Dimensional Securities Pvt Ltd.

Indiabulls Housing Finance Ltd.

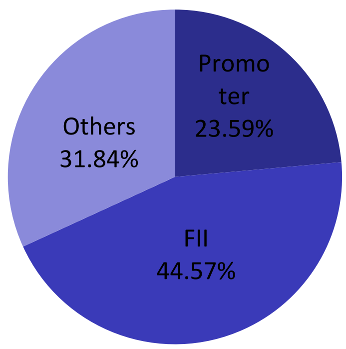
Initiating Coverage Report

Date: 8th Jan, 2016	
Recommendation:	HOLD
CMP:	716
Target Price:	729

MARKET DATA	
NSE TICKER	IBULHSGFIN
Net worth (₹ Cr) (FY16E)	11,539
P/BV Ratio (FY16E) (x)	2.6
EPS (FY16E) (₹)	53
Market Price (₹)	716
P / E Ratio (FY16E) (x)	13.6
52 Week High (10/08/2015)(₹)	820
52 Week Low (13/01/2015) (₹)	488
Market Capitalisation (₹ Cr)	30,172

AVERAGE MONTHLY VOLUME ('000)	
BSE	53.6
NSE	964.2

SHAREHOLDING PATTERN



RETURN	3M	6M	12M
IBHFL	-9%	9%	44%
Sensex	-8%	-12%	-8%

Vishal Rampuria
(Director, Research)
vishal.rampuria@dimensional.in
+91-22-66545256
Siddhesh Mhatre
(Research Analyst)
siddhesh.mhatre@dimensional.in
+91-22-66545284

Indiabulls Housing (IBHFL) is the 4th largest HFC player with loan book of ₹582 bn as on Q2FY16. With 220 branches spread across 18 states, the company has grown at a CAGR of 20% and delivered strong return ratios.

Loan book composition to support NIMs going forward

With high share of LAP (26%) and corporate credit (22%), IBHFL has been able to report higher NIMs than that of peers. Going forward, NIM will remain stable despite contraction in yields as cost of funds is likely to move south where the benefit would have to be passed due to increasing competitive pressures. AUM is geographically diversified with western & northern India being the key regions. Loan asset has swelled at a CAGR of 21% over FY 13-15 compared to industry growth of 19%. Industry dynamics like low penetration, government "Housing for All" etc. would support growth of 15-18% over the next 5 years. We expect the company to continue to grow faster at 18-20% due to better service quality, innovative products and increase in branches.

Healthy asset quality, despite higher percentage of risky assets

Despite high share of LAP and corporate credit, IBHFL has maintained strong asset quality with Gross NPA at 0.85% in FY15. Our channel check suggests that the company lays huge emphasis on recovery of loan. Processes like more emphasis on in-house sourcing of loan, accountability of the sourcing personal has helped in managing the asset quality. The company also has put innovative checks like financing where business has been in existence for more than 10 years,

Borrowing mix, rating upgrade help lower cost of borrowing

IBHFL has a well-diversified borrowing profile. Term loan constituted 51% of the total borrowings followed by bonds which stood at 29% and other short term financing 20%. With increasing size and consistent performance, the company rating was upgraded to AA+ by CRISIL. This along with higher share of money market instrument has helped in lowering borrowing costs and improving profitability.

Rise in competition from banks & HFCs; Risk of higher delinquency

Due to economic stress and slow revival in capex cycle, banks have been aggressively focusing on housing market as it has strong asset quality. In the short to medium term, this is expected to put pressure on spreads in home loan category. Also, the slow economic recovery may lead to increase in delinquency in the Non-Home loan portfolio. Overall, ability to maintain asset quality remains a key monitorable for us.

Financial Outlook & Valuation

The recent equity raising of INR 40bn at Rs. 702/share through QIP has further strengthened its B/S. We expect loan book to grow better than the industry at 22% CAGR (FY15-18E). As on H1FY16, IBHFL has capital adequacy ratio (CAR) of 21.6%. We build in lower profitability due to rising competition and slowdown in the economy. At CMP, the stock is trading at P/B multiple of 2.7x FY16E BV of 273 and 2.5x FY17E BV of Rs.297. We recommend a HOLD rating with a target of **₹729** valuing at 2.5x FY17E BV of Rs 282; after adjusting networth for investment in North Oak Bank (Rs 660 crs). Investment in North Oak Bank is valued at 1x its BV.

