

BUY Fusion Micro Finance

Your success is our success

Growth moderates, but margins accelerates

BFSI - Banks ▶ Result Update ▶ November 7, 2023

TARGET PRICE (Rs) : 810

Fusion MFI reported in-line PAT of Rs1.3bn/~5% RoA in Q2FY24, mainly on the back of healthy margins and higher 'other income', and partly offset by an elevated LLP (3.8% of loans). The company has received the first tranche of recovery from the Assam loan relief scheme (of Rs50mn) and should see further recovery going ahead. The management expects slippages/credit cost to remain elevated in the near term due to seasonality factors and its new aggressive write-off policy, but should start normalizing 4Q onwards.

Factoring-in a better margin/fee income delivery, partly offset by a higher LLP, we revise FY24-26E earnings estimate by 2-4% and expect Fusion to report a strong RoA/RoE of 4.7-5.1%/20-21%, respectively. Hence, we retain our target price at Rs810/share, valuing the stock at 2.1x its Sep-25E ABV and maintain our BUY rating.

Fusion Micro Finance: Financial Snapshot (Standalone)

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net profit	217	3,871	5,308	6,514	7,704
Loan growth (%)	46.3	37.0	25.0	24.0	23.0
NII growth (%)	25.6	68.4	32.4	23.2	20.6
NIM (%)	9.0	12.0	12.5	12.3	11.9
PPOP growth (%)	41.6	81.2	38.5	20.6	17.6
Adj. EPS (Rs)	2.7	42.3	52.9	64.8	76.7
Adj. EPS growth (%)	(51.8)	1,477.6	25.0	22.6	18.3
Adj. BV (INR)	151.5	245.0	277.6	342.6	418.0
Adj. BVPS growth (%)	5.2	61.8	13.3	23.4	22.0
RoA (%)	0.3	4.6	5.1	5.0	4.7
RoE (%)	1.7	21.2	20.5	20.5	19.8
P/E (x)	212.2	13.5	10.8	8.8	7.4
P/ABV (x)	3.8	2.3	2.0	1.7	1.4

Source: Company, Emkay Research

Growth moderates a tad, but Fusion delivers healthy margin

Fusion reported some growth moderation at 25% YoY/3.2% QoQ from 31% YoY/4% QoQ in 1Q which we believe could be partly owing to seasonal factors and the recent stress build-up in select northern pockets due to floods. But better loan yields and a surprisingly near-flat funding cost led to a 23bps QoQ jump in NIM to a high of 11.1%. Going forward, the management guides for better growth led by existing geographies (UP and Bihar) as well as new geographies in western (Gujarat)/southern (Karnataka, Tamil Nadu, Andhra Pradesh and Telangana) India. This, coupled with continual asset re-pricing/better cost management, is likely to help Fusion sustain a healthy margin trajectory.

Elevated slippages, but higher write-off led to decline in NPA ratio

Slippages stayed elevated for the second quarter in a row at 3.7% of loans due to seasonal factors, including the recent floods in northern India. However, GNPA ratio declined by 52bps to 2.7%, due to a higher write-off of Rs1bn on account of the latest change in the write-off policy (270 days vs. 360 days); NNPA ratio too declined, by 13bps to 0.7%. The management indicates that LLP would remain elevated in 3Q, given its current aggressive write-off policy, post which the LLP should start normalizing.

We retain BUY

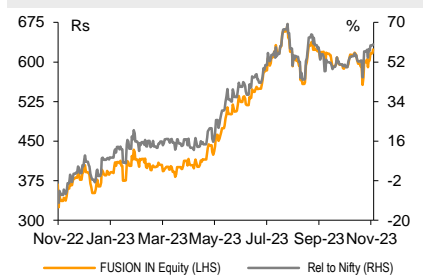
Factoring-in a better margin/fee income delivery and partly offset by the higher LLP, we revise FY24-26E earnings by 2-4% and expect Fusion to report a resilient RoA/RoE of 4.7-5.1%/20-21%, respectively. Hence, we retain our target price at Rs810/share, valuing the stock at 2.1x its Sep-25E ABV. We maintain our BUY rating on the stock. Key risks: Impact on asset quality due to rising micro/climatic disruptions, execution risk in the highly-penetrated South, managing cost in a build-up phase, and stock supply from existing investors as seen across MFI players.

