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ANCHOR REPORT

Global Markets Research

11 December 2020

Microfinance – the next decade of opportunity

Long-term opportunity outweighs near-term risk

India Financials

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Microfinance still presents a huge growth opportunity over the next decade and we forecast 18%/16% AUM CAGR over the next 5/10 years. The rural segment, with penetration rates fairly low at c.30%, has the greatest growth potential, in our view, and we estimate 18% AUM CAGR over the next decade. Looking beyond COVID-19, we remain confident that the MFI space will deliver both superior growth and through-cycle profitability. We find CREDAG to be well-positioned to capitalize on this opportunity and initiate coverage with a Buy rating. We also turn positive on small finance banks with better visibility on holdco discounts reducing, and reiterate our positive stance on Bandhan Bank.

Key themes and analysis in this Anchor report include:

- Penetration opportunity and key players' market share trends across geographies.
- Cost efficiency benchmarking across MFI players and their loss-absorption capacity (Covid impact).
- Initiating on CreditAccess Grameen (CREDAG IN) with Buy, and maintain Buy on Bandhan (BANDHAN IN) and Equitas Holdings (EQUITAS IN), and upgrade Ujjivan Financial Services (UJJIVAN IN) to Buy.

Production Complete: 2020-12-12 07:58 UTC

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Long-term opportunity outweighs near-term risks; Initiating on CREDAG at Buy

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Action: Initiating on CREDAG at Buy, with 24% implied upside; raise TPs for Bandhan, Equitas and Ujjivan

We see huge opportunity in the MFI space over the next decade despite penetration levels having already improved to 38% (FY20). Specifically, we expect opportunities in the rural market to remain large and forecast 18%/16% AUM CAGRs over the next 5/10 years, with rural segment growing at a faster clip. We think rural-focused NBFC-MFIs are best-placed to capitalize on this opportunity with: 1) a large segment of the MFI players either converting to banks/SFBs (and diversifying away from MFI); 2) the COVID-19 impact further accelerating consolidation among top players, and 3) improving funding environment.

CREDAG – tailored to capitalize on the opportunity

We believe CREDAG is best-positioned to capitalize on the opportunities in the rural market (we estimate 18% five-year CAGR for the industry, within which we expect rural to grow faster at 21%) with: 1) its rural focus (86% of AUMs); 2) strong operational practices; 3) tailor-made approach; and 4) strong parentage aiding a 19% AUM CAGR over FY20-23F. We think CREDAG has been ticking the right boxes with its prudent underwriting and its customer-centric approach. The pandemic remains a near-term concern and resurgent cases in Maharashtra have led to relatively lower collection efficiency for CREDAG (89% in Oct-20). However, we think standard provisions of 3.5% of AUMs, robust PPOP/AUMs of 7% (FY21-23F average), and strong capital position (Tier-1 of 25.6%) should not only aid CREDAG to absorb the COVID-19 impact, but also benefit from the growth opportunity over the medium term. We initiate coverage on CREDAG at Buy with a TP of INR950, implying 24% upside.

Upgrade Ujjivan to Buy; re-iterate our positive stance on Equitas and Bandhan

We upgrade Ujjivan Financial Services to Buy and reiterate our positive stance on Equitas Holdings (Buy) building in a lower holdco discount now, and re-iterate our positive stance on Bandhan Bank (Buy).

Premium valuations to sustain; initiating coverage on CREDAG at Buy

We value CREDAG at INR950 based on the residual income model, implying 2.7x FY23F book multiple and believe its premium valuations are likely to sustain, given: 1) its strong parentage and management; 2) solid pedigree with a proven track record; and 3) robust growth/ earnings delivery. Further, the standard provision buffer of 3.5% of loans and strong PPOP/AUMs and strong capital positioning (Tier 1 of 25.6%) should help CREDAG navigate the current cycle well. We find current valuations at 2.3x FY23F book reasonable in that context and expect ROEs to normalize to 18% by FY23F, with FY20-23F EPS CAGR of 35% despite building in 430/200bp credit costs for FY21/22F.

Key risks: Unsecured book, concentration risks and higher-than-expected COVID-19 stress remain key near-term risks.

Fig. 1: Stocks for action

Stock	Ticker	Rating	M cap (USD mn)	3M ADTV (USDmn)	TP (INR)	Price (INR)	Upside (%)
CREDAG	CREDAG IN	Buy (IC)	1,623	1.3	950	768	23.7%
Bandhan	BANDHAN IN	Buy	8,758	58.7 ↑	490	400	22.5%
Equitas	EQUITAS IN	Buy	337	4.7 ↑	95	73	30.9%
Ujjivan	UJJIVAN IN	Buy ↑	472	4.8 ↑	360	286	26.1%

Note: Priced as at close of markets on 9 December 2020
Source: Bloomberg, Nomura estimates. Initiating coverage on CREDAG

Fig. 2: Peer valuation comps

Banks	Ticker	Rating	TP	P/B			P/E			ROE			LTP
				FY21F	FY22F	FY23F	FY21F	FY22F	FY23F	FY21F	FY22F	FY23F	
Corporate Banks													
Axis	AXSB IN	Buy	640	1.79	1.60	1.40	23.3	14.4	10.7	8.4%	11.8%	13.9%	635
ICICI	ICICIBC IN	Buy	625	1.87	1.68	1.47	18.1	13.5	10.5	11.4%	13.1%	14.9%	511
SBI	SBIN IN	Buy	275	0.65	0.60	0.54	13.5	6.8	5.4	4.9%	9.2%	10.5%	271
BOB	BOB IN	Neutral	50	0.53	0.51	0.47	NM	37.5	8.0	-3.7%	1.2%	5.3%	66
Retail Banks													
HDFCB	HDFCB IN	Buy	1,450	3.87	3.35	2.85	27.5	21.7	17.0	14.9%	16.6%	18.2%	1,406
Kotak	KMB IN	Neutral	1,570	4.71	4.19	3.71	41.0	35.7	30.8	13.0%	12.4%	12.8%	1,885
NBFCs/ HFCs													
HDFC	HDFC IN	Buy	2,425	2.33	2.13	1.94	25.8	20.1	16.8	10.6%	11.6%	12.6%	2,309
MMFSL	MMFS IN	Neutral	130	1.40	1.29	1.17	26.5	12.1	9.5	5.8%	10.8%	12.6%	177
New Banks/ MFIs													
Equitas	EQUITAS IN	Buy	95	1.03	0.93	0.81	12.3	9.5	6.5	9.3%	10.3%	13.4%	73
Bandhan Bank	BANDHAN IN	Buy	490	3.76	3.18	2.68	24.0	15.9	13.6	16.6%	21.7%	21.5%	400
AU SFB	AUBANK IN	Neutral	790	5.78	5.10	4.27	44.6	40.6	24.6	10.4%	13.4%	18.9%	918
Ujjivan	UJJIVAN IN	Buy	360	1.51	1.36	1.19	19.2	12.9	9.1	8.2%	11.1%	13.9%	286
CREDAG	CREDAG IN	Buy	950	3.03	2.62	2.20	36.6	19.6	13.7	9.9%	14.3%	17.5%	768

Note: Priced as at close of markets on 9 December 2020
Source: Company data, Nomura estimates

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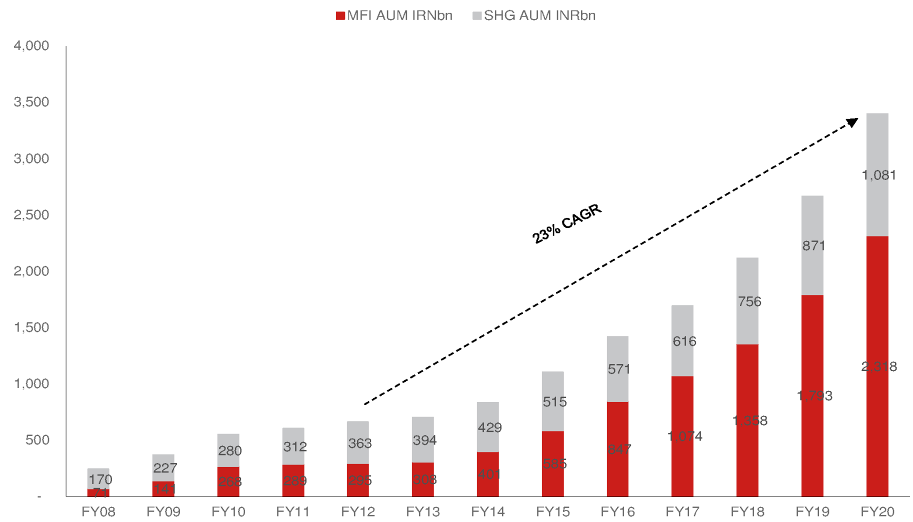
Microfinance segment is meaningfully large now

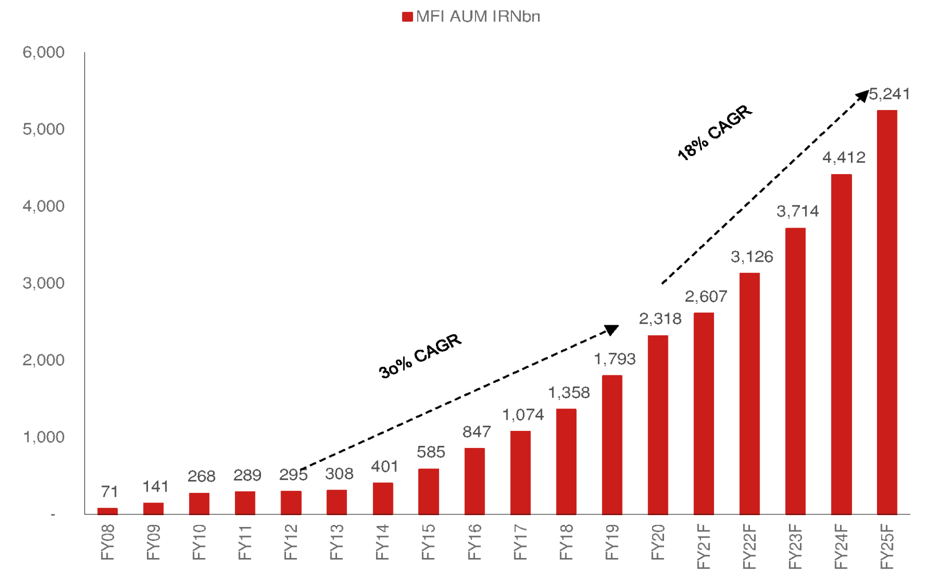
- India's microfinance (MFI) sector has become a meaningfully large segment with INR3.4tn of AUM (including self-help groups [SHG]) as of end-FY20 and has grown at ~23% CAGR over FY12-20. Excluding SHG, growth has been even stronger at ~30% CAGR with an AUM of INR2.3tn for the same period. This makes it one of the largest retail segments after mortgages, as well as the fastest-growing segment with a three-year CAGR of ~30% vs retail loan CAGR of 17% for FY17-20.
- Penetration levels have improved from <18% in FY12 to ~38% of the addressable market as of end-FY20; however, we see a sustainable growth opportunity in this segment with penetration levels likely to improve further, especially in the rural segment. We expect retail loans to provide further growth tailwind as a small portion of borrowers graduate from MFI to retail loans.
- Such strong growth was driven by a 12% CAGR for both ticket sizes, as well as overall unique borrowers reaching ~60mn (>85mn including SHG borrowers, assuming a 50% overlap).
- The industry has consolidated with every past crisis, with AUMs getting more concentrated in the top 6-7 players, which currently account for ~50% of the industry's total AUM (ex-SHGs) vs 40% in FY12. Of the total 105mn MFI accounts (including overlap accounts and excluding SHG), top 7 players account for ~37% of the borrower accounts. We expect the COVID-19 pandemic to further accelerate the consolidation, benefitting the top players in the segment.

Fig. 3: Overall microfinance AUM (incl. SHGs) has recorded 23% CAGR for FY12-20



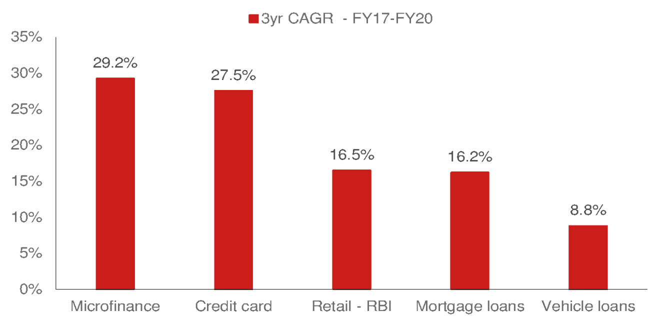
Source: Company data, Nomura research

Fig. 4: Growth has been even faster for MFIs (ex-SHG) at 30% CAGR; we forecast an 18% CAGR for FY20-25F



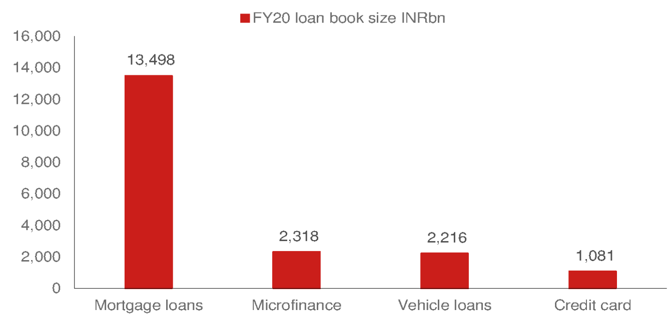
Source: Company data, Nomura estimates

Fig. 5: Microfinance 3-year CAGR at 30% for FY17-20F is the best across all retail categories...



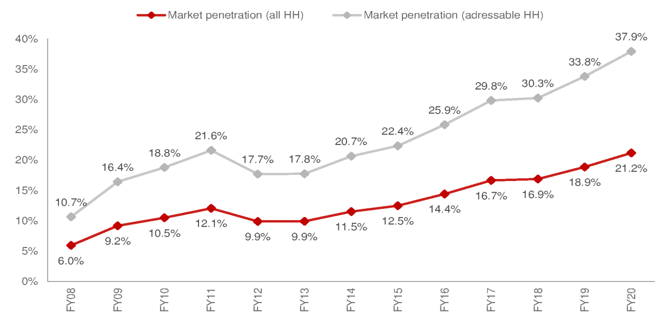
Source: RBI, Nomura research

Fig. 6: ...making MFI the the second-largest retail category after mortgages



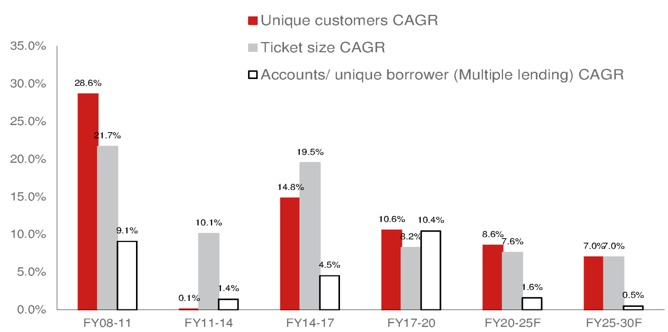
Source: RBI, Nomura research

Fig. 7: We estimate the current penetration level at ~38% of the addressable households in India



Source: Equifax, Nomura estimates

Fig. 8: We expect both ticket sizes and unique customers to grow at 7-8% – leading to total MFI book growth of 18% over FY20-25F



Source: MFIN, Equifax, Nomura estimates

Fig. 9: Past crisis has lead to further consolidation – top-7 players hold 47% market share (by AUM) currently

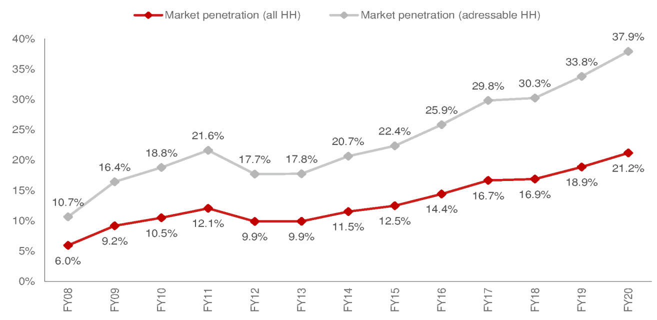
Top Player market share -	AP crisis impact					Demonetisation impact				
Disruptions impact	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Bandhan	8.7%	12.6%	14.4%	15.2%	16.3%	18.2%	19.9%	20.4%	21.5%	19.9%
Equitas	2.7%	2.5%	3.7%	3.7%	3.7%	3.9%	3.1%	1.7%	1.7%	1.6%
Ujjivan	2.2%	2.4%	3.5%	3.8%	5.0%	5.5%	5.0%	4.7%	5.2%	4.6%
SKS/ BHAFIN	14.2%	5.7%	7.7%	7.8%	7.1%	9.1%	8.5%	9.3%	9.7%	10.5%
CREDAG	0.9%	1.4%	1.9%	2.0%	2.5%	3.0%	2.9%	3.7%	4.0%	4.3%
Spandana	12.0%	9.2%	3.8%	2.2%	2.0%	1.4%	1.2%	2.3%	2.4%	2.9%
Madura		0.5%	0.5%	0.6%	0.6%	0.6%	0.8%	0.9%	1.1%	0.9%
Satin		1.1%	1.9%	2.6%	3.7%	3.9%	3.4%	3.2%	3.6%	3.1%
ESAF		1.0%	1.4%	1.5%	1.7%	2.3%	2.5%	2.5%	2.7%	2.7%
Fincare (Disha + Future)		0.8%	0.8%	0.9%	1.1%	1.1%	1.1%	1.3%	1.6%	1.8%
Jana	0.6%	1.2%	3.1%	5.1%	6.4%	13.0%	11.9%	4.3%	3.1%	3.0%
North East				0.3%	0.4%	0.6%	0.6%	0.8%	0.8%	0.6%
Suryoday		0.3%	0.5%	0.8%	1.0%	1.2%	0.8%	1.1%	1.2%	1.2%
Utkarsh		0.3%	0.6%	0.8%	1.2%	1.7%	1.5%	2.0%	2.3%	2.6%
Share		7.1%	3.1%	2.1%	1.1%					
Top 7		**34.8%**	**36.7%**	**37.3%**	**40.2%**	**45.0%**	**44.0%**	**45.1%**	**48.1%**	**46.9%**
All SFBs		**8.3%**	**13.6%**	**16.9%**	**20.6%**	**29.3%**	**26.6%**	**18.4%**	**18.6%**	**18.1%**
Top 3 NBFC-MFIs (incl BHAFIN)		**8.1%**	**11.4%**	**12.4%**	**13.3%**	**15.9%**	**14.8%**	**16.1%**	**17.2%**	**17.8%**

Source: MFIN, Nomura research

Penetration levels have improved meaningfully – opportunity still large; especially in rural

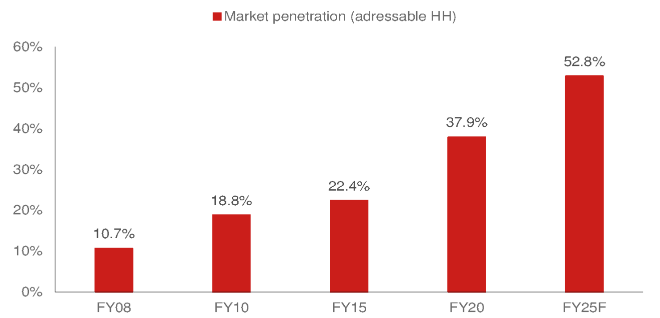
- Penetration levels have improved meaningfully over the past decade with <18% levels as of FY12 improving to ~38% by end-FY20, on our estimate. We forecast penetration levels to improve further to 53% over the next five years.
- Although penetration is not low anymore, we see few pockets of opportunities remain large, especially in rural areas. With ~38% penetration level on a pan-India basis, we estimate the urban market to have reached >50% level while rural remains low at ~30%. Growth in rural areas has outpaced the urban segment, recording 38% CAGR over the past three years vs the urban segment at 24% CAGR for the same period. This trend, in our view, should continue going forward, with lower COVID-19 pandemic-related impact in the rural segment.
- We expect rural segment to continue to drive growth for the sector over the next decade, as cost efficiencies over the past decade and investments in technology/digital initiatives enable a much deeper penetration.
- AUMs currently remain concentrated in top-10 states, which account for >80% of the MFI AUMs – with top-5 states contributing ~55% of the AUMs. States like Tamil Nadu, Karnataka, West Bengal, Assam, Bihar and Odisha seem to be fairly penetrated, with incremental growth of 30-50% CAGR for the past four years and ahead of the industry growth rate.
- That said, we see incrementally lower-penetrated states like Maharashtra, Uttar Pradesh, Madhya Pradesh and other states (below top-10) to drive incremental growth; these states have delivered 35-45% CAGR over the past two years – ahead of the industry CAGR of ~30%.

Fig. 10: We estimate the current penetration level at 38% of the addressable households in India



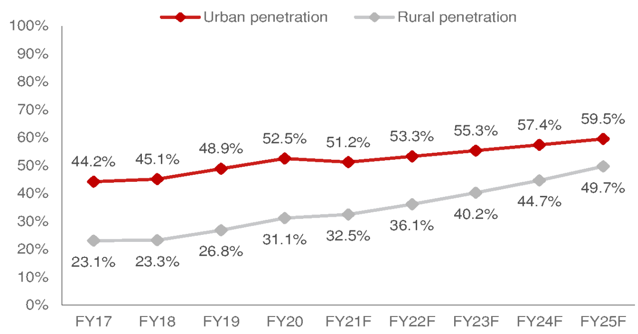
Source: Equifax, Nomura estimates

Fig. 11: We forecast penetration levels of 52-53% by FY25F



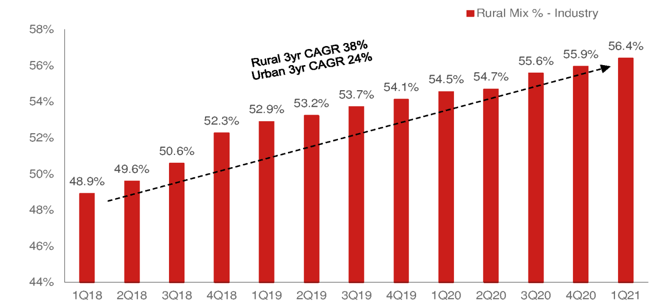
Source: Equifax, Nomura estimates

Fig. 12: Rural vs urban penetration – we estimate much higher penetration in urban at >50% vs ~30% level in rural



Source: CRIF Highmark, Nomura estimates

Fig. 13: Over the past two years – rural segment has grown faster, at 38% CAGR, vs urban at 24%



Source: CRIF Highmark, Nomura research

Fig. 14: Lower-penetrated states like Maharashtra, UP, MP and B-10 states should support growth, in our view

	GLP INRbn						
States with portfolio >INR10bn	FY16	FY18	FY20	4yr CAGR	2 yr CAGR	Penetration (incl. SHG)	30+ DPD - 4Q20 - Industry
Tamil Nadu	110	188	324	30.9%	31.2%	80.3%	1.19%
West Bengal	101	196	309	32.1%	25.5%	52.6%	0.70%
Bihar	53	117	262	49.0%	49.6%	61.4%	0.30%
Karnataka	81	110	190	23.9%	31.3%	65.0%	3.16%
Maharashtra	**81**	**89**	**164**	**19.2%**	**35.5%**	**28.6%**	**1.15%**
Uttar Pradesh	**72**	**84**	**152**	**20.7%**	**34.4%**	**19.4%**	**0.73%**
Madhya Pradesh	**53**	**73**	**133**	**25.7%**	**34.8%**	**45.0%**	**1.41%**
Odisha	37	80	128	36.2%	26.9%	72.3%	1.38%
Assam	38	82	113	31.4%	17.7%	72.8%	13.90%
Kerala	30	58	94	33.3%	27.5%	42.6%	1.28%
Others	**125**	**196**	**412**	**34.9%**	**45.2%**	**25.3%**	**1.03%**
India	**781**	**1,272**	**2,281**	**30.7%**	**33.9%**	**56.1%**	**1.78%**
Top 5	**427**	**700**	**1,248**	**30.8%**	**33.5%**	**60.4%**	**1.3%**
Top 10	**657**	**1,077**	**1,868**	**29.9%**	**31.7%**	**56.6%**	**2.5%**

Source: MFIN, Nomura research

Penetration level divergence still exists – few states are getting overheated

- We see a sharp increase in penetration in states like Tamil Nadu, Karnataka, Odisha, Assam and Bihar where we incrementally see some signs of overheating.
- Penetration levels in these key states have improved, aided by the higher AUM CAGR of 30-50% for FY16-20 v/s ~30% growth for the industry.
- Increasing competitive intensity in these states is also visible from a relatively sharper increase in the number of MFIs operating there. For example, the number of MFIs operating in Odisha has increased from 10 in FY16 to 27 in FY20, and Assam has seen MFIs rising to 19 currently from 8 in FY16 while Bihar has seen 17 MFIs increasing to 35 over the same period.
- Ticket sizes too have recorded 18-20% CAGR for FY17-20, showing some signs of overheating in these states.
- That said, incremental growth in these states has been slowing down with 20-30% CAGR recorded for FY18-20, while the lesser-penetrated states like Maharashtra, Uttar Pradesh and Madhya Pradesh are growing at a faster pace of ~40% CAGR for FY18-20 as MFIs make inroads into new geographies.

Fig. 15: State-wise penetration levels: Few states like TN, Karnataka, Odisha, Assam and Bihar are showing signs of over-heating

States (mn)	Population		Households			MFI		SHG		Total (ex overlap 50%)	Penetration levels %		
	FY19	FY20F	Avg = 5 member	Ex BPL	Adressable 70%	Accounts	Borrowers	Groups	Members		MFI	SHG	Total (ex overlap)
Tamil Nadu	78	79	15.8	14.0	9.8	15.7	7.9	0.4	3.9	9.8	80.3%	39.5%	100.1%
Karnataka	68	69	13.7	10.9	7.6	9.7	4.9	0.7	6.7	8.3	65.0%	87.6%	108.8%
West Bengal	100	101	20.2	16.2	11.3	10.7	6.0	0.8	8.2	10.1	52.6%	72.7%	88.9%
Kerala	36	36	7.3	6.7	4.7	4.5	2.0	0.3	2.9	3.5	42.6%	61.6%	73.3%
Odisha	46	47	9.4	6.3	4.4	6.6	3.2	0.3	3.3	4.8	72.3%	74.7%	109.7%
Maharashtra	123	125	25.0	20.7	14.5	8.2	4.1	0.2	2.3	5.3	28.6%	16.2%	36.7%
Uttar Pradesh	238	242	48.3	34.1	23.9	7.3	4.6	0.2	1.5	5.4	19.4%	6.4%	22.6%
Assam	36	36	7.2	4.9	3.4	4.3	2.5	0.1	1.0	3.0	72.8%	29.4%	87.5%
Bihar	125	127	25.4	16.8	11.8	11.9	7.2	0.7	6.9	10.7	61.4%	58.4%	90.6%
Madhya Pradesh	84	85	17.0	11.6	8.1	6.4	3.7	0.1	1.1	4.2	45.0%	13.0%	51.5%
Others	385	391	78.3	61.8	43.3	19.0	10.9	1.0	10.3	16.1	25.3%	23.8%	37.2%
India	**1,371**	**1,393**	**278.7**	**217.6**	**152.3**	**104.1**	**57.1**	**5.7**	**56.8**	**85.5**	**37.5%**	**37.3%**	**56.1%**

Source: MFIN, Equifax, Nomura research

Fig. 16: Lesser-penetrated states like Maharashtra, UP, MP and B-10 states should support growth, in our view

States with portfolio >INR10bn	GLP INRbn			4yr CAGR	2 yr CAGR	Penetration (incl. SHG)	30+ DPD - 4Q20 - Industry
	FY16	FY18	FY20				
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Uttar Pradesh	**72**	**84**	**152**	**20.7%**	**34.4%**	**19.4%**	**0.73%**
Madhya Pradesh	**53**	**73**	**133**	**25.7%**	**34.8%**	**45.0%**	**1.41%**
Odisha	37	80	128	36.2%	26.9%	72.3%	1.38%
Assam	38	82	113	31.4%	17.7%	72.8%	13.90%
Kerala	30	58	94	33.3%	27.5%	42.6%	1.28%
Others	**125**	**196**	**412**	**34.9%**	**45.2%**	**25.3%**	**1.03%**
India	**781**	**1,272**	**2,281**	**30.7%**	**33.9%**	**56.1%**	**1.78%**
Top 5	**427**	**700**	**1,248**	**30.8%**	**33.5%**	**60.4%**	**1.3%**
Top 10	**657**	**1,077**	**1,868**	**29.9%**	**31.7%**	**56.6%**	**2.5%**

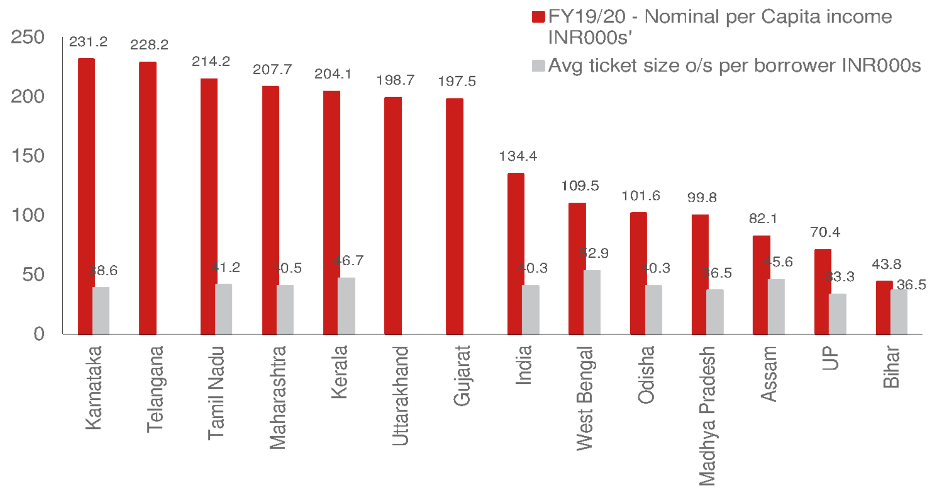
Source: MFIN, Nomura research

Fig. 17: Significant increase in the number of MFIs operating in overheated states

State wise Count of NBFC-MFIs operational	FY12	FY14	FY17	FY20
Assam	7	6	6	19
Bihar	14	17	15	35
Chattisgarh	8	8	16	27
Delhi	8	9	5	4
Gujarat	16	18	11	22
Haryana	10	9	11	21
Jharkand	7	10	12	28
Karnataka	15	18	12	18
Kerala	7	7	7	10
Maharashtra	17	22	24	26
Madhya pradesh	17	21	19	26
Orrisa	11	11	13	27
Punjab	4	5	8	13
Rajasthan	12	14	14	24
Tamil Nadu	24	20	10	18
Uttarakhand	7	10	10	12
Uttar Pradesh	14	15	15	29
West Bengal	11	12	8	23

Source: MFIN, Nomura research

Fig. 18: Average income levels vs average microfinance loan outstanding tickets across states

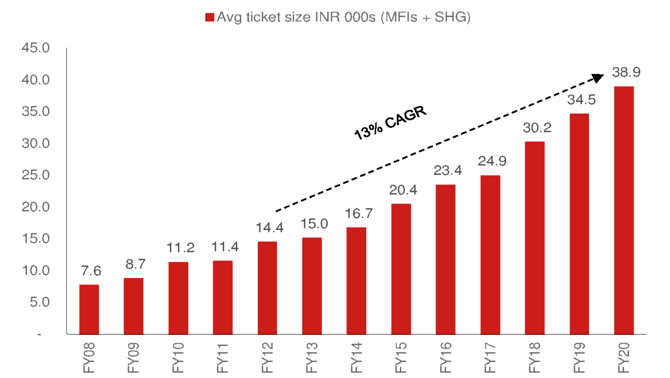


Source: Sa DHAN, Nomura research

Improving customer vintage has aided ticket size growth

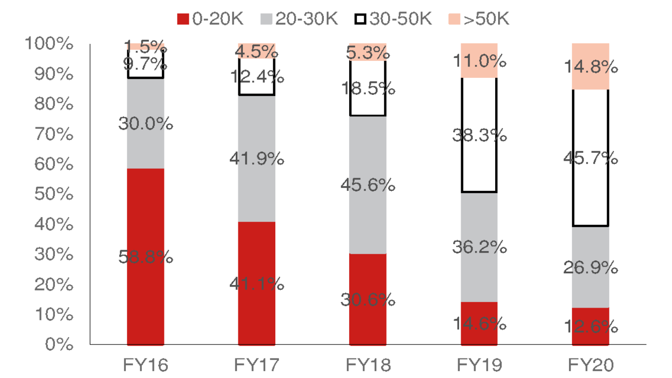
- Aided by better credit information through credit bureaus, increasing regulatory limits on ticket sizes and the improving vintage of borrowers, AUM growth has been aided by the healthy growth in ticket size as well.
- Including SHG, we estimate disbursement ticket sizes for unique borrowers to have seen a 13% CAGR over FY12-20 and evidence of the vintage benefit is also visible from a 16% CAGR in ticket size over FY17-20.
- We estimate overall ticket size per unique borrower to have increased to INR39K, with a similar ticket size for both SHG and MFI (ex-SHG).
- Within top 6-7 players, ticket size growth has been strong at an 18% CAGR over FY12-20, while it has moderated to ~13% CAGR over FY17-20, but excluding Bandhan, ticket sizes are rather similar to industry levels.
- Ticket size for NBFC-MFI players is relatively lower at <20K, but has grown at a similar pace with a 10/14% CAGR over 8 and 3 years, respectively.
- On disbursement basis, ticket size is lower for NBFC-MFI at INR30k vs INR35-40K for Banks/SFBs.
- We see an improvement in the vintage of customers to also play a significant role in increasing the ticket size, with loans disbursed of over INR20k tickets, increasing from ~40% in FY16 to +85% in FY20.
- We expect this trend to continue, especially with just 10-15% of loans disbursed at above the INR50k ticket size currently.
- Further, improving customer vintage aids asset quality which is clearly visible from a better PAR (portfolio at risk) trends for higher vintage customers.

Fig. 19: Ticket sizes have recorded 13% CAGR over FY12-20 (MFI + SHG)



Source: MFIN, Nomura research

Fig. 20: Share of >INR20K disbursement ticket size has increased to +85% in FY20 from 40% in FY16 – partly led by better vintage



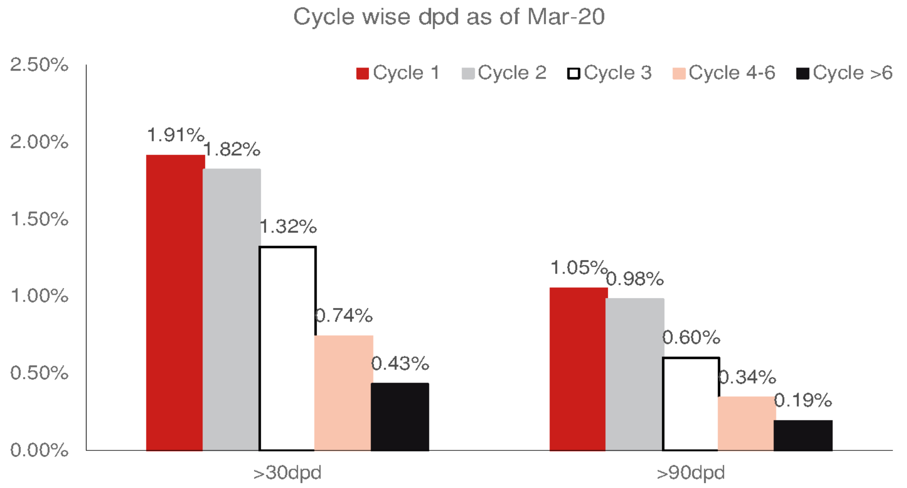
Source: Equifax, Nomura research

Fig. 21: Ticket sizes – lower for NBFC-MFIs v/s banks/SFBs

Disbursement ticket (INR 000s)	FY16	FY17	FY18	FY19	FY20	CAGR
Banks	17.1	32.5	37.1	41.1	41.4	**24.8%**
SFBs	19.0	23.5	27.9	32.0	34.6	**16.1%**
NBFCs MFIs	17.8	17.8	23.2	27.6	30.0	**13.9%**
NBFCs	19.3	24.1	26.8	31.8	38.2	**18.6%**

Source: Credit Bureau, Nomura research

Fig. 22: Better vintage customers show better repayment discipline



Source: Equifax, Nomura research

Fig. 23: Ticket sizes for top players (ex-Bandhan) similar to industry levels

GLP INRbn	FY12	FY14	FY17	FY18	FY19	FY20	CAGR FY12-20	CAGR FY17-20
Bandhan	37	61	214	277	386	462	**37.0%**	**29.3%**
BHAFIN	17	31	92	126	174	235	39.2%	37.9%
Ujjivan	7	15	54	63	84	93	38.1%	19.8%
Equitas	7	15	33	23	31	36	22.3%	3.2%
CREDAG	5	8	31	50	72	92	43.0%	44.0%
Satin	3	11	33	43	64	72	47.6%	29.2%
Spandana	27	9	13	32	44	68	12.3%	74.0%
Top 7	**104**	**150**	**470**	**613**	**854**	**1,058**	**33.7%**	**31.1%**
Top 7 (ex Bandhan)	**66**	**89**	**256**	**336**	**468**	**596**	**31.6%**	**32.6%**
Industry	**295**	**401**	**1,074**	**1,358**	**1,793**	**2,318**	**29.4%**	**29.2%**
Borrowers (mn)								
Bandhan	3.6	5.4	6.9	7.7	9.5	11.1	**15.1%**	**17.2%**
BHAFIN	4.3	5.0	7.0	7.9	9.1	12.2	14.1%	13.9%
Ujjivan	0.8	1.3	3.6	3.7	4.0	4.4	23.2%	6.8%
Equitas	1.2	1.8	2.5	1.6	2.0	2.1	7.5%	-5.7%
CREDAG	0.3	0.5	1.5	1.9	2.5	2.9	30.4%	24.6%
Satin	0.4	0.8	2.3	2.3	3.2	3.1	30.8%	10.7%
Spandana	3.4	1.2	1.1	1.6	2.5	2.6	-3.6%	32.7%
Top 7	**14.0**	**15.9**	**24.9**	**26.7**	**32.7**	**38.4**	**13.4%**	**15.6%**
Top 7 (ex Bandhan)	**10.4**	**10.5**	**18.0**	**19.0**	**23.2**	**27.3**	**12.8%**	**14.9%**
Industry	**32.1**	**39.5**	**62.0**	**76.6**	**86.5**	**105.5**	**16.0%**	**19.4%**
Average Ticket size (o/s) INR 000's								
Bandhan	10.3	11.3	30.9	35.9	40.7	41.5	**19.0%**	**10.3%**
BHAFIN	3.9	6.3	13.1	16.0	19.2	19.2	21.9%	21.1%
Ujjivan	8.6	11.6	15.2	17.0	21.0	21.4	12.1%	12.1%
Equitas	6.1	8.3	13.0	14.0	15.5	17.0	13.7%	9.4%
CREDAG	15.1	16.0	20.5	26.2	28.6	31.6	9.6%	15.5%
Satin	8.9	13.2	14.7	18.5	20.2	23.4	12.9%	16.7%
Spandana	7.9	7.7	11.8	19.8	17.8	26.6	16.5%	31.1%
Top 7	**7.4**	**9.4**	**18.9**	**22.9**	**26.1**	**27.5**	**17.9%**	**13.4%**
Top 7 (ex Bandhan)	**6.4**	**8.4**	**14.2**	**17.7**	**20.2**	**21.9**	**16.6%**	**15.4%**
Industry	**9.2**	**10.2**	**17.3**	**17.7**	**20.7**	**22.0**	**11.5%**	**8.2%**

Source: Company data, Nomura research

Opportunity still large – we expect a 16% AUM CAGR for the next decade (18% CAGR over FY20-25F)

- We still see a large opportunity in the MFI space and expect ~16% CAGR for the next decade (~18% CAGR for FY20-25F), with AUMs expected to increase from INR2.3tn to >INR5tn by FY25F (up 2x from current levels), and further to >INR10tn (4x the current levels) by FY30F.
- We expect growth to be driven by an 8% CAGR for unique borrowers (to ~90mn) by FY25F and ~125mn by FY30F (vs ~60mn unique borrowers currently), and expect ~7% CAGR for ticket sizes over FY20-30F.
- Within that, we expect NBFC-MFIs to continue to grow at a healthy pace with 20%/17% CAGR over the next 5/10 years, gaining market share from 32% currently to 38% by FY30F as SFBs shift their focus incrementally towards retail assets and liability franchise building.
- With this, we expect penetration levels to improve further to >50% by FY25F and >65% by FY30F, from 38% currently.
- We expect rural to present a strong growth opportunity with penetration levels still low at ~30% in FY20, based on our estimates, while the urban penetration opportunity remains low given the high penetration levels – already at >50% in FY20. We expect rural to continue to drive growth for the sector, with an 18% CAGR expectation over FY20-30F vs a 12% CAGR for urban.

Fig. 24: Microfinance industry level projections – we expect MFI AUM of INR5.2tn by FY25F vs INR2.3tn currently (an 18% CAGR)

												CAGR %		
Microfinance macro estimates	**FY08**	**FY11**	**FY14**	**FY17**	**FY18**	**FY19**	**FY20**	**FY25F**	**FY30F**	**FY12-20**	**FY17-20**	**FY20-25**	**FY25-30**	**FY20-30**
MFI total INRmn	**71,310**	**2,88,779**	**4,01,427**	**10,73,650**	**13,57,960**	**17,93,130**	**23,17,870**	**52,41,040**	**1,03,09,918**	**29.4%**	**29.2%**	**17.7%**	**14.5%**	**16.1%**
Total Accounts (mn)	16.9	38.0	39.5	62.0	76.6	86.5	105.5	165.5	232.1	16.0%	19.4%	9.4%	7.0%	8.2%
Ticket size - Avg O/s	4,223	7,606	10,157	17,327	17,728	20,730	21,970	31,676	44,427	11.5%	8.2%	7.6%	7.0%	7.3%
O/w Rural				5,57,170	6,82,000	10,20,000	12,99,000	33,25,081	70,56,433		32.6%	20.7%	16.2%	18.4%
O/w Urban				4,99,830	6,23,000	8,64,000	10,23,000	19,15,959	32,53,485		27.0%	13.4%	11.2%	12.3%
Mix														
Rural				52.7%	52.3%	54.1%	55.9%	63.4%	68.4%					
Urban				47.3%	47.7%	45.9%	44.1%	36.6%	31.6%					
Unique clients in mn	**13.5**	**28.8**	**28.8**	**43.7**	**45.0**	**51.8**	**59.0**	**89.0**	**124.9**	**11.9%**	**10.6%**	**8.6%**	**7.0%**	**7.8%**
Avg- Accounts per client	1.25	1.32	1.37	1.42	1.70	1.67	1.79	1.86	1.86	3.7%	8.0%	0.8%	0.0%	0.4%
SHGs:														
SHG AUM INRmn	1,69,999	3,12,212	4,29,275	6,15,813	7,55,985	8,70,982	10,80,751			**14.6%**	**20.6%**			
SHG in mn	3.6	4.8	4.2	4.8	5.0	5.1	5.7							
SHG borrowers (@10ppl per group)	36.3	47.9	42.0	48.5	50.2	50.8	56.8							
Unique borrowers assuming 50% overla	**18.1**	**23.9**	**21.0**	**24.2**	**25.1**	**25.4**	**28.4**			**3.4%**	**5.4%**			
Total MFI AUM (incl SHGs)	**2,41,309**	**6,00,991**	**8,30,703**	**16,89,463**	**21,13,945**	**26,64,112**	**33,98,621**			**22.8%**	**26.2%**			
Total MFI unique borrowers (incl SHG)	**31.6**	**52.7**	**49.8**	**67.9**	**70.1**	**77.2**	**87.4**			**8.4%**	**8.8%**			
MFI growth drivers														
Total AUM (incl SHGs)		**9.5%**	**18.4%**	**19.1%**	**25.1%**	**26.0%**	**27.6%**							
MFI AUM		**7.6%**	**30.4%**	**26.7%**	**26.5%**	**32.0%**	**29.3%**	**18.8%**	**14.5%**					
-o/w Ticket size		***-9.4%***	***8.7%***	***6.7%***	***2.3%***	***16.9%***	***6.0%***	***8.0%***	***7.0%***					
- o/w No. of accounts		***18.7%***	***20.0%***	***18.8%***	***23.6%***	***12.9%***	***22.0%***	***10.0%***	***7.0%***					
-- w/w Unique client driven			*18.2%*	*17.2%*	*3.0%*	*15.1%*	*14.0%*	*10.00%*	*7.00%*					
-- w/w Multiple lending driven					*20.0%*	*-1.9%*	*7.0%*	*0.0%*	*0.0%*					
Market Share:														
SHGs	70.4%	51.9%	51.7%	36.5%	35.8%	32.7%	31.8%							
MFIs	29.6%	48.1%	48.3%	63.5%	64.2%	67.3%	68.2%							
NBFC MFIs INRMn:	**59,540**	**2,41,115**	**3,35,170**	**3,03,490**	**4,85,220**	**6,70,090**	**7,37,920**	**18,23,882**	**39,48,699**	**14.7%**	**34.5%**	**19.8%**	**16.7%**	**18.3%**
Market share	83.5%	83.5%	83.5%	28.3%	35.7%	37.4%	31.8%	34.8%	38.3%					
Total Accounts (mn)	14.1	31.7	33.0	23.3	33.0	38.7	38.4							
Ticket size - Avg O/s	4,223	7,606	10,157	13,025	14,704	17,315	19,217							

Source: Credit Bureaus, Nomura estimates

Our approach on penetration

- On our estimate of 280mn households in India, assuming five individuals per household on average, MFIs have already reached 60mn households, taking the penetration level to 38% (of addressable households).
- Of the 280mn households, we assume ~22% of the households to be below poverty line and hence not addressable. Further, we expect urban addressable households to be 65% and rural at around 75%, leading to an addressable market of 180mn households that MFIs can tap by FY30F.
- Within that, we see a large opportunity for the rural segment, where the penetration levels are lower, at ~30%, and expect this segment to record an 18% CAGR, with the penetration level improving to 70% over the next 10 years; on the other hand, we

expect urban segment to record a relatively slower CAGR of 12%, with the penetration level improving from >50% currently to 65%.

- Further, assuming ~7% CAGR for ticket sizes – aided by both nominal inflation/growth and improving customer vintage, as well as 7-8% growth in unique borrowers, we forecast industry AUMs to record 18%/16% CAGR over the next 5/10 years. This, on our calculation, should improve penetration to >50%/65% by FY25/30F vs. 38% currently.