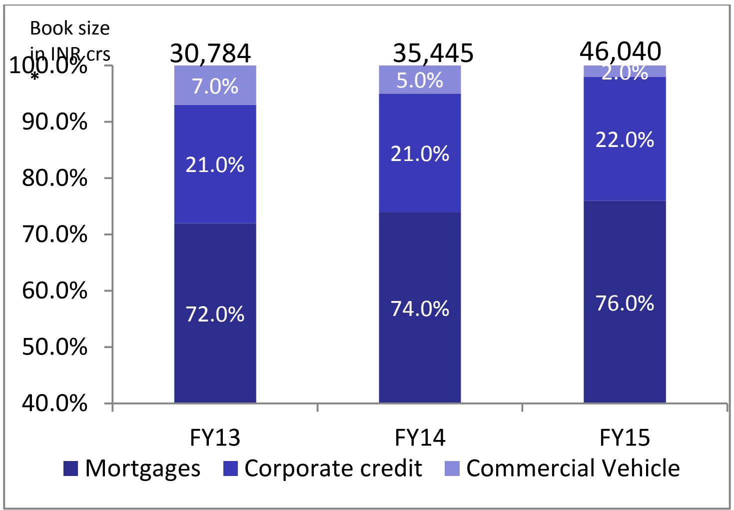
Financial Summary:

Rs. Cr	Net Interest Income	Total Income	Operating Profit before provisions	PAT	P/B (X)	P/E (X)	ROA	ROE
FY14	1,904	2,622	2,211	1,568	1.4	5.0	3.8%	29%
FY15	2,176	3,326	2,772	1,901	3.0	10.4	3.7%	31%
FY16E	2,860	4,333	3,675	2,218	2.7	14.0	3.5%	24%
FY17E	3,583	5,168	4,409	2,722	2.4	11.4	3.5%	23%
FY18E	4,040	5,731	4,887	3,010	2.2	10.3	3.2%	23%

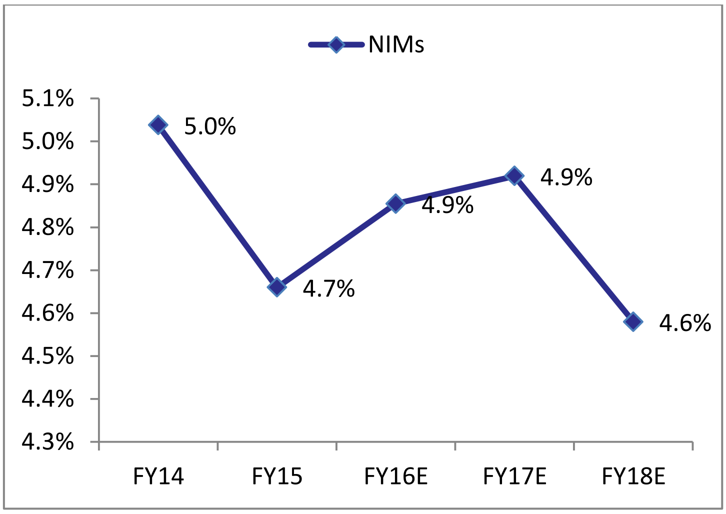
Loan book composition to support NIMs going forward

Higher share of LAP (26%) and corporate credit (22%) has acted as yield kicker whereas Housing loans (50%) has provided safety to IBHL loan book. Due to such composition, it has been able to maintain NIMs higher than that of peers. Network of over 220 branches that has grown at CAGR of 5% over FY13-15 and sourcing team of 2,300 members have helped IBHFL to grow loan book at CAGR of 21% over FY 13-15. CV book is on run down mode and we expect it to fully run down by FY 16E. We expect the composition of the loan book to remain at similar levels.

