

## Result Update

## Q2 FY11-12

Key Data	
Date	18/10/2011
CMP (₹)	66
Target Price (₹)	99
Bloomberg Code	MGMA IN
Reuters Code	MAGM.BO
BSE Code	524000
NSE Code	MAGMA
Face Value (₹)	2
Market Cap (₹ Bn)	12
52 Week High (₹)	88
52 Week Low (₹)	56
Avg. Daily Volume (6m)	386703
Beta (Sensex)	0.58

Shareholding	%
Promoters	29.3
Foreign Institutional Investors	44.3
Other Domestic Institutions	14.4
Others	12.0
Total	100.0

## Magma Fincorp Ltd

Magma Fincorp (Magma) reported results for Q2FY12. The Company has registered a healthy disbursement growth of 37% in Q2FY12. With a significant rise in the cost of funds and lower assignments, the net interest income has declined by 5.7% to ₹924.2 million, on a YoY basis. The Net profits have also declined by 20% YoY in Q2FY12 to ₹205.7 million.

### KEY HIGHLIGHTS:

- Magma's disbursements grew by 37% YoY in Q2FY12 to ₹15.6 billion. The disbursement mix continues to undergo a change with the focus of the company shifting to high yield segments.
- Magma's funding mix in the recent past has moved in favour of working capital (50% of total borrowings). With interest rates firming up, the company's cost of funds has increased from 10% in Q1FY12 to 10.2% in Q2FY12.
- With the shift in the disbursement mix toward the high yielding loan segments, the blended yields have moved up. However with the significant rise in cost of funds, the spreads have come under pressure. The spreads have declined from 4.6% in Q1FY12 to 4.4% in Q2FY12.
- The net interest income has declined on by 5.7% on YoY basis mainly due to a rise in the cost of funds. Also the company has minimized the assignment transactions during the quarter and has also changed the accounting for the securitization income. The company has now started to amortize the assignment income over the period of tenor rather than recognizing it upfront. In Q2FY11, the interest income included income from assignment of ₹309.1 million. Excluding the same, the net interest income would have been up by 38% YoY. The net profits have in turn declined by 20% YoY to ₹205.7 million in Q2FY12.
- Magma has a capital adequacy ratio of 20% as on September 11 against the requirement of 15%.

### Valuation and Recommendation

During Q2FY12, the company registered strong growth in disbursements. Despite this, the net interest income declined mainly due to the higher cost of funds and the change in strategy pertaining to assignments. The management has indicated that securitisation will now be used as a tool for treasury rather than funding. We have revised our NII estimates downwards to incorporate the accounting change. Further we have also made higher provisioning and therefore our net profit estimates have also been revised downwards.

Going forward, we expect the Net Interest Income (NII) to register a CAGR of 18% during FY11-13. We maintain a **"BUY"** rating on Magma Fincorp Ltd for a revised target of ₹99. (1.5x its book value of ₹65.7 of FY13).

#### Analyst

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## Disbursement growth

Magma's disbursements grew by 37% YoY in Q2FY12 to ₹15.6 billion. The disbursement mix continues to undergo change with the focus of the company shifting to high yield segments. The share of high yield segments has gone up from 18% as on Q2FY11 to 23% as on Q2FY12. These segments being high yield are likely to increase the overall yields and thereby aid the improvement in spreads for the company. With the strong traction being witnessed by the company, we have revised our disbursement growth forecast. We expect the disbursements to register a 30% CAGR during FY11-13 from ₹54.1 billion in FY11 to ₹91.5 billion in FY13.

During the first quarter, in view of the regulatory uncertainty prevailing over securitisation transactions, the management has decided not to lower assignment transactions. Therefore in line with these changes, our loan book assumptions have undergone a change. Given higher on-the-book loans, we expect the loan book to grow at 66% CAGR during FY11-13.