Fig. 25: We forecast the penetration level to improve to 53% by FY25F vs. 38% currently

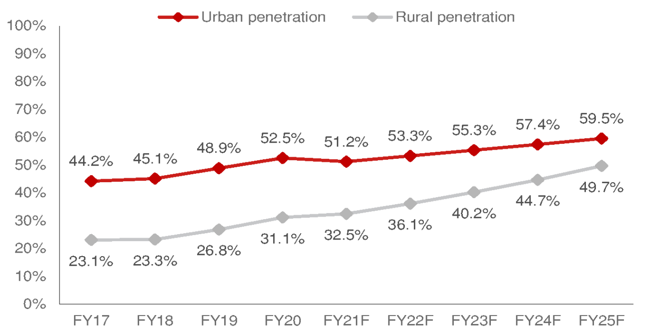
MFI Penetration - India	FY08	FY11	FY14	FY17	FY18	FY19	FY20	FY25F	FY30F	FY12-20	FY17-20	FY20-25	FY25-30	FY20-30
Population (bn)	**1,133**	**1,191**	**1,250**	**1,311**	**1,332**	**1,371**	**1,393**	**1,508**	**1,633**	**1.8%**	**2.1%**	**1.6%**	**1.6%**	**1.6%**
Urban	338	367	392	416	425	433	442	488	538	2.0%	2.0%	2.0%	2.0%	2.0%
Rural	796	824	858	895	907	938	952	1,021	1,095	1.7%	2.1%	1.4%	1.4%	1.4%
Households	**227**	**238**	**250**	**262**	**266**	**274**	**279**	**302**	**327**					
- Urban	68	73	78	83	85	87	88	98	108					
- Rural	159	165	172	179	181	188	190	204	219					
Households (excl below poverty line)	**177**	**186**	**195**	**205**	**208**	**214**	**218**	**236**	**256**					
- Urban	58	63	68	72	73	75	76	84	93					
- Rural	118	122	127	133	135	139	141	152	163					
Adressable Households	**127**	**133**	**140**	**146**	**149**	**153**	**156**	**168**	**182**					
- Urban	38	41	44	47	48	49	50	55	60					
- Rural	89	92	96	100	101	105	106	114	122					
Market Penetration (unique clients):														
India (on all HH)	**6.0%**	**12.1%**	**11.5%**	**16.7%**	**16.9%**	**18.9%**	**21.2%**	**29.5%**	**38.2%**					
India (on adressable market)	**10.7%**	**21.6%**	**20.7%**	**29.8%**	**30.3%**	**33.8%**	**37.9%**	**52.8%**	**68.5%**					
- Urban				44.2%	45.1%	48.9%	52.5%	59.5%	65.2%					
- Rural				23.1%	23.3%	26.8%	31.1%	49.7%	70.1%					

Source: Credit Bureaus, Nomura estimates

Rural segment presents large opportunity – rural MFIs better positioned

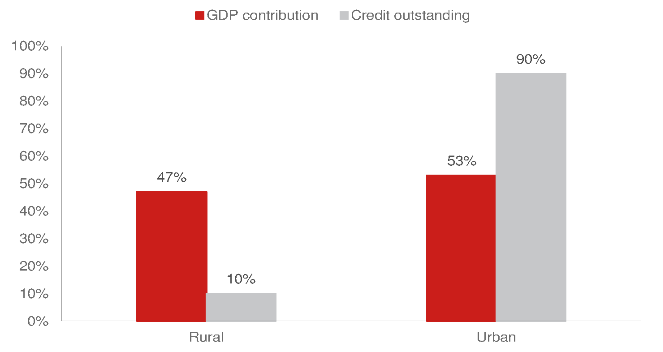
- In our view, higher penetration in urban is a result of lower opex intensity due to high population density, as well as SFBs/banks' attempt to focus on the right mix of asset and liability accretion from their target geographies.
- However, we see a larger growth opportunity for the rural segment given the lower penetration, at ~30%, on our estimate, and expect the rural segment to grow at a much faster pace over the next decade (an 18% CAGR) vs the urban segment, with the penetration level improving from 30% to 65% over FY20-30F.
- This trend is also evidenced from a 38% 3-year CAGR for the rural segment vs the urban segment growing slower, at a 24% CAGR over the same period. Hence, we think rural MFIs are much better positioned to capture this opportunity, and deliver on a faster and a more sustainable growth.
- Within rural players, Bandhan is present in highly-penetrated geographies like Assam, Odisha and West Bengal, and enjoys a dominant market share. Further, given its already elevated ticket size, we expect Bandhan to grow at a slower pace; even as it diversifies into home loans (GRUH portfolio), the growth contribution from microfinance will likely remain relatively low. We expect Bandhan to grow its MFI portfolio (excluding individual loans) at a 16% CAGR over FY20-23F.
- SFBs we cover are more urban-focused, like Equitas and Ujjivan, where we think penetration levels are relatively higher, and hence, we expect 16-17% CAGR for the MFI portfolio over FY20-23F. For these SFBs, we believe the incremental growth will likely come from relatively new segments – we estimate overall AUM CAGR of 18-20% over FY20-23F.
- We forecast AUM growth for CREDAG at 19% CAGR over FY20-23F, and expect it to be the key beneficiary of the rural opportunity.

Fig. 26: Lower rural penetration levels present an opportunity for MFIs



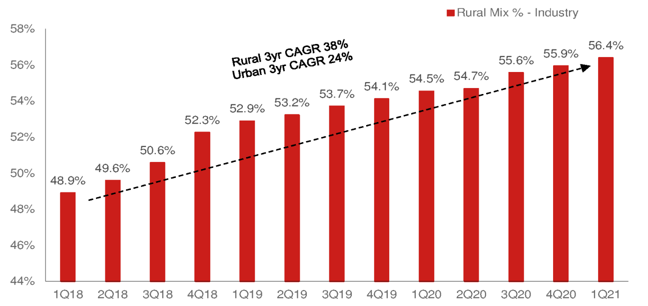
Source: CRIF Highmark, Nomura research

Fig. 27: While rural economy contributes 47% of the country's GDP, credit off-take is just 10% of the system



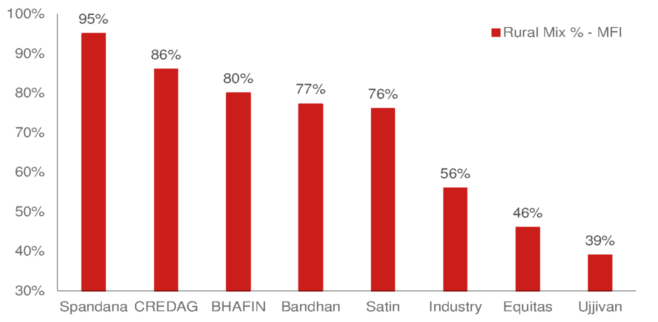
Source: Company data, Nomura research

Fig. 28: Rural MFI has recorded a 38% CAGR over the past 3 years, compared to 24% for urban



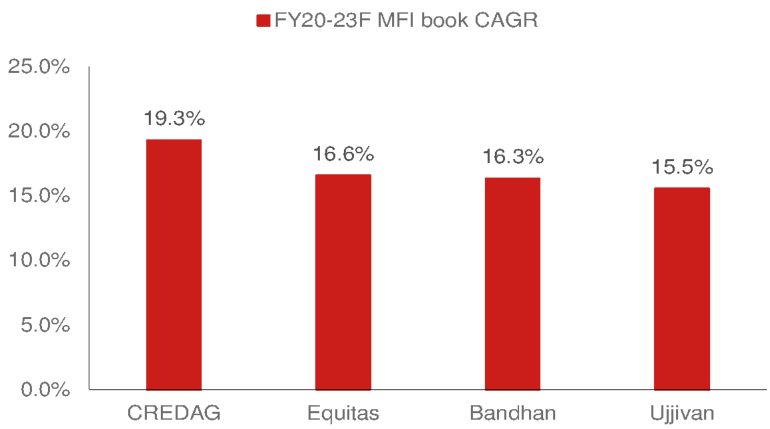
Source: CRIF Highmark, Nomura research

Fig. 29: More rural-focused MFIs like CREDAG, Spandana, BHAFIN to benefit from the opportunity in rural



Source: Company data, Nomura research

Fig. 30: Our growth expectations for top MFI players



Source: Company data, Nomura estimates

Individual loans – a large cross-sell opportunity

- With >65% of customers still in their first/ second MFI loan cycles (50% in first cycle), we see large vintage-related opportunity over the next decade, providing further tailwind to growth.
- As the sector matures and the borrower vintage improves, we see a huge opportunity for cross-selling of retail/individual loans, where MFI borrowers shall over time graduate to individual/retail loan categories.
- This will not only aid growth led by ticket sizes (4-5x of the current MFI loan ticket size), but also benefit through an increase in duration (vs 1-2 year duration of MFI loans), thereby aiding a strong growth opportunity.

- We have seen improving PAR (portfolio at risk) trends with increasing customer vintage (fig *34*), which should allow MFIs to graduate higher vintage customers to retail/individual loans over time.
- Assuming 10% of the five-year lagged borrower base potentially graduating to individual loans over the next decade, with ticket sizes at 4-5x of the MFI ticket size, we expect another INR1.5/3tn of opportunity for the system over the next 5/10 years. Further, given the higher duration of these individual loans (>3 years), we expect the AUM growth delta to be even larger.
- Most players have already started taking initial steps in that direction, with top MFIs having 2-13% of micro loans as individual loans (NBFC-MFI retail mix capped at 15% currently by the regulator).

Fig. 31: We estimate the retail lending opportunity at INR1.5-3tn by FY25/30F

Retail lending opportunity	FY20	FY25F	FY30F
Unique borrowers - 5 yr lagged	31.7	59.0	89.0
10% graduating to retail lending	3.2	5.9	8.9
Ticket size @ 4x of MFI ticket size INR		2,53,404	3,55,412
Opportunity size INRbn - Retail		**1,496**	**3,164**
% of MFI AUMs		**28.5%**	**30.7%**
MFI	**2,318**	**5,241**	**10,310**
MFI + retail lending INRbn		**6,737**	**13,474**

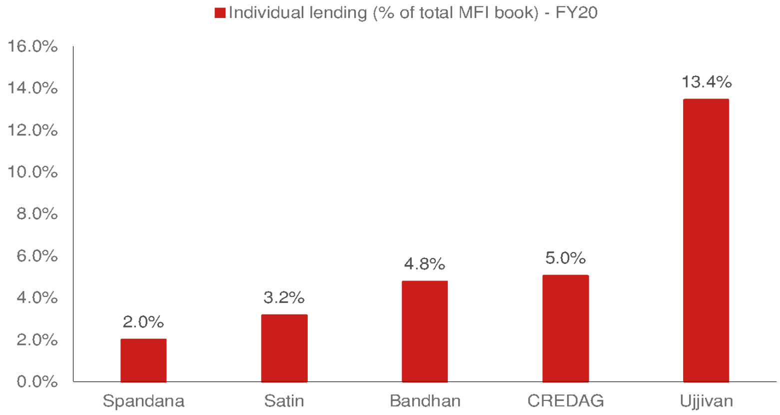
Source: Nomura estimates

Fig. 32: Higher vintage customers for top players portray a better opportunity to upgrade to retail loans

Customer mix by cycle	Bandhan	BHAFIN	Satin	Spandana	CREDAG	Industry
Cycle 1	22%	38%	44%	22%	26%	54%
Cycle 2 / 3	24%	34%	NA	39%	42%	35%
>= Cycle 4	54%	29%	NA	39%	33%	11%

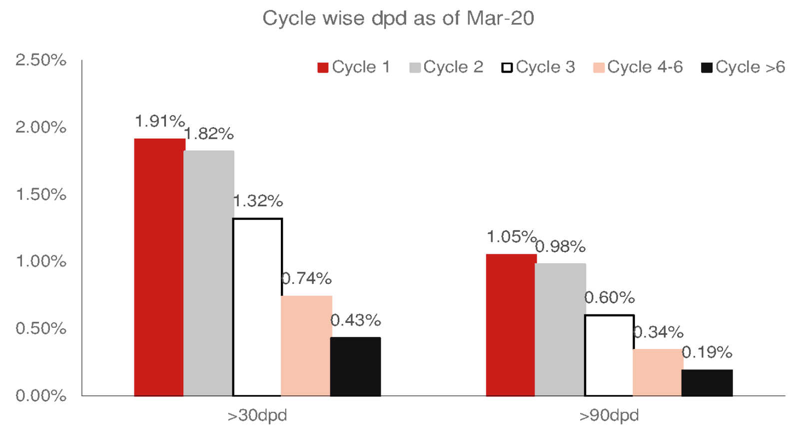
Note: For CREDAG, we have used borrower vintage by years – <1 year: Cycle 1, 1-3 years: Cycle 2/3, >3years: 4 or more cycles
Source: Company data, Nomura research

Fig. 33: Most MFIs currently have just 2-5% of MFI book towards individual lending



Source: Company data, Nomura research

Fig. 34: Better vintage customers are generally more disciplined, providing good opportunity to graduate to individual retail loans



Source: Equifax, Nomura research

Opportunity in every disruption; COVID-19 should further aid consolidation

- Every disruption historically has created market share opportunities, with large market-share shifts towards less-impacted players. Top 7 players account for ~48% of the total industry AUM, recording a 35% CAGR over FY12-20 compared to the industry CAGR of ~30%, with ~400bps market share gains post-demonetization. Further, top-3 NBFC-MFIs have recorded a 47% CAGR, with market share gains of ~400bps for FY17-20, driven by: (1) better access to funding; (2) lesser competition from peers turned SFBs; and (3) relatively lower impact from demonetization.
- Disruptions in the recent past have been rather brutal with large market share losses seen for the impacted MFIs, especially for those with high geographic concentrations. For example, BHAFIN, Spandana and Share commanded total market share of >25% in FY11/12; due to the impact from the TN crisis, their combined market share had reduced to 10% as of end-FY15. Jana and Equitas were amongst the most impacted players during demonetization, having lost market share from 17% in FY16 to <5% in FY19.
- That said, MFI players have recognized the need and have been diversifying their geographic mix, with top-3 states currently accounting for 40-85% for the top players, down from 40-95% three-four years back (fig. *35*).
- We think the COVID-19 pandemic should further trigger consolidation to the benefit of larger and relatively less-impacted MFIs.

Fig. 35: Past disruptions have been rather brutal for highly concentrated players; other top players saw significant market-share gains

Top Player market share - Disruptions impact	AP crisis impact					Demonetisation impact				
	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Bandhan	8.7%	12.6%	14.4%	15.2%	16.3%	18.2%	19.9%	20.4%	21.5%	19.9%
Equitas	2.7%	2.5%	3.7%	3.7%	3.7%	3.9%	3.1%	1.7%	1.7%	1.6%
Ujjivan	2.2%	2.4%	3.5%	3.8%	5.0%	5.5%	5.0%	4.7%	5.2%	4.6%
SKS/ BHAFIN	14.2%	5.7%	7.7%	7.8%	7.1%	9.1%	8.5%	9.3%	9.7%	10.5%
CREDAG	0.9%	1.4%	1.9%	2.0%	2.5%	3.0%	2.9%	3.7%	4.0%	4.3%
Spandana	12.0%	9.2%	3.8%	2.2%	2.0%	1.4%	1.2%	2.3%	2.4%	2.9%
Madura		0.5%	0.5%	0.6%	0.6%	0.6%	0.8%	0.9%	1.1%	0.9%
Satin		1.1%	1.9%	2.6%	3.7%	3.9%	3.4%	3.2%	3.6%	3.1%
ESAF		1.0%	1.4%	1.5%	1.7%	2.3%	2.5%	2.5%	2.7%	2.7%
Fincare (Disha + Future)		0.8%	0.8%	0.9%	1.1%	1.1%	1.1%	1.3%	1.6%	1.8%
Jana	0.6%	1.2%	3.1%	5.1%	6.4%	13.0%	11.9%	4.3%	3.1%	3.0%
North East				0.3%	0.4%	0.6%	0.6%	0.8%	0.8%	0.6%
Suryoday		0.3%	0.5%	0.8%	1.0%	1.2%	0.8%	1.1%	1.2%	1.2%
Utkarsh		0.3%	0.6%	0.8%	1.2%	1.7%	1.5%	2.0%	2.3%	2.6%
Share		7.1%	3.1%	2.1%	1.1%					
Top 7		**34.8%**	**36.7%**	**37.3%**	**40.2%**	**45.0%**	**44.0%**	**45.1%**	**48.1%**	**46.9%**
All SFBs		**8.3%**	**13.6%**	**16.9%**	**20.6%**	**29.3%**	**26.6%**	**18.4%**	**18.6%**	**18.1%**
Top 3 NBFC-MFIs (incl BHAFIN)		**8.1%**	**11.4%**	**12.4%**	**13.3%**	**15.9%**	**14.8%**	**16.1%**	**17.2%**	**17.8%**

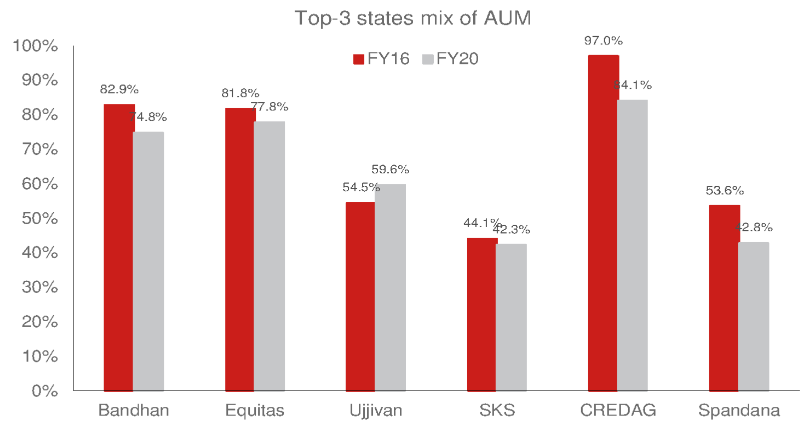
Source: MFIN, Nomura research

Fig. 36: State-wise market-share trends for top players

State wise Market Share %					
Maharashtra	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**
Bandhan	4.8%	5.3%	6.0%	6.6%	6.0%
Equitas	5.4%	4.2%	2.5%	2.6%	2.6%
Ujjivan	8.6%	7.0%	7.1%	6.5%	7.2%
BHAFIN	11.6%	10.0%	11.1%	11.3%	12.4%
CREDAG	**9.4%**	**8.5%**	**11.9%**	**12.9%**	**15.9%**
Spandana	2.1%	1.7%	3.8%	3.3%	4.8%
Top players	**41.9%**	**36.8%**	**42.4%**	**43.3%**	**48.9%**
Tamil Nadu					
Bandhan	0.8%	0.8%	1.0%	1.0%	1.1%
Ujjivan	6.3%	5.5%	5.6%	6.9%	6.8%
CREDAG	**0.8%**	**1.1%**	**1.7%**	**2.7%**	**7.2%**
Top players	**24.4%**	**19.1%**	**14.5%**	**16.9%**	**21.0%**
Karnataka					
Bandhan	1.9%	2.1%	2.0%	2.0%	2.3%
Equitas	2.8%	2.3%	1.3%	1.9%	1.9%
Ujjivan	11.6%	9.3%	8.2%	8.7%	11.1%
BHAFIN	13.5%	10.7%	10.9%	12.0%	14.0%
CREDAG	**19.8%**	**17.5%**	**22.2%**	**22.9%**	**24.6%**
Spandana	2.9%	2.2%	5.5%	3.6%	4.4%
Top players	**52.6%**	**44.1%**	**50.1%**	**51.1%**	**58.4%**
West Bengal					
Bandhan	80.2%	77.7%	74.2%	67.9%	64.7%
Ujjjivan	8.4%	6.4%	5.4%	5.7%	6.2%
BHAFIN	7.3%	7.9%	8.2%	8.1%	9.6%
Top players	**95.9%**	**92.1%**	**87.8%**	**81.7%**	**80.5%**
Bihar					
Bandhan	30.0%	27.9%	26.0%	22.6%	24.1%
Ujjjivan	5.0%	3.7%	3.3%	3.7%	3.4%
BHAFIN	16.1%	17.2%	15.7%	14.1%	13.8%
Top players	**51.1%**	**48.8%**	**45.0%**	**40.4%**	**41.3%**
Uttar Pradesh					
Bandhan	8.3%	10.2%	10.8%	14.1%	15.1%
Ujjjivan	4.1%	3.2%	2.6%	2.4%	3.4%
BHAFIN	10.1%	7.6%	9.8%	13.1%	14.4%
Top players	**22.5%**	**21.0%**	**23.2%**	**29.6%**	**32.8%**
Odisha					
Bandhan	9.3%	8.8%	10.1%	13.5%	13.3%
Ujjjivan	3.4%	2.7%	2.5%	3.4%	2.6%
BHAFIN	30.1%	25.1%	24.3%	23.1%	25.5%
Spandana	5.4%	4.4%	7.0%	7.9%	8.5%
Top players	**48.3%**	**40.9%**	**43.9%**	**48.0%**	**49.9%**
Assam					
Bandhan	80.3%	76.3%	66.4%	55.6%	60.4%
Ujjivan	5.3%	4.6%	4.1%	4.1%	3.4%
Top players	**85.6%**	**80.9%**	**70.4%**	**59.6%**	**63.7%**
Rest of India					
Bandhan	3.9%	5.0%	6.1%	10.5%	9.1%
Equitas	2.4%	2.5%	1.5%	1.6%	1.3%
Ujjivan	2.1%	3.2%	3.2%	4.2%	1.4%
SKS	7.8%	8.1%	10.2%	12.3%	11.0%
CREDAG	0.3%	0.7%	1.2%	2.0%	-0.3%
Spandana	2.2%	2.2%	4.2%	6.2%	6.4%
Top players	**18.7%**	**21.7%**	**26.5%**	**36.8%**	**28.9%**

Source: Company data, Nomura estimates

Fig. 37: Top players have recognized the need to diversify geographically, and have reduced exposure to respective top-3 states

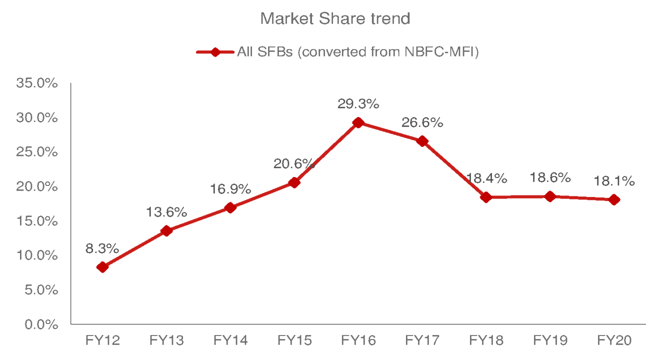


Source: Company data, Nomura research

SFBs diversifying away from MFIs - opportunity for NBFC-MFIs to gain market share

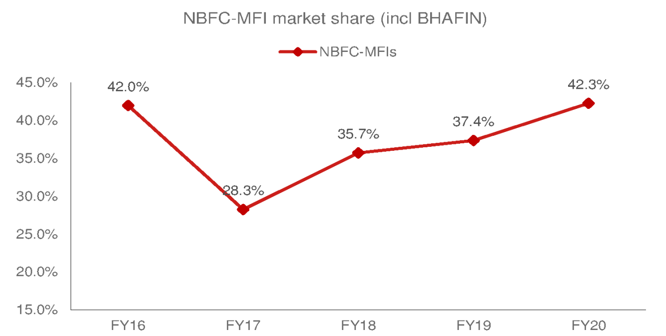
- Over the past five years, the MFI space has seen 9-10 larger players either converting into SFBs or banks, with Bandhan having converted into a bank in FY16 (BHAFIN acquired by IndusInd Bank in early-FY20) and 7-8 MFIs having converted into SFBs over FY15-16. These players accounted for 46% of the total market share with AUMs of INR1.1tn as of end-FY20, and grew at a faster pace over FY12-17 relative to the industry, with a combined AUM CAGR of 48%.
- Incrementally, as these players were converted into banks, they have been focusing on diversifying their asset base; demonetization impact along with branch banking-related drags severely impacted momentum for them. Bandhan, too, is largely present in highly-penetrated states like West Bengal and Assam, and already disburses higher ticket size loans vs the industry (better vintage customers), with currently lesser penetration opportunity, in our view.
- These MFI players (converted to banks) have recorded market share losses since FY17, with total SFB market share falling from 29% in FY16 to ~18% in FY20; we note that Bandhan has also not seen any market share gains during this period. This has led to market share gains for NBFC-MFIs from 28% in FY17 to 42% in FY20 (including BHAFIN). We expect this trend to continue as MFIs turned into banks, focusing on building a liability franchise and diversify their asset base.
- Looking at state-wise market share trends, we note a similar pattern with MFI-turned-banks losing market shares or at least the top NBFC-MFIs gaining market share at a faster pace in most key states, including Maharashtra, UP, Karnataka, Odisha and B-10 states.
- We expect NBFC-MFIs to gain >50bps market share annually over the next decade, and account for ~38% of the total industry AUM by FY30F vs ~32% currently. That said, we acknowledge that larger NBFC-MFIs will eventually have to convert into banks as they grow larger in size.

Fig. 38: SFBs have lost quite some market share as they shift focus towards retail lending and deposit accretion



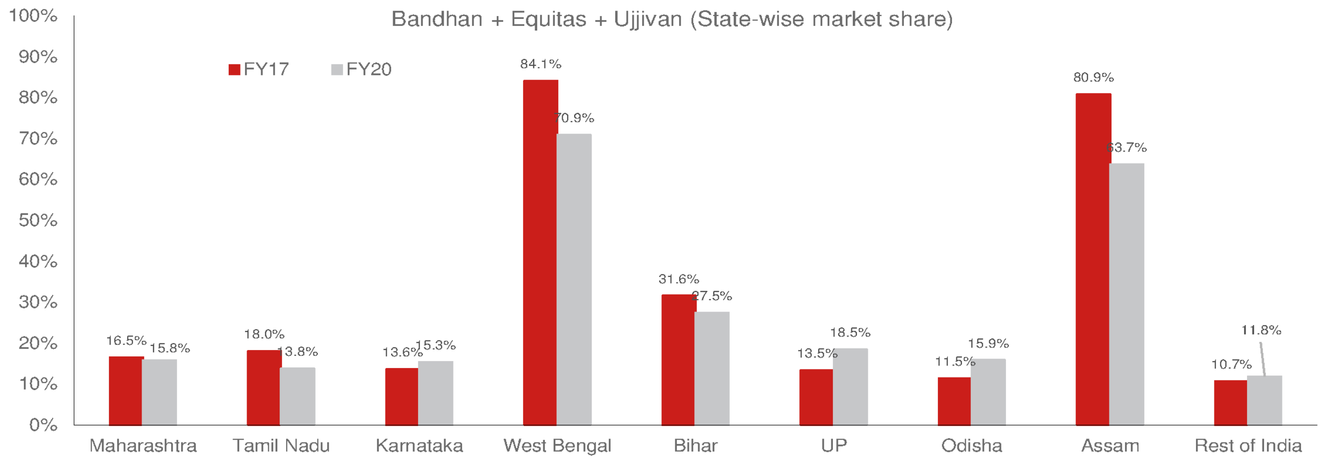
Source: MFIN, Nomura research

Fig. 39: NBFC-MFI market share has improved with large players shifting focus as they became SFBs



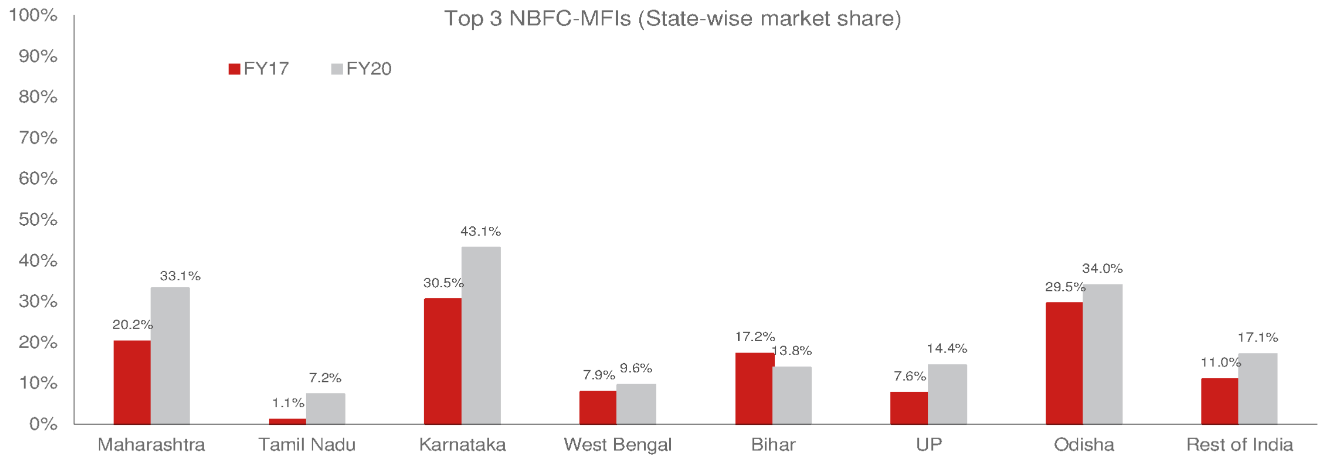
Source: MFIN, Nomura research

Fig. 40: Banks and SFBs (converted from NBFC-MFIs) have lost market share across states as well



Source: Company data, Nomura estimates

Fig. 41: NBFC-MFIs have capitalized by gaining market share over the same period across most states

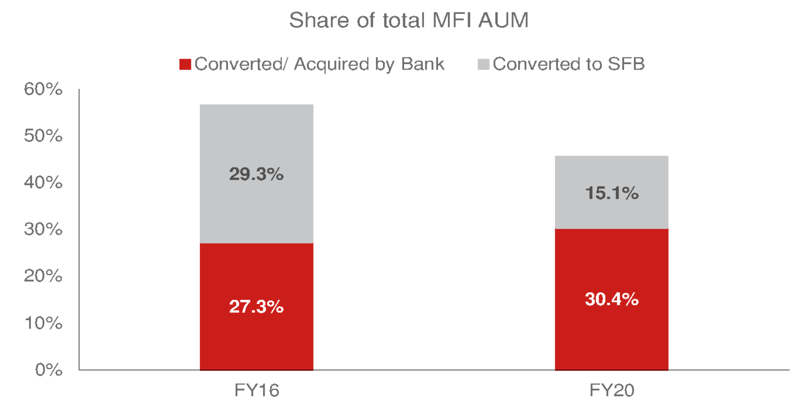


Note: *Tamil Nadu data for FY20 also includes the impact of Madura's merger with CAGL (5% market share)*
Source: Company data, Nomura estimates

Funding constraints getting resolved now

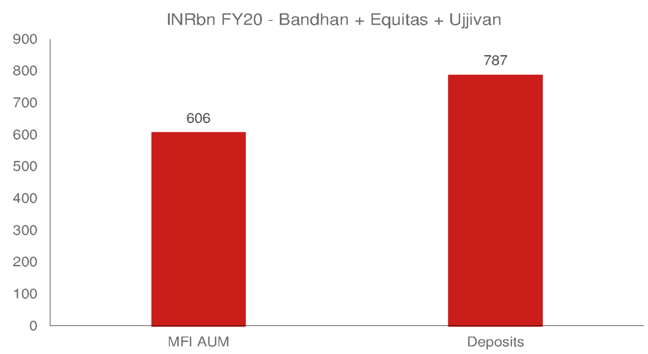
- With 40-45% of the industry converting into banks/SFBs over the past 4-5 years, we see a fair amount of funding stability coming into the sector. These MFIs turned into banks/SFBs account for INR1.1tn of the total AUM (INR810bn excluding BHAFIN) as of end-FY20, against which they have built up a deposit base of INR1.1tn (excluding BHAFIN).
- More importantly, incremental growth has largely been funded by deposits, with INR204bn of deposit accretion for Equitas + Ujjivan, vs. INR160bn of AUM accretion over FY17-20 and INR57bn of AUM accretion in the MFI segment.
- We see this as a clear game-changer for the industry given funding shocks will likely get meaningfully minimized in the sector; moreover, as liabilities build up for SFBs, capital availability should meaningfully ease out for NBFC-MFIs.
- That said, we believe that NBFC-MFIs will eventually have to convert into banks/SFBs as they gain size and scale.

Fig. 42: Most of the top players (~45% of the market share) have converted into banks/SFBs – leading to more funding stability for the sector



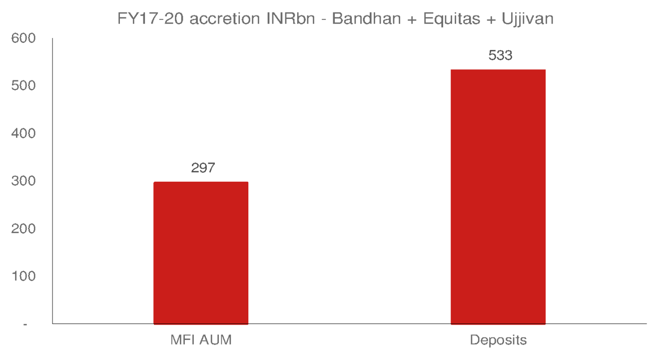
Source: Company data, Nomura research

Fig. 43: Deposits vs MFI AUM for top large banks/SFBs (converted from NBFC-MFIs)



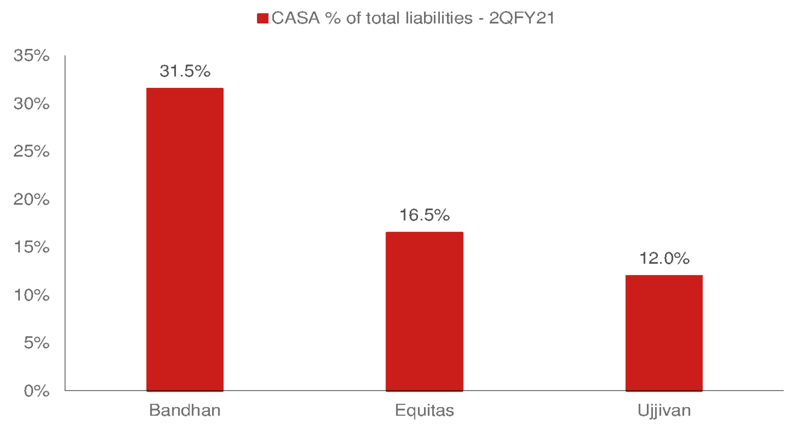
Source: Company data, Nomura research

Fig. 44: Deposit accretion has been quite strong and has aided loan book growth



Source: Company data, Nomura research

Fig. 45: CASA build-up for SFBs still nascent; Bandhan has seen strong momentum

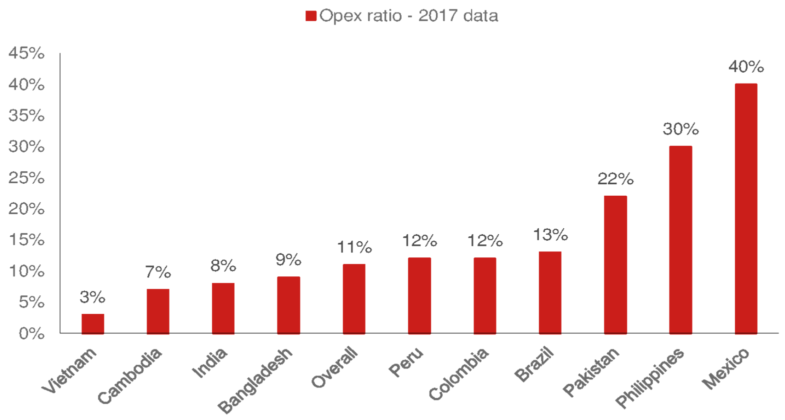


Source: Company data, Nomura research

Opex efficiency – Indian MFIs best-placed globally

- Indian MFIs have meaningfully improved their operational efficiency over the past decade, and remain one of the most efficient class of MFIs globally. Based on 2017 data, opex/AUM for Indian MFIs stands at 8% and is amongst the best-in-class compared to peers and an Industry average of 11%.

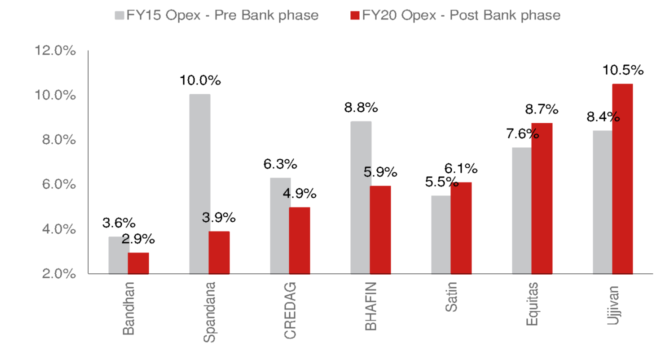
Fig. 46: India is among the best-placed countries in terms of MFI opex efficiency



Source: Global Benchmark Report, Nomura research

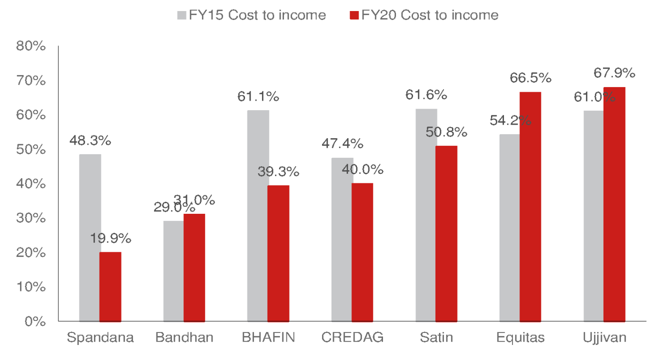
- Opex/AUMs have improved further since FY15 to 4-6% for most top players, barring MFIs turned into SFBs, which have been dragged by branch banking-related costs. That said, even SFBs' branch-banking drag is largely behind us now and opex ratios should continue to improve from here on, in our view.
- We look at BHAFIN to benchmark for cost efficiency delivered over time and note that its opex/AUM improved from ~8-9% in FY14/15 (partly lower growth impact post the Andhra crisis) to ~6% in FY19. Spandana's opex intensity has also reduced as it got back to growth after exiting corporate debt restructuring (CDR) in FY17 – currently ~4% compared to 10% in FY15 (AP crisis impact on growth). Moreover, as the share of individual lending picks up and the book duration increases over time, we expect cost ratios to improve further for the sector.
- Within the top players, Bandhan remains the most efficient player with opex/AUMs of just 3.8-3.9% as of FY18-19; further opex improvement to <3% is not directly comparable due to the Gruh merger while SFBs' opex ratios remain high at 6.5-8.5% for Equitas and Ujjivan due to branch-banking drags and investments in new asset verticals. For NBFC-MFIs like CREDAG, Spandana, BHAFIN and Satin – opex/AUM has improved to 4-6% for FY20, from 6-10% in FY15.
- Cost-to-income ratios for NBFC-MFIs have improved to 30-40% levels for FY20, compared to 50-60% levels seen in FY15, aided by a pickup in growth. With a cost-to-income ratio of 30%, Bandhan continues to be among the best in league, while the cost-income ratio remains elevated for SFBs at 65-70%.
- Improving cost efficiency has been noted despite the 6-30% CAGR for branch networks and 20-35% CAGR for the employee base over the past five years for the top players, aided by strong growth at 30-45% for all players.

Fig. 47: Opex/AUM for top players – FY15 (pre-bank) vs. FY20 (post-bank for some players)



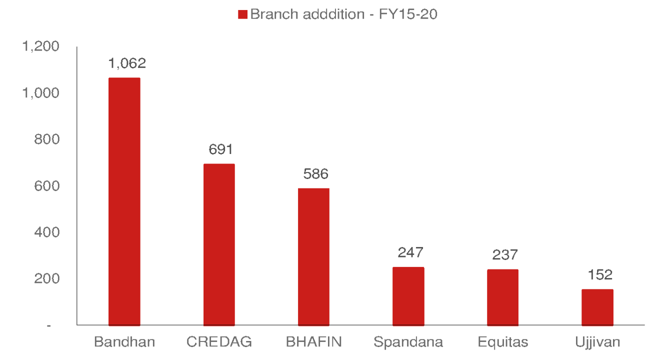
Note: BHAFIN data for FY19
Source: Company data, Nomura research

Fig. 48: Cost-to-income for top players – FY15 (pre-bank) vs. FY20 (post-bank for some players)



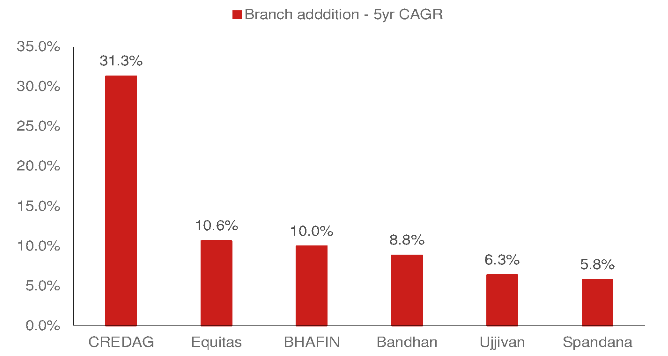
Note: BHAFIN data for FY19
Source: Company data, Nomura research

Fig. 49: Absolute branch additions over FY15-20



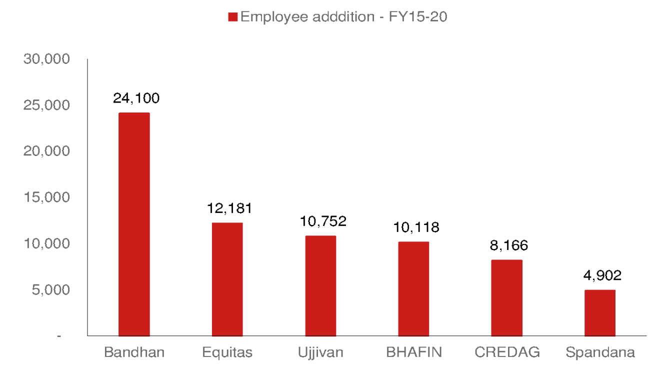
Note: DSCs for Bandhan
Source: Company data, Nomura research

Fig. 50: Branch addition CAGR over FY15-20 – CREDAG has expanded aggressively



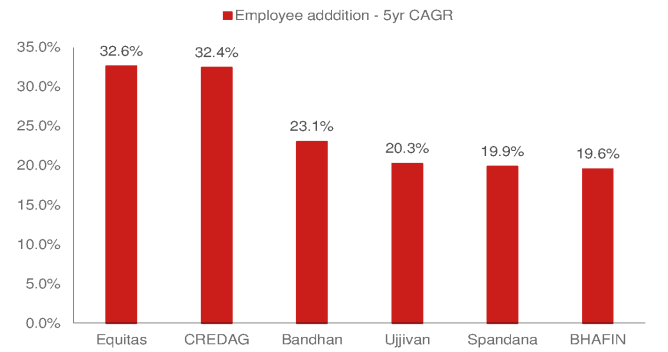
Note: DSCs for Bandhan
Source: Company data, Nomura research

Fig. 51: Employee additions have been high for banks/SFBs due to banking operations



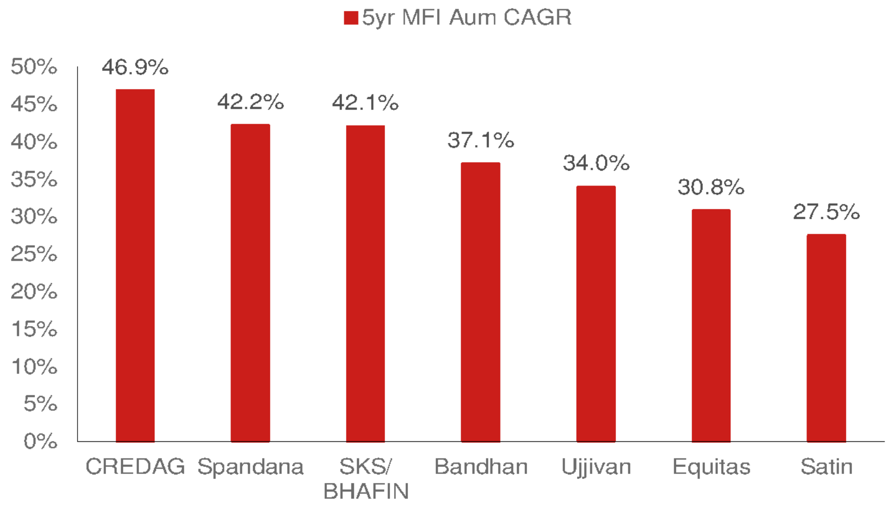
Source: Company data, Nomura research

Fig. 52: 5-year (FY15-20) employee addition CAGR



Source: Company data, Nomura research

Fig. 53: Strong growth across players has supported cost ratios

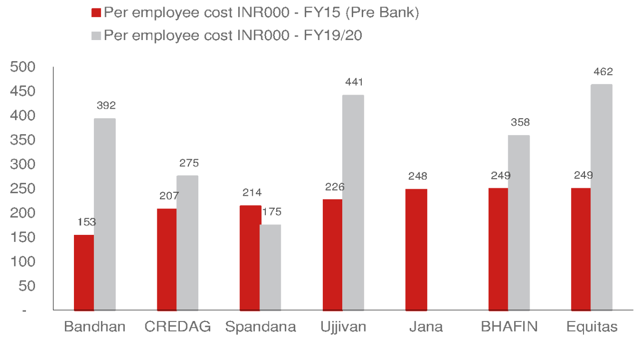


Note: 1) CREDAG is excluding Madura acquisition; 2) BHAFIN – estimated FY20 data; 3) Equitas, Ujjivan based on total AUM growth – for cost comparison purpose
Source: Company data, Nomura research

Employee costs have remained stable for NBFC-MFIs

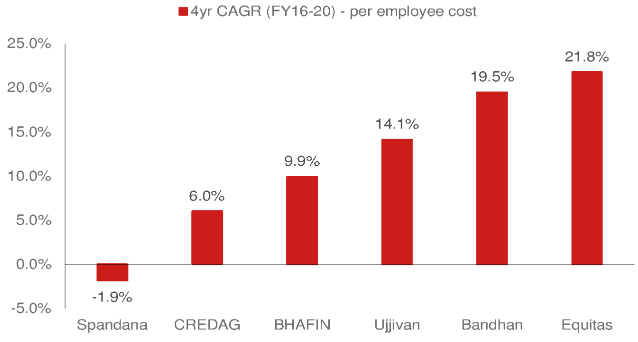
- **CREDAG and Spandana are best-placed on the employee cost metric** with per employee cost <INR0.2mn, and recorded lower per employee cost even in the pre-bank phase and were second only to Bandhan. More importantly, CREDAG and Spandana have been able to maintain employee costs at the same level for the past four years. Higher rural mix at 80-95% for Bandhan, CREDAG and Spandana does help in maintaining a lower employee cost, compared to their more urban-focused peers like Ujjivan and Equitas (40-45% rural mix). Post-bank phase, employee costs for Bandhan, Equitas and Ujjivan are not comparable with NBFC-MFIs due to branch banking and retail lending-related hiring, which have led to a significant spike in their per employee costs.
- **For CREDAG**, lower employee expense is also a function of overall better employee experience in terms of basic needs like food and shelter, better attrition rate at 20-25% compared to 35% for the industry, and its strategy to only hire freshers from nearby villages and no lateral hiring.
- **Employee productivity**: In terms of gross loan portfolio (GLP)/loan officer, CREDAG has an average GLP/loan officer of INR12.8mn and is amongst the best in the Industry, likely driven by higher AUM outstanding per customer. This is despite lower customers per loan officer for CREDAG due to a weekly meeting model followed by CREDAG, limiting the bandwidth per loan officer. GLP per customer and retention remain superior for CREDAG, and thus fills up the opex drag created by weekly collections, in our view. Better GLP outstanding per customer due to multiple loan products within the eligible limits, customer-friendly practices, and more customized offerings based on individual needs lead to better GLP/employee.

