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SYSTEMATIX INSTITUTIONAL EQUITIES

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Institutional Equities

## Mahindra and Mahindra Financial Services 30 January 2024

## Lower provisioning drive beat in earnings; Stressed asset pool stable

## RESULT UPDATE

Sector: NBFCs Rating: HOLD

CMP: Rs 279 Target Price: Rs 260

## Stock Info

Sensex/Nifty	71,130/21,520
Bloomberg	MMFS IN
Equity shares	1,235mn
52-wk High/Low	346/216
Face value	Rs 2
M-Cap	Rs.348bn/USD 4.2bn
3-m Avg volume	USD 13.6mn

## Financial Snapshot (Rs mn)

Y/E March	FY24E	FY25E	FY26E
NII	66,222	77,642	91,042
PPP	40,836	49,801	62,536
PAT	17,241	24,453	31,594
EPS (Rs)	14.0	19.8	25.6
EPS Gr. (%)	-13.1	41.8	29.2
BV/Sh (Rs)	147	159	175

## Ratios

NIM (%)	7.2	7.0	6.9
C/I ratio (%)	42.1	39.8	36.8
RoA (%)	1.6	2.0	2.2
RoE (%)	9.8	12.9	15.3
Payout (%)	39.0	39.0	39.0

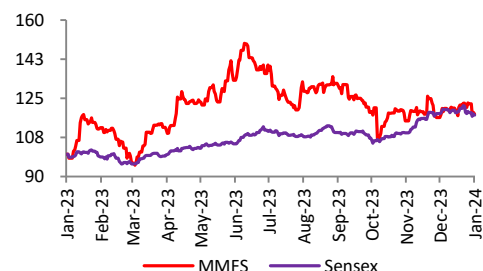
## Valuations

P/E (x)	20.0	14.1	10.9
P/BV (x)	1.9	1.8	1.6
Div. Yield (%)	2.0	2.8	3.6

## Shareholding pattern (%)

	Jun'23	Sep'23	Dec'23
Promoter	52.2	52.2	52.2
-Pledged	-	-	-
FII	13.9	14.1	12.7
DII	26.9	25.8	26.9
Others	7.0	7.9	8.2

## Stock Performance (1-year)



Mahindra and Mahindra Financial Services (MMFS) reported in-line NII at Rs17bn aided by 25%yoy growth in AUM and 9bps qoq expansion in NIMs (Calc.) at 7.1%. However due to lower-than-expected opex and provisions, OP/ PAT came higher at Rs10.6bn/ 5.5bn vs est. of Rs9.9bn/4.6bn. Opex growth was controlled with 3% QoQ increase, and credit cost declined to 1.4% (vs 2.8% in Q2). The company tweaked its ECL model during the quarter, which reduced its provisioning requirement by Rs860mn. As a result overall ECL provisioning declined by 26bps to 3.8%. Overall stressed assets pool (Stage 2 + Stage 3) remains steady at 10% (GS3 ratio declined 30 bps to 4.3%; GS2 ratio increased 24bps to 6%). We have reduced our earnings estimates for FY24/25 by 9%/1% to factor in lower loan growth & NIMs. We maintain our HOLD rating, with an unchanged target price of Rs 260, as we roll over to Mar-26, valuing the company at ~1.5x FY26E BV.

## Q3FY24 Result key highlights

- MMFS Q3FY24 NII was in-line with our expectation at Rs16.9bn (9% YoY) led by 9bps increase in NIMs to 7.1% and of 26% YoY growth in AUM.
- NIMs improved by 9bps QoQ due to an increase in yields by 17bps QoQ to 14.1%. Conversion of the interest free dealer portfolio to retail loans aided yields, on expected lines.
- Disbursements growth was higher in Auto/UV segment (21% YoY), followed by cars (15% YoY). Other segments like CV and used vehicles grew 8-10% YoY. Tractor segment de-grew 18% YoY, however market share in tractor segment maintained.
- With lower-than-expected opex and credit cost, OP/ PAT was ahead of our estimates at Rs 10.6bn/ Rs 5.5bn (vs estimate of Rs 9.8bn/ Rs 4.6bn). Provisions were lower by Rs 860mn on account of the change in ECL model, resulting in improvement in credit cost from 2.8% in Q2 to 1.4%.
- Operating expenses were controlled at Rs 7.5bn (up 3% QoQ, 16% YoY) led by steady employee cost QoQ. Cost/asset ratio remains steady at 2.8%, management confident of improving it to 2.5% by FY25.
- Overall stressed assets pool (Stage 2 + Stage 3) remains steady at 10% (GS3 ratio declined 30 bps to 4.3%; GS2 ratio increased 24bps to 6%). Stage 3 ECL provision cover increased further to 62.7% (up 154bps QoQ).

