

Company update

Financials

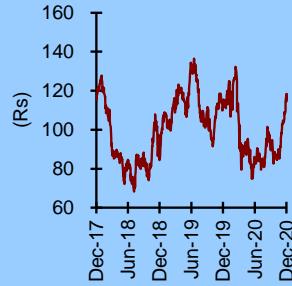
Target price Rs151

Shareholding pattern

	Mar '20	Jun '20	Sep '20
Promoters	56.0	56.0	56.0
Institutional investors	39.3	38.6	37.5
MFs and other	13.8	14.5	14.3
Banks/FIs	0.5	0.5	0.3
Insurance	6.1	6.1	6.1
FIs	18.9	17.5	16.8
Others	4.7	5.4	6.5

Source: BSE

Price chart



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Power Finance Corporation

BUY

Maintained

Investment thesis intact; dividend payout
guidelines to inculcate long-term discipline

Rs115

RBI's draft circular on dividend declaration by NBFCs links eligibility and quantum of dividend distribution to net NPA, CRAR and leverage. For PFC, categorised as NBFC-ND-SI, based on its past three years' CRAR and current net NPA print, the criteria matrix (as per draft circular) makes it eligible to dividend payout up to 25% of earnings (vs its current policy of 30% of earnings or 5% of net worth, whichever is higher). However, eligibility criteria are expected to accelerate structural improvement of PFC's balance sheet for it to pay out higher dividends (shore up CRAR to >18% and contain net NPA to sustain at <2% for 40-45% payout). Note that being a PSE, the government would be keen to receive higher dividend from PFC. In any case, dividend yield would remain above 6%, hence there is no change in our investment rationale. Given PFC's balance sheet expansion of >10%, steady-state RoE profile of >14% and anticipated stress resolution, we maintain BUY on the stock.

► **Draft RBI circular links dividend payout to net NPA, CRAR and leverage:** RBI's draft circular subjects NBFCs to comply with certain criteria for distributing dividends from FY21 onwards. In case of PFC, which is a systemically important non-deposit taking NBFC (NBFC-ND-SI), the eligibility criteria include: a) at least 15% CRAR for past three years (including the accounting year for which dividend is proposed); b) net NPA ratio below 6% in each of the past three years; c) proposed dividend should be payable only out of the current year profit; and d) extraordinary profits/income to be excluded for net profit calculation.

► **PFC eligible to pay up to 25% of net profit in near term, though it can be structurally higher in the longer term:** PFC's past 3-year CRAR for FY21 dividend eligibility will be in the range of 15-18% and FY20 net NPA at 3.8%. Company therefore falls in category 'C' as per the criteria matrix and is eligible to pay out 25% dividend (vs its current policy of 30% of net profit or 5% of net worth, whichever is higher). This translates to a dividend of Rs7-8/share for FY21E. At CMP, PFC's yield would still be higher than 6% (better than prevailing G-Secs). In addition, a relatively lower dividend payout for the year will result in higher book value accretion.

► **Investment thesis intact; guidelines inculcate long-term discipline:** Our investment thesis on PFC remains unchanged. In fact, we expect the company to work towards containing net NPLs below 2% and shore up CRAR to above 18%, so that payout can increase to 40-45%. This is possible with big-ticket resolutions going forward. Thus, the guidelines are structurally positive as they inculcate long-term discipline.

► **Final guidelines may be a non-event for PFC:** We expect the final circular from RBI to be released by Jan'21 (last date for submission of comments is 24th Dec'20). ***There is a likelihood of state-owned NBFCs being exempted in the final guidelines as government is keen to receive higher dividends from profitable PSEs*** (DIPAM issued an advisory in Nov'20 to PSEs to pay higher dividends). In such a situation, there will be no impact on PFC.

