

Retail Research	IPO Note
Sector: BFSI	Price Band (Rs): 36 - 37
29th November, 2019	

Ujjivan Small Finance Bank Limited

Company Overview:

Ujjivan Small Finance Bank is a mass market focussed Small Finance Bank (SFB) in India, catering to unserved and underserved segments and committed to building financial inclusion in the country. Its portfolio of products and services includes various asset and liability products and services such as loans to micro banking customers, agriculture and allied loans, MSE loans, affordable housing loans, financial institutions group loans, personal loans and vehicle loans.

Bank's promoter, Ujjivan Financial Services Ltd. (UFSL) commenced operations as an NBFC in 2005 with the mission to provide a full range of financial services to the 'economically active poor' who were not adequately served by financial institutions. On October 7, 2015, UFSL received RBI In-Principle Approval to establish an SFB, following which it incorporated Ujjivan Small Finance Bank Limited as a wholly-owned subsidiary.

Key Highlights:

- Customer centric organization with multiple delivery channels
- Provides a variety of banking services in mass market customer segments with a focus on serving the financially unserved and underserved segments in India
- One among the leading SFBs in terms of branch count and geographical spread across India
- Strong growth credentials since inception through high rates of customer retention, geographical expansion, improved productivity, lower credit cost, etc.
- Technology driven operating model with advanced digital platform
- Robust risk management framework to identify, measure, monitor and manage credit, market, liquidity, IT and operational risks

Valuation:

At the price band of Rs. 36-37, the issue is priced at 29.8x and 30.5x respectively of its FY19 earnings whereas it is available at 2.5x of its book value at the lower and upper bands each.

While comparing with its closest peers, the stock is reasonably priced with robust NIMs, healthy return ratios and better asset quality than its peers.

We recommend investors to subscribe the issue at Cut-Off price.

Issue Details	
Date of Opening	02-Dec-19
Date of Closing	04-Dec-19
Price Band	Rs. 36 - Rs. 37
Issue Size	Rs. 750 cr.
No. of shares	20.8 cr. – 20.3 cr.
Face Value	Rs. 10
BRLM	Kotak Mahindra Capital Co. Limited IIFL Securities Limited JM Financial Limited
Registrar	Karvy Fintech Private Limited
Bid Lot	400 equity shares and in multiples of 400 equity shares thereafter

Objects of Issue	
Description	
Augment bank's Tier-1 capital base to meet its future capital requirements such as organic growth and expansion	
Meeting the expenses in relation to the issue	

Shareholding Pattern		
Pre Issue	No. of Shares	%
Promoter & Promoter Group	1,44,00,36,800	100.0
Public & Others	-	-
Total	1,44,00,36,800	100.0

Post Issue @ Rs.36 Per Sh.	No. of Shares	%
Promoter & Promoter Group	1,44,00,36,800	87.4
Public & Others	20,83,33,333	12.6
Total	1,64,83,70,133	100.0

Post Issue @ Rs.37 Per Sh.	No. of Shares	%
Promoter & Promoter Group	1,44,00,36,800	87.7
Public & Others	20,27,02,703	12.3
Total	1,64,27,39,503	100.0

Source: RHP, SSL Research

For complete information and a complete list of the risk factors, please refer the Red Herring Prospectus.

Investment Rationale

- **Deep understanding of mass market serving unserved and underserved segments:**

Bank's SFB operations are focused on serving the financially unserved and underserved segments in India. As of June 30, 2019, the bank operated 181 Banking Outlets located in 78 districts classified by the RBI as under-banked districts as per the Census 2011. The experience of its Promoter, UFSL, as an erstwhile microfinance institution, coupled with its ability to address mass market customer segments has allowed it to become among the leading small finance banks in India in terms of deposits, branch count and geographical spread, as of March 31, 2019.

- **Pan-India presence:**

As of March 31, 2019, the bank was among the leading SFBs in terms of branch count and geographical spread across India. As of June 30, 2019 the bank was present in 24 states and union territories encompassing 221 districts in India. The bank operated from 474 Banking Outlets that included 120 Banking Outlets in Unbanked-Rural Centres (of which seven were business correspondent centres) and additionally operated 50 Asset Centres. Its diversified operations also allow it to de-risk its business by mitigating political and state-specific risks. Its operations are well-diversified and in Fiscal 2019, no single state constituted more than 18% of the overall loan portfolio. As a result of the geographic spread, the bank has been able to reduce its concentration risk and diversify its loan portfolio.

