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Initiating Coverage
Home First Finance Company India Ltd.

25-May-2021

RETAIL RESEARCH

Home First Finance Company India Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
HFC	Rs.512	Buy at LTP and add more at Rs.461	Rs.565	Rs.611.5	2 quarters

HDFC Scrip Code	HOMEFIRST
BSE Code	543259
NSE Code	HOMEFIRST
Bloomberg	HOMEFIRS
CMP May 24, 2021	512
Equity Capital (RsCr)	17.5
Face Value (Rs)	2
Equity Share O/S (Cr)	8.7
Market Cap (Rs Cr)	4,477.35
Adj. Book Value (Rs)	153
Avg. 52 Wk Volumes	810830
52 Week High	639.5
52 Week Low	441.0

Share holding Pattern % (Mar, 2021)	
Promoters	33.70
Institutions	53.50
Non Institutions	12.79
Total	100.0

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Our take

Home First Finance Company India Ltd (HomeFirst) is a technology driven affordable housing finance company that targets first time home buyers in low and middle-income groups. Its AUM as on FY21 stood at Rs. 4141cr which has grown at CAGR 45% over FY17-20 which makes it one of the fastest growing HFC's in India. The company mainly offers customers housing loans for the purchase or construction of homes, which comprised 92.1% of gross loan assets with average ticket size of Rs. 10 lakhs. Majority of customers are salaried class (~75%) who are typically employed by small firms or work in junior positions in larger companies. Around 69% of the loans are given to completely new-to-credit category of customers who have no credit history. The company operates mainly in Tier-I and II cities and its target audience is low ticket size customers which are underserved by larger corporate banks. These are typically people looking out for home loans in the periphery of larger cities.

We believe that India's low-cost housing segment provides a huge opportunity and it is at a decadal structural upswing. Strategically the company is well placed as based on the home loans outstanding in the affordable housing segment, the top 15 states account for over 90% of the market size in this segment. Its top 3 states contribute ~68% of its total AUM which comprises of -Maharashtra 19% share, Gujarat 38% and Tamil Nadu has 11% - these are key focused markets for HomeFirst. The Company has a diverse range of lead sourcing channels and unlike other affordable housing finance companies, HomeFirst has relied more on external means for lead generation. The company has technology at the core - right from sourcing to collections and this elevated level of focus on technology is creating an edge for the company in many ways like reducing turn-around times and transaction costs, building a scalable operating model, uniformity in operations, enhance customer experience. The company has experienced management team and has marquee investors.

Valuation and recommendation:

We have envisaged 28% CAGR for Net Interest Income and 36% CAGR for net profit over FY21-FY23E. Further, we have estimated that the AUM would grow at 25% CAGR (home loans at 25% and other loans at 21% CAGR). The initial asset quality picture, post moratorium, looks positive and collection efficiencies have also reached the pre-COVID level. Rising operating and financial leverage will result in increase in RoE and RoA. We believe that the NPAs will start to reduce from H2FY22. The stock is currently trading at a 3.1x and 2.7x FY22E and FY23E ABV. We believe that investors can buy HomeFirst at LTP and add more at Rs.461 (2.45xFY23E ABV) for the base case fair value of Rs.565 (3xFY23E ABV) and for the bull case fair value of Rs.611.5 (3.25xFY23E ABV) over the next two quarters.

Home First Finance Company India Ltd.

Financial Summary

Particulars (RsCr)	Q4FY21	Q4FY20	YoY-%	Q3FY21	QoQ-%	FY19	FY20	FY21	FY22E	FY23E
NII	75	49	53	53	40	127	198	248	315	404
PPOP	51	28	81	29	78	72	124	166	228	312
PAT	31	12	151	16	97	45	79	100	131	185
EPS (Rs)						35.6	10.1	11.5	15.0	21.1
ABV (Rs)						402.9	116.2	153.4	167.2	188.1
P/E (x)						14.4	50.7	44.5	34.1	24.3
P/ABV (x)						1.3	4.4	3.3	3.1	2.7
RoAA (%)						2.3	2.7	2.5	2.6	3.1

(Source: Company, HDFC sec)

Q4FY21 Result Update

In Q4FY21, HomeFirst reported strong earnings with profit after tax growth of 150% YoY and 96.6% QoQ. The company saw record disbursements of Rs. 452 Cr in Q4FY21, growth of 30.4% YoY and a sequential growth of 29.5%. Assets Under Management stood at Rs.4141 Cr, up 14.4% on a YoY basis. The Southern India markets now contribute to more than 30% of disbursements and about 27.6% of AUM. Cost of borrowings declined 60bps QoQ and 120bps YoY to 7.4%. This aided spreads increase of 40bps QoQ and 90bps YoY to 5.4%.

For FY21, HomeFirst’s Profit crossed Rs.100 Cr mark, which is the highest in the history of the company with a growth of 25.9% on a YoY basis. Net Interest Income grew by 23% YoY at Rs.186 Cr.

