

Spandana Sphoorty Financial Ltd

BUY

CMP Rs535

Target Rs800

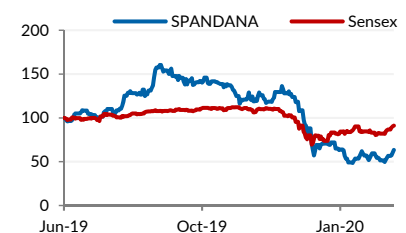
Upside 50.0%

HIGHLIGHTS	<ul style="list-style-type: none"> Spandana reported robust AUM growth of 16% qoq and 56% yoy in Q4 FY20. Disbursements grew by 67% yoy notwithstanding Covid induced distortion in March. Borrower base grew 5% qoq, after being static in preceding three quarters. AUM/Borrower jumps 11% qoq and 50% yoy to Rs26,600, still materially lower than industry average. Branch addition remained calibrated with steady ramp-up in the number of Loan Officers per Branch. Opex/Avg. AUM ratio came-off further and stood at 3.9%. Company made additional provisions of Rs1.29bn (2.75% of on-BS loans) for potential Covid impact. Even adjusted for it, the credit cost was sequentially higher due to write-off of the impacted portfolio in coastal Karnataka (adverse external influence) and Maharashtra (hit by floods). Assignment income was substantially higher at Rs1.09bn driven by Rs12.6bn worth of assignment done during the quarter. This mitigated the impact of higher provisions on PAT and annualized RoA stood above 5%. Adjusted for lumpy assignment income and additional provisions, PBT declined 2% qoq but grew 20% yoy. With the proportion of DA + PTC rising to 35% of AUM, Spandana's CAR improved to 53% and D/E remained low at 1.2x. Spandana has collected Rs1.45bn since resuming its operations on April 20. It expects to collect Rs3bn in June. By May-end, all branches were operational and >92% of the staff resumed work. As end-May, the company had cash balance of Rs4bn, undrawn sanctions of Rs3.4bn and a sanction pipeline of Rs18.3bn. Management is hopeful of drawing Rs5.5bn in June. Most lenders are providing support, either by extending moratorium or by offering fresh loans.
	<ul style="list-style-type: none"> We built-in a near worst case scenario of 10% AUM growth and 9% credit cost (on opening on-book portfolio) in FY21. FY22 should be a normal year, but we factor higher-than-usual credit cost. Retain BUY rating with a 12m TP of Rs800. We are positive about profitability/growth normalization in FY22, robust CAR (supportive of liquidity position) and attractive valuation.
	<ul style="list-style-type: none"> Spandana trades at 1x/5.6x FY22 ABV/EPS. Valuation will be most sensitive to the collection experience in coming months
	<ul style="list-style-type: none"> Prolonged Covid episode and a large scale moral hazard issue

Stock data (as on June 03, 2020)

Sensex:	34,110
52 Week h/l (Rs)	1397 / 405
Market cap (Rs/USD mn)	34586 / 458
Outstanding Shares	64
6m Avg t/o (Rs mn):	58
Div yield (%):	-
Bloomberg code:	SPANDANA IN
NSE code:	SPANDANA

Stock performance



	1M	3M	1Y
Absolute Rtn	18.4%	(51.3)%	-

Shareholding pattern (As of Mar'20 end)

Promoter	62.6%
FII+DII	16.3%
Others	21.1%

Δ in earnings estimates

	FY20	FY21e	FY22e
EPS (New)	61.5	101.8	129.0
EPS (Old)	52.4	33.9	95.1
% change	(14.9)	(66.7)	(26.3)

Exhibit 1: Financial Summary

Y/e 31 Mar (Rs mn)	FY19	FY20	FY21E	FY22E
Operating income	6,852	10,873	9,754	13,365
yoy growth (%)	92.6	58.7	(10.3)	37.0
Net profit	3,087	3,367	2,179	6,113
yoy growth (%)	64.3	9.1	(35.3)	180.6
EPS (Rs)	51.8	52.4	33.9	95.1
Adj.BVPS (Rs)	316.3	405.5	439.4	534.5
P/E (x)	10.3	10.2	15.8	5.6
P/adj.BV (x)	1.7	1.3	1.2	1.0
ROE (%)	18.8	15.0	8.0	19.5
ROA (%)	7.1	6.2	3.2	7.3
CAR (%)	39.6	52.9	43.9	46.2

