

# Magma Fincorp (MGMA IN)

**OUTPERFORMER**
**Margins under stress**
**Rs57**
**Mkt Cap: Rs10.9bn; US\$215m**

## Q3FY12 result highlights

**Quarterly performance:** Magma reported Q3FY12 PAT of Rs139m – well below our estimate of Rs301m. The underperformance can be attributed to NII being lower at Rs897m (down 22% yoy and 3% qoq) owing to sharp rise in cost of funds (interest expense to average assets up 60bp qoq). Also, the financier booked Rs50m of MTM forex losses during the quarter.

**Key positives:** Business volumes remained robust with disbursements increasing by 50% yoy (23% qoq) to Rs 19.2bn. Further, the increasing share of high-yielding segment in disbursements (25% vs 22% in Q3FY11) contributed to 20bp qoq rise in calculated yield on advances.

**Key negatives:** Calculated NIMs (on quarterly average balances) declined to 4.8% in Q3FY12 from 5.2% in Q2FY12 as increase in yield on advances was more than offset by higher cost of funds.

## Impact on financials

Magma's Q3FY12 earnings disappointed due to high funding costs and lower securitization income. Factoring in lower securitization income and stress on NIMs, we pare our earnings estimates by 30% for FY12 and 20% for FY13. However, we expect spreads to revive hereon owing to an increasing share of high-yielding segment. Also, disbursement growth is likely to stay robust at 34% CAGR over FY11-13E. Momentum in disbursements and lower securitization (at ~24% of AuM by FY13E), we believe, would drive 66% CAGR in advances and 21% CAGR in profits over FY11-13.

## Valuations & view

We see significant upside potential for the stock as Magma attains scale, profitability improves and the balance sheet strengthens. At 0.9x FY13E book, the stock trades at a deep discount to peers. Given Magma's high growth and profitability potential, we reiterate Outperformer with a lowered 12-month price target of Rs100 (1.5x FY13E BV).

### Key financials (quarterly)

(Rs m)	Q3FY11	Q2FY12	Q3FY12	% ch qoq	% ch yoy	% var from est
<b>NII</b>	<b>1,152</b>	<b>924</b>	<b>897</b>	<b>(2.9)</b>	<b>(22.1)</b>	<b>(18.7)</b>
Non-intt income	138	149	127	(14.8)	(8.2)	(36.7)
<b>Net revenue</b>	<b>1,290</b>	<b>1,073</b>	<b>1,024</b>	<b>(4.5)</b>	<b>(20.6)</b>	<b>(21.5)</b>
Operating expense	730	683	726	6.3	(0.5)	(1.9)
Operating profit	560	389	298	(23.5)	(46.8)	(47.2)
Provisions	70	87	92	5.9	32.2	(23.5)
<b>PAT</b>	<b>327</b>	<b>213</b>	<b>139</b>	<b>(34.7)</b>	<b>(57.5)</b>	<b>(53.9)</b>
Disbursements (Rs bn)	12.7	15.6	19.2	22.9	50.3	
AUM (Rs bn)	90.0	113.8	118.6	4.2	31.7	

### Key valuation metrics

YE 31 March	FY11	FY12E	FY13E
Net profit (Rs m)	1,221	826	1,798
yoy growth (%)	71.0	(32.3)	117.7
Shares in issue (m)	130.0	190.0	190.0
EPS (Rs)	9.4	4.3	9.5
EPS growth (%)	43.2	(53.7)	117.7
PE (x)	6.0	12.9	5.9
Book value (Rs/share)	45.0	57.0	65.3
P / BV (x)	1.2	1.0	0.9
ROAE (%)	24.8	9.2	15.0

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## Quarterly results: Detailed

