KEYNOTE
INSTITUTIONAL RESEARCH

Initiating Coverage
April 26, 2010

# Manappuram General Finance & Leasing Ltd.


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# Manappuram General Finance & Leasing Ltd.

*Minting money, lending against gold*

**April 26, 2010**

| Stock Data | |
|---|---|
| Sector | NBFC |
| CMP | Rs786 |
| Fair Value (Residual Income model) | Rs897 |
| 52-wk High / Low | 840/120 |
| Market Cap | Rs26.8bn ($604mn) |
| 6m Avg. Daily Turnover | 54615 |
| BSE Sensex | 17694 |

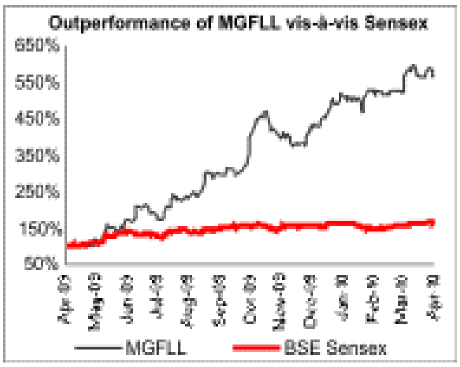
| Stock Codes | |
|---|---|
| Bloomberg Code: | MGFL IN |
| Reuters Code: | MGFL BO |
| BSE Code: | 531213 |
| Face Value: | Rs10 |

| Top Shareholders (Mar-31-10) | |
|---|---|
| Promoters | 41.0% |
| Sequoia Capital India | 11.6% |
| Hudson Equity | 11.1% |
| AA Development Capital | 6.4% |
| SmallCap World Fund | 4.5% |
| GHIOF Mauritius | 1.2% |
| Hellington Management | 1.1% |

**Price Performance (%)**

| 1 Mth | 3 Mths | 6 Mths | 1 Yr |
|---|---|---|---|
| 7.1% | 10.0% | 39.0% | 466.7% |

**Stock Price Performance**




## Executive Summary

- Manappuram General Finance & Leasing Ltd. (MGFLL), incorporated in 1992, is a Kerala-based NBFC focused on the niche segment of loans against gold (LAG), with a group track record of 6 decades.

- The lending against gold industry in India is dominated by money-lenders from the unorganized sector and therefore, extremely under-penetrated by the organized sector. As per IMaCS, organized lending against gold will grow at 40.1% CAGR from Rs270bn in FY09 to Rs530bn in FY11E.

- MGFLL's AUM grew 3.3x between March, 2007 and December, 2009, to reach Rs22.6bn. LAG AUM was Rs21.8bn as of December 31, 2009, up 3.9x over FY07. We believe merger with Manappuram Finance Tamilnadu Ltd. (MFTL) has helped grow the loan book and balance sheet size, enabling further fund raising. We expect AUM to grow at 48.2% CAGR during FY10E-12E, to reach Rs70.8bn, translating into average ROE of 29.7% over next 3 years.

- The stock trades at 13.3x FY11E and 7.9x FY12E earnings and 3.2x FY11E and 2.3x FY12E book with ROAE and ROAA of 34.2% and 5.9% respectively in FY12E. We believe MFGLL's high ROE deserves rich valuations vis-à-vis domestic NBFCs and global peers (Harvey & Thompson Pawnbrokers, Albemarle Bond Holdings and Cash America International). On the basis of residual income model considering MGFLL's book value of FY12E, we arrive at a fair value of Rs897 per share.

- Our concerns include need for frequent capitalization and frequent rollout of new branches (since existing branches tend to mature within 2-3 years) as well as decline in gold prices. In addition, there is a small risk of maintain custody of gold, the collateral.

### Financial Snapshot

| Particulars | FY09 | FY10E | FY11E | FY12E |
|---|---|---|---|---|
| NII (RsCr) | 167.11 | 368.78 | 607.56 | 908.68 |
| PAT (RsCr) | 47.49 | 119.84 | 200.70 | 339.55 |
| EPS (Rs) | 20.95 | 35.29 | 59.04 | 99.74 |
| BVPS (Rs) | 112.10 | 183.68 | 242.63 | 340.02 |
| P/e (x) | 37.5 | 22.3 | 13.3 | 7.9 |
| P/b (x) | 7.0 | 4.3 | 3.2 | 2.3 |
| Mkt Cap / AUM (x) | 1.1 | 0.8 | 0.5 | 0.4 |
| EV/AUM (x) | 1.8 | 1.4 | 1.2 | 1.0 |
| ROAE % | 24.7% | 27.3% | 27.7% | 34.2% |
| ROAA % | 3.0% | 5.5% | 5.4% | 5.9% |

Note: Financials are in respect of merged entity incl. assignments, merger effective January 11, 2010

(E - Keynote Capitals Institutional Research Estimates)

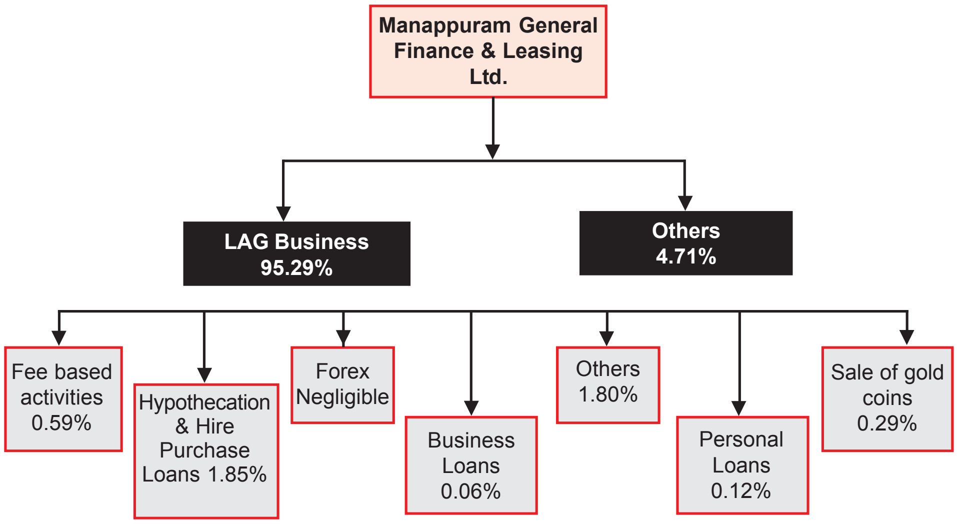
## Company Background

MGFLL was founded in 1949 and incorporated in 1992. The group has 6 decades of experience in the loans against gold (LAG) business and has shifted focus from a relatively risky, vehicle financing / hypothecated loans business to a more secure, LAG business.

On the demise of the founder in 1986, his son Mr. V.P. Nandakumar, CMD, took over. Mr. Nandakumar is also the Chairman of Equipment Leasing Association and Kerala Non-Banking Finance Companies Welfare Association (KNBFC).

Manappuram Finance Tamilnadu Ltd. (MFTL), a group company involved in a similar business, has been merged with MGFLL, as of January 11, 2010.

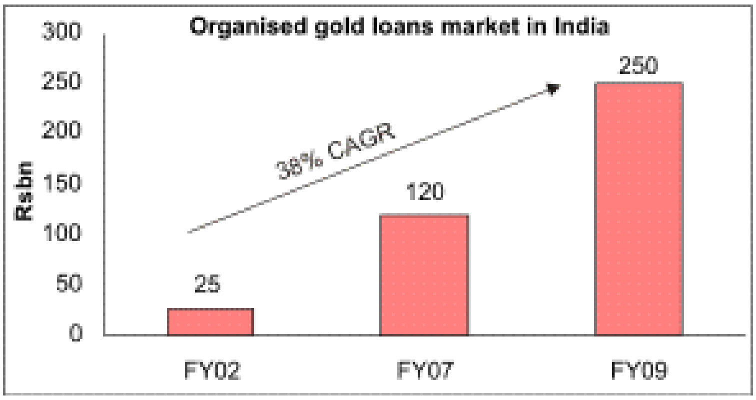
**Revenue contribution of various segments (9m-FY10)**




LAG AUM was Rs21.8bn as of December 31, 2009, up 3.9x over FY07.

## LAG Industry in India

Though overall market for LAG is large, organized LAG industry constitutes a very small fraction ~20% of the same. Organized LAG market in India is estimated at Rs220-270bn which grew @ 38% CAGR during FY02-FY09.




(Source: IMaCS)

As per a World Gold Council research study, global stock of gold was estimated at 145,000 tonnes in 2009, while gold stock owned by private households in India is 15,000 tonnes, i.e., ~10% of the privately held global gold stock. Organized LAG translate into just 1.1% of the value of total gold stock in India. This highlights the huge untapped potential for loans against gold in India. Banks and NBFCs consider this as an opportunity to grow their secured lending book and earn high yields. Organized gold loans portfolio is expected to grow @ 40% to reach Rs500-530bn by FY11.

**Gold holdings in India**

It is estimated that 40% of the gold holding is in South India, 25% in the West, 20% in the North and 15% in the East. Key reasons for large gold holdings in South India can be attributed to a large part of the population from that region which is working in the Middle East. According to the company, of the total LAG in India, over 50% is from the southern region.

### A) Domestic Competition

**Sources of LAG**

**1) Money Lenders**

According to IMaCS report, un-organized LAG market in India is believed to be several times the size of the organized market. Money lenders are active in rural areas, with the USP of quickly disbursing loans against jewellery.

Being unregulated, money lenders however charge extremely high rates of interest of as much as 30% p.a., which prove to be detrimental to the borrower's interests. ~60% of rural households in India are farmers, 49% of whom are in debt. As per regulatory norms, LAG for agriculture purposes have been made eligible as priority sector lending in the banking industry and are considered more secure by lenders. Gold loans of up to Rs50,000 are considered as part of micro credit. Banks and NBFCs consider this as an opportunity to grow their secured lending book and earn high yields. As a result, a significant part of LAG may shift from the un-organized sector to the organized sector.

**2) NBFCs**

There are 2 focused lenders against gold in India, in the organized sector, viz. MGFLL and Muthoot Finance, both of which have a large presence in South India. Muthoot Finance has a wider reach in terms of no. of branches (at 1300) vis-à-vis MGFLL which has a network of 850 branches.

However MGFLL scores over closest NBFC peer Muthoot Finance with the USP that the former charges interest only till the date of re-payment and not for a minimum no. of days. In contrast, Muthoot Finance charges interest for a minimum of 7 days, interest irrespective of the re-payment date (as per MGFLL sources).

