Magma Fincorp Ltd.

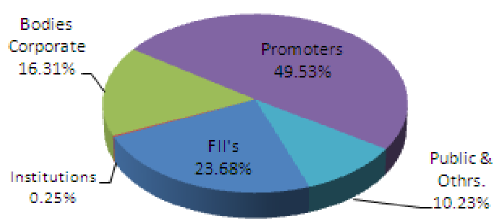
SKP Securities Ltd

...financing assets & dreams

CMP Rs. 305.75 | **Target Rs. 549.00** | **Initiating Coverage- Buy**

Key Share Data	
Face Value (Rs.)	10.00
Equity Capital (Rs. Crs)	21.78
Market. Capitalization (Rs. Crs)	665.92
52-wk High / Low (Rs.)	312.40/122.00
Average Yearly Volume	85429
BSE code	524000
NSE code	MAGMA
Reuters code	MAGM.BO
Bloomberg code	MGMA.IN

Shareholding Pattern – 31st December, 2009



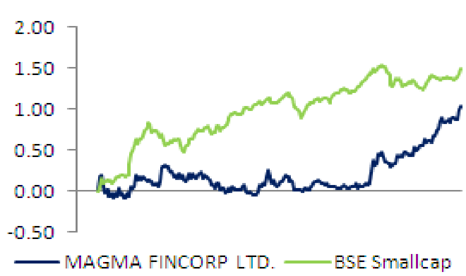
Financials (Consolidated) (Rs. Crs)

	FY09	FY10E	FY11E	FY12E
Op. Income	621.03	768.70	994.16	1317.2
Gr%	33.35%	23.78%	29.33%	32.50%
EBDTA	95.28	136.29	187.60	254.20
PAT	39.85	67.29	106.41	149.39
PAT Gr %	-20.80%	69.33%	58.04%	40.36%
EPS (Rs.)	14.79	30.90	48.86	68.59
CEPS (Rs)	37.59	52.79	71.76	96.53

Key Financial Ratios (Consolidated)

	FY09	FY10E	FY11E	FY12E
Div. yield	0.63%	0.33%	0.33%	0.33%
P/E	10.72	9.90	6.26	4.46
P/BV	1.16	1.42	1.18	0.95
P/Cash EPS	4.22	5.79	4.26	3.17
MCap/Sales	0.56	0.87	0.67	0.51
EV/EBDTA	20.17	15.69	12.75	8.57
ROCE	11.93%	12.55%	13.37%	14.12%
RONW	9.65%	14.37%	18.90%	21.36%
EBTDM(%)	15.34%	17.73%	18.87%	19.30%
NPM (%)	6.41%	8.77%	10.71%	11.35%
Debt-Equity	6.08	6.16	6.20	6.25

Performance comparison MFL v/s BSE Smallcap



Analyst: Soumen Ghosh
Tel No.: +91 33 4007 7416; Mobile: +919830447472
Email: soumen.ghosh@skpmoneywise.com

Company Profile

Magma Fincorp Limited (formerly Magma Leasing Limited) is a Kolkata headquartered asset financing company. It was incorporated in 1988, and commenced operation in 1989. The company has a vast distribution network with more than 150 branches and a range of products and services that cater to the needs of both corporate and individuals.

Investment Rationale

Broad spectrum of services offered to a specific customer segment

- MFL offers a broad spectrum of services viz. Consumer Vehicle (CV) Finance, Construction Equipment (CE) Finance, Car & utility vehicle finance, Used car finance, SME loans, Tractor Finance and Insurance services.
- The company offers its services to the rural and semi urban population, which is approximately 70% of the population.

Extensive network and strategic tie-ups with auto manufacturers and OEM

- MFL has 150 branches spanning across 20 states and 1 Union Territory.
- The company has entered into tie ups with M&M, Tata Motors, Ashok Leyland, MUL, GM, HMIL, Telcon, JCB, ACE, TIL, BEML, Terex Vectra, TAFE etc. to finance their vehicles/products. This provides MFL an access to a large captive customer base.

Best in class collection mechanism resulting in lowest NPA in the industry

- In FY09, Magma had zero NPA on its books. The write offs also went down from 0.7% of loans in FY08 to 0.6% in FY09.
- MFL had collection efficiency of 97.8% in FY09, and 98.9% for 9MFY10. Such strong collection process ensures that the NPA and write offs are kept at a minimum.

