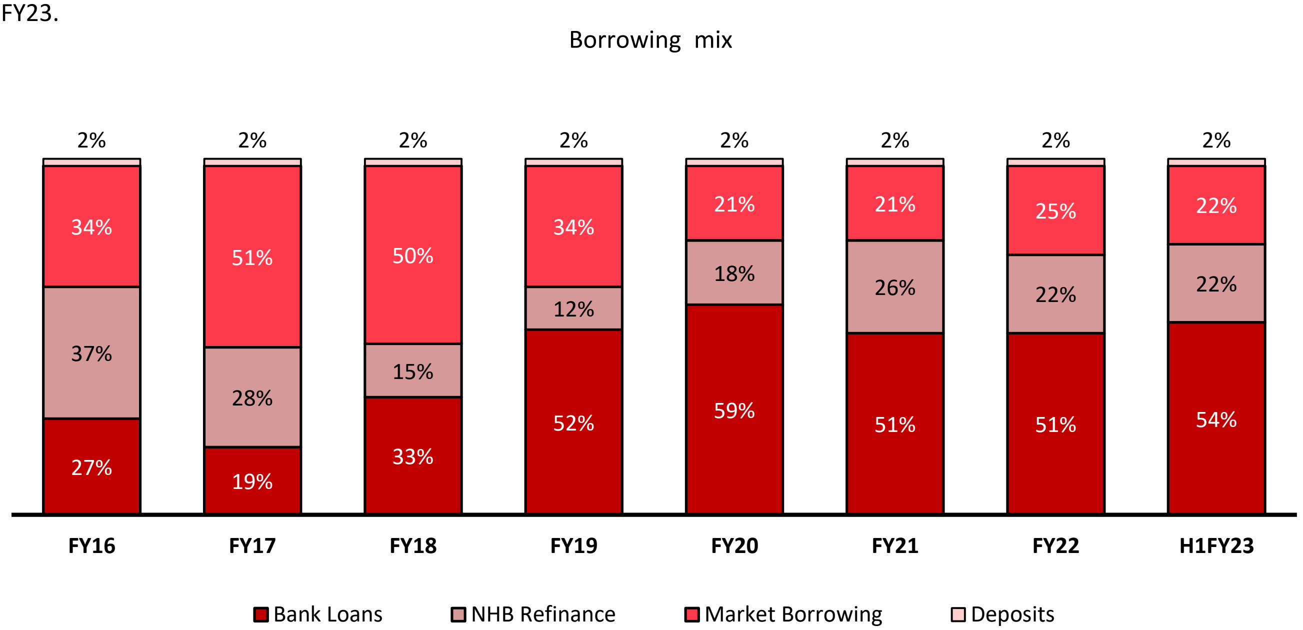



*Source: Company, Keynote Capitals Ltd.*

**Borrowing Mix**

The percentage of bank loans has increased from 27% in FY16 to 54% in H1FY23, benefiting from term loans' competitive rates. However, after the IL&FS liquidity crisis in 2018, market borrowings have drastically decreased to 22% (NCD with 14%, CP with 8%).

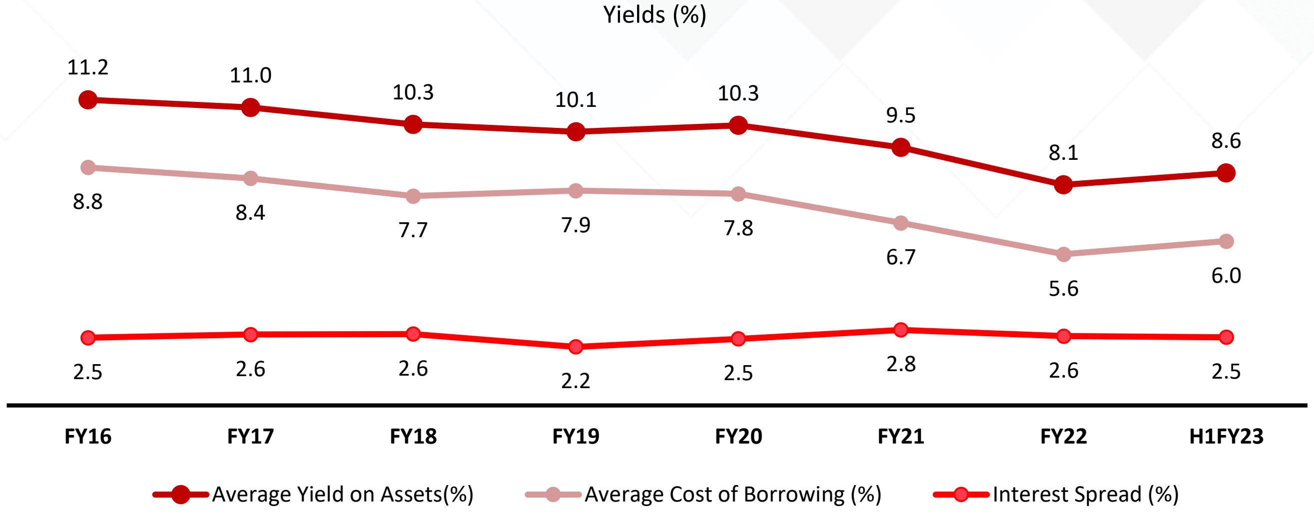
NHB refinancing has a maturity tenure of 10-15 years, and banks have around 7-10 years. This closely matches the Company's average loan tenure of 8.5 years. Deposits have been stable across the decade because the direct cost (cost of borrowing) of accepting deposits is lower. While in comparison, the implicit cost (costs to operate like a bank) is higher for the Company. Additionally, the company has been guided to raise Rs. 10 Bn Tier 1 capital in FY23.




