

RETAIL EQUITY RESEARCH

M&M Financial Services Limited (MMFSL) NBFC

BSE CODE: 532720

NSE CODE: M&MFIN

Bloomberg CODE: MMFS:IN

SENSEX: 36,347

18th December, 2018

HOLD

Rating as per Large Cap

12 month investment period

CMP Rs. 461 TARGET Rs. 487 RETURN 6% ↑

All round strong performance...

MMFSL, a subsidiary of Mahindra and Mahindra (M&M), is a non-banking financial company. It provides financing for commercial vehicles, construction equipment, tractors, cars and SMEs. It mainly focusses on the rural and semi urban markets.

- AUM continued to grow at a strong pace of 21% YoY mainly led by CVs & CEs (↑51% YoY) and tractors (↑21% YoY).
- Net interest income (NII) increased at a robust pace of 28% YoY (in line with our expectation) supported by 35 bps improvement in NIM to 7.8%.
- Gross NPA ratio declined by 350 bps YoY and 40 bps QoQ to 9.0% on the back of an improvement in rural cash flows.
- We expect MMFSL's AUM to grow at a CAGR of 18% over FY18-20E mainly led by higher growth in SMEs, used vehicles and CV & CE segments.
- We expect net profit to increase at a CAGR of 35% over FY18-20E and estimate RoA/RoE to expand to 2.4%/14.9% by FY20E driven by lower provisioning on account of higher recoveries in rural business.
- Hence, we continue to maintain Hold rating on the stock with a similar TP of Rs487 (SOTP).

Higher AUM traction

MMFSL reported strong assets under management (AUM) growth of 21% YoY in Q2FY19 mainly led by CVs & CEs (↑51% YoY) and tractors (↑21% YoY). However, Auto/Utility vehicles (UV) loan portfolio grew at a moderate pace of 8% YoY. As a result, the share of Auto/UV in total AUM declined from 28% to 25% over the last year which was offset by SME financing (12% to 14%). Disbursement also grew at a robust pace of 43% YoY on the back of higher penetration and growth in the rural areas outpaced urban demand. Going forward, we estimate AUM to grow at a CAGR of 18% over FY18-20E led by buoyancy in rural markets as well as market share gains in certain products by the company.

Strong operating performance

Net interest income (NII) grew at a robust pace of 28% YoY (in line with our expectation) supported by 35 bps expansion in net interest margin (NIM) to 7.8% in Q2FY19. NIM improved as improving asset quality helped the company to outweigh rise in cost of funds. Cost to income (C/I) ratio declined by 453 bps YoY to 35.1% as operating efficiency kicked in. As a result, pre-provisioning profit increased at a faster pace of 38% YoY. Net profit jumped by 4.9x YoY mainly due to low base of Q2FY18. Going forward, we expect net profit to increase at a CAGR of 35% over FY18-20E on the back of improving NIM (~8.2%) and declining provisioning expenses.

Asset quality continues to improve

Asset quality improved remarkably as Gross non-performing asset (NPA) ratio (stage 3) declined by 350 bps YoY and 40 bps QoQ to 9.0% as strong collections sustained in Q2FY19. Net NPA ratio also improved by 50 bps YoY and 30 bps QoQ to 6.0%. Management pointed to an improvement in asset quality trends to persist and expects credit costs to trend downward in H2FY19. We expect positive rural sentiment and healthy farm cash flows to sustain, hence, collections will improve further. Thus, we project Gross/Net NPA ratios to decline further to 6.0%/3.0% by FY20E.

Outlook & Valuation

We continue to like MMFSL as its long-term prospects remain strong. Further, MMFSL is a pure play on rural India. Hence, it is well placed to benefit from rural recovery driven by an improvement in higher farm-related cash flows and an increase in government spending. We expect RoA/RoE will expand to 2.4%/14.9% by FY20E. Hence, we continue to maintain our HOLD rating with a similar target price (TP) of Rs487. We value its standalone business at Rs455 (P/ABV of 3.0x for FY20E) and subsidiaries at Rs32.

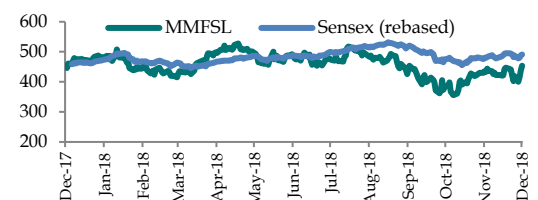
Company Data

Market Cap (cr)	Rs. 28,470
Outstanding Shares (cr)	61.8
Free Float	49%
Dividend Yield	1.0
52 week high	Rs. 537
52 week low	Rs. 351
6m average volume (cr)	0.2
Beta	1.2
Face value	Rs. 2

