

## Subscribe for Long Term

Issue Details	
Price Band (Rs)	853 - 856
Face Value(Rs)	10
Issue Size(Rs)	1200 Cr
Issue Type	Book Building
Minimum lot	17 Shares
Issue Opens	August 5, 2019
Issue Closes	August 7, 2019
Listing on	BSE, NSE

Indicative Timeline	On or before
Finalization of Basis of Allotment	August 14, 2019
Unblocking of Funds	August 14, 2019
Credit of shares to Demat Account	August 16, 2019
Listing on exchange	August 19, 2019

Other Detail	
Book Running Lead Managers	Axis Capital Limited, ICICI Securities Limited, IIFL Holdings Limited, Indusind Bank Limited, JM Financial Consultants Private Limited, Yes Securities (India) Limited
Registrar	Karvy Computershare Private Limited

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## Spandana Sphoorty Financial Limited

### Company Background

Incorporated as an NGO in 1998 at Hyderabad, Spandana Sphoorty Financial Limited (SSF) grew to become the fourth largest NBFC-MFI and the sixth largest amongst NBFC-MFIs and SFBs in India, in terms of AUM. In 2004, it was registered with the RBI as an NBFC and subsequently in 2015 got registered as NBFC-MFI. Founded by Ms.Padmaja Reddy, SSFL is a leading rural-focused NBFC-MFI with a geographically diversified presence in India. They offer income generation loans under the joint liability group model, predominantly to women from low-income households.

In 2010, due to implementation of AP Microfinance Ordinance, SSF underwent the corporate debt restructuring (CDR) mechanism and restructured its borrowings. They managed to restructure their outstanding debts through operating profit from operations in other states and also raised refinancing debt from existing CDR lenders.

With the help of fresh capital infusion from Kangchenjunga (corporate promoter) and Kedaara AIF 1, the company was able to successfully exit from CDR in March 2017. As per ICRA Research notes they were one of the two major NBFC MF companies that were able to successfully exit from CDR. As on today, SSF operates through 929 branches in 269 districts across 16 states and a union territory with a workforce of 7062 employees (including 5051 credit assistants).

### Issue Details

IPO offers 1.4Cr shares of face value Rs.10 each amounting to Rs.1200 Cr on the upper price band of Rs.856. Out of total shares, 46,61,966 shares will be fresh issue (amounting Rs.400 Cr) and 93,56,725 shares are under offer for sale (amounting Rs.800 Cr) by the promoter and promoter group.

### Promoters selling in OFS

Promoter	No. of shares offered, up to
Kangchenjunga	5,967,097
Padmaja Gangireddy	1,423,114
Vijaya Siva Rami Reddy Vendidandi	796,509
Valiant	783,747
Helion II	132,831
Kedaara AIF 1	129,732
Helion	123,695
<b>Total</b>	<b>9,356,725</b>

Source: Company RHP, ACMIL

### Objectives Of the Issue are

- Augmenting capital base
- General corporate purposes
- Issue expenses

### IPO share allotment pattern

Category	Allocation	Number of Shares	Issue Size (Rs.Cr) at	
			Lower Band (Rs.853)	Upper Band (Rs.856)
QIB	50%	70,09,346	598	600
Non Institutional	15%	21,02,803	179	180
Retail	35%	49,06,542	419	420
<b>Total</b>	<b>100%</b>	<b>1,40,18,691</b>	<b>1,196</b>	<b>1,200</b>

Source: Company RHP, ACMIL

## Outlook and Valuations

Spandana Sphoorty Financial Limited is one of the largest NBFC - MF in the country with diversified geographical presence across Eastern and Southern India. Moving further, they are planning to expand towards under penetrated states and districts across the country supporting the upliftment of low income women and households. At the upper price band, asking price is at a P/BV of 2.73x at FY19 BVPS of Rs.317. Anticipating the good growth in NBFC - MF sector, we believe Spandana Sphoorty Financial Limited is well placed to grow. Hence, we recommend to SUBSCRIBE the issue with a long-term perspective.