Loan book composition a key differentiator…



NIMs to remain stable over FY15-FY18E



* Including assigned loans

Home loans: IBHFL is focused on salaried class, first time home buyer with average ticket size of INR 2.4 mn in tier II and tier III cities. The segment's LTV is typically 71% at origination and is characterized by loan tenures of ~15 years. Home loan segment constitutes ~50% of the loan book. We expect home loan book to grow at CAGR of 16% over FY15-18E driven by low mortgage penetration in India (9% compared to 17-43% in Asian countries and around 80% in developed countries), government policy focus (housing for all by 2022, 100 smart city plan in next 5 years) coupled with wide distribution reach of over 220 branches and team of 2,300 sourcing members. AUM is geographically diversified with focus on western & northern regions in India.

AUM diversification geographically

North	30%
West	36%
Central	14%
South	20%

LAP: IBHFL has emerged as an important player in Loan against Property (LAP) segment. LAP book constitutes ~26% of the loan book with average ticket size of INR 6.8 mn. The company is focused on small businessman who is willing to mortgage self-occupied residential property to fulfill their business needs. The segment's LTV is typically 49% at origination and is characterized by loan tenures of ~7 years. Appraisal capabilities, established position and quality of service separate IBHFL from peers. We expect LAP book to grow at CAGR of 16% over FY15-18E.

Corporate Credit: Corporate credit accounts for ~22% of the loan book of which 75% comes from lease rental discounting (LRD) and the rest from construction finance. A) LRD: The Company is focused on multi-tenant properties where lease rentals are low at Rs. 50-60/sq ft/month with maximum lease rentals capped as a risk management strategy. Such strategy lowers the leasing risk. Construction finance: IBHFL provides finance to real estate developers against unsold inventory. Ticket size in this segment is ~INR 1 bn. The company generally finances a project which has received regulatory approvals and pre-sales have started.

Industry overview

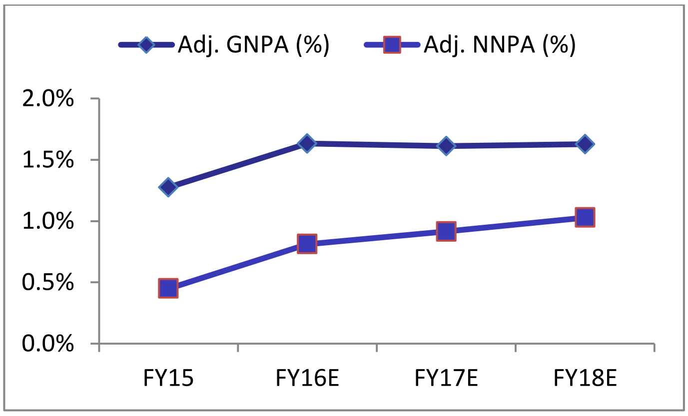
Housing finance industry has grown at health double digit growth in last five years. Though mortgage to GDP ratio in India (9%) remains very low compared to Asian peers where it is ranging from 17-43% and developed countries where it hovers around 80%. The industry is expected to grow at CAGR of 19% over FY15-20. Moreover, share of Housing Finance companies is expected to be around 39% by 2020 from 38% in FY15.

The Industry is expected to grow at CAGR of around 19% in the next five years. According to industry reports, AUM under LAP segment to more than double from 2.3 lakh crores as on March 2015 to 5 lakh crores by March 2019 driven by low mortgage penetration, government focus. Moreover, share of housing finance companies in the LAP segment is expected to be at 24% by FY19 from 22% as on FY15.

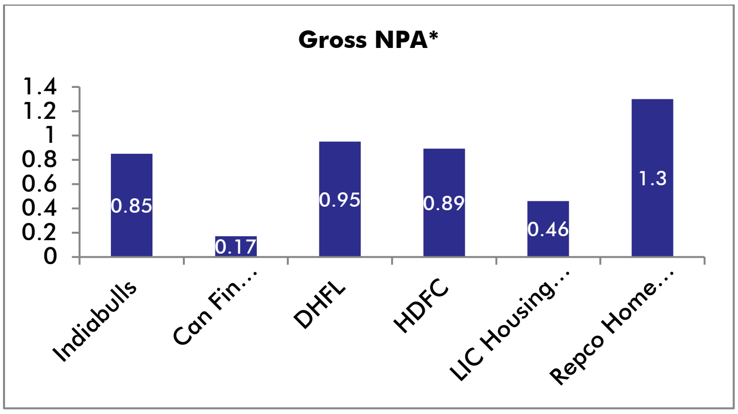
Healthy asset quality, despite high percentage of risky assets

IBHFL has been able to maintain healthy asset quality with Gross NPAs, on consolidated basis, at 0.85% in FY15. However, we expect asset quality to deteriorate going ahead due to slowdown in the real estate sector. The strength lies in risk mitigation processes like financing salaried first time buyer in home loan segment, against self-occupied property for business purpose in LAP segment, financing projects where all permissions are in place and pre-sales have taken place.

