

BUY **UGRO Capital**

Your success is our success

Another quarter of solid progressBFSI - NBFCs ▶ Result Update ▶ **October 28, 2023****TARGET PRICE (Rs) : 425**

UGRO Capital reported a good set of numbers in Q2FY24, with growth in AUM (+74% YoY/+12% QoQ), Profitability (PAT: Rs289mn, over 14% YoY, and above 5x YoY) and Asset Quality (GS3/NS3: 2.85%/1.52%)—broadly conforming with Company guidance. UGRO's investments in tech, data and physical infra have delivered strong growth in the 'on-book' and 'off-book' (co-lending/co-origination), with reasonable asset quality driving stronger profitability growth, led by operating leverage. Overall, the Q2 results reaffirm our conviction on UGRO Capital's rising MSME specialist lender stature (refer to our coverage initiation: [The rise of an MSME specialist lender](#)). We reiterate our BUY rating on the stock, with unchanged Sep-24E Target Price of Rs425/share (implied FY25E P/BV: 2.1x), which offers ~40% upside.

UGRO Capital: Financial Snapshot (Standalone)

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net profits	146	398	1,319	2,683	3,671
AUM growths (%)	125.4	104.8	55.1	50.7	36.8
NII growths (%)	30.2	40.7	85.4	47.6	33.7
NIMs (%)	9.2	12.5	13.6	14.9	14.2
PPOP growth (%)	56.2	183.6	104.7	71.4	34.8
Adj. EPS (Rs)	2.1	5.7	14.4	24.9	34.0
Adj. EPS growth (%)	(49.4)	176.2	153.8	72.3	36.8
Adj. BV (INR)	137.0	142.0	181.4	206.3	240.3
Adj. BVPS growth (%)	1.4	3.6	27.8	13.7	16.5
RoA (%)	0.6	1.1	2.6	4.0	4.0
RoE (%)	1.5	4.1	9.4	12.8	15.2
P/E (x)	147.6	53.4	21.0	12.2	8.9
P/ABV (x)	2.2	2.1	1.7	1.5	1.3

Source: Company, Emkay Research

Strong performance boosts confidence on business model

UGRO's Q2 performance remained strong, with AUM growing 74% YoY/12% QoQ, led by healthy disbursement of over 20% growth across the products segment, barring Secured prime and Machine loans. Disbursement share of Unsecured product stayed the highest, leading to improvement in NIM. Income from the off-balance-sheet asset saw sequential growth of ~32%, which resulted in NIM+Fee expansion by 99bps QoQ, thus boosting our confidence on UGRO's strong partnership model of co-lending/co-origination. In terms of cost, opex was slightly elevated due to higher employee costs on account of branch expansion and increasing head-count. Q1 employee cost was low owing to reversal of Rs50mn from provisioning for employee bonus; employee cost in Q2FY24 is the actual normalized employee cost and would track similar levels. UGRO plans adding ~75 branches in the next two quarters, thus expanding presence across MP, UP, AP and its existing locations in the South.

Strong collection infra keeping collection efficiency steady

Collection efficiency for Sep-23 stood at 92% (97%, including overdue), a 1% improvement over Aug-23. Management stresses on its dynamic 'Early Warning System', which uses bureau data every quarter for existing and non-disbursed cases, for asserting the PD of disbursed and rejected loans, indicating customers' leverage level; this hence helps the company take proactive action regarding high-risk customers. Company has a Collections work-force of ~250, with a legal team that takes care of collections. Collection efficiency of the X-bucket stands at 95%.

UGRO Capital is our conviction BUY

Q2 results reaffirm our belief in the UGRO story. Our conviction about UGRO's strategy rests on 3 pillars: i) MSME-focused lending with large TAM. ii) Business model optimized for sectors, with stress on data homogeneity and underwriting tech models for six sigma events like GST/pandemic. iii) Its unique asset underwriting skills that can be symbiotically exploited to co-lend/co-originate with PSBs/others, which otherwise incur high credit cost on priority lending. UGRO would clock AUM growth of 3x to ~Rs194bn by FY26E and 54% EPS CAGR over FY24-26E. We reiterate our BUY on the stock, with unchanged Sep-24E TP of Rs425/share (implied FY25E P/BV: 2.1x).

