

LIC Housing Finance (LICHF IN)

Target Price **Rs525.0**
 Current Price **Rs550.5**
 % Downside **5%**

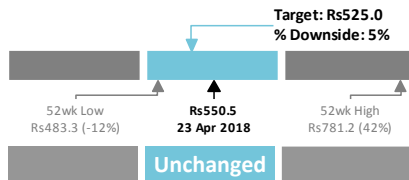
The Scoop: Pressure on NIM Continues

Diversified Financials

India

24 Apr 2018

NEUTRAL



Basic Share Information

Market cap	Rs277.8b / US\$4.18b
Daily traded value (3mth)	US\$14.45m
Shares outstanding	504.7m
Free float	60%
Foreign Shareholding	34%
1 yr high	Rs781.2
1 yr low	Rs483.3
Share price date	23 Apr 18

Price/Volume



Source: Bloomberg

	1mth	3mth	12mth
Absolute	5.9%	-4%	-14.5%
Absolute USD	3.6%	-7.9%	-16.9%
Relative to SENSEX	0.2%	0.7%	-31.8%

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What event has happened?

LIC Housing Finance reported its Q4 FY3/18 results on 23 April 2018. Net interest margin (NIM) for the company fell to 2.49% in the quarter (compared to 2.97% in Q4 FY3/17) despite the fact that the composition of loan against property (LAP) and corporate loans increased to 19.2% of its total loan book. Hence, despite the company reporting almost 15% YoY growth in AUM, the net interest income declined by 3% YoY for Q4 FY3/18. Also, the gross non-performing asset (GNPA) ended at 0.78% as of March 2018 (compared to 0.43% as of March 2017). As a result, the company's NP grew by 2% YoY in Q4 FY3/18 and was lower than our forecast for the quarter.

Why is it significant?

With 10-year government bond yields rising (around 130bps up in the last nine months), the new non-convertible debenture (NCD) borrowing rates have started moving up. Hence, LIC Housing's NIMs are unlikely to improve in the next year, in our view. The company has already reported that Q4 FY3/18 borrowing cost is 7.76% and that the incremental spread for the full year was at 2.25%, which is significantly lower than the incremental spread of 2.44% seen until Q3 FY3/18. Moreover, with increasing GNPA owing to increasing exposure to the high-risk developer segment, credit costs are likely to remain elevated.

Implications for our earnings forecast?

We change our NIM forecast to 2.25% for FY3/19E and FY3/20E, from 2.30% previously. This leads to NP reduction of around 2% each for FY3/19 and FY3/20, and results in a reduced target price of Rs525 (from Rs536 previously). Our target price is based on a discounted cash flow (DCF) analysis.

How do valuations look now?

LIC Housing currently trades at 1.9x FY3/19 PBR, much higher than its historical five-year average of 1.8x. We do not see any catalysts for the stock to move up, and maintain our NEUTRAL rating, given the stock price correction (stock is down by around 14% versus SENSEX up around 17% in the last 12 months) and no upside to our target price. The main upside risk to our rating and target price would be a scenario where non-convertible debenture (NCD) rates start falling again. The main downside risk is the scenario where the 10-year government bond yield continues to surge further upwards, which would then lead to higher cost of NCD borrowings for LIC Housing.

What is distinctive about our stock view?

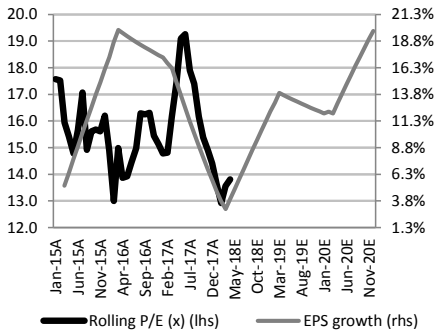
We have an out-of-consensus NEUTRAL recommendation on the stock based on our view that the company's NIMs would struggle to increase given the rise in bond yields.

