

RESULT NOTE

Mkt Cap: Rs34.4bn; US\$750m

Analyst: Pathik Gandotra (91-22-6622 2525; pathik@idfcsski.com)
 Chinmaya Garg (91-22-6622 2563; chinmaya@idfcsski.com)
 Sameer Bhise (91-22-6622 2574; sameer@idfcsski.com)

Result: Q3FY10

Comment: Strong expansion in margins, Gross NPAs decline

Revision: Earnings estimates upgraded by 28.8% for FY10 and 14.2% for FY11

Key valuation metrics

| Year to March 31 (Rs m) | NII | yoy chg (%) | Net profit | yoy chg (%) | EPS (Rs) | Adj. Bk Val | P/ Adj.Bk | PER | RoE |
|-------------------------|--------|-------------|------------|-------------|----------|-------------|-----------|------|------|
| | | | | | (Rs) | (Rs/ share) | (x) | (x) | (%) |
| FY07 | 5,050 | 33.1 | 1,329.2 | 21.8 | 15.6 | 85.7 | 4.1 | 22.8 | 18.1 |
| FY08 | 7,497 | 48.5 | 1,770.1 | 33.2 | 18.3 | 132.0 | 2.7 | 19.4 | 16.9 |
| FY09 | 8,550 | 14.0 | 2,145.2 | 21.2 | 22.1 | 152.8 | 2.3 | 16.1 | 15.4 |
| FY10E | 9,882 | 15.6 | 3,225.9 | 50.4 | 33.3 | 194.6 | 1.8 | 10.7 | 20.1 |
| FY11E | 11,533 | 16.7 | 3,569.9 | 10.7 | 36.8 | 238.9 | 1.5 | 9.6 | 18.9 |

Highlights of Q3FY10 results

Mahindra & Mahindra Finance ('MMFIN') reported PAT of ~Rs950m, ~113% yoy growth – ahead of our estimates of Rs699m. The outperformance was led by sharply lower provisioning expenses (~16% qoq).

- **Healthy NII growth; strong expansion in margins:** MMFIN reported NII of ~Rs2.57bn – a 21.6% yoy growth, buoyed by expansion in margins. Margins continued to improve - up 50bp qoq (124bp yoy) - to 12.25% led by ~180bp qoq expansion in loan yields. Yield expansion was driven by higher incremental disbursements of tractor loans (a relatively high yielding product). Net of securitization gains, NII growth is at ~17% yoy. (Exhibit 1)
- **Gross NPAs decline, provision coverage improves:** Gross NPAs declined by 30bp qoq to 8.7% in Q3FY10. In absolute terms, GNPA remained steady at Rs7.9bn. Net NPAs declined by ~50bp qoq to 2.3%, resulting in coverage ratio improving by ~370bp qoq to 74.9% in Q3FY10. Contrary to expectations, the monsoon deficit has not had a detrimental impact on asset quality, which is a positive. (Exhibit 5)
- **Lower provisions bolster bottom-line:** In line with improving asset quality, provisions were sharply below estimates at Rs502mn. Provisions to average loans ratio has declined by 60bp qoq to 2.4%. Notably, collection efficiency has improved to ~92%.
- **Strong momentum in disbursements:** Disbursements grew by a strong 74% yoy to and 9% qoq to Rs23.7bn. Of the total, 36% of disbursements are from Auto/UV segment, another 29% from cars. Average monthly contracts increased by ~23% qoq. Since Q1FY10, disbursement momentum has picked up sequentially buoyed by improved access to funds and economic revival. (Exhibit 2)
- **Loan book composition broadly stable:** Product mix (as a % of AUM) saw some changes on a yoy basis. UVs financed as a % of total AUM stood at 35%, lower than ~39% in Q3FY09. Cars gained share comprising 28% of AUM (from 24% in Q3FY09). (Exhibit 4)

IDFC - SSKI Securities Ltd.

