Stock Update

Spandana Sphoorty Financial Ltd.

Jan 01, 2024

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Spandana Sphoorty Financial Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
BFSI – NBFC (MFI)	Rs 1129	Buy in Rs 1120-1145 band and add on dips in Rs 1015-1035 band	Rs 1242	Rs 1340	2 quarters

HDFC Scrip Code	SPASPHEQNR
BSE Code	542759
NSE Code	SPANDANA
Bloomberg	SPANDANA IN
CMP Dec 29, 2023	1128.7
Equity Capital (Rs cr)	71.1
Face Value (Rs)	10
Equity Share O/S (cr)	7.1
Market Cap (Rs cr)	8033
Book Value (Rs)	472.6
Avg. 52 Wk Volumes	182,300
52 Week High (Rs)	1135.6
52 Week Low (Rs)	470.0

Share holding Pattern % (Sep, 2023)	
Promoters	60.4
Institutions	31.8
Non Institutions	7.8
Total	100.0

* Refer at the end for explanation on Risk Ratings

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Our Take:

Spandana Sphoorty Financial Ltd. (SSFL) has made significant progress on the vision it had set out in 2022 for 2025 i.e. reinforcing the middle and senior management team, strengthening governance risk and control, customer acquisition, technology scale up and customer led initiatives. It has started planning for the next 3 years of growth i.e. FY25-FY28. With the top and middle management team in place, SSFL is on course to becoming a process driven and stable enterprise with professionals manning their respective domains.

The company aims to achieve assets under management (AUM) of Rs 15,000cr by FY25 and Rs 24,500cr by FY28, supported by its new customer acquisition strategy, increasing ticket sizes for its existing customers as needed and by diversifying within its distribution models, such as business correspondence, co-lending, and balance sheet funding in the near to medium term. It has introduced shorter tenure loans of 12 and 18 months in addition to 24 months which could aid in higher earnings. Modest credit costs and improvement in cost-to-income ratio is likely to result in higher profitability and expansion of return ratios.

On Aug 10, 2023, we had released a Stock Update report (Link) with a recommendation to 'Buy in Rs 825-845 band and add on dips in Rs 740-755 band' for base case fair value of Rs 916 and bull case fair value of Rs 974 over next 2 quarters. Both the targets were achieved within the given time frame.

Financial Summary

Particulars (Rs cr)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	FY23	FY24E	FY25E	FY26E
NII	383	206	*85.4*	312	*22.6*	943	1360	1717	2146
PPoP	258	110	*134.1*	189	*36.2*	562	837	1086	1376
PAT	125	55	*126.9*	119	*4.8*	12	480	632	802
EPS (Rs)	17.6	7.8	*126.7*	16.8	*4.7*	1.8	67.8	89.3	113.3
P/E (x)						645.5	16.7	12.7	10.0
P/ABV (x)						2.6	2.3	1.9	1.6
RoAA (%)						0.2	4.4	4.5	4.6

(Source: Company, HDFC sec)

Valuation & Recommendation:

We expect advances of the company to increase at 29% CAGR over FY23-FY26E after a strong growth of 40% in FY23. Return ratios are likely to improve as the company has cleaned up its balance sheet and it focusses on growing its book and improving its yield. The valuation of the stock has not moved up in line with the improved performance and guidance and with that of most of its peers. We have valued the company at 1.95x Sep'25E ABV for a base case target of Rs 1242 and 2.1x Sep'25E ABV for a bull case target of Rs 1340 over next 2 quarters. Investors can buy the stock in the band of Rs 1120-1145 and add on dips in Rs 1015-1035 band (1.6x Sep'25E ABV).

Q2FY24 Result Update

SSFL reported another strong quarter of growth with PAT of Rs 125cr (+127%/5% YoY/QoQ) driven by a healthy AUM growth and stable NIMs. AUM grew by 11% sequentially to Rs 9784cr on back of 51% increase in disbursements to Rs 2513cr. AUM/Loan officer to improve to Rs 1.4-1.5cr and Borrowers/Loan officer to increase to 380-400 by the end of FY24E. SSFL added 3.5 lakh new customers taking the number of borrowers to 27.6 lakh.

Net operating income grew 23% YoY to Rs 383cr as yields improved by ~500bps YoY to 24.5%. NIM was stable sequentially but expanded by ~110bps YoY to 14.1%. On the asset quality front, GNPA/NNPA improved from 1.6%/0.5% to 1.5%/0.4% sequentially. Provision coverage ratio stood at 70%. SSFL has recovered Rs 54cr from written off accounts in H1 and is targeting another Rs 50cr in H2.

