

Recommendation	Subscribe
Price Band	Rs 350 – 368
Bidding Date	2 – 4 Nov
Book Running Lead Manager	ICICI Securities, CLSA India, IIFL Securities, JM Financial
Registrar	LinkIn time
Sector	NBFC

#### Minimum Retail Application- Detail At Cut off Price

Number of Shares	40
Minimum Application Money	Rs. 14720
Discount to retail	0
Payment Mode	ASBA

Consolidated Financials (Rs Cr)	FY21	FY22
Total Income	498	705
Pre Prov. Profit	278	393
Adj PAT	44	22

Valuations (Q1FY23)	Upper Band
Market Cap post issue (Rs Cr)	3703
BVPS post issue	201
Dil. EPS Q1FY23 Annualised	29.9
P/B	1.8
P/E	12.3

#### Post Issue Shareholding Pattern

Promoters	68.2%
Institutions	31.8%

#### Offer structure for different categories

QIB (Including Mutual Fund)	50%
Non-Institutional	15%
Retail	35%
Post Issue Equity (Rs. in cr)	100.63
Issue Size (Rs in cr)	1104
Face Value (Rs)	10

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#### BACKGROUND

Incorporated in 2010, Fusion Micro Finance has the fastest gross loan portfolio CAGR of 37% between FY20-22 among listed NBFC-MFIs in India. As of June 30, 2022 its total AUM was Rs. 7,389 Cr of which 91% is represented by rural areas. Its robust underwriting processes have resulted in healthy portfolio quality indicators with GNPA/NNPA at 3.7%/1.4% resulting in healthy ROA/ROE of 4.2%/21.8% for Q1FY23.

#### Objects and Details of the Issue:

The public issue consists of Offer For Sale of ~Rs. 504 Cr by Promoters and investors as well as Fresh Issue of Rs. 600 Cr to be utilized towards augmenting the capital base.

#### Investment Rationale:

- Well Diversified and Extensive Pan-India Presence
- Access to Diversified Sources of Capital
- Robust Underwriting Process and Risk Management Policies
- Stable and Experienced Management Team Supported by Marquee Investors
- Proven Execution Capabilities with Strong Rural Focus

#### Valuation and Recommendation:-

Fusion has grown its AUM at a CAGR of 37% over FY20-22, one of the fastest amongst listed financials. With a low base of Rs. 7,389 Cr in AUM, the runway for accelerated growth has decent scope over the next 3-5 years. Despite covid, Fusion has managed its asset quality well by restricting GNPA/NNPA below the 6%/3% mark over FY21 & 22. Fusion is well placed to deliver ROA/ROE in excess of 4%/20% on a sustained basis barring any unforeseen event which hampers the micro finance industry every few years. Fusion's metrics are similar to those of the largest listed MFI player viz CreditAccess, while Fusion's valuations are at a steep discount of 45% in comparison. **We recommend to 'Subscribe' to the issue.**

Financials (Rs Cr)	FY20	FY21	FY22	Q1FY23 Annualised
Total Income	393	498	705	869
<i>Growth</i>	-	<b>27%</b>	<b>42%</b>	<b>23%</b>
Pre Prov. Profit	193	278	393	481
<i>Growth</i>	-	<b>44%</b>	<b>42%</b>	<b>78%</b>
PAT	70	44	22	300
<i>Growth</i>	-	<b>-37%</b>	<b>-50%</b>	<b>1281%</b>
Diluted BVPS	119	124	133	201 #
EPS	6.9	4.4	2.2	29.9
ROA	1.4%	2.4%	2.7%	4.2%
ROE	5.1%	10.7%	10.9%	21.8%
P/E *	53.2	84.3	170.2	12.3
P/B #	3.1	3.0	2.8	1.8

