Retail Equity Research (South India Focus)

Manappuram Finance Ltd

NBFC

BSE CODE : 531213 NSE CODE: MANAPPURAM
BLOOMBERG CODE: MGFL:IN SENSEX : 38,897

BUY

12M Investment Period | Rating as per Mid Cap

CMP Rs129 TARGET Rs154 RETURN +20%
(Closing: 15-07-19)

Reclaiming the glittering growth phase…

Manappuram Finance (MGFL) is one of the leading gold loan NBFCs in India and is well diversified into other business segments like housing loan, vehicle loan and microfinance.

- **With shorter tenure products and online gold loans (OGL), we expect the gold loan AUM to grow at 10% CAGR over FY19-21E.**
- **New synergistic product segments, which currently constitute around one-third of the total assets under management (AUM), to grow at 34% CAGR over FY19-21E by leveraging strong brand equity of Manappuram Finance, supported by sufficient capital.**
- **Positive macros supported by rising gold prices and lowering interest rate scenario to give a twin benefit to the company.**
- **MGFL's impressive capital adequacy ratio, lower NPA levels, and positive asset-liability mismatches give an edge over other NBFCs.**
- **With an estimated PAT growth of over 18%, both in FY20 and FY21, we expect higher return ratios going ahead.**
- **We value MGFL at 2.0x on FY21E Adj. BV/Share and arrive at a target price of Rs154 and recommend 'Buy' rating.**

Gold loan business back on track after demonetisation

After facing the challenging years of FY13 and FY14, MGFL has moved to short-term gold loan products that helped them to effectively manage the gold price volatility and to significantly reduce the default risks and the auction losses. The company has also launched online gold loans (OGL) back in 2015, which now constitute about 39% of the total gold loan portfolio. After temporary hiccups in the business caused by demonetisation and GST implementation, the gold loan business is back on the growth track and we expect gold loan AUM to grow at 10% CAGR over FY19-21E. The rising gold prices, accompanied by a decrease in interest rates in the latest RBI monetary policy, to act positively for the company.

Robust growth seen in new synergistic product segments

The strategy that was envisioned to use the surplus capital and to leverage the strong brand equity acquired over the years has started bearing fruit with these new product segments constituting almost around one-third of the total asset under management of the company in Q4 FY19. Over the next few years, the company expect these non-gold businesses to contribute about 50% of the total AUM. With a wider branch network and strong penetration, we expect these new businesses to grow at 34% CAGR over FY19-21E, with microfinance at 28% CAGR, Housing finance at 29% CAGR and Vehicle finance at 47% CAGR growth from FY19-21E.

Healthy capital adequacy, asset quality and return ratios

In Q4 FY19, the company has a capital adequacy ratio (CAR) of 23.9%, which is much above the regulatory requirement of 15%. MGFL's standalone GNPA stands at 0.5% in Q4 FY19, which is one of the lowest in the NBFC space. Also, the GNPA levels of Microfinance, Housing Finance and Vehicle Finance stand at 0.5%, 3.9% and 1.9% respectively. On a consolidated basis, the GNPA stands at 0.6% and NNPA stands at 0.3% in Q4FY19. The company also have healthy return ratios, with ROE at 23% and ROA at 5.2% in the latest quarter.

Valuations

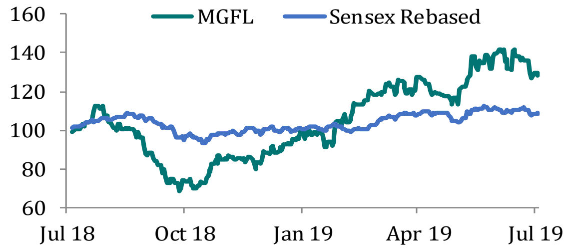
At CMP, the stock is trading at P/BV of 2.0x and 1.7x respectively for FY20E BVPS of Rs64.9 and FY21E BVPS of Rs78. With demonetisation impact left behind, the company is targeting healthy growth in gold loan business going forward, supported by rising gold prices and decreasing interest rates. The new business segments are also expected to do well in the coming years. Also, the company is having healthy CAR, one of the lowest NPAs among NBFC space, and positive asset-liability mismatches. Hence, we value MGFL at 2.0x on FY21E Adj. BV/Share and arrive at a target price of Rs154 and recommend 'Buy' rating.

Company Data	
Market Cap (cr)	Rs10,839
Outstanding Shares (cr)	84.3
Free Float	65%
Dividend Yield	1.7%
52 week high	Rs145
52 week low	Rs66
6m average volume (cr)	0.42
Beta	1.32
Face value	Rs2

Shareholding (%)	Q2FY19	Q3FY19	Q4FY19
Promoters	35	35	35
FII's	38	39	44
MFs/Insti	7	6	4
Public	20	20	17
Total	100	100	100

Price Performance	3 month	6 month	1 year
Absolute Return	1.8%	31.5%	25.8%
Absolute Sensex	-1.0%	7.1%	6.4%
Relative Return*	2.7%	24.4%	19.4%

over or under performance to benchmark index



Consolidated (cr)	FY19A	FY20E	FY21E
Interest Income	4,012	4,930	5,803
Interest Expense	1,319	1,559	1,803
NII	2,693	3,371	4,000
Growth(%)	*15.9*	*25.2*	*18.6*
NIM(%)	15.3	15.8	15.8
Provisions	46	42	50
Adj. PAT	929	1,144	1,352
Growth(%)	*37.4*	*23.0*	*18.2*
Adj. EPS	11.0	13.6	16.1
Growth(%)	*37.3*	*22.7*	*18.2*
P/E	11.7	9.5	8.1
BVPS	53.8	64.9	78.0
Growth(%)	*18.3*	*20.3*	*20.3*
Adj.BVPS	53.1	63.9	77.2
Growth(%)	*19.0*	*20.3*	*20.7*
P/B	2.4	2.0	1.7
Adj. P/B	2.4	2.0	1.7
ROE (%)	22.1	22.9	22.5

Abijith T Cherian
Research Analyst

Industry Outlook...

India has seen the emergence of gold loan speciality players over the last decade.

Non-banking finance companies (NBFCs) form a vital part of the Indian financial system. They help in taking credit to the unbanked segments of the society, driving financial inclusion and nation-building, complementing the banking sector. With the Government of India (GoI) focussing prominently on promoting innovation and entrepreneurship, gives a wider scope for NBFCs. NBFCs enjoy the advantages of better product lines, lower cost, wider and effective reach, robust risk management capabilities to check and control bad debts and a better understanding of their customer segments vis-à-vis the traditional banks.

Till the middle of the last decade, the unorganised sector catered to India's gold loan market with limited penetration of organised lenders. However, the gold loan industry is increasingly formalising now with established and organised players gaining market share. Traditionally known as a hyper retail local business, India's gold loan market has started attracting large investors since last decade. India has seen the emergence of gold loan speciality players like Manappuram Finance during this time.

In next few years, Gold loan market is projected to grow at a CAGR of 10 - 12%.

With credit demand expected to rise, the gold loan market is projected to grow between 10 to 12 per cent over the next few years to reach a market size of Rs. 2300 to 2500 billion by FY 2021-22. Digital onboarding, delivery solutions and successful geographical expansion of the gold loan market to non-south geographies are a few key factors that facilitate the growth of specialised gold loan NBFCs. With the organised gold loan penetration levels below 4%, there is headroom for growth in this market. Financial institutions with the right focus, operational capabilities, and availability of funds, refreshing products and modern technology are concentrating to capture a large market share and profitable returns.

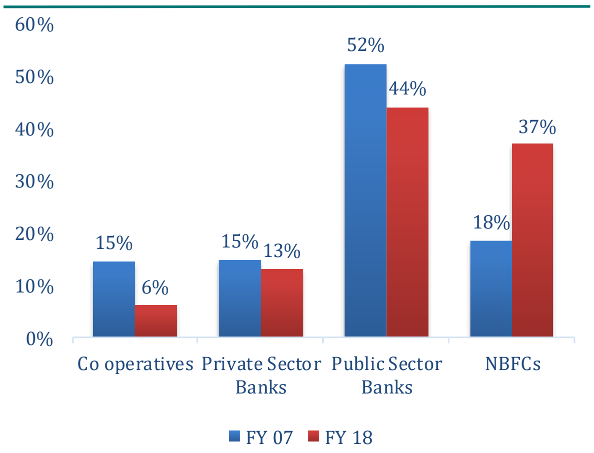
Gold Loans – Are NBFCs better positioned?

Gold loans occupy a special place in the portfolio of Indian financial service provider's book. The potential borrowers – those in urgent need of money and possess some gold, gives a marked preference for the service of these gold loan NBFCs compared to other institutional options. By offering advantages in terms of cost, security, and convenience, these NBFCs meet a vital need of the market in a way superior to other players.

