

Dewan Housing Finance Ltd

Industry	CMP	Recommendation	Add on Dips to band	Sequential Targets	Time Horizon
BFSI	Rs. 438	Buy at CMP and add on dips	Rs. 392-400	Rs. 516 & Rs. 578	2-3 quarters

HDFC Scrip Code	DEWHOUQNR
BSE Code	511072
NSE Code	DHFL
Bloomberg	DEWH IN
CMP as on 04 May 17	438.00
Eq. Capital (Rs crs)	313.15
Face Value (Rs)	10.0
Equity Sh. Outs (Cr)	31.3
Market Cap (Rs crs)	13716
Book Value	255.3
Avg. 52 Week Vol	27,82,000
52 Week High	455.20
52 Week Low	182.70

Shareholding Pattern-% (Mar-2017)	
Promoters	39.29
Institutions	32.50
Non Institutions	28.21
Total	100.00

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We had issued a Stock Note report on Oct 19, 2016 with a recommendation to buy at CMP and add the stock in the price band of Rs. 281-292 for sequential targets of Rs. 387 and Rs. 428 in 2-3 quarters. The stock achieved both the targets on 6th Apr and 25th Apr 2016 respectively and later made a high of Rs. 455 on 3rd May 2017. Refer: http://hdfcsec.com/Research/ResearchDetails.aspx?report_id=3019606. We now review the latest developments in the company and provide our updated view on the stock.

Company Description:

Dewan Housing Finance Ltd. (DHFL) was established in 1984 by Late Shri Rajesh Kumar Wadhawan to enable access to affordable housing finance to the lower and middle income groups in semi-urban and rural parts of India. Since its inception the company has grown stronger and has become the second largest housing finance company in the private sector. DHFL has an extensive network of 352 offices and an outstanding loan book of Rs 738 bn at the end of FY17. It also has tie-ups with leading private sector banks namely United Bank of India, Dhanlaxmi Bank and YES bank to provide home loans to customers sourced by them through a home loan syndication agreement. DHFL has also set up representative offices in London and Dubai to serve the ever increasing NRI population in these regions.

Investment Rationale

- Strong results despite lower disbursements growth in Q4/H2FY17
- Sale proceeds of stake in Insurance company received; CAR strengthens
- Other investments awaiting unlocking of value
- Significant reduction in CoF leading to steady NIMs

Concerns

- Slowdown in real estate sector
- Regulatory changes
- Rising competition from banks and peer companies
- Asset quality might worsen as lending to projects and LAP/SME book rises

Financial Summary

Rs in Cr	Q4FY17	Q4FY16	YoY (%)	Q3FY17	QoQ (%)	FY16	FY17	FY18E	FY19E
NII	536	486	10.3	516	3.9	1669	2000	2398	3022
PPP	459	333	37.9	417	10.1	1277	1621	1979	2506
PAT	249	190	31.3	245	1.5	729	928	1129	1430
EPS (Rs)	8.0	6.5	22.3	7.8	1.5	25.0	29.6	36.1	45.7

P/E (x)						17.5	14.8	12.1	9.6
P/ABV (x)						2.7	1.8	1.6	1.4
RoAA (%)						1.2	1.2	1.2	1.3

(Source: Company, HDFC sec)

View and Valuation

DHFL, with its expertise in lending to the lower/middle income group in Tier II and Tier III cities while maintaining strong asset quality would be a key beneficiary of the government's thrust on promoting affordable housing. Management's commitment to lower funding cost along with a higher proportion of non-housing loans should result in net interest margin expansion for the company. DHFL trades at a significant discount (as per street estimates) to other HFC like Indiabulls Housing Finance (quoting at 2.6x FY19E ABV) and Canfin Home Finance (quoting at 4.7x FY19E ABV) and given the strong growth trajectory this gap is likely to come down. The company has sold its stake in life insurance business resulting in a 33% jump in its networth. While monetization of stake in other associate companies could result in significant value unlocking we have valued the company on a standalone basis and have not attributed any value to the subsidiaries/associates.