Source: Company, YES Sec - Research

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CON-CALL HIGHLIGHTS

- ✓ Loan officers have been able to meet 80% of borrowers; and of this 75-80% are willing to pay. This is the basis of assuming 50% collection efficiency for the month of June. The remaining 20% borrowers whom the loan officers met wanted few weeks to start repayments and thus may not opt for moratorium till August 31st.
- ✓ The company collected Rs1.3bn in May with only 40-50% of the loans officers available. With about 92% of field staff back now, collection of the estimated Rs3bn in June should not be a logistical challenge. On June 2, the portfolio collection was Rs120mn, and the management expects daily run-rate to improve from here.
- ✓ Money is being collected by meeting borrowers in small groups or from the doorstep of the borrowers/group leaders. From July 1st, the company plans to revert to center meetings to meet all customers on scheduled date. Meetings will be conducted at venues other than borrower's house.
- ✓ Members paying within a group has a motivating effect on other borrowers who have not started to pay despite having the ability to pay (income not impacted significantly for most rural borrowers). The borrowers who are paying become eligible for a larger next-cycle loan earlier. Spandana is keen on disbursing loans to borrowers who are completing existing loans. The company expects to disburse Rs1.5bn in June and expects monthly disbursements to rise to Rs5-6bn by September.
- ✓ 68% of lenders offered moratorium in the first phase, but Spandana repaid all in April and availed moratorium for only Rs0.3bn term loan dues in May. For the second moratorium term, the NBFC lenders are expected to extend moratorium whereas banks are offering fresh loans over moratorium (however, new loans at higher rate than existing ones).
- ✓ Spandana raised Rs19.4bn of borrowings during Q4 FY20 comprising Rs12.6bn via direct assignments (DA), around Rs1.5bn through PTC and Rs5.3bn in the form of term loans. With higher share of DA (coming at <9%), the marginal cost of borrowing was lower at 9.4%. In Q1 FY21, the marginal cost of borrowing is likely to be 11%+ in the absence of any form of securitization.
- ✓ As of FY20, the DA and PTC portfolio stood at Rs24bn forming ~35% of AUM. Within this, DA was ~Rs19bn. In DA transaction 100% of the risk is transferred to the bank. For PTC, the company provides a guarantee in the form of cash deposit (max 5% of transaction value). Spandana has received moratorium from all PTC investors (they accept to receive whatever amount being collected currently and will not invoke the cash collateral)
- ✓ The decline in Opex/Avg. AUM is driven by growth coming from existing branches and borrowers. Spandana's avg. AUM/Branch is still lower than peers at <Rs70mn (larger peers operating at Rs80-90mn). On reaching here, the cost metric would have further improved.
- ✓ ~Rs640mn impacted portfolio in a couple of districts of coastal Karnataka (external influence) and in some of Maharashtra (due to floods) was fully written-off in Q4 FY20
- ✓ ECL model is updated annually after fiscal end. Q4 FY20 provision run-rate slightly increased due to this revision, as the loss experience of FY20 was incorporated. Spandana has a policy of writing-off PAR 90 loans, but in some cases it also writes-off PAR 60 loans based on underlying reason for default.
- ✓ As per management, Covid will lead to higher portfolio write-off than demonetization. The impact of demonetization was acute only in few states and MFIs could carry center meetings activities (collections, disbursements, etc.). The current scenario is far worse as there was complete suspension of operations and there could be prolonged difficulties in reaching out to customers. Spandana expects normalized credit cost to be 2% in next two years.

- ✓ Within company's total borrower base of 2.6mn, about 32% are unique customers and 35% of borrowers would have one more lender. About 57% of borrowers are in dairy activity, 20-22% have a small business (shops, vegetables sellers, fruit vendors, etc.) and majority of remaining are laborers in farm, shops, house, etc.
- ✓ RBI's observation pertains to pricing of loans during the inspection of FY19 financials. A similar observation was raised in FY18 inspection also. Spandana made a provision of Rs135mn in Q4 FY20, being the amount involved in both observations. The company has also lowered its interest rate on loans to 21.55% from February 26, 2020 on RBI's directions.

