

Stock Update Home First Finance Company India Ltd.

September 30, 2021





| Industry | LTP | Recommendation | Base Case Fair Value | Bull Case Fair Value | Time Horizon |
|----------|----------|---|----------------------|----------------------|--------------|
| NBFC-HFC | Rs.593.5 | Buy at LTP of Rs.593.5 & add more on dips of Rs.528 | Rs.630 | Rs.677 | 2 quarters |

| | |
|------------------------|-----------|
| HDFC Scrip Code | HOMEFIRST |
| BSE Code | 543259 |
| NSE Code | HOMEFIRST |
| Bloomberg | HOMEFIRS |
| CMP Sep 29, 2021 | 593.5 |
| Equity Capital (Rs Cr) | 17.5 |
| Face Value (Rs) | 2 |
| Equity Share O/S (Cr) | 8.7 |
| Market Cap (Rs Cr) | 5,194.4 |
| Book Value (Rs) | 153 |
| Avg. 52 Wk Volumes | 481192 |
| 52 Week High | 639.5 |
| 52 Week Low | 441.0 |

| Share holding Pattern % (Jun, 2021) | |
|-------------------------------------|-------|
| Promoters | 33.7 |
| Institutions | 56.5 |
| Non Institutions | 9.8 |
| Total | 100.0 |



HDFCsec Retail research
stock rating meter

for details about the ratings, refer at the end of the report

* Refer at the end for explanation on Risk Ratings

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Our Take:

Home First Finance Company India Ltd (HFFC) is a technology driven affordable housing finance company that targets first time home buyers in low and middle-income groups. Majority of the customers are salaried class (74%) and housing loan contributes 92% of total AUM. It is one of the fastest growing housing finance company. The management has put its conscious efforts to reduce concentration from key four states and establish its presence in newer areas/states. The expansion strategy includes pan India distribution driven by strategic market selection & contiguous expansion. Going forward, its future growth is likely to be driven by expansion of its successful credit delivery model into new markets and deeper penetration in the existing ones. The core technology focus and implementation across the process cycle has resulted in reduced TAT (Turn Around Time), efficient collection methods and higher productivity (highest employee as well as branch productivity among the peers).

Revival in demand for housing especially in the affordable housing segment due to conducive environment has improved the sentiments for the housing finance segment. The company is well capitalized to fund the higher growth. We believe that due to lower penetration and favorable demographics there is a good visibility of a decadal growth story for the HFCs.

Prolonged economic slowdown poses risk to the pace of collections and business growth. Any news on exit of PE players could bring volatility in the stock. High competition from large banks which have access to low cost funds could hurt the company in long term.

We had issued Initiating Report on HFFC on 25th May, 2021 and recommended Buy at LTP and add more on Rs.461, for base case target of Rs.565 and bull case target of Rs.611.5 over the next two quarters. The bull case target of Rs.611.5 was achieved on 9th July, 2021 yielding return of 19.4%.

Link for the Initiating Coverage:

<https://www.hdfcsec.com/hsl.research.pdf/Home%20First%20Finance%20Company%20India%20Ltd-Initiating%20Coverage%20-%2025052021.pdf>

Valuation & Recommendation:

HFFC has a track record of delivering industry leading growth. With branches maturing, the operating leverage will start kicking in. We have envisaged 25% CAGR for Net Interest Income and 29% CAGR for net profit over FY21-FY23E. Further, we have estimated that the AUM would grow at 24% CAGR (home loans at 24% and other loans at 21% CAGR). NIMs are estimated to improve gradually with



enhanced liquidity management. The company is planning to increase its LAP mix from current 6% of AUM to 15% of AUM over the medium term which is likely to support yields. The cost of funds is on a declining trend with improved borrowing mix. Management has guided to reduce GNPA by 10 bps every month for the next 2 to 3 quarters. With gradual economic pickup and improved sentiments, we believe that H2FY22 will post better overall performance compared to the first half. The stock at LTP is trading at 3.2x FY23 ABV.

We believe that investors can buy HFFC at LTP of Rs. 593.5(3.2x FY23E ABV) and add more at Rs.528 (2.85x FY23E ABV) for the base case fair value of Rs.630 (3.4x FY23E ABV) and for the bull case fair value of Rs.677 (3.65x FY23E ABV) over the next two quarters.

