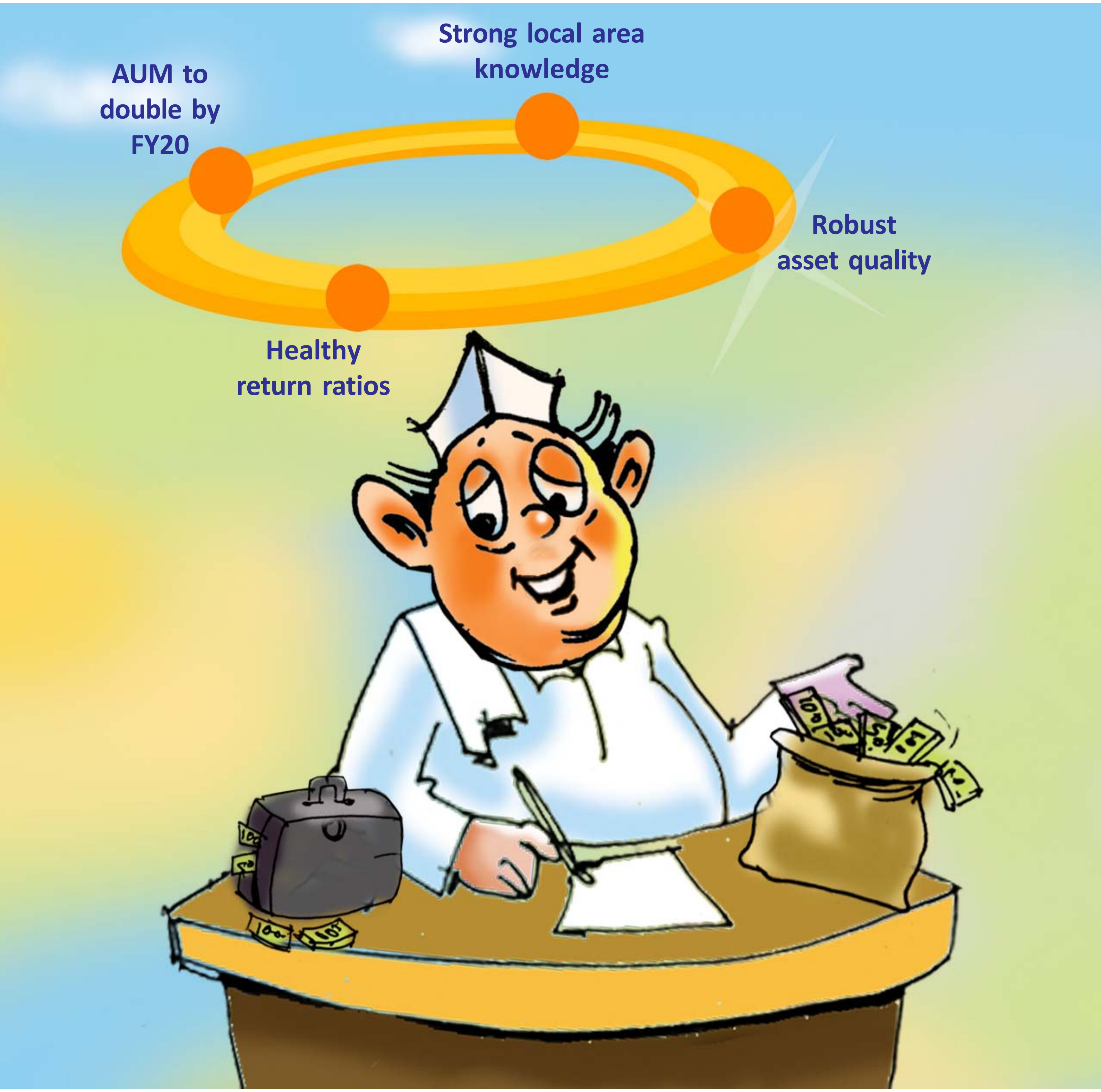
Initiating Coverage | 11 January 2018
Sector: Financials

MAS Financial Services



Grassroots financier

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MAS Financial

BSE Sensex	S&P CNX
34,503	10,651

CMP: INR626 TP: INR740 (+18%) Buy

Grassroots financier

An efficient player in high growth product segment

MAS Financial Services (MASFIN) is an Ahmedabad-headquartered, non-deposit-taking NBFC incorporated in 1995 by first-generation entrepreneurs, Mr. Kamlesh Gandhi and Mr. Mukesh Gandhi. It operates out of six states, of which Gujarat and Maharashtra account for bulk of the AUM. A quintessential NBFC, it targets the middle and low income customer segments. Over the past five years, MASFIN's AUM grew at a robust 35% CAGR to reach INR37b in 1HFY18. Growth was driven by their flagship product (MEL loans) and new product such as SME loans. MEL and SME accounts for 83%+ of the total AUM vs 64% in FY13. The company has impeccable track record of 39% PAT CAGR over FY12-17 with consistent ROA (on AUM) of 2%+. Given a favorable backdrop, we expect the company to deliver 25% AUM over FY17-20, resulting in 25% EPS CAGR over the same time period.

Present in high growth segments, with differentiated offering

MASFIN is present in high-growth segments like Micro-lending (57% of AUM), MSME Lending (25%), Vehicle Finance (13%) and Housing Finance (5%). It has a unique business model, with over 55% of AUM coming from on-lending to other NBFCs and sourcing agents across focused product categories. AUM generated by NBFCs is hypothecated to MASFIN. 35-40% of AUM is assigned to banks (for PSL). The existing network offers immense growth opportunities and we expect the company to focus on local area expertise rather than expanding aggressively. MASFIN should deliver 25% AUM CAGR over FY17-20.

Strong risk management leading to superior asset quality

The company has consistently delivered GNPA ratio of 0.8-1.2%, despite change in norms on NPA migration and macroeconomic factors outside management control. Being a grassroots financier with strong local area knowledge, a unique business model of on-lending to other financiers and hypothecation of portfolio, and strong credit control, MASFIN maintains strong control over asset quality. Credit cost (including standard asset provision) for the company stands at ~1% - this is among the lowest in our NBFC coverage.

RoA to improve; PAT CAGR of 35%+

Margin improvement, operating efficiency and controlled credit cost should drive ROA improvement of 60bp+ and the company is expected to report 18%+ ROE on a consistent basis. The recent capital raise would be sufficient for next three years of growth, in our view. We believe MASFIN has all the ingredients of a good investment: (a) a small base and presence in well-developed states for strong growth, (b) superior asset quality, (c) relentless management focus on generating sustainable, high return ratios, (d) healthy capitalization, and (e) consistent dividend payout. We initiate coverage with a **Buy** rating and a target price of INR740 (25x FY20 EPS, Implied 4.3x FY20 BV).

Stock Info

Bloomberg	MASFIN IN
Equity Shares (m)	55
52-Week Range (INR)	701/564
1, 6, 12 Rel. Per (%)	-5/-/-
M.Cap. (INR b)	34.2
M.Cap. (USD b)	0.5
Avg Val, INRm	397
Free float (%)	26.8

Financial snapshot (INRb)

Y/E MARCH	FY18E	FY19E	FY20E
NII	2,485	3,162	3,948
PPP	1,940	2,452	3,027
PAT	1,002	1,315	1,619
EPS (INR)	18.3	24.1	29.6
BV/Share (INR)	132.6	150.7	172.9
RoA on AUM, %	2.7	2.8	2.7
RoE (%)	19.8	17.0	18.3
Valuations			
P/E (x)	34.1	26.0	21.1
P/BV (x)	4.7	4.2	3.6

Shareholding pattern (%)

As On	Sep-17
Promoter	73.2
DII	13.7
FII	2.6
Others	10.5

FII Includes depository receipts

MAS Financial Services

Grassroots financier

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Exhibit 1: Dupont Analysis (on avg. AUM) : ROAs to improve 60bp+ over FY17-20 led by margin expansion

MAS Financial Services	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Net Interest Income	**8.03**	**7.16**	**5.88**	**5.65**	**5.71**	**6.60**	**6.69**	**6.68**
Fee Income	1.53	1.17	1.15	1.05	0.91	0.83	0.76	0.70
Net Income	**9.57**	**8.33**	**7.04**	**6.71**	**6.61**	**7.43**	**7.46**	**7.39**
Non interest Income	0.29	0.13	0.08	0.04	0.03	0.03	0.03	0.03
Net Income	**9.86**	**8.46**	**7.11**	**6.75**	**6.65**	**7.46**	**7.49**	**7.42**
Operating Expenses	**4.31**	**3.33**	**2.55**	**2.49**	**2.23**	**2.31**	**2.30**	**2.30**
Operating Profits	**5.55**	**5.12**	**4.57**	**4.25**	**4.42**	**5.15**	**5.19**	**5.12**
Provisions/write offs	0.96	1.16	1.10	0.98	0.90	1.05	0.90	0.90
PBT	**4.59**	**3.96**	**3.47**	**3.27**	**3.52**	**4.10**	**4.29**	**4.22**
Tax	1.48	1.32	1.17	1.13	1.22	1.41	1.48	1.46
PAT	**3.11**	**2.64**	**2.29**	**2.14**	**2.30**	**2.69**	**2.81**	**2.77**
Less: Preference shares and MI	0.56	0.30	0.24	0.17	0.16	0.03	0.03	0.03
PAT for Equity shareholders	**2.55**	**2.34**	**2.05**	**1.97**	**2.14**	**2.66**	**2.78**	**2.74**
*Leverage (x)**	*16.65*	*17.08*	*17.69*	*18.74*	*14.22*	*7.46*	*6.10*	*6.68*
RoE	**42.48**	**39.91**	**36.32**	**36.92**	**30.47**	**19.85**	**16.99**	**18.31**

Source: MOSL, Company; *: On-book leverage for FY17 is 7.7x

Exhibit 2: Valuation comparison

	AUM (INR b)	Price	Market Cap (INR b)	AUM CAGR (FY17-20E)%	EPS CAGR (FY17-20E)%	Net NPL (1HFY18, %)	RoA (%)		RoE (%)		P/B		P/E	
							FY18E	FY19E	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
SHTF	855	1,497	339	16	32	2.45	2.7	3.1	15.1	17.4	2.6	2.3	18.1	13.7
LTFH	723	182	331	17	35	3.31	1.7	2.2	15.8	19.6	3.3	2.8	23.0	15.6
BAF	721	1,781	1,030	35	40	0.51	3.5	3.6	20.2	20.4	6.0	5.1	37.7	27.0
MMFS	499	482	286	17	51	6.50	1.8	2.1	10.7	12.2	3.1	2.9	34.2	24.7
CIFC	365	1, 306	205	18	23	2.89	3.0	3.0	19.6	19.2	3.9	3.3	21.9	18.8
SCUF	249	2,140	142	16	27	1.83	3.3	3.6	14.3	15.9	2.5	2.2	18.2	14.5
CAFL	230	836	83	25	32	1.00	1.7	1.8	13.2	15.4	2.6	2.3	21.3	15.9
MUTH	276	451	181	10	19	3.99	5.5	5.0	23.8	19.9	2.3	2.0	10.8	10.9
MASFIN	37	626	34	25	25	0.96	2.7	2.8	19.8	17.0	4.9	4.3	35.5	27.0

