

Equity Research

July 12, 2022

BSE Sensex: 53887

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Financials

Q4FY22 result review,
reco, TP change

Target price: Rs550

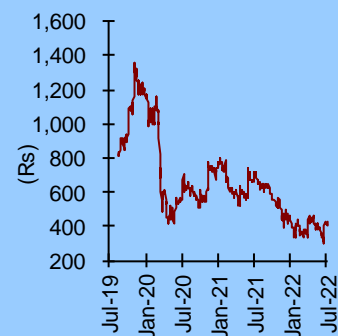
Target price Revision
Rs550 from Rs450

Shareholding pattern

| | Sep '21 | Dec '21 | Mar '22 |
|-------------------------|------------|------------|------------|
| Promoters | 62.3 | 62.3 | 63.6 |
| Institutional investors | 17.0 | 14.8 | 16.6 |
| MFs and other | 0.0 | 0.0 | 0.0 |
| Banks/ FIs | 0.4 | 0.4 | 0.4 |
| Insurance | 0.0 | 0.0 | 0.0 |
| FII | 16.6 | 14.3 | 16.2 |
| Others | 20.7 | 23.0 | 19.8 |

Source: BSE

Price chart



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INDIA



Spandana Sphoorty

BUY

Upgraded from Add

Newly-appointed management in place; setting up
processes to achieve Vision 2025 goals

Rs428

FY22 had been an eventful year for Spandana Sphoorty (Spandana), starting with the resignation of its erstwhile MD & CEO which triggered operational instability followed by course correction. Corrective measures included: a) Appointing new and experienced core management, b) settling all the disputes with the erstwhile MD by paying one-time settlement amount of ~Rs400mn, c) streamlining the business process as per the revised RBI guidelines and d) rolling out Vision 2025 with RoA / RoE target of >4.5% / >20%, respectively.

Therefore, in Q4FY22, it was focussing more on setting up its strategies, aligning and refining processes to pave the way for achieving Vision 2025 goals. Consequently, it reported a PAT of Rs286mn in Q4FY22, a decline of 37% QoQ due to 14% QoQ decline in NII and one-time settlement fees of Rs400mn. Further, accelerated recognition of stress resulted in GNPL ratio doubling to 15% in Q4FY22 vs 5.7% in Q3FY22. While total stress with NNPL ratio at 6% and PAR 31-90 at 6.6% remained elevated, collection efficiency at 100% in non-restructured book and 74% (March'22) in restructured book gives some hope of credit cost in FY23E to remain lower than FY22 (7%).

Considering the management and the operational stability, improving visibility on earnings recovery led by credit cost normalisation and favourable risk-reward (trading at 0.7x FY24e P/BV), we upgrade the stock to BUY from ADD earlier with a revised TP of Rs550 (earlier: Rs450). We roll over estimates to Sep-23 and assign P/BV multiple of 1x.

- **Vision 2025 aims at sharp improvement in profitability – targets RoA / RoE of >4.5% / >20% by FY25.** After a turbulent FY22, which saw AUM decline of 19% YoY, 4% YoY decline in borrower base and GNPL increasing to 15% by March'22 on the back of operation and management instability triggered by the resignation of the erstwhile MD & CEO, Spandana has initiated various measures to get back on feet. As a part of course-correction, it appointed Mr. Shalabh Saxena (former MD & CEO of BFIL) as its new MD & CEO, who took charge in March'22. In a span of <4 months, the new management has successfully completed transition and has set ambitious goals for Vision 2025. Key goals are: a) Scaling MFI AUM to Rs182bn by FY25 mainly driven by taking customer base to 4.0mn vs 2.4mn currently, b) building 10-15% of secured portfolio, c) to achieve near industry best credit cost of ~1.5% and RoA/RoE of 4.5-5.3%/22.0-24.0%, respectively, by FY25.
- **Credit cost to remain elevated in FY23E, but NIMs could surprise positively.** While the management envisages to bring down credit cost to 2% in FY23E, we believe elevated stress pool (NNPL at 6% + PAR 31-90 at 6.6%) would keep credit cost higher. We are modeling credit cost at 4.6% in FY23E. However, we also estimate >100bps margin expansion driven by lower interest reversal and likely price hike (in line with industry trend) during FY23E.

