

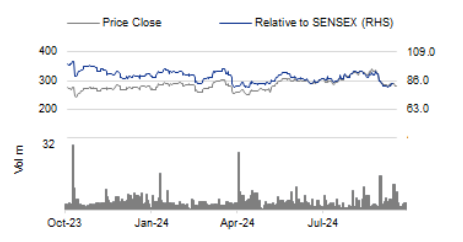
India

ADD (no change)

Consensus ratings*: Buy 16 Hold 13 Sell 8	
Current price:	Rs282
Target price:	Rs330
Previous target:	Rs370
Up/downside:	17.0%
InCred Research / Consensus:	6.1%
Reuters:	MMFS.BO
Bloomberg:	MMFS IN
Market cap:	US\$4,139m
	Rs347,987m
Average daily turnover:	US\$14.2m
	Rs1190.8m
Current shares o/s:	1,232.3m
Free float:	46.4%
*Source: Bloomberg	

Key changes in this note

- Cyclicity in vehicle sales is hurting the growth momentum for MMFS in the absence of implementation of successful product diversity like in Chola & Shriram Finance.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(15.2)	(4.8)	3.2
Relative (%)	(10.2)	(4.6)	(16.9)

Major shareholders	% held
Mahindra & Mahindra	52.0
LIC	6.3
HDFC Life	2.6

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Mahindra & Mahindra Finance

Cyclicity impacting growth & asset quality

- MMFS reported a lower-than-expected 2Q PAT of Rs3.7bn amid a spurt in provisioning as delayed monsoons hit repayment capability of rural borrowers.
- In the absence of AUM diversity (88% vehicle AUM), the cyclicity of slowdown in vehicle demand & volatility in rural stress elevated the impact on earnings.
- Weak momentum in disbursements to stay in the near term, although the asset quality trend may improve in 2HFY25F. Retain ADD with a lower TP of Rs330.

Weak momentum in vehicle sales impacts overall disbursements

Mahindra & Mahindra Financial Services or MMFS reported weak disbursements at Rs131bn in 2QFY25, down 1% yoy, reflecting the slowdown in rural demand amid delayed monsoons as well as a cautious approach of its management. AUM growth remained healthy at Rs1,124.5bn (+20% yoy/+5.8% qoq) as of Sep 2024-end amid lower repayments. However, drying disbursements will gradually catch up on AUM growth as well. MMFS managed flat margin qoq at 6.5% amid a gradual rise in yields as well as improved fee-based income. Vehicle sales in India is witnessing a cyclicity which, in turn, is impacting the growth momentum for MMFS in the absence of implementation of successful product diversity like Cholamandalam Finance & Shriram Finance. We have cut our disbursement & AUM growth estimates for FY25F/26F as the recovery in vehicle demand may take some time. We are building in ~9% CAGR in disbursements, leading to ~14% CAGR in assets under management or AUM over FY25F-27F.

'Collections delayed but there's no default' amid delayed monsoons

MMFS has witnessed a volatile trend in asset quality during 2QFY25, mainly in agri-based states like Maharashtra, Gujarat, Rajasthan, Madhya Pradesh, etc. as delayed monsoons, along with stretched liquidity positioning, impacted the loan repayment capacity of rural borrowers, but management remains confident of improved recoveries in 2HFY25F. Though the management attributed loan defaults arising primarily from the tractor portfolio (~40% of slippage), the weakness is visible across asset classes.

Perception issue to stay amid inability to manage sustainable RoA

MMFS has a perception issue amid its long-term track record of delivering a volatile performance, despite superior corporate parentage as well as strong brand recognition. With ~88% of its portfolio still linked to vehicle sales, MMFS has been slow in achieving product diversity unlike Cholamandalam Finance & Shriram Finance which, in turn, is impacting on its growth possibility. Also, with an elevated rural presence and monoline product line (vehicle financing), MMFS is unable to address volatility in the asset cycle, despite an improvement in the underwriting process. We believe the inability of MMFS to achieve a sustainable RoA of ~2% will weigh over its valuation. We cut our earnings estimates for FY25F/26F by 15.5%/12.6%, respectively, to arrive at a lower target price of Rs330 (Rs370 earlier). We value the standalone MMFS at ~1.9x FY26F BV and add Rs20/share for its arms. We retain ADD rating but have removed MMFS from our high-conviction stocks list. Downside risks: Slowing growth and a deterioration in asset quality.