Source: Company, MOSL

A grassroots financier

Unique business model

- **MASFIN was incorporated in 1995 by two first-generation entrepreneurs, Mr. Kamlesh Gandhi and Mr. Mukesh Gandhi. A quintessential NBFC, MASFIN targets the middle and low income customer segments with products ranging from MSME loans, SME loans, 2W loans, CV loans and home loans. Around 55% of the loan book is on-lending, i.e. lending to other NBFCs which are in similar product segments as MASFIN.**
- **The company registered 36% AUM CAGR over FY12-17, driven by 35% CAGR in micro-enterprise loans as well as introduction of new products such as SME & housing finance.**
- **With focus on the self-employed segment, NBFC partnerships for sourcing and robust underwriting methodology, MASFIN is poised to deliver 25% AUM CAGR over FY17-20E. The strong growth will be driven from existing geographies (capitalizing on local area knowledge), higher share of direct lending, and continued growth in on-lending book and new product additions.**

Over two decades of lending experience

MASFIN is an Ahmedabad-headquartered, non-deposit taking NBFC with more than two decades of business operations in financial services spread across seven states. The company is focused on catering to the needs of the lower and middle-income customer segments via a suite of products including MSME/SME lending, 2W loans, CV loans and home loans. The company has a total AUM of INR37b currently, with over 50% of the AUM in micro-enterprise lending.

Exhibit 3: Key milestones

Source: MOSL, Company

Run by first-generation entrepreneurs

Mr. Kamlesh Gandhi – Chairman and Managing Director

- Founded the company is 1995
- Over 21 years of experience in the financial services sector
- First-generation entrepreneur

Mr. Mukesh Gandhi - Chief Financial Officer

- Co-founded the company in 1995
- Designated Director (Finance) and CFO since 2015
- Bachelor's and Master's degree in commerce from Gujarat University with over two decades of work experience
- Also, Chairman of Gujarat Finance Company Association and Director of Finance Industry Development Council

Ms Darshana Pandya – Chief Operating Officer

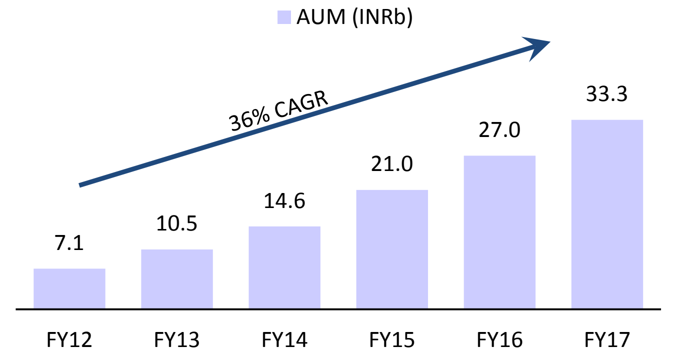
- Joined MASFIN in 1996 and has over two decades of work experience
- Promoted to Executive Director since 2016
- Bachelor's degree in commerce from Gujarat University

AUM grew at a CAGR of 36% over FY12-17 to INR33b

Capitalizing on local area expertise – focus on profitable growth

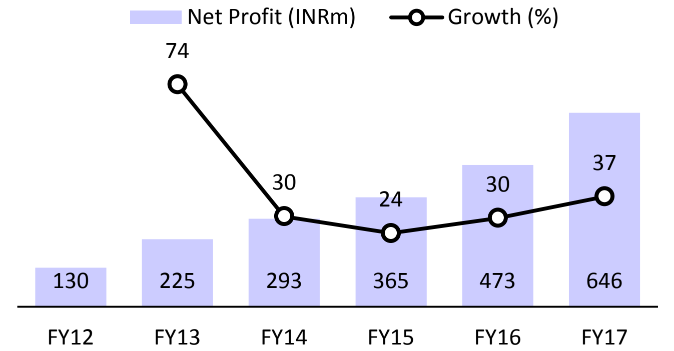
MASFIN operates across six states (74 NBFC branches and 55 housing finance branches) and the NCT of Delhi, and has a presence in 3,200+ locations. Bulk of its AUM comes from Gujarat and Maharashtra. The company focuses on judicious use of capital and develops local area expertise before becoming aggressive in any state. While it has a presence in Tamil Nadu, Karnataka and Rajasthan, the contribution of these states to its overall AUM is less than 20% – MASFIN is trying to build expertise in understanding the credit culture/customer behavior in these states. Existing states would be the key growth driver in the ensuing years. We do not expect MASFIN to expand aggressively in new states.

Exhibit 4: 36% AUM CAGR over FY12-17



Source: MOSL, Company

Exhibit 5: 38% PAT CAGR over FY12-17

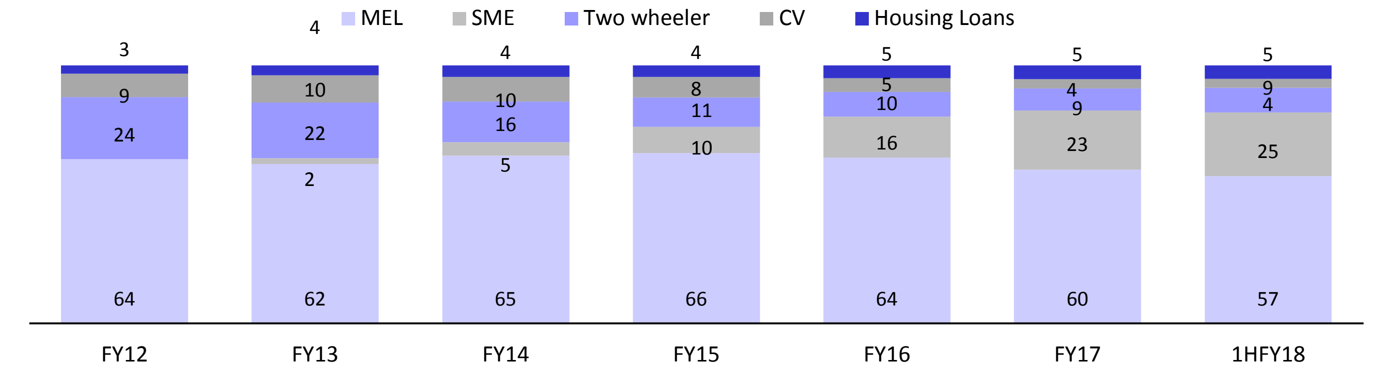


Source: MOSL, Company

MASFIN focuses on serving the underserved credit needs of mid and low income group segments

MASFIN's business and financing products are primarily focused on high-yielding and low-penetration middle and low income customer segments, and include five principal categories: (i) micro-enterprise loans, (ii) SME loans, (iii) two-wheeler loans, (iv) commercial vehicle loans (which include new and used commercial vehicle loans, used car loans, and tractor loans), and (v) housing loans. The share of SME loans in overall AUM has increased from 2% in FY13 to 25% currently, whereas the share of 2W+CV loans has declined from 32% to 13% during the same period. This was a conscious decision by management due to adverse macroeconomic factors.

Exhibit 6: SME portfolio gaining share (%)



Source: MOSL, Company

Perfect blend of sourcing

MASFIN's AUM grew at a CAGR of 36% over FY12-17 from INR7.1b to INR33.3b. As at September 2017, its AUM was at INR36.6b. It has over 500,000 active loan accounts. Around 55% of AUM is sourced through on-lending to other NBFCs (100+ relationships). Further, MASFIN has 300+ sourcing agent relationships for sourcing car and 2W loans. It also has 675+ feet-on-street sales agents, who not only help in scouting AUM for direct lending but also for on-lending relationships.

Exhibit 7: Sourcing through various channels

What?	Description
Number of branches	74
Number of sales feet on street (FOS)	683
Number of CV loan sourcing intermediaries	316
Number of 2W loan sourcing intermediaries	328
Number of NBFC partnerships	105
Underlying %age of AUM sourced by partnerships	56%

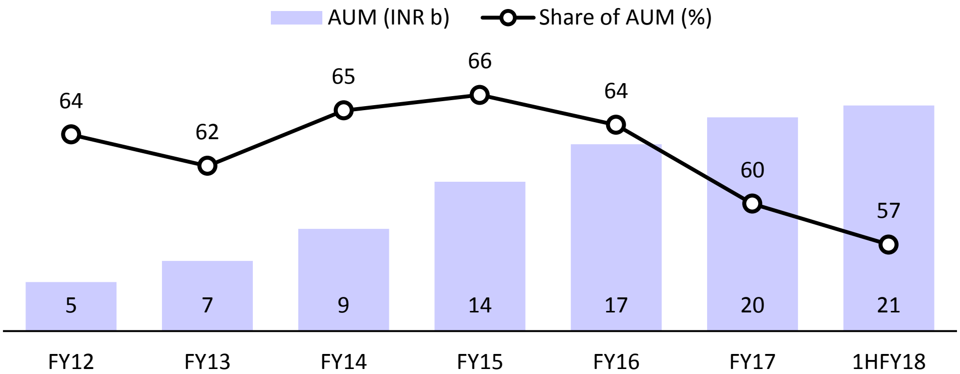
Source: MOSL, Company

Micro-enterprise loans (MEL) – a key growth driver

90% of the active customer base from MEL product; Avg. ticket size of ~INR34k

MASFIN provides two categories of micro-enterprise loans: (i) loans up to INR75k, typically to self-employed individuals engaged in trading or manufacturing business, and (ii) loans of INR75k-300k, typically to sole proprietors and partnership firms. In FY17, the average disbursement in its MEL segment was ~INR34k. Larger proportion of this portfolio is sourced via on-lending book. This portfolio contributes ~90% of the company's active customer base.

