10 April 2024

Company Update| Sector: NBFCs

PNB Housing

BSE SENSEX	S&P CNX
75,038	22,754

Ghar Ki Baat

Bloomberg	PNBHOUSI IN
Equity Shares (m)	260
M.Cap.(INRb)/(USDb)	198.6 / 2.4
52-Week Range (INR)	914 / 407
1, 6, 12 Rel. Per (%)	8/-9/38
12M Avg Val (INR M)	601

Financials &Valuations (INR b)

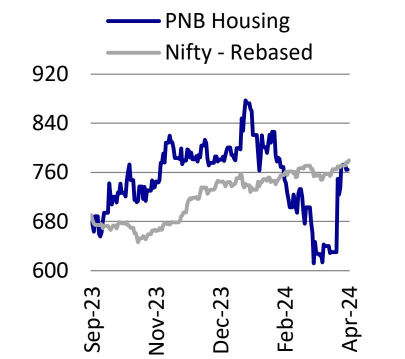
Y/E March	FY24E	FY25E	FY26E
Total Income	24.5	29.2	35.0
PPP	20.6	25.4	31.5
PAT	14.4	18.2	22.7
EPS (INR)	55	70	87
EPS Gr. (%)	-11	26	25
BV (INR)	576	636	711
Ratios			
NIM (%)	4.0	4.1	4.2
C/I ratio (%)	24.6	23.9	22.8
RoAA (%)	2.1	2.3	2.4
RoE (%)	11.1	11.5	13.0
Valuations			
P/E (x)	13.9	11.0	8.8
P/BV (x)	1.3	1.2	1.1
Div. Yield (%)	1.3	1.6	1.9

Shareholding pattern (%)

As On	Dec-23	Sep-23	Dec-22
Promoter	28.1	28.1	32.5
DII	7.9	7.7	3.0
FII	24.7	24.8	23.6
Others	39.3	39.5	40.8

FII Includes depository receipts

Stock performance (one-year)



CMP: INR769 TP: INR1,000 (+30%) Buy

Steering through near-term headwinds for a robust franchise ahead

Improvement in product mix to offset the adverse impact on NIM

- **PNB Housing Finance (PNBHF) plans to transform from a prime housing financier into a lender that offers a wide bouquet of mortgage products across cohorts of product and customer profiles. In addition to its existing affordable housing loans (Roshni) vertical, it will also enter the emerging market vertical from FY25.**
- **PNBHF has restructured its business model and prioritized the retail segment by reducing corporate loans in the overall loan mix to ~4% in Dec'23 from ~21% in Mar'20, through down-selling, recoveries, and ARC sales.**
- **All the three Credit Rating Agencies (CRA) – India Ratings, ICRA and CARE – have upgraded PNBHF to AA+ within the last three months. This credit rating upgrade can help PNBHF reduce its cost of borrowings by 20-25bp.**
- **However, there could be a near-term pressure on its NIM because of the much lower revenue contribution from the corporate loan books and higher competitive intensity. However, its pivot towards affordable housing and emerging vertical will help PNBHF improve its product mix that can mitigate the impact on its NIM.**
- **PNBHF has made notable enhancements to its collection framework, including the introduction of digital channels to streamline the collection process. Improvements in GS3 should sustain, and we model credit costs of ~30bp each in FY25E/FY26E. It has a written-off pool of ~INR17b and ~INR5b in corporate and retail, respectively. Recoveries from this pool (if executed well) could result in further reductions in credit costs and improvements in profitability.**
- **We had earlier stated PNBHF as our Top Pick for CY24 (refer to: Tide has turned, smooth ride ahead). We remain constructive on the company. Our conviction in PNBHF is predicated on: 1) the visibility of a healthy retail loan growth trajectory from FY25 onwards, 2) the ability to mitigate near-term NIM compression through improvement in product mix and decline in CoB, and 3) normalization to steady-state credit costs of ~30bp.**
- **We expect PNBHF to deliver a PAT CAGR of ~26% over FY24-26 and an RoA/RoE of 2.5%/13.0% in FY26. Reiterate BUY with a TP of INR1,000 (based on 1.4x FY26E P/BV).**

Building capabilities for healthy retail loan growth from FY25

- PNBHF has scaled up to 212 branches (as of Dec'23) and guided its branch network to increase to ~300 (including ~160 affordable housing branches) by Mar'24. Branch additions and gradual productivity improvements in new branches will drive healthy retail loan growth for the company.
- From FY25 onwards, PNBHF will also embark on its Emerging Market Strategy, wherein the customer segment will be in the Tier 2/3 markets between prime and affordable housing. Effectively, PNBHF will now operate across Prime, Affordable and Emerging markets. We estimate retail loan CAGR of ~17% over FY24-FY26.

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Better product mix and lower CoF to offset the near-term impact on NIM

- Loss of interest income from the sharp rundown in the corporate loan book has led to a near-term hit on NIM. We expect this adverse impact to sustain for the next few quarters and subsequently be mitigated through an improvement in the product mix.
- The company plans to come up with 40-50 emerging-market branches that will focus on a product/customer segment where yields will be 35-40bp higher than that of prime customer yields. This will help improve the blended yields.
- India Ratings upgraded PNBHF's credit rating to AA+ (Stable) in Jan'24. Subsequently, ICRA and CARE also upgraded the company's credit rating to AA+ in Mar'24. We expect PNBHF's borrowing costs to decline ~20-25bp from the credit rating upgrades. Moreover, the company has again started receiving sanctions from NHB in FY24, which will further aid the CoB. We model NIM of 4.1%/4.2% in FY25/FY26E (v/s. 4.0% in FY24E).