Management has maintained AUM guidance of Rs 15,000cr by the end of FY25 and credit costs of less than 2%. The company added ~200 branches on a net basis and its branch count stood at 1502 at the end of Q2FY24.

SSFL is changing its collection model under project 'Parivartan' to weekly repayment system from the monthly repayment followed currently. This impacted on its collection efficiency in Q2 which dipped to 97.7% from 98.1% in Q1FY24.

Recent developments

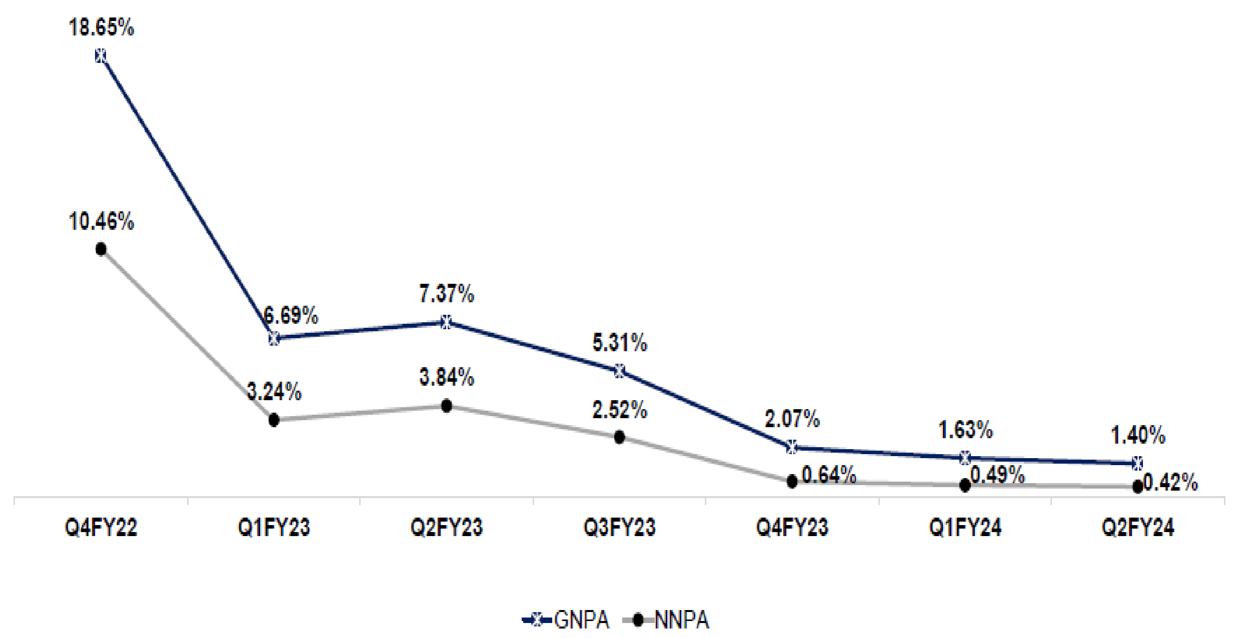
Diversifying borrowing sources to drive lower cost of funds

SSFL continues to diversify its borrowing sources and has added three big lenders in Q2FY24 i.e. SBI, NABARD and SIDBI. Its improved operating performance has also resulted in a rating upgrade from ICRA to A stable from A minus earlier. This has helped the company to lower its marginal cost of borrowing to 12.3% in Q2FY24 from 12.6% in Q4FY23. With higher borrowings from PSUs and rating upgrade, incremental cost of borrowing is expected to remain benign.

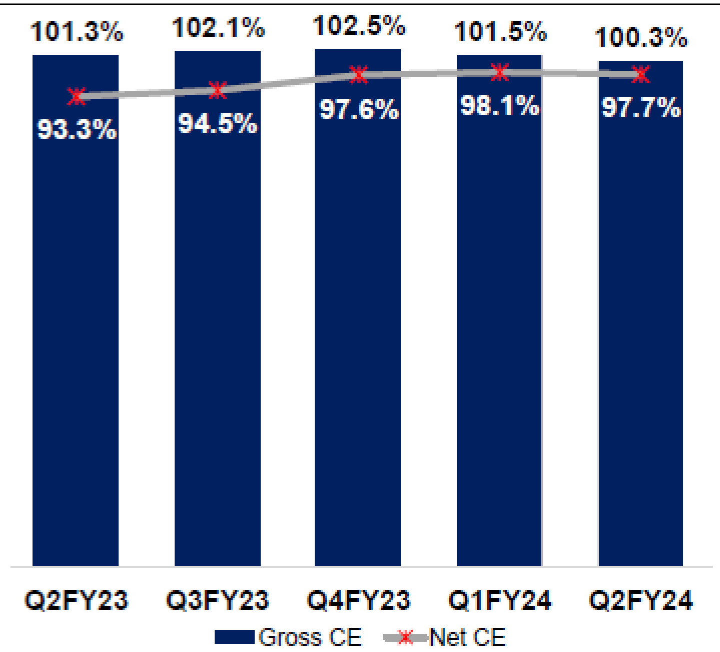
Portfolio quality continues to improve; collection efficiency remains strong

