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IPO Note – Aptus Value Housing Finance India Limited

08-August-2021

RETAIL RESEARCH

Issue Snapshot:
Issue Open: Aug 10 – Aug 12 2021

Price Band: Rs. 346 – 353

*Issue Size: 78,755,001 eq shares
(Fresh issue of 500 cr + offer for sale of 64,590,695 eq sh cr)

Issue Size: Rs.2724.9 – 2780.0 cr

Reservation for:

QIB	Upto	50% eq sh
Non Institutional	atleast	15% eq sh
Retail	Upto	35% eq sh

Face Value: Rs 2

Book value: Rs 41.12 (Mar 31, 2021)

Bid size: - 42 equity shares and in multiples thereof

100% Book built Issue

Capital Structure:

Pre Issue Equity:	Rs. 96.28 cr
*Post issue Equity:	Rs. 99.12 cr

Listing: BSE & NSE

Book Running Lead Managers: ICICI Securities Ltd, Citigroup Global Markets India Private Ltd, Edelweiss Financial Services Ltd, Kotak Mahindra Capital Company Ltd

Registrar to issue: Link Kfin Technologies Private Ltd

Shareholding Pattern

Shareholding Pattern	Pre issue %	Post issue %
Promoter and Promoter Group	74.9	72.2
Public	25.1	27.8
Total	100.0	100.0

*=assuming issue subscribed at higher band
Source for this Note: RHP

Background & Operations:

Aptus Value Housing Finance India Ltd (AVHFL) is an entirely retail focussed housing finance company primarily serving low and middle income self-employed customers in the rural and semi-urban markets of India. The Company had the highest RoA of 5.7% among the Peer Set during the financial year 2021. It is one of the largest housing finance companies in south India in terms of AUM, as of March 31, 2021. AUM has increased from Rs. 22,472.33 million, as of March 31, 2019 to Rs. 40,677.62 million, as of March 31, 2021, at a CAGR of 34.54%. It had the lowest cost to income ratio among the Peer Set during the financial year 2021. Operating Expenses to Net Income Ratio for the financial year 2021 was 21.80%. Since the inception of the Company, it has not restructured any loans or written-off any loans receivable and as of March 31, 2021, March 31, 2020 and March 31, 2019, its Gross NPAs expressed as a percentage of Gross Loan Assets was 0.68%, 0.70% and 0.40%, respectively. During the financial years 2021, 2020 and 2019, its Credit Costs to Average Total Assets was 0.14%, 0.11% and 0.06%, respectively.

AVHFL offers customers home loans for the purchase and self-construction of residential property, home improvement and extension loans; loans against property; and business loans, which accounted for Rs. 21,032.10 million, or 51.70%, Rs.8903.39 million, or 21.89% and Rs. 10,742.13 million, or 26.41% of its AUM, as of March 31, 2021, respectively. It only offers loans to retail customers and do not provide any loans to builders or for commercial real estate. It targets first time home buyers where the collateral is a self-occupied residential property and do not provide any loans with a ticket size above Rs.2.50 million and the average ticket size of its home loans, loans against property and business loans on the basis of disbursement amounts was Rs.0.72 million, Rs.0.71 million and Rs.0.62 million, as of March 31, 2021, respectively. As of the same date, its home loans, loans against property and business loans had an average loan-to-value of 38.89%, 38.27% and 39.21%, respectively, at the time of sanctioning of the loans.

The Company has diversified its geographical presence by adopting a strategy of contiguous expansion across regions and is focused on achieving deeper penetration in its existing markets. As of March 31, 2021, the states of Tamil Nadu (including the union territory of Puducherry), Andhra Pradesh, Karnataka and Telangana accounted for Rs. 21,263.74 million, or 52.27%, Rs. 11,116.08 million, or 27.33%, Rs. 4,038.13 million, or 9.93% and Rs. 4,259.67 million, or 10.47% of its AUM, respectively, and it had a network of 190 branches covering 75 districts in such states and the union territory of Puducherry. It had the largest branch network in south India among the Peer Set, as of March 31, 2021. Over the years, AVHFL has successfully grown its presence outside its home state of Tamil Nadu, which accounted for Rs. 13,418.55 million, or 59.71% of its AUM, as of March 31, 2019. It has increased the number of its branches from 142 as of March 31, 2019 to 190 as of March 31, 2021. It categorizes its branches on the basis of the duration since the commencement of its operations and as of March 31, 2021, it had 108 branches that were operational for over three years with AUM of Rs. 32,298.90 million, while 82 branches were operational for less than three years with AUM of Rs. 8,378.72 million.

AVHFL' financing requirements historically has been met from several sources, including refinancing from the NHB, financing from IFC, term loans, working capital loans and issuance of non-convertible debentures ("NCDs") to meet capital requirements. It also monetizes loans through securitization to banks and financial institutions, which enables to optimize its cost of borrowings, liquidity and capital. As of March 31, 2021, March 31, 2020 and March 31, 2019, Total Borrowings were Rs. 25,150.66 million, 20,216.45 million and Rs. 16,060.62 million and average cost of borrowings was 9.11%, 10.17% and 9.48%, respectively. As of March 31, 2021, the weighted average tenure of outstanding borrowings was 83.3 months and credit ratings were ICRA A+ (Stable) and CARE A+ (Stable). As of the same date, the Company had a positive asset-liability position across all maturity buckets. It seeks to improve the standard of living of its customers and include them into the financial mainstream. Its presence in the rural and semi urban markets of India also provides employment opportunities in these regions since it primarily recruits its employees locally. As of March 31, 2021, it employed 1,913 personnel.

Objects of Issue:

The Offer comprises of the Fresh Issue and an Offer for Sale.

Offer for Sale

Padma Anandan, Aravali Investment Holdings, JIH II, LLC, GHIOF Mauritius, Madison India Opportunities IV, KM Mohandass HUF*, R Umasuthan** and Saurabh Vijay Bhat (collectively, referred to as the "Selling Shareholders"), shall be entitled to the proceeds of the Offer for Sale, net of their proportion of Offer-related expenses and the relevant taxes thereon. AVHFL shall not receive any proceeds from the Offer for Sale.

Fresh Issue

The Company proposes to utilize the Net Proceeds from the Fresh Issue towards fully augmenting the tier I capital requirements of the Company. Considering tier, I position, AVHFL has no plans to augment the tier II capital in the near future. In case the Company decides to augment its tier II capital in the future, it shall be in compliance with the RBI Master Directions for the HFCs. The main objects clause of its Memorandum of Association enables it to undertake the activities for which the funds are being raised by it in the Fresh Issue.