Fig. 54: Per employee cost – NBFC-MFIs are best placed



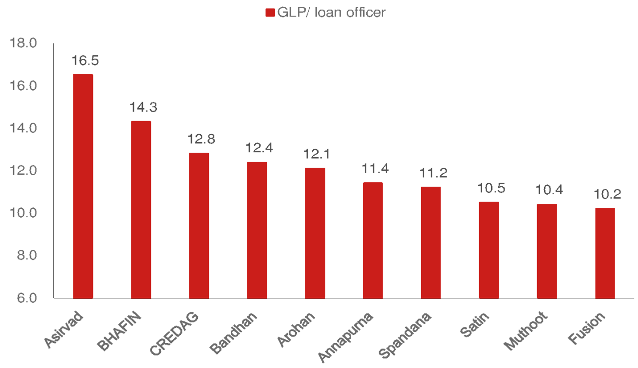
Note: BHAFIN data as of FY19
Source: Company data, Nomura research

Fig. 55: Per employee costs for NBFC-MFIs have remained steady; banks/SFBs are impacted by branch banking drags



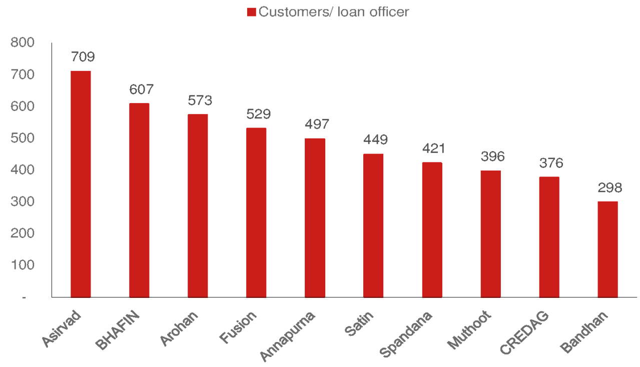
Note: BHAFIN data as of FY19
Source: Company data, Nomura research

Fig. 56: Better ticket size for CREDAG aids better GLP/loan officer despite its weekly model



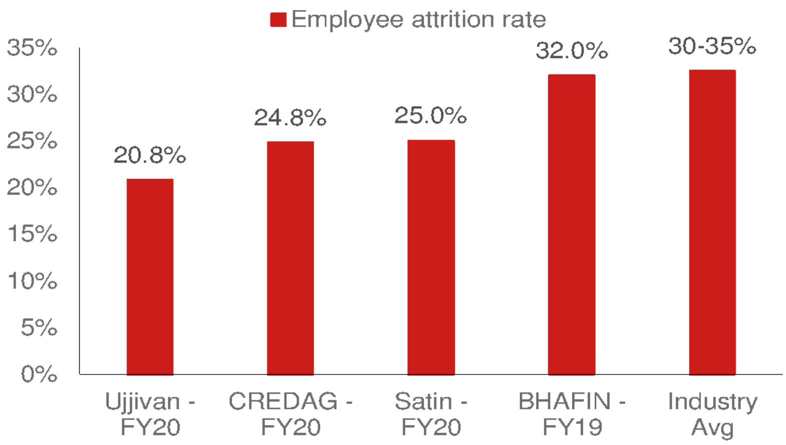
Note: 1) Total employees (branch + asset) used for Bandhan and thus not directly comparable; 2) BHAFIN data for FY19
Source: MFIN, Nomura research

Fig. 57: Weekly model leads to lower customers/loan officer for CREDAG



Note: 1) Total employees (branch + asset) used for Bandhan and thus not directly comparable; 2) BHAFIN data for FY19
Source: MFIN, Nomura research

Fig. 58: Better employee retention for CREDAG also improves cost efficiency



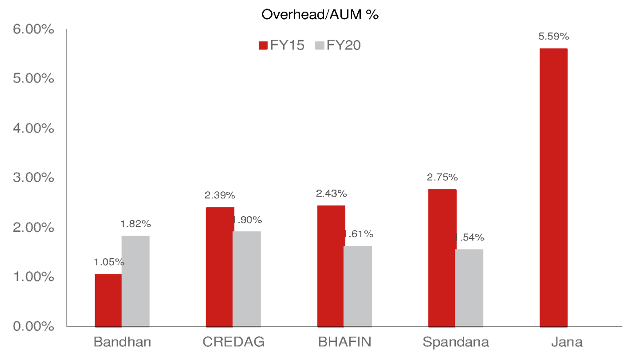
Source: Company data, Nomura research

Overheads – SFBs dragged

- **Monthly vs. weekly model**: In theory, monthly collection model is more cost efficient, while most large players like Bandhan, BHAFIN, CREDAG and Spandana follow a weekly collection model given the high touch nature of the segment leading to a better asset quality experience. A monthly collection model can aid better scalability as more customers can be handled per loan offer, and is a lot more efficient in terms of travel and rent costs.

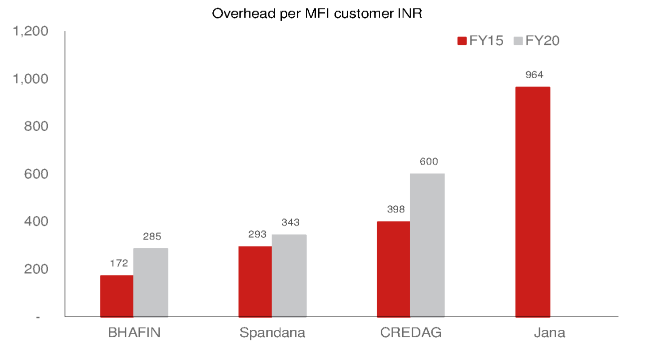
- **Overheads vs. credit cost trade-off**: Despite different cost dynamics between a weekly and a monthly collection model, we do not see a meaningful differentiation in costs given the limitation on the number of customers a loan officer can handle. However, delinquency data for the demonetization phase does show a much superior asset quality experience for the weekly collection model (fig. *60*).

Fig. 59: Overheads to AUM trends for top players



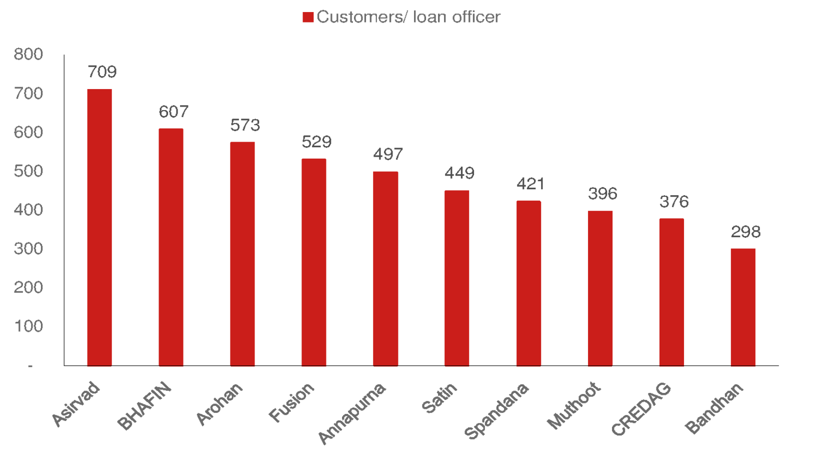
Note: BHAFIN data as of FY19
Source: Company data, Nomura research

Fig. 60: Overheads per MFI customer in INR terms



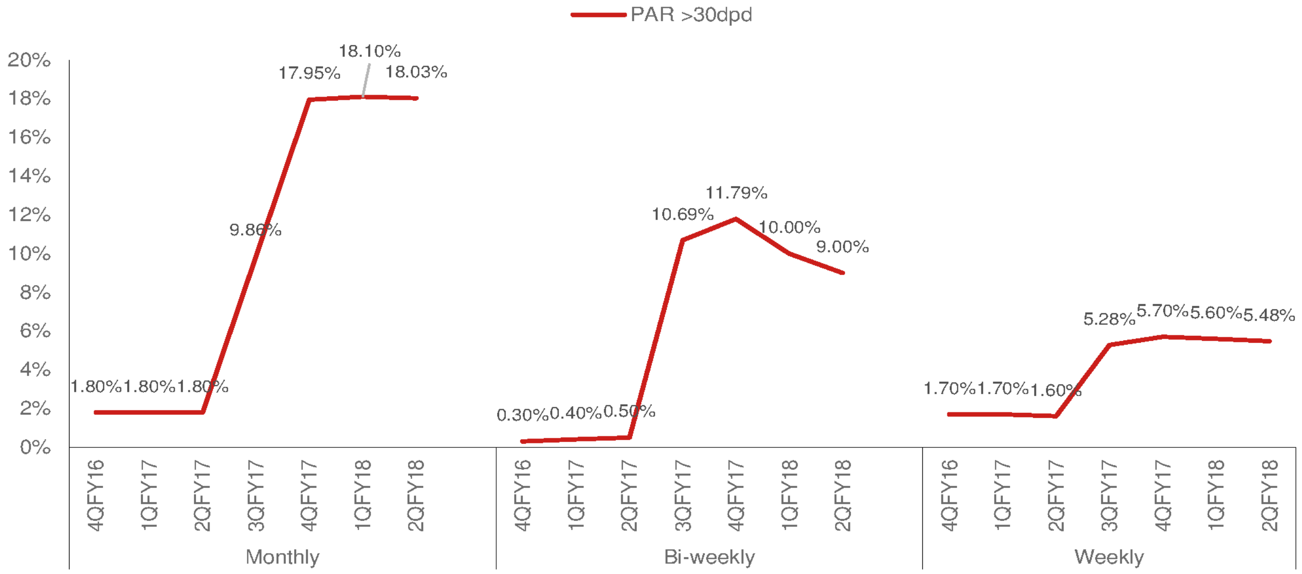
Note: 1) BHAFIN data as of FY19; 2) Bandhan, Equitas and Ujjivan non comparable in post bank phase – thus excluded
Source: Company data, Nomura research

Fig. 61: Collection model cost impact: lower customers per loan officer for weekly collection players like CREDAG and Spandana



Note: 1) Total employees (branch + asset) used for Bandhan and thus not directly comparable; 2) BHAFIN data for FY19
Source: MFIN, Nomura research

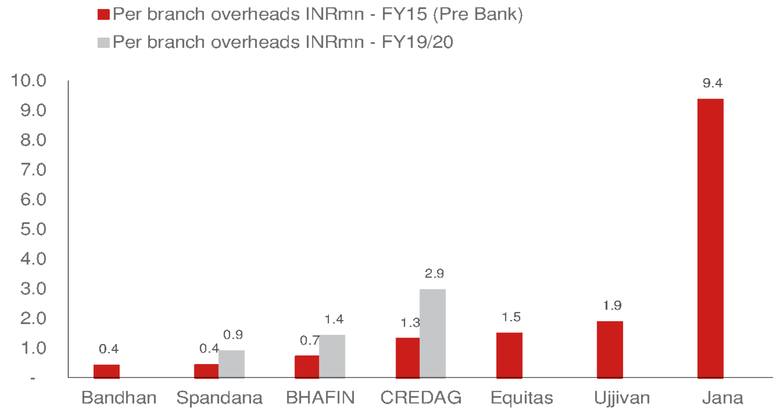
Fig. 62: Varied delinquency experience across collection models during demonetization– weekly collection model proves to be far superior



Source: Company data, Nomura research

- **Banks/SFBs vs. NBFC-MFIs**: Overheads for NBFC-MFIs converted into banks/SFBs are not directly comparable due to branch banking drags, and we thus look at the pre-bank phase overheads for top players; more rural-focused players like Bandhan, BHAFIN, Spandana and CREDAG have lower overheads per branch compared to Equitas and Ujjivan, which have been more urban-focused. SFBs/banks have much higher overheads per branch compared to NBFC-MFIs as they invest in building a liability franchise (costlier branches – more urban/semi-urban), as well as a diverse product profile.

Fig. 63: NBFC-MFIs operate at much lower overheads per branch, especially those with a rural focus

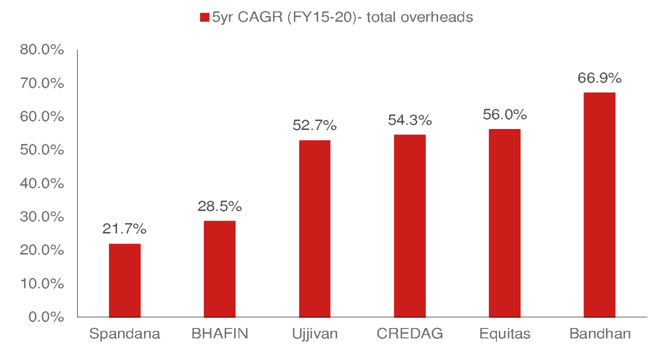


Note: 1) Bandhan, Equitas and Ujjivan FY20 is not comparable due to branch banking drags; 2) BHAFIN data as of FY19

Source: Company data, Nomura research

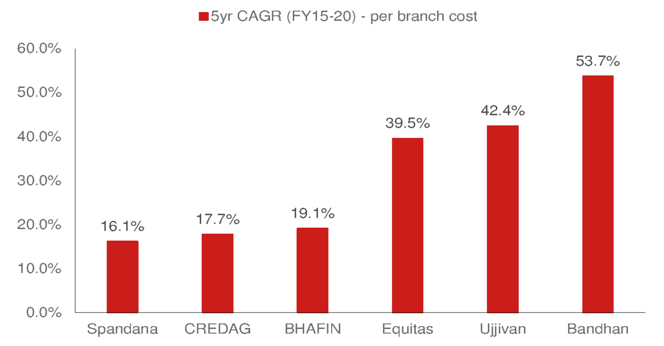
- **Overheads per branch** CAGRs for CREDAG and Spandana have been modest at 16-18% over the past four-five years, compared to AUM CAGRs of >40-45%; absolute overheads five-year CAGR for CREDAG has been high >50%, as it added ~700 branches over FY15-20.

Fig. 64: Total overheads CAGR – high for CREDAG as it opened ~700 branches over FY15-20



Source: Company data, Nomura research

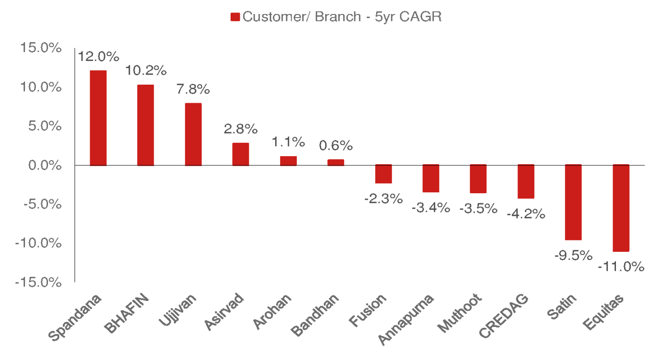
Fig. 65: Average per branch cost increase – higher for banks/SFBs due to banking operations



Source: Company data, Nomura research

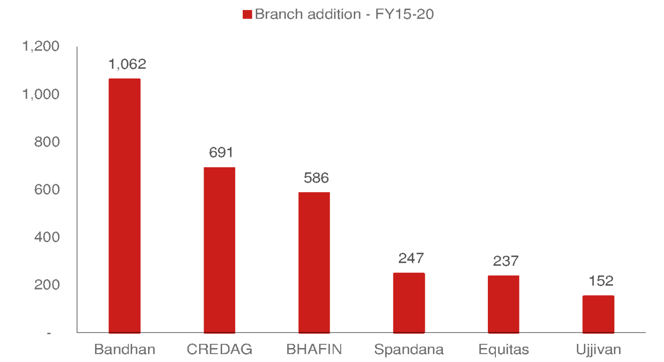
- For CREDAG, network expansion has outpaced customer additions – which reflects in both its customer per branch and GLP per branch growth trends. Over the next two-three years, we expect operating leverage to kick in for CREDAG as newer set of branches mature and start serving more customers, leading to better GLP per branch growth vs. peers.

Fig. 66: Customers per branch growth has been weak for CREDAG due to its aggressive expansion; we expect operating leverage to kick-in



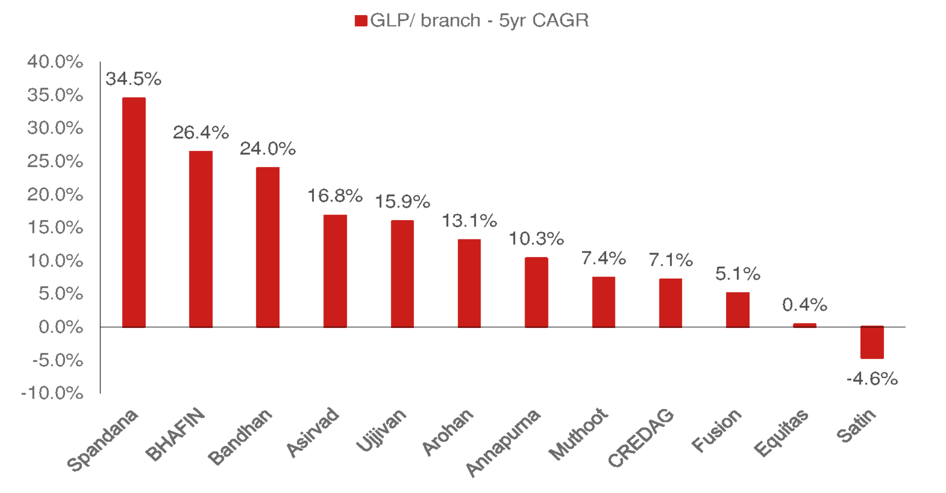
Note: DSCs for Bandhan
Source: Company data, Nomura research

Fig. 67: CREDAG has opened ~700 new branches over the past 5 years



Note: DSCs for Bandhan
Source: Company data, Nomura research

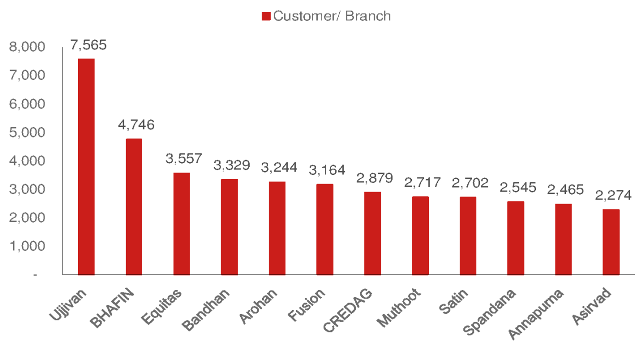
Fig. 68: GLP per branch CAGR across top players



Source: Company data, Nomura research

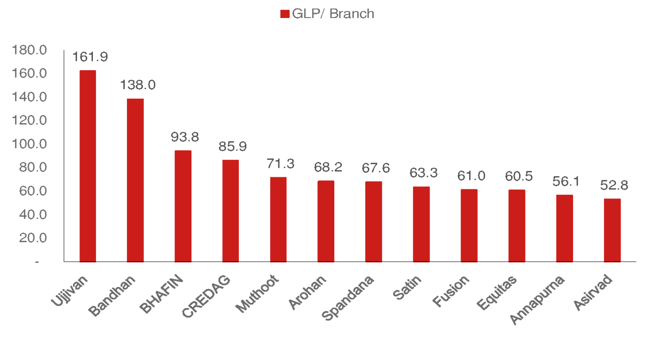
- **Urban vs. rural**: The benefits from greater urban focus (high population density) can be seen from the higher number of customers served per branch by Ujjivan (~7,500 customers per branch) and Equitas (~3,500 customers per branch) (fig. 67) compared to peers (~2,500-3,000 customers per branch), in addition to the liability accretion benefit for SFBs. Higher footfall per branch translates into best-in-class MFI AUM/branch at ~INR162mn for Ujjivan.

Fig. 69: Urban-focused players like Ujjivan/Equitas enjoy better customer reach per branch due to higher population density



Source: MFIN, Nomura research

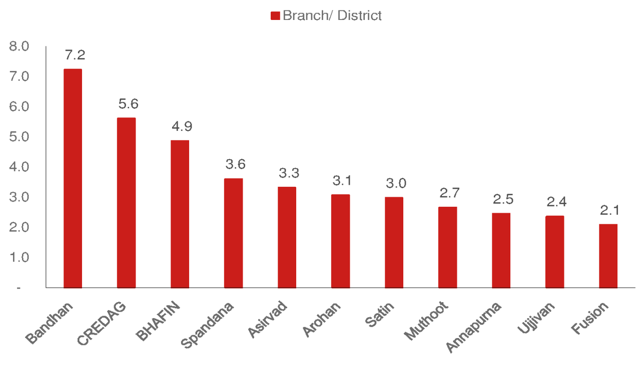
Fig. 70: CREDAG's GLP per branch still good vs. peers due to higher average loan outstanding per customer



Source: MFIN, Nomura research

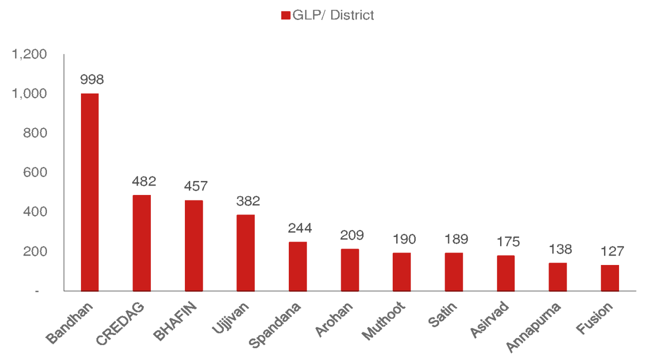
- **CREDAG strategy**: CREDAG follows a contiguous expansion model and has been very selective in entering new districts, based on criteria like penetration, competitive landscape, bureau data and past asset quality experience. CREDAG's branches/district is also high at 5.6, compared with other players at 2-3 branches/ district, leading to a higher GLP/district at ~INR480mn vs. peers at ~INR200-250mn. Bandhan Bank has the highest GLP/district at ~INR1bn due to higher ticket sizes, better customer vintage and higher penetration in its covered geographies.

Fig. 71: CREDAG has relatively higher branches per district...



Note: DSCs in case of Bandhan
Source: Company data, Nomura research

Fig. 72: … leading to higher GLP per district served

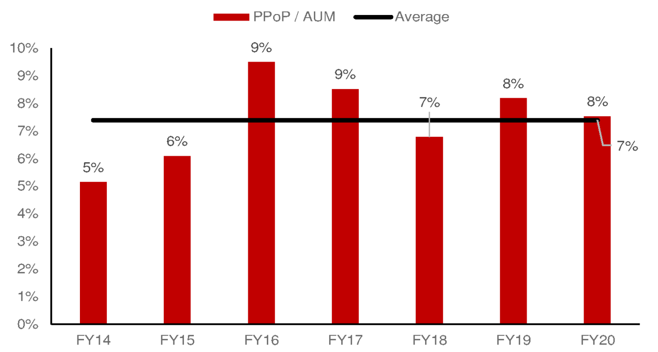


Source: MFIN, Nomura research

Through-cycle profitability has remained strong

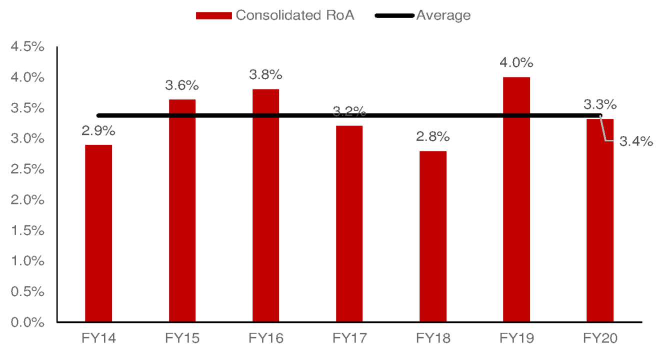
- Microfinance has not only delivered strong growth over the past decade but also strong profitability after the AP crisis. The sector has delivered strong through cycle profitability with PPOP/AUMs averaging 8% over the past 5-7 years, and ROAs of ~3-4% for the top players.
- Leverage has also come down over this period, with MFI players operating at higher capital levels now. Despite reducing their leverage, these top players have delivered ROEs of 17-18% over the past 5-7 years despite frequent disruptions like demonetization (pan India), farm waivers, natural calamities like floods/cyclones in few states such as Odisha, Kerala and Assam.
- COVID-19 pandemic-related disruptions clearly remain one of the key risks in the near-term; however, we expect PPOP/assets of 4-7% for top players, and higher capital levels – tier-1 of 20-30% for top players should be more than adequate to absorb the impact, in our view. Collection efficiency numbers for Sep/ Oct are also indicative of a strong recovery with collections nearing pre-COVID-19 levels. We do pencil in a credit cost of 350-450bps in FY21F in addition to the 50-100bps of contingent provisions created in 4Q20 to factor in the COVID-19 pandemic-related impact and think credit cost impact may be contained (explained in detail in the section below).

Fig. 73: PPOP/AUM for top-7 players has averaged ~8% over the past 7 years...



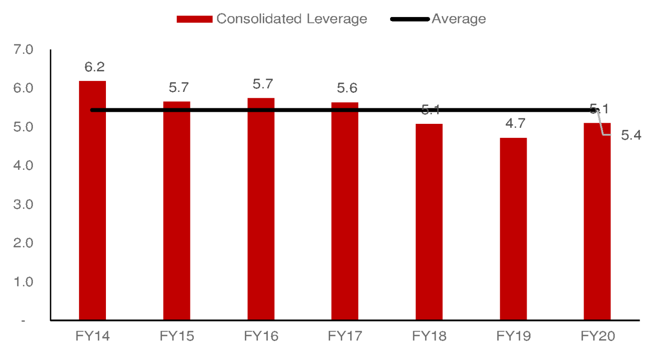
Source: Company data, Nomura research

Fig. 74: ...leading to superior RoAs of 3.5%



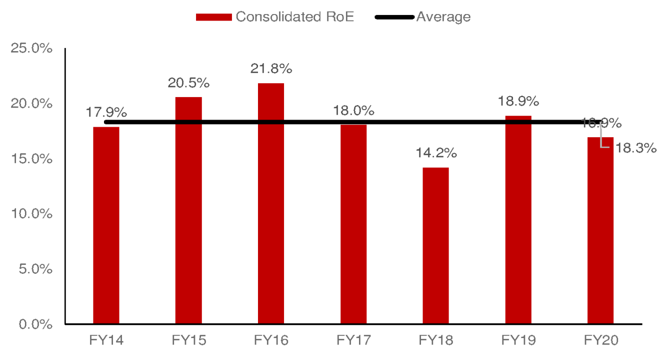
Source: Company data, Nomura research

Fig. 75: Consolidated leverage levels have declined over FY14-20...



Source: Company data, Nomura research

Fig. 76: ...yet through cycle RoEs remain quite strong at 18-19%



Source: Company data, Nomura research

Fig. 77: Key estimates for microfinance players under our coverage

Key microfinance players - NMR estimates			
PPOP	**FY21F**	**FY22F**	**FY23F**
Bandhan	6.28%	6.07%	6.07%
Equitas	3.48%	3.30%	3.50%
Ujjivan	4.68%	4.40%	4.51%
CREDAG	6.99%	7.28%	7.63%
Credit Cost			
Bandhan	3.50%	1.63%	1.58%
Equitas	2.51%	2.07%	1.56%
Ujjivan	3.58%	2.48%	2.07%
CREDAG	4.33%	1.99%	1.36%
RoA			
Bandhan	2.81%	3.69%	3.72%
Equitas	1.26%	1.36%	1.73%
Ujjivan	1.46%	1.88%	2.19%
CREDAG	2.55%	4.09%	4.76%
AUM growth			
Bandhan	13.1%	16.7%	18.7%
Equitas	26.0%	24.5%	23.3%
Ujjivan	8.7%	24.2%	21.5%
CREDAG	33.7%	25.6%	24.2%
RoE			
Bandhan	16.6%	21.7%	21.5%
Equitas	9.3%	10.3%	13.4%
Ujjivan	8.2%	11.1%	13.9%
CREDAG	9.9%	14.3%	17.5%
Tier 1			
Bandhan	24.9%	25.3%	25.5%
Equitas	22.8%	20.4%	19.1%
Ujjivan	31.0%	27.6%	25.9%
CREDAG	31.9%	29.3%	28.1%

Source: Company data, Nomura estimates

COVID-19 impact not small, but manageable

We expect the near-term stress levels to remain elevated given the COVID-19 pandemic-related impact and unsecured nature of the product. Initial trends were concerning with very high moratorium levels; however, the segment has seen much better recovery trends with collection efficiency improving sharply and nearing pre-pandemic levels for most players. While collections at MFIs are still lagging other secured retail products, the pace of recovery – with Sep-Oct collections at 90-93% –gives us confidence that the MFI segment will likely normalize over the next couple of months, and recognition/provision drags will be behind us over the next 2-3 quarters.

We build in 350-450bp credit costs (FY21F) for MFIs under our coverage, in addition to 50-100bs of COVID-19 pandemic-related provisions made in 4Q FY20, as well as some spill-over in FY22F as well, which should take care of the pandemic stress, in our view.

That said, we see multiple reasons which make us believe that credit cost outcomes may not be very severe in the microfinance sector:

1. Increase in credit costs/PAR around demonetization was also a function of multiple upcoming elections in the states of Punjab, Goa, UP and Uttarakhand in the consecutive 12 months of demonetization, which led to wide-scale announcements of farm waivers and hence impacting the repayment behavior.

2. Over the next 12 months, barring West Bengal, Tamil Nadu, Kerala and Assam, there are no upcoming elections and hence we see lower political incentives to impact the sector. We perceive election risks to be potentially higher only for Bandhan and Equitas.

3. State government balance sheets are stretched as well, given the COVID-19 pandemic-related impact, and hence their ability to announce farm waivers, like in the past, is relatively lower. Bihar did not see any disruptions during recent elections – this gives us some confidence as well.

4. In the past, MFI players demanded the entire amount overdue, thereby putting repayment burden on borrowers - who ultimately defaulted. In the current environment, with COVID-19-related moratoriums granted, customers have to start paying only single EMIs as the loan tenure gets extended. This will not put unnecessary burden on borrowers, in our view, and given that customers are not interest-sensitive and remain largely perpetual borrowers, the tenure extension won't hurt MFI players as well.

5. Furthermore , the COVID-19 pandemic impact on the rural economy has been much lower due to lesser COVID-19 infections, good monsoon and farm cashflows and the lockdowns were not too stringent; hence, we think the rural segment (56% of the industry) will see meaningfully lower credit costs while the urban segment may see higher impact.

Fig. 78: State assembly elections – timeline for the next 12 months vs demonetization period

Assembly elections timeline	States
Pre - Demonetisation period	
Apr/ May 2016	Assam
	West Bengal
	Tamil Nadu
	Kerala
Post - Demonetisation period	
Feb/ Mar 2017	Punjab
	Goa
	Uttar Pradesh
	Uttarakhand
	Manipur
Nov 2017	Himachal Pradesh
Dec 2017	Gujarat
Next 12 months	
Oct/ Nov 2020	Bihar
Apr/ May 2021	Assam
	West Bengal
	Tamil Nadu
	Kerala

Source: Nomura research

Fig. 79: Farm loan waivers in the past have also impacted delinquencies

State	Year announced	Amount announced INRbn
Andhra Pradesh	2014-15	240.0
Telangana	2014-15	170.0
Tamil Nadu	2016-17	52.8
Maharashtra	2017-18	340.2
Uttar Pradesh	2017-18	363.6
Punjab	2017-18	100.0
Karnataka	2018-19	440.0
Rajasthan	2018-19	180.0
Madhya Pradesh	2018-19	365.0
Chhattisgarh	2018-19	61.0
Total		**2,364.6**

Source: RBI, Nomura research

Fig. 80: Collection efficiencies nearing pre-COVID-19 levels for most top players

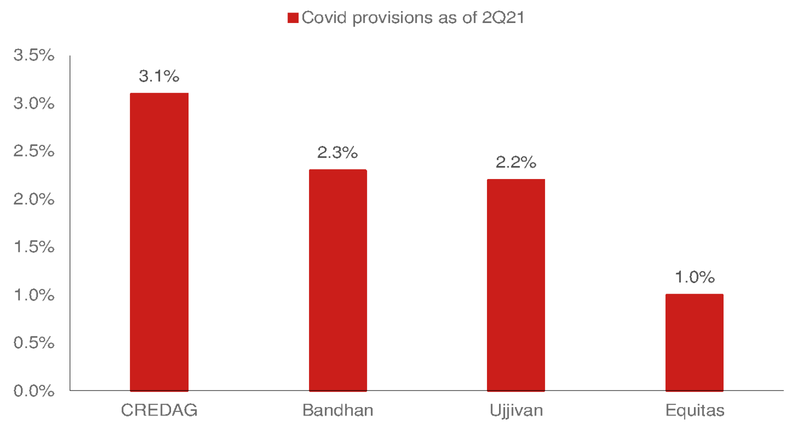
MFI collection efficiency (%)	Covid							
	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20
Ujjivan	93.0%	2.0%	14.0%	53.0%	60.0%	68.0%	83.0%	88.0%
Equitas	77.0%	0.0%	7.0%	42.0%	61.0%	77.0%		91.0%
BHAFIN			12.5%	71.0%			91.0%	93.0%
Satin		3.0%	17.0%	62.0%	85.0%	86.0%	94.0%	
Spandana		2.0%	23.0%	60.0%	75.0%	80.0%	88.0%	93.0%
CREDAG	98.0%	0.0%	0.0%	74.0%	76.0%	82.0%	88.0%	89.0%
Bandhan				68.0%			89.0%	91.0%

Source: Company data, Nomura research

Top players can absorb 13-40%of credit costs (MFI book)

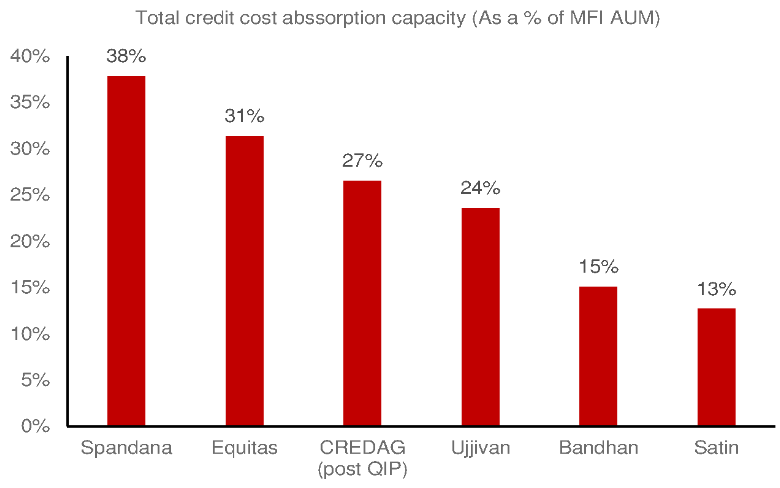
- We run a sensitivity analysis to look at the top players' ability to absorb credit costs, assuming minimum capital (tier-1) level of 15%.
- COVID-19 pandemic-related provisions of 100-300bps have already been made for our covered MFIs. With minimum tier-1 assumed at 15% and PPOP/AUM assumed to be sustainably 10% below the FY18-20 aver, we expect the top players to be able to further absorb 13-40% credit cost of the MFI book; assuming a 90% loss given default (LGD), this can help absorb slippages of 14-45% over FY21/22F.
- As explained earlier, we think there are multiple factors which make us believe that credit costs may positively surprise.

Fig. 81: Key MFI players have already created 100-300bps of COVID-19 contingent cover



Source: Company data, Nomura estimates

Fig. 82: Credit cost absorption capacity for top MFI players



Source: Company data, Nomura estimates

Key risks

Microfinance remains a high-risk segment

- While growth opportunity remains large, the sector has seen multiple risk events in the past leading to spikes in credit costs and NPAs.
- However, the sector has come a long way after the AP crisis (2010), especially with the sector coming under RBI regulation and the emergence of credit bureaus. That said, most of the recent credit events have been more politically inflicted while ultimate credit loss from natural calamities have been limited.
- In that context, we see concentration risks to be one of the key risks in microfinance. During the AP crisis as well, 62% of India's MFI GLP was concentrated in Andhra Pradesh. Top 3 MFIs – SKS, Spandana and Share – had significant exposure to AP, ranging from 35-50% of their books. Top 5 of the 6 largest MFIs in AP had to restructure under the CDR scheme as a result of the disproportionate exposure to AP, and the inability to deal with such high write-offs.
- That said, we see some merits in having concentrated exposures as well – for example, the credit experience in home geographies for the MFI players has been better than peers, given the deeper penetration and better connect with customers. Also, it does help in reducing the frequency of such credit events.
- Further, incrementally MFI players such as CREDAG have been choosing to diversify its district-wise exposure rather than diversifying across states, like in the case of Ujjivan. This not only helps in maintaining customer connect and strengthening market understanding, but also in mitigating concentration risks to a great degree. This also aids in a much better cost management. That said, we also think that a "state" remains an important administrative unit for the purpose of asset quality assessment, and usually the impact of certain events is seen across districts in a state.
- In the section below, we analyze the past MFI cycles/calamities and their impact on key players, delinquencies and final credit cost outcomes.

Lower entry barrier has been another key risk

- Lower entry barrier has been one of the key risks in the sector which has seen a surge in PE-backed MFIs chasing high growth and high ROEs that the segment offers.
- This has led to a significant rise in the number of MFIs operating in various states over the past 5-6 years. This is evident from the steep rise in MFIs in faster-growing states, e.g., Assam, Bihar, Chattisgarh, Gujarat, Haryana, Jharkhand, MP, Orrisa, Rajasthan, UP and West Bengal have seen a significant rise in the number of NBFC-MFIs operating in the region (10-15 new players added over the past 3-4 years).
- Hence, we think it is best to stick to more disciplined players in the sector – which have a much better learning curve from its past mistakes.
- That said, we do acknowledge that there is limited scope to escape from this risk as with increasing competitive intensity, even stronger players get impacted. Bandhan Bank has seen its unique customer mix falling from 70% in FY17 to 50% currently, with a rise in the number of MFIs operating in that segment.

Fig. 83: Significant increase in the number of MFIs operating across most states

State wise Count of NBFC-MFIs operational	FY12	FY14	FY17	FY20
Assam	7	6	6	19
Bihar	14	17	15	35
Chattisgarh	8	8	16	27
Delhi	8	9	5	4
Gujarat	16	18	11	22
Haryana	10	9	11	21
Jharkand	7	10	12	28
Karnataka	15	18	12	18
Kerala	7	7	7	10
Maharashtra	17	22	24	26
Madhya pradesh	17	21	19	26
Orrisa	11	11	13	27
Punjab	4	5	8	13
Rajasthan	12	14	14	24
Tamil Nadu	24	20	10	18
Uttarakhand	7	10	10	12
Uttar Pradesh	14	15	15	29
West Bengal	11	12	8	23

Source: MFIN, Nomura research

COVID-19 pandemic-related impact remains a key near-term risk

- We build in 350-450bps credit costs (FY21F) for MFIs under our coverage, in addition to 50-100bps of COVID-19 pandemic-related provisions made in 4Q FY20 and some spill-over in FY22F as well, which should take care of the pandemic stress, in our view. However, higher-than-expected COVID-19 stress remains a key near-term risk.

Appendix

Learnings from the past cycles

Krishna Crisis 2006

- Across the whole Krishna district (in the state of Andhra Pradesh) 50 offices of leading MFIs including Spandana, Asmita and Share were shut by the local government, impacting collections, and clients were instructed to not repay loans. Of the INR20bn of total loan outstanding in AP – INR10bn was lent in the Krishna district and INR6bn in the nearby Guntur district.
- **What led to it?** – Very high interest rates, coercive collection methods, and exorbitant profiteering from poor and under-privileged.
- **Impact** – RBI intervention prevented prolonged shutdown, although funding and borrowing rates for MFIs were impacted in the shorter run. MFIs agreed to bring down interest rates and to introduce a code of conduct. The situation lasted for eight months. However, the code of conduct was implemented in theory only and lending practices remained aggressive, leading to over-leveraging even later on.

Karnataka Crisis – 2009/10

- During Jan/ Feb 2009, in the town of Kolar in Karnataka, the local community body directed non-payment of MFI loans and prohibited any dealings with the MFIs in light of an attempted suicide case; the Muslim community formed 60-70% of the borrowers at the time. Default rates for Kolar increased to ~35%. (*link*)
- The Association of Karnataka Microfinance Institutions (AKMi) *report* (published in April 2010) suggests overleveraging, irresponsible lending practices did exist, which along with community issues, led to the crisis. The local Muslim community body, in light of an attempted suicide case, issued fatwa prohibiting all dealings with MFIs – triggering mass defaults.
- MFI practices like lending to women borrowers (due to better repayment profile compared to men), regular group meetings with unrelated men (loan officers), and filing of personal photographs, etc., were considered in violation of its socio-cultural norms by the local Muslim community.
- The Kolar incident spread out to the nearby districts of Sidlaghatta (default rates 8-28%), Ramnagaram (default rates 6-30%) and Mysore (default rates 5-60%). The defaults were partly incited by the events in Kolar and the socio-communal issues, and partly due to the silk industry slow-down due to GFC, while raw material prices rose sharply leading to significant stress for borrowers. In Mysore, communal riots lead to widespread disruption and impacted the repayment capacity of borrowers in April-July 2009.

Fig. 84: Karnataka 2009/10 disturbances – timeline

Date of first mass default	02-Feb-09	3-10 March 2009	8-9 May 2009	19 May/ 2-5 July 2009
Town/ District	Kolar	Siglaghatta	Ramanagaram	Mysore
Trigger in the operating environment	Attempted suicide led to Anjuman Committee edict that no Muslim client should repay MFI loans	Rise in input prices over the previous 6 months led to payment difficulties – Kolar provided excuse for mass default	Announcements from the local Masjids banning repayment of MFI loans	Communal riots led to business failure.

Source: AKMi Report, Nomura research

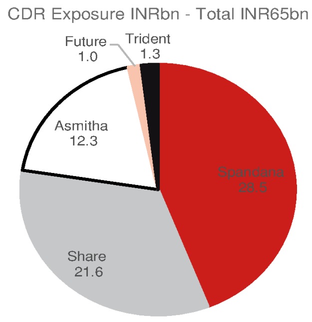
AP Crisis – 2010

- The AP government in October 2010 enacted an ordinance disallowing MFIs to make weekly collections; they were forced to move to monthly collections and could not conduct door-to-door collections (only allowed in public places), and coercive methods were prohibited. AP was an important state for MFI players at that time, with 62% of the industry GLP concentrated in AP in FY11. Industry leaders like BHAFIN, Share and Spandana had significant exposure to AP, ranging at 35-50% of their book. Five out of top six AP players had to undergo corporate debt restructuring (CDR).
- **Reason to enact the ordinance**: The ordinance was enacted on the grounds that

MFIs were charging usurious interest rates, and were using coercive means of collections – which in certain cases had led to suicides.

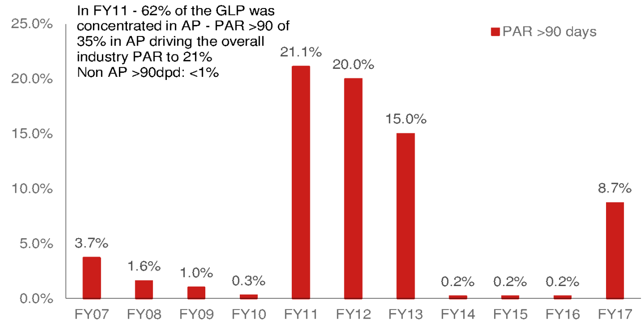
- This, coupled with political instigation to not repay loans, led to mass defaults. AP was particularly overheated, and multiple and irresponsible lending led to over-leveraging; as per *reports,* average household debt in AP at that time was INR65,000, compared to national average of INR7,700.
- Note that 84% of households in AP had two or more loans, while as high as 58% had 4 or more loans at that time. *Reports* suggest delinquency levels had already started rising in June 2010, while lenders managed to hide them by rolling over loans before reports of borrower suicides started emerging in Sept/Oct 2010.
- **Impact**: Over 9.2mn loans worth INR72bn (about USD1.5bn at that time) became overdue, and 90% remained unpaid even by April 2012. Banks panicked and stopped lending to MFIs all over India, leading to funding issues for the whole sector.
- Five players (excluding BHAFIN) of the top 6 operating in AP had to undergo CDR (INR65-70bn of debt was restructured).

Fig. 85: 5 of the top 6 MFIs in AP had to undergo CDR



Source: Company data, Nomura research

Fig. 86: PAR90 inched up significantly to +20% levels during the AP crisis; PAR90 was 35% for AP (+60% of India MFI AUM)



Source: Company data, Nomura research

- **Player-wise impact:**
  - **Bharat Financial (formerly SKS):** BHAFIN was the largest MFI player at that time and had large presence in AP. It was the only listed MFI player and had just concluded its IPO in August 2010, before the AP ordinance came into effect in October 2010. Of its ~INR45bn odd loan book at the time, 35-36% of the same was in AP (~INR15bn of loans).
  - BHAFIN over the next 2-3 years had to eventually write off effectively +90% of its exposure to AP. Its net worth declined by 75-80% as a result, thus forcing it to de-grow its loan book to meet capital adequacy requirements. It was the only MFI amongst the top 7 in AP to not get into CDR.
  - BHAFIN went on to raise INR2.3bn in its QIP issue in 1Q13 and returned to profitability there from, leading to capital generation internally. BHAFIN was thus able to recoup a significant part of the lost market share – 10% market share in FY19/20, compared to 14% market share in FY11.
  - BHAFIN was eventually acquired by IIB in an all-stock deal worth ~INR150bn in October 2017.
  - **Spandana (*link*):** Prior to the AP crisis, Spandana was the second-largest MFI with an INR45bn portfolio (12% market share in FY11), with 51% of it sitting in AP, and thus was severely impacted during the crisis – impacting its performance over the next 6-7 years.
  - In 2014, it started generating profits again, and got its CDR debt refinanced in 2017 by raising USD275mn in debt and equity, and moved out of the CDR mechanism – post which it has started to grow meaningfully since FY18, and has improved its market share to 3% from 1% in FY17.
  - **Share Microfin and Asmitha Microfin**: Share Microfin was the third-largest MFI in the country with an AUM of INR20bn (7% market share) and 3.3mn clients, and

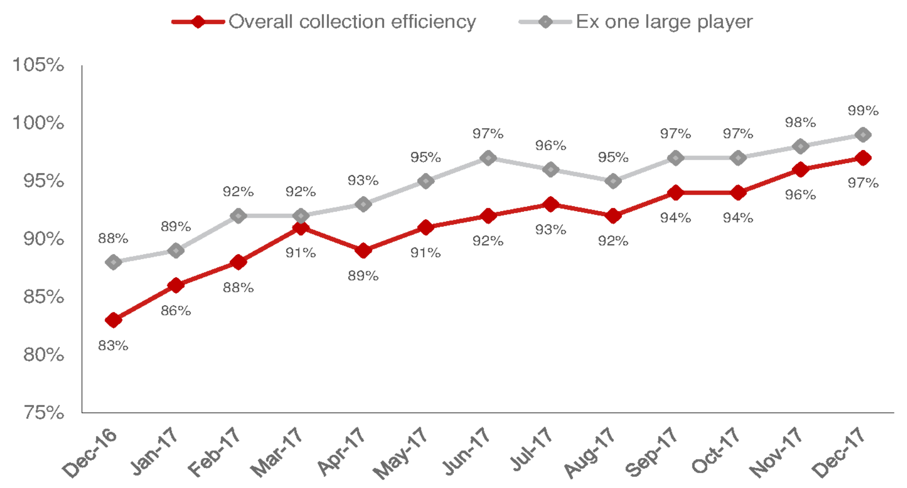
had been operating since 1989.

- Share Microfin underwent an INR19bn debt restructuring after the AP crisis. Its current loan book at ~INR8bn is barely one-third of the pre-AP times (<0.5% market share).
- Asmitha had an AUM of INR14bn as of FY10, of which 50% was concentrated in AP. Share Microfin and Asmitha had entered into an arrangement to demerge their AP and non-AP portfolios into one company – Share to hold non-AP portfolio, while Asmitha to hold AP portfolio.
- **Trident Microfin (*link*)**: Trident had initiated operations in 2007. Trident was relatively small with INR1.4bn in AUM as of Jun-2010 (<1% market share), but was predominantly AP-based.
- Despite efforts to revive the company under the CDR mechanism, Trident was unable to recover bad debts from AP (80% of the loan book in AP at the time of ordinance), and thus its condition only deteriorated further.
- The CDR cell eventually asked the lenders' consortium to consider a one-time settlement offer of 18%. Trident was the only company to be wound up of the 6 CDRs from the AP crisis.
- **Future Financial Services** (*link*): FFSL was the first MFI to be admitted under the CDR mechanism. It had 23% of its portfolio in AP at the time of ordinance, and was severely impacted. FFSL was successfully able to complete a turnaround, with its private equity shareholder India Value Fund Advisors (IVFA) raising its stake from 18% to 45.3% over multiple capital infusion rounds. FFSL was later acquired by Disha Microfin, which now operates as an SFB – Fincare small finance bank.

