

31 October 2023

India | Equity Research | Q2FY24 results review

Spandana Spoorthy Financial

Financial Services

RoA sustains at >5% for third consecutive quarter; RoE expands to 15%

Since the new management took charge in Mar'22, Spandana Spoorthy (Spandana) embarked on a transformation journey to build a long-term sustainable micro-finance business model. Ever since, Spandan's earnings trajectory kept improving (all the past six quarters) – RoA expanding to 5.5% by Q2FY24, from 2.9% in Q2FY23; RoE expanding to 15% by Q2FY24, from 8% in Q2FY23. While business growth momentum sustained in Q2FY24, evident in strong 11% QoQ AUM growth and NNPL falling to 0.4%, a drop in collection efficiency to 97.7% versus 98.1% QoQ and 1-90 DPD portfolio increasing to 2.04% versus 1.36% QoQ pose risks to the credit cost trajectory ahead. However, management highlighted that the drop in collection is transitory in nature led by change in collection frequency for customers as part of its 'Project Parivartan'. Maintain **BUY** and target price of INR 1,100, valuing at 2x Sep'24E BVPS.

AUM growth stood at 11% QoQ, one of the highest within MFI space and driven by new customer acquisition

Spandana spent initial phase of FY23 towards redefining its business model, which includes: 1) Improving people practices and communication – initiated Town Hall meetings for two-way communication, introduction of Mediclaim for all employees, long service awards etc. 2) Weekly model: Expect ~80% of AUM by FY25 will be on weekly collection. 3) Focus on customer-led growth. 4) Geographical mitigation approach – by FY25, no single state would contribute >12% of total AUM. 5) Focus on JLG: 5 days a week meeting, 5 members per group and 5 groups per centre. While management has highlighted that all of the above initiatives are a work in progress, it has refocused on growth from H2FY23. AUM growth momentum sustained in Q2FY24 as reflected in 11% QoQ growth largely driven by new customer acquisition as reflected in total borrower base increasing to 2.7mn (up 12% QoQ) during Q2FY24. Notably, average outstanding per borrower fell for the second consecutive quarter to ~INR 36,000. Disbursement stood at INR 25bn and is well on course to disburse INR 100bn in FY24. Further, management sounded confident of scaling AUM to >INR 120bn by FY24, translating into 35-40% YoY growth.

Financial Summary

Y/E March (INR mn)	FY22A	FY23A	FY24E	FY25E
Net Interest Income (NII)	7,964	8,196	12,703	16,800
PAT	698	124	5,154	7,242
EPS (INR)	10.1	1.7	72.6	102.0
% Chg YoY	(55.3)	(82.7)	4,054.8	40.5
P/E (x)	90.3	522.4	12.6	8.9
P/BV (x)	2.0	2.1	1.8	1.5
GNPA (%)	15.0	2.1	2.0	2.0
RoAA (%)	0.9	0.2	4.7	5.1
RoAE (%)	2.4	0.4	15.4	18.2

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Market Data

Market Cap (INR)	65bn
Market Cap (USD)	779mn
Bloomberg Code	SPANDANA IN
Reuters Code	SPAD BO
52-week Range (INR)	920 /470
Free Float (%)	24.0
ADTV-3M (mn) (USD)	2.6

Price Performance (%)	3m	6m	12m
Absolute	8.2	52.8	52.3
Relative to Sensex	10.9	46.8	44.0

ESG Disclosure	2021	2022	Change
ESG score	-	-	-
Environment	-	-	-
Social	-	-	-
Governance	-	-	-

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Previous Reports

25-07-2023: [Q1FY24 results review](#)

25-05-2023: [Company update](#)

Third straight quarter of RoA sustaining at >5%

Spandana sustained its improving trajectory in financial performance for the sixth consecutive quarter as reflected in 5% QoQ growth in PAT at INR 1.3bn, translating into >5% RoA during Q2FY24. Earnings were driven by robust core income growth (adjusted for DA income), which grew 8% QoQ supported by stable NIMs at 14.1% and strong credit growth at 11% QoQ. DA income of INR 0.6bn also supported the top-line. Operating expenses grew 11% QoQ, as the company continued to invest towards franchise building. The company added 200 new branches and 1,500 employees in Q2FY24. Despite that, the cost to income ratio reduced to 65% with AUM growth driving efficiencies. Improvement in profitability was partially offset by a spike in credit costs to INR 0.9bn from INR 0.6bn, led by one-off impairment cost towards SR and pre-Apr'21 book.