Target Price – 12M	Sep-24
Change in TP (%)	NA
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	39.8
CMP (27-Oct-23) (Rs)	304.0

Stock Data	Ticker
52-week High (Rs)	320
52-week Low (Rs)	131
Shares outstanding (mn)	92.5
Market-cap (Rs bn)	28
Market-cap (USD mn)	338
Net-debt, FY24E (Rs mn)	560
ADTV-3M (mn shares)	-
ADTV-3M (Rs mn)	129.1
ADTV-3M (USD mn)	1.6
Free float (%)	-
Nifty-50	19,047
INR/USD	83.2
Shareholding, Sep-23	
Promoters (%)	2.2
FPIs/MFs (%)	19.2/5.8

Price Performance

(%)	1M	3M	12M
Absolute	3.5	16.4	70.5
Rel. to Nifty	7.2	20.2	58.8

1-Year share price trend (Rs)**Avinash Singh**

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Guidance

- PAT in H2 to grow at 20%, higher than that in H1 led by improved product mix, and resulting in 3% ROA in Q4FY24. Longer-term sustainable ROA and ROE guidance is 4% and 18%, respectively
- Operating cost to remain stable or see a marginal decline; would come below 45% by FY25.
- Almost 75 new branch additions in the next two quarters; Company is expanding presence in MP, UP and AP, and increasing its presence in its existing southern locations.
- AUM to grow over 30%, with targeted off-book at above 50% by FY25. AUM expected to reach ~Rs100bn by the end of FY24.
- Focus will be on improving margins, along with achieving the targeted AUM. AUM to reach near the aspirational target of ~Rs100bn.
- Credit cost to remain stable and see some improvement, sustaining below 2% levels beyond FY25. Management will avail the CGTMSE facility for all unsecured loans less than Rs1mn.
- In machinery finance, UGRO does not fund large machinery or parts of machinery, and will continue to follow the defined policy.

Exhibit 1: Strong quarterly performance

UGRO—Result snapshot (Rs mn)	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	QoQ change	YoY Change
AUM	43,750	50,960	60,810	67,770	75,920	12%	74%
Disbursement	16,530	18,740	23,130	20,270	25,070	24%	52%
NII	463	515	507	688	665	-3%	44%
NIMs (%)	6.2	6.4	5.8	7.4	6.6	-73bps	44bps
NII + Fees	808	1,001	1,186	1,206	1,392	15%	72%
NIMs + Fees (%)	10.82	12.47	13.63	12.88	13.88	99bps	306bps
Cost of Borrowing (%)	11.34	11.64	11.98	11.42	11.81	38bps	46bps
Opex-to-AUM (%)	5.48	5.83	5.07	4.30	4.61	32bps	-87bps
PPoP	258	311	429	515	563	9%	118%
Credit cost on AUM (%)	1.48	1.41	1.25	1.30	1.37	7bps	-11bps
Credit cost on on-book AUM (%)	1.98	2.08	2.01	2.24	2.45	21bps	47bps
PAT	53	131	140	252	289	14%	448%
Networth	9,549	9,687	9,840	13,373	13,710	3%	44%
AUM	43,750	50,960	60,810	67,770	75,920	12%	74%
Disbursement	11,640	14,590	14,590	12,790	14,770	15%	27%
GS3 (%)	2.16	2.46	2.46	2.67	2.85	18bps	69bps
NS3 (%)	1.51	1.58	1.31	1.45	1.52	7bps	1bps
GNPA % (GS3 on Total AUM)	1.70	1.70	1.60	1.80	1.92	12bps	22bps
NNPA % (NS3 on Total AUM)	1.20	1.10	0.90	1.00	1.00	0bps	-20bps
PCR (%)	31.8	38.0	48.6	48.0	49.0	100bps	1720bps

Source: Company, Emkay Research

Exhibit 2: Valuation

	CMP/TP (Rs/sh)	Upside	Mkt Cap (Rs bn)	P/BV			P/E			RoA (%)			RoE (%)			Book Value (Rs/sh)			EPS (Rs)		
				FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
At current market price	304	40%	28.1	1.7x	1.5x	1.3x	21.0x	12.2x	8.9x	2.6	4.0	4.0	9.4	12.8	15.2	181	206	240	14	25	34
At target price	425		28.1	2.3x	2.1x	1.8x	29.4x	17.1x	12.5x	2.6	4.0	4.0	9.4	12.8	15.2	181.4	206.3	240.3	14.4	24.9	34.0

Source: Company, Emkay Research

Exhibit 3: AUM mix

(Rs mn)	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
On-book	24,077.7	24,910	28,750	31,030	33,210	36,390	38,480	41,756
Off-book	1,812.3	4,780	7,820	12,720	17,750	24,420	29,290	34,164
Total AUM	25,890	29,690	36,570	43,750	50,960	60,810	67,770	75,920
On-book	93%	84%	79%	71%	65%	60%	57%	55%
Off-book	7%	16%	21%	29%	35%	40%	43%	45%

Source: Company, Emkay Research

Exhibit 4: Diverse product offering

Product-portfolio mix	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Prime - Secured Loans	31.4%	29.6%	28.7%	28.4%	29.3%	28.5%
Prime - Unsecured Loans	27.3%	28.8%	30.0%	31.2%	31.1%	31.3%
Micro Enterprise Loan	4.6%	5.5%	6.6%	7.8%	8.1%	8.4%
Supply Chain Financing	9.7%	9.1%	9.0%	9.3%	8.6%	8.8%
Machinery Loan	9.9%	10.6%	11.1%	11.5%	11.8%	11.8%
Partnerships & Alliances	17.0%	16.4%	14.6%	11.8%	11.1%	11.2%