## Business Overview

SSF is focused on rural areas and have variety of loans to offer in their product portfolio taking care of every need of borrower, making him/her independent and competent. Few of the products offered by SSF are :

- **Loan Against Property (LAP):** Offered in the states of Andhra Pradesh, Telangana, Karnataka, and Tamil Nadu, LAP is to support non BPL customers for business expansion, working capital requirement or to acquire assets. Loan size is up to Rs.50,00,000 with a tenure of 1 to 10 years. The interest rate of this product is 22% to 24% with 2% upfront processing fee exclusive of GST.
- **Abhilasha (JLG Loans):** This loan is designed especially for low-income households who aspire to improve their financial well-being. The primary objective of this loan is to empower women in setting up and expanding income generating activities, smoothen household cash flows and acquire productive assets. A hassle-free Weekly/Bi-Weekly/Monthly repayment option ensures that clients can save from their daily cash-flows and do not face repayment stress. The loan size is up to Rs.65,000 with tenure of 1 to 3 Years. The interest rate of this product is 24% with 1% upfront processing fee exclusive of GST.
- **Phinix:** These Loans are given exclusively to women in the state of Andhra Pradesh who already have an income generating source and want to expand their income generating activities or to acquire productive assets. It has a hassle free Weekly/Bi-Weekly/Monthly repayment structure makes it easy for borrowers to clear the loan without any stress. Loan amount is up to 52,000 with tenure of 1 to 2 years. The interest rate of this product is 24% with 1% upfront processing fee exclusive of GST.
- **Shree Loan:** Shree stands for "Good Beginning". Offered in the state of Andhra Pradesh, this loan is given to low/lower-middle-income people with clear credit history. These are Small Ticket Personal Loans up to Rs.52,000 with tenure of 1 to 2 years. The repayment frequency is Weekly/Bi-Weekly/Monthly. The interest rate of this product is 24% with 1% upfront processing fee exclusive of GST.
- **Gold Loans (Keertana):** Gold Loans are given against the mortgage of Jewellery. Loan size is up to Rs.50,00,000 with tenure up to 1 year. Repayment frequency is flexible/Monthly. The interest rate on this product varies between 16% - 24%. This loan is generally given for Agriculture, Business, and short-term liquidity needs. Currently, the loan is offered in the states of Andhra Pradesh and Telangana only.
- **Interim Loans:** These loans are to assist existing borrowers who are struggling to meet short-term liquidity requirements. This loan is offered to an individual on a group guarantee. Loan amount is up to Rs.18,000 with loan tenure of 1 to 3 years. The repayment frequency is Weekly/Bi-Weekly/Monthly. Interest rate of this product is 24% with 1% upfront processing fee exclusive of GST.

## Investment Rationale

### Geographically diversified business with a well structured business model

Over time, SSF has developed an in-depth understanding of the borrowing requirements of the low-income client segment. They have a well built business model, which involves regular client meeting processes at village/block level and client training across the places. A strong network of 7062 employees including 5051 credit assistants maintains regular contact with the clients. They operate out of 929 branches in 269 districts across 16 states and one union territory. To keep a check on geographical concentration risk they follow specified exposure caps at the state, district and branch levels i.e. the gross loan portfolio (GLP) of each state must not exceed 22.5% of the total portfolio (for AP and Telangana the combined cap at 6% of GLP) and the GLP for each district must not exceed 2.5% of total portfolio and 7.5% of net worth. No single state contribute more than 20.01% to AUM, no district contribute more than 1.82% to AUM and no branch more than 0.3% to AUM as of March 31, 2019.

