

Repc Home Finance (RHFL.NS)

India | Banks

HOLD

Smooth sailing ahead but valuation caps upside

REPCO has had a strong run since its IPO and is now trading at 3.9x forward P/B (vs. listing at 1.4x). We expect the company to grow faster than the industry on account of small size (loan book of Rs60bn), presence in less crowded markets and focus on high yielding self-employed segment. It enjoys a competitive advantage in loan sourcing and originates loans at a fraction of costs incurred by peers. We expect RoEs improvement driven by growth higher than RoEs, stable margins and positive operating leverage. However, current valuations appear fair and we Initiate with HOLD.

Price: INR706.00
Target: INR735.00
Forecast Total Return: 4.4%

Market Cap: INR44bn
Average daily volume: 140k

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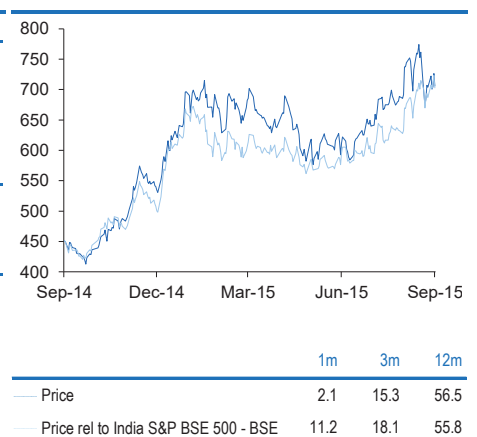
- **REPCO performance has been strong** – Repco’s loan book, disbursements, PAT has grown at a CAGR of 34%, 30% and 26% respectively from FY10-FY15. RoAs have been consistently sustained at 2.4%. The strong performance has led to stock re-rating from 1.4x to 3.9x forward BV.
- **REPCO operates in very different segments** – REPCO operates in Tier-II and Tier-III cities with a strong focus on the self-employed segment (57% of book). Also, the share of loans for self-construction is around 50% of book while peers concentrate mostly on funding for purchase of flats.
- **Growth rates to sustain at higher than industry growth** – Given the small size, focus on less penetrated market and comfortable incremental ticket size of around Rs1.6mn (in housing loans), we believe that the company could grow at faster than the industry rate. A higher loan book growth will improve the leverage and aid RoEs of the company.
- **Cost effective distribution model** – Repco has a cost effective home loan origination model through ‘loan melas’ (70% of origination) where the origination cost is a fraction of origination cost through other channels and versus peers.
- **Scalability could be an issue**– It remains primarily a Tamil Nadu based company (63% of loan book) with Karnataka (12.4%) the second largest state. We believe that scalability in other states could be an issue but current small size with market share at just 0.6% provides comfort to us.
- **Valuations leave little upside - Initiate at HOLD** – Repco is trading at 3.6x FY17E P/B and 22x FY17E EPS which makes this the most expensive HFC in our coverage. We like the business model of the company but would wait for better valuations to turn Buyers on the stock.

Financials and valuation

Year end: 31 March

Price Performance

	2014A	2015A	2016E	2017E	2018E
Total operating income (INRm)	2,106	2,613	3,168	3,756	4,469
Operating expenses (INRm)	388	547	692	819	962
Impairments (INRm)					
Exceptionals (INRm)	0	0	0	0	0
Profit before tax (reported) (INRm)	1,492	1,862	2,212	2,685	3,209
EPS (reported)	17.7	19.8	23.6	28.7	34.3
DPS (INR)	1.2	1.5	1.8	2.1	2.6
tNAV per share (INR)	119.2	139.0	165.4	197.3	235.4
PE (reported) (x)	39.8	35.7	29.9	24.6	20.6
Dividend yield (%)	0.2	0.2	0.3	0.3	0.4
Price/tNAV (x)	5.9	5.1	4.3	3.6	3.0
Return on equity (reported) (%)	0.3	0.2	0.2	0.2	0.2
Core tier 1 capital ratio (CRD IV "fully loaded") (%)	0.2	0.2	0.3	0.2	0.2
Loans:deposit ratio (%)	n.m.	n.m.	n.m.	n.m.	n.m.