'Project Parivartan' led to drop in collection, but transitory in nature and right step towards building long-term sustainable franchise

While management committed towards achieving its full year FY24 growth (35-40%) and profitability guidance, it also remained at the forefront of taking initiative to build long-term sustainable franchise, even if it leads to temporary disruption in business momentum. In line with this, it launched 'Project Parivartan', wherein it proposed shifting repayment policy to first week of the month (Monday to Friday), from the previous practice of collecting on the 1st and 10th day of the month. The company implemented this project at 700 of its existing branches in Q2FY24, covering 1.5mn customers. Owing to the administrative issues thereby, gross collection efficiency dropped to 100% in Q2FY24, from 102% in Q1FY24. The impact of the lower collections also resulted in a rise in the early delinquencies as the 1-30dpd/31-60dpd/61-90dpd to 0.85%/0.60%/0.59% versus 0.55%/0.42%/0.39% in Q1FY24. Gross NPA, on the other hand, saw an improvement as it fell 23bps QoQ to 1.4%. Management highlighted that the rise in the early buckets is transitory in nature and will normalise in subsequent quarters. With respect to the other branches, where the project is yet to be implemented, management plans to do so in calibrated manner, as these branches are relatively larger in size. Overall, management sounded confident on bettering credit costs in the coming quarters. The company continues to maintain adequate provisions with stage-3 PCR of 70.3% in Q2FY24 versus 70.1% in Q1FY24.

Strong borrower profile with >60% of the customers having less than 2 lenders; it plans to increase the share to ~80%

Following its customer-led growth journey, Spandana continued to improve its new customer acquisition run-rate – added 0.35mn new customers during Q2FY24 (vs. 0.26mn in Q1FY24 vs. 0.12mn in Q2FY23). Notably, it continued to focus on onboarding quality customers reflecting in ~33% unique borrowers and another 30% borrowers having additional loans from other lenders. The company plans to further this share by specifically targeting only those geographies where it can get a single-lender relationship. It aims to increase unique customers to 38%, with unique-plus-one-additional lender share being at ~80%.

Diversifying lender base to drive lower cost of funds; NIM to remain steady at 14%, but on sustainable range would be ~12.5%

With sustained improved operating performance and controlled asset quality, Spandana has been able to add three big players to its liability mix, i.e., SBI, NABARD and SIDBI. The same helped it lower marginal cost of borrowing by 30bps to 12.3% in Q2FY24 from 12.6% in Q4FY23. Further, the company also received a rating upgrade from ICRA to A/Stable, with ICRA, CRISIL and India Ratings exhibiting the same rating outstanding on the company. With strong operating performance and recent rating upgrade, the company expects active participation from the public sector banks, which

will further help it to improve cost of borrowings going forward. However, as the company funds its incremental growth through debt, management expects NIMs to settle at ~12.5% as the gearing reaches 4 times in the medium term. Nevertheless, it is expected to be offset by the steady-state credit cost level of ~2%, which will keep overall RoAs 5% on a sustainable-basis.

Key risks: Stress unfolding higher than anticipated; and operational instability caused by outside interference.