| | | | | | | |
|-------------------------|--------------------|--------------------|--------|--------|-------|-------|
| Market Cap | Rs30.4bn/US\$381mn | Year to Mar | FY21 | FY22 | FY23E | FY24E |
| Bloomberg | SPANDANA IN | NII (Rs bn) | 10.6 | 9.2 | 10.4 | 12.8 |
| Shares Outstanding (mn) | 70.9 | Net Profit (Rs bn) | 1.5 | 0.7 | 2.7 | 4.7 |
| 52-week Range (Rs) | 716/295 | EPS (Rs) | 22.6 | 10.1 | 39.3 | 77.8 |
| Free Float (%) | 36.4 | % Chg YoY | (58.7) | (55.3) | 288.9 | 97.9 |
| FII (%) | 16.2 | BVPS (Rs) | 427.8 | 447.2 | 478.6 | 629. |
| Daily Volume (US\$'000) | 2,530 | P/E (x) | 19.0 | 42.5 | 10.9 | 5.5 |
| Absolute Return 3m (%) | (0.1) | P/BV (x) | 1.0 | 1.0 | 0.9 | 0.7 |
| Absolute Return 12m (%) | (40.2) | Net NPA (%) | 1.4 | 6.0 | 1.0 | 0.5 |
| Sensex Return 3m (%) | (7.4) | RoAuM (%) | 1.9 | 0.9 | 3.6 | 4.7 |
| Sensex Return 12m (%) | 4.1 | RoE (%) | 5.4 | 2.4 | 8.5 | 13.2 |

Please refer to important disclosures at the end of this report

- **Management and operational stability to help improve earning trajectory going forward.** Monthly disbursements of Rs8.6bn in March'22 suggest fast approaching business normalcy and also reflect operation realignment. Further, settlement with the erstwhile MD & CEO would ensure operation stability going forward. Spandana has taken the opportunity to beef up top and mid management teams, post the resignation of its erstwhile MD in Nov'21. It has hired CEO, CFO and CTO in the past six months. Management stability along with realigned business process would help it execute Vision 2025 in an effective manner. The key parameters of Vision 2025 are improving RoA to >4.5% (2.8% in FY22) and RoE to >20% (6.9% in FY22) by March'25.
- **Key risks** - A) stress unfolding higher than anticipation, B) operational instability caused by outside interference.

Table 1: Q4FY22 result table

| (Rs mn) | Q4FY22 | Q4FY21 | % change YoY | Q3FY22 | % change QoQ |
|----------------------------------|--------------|--------------|-----------------|--------------|-----------------|
| Interest Income | 2,868 | 4,739 | (39.5) | 3,461 | (17.1) |
| Interest Expended | 1,079 | 1,381 | (21.9) | 1,390 | (22.4) |
| Net interest income (NII) | 1,789 | 3,358 | (46.7) | 2,071 | (13.6) |
| Other income | 123 | 64 | 92.2 | 37 | 227.9 |
| Total income | 1,912 | 3,422 | (44.1) | 2,108 | (9.3) |
| Operating expenses | 1,334 | 634 | 110.5 | 871 | 53.2 |
| -Staff expenses | 641 | 441 | 45.4 | 613 | 4.6 |
| -Other expenses | 693 | 193 | 259.2 | 258 | 168.7 |
| Operating profit | 578 | 2,788 | (79.3) | 1,238 | (53.3) |
| Total provisions | 200 | 2,116 | (90.6) | 643 | (69.0) |
| Profit before tax | 378 | 672 | (43.7) | 595 | (36.4) |
| Tax | 92 | 179 | (48.5) | 144 | (35.9) |
| Profit after tax | 286 | 493 | (41.9) | 451 | (36.5) |

| Key statistic (Rs mn) | | | % change YoY | | % change QoQ |
|-----------------------|--------|--------|-----------------|--------|-----------------|
| AuM | 65,810 | 81,570 | (19.3) | 66,950 | (1.7) |
| Borrowers (in Lakh) | 24 | 25 | (4.1) | 26 | (9.3) |
| Calc. Avg ticket size | 28,004 | 33,294 | (15.9) | 25,849 | 8.3 |