(Rs m)	Q3FY11	Q2FY12	Q3FY12	FY11	FY12E	FY13E	Remarks
Interest income	2,120	2,371	2,655	7,952	10,342	16,801	
Interest expense	968	1,447	1,758	3,523	6,498	10,075	
<b>NII</b>	<b>1,152</b>	<b>924</b>	<b>897</b>	<b>4,429</b>	<b>3,843</b>	<b>6,726</b>	<b>Lower owing to margin compression</b>
yoy growth (%)	53.2	(5.7)	(22.1)	37.3	(13.2)	75.0	
Other income	138.0	148.6	126.7	788	661	785	
yoy growth (%)	(21.6)	5.6	(8.2)	4.5	(16.1)	18.7	
Operating expenses	730	683	726	3,039	2,945	4,132	Lower due to amortisation of origination expenses
yoy growth (%)	84.5	(12.0)	(46.8)	23.2	(3.1)	40.3	
<b>Operating profit</b>	<b>560</b>	<b>389</b>	<b>298</b>	<b>2,178</b>	<b>1,560</b>	<b>3,378</b>	
yoy growth (%)	84.5	(12.0)	(46.8)	43.9	(28.4)	116.6	
Provisions	70	87	92	356	345	734	Asset quality remains robust
Profit before tax	490	302	206	1,822	1,215	2,645	
yoy growth (%)	104.2	(23.4)	(58.1)	64.8	(33.3)	117.7	
<b>Net profit</b>	<b>327</b>	<b>213</b>	<b>139</b>	<b>1,221</b>	<b>826</b>	<b>1,798</b>	<b>Well below estimates</b>
yoy growth (%)	82.2	(19.2)	(57.5)	71.0	(32.3)	117.7	
<b>Ratios (%)</b>							
Reported net spread on loans	4.7	4.2	4.3				Impacted by higher cost of funds
Calc Net interest margin	6.2	5.2	4.6	5.4	4.7	5.2	
Other income /Avg assets	1.2	0.8	0.6	1.5	0.8	0.7	
Expenses/Avg assets	6.1	3.8	3.7	5.8	3.7	3.4	
Cost/Income	56.6	63.7	70.9	58.3	65.4	55.0	
Provisions/Avg assets	0.6	0.5	0.5	0.7	0.4	0.6	
PBT/Avg assets	4.1	1.7	1.0	3.5	1.5	2.2	
RoA	2.7	1.2	0.7	2.3	1.1	1.5	
Tax/PBT	33.3	29.6	32.4	33.0	32.0	32.0	
Tier-I CRAR (%)	11.7	15.1	13.9	11.3			
Overall CAR (%)	19.2	20.0	20.3	18.2			
<b>Balance Sheet (Rs bn)</b>							
Loan Book	41	64	73	45	83	124	
yoy growth (%)	21.0	65.0	65.7	36.7	83.1	50.1	
Disbursements	13	16	19	54	74	97	Strong traction across segments
yoy growth (%)	21.5	36.8	50.3	18.8	35.9	31.2	
AUM	90	114	119	109	140	182	High yielding assets gaining share
yoy growth (%)		17.4	31.7	15.0	28.7	29.5	

## Other Highlights

- NIMs decline sequentially:** Calculated NIMs declined to 4.8% (on average quarterly assets) in Q3FY12 from 5.2% in Q2FY12 (excluding the impact of MTM forex loss of Rs50m). A ~20bp qoq rise in yield on advances on the back of higher share of high-yielding segment was more than offset by increase in cost of funds. Going forward, while yields are prone to competitive pressure, tempering of mix towards high-yielding segments would bolster spreads. (exhibit 1 & 4)
- Strong disbursement momentum:** Disbursement momentum continued in Q3FY12 (up 50% yoy) led by sharp rise in disbursements to cars and UVs (up 84% yoy) and high yielding segments (up 70% yoy on a low base). We expect the lender to clock 34% CAGR in disbursements over FY11-13. (exhibit 2 & 3)

