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SPANDANA SPHOORTY FINANCIAL LTD

August 02, 2019

SMC Ranking

★★☆☆☆ (2/5)

Issue Highlights

Industry	NBFC
Offer for sale (Shares)	9,356,725
Fresh Issue (Shares)	4,672,897
Total Offer	14,029,622
Issue Size (Rs. Cr.)	1196-1200
Price Band (Rs.)	853-856
Offer Date	5-Aug-19
Close Date	7-Aug-19
Face Value	10
Lot Size	17

Issue Composition

	In shares
Total Issue for Sale	14029622
QIB	7,014,811
NIB	2,104,443
Retail	4,910,368

Shareholding Pattern (%)

Particulars	Pre-issue	Post-issue
Promoters & promoters group	81.22%	62.58%
QIB	18.78%	26.51%
NIB	0.00%	3.27%
Retail	0.00%	7.64%
Total	**100.00%**	**100.00%**

*Calculated on the upper price band

Objects of the Issue

- Augmenting the capital base and
- General corporate purposes

Book Running Lead Manager

- Axis Capital Limited
- ICICI Securities Limited
- IIFL Securities Limited
- JM Financial Limited
- IndusInd Bank Limited
- YES Securities (India) Limited

Name Of The Registrar Karvy Fintech Private Limited

About the Company

Spandana Sphoorty Financial Limited is 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. The company offers products such as Abhilasha (JLG Loans), Shree Loans. Loans Against Property (LAP), Gold Loans (Keertana), Phinix Loans and Interim Loans. The company provides income generation loans, business loans and loans against gold jewellery. As of March 31, 2019, it was the fourth largest NBFC-MFI and the sixth largest amongst NBFC-MFIs and SFBs in India, in terms of AUM. As of June 30, 2019, it had 7,062 employees (including 5,051 credit assistants) operating out of 929 branches in 269 districts across 16 states and 1 union territory in India.

Strength

Seasoned business model with resilient performance through business cycles: The company believes that its track record of dealing with the aftermath of the 2010 AP Crisis, CDR and demonetization demonstrates the strength of the company business model, policies and client relationships as well as the company ability to manage the expectations of varying stakeholders in the company business, including staff, lenders, shareholders and clients.

High degree of client engagement and robust risk management, leading to superior asset quality and collections: The Company focuses on a high degree of client engagement through the company large employee base and operating procedures. The company risk management norms are designed keeping in mind the various kinds of risks to the company business. It also has well-established internal controls, a well-designed system for operations, strong policies and procedures to maintain financial discipline. The company high degree of client engagement and effective risk management policies have resulted in healthy asset quality.

Streamlined systems and processes and high employee productivity leading to low operating expense ratio: The company business processes are designed for scale and efficiency and it constantly reviews and endeavours to strengthen them as the scale of the company operations increase. The company operational efficiency is also driven by streamlined systems and procedures and scalable workforce deployment.

Focus on the high potential and under-served rural segment: Rural Areas in India are a highly under-served market for formal banking services in terms of access, availability and suitability of products and services. Therefore, the company strategically focuses on clients in the rural sector. Accordingly, with the company focuses on the rural segment as of December 31, 2018, 88% of the company portfolio was located in Rural Areas, as compared with 61% for 33 NBFC-MFIs as a whole. As of March 31, 2019, 94.6% of the company portfolio was located in Rural Areas.

Geographically diversified operations leading to risk containment and business resilience: As of June 30, 2019, the company covers 74,749 villages in 269 districts in 16 states and 1 union territory across India through 929 branches. The company operations are well-diversified at the branch, district and state levels. Presence in widespread geographies in India offers it a potential growth opportunity to further grow the business penetration in same areas and also reach out to more congruent geographies. With this adopted norm, the company operations are geographically well-diversified with no single state contributing more than 20.01% to the company AUM, no district contributing more than 1.82% to the company AUM and no branch more than 0.3% to the company AUM as of March 31, 2019.

Strategy

Leverage the company popular income generation loan products to derive organic business growth: Through the client-centric business model, it focuses on providing financing to clients on a speedy and continual basis. The company also focuses on providing income generation loans and the company popular 'Abhilasha' loans (which are income generation loans) amounted to 84.62% of the company Gross AUM, as of March 31, 2019. It expects to derive organic growth through the company popular income generation loan products that are offered through the JLG model. To this end, it intends to utilize the company existing branch infrastructure and employee base to increase the company volume of income generation loans.

Leverage the company existing branch network by increasing loan portfolio and enhancing employee productivity: The Company has a large branch network which can be further leveraged since it has maintained low exposure levels per branch thus far. The company believes that it has the existing physical infrastructure and workforce in place to increase the company loan portfolio, without a proportionate increase in operating expenses. Further, it believes that it has latent growth potential (i) by way of opening new branches in adjacent areas to the company existing branch network; (ii) splitting large branches according to demand (allowing them to grow by acquiring more clients in the same geographies); and (iii) leverage on those states where it has less penetration though the states have large unmet potential.

