Muthoot Finance (MUTH IN)

Rating: BUY | CMP: Rs1,152 | TP: Rs1,364

Paragon of gold lending

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December 1, 2020

Company Initiation

Key Financials - Standalone

Y/e Mar	FY20	FY21E	FY22E	FY23E
Net Int.Inc. (Rs m)	57,735	66,639	77,133	89,706
Growth (%)	*27.7*	*15.4*	*15.7*	*16.3*
Op. Profit (Rs m)	41,531	50,163	57,904	66,667
PAT (Rs m)	30,183	36,367	42,340	48,874
EPS (Rs.)	75.3	90.7	105.6	121.9
Gr. (%)	*52.9*	*20.5*	*16.4*	*15.4*
DPS (Rs.)	15.0	14.0	15.0	16.0
Yield (%)	*1.3*	*1.2*	*1.3*	*1.4*
Margin (%)	*14.9*	*14.7*	*14.2*	*14.0*
RoAE (%)	*28.3*	*25.0*	*23.4*	*22.0*
RoAA (%)	*6.8*	*6.7*	*6.5*	*6.2*
PE (x)	15.3	12.7	10.9	9.5
P/BV (x)	4.0	3.2	2.6	2.1
P/ABV (x)	4.0	3.4	2.7	2.2

Key Data	MUTT.BO | MUTH IN
52-W High / Low	Rs. 1,406 / Rs. 477
Sensex / Nifty	44,150 / 12,969
Market Cap	Rs. 462 bn/ $ 6,241 m
Shares Outstanding	401m
3M Avg. Daily Value	Rs. 5287.33m

Shareholding Pattern (%)

Promoter's	73.40
Foreign	13.92
Domestic Institution	7.71
Public & Others	4.97
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	(7.8)	36.5	66.4
Relative	(15.4)	(2.3)	54.6

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We initiate coverage on Muthoot Finance (MUTH), with a BUY rating as it is a 1) market leader (18% market share) and proxy play on gold financing market in India 2) carries robust capital (Tier I of 24%) 3) maintains low leverage(4x) and 4) comes at reasonable valuations at 2.2xPBV (FY23E). We expect MUTH to maintain market leadership in gold lending underpinned by pricing power, improved productivity and insulation from underlying collateral price fluctuations. A low risk (0.3% credit costs/ 2% NPA), high return business (RoA/RoE: 6%/22%), MUTH is expected to clock healthy growth momentum (19% CAGR) over FY22-23 defying pandemic challenges. We recommend BUY based on SoTP metrics assigning PBV multiple of 2.6x to core book at Rs1,330 value per share and subsidiaries at Rs34 per share arriving at price target of Rs 1,364.

- **Pandemic and gold price momentum place MUTH in sweet spot; 19% AUM CAGR:** We expect MUTH to clock 19% consolidated AUM CAGR (19% gold CAGR, 25% non-gold) over FY21-23E led by: (a) buoyancy in gold loan business during pandemic as other asset classes suffer (b) tailwinds of steady gold price momentum (c) aggressive marketing initiatives positioning gold loan as a push product (d) non-South geographic expansion and (e) granular book focus with non-gold expansion (gold: non-gold mix at 80:20 over 3-5 years).

- **Pricing power to be maintained; steady NIMs:** While gold price uptick aids yield expansion and higher realizations, MUTH's spreads (~11% spreads over FY15-20) are relatively stable to price fluctuations given its pricing power. Despite high competitive intensity and slower non-gold uptick, NIMs are expected to stabilize at ~14.3% over FY21-23E led by (a) customer stickiness and brand recall, (b) high churn model (60% of book runs off in < 6 months) (c) liquidity sufficiency (Rs79bn: Sep'20) (d) diversified borrowings backed by stable credit ratings and (e) comfortable ALM position.

- **Paring costs- operating leverage to play out:** MUTH's superior business productivity versus peers as reflected in double the AUM per branch (Rs85mn), higher AUMs/employee (Rs15mn) and avg opex/loan assets (~4.5%; 200-300bps lower than peer) continues to aid operating efficiencies. With meaningful investments in branch, brand, customer relationships and digital make-shift in place, we expect opex to AUM to decline from ~5% (5 year avg) to 4.1% over FY21-23E.

- **Premium asset quality- high return profile to stay:** With 90% business revolving around secured gold lending coupled with 75% LTV cap and highly liquid collateral, MUTH is expected to maintain low asset quality risk. Therefore, despite gold price fluctuations, ultimate credit losses for MUTH have been restricted to <10bps over past few years. We envisage 2.1% GNPA for standalone gold lending and 3-5% GNPAs for non-gold lending business over FY21-23E. While non-gold lending stands restricted to 10% of business mix and the core underlying demographics remaining healthy, MUTH's business stands resilient. MUTH's high margin and low asset quality risk oriented business model stands poised to clock 6%RoA/22%RoE by FY23E.

Story in Tables

Incorporated in 1997, Muthoot Finance Limited (Headquartered in Kerala) is the largest gold financing company (Rs523bn consolidated AUMs) with ~18% market share as of FY20. With 90% gold lending business share, MUTH boasts of robust 4,607 branch presence with 60% of network focused in South. To diversify its portfolio, Co. incorporated Muthoot Homefin and acquired Belstar Micro-Finance in 2017. While home finance (107 branches in 16 states) operates as a hub and spoke model in affordable housing segment, micro finance business (603 branches in 17 states) follows a Joint Liability Group model to provide income generating loans. To foray into CV financing, company acquired Muthoot Money Ltd (24 branches) in 2018.

Exhibit 1: AUM mix to remain tilted towards gold; AUM to growt at 19% CAGR over next 3 years

Consolidated AUM Mix (%)	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Gross AUM year-end (Gold)	**99.1%**	**99.0%**	**98.5%**	**98.9%**	**99.7%**	**99.8%**	**99.8%**	**90.4%**	**87.7%**	**87.0%**	**87.4%**	**87.9%**	**86.3%**
Non Gold AUM	**0.9%**	**1.0%**	**1.5%**	**1.1%**	**0.3%**	**0.2%**	**0.2%**	**10.4%**	**13.6%**	**13.9%**	**12.6%**	**12.1%**	**13.7%**
Loans against NCDs	0.8%	1.0%	1.4%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Home Loans	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	5.0%	4.2%	3.7%	3.6%	4.2%
MFI (Belstar)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	4.8%	5.6%	5.2%	5.0%	5.9%
Asia Asset Finance	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.3%	1.1%	1.0%	1.0%	1.0%
Personal Loans	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.7%	1.8%	1.7%	1.6%	1.6%
Muthoot Money Limited	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.8%	1.1%	1.0%	1.0%	1.1%

Source: Company, PL

Exhibit 2: Geographic business share tilting towards non-South could be biggest growth trigger over next 3 years

Geographic AUM mix (%)	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
North									
AUM Mix	18%	19%	22%	22%	22%	23%	23%	23%	23%
Branch Mix	18%	17%	16%	16%	16%	17%	17%	17%	17%
South									
AUM Mix	67%	65%	59%	57%	54%	52%	50%	49%	49%
Branch Mix	64%	65%	65%	65%	64%	62%	62%	61%	60%

Source: Company, PL

Exhibit 3: Calibrated book expansion and granular book coupled to support stable business outlook

Key business parameters	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Gold Price per gram (Rs)	1,858	2,492	2,908	2,637	2,483	2,437	2,705	2,708	3,050	4,332	4,982	4,533	4,488
Gold AUM growth (%)	*114.2%*	*55.2%*	*6.5%*	*-16.9%*	*8.0%*	*4.2%*	*11.9%*	*6.0%*	*16.4%*	*21.4%*	*18.3%*	*24.6%*	*12.6%*
Tonnage Growth (%)	*72.3%*	*22.3%*	*-2.2%*	*-11.9%*	*11.0%*	*8.4%*	*4.9%*	*4.0%*	*9.0%*	*4.1%*	*11.9%*	*0.3%*	*14.7%*
Branch Growth (%)	*-*	*34.6%*	*11.0%*	*4.6%*	*-0.6%*	*0.7%*	*0.7%*	*0.4%*	*3.6%*	*1.9%*	*5.1%*	*1.8%*	*4.8%*
Yields (%)	*19.4%*	*27.1%*	*22.2%*	*20.2%*	*18.7%*	*20.0%*	*21.5%*	*21.6%*	*21.0%*	*22.1%*	*22.3%*	*22.0%*	*21.8%*

Source: Company, PL

Exhibit 4: Pricing power and controlled delinquencies to aid high quartile return profile

Profitability metrics	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Consol AUM (Rs mn)	**1,58,685**	**2,46,736**	**2,63,868**	**2,18,615**	**2,34,085**	**2,43,789**	**2,72,785**	**3,19,213**	**3,83,036**	**4,68,705**	**5,51,688**	**6,83,774**	**7,84,342**
Yields (%)	19.4%	27.1%	22.2%	20.2%	18.7%	20.0%	21.5%	21.6%	21.0%	22.1%	22.3%	22.0%	21.8%
CoF (%)	8.7%	15.1%	13.0%	12.1%	10.8%	11.9%	11.6%	9.2%	9.3%	8.7%	8.8%	8.9%	8.9%
NIM (%)	10.6%	12.9%	10.5%	9.3%	9.5%	10.6%	12.7%	14.9%	14.0%	14.9%	14.7%	14.2%	14.0%
Leverage (x)	**10.3**	**8.0**	**7.9**	**6.0**	**5.3**	**4.8**	**4.6**	**3.9**	**3.9**	**4.4**	**4.0**	**4.0**	**3.8**
NPA (%)	0.29%	0.56%	1.99%	1.90%	2.19%	2.88%	2.06%	4.42%	2.72%	2.16%	2.35%	2.11%	1.96%
ROA (%)	3.6%	4.8%	3.8%	2.8%	2.6%	3.0%	4.1%	5.8%	5.7%	6.8%	6.7%	6.5%	6.2%

Source: Company, PL

Investment Argument

MUTH at point of inflection

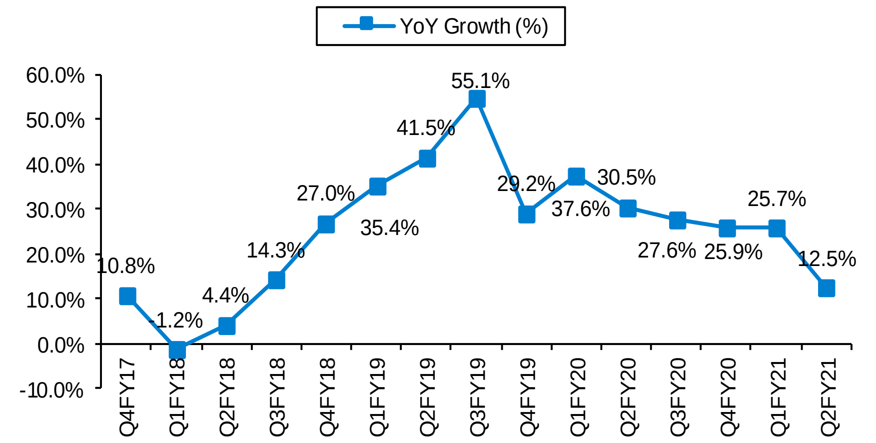
MUTH, today, stands at a point of inflection as pandemic related uncertainties and gold price momentum have been auguring well for the growth outlook of the company. Moreover, focused leadership and strong brand recall continues to defy competition and underlying asset volatility.

Macro tailwinds supportive of growth: Gold prices increased 30% the year so far and the momentum is expected to sustain led by (a) coronavirus uncertainty that continues to push the precious metal prices higher while underpinning its status as a safe haven (b) rising geopolitical tensions (c) tumbling real rates (d) weakening dollar and (e) logjam on COVID stimulus. While gold price momentum stands supportive of growth, MUTH's business model stands insulated from gold price fluctuations on the back of its proven track record of risk management.

Pandemic uncertainties putting unsecured credit products at risk in terms of asset quality and continued gold price momentum stands supportive of gold lending traction

Gold financing to outgrow other retail loans in light of pandemic: Latest RBI data suggests that unsecured loan growth stands in a negative zone. Retail loan growth has remained at 16-17% YoY over the past few quarters but gradually slowed down 11-12% post-Covid. The moratorium led uncertainties have compelled lenders turn cautious, as priorities shift to collections and liquidity maintenance over growth. Moreover, as bad loans are expected to rise by at least 400bps in FY21, lenders seem more comfortable with secured loans where chances of recovery are greater. Concurrently, in the last one month, gold loans saw robust 25-30% growth on month-on-month basis. According to KPMG (2019), India's gold loan market is expected to reach Rs4.62tn by 2022 at a five-year CAGR of 13.4%.

Exhibit 5: Falling unsecured credit, paving way for secured lending



Source: RBI, PL

Said that, COVID challenges are expected to see demand shift to gold loans in FY21 for personal and working capital requirements of individuals and small entrepreneurs respectively. Subsequently, niche financiers like MUTH and MGFL should prove greater beneficiaries.

MUTH at point of inflection defying competition: Where only 35-40% of the organized gold lending market is led by specialized gold finance NBFCs, competitive intensity have been part of the business for years. India, today possess 20,000 tonnes of gold but only about 2 tonnes of gold comes to the organized market. With new entrants and banks coming in, any volume increase will only aid market expansion.

As secured lending in light of pandemic gathered pace, competitive intensity have flared up in the gold lending market. Specialized gold financiers like MUTH typically faces competition from:

PSUs and private banks, so also new entrants and diversified NBFCs tend to be opportunistic players in the market and have observed to remain benign across periods. Unorganized market, although have intensified competition, collateral security, accuracy w.r.t collateral valuations and customer service are certain key parameters wherein specialized financiers have an edge

- **PSU banks** have started to shift focus towards retail loans in the absence of corporate loan growth. In a post-COVID reality, lenders are likely to shy away from unsecured lending and focus on the secured, well-collateralized gold loan product underpinned by increasing demand led by small entrepreneurs who seek to manage cash flows mismatch.

- **South-based private sector banks** which have 60-85% of their gold loan portfolio as loans against pledged ornaments are primary competitors to specialized gold financiers. However, their growth over the past 4-5 years has been restricted by a focus on other segments, slow growth in the overall balance sheet and geographical concentration in one or two states of South India.

- While opportunistic growth has led banks to focus on gold loans, the long term traction should remain benign as for these banks gold loans stand as means to priority sector requirements (PSL) with limited flexibility over loan turnaround time as against NBFCs.

- **New players foraying** into gold finance space have been equally opportunistic, but being diversified in nature gold financing never stood as a core business. Likes of SCUF, IIFL have witnessed benign growth traction. Bajaj Finance and few digital fintech players have observed pick-up in gold loans, yet long way to traverse in comparison with full-fledged focused players like MUTH, MGFL. To tackle such competition, MUTH has been scaling up digital vertical and focusing on customer convenience.

- Specialized gold financiers also face acute competition from **unorganized market** with latter constituting as high as 65% share. Gold loans being emergency in nature, higher LTVs backed unorganized lending have remained upbeat over the years.