- **Reducing reliance on bank funding:** Diversifying the funding sources, the lender has decreased the share of bank in total funding mix to 58% vs. 78% in Q3FY11. Correspondingly, proportion of NCDs in Magma's funding mix increased to 19% in Q3FY12 from 4% in FY11. Also, the lender is in the process of reducing securitization of loans leading to a spike in on-book borrowings. (exhibit 5)
- **Amortisation of expenses supports bottom-line:** Magma's operating expenses came in at Rs726m – a 1% yoy decline. Low level of expense can be attributed to 35% yoy reduction in origination expenses, owing to change of policy towards amortization of such expenses. Consequent to this change, expenses of Rs161m were deferred in the quarter and would be amortized over the tenor of the loans.
- **Asset quality remains strong:** Collection efficiency remained strong at 100.4% as against 99.5% in Q2FY12. Write-offs as a % of AUM came in at 0.3% for the quarter. We continue to build in higher credit costs for FY12 and FY13 to factor in a potential rise in delinquencies owing to rapid growth in high yielding segments. (exhibit 6)

Exhibit 1: NIMs

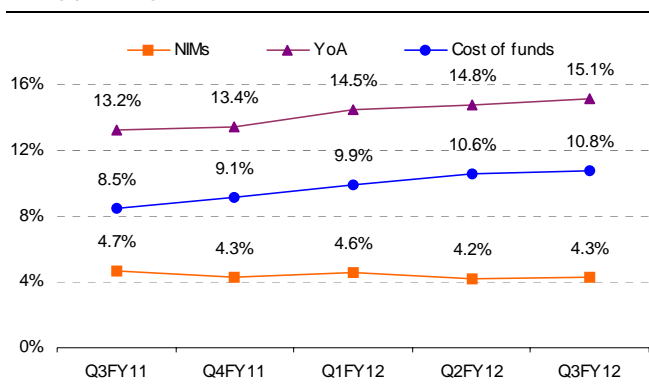


Exhibit 2: Strong volume growth

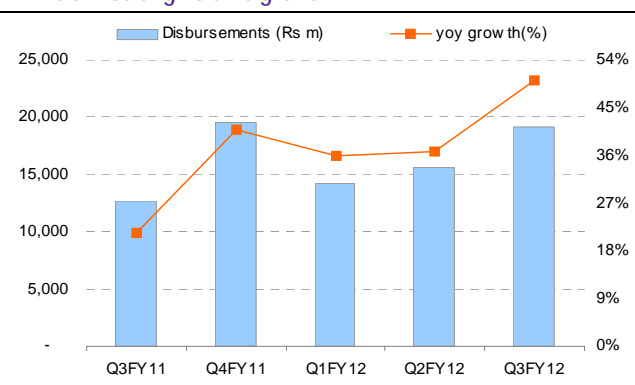


Exhibit 3: Segment-wise composition of disbursements (%)

(%)	Q3FY11	Q2FY12	Q3FY12
CVs	34	29	27
Constr equipment	20	19	18
Cars and Uvs	24	29	30
Used CV	5	6	7
Tractor	10	11	13
SME loans	7	6	5

Exhibit 4: Yields on disbursements by segments (%)

	Q3 FY11	Q2 FY12	Q3 FY12	change (bp)	
				qoq	yoy
CVs	11.3	13.0	13.2	20	190
Constr equipment	11.8	13.6	13.6	-	180
Cars and Uvs	12.7	14.2	14.4	20	170
Used CV	17.9	19.0	19.6	60	170
Tractor	19.5	20.1	20.0	(10)	50
SME loans	16.2	16.7	16.5	(20)	30
Wtd average	13.2	14.8	15.1	30	189

Exhibit 5: Funding profile (Rs m)