The potential borrowers give a marked preference for the service of specialised gold loan NBFCs compared to other institutional players.

The large gold loan NBFCs stands out in this business where credibility and credentials play a vital role as people entrust someone to keep family jewels that are precious to them beyond monetary values. These NBFCs are almost like banks and are well governed, with established procedures and policies. Their branches have sufficient security measures to ensure the safety of the collateral. The highly penetrated branch network of these NBFCs acts as an added advantage as the borrowers may not desire to commute long distance with gold. Also, these NBFCs ensure that the borrower enjoys the benefit of familiarity by recruiting at least some of their staffs in each branch locally. For those borrowers who are migrants from pawnbrokers, the rates charged by these NBFCs are considerably lower and others outweigh the benefits of an NBFC experience against a busy bank branch.

NBFCs gaining market share from FY 07 to FY 18



Source: Company, Geojit Research.

Over the years, the specialised gold loan NBFCs have captured a significant market share.

Over the years, these specialised gold loan NBFCs have captured a significant market share in India. They have also increased the overall demand for gold loans with their niche focus and targeted market expansion activities. Traditionally, southern India is the hub for gold loans. However, growing economic stability in India, coupled with increasing gold prices is bolstering the specialised gold loan NBFCs across the nation. Additionally, these NBFCs are adopting an aggressive approach to expand and penetrate to the non-South geographies, while at the same time focus on improving the productivity of their existing branches, beyond their traditional strongholds.

On various dimensions, gold loan NBFCs stand a notch ahead compared to banks and moneylenders.

Competitive advantages of gold loan NBFCs

Parameter	Gold Loan NBFCs	Banks	Moneylenders
Loan to Value (LTV)	Up to 75%	Lower than NBFCs	Higher than 75%
Processing Fees	No/Minimal	Much higher than NBFC's	Nil
Interest Charges	~ 18 to 26% p.a	~ 12 to 15% p.a	~ 36 to 60%
Penetration	High	Only Selective Branches	High
Disbursement mode	Cash/Cheque	Cheque	Cash
Working Hours	Beyond banking hours	Typical banking hours	Beyond banking hours
Regulation	By RBI	By RBI	No Regulation
Customer Service	High - Core Focus	Non-Core focus	Core Focus
Documentation	Minimal/ID proof	Entire KYC Compliance	Minimal
Repayment Flexibility	Flexible	Rigid	-
Turnaround time	10 minutes	1-2 hours	10 minutes

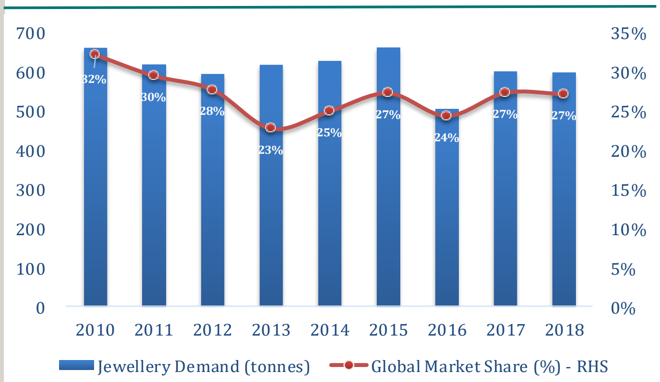
Source: Company, Geojit Research.

India is one of the largest consumers of gold jewellery in the world & together with China it makes up over half of the global consumer demand for gold.

Gold Demand in India

India is one of the largest consumers of gold jewellery in the world, together with China it makes up over half the global consumer demand for gold. India's fascination for gold dates back to ancient times, owing to the metals religious, cultural and investment significance. Gold continues to capture the imagination of all Indian's till date and there is an insatiable demand for the 'yellow metal' irrespective of movements in its prices. Consumption, instant liquidity and investment benefits are factors that drive people to buy and store gold. For Indian's, investments in gold have always been viewed as a reliable source in times of need, especially by rural households. Gold is a means to get quick liquidity to meet any exigencies. India continues to be one of the largest markets for gold and is estimated to hold ~12.9% of the world's total gold stock in FY18, up from 11.7% in FY12.

Jewellery demand in India



Source: World Gold Council, Geojit Research.

Rising income, inflation and excess rainfall have a positive impact on the gold demand, where as gold price have a negative effect.

Factors affecting demand for gold in India

There are various long term and short term factors which affect the gold demand in India, which is explained briefly in the following table

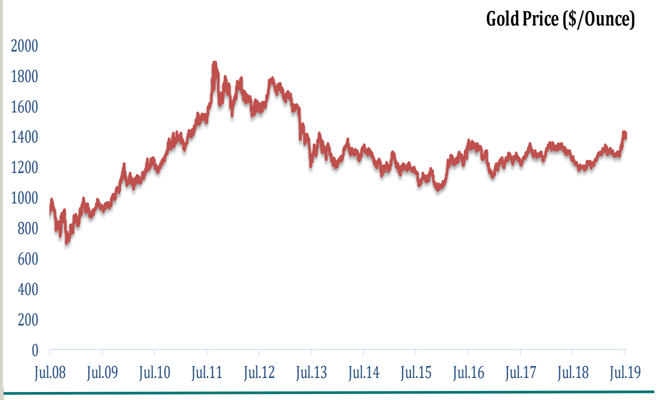
Long-Term Factors	Rising Income	For a 1% increase in income, the demand for gold will rise by 1%
	Gold Price	For a 1% increase in gold price, demand will decrease by 0.5%
Short-Term Factors	Inflation	For a 1% increase in inflation, demand increases by 2.6%
	Excess Rainfall	For a 1% increase in monsoon rainfall, gold demand rises by 0.5%

Source: World Gold Council, Geojit Research.

Tracking the journey of gold loan NBFCs

The evolution of gold loan business in India, over the past decade, can be understood in three phases, which are strongly influenced by gold prices and various regulatory changes from RBI, related to priority sector lending norms (PSL) and Loan to Value (LTV) ratios.

Gold price trend over past decade



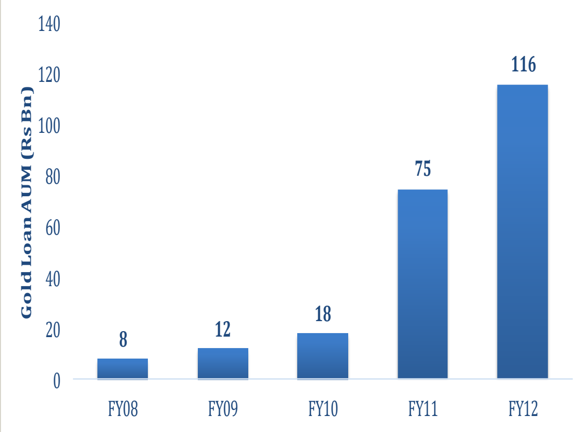
Source: Bloomberg, Geojit Research.

A) Phase 1 – The rapid growth phase

FY08-12 marked a rapid growth phase for gold loan NBFCs supported by various regulatory and macro parameters.

This phase extends from FY08 to FY12, which marked a glittering growth period for gold loan NBFCs. During this period, the AUM of Manappuram Finance has grown from just Rs8 Billion to Rs116 Billion while the number of branches has increased over 6 times. This rapid growth was supported by higher loan to value (LTV) ratios up to 85%, lower cost of funds due to the eligibility under Priority Sector Lending (PSL), buoyant economic growth and rising gold prices

Significant AUM growth from FY08 to FY12



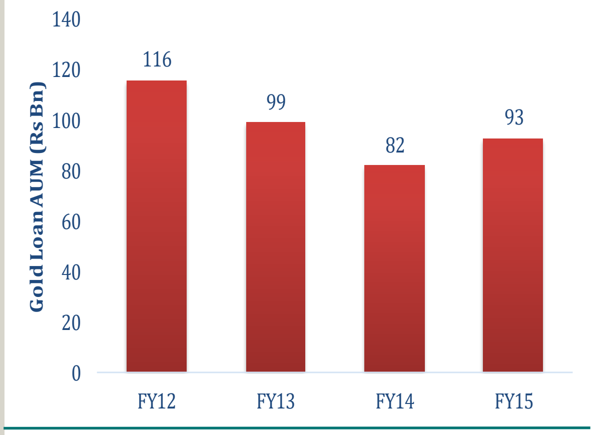
Source: Company, Geojit Research.

B) Phase 2 – The turbulent phase

The period of declining gold prices from FY12 to FY14 constitute phase 2, which was also further tightened by some of the regulatory changes adopted by the Reserve Bank of India (RBI).

From FY13 to FY14 Manappuram Finance has registered a de-growth of around 17% in the gold loan portfolio.

Declining AUM growth from FY12 to FY14



Source: Company, Geojit Research.

