

Can Fin Homes

18 June 2020

Reuters: CNFH.NS; Bloomberg: CANF IN

Prudent underwriting to keep the ship steady; retain BUY

Can Fin Homes Ltd delivered a strong performance during 4QFY20, followed by not-so-bad commentary on outlook for FY21. We think that following a prudent underwriting strategy over the years has helped the company keep its asset quality in good stead with NPAs of 0.8% (one of the lowest in the industry). While we build in higher NPAs in FY21 given the external macros and the impact on the self-employed segment, we think that the company should be able to revert back to normalcy faster than peers. Growth should take a backseat in FY21 due to greater focus on collections and recoveries in addition to a weak demand environment amid a slowing economy. Reducing the intensity of balance transfers is a key lever to ensure the book grows over FY20 as disbursements are expected to be lower than FY20. For FY22, we expect growth to come back to 10%. Liquidity is comfortable up to Dec'20, net of repayment to banks and disbursements. In addition, the company is looking to raise equity capital in the near future, which should provide comfort from a funding standpoint besides strengthening the balance sheet. Cost of funds continues to be favorable and least among peers, coming in at 7.5% incrementally compared to 7.8% for 4QFY20, which should support NIMs. Despite higher provisioning in FY21, we expect the company to deliver 16% ROE (partly impacted by capital raise/larger base), which is the highest across our HFC coverage. Given its overall track record, we remain positive on the company's ability to manage the near-term crisis well. We also believe that the company has the potential to deliver 20% ROE under normal economic conditions, given its overall business strategy. We retain BUY rating on the stock with a target price of Rs432, based on 2.0x FY22E ABV.

Growth outlook subdued, loan mix favorable: During 4QFY20, disbursements declined by 10% YoY and 6% QoQ, primarily due to the lockdown. For FY20, disbursements were flat while fresh approvals were down 1%. For FY21, total disbursements are expected to be lower than FY20 on the back of 1Q being a wash-out followed by a weak demand environment for the rest of year. Demand is expected to return only after 8-10 months. In terms of the loan book break-up, salaried/professionals account for ~71% of the loan book with 50% of these customers employed in government jobs. SENP segment accounts for ~29% of the total loan book and is expected to see higher slippages in the near term. Given the impact of the lockdown on the self-employed segment, the management has turned cautious on this segment from a strategy standpoint. In terms of product, 95% of the loan book comprises housing loans while LAP is only about 5%. Developer exposure is Rs60mn, which is beneficial from an asset quality standpoint, especially in the current environment. In line with the previously stated strategy, growth was better in non-metros.

Asset quality holding good, should be least impacted among peers: GNPA's, at 0.76%, were down 4bps QoQ and NNPA's, at 0.54%, were down 5bps QoQ. Of total provisions worth Rs408mn, ~Rs365mn was provided for standard overdue accounts against regulatory requirement of Rs211mn. Excluding this, provisions were broadly flat QoQ. 28% of loan accounts have availed moratorium. Given the inherent portfolio construct, the propensity of customers moving into NPA bucket is higher for the delinquent pool rather than for the regular/standard pool. Therefore, most of the slippages are likely to come from the delinquent pool. We think that asset quality pain for Can Fin Homes would be relatively less than peers.

Lower CoF to support NIMs in a competitive market: NIM for the quarter stood at 3.52%, up 19bps YoY/10bps QoQ. The expansion has primarily come on account of improvement in cost of funds, which declined 13bps YoY/11bps QoQ to 7.77%. Incremental cost of funds, at 7.5%, should help keep pricing competitive while ensuring margin stability. Liquidity remains comfortable.

