

Muthoot Finance

17 February 2020

Reuters: MUTT.BO; Bloomberg: MUTH IN

Growth intact, NII/PAT aided by exceptionally high collections

Muthoot Finance (MFL) reported its 3QFY20 results with the key takeaways being: (1) Gold loan growth was robust (2) Funding situation has eased (3) Exceptional collections helped push up yield/NIM (4) Asset quality improved but home loans under stress (See *detailed conference call takeaways on page 2 for significant incremental colour*). Per se, on the key P&L items, MFL posted NII growth of 45% YoY at Rs15,869mn, PPOP growth of 46% YoY at Rs11,443mn and PAT growth of 66% YoY at Rs8,034mn. We have revised our estimates for FY20/FY21/FY22 and retained Buy rating on MFL, revising our target price to Rs909 (from Rs879 earlier) and valuing the stock at 2.1x H1FY22E P/BV.

Gold loan growth was robust: Gold loan AUM stood at Rs377bn, up 19% YoY/8% QoQ. The growth was led by a combination of increase in prices and gold holdings. For the quarter, gold holding was 173 tonnes, up 4.2% YoY/1.2% QoQ. YTD, the gold AUM is up 12% compared to 10% in FY19. Given the strong growth in Q3FY20, the company seems to have more than made up for the momentum lost in Q2FY20 when the gold book growth was 9% YoY. Traction so far during Q4FY20 has been good as well. The company is likely to deliver better than its guidance of 15% AUM growth in FY20. For FY21, the management has reiterated AUM growth of more than 15%. The home loan portfolio stood at Rs20bn, up 10% YoY but down 3.5% QoQ. The company is targeting a home loan portfolio of Rs22bn by Q4FY20-end, which implies a growth of 15.3% over FY19. Disbursements in home loan portfolio were Rs1bn, down 31.6% YoY/5.3% QoQ. The reason for drop in disbursements is on account of cautious lending since the market sentiment in the company's target market has deteriorated (also reflected in increased NPAs). Belstar Microfinance has reported an AUM of Rs22.8bn, up 46% YoY.

Funding situation has eased: The company raised funds through its offshore bond issuance program (Rs 32bn) and public issue of NCDs. Banks have also become more willing to lend than before, which augurs well for the company in terms of funding growth going forward. As part of its overall balance sheet management strategy, the company has increased the level of on-balance sheet liquidity as indicated by higher levels of cash/equivalents. As opposed to keeping un-utilized bank lines earlier (before NBFC crisis), the company would now be fully drawing down the bank lines. This would also help address the new LCR requirements. During the quarter, funding through listed/secured NCDs was up 42% YoY/20% QoQ to Rs103.9bn. Funding from banks/FIs was up 6% YoY (down 4% QoQ) to Rs129bn. CPs were up 15% YoY (down 6% QoQ) to Rs46.1bn. Total borrowings were up 29% YoY/14% QoQ.

Exceptional collections helped push up yield/NIM: Interest income for the quarter was Rs22.8bn, up 36% YoY/8% QoQ compared to interest expense of Rs6.9bn, up 18% YoY/4% QoQ. NII was Rs15.9bn, up 45% YoY/11% QoQ. Loan yields (reported) were 24.58%, up 380bps YoY/103bps QoQ, driven by non-recurring penal interest collections. In Q2FY20, the company had seen about Rs2bn worth of exceptional income which helped push up yields/NIMs. (Continued on Page 2)

Valuation and outlook: We have revised our NII estimates by 7.7%/8.2%/9.4%, PPOP estimates by 7.7%/8.6%/10.2% and PAT estimates by 5.5%/7.4%/9.7% for FY20/FY21/FY22, respectively, valuing the stock at 2.1x H1FY22E P/BV and revising our target price to Rs909 (from Rs879 earlier).

