

Provisioning volatility continues

Mahindra Finance reported disappointing earnings for 2QFY24. NIMs compression due to rising CoB is NBFC wide narrative however Mahindra Finance faced twin challenges - yield compression (upgrade to better customer segment and high proportion of interest free advances this quarter) and rising CoB. 2Q witnessed higher credit costs due to rise in provisions and write-offs led by tractor segment which faced an erratic monsoon. Opex/avg assets (2.85%) stays above the management guidance of 2.5%. AUM growth continues to remain strong however its translation into profitability is unpredictable. 2H is expected to be better as (1) management has initiated yield hike in certain portfolio and large chunk of dealer financing is expected to be converted into yield earning assets; (2) recoveries have been historically better in 2H which may reflect in lower credit costs; however opex may continue to remain elevated. Management reiterated its willingness to meet FY25 guidance on RoA of 2.5% and Gross Stage 3 of <6%. Lower yields, elevated opex and credit costs may push the RoA target ahead in our view. We build in RoA/RoE of 2.1%/13.5% in FY25E. Post 5%/10%/52% miss on NII/PPOP/PAT in 2QFY24, we have cut our earnings estimate by 14% for FY24E and 7% for FY25E. We value Mahindra Finance at 2x (2.5x earlier) 1HFY26E P/ABV to arrive at our Target Price of Rs 302. Downgrade to an Accumulate

Increase in loan loss provisions hit earnings

Mahindra Finance reported loan loss provisions of Rs6.3bn, up 19% QoQ and 2.2x YoY. 44% of the provisions were attributable to the increase in ECL coverage while the rest 56% were write-offs. Credit costs (on avg assets) for 1H stood at 2.3% and management expects to contain it in the range of 1.5%-1.7% (on avg assets) in FY24E driven by recoveries in 2H. Stage 2 / Stage 3 assets stood at 5.8%/4.3% down from 9.7%/6.7% in 2QFY23 and 6.4%/4.3% in 1QFY24, respectively. 30+ dpd is down to 10.1%.

NIMs impacted by lower yield and increase in CoB

Reported spreads were down 100bps YoY and 30 bps QoQ to 6.5% as company moved up in terms of customer selection impacting yields. CoB continue to rise across companies and is expected to increase further in 2H. Management eluded to increasing lending yields in certain geographies and products as well as focus on high yielding products of tractors and two wheelers. In our view, competitive intensity may limit company's ability to raise lending yields in its target customer segment however, decline in share of dealer funding may positively impact yields next quarter. Calculated NIMs (on BS loans) was at 7.3%, down 140bps YoY and 46bps QoQ.

AUM growth continues to remain healthy, disbursement growth decelerates to 13%

Disbursements growth decelerated to 12.6% YoY after registering 28%+ YoY growth in previous 9 quarters. AUM growth remained strong, up 27% YoY and 8% QoQ to Rs 937 bn driver by strong disbursements in previous quarters and dealer financing in pre-festive quarter. Company expects to maintain AUM growth above 20% and will revisit guidance post festive season.

Financial and valuation summary

YE Mar (Rs mn)	2QFY24A	2QFY23A	YoY (%)	1QFY24A	QoQ (%)	FY24E	FY25E	FY26E
NII	16,455	15,170	8.5	16,341	0.7	69,693	83,908	97,722
PPoP	9,428	8,632	9.2	10,000	(5.7)	43,799	55,017	65,485
Provisions	6,266	1,980	216.4	5,264	19.0	17,762	20,073	22,897
PAT	2,352	5,032	(53.3)	3,527	(33.3)	19,267	25,859	31,515
AUM growth (%)	27.0	16.0	68.2	28.1	(4.1)	22.0	17.8	15.0
NIM (%)	7.3	8.7	(16.0)	7.8	(5.9)	7.6	7.6	7.6
C / I (%)	43.7	44.0	(0.7)	40.3	8.4	40.7	37.8	36.2
GNPA (%)	4.3	6.7	(35.9)	4.3	(1.2)	4.4	4.5	4.6
RoA (%)	0.9	2.2	(58.0)	1.4	(36.3)	1.8	2.1	2.2
RoE (%)	5.5	11.4	(52.0)	8.2	(33.1)	10.9	13.5	15.0
P/BV (x)	0.0	0.0	0.0	0.0	0.0	1.9	1.7	1.6

