

Can Fin Homes

2 May 2019

Reuters: CNFH.NS; Bloomberg: CANF IN

Multiple Levers To Aid NIM; Karnataka Turns Conducive

Can Fin Homes (CFHL) has reported its 4QFY19 results with the key pointers being: (1) Non metro push continues strong while conditions in Karnataka turn conducive (2) NIM has possibly bottomed out at 3.14% (-4 bps QoQ) with positive outlook given re-pricing and favorable funding (3) GNPA ratio was down 9 bps QoQ to 0.62% with scope for further improvement (4) Consolidation of metro operations would aid cost efficiencies (See *comprehensive* conference call takeaways on page 2 for *significant incremental colour*). Per se, on the key P&L items, CFHL posted 5% YoY NII growth at Rs1,377mn, PPOP growth of 5% YoY at Rs1,176mn and PAT decline of 9% YoY at Rs670mn. We have revised our estimates for FY20/FY21 and retained Buy rating on CFHL, revising our target price to Rs422 (from Rs420 earlier) and valuing the stock at 2.1x FY21E P/BV.

Non metro push continues strong while conditions in Karnataka turn conducive: As of FY19, CFHL has 62% of total branches in non-metro areas compared with 51% in FY16. The management's strategy to avoid the hyper competitive metros has helped deliver a loan book growth of 30% YoY in non-metros while growth in metros was 11% YoY. Overall, loan book growth was 16.7% for FY19. For FY20, CFHL has outlined a plan to open 20 more branches (11% of current branch network) in Tier II/III centres which should help sustain the growth momentum as well as protect NIM. Furthermore, CFHL stated its home-state of Karnataka has turned conducive, delivering an overall loan book growth of ~6.5% while sanctions in Q4FY19 are up 12% YoY on back of takeovers and balance transfers cooling down. Additionally, supply side constraints on the housing front have started receding as new projects have commenced. Considering that demand has not been an issue, broader underlying economic factors could turn supportive. Lastly, given CFHL's philosophy of lending only against evidence of formal income proof, expanding base of people filing ITRs provides an opportunity on the non-salaried front.

NIM has possibly bottomed out at 3.14% (-4 bps QoQ) with positive outlook given re-pricing and favorable funding: While yields have increasingly come under pressure primarily due to competition, stable cost of funds at 7.9% (+1 bps QoQ) have restricted margin compression. As stated earlier, CFHL's push into non metros where ticket sizes are lower would enable it to qualify for funding under NHB's Affordale Housing Fund wherein spreads are 300-350 bps. Further, as part of its annual rate reset regime introduced in April 2017, the company increased rates twice in FY19 (8.5% to 8.95% in April 2018, 8.95% to 9.5% in October 2018). Considering this, annual resetting of rates in the ensuing months could provide further fillip to NIM. Incremental cost of borrowings has been more or less unchanged on sequential basis.

GNPA ratio was down 9 bps QoQ to 0.62% with scope for further improvement: Absolute levels of GNPA's reduced to Rs1.15bn compared with Rs1.25bn as of Q3FY19. NNPA's also reduced by 8 bps QoQ to 0.43%. During the year, CFHL initiated SARFAESI in 367 accounts (Rs603.1mn) while the total stock of SARFAESI initiated accounts stands at 639 (Rs955.6mn). Recoveries through SARFAESI were Rs382.4mn (307 accounts) while leaving scope for more which should eventually lead to improvement in asset quality. Overall, current NPA levels are not too alarming.

Consolidation of metro operations would aid cost efficiencies: While new branches in non metros are being opened at minimum cost and are breaking even within a year, CFHL is simultaneously focusing on rationalizing metro branches. Opening of Central Processing Centres (CPC) is expected to consolidate operations in metros and help cut down costs. Post establishing two CPCs, Bangalore and Hyderabad, CFHL would be opening one each in Delhi and Chennai.

Valuation and outlook: We have revised our NII estimates by -4.7%/-2.0%, PPOP estimates by -7.9%/-7.0% and PAT estimates by -7.8%/-9.3% for FY20/FY21 respectively. We have retained Buy rating on CFHL, revising our target price to Rs422 (from Rs420 earlier) and valuing the stock at 2.1x FY21E P/BV.