| Ratios (%) | | | bp change YoY | | bp change QoQ |
|------------------------------------|-------------|-------------|------------------|-------------|------------------|
| Profitability ratios | | | | | |
| Portfolio Yields | 20.4 | 23.1 | (270) | 21.7 | (130) |
| Cost of Funds | 11.5 | 11.4 | 10 | 11.5 | - |
| NIM | 12.5 | 15.4 | (290) | 13.3 | (80) |
| RoAum | 1.6 | 2.6 | (108) | 2.5 | (94) |
| Asset Quality | | | | | |
| Gross NPL ratio | 15.0 | 3.1 | 1,190 | 5.7 | 935 |
| Business & Other Ratios | | | | | |
| Cost-income ratio | 69.8 | 18.5 | 5,125 | 41.3 | 2,848 |
| CAR | 51.1 | 40.0 | 1,109 | 46.0 | 509 |

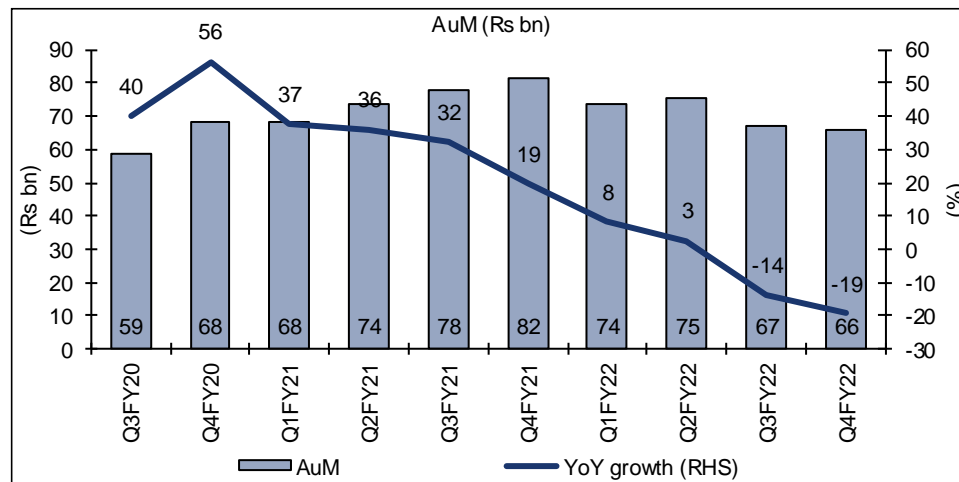
Source: Company data, I-Sec research.

Table 2: Vision 2025

| Particulars | FY22 | FY23 | FY25 |
|-----------------------|-------------|------------------|------------------|
| No of Branches | 1,120 | 1,120 | 1,500 |
| Customers (mn) | 2.4 | 2.8 | 4.0 |
| Disbursements (Rs mn) | 33,730 | 81,000 | 1,80,000 |
| Average ticket size | 32,000 | 33,000 | 47,800 |
| AUM (Rs mn) | 65,810 | 92,430 | 1,81,640 |
| NIM | 12.5% | 10.0% | 10.0% |
| Cost to income ratio | 32.9% | 43.7% | 35.7% |
| Opex to ANR | 4.3% | 6.0% | 5.2% |
| Credit cost | 7.0% | 2.0% | 1.5% |
| RoA | 2.8% | 4.0-4.75% | 4.5-5.25% |
| RoE | 6.9% | 11-14% | 22-24% |