## Valuation &amp; Recommendation

Though MMFS reported numbers look optically better, the quality of the earnings remains weak. The outperformance during the quarter was led by a few one offs in yield and credit cost. While Management believes it is on track to achieve its earlier guidance of ~30% cagr growth in AUM and 2.5% RoA, we remain skeptical on the same given pressure on growth and margins. We have reduced our earnings estimates for FY24/25 by 9%/1% to factor in lower loan growth & NIMs. At CMP, the stock is trading at 1.6x FY26 BV with RoA/ RoE of 2.2%/15%. We maintain our HOLD rating, with an unchanged target price of Rs 260, as we roll over to Mar-26, valuing the company at ~1.5x FY26E BV.

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Investors are advised to refer disclosures made at the end of the research report.

## Exhibit 1: Quarterly performance

(Rs mn)	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	YoY (%)	QoQ (%)
Net Interest Income	15,528	16,004	15,844	15,870	16,983	9.4	7.0
Other Income	969	1,223	905	870	1,172	21.0	34.7
<b>Net Income</b>	<b>16,496</b>	<b>17,227</b>	<b>16,750</b>	<b>16,740</b>	<b>18,155</b>	<b>10.1</b>	<b>8.4</b>
Total Operating Expenses	6,513	7,786	6,750	7,312	7,530	15.6	3.0
<i>As % Of Net Income</i>	39.5	45.2	40.3	43.7	41.5	199bps	(220bps)
Employee Expenses	3,997	4,552	4,174	4,368	4,342	8.6	-0.6
<i>As % Of Net Income</i>	24.2	26.4	24.9	26.1	23.9	(31bps)	(217bps)
Other Expenses	2,517	3,233	2,577	2,944	3,188	26.7	8.3
<i>As % Of Net Income</i>	15.3	18.8	15.4	17.6	17.6	230bps	(3bps)
<b>Operating Profit</b>	<b>9,983</b>	<b>9,441</b>	<b>10,000</b>	<b>9,428</b>	<b>10,625</b>	<b>6.4</b>	<b>12.7</b>
<i>As % Of Net Income</i>	60.5	54.8	59.7	56.3	58.5	(199bps)	220bps
Provisions	1,551	4	5,264	6,266	3,284	111.7	-47.6
PBT	8,431	9,437	4,735	3,163	7,341	-12.9	132.1
Total Tax	2,142	2,596	1,209	811	1,813	-15.3	123.6
<b>Reported PAT</b>	<b>6,290</b>	<b>6,841</b>	<b>3,527</b>	<b>2,352</b>	<b>5,528</b>	<b>-12.1</b>	<b>135.0</b>
Adjusted PAT	6,290	6,841	3,527	2,352	5,528	-12.1	135.0
Adjusted EPS	5.1	5.5	2.9	1.9	4.5	-12.1	135.0
<b>Yield Analysis (%)</b>	<b>3QFY23</b>	<b>4QFY23</b>	<b>1QFY24</b>	<b>2QFY24</b>	<b>3QFY24</b>	<b>YoY (bps)</b>	<b>QoQ (bps)</b>
Yield on AUM	14.8	14.7	14.3	14.0	14.1	(64bps)	17bps
Cost of funds (AUM)	6.6	6.7	6.8	6.9	7.0	45bps	8bps
NIMs on AUM	8.2	8.0	7.5	7.0	7.1	(110bps)	9bps
<b>Asset quality (Rs mn)</b>	<b>3QFY23</b>	<b>4QFY23</b>	<b>1QFY24</b>	<b>2QFY24</b>	<b>3QFY24</b>	<b>YoY (%)</b>	<b>QoQ (%)</b>
Gross NPAs	45,890	37,170	37,700	40,240	38,520	-16.1	-4.3
Net NPAs	18,820	15,070	15,030	15,620	14,360	-23.7	-8.1
Gross NPAs (%)	5.9	4.5	4.3	4.3	4.0	(196bps)	(32bps)
Net NPAs (%)	2.5	1.9	1.8	1.7	1.5	(100bps)	(19bps)
Provision cover (%)	59.0	59.5	60.1	61.2	62.7	373bps	154bps