Financial Summary

| Particulars (Rs Cr) | Q1 FY22 | Q1 FY21 | YoY (%) | Q4 FY21 | QoQ (%) | FY20 | FY21 | FY22E | FY23E |
|---------------------|---------|---------|---------|---------|---------|-------|-------|-------|-------|
| NII | 83 | 77 | 8 | 75 | 11 | 198 | 248 | 304 | 386 |
| PPOP | 61 | 57 | 6 | 51 | 19 | 124 | 166 | 213 | 283 |
| PAT | 35 | 39 | -9 | 31 | 12 | 79 | 100 | 123 | 168 |
| EPS (Rs) | | | | | | 10.1 | 11.5 | 14.1 | 19.2 |
| ABV (Rs) | | | | | | 116.2 | 153.4 | 166.3 | 185.3 |
| P/E (x) | | | | | | 58.7 | 51.8 | 42.2 | 30.9 |
| P/ABV (x) | | | | | | 5.1 | 3.9 | 3.6 | 3.2 |
| RoAA (%) | | | | | | 2.7 | 2.5 | 2.5 | 2.9 |
| ROAE (%) | | | | | | 10.9 | 8.7 | 8.5 | 10.6 |

(Source: Company, HDFC sec)

Recent Developments

Q1FY22 Result Update

During the quarter, Net Interest Income stood at Rs. 83 Cr, up 11% on QoQ basis. Operating profit at Rs.60.6 Cr was up 6%/19% YoY/QoQ. The net profit was impacted by higher provisioning due to rise in NPA levels on account of COVID-19 second wave.

AUM grew by 18.5% YoY/3.7% QoQ to Rs.4294 Cr in Q1FY22. Disbursement of Rs.305 Cr was down 32.6%QoQ (though compared to peak quarter) and up 476% YoY (due to lower base). Growth was broad based across all the markets. The company completed transaction worth Rs.118 Cr on Direct assignment business.

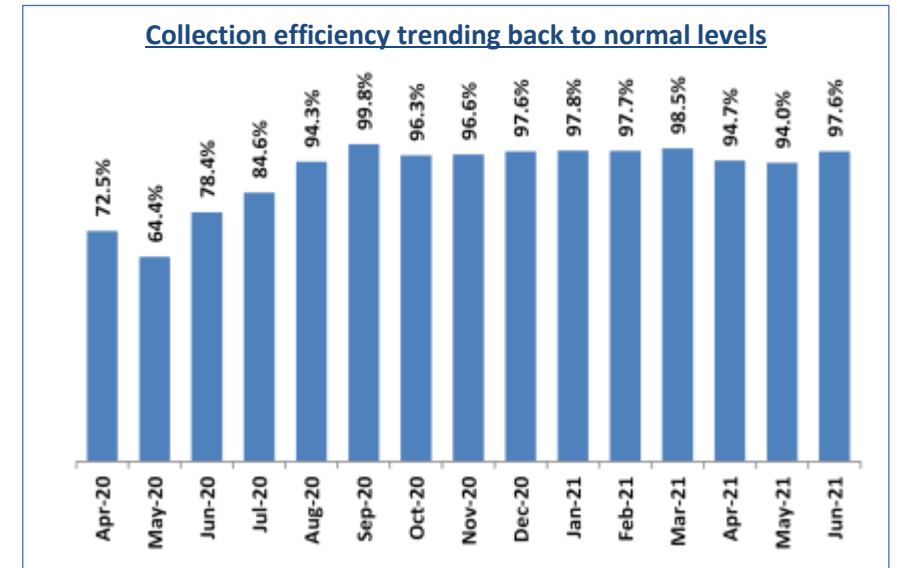
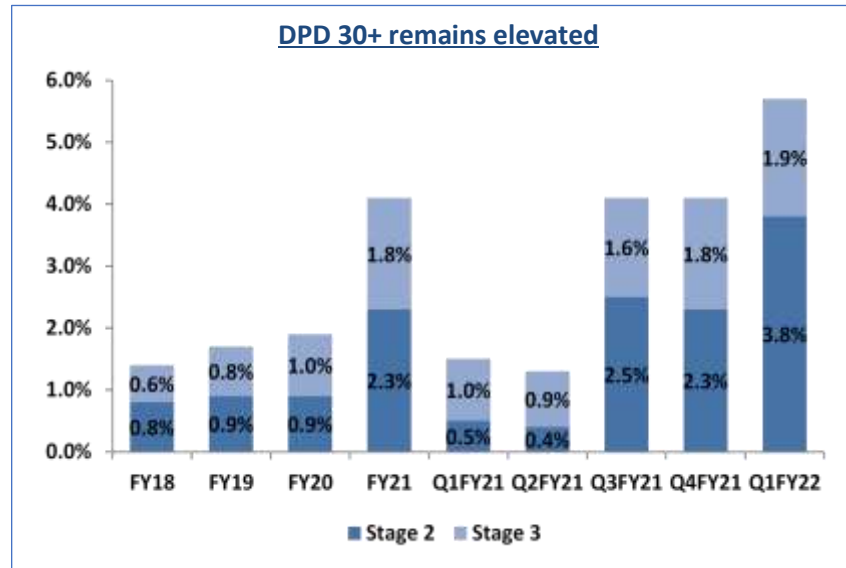