Management has indicated that they have identified about 50 more locations for physical or digital presence and they will commence business in these locations by Q3 to Q4 of FY22; these branches will contribute to the growth in FY23.

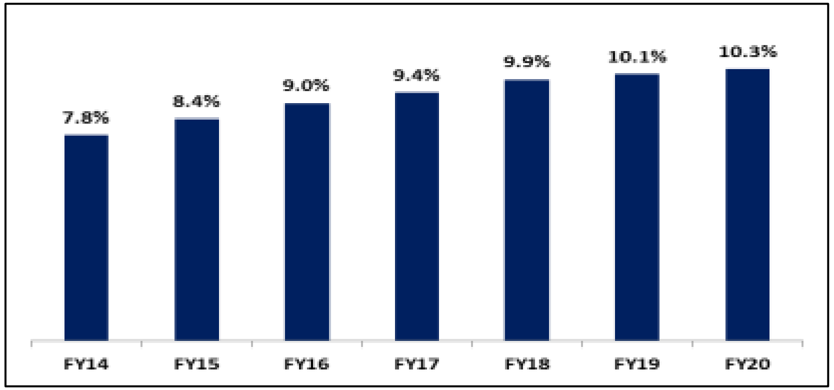
Long-term triggers

Vast opportunity in India's low-cost housing segment

The Indian Housing Finance market size is Rs.21.2 Lakh Cr., Mortgage penetration in India is just 10.3% (as of Mar-20), which is substantially lower than developed and other developing nations, leaving huge scope for growth in demand for housing loans. The situation is even worse in the lower income segments in urban as well as rural areas. We believe that the Affordable segment could grow at a faster pace than overall industry due to: (a) interest subsidy by the Government for affordable housing; (b) favorable demographics; (c) increasing affordability; (d) rapid urbanisation. Moreover, the current urban housing shortage is estimated at 10 mn houses, which is slated to rise in future. As per a CRISIL study, the combined housing finance demand for 2022 stands at Rs.5 trillion for the economically weaker sections (EWS) category and Rs. 30 trillion for the low-income group (LIG) category, both of which are the key target markets for players like HomeFirst. All these factors show that the housing industry is in a decadal structural upswing and in a good place for delivering future growth.

Since the past five years, the residential real estate sales have been almost stagnant. COVID-19 pandemic has further created a sharp price cut. Early economic indicators are encouraging. The government's constant aids to the sector along with lowest interest rates are key triggers for us to believe that the real estate and housing finance sectors have bottomed out.

Mortgage Penetration (%)

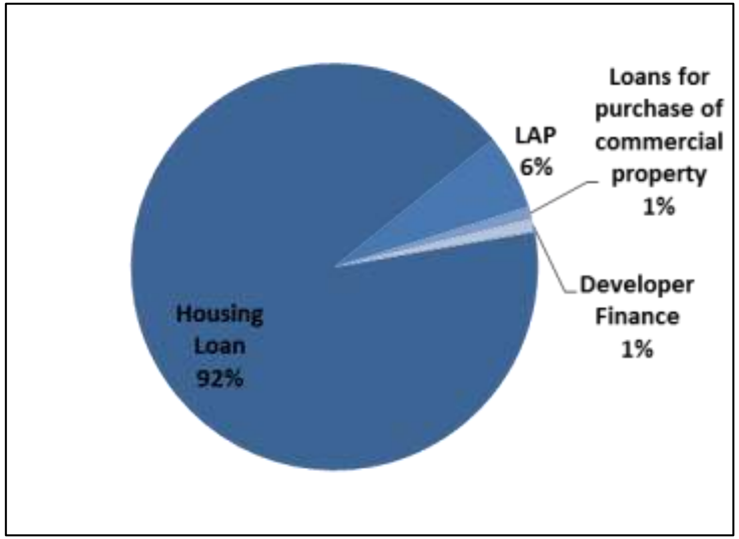


(Source: Company, HDFC sec)