Exhibit 1: Q2FY24 result review

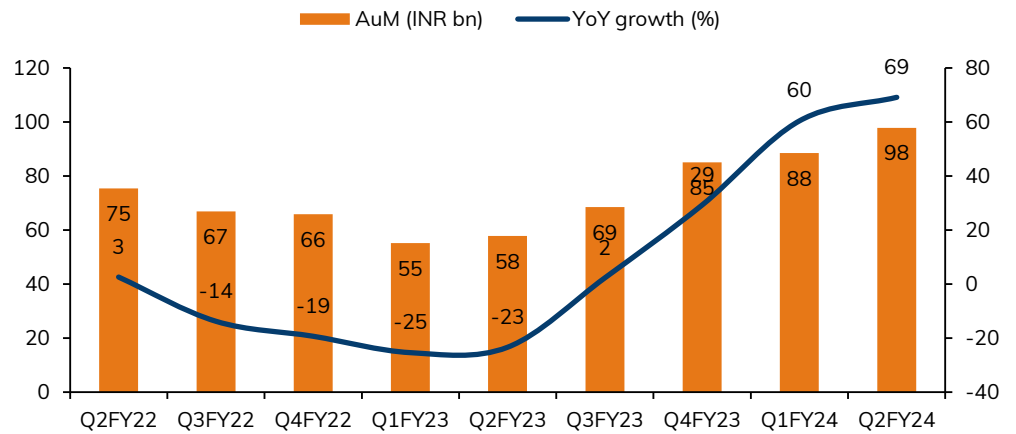
(INR mn)	Q2FY24	Q2FY23	% change YoY	Q1FY24	% change QoQ
Interest Income	6,103	2,977	105.0	5,116	19.3
Interest Expended	2,277	914	149.3	1,995	14.1
Net interest income (NII)	3,825	2,063	85.4	3,121	22.6
Other income	300	125	140.3	157	91.1
Total income	4,125	2,188	88.5	3,277	25.9
Operating expenses	1,549	1,088	42.4	1,386	11.8
-Staff expenses	1,120	722	55.2	1,031	8.7
-Other expenses	429	366	17.4	356	20.7
Operating profit	2,576	1,100	134.1	1,891	36.2
Total provisions	901	258	249.7	286	215.1
Profit before tax	1,675	843	98.7	1,605	4.3
Tax	423	291	45.4	411	3.0
Profit after tax	1,252	552	126.9	1,195	4.8

Key statistic			% change YoY		% change QoQ
AuM (INR Mn)	97,840	57,820	69.2	88,480	10.6
Borrowers (in Lakh)	27	22	24.4	24	12.0
Calc. Avg ticket size (INR)	36,237	26,645	36.0	36,714	(1.3)

Ratios (%)			bp change YoY		bp change QoQ
Profitability ratios					
Portfolio Yields	24.5	19.5	500	24.0	50
Cost of Funds	12.5	11.2	130	12.5	-
NIM	14.1	13.0	110	14.2	(10)
RoAum	5.5	2.9	260	6.0	(42)
Asset Quality					
Gross NPL ratio	1.3	7.3	(604)	1.5	(22)
Business & Other Ratios					
Cost-income ratio	37.6	49.7	(1,215)	42.3	(474)
CAR	36.6	45.3	(870)	37.6	(100)