Asset quality of the company continued to improve, with GNPA/NNPA declining ~23bp/7bp QoQ to 1.4%/0.4%. There was increase in Stage 1 and Stage 2 loan books on account of change in collection model which is expected to normalize going forward. Gross collection efficiency stood at 100.3% indicating payments are being received after a lag. PCR on Stage 3 loans were stable at ~70%. Credit costs increased to ~4% in Q2FY24 on account of increased provision for older portfolio and some correction in the assignment portfolio. The management maintained the guidance of sub 2% in FY24.

Improving asset quality



Strong collection efficiency



(Source: Company, HDFCsec)

Aggressive branch expansion to capture higher market share

SSFL has added ~200 branches in Q2FY24 taking its network to 1502 branches thereby completing its vision of having 1500 branches by FY25. The management intends to have strong growth next year across all its branches. A typical microfinance branch takes about five months to break even on its own, and about 11 months to come into the full black.

Risks & Concerns

Unsecured nature of business

Microfinance loans are unsecured and are susceptible to various operational and credit risks. SSFL lends to women under the JLG model. These women typically do not have any stable source of income and are usually adversely affected by declining economic conditions. Natural calamities lead to a fall in incomes and consequently default in repayment of Microfinance loans.

Limited product and revenue diversification

Presently, SSFL's portfolio comprises almost solely of microfinance loans. The management is looking to diversify into other loan segments including secured lending like vehicle loans, mortgage loans etc. over the next 2-3 years. However, we will have to wait and watch if the company is able to scale up its operations in that direction.

Competition from SFBs

Many of the erstwhile MFIs have converted to small finance banks (SFBs) or merged with a large bank. It has provided them with access to low-cost funds which they can utilize to offer lower interest rates. This could hamper the growth of MFIs like SSFI who must depend on bank/market borrowings.

Political interference in MFI dues

Political instigation in some states asking people not to pay back their Microfinance dues could result in higher NPAs.

Higher dependence on few states

Spandana's business is heavily dependent on its operations in Madhya Pradesh, Orissa and Karnataka, accounting for over ~40% of its AUM. Although the company is diversifying geographically, any material changes in the socio-political and economic conditions affecting these markets could adversely impact its business.

