

02nd November 2022

Fusion Microfinance - Subscribe

Investment Thesis

Fusion Microfinance Ltd. (FML) is coming out with an initial public offering (IPO) on November 02, 2022. Fusion Micro Finance IPO Size is Rs 1,104 Crores which has OFS for Rs 504Cr and fresh issue of Rs 600Cr. The IPO proceeds will be utilized to augment the company's capital base. FML provides financial services to underserved women across India in order to facilitate their access to greater economic opportunities. FML serves 2.90 million active borrowers through its network of 966 branches and 9,262 permanent employees spread across 377 districts in 19 states and union territories in India, as of 30 June 2022. Its share of AUM from customers in rural areas represented 91.37% of total AUM. Its focus customer segment is women in rural areas with an annual household income of up to Rs 3 lakhs. The company's business runs on a joint liability group-lending model, wherein a small number of women form a group (typically comprising five to seven members) and guarantee one another's loans. FML is well placed to offer an increasing variety of financial products in areas where financial services penetration remains limited on the back of a long history of serving rural customers, its customer-centric model and strong distribution network. Further, their focus remains continuously on understanding the financial needs coupled with consistent engagement and improving customers risk profile in rural areas. Fusion has a long history of serving rural markets with high growth potential in the microfinance segment. The microfinance industry (joint-liability group ("JLG") portfolio) has recorded healthy growth in the past few years. The industry's gross loan portfolio ("GLP") increased at a CAGR of 21% since the financial year 2018 to reach approximately Rs 3.1 trillion in the first quarter of the financial year 2023. The growth rate for NBFC-MFIs is the fastest as compared to other player groups. NBFC-MFI are expected to grow much faster rate of 22% as compared to the MFI industry at 18-20% CAGR between FY22-25. This growth is expected to be driven by penetration into newer states, faster growth in rural segment, expansion in average ticket size and support systems like credit bureaus. Microfinance sector in India is regulated by the RBI and its new regulatory regime suggests interest rate cap on loans given by NBFC-MFIs which has been effective from April 22, so this is helping players to adjust pricing in line with customer risk

Revenue from business Verticals

FML has the 4th fastest gross loan portfolio CAGR of 53.89% between the FY17 and FY21.

Particular (Cr.)	FY20	FY21	FY22	Q1FY22	Q1FY23
Net Interest Income	312.3	430.9	560.7	124.6	184.7
Pre-Provision Operating Profit	192.7	277.6	393.1	74.6	120.2
Profit After Tax	69.6	43.9	21.8	4.4	75.1
Gross Disbursement	3,574.0	3,710.3	6,179.8	761.5	1,983.0
Asset Under Management	3,606.5	4,637.8	6,786.0	4,631.1	7,389.0
Earning per Share	10.5	5.6	2.7	0.6	9.1
Gross NPA	1.1	5.5	5.7	6.2	3.7
Net NPA	0.4	2.2	1.6	2.8	1.4

IPO Details

Issue Open Date	2 nd November 2022
Issue Close Date	4 th November 2022
Price Band (Rs.)	Rs 350 – Rs 368
Issue Size (Rs in Cr)*	Rs. 1104Cr.
Issue Size (Mn. Shares)*	13.69 Shares
Market Lot	40 Shares
Listing Exchanges	NSE /BSE
Face Value (Rs.)	Rs. 10

* At highest price band

Key Details

Fresh Issue	Rs. 600 Cr
Issue Type	Book Building
Book Running Lead Manager	ICICI Securities, CLSA India Private Ltd., IIFL Securities, JM Financials Ltd.
Issue structure	QIB: 50% NII:15% Retail: 35%
Credit of Shares to Demat Account	14 th November 2022
Issue Listing Date	15 th November 2022

* At highest price band

and has maintained a track record of financial performance and operational efficiency through consistently high rates of customer acquisition and retention and low-cost expansion into underpenetrated areas. The total AUM grew at a CAGR of 37% from Rs. 3,607 Cr as of FY20 to Rs. 6,786 Cr as of FY22. Through such growth, Fusion has achieved a consistent reduction in cost to income ratio from 63% for FY19 to 44% for FY22 in the back of operating leverage. The average effective costs of borrowings have declined at a steady rate over the years. Fusion benefits from a large and diversified mix of lenders which has increased over the years and included 56 lenders as of June 30, 2022. Fusion also benefits from support of marquee investors, including Warburg Pincus LLC (will hold 39.4% stake post IPO vs 48.6% pre IPO), a leading private equity firm focused on growth investing across several sectors, and Creation Investments Fusion, LLC (will hold 23.7% stake post IPO vs 30.0% pre IPO), a leading alternative investment management company with a focus on private equity and private credit investments in emerging market financial services companies serving underserved and under banked clients, both of whom are now Fusion's promoters.