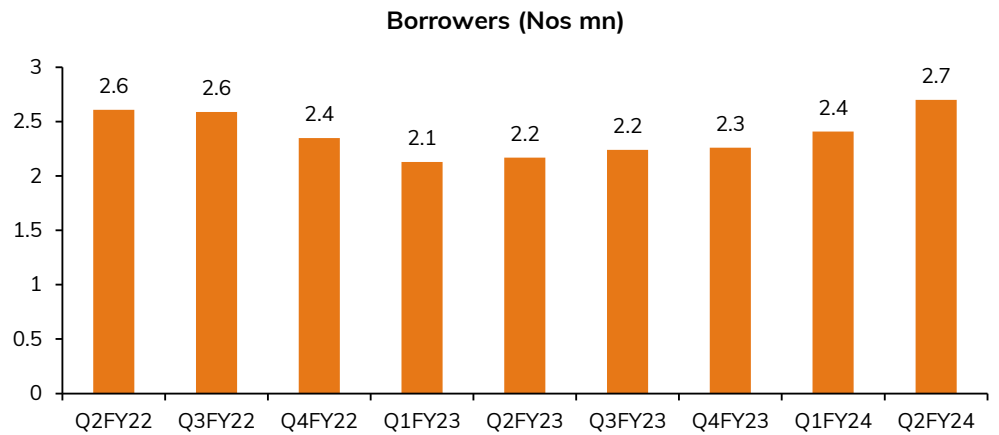
Source: Company data, I-Sec research

Exhibit 2: Growth momentum sustained as AUM grew 69% YoY/11%QoQ



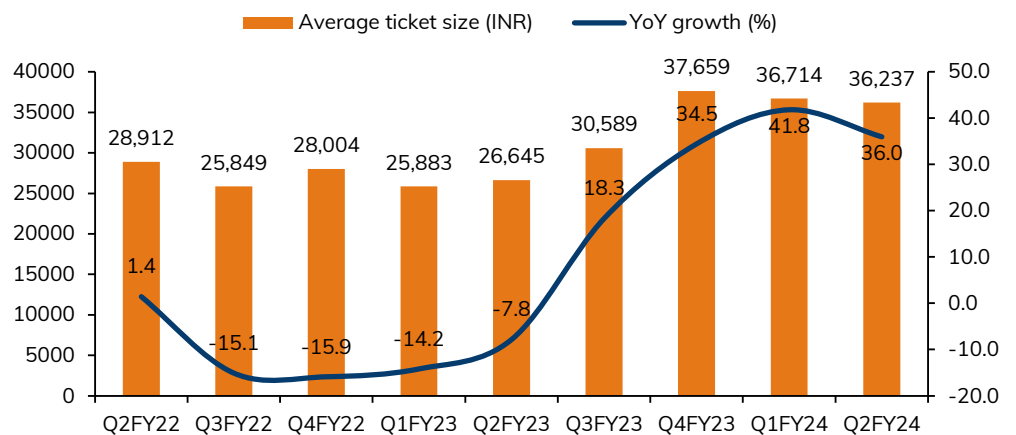
Source: Company data, I-Sec research

Exhibit 3: Q2FY24 sees 0.3mn new customers; total borrower base grew 24% YoY



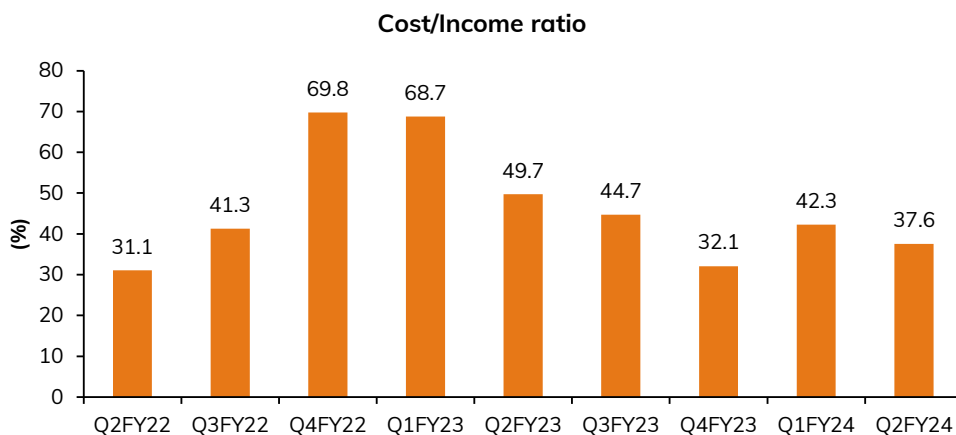
Source: Company data, I-Sec research

Exhibit 4: Average ticket-size at INR 36,237, remains lower than industry average



