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Rating	BUY
Price	Rs58
Target Price	Rs75
Implied Upside	29.3%
Sensex	24,436
Nifty	7,422

(Prices as on January 22, 2016)

Trading data

Market Cap. (Rs bn)	100.0
Shares o/s (m)	1,720.3
3M Avg. Daily value (Rs m)	105

Major shareholders

Promoters	67.96%
Foreign	8.27%
Domestic Inst.	1.92%
Public & Other	21.85%

Stock Performance

(%)	1M	6M	12M
Absolute	(10.1)	(20.4)	(18.7)
Relative	(5.6)	(6.1)	(3.0)

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2017	4.7	6.0	-22.0
2018	6.3	7.6	-16.8

Price Performance (RIC: LTFH.BO, BB: LTFH IN)



Source: Bloomberg

L&T Finance Holdings (LTFH) reported 17% YoY growth in adjusted net profits at Rs2.12bn (PLe: Rs2.28 bn). NII growth stood at 19% YoY (2% below PLe) led by ~20bp QoQ moderation in margins and high NPL formation in rural portfolio. Loan book grew 23% YoY led by 29% YoY growth in the infra portfolio while retail book grew 17% YoY led by strong growth in housing, microfinance and supply chain segments. The proportion of operational projects increased further to 59% and asset quality in the wholesale business remained stable. Challenging outlook in the farm portfolio and sticky credit costs in the infra business (also due to ARC loss amortization) remains an overhang. We increase our credit cost estimates and reduce our PT to Rs75 (from Rs80) based on 1.7x Sep-17E ABV. Retain BUY.

- **Loan book grows 17% YoY; proportion of operational projects increases to 59%:** LTFH reported 17% YoY growth in loan portfolio led by strong 29% YoY growth in infra lending business while retail loan growth stood at modest 17% YoY and was aided by robust growth in Housing (92% YoY), MFI (154% YoY) and Supply chain business. In retail business the share of housing increased to 23% from 21% in 2Q FY16. On infra front, share of operational projects further increased to 59% from 51% in Q1FY16 as renewable energy (dominated by wind power) and roads remain the key growth segments.
- **Asset quality impairment driven by rural portfolio:** GNPL ratio on 150dpd basis increased by 25bp QoQ to 3.33% while NNPL ratio also increased by 23bp QoQ. This was completely led by sharp deterioration in the farm portfolio farm portfolio while the infra segment reported stable trends. Management expressed caution on farm portfolio which will likely keep credit cost elevated.
- **Investment management doing well; maintain BUY with revised PT of Rs75:** LTFH reported steady growth in overall AUMs (share of equity AUMs increased to 41%) and reported profits of Rs48mn vs Rs24 mn last year. We increase our credit cost estimate and revise our PT to Rs75, based on 1.7x Sep-17E ABV.

Key Financials (Y/e March)	2015	2016E	2017E	2018E
Net interest income (Rs m)	24,237	28,589	34,393	42,009
Growth (%)	26.7	18.0	20.3	22.1
Non-interest income (Rs m)	3,460	4,151	5,065	6,128
Operating Profit (Rs m)	16,926	19,715	23,889	30,147
PAT (Rs m)	7,108	8,206	10,305	13,578
EPS (Rs)	3.5	3.8	4.7	6.3
Growth (%)	15.2	8.5	24.4	33.8
Net DPS (Rs)	0.8	0.9	1.2	1.5

Profitability & valuation	2015	2016E	2017E	2018E
Spreads / Margins (%)	5.3	5.1	4.9	4.8
RoAE (%)	9.8	9.9	11.3	13.9
RoAA (%)	1.1	1.1	1.2	—
P/E (x)	16.7	15.4	12.3	9.2
P/BV (x)	1.6	1.5	1.3	1.2
P/ABV (x)	1.7	1.8	1.6	1.5
Net dividend yield (%)	1.4	1.5	2.1	2.6

Source: Company Data; PL Research

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Exhibit 1: LTFH Q3FY16 – higher delinquencies in farm business drags overall performance