Demonetization - Nov/Dec 2016:

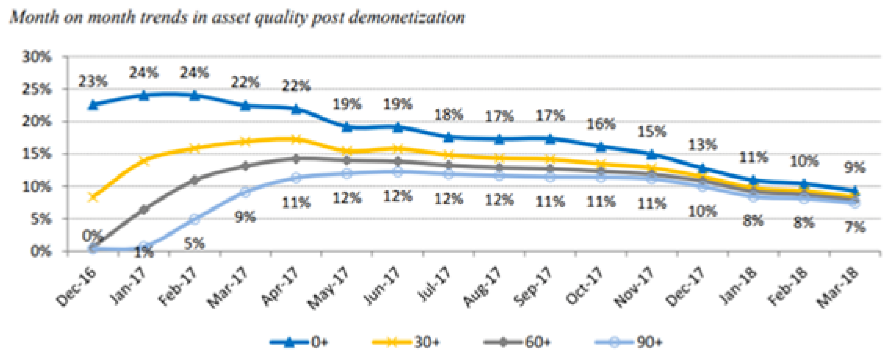
- In November 2016, the government of India announced the demonetization of bank notes of INR500 and INR1,000 denominations, which resulted in a severe cash crunch and a sizeable loss for the industry. MFI industry is heavily dependent on cash, and thus, the shortage of cash lead to a direct impact on repayment capabilities.
- In the aftermath of demonetization, inadequate currency supply, political interference in some states, and disruption in borrower cash flows led to a sharp dip in MFIs' collection efficiencies (from over 98% prior to demonetization to approximately 75-80 % in November and December 2016). However, subsequently, overall monthly collection efficiencies (including overdue collections) improved to 97% in December 2017, from sub-90% as of March 2017.
- Overall industry had to write-off 5-10% of loans. Meanwhile, RBI had granted a 60 day moratorium on loan repayments, which was construed as loan waiver by many borrowers – this was also one of the reasons for the rise in delinquencies. Farm loan waivers in certain states like Maharashtra, Uttar Pradesh, Karnataka and Punjab during the same time also sparked confusion, leading to lower collections.
- Political parties also *fueled defaults* in some of the states like Maharashtra, UP, Punjab, Goa, as assembly elections were in vicinity then. This, in addition to the high number of MFIs operating in these states, led to much higher delinquencies in these states, compared to the national average.

Fig. 87: Collection efficiency post-demonetization



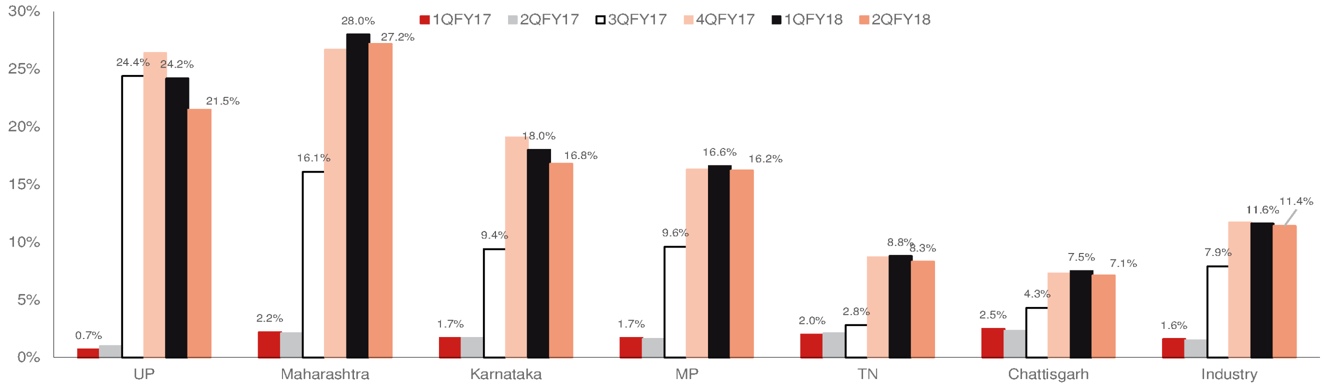
Source: ICRA, Nomura research

Fig. 88: Delinquency trends across various cohorts post-demonetization



Source: ICRA, Nomura research

Fig. 89: State-wise PAR >30 delinquencies during demonetization



Source: ICRA, Nomura research

Fig. 90: Assembly elections around demonetization also caused some disruptions in election states

Assembly elections timeline	States
Pre - Demonetisation period	
Apr/ May 2016	Assam
	West Bengal
	Tamil Nadu
	Kerala
Post - Demonetisation period	
Feb/ Mar 2017	Punjab
	Goa
	Uttar Pradesh
	Uttarakhand
	Manipur
Nov 2017	Himachal Pradesh
Dec 2017	Gujarat
Next 12 months	
Oct/ Nov 2020	Bihar
Apr/ May 2021	Assam
	West Bengal
	Tamil Nadu
	Kerala

Source: Nomura research

Fig. 91: Farm loan waivers also contributed to rising delinquencies during demonetization

State	Year announced	Amount announced INRbn
Andhra Pradesh	2014-15	240.0
Telangana	2014-15	170.0
Tamil Nadu	2016-17	52.8
Maharashtra	2017-18	340.2
Uttar Pradesh	2017-18	363.6
Punjab	2017-18	100.0
Karnataka	2018-19	440.0
Rajasthan	2018-19	180.0
Madhya Pradesh	2018-19	365.0
Chhattisgarh	2018-19	61.0
Total		**2,364.6**

Source: RBI, Nomura research

Fig. 92: State-wise delinquency trends

States	FY16	1QFY17	2QFY17	3QFY17	FY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20
Par 30																	
Karnataka	0.49%	0.44%	0.40%	5.67%	18.00%	4.94%	4.40%	4.19%	3.70%	3.41%	2.04%	1.57%	1.13%	1.20%	1.95%	3.24%	3.76%
Tamil Nadu	0.21%	0.21%	0.37%	1.04%	14.00%	1.92%	1.67%	1.90%	1.50%	1.36%	1.09%	1.67%	2.07%	1.20%	2.29%	3.07%	2.14%
Uttar Pradesh	0.39%	0.44%	0.76%	28.72%	37.00%	23.67%	17.68%	14.08%	10.80%	6.34%	5.89%	4.99%	3.17%		2.91%	2.71%	1.98%
Maharastra	0.29%	0.32%	0.44%	9.10%	28.00%	15.54%	17.44%	14.08%	10.40%	8.37%	4.97%	4.67%	2.73%	0.40%	2.62%	2.53%	1.96%
Madhya Pradesh	0.46%	0.42%	0.58%	7.15%	17.00%	12.78%	11.51%	8.67%	6.30%	5.22%	3.58%	4.66%	3.34%	1.30%	3.27%	3.04%	2.14%
Bihar	**0.22%**	**0.17%**	**0.16%**	**0.74%**	**3.00%**	**0.51%**	**1.14%**	**1.20%**	**0.80%**	**0.57%**	**0.51%**	**0.53%**	**0.30%**		**0.34%**	**0.51%**	**0.40%**
Odisha	0.09%	0.07%	0.08%	0.36%	1.00%	0.34%	0.63%	0.73%	0.60%	0.49%	0.48%	0.55%	0.59%	0.50%	2.26%	2.24%	1.82%
West Bengal	**0.18%**	**0.15%**	**0.21%**	**2.41%**	**14.00%**	**1.81%**	**3.24%**	**2.72%**	**1.10%**	**0.98%**	**0.65%**	**0.74%**	**0.54%**	**0.10%**	**0.89%**	**1.35%**	**1.22%**
Gujarat	0.53%	0.66%	0.68%	5.29%	16.00%	7.68%	6.42%				2.89%		1.42%	1.70%	2.72%		
Kerala	0.10%	0.08%	0.07%	0.75%	1.00%	1.46%	2.37%	2.42%	2.70%	2.62%		2.76%	2.28%	0.20%	4.76%	3.79%	3.71%
Punjab	0.19%	0.20%	0.19%	8.12%	16.00%	18.79%	9.25%	7.17%	5.90%	2.99%	2.68%	2.11%	1.59%		1.28%	1.85%	0.78%
Rajasthan	0.64%	0.59%	0.56%	8.22%	11.00%	5.11%	7.16%	5.73%	3.70%	1.85%	1.74%	0.97%	0.61%	0.90%	0.76%	1.04%	0.72%
Jharkhand		0.20%	0.29%	2.82%	10.00%	4.33%	7.48%	5.38%	3.40%	2.37%	2.49%	1.31%	0.92%		1.57%	1.46%	1.22%
Haryana	0.38%	0.52%	0.70%	13.97%	22.00%	15.39%	15.82%	13.76%	10.50%	6.06%	4.32%	3.58%				1.81%	
Assam	**0.07%**		**0.16%**	**0.61%**	**1.00%**			**1.43%**	**0.90%**	**0.67%**	**0.44%**	**0.46%**	**0.33%**		**0.96%**	**9.21%**	**20.95%**
Chattisgarh		0.28%				2.15%	2.22%	1.62%	1.20%	0.88%	1.36%	0.73%	0.71%	0.30%	1.13%	1.48%	1.49%
PAR90																	
Karnataka	0.33%	0.31%	0.30%	0.34%	12.00%	3.88%	3.40%	3.55%	3.20%	3.03%	1.68%	1.35%	0.91%	1.40%	0.98%	1.04%	2.91%
Tamil Nadu	0.11%	0.13%	0.26%	0.21%	2.00%	1.15%	1.04%	1.32%	1.00%	0.94%	0.86%	0.69%	0.94%	1.70%	1.36%	1.97%	1.47%
Uttar Pradesh	0.23%	0.19%	0.36%	0.87%	14.00%	11.17%	12.58%	10.11%	8.40%	4.90%	4.56%	3.95%	2.46%		2.24%	2.05%	1.35%
Maharastra	0.19%	0.20%	0.25%	0.40%	20.00%	13.17%	14.76%	12.63%	9.70%	7.70%	4.34%	4.14%	2.31%	0.80%	1.78%	1.93%	1.51%
Madhya Pradesh	0.30%	0.27%	0.32%	0.59%	9.00%	8.33%	8.07%	6.64%	5.10%	4.20%	2.85%	3.90%	2.54%	1.80%	2.44%	2.22%	1.47%
Bihar	**0.14%**	**0.12%**	**0.10%**	**0.12%**	**1.00%**	**0.28%**	**0.65%**	**0.77%**	**0.50%**	**0.41%**	**0.35%**	**0.35%**	**0.20%**		**0.21%**	**0.31%**	**0.26%**
Odisha	0.06%	0.05%	0.05%	0.15%	0.30%	0.19%	0.40%	0.54%	0.40%	0.36%	0.34%	0.37%	0.42%	1.80%	1.17%	1.41%	1.37%
West Bengal	**0.13%**	**0.10%**	**0.12%**	**0.30%**	**4.00%**	**1.27%**	**2.35%**	**2.23%**	**0.90%**	**0.77%**	**0.51%**	**0.54%**	**0.37%**	**0.10%**	**0.62%**	**0.95%**	**0.90%**
Gujarat	0.33%	0.40%	0.42%	0.66%	9.00%	4.67%	4.53%				1.71%		1.17%	3.20%	2.12%		
Kerala	0.06%	0.04%	0.05%	0.08%	1.00%	0.72%	1.32%	1.58%	1.80%	1.72%		1.76%	1.44%	0.40%	2.78%	3.15%	2.72%
Punjab	0.13%	0.12%	0.12%	0.14%	5.00%	9.04%	6.62%	5.34%	4.40%	2.38%	2.17%	1.75%	1.28%		1.02%	1.40%	0.60%
Rajasthan	0.47%	0.36%	0.31%	0.56%	5.00%	2.61%	5.30%	10.39%	2.80%	1.43%	1.35%	0.73%	0.44%	1.40%	0.52%	0.75%	0.49%
Jharkhand		0.14%	0.16%	0.40%	5.00%	2.70%	5.56%	4.49%	2.90%	2.07%	2.15%	0.93%	0.68%		1.08%	1.01%	0.92%
Haryana	0.20%	0.28%	0.37%	0.62%	11.00%	8.03%	11.32%	10.54%	8.40%	5.01%	3.40%	2.70%				1.38%	
Assam	**0.04%**		**0.10%**	**0.14%**	**0.30%**			**1.12%**	**0.70%**	**0.53%**	**0.29%**	**0.33%**	**0.24%**		**0.36%**	**0.85%**	**9.89%**
Chattisgarh		0.07%				1.48%	1.59%	1.32%	1.00%	0.69%	0.59%	0.55%	0.49%	0.50%	0.72%	0.98%	1.00%
PAR180																	
Karnataka	0.19%	0.18%	0.20%	0.25%	0.20%	1.95%	2.36%	2.77%	2.60%	2.57%	1.42%	1.12%	0.71%	0.90%	0.50%	0.45%	0.99%
Tamil Nadu	0.05%	0.07%	0.13%	0.14%	0.20%	0.63%	0.51%	0.88%	0.70%	0.66%	0.59%	0.45%	0.42%	1.10%	0.38%	0.84%	0.85%
Uttar Pradesh	0.16%	0.16%	0.14%	0.27%	0.60%	2.27%	8.85%	7.20%	6.30%	3.54%	3.21%	2.83%	1.88%		1.73%	1.51%	0.97%
Maharastra	0.08%	0.12%	0.13%	0.16%	0.20%	7.90%	12.99%	10.28%	8.60%	6.99%	3.60%	3.54%	1.93%	0.50%	1.41%	1.31%	1.09%
Madhya Pradesh	0.17%	0.17%	0.16%	0.19%	0.40%	3.52%	6.02%	4.14%	3.60%	3.15%	2.10%	3.02%	1.92%	0.80%	1.81%	1.61%	1.06%
Bihar	**0.08%**	**0.08%**	**0.07%**	**0.03%**	**0.10%**	**0.13%**	**0.40%**	**0.49%**	**0.30%**	**0.28%**	**0.24%**	**0.23%**	**0.12%**		**0.13%**	**0.17%**	**0.14%**
Odisha	0.03%	0.02%	0.03%	0.08%	0.10%	0.08%	0.25%	0.34%	0.30%	0.25%	0.24%	0.24%	0.23%	1.60%	0.42%	0.75%	0.90%
West Bengal	**0.08%**	**0.07%**	**0.07%**	**0.07%**	**0.20%**	**0.66%**	**1.74%**	**1.79%**	**0.60%**	**0.55%**	**0.36%**	**0.40%**	**0.26%**	**0.10%**	**0.40%**	**0.56%**	**0.55%**
Gujarat	0.14%	0.20%	0.18%	0.30%	0.40%	1.43%	2.65%				1.01%		0.90%	2.20%	1.06%		
Kerala	0.04%	0.03%	0.04%	0.06%	0.10%	0.26%	0.48%	0.85%	1.00%	1.00%		1.00%	0.80%	0.30%	0.98%	1.72%	2.11%
Punjab	0.10%	0.07%	0.05%	0.05%	0.03%	0.52%	4.72%	3.98%	3.30%	1.75%	1.60%	1.26%	1.04%		0.87%	1.01%	0.47%
Rajasthan	0.18%	0.24%	0.13%	0.18%	0.30%	0.54%	3.92%	7.95%	2.10%	1.01%	0.99%	0.47%	0.30%	0.90%	0.37%	0.45%	0.32%
Jharkhand		0.08%	0.10%	0.15%	0.40%	1.07%	3.16%	3.19%	2.30%	1.68%	1.91%	0.70%	0.39%		0.68%	0.60%	0.57%
Haryana	0.11%	0.12%	0.15%	0.18%	0.40%	2.52%	7.71%	7.30%	5.90%	3.83%	2.68%	1.88%				0.95%	
Assam	**0.03%**		**0.08%**	**0.07%**	**0.10%**			**0.70%**	**0.50%**	**0.39%**	**0.19%**	**0.19%**	**0.14%**		**0.19%**	**0.29%**	**0.70%**
Chattisgarh		0.03%				0.76%	0.98%	0.92%	0.70%	0.52%	0.43%	0.38%	0.31%	0.30%	0.39%	0.54%	0.57%

Source: MFIN, Nomura research

Fig. 93: Demonetization impact for top players

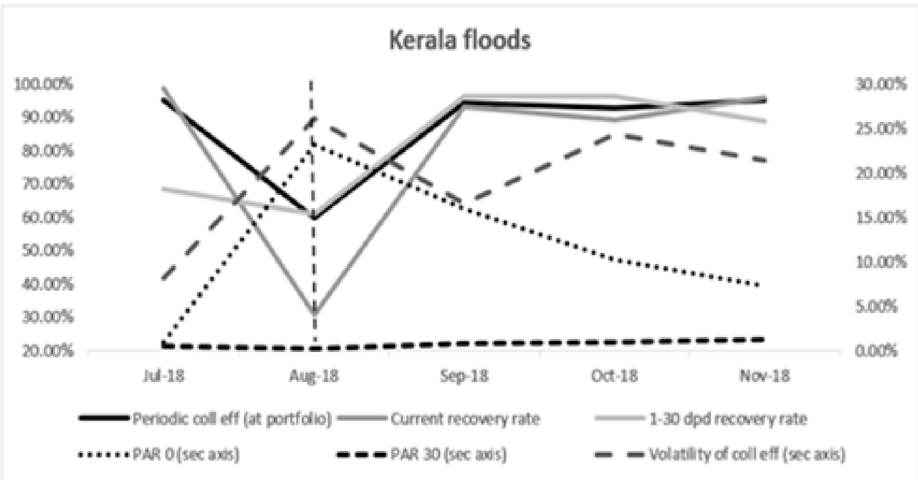
MFIs	Demonetisation impact
Bandhan Bank	Not much impacted through demonetization as West Bengal and Assam were least impacted states.
Ujjivan SFB	Geographically diversified book with Maharashtra/ Karnataka/ West Bengal / Tamil Nadu having relatively higher exposures – 130/450bps of credit cost in FY17/18.
Equitas SFB	Tamil Nadu focused book (less impacted during demonetisation) + Diversified product mix led to lower credit cost experience 165/220bps.
Jana SFB	Having grown very aggressively from INR10bn to INR128bn over FY13-17, Jana was the worst hit during demonetization as it lost significant market share from 13% as of FY17 to 3% in FY19. Over FY18-20 – Cumulative slippages were INR52bn (41% of FY17 o/s GLP) and of which cumulative write-offs were INR31bn (24% of FY17 o/s GLP).
Suryodaya SFB	Large presence in Maharashtra (INR 5bn) and Tamil Nadu (INR5.5bn) – GNPA inched up to 6.2% in FY17 from 16bps in FY16, declined to 3.5% and to 1.8% in FY18 and FY19 respectively – largely write-off driven. Absorbed credit cost of 1.5% /4.2% /1.9% over FY17-19.
CREDAG	High exposure to Maharashtra (16% mkt share) and Karnataka (25% mkt share) led to higher delinquencies compared to national average as a result– Credit cost of 390/320bps in FY17-18.
Spandana	Karnataka, MP, Odisha, Maharashtra are the key states (Mid single digit market share in all 4 states) - credit cost inched up to 3.3%/1.7% in FY17-18.

Source: Company data, Nomura research

Kerala Floods – August 2018:

- A *study* by Northern Arc Capital on 27,000 loans in the nine impacted districts of Kerala suggested a drop in collection efficiency to 60% from 96% (pre-event) in August 2018, but improved gradually over Sept-Nov 2018. Not much impact was seen in PAR30 >30 – as mostly just a single installment was missed (due to the event). Current recovery rates normalized, starting from September 2018.
- **Key player – ESAF Small Finance Bank** – ESAF SFB had a portfolio outstanding of INR66bn (largely MFIs) as of end-FY20 (INR46bn as of FY19), of which INR37bn (50-55% of the total exposure) lies in Kerala (INR24bn as of FY19) – 35-40% market share in Kerala. Credit costs increased to 240bps for FY19 owing to the flood-related disruption, vs. ~100bps of steady state credit cost.

Fig. 94: Current recovery rates normalized over the next 2-3 months, post Kerala floods

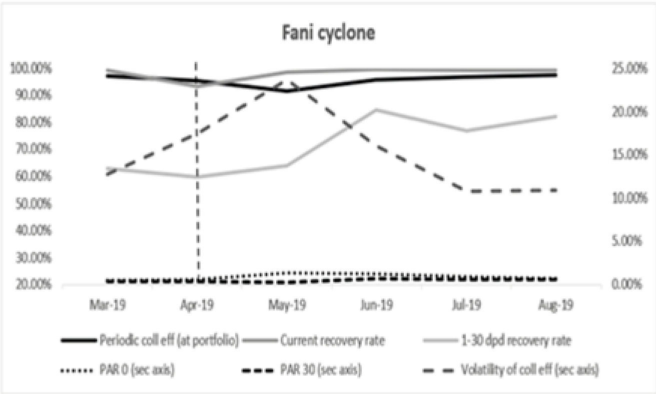


Source: Northern Arc Capital, Nomura research

Cyclone Fani in Orrisa – April 2019:

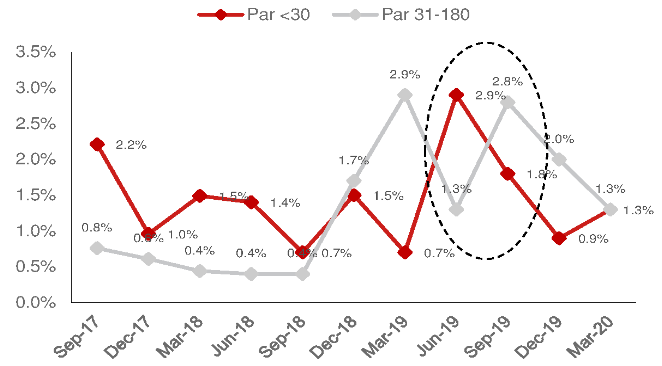
- Based on an *analysis* of 75,000 loans by Northern Arc Capital across 14 districts in Odisha, an immediate drop from 97% to 90% in collections was observed. The pick-up in collections was swift and normalized in two months' time, given that Odisha is accustomed to frequent cyclones.
- We observe that, bounce back from natural calamities has been much stronger compared to moral hazard created by politically motivated interference.
- PAR<30 increased to 290bps, from 70bps in 1Q20; however, it normalized over the next couple of quarters.

Fig. 95: Recovery post the cyclone was quite quick, and current recovery rates touched normalcy in the next month itself



Source: Northern Arc Capital, Nomura research

Fig. 96: PAR book stabilized over the next 2 quarters



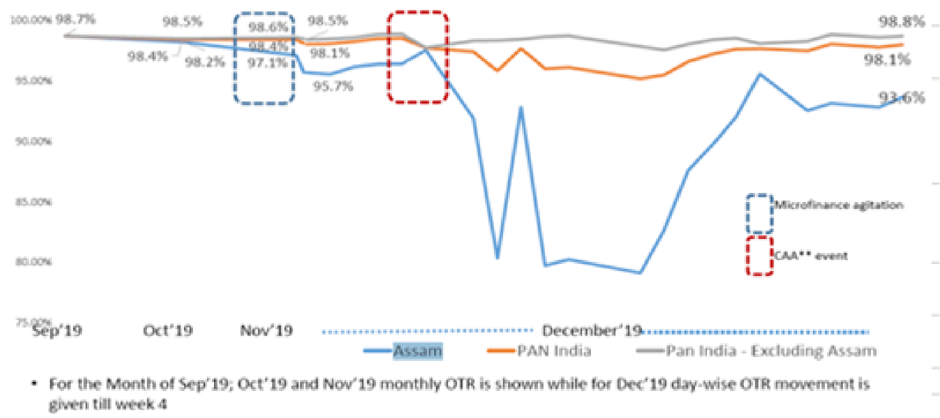
Source: CRIF Highmark, Nomura research

Assam crisis (*link*) – Nov/Dec 2019

- Towards the end of 2019, MFIs in Assam were impacted due to CAA (Citizenship Amendment Act) protests in December 2019 and protests against the MFIs in November 2019– demanding a ban on MFIs holding them responsible for suicides.
- Internal surveys by Microfinance Institutions network (MFIN) suggest over-indebtedness in Assam (*link* , *link*) – 7% of customers have an o/s of >INR1lakh, compared to the national average of 3%.
- Bureau data suggests 22% portfolio (remains high) still in PAR 0-180 bucket in 3Q and 4Q20. The situation in Assam remains precarious and has been further impacted by the recent floods. Bandhan Bank (60% market share) in its 2Q21 commentary reported normalization in repayments in Assam though.

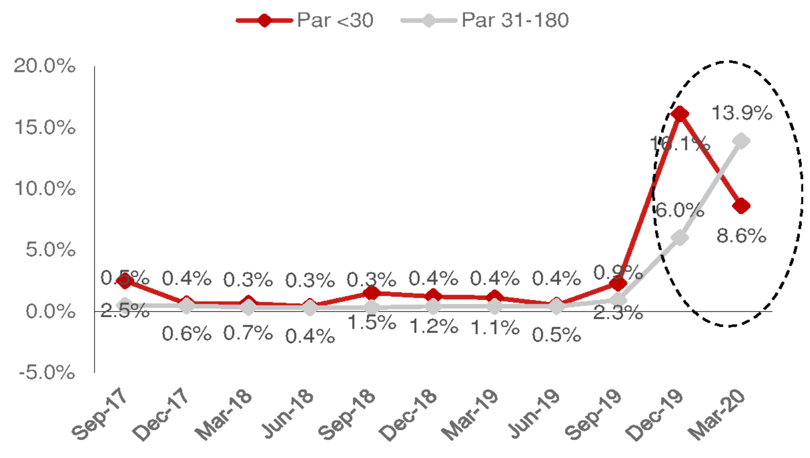
Fig. 97: Bandhan Bank's collection efficiency shows an improvement post the initial impact

OTR movement for 3Q20



Source: Company data, Nomura research

Fig. 98: Credit Bureau data still reflects high % of overdues – 22% portfolio in 0-180 day bucket as of March-2020



Source: CRIF Highmark, Nomura research

NOMURA

Global Markets Research

11 December 2020

CreditAccess Grameen CRDE.NS CREDAG IN

EQUITY: FINANCIALS

Tailor-made; initiating with a Buy rating

Ticking the right boxes; our TP of INR950 implies 24% upside

Action: Initiating at Buy with a TP of INR950, implying 24% upside

CREDAG is the largest NBFC-MFI in India with consolidated AUM (including Madura Microfinance) of INR112bn (as of Sep-20), implying an industry market share of >5% (16.3% within NBFC-MFI) and recorded a 52% AUM CAGR over FY14-20, with a strong presence in Karnataka, Maharashtra and Tamil Nadu (84% of AUMs). We believe CREDAG is best-positioned to capitalize on the rural opportunity (we estimate 21%/13% five-year CAGR in rural/ urban geographies for the industry) with: (1) its rural focus (86% of AUMs), (2) strong operational practices, (3) tailor-made approach, and (4) strong parentage aiding to record a 19% AUM CAGR over FY20-23F. While COVID does remain a near-term concern and resurgent cases in Maharashtra has led to lower collection efficiency for CREDAG (89% in Oct-20), we think standard provisions of 350bps of AUMs, robust PPOP/AUMs of 7% (FY21-23F average) as well as strong capital position (tier-1 of 25.6%) should not only aid CREDAG in absorbing the COVID impact but also benefit from the medium-term growth opportunity. We initiate coverage on CREDAG with a Buy rating and a TP of INR950.

- **Opportunity still large:** We expect the segment to deliver 18% CAGR over the next five years with faster growth in the rural segment at 21% CAGR, given the large penetration opportunity. We believe CREDAG is best-placed to capitalize on this opportunity with: (1) improving customer vintage-led ticket size growth (68% of borrowers with <3-year vintage), (2) improving branch productivity (~400 CREDAG branches set up over the past two years), and (3) growth opportunity in new geographies (44% of incremental branches beyond top-3 states in the past 3 years).
- **Ticking the right boxes:** CREDAG's customer-centric approach, calibrated branch expansion strategy with deeper penetration, prudent HR practices, strong parentage and prudent underwriting practices make it suited to scale up in this segment and gain dominance.

Valuation and our view; initiating with a Buy rating (24% implied upside)

- Current valuation at 2.3x FY23F book is not undemanding, but with large growth opportunity (19% CAGR over FY20-23F) and superior ROE profile (18% by FY23F), we believe the premium valuations will sustain. We value CREDAG based on residual income model at INR950, implying a 2.7x FY23F book multiple. Higher impact of COVID and concentration risks remain key risks.

Year-end 31 Mar	FY20	FY21F		FY22F		FY23F	
Currency (INR)	Actual	Old	New	Old	New	Old	New
PPOP (mn)	6,899		9,074		11,026		14,179
Reported net profit (mn)	3,275		3,314		6,189		8,848
Normalised net profit (mn)	3,275		3,314		6,189		8,848
FD normalised EPS	22.81		20.98		39.18		56.01
FD norm. EPS growth (%)	1.8		-8.0		86.7		43.0
FD normalised P/E (x)	33.6	–	36.6	–	19.6	–	13.7
Price/adj. book (x)	4.1	–	3.0	–	2.6	–	2.2
Price/book (x)	4.1	–	3.0	–	2.6	–	2.2
Dividend yield (%)	–	–	–	–	–	–	–
ROE (%)	13.0		9.9		14.3		17.5
ROA (%)	3.5		2.6		3.8		4.5

Source: Company data, Nomura estimates

Rating Starts at	**Buy**
Target price Starts at	**INR 950**
Closing price 09 December 2020	**INR 768**
Implied upside	**+23.7%**
Market Cap (USD mn)	1,622.5
ADT (USD mn)	1.2

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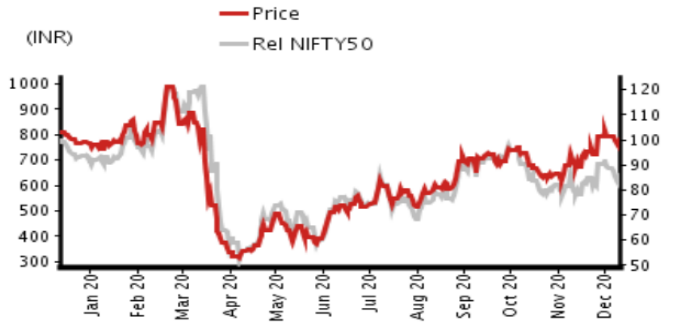
Key Data on CreditAccess Grameen

Relative Performance Chart



Performance

(%)	1M	3M	12M		
Absolute (INR)	6.2	17.6	-4.0	M cap (USDmn)	1,622.5
Absolute (USD)	7.0	17.6	-7.1	Free float (%)	20.0
Rel to NIFTY50	-2.4	-2.3	-17.3	3-mth ADT (USDmn)	1.2

Profit and loss (INRmn)

Year-end 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Interest income	12,183	16,172	23,531	28,094	35,010
Interest expense	-4,168	-5,727	-8,725	-10,001	-12,208
Net interest income	8,016	10,445	14,807	18,093	22,802
Net fees and commissions	9	38	44	44	55
Trading related profits	566	562	400	300	300
Other operating revenue	75	72	75	140	225
Non-interest income	650	672	519	484	580
Operating income	8,666	11,117	15,325	18,576	23,381
Depreciation	-78	-196	-275	-330	-379
Amortisation	0	0	0	0	0
Operating expenses	-1,001	-1,425	-1,931	-2,242	-2,641
Employee share expense	-1,861	-2,596	-4,045	-4,978	-6,182
Pre-provision op profit	5,726	6,899	9,074	11,026	14,179
Provisions for bad debt	-59	-106	-4,643	-2,752	-2,350
Other provision charges	-689	-2,284	0	0	0
Operating profit	4,977	4,509	4,431	8,274	11,829
Other non-op income					
Associates & JCEs					
Pre-tax profit	4,977	4,509	4,431	8,274	11,829
Income tax	-1,760	-1,234	-1,117	-2,085	-2,981
Net profit after tax	3,218	3,275	3,314	6,189	8,848
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	3,218	3,275	3,314	6,189	8,848
Extraordinary items					
Reported NPAT	3,218	3,275	3,314	6,189	8,848
Dividends					
Transfer to reserves	3,218	3,275	3,314	6,189	8,848

Growth (%)

Net interest income	30.3	41.8	22.2	26.0
Non-interest income	3.3	-22.8	-6.7	19.9
Non-interest expenses	42.4	35.5	16.1	17.8
Pre-provision earnings	20.5	31.5	21.5	28.6
Net profit	1.8	1.2	86.7	43.0
Normalised EPS	1.8	-8.0	86.7	43.0
Normalised FDEPS	1.8	-8.0	86.7	43.0
Loan growth	38.9	33.7	25.6	24.2
Interest earning assets	38.9	33.7	25.6	24.2
Interest bearing liabilities	60.7	29.9	23.7	23.3
Asset growth	44.9	33.9	20.7	21.5
Deposit growth	–	–	–	–

Source: Company data, Nomura estimates

Balance sheet (INRmn)

As at 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Cash and equivalents	6,156	5,804	10,689	9,620	10,582
Inter-bank lending	0	0	0	0	0
Deposits with central bank	0	0	0	0	0
Total securities	0	0	0	0	0
Other int earning assets	0	0	0	0	0
Gross loans	66,028	91,726	122,626	154,014	191,281
Less provisions	0	0	0	0	0
Net loans	66,028	91,726	122,626	154,014	191,281
Long-term investments	2	6,614	3,000	3,000	3,000
Fixed assets	271	895	5,569	5,517	5,414
Goodwill	0	0	0	0	0
Other intangible assets	0	0	0	0	0
Other non IEAs	3,836	5,485	6,069	6,373	6,691
Total assets	76,293	110,525	147,954	178,525	216,968
Customer deposits	0	0	0	0	0
Bank deposits, CDs, debentures	48,666	78,226	101,617	125,686	154,952
Other int bearing liabilities	0	0	0	0	0
Total int bearing liabilities	48,666	78,226	101,617	125,686	154,952
Non-int bearing liabilities	3,977	5,609	6,272	6,585	6,915
Total liabilities	52,643	83,834	107,889	132,271	161,867
Minority interest					
Common stock	1,436	1,440	1,580	1,580	1,580
Preferred stock					
Retained earnings	22,215	25,251	38,485	44,674	53,522
Reserves for credit losses					
Proposed dividends					
Other equity					
Shareholders' equity	23,651	26,691	40,065	46,254	55,102
Total liabilities and equity	76,293	110,525	147,954	178,525	216,968
Non-perf assets	335	1,421	4,416	3,962	2,952

Balance sheet ratios (%)

Loans to deposits	–	–	–	–	–
Equity to assets	31.0	24.1	27.1	25.9	25.4
Asset quality & capital					
NPAs/gross loans (%)	0.5	1.5	3.6	2.6	1.5
Bad debt charge/gross loans (%)	0.09	0.12	3.79	1.79	1.23
Loss reserves/assets (%)	0.00	0.00	0.00	0.00	0.00
Loss reserves/NPAs (%)	0.0	0.0	0.0	0.0	0.0
Tier 1 capital ratio (%)	–	–	–	–	–
Total capital ratio (%)	–	–	–	–	–
Per share					
Reported EPS (INR)	22.41	22.81	20.98	39.18	56.01
Norm EPS (INR)	22.41	22.81	20.98	39.18	56.01
FD norm EPS (INR)	22.41	22.81	20.98	39.18	56.01
DPS (INR)	0.00	0.00	0.00	0.00	0.00
PPOP PS (INR)	39.89	48.06	57.44	69.80	89.76
BVPS (INR)	164.76	185.37	253.62	292.80	348.81
ABVPS (INR)	164.76	185.37	253.62	292.80	348.81
NTAPS (INR)	164.76	185.37	253.62	292.80	348.81

Valuations and ratios

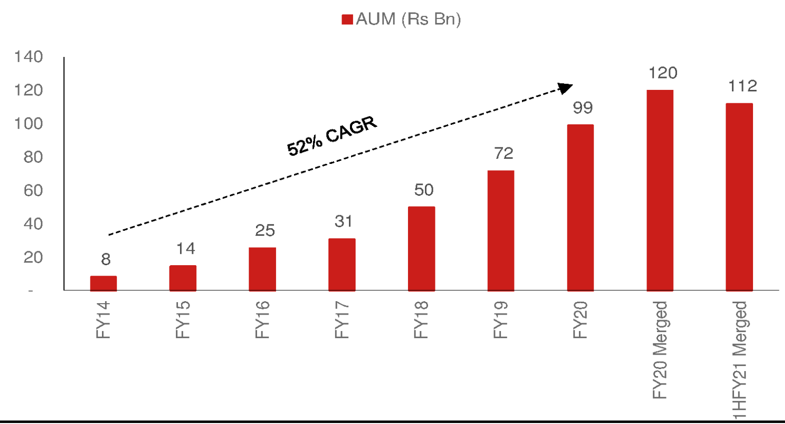
Reported P/E (x)	34.2	33.6	36.6	19.6	13.7
Normalised P/E (x)	34.2	33.6	36.6	19.6	13.7
FD normalised P/E (x)	34.2	33.6	36.6	19.6	13.7
Dividend yield (%)	–	–	–	–	–
Price/book (x)	4.7	4.1	3.0	2.6	2.2
Price/adjusted book (x)	4.7	4.1	3.0	2.6	2.2
Net interest margin (%)	–	13.24	13.82	13.08	13.21
Yield on assets (%)	–	20.50	21.96	20.31	20.28
Cost of int bearing liab (%)	–	9.03	9.70	8.80	8.70
Net interest spread (%)	–	11.48	12.25	11.51	11.58
Non-interest income (%)	7.5	6.0	3.4	2.6	2.5
Cost to income (%)	33.9	37.9	40.8	40.6	39.4
Effective tax rate (%)	35.4	27.4	25.2	25.2	25.2
Dividend payout (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	–	13.0	9.9	14.3	17.5
ROA (%)	–	3.51	2.56	3.79	4.47
Operating ROE (%)	–	17.9	13.3	19.2	23.3
Operating ROA (%)	–	4.83	3.43	5.07	5.98

Source: Company data, Nomura estimates

Largest and the best-placed NBFC-MFI

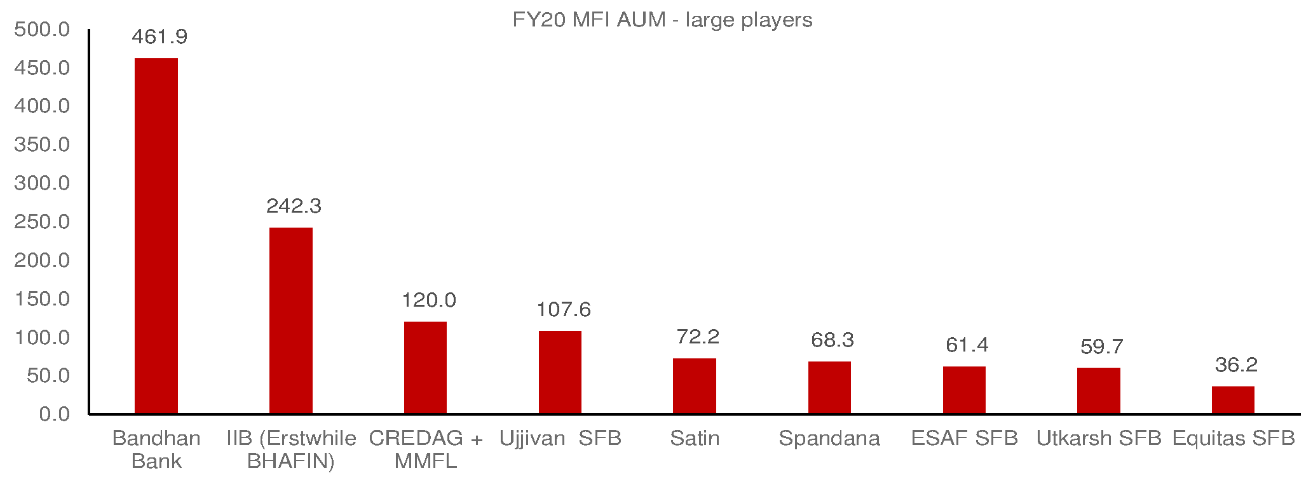
CREDAG is the largest NBFC-MFI in India with consolidated AUM (including Madura) of INR112bn, implying an industry market share of >5% (16.3% within NBFC-MFI) and recorded a 52% AUM CAGR over FY14-20, with a strong presence in Karnataka, Maharashtra and Tamil Nadu. These states currently form 84% of the consolidated AUM and 81% of the borrower count for CREDAG, while it has been making inroads into states like MP, Chhattisgarh and Odisha.

Fig. 99: CREDAG has delivered a strong 52% AUM CAGR over FY14-20



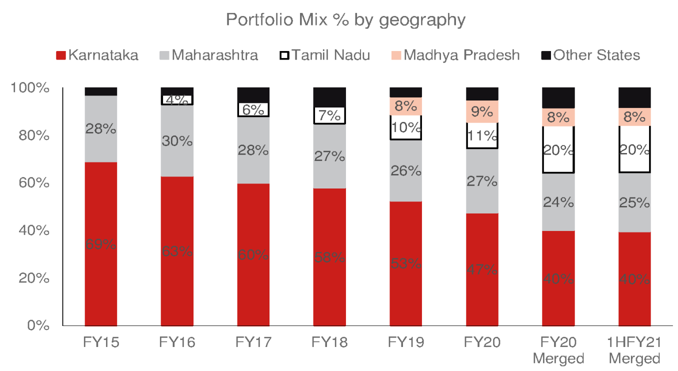
Source: Company data, Nomura research

Fig. 100: Top microfinance players by AUM INRbn



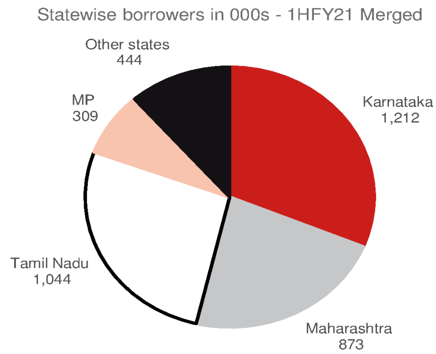
Source: Company data, Nomura research

Fig. 101: Portfolio mix by geography



Source: Company data, Nomura research

Fig. 102: State-wise borrowers in 000s - 1HFY21 Merged (4mn borrowers)



Source: Company data, Nomura research

Fig. 103: Strong market share gains for CREDAG over the past five years – >5% now

Top Player market share	AP crisis impact				Demonetisation impact				
	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Bandhan	12.6%	14.4%	15.2%	16.3%	18.2%	19.9%	20.4%	21.5%	19.9%
Equitas	2.5%	3.7%	3.7%	3.7%	3.9%	3.1%	1.7%	1.7%	1.6%
Ujjivan	2.4%	3.5%	3.8%	5.0%	5.5%	5.0%	4.7%	5.2%	4.6%
SKS/ BHAFIN	5.7%	7.7%	7.8%	7.1%	9.1%	8.5%	9.3%	9.7%	10.5%
CREDAG	**1.4%**	**1.9%**	**2.0%**	**2.5%**	**3.0%**	**2.9%**	**3.7%**	**4.0%**	**4.3%**
Spandana	9.2%	3.8%	2.2%	2.0%	1.4%	1.2%	2.3%	2.4%	2.9%
Madura	**0.5%**	**0.5%**	**0.6%**	**0.6%**	**0.6%**	**0.8%**	**0.9%**	**1.1%**	**0.9%**
Satin	1.1%	1.9%	2.6%	3.7%	3.9%	3.4%	3.2%	3.6%	3.1%
ESAF	1.0%	1.4%	1.5%	1.7%	2.3%	2.5%	2.5%	2.7%	2.7%
Fincare (Disha + Future)	0.8%	0.8%	0.9%	1.1%	1.1%	1.1%	1.3%	1.6%	1.8%
Jana	1.2%	3.1%	5.1%	6.4%	13.0%	11.9%	4.3%	3.1%	3.0%
North East			0.3%	0.4%	0.6%	0.6%	0.8%	0.8%	0.6%
Suryoday	0.3%	0.5%	0.8%	1.0%	1.2%	0.8%	1.1%	1.2%	1.2%
Utkarsh	0.3%	0.6%	0.8%	1.2%	1.7%	1.5%	2.0%	2.3%	2.6%
Share	7.1%	3.1%	2.1%	1.1%					
Top 7	**34.8%**	**36.7%**	**37.3%**	**40.2%**	**45.0%**	**44.0%**	**45.1%**	**48.1%**	**46.9%**
All SFBs	**8.3%**	**13.6%**	**16.9%**	**20.6%**	**29.3%**	**26.6%**	**18.4%**	**18.6%**	**18.1%**
Top 3 NBFC-MFIs (incl BHAFIN)	**8.1%**	**11.4%**	**12.4%**	**13.3%**	**15.9%**	**14.8%**	**16.1%**	**17.2%**	**17.8%**

Source: Company data, Nomura research

Fig. 104: State-wise (top-3 states for CREDAG accounting for 84% of the consolidated AUM) market share

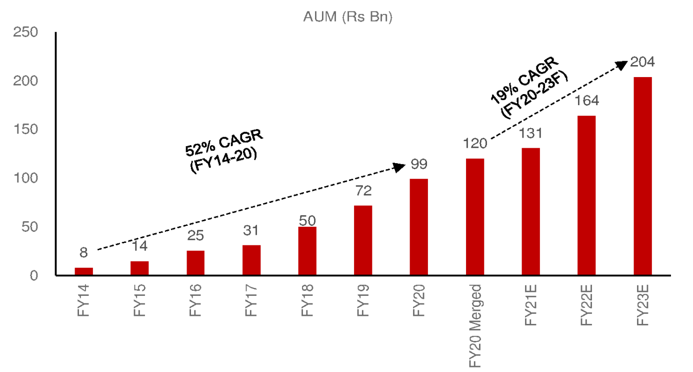
State wise Market Share %					
Maharashtra	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**
Bandhan	4.8%	5.3%	6.0%	6.6%	6.0%
Equitas	5.4%	4.2%	2.5%	2.6%	2.6%
Ujjivan	8.6%	7.0%	7.1%	6.5%	7.2%
SKS	11.6%	10.0%	11.1%	11.3%	12.4%
CREDAG	**9.4%**	**8.5%**	**11.9%**	**12.9%**	**15.9%**
Spandana	2.1%	1.7%	3.8%	3.3%	4.8%
Top players	**41.9%**	**36.8%**	**42.4%**	**43.3%**	**48.9%**
Tamil Nadu					
Bandhan	0.8%	0.8%	1.0%	1.0%	1.1%
Ujjivan	6.3%	5.5%	5.6%	6.9%	6.8%
CREDAG	**0.8%**	**1.1%**	**1.7%**	**2.7%**	**7.2%**
Top players	**24.4%**	**19.1%**	**14.5%**	**16.9%**	**21.0%**
Karnataka					
Bandhan	1.9%	2.1%	2.0%	2.0%	2.3%
Equitas	2.8%	2.3%	1.3%	1.9%	1.9%
Ujjivan	11.6%	9.3%	8.2%	8.7%	11.1%
SKS	13.5%	10.7%	10.9%	12.0%	14.0%
CREDAG	**19.8%**	**17.5%**	**22.2%**	**22.9%**	**24.6%**
Spandana	2.9%	2.2%	5.5%	3.6%	4.4%
Top players	**52.6%**	**44.1%**	**50.1%**	**51.1%**	**58.4%**

Source: Company data, Nomura research

- CREDAG recorded 52% AUM CAGR over FY14-20, with 34% CAGR in borrowers and 13% growth in ticket size leading to significant market share gain from 1.5%-2.0% in FY12-13 to >5% now (including Madura). Its growth delivery has been driven by 32% CAGR expansion in branch network. More importantly, 68% of borrowers are with <three-year vintage (or customer stickiness), 42% borrowers are new to credit and 45% of branches are with <two-year vintage (>400 branches set up), providing CREDAG enough runway for growth. We also analyze the key operational metrics for state-wise branches which gives us some direction of the business potential for the new branches. Newly set up branches with a vintage of 0-18 months (~20-25%) could expand branch AUMs up to 6-8x over the next three-five years while 18-36 month vintage branches (30-35%) could grow AUMs by 1.5-2x the current size. CREDAG's growth has been primarily driven by its focus on the rural segment which has improved from 64% of AUMs in FY14 to 82% in FY20 (86% for the merged entity).