Exhibit 8: MEL is the key product for company



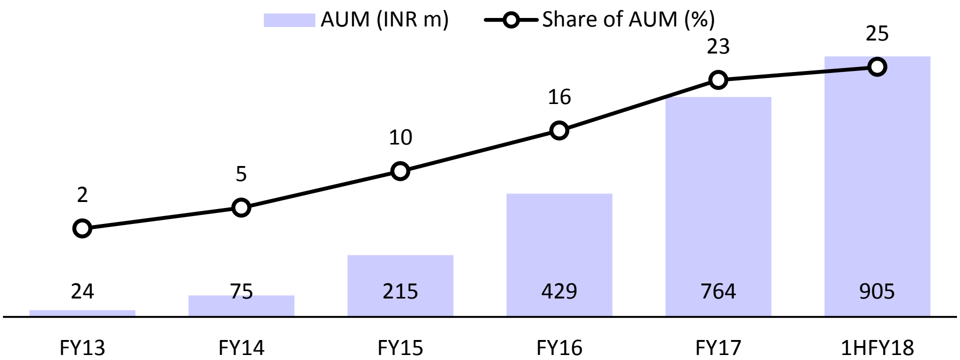
Source: MOSL, Company

SME loans – sharp increase in share of AUM

SME loans a key growth driver; share in AUM up from 2% in FY13 to 25% in 1HFY18

MASFIN provides loans of up to INR50m to its SME customers (primarily small and medium-sized manufacturers, dealers and service providers). The SME loan segment includes working capital loans (up to INR50m), loans for machinery and facilities (up to INR20m), loans against property (up to INR20m), and loans extended to housing finance companies. In FY17, the average disbursement in its SME loan segment was INR5.5m. Within its SME portfolio, MASFIN also plans to finance the working capital needs of manufacturers, distributors and dealers of agricultural inputs like seeds, fertilizers, insecticides and pesticides, and farm accessories and equipment.

Exhibit 9: SME loans' share in AUM rising



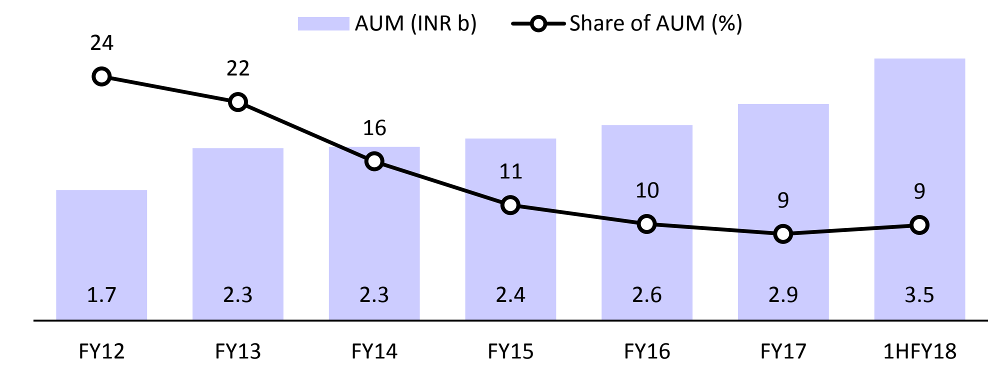
Source: MOSL, Company

Two-wheeler (2W) loans – decline in AUM share over the years

Share of 2W loans in total AUM declined from 24% in FY12 to 9% in 1HFY18

MASFIN provides two-wheeler loans primarily to farmers, self-employed or salaried individuals, as well as professionals. Disbursements are largely sourced at the dealer level. In absolute terms, this portfolio has remained largely stable at INR2.2b-2.8b. In FY17, the average ticket size in the two-wheeler loan segment was ~INR43k. This portfolio contributes ~20% of the company's active customer base.

Exhibit 10: Two wheeler portfolio in the narrow range of INR2-3b



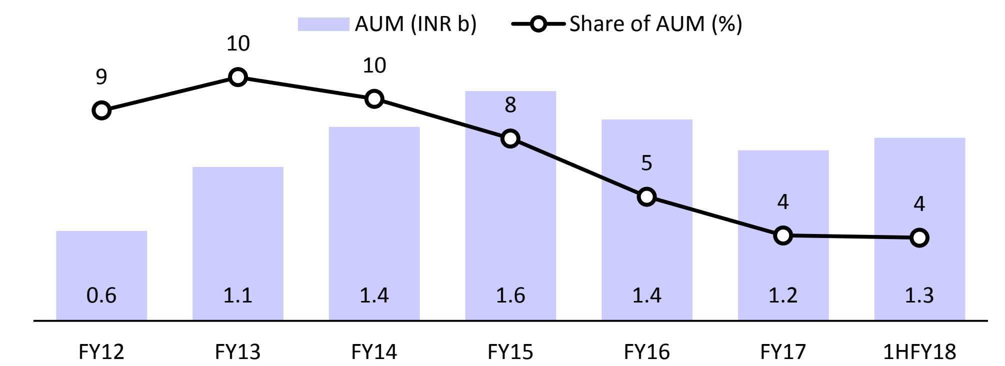
Source: MOSL, Company

CV loans account for 4% of the loan book

Commercial vehicle (CV) loans – risk aversion led by macro headwinds

MASFIN provides loans up to INR0.7m for the purchase of new and used commercial vehicles, used cars as well as tractors. In this segment, customers primarily include traders and manufacturers (for loading vehicles), travel businesses, and small road-transport operators. In absolute terms, this portfolio has remained largely stable at INR1b-1.3b due to macroeconomic issues like (a) sand mining ban, (b) moderate economic activity, (c) Scrappage policy. In FY17, the average disbursement in its CV loan segment was INR0.15m.

Exhibit 11: CV loans' share in AUM declining



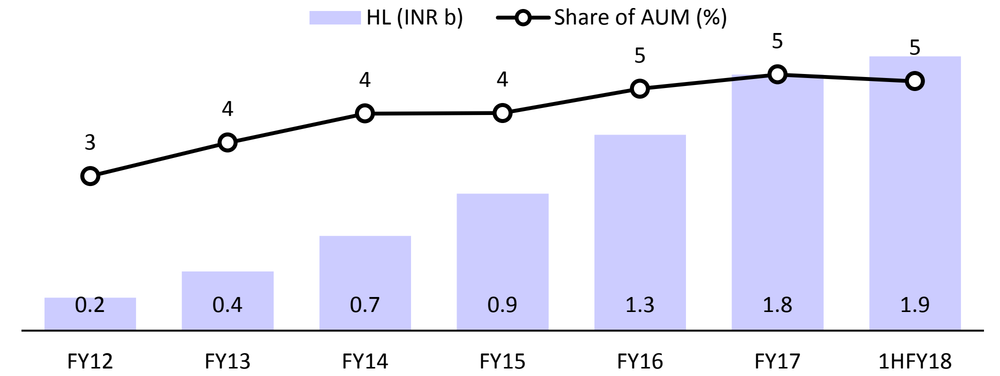
Source: MOSL, Company

MASFIN owns 60% stake in its housing finance subsidiary

Strong momentum in affordable housing

MASFIN provides housing loans to customers for the purchase of new and old houses, construction of houses on owned plots, home improvement, and purchase and construction of commercial property. Its customers in this segment typically include salaried and self-employed individuals. It also extends loans to developers for the construction of affordable housing projects. The loan amount ranges between INR50k and INR5m for residential property and between INR50k and INR10m for commercial property. The housing finance business is operated through subsidiary, MRHMFL (MASFIN owns 60%; promoters own the balance). As of September 2017, the company had 45 sourcing intermediaries (typically project developers and property agents) and 68 branches. In FY17, average disbursement in the housing loan segment was INR1.22m.

Exhibit 12: Share of Housing loans in AUM gradually increasing



Source: MOSL, Company

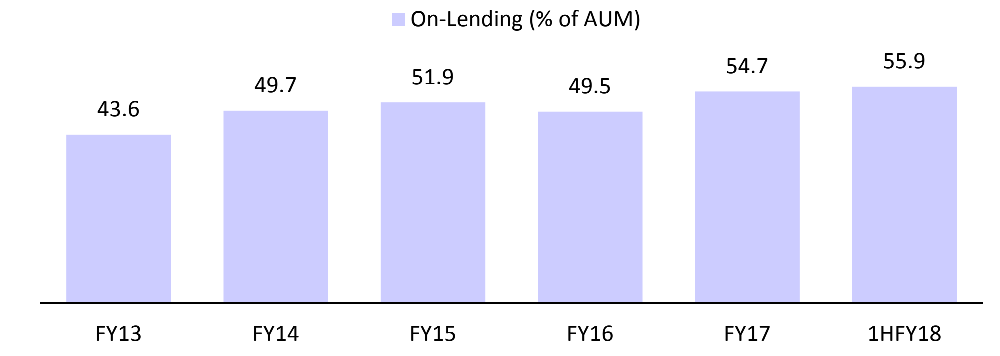
We believe MASFIN will expand its housing finance business by increasing the geographic reach of MRHMFL's operations. MRHMFL currently operates in semi-urban and rural areas of Gujarat, Maharashtra, Rajasthan and Madhya Pradesh, and is likely to establish additional branches in states that have favorable business potential for affordable housing loans. MASFIN is equipped to understand customer preferences by assessing income levels. It will leverage its existing operational network and customer base to cross-sell housing loans to its existing customers.

Leveraging sourcing channels to augment growth

Loan sourcing done by own feet on street, sourcing intermediaries and NBFC partnerships

MASFIN extends loans largely to self-employed individuals; its focus is more on the rural and semi-urban geographies. It sources loans through its own sales force; it also extends loans to MFIs, HFCs and other NBFCs operating in sectors similar to its own, particularly in geographical areas where it has limited direct operations.

Exhibit 13: Effectively utilizing on-lending model for growth



Source: MOSL, Company

More than 55% of AUM driven by on-lending business with an aim to create quality assets within targeted class

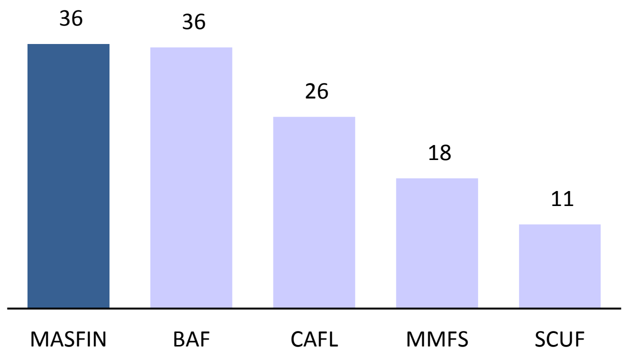
When it lends to other financial institutions, a portion of their receivables and book debts are hypothecated to MASFIN. Additionally, these financial institutions are required to maintain an agreed percentage of the loan amount as cash collateral or security receipts along with promoter guarantees in certain cases. As of September 2017, MAS had 683 sales feet on street (FOS), 316 CV loan sourcing intermediaries, 328 2W loan intermediaries, and 105 NBFC partnerships. As of September 2017, 56% of underlying assets (of total AUM) were sourced through NBFC partnerships.