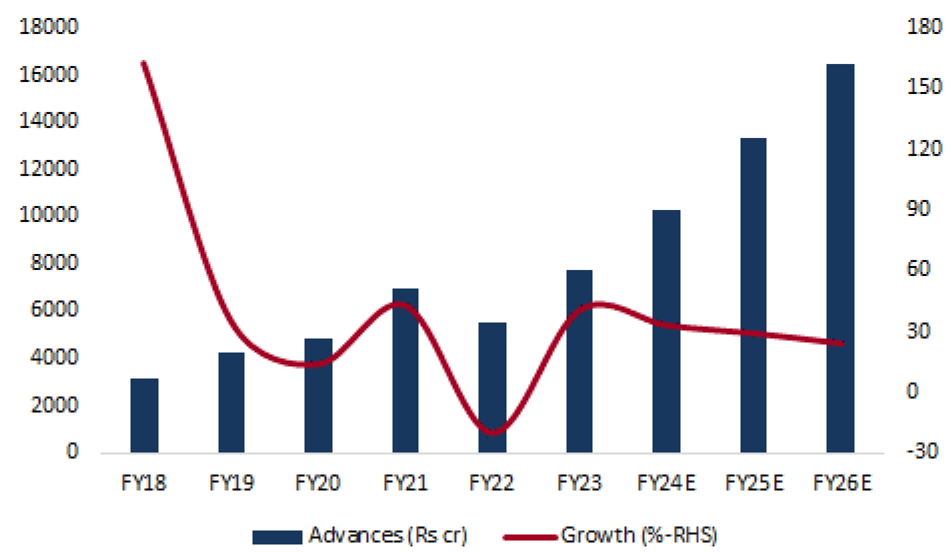
Industry Overview

- As on 30 September 2023, 4.0cr clients have loan outstanding from NBFC-MFIs, which is 23.0% higher than clients as on 30 September 2022.
- The Asset Under Management (AUM) of MFIs is Rs 1,33,963cr as on 30 September 2023 , including owned portfolio Rs 1,09,462cr and managed portfolio (off BS) of Rs 24,501cr. The owned portfolio of MFIN members is 74.0% of the NBFC-MFI universe portfolio of Rs 1,47,829cr.
- On a YoY basis AUM has increased by 39.2% as compared to 30 September 2022 and by 6.3% in comparison to 30 June 2023.
- Loan amount of Rs 32,732cr was disbursed in Q2FY23-24 through 79.1 Lakh accounts, including disbursement of Owned as well as Managed portfolio. This is 16.8% higher than the amount disbursed in Q2FY22-23.
- Average loan amount disbursed per account during Q2FY23-24 was Rs 41,373 which has reduced by around 0.4% in comparison to same quarter of last financial year.
- As on 30 September 2023, the borrowings O/s were Rs 1,00,438cr. Banks contributed 58.8% of borrowings O/s followed by 19.8% from Non-Bank entity, 10.5% from AIFIs, 5.8% from External Commercial Borrowings (ECB) and 5.1% from other sources.
- During Q2FY23-24, NBFC-MFIs received a total of Rs 26,503cr in debt funding, which is 64.2% higher than Q2FY22-23. Banks contributed 66.2% of the total Borrowing received followed by Non-Bank entities 18.9%, AIFIs 9.0%, Others 4.3% and ECB 1.7%.
- Total equity increased by 33.1% as compared to end of Q2FY22-23 and is at Rs 28,138cr as on 30 September 2023.
- Portfolio at Risk (PAR)>30 days as on 30 September 2023 has improved to 3.1% as compared to 7.5% as on 30 September 2022.
- MFIs have presence in 27 states and 5 union territories.
- In terms of regional distribution of portfolio (AUM), East and North-East accounts for 32% of the total NBFC-MFI portfolio, South 25%, West 17%, North 16%, and Central contributes 10%.

Company Background:

Founded in 1998 Spandana Sphoorty Financial Ltd. (SSFL) is a rural focused NBFC-MFI with a geographically diversified presence in India. The company offers income generation loans under the joint liability group model, predominantly to women from low-income households in Rural Areas. At its peak, SSFL had 1,856 branches with presence across 10 states and a workforce of over 13,500 employees. As of Q2FY24, SSFL had over 12,500 employees operating out of 1,502 branches. It disbursed ~Rs 4,177cr of loans in H1FY24 and had an outstanding AUM of Rs 9,784cr.

Outstanding loan book growth



(Source: Company, HDFC sec)

Business Overview:

The operations of SSFL focus on women from low-income groups in Rural Areas who aspire to improve their financial well-being.

Chetana Loans: SSFL's main lending product is 'Chetana' loans, which are income generation loans designed to empower women by enabling them to set up and expand income generating activities. These loans are primarily given to women, who are willing to borrow in a group and are agreeable to accept joint liability for the loans. Loans are provided to groups without any collateral, with each group consisting of 8 to 10 women. Under the JLG model, loans are provided to individual clients as well where the group guarantees the repayment of loans given to individual members of the group. In FY23 Chetana accounted for over 90% of the total loans.

Other Loans: Besides Chetana loans SSFL also provides certain other categories of loans which include:

- loans against property to clients who run businesses, are self-employed or salaried;
- personal loans for meeting with the working capital requirements, increasing the scale of business
- interim loans, which are top up loans given to existing clients (on a group guarantee) to use for their capital working needs, seasonal requirements or emergency needs.

Peer Comparison

(Rs cr)	CMP	Mcap	Revenue			PAT			BV (Rs)			P/BV (x)			RoE (%)		
	Rs		FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Satin Cr.	240	2664	1687	2129	2638	325	475	626	237	285	348	1.0	0.8	0.7	15.2	18.3	19.9
CreditAccess	1597	25482	3902	4812	5705	1381	1675	2024	407	511	639	3.9	3.1	2.5	24.0	23.0	22.0
Ujjivan SFB	57	11152	4123	4981	5988	1287	1416	1613	26	33	40	2.2	1.7	1.4	27.7	24.2	22.6
Bandhan Bank	241	38839	13114	15532	18181	3605	4556	5327	139	164	194	1.7	1.5	1.2	17.0	18.0	17.9
Spandana	1129	8033	2308	2948	3669	480	632	802	504	593	706	2.2	1.9	1.6	14.4	16.2	17.4

