

Ujjivan Financial Services

11 May 2018

Reuters: UJVF.BO; Bloomberg: UJJIVAN IN

Farm Loan Waiver a Non-Issue

Ujjivan Financial Services (UFSL) reported its 4QFY18 results with the key strategic pointers being: (1) Management has clarified that any potential farm loan waiver will have minimal impact on business (2) There will be greater focus on retail deposits going forward (3) Branch conversion will be accelerated in FY19 leading to opex spike but will augment business opportunity (please see [initiating coverage report here](#), see conference-call highlights below). Per se, on the results front, UFSL posted Nil growth of 66% YoY to Rs2,109mn, PPOP growth of 217% YoY to Rs1,326mn and PAT growth of 236% YoY to Rs649mn. We have marginally modified our estimates for FY19/FY20 and retained Buy rating on UFSL, revising our target price to Rs467 (from Rs437 earlier), valuing the stock at 2.4x FY20E P/BV.

Liability profile continues to transform rapidly with increasing focus on retail deposits going forward: Having acquired a scheduled bank licence, UFSL has been garnering institutional deposits quickly and deposits now form 49% of total borrowings compared with 3% contribution a year ago. Legacy NBFC-style borrowings viz. term loans and NCDs have seen their share plummet to 17% and 8% from 63% and 12%, respectively. Refinance, which does not require CRR/SLR cover, has risen favourably to garner 26% share compared with 15% a year ago. Consequently, average cost of funds (deposits and borrowings) stands at 9% in FY18 compared with 10.4% in FY17. While the share of wholesale deposits is 88% of total deposits and CASA ratio is low at 3.7%, deposit traction is a significant favourable departure from the erstwhile NBFC-style higher cost funding. The management stated that USFL will increase focus on retail deposits going forward.

Branch conversion will be accelerated in FY19 leading to opex spike but will augment business opportunity: 187 out of 464 legacy branches stand converted as of FY18. Both achieved and expected pace of branch conversion keeps improving continually compared with earlier indications and augurs well from asset capacity addition perspective. Cost-to-income ratio improved significantly (~1966bps YoY) to 56.9% compared with 76.6% in 4QFY17 and 69.05% in 3QFY18 due to most of the branch openings being low cost URCS. Branch conversion will be accelerated and completed in FY19 leading to opex spike but this would augment business capacity. Importantly, converted branches will be equipped to deliver all asset and liability products and will help register strong traction in new MSE, and housing loan businesses, which grew 37% and 42% QoQ respectively. MSE and housing now account for 3% and 4% of gross loans, respectively.

Any potential farm loan waiver will have minimal impact on business: Management has clarified that farm loan waiver will have minimal impact on business as USFL is minimally rural focused, especially in Karnataka. 'New book' created after 1 January 2017 continues to see pristine asset quality with a collection efficiency of 99.6%, indicating stress is contained within the legacy book. GNPA ratio eased 60bps QoQ to 3.6%. USFL maintains a provision cover of 81.5%. PAR declined by Rs3460mn during FY18, with PAR>0 at 4% and PAR>90 at 3.6% as of FY18-end.

Valuation and outlook: We have revised our Nil estimates by 0.8%/0.1% for FY19/FY20, our PPOP estimates by -16.8%/-1.1% and our PAT estimates by -9.4%/3.1%, respectively. We have retained Buy rating on USFL, valuing the stock at 2.4x FY20E P/BV and revising our target price to Rs467 (from Rs437 earlier).

Y/E March (Rsmn)	4QFY18	4QFY17	3QFY18	YoY (%)	QoQ (%)
Interest income	3,642	2,891	3,372	26.0	8.0
Interest expenses	1,533	1,617	1,414	(5.2)	8.5
Net interest income	2,109	1,274	1,958	65.5	7.7
NIM (%)	0.0	8.6	11.1	-861 bps	-1,108 bps
Fee & other income	968	510	469	89.8	106.2
Operating income	3,077	1,784	2,428	72.5	26.7
Staff costs	958	765	932	25.2	2.8
Other operating exp.	793	601	742	31.9	6.9
Total operating expenses	1,751	1,366	1,674	28.2	4.6
Cost-to-income (%)	56.9	76.6	69.0	-1,966 bps	-1,205 bps
Cost-to-AUM (%)	9.6	8.4	9.7	113 bps	-17 bps
Operating profit	1,326	418	754	217.2	75.9
Provisions	347	72	287	381.9	20.9
Credit cost (%)	1.9	0.5	1.7	144 bps	19 bps
PBT	979	346	467	182.9	109.8
Tax	330	153	173	115.7	90.3
-Effective tax rate	33.7	44.2	37.2	-1,051 bps	-344 bps
PAT	649	193	293	236.2	121.3
EPS (Rs)	5.4	1.6	2.4	232.0	120.7
BV (Rs)	145.7	147.0	140.4	-0.9	3.7
AUM	75,600	63,795	70,953	18.5	6.5
Deposits	37,968	1,064	23,354	3,468.4	62.6