We feel investors could buy the stock at the CMP and add on declines to Rs. 392-400 band (~1.3x FY19E ABV) for sequential targets of Rs. 516 (1.7x FY19E ABV) and Rs. 578 (1.9x FY19E ABV) in 2-3 quarters.

Investment Rationale

Strong results despite lower disbursements in Q4/H2FY17

DHFL reported a PAT of Rs 2218 cr in Q4FY17 which included exceptional profit of Rs 1969 cr from sale of its 50% stake in DHFL Pramerica Life Insurance (DPLI) to its wholly owned subsidiary. Excluding the exceptional gains PAT grew by 31% yoy to Rs 249 cr. Net interest income grew by 10% yoy as interest expenses grew faster than interest income resulting in 3 bps compression in NIMs to 3.04%. Disbursements continued to be impacted by the demonetization as the growth remained at a subdued 11% yoy (H2FY17 growth ~11%) as compared to 29% growth in H1FY17. AUM was up 20% yoy to Rs 83560 cr driven by higher growth in non-home loans which now constitute 34.2% of AUMs against 31.1% at the end of Q3FY17. Asset quality was stable with GNPA at 0.94%. The company utilized gains from non-interest income to make prudent provisions.

Particulars	Q4FY17	Q4FY16	YoY (%)	Q3FY17	QoQ (%)	FY17	FY16	YoY (%)
Interest Income	2283	1964	16.2	2316	-1.4	8654	7246	19.4
Interest Expenses	1747	1479	18.2	1800	-3.0	6653	5490	21.2
Net Interest Income	536	486	10.3	516	3.9	2000	1756	13.9
Non-interest income	95	45	111.0	51	86.3	219	71	208.9
Total Income	631	488	29.3	567	11.3	2219	1827	21.5
Operating Expenses	172	155	10.8	150	14.7	597	598	0.0
Pre Prov. Profit	459	333	37.9	417	10.1	1622	1229	31.9
Prov. & Cont.	83	50	66.0	45	84.4	218	127	71.7

PBT	376	283	33.0	372	1.1	1404	1102	27.3
Tax	127	93	36.3	127	0.3	475	373	27.4
PAT	249	190	31.3	245	1.5	928	729	27.3
EPS	8.0	6.5	22.3	7.8	1.5	29.6	25.0	18.6

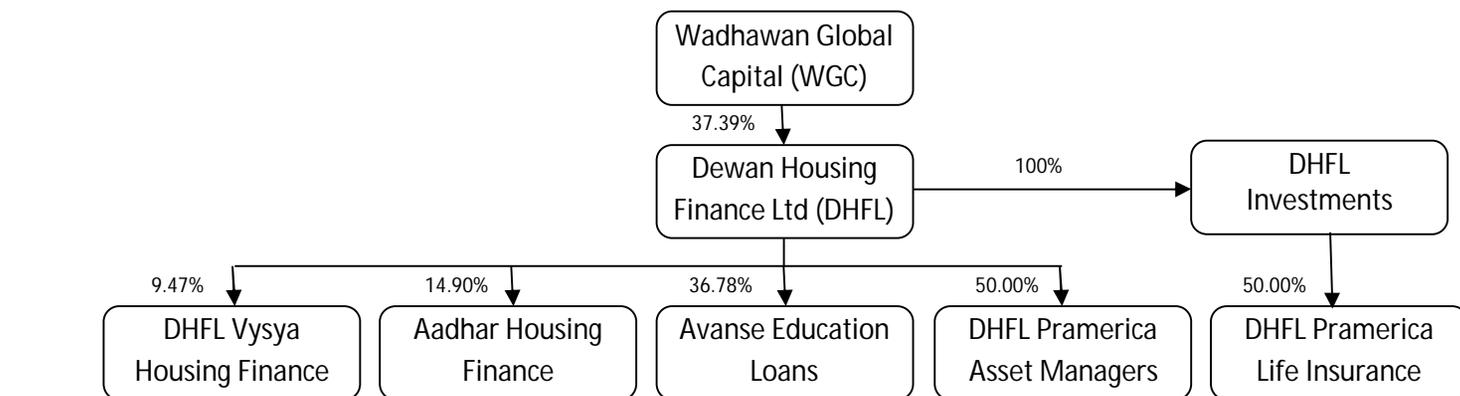
Sales proceeds of stake in Insurance JV received; CAR strengthens