The following table sets forth certain key financial and operational information, as of and for the years indicated:

	As of and for the financial year ended March 31		
Metric (Rs in million)	2021	2020	2019
AUM	40677.62	31786.94	22,472.33
Growth rate of AUM	28%	41%	59%
Gross Loan Book	40,648.75	31,720.19	22,341.31
Disbursements	12,981.81	12,709.80	10,890.42
Total Income	6,552.42	5,237.20	3,371.15
Profit for the year	2,669.44	2,110.12	1,114.83
Net Worth	19,794.54	17,090.13	6,983.75
AUM / Net Worth	2.05	1.86	3.22
Return on Total Assets	6.46%	6.95%	5.91%
Return on Equity	14.47%	17.53%	17.38%
Gross NPAs	276.2	222.45	89.28
Gross NPAs / Gross Loan Assets	0.68%	0.70%	0.40%
Net NPAs / Gross Loan Assets	0.49%	0.54%	0.30%
Average Yield on Gross Loan Book	17.24%	17.95%	17.13%
Average cost of borrowings (including securitization)	9.11%	10.17%	9.48%
Net Interest Margin	10.10%	9.90%	10.32%
Operating Expenses to Net Income	21.80%	26.08%	30.34%
Operating Expenses to Average Total Assets	2.37%	2.91%	3.55%
Credit Cost to Average Total Assets	0.14%	0.11%	0.06%
Capital Adequacy Ratio	73.63%	82.49%	43.64%
Number of branches	190	174	142
Live accounts (including securitised accounts)	58,069	43,987	30,749

Recent Developments

The following table sets forth certain key operational information, as of the dates (or for the periods then ended) indicated:

Metric	As of July 10, 2021	As of March 31, 2021
AUM (₹ million)	42,668.11	40,677.62
Gross Loan Book (₹ million)	42,643.18	40,648.75
Disbursement (₹ million)	3,101.01*	4,193.32 #
Gross NPA** (₹ million)	855.32	276.2
Gross NPAs / Gross Loan Assets	2.00%	0.68%
Net NPAs / Gross Loan Assets	1.69%	0.49%
Collection Efficiency	93.94%	99.76%
Live accounts (including securitized accounts)	60,305	58,069
Number of branches	192	190

Figures disclosed in the table above are not measures of financial position, operating performance or liquidity defined by generally accepted accounting principles and may not be comparable to similarly titled measures presented by other companies.

** Disbursement numbers are for the period from April 1, 2021 to July 10, 2021.*
 # Disbursements numbers are for the three months ended March 31, 2021.
*** We have not restructured any loans under resolution framework for COVID-19 related stress (Resolution framework 2.0).*

Competitive Strengths

Presence in large, underpenetrated markets with strong growth potential: AVHFL is one of the largest housing finance companies in south India in terms of AUM, as of March 31, 2021. Its AUM has grown at a CAGR of 34.54% from Rs.22,472.33 million as of March 31, 2019 to Rs.40,677.62 million as of March 31, 2021. As of March 31, 2021, the states of Tamil Nadu (including the union territory of Puducherry), Andhra Pradesh, Karnataka and Telangana accounted for Rs.21,263.74 million, or 52.27%, Rs.11,116.08 million, or 27.33%, Rs.4,038.13. million, or 9.93% and Rs.4,259.67 million, or 10.47% of its AUM, respectively, and it had a network of 190 branches covering 75 districts in such states and the union territory of Puducherry. It had the largest branch network in south India among the Peer Set, as of March 31, 2021. These four states have high per-capita incomes, better financial literacy and GDP growth rates. Further, its market shares for home loans among housing finance companies with assets under management of up to Rs.150 billion in Tamil Nadu, Andhra Pradesh, Karnataka and Telangana was 21.3%, 11.7%, 7.7% and 6.5% as of December 31, 2020, respectively, ensuring that its leading position in these states offers high growth potential. As a result, AVHFL is well positioned to capitalize on growth opportunities and cater to the housing finance requirements of its target customer base in these geographies.

Robust risk management architecture from origination to collections leading to superior asset quality: AVHFL has implemented a robust risk management architecture to identify, monitor and mitigate risks inherent in its lending operations. As a result, it has maintained its asset quality across economic cycles including events such as demonetization, the implementation of the Goods and Services Tax, the liquidity crisis that was triggered by defaults by large financial services companies and the COVID-19 pandemic. As of March 31, 2021, March 31, 2020, and March 31, 2019, Gross NPAs expressed as a percentage of Gross Loan Book were 0.68%, 0.70% and 0.40%, (the GNPA for rural portfolio was 0.68%, 0.72% and 0.49% and the same for urban portfolio was 0.71%, 0.67% and 0.28%) while its Net NPAs expressed as a percentage of Net Loan Assets were 0.49%, 0.54% and 0.30%, respectively. Further, it has not restructured any loans or written-off any loans receivable since the inception of the Company.

AVHFL operates its business in a centralized manner and has set up separate internal verticals for its sales, legal, technical and collection functions who report independently to its head office. Its personnel at branch offices are responsible for sales, customer service, field verification and collection functions, while credit assessment and disbursement of loans is undertaken at the central office. It has a credit officer at its branches who is responsible for collating and verifying relevant documentation, conducting reference checks and responding to basic queries. It has created over 60 types of customer profiles to assist with credit assessment and also have a credit application, which helps verify details of a customer's residence and business and is integrated with its core lending application for credit evaluation.

After the disbursement of a loan, AVHFL closely monitor loan accounts for the first 15 to 24 months to check for early signals of potential defaults and conduct post disbursement audits. It also conducts site visits after three months of disbursing a loan and periodically thereafter. It utilizes its analytics platform to maintain different templates of customer profiles and increase business while managing risks. It also conducts stress testing of its portfolio, a portfolio-wise analysis, pin-code wide analysis and sourcing-wise analysis to check for probability of defaults. Further, it monitors profile-wise concentration risk at the portfolio level as well as for individual profiles at each of its branches. It also performs analysis on lagged delinquency and executive wise delinquencies. The Company has also entered into arrangements with insurance companies to offer credit shield insurance and property insurance to its customers.

In-house operations leading to desired business outcomes*:* AVHFL conducts all aspects of its lending operations in-house including sourcing, underwriting, valuation and legal assessment of collateral and collections, which enables to maintain direct contact with its customers, reduce turn-around-times and the risk of fraud. It sources customers directly through its sales team, which comprised over 1,085 personnel as of March 31, 2021. A direct sourcing model has helped to maintain contact with customers and establish strong relationships with them, led to customer referrals, high levels of customer satisfaction and increased loyalty. It has also helped mitigate underwriting and default risks by enabling it to have a customer base with a better credit profile. Its in-house sourcing model helps it make a better credit evaluation of customers on a wide range of parameters after collating all customer information in its database. It has also developed up in-house teams for property evaluation, property valuation, conducting legal assessments and collections. As of March 31, 2021, its legal and technical team comprised over 206 personnel.

AVHFL is a customer centric organization and has developed strong relationships with its customers by addressing its concerns in availing housing finance. It seeks to maintain high levels of customer service and has set up a centralized customer relationship management department. It sends regular updates to customers on the status of its loan applications and remind them of their payment schedules through text messages. Its customer centric approach has been a key driver of growth and helped it differentiate itself from competition.

Domain expertise built over time resulting in a business model difficult to replicate by others in geographies: AVHFL is an entirely retail focussed housing finance company primarily serving low and middle income self-employed customers in the rural and semi-urban markets of India. It commenced its business in June 2010 and its operations are currently focused in the states of Tamil Nadu, Andhra Pradesh, Karnataka and Telangana. It targets first time home buyers where the collateral is a self-occupied residential property. Since it primarily caters to self-employed customers, many of who are new to credit and do not have formal income proofs such as pay slips or income tax returns, it assesses their income through various methods and conduct a cash flow assessment of their income to determine ability to repay loans. AVHFL has developed an in-depth understanding of the requirements of customers in these regions and methods to determine its credit worthiness. Over years, it has studied and developed credit assessment models specific to over 60 types of customer profiles. Some of its profiles are customized to regions and specific types of employment. on account of its domain expertise to underwrite self-employed customers with limited income proofs, it has been able to effectively serve customers, grow business and create a business model that is difficult to replicate in its geographies.