Source: Company, Emkay Research

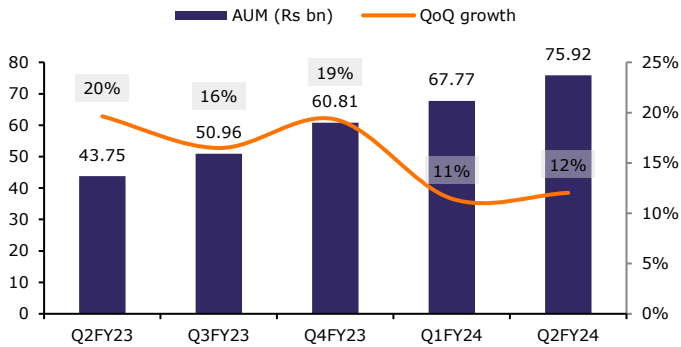
Exhibit 5: Increasing share of USL disbursement leading to yield improvement.

Disbursement mix	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Prime - Secured Loans	21.0%	22.8%	25.3%	24.7%	28.4%	20.6%
Prime - Unsecured Loans	33.3%	32.1%	33.2%	28.6%	33.5%	35.5%
Micro Enterprise Loan	9.9%	10.9%	11.7%	14.1%	11.8%	12.7%
Supply Chain Financing	55.5%	55.4%	66.6%	66.0%	59.3%	75.5%
Machinery Loan	7.2%	5.3%	5.6%	7.5%	0.9%	5.8%
Partnerships & Alliances	13.0%	11.4%	11.5%	11.9%	12.0%	11.3%

Source: Company, Emkay Research

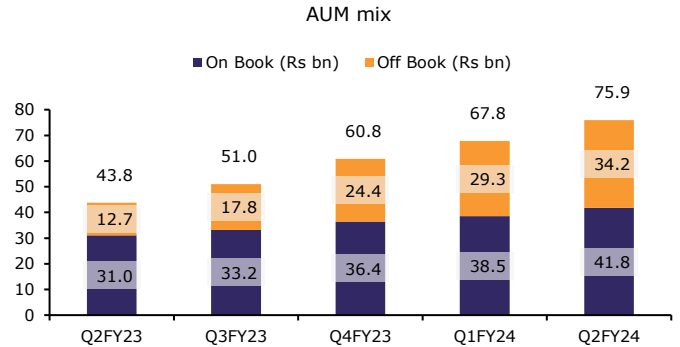
Result in charts

Exhibit 6: AUM growth led by strong disbursement across the products segment



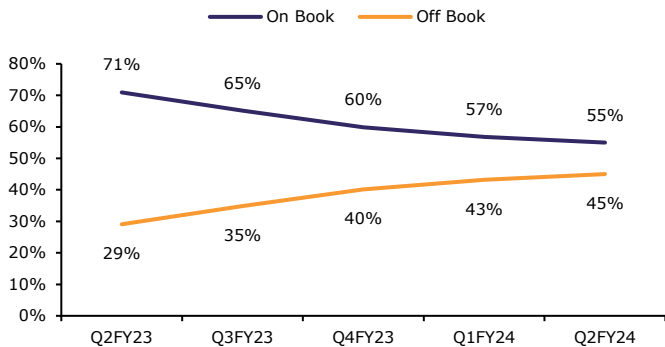
Source: Company, Emkay Research

Exhibit 7: Mix of on-book:off-book stood at 55:45



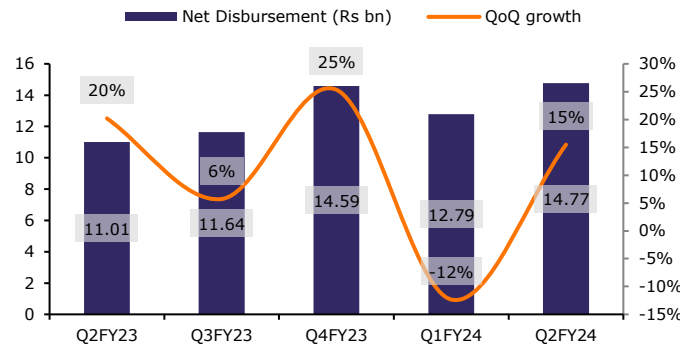
Source: Company, Emkay Research

Exhibit 8: UGRO's AUM mix moving swiftly towards its long-term target of 50:50



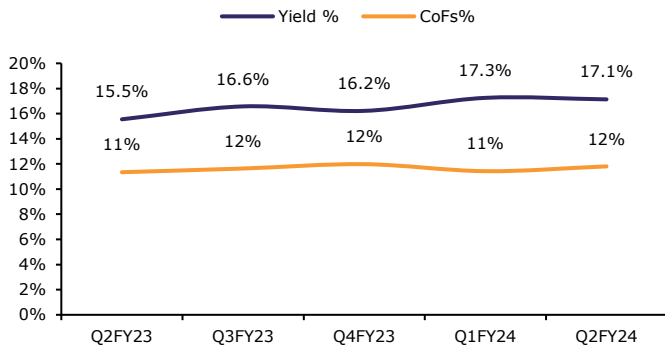
Source: Company, Emkay Research

Exhibit 9: Strong sequential disbursement growth of >20% in most of the products segment



