

9 November 2022

Star Housing Finance – BUY

CMP : Rs.208.0
Target Price : Rs.256.0
Upside : 23%+
Stop Loss : Rs.178.0 (Closing basis)

Investment Thesis

Star Housing Finance Limited (Star HFL) has reported strong business and financial performance for H1FY23, however the stock price of Star HFL corrected by ~9% from 52-week high of Rs.226.70.

Till September 2019, STAR HFL's operation was only concentrated in Rajasthan. Post equity infusion by Arkfin in October 2019, STAR HFL has transformed itself and expanded its geographic presence to Maharashtra, Madhya Pradesh, Gujarat, Rajasthan and Tamil Nadu with 10 physical branches and 20 digital points. Star HFL now exclusively focuses on retail home loans, targeting first time home buyers from the economically weaker section / low income group (EWS / LIG) borrower segment looking to purchase/construct own homes that qualify under Pradhan Mantri Awas Yojana in tier-II, tier-III cities and semi-urban geographies. STAR HFL has completely revamped its earlier strategy of franchise-based business model with in-house sourcing, underwriting, processing and collection. STAR HFL has also entered into co-lending agreement with Capital India Home Loans and Singularity Creditworld.

STAR HFL has set a target as the first milestone to achieve asset size (AUM) of Rs.5,000mn to become a systemically important home finance company in the next 4-6 operational quarters. Its leverage levels has come down to sub 1.0x courtesy three capital infusions in last 12 months resulting in net worth set to cross Rs.1,000mn. This gives enough headroom for liability scale up for Rs.5,000mn AUM growth. The milestone will open the door of the lenders and give a huge boost to STAR HFL in lowering cost of borrowing. Currently, STAR HFL has network covering 40 districts in 5 states and planning to expand to 100 districts and new states such as UP and Haryana in the next 4-6 quarters. STAR HFL has increased the number of lenders to 15, which has helped in increasing the spread by 40-50bps in the current quarter. It has recently tied-up with some more banks and financial institutions like SBI, LIC HFL, MAS and CIFCL to take this number to 35. Current cost of borrowing of STAR HFL is 10.25-10.55%. With the capitalization and growth given by STAR HFL, we are expecting a re-rating going ahead which will bring down the cost of borrowing.

Financials

- During the past 5 years, NII of STAR HFL grew at a CAGR of 34.7% while PAT grew at a CAGR of 11.1% in the same period.

Standal. (INR Mn)	FY20	FY21	FY22	FY23E	FY24E
NII	109	105	118	189	223
% growth	53.1	-3.2	12.2	60.0	18.0
PAT	50	16	24	75	90
ABV (Rs.)	31.6	32.3	36.8	52.4	62.5
P/ABV (x)	6.6	6.4	5.6	4.0	3.3
EPS (Rs.)	3.2	1.0	1.4	4.0	4.7
P/E (x)	64.7	209.4	144.8	52.0	44.2
RoE (%)	9.6%	2.9%	3.7%	7.4%	7.3%

- STAR HFL reported 64.8% YoY and 48.7% QoQ growth in NII to Rs.74.2mn in Q2FY23, driven by healthy AUM growth of 51.7% YoY to Rs.1,522.9mn.

Stock Data

Market Cap (Rs. Mn)	3,814
Market Cap (\$ Mn)	46.77
Shares O/S (in Mn)	18.2
Avg. Volume (3 month)	150,000
52-Week Range (Rs.)	226.70 / 80.20

Shareholding Pattern

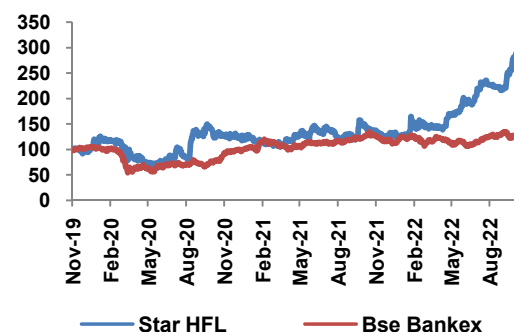
Promoters	25.62%
FII's	0.00%
Institutions	0.00%
Others (incl. body corporate)	74.38%

Key Ratios

Div Yield	0.1%
P/ABV (x)	5.7x
ROE	3.7%
ABV (Rs.)	36.8/-

Stock Performance

Performance (%)	1M	6M	1Yr
Absolute	7.8%	82.4%	123.8%
BSE Bankex	6.8%	19.8%	5.8%



- STAR HFL has recorded highest disbursements at Rs. 642.1mn and registered a 358% YoY growth for H1FY23.
- STAR HFL has reported 483.5% YoY and 60.1% QoQ growth in PAT to Rs.21.7mn in Q2FY23 led by 40-50bps increase in spread in the current quarter. PAT is expected to grow backed by business uptick in the current growth phase that has started since the current financial year.

Key Business Highlights

- STAR HFL is primarily engaged in providing housing loans to individuals for construction, purchase, repair, and upgradation of houses to the underserved segments in the lower and middle-income categories.
- Arkfin Investments invested equity capital of Rs.155mn in October 2019 for a stake of 21.5%. Post receipt of equity capital from Arkfin, STAR HFL has expanded its branch network to 5 states. It has consistently strengthened its network through regular capital infusion with latest capital raise post all approvals expected to result net worth crossing Rs.1,000mn.
- Currently, STAR HFL operates in the Udaipur, Jaipur, Mumbai, Pune, Mahad, Baramati, Akola, Indore, Chennai and Surat with AUM of Rs.1,522.9mn with more than 1,300 customers as on September 30, 2022.

