



Issue at a Glance

Issue Summary	
Total Issue of Shares (Cr)	5.15
QIB Investors (Cr)	1.80
Non -Institutional Investors (Cr)	0.77
Retail Investors (Cr)	1.80
Anchor Investor	0.78
Issue opens on	18 th Apr,2011
Issue closes on	21 st Apr,2011
Price Band (Rs.)	160-175
Lot size (No. of shares) and multiple	40
Face Value (Rs)	10.00
Issue Size (Rs in Cr.)	824- 901.25
Equity Shares outstanding prior to the Issue (Cr)	32.02
Equity Shares outstanding after the Issue (Cr)	37.17

Shareholding Pattern

	Pre-Issue (%)	Post- Issue (%)
Promoters and Promoter Group Holdings	93	80.12
Non Institution	7	-
Public	-	19.88
Total Share Capital	100	100

CARE & ICRA GRADING 4/5 indicating “Above Average Fundamentals”

CRISIL GRADING 4/5 indicating “Above Average Fundamentals”



Issue Objectives

Muthoot Finance Ltd (MFL) is coming out with an IPO of 5.15cr equity shares. This issue consists of 13.85 of the fully diluted post issue paid up equity share capital. The total share holding of promoter will reduce from 93% to 80.12%.

- **Muthoot finance wants to augment its capital base to meet future capital requirements and to provide funding of loans to its customers.**

Company Background

MFL is the largest gold financing company in India in terms of loan portfolio. It provide personal and business loans secured by gold jewellery, or Gold loans, to its customer who possess gold jewellery but could not access formal credit within a reasonable time or to those credit may not available at all, to meet unanticipated or other short term liquidity requirement. Their customers are basically small businessmen, vendors, traders, farmers, and salaried individuals. **Their gold loan portfolio as of on November comprised approximately 4.1 million loan accounts in India that are serviced through 2263 branches across India.**

MFL is a “Systematically Important Non- deposit taking NBFC” headquartered in Kerala. It has broadened its geographical scope of retail lending operations so that as of 31 March, 2010, **they were the largest Gold Financing Company in the country.** Apart from gold loan business they are also in money transfer services through their branches as sub-agents of various registered money transfer agencies, and recently have commenced providing collection agency services. They also operate three windmills in the state of Tamil Nadu.



Overview of MFL

Gold demand in India

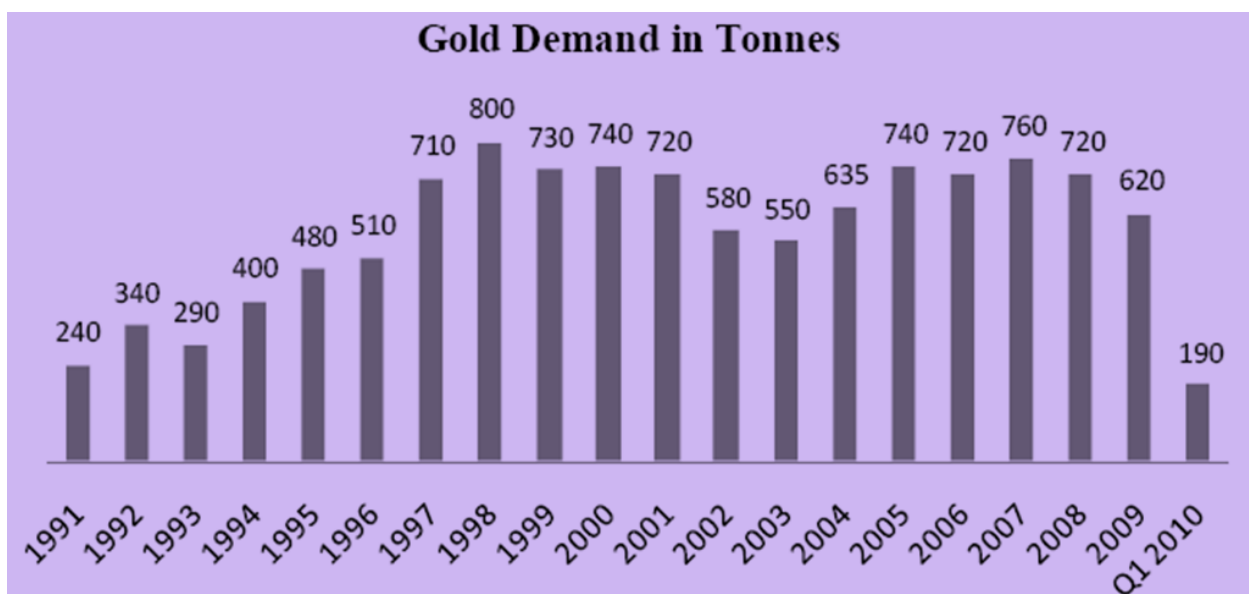
Demand is relatively price in-elastic: Demand for gold has not been affected by gold prices. Despite of surge in prices of gold during from Rs 15026 Rs to Rs 51150 per ounce during the period from 2002 to 2009, the demand for gold has risen from 580 tonnes in 2002 to 620 tonnes in 2009. (Source IMAcS Industry Report 2009)

