

## IPO Note- Ujjivan Small Finance Bank

02 December 2019

Ujjivan Small Finance Bank Ltd (USFB), promoted by Ujjivan Financial Services Ltd (UFSL), is a mass market focused small finance bank (SFB), catering to the unserved & underserved segment. USFB is doing an IPO to meet the RBI regulation which requires the SFB to list within a period of 3 years. Currently, the holding promoter company UFSL is listed which will have 83.3% stake in USFB post IPO. As per RBI guidelines, the promoter is required to reduce its shareholding in SFB to 40% within a period of 5 years from the date of commencement (1st Feb, 2017 for USFB) of business operations. This could act as an overhang on the stock. However, once the IPO process is completed, USFB will consult the RBI on the reverse merger process which if approved, will act as a positive trigger. These events outcome are likely to have significant bearing on stock price in medium term. The IPO consists of fresh issue of ₹ 7.5 bn.

### Key Investment Rationale

- Business growing at a brisk pace with shift towards non-MFI segment:-** In the latest quarter, credit book has grown by strong 55% YoY to ₹ 128.64 cr, led by non-MFI book which grew nearly 3x on YoY basis. MFI business growth was also healthy at 38% YoY. The company continues its transition from MFI to being a diversified player. As on Q2FY20, micro-banking constitutes 79.2% of credit which the bank consciously plans to grow at moderate pace of 20-25% from ~35% earlier. The bank has built a decent Affordable Housing and MSE loans portfolio, constituting 9.4% and 6.5% of advances respectively. Besides, the other sectors of focus will be financial institution, personal loans, 2-wheeler, electric 3-wheeler financing, etc. Share of secured loan has risen to 19.4% vs 9% in Sept 18. Currently, USFB earns superlative NIM of 10.8% owing to high yield of ~20% on its credit book. It earns 21% yield on its micro-banking book, 17% on its MSE book and 14% on affordable housing book. With secured loan book share expected to further increase, NIM is likely to decline going ahead despite expected increase in CASA ratio and retail term deposits. Deposit mobilisation has been strong which grew 142% YoY to ₹ 101.3 bn in Q2FY20, covering 78.7% of total advances against 50.4% in Sep'18. Retail deposits comprise 41.9% vs 30% a year ago. Similarly, CASA ratio stood at 11.9% vs 9.0%.
- Stable asset quality:-** Despite lending to lower strata of the society, the asset quality of USFB has been stable which is noteworthy. As on Q2FY20, it has GNPA ratio of 0.9% and NNPA ratio of 0.3%. Geographic diversification, stringent credit monitoring mechanism and group lending model in micro-banking has enabled the company to maintain stable asset quality. Geographically, USFB is amongst the most diversified player w.r.t. its micro-banking business. It exists in 24 states and UTs covering 232 districts in India as of Sept'19. The bank is operating from 552 banking outlets which include 141 outlets in URCs, 4 Asset Centres and 442 ATMs.

**Rating** **SUBSCRIBE**

### Issue Details

Issue Opens	2-Dec-19
Issue Closes	4-Dec-19
Equity Offerings (In MN shares)	202.7
Face Value	10
Price Band (₹)	36-37
Bid Lot	400
Issue Size (₹bn)	7.5
Maximum Application for Retail Investor (₹)	2,00,000.0
Issue Type	100% Book Building
Listing	NSE/BSE
BRLMs	Kotak, IIFL Securities, JM Financial
Registrar	Karvy

### Shareholding Pattern (%)

	Pre Issue	Post Issue
Promoter	94.4%	83.3%
Non Promoter	5.6%	16.7%

### Issue Structure (In mn no. of shares)

<b>Issue size</b>	<b>202.7</b>
Fresh Issue	202.7
<b>Break-up of net issue to public:</b>	
QIB's portion	75.0
Non-institutional portion	15.0
Retail Portion	10.0

Source: ABML Research, RHP

### Analyst Details

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As far as new lending segments are concerned, the company runs pilots for 3-5 years and then makes necessary changes before rampantly growing it up. This will enable the company to manage risk which is of utmost importance in lending business. However, it yet remains to be seen how asset quality pans out in new segments including affordable housing, MSE, etc. in medium to long term.