In view of the under-penetrated market, high margins and low default risk, other NBFCs too are eyeing this segment. However, MGFLL being a focused player in the LAG segment, with established an brand and wide branch network, is far better poised to exploit the untapped opportunity, than the new competitors or even Muthoot Finance.

**3) Banks**

LAG is a segment where banks too are attempting to establish their presence. LAG can be availed for agricultural, personal consumption / domestic purposes. The rates of interest vary according to the loan amount and its usage. As LAG for agriculture purpose have been made eligible as priority sector lending in the banking industry, banks target this segment to grow their loan book with superior quality as an add-on. LAG are provided by private sector banks viz. HDFC Bank, Axis Bank, ICICI Bank, Federal Bank, South Indian Bank and public sector banks viz. State Bank of India, Bank of India, Andhra Bank, Central Bank of India, Allahabad Bank, etc.

Personal Loans are an alternative to LAG, however they are typically more expensive. LAG are offered by banks in the range of 12% to 17% on floating basis, compared with personal loans offered at 13% to 19% on fixed/ floating basis.

| | Personal Loan | | Loans against gold | |
|---|---|---|---|---|
| | Interest type | Interest rate % | Interest type | Interest rate % |
| HDFC Bank | Floating | 14.5-16.5 | Floating | 12.5 |
| Andhra Bank | Floating | 15 | Floating | 12.75 |
| Canara Bank | Fixed | 14.5 | Floating | 12.75 |
| Federal Bank | Fixed | 16.25 | Floating | 12.5 |
| Indian Overseas Bank | Fixed | 12.75 | Floating | 12 |
| State Bank of Hyderabad | Floating | 13.75-14.75 | Floating | 12.25 |
| State Bank of Indore | Floating | 15 | Floating | 11.75 |
| State Bank of Travancore | Floating | 16.75 | Floating | 12 |
| Karur Vysya Bank | Fixed | 12.75 | Floating | 13.5 |
| South Indian Bank | Floating | 15.25 | Floating | 13.75 |

(Source: Websites)

Implementation of base rate from April 1, 2009 has benefited banks offering LAG, as they can now charge rates at PLR.

**Comparison of NBFCs and Banks in respect of lending against gold**

| Criterion | NBFCs | Banks |
|---|---|---|
| Time taken for processing loan application | ~15 minutes | ~1 hour |
| Rate of interest | High (~24%) | Low (~14%) |
| Nature of Interest | Fixed | Floating |
| Average LTV | Rs1200-1500 per gram or 75% of value of gold collateral | Rs600-1100 per gram or 65% of value of gold collateral |
| KYC norms | Minimum | Essential |
| Processing fees | Nil | Chargeable |
| Average Ticket size | Small (~Rs20,000) | Larger |
| Specialized attention to gold loans | Yes | No |
| Documentation | Minimum | Relatively higher |
| Accessibility to middle and lower class | Easy | Difficult |
| Other formalities | None | Banks insist of having a deposit account with the bank. |
| Valuation capability | Trained valuers at every branch | Valuers visit branch regularly or as required basis. |
| Working hours | 9am - 6pm | 9.30am - 3.30pm |

(Source: Company data, Keynote Capitals Institutional Research)

## B) Global Peers

MGFLL has no listed domestic peer, which is focused solely on the LAG segment. Three companies in UK/US have similar business model (detailed discussion on page 22).

**Harvey & Thompson Pawnbrokers Plc (UK)**

Harvey & Thompson (H&T) a UK-listed pawn broking entity. 89% of CY08 revenues was derived from pawn broking business. 98% of the pawn broking is from gold. Pawn broking will remain a core business for H&T.

**Albemarle Bond Holdings Plc (UK)**

Albemarle Bond Holdings, founded 1983, currently has 115 branches in the UK, providing pawn broking, jewellery retailing and associated financial services. Interest rates are charged at 7.5% on monthly basis. The average ticket size of gold loans is £140. Though the tenure of such loans is 6 months, loans are usually repaid within 2-3 months.

**Cash America International Inc. (US)**

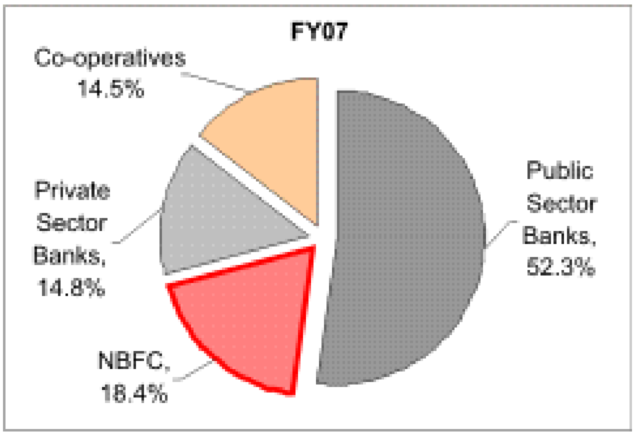
Founded in 1983, Cash America International Inc. is a provider of secured loans, referred to as pawn loans and operates via 613 locations. These stores operate under the brand names, Cash America Pawn and Super Pawn.

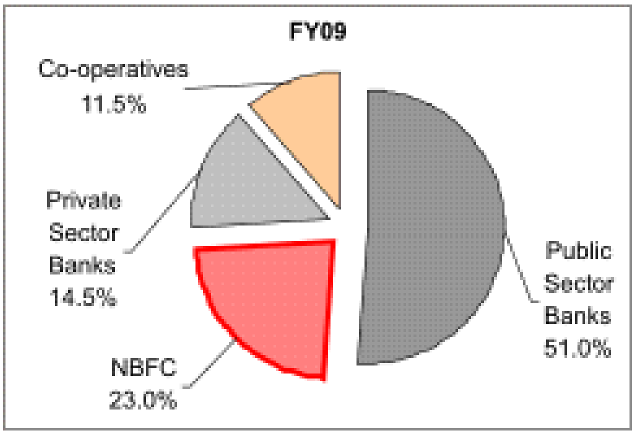
## Investment Rationale

**1) Organised sector loans against gold, an under-penetrated segment with huge potential in India**

Though the overall market for loans against gold (LAG) in India is large, the organized segment constitutes just a fraction, ~20% of the market. According to ICRA Management Consulting Services (IMaCS), the organized market for LAG in India grew at 38% CAGR during FY02-09 and is currently estimated at Rs220-270bn. It is expected to grow at 40% CAGR to reach Rs500-530bn by FY11. Currently, ~85% of the LAG market is in South India.

**Market shares of organized LAG players**




(Source: Company website)

**LAG Providers**

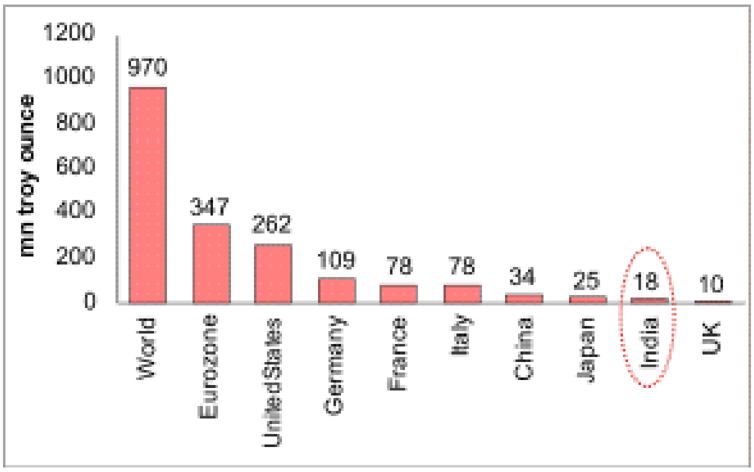
| | LAG Portfolio (Rsbn) | % market share |
|---|---|---|
| Muthoot Finance | 33.0 | 13.4% |
| Indian Bank | 32.5 | 13.2% |
| Indian Overseas Bank | 31.0 | 12.6% |
| State Bank of Travancore | 16.0 | 6.4% |
| South Indian Bank | 15.0 | 6.1% |
| Manappuram General Finance | 12.0 | 4.9% |
| Muthoot Fin Corp | 11.8 | 4.8% |
| Federal Bank | 10.7 | 4.3% |
| Andhra Bank | 9.0 | 3.6% |

Data for FY09
(Source: IMaCS report)

**LAG considered priority sector lending**

~60% of rural households in India are farmers, of which, 49% are in debt. As per banking industry regulatory norms, loans against gold for agriculture purposes are eligible as priority sector lending since 2004 and are considered more secure by lenders. LAG of up to Rs50,000 is considered part of micro credit. Banks and NBFCs consider this as an opportunity to grow their secured lending book and earn high yields.

**Gold reserves held by central banks around the world**




(Source: Bloomberg)

As on Dec-31-09, MGFLL held 0.1% of privately held gold stock in India. It envisages imparting liquidity to 10% of privately held gold over the next 8-9 years.

**Untapped potential of the LAG segment**

| | (tonnes) |
|---|---|
| Estimated gold stock privately held by households in the World | 145,000 |
| Estimated gold stock privately held by households in India | 15,000 |
| Gold AUMs of Manappuram (Dec-31-09) | 20 |

(Source: World Gold Council Research 2009)

**Organized LAG just 1.1% of value of gold stock in India**

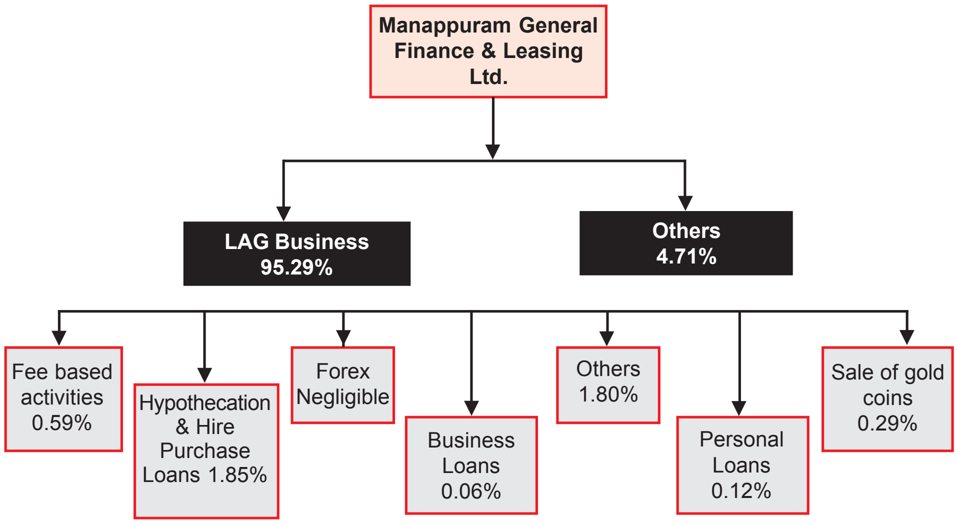
| | By weight | By value Rsbn |
|---|---|---|
| | 10 gm | 0.000017 |
| | 1 Kg | 0.0017 |
| | 1 tonne | 1.7 |
| Total gold stock in India | 15,000 tonnes | 24,998 |
| Organized sector LAG in India | | 270 |
| Organized LAG as % of gold stock value in India | | 1.1% |

(Assuming gold price of Rs16665 per 10 gms)

2) **MGFLL: Focused Lender against Gold Jewellery**

Incorporated in 1992, MGFLL is a Kerala-based NBFC with business model of lending against used gold jewellery to households.