DHFL sold its 50% stake in DPLI (DHFL Pramerica Life Insurance) (out of 51% held) to its wholly owned subsidiary DHFL Investments (DIL) for a consideration of Rs 2000.5 cr. The book value of the stake stood at Rs 31.1 cr resulting in profit of Rs 1969.4 cr which was booked during the quarter. DIL would fund the transaction by issuing Compulsorily Convertible Debentures (CCD) worth Rs 1901 cr to DHFL’s promoters. The transaction has added Rs 62.9 per share to DHFL’s networth while CRAR has strengthened by ~400 bps. This would be sufficient to drive the company’s business for the next 2-3 years without any further dilution.

Other investments awaiting unlocking of value

DHFL has other minority investments in DHFL Vysya Housing Finance (9.47%), Aadhar Housing Finance (14.90%), Avanse Education Loans (36.78%) and DHFL Pramerica Asset Management (50%). All these companies have witnessed substantial growth over the past year. These investments can result in significant value unlocking whenever the company decides to monetize them.

Corporate Structure



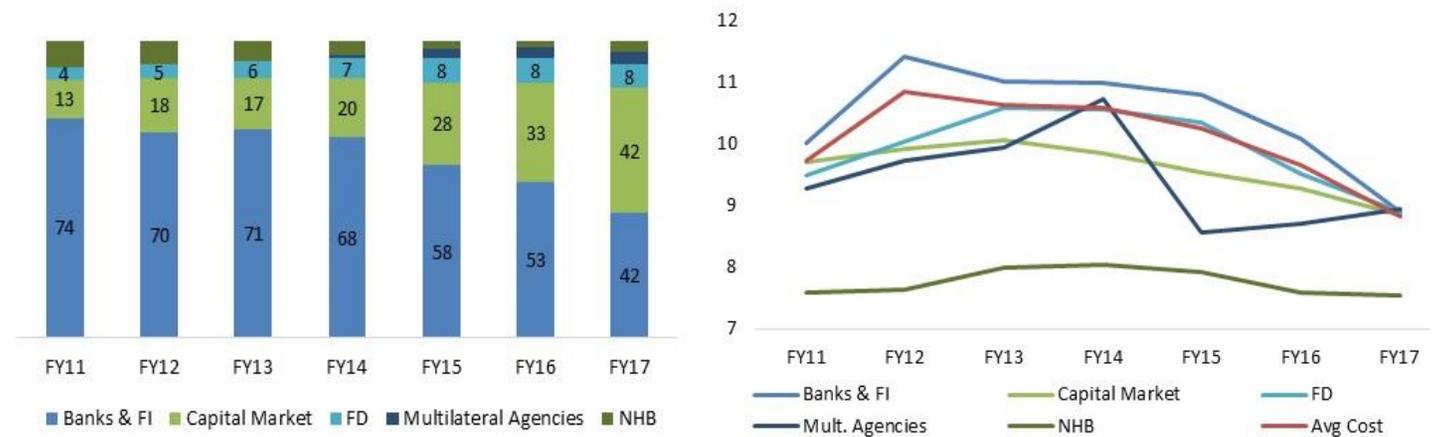
(Source: Company, HDFC sec)

Company	FY17 Performance
DHFL Vysya Housing Finance	Disbursements increased by 46% to Rs 646 cr, AUM were up 23% to Rs 1808 cr
Aadhar Housing Finance	Disbursements increased by 68% to Rs 1696 cr, AUM were up 76% to Rs 3184 cr
Avanse Education Loans	Disbursements increased by 70% to Rs 584 cr, AUM were up 85% to Rs 982 cr
DHFL Pramerica Asset Management	AUM were up 37% to Rs 28224 cr

Significant reduction in CoF...