Minor uptick in opex despite the pivot towards affordable housing

- Management guides a minor uptick in opex as it develops the affordable housing vertical. This is because it is incrementally only required to invest in branch premises and manpower to buildout its affordable housing vertical.
- The opex-to-average assets ratio is likely to be 1.0% in FY24 (vs. 0.8%/0.7% in FY23/FY22) due to investments in physical branch distribution and technology. We expect opex ratio to remain stable at similar levels over FY25-FY26E.

Asset quality stress behind; write-backs to further support profitability

- PNBHF has successfully navigated through the asset quality stress in its retail and corporate segments, which had earlier made it ineligible for NHB borrowings. Through a combination of recoveries, ARC sales, and write-offs, the company has improved its asset quality, with GS3 at 1.7% as of Dec'23 (vs. the peak of 8.2% in Dec'21).
- PNBHF now has a tiered collection framework, with dedicated teams for X-bucket, pre-NPA, NPA, Recovery and SARFAESI. Further, the company has a written-off pool of ~INR17b and ~INR5b in corporate and retail, respectively. Recoveries (if executed well) from the written-off pool and the consequent write-backs can result in credit costs below ~30bp in FY25E/FY26E.

Valuation and view: Risk-reward attractive for a strengthening franchise

- PNBHF is well equipped to successfully navigate the near-term headwinds in its NIM profile, and further offset them with product mix improvement. We expect the company to deliver a healthy ~18% CAGR in AUM and ~26% CAGR in PAT over FY24-26, with an RoA/RoE of 2.4%/13.0% by FY26.
- The company trades at 1.1x FY26E P/BV, and the risk-reward is favorable for a further re-rating in the valuation multiple as investors gain more confidence in its sustained execution in retail (both prime and affordable). **Reiterate BUY with a TP of INR1,000 (based on 1.4x FY26E P/BV).**
- Key risks: a) a slowdown in the economy leading to lower demand for housing and moderation in loan growth, and b) subsequent seasoning in the affordable loan book leading to asset quality deterioration.