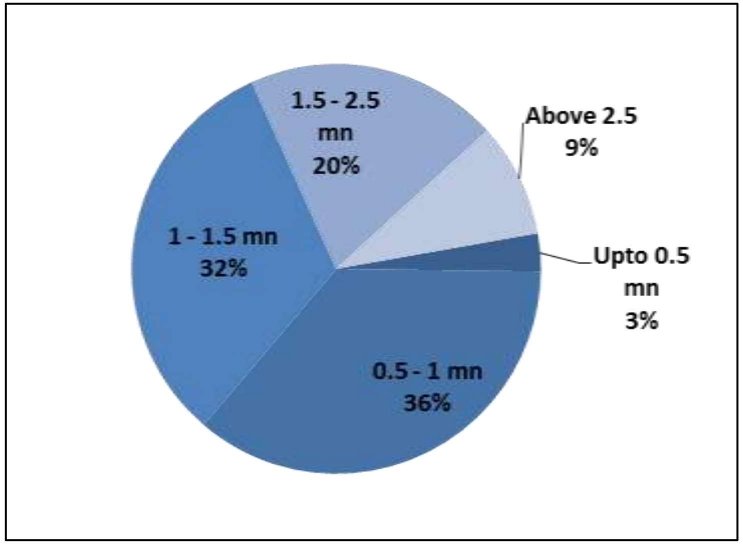
Unique Business Model

In the mortgage lending business, HomeFirst has created a niche business model to serve the underpenetrated and under-served segments. It has a centralized systerm-driven underwriting process which reduces any chances of fraud or inconsistency in underwriting at the branch level. It focuses on customers who are from low and middle income groups. Primarily it offer customers housing loans for the purchase or construction of homes, which comprised 92.1% of gross loan assets. Remaining 6% is loan againts properties, 1% loans for purchase of commercial property and 1% developer finance. As of FY21, 74% of its total borrowers are Salaried, 25% are Self Employed and the remaining 1% is Corporates. Salaried customers are typically employed by small firms or work in junior positions in larger companies, while self-employed customers are small business owners. 69% of the loans are given to completely new-to-credit category or customers who have no credit history.

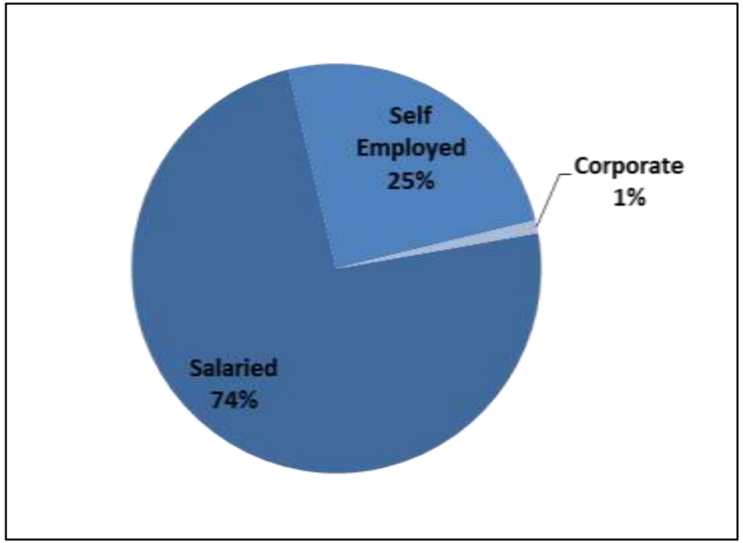
AUM Split by Product (%)



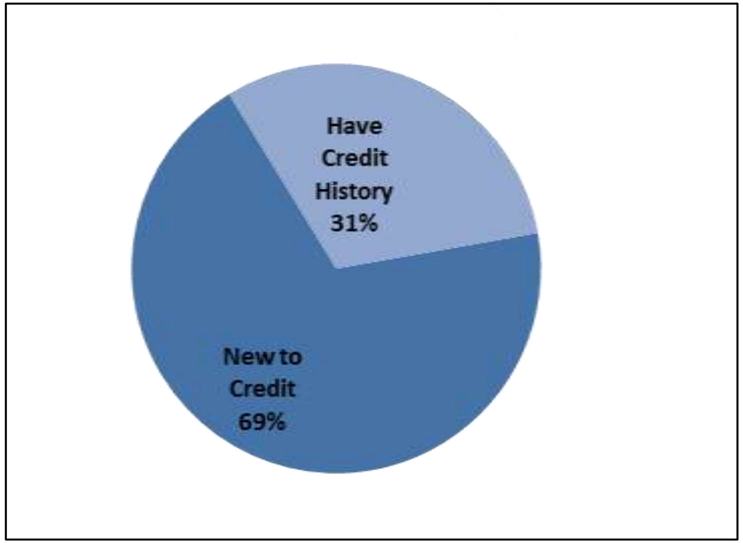
AUM Split by Ticket Size (%)



AUM Split by Occupation (%)



AUM Split by Credit history (%)



(Source: Company, HDFC sec)

Strategically Well Placed

Since the beginning, the company has focused on a few geographies where it understands the market well. The branches are highly concentrated in top-3 states. Out of 72 branches, 20 are in Gujarat, 15 in Maharashtra and 11 in Tamil Nadu. 68.5% of Gross Loan Assets as on FY21 are from these 3 states. Strategically the company is well placed as based on the home loans outstanding in the affordable housing segment, the top 15 states account for over 90% of the market size in this segment. Maharashtra has 19% share, Gujarat 10% and Tamil Nadu has 10% - these are key focused markets for HomeFirst. Even before expanding to newer geographies or setting up new branches, the company conducts in-depth studies and market research to assess potential sustainable demand for its products and engage with local property valuers and legal advisors.

