

**SECTOR WATCH** Niche play, likely rebound in rural consumption and good asset quality have lifted NBFC stocks. ET checks out their real-worthiness

# Should You Ride the Rally in NBFC Stocks?

Sanket Dhanorkar

Over the past few months, shares of non-banking financial companies have been on a joyride even though the bad-loan problem has dragged banking stocks down. NBFC stocks have even trumped stocks of private banks, which had been hitherto investors' favourites. Some NBFC shares have surged 60-80% in the current rally with investors buying these based on the higher growth numbers and superior asset quality reported by them.

But does the risk-reward equation favour investment in NBFC stocks at current levels? The earnings for the March quarter clearly reveal a wide gap in the quality of financials between the banking and non-banking segments. On an aggregate level, profit after tax for private sector banks increased by 23% while that for NBFCs rose 32%. Public sector banks suffered huge losses due to stricter non-performing asset provisioning while NBFCs managed to clock this growth maintaining a healthy asset quality in their loan book.

These players are making their presence felt in the credit space, across segments, eating into the market share of banks. With banks focused on fire-fighting the NPA problem, NBFCs' healthier books have put them in a better position to expand their loan book. Housing finance is one segment where NBFCs have shone bright.

A Crisil report says share of NBFCs in the housing finance industry has increased from 26% to 38% shrinking the share of banks from 74% to 62%. This rising trend apart, NBFCs already dominate segments like auto finance and consumer durable finance.

## NICHE PLAY IS FINE

The rural, semi-urban focus offered by these players (NBFCs) has attracted the attention of investors

**Ambareesh Baliga**

Independent Market Analyst

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## COMPANY

COMPANY	CMP	P/BV	3 month return (%)	1 year return (%)
Cholamandalam Investment and Finance	964	4.1	44.2	64.9
GIC Housing Finance	275	2.0	30.8	33.1
Repcos Home Finance	745	4.9	28.9	26.3
Shriram Transport Finance Company	1,160	2.6	25.4	41.3
Gruh Finance	279	12.2	19.3	27.5
Sundaram Finance	1,428	4.2	16.4	-2.6
Bajaj Finance	7,498	6.5	15.9	59.0
Canfin Homes	1,185	3.6	15.6	77.1
Dewan Housing Finance Corp	203	1.1	10.8	4.6
Housing Development Finance Corp	1,207	3.8	8.4	-0.6
SREI Infrastructure Finance	59	0.8	7.5	81.1
LIC Housing Finance	471	2.6	3.7	19.0

CMP is current market price; P/BV is price to book value

Data as on 13/06/2016

COMPILED BY ETIG DATABASE

The focused approach of NBFCs has made them investor favourites while they are perceived to be best placed to tap opportunities arising from the base of the pyramid. Several microfinance-focused NBFCs as well as home finance providers catering to low ticket-size borrowers are in the limelight for this reason. Most of these NBFCs offer a play on bountiful monsoon which is expected to revive rural consumption. Higher disposable income in the hands of rural households would likely see an expansion in the loan books of these companies.

"The rural, semi-urban focus offered by these players has attracted the attention of investors," says Ambareesh Baliga, a Sebi-registered independent market analyst. Microfinance institutions-turned small finance banks Equitas Holdings and Ujjivan Financial Services both enjoyed spectacular debuts on the bourses riding on the same theme. The two stocks are currently trading at 58% and 72% above their offer price. Lalit Nambiar, fund manager at UTI Mutual Fund, reckons some NBFCs have benefited due to their exposure

## A WORD OF CAUTION

We do not doubt the credit processes...but highlight that the stocks have rallied on hopes of growth in assets

### A Report

Kotak Securities

to niche segments like tractors or HCV finance. Shriram Transport Finance and Sundaram Finance are leaders in this segment. Home finance firms such as CanFin Homes, Gruh Finance and Repco Home Finance are gaining because of their presence in the lower income segments.

These lenders can benefit from a Budget provision that allows first-time home buyers more deduction for interest payment of ₹50,000 per annum for loans up to ₹35 lakh sanctioned during this financial, provided the home value is less than ₹50 lakh.

### WHAT SHOULD YOU DO

Clearly, NBFCs have been an alter-

nate play in the financial services space with investors moving away from richly valued private bank stocks. But do these stocks provide good buy opportunity at current levels? Valuations have surged in the recent run-up with Bajaj Finance and Sundaram Finance trading at 6.5 times and 4.2 times the book value, respectively. To boot, housing finance major HDFC — the largest listed NBFC — is trading at 3.8 times its book value.

Some analysts suggest it is time to be cautious given the risk-reward equation is less favourable. Kotak Securities in a report notes how the banking and financial services sector has seen an astonishing change in perception in the past few weeks and cautions against over-optimism in NBFC stocks. "We note that the market had been quite prompt to award the rapid growth in assets of banks over the past few years, only to regret it later," the report points out adding, "We do not doubt the credit processes of NBFCs but simply highlight that the stocks have rallied sharply on hopes of...growth in their assets."