Consolidated (Figures in Rs mn)	Q3FY16	Q3FY15	YoY gr.	Q2FY16	QoQ gr.
Income Statement					
Interest income	18,198	15,720	16%	17,934	1%
Interest expense	10,146	8,950	13%	9,976	2%
NII	8,052	6,770	19%	7,957	1%
Other Income	442	395	12%	441	0%
Total Income	8,494	7,165	19%	8,399	1%
Staff expenses	1,348	794	70%	1,312	3%
Other expenses	1,852	1,919	-3%	2,081	-11%
Total Operating Expenses	3,200	2,713	18%	3,392	-6%
Operating profit	5,294	4,452	19%	5,007	6%
Provisions	2,035	1,794	13%	1,834	11%
PBT	3,259	2,658	23%	3,173	3%
Tax	1,147	848	35%	1,029	11%
PAT	2,112	1,810	17%	2,144	-1%
<i>Tax rate (%)</i>	<i>35</i>	<i>32</i>		<i>32</i>	
Asset Quality					
<i>at 180 days recognition</i>					
GNPA (%)	2.9	3.0	(13)	2.7	17
NNPA (%)	1.8	2.0	(19)	1.7	14
Coverage ratio (%)	37.8%	34.2%	363	39.1%	(127)
<i>at 150 days recognition</i>					
GNPA (Rs m)	18,176	19,766	-8%	15,425	18%
NNPA (Rs m)	12,064	14,893	-19%	9,926	22%
GNPA (%)	3.3	4.5	(115)	3.1	25
NNPA (%)	2.2	3.4	(119)	2.0	23
Coverage ratio (%)	33.0%	23.7%	937	35.1%	(20)
Balance Sheet					
Networth (excl. Preference Cap)	69,909	64,550	8%	67,480	4%
Preference Capital	19,630	13,630	44%	12,630	55%
Borrowings	488,300	395,840	23%	453,220	8%
Loans & Advances	531,274	452,250	17%	509,860	4%
Disbursements	131,400	94,380	39%	90,970	44%

Source: Company Data, PL Research

Key Q3FY16 concall highlights:

Management Commentary:

- **Strategy** – Have focused on improving ROEs & sustaining it. From last 18-24 months have been looking at improving or sustain metrics like margins, reduce cost and contain credit cost.
- **Asset quality** – Stressed assets (NNPA + Rest. assets + Net SRs) has seen internal movement but overall has come off to sub 5% in Q3FY16, with overall impaired assets down 100bps QoQ to 6%.

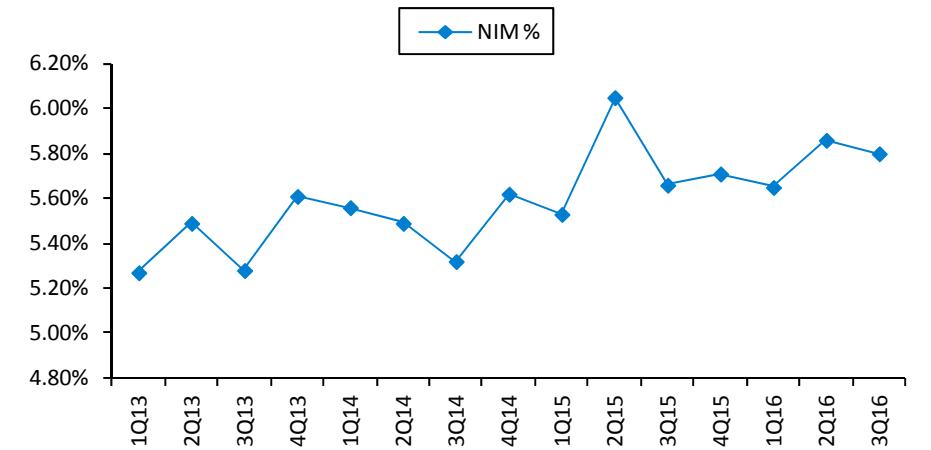
L&T Finance:

- **Businesses** – Retail business have been using analytics and technology to disburse loans. Most of business have been paperless & originated through wireless devices. Tractors – Q3FY16 growth has been improved on festive season but business remains under pressure especially in North India, to offset have aggressively disbursed in used tractor, top up loans & refinancing – 20% of disbursements in these segments. Housing finance – Business continues to well coming off from lower base, CV/CE - book has started to pick-up, also run down has slowed down but remains defocus segment. Mid-market finance – Business has seen some good deals, could continue to growth well. Microfinance – Have seen increase in branches by 19% YoY, which has improved loan growth by 6% QoQ. Growth outlook – Going ahead would grow at 20% YoY (ex housing), but de-focus remains on CV/CE, Cars.
- **Capital** – Retail business ex-housing will require lower capital for some quarters going ahead as growth in business to be moderate & in businesses which will require lower RWAs
- **Margins** – Margins have been stable, Q2FY16 has seen some pre-payment which reflected in margins.
- **Asset quality – Farm delinquencies** – Farm NPAs are up on drought in five states which have been facing issues like MP, Haryana, Punjab & Maharashtra. Also reservoir levels are at 50% in many areas, but late winter has improved sowing and rain outlook seems to be decent. 37% of NPAs has balance of “one EMI” which suggests farmers have paid partially and trends suggest this could improve from the total credit costs of 329bps which increased by 48bps QoQ in Q3FY16 are largely from farm delinquencies.
- Credit cost were higher in housing finance mainly on some frauds detected (50% of provisions related to fraud)