Financial Summary

	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Net Interest Income (Rsm)	63,521	69,772	79,688	93,525	106,757
Total Non-Interest Income (Rsm)	1,268	1,583	1,792	2,030	2,288
Operating Revenue (Rsm)	64,789	71,355	81,479	95,555	109,045
Total Provision Charges (Rsm)	(9,988)	(18,228)	(22,205)	(25,481)	(25,910)
Net Profit (Rsm)	19,845	17,596	19,507	24,647	30,871
Core EPS (Rs)	16.07	14.25	15.80	19.97	25.01
Core EPS Growth	100%	(11%)	11%	26%	25%
FD Core P/E (x)	17.53	19.76	17.82	14.11	11.26
DPS (Rs)	6.00	6.30	8.00	10.00	12.00
Dividend Yield	2.13%	2.24%	2.84%	3.55%	4.26%
BVPS (Rs)	138.4	147.1	154.9	164.9	177.9
P/BV (x)	2.04	1.91	1.82	1.71	1.58
ROE	12.1%	10.0%	10.5%	12.5%	14.6%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 1: Quarterly earnings summary

Rs m	1QFY24	2QFY24	3QFY24	4QFY24	1QFY25	2QFY25	% yoy	% qoq
Operating Income	30,846	32,119	34,536	36,540	37,222	38,975	21.3%	4.7%
Interest Expenses	14,505	15,665	16,750	17,351	18,286	19,343	23.5%	5.8%
Net Operating Income	16,341	16,455	17,787	19,190	18,936	19,632	19.3%	3.7%
Other Income	409	286	368	521	379	276	-3.4%	-27.3%
Total Income	16,750	16,740	18,155	19,710	19,316	19,908	18.9%	3.1%
Operating Expenses	6,750	7,312	7,530	7,980	7,970	7,947	8.7%	-0.3%
Operating Profit	10,000	9,428	10,625	11,730	11,345	11,961	26.9%	5.4%
Provisions	5,264	6,266	3,284	3,415	4,482	7,035	12.3%	57.0%
CoR%	2.5%	2.8%	1.4%	1.4%	1.7%	2.6%	-7.4%	49.9%
PBT	4,735	3,163	7,341	8,315	6,864	4,927	55.8%	-28.2%
Tax	1,209	811	1,813	2,126	1,734	1,232	51.9%	-29.0%
Tax rate (%)	25.5%	25.6%	24.7%	25.6%	25.3%	25.0%	-2.5%	-1.0%
Reported PAT	3,527	2,352	5,528	6,190	5,130	3,695	57.1%	-28.0%
AUM	8,67,320	9,37,230	9,70,480	10,25,970	10,63,390	11,24,540	20.0%	5.8%
Disbursements	1,21,650	1,33,150	1,54,360	1,52,940	1,27,410	1,31,620	-1.1%	3.3%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Our revised earnings estimates

Y/E Mar (Rs m)	FY25F			FY26F			FY27F		
	Earlier	Revised	% change	Earlier	Revised	% change	Earlier	Revised	% change
Net Interest Income	83,216	79,688	-4.2%	98,912	93,525	-5.4%	1,13,138	1,06,757	-5.6%
PPOP	51,239	48,388	-5.6%	62,778	58,564	-6.7%	72,406	67,348	-7.0%
PAT	23,096	19,507	-15.5%	28,199	24,647	-12.6%	33,895	30,871	-8.9%
EPS (Rs)	18.7	15.8	-15.5%	22.8	20.0	-12.6%	27	25.0	-8.9%
AUM (Rs)	12,22,628	11,94,524	-2.3%	14,01,328	13,53,551	-3.4%	15,88,678	15,25,388	-4.0%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

2QFY25 earnings-call highlights

Guidance

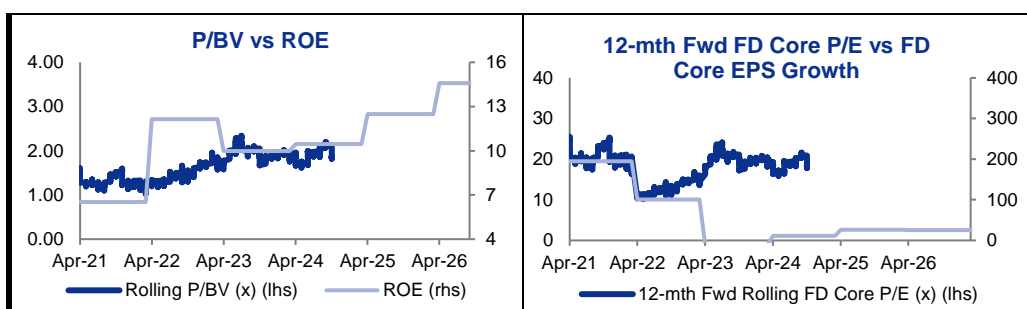
- The loan growth guidance for the next three years is around 15-20% CAGR.
- Credit cost to be in the range of 1.3-1.5% for FY25.
- RoA for FY25F is expected to be ~1.8-2%.

Conference-call highlights

- Tractor segments contributed ~40% to incremental stage-3 assets for the quarter. States which are highly agri-dependent like Maharashtra, Gujarat, Madhya Pradesh, Telangana and Andhra Pradesh have seen some delay in repayments due to the cash crunch. Management believes the cash crunch has led to defaults, which is not an area of concern as a recovery is expected in the second half of the financial year.
- Sales volume in the first half of Oct 2024, overall good monsoon season, minimum support prices or MSPs for crops & the overall yield remaining positive are healthy signs which are indicating to the management about demand recovery in the second half, but delayed monsoons may still have a negative impact on demand.
- Conservative full-year growth, and the first half of the festive season was decent. There are green shoots like M&M's sales in the passenger vehicle segment not very high but likely to witness moderate growth this year.
- Passenger vehicles have reasonable new to credit customers where the company sees good participation.
- The second half will be positive to cover for the first half.
- This year cannot be compared to last year due to higher financial stress.
- Gross non-performing assets or GNPA's stood at Rs60bn and stage-3 assets at Rs43bn.
- Slippage is expected to be recovered in the second half, and therefore the credit costs will be lower.
- The segment-wise market share in commercial vehicles, passenger vehicles and tractors will be maintained, but management is not bullish at gaining market share.