	Mar-16A	Mar-17A	Mar-18A	Mar-19E	Mar-20E	Trend
Net interest income (Rsm)	29,441	36,452	37,013	41,597	46,818	▬ ▬ ▬ ▬ ▬
Pre-provisional operating profit (Rsm)	27,104	32,371	33,007	36,685	40,979	▬ ▬ ▬ ▬ ▬
Pre-tax profit (Rsm)	25,639	29,558	30,619	34,696	38,860	▬ ▬ ▬ ▬ ▬
Net income to ord equity (Rsm)	16,612	19,311	19,896	22,667	25,388	▬ ▬ ▬ ▬ ▬
Net profit growth	19.8%	16.2%	3.0%	13.9%	12.0%	▬ ▬ ▬ ▬ ▬
P/E (x)	16.73	14.39	13.97	12.26	10.95	▬ ▬ ▬ ▬ ▬
P/B (x)	3.04	2.51	2.19	1.91	1.68	▬ ▬ ▬ ▬ ▬
ROE	19.6%	19.1%	16.7%	16.7%	16.3%	▬ ▬ ▬ ▬ ▬
Dividend yield	1.2%	1.4%	1.4%	1.6%	1.8%	▬ ▬ ▬ ▬ ▬
EPS HTI old (Rs)	32.90	38.24	40.81	45.82	51.38	▬ ▬ ▬ ▬ ▬
EPS HTI New (Rs)	32.90	38.24	39.40	44.89	50.28	▬ ▬ ▬ ▬ ▬
Consensus EPS (Rs)		40.23	39.74	46.45	55.12	▬ ▬ ▬ ▬ ▬
HTI EPS vs Consensus	na	(4.9%)	(0.9%)	(3.4%)	(8.8%)	▬ ▬ ▬ ▬ ▬

Source: Company data, Bloomberg, HTI estimates

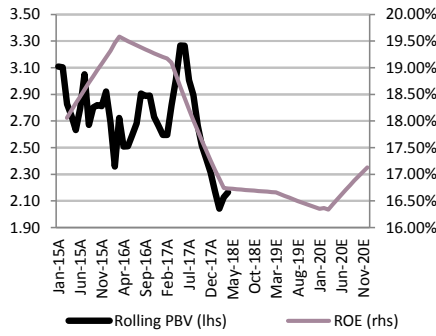
Click [here](#) to download the working model

P/E (x) vs EPS Growth (%)



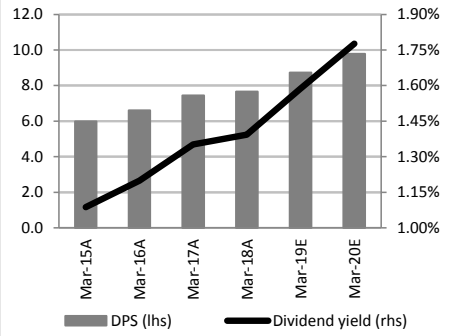
Source: Company data, Bloomberg, HTI estimates

P/B (x) vs ROE



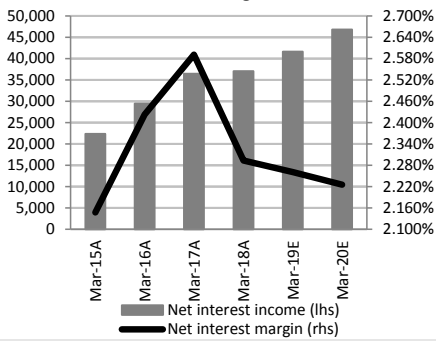
Source: Company data, Bloomberg, HTI estimates

Dividend Payout and Yield



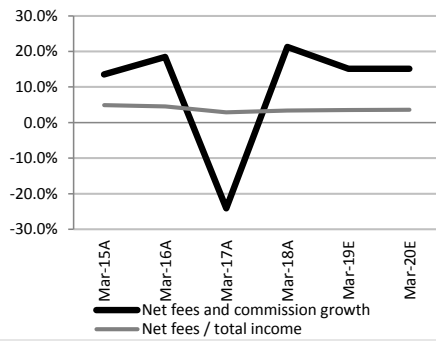
Source: Company data, Bloomberg, HTI estimates