Even after high liquidity situation, the margin improved to 4.9% compared to 4.7% QoQ. This was due to better borrowing cost management (cost of borrowings 7.2% vs 7.4% QoQ). Another noteworthy improvement was Cost to income ratio at 32.1% (-595 bps QoQ), due to lower opex growth. Opex to AUM stood at 2.5% for the quarter, lower by 40bps on QoQ basis.

Management has informed that they are looking to reduce the liquidity in next couple of quarters, which will improve NIMs further. Branch expansion strategy could increase the cost burden, but continuous focus on technology could result in declining opex trend.

Asset Quality

The non-performing assets increased during the quarter due to COVID-19 second wave and subsequent lock downs. GNPA were at 1.9% compared to 1.8% QoQ and 1.0% YoY, while NNPA were at 1.4% compared to 1.2% QoQ and 0.7% YoY. Total provision to loan outstanding ratio stood at 1.4%. 30+DPD (Stage 2 at 1.9% and Stage 3 at 3.8%) rose to 5.8% from 4.1% QoQ and DPD 1+ was increased to 8.9% in Q1FY22 from 6.2% in Q4FY21. The restructuring of loans was at 0.6% in Q1FY22. Management has indicated that with the normalization of collections and business momentum, DPD 1+ print should gradually approach its pre-covid range of 3- 5% and they are looking to improve its Stage 3 assets by 10 bps every month for the next 2 to 3 quarters (lead reach to <1%). The collection efficiency level was also impacted in Mid-April to May and from June onwards it started to improve.



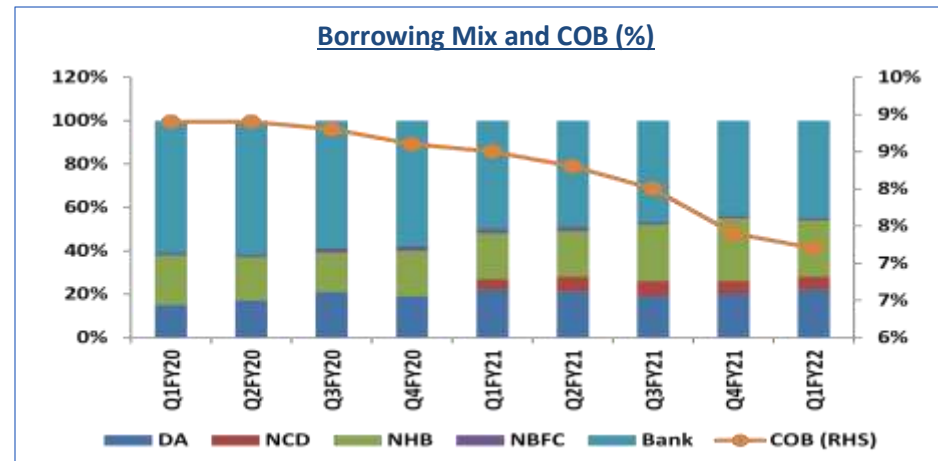


Credit underwriting process: HFFC has created a robust underwriting process. It incorporates advancements in technology, data aggregator and analytics to make the outcome consistent, accurate and cost effective. The underwriting spans across three levels: evaluation at the branch level, validation against digital databases, centralised underwriting at the head office level at the time of loan approval and centralised validation of all the previous processes at the time of disbursement of the loan. A single loan passes through at least 5 different pairs of eyes internally and 2 different pairs of eyes externally before the disbursement is initiated.

Strong capitalization level and diversified funding mix

The company continues to have adequate capitalization levels backed by healthy internal accruals and regular equity infusions in the past. The capital adequacy ratio remains strong with Tier 1 and overall CAR of 55.2% and 56.4% respectively as of Q1FY22. This is one of the best in class. This shows that HFFC has enough capital to fund the loan growth and strategy of aggressive branches expansion without any external capital infusion in the foreseeable future. Also, it gives the company a competitive advantage over peers as strong capital buffer could provide cushion for absorbing any asset-side shocks. It also has robust ALM profile ensuring sufficient liquidity buffers (Cumulative Positive flows across all the time buckets).

