

May 14, 2018

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Rating	Accumulate
Price	Rs502
Target Price	Rs553
Implied Upside	10.2%
Sensex	35,536
Nifty	10,807

(Prices as on May 11, 2018)

Trading data

Market Cap. (Rs bn)	308.5
Shares o/s (m)	614.5
3M Avg. Daily value (Rs m)	856.1

Major shareholders

Promoters	51.19%
Foreign	29.41%
Domestic Inst.	11.57%
Public & Other	5.71%

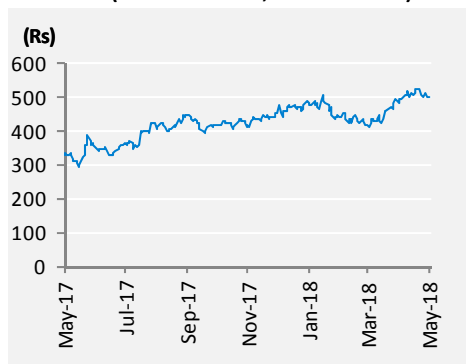
Stock Performance

(%)	1M	6M	12M
Absolute	1.1	21.1	48.6
Relative	(3.6)	14.4	31.2

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2019	24.2	22.6	6.9
2020	30.6	29.2	4.9

Price Perf. (RIC: MMFS.BO, BB: MMFS IN)



Source: Bloomberg

PL hosted the Farm & Motor Vehicle vertical heads of MMFS for investors and based on the feedback received, we continue to be optimistic on commentary of rural economy improvement seen post the headwinds earlier. Key takeaways were (i) Growth has been improving from return in infra activity and cash flow in many troubled pockets as well from penetration in new areas (ii) two years into vertical led business model has turned out to be successful improving reach & with targeted collections ability and (iii) internal programs for customers coupled with reach has helped strong relationships with OEM & dealerships helping retain market shares. We believe, rural recovery should agur well for growth and recovery from NPAs can bring tailwind to earnings helping deliver ROA of 2.6-2.8% by FY20. We retain Accumulate with revised TP of Rs553 based on 3.2x Mar-20 ABV.

- **Vertical based lending model has helped on tight collections:** Moving to separate vertical based lending has not only ensured improvement in business growth but also collections which remains with the vertical for first 12 months of origination and then passed on to collections team. Performance of verticals are assessed on the zero dpd pools passed on to the collections team which has ensured better portfolio and lower defaulting contracts. This has ensured improvement in asset quality by huge gap from traditional working model.
- **Margins/Spreads pressure mitigated from geography & mix:** Yields have been under pressure especially on the cars segment, but pressure on yields have been mitigated by entering into newer geographies especially where MMFS remains sole lender and lending in newer business segments. This has also helped MMFS to price some of the credit risk in recent time in pricing of the products.
- **Relationship across dealerships & OEMs helping retain market share:** Strong parent & its products has helped MMFS grow (40-45% of mix), but despite that due to deeper penetration in rural has bought on board other OEMs for strong partnership with MMFS. MMFS has benefited from strong relationships with dealers (+2500-3000) has helped brush aside competition as dealers' track reachability, stability of players in the business and ability to generate volumes.

Key Financials (Y/e March)	2017	2018	2019E	2020E
Net interest income (Rs m)	31,971	40,682	50,345	59,630
Growth (%)	6.3	27.2	23.8	18.4
Non-interest income (Rs m)	636	590	637	688
Operating Profit (Rs m)	19,292	25,344	32,612	39,174
PAT (Rs m)	4,002	8,269	14,850	18,802
EPS (Rs)	7.1	14.0	24.2	30.6
Growth (%)	(40.5)	97.9	72.4	26.6
Net DPS (Rs)	—	2.2	3.4	5.6