AUM to double by FY20

Fastest FY12-17 AUM CAGR among peers

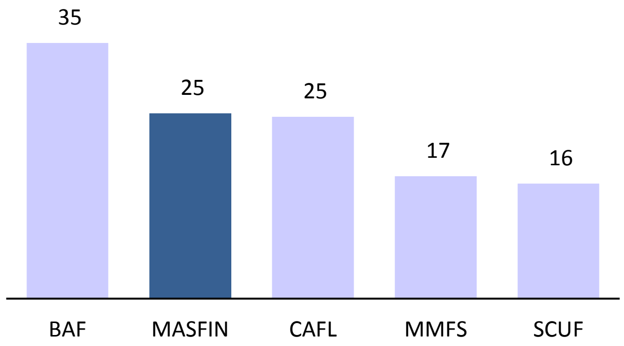
We expect MASFIN to report 25% AUM CAGR over FY17-20 aided by continued growth in MEL, SME loans and housing loans. We also expect a pickup in vehicle loans led by macroeconomic factors. MASFIN is also introducing agri loan/ equipment loan products, which could drive growth further.

Exhibit 14: FY12-17 loan book CAGR (%) – best among peers



Source: MOSL, Company

Exhibit 15: FY17-20E loan book CAGR (%) – among top-3



Source: MOSL, Company

Strong risk management driving superior asset quality

Among the lowest credit cost companies in our NBFC coverage universe

- **MASFIN has strong credit policies for loan monitoring, collection and recovery, manifesting into low credit costs.**
- **Its unique business model of on-lending to other financiers and in turn hypothecating the portfolio (providing at least 100% coverage) also helps MASFIN to maintain strong control over asset quality. It also takes promoter guarantees and certain percentage of exposure as cash collateral.**
- **Focus on asset quality versus growth and strong local area knowledge helps the company to keep control over credit costs.**

Superior underwriting standards

In case of on-lending, part of default risk is borne by sourcing partners

Customer origination is primarily through MASFIN's sales team. The sales team informs its target customers on MASFIN's various product offerings. MASFIN has entered into commercial arrangements with sourcing intermediaries, including commission-based DSAs and various dealers/distributors, where part of the loan default is guaranteed by such sourcing partners.

Credit policies for loans on-lending book

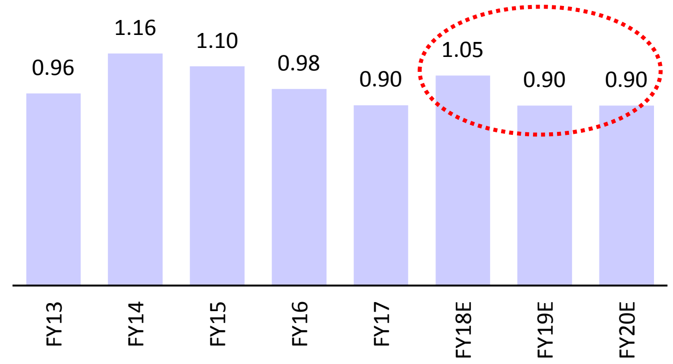
- Financial institution must have been in existence for at least three years.
- Undertake due diligence and analyze audited balance sheets for three years, verify bank account statements for previous six months and examine credit history.
- Analyze systems, operations, credit processes and policies.
- Analyze portfolio at risk and NPA details, and obtain an internal de-duplication report.
- Conduct an overdue analysis, site verification, market reference checks and interviews.
- PAR90 should be less than 5%.
- MASFIN hypothecates the entire portfolio with itself. It also insists on cash collateral (certain percentage of lending) as security deposit and promoter guarantees (in certain cases). Margin money and other charges are collected prior to disbursements.
- If the underlying portfolio turns sub-standard, the company has an arrangement with intermediaries that it will be replaced with standard portfolio.
- MASFIN also takes demand promissory notes, letters of continuity, and other general undertakings as collateral security.
- In certain circumstances, the company has the right to convert outstanding loan amounts into fully paid-up shares in such institutional borrowers.

Loan monitoring, collection and recovery for sourcing intermediaries

- Complete set of documents are stored at central office.
- Borrowers with larger exposure are specifically reviewed every quarter by risk management committee.
- Delinquent borrowers are under constant scrutiny and follow-up by collection team.
- 100% collection is non-cash – either post-dated cheques or NACH mandates.

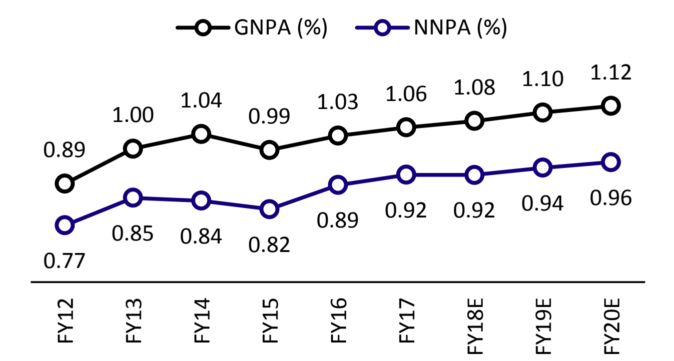
- In certain cases, defaults are managed through financial counseling.
- For any further delinquencies, the legal team initiates legal action for seizure of collateral for recovery of dues.

Exhibit 16: We bake in stable credit costs through FY18-20



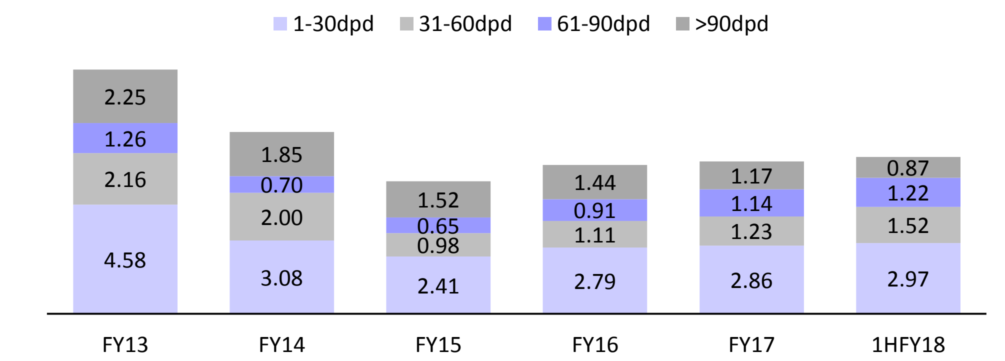
Source: MOSL, Company

Exhibit 17: GNPA remains in the range of 1-1.2%



Source: MOSL, Company

Exhibit 18: AUM – dpd profile



Source: MOSL, Company

35%+ PAT CAGR over the medium term

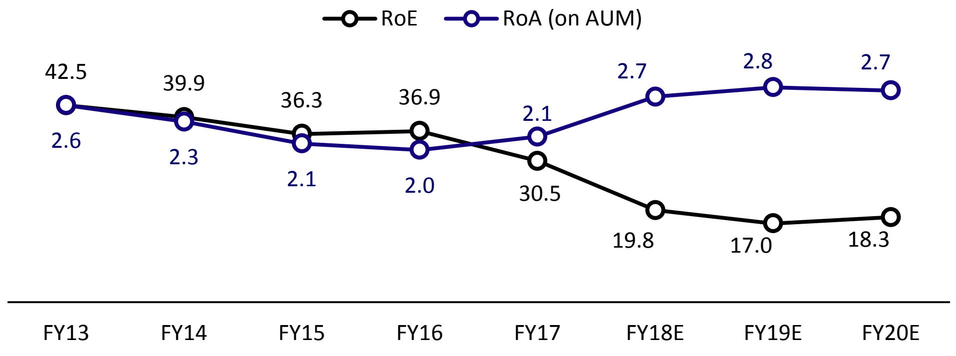
Sustainable RoE to be healthy at 19%+

- **We model AUM CAGR of 25% and PAT CAGR of 36% over FY17-20E. RoA (on AUM) expansion would be largely led by higher margins, as equity contribution in overall funding has increased sharply (7% of funds to 13% of funds) and portfolio diversification towards higher yielding assets to take place. We also expect operating efficiency to play out with higher growth from existing branch network.**
- **Higher share of direct lending coupled with stable asset quality would support RoA. We bake in RoA (on AUM) improvement of 60bp+ to 2.7% over FY17-20; however, reduction in equity leverage would reduce RoE from 30%+ in FY17 to ~19% in FY20E.**

Expect sharp RoA improvement; reduction in leverage to lower RoE

Improvement in spreads and operating leverage would improve PPoP to average AUM by ~60bp over the next three years and RoA by 60bp to 2.7% by FY20. On the back of large capital issuance, leverage (on AUM/loans) is expected to decline from ~17x /11xto ~7x/5x over the next three years. Overall, we expect the company to report healthy RoE of 18-20% over the next three years.

Exhibit 19: Superior return ratios through FY17-20E, as operating leverage plays out



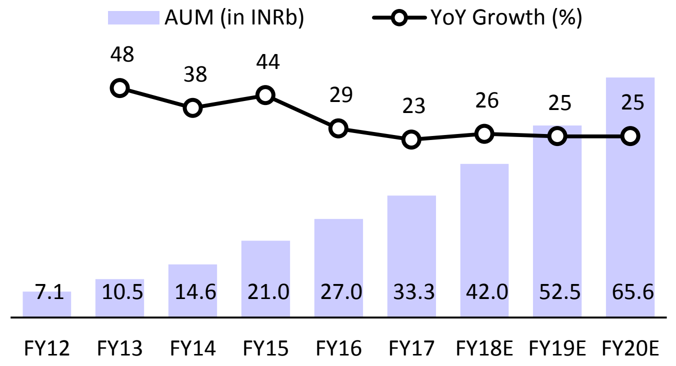
Source: MOSL, Company

NIM to improve, helped by asset and liability diversification; Capital raise to benefit

Expect 32% CAGR in NII over FY17-20, helped by AUM CAGR of 25% and NIM expansion of 100bp

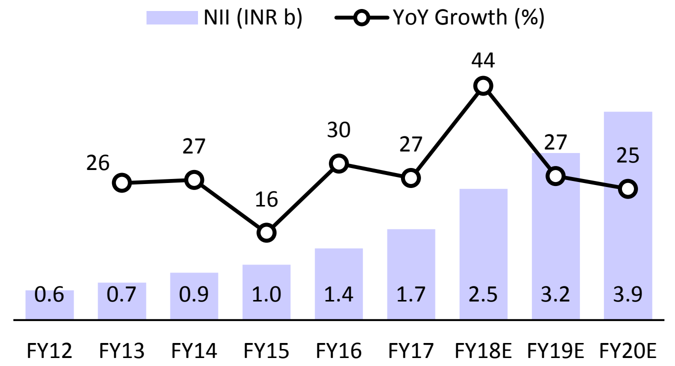
We bake in 100bp NIM (on AUM) expansion to 6.7%, helped by capital infusion of INR4.4b (INR1.35b pre-IPO + INR2.3b of IPO + INR0.9b hybrid conversion) in 1HFY18, rising share of direct lending, and diversification of asset and liability profile. Backed by 25% AUM growth and margin expansion, we expect NII CAGR of 32% over FY17-20E.