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BUY

Sector: NBFC

CMP: Rs332

Target Price: Rs432

Upside: 30%

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Key Data

| | |
|--------------------------|------------|
| Current Shares O/S (mn) | 133.2 |
| Mkt Cap (Rsbn/US\$m) | 44.3/581.1 |
| 52 Wk H / L (Rs) | 519/253 |
| Daily Vol. (3M NSE Avg.) | 607,634 |

Price Performance (%)

| | 1 M | 6 M | 1 Yr |
|---------------|------|--------|--------|
| Can Fin Homes | 12.4 | (20.8) | (1.4) |
| Nifty Index | 8.1 | (18.8) | (15.3) |

Source: Bloomberg

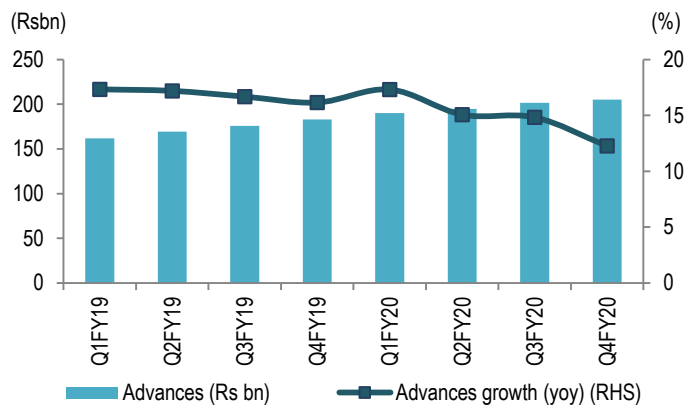
| Y/E Mar (Rsmn) | Q4FY20 | Q4FY19 | Q3FY20 | YoY (%) | QoQ (%) |
|------------------------------------------|--------------|--------------|--------------|--------------|---------------|
| Interest Income | 5,251 | 4,552 | 5,135 | 15.3 | 2.2 |
| Interest Expense | 3,366 | 3,137 | 3,398 | 7.3 | (0.9) |
| Net Interest Income | 1,885 | 1,415 | 1,737 | 33.2 | 8.5 |
| NIM (%) | 3.52 | 3.33 | 3.42 | 19bps | 10bps |
| Fee & Other income | 38 | 77 | 33 | (50.8) | 16.3 |
| Total Income | 1,923 | 1,492 | 1,770 | 28.9 | 8.6 |
| Staff Cost | 155 | 163 | 138 | (5.1) | 12.0 |
| Other Op Exp | 170 | 162 | 130 | 5.2 | 30.5 |
| Total Operating Expenses | 325 | 325 | 269 | 0.0 | 20.9 |
| Cost to Income (%) | 16.9 | 21.8 | 15.2 | -488bps | 172bps |
| Cost to AUM (%) | 0.6 | 0.7 | 0.5 | -8bps | 10bps |
| Pre-Provisioning Operating profit | 1,598 | 1,167 | 1,501 | 36.9 | 6.4 |
| Provisions | 408 | 11 | 45 | 3,638.8 | 797.6 |
| Credit Cost (%) | 0.80 | 0.02 | 0.09 | 78bps | 71bps |
| PBT | 1,189 | 1,156 | 1,456 | 2.9 | (18.3) |
| Tax | 280 | 495 | 390 | (43.4) | (28.1) |
| -effective tax rate | 23.6 | 42.8 | 27 | -1924bps | -321bps |
| PAT | 909 | 661 | 1,066 | 37.5 | (14.7) |
| Other Comprehensive Income | -2 | 8 | -5 | (128.6) | (53.1) |
| Total Comprehensive Income | 907 | 669 | 1,061 | 35.5 | (14.6) |
| EPS (Rs) | 6.8 | 5.0 | 8.0 | 35.5 | (14.6) |
| Advances | 205,257 | 182,845 | 201,716 | 12.3 | 1.8 |