Omni-channel Lead generation

HomeFirst has a diverse range of lead sourcing channels such as connectors, architects, contractors, affordable housing developers, in addition to conducting loan camps, micro marketing activities, employee and customer referrals and branch walk-in customers. As of FY21, 62.2% of the leads were generated via connectors, 14.6% via builder ecosystem, 7.4% via branch, 6.1% via construction community, 4% via marketing and remaining by others. Unlike affordable housing finance companies, HomeFirst has relied more on external means for lead generation.

Connectors are generally individuals such as insurance agents, chartered accountants, tax practitioners, local retail outlets, building material suppliers etc. The company has more than 1000 active connectors. They work on commission basis. 92.2% connectors are registered on the Connector App.

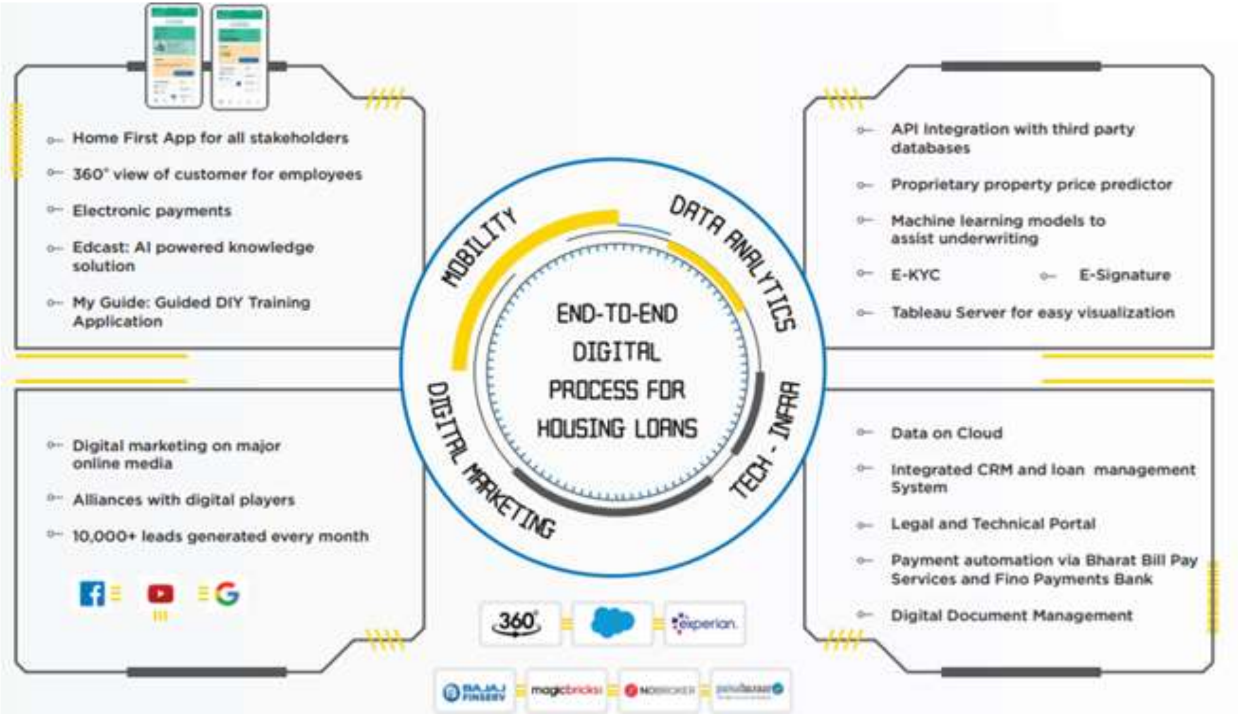
The company has also entered into arrangements with certain digital lead aggregators and other digital companies in the housing and real estate ecosystem such as Homelane, Paisa Bazaar, Quikr India, Credit Mantri and Aapka Painter, which helps it source leads embedded with customer data.

Technology Driven Company

The company has technology at the core - right from sourcing to collections. This elevated level of focus on technology is creating an edge for the company in many ways like reducing turn-around times and transaction costs, building a scalable operating model, uniformity in operations, enhance customer experience.

HomeFirst is truly a technology driven affordable housing finance company as it has Rs.5-7.5Cr of software and technology spend every year (almost 7% of opex). This has helped the company in getting industry-leading productivity ratios. The turnaround time is only 48 hours against the industry average of 8 to 10 working days. It is able to digitally capture over 100 data points of a customer in addition to credit bureau data, observations of its front-end teams and feedback from its underwriting and management teams. This integrated customer relationship management and loan management system provides a holistic view of its customers and ensures connectivity and uniformity across its branches. It has set up a robust collections management system wherein ~93% of their collections for FY20 were non-cash based, which eases stress on monitoring financial transactions and reduces their cash management risk.

