

Manappuram General Lease & Finance

BUY

Bearing the golden touch

Current price: Rs253

Table 1: Valuation (Rs mn)

Year ended	Net Interest Income	Other Income	Net Profit	EPS (Rs)	EPS growth (%)	P/E (x)	P/ABV (x)	RoE (%)	RoA (%)	DPS (Rs)
FY08	640	23	214	19.4	-	13.0	3.0	34.9	9.7	2
FY09	1,698	36	478	16.5	-14.9	15.3	2.9	27.3	4.9	1.5
FY10E	3,125	39	1,219	31.7	91.7	8.0	1.8	30.9	5.0	4.0
FY11E	4,461	47	1,975	51.3	62.0	4.9	1.4	33.9	5.0	8.7
FY12E	5,840	57	2,655	69.0	34.4	3.7	1.1	34.6	4.7	14.5

Source: BRICS Research

Major shareholders - Promoters: 45.7%, PE Investors: 32.2%, Public: 22.1%

Issued capital: 28.9mn shares of Rs10 each

Manappuram General Lease & Finance (MGF), India's largest gold-lending NBFC, has seen its loan book (Rs12.5bn) post 260% CAGR over FY06-FY09. Opportunity size of Rs2,000bn gives enough room for growth. MGF's single product strategy of lending against household jewellery is an opportunity to participate in the untapped potential of micro finance space in India. With 30% sustainable RoE, 60% book growth, and 31% CAR, we think MGF deserves premium valuation. BUY.

Faster processing of loans enables MGF to charge higher rates on sustainable basis

Manappuram enjoys a high level of spread inherent to the business - lending yields are high (~29%) backed by ~120% gold security. The unique advantage of Manappuram is its faster processing of applications (under fifteen minutes in many cases), while maintaining impeccable integrity on the gold appraisal/safe-keeping process, which dissuades customers from going to banks (although the lending yield is 14%). Besides, the smaller tenure of loan (~110 days, lent typically for harvest, festival, family function requirements) and smaller ticket size (~Rs15,000) make customers look at absolute amount of interest over rate of interest charged.

Favorable asset liability tenure provides business stability

MGF borrows mostly from banks with 1-year tenure, while its average lending period is ~110 days. This ensures that MGF has a positive asset liability management (ALM).

Gold NPAs of <0.3% ensure healthy balance sheet

MGF's current NPAs stand at 1.93%; of which gold NPAs are at 0.3% and the remaining NPAs are dominated by legacy auto finance assets (ceased in FY09). Given the company's strong gold appraisal/lending skills and emphasis on lending against household jewellery, we think asset quality is not likely to deteriorate anytime soon. Gold price risk is largely covered via the 85% maximum loan to value ratio on the collateral.

Strong technology an added advantage

Technology is a key differentiator between Manappuram and other unorganized money lenders. While traditional money lenders find it difficult to scale up business outside family, organized players like Manappuram rely on backend technology to control complete flow transactions - from loan origination to loan repayment. This ensures better management of treasury and MIS reporting. Also, management can track aggregate lending status of the company with a fifteen minute lag from the head office.

Margin to improve on higher branch capacity utilisation

As of March 2009, Manappuram operates 645 branches with gold loan portfolio of Rs12bn (~Rs20mn per branch). As the branches grow older, we expect capacity utilisation to improve to Rs50mn per branch by FY12, which would effectively ensure higher operating profit margin as operating costs grow slower than net interest income.

60% CAGR asset growth over FY09-FY12 to be the value driver

The merged entity (Manappuram General Finance and Manappuram Finance Tamilnadu) has an ABV of Rs89/share as of March 2009. At Rs482mn, the company's net profit for FY09 represents a 28% ROE. We believe this is sustainable and will improve, as the company has enough headroom to increase leverage and as branch utilization improves from the current levels of ~40% to ~80% by FY12. Loan book is expected to grow at a scorching pace; FY07-09 saw a 260% CAGR, while our FY09-12 estimates peg it at 60%, as MGF

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spreads across the country, targeting states such as Maharashtra, Andhra Pradesh, Karnataka and West Bengal in addition to Kerala and Tamil Nadu, where it has a sizable presence already.