Source: Company, Nirmal Bang Institutional Equities Research

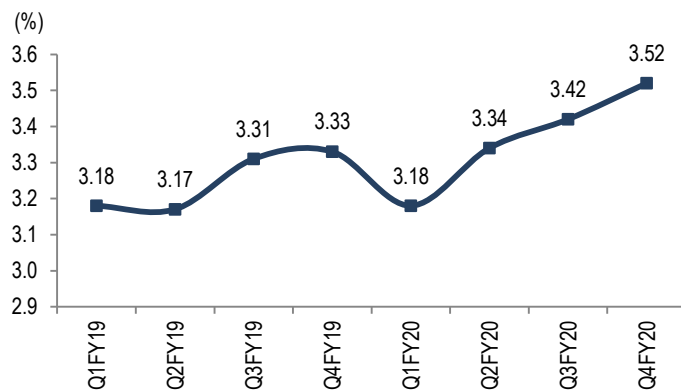
Comprehensive conference call takeaways

- 3Q disbursals growth was good and was expected to continue in 4Q as well but got impacted due to the lockdown. Operations across the branches were suspended on 24th March 2020. Had the lockdown not happened, disbursals growth would have been 17-18%.
- Liquidity has been comfortable after IL&FS and DHFL incidents. The company has been conscious about managing its cost of funds. As of today, undrawn bank lines stand at Rs40bn, which should take care of liquidity requirements up to December 2020. This unutilized amount is net of repayments to banks and disbursements. As per the company, it would be comfortable even if 100% customers opted for the moratorium.
- Number of customers under moratorium is 29%. On value basis, loan book under moratorium is slightly less than 29%. Given the moratorium figures and the inherent construct of the portfolio, the propensity of customers moving into NPA bucket is higher for the delinquent pool rather than for the regular/standard pool. Therefore, most of the slippages are likely to come from the delinquent pool. Share of SENP is higher in the morat pool.
- Broad expectation is that default rates in mortgages will be lower than that in unsecured retail loans.
- Assuming there was no morat, NPAs would have been lower than 3Q.
- The company has been in touch with 100% of its customers and every single effort since going into lockdown has been on collections and recovery. From 20th April to 3rd week of May, focus has been on collections and recovery. New business generation started from end of May. June has been better than May but still not up to the previous levels. Overall demand is likely to take about 2-3 quarters to come back. For FY21, the company expects disbursements to be flat or lower than FY20 but would aim for some bit of AUM growth by reducing balance transfers among other measures.
- Reasons given for availing morat are cash conservation, job losses and pay cuts. The last two are not major reasons for customers who have taken the morat.
- Overall near term strategy is to focus on liquidity, asset quality and profitability.
- Exposure to developers is Rs60mn.
- Geographical focus remains tier 2/3/4 cities. Aim is to grow in markets where there are market share gain opportunities, but that is unlikely to come at the cost of lower profitability.
- Aim is to keep the salaried/self-employed mix same.
- NPAs are likely to surge, especially in the self-employed segment as they have suffered income losses due to the shutdown. However, given the company's customer profile, impact is expected to be lower. Current expectation is that NPAs should revert to current levels in another 4-5 quarters.
- Inherent health of the portfolio is very good because of the underwriting criteria which include focus on salaried segment and not taking into account surrogate income, among other things.
- In terms of offering top-up loan to a customer, one of the criteria is to have a satisfactory repayments history for at least a year. Tenor of top-up loans is not higher than that of the primary loan. Further, top-up loans are offered to the extent the LTV is unutilized on the primary loan. The purpose of such loans is usually home extension/improvement, education or other consumption activities. Top-up loans are not given for speculative purposes. Rate differential for a top-up loan is usually about 25-50bps.
- There has been significant improvement in the standstill pool (worth Rs2.1bn) as customers have been paying their EMLs. Apart from a few pockets like Delhi, Maharashtra, business is coming back to normal.