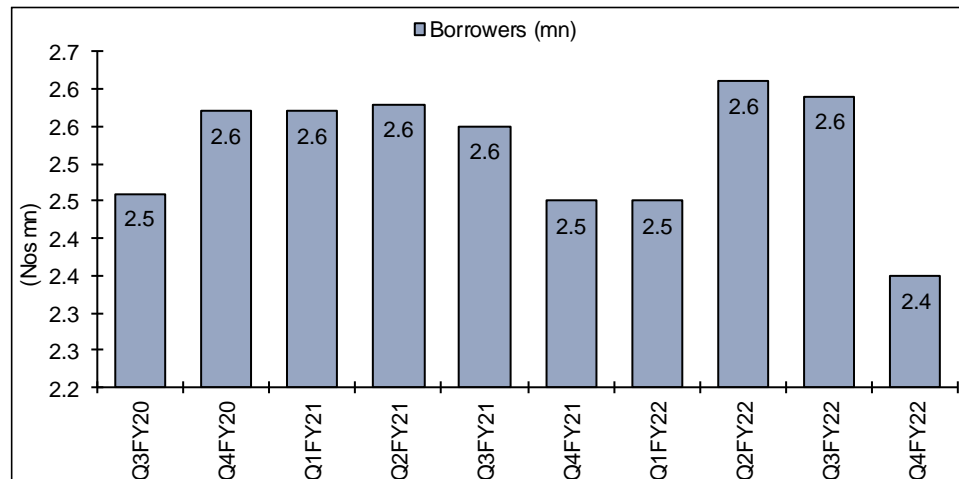
Source: Company data, I-Sec research.

Chart 1: AUM growth continued to remain weak due to transition at operational as well as management level during Q4FY22; trend likely to reverse from hereon



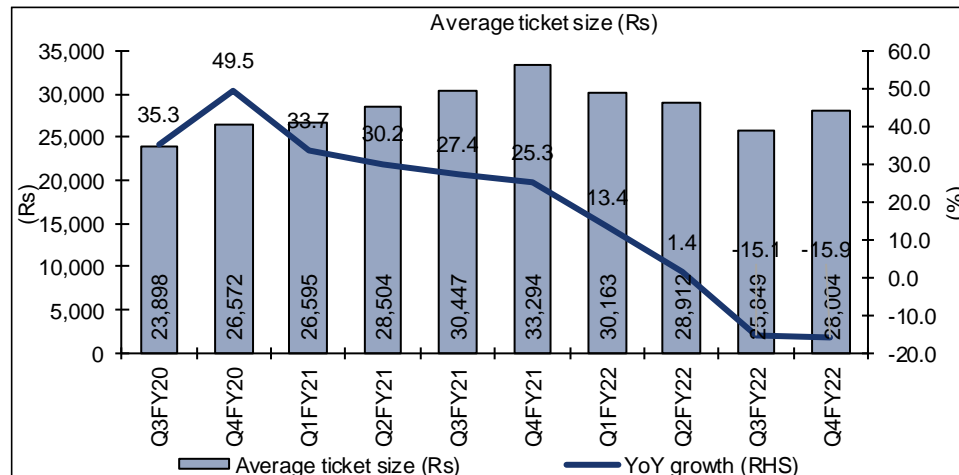
Source: Company, I-Sec research

Chart 2: Borrower base fell to 2.4mn



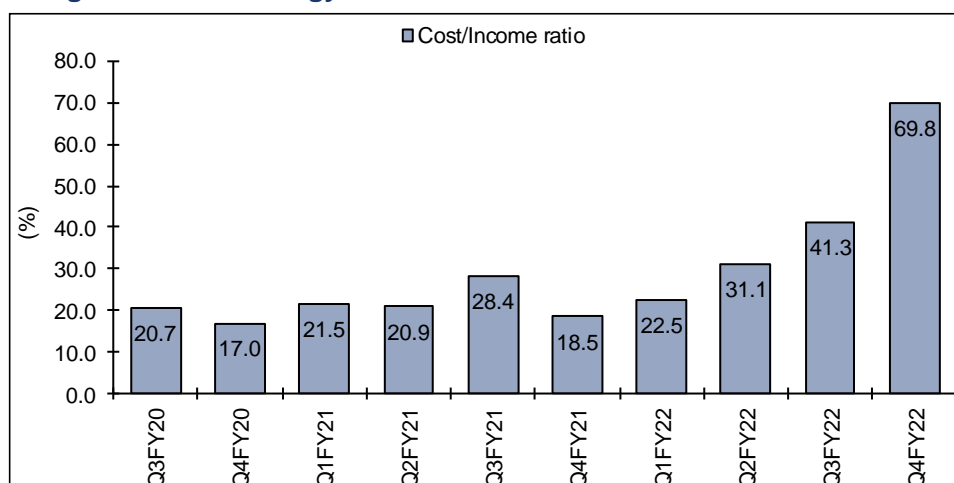
Source: Company, I-Sec research

Chart 3: Average ticket size increases to Rs28,000, but still significantly lower than industry average