Experienced and stable management team with marquee shareholders: AVHFL has an experienced management team, which is supported by qualified and experienced operational personnel. Its Promoter, Chairman and Managing Director, M. Anandan, has over 40 years of experience in the financial services sector, and has previously served as the managing director of Cholamandalam Investment and Finance Company Limited, part of the Murugappa Group and was also managing director of Cholamandalam MS General Insurance Company Limited. It has successfully recruited and retained talented employees from a variety of backgrounds, including credit evaluation, risk management, treasury, technology and marketing. Its senior managers have diverse experience in various financial services and functions related to its business. The knowledge and experience of senior and mid-level management team members provides with a significant competitive advantage as it seeks to grow business and expand to new geographies. It has and expect to continue to benefit from strong capital sponsorship and professional expertise of its marquee shareholders. Its shareholders have assisted it in implementing strong corporate governance standards, capital raising and strategic business advice, which has been critical to the growth of its business.

Established track record of financial performance with industry leading profitabili*ty:* AVHFL focus on serving self-employed customers has resulted in high yields for its loan portfolio. As of March 31, 2021, its average yield on disbursements was 16.88%, with home loans, loans against property and business loans accounting for 15.38%, 17.00% and 20.45%, respectively. Further, as of March 31, 2020, its average yield on disbursements was 17.18%, with home loans, loans against property and business loans accounting for 15.57%, 17.00% and 20.40%, respectively. Moreover, as of March 31, 2019, average yield on disbursements was 17.23%, with home loans, loans against property and business loans accounting for 15.64%, 17.00% and 20.30%, respectively. Its loan portfolio also qualifies for priority sector lending. It lay emphasis on improving cost efficiencies by monitoring and controlling its operating costs and it typically set up its branches in an economical manner. During the financial years 2021, 2020 and 2019, its Credit Costs to Average Total Assets was 0.14%, 0.11% and 0.06%, respectively. Its AUM per employee grew from Rs.17 million as on financial year 2019 to Rs.21.26 million as on March 31, 2021. This indicates its focus on low credit costs which has resulted in high Return on Assets. The Company is able to access borrowings at a competitive cost due to its credit ratings, stable credit history, conservative risk management policies and strong brand equity.

Focus on the social impact of busines*s:* AVHFL focus on the social impact of its business and seeks to improve the standard of living of its customers. Its presence in the rural and semi urban markets of India also provides employment opportunities in these regions since it primarily recruits its employees locally. Many of AVHFL's loans are provided under the affordable housing schemes promoted by the Government of India, such as the Pradhan Mantri Awas Yojana, which benefit the economically weaker section and low and middle income groups in semi urban and rural areas. Its customers are generally not served by the mainstream financial services sector and by providing them employment opportunities, it is fulfilling an important social objective of economic upliftment for these segments of the Indian society.

Business Strategy:

Continue to focus on low and middle income self-employed customers in rural and semi-urban markets: AVHFL primarily serves low and middle income self-employed customers in rural and semi-urban markets. As an organization, it believes in the social impact of its business and operate a financially inclusive customer centric business model. It seeks to improve the standard of living of its customers and include them into the financial mainstream. It has focused on disbursing loans which has an average ticket size in the range of Rs.0.5 million to Rs.1.5 million and intends to continue to focus on serving such customer base and increase overall market share. The housing shortage in India is estimated to increase to 100 million units by 2022, of which 95% of the household shortage will be from the lower income group and economic weaker section, while the remaining 5% will be from the middle income group or above. This customer segment offers significant growth opportunities since it is primarily new to credit customers, without formal income proofs and are unserved or underserved by formal financial institutions. AVHFL continue to disburse loans only to retail customers for the purchase or construction of self-occupied homes as part of its risk mitigation strategy.

Increase penetration in existing markets and expand branch network in large housing markets: AVHFL operations are currently focused in the states of Tamil Nadu (including the union territory of Puducherry), Andhra Pradesh, Karnataka and Telangana and had a network of 190 branches in these states and the union territory of Puducherry, as of March 31, 2021. It intends to continue to expand its presence in an on-ground contiguous manner in order to achieve deeper penetration in these regions. It also intends to expand its branch network in large housing markets in the states of Maharashtra, Odisha and Chhattisgarh. Its operating model is scalable and will assist it expand its operations with lower incremental costs to drive efficiency and profitability.

Continue to be an asset quality focused financier: AVHFL intends to grow its business while focussing on maintaining asset quality. It has maintained its asset quality across economic cycles including events such as demonetization, the liquidity crisis that was triggered by defaults by large financial services companies and the COVID-19 pandemic. It was able to consistently perform well through such macroeconomic challenges due to several factors including its risk management architecture, the strength of management team and proactive measures undertaken during such periods.

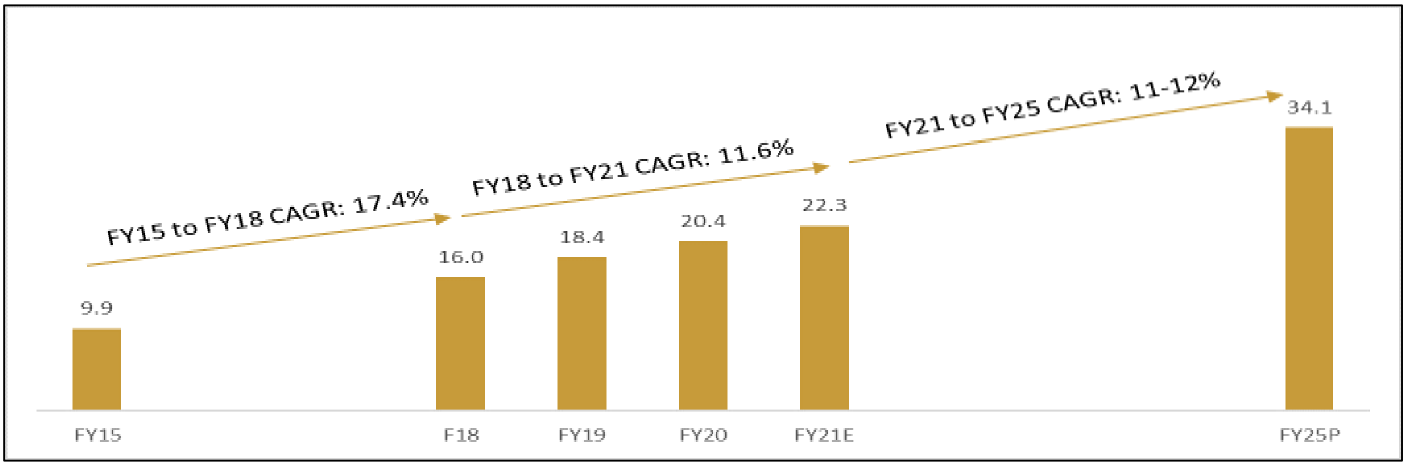
Reduce cost of borrowings by diversifying sources of borrowing and improving credit rating: AVHFL seeks to reduce its average cost of long term borrowings through improved credit ratings and by diversifying its borrowing profile. It has historically secured financing from private and public sector banks, the NHB, through the issuance of NCDs and securitization transactions. It has been able to obtain cost-effective financing and optimize its borrowing costs due to several factors including improved credit ratings and financial performance. Its credit ratings by both ICRA and CARE are ICRA A+(Stable) and CARE A+; Stable, respectively as of March 31, 2021. It has also reduced its average cost of borrowings including securitization from 10.17% as of March 31, 2020 to 9.11% as of March 31, 2021. As it continues to grow the scale of its operations, it seeks to reduce its dependence on term loans, reduce its cost of funds and continue to improve its credit ratings. It also intends to increase lender base which has grown from 14 as of March 31, 2019 to 17 as of March 31, 2021.