South India has the largest market for approximately 40% of the gold demand. Rural India is estimated to hold around 65% of total gold stock because they consider gold as a secure and easily accessible savings vehicle.

Apart from growing organized gold loans market in India, there is a large long-operated, unorganized Gold Loans market which includes numerous pawnbrokers, money lenders and cooperative societies, operating primarily in rural India.

The southern region of India accounts for 85-90% of the Gold Loans market in India. Recently, large specialized NBFCs such as Muthoot Finance Ltd and Manappuram Finance have started expanding their businesses in northern and western India, and it is expected that there will be a gradual increase in the acceptability of Gold Loans product in these regions due to the concentrated marketing efforts of large NBFCs.

The following Chart illustrates gold demand in India.



Source DRHP



Gold finance Industry in India

India is one of the largest markets for gold and as of fiscal 2010, accounts for approximately 10% of the total world gold stock with an annual demand of approximately 700 tonnes.

Several gold based financial products have been made available to retail consumers in the Indian market from time to time with a view to bring the gold holdings to the core financial market. Lending against gold has been one of the most popular instruments based on gold, and it works well with the Indian rural population, which typically views gold as an important savings instrument that is liquid and can be into converted into cash instantly to meet their urgent cash requirements. Moreover, traditionally gold owners in southern India are more open than elsewhere in the country to accept and exercise the option of pledging gold to borrow money

Indian consumers have an affinity for gold that emanates from various social and cultural factors. Furthermore, the low level of financial inclusion and poor access to financial products and services make gold a safe and attractive investment proposition. In an effort to tap the market for gold related investment and services, companies in the financial sector have launched several products such as gold coins and bars; exchange traded gold funds and lending against gold. Gold Loans in India, have largely been concentrated in southern India, which holds the largest proportion of India's gold portfolio, and is typically more open to borrowing against gold as compared to consumers in the northern and western regions of India.

Gold Loans have emerged as key gold based financial products, and in the year ended March 31, 2010, the organized Gold Loans market in India was estimated at between Rs 350 billion and Rs 400 billion with a CAGR of approximately 40% during fiscal 2002 to fiscal 2010. Notwithstanding the above, the organized Gold Loans portfolio accounted for merely 1.2% of the value of total gold stock in India. The Gold Loans market is significantly under-penetrated and is expected to continue growing at the rate of 35-40% in the future.

(Source: IMAcS Industry Report 2010 and DRHP).



Drivers of Growth in Gold Loans Market in India

i. **Regulatory incentives to lenders: The prescribed risk weight on Gold Loans has been ~ 50% for commercial banks, further reducing the associated capital costs.**

ii. **Policy focus:** The Government of India views Gold Loans as an effective means to meet the potential micro- finance demand in India. In fiscal 2007, the Government of the state of Tamil Nadu set a jewellery loans target of Rs 60 billion (75% of the total loan disbursement target) for co-operatives in Tamil Nadu.

iii. **Increasing interest of the lenders in the segment: Considering the recent rise in default rates(expected to vary from 8-10% in fiscal 2009)** in personal loans, banks have started focusing on the Gold Loans segment because it offers attractive returns (although lower than personal loans) with very low levels of defaults. Several private sector banks have started participating in the segment by getting into bilateral sale agreements with NBFCs that specialize in Gold Loan. A few private sector banks have also initiated efforts to tap into such segments.