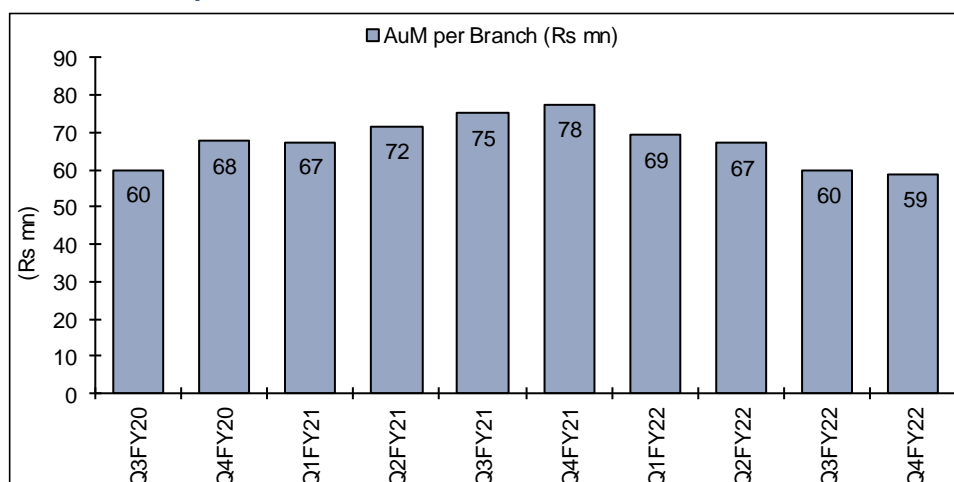
Source: Company, I-Sec research

Chart 4: Cost/income ratio increased due to transitory cost towards process realignment / technology and one-time settlement cost of Rs400mn