Source: Company accounts/Investec Securities estimates

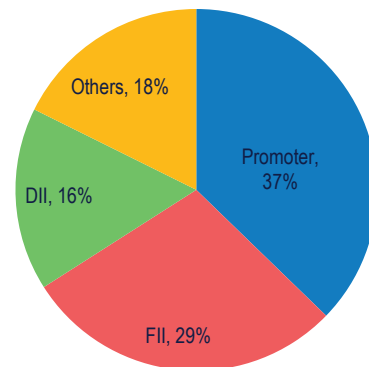
Source: FactSet

Figure 81: Company snapshot

Repro Home Finance is a housing finance company (HFC) operating in the low-middle income segment with a focus on the southern states of India. The company was incorporated in 2000 as a 100% subsidiary of Repco Bank (The Repatriates Co-operative Finance and Development Bank) and started its operations as a Housing Finance Company (HFC) in 2002. In 2007, Carlyle Group picked up a stake in the company for Rs759m and currently holds 23.75% (50.02% is held by Repco Bank). Currently, the loan book of the company stands at Rs60bn with presence in eight states on India. Tamil Nadu continues to form 63% of the loan book of the company.

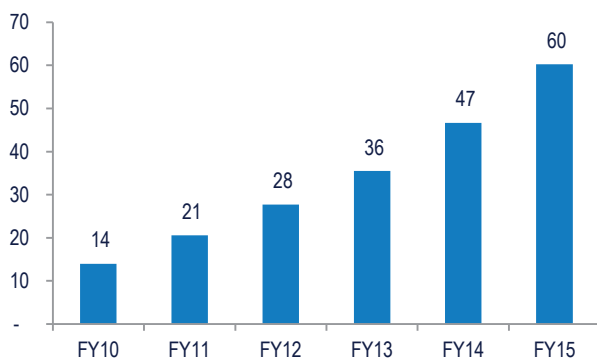
Source: Investec Securities Research, Company Data

Figure 82: Shareholding pattern (June'15)



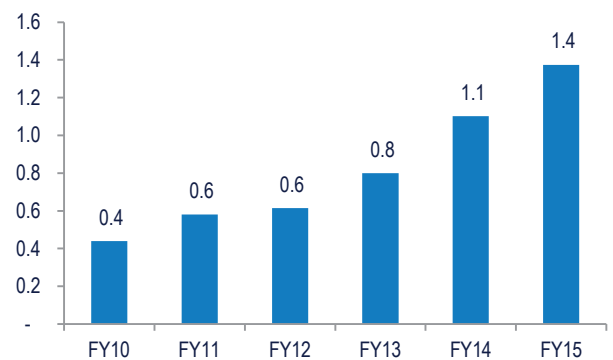
Source: Investec Securities Research, Company Data

Figure 83: Loan book – 34% CAGR over last five years (Rs Bn)



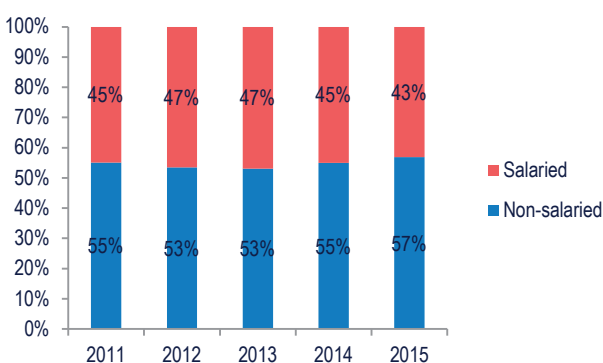
Source: Investec Securities Research, Company Data

Figure 84: PAT CAGR of 26% over last five years (Rs Bn)