DHFL has re-negotiated its bank loans in FY17 bringing down its cost of bank borrowings by 119 bps to 8.91%. Further share of NCDs in total borrowings has increased from 33% in FY16 to 42% in FY17. Overall cost of funds decreased by 84 bps in FY17 enabling the company to offer loans at competitive rates without impacting its NIMs. The company is seeking shareholder approval to raise upto Rs 20,000 cr through debentures in FY18 which should result in further decline in cost of funds.

Capital market borrowing increased in funding mix leading to lower cost of funds (%)



(Source: Company, HDFC sec)

...leading to steady NIMs

Reported NIMs were steady at 3.04% in Q4FY17 and 2.99% for the entire year against 2.90% in Q4FY16 and 2.96% for FY16. The improvement was largely driven by re-negotiation of bank loans to a lower rate and higher share of borrowing from debt capital markets. Decreased cost of funds was offset by decline in yields on back of falling interest rates. Margins of the company have stayed at ~3% levels historically and the management has guided for similar range going forward.

Sharp improvement in cost/income ratio

Cost-income has always been higher as compared to peers and a cause of concern for the company. DHFL has been reducing its Cost/Income Ratio through focus on efficiency improvement and technology led initiatives. Calculated cost-

income ratio improved by 360 bps in FY17 to 26.5% as compared to 30.1% in FY16. While the last 3 years have witnessed a steady improvement, sustenance of the same would be important going forward.

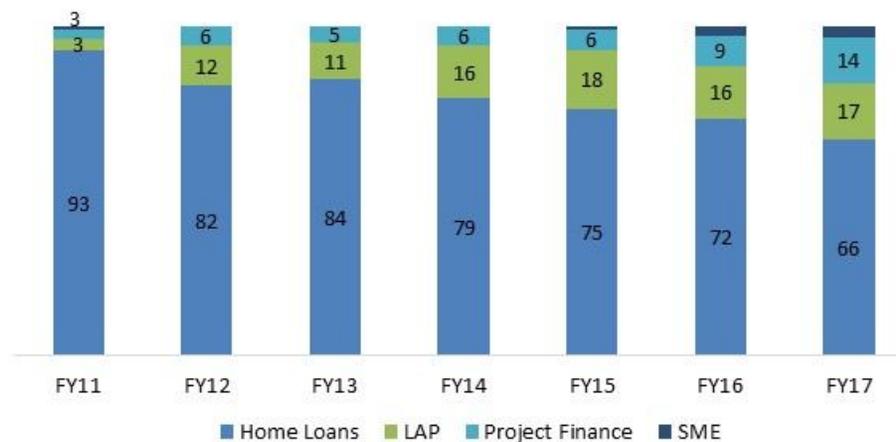
Stable asset quality

Despite of demonetization asset quality (GNPA) of DHFL has remained fairly stable at <1% due to the robust credit appraisal process followed by the company. GNPA in Q4FY17 came in at 0.94% compared to 0.95% in Q3FY17. Lower dependence on intermediaries and lower LTV ratios provide comfort on the asset quality front. However, increasing project/construction finance loans and LAP/SME loans can be a cause of concern going forward.

AUM growth driven by non-housing loans

Post demonetization, though we have witnessed some traction in disbursements sequentially, it continues to remain subdued as compared to the high growth seen in H1FY17. Disbursements grew 23% qoq/11% yoy largely driven by non-housing loans. Housing loans AUM were up 2% qoq/9.4% yoy as compared to 17.3% qoq/48.4% yoy growth in non-housing loans. Average ticket size increased by 12.9% in FY17 to Rs 14 lakhs. Project finance now constitutes 14% of AUM with management earlier stating a higher proportion at 15%, which is a key monitorable. Share of LAP loans increased to 16.9% at the end of FY17 against 15.7% in FY16.

