

August 6, 2019

IPO Note

Key Financials - Standalone

Y/e Mar	2017	2018	2019
Net Int.Inc. (Rs m)	2,277	3,555	6,852
Growth (%)	6.2	56.2	92.7
Op. Profit (Rs m)	1,335	2,473	5,188
PAT (Rs m)	4,329	1,879	3,119
EPS (Rs.)	216.93	42.52	52.92
Gr. (%)	318.1	-80.4	24.5
Margin (%)	17.5	15.0	16.4
RoAE (%)	79.8	16.2	19.0
RoAA (%)	35.2	8.4	8.2
PE (x)	11.8	27.3	16.4
P/BV (x)	5.5	3.7	2.7

IPO Fact Sheet

Opening Date	August 5, 2019
Closing Date	August 7, 2019
BRLMs	Axis Capital, ICICI Sec.
Issue Size	12009mn
Fresh Issue (mn share)	4000
Offer for Sale (mn share)	9.36

Issue Details

Post-issue Market Cap (Rs bn)	54.9-55.0
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Shareholding Pattern

(%)	Pre-Issue	Post-Issue
Promoters	81.2	62.6

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Turnaround play

Spandana Sphoorty Financial Ltd (SSFL) is India's fourth largest NBFC-MFI with AUM of Rs 44bn headquartered in Hyderabad. Promoted by Padmaja Gangireddy (MD) and Kangchenjunga (Kedaara Capital), SSFL specializes in MSE financing for low-income women borrowers. With systematic expansion of geographic footprint to tap the underserved high potential rural segment, SSFL'S business model follows client centric approach.

We do laud company's successful exit from corporate debt restructuring (CDR) mechanism in Mar'17 and expect growth trends to slow at 20-25% annual momentum. While there remains sufficient scope to improve on elevated GNPA at ~8%, cost of funds at 13.5% and opex to assets at 4.5%, we remain cautious given tough macros and the credit risks associated with the MFI industry. Besides, SSFL's has 54% exposure to Odisha, Karnataka and MP, which adds risk to credit profile. Improvement in credit profile post IPO will likely reduce funding costs aiding NIM sustenance while further reduction in NPAs (current 7.9%) can stabilize operations. At higher end of price band of Rs856, issue is priced at 2.0x BV (Post IPO) FY20 which stands at discount to closest peer, i.e., Credit Access Grameen at 2.6xP/ABV, but higher to peers like Equitas SFB at 1.3x, Ujjivan SFB at 1.6x and Satin Credit at 0.9x. We see limited listing gains given the weak market environment; we recommend to SUBSCRIBE FOR LONG TERM.

- AP woes behind; concentration risks stay:** SSFL successfully bucked Andhra Pradesh (AP) Ordinance (FY11) and demonetization (FY17) which severely affected the collection efficiencies of MFI players. However, with 54% business dominance in states of Karnataka, MP, Orissa, the business remains susceptible to politico-economic risks. Moreover, a competitive business environment and opex intensive model (opex/AUM: 4.5%) would make its product diversification strategy (currently income generation loans comprise 84.6% of overall JLG loans) a daunting task.
- Strong business momentum— Wait and watch:** Post CDR exit, SSFL recorded robust 143% YoY AUM growth for FY18 followed by 40% AUM growth in FY19 to Rs44bn. While current equity infusion should support management's aspiration of 4 times AUM expansion over next 4-5 years, the elevated growth rates (57% CAGR FY17-FY19) may not be maintained. Market challenges would result in more moderate growth. While company maintains strategy of no district contributing more than 2.5% to overall loans, beyond home turf expansion stands imminent. Against this backdrop, and macros coming to play, we expect 25% AUM CAGR ahead.
- Profitability indicators improve; Sustenance key:** SSFL's profitability was impacted in the past due to high credit costs post the AP crisis. While it has improved on parameters like AUM growth (52% CAGR), cost of borrowing declined from 16.3% to 12.3% and PAR (zero DPD) decreased from Rs1391mn to Rs383mn over FY17-19 increasing RoE to 18%+. Going ahead, high return profile maintenance is subject to higher business growth, which looks difficult.
- View:** While the comparative valuations post dilution are in-line with industry, SSFL is in the turnaround stage with greater scope for improvement on operating metrics. We believe Credit Access Grameen stands as a better play in the MFI space with improved processes, steady asset quality and higher business visibility.