### Resilient business practices led to support from strong Investors

Factors like client centric business model, strong internal control and expertise in understanding the borrower's requirements SSF have been able to strengthen their business and sustain crises like 2010 Andhra Pradesh CDR Regulation and demonetization. Even while under CDR, they continued operations outside Andhra Pradesh in various states focusing on rebuilding profitable operations through portfolio diversification, cost rationalization, customer retention, and recovery from Andhra Pradesh portfolio. These measures helped raising new debt from existing lenders and capital infusion from Kangchenjunga, their Corporate Promoter and Kedaara AIF 1, and also

helped to exit CDR in March 2017. They also increased their lender base, diversified borrowings to new banks and NBFCs and also issued NCDs in the capital markets which reduced average effective cost of borrowing from 16.31% for FY17 to 14.74% for FY18. According to ICRA Research, SSF were one of the only two major MFIs to successfully exit from CDR post AP crisis.

According to ICRA Research notes, due to demonetization collection efficiencies of MFIs dipped sharply from 98% to 75-80% during December 2016. However, SSF maintained collection efficiency of 97.13% for FY17.

### Focused on under penetrated rural areas

As on December 31, 2018 SSF had 88% of its portfolio located in rural areas compared to NBFC - MF segment average of 61%. Moving ahead they are planning to expand its branch network in under-penetrated states and districts of country. They are very much focused on clients in the rural areas which are a highly under-served market for formal banking services in terms of access, availability and suitability of products and services. According to ICRA Research, while rural India accounts for approximately 68% of India's population as of March 2018, it accounted for only 34% of total deposit accounts and 23% of the loan accounts in scheduled commercial banks. Such low borrowings from rural areas which are always in need of finance for upliftment provides strong potential for NBFC - MF institutions to explore business opportunities.

### Risk Management

Apart from geographical risk, SSF also take care of other business risks. They change norms in timely manner in response to business environment to ensure a responsive risk management strategy. They follow a set of eligibility criteria for clients as in every prospective client prior to disbursement is also assessed for their credit history with other lenders reporting into the credit bureau. As per ICRA research, vintage of SSF's portfolio is better than the industry, with over 25% of the portfolio in the fourth cycle compared to 11% for the industry as of December 2018. Further, in order to prevent frauds by employees, all field employees are transferred after spending a fixed period (not exceeding 18 months) at one location. They follow certain criteria while transferring employees to prevent the possibility of collusion with each other. For example, no two employees from the same village or tehsil of origin are allowed to work in the same branch and no two employees who have worked together in a branch are allowed to work together again in the same branch even after their transfers. These controls are automated with the use of technology. They also have well-established internal controls, a well-designed system for operations, strong policies and procedures to maintain financial discipline.

### Strong Financials despite of subdued industry growth

For FY19 standalone total income was Rs.10417mn, up 77% YoY backed by interest income of Rs.9914mn which increased 73% on yearly basis. Net profits for FY19 were Rs.3087mn, up 64% YoY. As on March 31, 2019, Gross AUM was Rs.44373mn, up 40% YoY with an average of Rs.12.58mn per employee. Operating Expense to Annual Average Gross AUM ratio for FY19 was 4.52% reflecting the cost efficiency of business operations. As of March 31, 2019, total borrowings were Rs.29,677.37mn, comprising debt securities amounting to Rs.13,719.64mn, borrowings (other than debt securities) amounting to Rs.15,754.79mn and subordinated liabilities amounting to Rs.202.94mn. Average Effective Cost of Borrowing was 12.84% for FY19 and finance cost to total income ratio was 34.13% compared to 39.45% in FY18, improving every year. Credit rating has improved to A- with stable outlook.

