Stock Update

Manappuram Finance Ltd.

November 21, 2022

RETAILRESEARCH

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Manappuram Finance Ltd.

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Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
BFSI - NBFC	Rs 112	Buy in Rs 111-114 band & add more on dips in Rs 100-103 band	Rs 126	Rs 132	2 quarters

HDFC Scrip Code	MAGFIN
BSE Code	531213
NSE Code	MANAPPURAM
Bloomberg	MGFL IN
CMP Nov 18, 2022	111.9
Equity Capital (Rs cr)	169.3
Face Value (Rs)	2
Equity Share O/S (cr)	84.6
Market Cap (Rs cr)	9471
Book Value (Rs)	105.8
Avg. 52 Wk Volumes	62,11,000
52 Week High (Rs)	191.4
52 Week Low (Rs)	81.5

Share Holding Pattern % (Sep, 2022)	
Promoters	35.2
Institutions	40.6
Non Institutions	24.3
Total	100.0

* Refer at the end for explanation on Risk Ratings

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Our Take:

Manappuram Finance (MFL) has now prioritized profitability over loan book growth and stopped disbursing gold loans at extremely low teaser rates which were launched in competition with banks and other NBFCs during the pandemic to support loan book growth. Disbursement have improved across segment and barring microfinance segment (due to regulatory changes) AUM witnessed significant growth. The gold loan book is fully secured (gold being a fairly liquid asset) with LTV of 66% as on Q2FY23.

The non-gold loan book which accounts for ~37% of the AUM remains to be a cause of concern with high delinquencies. The management has also taken significant provisions over the last 4-5 quarters and credit costs are likely to moderate. Improvement in collection efficiency could free up provisions and recognition of interest would provide a higher yield. MFL has also started lending at higher rates after interest rate cap removal by RBI for MFI.

MFL has sufficient liquidity, it is well capitalized (~32% Tier 1 ratio), with strong ALM and access to diversified sources of funds. The management has guided for 10% gold loan AUM growth and 20% in other segments.

Valuation & Recommendation:

We expect the consolidated loan book of the company to grow at a CAGR of ~13% over FY22-FY24. PAT is expected to grow at ~15-16% CAGR as provisioning requirement could moderate going forward. The worst seems to be over for MFL as AUM growth returned, stress recognized and is expected to moderate, yields to stabilise at 20-21%. We believe MFL is available at an attractive valuation and if it can maintain steady growth in non-gold business and improve its asset quality over a period of time, it can be re-rating candidate. We feel investors could buy the stock in Rs 111-114 band and add on dips in Rs 100-103 band (0.8x FY24E ABV) for base case fair value of Rs 126 (1x FY24E ABV) and bull case fair value of Rs 132 (1.05x FY24E ABV) over next 2-3 quarters.

Financial Summary

Particulars (Rs cr)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	FY21	FY22	FY23E	FY24E
NII	1079	986	*9.4*	957	*12.8*	3971	3828	4132	4738
PPoP	642	603	*6.5*	509	*26.1*	2756	2270	2292	2719
PAT	418	370	*13.1*	282	*48.4*	1725	1329	1432	1767
EPS (Rs)	5.0	4.4	*13.4*	3.3	*48.8*	20.4	15.7	17.0	20.9
P/E (x)						5.5	7.1	6.6	5.3
P/ABV (x)						1.4	1.2	1.0	0.9
RoAA (%)						5.7	4.1	4.0	4.5

(Source: Company, HDFC sec)

Q2FY23 result update

MFL reported good set of numbers for Q2FY23 with consolidated PAT at Rs 419cr (+13/48% YoY/QoQ) on better than expected NII which came in at Rs 1079cr up 9%/13% YoY/QoQ due to run down of teaser loans and improvement in yields. Overall AUM grew by 8% YoY to Rs 30,665cr. However, it declined 0.3% sequentially as Gold loan AUM de-grew ~6% to Rs 19,190cr. Gold tonnage declined by similar percentage to 62.7 tonnes. LTV improved by 100bps QoQ to 66%. Asset quality for standalone business deteriorated significantly as GNPA/NNPA increased to 2.0%/1.8% from 1.4%/1.3% in Q1FY23.

