

Manappuram Finance

9 February 2018

Reuters: MNFL.BO; Bloomberg: MGFL IN

The Glitter Is Back In Gold Loans

Manappuram Finance (MFL) reported its 3QFY18 results with the key strategic pointers being: (1) Material reversion to growth for gold loan book at 5.3% QoQ. (2) Security expenses would revert to prior levels on technology initiatives (please see conference-call highlights). Per se, on the results front, MFL posted NII growth of 5.5% QoQ to Rs6,153mn, PPOP growth of 6.2% QoQ to Rs3,057mn and PAT growth of 8.2% to Rs1734mn. We have marginally modified our legacy estimates for FY18/FY19 and retained Buy rating on MFL, increasing our target price to Rs136 (from Rs132 earlier), valuing the stock at 2.2x FY20E P/BV.

Reversion to growth for gold loan book dispels doubts about core business: Gold loan book growing 5.3% QoQ shows that lending against gold is a truly bottom-of-pyramid business that is now recovering from the cash-cycle disruption that had arisen because of a variety of factors (demonetisation, drought-like condition in parts of South India). Non-gold loan businesses continued their strong performance with MFI and CV growing 7.5% and 19% QoQ, respectively. CV loans seem to be benefiting from operating leverage as they are disbursed entirely from gold loans branches. Housing loans grew 4.8% with continued but transient impact of management change. Overall AUM growth was 6.8% QoQ.

Microfinance subsidiary is back in the black with significantly lower provisioning expected going forward: Asirvad Microfinance posted a profit in 3QFY18, for the first time since 3QFY17. Rs310mn provision for Asirvad Microfinance is Rs260mn in excess of the RBI requirement and marks the last somewhat chunky bout of provisioning. Akin to leading industry peers, collection efficiency of 'new book' created since 1 January 2017 is a pristine 99.04%, indicating stress is contained within the legacy book. Similarly, PAR0 has diminished by ~Rs110mn-Rs120mn sequentially, indicating stress of legacy book itself is not rising but rather diminishing.

Nimble management plans to address higher security expenses with technology: Expenses related to security have spiked to a quarterly run-rate of ~Rs450mn, but the management is confident that these expenses could revert to the earlier level of ~Rs250mn per quarter on the back of technology initiatives. The management also sounded confident about maintaining spread with sticky yield (borrower profile largely insensitive to interest rates) and with flat-to-lower cost of borrowings (NCDs to still re-price lower from higher legacy levels).

Valuation and outlook: We have revised our legacy NII estimates by -0.3%/-3.3% for FY18/FY19, our PPOP estimates by 3.2%/2.3% and our PAT estimates by 0.4%/2.8%, respectively. We have rolled forward our valuation of MFL based on FY20E financials, valuing the stock at 2.2x FY20E P/BV and increasing our target price to Rs136 (from Rs132 earlier).

BUY

Sector: NBFC

CMP: Rs109

Target Price: Rs136

Upside: 25%

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Key Data

Current Shares O/S (mn)	842.0
Mkt Cap (Rsbn/US\$bn)	91.4/1.4
52 Wk H / L (Rs)	126/82
Daily Vol. (3M NSE Avg.)	8,122,476

Price Performance (%)

