Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Mahindra & Mahindra Financial Services Ltd

Lower credit cost boosts profitability

NBFC	Sharekhan code: M&MFIN

Reco/View: Buy	↔	CMP: **Rs. 280**	Price Target: **Rs. 345**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

Summary

- M&M Finance reported strong profitability in Q3 at Rs. 553 crore (11% higher than our estimate) driven by significant decline in credit cost and higher other income.
- Credit cost (cal) reduced to 1.4% (vs 2.8% q-o-q) due to write-back of provisions. Gross stage 3 and stage 2 assets remained sequentially flat at 10% of AUM.
- NII grew by 7.0% q-o-q (vs 0.2% on q-o-q basis) on healthy NIM. NIM (cal) rose to 7.1% (7.0% q-o-q) driven by increase in yield on loans.
- At CMP, the stock trades at 1.7x/1.5x FY2025E/FY2026E BV estimates. We maintain Buy on M&M Finance with an unchanged TP of Rs. 345.

M&M Finance reported strong profitability growth in Q3 due to decline in credit cost and higher other income. NII grew by 9.4% y-o-y/7.0% q-o-q led by increase in margin. NIM (cal as of AUM) rose to 7.1% (vs 7.0%) due to increase in yield. Yield on loans rose to 14.7% (vs 14.6% q-o-q) while CoB remained elevated at 7.8%. Fee & other income remained strong at 21.0% y-o-y/34.7% q-o-q. Opex remained contained at 3.0% q-o-q and thus C/I ratio declined to 41.5% (vs 43.7% q-o-q) amid strong core income growth. Provisioning declined by 48% q-o-q due to write back of Rs. 121 crore of provisions on ECL model update. Credit cost (cal as a avg AUM) reduced to 1.4% (vs 2.8% q-o-q). PAT grew by 135% q-o-q to Rs. 553 crore (vs our estimate of Rs. 498 crore). However, PAT reduced by 12% y-o-y despite PPOP growth of 6.4% as write-back of provisions (Rs. 343 crore) was higher in year ago quarter. GS3/NS3 reduced 4.0%/1.5% (vs 4.3%/1.7% q-o-q). Meanwhile, GS2 assets/AUM rose to 6.0% (vs 5.8% q-o-q), however provisioning maintained at 11% against GS2. M&M Finance recorded highest quarterly disbursements of Rs. 15,436 crore (rose by 16% q-o-q) led by auto/UV, cars and CV/CEs segments. AUM rose by 25.5% y-o-y/3.5% q-o-q to Rs. 97,048 crore.

Key positives

- Decline in credit cost (1.4% vs 2.8% q-o-q)
- NIM (cal) rose to 7.1% (7.0% q-o-q)

Key negatives

- AUM growth remained weak sequentially despite strong disbursements growth.

Management Commentary

- Management retained credit cost guidance of 1.5-1.7% for FY24.
- Management lowered NIM guidance to 7.0% for FY24 (vs earlier at 7.5%)
- ECL model update led to decline in provisioning of Rs. 86 crore.
- **Vehicles loan growth outlook** – Management expects CV finance growth to remain strong over next two years, increase in ticket size are driving UV financing growth. Tractor segment growth is expected to remain sluggish.

Our Call

Valuation: We maintain Buy on M&M Finance with an unchanged price target of Rs. 345. At CMP, the stock trades at 1.7x/1.5x FY2025E/FY2026E BV estimates. We are positive on business outlook as growth is expected to remain healthy (>20% CAGR over FY23-26E) as the company is diversifying its growth engines and increasing its non-vehicle financing share in SME, LAP, and digital segments. We believe healthy NIM and contained credit cost along with strong growth to upgrade the ROA trajectory over 2.0% going forward. Assets quality outlook is expected to remain stable. Higher PCR of 62% on largely secured book also provides comfort on assets quality front. We estimated 19% CAGR in PAT over FY23-26E which will drive 370 bps expansion in RoE to 16.0%.

Key Risks

Elevated CoB, volatility in earnings and credit cost trajectory, slowdown in rural demand can lower business growth.