BUY

Sector: NBFC

CMP: Rs747

Target Price: Rs909

Upside: 22%

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Key Data

Current Shares O/S (mn)	401.0
Mkt Cap (Rsbn/US\$bn)	299.6/4.2
52 Wk H / L (Rs)	800/507
Daily Vol. (3M NSE Avg.)	1,151,425

Price Performance (%)

	1 M	6 M	1 Yr
Muthoot Finance	(2.3)	21.7	41.7
Nifty Index	(2.0)	9.8	12.7

Source: Bloomberg

Y/E Mar (Rsmn)	Q3FY20	Q3FY19	Q2FY20	YoY (%)	QoQ (%)
Interest Income	22,806	16,827	21,057	35.5	8.3
Interest Expenses	6,938	5,889	6,699	17.8	3.6
Net Interest Income	15,869	10,938	14,358	45.1	10.5
NIM (%)	17.10	13.51	16.05	359 bps	105 bps
Fee & Other income	325	344	348	-5.4	-6.6
Total Income	16,194	11,282	14,707	43.5	10.1
Staff Cost	2,580	1,980	2,327	30.3	10.9
Other Op Exp	2,171	1,460	1,642	48.8	32.2
Total Operating Expenses	4,751	3,440	3,969	38.1	19.7
Cost to Income (%)	29.3	30.5	27.0	-115 bps	235 bps
Cost to AUM (%)	4.94	4.24	4.44	70 bps	49 bps
Pre-Provisioning Operating Profit	11,443	7,842	10,738	45.9	6.6
Provisions	640	19	265	3,255.9	141.9
Credit Cost (%)	0.68	0.02	0.29	66 bps	39 bps
PBT	10,803	7,823	10,473	38.1	3.1
Tax	2,769	2,971	1,894	-6.8	46.2
-effective tax rate	25.6	38.0	18.1	-1234 bps	755 bps
PAT	8,034	4,852	8,579	65.6	-6.4
Other Comprehensive Income	(49)	(8)	(39)	523.3	25.2
Total Comprehensive Income	7,985	4,845	8,540	64.8	-6.5
EPS (Rs)	20.0	12.1	21.4	65.4	-6.4
BV (Rs)	284.3	231.6	264.5	22.7	7.5
AUM	384,982	324,704	357,305	18.6	7.7

Source: Company, Nirmal Bang Institutional Equities Research

Continued from Page 1

Exceptional collections helped push up yield/NIM: For Q3FY20, though the management has not quantified the amount of penal interest collection, our sense is that normalized loan yields would be ~21%. Cost of funds for the quarter was 8.98%, easing 32bps QoQ/YoY. As per the management, CoF could range between 9.2-9.5% going forward. The ECBs raised at 6.125% are now trading at 4.38%; including hedging cost, cost of foreign borrowings could come down to single digits compared to double digits earlier.

Asset quality improved but home loans under stress: Gross stage 3 assets stood at 2.54%, compared to 3.43% in Q2FY20. Average monthly collections for the quarter were robust at Rs82bn compared to a run-rate of Rs60-70bn in H1FY20. Given that the average LTV is 70%, we do not fret too much with respect to asset quality. Write-offs during the quarter were Rs330mn on account of burglaries. GNPA in the home loan segment have seen material deterioration; have increased from 1.10% in Q2FY20 to 1.87% in Q3FY20. The company has stated that it has seen some deterioration/increased levels of stress in the market it is operating in and that current levels should be taken as normalized for now.

Comprehensive Conference Call Takeaways

Asset Quality

- Credit costs were elevated due to incremental provisions on new (standard) loans and write-offs (Rs330mn). The write-offs were on account of burglary in 2 branches where the company has made additional provisions worth Rs140mn. The company has filed an insurance claims against these burglaries.
- Company has increased PCR on its vehicle finance and home finance portfolio as it perceives stress to have gone up, given the market it operates in for these products.
- The current GNPA in the home loan portfolio may indicate normalized levels for now.