Target Price – 12M	Sep-24
Change in TP (%)	NA
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	42.4
CMP (07-Nov-23) (Rs)	568.9

Stock Data	Ticker
52-week High (Rs)	691
52-week Low (Rs)	321
Shares outstanding (mn)	101.0
Market-cap (Rs bn)	57
Market-cap (USD mn)	690
Net-debt, FY24E (Rs mn)	NA
ADTV-3M (mn shares)	-
ADTV-3M (Rs mn)	153.5
ADTV-3M (USD mn)	1.8
Free float (%)	32.0
Nifty-50	19,407
INR/USD	83.3
Shareholding, Sep-23	
Promoters (%)	67.9
FPIs/MFs (%)	5.2/15.4

Price Performance

(%)	1M	3M	12M
Absolute	(3.7)	(3.9)	-
Rel. to Nifty	(2.5)	(2.9)	-

1-Year share price trend (Rs)**Anand Dama**

anand.dama@emkayglobal.com
+91 22 6624 2480

Kunaal N

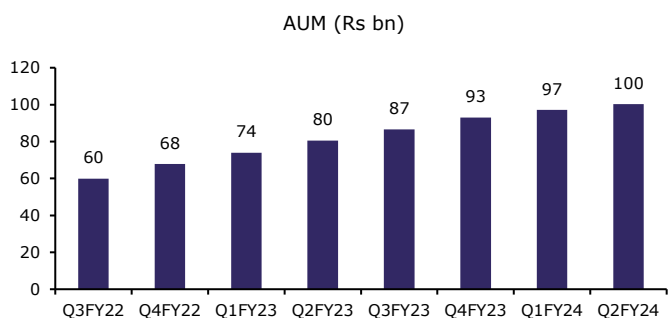
kunaal.n@emkayglobal.com
+91 22 6612 1275

Marazbaan Dastur

marazbaan.dastur@emkayglobal.com
+91 22 6612 1281

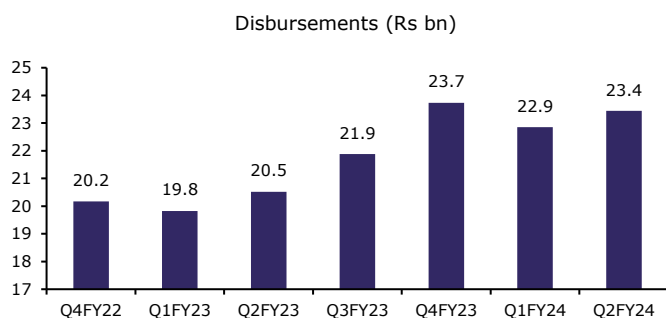
Story in Charts

Exhibit 1: AUM touched the milestone of Rs.100bn...