Asset quality to remain stable



Gross NPA for FY15 in line with peers



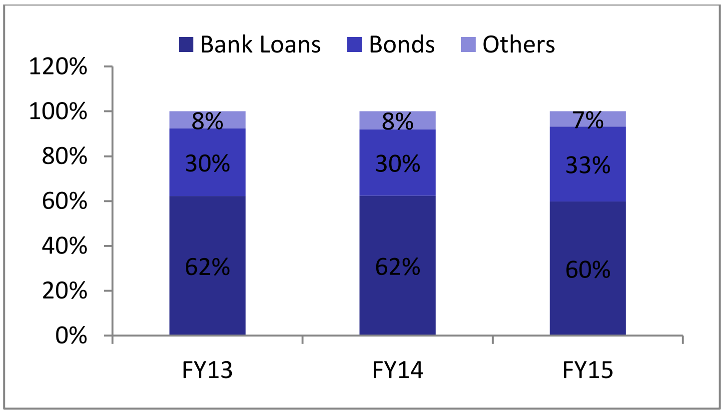
Note: Adjusted NPA= Gross NPA of current year / Loan book of year preceding previous year

**Reported NPA*

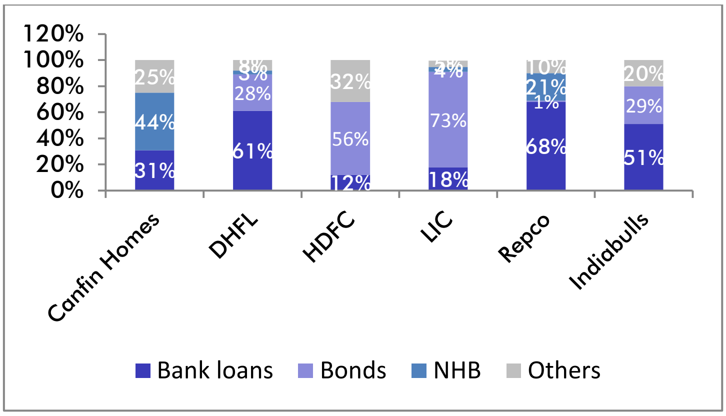
Borrowing mix, rating upgrade help lower cost of borrowing

Share of bank borrowings has come down from 62% in FY13 to 60% in FY15 but is still higher than larger and established peers like HDFC and LIC housing finance. Bank loans constituted 60% of the total borrowings followed by bonds (including ECB) which stood at 33% and other short term financing at 7% in FY15. Moreover, the company fully utilized the RBI approved external commercial borrowing (ECB) limit of USD 200 mn in FY 15 which resulted in reduction in the average cost of borrowing. The management has guided that 50% of the incremental borrowing would come from bonds. Going ahead, we expect fall in borrowing yield would offset fall in the lending yield.

Share of Bank Loans in borrowing profile declining



Borrowing mix moving towards larger peers



In the first half of FY 15, IBHFL was upgraded by all the rating agencies that rate the company. Its current rating stands as follows:

Rating agency	Rating
CARE	AAA
CRISIL	AA+
S&P	AA+
ICRA	AA+

Rating upgrade to help company in being more competitive

Well capitalized to grow above industry average

IBHFL is well capitalized with best capital adequacy ratio (CAR) of 18.4% amongst peers. Moreover, it has raised INR 4,000 crores at Rs. 702/share in September 2015 to strengthen its capital base. With such strong capital base, IBHFL is aptly placed to capture growth.