iv. **High levels of indebtedness:** The National Sample Survey Organization (NSSO) 2003 survey on situational assessment of farmers' indebtedness in the country has estimated that 60.4% of rural households in India were farmer households, out of which 48.6% were indebted. The incidence of indebtedness was highest in the state of Andhra Pradesh (82%) followed by Tamil Nadu (74.5%), Punjab (65.4%), Kerala (64.4%), Karnataka (61.6%) and Maharashtra (54.8 %)

v. **Changing customer attitudes and preferences:** Indian customers have demonstrated a change in their traditionally debt-averse psychology, promoting the creation of assets through growth in financial liabilities which has been reflected in an annual growth of more than 30-35% in retail credit between fiscal 2002 and fiscal 2009.

(Source: IMAcS Industry Report 2009).



MFL's Competitive Strengths

- 1) **Market leading Position in the gold loan business with a strong presence in under- served rural semi urban Markets:** Gold loans are the core products in asset portfolio.
 - It is the largest gold financing company in India in terms of loan portfolio.
 - It has the largest branch network among gold loan NBFCs
 - Due to early entry it has built a recognizable brand in semi-urban rural markets of India particularly in southern India.
 - It offers Products varying loan amounts, advance rates (per gram of gold) and interest rates.

- 2) **Strong brand name, track record, management expertise and Promoter support:** The management team has extensive experience in the Gold Loan industry. A strong brand name has contributed to their ability to earn the trust of individuals who entrust them with their gold jewellery, and will be a key in allowing them to expand their growth and consolidate this fragmented industry across India.

- 3) **High quality customer service and short response time:** It provides its customers a clean, attractive and secure environment to transact their business with it. Each of the branches is staffed with persons with local knowledge and understanding of customers.

- 4) **Strong fund raising ability:** It has a track record of successful raising capital from various sources. It regularly issued redeemable non convertible debentures to retail investors on a private placement basis as a means to access capital for its gold Loan business. It has also issued shares in three tranches to institutional investors.



MFL's Business Strategy

1. **Expand branch network and visibility to maintain our leadership position:** MFL intend to continue to grow its loan portfolio by expanding its network through the addition of new branches. Expansions are taken care by assessing potential markets by analyzing demographic, competitive and regulator factors. Its strategy for branch expansion includes further strengthening its market leading position in southern India to enhance its presence in other regions of India.
2. **Target new Customer Segments:** The market for its loan products was traditionally confined to lower and middle income groups, who viewed Gold loans as an option of the last resort in case of emergency. It planned to work to position gold Loans as a “Lifestyle product” and expand its customer base to include upper-middle income and upper income groups.
3. **Access low cost and diversified sources of funds:** It source its funds for its Gold Loan business primarily from the proceeds of private placements of debentures in India and from secured and unsecured credit facilities from banks and other financial institutions. In addition, it intends to expand its program of selling a portion of its receivables under various bilateral assignment agreements with financial institutions. It may also consider the possibility of concluding rated securitization transactions in the future. It intends to increase the levels of its capital adequacy ratios in excess of regulatory requirements and strengthen its balance sheet with a view to have access to other sources of low-cost funds. Furthermore, it also intends to seek strong investments in MFL as another source of funding to expand its business.
4. **Strengthen its operating processes and risk management systems:** Risk management forms an integral part of its business as it is exposed to various risks relating to Gold Loan business. The objective of its risk management systems is to measure and monitor various risks that are subject to and to implement policies and procedures to address such risks. It intends to continue to improve its operating processes and risk management systems that will further enhance its ability to manage the risks.