STORY IN CHARTS

Exhibit 1: Disbursement CAGR of ~25% over FY24-26E…

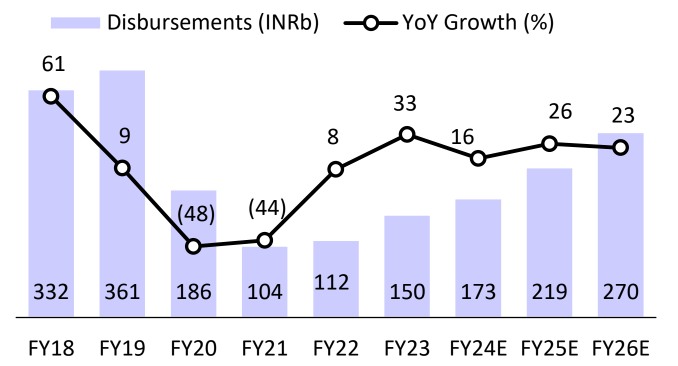


Exhibit 2: …leading to ~18% AUM CAGR over this period

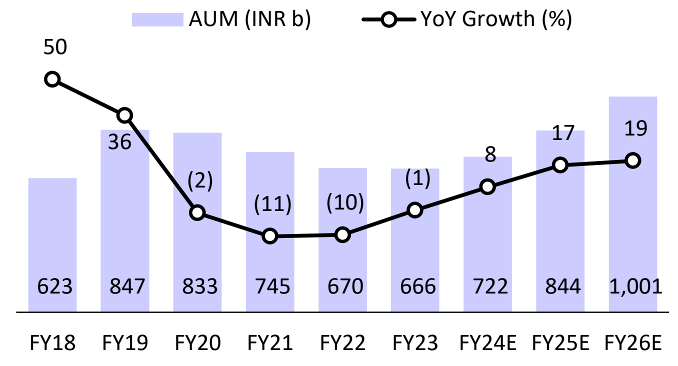


Exhibit 3: NIM expansion from improvement in product mix

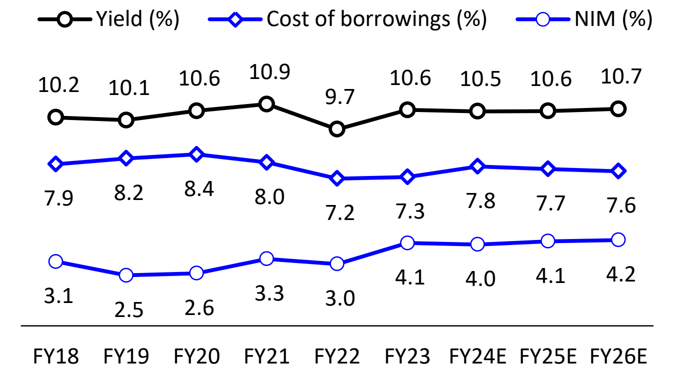


Exhibit 4: Opex-to-assets ratio to remain stable over FY25-FY26E

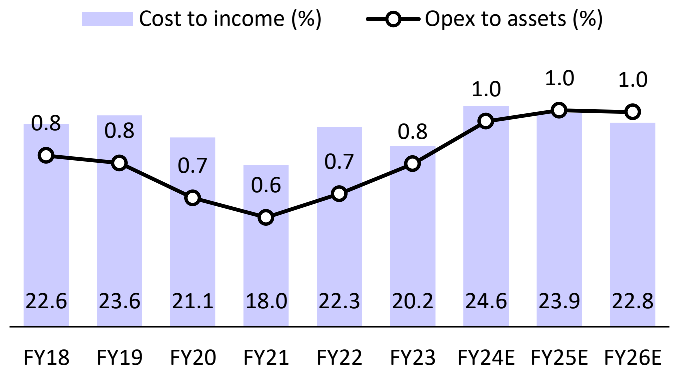


Exhibit 5: Asset quality would continue to improve

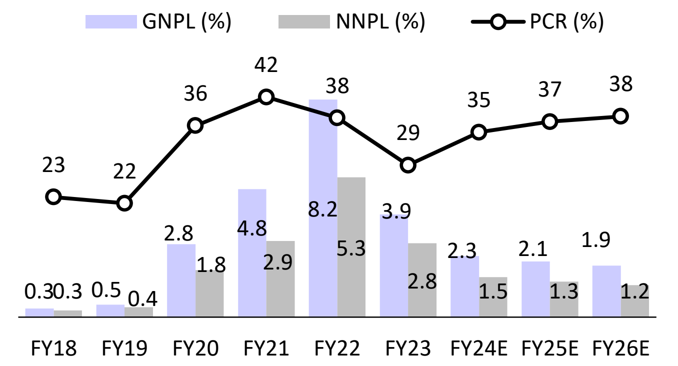


Exhibit 6: Estimate credit costs at ~30bp over FY25-26

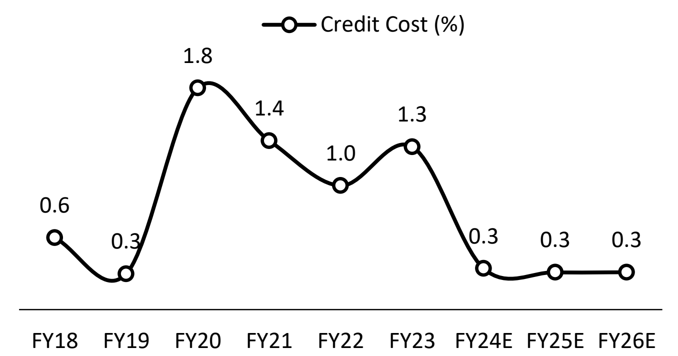
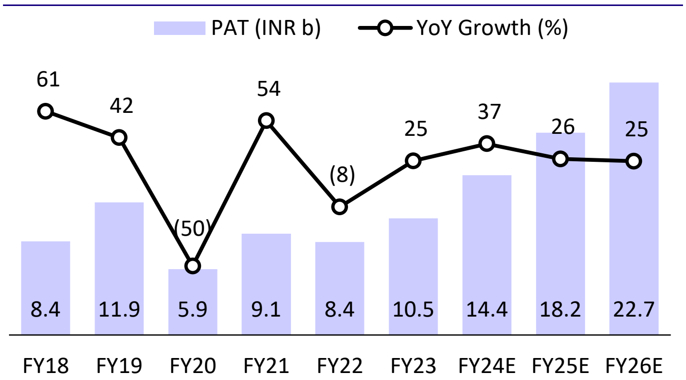
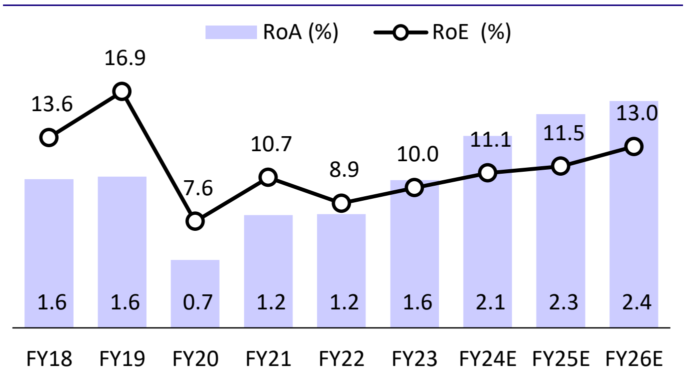


Exhibit 7: PAT CAGR at ~26% over FY24E–26E



Source: MOFSL, Company

Exhibit 8: RoA/RoE at ~2.4%/~13.0% in FY26E

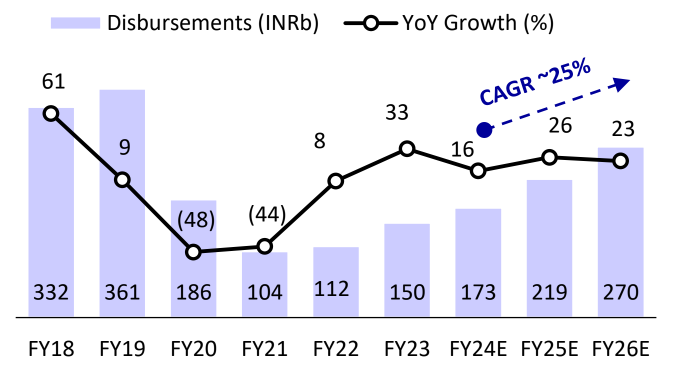


Source: MOFSL, Company

Primed for healthy retail loan growth from FY25 onwards

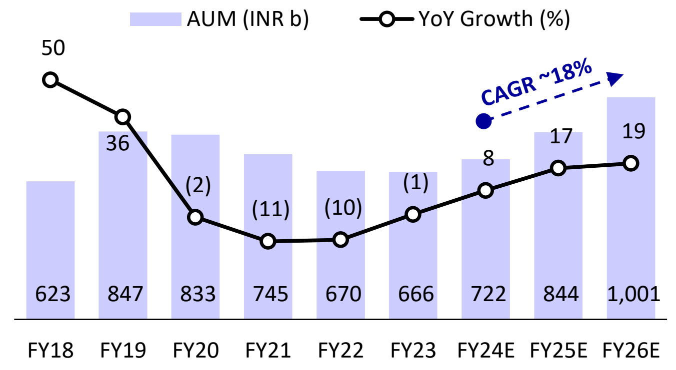
- PNBHF has undergone a significant transformation in its business model by shifting its focus towards retail. It has reduced its corporate loan portfolio [through down-selling and Asset Reconstruction Company (ARC) sales], to 4% of the total AUM as of Dec'23. PNBHF does not envisage any strong growth in its corporate loan book and will keep it below 10% of the total AUM.
- Conversely, we expect a retail loan growth of ~14% in FY24 vs. its earlier guidance (in the beginning of the year) of ~17%. However, management is confident of achieving ~17% retail loan growth from FY25 onwards through expansion of affordable housing branches and introduction of the emerging market vertical. We expect PNBHF to deliver ~18% AUM CAGR over FY24-FY26E.
- Southern India contributed ~37% to the disbursement mix in 9MFY24 (9MFY23: ~31%), while the share of the western region declined to ~28% (9MFY23: ~35%).