Scalable operating model built on holistic technology usage



(Source: Company, HDFC sec)

<u>Experienced Management Team and Marquee Investors</u>

The company has a professional and experienced management team, led by CEO and founder, Manoj Viswanathan, who has over 24 years of experience in the consumer lending industry. In addition, Ajay Khetan, Gaurav Mohta and Vilasini Subramaniam joined founding team over five years ago. The management team has extensive experience in the financial services sector and is supported by qualified operational personnel who have an in-depth understanding of the geographic regions in which the company operates. It has distinguished Board comprising industry professionals with significant experience in the financial services industry.

The promoters are True North Fund V LLP and Aether (Mauritius) Limited. Further, Bessemer has invested in the Company since January 2011 and Orange Clove Investments B.V. (an affiliate of Warburg Pincus, a global private equity investor) has acquired a stake in the Company in October 2020. HomeFirst has continued to benefit from strong capital sponsorship and professional expertise of marquee shareholders. In addition to assisting with capital raising and strategic business advice, these shareholders have assisted it in implementing strong corporate governance, which is critical to the growth of the business. As on March 31, 2021, private equity investors had a significant stake in Home First – True North (20.3%) and Aether (13.4%) in the promoter category while Bessemer Venture Partners (7.8%) and Orange Clove Investments B.V (28.8%) are other key investors.

Robust financials

Despite weak industry scenario i.e. liquidity crunch, weak real estate demand, the company has posted AUM CAGR of 61% while disbursements grew by 50% CAGR over FY15-20.

HomeFirst has diversified funding profile at competitive cost of borrowing. As of Q4FY21, 44% of total borrowing is funded via Banks, 29% via NHB, 1% via NBFC, 6% via NCD and 20% via Direct Assignment. The company has constantly focused on reducing dependence from bank's funding. Cost of borrowing has gone down to 7.4% as of March 2021 compared to 8.9% in June 2019.

The operating expenses have seen a downward trend due to improving operating efficiencies, opex to AUM stood at 2.7% for FY21.

On margin side, HomeFirst has been operating at a healthy and consistent spread of over 4.5% over the past few quarters; spread went up from 5% in Q3FY21 to 5.4% in Q4FY21.

Strong Capital adequacy Ratio

The capital adequacy ratio remains strong with Tier 1 and overall CAR of 56.2% and 55.2% respectively (as of Q4FY21), which is well above the regulatory requirement at 10% and 13% respectively. This is the best in class and we believe that HomeFirst should be able to meet its growth target 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. HomeFirst has also always taken a conservative approach on ALM management and has a surplus across all its lending buckets. In Q4FY21, ~Rs. 1300cr of surplus funds were available to the business.

Asset Quality

The company has created a robust underwriting team comprising credit managers and disbursement officers, who evaluate the customers' business and financing needs as well as their ability to repay. The company has also been constantly investing in data analytics for better market intelligence, which helps it track the client's credibility and worthiness.

Even during the time of Covid-19 stress, the company has been able to manage industry level asset quality. In Q4FY21, its gross NPLs were at 1.8% of total loans and net NPLs at 1.2% with zero restructuring. All the leading indicators of asset quality such as bounce rates and 1 DPD have shown improvement over the previous quarter. Bounce rates have improved from 20.1% in Q3FY21 to 17.3% in Q4FY21. 30 DPD was at 4.1% and was stable on a quarter-on-quarter basis and 1 DPD has improved significantly from 7.5% in Q3FY21 to 6.2% in Q4FY21. The collection efficiency has ratio has improved to 98.5%+ in Mar-21.

Productivity Parameters

The company has put in place the well-defined operational strategies and frameworks with the help of technology. It also has trained and educated front line team. All these have enabled the company in achieving much higher branch as well as employee productivity. It has amongst the lowest numbers in branch presence amongst its peer group but has comparable employee strength. Disbursement per branch stood at Rs.25-30 Cr compared to Rs.10-14 Cr for other affordable housing finance companies; also the disbursement per sales employee is at Rs.3-4.5 Cr compared to Rs.1.5-2.5 Cr for peers. The turnaround time is only 48 hours against the industry average of 8 to 10 working days.

Risks and concerns

Inherently risky business profile

HomeFirst focuses on providing retail home loans to lower income groups, mainly the salaried groups (employed by small firms or work in junior positions in larger companies) in semi-urban and urban regions, which makes its business profile inherently risky. As of FY21, 74% of its total borrowers are Salaried, 25% are Self Employed and the remaining 1% is Corporates. The company caters to economically vulnerable borrowers, who have low and undocumented incomes. 69% of the AUM is new to credit category.

However, the company has created an effective risk management system with advance technology and analytics, which helps it analyse borrower's profile and monitor collection trends, thereby allowing it to manage its asset quality well.

Higher C/I ratio of 39% as on FY21

Home first, despite being a largely digital driven HFC, has a cost structure that is significantly on the higher side when compared to some manual HFCs. In case the company is unable to improve its its operational efficiencies the benefits of being digital will not fully flow down in the bottom-line.

Also its RoE is low at the moment because of overcapitalized Balance sheet. As the leverage ratio rises, this could get corrected.