Naman Chambers, C-32, G- Block, Bandra-Kurla Complex, Bandra (East), Mumbai 400 051 Tel: 91-22-6622 2600 Fax: 91-22-6622 2501

“For Private Circulation only” and “Important disclosures appear at the back of this report”

- **Banks dominate funding mix:** During Q3FY10, bank loans increased to ~64% of funding mix (from ~61% in Q2FY10) as the company entered into term loans at attractive rates. Over the last year, bank loans dominated incremental funding mix as MMFIN is focused on reducing dependence on mutual funds and insurance companies in the aftermath of the liquidity crisis. (Exhibit 3)

Valuations & View

In Q3FY10, MMFIN reported strong NII growth buoyed by continued expansion in margins as wholesale borrowings re-priced at lower rates while yields improved on a qoq basis. In a key positive, Gross NPLs declined by 30bp qoq (steady in absolute terms) on the back of higher collection efficiency and improving economic environment. Disbursements continued to demonstrate momentum (up by ~9% qoq), with outlook for the year indicated to be robust. The company's asset quality woes may well have bottomed-out and pick up in economic activity should catalyze core performance. We are upgrading our estimates for FY10 by 28.8% and FY11 by 14.2% to factor in margin expansion, strong revival in business volumes and declining provisioning costs from our earlier conservative stance. Stock is currently trading at 1.5x FY11E adjusted book and a PE of 9.6x FY11E. Reiterate Outperformer with a 12-month price target of Rs430 (~1.8x FY11 adjusted book and 12x FY11E EPS).

Quarterly results

| P&L (Rs m) | Q3FY09 | Q4FY09 | Q1FY10 | Q2FY10 | Q3FY10 | FY09 | FY10E | FY11E | Comments |
|------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|---------------|---|
| Interest income | 3,532 | 3,893 | 3,202 | 3,530 | 3,939 | 13,648 | 15,052 | 17,679 | |
| of which securitization income | 213 | 426 | 164 | 165 | 340 | 1,043 | 1,413 | 1,679 | |
| Net interest income | 2,120 | 2,622 | 1,992 | 2,325 | 2,578 | 8,550 | 9,882 | 11,533 | Ahead of estimates as margins expand strongly; NII (net of securitization) up 17% yoy |
| yoy growth (%) | 10.2 | 10.7 | 8.1 | 18.3 | 21.6 | 14.0 | 15.6 | 16.7 | |
| Other income | 34 | 83 | 91 | 95 | 81 | 198 | 357 | 411 | |
| Operating expenses | 679 | 642 | 703 | 790 | 754 | 2,668 | 3,021 | 3,452 | |
| yoy growth (%) | 12 | (4) | 19 | 5 | 11 | 5.6 | 13.2 | 14.3 | Employee expenses decline as Q2FY10 had bonus payments to employees |
| Operating profit | 1,475 | 2,063 | 1,380 | 1,630 | 1,905 | 6,080 | 7,218 | 8,492 | |
| yoy growth (%) | 7.8 | 17.1 | 6.3 | 31.0 | 29.2 | 17.3 | 18.7 | 17.6 | |
| Provisions & write-offs | 788 | 458 | 778 | 596 | 503 | 2,824 | 2,330 | 2,999 | Lower than expected provisions as gross NPAs decline |
| Profit before tax | 687 | 1,605 | 602 | 1,034 | 1,402 | 3,256 | 4,888 | 5,452 | |
| yoy growth (%) | 5.0 | 38.0 | 43.8 | 89.3 | 104.2 | 19.7 | 50.1 | 12.4 | |
| Profit after tax | 445 | 1,080 | 400 | 692 | 950 | 2,145 | 3,226 | 3,570 | Beats estimates due to lower than expected provisions and stronger margin expansion |
| yoy growth (%) | 4.8 | 43.3 | 49.5 | 96.5 | 113.4 | 21.2 | 50.4 | 10.7 | |