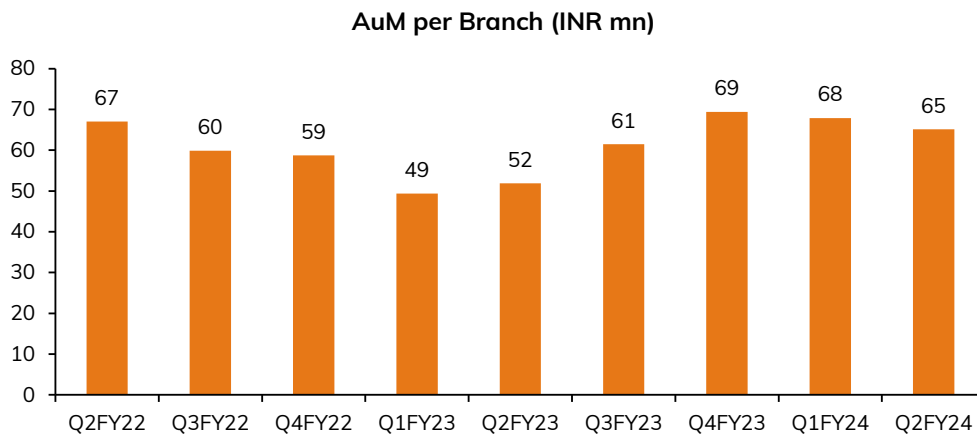
Source: Company data, I-Sec research

Exhibit 5: Q2FY24 cost-to-income improves to 37.6%



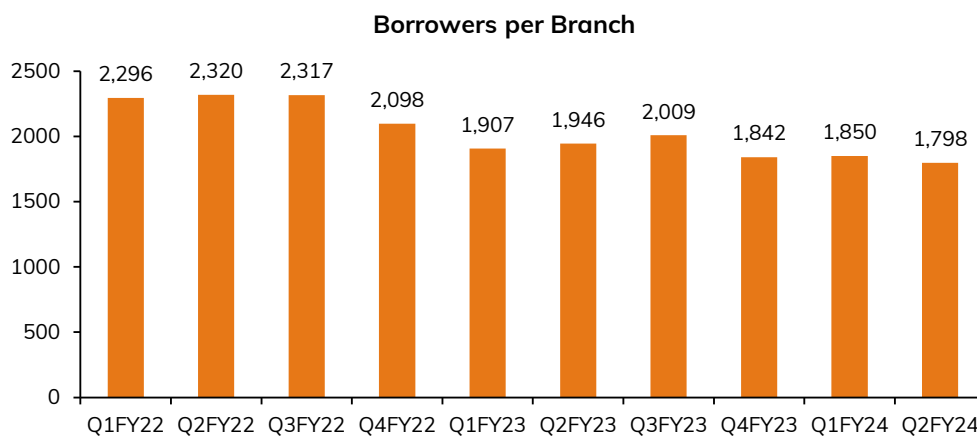
Source: Company data, I-Sec research

Exhibit 6: AUM per branch declined as company added 200 branches in Q2FY24; with 95 branches yet to start operations...



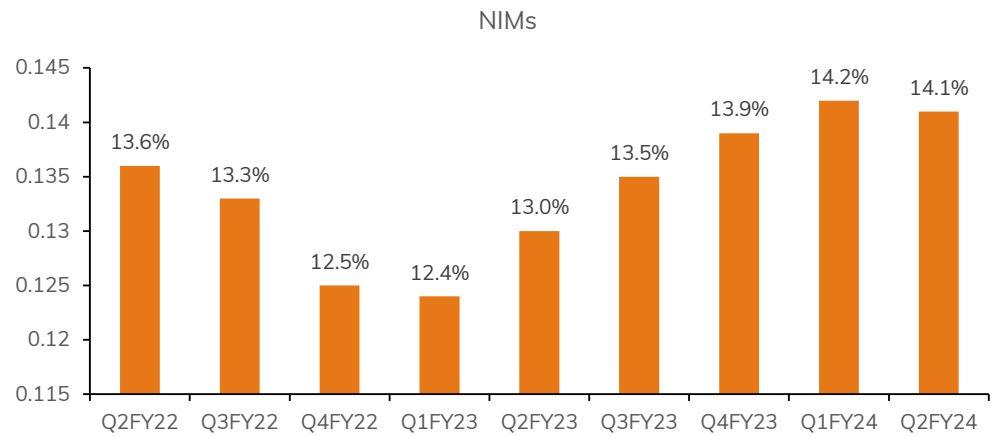
Source: Company data, I-Sec research

Exhibit 7: ...which also resulted in decline in the borrowers per branch



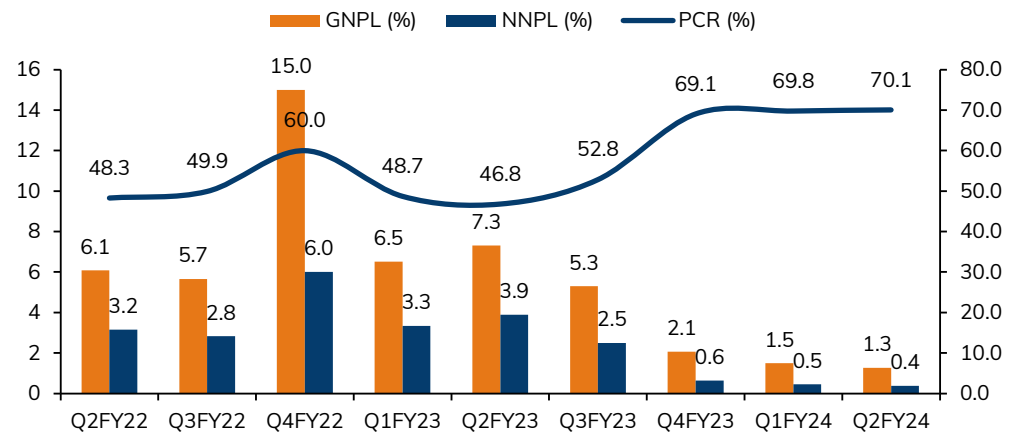
Source: Company data, I-Sec research

Exhibit 8: NIMs remain flat at 14.1%



Source: Company data, I-Sec research

Exhibit 9: GNPL fell further by 23bps QoQ to 1.4%; PCR maintained at 70%



Source: Company data, I-Sec research

Exhibit 10: Shareholding pattern

%	Mar'23	Jun'23	Sep'23
Promoters	63.0	62.4	60.4
Institutional investors	28.7	29.7	31.8
MFs and other	0.6	0.6	1.3
Banks/ FIs	0.3	0.3	0.3
Insurance Cos.	4.1	4.1	8.0
FIs	23.7	24.6	22.2
Others	8.3	7.9	7.8