With focus on customer centricity, MUTH's TAT stands at 30 minutes for new loans and 15 minutes for repeat loans. Such expertise and high operational intensive business nature place MUTH ahead of competition vis-à-vis banks

- Said that, armed with quicker loan processing capabilities, accuracy in gold valuations and auctioning, security, and easy accessibility with entrenched branch network and comfort and confidence in transparent practices of specialized gold financiers would continue to see customers shifting to organized from unorganized sector.

With roughly 18% market share in the organized gold lending market, MUTH continues to maintain dominant position with its extensive pan-India footprint, expertise, high share of repeat customers and strong brand visibility.

Exhibit 6: Dominance of MUTH and MGFL in gold loan market (FY20)

Banks/NBFCs/SFBs (Rs mn)	Gold Loans	AUM	*as a % of total AUM*	Interest rates	Loan tenure
SBIB	21,790	2,32,52,900	*0.1%*	7.50%	upto 36 months
HDFC Bank	54,300	49,44,010	*1.1%*	9.9%-17.9%	3-24 months
ICICI Bank	1,29,058	64,52,900	*2.0%*	10.0%-19.76%	3-12 months
Federal	93,010	12,41,530	*7.5%*	8.5%	NA
South Indian Bank	17,460	2,11,730	*8.2%*	NA	NA
Bandhan Bank	2,219	7,18,460	*0.3%*	11.0%-18%	NA
IIFL	91,082	3,79,510	*24.0%*	12%	Upto 11 months
SCUF	31,190	2,90,850	*10.7%*	NA	NA
BAF	15,575	11,34,171	*1.4%*	NA	NA
MGFL	1,69,672	2,52,252	*67.3%*	12%-29%	3 months onwards
MUTH	4,07,724	4,16,106	*98.0%*	12%-27%	NA
Total	**10,33,081**				

Source: Company, PL

AUM to clock 19% CAGR over FY21-23

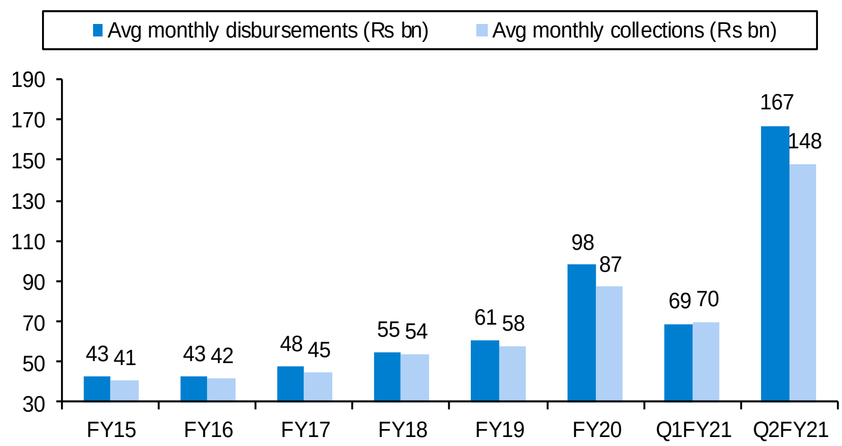
MUTH's well established market position and its track-record in the niche gold loan business segment has enabled it to maintain healthy 3 year AUM CAGR of 21% to Rs468.7bn as at Mar'20. The gold loan book grew at 19% CAGR while non-gold segments registered 40% CAGR over similar period, albeit on a smaller base over past 3 years.

Increasing branch additions, expanding repeat customer base and online gold lending push has enabled MUTH to record higher order disbursements during pandemic periods

Strong level of disbursements: MUTH recorded a healthy 18% CAGR in avg. monthly disbursements over past 5 years. While funding constraints implied slower traction of 11%YoY growth during FY19 post ILFS fiasco, the same jumped to 61% growth YoY as at FY20-end once the liquidity eased. With more than doubling of average monthly disbursements to ~Rs100bn over FY15-FY20, FY20 recorded consistent traction led by liquidity easing, diversified liability profile and gold price momentum. Q3FY20 saw highest sequential growth of 34% with disbursements climbing to Rs90bn+. However, the momentum slowed to 8%QoQ in Q4FY20 due to lockdown-related disruptions. With 100% branch opening in Q4 itself and footfalls up 60-70%, gold demand led by pandemic, repeat customer base (80%+) and online gold schemes would ensure continuity in disbursement traction ahead.

Q2FY21 monthly disbursements stood >3x of avg. disbursements of FY15-FY19 defying pandemic challenges

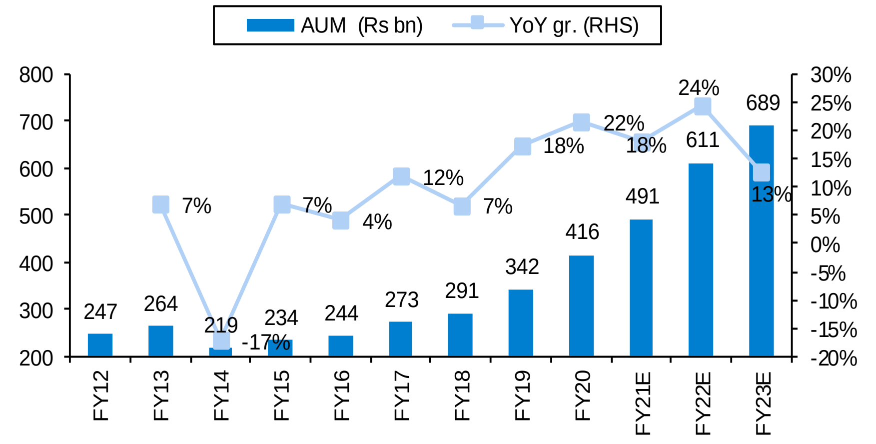
Exhibit 7: Improved monthly disbursements led by liquidity ease & gold price



Source: Company, PL

MUTH recorded 20% consolidated AUM CAGR over FY17-FY20 on increasing penetration into organized lending, substitution effect on gold loans due to tightening credit underwriting for small-ticket business and consumer loans, on the back of concerns over deteriorating asset quality and rally in gold prices. **Led by best asset class, easing funding access with diversification and higher share of core gold business (80:20 mix to be maintained over long term), we envisage another spell of similar growth traction and expect 19% consolidated AUM CAGR over FY21-23E.**

Exhibit 8: Defying pandemic challenges, AUM to grow at 19% CAGR



Source: Company, PL

Key determinants to healthy AUM CAGR:

Gold price momentum is one of the keys to gold lending traction. Pandemic uncertainties to ensure sustenance of the same as the world finds safe-heavens into yellow metal

- **Gold price momentum:** Historically, there remains strong co-relation between growth in gold loans and movement in gold prices. The continued increase in gold prices between FY08-FY12 saw emergence of many gold loan NBFCs with few witnessing AUMs exceeding Rs100bn in FY12, as depicted in the data hereunder. The same period also saw MUTH clocking stellar 83%CAGR in gold loan AUMs with yields climbing 22%+. However, tables turned in FY12 as gold prices plunged, LTVs stood capped and cap on borrowings (maximum borrowing upto INR 2.5 mn) dampened business performance. While AUM growth momentum slowed, concurrently branch addition too declined. Return in normalcy in FY19 saw AUM growth renewed at 16%+ levels with branch network resuming to expansion mode. Gold price tailwind continues to reflect in loan momentum with an avg 19% growth over FY19-20. We believe continued gold price momentum backed by improved liquidity to clock 20% gold AUM CAGR over FY20-23E. Defying pandemic challenges, improved branch traction and productivity with sustained gold loan demand would help record healthy 17% growth in tough year of FY21.

Exhibit 9: AUM traction tracking gold price momentum

	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Gold Price per grm (Rs)	**862**	**1,100**	**1,232**	**1,550**	**1,858**	**2,492**	**2,908**	**2,637**	**2,483**	**2,437**	**2,705**	**2,708**	**3,050**	**4,332**	**4,982**	**4,533**	**4,307**
YoY Growth		*27.5%*	*12.0%*	*25.9%*	*19.9%*	*34.1%*	*16.7%*	*-9.3%*	*-5.8%*	*-1.9%*	*11.0%*	*0.1%*	*12.6%*	*42.0%*	*15.0%*	*-9.0%*	*-5.0%*
MUTH																	
Gold AUM (Rs bn)	14	22	33	73	157	244	260	216	233	243	272	288	336	408	480	591	686
YoY Growth		*53.4%*	*51.5%*	*122.5%*	*114.2%*	*55.2%*	*6.5%*	*-16.9%*	*8.0%*	*4.2%*	*11.9%*	*6.0%*	*16.4%*	*21.4%*	*17.8%*	*23.0%*	*16.1%*
Gold Holdings (in tonnes)	23	30	39	65	112	137	134	118	131	142	149	155	169	176	195	192	201
YoY Growth		*30.4%*	*30.0%*	*66.7%*	*72.3%*	*22.3%*	*-2.2%*	*-11.9%*	*11.0%*	*8.4%*	*4.9%*	*4.0%*	*9.0%*	*4.1%*	*11.0%*	*-1.6%*	*4.6%*
MGFL																	
Gold AUM (Rs bn)	4	6	10	26	64	96	99	82	92	101	111	117	130	170	199	232	279
YoY Growth		*51.6%*	*70.6%*	*165.3%*	*143.3%*	*51.0%*	*3.4%*	*-18.0%*	*13.0%*	*9.4%*	*10.4%*	*5.5%*	*10.4%*	*30.9%*	*17.0%*	*17.0%*	*20.0%*
Gold Holdings (in tonnes)					53	66	51	46	53	60	61	64	68	72	80	89	NA
YoY Growth						*23.8%*	*-21.5%*	*-11.4%*	*16.5%*	*12.2%*	*2.5%*	*4.7%*	*5.5%*	*7.3%*	*10.0%*	*11.5%*	*NA*

Source: Company, PL

Calibrated ticket size increase led by continuous network expansion and customer retention aids gold loan book growth. Gold price momentum is an added advantage that cushions tonnage growth in turn boosting gold lending

Past two quarters, tonnage has been de-growing as new loans are more of shorter tenure and priced at new LTV

- **Granularity in portfolio:** Granularity of the book lies in calibrated increase in ticket size, largely emanating from network expansion, customer addition and retention and underlying macros. MUTH has witnessed avg.6% gold tonnage growth over past 5 years, followed by 9%CAGR in ticket size and subsequent 12%CAGR in gold loans over the same period. While gold price momentum stood healthy mostly, the gold loan traction stood intact. MUTH observed 30% increase in ticket size over past two years led by buoyant gold price momentum and steady customer (5% CAGR) and branch network expansion (3% CAGR). We believe FY21 should also reflect similar trends with stead-state ticket size expansion. FY22, however, should observe marginal increase.

Exhibit 10: Calibrated ticket size improvement aiding growth expansion

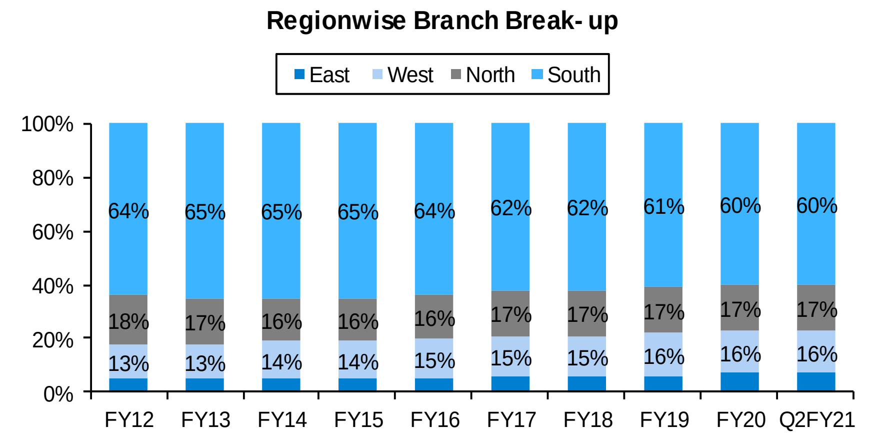
MUTH	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	Q1FY21	Q2FY21
ATS (Rs)	40,000	41,120	38,931	37,000	36,000	37,000	40,000	42,478	50,000	54,482	61,727
YoY Growth		*2.8%*	*-5.3%*	*-5.0%*	*-2.7%*	*2.8%*	*8.1%*	*6.2%*	*17.7%*	*NA*	*NA*
LTV	60.0%	NA	NA	72.0%	64.0%	67.0%	66.0%	68.0%	58.0%	55.0%	61.0%
Gold Price per grm (Rs)	2,492	2,908	2,637	2,483	2,437	2,705	2,708	3,050	4,332	4,448	4,621
YoY Growth		*16.7%*	*-9.3%*	*-5.8%*	*-1.9%*	*11.0%*	*0.1%*	*12.6%*	*42.0%*	*42.3%*	*33.9%*

Source: Company, PL

Reducing geographic concentration risks and tapping the high potential profitable markets, MUTH has been pushing gold loan product as an alternate alongside other retail lending offerings by other institutions

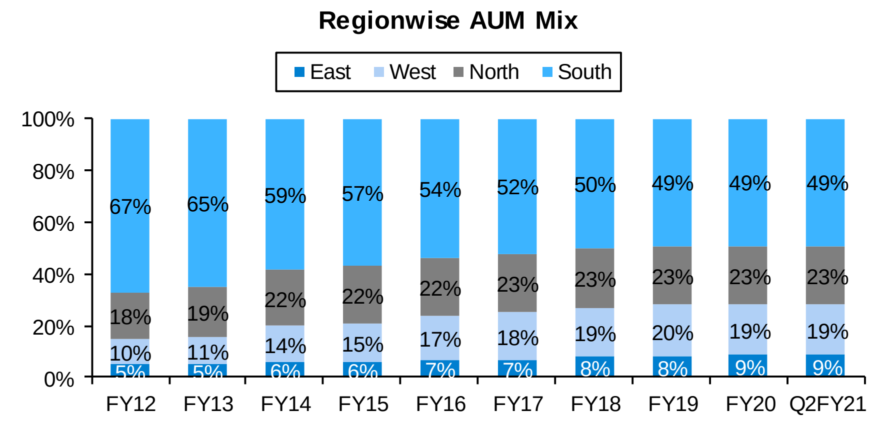
- **Nimble footed presence in non-south belt:** MUTH's meaningful presence in Southern belt (60% of the branches and 49% of AUMs as of 31st Mar'20) over the years has enabled the Co. to cash-in on largest gold market (South accounts for 40% of India's annual gold demand) in India. MUTH stood nimble footed with quicker expansion outside home turf as well. Back in Mar'13-Mar'18, Southern regional network declined from 65% to 50% as the Co. lost to competition for a brief period of FY13-FY14. Said that, in the process, Co. chose to untap newer markets posing gold as a push product led by marketing campaigns and building customer service quality. Resultantly, period between FY16-FY20 saw non-South contribution to overall branch share climbing from 35% to 40% and AUM share rising from 43% to 51%. Going forward, banking on existing branch & customer network in southern belt and continued expansion into untapped markets, MUTH is expected to maintain market leadership.