Company Background

Headquartered in Hyderabad, Spandana Sphoorty Financial Limited, rural focused NBFC-MFI is promoted by Padmaja Gangireddy (MD) and Kangchenjunga (Kedaara Capital) specializing in MSE financing for low-income women borrowers. Incorporated in 2003, the company registered as NBFC with RBI in 2004 and subsequently as NBFC-MFI in 2015. In October 2010, like other players, Spandana was also sorely impacted due to Andhra Pradesh Microfinance Ordinance. It severely impacted its collections and cash flows denting its growth and profitability which resulted in lenders referred it to Corporate Debt Restructuring (“CDR”) to develop a plan to fortify its business. With cash-flow relaxations under CDR, Spandana gathered arsenal to diversify portfolio, improve processes, rationalize costs and retain customers which resultantly turned profitable in FY14. Also, collections from beleaguered AP portfolio, profits outside home turf states and capital infusion from promoter entities enabled Spandana successfully exit CDR mechanism in FY17.

The company is spearheaded by Ms Padmaja Gangireddy, Managing Director with 24 years of experience in social development and microfinance sector. CFO Sudhesh Chandrasekar has had previous assignments with Unitus Capital and ICICI Bank.

The company follows the contiguous expansion of geographic footprint and network of branches to tap the underserved high potential rural segment. Operating at 929 branches across 16 states and 1 union territory in India and employees around 7062 employee strength, SSFL’s 94.6% portfolio stands located in rural areas. Providing income generation loans that form 84.6% of AUMs (FY19) through JLG model, SSFL’s business model encompasses client-centric approach and focus on internal controls backed by promoter and core management team expertise. With a typical bi-weekly/monthly based repayment model, the avg. loan size of these income generation loans stand at Rs 26,000 spread across tenure of 12-36 months carrying interest rate of 25% (24%+1% processing fees). Besides, the company engages in providing loan against property, gold loans, working capital loans and top-up loans to existing borrowers.

Key concerns

Nature of business: The unsecured nature of microfinance loans stands susceptible to various operational, credit and political risks which may result in increased levels of NPAs for the company. Moreover, women centric borrowers in rural Areas typically have limited sources of income, savings and credit histories and as a result, are usually adversely affected by declining economic conditions. Also with limited or negligible collateral, the credit risks augmentation could stand higher for SSFL.

Portfolio concentration: Business Operations of SSFL stand concentrated in the states of Karnataka, Madhya Pradesh, Orissa at 20.01%, 19.98%, 13.48% respectively. In the event of regional economic slowdown, political upheavals, state level disturbances or natural calamity, SSFL may experience an adverse impact on its business operations and cash flows.

Operational processes: SSFL takes support of credit bureau reports to check certain background information such as the total indebtedness of each potential client and her existing repayment/ default history. Such data fails to capture complete borrower leverage position, assessment of borrower indebtedness from informal sources and misrepresentation of information. These uncertainties associated with the inherent customer profile pose credit risks for the business ahead. Said that, company has implemented standardized systems and a front-end interface that gives real time information on demand and collections at branch level.