## Borrowing profile

Magma's funding mix in the recent past has moved in favour of working capital (50% of total borrowings). With interest rates firming up, the company's cost of funds has increased from 10% in Q1FY12 to 10.2% in Q2FY12. . With the shift in disbursement mix toward the high yielding loan segments, the blended yields have moved up. However with the significant rise in cost of funds, the spreads have come under pressure. The spreads have declined from 4.6% in Q1FY12 to 4.4% in Q2FY12. Going forward, with the rising interest rate environment, we expect the cost of funds to be under pressure. However the rising proportion of high yield loans will aid spreads to some extent. We expect spreads to decline to 4.6% in FY12 and 4.9% in FY13 from 5% in FY11.

## Asset quality witnessed moderate deterioration

The collection efficiency is at 99.8% as on Q2FY12 lower than 100.1% as on Q1FY12. Although the credit costs have been coming down over the past few quarters, we believe that as the company focuses more on the high yield loan segments; the risk profile is likely to increase thereby impacting the credit/default cost going forward.

## Capital Adequacy

With the recent capital infusion in the company, the capital adequacy (CAR) stands at 20% as on September 2011 of which Tier I capital is at 15%.

## Revision in Estimates

- With the strong traction being witnessed by the company, we have revised our disbursement growth forecast. Against our forecast of 26%, we expect the disbursements to register a 30% CAGR during FY11-13 from ₹54.1 billion in FY11 to ₹91.5 billion in FY13.
- Also, with the lower reliance on assignment and the change in accounting policy for assignment transactions, our net interest income estimates have been revised downwards due to lower securitisation income.
- Given the slowdown being witnessed and the focus on high yielding loan segments, we have revised our provisioning estimates upwards with the increase in risk profile.

	FY12E		FY13E	
	Original	Revised	Original	Revised
Net Interest Income	5,380.6	5,016.9	5,985.5	6,444.5
Net Profits	1,575.7	868.0	1,746.7	1,221.4
EPS	8.3	4.6	9.2	6.4
Book Value	62.2	60.0	70.5	65.7
<b>Source: ACMIIL Research</b>				

## Valuation and Recommendation

Magma Fincorp has been consistently improving its operating performance. During Q2FY12, the company registered strong growth in disbursements. Despite this, the net interest income declined mainly due to the higher cost of funds and the change in strategy pertaining to assignments. The management has indicated that securitisation will now be used as a tool for treasury rather than for funding. With lower reliance on assignment and a change in the accounting policy for assignment transactions, our net interest income estimates have been revised downwards. Provisioning has also gone up with higher risk profile of assets.

On the back of strong growth in disbursements, we expect the Net Interest Income (NII) to register a CAGR of 18% during FY11-13. We maintain a **“BUY”** recommendation on Magma Fincorp Ltd for a revised target of ₹99. (1.5x its book value of ₹65.7of FY13).

Interim Results (₹ Mn)	Q2FY12	Q2FY11	% Chng	Q1FY12	% Chng
Interest Income	2370.8	1849.7		2044.1	
Interest expended	1446.6	869.8		1207.9	
<b>Net Interest Income</b>	<b>924.2</b>	<b>980.0</b>	<b>-5.7</b>	<b>836.2</b>	<b>10.5</b>
Other Income	148.6	140.7		167.3	
Operating Income	1072.8	1120.7		1003.4	
Operating Expenses	683.5	678.1		665.0	
Profit before provisions	389.2	442.6		338.5	
Provision for Bad debts	87.0	47.8		84.8	
Profit before Taxes	302.3	394.7		253.7	
Provisions for taxes	89.5	131.3		82.5	
Minority Interest	7.0	5.1		7.5	
<b>Net Profit</b>	<b>205.7</b>	<b>258.4</b>	<b>-20.4</b>	<b>163.7</b>	<b>25.6</b>
Equity Share capital	359.3	258.7		359.3	
EPS	1.1	2.0		0.9	
<b>Source: Company</b>					