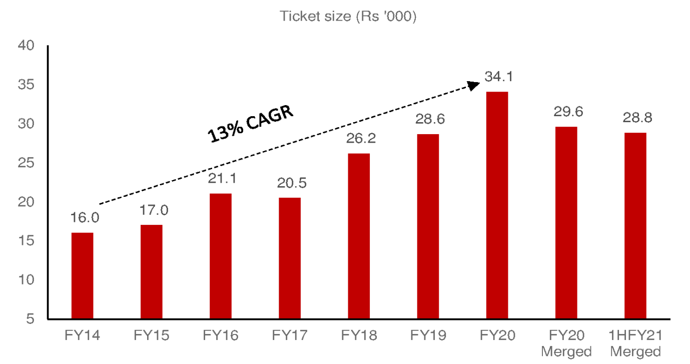
- We think CREDAG will be one of the key beneficiaries of the underlying trends with: (1) higher growth opportunity in the rural segment, (2) NBFC-MFIs gaining market share as banks/SFBs focus on diversifying their asset mix, and (3) acceleration in consolidation post COVID19-led crisis. With this, we expect CREDAG to record 19% CAGR in consolidated AUMs over FY20-23F. We expect growth to be further supported by: (1) improving customer vintage-led ticket size growth (68% of borrowers <three-year vintage), (2) improving branch productivity (~400 CREDAG branches set up over the past two years to mature), and (3) growth opportunity in new geographies (44% of incremental branches beyond top-3 states in the past three years).

Fig. 105: Strong 52% AUM CAGR over FY14-20...



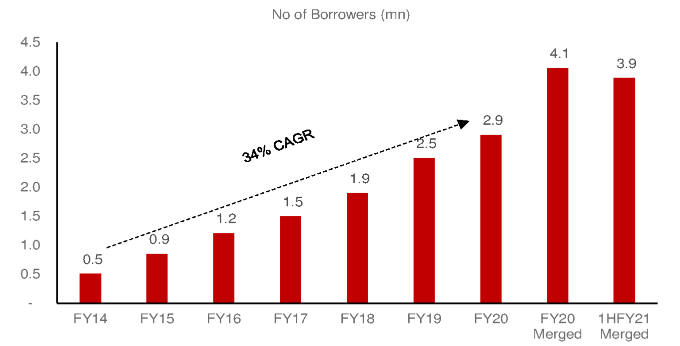
Source: Company data, Nomura estimates

Fig. 106: ...supported by 13% ticket size CAGR...



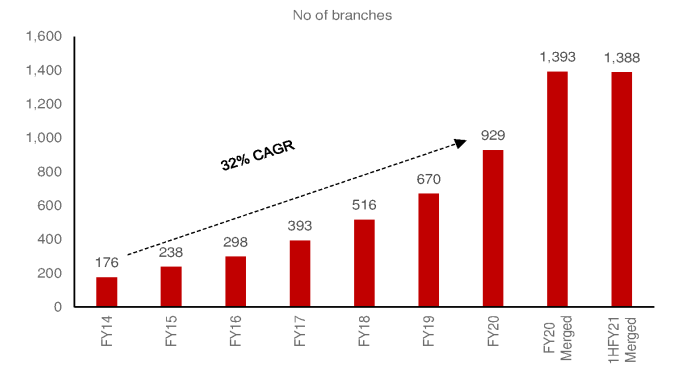
Source: Company data, Nomura research

Fig. 107: ...and a strong 34% CAGR in no. of borrowers



Source: Company data, Nomura research

Fig. 108: Branch network expansion at 32% CAGR has aided AUM growth



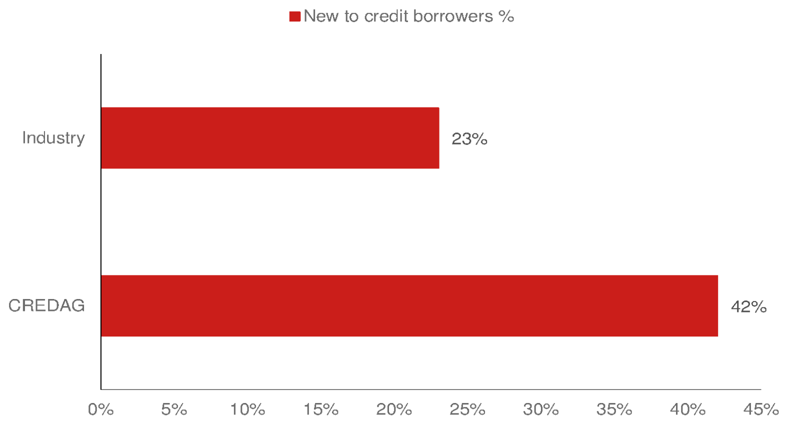
Source: Company data, Nomura research

Fig. 109: ~70% borrowers are <3 year old vintage

Borrower vintage	FY16	FY17	FY18	FY19	FY20
< 1 year	37%	27%	32%	33%	26%
1-3 years	42%	49%	37%	34%	42%
3-6 years	10%	15%	23%	25%	23%
6 years and above	10%	9%	8%	8%	9%
Borrower less than 3 year vintage	**79%**	**76%**	**69%**	**67%**	**68%**
Borrowers >3 year vintage	**20%**	**24%**	**31%**	**33%**	**32%**

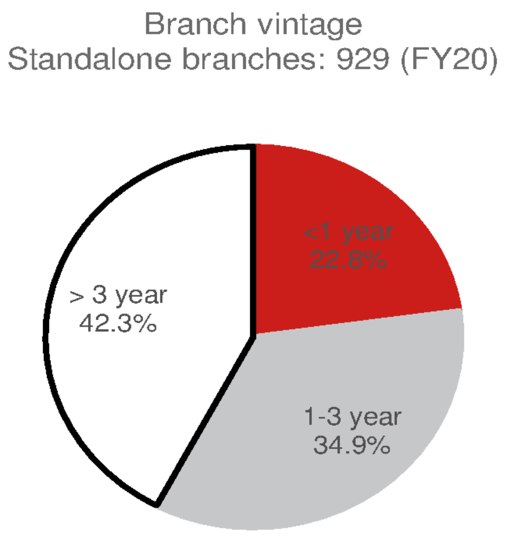
Source: Company data, Nomura research

Fig. 110: New to credit customers at 42% – better growth potential



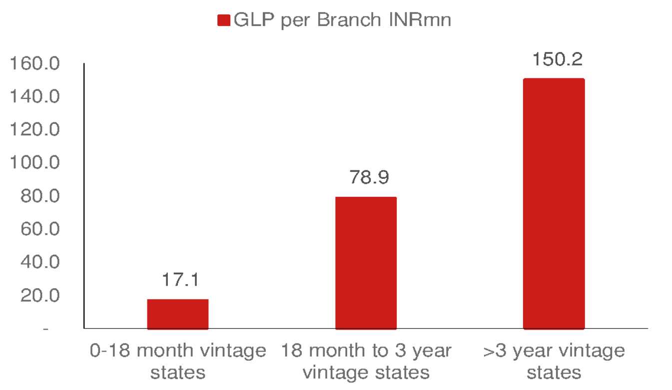
Source: Company data, Nomura research

Fig. 111: 45% of branches are <2yr vintage – better growth potential



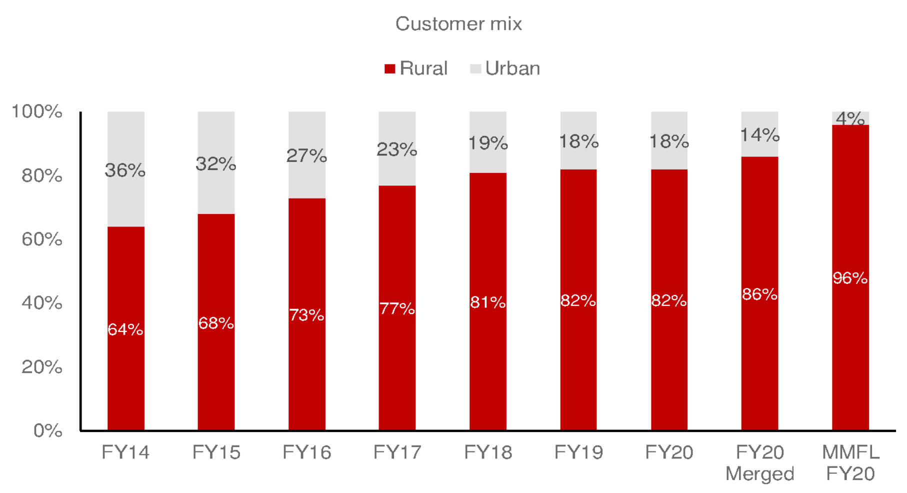
Source: Company data, Nomura estimates

Fig. 112: Branch productivity comparison by vintage



Source: Company data, Nomura estimates

Fig. 113: Rural focus has also aided growth for CREDAG

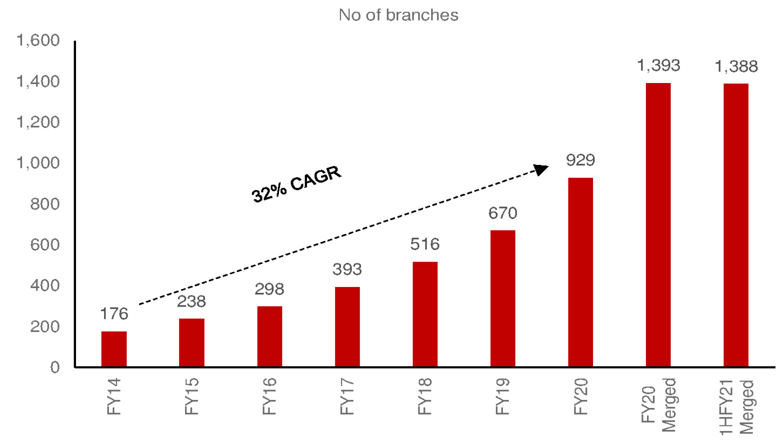


Source: Company data, Nomura research

Network expansion to provide further tailwinds

- CREDAG follows a contiguous expansion model and is very selective in entering new districts based on criteria like penetration, competitive landscape, bureau data, past asset quality experience, etc. While CREDAG is still concentrated in the top-3 states, 44% of incremental branch addition over the past three years has come from new geographies which will drive the necessary diversification, in our view. New geographies have contributed 18% of the incremental growth, recording 97% CAGR vs top-3 states recording 43% CAGR over FY17-20.

Fig. 114: Strong branch expansion over the past 2-3 years



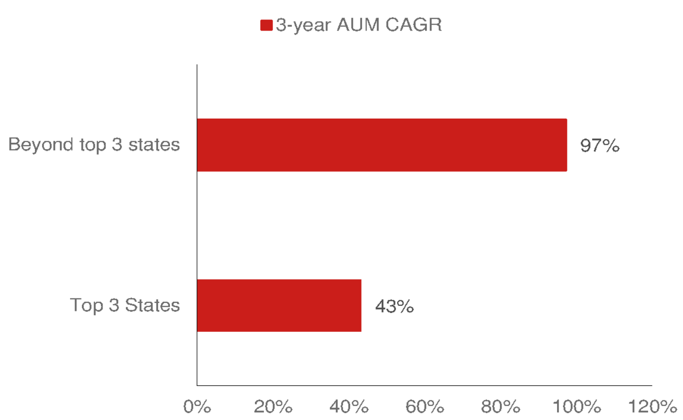
Source: Company data, Nomura research

Fig. 115: Incrementally branches have been opened beyond the top-3 states

									Incremental			Incremental mix (%)		
State-wise branches (In nos)	**FY14**	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**1HFY21**	**1yr**	**2yr**	**3yr**	**1yr**	**2yr**	**3yr**
Karnataka	117	139	145	165	191	237	269	269	32	78	104	15.1%	18.9%	19.4%
Maharashtra	54	84	102	122	144	198	222	222	24	78	100	11.3%	18.9%	18.7%
Tamil Nadu	5	7	17	37	80	116	131	131	15	51	94	7.1%	12.3%	17.5%
MP	-	6	29	53	63	93	115	115	22	52	62	**10.4%**	**12.6%**	**11.6%**
Chattisgarh		2	5	16	25	25	41	41	16	16	25	**7.5%**	**3.9%**	**4.7%**
Rest of India	-	-	-	-	13	48	151	151	103	138	151	**48.6%**	**33.4%**	**28.2%**
Total	**176**	**238**	**298**	**393**	**516**	**717**	**929**	**929**	**212**	**413**	**536**			
Branches in Top 3 States (%)	100%	96.6%	88.6%	82.4%	80.4%	76.8%	67.0%	67.0%	33.5%	50.1%	55.6%			
Branches beyond top 3 states (%)	0%	3.4%	11.4%	17.6%	19.6%	23.2%	33.0%	33.0%	66.5%	49.9%	44.4%			

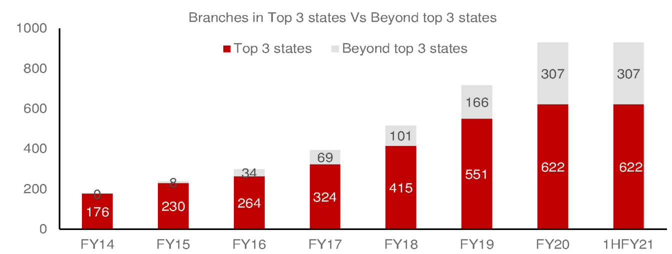
Source: Company data, Nomura research

Fig. 116: 3yr AUM CAGR – Top 3 states vs beyond top 3 states



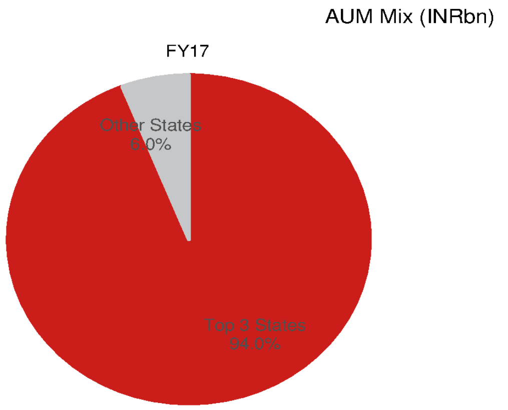
Source: Company data, Nomura research

Fig. 117: No. of branches: Top 3 states vs beyond top 3 states



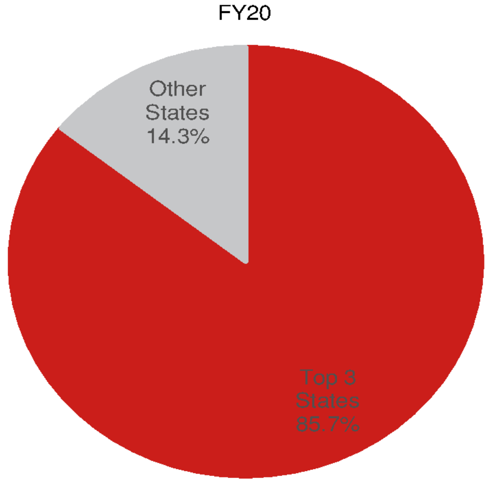
Source: Company data, Nomura research

Fig. 118: AUM concentration in Top-3 states has reduced from 94% as of FY17...



Source: Company data, Nomura research

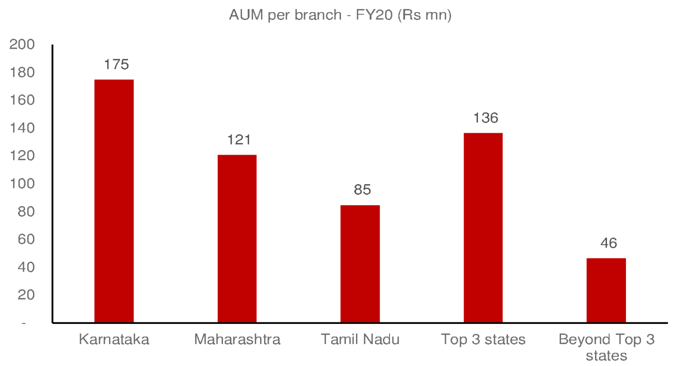
Fig. 119: ...to 85% as of FY20



Source: Company data, Nomura research

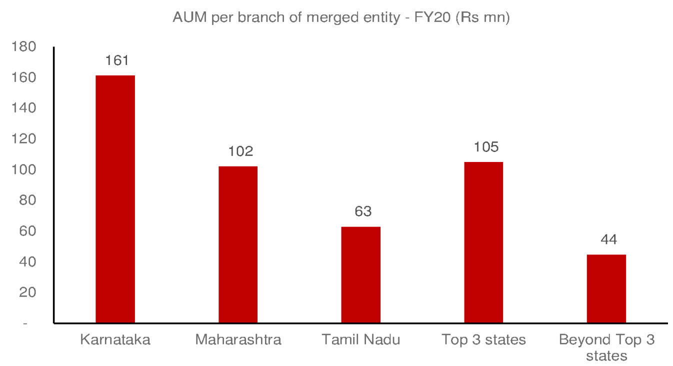
- We see tailwinds from new geographies where AUM/branch is meaningfully lower at INR46 vs INR136 of AUM/branch in top-3 states. As CREDAG continues to penetrate deeper in these new geographies and with branches maturing and borrower vintage improving, we think growth tailwind will remain strong for CREDAG over the medium-term.

Fig. 120: AUM per branch lower for newer states – should aid growth as scale improves



Source: Company data, Nomura research

Fig. 121: State-wise AUM per branch (merged entity)



Source: Company data, Nomura research

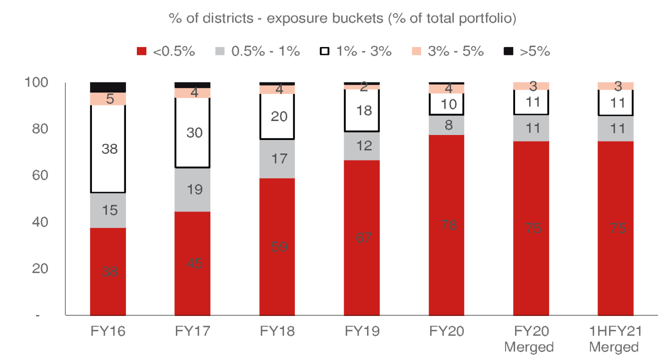
- Further, CREDAG has focused on minimizing concentration risks with diversification at a district level. While top-10 districts contribute only 24% of the consolidated AUM, CREDAG's portfolio is quite granular with >85% of districts having less than 1% AUM concentration.

Fig. 122: District level concentration low for CREDAG with +75% of AUM coming from below Top-10 states

District level portfolio concentration (In %)	FY16	FY17	FY18	FY19	FY20	FY20 Merged	1HFY21 Merged
Top 1	6	6	6	5	4	4	3
Top 3	17	15	15	13	12	10	9
Top 5	26	23	22	20	17	15	14
Top 10	41	37	36	32	29	24	24
Other (below Top-10)	59	63	64	68	71	76	76

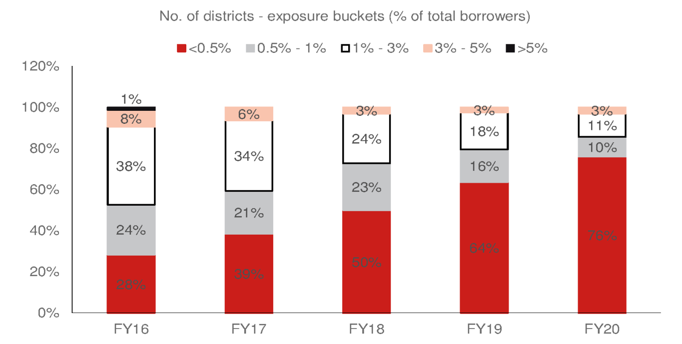
Source: Company data, Nomura research

Fig. 123: AUM concentration by districts



Source: Company data, Nomura research

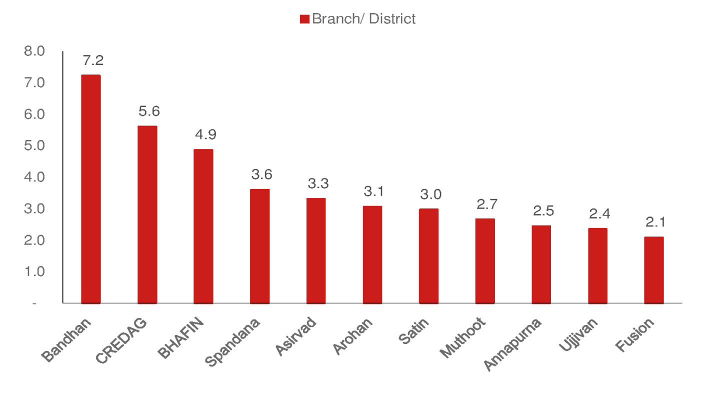
Fig. 124: Borrower concentration by districts



Source: Company data, Nomura research

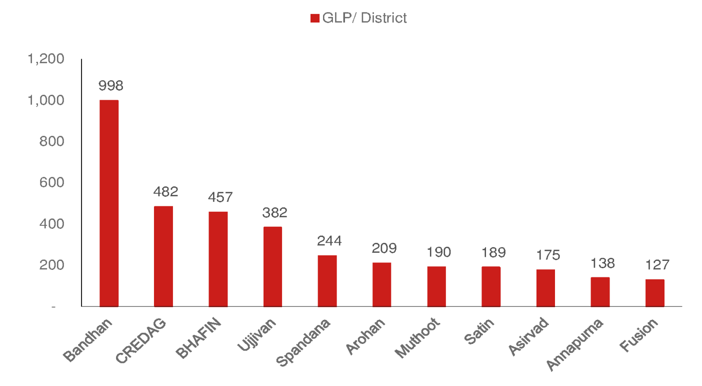
- CREDAG's number of branches / district is also high at 5.6/district compared to other players at 2-3 branches/ district, leading to higher gross loan portfolio (GLP) / district at ~INR480mn vs peers at ~INR200-250mn.

Fig. 125: CREDAG has higher branches per district vs peers...



Source: Company data, Nomura research

Fig. 126: ...leading to better GLP per district



Source: Company data, Nomura research

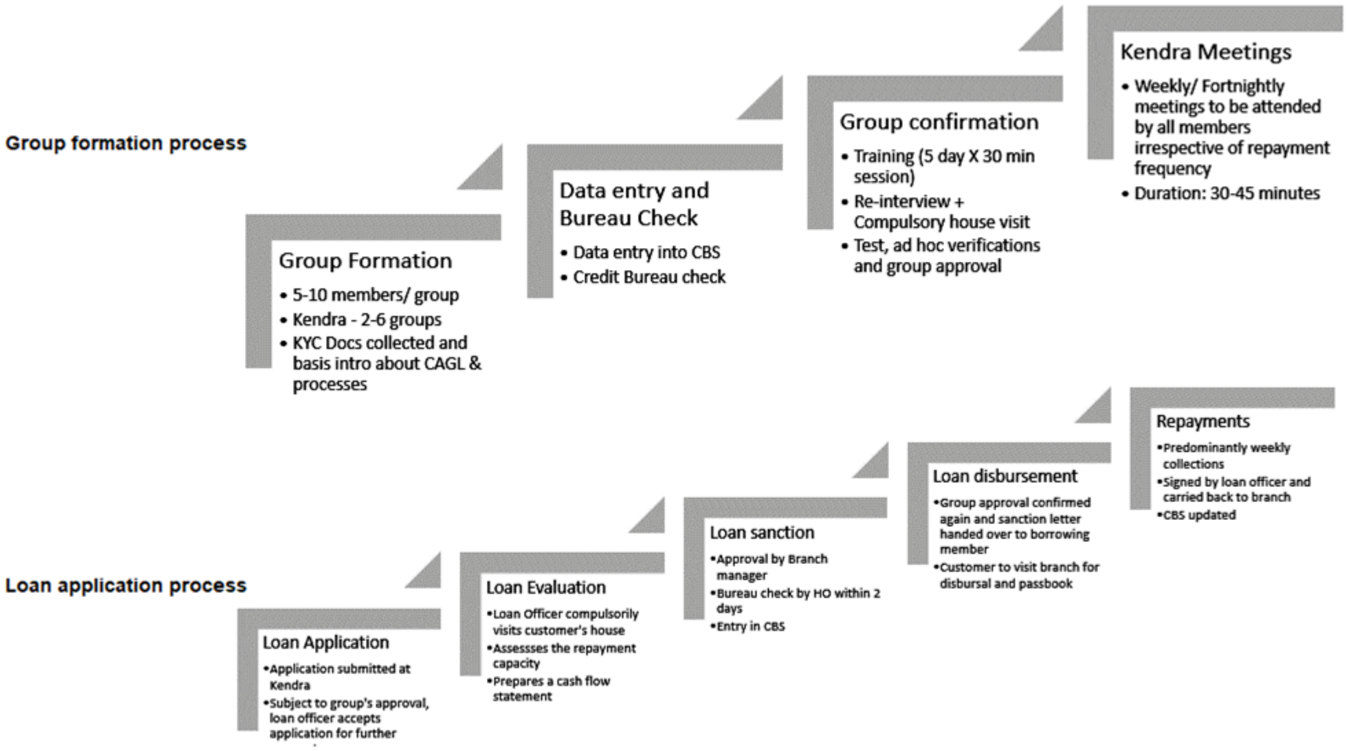
Tailor-made approach

- One of the most important success factors, in our view, for CREDAG is its tailor-made customized approach to cater to its customers and the company does not follow a one-size-fits-all approach.
- This has enabled CREDAG to capture market potential by enhancing the customer proposition in a much better fashion without diluting its operational and underwriting discipline.
- Customized offering has led to best-in-class customer retention, higher credit need fulfilment for customers and better monetization of life cycle value of a customer.

Superior product proposition – retail loans to support sustainable growth:

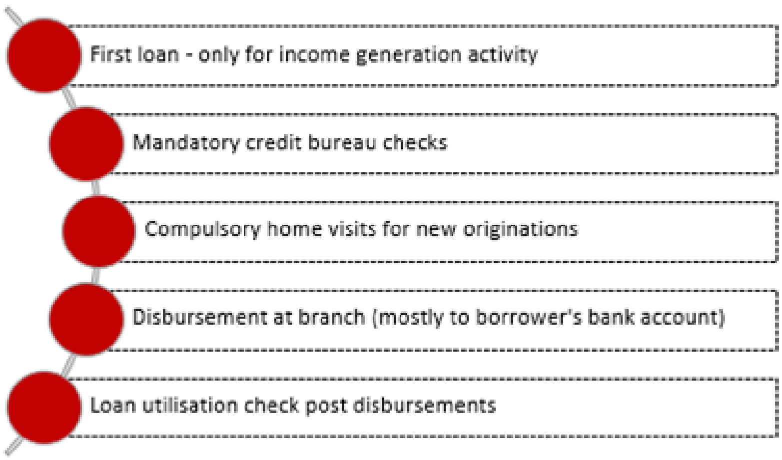
- CREDAG does capture the life cycle of a borrower much better than its peers by offering multiple products to its microfinance customers, ranging from pure MFI loans, home improvement loans, education loans, family welfare loans, etc. It sets limits per borrowers based on existing leverage and income profile for each borrower and offers a much more customized loan size, loan tenure and repayment frequency for each borrower (even in the same group).

Fig. 127: Brief Joint liability group (JLG) based lending process



Source: Company data, Nomura research

Fig. 128: Checks and balances



Source: Company data, Nomura research

- It also offers retail loans by moving its existing MFI customers (who have completed > three years with CREDAG) outside of the JLG model. While this forms >5% of the AUMs currently, it only forms 3% of its customer base. We see individual loans to be a large growth opportunity for the next decade with ~9% customers with >6-year vintage. Over the next decade, we see a INR1.5-3tn opportunity in this segment by FY25F/30F– CREDAG has 32% of its 2.9mn borrowers with a vintage of >3-year currently and looks well-placed to leverage this opportunity.

Fig. 129: Individual lending opportunity – 32% borrowers with >3y ear vintage

Borrower vintage	FY16	FY17	FY18	FY19	FY20
< 1 year	37%	27%	32%	33%	26%
1-3 years	42%	49%	37%	34%	42%
3-6 years	10%	15%	23%	25%	23%
6 years and above	10%	9%	8%	8%	9%
Borrower less than 3 year vintage	**79%**	**76%**	**69%**	**67%**	**68%**
Borrowers >3 year vintage	**20%**	**24%**	**31%**	**33%**	**32%**

Source: Company data, Nomura research

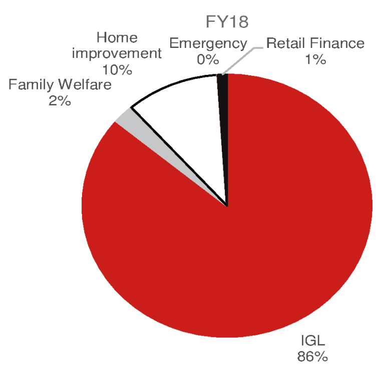
- While group loans still form 95% of AUMs, its retail loans have grown at a much faster pace of 213% CAGR over the past two years vs MFI group loans which have recorded 38% CAGR. We expect retail loans to grow faster at 45% CAGR over FY21-23F once the merger with Madura materializes vs. an overall loan growth of 25% and group loan growth at 24%.

Fig. 130: Product suite

Loan Type	Product	Purpose	Ticket Size (INR)	Tenure (months)	AUM FY20 INRmn	Aum Mix (%)	FY18-20 CAGR
Group	Income Generation Loan(IGL)	Business Investments and Income Enhancement activities	INR5,000 - INR80,000	12-24 mths	84,473	85.4%	40.4%
	Home Improvement Loans	Water Connections, Sanitation and Home Improvement & Extensions	INR5,000 - INR50,000	12-48 mths	7,696	7.8%	21.7%
	Family Welfare Loans	Festival, Medical, Education and Livelihood Improvement	INR1,000 - INR15,000	3-12 mths	1,678	1.7%	19.7%
	Special Situation Loans	Emergencies	INR2,000	6 mths	-	-	
	Emergency Loans	Emergencies	INR1,000	3 mths	125	0.1%	138.4%
Individual	Retail Finance Loans	Purchase of inventory, machine, assets or for making capital investment in business or business expansion	Up to INR5,00,000	6-60 mths	**4,991**	**5.0%**	**211.9%**

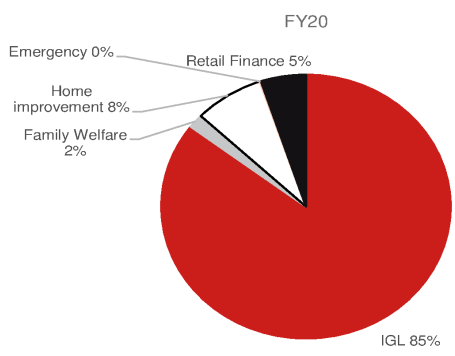
Source: Company data, Nomura research

Fig. 131: Product mix – FY18



Source: Company data, Nomura research

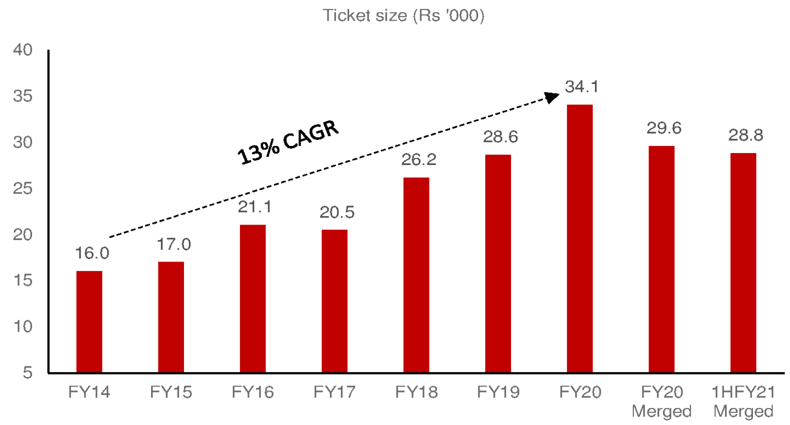
Fig. 132: Product mix – FY20



Source: Company data, Nomura research

- Further, CREDAG offers these loans on a need-basis (within overall sanction limit) and not restricted on the basis of the loan cycle for the group. With a diversified loan offering, CREDAG has been able to maintain a much better average loans outstanding per borrower as compared to its peers despite similar/ lower disbursement ticket size, thereby monetizing its customer life cycle much better than peers and also improving customer retention.

Fig. 133: Average loans per customer higher for CREDAG vs peers due to more customi zed offering

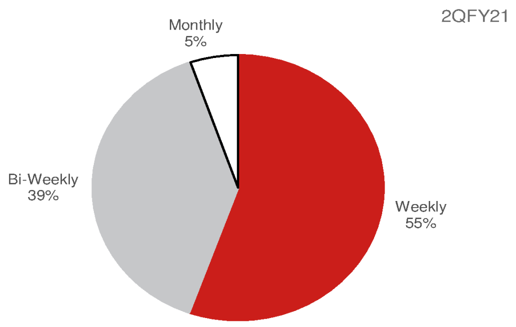


Source: Company data, Nomura research

Flexible repayment – a much more customer-focused approach:

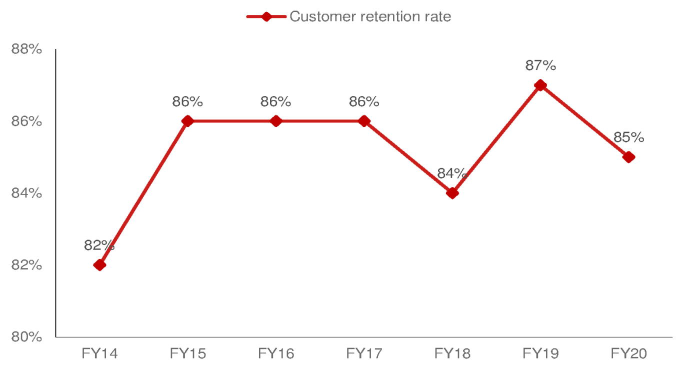
- With most MFIs focusing on maximizing profitability through cost efficiencies, we see customer needs getting ignored and ultimately also not leading to any sustainable cost benefit for MFI players.
- CREDAG follows a multi frequency collection model with 55% weekly, 39% fortnightly and 5% monthly collection, based on its customer cashflow and convenience rather than just focusing on cost optimization. That said, CREDAG does conduct weekly centre meetings which ensure a much better connectivity and connect with its customers even if they are on a monthly/fortnightly repayment frequency.
- This customer-focused, tailor-made solutions have helped CREDAG to maintain a much higher customer retention rate at 85% vs industry average of 78% (as of Sep-17) and capture the lifecycle of borrowers much better than peers. This has also helped CREDAG deliver well on asset quality in the past cycles.

Fig. 134: CREDAG offers re-payment flexibility to customers



Source: Company data, Nomura research

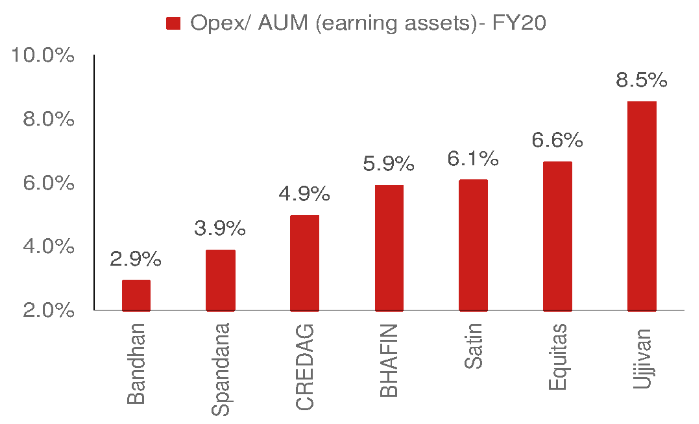
Fig. 135: More customized offerings lead to better customer retention



Source: Company data, Nomura research

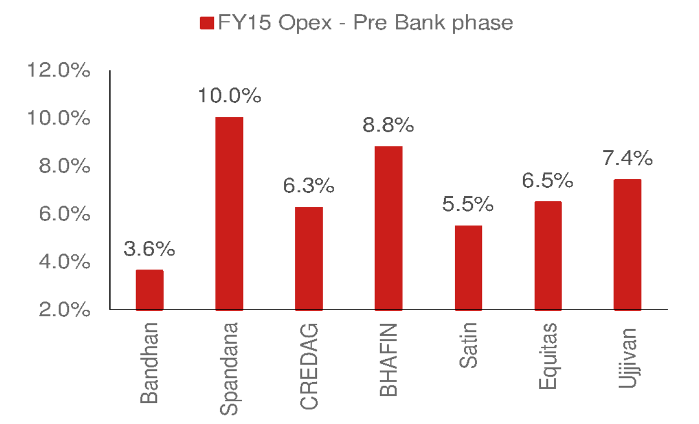
- More importantly, despite its focus on the rural segment (82% of AUMs) and weekly collection mod el (55% of AUMs) , we have not seen a meaningful gap in cost efficiencies with opex/AUMs at 6.3% (FY15) vs 6.5-7.4% (FY15 – pre-bank phase) for small finance banks (SFBs) with monthly collection model and also at 4.9% (FY20) vs . peers like Satin/BHAFIN with opex/AUMs of 6.1% (FY20)/ 5.9% (FY19), respectively.

Fig. 136: Opex / AUM – FY20



Note: BHAFIN data for FY19
Source: Company data, Nomura research

Fig. 137: Opex / AUM – FY15

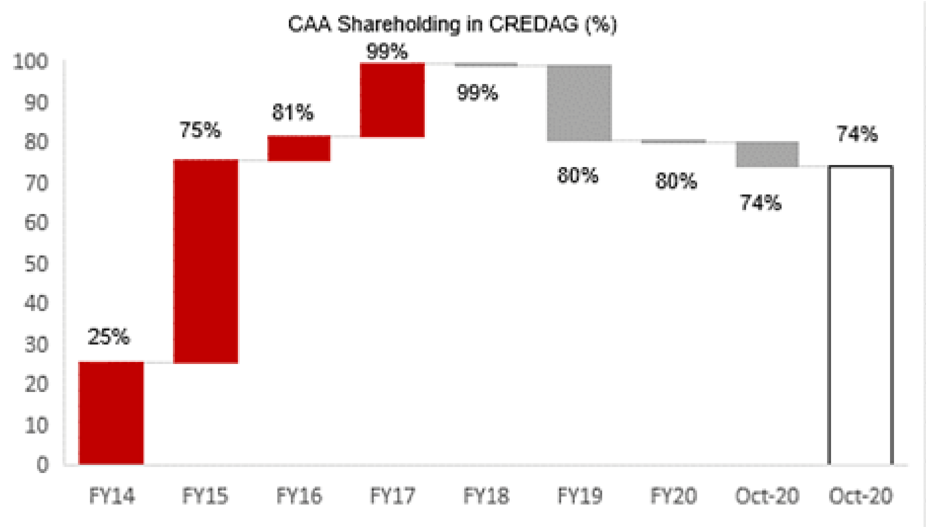


Source: Company data, Nomura research

Strong parentage – funding constraints meaningfully lower

- CREDAG is promoted by "Credit Access Asia" which is a professionally managed company and specializes in micro financing. It has its operations in India – through CREDAG (since 2010), the Philippines – through Credit Access – Philippines (since 2014), Indonesia – through PT Bina Artha Ventura (since 2012) and Vietnam through CreditAccess Vietnam. CAA is focused on the MFI sector across Asia with India contributing 91% of AUMs (FY19) for them.
- Its investor base includes Olympus Capital Asia (US PE firm, focusing on mid-cap Asian companies), holding 17% and Asian Development Bank holding 9%. The initial shareholders were a large group of family offices and HNIs, and still represent around 50% of the share capital.
- While we think funding remains one of the key risks in the sector and converting into a bank does help in mitigating this risks meaningfully, having such a strong promoter backing does address large part of our concern on the longer term funding challenges as well.
- Unlike a PE investor with a specific time horizon, CAA acts as a promoter which ensures CREDAG to deliver longer term sustainable business in a disciplined way. It further supports CREDAG in both equity and debt needs in times of stress and opens up opportunity to tap foreign funding.
- Such strong promoter backing has helped in the past when CAA invested €20.5mn via equity and €20.5mn via Compulsory Convertible Debenture into CREDAG during demonetization period which helped CREDAG navigate the cycle without any funding challenges.

Fig. 138: CAA shareholding in CREDAG



Source: Company data, Nomura research

Well-diversified funding avenues and well-matched ALM

- MFIs have a relatively shorter tenure loan book (12-24 months) and thus usually have a well-matched ALM compared to longer-duration lenders like mortgage, vehicle, etc. CREDAG focuses on a diversified funding profile, both in terms of duration and funding source. CREDAG also aims at leveraging its strong parentage in raising money from foreign sources. CREDAG's liabilities are well diversified on duration basis with 21% of the liabilities having >3-year duration, 63% having 1-3 year duration and 16% <1 year as of 2QFY21. Funding sources are also quite diversified with banks contributing 61%, financial institutions and NBFCs contributing ~24%, 10% from foreign sources and 6% by means of assignment.

Operationally most prudent – sticking to basics

- We see operational discipline to be the single-most critical metric on which MFIs need to be evaluated and remains one of the key determinant in making a strong and a sustainable business model. With growth opportunity being abundant, we have seen failures in the MFI space driven by operational lapses either by chasing growth aggressively, lack of confidence in the business or poor customer connect.
- We see CREDAG ticking most of the right boxes here with: (1) calibrated expansion without diluting its market understanding and strength, (2) relentless focus on maintaining strong customer connect, (3) customer-centric approach, (4) prudent underwriting practices and superior risk management framework, and (5) alignment of employee interests.

Calibrated expansion without diluting its market understanding and strength

- CREDAG follows a calibrated network expansion strategy, expanding into neighboring geographies which ensures a much better market understanding, availability of human capital and better connect with its customers.
- CREDAG has expanded its branch network by 32% CAGR over FY14-20 with a borrower CAGR of 34% and has been able to reduce its concentration risks from 94% contribution from top-3 states to 85% now and further to 84% with the merger of Madura. With Madura acquisition and 44% of incremental branches opened in new geographies over the past three years, we think concentration risks will dilute further over the medium term as new branches mature.
- Further, as discussed earlier, we think there is some merit in maintaining some concentration as well which CREDAG rightfully balances well by diversifying its district exposures.