Increase the company presence in under-penetrated states and districts. The company's contiguous growth strategy is also relevant for expanding into newer districts within the states where it has already operations. It intends to continue to expand the company geographical coverage into newer states and union territories as well where it sees business potential (for instance, Assam, Punjab and Haryana).

Further diversify the company borrowing profile and reduce the company cost of borrowings: The company funding sources are varied, as it believes that a diversified debt profile ensures that it is not overly dependent on any one type or source for funding. Post the company exit from CDR, it has diversified the company lender base and accessed diverse sources of liquidity, such as term loans, cash credit and subordinated debt from banks, financial institutions and non-banking financial companies, proceeds from loan assets securitized, and proceeds from the issuance of NCDs to meet the company funding requirements. It intends to further diversify the company lender base by raising financing through lower cost avenues such as capital markets instruments such as NCDs, commercial paper and securitizations and through term loans from banks under priority sector lending. It believes that this diversification will enable the company to meet funding requirements and further optimize Average Cost of Borrowings.

Risk Factor

Business concentration is on a few states: The Company's operations are concentrated in the states of Karnataka, Madhya Pradesh, Orissa, Maharashtra and Chhattisgarh and any adverse developments in these states could have an adverse effect on the company's business, financial condition, results of operations and cash flows.

Loans are unsecured: Microfinance loans are unsecured and are susceptible to various operational, credit and political risks which may result in increased levels of non-performing assets ("NPAs"), thereby adversely affecting the company business, results of operation and financial condition.

Business is vulnerable to interest rate risk: The company business is vulnerable to interest rate risk, and volatility in interest rates could have a material adverse effect on the company net interest income, net interest margin and the company financial performance.

Dependent on credit bureaus for information: The Company depends on the accuracy and completeness of information provided by credit bureaus about clients and counterparties for the company credit assessment and risk management. Any misrepresentation, errors in or incompleteness of such information could adversely affect the company business and financial performance.

Peer Comparison

Co_Name	Total Income	PAT	EPS	P/E	P/BV	BV	FV	Price	Mcap
Shri.City Union.**	6036.44	1024.9	151.86	9.24	1.41	997.7	10	1402.7	9257.14
Satin Creditcare	1448.04	201.19	38.66	6.89	1.22	218.68	10	266.4	1386.3
Ujjivan Fin.Ser.	2013.62	150.44	12.46	20.41	1.64	154.71	10	254.4	3087.96
Spandana Sphoorty Fin. Ltd.	1,043.10	311.90	48.50	17.65	2.40	356.16	10	856	5504.64

** TTM

Valuation

Considering the P/E valuation on the upper end of the price band of Rs. 856, the stock is priced at pre issue P/E of 16.37x on its FY19 EPS of Rs. 52.30. Post issue, the stock is priced at a P/E of 17.65x on its EPS of Rs. 48.50. Looking at the P/B ratio at Rs. 856 the stock is priced at P/B ratio of 2.70x on the pre issue book value of Rs.317 and on the post issue book value of Rs. 356.10 the P/B comes out to 2.40x.

On the lower end of the price band of Rs.853 the stock is priced at pre issue P/E of 16.31x on its FY19 EPS of Rs. 52.30. Post issue, the stock is priced at a P/E of 17.59x on its EPS of Rs. 19.15. Looking at the P/B ratio at Rs. 853, the stock is priced at P/B ratio of 2.69x on the pre issue book value of Rs. 317 and on the post issue book value of Rs. 356.16 , the P/B comes out to 2.39x.

Industry Overview

Between 2014 and 2017, approximately 515 million adults worldwide opened an account at a financial institution or through a mobile money provider, which led to an increase in account ownership among adults from 51% in 2011 to 62% in 2014, and further to 69% in 2017. As of March 2018, there were only about 642 million deposit accounts and 39 million credit accounts in rural India, which accounted for about 34% of the total deposit accounts and 23% of the loan accounts in scheduled commercial banks despite rural India making up about 68% of the total population. The significant under-penetration of credit in rural areas offers strong potential for improvement. Given that microfinance institutions ("MFIs") have relatively deeper reach, existing customer relationships and employee bases, they are well placed to address this demand which is currently being met by informal sources of funds such as local money lenders.

The RBI and the government of India have launched various schemes for improving the penetration of credit, banking services, insurance and other social security programmes over the past three to four years. The RBI permitted continuation of the priority sector status to MFIs vide its circular in May 2011. The continuation of PSL status for NBFC-MFIs and allowing NBFC-MFIs to act as business correspondents for banks augurs well for funding profile of NBFC MFIs. Further NBFC MFIs also have opportunities to raise off balance sheet funding through business correspondent model, securitization and assignments as a significant proportion of underlying portfolios which would quality under the key categories of PSL targets.