	Q3FY11	Q2FY12	Q3FY12	% of total
Working capital	21,050	28,137	26,988	28
Pref shares/Sub debt/ PD	5,400	5,742	6,316	7
NCDs	4,320	14,356	17,801	19
Term loans	10,490	9,188	9,188	10
<b>Total borrowings</b>	<b>41,260</b>	<b>57,422</b>	<b>60,293</b>	<b>63</b>
<b>Securitization</b>	<b>40,000</b>	<b>39,186</b>	<b>35,724</b>	<b>37</b>

Exhibit 6: Robust asset quality

(%)	Q3FY11	Q2FY12	Q3FY12
Provisions/ AUM	0.30	0.31	0.32
Collection efficiency	100.9	99.5	100.4

## Income statement

Year to 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
<b>Net interest income</b>	<b>3,227</b>	<b>4,429</b>	<b>3,843</b>	<b>6,726</b>
<i>yoy growth (%)</i>	12.6	37.3	(13.2)	75.0
Other income	754	788	661	785
<i>yoy growth (%)</i>	33.6	4.5	(16.1)	18.7
<b>Net revenue</b>	<b>3,981</b>	<b>5,217</b>	<b>4,504</b>	<b>7,511</b>
<i>yoy growth (%)</i>	16.0	31.1	(13.7)	66.7
Operating expenses	2,467	3,039	2,945	4,132
<i>yoy growth (%)</i>	2.6	23.2	(3.1)	40.3
Provisions	408	356	345	734
<b>PBT</b>	<b>1,105</b>	<b>1,822</b>	<b>1,215</b>	<b>2,645</b>
<i>yoy growth (%)</i>	81.0	64.8	(33.3)	117.7
Provision for tax	391	601	389	846
<b>PAT</b>	<b>714</b>	<b>1,221</b>	<b>826</b>	<b>1,798</b>
<i>yoy growth (%)</i>	79.3	71.0	(32.3)	117.7

## Balance sheet

As on 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
Loan book on balance sheet	33,014	45,143	82,650	124,067
<i>yoy growth (%)</i>	61.4	36.7	83.1	50.1
Off balance sheet assets	48,184	50,153	42,168	39,964
Total managed assets	81,197	95,296	124,818	164,031
<i>yoy growth (%)</i>	15.8	17.4	31.0	31.4
Total assets	46,630	58,917	98,225	141,875
<i>yoy growth (%)</i>	39.1	26.4	66.7	44.4
Networth	3,523	5,848	10,830	12,398
Loan funds	36,543	45,924	78,911	118,538
Gearing (no of times)	13.2	10.1	9.1	11.4
Debt/ Equity	10.4	7.9	7.3	9.6

## Key valuation metrics

Year to 31 Mar	FY10	FY11	FY12E	FY13E
Net profit (Rs m)	714	1,221	826	1,798
<i>yoy growth (%)</i>	79.3	71.0	(32.3)	117.7
Shares in issue (m)	108.9	130.0	190.0	190.0
EPS (Rs)	6.6	9.4	4.3	9.5
EPS growth (%)	79.3	43.2	(53.7)	117.7
PE (x)	8.6	6.0	12.9	5.9
Book value (Rs/share)	32.4	45.0	57.0	65.3
P / BV ( x)	1.7	1.2	1.0	0.9
ROAE (%)	20.2	24.8	9.2	15.0

## Ratio analysis

Year to 31 Mar (%)	FY10	FY11	FY12E	FY13E
Net int. margin/avg assets	8.1	8.4	4.9	5.6
Non-fund rev./avg assets	1.9	1.5	0.8	0.7
Operating exp./avg assets	6.2	5.8	3.7	3.4
Cost/Income	62.0	58.3	65.4	55.0
Prov./avg b/s loan assets	1.0	0.7	0.4	0.6
PBT/Average assets	2.8	3.5	1.5	2.2
RoA	1.8	2.3	1.1	1.5
RoE	20.2	24.8	9.2	15.0
Tax/PBT	35.4	33.0	32.0	32.0
Tier I Capital adequacy	8.6	11.3	12.2	9.7

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- |                   |   |
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