Exhibit 11: Presence in high profitable regions of North & West on rise



Source: Company, PL

Exhibit 12: Non-southern contributed 51% to AUMs as at FY20-end

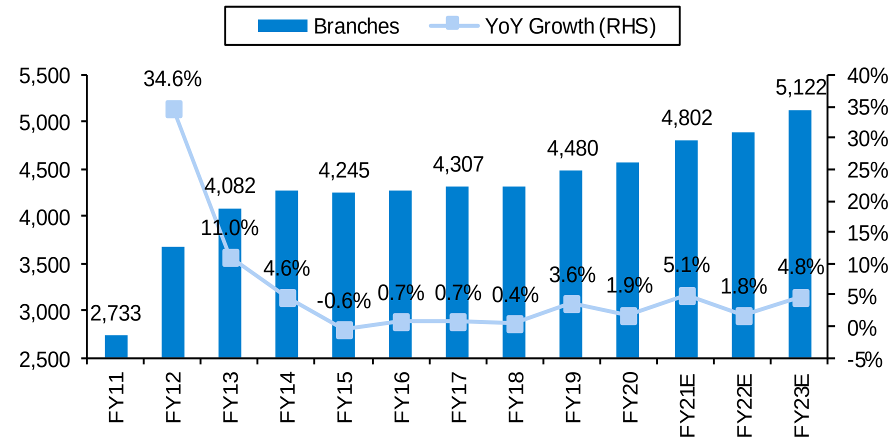


Source: Company, PL

Gold lending model stands branch centric. Higher the presence, higher the business augmentation. A strong network and better productivity can compensate for lower volumes (gold tonnage) maintaining gold book traction

- **Steady branch expansion into newer markets & newer businesses:** Gold business, typically, being branch centric model, MUTH has garnered higher business volumes with continuous branch expansion. Back during FY09-FY13, while the branch network expanded ~4x, business grew ~8x. Over past 5 years, MUTH observed a calibrated expansion in footprint with addition of 300+ branches translating into 1.7x increase in business. Going forward, we expect incremental 500+ branch count addition over FY21-23 as Co. penetrates into newer markets and expands into newer businesses.

Exhibit 13: Incremental branch expansion to emerge from newer markets



Source: Company, Company, PL

Exhibit 14: Steady-state branch expansion into newer businesses

	FY17	FY18	FY19	FY20	Q2FY21
Belstar					
Branches	155	235	400	603	618
YoY Growth		*52%*	*70%*	*51%*	*24%*
Muthoot Money					
Branches	0	1	21	24	18
YoY Growth			*2000%*	*14%*	*-25%*
Muthoot Home Finance					
Branches	9	19	96	107	108
YoY Growth		*111%*	*405%*	*11%*	*5%*

Source: Company, PL

That MUTH operates out of same number of branches (4567) as its immediate competitor MGFL (4622), former boasts 3x higher business than that of MGFL.

Exhibit 15: MUTH garners 3x of higher gold business of MGFL's

MUTH	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Branch (Units)	2,733	3,678	4,082	4,270	4,245	4,275	4,307	4,325	4,480	4,567	4,802	4,887	5,122
YoY Growth		*34.6%*	*11.0%*	*4.6%*	*-0.6%*	*0.7%*	*0.7%*	*0.4%*	*3.6%*	*1.9%*	*5.1%*	*1.8%*	*4.8%*
Gold Holding/Branch (Kg)	41	37	33	28	31	33	35	36	38	39	41	40	44
YoY Growth		*-9.1%*	*-11.9%*	*-15.8%*	*11.7%*	*7.6%*	*4.1%*	*3.6%*	*5.3%*	*2.2%*	*6.4%*	*-1.5%*	*9.4%*
Gold AUM per Branch (Rs mn)	58	64	64	51	55	57	63	67	75	89	85	99	117
YoY Growth		*10.7%*	*0.0%*	*-20.5%*	*8.7%*	*3.5%*	*11.0%*	*5.5%*	*12.4%*	*19.1%*	*-4.9%*	*16.2%*	*18.9%*

Source: Company, PL

A marketing push model, MUTH has been encouraging customer centric approach through varied offerings such as online gold, tailor-made gold schemes, recent Loan@Home product (issue gold loans without customers having to leave their houses), gold unlocker (gold remains in customer lockers and stands insured, free COVID insurance cover (Rs 1lakh) for new customer

- **Customer traction and digital pick-up:** MUTH primarily follows a branch led model guided by steady customer footfalls. MUTH boasts of 80%+ repeat customer base for its gold business which is indicative of customer stickiness. From marketing pull to marketing push, the Co. has come a long way with innovative product schemes that are tailor-made for customer needs, service quality digitisation initiatives through online gold loans positioning gold loan as an attractive lending product to retail customer base. The most lucrative being the online gold loans which enable customers to withdraw amounts from their accounts within the sanctioned limit at their convenience. MUTH observed 105bps expansion in online customer expansion over FY17-FY20. While

Q2FY21 saw MUTH focusing on inactive and new customers with disbursements to 4 lakh customers in each category

pandemic challenges stood arduous, the Jun'20 period saw renewed footfalls to ~60-70% of pre-Covid levels. Q2FY21 witnessed strong addition of new customers (up 18% YoY), 92% QoQ growth in customer footfalls, 50% growth on mobile applications (4x jump in loan disbursals in Q1FY21 on mobile app) and 100% growth in online gold loan disbursements led by increasing focus on activating inactive customers. Going forward, gradual improvement in footfall and pick-up in digital gold loans will continue to support growth.

Exhibit 16: Steady customer traction over past 2 years barring H1FY21

	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
No.of customers	47,21,243	48,51,024	48,57,129	48,95,029	49,33,886	47,45,491	48,28,505
QoQ (%)		*3%*	*0%*	*1%*	*1%*	*-4%*	*2%*

Source: Company, PL

Exhibit 17: 45% fresh loans with new collaterals and 28% fresh loans to new customers in pandemic quarter stand credible

Customer mix(%)	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Fresh Loan to Inactive Customers	25.0%	25.2%	24.3%	25.4%	25.1%	26.1%	27.3%
Fresh Loan to New Customers	23.7%	23.5%	23.0%	23.8%	24.7%	22.5%	28.2%
Fresh loan with new collateral to existing customers	51.3%	51.3%	52.8%	50.8%	50.1%	51.4%	44.5%

Source: Company, PL

As against 40% business CAGR over FY18-FY20, non-gold businesses are expected to clock 25% CAGR over FY21-23 on account of pandemic led uncertainties

- **Calibrated growth in subsidiaries:** MUTH's foray into high profitable businesses of micro finance, vehicle finance and home finance can bolster overall business traction. Proven operating systems, huge customer base, established brand name, capable business team and robust risk management practices place MUTH favorably to chase next phase of growth. The synergistic RoE accretive non-gold businesses carry potential to record 25% AUM CAGR over FY21-23E underpinned by: (i) Leveraging existing customer base and (ii) Improved branch expansion & productivity.

Exhibit 18: Non-gold business dynamics

Loan Book (Rs mn)	FY17	FY18	FY19	FY20	YoY gr. (%)
Muthoot (Parent)	**2,72,785**	**2,91,420**	**3,42,461**	**4,16,106**	***21.5%***
Susbidiaries	10,167	25,970	37,494	46,079	*22.9%*
Homefin	4,408	14,589	19,075	19,769	*3.6%*
Belstar	5,759	11,381	18,419	26,310	*42.8%*
Susbidiaries to parent (%)	*3.7%*	*8.9%*	*10.9%*	*11.1%*	*0.1%*
PBT (Rs mn)					
Muthoot (Parent)	19,210	8,194	7,942	10,974	*38.2%*
Susbidiaries	213	142	390	310	*-20.5%*
Homefin	53	70	87	5	*-94.3%*
Belstar	160	72	303	305	*0.7%*
Susbidiaries to parent (%)	*1.1%*	*1.7%*	*4.9%*	*2.8%*	*-2.1%*
Networth (Rs mn)					
Muthoot (Parent)	65,164	78,120	97,928	1,15,718	*18.2%*
Susbidiaries	1,785	3,335	7,944	9,238	*16.3%*
Homefin	882	2,079	3,942	4,260	*8.1%*
Belstar	903	1,256	4,002	4,978	*24.4%*
Susbidiaries to parent (%)	*2.7%*	*4.3%*	*8.1%*	*8.0%*	*-0.1%*

Source: Company, PL

Q2FY21 witnessed 27%YoY/4%QoQ growth for MFI business with overall AUMs at Rs27bn forming 5% of consolidated AUMs

Belstar Micro finance: MUTH carries out its MFI operations through its subsidiary – Belstar Microfinance – in which it owns 70% stake. Belstar posted 65% AUM CAGR over FY17-20 As at FY20, Belstar's AUM stood at R26.8bn growing 43% YoY. The pace of growth has gradually slowed down over the past few quarters. On the back of Covid-19 related disruptions, the company will focus on collections in the next few quarters. Going ahead, disbursements will gradually revive over the next few quarters although normalization is still away. Against this backdrop, we expect the microfinance business to report 27% CAGR over FY21-23 as against 52% CAGR over FY18-FY20.

Q2FY21 witnessed 8%YoY/2%QoQ de-growth for home finance with overall AUMs at Rs19bn forming 4% of consolidated AUMs

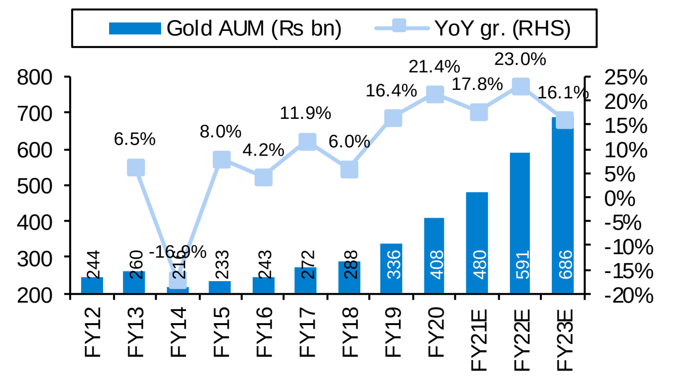
Muthoot home finance: Muthoot HomeFin (MHIL), a wholly owned subsidiary of MUTH, focuses on affordable housing loans and targets customers in Economically Weaker Sections (EWS) and Lower Income Groups (LIG) in Tier II/III locations. The company extends loans with average ticket size of ~Rs1 mn. Adopting feet-on-street mdoel for sourcing, Co. banks upon existing branch network. Case in point being, ~10% of incremental monthly disbursements happen through gold loan branches. Owing to concerns over asset quality in select geographies (like Surat), MHIL had slowed down disbursements 3QFY20 onwards. 4QFY20 witnessed overall disbursements declining 67%YoY followed by 45%YoY decline in Q1FY21 and as high as 92%YoY decline in Q2FY21. While near term focus remains on collections, we expect muted loan traction for FY21. Said that, FY22-23 is expected to be promising with bettering macro tailwinds and low base effect. Against this backdrop, we expect the home finance business to report 26% CAGR over FY21-23 as against 16% CAGR over FY18-FY20.

Muthoot Money: Muthoot Money, a wholly owned subsidiary of MUTH, commenced operation from Oct'18. The Co. is involved in extending loans for commercial vehicles, equipment and cars with operations centered in Hyderabad. As macros turn vulnerable, the vehicle finance subsidiary has reported deceleration in AUMs since two quarters in a row with loan assets declining 2% in Q1FY21 and 7% in Q2FY21. Against this backdrop, we expect the vehicle finance business to report 25% CAGR over FY21-23 as against 64% YoY growth over FY19-FY20.

The vehicle finance business clocked 9%YoY growth but 7% QoQ de-growth for Q2FY21; forms mere 1% of the overall consolidated business

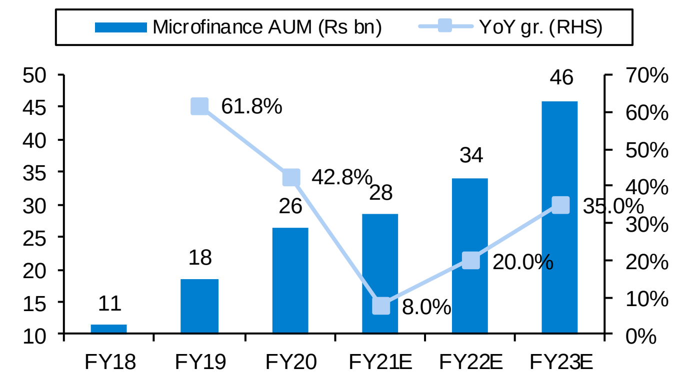
MUTH's ability to grow the non-gold loan portfolio profitably would be critical over the medium term as share of non-gold business is expected to increase to 15-20% over next 5 years from 13% in Dec'19. As at the end of Sep'20, the non-gold share declined to 10% of overall Co. AUMs as incremental focus largely remained centered around gold financing. Non-gold financing portfolio to face near term disruptions given the vulnerability of underlying customer segment; particularly, microfinance and vehicle finance, to Covid-19. Against this backdrop, we expect non-business to clock 25% CAGR over FY21-23 as against 40% over FY18-20.

Exhibit 19: Gold AUM to expand 19% CAGR over FY21-23E



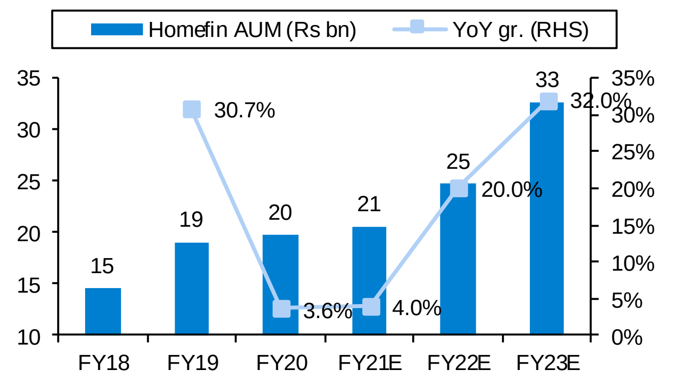
Source: Company, PL

Exhibit 20: Microfinance to record 27%CAGR over FY21-23E



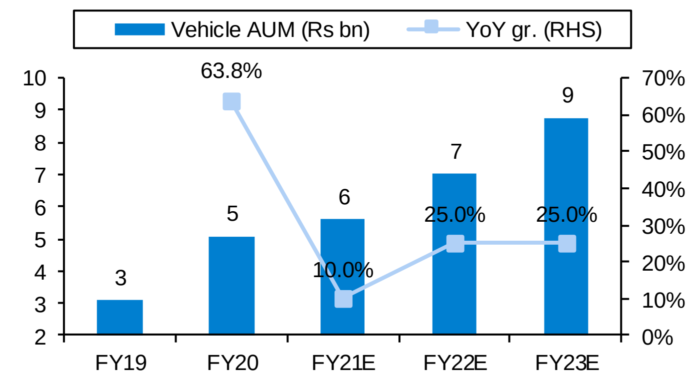
Source: Company, PL

Exhibit 21: Home finance to grow at 26%CAGR for FY21-23E



Source: Company, PL

Exhibit 22: Vehicle fin. to grow at 25%CAGR for FY21-23E



Source: Company, PL

Higher portfolio churn and regular interest collections have enabled MUTH tackle periods of gold price descent maintaining steady loan traction

Pricing power to be maintained; long terms NIMs stable

Theoretically, gold price momentum supports yield expansion and higher realizations (on gold auction). On similar lines, MUTH has witnessed yields climbing as high as 27% during high gold price period of FY12. On the flip side, Co. has also observed yield compression in FY14-FY15 when gold prices took a u-turn. Said that, MUTH observed steady-state yields momentum post FY15 onwards despite somber price movement (during FY16 and FY18) backed by pricing power.