- **Technology driven operating model with advanced digital platform:**

The bank leverages technology to serve its customers better, identify opportunities, deliver innovative products and services and advance on its goal of facilitating financial inclusion in India. It manages the entire life cycle of its customers' banking transactions, from on-boarding to customer management, through its various technology platforms. Over the years, the use of technology has improved the bank's work place engagement and governance, increased the accessibility of its products to 101 customers and enabled it to rapidly scale up operations in a secure and efficient manner. With digital platform, the bank has enabled paperless and handheld device based loan origination and cashless disbursements for customers with remittances directly to their accounts.

- **Robust risk management framework:**

The bank has an established risk management framework to identify, measure, monitor and manage credit, market, liquidity, IT and operational risks. It has implemented credit management models such as decentralized loan sanctioning and stringent credit history checks. It uses technology and data analytics to manage credit risks and its in-house analytics team has developed a credit application scorecard to make informed decisions on lending. The bank has implemented SaaS for measuring capital adequacy, asset liability management and preventing money laundering. The bank's effective credit risk management is also reflected in its portfolio quality indicators such as robust repayment rates, stable portfolio at risk and low gross and net NPAs. As of June 30, 2019, its gross NPAs accounted for 0.84% of gross advances, while net NPAs accounted for 0.26% of Net Advances. Bank's GNPA was the lowest among the small finance banks in India, as of March 31, 2019.

- **Strong track record of financial performance:**

The bank has maintained strong growth credentials since inception through high rates of customer retention, geographical expansion, operationalization of Banking Outlets, improved productivity, lower credit cost and growth in customer base. Operational efficiencies, low turn-around time and network of Banking Outlets have resulted in the rise in profitability. Gross Advances (including securitization/ IBPC) of the bank has grown from ~Rs6,384 crore as of March, 2017 to Rs11,048.59 crore as of March, 2019 and were Rs11,782.94 crore as of June, 2019. The Net Interest Income in FY 2018 and 2019 was Rs861 crore and Rs1,106.41 crore, respectively, and was Rs352.45 crore in the three months ended June, 2019. The Net Interest Margins in FY 2018 and 2019 were 10.31% and 10.93%, respectively, and was 10.51% in the three months ended June, 2019. Total deposits have increased from Rs206.45 crore as of March, 2017 to Rs7,379.44 crore as of March, 2019 and were Rs7,956.76 crore as of June, 2019. Moreover, bank's CASA to total deposits ratio has improved from 1.57% in March 2017 to 10.63% as of March 2019 and was 10.39% as of June, 2019.

- **Professional management, experienced leadership with focus on employee welfare:**

The bank is professionally managed and its senior management team has a diversified track record in the financial services industry. Bank's Board consists of Directors with a diverse mix of experience in various sectors, in particular, the financial services industry and technology. Bank's focus on ensuring strong corporate governance is evident from its leadership transition process that has been a Board managed process for over a period of one year. The experience of its independent directors, who constitute a majority of the Board, ensures transparency and accountability in operations while the heads of functional groups, such as finance, financial planning and analysis, risk and human resources enhance the quality of management with their specific and extensive industry experience.

Growth Strategies

- **Diversify revenue streams:**

An important strategic focus is to diversify fee and non-fund based revenues. The bank intends to leverage on Banking Outlet network, digital channels and increasingly diversified product and service portfolio to develop fee and commission-based business. For MSE customers, the bank aims to market fee and non-fund based products such as letters of credit, bank guarantees, foreign exchange remittance services and third-party insurance products. The bank also intends to offer POS terminals to MSE customers in partnership with third party providers.

- **Expand distribution network to increase customer penetration:**

The bank intends to expand its Banking Outlets and infrastructure by focusing on rural and semi-urban areas as these areas represent a significant opportunity for continued growth as it expand banking services to those areas which have traditionally been underserved. It also intends to deploy ACRs for the convenience of our customers.

- **Diversify product offerings to enable multiple customer relationships:**

Bank's endeavour is to be a one-stop-shop for financial services, delivering quality products and solutions, along with a personalized customer experience to a diversified customer base. It intends to develop and offer a comprehensive suite of 103 asset and liability products that will help attract new customers and deepen relationship with existing customer base. It also intends to expand its range of third party products and services in order to serve customers better.