Key Business Highlights

FML has the 4th fastest gross loan portfolio CAGR of 53.89% between the financial years 2017 and 2021 and one of the youngest companies (in terms of obtaining an NBFC-MFI license) among the top NBFC-MFIs in India in terms of AUM as of June 30, 2022. As per CRISIL, Cost to Income ratio stands at 19%, with 3rd lowest Capital Adequacy ratio and Debt to Equity ratio among the top 10 NBFC-MFI Competitors in FY22. FML GNPA stands at 6th lower in FY22, with lowest average asset quality of 2.4% between FY15-FY22 among all the NBFC-MFIs. Income-generating loans typically fund businesses includes: Agriculture-allied and agriculture, Manufacturing and production, Trade and retail, Services, and Others. FML income-generating loans: Top-up loans, and Cross-sell loans

Valuation

FML is focused on maintaining an adequate liquidity buffer and plan to further increase its lender base to access funds from insurance, pension and provident funds, mutual funds, overseas lenders as well as external commercial borrowings ("ECBs") though the issuance of NCDs and commercial papers. FML already have existing borrowing arrangements with a large number of lenders and continuously engage with new institutions through which they may further diversify its sources of borrowings. FML has been able to raise Rs 10878 Cr in debt as well as Rs 573Cr in equity over the last three financial years and three months ending June 30, 2022.

FML has strong NII growth (CAGR of 38.27%) and healthy PPOP growth (CAGR of 60.98%) over period of FY19-FY22. Fusion has grown its AUM at a CAGR of 37% over FY20-22, one of the fastest amongst amongst listed financials. Company is well diversified and has extensive pan-India Presence with a low base of Rs. 7,389 Cr in AUM. The company also has access to diversified and recognized sources of capital and has a good financial track record.

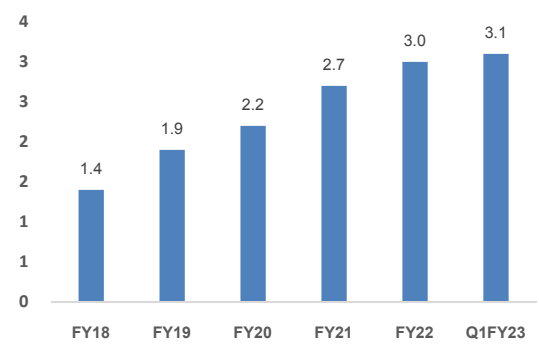
Company's profitability decline in past due to covid impact now it is on a revival trail as indicated by Q1FY23 based on these earnings we can say that sector is going from headwinds to tailwinds. Despite covid, Fusion has managed its GNPA/NNPA asset quality ratio below the 6%/3% mark over FY21 & 22. Fusion is well placed to deliver ROA/ROE in excess of 4%/20% on a sustained basis as compared to micro finance industry peers. The company offers a price-book (P/B) multiple of 1.8 on a post IPO basis, where its peers like credit Access command a P/B of 3.3. Thus, considering all the parameters fusion's valuation are at a discount compared to peers. **We recommend to 'Subscribe' to the issue.**

Risk & Concern

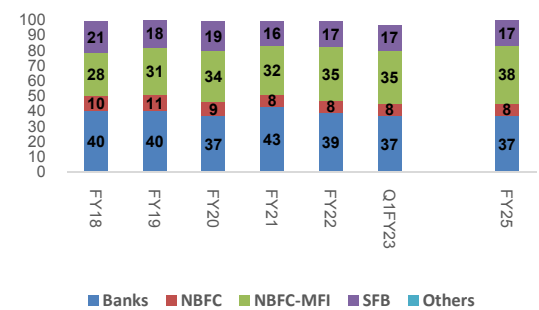
Competition from other MFIs, banks, financial institutions.
 Increase in NPAs may adversely affect business & earnings.
 Substantial collections, disbursements in cash exposes to operational risk.
 May have difficulties in managing opex structure if volumes of disbursement and size of AUM decline.

Graphs & Charts

Industry level GLP (lk. cr.)



NBFC-MFI to gain market share (%)



Disbursement & Collections

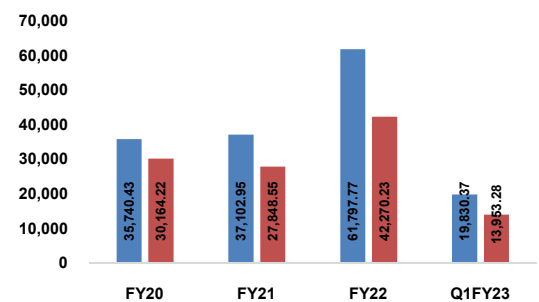
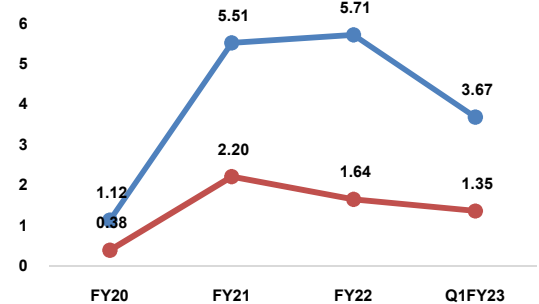


Fig.4: Gross NPA & Net NPA(Q1FY23)



