

# L&T Finance: Potential for stock re-rating

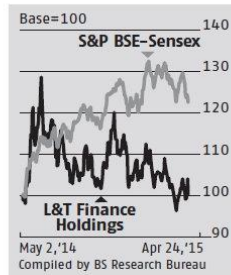
Inexpensive valuations, strong growth prospects and improving return ratios have made most analysts bullish

SHEETAL AGARWAL

L&T Finance Holdings (L&T Finance) posted in-line results for the March quarter, wherein improvement in asset quality, healthy loan growth and margin uptick stood out. Its consolidated net interest income (NII) grew 21.3 per cent year-on-year (y-o-y) to ₹706 crore. Net profit grew 9.3 per cent y-o-y to ₹203 crore, in line with the Bloomberg consensus estimate. Notably, its gross non-performing assets (NPA) and net NPA ratios improved both sequentially and on a y-o-y basis. The gross NPA ratio stood at 2.25 per cent, down 76 basis points (bps) sequentially and 93 bps over the March 2014 quarter. The net NPA ratio fell 72 bps sequentially and 103 bps y-o-y to 1.26 per cent. Improving collections, coupled with sale of some stressed assets to asset restructuring companies, aided asset quality in the quarter.

L&T Finance deployed some of the above gains towards higher provisioning, which stood at ₹244 crore, up 55.4 per cent y-o-y and eight per cent sequentially. This number was higher than Street expectations of ₹230 crore, mainly due to increase of standard asset provisions to 0.30 per cent from 0.25 per cent, income reversal on 150-180 days past due assets and voluntary provisions on select stress accounts. While the management expects provisions to remain flattish, with a downward bias, they are keeping an eye on the monsoon, crucial to keep asset quality pressures in check.

For FY15, NII grew 33 per cent to ₹2,628 crore, while net profit surged 43 per cent to ₹851 crore. These were driven by loans and advances that grew 18 per cent in FY15, on the back of continued traction in the



wholesale business (47 per cent of the overall loan book). Which, in turn surged 26 per cent in the year gone by. Wholesale business growth was led by operational projects in the renewable power and roads sectors. Given the traction in these two sectors, it should not come as a surprise if the momentum is sustained.

The retail finance business grew 11 per cent in FY15 led by tractors, two-wheelers, housing finance and micro finance segments. The company aims to achieve 25 per cent growth in total assets in FY16, subject to an improving macro economy.

Positively, net interest margins improved to 5.7 per cent in FY15, compared to 5.5 per cent in FY14. Secondly, the management also remains confident of future growth and expects the return on equity ratio to improve from 12 per cent in FY15 to 18 per cent over the next three years.

In this backdrop and given inexpensive valuations, most analysts remain positive on L&T Finance. Their average target price of ₹77.6 indicates upside potential of 21 per cent from the current levels of ₹63.90. The stock, which has under-performed the S&P BSE Sensex in the past year, trades at 1.4 times the FY16 estimated consolidated book value versus two-to-three times for its peers.