BUY

Sector: NBFC

CMP: Rs343

Target Price: Rs422

Upside: 23%

Shivaji Thapliyal
 Research Analyst
 shivaji.thapliyal@nirmalbang.com
 +91-22-6273 8068

Raghav Garg
 Research Analyst
 raghav.garg@nirmalbang.com
 +91-22-6273 8192

Key Data

Current Shares O/S (mn)	133.2
Mkt Cap (Rsbn/US\$m)	45.6/657.3
52 Wk H / L (Rs)	429/217
Daily Vol. (3M NSE Avg.)	1,813,113

Price Performance (%)

	1 M	6 M	1 Yr
Can Fin Homes	(2.0)	24.8	(17.7)
Nifty Index	0.5	13.0	9.2

Source: Bloomberg

Y/E March (Rsmn)	4QFY19	4QFY18	3QFY19	YoY (%)	QoQ (%)
Interest income	4,514	3,863	4,376	16.8	3.1
Interest expenses	3,137	2,551	3,015	23.0	4.1
Net interest income	1,377	1,312	1,361	4.9	1.1
NIM (%)	3.14	3.53	3.18	-39bps	-4bps
Fee & other income	124	69	55	79.5	127.4
Total income	1,501	1,381	1,416	8.6	6.0
Total operating expenses	325	257	216	26.6	50.8
Cost to Income (%)	21.7	18.6	15.2	308bps	643bps
Cost to AUM (%)	0.7	0.7	0.5	5bps	22bps
Pre-provisioning Operating Profit	1,176	1,125	1,200	4.5	-2.0
Provisions	11	8	0	42.9	NA
Credit cost (%)	0.02	0.02	0.0	0bps	2bps
PBT	1,165	1,117	1,200	4.3	-2.9
Tax	495	378	451	31.0	9.8
-effective tax rate	42.5	33.8	37.6	865bps	491bps
PAT	670	739	749	-9.4	-10.6
Other comprehensive income	8	1	-16	641.9	-148.1
Total comprehensive income	678	740.3	733	-8.4	-7.6
EPS (Rs)	5.1	5.6	5.9	-8.4	-13.9
AUM	182,845	156,440	175,680	16.9	4.1

Source: Company, Nirmal Bang Institutional Equities Research

Comprehensive conference call takeaways

Asset Quality

- Of the Rs 1.13bn NPA book, SARFAESI has been initiated on Rs 9.56bn, of which Rs 6.03bn was done in FY19 alone.
- The company feels it was sub-optimal to expend effort beyond a point on collection from truant accounts and allowed them to fall into the NPA bucket so that SARFAESI could be initiated.
- The company stated that despite having relatively modest NPA provisioning, it has made provisions as per IRAC norms, which are in excess of ECL requirements.
- The company feels that, on a steady state basis, for an HFC like theirs, ECL provisioning requirement would be lower than that mandated by IRAC norms.

Business and Loan Growth

- The company stated that the loan book growth has been encouraging during the quarter as all new branches have started yielding results.
- Home state of Karnataka has also shown positive signs. Overall loan book growth for Karnataka was 6.5%. Excluding Karnataka, disbursements growth was 12.6% and loan book growth was 22%.
- New sanctions in Karnataka in Q4 are up 12% yoy which is encouraging. One of the reasons is that takeovers and transfers have cooled off compared to last year.
- 31% of the total book is still based out of Karnataka.
- Also, supply side issues in the housing segment have also started receding. The company stated that new projects have started post a lull after RERA implementation and that the stocks are getting ready which should help address supply going forward.
- Pace of housing loans has been much faster than non-housing loans. In last few quarters, growth in individual housing has been much faster and going forward, housing loan segment is expected to grow faster than non-housing segment.
- From new customer acquisition and growth perspective, the company stated that as the base of people filing ITRs increase, the opportunity size for the company would also increase since the company gives loans only to people with formal income proofs.
- Over the last few quarters, the quantum of non-salaried loans has continued to rise. This should translate into higher yields going forward.
- The company stated that Q1FY20 could be slightly dull on account of general elections while Q2FY20 will be impacted by monsoon, for housing loans. However, Q3 and Q4 are expected to see resumption of growth. Q1 and Q2FY20 could see higher growth non-housing loans.
- A typical customer profile for the company would be someone of 25-35 years of age, earning Rs. 50,000 a month, looking to loan Rs. 25 lacs and putting in his own equity of Rs 6-7 lacs.
- In FY20 and FY21, salaried segment is expected to play a bigger role as far as tier-2/3 cities are concerned.
- Post IL&FS and liquidity crisis, poaching and balance transfers by other institutions have reduced considerably.