L&T Infra finance:

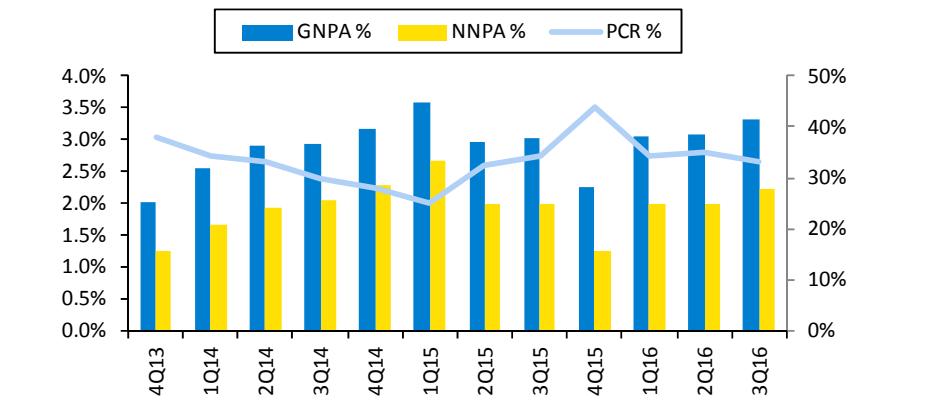
- **Businesses - Operational projects** - Focus remains on financing operational projects as new projects have seen aggressive bidding, so will wait and watch on sidelines. The share of operational has increased further to 59% from 58% in Q2FY16 & 51% in Q1FY16. 70% of operational assets originated are post year 2012, which have are running for 3 years and more despite 1-1.5 years with LTIF. Renewable – Disbursements predominantly in Wind segment and nil in Solar as bidding in projects has been aggressive and hence is being selective by reducing disbursements to Greenfield projects. IDF – Will transfer some assets to IDF subsidiary in coming quarters to take benefits of lower cost, non-taxation and leverage in LTIF has reached close to peak.
- **Monetizing assets** – Have reached substantial progress on selling stake in two equity assets which could likely provide gains of Rs2bn in Q4FY16 and this monetization would be used to do buffer in provisions.
- **Margins** – Margins could sustain at levels of 3.9%-4%.
- **Capital** – Would like to keep leverage cap at 7-7.5x in both LTIF & LT Fincorp where LTIF is close to 7x, while have room in LT Fincorp subsidiary.
- **Asset quality** – Nothing major slippages happened in Q3FY16. Overall stressed assets ratio is coming down, but LTIF could likely see addition of Rs7.5bn to restructured assets mainly on DCCO movement in either Q4FY16 or Q1FY17. LTIF has done at least 40% of required provisions in Q3FY16 itself.
- **On SDR cases** LTIF has already provided on MTM requirement on equity conversions.
- **Credit cost** – Provisions are likely to continue to be sticky as LTIF is amortizing provisions on ARC sale done in FY15 of Rs300mn till Q1FY16, and Rs150mn up till Q2FY17.

Exhibit 2: LTFH – Margins reported a slight drop on higher delinquencies and asset de-risking



Source: Company Data, PL Research

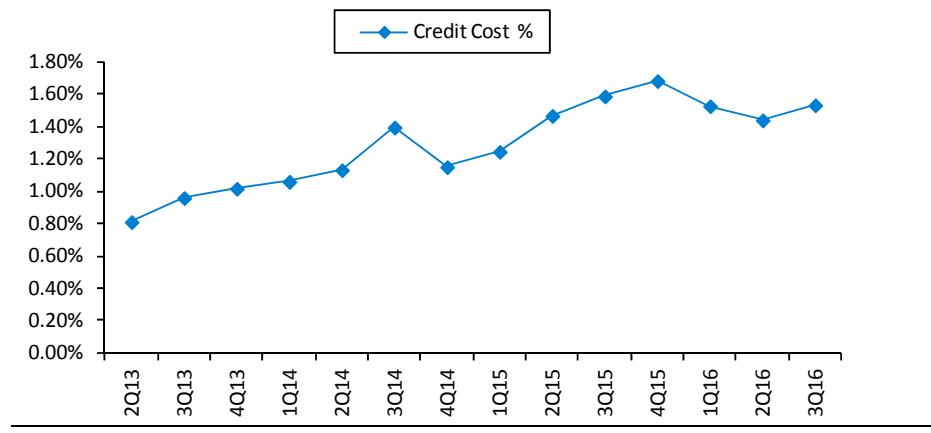
Exhibit 3: LTFH – Asset quality deteriorated on higher delinquencies in farm segment



