NSSPL RESEARCH

GIC Housing Finance Ltd

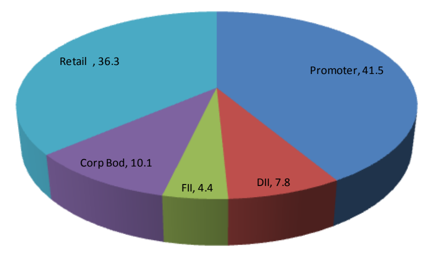
BUY

BSE Code	511676
NSE Code	GICHSGFIN
Bloomberg Code	GICHF:IN
Current Price	156
Target Price	238
Mcap ₹ Mn	8405.3
Mcap US$ Mn	137.8
52 wk H/L	181/93
Face Value	10
2 wk avg vol (000)	168

Financial Snapshot

₹ mn	FY14	FY15E	FY16E
NII	1,897	2,178	2,505
% ch	15.5	14.8	15.0
PBDT	1,601	1,811	2,097
%ch	12.7	13.2	15.7
PAT	976	1,113	1,281
%ch	14.7	14.1	15.1
EPS	18.1	20.7	23.8
BV	113.3	126.1	140.9
P/E	8.6	7.6	6.6
P/BV	1.38	1.24	1.11

Shareholding Pattern



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Growth momentum to revive, attractively valued

GIC Housing finance ltd (GIC HF) was promoted by a few public sector general insurance companies. It has predominantly focused on small ticket loans in the suburbs of Mumbai city largely focused on the retail side. In view of this it has been a slow performer over the past and lagged behind many of its peers in terms of its outstanding loans and profitability growth. This tardy pace of growth has made the markets value the company at much lower valuations than most of the other peers in the industry. The management is now looking to grow its loan book more aggressively and has increased its geographic spread through multiple branches which is expected to continue to grow. Further they have already started diversifying their loan book from retail housing finance to LAP and is now looking at financing some real-estate projects. As the book diversification occurs the profitability too will increase at an even higher pace.

Loan book growth momentum to increase: GIC HF has historically focused on housing loans to retail consumers. The focus of the company has been largely restricted to the suburbs of Mumbai city which contribute to 65% of its current loans. Given these constraints the growth of assets has been restricted to 17% over the past couple years. Further there has been loss of loan book to the large nationalized banks who have been offering housing loans at extremely low rates. This double whammy will reduce as banks move out of the housing finance space when corporate loan demand revives.

Diversification of loan portfolio to be margin accretive: GIC HF has been focused on retail housing loans it has recently started Loan against property (LAP) which now composes 10% of its overall loan book. The plan is to increase this portfolio as it generates higher revenues than a housing loan, further the management has guided they would look at loans towards real-estate projects. With both books expected to grow we believe the overall margins too will increase along with the growth in loan book from diversification.

Focus on controlling cost of fund to drive profitability: Cost of funds has been a real concern over the past couple years, bank borrowing has become extremely expensive with the RBI increasing its benchmark rates. During this period the management has raised some short term funds to counter the high long term funding. It has also looked at raising some funds through ECB which could be the future steps as the INR seems to have finally stabilized.

Stable asset quality: Housing loans are relatively safe as this is the last place a default were to be made, further the collateral of the property acts as a natural defense. These factors have ensured a stable asset quality with gross and net NPA's at 1.6% and 0% respectively. We believe they would be able to keep a stable asset quality going forward as well. This aside they provisions created above the required level will act as a buffer which could mean lower provisioning requirement going forward driving profitability.

Valuations: At present GIC HF is trading at a P/E of 7.6x and 6.6x and a P/BV of 1.2x and 1.1x its FY15E and FY16E earnings respectively. This is a significant discount to most peers in the housing finance space. We believe the loan growth would increase from the present 17% to 25% over the next couple years which in turn will drive profitability. A 10x P/E for FY16E is justifiable, with this we arrive at a target price of ₹237 and hence initiate coverage on GIC HF with a BUY recommendation with an upside of 52% from the current levels.