High geographical concentration

The branches are highly concentrated in top-3 states. Out of 72 branches, 20 are in Gujarat, 15 in Maharashtra and 11 in Tamil Nadu. 68.5% of Gross Loan Assets as on FY21 is from these 3 states. Any natural calamities, policy change or adverse conditions in these regions could affect the business significantly. To tackle this problem, management has started diversifying away from these main states; new branches are opening in other geographies. However, looking at distribution strategy, we believe that diversification would be slow.

Sourcing as well as collections management

The company has front-end team which is responsible for both sourcing as well as collections management. This is contrary to other HFC's operating structure, where sourcing, operations, credit/underwriting and collections are managed separately by different teams with no overlap in functionalities. Because of this dual responsibility increased focus on one may sometimes come at the cost of focus on other i.e. in H1FY20 there was a sharp dip in disbursements as the focus diverted towards collections and stringent underwriting standards.

Competition

The housing finance industry is highly competitive. It has always faced competition from small finance banks, banks and other HFCs. Banks with wider branch and distribution network and cheaper cost of funds have greater competitive advantage. The stiff competition from banks may pose increasing challenges by way of lower-than-expected loan growth and lower NIMs. Also, any adverse change of norms for housing finance companies can impact the growth prospects, especially so since the change of the regulatory body from NHB to RBI, as mentioned in Budget FY20.

Macro situation

Over the past 2-3 years, inventory for the real estate sector has been piling up in India, while launch of new projects has come down in the past one and half year, as the COVID-induced economic slowdown has made matters worse.

Slower-than-expected pick-up in the economy could impact the growth of the company’s Assets Under Management. The key risks to our thesis are lower-than-expected loan growth and more-than-expected asset quality deterioration.

Ownership Structure

The company is owned by private equity players. Therefore, it is exposed to 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.

Home First Finance Company India Ltd.

Company background

Home First Finance Company India Limited (HomeFirst) 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. The Company has deep penetration in the largest housing finance market with network of 72 branches across 60 districts in 11 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.

In February 2010, the company was co-founded by former Mphasis Chairman, Mr. Jaithirth (Jerry) Rao and Mr. P. S. Jayakumar (former Citibank Consumer Banking Head and former MD & CEO of Bank of Baroda).

The company got listed recently on 3rd February, 2021. The initial public offer (IPO) was of Rs.1153.7 Cr, comprising a fresh issue of up to Rs.265 Cr and an offer for sale of up to RSs.888.7 Cr. The issue was subscribed 26.21 times and made a strong debut on the day of listing on exchanges with prices rising about 23% to Rs.639 apiece, as compared IPO issue price range of Rs.517-518.

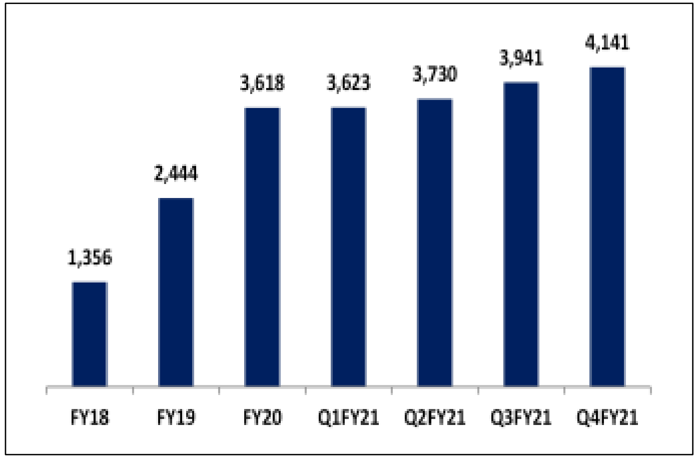
As on March 31, 2021, private equity investors had a significant stake in Home First – True North (20.3%) and Aether (Mauritius) Limited (13.4%) in the promoter category while Bessemer Venture Partners (7.8%) and Orange Clove Investments B.V (Warburg Pincus) (28.8%) are other key investors.

Peer Comparison:

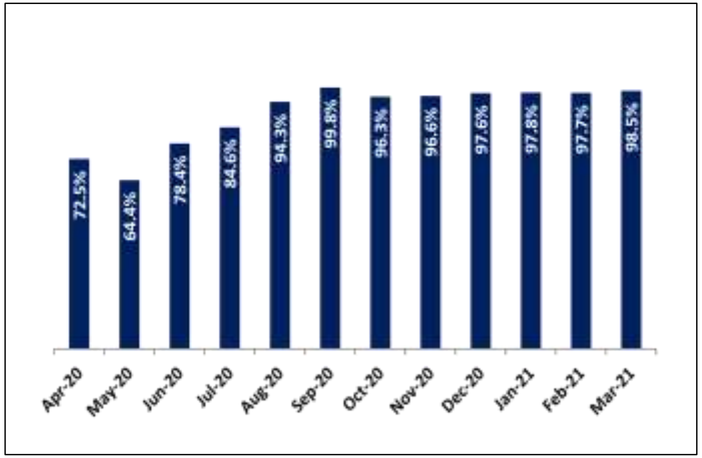
	CMP	Mcap	AUM (Rs. Cr)	GNPA	NNPA	NIM	ROA	P/ABV		
								FY21	FY22	FY23
AAVAS	2322	18,228.4	9454.3	1	0.7	7.7	3.5	7.8	6.8	5.9
HomeFirst	512	4,477.4	4141.1	1.8	1.2	7.8	2.5	3.3	3.1	2.7

Home First Finance Company India Ltd.

