Eastern Financiers

19th Oct, 2023

Recommendation

LIC Housing Finance Ltd.	BUY
Current Market Price (CMP) **Rs. 467.45**	Target Price **Rs. 720**

Our price target of Rs. 720 offers upside of approximately 54% from current market price, over a 1.5 year period.

Company Profile

LIC Housing Finance Ltd (LICHFL) is the housing finance subsidiary of the life insurance giant, LIC of India, which holds a 45.24% stake. After the merger of HDFC Ltd. into HDFC Bank, LICHFL is the largest pure play housing finance company in India, with an outstanding loan portfolio of Rs 2.76 lakh crs. .

Rationale

- **The numbers have started to look up after a lean patch :** LICHFL posted a weak 5% revenue CAGR and a 6% PAT CAGR in the last 3 Financial Years, mainly due to caution after a bad experience with NPAs and substantial provisioning for the same. But now it seems to be back on the growth path – in Q1FY24, revenue grew a strong 28% and PAT grew a stellar 43%, yoy. Net interest income grew a strong 39% and sharp margin improvement was noticed, with Net Interest Margin (NIM) coming in at 3.21% for Q1FY24 vs 2.51% for Q1FY23.
- **The retail book has been inching up, promises better margin :** - The individual retail home loans constituted 83.6% of the total loan book as on June 30, 2023 vs 82% as on June 30, 2022. As on June 30, 2023, non-housing loans comprised 9.9% and project loans - 4.1% of the entire portfolio. The comforting factor is that out of this 84% retail loans, about 80% is to salaried individuals (of which many work for Govt/PSU) and thus chances of loan default, in the retail portfolio, are quite low. After RBI hiked interest rates in H2FY23, LICHFL increased its prime lending rate by 2.1%, which resulted in the spike in NIM. The weighted average cost of borrowing for LICHFL stood at 7.62% as on June 30, 2023, up from 6.70% as on June 30, 2022. Thus, in the current rising interest rate scenario, LICHF may be able to sustain high NIM.
- **No threat of Equity Dilution :** LICHFL has adequate capitalization with a reported capital adequacy ratio (CAR) of 18.23% and Tier-I CAR at 16.56% as on March 31, 2023. Thus, there's no risk of equity dilution for the next few years.

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- **The NPA nightmare is receding :** The majority share of the loan book (84% of the total portfolio) is individual home loans, where the company enjoys a relatively sound asset quality, with NPA at 1.63% as on March 31, 2023 (1.79% as on March 31, 2022). The major deterioration of the asset quality has been reported in non-housing corporate loans, which forms around 4.3% of the overall loan portfolio, with NPA around 7.09% as on March 31, 2023 of the total advances (6.21% as on March 31, 2022). As on March 31, 2023, the non-housing individual loan portfolio and non-housing project loan portfolio reported NPA of around 4.69% and 0.14%, respectively (March 31, 2022: 5.47% and 0.14%, respectively).

  The loan to value ratio (LTV) which indicates the value of the loan exposure against the value of the underlying mortgaged asset is a very comfortable 52% for Q1FY24. The LTV comfort is even better now as real estate prices have risen across India in 2023. Also, with the backing of the Real Estate Regulatory Authority (RERA), the risk of housing project completion has been mitigated.

- **Primed to deliver growth:** LICHFL underwent an organizational restructuring, on the advice of the Boston Consulting Group (BCG) and also undertook a major overhaul of its technology platform recently. The new MD, who took charge earlier this year, seems to be keen to deliver growth, mainly led by a foray into tier 2 and tier 3 towns.

  LICHFL's business of borrowing wholesale and lending retail is on a good wicket now since the system deposit growth is slack and it's very competitive to build a low-cost deposit franchise.

Recommendations

- Housing Finance Companies (HFCs) now account for about a third of housing loans and this share has stabilized in the last few years despite the onslaught of banks and NBFCs. It seems the competitive pressure on HFCs has eased and the current market share of about 33-35% is sustainable.
- LICHFL is poised to do well, backed by a diverse Board of Directors. The new CEO has growth aspirations and the CFO is an old hand in the same Company.
- The LICHFL stock is fairly cheap and quotes at a PE of 7, while peers quote at PE of around 15. It also quotes below Book Value while peers quote between 2-3X of Book Value. The RoE in Q1FY24 is a good 19%, making it more compelling.
- Another upside could be a hike in the dividend payout ratio to about 20-25%, which may then result in a dividend yield of about 3%, making it worth a wait till markets wake up to see this opportunity.

Contact Us ***(033) 40006800*** ***service@easternfin.com***

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