Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Mahindra & Mahindra Financial Services Ltd

Adjusted earnings broadly in line

NBFC		Sharekhan code: M&MFIN	
Reco/View: Buy	↔	CMP: **Rs. 260**	Price Target: **Rs. 345** ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Earnings were broadly in line adjusting for fraud provisions of ~Rs. 136 crore.
- The company has conducted stress test pan India across all its branches and concluded that there were no further adverse outcomes. The fraud at North-East branch is considered as an outlier by management.
- Asset quality trends were better led by higher write offs. GS3/GS2 assets reduced to 3.4%/5.0% vs 4.0%/6.0% q-o-q respectively. The company is targeting RoA expansion in FY25E led by yield improvement, fee, and lower credit cost.
- The stock trades at 1.6x/ 1.4x its FY2024E/FY2025E BV estimates, respectively. We maintain Buy with an unchanged PT of Rs. 345.

Net interest income (NII) at Rs. 1,812 crore (marginally above estimates) grew by 13% y-o-y/ 7% q-o-q. NIMs (cal.) improved by 14 bps q-o-q to 7.3%. Core fee income grew robustly by 64% y-o-y/ 76% q-o-q. Total operating expenses increased by 2% y-o-y /6% q-o-q. Opex to Avg. loans remained stable at 3.2% q-o-q. Operating profit grew by 24% y-o-y/ 10% q-o-q led strong revenue growth and contained opex growth. Provisions were higher than estimates at Rs. 342 crore. A one-time provision of Rs 136 crores was provided towards fraud. Total credit cost stood at 137 bps vs nil y-o-y and 138 bps q-o-q. Thus, PBT fell by 12% y-o-y/ up 13% q-o-q. PAT at Rs. 619 crore (below estimates mainly led by higher provisions) fell 10% y-o-y/ up 12% q-o-q. Loan assets grew by 24% y-o-y/ 6% q-o-q led by disbursements growth of 11% y-o-y/ down 1% q-o-q. Asset quality trends were better sequentially with GS-3/ NS-3 assets ratio at 3.4%/1.3% vs. 4.0%/1.5% q-o-q, respectively. GS2 assets were also lower at 5.0% vs. 6.0% q-o-q. PCR on Stage-3 assets stood at 63% stable q-o-q. Write-offs were at Rs. 602 crore vs Rs. 601 crore y-o-y and Rs. 449 crore q-o-q.

Key positives

- Core operational performance (ex. Net gain / (loss) on fair value changes) was strong, grew by 24% y-o-y/ 10% q-o-q.

Key negatives

- Higher write-offs q-o-q led to improvement in asset quality.
- Credit cost was higher led by one off provisions related to fraud.

Management Commentary

- The company is targeting RoA improvement by 50 bps in FY25E vs FY24 led by yield improvement driven by product mix, fee and lower credit cost.
- The company guided for 14-15% disbursement growth translating into 17-18% loan assets growth.
- The company has conducted stress test pan India across all its branches and concluded that there were no further adverse outcomes. The fraud at North-East branch was an outlier.
- It has also established fraud control unit to further strengthen underwriting & onboarding process. 50% of branches are centralized while 50% will become centralised in FY25E.

Our Call

We maintain buy with an unchanged PT of Rs. 345: The company is focusing on improving the product mix (increasing the share of used CV) resulting in yield improvement, increasing fee income, along with lower credit cost to support earnings however growth moderation, higher cost of funds may pose risk to earnings in FY25E. At the CMP, M&M Finance trades at 1.6x/ 1.4x its FY2025E and FY2026E ABV, respectively.

Key Risks

Slower loan growth, lower margins, and higher credit cost.

Valuation (standalone) Rs cr

Particulars	FY22	FY23	FY24	FY25E	FY26E
NII	5,555	6,106	6,682	8,482	10,390
PAT	989	1,984	1,760	2,639	3,365
EPS (Rs.)	8.0	16.1	14.3	21.3	27.2
ROA	1.3	2.3	1.7	2.0	2.0
ROE	6.5	12.1	10.0	14.1	15.9
P/E (x)	32.4	16.2	18.2	12.2	9.6
P/BV (x)	2.0	1.9	1.8	1.6	1.4

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		↔	

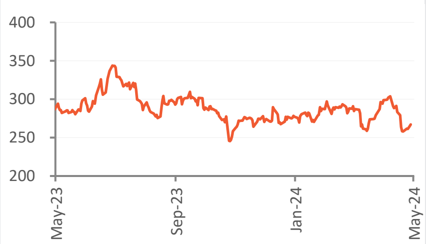
Company details

Market cap:	Rs. 32,105 cr
52-week high/low:	Rs. 346 / 244
NSE volume: (No of shares)	36.9 lakh
BSE code:	532720
NSE code:	M&MFIN
Free float: (No of shares)	59.3 cr

Shareholding (%)

Promoters	52.2
FII	12.0
DII	28.6
Others	7.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-13.0	-11.0	-1.1	-9.1
Relative to Sensex	-13.0	-13.4	-16.4	-29.5