Fund raising plans in FY10 will fund growth going forward

Our estimates indicate that if Manappuram wants to maintain CAR of ~ 18%, considering 60% CAGR in advances, it will have to raise capital of Rs1-2bn by end of FY10. As of now, marquee venture investors such as Sequoia, Hudson, Ashmore, Granite Hill hold about 23% acquired at Rs142/sh and Rs166/sh and this should provide comfort to new investors.

Valuation

At 30% sustainable RoE, 60% book growth and 31% CAR, we think MGF deserves premium valuation. At Rs253, the stock trades at P/E of 8x FY10E earnings and 1.8x FY10E ABV. Our price target is Rs350, assuming 2x P/ABV FY11E. Recommend BUY

Company Background

Manappuram General Finance (MGF) is India's largest gold-lending listed NBFC, with a book of Rs12.5bn, which has grown at 260% CAGR over the last three years. Some banks do have a larger gold loan book than Manappuram's (eg. Federal, SBT, SIB, etc) but gold lending is not a focus area for them. Total bank credit in this category ~ Rs300bn.

The business is inherently profitable as it competes with unorganized lending (small ticket, high yields ~29%, targets low income households). NIM for FY09 was over 20% aided by low leverage on books (~5.3x). Although cost-income ratio was a high 47%, RoA came in at 5.1%. Management sees loan book growth as the chief driver of value in Manappuram.

A group consolidation has been proposed wherein an unlisted company of the group in the same business (Manappuram Finance Tamilnadu) will merge with the listed company (Manappuram General Finance). The merged entity will have a net worth of Rs2.55bn, fully diluted equity capital of Rs 305mn (post conversion of 1.57mn warrants to promoters at Rs 167/sh, which will add Rs250mn to net worth) and a loan book of Rs12.5bn as of March 2009.

INCOME STATEMENT

(Rs mn)

Year ended 31 March	FY07	FY08	FY09	FY10E	FY11E	FY12E
Interest income	427	783	2,143	4,382	6,188	8,275
Interest expense	(90)	(144)	(445)	(1,256)	(1,727)	(2,435)
Net interest income	337	640	1,698	3,125	4,461	5,840
Non-interest income	15	23	36	39	47	57
Operating income	352	662	1,734	3,165	4,508	5,897
Core operating income	352	662	1,734	3,165	4,508	5,897
Operating expenses	(155)	(303)	(825)	(1,119)	(1,414)	(1,789)
Operating profit	197	359	909	2,046	3,094	4,107
Provision charges	(10)	(19)	(63)	(58)	(36)	(52)
Profit before tax and exceptionals	166	325	729	1,858	2,993	4,023
Exceptionals	0	0	0	0	0	0
Profit before tax	166	325	729	1,858	2,993	4,023
Tax provided	(59)	(112)	(251)	(639)	(1,018)	(1,368)
Net profit	108	214	478	1,219	1,975	2,655
Adjusted profit	108	214	478	1,219	1,975	2,655

BALANCE SHEET

(RS MN)

Year ended 31 March	FY07	FY08	FY09	FY10E	FY11E	FY12E
Cash & bank balances	219	679	2,677	5,629	7,229	9,205
Net advances	967	1,856	4,831	9,662	14,491	20,287
Investments	24	24	11	11	11	11
Other investments	24	24	11	11	11	11
Interest earning assets	1,209	2,559	15,188	30,641	44,740	61,715
Fixed assets	107	163	333	383	440	507
Other assets	155	202	878	1,310	1,959	2,931
Total assets	1,472	2,925	16,402	32,335	47,140	65,153
Borrowings	685	1,661	5,558	10,990	16,485	23,236
Other liabilities	253	242	561	636	693	756
Total liabilities	1,186	1,987	13,837	27,014	40,237	56,255
Shareholders funds	286	938	2,565	5,320	6,903	8,897
Capital	110	110	289	385	385	385
Reserves and surpluses	136	320	2,260	4,935	6,518	8,513
Total liabilities and equity	1,472	2,925	16,402	32,335	47,140	65,153