	1 M	6 M	1 Yr
Manappuram Finance	(10.9)	10.0	10.6
Nifty Index	(0.6)	6.8	20.5

Source: Bloomberg

Y/E March (Rsmn)	3QFY18	3QFY17	2QFY18	YoY (%)	QoQ (%)
Interest income	8,728	8,977	8,291	(2.8)	5.3
Interest expenses	2,575	3,174	2,458	(18.9)	4.8
Net interest income	6,153	5,803	5,833	6.0	5.5
NIM (%)	17.4	16.0	17.2	135bps	21bps
Fee & other income	83	75	103	10.9	(19.3)
Operating income	6,237	5,878	5,936	6.1	5.1
Staff costs	1,594	1,252	1,549	27.3	2.9
Other operating expenses	1,586	1,133	1,510	39.9	5.0
Total operating expenses	3,180	2,385	3,059	33.3	4.0
Cost-to-income (%)	51.0	40.6	51.5	1,041bps	(54bps)
Cost-to-AUM (%)	9.2	6.4	9.3	280bps	(10bps)
Operating profit	3,057	3,493	2,877	(12.5)	6.2
Provisions	402	352	460	14.1	(12.7)
Credit costs (%)	1.1	1.0	1.4	16bps	(22bps)
PBT	2,655	3,141	2,417	(15.5)	9.8
Tax	921	1,116	815	(17.4)	13.0
-Effective tax rate	34.7	35.5	33.7	(83bps)	98bps
PAT	1,734	2,025	1,602	(14.4)	8.2
EPS (Rs)	2.1	2.4	1.9	(14.9)	8.8
BV (Rs)	43.9	38.2	42.5	15.2	3.5
AUM (Rsmn)	146,502	145,544	137,232	0.7	6.8

Source: Company, Nirmal Bang Institutional Equities Research

Please refer to the disclaimer towards the end of the document.

Key conference-call highlights

- Average **loan-to-value ratio** for gold loan business stood at 67%.
- Share of **online gold loans** moved up to 25.1% of total gold loans.
- For Asirvad Microfinance, **disbursements** are now 100% into bank accounts of borrowers.
- Consolidated **headcount** stood at 24,761 employees.
- Management stated that the long-term growth CAGR expectation for gold loans is ~10%-15%. Furthermore, management stated that this could have been higher but for competition from other products such as micro SME and fintech.
- The “**investment proposals**” placed before the board of directors were not taken up for implementation, but have also not been rejected outright for future reconsideration. These would be “outward” proposals and not any proposal of MFL being acquired.
- While branch count has not increased significantly, the process of shutting down **unprofitable branches** and opening of branches in areas of high potential is an ongoing process.
- Asirvad Microfinance has **intrinsic capacity** to take the customer count to 2mn without meaningfully augmenting branch count. The company is also the third-lowest in terms of interest rate offered to borrowers.
- Loan **ticket sizes** of housing and CV loan businesses are ~Rs1.1mn and ~Rs0.6mn, respectively. For two-wheelers, where the loan book stands at ~Rs0.3bn, the average ticket size is ~Rs 35,000.
- Asirvad Microfinance may register 25%-28% **AUM growth** in FY19.
- **Capital infusion** in Asirvad Microfinance may be Rs1bn-Rs2bn over the next two years.
- **Borrowing mix** for Asirvad Microfinance is 30% NCD, 30% bank loans and 11% NBFCs.
- **CV loans** are mostly for financing heavy commercial vehicles.
- The 100% **insurance broking subsidiary** is being used for cross-selling insurance, primarily general and health insurance.
- ~50% of two-wheeler loan customers, ~20% of CV loan customers and ~10% of housing loan customers are **existing gold loan customers**. However, these are not “cross-sell” customers as these are clients who have approached MFL largely on their own. The management plans to now start cross-selling in a meaningful way.
- **Interest income reversal** for the quarter was ~Rs130mn.
- **GNPA ratio** in the housing business was ~3%.
- Break-up of **other expenses**: Rs450mn for security, Rs290mn for rent and Rs110mn for advertising are among the major components.
- **Other loans** (amounting to Rs3,695mn) are primarily to other NBFCs (~Rs3.3bn). Yield in the NBFC business was ~14%.
- **Employee expenses** have also gone up because of higher minimum wage, new verticals being formed and increments.
- 15%-20% of delinquent microfinance loans may be **recovered**.
- Of the **home loan book**, ~80% is to self-employed borrowers and ~20% to salaried borrowers and this mix will largely stay the same going forward.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Net interest income	14,016	22,075	24,266	27,920	33,282
Pre-provision profit	5,907	12,749	12,902	14,100	16,239
PAT	3,552	7,584	7,111	8,326	9,558
EPS (Rs)	4.2	9.0	8.4	9.9	11.4
BV (Rs)	32.8	39.9	46.2	53.4	61.9
P/E (x)	25.7	12.1	12.9	11.0	9.6
P/BV (x)	3.3	2.7	2.4	2.0	1.8
Gross NPAs (%)	0.9	2.3	2.5	2.8	2.9
Net NPAs (%)	0.7	1.6	1.5	1.6	1.6
RoA (%)	2.9	5.4	4.3	4.1	3.8
RoE (%)	13.2	24.8	19.6	19.8	19.7