- **Professional & experienced management:-** USFB is a professionally managed institution with a senior management team having a diversified track record in the financial services industry. The board consists of directors with a diverse mix of experience in various sectors including the financial services industry and technology. Nitin Chugh, has taken over as MD & CEO with effect from December 1, 2019, following the retirement of Samit Kumar Ghosh. Nitin Chugh has experience of working with HDFC Bank, Standard Chartered Bank, HCL Hewlett Packard and Modi Xerox.

### Outlook & Valuation

The bank has been delivering strong growth in recent times with steady shift in business model from micro-banking to a diversified SFB. Deposits have been growing at strong pace, led by retail deposits and CASA. With this capital raise, the company will be more than adequately capitalised for growth. Besides, the company earns healthy return ratios with RoA of ~2.5% and RoE of ~19%. At higher price band of ₹ 37, the stock is attractively priced at 2.2x P/ABV post considering the fresh capital infusion. This leaves enough room for stock appreciation. Recommend investors to **SUBSCRIBE** the issue for listing gains.

### Risks & concerns

- **Success in New business segments yet to be proved:** USFB has diversified into several new business segments including MSE loans, affordable housing loans, personal loans, vehicle loans and agriculture loans. With limited experience in offering new products, growing the book while managing cost structure remains a key risk. In addition, asset quality experience in new product offering remains a risk. Inability to effectively manage any of these risks could materially and adversely affect business and impact the future financial performance.
- **Regulatory risk:** As per RBI guidelines, the promoter is required to reduce its shareholding in SFB to 40% within a period of 5 years from the date of commencement of business operations. This could act as an overhang on the stock unless some relief measure like reverse merger is allowed by RBI.
- **MFI business still poses concentration risk:** With ~79% of credit book still comprising of micro-banking, it poses a concentration risk. This business is highly exposed to political circumstances and natural calamities.

### Objects of the issue

- To utilize proceeds to augment capital base
- To receive benefits of listing of equity shares on stock exchanges
- General Corporate Purposes

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### Income Statement

In ₹ mn	FY18	FY19	H1FY20
Interest earned	14,679	18,316	12,597
Interest expense	6,069	7,252	5,192.80
<b>NII</b>	<b>8,610</b>	<b>11,064</b>	<b>7,404</b>
Growth (%)	-	28.5%	33.8%
Non-interest income	1,115	2,060	1,752
Net total income	9,725	13,124	9,156
Operating expenses	6,529	10,034	6,130
<b>PPP</b>	<b>3,196</b>	<b>3,090</b>	<b>3,026</b>
Growth (%)		-3.3%	95.9%
Provisions	3,108	406	436
PBT	88	2,684	2,590
Tax	20	692	719.3
<b>PAT</b>	<b>69</b>	<b>1,992</b>	<b>1,871</b>
Growth (%)		2802.8%	87.8%

Source: ABML Research, RHP

### Balance Sheet

In ₹ mn	FY18	FY19	H1FY20
<b>Sources of funds</b>			
Equity Capital	14400	14400	14400
Preference share	2000	2000	2000
Reserves	69	1796	4001
Networth	16469	18196	20401
Deposits	37725	73794	101298
Borrowing	38528	41661	34702
Other liabilities	2006	3771	4678
<b>Total liabilities</b>	<b>94729</b>	<b>137422</b>	<b>161079</b>
<b>Application of funds</b>			
Cash & Bank Balance	4948	10945	7093
Advances	73362	105525	127804
Investment	12325	15266	20184
Fixed assets	1983	2845	2962
Other assets	2110	2842	3036
<b>Total assets</b>	<b>94729</b>	<b>137422</b>	<b>161079</b>

Source: ABML Research, RHP

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### Key Ratios

Particulars	FY18	FY19	H1FY20
AUM (₹ mn)	73362	105525	127804
Growth (%)	25.2%	43.8%	-
NIM (%)	10.3%	10.9%	10.6%
GNPA ratio (%)	3.7%	0.9%	0.9%
NNPA ratio (%)	0.7%	0.3%	0.3%
RoA (%)	0.1%	1.7%	2.5%
RoE (%)	0.4%	11.5%	19.6%
Bv/share*	11.4	12.6	14.2
Adj Bv/share*	11.1	12.4	13.9

\*On Pre-diluted basis

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ABML research is also accessible in Bloomberg at ABMR

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