**Segment wise revenue contribution (9m-FY10)**




LAG loan book was Rs21.8bn as of December 31, 2009, up 358% y-o-y over FY07. LAG constituted 96% of total Assets under Management (AUM), with the balance comprising vehicle loans, hire purchase, etc.

**Focused target audience**

MGFLL is focused on professions and persons with irregular income streams and short-term fund requirements, such as farmers, agriculturists, small vendors and middle and lower class families. These customers pawn gold to obtain extremely short term, stop-gap finance, to meet various requirements such as festival expenses, harvest, agricultural inputs or fund day-to-day business operations.

It services 0.5mn customers via a network of 1020 branches spread across 15 states in India. It offers LAG with an average 75% Loan to Value (LTV) at interest rate of 2% on monthly basis of an average ticket size of ~Rs20,000.

It is a secured lending business (low default risk) with gold pledged as collateral, delivering superior Net Interest Margin (NIM) of 14%+, with ROAE of 25%.

3) **USPs of MGFLL include:**

- **Focused player**

  MGFLL enjoys a tremendous advantage of being a specialized lender against gold, vis-à-vis banks, for which, LAG is just one of the various categories of advances. Banks cannot be as competitive as MGFLL in terms of focused manpower, since the same set of bank employees that offers other loans such as auto loans and home loans, also offers gold loans.

- **Quick processing of loans**

  MGFLL processes gold loans within 15 minutes with minimum formalities, compared to banks that take almost a day of processing time, with proper introduction by an existing customer.

- **Interest charged only till re-payment**

  Usually, the tenure of LAG is short due to sentimental value attached to gold jewellery and the nature of requirements, viz. harvest, festival time, etc. MGFLL charges interest only till the date of repayment vis-à-vis banks which charge minimum 15 days' interest irrespective of date of repayment.

  Thus, MGFLL is able to generate better yields, in spite of charging interest only till date of repayment. On their part, customers too are happy since the absolute amount of interest (even @ 24% p.a.) is not significant, for loans which are repaid within a few days say within a couple of weeks. This is the key reason why customers prefer MGFLL over banks, though the former charges higher rates of interest of ~24% (with nil processing fees) vis-à-vis banks which charge rate of ~14% (plus processing fees).

  Also, with the recent announcement of the 'base rate system' to be effective July 1, 2010 in banks, we believe banks may increase rates of interest applicable to LAG, reducing the gap between rates charged by MGFLL and banks.

- **Higher LTV vis-à-vis banks**

  MGFLL also scores over banks on the parameter of Loan to value (LTV). It offers higher LTV of ~75% @ 24% yield, compared to banks' ~65% LTV @ 14% yield. To be more competitive, MGFLL launched schemes, such as offering 65% LTV @ 11% yield (capped at ticket size of Rs10,000 per customer); which is more attractive than the banks' offerings and also involves quicker disbursement.

4) **Merger offers dual benefits: Expansion of loan book and growing balance sheet size, improving fund raising capacity**

- **Expansion of loan book**

  MGFLL merged Manappuram Finance Tamilnadu Ltd. (MFTL) with itself, effective January 11, 2010. MFTL is in the same line of business of providing gold loans. However MGFLL, unlike MFTL, is a deposit taking entity (detailed financials of standalone MGFLL and MFTL on page 26).

  The merger of MFTL with MGFLL increases the total loan book as well as balance sheet size by 27.7% and 37.7% respectively and helps improve fund raising capacity.

**Comparison of Key Numbers - MGFLL and MFTL (FY09)** **(RsCr)**

| | Loan Book | Balance sheet size |
|---|---|---|
| Standalone MGFLL | 986.74 | 1157.1 |
| Standalone MFTL | 272.85 | 435.83 |
| Merged entity | 1259.59 | 1592.93 |
| **Growth** | **27.7%** | **37.7%** |

(All figures include assignment transactions)

- **Merger mutes impact of equity dilution (QIP) on promoter holding**

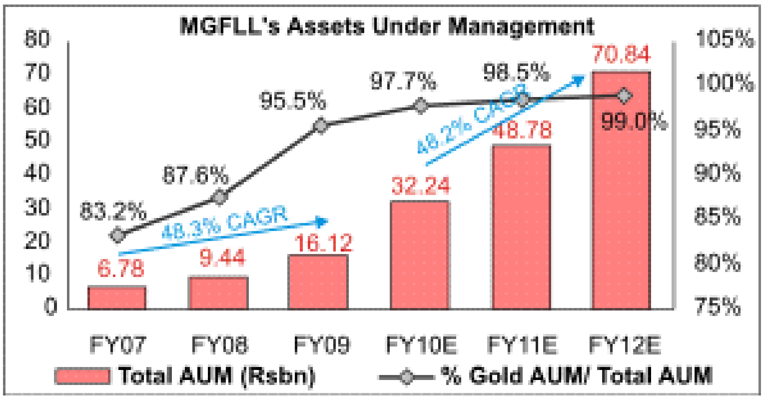
  MGFLL recently made a QIP of Rs245Cr @ Rs 691 per share. The changes in promoter shareholding are as follows:

| | Pre-merger | | Post-merger | | Post-QIP | |
|---|---|---|---|---|---|---|
| | No. of Shares | % stake | No. of Shares | % stake | No. of Shares | % stake |
| Promoters | 5,240,047 | 30.4% | 12,371,340 | 42.8% | 13,948,790 | 41.0% |
| **Total** | **17,255,828** | **100.0%** | **28,933,210** | **100%** | **34,038,522** | **100.0%** |

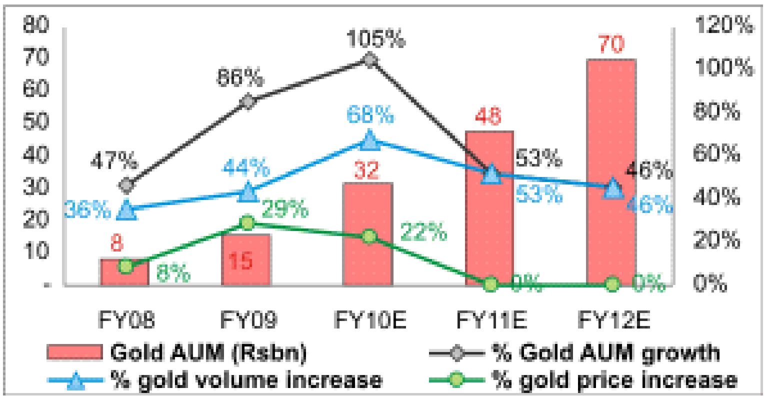
**5) Growth in AUM driven by volumes, gold prices and branch rollout**

MGFLL's AUM (including assignments) grew at 48.3% CAGR from FY07 to FY09 to Rs12.6bn and is expected to grow at 48.2% CAGR during FY10-12E aggregating to Rs70.8bn by FY12E.

**AUM growth trajectory**

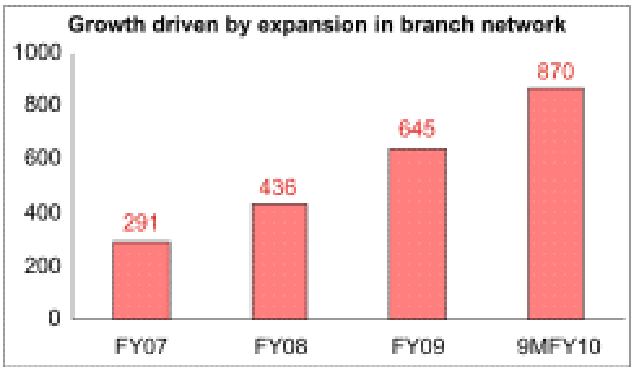


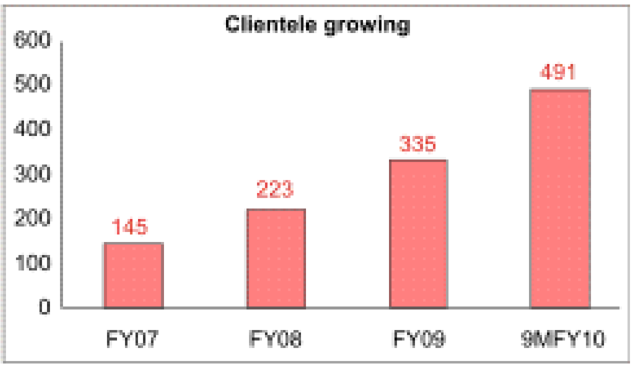

**Growth in AUMs driven by gold pledged and gold prices**



**Branch roll out**

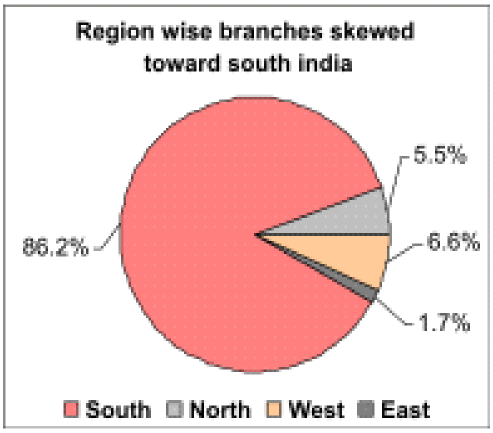
Loan growth driven by branch network expansion and increase in average loan per branch.The branch strength almost doubled from FY07 to FY09, in line with clientele growth.