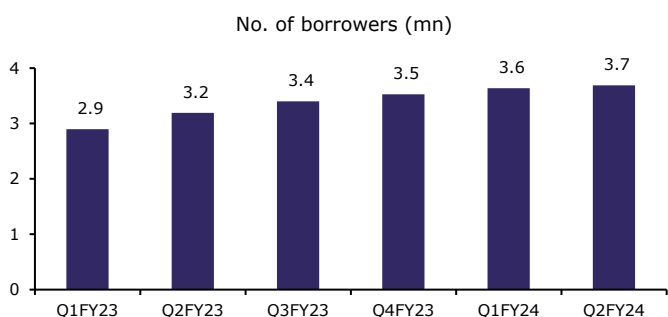
Source: Company, Emkay Research

Exhibit 2: ...led by strong disbursements



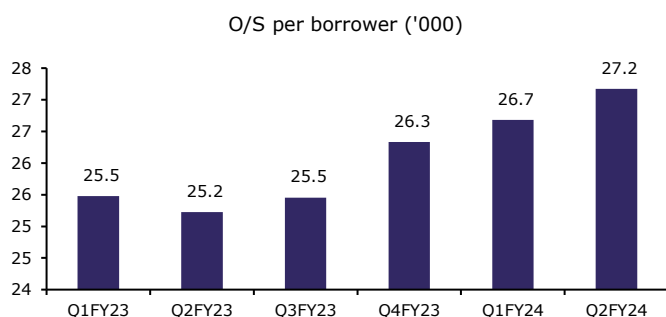
Source: Company, Emkay Research

Exhibit 3: Customer base grew 16% YoY...



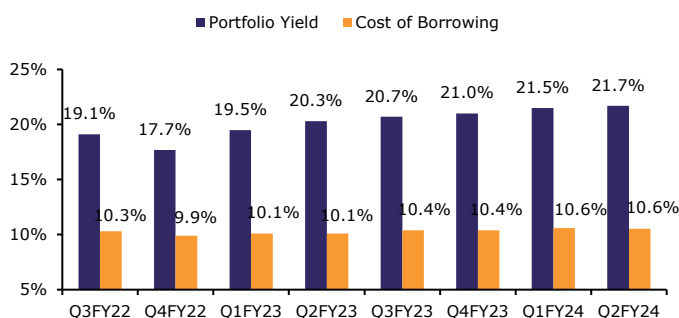
Source: Company, Emkay Research

Exhibit 4: ...with steady increase in o/s per borrower



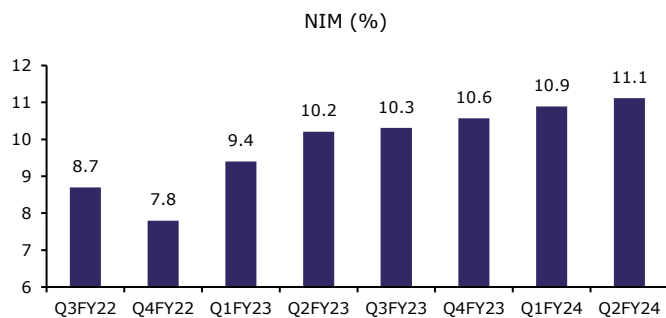
Source: Company, Emkay Research

Exhibit 5: Better portfolio yields, coupled with contained CoF...