Shareholding (%)	Q4FY18	Q1FY19	Q2FY19
Promoters	51.2	51.2	51.2
FII's	29.4	28.1	27.5
MFs/Insti	11.6	12.4	12.5
Public	7.8	8.4	8.8
Others	-	-	-
Total	100.0	100.0	100.0

Price Performance	3 Month	6 Month	1 Year
Absolute Return	4.0%	-3.1%	0.3%
Absolute Sensex	-2.5%	2.2%	8.2%
Relative Return*	6.5%	-5.4%	-7.9%

*over or under performance to benchmark index



Standalone (Rs.cr)	FY18	FY19E	FY20E
Net Interest Income	4,147	4,920	5,786
Growth (%)	25%	19%	18%
NIM (%)	8.1	8.2	8.2
Pre Pro Profit	2,534	3,131	3,777
Growth (%)	31%	24%	21%
Net Profit	892	1,292	1,625
Growth (%)	123%	45%	26%
EPS	14.5	21.0	26.4
Growth (%)	105%	45%	26%
P/E	31.8	21.9	17.4
P/BV	3.0	2.8	2.4
P/ABV	3.9	3.6	3.0
RoE (%)	11.3	13.2	14.9
RoA (%)	1.8	2.2	2.4

Quarterly Financials (Standalone)

Profit & Loss Account

(Rs cr)	Q2FY19	Q2FY18	YoY Growth %	Q1FY19	QoQ Growth %
Interest Income	2,103	1,661	26.6	1,926	9.2
Interest Expense	937	750	24.9	849	10.4
Net Interest Income	1,167	911	28.1	1,077	8.3
Non-Interest Income	45	22	104.2	14	225.9
Total Net Income	1,212	933	29.9	1,091	11.1
Operating Expenses	425	369	15.0	385	10.4
Employee Cost	241	186	29.4	263	(8.5)
Other Operating Exp.	184	183	0.3	121	51.4
Total Income	2,148	1,683	27.7	1,940	10.8
Total Expenditure	1,361	1,119	21.6	1,234	10.4
Pre-Provisioning profit	787	564	39.6	706	11.5
Provisions	231	445	(48.0)	294	(21.3)
Profit Before Tax	556	119	366.8	412	34.8
Tax	174	41	324.9	143	21.8
Net Profit	381	78	388.8	269	41.7
EPS - Diluted (Rs)	6.2	1.4	349.3	4.4	41.9

Business Performance (Rs cr)	Q2FY19	Q2FY18	YoY Growth %	Q1FY19	QoQ Growth %
Loan	55,482	46,011	20.6	43,814	26.6
AUM	60,500	49,918	21.2	58,700	3.1
Borrowings	46,707	38,153	22.4	42,887	8.9

Key Ratios (%)	Q2FY19	Q2FY18	YoY bps	Q1FY19	QoQ bps
Net Interest Margin	7.8	7.5	35	7.6	26
Cost of Borrowings	8.4	8.1	26	8.2	20
Yield on AUM	14.1	13.6	49	13.5	58
Cost to Income	35.1	39.6	(453)	35.3	(22)
Debt to Equity	4.7	5.8	(115)	4.3	35
Capital Adequacy	19.7	19.3	40	21.9	(220)
Tier I Capital	14.5	12.4	210	16.6	(210)
Gross NPA	9.0	12.5	(350)	9.4	(40)
Net NPA	6.0	6.5	(50)	6.3	(30)
Provision Coverage	34.9	51.1	(1620)	35.1	(20)
Credit Cost	1.6	3.2	(165)	2.5	(90)
RoE (Ann.)	15.5	4.8	1073	11.4	419
RoA (Ann.)	2.6	0.6	197	1.9	69

Source: Company, Geojit Research

Sum of the parts (SOTP) valuation

Particulars	Basis	Multiple	Year	Value/Share
MMFSL (standalone)	ABV	3.0x	FY20E	455
Rural Housing Finance	ABV	2.0x	FY20E	27
Others			FY20E	13
			20% holding discount to subsidiaries	(8)
			Target Price	487

Standalone Financials

Profit & Loss Account

Y.E March (Rs cr)	FY16	FY17	FY18	FY19E	FY20E
Interest Income	5,853	6,174	7,147	8,367	9,802
Interest Expense	2,639	2,857	3,000	3,447	4,016
Net Interest Income	3,214	3,316	4,147	4,920	5,786
% Change	5.7	3.2	25.0	18.7	17.6
Non-Interest Income	52	64	59	100	118
Net Income	3,266	3,380	4,206	5,021	5,903
Operating Expenses	1,178	1,451	1,671	1,889	2,126
Total Income	5,905	6,238	7,206	8,467	9,920
Total Expenditure	3,817	4,308	4,672	5,336	6,142
Pre-Provisioning Profit	2,088	1,929	2,534	3,131	3,777
% Change	0.3	(7.6)	31.4	23.6	20.6
Provisions	1,050	1,309	1,227	1,171	1,311
Profit Before Tax	1,038	620	1,373	1,960	2,466
Tax	366	220	481	668	841
<i>Tax Rate (%)</i>	35	35	35	34	34
Net Profit	673	400	892	1,292	1,625
% Change	(19.1)	(40.5)	122.8	44.8	25.8
No. of Shares (cr)	56	57	61	61	61
EPS (Rs)	11.9	7.1	14.5	21.0	26.4
% Change	(19.2)	(40.5)	104.9	44.8	25.8