The non-gold portfolio increased 17.3% to Rs 11,475cr. Non-gold AUM accounts for 37% of the book. Asirvad Microfinance performance continued to be under pressure as microfinance AUM de-grew 0.6% YoY to Rs 7,118cr and asset quality also deteriorated due to stress in restructured book with GNPA/NNPA coming in at 8.8%/1.7% vs 7.7%/1.9% in Q1FY23. GNPA improved in CV segment from 4.0% to 3.6% while it improved from 5.9% to 5.5% in home finance. Collection efficiency in MFI/Home/Vehicle/Others stood at 103%/98%/101%/107% respectively.

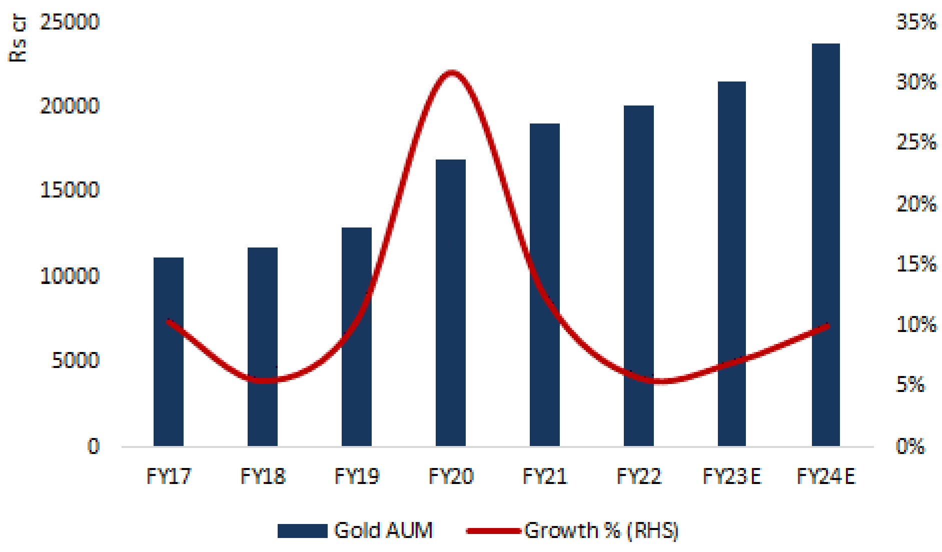
MFL carries Rs 520cr of ECL provision on books in microfinance business and has surplus liquidity across all businesses. MFL infused Rs 250cr in Asirvad Microfinance through a rights issue in Sep'22. Cash and cash equivalents on hand on a consolidated basis was Rs 5633cr and undrawn bank line was Rs 3368cr.

Key Triggers

Gold loan demand to pick up

Gold loans AUM growth suffered during the time of pandemic due to stiff competition from banks, who were offering gold loans at very low rates. Gold loan growth has started to pick up, and the company reported AUM of Rs 19,190cr in Q2FY23 (+2.5% YoY). The management expects the demand to increase in H2FY23 when the farmers go for purchasing fertilizer, sowing assets etc. ~25% of the loan book is still under teaser loans which would run down by Dec'22. LTV has increased to 66% from 62% in Q4FY22. It has guided for gold loan growth on ~5-10% in FY23. Gold loan AUM accounted for 63% of the consolidated AUM of the company.