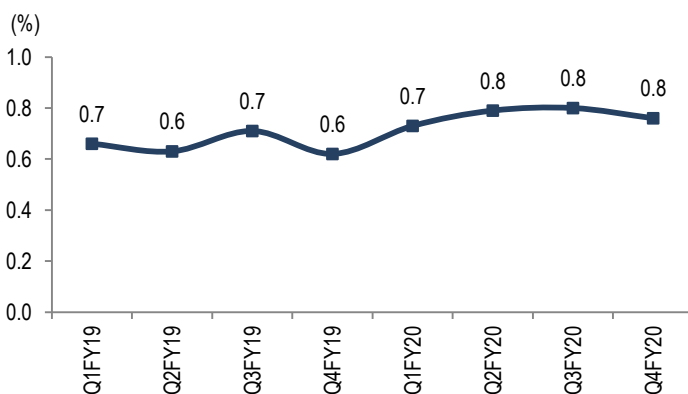
- Equity capital raising plans have been deferred due to the covid-19 outbreak. However, at a later stage during the year, the company would again consider raising equity capital.
- Cost of funds has been coming down and is expected to come down further during FY21 as incremental cost of funds is 7.5%. The company has also been able to secure funds from the NHB at lower rates under a special refinance scheme. Overall funding mix will depend on the respective rates for each funding source.
- Cost of deposits remains high. Growth in deposits will be normal.
- Cost/income ratio may surge a bit due to investments in technology. On the other hand, the company is also working on rationalizing some costs such as lease rentals.
- March collections were normal but April was impacted badly. May and June have seen better collections than preceding months.
- Collections model is largely in-house. For certain locations, the company engages external agencies.
- Within the salaried customers, 50% are government employees. Customers' salary levels are Rs20,000-45,000/month.
- The company does not compete with banks as product and customer profiles are different. There may be some overlap but that is mitigated by being choosy in terms of the geography. Data over the last 10-20 years suggests that despite there being a rate differential between the company and the banks, the company has been able to grow as its customer base/catchment is different.
- Incrementally, branches are being opened outside south. In these areas, proportion of self-employed is higher. For the next one year, the company is cautious on the self-employed segment and has tweaked its internal policies accordingly. Within south, the customer mix is towards the salaried class.
- On the home loans front, sourcing and lead management is likely to be 100% automated.
- Average tenor of a loan is 7-8 years.
- ECL provisioning requirement is lower than NHB/IRAC norms.
- The company funds an apartment usually when it is near the completion stage. In case of independent houses, the land value provides comfort and disbursements are done based on the construction progress.
- Loan of ticket-size of Rs5mn is only 3% of the total portfolio.

Exhibit 1: Advances, advances growth


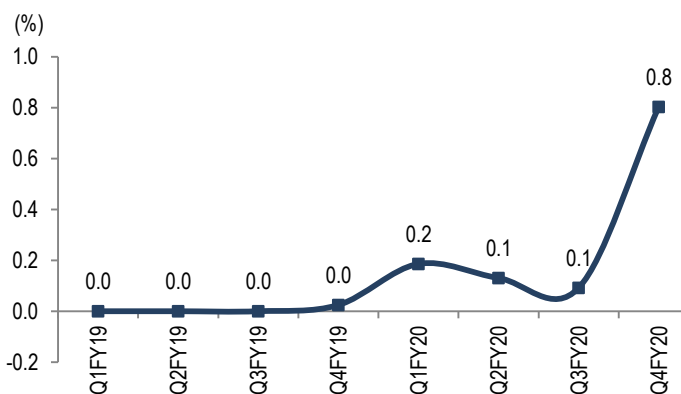
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: NIM (Reported, %)


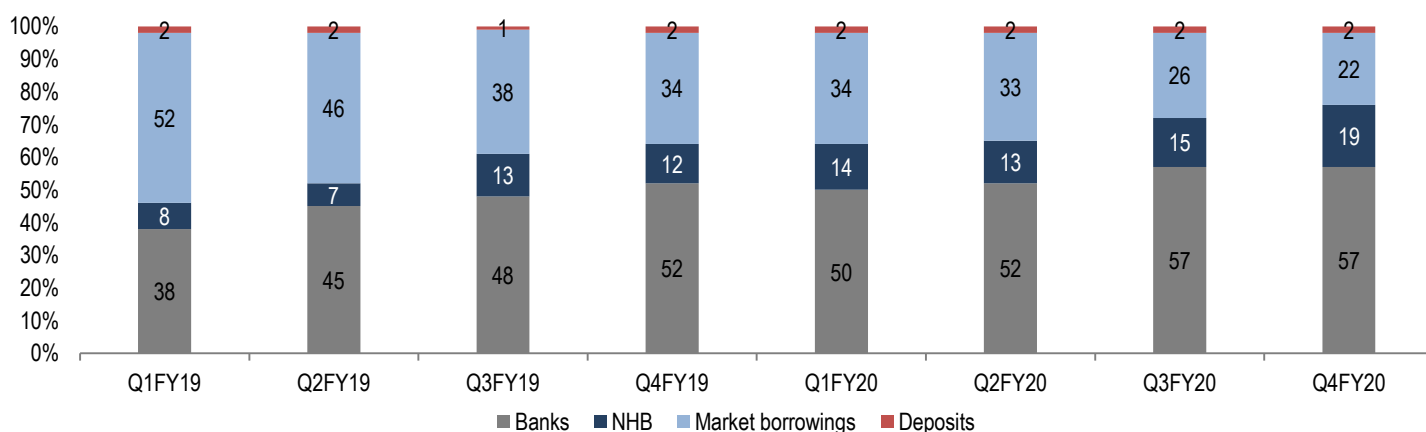
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: GNPA (%)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Credit Cost (Calculated, Annualized, %)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Borrowings Profile (%)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Financial summary