*Source: Company, Keynote Capitals Ltd.*

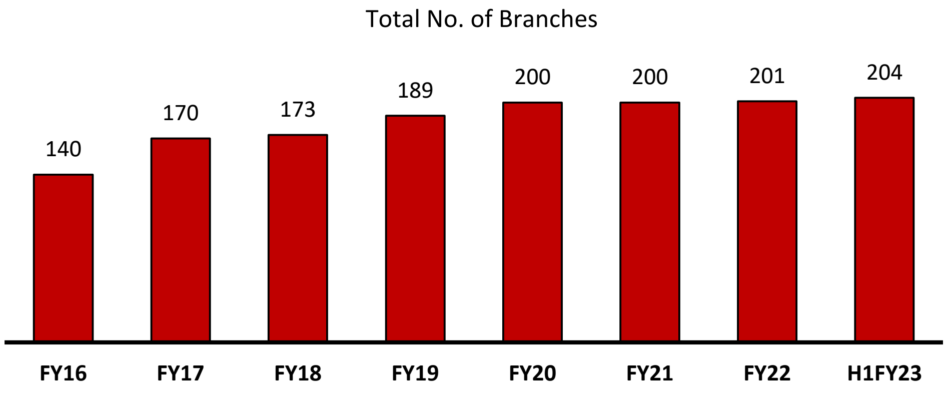
## Yields

Because of the downward-sloping interest rate trajectory, average lending rates have been dropping. However, interest spreads have stayed essentially unchanged at 2.5%, demonstrating the Company's constancy in loan pricing and re-pricing. According to management, the interest spread is expected to be 2.5% in the short term before it settles down at 2.4% in the long run.

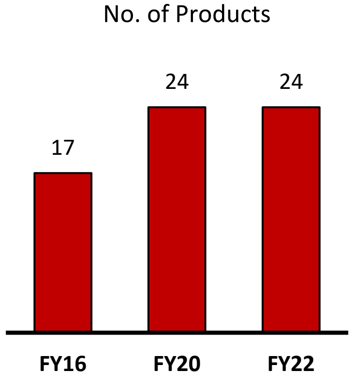


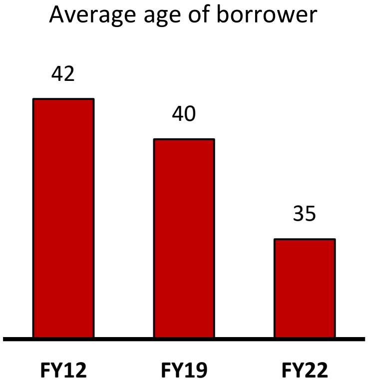

*Source: Company, Keynote Capitals Ltd.*

## Other Metrics




*The company plans to add 12 to 15 branches annually, which would breakeven in the year of the establishment itself.*

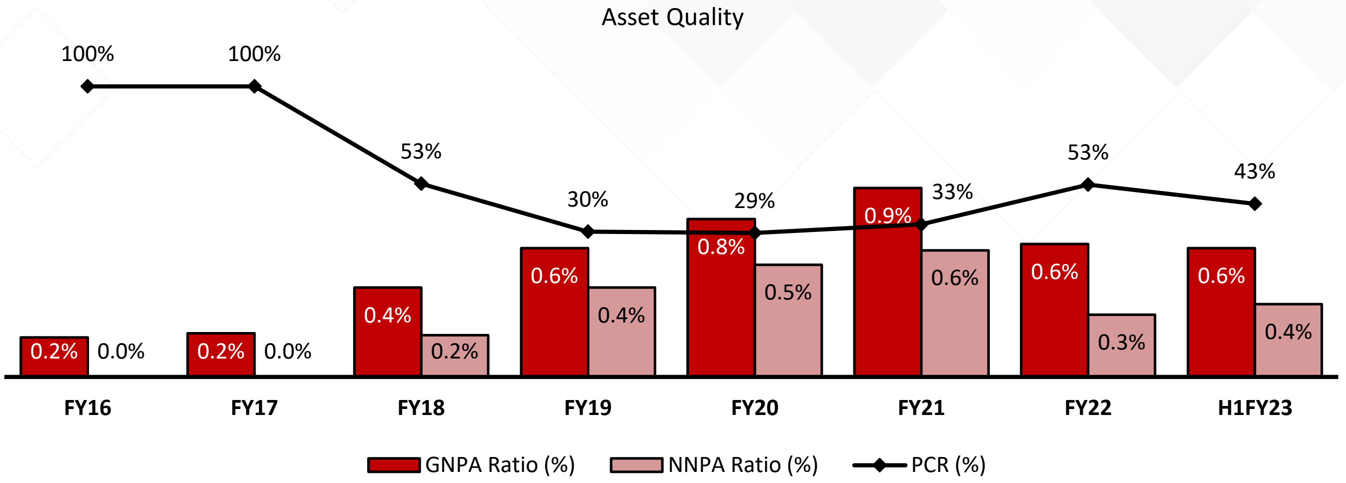



*Source: Company, Keynote Capitals Ltd.*

### Asset Quality

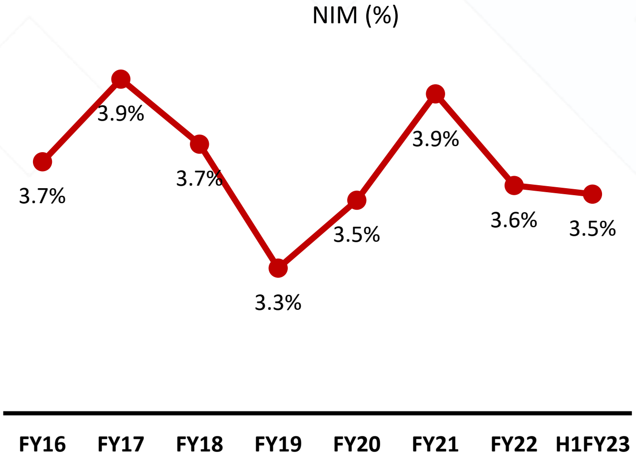
The Company has managed to keep the asset quality under check irrespective of the macro environment. GNPA has stayed below 1%, even during the stressful COVID period from FY20-FY22. This results from management's meritorious decision to lend more than 75% of the loan book to salaried customers.