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Actual performance versus our estimates

(Rsmn)	3QFY18	3QFY17	2QFY18	YoY (%)	QoQ (%)	3QFY18E	Devi. (%)
Net interest income	6,153	5,803	5,833	6	5	5,803	6
Pre-provision profit	3,057	3,493	2,877	(12)	6	3,493	(12)
PAT	1,734	2,025	1,602	(14)	8	2,025	(14)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

	Revised estimate		Earlier estimate		% Revision	
	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Net interest income (Rsmn)	24,266	27,920	24,349	28,859	(0.3)	(3.3)
Net interest margin (%)	16.1	15.3	15.9	15.3	25bps	-
Operating profit (Rsmn)	12,902	14,100	12,500	13,778	3.2	2.3
Profit after tax (Rsmn)	7,111	8,326	7,082	8,095	0.4	2.8
EPS (Rs)	8.4	9.9	8.4	9.6	0.4	2.8
ABV (Rs)	43.3	49.6	43.2	49.2	0.3	0.8

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Interest income	23,490	33,762	35,481	41,656	50,176
Interest expenses	9,474	11,687	11,216	13,736	16,894
Net interest income	14,016	22,075	24,266	27,920	33,282
Non-interest income	249	326	570	508	619
Net revenues	14,265	22,401	24,836	28,428	33,901
Operating expenses	8,358	9,652	11,934	14,328	17,662
-Employee expenses	4,327	5,026	6,151	7,678	10,014
-Other expenses	4,031	4,626	5,783	6,650	7,647
Operating profit	5,907	12,749	12,902	14,100	16,239
Provisions	423	1,093	1,963	1,291	1,535
PBT	5,484	11,656	10,939	12,809	14,704
Tax	1,932	4,072	3,829	4,483	5,146
PAT	3,552	7,584	7,111	8,326	9,558

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Share capital	1,682	1,684	1,684	1,684	1,684
Reserves & surplus	25,898	31,934	37,220	43,301	50,417
Net worth	27,580	33,618	38,904	44,985	52,101
Borrowings	96,379	1,09,861	1,32,639	1,67,595	2,05,751
Other liability & provisions	4,432	8,042	9,667	12,507	16,269
Total liabilities	1,28,391	1,51,521	1,81,450	2,25,343	2,74,388
Fixed assets	1,948	1,869	2,149	2,472	2,843
Investments	490	50	50	50	50
Loans	1,13,853	1,38,417	1,62,978	2,03,022	2,47,761
Cash	6,045	5,227	8,149	10,151	12,388
Other assets	6,055	5,958	8,123	9,648	11,346
Total assets	1,28,391	1,51,521	1,81,450	2,25,343	2,74,388