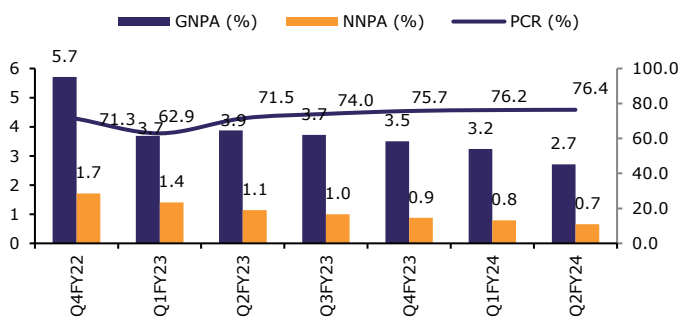
Source: Company, Emkay Research

Exhibit 6: ...led to continued margin expansion



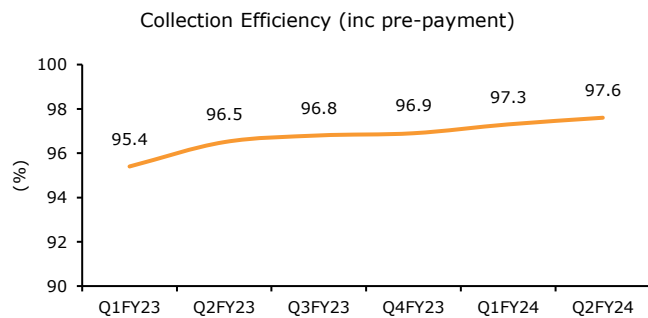
Source: Company, Emkay Research

Exhibit 7: Receding GNPA + rising PCR led to lower NNPA



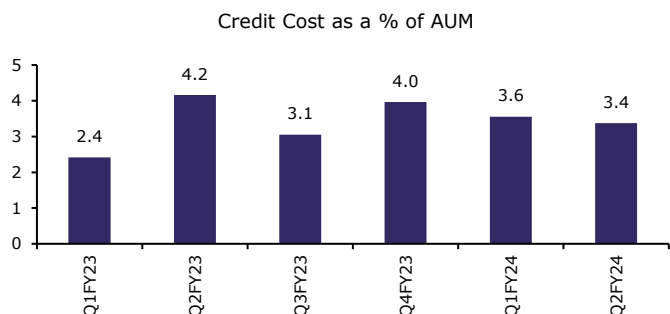
Source: Company, Emkay Research

Exhibit 8: Collection efficiency continued to improve



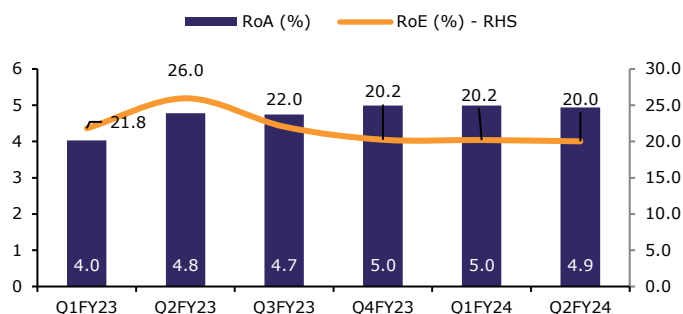
Source: Company, Emkay Research

Exhibit 9: Credit cost remained elevated due to rising PCR + management overlay + aggressive write-off policy



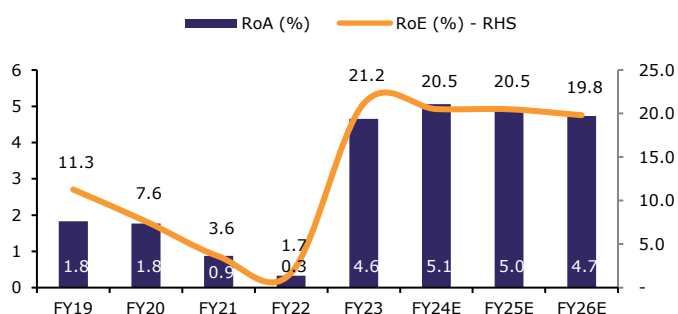
Source: Company, Emkay Research

Exhibit 10: Return ratios remain healthy



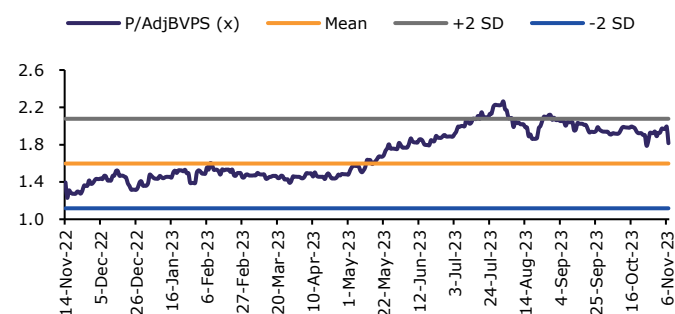
Source: Company, Emkay Research

Exhibit 11: Strong growth/margins, partly offset by elevated credit cost, to keep return ratios healthy