Industry

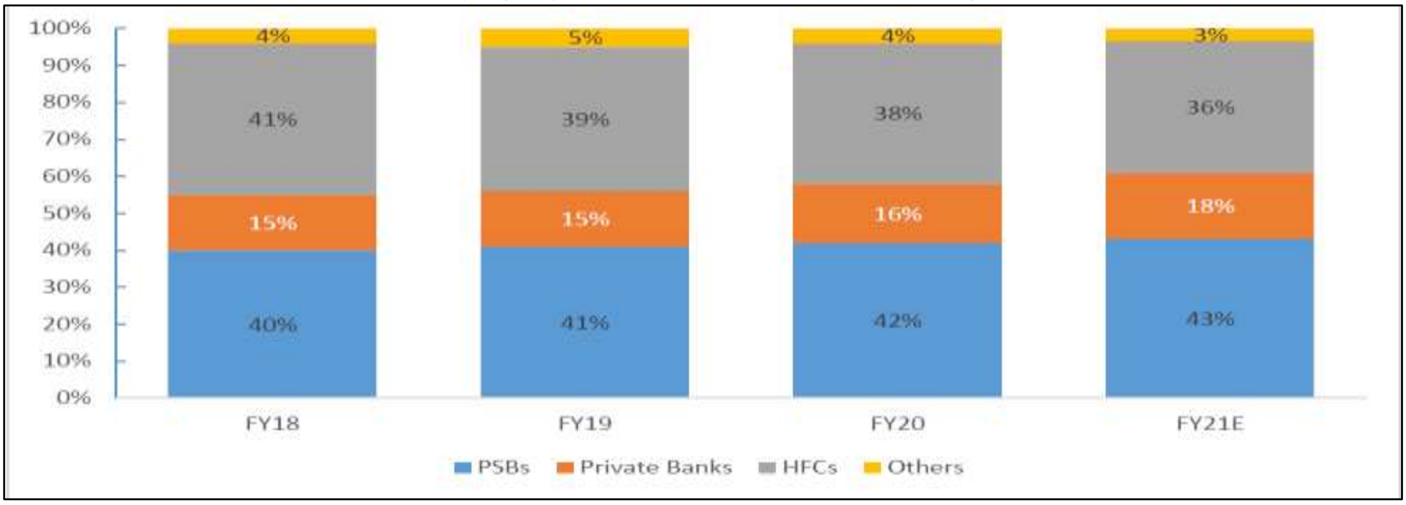
Indian housing finance market

Overall housing finance market to log a CAGR of 11-12% in the long term

The Indian housing finance market clocked a healthy CAGR of approximately 12% (growth in loan outstanding) over Fiscals 2018 to 2021 on account of a rise in disposable income, healthy demand emanating from smaller cities and markets, attractive interest rates and government impetus on housing. In the past also, the housing finance market has shown secular growth with outstanding loans increasing from Rs. 9.9 billion as of FY15 to Rs 16 trillion as of FY18, translating into a CAGR of 17.4%. Growth in housing loans outstanding (Rs trillion).



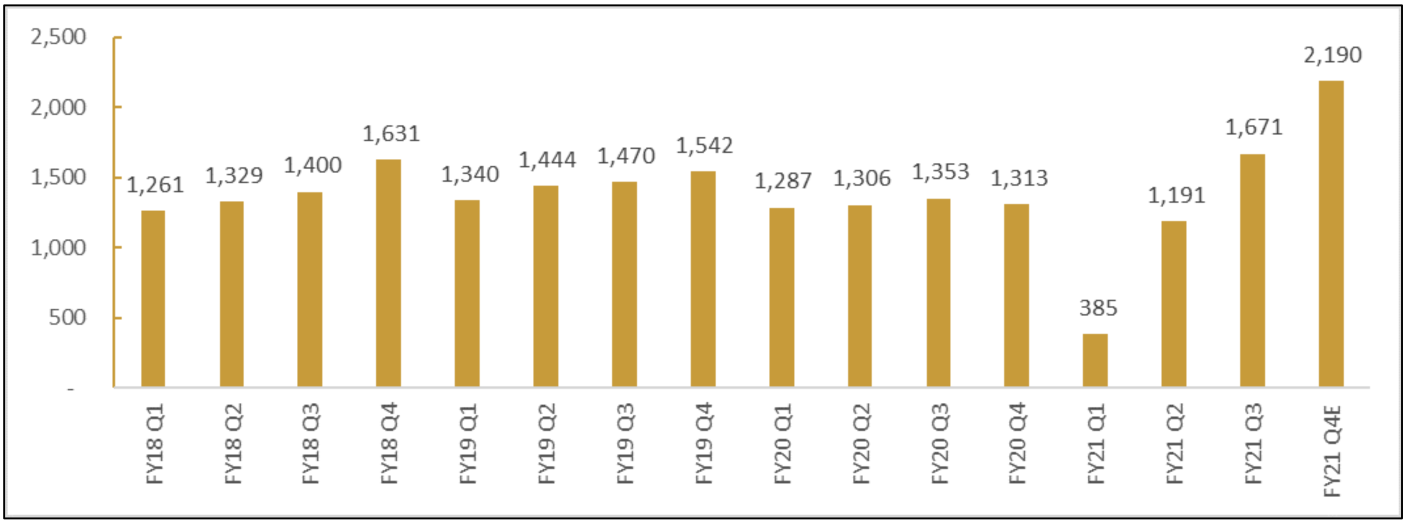
Player group wise share in home loans outstanding



Total home loans outstanding in the country is estimated at approximately Rs. 22.3 trillion as of March 2021, approximately double the amount five years back. Growth slowed down somewhat from the earlier years in Fiscals 2019 and 2020 in the wake of sluggish growth of HFCs post the IL&FS crisis and economic slowdown, respectively in addition to the tighter liquidity conditions faced by the NBFCs and HFCs. However, the latent demand for housing in India remains strong, given the vast housing shortage in India and the psychological comfort provided by owning a house post the uncertainty created by the COVID-19 pandemic. With low disbursements and low repayments in the first half of Fiscal 2021, growth of housing loans outstanding of HFCs and NBFCs was low at 1% to 3% on-year as on September 2020 as compared to March 2020. Sharp revival of the economy subsequently propelled an increase in disbursements to all-time highs in the third and fourth quarters of Fiscal 2021, with disbursements even crossing the quarterly averages of Fiscal 2020. CRISIL Research expects the home loan market to bounce back more strongly in the long term and grow at 11-12% CAGR in between Fiscals 2021 and 2025.

Home loan enquiries have increased post the first quarter of Fiscal 2021 on the back of pent up demand, reduced interest rates and attractive schemes provided by developers and have continued the trend in the third quarter as well. There is some demand for balance transfers of existing loans as well due to the attractive home loan rates. Home prices too have seen a drop in some markets, and this, along with steps taken by state governments such as reduction in stamp duty for homes registered during a certain period, has made home buying more attractive for consumers. However, the players are still a little cautious in retail lending and have become conservative in customer selection. The approval rates are below the pre-COVID-19 levels but are better than in the previous months this fiscal.

Home loans disbursements have grown post the first quarter into the pandemic (Rs billion)



Share of top 15 states in housing loan outstanding

The housing loan market remains fairly concentrated in top 15 states which account for ~92% of the loan outstanding as of March 2020. Maharashtra tops with the overall share of 23% followed by Karnataka (10%), Tamil Nadu (10%), Gujarat (8%) and Uttar Pradesh (6%). Cumulatively, the top four states account for half (50%) of the housing loans outstanding as of March 2020. Within these, out of the top 7, 4 of the states are from the southern region of the country.