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Key ratios

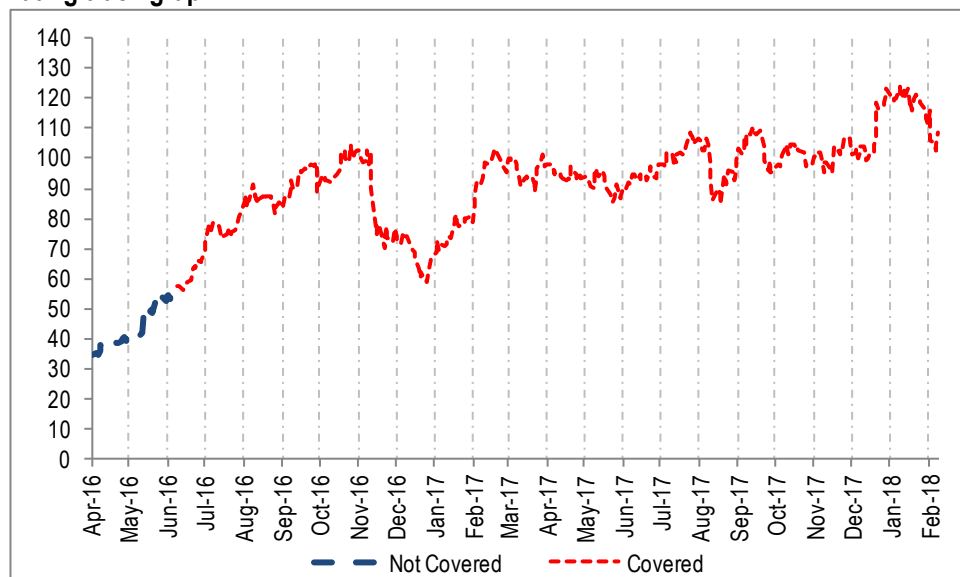
Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Growth (%)					
Net interest income	28.5	57.5	9.9	15.1	19.2
Operating profit	33.7	115.8	1.2	9.3	15.2
Profit after tax	30.8	113.5	-6.2	17.1	14.8
Business (%)					
Advances growth	18.3	21.6	17.7	24.6	22.0
Spread (%)					
Yield on loans	22.4	26.8	23.5	22.8	22.3
Cost of borrowings	10.4	11.3	9.3	9.2	9.1
Spread	12.0	15.4	14.3	13.6	13.2
NIM	13.3	17.5	16.1	15.3	14.8
Operational efficiency (%)					
Cost to income	58.6	43.1	48.1	50.4	52.1
Cost to assets	8.0	7.7	7.9	7.8	7.8
Productivity (Rsmn)					
AUM per branch	31.1	33.8	38.8	42.2	45.4
AUM per employee	6.1	6.3	6.8	7.8	8.4
Employee per branch	5.1	5.4	5.7	5.4	5.4
CRAR (%)					
Tier I	23.5	25.7	24.2	22.5	21.3
Tier II	0.5	0.4	0.6	0.6	0.6
Total	24.0	26.1	24.8	23.1	21.9
Asset quality (%)					
Gross NPAs	0.9	2.3	2.5	2.8	2.9
Net NPAs	0.7	1.6	1.5	1.6	1.6
Provision coverage	22.7	29.7	41.2	42.9	44.3
Credit costs (excluding std. assets)	0.2	0.9	1.1	0.6	0.6
Credit costs (including std. assets)	0.4	0.9	1.3	0.7	0.7
Return ratios (%)					
RoE	13.2	24.8	19.6	19.8	19.7
RoA	2.9	5.4	4.3	4.1	3.8
Per share (%)					
EPS	4.2	9.0	8.4	9.9	11.4
BV	32.8	39.9	46.2	53.4	61.9
ABV	31.9	37.3	43.3	49.6	57.0
Valuation (x)					
P/E	25.7	12.1	12.9	11.0	9.6
P/BV	3.3	2.7	2.4	2.0	1.8
P/ABV	3.4	2.9	2.5	2.2	1.9

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
9 June 2016	Buy	58	85
10 August 2016	Buy	87	130
11 November 2016	Buy	100	145
9 February 2017	Buy	93	140
14 February 2017	Buy	98	140
26 May 2017	Buy	89	120
11 August 2017	Buy	95	120
8 November 2017	Buy	99	132
9 February 2018	Buy	109	136

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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