Year ended 31 March	FY07	FY08	FY09	FY10E	FY11E	FY12E
Basic data						
No. of shares outstanding	11	11	29	38	38	38
Avg. no. of shares outstanding	11	11	29	38	38	38
Market capitalisation	473	1,752	3,674	9,739	9,739	9,739
Per share data						
EPS	9.8	19.4	16.5	31.7	51.3	69.0
Adj. EPS	9.8	19.4	16.5	31.7	51.3	69.0
DPS	1.8	2.0	1.5	4.0	8.7	14.5
BVPS	26	85	89	138	179	231
Profitability						
RoE (%)	75.4	34.9	27.3	30.9	32.3	33.6
Adj. RoE (%)	75.4	34.9	27.3	30.9	32.3	33.6
RoA (%)	14.6	9.7	4.9	5.0	5.0	4.7
Adj. RoA (%)	14.6	9.7	4.9	5.0	5.0	4.7
Growth ratios						
Operating income growth (%)		88.0	161.8	82.5	42.4	30.8
Core operating income growth (%)		88.0	161.8	82.5	42.4	30.8
Operating cost growth (%)		95.8	171.9	35.7	26.4	26.6
Operating profit growth (%)		82.0	153.3	125.0	51.2	32.7
Net profit growth (%)		98.3	123.8	155.1	62.0	34.4
EPS growth (%)		98.3	-14.9	91.7	62.0	34.4
Adj. EPS growth (%)		98.3	-14.9	91.7	62.0	34.4
BVPS growth (%)		228.3	3.9	55.9	29.7	28.9
Advances Growth (%)		92.0	160.3	100.0	50.0	40.0
Yields						
Yield on advances (%)	42.8	54.6	29.2	28.0	26.0	25.0
Cost of deposits						
Cost of liabilities (%)	19.3	10.7	12.1	15.1	12.5	12.2
NIM (%)	55.7	33.9	19.1	13.6	11.8	11.0
Interest spread (%)	0.0	0.0	17.0	16.0	15.0	14.0

Year ended 31 March	FY07	FY08	FY09	FY10E	FY11E	FY12E
Dupont analysis						
Net interest income (%)	45.8	29.1	17.6	12.8	18.9	17.9
Non-interest income (%)	2.1	1.0	0.4	0.2	0.2	0.2
Trading profit (%)	0.0	0.0	0.0	0.0	0.0	0.0
Operating income (%)	47.9	30.1	17.9	13.0	19.1	18.1
Operating costs (%)	-21.1	-13.8	-8.5	-4.6	-6.0	-5.5
Pre-provision profits (%)	26.8	16.3	9.4	8.4	13.1	12.6
Provisions (%)	-1.3	-0.9	-0.6	-0.2	-0.2	-0.2
PBT (%)	22.6	14.8	7.5	7.6	12.7	12.3
Tax (%)	-8.0	-5.1	-2.6	-2.6	-4.3	-4.2
ROA (%)	14.6	9.7	4.9	5.0	5.0	4.7
Leverage (%)	515.2	359.3	551.8	618.1	682.9	732.3
ROE (%)	75.4	34.9	27.3	30.9	33.9	34.6
Asset quality						
Gross NPLs	31	171	243	256	299	406
Net NPLs	12	111	144	149	207	286
Gross NPLs (%)	0.6	2.2	1.9	1.0	0.8	0.8
Net NPLs (%)	0.2	1.4	1.2	0.6	0.6	0.5
PL provisions/avg. loans (%)	1.0	1.3	0.9	0.8	0.3	0.3
Inc. NPA/avg. loans (%)	0.0	0.0	0.0	0.3	0.3	0.3
Capitalisation ratios						
Tier 1 capital	336	1,276	2,504	5,320	6,903	8,897
Tier 2 capital	139	239	523	784	1,177	1,765
CAR	475	1,515	3,027	6,105	8,079	10,662
Risk weighted assets	2,361	3,975	7,560	25,002	37,500	52,499
Tier 1 ratio (%)	14.2	32.1	33.1	21.3	18.4	16.9
Tier 2 ratio (%)	5.9	6.0	6.9	3.1	3.1	3.4
Capital Adequacy ratio (%)	20.1	38.1	40.0	24.4	21.5	20.3

VALUATIONS

Year ended 31 March	FY07	FY08	FY09	FY10E	FY11E	FY12E
P/E	25.8	13.0	15.3	8.0	4.9	3.7
P/Adj. E	25.8	13.0	15.3	8.0	4.9	3.7
P/BV	9.7	3.0	2.9	1.8	1.4	1.1
Dividend yield	0.7	0.8	0.6	1.6	3.4	5.7