Outlook

The NBFC sector is facing a liquidity crisis and NBFC companies are finding hard to mobilize funds from the market in the current scenario. The weak economic environment will continue to put stress in the NBFC sector as adverse economic scenario may lead to higher delinquencies. Following the implementation of AP Microfinance Ordinance 2010 which crippled the company's collections and cash-flows, Spandana Sphoorty underwent the corporate debt restructuring (CDR) mechanism and restructured its borrowings. In March 31, 2017 and March 8, 2018, it has raised money at a price of Rs.235.48 through private placement as well as preferential allotment. Moreover, thorough this public issue, only 400 cr will come to the company, and rest i.e. Rs 800 Cr is going to the promoter itself. A long term investor with high risk appetite may opt the issue.

EVENT	INDICATIVE DATE (On or about)
FOR ALL BIDDERS	Mon, Aug 5, 19
Bid/ Offer Closing Date	Wed, Aug 7, 2019
Finalisation of Basis of Allotment with the Designated Stock Exchange	On or about Wed, Aug 14, 19
Initiation of refunds for anchor investors/unblocking of funds	On or about Wed, Aug 14, 2019
Credit of Equity Shares to demat accounts of Allottees	On or about Friday, Aug 16, 2019
Commencement of trading of the Equity Shares on the Stock Exchanges	On or about Friday, August 19, 2019

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Annexure

Consolidated Financials

Profit & Loss

Rs. in Cr.

Particulars	31-Mar-19	31-Mar-18	31-Mar-17
Revenue from operations	1,043.10	587.31	377.06
Total expenditure	210.23	67.32	305.83
Operating Profit	**832.87**	**519.99**	**71.23**
OPM%	79.85	88.54	18.89
Other Income	5.43	0.23	1.60
PBDIT	**838.30**	**520.22**	**72.83**
Depreciation	6.97	5.72	8.33
PBIT	**831.34**	**514.49**	**64.50**
Interest	357.87	231.79	29.40
PBT	**473.47**	**282.70**	**35.10**
Tax	161.57	94.76	-408.31
Profit After Tax	**311.90**	**187.95**	**443.41**

Balance sheet is on next page

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Balance Sheet

Rs. in Cr.

Particulars	31-Mar-19	31-Mar-18	31-Mar-17
Financial assets			
Cash and cash equivalents	148.61	104.54	290.12
Bank Balances other than cash and cash equivalents	203.19	103.25	2.31
Trade Receivables	3.55	2.50	1.46
Loan Portfolio	4267.76	3089.63	1194.55
Investments	0.10	0.10	0.10
Other financial assets	60.447	65.96	1.74
Total financial assets	**4683.65**	**3365.97**	**1490.28**
Non-financial assets			
Current tax assets (net)	8.337	4.186	4.66
Deferred tax assets (net)	199.98	384.08	421.50
Property, Plant and Equipment	7.17	5.85	6.62
Intangible assets	2.22	2.60	2.39
Goodwill	17.37	0.00	0.00
Other non-financial assets	12.97	1.55	3.17
Total current assets	**248.05**	**398.28**	**438.34**
Total Assets	**4931.71**	**3764.25**	**1928.62**
Financial Liabilities			
Debt Securities	1371.96	1014.71	0.00
Borrowings (Other than Debt Securities)	1575.48	1296.51	932.46
Subordinated Liabilities	20.29	20.16	1.01
Other Financial liabilities	44.49	14.51	25.95
Total non-current liabilities	**3012.22**	**2345.89**	**959.42**
Non-Financial Liabilities			
Current Tax Liabilities (net)	6.28	9.30	23.58
Provisions	0.36	0.39	0.60
Other Non-Financial liabilities	22.49	18.03	17.45
Total current liabilities	**29.13**	**27.72**	**41.64**
Total	**3041.35**	**2373.61**	**1001.05**
NET Worth	**1890.36**	**1390.64**	**927.57**
Net worth represented by:			
Equity Share Capital	59.63	29.76	28.449
Other Equity	1829.80	1360.88	899.12
Equity attributable to shareholders of the company	1889.44	1390.64	927.57
Non Controlling Interest	0.922	0	
Total Equity	**1890.36**	**1390.64**	**927.57**
Total Net Worth	**1890.36**	**1390.64**	**927.57**

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RANKING METHODOLOGY

WEAK	★
NEUTRAL	★★
FAIR	★★★
GOOD	★★★★
EXCELLENT	★★★★★

E-mail: smc.care@smcindiaonline.com

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Corporate Office:
11/6B, Shanti Chamber,
Pusa Road, New Delhi - 110005
Tel: +91-11-30111000
www.smcindiaonline.com

Mumbai Office:
Lotus Corporate Park, A Wing 401 / 402 , 4th Floor , Graham Firth Steel Compound, Off Western Express Highway, Jay Coach Signal, Goreagon (East) Mumbai - 400063
Tel: 91-22-67341600, Fax: 91-22-67341697

Kolkata Office:
18, Rabindra Sarani, Poddar Court, Gate No-4,
5th Floor, Kolkata - 700001
Tel.: 033 6612 7000/033 4058 7000
Fax: 033 6612 7004/033 4058 7004

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