The company strengthened its asset liability profile through various strategies, which includes diversified the funding mix, broad-based the lender mix and consciously resisted the mobilization of commercial paper. It has also constantly tried to reduce dependence from bank's funding. Further, being an affordable housing financier, major part of the portfolio qualifies for priority sector lending. This opens up additional source of fund raising via assignment. It has a well-diversified funding mix from 18 financiers. As of Q1FY22, banks contribute 45%, assignment contributes 22%, NHB refinancing contributes 26%, NBFC contributes 1%, and NCDs contribute 6%.





Distribution strategy

HFFC has 72 physical branches with a significant presence in urbanized regions in the states of Gujarat, Maharashtra, Karnataka and Tamil Nadu. The focus for branch expansion will be on states which are more urbanized and which are larger contributors to the country's GDP because there is strong correlation between that and the demand for affordable housing. The company had started expansion in South about two years ago and now south contributes about 30% to the overall business. The next states of focus for expansion strategy are like Chhattisgarh, Madhya Pradesh, Rajasthan and Uttar Pradesh. Management has informed that the company will prefer to focus on the larger markets and the big pockets in these states. The expansion strategy is pan India distribution driven by strategic market selection & contiguous expansion. The biggest benefit from this strategy will be that it will reduce the over dependence of a few regions.

During the quarter, the company continued to increase its distribution, with commencing business at 33 potential branch locations, which contributes 14% of incremental business. The company has also established a physical presence in 32 new locations that are currently contributing 6% of incremental business. Management aims to add 20 branches over the next two years, while 50 different locations have been identified for digital expansion. As these new branches will start operating, the cost to income ratio will improve and rapid growth will be attained. The company has presence mainly in Tier-I/II cities and that too caters mainly to areas which are on the outskirts of cities.

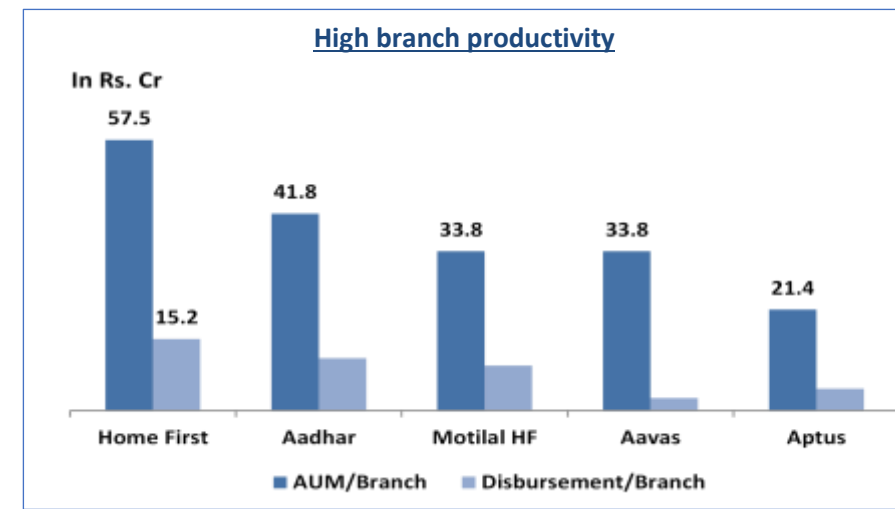
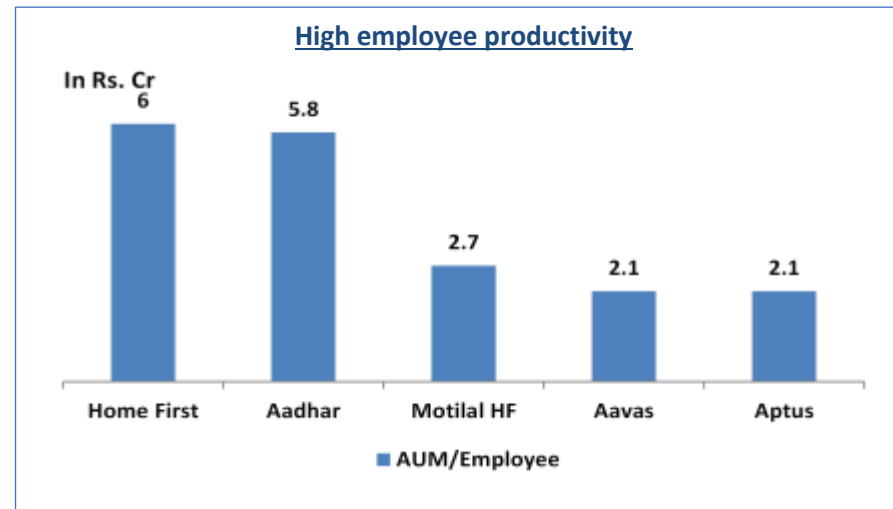
Geographic Expansion:

