

# 3Q: Earnings beat; Buy for growth, high return ratios

## 3Q: Earnings up 117% yoy driven by strong AUM growth

MGFL reported earnings of Rs1.6bn, a 117% yoy growth and +9% higher than est. driven by stronger than est. AUM growth of ~90% yoy (~15% qoq). Disbursements growth also strong at 86% yoy (Rs104bn) in 3Q, partly aided by higher gold prices. Average LTV (AUM) at ~69%. Moreover, spreads were stable qoq at <14%. Cost-inc. ratio more or less stable yoy at ~43%, despite +45% employee base yoy and +50% branches (2738 now) yoy. Asset quality is comfortable, with gross largely stable at ~45bps and net at ~19bps.

## Other variables too showing traction, key for future growth

The average loan outstanding per branch increased 24% yoy (6% qoq) to Rs45mn in 3Q. MGFL added 0.14mn customers in 3Q12 (total customer base now at 1.6mn). The company opened 235 branches in 3Q12 (943 branches in the last 12 months), taking its total branches to 2,738.

## Buy for growth, high RoAs and rising RoEs

We have raised earnings by +9/4% for FY12/13 post the 3Q surprise. We estimate net profit growth at +94/28% over FY12/13 driven by AUM growth (+45% CAGR over FY11-13) and operating leverage (+35% of branches added in last 1 year). Hence, RoAs to remain high (+4.5%) and RoEs to improve (~22% in FY11 to +26% in FY13), as an improvement in operational efficiency would largely mitigate adverse impact of margin compression ahead (est. ~100bps compression over FY11-13). Our FY12/13 est. factors in 1.0% gross NPLs / credit costs at +50-60bps (<20bps now). Hence, we believe stock trading at ~2.2x FY12E book may likely trade at similar multiples one-year out (FY13), implying a PO of Rs80.

## Estimates (Mar)

(Rs)	2010A	2011A	2012E	2013E	2014E
Net Income (Adjusted - mn)	1,197	2,827	5,493	7,056	8,434
EPS	2.03	3.93	6.56	8.43	10.07
EPS Change (YoY)	83.8%	93.2%	67.0%	28.5%	19.5%
Dividend / Share	0.282	0.600	1.00	1.30	1.60
Pre-exceptional EPS	2.03	3.93	6.56	8.43	NA
Pre-exceptional EPS Change (YoY)	83.8%	93.2%	67.0%	28.5%	-100.0%
Book Value / Share	8.97	23.08	28.50	35.45	43.70

## Valuation (Mar)

	2010A	2011A	2012E	2013E	2014E
P/E	29.0x	15.0x	9.0x	7.0x	5.8x
Dividend Yield	0.479%	1.02%	1.70%	2.21%	2.72%
Pre-exceptional PE	28.95x	14.99x	8.97x	6.98x	NA
Price / Book	8.07x	2.56x	2.07x	1.67x	1.35x
RoE / PB	3.85x	8.71x	12.32x	15.87x	18.90x
Price / Pre-Provision Profit	17.68x	10.66x	5.49x	4.31x	NA

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## Stock Data

Price	Rs58.85
Price Objective	Rs80.00
Date Established	4-Nov-2011
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs41.70-Rs72.50
Mrkt Val / Shares Out (mn)	US\$1,003 / 837.4
Market Value (mn)	Rs49,282
Average Daily Volume	1,121,990
BofAML Ticker / Exchange	XMGPF / BSE
Bloomberg / Reuters	MGFL IN / MGFL.BO
ROE (2012E)	25.5%
Total Dbt to Cap (Mar-2010A)	NA
Est. 5-Yr EPS / DPS Growth	40.0% / 40.0%
Free Float	63.6%

## Key Changes

(Rs)	Previous	Current
2012E EPS	6.02	6.56
2013E EPS	8.10	8.43
2014E EPS	10.15	10.07

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## iQprofile<sup>SM</sup> Manappuram