Source: Company, Nirmal Bang Institutional Equities Research

BUY

Sector: Banking

CMP: Rs404

Target Price: Rs467

Upside: 16%

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Key Data

Current Shares O/S (mn)	120.9
Mkt Cap (Rsbm/US\$m)	48.8/725.5
52 Wk H / L (Rs)	428/285
Daily Vol. (3M NSE Avg.)	1,218,119

Price Performance (%)

	1 M	6 M	1 Yr
Ujjivan Financial Services	7.1	5.6	16.4
Nifty Index	3.0	3.8	13.9

Source: Bloomberg

Key conference-call highlights

- USFL continues to make investments in new technology infrastructure by introducing hand held devices and biometrics in ATMs, etc.
- USFL plans to increase banking outlet count to 475 by the end of FY19.
- The management expects greater traction on CASA and retail deposits in FY19.
- USFL has repaid Rs43530mn of legacy borrowings in FY18.
- 73% of retail deposits were from new customers.
- The management expects 18-20% growth in microfinance loans in FY19.
- The management does not expect any material impact from farm loan waivers since they are non-rural focused and loans with agri-end use have low proportion.
- USFL is targeting a 25% share of retail deposits in total deposits.
- Due to accelerated branch openings, the management expects a cost to income ratio of ~70% for FY19.
- Write offs for the year stood at Rs1770mn.
- The management guided for 30-50bps credit costs for FY19.
- Incremental cost of deposits stood at 7.5%.
- Yield on the housing loan book stood at 14% and yield on the MSE book was in the 18-20% range.
- The management stated that the off balance sheet book is negligible and that USFL will not be undertaking any securitization transactions.
- The management expects a 30-35% CAGR on the overall portfolio.
- The management guided for flattish NIM expectations for FY19.
- USFL will not require additional capital till FY20, and will look to raise additional capital post FY20.
- There were 127 branches with PAR>5%, and USFL will resume business in the branches with good business traction.
- USFL's average loan cycle is ~18 months.
- The management expects ~10% growth in JLG ticket sizes.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Net Interest Income	5,075	6,831	7,095	9,549	11,844
Pre-Provision Profit	2,973	3,969	3,226	4,030	6,828
PAT	1,772	2,077	73	2,305	3,685
EPS (Rs)	17.5	17.4	0.6	19.1	30.5
BV (Rs)	118.4	147.0	145.7	167.7	197.2
P/E (x)	23.1	23.2	663.8	21.2	13.2
P/BV (x)	3.4	2.7	2.8	2.4	2.0
Gross NPA (%)	0.2	0.3	3.6	2.2	1.5
Net NPA (%)	0.0	0.0	0.7	0.4	0.3
RoA (%)	3.7	2.9	0.1	1.9	2.4
RoE (%)	18.3	14.1	0.4	12.2	16.7

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Actual performance versus our estimates

(Rsmn)	4QFY18	4QFY17	3QFY18	YoY (%)	QoQ (%)	4QFY18E	Devi. (%)
Net interest income	2,109	1,274	1,958	66%	8%	2,663	-21%
Pre-provision profit	1,326	418	754	217%	76%	1,349	-2%
PAT	649	193	293	236%	121%	657	-1%

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

	Revised estimate		Earlier estimate		% revision	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Net interest income (Rsmn)	9,549	11,844	9,474	11,831	0.8	0.1
NIM (%)	9.9	9.7	9.9	9.6	-1 bps	16 bps
Operating profit (Rsmn)	4,030	6,828	4,845	6,907	(16.8)	(1.1)
Profit after tax (Rsmn)	2,305	3,685	2,543	3,575	(9.4)	3.1
EPS (Rs)	19.1	30.5	21.3	29.9	(10.5)	1.8
ABV (Rs)	164.6	194.5	163.8	193.2	0.5	0.7

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: One-year forward P/ABV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Interest income	9,310	12,258	13,145	16,529	20,834
Interest expense	4,235	5,427	6,049	6,979	8,990
Net interest income	5,075	6,831	7,095	9,549	11,844
Loan origination fees	708	776	2,673	1,686	2,149
Other income	258	943	-	1,661	2,454
Net revenues	6,041	8,550	9,768	12,896	16,448
Operating expenses	3,068	4,581	6,542	8,867	9,620
-Employee expenses	1,967	2,716	3,666	5,127	4,758
-Other expenses	1,102	1,865	2,877	3,740	4,861
Operating profit	2,973	3,969	3,226	4,030	6,828
Provisions	253	751	3,107	483	1,158
PBT	2,720	3,218	119	3,546	5,670
Tax	948	1,141	46	1,241	1,984
PAT	1,772	2,077	73	2,305	3,685