Source: Company, Centrum Broking

Result Update

India I NBFC

29 October, 2023

ADD

Price: Rs277

Target Price: Rs302

Forecast return: 9%

Institutional Research

Market Data

Bloomberg:	MMFS IN
52 week H/L:	347/191
Market cap:	Rs342.6bn
Shares Outstanding:	1235.5mn
Free float:	39.9%
Avg. daily vol. 3mth:	43,41,829

Source: Bloomberg

Changes in the report

Rating:	Changed from BUY to ADD
Target price:	Changed from Rs350 to Rs302
EPS:	FY24E; Changed by -14.3%
	FY25E; Changed by -7.1%

Source: Centrum Broking

Shareholding pattern

	Sep-23	Jun-23	Mar-23	Dec-22
Promoter	52.2	52.2	52.2	52.2
FIs	14.1	13.9	14.9	16.1
DIs	19.3	19.5	17.8	16.4
Public/other	14.4	14.4	15.1	15.3

Source: BSE

Centrum estimates vs Actual results

YE Mar (Rs mn)	Centrum Q2FY24	Actual Q2FY24	Variance (%)
NII	16,721	15,870	-5.1
PPOP	10,559	9,428	-10.7
PAT	4,873	2,352	-51.7

Source: Bloomberg, Centrum Broking



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Thesis Snapshot

Estimate revision

YE Mar (Rs mn)	FY24E New	FY24E Old	% chg	FY25E New	FY25E Old	% chg
NII	69,693	71,561	-2.6	83,908	85,307	-1.6%
PPoP	43,799	45,666	-4.1	55,017	56,416	-2.5%
PAT	19,267	22,445	-14.2	25,859	27,846	-7.1%

Source: Centrum Broking

MMFS versus NIFTY Midcap 100

	1m	6m	1 year
MMFS IN	(7.0)	8.0	33.7
NIFTY Midcap 100	(4.5)	21.7	24.8

Source: Bloomberg, NSE

Key assumptions

Y/E Mar	FY24E	FY25E
Disbursement growth	17.0%	15.0%
AUM growth	22.0%	17.8%
NIMs	7.6%	7.6%
C/I ratio	40.7%	37.8%
Credit costs	2.0%	1.9%

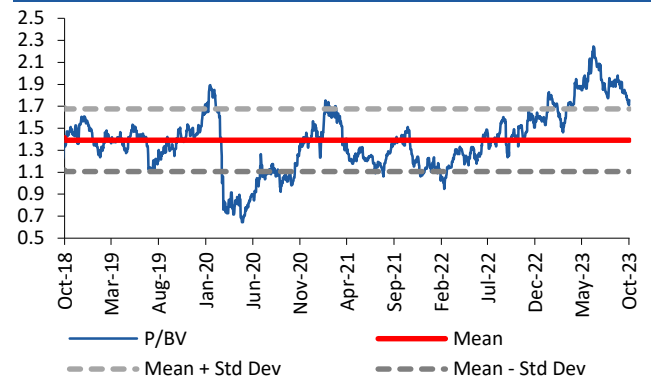
Source: Centrum Broking

Valuations

We build in RoA/RoE of 2.1%/13.5% in FY25E. Post 5%/10%/52% miss on NII/PPOP/PAT in 2QFY24, we have cut our earnings estimate by 14% for FY24E and 7% for FY25E. We value Mahindra Finance at 2x (2.5x earlier) 1HFY26E P/ABV to arrive at our Target Price of Rs 302. Downgrade to an Accumulate.