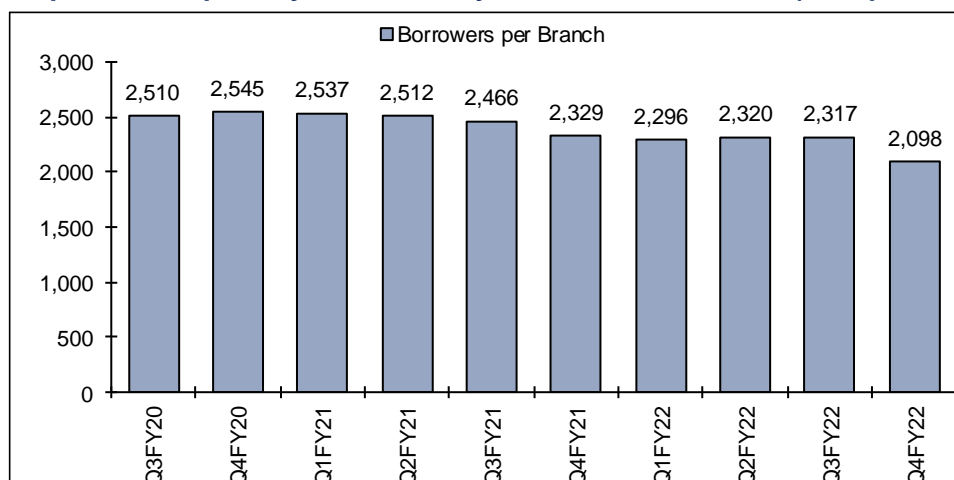
Source: Company, I-Sec research

Chart 5: AUM per branch moderated in Q4FY22 due to muted disbursement

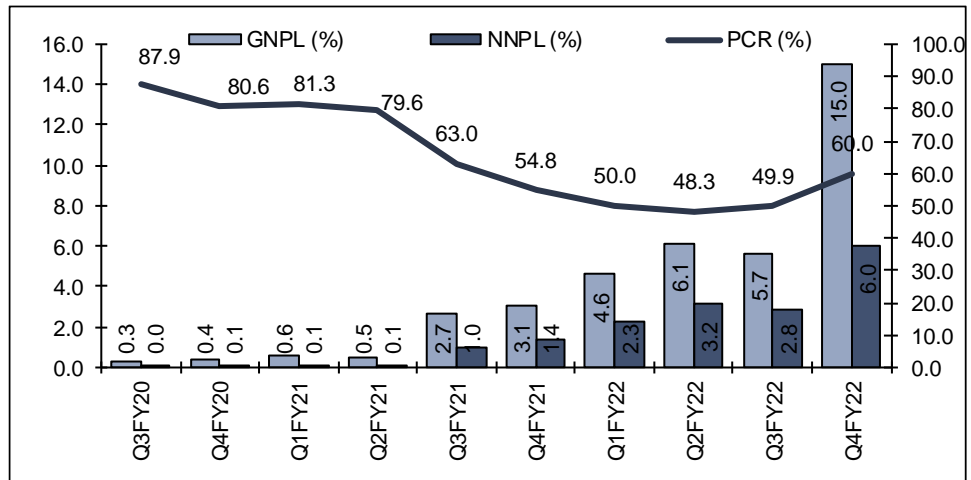


Source: Company, I-Sec research

Chart 6: Borrowers per branch remained lower due to tepid new customer acquisition, especially from recently added <100 branches (over past 1 year)



Source: Company, I-Sec research

Chart 7: Asset quality deteriorated

Source: Company, I-Sec research

Financial summary

Table 3: Profit and loss statement

(Rs mn, year ending March 31)

| | FY21 | FY22 | FY23E | FY24E |
|----------------------------------------|---------------|---------------|---------------|---------------|
| Interest income | 13,627 | 13,365 | 14,981 | 20,167 |
| Finance costs | 4,232 | 5,401 | 6,097 | 8,816 |
| NII | 10,595 | 9,227 | 10,427 | 12,803 |
| Y-Y growth | -2% | -13% | 13% | 23% |
| Net Revenue | 10,824 | 9,399 | 10,599 | 12,975 |
| Total Opex | 2,369 | 3,625 | 3,498 | 4,506 |
| Employee benefits expenses | 1,715 | 2,284 | 2,656 | 3,506 |
| Y-Y growth | 0% | 33% | 16% | 32% |
| Other expenses | 577 | 1,249 | 750 | 900 |
| Y-Y growth | 39% | 116% | -40% | 20% |
| Depreciation and amortisation expenses | 76 | 92 | 92 | 100 |
| PPoP | 8,456 | 5,774 | 7,101 | 8,469 |
| Y-Y growth | -5% | -32% | 23% | 19% |
| Provision and write-offs | 6,451 | 4,806 | 3,472 | 2,232 |
| Adjusted PBT | 2,004 | 969 | 3,629 | 6,237 |
| Exceptional items (IV) | 0 | 0 | 0 | 0 |
| Profit before tax | 2,004 | 969 | 3,629 | 6,237 |
| Tax | 550 | 270 | 913 | 1,570 |
| Profit after tax | 1,455 | 698 | 2,716 | 4,667 |

Source: Company data, I-Sec research

Table 4: Balance sheet

(Rs mn, year ending March 31)

| Year to March | FY21 | FY22 | FY23E | FY24E |
|-----------------------------------------|---------------|---------------|---------------|-----------------|
| Share capital | 643 | 691 | 691 | 691 |
| Reserves and surplus | 26,848 | 30,209 | 32,381 | 37,048 |
| Shareholders' funds | 27,511 | 30,899 | 33,072 | 37,739 |
| Debt securities | 20,347 | 17,782 | 17,891 | 24,306 |
| Borrowings (other than debt securities) | 33,184 | 19,737 | 41,746 | 56,714 |
| Subordinated liabilities | 202 | 202 | 202 | 202 |
| Other financial liabilities | 2,697 | 1,312 | 1,312 | 1,312 |
| Other non-financial liabilities | 414 | 509 | 509 | 509 |
| Equity and liabilities | 85,769 | 70,763 | 95,053 | 1,21,104 |
| Total borrowings | 53,733 | 37,721 | 59,838 | 81,222 |
| Assets | | | | |
| Property, plant and equipment | 199 | 68 | 68 | 68 |
| Intangible assets | 8 | 71 | 71 | 71 |
| Non-current investments | 23 | 24 | 750 | 750 |
| Loan Portfolio | 69,330 | 55,184 | 75,085 | 96,552 |
| Other non-financial assets | 441 | 618 | 742 | 742 |
| Cash and bank balances | 13,810 | 12,022 | 15,017 | 19,310 |
| Other financial assets | 757 | 745 | 969 | 1,259 |
| Tax assets | 1,201 | 2,030 | 2,030 | 2,030 |
| Assets | 85,769 | 70,763 | 95,053 | 1,21,104 |