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Share capital	1,012	1,194	1,209	1,209	1,209
Reserves & surplus	10,966	16,359	16,405	19,060	22,629
Net worth	11,978	17,553	17,613	20,269	23,838
Deposits	-	1,064	37,968	47,350	72,763
Borrowings	43,380	62,914	38,528	53,217	62,636
Other liabilities & provisions	1,915	3,255	4,540	16,249	17,107
Total liabilities	57,273	84,786	98,649	137,085	176,344
Fixed assets	242	1,398	1,984	2,710	3,436
Investments	1	14,467	12,325	20,821	27,047
Loans	50,643	58,712	75,597	84,979	110,392
Cash	4,913	7,601	5,937	11,897	15,455
Other assets	1,475	2,608	13,898	16,678	20,014
Total assets	57,273	84,786	109,741	137,085	176,344
AUM	53,885	63,795	75,597	94,421	122,658

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Key ratios

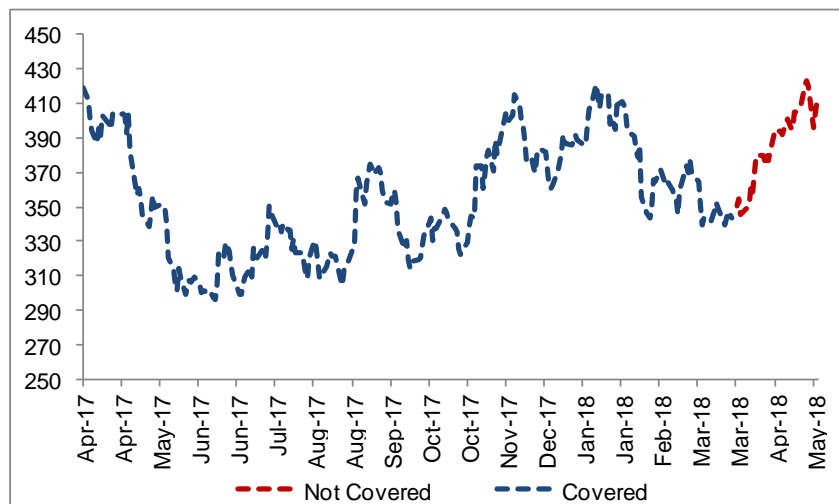
Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Growth (%)					
Net interest income	34.6	3.9	34.6	24.0	34.6
Operating profit	33.5	(18.7)	24.9	69.4	33.5
Profit after tax	17.2	(96.5)	3,036.8	59.9	17.2
Business (%)					
Deposit growth	-	3,468.4	24.7	53.7	-
CASA	3.0	3.0	4.0	7.0	3.0
Advance growth	15.9	28.8	12.4	29.9	15.9
AUM growth	18.4	18.5	24.9	29.9	18.4
Spread (%)					
Yield on AUM	20.8	18.9	18.3	17.9	20.8
Yield on BS loans	22.4	19.6	19.4	19.9	22.4
Cost of funds	10.8	8.6	7.9	7.6	10.8
Core spread	11.7	11.0	11.5	12.2	11.7
NIM	12.5	8.8	9.9	9.7	12.5
Operational efficiency (%)					
Cost-to-income	53.6	67.0	68.8	58.5	53.6
Cost-to-AUM	7.8	9.4	10.4	8.9	7.8
Productivity (Rsmn)					
AUM per branch	139.6	162.9	203.5	264.3	139.6
AUM per employee	6.3	6.7	7.0	10.3	6.3
Employee per branch	22.2	24.2	29.1	25.6	22.2
CRAR (%)					
Tier I	16.8	22.3	18.9	17.1	16.8
Tier II	1.4	0.7	1.3	1.2	1.4
Total	18.2	23.0	20.2	18.3	18.2
Asset quality (%)					
Gross NPAs	0.3	3.6	2.2	1.5	0.3
Net NPAs	0.0	0.7	0.4	0.3	0.0
Provision coverage	89.3	81.6	80.0	80.0	89.3
Credit cost (excluding std asset)	1.4	6.0	0.3	0.8	1.4
Credit cost (including std asset)	1.6	6.2	0.6	1.2	1.6
Return ratios (%)					
RoE	14.1	0.4	12.2	16.7	14.1
RoA	2.9	0.1	1.9	2.4	2.9
Per share (%)					
EPS	17.4	0.6	19.1	30.5	17.4
BV	147.0	145.7	167.7	197.2	147.0
ABV	146.9	141.5	164.6	194.5	146.9
Valuation (x)					
P/E	23.2	663.8	21.2	13.2	23.2
P/BV	2.7	2.8	2.4	2.0	2.7
P/ABV	2.7	2.9	2.5	2.1	2.7

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 March 2018	Buy	343	437
11 May 2018	Buy	404	467

Rating track graph



DISCLOSURES

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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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