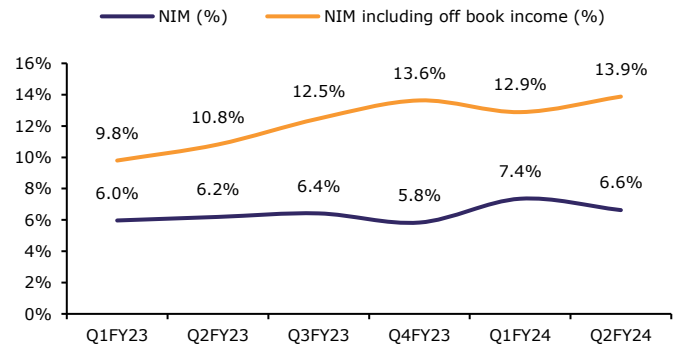
Source: Company, Emkay Research

Exhibit 10: Yield improvement led by increasing mix of high-yielding product



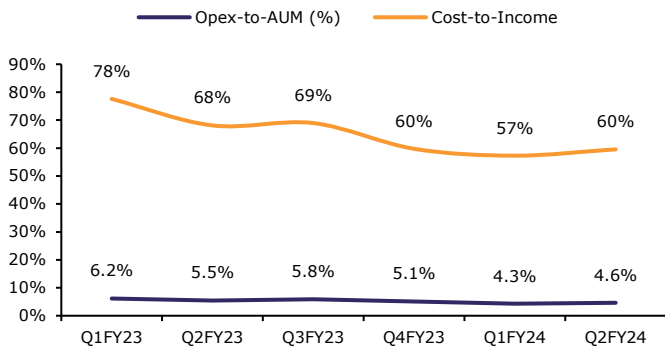
Source: Company, Emkay Research

Exhibit 11: Margin improvement led by increasing share of off-book lending.