Profitability & valuation	2017	2018	2019E	2020E
Spreads / Margins (%)	8.2	9.1	9.5	9.5
RoAE (%)	6.4	10.5	15.4	17.7
RoAA (%)	1.0	1.8	2.8	3.0
P/E (x)	70.9	35.8	20.8	16.4
P/BV (x)	4.4	3.2	3.1	2.7
P/ABV (x)	5.8	4.0	3.8	3.3
Net dividend yield (%)	—	0.4	0.7	1.1

Source: Company Data; PL Research

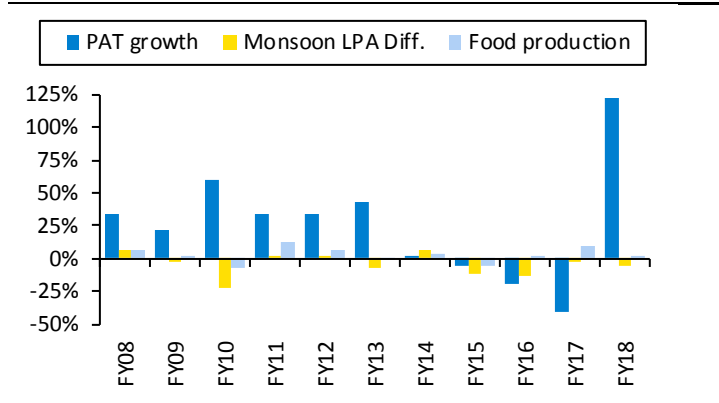
Farm Equipment Segment

- **Growth Outlook & Commentary** – Tractor industry grew by 20% YoY in FY18. MMFS reached to 1.0 million customer base in FY18 achieved after 20 years of getting into the business. Used vehicle has been good area of growth, doing 3,500/month used vehicle financing. MMFS has tied up with +3,000 dealer relationship with a push sale approach by sales people on ground.
- **Tractor segment** - 35% of business has exchange program on tractor, while 65% customers are new to industry. For MMFS, 90% of tractor are M&M (incl. Swaraj & Grow max) of the 44% tractor market share M&M has. Of the total loans, 55% of disbursement is half yearly EMI, 15% disbursement is on monthly EMI and 30% on quarterly EMI.
- **Implements** – Market & MMFS both are moving towards implements especially for haulage customers who can buy trailer but currently targeting only existing customer base. Have seen good traction of tractor mounted harvester in AP/Telangana which has improved cash flow and many cases have seen loan repayment in two years. Subsidy driven sales only in some states like AP where 30-40% of sales on subsidy based and even in Orissa.
- **Geography wise trends** - UP remains strong market with 17-18% of tractor sales UP has seen good crop season with June-July being 45% of volume and October (festive season) being also strong growth time. All other states such as Maharashtra, Rajasthan are doing good barring Karnataka. Maharashtra has seen lower LTV 1st time with improved cash flow especially in the sugar belts where cash flow has improved.
- **Business process under vertical & productivity** - Vertical has helped to use digital and analytics especially at dealer level for TAT. Productivity measured by no of units done than value. Have structured bucket wise collections and rigorous follow up is done and substantial weightage on the business team (originating) for collections by measuring on “Odpd” contracts transferred to collections team. Exclusive team has helped to penetrate better along with knowledge know-how on specialization.
- **Customer centric initiatives** – “Selfie with customer” remains a key engaging initiative which ensures higher time spend at customer close to the customer. MMFS also has been periodically doing melas at local village which helps for both collections & direct marketing.