Quarterly results

| Ratios (%) | Q3FY09 | Q4FY09 | Q1FY10 | Q2FY10 | Q3FY10 | FY09 | FY10E | FY11E | Comments |
|-----------------------------------|--------|--------|--------|--------|--------|--------|--------|---------|---|
| Gross spread (reported) | 11.00 | 12.20 | 10.60 | 11.10 | 11.70 | | | | Up 60bp qoq |
| Spread on loans (calculated) | 8.2 | 10.3 | 8.3 | 9.5 | 9.3 | 9.1 | 9.2 | 8.9 | |
| NIMs | 11.0 | 14.0 | 10.6 | 11.8 | 12.3 | 11.8 | 12.0 | 11.5 | Decline in cost of funds as wholesale liabilities re-price at lower rates fuelled margins expansion of 124bp yoy and 50bp qoq |
| NIM (net of securitization) | 9.9 | 11.8 | 9.8 | 10.9 | 10.6 | 10.4 | 10.3 | 9.8 | Rs3.3bn of fresh securitization undertaken |
| Other income / avg assets | 0.2 | 0.4 | 0.5 | 0.5 | 0.4 | 0.3 | 0.4 | 0.4 | |
| Total operating exp / avg assets | 3.5 | 3.4 | 3.8 | 4.0 | 3.6 | 3.7 | 3.7 | 3.5 | |
| Cost-Income ratio | 31.5 | 23.7 | 33.8 | 32.7 | 28.3 | 30.5 | 29.9 | 29.0 | |
| Provisions / avg assets | 4.1 | 2.5 | 4.2 | 3.0 | 2.4 | 3.9 | 2.9 | 3.0 | In line with decline in Gross NPAs, provision costs decline |
| PBT/Avg assets | 3.6 | 8.6 | 3.2 | 5.2 | 6.7 | 4.5 | 5.8 | 5.5 | |
| Tax/PBT | 35.2 | 32.7 | 33.5 | 33.1 | 32.3 | 34.1 | 34.5 | 35.0 | |
| PAT/avg assets | 2.3 | 5.8 | 2.1 | 3.5 | 4.5 | 3.0 | 3.8 | 3.5 | |
| CRAR (%) | 18.9 | 19.5 | 18.8 | 17.7 | 19.4 | | | | Comfortably capitalized against regulatory requirement of 12% |
| Tier-I CRAR (%) | 16.8 | 17.4 | 17.2 | 16.2 | 16.8 | | | | |
| Balance Sheet (Rsbn) | | | | | | | | | |
| Advances | 70,857 | 68,384 | 69,630 | 77,206 | 78,855 | 68,383 | 81,972 | 102,447 | Some pick up qoq as disbursals gather momentum |
| yoy growth (%) | 5.4 | 2.9 | 2.0 | 3.3 | 11.3 | 6.7 | 19.9 | 25.0 | |
| Total Assets | 75,024 | 74,439 | 75,466 | 82,690 | 85,628 | 74,439 | 89,070 | 110,886 | |
| yoy growth (%) | (5.1) | (0.8) | 1.4 | 9.6 | 3.6 | 6.0 | 19.7 | 24.5 | |
| Borrowings (excl. securitization) | 53,737 | 52,130 | 51,502 | 58,173 | 61,292 | 52,130 | 63,791 | 82,197 | Bank loans dominate incremental funding mix. |

Exhibit 1: Margins expand as cost of funds decline (%)