Valuations	Networth	Multiple	Value(Bn)	Value/Sh	% of Total
Core business	1,74,591	2.0	349	283	93.9
Mahindra Rural housing	17,811	1.0	18	14	4.8
Mahindra Insurance brokers			11	9	3.0
Total Value of Subsidiaries			29	24	7.8
Less: 20% holding discount			6	5	1.6
Value of Key Subsidiaries			23	19	6.2
Target Value Post 20% holding co Disc			372	302	100.0
CMP			343	277	-
Upside - %			9.1	9.0	-

P/BV mean and standard deviation



Peer comparison

Company	Market cap		P/B (x)			P/ABV(x)			RoE (%)		
	Rs bn	US \$bn	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
Cholamandalam	980.7	11.7	6.7	5.5	4.5	6.8	5.6	4.6	20.5	20.6	21.0
Shriram Fin	726.3	8.6	1.6	1.5	1.3	1.9	1.7	1.5	17.3	15.2	16.1
Sundaram Fin	355.7	4.2	4.1	3.7	3.3	4.3	3.8	3.4	14.9	14.8	15.4
Mahindra Fin	342.4	4.1	2.0	1.9	1.7	2.1	2.0	1.9	12.5	10.9	13.5

Source: Company, Centrum Broking

Key Concall takeaways

- Loan loss provision was high in 2QFY24 due to increase in stress in tractor portfolio which will self-correct in H2, once rural cash flows improve, in line with historical trends. The company remains confident of 1.5% to 1.7% credit costs for FY24E
- Tier 1 capital is down to 16.5% due to dividend payout, low profitability and strong AUM growth.
- Company remains confident of 20%+ AUM growth and will revisit guidance post festive season
- Interest yields were lower than anticipated due to (1) Rs 5000 crores of dealer finance in this quarter which carries no interest (2) change in customer mix towards affluent customers and (3) growth in low yield products of PV of Mahindra, CV and cars. Management expects yields to improve as it takes selective rate hikes in products and geographies and proportion of high yield products of tractors and pre-owned product increases. Dealer finance will convert into retail loans supporting yields. Lending rate hike will reflect slightly in Nov/Dec and reflect fully by 4QFY24.
- Management eluded to going wrong on its projection in CoB which it anticipated to go down in this year. It now expects CoB to remain slightly higher in H2 and start reducing from next year.
- NIMs (spread) are likely to increase to 6.8% by FY24 end and be at 7% in FY25E. Increase in yields across products will support NIMs growth over next 2 quarters while FY25E will have an added benefit of lower CoF
- Opex has remained high due to transformation agenda and will gradually come down to 2.5% by FY25 end/FY26E
- Gross stage 2 and gross Stage 3 stood at 5.7%/4.3% (this is partially aided by write-offs too). Stage 2/ Stage 3 PCR stood at 11.3%/61.2% with overall PCR on gross loans at 4%. ECL provisions are based on data for 42 months and remains high because of higher write-offs during covid period. As base gets corrected, PCR requirement will go down. Additionally, it draw comfort from low 30+dpd book of 10% and expect it to settle at 8.5% over next few quarters. Write-offs for the quarter stood at Rs 351 crores (1.6% of opening gross loans) and management expects recovery from this written-off pool
- Bridge to achieve March'25 target: Expect spreads at 7% (vs 7.5% set out initially), opex at 2.5%, credit costs at 1.5%, RoA at 2.25%

Exhibit 1: Quarterly performance

Y/E March (Rs mn)	Q2FY24	Q2FY23	Q1FY24	YoY (%)	QoQ (%)
Interest Income	31,535	25,163	30,349	25.3	3.9
Interest Expense	15,665	10,688	14,505	46.6	8.0
Net Interest Income	15,870	14,475	15,844	9.6	0.2
NIM (%)	7.3	8.7	7.8	-140bps	-46bps
Non Interest income	870	930	905	(6.5)	(3.9)
Total Income	16,740	15,405	16,750	8.7	(0.1)
Staff cost	4,368	3,762	4,174	16.1	4.7
Other Op Exp	2,944	3,011	2,577	(2.2)	14.3
Total Op Exp	7,312	6,773	6,750	8.0	8.3
Cost to Income (%)	43.7	44.0	40.3	-29bps	338bps
Pre-provision op profit	9,428	8,632	10,000	9.2	(5.7)
Provisions	6,266	1,980	5,264	216.4	19
PBT	3,163	6,652	4,735	(52.5)	(33.2)
Tax	811	1,620	1,209	(49.9)	(32.9)
-effective tax rate	25.6	24.4	25.5	129bps	11bps
PAT	2,352	5032	3527	(53)	(33.3)
Reported PAT	2,352	4,482	3,527	(47.5)	(33.3)
Borrowings	8,48,700	6,73,480	7,89,740	26.0	7.5
Gross Advances	9,37,230	7,38,170	8,67,320	27.0	8.1