Shifting to high yield products to result in better profitability

- The share of high yield products in MFL's product portfolio has gone up to 13.5%, and this figure is expected to go up in future.
- High yield products like SME loans and Tractor Loans enhance the overall Net Interest Margins (NIM) of the company.

Specialized verticals resulting in better operational efficiency

- MFL has segregated business vertical from the credit vertical, ensuring better focus and operational efficiency. The segregation also strengthened the internal credit appraisal filter.

Outlook & Recommendation

MFL is expected to do better than the industry by virtue of growth in topline, supported by improving NIM, vast reach and operating efficiency.

We recommend BUY rating on the stock with an 18 months target price of Rs 549, at 8x FY12 earnings, giving it an upside potential of 79% from the current levels.

Key features of NBFCs

- The major role of Non Banking Finance Companies-Asset Financing Companies (NBFC-AFCs, as recognized by RBI/ Expert committee) are Development of sectors like transport & infrastructure, irreplaceable supplement to bank credit in rural segment and finance economically weak section.

- NBFCs on a whole account for 9.1% of the assets of the total financial system.

- The road transport sector accounts for nearly 70% of goods movement and 80% of passenger movement across the length and breadth of the country and the role of NBFC-AFCs (NBFC-AFCs provide 80% to 90% of funding for the Road Transport Sector) in the growth and development of this sector has been historically acknowledged by several committees set up by the Government and RBI, over the years.

- NBFCs not only provide financial assistance to its customers but also guidance relating to matters of insurance.

- NBFCs have low operating cost as compared to other financial institutes due to their smaller size, efficient operation and faster decision making.

- Default risk is lower for NBFCs due to aggressive collecting mechanism and lower portion of big corporate loans.

- NBFCs provide prompt, tailor made services with least hassles. This more than compensates for the high lending rates for the NBFCs.

- The cost of capital for NBFCs is usually 200-300 bps higher than that of banks, but these firms can leverage up to 8 times on their equity. NBFCs typically leverage 5-6 times, sourcing funds from banks, MFs, wholesale markets and retail deposits to generate 13-14% return on equity (RoE).

- RoE for NBFCs, a measure of their profitability as compared to their equity, is a function of the number of times they can leverage. When the number of times an NBFC is leveraged falls to 4, its RoE falls to 10% or below. When leveraging falls further, the business cannot sustain itself.

Financial Industry Overview

- After clocking annual growth of 8.9 % on an average over the last five years (2003-08), India was headed for a cyclical downturn in 2008-09. But the growth moderation has been much sharper because of the negative impact of the crisis. In fact, in the first two quarters of 2008-09, the growth slowdown was quite modest; the full impact of the crisis began to be felt post-Lehman in the third quarter, which recorded a sharp downturn in growth.

- India's GDP Growth during Q2 of 2009-10, at 7.9 %, revealed a degree of resilience that was unexpected. Subsequent data releases, whether on industrial production, infrastructure or exports, confirm the assessment that the economy is steadily gaining momentum. Based on this better-than-expected performance, growth forecasts for 2009-10 have generally been revised upwards.

- Non-food bank credit growth decelerated significantly from its peak of over 29 % in October 2008 to a little over 10 % in October 2009. Thereafter, it recovered to over 14 % by mid-January 2010. As per the RBI data, total flow of financial resources from banks, domestic non-bank and external sources to the commercial sector during 2009-10 (up to January 15, 2010) at Rs.5,89,000 crore was only marginally lower than Rs.5,95,000 crore in the corresponding period of the previous year.

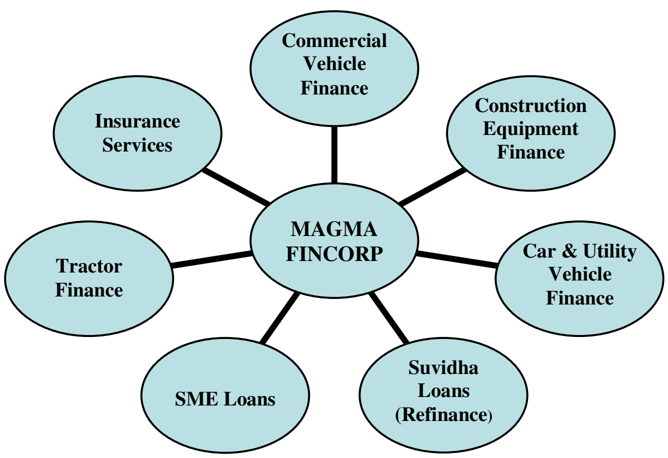
- During the current financial year, the year-on-year growth in money supply (M3) moderated from over 20.0 % at the beginning of the financial year to 16.5 % on January 15, 2010, reflecting deceleration in bank credit growth during 2009-10. Year-on-year increase in non-food bank credit to the commercial sector, at 14.4 % as on January 15, 2010, was significantly lower than the 22.0 % growth a year ago.