(Source: HDFC sec, Bloomberg)

Financials

Income Statement

(Rs cr)	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	1463	1401	2217	2829	3535
Interest Expenses	540	458	857	1112	1389
Net Interest Income	**923**	**943**	**1360**	**1717**	**2146**
Non interest income	17	76	90	118	134
Operating Income	**940**	**1019**	**1451**	**1835**	**2281**
Operating Expenses	362	457	614	749	905
PPoP	578	562	837	1086	1376
Prov & Cont	481	544	190	236	298
Profit Before Tax	97	18	647	850	1077
Tax	27	5	167	218	276
PAT	**70**	**12**	**480**	**632**	**802**

Balance Sheet

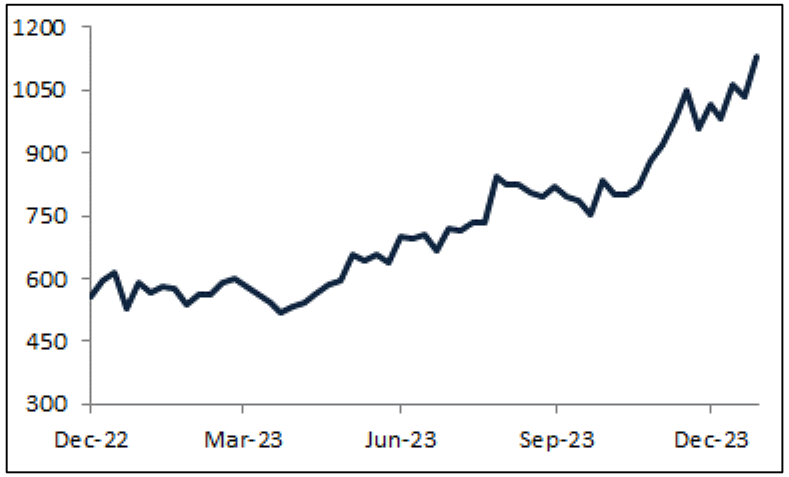
(Rs cr)	FY22	FY23	FY24E	FY25E	FY26E
Share Capital	69	71	71	71	71
Reserves & Surplus	3018	3028	3508	4140	4942
Shareholder funds	**3088**	**3099**	**3579**	**4211**	**5013**
Minority Interest	2	0	0	0	0
Borrowings	3772	6074	8205	10651	13290
Other Liab & Prov.	214	209	504	719	879
SOURCES OF FUNDS	**7076**	**9383**	**12288**	**15581**	**19181**
Fixed Assets	31	47	58	71	81
Investment	2	189	206	240	281
Cash & Bank Balance	1202	1005	1238	1398	1651
Advances	5518	7760	10321	13313	16509
Other Assets	322	382	464	559	660
TOTAL ASSETS	**7076**	**9383**	**12288**	**15581**	**19181**

Ratio Analysis

Particulars	FY22	FY23	FY24E	FY25E	FY26E
Return Ratios (%)					
Calc. Yield on advances	23.5	20.8	24.0	23.5	23.3
Calc. Cost of borrowing	11.8	9.3	12.0	11.8	11.6
Calc. NIM	14.8	14.0	14.7	14.3	14.1
RoAE	2.4	0.4	14.4	16.2	17.4
RoAA	0.9	0.2	4.4	4.5	4.6
Asset Quality Ratios (%)					
GNPA	17.7	2.1	1.9	1.9	2.0
NNPA	11.8	0.6	0.6	0.6	0.5
Growth (%)					
Advances	-20.4	40.6	33.0	29.0	24.0
Deposits	-29.8	61.0	35.1	29.8	24.8
NII	-12.9	2.2	44.3	26.2	25.0
PPoP	-31.7	-2.7	48.9	29.8	26.7
PAT	-51.9	-82.3	3773.1	31.7	26.8
Valuation Ratios					
EPS (Rs)	10.1	1.7	67.6	89.1	112.9
P/E (x)	111.4	645.5	16.7	12.7	10.0
Adj. BVPS (Rs)	357.0	429.5	495.8	582.8	693.5
P/ABV (x)	3.2	2.6	2.3	1.9	1.6
Dividend per share (Rs)	0.0	0.0	0.0	0.0	0.0
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0
Operating efficiency					
Cost-average assets	38.6	44.8	42.3	40.8	39.7
Cost-income	1.8	2.5	2.9	3.2	3.3

(Source: Company, HDFC sec)

Price chart



HDFC Sec Retail Research Rating description

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This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks
This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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Disclosure:

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