Sharekhan Research, Bloomberg

Key result highlights

- **NIMs outlook:** Net interest income (NII) at Rs. 1,812 crore (marginally above estimates) grew by 13% y-o-y/ 7% q-o-q. NIMs (cal.) improved by 14 bps q-o-q to 7.3%. Cost of borrowings is expected to stabilize in H2FY25 thus to manage NIMs, loan mix is expected to be skewed towards pre-owned vehicles which have higher yield. The company is looking to optimise COF by diversifing the liability mix and also focusing on improving realisation through fee and distribution income.
- **Cost ratios to remain stable:** The company would continue to make investments in tech & digital, branch and distribution in calibrated manner, augment -risk, business and tech team.
- **Provisions higher led by one off:** Provisions were higher than estimates at Rs. 342 crore. A one-time provision of Rs 136 crores was provided towards fraud.
- **Asset-quality trends improved:** Asset quality trends were better sequentially led by higher write offs with GS-3/ NS-3 assets ratio at 3.4%/1.3% vs. 4.0%/1.5% q-o-q, respectively. GS2 assets were also lower at 5.0% vs. 6.0% q-o-q. PCR on Stage-3 assets stood at 63% stable q-o-q. Write-offs were at Rs. 602 crore vs Rs. 601 crore y-o-y and Rs. 449 crore q-o-q.
- **Loan growth outlook :** Loan assets grew by 24% y-o-y/ 6% q-o-q while disbursements were up 11% y-o-y/ down 1% q-o-q. Disbursements were healthy in PV/CV/CE segment and Pre owned vehicles while sharp decline was seen in tractor segment. Three wheelers and SME segment growth was flat. The company is guiding for 14-15% disbursement growth translating into 17-18% loan assets growth.
- **Return ratio guidance:** The company is targeting RoA improvement by ~50 bps in FY25E vs FY24 led by yield improvement driven by product mix, fee and lower credit cost.
- **Update on fraud:** The fraud was an outlier and was identified during a management review of the branch. The company had conducted stress test pan India across all its branches and concluded that there were no further adverse outcomes. This was a case of extreme collusion between the company's employees and external parties. The fraud involved forgery of KYC and other related documents leading to embezzlement of company funds. The company had appointed a law and accounting firm to undertake assessment of the irregularities. Based on the assessment by the accounting firm and the management, 2,887 loan accounts were identified fraudulent in nature with outstanding balance of Rs. 136 crore. With regards to the corrective measures, It has established fraud control unit to further strengthen underwriting & onboarding process. 50% of branches are centralized while 50% will become centralised in FY25E.

Results Rs cr

Particulars	Q4FY24	Q4FY23	y-o-y	Q3FY24	q-o-q
Net Interest Income	1,812	1,600	13%	1,698	7%
Other income	159	122	30%	117	36%
Net Income	1,971	1,723	14%	1,815	9%
Opex	798	779	2%	753	6%
Operating Profit	1,173	944	24%	1,062	10%
Provisions	341	0	NM	328	4%
PBT	832	944	-12%	734	13%
Tax	213	260	-18%	181	17%
PAT	619	684	-10%	553	12%

Source: Company, Sharekhan Research

Outlook and Valuation

Sector View – Moderate volume growth expectations

Passenger vehicles sales are expected to be in single digit in FY25 and CV volumes are expected to see gradual recovery after flat volume growth seen in FY24 as investments resumes in the infrastructure and construction/ real estate sector after general elections. There has been an increase in penetration in used CV. There are also some green shoots in rural economy which is giving hope for better demand Asset-quality trends are stable for the sector.

Company Outlook – Sustaining improved asset quality is key

Asset quality has seen improvement however trends have remained volatile in the past. Key monitorable remains collection trends and tightening of internal system & processes (due to recent fraud reported). The company expects to offset moderation in business growth with improvement in yields and fee income.

Valuation – We maintain buy with an unchanged PT of Rs. 345

The company is focusing on improving the product mix (increasing the share of used CV) resulting in yield improvement, increasing fee income, along with lower credit cost to support earnings however growth moderation, higher cost of funds may pose risk to earnings in FY25E. At the CMP, M&M Finance trades at 1.6x/ 1.4x its FY2025E and FY2026E ABV, respectively.

Peer valuation

Company	CMP (Rs / Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY25E	FY26E	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
M&M Finance	260	32,105	12.2	9.6	1.6	1.4	14.1	15.9	2.0	2.0
Cholamandalam	1,326	1,11,358	23.2	18.7	4.4	3.6	22.4	22.6	2.9	2.9

Source: Company, Sharekhan Research

About company

M&M Financial 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 1,402 branches, spread across 27 states and 7 Union Territories in India.

Investment theme

Asset quality has seen improvement however trends have remained volatile in the past. Key monitorable remains collection trends and tightening of internal system & processes (due to recent fraud reported). The company expects to offset moderation in business growth with improvement in yields and fee income.

Key Risks

Slower loan growth, lower margins, and higher credit cost.

Additional Data

Key management personnel

Mr. Raul Rebello	MD & CEO
Mr. Vivek Karve	Chief Financial Officer
Mr. Sandeep Mandrekar	Chief Business Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mahindra & Mahindra Ltd	52.16
2	Life Insurance Corp of India	9.89
3	HDFC Asset Management Co Ltd	3.58
4	HDFC Life Insurance Co Ltd	2.43
5	SBI Funds Management Ltd	2.22
6	Vanguard Group Inc/The	1.85
7	ICICI Prudential Asset Management	1.63
8	Kotak Mahindra Asset Management Co	1.59
9	Kotak Funds	1.53
10	Dhawan Ashish	1.18

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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