Risks & Concerns

- 1) MFL requires substantial capital and any disruption in funding sources would have material adverse effect on our liquidity and financial condition.
- 2) MFL had negative cash flows from operating and investing activities in the last three fiscal years and may continue to do in the future.
- 3) MFL profitability would be affected if there is sustainable fall in gold prices.
- 4) MFL is exposed to greater interest rate risk than banks or deposit taking NBFCs. In arising rate environment, if the yield on its interest- earning assets does not increase at the same time or to the same extent as its cost of funds, or in a declining interest rate environment and vice versa.
- 5) MFL branches are concentrated in southern India and any disruption or downturn in the economy of the region would adversely affect its operations.
- 6) MFL gold loans are due within one year of disbursement and a failure to disburse new loans may result in a reduction of its loan portfolio and a corresponding decrease in its interest income.
- 7) MFL face difficulties in carrying out credit risk analyses on its customer, most of those are individual borrowers.
- 8) MFL handle high volume of cash and gold jewelry in a dispersed network branches , these are exposed to operational risks, including employee negligence, fraud, petty theft, burglary and embezzlement, which could harm our results of operations and financial position.
- 9) MFL may experience difficulties in expending business into additional geographical markets in India.
- 10) MFL ability to borrow from various banks may be restricted an account of guidelines issued by the RBI imposing restrictions on banks in relation to its exposure to NBFCs.
- 11) MFL do not own its branches of operation it has only 14 branches offices which are owned by it.



Financials

Consolidated Summary Statement of P & L

(Rs in Cr)

Particulars	Mar 31, 2008	Mar 31, 2009	Mar 31, 2010	8M Dec 31, 2010
Total Operating Income	368.64	620.40	1089.38	1301.66
Total Operating Expenditure	84.45	152.58	255.21	267.49
Operating Profit	284.19	467.82	834.17	1034.17
Depreciation	7.41	9.88	14.89	10.50
PBT	96.98	148.17	345.55	441.12
Tax	33.38	50.45	117.98	149.63
Net Profit	63.60	97.72	227.58	291.48
Basic EPS (Rs)	127.19	19.94	7.56	9.10
Diluted EPS (Rs)	-	-	6.12	7.84



Consolidated Summary Statement of Balance Sheet

(in Rs Cr)

Particulars	Mar 31, 2008	Mar 31, 2009	Mar 31, 2010	8M Dec 31, 2010
LIABILITIES				
Share Capital (A)	5.00	49.00	301.00	320.21
Reserves and Surplus (B)	217.36	321.23	283.55	811.51
Less : Miscellaneous Exp (D)	9.25	8.78	0.35	0.27
Net worth E(A+B+C-D)	213.11	361.45	584.19	1131.45
Loan Funds Secured(F)	1915.31	3165.59	5280.53	9082.92
Total G(E+F)	2128.41	3527.04	5864.72	10214.38
ASSETS				
Gross Block	121.53	148.27	169.11	203.46
Less: Depreciation	22.27	32.08	449.04	55.40
Net Block (H)	99.25	116.19	124.21	148.05
Capital Work in Progress (I)	9.36	13.12	29.07	51.04
Investments (J)	18.34	8.53	7.51	7.51
Net Current Assets (K)	2005.63	3392.99	5706.42	10010.22
Less Deferred Tax Liability (Net) (L)	4.17	3.79	2.48	2.44
Total M (H+I+J+K+L-M)	2128.41	3527.04	5864.72	10214.38



Financial performance snapshot

		FY08	FY09	FY10
Gold AUM (including assignments)	Rs mn	21,790	33,001	73,417
Gold volume pledged	tons	30	39	68
Interest income	Rs mn	3,579	6,062	10,775
Interest expense	Rs mn	1,798	3,098	4,737
Net interest income	Rs mn	1,781	2,965	6,037
Other income	Rs mn	107	142	119
Net profit	Rs mn	636	977	2,276
Adjusted EPS	Rs	2.6	3.5	7.6
Adjusted equity shares	mn	246	280	301
Net worth	Rs mn	2131	3614	5842
Adjusted book value	Rs	8.7	12.0	19.4
RoE	%	34%	34%	48%
RoA	%	3%	3%	5%
Gross NPA	%	0.42%	0.48%	0.46%
CRAR	%	12.6%	16.3%	14.8%
Tier I capital	%	10.6%	12.5%	9.9%