Source: Company Data, PL Research

Note – 9MFY16 asset quality based on 150dpd

Exhibit 4: LTFH – Credit cost increases further; company carries excess provisions in its balance sheet of Rs2.3bn



Source: Company Data, PL Research

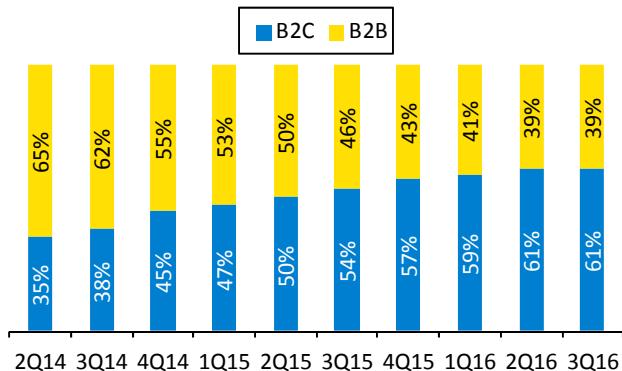
Exhibit 5: L&T Finance – Retail business: High credit cost remains a drag on earnings

L&T Finance (P&L mn)	Q3FY16	Q3FY15	YoY gr.	Q2FY16	QoQ gr.
Interest Income	8,410	8,190	3%	8,600	-2%
Interest Expenses	4,020	4,170	-4%	4,020	0%
Net interest income	4,390	4,020	9%	4,580	-4%
Fee income	400	350	14%	120	233%
Total income	4,790	4,370	10%	4,700	2%
Operating cost	1,670	1,620	3%	1,800	-7%
Operating Profit	3,120	2,750	13%	2,900	8%
Credit cost	1,750	1,260	39%	1,440	22%
Profit before Tax	1,370	1,490	-8%	1,460	-6%
Tax	490	510	-4%	510	-4%
Profit after tax	880	980	-10%	950	-7%
Tax rate (%)	36	34		35	
Gross NPA	12,670	7,960	59%	10,010	27%
Net NPA	8,400	4,570	84%	6,337	33%
Gross NPA (%)	5.9	3.9	199	4.8	107
Net NPA (%)	4.0	2.3	172	3.0	97
Credit Cost (%)	3.3	2.4	85	2.7	57
Yield on loans (%)	15.8	15.9	-11	16.2	-47
Cost of funds (%)	8.9	9.5	-61	8.9	-3
Spreads (%)	6.9	6.4	50	7.3	-44
NIM (%)	8.2	7.8	45	8.6	-39
Tier I (%)	13.9	15.3	-138	14.3	-44
CAR (%)	16.5	17.9	-145	16.8	-33
Disbursement	69,880	52,770	32%	58,430	20%
Loans portfolio (Rs mn)	276,860	239,680	16%	261,860	6%
Retail loans	184,560	152,430	21%	175,260	5%
CV / CE	15,450	24,160	-36%	15,680	-1%
Rural Products Finance	58,450	59,850	-2%	60,720	-4%
Housing Finance	64,350	33,490	92%	55,330	16%
Micro Finance	17,170	6,750	154%	15,100	14%
Personal vehicle	29,140	28,180	3%	28,430	2%
Corporate loans	92,300	87,250	6%	86,600	7%
Supply chain finance	18,750	13,730	37%	18,210	3%
Mid-market finance	73,550	73,520	0%	68,390	8%

Source: Company Data, PL Research

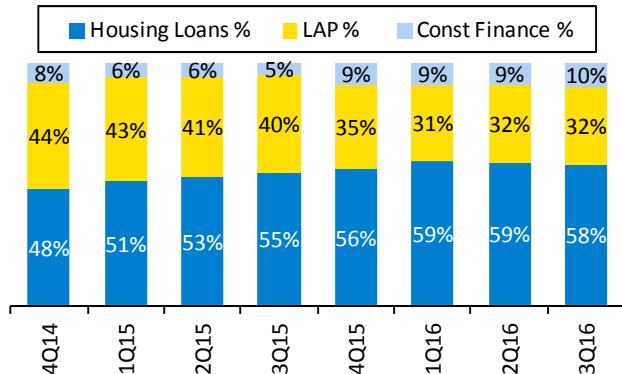
*Note – Q3FY15 GNPA & NNPA based on 180dpd NPA recognition

Exhibit 6: Share of consumers loans (B2C) remains stable



Source: Company Data, PL Research

Exhibit 7: Housing segment continues to report strong growth – mix of individual housing loans remain stable



Source: Company Data, PL Research

Exhibit 8: Margins decline on yield moderation – led by increasing mix of low-yielding housing loans