In March 2012, the Priority Sector Lending status of these NBFCs was removed by RBI, which led to higher borrowing cost. Apart from this, the LTV was capped at a maximum of 60%, which means these NBFCs can lend only up to 60% of the price of the gold. This has weakened the competitive positioning vis-à-vis banks and moneylenders as higher LTV focused customers moved to moneylenders whereas interest rate sensitive customers moved to banks. Thus, phase 2 is marked by fall in return ratios and profitability. From FY13 to FY14 Manappuram Finance has registered a de-growth of around 17% in the gold loan portfolio.

C) Phase 3 – The stable growth phase

From FY15 onwards, the gold loan NBFCs are on its revival path entering to the next phase of growth, supported by stable gold prices, regulatory changes and various strategic initiatives. RBI has increased the LTV ratio for gold loans to 75% creating an almost level playing field for gold loan NBFCs and commercial banks. These companies started reaching out to customers through enhanced marketing and branch activation initiatives like incentives and performance scorecards. Some gold loan companies started delinking the gold price volatility risk by offering more variants of lower tenure loan products.

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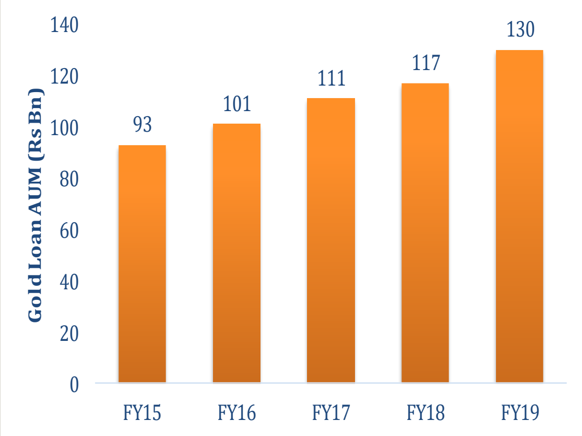
AUM growth picking up from FY15 onwards



Source: Company, Geojit Research.

Growth drivers for Gold Loan NBFCs

Although gold loans as a credit product is not a new phenomenon in the country, it is only in the recent past that Indian's have started losing their inhibitions over pledging their family heirlooms to mainstream commercial lenders and leveraging multiple benefits, such as instant credit, flexible schemes, lower interest rates and minimal paperwork without hassles of rigid credit appraisals. The growing penetration of gold loans in India can be attributed to various factors as follows:

A) Exclusion from mainstream loans

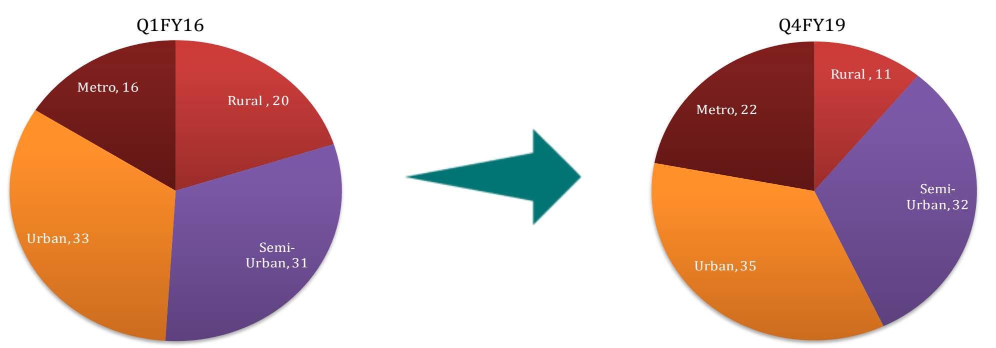
Gold loan comes as a relief to those rural and lower income groups who have lower accessibility to traditional banking products.

Traditional banking products are not as accessible to rural and lower-income groups as compared to relatively higher income groups. Also, lower credit scores would undermine one's efforts to get normal loans during distress periods. This is the situation faced by a large portion of the Indian population, especially those working in the unorganised sector in rural as well as urban areas. Gold loan offers a viable solution for them. As the gold loans are fully securitised, lenders have the option to recoup the full principal amount (in most cases) if the borrower defaults. Hence there is no need for extensive checks on borrower's previous payment records. Hence the relative ease in obtaining a loan approval has boosted the popularity of gold loans

B) Changing attitude towards applying gold loans

Apart from the rural communities who are willing to put household jewellery in the market, acceptance towards using family gold for financial needs is increasing in the relatively untapped urban market. Using gold loans to meet household exigencies is gaining popularity in Indian cities and metros.

Gold loans are getting more and more popular in nonrural areas.



Leveraging the vast customer base created through mainstay gold loan business through new synergistic non-gold products.

C) Diversifying Incomes for sustainable growth

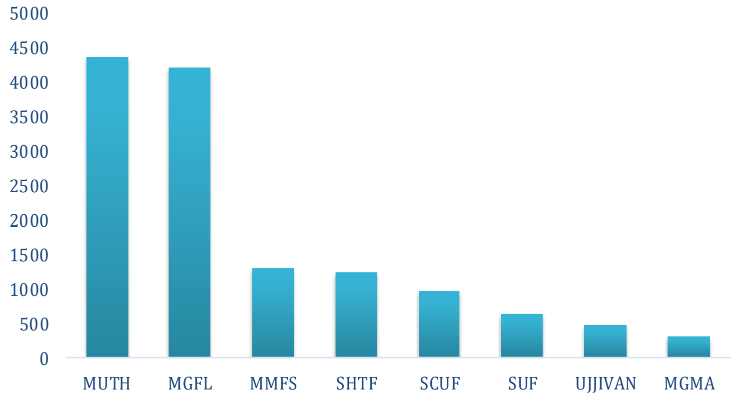
These NBFCs are strategically diversifying their business to leverage on the vast customer base developed through their mainstay gold loan business over the years. Under this strategy, Manappuram finance currently focuses on three main areas apart from the gold loan, namely housing finance, commercial vehicle loans and microfinance, with an aim to build their total non-gold portfolio to around 40 to 50 per cent of their total assets under management in coming years. In Q4FY19, these new business segments together constitute around one-fourth of their total loan portfolio.

D) Wider network auger well for diversification

Both these gold loan NBFCs have a relatively higher number of branches in the sector. By leveraging the strong brand name acquired through the gold loan business over the years, these companies can effectively utilize the well-established infrastructure for further growth and diversification.

Gold loan NBFCs have relatively larger number of branches, which cater to the growth through diversification.

Strong branch network of gold loan NBFCs



Source: Company, Geojit Research

E) A larger share of gold held by rural communities

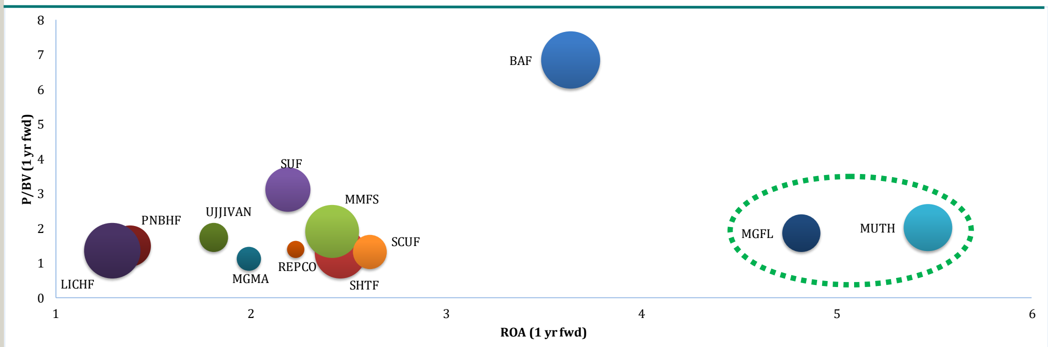
According to the World Gold Council (WGC) estimates, about 65 per cent of the Indian household gold held by the rural communities. With largely unpredictable rain and harvest seasons, accompanied by limited access to credit, farmers become cash trapped frequently. For them, unlocking the value of their household gold is the easiest way to meet their financial obligations. Additionally, the rising consumerism in rural areas is leading to increased gold loans being taken for non-income generating purposes.

Valuation

The gold loan NBFCs have relatively lower valuations and higher return on assets compared to other NBFCs.

Compared to peers, Gold loan NBFCs have higher ROA for relatively moderate valuation .