Exhibit 1: Issue Details

Issue Opens	Issue Opens On: Monday, August 5, 2019
Issue Closes	Issue Closes On: Wednesday, August 7, 2019. The Anchor Investor Bidding Date shall be on 2nd August, 2019
Issue Details	Fresh Issue of Equity Shares aggregating upto Rs.400 Cr + Offer for Sale of upto 9,356,725 Equity Shares
Issue Size (Rs. Cr)	Rs.1,198.13~ Cr – Rs.1,200.94^ Cr
Face Value	Rs10 per share
Price Band	Rs.853 – 856
Bid Lot	17 Equity Shares and multiple thereof
Issue Structure :	
QIB	50% of the offer (7,023,027~ - 7,014,810^ Equity Shares) (Rs.599.06~Cr - Rs.600.47^ Cr)
NIB	15% of the offer (2, 106,909~ - 2,104,444^ Equity Shares) (Rs. 179.72~Cr - Rs.180.14^ Cr)
Retail	35% of the offer (4,916,120~ - 4,910,368^ Equity Shares) (Rs.419.35~Cr -Rs.420.33^ Cr) ~ Lower Price Band and ^Upper Price Band
GCBRLMs	Axis Capital, ICICI Securities, IIFL Holdings, JM Financial
BRLMs	IndusInd Bank, Yes Securities

Source: Company

Exhibit 2: Shareholding of promoters post dilution

Shareholding of the Promoters and Promoter Group:	Pre-Offer		No. of shares Offered	Post Offer	
	No. of Equity shares held	% of total equity share capital		No. of Equity shares held	% of total equity share capital
Kangchenjunga	11,670,067	19.6	1,423,114	10,246,953	15.9
Padmaja Gangireddy	35,270,269	59.1	5,967,097	26,452,702	45.6
Vijaya Siva Rami Reddy Vendidandi	1,491,483	2.5	796,509	314,483	1.1
Total	48,431,819	81.2	8,186,720	37,014,138	62.6

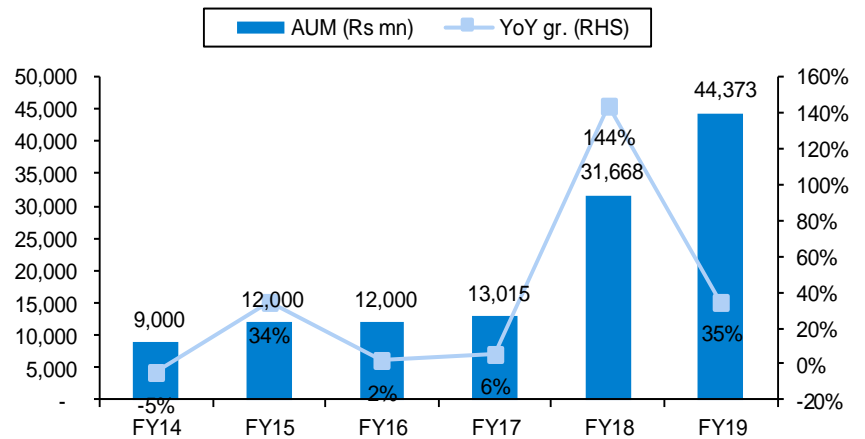
Source: Company

Exhibit 3: Current Shareholding pattern

Kangchenjunga Ltd	59.1%
Padmaja Gangireddy	19.6%
Valiant Mauritius Partners	7.8%
JM Financial India Trust	5.6%
Vijaya Siva Rami Reddy	2.5%
Helion Venture Partners	1.3%
Kedaara AIF	1.3%
Helion Venture Partners LLC	1.2%
JM Financial Products Ltd	91.0%
Spandana Employee welfare trust	0.5%
Others	0.3%

