

March 09, 2011
Mumbai

CRISIL Equities assigns IPO grade 4/5 to Muthoot Finance Limited

CRISIL Equities has assigned a CRISIL IPO grade of "4/5" (pronounced "four on five") to the proposed initial public offer (IPO) of Muthoot Finance Limited (Muthoot Finance). This grade indicates that the fundamentals of the IPO are above average relative to other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to the issue fundamentals. The grade is not a recommendation to buy, sell or hold the graded instrument, or a comment on the graded instrument's future market price or its suitability for a particular investor.

The assigned grade reflects Muthoot Finance's leadership position in the gold financing business in terms of assets under management (AUM) backed by a wide branch distribution network. It enjoys a strong brand name especially in South India. A highly under-penetrated domestic market for loans against gold ornaments (LAG) and increasing market share of organised players augur well for Muthoot Finance. The company's promoters have decades of experience in the industry and have shown the ability to manage aggressive expansion and growth in AUM. Also, Muthoot Finance's first-mover advantage in the non-southern regions of India will support its growth plans over the medium term. It has shown the ability to maintain strong underwriting norms with a comfortable loan to value ratio (LTV). Further, emotional attachment of the customer to household ornaments has resulted in strong asset quality. It has implemented robust operational systems and processes resulting in quick disbursement of loans, giving it a competitive edge over banks.

However, the grade is moderated by the company's dependence on a single line of business and its largely South India focus (~75% of AUM in FY10). Also, competition is expected to increase with the entry of many players, which is expected to lower yields. A sharp drop in gold prices and restrictive measures by regulators may pose challenges and remain the key monitorables for the industry.

About the company and the issue

Headquartered in Kerala, Muthoot Finance Ltd is a non-deposit taking 'systemically important' non-banking finance company (NBFC) incorporated in 1997. It is primarily in the business of lending against used household gold jewellery to individuals. Muthoot Finance's operating history has evolved over a period of 70 years since Mr M George Muthoot (the father of the present promoters) founded a gold loan business in 1939 under the trading business (under partnership firm) established by his father, Ninan Mathai Muthoot, in 1887. In 2001, Muthoot Finance received the NBFC licence from the RBI.

It has the largest branch network among gold loan providers in India with 1,605 branches and a strong presence in the under-served rural and semi-urban markets. In 2010, it received a fund infusion of Rs 2.5 bn from private equity players like Baring India Private Equity, Matrix Partners India, Kotak India Private Equity Fund and Wellcome Trust for a 6% stake in the company. In 2011, Wellcome Trust picked up an additional 1% stake from the promoters, taking the total stake of private equity investors to 7%.

During FY06 to FY10, Muthoot Finance's AUM increased at a CAGR of 74% driven by the rise in pledged gold and a spurt in gold prices. It reported gross AUM of Rs 74 bn and PAT of Rs 2.3 bn on a total income of Rs 11 bn in FY10. The average yield on the AUMs during the same period was 19.9%. In FY10, while asset quality remained strong with gross NPA of only 0.46%, the capitalisation level was comfortable with a capital adequacy ratio of 14.8%.

Muthoot Finance will utilise the IPO proceeds to augment its capital base to meet future capital requirements for funding of loans to customers as well as general corporate expenses. The amount to be used for the above purposes was not disclosed at the time of the grading.

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Last updated: 01 January, 2010

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