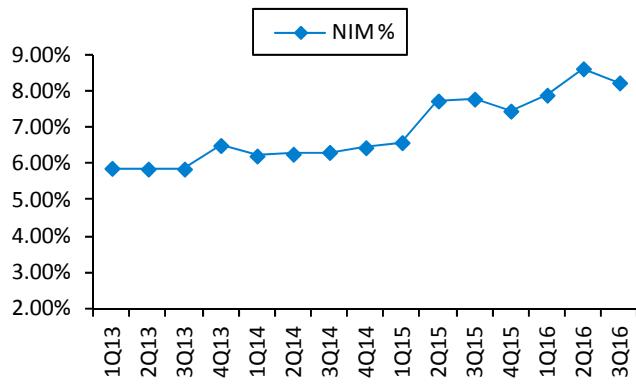
Source: Company Data, PL Research
Note - Excludes housing finance biz

Exhibit 10: Asset quality continues to deteriorate mainly from rural book especially tractors

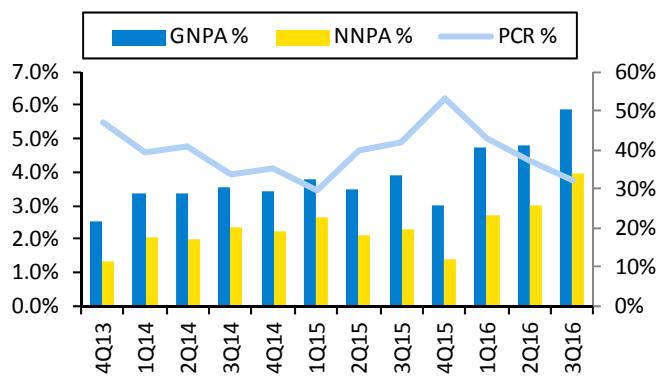
Source: Company Data, PL Research
Note – 9MFY16 asset quality on 150dpd recognition

Exhibit 9: Capital adequacy in retail finance business declines due to dividend payment

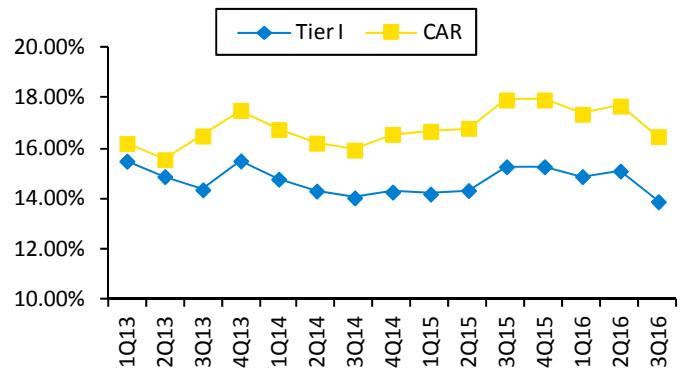
Source: Company Data, PL Research
Note – Tier I excludes housing finance biz

Exhibit 11: Credit cost inches up to over 300bps



Source: Company Data, PL Research

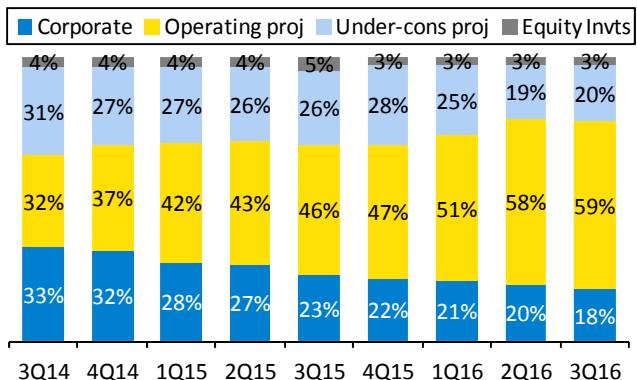
Exhibit 12: L&T Infra Finance – Stable performance