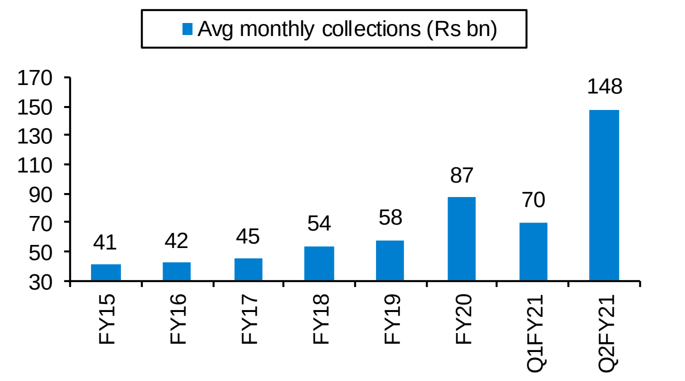
MUTH stands better placed over others owing to steady pricing power emanating from: (1) high churn model (2) easing liquidity challenges & sufficiency (3) comfortable ALM position (4) focus on diversification of borrowings backed by healthy credit ratings.

While MUTH maintains 12-month loan product model, the average tenure of the book stands at <5months with 60% of the book running off in <6 months

High churn model: MUTH maintains high churn model with greater focus on regular interest collections. While the overall gold loan tenure stands at 12 months, 60% of loans get repaid within six months. Such a high-churn portfolio backed by robust collections mechanism enables yield expansion for MUTH. Collections and auctions realization are relatively high during periods of high price which aid yield expansion. Over FY19-20, increased focus on collection of interest on a regular basis alongside revision in interest rates on different schemes, resulted in sustenance of margins. The net interest margin improved to 15.5% in 9MFY20 from 14% in FY19 due to improvement in the yields on account of settlement of overdue loans led by higher collections. Q4FY20-Q1FY21, however, witnessed dip in collections in light of COVID as Co. preferred loan tenure extension rather than auctions to protect customers' interests. While yields would stay benign in near term, such high tenure will attract penal interests.

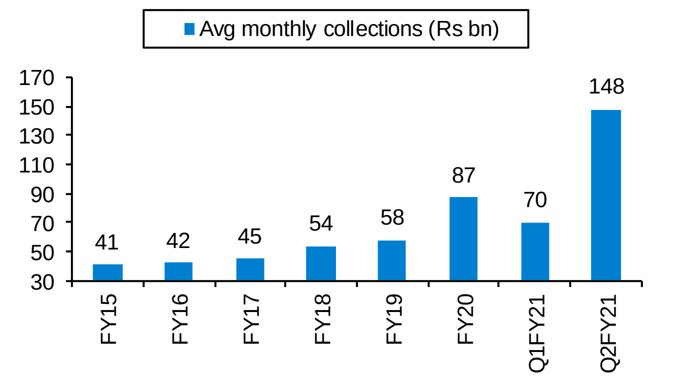
MUTH's disbursements and collections in the Sep'20 quarter exceeded their averages for the past five years

Exhibit 23: Improvement in avg monthly interest collections



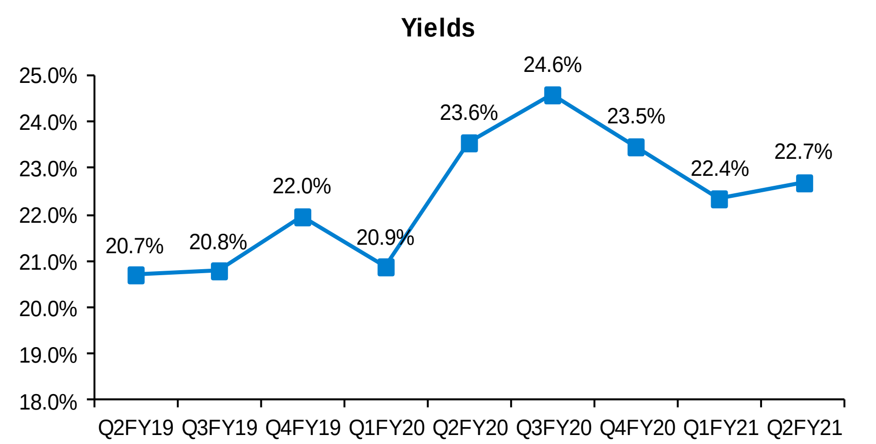
Source: Company, PL

Exhibit 24: Improved avg monthly disbursements



Source: Company, PL

Exhibit 25: Steady sequential yield trends barring peak COVID periods



Source: Company, PL

Liquidity challenges did reflect in flattish loan book of MUTH during H1FY20. Overall liquidity situation eased with increased bank lines and support through GOI/RBI liquidity schemes

Liquidity sufficiency and ease: Historically, MUTH has maintained 5-6% cash on BS especially since ILFS breakout. In light of COVID, the same stood at 10-11% levels over Q4FY20-Q2FY21. As on Sep'20 (excluding un-utilized portion of existing term loans, cash credit and working capital demand loans), Co's liquidity position remains adequate with cash and equivalents balance of ~Rs75bn. The repayment obligations over Sep'20-Feb'21 stand at Rs138bn of which Rs84bn is cash credit/short term loans from banks which is expected to be rolled over and

CPs/NCDs of ~Rs50bn. As at the end of Aug'20, MUTH held sizeable ~Rs8bn as undrawn working capital limits from banks. MUTH also witnessed meaningful increase in loan rollovers aiding improved cash collections and disbursements over past few months.

Exhibit 26: MUTH recent fund raising program indicative of easing liquidity

Issue Date	02-Mar	17-Mar
Issue Size	USD 550 mn	Rs. 60 bn
Coupon (%)	4.40%	
Type	Global Medium Term Note	NCDs Private placement

Source: Company, PL

Co. reported 1% sequential decline in loan growth during Q1FY21 on account of tightness in liquidity in Apr-May'20. Said that, loan growth renewed at healthy levels (14%QoQ/32%YoY) in Q2FY21 as liquidity challenges eased.

Comfortable ALM position: MUTH's ALM position is comfortable with no cumulative mismatch in all buckets up to 1 year as of FY20. According to its ALM profile, the company has outflows of Rs211bn up to 1 year and against this the expected inflows were Rs482bn. Of the inflows maturing within the 1-year bucket, 75% were due for maturity within 6 months and the company has serviced most of its obligations.

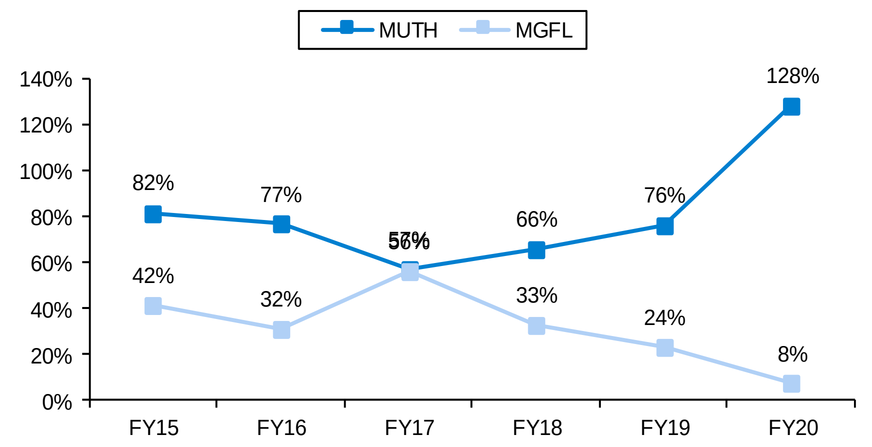
Despite being a short tenure high churn model, MUTH's <1 year bucket stands sufficiently healthy with inflows almost doubling the outflows

Exhibit 27: MUTH's ALM for short term 1 year bucket stands healthy

	FY15	FY16	FY17	FY18	FY19	FY20
Assets	95%	92%	98%	97%	95%	96%
Liabilities	65%	71%	79%	79%	73%	55%

Source: Company, PL

Exhibit 28: ALM mismatch gap: MUTH vs MGFL



Source: Company, PL

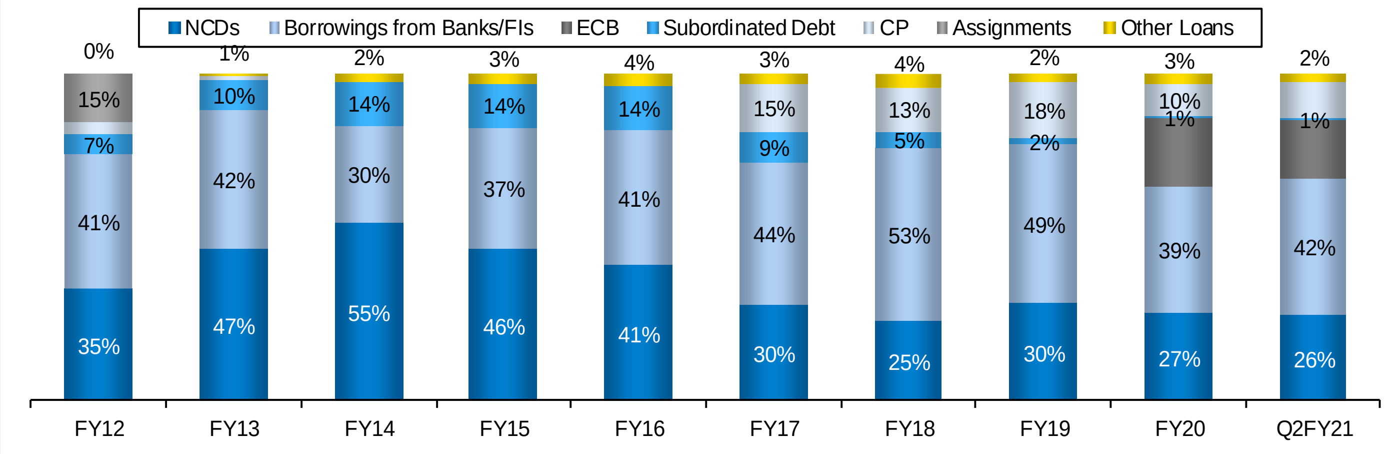
Focus on diversifying sources of borrowings: In terms of funding, while a larger proportion of borrowing has been sourced from banks and financial institutions (42%), the Co.'s resource profile remains diversified across avenues like non-convertible debentures and subordinated debt (28%), commercial paper (11%), external commercial borrowing (17%) and other sources (2%) as of Q2FY21. Notably, CP borrowing mix stands pared own to 11% from 18% a year ago being

While funding constraints have eased, borrowing rates are expected to stabilize

replaced by ECB borrowings that formed 17% of overall mix as at the end of FY20. MUTH has mobilized fresh resources through TLTRO.

While MUTH faced challenges on incremental funding during Apr-May'20, overall liquidity situation eased with increased bank lines and support through GOI/RBI liquidity schemes. While decline in cost of funds stood supportive of NIMs in H1FY21, the company should likely pass the funding side benefits to customers in order to support growth traction.

Exhibit 29: Borrowing mix begins to shift towards long term as liquidity stress eases



Source: Company, PL

Exhibit 30: Headroom for further leveraging

	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	Q2FY21
Outside Liabilities	2,37,817	2,56,806	2,13,293	2,16,857	2,14,295	2,41,966	2,29,802	2,82,759	3,88,878	4,40,401
Cash & Bank Balances	7,950	13,420	20,489	17,366	6,791	15,343	4,869	17,355	59,253	79,465
Tangible Networth	29,257	37,310	42,579	50,775	56,146	65,104	78,055	97,868	1,15,668	1,31,914
Capital Gearing	7.86	6.52	4.53	3.93	3.70	3.48	2.88	2.71	2.85	2.74

Source: Company, PL

Steady credit ratings: Even as squeeze in liquidity posed challenges in recent past, the company stands better placed than others due to AA credit rating across key debt instruments.

Exhibit 31: MUTH maintains superior credit rating enabling easier funding

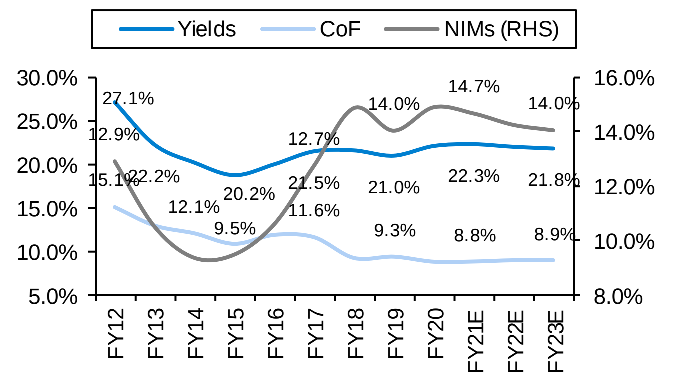
	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	Q2FY21
CPs	A1+	A1+	A1+	A1+	A1+	A1+	A1+	A1+	A1+	A1+
Bank Loans	AA-	AA-	AA-	AA-	AA	AA	AA	AA	AA	AA
NCDs	AA-	AA-	AA-	AA-	AA	AA	AA	AA	AA	AA

Source: Company, PL

MUTH is poised to maintain 14%+ NIMs over FY21-23 as yields stand poised to stay higher at 21.5% levels and borrowing costs steadying ~8.9%

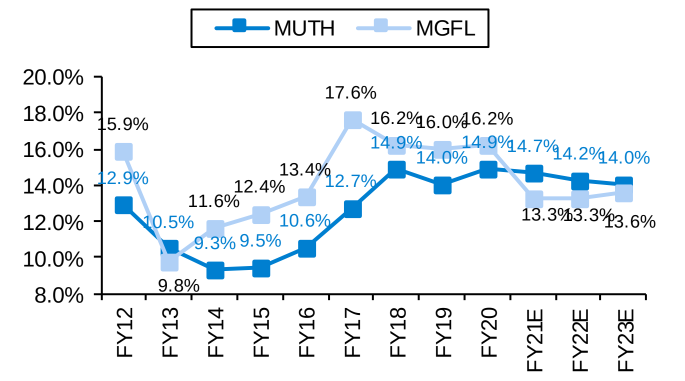
Given a positive asset-liability mismatch in the one-year bucket and a diversified borrowing mix, we model for stable spreads of ~13.4% in the gold finance business over FY21-FY23. In the pandemic led gold demand and continued gold price momentum could keep yields on higher side (~avg 22%) over FY21-22. However, the same should normalize FY23 onwards retreating back to <22% levels. While high cost borrowings have been curtailed, COVID-led challenges manifesting into risk aversion would keep funding costs in check. Against this backdrop, we expect marginal increase in borrowing cost to 8.8%+ in FY21E from current 8.4% (Q2FY21). As higher on-balance sheet liquidity gradually runs off, we expect calculated NIM to hover around ~avg 14.3% levels over FY21-23.