Light Motor Vehicle

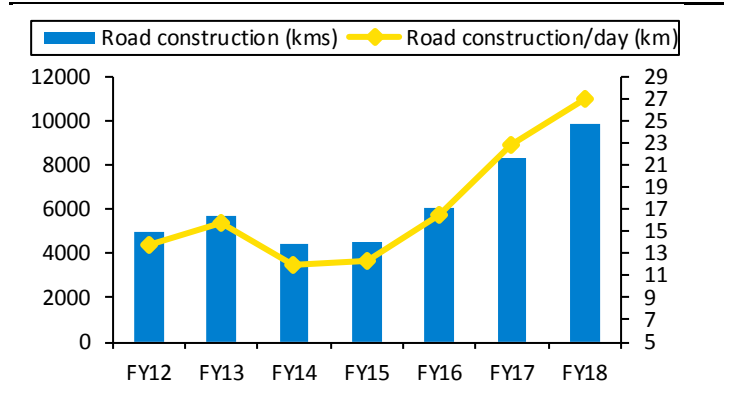
- **Product Segments** - 60% Earn or Pay (CV & Private) and 40% personal with overall yields for the portfolio is 14.5-15%. Demand for school vans has been coming nicely which are mostly tailor made products. MMFS has 25-30% market share in cab aggregators (Ola/Uber/Zoom) cars but all vehicles are driver owned (DCO). Viability in the model has deteriorated mainly on the invest & driver model, and MMFS differentiates lending by only lending to DCO segment. Currently, to improve viability switch has happened from Sedan to hatch back vehicles which helps in similar earning and with less EMI.
- **Market shares** – Getting direct credit from Ola/Uber having incremental avg. yields of 16-16.5% for 4 years. Maruti growth is mainly coming from Nexa division and hence MMFS has set up a separate vertical for Nexa products to improve the small market share it has of 700-1000/month vehicles. MMFS has 35% market share in Maruti of which 8-10% is Nexa's share, while MMFS enjoys 15% market share of Hyundai market.
- **Geography wise** - MP/UP/JK/HP/Bihar/Uttaranchal have been doing well. Maharashtra has started turning out to be good recently, while South India is still under stress especially Kerala and taxi segment is badly hit in Chennai/Bangalore/Hyderabad in metros side.
- Rural market better than Urban. Overall portfolio has seen decent growth in April on track with expectations. New branches should add more to growth.
- **Sourcing** - 15% of business done by MMFS by direct approach which leads to lower opex as saves on commission/brokerage.

Exhibit 1: FY14-FY17 was bad monsoon period impacting rural economy and MMFS performance



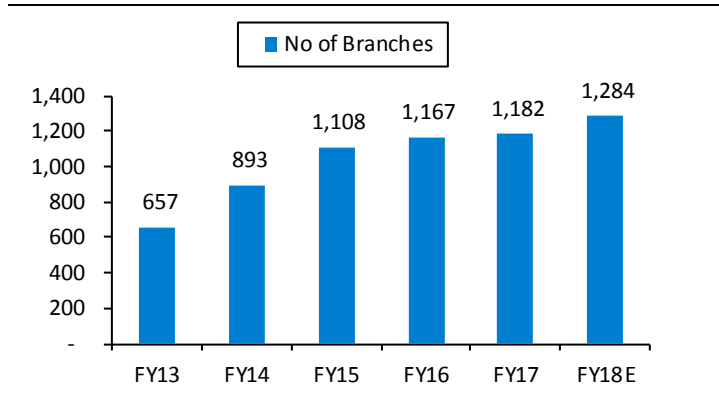
Source: Company Data, PL Research

Exhibit 2: Infra thrust has been much higher in last 2 years helping improve cash flow in rural economy