| Y/E March (Rsmn) | FY18 | FY19 | FY20 | FY21E | FY22E |
|-----------------------------------|-------|-------|-------|-------|-------|
| Net interest income | 5,096 | 5,304 | 6,747 | 7,245 | 7,866 |
| Pre-provisioning operating profit | 4,532 | 4,706 | 5,786 | 6,272 | 6,849 |
| PAT | 2,862 | 2,967 | 3,761 | 3,912 | 4,791 |
| EPS (Rs) | 21.5 | 22.3 | 28.2 | 27.7 | 34.0 |
| BV (Rs) | 111.7 | 133.8 | 161.5 | 193.9 | 225.5 |
| P/E (x) | 15.5 | 14.9 | 11.8 | 12.0 | 9.8 |
| P/BV (x) | 3.0 | 2.5 | 2.1 | 1.7 | 1.5 |
| Gross NPAs (%) | 0.4 | 0.6 | 0.8 | 1.1 | 0.9 |
| Net NPAs (%) | 0.2 | 0.5 | 0.5 | 0.7 | 0.6 |
| RoA (%) | 2.0 | 1.7 | 1.9 | 1.8 | 2.1 |
| RoE (%) | 21.3 | 18.2 | 19.1 | 16.0 | 16.2 |

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Actual performance versus our estimates

| (Rsmn) | Q4FY20 | Q4FY19 | Q3FY20 | YoY (%) | QoQ (%) | Q4FY20E | Devi. (%) |
|-----------------------------------|--------|--------|--------|---------|---------|---------|-----------|
| Net interest income | 1,885 | 1,415 | 1,737 | 33.2 | 8.5 | 1,687 | 11.7 |
| Pre-provisioning Operating Profit | 1,598 | 1,167 | 1,501 | 36.9 | 6.4 | 1,499 | 6.6 |
| PAT | 909 | 661 | 1,066 | 37.5 | (14.7) | 1,203 | (24.4) |

Source: Company, Nirmal Bang Institutional Equities Research.

Exhibit 8: Change in our estimates

| | Revised Estimate | | Earlier Estimate | | % Revision | |
|-----------------------------|------------------|-------|------------------|-------|------------|--------|
| | FY21E | FY22E | FY21E | FY22E | FY21E | FY22E |
| Net Interest Income (Rs mn) | 7,245 | 7,866 | 7,275 | 8,458 | -0.4 | -7.0 |
| Net Interest Margin (%) | 3.5 | 3.5 | 3.3 | 3.3 | 17 bps | 20 bps |
| Operating Profit (Rs mn) | 6,272 | 6,849 | 6,464 | 7,465 | -3.0 | -8.3 |
| Profit after tax (Rs mn) | 3,912 | 4,791 | 4,617 | 5,365 | -15.3 | -10.7 |