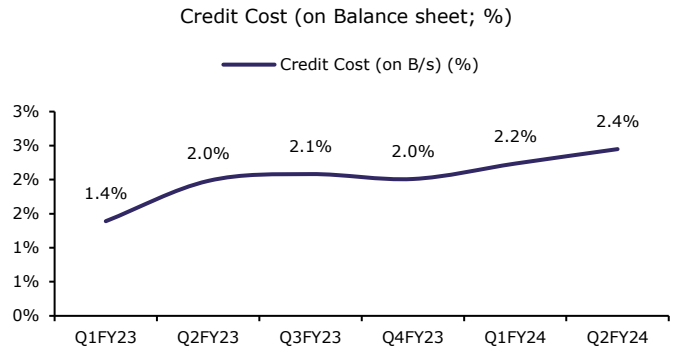
Source: Company, Emkay Research

Exhibit 12: Opex to moderate with increasing scale



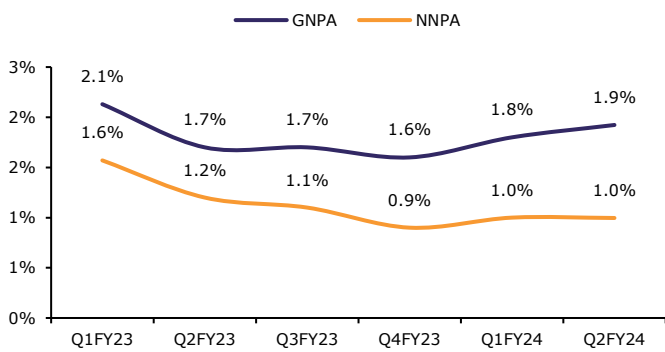
Source: Company, Emkay Research

Exhibit 13: Credit cost to sustain below 2%



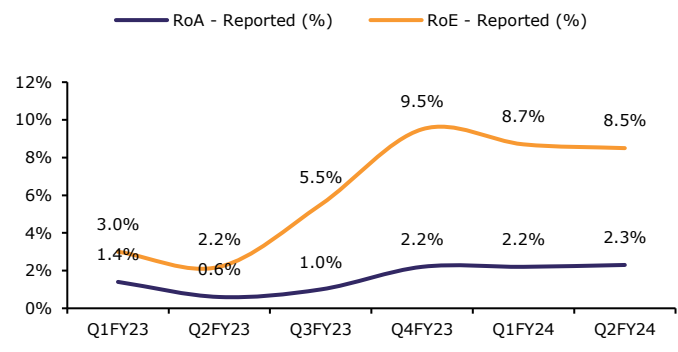
Source: Company, Emkay Research

Exhibit 14: Stable asset quality a result of prudent underwriting



Source: Company, Emkay Research

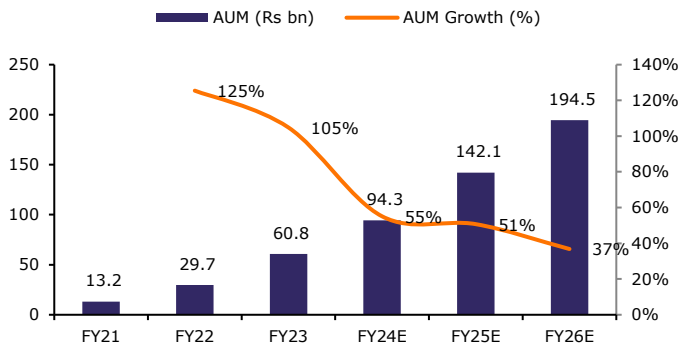
Exhibit 15: RoA to reach 3% levels by the end of Q4FY24E