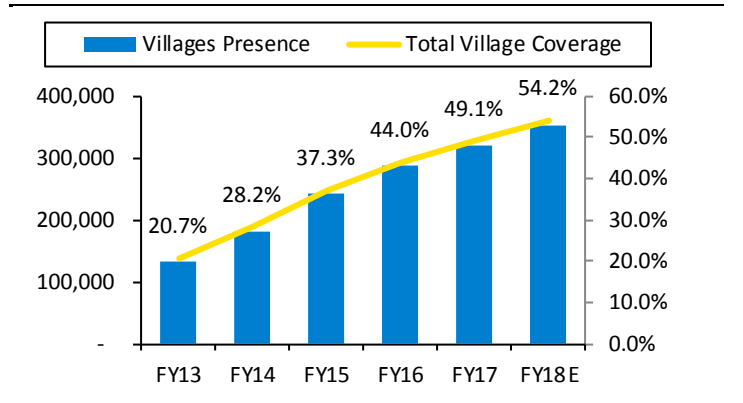
Source: Company Data, PL Research

Exhibit 3: MMFS has been improving its presence across Pan-India states



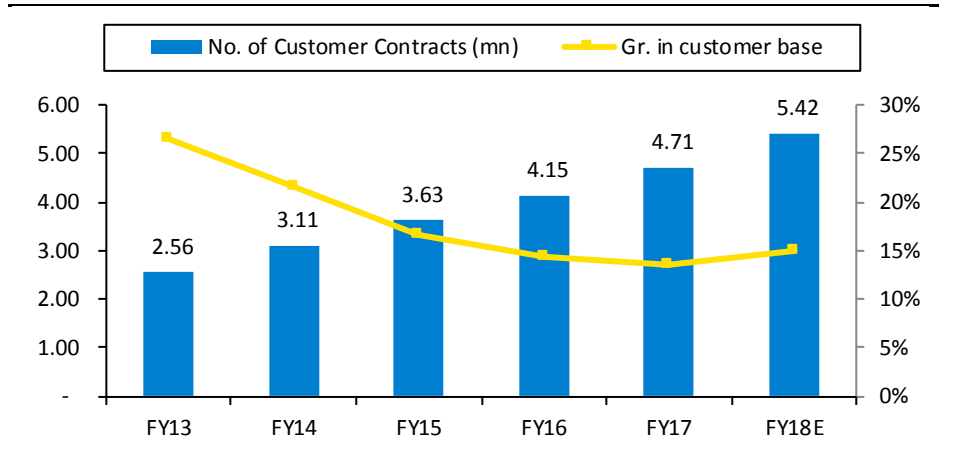
Source: Company Data, PL Research

Exhibit 4: Presence addition has been more deeper into villages improving coverage



