

Magma Fincorp

Event Update

24 May 2011

Buy

Target Price: Rs125

CMP: Rs75

Upside: 67%

*as on 23 May 2011

Capital infusion addresses growth concerns

Magma Fincorp announced an investment of Rs 4.4bn led by funds managed by Kohlberg Kravis Roberts and International Finance Corporation. Of the total infusion of Rs4.4bn, KKR will invest Rs2.4bn (for a stake of 14.95%) while IFC will invest Rs2.0bn (for a 12.80% stake) in the expanded equity capital. The stake sale values Magma at Rs88 per equity share (~25% premium over cmp of Rs75). Magma is likely to receive the funds by June'2011 following the approval of the shareholder in the scheduled AGM.

Impact analysis

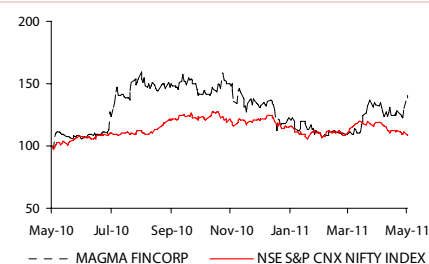
- **Capital adequacy to improve:** As at end of Q4FY11, the CAR of Magma reached ~18% vs 15% required by RBI. Considering the aggressive growth plan (guidance of 50% growth in disbursement), capital raising was crucial for funding the growth especially for FY13. With equity infusion of Rs4.4bn, the CAR should inch up to ~26% with FY12 CAR estimated at ~22%. Collectively, the two transactions imply an equity dilution of 27.8% on expanded equity base.
- **Improved growth visibility:** As highlighted in our Q4FY11 result update, capital constraint was one of the key reasons behind our below guidance disbursement growth estimate (of 42% in FY12). With this capital infusion, we believe that Magma should be able to fund its balance sheet growth comfortably while honoring capital adequacy requirements. The capital infusion assumes great significance in current operating environment marked by increased hawkish stance taken by RBI on NBFCs in general (loss of priority status of non-MFIs, potential revision of regulations governing assignment of loans etc). We expect Magma to reduce reliance on securitization further to ~35% in FY12 and 25% in FY13 (from ~50% share currently).
- **Positive for profitability:** The infusion of equity capital should also cushion the pressure on NIMs arising from high cost of debt capital to an extent. Moreover, plans to increase the share of high-yield loans to 25% by FY12 should also help cushion pressure on NIMs. While the company continues to guide improvement in NIM (led by increase in yields), we have conservatively factored in a ~20bps contraction over FY2012.
- **Revision in estimates:** We are factoring in the capital infusion into our estimates and raise our disbursement growth estimate upwards (from 42% yoy to 50% yoy) while we bring down the share of off-balancesheet loan book. Effectively, the estimate revisions lead to a 25% increase in our FY12 BVPS and 17% increase in FY13 BVPS. In line, we revise our target price upwards to Rs125 (at 1.7x FY13E BVPS), implying an upside of 67%. At current market price of Rs75, the stock trades at 1.0x FY13E Adj. BVPS and offers an excellent entry point for long term investors. We maintain Buy.

Key Data

Bloomberg Code	MGMA IN
Reuters Code	MAGM.BO
Current Shares O/S (mn)	129.8
Diluted Shares O/S(mn)	129.8
Mkt Cap (Rsbn/USDmn)	9.7/214.9
52 Wk H / L (Rs)	88/50
Daily Vol. (3M NSE Avg.)	412,434
Face Value (Rs)	2

1 USD = Rs45.3

One Year Indexed Stock Performance



Price Performance (%)

	1M	6M	1Yr
MGMA IN	6.0	(6.4)	40.7
NIFTY	(8.2)	(7.9)	9.3

Source: Bloomberg, Centrum Research
*as on 23 May 2011

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Y/E Mar	NII	Non Int. Inc.	PAT	YoY gr (%)	EPS (Rs)	P/E (x)	Adj BV (Rs)	P/Adj BV (x)	RoA (%)	RoE (%)
FY09	3,410	21	398	(21.2)	3.0	24.9	27.6	2.7	1.3	14.1
FY10	3,943	37	713	79.2	5.8	12.9	32.8	2.3	1.8	21.7
FY11	5,200	17	1,221	71.2	8.2	9.2	41.0	1.8	2.3	26.3
FY12E	6,344	20	1,574	28.8	7.9	9.5	63.1	1.2	2.0	25.7
FY13E	8,497	25	2,317	47.2	11.8	6.4	74.0	1.0	2.0	22.5