Source: Company data, I-Sec research

Table 5: Key ratios

(Year ending March 31)

| | FY21 | FY22 | FY23E | FY24E |
|----------------------------------|--------------|--------------|--------------|--------------|
| Growth ratios (%) | | | | |
| NII growth | -2% | -13% | 13% | 23% |
| AUM Growth | 19% | -19% | 32% | 29% |
| Asset yields | 18% | 18% | 20% | 20% |
| Cost of funds | 10% | 12% | 13% | 13% |
| Spread | 8% | 6% | 7% | 8% |
| Opex growth | 7% | 53% | -4% | 29% |
| PPP growth | -5% | -32% | 23% | 19% |
| Provisions growth | 136% | -26% | -28% | -36% |
| Credit cost | 8.6% | 6.5% | 4.6% | 2.3% |
| PAT growth | -59% | -52% | 289% | 72% |
| Key ratios (%) | | | | |
| Cal NIM | 14.1% | 12.5% | 13.7% | 12.9% |
| Opex/AUM | 3.2% | 4.9% | 4.6% | 4.5% |
| Opex/AUM (Cal.) | 3.2% | 4.9% | 4.6% | 4.5% |
| Cost/Income ratio | 21.9% | 38.6% | 33.0% | 34.7% |
| Credit cost | 8.6 | 6.5 | 4.6 | 2.3 |
| Asset quality (%) | | | | |
| GNPA | 3.1 | 15.0 | 3.0 | 2.0 |
| NNPA | 1.4 | 6.0 | 1.0 | 0.5 |
| PCR | 55% | 60% | 67% | 75% |
| Per share data Rs) | | | | |
| Diluted EPS | 22.6 | 10.1 | 39.3 | 77.8 |
| EPS growth (%) | (58.7) | (55.3) | 288.9 | 97.9 |
| Book value per share | 427.8 | 447.2 | 478.6 | 629.0 |
| BVPS growth (%) | 4.5 | 4.5 | 7.0 | 31.4 |
| Valuation | | | | |
| P/E (x) | 19.0 | 42.5 | 10.9 | 5.5 |
| P/B (x) | 1.0 | 1.0 | 0.9 | 0.7 |
| RoA decomposition | | | | |
| Net interest income (%) | 14.1% | 12.5% | 13.7% | 12.9% |
| Other income (%) | 0.3% | 0.2% | 0.2% | 0.2% |
| Total income (%) | 14.4% | 12.8% | 13.9% | 13.1% |
| Employee expenses (%) | 2.3% | 3.1% | 3.5% | 3.5% |
| Depre (%) | 0.8% | 1.7% | 1.0% | 0.9% |
| Other operating expenses (%) | 0.1% | 0.1% | 0.1% | 0.1% |
| Total operating expenses (%) | 3.2% | 4.9% | 4.6% | 4.5% |
| Pre provisioning profits (%) | 11.3% | 7.8% | 9.3% | 8.5% |
| Provisions (%) | 8.6% | 6.5% | 4.6% | 2.3% |
| Pre tax profits (%) | 2.7% | 1.3% | 4.8% | 6.3% |
| Tax (%) | 0.7% | 0.4% | 1.2% | 1.6% |
| RoAUM (%) | 1.9% | 0.9% | 3.6% | 4.7% |
| Leverage | 2.8 | 2.5 | 2.4 | 2.8 |
| RoE (%) | 5.4% | 2.4% | 8.5% | 13.2% |
| Capital Adequacy | | | | |
| CRAR - Tier I capital (%) | 39.0% | 53.5% | 40.0% | 35.7% |
| CRAR - Tier II capital (%) | 1.0% | 1.0% | 1.0% | 1.0% |
| CRAR (%) | 40.0% | 54.6% | 41.1% | 36.8% |

Source: Company data, I-Sec research

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