Valuation

- STAR HFL continue to be rural and semi-urban focused affordable housing finance company under priority sector lending catering to retails loans to first time home buyers in low income / weaker section. STAR HFL is targeting loan ticket size of Rs.11-12 Lakhs for semi urban and Rs.6-8 Lakhs for rural area. STAR HFL is launching customer centric products like 'Star Gram Loans' to be a niche player in rural centric HFCs. It is also investing on digital platform for better collection and disbursal framework.
- STAR HFL has announced the bonus equity shares in 1:1 ratio i.e. one bonus equity share for every one fully paid-up equity share. It has also announced of stock split in 1:2 ratio.
- Housing Finance Companies (HFCs) provides a much hassle-free housing finance, thus increasing their attractiveness to potential borrowers. Housing finance market is expected to grow at a CAGR of over 20.0% during FY22-27E majorly due to increasing urbanization and affordable mortgage rates. Government initiatives for affordable housing and interest subsidies under PMAY also propel demand for housing finance. Demand for affordable housing are majorly in tier-II, tier-III & beyond geographies where banks and large HFCs are reluctant to lend due to difficulty in credit appraisal, lack of proper documentation, intense KYC checks, NPL volatility and aggressive follow-up. Affordable housing finance business has created an un-tapped market to be tapped by specialized HFCs like STAR HFL. We believe STAR HFL is well placed to mirror the strong growth of HFCs in India going ahead led by virtue of competitive product offerings, competitive product pricing, superior customer service and last mile connectivity where the demand is soaring.
- With a target to achieve asset size (AUM) of Rs.5,000mn in the next 4-6 operational quarters, plan to expand to 100 districts and new state such as UP and Haryana, expected re-rating will bring down the cost of borrowing and targeting 400-500bps spread to cover credit cost and healthy profit margins, we are valuing STAR HFL at 4.1x FY24E ABV of Rs.62.50 to arrive at target price of Rs.256.00, an upside of ~23%.

Risk & Concern

- Over 90% of loan book is from top 3 states i.e. Rajasthan, MP and Maharashtra, any significant change in government policies, economic or political disruption in these states may impact the business activities.
- Any major change in regulatory policies e.g. increase in regulation by NHB, fall in government incentives for housing loans may negatively impact growth and profitability of STAR HFL.
- STAR HFL is largely focused on low income first time buyer, which is comparatively more vulnerable to default and may impact its operating efficiencies and asset quality.

Graphs & Charts

Figure 1: Interest Income Trend

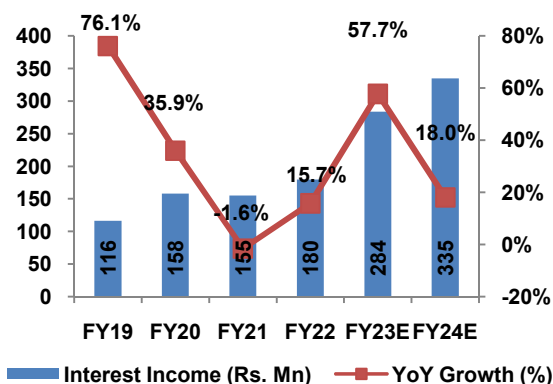


Figure 2: NII Trend

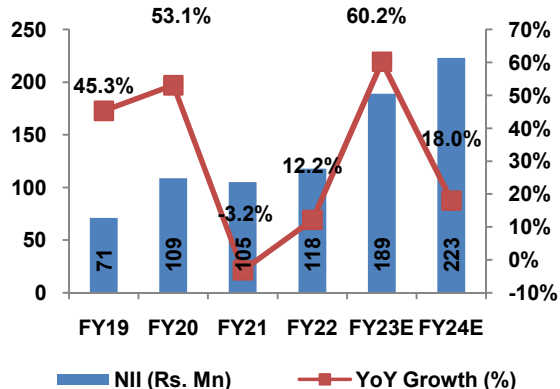


Figure 3: PAT Trend

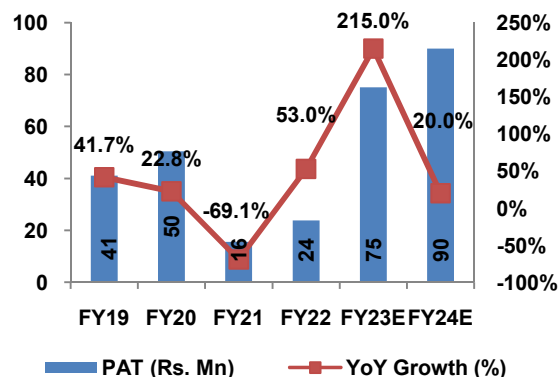
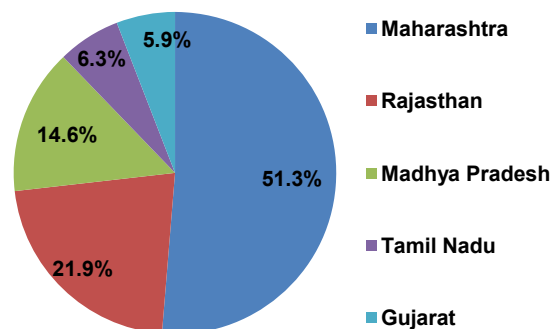


Figure 4: Region-Wise Loan Book



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