Exhibit 32: Margins to stabilize led by steady Yields



Source: Company, PL

Exhibit 33: MUTH stands better placed on margins due to pricing power



Source: Company, PL

Leveraging digital platform, recent branch set-up beginning to churn business and improving productivity both at business and employee levels should aid cost efficiencies over FY22-23

Cost efficiencies to drive RoAs

We reckon MUTH's gold finance business an opex intensive model with meaningful investments channeled into branch, brand, customer relationships, digital make-shift and security. As business volumes rise, major components of opex, namely; employee (largely variable; 58% of overall expense mix), rental (12% of overall expense) and advertisements/business promotion expenses (10% of overall expenses) increase in tandem. Over past few years the company has invested in advertising and publicity expenses to enhance brand recognition, as competition from smaller players and fintech companies gathered pace. While advertisement expenses dipped in Q1FY21 on account of lockdown effect, Q2FY21 witnessed these expenses reverting to 50% of the year ago levels. Rental costs continue to remain elevated gold financing being branch-led business model; H1FY21 saw 107 incremental branch addition. Past few years, MUTH has witnessed continued network expansion with diversification into microfinance, housing and vehicle financing businesses.

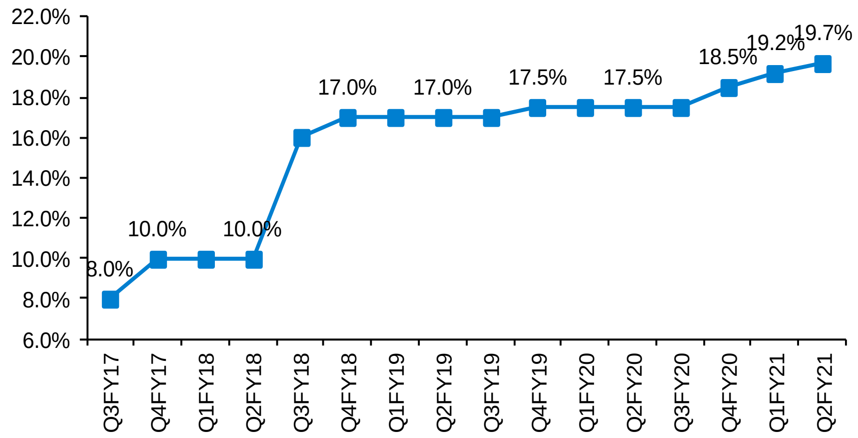
Exhibit 34: Overview of operational expense mix – Rent + advertisement form higher share next to salaries as part of opex

Particulars (Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Salaries and Wages	2,209	4,145	5,453	5,917	6,304	6,419	7,638	7,824	8,976	10,290
as a % of total opex	*46%*	*51%*	*56%*	*55%*	*55%*	*56%*	*61%*	*59%*	*58%*	*58%*
Rent	603	1,042	1,309	1,542	1,650	1,713	201	1,913	1,974	2,158
as a % of total opex	*12%*	*13%*	*14%*	*14%*	*14%*	*15%*	*2%*	*15%*	*13%*	*12%*
Advertisement	647	866	579	702	651	626	0	720	1,056	1,163
as a % of total opex	*13%*	*11%*	*6%*	*6%*	*6%*	*6%*	*0%*	*5%*	*7%*	*7%*
Business Promotion	119	267	332	279	140	149	61	209	477	553
as a % of total opex	*2%*	*3%*	*3%*	*3%*	*1%*	*1%*	*0%*	*2%*	*3%*	*3%*

Source: Company, PL

Increased digital initiatives supportive of customer centric model: Serving 2 lakh customers each day, MUTH's customer base predominantly comprises of individuals with no access to formal credit but who possess sizeable gold jewellery. The technology-centric business model of the specialized gold NBFCs have enabled paring down on manual tasks and leg-work oriented practices and migration towards automated processes leading to greater accessibility, cost-effectiveness, efficiencies in credit quality and turn-around times over the traditional lending models of banks and others. In-line with increased digital initiatives, Co. also launched online gold products in FY15 offering an online platform to make transactions and payments using Debit Card/Net Banking at customer's ease. While MUTH remains a branch focused model, the online customer traction has observed calibrated increase from 8% in Q3FY17 to ~20% as at the end of Sep'20.

Exhibit 35: Calibrated increase in on-line customer base



Source: Company, PL

We believe meaningful investments in branch, brand and technology has begun to translate into operating efficiencies for MUTH as reflected in improving branch and employee productivity.

MUTH generates 2.5x higher business per branch and 1.5x higher business per employee over MGFL despite both maintaining similar branch and employee count

Improved branch/employee productivity: Post tough period of FY12-14, MUTH clocked 10% CAGR in gold AUM per branch and 5% CAGR in gold held per branch during FY15-FY20. Such a value growth was recorded despite low branch network expansion (3% avg growth) during the same period of FY15-19. MUTH witnessing doubling of gold loan generation per branch in a span of 5 years from rs50mn in FY15 to Rs100mn+ in Q2FY21. Notably, MUTH's per branch business generation at ~Rs75-80mn (as at FY20-end) stands 2.5 times higher than the closest competitor MGFL despite both operating off same branch count. Over the years MUTH has demonstrated improving branch productivity that stands superior to its immediate competitor despite similar branch network and closer to similar salary structures. As depicted in the comparison metrics below, 5-6 employees per branch and similar branch network as competitor, MUTH has delivered almost 2x the business per branch and 1.5x business per employee.

Exhibit 36: Superior branch and employee productivity to begin reflect in operating efficiencies for MUTH

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
MUTH													
Employees / Branch	6.1	6.9	6.1	5.9	5.4	5.3	5.6	5.4	5.4	5.6	5.5	5.6	5.4
Average AUM / Branch (Rs Mn)	43.2	45.2	58.8	56.8	53.6	56.2	60.9	66.4	71.9	84.9	94.6	110.8	124.7
Average AUM / Employee (Rs Mn)	7.1	6.6	9.6	9.7	10.0	10.5	10.8	12.3	13.3	15.2	17.2	19.9	23.0
Average Salary / Employee (Rs Mn)	0.13	0.16	0.22	0.24	0.28	0.28	0.32	0.33	0.37	0.40	0.39	0.40	0.47
MGFL													
Employees / Branch	8.1	7.5	5.5	5.1	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
Average AUM / Branch (Rs Mn)	36.6	33.0	32.8	27.5	25.8	28.6	30.2	35.1	40.5	47.9	59.2	68.5	76.9
Average AUM / Employee (Rs Mn)	4.5	4.4	5.9	5.4	5.6	6.3	6.6	5.9	6.9	10.1	11.5	11.6	13.4
Average Salary / Employee (Rs Mn)	0.10	0.14	0.19	0.19	0.20	0.28	0.32	0.30	0.35	0.39	0.42	0.41	0.44

Source: Company, PL

We expect the operating expense at 18%CAGR to grow in tandem with book expansion CAGR at 19% over FY21-23

The opex CAGR halved from 24% during period FY11-FY15 to 12% between FY16-FY20. The opex pressure on P/L as measured by opex as % of PPoP declined from higher levels of avg.75% for FY11-FY16 to 48% during FY17-FY20. Incorporating COVID-led challenges prompting cost rationalization measures, the overall operating costs to exhibit only 6%YoY increase in FY21 from 16%YoY in FY20. That's also because MUTH benefitted from discounts on branch rentals for few months in light of COVID. Said that, as business environment stabilizes, investment in expansionary efforts will pick up pace FY22 onwards. Against this backdrop, we foresee calibrated increase in operating costs at 18%CAGR over FY21-23E.

Exhibit 37: Patterned increase in opex ahead; cost rationalization in place

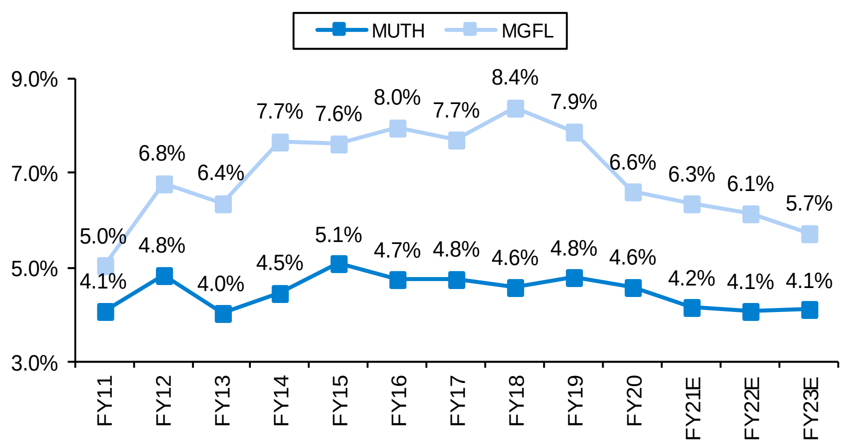
	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Opex (Rs mn)	8,059	9,667	10,841	11,533	11,381	12,503	13,174	15,394	17,787	18,852	22,080	26,175
YoY Growth		*20.0%*	*12.1%*	*6.4%*	*-1.3%*	*9.9%*	*5.4%*	*16.9%*	*15.5%*	*6.0%*	*17.1%*	*18.5%*
AUM (Rs mn)	2,46,736	2,63,868	2,18,615	2,34,085	2,43,789	2,72,785	2,91,420	3,42,461	4,16,106	4,91,423	6,11,461	6,89,402
YoY Growth		*6.9%*	*-17.1%*	*7.1%*	*4.1%*	*11.9%*	*6.8%*	*17.5%*	*21.5%*	*18.1%*	*24.4%*	*12.7%*

Source: Company, PL

Sizeable investments into branch, brand, customer relationships and digital make-shift leading to AUM expansion would imply marginal downtrend in opex to loan assets to avg. 4.1% over FY21-23E from ~5% over past five years. As compared to closest competitor MGFL, MUTH has maintained ~200bps lower opex-loan assets indicative of better operational efficiencies.

MUTH's opex/assets ratio has stood ~200bps lower than MGFL across periods

Exhibit 38: Low cost model, MUTH exhibits lower opex-assets vs peer



Source: Company, PL

Superior asset quality; subsidiaries closely watched

<1% write-offs as % of loans, mere 0.5% customers abandoning gold and LTVs ranged at ~60% have restricted NPAs at <2% levels for MUTH across periods

MUTH has maintained superior asset quality despite gold price fluctuations owing to (i) regular interest collections, (ii) high churn model (60% of the loans get repaid in less than six months), (iii) high collateral value, (iv) high sentimental value associated with the collateral (only 0.5% of customers abandon their gold) and (v) cap on LTVs (regulatory:75%, MUTH: avg 60%). With barely 1% write-offs, lower slippages and lower auctions and GNPA restricted <2% across periods (barring aberrations during FY16 and demo periods of FY18-FY19), MUTH has recorded negligible ultimate credit losses. GNPAs doubled from 2.2% in FY15 to 4.4% in FY18 due to shift to 90dpd NPA recognition norms and new 6-month loan product. However, post discontinuation of the product backed by better recoveries, GNPA declined back to 2.2% by FY20.

Pillars of strengthened asset quality for MUTH:

- **Adequate margin retention on collateral:** While periods of price fluctuations give rise to collateral risks, MUTH has been able to partially mitigate these with at least 25% margin retention on collateral value for assessment of loan amount.

Exhibit 39: >40% margin retention, >50% borrower's equity ensure sufficient margin of safety

	FY15	FY16	FY17	FY18	FY19	FY20	Q2FY21
Gold Loan assets (Rs bn)	233	243	272	288	336	407	462
Gold jewellery kept as security (In tonnes)	131	142	149	155	169	176	163
Gold Price/gm (Rs)	2,470	2,670	2,725	2,824	2,910	3,955	4,621
Lender's Perspective							
MV of Gold Content in Ornaments (Rs bn)	324	379	406	438	492	696	753
Margin of safety on loans	28%	36%	33%	34%	32%	42%	39%
Borrower's Perspective							
Market Value of Gold Ornaments (Rs bn) with 20% additional value towards making charges etc	389	455	487	526	590	835	904
Equity of Borrower in the Gold Ornaments net of loans availed	40%	47%	44%	45%	43%	51%	49%

Source: Company, PL

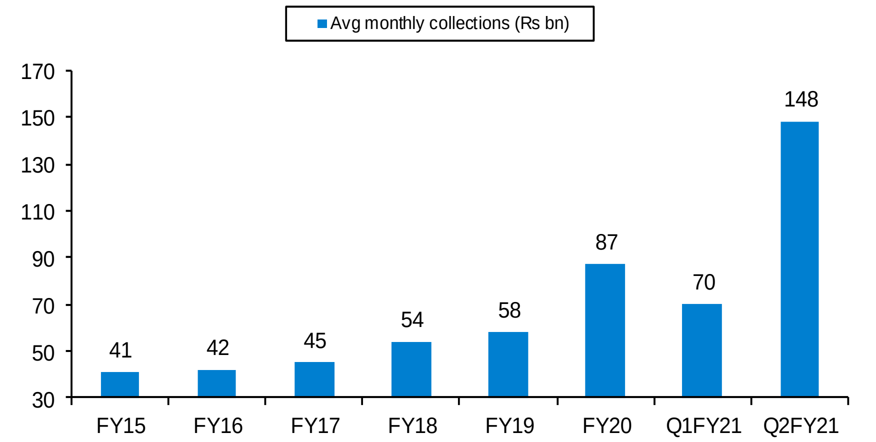
Avg LTV at 60% with higher borrower equity (49% of net loans), 30-day price moving average norm in LTV calculations, pledged collateral value exceeding loan ticket and financing only the gold content arrest delinquencies that could arise due to gold price descent

- **Stringent collateral valuation:** Loan amount assessment does not consider production costs, design cost and the gemstones associated with making the item but solely appraises the jewellery collateral based. This ensures minimal eventual credit loss in times of gold price slump.

- **Regulatory ceiling on LTVs:** Time and again regulatory interference (refer Annexure 1) led by stringent norms have led to stability of books of specialized gold NBFCs. NBFCs have observed more stringent LTVs over banks on regulatory front and yet maintained decent growth with minimal market share cedence. LTV's stand capped at 75% as per RBI mandate for gold financiers vs the recent tweaking to 90% for the banks. A regulatory LTV ceiling of 75% and standardized valuation coupled with auctioning procedures aid mitigation against gold-price falls. Also, regulatory cap on LTVs have enabled credit discipline amongst borrowers with higher borrower's equity in the game and minimal write-offs (Rs2bn over past 5 years for MUTH vs Rs3bn for MGFL) for lenders ensuring lowest credit losses.

- **Regular interest collections:** Gold loans tend to have low delinquencies as liquidation process generally does not incur any loss on the principal amount of loan but instead the Co. is able to recover most portion of the interest receivables. With greater focus on regular interest collections and 60% of loans getting repaid within six months, eventual credit losses tend to be lower.