Increasing share of non-housing loans (%)



(Source: Company, HDFC sec)

Concerns

Slowdown in real estate sector

Over the last 2-3 years, housing sector has seen an inventory pile up situation in India and launching of new projects has come down in the past two years. A number of houses, flats and apartments are being sold without getting booked. However, slowdown in loan demand has been reported in the high end segments, which are driven by investment demand.

Regulatory changes

Regulatory changes like increase in risk weights for a certain category, cap on interest rates under refinance could mar the growth and profitability of the company.

Rising competition from banks and peer companies

There is strong competition from banks and peer companies in the housing finance industry as it is considered relatively lower risk loan. Higher competition might result in lower yields going forward. This also means that the monies raised by DHFL by way of NCDs in early FY17 will sit on its books as current Investments till it is profitably deployed, impacting its spread/NIMs in the meanwhile.

Asset quality might worsen

Although the asset quality has largely remained stable, high proportion of LAP loans to self-employed category where income is volatile could result in defaults leading to higher provisioning requirements. The company has also increased project finance loans which could turn into NPAs in the event of slowdown.

Unclear terms about sale of stake in Insurance JV

DHFL Investments will issue compulsorily convertible debentures (CCDs) to Wadhawan Global Capital Pvt. Ltd, with a conversion period of 100 months. Wadhawan Global is the promoter entity of DHFL. DHFL will continue to have an option in it which may result in the housing financier owning DHFL Pramerica Life Insurance once again. Once the conversion period on the CCDs ends, Wadhawan Global would own more than 50% in DHFL Investments and would thus end up controlling the insurance company as well. There is uncertainty on the terms of CCD issue, interest rate on CCD, conversion price, stake in DHFL Investments to be acquired in future by Wadhawan Global, terms of option exercise by DHFL etc.

View and Valuation

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Financial Statements (Standalone)
Income Statement

Particulars	FY15	FY16	FY17	FY18E	FY19E
Interest Income	5716	7159	8654	10194	11934
Interest Expenses	4460	5490	6654	7796	8912
Net Interest Income	1256	1669	2000	2398	3022
Non interest income	142	158	204	268	291
Operating Income	1399	1827	2204	2666	3313
Operating Expenses	474	550	583	687	807
PPP	925	1277	1621	1979	2506
Prov & Cont	105	175	218	268	340
Profit Before Tax	820	1102	1403	1711	2167
Tax	322	373	475	582	737
PAT	498	729	928	1129	1430