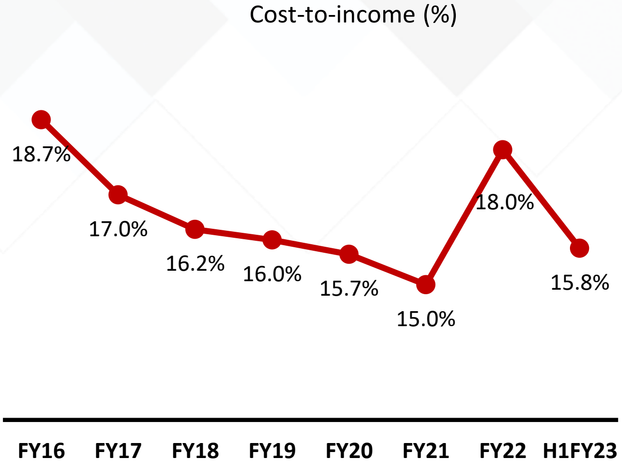

*Source: Company, Keynote Capitals Ltd.*

## Profit and Loss Statement Analysis

**Net Interest Income –** NIM for the Company has stayed in a tight range of 3.5%-3.7% since FY16. Going forward, the Management expects NIM to remain close to 3.5% and mature to 3.0% in the long run.

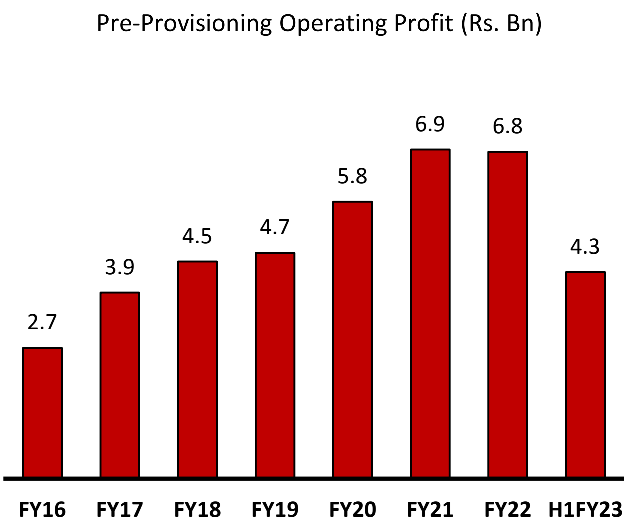



**Cost-to-income -** The Company's cost-to-income ratio has been steadily declining since FY16. This indicates that the Company is earning a higher income per unit of cost with each passing year, signifying an operating leverage advantage.

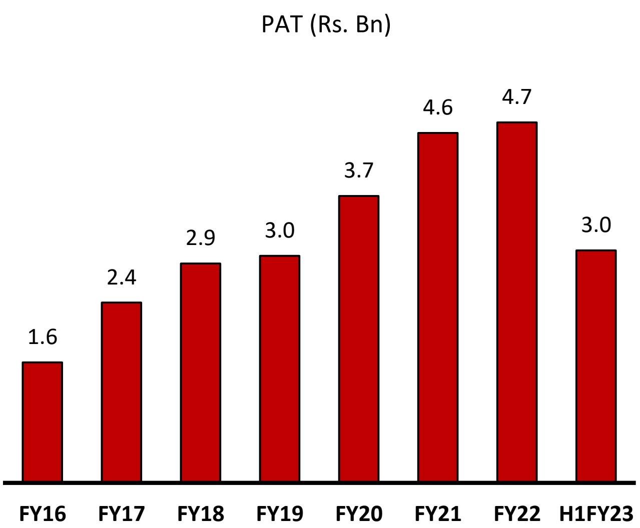



*Source: Company, Keynote Capitals Ltd.*

**Pre-Provisioning Operating Profit (PPOP) –** Between FY16 and FY22, the Company's PPOP steadily increased at a 16% CAGR, doubling from Rs. 3 Bn to Rs. 7 Bn in 6 years.