- **Continue its focus on technology and data analytics to grow operations:**

The optimum use of advanced, cost-effective technology has significantly driven bank's operations, and going forward, it intends to strategically invest its resources for further integration of technology into its operations. By furthering its digital and technology platform, its endeavour is to empower the customers to access various products and services on their own, reduce bank's operating costs and increase efficiencies.

- **Strengthen liability franchise and focus on increasing our retail base:**

The bank intends to strengthen the liability franchise with a focus on growing retail deposit base to provide a stable, low-cost source of funding. Bank believes that with simple, flexible products, which are accessible through assisted and self-serviced channels, bank can position itself as a reliable alternative to informal players.

- **Focus on developing responsible banking behavior for unserved and underserved segments:**

Bank's focus will continue to remain on serving the unserved and underserved segments to build responsible banking behavior by educating potential customers and increasing financial literacy.

Risk factors

- Significant dependence on micro banking business, particularly group loans, and any adverse developments in this segment could adversely affect business, results of operations, financial condition and cash flows.
- Continuous requirement of funds and bank's inability to access sources of funds in an acceptable and timely manner or any disruption in the access to funds would adversely impact results of operations and financial condition.
- Growth strategy depends on bank's ability to compete effectively as The Indian banking industry is very competitive.
- Inability to control the level of non-performing assets in portfolio or any increase in RBI mandated provisioning requirements could adversely affect business, financial conditions and results of operations.
- Bank extensively relies on and continuously upgrades its information technology systems and any disruptions in such systems, or breach of data, could adversely affect operations and reputation. Further, bank's success depends on its ability to respond to new technological advances.
- Dependency on brand recognition and failure to maintain and enhance awareness of its brand would adversely affect its ability to retain and expand its base of customers.

Financial Snapshot / Relative Valuation

Ujjivan Small Finance Bank Ltd			
(Rs. Cr.)	Pre Issue	Post Issue	
	FY18	FY19	
Particulars		Price Band	
		36	37
Net Interest Income	861.0	1,106.4	1,106.4
Net Revenue	861.0	1,106.4	1,106.4
PAT	6.9	199.2	199.2
Equity Share Capital	1,440.0	1,648.4	1,642.7
No of Equity Shares	144.0	164.8	164.3
Face Value	10.0	10.0	10.0
EPS	0.0	1.2	1.2
CMP	37.0	36.0	37.0
Deposit and Borrowings	7,625.4	11,545.5	11,545.5
Net Worth	1,646.9	2,396.9	2,396.9
Advances	7,336.2	10,552.5	10,552.5
Cash and Investment	1,477.7	2,174.6	2,174.6
Interest Earning Assets	8,813.9	12,727.1	12,727.1
Total Asset	9,472.9	13,742.2	13,742.2
Market Cap	5,328.1	5,934.1	6,078.1
BV per share (Rs)	11.4	14.5	14.6
GNPA (Rs cr)	275.9	97.9	97.9
Adj. BV per share (Rs)	9.5	13.9	14.0
PE(x)	776.4	29.8	30.5
P/BV (x)	3.2	2.5	2.5
NIM (%)	9.8	10.3	10.3
ROA (%)	0.1	1.7	1.7
Cost of fund (%)	8.0	7.6	7.6
Yield on Advances (%)	17.9	19.3	19.3
Spread (%)	9.9	11.8	11.8
Yield on Assets (%)	16.7	17.0	17.0
Cost to Income Ratio (%)	67.1	76.5	76.5
RoE (%)	0.4	11.5	11.5
GNPA (%)	3.7	0.9	0.9
NNPA (%)	0.7	0.3	0.3

Relative Valuation

Particulars	Ujjivan Small Finance Bank		Equitas Holdings	Federal Bank	City Union Bank
	Lower	Upper			
CMP (Rs)	36.0	37.0	101.5	90.9	220.5
Market. Cap (Rs C)	5,934.1	6,078.1	3,464.1	18,098.2	16,209.7
P/BV (x)	2.5	2.5	1.4	1.3	3.3
P / E (x)	29.8	30.5	19.6	13.9	23.8
NIM (%)	10.3	10.3	8.8	3.1	4.1
ROA (%)	1.7	1.7	1.2	0.9	1.6
GNPA (%)	0.9	0.9	2.5	3.1	3.4
RoE (%)	11.5	11.5	7.5	10.1	15.1

Note: Valuation and return ratios are based on FY19 full year earnings while CMP is taken as on 28th November

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