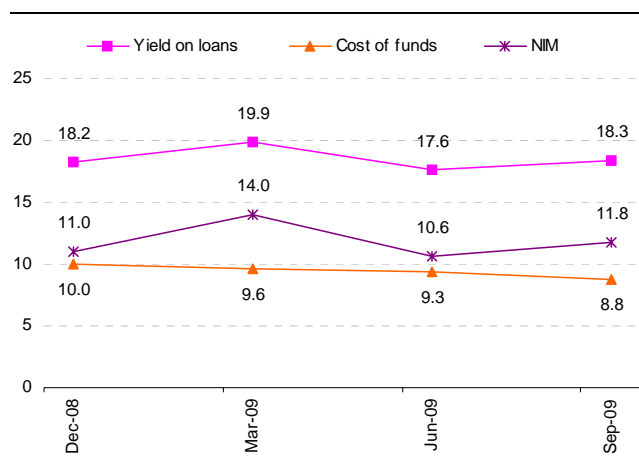
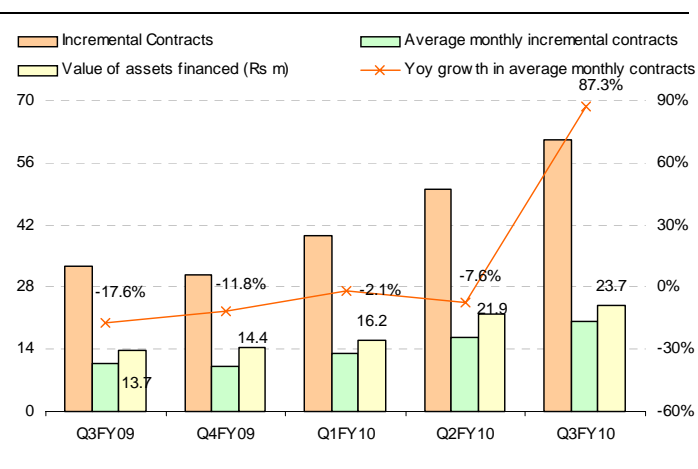


Exhibit 2: Disbursements show strong recovery



*NIMs gross of securitization, calculated ratios on average quarterly balances

Exhibit 3: Bank loans dominate incremental funding (Rsbn)

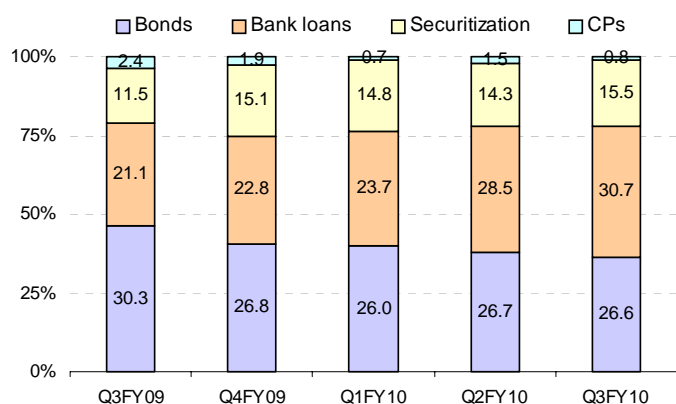


Exhibit 4: Composition of AUM broadly stable

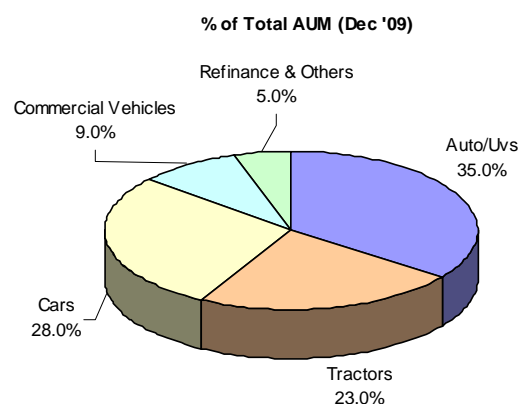


Exhibit 5: Gross NPAs decline; coverage improves

| For the quarter ended (%) | Dec-08 | Sep-09 | Dec-09 | yoy chg (% / bps) | qoq chg (% / bps) |
|----------------------------|--------|--------|--------|-------------------|-------------------|
| Gross NPAs (Rs mn) | 8,082 | 7,933 | 7,988 | 0.9 | 0.0 |
| Net NPAs (Rs mn) | 2,857 | 2,285 | 2,001 | (27.2) | (2.5) |
| Gross NPAs (%) | 10.1 | 9.0 | 8.7 | (40) | (80) |
| Net NPAs (%) | 3.8 | 2.8 | 2.3 | (120) | (30) |
| Provisioning coverage | 64.6 | 71.2 | 74.9 | 1,108 | 73 |
| Provisions / average loans | 4.3 | 3.2 | 2.6 | (66) | (126) |