Exhibit 20: AUM to grow at 25% CAGR over FY17-20



Source: MOSL, Company

Exhibit 21: Expect NII CAGR of 33% over FY17-20

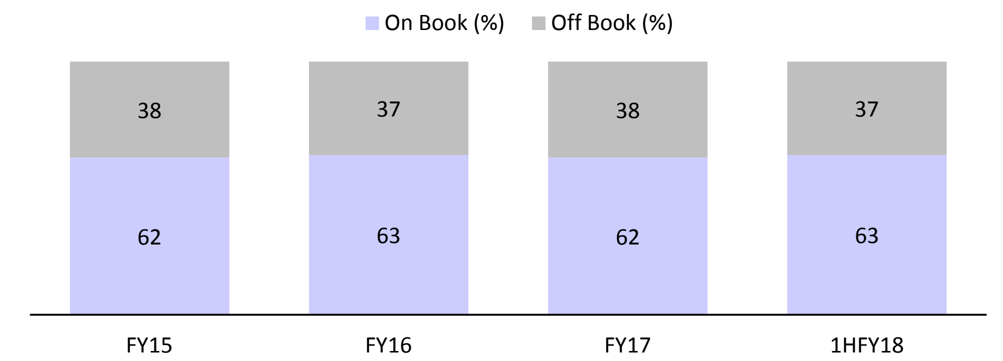


Source: MOSL, Company

37% of AUM is off-balance sheet

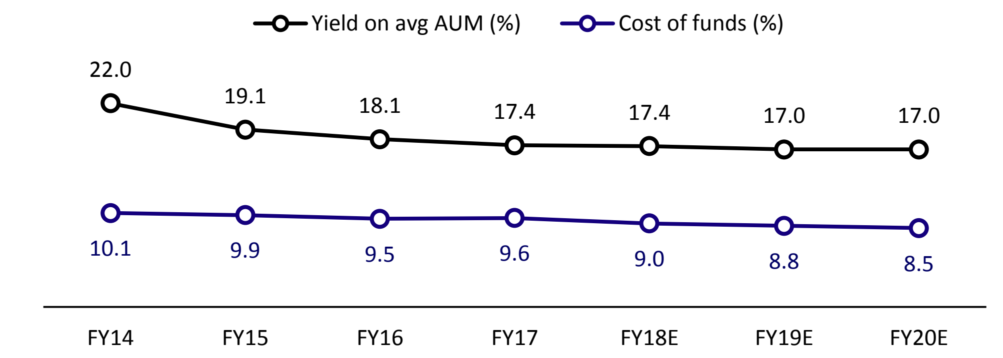
Historically, the company has effectively utilized the securitization and assignment route to lower cost of funds. Since a large part of the portfolio qualifies for PSL and performance of the portfolio is superior, the share of off-balance sheet assets has remained 35%+ of the overall portfolio.

Exhibit 22: Share of on-book and off-book AUM



Source: MOSL, Company

Exhibit 23: Reduction in spreads led by higher share of on-lending portfolio

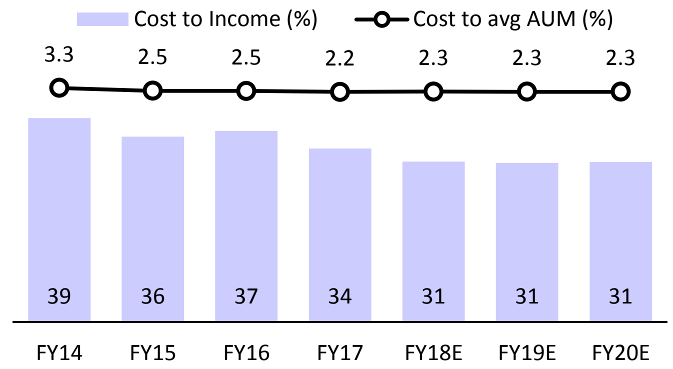


Source: MOSL, Company

Operating efficiencies to play out

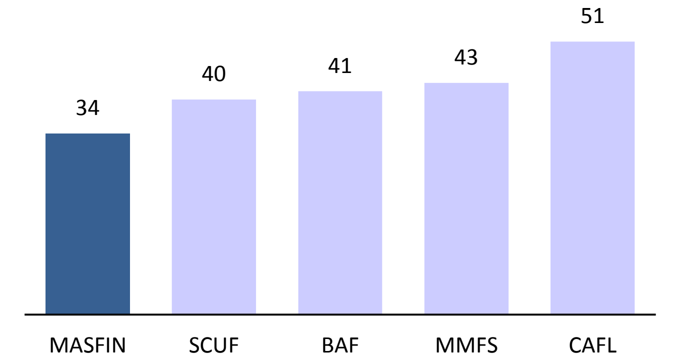
MASFIN had an opex CAGR of 15% over FY12-17 versus AUM CAGR of 36%. Sourcing arrangements for loans coupled with higher share of on-lending portfolio helps in keeping employee count and admin costs in check. We bake in opex CAGR of 26% versus AUM CAGR of 25% over FY17-20. Opex to AUM is expected to remain stable at 2.30% while C/I ratio is expected to decline 250bp to 31% over FY17-20.

Exhibit 24: C/I ratio to decline 250bp



Source: MOSL, Company

Exhibit 25: Cost-to-Income ratio v/s peers in FY17

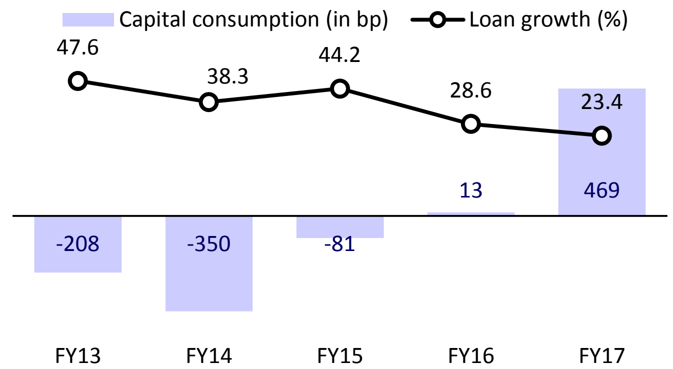


Source: MOSL, Company

Sufficiently capitalized for at least three years of growth

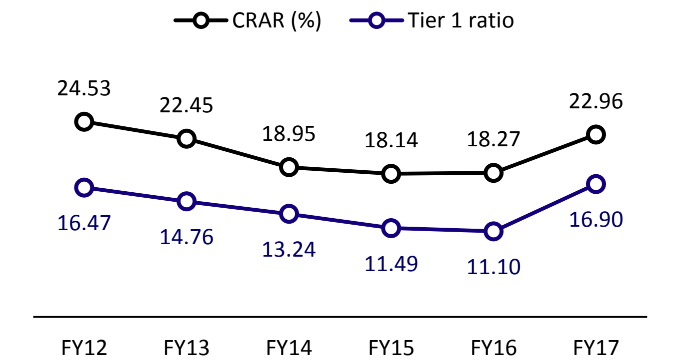
MASFIN has effectively used various measures (assignment/securitization, hybrid instruments, and focused profitable growth) for capital conservation and deliver higher value to shareholders. In 1HFY18, it raised INR4.4b and net worth has increased to INR6.5b (from INR1.8b). Post the capital raising, leverage (on balance sheet) reduced to ~4x and tier-I ratio improved to 32%+. Based on expected internal accruals, focus on 25-30% growth, and strong capitalization, we believe MASFIN is adequately capitalized for at least three years of growth.

Exhibit 26: Capital consumption v/s loan growth



Source: MOSL, Company

Exhibit 27: MASFIN remains well capitalized



Source: MOSL, Company

SWOT analysis

Strength

- Presence in high-growth business segments, with lower asset quality risk.
- Highly scalable loan sourcing business model.
- Strong technology platform.
- Best-in-class liability franchise, with declining dependence on bank borrowings.

Weaknesses

- Dependence on loan sourcing intermediaries.
- Geographic concentration in six states.

Opportunities

- Operates in underpenetrated business segments with huge growth potential.
- With implementation of GST and RERA, there could be a shift to more formal sources of financing.

Threats

- High share of informal sector exposure.
- Intense competition in new markets like the NCR, Karnataka and Tamil Nadu may impact yields.

Bull & Bear case

Bull Case

- ☑ In our bull case, we assume strong AUM CAGR of 30% (v/s 25% in base case). We believe scale up of housing finance business and growth in MEL business could surprise on the upside.
- ☑ We expect margins to increase slightly to 6.8% by FY20E (v/s 6.7% in the base case) as the company is able to hold on to yields despite a competitive scenario.
- ☑ We expect significant cost control, with cost-to-income ratio declining to 27% by FY20E compared to 31% in our base case.
- ☑ This results in PAT CAGR of 44% (v/s 36% in our base case) over FY17-20e, with RoA/RoE of 4.4%/21% in FY20E (4.0%/18% in base case).
- ☑ Based on the above assumptions, we value the company at INR907 (25x FY20E EPS) – an upside of 47%.

Bear Case

- ☑ In our bear case, we assume AUM CAGR of 15% (v/s 25% in our base case). Delay in scaling up the newly-launched lending products and modest trend in the MEL segment may result in such a scenario.
- ☑ We expect margins to decline to 6.2% by FY20E v/s 6.7% in the base case driven by continued yield pressure
- ☑ We expect cost ratios to increase, resulting in C/I ratio increasing to 38% by FY20E (v/s 31% in our base case).
- ☑ This results in PAT CAGR of 21% (v/s 36% in our base case) over FY17-20E, with RoA/RoE at 3.3%/13.4% in FY20E.
- ☑ Based on the above assumptions, we value the stock at INR480 (23x FY20E EPS) – a downside of 22%.