Key Income Statement Data (Mar)	2010A	2011A	2012E	2013E	2014E
<b>(Rs Millions)</b>					
Net Interest Income	3,371	8,478	15,836	21,139	26,877
Net Fee Income	107	181	307	520	858
Securities Gains / (Losses)	NA	NA	NA	NA	NA
Other Income	0	0	0	0	0
<b>Total Non-Interest Income</b>	<b>106.91</b>	<b>181.14</b>	<b>306.91</b>	<b>520.00</b>	<b>858.01</b>
Total Operating Income	3,477	8,659	16,143	21,659	27,735
Operating Expenses	(1,517)	(4,037)	(7,164)	(10,234)	(14,043)
<b>Pre-Provision Profit</b>	<b>1,960</b>	<b>4,622</b>	<b>8,978</b>	<b>11,425</b>	<b>13,692</b>
Provisions Expense	(88.58)	(133.81)	(180.64)	(198.71)	(238.45)
<b>Operating Profit</b>	<b>1,872</b>	<b>4,488</b>	<b>8,798</b>	<b>11,226</b>	<b>13,453</b>
Non-Operating Income	(53.42)	(248.94)	(560.12)	(644.13)	(805.17)
<b>Pre-Tax Income</b>	<b>1,818</b>	<b>4,239</b>	<b>8,238</b>	<b>10,582</b>	<b>12,648</b>
Net Income to Comm S/Hold.	1,197	2,827	5,493	7,056	8,434
<b>Adjusted Net Income (Operating)</b>	<b>1,197</b>	<b>2,827</b>	<b>5,493</b>	<b>7,056</b>	<b>8,434</b>

### Key Balance Sheet Data

Total Assets	25,477	77,691	135,384	175,171	224,021
Average Interest Earning Assets	14,313	47,102	99,507	147,503	191,438
<b>Weighted Risk Assets</b>	<b>23,305</b>	<b>71,622</b>	<b>147,131</b>	<b>203,545</b>	<b>272,048</b>
Total Gross Customer Loans	18,907	64,142	120,727	160,383	208,330
Total Customer Deposits	NA	NA	NA	NA	NA
<b>Tier 1 Capital</b>	<b>6,072</b>	<b>19,209</b>	<b>23,734</b>	<b>29,530</b>	<b>36,413</b>
Tangible Equity	6,834	21,224	27,395	34,569	43,412
<b>Common Shareholders' Equity</b>	<b>6,106</b>	<b>19,240</b>	<b>23,761</b>	<b>29,555</b>	<b>36,435</b>

### Key Metrics

Net Interest Margin	23.55%	18.00%	15.91%	14.33%	14.04%
<b>Tier 1 Ratio</b>	<b>26.1%</b>	<b>26.8%</b>	<b>16.1%</b>	<b>14.5%</b>	<b>13.4%</b>
Effective Tax Rate	34.2%	33.3%	33.3%	33.3%	33.3%
Loan / Assets Ratio	74.2%	82.6%	89.2%	91.6%	93.0%
<b>Loan / Deposit Ratio</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>
Oper Leverage (Inc Growth - Cost Growth)	38.2%	-17.1%	9.0%	-8.7%	-9.2%
Gearing (Assets / Equity)	4.2x	4.0x	5.7x	5.9x	6.1x
Tangible Common Equity / Assets	26.8%	27.3%	20.2%	19.7%	19.4%
Tangible Common Equity / WRAs	29.3%	29.6%	18.6%	17.0%	16.0%
Revenue Growth	166.4%	149.0%	86.4%	34.2%	28.1%
Operating Expense Growth	128.2%	166.1%	77.5%	42.9%	37.2%
Provisions Expense Growth	46.9%	51.1%	35.0%	10.0%	20.0%
Operating Revenue / Average Assets	21.7%	16.8%	15.2%	13.9%	13.9%
Operating Expenses / Average Assets	9.5%	7.8%	6.7%	6.6%	7.0%
<b>Pre-Provision ROA</b>	<b>12.2%</b>	<b>9.0%</b>	<b>8.4%</b>	<b>7.4%</b>	<b>6.9%</b>
ROA	7.5%	5.5%	5.2%	4.5%	4.2%
<b>Pre-Provision ROE</b>	<b>50.8%</b>	<b>36.5%</b>	<b>41.8%</b>	<b>42.9%</b>	<b>41.5%</b>
ROE	31.0%	22.3%	25.5%	26.5%	25.6%
RoTE	17.5%	13.3%	20.1%	20.4%	19.4%
RoWRAs	5.1%	3.9%	3.7%	3.5%	3.1%
Dividend Payout Ratio	13.8%	15.2%	15.2%	15.4%	15.8%
<b>Efficiency Ratio (Cost / Income Ratio)</b>	<b>43.6%</b>	<b>46.6%</b>	<b>44.4%</b>	<b>47.3%</b>	<b>50.6%</b>
<b>Total Non-Interest Inc / Operating Inc</b>	<b>3%</b>	<b>2%</b>	<b>2%</b>	<b>2%</b>	<b>3%</b>
Market-Related Revenue / Total Revenues	0%	0%	0%	0%	0%
Provisioning Burden as % of PPP	4.5%	2.9%	2.0%	1.7%	1.7%
NPLs plus Foreclosed Real Estate / Loans	1.8%	0.9%	0.7%	1.0%	1.0%
<b>Loan Loss Reserves / NPLs</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>
Loan Loss Reserves / Total Loans	NA	NA	NA	NA	NA
Provisions Expense / Average Loans	0.8%	0.3%	0.2%	0.1%	0.1%

