

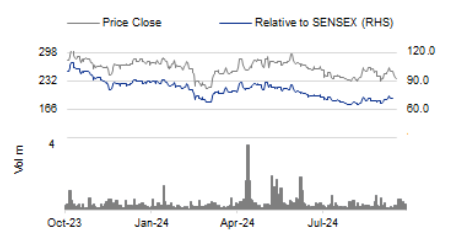
India

ADD (no change)

Consensus ratings*:	Buy 7 Hold 0 Sell 0
Current price:	Rs237
Target price:	Rs350
Previous target:	Rs350
Up/downside:	47.7%
InCred Research / Consensus:	-1.5%
Reuters:	UGRO BO
Bloomberg:	UGRO IN
Market cap:	US\$304m
	Rs22,059m
Average daily turnover:	US\$1.6m
	Rs119.4m
Current shares o/s:	69.2m
Free float:	97.8%
*Source: Bloomberg	

Key changes in this note

- Strong disbursement growth led to healthy AUM growth. Write-offs in the exiting SCF portfolio led to high provisioning, which weighed down PAT.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(10.2)	(8.3)	(15.7)
Relative (%)	(4.8)	(8.2)	(32.0)

Major shareholders	% held
DANISH SUS Fund	16.4
Clear Sky investments	16.3
New Quest Asia	16.3

Research Analyst(s)



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Ugro Capital

Moving towards better returns

- Missed 2Q PAT estimate at Rs355m (vs. InCred estimate of Rs429m) due to elevated credit costs, but a large part of the book clean-up is behind us.
- Strong disbursement growth (net SCF) at ~72% qoq and ~33% yoy led by robust offtake in micro enterprise loans and healthy growth in other segments.
- We believe the focus on micro branches, along with co-lending partnerships, should lead to better return ratios. Maintain ADD rating with a TP of Rs350.

Micro enterprise disbursements shoot up

UGRO Capital reported 2QFY25 PAT of Rs355m, missing estimate, due to higher than-expected provisioning on account of write-off of the supply chain financing (SCF) book. Disbursements (net SCF) grew strongly by ~33% yoy and sharply by ~72% qoq, led by a strong offtake of micro enterprise loans where disbursements increased by ~2.4x yoy and 2.2x qoq, and also broad-based growth of other segments barring SCF. The company has been incrementally investing in micro branches, with a renewed focus to increase productivity from these branches. The share of micro branches rose to 187 from 81 a year ago, with a faster breakeven at ~9-12 months from 14-18 months earlier. We believe the company's focus is on increasing the share of micro enterprise loans from ~11% to ~35% in the medium term, which will be a key driver of profitable AUM growth.

Co-lending book strengthens further

Co-lending assets under management or AUM increased rapidly by ~21% qoq and ~91% yoy to Rs22bn led by garnering the highest-ever co-lending volume at Rs6.15bn. We believe that co-lending will be another key parameter to augur return ratios on the back of high returns. Operating leverage is gradually seen improving, with the cost-to-income ratio improving by ~120bp qoq led by strong co-lending income.

Major asset quality pain behind, ageing-related pressure rises

Gross stage-3 assets inched up by ~10bp qoq to 2.1% of AUM, largely on the back of higher slippage from the existing SCF book. Credit costs were elevated at ~2.9%, up by ~60bp qoq, due to higher provisioning (~1.2% annualized) related to write-offs in the SCF book. Although management indicated no further stress in the SCF book, we believe that credit costs will remain high in 2HFY25F due to ageing of the book.

Outlook and valuation

UGRO Capital is well-positioned to enter the next phase of its growth, with a rising market share in the growing landscape of MSME lending. We expect strong AUM growth (+34.2% CAGR over FY24-27F) led by both on-and off-balance sheet growth resulting in improving operating leverage, which will shore up return ratios to ~4% RoA and ~14% RoE (adjusting for equity infusion of Rs12.7bn) by FY27F. We maintain our ADD rating, valuing the stock at ~1.5x FY26F P/BV with a stable target price of Rs350. Slower growth and weak asset quality are key downside risks to our investment thesis.