Exhibit 28: Scenario Analysis – Bull Case

Bull Case	FY18E	FY19E	FY20E
Total Income	2,892	3,919	4,943
Opex	871	1,087	1,357
Provisions	412	467	594
PBT	1,609	2,365	2,993
PAT	1,044	1,537	1,945
NIM (%)	6.5	6.8	6.8
RoA (%)	4.0	4.4	4.4
RoE (%)	20.6	19.6	21.2
EPS	19.1	28.1	35.6
BV	133.2	154.3	181.0
Target earnings multiple	**25**		
Target price (INR)	**907**		
Upside (%)	**47%**		

Source: Company, MOSL

Exhibit 29: Scenario Analysis – Bear Case

Bear Case	FY18E	FY19E	FY20E
Total Income	2,785	3,119	3,448
Opex	871	1,111	1,386
Provisions	395	397	436
PBT	1,519	1,611	1,626
PAT	985	1,043	1,050
NIM (%)	6.5	6.2	6.2
RoA (%)	3.9	3.4	3.0
RoE (%)	19.5	13.7	12.5
EPS	18.0	19.1	19.2
BV	132.4	146.7	161.1
Target earnings multiple	**23**		
Target price (INR)	**480**		
Upside (%)	**-22%**		

Source: Company, MOSL

Initiate with a Buy; target price of INR740

Consistent performance warrants premium valuations

Strong growth, best-in-class asset quality and efficient use of capital are some of the key strengths of the company

Margin improvement, operating leverage and controlled credit cost should drive RoA improvement of 60bp+ and we expect the company to consistently report 18%+ RoE. The recent capital raising would be sufficient for the next three years of growth, in our view. We believe MASFIN has all the ingredients of a good investment: (a) a small base and presence in well-developed states for strong growth, (b) superior asset quality, (c) relentless management focus on generating sustainable, high return ratios, (d) healthy capitalization, and (e) consistent dividend payout. We initiate coverage with a **Buy** rating and a target price of INR740 (25x FY20E EPS, implied 4.3x FY20E BV).

Exhibit 30: DuPont analysis (on avg. AUM)

%	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Net Interest Income	**8.03**	**7.16**	**5.88**	**5.65**	**5.71**	**6.60**	**6.69**	**6.68**
Fee Income	1.53	1.17	1.15	1.05	0.91	0.83	0.76	0.70
Net Income	**9.57**	**8.33**	**7.04**	**6.71**	**6.61**	**7.43**	**7.46**	**7.39**
Non interest Income	0.29	0.13	0.08	0.04	0.03	0.03	0.03	0.03
Net Income	**9.86**	**8.46**	**7.11**	**6.75**	**6.65**	**7.46**	**7.49**	**7.42**
Operating Expenses	**4.31**	**3.33**	**2.55**	**2.49**	**2.23**	**2.31**	**2.30**	**2.30**
Operating Profits	**5.55**	**5.12**	**4.57**	**4.25**	**4.42**	**5.15**	**5.19**	**5.12**
Provisions/write offs	0.96	1.16	1.10	0.98	0.90	1.05	0.90	0.90
PBT	**4.59**	**3.96**	**3.47**	**3.27**	**3.52**	**4.10**	**4.29**	**4.22**
Tax	1.48	1.32	1.17	1.13	1.22	1.41	1.48	1.46
PAT	**3.11**	**2.64**	**2.29**	**2.14**	**2.30**	**2.69**	**2.81**	**2.77**
Less: Preference shares and MI	0.56	0.30	0.24	0.17	0.16	0.03	0.03	0.03
PAT for Equity shareholders	**2.55**	**2.34**	**2.05**	**1.97**	**2.14**	**2.66**	**2.78**	**2.74**
Leverage (x)	*16.65*	*17.08*	*17.69*	*18.74*	*14.22*	*7.46*	*6.10*	*6.68*
RoE	**42.48**	**39.91**	**36.32**	**36.92**	**30.47**	**19.85**	**16.99**	**18.31**

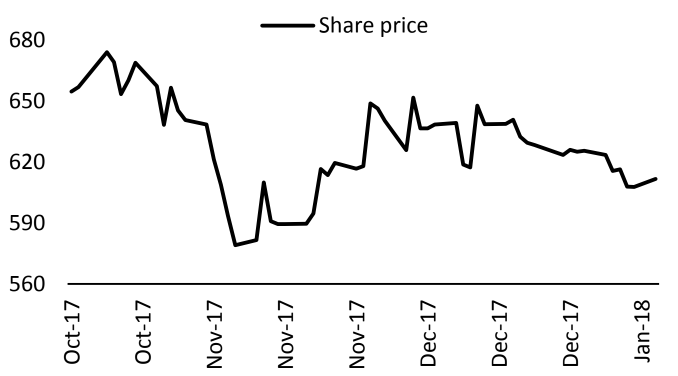
Source: MOSL, Company

Exhibit 31: DuPont analysis (average FY18-20E) – vs. competition

	SCUF	MMFS	BAF	CAFL	MASFIN
Net Interest Income	**13.41**	**8.25**	**10.61**	**8.16**	**6.66**
Fee Income	0.16	0.23	1.49	2.17	0.77
Net Income	**13.57**	**8.48**	**12.10**	**10.33**	**7.42**
Other Income	0.03	0.20	0.09	0.28	0.03
Total Income	**13.60**	**8.68**	**12.19**	**10.61**	**7.46**
Operating Expenses	**5.33**	**3.48**	**4.82**	**5.30**	**2.30**
Operating Profits	**8.27**	**5.19**	**7.36**	**5.31**	**5.15**
Provisions/write offs	3.20	2.28	1.66	3.09	0.95
PBT	**5.07**	**2.91**	**5.70**	**2.21**	**4.20**
Tax	1.77	0.99	1.99	0.73	1.45
PAT	**3.30**	**1.92**	**3.71**	**1.49**	**2.75**
Less: Preference shares and MI	0.00	0.00	0.00	0.00	0.03
PAT for Equity shareholders	**3.30**	**1.92**	**3.71**	**1.49**	**2.73**
Leverage (x)	4.71	7.57	5.71	10.23	6.75
RoE	**15.57**	**14.59**	**21.25**	**15.26**	**18.38**

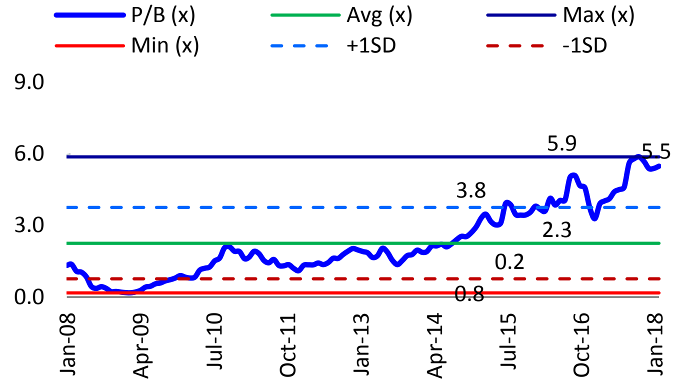
Source: MOSL, Company

Exhibit 32: MASFIN price chart (INR)



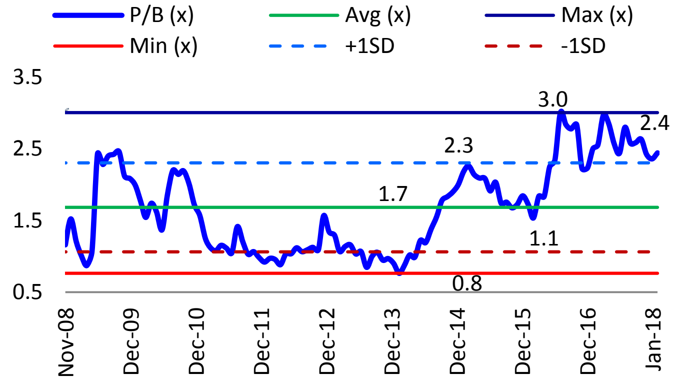
Source: MOSL, Company

Exhibit 33: BAF P/B chart



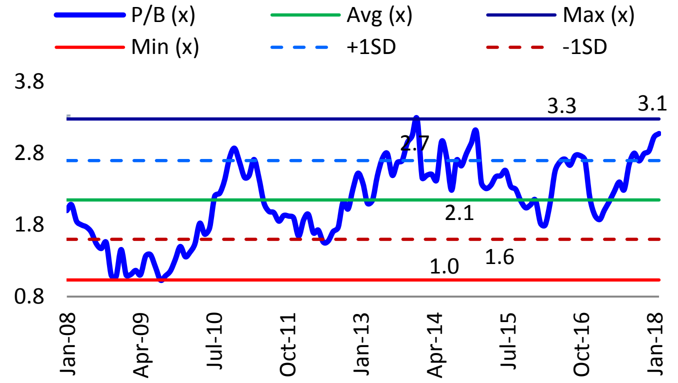
Source: MOSL, Company

Exhibit 34: CAFL P/B chart



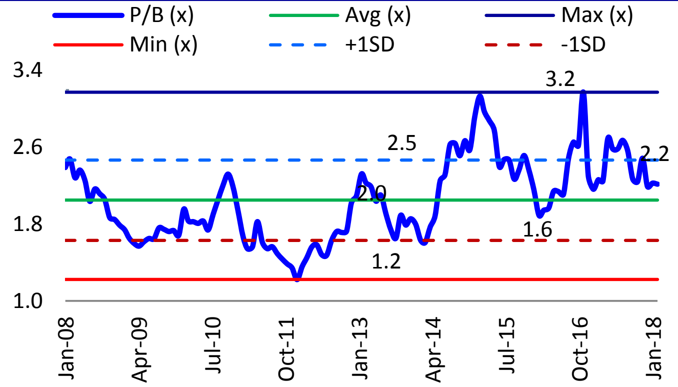
Source: MOSL, Company

Exhibit 35: MMFS P/B chart



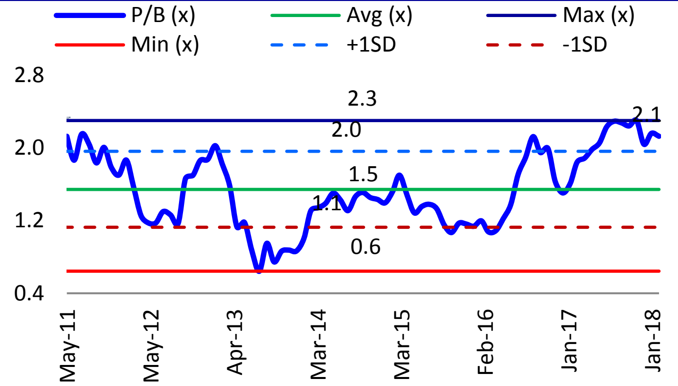
Source: MOSL, Company

Exhibit 36: SCUF P/B chart



Source: MOSL, Company

Exhibit 37: Muthoot Finance P/B chart



Source: MOSL, Company

Key risks

Geographic concentration

The company has significant concentration in Gujarat (36 branches) and Maharashtra (20); these two states account for ~90% of its branches. Though the management has chalked out plans to diversify into new geographies, the high geographic concentration is likely to remain in the medium term.