Gold Loans growth



(Source: Company, HDFC sec)

Non-gold loans to grow at a faster rate

The non-gold loan portfolio witnessed a jump of 18.3% YoY in AUM to Rs 11,475cr primarily driven by significant jump in vehicle and other loans. We expect non-gold AUM to increase by ~20-25% in FY23. Collection efficiency in microfinance stood at 103% in Q2FY23. The vehicle finance AUM increased 49% YoY to Rs 1,886cr while other loans increased 187% YoY to Rs 1,549cr. Collection efficiency in other loans stood at 107%.

NIMs to expand

The company has stopped offering teaser rates on gold loans and focusing on profitability. Also, with the NIM cap removal by the RBI, the incremental disbursals in the micro finance portfolio is ~15% NIM from ~10% earlier. Additionally, MFL is negotiating with lenders to reduce the cost of borrowing in Asirvad. It has repaid some of the high cost borrowing with surplus liquidity. The consolidated cost of borrowing has declined by ~40bps YoY in Q2FY23 to 8.1%. However, with the increase in repo rates by the RBI overall borrowing costs is likely to increase, which will get passed on in lending rates.

Branch expansion on the cards

MFI is awaiting approval from the RBI to open newer branches. RBI had conducted an inspection and recommended some action points to work on. Once they are completed, it expects to get approval from the RBI to open newer branches. In the meantime, it is increasing gold loan lending from Asirvad.

Most of the stress recognized, credit costs to moderate

The management has taken significant provisioning over the past few quarters due to higher stress during the pandemic, especially in the MFI book. The company had restructured many accounts which have slipped into NPA in Q2FY23, leading to GNPA of 8.8% (stage II at 3.9%). It holds provision of Rs 520cr against stage II and Stage III loans and going forward it anticipates credit costs to moderate.

Sequentially GNPA deteriorated from 1.4% to 2.0% for gold loans in Q2FY23 but improved from 4% to 3.6% in vehicle finance and 5.5% to 5% in home finance.

Risks & Concerns

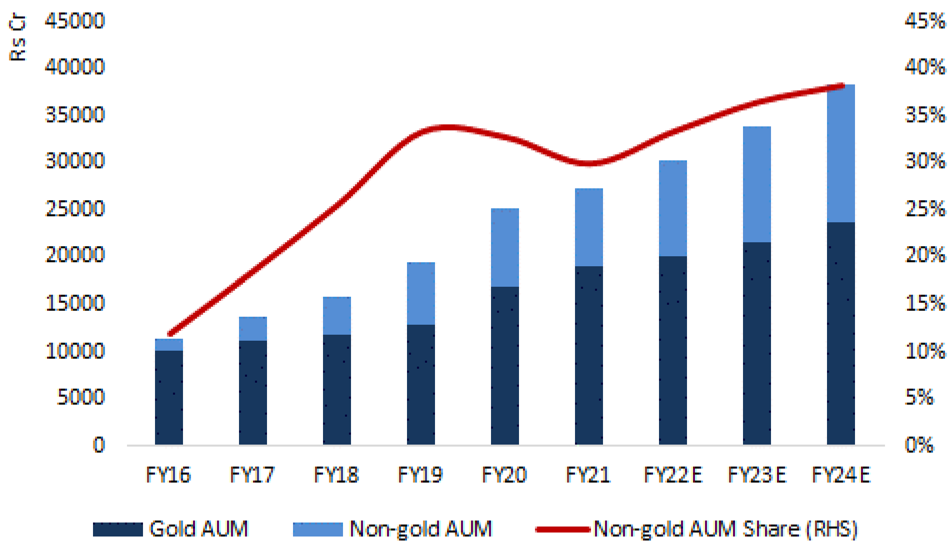
- Fluctuation in gold prices – A fall in these could lead to higher LTV and lower margin of safety.
- Overdependence on Gold loans – Despite its attempts to bring down dependence on Gold loans, Gold loan AUM is still 63% in Sep'22.
- Regulatory changes by Centre/State governments/RBI.
- Increase in delinquency in non-gold business leading to higher NPA – MFI, Housing Finance and Vehicle finance typically have higher slippages in difficult economic conditions.
- Emerging competition from other NBFCs and Banks who are entering Gold loan space – Gold loans seems to be the safest and most profitable businesses to most lenders and hence more and more of them keep entering it from time to time.