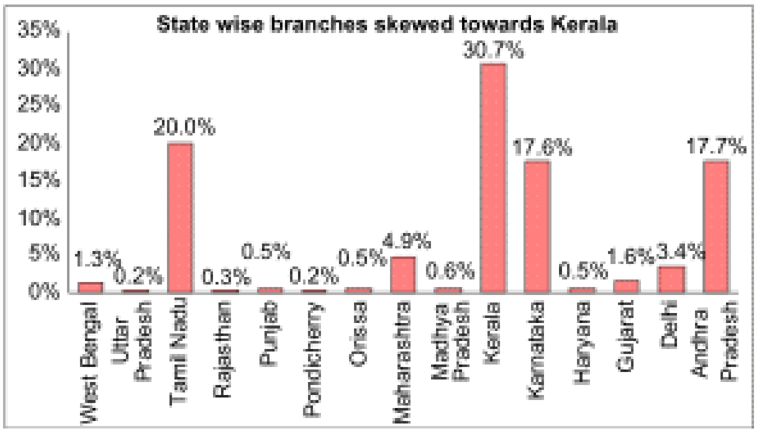



As of December 31, 2009, it operated 870 branches (all housed in leased premises) spread across India, with large concentration in Kerala in South India.

**Wide geographic reach: distribution of branch network**




**The way forward**

In order to further grow its operations, MGFLL needs to grab market share from the unorganized sector moneylenders, in other words, attract the latter's customers. Since gold cannot be transported over long distances for safety reasons, it becomes essential for MGFLL to set up new branches in close proximity of clients.

Currently, South India accounts for ~85% of the LAG market in India. However, MGFLL is of the view that there exists an as yet untapped market in South India, as there are almost 8500 active moneylenders in the state of Karnataka alone. MGFLL intends to have a pan-India presence going forward. Towards this objective, it has launched various ad campaigns in West, East and North India to increase the level of awareness of its services.

Going forward, it plans to add ~ 200 branches p.a., over the next 3 years.

**Efficiency Ratios** **(RsCr)**

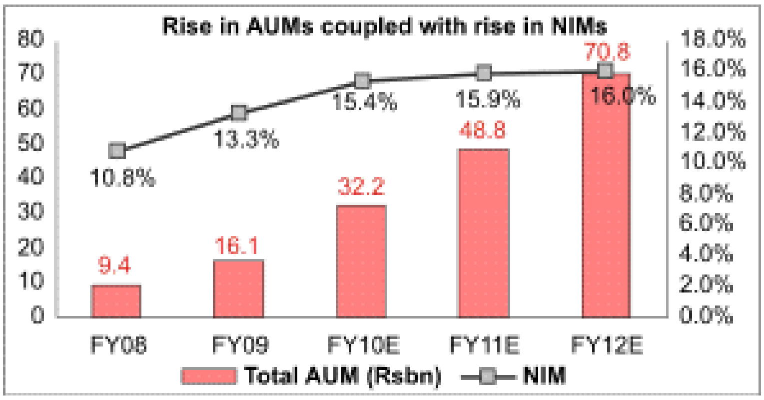
| Particulars | FY08 | FY09 | FY10E | FY11E | FY12E |
|---|---|---|---|---|---|
| **No of branches** | **436** | **645** | **1005** | **1205** | **1405** |
| Revenues | 168 | 302 | 605 | 1013 | 1555 |
| Average Revenues | 122 | 235 | 453 | 809 | 1284 |
| Average Revenue per branch | 0.28 | 0.36 | 0.45 | 0.67 | 0.91 |
| Avg costs per branch | 0.23 | 0.31 | 0.37 | 0.54 | 0.72 |
| Profits available to shareholders | 28 | 48 | 120 | 201 | 340 |
| Average Profits | 21 | 38 | 84 | 160 | 270 |
| Average Profits per branch | 0.05 | 0.06 | 0.08 | 0.13 | 0.19 |
| Total Loan Outstanding | 793 | 1260 | 2394 | 3810 | 5671 |
| Average Loan Outstanding | 683 | 1026 | 1827 | 3102 | 4740 |
| Average Loans O/s Per branch | 1.6 | 1.6 | 1.8 | 2.6 | 3.4 |
| Total AUM | 944 | 1612 | 3224 | 4878 | 7084 |
| Average AUM | 811 | 1278 | 2418 | 4051 | 5981 |
| Average AUMs per branch | 1.9 | 2.0 | 2.4 | 3.4 | 4.3 |

(E - Keynote Capitals Institutional Research Estimates)

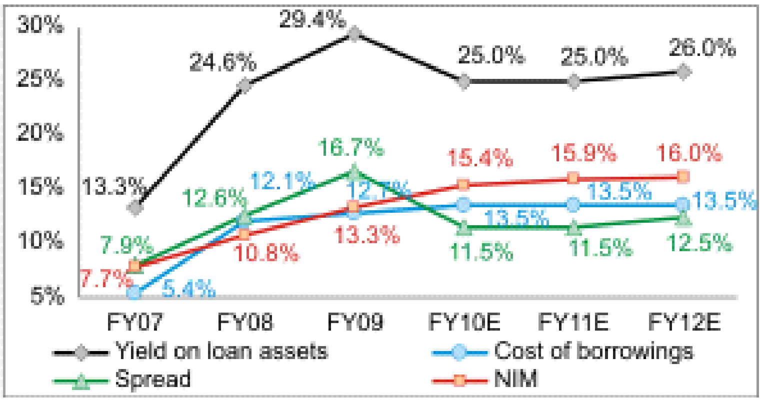
The average loan outstanding per branch is expected to increase from Rs1.6Cr in FY09 to Rs3.3Cr in FY12E. This is on account of the ramp up in lending by old branches. However, the maximum outstanding loan per branch is capped at ~Rs10Cr. Once this limit is crossed, a new branch is set up in the vicinity.

### 6) Superior margins and secured form of lending delivering high return ratios

**AUMs increase with superior net interest margins...**

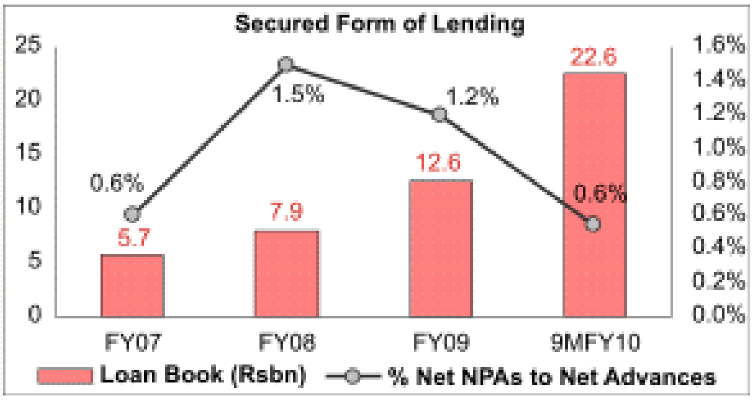



Backed by higher yields on loan assets

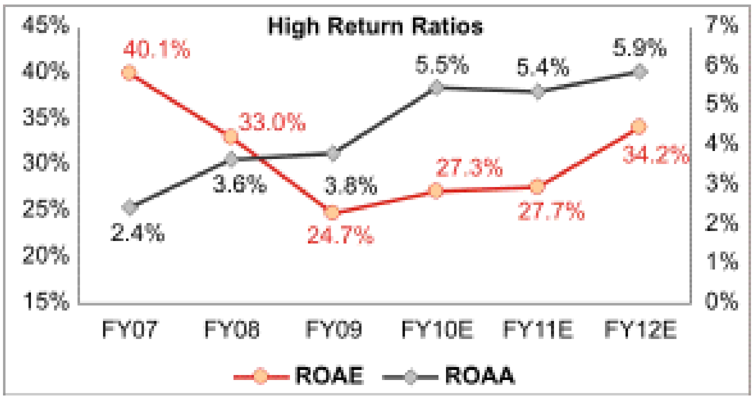


**...Without compromising on quality of assets**

AUM grew from Rs5.7bn in FY07 to Rs22.6bn in 9MFY10, but comprising on the asset quality, as Net NPAs are on a declining trajectory. As on December 31, 2009, Net NPAs was 0.6% of Net Advances. Of these, Net NPA pertaining to LAG would be ~0.3%, with the balance attributable to the legacy vehicle finance loans business, which is not the focus area for the company. Considering this, going forward, NNPAs are set to decline further.




As of December 31, 2009, it reported Return on Assets (ROA) of 4% and Return on Equity (ROE) of 41.61%. In spite of the equity dilution of 4.7% on account the QIP of Rs245Cr, MGFLL is expected to generate an average ROAE of 29.7% and ROAA of 5.6% during FY10E-12E.




7) **Balance sheet quality likely to be maintained**

We believe MGFLL's balance sheet will continue to be of good quality for the following reasons:

- Low cost of borrowings, coupled with high yields, will protect margins: As explained earlier in the report, MGFLL's margins are unlikely to be drastically impacted going forward, by virtue of it being a focused lender against used gold jewellery.

- Low NPAs: Since the collateral for loans, in the form of used gold jewellery has sentimental value, we believe chances of default are low. In any case, since LTV does not usually exceed 75% (usually 15% are the making charges and rest 10% is the cushion against decline in gold prices), the gold price risk is also covered.

## Valuations

MGFLL is likely to grow AUM at CAGR of 48.2% during FY10E-12E, translating into superior return ratios, viz. ROAE and ROAA of 34.2% and 5.9% respectively during FY10E-12E. The stock trades at 7.9xFY12E earnings and 2.3xFY12E book.

MGFLL has no listed domestic peer, which is focused solely on the LAG segment, so we compare it with global peers 'Harvey & Thompson Pawnbrokers Plc', 'Albemarle Bond Holdings Plc' and Cash America International, Inc. as they are gold pawnbrokers. We also compared its valuations with other NBFCs. There are talks of NBFCs viz. M&M Financial, Reliance consumer finance, etc entering the loans against gold segment.