Exhibit 40: Doubling of average monthly collections over past 5 years



Source: Company, PL

MUTH's flexible auction policy ensures full repayment of gold loans. Auction losses stand under control with consistent interest collections and related employee compensation

MUTH's flexible auction policy ensures full repayment of gold loans. MUTH being a customer centric model, a two to three months of auction-free dispensation to customers ensures interest receivables and cementing customer relationships. Notably, Co. has maintained strong control on auction losses with higher weightage on regular interest collections and healthy employee compensation. Subsequently, auction losses observed steep decline in FY17 (to Rs1.15mn from 8mn in FY16) maintaining downtrend till Rs 1.18mn in FY19. Moreover, not only did the accounts under auction fell from as high as 0.9mn in FY16 to Rs0.37 in FY19, auction losses per account also dropped in tandem from Rs8.96 to Rs3.23 during the same period.

Exhibit 41: Reduction in auction accounts and minimal losses across periods

Auction Details	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Accounts Auctioned (units in mn)	0.71	0.65	0.91	0.26	0.54	0.37	0.20
YoY Growth		*-9%*	*40%*	*-72%*	*111%*	*-32%*	*-45%*
O/S Dues of these accounts (Rs bn)	37.35	32.04	46.91	12.99	27.17	15.18	9.13
YoY Growth		*-14%*	*46%*	*-72%*	*109%*	*-44%*	*-40%*
Amt Realised (Rs bn)	34.29	27.88	38.80	11.85	25.18	14.00	8.55
YoY Growth		*-19%*	*39%*	*-69%*	*113%*	*-44%*	*-39%*
Auction Losses (Rs bn)	3.05	4.16	8.11	1.15	1.99	1.18	0.58
YoY Growth		*36%*	*95%*	*-86%*	*74%*	*-41%*	*-51%*
Auction losses per account (Rs)	4.3	6.42	8.96	4.48	3.68	3.23	2.89
YoY Growth		*50%*	*39%*	*-50%*	*-18%*	*-12%*	*-10%*

Source: Company, PL

MUTH's write-offs account for mere 1% of cumulative operating profit

- **Steady write-offs policy:** Over the past decade, MUTH has written off less than Rs2bn, amounting to merely 1% of cumulative operating profit. Likewise, MGFL has written off only INR2.6b over the past decade on a standalone basis, amounting to less than 3% of cumulative operating profit. Hence, bulk of the credit costs typically go into standard asset provisions, rather than in NPL provisions or in write-offs. While morat month saw higher write-offs, historically write-offs for MUTH has remained steady anywhere between 0.4-0.8% of avg loans over past five years.

Exhibit 42: Steady write-offs ensure quicker asset resolution

(Rs mn)	FY15	FY16	FY17	FY18	FY19	FY20	Q2FY21
Bad Debt Written off	192	107	165	316	259	599	10
% of Bad Debts written off to Gross Loan Assets	*0.08%*	*0.04%*	*0.06%*	*0.11%*	*0.08%*	*0.14%*	*0.00%*

Source: Company, PL

Around two-thirds of the customers close the accounts within the loan duration itself given the emotive value associated with the pledged ornaments ruling out the possibility of willful defaults.

- **Moat associated with gold lending:** A secured lending product like gold loan backed by high liquid asset makes it attractive as against other lending products. Around two-thirds of the customers close the accounts within the loan duration itself given the emotive value associated with the pledged ornaments ruling out the possibility of willful defaults. The average life of gold loan being 72 days and borrowers striving to avoid delinquencies makes this credit product self-liquidating. With MUTH's 90% of the business centred around this secured loan asset, the company faces lower delinquencies and faster asset resolution. While pandemic led disruptions might delay auction periods but realizations remain intact due to continued gold price momentum coupled with lower LTVs which would limit eventual credit losses. While gold loans with largely four to five months tenure do not carry moratorium risks, Co. has decided to postpone auctions in an effort to bolster customer relationships during pandemic times. Lower auctions in the interims to drive marginal rise in gross stage 3 ratio in near term.

  Said that, Co. still should remain in-the-money given the continued gold price momentum that stands supportive of the portfolio LTV and also aid reduction in the risk of haircuts/credit losses on loan auctions apart from enabling the Co. to charge penal interest. During Q4FY20, Gross stage 3 loans decreased 8% qoq/4% yoy to ~Rs9bn. Gross stage 3 ratio decreased 38 bps qoq to 2.2% which further declined 90bps to 1.3% in Q2FY21.

Exhibit 43: Tracking MUTH's controlled NPAs in light of key parameters

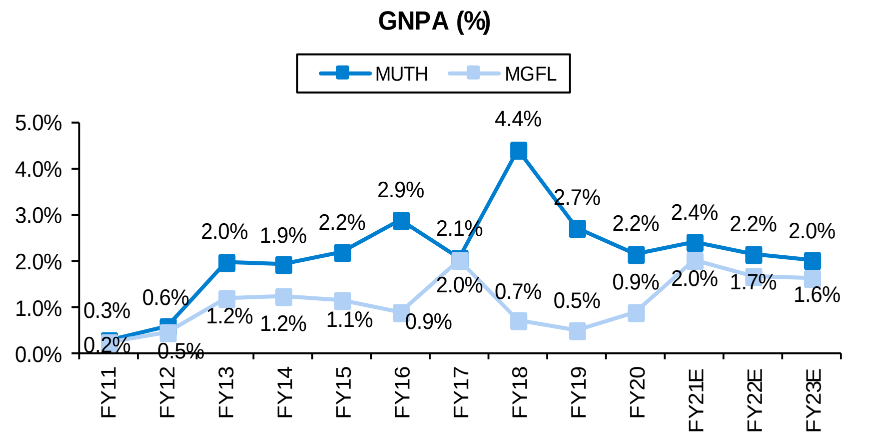
	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19s	FY20	Q2FY21
Gold price per gram (Rs)	2,492	2,908	2,637	2,483	2,437	2,705	2,708	3,050	4,332	4,621
LTV	60.0%	NA	NA	72.0%	64.0%	67.0%	66.0%	68.0%	58.0%	61.0%
No. of auctions	NA	NA	7,14,014	6,48,123	9,05,056	2,55,852	5,40,858	3,67,087	2,02,330	NA
NPA	0.56%	1.99%	1.90%	2.19%	2.88%	2.06%	4.42%	2.72%	2.16%	1.26%

Source: Company, PL

90% collateral backed gold lending mix and moderate LTVs (55-60%) to arrest delinquencies that could arise if gold prices were to correct

Our view on asset quality for consolidated book remains positive as the recoverability rate due to the gold collateral backed gold loans (~90% of the book) will generally remain higher. Moreover, the recent gold price momentum has enabled MUTH to build a large collateral buffer in its gold-loan portfolio against credit and collateral value risk. Even if gold prices were to correct and such buffers to diminish, the moderate LTV on gold loan portfolio (55-60%) would cushion against the price falls. While the Co. expects to maintain 80-20 gold : non-gold business mix over long run, we reckon MUTH's asset quality should remain in good stead at 2.0-2.1% NPA over FY22-23E.

Exhibit 44: Core business focus ensures better asset quality fro MUTH



Source: Company, PL

Healthy coverage and lower credit costs are further reassuring:

- Overall ECL coverage on the book decreased to 1.2% in Q2FY21 from 1.9% in 3QFY20 and 4QFY19. ECL coverage to increase marginally going ahead as Co. would provide additionally towards unforeseen pandemic led uncertainties.

Exhibit 45: NPA trends expected to decline followed by healthy coverage

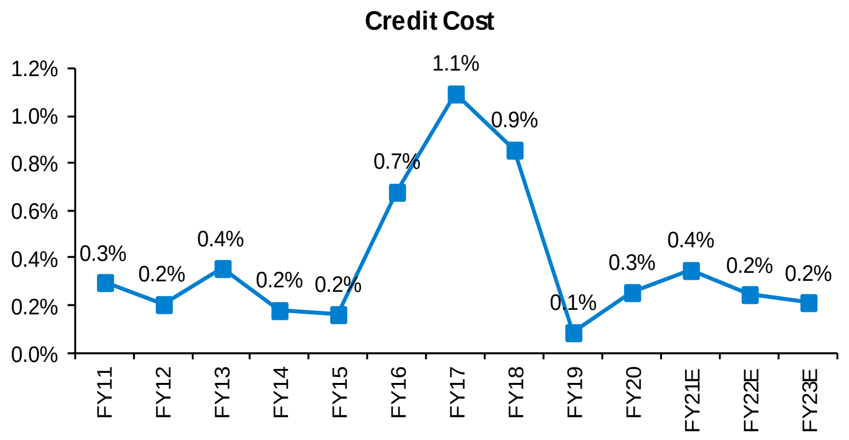
	FY18	FY19	FY20
ECL Classification			
Stage 1	2,80,735	3,37,619	4,16,148
Stage 2	7,710	8,916	6,542
Stage 3	12,872	9,326	8,992
Total	3,01,317	3,55,861	4,31,682
ECL Classification (%)			
Stage 1	93.2%	94.9%	96.4%
Stage 2	2.6%	2.5%	1.5%
Stage 3	4.3%	2.6%	2.1%
ECL Provisions			
Stage 1	4,078	4,934	4,391
Stage 2	112	131	81
Stage 3	1,901	1,295	956
Total	6,091	6,359	5,427
ECL coverage ratio (%)			
Stage 1	66.9%	77.6%	80.9%
Stage 2	1.8%	2.1%	1.5%
Stage 3	31.2%	20.4%	17.6%

Source: Company, PL

Credit costs have remained sub 1% of total assets over past three years, we expect ~26bps credit cost over FY21-23E

- Lower asset-side risk (security of gold, which is liquid and is in the lender's possession) aids in controlling credit costs in the gold finance business. Barring aberrations in FY17, credit costs have remained sub 1% of total assets over past three years. During Q4FY20, the credit cost stood muted at 5 bps (<1.1% over FY2005-19); provisions dropped 77% yoy. MUTH's credit costs are likely to remain muted due to high gold prices and low LTVs. We expect ~26bps credit cost over FY21-23E.

Exhibit 46: Average credit costs to sustain at 0.3% over long term



Source: Company, PL

Subsidiaries' asset quality – a key monitorable:

As the group is diversifying into other segments, asset quality within non-gold businesses would remain a monitorable. The share of the subsidiaries is expected to increase to about 15-20% over next 5 years. The less seasoned and unsecured nature of some of these businesses and the higher inherent risks expose them to credit risks.

Vehicle finance business to witness sharp climb in GNPA to 6% for FY21, the same should normalize closer to 3% levels by FY23

- **Muthoot Money:** Gross stage 3 assets witnessed 459bps spike between Q1FY20 to Q4FY20 to 4.9%. While such steep asset quality deterioration stands in-line with industry standards, relatively lower seasoning risks in the book to further accentuate asset quality stress. In light of COVID, moratorium was granted only from 1st Apr'20, collections witnessed good uptick with lifting of lockdown. On a lower base, we expect sharp climb in GNPA to 6% for FY21, the same should normalize closer to 3% levels by FY23.

Home finance business to witness rise in gross stage 3 loans to 2.5% owing to weak collections in FY21E, the same should normalize closer to 2% levels by FY23

- **Muthoot Home Finance:** Gross stage 3 witnessed 106bps deterioration during Q1FY20-Q3FY20. With dpd freeze due to moratorium dispensation, Q4FY20 Stage 3 assets dropped 15 bps QoQ to 1.7%. Said that, Muthoot Home Finance's comfortable capital position at 52% CAR, total liquidity of Rs1420mn and additional funding commitment of Rs5.5 bn from its parent entity. In light of COVID, Management has guided incremental Covid-19 provisions of ~Rs150 mn in 1QFY21E. ~6,000-7,000 customers out of total customer base of 24,390 have opted for moratorium, in-line with other affordable housing financiers. While, share of self-employed customers is a tad high at ~40% as of FY2019, this can lead to marginal deterioration in asset quality going ahead. We expect rise in gross stage 3 loans to 2.5% owing to weak collections in FY21E, the same should normalize closer to 2% levels by FY23.

MFI's rural focus would aid arresting decline in Stage 3 assets, we expect 2.5% GNPA for FY21, the same should normalize closer to 2% levels by FY23.

- **Belstar Micro finance:** MUTH's micro finance subsidiary has always maintained healthy CAR (avg. 25%) and ECL at 1.4-1.5% of total assets over past two years. NPAs, therefore, stood under control at avg. 1.1% over past one year. While Q4FY20 saw Stage 3 assets at 0.9%, COVID challenges can distort the near term picture. Focus on collections stay at forefront with figure standing at 35% as at May-end, Management expects the same to climb to

65% levels ahead. Belstar had provided moratorium to all its customers (opt-out basis). Going forward, asset quality deterioration cannot be ruled out given the riskier inherent customer segment. However, Co.'s rural focus would imply restricted fall in Stage 3 assets, we expect 2.5% GNPA for FY21, the same should normalize closer to 2% levels by FY23.

We reckon, asset quality is expected to deteriorate in MFI and affordable housing finance as the underlying customer segment is relatively more vulnerable to business disruptions due to Covid-19. Weak freight volumes, extended lockdown and sizeable dependence on cash transactions will drive deterioration in asset quality for Muthoot Money.

Exhibit 47: Subsidiaries asset quality snapshot

	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Standalone	0.6%	2.0%	1.9%	2.2%	2.9%	2.1%	4.4%	2.7%	2.2%	2.4%	2.2%	2.0%
Belstar	Na	Na	Na	Na	Na	0.1%	0.8%	1.2%	0.9%	2.5%	2.3%	2.2%
Homefin	Na	Na	Na	Na	Na	Na	0.4%	0.7%	1.7%	2.5%	2.3%	2.2%
Muthoot Money	Na	Na	Na	Na	Na	Na	0.0%	0.0%	4.9%	6.0%	4.5%	3.0%

Source: Company, PL

Regulatory requirement for appropriate Infrastructure for gold financing NBFCs:
(i) no transaction shall take place where there are no proper facilities for storage and security
(ii) Prior approval of RBI For opening branches in excess of 1000
(iii)Standardization of value of gold
(iv) Verification of Gold owner
NBFC shall keep record of verification of ownership of jewelry if loan is for more than 20 gram

Robust Risk matrix and collection infra across business segments

MUTH has built risk metrics and collection infrastructure across gold and key non-gold businesses. While the non-gold businesses are yet to observe business cycles, Belstar micro finance business and housing finance have maintained collection efficiencies during tough demonetization periods. While hard bucket delinquencies did catch up, the micro finance business' asset quality returned to normalcy in FY19. Going forward, while incremental focus should revolve around gold lending, credit risks pertaining to non-gold businesses in light of pandemic could be restricted. Moreover, conservative risk management practices and adequate infrastructure and checks should enable MUTH to maintain superior asset quality across businesses.