Loan Book Momentum to revive

Over the past couple years GIC HF has been able to grow its loan book but the growth has been rather mediocre to speak of. Although they have been able to attract enough business they have been losing business to banks who are offering funding to the housing sector at extremely low rates. The real struggle for GIC HF over the past couple years has been this ability to grow its loan book given the stiff competition that has been present in the housing finance space. With the RBI removing any pre payment loads many existing customers have been looking to refinance their loans at more competitive rates being offered by these banks. GIC disbursed a gross amount of ₹16.6bn during FY14, which is good given the current loan book size. However the average AUM increased by only ₹7.7bn to 53.1bn as a few clients moved out to more competitive funding offered by banks.

Property price correction & interest rate reduction to shore up demand for housing: Demand for houses at present continues to persist at lower levels as real estate prices continue to remain at high levels. Interest cost too has increased which increases the EMI payments for the borrower making it difficult for them to buy properties. Both these are acting as deterrents to new home owners. We believe real estate prices will probably correct by 10 to 15% over the next few quarters as supply would increase. This would get some prospective buyers to convert seriously. The interest rates too we believe have peaked and would probably move down after a couple quarters. Both these would bode well for GIC HF by increasing demand for housing which would drive the loan book growth.

Government investment plans to boost demand for loans: The new government has embarked on some large plans to develop 100 cities which would lead to more housing projects. The government has plans to attempt that every citizen in India should have a house, for this they would be taking up many low income housing projects. These too would require funding over the next few years. All of these factors put together will have a significant impact on demand for housing loans.

Banks shifting focus to other sectors to reduce competition: On the supply side too we believe competition will reduce marginally over time. As mentioned banks have become rather aggressive on pricing of home loans over the past couple years. The reason for this has been almost no safe credit demand coming from industry or from the infrastructure side. Banks are constantly looking to increase their loan assets and housing having one of the safest collaterals, the property makes it a very safe avenue for growth. However this trend we believe will reverse as banks will move back to funding infrastructure and corporate, where they are able to charge higher rates of interest enabling them to earn higher returns. Further housing loans are much smaller in nature which increase the cost of generating business for the bank while corporate loans are much larger which bodes well for banks who have large funds at their disposal. Although this could be a couple quarters down the line we believe all these factors will bode well for GIC HF who would be able to show higher disbursement growth going forward.

Increasing reach towards customers:

Branch Expansion: GIC HF has been very focused on the Mumbai markets with almost 63% of loans being sanctioned in the suburbs of Mumbai. Although this is a lucrative market this has restricted growth as competition too is highest in the region. It has over the past couple years increased its spread into different geographies of India with new branch expansions. At present they have 47 full-fledged branches and smaller collection centers in the metro's and tier 1 and tier 2 cities. They plan on increasing their braches by another 6-7 during the current financial year. Although branch expansion does not mean new business immediately it would over time help brand building and the reach would definitely help get more business over time.

Direct selling agent tie ups: Having limited reach throughout the country it is not easy for them to generate business by themselves through branch expansion alone. This can be time consuming and increases fixed costs for the company. To ensure a steady growth in loan books GIC HF has entered into agreements with a few large direct selling agents. These agents would bring customers from various regions. This would allow them to ensure sufficient work for the new branches as well.

New product offering to aid loan book growth:

Developer loans book to grow: GIC HF is also looking to diversify its asset book from only looking at housing finance to getting into real-estate project financing, although this is a little riskier in nature with strong guidelines in place this would open up a good market to tap. Real-estate financing usually generates a much higher yields which would help them increase spreads going forward. There would be a very limited exposure to this segment in the near term. At the end of FY14 the non individual loan book stands at only 0.2% of total disbursements which we could see gradually increasing to 4-5% of the total loans.

Loans against Property: The LAP business too has seen many players enter the fray and this has caused yields to decline in the division. However even post this competition the yields are still higher than that for housing finance. At present 10% of the total loans are towards the LAP business which will increase as the overall loan book grows and we could see this component move up higher to 12-15% of the overall book.

Insurance covers clubbed with loans a benefit for both parties: Housing loans has become commoditized and this has led to a big jump in the players and competition within the industry. In an attempt differentiate itself and give additional benefits to draw customers to avail funding from them GIC which provides a little something else to them. The two products offered free of cost are a personal accident cover (death only) free of cost to the borrower for the value of the loan availed. This acts as a protection for GIC HF as well in case of untimely death of the client. They also provide property insurance to the value of the loan outstanding against fire and other natural disasters. Both of these protect not only the customer but also the GIC to a large extent. Although these would add to the cost for GIC these differentiating factors would appeal to borrowers as insurance is something most people look at acquiring.