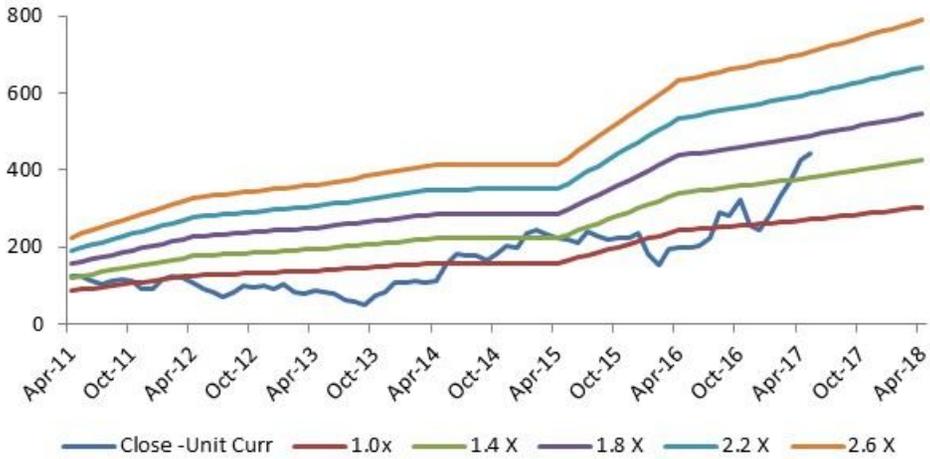
Balance Sheet

Particulars	FY15	FY16	FY17	FY18E	FY19E
Share Capital	146	292	313	313	313
Reserves & Surplus	4490	4725	7683	8605	9772
Shareholder funds	4636	5017	7996	8918	10085
Borrowings	46848	58781	77799	84608	101056
Other Liab & Prov.	3131	4055	6503	5970	7094
SOURCES OF FUNDS	54615	67853	92298	99496	118235
Fixed Assets	188	202	209	214	217
CWIP	796	579	634	634	634
Investment	1006	893	13535	7532	8963
Cash & Bank Balance	676	3408	3430	1772	2109
Advances	51511	62295	73840	88608	105443
Other Assets	437	476	651	736	870
TOTAL ASSETS	54615	67853	92298	99496	118235

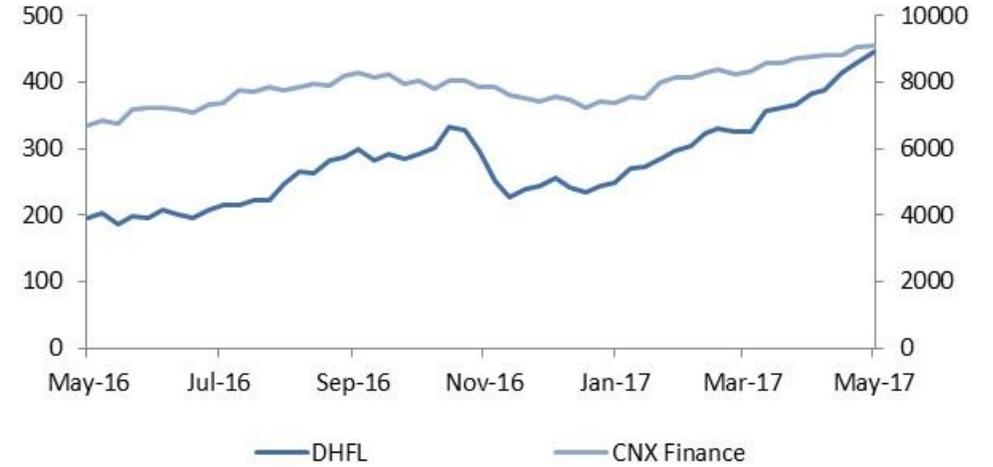
Ratio Analysis

Particulars	FY15	FY16	FY17	FY18E	FY19E
Return Ratios					
Calc. Yield on adv	12.4%	12.6%	12.7%	12.6%	12.3%
Calc. Cost of borr	10.5%	10.4%	9.7%	9.6%	9.6%
NIM	2.7%	2.9%	2.9%	3.0%	3.1%
RoAE	12.1%	15.1%	14.3%	13.4%	15.0%
RoAA	1.0%	1.2%	1.2%	1.2%	1.3%
Asset Quality Ratios					
GNPA	1.0%	0.9%	0.9%	1.0%	1.0%
NNPA	0.7%	0.6%	0.5%	0.5%	0.5%
Growth Ratios					
Advances	25.6%	20.9%	18.5%	20.0%	19.0%
Borrowings	22.2%	25.5%	32.4%	8.8%	19.4%
NII	81.0%	32.8%	19.8%	19.9%	26.0%
PPP	82.9%	38.1%	26.9%	22.1%	26.7%
PAT	117.0%	46.5%	27.2%	21.7%	26.6%
Valuation Ratios					
EPS	17.1	25.0	29.6	36.1	45.7
P/E	25.6	17.5	14.8	12.1	9.6
Adj. BVPS	159.1	159.6	243.0	269.6	303.7
P/ABV	2.8	2.5	1.7	1.5	1.4
Dividend per share	6.0	8.0	4.0	5.5	7.0
Dividend Yield (%)	1.4	1.8	0.9	1.3	1.6
Other Ratios					
Cost-Income	33.9	30.1	26.5	25.8	24.4

One year Forward PABV



One year Price chart



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Disclosure:

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