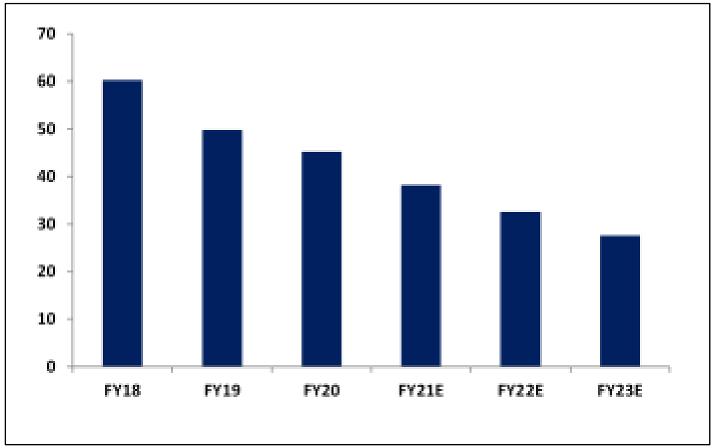
AUM (Rs Cr)



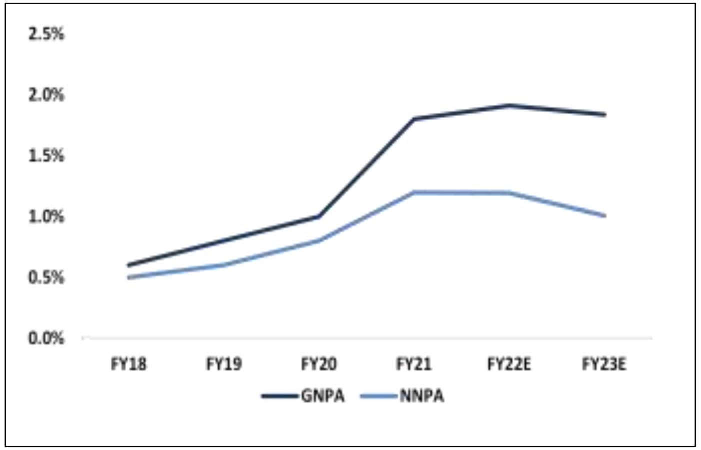
Collection Efficiency



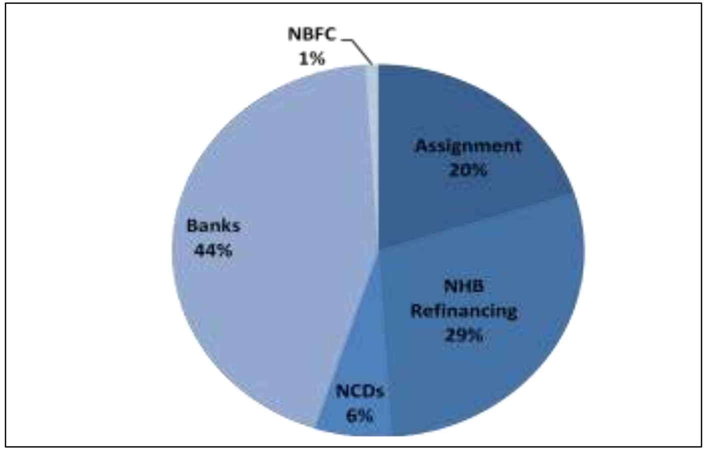
Cost to Income Ratio



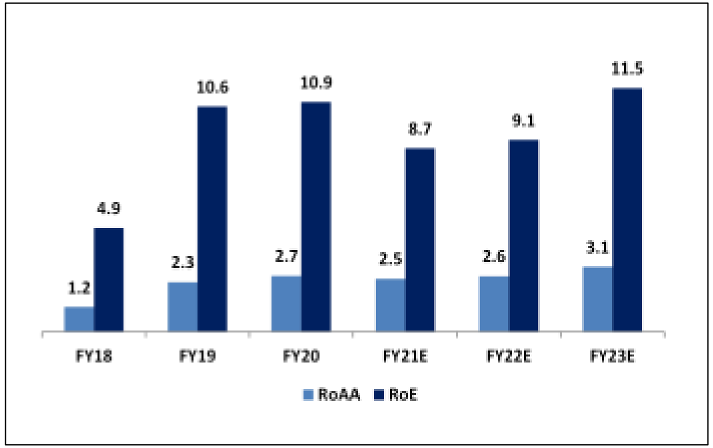
NPAs Trend



Well diversified liability profile



Return Ratios



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Home First Finance Company India Ltd.