Business and Loan Growth

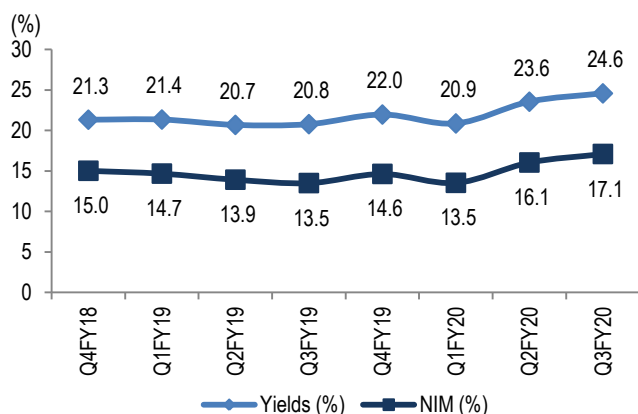
- Credit growth guidance stands at >15% for FY20. For FY21, company has guided for minimum 15% growth.
- Company is piloting the doorstep loan delivery model which is also being used by some fintech companies. This will be scaled up in a few quarters.
- FY20 target for housing book AUM stands at Rs22bn. Company expects to disburse ~7-8bn in FY21 and bring RoA to 2%.
- Home loans are sold through branches and sales executives (feet on street). 10% of monthly home loan disbursements are done through gold loan branches.
- There are no plans for inorganic growth as of now.
- Kerala loan book stands at Rs 12bn (3% of overall portfolio).
- Average LTV on the book is 70%.

Margin, Liabilities and Liquidity

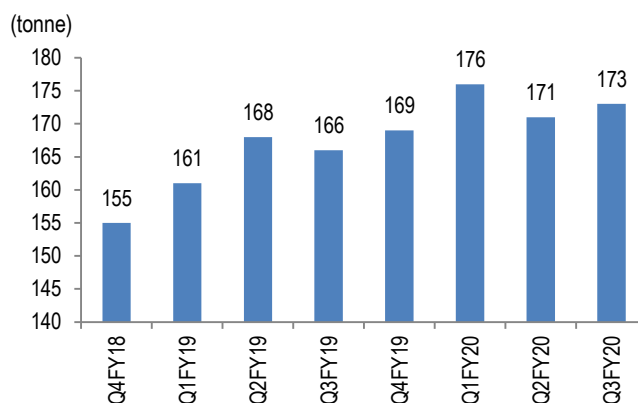
- The company raised funds through its offshore bond issuance program (Rs 32bn) and public issue of NCDs. Besides, the banks are also more willing to lend than before.
- ECBs raised by company at 6.125% are now trading at 4.38%.
- Company is drawing all its bank limits and keeping higher cash on balance sheet. This would be the trend going forward, which would help in complying with LCR requirements as well as maintaining balance sheet liquidity.
- Yields were higher during the quarter due to collection of penal interest and increase in rates done last year (June 2019).
- Average cost of funds stands at 9.2-9.3%. Going forward, it would range between 9.2-9.5%.

Operating Expenses

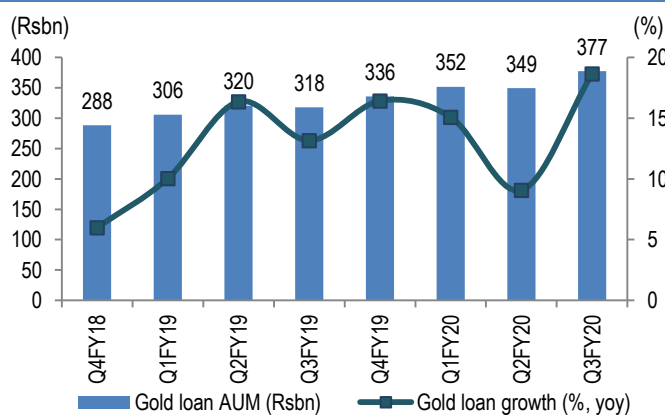
- Increase in other expenses was on account of higher rentals and expenses related to ECB hedging (Rs 0.21bn).
- Company is rationalizing its branch count and is trying to increase Business per branch. Also, it would be opening 100-200 branches per year and expanding into new geographies.
- Company expects ad expenses to increase with growth in loan book.