Source: DRHP



Table 9: Key Financial Ratios

KEY RATIOS	Sep-10	Mar-10	Mar-09	Mar-08	Mar-07
Yield on Average Loans	18.51%	19.42%	21.13%	19.00%	19.45%
Yield on Average Earning Assets	17.47%	17.15%	17.59%	17.44%	18.43%
Cost of Average Interest Bearing Funds	8.99%	8.41%	9.79%	9.43%	8.80%
Lending Spreads	9.51%	11.01%	11.34%	9.57%	10.65%
Gross Interest Spread	8.47%	8.74%	7.80%	8.01%	9.62%
PROFITABILITY RATIOS					
Interest income /AMA	17.03%	16.54%	16.72%	16.35%	17.17%
Interest Expense / AMA	7.83%	7.27%	8.48%	8.13%	7.57%
Net Interest Margin /AMA	9.20%	9.27%	8.24%	8.22%	9.60%
Non- interest income/ AMA	0.14%	0.18%	0.24%	0.32%	0.54%
Operating expenses / AMA	3.61%	4.10%	4.43%	4.12%	5.03%
Operating Profit / AMA	5.73%	5.35%	4.05%	4.41%	5.11%
Credit Prov. & Write-offs /AMA	0.03%	0.04%	0.02%	0.03%	0.01%
PAT/ AMA	3.76%	3.49%	2.68%	2.88%	3.33%
PAT / Average Net worth	48.83%	48.08%	33.90%	34.01%	35.12%
Cost Income Ratio	38.69%	43.42%	52.26%	48.32%	49.63%

Source: MFL financial statements and ICRA research

	Mar	Mar	Mar	8M Dec
Particulars	31, 2008	31, 2009	31, 2010	31, 2010
Capital Adequacy Ratio	12.56%	16.30%	14.79%	15.06%

Valuation & Outlook

MFL's P/B ratio is currently at 4.95x multiples on the higher band of IPO price & 4.52 x on lower end of IPO price. The Book value of MFL is Rs 35.33 as on 30th Nov, 2010.

Peer Group Comparison

Company	PAT		FV	CMP	EPS	PE	BV	P/BV	RoNW (%)
	8/9MFY11	FY10			8/9MFY11		Latest		FY10
Manappuram General Finance & Leasing	180.86	119.72	2	129.85	4.34	22.43	41.08	3.16	30.93
Muthoot Finance Ltd	291.48	227.58	10	160.00	9.10	11.72	35.33	4.53	39.12
Muthoot Finance Ltd	291.48	227.58	10	175.00	9.10	12.82	35.33	4.95	39.12

P/E ratio for both companies are calculated by annualising 8/9 months FY11 EPS,

(Source:RHP, Capitaline Database)



Investment Rationale

- ❖ MFS's is a market leader in the segment with strong presence in almost 2000 places. And highly under-penetrated domestic market for loans against gold ornaments (LAG) and increasing market share of organized players augur well for Muthoot Finance Ltd.
- ❖ Company has implemented the robust operational systems and processes resulting in quick disbursement of loans, giving it a competitive edge over banks.
- ❖ The average RONW in the last three years is 34%. And gross non-performing assets NPAs level is have remained below 0.5%.
- ❖ Private equity players Baring, Citigroup and Credit Suisse have invested money in the company
- ❖ Given the expected GDP growth and appetite for gold in the country, the company is likely to witness growth in the years to come.

“Investors with high risk appetite can **Subscribe for listing gains”**

**Disclaimer:**

This document is not for public distribution and has been furnished to you solely for your information and must not be reproduced or redistributed to any other person. Persons into whose possession this document may come are required to observe these restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. It is for the general information of clients and Associates of arm research. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. We have reviewed the report, and in so far as it includes current or historical information, it is believed to be reliable though its accuracy or completeness cannot be guaranteed. Neither arm research, nor any person connected with it, accepts any liability arising from the use of this document. The recipients of this material should rely on their own investigations and take their own professional advice. Price and value of the investments referred to in this material may go up or down. Past performance is not a guide for future performance. Certain transactions -including those involving futures, options and other derivatives as well as non-investment grade securities - involve substantial risk and are not suitable for all investors. Reports based on technical analysis centers on studying charts of a stock's price movement and trading volume, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein. We and our affiliates, officers, directors, and employees may: (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or act as advisor or lender / borrower to such company (ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report. No part of this material may be duplicated in any form and/or redistributed without arm research's prior written consent.