Exhibit 9: Disbursement CAGR of ~25% over FY24-26E…



Source: MOFSL, Company

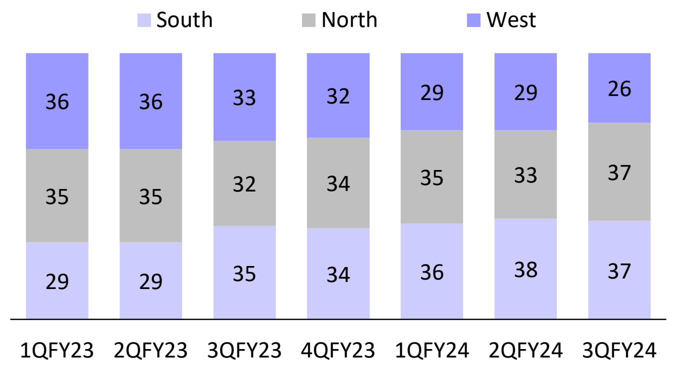
Exhibit 10: …leading to ~18% AUM CAGR over this period



Source: MOFSL, Company

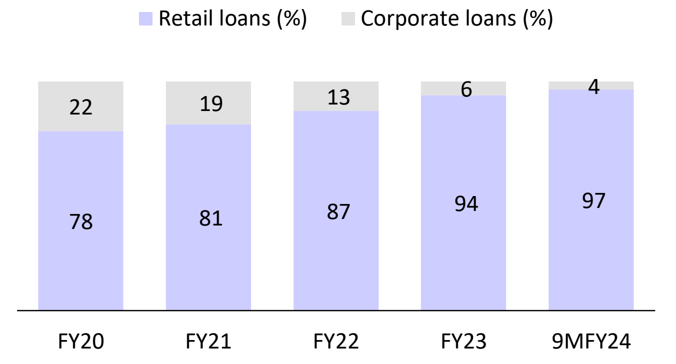
- The company has come up with 50 'Emerging Markets' branches that will focus on a product/customer segment where yields will be 35-40bp higher than that of prime customer yields. This will help improve the blended yields.

Exhibit 11: Ramping up disbursements in South India (%)



Source: MOFSL, Company

Exhibit 12: PNBHF has rundown the corporate book

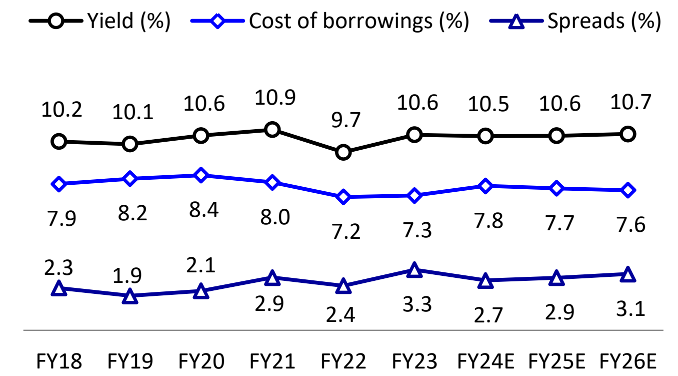


Source: MOFSL, Company

Better product mix and lower CoF to offset the impact on NIM

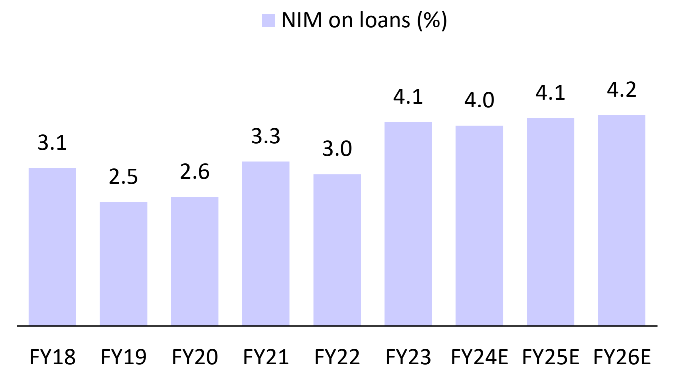
- Management has implemented several strategic decisions to reduce portfolio risk, which impacted NIMs adversely earlier. These decisions include reduction of the corporate book, leaning towards salaried customers, and placing more emphasis on home loans than non-home loans.
- Reported NIMs for 3QFY24 contracted ~45bp QoQ to ~3.5% due to ~20bp QoQ decline in yields. This was attributed to: 1) book retention strategies to address BT-OUTs, b) competitive dynamics resulting in lower interest rate lending in specific regions, c) decline in the corporate book, and d) a one-off interest income reversal of ~INR160m due to MCLR changes in the securitized pool. Excluding the one-off, yields stood at 10.3%, CoF stood at ~8.0%, spread was at 2.3%, and NIM stood at 3.65% in 3QFY24.
- PNBHF aims to increase yields by ~100bp in the affordable housing vertical from Apr'24. In addition to this, the introduction of emerging market vertical will further help improve the yields. We expect spread to improve to ~2.9% in FY25, before expanding gradually to ~3.1% by FY26 through a combination of improvement in yields and decline in CoB.