TL shows an effort to hold before Budget

Technical View

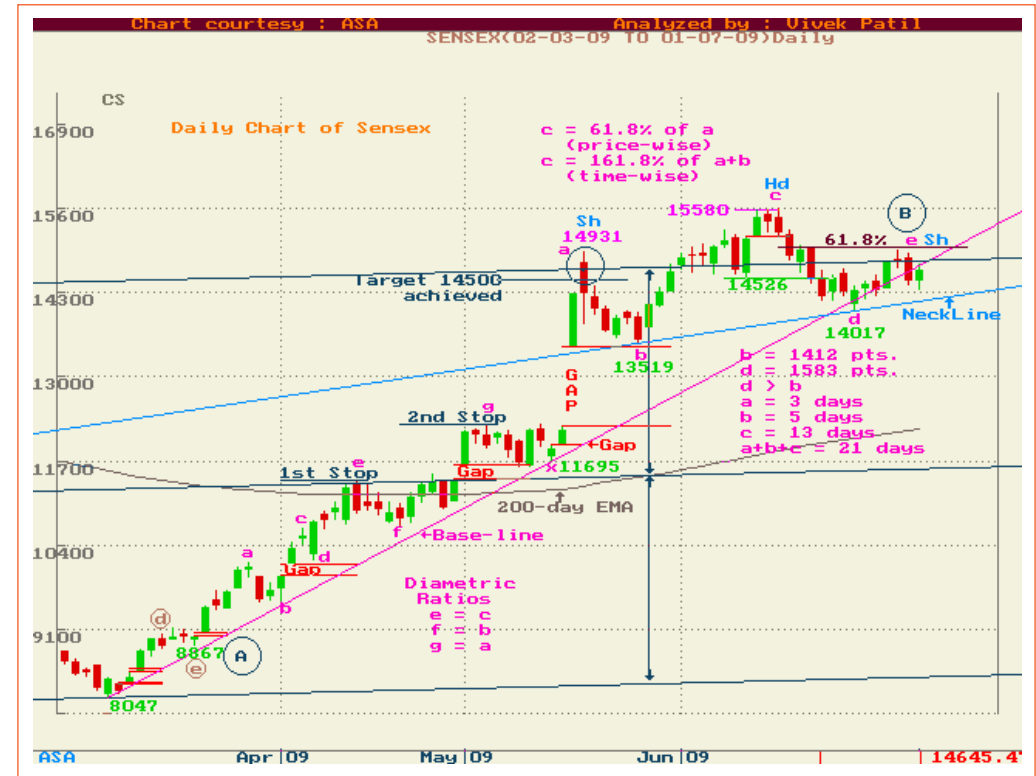
Yesterday we watched immediate supports for Sensex at 14420 - 14261. Sensex traded volatile. Initially up 154, it suddenly tanked 293 points, only to recover 372 points in the latter half. Its low, at 14356, held the immediate supports I had mentioned. The net result was a gain of 1% for the day. Realty Index bounced back 4.2%. Small-Cap Index closed flat, however, with A/D turning marginally positive. The action formed a Thrusting Line pattern, which can be seen as an attempt to hold the market before the Budget. This pattern can be bearish on failure to sustain above its head at 14727. A sustained move above the head can, however, see positive attempts, perhaps to reach levels closer to the 61.8% level once again.

In the recent past, a similar H&S formation or Extracting Triangle was formed during Jul-Sep'2008. Its Head was at 15580, and Right Shoulder at 15107. Within the Right Shoulder, 15107 level was attempted twice, before the Index tanked lower to 7697 by Oct'2008. A positive follow-up to Thrusting Line before Budget can generate a similar attempt.

Post-Budget, failure to reach levels higher than 61.8% retracement can see bearish effect of H&S formation. Remember, we are looking for a faster fall below the Neckline or below recent low of 14017 to confirm the bearish implications of the suspected H&S formation. This, as I said, can generate a drop to 50% retracement level to the current rally, seeking 12300-11800 levels.

Yesterday's action broke above the Intra-day falling channel for Tuesday's fall. Failure to trade above day's high at 14727 can lead to immediate weakness. However, sustaining above 14727 can see further attempts to reach towards 61.8% level.

Chart: BSE Sensex



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