Source: Company, Systematix Institutional Research

## Exhibit 2: AUM

(Rs bn)	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	YoY (%)	QoQ (%)	% of total
Auto/ Utility vehicles	255	273	286	309	340	33.1	9.8	35.0
Cars	116	116	113	122	126	8.7	3.5	13.0
Tractors	155	166	182	178	184	19.2	3.5	19.0
Commercial Vehicles	85	91	95	103	107	25.5	3.5	11.0
Refinance & Others	93	99	104	112	126	35.9	12.2	13.0
SME & Others	70	83	87	112	87	25.5	-22.3	9.0
<b>Total</b>	<b>773</b>	<b>828</b>	<b>867</b>	<b>937</b>	<b>970</b>	<b>25.5</b>	<b>3.5</b>	<b>100.0</b>

Source: Company, Systematix Institutional Research

**Exhibit 3: Disbursements**

(Rs bn)	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	YoY (%)	QoQ (%)	% of total
Auto/Utility Vehicles	49.7	42.7	42.7	51.2	60.1	20.8	17.4	38.9
Tractors	20.4	14.3	15.7	12.8	16.8	-17.6	31.0	10.9
Cars	25.9	24.6	23.9	24.6	29.7	15.0	21.1	19.3
Commercial Vehicles and construction equipment	16.0	20.7	13.1	15.1	17.6	10.3	16.5	11.4
Pre-owned vehicles	22.4	25.5	20.7	23.3	24.3	8.5	3.9	15.7
SME and others	10.4	10.1	5.7	6.2	5.9	-43.2	-4.2	3.8
<b>Total</b>	<b>144.7</b>	<b>137.8</b>	<b>121.7</b>	<b>133.2</b>	<b>154.4</b>	<b>6.7</b>	<b>15.9</b>	<b>100.0</b>

Source: Company, Systematix Institutional Research

**Exhibit 4: Source of Borrowing**

(Rs bn)	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	YoY (%)	QoQ (%)	% of total
NCDs	225	240	244	254	244	8.6	-3.8	28.1
Bank Loans	274	304	331	386	431	57.6	11.8	49.7
Offshore Borrowings	14	31	27	27	27	89.3	-1.5	3.1
Fixed Deposits	60	56	55	58	67	12.5	15.7	7.7
CP, ICD, TREPS	58	57	82	78	56	-3.2	-27.4	6.5
Securitisation/Assignment	81	67	56	51	43	-47.5	-17.0	4.9
<b>Total</b>	<b>711</b>	<b>754</b>	<b>795</b>	<b>854</b>	<b>868</b>	<b>22.1</b>	<b>1.6</b>	<b>100.0</b>

Source: Company, Systematix Institutional Research

**Exhibit 5: Mahindra Insurance Brokers Limited**

(Rs mn)	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	YoY (%)	QoQ (%)
Total income	1,230	1,210	1,640	2,890	3,310	169.1	14.5
PBT	180	170	240	380	590	227.8	55.3
PAT	130	130	170	290	430	230.8	48.3

Source: Company, Systematix Institutional Research

**Exhibit 6: Mahindra Rural Housing Finance**

(Rs mn)	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	YoY (%)	QoQ (%)
Loans disbursed	4,440	7,400	2,890	4,820	5,540	24.8	14.9
Outstanding loan book	68,350	68,450	66,260	66,250	66,930	-2.1	1.0
Total income	3,380	3,550	3,420	3,310	3,110	-8.0	-6.0
PAT	140	-260	-230	120	130	-7.1	8.3
GNPA (%)	16.4	10.5	12.0	12.0	11.6	(487bps)	(49bps)
NNPA (%)	11.8	7.8	8.5	8.6	8.4	(341bps)	(16bps)