**MGFLL deserves better valuations vis-à-vis domestic NBFCs and global peers, due to higher ROE**

| | Year | Sales | PAT | EPS | BVPS | ROE | P/e (x) | P/b (x) |
|---|---|---|---|---|---|---|---|---|
| **MGFLL** | **Mar-10** | 368.78 | 119.84 | 35.29 | 183.68 | **27.3%** | 22.3 | **4.3** |
| | **Mar-11** | 607.56 | 200.70 | 59.04 | 242.63 | **27.7%** | 13.3 | **3.2** |
| | **Mar-12** | 908.68 | 339.55 | 99.74 | 340.02 | **34.2%** | 7.9 | **2.3** |
| **Albemarle & Bond Holdings** | **Jun-10** | 73.90 | 13.80 | 0.24 | 1.10 | **20.7%** | 9.7 | **2.1** |
| | **Jun-11** | 75.52 | 13.70 | 0.25 | 1.24 | **15.5%** | 9.3 | **1.9** |
| | **Jun-12** | 78.50 | 14.35 | 0.27 | 1.39 | **14.6%** | 8.9 | **1.7** |
| **Harvey & Thompson** | **Dec-10** | 72.09 | 11.87 | 0.29 | 1.54 | **16.9%** | 8.2 | **1.5** |
| | **Dec-11** | 78.72 | 10.85 | 0.30 | 1.74 | **14.4%** | 7.9 | **1.4** |
| | **Dec-12** | 85.00 | 10.60 | 0.30 | 1.95 | **N.A.** | 7.9 | **1.2** |
| **Cash America International** | **Dec-10** | 1,244.00 | 113.43 | 3.62 | 25.53 | **14.8%** | 11.6 | **1.6** |
| | **Dec-11** | 1,364.00 | 130.29 | 4.12 | 18.99 | **14.9%** | 10.2 | **2.2** |
| | **Dec-12** | 905.00 | 141.00 | 4.72 | 35.51 | **14.3%** | 8.9 | **1.2** |
| **Shriram Transport Finance** | **Mar-10** | 1,996.50 | 759.10 | 34.33 | 141.10 | **28.2%** | 15.3 | **3.7** |
| | **Mar-11** | 2,470.90 | 892.20 | 40.40 | 176.20 | **25.5%** | 13 | **3** |
| | **Mar-12** | 2,775.30 | 1,063.00 | 50.30 | 218.60 | **25.6%** | 10.5 | **2.4** |
| **M&M Financial** | **Mar-10** | 1,004.25 | 300.53 | 32.20 | 176.18 | **18.9%** | 13.2 | **2.4** |
| | **Mar-11** | 1,163.40 | 353.33 | 37.68 | 207.05 | **19.1%** | 11.3 | **2.1** |
| | **Mar-12** | 1,350.75 | 424.10 | 44.10 | 226.50 | **19.9%** | 9.7 | **1.9** |

(Financials for MGFLL, Shriram and M&M Financial are in RsCr while H&T Pawnbrokers and Albemarle & Bond Holdings is in GBP [mn] and Cash America International is in USD [mn])

**Constant growth Residual Income Model (RIM) Valuation**

Intrinsic Value under RIM represented by

$$V_0 = B_0 + \frac{ROE - r}{r - g} B_0$$

**Components of RIM**

- Book Value of FY12E : Rs340 per share (from financial model)
- Stable ROE : 29.4%
- Cost of equity: 15.6%
  - Risk Free Rate: 7.5%
  - Market Risk Premium: 9.5%
  - Beta: 0.85

On the basis of residual income model considering MGFLL's book value of FY12E, we arrive at a fair value of **Rs897** per share.

## Sensitivity Analysis

We evaluate the change in FY12E key numbers and valuations w.r.t. change in gold volume (tonnes) and price of gold (Rs per 10 gm)

**For Gold price : Rs14255 per 10 gms**

| FY12E | Gold Volume (tonnes) | | |
|---|---|---|---|
| | **35** | **45** | **55** |
| AUM (Rsbn) | 50.62 | 64.88 | 79.13 |
| Profits (Rsbn) | 2.36 | 3.09 | 3.82 |
| EPS (Rs) | 69.18 | 90.73 | 112.28 |
| Book value (Rs) | 309.46 | 331.01 | 352.56 |
| **P/e (x)** | **11.4** | **8.7** | **7.0** |
| **P/b (x)** | **2.5** | **2.4** | **2.2** |
| **Intrinsic Value (Residual Income Model)** | **749** | **853** | **959** |

**For Gold Price: Rs 15755 per 10 gms**

| FY12E | Gold Volume (tonnes) | | |
|---|---|---|---|
| | **35** | **45** | **55** |
| AUM (Rsbn) | 55.87 | 70.84 | 87.38 |
| Profits (Rsbn) | 2.63 | 3.40 | 4.25 |
| EPS (Rs) | 77.11 | 99.74 | 124.75 |
| Book value (Rs) | 317.39 | 340.02 | 365.03 |
| **P/e (x)** | **10.2** | **7.9** | **6.3** |
| **P/b (x)** | **2.5** | **2.3** | **2.2** |
| **Intrinsic Value (Residual Income Model)** | **787** | **897** | **1022** |

**For Gold Price: Rs 17255 per 10 gms**

| FY12E | Gold Volume (tonnes) | | |
|---|---|---|---|
| | **35** | **45** | **55** |
| AUM (Rsbn) | 61.12 | 78.38 | 95.63 |
| Profits (Rsbn) | 2.9 | 3.79 | 4.67 |
| EPS (Rs) | 85.05 | 111.14 | 137.22 |
| Book value (Rs) | 325.33 | 351.42 | 377.5 |
| **P/e (x)** | **9.2** | **7.1** | **5.7** |
| **P/b (x)** | **2.4** | **2.2** | **2.1** |
| **Intrinsic Value (Residual Income Model)** | **825** | **954** | **1086** |

## Investment Risks

**1) Need for frequent rollout of new branches, and consequently, frequent capitalization**

Typically, most of MGFLL's branches tend to mature within 2-3 years of being set up, in terms of number of accounts they can service efficiently. Therefore, the company has to necessarily keep opening new branches, at times in the same locality or nearby. This frequent rollout leads to need for frequent capitalization.

**Highly capital intensive business, requires continuous source of funding and high borrowings to fund loan book**

MGFLL is highly capital intensive business. Its loan book has been augmented with funding from private equity investors, merger, QIP, borrowings and internal accruals.

**Private equity investments**

| Name of Investor | Name of Fund | Date of Conversion of CCPS into equity shares | Avg. Cost per share (Rs) | % stake as on Mar. 31, 2010 |
|---|---|---|---|---|
| Sequoia Capital | Sequoia Capital India Growth Investments I | FY09 | 154.56 | 11.6%* |
| India Equity Partners | Hudson Equity Holdings | FY09 | 154.56 | 11.1% |
| Ashmore-Alchemy | AA Development Capital India Growth Investments | FY09 | 166.62 | 6.4% |
| Granite Hill | GHIOF Mauritius | FY09 | 166.62 | 1.2% |

(* Sequoia Capital exited MGFLL in April, 2010)

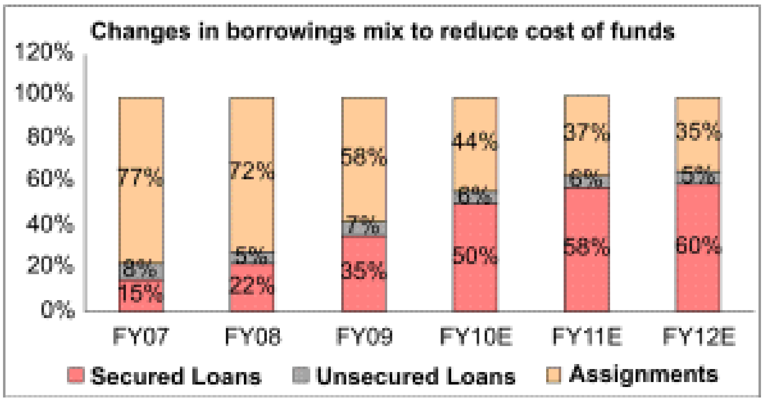
Merger of MFTL with MGFLL. 11.68mn shares allotted to MFTL on its merger with MGFLL, as of January 11, 2010. Net worth grew by 55% post merger. Post merger of MFTL with MGFLL, promoter stake will increase from 30.4% to 42.8% as per our estimates. In spite of equity dilution via the recent QIP, promoter stake has reduced to only 41%, which is higher than before the merger.

However, we note that this may not be a one-time phenomenon; in order to grow its business MGFLL will always need resources. In the past, private equity investors have infused funds into the company. Further growth is being funded by merger and the recent QIP. Although it sits on internal accruals from the business, external funding is essential for growth.

QIP of Rs245Cr at Rs691 per share. With this CAR moved up from 20% to ~30%. QIP investors include Small Cap World Fund, Credit Suisse Singapore, Merill Lynch, Capital Market, India Capital Fund, Morgan Stanley Mutual Fund, SBI Mutual Fund, Deutsche Mutual Fund, Nomura, etc

**Borrowings and Internal Accruals**

| | FY09 | FY10E | FY11E | FY12E |
|---|---|---|---|---|
| Net Worth | 2.6 | 6.3 | 8.3 | 11.6 |
| Borrowings | 13.4 | 21.5 | 38.5 | 57.3 |
| Leverage | 5.2 | 3.4 | 4.7 | 4.9 |
| Total Assets | 15.9 | 27.8 | 46.7 | 68.8 |
| Net Worth % of Total Assets | 16.1% | 22.5% | 17.7% | 16.8% |
| Borrowings % of Total Assets | 83.9% | 77.5% | 82.3% | 83.2% |
| Loan book funding | 12.6 | 23.9 | 38.1 | 56.7 |




**Decent credit ratings help access low cost funds**

In September 2009, ICRA upgraded MGFLL's short term credit rating from A1 to A1+. MGFLL has had a continuous rating since the past 15 years and currently enjoys the highest short term credit rating.

ICRA has also upgraded its rating to MA+ for its Fixed Deposit Programme and to LA+ for working capital limits.

The share of commercial paper (CP) within the overall borrowing mix rose, as it was able to source funds via CP at an average cost of 10-11%.

**Securitization process mutually beneficial for both MGFLL and banks**

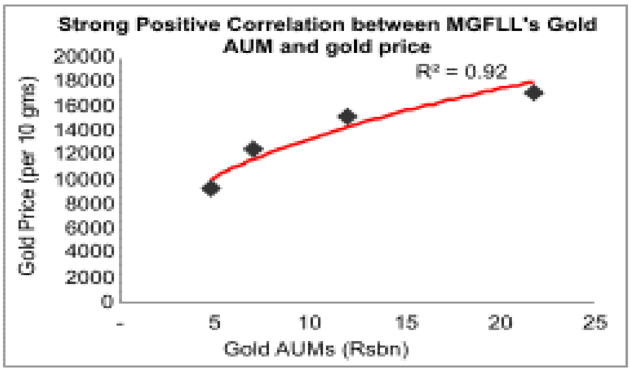
Regulatory provisions allow MGFLL to securitize its loan book with banks (LAG falls under priority sector lending for these banks). The securitisation process is mutually beneficial for both MGFLL and banks. MGFLL gets funding to scale up its business. Also since 40% of the total lending by banks is required to be priority sector lending, banks are able to classify LAG in their books as priority sector lending, enabling them to meet the regulatory norm.