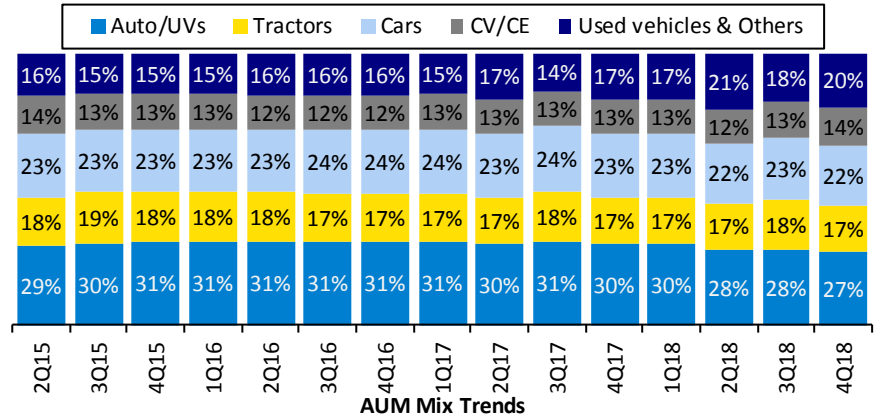
Source: Company Data, PL Research

Exhibit 5: Steady growth seen in customer additions



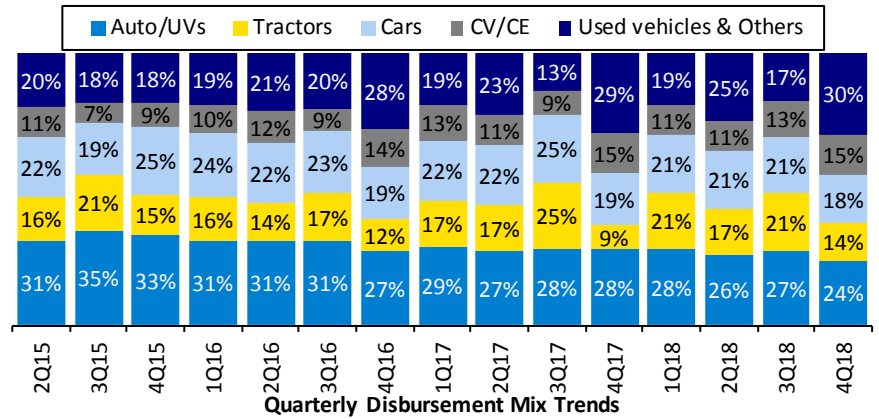
Source: Company Data, PL Research

Exhibit 6: AUM mix - Steady mix across segments with more tilt towards used vehicles



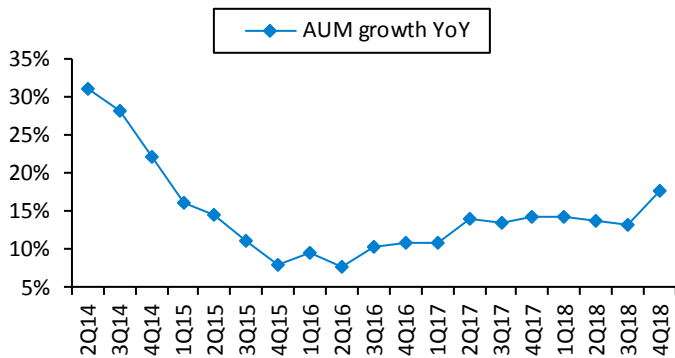
Source: Company Data, PL Research

Exhibit 7: Disbursement mix steady in cars/CV, while improved in used vehicle & tractor



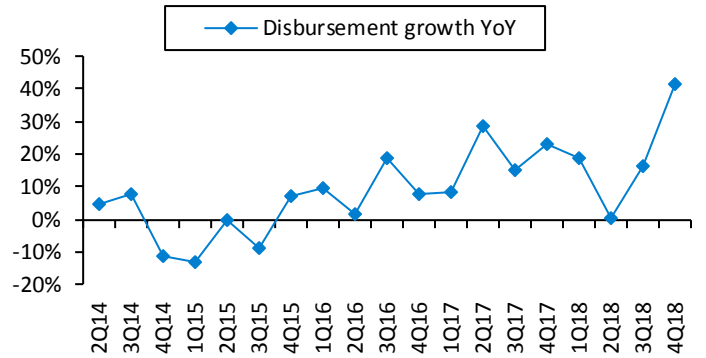
Source: Company Data, PL Research

Exhibit 8: AUM growth has improved after many quarters...