Source: Company, Systematix Institutional Research

**Exhibit 7: Change in estimates (Introduced FY26 estimates)**

(Rs bn)	Old Estimates			New Estimates			% Change		
	FY24	FY25	FY26	FY24	FY25	FY26	FY24	FY25	FY26
NII	69.1	85.8	-	66.2	77.6	91.0	-4.1	-9.5	-
Operating Profit	43.8	55.7	-	40.8	49.8	62.5	-6.8	-10.7	-
PAT	18.3	24.1	-	17.2	24.5	31.6	-5.8	1.6	-
BV	148	160	-	147	159	175	-0.4	-0.2	-
EPS	15.3	20.0	-	14.0	19.8	25.6	-8.5	-0.7	-

Source: Company, Systematix Institutional Research

## Earnings call highlights

### Business

- Management transition is well on track. Maintained leadership position in tractors, pre-owned vehicles, PVs and 3W segments.
- Business traction – PV segment: inventory levels at dealerships at 2 months. Though volume growth is lower, ticket size is increasing. Most of the new models in PV are witnessing good demand. Used vehicle segment: Seeing more formalization now. It is a highly underpenetrated market, so MMFS have good headroom for growth. CV segment witnessing strong demand led by good Infra & mining activities. Tractor segment: in tough spot and no huge rebound is expected in near future. Though growth in the tractor segment is moderate, MMFS is not losing market share.
- SME – Slowed down large ticket size LAP mainly due to lower yields. Focusing more on business enterprises with turnover below 25 crores.
- New business contribution (SME, Personal and Consumer Loans) contributed ~9% of total AUM (vs ~12% in Q2). Management aim to increase new business contribution to 15% by FY25.
- Cautious on consumer durable loan and stopped disbursements in Dec'23 due to competitive market. Personal loans are extended to only existing customer base and is in initial phase.
- The proportion of NTC is coming down for MMFS as they are focusing more on prime and sub-prime customers.
- Higher contribution from other income on a sustainable basis and improvement in credit cost to drive RoAs.
- Rural Housing Subsidiary – on IPO timeline, management stated that currently they are focusing on bringing down the NPAs before going for value unlocking.

### Margins

- Incremental CoF is ~8%.
- Cost of funds expected to broadly remain at Q3 levels.
- Borrowing mix - 46% are floating; 54% are fixed.

### Asset quality

- In Q3, the company updated the ECL model for its retail vehicle loans by including multi-factor macro-economic variables and product classification of loan portfolio which has resulted in Rs 860mn lower provision towards ECL.
- Improvement in GS3 is led by healthy sourcing of new book.
- Write offs were largely due to refinement of ECL model.
- PCR is expected to normalize by Q3FY25.
- GNPA as per RBI – 5.5% vs 4% in Q2.

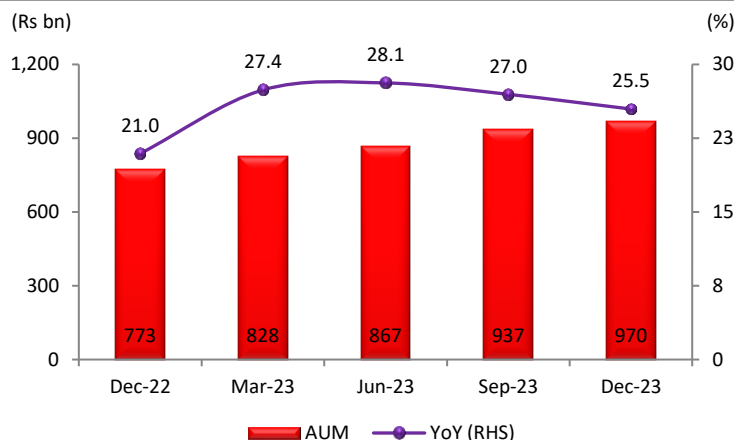
### OPEX

- Investments in technology, data, people and processes will continue.
- Aim to add 150-200 branches over next 1-1.5 years.