Exhibit 13: Spread likely to expand further (%)



Source: MOFSL, Company

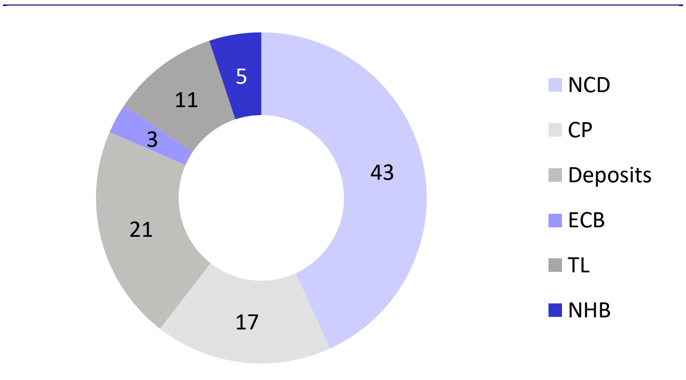
Exhibit 14: NIM likely to improve to ~4.2% in FY26 (%)



Source: MOFSL, Company

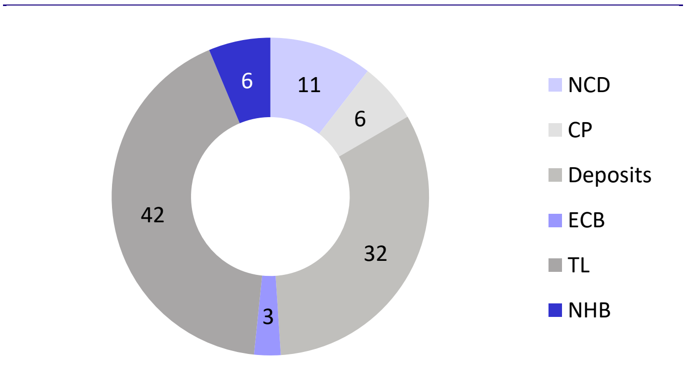
- PNBHF has a fairly diversified liability profile with the ability to raise funds from banks and debt capital markets. It holds a deposit-taking license, with deposits constituting ~32% of the total funding mix as of Dec'23. During 3QFY24, ECBs were refinanced with lower-cost domestic borrowings, resulting in a decline in the proportion of ECBs to ~3% (PY: ~11%).

Exhibit 15: Borrowing mix as of Dec'18 (%)



Source: MOFSL, Company Note: Data as on Dec'18

Exhibit 16: Borrowing mix as of Dec'23 (%)



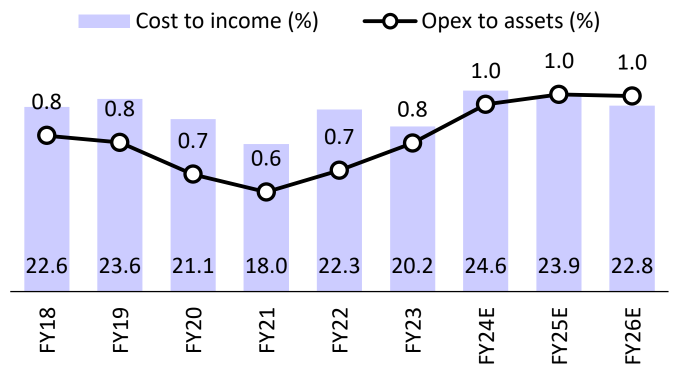
Source: MOFSL, Company Note: Data as on Dec'23

- India Ratings, CARE, and ICRA upgraded PNBHF's credit rating to AA+ (Stable), and we anticipate CRISIL to follow suit within 3-6 months. These upgrades will significantly enhance the company's access to debt capital markets and help it better negotiate spreads on bank term loans.
- With decline in borrowing costs and expansion in yields, we expect NIM to improve ~20bp over the next two years. This would result in a NIM (as a % of avg. loans) of ~4.2% in FY26E (FY24E: ~4.0%).

Controlled opex despite branch expansion

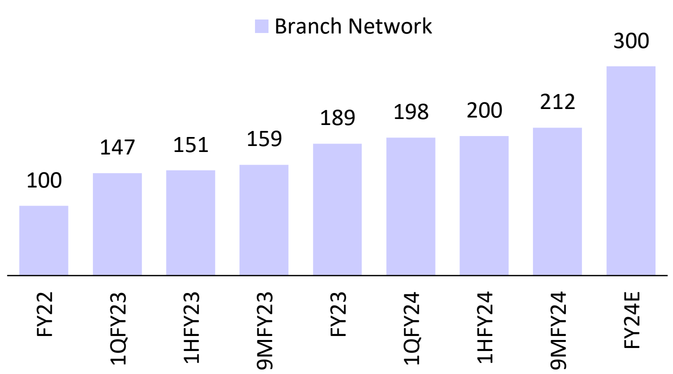
- As of Dec'23, PNBHF operated in 20 states/UTs with 212 branches, including 100 branches dedicated to affordable housing. It plans to expand to ~300 branches by Mar'24, with ~160 being focused on affordable housing. Additionally, from Apr'24 onwards, management intends to introduce the Emerging Market vertical where it will target Tier 2 and 3 markets.
- There will only be a slight increase in opex due to branch and manpower expenses for Roshni branches. However, there will be no additional costs for the emerging vertical, as ~50 existing prime branches will be converted into emerging vertical branches. We expect the opex-to-average assets ratio to remain stable at ~1% and cost-to-income ratio to drop to ~23% by FY26 (FY24E: ~25%).