| States/Territories | FY19 | FY20 | FY21 | Q1FY22 |
|--------------------|-------|-------|-------|--------|
| Gujarat | 40.8% | 39.7% | 38.2% | 38.2% |
| Maharashtra | 28.4% | 21.7% | 19.2% | 18.7% |
| Tamil Nadu | 8.5% | 9.9% | 11.1% | 11.4% |
| Karnataka | 8.2% | 9.0% | 9.1% | 8.9% |
| Rajasthan | 3.8% | 5.0% | 5.5% | 5.3% |
| Telangana | 3.2% | 4.9% | 5.5% | 5.7% |
| Madhya Pradesh | 2.6% | 3.9% | 4.4% | 4.5% |
| UP & Uttarakhand | 2.0% | 2.6% | 2.9% | 3.0% |
| Haryana & NCR | 1.3% | 1.1% | 1.0% | 0.9% |
| Chhattisgarh | 0.8% | 0.9% | 1.2% | 1.2% |
| Andhra Pradesh | 0.4% | 1.3% | 1.9% | 2.2% |



Tech focus underpinning high productivity

The moat for HFFC is its ability to make technology driven process right from sourcing to collections. It has lowest number of branches among the peer group. More than 60% of the loans are being generated from connectors (individuals such as insurance agents, chartered accountants, tax practitioners, local retail outlets, building material suppliers etc.). They work on commission basis and use the Connector App for lead generation. Further, the centralized cloud-based platform helps in processing loan at a lower turn-around time and transaction cost. For collection management, the company has also built the digital platform. This tech focus helps the company in achieving higher productivity. Higher employee productivity (AUM/Employee) drives higher branch productivity (AUM/Branch), which in turns brings industry leading profitability. During the quarter the digital initiatives continue to see further progress. It has now launched electronic stamp paper, e-signatures and e-NACH across all branches. The company also has a centralized underwriting process which reduces any chances of fraud or inconsistency in underwriting.



Favorable environment

India's low mortgage penetration, favorable demographics and constant government push have already created structural upswing for the affordable housing segment. Moreover since last few months there has been a revival in demand for housing due to attractive prices, lower interest rates, lower stamp duties, and other benefits. Home sales volume across eight major cities in India jumped significantly. The improved sales momentum has lifted confidence among realty developers who have new offerings. The housing inventory is around seven year low. Industry experts believe that it is not only pent-up demand that will push growth but the country is going through a



structural transformation in housing demand. This is because of a combination of first-time homebuyers, and customers moving up the property ladder to shift to larger homes or acquiring a second home in another location, that is at play.

The pandemic was in fact the blessing in disguise for real estate, helping the industry establish its importance in the residential segment. Especially the millennial, who were earlier in favour of the rented house, have started showing great interest in buying their own home. As mobility was restricted to the house, people started searching for homes that accommodated entertainment, exercise and recreational area. HFFC being an aggressive player with stringent asset management practices remains in a sweet spot to ride the expected growth.

Risks & Concerns

Prolonged economic slowdown

The possibility of third wave and fresh lock downs could hurt the business on multiple fronts i.e. liquidity, asset quality, loan growth, collections etc. However, the company has 60% of the outstanding loan book coming from salaried segment and 70% of customers have credit history.

Competition

In the Covid-19 era of challenging time the banks and several other financial institutions have refrained from lending to the more risky segments such as unsecured consumer loans, SMEs, and vehicle finance. Banks have started focusing on mortgage business due to lack of other opportunities. This has created high competition in the housing finance segment. Some of the competitors like Canfin homes have taken price action. If this level of severity in competition continues, there could be impact on profitability of the company and fear of losing market share also remains high. However, due to niche focus of HFFC the severity is less.

A lot of fintechs are emerging, and in next few years they would probably enable themselves in delivering faster disbursement, automated sanction or automated disbursement. This risk factor is also emerging in the NBFC segment.