Company Background:

Promoted by Shri. V.P. Nandakumar, Manappuram Finance Ltd (MFL) was incorporated in 1992 and today is the second largest gold loan company in India. The Manappuram Group was started in 1949 by Late Mr. V. C. Padmanabhan, with focus primarily on money lending activities. To reduce its concentration risk in gold loans, MFL since FY16, has diversified into new business areas like microfinance, vehicle and housing finance, and SME lending. In February 2015, the company acquired Asirvad Microfinance Pvt. Ltd., which is one of the lowest cost microfinance lenders in India.

MFL is the second largest Gold loan company in organized gold loan market. Organised Gold loan market is 35% of the total gold loan market. There is a scope for shift of the market gradually from unorganised to organised going forward. Rise in gold prices allows higher lending on the same quantity of gold keeping the LTV intact.

AUM growth and breakup



(Source: Company, HDFC sec)

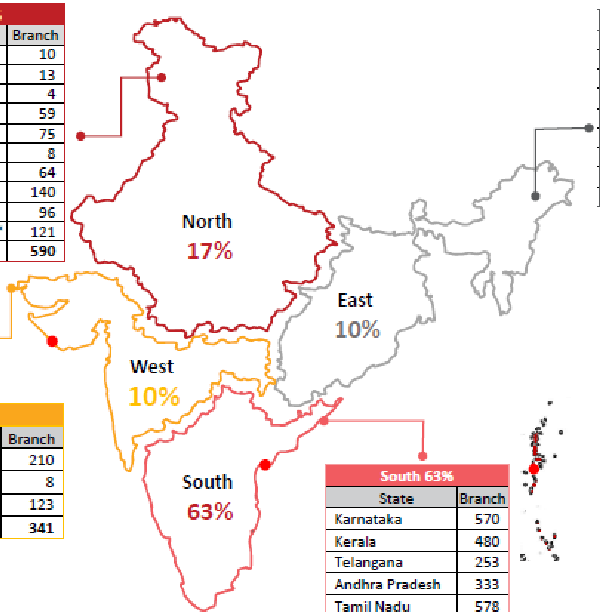
Besides microfinance, the company has also diversified into commercial vehicle loans, housing finance and SME loans with promising results. Put together, MFL had an AUM of Rs 11,475cr of non-gold loans. Overall, non-gold businesses contributed 37% of the total business as of Q2FY23.

As on Sep'22, MFL had 3,897 gold loan branches spread across India, with assets under management (AUM) of Rs 19,190cr. MFL has put in place adequate risk management systems. The branch employees have been trained to appraise gold jewellery provided as security against loans by prospective borrowers. The company has implemented systems for ensuring gold security and reducing custodial risks, including highly secured vaults with dual control and insurance of gold. All the branches are monitored by surveillance cameras. The core gold loan application software, which was developed in-house by the MAFIL team, is used by the branches and is linked to the financial software.

Pan India presence & Distribution network (Gold loan branches- Q2FY23)

North 17%

State	Branch
Jammu & Kashmir	10
Himachal Pradesh	13
Chandigarh	4
Delhi	59
Punjab	75
Uttarakhand	8
Haryana	64
Uttar Pradesh	140
Rajasthan	96
Madhya Pradesh**	121
Total	590



East 10%

State	Branch
Assam	18
Bihar	24
Tripura	2
Jharkhand	12
West Bengal	105
Chhattisgarh	51
Odisha	150
Total	362