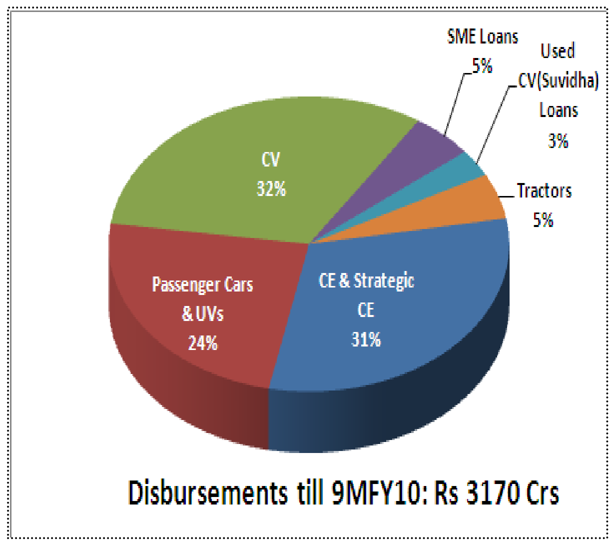
- Since over 98 % of the net market borrowing programme of the Central Government for 2009-10 has already been completed by January 28, 2010, the anticipated increase in credit demand by the commercial sector in the remaining period of 2009-10 can, therefore, be easily met from the market as adequate liquidity is available in the system.

Company overview

Magma Fincorp Limited (formerly Magma Leasing Limited) is a Kolkata headquartered asset financing company. It was incorporated in 1988, and commenced operation in 1989. The company has a vast distribution network with more than 150 branches and a range of products and services that cater to the needs of both corporate and individuals.

Business overview





Source: Company

Credit Rating of MFL

Rating	Instrument	Rating Agency
AAA (SO)	Securitization Pool	CRISIL/CARE
AA	LT Loans from Banks, Unsecured LT Borrowings, Secured Redeemable LT Bond/Note	CARE
AA-	Unsecured Subordinated Tier II Bonds	CARE
A+	Perpetual debt Instrument	CARE
PR1+	CC from Banks, CP/ST Debt (90 Days & 1 Year maturity)	CARE

** LT denotes Long term, ST denotes Short Term, CC denotes Cash Credit and CP denotes Commercial Papers*

Applicability of Porter's 5 Forces Model in MFL's business

THREAT OF NEW ENTRANTS

- NBFC has been a sector which drew many players in early '90s due to easy cash flow and huge liquidity. After stringent policy of regulatory bodies like RBI, the no. has reduced significantly.
- The sector of non deposit taking Asset financing NBFC, under which Magma falls, is considered vital for development of sectors like transport & infrastructure. Thus RBI is planning to apply regulations at par with banks on this sector. This will further reduce entry of new players into this particular segment.

DETERMINANTS OF SUPPLIER POWER

- Magma has entered into alliance with OEMs and companies like Tata Motors, ALL, M&M, etc thus enhancing their access to dispersed customers.
- MFL has formed a JV with HDI Gerling International Holding AG (HDI), part of Talanx AG Group, the third largest insurance group in Germany.

RIVALRY AMONG EXISTING FIRMS

- MFL's competitors viz. Sundaram Finance, Shriram Finance & SREI Infrastructure have little or no presence in rural & semi-urban area. This gives Magma a clear advantage.
- The entry of PSU and Private banks in segments like car loans and SME loans have intensified competition amongst the existing players. However, the banks have stringent credit filters and their reach is limited, whereas MFL's strength lies in its vast network and target customers who are first time buyers and small entrepreneurs, who may be overlooked/ denied by banks.