Particular	Yield On Advances	Cost of borrowings	Net Interest Margins	Operating Expenditure	Cost to Income	Credit Costs
Top 10 NBFC-MFIs						
Credit Access Grameen	19.16%	8.18%	9.72%	3.25%	29.73%	3.27%
Fusion Microfinance	20.56%	9.72%	8.66%	4.76%	44.26%	5.62%
Asirvad microfinance	23.11%	11.22%	9.64%	6.51%	49.65%	6.28%
Muthoot Finance	18.04%	9.70%	7.50%	6.32%	61.47%	2.27%
Annapurna Finance	21.33%	10.16%	6.62%	5.75%	63.07%	3.00%
Samasta Mircofinance	20.54%	8.96%	10.91%	6.08%	52.59%	1.83%
Satin Creditcare	21.31%	10.47%	7.46%	5.58%	64.44%	2.30%
Svatantra Mircofinance Pvt.	17.74%	9.56%	6.37%	5.18%	54.33%	3.03%
Spandana Sphoorty	20.64%	11.64%	9.69%	4.10%	32.81%	6.13%
Belstar Microfinance	20.80%	9.17%	9.61%	5.27%	48.41%	3.73%
Banks & SFBs						
Bandhan Bank	13.88%	4.88%	6.87%	2.78%	30.54%	6.21%
Equitas SFB	17.33%	6.75%	7.89%	6.60%	66.12%	1.91%
Ujjivan SFB	16.73%	5.70%	8.07%	6.80%	71.68%	5.19%
Jan SFB	22.15%	7.58%	7.08%	5.80%	66.46%	2.90%
ESAF SFB	19.59%	5.99%	7.64%	5.74%	63.69%	2.78%
Utkarsh SFB	17.85%	6.92%	7.80%	5.41%	59.11%	3.04%
Fincare SFB	21.45%	7.07%	9.28%	6.85%	60.01%	4.51%
Suryoday SFB	18.72%	6.31%	7.85%	5.55%	60.93%	5.26%

Particular	CAGR	Net Interest Income				CAGR	Pre-Provision Operating Profits			
	(FY19-FY22)	FY22	FY21	FY20	FY19	(FY19-FY22)	FY22	FY21	FY20	FY19
Top 10 NBFC-MFIs										
Credit Access Grameen	17.69%	12.80%	36.06%	37.31%	62.04%	19.23%	48.46%	35.65%	32.90%	73.29%
Fusion Microfinance	38.27%	25.63%	25.42%	78.26%	159.82%	60.98%	10.39%	41.99%	198.57%	257.78%
Asirvad microfinance	16.25%	21.87%	-7.78%	66.41%	74.34%	3.81%	-6.03%	-25.54%	132.16%	133.33%
Muthoot Finance	8.74%	13.92%	23.98%	8.92%	50.32%	13.72%	-23.42%	429.54%	-33.18%	-25.86%
Annapurna Finance	24.05%	8.04%	NA	48.96%	42.60%	9.18%	-54.42%	NA	94.86%	-17.69%
Samasta Mircofinance	48.76%	35.74%	33.62%	85.82%	287.34%	68.62%	-24.59%	67.46%	141.09%	1032.29%
Satin Creditcare	1.73%	13.87%	-20.58%	52.35%	26.87%	-4.41%	23.57%	-32.65%	144.79%	7.90%
Svatantra Mircofinance Pvt.	45.83%	68.03%	21.85%	134.22%	139.94%	29.37%	312.51%	24.36%	245.51%	1439.40%
Spandana Sphoorty	5.09%	-18.91%	-1.84%	68.64%	87.52%	-2.93%	-37.00%	-3.82%	82.59%	101.72%
Belstar Microfinance	25.90%	33.57%	-8.98%	61.00%	80.80%	20.19%	44.17%	-22.05%	54.50%	103.99%
Banks & SFBs										
Bandhan Bank	24.68%	15.21%	19.60%	40.66%	48.28%	24.57%	9.36%	21.79%	45.13%	55.76%
Equitas SFB	20.97%	13.41%	20.26%	29.80%	33.84%	12.54%	-28.50%	48.78%	34.00%	251.12%
Ujjivan SFB	17.04%	2.63%	7.79%	47.68%	28.50%	39.21%	-44.23%	68.63%	205.66%	-53.64%
Jan SFB	47.07%	10.03%	NA	131.43%	11.77%	NA	16.28%	NA	NA	NA
ESAF SFB	26.01%	24.47%	16.37%	38.12%	103.30%	33.32%	-1.88%	50.95%	6.00%	NA
Utkarsh SFB	28.72%	26.40%	15.12%	46.57%	85.97%	23.88%	10.30%	16.50%	47.95%	435.20%
Fincare SFB	32.55%	24.99%	13.28%	64.48%	92.75%	41.89%	-3.54%	23.40%	139.98%	368.87%
Suryoday SFB	19.33%	42.38%	-16.31%	44.77%	106.94%	5.65%	109.35%	-62.52%	50.31%	349.12%

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