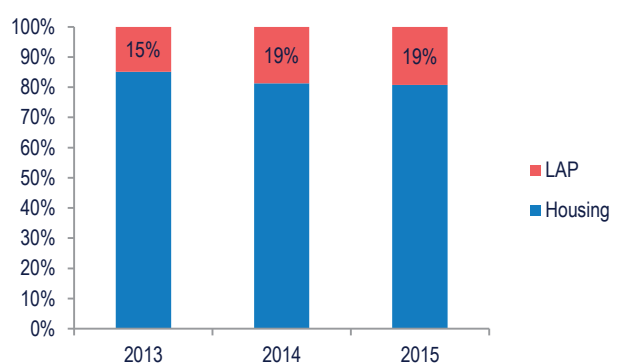
Source: Investec Securities Research, Company Data

Figure 85: High share of salaried customers



Source: Investec Securities Research, Company Data

Figure 86: Increasing share of LAP in loan book



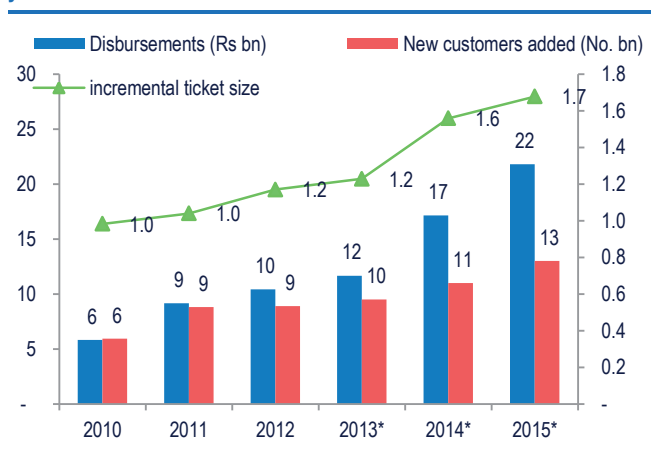
Source: Investec Securities Research, Company Data

RoE improvement may be slower than expectations

We believe that RoE improvement for the company may be slower than what consensus is factoring in given

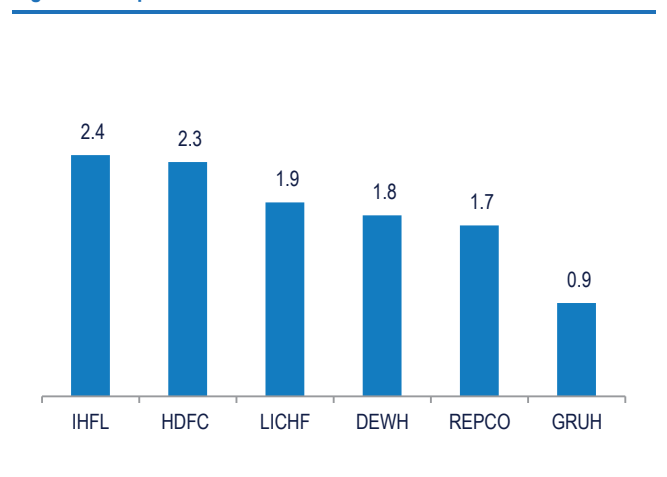
- **Loan book growth may slow down** – REPCO has high RoAs (2.6%) while ROEs are around 18%. The RoE improvement story is contingent on the company’s ability to grow its loan book at higher than RoE rate. The loan book has grown at 34% CAGR over last five years. We expect the rate to come down to less than 25% for next three years given –
- **Significant growth in the last five years has come from ticket size increases** on account of strong real estate price appreciation and construction costs inflation. Tamil Nadu accounts for more than 60% of its loan book.
- **Incrementally, the target segment of Repco is similar to LICHF and DEWH** – Our analysis suggests that the incremental ticket size of the company is closer to that of both LICHF and DEWH where the competition is high.
- **Margins may be under pressure** – In addition, decline in loan book growth trajectory, margins may also decline over the next three years given –
- **Yields may be under pressure** – Given the competition in the loan against property segment and incrementally company encroaching in the target segments of large HFCs, we expect some pressures on yields.
- **Cost of funding may not decline in line with market** – Around 20% of the funding is coming from NHB, and it has been declining over the last five years. We expect this to further decline as incrementally, the company is operating in a higher ticket size segment. NHB funding is low cost versus other source of funding and hence a decline in funding from NHB will mean that the costs of fund may remain high. However, the company is tapping bond markets which are 70bps lower than bank loans and a replacement of bank loan with bonds could help it in reducing funding costs.