Gold Loan NBFCs – Better positioned in ROA Vs P/BV Matrix



** Size indicates market cap*
Source: Bloomberg, Geojit Research

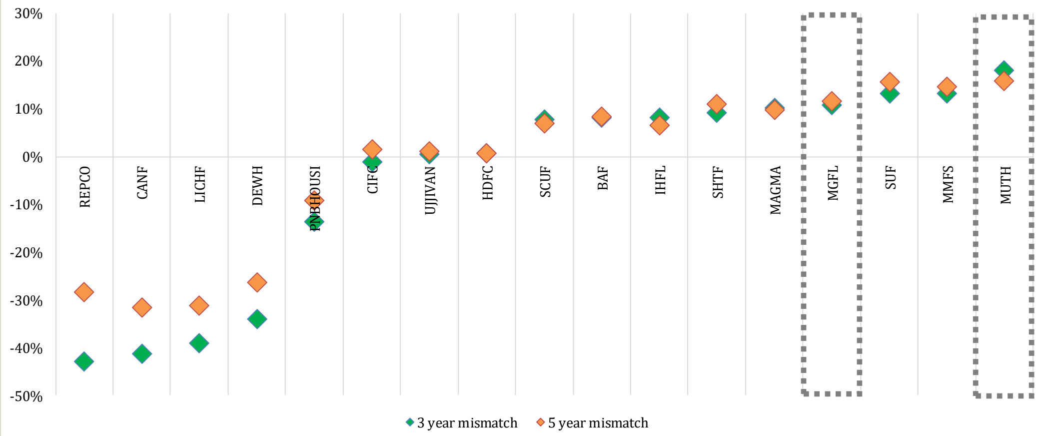
Note: MUTH Muthoot Finance, MGFL Manappuram Finance, MMFS Mahindra & Mahindra Financial Services, SHTF Shriram Transport Finance, SCUF Shriram City Union Finance, SUF Sundaram Finance, UJJIVAN Ujjivan Financial Services, MGMA Magma Fincorp, CANFIN Can Fin Homes, REPCO Repco Home Finance, CAFL Capital First, BAF Bajaj Finance

Asset Liability Management

As far as asset liability management (as per FY18 balance sheet) is considered, gold loan NBFCs are better positioned compared to others.

Gold loan NBFCs have better asset liability management, which gives them pretty comfortable position in issues of drying liquidity.

ALM mismatch—Gold loan NBFCs are better positioned



Source: Company, Geojit Research.

Industry Risks

A) Reduction in collateral value

Decrease in gold prices and the steep decline in the asset value, which in a way diminishes the sentimental attachment to the collateral, can pose a serious threat to gold loan business. Companies across the industry are implementing robust risk management mechanisms to meet the contingencies of fall in collateral value with shorter tenure products and duration linked loan to value ratios.

B) Adverse Regulatory Changes

Competition from banks and unorganised sector, a sharp decrease in the price of gold over a shorter span of time, some adverse regulatory measures, and introduction of some alternate loan products forms the key risk to this industry.

Even though ample guidelines have been framed for regulating the industry, any further change in the regulations can have the capacity to adversely affect the growth of gold loan business. In such cases, the players may find the business less profitable which may in-turn disturb their sustainability.

C) Alternate loan products

Popularisation and availability of other loan products like personal loan, loan against property and home loan, among others can reduce the demand for gold loan. Additionally, diminishing the availability of gold jewellery with borrowers and their unwillingness to pledge, serve as a potential threat to the growth of this sector.

D) Competition

Banks which have a significant advantage in cost of funds and can grow their gold loan business by offering lower interest rates compared to NBFCs, thereby imposing a threat to the NBFCs gold loan business. Besides. Also, even today, the unorganised sector caters to a large segment of customers and retains their niche customer segment thus limiting the growth opportunities of NBFCs.

Note:
REPCO Repco Home Finance, CANF Can Fin Homes, LICHF LIC Housing Finance, DEWH Dewan Housing Finance,
PNBHOUSI PNB Housing Finance, CIFC Cholamandalam Investment and Finance Company, UJJIVAN Ujjivan Financial Services,
HDFC Housing Development Finance Corporation, SCUF Shriram City Union Finance, BAF Bajaj Finance,
IHFL Indiabulls Housing Finance, SHTF Shriram Transport Finance, MGMA Magma Fincorp, MGFL Manappuram Finance,
SUF Sundaram Finance, MMFS Mahindra & Mahindra Financial Services, MUTH Muthoot Finance

Investment Rationale...

Gold loan business on a revival path

After going through the challenging years of FY13 and FY14, the company decided to change its strategy in FY15, to strengthen the gold loan business and protect the business from volatility in gold prices and drive volume growth. Accordingly, the company introduced short tenure gold loans and over the last couple of years, it has managed to shift more than 90% of gold loan portfolio to the short term bucket of three months.

Earlier Scenario

Loan Tenure	1 year
Gold Value	100
LTV	75%
Gold Loan	75
Interest Rate	24%
Interest Cost	21
Total	96

Source: Company, Geojit Research.

Introduction of shorter tenure products to reduce the risk from volatility in gold prices and to drive business growth.

In this case, if the customer does not pay or close the loan, there is only a very little margin of safety to recover the principal as well as the interest. In order to overcome this, the product structure was recalibrated by linking Loan to Value (LTV) to the loan tenure.

Current Scenario

Loan tenure	3 months	6 months	9 months	1 year
Gold Value	100	100	100	100
LTV	75%	70%	65%	60%
Gold Loan	75	70	65	60
Interest Rate*	24%	24%	24%	24%
Interest Cost	7.5	11.2	14.3	16.8
Total	82.5	81.2	79.3	76.8

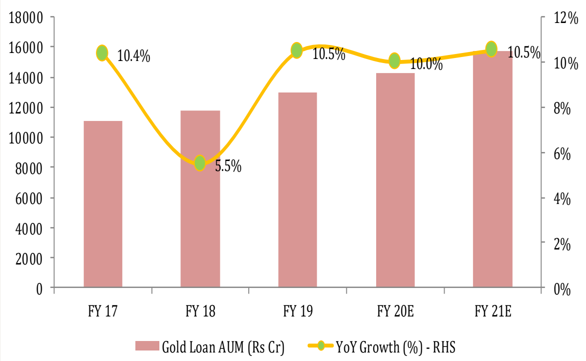
Source: Company, Geojit Research.

In the current scenario, the maximum permissible LTV of 75% is available on loans of shorter tenure rather than one year as was the standard practice earlier. In case of default, this would ensure ample margin of safety in order to recover principal as well as interest. This has helped the company to improve the credit quality of the gold loans.

Online gold loans (OGL) accounts for about 39% of total gold loan assets under management.

With the brick and mortar branches less relevant in today's world, MGFL has launched Online Gold Loan (OGL) back in 2015. These loans are offered at the convenience of the borrower, where only one-time branch visit is required to deposit the gold and loans up to Rs1.5cr can be availed online at anytime from anywhere in the world. With features like instant approval and free safe custody of gold, OGL is gaining popularity and currently account for about 39% of the total gold loan AUM.

Gold Loan AUM to grow at 10% CAGR over FY19-21E



Source: Company, Geojit Research.

** Interest rate may vary depending upon the loan tenure*

The Company's gold loan portfolio registered a YoY growth of 5.5% to increase from Rs11,125cr to Rs11,735cr as of March 31, 2018, which further increased to Rs12,961cr in Q4 FY19. The growth in gold loan business was backed by moderate growth in gold tonnage which increased by 4.8% to reach 64 tonnes in FY18, presently standing at around 67.5 tonnes. The average gold prices were relatively firm during the past year, helping the AUM growth to an extent. The momentum of growth picked up in the third and fourth quarters of FY18 as the first two quarters faced the after effects of demonetisation, particularly its lingering impact on the rural and unorganised sector which is a key market for the company. It is expected that the pick-up in volumes seen in the second half of FY18 will be sustained going ahead. With increasing gold prices and declining interest rates, we expect the gold loan AUM to register a 10% CAGR growth in FY19-21E, with about Rs14,250cr in FY20.

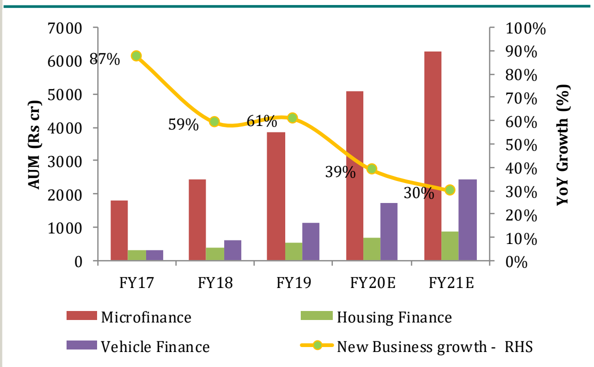
Robust growth in new product segments

The company has acquired Milestone Home Finance in 2014 (later renamed to Manappuram Home Finance), Asirvad Microfinance in 2015, and has organically initiated commercial vehicle lending and loan against property during FY15.