Source: NBFC, Centrum Broking

Exhibit 2: Actual performance vs our estimates

(Rs mn)	Q2FY24A	Q2FY24E	Devi. (%)
Net Interest Income	15,870	16,721	(5.1)
PPOP	9,428	10,559	(10.7)
PAT	2,352	4,873	(51.7)

Source: NBFC, Centrum Broking

Exhibit 3: Financial Summary

Y/E March (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Net Interest Income	51,130	55,338	55,554	61,059	69,693	83,908	97,722
PPOP	33,982	41,512	37,252	37,518	43,799	55,017	65,485
PAT	9,064	3,291	9,888	20,388	19,267	25,859	31,515
P/E (x)	19	104	35	17	18	13	11
P/BV (x)	1.5	2.3	2.2	2.0	1.9	1.7	1.6
P/ABV (x)	2.0	2.7	2.4	2.1	2.0	1.9	1.7
EPS (Rs)	14.7	2.7	8.0	16.5	15.6	21.0	25.5
BV (Rs)	184.5	119.3	126.7	138.5	147.9	161.5	178.1
ABV (Rs)	136.2	104.5	114.3	129.6	137.2	147.8	162.2
Gross NPAs (%)	8.4	9.0	7.7	4.5	4.4	4.5	4.6
Net NPAs (%)	6.1	4.0	3.4	1.9	1.9	2.1	2.1
RoA (%)	1.3	0.4	1.3	2.4	1.8	2.1	2.2
RoE (%)	8.3	2.5	6.5	12.5	10.9	13.5	15.0

Source: NBFC, Centrum Broking

Exhibit 4: Estimate revision

Change in our estimates	Revised Estimates			Earlier Estimates			% Revision		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Net Interest income (Rs mn)	69,693	83,908	97,722	71,561	85,307	N/A	-2.60%	-1.60%	-
Operating Profit (Rs mn)	43,799	55,017	65,485	45,666	56,416	N/A	-4.10%	-2.50%	-
Profit after tax (Rs mn)	19,267	25,859	31,515	22,445	27,846	N/A	-14.20%	-7.10%	-
ABV (Rs)	137	148	162	138	149	N/A	-0.60%	-0.70%	-

Source: NBFC, Centrum Broking

Exhibit 5: Detailed Quarterly Financials

Y/E March (Rs mn)	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Interest Income	21,395	24,577	24,867	23,917	24,372	25,163	27,947	29,344	30,349	31,535
Interest Expense	10,179	10,151	9,514	9,357	9,320	10,688	12,419	13,340	14,505	15,665
Net Interest Income	11,216	14,426	15,353	14,560	15,052	14,475	15,528	16,004	15,844	15,870
NIM (%)	7.7	10.2	10.6	9.8	9.7	8.7	8.7	8.4	7.8	7.3
Non-Interest income	475	647	563	747	613	930	968	1,223	905	870
Total Income	11,691	15,073	15,916	15,306	15,666	15,405	16,496	17,227	16,750	16,740
Employee cost	2,698	2,788	3,027	3,200	3,532	3,762	3,997	4,552	4,174	4,368
Other Op Exp	1,505	2,122	2,266	3,127	2,676	3,011	2,518	3,233	2,577	2,944
Total Op Exp	4,203	4,910	5,294	6,327	6,208	6,773	6,515	7,786	6,750	7,312
Cost to Income (%)	36.0	32.6	33.3	41.3	39.6	44.0	39.5	45.2	40.3	43.7
Pre-provision op profit	7,488	10,163	10,622	8,979	9,458	8,632	9,981	9,441	10,000	9,428
Provisions	28,186	-3,668	-1,474	639	6,453	1,980	1,550	4	5,264	6,266
PBT	-20,698	13,831	12,096	8,341	3,005	6,652	8,431	9,437	4,735	3,163
Tax	-5,411	3,602	3,158	2,333	776	1,620	2,140	2,596	1,209	811
-effective tax rate (%)	26.1	26.0	26.1	28.0	25.8	24.4	25.4	27.5	25.5	25.6
PAT	(15,288)	10,229	8,938	6,008	2,229	5,032	6,291	6,841	3,527	2,352
Extraordinary items	-	-	-	-	-	550	-	-	-	-
Reported PAT	(15,288)	10,229	8,938	6,008	2,229	4,482	6,291	6,841	3,527	2,352
Gross Loans	6,35,820	6,36,180	6,39,440	6,49,610	6,76,930	7,38,170	7,73,440	8,27,700	8,67,320	9,37,230
Growth (%)	(6.0)	(6.1)	(3.9)	0.6	6.5	16.0	21.0	27.4	28.1	27.0
Disbursements	38,720	64,750	80,320	92,020	94,720	1,18,240	1,49,110	1,37,500	1,21,650	1,33,150
Growth (%)	42	61	28	54	145	83	86	49	28	13
Gross Stage 2 (%)	19.4	19.7	17.8	14.3	11.7	9.7	8.4	6.0	6.4	5.8
Stage 2 PCR (%)	12.2	13.6	12.7	12.7	11.5	11.0	10.7	10.6	10.9	11.3
Gross Stage 3 (%)	15.5	12.7	11.3	7.7	8.0	6.7	5.9	4.5	4.3	4.3
Stage 3 PCR (%)	53.7	53.0	53.2	58.1	58.1	58.2	59.0	59.5	60.1	61.2
Tier 1 Capital (%)	20.1	22.3	23.3	24.3	22.8	20.5	20.5	19.9	18.9	16.7
CAR (%)	23.8	26.1	26.8	27.8	25.9	23.8	23.4	22.5	21.2	18.7