Union Territories

State	Branch
Daman Diu	3
Andaman & Nicobar	5
Puducherry	9
Total	17

West 10%

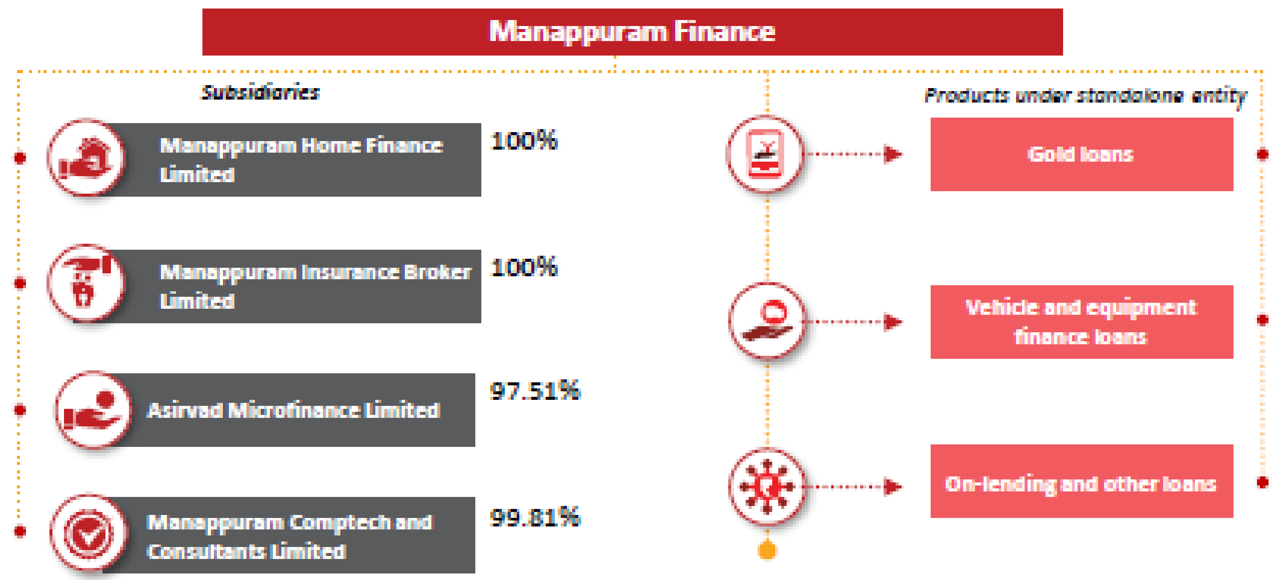
State	Branch
Maharashtra	210
Goa	8
Gujarat	123
Total	341

South 63%

State	Branch
Karnataka	570
Kerala	480
Telangana	253
Andhra Pradesh	333
Tamil Nadu	578
Total	2,214

**- Considering Madhya Pradesh in North Region

Group Structure



(Source: Company)

Financials

Income Statement

(Rs cr)	FY20	FY21	FY22	FY23E	FY24E
Interest Income	5217	6190	5840	6436	7404
Interest Expenses	1832	2219	2011	2304	2666
Net Interest Income	**3385**	**3971**	**3828**	**4132**	**4738**
Non interest income	334	185	287	231	261
Operating Income	**3719**	**4156**	**4115**	**4363**	**4999**
Operating Expenses	1474	1400	1845	2071	2279
PPoP	2245	2756	2270	2292	2719
Prov & Cont	238	440	486	370	348
Profit Before Tax	2007	2316	1784	1922	2372
Tax	527	591	455	490	605
PAT	**1480**	**1725**	**1329**	**1432**	**1767**
Adj. PAT	**1468**	**1724**	**1328**	**1434**	**1770**

