Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Mahindra & Mahindra Financial Services Ltd

Strong beat on profitability

NBFC	Sharekhan code: M&MFIN	
Reco/View: Buy ↔	CMP: Rs. 180	Price Target: Rs. 220 ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- M&M Financial Services (MMFS) posted higher-than-expected PAT due to significant improvement in asset quality, leading to lower credit costs. PAT was at Rs. 601 crore versus our expectation of Rs. 395 crore, up ~300% y-o-y and down ~33% q-o-q.
- Further, disbursements grew strongly by 54% y-o-y and 15% q-o-q to Rs. 9,202 crore, aided by robust growth in CV/CE, pre-owned, and SME and other segments.
- Asset quality improved sequentially with GNPL declining by ~130 bps y-o-y to 7.7% in Q4FY2022. This was primarily due to higher collection efficiencies and write-offs. The company articulated its Vision 2025 with goals on AUM growth, asset quality, NIM, cost ratios, and RoA target going forward.
- At the CMP, the stock trades at 1.2x and 1.1x its FY2023E and FY2024E P/BV, respectively. We maintain our Buy rating on the stock with a revised PT of Rs. 220.

M&M Financial Services (MMFS) reported PAT of Rs. 601 crore, increased by ~300% y-o-y and ~33% q-o-q. Net interest income (NII) declined by 1% y-o-y and 5% q-o-q on subdued assets under management (AUM) growth 0.5% y-o-y and 2% q-o-q. Net interest margin (NIM) declined by ~60 bps q-o-q to 9% in Q4FY2022 (calculated), as there was interest reversals (~Rs. 140 crore), driven by the Reserve Bank of India's (RBI) inspection, leading to excess interest refund. However, other operating expenses were higher on account of spends towards collections, investment in technology, and talent. Provisions was at Rs. 64 crore versus write-back of Rs. 147 crore in Q3FY2022 versus Rs. 886 crore in Q4FY21. Disbursements grew strongly by 54% y-o-y and 15% q-o-q to Rs. Rs. 9,202 crore, aided by robust growth in CV/CE, pre-owned, and SME and other segments. Asset quality improved sequentially with GNPL declining by ~130 bps y-o-y to 7.7% in Q4FY2022. This was primarily due to higher collection efficiencies and write-offs. The company did not specify GNPA ratio under IRACP but indicated improvement in asset quality.

Key positives

- Disbursements grew strongly by 54% y-o-y and 15% q-o-q to Rs. Rs. 9,202 crore, aided by robust growth in CV/CE, pre-owned, and SME and other segments.
- The company has 100% provision coverage on 18 plus months aging contracts.
- Collection efficiency improved to 100% in Q4FY2022 versus 95% in Q3FY2022.

Key negatives

- Operating expenses were higher on account of spends towards collections, investment in technology, and talent, thus leading to lower operating profit.

Management Commentary

- The company unveiled its Vision 2025 with goals on AUM growth, asset quality, NIM, cost ratios, and RoA target going forward.
- Under its Vision 2025, the company plans to grow its AUM to 2x, maintain stable asset quality with GS-3 less than 6%, NIM at ~7.5%, cost-to-asset ratio at ~2.5%, and RoA of ~2.5%.

Our Call

Valuation: We maintain Buy on MMFS with a revised PT of Rs. 220. MMFS reported better-than-expected earnings largely on account of lower provisioning. Disbursements also picked up significantly with better collection efficiency signaling recovery in vehicle finance, which is encouraging. Further, management has unveiled its Vision 2025, which is expected to give it a fillip to deliver on earnings performance going ahead. Hence, given its strong liability franchise, leadership in rural financing along with strong parentage, the company is well on track to deliver on its aspirational goals. At the CMP, MMFS trades at 1.2x and 1.1x its FY2023E and FY2024E P/BV, respectively. Hence, we maintain our Buy recommendation on the stock with a revised PT of Rs. 220.

Key Risks

Likely deterioration in asset quality and its exposure to the SME segment are vulnerable and may take longer time to recover.