Exhibit 1: Yields, NIMs (%)


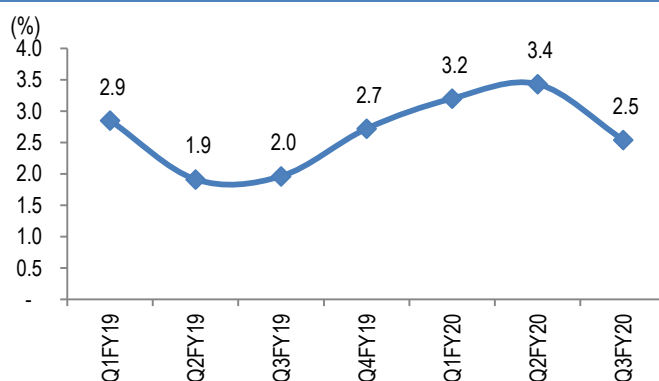
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Gold holdings (tonnage)


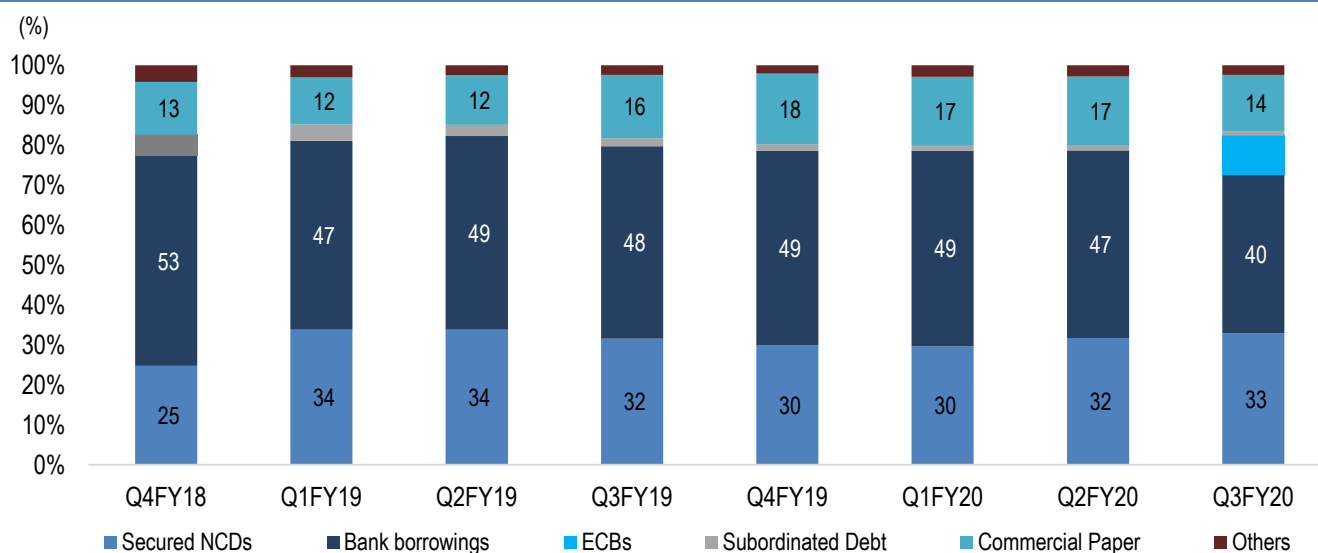
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Gold AUM (Rsbn)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Gross stage 3 assets (%)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Borrowings mix (%)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Financial summary

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Net interest income	42,707	45,202	55,606	63,732	76,666
Pre-provisioning operating profit	30,843	31,044	39,478	45,716	56,553
PAT	17,776	19,721	28,418	33,493	41,591
EPS (Rs)	44.4	49.2	70.9	83.6	103.8
BV (Rs)	195.3	244.4	308.1	384.5	481.1
P/E (x)	16.8	15.2	10.5	8.9	7.2
P/BV (x)	3.8	3.1	2.4	1.9	1.6
Gross NPAs (%)	4.4	2.7	2.6	2.5	2.4
Net NPAs (%)	3.7	2.3	2.2	2.1	2.0
RoA (%)	5.8	5.7	6.7	6.5	6.8
RoE (%)	24.8	22.4	25.7	24.1	24.0

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Actual performance versus our estimates

