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FUNDAMENTAL PICK

LOW RISK / HIGH RETURN

HOLDING PERIOD – SIX MONTHS PLUS

LIC HOUSING FINANCE

Present Price – Rs.630.30

Projected Price – Rs.900 plus

LIC Housing Finance Ltd. (LICHF) is one of the largest housing finance companies in India. Almost 93% of the company's loans are to retail customers and the balance 7% to project developers. The promoter, namely LIC of India, meets 8% of the total fund requirements, whereas 80% is funded by term loans from banks, bonds and debentures, and the remaining 12% in the form of refinance from NHB and others.

Over the past two years, LICHF has been regaining its old glory by consistently gaining market share. Over FY02-07, LICHF lost market share to private banks as well as other housing finance companies owing to the following factors:

- a) Sharp drop in systemic and policy interest rates favoured the banks
- b) Aggressive entry of the private sector banks in the housing finance space
- c) Lack of proper processes and risk management systems for LICHF

Over FY04-06, LICHF put proper loan processing and risk assessment procedures in place and since then, has been gaining market share in the housing finance sector. LICHF is estimated to have improved its market share to 9% plus in FY09 from ~6% in FY08. After muted disbursements over FY05-07, LICHF has been gaining market share (due to internal restructuring) in the past two years, growing its disbursements by 38% in FY08 and 24% in FY09. Its focus on the salaried class (which forms 80% of its individual loan segment), and

particularly public sector entities (~50-60% of salaried class), has enabled to post better-than-industry growth; these segments have benefited from implementation of Sixth Pay Commission recommendations and no job losses.

Over the last two years, LICHF has invested immensely in the expansion of its distribution network. LICHF markets its home loans through three channels – home loan agents(HLS; includes LIC agents), direct sales agents (DSA) and customer relationship agents (CLA). Over the past two years, LICHF has almost doubled its distribution network, with major expansion coming from the home loan agents. The company is now planning to increase its presence in the mid-ticket size segment and add 26 new offices in Q1FY10.

The wholesale funding cost has come down significantly and, incrementally, the company is raising funds at the rate of ~7.0-7.5%; there is further scope of reduction in average funding cost, going forward. Taking this into account, the company has reduced its lending rates further by 75bps with effect from April 2009 (besides 75bps reduction in January).

LICHF has created its own niche customer segment in the housing finance space, with the PSU employees comprising a large part of LICHF's customer base. In the current volatile scenario, we believe that LICHF is better placed vis-à-vis competitors driven by the strong position of its target customers.

LICHF's target customer base has benefited immensely from the recommendations of the sixth pay commission. We expect the sixth pay commission to help LICHF in two ways :

- a) One time payment totaling Rs180bn will help the government employees in making the equity contribution/down payment for the housing property
- b) Average hike of 30-40% in salaries will improve the loan servicing ability of the government employees.

Home loans to Gross Domestic product (GDP) Ratio in India is 7.25% as against 50% in developed countries like United States and United Kingdom, according to Assocham. This indicates a huge growth potential for the housing sector and in turn presents a fantastic growth opportunity for the housing finance industry.

Life Insurance Corporation (LIC), which owns 40.8% of LICHF, is a well-known brand (leader in the Life Insurance Sector in India) and has high safety perception. The company uses the agency network of the parent and so can potentially leverage on a huge customer base. LIC of India helps the company to raise funds in times of liquidity crunch by participating in its bond offerings. Also due to its parentage, the LICHF enjoys equally good brand recall. Further the public sector nature of the parent has helped LICHF to follow a conservative approach in terms of loan disbursements helping to mitigate downside risks.

The company has an Equity Capital of Rs.84.99 cr and a strong Book Value of Rs.262. Last paid dividend was 130%. We expect the company to report an EPS of Rs.95 for FY10 which discounts the current market price by just 6.63 times.

BUY FOR MEDIUM TERM INVESTMENT.

Note: In case of any problem in receiving NEWSLETTER, kindly contact Mr Devesh Chauhan at 9350171231

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