Source: Company, Emkay Research

Exhibit 12: The stock trades at 2.1x its one-year forward ABV



Source: Bloomberg, Emkay Research

Exhibit 13: Actuals vs Estimates (Q2FY24)

(Rs mn)	Actuals	Estimates		Variation		Comments
		Emkay	Consensus	Emkay	Consensus	
Net income	3,803	3,685	NA	3%	NA	Better margins, higher other income led to a beat
PPOP	2,418	2,324	NA	4%	NA	Higher Net income led to a beat
PAT	1,257	1,275	1,216	-1%	3%	Higher PPOP, partly offset by higher provisions, led to beat

Source: Company, Emkay Research

Exhibit 14: Quarterly Summary

(Rs mn)	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	YoY (%)	QoQ (%)	FY23A	FY24E	YoY (%)
Interest Earned	3,998	4,202	4,507	4,790	4,968	24	4	16,001	20,895	31
Interest Exp.	1,573	1,680	1,742	1,835	1,910	21	4	6,428	8,222	28
Net Interest Income	2,424	2,522	2,765	2,955	3,058	26	3	9,573	12,673	32
Global NIMs (reported)	10.21	10.31	10.57	10.89	11.12	91bps	23bps	8.54	9.29	74bps
Non-interest Income	526	463	700	738	745	42	1	1,999	2,911	46
Operating Expenses	1,077	1,147	1,253	1,339	1,385	29	3	4,448	5,720	29
Pre Provisioning Profit	1,873	1,838	2,211	2,354	2,418	29	3	7,124	9,864	38
Provision & Contingencies	612	499	692	759	762	25	0	2,004	2,768	38
PBT	1,261	1,339	1,519	1,595	1,656	31	4	5,120	7,096	39
Income Tax Expense (Gain)	310	314	374	390	399	29	2	1,248	1,788	43
Net Profit/(Loss)	951	1,025	1,145	1,205	1,257	32	4	3,871	5,308	37
Gross NPA (%)	3.87	3.72	3.50	3.24	2.72	-116bps	-52bps	1.14	5.67	453bps
Net NPA (%)	1.14	0.99	0.87	0.79	0.65	-48bps	-13bps	0.39	2.35	196bps
Net Advances (Rs bn)	70	76	80	84	87	24	3	80	102	26

Source: Company, Emkay Research

Exhibit 15: Revision in Estimates

Y/E March (Rs mn)	FY24E			FY25E			FY26E		
	Earlier	Revised	Change	Earlier	Revised	Change	Earlier	Revised	Change
Net income	15,186	15,584	2.6%	18,388	19,037	3.5%	22,042	22,615	2.6%
PPOP	9,603	9,864	2.7%	11,472	11,897	3.7%	13,604	13,990	2.8%
PAT	5,199	5,308	2.1%	6,234	6,514	4.5%	7,385	7,704	4.3%
EPS (Rs)	51.8	52.9	2.0%	62.1	64.8	4.3%	73.6	76.7	4.2%
BV (Rs)	282.4	283.3	0.3%	344.5	348.0	1.0%	418.1	424.6	1.6%

Source: Emkay Research

Exhibit 16: Key Assumptions

	FY23A	FY24E	FY25E	FY26E
Loan Growth (%)	35.9	26.3	25.8	24.1
Deposit Growth (%)	37.0	25.0	24.0	23.0
NIM (%)	12.0	12.5	12.3	11.9
GNPA (%)	3.5	2.3	1.9	2.1
Credit Cost (%)	2.8	3.0	2.7	2.5