L&T Infra (P&L mn)	Q3FY16	Q3FY15	YoY gr.	Q2FY16	QoQ gr.
Interest Income	7,530	5,950	27%	7,140	5%
Interest Expenses	4,940	4,050	22%	4,840	2%
Net interest income	2,590	1,900	36%	2,300	13%
Fee income	280	340	-18%	210	33%
Total income	2,870	2,240	28%	2,510	14%
Operating cost	180	290	-38%	290	-38%
Operating Profit	2,690	1,950	38%	2,220	21%
Credit cost	1,140	950	20%	950	20%
Profit before Tax	1,550	1,000	55%	1,270	22%
Tax	510	190	168%	270	89%
Profit after tax	1,040	810	28%	1,000	4%
Tax rate (%)	33	19		21	
Gross NPA	4,910	4,840	1%	4,910	0%
Net NPA	3,310	3,720	-11%	3,470	-5%
Gross NPA (%)	1.8	2.3	-49	2.0	-23
Net NPA (%)	1.2	1.8	-55	1.5	-22
Credit Cost	1.7	1.8	-11	1.6	15
Restructured loans %	4.2	5.0	-84	4.8	-63
Net O/s SRs	0.7	0.8	-11	0.8	-9
Yield on loans	11.4	11.5	-11	11.9	-45
Cost of funds	8.5	9.0	-56.7	9.0	-53.7
Spreads	3.0	2.5	45.7	2.9	8.7
NIM	3.9	3.7	24	3.8	11
Tier I (%)	13.4	13.6	-22	13.6	-19
CAR (%)	19.3	16.3	302	19.9	-60
Borrowings	251,780	194,500	29%	225,110	12%
Disbursements	61,520	41,610	48%	32,540	89%
Loans Portfolio (Rs mn)	280,070	216,600	29%	247,990	13%
Thermal power	34,630	30,090	15%	33,080	5%
Renewable power	86,200	48,650	77%	67,240	28%
Power Corp	28,270	25,140	12%	26,750	6%
Roads	64,080	45,190	42%	51,530	24%
Telecom	14,000	13,060	7%	14,110	-1%
Others	52,890	54,470	-3%	55,280	-4%

Source: Company Data, PL Research

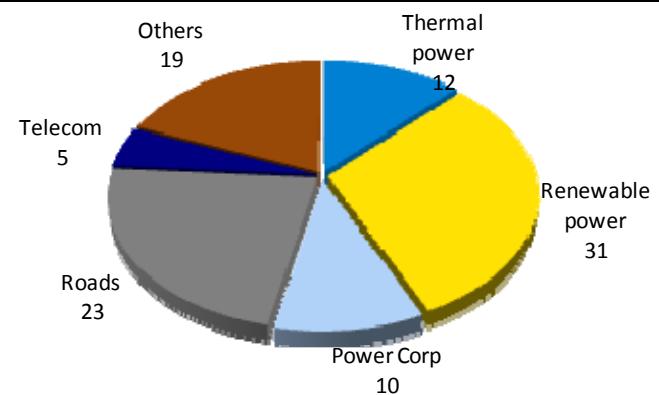
*Note – Q3FY15 GNPs & NNPs based on 180dpd NPA recognition

Exhibit 13: Share of operational projects continues to increase; up 13% YoY



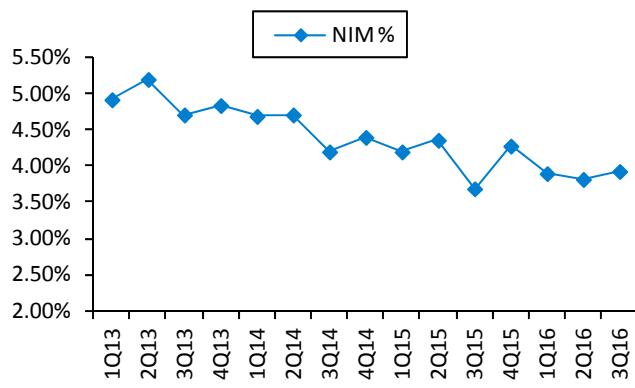
Source: Company Data, PL Research

Exhibit 14: Focus continues to be on renewable, also higher growth in roads was witnessed



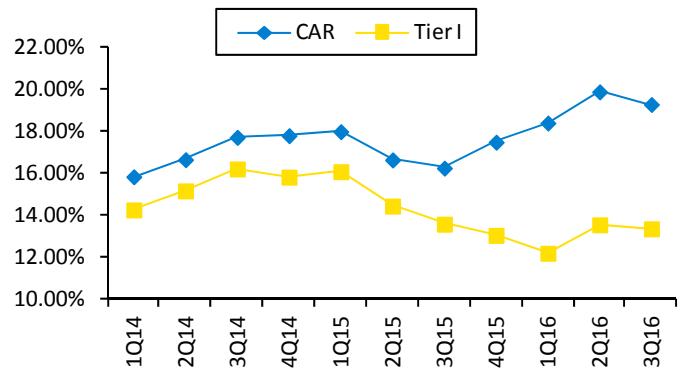
Source: Company Data, PL Research

Exhibit 15: Margins remain largely stable



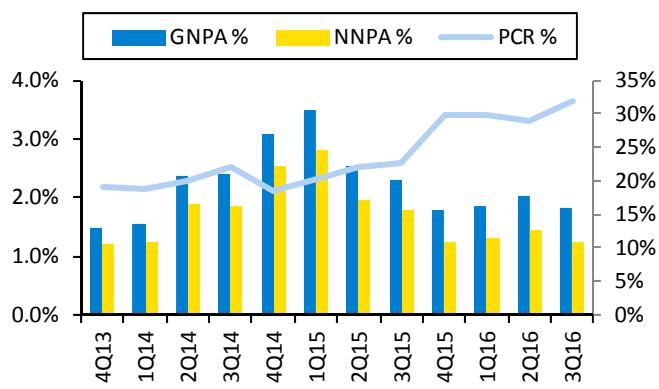
Source: Company Data, PL Research

Exhibit 16: Tier I burn at lower pace but infusion is likely given stronger growth