Source: Bloomberg, I-Sec research

Exhibit 11: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 12: Profit & Loss

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Interest Income	13,365	12,775	20,775	27,663
Interest Expenses	(5,401)	(4,579)	(8,072)	(10,863)
Net Interest Income (NII)	7,964	8,196	12,703	16,800
Other Income	1,435	1,995	1,798	2,079
Total Income (net of interest expenses)	9,399	10,192	14,502	18,879
Employee benefit expenses	(2,284)	(3,057)	(3,730)	(4,550)
Depreciation and amortization	(92)	(109)	(110)	(120)
Other operating expenses	(1,249)	(1,404)	(1,657)	(1,988)
Total Operating Expense	(3,625)	(4,570)	(5,497)	(6,659)
Pre Provisioning Profits (PPoP)	5,774	5,622	9,005	12,221
Provisions and write offs	(4,806)	(5,443)	(2,118)	(2,543)
Profit before tax (PBT)	969	178	6,887	9,678
Total tax expenses	(270)	(54)	(1,733)	(2,436)
Profit after tax (PAT)	698	124	5,154	7,242

Source Company data, I-Sec research

Exhibit 13: Balance sheet

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Share capital	691	710	710	710
Reserves & surplus	30,209	30,283	35,436	42,678
Shareholders' funds	30,899	30,992	36,146	43,388
Borrowings	37,721	60,743	86,016	1,11,501
Provisions	1,861	2,051	2,051	2,051
Deferred tax liabilities (net)	282	40	40	40
Other Liabilities	1,861	2,051	2,051	2,051
Total Liabilities and Stakeholder's Equity	70,763	93,826	1,24,253	1,56,979
Fixed assets	68	249	249	249
Loans	55,184	77,598	1,07,070	1,36,124
Investments	24	1,894	750	750
Deferred tax assets (net)	2,030	2,364	2,364	2,364
Current Assets including cash and bank	12,022	10,045	11,778	14,974
Other Assets	1,434	1,677	2,043	2,519
Total Assets	70,763	93,826	1,24,253	1,56,979

Source Company data, I-Sec research

Exhibit 14: Key Ratios

(Year ending March)

	FY22A	FY23A	FY24E	FY25E
AUM and Disbursements (INR mn)				
AUM	65,810	85,110	1,17,659	1,49,587
Disbursements	33,730	81,250	95,904	1,12,475
Repayments	49,490	61,950	63,355	80,547
Growth (%):				
Total AUM (%)	(19.3)	29.3	38.2	27.1
Disbursements (%)	(47.5)	140.9	18.0	17.3
Repayments (%)	(2.9)	25.2	2.3	27.1
Total Assets (%)	(17.5)	32.6	32.4	26.3
Net Interest Income (NII) (%)	(15.2)	2.9	55.0	32.2
Non-interest income (%)	0.5	39.1	(9.9)	15.6
Total Income (net of interest expenses) (%)	(13.2)	8.4	42.3	30.2
Operating Expenses (%)	53.0	26.1	20.3	21.1
Employee Cost (%)	33.1	33.9	22.0	22.0
Non-Employee Cost (%)	116.5	12.4	18.0	20.0
Pre provisioning operating profits (PPoP) (%)	(31.7)	(2.6)	60.2	35.7
Provisions (%)	(25.5)	13.3	(61.1)	20.1
PBT (%)	(51.7)	(81.6)	3,760.9	40.5
PAT (%)	(52.0)	(82.2)	4,054.8	40.5
EPS (%)	(55.3)	(82.7)	4,054.8	40.5
Yields, interest costs and spreads (%)				
NIM on loan assets (%)	14.4	10.6	11.9	12.3
NIM on IEA (%)	9.2	9.5	11.3	11.4
NIM on AUM (%)	10.8	10.9	12.5	12.6
Yield on loan assets (%)	24.2	16.5	19.4	20.3
Yield on IEA (%)	15.4	14.8	18.5	18.8
Yield on AUM (%)	18.1	16.9	20.5	20.7
Cost of borrowings (%)	11.8	9.3	11.0	11.0
Interest Spreads (%)	9.7	9.9	11.5	11.8
Operating efficiencies				
Non-interest income as % of total income	9.7	13.5	8.0	7.0
Cost to income ratio	38.6	44.8	37.9	35.3
Op.costs/avg assets (%)	4.6	5.6	5.0	4.7
Op.costs/avg AUM (%)	4.9	6.1	5.4	5.0
No of employees (estimate) (x)	8,763	10,016	-	-
No of branches (x)	1,120	1,227	1,337	1,462
Salaries as % of non-interest costs (%)	63.0	66.9	67.9	68.3
NII /employee (INR mn)	0.9	0.8	-	-
AUM/employee(INR mn)	7.5	8.5	-	-
AUM/ branch (INR mn)	58.8	69.4	88.0	102.3
Capital Structure				
Average gearing ratio (x)	1.2	2.0	2.4	2.6
Leverage (x)	2.3	3.0	3.4	3.6
CAR (%)	50.0	36.3	34.2	32.5
Tier 1 CAR (%)	49.0	35.3	33.2	31.5
Tier 2 CAR (%)	1.0	1.0	1.0	1.0
RWA (estimate) - INR mn	56,610	79,752	1,05,615	1,33,432
RWA as a % of loan assets	102.6	102.8	98.6	98.0