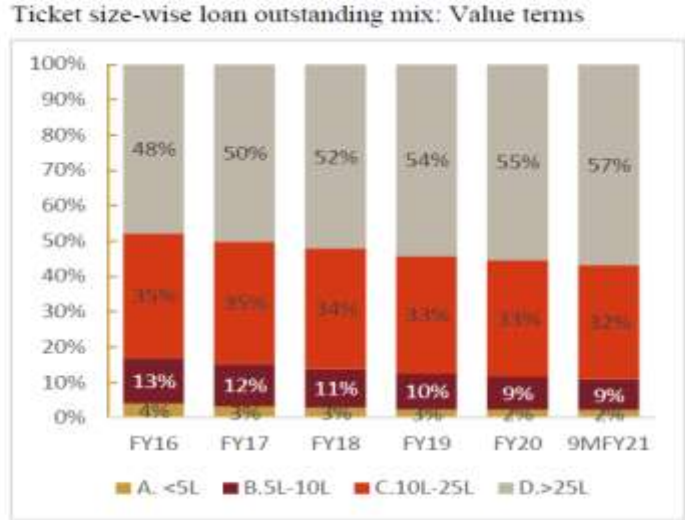
Top 15 states accounts for more than 90% of overall housing finance outstanding

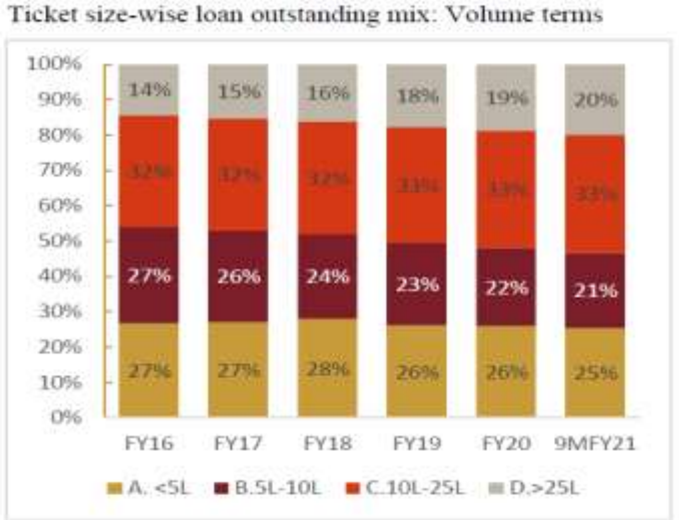
The size of the housing finance market in a state is strongly linked to its level of GDP and economic growth. The top 8 states viz. Maharashtra, Karnataka, Tamil Nadu, Gujarat, Uttar Pradesh, Telangana, Andhra Pradesh, and Delhi account for ~70% of the overall housing loans outstanding in the country. Going forward also, AVHFL expect these markets to continue to drive the industry volumes, given the sheer population in these states and the level of industrial activity. Increasing upcoming supply into mid ticket size segments and strong progress in PMAY houses sanctioned/ completed are also key factors that will support growth. Furthermore, players are also likely to focus more on markets that exhibit relatively lower delinquency trends compared to other markets.

Amongst the top 15 states, Bihar recorded the fastest CAGR (FY16 to FY20) of 27% in housing loans growth, followed by Andhra Pradesh at 22%. In terms of asset quality, Telangana had the lowest GNPA ratio of 0.9% as of fiscal 2020, followed by Andhra Pradesh (1.3%), Rajasthan (1.5%) and Gujarat (1.8%) as of March 2020. States like Maharashtra, West Bengal, Tamil Nadu and Kerala had GNPA ratio of around 2.3-2.5% during the same period.

Majority of the market dominated by lower ticket size loans in volume terms

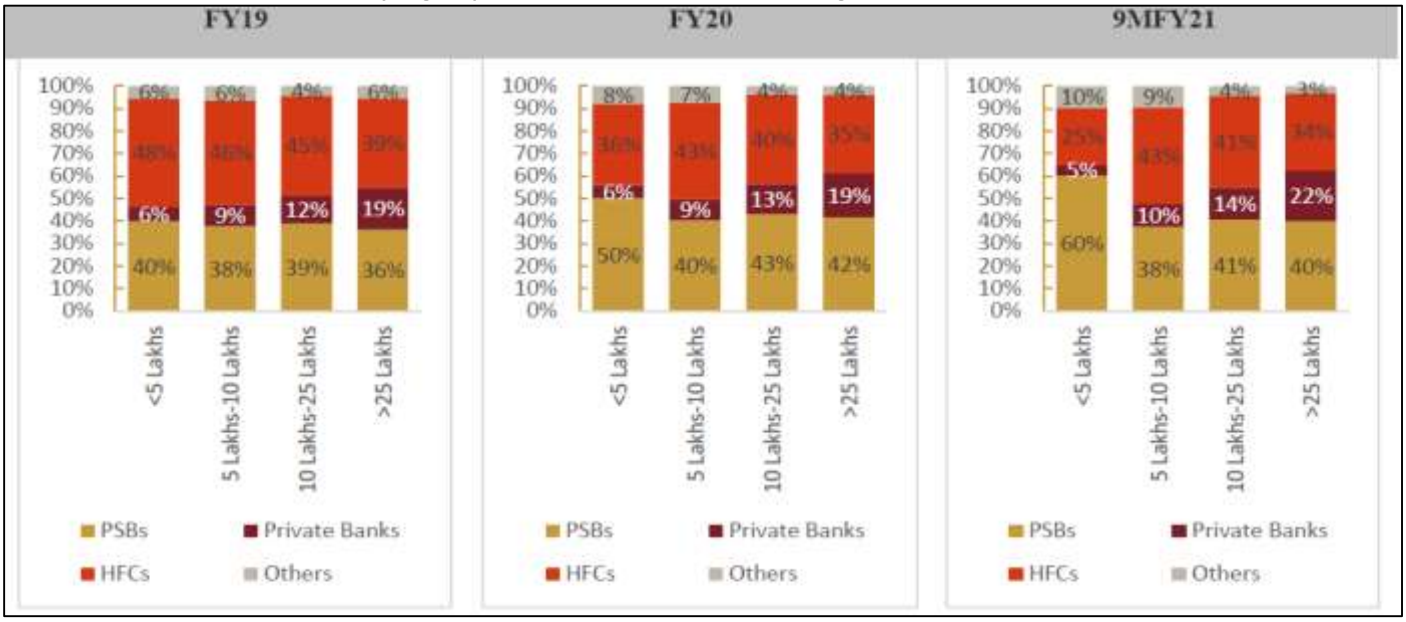
Their share of loans up to Rs. 25 lakhs declined from 52% in Fiscal 2016 to 45% in Fiscal 2020 in terms of value. The share further declined to ~43% as of 9MFY21. However, majority of the housing loan volumes are still in the lower ticket size segment (upto Rs. 25 Lakhs), with this segment accounting for ~80% of housing loans outstanding volumes as of 9MFY21.





Banks mostly provide loans to customers whose income sources, banking behavior and credit history can be easily assessed. On the other hand, several HFCs cater to customers whose formal income proofs may not be strong, and therefore, an HFC's understanding of underwriting for this customer segment as well as micro market related dynamics are critical for success. Besides, banks also have a lower cost of funds than HFCs, allowing them to offer loans at more attractive rates to customers with good credit scores. Both banks and HFCs are exposed to general risks in the housing finance market such as delay in project approvals and construction, title and valuation related risks. In lower ticket size loans up to Rs. 10 lakhs, public sector banks have seen a strong competition from the HFCs. These both combined have more than 80% share between them in Fiscal 2020 in the housing loans disbursements in lower ticket size buckets (upto Rs. 10 lakhs).