Source: Company Data, PL Research

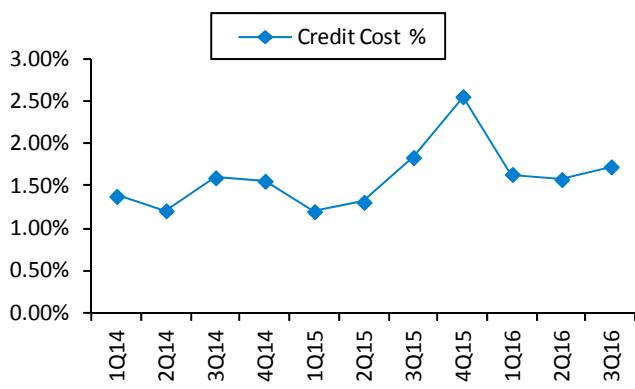
Exhibit 17: Asset quality remains stable with improvement in PCR



Source: Company Data, PL Research

Note - Q1FY16 & Q2FY16 asset quality on 150dpd

Exhibit 18: Credit cost remains steady as well on lower slippages



Source: Company Data, PL Research

Exhibit 19: Earnings change table – We have tweaked our estimates to factor in slightly higher credit costs mainly in the retail business

(Rs m)	Old		Revised		Change		New
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E	FY18E
Net Interest Income	28,684	35,685	28,589	34,393	(0)	(4)	42,009
Operating Profit	19,983	25,306	19,715	23,889	(1)	(6)	30,147
Net Profit	8,745	11,437	8,206	10,305	(6)	(10)	13,578
ABVPS (Rs)	37.0	42.1	32.9	35.9	(11)	(15)	40.1
Price Target (Rs)	80		75				
Reco	BUY		BUY				

Source: Company Data, PL Research

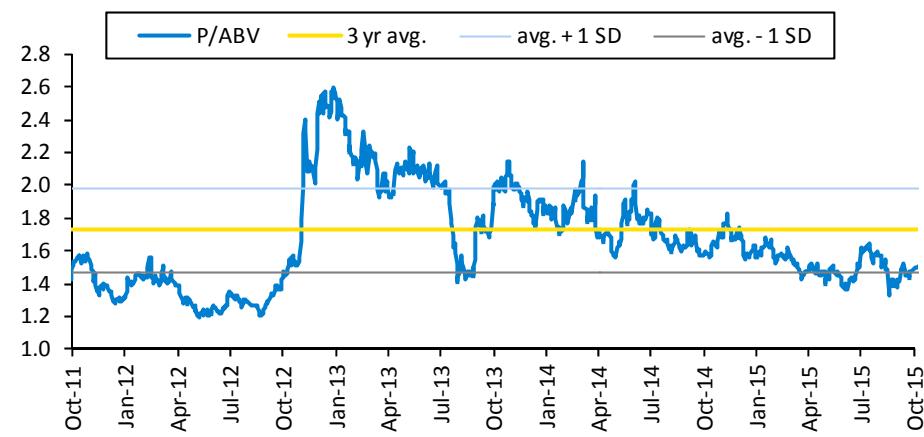
Exhibit 20: We value LTFH on SOTP basis of Rs75 per share based on Sep-17 book

PT calculation and upside

Fair value of LTF	36
Fair value of LTIF	28
Fair value of LTIM	9
Fair value of PE/wealth management	2
Total - Fair value of LTFH	75
Target P/ABV - lending business	1.7
Target P/E	11.6
Current price, Rs	58
Upside (%)	29%
Dividend yield (%)	1%
Total return (%)	30%