Source: Emkay Research

Fusion Micro Finance : Standalone Financials and Valuations

Profit & Loss

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	10,643	16,001	20,895	25,826	31,203
Interest Expense	4,960	6,428	8,222	10,207	12,369
Net interest income	5,684	9,573	12,673	15,619	18,834
NII growth (%)	25.6	68.4	32.4	23.2	20.6
Other income	1,370	1,999	2,911	3,419	3,781
Total Income	7,054	11,572	15,584	19,037	22,615
Operating expenses	3,123	4,448	5,720	7,140	8,625
PPOP	3,931	7,124	9,864	11,897	13,990
PPOP growth (%)	41.6	81.2	38.5	20.6	17.6
Core PPOP	3,931	7,124	9,864	11,897	13,990
Provisions & contingencies	3,687	2,004	2,768	3,188	3,690
PBT	244	5,120	7,096	8,709	10,300
Extraordinary items	0	0	0	0	0
Tax expense	27	1,248	1,788	2,195	2,596
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	217	3,871	5,308	6,514	7,704
PAT growth (%)	(50.7)	1,685.4	37.1	22.7	18.3
Adjusted PAT	217	3,871	5,308	6,514	7,704
Diluted EPS (Rs)	2.6	41.6	52.1	63.9	75.5
Diluted EPS growth (%)	(51.9)	1,475.6	25.2	22.6	18.3
DPS (Rs)	0.0	0.0	0.0	0.0	0.0
Dividend payout (%)	0.0	0.0	0.0	0.0	0.0
Effective tax rate (%)	11.2	24.4	25.2	25.2	25.2
Net interest margins (%)	9.0	12.0	12.5	12.3	11.9
Cost-income ratio (%)	44.3	38.4	36.7	37.5	38.1
Shares outstanding (mn)	92.3	108.3	108.5	108.5	108.5

Source: Company, Emkay Research

Asset quality and other metrics

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Asset quality					
Gross NPLs	3,584.3	2,889.0	2,397.7	2,449.6	3,336.6
Net NPLs	1,030.3	707.9	575.5	538.9	667.3
GNPA ratio (%)	5.8	3.5	2.3	1.9	2.1
NNPA ratio (%)	1.7	0.9	0.6	0.4	0.4
Provision coverage (%)	71.3	75.5	76.0	78.0	80.0
Gross slippages	3,959.8	1,776.7	1,964.9	2,593.6	3,548.1
Gross slippage ratio (%)	6.4	2.2	1.9	2.0	2.2
LLP ratio (%)	6.9	2.8	3.0	2.7	2.5
NNPA to networth (%)	7.7	3.0	2.0	1.5	1.5
Capital adequacy					
Total CAR (%)	21.9	27.9	27.2	26.5	26.0
Tier-1 (%)	19.9	27.0	26.4	25.7	25.2
CET-1 (%)	2.0	0.9	0.8	0.8	0.8
RWA-to-Total Assets (%)	83.1	88.4	90.4	91.4	92.4
Miscellaneous					
Total income growth (%)	37.6	49.8	32.3	22.8	19.6
Opex growth (%)	41.7	42.5	28.6	24.8	20.8
Core PPOP growth (%)	41.6	81.2	38.5	20.6	17.6
PPOP margin (%)	6.0	8.6	9.4	9.1	8.6
PAT/PPOP (%)	5.5	54.3	53.8	54.8	55.1
LLP-to-Core PPOP (%)	93.8	28.1	28.1	26.8	26.4
Yield on advances (%)	21.0	23.1	23.1	22.6	21.8
Cost of funds (%)	9.7	10.2	10.8	10.6	10.2