DETERMINANTS OF BUYER POWER

- Majority of MFL's customers belong to rural and semi-urban areas. This is a segment that has lesser no. of players and the customers have low reach to financial institutions. Thus the power of customers is considerably low.
- Magma's separate credit vertical and internal loan appraisal filter help it in selecting credit-worthy customers.

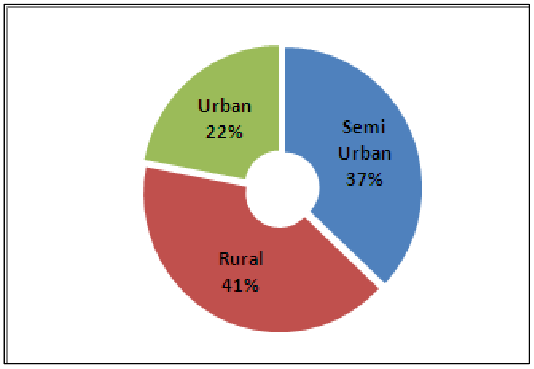
THREAT OF SUBSTITUTE PRODUCT

- MFL has a diverse product portfolio, which very few players in the NBFC space offer.
- However, banks are present in this segment, albeit in primarily urban markets, where the loans are offered at a lower than MFL's rate.

Investment Rationale

Broad spectrum of services offered to a specific customer segment

- MFL offers a broad spectrum of services viz. Consumer Vehicle (CV) Finance, Construction Equipment (CE) Finance, Car & utility vehicle finance, Used car finance (Suvidha Finance), SME loans, Tractor Finance and Insurance services.

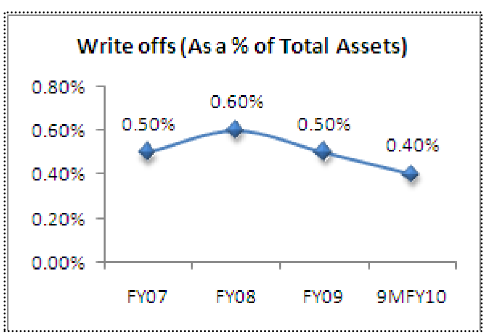


- The company offers its services to the rural and semi urban population, which is more than 70% of the population.
- A major portion of MFL's customers comprise of first time buyers and entrepreneurs, who do not have access to banks, or have been denied financing by banks due to lack of track record.
- Magma strategically focuses on under banked rural and semi urban population, using its strong network, thereby ensuring minimum competition from the established players like banks and competitors viz. Sundaram Finance and Shriram Transport Finance.

Extensive network and strategic tie-ups with auto manufacturers and OEM

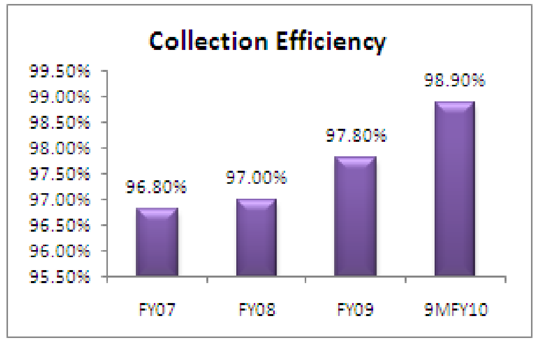
- MFL has 150 branches spanning across 20 states and 1 Union Territory. The company covers almost the whole of the country except, J&K and the North East regions.
- Magma has entered into tie ups with M&M, Tata Motors, Ashok Leyland, MUL, GM, HMIL, Telcon, JCB, ACE, TIL, BEML, Terex Vectra, TAFE etc. to finance their vehicles/products. This provides MFL with an access to a large captive customer base.
- The company reduced the number of branches from 161 in FY08 to 150 in FY09, in order to rationalize the rental and administrative costs. However, going forward, MFL is expected to increase the branch size, once the company increases its presence in the southern and western parts of the country.