Net Interest Income and Margin



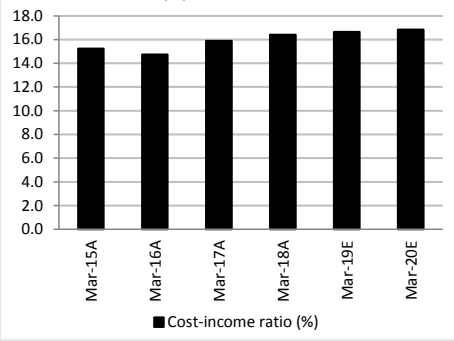
Source: Company data, Bloomberg, HTI estimates

Fees Income Growth vs Contribution



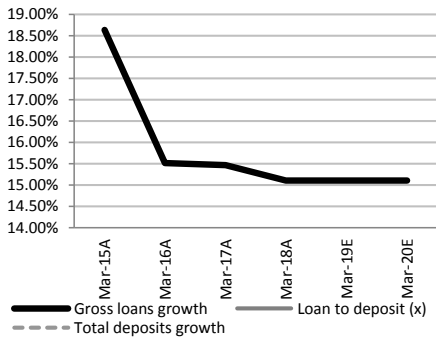
Source: Company data, Bloomberg, HTI estimates

Cost-income ratio (%)



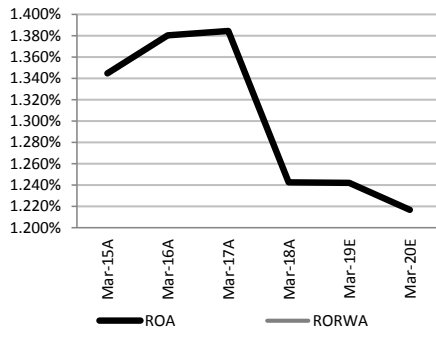
Source: Company data, Bloomberg, HTI estimates

Loan and Deposit Growth and LDR



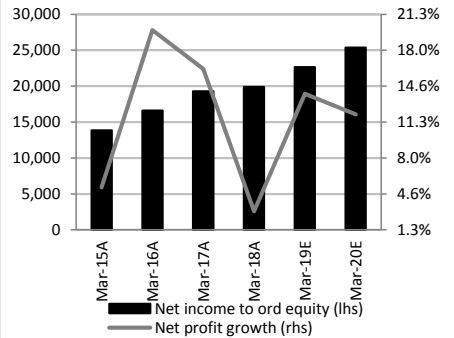
Source: Company data, Bloomberg, HTI estimates

ROA vs RORWA



Source: Company data, Bloomberg, HTI estimates

Net Income To Ord Equity and Growth (Rsm)



Source: Company data, Bloomberg, HTI estimates

APPENDIX

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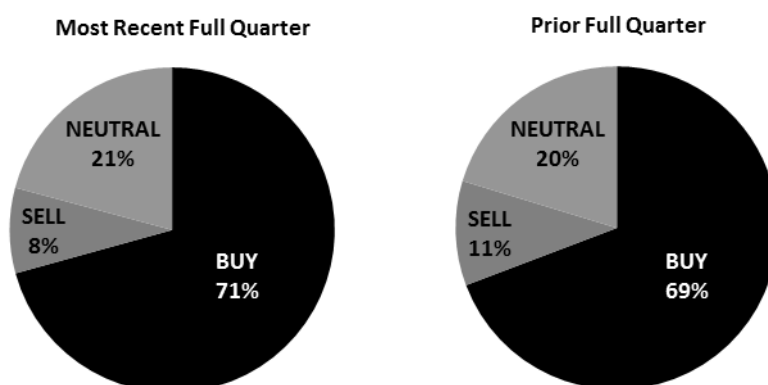
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Recommendation Chart



Date	Recommendation	Target (Rs)	Price (Rs)
2018-02-14	Neutral	536.0	525.1
2017-07-01	Sell	494.0	742.2
2017-01-23	Sell	433.8	525.7

Source: Company data Bloomberg, HTI estimates

Definitions for Key Investment Metrics

Business Growth

This is the metric which matches the top line in our report.

Business profit

This is the metric which best represents operating profit in our report

Shareholder Returns

Return on Equity

Balance Sheet Risk

Net Debt to Equity