### Other Metrics

Income / Employee	0.501	0.559	0.694	0.745	0.763
(Operating Expenses) / Employee	0.219	0.260	0.308	0.352	0.387
Pre-Provision Profit / Employee	0.282	0.298	0.386	0.393	0.377
Net Profit / Employee	0.173	0.182	0.236	0.243	0.232

### Company Description

Manappuram General Finance, the flagship company of Manappuram Group, is the leading gold-loan providing NBFC based out of Kerala, with assets under management of Rs65 bn and market share estimated at 7%. It is present in the (collateralised) micro-finance space (average ticket size of Rs25k), with the main line of business being lending against household jewellery. It does not provide loans to jewelers, banks, or against bullion.

### Investment Thesis

We like Manappuram owing to a strong earnings trajectory (earnings growth of +55% through FY10-13E), driven by MGFL capitalizing on US\$11bn market opportunity growing at +30-35% yoy. MGFL is better positioned vs. peers driven by rapidly rising distribution and proven expertise. Default risk is low for MGFL and asset quality is manageable (net NPLs at <0.2%) driven by strong risk management systems and sentimental value of collateral. Hence, above average RoAs (+4.9%E) and RoEs (+22%E) to sustain

### Stock Data

Price to Book Value 2.1x

## 3QFY12 Result Summary

Table 1: 3QFY12 Result Summary

Particulars	3QFY12	3QFY11	yoy growth	Remarks
Income from operations	7264	3296	120%	Strong AUM growth of 88% yoy, 15% qoq
Interest expended	2964	963	208%	Cost of borrowings up +325bps yoy
<b>Net Interest income</b>	<b>4300</b>	<b>2334</b>	<b>84%</b>	5% ahead of estimates; margins more or less stable yoy at ~14%
Other income	67	8	694%	
<b>Operating Income</b>	<b>4367</b>	<b>2342</b>	<b>86%</b>	
Staff cost	872	442	97%	
Other Exp	998	569	76%	
Operating Exp	1870	1011	85%	Addition of +940 branches and +6940 staff yoy
<b>PPP</b>	<b>2497</b>	<b>1331</b>	<b>88%</b>	4% higher than estimate
Provision	102	216	-53%	Asset quality comfort high; Net NPA (Gold loan) at 19bps (down 6bps qoq)
Pre-tax profit	2395	1115	115%	
Tax expenses	782	370	112%	
<b>PAT</b>	<b>1614</b>	<b>745</b>	<b>117%</b>	9% higher than estimates owing to stronger topline

Source: BoFA Merrill Lynch Global Research Estimates

## Price objective basis & risk

### Manappuram (XMGPF)

We set our PO at Rs80/shr. for MGFL. MGFL is the second largest NBFC with market share of +7-8% in organized segment. We believe the stock trading at +2.2-2.3x FY12E book will likely trade at similar multiples one-year out (FY13) given a) high earnings trajectory (+67/28% in FY12/13E), b) rising return ratios (ROEs to rise to +25.5% in FY12E and further to +26.5% in FY13E) and c) comfort on asset quality (gross only at 44bps). Our PO is based on Gordon theory multiples assuming RoE of 25%, CoE at 14% and sustainable growth of 6%), as growth potential for MGFL is strong. Our Rs80 price objective implies P/E of 9.5x FY13E EPS (trades at 9x FY12E earnings), with higher earnings trajectory. Risks to our price objective are a rise in theft and fraud and increase in competition, which can hurt growth. In light of RBI's recent actions, while the cost of capital will go up, access to capital also could be challenging as banks may no longer find it attractive to lend to gold finance companies. MGFL's inability to scale up in a timely manner its risk management systems in line with expanding business could potentially lead to asset quality issues.

## Link to Definitions

### Financials

Click [here](#) for definitions of commonly used terms.