Geographic concentration

The business is highly concentrated in the top four states, and now spreading its presence in the rest part of the country. Any political and economic uncertainty in that region could impact the business. Even entry to newer geographies presents the risk on asset quality, as they are less discovered and the company does not have much history about the behavior of customers in those regions.

Ownership Structure

High ownership of private equity player and low float for the shareholders other than promoters / institutions could hurt the stock price in the case of exit by any of the large institutional holder. Any sustained offloading by the institutions could result in higher float and de-



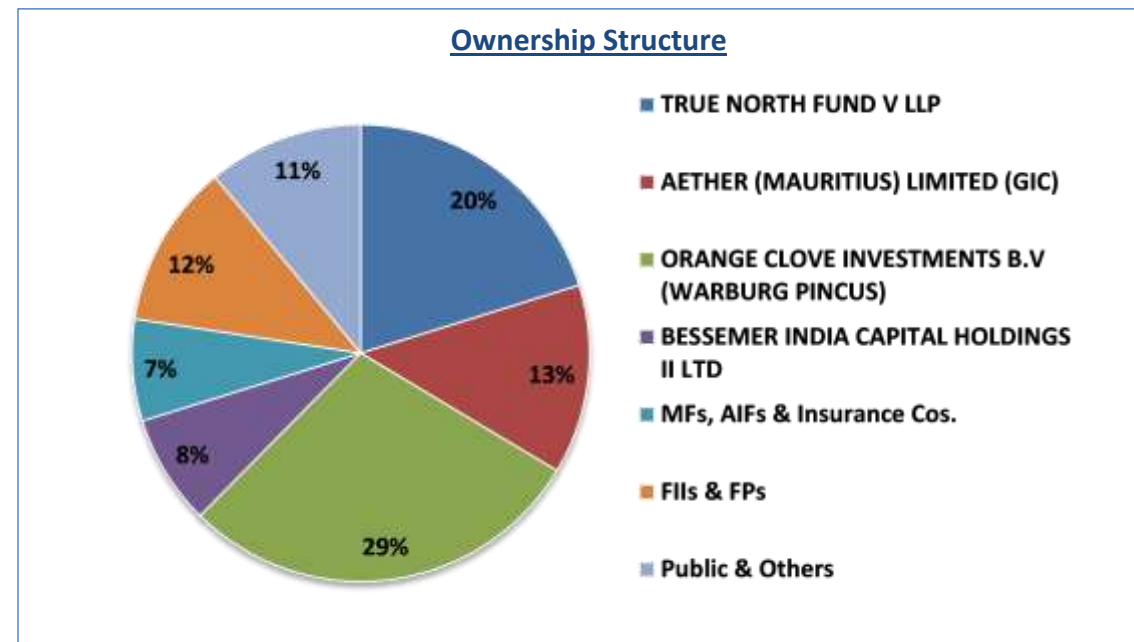
rating of the stock. This also brings the risk of change of ownership, which, if it happens, could change business functioning drastically while also impact its stock price significantly. Lack of long term strategic promoters is a weakness.

Low RoE

Due to excessive capitalisation (tier-1 at 55%) and despite 2.5% RoAs, RoEs will be modest at ~11%.

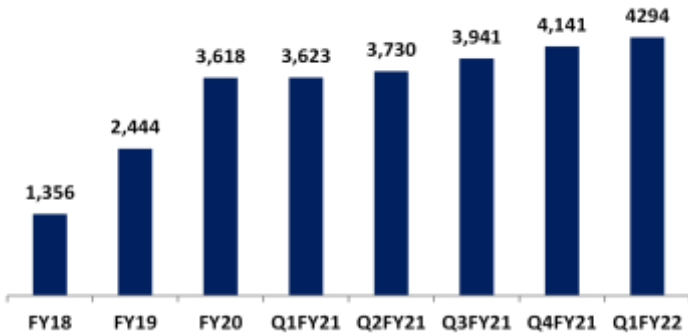
Company Background:

Home First Finance Company India Limited (HFFC) is a technology driven affordable housing finance company that targets first time home buyers in low and middle-income groups. It primarily offers housing loans for the purchase or construction of homes. 92% of book comprise of housing loans with average ticket size of Rs.10 lakh. The Company has deep penetration in the largest housing finance market with network of 72 branches across 76 districts in 12 states and 1 union territory in India, with a significant presence in urbanized regions in the states of Gujarat, Maharashtra, Karnataka and Tamil Nadu. The company has diversified lead generating channels with wide network of connectors.