Source: Company, Emkay Research

Balance Sheet

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	923	1,083	1,085	1,085	1,085
Reserves & surplus	12,457	22,136	27,444	33,958	41,662
Net worth	13,380	23,219	28,528	35,043	42,747
Deposits	0	0	0	0	0
Borrowings	57,758	67,784	84,575	1,07,968	1,35,003
Interest bearing liab.	57,758	67,784	84,575	1,07,968	1,35,003
Other liabilities & prov.	1,767	2,632	2,968	2,384	2,232
Total liabilities & equity	72,905	93,635	1,16,071	1,45,394	1,79,982
Net advances	59,182	80,416	1,01,596	1,27,768	1,58,608
Investments	0	0	0	0	0
Cash, other balances	11,536	10,650	11,620	14,409	17,723
Interest earning assets	70,718	91,066	1,13,216	1,42,177	1,76,331
Fixed assets	192	212	224	191	246
Other assets	1,995	2,357	2,631	3,026	3,405
Total assets	72,905	93,635	1,16,071	1,45,394	1,79,982
BVPS (Rs)	165.4	253.6	284.1	348.8	425.4
Adj. BVPS (INR)	157.0	248.5	280.3	345.2	421.0
Gross advances	67,860	92,960	1,16,200	1,44,088	1,77,228
Credit to deposit (%)	102.5	118.6	120.1	118.3	117.5
CASA ratio (%)	17.0	11.5	10.0	10.0	10.0
Cost of deposits (%)	9.7	10.2	10.8	10.6	10.2
Loans-to-Assets (%)	81.2	85.9	87.5	87.9	88.1
Net advances growth (%)	46.3	37.0	25.0	24.0	23.0
Deposit growth (%)	30.3	17.4	24.8	27.7	25.0
Book value growth (%)	4.8	53.3	12.0	22.8	22.0

Source: Company, Emkay Research

Valuations and key Ratios

Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	212.2	13.5	10.8	8.8	7.4
P/B (x)	3.5	2.3	2.0	1.6	1.3
P/ABV (x)	3.8	2.3	2.0	1.7	1.4
P/PPOP (x)	13.4	8.7	6.3	5.2	4.4
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
DuPont-RoE split (%)					
NII/avg assets	8.7	11.5	12.1	11.9	11.6
Other income	2.1	2.4	2.8	2.6	2.3
Fee income	1.6	1.9	2.2	2.1	1.9
Opex	4.8	5.3	5.5	5.5	5.3
PPOP	6.0	8.6	9.4	9.1	8.6
Core PPOP	6.0	8.6	9.4	9.1	8.6
Provisions	5.6	2.4	2.6	2.4	2.3
Tax expense	0.0	1.5	1.7	1.7	1.6
RoA (%)	0.3	4.6	5.1	5.0	4.7
Leverage ratio (x)	5.1	4.6	4.1	4.1	4.2
RoE (%)	1.7	21.2	20.5	20.5	19.8

Quarterly data

Rs mn, Y/E Mar	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
NII	2,424	2,522	2,765	2,955	3,058
NIM(%)	10.2	10.3	10.6	10.9	11.1
PPOP	1,873	1,838	2,211	2,354	2,418
PAT	951	1,025	1,145	1,205	1,257
EPS (Rs)	11.48	10.22	11.41	12.00	12.52

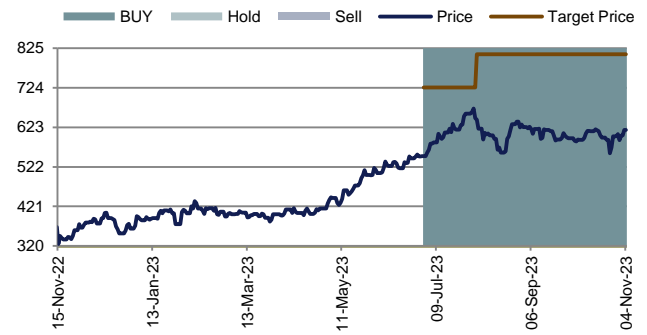
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	Closing Price (INR)	TP (INR)	Rating	Analyst
03-Aug-23	643	810	Buy	Anand Dama
01-Jul-23	549	725	Buy	Anand Dama

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Bloomberg, Company, Emkay Research

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Emkay Global Financial Services Ltd.

CIN - L67120MH1995PLC084899

7th Floor, The Ruby, Senapati Bapat Marg, Dadar - West, Mumbai - 400028. India

Tel: +91 22 66121212 Fax: +91 22 66121299 Web: www.emkayglobal.com

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