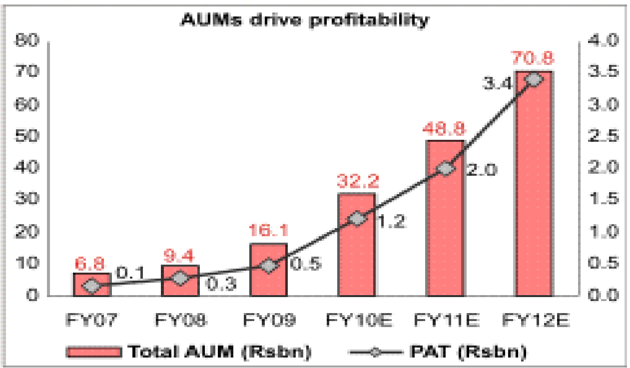
**2) Decline in gold prices**

Since the collateral is used gold jewellery, a crash in gold prices can hit the company. MGFLL lends against gold jewellery over short tenure considering the average gold price of last 90 days. If gold prices fall below the LTV, its top line and profitability can get impacted. However, given that the LTV is ~75%, the company is insulated from small declines in gold prices.

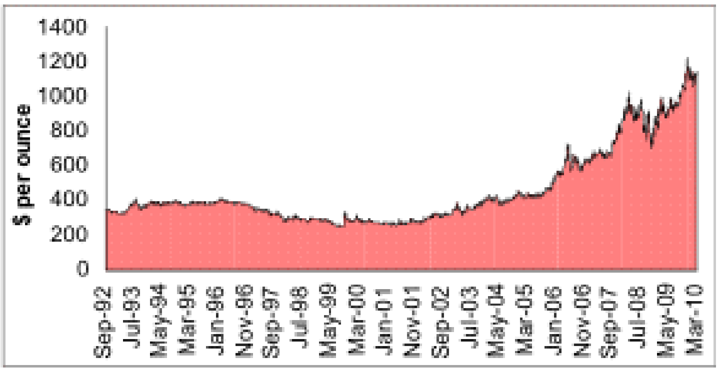
**Correlation between gold prices and gold AUM**

We attempted to ascertain how much of the change in MGFLL's gold AUM from March 2007 to December 2009 is attributable to changes in gold prices. We have established a strong positive correlation of 0.92 between MGFLL's gold AUM and gold prices in India.



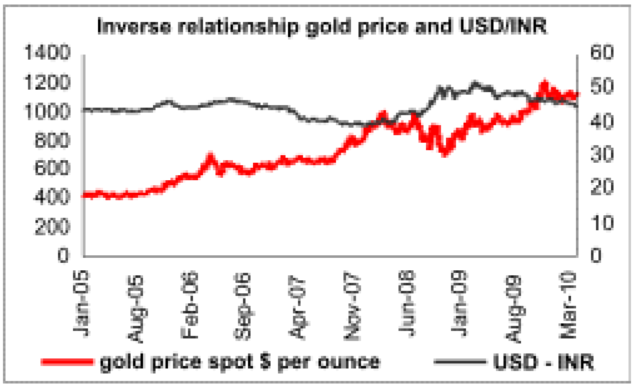



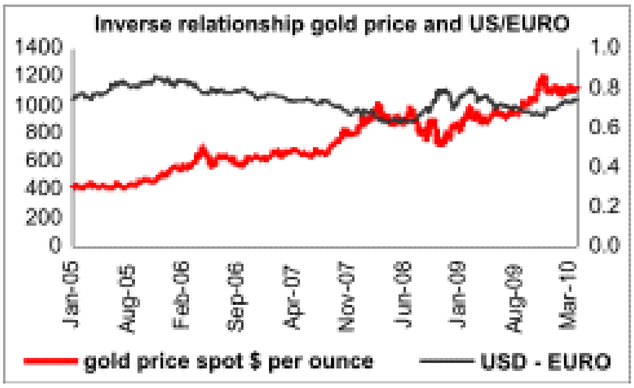

**Gold Price Chart**

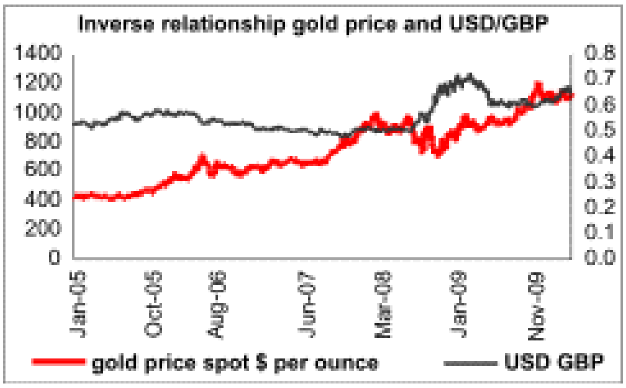



Gold prices gained in the recent past on dollar weakness, since the latter increases the demand for metal as an alternative investment. There has been demand with central banks to steadily increase their exposure to gold as a hedge against the weakening dollar.

**Inverse relationship between gold price and dollar movements**



**Gold price forecasts**

| | Current Price | FY11E | FY12E | FY13E |
|---|---|---|---|---|
| Gold price ($ per ounce) | 1135 | 1192 | 1215 | 1206 |
| % change y-o-y | | 5.0% | 1.9% | -0.7% |

(E: weighted averages from Bloomberg)

**3) Large geographic concentration**

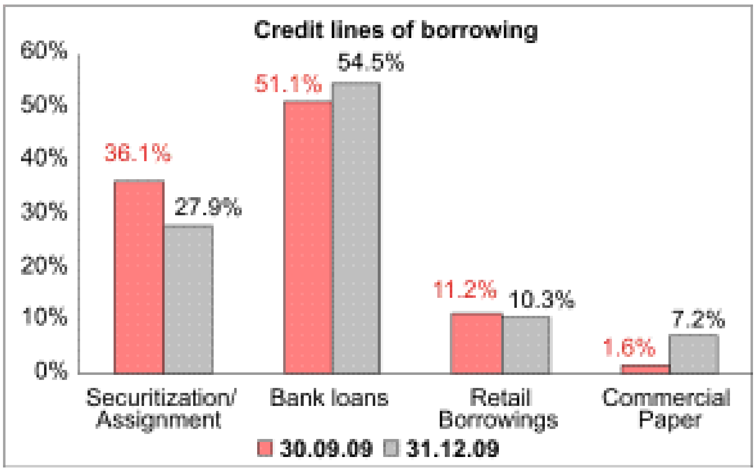
Most of MGFLL's branches are located in South India, particularly in the state of Kerala. In case of a sustained downturn in the economies of south Indian states, or a sustained change in consumer preferences in that region, MGFLL may be impacted. Though MGFLL intends to expand its reach pan-India, South India will remain the revenue driver over the next few years.

**4) Growing competition**

Given that this segment is relatively under-penetrated within the organized lending industry, and its attractiveness in terms of high yields, we expect new players to enter, going forward. Growing competition may impact MGFLL's margins.

**5) Alterations in priority sector lending norms to affect lines of credit from banks**

As of December 31, 2009, MGFLL had credit lines of Rs20.7bn, Rs10.6bn and Rs 3.93bn via bank O/D, securitization and retail borrowings respectively, boosting loan growth. It takes credit lines from various banks viz. SBI, ICICI Bank, Axis Bank, Kotak Mahindra Bank, HDFC Bank, etc. Any changes in priority sector lending norms currently being 40% will affect the credit lines thereby affecting borrowings.




**6) Custody risk; high attrition rates**

Since the business involves keeping custody of sizeable volume of gold jewellery, the company faces the risk of burglaries, etc. Also, retaining staff is a challenge, with high attrition level of ~50%.

## Global Peers

MGFLL has no listed domestic peer, which is focused solely on the LAG segment. We therefore compared it with UK-based pawnbrokers “Harvey & Thompson Pawnbrokers Plc” and “Albemarle Bond Holdings Plc” which are listed on AIM, and also with Cash America International, Inc., based in the US

### Harvey & Thompson Pawnbrokers Plc (UK)

Harvey & Thompson (H&T) a UK-listed pawn broking entity. 89% of CY08 revenues was derived from pawn broking business. 98% of the pawn broking is from gold. Pawn broking will remain a core business for H&T.

**AUM and Pledged book numbers** (£mn)

| For period ended | 31.12.07 | 31.12.08 |
|---|---|---|
| Total AUM | 36.11 | 41.54 |
| Pledged Book | 27.8 | 32.0 |
| Pledged book as a % of total AUM | 77.00% | 77.03% |

### Albemarle Bond Holdings Plc (UK)

Albemarle Bond Holdings, founded 1983, currently has 115 branches in the UK, providing pawn broking, jewellery retailing and associated financial services. Interest rates are charged at 7.5% on monthly basis. The average ticket size of gold loans is £140. Though the tenure of such loans is 6 months, loans are usually repaid within 2-3 months.

In FY09, 46.5% of its revenues and 61% of its gross profit was from pawn broking services. It operates via 2 distinct brands viz. Albemarle Bond and Herbert Brown. All financials for this company are as of June 30, 09.

### Growth in average revenues per branch for MGFLL, exceeded that for Albemarle Bond

The average revenues per branch is higher for Albemarle, but MGFLLs average revenues per branch are growing faster than Albemarle Bond.

**MGFLL**

| For period ending | Mar-31-07 | Mar-31-08 | Mar-31-09 | Dec-31-09 |
|---|---|---|---|---|
| No. of branches | 291 | 436 | 645 | 870 |
| Revenues (RsCr) | 76.20 | 168.17 | 301.95 | 606.64 |
| Average Revenues (RsCr) | 76.20 | 122.18 | 235.06 | 454.30 |
| **Avg. revenues per branch (RsCr)** | **0.26** | **0.28** | **0.36** | **0.52** |
| *Growth %* | | *7.0%* | *30.0%* | *43.3%* |

### Albemarle Bond Holdings

| For period ending | Jun-30-06 | Jun-30-07 | Jun-30-08 | Jun-30-09 |
|---|---|---|---|---|
| No. of branches | 75 | 86 | 111 | 115 |
| Revenues (RsCr) | 202.34 | 225.85 | 321.43 | 380.85 |
| Average Revenues (RsCr) | 202.34 | 214.10 | 273.64 | 351.14 |
| **Avg. revenues per branch (RsCr)** | 2.70 | 2.49 | 2.47 | 3.05 |
| *Growth %* | | *-7.7%* | *-1.0%* | *23.9%* |

(Conversion : 1 £ =Rs68.6)

### Cash America International Inc. (US)

Founded in 1983, listed on the NYSE in 1990, Cash America International Inc. is a provider of secured loans, referred to as pawn loans and operates via 613 locations. These stores operate under the brand names, Cash America Pawn and Super Pawn.