Dependence on sourcing partners

As of September 2017, 56% of MASFIN's outstanding AUM was sourced by NBFC, MFI and HFC partnerships. We reckon that these sourcing channels may not yield the growth desired by MASFIN. Also, such partnerships increase the counterparty risk, though MASFIN has portfolio hypothecated as additional collateral apart from promoter guarantees.

Exposure to informal sector

MASFIN largely caters to self-employed/salaried individuals and farmers in semi-urban and rural areas. Given that most of these people have uneven cash flows as income, any adverse event could trigger large scale migration to hard-bucket NPAs, and eventually to loss assets and write-offs.

Significant dependence on bank borrowings

Funding requirement has historically been met through term loans from financial institutions (primarily banks). While the company is planning to diversify its liability mix, near-term concentration on one source of borrowings will remain a key risk.

APPENDIX - 1

PRODUCT AND CLIENT-WISE CREDIT ASSESSMENT CRITERIA

*TYPES OF LOAN

MEL

Loan size	Client type	Credit assessment and approval criteria
Up to INR 75k	Self-Employed Non-Professionals (SENP) involved in manufacturing and trading	❖ Age between 21 and 65 years ❖ Applicant below 25 years need a family member as co-applicant ❖ Credit Bureau and internal database check on applicant, co-applicant and guarantor ❖ Site visits and interviews with applicant ❖ Collect bank statements for previous six months for all accounts, where applicable ❖ Loans upto INR50k approved by credit officer, INR50-60k Senior Credit officer and >INR60k by credit – in – Charge
INR75k to INR 300k	Sole proprietors and partnerships	❖ Minimum age of 22 years (family owned business) and 25 years (first generation business); Maximum age 65 years ❖ Applicant's spouse as a co-applicant in all cases ❖ Residence/business premises should be owned either by applicant/parent/spouse/child ❖ Credit Bureau and internal database check on applicant, co-applicant and guarantor ❖ Site visits and interviews with applicant; Upto INR0.1m interviews done by local site officer and loans >INR0.1m by branch manager or branch credit officer ❖ Loans upto INR0.1m approved by senior credit officer, INR100-150k by credit - in - Charge and >INR150k by director or COO ❖ Collect bank statements for last 6 months for all applicable accounts ❖ Verify IT returns along with financial statements to ensure for cash profit in previous 3 years

SME

Key underwriting standards applied across categories in SME

- Cash collateral
- One woman borrower as co-applicant and a third party guarantee
- Credit bureau, internal de-duplication and market reference checks, as applicable, along with site visits and interviews
- Personal Guarantees along with post-dated checks mandatory
- Cash Collateral as an additional security, if required
  Financial statements of past three years

SME

Loan size	Client type	Credit assessment and approval criteria
Up to INR5m	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of at least one year or more; Machinery loans operating history of >5years ❖ Ownership of at least one property. ❖ 50% of turnover (70% for machinery loans), as assessed by our credit team, present in current account. ❖ Guarantor is required for machinery loans
Up to INR10m	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of at least two years or more; Machinery loans operating history of >5years ❖ Ownership of at least one property. ❖ 55% of turnover (70% for machinery loans), as assessed by our credit team, present in current account. ❖ Guarantor is required for machinery loans
Up to INR20m	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of at least three years or more ; Machinery loans operating history of >5years upto INR1.5m and >7years for upto INR2m ❖ Ownership of residential and business property. ❖ 60% of turnover (70% upto INR1.5m and 75% upto INR2m for machinery loans) as assessed by our credit team, present in current account. Audited financial statements required for machinery loans
Up to INR30m	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of at least four years or more. ❖ Ownership of residential and business property. ❖ 65% of turnover, as assessed by our credit team, present in current account.
Up to INR50m	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of at least five years or more. ❖ Ownership of residential and business property. ❖ 70% of turnover, as assessed by our credit team, present in current account.

LAP

Loan size	Client type	Credit assessment and approval criteria
Up to INR7.5m in metro cities, INR5m in urban areas, INR4m in semi-urban areas	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of one year or more. ❖ Ownership of at least one property. ❖ 50% - 60% turnover, as assessed by our credit team, present in current account.
Up to INR15m in metro cities, INR12.5m in urban areas, INR10m in semi-urban areas	Small and medium size manufacturers, distributors, dealers and service providers	❖ Business is required to have an operating history of two years or more. ❖ Ownership of residence and business property. ❖ 60% - 75% turnover, as assessed by our credit team, present in current account.
Up to INR20m in metro cities, INR15m in urban areas, INR10m in semi-urban areas		❖ Business is required to have an operating history of three years or more. ❖ Ownership of residence and business property. ❖ At least 75% turnover, as assessed by our credit team, present in current account.

Two-Wheelers

Loan size	Client type	Credit assessment and approval criteria
INR 15k to INR200k	SENP, Farmers and Salaried	❖ Age between 18 to 60 ❖ At least one property (residential or business) should be owned by the applicant or jointly residing family members. ❖ A family member as a co-applicant is compulsory if the applicant is self-employed ❖ Conduct credit bureau and other database checks on the applicant, co-applicant and guarantor. ❖ Site visit

Commercial Vehicles

Loan size	Client type	Credit assessment and approval criteria
Up to INR700k	Traders, Manufacturers and Road transporters	❖ Age between 18 to 65 ❖ A family member as a co-applicant is compulsory if the applicant is self-employed ❖ At least one property (residential or business) should be owned by the applicant or jointly residing family members. ❖ The vehicle is hypothecated to MASFIN and the insurance policy is required to be executed in its favor. ❖ Conduct credit bureau and other database checks on the applicant, co-applicant and guarantor. ❖ Collect bank statements for previous six months for all accounts, where applicable ❖ Site visit

Home Loans

Loan size	Client type	Credit assessment and approval criteria
INR50k to INR5m for residential properties	SENP and Salaried	❖ Age between 18 to 65
INR50k to INR10m for commercial properties		❖ Conduct credit bureau and other database checks on the applicant, co-applicant and guarantor. ❖ For loans extended to developers for affordable housing projects, the applicant is required to have at least three years' ❖ Operating experience with ownership of residential or office property. ❖ Site visit

Appendix -2 History of capital raise

Exhibit 38: Equity Share Capital Raise

Date	Investor	Issuance	Price	Terms	Others
21-Sep-17	DEG	Issued 24,70,175 Equity Shares	263.03	❖ Conversion of 4998 CCD	❖ All offered for sale in IPO
12-Sep-17	FMO	Issued 17,39,865 Equity Shares	124.93	❖ Conversion of 2,17,35,545 Series A CCCPS	❖ All offered for sale in IPO
12-Sep-17	Sarva Capital	Issued 12,80,723 Equity Shares	322.71	❖ Conversion of 2,17,35,545 Series B CCCPS	❖ 60% offered for sale in IPO
12-Sep-17	Nine Individual Shareholders	Issued 87,716 Equity Shares	456	❖ Conversion of 400 Series C CCCPS	
19-Apr-17	Motilal Oswal Securities and Motilal Oswal Financial Services	Issued 10,34,553 Equity Shares	338.31 (INR350m)	❖ Preferential Allotment	
30-Mar-17	Motilal Oswal Securities and Motilal Oswal Financial Services	Issued 29,55,819 Equity Shares	338.31 (INR1,000m)	❖ Preferential Allotment	
13-Jun-12	DEG	Issued 125 shares	1200 (Including premium of INR1190)	❖ Along with CCDs	

Exhibit 39: Preference Equity Share Capital Raise

Date	Investor	Issuance	Price	Terms	Others
13-May-16	Nine Shareholders (Individual)	Issued 400 CCPS	FV of INR0.1m	❖ 9.75% CCCPS; To be converted into Equity Shares at INR1685 (pre bonus, split etc)	❖ Conversion price near to IPO price
29-Jan-14	Sarva Capital	Issued 2,17,35,545 CCPS	FV of INR10 (at PAR)	❖ 13.31% (from 17-02-2014) Series B CCCPS ❖ (Conversion from FMO holding of 30-06-2008)	❖ Acquired from FMO for INR413.3m ❖ To be converted into ES by 17-02-2021 or at IPO whichever is earlier
29-Jan-14	FMO	Issued 2,17,35,545 CCPS	FV of INR10 (at PAR)	❖ 0.01% (from 17-02-2014) CCCPS Series A ❖ (Conversion from FMO holding of 30-06-2008)	❖ To be converted into ES by 13-10-2021 or at IPO whichever is earlier
28-Jul-12	DEG	Issued 4998 CCDs	At a premium INR30,000 per CCD; FV of INR1,00,000 per CCD		❖ To be converted into Equity shares
23-Jul-08	FMO	Issued 4,34,71,090	FV of INR10 (at PAR)	❖ 7% CCCPS	❖ Half of these sold to Sarva on 29-01-2014 at INR413.3m after breaking the holding in Series A CCPS (FMO holds it) and Series B CCPS (Sarva holds it)