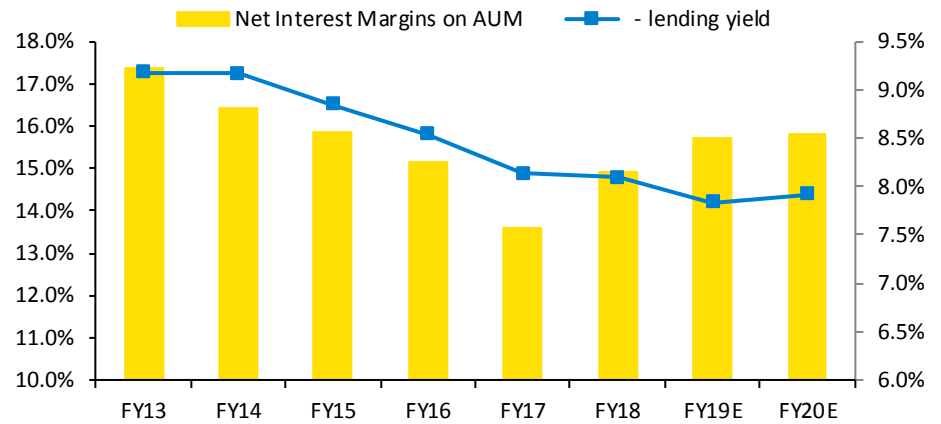


Source: Company Data, PL Research

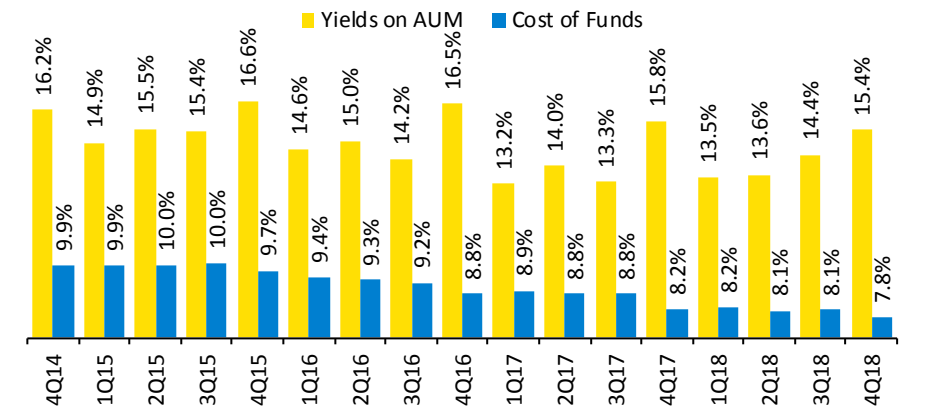
Exhibit 9: ...which was on strong outlook & cash flow improvement



Source: Company Data, PL Research

Exhibit 10: Post down trending, NIMs have seen improvement on growth & asset quality improvement


Source: Company Data, PL Research

Exhibit 11: Cost benefit to slow but yields improvement from growth & mix change


Source: Company Data, PL Research

Exhibit 12: ROA tree – Factoring in 17-18% ROE in FY20

ROE Decomposition	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Net Interest Income/AUM	8.3%	8.1%	7.8%	7.7%	7.3%	8.0%	8.4%	8.4%
Fees/AUM	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%
Net revenues/AUM	9.4%	8.9%	8.7%	8.4%	7.7%	8.3%	8.6%	8.6%
Operating Expense/AUM	3.1%	2.9%	2.8%	3.0%	3.3%	3.3%	3.2%	3.1%
Provisions/AUM	1.2%	1.6%	2.3%	2.7%	3.0%	2.4%	1.7%	1.5%
Taxes/AUM	1.6%	1.5%	1.2%	0.9%	0.5%	0.9%	1.3%	1.4%
ROA	3.5%	2.9%	2.3%	1.7%	0.9%	1.6%	2.5%	2.7%
Equity/AUM	15.3%	15.4%	15.2%	15.1%	14.3%	15.5%	16.1%	15.1%
ROE	23.1%	18.6%	15.5%	11.4%	6.4%	10.5%	15.4%	17.7%

Source: Company Data, PL Research

Exhibit 13: Change in estimates table – We retain our estimates

(Rs mn)	Old		Revised		% Change	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Net interest income	51,073	60,403	51,073	60,403	-	-
Operating profit	32,612	39,174	32,612	39,174	-	-
Net profit	14,850	18,802	14,850	18,802	-	-
EPS (Rs)	24.2	30.6	24.2	30.6	-	-
ABVPS (Rs)	131.8	151.1	131.8	151.1	-	-
Price target (Rs)	553		553		0.0	
Recommendation	ACCUMULATE		ACCUMULATE			

Source: Company Data, PL Research

Exhibit 14: Fair valuation table for subsidiaries

Mahindra Insurance Brokers				
Rs mn		FY20E PAT	P/E	Total Value
Valuation		847	20.0	16,942
Mahindra stake		80.0%		13,554
Initial investment				4,798
Gain in investments				13,549
Per Share Value				22.0
Mahindra Rural housing Finance				
Rs mn		FY20E book	P/B	Total Value
Networth		11,413	3.00	34,238
MMFSL Share		87.5%		29,958
Equity Value (Rs mn)				838
Gain in investments				29,120
Per Share Value				47.4