### MGFLL vis-à-vis Global Peers

| Parameters | MGFLL (post-merger) | H&T Pawnbrokers | Albemarle Bond | Cash America International |
|---|---|---|---|---|
| Country of Operations | India | UK | UK | US |
| Products | Lending loans against gold jewellery & hypothe cation loans | Pawnbroking and other financial services | Pawnbroking and other financial services | Pawnbroking and other financial services |
| Currency | INR (Crs) | GBP (mn) | GBP (mn) | USD (mn) |
| Financial Year ending | 31-03-09 | 31-12-09 | 30-6-09 | 31-12-08 |
| Revenues | 301.95 | 83.98 | 55.52 | 1030.79 |
| Profit after Tax | 47.79 | 13.34 | 10.7 | 81.14 |
| Net Profit margin | 15.80% | 15.88% | 19.27% | 7.90% |
| EPS | Rs20.95 | £0.38 | £0.20 | $2.75 |
| Market Cap | 2677 | 84 | 129 | 1234 |
| Market Price | 786.35 | 2.38 | 2.33 | 41.82 |
| Paid-up Equity Capital | 34.04 | 1.8 | 2.22 | 2.95 |
| Face Value | 10.00 | 0.05 | 0.04 | 0.10 |
| P/e (x) | 37.5 | 6.3 | 11.6 | 15.2 |
| P/b (x) | 7.0 | 1.8 | 2.5 | 2.1 |
| Market Cap/AUM (x) | 1.3 | 2.9 | 5.4 | 7 |
| EV / AUM (x) | 2.1 | 3.9 | 6.5 | 9.4 |
| Total pledged AUM | 1259.59 | 32.00 | 26.50 | 168.75 |
| Book- value | 112.10 | 1.33 | 0.93 | 19.51 |
| Debt-equity ratio (x) | 5.2 | 1.2 | 0.8 | 0.8 |
| EV | 2667 | 126 | 173 | 1581 |
| Market Price 52-wk High | 689 | 3 | 3 | 41 |
| Market Price 52-wk Low | 97 | 1 | 2 | 15 |

(Source: Keynote Capitals Institutional Research)

**MGFLL: Latest Quarter and Nine months Performance** **(RsCr)**

| Particulars | Q3 FY09 | Q3 FY10 | *y-o-y* | 9M FY09 | 9M FY10 | *y-o-y* |
|---|---|---|---|---|---|---|
| **Income from Operations** | **44.33** | **131.95** | ***197.7%*** | **110.64** | **322.83** | ***191.8%*** |
| Staff Cost | 7.57 | 12.89 | *70.2%* | 19.96 | 34.66 | *73.7%* |
| Advertisement | 1.30 | 13.50 | *941.6%* | 4.50 | 33.73 | *649.1%* |
| Rent | 1.53 | 3.63 | *136.4%* | 3.57 | 8.39 | *135.2%* |
| Bad debts & prov. for doubtful debts | 4.03 | 3.03 | *-24.7%* | 11.71 | 9.87 | *-15.7%* |
| Other Expenditure | 4.49 | 7.86 | *75.0%* | 13.04 | 19.52 | *49.7%* |
| Total Expenditure | 18.92 | 40.91 | *116.2%* | 52.78 | 106.18 | *101.2%* |
| **EBITDA** | **25.40** | **91.04** | ***258.4%*** | **57.86** | **216.66** | ***274.4%*** |
| Other Income | 0.81 | 0.19 | *-76.9%* | 0.94 | 1.08 | *14.5%* |
| Interest | 12.41 | 36.99 | *197.9%* | 24.33 | 94.28 | *287.5%* |
| **PBDT** | **13.79** | **54.24** | ***293.2%*** | **34.47** | **123.45** | ***258.1%*** |
| Depreciation | 0.83 | 1.51 | *81.5%* | 2.15 | 3.92 | *82.2%* |
| **PBT** | **12.96** | **52.73** | ***306.8%*** | **32.32** | **119.53** | ***269.9%*** |
| Tax | 4.21 | 17.74 | *321.1%* | 10.89 | 40.60 | *272.6%* |
| **PAT** | **8.75** | **34.99** | ***299.9%*** | **21.42** | **78.93** | ***268.5%*** |
| **Paid up equity capital** | **14.28** | **17.26** | | **14.28** | **17.26** | |
| **EPS (Rs)** | **6.13** | **20.28** | | **15.00** | **45.74** | |

**Comments on Q3-FY10 Results**

- Outstanding equity shares of the unmerged entity (17.3mn) only are considered, since the expanded equity capital of 28.9mn shares of the merged entity is effective January 11, 2010.
- Our analysis of the cost structure reveals that advertisement costs increased 731bps, as it entered new regions in India. As bad debts fell 679 bps along with operating cost efficiencies, overall expenditure as % of total sales dipped 11.7 pps.
- PAT margin expanded sharply from 19.7% in Q3-09 to 26.5% in Q3-10, helped by growth at operating level in spite of higher interest costs.

**Cost Structure (% of sales)**

| | Q3-09 | Q3-10 | *y-o-y* | 9 mnts 2008 | 9 mnts 2009 | *y-o-y* |
|---|---|---|---|---|---|---|
| Staff Cost | 17.1% | 9.8% | *-732* | 18.0% | 10.7% | *-730* |
| Advertisement | 2.9% | 10.2% | *731* | 4.1% | 10.4% | *638* |
| Rent | 3.5% | 2.7% | *-71* | 3.2% | 2.6% | *-63* |
| Bad debts & prov. for doubtful debts | 9.1% | 2.3% | *-679* | 10.6% | 3.1% | *-753* |
| Other Expenditure | 10.1% | 6.0% | *-418* | 11.8% | 6.0% | *-574* |
| **Total Expenditure** | **42.7%** | **31.0%** | ***-1169*** | **47.7%** | **32.9%** | ***-1482*** |

**Key Data-points for Q3-FY10**

| Particulars | Q3-FY09 | Q2-FY10 | Q3-FY10 | *y-o-y* | *q-o-q* |
|---|---|---|---|---|---|
| Total AUM (RsCr) | 1,095 | 1,784 | 2,260 | *106%* | *27%* |
| Gold loan AUM (RsCr) | 1036 | 1726 | 2178 | *110%* | *26%* |
| No. of Customers | 309,024 | 440,033 | 492,344 | *59%* | *12%* |
| No. of Branches | 588 | 765 | 870 | *48%* | *14%* |
| ROA % | 3.75 | 5.03 | 4.91 | *31%* | *-2%* |
| Cost of borrowings - % | 12.58% | 12.86% | 11.79% | *-6%* | *-8%* |
| Return on Equity % | 31.55% | 34.93% | 41.61% | *32%* | *19%* |
| Head Count - No. | 4,344 | 5,064 | 5,641 | *30%* | *11%* |

(Pre-merger Financials)

## Financials for unmerged MGFLL

**P&L Statements** (RsCr)

| Particulars | FY07 | FY08 | FY09 |
|---|---|---|---|
| Interest income | 54.43 | 120.28 | 213.54 |
| Interest expense | 21.38 | 56.67 | 91.60 |
| **Net Interest income** | **33.05** | **63.61** | **121.94** |
| Fee & other income | 1.62 | 1.70 | 5.58 |
| **Total Operating Income** | **34.67** | **65.31** | **127.52** |
| **Expenditure** | | | |
| Personnel Expenses | 6.06 | 11.48 | 27.70 |
| Other Operating costs | 11.19 | 20.04 | 50.17 |
| Depreciation | 1.07 | 1.83 | 3.37 |
| **Total Expenditure** | **18.31** | **33.35** | **81.24** |
| Profit before tax | 16.35 | 31.96 | 46.28 |
| Tax | 5.74 | 10.97 | 15.99 |
| **Profit after tax** | **10.61** | **20.99** | **30.29** |
| EPS (Rs) | 9.65 | 19.08 | 17.56 |
| Book value (Rs) | 25.57 | 84.53 | 97.28 |
| FVPS (Rs) | 10 | 10 | 10 |
| ROAE % | 37.7% | 34.7% | 23.2% |
| ROAA | 2.5% | 3.9% | 3.3% |

**Balance Sheets** (RsCr)

| Particulars | FY07 | FY08 | FY09 |
|---|---|---|---|
| **Sources of Funds** | | | |
| **Share Capital** | 15.00 | 61.80 | 21.26 |
| Equity Share Capital | 11.00 | 11.00 | 17.26 |
| Preference Share Capital | 4.00 | 4.00 | 4.00 |
| Comp. convertible Preference Shares | 0.00 | 46.80 | 0.00 |
| Share warrants | 0.00 | 0.00 | 3.00 |
| Reserves & Surplus | 13.13 | 31.18 | 143.62 |
| **Total Shareholders funds** | **28.13** | **92.98** | **167.87** |
| Secured Loans | 51.19 | 135.11 | 371.24 |
| Unsecured Loans | 42.09 | 39.39 | 79.85 |
| Assignments | 300.90 | 393.01 | 538.14 |
| **Total Loan Funds** | **394.19** | **567.51** | **989.23** |
| **Total Liabilities** | **422.31** | **660.49** | **1157.10** |
| **Applications of Funds** | | | |
| **Gross Block** | **13.37** | **20.81** | **35.56** |
| Less: Acc. Depn | 2.68 | 4.49 | 7.79 |
| **Net Block** | **10.69** | **16.32** | **27.78** |
| CWIP | 0.00 | 0.00 | 0.26 |
| Investments | 2.90 | 2.93 | 1.08 |
| **Curr Assets, Loans and Adv.** | | | |
| Cash & Bank balances | 21.57 | 67.22 | 113.40 |
| Other Current Assets | 15.62 | 20.27 | 67.59 |
| **Loans & Advances** | **396.81** | **578.32** | **986.74** |
| Total Current Assets | 434.00 | 665.81 | 1167.73 |
| Total Current liabilities | 25.08 | 24.53 | 41.10 |
| Net Current Assets | 408.92 | 641.28 | 1126.63 |
| Net Deferred Tax | -0.10 | -0.04 | 1.36 |
| **Total Assets** | **422.41** | **660.49** | **1157.10** |

**Note:** In order to give a better perspective, we have also considered the line item 'Assignments' in the Balance sheet. Therefore the current numbers in our report may not match with those in the annual report.