Exhibit 48: Robust risk management practices across businesses ensure minimal losses and credit risks

Gold Loans	Housing loan and Vehicle loan
Adequate margin of 25% or more retained while disbursing the loan	Standardization of process of identifying new risks and designing appropriate controls for these risks
Careful collateral appraisal and loan approval process	Extra vigilance on untimely payments by borrowers
Delegation of sanctioning power for gold loans to various authorities at branches/controlling offices. LTV never exceeds RBI mandate	Maintainenance of appropriate credit administration and loan review system
Pledged gold ornaments - primary responsibility of Branch Manager. Extra vigilance for pledged jewelry exceeding 20gm	Established metrics for portfolio monitoring and appropriate systems for credit risk mitigation
Safe storage hubs at every branch, grading of branches and regional offices, electronic surveillance and cybersecurity measures to safeguard customer data	Adequate due diligence over selection of customer base
Conduct of auctions are in-line with regulatory norms. Auction is generally conducted before loan amount plus interest exceeds realizable value of gold.	Credit assessment - credit rating and credit bureau check
iMSecure App: recognizes existing customer, prevents fraudulent practices by visitors	Follow up and regular monitoring of the borrower base

Source: Company, PL

MUTH’s high return controlled risk model

Reducing risk element associated with balance sheet have witnessed retention of profits and net worth as well as capital structure improvement for MUTH. We expect a steady-state growth and calibrated book expansion translating into healthy return metrics over next 3 years for Muthoot Finance.

Exhibit 49: Strong operating and profitability metrics across businesses

	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Standalone												
PAT YoY Growth	80.5%	12.6%	-22.3%	-14.0%	20.7%	45.7%	50.7%	10.9%	53.0%	20.5%	16.4%	15.4%
ROE	41.9%	30.2%	19.5%	14.3%	15.1%	19.5%	24.8%	22.4%	28.3%	25.0%	23.4%	22.0%
ROA	4.8%	3.8%	2.8%	2.6%	3.0%	4.1%	5.8%	5.7%	6.8%	6.7%	6.5%	6.2%
Belstar												
PAT YoY Growth	Na	Na	Na	Na	Na	70.5%	224.0%	116.3%	35.8%	-58.6%	356.9%	-3.9%
ROE	Na	Na	Na	Na	15.3%	16.0%	31.2%	27.7%	22.0%	7.9%	29.6%	22.0%
ROA	Na	Na	Na	Na	2.3%	2.5%	3.9%	4.9%	4.4%	1.5%	6.0%	4.5%
Homefin												
PAT YoY Growth	Na	Na	Na	Na	Na	Na	858.6%	30.6%	-12.4%	-52.6%	348.6%	26.5%
ROE	Na	Na	Na	Na	4.0%	3.3%	17.3%	14.1%	7.8%	3.5%	14.3%	15.5%
ROA	Na	Na	Na	Na	0.1%	2.4%	3.4%	2.2%	1.7%	0.8%	3.2%	3.2%
Muthoot Money												
PAT YoY Growth	Na	Na	Na	Na	Na	Na	Na	50.0%	800.0%	-57.0%	26.0%	26.0%
ROE	Na	Na	Na	Na	Na	Na	6.3%	0.6%	2.6%	1.1%	1.4%	1.7%
ROA	Na	Na	Na	Na	Na	Na	3.1%	0.2%	0.7%	0.2%	0.2%	0.2%

Source: Company, PL

The following trends of AUM/net worth continued accruals to net worth indicative of strong balance sheet and ability to absorb losses arising from unfavorable events, especially, gold price fluctuations.

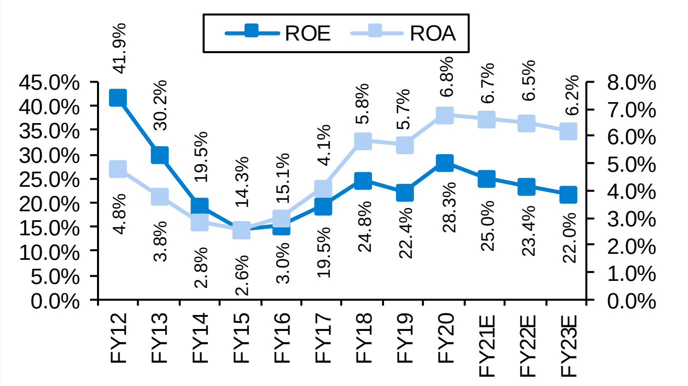
Exhibit 50: MUTH’s standalone business stands resilient

	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
AUM (Rs bn)	247	264	219	234	244	273	291	342	416	491	611	689
Networth (Rs bn)	29	37	43	51	56	65	78	98	116	146	181	222

Source: Company, PL

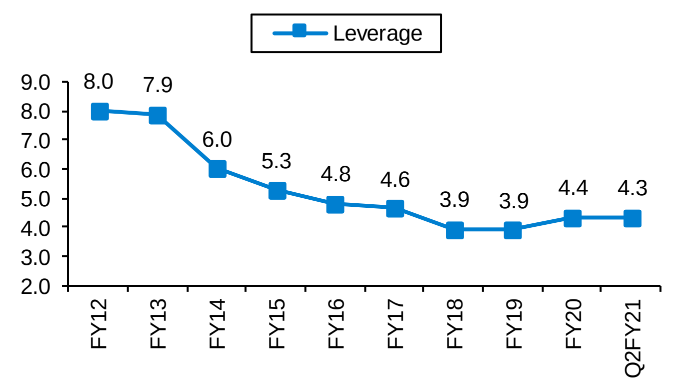
While a typical higher yielding business like gold and micro finance (87% of total) carry inherent potential to fetch higher returns (6.5%RoA/ 23.4%RoE: FY22E), it’s the core business efficiency and effective capital deployment that would largely determine quality of the balance sheet.

Exhibit 51: MUTH's standalone biz has high return potential



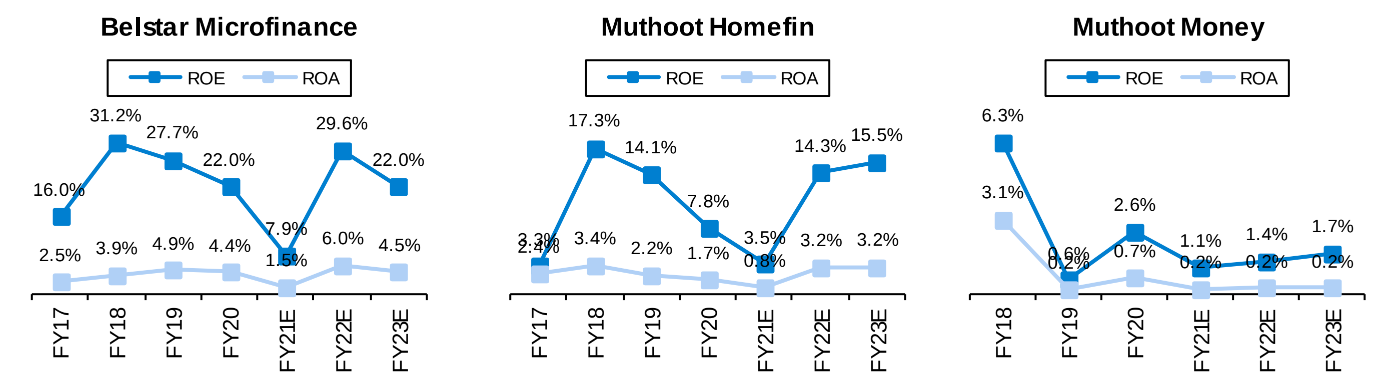
Source: Company, PL

Exhibit 52: …at low leverage



Source: Company, PL

Exhibit 53: Subsidiaries' RoAs to improve as economy stabilizes



Source: Company, PL

Valuation Analysis

Tailwinds to ensure tenacity; superior valuations justified

We expect the company to maintain market leadership in NBFC gold financing and yield steady-state ROA of ~6%, with leverage at ~3.9x.

Gold financing is back in action bringing tailwind to business growth while buoyancy is expected to sustain on the back of (a) steep run-up in gold prices (b) soaring gold loan demand due to pandemic (c) muted offtake for other loans and (d) overhang on asset quality due to moratorium dispensation.

Growth will likely come from non-south geographies, tailor-made processes & systems for small-ticket disbursement and an ability to recover adequate value on gold auctioned to contain credit losses. Subsequently, we expect MUTH to clock ~19% CAGR over FY21-23E. Being a high yielding business, spreads for MUTH sustained at ~15% though we expect some near term compression due to lower penal interest income. Also well collateralized gold loans carry minimal challenges to ALM, hence we expect the company's spreads/NII to stand resilient in current challenging environment. MUTH is the lowest cost gold financier in India and its expense ratio is forecast to remain at ~4.1% of AUM through FY22. Backed by flexible auctions and regular collections, write-offs have halved over past couple of years maintaining MUTH's asset quality. We expect the company to maintain market leadership in NBFC gold financing and yield steady-state ROA of ~6%, with leverage at ~3.9x.

MUTH has diversified into home finance and microfinance (Belstar) with vehicle finance as a second priority. Belstar being a dominant SHG business model is a safer MFI play despite geographic concentration in Tamil Nadu. We expect incremental capital to be allocated to these fledgling businesses, of which Belstar is well placed to contribute meaningfully in the near term. However, we turn cautious on the outlook for its HFC/MFI subsidiaries. We expect FY21 to be a tough year for these companies. While FY22-23 looks promising, we expect non-gold AUM CAGR at 25% over FY21-23E.

With an impending credit squeeze and asset quality overhang due to Covid-19, we believe MUTH's clear edge over peers positions itself as a formidable retail gold loan franchise. We expect premium valuations to sustain on the back of (a) no challenges on fund raising for MUTH, given positive ALM (short loan tenure high churn book) (b) adequate liquidity (Rs79bn: Sep'20) backed by liability diversification (raised USD1bn from ECBs) (c) capital sufficiency with Tier I capital at 24%, (d) granular asset mix backed by pricing power (e) healthy business productivity.

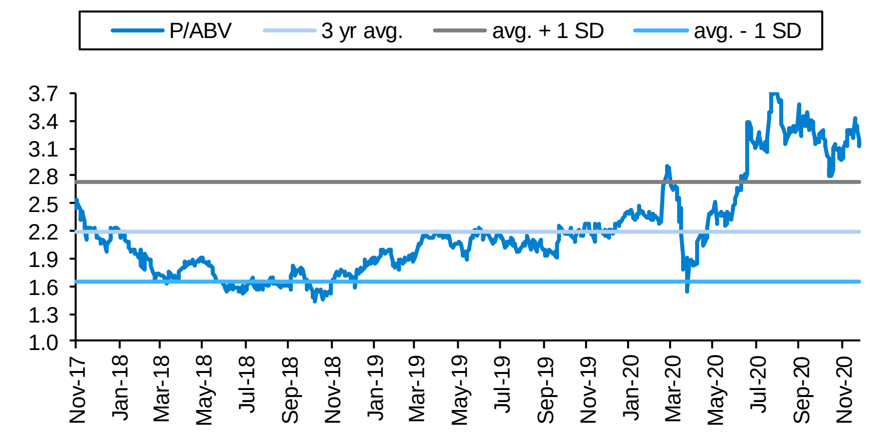
We recommend BUY on Muthoot Finance valuing the stock on SoTP basis and arriving at price target of Rs1,364 wherein core book is valued at 2.6x Sep'22E BVPS (Rs1,330) and subsidiaries at Rs34.

Exhibit 54: MUTH vs MGFL Comparison metrics

	MGFL					MUTH				
	FY19	FY20	FY21	FY22	FY23	FY19	FY20	FY21	FY22	FY23
AUM (Rs mn)	1,94,384	2,52,252	2,96,791	3,50,054	4,20,540	3,42,461	4,16,106	4,91,423	6,11,461	6,89,402
AUM (growth YoY %)	*23.3%*	*29.8%*	*17.7%*	*17.9%*	*20.1%*	*17.5%*	*21.5%*	*18.1%*	*24.4%*	*12.7%*
AUM Mix										
Gold Loan	*66.7%*	*67.3%*	*70.2%*	*70.1%*	*70.0%*	*87.7%*	*87.0%*	*87.4%*	*87.9%*	*86.3%*
Non-Gold Loan	*33.3%*	*32.7%*	*29.8%*	*29.9%*	*30.0%*	*12.3%*	*13.0%*	*12.6%*	*12.1%*	*13.7%*
Key operating metrics										
NII (Rs mn)	28,145	36,142	37,849	42,310	51,210	45,202	57,735	66,639	77,133	89,706
NII (growth YoY %)	*18.1%*	*28.4%*	*4.7%*	*11.8%*	*21.0%*	*5.8%*	*27.7%*	*15.4%*	*15.7%*	*16.3%*
NIM (%)	*16.0%*	*16.2%*	*13.8%*	*13.1%*	*13.3%*	*14.0%*	*14.9%*	*14.7%*	*14.2%*	*14.0%*
Operating profit (Rs mn)	15,113	22,449	22,727	24,687	30,026	31,044	41,531	50,163	57,904	66,667
Operating profit (growth YoY %)	*24.5%*	*48.5%*	*1.2%*	*8.6%*	*21.6%*	*0.6%*	*33.8%*	*20.8%*	*15.4%*	*15.1%*
PAT (Rs mn)	9,415	14,678	13,017	16,141	21,105	19,721	30,183	36,367	42,340	48,874
PAT (growth YoY %)	*39.3%*	*55.9%*	*-11.3%*	*24.0%*	*30.8%*	*10.9%*	*53.0%*	*20.5%*	*16.4%*	*15.4%*
ROE (%)	22.4%	28.5%	21.7%	23.3%	24.9%	22.4%	28.3%	25.0%	23.4%	22.0%
ROA (%)	4.6%	5.9%	4.0%	4.1%	4.4%	5.7%	6.8%	6.7%	6.5%	6.2%
No. of Branches	4,351	4,666	4,460	4,429	4,671	4,480	4,567	4,802	4,887	5,122
AUM/Branch (Rs mn)	40	48	62	73	82	72	85	95	111	125
Asset quality										
GNPA (%)	*0.50%*	*0.90%*	*1.86%*	*1.53%*	*1.51%*	*2.7%*	*2.2%*	*2.4%*	*2.1%*	*2.0%*
Capital Adequacy										
CAR	23.7%	28.3%	27.2%	27.9%	24.6%	26.1%	25.5%	26.4%	26.5%	28.3%
Valuations										
Book value (Rs)	53.9	68.2	74.1	90.0	111.5	244	289	363	451	554
P/ABV (x)	3.2	2.6	2.4	2.0	1.6	4.7	4.0	3.3	2.7	2.1
P/E (x)	15.5	9.9	11.2	9.0	6.9	23.0	15.0	12.5	10.7	9.3
LLP	547	2,376	4,970	2,570	1,840	275	957	1,562	1,322	1,353

Source: Company, PL

Exhibit 55: Superior valuations justified, yet expect healthy upside potential



Source: Company, PL

Key risks:

- Any reversal in the gold price rally.
- Liquidity support from banks.
- Ability of the company to deliver high tonnage growth.
- Any further tightening of the regulatory environment for NBFCs and
- Any significant change in customers' preference from gold loan to other alternative lending products like personal loans, microfinance etc. among others.
- COVID-led disruptions on MFI, vehicle financing and Housing finance business

  Risks may arise from gold collateral safe keeping, lending against stolen or spurious gold as well as staff fraud at branches