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials
Exhibit 10: Income statement

| Y/E March (Rsmn) | FY18 | FY19 | FY20 | FY21E | FY22E |
|-----------------------------|--------------|--------------|--------------|--------------|--------------|
| Interest income | 14,906 | 16,995 | 20,189 | 21,320 | 22,603 |
| Interest expense | 9,810 | 11,691 | 13,442 | 14,075 | 14,738 |
| Net interest income | 5,096 | 5,304 | 6,747 | 7,245 | 7,866 |
| Non-interest income | 314 | 318 | 115 | 211 | 233 |
| Net revenues | 5,410 | 5,622 | 6,862 | 7,456 | 8,098 |
| Operating expenses | 878 | 916 | 1,076 | 1,184 | 1,249 |
| -Employee expenses | 448 | 414 | 542 | 607 | 644 |
| -Other expenses | 430 | 503 | 534 | 577 | 606 |
| Pre-prov. Op. Profit | 4,532 | 4,706 | 5,786 | 6,272 | 6,849 |
| Provisions | 221 | 11 | 603 | 1,042 | 444 |
| PBT | 4,311 | 4,695 | 5,183 | 5,230 | 6,405 |
| Tax | 1,449 | 1,728 | 1,422 | 1,318 | 1,614 |
| PAT | 2,862 | 2,967 | 3,761 | 3,912 | 4,791 |

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Balance sheet

| Y/E March (Rsmn) | FY18 | FY19 | FY20 | FY21E | FY22E |
|------------------------------|----------------|----------------|----------------|----------------|----------------|
| Share capital | 266 | 266 | 266 | 282 | 282 |
| Reserves & surplus | 14,604 | 17,556 | 21,234 | 27,053 | 31,504 |
| Net worth | 14,870 | 17,822 | 21,501 | 27,335 | 31,786 |
| Borrowings | 139,210 | 166,944 | 187,484 | 187,859 | 205,142 |
| Other liability & provisions | 3,215 | 3,032 | 1,451 | 1,593 | 1,513 |
| Total liabilities | 157,295 | 187,798 | 210,436 | 216,787 | 238,442 |
| Fixed assets | 96 | 99 | 379 | 417 | 459 |
| Investments | 160 | 161 | 243 | 243 | 243 |
| Loans | 156,440 | 182,845 | 205,257 | 211,415 | 232,556 |
| Cash | 190 | 4,203 | 3,924 | 4,017 | 4,419 |
| Other assets | 409 | 491 | 633 | 696 | 765 |
| Total assets | 157,295 | 187,798 | 210,436 | 216,787 | 238,442 |