Market Cap	Rs302bn/US\$4.1bn
Reuters/Bloomberg	PWFC.BO/POWF IN
Shares Outstanding (mn)	2,640.1
52-week Range (Rs)	132/75
Free Float (%)	44.0
FII (%)	16.8
Daily Volume (US\$'000)	10,202
Absolute Return 3m (%)	25.5
Absolute Return 12m (%)	11.7
Sensex Return 3m (%)	18.6
Sensex Return 12m (%)	15.6

Year to March	FY19	FY20	FY21E	FY22E
Net revenue	97,355	120,944	129,435	136,474
Net profit	69,529	56,551	73,120	75,148
Diluted EPS (Rs)	26.3	21.4	27.7	28.5
BV (Rs)	164.0	171.1	188.3	207.4
Adj. BV (Rs)	123.2	133.8	156.0	176.9
Price/book (x)	0.7	0.7	0.6	0.6
Price/ Adj book (x)	0.9	0.9	0.7	0.7
Diluted P/E (x)	4.4	5.4	4.2	4.0
Dividend yield (%)	-	8.3	6.0	6.2
RoE (%)	17.4	16.7	14.7	14.2

Please refer to important disclosures at the end of this report

Table 1: Draft dividend payout criteria matrix

(Rs mn, year ending March 31)

Category	CRAR	Net NPA			
		Zero	< 2%	2% - 4%	4% - 6%
A	> 20% for each of the last 3 years*	Up to 50	Up to 45	Up to 35	Up to 25
B	18% - 20% for each of the last 3 years*	Up to 45	Up to 40	Up to 30	Up to 20
C	15% - 18% for each of the last 3 years*	Up to 40	Up to 35	Up to 25	Up to 15
D	> 15% in the accounting year for which dividend is to be declared		Up to 15	Up to 10	Nil

Source: Company data, I-Sec research

* including the accounting year for which the NBFC proposes to declare dividend

Table 2: Trends for PFC

(Rs mn, year ending March 31)

	Net NPA			CRAR			Dividend pay-out		
	FY18	FY19	FY20	FY18	FY19	FY20	FY18	FY19	FY20
PFC	7.4%	4.6%	3.8%	20.0%	17.1%	17.0%	31%	0%	44%

Source: Company data, I-Sec research

Financial summary

Table 3: Profit and Loss statement

(Rs mn, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Interest income	264,747	287,961	322,301	347,014	379,593
Interest expended	172,256	193,860	215,589	232,025	259,176
Net interest income	92,491	94,101	106,712	114,988	120,417
Non-interest income	1,499	1,490	1,230	2,434	2,714
Income from operations	93,990	95,591	107,941	117,423	123,130
Other income	3,233	1,763	13,003	12,012	13,343
Net revenues	97,222	97,355	120,944	129,435	136,474
Operating expenses	3,828	4,016	3,969	4,405	4,923
- Employee exp	3,560	3,888	3,799	4,240	4,749
- Depreciation /amortisation	64	61	91	82	87
- Other opex	205	67	79	83	87
Pre-provision profit	93,394	93,338	116,975	125,031	131,551
Provisions	8,153	(8,715)	9,912	32,048	32,611
- Loan loss provisions	5,608	(8,715)	9,912	32,048	32,611
PBT	85,241	102,053	107,063	92,983	98,940
Taxes	25,302	29,765	33,160	23,432	24,933
PAT	59,938	72,288	73,903	69,551	74,007
Extraordinaries	(1,386)	(2,759)	(17,352)	3,569	1,141
Reported PAT	58,552	69,529	56,551	73,120	75,148
Basic number of shares (mn)	2,640	2,640	2,640	2,640	2,640
Basic EPS (INR)	22.2	26.3	21.4	27.7	28.5
Diluted number of shares (mn)	2,640	2,640	2,640	2,640	2,640
Diluted EPS (INR)	22.2	26.3	21.4	27.7	28.5
DPS (INR)	7.8	-	9.5	6.9	7.1
Dividend payout (%)	42.1	-	49.0	25.0	25.0