Best in class collection mechanism resulting in lowest NPA in the industry



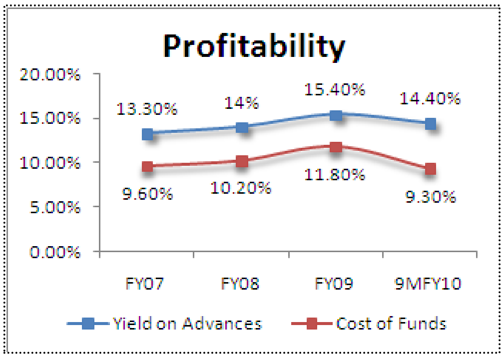
- In FY09, Magma had zero NPA on its books. The write offs also went down from 0.7% of loans in FY08 to 0.6% in FY09.
- For 9MFY10, the write offs further reduced to 0.4% of the total asset base.

- MFL had collection efficiency of 97.8% in FY09, and 98.9% for 9MFY10. Such strong collection process ensures that the NPA and write offs are kept at a minimum.



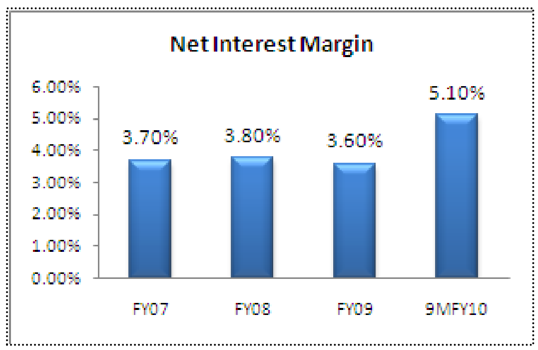
- The company has segregated delinquencies into brackets of 0-60 days, 61-180 days and more than 180 days. This helped MFL to make a detailed analysis and understanding of the receivables, which in turn, helped the company to keep a tab on the write offs and NPAs.

Shifting to high yield products to result in better profitability



- The share of high yield products in MFL's product portfolio has gone up to 13.5%, and this figure is expected to go up in future.

- High yield products like SME loans, Suvidha Loans and Tractor Loans enhance the overall Net Interest Margins (NIM) of the company.



Specialized verticals resulting in better operational efficiency

- MFL has segregated business vertical from the credit vertical, ensuring better focus and operational efficiency.

- Magma also introduced an additional loan appraisal filter during FY09-10, thus bolstering the internal credit analysis of the company.

- The segregation of business from the credit vertical also meant that the credit team became the single point sanctioning authority. This helped the company in maintaining a low Turn Around Time (TAT) for processing of credit disbursals during the period.

Financial Performance

Latest Results Update

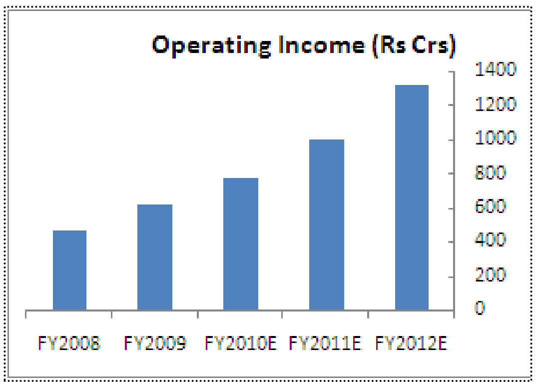
- In Q3FY10, the topline of MFL expanded by 15.5% to Rs 182.02 crore, while the bottomline swelled by 161% to Rs 17.93 crore.

- The disbursals for Q3FY10 stood at Rs 1049 crore, which is 19% higher than the corresponding figure of Rs 883 crore in Q3FY09. The disbursals also went up 18% sequentially on a Q-o-Q basis, against Q2FY10 figure of Rs 892 crore.

- For 9MFY10, topline expanded by 12.3% to Rs 505.91 crore from Rs 450.48 crore in the corresponding period, while the bottomline expended by 38.9% to Rs 44.95 crore, against Rs 32.36 crore in 9MFY10.

- For 9MFY10, the disbursements stood at Rs 3170 crore, while the total AUM was at Rs 9390 crore.