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Key ratios

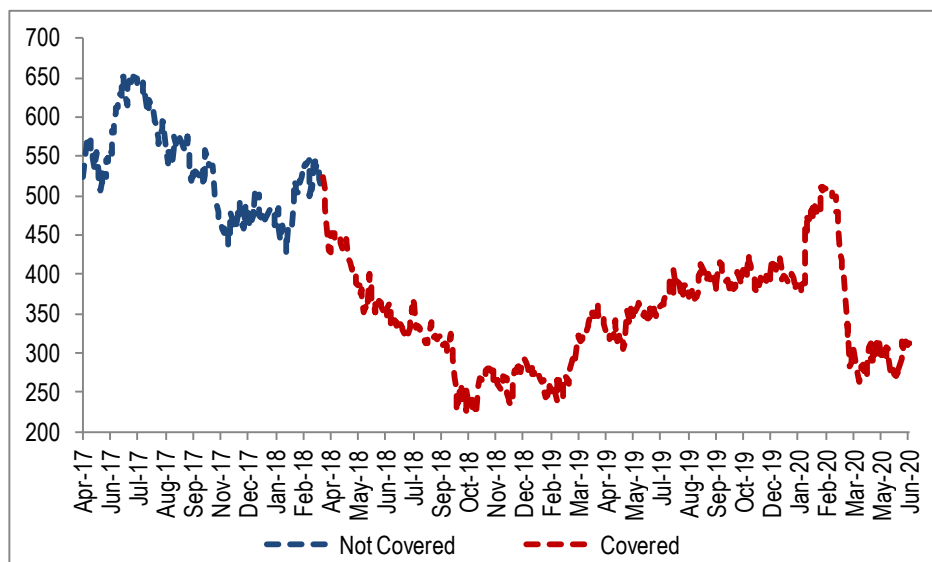
| Y/E March- Ratios | FY18 | FY19 | FY20 | FY21E | FY22E |
|-----------------------------------|-------|-------|-------|-------|-------|
| Growth (%) | | | | | |
| Net Interest Income | 20.8 | 4.1 | 27.2 | 7.4 | 8.6 |
| Operating Profit | 23.6 | 3.8 | 23.0 | 8.4 | 9.2 |
| Profit After Tax | 28.2 | 3.7 | 26.8 | 4.0 | 22.5 |
| Business (%) | | | | | |
| Advance Growth | 18.3 | 16.9 | 12.3 | 3.0 | 10.0 |
| Spreads (%) | | | | | |
| Yield on loans | 10.3 | 10.0 | 10.4 | 10.2 | 10.2 |
| Cost of Borrowings | 7.6 | 7.6 | 7.6 | 7.5 | 7.5 |
| Spread | 2.7 | 2.4 | 2.8 | 2.7 | 2.7 |
| NIMs | 3.5 | 3.1 | 3.5 | 3.5 | 3.5 |
| Operational Efficiency (%) | | | | | |
| Cost to Income | 16.2 | 16.3 | 15.7 | 15.9 | 15.4 |
| Cost to AUM | 0.6 | 0.5 | 0.6 | 0.6 | 0.6 |
| CRAR (%) | | | | | |
| Tier I | 17.0 | 14.6 | 20.5 | 23.3 | 22.8 |
| Tier II | 2.1 | 1.8 | 1.8 | 2.6 | 2.5 |
| Total | 19.1 | 16.4 | 22.3 | 25.8 | 25.3 |
| Asset Quality (%) | | | | | |
| Gross NPA | 0.4 | 0.6 | 0.8 | 1.1 | 0.9 |
| Net NPA | 0.2 | 0.5 | 0.5 | 0.7 | 0.6 |
| Provision Coverage | 56.0 | 27.5 | 28.8 | 35.0 | 35.0 |
| Credit Cost (excluding std asset) | 0.1 | 0.0 | 0.3 | 0.4 | 0.2 |
| Credit Cost (including std asset) | 0.2 | 0.0 | 0.3 | 0.5 | 0.2 |
| Return Ratio (%) | | | | | |
| ROE | 21.3 | 18.2 | 19.1 | 16.0 | 16.2 |
| ROA | 2.0 | 1.7 | 1.9 | 1.8 | 2.1 |
| Per Share (%) | | | | | |
| EPS | 21.5 | 22.3 | 28.2 | 27.7 | 34.0 |
| BV | 111.7 | 133.8 | 161.5 | 193.9 | 225.5 |
| ABV | 109.4 | 127.7 | 153.1 | 183.2 | 215.8 |
| Valuation (x) | | | | | |
| P/E | 15.5 | 14.9 | 11.8 | 12.0 | 9.8 |
| P/BV | 3.0 | 2.5 | 2.1 | 1.7 | 1.5 |
| P/ABV | 3.0 | 2.6 | 2.2 | 1.8 | 1.5 |

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

| Date | Rating | Market price (Rs) | Target price (Rs) |
|-----------------|--------|-------------------|-------------------|
| 26 March 2018 | Buy | 503 | 638 |
| 30 April 2018 | Buy | 421 | 513 |
| 31 July 2018 | Buy | 335 | 441 |
| 9 October 2018 | Buy | 225 | 321 |
| 23 October 2018 | Buy | 227 | 316 |
| 24 January 2019 | Buy | 255 | 355 |
| 8 April 2019 | Buy | 360 | 420 |
| 2 May 2019 | Buy | 343 | 422 |
| 8 July 2019 | Buy | 360 | 426 |
| 23 July 2019 | Buy | 405 | 472 |
| 7 October 2019 | Buy | 393 | 470 |
| 5 November 2019 | Buy | 416 | 486 |
| 8 January 2020 | Buy | 384 | 490 |
| 22 January 2020 | Buy | 464 | 540 |
| 27 March 2020 | Buy | 305 | 457 |
| 9 April 2020 | Buy | 283 | 457 |
| 18 June 2020 | Buy | 332 | 432 |

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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