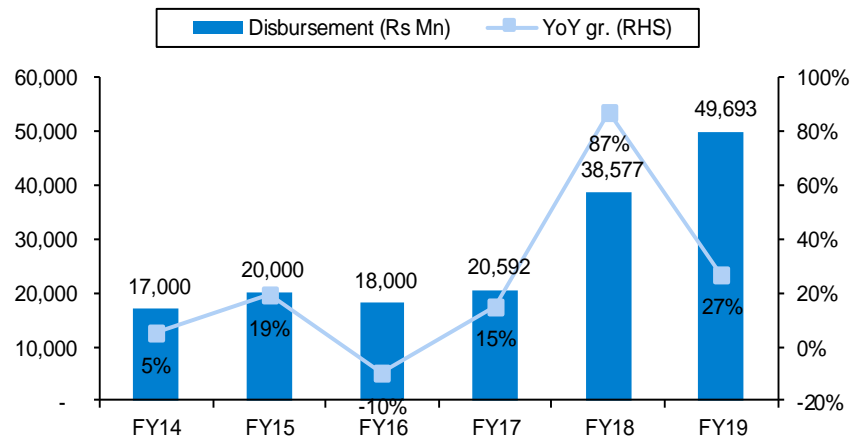
Source: Company

Exhibit 4: Volatile AUM growth



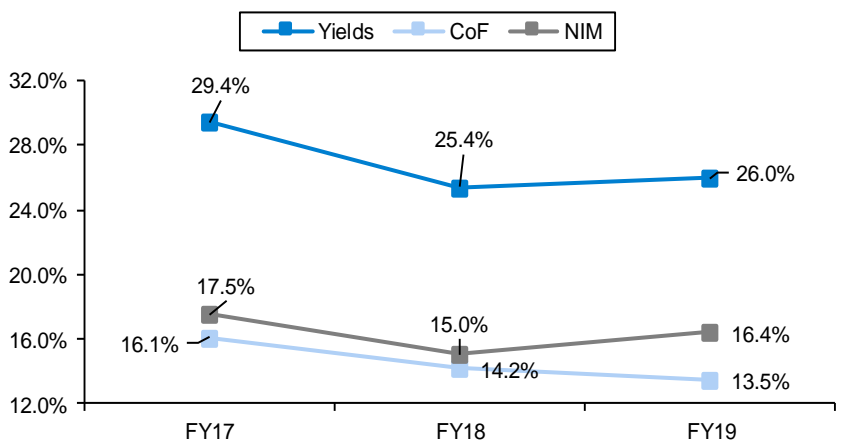
Source: Company, PL

Exhibit 5: ...backed by steady disbursements growth



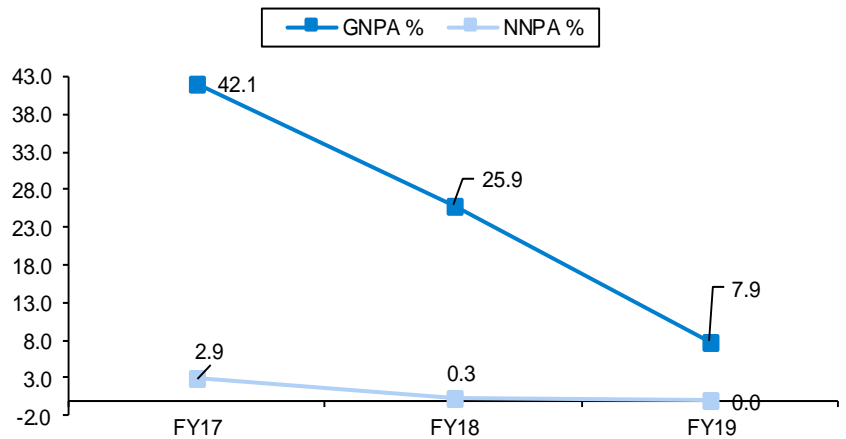
Source: Company, PL

Exhibit 6: Heathy margin performance



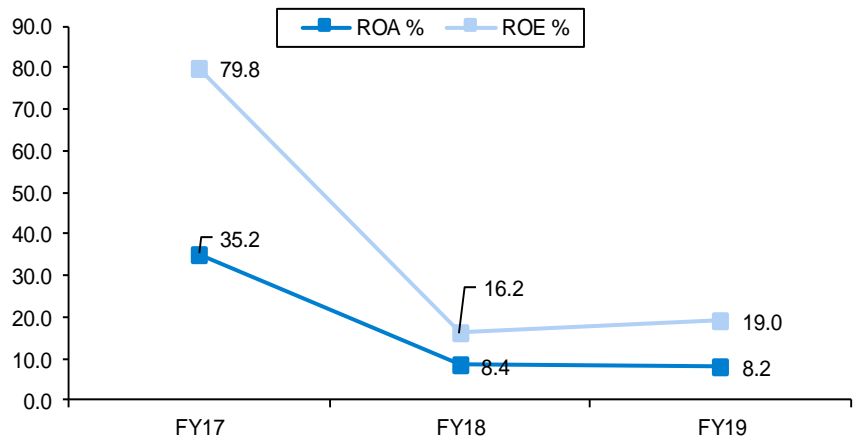
Source: Company, PL

Exhibit 7: GNPA's on declining mode; yet high vs industry standards



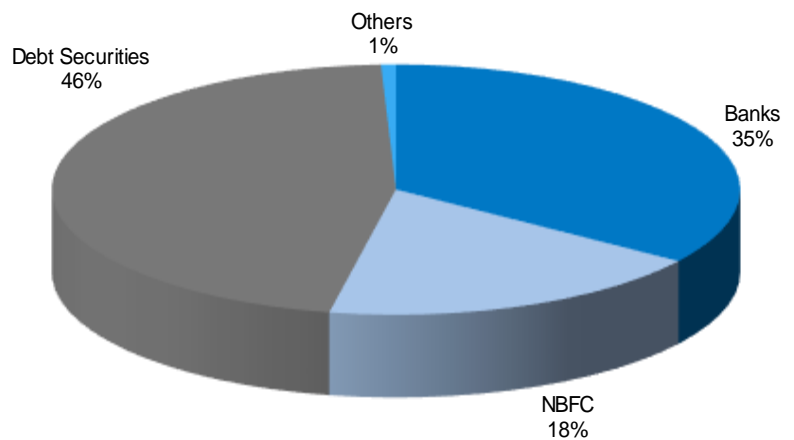
Source: Company, PL

Exhibit 8: Rich return profile



Source: Company, PL

Exhibit 9: Balanced borrowing mix



Source: Company, PL

Exhibit 10: Geography AUM Mix

State-wise	FY17	FY18	FY19
Orissa	22.25%	18.75%	19.98%
Madhya Pradesh	20.94%	22.00%	20.01%
Karnataka	18.30%	22.33%	13.48%
Maharashtra	13.38%	13.79%	10.77%
Chhattisgarh	9.27%	7.43%	8.70%
Andhra Pradesh	3.36%	3.62%	6.73%
Kerala	3.47%	3.17%	4.53%
Jharkhand	3.83%	3.65%	4.41%
Gujarat	2.80%	2.93%	3.17%
Bihar	0.01%	0.39%	2.58%
Rajasthan	0.00%	0.02%	2.21%
West Bengal	1.00%	0.86%	1.17%
Goa	0.77%	0.66%	0.90%
Telangana	0.16%	0.15%	0.66%
Uttar Pradesh	0.46%	0.24%	0.62%