Margin, Liabilities and Liquidity

- Margins during the quarter have been more or less held onto on QOQ basis on account of stable cost of funds. Yields have come under pressure over the last 12 months due to competition.
- The company stated that under its annual resetting regime, it increased rates from 8.5% in March 2018 to 8.95% in April 2018 and further to 9.5% in October 2018. Going forward, as rates on loans start getting reset, the company expects yields to improve.
- Any positive traction on NIMs due to increase in rates on account of resetting of rates would come with a lag.
- Funds borrowed under the NHB Affordable Housing Fund come at a lower cost. Though yields would also come down but spread of 300-350 bps would be guaranteed.
- The company stated it would be able to hold on to current levels in terms of cost of funds.
- Share of CP borrowings is 12% versus 15% last year.
- The company stated that the spreads could increase as loan book starts getting re-priced.
- The company stated it would try to hold onto margins of 300-350 bps.

Operating Expenses

- Company stated that its normalized tax rate would be 33-34%. There was a one-time tax impact during Q4 on account of tax liability from previous years.
- The company stated it is trying to operate new branches at the minimum cost and these are breaking even within 1 year. Branches in metros maybe rationalised. The company is in the process of opening Central Processing Centres (CPCs) which should help consolidated operations in the metros and cut down costs.

Fee and Other Income

- Under IND-AS, the total income has been impaired to the extent of processing fee that has been amortised over the life of loan. Average life of assets is 20 years, which means only 1/20th of the fee generated on loans has been recognized during the year. This is one of the major reasons that impacted return ratios and cost/income ratio.

Capital adequacy

- The company stated there are no plans of raising the debt/equity ratio any further. From present 9.37x, the company stated it would bring it down to ~7.5x post raising equity capital which is currently under discussion.
- The company stated it doesn't require growth capital at the moment. However, it is looking to raise equity capital in order to reduce its leverage which would help in securing favourable rates from the banks. The company may not go for a full Rs. 10 bn raise as stated earlier.
- The equity base during the quarter expanded on account of transfer of DTL to reserves, as part of transition towards IND-AS. Under the previous regime, the company would transfer 20% of PAT to special reserves on which it would avoid paying tax.

Other

- The search process for a new CEO is currently underway.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Net interest income	4,221	5,096	5,304	6,569	8,291
Pre-provisioning operating profit	3,884	4,532	4,706	5,955	7,623
PAT	2,347	2,862	2,967	3,511	4,494
EPS (Rs)	17.6	21.5	22.3	24.2	31.0
BV (Rs)	80.9	111.7	133.8	172.4	201.0
P/E (x)	19.4	16.0	15.4	14.2	11.1
P/BV (x)	4.2	3.1	2.6	2.0	1.7
Gross NPAs (%)	0.2	0.4	0.6	0.7	0.7
Net NPAs (%)	0.0	0.2	0.4	0.4	0.4
RoA (%)	1.9	2.0	1.7	1.7	1.8
RoE (%)	24.0	22.3	18.2	16.4	16.6

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Actual performance versus our estimates

(Rsmn)	4QFY19	4QFY18	3QFY19	YoY (%)	QoQ (%)	4QFY19E	Devi. (%)
Net interest income	1,377	1,312	1,361	4.9	1.1	1,490	(7.6)
Pre-provisioning Operating Profit	1,176	1,125	1,200	4.5	(2.0)	1,376	(14.6)
PAT	670	739	749	(9.4)	(10.6)	851	(21.3)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

	Revised estimate		Earlier estimate		% Revision	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net interest income (Rsmn)	6,569	8,291	6,890	8,463	(4.7)	(2.0)
NIM (%)	3.20	3.25	3.34	3.27	-14 bps	-2 bps
Operating profit (Rsmn)	5,955	7,623	6,462	8,200	(7.9)	(7.0)
Profit after tax (Rsmn)	3,511	4,494	3,808	4,957	(7.8)	(9.3)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Interest income	13,061	14,906	16,995	20,728	25,704
Interest expense	8,840	9,810	11,691	14,160	17,414
Net interest income	4,221	5,096	5,304	6,569	8,291
Non-interest income	471	314	318	455	567
Net revenues	4,691	5,410	5,622	7,024	8,857
Operating expenses	807	878	916	1,069	1,234
-Employee expenses	394	448	414	491	569
-Other expenses	414	430	503	578	665
Pre-provisioning Operating Profit	3,884	4,532	4,706	5,955	7,623
Provisions	188	221	11	468	601
PBT	3,696	4,311	4,695	5,486	7,023
Tax	1,349	1,449	1,728	1,975	2,528
PAT	2,347	2,862	2,967	3,511	4,494

