

L&T Finance: Deserves credit

The firm has improved its fundamentals and offers a favourable risk-reward ratio to investors.

L&T Finance, for two consecutive quarters, has beaten the Street expectations. Its consolidated net profit for the fourth quarter of 2014-15 stood at ₹203 crore—a growth of 9% compared to the same period last year, and a growth of 12% over the previous quarter. Continued good performance by retail finance—earnings grew 27% year on year (y-o-y)—is primarily responsible for the impressive consolidated numbers.

Allaying concerns about the credit quality of its wholesale finance book, the company brought down its gross non-performing assets (NPA) in this quarter. Improvement in collections and sale of some stressed assets to asset reconstruction companies helped bring down NPAs. With a 93 basis point y-o-y fall, gross NPA reached 2.25%, the lowest in the past eight quarters.

Return on equity (ROE) reached 13.2% in the fourth quarter, the highest in the past eight quarters. More importantly, the company is looking to improve its ROE further over the next three years. This will be achieved by focusing on a new portfolio in retail and wholesale opportunities where the company has a competitive advantage, and by driving down credit costs to more manageable levels. Because of this, the company expects to achieve a 25% growth in loans, while keeping its credit cost at current levels. It is also planning to unlock value from its private equity book and its investment management business. In the long term—5-7 years—the company should emerge as a comprehensive financial services player in India. A strong brand, access to the vendor and customer network of its parent, and the ability to lend to multiple channels, among other things, should help

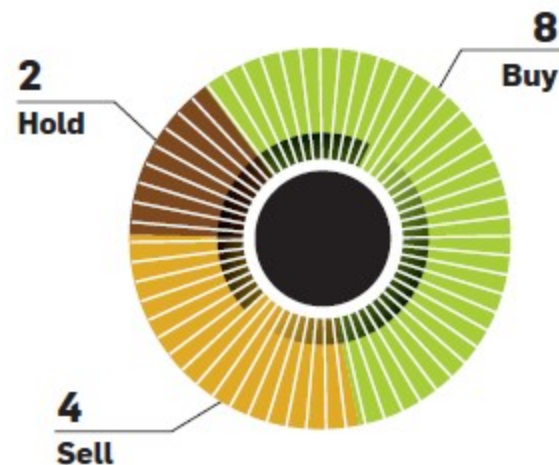
the company in the long run. The management also has considerable experience in incubating projects with long gestation periods. Though the market has penalised the counter for its exposure to infrastructure lending, sentiment should improve once the economy gathers pace.

More and more analysts are finding this counter attractive now because the valuation, due to the stock's underperformance in the past one year, has come to reasonable levels. Currently, it is trading at a discount to its NBFC peers. Pick-up in the economy and improvement in the sentiment towards the infrastructure sector will be triggers for the counter. Continued rate cut by the Reserve Bank and the fall in the interest rate structure will also result in heightened activity at the counter. If the company gets a banking licence, it will be another trigger. Since the price has not yet jumped up, despite a visible improvement in fundamentals, the risk-reward ratio is favourable for long-term investors.

Selection Methodology: We pick the stock that has shown the maximum increase in 'consensus analyst rating' in the past one month. Consensus rating is arrived at by averaging all analyst recommendations after attributing weights to each of them (5 for strong buy, 4 for buy, 3 for hold, 2 for sell and 1 for strong sell) and any improvement in consensus analyst rating indicates that the analysts are getting more bullish on the stock. To make sure that we pick only companies with decent analyst coverage, this search is restricted to stocks that are covered by at least 10 analysts. You can see similar consensus analyst rating changes during the past week in the ETW 50 table.

— Narendra Nathan

Analysts' views



Improvement in fundamentals, impending rate cuts, uptick in the economy and lower valuation have made the counter attractive.

> Fundamentals

	Actual		Consensus estimate	
	2013-14	2014-15	2015-16	2016-17
Revenues (₹ cr)	2,074.70	2,628.44	3,213.64	3,871.97
Operating profit (₹ cr)	826.93	1,178.79	1,353.32	1,670.19
Net profit / loss (₹ cr)	596.89	854.68	951.49	1,178.58
EPS (₹)	3.03	4.13	5.57	6.51

> Valuation

	PBV	PE	Dividend yield (%)
L & T Finance Holdings	3.07	12.72	1.27
Bajaj Finserv	9.23	13.44	0.12
Mahindra & Mahindra Fin. Services	2.69	16.69	1.49
Bajaj Holdings & Investment	2.60	6.86	2.32
Reliance Capital	0.85	11.85	2.10

> Latest brokerage calls

Reco date	Research house	Advice	Target price (₹)
27 April '15	Equirus Securities	buy	83.00
27 April '15	IndiaNivesh Securities	buy	84.00
24 April '15	JPMorgan	overweight	77.00
24 April '15	Axis Capital	buy	80.00
24 April '15	Firstcall India Equity Advisors	buy	78.00

> Relative performance

Market price: ₹63.20



Performance of L&T Finance compared with the Sensex. Figures are normalised to a base of 100. Source: ETIG Database & Bloomberg