Pondicherry	0.00%	0.00%	0.06%
Tamil Nadu	0.00%	0.00%	0.03%

Source: Company, PL

Exhibit 11: Peer Comparison

	Standalone / Consolidated	Face Value	Closing Share price as on 29.03.2019	Net Profit in Mn	Net worth in Mn	EPS	NAV	P/E (Basic)	RoNW (%)
Spandana Sphoorty Financial Ltd*	Consolidated	10	-	3,119	18,894	53.5	316.8	16.01~	16.5%
Bharat Financial Inclusion Ltd	Standalone	10	1,131.8	9,846	42,246	70.4	301.3	16.1	23.3%
Satin Creditcare Network Ltd	Consolidated	10	364.9	2,015	11,494	41.7	235.0	8.8	17.5%
Ujjivan Financial Services Ltd	Consolidated	10	348.0	1,504	18,777	12.4	155.0	28.0	8.0%
Bandhan Bank Ltd	Standalone	10	525.0	19,515	112,017	16.4	93.9	32.1	17.4%
Bajaj Finance Ltd	Consolidated	2	3,024.9	39,950	196,970	69.3	340.8	43.6	20.3%
Cholamandalam Investment & Finance Ltd	Consolidated	10	1,447.5	11,966	62,087	76.6	397.1	18.9	19.3%
Shriram City Union Finance Ltd	Consolidated	10	1,859.7	10,055	66,898	151.8	1,013.7	12.2	15.0%
Sundaram Finance	Consolidated	10	1,859.7	10,298	79,982	105.4	719.9	17.6	12.9%
Mahindra Mahindra Financial Services Ltd	Consolidated	2	421.0	18,673	113,475	29.7	183.7	14.2	16.5