With comfortable Capital Adequacy Ratio (CAR) levels, much above the regulatory requirement of 15%, and by leveraging the strong brand equity acquired through the mainstay gold loan business over several years, reinforced with the existing retail customer base and pan India distribution presence, the company has ventured into new synergistic product segments like Microfinance (MFI), Housing Finance (HF), and Vehicle Finance (VF) back in FY15. The company has acquired Milestone Home Finance in 2014 (later renamed to Manappuram Home Finance), Asirvad Microfinance in 2015, and has organically initiated commercial vehicle lending and loan against property during FY15.

The strategy that was envisioned to utilise the surplus capital to build or acquire new lending products relevant to the prevailing retail customer base started bearing fruit with these new businesses currently representing around one-third of the total assets under management. In FY19, the new businesses helped the overall AUM growth as microfinance (57.6% growth), home loans (38.5%), commercial vehicle loans (78.2%) and other (Non-gold) loans (69.2%) portfolios have marked notable performance. With all these new businesses getting stabilized, we expect the total AUM from these businesses to grow at 34% CAGR in FY19-21E. As per the latest quarterly result of Q4FY19, the asset under management of microfinance has reached Rs3,841cr, that of vehicle finance has reached Rs1,115cr, and the housing finance AUM has reached Rs519cr, which is as per our expectations.

New businesses AUM to grow at 34.3% CAGR over FY19-21E

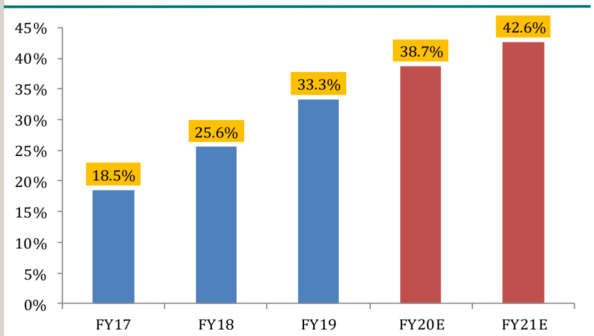


Source: Company, Geojit Research.

Over the years, company targets 50:50 mix in gold and non-gold business, to mitigate the risk of being a single-product NBFC.

Over the years, MGFL expects the non-gold portfolio to contribute around 50% of the total assets under management, thus mitigating the risk of being a single-product NBFC. We estimate the new businesses to constitute about 43% of the consolidated AUM by FY21E.

New business to have ~43% of AUM mix by FY21E



Source: Company, Geojit Research.

MFI - Leading player in non-gold business

Spread across 22 states/union territories with 942 branches, Asirvad has a pan India presence catering to the needs of 1.80million customers

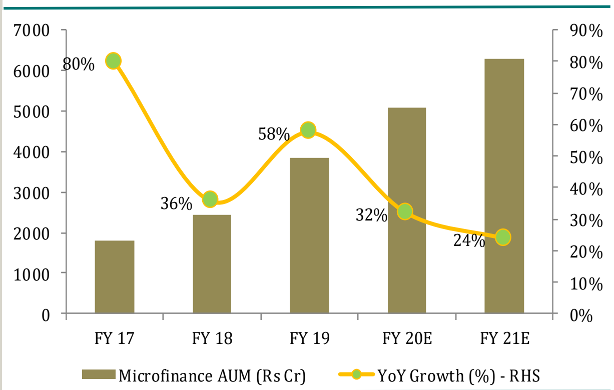
In February 2015, MGFL acquired an 85% stake in Asirvad Microfinance Ltd. and subsequently increased it to 90%. Spread across 22 states/union territories with 942 branches, Asirvad has a pan India presence catering to the needs of 1.80 million customers, making it the sixth largest NBFC-MFI in India. Three types of loans are offered at present, which are Income generating programme (IGP) loan, Product loan and SME loan, with tenure of up to 24 months.

With both micro and macro factors playing well, we expect the AUM of Asirvad to reach a little above Rs5000cr in FY20 with a CAGR growth rate of 28% from FY19 to FY21E.

Currently Manappuram Home Finance has 35 branches across 6 states majorly concentrated in southern and western India.

The company exhibited a spectacular performance soon after the acquisition, with a five-fold AUM growth from FY15 to Q2FY17. From Q3FY17 onwards till the 1st half of FY18, the sailing was difficult for microfinance sector with the rural economy and the unorganised sector continued facing the after effects of demonetisation and GST implementation. In fact, it was only in the 2nd half of FY18, Asirvad could get back on the growth track and since then it picked up quite well. With an AUM of Rs2,437cr in FY18 as compared to Rs1,796cr in FY17, Asirvad registered about 36% YoY growth. In Q4FY19, the microfinance AUM has reached about Rs3,841cr, registering 58% YoY growth.

MFI AUM to grow at 28% CAGR over FY19-21E



Source: Company, Geojit Research.

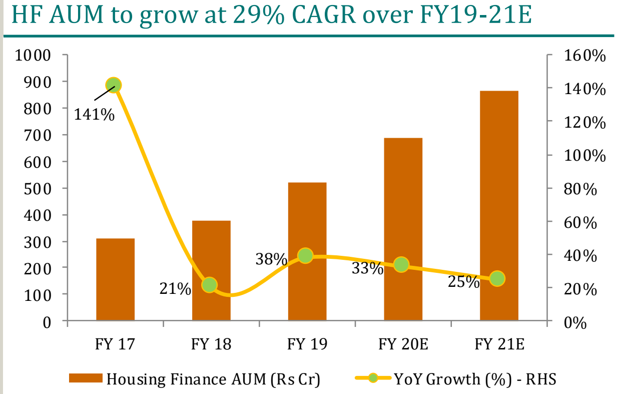
In India, the MFI industry is at a robust growth phase for the past few years (except for the small period during demonetisation) and has the potential to grow even stronger. The lower penetration of microfinance lending coupled with relentless efforts of the Government of India (GoI) and the Reserve Bank of India (RBI) to nurture the growth of formal finance enhance the prospects of organised lenders, which currently constitute only about 28% of the 6 lakh crore industry. Asirvad Microfinance, being a leading player, is effectively tapping this opportunity catering to the needs of a larger segment of the people at the bottom of the pyramid via microfinance route using collateral-free, joint liability model. With both micro and macro factors playing well, we expect the AUM of Asirvad to reach a little above Rs5000cr in FY20 with a CAGR growth rate of 28% from FY19 to FY21E.

Housing finance– focusing affordable segment

Manappuram Home Finance, a wholly owned subsidiary of Manappuram Finance, was incorporated as Milestone Home Finance Company Pvt. Ltd. (Milestone), which was acquired in February 2014 and renamed as Manappuram Home Finance Ltd. The company started commercial operations in January 2015 with focus on affordable housing finance segment, for mid to low-income group. Currently, HF has 35 branches across 6 states majorly concentrated in southern and western India. The company offers two types of products, namely home loans and loan against property with an average ticket size of about Rs10 lakh and Rs. 8.00 lakh respectively.

India's housing finance market is worth an estimated Rs9.7 trillion and has achieved steady growth over the last 3 years. In spite of this, the housing finance market continues to face considerable supply constraints, particularly in the lower income segment, due to the perceived high risk of lending to the informal sector. The lower income housing market is worth over Rs1,100,000cr, comprises of approximately 2.2cr households consisting of both salaried and self-employed individuals. The housing finance market in India has the potential to expand and include these borrowers who are currently not being served by financial institutions. The Bing Bang reforms implemented in 2017, though caused some hiccups in the sector, have also brought significant changes in the tax, regulatory, and business environment in India. Post demonetisation, the introduction of RERA and GST has improved the transparency and accountability in the sector. Also with increasing urbanisation and the expanding urban fabric of tier II and tier III cities in the country, affordable housing finance is promised to grow at a higher rate.

HF AUM to grow at 29% CAGR over FY19-21E



Source: Company, Geojit Research.

Housing Finance business is expected to grow at 29% CAGR over FY19-21E.

Housing Finance has grown from Rs129cr AUM in FY16 to Rs375cr in FY18, at a remarkable rate of over 70% CAGR. With a focus on steady phase growth, the company has an AUM target of Rs1,000cr over the next 2-3 years while maintaining the profitability and credit quality upbeat. The comparatively lower ticket size also gives an added advantage for the company in the housing finance sector. In Q4FY19, the company has shown a 39% YoY growth in housing finance AUM, reaching at Rs518cr.

Given the strategic importance of affordable home finance to MGFL's future plans, as it proceeds with the diversification of the range of its financial products, it is reasonable to expect strong support from the parent. The business is scalable and is expected to grow substantially, to the tune of 29% CAGR over FY19-21E.