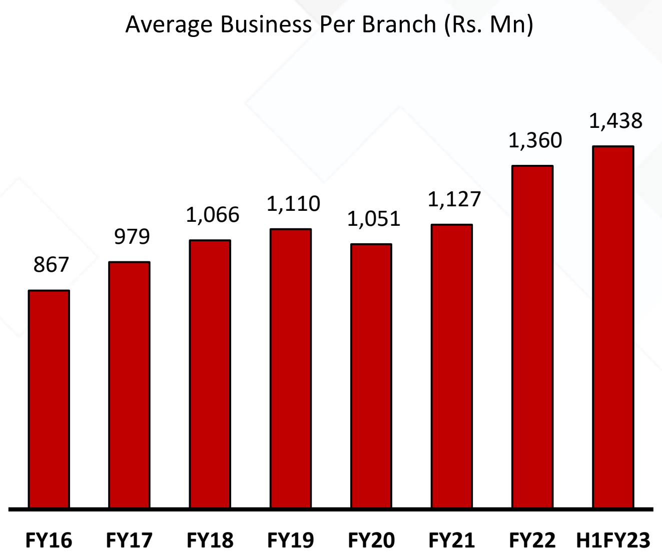

**PAT –** The Company's PAT compounded at a strong 20% rate between FY16-22. PAT for the Company went up ~3x in 6 years.

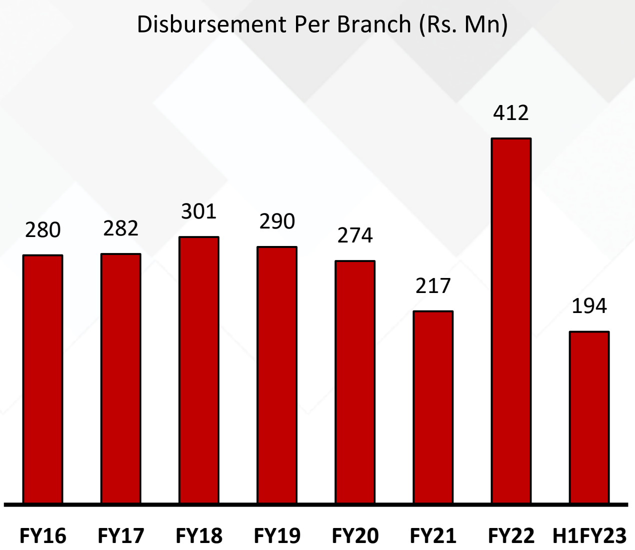



*Source: Company, Keynote Capitals Ltd.*

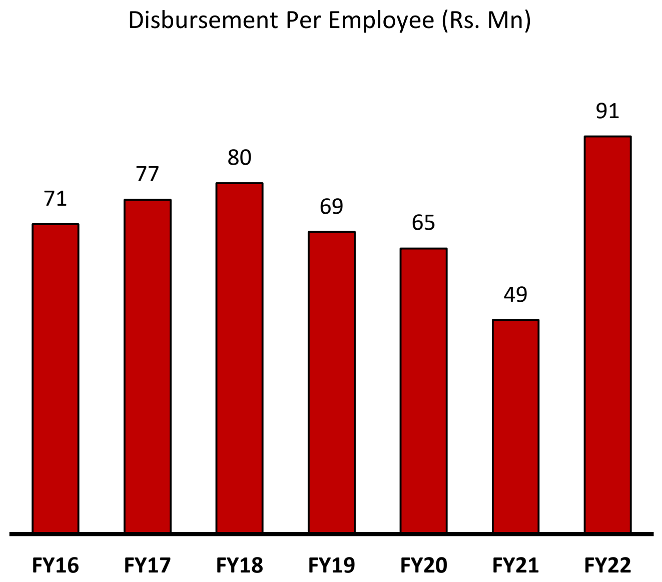
KEYNOTE

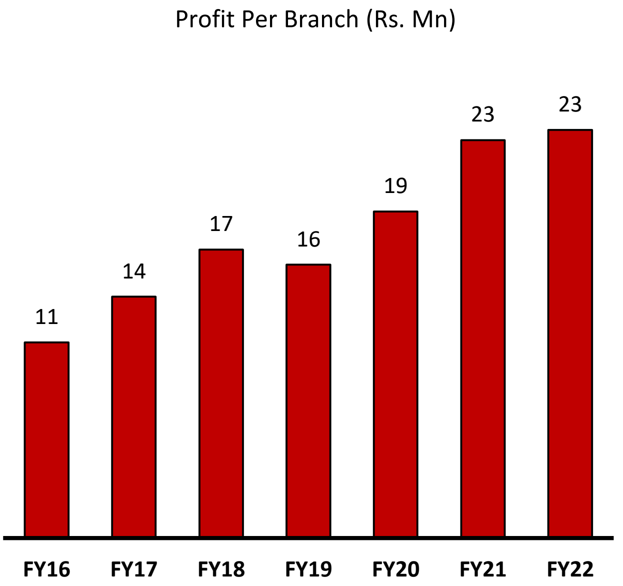
**Productivity Metrics**




*Source: Company, Keynote Capitals Ltd.*



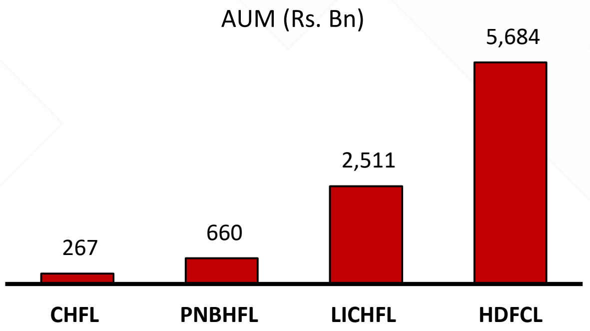



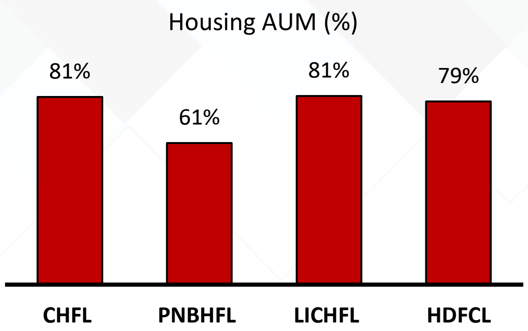

*Source: Company, Keynote Capitals Ltd.*

Barring the COVID period (FY20-FY21), all productivity metrics indicate that the Company has sequentially improved its efficiency in each passing year since FY16. The Company has also managed to nullify the negative impact created by COVID and has surpassed pre-COVID levels on all counts, which shows that CFHL is currently stronger than ever.

## Peer Comparison (FY22)

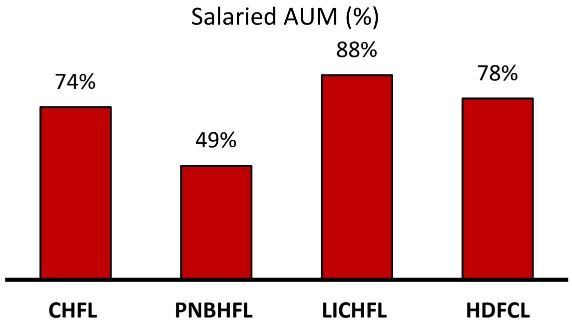
We have reviewed Can Fin Homes Ltd. (CFHL) against peers with similar characteristics. The list includes PNB Housing Finance Ltd. (PNBHFL), LIC Housing Finance Ltd. (LICHFL), and Housing Development Finance Corporation Ltd. (HDFCL) for FY22.