Exhibit 6: Performance of insurance subsidiary

| Rs mn | Q3FY09 | Q2FY10 | Q3FY10 | YoY growth (%) |
|--------------|--------|--------|--------|----------------|
| Total Income | 58 | 68 | 88 | 24.2 |
| PBT | 23 | 34 | 52 | 50.0 |
| PAT | 14 | 22 | 34 | 56.3 |

IDFC - SSKI INDIA

| Analyst | Sector/Industry/Coverage | E-mail | Tel. +91-22-6622 2600 |
|----------------------|---|-----------------------------|-----------------------|
| Pathik Gandotra | Head of Research: Financials, Strategy | pathik@idfcsski.com | 91-22-662 22525 |
| Shirish Rane | Construction, Power, Cement | shirish@idfcsski.com | 91-22-662 22575 |
| Nikhil Vora | FMCG, Media, Mid Caps, Education, Exchanges | nikhilvora@idfcsski.com | 91-22-662 22567 |
| Ramnath S | Automobiles, Auto ancillaries, Real Estate, Oil & Gas | ramnaths@idfcsski.com | 91-22-662 22570 |
| Nitin Agarwal | Pharmaceuticals | nitinagarwal@idfcsski.com | 91-22-662 22568 |
| Chirag Shah | Metals & Mining, Telecom, Pipes, Textiles | chirag@idfcsski.com | 91-22-662 22564 |
| Bhoomika Nair | Logistics, Engineering | bhoomika@idfcsski.com | 91-22-662 22561 |
| Hitesh Shah, CFA | IT Services | hitesh.shah@idfcsski.com | 91-22-662 22565 |
| Bhushan Gajaria | Retailing, FMCG, Media, Mid Caps | bhushangajaria@idfcsski.com | 91-22-662 22562 |
| Salil Desai | Construction, Power, Cement | salil@idfcsski.com | 91-22-662 22573 |
| Ashish Shah | Construction, Power, Cement, Telecom | ashishshah@idfcsski.com | 91-22-662 22560 |
| Probal Sen | Oil & Gas | probal@idfcsski.com | 91-22-662 22569 |
| Chinmaya Garg | Financials | chinmaya@idfcsski.com | 91-22-662 22563 |
| Aniket Mhatre | Automobiles, Auto ancillaries | aniket@idfcsski.com | 91-22-662 22559 |
| Abhishek Gupta | Telecom | abhishek.gupta@idfcsski.com | 91-22-662 22661 |
| Ritesh Shah | Pharmaceuticals, IT Services | riteshshah@idfcsski.com | 91-22-662 22571 |
| Saumil Mehta | Metals, Pipes | saumil.mehta@idfcsski.com | 91-22-662 22578 |
| Vineet Chandak | Real Estate | vineet.chandak@idfcsski.com | 91-22-662 22579 |
| Swati Nangalia | Mid Caps, Media, Exchanges | swati@idfcsski.com | 91-22-662 22576 |
| Sameer Bhise | Strategy, Financials | sameer@idfcsski.com | 91-22-662 22574 |
| Nikhil Salvi | Construction, Power, Cement | nikhil.salvi@idfcsski.com | 91-22-662 22566 |
| Shweta Dewan | Mid Caps, Education, FMCG | shweta.dewan@idfcsski.com | 91-22-662 22577 |
| Dharmendra Sahu | Database Analyst | dharmendra@idfcsski.com | 91-22-662 22580 |
| Rupesh Sonawale | Database Analyst | rupesh@idfcsski.com | 91-22-662 22572 |
| Dharmesh Bhatt | Technical Analyst | dharmesh@idfcsski.com | 91-22-662 22534 |
| Equity Sales/Dealing | Designation | E-mail | Tel. +91-22-6622 2500 |
| Naishadh Paleja | MD, CEO | naishadh@idfcsski.com | 91-22-6622 2522 |
| Paresh Shah | MD, Dealing | paresh@idfcsski.com | 91-22-6622 2508 |
| Vishal Purohit | MD, Sales | vishal@idfcsski.com | 91-22-6622 2533 |
| Nikhil Gholani | MD, Sales | nikhil@idfcsski.com | 91-22-6622 2529 |
| Sanjay Panicker | Director, Sales | sanjay@idfcsski.com | 91-22-6622 2530 |
| V Navin Roy | Director, Sales | navin@idfcsski.com | 91-22-6622 2528 |
| Suchit Sehgal | AVP, Sales | suchit@idfcsski.com | 91-22-6622 2532 |
| Pawan Sharma | MD, Derivatives | pawan.sharma@idfcsski.com | 91-22-6622 2539 |
| Jignesh Shah | AVP, Derivatives | jignesh@idfcsski.com | 91-22-6622 2536 |
| Sunil Pandit | Director, Sales trading | sunil@idfcsski.com | 91-22-6622 2524 |
| Mukesh Chaturvedi | SVP, Sales trading | mukesh@idfcsski.com | 91-22-6622 2512 |
| Viren Sompura | VP, Sales trading | viren@idfcsski.com | 91-22-6622 2527 |
| Rajashekhar Hiremath | VP, Sales trading | rajashekhar@idfcsski.com | 91-22-6622 2516 |