Source: NBFC, Centrum Broking

P&L					
YE Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Interest income	94,756	1,06,826	1,34,436	1,59,376	1,85,613
Interest expense	39,202	45,767	64,742	75,468	87,892
NII	55,554	61,059	69,693	83,908	97,722
Other income	2,432	3,735	4,109	4,520	4,972
Total income	57,986	64,794	73,802	88,428	1,02,693
Operating expenses	20,734	27,276	30,003	33,411	37,208
Employee	11,714	15,843	17,427	19,518	21,860
Others	9,020	11,433	12,576	13,893	15,348
PPOP	37,252	37,518	43,799	55,017	65,485
Provisions	23,683	9,992	17,762	20,073	22,897
PBT	13,569	27,526	26,037	34,945	42,587
Tax	3,682	7,138	6,770	9,086	11,073
PAT	9,888	20,388	19,267	25,859	31,515

Ratios					
YE Mar	FY22A	FY23A	FY24E	FY25E	FY26E
Growth (%)					
AUM	0.5	27.4	22.0	17.8	15.0
Borrowings	(4.7)	34.3	21.5	18.1	15.1
NII	0.4	9.9	14.1	20.4	16.5
Other income	(2.7)	53.6	10.0	10.0	10.0
Opex	27.0	31.5	10.0	11.4	11.4
PPoP	(10.3)	0.7	16.7	25.6	19.0
Provisions	(36.6)	(57.8)	77.8	13.0	14.1
PAT	200.5	106.2	(5.5)	34.2	21.9
Profitability (%)					
Yield on advances	15.7	15.3	15.2	15.0	15.0
Cost of funds	6.9	7.0	7.8	7.6	7.6
NIM (on AuM)	8.6	8.3	7.6	7.6	7.6
Other Income/ Total Income	1.0	2.0	1.9	1.7	1.6
Other Income / Total Assets	0.1	0.1	0.1	0.1	0.1
Cost/Income	35.8	42.1	40.7	37.8	36.2
Employee	20.2	24.5	23.6	22.1	21.3
Others	15.6	17.6	17.0	15.7	14.9
Opex/ Avg AuM	3.2	3.7	3.3	3.0	2.9
Provisions	3.7	1.4	1.9	1.8	1.8
Tax Rate	27.1	25.9	26.0	26.0	26.0
RoA	1.3	2.4	1.8	2.1	2.2
RoE	6.5	12.5	10.9	13.5	15.0