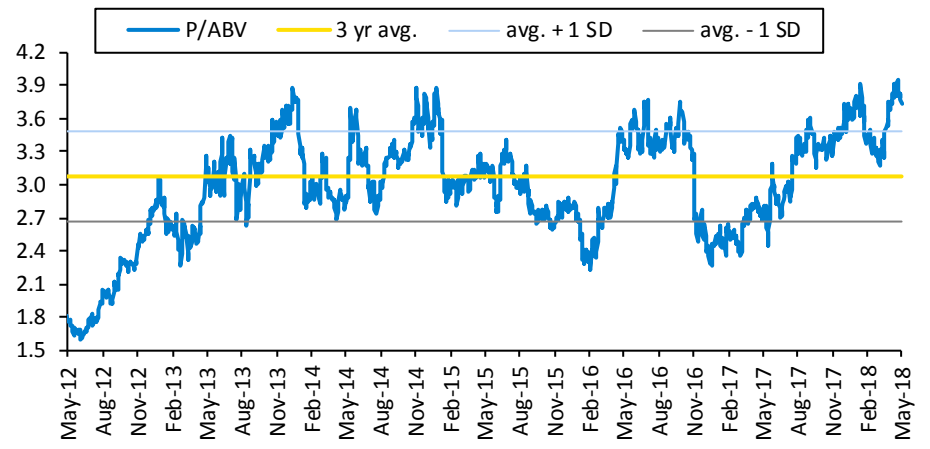
Source: Company Data, PL Research

Exhibit 15: We maintain ACCUMULATE with TP of Rs530 based on 3.2x P/ABV Mar-20

Fair price – EVA	495
Fair price - P/ABV	472
Average of the two	484
Subsidiary Value	69
Target Price	553
Target P/ABV	3.2
Target P/E	15.8
Current price, Rs	502
Upside (%)	10%
Dividend yield (%)	1%
Total return (%)	11%

Source: Company Data, PL Research

Exhibit 16: MMFS: One year forward P/ABV trend



Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2017	2018	2019E	2020E
Int. Inc. / Opt. Inc.	60,545	70,686	86,933	103,898
Interest Expenses	28,574	30,004	36,588	44,268
Net interest income	31,971	40,682	50,345	59,630
<i>Growth (%)</i>	6.3	27.2	23.8	18.4
Non interest income	636	590	637	688
<i>Growth (%)</i>	22.5	(7.3)	8.0	8.0
Net operating income	33,801	42,057	51,710	61,091
Expenditure				
Employees	6,809	8,517	9,795	11,264
Other expenses	7,240	7,754	8,840	10,165
Depreciation	460	442	464	487
Total expenditure	14,509	16,713	19,098	21,917
PPP	19,292	25,344	32,612	39,174
<i>Growth (%)</i>	(7.6)	31.4	28.7	20.1
Provision	13,091	12,266	9,941	10,468
Other income	—	—	—	—
Exchange Gain / (Loss)	—	—	—	—
Profit before tax	6,201	13,078	22,671	28,706
Tax	2,198	4,809	7,822	9,903
<i>Effective tax rate (%)</i>	35.5	36.8	34.5	34.5
PAT	4,002	8,269	14,850	18,802
<i>Growth (%)</i>	(40.5)	106.6	79.6	26.6

Balance Sheet (Rs m)

Y/e March	2017	2018	2019E	2020E
Sources of funds				
Equity	1,130	1,229	1,229	1,229
Reserves & Surplus	63,642	91,802	99,092	111,423
Networth	64,772	93,031	100,321	112,652
<i>Growth (%)</i>	6.4	43.6	7.8	12.3
Loan funds	346,016	394,035	476,217	570,470
<i>Growth (%)</i>	—	—	—	—
Others	—	—	—	—
Minority Interest	—	—	—	—
Deferred Tax Liability	—	—	—	—
Total	410,788	487,066	576,538	683,122
Application of funds				
Net fixed assets	1,120	1,197	1,221	1,245
Advances	425,234	510,043	601,542	709,712
<i>Growth (%)</i>	16.0	19.9	17.9	18.0
Net current assets	(42,899)	(51,413)	(55,831)	(60,066)
Investments	18,895	18,732	20,605	22,665
<i>Growth (%)</i>	27.4	(0.9)	10.0	10.0
Other Assets	8,440	8,508	9,001	9,567
Total	410,789	487,066	576,538	683,122

Source: Company Data, PL Research.