Source: Company data, NBRR

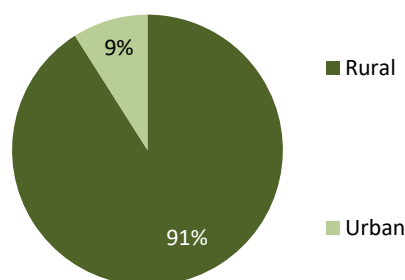
\* Q1FY23 P/E is annualized and post IPO

# Q1FY23 BVPS (not annualized) & P/BV is adjusted for fresh IPO infusion

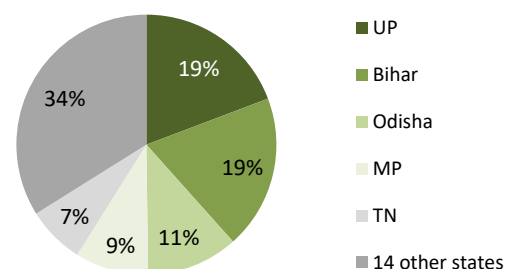
**Company Background**

Fusion (Fusion Micro Finance) obtained its license to operate as a Micro Finance Institution in the year 2010. Fusion has the fastest gross loan portfolio CAGR of 37% between FY20-22 among listed NBFC-MFIs in India.. As of June 30, 2022 its total AUM was Rs. 7,389 Cr. The share of AUM from customers in rural areas represented 91% of total AUM.

**Rural / Urban AUM Mix**



**State-wise AUM Mix**



Source: Company, NBRR

Fusion has achieved a significant footprint across India, where it has extended its reach to 29 Lac active borrowers which were served through a network of 966 branches and 9,262 permanent employees spread across 377 districts in 19 states and union territories in India. Fusion’s significant footprint of active borrowers and branch network puts it in a vantage position to further penetrate and deepen its presence in areas in which it has established branch infrastructure but remain relatively untapped and also to expand into new regions that have significant growth potential. Fusion has the fourth lowest gross loan portfolio per district and second lowest gross loan portfolio per customer among the top ten NBFC-MFIs in India, for FY22, demonstrating better diversification and lower risk per customer. As a result of its active management of state concentration, it has been able to maintain low levels of AUM concentration per state despite its growth over the years. As of June 30, 2022, no single state contributed to more than 20% of its total AUM, and the proportion of AUM in five largest states in terms of AUM concentration has further decreased from 95% as on FY16 to 66% as on June 30, 2022.

Fusion’s long-term credit ratings have improved from a rating of “BBB” by CARE as of FY17 to a rating of “A-” by CRISIL, CARE and ICRA as of June 30, 2022, making it one of the youngest NBFC-MFIs with such a strong credit rating.

Its robust underwriting processes and risk management policies, such as its extensive customer assessment methodologies and monitoring systems, have resulted in healthy portfolio quality indicators such as low rates of gross NPAs and net NPAs. As of June 30, 2022 its gross NPA ratio was 3.67% and net NPA ratio was 1.35%.