Annexures

Exhibit 56: Regulatory changes across periods for gold lending institutions

Date	Regulations
Jul-2010	NBFCs-Gold loans removed from PSL
Feb-2011	Investments made by banks in securitised assets originated by NBFCs, where the underlying assets are loans against gold jewellery, and purchase/assignment of gold loan portfolio from NBFCs are also not eligible for classification under agriculture sector.
Mar-2012	**NBFCs** 1. LTV shall not exceed 60% 2. Maintain Tier 1 ratio at 12% by April 2014 3. Should not grant any loan against Bullion/primary gold and gold coins
May-2012	Banks advised to 1.Reduce their regulatory exposure ceiling on single NBFC-Gold from 10% to 7.5%. This May go up to 12.5% if additional exposure is on account of fund lend by NBFCs to Infra sector 2.Have an internal sub-limit on their exposures to NBFC- Gold. It should be within the internal limit fixed by banks for their aggregate exposure.
May-2013	Lending against minted gold coins by bank: Advised that the weight of coins shall not exceed 50 grams per customer and amt of loan shpuld be within Board approved limit Clarification on Lending against Gold ETFs by Bank: Not permitted as ETFs Backed by bullion
Sept-2013	**NBFCs** **Appropriate Infrastructure:** no transaction shall take place where there are no proper facilities for storage and security Prior approval of RBI For opening branches in excess of 1000 Standardization of value of gold Gold should be valued at avg of closing price of 22 carat gold for preceding 30 days quoted by Bombay Bullion Association Verification of Gold owner NBFC shall keep record of verification of ownership of jewelry if loan is for more than 20 gram **Auction policy:** 1. Should be in same town in which branch has extended loan. 2.Should declare reserve price of gold and same shall not be less than 85% of avg of previous 30 days closing price of 22 carat by BBA 3. Mandatory to provide full details of value fetched in auction and o.s dues adjusted to any amount over and above loan o/s should be payable to borrowers. 4. Must disclose in their AR regarding no. of loan ac, O/S amt , value fetched and its sister concerned participated in the auction. Other: a. must insist on PAN card copy for transaction above Rs 5 lac b More than Rs. 1 lakh loan should be disbursed by cheque only c documentation across all branched should be standardized d. not issue misleading advertisement claiming availability of loans in 2-3 minutes
Dec-2013	Non-agricultural loans against ornaments and gold jewelry 1. Amt shall not exceed Rs .1 Lakh 2 Period of loan shall not exceed 12 months 3. Interest will be charged on monthly basis but will be due for payment along with principal at maturity 4.Bank should prescribe min margin to be maintain in cash and fix the laon limit taking into account the MV of security, expected price fluctuations , interest that will accrue due to tenure of the loan 5. account will be classified at NPA even before repayment date if prescribed margins is not maintained. 6. Shall recognise interest income on such loans in their P&L account on collection
Jan-2014	LTV Ratio increased to 75% for banks & NBFCs No making charges should be added while arriving value of gold
May-2014	Urban co-operative bank loan should not exceed 75% LTV
Jul-2014	Banks: LTV of 75% shall be maintained throughout the tenure of the loan for all loans. The LTV ratio shall be computed against the total o/s in the account, including accrued interest Banks allowed to se the historical spot gold price data publicly disseminated by a commodity exchange regulated by the Forward Markets Commission on a consistent manner as per their Board approved policy, in addition to the prices disseminated by the India Bullion and Jewellers Association Ltd.
Oct-2014	Urban Commercial Banks permitted to grant loan loan above 1 lakh to 2 lakhs
Feb-2017	Regional Rural Banks permitted to grant loan loan above 1 lakh to 2 lakhs
Jan-2020	NBFCs can pool gold jewellery from different branches in a district and auction it at any location within the district, subject to meeting the following conditions: a) The first auction has failed. b) The NBFC shall ensure that all other requirements of the extant directions regarding auction (prior notice, reserve price, arms-length relationship, disclosures, etc.) are met.
Aug-2020	LTV Ratio increased to 90% from 75% for Banks; for NBFCs it stands maintained at 75%

Source: Company, PL

Exhibit 57: Management background

Name	Designation	Education	Experience	Remuneration (Rs mn)		
				Sitting fee	Salary allowance & Commission	Total
M. G. George Muthoot	Chairman & Wholetime Director	Graduate in Mechanical Engineering & attended various Executive Management courses at Harvard	Over four decades of experience in managing business operations	0.0	154.2	154.2
George Thomas Muthoot	Wholetime Director	Businessman by profession	Over three decades of experience in managing business operations	0.0	154.2	154.2
George Jacob Muthoot	Wholetime Director	Degree in civil engineering	Over three decades of experience in managing business operations	0.0	154.2	154.2
George Alexander Muthoot	Managing Director	Chartered Accountant and Bachelor's degree in Commerce	Over three decades of experience in managing business operations	0.0	154.2	154.2
Alexander M. George	Wholetime Director	MBA Graduate and Advanced diploma in Business Administration	Manages the entire business operations of North, East and West India of Muthoot Finance	0.0	17.1	17.1
George Joseph	Independent Director	Certified Associate of Indian Institute of Banking and Finance and B.Com Graduate	39 years of experience in the banking sector. Former Chairman and MD of Syndicate Bank	0.4	0.6	0.9
John K.Paul	Independent Director	Graduate in engineering	Served as President of Chamber of Commerce and Industry from 2005-2006. Currentlt MD of Popular Vehicles & Services Ltd and MD of Prabhal Trucking	0.3	0.6	0.9
Pamela Anna Mathew	Independent Director	Postgraduate in Economics and Degree in Business Administration	43 years of experience as a well-known business leader and currently serving as MD of O/E/N India Ltd	0.7	1.1	1.8
Jose Mathew	Independent Director	Chartered Accountant	Served as MD of M/s Kerala State Drugs & Pharmaceutical Ltd and currently serves as MD of M/s Green Shore Holidays and Resorts and Independent Director of M/s Muthoot Vehicle and Asset Finance	1.0	1.1	2.1
Justice (Retd.) Jacob Benjamin Koshy	Independent Director	Graduate in Law	Former Chief Justice of Patna High Court and Former Judge of High Court of Kerala	0.8	1.1	1.9
Ravindra Pisharody	Independent Director	B. Tech in Electronics and Electrical Communication	Former Whole-time Director at Tata Motors Limited, where he headed CV Business Unit	0.3	0.6	0.8
Pratip Chaudhuri	Independent Director	Master's degree in Science and Statistics	Former Chairman of SBI and 40 years of experience in banking industry	0.1	0.6	0.6
V A George	Independent Director	Bachelor's degree in Mechanical Engineering	More than 40 years of experience in corporate field and former chairman of Equipment leasing association of India	0.3	0.6	0.9
Oommen K Mammen	Chief Financial Officer	Chartered Accountant	12 years of experience in the industry	NA	NA	NA
Maxin James	Company Secretary	Company secretary and B.Sc. In Mathematics and Computer Science	Company Secretary and Group Manager at Sabari Group of Co's	NA	NA	NA

Source: Company, PL

Income Statement (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Int. Inc. / Opt. Inc.	85,644	1,01,269	1,19,137	1,39,251
Interest Expenses	27,909	34,630	42,004	49,546
Net interest income	**57,735**	**66,639**	**77,133**	**89,706**
Growth(%)	*27.7*	*15.4*	*15.7*	*16.3*
Non-interest income	1,584	2,376	2,851	3,136
Growth(%)	*28.1*	*50.0*	*20.0*	*10.0*
Net operating income	59,319	69,015	79,984	92,842
Expenditures				
Employees	10,290	11,010	13,102	15,722
Other Expenses	7,067	7,369	8,386	9,742
Depreciation	431	474	592	711
Operating Expenses	17,356	18,378	21,488	25,464
PPP	**41,531**	**50,163**	**57,904**	**66,667**
Growth(%)	*33.8*	*20.8*	*15.4*	*15.1*
Provisions	957	1,562	1,322	1,353
Profit Before Tax	**40,574**	**48,600**	**56,582**	**65,314**
Tax	10,391	12,233	14,242	16,439
Effective Tax rate(%)	*25.6*	*25.2*	*25.2*	*25.2*
PAT	**30,183**	**36,367**	**42,340**	**48,874**
Growth(%)	*53.0*	*20.5*	*16.4*	*15.4*

Balance Sheet (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Source of funds				
Equity	4,010	4,010	4,010	4,010
Reserves and Surplus	1,11,708	1,41,529	1,76,855	2,18,247
Networth	1,15,718	1,45,539	1,80,865	2,22,257
Growth (%)	*18.2*	*25.8*	*24.3*	*22.9*
Loan funds	3,71,300	4,20,245	5,23,655	5,89,733
Growth (%)	*38.4*	*13.2*	*24.6*	*12.6*
Deferred Tax Liability	-	-	-	-
Other Current Liabilities	7,342	24,285	28,031	33,916
Other Liabilities	10,236	(4,922)	(11,025)	4
Total Liabilities	**5,04,597**	**5,85,147**	**7,21,525**	**8,45,910**
Application of funds				
Net fixed assets	2,565	3,743	4,169	5,393
Advances	4,26,042	4,82,203	6,00,858	6,76,678
Growth (%)	*22.0*	*13.2*	*24.6*	*12.6*
Investments	14,383	16,541	18,857	27,342
Current Assets	61,606	82,661	97,643	1,36,497
Net current assets	**54,264**	**58,376**	**69,612**	**1,02,581**
Other Assets	-	-	-	-
Total Assets	**5,04,596**	**5,85,147**	**7,21,526**	**8,45,910**
Growth (%)	*32.5*	*16.0*	*23.3*	*17.2*
Business Mix				
AUM	4,16,106	4,91,423	6,11,461	6,89,402
Growth (%)	*21.5*	*18.1*	*24.4*	*12.7*
On Balance Sheet	-	-	-	-
% of AUM	-	-	-	-
Off Balance Sheet	-	-	-	-
% of AUM	-	-	-	-

Profitability & Capital (%)

Y/e Mar	FY20	FY21E	FY22E	FY23E
NIM	14.9	14.7	14.2	14.0
ROAA	6.8	6.7	6.5	6.2
ROAE	28.3	25.0	23.4	22.0

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Int. Inc. / Operating Inc.	22,806	23,506	23,160	25,066
Income from securitization	-	-	-	-
Interest Expenses	7,094	7,700	8,715	9,241
Net Interest Income	**15,712**	**15,806**	**14,445**	**15,825**
Growth (%)	*43.6*	*29.5*	*21.8*	*10.2*
Non-Interest Income	403	520	694	779
Net Operating Income	**16,115**	**16,326**	**15,139**	**16,603**
Growth (%)	*42.8*	*28.6*	*24.4*	*12.9*
Operating expenditure	4,542	5,304	3,738	4,496
PPP	**11,573**	**11,021**	**11,401**	**12,107**
Growth (%)	-	-	-	-
Provision	612	48	146	107
Exchange Gain / (Loss)	-	-	-	-
Profit before tax	10,961	10,974	11,255	12,000
Tax	2,809	2,822	2,847	3,056
Prov. for deferred tax liability	1,914	3,633	-	-
Effective Tax Rate	25.6	25.7	25.3	25.5
PAT	**8,152**	**8,151**	**8,408**	**8,944**
Growth	*68*	*59*	*59*	*4*
AUM	3,84,982	4,16,106	4,12,957	4,70,163
YoY growth (%)	18.6	21.5	15.3	31.6
Borrowing	3,25,036	3,71,301	3,87,839	4,21,571
YoY growth (%)	-	*38.4*	*38.2*	*48.4*

Key Ratios

Y/e Mar	FY20	FY21E	FY22E	FY23E
CMP (Rs)	1,152	1,152	1,152	1,152
EPS (Rs)	75.3	90.7	105.6	121.9
Book value (Rs)	288.5	362.9	451.0	554.2
Adj. BV(Rs)	286.2	339.8	425.2	527.2
P/E(x)	15.3	12.7	10.9	9.5
P/BV(x)	4.0	3.2	2.6	2.1
P/ABV(x)	4.0	3.4	2.7	2.2
DPS (Rs)	15.0	14.0	15.0	16.0
Dividend Payout Ratio(%)	-	-	-	-
Dividend Yield(%)	*1.3*	*1.2*	*1.3*	*1.4*

Asset Quality

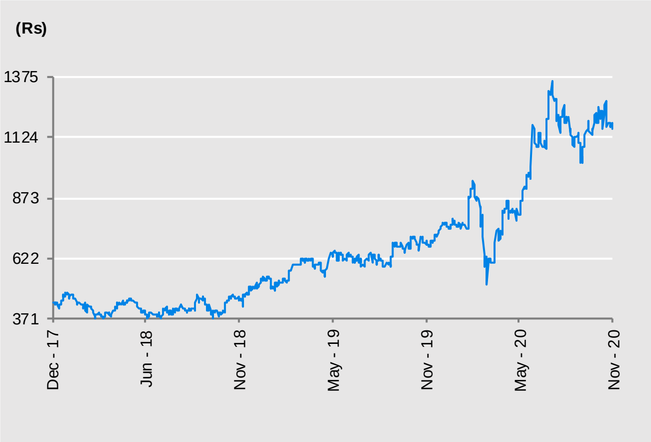
Y/e Mar	FY20	FY21E	FY22E	FY23E
Gross NPAs(Rs m)	8,992	11,573	12,918	13,534
Net NPA(Rs m)	8,036	9,258	10,335	10,827
Gross NPAs to Gross Adv.(%)	2.2	2.4	2.1	2.0
Net NPAs to net Adv.(%)	1.9	1.9	1.7	1.6
NPA coverage(%)	10.6	20.0	20.0	20.0

Du-Pont as a % of AUM

Y/e Mar	FY20	FY21E	FY22E	FY23E
NII	*13.9*	*13.6*	*12.6*	*13.0*
NII INCI. Securitization	13.9	13.6	12.6	13.0
Total income	14.3	14.0	13.1	13.5
Operating Expenses	4.2	3.7	3.5	3.7
PPOP	10.1	10.3	9.6	9.8
Total Provisions	0.2	0.3	0.2	0.2
RoAA	6.8	6.7	6.5	6.2
Avg. Assets/Avg. net worth	4.4	4.0	4.0	3.8
RoAE	28.3	25.0	23.4	22.0

Source: Company Data, PL Research

Price Chart



Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Bajaj Finance	BUY	3,805	3,233
2	Cholamandalam Investment and Finance Company	BUY	310	273
3	HDFC	Accumulate	2,185	2,041
4	L&T Finance Holdings	Sell	52	65
5	LIC Housing Finance	Hold	316	324
6	Mahindra & Mahindra Financial Services	Reduce	124	131
7	Manappuram Finance	Accumulate	196	162
8	SBI Cards and Payment Services	Accumulate	895	852
9	Shriram Transport Finance	Accumulate	809	693

PL's Recommendation Nomenclature

Buy	:	>15%
Accumulate	:	5% to 15%
Hold	:	+5% to -5%
Reduce	:	-5% to -15%
Sell	:	< -15%
Not Rated (NR)	:	No specific call on the stock
Under Review (UR)	:	Rating likely to change shortly

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