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**India - Financials Coverage Cluster**

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	Corporation Bank	XCRRF	CRPBK IN	Veekesh Gandhi
	Federal Bank	XDFRF	FB IN	Veekesh Gandhi
	HDFC	HGDF	HDFC IN	Rajeev Varma
	HDFC Bank	XHDF	HDFCB IN	Rajeev Varma
	HDFC Bank	HDB	HDB US	Rajeev Varma
	ICICI Bank	ICIJF	ICICIB IN	Rajeev Varma
	ICICI Bank - A	IBN	IBN US	Rajeev Varma
	IndiaBulls Financial Services	IBLFF	IBULL IN	Veekesh Gandhi
	Indian Bank	INDIF	INBK IN	Rajeev Varma
	LIC Housing Finance, Ltd.	LHFLF	LICHF IN	Veekesh Gandhi
	Manappuram	XMGPF	MGFL IN	Veekesh Gandhi
	Max India	XMIF	MAX IN	Rajeev Varma
	Power finance corporation Ltd	PWFEE	POWF IN	Veekesh Gandhi
	Punjab	PUJBF	PNB IN	Rajeev Varma
	Reliance Capital	RLCCF	RCAPT IN	Veekesh Gandhi
	Rural Electrification Corporation Ltd	XULEF	RECL IB	Veekesh Gandhi
	SBI	SBINF	SBIN IN	Rajeev Varma
	SBI -G	SBKFF	SBID LI	Rajeev Varma
	Shriram Transport Finance	SHTFF	SHTF IN	Veekesh Gandhi
	Yes Bank Ltd	YESBF	YES IN	Veekesh Gandhi
<b>NEUTRAL</b>				
	Axis Bank	XAXSF	AXSB IN	Rajeev Varma
	Axis Bank - GDR	XBKSF	AXB LI	Rajeev Varma
	Bank of Baroda	BKBAF	BOB IN	Rajeev Varma
<b>UNDERPERFORM</b>				
	Bank of India	XDIIF	BOI IN	Rajeev Varma
	Canara Bank	CNRKF	CBK IN	Rajeev Varma
	IDBI	XDBIF	IDBI IN	Veekesh Gandhi
	Infrastruct Dev	IFDFF	IDFC IN	Rajeev Varma
	Kotak Mahindra Bank	XXRVF	KMB IN	Rajeev Varma
	ORBC	ORBCF	OBC IN	Rajeev Varma
	Union Bank India	UBOIF	UNBK IN	Rajeev Varma

**iQmethod<sup>SM</sup> Measures Definitions**

<b>Business Performance</b>	<b>Numerator</b>	<b>Denominator</b>
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
<b>Quality of Earnings</b>		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
<b>Valuation Toolkit</b>		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

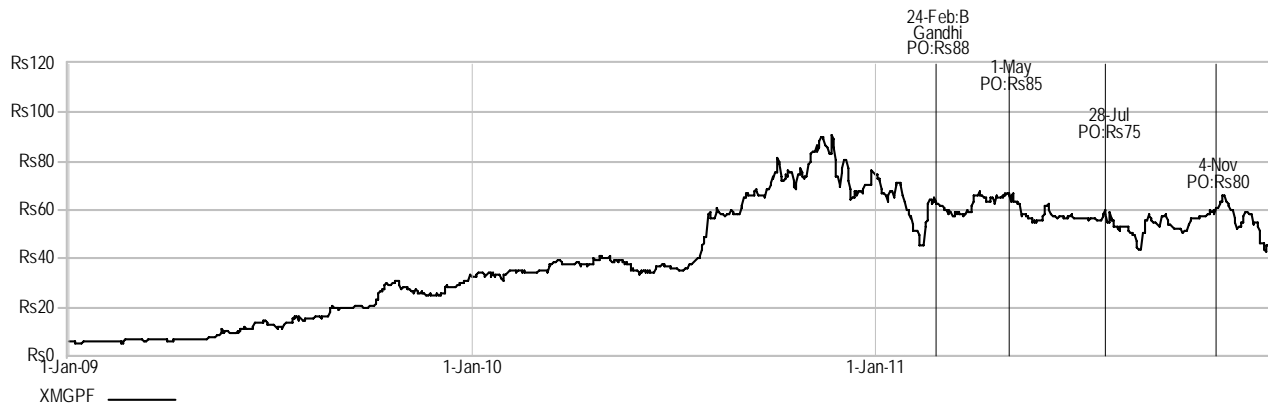
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### XMGPF Price Chart



B : Buy, N : Neutral, U : Underperform, PO : Price objective, NA : No longer valid, NR : No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of December 31, 2011 or such later date as indicated.

### Investment Rating Distribution: Financial Services Group (as of 01 Jan 2012)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	186	53.76%	Buy	117	65.73%
Neutral	103	29.77%	Neutral	65	64.36%
Sell	57	16.47%	Sell	34	59.65%

### Investment Rating Distribution: Global Group (as of 01 Jan 2012)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	2029	52.00%	Buy	1337	72.11%
Neutral	1009	25.86%	Neutral	657	71.34%
Sell	864	22.14%	Sell	487	60.20%

\* Companies in respect of which BofA Merrill Lynch or one of its affiliates has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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