Cheaper sources of funds to help spreads further:

GIC has been unable to compete with many of the public sector banks in the recent times as the housing loans offered by them are close to the base rates of most banks. This means their borrowing rates are similar to those being offered to customers by banks. With this we have seen a drastic shift with many new borrowers looking at banks since rates are lower. This apart many of the existing customers too are attempting to get their loans refinanced by these public sector banks. To be able to compete with banks GIC HF along with many other players in the markets are looking for alternate sources of funds. NCD and bonds have become the best option for them and they would look to increase their borrowing from these alternate channels where funding can be done at a discount to most bank base rates. Although the difference in the cost of funds is small it makes it able to compete at some levels and allows them to increase their interest spreads. At present borrowing from these sources is about 10.4% we believe this too could be increased closer to 20% over the next couple years as demand for these products would see an uptick going forward as interest rates start declining.

Stable asset quality:

The banking and NBFC space over the past few years have seen a lot of asset quality deterioration. GIC HF however has property as collateral which we consider one of the most secure forms of collateral. Even in a case of default the probability of recovery of funds is extremely high given the LTV are usually below the 75% level. GIC HF even during these difficult times has not seen any major deterioration in its asset quality with Gross NPA declining by 1.2% in value terms and by 29bps to 1.57% against 1.86% in the previous year. With the economy now showing signs of revival we would see them able to grow their loan book with limited defaults which would lead to even lower gross NPA going forward. The Net NPA level is 0% with the high provisioning that has been done by it over the past couple years.

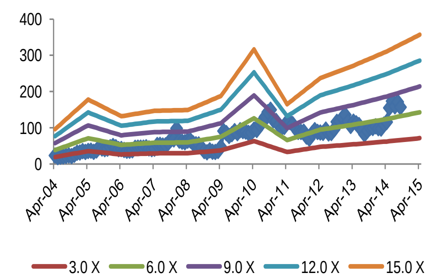
Maintain high provisioning:

GIC HF has been making large provisions over the past couple years. As per the management they have provided in excess of required by a total of ₹586mn. This will help keeping future provisions at lower levels which would help give a boost to profitability. The total provisioning now stands at 1.889bn of which 1.774bn is against housing loans. They have provided a sum of 99.2mn against investments. This would be the total long term investments of the company as they probably don't expect any fund recovery.

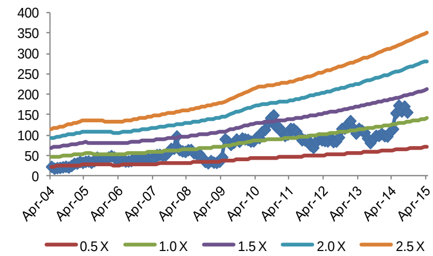
Capital adequacy at comfortable levels:

GIC CAR at the end of FY14E has increased to 17.26% from 14.04% over the previous year. They are well above the NHB prescribed limit of 12%. This would allow them to grow their profitability further before the need for capital arises. Based on our expectations for growth they may need to raise money only by end FY16E or early FY17E. This would allow them to grow their EPS at a steady pace over the next couple years.

Forward P/E



Forward P/BV



Valuations:

At present GIC HF is trading at a P/E of 7.6x and 6.6x and a P/BV of 1.2x and 1.1x its FY15E and FY16E earnings respectively. This is a significant discount to most other players in the housing finance space. The lower valuations are due to the strong concentration of loans to the city of Mumbai which currently exists. Further GIC HF has not been able to match growth rates of various other housing finance institutions in the space be it the market leader in the private space HDFC or the public sector such as LIC HF. Going forward too we believe the growth rates will be lower than some of its competitors as the reach of GIC will still remain much smaller than that of the other institutions mentioned. In View of this we believe the stock would continue to trade at some discount to these players. However at present we believe the discount is rather large closer to 50% and we believe this discount will rationalize. Further GIC HF has a relatively smaller book and once growth returns with increased demand and supply reduces from banks we believe the growth rates would see a good increase. Taking all these into consideration we believe a 10x P/E for FY16E is justifiable, with this we arrive at a target price of ₹237 and hence initiate coverage on GIC HF with a BUY recommendation with an upside of 52% from the current levels. At this price the stock would trade at a P/BV of 1.7x its FY16E which would be a fair valuation multiple.