Figure 87: Ticket size have increased by 13% CAGR over last 5 years



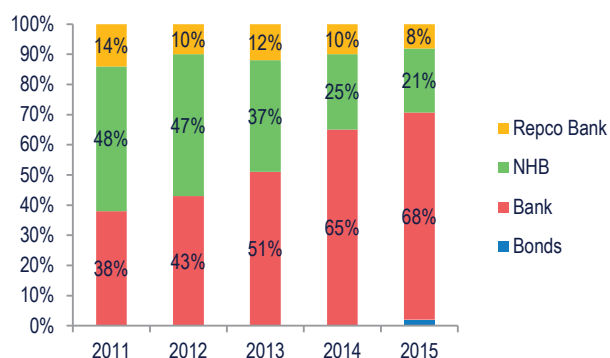
Source: Investec Securities Research, Company Data

Figure 88: Repco’s ticket size is similar to LICHF and DEWH



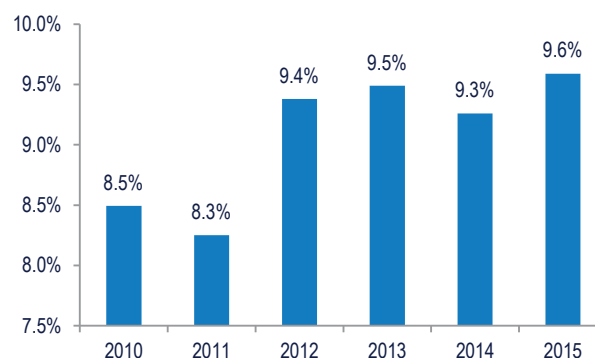
Source: Investec Securities Research, Company Data

Figure 89: Share of NHB funding is coming down...



Source: Investec Securities Research, Company Data

Figure 90: ...Leading to upward pressure on funding costs



Source: Investec Securities Research, Company Data

Table 55: Repco Home Finance – DuPont Analysis

DuPont	2011	2012	2013	2014	2015A	2016E	2017E	2018E
NII	4.7%	4.1%	3.7%	4.4%	4.4%	4.2%	3.9%	3.8%
Fee Income and Other	0.8%	0.7%	0.6%	0.6%	0.6%	0.4%	0.4%	0.4%
Total Income	5.5%	4.8%	4.3%	5.0%	4.9%	4.7%	4.4%	4.2%
Employee costs	0.4%	0.4%	0.4%	0.5%	0.6%	0.6%	0.6%	0.6%
Operating costs	0.3%	0.3%	0.3%	0.4%	0.3%	0.3%	0.3%	0.3%
Operating profit	4.8%	4.1%	3.6%	4.2%	3.9%	3.7%	3.5%	3.3%
Credit costs	0.2%	0.6%	0.3%	0.5%	0.4%	0.4%	0.3%	0.3%
PBT	4.6%	3.4%	3.3%	3.6%	3.6%	3.3%	3.2%	3.0%
PAT (before DTL)	3.3%	2.5%	2.4%	2.6%	2.6%	2.4%	2.3%	2.2%
RoE (before DTL)	26.3%	22.3%	17.1%	16.0%	17.1%	17.1%	17.4%	17.4%
Leverage (x)	8.0	8.8	7.0	6.1	6.6	7.2	7.6	8.0