## Financials for unmerged MFTL

**P&L Statements** (RsCr)

| Particulars | FY07 | FY08 | FY09 |
|---|---|---|---|
| Interest Income | 21.77 | 47.89 | 88.41 |
| Interest Expense | 10.52 | 25.92 | 43.24 |
| **Net Interest Income** | **11.25** | **21.96** | **45.17** |
| Fees & Other Income | 0.43 | 0.69 | 0.70 |
| **Total Operating Income** | **11.69** | **22.65** | **45.88** |
| **Expenditure** | | | |
| Personnel Expenses | 2.13 | 6.35 | 9.05 |
| Other Operating costs | 2.41 | 5.12 | 9.87 |
| Depreciation | 0.27 | 0.68 | 0.39 |
| **Total Expenditure** | **4.81** | **12.15** | **19.31** |
| Profit before Tax | 6.88 | 10.51 | 26.57 |
| Tax | 2.42 | 3.58 | 9.07 |
| **Profit after Tax** | **4.46** | **6.93** | **17.50** |
| EPS (Rs) | 13.74 | 21.31 | 31.48 |
| Book value (Rs) | 29.22 | 14.57 | 158.10 |
| FVPS (Rs) | 10 | 10 | 10 |
| ROAE % | 47.0% | 28.8% | 27.7% |
| ROAA | 2.2% | 3.1% | 5.1% |

**Balance Sheets** (RsCr)

| Particulars | FY07 | FY08 | FY09 |
|---|---|---|---|
| **Sources of Funds** | | | |
| **Share Capital** | **3.25** | **26.45** | **5.56** |
| Equity Share Capital | 3.25 | 3.25 | 5.56 |
| Preference Share Capital | 0.00 | 23.20 | 0.00 |
| Reserves & Surplus | 6.25 | 12.09 | 82.34 |
| **Total Shareholders funds** | **9.50** | **38.54** | **87.90** |
| Secured Loans | 36.63 | 38.56 | 99.81 |
| Unsecured Loans | 2.32 | 2.68 | 9.75 |
| Assignments | 153.08 | 173.06 | 238.37 |
| **Total Liabilities** | **201.52** | **252.85** | **435.83** |
| **Applications of Funds** | | | |
| **Gross Block** | **3.63** | **6.03** | **7.05** |
| Less: Acc. depn | 0.49 | 1.17 | 1.52 |
| **Net Block** | **3.14** | **4.86** | **5.53** |
| Curr. Assets, Loans & Adv. | | | |
| Cash & Bank Bal. | 19.02 | 30.99 | 154.28 |
| Other Current Aassets | 6.04 | 5.03 | 18.16 |
| **Loans & Advances** | **175.60** | **214.93** | **272.85** |
| Total Current Assets | 200.66 | 250.96 | 445.28 |
| Total Current Liabilities | 2.17 | 2.90 | 15.00 |
| Net Current Assets | 198.49 | 248.06 | 430.28 |
| Deferred Tax Liability (net) | 0.10 | 0.08 | (0.02) |
| **Total Assets** | **201.52** | **252.85** | **435.83** |

## Post merger Projected Financials (MGFLL & MFTL)

**P&L Statements** (RsCr)

| Particulars | FY10E | FY11E | FY12E |
|---|---|---|---|
| Interest Income | 604.45 | 1012.71 | 1555.01 |
| Interest Expense | 235.67 | 405.15 | 646.33 |
| **Net Interest Income** | **368.78** | **607.56** | **908.68** |
| Fees & Other Income | 13.90 | 23.29 | 35.77 |
| **Total Operating Income** | **382.68** | **630.85** | **944.44** |
| **Expenditure** | | | |
| Personnel Expenses | 66.60 | 112.00 | 158.40 |
| Other Operating costs | 125.77 | 202.81 | 252.22 |
| Depreciation | 7.18 | 9.66 | 16.24 |
| **Total Expenditure** | **199.55** | **324.47** | **426.87** |
| Profit before Tax | 183.13 | 306.38 | 517.58 |
| Tax | 62.99 | 105.38 | 178.03 |
| **Profit after Tax** | **120.14** | **201.00** | **339.55** |
| Preference Dividend | 0.30 | 0.30 | 0.00 |
| **PAT for Equity Shareholders** | **119.84** | **200.70** | **339.55** |
| EPS (Rs) | 35.29 | 59.04 | 99.74 |
| Book value (Rs) | 183.68 | 242.63 | 340.02 |
| ROAE % | 27.3% | 27.7% | 34.2% |
| ROAA | 5.5% | 5.4% | 5.9% |

(E - Keynote Capitals Institutional Research Estimates)

**Balance Sheets** (RsCr)

| Particulars | FY10E | FY11E | FY12E |
|---|---|---|---|
| **Sources of Funds** | | | |
| Equity share capital | 34.04 | 34.04 | 34.04 |
| Preference share capital | 4.00 | 4.00 | 0.00 |
| Reserves and surplus | 587.26 | 787.96 | 1,123.51 |
| **Total Shareholders funds** | **625.30** | **826.00** | **1,157.55** |
| Secured Loans | 1,076.14 | 2,226.70 | 3,433.29 |
| Unsecured Loans | 120.63 | 211.64 | 309.27 |
| Securitization/Assignments | 957.42 | 1,409.66 | 1,984.69 |
| Total Borrowings | 2,154.19 | 3,848.00 | 5,727.25 |
| **Total Liabilities** | **2,779.50** | **4,674.00** | **6,884.80** |
| **Applications of Funds** | | | |
| **Gross Block** | **81.60** | **109.80** | **184.60** |
| Less: Acc Depn | 16.49 | 26.15 | 42.40 |
| **Net Block** | **65.11** | **83.65** | **142.20** |
| Investments | 2.39 | 3.81 | 5.67 |
| **Curr Assets, Loans & Adv.** | | | |
| Cash/ bank bal & Other Curr Assets | 418.87 | 944.86 | 1,309.90 |
| **Loans and advances** | **2,393.55** | **3,809.90** | **5,670.54** |
| Total Current Assets | 2,812.42 | 4,754.76 | 6,980.44 |
| Total Current liabilities | 98.73 | 166.91 | 244.28 |
| Net current assets | 2,713.69 | 4,587.85 | 6,736.15 |
| Net deferred tax | -1.7 | -1.3 | 0.77 |
| **Total Assets** | **2,779.50** | **4,674.00** | **6,884.80** |

(E - Keynote Capitals Institutional Research Estimates)

**Assumptions for future projections**

Equity Share Capital enhanced from Rs17.26Cr in FY09 to Rs34.04Cr in FY10E on account of merger, QIP and conversion of share warrants.

- 17.26mn equity shares outstanding as on December 2009. Post merger on January 11, 2010, the number of equity shares increased to 28.93mn.
- Dilution of account of QIP effective FY10E itself (QIP of Rs245Cr @ Rs691 per share)
- Warrant conversion is taken in account effective FY10E. 1.6mn warrants @ Rs166.62 each were issued to promoters in Sep, 2008 and were to be converted into equity shares of Rs10 each within 18 months.

Preference share capital

0.4mn preference shares of Rs100 each fully paid up issued to promoters, to be redeemed at par by September, 2011. Shareholders have a right to early redemption but not earlier than 2 years from the date of allotment. We have factored the redemption of preference shares in FY12E.

Tax rate of 34.4% p.a.

Average gold prices of Rs15755 for FY10E.

In spite of dilution on account of QIP, average ROE going forward is expected to remain in the range of 29.7%, considering 68.3% CAGR in the bottom line during FY09-12E.

Management has approved on March 19, 2010, a bonus issue in the ratio of 1:1 and stock split in the ratio of 5.1 (face value to be reduced from Rs10 to Rs2 per share).

**Key Data Points**

| Particulars | FY09 | FY10E | FY11E | FY12E |
|---|---|---|---|---|
| Yield on loan assets | 29.4% | 25.0% | 25.0% | 26.0% |
| Cost of borrowings | 12.7% | 13.5% | 13.5% | 13.5% |
| Spread | 16.7% | 11.5% | 11.5% | 12.5% |
| NIM | 13.3% | 15.4% | 15.9% | 16.0% |
| Cost to income ratio | 55.8% | 50.3% | 49.9% | 43.5% |
| Net Interest Income / Avg. Assets | 13.3% | 16.9% | 16.3% | 15.7% |
| Fee and other income / Avg. Assets | 0.5% | 0.6% | 0.6% | 0.6% |
| Total Operating Income / Avg. Assets | 13.8% | 17.5% | 16.9% | 16.3% |
| Average AUM (RsCr) | 1,278.02 | 2,417.79 | 4,050.84 | 5,980.80 |
| Average Loan Book (RsCr) | 1,026.42 | 1,826.57 | 3,101.73 | 4,740.22 |
| Average Networth (RsCr) | 193.65 | 440.54 | 725.65 | 991.78 |
| Average Borrowings (RsCr) | 1,059.49 | 1,745.68 | 3,001.10 | 4,787.62 |
| Average total assets (RsCr) | 1,253.14 | 2,186.21 | 3,726.75 | 5,779.40 |

(E - Keynote Capitals Institutional Research Estimates)

### Growth Rates

| Particulars | FY09 | FY10E | FY11E | FY12E |
|---|---|---|---|---|
| AUM | 70.7% | 100.0% | 51.3% | 45.2% |
| Loan Book | 58.8% | 90.0% | 59.2% | 48.8% |
| Net Worth | 94.5% | 144.5% | 32.1% | 40.1% |
| Borrowings | 71.0% | 61.1% | 78.6% | 48.8% |
| Total Assets | 74.4% | 74.5% | 68.2% | 47.3% |
| Net Interest Income | 95.3% | 120.7% | 64.7% | 49.6% |
| Operating income | 97.1% | 120.7% | 64.8% | 49.7% |
| Net Profit | 72.0% | 152.3% | 67.5% | 69.2% |
| EPS (Rs) | 6.9% | 68.5% | 67.3% | 68.9% |
| Book value (Rs) | 21.5% | 63.8% | 32.1% | 40.1% |

(E - Keynote Capitals Institutional Research Estimates)

### Valuation Matrix

| Particulars | FY09 | FY10E | FY11E | FY12E |
|---|---|---|---|---|
| No. of Equity Shares (mn) | 17.26 | 34.04 | 34.04 | 34.04 |
| EPS (Rs) | 20.95 | 35.29 | 59.04 | 99.74 |
| Book value (Rs) | 112.10 | 183.68 | 242.63 | 340.02 |
| P/e (x) | 37.5 | 22.3 | 13.3 | 7.9 |
| P/b (x) | 7.0 | 4.3 | 3.2 | 2.3 |
| Market Cap / AUM (x) | 1.1 | 0.8 | 0.5 | 0.4 |
| EV / AUM (x) | 1.8 | 1.4 | 1.2 | 1.0 |
| ROAE | 24.7% | 27.3% | 27.7% | 34.2% |
| ROAA | 3.0% | 5.5% | 5.4% | 5.9% |

(E - Keynote Capitals Institutional Research Estimates)

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**Keynote Capitals Ltd.**

**Member**

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