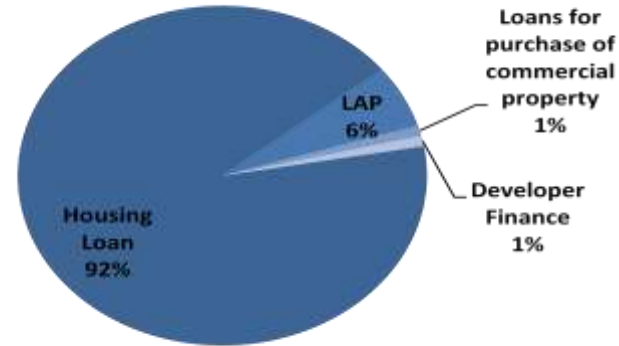




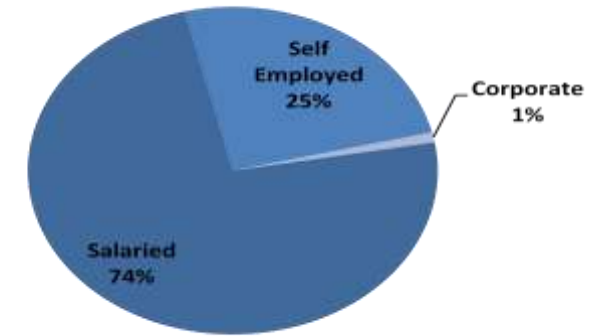
Continuous Growth in AUM (Rs cr)



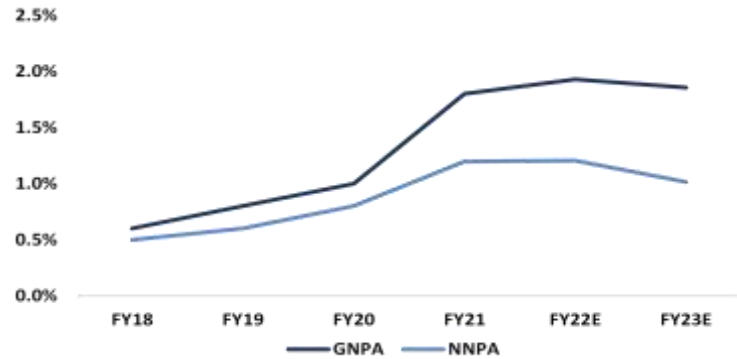
AUM Mix by Product



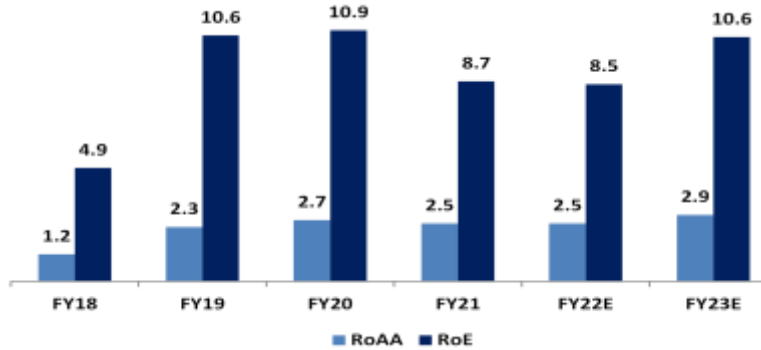
AUM by Occupation



NPA Trend



Return Ratios(%)



Peer comparisons

| | CMP | Mcap | Avg Ticket Size (Rs. Lk) | AUM (Rs. Cr) | GNPA | NNPA | NIM | ROA | P/ABV | | |
|---------------|------|--------|--------------------------|--------------|------|------|-----|-----|-------|-------|-------|
| | | | | | | | | | FY21 | FY22E | FY23E |
| AAVAS | 2609 | 20,586 | 10 | 9,616 | 1.1 | 0.9 | 7.0 | 2.6 | 8.7 | 7.7 | 6.6 |
| Can Fin Homes | 652 | 8,686 | 25 | 22,221 | 0.9 | 0.57 | 4.0 | 2.1 | 3.5 | 3.0 | 2.5 |
| HFFC | 594 | 5,194 | 10 | 4,294 | 1.9 | 1.4 | 7.8 | 2.5 | 3.9 | 3.6 | 3.2 |