**Investment Rationale**

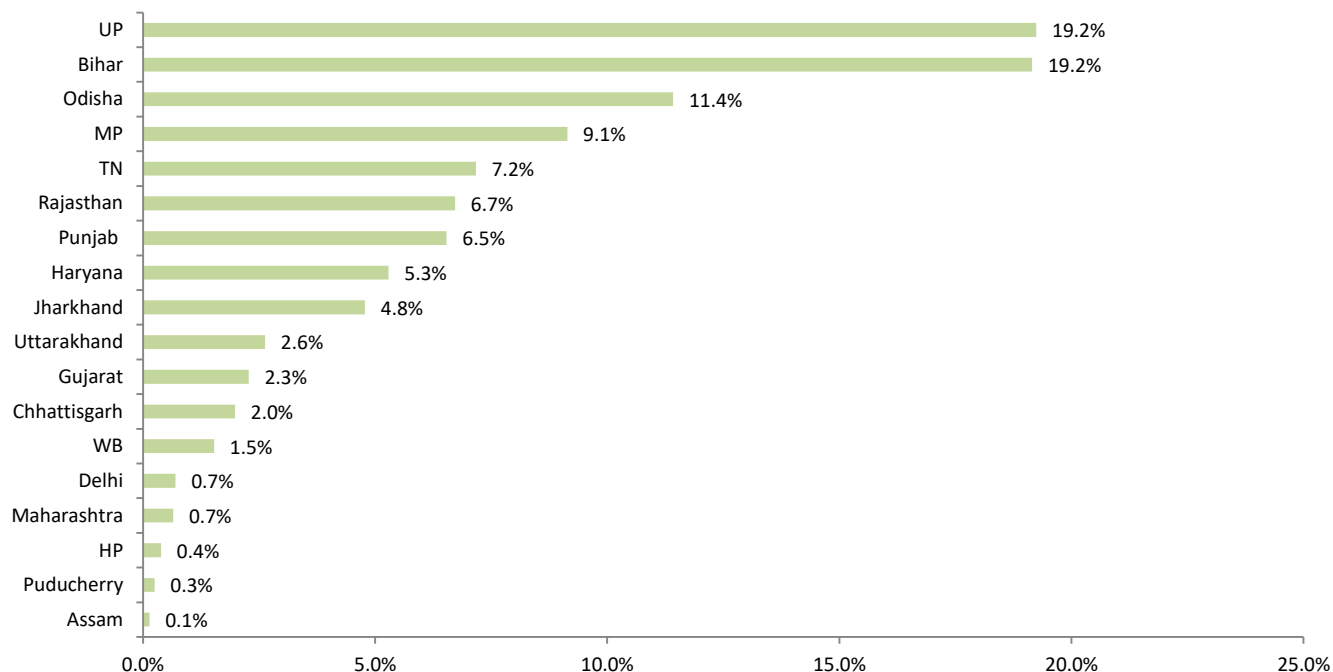
**Well Diversified and Extensive Pan-India Presence**

As of June 30, 2022, Fusion had 29 lac active borrowers which were served by 966 branches and 9,262 employees spread across 377 districts in 19 states and union territories in India. Fusion’s extensive geographic presence puts it in a vantage position to lend across the country in a scalable manner while maintaining low operating costs, helps it mitigate any risks arising from economic, political, cultural or environmental factors particular to a specific region, and allows it to offer “last-mile” connectivity to its customers in even the most remote areas.

Between March 31, 2016 and June 30, 2022, Fusion’s number of active borrowers grew at a CAGR of 34% and its number of branches grew at a CAGR of 32%. As a result of the expansion efforts, as of June 30, 2022, no single state contributed to more than 20% of its total AUM, and its proportion of AUM in five largest states in terms of AUM concentration has further decreased from 95% in FY16 to 66% as of June 30, 2022.

Similarly, the proportion of AUM in 50 largest districts in terms of AUM has also decreased over the years from 88% of total AUM as of FY16 to 38% as of June 30, 2022. Fusion has the fourth lowest gross loan portfolio per district and second lowest gross loan portfolio per customer among the top ten NBFC-MFIs in India, for FY22.

**State wise portfolio mix (as on June 2022)**

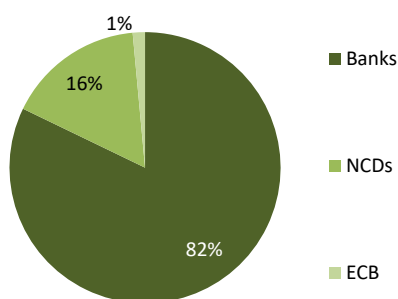


Source: Compamy, NBRR

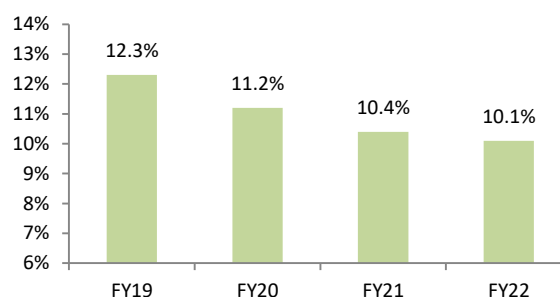
### Access to Diversified Sources of Capital

Over the years, Fusion has adopted a calibrated approach towards diversifying its fund-raising sources and minimizing the cost of borrowings with prudent asset liability management and effective liquidity management. The average effective cost of borrowings have declined at a steady rate over the years. Fusion benefits from a large and diversified mix of lenders which has increased over the years and included 56 lenders as of June 30, 2022, comprising a range of public banks, private banks, foreign banks and financial institutions to meet its capital requirements.