## Guidance

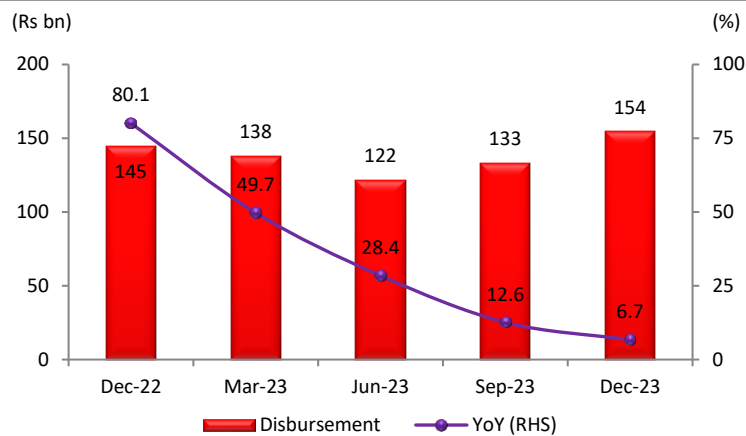
- Long term NIMs guidance lowered to 7% from 7.5% earlier.
- Opex to asset and credit cost guidance maintained at 2.5% and 1.5-1.7%
- RoA guidance maintained at 2.5% for FY25.

**Exhibit 8: AUM growth moderated a bit**



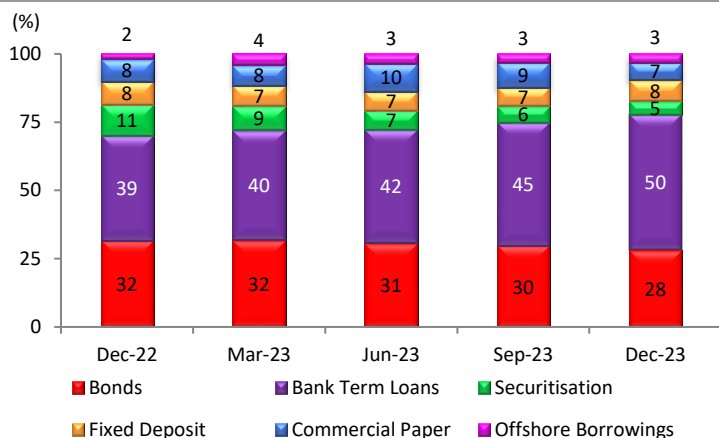
Source: Company, Systematic Institutional Research

**Exhibit 9: Disbursement growth remained slower**



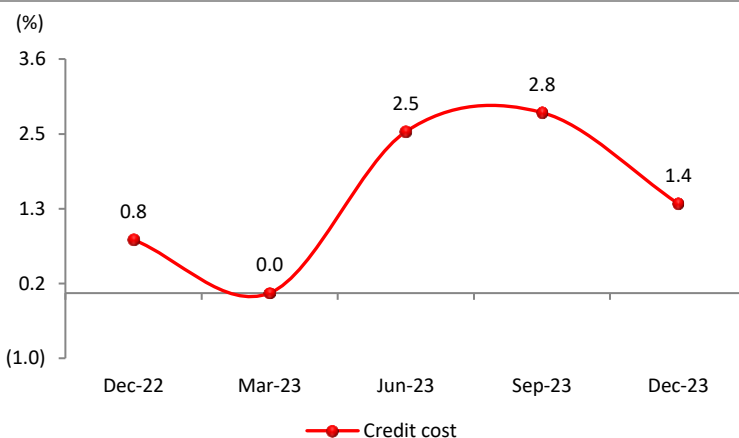
Source: Company, Systematic Institutional Research

**Exhibit 10: Diversified borrowing mix**



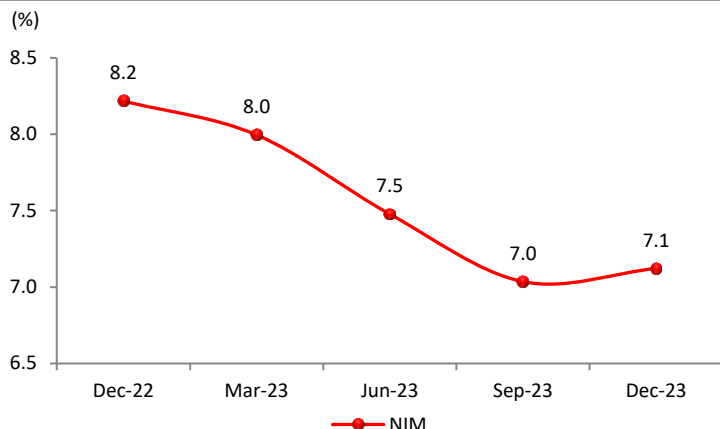
Source: Company, Systematic Institutional Research