Risks

Delayed recovery in economy keeping completion stiff in housing finance:

As discussed banks have entered the space with great vigor which has led to reduction in rates which in turn have affected profitability. We believe the revival in the economy will see banks reduce dependence on this sector and will focus on other sectors where they are able to earn higher margins. Our assumptions include this happening by early FY16E and hence if the economic revival takes longer then it could lead to a lower growth in its loan book than presently expected

Liquidity reduction in debt markets:

With Mutual funds and insurance companies having to invest in debt products there has been a good market for NCD's and bonds respectively. With this many institutions have been able to lower their borrowing costs as these bonds are presently prices 75bps to 100bps below the bank benchmark rates. If this money to these institutions were to get lowered we could see the demand for such bonds lowered pushing interest rates up. This could negatively affect earnings as spreads could come under pressure.

Increase in defaults:

Although we do not see this happening as the last thing a person defaults on is his property asset. However in case the economy turns for the worse and we see another round of job cuts which lead to defaults this would bode negatively to earnings. Although even this would not have a major impact as they would get most of their funds recovered as the LTV are low and the property collateral would ensure full recovery, it would negatively impact earnings as they would not be able to earn interest on loans disbursed but would have to provide for interest expenses on all loans borrowed.

Financials

Profit & Loss

In Rs million	FY13	FY14E	FY15E	FY16E
Interest Income	5,375	6,090	6,976	8,248
YoY (%)	26.9	13.3	14.6	18.2
Interest Expenses	3,732	4,193	4,798	5,743
YoY (%)	19.9	12.3	14.4	19.7
NII	1,642	1,897	2,178	2,505
YoY (%)	46.4	15.5	14.8	15.0
Other Income	164	160	138	131
Total Income	1,807	2,057	2,316	2,637
Operating Expenses	386	456	504	540
Employee Expenses	128	139	155	163
Establishment Expenses	258	317	349	377
PBDIT	1,421	1,601	1,811	2,097
Depreciation	21	21	24	28
Provisions & contigencies	269	248	263	313
PBT	1,130	1,333	1,524	1,755
Tax Expenses	280	357	412	474
PAT	850	976	1,113	1,281
Exceptional Items	0	0	0	0
Net Profit	850	976	1,113	1,281
YoY (%)	44.0	14.7	14.1	15.1

Balance Sheet

In Rs million	FY13	FY14E	FY15E	FY16E
Equity capital	539	539	539	539
Reserves	4,969	5,566	6,257	7,053
Net worth	5,507	6,105	6,796	7,591
Total borrowings	39,728	46,518	53,063	67,174
Other non current Liabilitie	1,639.8	1,889.1	2,151.8	2,464.9
Current Liabilities	638	670	732	800
Total Liabilities	**47,513**	**55,181**	**62,742**	**78,030**
Fixed Assets	64	52	48	50
C WIP	0	0	10	10
Housing loans	45,392	53,126	61,095	76,369
Investments	99	99	99	99
Deffered Tax	516	604	604	604
Non Current assets	141	250	264	281
Curent Assets	1,301	1,050	622	617
Total Assets	**47,513.3**	**55,181.2**	**62,742.3**	**78,029.7**

Key Ratios	FY13	FY14E	FY15E	FY16E
EPS (Rs)	15.8	18.1	20.7	23.8
CEPS (Rs)	14.5	16.9	21.1	24.3
Book value (Rs)	102.2	113.3	126.1	140.9
DPS (Rs)	5.0	6.0	6.5	7.5
Leverage	7.2	7.6	7.8	8.8
ROE	15.4	16.0	16.4	16.9

Valuations	FY13	FY14E	FY15E	FY16E
PE (x)	9.9	8.6	7.6	6.6
Cash PE (x)	10.8	9.3	7.4	6.4
Price/book value (x)	1.5	1.4	1.2	1.1
Dividend Yield	3.2	3.8	4.2	4.8
Dividend Payout ratio	31.7	33.1	31.5	31.5

Disclosures

The information provided in the document is from publicly available data and other sources, which we believe are reliable. It also includes analysis and views expressed by our research team.

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