Financials

Income Statement

| (Rs Cr) | FY19 | FY20 | FY21 | FY22E | FY23E |
|----------------------------|------------|------------|------------|------------|------------|
| Interest Income | 253 | 392 | 468 | 551 | 684 |
| Interest Expenses | 127 | 194 | 220 | 247 | 298 |
| Net Interest Income | 127 | 198 | 248 | 304 | 386 |
| Non interest income | 6 | 7 | 10 | 11 | 14 |
| Other Income | 11 | 21 | 12 | 12 | 13 |
| Operating Income | 144 | 226 | 269 | 328 | 412 |
| Operating Expenses | 72 | 102 | 103 | 114 | 129 |
| PPP | 72 | 124 | 166 | 213 | 283 |
| Prov & Cont | 7 | 17 | 32 | 45 | 53 |
| Profit Before Tax | 65 | 107 | 134 | 169 | 230 |
| Tax | 20 | 28 | 34 | 46 | 62 |
| PAT | 45 | 79 | 100 | 123 | 168 |

Balance Sheet

| (Rs Cr) | FY19 | FY20 | FY21 | FY22E | FY23E |
|----------------------------------|-------------|-------------|-------------|-------------|-------------|
| Share Capital | 13 | 16 | 17 | 17 | 17 |
| Reserves & Surplus | 510 | 918 | 1363 | 1486 | 1654 |
| Shareholder funds | 523 | 934 | 1380 | 1504 | 1671 |
| Borrowings | 1927 | 2494 | 3054 | 3713 | 4506 |
| Other Liab & Prov. | 32 | 52 | 76 | 110 | 163 |
| SOURCES OF FUNDS | 2482 | 3480 | 4510 | 5327 | 6341 |
| Fixed and Other Intangible Asset | 17 | 21 | 17 | 22 | 28 |
| Investments | 103 | 146 | 375 | 375 | 375 |
| Cash & Bank Balance | 192 | 222 | 680 | 640 | 643 |
| Advances | 2135 | 3014 | 3327 | 4148 | 5120 |
| Other Assets | 35 | 77 | 112 | 141 | 174 |
| TOTAL ASSETS | 2482 | 3481 | 4510 | 5327 | 6341 |

(Source: Company, HDFC sec)



Home First Finance Company India Ltd.

Key Ratios

| | FY19 | FY20 | FY21 | FY22E | FY23E |
|-----------------------------|--------|-------|-------|-------|-------|
| Return Ratios | | | | | |
| Calc. Yield on adv | 14.7% | 15.2% | 14.7% | 14.8% | 14.8% |
| Calc. Cost of borr | 6.6% | 7.8% | 7.2% | 6.7% | 6.6% |
| NIM | 7.4% | 7.7% | 7.8% | 8.1% | 8.3% |
| RoAE | 10.6% | 10.9% | 8.7% | 8.5% | 10.6% |
| RoAA | 2.3% | 2.7% | 2.5% | 2.5% | 2.9% |
| Asset Quality Ratios | | | | | |
| GNPA | 0.8% | 1.0% | 1.8% | 1.9% | 1.9% |
| NNPA | 0.6% | 0.8% | 1.2% | 1.2% | 1.0% |
| PCR | 24.7% | 25.7% | 36.0% | 37.5% | 45.3% |
| Growth Ratios | | | | | |
| Advances | 63.1% | 41.2% | 10.4% | 24.7% | 23.4% |
| Borrowings | 88.8% | 29.4% | 22.4% | 21.6% | 21.4% |
| NII | 98.3% | 56.1% | 25.0% | 22.9% | 26.7% |
| PPP | 167.3% | 70.7% | 34.5% | 28.3% | 32.7% |
| PAT | 182.9% | 75.3% | 26.6% | 22.8% | 36.4% |

(Source: Company, HDFC sec)

One Year Price Chart



Key Ratios

| | FY19 | FY20 | FY21 | FY22E | FY23E |
|---------------------------------|-------|-------|-------|-------|-------|
| Valuation Ratios | | | | | |
| EPS | 35.6 | 10.1 | 11.5 | 14.1 | 19.2 |
| P/E | 16.7 | 58.7 | 51.8 | 42.2 | 30.9 |
| Adj. BVPS | 402.9 | 116.2 | 153.4 | 166.3 | 185.3 |
| P/ABV | 1.5 | 5.1 | 3.9 | 3.6 | 3.2 |
| Dividend per share | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other Ratios | | | | | |
| Cost-Income | 49.8 | 45.2 | 38.2 | 34.9 | 31.3 |
| Avg Net worth/ Avg Total Assets | 4.2 | 4.7 | 3.7 | 3.3 | 3.5 |



HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicity of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

Disclosure:

I, **Nisha Sankhala, (MBA)**, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. HSL has no material adverse disciplinary history as on the date of publication of this report. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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