Vehicle Finance to cross Rs1,700cr AUM in FY20E

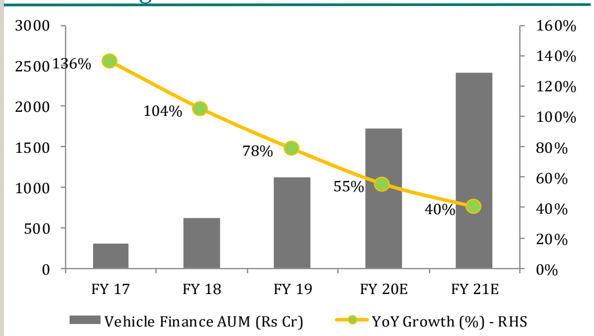
The vehicle finance portfolio is about Rs11 billion, spread across 168 locations in 21 states.

In order to diversify and de-risk the portfolio, Manappuram Finance had entered into commercial vehicle financing activity in FY15, operating from southern and western regions and subsequently entering into other regions, catering to the needs of underserved customers who do not have access to the formal banking system.

The vehicle finance portfolio is about Rs11 billion, spread across 168 locations in 21 states as on March 31, 2019. The portfolio mainly comprises commercial vehicles, and has a smaller share of two-wheeler and used cars, with an average ticket size of around Rs7.3 lakhs.

We expect the vehicle finance AUM to reach above Rs1,700cr in FY20E, registering a 47% CAGR growth in FY19-21E.

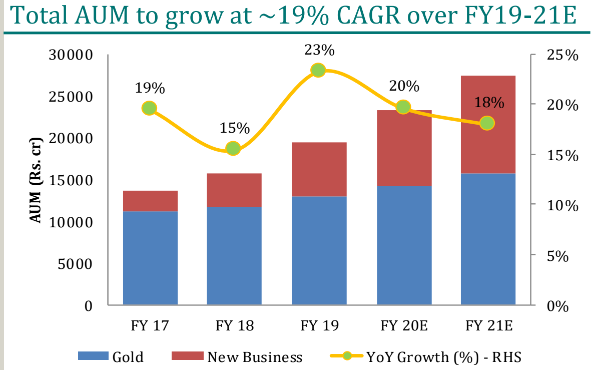
VF AUM to grow at 47% CAGR over FY19-21E



Source: Company, Geojit Research.

The AUM of vehicle finance business almost doubled in FY19 to Rs1,115cr compared to FY18, owing to healthy traction and improved demand momentum in the pre-owned commercial space. The company is leveraging the existing gold loan branches to expand vehicle finance business and hence will incur very little expenditure leading to greater profitability. Going forward, with sustained growth momentum and by leveraging the existing customers, we expect the vehicle finance AUM to reach above Rs1,700cr in FY20E, registering a 47% CAGR growth in FY19-21E.

Total AUM to grow at ~19% CAGR over FY19-21E



Source: Company, Geojit Research.

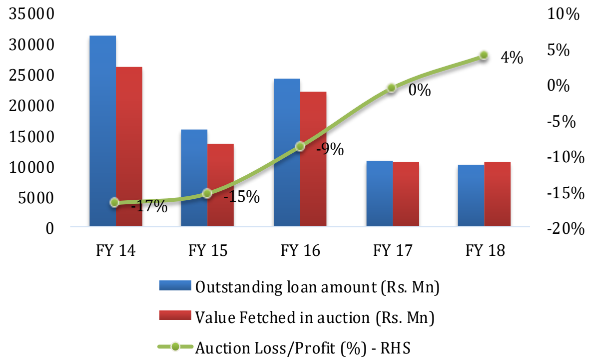
With gold loan AUM growing at 10% CAGR and new businesses AUM growing at 34% CAGR, we expect the total AUM to grow at ~19% CAGR in FY19-21E.

With gold loan AUM growing at 10% CAGR and new businesses AUM growing at 34% CAGR, we expect the total AUM to grow at around 19% CAGR in FY19-21E.

Significant reduction in auction losses

With the introduction of shorter tenure gold loan products in recent years, the company was able to significantly bring down the auction losses. With an auction loss of around 17% in FY14, the company was able to reduce the auction loss to 0% and in fact had an auction gain in FY18. The relatively stable nature of gold prices over the years also helped the company to achieve this.

Auction losses to auction gain



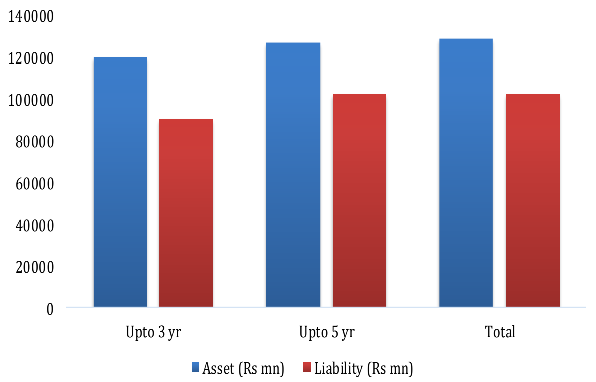
Source: Company, Geojit Research.

Healthy asset-liability management

Mainly due to the shorter tenure gold loan products, MGFL have a positive asset-liability maturity pattern.

As per the latest annual report, the company has a healthy asset-liability maturity pattern going forward, which is mainly due to the shorter tenure gold loan products. As of March 2018, on a one-year, three-year and five-year basis, the total assets that get matured is about 1.33, 1.24 and 1.26 times the total liabilities that get matured in the same time period, respectively. This gives a much safer and comfortable position for the company in case of a difficult situation like as of liquidity crisis.

Asset liability maturity pattern



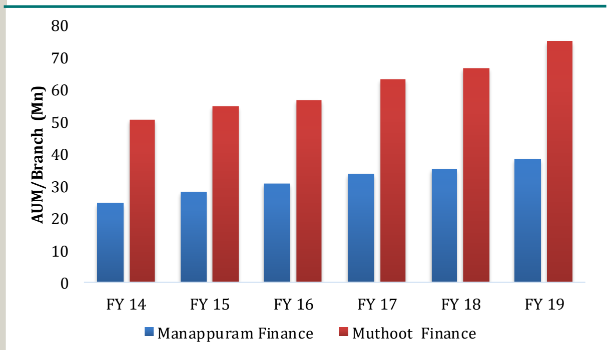
Source: Company, Geojit Research.

Ample space for AUM growth

The total asset under management of Muthoot Finance is nearly double to that of Manappuram Finance, which can be mainly attributed to the history as well as size of the their businesses. The gold loan AUM per branch of Muthoot is almost 2 times to that of Manappuram in FY19. This signifies that there is a lot of scope for the company to enhance the productivity of the business, which can lead to better operating leverage going forward.

Significant scope for scaling up AUM/Branch.

Wider scope for increasing business



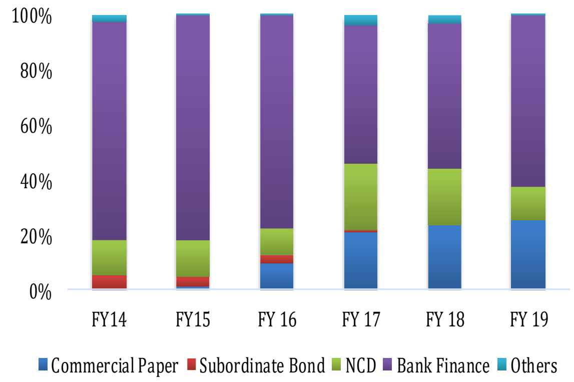
Source: Company, Geojit Research.

Financials...

Well diversified borrowing mix

MGFL has a well-diversified borrowing mix across commercial paper, non-convertible debentures and bank finance. The company has reduced the dependency on bank finance from more than 80% in FY15 to the range of about 62% in FY19. The company has increased the share of commercial paper from 0% in FY14 to 25% in FY19, whereas the share of Non-Convertible Debentures (NCDs) is almost at the same level around13%.

Borrowing Mix



Source: Company, Geojit Research.

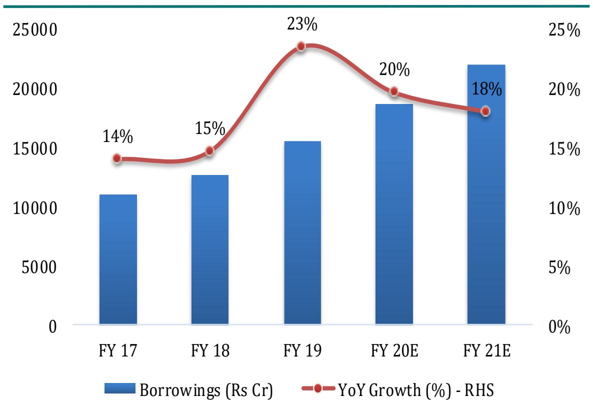
Besides, the company also enjoys good credit ratings for its long term and short term borrowings, which is depicted below.