- Due to dividend payment and advances, the base growth led to a drop in the capital adequacy ratio.
- Management expects 15-20% incremental sourcing from new partnerships in the super prime and prime segments of the company.

BY THE NUMBERS



Profit & Loss

(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Net Interest Income	63,521	69,772	79,688	93,525	106,757
Total Non-Interest Income	1,268	1,583	1,792	2,030	2,288
Operating Revenue	64,789	71,355	81,479	95,555	109,045
Total Non-Interest Expenses	(25,404)	(27,285)	(30,392)	(33,860)	(38,129)
Pre-provision Operating Profit	37,511	41,783	48,388	58,564	67,348
Total Provision Charges	(9,988)	(18,228)	(22,205)	(25,481)	(25,910)
Operating Profit After Provisions	27,524	23,555	26,183	33,084	41,437
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	27,524	23,555	26,183	33,084	41,437
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	36,284	32,615	35,968	43,749	53,169
Exceptional Items					
Pre-tax Profit	27,524	23,555	26,183	33,084	41,437
Taxation	(7,134)	(5,959)	(6,677)	(8,436)	(10,567)
Consolidation Adjustments & Others					
Exceptional Income - post-tax	(545)				
Profit After Tax	19,845	17,596	19,507	24,647	30,871
Minority Interests					
Prof. & Special Div					
FX And Other Adj.					
Net Profit	19,845	17,596	19,507	24,647	30,871
Recurring Net Profit					

Balance Sheet Employment

(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Gross Loans/Cust Deposits					
Avg Loans/Avg Deposits					
Avg Liquid Assets/Avg Assets	84.9%	85.1%	86.5%	87.1%	87.8%
Avg Liquid Assets/Avg IEAs	104.9%	103.0%	103.6%	105.9%	110.1%
Net Cust Loans/Assets					
Net Cust Loans/Broad Deposits					
Equity & Provns/Gross Cust Loans					
Asset Risk Weighting					
Provision Charge/Avg Cust Loans					
Provision Charge/Avg Assets					
Total Write Offs/Average Assets					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Total Gross Loans	810,443	1,000,020	1,143,986	1,295,581	1,459,373
Liquid Assets & Invst. (Current)					
Other Int. Earning Assets					
Total Gross Int. Earning Assets	810,443	1,000,020	1,143,986	1,295,581	1,459,373
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets	810,443	1,000,020	1,143,986	1,295,581	1,459,373
Intangible Assets					
Other Non-Interest Earning Assets	48,938	52,283	57,505	63,249	69,567
Total Non-Interest Earning Assets	62,120	68,502	74,655	81,423	88,867
Cash And Marketable Securities	28,321	26,891	50,904	92,228	187,372
Long-term Investments	99,886	96,508	107,124	119,443	133,777
Total Assets	1,000,770	1,191,921	1,376,669	1,588,675	1,869,388
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others	753,640	926,530	1,089,490	1,272,370	1,514,935
Total Interest-Bearing Liabilities	753,640	926,530	1,089,490	1,272,370	1,514,935
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	76,240	83,816	95,979	112,807	134,905
Total Liabilities	829,880	1,010,346	1,185,468	1,385,177	1,649,840
Shareholders Equity	170,890	181,575	191,201	203,498	219,548
Minority Interests					
Total Equity	170,890	181,575	191,201	203,498	219,548

Key Ratios					
	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Total Income Growth	9.9%	9.8%	14.2%	17.4%	14.1%
Operating Profit Growth	2.2%	11.9%	15.9%	20.8%	14.9%
Pretax Profit Growth	103%	(14%)	11%	26%	25%
Net Interest To Total Income	98.0%	97.8%	97.8%	97.9%	97.9%
Cost Of Funds	6.98%	7.65%	7.90%	7.40%	6.80%
Return On Interest Earning Assets	15.4%	14.8%	14.9%	14.8%	14.6%
Net Interest Spread	8.42%	7.16%	6.96%	7.43%	7.83%
Net Interest Margin (Avg Deposits)					
Net Interest Margin (Avg RWA)					
Provisions to Pre Prov. Operating Profit	27%	44%	46%	44%	38%
Interest Return On Average Assets	7.24%	6.36%	6.20%	6.31%	6.17%
Effective Tax Rate	25.9%	25.3%	25.5%	25.5%	25.5%
Net Dividend Payout Ratio					
Return On Average Assets	2.26%	1.60%	1.52%	1.66%	1.79%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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Definition:

- Add** The stock's total return is expected to exceed 10% over the next 12 months.
- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
- Reduce** The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

- Overweight** An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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Definition:

- Overweight** An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral** A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight** An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.