#### Sources of borrowings (FY22)



#### Cost of borrowing

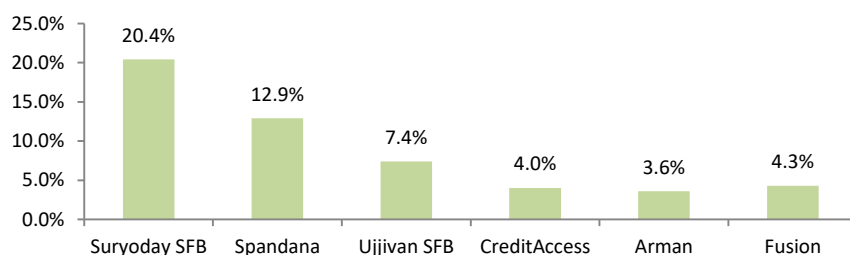


Source: Companies, NBRR

### Robust Underwriting Process and Risk Management Policies

Fusion's robust risk management policies and underwriting processes, such as extensive customer assessment methodologies and monitoring systems, have resulted in healthy portfolio quality indicators. Fusion's average GNPA of 2.4% between FY15-22 was the lowest among all NBFC-MFIs operating in North India. Fusion's customer due diligence procedures encompass multiple levels of checks and controls designed to assess the quality of customers and to confirm that they meet its stringent selection criteria, and include comprehensive evaluation of repayment capacity and detailed cash flows analysis of the customer as well as thorough group training sessions and knowledge testing. Fusion utilizes credit bureau data to verify customer details and obtain information on past credit behaviour. Further, it employs proactive practices that involve frequent evaluations of portfolio risk levels on a periodic basis and rigorous monitoring and analysis of cash disbursements and collection, roll rates and customer retention at both branch and head office levels, which minimize the incidence of bad debts.

#### Superior asset quality metrics: GNPA + Standard Restructured as % of AUM (Q1FY23)



Source: Company, NBRR

**Stable and Experienced Management Team Supported by Marquee Investors**

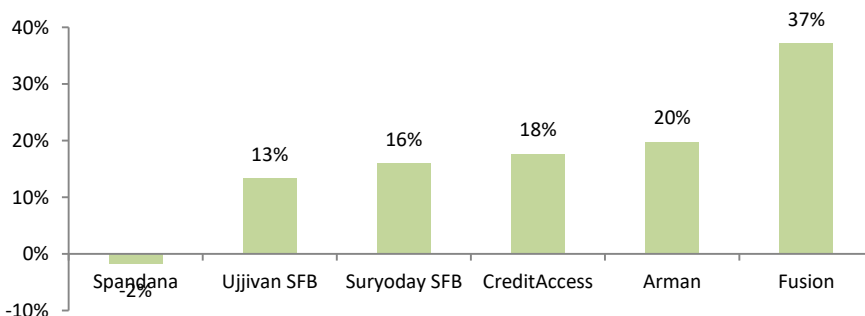
Fusion was founded by Mr. Devesh Sachdev (will hold 4.9% stake post IPO vs 6.6% pre IPO), a first-generation entrepreneur who has 26 years of experience in the banking and financial services and logistics industry. Fusion’s senior management team comprises experts and professionals heading various functions with an average of 17 years of leadership experience in their respective fields. Fusion also benefits from support of marquee investors, including Warburg Pincus LLC (will hold 39.4% stake post IPO vs 48.6% pre IPO), a leading private equity firm focused on growth investing across several sectors, and Creation Investments Fusion, LLC (will hold 23.7% stake post IPO vs 30.0% pre IPO), a leading alternative investment management company with a focus on private equity and private credit investments in emerging market financial services companies serving underserved and underbanked clients, both of whom are now Fusion’s promoters.