CREDIT RATING		
Manappuram Finance		
Long Term	AA- (Positive)	CRISIL
Long Term	AA- (Stable)	ICRA
Long Term	AA+ (Stable)	Bricwork
Long Term	AA (Stable)	CARE
Short Term	A1+	CARE
Commercial Paper	A1+	CRISIL, CARE
Asirvad Microfinance		
Long Term	A+ (Positive)	CRISIL
Long Term	A+ (Stable)	CARE
Short Term	A1+	CRISIL
Housing Finance		
Long Term	A+ (Positive)	CRISIL
Long Term	AA- (Stable)	CARE
Short Term	A1+	CRISIL

Source: Company, Geojit Research.

We expect the total borrowings of the company to grow at a CAGR of 19% from FY19-21E, which will strongly support the total AUM growth estimated around 19% CAGR over the same period.

Total Borrowings to grow at 19% CAGR over FY19-21E



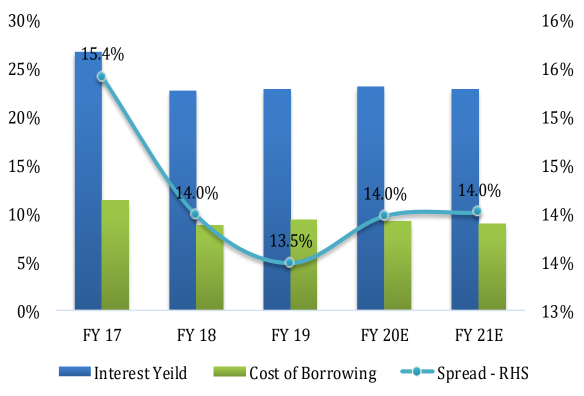
Source: Company, Geojit Research.

Net Interest Margin to be maintained around 14%

We expect the cost of borrowing to decline by around 50-60bps, with a marginal decline in yield, the spread to be maintained around 14% in the coming years

The company has significantly brought down the cost of borrowing from 11.7% in FY14 to 8.7% in FY18. With Interest rate and bond yield on a higher side for a significant portion of FY19, with repo rate at 6.50% till the 6th bimonthly monitory policy on 6th February 2019, the cost of borrowing has increased by 57 bps to 9.27% in FY19. Going forward, with three consecutive rate cuts in the last two monetary policy review meeting (repo rate currently standing at 5.75%), along with the benefits from using credit rating for assigning risk weighted assets by the lending institutions, we expect the cost of borrowing to decline to the tune of around 50 to 60bps in the coming years. Also, we expect the interest yield to marginally decline by around 20bps, with increasing share of new businesses with comparatively lower yields going ahead. With these effects, we expect the total spread to be maintained around 14% in FY20E and FY21E.

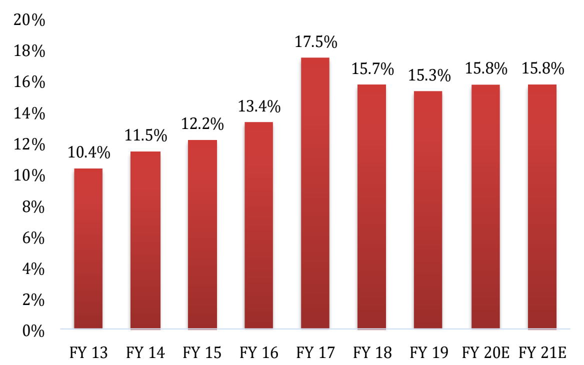
Interest spread to marginally improve going ahead



Source: Company, Geojit Research.

The company has exhibited a continuous increase in net interest margin from FY13 to FY17 and showed some decline in FY18 as the business was affected by the repercussions of demonetisation and GST implementation. It further declined marginally in FY19 due to the side effects of liquidity crisis and rising cost of funds. However, with a declining interest rate scenario we expect NIM to marginally improve going ahead.

NIM to be maintained above 15% over FY19-21E



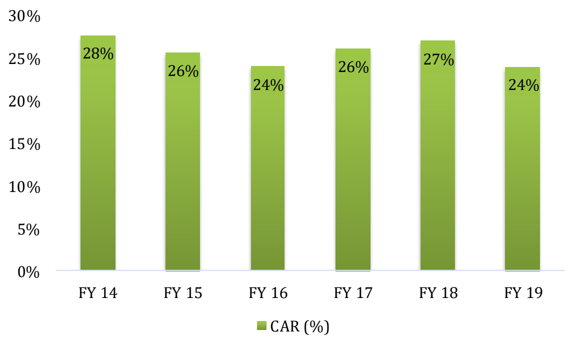
Source: Company, Geojit Research.

Healthy capital adequacy ratio (CAR)

Capital adequacy ratio (CAR) consistently maintained much above the regulatory requirement of 15%.

The company have a capital adequacy ratio of 23.9 per cent in FY19, which is far above the regulatory requirement of 15 per cent. In fact, the company has ventured into new business segments to effectively utilise this excess capital.

CAR to be maintained well above regulatory requirement



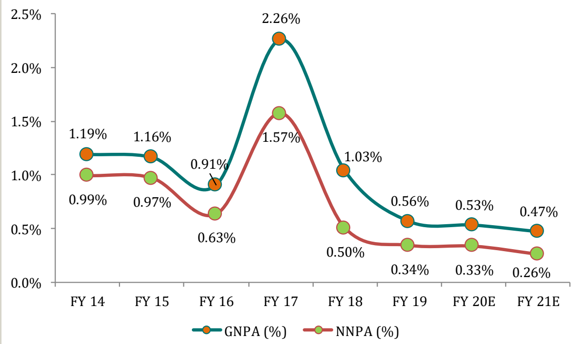
Source: Company, Geojit Research.

One of the lowest NPAs among NBFC space

In Q4FY19, the consolidated GNPA and NNPA stood at 0.6% and 0.3% respectively.

Gold loan being a low risk business, as the company have the option to auction the gold in case of a default, the gross non-performing assets of the standalone business stood at just 0.7% in FY18. In FY19, the company was able to maintain the reduce this to 0.5%. We don't expect the company to overshoot the current NPA levels in the years ahead. As far as microfinance business is considered, GNPA stood at 2.33% as of FY18, and further reduced to 0.48% in Q4 FY19, whereas the Net NPA was maintained at 0% for the past few quarters. Considering the housing finance business, the GNPA stood at 4.8% in FY18, and reduced to 3.9% in Q4 FY19. The GNPA and NNPA of vehicle finance stands at 1.9% and 0.8% respectively inQ4FY19. In Q4FY19, the consolidated GNPA and NNPA stood at 0.6% and 0.3% respectively. We expect both gross & net NPA to decline in the upcoming years.

NPA's expected to improve going forward

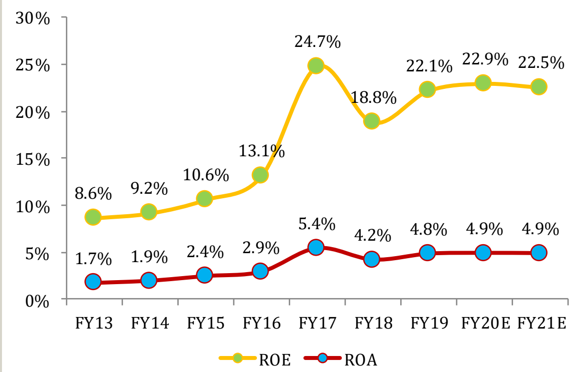


Source: Company, Geojit Research.

Attractive return ratios going ahead

As per our analysis, we expect a gradual increase in the return on assets (ROA) and return on equity (ROE) ratios going forward supported by a PAT growth of 23% and 18.2% in FY20E and FY21E respectively.

Return ratios to be well maintained



Source: Company, Geojit Research.

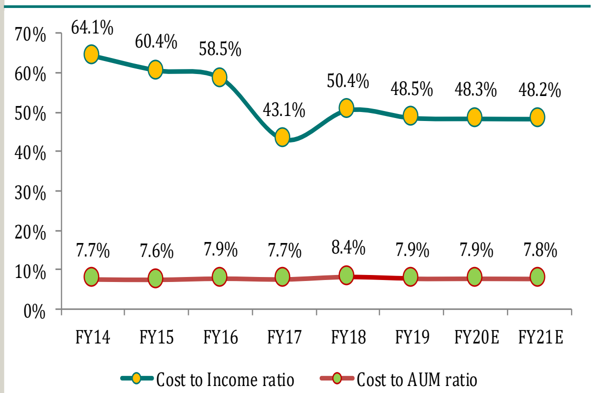
Cost to be controlled by co-locating businesses

The cost to income ratio expected to reduce to 48.2% by FY21E.