Exhibit 2: Result Table

(Rs mn)	Q4 FY20	Q3 FY20	% qoq	Q4 FY19	% yoy
Total Operating Income	4,211	3,436	22.6	2,591	62.5
Interest Expenses	(822)	(844)	(2.6)	(887)	(7.3)
Net Interest Income	3,389	2,591	30.8	1,704	98.9
Other income	88	85	4.5	33	166.3
Total Income	3,477	2,676	29.9	1,737	100.2
Operating expenses	(592)	(550)	7.7	(482)	22.7
PPOP	2,885	2,126	35.7	1,255	129.9
Provisions	(1,874)	(415)	351.2	(213)	781.2
PBT	1,011	1,711	(40.9)	1,042	(3.0)
Tax	(236)	(450)	(47.5)	(332)	(28.9)
PAT	775	1,261	(38.6)	710	9.1

Source: Company, YES Sec - Research

Exhibit 3: Business and Productivity data

Particulars	Q4 FY20	Q3 FY20	chg qoq	Q4 FY19	chg yoy
Gross Loan Portfolio (Rs mn)	68,290	58,790	16.2	43,720	56.2
Disbursement (Rs mn)	23,240	19,710	17.9	13,900	67.2
Branches (no)	1,010	980	3.1	925	9.2
Employees (no)	8,224	7,545	9.0	6,655	23.6
Loan Officers (no)	6,103	5,586	9.3	4,673	30.6
Borrowers (mn)	2.6	2.5	4.5	2.5	4.5
Borrowers/Branch (no)	2,541	2,506	1.4	2,658	(4.4)
AUM/Borrowers (Rs)	26,610	23,940	11.2	17,780	49.7
AUM/Branch (Rs mn)	68	60	13.4	47	43.9
Borrower/LO (Incl. trainees)	421	440	(4.3)	526	(20.0)
AUM/LO (incl. Trainees) (Rs mn)	11.2	10.5	6.3	9.4	19.6

Source: Company, YES Sec - Research

Exhibit 4: Key ratios

Particulars	Q4 FY20	Q3 FY20	chg qoq	Q4 FY19	chg yoy
NIM	16.6	16.4	0.2	15.9	0.7
Portfolio Yield	24.0	24.0	-	26.2	(2.2)
Cost of Borrowing (WA)	11.0	10.9	0.1	12.0	(1.0)
C/I	17.0	20.7	(3.7)	27.8	(10.8)
Opex/AUM	3.9	4.0	(0.1)	4.7	(0.8)
RoA	5.2	9.1	(3.9)	7.0	(1.8)
RoE	13.0	21.1	(8.1)	15.1	(2.1)
GNPA	0.4	0.3	0.0	-	0.4
CRAR	52.9	50.5	2.4	-	52.9

Source: Company, YES Sec - Research

Exhibit 5: Branch mix

Particulars	Q4 FY20	Q3 FY20	% qoq	Q4 FY19	% yoy
MP	158	154	2.6	149	6.0
Orissa	148	145	2.1	149	(0.7)
KTK	130	130	-	139	(6.5)
MH	122	121	0.8	111	9.9
AP	112	102	9.8	83	34.9
Chattisgarh	79	78	1.3	83	(4.8)
Others	261	250	4.4	211	23.7

Source: Company, YES Sec – Research

Exhibit 6: States concentration of AUM

Particulars	Q2 FY20	Q3 FY20	Q4 FY20
MP	18.7	17.5	17.1
Orissa	18.9	17.9	17.3
KTK	12.9	13.4	12.6
MH	11.4	12.3	12.9
AP	7.2	8.2	9.2
Chattisgarh	8.9	8.6	8.1
Others	22.0	22.1	22.8

Source: Company, YES Sec – Research

Exhibit 7: District concentration of AUM

Particulars	Q2 FY20	Q3 FY20	Q4 FY20
% of Portfolio			
<0.5%	194	208	211
0.5-1%	55	52	56
1-2%	15	16	13
>2%	0	0	0
Total Districts	264	276	280

Source: Company, YES Sec – Research

Exhibit 8: Funding mix

Particulars (%)	Q2 FY20	Q3 FY20	Q4 FY20
Private banks	55.0	51.0	38.0
Public sector banks	21.0	33.0	49.0
Small finance banks	4.0	2.5	2.0
NBFCs	10.0	7.5	7.0
FPIs	6.0	5.0	4.0
Mutual funds	4.0	1.0	0.0

Source: Company, YES Sec – Research

Exhibit 9: Comfortable liquidity position

Particulars (Rs mn)	Apr-20 (A)	May-20 (A)	Jun-20 (P)
Opening Cash and cash equivalents	5,470	4,060	4,000
Loan collections (Principal & Interest)	140	1,320	3,000
Fresh Borrowings	3,000	-	5,500
Total Inflows	3,140	1,320	8,500
Disbursements	-	20	1,500
Repayment (Principal & Interest)			
- Term Loan & NCDs	2,020	1,280	2,180
- PTC & DA	2,350	40	410
Others (net)	180	50	200
Total Outflows	4,550	1,390	4,290
Closing Cash and cash equivalents	4,060	3,990	8,210

* (A) stands for actual, (P) for Projected

Source: Company, YES Sec – Research

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