Player group-wise – ticket size mix of housing loan disbursement



HFCs have increased the share of home loans in their product profile

CRISIL Research estimates that housing loans account for ~60-65% of the HFCs' total loan portfolio. Loan against property ("**LAP**") comprised ~20% of the HFCs' loan portfolio as of Fiscal 2020 with share of developer loans and other corporate loans marginally declined compared to the previous year at ~10-15%. Over the next two to three years, with HFCs increasingly looking at conserving liquidity and getting cautious on funding developers, CRISIL Research expects the share of developer loans in the overall outstanding loans to further come down. The growth in the LAP portfolio of HFCs is also likely to moderate, given growing concerns on asset quality within the MSME segment. Consequently, the share of housing finance in the overall portfolio is expected to increase further. It is important to note that a large proportion of loans currently tagged as LAP are also in multiple cases housing loans taken for renovation, reconstruction, self-construction, plot purchase related housing activities with the security of the property. However, the HFCs cannot tag them as housing loans on account of the classification guidelines set forth by NHB. However, despite them not being housing loans, the risk emerging out of these loans is lower than in case of LAP. Advanced appraisal mechanism and monitoring systems as well as robust collection systems help these HFCs maintain good asset quality despite providing a considerable chunk of loans under wholesale finance, developer loans, loans against property and other such riskier categories than the usual home loans.

Home loans followed by Loans against property have the lowest annual credit losses across major asset segments

Housing finance as an asset class has the lowest annual credit losses amongst all large financial asset classes mainly on account of the collateral and the secured nature of the funding. The GNPA ratio for MSME loans has been in the range of 4-6% for NBFCs in the past three years and that for auto loans has been between 5-7% for NBFCs whereas, for housing loans it has been comparatively better at 1-3%. Thus, for HFCs the asset quality is better in comparison to other NBFCs operating in asset classes having higher GNPA levels. The average credit costs as a percentage of average annual assets across FY 19-21 for NBFCs are estimated to be approximately 0.9% in the case of housing loans as against 1.4% for LAP, 1.7% for auto loans, 2.9% for micro finance loans and 4.5% for unsecured MSME loans. Thus, credit losses for mortgage loans (home loans and LAP) are the lowest amongst all the major asset classes.

Monthly collection efficiency impacted by second wave of COVID-19; asset quality to improve in long term

Collections in the home loans segment were impacted by the second wave of COVID-19 and the subsequent lockdowns in various states across the country. However, the overall collection efficiency trends have been better than in the other asset classes. CRISIL Research estimates the collection efficiency to have declined to around 95% and 93% in the months of April and May 2021, respectively, but in June 2021, there has been a strong rebound with collection efficiency reaching close to normal levels. During the first wave of COVID-19 as well, the home loans segment had seen a strong bounce-back in collections efficiency after an initial stutter. Collections in the housing finance segment, which had slipped to ~70-75% in April 2021 because of the nationwide lockdown due to the pandemic, rebounded to 85-90% in July and August after the Government relaxed restrictions gradually. In October and November 2020, collection efficiency rose further to 90-95%, as per CRISIL Research estimates, and in December 2020, the collection efficiency is estimated to have further increased to 98-99%. Collection efficiency continued to be strong at around the same level as December 2020 in the fourth quarter of Fiscal 2021 as well.

Despite increases in delinquency, home loans to be least affected

Despite the rising monthly collections in home loans, lower income generation on account of COVID-19 will impact the asset quality in Fiscals 2021 and 2022. Players with significant exposure to developer finance and having aggressive underwriting policies will be more vulnerable in comparison to others. The rapid increase in COVID-19 infections and intermittent local lockdowns has impacted self-employed borrowers and informal salaried more than the formal salaried segment. The formal salaried borrower segment, which forms a significant chunk of borrowers especially for HFCs, is more resilient despite pay cuts and job losses. For overall housing finance, where salaried customers make up for majority of the overall home loan portfolio, CRISIL Research expects the GNPA of HFCs to increase by ~40 bps in Fiscal 2021 from 2.4% as of March 2020, but slightly decline in Fiscal 2022.

Banks borrowing to gain further share in the borrowing mix of stronger HFCs

CRISIL Research expects the share of bank borrowings in the resources mix of HFCs to increase further over the medium term due to continuing support offered by banks to the stronger HFCs and liquidity support measures announced by RBI. Risk in the housing finance sector increased after late 2018, which restricted the HFCs' easy access to market borrowings. During this period, while players with high asset liability management ("**ALM**") mismatch and higher share of non-retail portfolio found it difficult to raise funds, players with strong parent company support and relatively higher proportion of retail assets were able to raise funds from the market. However, over time and with aggressive repo rate cuts by the RBI, the benchmark commercial paper and non-convertible debentures rates have softened. Bank borrowings have been gaining share in the resources profile for HFCs, especially the smaller HFCs, on account of difficulty in accessing the capital markets post the liquidity crisis of 2018. CRISIL Research expects the proportion of bank borrowings to increase further over the medium term.

Overview of housing finance market focusing on low income housing segment

India's mortgage market can broadly be divided into two segments by ticket size of the housing loan at the time of disbursement - loans with ticket size of more than Rs. 10 lakhs, and loans with ticket size of Rs. 10 lakhs and below. The former can be called normal mortgage market, which is prominent in the metro/urban areas, and the latter which generally includes houses in the outskirts of these areas and semi-urban and rural areas can be defined as housing finance market focusing on low income housing segment. Housing loans with ticket size greater than Rs. 10 lakhs are termed normal housing loans, and loans with ticket size lower than Rs. 10 lakhs are referred to as housing loans focusing on low income housing segment.

Encouraging trends in housing finance market focused on low income housing segment (loans up to Rs. 10 lakhs); market to bounce back more strongly in long term

The overall size of the housing finance market focusing on low income housing segment in India was around Rs.2.6 trillion as of March 2021. The housing finance market focused on low income housing segment (ticket size less than Rs.1 million) accounts for around 10-11% of the overall housing finance market. Of the total outstanding housing finance focused on low income housing segment of Rs.2.6 trillion, PSBs accounted for 50% of the market with an absolute value of Rs.1,326 billion, private banks accounted for 7% with an absolute value of Rs.191 billion, while HFCs accounted for 36% with loans outstanding of Rs.937 billion as of March 2021.

Growth in the market, in terms of loans outstanding, has come down over the last four years due to the slowdown in economic growth, challenges faced by some HFCs in availing funding subsequent to the IL&FS meltdown, and in the more recent past, the onset of the COVID-

19 pandemic. The housing finance market focused on low income housing segment logged a growth of ~5.9% CAGR between Fiscal 2016 and 2021 after growing at a higher cliff in the years before that.

Growth drivers for housing finance

Higher transparency in the sector, increasing affordability and urbanisation, and government incentives will push up the housing finance market over the next five years.

Government's scheme to provide Housing for All by 2022 and various steps taken to implement it are expected to boost sales of affordable and low-cost housing units. This will, consequently, increase the demand for loans. Under the Housing for All missions, the government has introduced credit-linked subsidy scheme as a demand-side intervention in order to expand institutional credit flow and meet the urban demand.

Infrastructure status to ease financing for affordable housing developers

In November 2017, the Union government notified infrastructure status to the affordable housing sector. Projects having at least 50% of floor space index (FSI) consumed in units having carpet area of less than 60 square meters qualify as infrastructure projects. This move is aimed at increasing the availability of financing and reducing financing costs for affordable housing projects.

Business Model of housing financiers focused on low income housing segment

Housing financiers focused on low income housing segment typically serve the underserved category of low-income or midincome customers who may be salaried, working in the informal sector or self-employed running a small business. Many a times, these customers do not have adequate documentation that can serve as proof of their income. The high cost of serving this category of customers has prompted financiers to adopt innovative models to source business. An HFC targeting this segment of customers usually has a hub and spoke model where retail branches of the HFC operate as 'hubs' in urban areas, while small kiosks are set up near areas where construction activity is taking place to source customers. Financiers also spread awareness about their products in rural areas by setting up kiosks at 'gram sabhas' and arranging 'loan melas' for potential customers. However, some players also rely on customers indulging in self-construction of their houses in tier-2 and 3 cities in need of credit. These players have sourcing strategies focussed on attracting customers with touch points in nearby locations.