## FINANCIALS

Earnings Summary				₹ Mn
Particulars	FY10	FY11	FY12E	FY13E
Interest Income	6,565.9	8,190.4	11,455.3	16,572.2
Interest expended	3,250.5	3,523.4	6,438.5	10,127.7
<b>Net Interest Income</b>	<b>3,315.4</b>	<b>4,667.0</b>	<b>5,016.9</b>	<b>6,444.5</b>
Other Income	668.8	549.9	650.2	755.6
Operating Income	3,984.2	5,216.9	5,667.1	7,200.1
Operating Expenses	2,470.4	3,039.2	3,784.0	4,375.0
Pre Provisioning Profits	1,513.8	2,177.7	1,883.1	2,825.1
Provisions & contingencies	408.3	355.6	566.5	972.5
Prior Period Items	-0.9	1.2	0.0	0.0
Profit before Taxes	1,104.6	1,823.3	1,316.5	1,852.6
Provisions for taxes	391.4	600.6	434.5	611.4
Profit after Taxes	713.2	1,222.7	882.1	1,241.2
Minority Interest	12.6	20.1	14.1	19.9
<b>Net Profits</b>	<b>700.6</b>	<b>1202.6</b>	<b>868.0</b>	<b>1221.4</b>
<b>Source: Company, ACMIIL research</b>				

Sources & Application of Funds				₹ Mn
Particulars	FY10	FY11	FY12E	FY13E
<b>Liabilities</b>				
Capital	1,378.8	1,853.4	1806.2	1764.0
Equity Share Capital	217.8	259.5	379.5#	379.5
Preference Share Capital	1161.0	1593.8	1426.7	1384.5
Reserves & Surplus	3,304.9	5,462.9	10,998.0	12,090.8
Networth	4,897.6	7,316.3	12,804.2	13,854.8
Borrowings	36,543.3	45,924.5	80,219.8	113,380.6
Deferred Tax Liability	478.9	380.9	382.9	382.9
Minority Interest	52.3	98.4	112.5	132.3
<b>Total</b>	<b>41,972.0</b>	<b>53,720.1</b>	<b>93,519.4</b>	<b>127,750.6</b>
<b>Assets</b>				
Fixed assets	2,079.6	1,871.3	1,690.8	1,541.2
Investments	191.2	113.8	113.8	113.8
Loans and Advances	33,013.7	45,142.9	84,441.9	124,594.0
Net Current Assets	6,687.5	6,592.1	7,272.9	1,501.6
<b>Total</b>	<b>41,972.0</b>	<b>53,720.1</b>	<b>93,519.4</b>	<b>127,750.6</b>
Source: Company, ACMIIL research # Assumed conversion of warrants				

Key Ratios				
Particulars	FY10	FY11	FY12E	FY13E
<b>Spreads</b>				
Yield on Advances	13.7%	13.2%	14.8%	15.3%
Cost of Borrowings	8.7%	8.2%	10.2%	10.5%
Net Interest Income	5.0%	5.0%	4.6%	4.9%
<b>Profitability ratios</b>				
Return On Average Assets (ROAA)	2.0%	2.5%	1.2%	1.2%
Return On Average Net worth (ROANW)	20.8%	25.4%	10.2%	10.6%
<b>Balance sheet ratios</b>				
Loan to borrowings ratio (%)	90.3	98.3	105.3	109.9
Debt/Equity Ratio (Times)	7.5	6.3	6.3	8.2
<b>Growth Ratios</b>				
Borrowings	45.8%	25.7%	74.7%	41.3%
Loans	61.4%	36.7%	87.1%	47.5%
Networth	18.2%	49.4%	75.0%	8.2%
NII	15.7%	40.8%	7.5%	28.5%
<b>Valuation ratios</b>				
EPS (₹.)	6.4	9.3	4.6	6.4
Book value (₹.)	32.4	44.1	60.0	65.7
P/E (X)	10.3	7.1	14.4	10.3
P/BV (X)	2.0	1.5	1.1	1.0
Source: Company, ACMIIL research				

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