Source: Investec Securities estimates

Table 56: Repco Home Finance – Valuation metrics

Valuation Metrics	2014	2015	2016E	2017E	2018E
P/E*	39.6	31.8	27.0	22.3	18.6
P/BV*	5.9	5.1	4.2	3.6	3.0
ROA	2.6%	2.6%	2.4%	2.3%	2.2%
ROE	16.0%	17.7%	18.2%	18.6%	18.8%
Dividend Yield	0.2%	0.2%	0.3%	0.3%	0.4%
BV	119	131	155	184	218
Diluted EPS (Rs)	18	20	24	29	34
Implied Valuation Ratios	2014	2015	2016E	2017E	2018E
P/E	41.5	33.3	28.3	23.3	19.5
P/BV	6.2	5.3	4.4	3.7	3.1

Source: Investec Securities estimates

Table 57: Repco Home finance - Financials

P&L Summary	2014	2015	2016E	2017E	2018E
Net Interest Income	1,861	2,310	2,868	3,391	4,026
Fee Income	186	231	300	366	443
Other Income	59	72	-	-	-
Total Income	2,106	2,613	3,168	3,756	4,469
Operating expenses	364	518	663	789	932
Operating Costs	153	183	226	266	310
Employee Costs	211	335	437	524	622
Pre Provisioning Profit	1,742	2,095	2,505	2,967	3,537
Provisions	226	203	264	253	298
Operating Profit	1,516	1,891	2,241	2,714	3,238
Depreciation	24	29	29	29	29
PBT	1,492	1,862	2,212	2,685	3,209
Less:Tax	390	489	597	725	866
PAT before DTL	1,101	1,373	1,615	1,960	2,342
DTL	-	142	146	177	212
PAT after DTL	1,101	1,231	1,469	1,783	2,131
Basic EPS (Rs)	18	20	24	29	34
Diluted EPS (Rs)	18	20	24	29	34
Dividend per share(Rs)	1.2	1.5	1.8	2.1	2.6

Balance Sheet Summary	2014	2015	2016E	2017E	2018E
Equity					
Reserves and Surplus					
Networth	7,411	8,121	9,607	11,411	13,566
Deferred tax liability	-	529	675	852	1,064
Borrowings	39,020	51,044	66,511	84,173	104,964
Total Sources of funds	46,431	59,694	76,793	96,436	119,595
Loan Book	46,682	60,229	76,653	96,119	119,066
Investments	124	124	124	124	124
Fixed Assets	50	89	89	89	89
Other Assets	187	-	-	-	-
Net working Capital	(612)	(748)	(748)	(748)	(748)
Total Application of funds	46,431	59,694	76,118	95,584	118,531

Source: Investec Securities estimates

Summary Financials (INRm)

Year end: 31 March

Income Statement	2014	2015	2016E	2017E	2018E
Net interest income	1,861	2,310	2,868	3,391	4,026
Other operating income	244	303	300	366	443
Total operating income	2,106	2,613	3,168	3,756	4,469
Net insurance claims	0	0	0	0	0
Net operating income pre impairments	1,718	2,065	2,476	2,938	3,507
Impairments					
Net operating income					
Expenses	388	547	692	819	962
Operating income					
JVs and associates	0	0	0	0	0
Profit before tax pre-exceptionals	1,492	1,862	2,212	2,685	3,209
Exceptionals	0	0	0	0	0
Profit before tax	1,492	1,862	2,212	2,685	3,209
Tax	390	631	743	902	1,078
Profit after tax	1,101	1,231	1,469	1,783	2,131
Minorities/Preference dividends					
Profit attributable	1,101	1,231	1,469	1,783	2,131
EPS (reported)	17.7	19.8	23.6	28.7	34.3
DPS (INR)	1.2	1.5	1.8	2.1	2.6
Average number of group shares (m)	62	62	62	62	62
Total number of shares in issue (m)	62	62	62	62	62
Balance sheet	2014	2015	2016E	2017E	2018E
Customer loans	46,682	60,229	76,653	96,119	119,066
Customer deposits	0	0	0	0	0
RWAs	13,605	18,380	24,883	30,247	42,695
Core tier 1 capital ratio (%)	0.2	0.2	0.3	0.2	0.2