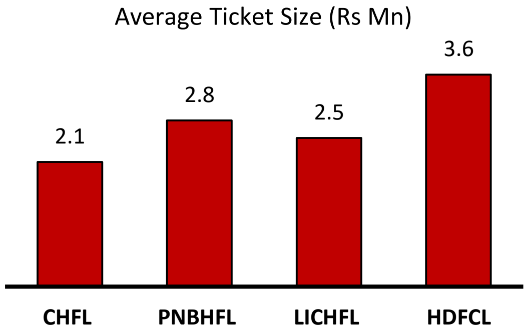



*Source: Company, Keynote Capitals Ltd.*

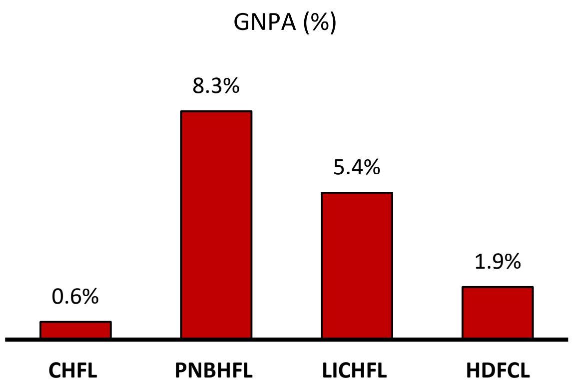
CFHL has the lowest AUM among peers like LIC and HDFC, who are multiple times bigger. The AUM mix of CHFL stands head-to-head with its peers. The Company disbursed 81% of its AUM to home buyers in the last fiscal year.

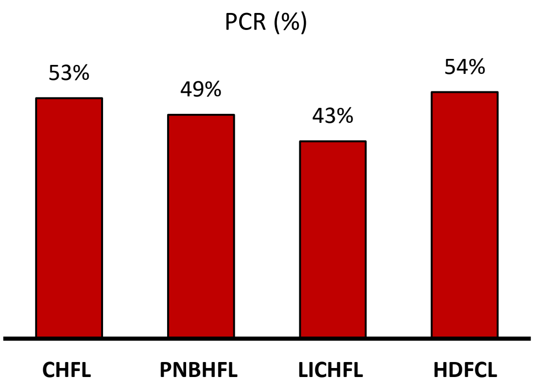



*Source: Company, Keynote Capitals Ltd.*

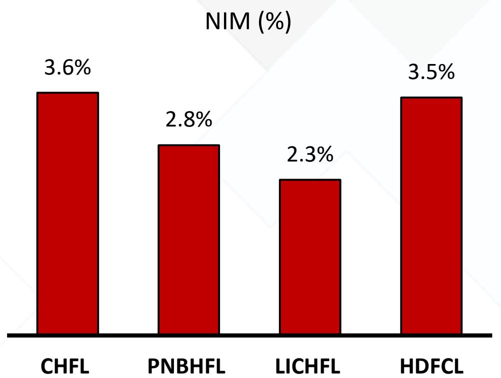
Like better quality, HFCs' salaried customers form more than 70% of CHFL's AUM. Along with this, the average ticket size of the loan remains the lowest for CHFL among its peers.

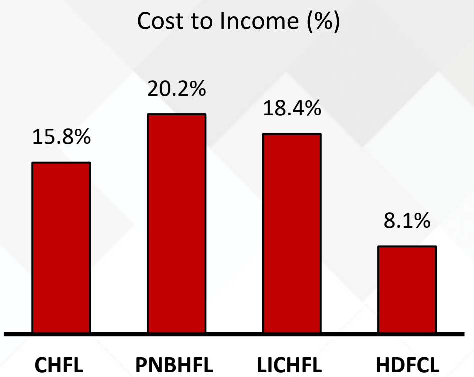



*Source: Company, Keynote Capitals Ltd.*

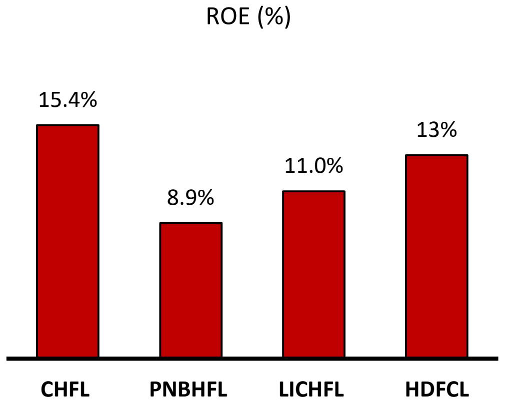
CHFL boasts the best credentials on asset quality, with a GNPA of less than 1%, which is half of the next best player, HDFCL. The Company has also adequately provisioned for bad loans as the PCR for the Company stands in line with the best players in the industry.

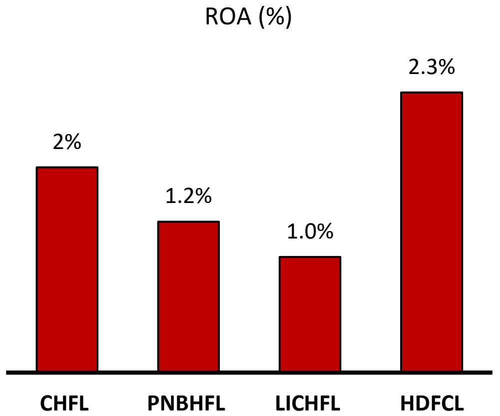



*Source: Company, Keynote Capitals Ltd.*

Besides having the best asset quality among peers, CFHL also makes the best margins. The Company makes a 3.6% NIM, slightly higher than the best player, HDFCL. The Company also earns better income per unit of cost than much more significant players like PNBH and LICHFL. This signifies the superior operational efficiency of CHFL. HDFCL leads this race by a considerable margin.