Valuation Rs cr

Particulars	FY21	FY22	FY23E	FY24E
NII	5,534	5,555	6,329	7,248
PAT	329	989	1,904	2,243
EPS (Rs)	2.7	8.0	15.4	18.0
BVPS (Rs)	119.4	126.5	144.5	158.5
P/E (x)	66.3	22.5	11.7	10.0
P/BVPS (x)	1.5	1.4	1.2	1.1
ROE (%)	2.6	6.5	11.4	11.9
ROA (%)	0.4	1.3	2.3	2.4

Source: Company; Sharekhan estimates

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 18.25

Updated Jan 08, 2022

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

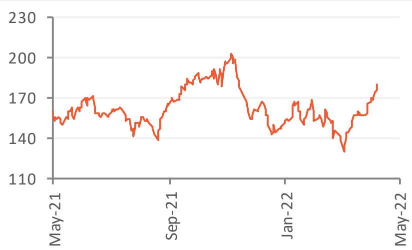
Company details

Market cap:	Rs. 22171.58 cr
52-week high/low:	Rs. 206/128
NSE volume: (No of shares)	52.1 lakh
BSE code:	532720
NSE code:	M&MFIN
Free float: (No of shares)	59.1 cr

Shareholding (%)

Promoters	52.2
FII	17.9
DII	16.2
Others	13.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.2	12.6	-7.8	16.0
Relative to Sensex	15.4	17.9	-0.5	0.6

Sharekhan Research, Bloomberg

Key Conference call takeaways

- **Unveiled well-articulated Vision 2025:** MMFS plans for stable asset quality going forward with GS3 less than 6% through better collections, product diversification, better customer segment mix, and use of digital and technologies. It foresees AUM growth of 2x through leveraging its leadership in vehicle financing and scaling up new growth engines such as SME lending, LAP, leasing, and Digi Finco. The company intends to strengthen its technologies and digital and differentiate itself through phygital (physical plus digital). It expects its new businesses (digi lending, SME financing, micro LAP) to contribute 15% to AUM mix. It targets NIM of ~7.5% and cost to asset of ~2.5% to generate RoA of ~2.5% by 2025.
- **Healthy disbursements:** It witnessed strong disbursements in pre-owned vehicles (up ~60% y-o-y and 45% q-o-q) in Q4FY2022. The company expects this trend to continue as customers are not ready to invest in the new vehicle. Tractors deployment in infrastructure activates is yet to pick up. The company has signed with three vehicle aggregators (not yet operational) and will soon enter into co-lending arrangement with a large bank. Management opined that rising farm income, pick up in infrastructure activities coupled with normal monsoon forecast are likely to augur growth in the coming quarters.
- **Improved asset quality:** Asset quality improved sequentially with GNPL and NNPL declining by ~130 bps y-o-y to 7.7% and ~60 bps y-o-y to 3.4% in Q4FY2022. However, the company did not report GNPA ratio under IRACP norms and management sounded confident that no additional provisioning would be required once it is implemented in September 2022. Its restructured book stood at 6.2% of business assets. Its PCR on stage 3 assets stood at 58.1% in Q4FY2022 versus 53.2% in Q3FY2022.

Results Rs cr

Particulars	Q4FY22	Q4FY21	Q3FY22	y-o-y (%)	q-o-q (%)
Interest Income	2,392	2,564	2,487	(6.7)	(3.8)
Interest expenses	936	1,089	951	(14.0)	(1.6)
Net Interest Income	**1,456**	**1,475**	**1,535**	**(1.3)**	**(5.2)**
Other income	75	74	56	1.0	32.7
Net Operating income	**1,531**	**1,549**	**1,592**	**(1.2)**	**(3.8)**
Employee cost	320	282	303	13.5	5.7
Depreciation	42	30	29	38.0	42.9
Other expenditure	271	179	197	51.1	37.2
Operating expenses	**633**	**492**	**529**	**28.7**	**19.5**
Pre-provisioning profit (PPoP)	**898**	**1,057**	**1,062**	**(15.1)**	**(15.5)**
Provisions & Writeoffs	64	886	-147	(92.8)	(143.3)
PBT	**834**	**171**	**1,210**		**(31.0)**
Tax	233	21	316		
Tax Rate	28.0	12.5	26.1		
PAT	**601**	**150**	**894**	**300.6**	**(32.8)**
Key ratios	**Q4FY22**	**Q4FY21**	**Q3FY22**	**y-o-y (%)**	**q-o-q (%)**
Reported AUM (Rs mn)	64,961	64,608	63,944	0.5	1.6
NIM on AUM (%)	9.0	9.0	9.6	3 bps	-60 bps
Cost of debt (%)	6.6	7.4	6.7	-77 bps	-11 bps
Cost to income (%)	41.3	31.7	33.3	960 bps	807 bps
GNPL (Rsmn)	4,976	5,786	7,223	-14.0	-31.1
NNPL (Rsmn)	2,086	2,434	3,381	-14.3	-38.3
GNPL (% of business assets)	7.7	9.0	11.3	-130 bps	-364 bps
NNPL (% of business assets)	3.4	4.0	5.6	-62 bps	-227 bps
Coverage ratio (%)	58.1	57.9	53.2	14 bps	488 bps