Source: Company accounts, Investec Securities estimates

Target Price Basis

Excess return on equity

Key Risks

Real estate price correction; Competition; NHB funding may come down

Disclosures

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Stock ratings for European/Hong Kong stocks

	Expected total return		All stocks		Corporate stocks	
	12m performance	Count	% of total	Count	% of total	
Buy	greater than 10%	170	55%	80	47%	
Hold	0% to 10%	105	34%	15	14%	
Sell	less than 0%	32	10%	0	0%	

Source: Investec Securities estimates

Stock ratings for Indian stocks

	Expected total return		All stocks		Corporate stocks	
	12m performance	Count	% of total	Count	% of total	
Buy	greater than 15%	29	59%	0	0%	
Hold	5% to 15%	13	27%	0	0%	
Sell	less than 5%	7	14%	0	0%	

Source: Investec Securities estimates

Stock ratings for African* stocks

	Expected total return		All stocks		Corporate stocks	
	12m performance	Count	% of total	Count	% of total	
Buy	greater than 15%	30	45%	7	23%	
Hold	5% to 15%	19	28%	2	11%	
Sell	less than 5%	18	27%	2	11%	

Source: Investec Securities estimates

*For African countries excluding South Africa, ratings are based on the 12m implied US dollar expected total return (ETR). This is derived from the expected local currency (LCY) ETR by making assumptions on the 12month forward exchange rates for the respective currencies. For South African stocks, ratings are based on the ETR in rand terms.

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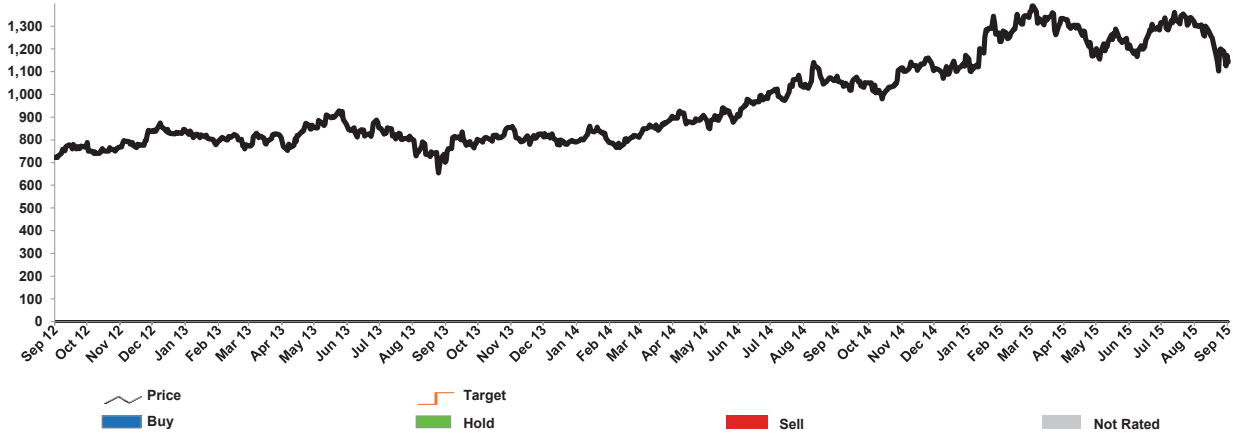
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Recommendation history (for the last 3 years to previous day's close)

Housing Development Finance Corporation (HDFC.NS) – Rating Plotter as at 07 Sep 2015