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Share capital	266	266	266	290	290
Reserves & surplus	10,497	14,604	17,556	24,694	28,840
Net worth	10,763	14,870	17,822	24,984	29,130
Borrowings	111,094	136,927	164,333	194,140	241,203
Other liability & provisions	12,719	5,498	5,643	9,623	14,292
Total liabilities	134,576	157,295	187,798	228,748	284,625
Fixed assets	102	96	99	108	119
Investments	159	160	161	161	161
Loans	132,905	156,440	182,845	227,572	283,270
Cash	125	190	4,203	341	425
Other assets	1,285	409	491	565	650
Total assets	134,576	157,295	187,798	228,748	284,625

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Key ratios

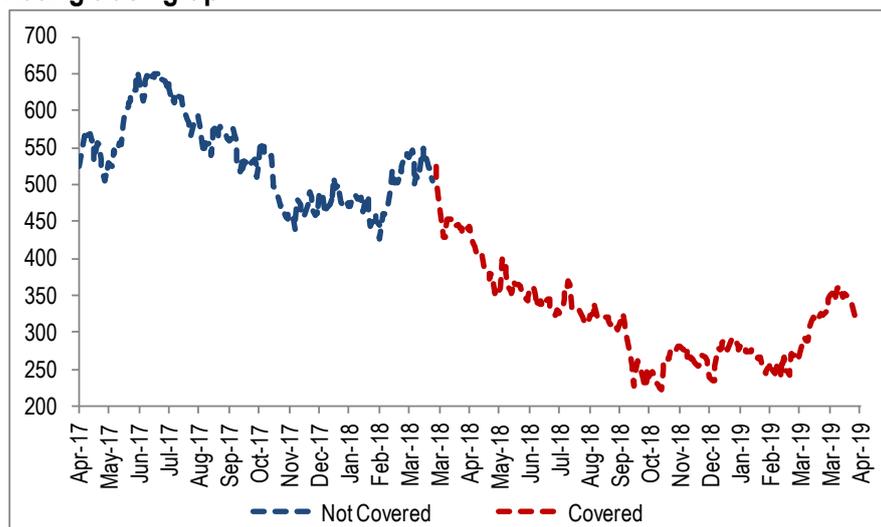
Y/E March	FY17	FY18	FY19	FY20E	FY21E
Growth (%)					
Net interest income	40.3	20.8	4.1	23.8	26.2
Operating profit	42.2	23.6	3.8	26.5	28.0
Profit after tax	49.4	28.6	3.7	18.3	28.0
Business (%)					
Advances growth	23.6	18.2	16.9	24.5	24.5
Spread (%)					
Yield on loans	10.9	10.3	10.0	10.1	10.1
Cost of borrowings	9.0	8.5	7.8	7.9	8.0
Spread	1.9	1.8	2.3	2.2	2.1
NIM	3.5	3.5	3.1	3.2	3.2
Operational efficiency (%)					
Cost- to-income	17.2	15.2	16.3	15.2	13.9
Cost-to-AUM	0.7	0.6	0.5	0.5	0.5
Productivity (Rsmn)					
Loan per branch	781.8	908.2	967.4	1,000.0	1,150.0
Loan per employee	212.3	242.5	284.5	294.1	328.6
Employee per branch	3.7	3.7	3.4	3.4	3.5
CRAR (%)					
Tier I	16.0	17.0	17.8	19.3	18.0
Tier II	2.5	2.1	1.8	2.1	2.0
Total	18.5	19.1	19.6	21.4	20.0
Asset quality (%)					
Gross NPAs	0.2	0.4	0.6	0.7	0.7
Net NPAs	0.0	0.2	0.4	0.4	0.4
Specific Provision coverage	100.0	53.2	30.0	50.0	50.0
Credit cost (excluding std. asset)	0.2	0.3	0.0	0.2	0.1
Credit cost (including std. asset)	0.2	0.4	0.0	0.2	0.2
Return ratios (%)					
RoE	24.0	24.9	18.2	16.4	16.6
RoA	1.9	2.1	1.7	1.7	1.8
Per share (%)					
EPS	17.6	22.7	22.3	24.2	31.0
BV	80.9	101.1	133.8	172.4	201.0
ABV	80.9	98.7	127.9	166.9	194.2
Valuation (x)					
P/E	19.4	15.1	15.4	14.2	11.1
P/BV	4.2	3.4	2.6	2.0	1.7
P/ABV	4.2	3.5	2.7	2.1	1.8