Exhibit 17: Opex/asset to remain stable (%)



Source: MOFSL, Company

Exhibit 18: Aims to scale total branches to ~300 by Mar'24

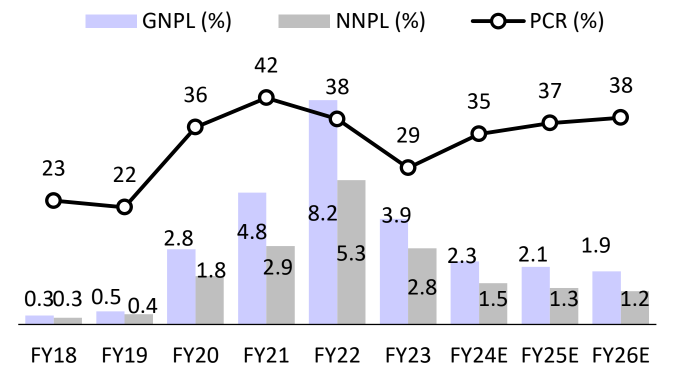


Source: MOFSL, Company

Asset quality stress behind; write-backs to further support profitability

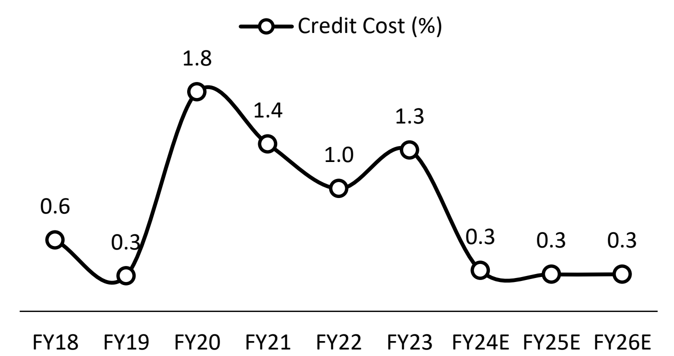
- PNBHF has successfully navigated through the asset quality stress in its retail and corporate segments, which had earlier made it ineligible for NHB borrowings. Through a combination of recoveries, ARC sales, and write-offs, the company has improved its asset quality, with GS3 at 1.7% as of Dec'23 (vs. the peak of 8.2% in Dec'21).
- PNBHF now has a tiered collection framework, with dedicated teams for X-bucket, pre-NPA, NPA, Recovery and SARFAESI. Further, the company has a written-off pool of ~INR17b and ~INR5b in corporate and retail, respectively. Recoveries (if executed well) from the written-off pool and the consequent write-backs can result in credit costs below ~30bp in FY25E/FY26E.

Exhibit 19: Asset quality would continue to improve



Source: MOFSL, Company

Exhibit 20: Est. credit costs to remain stable at 30bp (%)

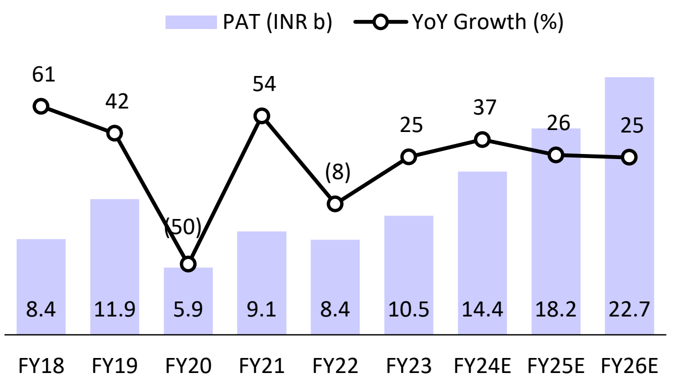


Source: MOFSL, Company

Risk-reward attractive for a strengthening franchise

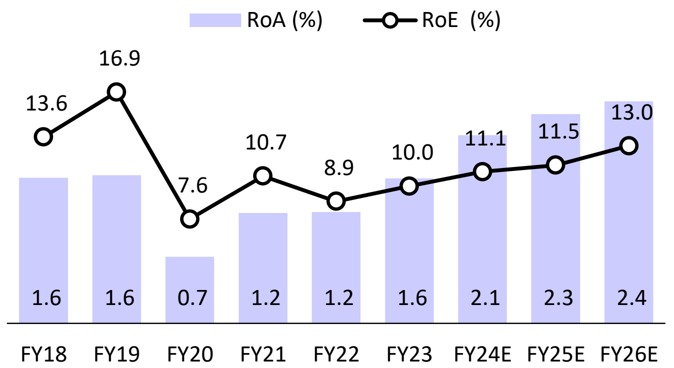
- PNBHF is well equipped to successfully navigate the near-term headwinds in its NIM profile, and further offset them with product mix improvement. We expect the company to deliver a healthy ~18% CAGR in AUM and ~26% CAGR in PAT over FY24-26, with an RoA/RoE of 2.4%/13.0% by FY26.
- The company trades at 1.1x FY26E P/BV, and the risk-reward is favorable for a further re-rating in the valuation multiple as investors gain more confidence in its sustained execution in retail (both prime and affordable). **Reiterate BUY with a TP of INR1,000 (based on 1.4x FY26E P/BV).**
- Key risks: a) a slowdown in the economy leading to lower demand for housing and moderation in loan growth, and b) subsequent seasoning in the affordable loan book leading to asset quality deterioration.