Source: MOSL, Company

Financials and valuations

INCOME STATEMENT									(INR Million)
Y/E MARCH	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Interest Income	1,002	1,270	1,687	2,164	2,779	3,364	4,199	5,223	6,528
Interest Expense	438	560	788	1,117	1,423	1,642	1,714	2,060	2,579
Net Financing income	**564**	**710**	**898**	**1,046**	**1,356**	**1,721**	**2,485**	**3,162**	**3,948**
Change (%)		26.0	26.5	16.5	29.6	26.9	44.3	27.3	24.9
Other operating income	127	135	147	205	253	273	314	362	416
Other Income	29	26	16	13	10	10	12	15	19
Net Income	**719**	**871**	**1,061**	**1,265**	**1,619**	**2,005**	**2,811**	**3,539**	**4,383**
Change (%)		21.2	21.8	19.2	28.0	23.8	40.2	25.9	23.8
Operating Expenses	**342**	**381**	**418**	**453**	**598**	**672**	**871**	**1,087**	**1,357**
Change (%)		11.4	9.8	8.3	32.0	12.4	29.7	24.8	24.8
Operating Profits	**377**	**491**	**643**	**812**	**1,021**	**1,333**	**1,940**	**2,452**	**3,027**
Change (%)		30.0	31.0	26.3	25.8	30.5	45.6	26.4	23.4
Total Provisions	**91**	**85**	**146**	**195**	**236**	**272**	**396**	**425**	**532**
% to operating income	24.0	17.3	22.7	24.0	23.1	20.4	20.4	17.3	17.6
PBT	**287**	**406**	**497**	**617**	**785**	**1,060**	**1,544**	**2,026**	**2,495**
Tax	85	131	166	209	271	367	533	699	861
Tax Rate (%)	29.7	32.3	33.4	33.8	34.5	34.6	34.5	34.5	34.5
PAT	**202**	**275**	**331**	**408**	**515**	**693**	**1,012**	**1,327**	**1,634**
Change (%)		36.2	20.5	23.3	26.1	34.8	45.9	31.2	23.1
Preference Dividend	73	48	33	35	35	40	0	0	0
Minority Interest	0	2	5	8	6	8	10	12	15
PAT for Equity Shareholders	**130**	**225**	**293**	**365**	**473**	**646**	**1,002**	**1,315**	**1,619**
Change (%)		74.0	30.1	24.5	29.5	36.7	55.1	31.3	23.1
Proposed Dividend	0	23	35	56	176	132	250	329	405

BALANCE SHEET									(INR Million)
Y/E MARCH	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Equity Share Capital	100	100	160	160	160	430	547	547	547
Reserves & Surplus	336	525	684	1,006	1,235	2,416	6,703	7,690	8,904
Networth	**436**	**625**	**844**	**1,166**	**1,395**	**2,846**	**7,250**	**8,236**	**9,451**
Minority Interest	24	40	66	92	98	105	115	127	142
Other Capital Instruments	835	935	935	935	955	975	0	0	0
Borrowings	**4,563**	**6,278**	**9,292**	**13,270**	**16,665**	**17,564**	**20,536**	**26,561**	**34,131**
Change (%)		37.6	48.0	42.8	25.6	5.4	16.9	29.3	28.5
Other liabilities	**183**	**140**	**195**	**257**	**345**	**522**	**678**	**882**	**1,147**
Change (%)		-23.5	38.7	32.3	34.0	51.3	30.0	30.0	30.0
Total Liabilities	**6,040**	**8,018**	**11,331**	**15,720**	**19,458**	**22,011**	**28,579**	**35,806**	**44,870**
Loans	**4,430**	**6,011**	**9,226**	**13,220**	**17,249**	**21,093**	**27,312**	**34,131**	**42,664**
Change (%)		35.7	53.5	43.3	30.5	22.3	29.5	25.0	25.0
Investments	**1**	**1**	**1**	**3**	**3**	**0**	**0**	**0**	**0**
Net Fixed Assets	62	61	58	46	82	87	101	116	133
Other assets	1,548	1,945	2,046	2,450	2,124	831	1,166	1,559	2,073
Total Assets	**6,040**	**8,018**	**11,331**	**15,720**	**19,458**	**22,011**	**28,579**	**35,806**	**44,870**

Assumptions	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**	**2020E**
AUM (INR M)	**7,137**	**10,532**	**14,563**	**20,996**	**26,999**	**33,326**	**42,019**	**52,509**	**65,637**
Change (%)		47.6	38.3	44.2	28.6	23.4	26.1	25.0	25.0
On Balance Sheet		62.0	57.4	63.8	63.4	64.4	63.6	65.0	65.0
Off Balance Sheet		38.0	42.6	36.2	36.6	35.6	36.4	35.0	35.0

E: MOSL Estimates

Financials and valuations

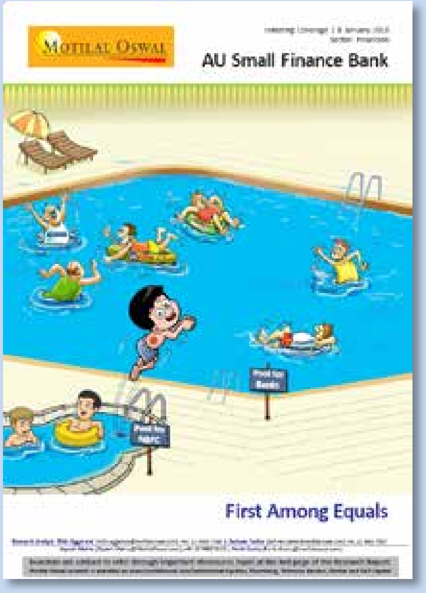
RATIOS									
Y/E MARCH	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Spreads Analysis (%)									
Yield on loans	22.6	24.2	22.0	19.1	18.1	17.4	17.4	17.0	17.0
Cost of Funds	9.6	10.3	10.1	9.9	9.5	9.6	9.0	8.8	8.5
Spreads (On books)	13.0	13.9	11.9	9.2	8.6	7.8	8.4	8.3	8.5
NIMs (On AUM)		8.0	7.2	5.9	5.7	5.7	6.6	6.7	6.7
Profitability Ratios (%)									
RoE		42.5	39.9	36.3	36.9	30.5	19.8	17.0	18.3
RoA		3.21	3.03	2.70	2.69	3.12	3.96	4.09	4.01
RoA (on AUM)		2.55	2.34	2.05	1.97	2.14	2.66	2.78	2.74
Op. Exps./Net Income	47.5	43.7	39.4	35.8	36.9	33.5	31.0	30.7	31.0
Empl. Cost/Op. Exps.	29.7	34.8	35.0	37.8	40.8	43.7	43.8	43.9	44.0
Asset-Liability Profile (%)									
Net NPAs to Adv.	0.8	0.8	0.8	0.8	0.9	0.9	0.9	0.9	1.0
Debt/Equity (x) - On BS	12.4	11.5	12.1	12.2	12.6	6.5	2.8	3.2	3.6
Average leverage	12.4	11.9	11.9	12.2	12.4	8.5	3.9	3.0	3.4
CAR	24.5	22.5	19.0	18.1	18.3	23.0	28.8	26.1	24.0

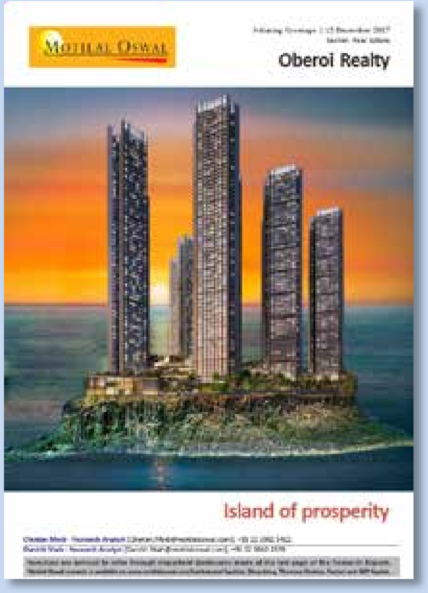
Valuations	2012	2013	2014	2015	2016	2017	2018E	2019E	2020E
Book Value (INR)	43.6	62.5	52.8	72.9	87.2	66.2	132.6	150.7	172.9
Price-BV (x)						9.4	4.7	4.2	3.6
Adjusted BV (INR)	39.8	56.3	47.4	65.4	76.7	63.8	130.2	147.5	168.9
Price-ABV (x)						9.8	4.8	4.2	3.7
EPS (INR)	13.0	22.5	18.3	22.8	29.5	15.0	18.3	24.1	29.6
EPS Growth (%)		74.0	-18.7	24.5	29.5	-49.1	21.9	31.3	23.1
Price-Earnings (x)						41.6	34.1	26.0	21.1

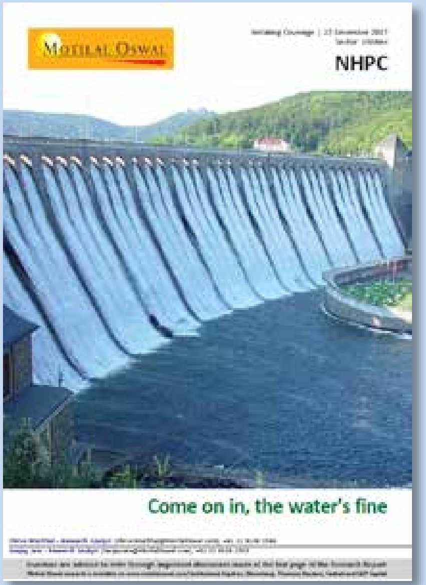
E: MOSL Estimates

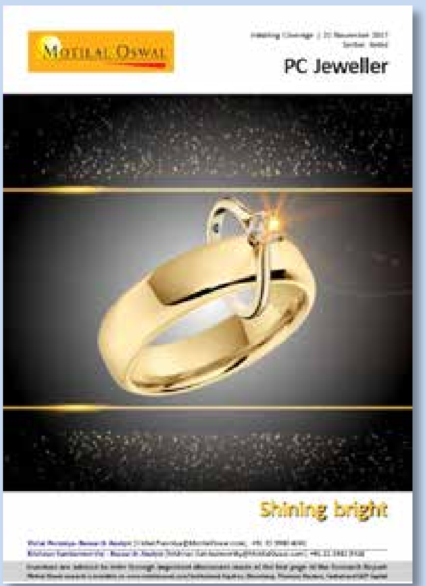
REPORT GALLERY

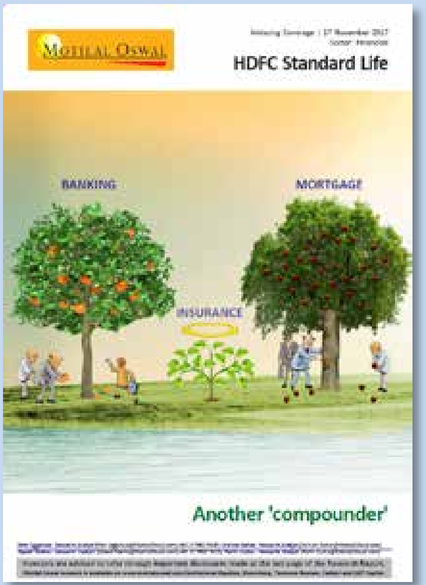
RECENT INITIATING COVERAGE REPORTS











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