**Proven Execution Capabilities with Strong Rural Focus**

Fusion has a long history of serving rural markets with high growth potential in the microfinance segment, and has maintained a track record of financial performance and operational efficiency through consistently high rates of customer acquisition and retention and low-cost expansion into underpenetrated areas. The total AUM grew at a CAGR of 37% from Rs. 3,607 Cr as of FY20 to Rs. 6,786 Cr as of FY22. Through such growth, Fusion has achieved a consistent reduction in cost to income ratio from 63% for FY19 to 44% for FY22 in the back of operating leverage. Fusion also achieved improving customer retention rates of 72%, 70%, 69% and 47% for Q1FY23, FY22, FY21 and FY20, respectively, which it attributes to its superior customer services and commitment to proactively address the specific needs of each individual across its large customer base. Fusion had the third highest growth in number of customers among the top ten NBFC-MFIs in India in FY22. As of June 30, 2022, 20.5 lac or 71% of its total customers, and 91% of its total AUM, were from rural areas. Connection with rural customers, in particular, has been largely driven by Fusion’s focus on continuously deepening its understanding of the financial needs of the rural customer segment.

Fusion’s customer-centric model and ability to leverage its extensive distribution network and deep-rooted presence in rural markets across India, makes it well placed to offer an increasing variety of financial products in areas where financial services penetration remains limited. According to CRISIL, in addition to having less competition, lower credit penetration and less migration, rural areas also benefit from overall better credit behaviours and, in turn, lower delinquency rates. As Fusion’s operations are focused on rural and peri-rural areas, it has not been as adversely affected by the current COVID-19 pandemic as compared to other lenders with relatively larger urban or semi-urban operations.

**Highest AUM CAGR among listed micro finance lenders (FY20-22)**



Source: Company, NBRR



## Key Risks

**Exposure to unsecured nature of loans poses a risk:** Micro finance loans being unsecured are inherently riskier than other forms of loans. Further micro loans are mainly focused towards the bottom of the pyramid borrowers and thus pose a high risk in the eventuality of a severe economic slowdown.

**Highly concentrated in the states of U.P & Bihar:** Any adverse changes in regulation, social unrest, economic disruption, a natural calamity including floods/drought or any district specific political interference in the states of UP (19% of AUM) and Bihar (19% of AUM) would have an adverse impact on Fusion.

**Resurgence of Covid:** A resurgence of covid could result in renewed lockdowns thus impacting the economic situation of the bottom of the pyramid population. This could result in an increase in defaults and thereby require higher provisions to be made by Fusion thus impacting profitability.

## Valuation and Recommendation

Fusion has grown its AUM at a CAGR of 37% over FY20-22, one of the fastest amongst listed financials. With a low base of Rs. 7,389 Cr in AUM, the runway for accelerated growth has decent scope over the next 3-5 years. Despite covid, Fusion has managed its asset quality well by restricting GNPA/NNPA below the 6%/3% mark over FY21 & 22. With covid becoming history, asset quality concerns have abated and demand for micro loans is on an upswing. Fusion is well placed to deliver ROA/ROE in excess of 4%/20% on a sustained basis barring any unforeseen event which hampers the micro finance industry every few years. Fusion's metrics are similar to those of the largest listed MFI player viz CreditAccess, while Fusion's valuations are at a steep discount of 45% in comparison. **We recommend to 'Subscribe' to the issue.**