**Exhibit 11: Credit cost declined partly led by updated ECL model**



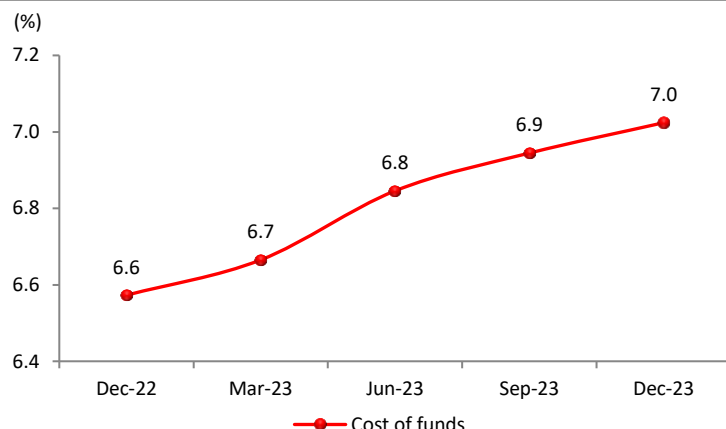
Source: Company, Systematic Institutional Research

**Exhibit 12: NIMs on AUM improved by ~10bps QoQ**



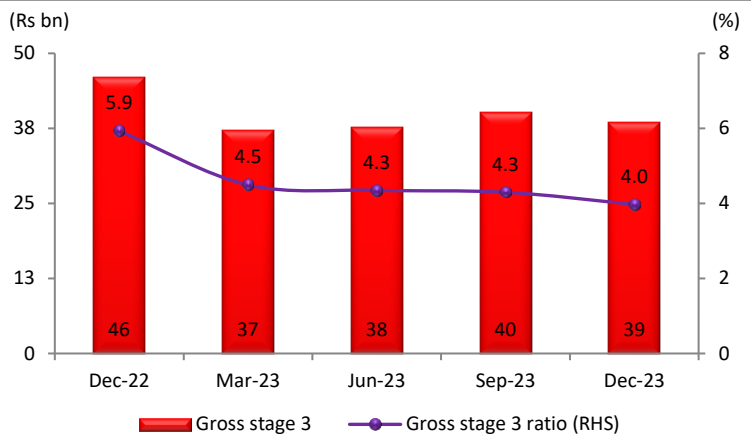
Source: Company, Systematic Institutional Research

**Exhibit 13: Cost of funds inched up by 8bps QoQ**



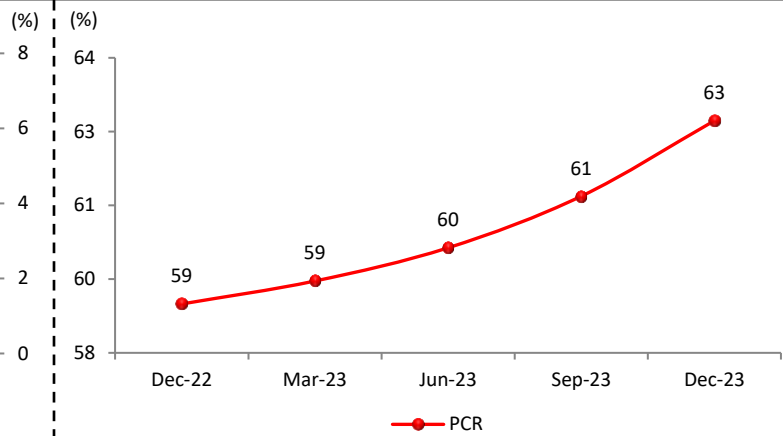
Source: Company, Systematic Institutional Research

Exhibit 14: ~30bps QoQ improvement in GS3 asset ratio



Source: Company, Systematix Institutional Research

Exhibit 15: Stage 3 provision cover continued to remain healthy



Source: Company, Systematix Institutional Research

## FINANCIALS

### Profit & Loss Statement

YE: Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net interest income	55,554	61,059	66,222	77,642	91,042
Other income	608	1,273	1,434	1,731	3,934
Net Income	57,986	64,794	70,563	82,764	98,915
Operating expenses	20,734	27,276	29,727	32,963	36,379
Preprovision profit	37,252	37,518	40,836	49,801	62,536
Provisions	23,683	9,992	17,442	16,623	19,668
Profit before tax	13,569	26,981	23,394	33,179	42,868
Tax	3,682	7,138	6,153	8,726	11,274
Tax rate	27.1	26.5	26.3	26.3	26.3
Reported Profit after tax	9,888	19,843	17,241	24,453	31,594

