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Mahindra Finance Limited

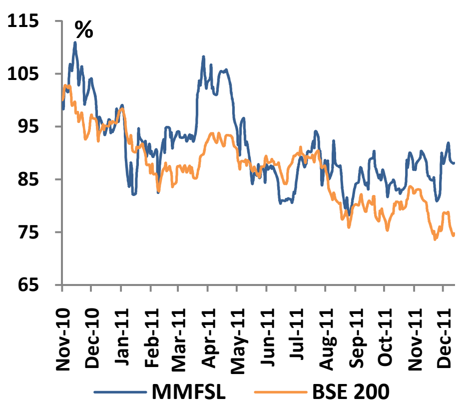
Rural Economy Still Holding High

CMP:	**Rs.658**
Target Price:	**Rs.768**
Recommendation:	**ACCUMULATE**

Stock Info	
BSE Group	A
BSE Code	532720
NSE Symbol	M&MFIN
Bloomberg	MMFS IN
Reuters	MMFS.BO
BSE Sensex	16003
NSE Nifty	4801

Market Info	
Market Capital	₹ 6955 cr
Equity Capital	₹ 104 cr
Avg. Trading Vol. (NSE Qtly)	84985
52 Wk High/ Low	835/590
Face Value	10

Shareholding Pattern (%)	**(30th Sept 2011)**
Promoters	57.4
Domestic Institutions	4.5
Foreign Institutions	34.5
Non Promoters Corp.	0.5
Public & Others	3.1
Govt. Holdings	-



December 14, 2011

We met Mahindra Finance management to get a feel of the operations in Q3 till date. Things are looking good in Q3 as the growth is robust, asset quality is good, Securitisation has begun and Insurance broking subsidiary has now been allowed to collect brokerage.

Growth – Remains healthy despite high base

- The growth prospects remain healthy as the rural economy is yet experiencing good cash flow. The cash purchase remains high as also the equity invested in assets which indicates that the fund position is good.
- Though overall passenger vehicle sales are down by 0.5% in FY12 till date, sales in rural markets are up 10%. MMFSL has also seen good growth and has infact increased its market share for Maruti from 19% in FY11 to 23% now. More and more car makers are stepping up their rural push. This all bodes well for MMFSL which has a good penetration in the rural market.
- Though the freight rates have softened, no alarming situation is anticipated by Co over a longer period.
- Growth is restricted to collection efficiency possible and the Co plans to grow by 25-30% in FY12. Otherwise the rural economy presents an opportunity to grow by even 40-50%.
- The growth in two months of this quarter has been quite robust despite a heavy base.

Margin – Marginal pressure ahead

- Change in product profile, increase in costs and absence of securitisation has seen a spread compression from 6.3% in FY11 to 4.9% in September. MMFSL could not pass the complete rise in cost to the customers.
- Further re-pricing of borrowings is expected to impact margins by another 15-20 bps.
- The interest subvention has come from few car manufacturers only resulting in lesser easing of margin pressure

Borrowing - Securitisation Begins

- The securitization of portfolio has begun as the Co is now getting favourbale rates and this quarter will see around Rs 650 cr of it. This is quite positive. Securitisation has been ~ 10-11% of MMFSL's total borrowing portfolio giving an advantage of 50-75 bps due to liquidity release.
- MF sponsored debentures have also resumed recently with rates like 10%-10.2%

Asset Quality – Remains under check

- The asset quality seasonally is better in H2 for MMFSL.
- As of now with demand, the asset quality is also looking pretty healthy.
- A bear case scenario may push it to at the most by 100 bps in H1 of FY12.

Subsidairy Co – Restriction removed

- Insurance Broking Co's income in the first half of FY12 was affected due to IRDA guideline in the beginning of the year which restricted payment of brokerage towards selling Group Life Insurance policies. The issue has now been resolved post several representations to IRDA and restriction has been removed w.e.f 1st December 2011.

Regulation Impasse–

- Minimum 12% Tier I – No major impact seen with present Tier I at 14.7%. It only advances frequency of capital raising.
- 90 day NPA recognition – At present NBFC's follow 180 days norm. Co expects Rs 30 - 35cr impact in P&L initially and ~150 bps on NPA. But some challenge will pose as the culture needs to be spread amongst customers. Increasing the loan schedule is not healthy and hence not envisaged.
- Securitisation – No clarity has emerged as yet. Representations are being made by industry to RBI. Co hopes for a practical solution or else the product will be useless for all.
- Priority Sector Lending – Co hopes that RBI looks at it constructively otherwise most hurt will be banks, especially foreign banks

The triggers for Co going forward will be - Monsoon, clarity on regulations, interest rate reversal and crude prices.

At CMP of Rs 658, the stock is available at price to book of 2.3x FY12 and 1.9x FY13. We have a price target of Rs 768 on the stock.

As of now we feel that the Co is in a sweet spot as it is a pure domestic play and that too rural economy which has seen very little impact of economic slowdown. The third quarter will be healthy YoY as well as QoQ. However the macro situation is getting very unpredictable, especially rupee dollar rate and hence "prospects of imported inflation". The increase in rates and slowing investment cycle may catch up faster and impact the rural economy. So we would recommend investing only on dips.

Rs in Cr	FY10	FY11P	FY12E	FY13E
Net Interest Income	1029	1314	1710	2225
Operating profits	742	859	1097	1415
Net Profit	344	463	579	751
NIM (%)(calculated)	13.2	12.4	11.7	11.6
Gross NPAs (%)	8.2	5.5	5.0	4.9
Net NPAs (%)	1.1	0.7	0.6	0.5
EPS	36	44	57	73
Book Value	180	243	288	349
RoA (%)	4.1	4.0	3.7	3.7
RoAE (%)	21.5	21.2	21.3	23.0
PE (x)	18.5	15.1	11.7	9.0
PBV (x)	3.7	2.7	2.3	1.9

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Stock Rating Scale

	Absolute Return
BUY	>20
ACCUMULATE	12-20
HOLD	5-12
REDUCE	<5