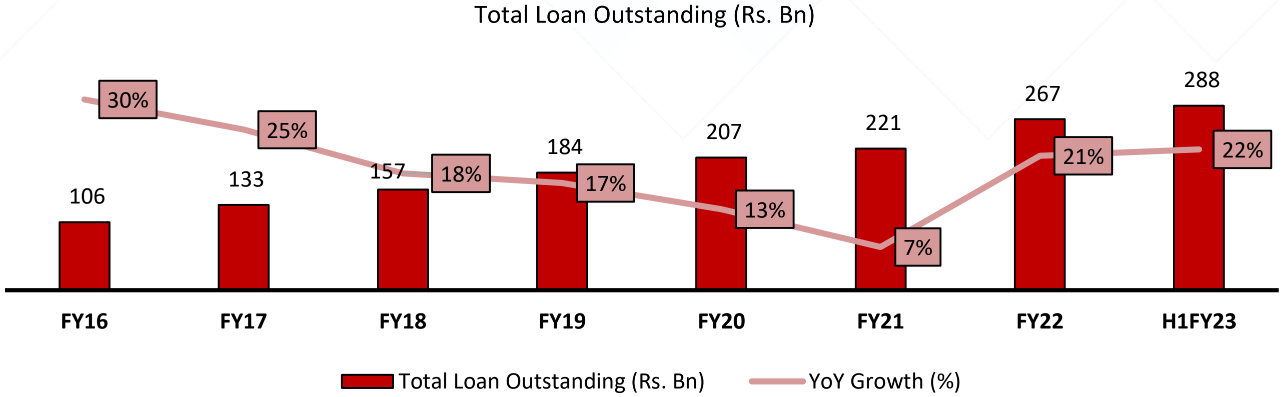

*Source: Company, Keynote Capitals Ltd.*

When compared on return ratios like ROA and ROE, CFHL generates best-in-class results with a ROA of 2%+ and an industry-leading ROE of 15.4%, which is even better than HDFCL.

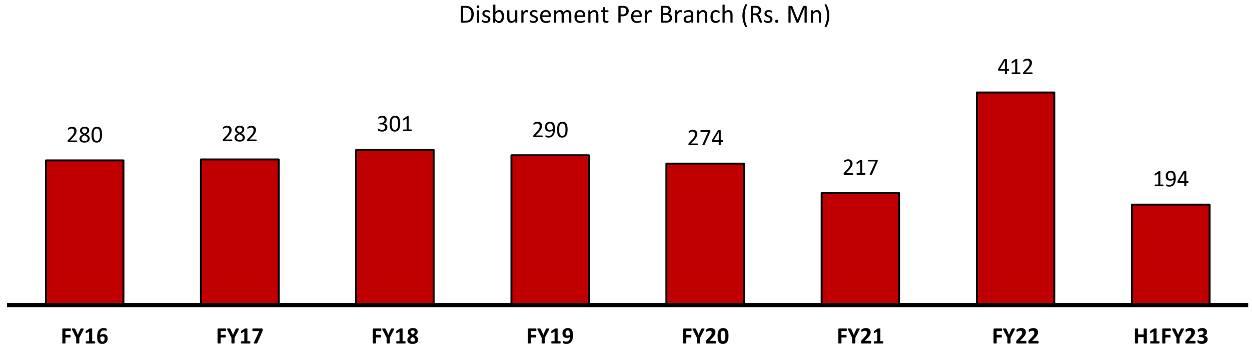
## Opportunities

### Stable growth in Advances to continue

The Company has demonstrated exceptional performance by increasing its advances at a 26% CAGR from Rs. ~27 billion in FY12 to Rs. ~270 billion in FY22. For the next several years, the Company anticipates to compound its advances at 18-20%. The Company has prudently decided on this growth rate as it would increase its advances significantly and maintain the historical level of GNPA ratio below 1%.




*Source: Company, Keynote Capitals Ltd.*

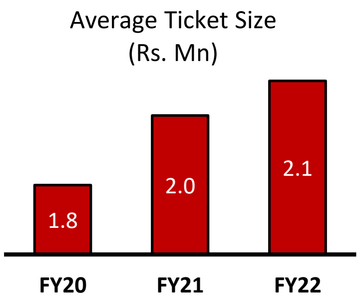



*Source: Company, Keynote Capitals Ltd.*

For this expansion, the Company intends to open 12-15 new branches annually. According to the Company, every branch breaks even within 9-10 months of opening, implying that the branches will become cash flow positive in the first year.

The cities and locations for new branches are meticulously selected such that they are not so competitive with banks. The Company is concentrating its efforts in tier 2, 3, and 4 cities where opportunities are growing. The Company has also begun to expand into tier one, where it was not active previously.

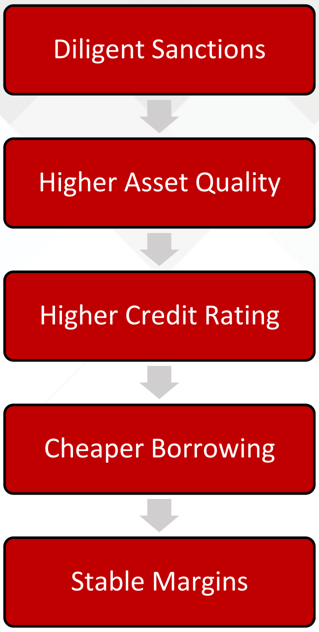
Competition is higher in tier-one cities compared to lower-tier cities. Also, if we look at customer negotiation power, higher ticket-size borrowers have more negotiating power compared to lower ticket-size borrowers. The locations, profiles, and ticket sizes are chosen so that the Company can have pricing power while growing its AUM.