Source: Company, Emkay Research

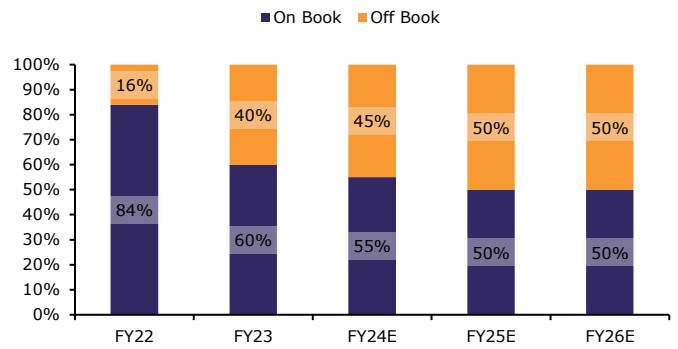
Story in Charts

Exhibit 16: We expect AUM to grow over 50% during FY24-25



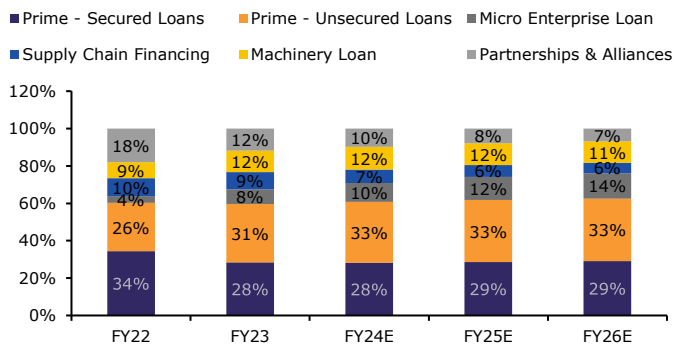
Source: Company, Emkay Research

Exhibit 17: On-book:Off-book AUM mix to reach 50:50 by FY25E



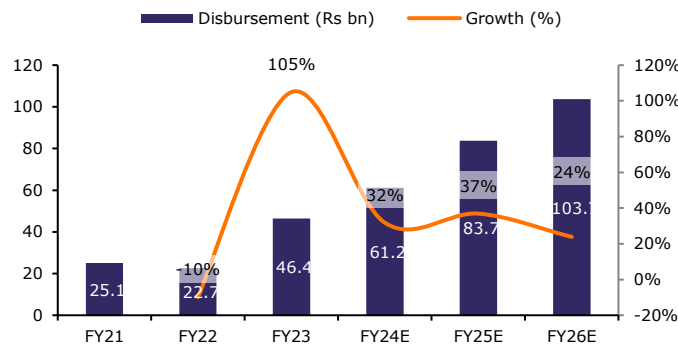
Source: Company, Emkay Research

Exhibit 18: Diverse product offering, with balance of secured and unsecured mix



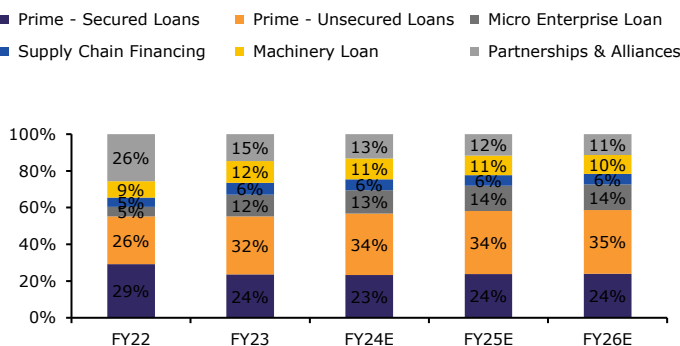
Source: Company, Emkay Research

Exhibit 19: Strong disbursement led by branch expansion and improved reach



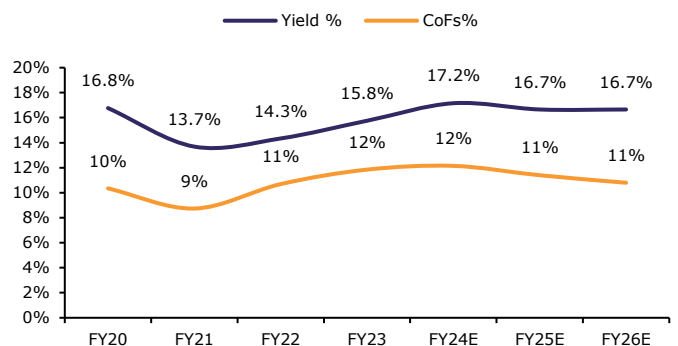
Source: Company, Emkay Research

Exhibit 20: Disbursement share of unsecured remains the highest



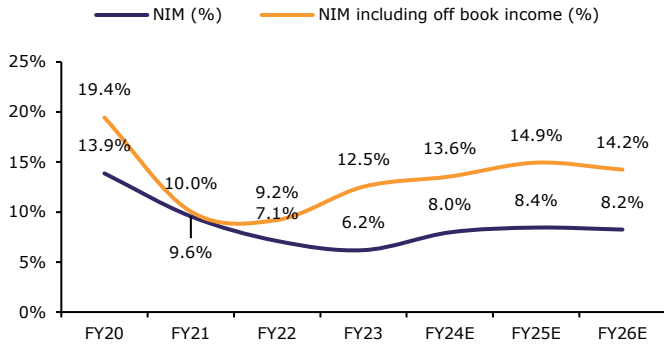
Source: Company, Emkay Research

Exhibit 21: CoFs to moderate over FY24-26 on account of increasing book size and improving asset quality



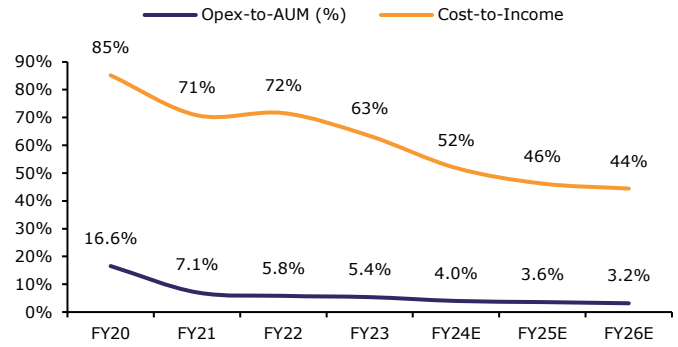
Source: Company, Emkay Research

Exhibit 22: Margin improvement led by increasing share of off-book lending as well as of high-yield products



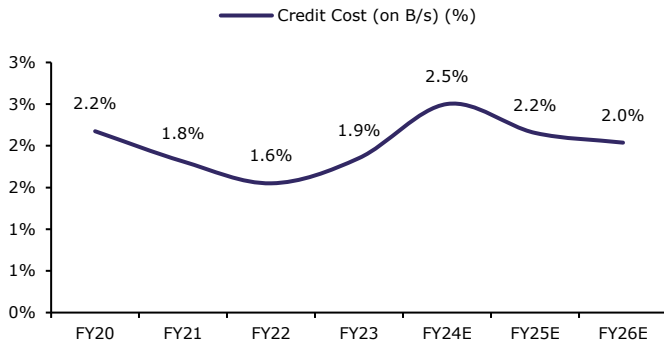
Source: Company, Emkay Research

Exhibit 23: Operating leverage to kick in, with growing book and improved efficiency