Company details

Market cap:	Rs. 34,563 cr
52-week high/low:	Rs. 346/216
NSE volume: (No of shares)	42.0 lakh
BSE code:	532720
NSE code:	M&MFIN
Free float: (No of shares)	59.3 cr

Shareholding (%)

Promoters	52.2
FII	12.7
DII	27.0
Others	8.1

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	1.5	14.3	-6.1	20.0
Relative to Sensex	0.0	3.3	-13.0	0.5

Sharekhan Research, Bloomberg

Valuation (standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E	FY26E
NII	5,555	6,106	6,625	8,482	10,390
Gr.	-7.7%	12.7%	22.3%	27.4%	22.5%
NIM	9.2%	8.7%	7.5%	7.7%	7.7%
C/I	35.8%	42.1%	41.8%	41.0%	39.2%
PPOP	3,725	3,752	4,098	5,310	6,701
A.PAT	989	1,984	1,690	2,639	3,365
RoE	6.5%	12.1%	9.7%	14.1%	15.9%
RoA	1.3%	2.3%	1.6%	2.0%	2.2%
Leverage (x)	5.0	5.2	6.1	6.9	7.4
AUM	64,916	82,770	1,03,311	1,29,272	1,57,881
P/E (x)	34.9	17.4	20.5	13.1	10.3
P/BV (x)	2.2	2.0	2.0	1.7	1.5

Source: Company; Sharekhan estimates

Key Result Highlights

In line AUM growth, disbursements picks-up

AUM rose by 25.5% y-o-y/3.5% q-o-q to Rs. 97,048 crore (in line with our estimates). The company-maintained leadership position in tractors, pre-owned vehicles, PV and three-wheelers. The company recorded highest quarterly disbursements of Rs. 15,436 crore (rose by 16% q-o-q) led by auto/UV (17.4% q-o-q), cars (21.1% q-o-q) and CV/CEs (16.5% q-o-q) segments. Management expects strong CV finance demand, diversification of book towards SME, PL and consumers loans to driven AUM growth.

Lower credit cost boosts profitability

PAT grew by 135% q-o-q to Rs. 553 crore (vs our estimate of Rs. 498 crore) led by lower credit cost and increase in NIM. NIM (cal as of AUM) rose to 7.1% (vs 7.0%) due to increase in yield. Yield on loans rose to 14.7% (vs 14.6% q-o-q). Credit cost (cal as a avg AUM) reduced to 1.4% (vs 2.8% q-o-q) due to Rs. 121 crore of provisioning write-back of which Rs. 86 crore was due to refinement of ECL model. Management retained credit cost guidance of 1.5-1.7% for FY24. CoB to remain elevated in coming quarters, though higher yield on loans to offset impact on margin.

Gross stage 3 assets decline

Assets quality improved as GS3/NS3 reduced 4.0%/1.5% (vs 4.3%/1.7% q-o-q). PCR on stage 3 assets stood at 62% which seems higher given the secured nature of the book. GS2 assets/AUM rose to 6.0% (vs 5.8% q-o-q), however provisioning maintained at 11% against GS2. GS3 and GS2 assets cumulatively stood flat at 10% of AUM. Management is optimistic towards assets quality outlook and expects contained credit cost. Management retained credit cost guidance of 1.5-1.7% for FY24.

Results Rs cr

Particulars	Q3FY23	Q2FY24	Q3FY24	YoY %	QoQ %
Interest Earned	2,795	3,154	3,373	20.7%	7.0%
Interest Expended	1,242	1,566	1,675	34.9%	6.9%
NII	1,553	1,587	1,698	9.4%	7.0%
Other Income	97	87	117	21.0%	34.7%
Total Income	1,650	1,674	1,815	10.1%	8.4%
Operating Expenditures	651	731	753	15.6%	3.0%
Pre- Prov Operating Profit	998	943	1,062	6.4%	12.7%
P&C	155	627	328	111.7%	-47.6%
PBT	843	316	734	-12.9%	132.1%
Tax	214	81	181	-15.3%	123.6%
Net Profit	629	235	553	-12.2%	135.2%
Dil. EPS	5.1	1.9	4.5	-12.2%	135.5%

Source: Company, Sharekhan Research

Balance sheet items Rs cr

Particulars	Q3FY23	Q2FY24	Q3FY24	YoY %	QoQ %
Disbursements	14,467	13,315	15,436	6.7%	15.9%
AUM	77,344	93,723	97,048	25.5%	3.5%
Loan book	73,400	89,948	93,392	27.2%	3.8%
Borrowings	57,053	79,059	79,781	39.8%	0.9%
Net worth (NW)	16,151	16,709	17,262	6.9%	3.3%