Operating Income: In the period FY2006-09, MFL registered a CAGR of 102.46% in Operating Income. **However, going forward, for the period FY2010-12, we expect the company to register CAGR of 35.68% in Operating Income.**

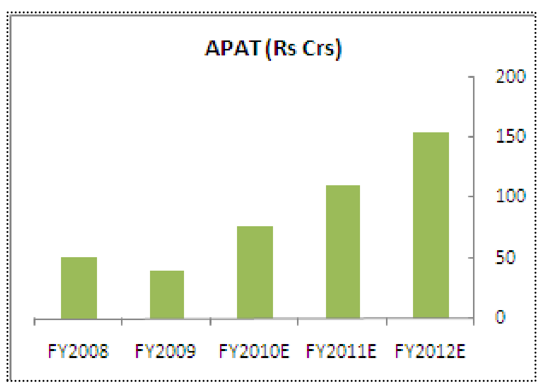


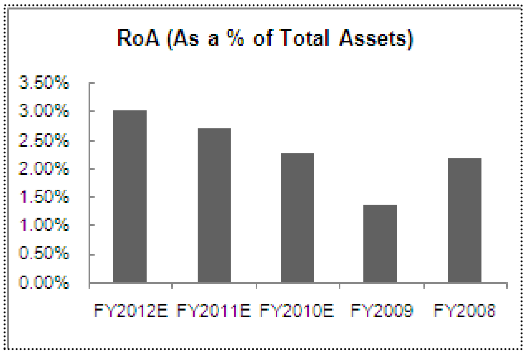
- The rise in Income from Leasing is going to drive the surge in Operating Income for the next few years.

- The SME Loans segment is expected to contribute substantially more in FY11 & FY12, from the current contribution level of 5%.

APAT: Magma had an APAT CAGR of 31.62% during FY2006-09. **However, we expect the company to achieve a CAGR of 61% during FY2010-12.**

- The enhancement in NIM is going to benefit the company in the next two years.



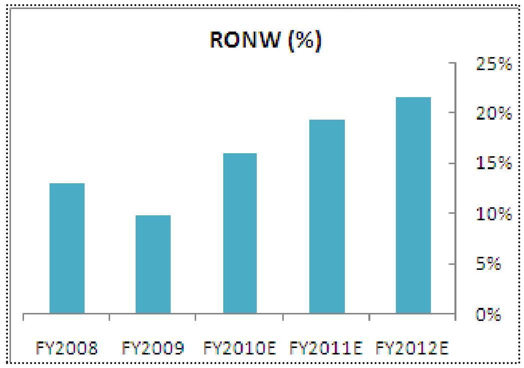


ROA: MFL had a RoA of 2.18% and 1.36% in FY08 and FY09 respectively.

- **Going forward, RoA is expected to be 2.01% in FY10, following which it is expected to be 2.63% and 2.95% in FY11 and FY12 respectively.**

RONW: MFL had RoNW of 12.86% and 9.65% in FY08 and FY09 respectively.

- **We expect the company to maintain RoNW of 14.37%, 18.9% and 21.36% in FY2010, FY2011 and FY2012 respectively.**



Concerns

- MFL's lending rates are 1-2% higher than that of the banks, as well as of competitors like Sundaram Finance. This may prove to be a hindrance in the fiercely competitive asset financing segment. However, MFL's presence in primarily semi urban and rural markets and catering to target customers who are financially disenfranchised, provide cushion to the apparent business risk.

- MFL is expected to grow at a better than industry growth rate, and topline growth will be a cornerstone of that growth. In order to do that, the asset quality may be compromised, which may prove to be a concern in future. However, separation of credit vertical from the business vertical and stringent internal credit analysis process will help MFL to mitigate that risk.

Outlook & Recommendation

- Increasing contribution from high yield advances, extensive branch network, strong collection mechanism and operational efficiency will bolster the growth in topline for MFL in future.

- **We recommend BUY rating on the stock with an 18 months target price of Rs 549, at 8x FY12 earnings, giving it an upside potential of 79% from the current levels.**

Financials (Consolidated) (in Rs. Crores)

Income Statement

Particulars	FY09	FY10E	FY11E	FY12E
Operating Income	621.03	768.70	994.16	1317.27
Growth (%)	*33.35%*	*23.78%*	*29.33%*	*32.50%*
Other Income	10.46	11.20	12.40	13.50
Total Income	*631.49*	*779.90*	*1006.56*	*1330.77*
Employees Cost	98.34	121.87	157.61	208.83
Interest & Fin. Charges	288.03	324.60	399.93	516.73
Operating & Adm. expenses	97.28	126.85	168.04	223.97
Misc. Expenses	52.56	70.29	93.39	127.03
Total Expenditure	*536.21*	*643.61*	*818.96*	*1076.57*
PBDT	95.28	136.29	187.60	254.20
PBDT %	15.34%	17.73%	18.87%	19.30%
PAT	39.85	67.29	106.41	149.39
PAT Margin (%)	6.41%	8.77%	10.71%	11.35%
Growth (%)	-20.80%	69.33%	58.04%	40.36%
O/S Shares (Crs)	2.178	2.178	2.178	2.178
EPS (Rs.)	14.79	30.90	48.86	68.59
PER (x)	10.72	9.90	6.26	4.46
Dividend Per Sh. (Rs.)	1.00	1.00	1.00	1.00