Over the last few years, by co-locating HF and VF businesses with gold loan branches, the company was able to significantly reduce the cost to income ratio and keep the cost to AUM ratio at almost constant level. We expect both cost to income ratio and cost to AUM ratio to reduce to 48.2% and 7.8% respectively by FY21E.

The cost to AUM ratio to marginally reduce to 7.8% in FY21E.

Synergistic business expansion to reduce costs



Source: Company, Geojit Research.

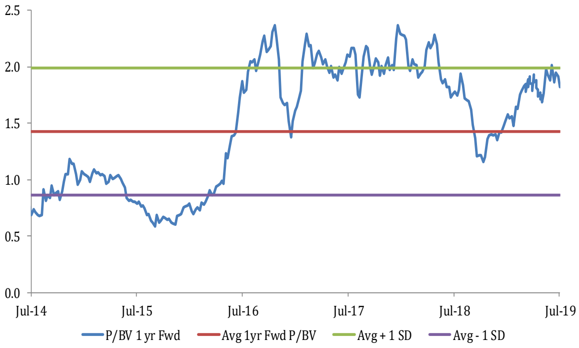
Valuation

With strong macro factors of rising gold prices and reducing interest rates, we value Manappuram Finance Ltd. At 2.0x FY21E Adj.BVPS and recommend 'Buy' with a target price of Rs154.

After temporary hiccups in the businesses caused by the lingering effects of demonitisation especially on the rural economy, the management is targeting healthy growth going forward. The company is also having one of the lowest NPA's in the non-banking finance space due to the secured nature of lending for the gold loan business, which accounts for about 2/3rd of their loan book. The capital adequacy ratio of the company is much above the regulatory requirement, which eliminates the need to raise any additional capital for coming few years. The company also doesn't have any notable asset liability mismatches to be a cause of concern.

At CMP, the stock is trading at P/BV of 2.0x and 1.7x for FY20E BVPS of Rs64.9 and FY21E BVPS of Rs 78 respectively. With strong macro factors of rising gold prices and reducing interest rates, we value Manappuram Finance Ltd. at 2.0x FY21E Adj.BVPS and recommend 'Buy' with a target price of Rs154.

One year forward Price to Book Value



Source: Company, Geojit Research.

Company Background

The company was incorporated as Manappuram General Finance and Leasing Limited on July 15, 1992 in Kerala, and later renamed as Manappuram Finance Limited. The company's origin goes back to 1949, when it was founded in the coastal village of Valapad in Thrissur district of Kerala, and was involved in pawn broking and money lending on a modest level. It is the first non-banking finance company in Kerala to receive a certificate of registration from RBI. The company went public in 1995, and since then it has grown substantially. At present the company has a total asset under management of around Rs194 billion, with Rs130 billion in gold loan business and remaining spread among microfinance, housing finance, vehicle finance and other loans.

Management team

Mr. V.P. Nandakumar
Managing Director & CEO
Chief Promoter of Manappuram Group

Mr. B.N. Raveendrababu
Executive Director
Director since 1992

Mrs. Bindu AL
CFO
Chartered Accountant with over 20 years in the area of finance and accounts

Mr. Raja Vaidhyanathan
Managing Director – MFI
Erstwhile promoter of Asirvad Microfinance with over 33 years of experience

Mr. Jeevandas Narayan
Managing Director – Housing Finance
Erstwhile MD of State Bank of Travancore with over 37 years of experience

Mr.Subhash Samant
CEO – Housing Finance
Over 21 years of experience

Mr. K Senthil Kumar
Head – Commercial Vehicle
Over 21 years of experience

Mr. Kamalakar Sai Palavalasa
EVP – Insurance
Over 24 years of experience

Mrs. Puneet Kaur Kohli
SVP –CTO
Over 22 years of experience

Consolidated Financials

PROFIT & LOSS

Y.E March (Rs cr)	FY17A	FY18A	FY19A	FY20E	FY21E
Interest Income	3,376	3,354	4,012	4,930	5,803
Interest Expense	1,169	1,030	1,319	1,559	1,803
Net Int. Income	**2,208**	**2,324**	**2,693**	**3,371**	**4,000**
Change	*57.5%*	*5.3%*	*15.9%*	*25.2%*	*18.6%*
Non Int. Income	33	125	167	111	111
Operating Income	2,240	2,449	2,859	3,482	4,111
Change	*57.3%*	*9.3%*	*16.8%*	*21.8%*	*18.0%*
Operating Exp.	965	1,235	1,386	1,681	1,982
Pre Prov. Profit	1,251	1,214	1,473	1,770	2,111
Prov. & Conting.	109	177	46	42	50
PBT	**1,166**	**1,037**	**1,427**	**1,760**	**2,079**
Change	*112.6%*	*-11.1%*	*37.6%*	*23.3%*	*18.2%*
Tax	407	360	498	616	728
Tax Rate	35%	35%	35%	35%	35%
Reported PAT	756	676	929	1,144	1,352
Adj*	0	0	0	0	0
Adj. PAT	**756**	**676**	**929**	**1,144**	**1,352**
Change	*113.6%*	*-10.5%*	*37.4%*	*23.0%*	*18.2%*
No. of shares (Cr)	84	84	84	84	84
EPS (Rs)	9.0	8.0	11.0	13.6	16.1
Change	*113.8%*	*-10.7%*	*37.3%*	*22.7%*	*18.2%*
DPS (Rs)	2.00	2.00	2.20	2.20	2.40

BALANCE SHEET

Y.E March (Rs cr)	FY17A	FY18A	FY19E	FY20E	FY21E
Cash	589	724	1,164	1,126	1,531
Loans & Advances	13,406	15,244	17,812	22,087	26,057
Investments	5	5	174	51	101
Gross Fixed Assets	494	639	693	747	796
Net Fixed Assets	183	269	312	216	169
CWIP	1	0	1	0	0
Intangible Assets	39	41	54	55	57
Def. Tax (Net)	96	110	89	144	170
Other Assets	665	637	848	734	790
Total Assets	**14,983**	**17,030**	**20,454**	**24,413**	**28,875**
Deposits	0	0	2	0	0
Debt Funds	10,781	12,487	15,176	18,086	21,525
Other Liabilities	813	684	697	842	989
Provisions	25	45	55	59	63
Equity Capital	168	169	169	169	169
Reserves & Surplus	3,195	3,645	4,356	5,289	6,398
Shareholder's Funds	3,363	3,813	4,525	5,458	6,566
Total Liabilities	**14,983**	**17,030**	**20,454**	**24,413**	**28,875**
BVPS (Rs)	**40.0**	**45.3**	**53.8**	**64.9**	**78.0**
Change	*21.8%*	*14.1%*	*18.3%*	*20.3%*	*20.3%*
Adj. BVPS (Rs)	**37.4**	**44.7**	**53.1**	**63.9**	**77.2**
Change	*17.0%*	*19.5%*	*19.0%*	*20.3%*	*20.7%*

RATIOS

Y.E March	FY17A	FY18A	FY19E	FY20E	FY21E
Profitab. & Return					
Interest yield (%)	26.7	22.7	22.9	23.1	22.9
Cost of funds (%)	11.3	8.7	9.4	9.1	8.9
Spread.(%)	15.4	14.0	13.5	14.0	14.0
NIM (%)	17.5	15.7	15.3	15.8	15.8
ROE (%)	24.7	18.8	22.1	22.9	22.5
ROA(%)	5.4	4.2	4.8	4.9	4.9
Business Growth (yoy)					
Gold Loan AUM (%)	10.4	5.5	10.5	10.0	10.5
Microfinance AUM (%)	79.8	35.7	57.6	32.0	24.0
Total AUM (%)	19.5	15.4	23.3	19.6	18.0
Operating Ratios					
Cost to Income (%)	43.1	50.4	48.5	48.3	48.2
Cost to Assets (%)	6.9	7.6	7.2	7.2	7.1
Asset Quality					
GNPA (%)	2.3	1.0	0.6	0.5	0.5
NNPA (%)	1.6	0.5	0.3	0.3	0.3
Capital Adequacy					
CAR (%)	26.1	27.0	24.0	27.0	27.0
Valuation ratios					
P/E (x)	14.4	16.1	11.7	9.5	8.1
P/B (x)	3.2	2.8	2.4	2.0	1.7
Adj. P/B (x)	3.5	2.9	2.4	2.0	1.7

Recommendation Summary (last 3 years)

Source: Bloomberg, Geojit Research.

Dates	Rating	Target
16 July 2019	Buy	154

Investment Rating Criteria

Large Cap Stocks;		
Buy	-	Upside is above 10%.
Hold	-	Upside is between 0% - 10%.
Reduce	-	Downside is more than 0%.
Neutral	-	Not Applicable

Mid Cap and Small Cap;		
Buy	-	Upside is above 15%.
Accumulate	-	Upside is between 10% - 15%.
Hold	-	Upside is between 0% - 10%.
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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