Source: Investec Securities / FactSet

LIC Housing Finance (LICH.NS) – Rating Plotter as at 07 Sep 2015



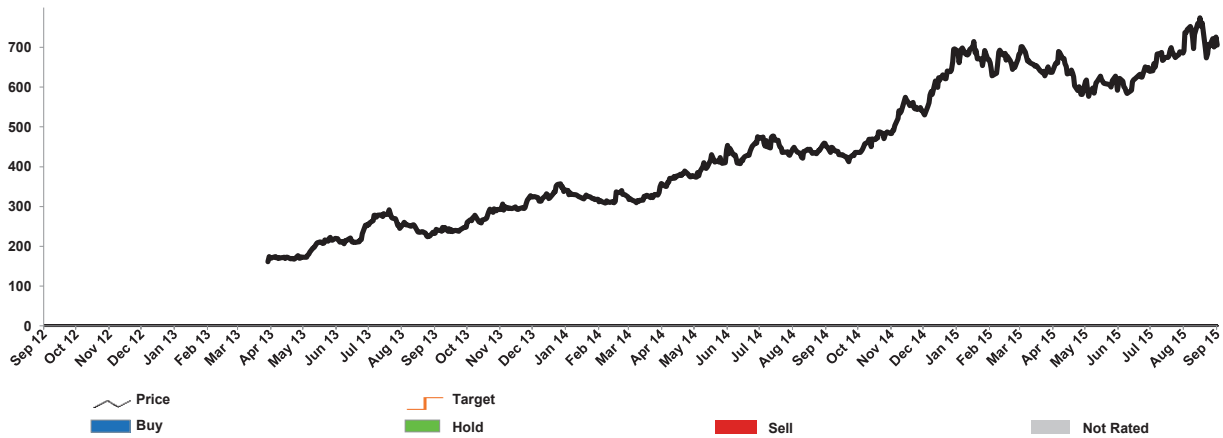
Source: Investec Securities / FactSet

Dewan Housing Finance Corporation (DWHN.NS) – Rating Plotter as at 07 Sep 2015



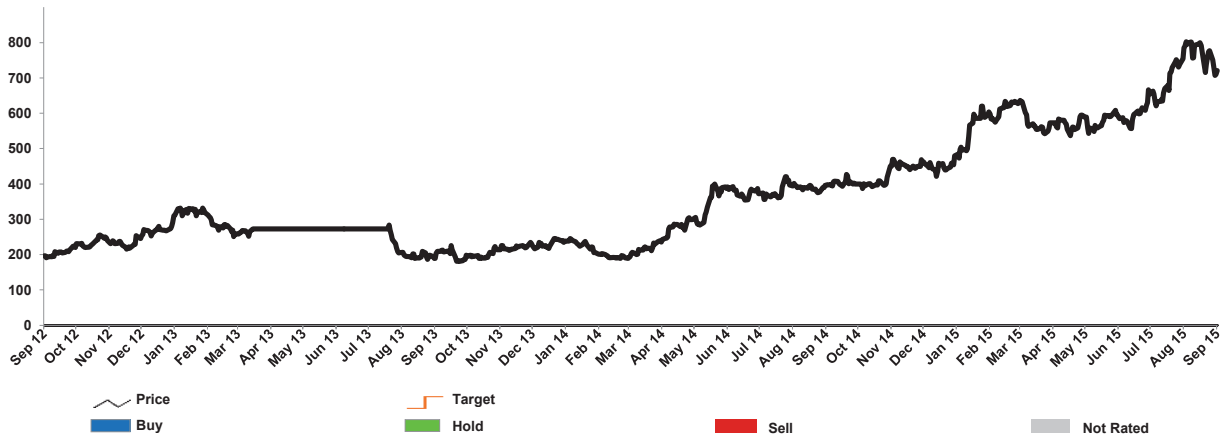
Source: Investec Securities / FactSet

Repro Home Finance (RHFL.NS) – Rating Plotter as at 07 Sep 2015



Source: Investec Securities / FactSet

Indiabulls Housing Finance (INBF.NS) – Rating Plotter as at 07 Sep 2015



Source: Investec Securities / FactSet

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