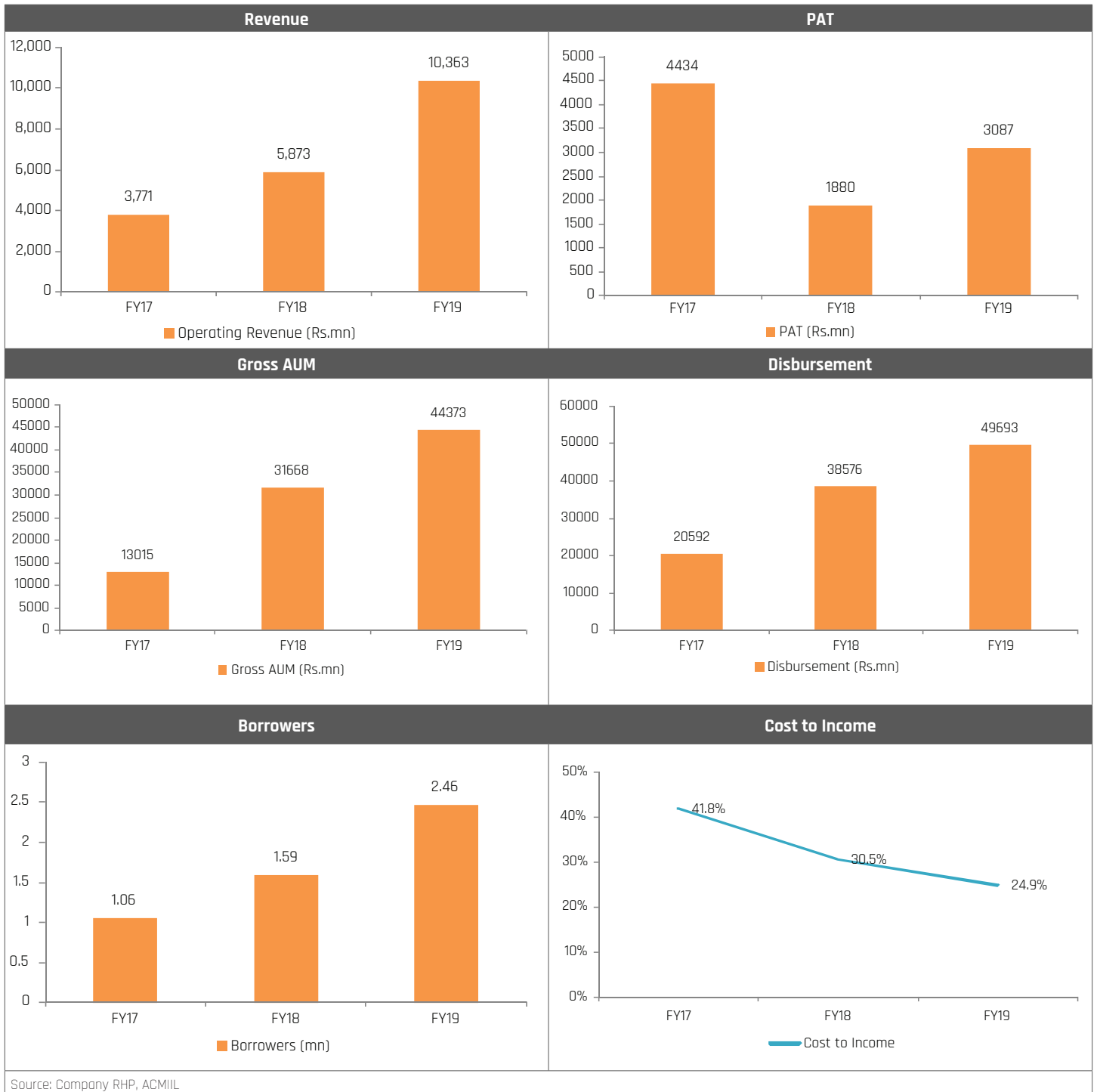
### Risk Factors

- **Government Policy and Regulation:** In India, NBFC - MF are highly regulated by RBI and Government policies & regulation. Any change in the regulatory framework affecting NBFC-MFIs might adversely affect operations and growth of SSF.
- **Geographical Presence:** SSF is dependent on few of the states for its business. Any geographical calamity in these geographies would impact the business and asset quality adversely.