Fig. 139: Incrementally new branch additions have been beyond top-3 states

State-wise branches (In nos)	FY14	FY15	FY16	FY17	FY18	FY19	FY20	1HFY21	Incremental 1yr	Incremental 2yr	Incremental 3yr	Incremental mix (%) 1yr	Incremental mix (%) 2yr	Incremental mix (%) 3yr
Karnataka	117	139	145	165	191	237	269	269	32	78	104	15.1%	18.9%	19.4%
Maharashtra	54	84	102	122	144	198	222	222	24	78	100	11.3%	18.9%	18.7%
Tamil Nadu	5	7	17	37	80	116	131	131	15	51	94	7.1%	12.3%	17.5%
MP	-	6	29	53	63	93	115	115	22	52	62	**10.4%**	**12.6%**	**11.6%**
Chattisgarh		2	5	16	25	25	41	41	16	16	25	**7.5%**	**3.9%**	**4.7%**
Rest of India	-	-	-	-	13	48	151	151	103	138	151	**48.6%**	**33.4%**	**28.2%**
Total	**176**	**238**	**298**	**393**	**516**	**717**	**929**	**929**	**212**	**413**	**536**			
Branches in Top 3 States (%)	100%	96.6%	88.6%	82.4%	80.4%	76.8%	67.0%	67.0%	33.5%	50.1%	55.6%			
Branches beyond top 3 states (%)	0%	3.4%	11.4%	17.6%	19.6%	23.2%	33.0%	33.0%	66.5%	49.9%	44.4%			

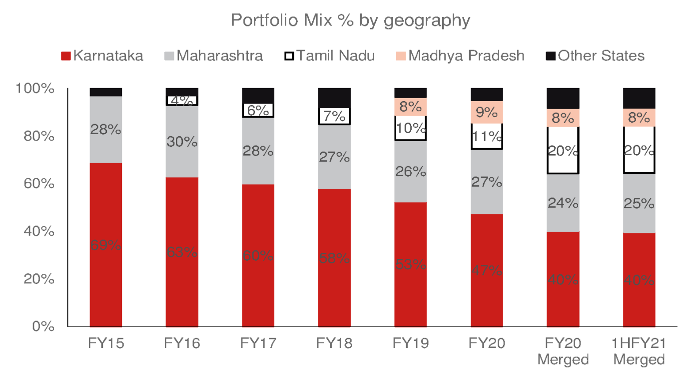
Source: Company data, Nomura research

Fig. 140: Beyond top-3 states , the mix of AUM has increased from 6% to 16% over FY17-20

Portfolio by states (INRmn)	FY15	FY16	FY17	FY18	FY19	FY20	Merged FY20	Merged 1HFY21	Incremental FY15-20	Incremental FY17-20	Growth FY15-20	Growth FY17-20
Karnataka	10,067	16,073	18,303	28,892	37,624	46,973	48,020	44,280	36,906	28,670	36.1%	36.9%
Maharashtra	4,008	7,540	8,760	13,296	18,451	26,761	28,970	27,720	22,753	18,001	46.2%	45.1%
Tamil Nadu	395	925	1,924	3,389	7,465	11,070	23,890	22,200	10,675	9,146	94.8%	79.2%
Rest of India	-	762	1,845	3,980	7,875	14,156	19,080	17,630	14,156	12,311		97.2%
Total	**14,470**	**25,300**	**30,832**	**49,557**	**71,415**	**98,960**	**1,19,960**	**1,11,830**	**84,490**	**68,128**	**46.9%**	**47.5%**
Aum mix by state (%)												
Karnataka	69.6%	63.5%	59.4%	58.3%	52.7%	47.5%	40.0%	39.6%	43.7%	42.1%		
Maharashtra	27.7%	29.8%	28.4%	26.8%	25.8%	27.0%	24.1%	24.8%	26.9%	26.4%		
Tamil Nadu	2.7%	3.7%	6.2%	6.8%	10.5%	11.2%	19.9%	19.9%	12.6%	13.4%		
Rest of India	0.0%	3.0%	6.0%	8.0%	11.0%	14.3%	15.9%	15.8%	16.8%	18.1%		
AUM												
Top 3 States	14,470	24,538	28,987	45,577	63,540	84,804	1,00,880	94,200	70,334	55,817	42.4%	43.0%
Other States	-	762	1,845	3,980	7,875	14,156	19,080	17,630	14,156	12,311	107.6%	97.2%

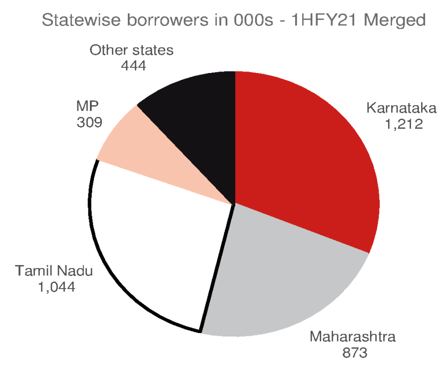
Source: Company data, Nomura research

Fig. 141: Portfolio mix by geography



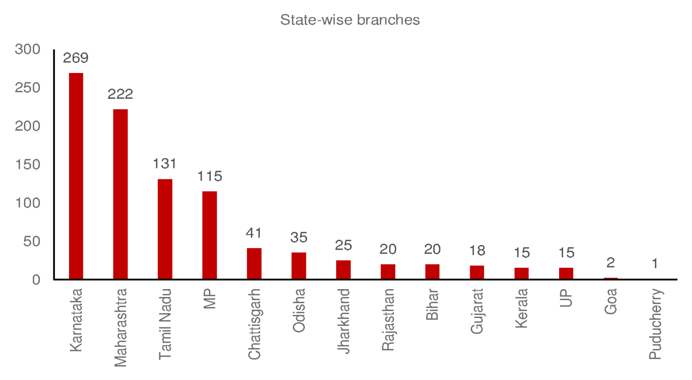
Source: Company data, Nomura research

Fig. 142: Borrower mix by states



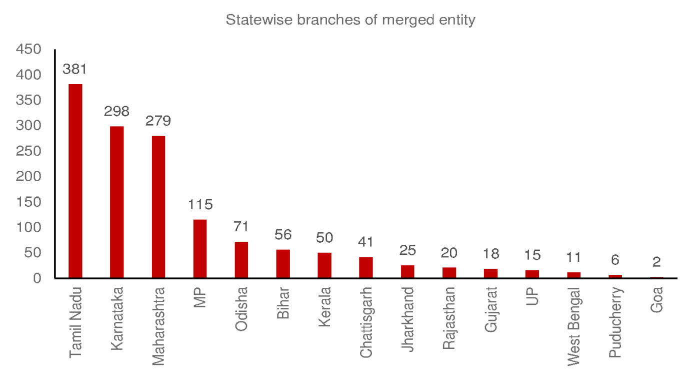
Source: Company data, Nomura research

Fig. 143: State-wise branches (1HFY21)



Source: Company data, Nomura research

Fig. 144: State-wise branches of merged entity (1HFY21)



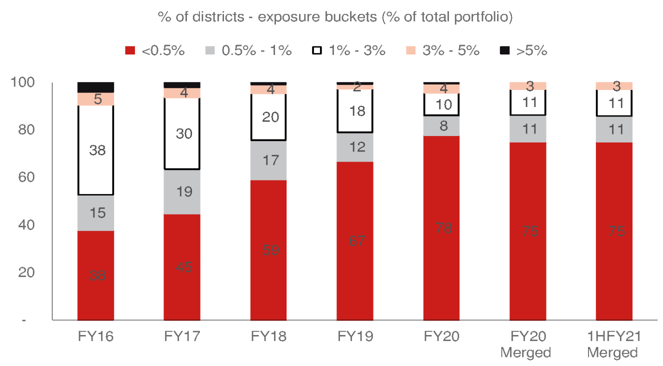
Source: Company data, Nomura research

Fig. 145: District -level concentration low for CREDAG with +75% of AUM coming from below Top-10 states

District level portfolio concentration (In %)	FY16	FY17	FY18	FY19	FY20	FY20 Merged	1HFY21 Merged
Top 1	6	6	6	5	4	4	3
Top 3	17	15	15	13	12	10	9
Top 5	26	23	22	20	17	15	14
Top 10	41	37	36	32	29	24	24
Other (below Top-10)	59	63	64	68	71	76	76

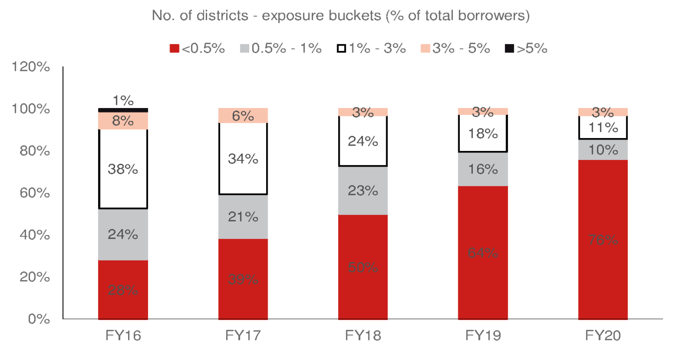
Source: Company data, Nomura research

Fig. 146: AUM concentration by districts



Source: Company data, Nomura research

Fig. 147: Borrower concentration by districts

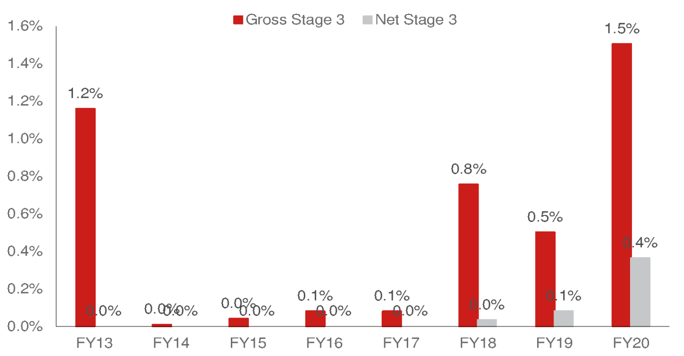


Source: Company data, Nomura research

Strong focus on maintaining solid customer connect

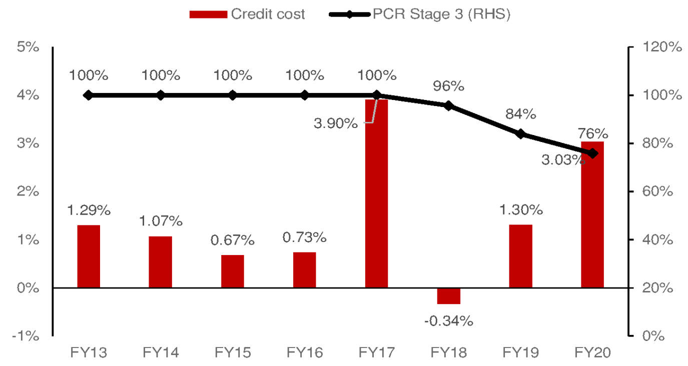
- CREDAG does provide flexibility in repayment options to suite its customer needs while irrespective of payment frequency, it conducts its centre meetings on a weekly basis. This not only aids in developing and maintaining better customer connect but also helps in delivering better asset quality. While this does increase costs for CREDAG, it also helps in lowering through-cycle credit costs. CREDAG has consistently delivered lower credit costs vs the industry. This superior performance has been maintained even during events like demonetization and even for the impacted districts.

Fig. 148: Strong asset quality trends...



Note: Stage 3 is 60+dpd starting FY19
Source: Company data, Nomura research

Fig. 149: ...leading to lower credit cost



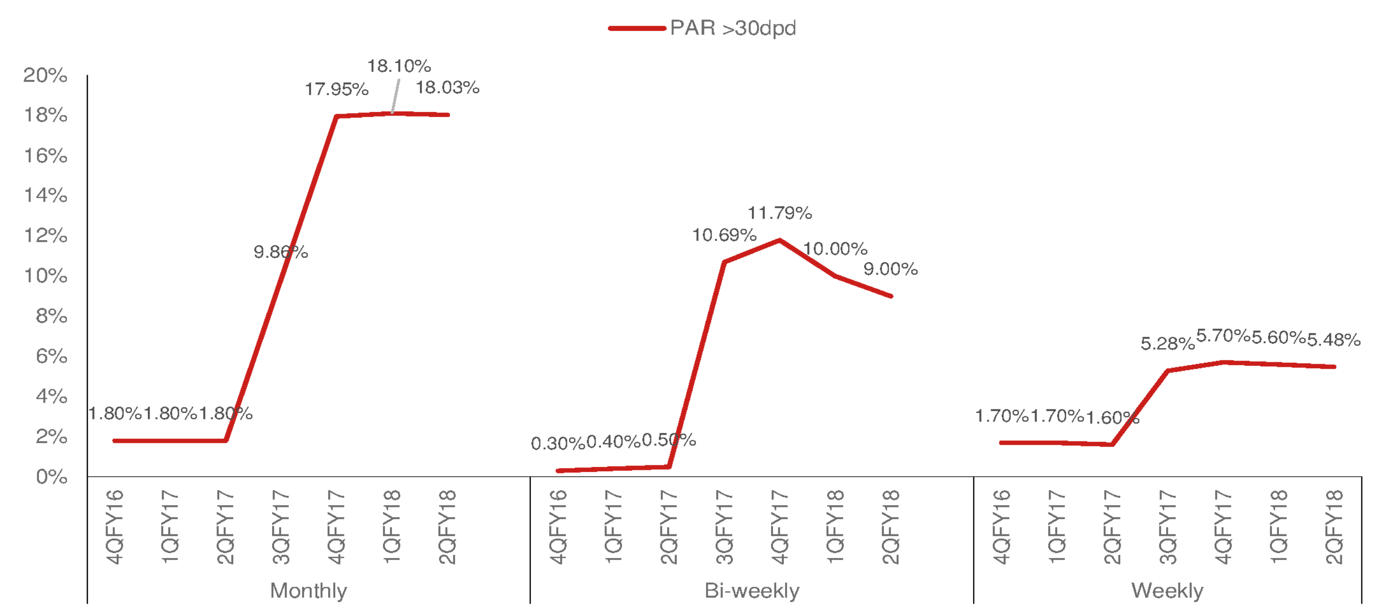
Source: Company data, Nomura research

Fig. 150: CREDAG has consistently delivered lower credit cost vs peers

Credit cost %	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Credit Access	-0.6%	1.3%	1.1%	0.7%	0.7%	3.9%	-0.3%	1.3%	3.0%
Spandana		68.1%	0.5%	0.5%	0.9%	3.3%	1.7%	1.2%	4.9%
BHAFIN	52.1%	20.1%	0.9%	0.4%	1.0%	5.9%	1.1%	0.8%	
Satin	0.3%	0.5%	1.1%	0.6%	0.6%	1.5%	1.0%	0.9%	2.8%
Bandhan						0.5%	1.4%	2.2%	2.6%
Ujjivan	0.9%	0.8%	0.6%	0.9%	0.6%	1.3%	4.5%	0.4%	1.4%
Equitas	0.8%	0.8%	0.9%	1.6%	1.2%	1.6%	2.2%	0.9%	1.8%
Top 7 MFI lenders - credit cost	**13.5%**	**17.9%**	**0.9%**	**0.8%**	**0.9%**	**2.0%**	**1.6%**	**1.4%**	**2.5%**

Source: Company data, Nomura research

Fig. 151: Weekly collection model has had superior asset quality outcomes

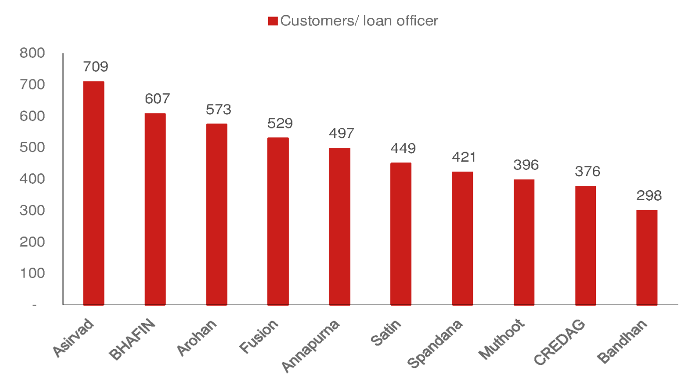


Source: Company data, Nomura research

Customer-centric approach

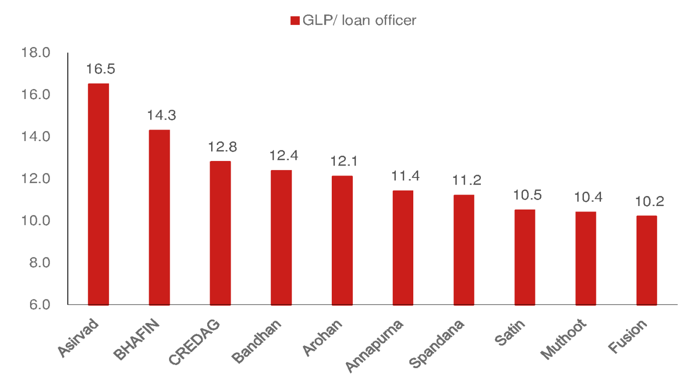
- CREDAG's uniqueness comes from its customer-centric approach where it has found a fine balance by placing customer needs at the centre (flexible repayment options, multiple product offering and flexible loan offerings) while not diluting its operational standards, risk management practices and ensuring a favourable work environment for its employees. This has helped CREDAG to achieve better productivity despite higher operational costs while maintaining better asset quality. While CREDAG does operate at a much low er borrower per loan officer ratio vs peers due to the weekly collection model, its opex/AUM has been comparable or better than peers due to better customer and employee retenti on, better AUM outstanding per customer and lower employee cost.

Fig. 152: Borrowers / loan officer lower for CREDAG due to the high touch model



Source: Company data, Nomura research

Fig. 153: More flexible offerings still lead to higher AUM/ loan officer

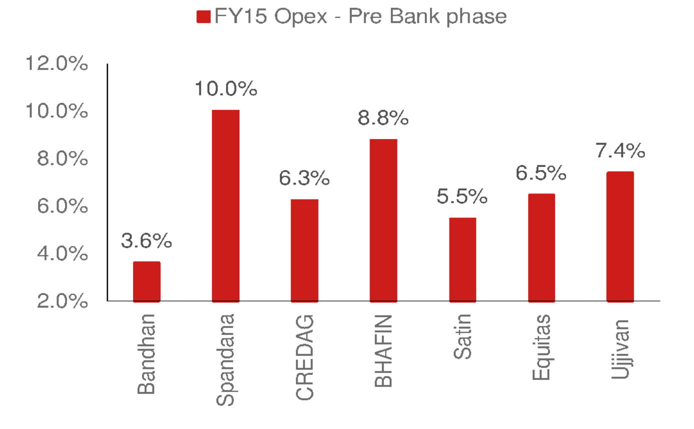


Source: Company data, Nomura research

Operational efficiency without diluting operational standards - benchmarking CREDAG

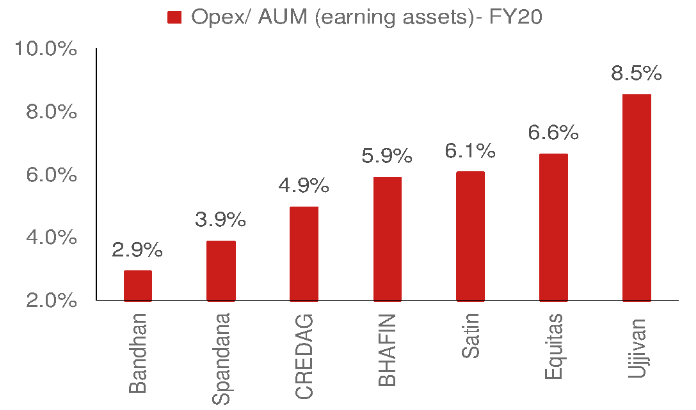
- With spreads capped at 10% levels and lower pricing sensitivity in the MFI segment, we highlight two most relevant factors to compare MFIs: 1) its trough cycle asset quality performance (explained earlier), and 2) operating efficiency, which remains the key determinant of a superior ROA/ROE delivery.
- On operational metrics as well, CREDAG does compare well vs its peers despite its tighter operating standards.

Fig. 154: Opex ratio comparison – pre - bank phase



Source: Company data, Nomura research

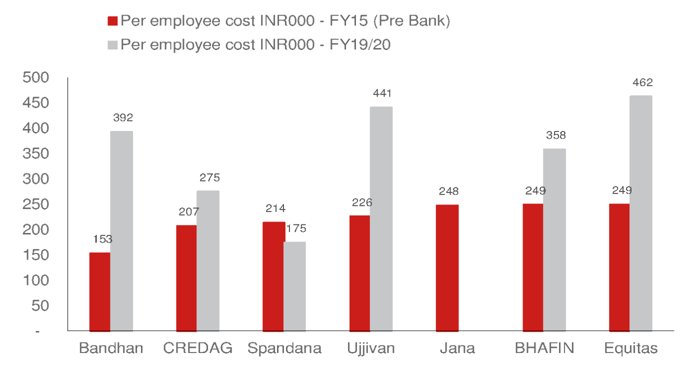
Fig. 155: Better employee and customer retention leads to lower/ similar opex/AUM vs . peers



Source: Company data, Nomura research

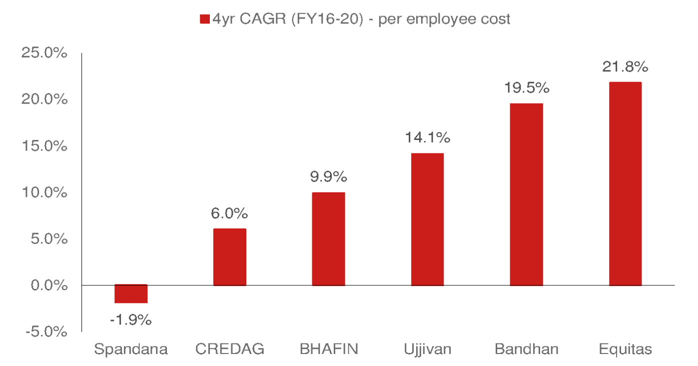
- **Best-in-class employee cost and employee retention** – CREDAG enjoys the lowest cost per employee amongst its peers, and has increased at 6% over the past four years. Bandhan, Equitas and Ujjivan have seen spikes in employee costs due to talent acquisitions after converting into bank/SFB.

Fig. 156: Per employee cost among the lowest for CREDAG



Source: MFIN, Company data, Nomura research

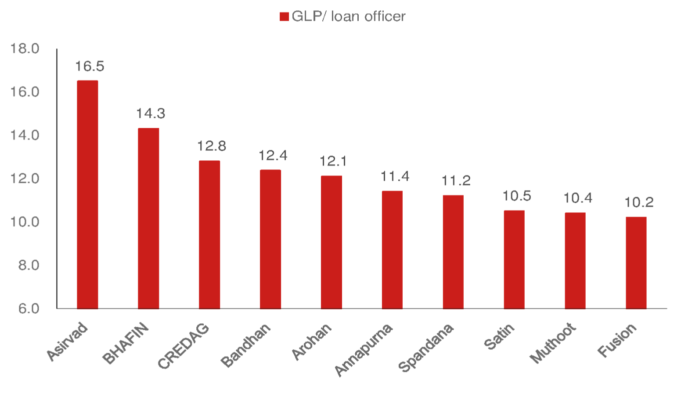
Fig. 157: Per employee cost CAGR vs . peers



Source: MFIN, Company data, Nomura research

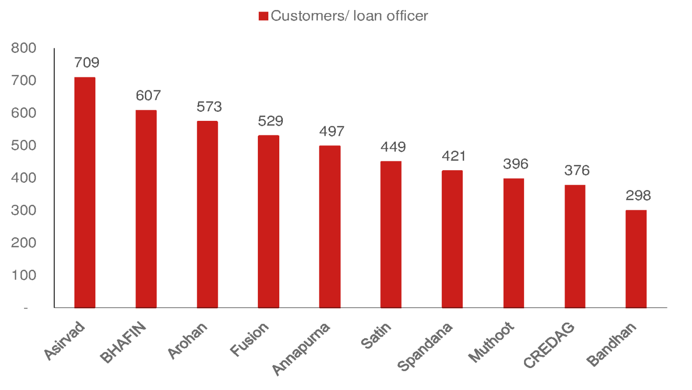
- Customers per loan officer remain lower due to its weekly collection model but GLP/ loan officer is still better than peers due to its higher AUM per customer, aiding to record similar or better productivity levels.

Fig. 158: GLP per loan officer still better due to higher AUM per customer



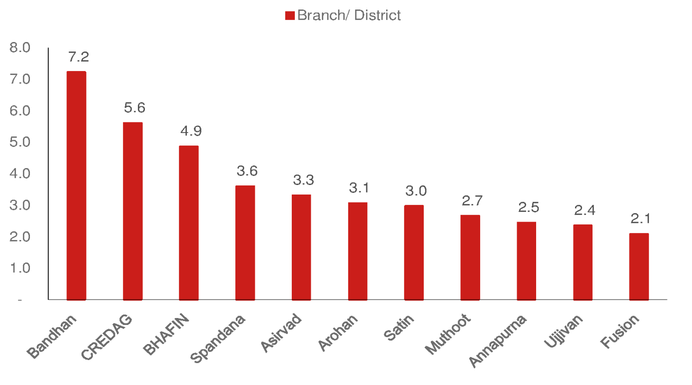
Source: Company data, Nomura research

Fig. 159: Customer/ loan officer lower due to the weekly collection model followed by CREDAG



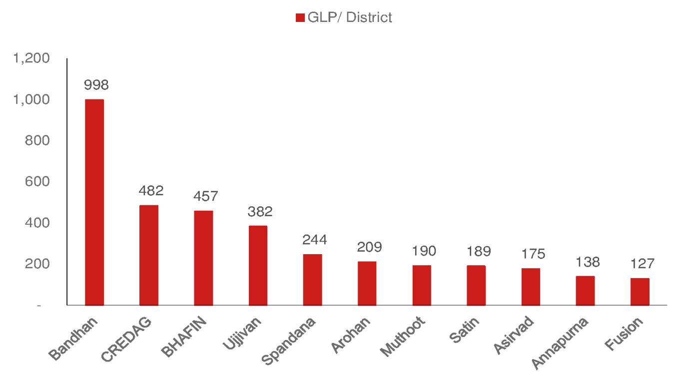
Source: Company data, Nomura research

Fig. 160: CREDAG has higher number of branches per district vs . peers ...



Note: *DSCs in case of Bandhan*
Source: Company data, Nomura research

Fig. 161: ...leading to its better GLP per district



Note: *DSCs in case of Bandhan*
Source: Company data, Nomura research

Prudent underwriting practices, and a superior risk management framework

Prudent borrower selection process

- CREDAG follows a strict leverage rule of INR0.1mn (vs a RBI's cap of INR0.125mn) to a borrower and the overall limit of three financial institutions where the borrower will be rejected if she does not meet the overall criteria.
- Further, it puts enough emphasis on the following at the time of group formation – (1) the borrower group has to necessarily be within the 500m radius; (2) the borrower group needs to be self-chosen, without any staff interference; and (3) multiple legs of credit bureau checks, along with compulsory five-day training, before the disbursement of loan. This does increase its turnaround time to around 15 days for the initial disbursement, but also ensures prudent selection of customers.
- From accounting perspective as well, CREDAG follows NPA recognition of 60 DPD (days past due) and 15 DPD for stage-2 vs. regulatory requirement of 90 DPD and 60 DPD, respectively. It also writes-off loans at 270 DPD.
- Collusion risk is mitigated by placing the employees 100-150kms away from their respective home locations.

Alignment of employee interests

- CREDAG has been successful in aligning its employee interests with the long-term goals of the business, as well as ensuring a strong employee culture which has led to a much stable employee base over time while keeping its employee costs lower.
- Its top management has an average vintage of 15-20 y ears in the financial services domain within CREDAG/ other large banks/ financial institutions.
- Its attrition rate is also lower than the industry, with 25% employee attrition vs. the

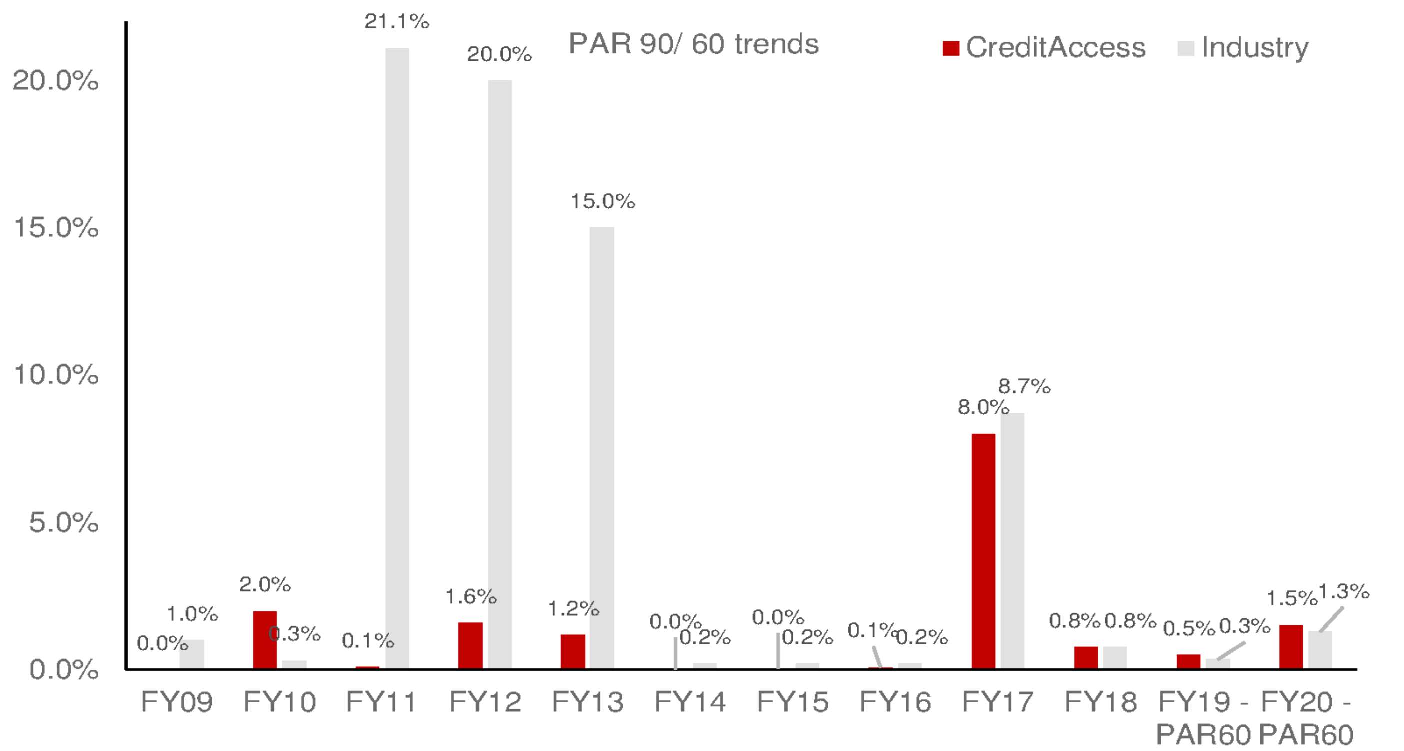
industry average of 35%.

- We see few reasons for its lower attrition and a much stable employee base: (1) CREDAG largely depends on fresh hires at entry level jobs, largely from the local community and a good portion of that comes from families of active customers; (2) t hese loan officers reside in branches itself, thereby saving on rental costs; (3) c ollusion risk is mitigated by placing the employees 100-150kms away from their respective home locations and keeps only five-day work week to ensure these employees can go back to their home towns on weekends; (4) a clear development path for its employees, with a potential to be promoted from loan officer to branch manager to area manager within the age of 30 years; and (5) its incentive structures are rightly aligned to number of customers serviced, the number of customers added and process adherence, and not linked to disbursements or collections which may lead to inferior underwriting practices.

Superior underwriting track record; delivered better in the past cycle

- CREDAG has benefitted from its customer-centric approach, its prudent customer selection, and superior risk management framework; this is evident from its superior performance during the past disruptions, such as demonetization, and has aided CREDAG to deliver sustainably lower through-cycle credit cost.
- Over FY16-20, the annual credit cost for CREDAG at 170bps was meaningfully lower than top players, at 160-240bps annually, despite the 60-day recognition followed by CREDAG starting from FY19.

Fig. 162: CREDAG 's delinquency trends have been superior through the past cycles...



Source: Company data, Nomura research

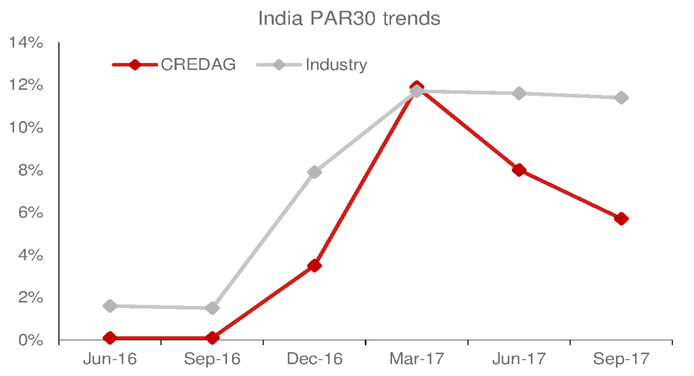
Fig. 163: ...driving superior credit cost vs . peers

Credit cost %	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Credit Access	-0.6%	1.3%	1.1%	0.7%	0.7%	3.9%	-0.3%	1.3%	3.0%
Spandana		68.1%	0.5%	0.5%	0.9%	3.3%	1.7%	1.2%	4.9%
BHAFIN	52.1%	20.1%	0.9%	0.4%	1.0%	5.9%	1.1%	0.8%	
Satin	0.3%	0.5%	1.1%	0.6%	0.6%	1.5%	1.0%	0.9%	2.8%
Bandhan						0.5%	1.4%	2.2%	2.6%
Ujjivan	0.9%	0.8%	0.6%	0.9%	0.6%	1.3%	4.5%	0.4%	1.4%
Equitas	0.8%	0.8%	0.9%	1.6%	1.2%	1.6%	2.2%	0.9%	1.8%
Top 7 MFI lenders - credit cost	**13.5%**	**17.9%**	**0.9%**	**0.8%**	**0.9%**	**2.0%**	**1.6%**	**1.4%**	**2.5%**

Source: Company data, Nomura research

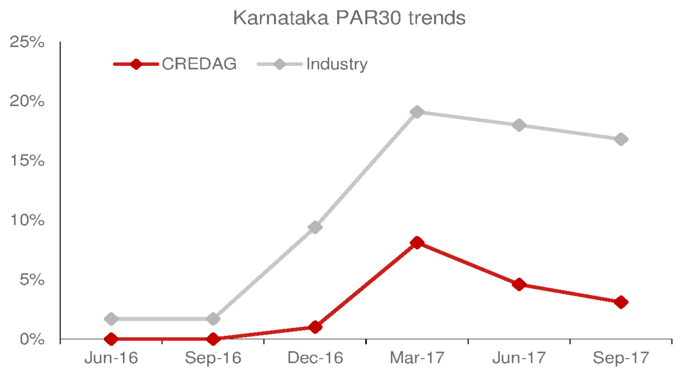
- More specifically, during demonetization, CREDAG's performance across impacted states was better than peers, with a relatively lower spike in portfolio at risk (PAR) and a much sharper recovery post-demonetization.

Fig. 164: India – PAR30 trends



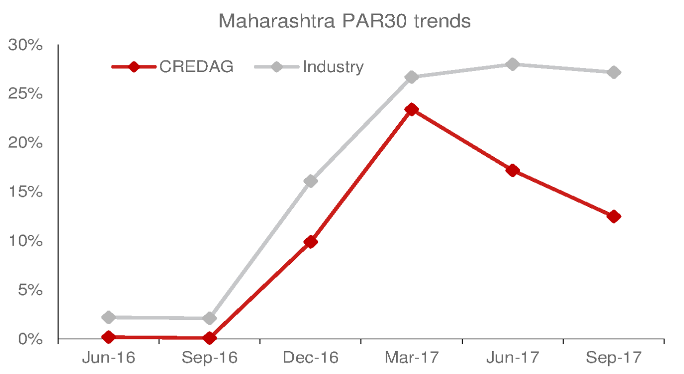
Source: Company data, Nomura research

Fig. 165: Karnataka – PAR30 trends



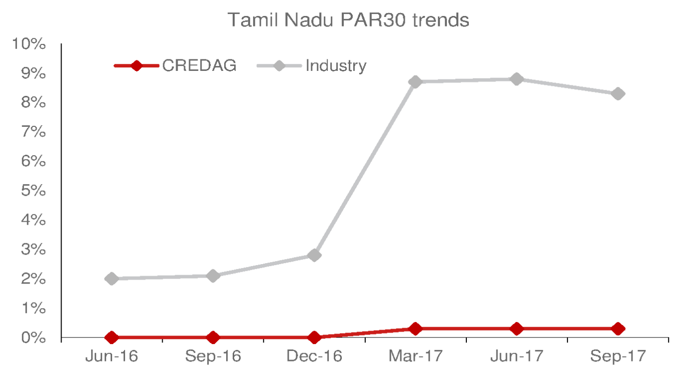
Source: Company data, Nomura research

Fig. 166: Maharashtra – PAR30 trends



Source: Company data, Nomura research

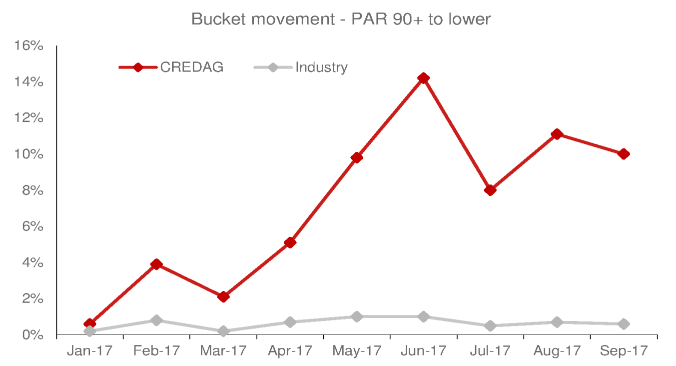
Fig. 167: Tamil Nadu – PAR30 trends



Source: Company data, Nomura research

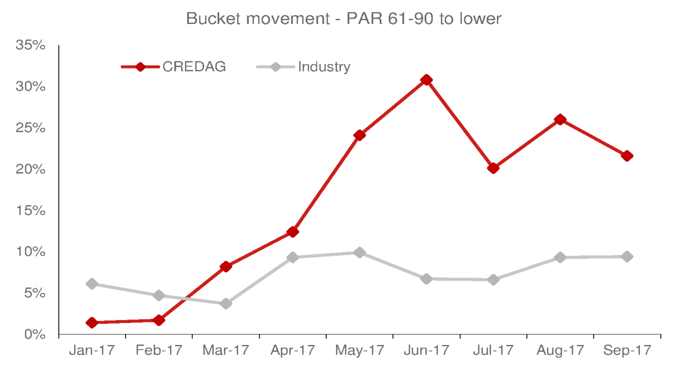
- Sharp backward bucket movement (upgrades across buckets) for CREDAG, compared with the industry, exhibits its ability to bounce back faster from the initial disruption.

Fig. 168: Rollbacks - PAR 90+ to lower bucket



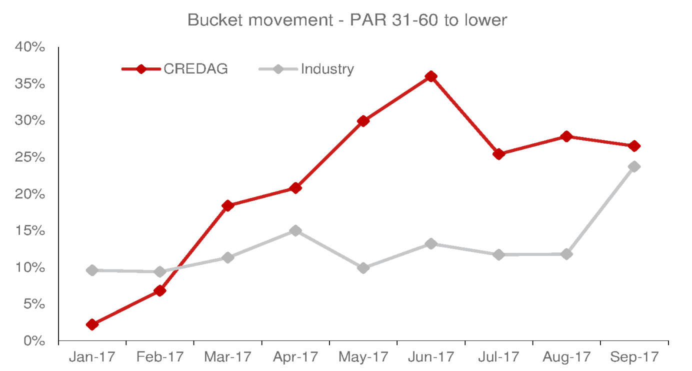
Source: Company data, Nomura research

Fig. 169: Rollbacks - PAR 61-90 to lower buckets



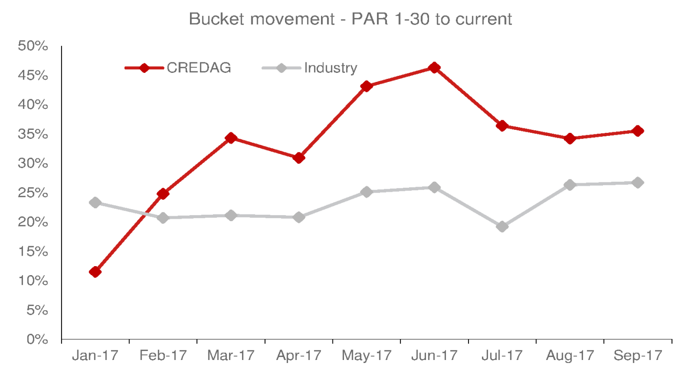
Source: Company data, Nomura research

Fig. 170: Rollbacks - PAR 31-60 to lower bucket



Source: Company data, Nomura research

Fig. 171: Rollbacks - PAR 1-30 to current bucket

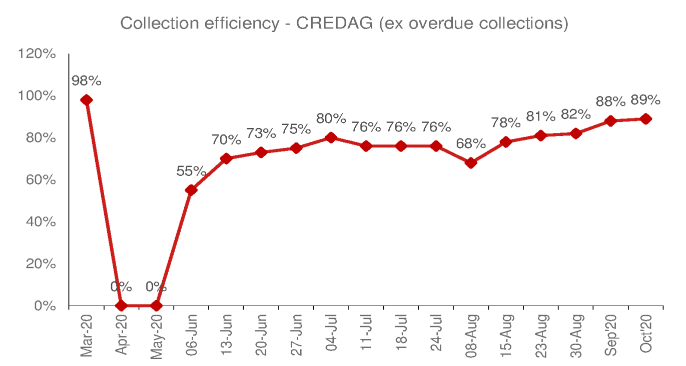


Source: Company data, Nomura research

COVID-19 pandemic impact large but still manageable

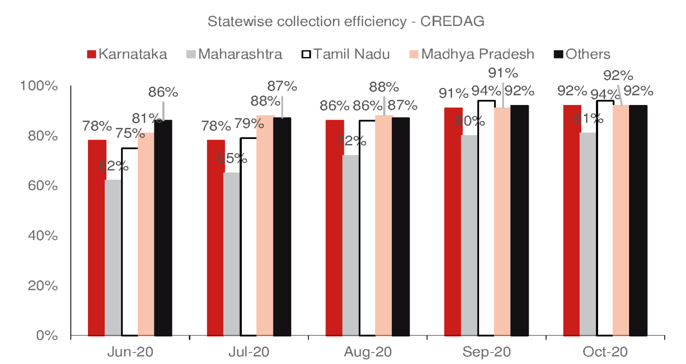
- The impact on unsecured retail products is clearly higher than secured products but we have seen a sharp recovery in collection efficiency across players and across geographies. CREDAG's collection efficiency for Oct-20 stood at 89%.
- We build in an av erag e credit cost of 350-450bp in FY21F for MFI companies under over coverage , and further build in a slightly elevated credit cost for FY22F ; however, we think eventual write-offs should be fairly manageable given the earnings profile s of these large MFIs.
- Collection efficiency for CREDAG has been m arginally below peers , with a higher share of Maharashtra (where the impact is higher) dragging overall collections.
- We remain confident that MFI s will see much sharper/faster normal ization both in growth (shorter duration boo k) and credit costs (accelerated provisioning) in FY22F; and think ROE should normalize soo ner t han anticipated earlier
- We are building in credit cost of 435/200bps for CREDAG in FY21/22F which should take care of the COVID-19 pandemic impact, in our view. CREDAG has already build in a COVID-19 pandemic buffer of 310bps for AUMs.

Fig. 172: Overall collections for CREDAG have improved to 89%



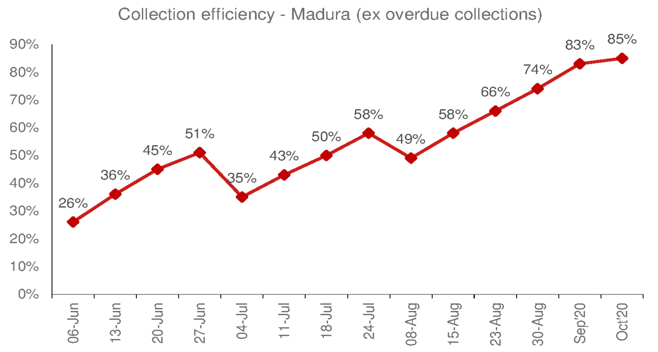
Source: Company data, Nomura research

Fig. 173: State-wise collection efficiency - CREDAG



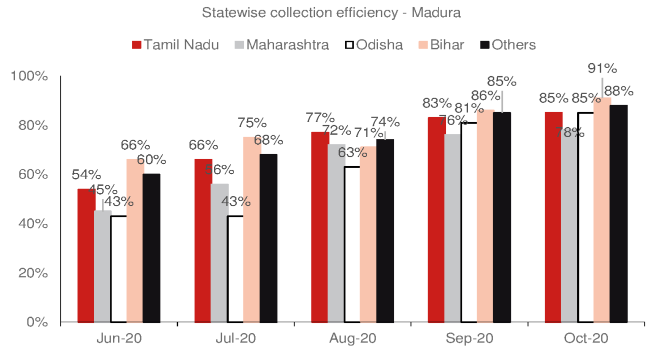
Source: Company data, Nomura research

Fig. 174: Madura collections still lagging at 85%



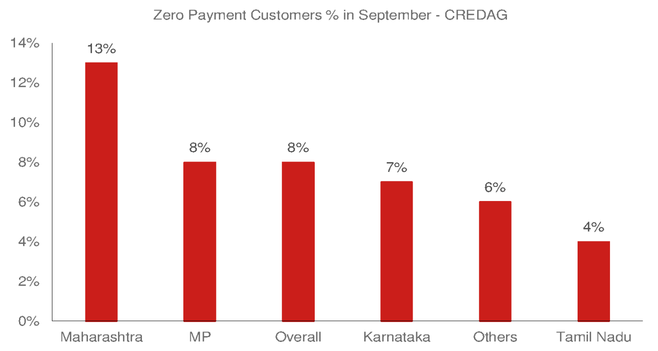
Source: Company data, Nomura research

Fig. 175: State-wise collection efficiency - Madura



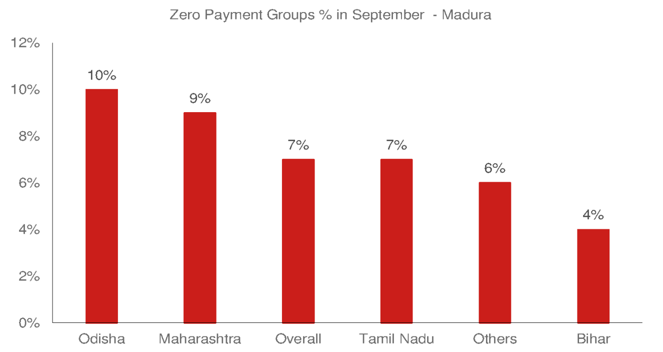
Source: Company data, Nomura research

Fig. 176: Zero payment customer at 8% in Sept (CAGL) – o f w hich 24% activated in October



Source: Company data, Nomura research

Fig. 177: Zero payment customer at 7% in Sept (MMFL) – o f w hich 33% activated in October



Source: Company data, Nomura research

Fig. 178: Collections nearing pre-C OVID-19 pandemic levels for top MFI players

MFI collection efficiency (%)		Covid						
	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20
Ujjivan	93.0%	2.0%	14.0%	53.0%	60.0%	68.0%	83.0%	88.0%
Equitas	77.0%	0.0%	7.0%	42.0%	61.0%	77.0%		91.0%
BHAFIN			12.5%	71.0%			91.0%	93.0%
Satin		3.0%	17.0%	62.0%	85.0%	86.0%	94.0%	
Spandana		2.0%	23.0%	60.0%	75.0%	80.0%	88.0%	93.0%
CREDAG	98.0%	0.0%	0.0%	74.0%	76.0%	82.0%	88.0%	89.0%
Bandhan				68.0%			89.0%	91.0%

Source: Company data, Nomura research

Expect ~40% PAT CAGR and ROEs to normalize to 18% (FY23)

- Over FY14-20, CREDAG has delivered a strong 52% AUM CAGR, and has delivered average ROEs of 16% and a PAT CAGR of >60%.
- We expect CREDAG to continue its m omentum over medium term, with >2x jump in branches over past 3 years, large market opportunity and possibility of improving operating efficiency (especially Madura), while we remain wary of the near-term risks.
- We build in an AUM CAGR of 19% over FY20-23F vs our industry growth expectations of 18% CAGR while we do not build in any meaningful improvement in cost ratios from here on.
- We do factor in the COVID-19 pandemic related impact for CREDAG, with credit cost expectations at 435/200bps for FY21/22F.
- With this we expect ROA/ROEs to mean revert to 4.8/18% by FY23F, with normalized credit cost of 1.35% (by FY23F). While the impact from COVID-19 pandemic may be higher than that for other secured products, a sharp rebound in collection efficiency, average PPOP/assets of >7% for FY21-23F and healthy capital ratios give us

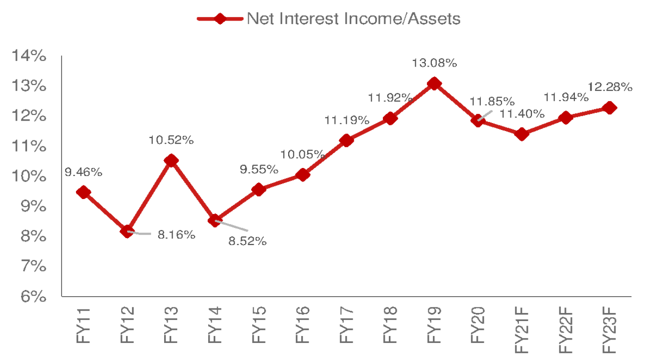
confidence that CREDAG will likely be able to navigate the crisis much better.