Moderate leverage and robust liquidity provides headroom for growth

IBHFL is moderately leveraged with leverage ratio of 5.7x net of cash and cash equivalent and short term investments. IBHFL enjoys robust liquidity with cash and cash equivalents constituting 16.8% of the total assets in FY 15. Moderate leverage and robust liquidity provides headroom for growth.

Key risks

Rise in competition

Banking industry has been facing asset quality issues especially in corporate loan segment. There has been a sharp rise in NPA's in last one year. This has made several banks to shift their focus to retail segment. We expect, housing finance with attractive growth potential and low risk will attract many banks and this will put pressure on profitability across the housing finance industry.

Slowdown in real estate sector

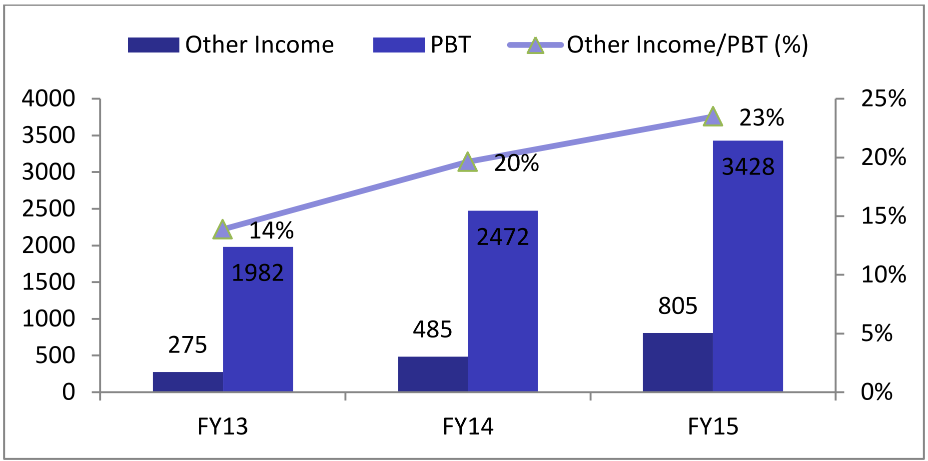
Real estate sector has witnessed slowdown post FY13. Large inventory (6.69 lacs) has remained unsold and it is expected to take more than 3 years to get rid of the same. Moreover, prices have come down across the country. IBHFL is exposed to vacancy risk especially in case construction financing segment and sustained slowdown could affect asset quality.

City	Unsold Inventory	Months
NCR	233,417	56
Mumbai Region	172,161	48
Bengaluru	101,168	35
Chennai	54,860	41
Pune	76,690	15
Hyderabad	31,008	24
Total	**669,304**	**37**

Earnings quality – monitorable

Proportion of other income to profit before tax has risen in from 16.7% in FY 13 to 35.9% in FY15. Increase in other income indicates deterioration in the quality of earnings, is a cause of concern and key monitorable going ahead.

Deterioration in quality of earnings red flag…



Opex cost efficiency

Opex to loan book has improved from 1.3% in FY13 to 1.2% in FY15 indicating strong control over costs and efficient utilization of resources. We expect opex to loan book ratio to reach 1% for FY18E.

Financial Outlook

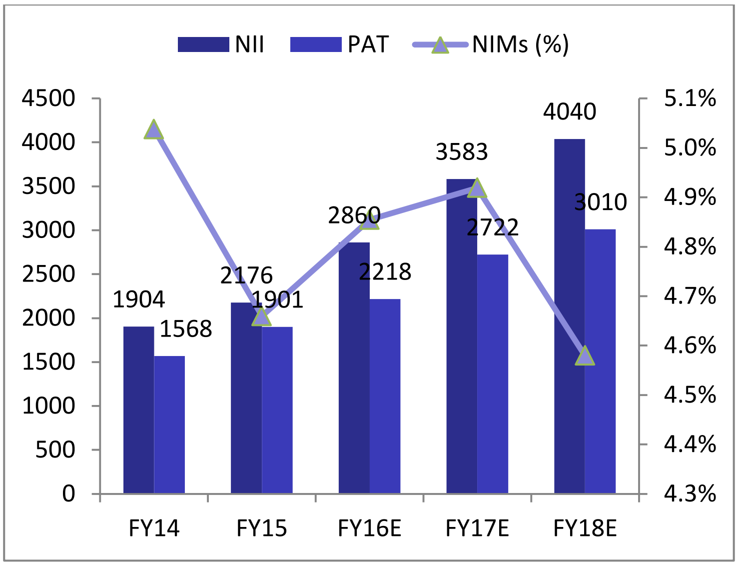
Loan Book expected to grow 21%; ROA and ROE to contract