Financial Summary

	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Net Interest Income (Rsm)	1,896	2,636	4,037	5,757	7,882
Total Non-Interest Income (Rsm)	2,008	3,752	4,923	6,881	9,168
Operating Revenue (Rsm)	3,905	6,388	8,960	12,638	17,050
Total Provision Charges (Rsm)	(568)	(1,163)	(1,819)	(2,580)	(3,820)
Net Profit (Rsm)	398	1,193	1,992	3,381	4,872
Core EPS (Rs)	5.75	13.03	21.74	23.97	34.54
Core EPS Growth	260%	127%	67%	10%	44%
FD Core P/E (x)	41.26	18.21	10.91	9.90	6.87
DPS (Rs)	0.00	0.00	0.00	0.00	0.00
Dividend Yield	0.00%	0.00%	0.00%	0.00%	0.00%
BVPS (Rs)	142.2	157.1	178.8	229.7	264.3
P/BV (x)	1.67	1.51	1.33	1.03	0.90
ROE	4.1%	9.9%	13.0%	13.9%	14.0%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 1: Quarterly results summary

Rs m	2QFY24	3QFY24	4QFY24	1QFY25	2QFY25	% yoy	% qoq
Interest Income	1,719	1,828	1,903	2,320	2,080	21.0	-10.3
Interest Expenses	1,054	1,167	1,281	1,361	1,431	35.8	5.1
Net Operating Income	665	661	622	958	649	-2.4	-32.3
Other Income	818	965	1,401	696	1,349	64.9	93.7
Total Income	1,482	1,626	2,022	1,654	1,998	34.8%	20.8
Operating Expenses	829	865	1,052	894	1,053	27.1	17.8
Operating Profit	654	761	970	760	945	44.5	24.3
Provisions	246	297	411	332	443	80.5	33.7
PBT	408	464	559	428	501	22.9	17.0
Tax	119	138	233	125	146	22.6	17.0
<i>Tax rate (%)</i>	<i>29.2</i>	<i>29.9</i>	<i>41.6</i>	<i>29.1</i>	<i>29.1</i>	<i>-0.2</i>	<i>0.0</i>
Reported PAT	289	325	327	304	355	23.0	17.0
AUM	75,920	83,640	90,470	92,180	1,01,570	33.8	10.2
Disbursements (net SCF)	14,770	15,520	15,540	11,450	19,710	33.4	72.1

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Our revised earnings estimates

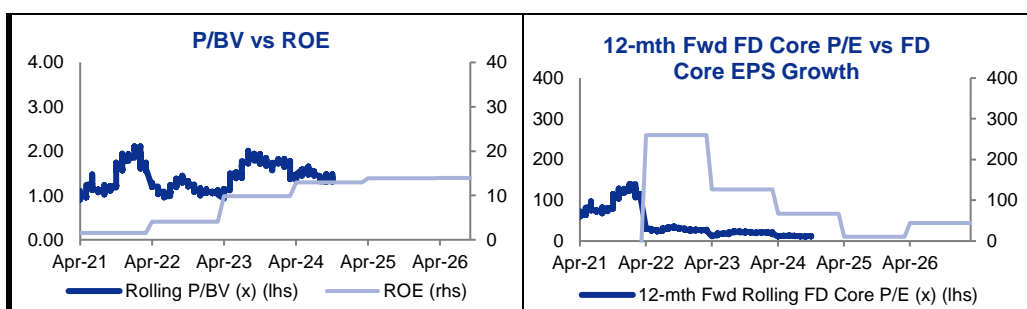
Y/E Mar (Rs m)	FY25F			FY26F			FY27F		
	Earlier	Revised	% change	Earlier	Revised	% change	Earlier	Revised	% change
Net interest income	4,037	4,037	0.0	5,757	5,757	0.0	7,882	7,882	0.0
PPOP	4,665	4,665	0.0	7,410	7,410	0.0	10,780	10,780	0.0
PAT	1,992	1,992	0.0	3,381	3,381	0.0	4,872	4,872	0.0
EPS (Rs)	21.7	21.7	0.0	24.0	24.0	0.0	34.5	34.5	0.0
AUM (Rs)	1,23,567	1,23,567	0.0	1,63,153	1,63,153	0.0	2,18,861	2,18,861	0.0

SOURCE: INCRED RESEARCH, COMPANY REPORTS

2QFY25 earnings-call highlights ►

- Management reiterated 4% RoA target by FY26F led by higher operating leverage and lower credit costs.
- Credit costs are guided to be elevated in 2HFY25F but drop to 2% or below by FY26F.
- Steady gross NPAs in the micro enterprise book are indicated to be at 3-3.5% as compared to 3.6% in 2QFY25 and credit costs at ~1%.
- The company will continue to invest in micro branch addition and has indicated an increase in the branch count to 250 by FY25F and to 400 by FY26F.
- Total branches stood at 210 at the end of Sep 2024, with an addition of 46 branches qoq.
- Geographically, the company has expanded its micro loan business to newer locations of Uttar Pradesh, Madhya Pradesh, Andhra Pradesh and Maharashtra.
- Cost of funds is indicated to rise by ~5bp in 2HFY25F before cooling down in 1QFY26F.
- Total collections remained stable qoq at ~96%.
- Management is comfortable in increasing the leverage to 4.5-5x from ~2x currently.