(Rsmn)	Q3FY20	Q3FY19	Q2FY20	YoY (%)	QoQ (%)	Q3FY20E	Devi. (%)
Net interest income	15,869	10,938	14,358	45.1	10.5	12,506	26.9
Pre-provisioning operating profit	11,443	7,842	10,738	45.9	6.6	8,743	30.9
PAT	8,034	4,852	8,579	65.6	(6.4)	6,651	20.8

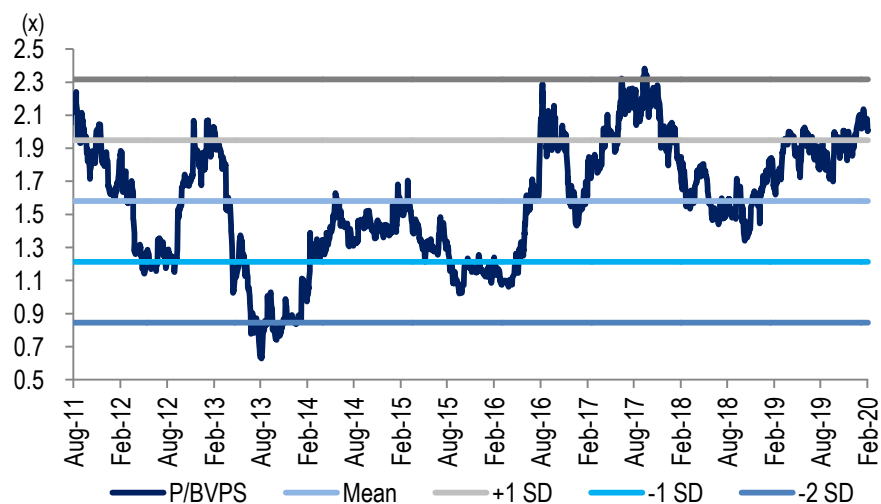
Source: Company, Nirmal Bang Institutional Equities Research.

Exhibit 8: Change in our estimates

	Revised Estimate			Earlier Estimate			% Revision		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Net Interest Income (Rs mn)	55,606	63,732	76,666	51,615	58,925	70,077	7.7	8.2	9.4
Net Interest Margin (%)	14.6	14.2	14.4	13.7	13.5	13.5	86 bps	73 bps	89 bps
Operating Profit (Rs mn)	39,478	45,716	56,553	36,648	42,110	51,300	7.7	8.6	10.2
Profit after tax (Rs mn)	28,418	33,493	41,591	26,924	31,185	37,909	5.5	7.4	9.7

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 10: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Interest income	62,021	67,570	83,255	96,842	114,764
Interest expenses	19,314	22,368	27,649	33,110	38,098
Net interest income	42,707	45,202	55,606	63,732	76,666
Non-interest income	1,310	1,236	1,319	1,459	1,736
Net revenues	44,017	46,438	56,925	65,191	78,402
Operating expenses	13,174	15,394	17,447	19,475	21,849
-Employee expenses	7,824	8,976	9,873	11,144	12,684
-Other expenses	5,350	6,419	7,574	8,331	9,165
Pre-provisioning operating profit	30,843	31,044	39,478	45,716	56,553
Provisions	2,397	275	1,588	1,059	1,099
PBT	28,447	30,768	37,890	44,657	55,454
Tax	10,671	11,047	9,473	11,164	13,864
PAT	17,776	19,721	28,418	33,493	41,591

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY21E
Share capital	4,000	4,007	4,007	4,007	4,007
Reserves & surplus	74,120	93,921	119,448	150,050	188,750
Net worth	78,120	97,927	123,454	154,056	192,756
Borrowings	211,670	268,332	332,731	379,313	440,004
Other liability & provisions	18,132	14,428	15,540	24,086	24,809
Total liabilities	307,923	380,687	471,725	557,456	657,569
Fixed assets	2,062	2,154	2,369	2,606	2,867
Investments	3,954	9,826	29,942	32,936	36,229
Loans	295,068	349,329	412,209	486,406	578,823
Cash	4,870	17,355	23,908	24,320	26,047
Other assets	1,968	2,023	3,298	11,187	13,602
Total assets	307,923	380,687	471,725	557,456	657,569