Source Company data, I-Sec research

	FY22A	FY23A	FY24E	FY25E
Asset quality and provisioning				
GNPA (%)	15.0	2.1	2.0	2.0
NNPA (%)	6.0	0.6	0.5	0.5
GNPA (INR mn)	8,278	1,606	2,141	2,722
NNPA (INR mn)	971	3,311	497	535
Coverage ratio (%)	60.0	69.1	75.0	75.0
Credit Costs as a % of avg AUM (bps)	652	721	209	190
Credit Costs as a % of avg on book loans (bps)	652	721	209	190
Return ratios				
RoAA (%)	0.9	0.2	4.7	5.1
RoAE (%)	2.4	0.4	15.4	18.2
ROAAUM (%)	0.9	0.2	5.1	5.4
Valuation Ratios				
No of shares	69	71	71	71
No of shares (fully diluted)	69	71	71	71
ESOP Outstanding	-	-	-	-
EPS (INR)	10.1	1.7	72.6	102.0
EPS fully diluted (INR)	10.1	1.7	72.6	102.0
Price to Earnings (x)	90.3	522.4	12.6	8.9
Price to Earnings (fully diluted) (x)	90.3	522.4	12.6	8.9
Book Value (fully diluted)	447	437	509	611
Adjusted book value	437	402	504	606
Price to Book	2.0	2.1	1.8	1.5
Price to Adjusted Book	2.1	2.3	1.8	1.5

Source Company data, I-Sec research

Exhibit 15: Key Metrics

(Year ending March)

	FY22A	FY23A	FY24E	FY25E
DuPont Analysis				
Average Assets (INR mn)	78,266	82,294	1,09,039	1,40,616
Average Loans (INR mn)	62,257	66,391	92,334	1,21,597
Average Equity (INR mn)	29,195	30,946	33,569	39,767
Interest earned (%)	17.1	15.5	19.1	19.7
Net gain on fair value changes (%)	-	-	-	-
Interest expended (%)	6.9	5.6	7.4	7.7
Gross Interest Spread (%)	10.2	10.0	11.7	11.9
Credit cost (%)	6.1	6.6	1.9	1.8
Net Interest Spread (%)	4.0	3.3	9.7	10.1
Operating cost (%)	4.6	5.6	5.0	4.7
Lending spread (%)	(0.6)	(2.2)	4.7	5.4
Non-interest income (%)	1.8	2.4	1.6	1.5
Operating Spread (%)	1.2	0.2	6.3	6.9
Tax rate (%)	27.9	30.5	25.2	25.2
ROAA (%)	0.9	0.2	4.7	5.1
Effective leverage (AA/ AE)	2.7	2.7	3.2	3.5
RoAE (%)	2.4	0.4	15.4	18.2

Source Company data, I-Sec research

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