Fig. 179: RoA decomposition: We expect RoEs to mean revert to 81% by FY23

											CREDAG + Madura Merged		
RoA decomposition	**FY11**	**FY12**	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**FY21F**	**FY22F**	**FY23F**
Net Interest Income/Assets	**9.46%**	**8.16%**	**10.52%**	**8.52%**	**9.55%**	**10.05%**	**11.19%**	**11.92%**	**13.08%**	**11.85%**	**11.40%**	**11.94%**	**12.28%**
Fees/Assets	4.77%	2.94%	2.00%	1.77%	1.77%	1.66%	1.15%	0.18%	0.14%	0.12%	0.09%	0.12%	0.15%
Investment profits/Assets	0.00%	0.00%	0.00%	0.24%	0.33%	0.18%	0.12%	0.10%	0.92%	0.64%	0.31%	0.20%	0.16%
Net revenues/Assets	**14.23%**	**11.11%**	**12.51%**	**10.53%**	**11.65%**	**11.88%**	**12.45%**	**12.20%**	**14.14%**	**12.61%**	**11.80%**	**12.26%**	**12.59%**
Operating Expense/Assets	-11.86%	-12.20%	-9.09%	-6.04%	-5.36%	-5.27%	-5.17%	-4.78%	-4.80%	-4.78%	-4.81%	-4.98%	-4.95%
PPOP/ Assets	**2.37%**	**-1.10%**	**3.43%**	**4.49%**	**6.29%**	**6.62%**	**7.28%**	**7.41%**	**9.34%**	**7.82%**	**6.99%**	**7.28%**	**7.63%**
Core PPOP/ Assets	**2.37%**	**-1.10%**	**3.43%**	**4.24%**	**5.96%**	**6.44%**	**7.17%**	**7.32%**	**8.42%**	**7.19%**	**6.68%**	**7.08%**	**7.47%**
Provisions/Assets	-1.24%	0.50%	-1.11%	-0.77%	-0.52%	-0.64%	-3.51%	0.32%	-1.22%	-2.71%	-3.57%	-1.82%	-1.27%
Taxes/Assets	-0.08%	-0.42%	-0.15%	-1.23%	-2.02%	-2.14%	-1.34%	-2.73%	-2.87%	-1.40%	-0.86%	-1.38%	-1.60%
Total Costs/Assets	**-13.19%**	**-12.12%**	**-10.35%**	**-8.04%**	**-7.90%**	**-8.04%**	**-10.02%**	**-7.19%**	**-8.89%**	**-8.89%**	**-9.25%**	**-8.18%**	**-7.82%**
ROA	**1.05%**	**-1.01%**	**2.16%**	**2.49%**	**3.75%**	**3.84%**	**2.43%**	**5.00%**	**5.25%**	**3.71%**	**2.55%**	**4.09%**	**4.76%**
Leverage (x)	6.4	5.5	4.8	4.6	4.5	5.2	5.4	4.0	3.2	3.5	3.9	3.5	3.7
ROE	**6.75%**	**-5.55%**	**10.36%**	**11.47%**	**16.71%**	**19.81%**	**13.02%**	**19.97%**	**16.92%**	**13.01%**	**9.93%**	**14.34%**	**17.46%**
LLP/ Loans (Credit cost)	1.60%	-0.62%	1.29%	1.07%	0.67%	0.73%	3.90%	-0.34%	1.30%	3.03%	4.33%	1.99%	1.36%
EPS	**1.4**	**-1.2**	**2.1**	**3.5**	**6.8**	**11.5**	**8.8**	**16.5**	**22.4**	**22.7**	**21.0**	**39.2**	**56.0**
BVPS	**21.6**	**20.5**	**28.4**	**39.9**	**52.2**	**63.7**	**80.6**	**111.9**	**164.8**	**185.4**	**253.6**	**292.8**	**348.8**

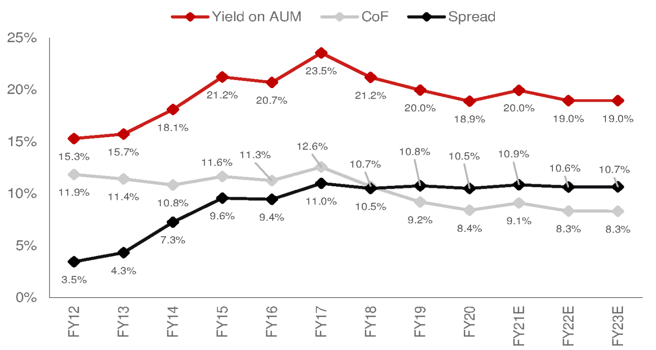
Source: Company data, Nomura estimates

Fig. 180: We expect some improvement in margins



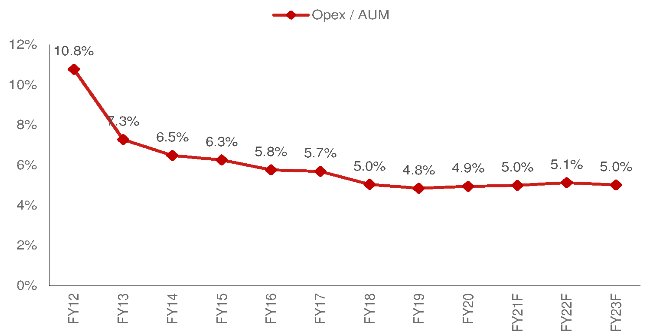
Source: Company data, Nomura estimates

Fig. 181: Lending spreads have improved



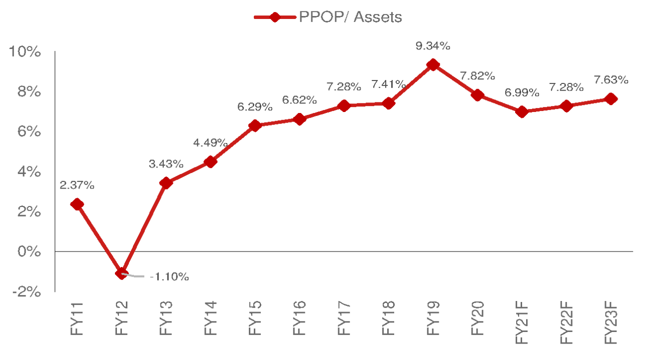
Source: Company data, Nomura estimates

Fig. 182: OPex to AUM steady at ~5%



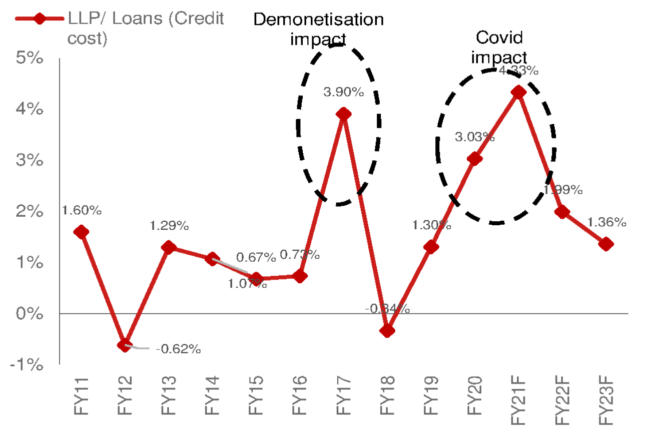
Source: Company data, Nomura estimates

Fig. 183: Strong operational performance – we expect PPOP/AUM at 7.3-7.6% over FY22-23



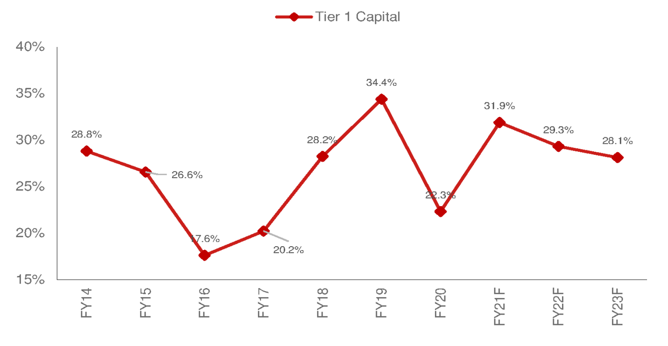
Source: Company data, Nomura estimates

Fig. 184: Credit cost performance has been better th an industry through past cycles



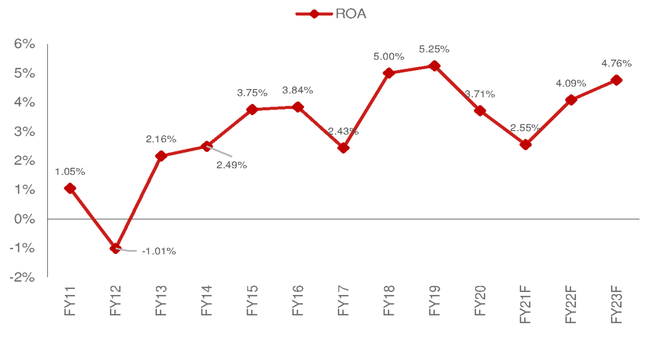
Source: Company data, Nomura estimates

Fig. 185: Capital adequacy strong post capital raise in October



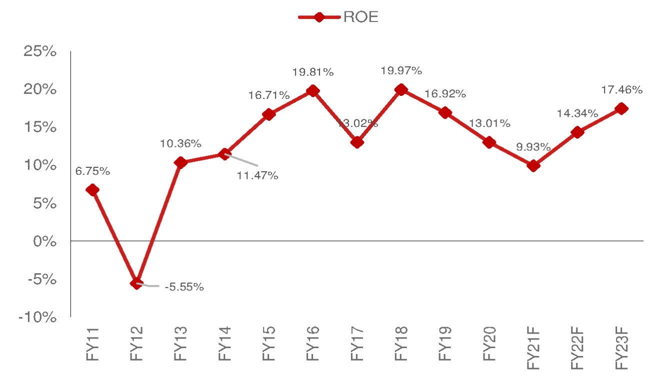
Source: Company data, Nomura estimates

Fig. 186: We expect RoAs to recover to 4.1-4.8% by FY22-23



Source: Company data, Nomura estimates

Fig. 187: We expect RoEs of 18% by FY23



Source: Company data, Nomura estimates

Fig. 188: Our expectations for key MFI players

Key microfinance players - NMR estimates			
PPOP	**FY21F**	**FY22F**	**FY23F**
Bandhan	6.28%	6.07%	6.07%
Equitas	3.48%	3.30%	3.50%
Ujjivan	4.68%	4.40%	4.51%
CREDAG	6.99%	7.28%	7.63%
Credit Cost			
Bandhan	3.50%	1.63%	1.58%
Equitas	2.51%	2.07%	1.56%
Ujjivan	3.58%	2.48%	2.07%
CREDAG	4.33%	1.99%	1.36%
RoA			
Bandhan	2.81%	3.69%	3.72%
Equitas	1.26%	1.36%	1.73%
Ujjivan	1.46%	1.88%	2.19%
CREDAG	2.55%	4.09%	4.76%
AUM growth			
Bandhan	13.1%	16.7%	18.7%
Equitas	26.0%	24.5%	23.3%
Ujjivan	8.7%	24.2%	21.5%
CREDAG	33.7%	25.6%	24.2%
RoE			
Bandhan	16.6%	21.7%	21.5%
Equitas	9.3%	10.3%	13.4%
Ujjivan	8.2%	11.1%	13.9%
CREDAG	9.9%	14.3%	17.5%
Tier 1			
Bandhan	24.9%	25.3%	25.5%
Equitas	22.8%	20.4%	19.1%
Ujjivan	31.0%	27.6%	25.9%
CREDAG	31.9%	29.3%	28.1%

Source: Company data, Nomura estimates

Premium valuations to sustain

- We see CREDAG to be the best placed in the MFI segment with its prudent management, superior track record, and best operating standards. This, coupled with its high growth and high return ratio opportunity, makes CREDAG best placed to play the MFI theme. We believe CREDAG will continue to command a premium over peers given its superior track record, high growth prospects and expectations of ROEs to normalize fully by FY23F. Thus, we initiate on CREDAG with a Buy rating and a TP of INR950/share, implying 24% upside.
- **Valuation based on a residual income model:** We value CREDAG based on Residual income model to arrive at our target price of INR950 implying a 2.7x FY23F book multiple. We expect CREDAG to deliver 17-18% sustainably v/s cost of equity of 12-13%. We assume avg RoEs and beta at 17.4% and 1.3 over stage 1 and stage 2

and terminal RoEs and beta of 17% and 1.2. Contribution of terminal value to our valuation is ~40% which is reasonable, in our view.

Fig. 189: Our TP of INR950/share implies 2.7x FY23F book

	INR mn	Contribution of value	Avg. ROE assumption	Avg. COE assumption
FY23 networth	55,102	36.8%		
PV of RI over FY24-28F	13,750	9.2%	17.4%	12.50%
PV of RI over FY29-35F	22,025	14.7%	17.4%	12.50%
Terminal value	57,360	38.3%	17.0%	12.00%
Total value of the firm	**1,49,719**	**100%**		
Total number of shares	158			
Value per share	**950**			
Implied P/B	**2.7**			
Terminal growth assumption	5.0%			

Source: Company data, Nomura estimates

Fig. 190: Peer valuation s – comp arison

Banks	Ticker	Rating	TP	P/B			P/E			ROE			LTP
				FY21F	FY22F	FY23F	FY21F	FY22F	FY23F	FY21F	FY22F	FY23F	
Corporate Banks													
Axis	AXSB IN	Buy	640	1.79	1.60	1.40	23.3	14.4	10.7	8.4%	11.8%	13.9%	635
ICICI	ICICIBC IN	Buy	625	1.87	1.68	1.47	18.1	13.5	10.5	11.4%	13.1%	14.9%	511
SBI	SBIN IN	Buy	275	0.65	0.60	0.54	13.5	6.8	5.4	4.9%	9.2%	10.5%	271
BOB	BOB IN	Neutral	50	0.53	0.51	0.47	NM	37.5	8.0	-3.7%	1.2%	5.3%	66
Retail Banks													
HDFCB	HDFCB IN	Buy	1,450	3.87	3.35	2.85	27.5	21.7	17.0	14.9%	16.6%	18.2%	1,406
Kotak	KMB IN	Neutral	1,570	4.71	4.19	3.71	41.0	35.7	30.8	13.0%	12.4%	12.8%	1,885
NBFCs/ HFCs													
HDFC	HDFC IN	Buy	2,425	2.33	2.13	1.94	25.8	20.1	16.8	10.6%	11.6%	12.6%	2,309
MMFSL	MMFS IN	Neutral	130	1.40	1.29	1.17	26.5	12.1	9.5	5.8%	10.8%	12.6%	177
New Banks/ MFIs													
Equitas	EQUITAS IN	Buy	95	1.03	0.93	0.81	12.3	9.5	6.5	9.3%	10.3%	13.4%	73
Bandhan Bank	BANDHAN IN	Buy	490	3.76	3.18	2.68	24.0	15.9	13.6	16.6%	21.7%	21.5%	400
AU SFB	AUBANK IN	Neutral	790	5.78	5.10	4.27	44.6	40.6	24.6	10.4%	13.4%	18.9%	918
Ujjivan	UJJIVAN IN	Buy	360	1.51	1.36	1.19	19.2	12.9	9.1	8.2%	11.1%	13.9%	286
CREDAG	CREDAG IN	Buy	950	3.03	2.62	2.20	36.6	19.6	13.7	9.9%	14.3%	17.5%	768

Note: Priced as at close of markets on 9 December 2020
Source: Company data, Nomura research

Brief history of CREDAG

Fig. 191: Key events and milestones

Year	Key events
1991	Incorporated as Sanni Collection Pvt Ltd (SCPL) in Jun-91 at Calcutta, West Bengal
1998	Obtained NBFC registration
2007	Feb '07 - The entire shareholding of SCPL was acquired by Vinatha M. Reddy, Vijitha Subbaiah and Suresh K. Krishna Oct '07 - SCPL acquired the microfinance business under T. Muniswamappa Trust (“TMT”) along with the brand name “Grameen Koota” (TMT had began its microfinance operation in Karnataka in 1999 under brane name "Grameen kota")
2008	Name of SPCL changed to Grameen Financial Services Private Limited Commenced operations in Maharashtra
2009	Started operations in Tamil Nadu
2013	RBI granted NBFC-MFI status and the name of the company was changed to Grameen Koota Financial Services Private Limited
2014	CAA acquired a majority stake in the Company
2015	Commenced operations in Madhya Pradesh and Chhattisgarh
2016	99% subsidiary of CreditAccess Asia
2017	Started Retail finance business
2018	Company name changed to CreditAccess Grameen Limited CREDAG listed on NSE & BSE - Raised fresh issue of INR6.3bn and OFS of INR5bn Enters Odisha, Goa, Kerala and Puducherry
2018	Crosses 2.5mn borrower Enters 5 new states - Jharkhand, Rajasthan, Gujarat, UP and Bihar
2019	Announced acquisition with Madura Microfinance

Source: Company data, Nomura research

Strong management pedigree

- CREDAG has an experienced top management team led by Mr. Udaya Kumar Hebbar (MD & CEO) and Mr. Diwakar BR (CFO), who have 25-30 years of experience in the financial services domain. The top management team is seasoned with 15-20 years of average work-experience at CREDAG or at other large banks/ financial institutions.

Fig. 192: Senior management personnel

Key Management	Brief Profile
Udaya Kumar Hebbar Managing Director and CEO	Mr Udaya Kumar Hebbar has 30 years of experience in the financial services domain. Prior to joining CREDAG, he has been associated with ICICI Bank, Barclays Bank and Corporation Bank. He holds a master’s degree in commerce, CAIIB from the Indian Institute of Bankers and is a graduate in banking operations and technology from BAI, USA.
Diwakar BR Director - Finance & CFO	Mr Diwakar joined the company in Oct -11 and has more than 25 years of experience in the financial services sector. Prior to joining CREDAG, he has worked with SIDBI, ICICI Bank and at ACCION International. He holds a Masters degree in Commerce.
Sundar Arumugam Head of Strategy and Innovation	Mr Arumugam was earlier associated with CreditAccess Asia as head of business innovation. Prior to CAA, he was head of product management at Equifax India where he led product strategy and execution. He was part of the start-up team at Equifax India and was instrumental in setting up the microfinance bureau, leading the business unit for four years. He holds a bachelor’s degree in technology and an MBA from INSEAD.
Ganesh Narayanan Chief Business Officer	Mr Narayanan joined CREDAG in Jan 20 and has +21 years of experience in the financial services industry. Prior to joining the company, he was the Group President & Deputy National Head – Indian Financial Institutions Banking at Yes Bank.
Firoz Anam Chief Risk Officer	Mr Firoz joined CREDAG in 2020. In his previous roles, he has managed credit and operational risk functions at IDFC Bank, JP Morgan Chase and Citibank. He is a B.Tech from IIT Kharagpur and holds PGDM from IIM-Bangalore.
Srivatsa H N Business Head - Group lending (Karnataka and Tamil Nadu)	Mr Srivatsa HN has been with CREDAG since 2007 (joined TMT in 2002) and has 15+ years of experience in microfinance operations. He holds a pre-university certificate issued by the Education Department, Government of Karnataka.
Gopal Reddy Business head - Group lending (Maharashtra, MP and Chhattisgarh)	Mr Reddy has been with CREDAG since 2007 (joined TMT in 1999) and has over 15 years of experience in microfinance operations. He holds a bachelor’s degree in commerce from Bangalore University.
Vishwanath Bhat Head - Retail Finance	Mr Vishwanath joined CREDAG in Jun-16. Previously he has been associated with Shriram Group, Chola, ICICI Bank, Copal Amba (Moody’s Analytics Company) and Axis Bank. He holds a post graduate degree in management.
Gururaj K S Rao Chief Audit Officer	Mr Rao joined CREDAG in 2009 and has 24 years of experience in auditing. He holds a bachelor’s degree in commerce from Bangalore University.
M. J. Mahadev Prakash Head - Compliance, Legal & CS	Mr Mahadev Prakash joined the company in Dec-19. Prior to joining CREDAG, he was associated with EY, J. Sagar Associates, Janalakshmi SFB, RMZ Corp, BPL Ltd., and Bal Pharma Ltd. He is also an Associate member of the Institute of Company Secretaries of India, New Delhi.

Source: Company data, Nomura research

Financial summary

Fig. 193: CREDAG – summary of financials

PL Statement	CREDAG						Merged		
	FY15	FY16	FY17	FY18	FY19	FY20	FY21F	FY22F	FY23F
Interest income	2,537	4,266	6,702	8,597	12,183	16,172	23,531	28,094	35,010
Interest expenses	1,279	2,074	3,243	3,537	4,168	5,727	8,725	10,001	12,208
NII	**1,258**	**2,192**	**3,459**	**5,060**	**8,016**	**10,445**	**14,807**	**18,093**	**22,802**
Other income	277	401	391	118	650	672	519	484	580
Total income	**1,535**	**2,593**	**3,850**	**5,179**	**8,666**	**11,117**	**15,325**	**18,576**	**23,381**
Employee exp	436	707	1,047	1,304	1,861	2,596	4,045	4,978	6,182
Other overheads	270	442	551	726	1,079	1,622	2,206	2,572	3,020
PPOP	**829**	**1,444**	**2,252**	**3,148**	**5,726**	**6,899**	**9,074**	**11,026**	**14,179**
Credit cost	68	140	1,086	-134	749	2,390	4,643	2,752	2,350
PBT	**761**	**1,304**	**1,166**	**3,282**	**4,977**	**4,509**	**4,431**	**8,274**	**11,829**
Tax	266	466	413	1,157	1,760	1,234	1,117	2,085	2,981
PAT	**495**	**838**	**753**	**2,125**	**3,218**	**3,275**	**3,314**	**6,189**	**8,848**
Balancesheet	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**FY21F**	**FY22F**	**FY23F**
Share Capital	730	730	857	1,284	1,436	1,440	1,580	1,580	1,580
Reserves	3,080	3,920	6,051	13,091	22,215	25,251	38,485	44,674	53,522
Net Worth	**3,809**	**4,649**	**6,908**	**14,375**	**23,651**	**26,691**	**40,065**	**46,254**	**55,102**
Borrowings	5,850	11,421	11,759	36,235	48,666	78,226	1,01,617	1,25,686	1,54,952
Other liabilities	7,619	11,976	16,489	1,643	3,977	5,609	6,272	6,585	6,915
Total liabilities	**13,469**	**23,397**	**28,248**	**37,877**	**52,643**	**83,834**	**1,07,889**	**1,32,271**	**1,61,867**
Equity + Liabilities	**17,278**	**28,047**	**35,156**	**52,252**	**76,293**	**1,10,525**	**1,47,954**	**1,78,525**	**2,16,968**
Advances	13,531	24,754	30,891	48,955	66,028	91,726	1,22,626	1,54,014	1,91,281
Investments	2	2	2	2	2	6,614	3,000	3,000	3,000
Cash and equivalents	2,798	2,549	3,637	1,431	6,156	5,804	10,689	9,620	10,582
Fixed assets (incl goodwill)	62	113	153	172	271	895	5,569	5,517	5,414
Other assets	885	628	473	1,692	3,836	5,485	6,069	6,373	6,691
Total Assets	**17,278**	**28,047**	**35,156**	**52,252**	**76,293**	**1,10,525**	**1,47,954**	**1,78,525**	**2,16,968**
Avg earning assets	13,173	21,818	30,917	42,459	61,287	88,166	1,29,882	1,51,475	1,85,749
Du PONT (on avg EA)	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**FY21F**	**FY22F**	**FY23F**
Interest income	19.3%	19.6%	21.7%	20.2%	19.9%	18.3%	18.1%	18.5%	18.8%
Interest expenses	9.7%	9.5%	10.5%	8.3%	6.8%	6.5%	6.7%	6.6%	6.6%
NII	**9.6%**	**10.0%**	**11.2%**	**11.9%**	**13.1%**	**11.8%**	**11.4%**	**11.9%**	**12.3%**
Other income	2.1%	1.8%	1.3%	0.3%	1.1%	0.8%	0.4%	0.3%	0.3%
Total income	**11.7%**	**11.9%**	**12.5%**	**12.2%**	**14.1%**	**12.6%**	**11.8%**	**12.3%**	**12.6%**
Employee exp	3.3%	3.2%	3.4%	3.1%	3.0%	2.9%	3.1%	3.3%	3.3%
Other overheads	2.0%	2.0%	1.8%	1.7%	1.8%	1.8%	1.7%	1.7%	1.6%
PPOP	**6.3%**	**6.6%**	**7.3%**	**7.4%**	**9.3%**	**7.8%**	**7.0%**	**7.3%**	**7.6%**
Credit cost	0.5%	0.6%	3.5%	-0.3%	1.2%	2.7%	3.6%	1.8%	1.3%
PBT	**5.8%**	**6.0%**	**3.8%**	**7.7%**	**8.1%**	**5.1%**	**3.4%**	**5.5%**	**6.4%**
Tax	2.0%	2.1%	1.3%	2.7%	2.9%	1.4%	0.9%	1.4%	1.6%
PAT - RoA	**3.8%**	**3.8%**	**2.4%**	**5.0%**	**5.3%**	**3.7%**	**2.6%**	**4.1%**	**4.8%**
RoE	**16.7%**	**19.8%**	**13.0%**	**20.0%**	**16.9%**	**13.0%**	**9.9%**	**14.3%**	**17.5%**
EPS	**6.8**	**11.5**	**8.8**	**16.5**	**22.4**	**22.7**	**21.0**	**39.2**	**56.0**
BVPS	**52.2**	**63.7**	**80.6**	**111.9**	**164.8**	**185.4**	**253.6**	**292.8**	**348.8**
No. of shares mn	73	73	86	128	144	144	158	158	158
Face value	10	10	10	10	10	10	10	10	10

Source: Company data, Nomura estimates

Snapshot of Madura

- Madura Micro Finance Ltd (Madura) was started by the erstwhile promoters of Bank of Madura, led by its Founder Chairman Dr. K M Thiagarajan.
- In 2006, Madura received the NBFC/MFI license. Initially, it used to lend to SHGs in Tamil Nadu. In 2006, Madura took over the SHG business of 9500 SHGs from its predecessor organization, Micro Credit Foundation of India (MCFI).
- As of Sep-20, Madura operates across 7 states covering 95 districts through its 459 branches, with strong presence in Tamil Nadu (>60% of GLP).

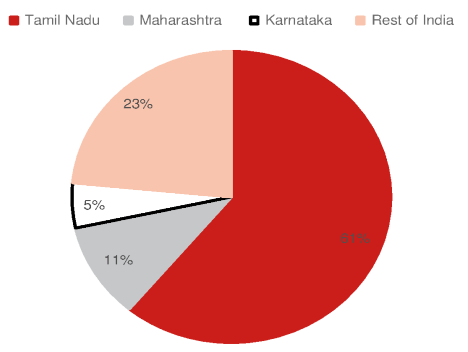
- Madura has an active borrower base of 1.14mn and a gross loan portfolio of INR19.8bn, as of Sep-20.
- Madura has a strong capital adequacy, as of Sep-20, with Tier-1 ratio at 21% and t otal CAR at 25%.

Fig. 194: Madura – summary financials

PL Statement	Madura						
	FY15	FY16	FY17	FY18	FY19	FY20	1HFY21
Interest income	720	1,103	1,677	2,130	3,689	4,549	2,110
Interest expenses	293	495	711	894	1,499	1,955	931
NII	**427**	**608**	**966**	**1,236**	**2,189**	**2,595**	**1,179**
Other income	54	85	118	201	179	210	35
Total income	**481**	**693**	**1,084**	**1,437**	**2,369**	**2,804**	**1,214**
Employee exp	109	164	262	345	464	674	400
Other overheads	123	194	253	261	334	494	162
PPOP	**249**	**335**	**569**	**832**	**1,571**	**1,636**	**652**
Credit cost	25	46	74	207	350	571	411
PBT	**224**	**289**	**495**	**625**	**1,221**	**1,064**	**241**
Tax	78	98	193	227	366	267	62
PAT	**146**	**192**	**302**	**398**	**855**	**797**	**179**
Balancesheet	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**1HFY21**
Share Capital	56	56	67	72	72	72	72
Reserves	812	1,004	1,695	2,333	3,150	3,944	4,122
Net Worth	**868**	**1,059**	**1,761**	**2,405**	**3,222**	**4,016**	**4,194**
Borrowings	3,099	4,694	7,420	9,228	17,264	17,106	16,496
Other liabilities	153	228	317	546	238	364	294
Total liabilities	**3,251**	**4,921**	**7,737**	**9,775**	**17,502**	**17,471**	**16,790**
Equity + Liabilities	**4,119**	**5,981**	**9,499**	**12,179**	**20,723**	**21,487**	**20,984**
Advances	3,500	5,177	8,240	11,162	18,415	19,266	18,197
Investments	137	51	67	17	103	454	504
Cash and equivalents	412	629	839	635	1,948	1,372	1,934
Fixed assets (incl goodwill)	16	18	21	37	70	101	80
Other assets	54	106	331	329	188	295	269
Total Assets	**4,119**	**5,981**	**9,499**	**12,179**	**20,723**	**21,487**	**20,984**
Avg earning assets	3,313	4,953	7,502	10,480	16,140	20,779	20,863
Du PONT (on avg EA)	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**1HFY21**
Interest income	21.7%	22.3%	22.3%	20.3%	22.9%	21.9%	20.2%
Interest expenses	8.9%	10.0%	9.5%	8.5%	9.3%	9.4%	8.9%
NII	**12.9%**	**12.3%**	**12.9%**	**11.8%**	**13.6%**	**12.5%**	**11.3%**
Other income	1.6%	1.7%	1.6%	1.9%	1.1%	1.0%	0.3%
Total income	**14.5%**	**14.0%**	**14.5%**	**13.7%**	**14.7%**	**13.5%**	**11.6%**
Employee exp	3.3%	3.3%	3.5%	3.3%	2.9%	3.2%	3.8%
Other overheads	3.7%	3.9%	3.4%	2.5%	2.1%	2.4%	1.6%
PPOP	**7.5%**	**6.8%**	**7.6%**	**7.9%**	**9.7%**	**7.9%**	**6.3%**
Credit cost	0.8%	0.9%	1.0%	2.0%	2.2%	2.8%	3.9%
PBT	**6.8%**	**5.8%**	**6.6%**	**6.0%**	**7.6%**	**5.1%**	**2.3%**
Tax	2.3%	2.0%	2.6%	2.2%	2.3%	1.3%	0.6%
PAT - RoA	**4.4%**	**3.9%**	**4.0%**	**3.8%**	**5.3%**	**3.8%**	**1.7%**
RoE	**18.4%**	**19.9%**	**21.4%**	**19.1%**	**30.4%**	**22.0%**	**8.7%**
EPS	**26.3**	**34.5**	**45.1**	**55.4**	**118.8**	**110.7**	**24.9**
BVPS	**156.1**	**190.6**	**263.0**	**334.2**	**447.8**	**558.2**	**582.9**
No. of shares mn	6	6	7	7	7	7	7
Face value	10	10	10	10	10	10	10

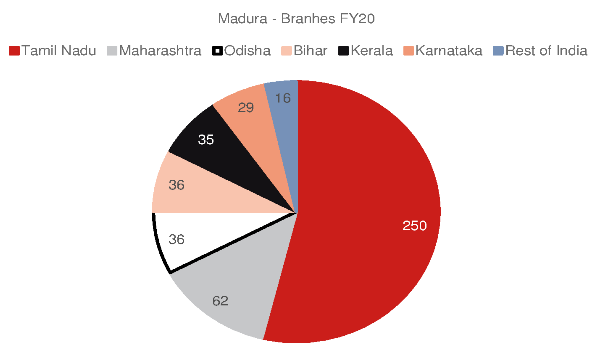
Source: Company data, Nomura research

Fig. 195: Madura AUM mix by state as of FY20



Source: Company data, Nomura research

Fig. 196: State-wise branch mix (FY20)



Source: Company data, Nomura research

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Bandhan Bank BANH.NS BANDHAN IN

Global Markets Research
11 December 2020

EQUITY: FINANCIALS

Reiterate Buy; TP increased to INR490

Further re-rating warranted for a deposit + profit engine

Rating	
Rating Remains	Buy
Target price Increased from INR 375	INR 490
Closing price 11 December 2020	INR 423
Implied upside	+15.8%
Market Cap (USD mn)	9,253.1
ADT (USD mn)	50.3

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Action: Reiterate Buy; TP increased to INR490

Bandhan has done exceptionally well on the liability side, with CASA scaling up to 38% of AUMs in just 4-5 years—far ahead of peers when compared with the same vintage in their journey. On the asset side as well, it is clearly a step ahead, gearing up for the next leg of its universal bank journey. It has created a new vertical- Emerging Entrepreneurs Business (EEB)—for its MFI and micro-home/enterprise business, and the GRUH merger provides the necessary diversification and additional legs to growth. Its strong liability profile (leading to lower cost of funds at 6.2% as at Sep-20) and focus on high-yielding assets makes it the most profitable bank in our India banks coverage (avg PPOP/ assets over FY21-23F of 6.1%), with ROEs expected to normalise from 17% to +21% by FY23F.

Moving in the right direction

Bandhan had highlighted its 5-year strategy, aimed at reducing its micro-banking mix from 65% currently to 30% (Target mix: MFI/ housing/ MSME/ retail loans at 30:30:30:10). It further intends to reduce its concentration in the North East from 65% currently to 27% by FY25. We think Bandhan offers best-in-class funding profile and return ratios, and with gradual diversification underway, it should continue to command premium valuations.

Near term risks a worry, but manageable

Upcoming elections in West Bengal and Assam and pace of recovery in collections moderating (89%/91% collection efficiency for MFI in Sep/Oct-20) does remain a near-term worry, especially for Bandhan, given its higher ticket sizes vs peers. But Bandhan has prudently created cumulative COVID-19 provisions of INR17.4bn—2.3% of AUM (3.5% of micro-banking book). Additionally, core PPOP/Assets of >6% and CET-1 of 22% provide enough buffers, in our view. We continue to factor in credit cost of 350/160bps in FY21/22F (in addition to 100bps prudently provided in 4Q20).

Further re-rating warranted; reiterate Buy with increased TP of INR490

After a 35% run-up in the past 3 months, valuations do reflect better-than-expected recovery trends. That said, we think investors will again start focusing on normalised ROEs and growth once the recognition cycle is behind us and we think Bandhan will see a faster ramp-up in growth and profitability, which will continue to drive a re-rating. Accordingly, we now assign a ~20% higher target P/BV (3.3x vs 2.7x earlier) and roll forward to FY23F to arrive at a TP of INR490 and expect ROEs to normalise to ~21%-22% by FY22/23F.

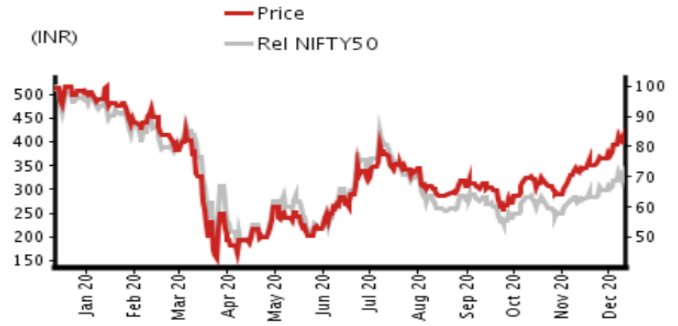
Year-end 31 Mar	FY20	FY21F		FY22F		FY23F	
Currency (INR)	Actual	Old	New	Old	New	Old	New
PPOP (mn)	54,466	60,715	60,715	67,411	67,411	78,721	78,721
Reported net profit (mn)	30,239	26,823	26,823	40,493	40,493	47,547	47,547
Normalised net profit (mn)	30,239	26,823	26,823	40,493	40,493	47,547	47,547
FD normalised EPS	18.78	16.66	16.66	25.15	25.15	29.53	29.53
FD norm. EPS growth (%)	14.8	-11.3	-11.3	51.0	51.0	17.4	17.4
FD normalised P/E (x)	22.5	–	25.4	–	16.8	–	14.3
Price/adj. book (x)	4.5	–	4.0	–	3.4	–	2.8
Price/book (x)	4.5	–	4.0	–	3.4	–	2.8
Dividend yield (%)	–	–	1.1	–	1.4	–	1.4
ROE (%)	22.9	16.6	16.6	21.7	21.7	21.5	21.5
ROA (%)	4.1	2.7	2.7	3.6	3.6	3.6	3.6

Source: Company data, Nomura estimates

See Appendix A-1 for analyst certification, important disclosures and the status of non-US analysts.

Key Data on Bandhan Bank

Relative Performance Chart



Performance

(%)	1M	3M	12M		
Absolute (INR)	24.8	35.7	-17.8	M cap (USDmn)	9,253.1
Absolute (USD)	25.9	35.5	-21.0	Free float (%)	12.8
Rel to NIFTY50	19.1	18.2	-31.0	3-mth ADT (USDmn)	50.3

Profit and loss (INRmn)

Year-end 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Interest income	66,441	108,855	120,924	138,253	161,595
Interest expense	-21,480	-45,616	-47,788	-54,023	-62,653
Net interest income	44,961	63,239	73,136	84,230	98,942
Net fees and commissions	4,483	5,937	6,627	7,667	8,986
Trading related profits	378	567	708	886	1,107
Other operating revenue	5,770	8,989	10,271	11,496	13,559
Non-interest income	10,630	15,493	17,606	20,048	23,652
Operating income	55,591	78,732	90,742	104,279	122,594
Depreciation	-782	-938	-1,126	-1,351	-1,621
Amortisation	0	0	0	0	0
Operating expenses	-7,241	-9,657	-12,554	-15,065	-17,776
Employee share expense	-10,087	-13,670	-16,348	-20,452	-24,475
Pre-provision op profit	37,482	54,466	60,715	67,411	78,721
Provisions for bad debt	-7,598	-5,031	-24,855	-13,276	-15,156
Other provision charges	246	-8,900	0	0	0
Operating profit	30,131	40,536	35,860	54,135	63,565
Other non-op income	0	0	0	0	0
Associates & JCEs	0	0	0	0	0
Pre-tax profit	30,131	40,536	35,860	54,135	63,565
Income tax	-10,616	-10,297	-9,037	-13,642	-16,018
Net profit after tax	19,515	30,239	26,823	40,493	47,547
Minority interests	0	0	0	0	0
Other items	0	0	0	0	0
Preferred dividends	0	0	0	0	0
Normalised NPAT	19,515	30,239	26,823	40,493	47,547
Extraordinary items	0	0	0	0	0
Reported NPAT	19,515	30,239	26,823	40,493	47,547
Dividends	-4,188	0	-7,536	-9,420	-9,420
Transfer to reserves	15,327	30,239	19,287	31,073	38,127

Growth (%)

	FY19	FY20	FY21F	FY22F	FY23F
Net interest income	48.3	40.7	15.6	15.2	17.5
Non-interest income	50.5	45.7	13.6	13.9	18.0
Non-interest expenses	35.5	33.4	30.0	20.0	18.0
Pre-provision earnings	54.2	45.3	11.5	11.0	16.8
Net profit	45.0	55.0	-11.3	51.0	17.4
Normalised EPS	7.4	55.0	-11.3	51.0	17.4
Normalised FDEPS	45.0	14.8	-11.3	51.0	17.4
Loan growth	33.4	68.1	13.1	16.7	18.7
Interest earning assets	28.7	63.7	15.8	16.6	18.7
Interest bearing liabilities	28.1	67.9	12.4	14.5	18.4
Asset growth	27.4	62.5	15.6	15.1	18.5
Deposit growth	27.6	32.0	17.7	16.3	21.0

Source: Company data, Nomura estimates

Balance sheet (INRmn)

As at 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Cash and equivalents	35,042	63,449	66,062	66,175	78,364
Inter-bank lending	0	0	0	0	0
Deposits with central bank	0	0	0	0	0
Total securities	22,985	20,080	41,289	47,268	55,974
Other int earning assets	0	0	0	0	0
Gross loans	402,346	672,333	779,248	911,337	1,082,511
Less provisions	-5,912	-6,034	-25,539	-31,812	-38,511
Net loans	396,434	666,299	753,709	879,524	1,044,000
Long-term investments	100,375	153,518	173,436	197,354	232,178
Fixed assets	3,312	3,688	4,618	5,549	6,480
Goodwill	0	0	0	0	0
Other intangible assets	0	0	0	0	0
Other non IEAs	6,270	10,144	20,858	23,879	28,277
Total assets	564,417	917,178	1,059,973	1,219,750	1,445,274
Customer deposits	432,316	570,815	671,985	781,572	945,695
Bank deposits, CDs, debentures	0	0	0	0	0
Other int bearing liabilities	5,214	163,792	153,792	163,792	173,792
Total int bearing liabilities	437,530	734,607	825,777	945,364	1,119,487
Non-int bearing liabilities	14,870	30,617	62,954	72,071	85,346
Total liabilities	452,400	765,223	888,731	1,017,436	1,204,833
Minority interest	0	0	0	0	0
Common stock	11,931	16,102	16,102	16,102	16,102
Preferred stock	0	0	0	0	0
Retained earnings	100,087	135,852	155,139	186,212	224,339
Reserves for credit losses	0	0	0	0	0
Proposed dividends	0	0	0	0	0
Other equity	0	0	0	0	0
Shareholders' equity	112,017	151,955	171,242	202,314	240,441
Total liabilities and equity	564,417	917,178	1,059,973	1,219,750	1,445,274
Non-perf assets	8,196	9,928	36,485	45,446	55,015

Balance sheet ratios (%)

	FY19	FY20	FY21F	FY22F	FY23F
Loans to deposits	93.1	117.8	116.0	116.6	114.5
Equity to assets	19.8	16.6	16.2	16.6	16.6
Asset quality & capital					
NPAs/gross loans (%)	2.0	1.5	4.7	5.0	5.1
Bad debt charge/gross loans (%)	1.89	0.75	3.19	1.46	1.40
Loss reserves/assets (%)	1.05	0.66	2.41	2.61	2.66
Loss reserves/NPAs (%)	72.1	60.8	70.0	70.0	70.0
Tier 1 capital ratio (%)	27.9	24.9	24.9	25.3	25.5
Total capital ratio (%)	29.2	27.1	26.9	27.0	26.9
Per share					
Reported EPS (INR)	12.12	18.78	16.66	25.15	29.53
Norm EPS (INR)	12.12	18.78	16.66	25.15	29.53
FD norm EPS (INR)	16.36	18.78	16.66	25.15	29.53
DPS (INR)	3.51	0.00	4.68	5.85	5.85
PPOP PS (INR)	23.28	33.82	37.71	41.86	48.89
BVPS (INR)	93.89	94.37	106.34	125.64	149.32
ABVPS (INR)	94.04	93.80	106.34	125.64	149.32
NTAPS (INR)	93.89	94.37	106.34	125.64	149.32

Valuations and ratios

	FY19	FY20	FY21F	FY22F	FY23F
Reported P/E (x)	34.9	22.5	25.4	16.8	14.3
Normalised P/E (x)	34.9	22.5	25.4	16.8	14.3
FD normalised P/E (x)	25.9	22.5	25.4	16.8	14.3
Dividend yield (%)	0.8	–	1.1	1.4	1.4
Price/book (x)	4.5	4.5	4.0	3.4	2.8
Price/adjusted book (x)	4.5	4.5	4.0	3.4	2.8
Net interest margin (%)	12.07	11.44	9.87	9.78	9.76
Yield on assets (%)	17.83	19.69	16.33	16.06	15.95
Cost of int bearing liab (%)	5.51	7.78	6.13	6.10	6.07
Net interest spread (%)	12.32	11.90	10.20	9.96	9.88
Non-interest income (%)	19.1	19.7	19.4	19.2	19.3
Cost to income (%)	32.6	30.8	33.1	35.4	35.8
Effective tax rate (%)	35.2	25.4	25.2	25.2	25.2
Dividend payout (%)	21.5	0.0	28.1	23.3	19.8
ROE (%)	19.0	22.9	16.6	21.7	21.5
ROA (%)	3.87	4.08	2.71	3.55	3.57
Operating ROE (%)	29.3	30.7	22.2	29.0	28.7
Operating ROA (%)	5.98	5.47	3.63	4.75	4.77

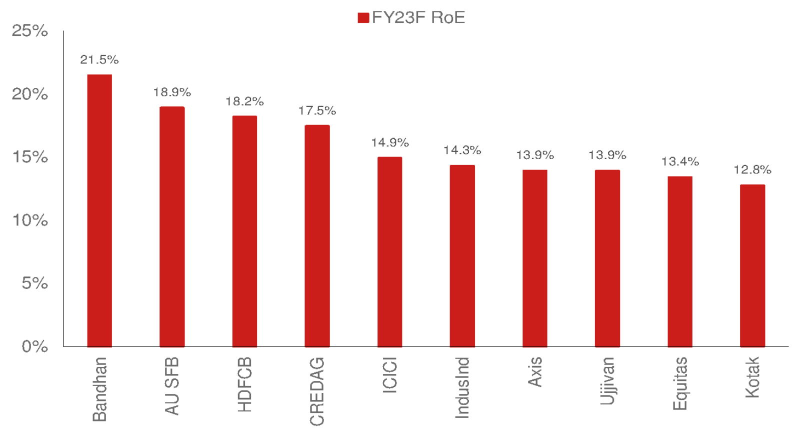
Source: Company data, Nomura estimates

Fig. 197: We value Bandhan Bank at INR490/ share based on a 3.3x FY23F book multiple

Valuation Summary	
FY23F RoE	21.5%
Mar-22 PT	**490**
Implied Mar-23F P/B	**3.3**
Implied Mar-23F P/E	**16.6**
Mar-23F BVPS	149
Mar-23F EPS	30

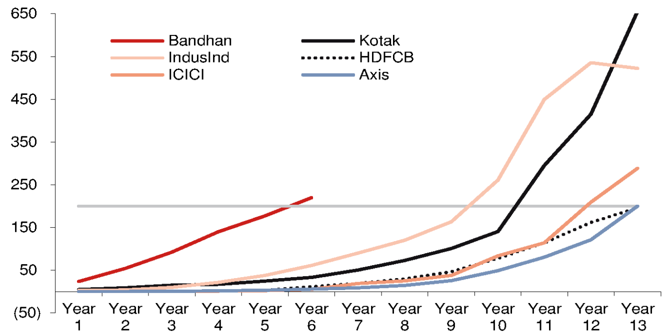
Source: Company data, Nomura estimates

Fig. 198: We expect Bandhan to deliver best-in-class normalized RoEs by FY23F



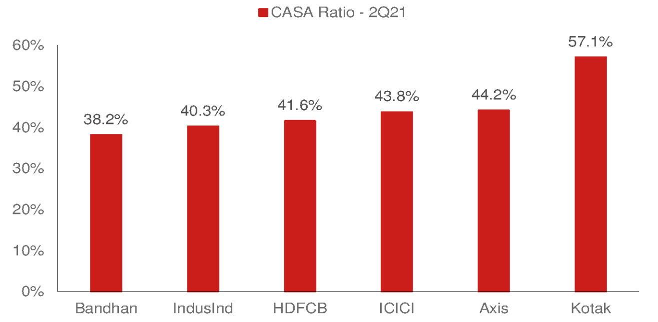
Source: Company data, Nomura estimates

Fig. 199: Bandhan has scaled to INR200bn SA deposits within 5.5 years of becoming a bank vs top pvt banks taking >10 years



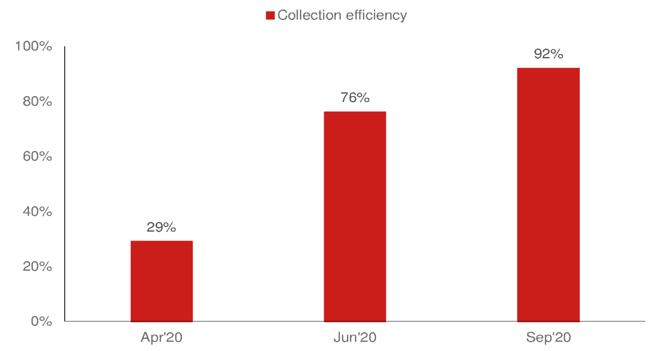
Note: For IndusInd, we have considered Year 1 as FY07-08, the year in which new management under the leadership of Mr. Sobti was appointed.
Source: Company data, Nomura research

Fig. 200: Strong CASA performance for Bandhan



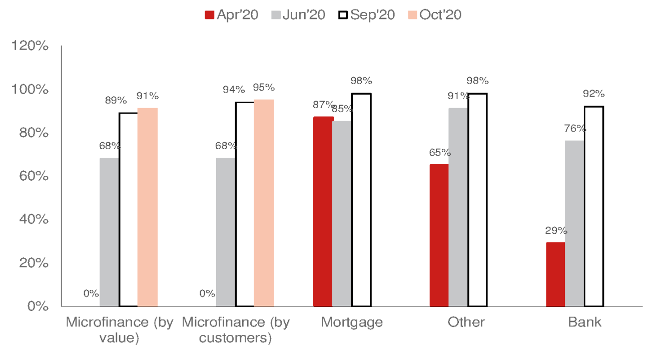
Source: Company data, Nomura research

Fig. 201: Collection efficiency improves to 92% in September (overall basis)



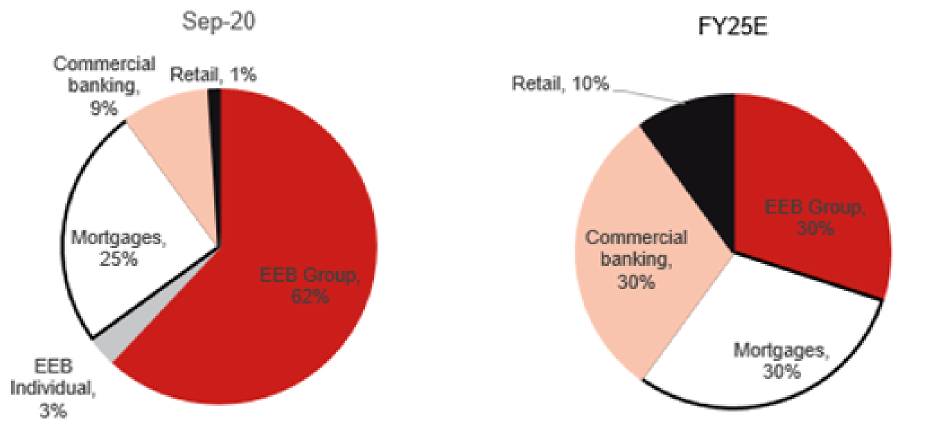
Source: Company data, Nomura research

Fig. 202: Product-wise collection efficiency trends: m/m improvement in micro-banking takes a pause in October



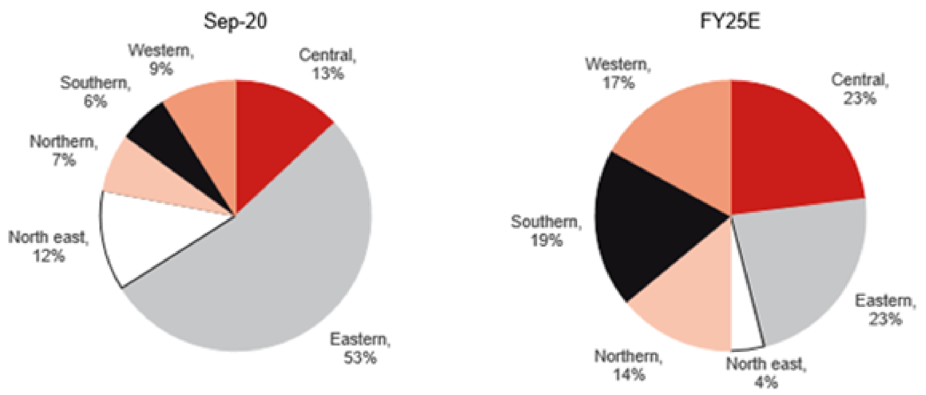
Source: Company data, Nomura research

Fig. 203: 5-year plan: Targeting a more balanced product mix with EEB (Microfinance) reducing to 30% from >60% currently



Note: EEB – Emerging entrepreneurs business; FY25F commercial banking portfolio includes EEB Individual book
Source: Company data, Nomura research

Fig. 204: 3x increase in bank branches planned: East + North east concentration to reduce from 65% currently to 27% by FY25E



Source: Company data, Nomura research

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Global Markets Research

11 December 2020

Equitas Holdings EQHL.NS EQUITAS IN

EQUITY: FINANCIALS

Probability of dual structure removal higher now

Reiterate Buy on undemanding valuations and lower holdco discount

Rating Remains	**Buy**
Target price Increased from INR 70	**INR 95**
Closing price 09 December 2020	**INR 73**
Implied upside	**+30.1%**
Market Cap (USD mn)	337.1
ADT (USD mn)	3.3

Action: Assuming lower holdco discount now; TP increased to INR95

With the recent RBI discussion paper (*link*) on harmonising banking guidelines, we see a higher probability of holdco discounts reducing: (1) **Proposal to remove NOFHC (Non-operative financial holding company) structure with no other business interest** – while SFB (small finance bank) holdcos are not registered as NOFHCs, we now see a higher probability of RBI permitting a reverse merger as these holdcos have no other operational businesses; (2) **Dilution overhang reduces** - we see supply risks and any merger/acquisition risks to reduce materially as the discussion paper no more requires promoter stake to come down to 40% within 5 years (26% cap in 15 years), and also interim dilution targets between 5-15 years are proposed to be removed.