Quarterly Financials (Rs m)

Y/e March	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Int. Inc. / Operating Inc.	15,924	16,608	18,340	20,600
Income from securitization	—	—	—	—
Interest Expenses	7,327	7,498	7,629	7,550
Net Interest Income	8,597	9,110	10,711	13,050
<i>Growth</i>	28.4	23.5	39.8	26.5
Non interest income	107	221	124	138
Net operating income	8,704	9,331	10,835	13,188
<i>Growth</i>	27.1	15.6	42.7	16.8
Operating expenditure	3,810	3,694	4,282	4,927
PPP	4,894	5,636	6,553	8,261
<i>Growth</i>	36.5	25.1	66.0	13.9
Provision	4,258	4,446	1,989	1,572
Exchange Gain / (Loss)	—	—	—	—
Profit before tax	636	1,190	4,563	6,688
Tax	162	410	1,793	2,443
Prov. for deferred tax liability	—	—	—	—
<i>Effective tax rate (%)</i>	25.5	34.5	39.3	36.5
PAT	474	780	2,770	4,245
<i>Growth</i>	(45.5)	(17.7)	(1868.9)	81.4

Key Ratios

Y/e March	2017	2018	2019E	2020E
CMP (Rs)	502	502	502	502
Eq. Shrs. O/s. (m)	565	615	615	615
Market Cap (Rs m)	283,679	308,510	308,510	308,510
Market Cap to AUM (%)	69.1	63.3	53.5	45.2
EPS (Rs)	7.1	14.0	24.2	30.6
Book Value (Rs)	114.7	157.7	163.3	183.3
Adjusted Book Value (Rs)	86.4	125.7	131.8	151.1
P/E (x)	70.9	35.8	20.8	16.4
P/BV (x)	4.4	3.2	3.1	2.7
P/ABV (x)	5.8	4.0	3.8	3.3
DPS (Rs)	—	2.2	3.4	5.6
Dividend Yield (%)	—	0.4	0.7	1.1

Asset Quality

Y/e March	2017	2018	2019E	2020E
Gross NPAs (Rs m)	41,827	46,987	48,279	49,507
Net NPAs (Rs m)	15,997	19,706	19,312	19,803
Gross NPAs to Gross Adv. (%)	9.8	9.2	8.0	7.0
Net NPAs to Net Adv. (%)	3.7	3.8	3.2	2.8
NPA Coverage (%)	61.8	58.1	60.0	60.0

Profitability (%)

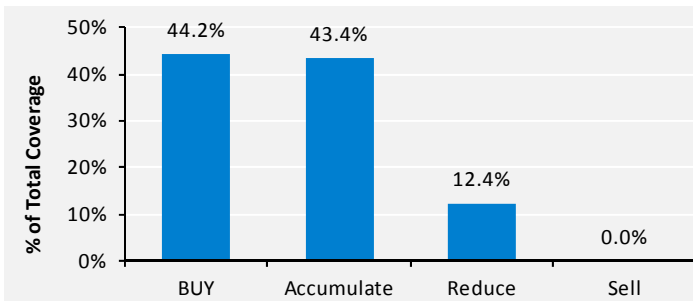
Y/e March	2017	2018	2019E	2020E
NIM	8.2	9.1	9.5	9.5
RoAA	1.0	1.8	2.8	3.0
RoAE	6.4	10.5	15.4	17.7

Source: Company Data, PL Research.

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