Exhibit 21: PAT CAGR of ~26% over FY24E–26E



Source: MOFSL, Company

Exhibit 22: Primed to deliver an RoA/RoE of ~2.4%/~13.0% in FY26E



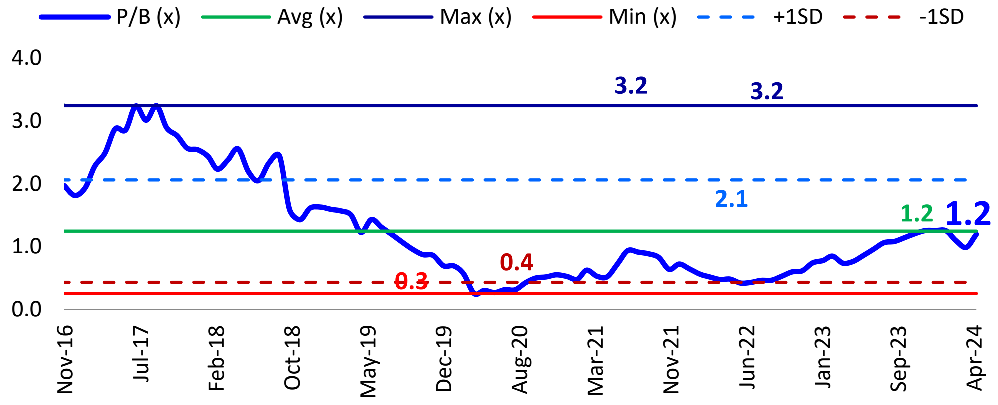
Source: MOFSL, Company

Exhibit 23: We cut our FY25/FY26E EPS by ~4% each to factor in lower NIM and higher opex, but partly offset by lower credit costs

INR b	Old Est.			New Est.			Change (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
NII	24.9	30.3	36.3	24.5	29.2	35.0	-1.5	-3.6	-3.5
Other Income	2.8	4.1	5.8	2.8	4.1	5.8	0.0	0.0	0.0
Total Income	**27.7**	**34.4**	**42.1**	**27.3**	**33.3**	**40.8**	**-1.3**	**-3.2**	**-3.0**
Operating Expenses	6.7	7.7	8.9	6.7	8.0	9.3	0.4	3.9	4.5
Operating Profits	**21.0**	**26.8**	**33.2**	**20.6**	**25.4**	**31.5**	**-1.9**	**-5.2**	**-5.1**
Provisions	2.2	2.5	2.8	2.0	2.1	2.5	-5.8	-14.4	-11.9
PBT	**18.8**	**24.3**	**30.4**	**18.6**	**23.3**	**29.0**	**-1.4**	**-4.3**	**-4.4**
Tax	4.3	5.3	6.7	4.2	5.1	6.4	-1.4	-4.3	-4.4
PAT	**14.6**	**19.0**	**23.7**	**14.4**	**18.2**	**22.7**	**-1.4**	**-4.3**	**-4.4**
Loan book	651	761	902	650	760	901	-0.2	-0.1	-0.1
NIM (%)	4.1	4.3	4.4	4.0	4.1	4.2			
Spreads (%)	2.8	3.0	3.2	2.7	2.9	3.1			
ROAA (%)	2.1	2.4	2.5	2.1	2.3	2.4			
RoAE (%)	11.2	12.0	13.5	11.1	11.5	13.0			

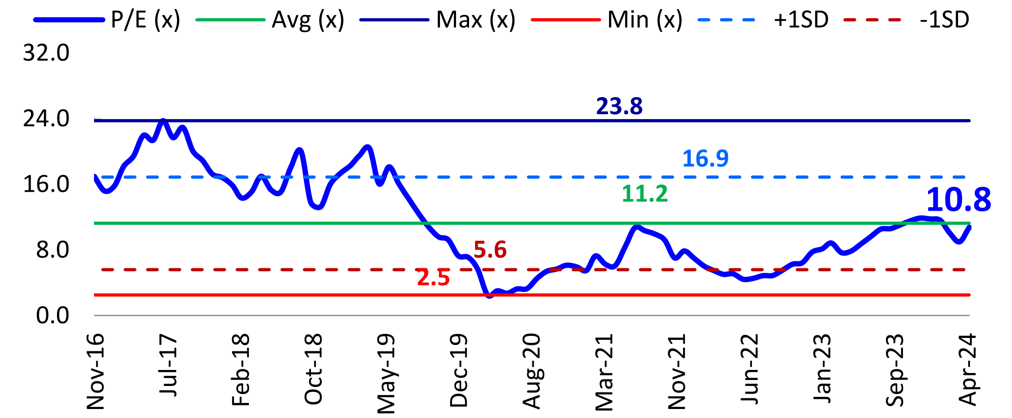
Source: MOFSL estimates; Note: Incorporated the above estimate changes in our preview report released on 4 April, 2024

Exhibit 24: One-year forward P/B



Source: MOFSL, Company

Exhibit 25: One-year forward P/E



Source: MOFSL, Company

Financials and Valuation

Income statement

(INR M)