BY THE NUMBERS



Profit & Loss					
(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Net Interest Income	1,896	2,636	4,037	5,757	7,882
Total Non-Interest Income	2,008	3,752	4,923	6,881	9,168
Operating Revenue	3,905	6,388	8,960	12,638	17,050
Total Non-Interest Expenses	(2,499)	(3,437)	(4,296)	(5,228)	(6,270)
Pre-provision Operating Profit	1,406	2,950	4,665	7,410	10,780
Total Provision Charges	(568)	(1,163)	(1,819)	(2,580)	(3,820)
Operating Profit After Provisions	838	1,788	2,845	4,830	6,960
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	838	1,788	2,845	4,830	6,960
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	838	1,788	2,845	4,830	6,960
Exceptional Items					
Pre-tax Profit	838	1,788	2,845	4,830	6,960
Taxation	(441)	(594)	(854)	(1,449)	(2,088)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	398	1,193	1,992	3,381	4,872
Minority Interests					
Pref. & Special Div					
FX And Other Adj.					
Net Profit	398	1,193	1,992	3,381	4,872
Recurring Net Profit					

Balance Sheet Employment					
(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Gross Loans/Cust Deposits					
Avg Loans/Avg Deposits					
Avg Liquid Assets/Avg Assets					
Avg Liquid Assets/Avg IEAs	106.4%	107.2%	104.1%	107.7%	109.8%
Net Cust Loans/Assets					
Net Cust Loans/Broad Deposits					
Equity & Provns/Gross Cust Loans					
Asset Risk Weighting					
Provision Charge/Avg Cust Loans					
Provision Charge/Avg Assets					
Total Write Offs/Average Assets					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Total Gross Loans	38,064	54,322	71,996	92,182	120,374
Liquid Assets & Invst. (Current)					
Other Int. Earning Assets					
Total Gross Int. Earning Assets	38,064	54,322	71,996	92,182	120,374
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets	38,064	54,322	71,996	92,182	120,374
Intangible Assets					
Other Non-Interest Earning Assets	1,644	2,785	3,481	4,177	5,013
Total Non-Interest Earning Assets	2,018	3,307	4,108	4,898	5,806
Cash And Marketable Securities	2,118	4,549	661	12,062	8,788
Long-term Investments					
Total Assets					
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others	31,489	46,532	58,361	74,059	94,318
Total Interest-Bearing Liabilities	31,489	46,532	58,361	74,059	94,318
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	1,726	1,884	2,626	3,281	3,981
Total Liabilities	33,215	48,416	60,987	77,339	98,299
Shareholders Equity	9,840	14,384	16,375	32,406	37,278
Minority Interests					
Total Equity					

Key Ratios					
	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Total Income Growth	38.6%	39.0%	53.2%	42.6%	36.9%
Operating Profit Growth	183.2%	109.8%	58.1%	58.9%	45.5%
Pretax Profit Growth	315%	113%	59%	70%	44%
Net Interest To Total Income	48.6%	41.3%	45.1%	45.6%	46.2%
Cost Of Funds	11.85%	11.35%	11.00%	10.70%	10.40%
Return On Interest Earning Assets	15.4%	15.3%	15.5%	15.6%	15.7%
Net Interest Spread	3.59%	3.94%	4.53%	4.94%	5.25%
Net Interest Margin (Avg Deposits)					
Net Interest Margin (Avg RWA)					
Provisions to Pre Prov. Operating Profit	40%	39%	39%	35%	35%
Interest Return On Average Assets					
Effective Tax Rate	52.5%	33.2%	30.0%	30.0%	30.0%
Net Dividend Payout Ratio					
Return On Average Assets					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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- Add** The stock's total return is expected to exceed 10% over the next 12 months.
- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
- Reduce** The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

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Definition:

- Overweight** An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

- Overweight** An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral** A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight** An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.