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Green shoots in the economy encouraging

The economy has been witnessing improved macro-economic sentiments, which are expected to boost the primary sectors, including automobiles and infrastructure sectors. Recovery in the vehicle finance (VF) sector over the past six months has been encouraging, with lower funding costs and improving traction (including sub-segments), among other factors. Asset-quality trends have also improved, and while the sector is not completely out of the woods (due to COVID-19 resurgence), we expect normalisation by H2FY2022. In this backdrop, aided by a strong liability franchise, highly rated and well-capitalised nimble NBFCs have ample growth opportunities and are well placed to overcome challenges.

■ Company Outlook – Strong fundamentals make MMFS attractive

MMFS has transformed in the past decade from primarily a financing entity for vehicle purchases (from parent M&M) to a leading multi-product NBFC in India with a pan-India presence, deep penetration, and strong network with a rural focus. The company's subsidiaries namely Mahindra Rural Housing Finance (MRHF) are expected to be strong franchises in the long term. Its insurance broking business, Mahindra Insurance Brokers Limited (MIBL) is an asset-light broking business and has a strong fee income engine in its favour. We believe strong subsidiaries also add to the company's overall value.

■ Valuation – We maintain Buy on MMFS with a revised PT of Rs. 220

MMFS reported better-than-expected earnings largely on account of lower provisioning. Disbursements also picked up significantly with better collection efficiency signaling recovery in vehicle finance, which is encouraging. Further, management has unveiled its Vision 2025, which is expected to give it a fillip to deliver on earnings performance going ahead. Hence, given its strong liability franchise, leadership in rural financing along with strong parentage, the company is well on track to deliver on its aspirational goals. At the CMP, MMFS trades at 1.2x and 1.1x its FY2023E and FY2024E P/BV, respectively. Hence, we maintain our Buy recommendation on the stock with a revised PT of Rs. 220.

Peer valuation

Particulars	CMP (Rs / Share)	MCAP (Rs Cr)	P/BV(x)		P/E(x)		RoA (%)		RoE (%)	
			FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Mahindra Finance	180	22,172	1.2	1.1	11.7	10.0	2.3	2.4	11.4	11.9
Cholamandalam Investment	714	58,477	5.1	4.4	26.9	23.5	2.7	2.7	21.0	20.1

Source: Company; Bloomberg, Sharekhan Research

About company

MMFS is a subsidiary of Mahindra and Mahindra Limited. MMFS is one of India's leading non-banking finance companies focused in the rural and semiurban sector. The key business area is primarily of financing purchase of new and pre-owned auto and utility vehicles, tractors, cars, commercial vehicles, construction equipment, and SME financing. MMFS's vision is to be a leading provider of financial services in rural and semi-urban areas of India. The company has 1,388 offices across 27 states and 7 union territories in India, with over 7.3 million vehicle finance customer contracts since inception.

Investment theme

MMFS has grown and transformed as a business in the past decade from being primarily a financing entity for vehicle purchases (from its parent M&M) to a leading multi-product NBFC in India with a pan-India presence, deep penetration, and strong network with a rural focus. MMFS is deeply penetrated in 27 states/7 UTs through a network of >1,246 branches.

Key Risks

- Likely deterioration in asset quality and its exposure to the SME segment are vulnerable and may take longer time to recover.

Additional Data

Key management personnel

Mr. Ramesh Iyer	Vice Chairman & Management Director
Dr. Rebecca Nugent	Independent Director
Mr. Amit Raje	Non-Executive Non-Independent Director
Mr. Vivek Karve	Chief Financial Officer
Ms. Arnavaz M Pardiwalla	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	LIC of India	5.7
2	WISHBONE FUND LTD	2.7
3	HDFC Life Insurance Co Ltd	2.5
4	ICICI Prudential Asset Management Co Ltd	2.2
5	SBI Funds Management Ltd	2.2
6	BlackRock Inc	2.0
7	Kotak Mahindra Asset Management Co. Ltd	1.5
8	Vanguard Group Inc/The	1.5
9	HDFC Asset Management Co. Ltd	1.5
10	Nippon Life India Asset Management	1.2

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;