Source: Company, Sharekhan Research

Key operating ratios

Particulars	Q3FY23	Q2FY24	Q3FY24	Y-o-Y %	Q-o-Q %
NIM (cal)	8.2%	7.0%	7.1%	-	-
C/I ratio	39.5%	43.7%	41.5%	-	-
D/Ex	4.3	5.0	4.9	-	-
CAR (standa)	23.4%	18.7%	18.3%	-	-
Fee income/NII	3.6%	2.0%	2.6%	-	-

Source: Company, Sharekhan Research

Assets Quality Rs cr

Particulars	Q3FY23	Q2FY24	Q3FY24	Y-o-Y %	Q-o-Q %
GS3	4,589	4024	3852	-16.1%	-4.3%
GS3/AUM	5.9%	4.3%	4.0%	-	-
NS3	2,707	1562	1436	-47.0%	-8.1%
NS3/AUM	3.6%	1.7%	1.5%	-	-
PCR	41.0%	61.2%	62.7%	-	-

Source: Company, Sharekhan Research

AUM Break-out (as per rep. % share) Rs cr

Particulars	Q3FY23	Q2FY24	Q3FY24	Y-o-Y %	Q-o-Q %
AUM	77,344	93,723	97,048	25.5%	3.5%
Auto/utility vehicles	25,524	30,929	33,967	33.1%	9.8%
Tractors	11,602	12,184	12,616	8.7%	3.5%
Cars	15,469	17,807	18,439	19.2%	3.5%
CV/CEs	8,508	10,310	10,675	25.5%	3.5%
Pre-owned vehicles	9,281	11,247	12,616	35.9%	12.2%
SME	3,867	4,686	4,852	25.5%	3.5%
Others	3,094	6,561	3,882	-	-40.8%

Source: Company, Sharekhan Research

Disbursements Rs cr

Particulars	Q3FY23	Q2FY24	Q3FY24	Y-o-Y %	Q-o-Q %
Disbursements	14,467	13,315	15,436	6.7%	15.9%
Auto/utility vehicles	4,973	5,117	6,007	20.8%	17.4%
Tractors	2,035	1,280	1,677	-17.6%	31.0%
Cars	2,585	2,455	2,974	15.0%	21.1%
CV/CEs	1,596	1,511	1,761	10.3%	16.5%
Pre-owned vehicles	2,235	2,334	2,425	8.5%	3.9%
SME	828	432	442	-46.6%	2.3%
Others	214	186	150	-29.9%	-19.4%

Source: Company, Sharekhan Research

Outlook and Valuation

Sector view - Growth outlook encouraging

Retail credit demand remains robust, driven by a strong demand environment. Volumes continue to see uptick. Urban demand has been robust and recovered fully from pandemic-induced disruptions. There are some green shoots related to improvement in rural demand. Asset-quality trends are encouraging. NBFCs with a diverse product offering strategy, strong asset-liability management, robust liquidity buffers, strong risk management framework, and healthy liability franchise have ample growth opportunities and are well placed.