Y/E March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	67,929	76,882	71,898	58,220	61,991	67,681	76,757	91,004
Interest Expended	51,664	58,750	50,998	40,645	38,985	43,139	47,516	56,008
Net Interest Income	**16,265**	**18,133**	**20,901**	**17,575**	**23,006**	**24,542**	**29,240**	**34,997**
Change (%)	7.7	11.5	15.3	-15.9	30.9	6.7	19.1	19.7
Other Operating Income	8,904	8,013	4,343	3,787	3,306	2,756	4,104	5,821
Net Income	**25,169**	**26,146**	**25,243**	**21,363**	**26,311**	**27,298**	**33,344**	**40,817**
Change (%)	28.9	3.9	-3.5	-15.4	23.2	3.7	22.1	22.4
Operating Expenses	5,935	5,522	4,554	4,760	5,313	6,719	7,953	9,286
Operating Income	**19,234**	**20,624**	**20,689**	**16,603**	**20,998**	**20,579**	**25,391**	**31,531**
Change (%)	27.3	7.2	0.3	-19.7	26.5	-2.0	23.4	24.2
Provisions/write offs	1,890	12,514	8,619	5,764	7,389	2,027	2,115	2,491
PBT	**17,344**	**8,110**	**12,070**	**10,840**	**13,609**	**18,552**	**23,276**	**29,040**
Extraordinary Items	0	0	0	0	0	0	0	0
Reported PBT	**17,344**	**8,110**	**12,070**	**10,840**	**13,609**	**18,552**	**23,276**	**29,040**
Tax	5,429	2,201	2,978	2,475	3,149	4,193	5,121	6,389
Tax Rate (%)	31.3	27.1	24.7	22.8	23.1	22.6	22.0	22.0
DTL on Special Reserve								
Reported PAT	**11,915**	**5,909**	**9,092**	**8,365**	**10,460**	**14,359**	**18,155**	**22,651**
Change (%)	41.7	-50.4	53.9	-8.0	25.0	37.3	26.4	24.8
PAT adjusted for EO	**11,915**	**5,909**	**9,092**	**8,365**	**10,460**	**14,359**	**18,155**	**22,651**
Change (%)	41.7	-50.4	53.9	-8.0	25.0	37.3	26.4	24.8
Proposed Dividend	1,809	0	0	0	0	2,556	3,105	3,873

Balance sheet

(INR M)

Y/E March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Capital	1,675	1,682	1,683	1,686	1,689	2,595	2,595	2,595
Reserves & Surplus	73,764	78,296	87,548	97,030	1,08,448	1,46,838	1,62,437	1,81,984
Net Worth	**75,439**	**79,978**	**89,230**	**98,716**	**1,10,137**	**1,49,433**	**1,65,032**	**1,84,579**
Borrowings	**7,18,589**	**6,77,351**	**5,93,925**	**5,30,050**	**5,36,211**	**5,65,691**	**6,68,496**	**8,06,359**
Change (%)	33.6	-5.7	-12.3	-10.8	1.2	5.5	18.2	20.6
Other liabilities	44,662	31,969	30,767	28,530	15,795	17,375	18,244	19,156
Total Liabilities	**8,38,690**	**7,89,297**	**7,13,922**	**6,57,296**	**6,62,143**	**7,32,499**	**8,51,772**	**10,10,094**
Loans	**7,42,879**	**6,66,280**	**6,06,447**	**5,53,359**	**5,78,398**	**6,50,220**	**7,59,655**	**9,00,960**
Change (%)	30.0	-10.3	-9.0	-8.8	4.5	12.4	16.8	18.6
Investments	**45,607**	**20,757**	**20,448**	**34,827**	**31,963**	**35,159**	**38,675**	**42,543**
Change (%)	89.0	-54.5	-1.5	70.3	-8.2	10.0	10.0	10.0
Net Fixed Assets	1,083	1,353	1,056	935	839	881	925	971
Other assets	49,122	1,00,906	85,971	68,175	50,943	46,239	52,517	65,620
Total Assets	**8,38,690**	**7,89,297**	**7,13,922**	**6,57,296**	**6,62,143**	**7,32,499**	**8,51,772**	**10,10,094**

Financials and Valuation

Ratios								(%)
Y/E March	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Spreads Analysis (%)								
Avg yield on loans	10.1	10.6	10.9	9.7	10.6	10.5	10.6	10.7
Avg. cost of funds	8.2	8.4	8.0	7.2	7.3	7.8	7.7	7.6
Interest Spread	1.9	2.1	2.9	2.4	3.3	2.7	2.9	3.1
NIM on loans	2.5	2.6	3.3	3.0	4.1	4.0	4.1	4.2
Profitability Ratios (%)								
RoE	16.9	7.6	10.7	8.9	10.0	11.1	11.5	13.0
RoA	1.6	0.7	1.2	1.2	1.6	2.1	2.3	2.4
Int. Expended/Int.Earned	76.1	76.4	70.9	69.8	62.9	63.7	61.9	61.5
Other Inc./Net Income	35.4	30.6	17.2	17.7	12.6	10.1	12.3	14.3
Efficiency Ratios (%)								
Op. Exps./Net Income	23.6	21.1	18.0	22.3	20.2	24.6	23.9	22.8
Empl. Cost/Op. Exps.	51.2	42.2	46.4	45.5	50.1	49.5	49.7	50.7
Asset Quality (INR m)								
Gross NPA	3,549	18,562	29,990	47,062	22,714	15,194	16,170	17,689
GNPA ratio	0.5	2.8	4.8	8.2	3.9	2.3	2.1	1.9
Net NPA	2,784	11,838	17,500	29,312	16,184	9,876	10,187	10,967
NNPA ratio	0.4	1.8	2.9	5.3	2.8	1.5	1.3	1.2
CAR	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0

VALUATION	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Book Value (INR)	450	476	530	586	652	576	636	711
BVPS Growth YoY	14.3	5.6	11.5	10.4	11.4	-11.7	10.4	11.8
Price-BV (x)			**1.5**	**1.3**	**1.2**	**1.3**	**1.2**	**1.1**
EPS (INR)	71.1	35.1	54.0	49.6	61.9	55.3	70.0	87.3
EPS Growth YoY	40.9	-50.6	53.8	-8.2	24.9	-10.7	26.4	24.8
Price-Earnings (x)		**21.9**	**14.2**	**15.5**	**12.4**	**13.9**	**11.0**	**8.8**
Dividend per share (INR)	9.0	0.0	0.0	0.0	0.0	9.8	12.0	14.9
Dividend yield (%)			**0.0**	**0.0**	**0.0**	**1.3**	**1.6**	**1.9**

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Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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