Source: Company Data, PL Research

Exhibit 21: LTFH – Historical P/ABV trends



Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2015	2016E	2017E	2018E
Int. Inc. / Opt. Inc.	59,915	71,772	88,334	108,817
Interest Expenses	35,678	43,182	53,940	66,808
Net interest income	24,237	28,589	34,393	42,009
<i>Growth (%)</i>	26.7	18.0	20.3	22.1
Non interest income	3,460	4,151	5,065	6,128
<i>Growth (%)</i>	38.6	20.0	22.0	21.0
Net operating income	27,697	32,741	39,458	48,137
Expenditure				
Employees	3,523	4,298	5,200	6,032
Other expenses	6,293	7,677	9,213	10,687
Depreciation	955	1,051	1,156	1,271
Total expenditure	10,771	13,026	15,569	17,990
PPP	16,926	19,715	23,889	30,147
<i>Growth (%)</i>	35.3	16.5	21.2	26.2
Provision	6,617	7,347	8,348	9,654
Other income	—	—	—	—
Exchange Gain / (Loss)	—	—	—	—
Profit before tax	10,309	12,368	15,541	20,493
Tax	3,241	4,205	5,284	6,968
<i>Effective tax rate (%)</i>	31.4	34.0	34.0	34.0
PAT	7,108	8,206	10,305	13,578
<i>Growth (%)</i>	19.1	15.5	25.6	31.8

Balance Sheet (Rs m)

Y/e March	2015	2016E	2017E	2018E
Sources of funds				
Equity	17,203	17,521	17,521	17,521
Reserves & Surplus	46,562	52,319	58,103	66,062
Networth	63,765	69,840	75,624	83,583
<i>Growth (%)</i>	9.5	9.5	8.3	10.5
Loan funds	420,906	538,704	687,216	866,451
<i>Growth (%)</i>	17.4	28.0	27.6	26.1
Others	—	—	—	—
Minority Interest	—	—	—	—
Deferred Tax Liability	(2,898)	(3,188)	(3,634)	(4,034)
Total	495,407	624,990	784,839	977,634
Application of funds				
Net fixed assets	13,572	14,341	15,107	16,051
Advances	457,631	577,187	727,256	909,070
<i>Growth (%)</i>	18.3	26.1	26.0	25.0
Net current assets	(3,209)	(2,998)	(968)	709
Investments	26,492	34,440	41,328	49,593
<i>Growth (%)</i>	(3.0)	30.0	20.0	20.0
Other Assets	6,642	7,306	8,037	8,840
Total	496,408	624,990	784,839	977,634

Source: Company Data, PL Research.

Quarterly Financials (Rs m)

Y/e March	Q4FY15	Q1FY16	Q2FY16	Q3FY16
Int. Inc. / Operating Inc.	16,346	17,176	17,934	18,198
Income from securitization	—	—	—	—
Interest Expenses	9,291	9,845	9,976	10,146
Net Interest Income	7,056	7,331	7,957	8,052
<i>Growth</i>	21.3	27.0	19.0	18.9
Non interest income	361	408	441	442
Net operating income	7,417	7,739	8,399	8,494
<i>Growth</i>	20.9	2.9	19.4	18.5
Operating expenditure	2,826	3,108	3,392	3,200
PPP	4,591	4,631	5,007	5,294
<i>Growth</i>	25.0	(8.8)	17.9	18.9
Provision	1,986	1,878	1,834	2,035
Exchange Gain / (Loss)	—	—	—	—
Profit before tax	2,605	2,752	3,173	3,259
Tax	573	831	1,029	1,147
Prov. for deferred tax liability	—	—	—	—
<i>Effective tax rate (%)</i>	22.0	30.2	32.4	35.2
PAT	2,056	1,925	2,154	2,120
<i>Growth</i>	10.2	(32.7)	18.6	16.7

Key Ratios

Y/e March	2015	2016E	2017E	2018E
CMP (Rs)	58	58	58	58
Eq. Shrs. O/s. (m)	1,720	1,752	1,752	1,752
Market Cap (Rs m)	100,035	101,886	101,886	101,886
Market Cap to AUM (%)	20.2	16.3	13.0	10.4
EPS (Rs)	3.5	3.8	4.7	6.3
Book Value (Rs)	37.1	39.9	43.2	47.7
Adjusted Book Value (Rs)	33.7	32.9	35.9	40.1
P/E (x)	16.7	15.4	12.3	9.2
P/BV (x)	1.6	1.5	1.3	1.2
P/ABV (x)	1.7	1.8	1.6	1.5
DPS (Rs)	0.8	0.9	1.2	1.5
Dividend Yield (%)	1.4	1.5	2.1	2.6

Asset Quality

Y/e March	2015	2016E	2017E	2018E
Gross NPAs (Rs m)	10,450	18,609	19,369	20,338
Net NPAs (Rs m)	5,800	12,121	12,653	13,388
Gross NPAs to Gross Adv. (%)	2.3	3.2	2.7	2.2
Net NPAs to Net Adv. (%)	1.3	2.2	1.9	1.6
NPA Coverage (%)	44.5	34.9	34.7	34.2

Profitability (%)

Y/e March	2015	2016E	2017E	2018E
NIM	5.3	5.1	4.9	4.8
RoAA	1.1	1.1	1.2	—
RoAE	9.8	9.9	11.3	13.9

Source: Company Data, PL Research.

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