*Source: Company, Keynote Capitals Ltd.*

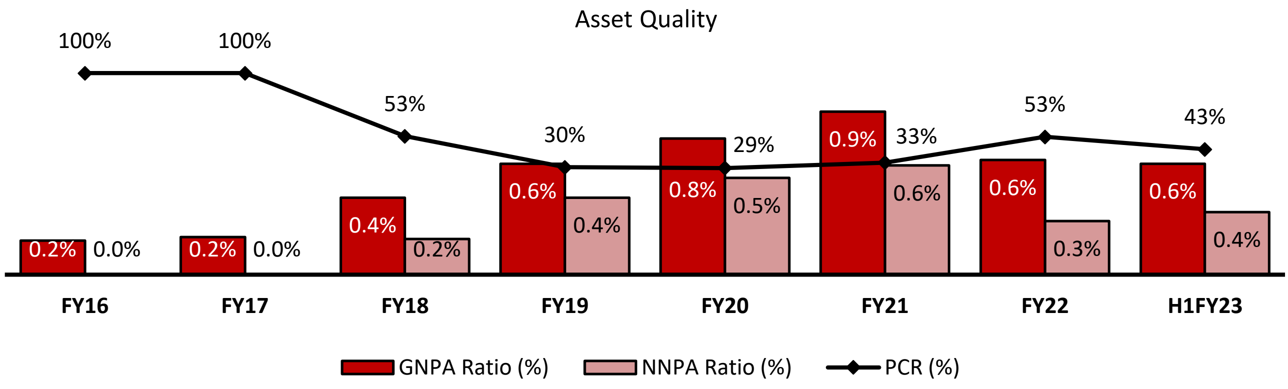
## Best in Class Asset Quality to be maintained

CFHL has maintained exceptional asset quality. The GNPA ratio has not surpassed 1% since FY16. The primary driver for this pristine asset quality is a strict credit risk policy and a systematic methodology for reviewing each borrower's subjective and objective information. The Company has a policy that gives branch managers the authority to analyze and sanction loans up to a particular amount, after which the application is routed to superiors above them. This checks-and-balances technique aids in the prevention of bad-asset-buildup. If we look at larger ticket-size loans, out of the total AUM, only 3% has a ticket size of more than Rs. 5 Mn.




Currently, the Company has lent ~75% of its AUM to salaried borrowers, 50% of whom are from the private sector, and the remaining 50% are government employees. These borrowers have a monthly disposable income of Rs. 20,000 to Rs. 45,000, which provides consistency in the monthly collection. The Company ensures that even self-employed non-salaried borrowers are equally capable of regular loan repayments. In summary, the Company strictly accepts low-risk customers. It purposefully selects locations with a solid payback culture, like Gujarat and Rajasthan, where there are more self-employed individuals, but it also inhibits healthy credit culture.

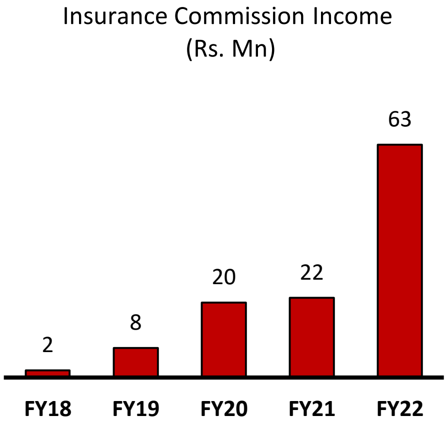
The Company has a superior track record of maintaining excellent asset quality across different borrower profiles.




## Increase in Additional Income

The Company applied for an IRDAI license in FY18 to operate as a corporate insurance agency. The Company sells life and general insurance products in partnership with Canara HSBC OBC Life Insurance Co. Ltd. and Bajaj Allianz General Insurance Co. Ltd.

The commission revenue for CHFL has grown astoundingly (at a low base) over the last five years. The Company has been prudently increasing this additional income by cross-selling insurance policies with its loans. The blended attachment rate for general and life insurance is 70%. Given the progression of this business in the previous years, it can be ascertained that this is a promising business.




*Source: Company, Keynote Capitals Ltd.*

## Challenges

### The Hustle and Juggle of BT (Balance Transfer) in and out

At the origination of loans, the Company doesn't compete with banks for sourcing customers. It transpires 2-4 years after a loan sanction when the customers want to refinance their loan. Amidst these circumstances, the Company's retention team works tirelessly but faces this structural issue in the industry forever. To combat the BT-outs, the Company tries to have BT-ins from HFCs that lend at higher rates.

One such significant difficult time was during COVID'19 when PSBs had priced home loans at 8.2-8.3%, private banks at 8.95-9.25%, and others at 8.75-15%; as a result, in FY21, HFCs lost many customers to these banks. The Company's yield on average housing assets in the same period was 9.14% which was higher than that of all the banks. In response, the Company pocketed customers from other HFCs' to nullify the BT-outs.

By and large, the Company offers loans at 1.5% higher than the best banks and HFCs in the country. Additionally, BT-ins typically represent 20% of the Company's monthly disbursement. Nevertheless, the Company has never degrown its AUM, showing how well it can budget its BT-ins and outs. However, the risk of not being able to fill the gap every time prevails.

### High-turnover of management

Historically, there have been frequent churns in KMPs at CFHL. In the past 25 years, the average time served by an MD is just around two years, which is precarious. However, the Company has been able to grow very well over the due course, which implies that the fundamentals, bylaws, credit policies, etc., that make the system of the Company are potent and robust.

Despite the high KMP turnover, the Company has succeeded in growing its AUM while maintaining a healthy lending culture visible in the best-in-class asset quality.

Apart from attracting good quality AUM, the Company has also shown steady improvement in its operating parameters and now stands at the strongest position in its history.

## Financial Statement Analysis

### Profit & Loss

| Y/E Mar, Rs. Mn | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| **Net Interest Income** | **8,067** | **8,280** | **10,156** | **11,041** | **12,214** |
| Other Income | 30 | 70 | 70 | 70 | 70 |
| Net Income | 8,097 | 8,350 | 10,226 | 11,111 | 12,284 |
| Operating Expenses | 1,230 | 1,530 | 1,879 | 1,822 | 1,832 |
| **Pre Provision Operating Profit** | **6,867** | **6,820** | **8,347** | **9,289** | **10,452** |
| Provisions | 680 | 460 | 638 | 552 | 651 |
| **Profit Before Tax** | **6,187** | **6,360** | **7,708** | **8,737** | **9,800** |
| Tax | 1,614 | 1,621 | 1,927 | 2,184 | 2,450 |
| **Profit After Tax** | **4,573** | **4,739** | **5,781** | **6,553** | **7,350** |