### Peer Comparison: Metrics for latest available quarter

As on Q1/Q2FY23 as available	CreditAccess (Q2)	Spandana (Q2)	Arman (Q1)	Fusion (Q1)
AUM (Rs cr)	16,539	5,782	1,388	7,389
NIM	12.0%	13.0%	15.6%	10.3%
Cost/Income	38%	51%	37%	45%
Credit Cost	2.5%	1.6%	3.4%	1.1%
Standard Restructured	0.5%	3.5%	NA	0.6%
GNPA	2.2%	7.3%	3.6%	3.7%
NNPA	0.8%	4.0%	0.3%	1.4%
Loan CAGR FY20-22	18%	-2%	20%	37%
ROA annualised	4.0%	3.8%	5.0%	4.2%
ROE annualised	16.1%	7.1%	27.5%	21.8%
P/E (x) Q1 annualised	21.7	21.2	23.0	12.3
P/Adj. BV (x) trailing	3.5	1.5	5.4	1.9
P/BV (x) trailing	3.4	1.6	5.5	1.8

Source: NBRR

## Financials

P&L (Rs. Crs)	FY20	FY21	FY22	Q1FY23	FY23 Ann.	Bal. Sheet (Rs. Crs)	FY20	FY21	FY22	Q1FY23
Interest earned	666	828	1,064	329	1,317	Equity capital	79	79	83	83
Interest expende	338	375	496	143	573	Reserves & surplus	1,120	1,167	1,255	1,334
<b>NII</b>	<b>329</b>	<b>452</b>	<b>568</b>	<b>186</b>	<b>745</b>	Net worth	1,199	1,246	1,338	1,416
Non interest incc	64	46	137	31	124	Borrowings	2,974	4,432	5,776	6,010
<b>Total income</b>	<b>393</b>	<b>498</b>	<b>705</b>	<b>217</b>	<b>869</b>	Other liab and prov	67	159	169	127
<i>Growth</i>	-	27%	42%		23%	<b>Total liab and equity</b>	<b>4,240</b>	<b>5,838</b>	<b>7,283</b>	<b>7,554</b>
Total Op. expens	200	220	312	97	388	Cash & Bank Balance	818	1,335	1,154	770
<i>Growth</i>	-	10%	42%		24%	Investments	1	0	0	0
Staff costs	148	169	233	72	289	<b>Net Advances</b>	<b>3,343</b>	<b>4,361</b>	<b>5,918</b>	<b>6,651</b>
Other Op Exp	52	52	79	25	99	<i>Growth</i>	-	30%	36%	54%
<b>Profit before pro</b>	<b>193</b>	<b>278</b>	<b>393</b>	<b>120</b>	<b>481</b>	Other assets	79	142	211	133
<i>Growth</i>	-	44%	42%		22%	<b>Total assets</b>	<b>4,240</b>	<b>5,838</b>	<b>7,283</b>	<b>7,554</b>
Provisions	93	221	369	20	80	<b>Asset Quality</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22</b>	<b>Q1FY23</b>
Profit before tax	100	57	24	100	401	GNPA ratio	1.1%	5.5%	5.7%	3.7%
Taxes	30	13	3	25	100	NNPA ratio	0.4%	2.2%	1.6%	1.4%
<b>Net profit</b>	<b>70</b>	<b>44</b>	<b>22</b>	<b>75</b>	<b>300</b>	Credit Cost	2.6%	5.4%	6.5%	1.1%
<i>Growth</i>	-	-37%	-50%		1281%	<b>Other Parameters</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22</b>	<b>Q1FY23</b>
						AUM	3,607	4,638	6,786	7,389
						<i>Growth</i>	-	29%	46%	60%
						Yield on Advances	21.2%	20.5%	18.8%	19.5%
						Cost of Borrowings	12.3%	11.2%	10.4%	10.1%
						Spread	8.9%	9.2%	8.4%	9.4%
						NIM	8.9%	9.2%	8.4%	NA
						CRAR Tier 1	33.1%	25.5%	19.9%	19.5%
						Cost / Income Ratio	50.9%	44.3%	44.3%	44.7%
						ROA	2.2%	1.1%	0.4%	4.2%
						ROE	7.6%	3.6%	1.7%	21.8%

Source: Company data, NBRR

\* All valuations are on post IPO basis

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