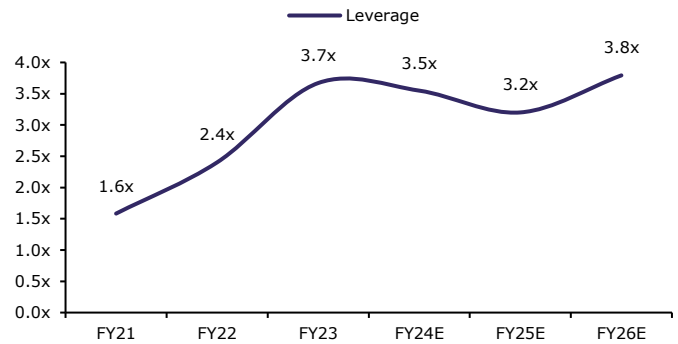
Source: Company, Emkay Research

Exhibit 24: We expect credit cost to remain at 2% levels



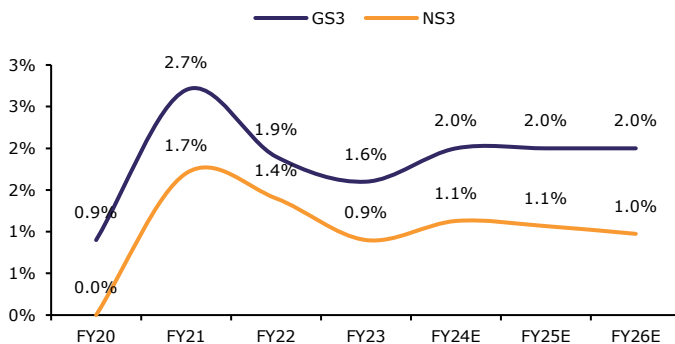
Source: Company, Emkay Research

Exhibit 25: Co-lending/Co-origination model leading to higher profitability with low leverage



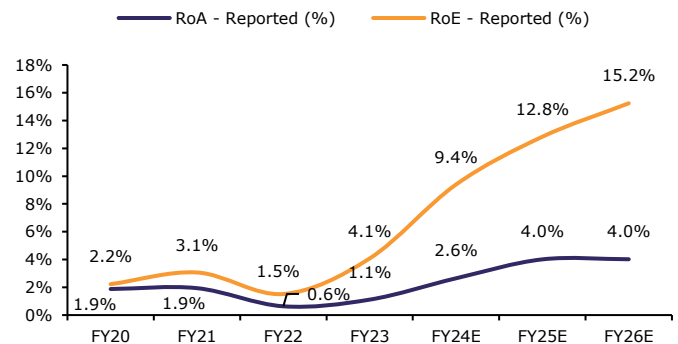
Source: Company, Emkay Research

Exhibit 26: Asset quality to remain stable



Source: Company, Emkay Research

Exhibit 27: RoA/RoE expansion over FY24-26 led by increasing share of off-book lending and improved product mix



Source: Company, Emkay Research

UGRO Capital : Standalone Financials and Valuations

Profit & Loss					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	2,721	4,829	7,571	10,239	14,016
Interest Expense	1,373	2,933	4,055	5,047	7,077
Net interest income	1,348	1,896	3,516	5,191	6,940
NII growth (%)	30.2	40.7	85.4	47.6	33.7
Non interest income	399	1,944	2,464	3,990	5,038
Total income	1,747	3,841	5,980	9,181	11,977
Operating expenses	1,251	2,435	3,101	4,245	5,322
PPOP	496	1,406	2,879	4,936	6,655
PPOP growth (%)	56.2	183.6	104.7	71.4	34.8
Provisions & contingencies	294	568	1,104	1,325	1,715
PBT	202	838	1,775	3,612	4,940
Extraordinary items	0	0	0	0	0
Tax expense	56	441	456	928	1,270
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	146	398	1,319	2,683	3,671
PAT growth (%)	(49.3)	173.4	231.6	103.5	36.8
Adjusted PAT	146	398	1,319	2,683	3,671
Diluted EPS (Rs)	2.1	5.7	14.4	24.9	34.0
Diluted EPS growth (%)	(49.4)	176.2	153.8	72.3	36.8
DPS (Rs)	0.0	0.0	0.0	0.0	0.0
Dividend payout (%)	0.0	0.0	0.0	0.0	0.0
Effective tax rate (%)	27.9	52.6	25.7	25.7	25.7
Net interest margins (%)	9.2	12.5	13.6	14.9	14.2
Cost-income ratio (%)	71.6	63.4	51.9	46.2	44.4
PAT/PPOP (%)	29.3	28.3	45.8	54.4	55.2
Shares outstanding (mn)	70.6	69.3	107.8	107.8	107.8

Source: Company, Emkay Research

Asset quality and other metrics					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Asset quality					
GNPL - Stage 3	564	957	1,401	1,990	2,820
NNPL - Stage 3	415	499	560	637	790
GNPL ratio - Stage 3 (%)	2.3	2.5	2.7	2.8	2.9
NNPL ratio - Stage 3 (%)	1.7	1.3	1.1	0.9	0.8
ECL coverage - Stage 3 (%)	27.0	49.0	60.0	68.0	72.0
ECL coverage - 1 & 2 (%)	0.0	0.0	0.0	0.0	0.0
Gross slippage - Stage 3	1	1	2	2	2
Gross slippage ratio (%)	0.0	0.0	0.0	0.0	0.0
Write-off ratio (%)	0.8	0.3	0.8	0.8	0.8
Total credit costs (%)	1.6	1.9	2.5	2.2	2.0
NNPA to networth (%)	4.3	5.1	2.9	2.9	3.0
Capital adequacy					
Total CAR (%)	34.5	20.2	34.8	30.3	26.0
Tier-1 (%)	33.6	19.6	34.3	29.9	25.7
Miscellaneous					
Total income growth (%)	60.6	119.9	55.7	53.5	30.5
Opex growth (%)	62.4	94.6	27.4	36.9	25.4
PPOP margin (%)	2.6	4.6	6.5	8.0	7.9
Credit costs-to-PPOP (%)	59.3	40.4	38.3	26.8	25.8
Loan-to-Assets (%)	85.9	88.4	88.2	88.7	88.8
Yield on loans (%)	14.3	15.8	17.2	16.7	16.7
Cost of funds (%)	10.7	11.8	12.1	11.4	10.8
Spread (%)	3.6	3.9	5.0	5.3	5.9