Fundamentally, we think SFBs are not the best positioned to absorb COVID-19 impact, as regulatory and branch banking requirements continue to weigh on core profitability. That said, we think valuations adequately reflect higher risks. For SFBs, technical overhangs have dragged stock performance in the past 2 years and with increasing probability of these overhangs going away, we now assign a lower holdco discount (20% vs 40% earlier). While the market is still awaiting better clarity, we find risk-reward favorable to play for reducing holdco discount as valuations remain reasonable and growth/ asset quality recovery is better than we had expected (*link*).

Strong bounce-back in growth momentum and collections

Collection efficiency bounced back to 87% in Oct 2020 (94% incl. arrears). Collections still lag in commercial-vehicle (CV) loans at 78% (88% incl. arrears), while those in MFI (91%) are in line with peers. In small-business loans, collections improved to 88% (103% incl. arrears), with near normalization in the 0DPD bucket. Business momentum also picked up pace, and while 2Q21 disbursements were still down 20% y-y, they picked up sharply q/q. Liabilities too registered a sharp improvement with CASA improving 370bp q-q to 17% (on liabilities).

Market still not assigning lower holdco discounts

Holdco discounts (27% based on current prices) have come-off highs, but remain elevated given further clarity is required, in our view. However, we think the increasing probability of a reverse merger being allowed and reasonable valuations at 0.8x FY23F book limit the downside risk. We hence re-iterate Buy and assign a lower holdco discount of 20%. We further roll over to FY23F and value Equitas at 1.1x FY23F book for an ROE expectation of ~13% (FY23F).

Year-end 31 Mar	FY20	FY21F		FY22F		FY23F	
Currency (INR)	Actual	Old	New	Old	New	Old	New
PPOP (mn)	5,976	8,059	8,059	9,137	9,137	11,211	11,211
Reported net profit (mn)	2,437	2,895	2,895	3,735	3,735	5,508	5,508
Normalised net profit (mn)	2,437	2,895	2,895	3,735	3,735	5,508	5,508
FD normalised EPS	7.14	8.48	8.48	10.94	10.94	16.13	16.13
FD norm. EPS growth (%)	15.4	18.8	18.8	29.0	29.0	47.5	47.5
FD normalised P/E (x)	10.2	–	8.6	–	6.6	–	4.5
Price/adj. book (x)	0.9	–	0.8	–	0.7	–	0.6
Price/book (x)	0.9	–	0.7	–	0.6	–	0.6
Dividend yield (%)	–	–	–	–	–	–	–
ROE (%)	9.7	9.3	9.3	10.3	10.3	13.4	13.4
ROA (%)	1.4	1.3	1.3	1.4	1.4	1.7	1.7

Source: Company data, Nomura estimates

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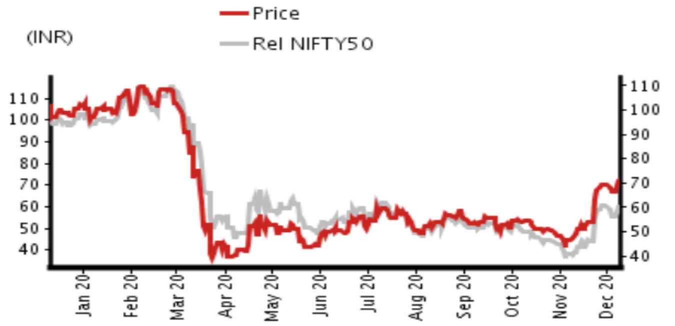
Key Data on Equitas Holdings

Relative Performance Chart



Performance

(%)	1M	3M	12M		
Absolute (INR)	60.9	40.1	-34.4	M cap (USDmn)	337.1
Absolute (USD)	62.1	40.0	-36.6	Free float (%)	85.7
Rel to NIFTY50	52.3	20.1	-47.7	3-mth ADT (USDmn)	3.3

Profit and loss (INRmn)

Year-end 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Interest income	21,119	26,454	32,646	39,480	46,460
Interest expense	-9,602	-11,501	-14,721	-19,274	-22,175
Net interest income	11,517	14,953	17,925	20,206	24,284
Net fees and commissions	186	210	263	329	411
Trading related profits	33	34	41	53	68
Other operating revenue	2,610	2,579	2,227	3,374	4,123
Non-interest income	2,829	2,824	2,531	3,755	4,603
Operating income	14,346	17,777	20,456	23,962	28,887
Depreciation	-918	-965	-1,157	-1,389	-1,667
Amortisation	0	0	0	0	0
Operating expenses	-3,654	-3,738	-3,626	-4,533	-5,439
Employee share expense	-5,513	-7,098	-7,613	-8,903	-10,570
Pre-provision op profit	4,261	5,976	8,059	9,137	11,211
Provisions for bad debt	-890	-1,470	-4,589	-4,144	-3,848
Other provision charges	-134	-996	400	0	0
Operating profit	3,237	3,510	3,870	4,993	7,363
Other non-op income	0	0	0	0	0
Associates & JCEs	0	0	0	0	0
Pre-tax profit	3,237	3,510	3,870	4,993	7,363
Income tax	-1,132	-1,073	-975	-1,258	-1,855
Net profit after tax	2,106	2,437	2,895	3,735	5,508
Minority interests	0	0	0	0	0
Other items	0	0	0	0	0
Preferred dividends	0	0	0	0	0
Normalised NPAT	2,106	2,437	2,895	3,735	5,508
Extraordinary items	0	0	0	0	0
Reported NPAT	2,106	2,437	2,895	3,735	5,508
Dividends	0	0	0	0	0
Transfer to reserves	2,106	2,437	2,895	3,735	5,508

Growth (%)

	FY19	FY20	FY21F	FY22F	FY23F
Net interest income	33.8	29.8	19.9	12.7	20.2
Non-interest income	17.3	-0.2	-10.4	48.4	22.6
Non-interest expenses	31.3	2.3	-3.0	25.0	20.0
Pre-provision earnings	93.1	40.2	34.9	13.4	22.7
Net profit	561.5	15.7	18.8	29.0	47.5
Normalised EPS	561.5	15.4	18.8	29.0	47.5
Normalised FDEPS	561.5	15.4	18.8	29.0	47.5
Loan growth	50.5	18.6	26.1	24.5	23.4
Interest earning assets	48.3	17.8	26.7	24.4	23.5
Interest bearing liabilities	20.4	22.7	35.8	15.1	19.4
Asset growth	18.5	22.5	34.3	12.7	17.8
Deposit growth	60.7	19.8	28.8	20.6	26.3

Source: Company data, Nomura estimates

Balance sheet (INRmn)

As at 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Cash and equivalents	8,579	21,560	28,649	17,233	10,841
Inter-bank lending	0	0	0	0	0
Deposits with central bank	4,027	3,809	5,730	6,893	8,673
Total securities	0	0	0	0	0
Other int earning assets	0	0	0	0	0
Gross loans	117,043	139,169	178,179	223,130	275,899
Less provisions	-1,093	-1,697	-4,870	-7,317	-9,589
Net loans	115,950	137,472	173,309	215,813	266,311
Long-term investments	23,445	23,425	43,476	47,032	54,707
Fixed assets	2,373	2,128	1,882	1,636	1,391
Goodwill	0	0	0	0	0
Other intangible assets	0	0	0	0	0
Other non IEAs	3,253	4,752	6,314	3,798	2,389
Total assets	157,627	193,145	259,361	292,407	344,311
Customer deposits	90,067	107,884	138,916	167,505	211,488
Bank deposits, CDs, debentures	2,800	5,030	2,200	2,200	2,200
Other int bearing liabilities	36,930	46,319	75,112	79,262	83,593
Total int bearing liabilities	129,798	159,233	216,228	248,966	297,281
Non-int bearing liabilities	5,286	6,471	8,599	5,173	3,254
Total liabilities	135,084	165,704	224,827	254,139	300,535
Minority interest	0	0	0	0	0
Common stock	3,415	3,415	3,415	3,415	3,415
Preferred stock	0	0	0	0	0
Retained earnings	19,129	24,027	31,119	34,853	40,361
Reserves for credit losses	0	0	0	0	0
Proposed dividends	0	0	0	0	0
Other equity	0	0	0	0	0
Shareholders' equity	22,543	27,441	34,533	38,268	43,775
Total liabilities and equity	157,627	193,145	259,361	292,407	344,311
Non-perf assets	2,957	4,173	9,740	13,304	15,981

Balance sheet ratios (%)

	FY19	FY20	FY21F	FY22F	FY23F
Loans to deposits	130.0	129.0	128.3	133.2	130.5
Equity to assets	14.3	14.2	13.3	13.1	12.7
Asset quality & capital					
NPAs/gross loans (%)	2.5	3.0	5.5	6.0	5.8
Bad debt charge/gross loans (%)	0.76	1.06	2.58	1.86	1.39
Loss reserves/assets (%)	0.69	0.88	1.88	2.50	2.78
Loss reserves/NPAs (%)	37.0	40.7	50.0	55.0	60.0
Tier 1 capital ratio (%)	20.9	22.4	22.8	20.4	19.1
Total capital ratio (%)	22.4	23.6	23.7	21.4	20.1
Per share					
Reported EPS (INR)	6.19	7.14	8.48	10.94	16.13
Norm EPS (INR)	6.19	7.14	8.48	10.94	16.13
FD norm EPS (INR)	6.19	7.14	8.48	10.94	16.13
DPS (INR)	0.00	0.00	0.00	0.00	0.00
PPOP PS (INR)	12.52	17.50	23.60	26.76	32.83
BVPS (INR)	66.02	80.37	101.13	112.07	128.20
ABVPS (INR)	63.16	76.78	95.43	106.23	123.52
NTAPS (INR)	66.02	80.37	101.13	112.07	128.20

Valuations and ratios

	FY19	FY20	FY21F	FY22F	FY23F
Reported P/E (x)	11.7	10.2	8.6	6.6	4.5
Normalised P/E (x)	11.7	10.2	8.6	6.6	4.5
FD normalised P/E (x)	11.7	10.2	8.6	6.6	4.5
Dividend yield (%)	–	–	–	–	–
Price/book (x)	1.1	0.9	0.7	0.6	0.6
Price/adjusted book (x)	1.1	0.9	0.8	0.7	0.6
Net interest margin (%)	11.47	11.45	11.19	10.06	9.76
Yield on assets (%)	21.02	20.25	20.38	19.65	18.67
Cost of int bearing liab (%)	8.08	7.96	7.84	8.29	8.12
Net interest spread (%)	12.94	12.29	12.54	11.37	10.55
Non-interest income (%)	19.7	15.9	12.4	15.7	15.9
Cost to income (%)	70.3	66.4	60.6	61.9	61.2
Effective tax rate (%)	35.0	30.6	25.2	25.2	25.2
Dividend payout (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	9.8	9.7	9.3	10.3	13.4
ROA (%)	1.45	1.39	1.28	1.35	1.73
Operating ROE (%)	15.1	14.0	12.5	13.7	17.9
Operating ROA (%)	2.23	2.00	1.71	1.81	2.31

Source: Company data, Nomura estimates

Fig. 205: We value Equitas Holdings at INR95 based on 1.1x FY23F book and lower holdco discount (20% vs 40% earlier)

Equitas SFB (opco)	FY20	FY21F	FY22F	FY23F
Networth	27,441	34,533	38,268	43,775
BVPS	26.1	29.3	32.4	37.1
ROE	9.7%	9.3%	10.3%	13.4%
Target Multiple	**1.1**	**1.1**	**1.1**	**1.1**
Fair value	29	32	36	40
Listed price	**33.4**	**33.4**	**33.4**	**33.4**
Implied multiple	**1.28**	**1.14**	**1.03**	**0.90**

Equitas Holdco	FY20	FY21F	FY22F	FY23F
Stake in Bank	82%	82%	82%	82%
Fair value (per Holdco share - pre holdco disc)	81	91	101	114
Holdco discount	**20%**	**20%**	**20%**	**25%**
Fair value (per holdco share - post holdco disc)	65	73	81	86
Standalone BVPS (adj for subs invst)		4.2	4.2	4.2
Implied Value	**65**	**77**	**85**	**90**

Holdco discount working	AT LTP
Holdco discount	**27%**
Equitas holdco (fair price)	90
Equitas holdco (Listed price)	**73**

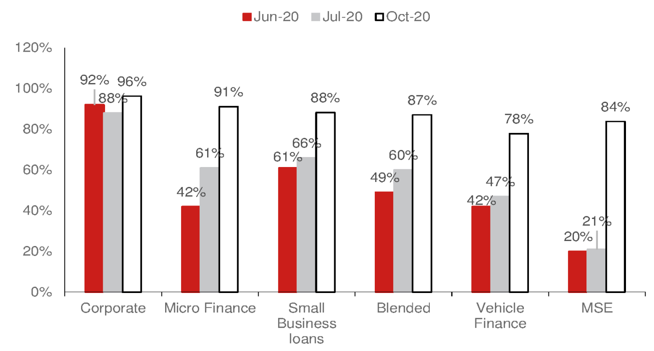
Source: Company data, Nomura estimates

Fig. 206: Expect RoEs to recover to 10-13% over FY22-23F

ROA decomposition	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21F	FY22F	FY23F
Net Interest Income/Assets	10.80%	10.55%	10.15%	6.20%	8.20%	8.05%	8.41%	7.78%	7.35%	7.62%
Fees/Assets	1.29%	1.39%	1.32%	2.51%	2.40%	1.96%	1.57%	1.08%	1.35%	1.42%
Investment profits/Assets	0.07%	0.13%	0.01%	0.19%	-0.10%	0.02%	0.02%	0.02%	0.02%	0.02%
Net revenues/Assets	**12.16%**	**12.07%**	**11.48%**	**8.90%**	**10.50%**	**10.03%**	**10.00%**	**8.88%**	**8.72%**	**9.06%**
Operating Expense/Assets	-6.69%	-6.47%	-6.08%	-5.91%	-8.40%	-7.05%	-6.64%	-5.38%	-5.39%	-5.55%
Provisions/Assets	-0.76%	-1.32%	-1.00%	-1.12%	-1.64%	-0.72%	-1.39%	-1.82%	-1.51%	-1.21%
Taxes/Assets	-1.64%	-1.48%	-1.57%	-0.66%	-0.16%	-0.79%	-0.60%	-0.42%	-0.46%	-0.58%
Total Costs/Assets	**-9.10%**	**-9.27%**	**-8.65%**	**-7.69%**	**-10.19%**	**-8.56%**	**-8.63%**	**-7.62%**	**-7.36%**	**-7.34%**
ROA	**3.07%**	**2.80%**	**2.83%**	**1.21%**	**0.30%**	**1.47%**	**1.37%**	**1.26%**	**1.36%**	**1.73%**
Equity/Assets	25.11%	25.04%	21.24%	19.42%	19.32%	15.02%	14.06%	13.45%	13.24%	12.87%
ROE	**12.21%**	**11.18%**	**13.31%**	**6.21%**	**1.57%**	**9.80%**	**9.75%**	**9.34%**	**10.26%**	**13.43%**
RORWA	**3.74%**	**3.30%**	**3.30%**	**1.81%**	**0.51%**	**2.49%**	**2.30%**	**2.28%**	**2.34%**	**2.79%**
LLP/average loans	0.93%	1.55%	1.17%	1.64%	2.20%	0.89%	1.09%	2.51%	2.07%	1.56%
Core PPOP	**5.40%**	**5.47%**	**5.38%**	**2.79%**	**2.20%**	**2.96%**	**3.34%**	**3.48%**	**3.30%**	**3.50%**

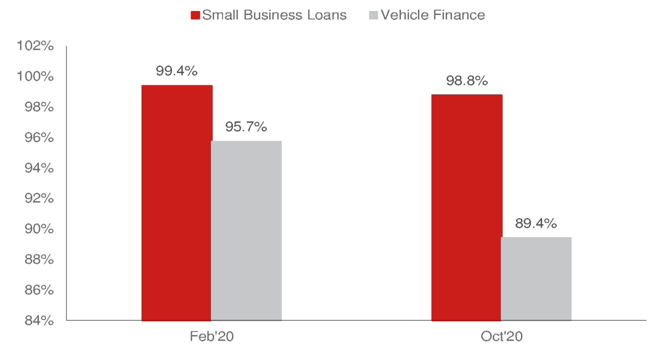
Source: Company data, Nomura estimates

Fig. 207: Overall collections improve to 87% (94% incl. arrears): CV still weak at 78%, while MFI in line with peers at 91%



Source: Company data, Nomura research

Fig. 208: 0Dpd buckets nearing normalized levels



Source: Company data, Nomura research

Key risks: Inability to sustain current improvement in collections and slower-than-expected pickup in growth momentum are key downside risks.

NOMURA

Global Markets Research

11 December 2020

Ujjivan Financial Services UJVF.NS UJJIVAN IN

EQUITY: FINANCIALS

Probability of dual structure removal higher now

Upgrade to Buy on lower holdco discount and comfortable capital position; raise TP to INR360

Rating Up from Neutral	**Buy**
Target price Increased from INR 250	**INR 360**
Closing price 09 December 2020	**INR 286**
Implied upside	**+25.9%**
Market Cap (USD mn)	472.4
ADT (USD mn)	2.9

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Action: Assuming lower holdco discount now; TP increased to INR360

With the recent RBI discussion paper (*link*) on harmonising banking guidelines, we see a higher probability of holdco discounts reducing: (1) **Proposal to remove NOFHC (non-operative financial holding company) structure with no other business interest** – while SFB (small finance bank) holdcos are not registered as NOFHCs, we now see a higher probability of RBI permitting a reverse merger as these holdcos have no other operational businesses; (2) **Dilution overhang reduces** - we expect supply risks and any merger/acquisition risks to reduce materially as the discussion paper no more requires promoter stake to come down to 40% within 5 years (26% cap in 15 years), and also interim dilution targets between 5-15 years are proposed to be removed.

Fundamentally, we think SFBs are not the best positioned to absorb COVID-19 impact, as regulatory and branch banking requirements continue to weigh on core profitability. That said, we think valuations adequately reflect higher risks. For SFBs, technical overhangs have dragged stock performance in the past 2 years and with increasing probability of these overhangs going away, we now assign a lower holdco discount (20% vs 40% earlier). While the market is still awaiting better clarity, we find risk-reward favorable to play for reducing holdco discount as valuations remain reasonable and growth/ asset quality recovery is better than we had expected (*link*).

Strong capital position to provide comfort

Oct collections at 88% (93% including arrears) (84% in Sep) and 78% collection efficiency in stressed states (30% of MFI AUM) reflect higher stress in the MFI book, but COVID-19 provision at 2.2% of AUM (2.9% of MFI AUM) gives some comfort. Overall, we remain circumspect on SFBs' ability to navigate the current crisis, given relatively lower PPOP/AUM at ~4.5%—ability to absorb impact is lower. That said, 2.9% COVID-19 provisions on MFI and strong capital position (Tier-1: 30%) provides comfort.

Markets still not assigning lower holdco discounts

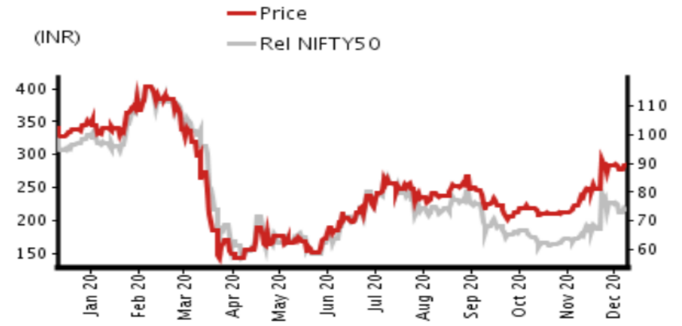
Holdco discounts (39% based on current prices) have come off their highs but still remain elevated given further clarity required, in our view. But we think increasing probability of a reverse merger being allowed and reasonable valuations at 1.2x FY23F book limit the downside risk. Hence, we reiterate our Buy stance and assign a lower holdco discount of 20%. We roll over to FY23F and value Ujjivan at 1.5x FY23F book for an ROE expectation of 14% (FY23F).

Year-end 31 Mar	FY20		FY21F		FY22F		FY23F
Currency (INR)	Actual	Old	New	Old	New	Old	New
PPOP (mn)	6,372	8,874	8,874	9,624	9,624	11,966	11,966
Reported net profit (mn)	3,499	2,701	2,701	4,020	4,020	5,698	5,698
Normalised net profit (mn)	3,499	2,701	2,701	4,020	4,020	5,698	5,698
FD normalised EPS	28.88	22.29	22.29	33.18	33.18	47.03	47.03
FD norm. EPS growth (%)	75.2	-22.8	-22.8	48.8	48.8	41.7	41.7
FD normalised P/E (x)	9.9	–	12.8	–	8.6	–	6.1
Price/adj. book (x)	1.1	–	1.0	–	0.9	–	0.8
Price/book (x)	1.1	–	1.0	–	0.9	–	0.8
Dividend yield (%)	–	–	0.6	–	0.6	–	0.6
ROE (%)	14.6	8.2	8.2	11.1	11.1	13.9	13.9
ROA (%)	2.2	1.4	1.4	1.8	1.8	2.1	2.1

Source: Company data, Nomura estimates

Key Data on Ujjivan Financial Services

Relative Performance Chart



Performance

(%)	1M	3M	12M		
Absolute (INR)	24.2	30.2	-17.7	M cap (USDmn)	472.4
Absolute (USD)	25.2	30.2	-20.4	Free float (%)	55.9
Rel to NIFTY50	15.7	10.2	-31.0	3-mth ADT (USDmn)	2.9

Profit and loss (INRmn)

Year-end 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Interest income	18,316	27,036	30,231	34,906	42,463
Interest expense	-7,252	-10,700	-11,260	-12,709	-15,309
Net interest income	11,064	16,336	18,971	22,197	27,154
Net fees and commissions	1,110	1,670	1,045	1,435	1,733
Trading related profits	97	146	189	208	229
Other operating revenue	853	1,406	1,498	1,798	2,309
Non-interest income	2,060	3,222	2,732	3,441	4,271
Operating income	13,124	19,557	21,704	25,638	31,425
Depreciation	-606	-1,436	-1,723	-2,068	-2,481
Amortisation	0	0	0	0	0
Operating expenses	-4,240	-4,564	-3,880	-5,043	-6,304
Employee share expense	-5,188	-7,185	-7,227	-8,902	-10,673
Pre-provision op profit	3,090	6,372	8,874	9,624	11,966
Provisions for bad debt	-406	-1,710	-5,263	-4,250	-4,348
Other provision charges	0	0	0	0	0
Operating profit	2,684	4,662	3,611	5,374	7,618
Other non-op income	0	0	0	0	0
Associates & JCEs	0	0	0	0	0
Pre-tax profit	2,684	4,662	3,611	5,374	7,618
Income tax	-692	-1,163	-910	-1,354	-1,920
Net profit after tax	1,992	3,499	2,701	4,020	5,698
Minority interests	0	0	0	0	0
Other items	0	0	0	0	0
Preferred dividends	0	0	0	0	0
Normalised NPAT	1,992	3,499	2,701	4,020	5,698
Extraordinary items	0	0	0	0	0
Reported NPAT	1,992	3,499	2,701	4,020	5,698
Dividends	-264	0	-207	-207	-207
Transfer to reserves	1,728	3,499	2,493	3,812	5,491

Growth (%)

Net interest income	29.1	47.6	16.1	17.0	22.3
Non-interest income	82.2	56.4	-15.2	25.9	24.1
Non-interest expenses	73.7	7.7	-15.0	30.0	25.0
Pre-provision earnings	-3.4	106.2	39.3	8.5	24.3
Net profit	2,668.9	75.6	-22.8	48.8	41.7
Normalised EPS	2,634.8	75.2	-22.8	48.8	41.7
Normalised FDEPS	2,634.8	75.2	-22.8	48.8	41.7
Loan growth	43.9	33.1	8.7	24.2	21.5
Interest earning assets	47.2	35.2	5.8	23.3	20.9
Interest bearing liabilities	50.1	25.4	8.6	23.9	22.5
Asset growth	45.1	34.0	8.6	21.5	21.0
Deposit growth	95.6	46.1	15.0	25.0	30.0

Source: Company data, Nomura estimates

Balance sheet (INRmn)

As at 31 Mar	FY19	FY20	FY21F	FY22F	FY23F
Cash and equivalents	3,566	1,184	1,359	1,693	2,194
Inter-bank lending	0	0	0	0	0
Deposits with central bank	7,379	12,249	8,818	9,418	10,173
Total securities	0	0	0	0	0
Other int earning assets	0	0	0	0	0
Gross loans	106,228	141,533	157,158	196,009	238,432
Less provisions	-703	-1,097	-4,494	-6,380	-7,948
Net loans	105,525	140,436	152,664	189,629	230,484
Long-term investments	15,266	23,961	30,235	34,534	42,728
Fixed assets	2,845	3,005	3,165	3,325	3,486
Goodwill	0	0	0	0	0
Other intangible assets	0	0	0	0	0
Other non IEAs	2,842	3,277	3,768	4,334	4,984
Total assets	137,422	184,112	200,010	242,934	294,049
Customer deposits	73,794	107,805	123,976	154,969	201,460
Bank deposits, CDs, debentures	4,500	2,000	2,000	2,000	2,000
Other int bearing liabilities	39,161	37,533	34,031	41,304	39,466
Total int bearing liabilities	117,455	147,338	160,007	198,273	242,926
Non-int bearing liabilities	3,771	4,898	5,632	6,477	7,449
Total liabilities	121,226	152,235	165,639	204,751	250,375
Minority interest	0	0	0	0	0
Common stock	1,212	1,212	1,212	1,212	1,212
Preferred stock	0	0	0	0	0
Retained earnings	14,985	30,666	33,159	36,971	42,462
Reserves for credit losses	0	0	0	0	0
Proposed dividends	0	0	0	0	0
Other equity	0	0	0	0	0
Shareholders' equity	16,196	31,877	34,371	38,183	43,674
Total liabilities and equity	137,422	184,112	200,010	242,934	294,049
Non-perf assets	979	1,371	5,617	7,975	9,935

Balance sheet ratios (%)

Loans to deposits	144.0	131.3	126.8	126.5	118.4
Equity to assets	11.8	17.3	17.2	15.7	14.9
Asset quality & capital					
NPAs/gross loans (%)	0.9	1.0	3.6	4.1	4.2
Bad debt charge/gross loans (%)	0.38	1.21	3.35	2.17	1.82
Loss reserves/assets (%)	0.51	0.60	2.25	2.63	2.70
Loss reserves/NPAs (%)	71.8	80.0	80.0	80.0	80.0
Tier 1 capital ratio (%)	18.4	28.0	31.0	27.6	25.9
Total capital ratio (%)	18.9	28.8	31.8	29.6	28.6
Per share					
Reported EPS (INR)	16.48	28.88	22.29	33.18	47.03
Norm EPS (INR)	16.48	28.88	22.29	33.18	47.03
FD norm EPS (INR)	16.48	28.88	22.29	33.18	47.03
DPS (INR)	2.18	0.00	1.71	1.71	1.71
PPOP PS (INR)	25.57	52.59	73.24	79.43	98.75
BVPS (INR)	133.67	263.09	283.66	315.13	360.44
ABVPS (INR)	133.67	263.09	283.66	315.13	360.44
NTAPS (INR)	133.67	263.09	283.66	315.13	360.44

Valuations and ratios

Reported P/E (x)	17.3	9.9	12.8	8.6	6.1
Normalised P/E (x)	17.3	9.9	12.8	8.6	6.1
FD normalised P/E (x)	17.3	9.9	12.8	8.6	6.1
Dividend yield (%)	0.8	–	0.6	0.6	0.6
Price/book (x)	2.1	1.1	1.0	0.9	0.8
Price/adjusted book (x)	2.1	1.1	1.0	0.9	0.8
Net interest margin (%)	11.67	12.30	12.08	12.31	12.35
Yield on assets (%)	19.32	20.36	19.25	19.36	19.31
Cost of int bearing liab (%)	7.41	8.08	7.33	7.09	6.94
Net interest spread (%)	11.91	12.28	11.92	12.27	12.37
Non-interest income (%)	15.7	16.5	12.6	13.4	13.6
Cost to income (%)	76.5	67.4	59.1	62.5	61.9
Effective tax rate (%)	25.8	25.0	25.2	25.2	25.2
Dividend payout (%)	13.3	0.0	7.7	5.2	3.6
ROE (%)	13.0	14.6	8.2	11.1	13.9
ROA (%)	1.72	2.18	1.41	1.82	2.12
Operating ROE (%)	17.5	19.4	10.9	14.8	18.6
Operating ROA (%)	2.31	2.90	1.88	2.43	2.84

Source: Company data, Nomura estimates

Fig. 209: We value Ujjivan Financial Services at INR360/ share based on 1.5x FY23F book multiple and lower holdco discount (20% v/s 40% earlier)

Ujjivan SFB (opco)	FY20	FY21F	FY22F	FY23F
Networth	31,877	34,371	38,183	43,674
BVPS	18.45	19.89	22.09	25.27
ROE	14.6%	8.2%	11.1%	13.9%
Target Multiple	**1.50**	**1.50**	**1.50**	**1.50**
Fair value	27.7	29.8	33.1	37.9
Listed price	**39.4**	**39.4**	**39.4**	**39.4**
Implied multiple	**2.13**	**1.98**	**1.78**	**1.56**

Ujjivan Holdco	FY20	FY21F	FY22F	FY23F
Stake in Bank	83.3%	83.3%	83.3%	83.3%
Fair value (per Holdco share - pre holdco disc)	329	355	394	450
Holdco discount	20%	20%	20%	20%
Fair value (Holdco - post holdco disc)	**263**	**284**	**315**	**360**

Holdco discount working	At LTP
Holdco discount	**39%**
Ujjivan holdco (fair price)	360
Ujjivan holdco (Listed price)	**286**

Note: Priced as at close of markets on 9 December 2020
Source: Company data, Nomura estimates

Fig. 210: We expect RoEs to recover to 11-14% over FY22-23F

ROA decomposition	FY15	FY16	FY17	FY18	FY19	FY20	FY21F	FY22F	FY23F
Net Interest Income/Assets	10.39%	11.01%	10.44%	10.00%	9.95%	10.55%	10.23%	10.36%	10.43%
Fees/Assets	1.75%	1.55%	1.88%	1.25%	1.78%	1.99%	1.37%	1.51%	1.55%
Investment profits/Assets	0.16%	0.19%	0.22%	0.07%	0.08%	0.09%	0.10%	0.10%	0.09%
Net revenues/Assets	**12.30%**	**12.75%**	**12.54%**	**11.32%**	**11.80%**	**12.64%**	**11.70%**	**11.97%**	**12.07%**
Operating Expense/Assets	-7.40%	-6.48%	-6.72%	-7.59%	-9.02%	-8.52%	-6.92%	-7.48%	-7.47%
Provisions/Assets	-0.76%	-0.53%	-1.10%	-3.63%	-0.37%	-1.10%	-2.84%	-1.98%	-1.67%
Taxes/Assets	-1.40%	-2.00%	-1.67%	-0.02%	-0.62%	-0.75%	-0.49%	-0.63%	-0.74%
Total Costs/Assets	**-9.56%**	**-9.01%**	**-9.49%**	**-11.24%**	**-10.01%**	**-10.37%**	**-10.25%**	**-10.09%**	**-9.88%**
ROA	**2.74%**	**3.74%**	**3.05%**	**0.08%**	**1.79%**	**2.26%**	**1.46%**	**1.88%**	**2.19%**
Equity/Assets	20.03%	20.41%	21.66%	18.68%	13.79%	15.53%	17.86%	16.94%	15.72%
ROE	**13.67%**	**18.32%**	**14.06%**	**0.45%**	**12.99%**	**14.56%**	**8.15%**	**11.08%**	**13.92%**
RORWA			**2.89%**	**0.10%**	**2.55%**	**3.54%**	**2.41%**	**3.09%**	**3.56%**
LLP/average loans	0.86%	0.58%	1.28%	4.46%	0.44%	1.36%	3.58%	2.48%	2.07%
Core PPOP	**4.74%**	**6.09%**	**5.61%**	**3.66%**	**2.70%**	**4.02%**	**4.68%**	**4.40%**	**4.51%**

Source: Company data, Nomura estimates

Fig. 211: Overall collections (excl. arrears) up to 88%; MFI/MSE still lagging

Loan segment	% of total book	Collection efficiency % (ex additional EMIs/ pre-closures)							
		Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20
MicroBanking	74.5%	93%	2%	14%	53%	60%	68%	83%	88%
MSE	7.6%	82%	19%	17%	46%	60%	58%	76%	81%
Affordable Housing	11.8%	94%	32%	33%	52%	67%	71%	92%	93%
Personal Loan	NA	91%	44%	38%	62%	62%	62%	79%	88%
Vehicle Loans	NA	95%	33%	23%	67%	72%	68%	92%	91%
FIG Lending	3.6%	100%	77%	67%	86%	100%	100%	100%	100%
Total		**93%**	**5%**	**16%**	**54%**	**61%**	**69%**	**84%**	**88%**

Source: Company data, Nomura research

Fig. 212: Maharashtra, West-Bengal, Assam and Punjab collections still lagging at 78% (30% of MFI AUM); other states' MFI collections at 91%

			Collections %			
State	**Exposure INRbn**	**% of total MFI book**	**June**	**July**	**Sep**	**Oct**
Maharashtra	8.1	7.9%	27%	27%	71%	79%
West Bengal	15.7	15.2%	41%	52%	74%	78%
Assam	3.9	3.7%	39%	37%	70%	74%
Punjab	3.6	3.5%	NA	NA	78%	83%
Total MFI book	**103.4**					

Source: Company data, Nomura research

Key risks: Inability to consistently improve collections and an extended slowdown are key downside risks.

Appendix A-1

Analyst Certification

We, Amit Nanavati and Tanuj Kyal, hereby certify (1) that the views expressed in this Research report accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Research report, (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Research report and (3) no part of our compensation is tied to any specific investment banking transactions performed by Nomura Securities International, Inc., Nomura International plc or any other Nomura Group company.

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Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Bandhan Bank	BANDHAN IN	INR 423.2	11-Dec-2020	Buy	N/A	
CreditAccess Grameen	CREDAG IN	INR 767.5	09-Dec-2020	Buy	N/A	A4,A5,A6,A7
Equitas Holdings	EQUITAS IN	INR 72.55	09-Dec-2020	Buy	N/A	
Ujjivan Financial Services	UJJIVAN IN	INR 285.6	09-Dec-2020	Buy	N/A	

A4 The Nomura Group has had an investment banking services client relationship with the subject company during the past 12 months.

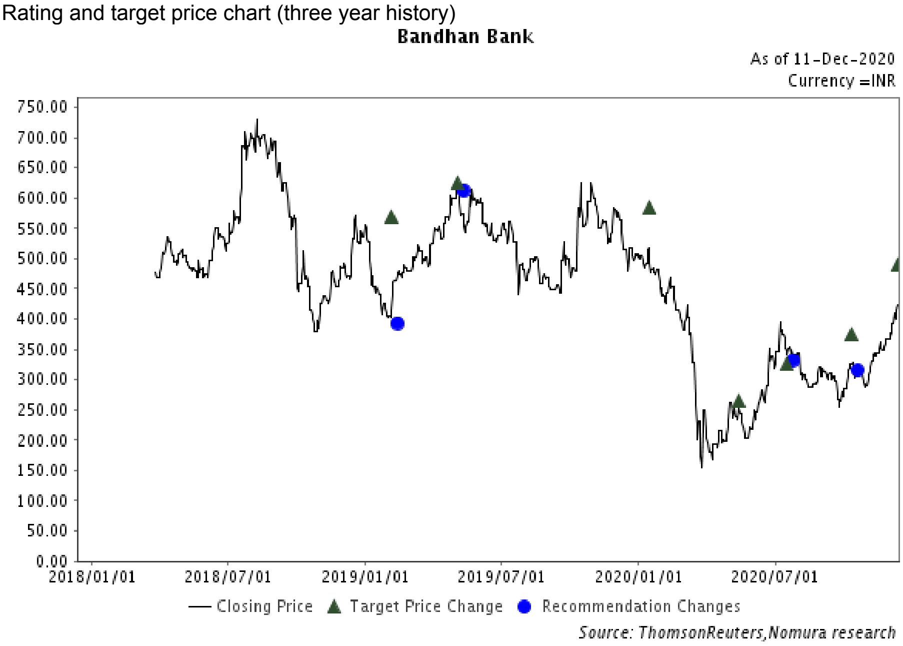
A5 The Nomura Group has received compensation for investment banking services from the subject company in the past 12 months.

A6 The Nomura Group expects to receive or intends to seek compensation for investment banking services from the subject company in the next three months.

A7 The Nomura Group has managed or co-managed a public or private offering of the subject company's securities in the past 12 months.

Bandhan Bank (BANDHAN IN) **INR 423.2 (11-Dec-2020)** Buy (Sector rating: N/A)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
11-Dec-20		490.00	423.20
10-Oct-20	Buy		325.45
10-Oct-20		375.00	325.45
16-Jul-20	Reduce		342.50
16-Jul-20		325.00	342.50
13-May-20		265.00	252.20
15-Jan-20		585.00	492.30
03-May-19	Neutral		622.50
03-May-19		625.00	622.50
04-Feb-19	Buy		403.80
04-Feb-19		570.00	403.80

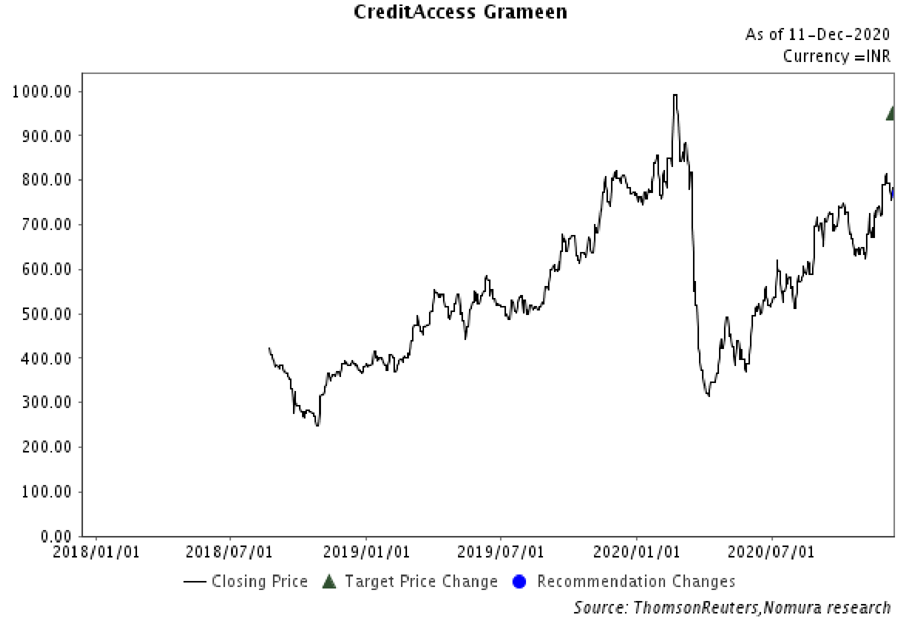
For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value Bandhan Bank at INR490 based on 3.3x Mar-23F P/B. The benchmark index for this stock in Nifty 50.

Risks that may impede the achievement of the target price Downside risks: Inability to maintain or improve collection efficiency from current levels and broader slowdown in economy are the key downside risks.

CreditAccess Grameen (CREDAG IN) **INR 767.5 (09-Dec-2020)** Buy (Sector rating: N/A)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
11-Dec-20	Buy		784.60
11-Dec-20		950.00	784.60

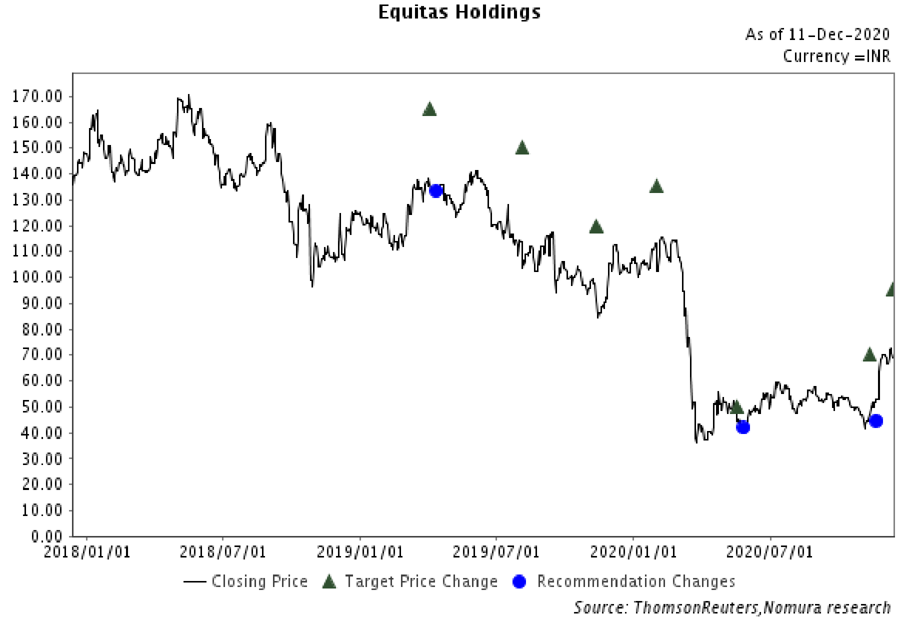
For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value CREDAG based on Residual income model to arrive at our target price of INR950 implying a 2.7x FY23F book multiple. We expect CREDAG to deliver 17-18% sustainably v/s cost of equity of 12-13%. The benchmark index is NIFYT50.

Risks that may impede the achievement of the target price Higher impact of COVID, inability to sustain current improvement in collections and concentration risks remains key risks.

Equitas Holdings (EQUITAS IN) **INR 72.55 (09-Dec-2020)** Buy (Sector rating: N/A)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
11-Dec-20		95.00	68.90
11-Nov-20	Buy		46.95
11-Nov-20		70.00	46.95
18-May-20	Neutral		44.25
18-May-20		50.00	44.25
31-Jan-20		135.00	109.10
11-Nov-19		120.00	90.80
05-Aug-19		150.00	103.85
04-Apr-19	Buy		135.70
04-Apr-19		165.00	135.70

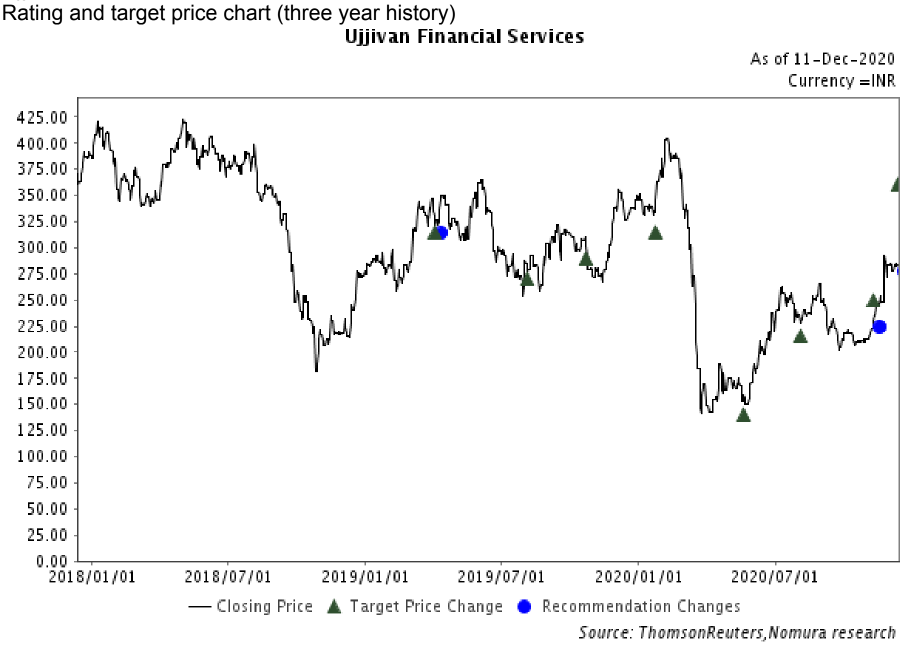
For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value Equitas Holdco at INR95/share which implies a muliple of 1.1x on Mar-23F book. We assign a holdco discount of 20% of the firm value. The benchmark index is NIFTY50.

Risks that may impede the achievement of the target price Inability to sustain current improvement in collections and slowr then expected pick-up in growth momentum is a key downside risk.

Ujjivan Financial Services (UJJIVAN IN) **INR 285.6 (09-Dec-2020)** Buy (Sector rating: N/A)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
11-Dec-20	Buy		282.85
11-Dec-20		360.00	282.85
09-Nov-20	Neutral		229.90
09-Nov-20		250.00	229.90
03-Aug-20		215.00	227.05
20-May-20		140.00	158.60
23-Jan-20		315.00	346.00
22-Oct-19		290.00	310.90
05-Aug-19		270.00	277.65
04-Apr-19	Reduce		319.95
04-Apr-19		315.00	319.95

For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value Ujjivan at 1.5x Mar-23 book and assign 20% holdco discount to arrive at INR360/share and value the bank at INR38/share. Nifty 50 is the benchmark index for this stock.

Risks that may impede the achievement of the target price Inability to consistently improve collections and extended slow-down are key downside risks.

Rating and target price changes

Issuer	Ticker	Old Stock Rating	New Stock Rating	Old Target Price	New Target Price
Bandhan Bank	BANDHAN IN	Buy	Buy	INR 375	INR 490
CreditAccess Grameen	CREDAG IN	Not Rated	Buy	N/A	INR 950
Equitas Holdings	EQUITAS IN	Buy	Buy	INR 70	INR 95
Ujjivan Financial Services	UJJIVAN IN	Neutral	Buy	INR 250	INR 360

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