Source: Company, Centrum Research Estimates

Exhibit 1: Estimate Revision

Key Revisions	Revised		Earlier		Remarks
	FY12E	FY13E	FY12E	FY13E	
<i>Disbursements (% growth YoY)</i>	50	37	42	30	Better growth visibility following capital infusion
<i>AUM (% growth YoY)</i>	34	35	29	29	
<i>% Incremental share of off-BS</i>	35	25	42	30	Reliance on securitization to come off materially
<i>NII (Rsmn)</i>	6,344	8,497	6,246	8,010	
<i>PPP (Rsmn)</i>	2,778	4,147	2,741	3,545	Marginal improvement in FY12 PPP as we factor in increase in opex
<i>PAT (Rsmn)</i>	1,574	2,317	1,549	1,932	
<i>CAR (%)</i>	21.4	16.6	16.1	13.9	Substantial improvement in CAR to fund growth for next 2 yrs
<i>NIM (%)</i>	5.7	5.7	5.7	5.7	
<i>RoA (%)</i>	2.0	2.0	2.2	2.0	
<i>RoE (%)</i>	25.7	22.5	24.2	24.4	Dilution in RoE due to equity infusion
<i>BVPS (Rs)</i>	63.1	74.0	50.7	62.9	

Source: Centrum Research Estimates

Financials

Exhibit 2: Income Statement

Y/E March (Rsmn)	FY09	FY10	FY11	FY12E	FY13E
Interest Income	6,291	7,194	8,723	12,101	18,426
Interest Expense	2,880	3,250	3,523	5,758	9,929
Net Interest Income	3,410	3,943	5,200	6,344	8,497
YoY Growth (%)	15.7	15.6	31.9	22.0	33.9
Non Interest Income	21	37	17	20	25
YoY Growth (%)	(66.9)	78.7	(54.3)	18.3	25.0
Total Income	3,431	3,980	5,217	6,364	8,522
Total Operating Expenses	2,406	2,467	3,039	3,586	4,375
YoY Growth (%)	30.7	2.6	23.2	18.0	22.0
Pre-provision Profit	1,026	1,513	2,178	2,778	4,147
Provisions	415	408	356	429	637
Profit Before Tax	610	1,105	1,822	2,349	3,510
Taxes	212.4	391.4	600.6	775.1	1,193.4
Net Profit	398	713	1,221	1,574	2,317

Source: Company, Centrum Research Estimates

Exhibit 3: Balance Sheet

Y/E March (Rsmn)	FY09	FY10	FY11	FY12E	FY13E
Share capital	218	218	260	379	379
Preference capital - 10-12% (cum & non cum)	1,180	1,161	1,594	1,594	1,594
Reserves & Surplus	2,789	3,357	5,463	11,589	13,645
Shareholders' fund	4,187	4,736	7,316	13,562	15,618
Borrowings	25,066	36,543	45,924	75,290	119,396
Current liabilities	4,273	5,350	5,676	6,243	6,868
Total Liabilities	33,526	46,629	58,917	95,095	141,882
Net block	2,382	2,080	1,871	2,058	2,264
Stock on Hire	20,459	33,014	45,201	75,290	119,396
Investments	290	191	114	250	250
Debtors	-	-	-	-	-
Cash & Bank	9,025	9,709	10,075	17,497	19,972
Loans & Advances	1,369	1,636	1,656	1,700	2,000
Total Assets	33,525	46,630	58,917	95,095	141,882

Source: Company, Centrum Research Estimates

Exhibit 4: Key Ratios

Y/E March	FY09	FY10	FY11	FY12E	FY13E
B/S Structure Ratios (%)					
Loan Growth	9.6	61.4	36.9	66.6	58.6
Assets Growth	16.1	39.1	26.3	61.4	49.2
Funds Growth	16.1	15.1	16.6	33.7	35.1
Operating Ratios (%)					
NIM	5.2	5.2	5.9	5.7	5.7
Non-interest income/Net income	0.61	0.94	0.33	0.32	0.29
Cost/Income	70.1	62.0	58.3	56.4	51.3
Operating cost growth	30.7	2.6	23.2	18.0	22.0
Total prov as % of avg. loans	0.6	0.5	0.4	0.5	0.5
Tax Rate (%)	34.8	35.4	33.0	33.0	34.0
Capital Adequacy Ratios (%)					
Total CAR	17.3	14.9	18.1	21.4	16.6
Tier 1 CAR	9.2	8.6	10.8	14.0	11.0
Profitability Ratios (%)					
RoAE	14.1	21.7	26.3	25.7	22.5
RoAA	1.3	1.8	2.3	2.0	2.0
Valuations Ratios (x)					
BVPS (Rs)	27.6	32.8	41.0	63.1	74.0
Price/BV (x)	2.9	2.3	1.8	1.2	1.0
EPS (Rs)	3.0	5.8	8.2	7.9	11.8
P/E (x)	26.9	12.9	9.2	9.5	6.4
DPS (Rs)	0.23	0.47	0.60	0.71	0.94
Dividend yield (%)	0.3	0.6	0.8	0.9	1.3

Source: Company, Centrum Research Estimates

Appendix A

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