Balance Sheet

Particulars	FY09	FY10E	FY11E	FY12E
Share Capital	137.88	137.88	137.88	137.88
Reserves	274.75	331.26	425.71	561.96
Share Warrants	0.00	0.00	0.00	0.00
Net worth	*412.63*	*469.14*	*563.59*	*699.84*
Secured Loan	1987.23	2350.21	2921.99	3784.16
Unsecured Loan	521.20	540.20	570.20	590.20
Deferred Tax Liab.	50.52	58.72	63.22	69.62
Total Liabilities	*2925.24*	*3359.55*	*4055.78*	*5074.21*
Net Fixed Assets	238.20	267.22	320.58	386.58
Investments	29.04	37.75	49.08	63.80
Assets on Finance	2045.91	2557.39	3529.19	4940.87
Debtors	6.56	10.83	16.49	25.15
Cash & Bank	902.47	1372.51	1710.03	2789.91
Loan & Advances	130.32	288.50	445.84	647.81
Total Current Assets	*3085.26*	*4229.22*	*5701.56*	*8403.74*
Current Liab.	353.49	1085.25	1905.84	3638.95
Provisions	24.13	32.18	47.18	72.18
Total Curr. liab. & prov.	*377.62*	*1117.43*	*1953.02*	*3711.13*
Net Current Assets	2707.64	3111.80	3748.54	4692.61
Total Assets	*2925.24*	*3359.55*	*4055.78*	*5074.21*

Cash Flow Statement

Particulars	FY09	FY10E	FY11E	FY12E
Profit before Tax	61.04	96.91	142.32	199.86
Add: Depreciation, Int. & Other Expenses	275.58	312.98	384.46	495.17
Cash flow from operating activities	336.62	409.89	526.78	695.03
Capital expenditure	0.00	0.00	0.00	0.00
Cash flow from investing activities	-6.97	-77.11	-109.97	-135.06
Cash flow from financing activities	338.27	92.69	251.25	428.06
Net Increase/Decrease in Cash & Cash Equivalents	293.43	470.04	337.52	1079.89
Opening Cash Balance	609.04	902.47	1372.51	1710.03
Closing Cash Balance	902.47	1372.51	1710.03	2789.91

Key Ratios

Particulars	FY09	FY10E	FY11E	FY12E
Valuation Ratios				
P/E	10.72	9.90	6.26	4.46
P/Cash EPS	4.22	5.79	4.26	3.17
P/BV	1.16	1.42	1.18	0.95
EV/EBDTA	20.17	15.75	12.79	8.60
EV/Sales	3.46	2.50	1.98	0.57
Earnings Ratios				
PBDTM	15.34%	17.73%	18.87%	19.30%
NPM	6.41%	8.77%	10.71%	11.35%
ROCE	11.93%	12.55%	13.37%	14.12%
RONW	9.65%	14.37%	18.90%	21.36%
Balance Sheet Ratios				
Current Ratio	8.17	3.78	2.92	2.26
Debt/Equity	6.08	6.16	6.20	6.25
ROA	1.36%	2.01%	2.63%	2.95%
FA Turnover	1.63	1.71	1.82	1.97

Notes:

The above analysis and data are based on last available prices and not official closing rates.

SKP Securities Ltd (Member of NSE & BSE)

Analyst: Soumen Ghosh Tel:(033) 4007 7000, Ext. 7416 E- Mail: soumen.ghosh@skpmoneywise.com	Kolkata Office (Head Office) Tel: (033) 40077000 Fax: (033) 40077007 Email: research@skpmoneywise.com
Institutional Sales (Mumbai) Tel. (022) 22811015 ; Fax 2283 0932 E-Mail : dealingdesk@skpmoneywise.com skp.sec@bloomberg.net	

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