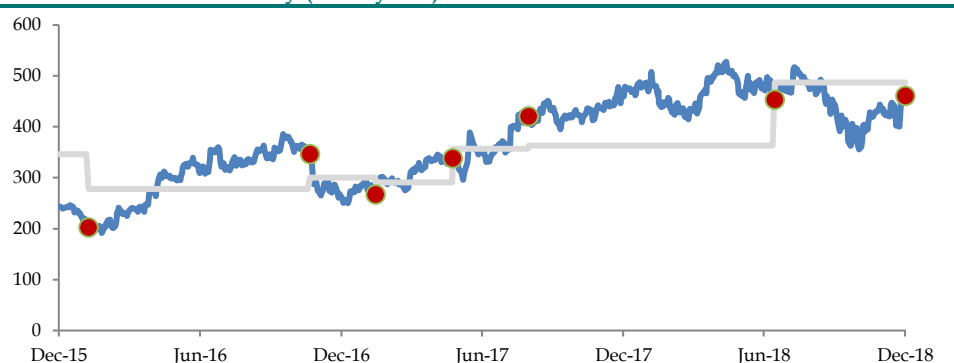
Balance Sheet

Y.E March (Rs cr)	FY16	FY17	FY18	FY19E	FY20E
Liabilities					
Capital	113	113	123	123	123
Reserves & Surplus	5,975	6,364	9,180	10,127	11,506
Borrowings	29,452	34,670	39,213	46,512	54,884
Provisions	1,955	2,166	2,420	2,856	3,370
Other Liabilities	2,084	2,672	3,432	3,809	4,495
Total Liabilities	39,579	45,985	54,368	63,426	74,377
Assets					
Cash & Bank Balances	113	112	120	120	120
Investments	1,483	1,889	1,873	2,210	2,608
Advances	36,658	42,523	51,004	59,730	69,944
Fixed Assets	736	882	960	1,040	1,228
Other Assets	589	578	411	326	478
Total Assets	39,579	45,985	54,368	63,426	74,377

Ratios

Y.E March (Rs cr)	FY16	FY17	FY18	FY19E	FY20E
EPS	11.9	7.1	14.5	21.0	26.4
DPS	4.0	2.4	4.0	4.0	4.0
BV	107.8	114.6	151.4	166.8	189.3
ABV	86.0	86.3	119.3	127.1	151.8
Valuation (%)					
P/E	38.7	65.1	31.8	21.9	17.4
P/BV	4.3	4.0	3.0	2.8	2.4
P/ABV	5.4	5.3	3.9	3.6	3.0
Div. Yield	0.9	0.5	0.9	0.9	0.9
Spreads (%)					
Yield on Funds	15.0	14.1	14.0	13.9	13.8
Cost of Funds	9.0	8.6	7.9	7.7	7.5
Capital (%)					
CAR	17.3	17.6	22.0	18.8	18.2
Tier I	14.6	13.2	16.1	15.8	15.2
Tier II	2.7	4.4	5.9	3.0	3.0
Asset (%)					
GNPA	8.0	9.0	8.5	7.5	6.0
NNPA	3.2	3.6	3.8	3.8	3.0
PCR	61.7	61.8	58.1	50.0	50.0
Management (%)					
Debt/Equity	4.8	5.4	4.2	4.5	4.7
Cost/ Income	36.1	42.9	39.7	37.6	36.0
Earnings (%)					
NIM	8.3	7.6	8.1	8.2	8.2
ROE	11.4	6.4	11.3	13.2	14.9
ROA	1.8	0.9	1.8	2.2	2.4

Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
25 January 2016	BUY	278
08 November 2016	REDUCE	300
31 January 2017	HOLD	291
11 May 2017	HOLD	357
18 August 2017	REDUCE	363
03 July 2018	HOLD	487
18 December 2018	HOLD	487

*Initiating Coverage

Investment Rating Criteria

Large Cap Stocks;		Mid Cap and Small Cap;			
Buy	-	Upside is above 10%.	Buy	-	Upside is above 15%.
Hold	-	Upside is between 0%-10%.	Accumulate	-	Upside is between 10% - 15%.
Reduce	-	Downside is more than 10%.	Hold	-	Absolute is between 0% - 10%.
Neutral	-	Not Applicable	Reduce/Sell	-	Downside is more than 0%.
			Neutral	-	Not Applicable

To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.

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