Source: Company data, I-Sec research

Table 4: Balance sheet

(Rs mn, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Liabilities					
Equity capital	26,401	26,401	26,401	26,401	26,401
Reserves & surplus	344,862	376,774	414,511	464,194	515,298
Net worth	371,263	403,175	440,911	490,595	541,699
Reserve for doubtful debts	33,830	37,402	25,142	21,255	20,762
Secured Loans	331,030	953,630	1,179,690	1,341,361	1,472,073
Unsecured loans	1,964,354	1,930,646	1,854,832	2,006,481	2,269,887
Deferred tax liability	3,009	-40,607	-29,521	-15,603	-12,634
Interest subsidy fund from government	1,160	0	0	0	0
Total liabilities	2,704,646	3,284,246	3,471,053	3,844,090	4,291,786
Assets					
Loans	2,728,122	3,032,104	3,341,126	3,708,321	4,149,147
Investments	23,364	165,862	164,733	164,733	164,733
Current assets	112,518	209,801	81,812	84,390	95,071
Current liabilities	166,493	131,501	131,705	128,695	132,762
Net current assets	-53,974	78,300	-49,893	-44,305	-37,691
Fixed assets (net block)	648	283	675	641	602
Foreign currency translation difference	6,486	7,697	14,412	14,700	14,994
Total assets	2,704,646	3,284,246	3,471,053	3,844,090	4,291,786
Balance sheet ratios (%)					
Loan growth	13.6	11.1	10.2	11.0	11.9
Borrowings growth	13.3	25.7	5.2	10.3	11.8
EA growth	12.7	21.4	5.7	10.8	11.6
Gross NPA ratio	9.6	9.4	8.1	7.5	7.3
Net NPA ratio	7.4	4.6	3.8	3.1	2.6
Provision coverage	22.9	51.5	52.9	61.0	66.0

Source: Company data, I-Sec research

Table 5: Growth metrics

(%, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Net interest income	(9.9)	1.7	13.4	7.8	4.7
Net revenues growth	(7.5)	0.1	24.2	7.0	5.4
Opex growth	2.6	4.9	(1.2)	11.0	11.8
PPP growth	(7.9)	(0.1)	25.3	6.9	5.2
PAT growth	185.5	20.6	2.2	(5.9)	6.4

Source: Company data, I-Sec research

Table 6: Operating ratios

(%, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Yield on assets	10.4	9.6	9.54	9.49	9.33
Cost of funds	8.0	7.5	7.28	7.27	7.31
Spread	2.4	2.1	2.3	2.2	2.0
Net interest margins	3.6	3.1	3.16	3.14	2.96
Cost-income	3.9	4.1	3.3	3.4	3.6
Tax rate	29.7	29.2	31.0	25.2	25.2

Source: Company data, I-Sec research

Table 7: Sanctions and disbursements

(Rs mn, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Sanctions	1,188,700	1,307,570	1,438,327	1,582,160	1,740,376
Disbursements	678,560	676,780	679,970	781,966	860,162
Disbursements to sanction ratio (%)	57.1	51.8	47.3	49.4	49.4
Disbursements growth (%)	1.7	(0.3)	0.5	15.0	10.0
Sanctions growth (%)	14.7	10.0	10.0	10.0	10.0

Source: Company data, I-Sec research

Table 8: RoE decomposition

(%, year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Net interest income/assets	3.6	3.1	3.2	3.1	3.0
Non-interest income/assets	0.2	0.1	0.4	0.4	0.4
Net revenues/Assets	3.8	3.3	3.6	3.5	3.4
Operating expense/Assets	0.2	0.1	0.1	0.1	0.1
Provisions/Assets	0.3	(0.3)	0.3	0.9	0.8
Taxes/Assets	1.0	1.0	1.0	0.6	0.6
Total costs/Assets	1.5	0.8	1.4	1.6	1.5
ROA	2.3	2.4	2.2	1.9	1.8
Equity/Assets	15.0	13.9	13.1	13.0	12.8
ROAE	15.7	17.4	16.7	14.7	14.2

Source: Company data, I-Sec research

Table 9: Valuation metrics

(year ending March 31)

	FY18	FY19	FY20	FY21E	FY22E
Diluted EPS (Rs)*	22.2	26.3	21.4	27.7	28.5
EPS growth (%)	175.4	18.7	(18.7)	29.3	2.8
Book value per share (Rs)	151.0	164.0	171.1	188.3	207.4
Adjusted book value per share (Rs)*	92.5	123.2	133.8	156.0	176.9
Diluted P/E (x)	5.2	4.4	5.4	4.2	4.0
Price/ BV (x)	0.8	0.7	0.7	0.6	0.6
Price/ Adj. BV (x)	1.2	0.9	0.9	0.7	0.7
Dividend yield (%)	6.8	0.0	8.3	6.0	6.2

Source: Company data, I-Sec research

Note: FY18 financial statements are as per I-GAAP and FY19-FY22E financials are as per Ind-AS

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