### Balance Sheet

| Y/E Mar, Rs. Mn | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| Share Capital | 266 | 266 | 266 | 266 | 266 |
| Reserves & Surplus | 25,832 | 30,400 | 35,719 | 41,747 | 48,510 |
| **Networth** | **26,098** | **30,666** | **35,985** | **42,014** | **48,776** |
| Borrowings | 1,92,929 | 2,46,477 | 2,93,090 | 3,45,846 | 4,08,098 |
| Other Liabilities & Provisions | 1,710 | 2,301 | 2,367 | 2,424 | 2,491 |
| **Total Liabilities** | **2,20,737** | **2,79,444** | **3,31,441** | **3,90,283** | **4,59,364** |
| **ASSETS** | | | | | |
| Cash and Balance | 711 | 14,501 | 13,667 | 15,505 | 17,337 |
| Advances | 2,18,915 | 2,63,781 | 3,16,537 | 3,73,513 | 4,40,746 |
| Fixed Assets & Others | 1,111 | 1,162 | 1,227 | 1,254 | 1,282 |
| **Total Assets** | **2,20,737** | **2,79,443** | **3,31,441** | **3,90,283** | **4,59,364** |

*Source: Company, Keynote Capitals Ltd.*

### Ratios

| | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| **Growth YoY (%)** | | | | | |
| Advance Growth (%) | 6.7% | 20.5% | 20.0% | 18.0% | 18.0% |
| Borrowing Growth (%) | 2.9% | 27.8% | 18.9% | 18.0% | 18.0% |
| NII Growth (%) | 18.1% | 2.6% | 22.7% | 8.7% | 10.6% |
| PPOP Growth (%) | 19.1% | -0.7% | 22.4% | 11.3% | 12.5% |
| **Ratios** | | | | | |
| NIM (%) | 3.8% | 3.4% | 3.5% | 3.2% | 3.0% |
| Cost to Income Ratio | 15.2% | 18.3% | 18.4% | 16.4% | 14.9% |
| C/D Ratio | 113.5% | 107.0% | 108.0% | 108.0% | 108.0% |
| Capital Adequacy Ratio (%) | 25.5% | 23.2% | 23.0% | 22.0% | 22.0% |
| ROE (%) | 17.5% | 15.5% | 16.1% | 15.6% | 15.1% |
| ROA (%) | 2.1% | 1.7% | 1.7% | 1.7% | 1.6% |
| **Asset Quality** | | | | | |
| GNPA | 0.9% | 0.6% | 0.5% | 0.4% | 0.3% |
| NNPA | 0.6% | 0.3% | 0.3% | 0.3% | 0.2% |
| PCR (%) | 33.5% | 52.7% | 40.0% | 35.0% | 33.3% |
| Credit Cost (%) | 0.3% | 0.2% | 0.2% | 0.2% | 0.2% |
| **Valuation** | | | | | |
| Book Value Per Share | | 230.6 | 270.6 | 315.9 | 366.7 |
| Adjusted Book Value Per Share | | 217.9 | 258.7 | 304.7 | 356.8 |
| P/BV (x) | | 2.3 | 1.9 | 1.7 | 1.4 |
| Price-ABV (x) | | 2.4 | 2.0 | 1.7 | 1.5 |

*Note: Price is taken as of 23rd Nov 2022*

## Valuation based on Adj. P/B

| Valuation | FY22 | FY24E |
|---|---|---|
| **Scenario** | **Current** | **Expectation** |
| Networth (Rs. Mn) – A | 30,666 | 42,014 |
| GNPA (Rs. Mn) – B | 1,688 | 1,494 |
| Adjusted Book Value (C = A - B) | 28,978 | 40,520 |
| No. of Shares (Mn) - D | 133 | 133 |
| Adj. Book Value Per Share (Rs.) – (E = C/D) | 217.9 | 304.7 |
| CMP (Rs.) | 525.7 | - |
| Adj. P/B – (CMP/E) | 2.4 | 2.2 |
| Target Price (Rs.) | - | 670 |
| % Upside/Downside | - | 27.4% |

*Source: Company, Keynote Capitals Ltd.*

After a prolonged period of stagnancy, the real estate sector is moving towards an upcycle of demand. This can be attributed to increased income and affordability, stable property prices, and more extensive housing space requirements. As per CRISIL, considering the demand prospects, the on-book portfolio of the housing finance companies is expected to grow at 13-15%. Further, the Government's continuous push toward the housing segment will continue to drive loan book growth.

In the past, the Company has consistently grown higher than the industry and is expected to expand its loan book at 18-20%, with a stable NIM of ~3%. The constant decrease in the Cost-to-Income ratio will lead to growth in PPOP at a CAGR (FY22-24) of 17%. Given the superior asset quality, we expect a Credit Cost of ~0.2%, leading to a Net Profit CAGR of 18% in the same period. This will lead to a 17% CAGR growth in net worth from FY22 to FY24.

We believe that the asset quality will further normalize. Therefore, we assume a 0.4% Gross NPA in FY24 from 0.6% in FY22.

The Company has best-in-class asset quality and will grow its loan book at 18-20% in the foreseeable future. Given the strong outlook, we ascribe an adjusted P/B multiple of 2.2x to FY24E adjusted Book Value resulting in a target price of Rs. 670 and an upside of ~27% from the CMP.

DEVIN PRAMOD JOSHI

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## Rating Methodology

| Rating | Criteria |
|---|---|
| BUY | Expected positive return of > 10% over 1-year horizon |
| NEUTRAL | Expected positive return of > 0% to < 10% over 1-year horizon |
| REDUCE | Expected return of < 0% to -10% over 1-year horizon |
| SELL | Expected to fall by >10% over 1-year horizon |
| NOT RATED (NR)/UNDER REVIEW (UR)/COVERAGE SUSPENDED (CS) | Not covered by Keynote Capitals Ltd/Rating & Fair value under Review/Keynote Capitals Ltd has suspended coverage |

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