Financials

Income Statement

(Rs Cr)	FY19	FY20	FY21P	FY22E	FY23E
Interest Income	253	392	468	556	697
Interest Expenses	127	194	220	241	293
Net Interest Income	**127**	**198**	**248**	**315**	**404**
Non interest income	6	7	10	11	14
Other Income	11	21	12	12	12
Operating Income	**144**	**226**	**269**	**338**	**431**
Operating Expenses	72	102	103	110	119
PPP	72	124	166	228	312
Prov & Cont	7	17	32	49	58
Profit Before Tax	65	107	134	180	253
Tax	20	28	34	48	68
PAT	**45**	**79**	**100**	**131**	**185**

Balance Sheet

(Rs Cr)	FY19	FY20	FY21P	FY22E	FY23E
Share Capital	13	16	17	17	17
Reserves & Surplus	510	918	1363	1494	1679
Shareholder funds	**523**	**934**	**1380**	**1512**	**1696**
Borrowings	1927	2494	3054	3831	4781
Other Liab & Prov.	32	52	76	110	163
SOURCES OF FUNDS	**2482**	**3480**	**4510**	**5453**	**6640**
Fixed and Other Intangible Asset	17	21	17	18	20
Investments	103	146	375	375	375
Cash & Bank Balance	192	222	680	731	901
Advances	2135	3014	3327	4186	5168
Other Assets	35	77	112	142	176
TOTAL ASSETS	**2482**	**3481**	**4510**	**5453**	**6640**

(Source: Company, HDFC sec Research)

Home First Finance Company India Ltd.

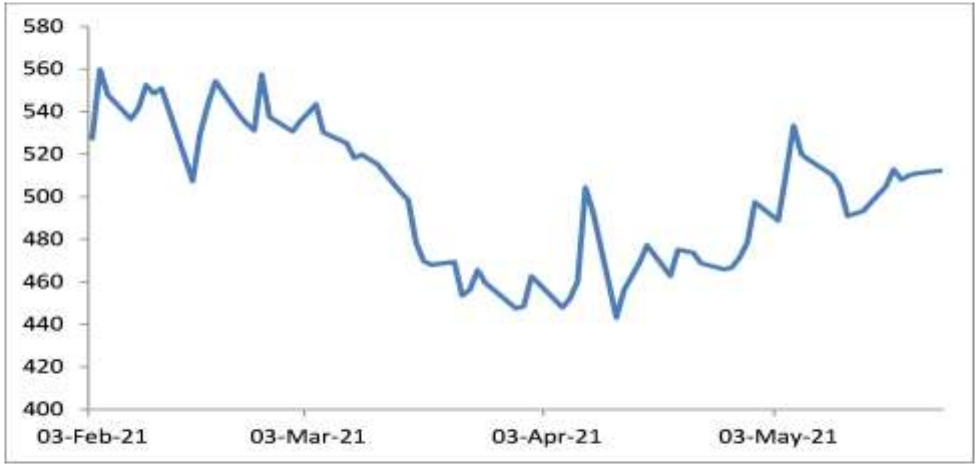
Key Ratios (%)

(Rs Cr)	FY19	FY20	FY21P	FY22E	FY23E
Return Ratios					
Calc. Yield on adv	14.7%	15.2%	14.7%	14.8%	14.9%
Calc. Cost of borr	6.6%	7.8%	7.2%	6.3%	6.1%
NIM	7.4%	7.7%	7.8%	8.4%	8.6%
RoAE	10.6%	10.9%	8.7%	9.1%	11.5%
RoAA	2.3%	2.7%	2.5%	2.6%	3.1%
Asset Quality Ratios					
GNPA	0.8%	1.0%	1.8%	1.9%	1.8%
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%	25.9%	23.4%
Borrowings	88.8%	29.4%	22.4%	25.4%	24.8%
NII	98.3%	56.1%	25.0%	27.3%	28.3%
PPP	167.3%	70.7%	34.5%	37.3%	36.5%
PAT	182.9%	75.3%	26.6%	30.8%	41.1%

Key Ratios (%)

(Rs Cr)	FY19	FY20	FY21P	FY22E	FY23E
Valuation Ratios					
EPS	35.6	10.1	11.5	15.0	21.1
P/E	14.4	50.7	44.5	34.1	24.3
Adj. BVPS	402.9	116.2	153.4	167.2	188.1
P/ABV	1.3	4.4	3.3	3.1	2.7
Dividend per share	0.0	0.0	0.0	0.0	0.0
Other Ratios					
Cost-Income	49.8	45.2	38.2	32.5	27.6
Avg. Net worth/ Avg. Total Assets	4.2	4.7	3.7	3.3	3.6

One Year Price Chart



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