Usually, close to 70% of the overall business of housing finance companies focused on low income housing segment is sourced through direct sales teams. Direct customer contact through these teams enables better visibility and helps limit fraud, thus making for reliable customer assessment. Moreover, all critical functions like origination, verification and credit appraisal are performed in-house, while certain non-core activities like loan documentation and document processing may be outsourced. This allows HFCs in this segment to allocate more internal resources towards vital aspects of lending such as verification, credit appraisal and credit assessment.

First time availing loan facility (New to Credit)
First time credit customers in housing finance focused on low income housing segment are higher than as compared to normal housing (ticket size more than Rs. 10 lakhs). The declining share of first time credit customers also indicates better availability of loan repayment records of customer while assessing them for credit underwriting. First time home loan consumers account for close to 62% of housing loan disbursements in case of housing finance focused on low income housing segment. However, in first time home loan consumers, the share is high in higher ticket sizes as well on account of comfort drawn from availability of prior credit history of the borrowers.

Clear understanding of micro markets
Given the target borrower's profile, players need to have a clear and deeper understanding of micro markets and develop a strong local network. The strong network helps players to source business from niche customer category by having references from their existing customers. It is observed that successful players in the segment generally focus on a few geographies where they have a good understanding and scale up gradually to manage costs and asset quality better.

Customer risk
Customers in housing finance focused on low income housing segment are generally in formal sector jobs with low incomes, or are self-employed (such as a carpenter, plumber, vegetable vendor, driver), people who may not have income proofs. Given the lack of income proofs, the underwriting process typically requires detailed personal discussion with the borrower as well as acquaintances and neighbours in order to assess the source of income and pattern of cash inflows and outflows as well as the stability and habits of the customer. Given the nature of the process, operating costs are typically very high; therefore, players who are, over a period of time, able to achieve a fair degree of standardisation in the process by building models revolving around specific customer profiles and/or geographies are likely to better manage operating costs.

Collateral risk assessment
Properties under the low income housing segment sometimes lack proper property titles, especially in the outskirts of large cities, semi-urban and rural areas. With better availability of information and due diligence by the technical team, players can mitigate the risk. While lenders do take appropriate due diligence measures to safeguard against this risk while sanctioning the loan, there have been instances of borrowers mortgaging the same property with multiple lenders. As of now, registration of charge on underlying property is undertaken by lenders on selective basis (high-ticket loans or in case of corporate borrowers) only. The RBI directive to register the charge on the underlying property with a central registry instead of the currently followed process, this will help mitigate this risk to a large extent.

Collection efficiency
Given that players in the segment typically cater to the lower income customer segment, many of whom may not be financially literate, a strong focus on collections and monitoring risk of default at customer level is vital to manage asset quality. It is observed that events that impact the economy as a whole (such as demonetisation) and local factors (natural calamities or other events in the place of employment/work of the borrower) have a disproportionate impact on asset quality in the segment. Therefore, players are increasingly using analytical and monitoring tools enabled by technology to better predict default risk. In addition, there is an increasing focus on pushing customers to make EMI payment through ECS.

Profitability of HFCs focused on low income housing segment to decline in Fiscal 2022 but improve over a long term
In Fiscal 2019, HFCs focused on low income housing segment saw a decline in RoA on-year, because of an increase in cost of funding following the default by IL&FS. However, they have witnessed improvement in RoA during the Fiscal 2020. A majority of the players had already made provisioning in Fiscal 2020, hence, RoA improved due to relatively low credit cost in Fiscal 2021. In Fiscal 2022, CRISIL Research estimates the profitability of HFCs to deteriorate, mainly due to increase in credit costs as they cater to riskier segments (self-employed and informal segment) which are more vulnerable to economic slowdown. Over the long term, CRISIL Research expects the industry's profitability to gradually improve. Cost of funds, which has shot up since the second half of Fiscal 2019, is expected to gradually normalise, once risk aversion wanes and capital availability for better performing HFCs improves. Additionally, for players in the low income housing category, operating expenses, too, would moderate, as business volumes increase and the level of standardisation and digitalisation in credit assessment increases.

Analysis of housing finance companies based on book size

CRISIL Research has analysed the variation in performance of HFCs on the basis of assets under management (including home loans, loan against property, developer loans and any other loans by the HFC) as well as focus segment in terms of ticket size. Accordingly, the HFCs have been classified as large HFCs, medium HFCs, small HFCs, and mini HFCs based on the book size of the company. HFCs have also been classified as HFCs focused on low income housing segment, based on higher share of housing loans with ticket size less than Rs. 1 million in their portfolio. The entities included in their analysis together account for ~99% of the outstanding retail home loans given by HFCs as on March 2020.

Profitability analysis: Higher returns, lesser competition makes the low income housing segment attractive for HFCs

Housing loans are considered to be a safer asset class compared with other asset classes such as vehicle loans, construction equipment loans and personal loans, as borrowing is usually for a self-occupied residential property of the borrower, where the propensity of default is relatively lower. In Fiscal 2019, HFCs across segments saw a decline in RoA, because of an increase in interest expenses following the default by IL&FS. Large, mini and HFCs focused on low income housing segment witnessed an improvement in RoA during Fiscal 2020. For large HFCs, improvement in profitability was mainly due to tax reduction, while for mini HFCs and HFCs focused on low income housing segment, the improvement was owing to significantly lower credit costs (on account of a significant decline in GNPA for a few HFCs such as Motilal Oswal Home Finance, Aavas and Shriram Housing). For medium HFCs, significantly higher credit costs compared with Fiscal 2019 led to lower profitability. Over the longer term, CRISIL Research expects the industry's profitability to gradually improve. Cost of funds, which has shot up since the second half of Fiscal 2019, is expected to gradually normalise, once risk aversion wanes and capital availability for better performing HFCs improves. As economy revives, delinquencies are also expected to normalise, leading to decrease in credit costs for HFCs. Additionally, for players in housing finance focused on low income housing segment, operating expenses, too, would moderate, as business volumes increase and the level of standardisation and digitalisation in credit assessment increases.

Aptus Value Housing Finance has the largest branch network in South India amongst peers; is also amongst the top 3 in terms of employees

According to the peer set analysed, Aadhar Housing Finance had the highest branch count (319 branches), followed by Aavas Financers (280 branches), Repco (177 branches) and Aptus Value Housing Finance (190 branches). Amongst the peers, Aptus Value Housing Finance is the largest HFC in South India in terms of branch network as of March, 2021. The market share of Aptus Value Housing Finance India in Tamil Nadu, Andhra Pradesh, Karnataka and Telangana, amongst all the HFCs in terms of gross home loan assets was 1.6%, 1.0%, 0.4% and 0.4% respectively as of December 31, 2020. Among the Small and Mini HFCs, the market share of Aptus Value Housing Finance India in Tamil Nadu, Andhra Pradesh, Karnataka and Telangana, in terms of gross home loan assets, was 21.3%, 11.7%, 7.7% and 6.5% respectively as of December 31, 2020. In terms of number of employees as on March 31, 2021, the top 4 HFCs amongst the peers considered are Aavas Financiers (4581 employees), Aadhar Housing Finance (2310 employees), Shubham Housing (1914) and Aptus Value Housing Finance (1913 employees). Having a large base of employees, especially for direct sales, enables these players to source a lot of the business on their own and stay in touch with their customers.