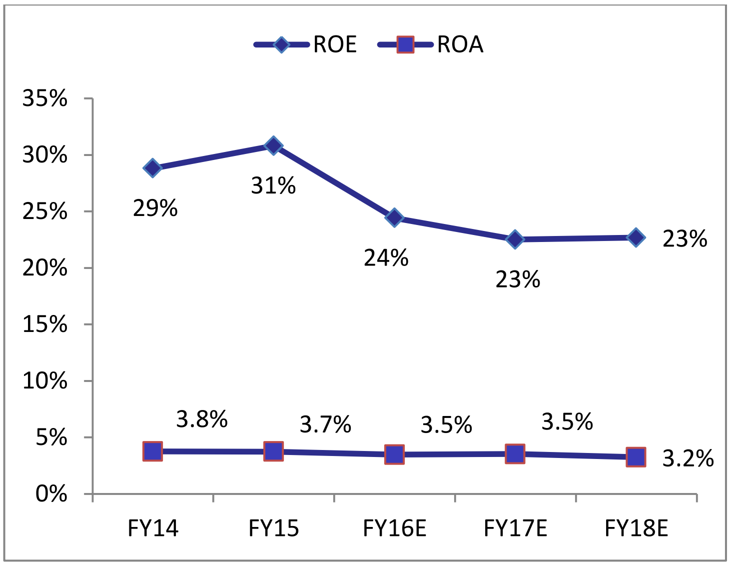
We expect loan book to grow better than industry at 21% CAGR (FY15-18E) and NIMs to remain stable. Backed by operating performance, we expect RoA and RoE to contract towards 2.8% and 18.9% by FY18E.

ROA Tree Analysis

DESCRIPTION	FY14	FY15	FY16E	FY17E	FY18E
Interest income	12.0%	12.6%	12.2%	11.8%	11.5%
Interest Expenses	8.2%	8.4%	8.0%	7.5%	7.6%
Net Interest Income	4.7%	4.7%	4.9%	4.9%	4.6%
Non - Interest Income	0.6%	0.7%	0.7%	0.7%	0.6%
NII + Non Interest Income	5.3%	5.4%	5.5%	5.6%	5.2%
Operating expenses	1.0%	1.2%	1.1%	1.0%	1.0%
Employee	0.7%	0.7%	0.6%	0.5%	0.5%
Others	0.4%	0.5%	0.5%	0.5%	0.5%
Operating Profit before Provisions	5.5%	5.9%	6.2%	6.1%	5.5%
Provisions	0.6%	0.6%	0.4%	0.3%	0.3%
Other Income	1.2%	1.7%	1.8%	1.5%	1.3%
PBT	4.9%	5.3%	5.8%	5.8%	5.3%
Provision for Tax	1.0%	1.2%	2.1%	2.0%	1.9%
Profit After Tax/RoA	3.9%	4.1%	3.8%	3.7%	3.4%
Average assets/Average equity	7	8	6	6	7
RoE	28.8%	30.8%	24.4%	22.5%	22.7%
Total Loan Assets	41,171	52,234	65,605	80,059	96,373
Average Assets	40,156	46,703	58,920	72,832	88,216

Key Profitability Charts





Outlook & Valuation

Stock has seen significant re-rating in last twelve months discounting its robust fundamentals which limit the upside from the current price level. However, since the company has a high dividend payout ratio (~50%), its net worth gets reduced which is not captured in the stock price.

We expect loan book to grow better than the industry at 22% CAGR (FY15-18E). However, we expect RoA and RoE to contract towards 3.2% and 23% by FY18E due to rise in competition and slowdown in real estate sector.