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	706	693	1,078	1,078	1,078
Reserves & surplus	8,960	9,147	18,486	21,169	24,840
Net worth	9,666	9,840	19,564	22,248	25,918
Borrowings	18,022	31,489	35,273	53,304	77,787
Other liabilities & prov.	861	1,726	1,725	1,725	1,725
Total liabilities & equity	28,549	43,056	56,563	77,277	1,05,430
Net loans	24,511	38,064	49,888	68,536	93,590
Investments	694	601	848	1,159	1,581
Cash, other balances	1,884	2,118	3,434	5,056	7,582
Interest earning assets	27,089	40,783	54,171	74,752	1,02,754
Fixed assets	43	38	38	38	38
Other assets	1,417	2,235	2,354	2,487	2,639
Total assets	28,549	43,056	56,563	77,277	1,05,430
BVPS (Rs)	137.0	142.0	181.4	206.3	240.3
Adj. BVPS (INR)	137.0	142.0	181.4	206.3	240.3
Gross loans	24,880	38,677	51,872	71,073	97,233
Total AUM	29,690	60,810	94,314	1,42,145	1,94,467
On balance sheet	24,910	36,390	51,872	71,073	97,233
Off balance sheet	4,780	24,420	42,441	71,073	97,233
Disbursements	22,650	46,410	61,174	83,739	1,03,736
Disbursements growth (%)	(9.9)	104.9	31.8	36.9	23.9
Loan growth (%)	91.1	55.3	31.1	37.4	36.6
AUM growth (%)	125.4	104.8	55.1	50.7	36.8
Borrowings growth (%)	135.4	74.7	12.0	51.1	45.9
Book value growth (%)	1.4	3.6	27.8	13.7	16.5

Source: Company, Emkay Research

Valuations and key Ratios					
Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	147.6	53.4	21.0	12.2	8.9
P/B (x)	2.2	2.1	1.7	1.5	1.3
P/ABV (x)	2.2	2.1	1.7	1.5	1.3
P/PPOP (x)	43.3	15.1	9.6	6.6	4.9
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Dupont-RoE split (%)					
NII/avg AUM	7.1	6.2	8.0	8.4	8.2
Other income	2.1	6.3	5.6	6.5	6.0
Securitization income	0.0	0.0	0.0	0.0	0.0
Opex	2.8	3.4	3.0	2.9	2.6
Employee expense	3.8	4.6	4.0	4.0	3.7
PPOP	2.6	4.6	6.5	8.0	7.9
Provisions	1.6	1.9	2.5	2.2	2.0
Tax expense	0.3	1.4	1.0	1.5	1.5
RoAUM (%)	0.8	1.3	3.0	4.4	4.4
Leverage ratio (x)	2.0	3.1	3.1	2.9	3.5
RoE (%)	1.5	4.1	9.4	12.8	15.2
Quarterly data					
Rs mn, Y/E Mar	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
NII	463	515	507	688	665
NIM(%)	10.8	12.5	13.6	12.9	13.9
PPOP	324	389	511	566	654
PAT	53	131	140	252	289
EPS (Rs)	0.75	1.89	2.03	3.06	3.50

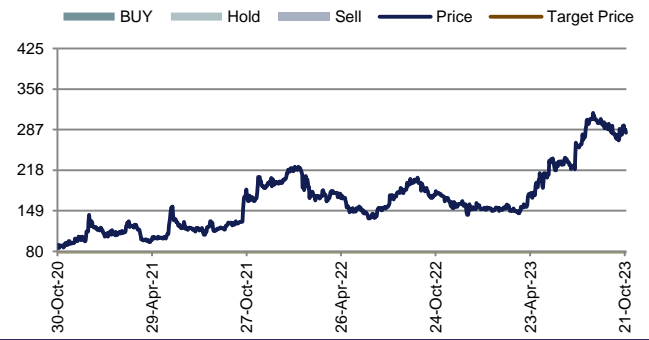
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	Closing Price (INR)	TP (INR)	Rating	Analyst
23-Oct-23	282	425	Buy	Avinash Singh

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Bloomberg, Company, Emkay Research

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