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

Rating track graph



DISCLOSURES

This Report is published by Nirmal Bang Equities Private Limited (hereinafter referred to as “NBEPL”) for private circulation. NBEPL is a registered Research Analyst under SEBI (Research Analyst) Regulations, 2014 having Registration no. INH000001436. NBEPL is also a registered Stock Broker with National Stock Exchange of India Limited and BSE Limited in cash and derivatives segments.

NBEPL has other business divisions with independent research teams separated by Chinese walls, and therefore may, at times, have different or contrary views on stocks and markets.

NBEPL or its associates have not been debarred / suspended by SEBI or any other regulatory authority for accessing / dealing in securities Market. NBEPL, its associates or analyst or his relatives do not hold any financial interest in the subject company. NBEPL or its associates or Analyst do not have any conflict or material conflict of interest at the time of publication of the research report with the subject company. NBEPL or its associates or Analyst or his relatives do not hold beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of this research report.

NBEPL or its associates / analyst has not received any compensation / managed or co-managed public offering of securities of the company covered by Analyst during the past twelve months. NBEPL or its associates have not received any compensation or other benefits from the company covered by Analyst or third party in connection with the research report. Analyst has not served as an officer, director or employee of Subject Company and NBEPL / analyst has not been engaged in market making activity of the subject company.

Analyst Certification: We, Shivaji Thapliyal and Raghav Garg, research analysts and the authors of this report, hereby certify that the views expressed in this research report accurately reflect our personal views about the subject securities, issuers, products, sectors or industries. It is also certified that no part of the compensation of the analysts was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research. The analysts are principally responsible for the preparation of this research report and have taken reasonable care to achieve and maintain independence and objectivity in making any recommendations.

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

This report is for the personal information of the authorized recipient and does not constitute to be any investment, legal or taxation advice to you. NBEPL is not soliciting any action based upon it. Nothing in this research shall be construed as a solicitation to buy or sell any security or product, or to engage in or refrain from engaging in any such transaction. In preparing this research, we did not take into account the investment objectives, financial situation and particular needs of the reader.

This research has been prepared for the general use of the clients of NBEPL and must not be copied, either in whole or in part, or distributed or redistributed to any other person in any form. If you are not the intended recipient you must not use or disclose the information in this research in any way. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. NBEPL will not treat recipients as customers by virtue of their receiving this report. This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject NBEPL & its group companies to registration or licensing requirements within such jurisdictions.

The report is based on the information obtained from sources believed to be reliable, but we do not make any representation or warranty that it is accurate, complete or up-to-date and it should not be relied upon as such. We accept no obligation to correct or update the information or opinions in it. NBEPL or any of its affiliates or employees shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. NBEPL or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This information is subject to change without any prior notice. NBEPL reserves its absolute discretion and right to make or refrain from making modifications and alterations to this statement from time to time. Nevertheless, NBEPL is committed to providing independent and transparent recommendations to its clients, and would be happy to provide information in response to specific client queries.

Before making an investment decision on the basis of this research, the reader needs to consider, with or without the assistance of an adviser, whether the advice is appropriate in light of their particular investment needs, objectives and financial circumstances. There are risks involved in securities trading. The price of securities can and does fluctuate, and an individual security may even become valueless. International investors are reminded of the additional risks inherent in international investments, such as currency fluctuations and international stock market or economic conditions, which may adversely affect the value of the investment. Opinions expressed are subject to change without any notice. Neither the company nor the director or the employees of NBEPL accept any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of this research and/or further communication in relation to this research. Here it may be noted that neither NBEPL, nor its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profit that may arise from or in connection with the use of the information contained in this report.

Copyright of this document vests exclusively with NBEPL.

Our reports are also available on our website www.nirmalbang.com

Access all our reports on Bloomberg, Thomson Reuters and Factset.

Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 6273 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 6273 8230, +91 22 6636 8833
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 6273 8100/8101, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 6273 8102/8103, +91 22 6636 8830

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address

B-2, 301/302, Marathon Innova,
 Nr. Peninsula Corporate Park,
 Lower Parel (W), Mumbai-400013.

Board No. : 91 22 6273 8000/1; Fax. : 022 6273 8010