At CMP, the stock is trading at P/B multiple of 2.7x FY16E BV of 273 and 2.5x FY17E BV of Rs.297. We recommend a HOLD rating with a target of ₹729 valuing at 2.5x FY17E BV of Rs 282; after adjusting networth for investment in North Oak Bank (Rs 660 crs). Investment in North Oak Bank is valued at 1x its BV.

Peer Comparison as on Q2FY16

Particulars	Loan book	Market Cap	Net worth	ROA	ROE	TTM P/E	TTM P/B
Indiabulls Housing Finance Ltd	58,224	33,193	10,205	3.7%	21.0%	15.8	3.2
Canfin Homes Ltd	9,303	2,427	829	1.2%*	11.0%*	20.9	2.9
DHFL	56,312	6,419	4,888	1.60%	18.7%	9.5	1.3
HDFC Ltd	267,116	186,259	60,534**	2.7%*	21.6%*	20.4	3.2**
LIC Housing Finance Ltd	114,069	23,729	8,612	1.50%	19.3%	17.0	3.0
Repco Home Finance Ltd	6,849	4,581	886	2.20%	16.10%	33.0	5.2

Source – Ace Equity
*Note - *ROA & ROE – For FY15*
*Note - **Networth & P/BV -after adjusting for investments in Gruh Finance & HDFC Bank*

CAGR & Average of 3 years

Average	Last year	Last 3 years
Provisions / Total Income (%)	9.03%	8.04%
Tax Rate (%)	23.12%	22.49%
NIM (%)	4.66%	4.84%
ROA (%)	3.74%	3.58%
ROE (%)	30.80%	28.55%
P/E (x)	10.4	NA
P/B (x)	2.99	NA
Dividend Yield (%)	4.59%	NA
GNPAs (%)	1.33%	1.07%
NNPAs (%)	0.30%	0.33%
Cost Income Ratio (%)	16.64%	16.90%
Advances growth (%)	29.89%	22.16%

CAGR Ratio (%)	Last Year	Last 2 Years
Interest Earned	18%	20%
Other Income	66%	71%
Total Income	27%	24%
Profit Before Tax	25%	22%
Profit After Tax	21%	23%
EPS	14%	15%
Book Value	9%	6%
Net NPAs	8%	17%

Company Description

Headquartered in New Delhi, Indiabulls Housing Finance Limited (IBHFL) was founded in 2005 as a subsidiary of Indiabulls Financial Services Limited (IBFSL). IBFSL reverse merged with IBHFl in 2012. IBHFL has 220 branches spread across 18 states, grown at CAGR of 5% over FY13-15 and two representative offices in Dubai and London. The reverse merged entity is regulated by NHB. IBHFL is engaged in providing mortgage i.e. housing loans, loan again property and commercial credit which contributes ~ 50%, 26% and 24% respectively to the loan book. CV book, constitutes ~2% of the loan book in FY15, is on run down mode.

Management

The Indiabulls group has undergone restructuring. Two founder promoters viz. Mr. Rajiv Ratten and Mr. Saurabh Mittal have separated from IHFL. Mr Sameer Gehlaut, founder promoter continues to control housing business. Mr Gagan Banga has been promoted to the post of MD&VC and now heads all operations.

Name	Designation	Profile
Gagan Banga	VC and MD	A management graduate, worked with NIIT before joining Indiabulls group. Associated with group for more than 15 years and is instrumental in driving firm's growth
Ajit Mittal	ED and Compliance Head	A seasoned banker with experience of more than 20 years with RBI and Qatar Bank. Holds Masters in Economics and MBA from University of Illinois, US
Ashwini Omprakash Kumar	DMD	Worked with HDFC for over 10 years; holds a B.Tech from IIT Roorkee and MBA from JBIMS, Mumbai
Sachin Chaudhary	Business Head – Mortgages	Worked with GE Money and ICICI Bank

Corporate Governance

The Board consists of eleven members out of them six (55%) are independent directors which is in compliance with the SEBI regulations. IBHFL appointed four independent directors on its board during FY15. Two of them are retired justice, Supreme Court of India, retired deputy governor RBI and ex-army official. The attendance of the board members has been reasonable in the board meetings held during FY15.