Disclaimer

This document has been prepared by IDFC-SSKI Securities Ltd (IDFC-SSKI). IDFC-SSKI and its subsidiaries and associated companies are full-service, integrated investment banking, investment management and brokerage group. Our research analysts and sales persons provide important input into our investment banking activities.

This document does not constitute an offer or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction.

The information contained herein is from publicly available data or other sources believed to be reliable. While we would endeavor to update the information herein on reasonable basis, IDFC-SSKI, its subsidiaries and associated companies, their directors and employees ("IDFC-SSKI and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent IDFC-SSKI and affiliates from doing so.

We do not represent that information contained herein is accurate or complete and it should not be relied upon as such. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved). The investment discussed or views expressed may not be suitable for all investors.

Affiliates of IDFC-SSKI may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject IDFC-SSKI and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

Reports based on technical analysis centers on studying charts of a stock's price movement and trading volume, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals.

IDFC-SSKI & affiliates may have used the information set forth herein before publication and may have positions in, may from time to time purchase or sell or may be materially interested in any of the securities mentioned or related securities. IDFC-SSKI and affiliates may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall IDFC-SSKI, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind. Any comments or statements made herein are those of the analyst and do not necessarily reflect those of IDFC-SSKI and affiliates.

This Document is subject to changes without prior notice and is intended only for the person or entity to which it is addressed to and may contain confidential and/or privileged material and is not for any type of circulation. Any review, retransmission, or any other use is prohibited.

Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. IDFC-SSKI will not treat recipients as customers by virtue of their receiving this report.

Explanation of Ratings:

1. Outperformer: More than 10% to Index
2. Neutral: Within 0-10% to Index
3. Underperformer: Less than 10% to Index

Disclosure of interest:

1. IDFC - SSKI and its affiliates may have received compensation from the company covered herein in the past twelve months for Issue Management, Capital Structure, Mergers & Acquisitions, Buyback of shares and Other corporate advisory services.
2. Affiliates of IDFC - SSKI may have mandate from the subject company.
3. IDFC - SSKI and its affiliates may hold paid up capital of the company.
4. IDFC - SSKI and its affiliates, their directors and employees may from time to time have positions in or options in the company and buy or sell the securities of the company(ies) mentioned herein.

Copyright in this document vests exclusively with IDFC-SSKI