Balance Sheet

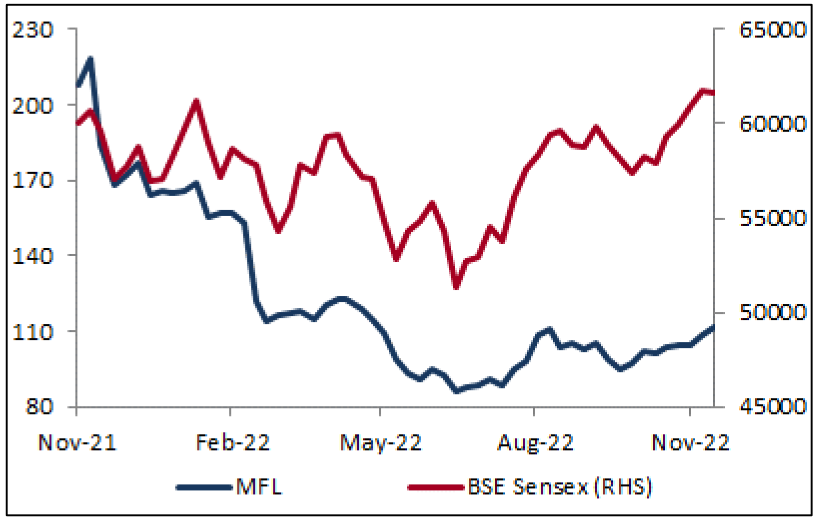
(Rs cr)	FY20	FY21	FY22	FY23E	FY24E
Share Capital	169	169	169	169	169
Reserves & Surplus	5577	7138	8199	9395	10874
Shareholder funds	**5746**	**7307**	**8368**	**9564**	**11044**
Minority Interest	58	47	16	18	21
Borrowings	20917	22716	24119	27070	30262
Other Liab & Prov.	2230	1267	1308	792	588
SOURCES OF FUNDS	**28951**	**31338**	**33811**	**37445**	**41915**
Fixed Assets	770	898	1029	946	952
Goodwill on Cons.	36	36	36	36	36
Investment	90	338	421	424	443
Cash & Bank Balance	3646	2912	2697	2609	2583
Advances	23189	26508	28971	32615	36904
Other Assets	1220	646	657	815	996
TOTAL ASSETS	**28951**	**31338**	**33811**	**37445**	**41915**

Ratio Analysis

As at March	FY20	FY21	FY22	FY23E	FY24E
Return Ratios (%)					
Calc. Yield on adv	25.4	24.9	21.1	20.9	21.3
Calc. Cost of borr	10.1	10.2	8.6	9.0	9.3
Calc. NIM	16.5	16.0	13.8	13.4	13.6
RoAE	28.6	26.4	16.9	16.0	17.2
RoAA	6.0	5.7	4.1	4.0	4.5
Asset Quality Ratios (%)					
GNPA	1.2	2.0	2.7	2.5	2.0
NNPA	0.9	1.1	1.9	1.6	1.1
Growth (%)					
Advances	30.2	14.3	9.3	12.6	13.2
Borrowings	36.8	8.6	6.2	12.2	11.8
NII	25.7	17.3	-3.6	7.9	14.7
PPoP	52.4	22.8	-17.6	1.0	18.6
PAT	59.3	16.5	-23.0	7.8	23.4
Per Share (Rs)					
EPS	17.4	20.4	15.7	17.0	20.9
Adj. BVPS	65.3	82.6	91.8	107.2	125.8
Dividend	2.2	2.0	3.0	2.8	3.4
Valuation Ratios					
P/E (x)	6.4	5.5	7.1	6.6	5.3
P/ABV (x)	1.7	1.4	1.2	1.0	0.9
Dividend Yield (%)	2.0	1.8	2.7	2.5	3.0
Other Ratios					
Cost-Income (%)	39.6	33.7	44.8	47.5	45.6
Leverage (x)	4.0	3.6	3.5	3.4	3.3
Opex-AUM	5.8	5.1	6.1	6.1	5.9

(Source: Company, HDFC sec)

Price Chart



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HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

Disclosure:

I, **Atul Karwa**, Research Analyst, **MMS,** authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. SEBI conducted the inspection and based on their observations have issued advise/warning. The said observations have been complied with. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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Any holding in stock – No

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