Key Concerns:

- The Coronavirus pandemic (COVID-19) has had certain adverse effects on the business, operations, cash flows and financial condition and the extent to which it or the effect of outbreaks of any other severe communicable disease may continue to do so in the future, is uncertain and cannot be predicted.
- Requires substantial capital for the business and any disruption in its sources of capital could have an adverse effect on its business, results of operations and financial condition.
- Inability to meet obligations, including financial and other covenants under debt financing arrangements could adversely affect the business, results of operations and financial condition.
- Liquidity may be affected by the COVID-19 pandemic which may affect AVHFL's ability to continue to operate and grow the business.
- The risk of non-payment or default by borrowers may adversely affect the business, results of operations and financial condition.
- A substantial portion of customers are first time borrowers which increases risks of non-payment or default for AVHFL.
- AVHFL is affected by volatility in interest rates for both its lending and treasury operations, which could cause net interest income to vary and consequently affect the profitability.
- Any downgrade in credit ratings could increase the borrowing costs, affect the ability to obtain financing, and adversely affect the business, results of operations and financial condition.

- AVHFL may face asset-liability mismatches, which could affect liquidity and consequently may adversely affect the operations and profitability.

- Operations are primarily focused in the states of Tamil Nadu and Andhra Pradesh and any adverse developments in these regions could have an adverse effect on the business and results of operations.

- Inability to recover the full value of collateral, or amounts outstanding under defaulted loans in a timely manner, or at all, could adversely affect the business, results of operations and financial condition.

- Inability to maintain capital adequacy ratio could adversely affect the business.

- Any deterioration in the performance of any pool of receivables securitized to banks and other institutions may adversely impact the financial performance.

- AVHFL has experienced significant growth in recent years and it may not be able to sustain such growth in the future.

- The Indian housing finance industry is highly competitive and inability to compete effectively could adversely affect the business and results of operations.

- Relies significantly on information technology systems for business and operations and any failure, inadequacy or security breach in such systems could adversely affect the business, results of operations and reputation.

- Any failure or significant weakness of internal processes or systems could cause operational errors or incidents of fraud, which would adversely affect the business, profitability and reputation.

- Lack of success in expanding business into new regions and markets in India or the sub-optimal performance of new branches could adversely affect the business, results of operations, financial condition and cash flows.

- Non-compliance with the NHB's or RBI's observations made pursuant to its periodic inspections and violations of regulations prescribed by the NHB or RBI, could expose AVHFL to certain penalties and restrictions.

- AVHFL may not be able to identify, monitor and manage risks or effectively implement its risk management policies.

- The Company may face difficulties and incur additional expenses in operating in rural and semi-urban markets, where infrastructure may be limited.

- The Indian housing finance industry is extensively regulated by the RBI and NHB and any changes in laws and regulations applicable to HFCs could have an adverse effect on the business.

- AVHFL in the past been has been subject to penalties and restrictions imposed by the NHB.

- A portion of AVHFL's collections from customers is in cash, exposing it to certain operational risks.

- Inability to detect money-laundering and other illegal activities fully and on a timely basis may expose it to additional liability and adversely affect the business and reputation.

- Requires certain statutory and regulatory approvals for conducting business and inability to obtain, retain or renew them in a timely manner, or at all, may adversely affect the operations.

- Depends on the accuracy and completeness of information provided by AVHFL's customers and its reliance on any misleading information may affect its judgment of their credit worthiness, as well as the value of and title to the collateral.

- Significant changes by the Government, the Reserve Bank of India or the National Housing Bank in their policy initiatives facilitating the provision of housing and housing finance or any change in the tax incentives that the Government currently provides to Housing Finance Companies may have an adverse effect on the business, results of operations and financial condition.

- AVHFL is exposed to risks that may arise if its customers opt for balance transfers to other banks or financial institutions, or if customers face increased difficulties in refinancing its existing housing loans from other banks and financial institutions to AVHFL.

- Fluctuations in the market values of investments could adversely affect the results of operations and financial condition.
- The bankruptcy code in India may affect AVHFL's rights to recover loans from its customers.
- The growth rate of India's housing finance industry may not be sustainable.

Profit & Loss

Particulars (Rs in million)	FY21	FY20	FY19
Revenue from Operations	6238.9	4852.3	3108.9
Net gain on fair value changes	7.6	31.4	42.5
Fees and commission income	119.7	119.6	87.2
Other income	186.3	233.9	132.6
Total Income	**6552.4**	**5237.2**	**3371.2**
Total Expenditure	**3101.5**	**2764.3**	**1844.1**
Finance costs	2065.3	1845.5	1162.2
Employee benefits expense	713.8	648.1	481.2
Depreciation and amortization	56.9	58.1	55.4
Impairment on Financial Instruments	58.2	34.3	11.7
Other expenses	207.3	178.4	133.6
PBT	**3450.9**	**2472.9**	**1527.1**
Tax (incl. DT & FBT)	**781.5**	**362.8**	**412.2**
Current tax	826.7	601.5	370.7
Income Tax relating to earlier years	-2.9	5.9	-1.1
Deferred tax charge/(credit)	-42.3	-244.7	42.6
PAT	**2669.4**	**2110.1**	**1114.8**
EPS (Rs.)	5.6	4.7	2.8
Face Value	2	2	2
OPM (%)	53.4	48.5	46.3
PATM (%)	42.8	43.5	35.9

(Source: RHP)

Balance Sheet

Particulars (Rs in million) As at	FY21	FY20	FY19
ASSETS			
Financial Assets			
Cash and cash equivalents	4227.4	4840.3	1068.5
Bank Balance other than cash and cash equivalents	150.6	1186.4	40.7
Loans	39898.0	31170.9	22002.5
Investments	527.5	0.0	0.0
Other Financial assets	116.2	26.8	31.0
Total Financial Assets	**44919.7**	**37224.4**	**23142.7**
Non-financial Assets			
Current tax assets (Net)	0.0	0.0	8.3
Deferred tax assets (Net)	169.9	127.2	11.5
Property, plant and equipment	24.8	32.7	32.0
Intangible assets	2.7	3.7	8.1
Right-of-use assets	68.1	64.8	60.8
Other non-financial assets	16.4	14.5	13.4
Total Non - Financial Assets	**281.9**	**242.8**	**134.2**
TOTAL ASSETS	**45201.7**	**37467.2**	**23276.9**
LIABILITIES AND EQUITY			
Liabilities			
Financial Liabilities			
Trade Payables			
total outstanding dues of creditors other than micro enterprises and small enterprises	18.8	6.9	8.2
Debt Securities	4301.8	6445.5	7013.9

Borrowings (Other than Debt Securities)	20777.9	13704.3	8983.1
Lease Liabilities	70.9	66.6	63.7
Other financial liabilities	133.5	52.4	52.4
Total Financial Liabilities	**25302.9**	**20275.7**	**16121.3**
Non-Financial Liabilities			
Current tax liabilities (Net)	44.5	58.4	9.8
Provisions	33.0	25.2	18.0
Deferred tax liabilities (Net)	0.0	0.0	128.6
Other non-financial liabilities	26.7	17.8	15.5
Total Non - Financial Liabilities	**104.2**	**101.4**	**171.9**
Total Liabilities	**25407.1**	**20377.1**	**16293.1**
Equity			
Equity Share capital	949.3	945.1	787.8
Other Equity	18845.2	16145.0	6195.9
Total Equity	**19794.5**	**17090.1**	**6983.8**
Total Liabilities and Equity	**45201.7**	**37467.2**	**23276.9**

(Source: RHP)