Source: Company, Systematix Institutional Research

### Balance Sheet

YE: Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Equity	2,466	2,467	2,467	2,467	2,467
Reserves	153,815	168,422	178,947	193,875	213,163
Net worth	156,281	170,889	181,415	196,342	215,630
Borrowings	558,139	749,459	924,898	1,121,356	1,320,630
Others	38,467	41,818	37,109	32,363	44,444
Total liabilities	752,887	962,166	1,143,422	1,350,061	1,580,704
Cash	41,507	28,321	25,209	30,200	35,359
Investments	84,403	99,886	100,834	96,640	113,150
Loans	604,446	794,547	969,987	1,166,445	1,365,719
Others	18,603	32,456	38,317	45,904	53,746
Total assets	752,887	962,166	1,143,422	1,350,061	1,580,704

Source: Company, Systematix Institutional Research

### Dupont (as % of Average Assets)

YE: Mar	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	12.4	12.5	12.4	12.7	12.8
Interest Expense	5.1	5.3	6.1	6.5	6.6
Net Interest Income	7.3	7.1	6.3	6.2	6.2
Other income total	0.3	0.4	0.4	0.4	0.5
Net Income total	7.6	7.6	6.7	6.6	6.8
Operating expenses total	2.7	3.2	2.8	2.6	2.5
Preprovision profit	4.9	4.4	3.9	4.0	4.3
Provisions	3.1	1.2	1.7	1.3	1.3
Profit before tax and exce. items	1.8	3.2	2.2	2.7	2.9
Profit before tax	1.8	3.1	2.2	2.7	2.9
Tax total	0.5	0.8	0.6	0.7	0.8
Profit after tax	1.3	2.3	1.6	2.0	2.2

Source: Company, Systematix Institutional Research

### Key Ratios

YE: Mar	FY22	FY23	FY24E	FY25E	FY26E
Yield on portfolio	14.6	14.5	14.2	14.3	14.3
cost of borrowings	6.9	7.0	7.7	7.9	7.9
Spread	7.8	7.5	6.5	6.4	6.4
NIM (on AUM)	8.6	8.3	7.2	7.0	6.9
Cost/ Income (%)	35.8	42.1	42.1	39.8	36.8
Credit cost (%)	3.1	1.2	1.7	1.3	1.3
RoA(%)	1.3	2.4	1.6	2.0	2.2
RoE(%)	6.5	12.5	9.8	12.9	15.3
Leverage (x)	5.0	5.2	6.0	6.6	7.1
Tier I (%)	24.2	19.9	17.9	16.5	15.6
CAR (%)	27.8	22.5	20.1	18.4	17.2
Gross NPA (%)	7.7	4.5	4.0	4.3	4.3
Net NPA (%)	3.4	1.9	1.6	2.2	2.2
Provision coverage (%)	58.1	59.5	61.2	50.0	50.0

Source: Company, Systematix Institutional Research

### Growth

YE: Mar (%)	FY22	FY23	FY24E	FY25E	FY26E
Net interest income	0.4	9.9	8.5	17.2	17.3
Net Income total	0.3	11.7	8.9	17.3	19.5
Preprovision profit	-10.3	0.7	8.8	22.0	25.6
Profit before tax	221.2	98.8	-13.3	41.8	29.2
Profit after tax	195.0	100.7	-13.1	41.8	29.2
Loan	0.8	31.5	22.1	20.3	17.1
Disbursement	45.2	79.6	20.0	15.0	15.0
AUM	0.5	27.4	21.8	19.8	17.1

Source: Company, Systematix Institutional Research

### Valuation ratios

YE: Mar	FY22	FY23	FY24E	FY25E	FY26E
FDEPS (Rs)	8	17	14	20	26
PER (x)	35	17	20	14	11
Book value (Rs)	127	139	147	159	175
P/BV (Rs)	2.2	2.0	1.9	1.8	1.6
Adj. book value (Rs)	110	126	134	138	150
P/ABV (Rs)	2.5	2.2	2.1	2.0	1.9
P/PPP (x)	9.2	9.2	8.4	6.9	5.5
Dividend yield (%)	1.1	2.2	2.0	2.8	3.6

Source: Company, Systematix Institutional Research



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