Name	Designation	Profile
Dr. K.C. Chakrabarty	Non-Executive Independent Director	Former deputy governor of the RBI; Holds a doctorate in statistics from Banaras Hindu University
Brig. Labh Singh Sitara	Non-Executive Independent Director	Ex-army official
Samsher Singh Ahlawat	Non-Executive Independent Director	A seasoned banker with more than 20 years of experience. Hi is the Chairman of the Audit Committee
Prem Prakash Mirdha	Non-Executive Independent Director	Expert in SME sector
Justice Surinder Singh Nijjar	Non-Executive Independent Director	Retired justice, Supreme Court of India
Justice Bisheshwar Prasad Singh	Non-Executive Independent Director	Retired justice, Supreme Court of India

Financial outlook

Profit & Loss Statement

DESCRIPTION Rs. Cr	FY14	FY15	FY16E	FY17E	FY18E
INCOME :					
Interest income	5,187	6,120	7,582	9,071	10,730
Interest Expenses	3,282	3,944	4,722	5,488	6,690
Net Interest Income	1,904	2,176	2,860	3,583	4,040
Fees & Other operating Income	233	344	403	475	561
Other Income	485	805	1,070	1,110	1,130
Net Revenues	2,622	3,326	4,333	5,168	5,731
EXPENDITURE :					
Employee Expense	264	325	355	388	426
Depreciation	8	19	21	25	28
Other Opex	139	210	282	346	390
Operating Profit before Provisions	2,211	2,772	3,675	4,409	4,887
Provisions and Contingencies	230	300	248	202	235
PBT	1,982	2,472	3,428	4,207	4,652
Tax	413	571	1,210	1,485	1,642
Profit After Tax	1,568	1,901	2,218	2,722	3,010

Balance Sheet

DESCRIPTION	FY14	FY15	FY16E	FY17E	FY18E
EQUITY AND LIABILITIES					
Share Capital	67	71	87	87	87
Total Reserves	5,636	6,558	11,452	12,567	13,801
Shareholder's Funds	5,706	6,632	11,539	12,654	13,888
Borrowings	29,313	40,967	50,224	61,036	75,425
Other Liabilities	9,394	9,627	8,592	10,290	12,562
Total Liabilities	44,417	57,231	70,360	83,985	101,880
ASSETS					
Non-Current Assets					
Loans & Advances	35,580	46,473	57,221	68,591	83,068
Fixed Assets & Goodwill	115	123	130	139	149
Investments	2,947	6,164	7,589	8,689	9,137
Cash & Bank	4,419	3,490	6,471	6,793	7,132
Other Assets	1,355	982	1,032	1,161	1,344
Total Assets	44,417	57,231	70,360	83,985	101,880

Ratio Analysis

	FY14	FY15	FY16E	FY17E	FY18E
Operational Ratios (Rs.)					
EPS	47	53	53	65	72
Book Value	171	187	274	301	330
DPS	29	26	23	28	31
Spread Analysis					
Yield on Loans	14.5%	14.4%	13.9%	13.4%	13.1%
Cost of Borrowings	9.8%	9.5%	9.3%	9.1%	9.0%
Interest Spread	4.7%	4.9%	4.6%	4.4%	4.1%
NIM	5.0%	4.7%	4.9%	4.9%	4.6%
Profitability Ratios					
RoE	29%	31%	24%	23%	23%
RoA	3.8%	3.7%	3.5%	3.5%	3.2%
Adjusted ROA*	3.8%	3.7%	3.5%	3.5%	3.2%
Asset Quality ratios					
G.NPA %	0.8%	0.9%	1.0%	1.1%	1.1%
N.NPA %	0.4%	0.3%	0.5%	0.6%	0.7%
Efficiency Ratios					
Int. Exp./Int. Earn	63%	64%	62%	61%	62%
Op. Exp/Net Inc.	19%	22%	20%	19%	18%
Debt / Equity	5.1	6.2	4.4	4.8	5.4
Valuation Ratios					
P/E (x)	5.0	10.4	13.6	11.1	10.0
P/B (x)	1.4	3.0	2.6	2.4	2.2
Dividend Yield	12%	5%	3%	4%	4%

* adjusted ROA: PAT/Total loans including assigned loans

ANALYST CERTIFICATION

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