### Peer Comparison

Name of the company	Face Value per share	EPS	PE	RoNW	NAV per share	PBV
Spandana Sphoorty Financial Limited	10	52.9	16.18	17%	317	2.70
Satin Creditcare Network Limited	10	39	6.71	17.5%	235	1.20
Ujjivan Financial Services Limited	10	12.4	22.5	8.0%	155	1.82
Bandhan Bank Limited	10	18.2	26	17.4%	94	5.01
Bajaj Finance Limited	2	75	42	20.0%	341	9.43
Cholamandalam Investment & Finance	2	15.5	16.78	19.0%	397	3.30
Shriram City Union Finance	10	153	9.08	15.0%	1014	1.37
Sundaram Finance Limited	10	101	14.3	13.0%	720	2.00
Mahindra & Mahindra Financials Services	2	21.95	13.44	16.4%	184	1.60

Source: Company RHP, ACMIL



Source: Company RHP, ACMIIL

## Standalone Financials

### Income statement

Particulars (Rs.mn)	FY17	FY18	FY19
Interest income	3,706	5,730	9,914
Commission income	38	40	148
Net gain on fair value changes	16	42	266
Others	10	61	35
<b>Total Revenue from operations</b>	<b>3,771</b>	<b>5,873</b>	<b>10,363</b>
Other income	16	2	54
<b>Total Income</b>	<b>3,787</b>	<b>5,875</b>	<b>10,417</b>
<b>Expenses</b>			
Finance cost	1,494	2,318	3565
Impairment on financial instruments	984	-354	454
Employee benefit expenses	581	759	1300
Depreciation and amortization expense	83	57	69
Other expenses	294	268	335
<b>Total expenses</b>	<b>3,436</b>	<b>3,048</b>	<b>5723</b>
Profit before exceptional items and tax	351	2827	4694
Exceptional items	105	-	0
<b>Profit before tax</b>	<b>456</b>	<b>2827</b>	<b>4694</b>
<b>Tax expense</b>			
Current tax	236	573	3
Deferred tax	-4214	374	1603
Income tax expense	-3978	948	1606
<b>Profit for the year</b>	<b>4434</b>	<b>1880</b>	<b>3087</b>

Source: Company RHP, ACMIIL

## Balance sheet

Particulars (Rs.mn)	FY17	FY18	FY19
<b>ASSETS</b>			
<b>Financial assets</b>			
Cash and cash equivalents	2,901	1,025	1,454
Bank balances other than cash and cash equivalents	23	1032	2,028
Trade receivables	15	26	35
Loan portfolio	11,945	30,896	41,654
Investments	1	21	646
Other financial assets	17	660	861
<b>Total financial assets</b>	<b>14,903</b>	<b>33,660</b>	<b>46,679</b>
<b>Non-financial assets</b>			
Current tax assets (net)	47	42	83
Deferred tax assets (net)	4,215	3,841	1,998
Property, plant and equipment	66	59	71
Intangible assets	24	26	22
Other non-financial assets	32	15	127
<b>Total non-financial assets</b>	<b>4,383</b>	<b>3,983</b>	<b>2,301</b>
<b>Total Assets</b>	<b>19,286</b>	<b>37,643</b>	<b>48,980</b>
<b>LIABILITIES AND EQUITY</b>			
<b>LIABILITIES</b>			
<b>Financial liabilities</b>			
Debt securities	0	10,147	13,720
Borrowings (other than debt securities)	9,325	12,965	15,530
Subordinated liabilities	10	202	202
Other financial liabilities	260	145	435
<b>Total financial liabilities</b>	<b>9,594</b>	<b>23,459</b>	<b>29,886</b>
<b>Non-financial liabilities</b>			
Current tax liabilities (net)	236	93	3
Provisions	6	4	3
Other non-financial liabilities	75	180	223
<b>Total non-financial liabilities</b>	<b>416</b>	<b>277</b>	<b>230</b>
<b>EQUITY</b>			
Equity share capital	284	298	596
Other equity	8,991	13,609	18,267
<b>Total equity</b>	<b>9,276</b>	<b>13,907</b>	<b>18,864</b>
<b>Total Liabilities and Equity</b>	<b>19,286</b>	<b>37,643</b>	<b>48,980</b>

Source: Company RHP, ACMIL

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