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Key ratios

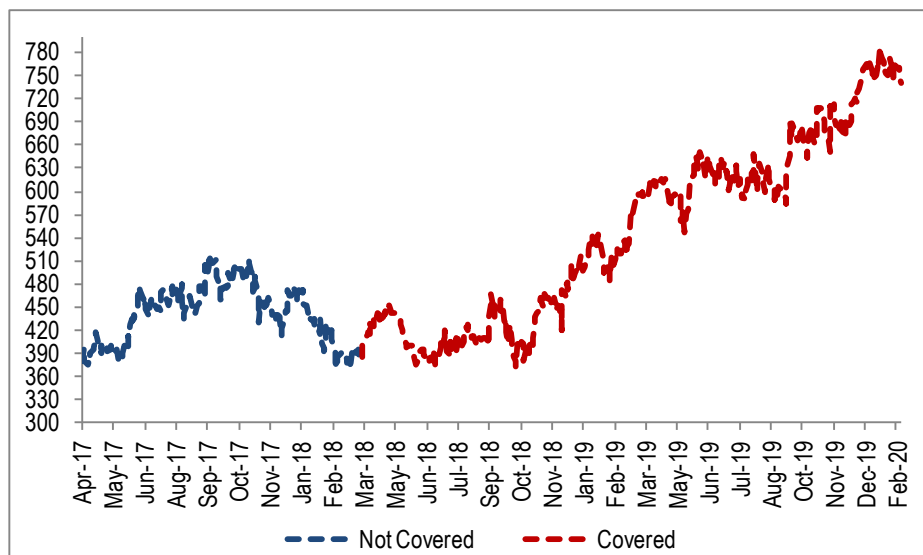
Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Growth (%)					
Net interest income	22.5	5.8	23.0	14.6	20.3
Operating profit	36.1	0.6	27.2	15.8	23.7
Profit after tax	45.8	10.9	44.1	17.9	24.2
Business (%)					
Advances growth	5.5	18.4	18.0	18.0	19.0
Spread (%)					
Yield on loans	21.6	21.0	21.9	21.6	21.5
Cost of borrowing	9.2	9.3	9.2	9.3	9.3
Spread	12.4	11.7	12.7	12.3	12.2
NIM	14.9	14.0	14.6	14.2	14.4
Operational efficiency (%)					
Cost-to-income	29.9	33.2	30.6	29.9	27.9
Cost-to-assets	4.6	4.8	4.6	4.3	4.1
CRAR (%)					
Tier I	25.5	25.6	26.0	26.3	26.3
Tier II	0.8	0.4	0.4	0.4	0.4
Total	26.3	26.1	26.4	26.7	26.7
Asset quality (%)					
Gross NPA / Stage 3	4.4	2.7	2.6	2.5	2.4
Net NPA / Net Stage 3	3.7	2.3	2.2	2.1	2.0
Specific PCR / Stage 3 PCR	14.8	13.9	15.0	17.0	17.0
Credit Costs / Asset Provisions	0.9	0.4	0.4	0.2	0.2
Return ratios (%)					
RoE	24.8	22.4	25.7	24.1	24.0
RoA	5.8	5.7	6.7	6.5	6.8
Per share (%)					
EPS	44.4	49.2	70.9	83.6	103.8
BV	195.3	244.4	308.1	384.5	481.1
ABV	167.9	224.4	285.4	359.3	452.3
Valuation (x)					
P/E	16.8	15.2	10.5	8.9	7.2
P/BV	3.8	3.1	2.4	1.9	1.6
P/ABV	4.4	3.3	2.6	2.1	1.7

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 March 2018	Buy	381	471
18 May 2018	Buy	441	485
6 September 2018	Buy	437	514
9 October 2018	Buy	380	501
10 December 2018	Buy	471	547
7 February 2019	Buy	485	558
8 April 2019	Acc	617	653
14 May 2019	Buy	547	670
8 July 2019	Buy	626	721
13 August 2019	Buy	600	720
23 September 2019	Buy	631	858
7 October 2019	Buy	665	874
14 November 2019	Buy	650	877
8 January 2020	Buy	746	879
17 February 2020	Buy	747	909

Rating track graph



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Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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