Source: Company, PL

Exhibit 12: Key Management Personnel

Padmaja Gangireddy.	Promoter And Managing Director	She also serves as a director on the board of directors of Caspian Financial Services Limited. She has been a Director on the Company Board since April 19, 2003. She founded Spandana Rural and Urban Development Organisation ("SRUDO") in 1998.
Sudhesh Chandrasekar	Chief Financial Officer	He holds a post graduate diploma in management from the Indian Institute of Management, Bangalore and a bachelor's degree in commerce (honours) from Shri Ram College of Commerce, University of Delhi, Delhi. Prior to joining the Company he worked with Unitus Capital and with ICICI Bank . Mr. Sudhesh Chandrasekar joined SSFI on August 17.
Abdul Feroz Khan	Chief Strategy Officer	He holds a masters' degree in business administration from Institute of Chartered Financial Analysts of India University, Dehradun. He joined Company on November 10, 2008 as an assistant finance manager and was designated as Chief Strategy Officer on May 15, 2018.

Source: Company, PL

Financials

Exhibit 13: Income Statement (Rs mn)

Y/e Mar	FY16	FY17	FY18	FY19
Int. Inc. / Opt. Inc.	3,439	3,771	5,873	10,431
Interest Expenses	1,294	1,494	2,318	3,579
Net interest income	2,144	2,277	3,555	6,852
<i>Growth (%)</i>		6.2	56.2	92.7
Non-interest income	49.44	16.02	2.25	54.33
<i>Growth (%)</i>		-67.6	-86.0	2314.7
Net operating income	2,194	2,293	3,557	6,907
Expenditures				
Employees	571	581	759	1,310
Other Expenses	286	294	269	339
Depreciation	37.01	83.33	57.24	69.66
Operating Expenses	893	958	1,084	1,719
PPP	1,300	1,335	2,473	5,188
<i>Growth (%)</i>		2.7	85.3	109.8
Provisions	107	984	-354	453
Profit Before Tax	1,193	351	2,827	4,735
Tax	0	-3,978	948	1,616
<i>Effective Tax rate (%)</i>			34%	34%
PAT	2,432	4,329	1,879	3,119
<i>Growth (%)</i>		78.0	-56.6	66.0

Source: Company, PL

Exhibit 14: Balance Sheet (Rs mn)

Y/e Mar	FY16	FY17	FY18	FY19
Source of funds				
Equity	8,114	284	298	596
Reserves and Surplus	-6,273	8,991	13,609	18,298
Non Controlling Interest				9.22
Networth	1,841	9,276	13,906	18,904
<i>Growth (%)</i>			49.9	35.9
Loan funds	11,024	9,335	23,314	29,677
<i>Growth (%)</i>			149.8	27.3
Other Liabilities	8,134	676	422	736
Total Liabilities	20,999	19,286	37,642	49,317
Application of funds				
Net fixed assets	145	90	85	268
Advances	20,374	11,945	30,896	42,678
<i>Growth (%)</i>			158.6	38.1
Investments	1	1	1	1
Current Assets	458	2,956	2,762	4,158
Net current assets	458	2,956	2,762	4,158
Other Assets	21	4,293	3,898	2,213
Total Assets	20,999	19,286	37,642	49,317
Business Mix				
AUM		20,991	39,601	47,957
<i>Growth (%)</i>		6.8	143.3	40.1

Source: Company, PL

**Analyst Coverage Universe**

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Capital First	UR	-	495
2	Cholamandalam Investment and Finance Company	BUY	322	260
3	Edelweiss Capital	NR	-	276
4	HDFC	BUY	2,270	2,125
5	L&T Finance Holdings	Accumulate	178	120
6	LIC Housing Finance	Accumulate	550	496
7	Mahindra & Mahindra Financial Services	Accumulate	527	396
8	Shriram Transport Finance	BUY	1,481	1,063

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Buy	: >15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly



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