DuPont (% avg assets)					
YE Mar	FY22A	FY23A	FY24E	FY25E	FY26E
Interest income	12.4	12.5	12.8	12.9	13.0
Interest expense	5.1	5.3	6.2	6.1	6.2
NII	7.3	7.1	6.6	6.8	6.9
Other income	0.3	0.4	0.4	0.4	0.3
Total income	7.6	7.6	7.0	7.2	7.2
Operating expenses	2.7	3.2	2.9	2.7	2.6
Employee	1.5	1.8	1.7	1.6	1.5
Others	1.2	1.3	1.2	1.1	1.1
PPOP	4.9	4.4	4.2	4.5	4.6
Provisions	3.1	1.2	1.7	1.6	1.6
PBT	1.8	3.2	2.5	2.8	3.0
Tax	0.5	0.8	0.6	0.7	0.8
PAT	1.3	2.4	1.8	2.1	2.2

Source: Company, Centrum Broking

Balance sheet					
YE Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Financial assets	7,30,353	9,22,754	10,93,728	12,77,306	14,62,395
Cash	41,504	28,321	9,509	5,770	5,278
Loans	6,04,446	7,94,547	9,74,344	11,50,674	13,24,168
Investment	84,403	99,886	1,09,875	1,20,862	1,32,949
Non-financial assets	22,534	39,411	45,323	50,247	55,722
Deferred tax assets	0	0	0	0	0
Fixed Assets	3,831	6,812	7,834	9,009	10,360
Other Non-fin. assets	18,703	32,599	37,489	41,238	45,362
Total Assets	7,52,887	9,62,166	11,39,051	13,27,553	15,18,117
Financial liabilities	5,58,139	7,49,459	9,10,602	10,75,396	12,37,540
Borrowings	5,58,139	7,49,459	9,10,602	10,75,396	12,37,540
Non-financial liabilities	38,467	41,818	46,000	52,900	60,834
Other Non-fin liabilities	38,467	41,818	46,000	52,900	60,834
Total equity	1,56,281	1,70,889	1,82,449	1,99,258	2,19,742
Share capital	2,466	2,467	2,467	2,467	2,467
Other equity	1,53,815	1,68,422	1,79,982	1,96,791	2,17,275
Total Liabilities	7,52,887	9,62,166	11,39,051	13,27,553	15,18,117
Balance Sheet ratios (%)					
Debt / Equity	3.6	4.4	5.0	5.4	5.6
Assets / Equity	4.8	5.6	6.2	6.7	6.9
Cash / Borrowings	7.4	3.8	1.0	0.5	0.4
Details on loans					
AUM	6,49,610	8,27,700	10,10,056	11,89,458	13,67,350
Disbursements	2,75,810	4,95,410	5,79,630	6,66,574	7,53,229
Capital Adequacy (%)					
CRAR	27.8	22.5	19.1	17.6	16.8
Tier-1	24.3	19.9	17.4	16.3	15.8
Tier-2	3.5	2.6	1.7	1.3	1.0
Asset quality (%)					
GNPA (Rs mn)	49,763	37,170	44,736	53,651	62,489
Growth (%)	(14.0)	(25.3)	20.4	19.9	16.5
NNPA (Rs mn)	20,860	15,070	18,789	24,143	28,120
Growth (%)	(14.3)	(27.8)	24.7	28.5	16.5
GNPA	7.7	4.5	4.4	4.5	4.6
NNPA	3.4	1.8	1.9	2.0	2.1
PCR	58.1	59.5	58.0	55.0	55.0
NNPA / Equity	13.3	8.8	10.3	12.1	12.8
Per share (Rs)					
EPS	8.0	16.5	15.6	21.0	25.5
BVPS	126.7	138.5	147.9	161.5	178.1
ABVPS	114.3	129.6	137.2	147.8	162.2
DPS	3.6	6.0	6.2	7.3	8.9
Valuation (x)					
P/E	34.5	16.8	17.7	13.2	10.8
P/BV	2.2	2.0	1.9	1.7	1.6
P/ABV	2.4	2.1	2.0	1.9	1.7
Dividend yield	1.3	2.2	2.3	2.6	3.2

Source: Company, Centrum Broking

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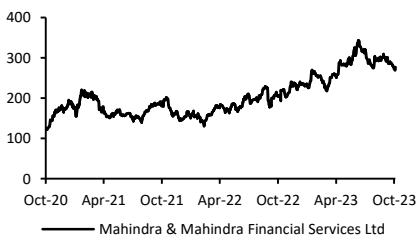
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M&M Financial Services



Source: Bloomberg

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