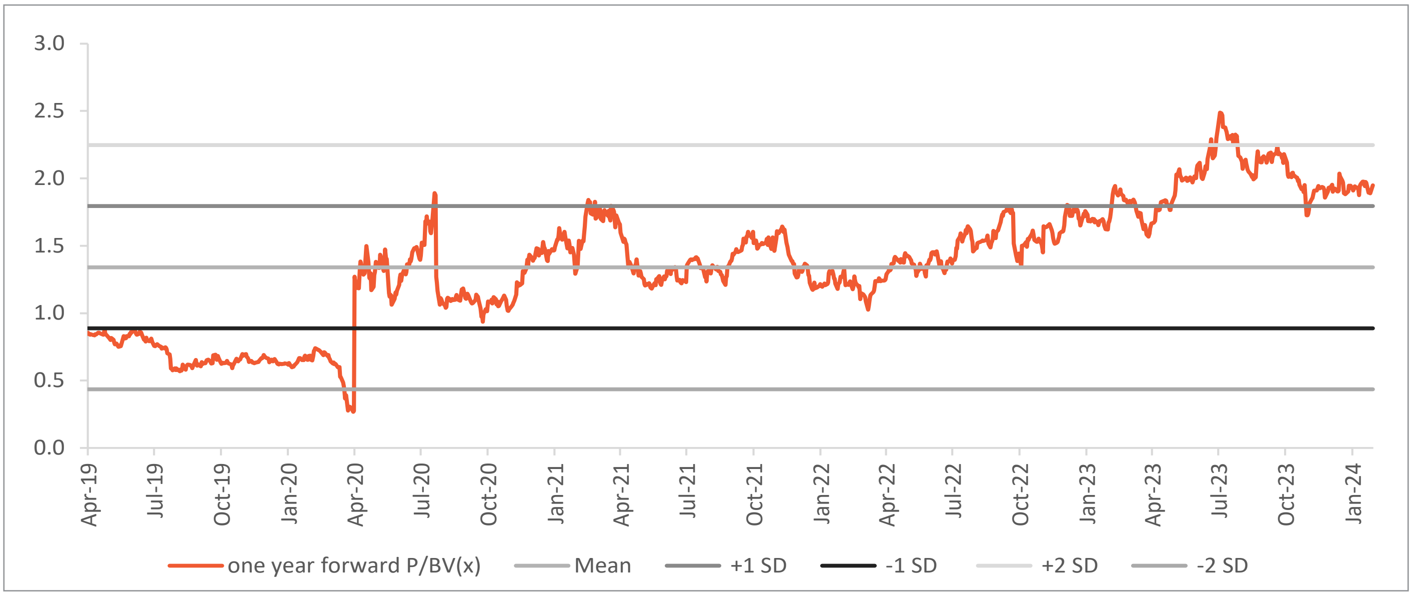
Company outlook - Better times ahead

Business momentum remains strong, as reflected in disbursement volumes. The company target to enhance business growth through a combination of core vehicles finance growth and diversification in to the new businesses like SME lending, LAP, leasing and digital lending. Besides propelling the growth, diversification is likely to strengthen the growth trajectory of the company. Earnings trajectory is also expected to be healthy. A majority of the clean-up has been done through accelerated write-offs in the past.

Valuation

We maintain Buy on M&M Finance with an unchanged price target of Rs. 345. At CMP, the stock trades at 1.7x/1.5x FY2025E/FY2026E BV estimates. We are positive on business outlook as growth is expected to remain healthy (>20% CAGR over FY23-26E) as the company is diversifying its growth engines and increasing its non-vehicle financing share in SME, LAP, and digital segments. We believe healthy NIM and contained credit cost along with strong growth to upgrade the ROA trajectory over 2.0% going forward. Assets quality outlook is expected to remain stable. Higher PCR of 62% on largely secured book also provides comfort on assets quality front. We estimated 19% CAGR in PAT over FY23-26E which will drive 370 bps expansion in RoE to 16.0%.

One-year forward P/BV (x) band



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs/ Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY24E	FY25E	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
M&M Finance	280	34,471	21.2	13.1	2.0	1.7	9.4	14.2	1.5	2.0
Cholamandalam	1,214	101,899	30.8	21.1	5.1	4.1	19.7	22.4	2.5	2.9

Source: Company; Sharekhan Research

About company

MMFS is a subsidiary of Mahindra and Mahindra Limited. The company is one of India's leading non-banking finance companies focusing on rural and semi-urban areas. The company finances the purchase of new and pre-owned auto and utility vehicles, tractors, cars, commercial vehicles, construction equipment, and SME Financing. The company has a strong network of 1,367 branches, spread across 27 states and 7 Union Territories in India.

Investment theme

Business momentum continues to remain strong, as reflected in disbursement volumes. We believe strong business growth is here to sustain, given the healthy underlying demand trends, the company's position in the rural/semi-urban customer segment, and better credit filters after pandemic-induced stress. The earnings trajectory is also expected to be healthy, as credit costs are expected to remain benign. A majority of the cleanup has been done through accelerated write-offs in the past.

Key Risks

Elevated CoB, volatility in earnings and credit cost trajectory, slowdown in rural demand can lower business growth.

Additional Data

Key management personnel

Mr. Ramesh Iyer	Vice Chairman and Management Director
Mr. Vivek Karve	Chief Financial Officer
Mr. Raul Rebello	Chief Operating Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	7.18
2	HDFC Assets Management Co. LTD.	2.84
3	ICICI Prudential Assets Management	2.73
4	HDFC Life Insurance Co Ltd.	2.46
5	SBI Funds Management Ltd	2.29
6	Vanguard Group Inc/The	1.85
7	Kotak Funds	1.79
8	KOTAK MAHINDRA ASSET MANAGEMENT CO LTD	1.70
9	Dhawan Ashish	1.18
10	Nippon Life India Asset Management	1.08

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

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