

Utkarsh Small Finance Bank Ltd — Aug 2024 Quarterly Analysis

1. VERDICT & BUSINESS QUALITY SNAPSHOT

Result: Inline **One-line:** Strong core operating profitability (highest-ever PPOP) and robust loan growth (31% YoY) were balanced by seasonal asset quality stress in the micro-banking portfolio and a slight NIM compression due to excess liquidity.

Dimension	This Quarter	Signal / Evidence	Sentiment
Beat/Miss vs Guidance	Inline	Loan growth at 31% (target 30%); ROA 2.3% (target >2.0%).	□
Earnings Quality	High	Growth driven by core NII (+36% YoY) and lower Cost-to-Income (54% vs 57% YoY).	□
Guidance Confidence	Neutral	Management maintained all FY25 targets despite Q1 credit costs (2.7%) exceeding the 2% annual guide.	□
Management Credibility	Strong	Proactive creation of floating provisions (₹20 Cr) and early implementation of MFIN responsible lending norms.	□
Business Quality Signal	Stable	Diversification into secured loans (35% of book) is progressing, reducing over-reliance on JLG.	□
Key Q&A Exchange	Q1 + Asset Quality	Analysts pushed on the spike in SMA 1 & 2; Mgmt blamed heatwaves/elections, not borrower insolvency.	□
The Street's Primary Anxiety	Micro-banking Stress	Fear of systemic over-indebtedness in North India (UP/Bihar/Jharkhand). Mgmt response: Low average ticket size (₹35k) protects them.	□
Capital Cycle Stage	Harvesting	Utilizing capital from the IPO to grow the book; focus on sweating existing branch vintage (50% < 3 years).	□
Margin Trajectory	Deteriorating	NIM fell to 9.4% (vs 9.9% QoQ) due to ₹3,000 Cr+ surplus liquidity and NPA interest reversal.	□
Pricing Power	Expanding	Disbursement yields in MSME rose by 70 bps; Housing and CE/CV yields rose 20-30 bps.	□
FCF Conversion	N/A	Sector-specific (Banking); however, Capital Adequacy remains strong at 23.18%.	□
Competitive Moat	Stable	Strong rural/semi-urban presence (86% of MB outlets) provides a granular, high-yield liability base.	□
Balance Sheet Strength	Strong	Surplus liquidity of ₹3,000 Cr+; CD ratio improved to 92.7%; no short-term borrowings.	□
Working Capital Efficiency	N/A	Sector-specific; RTD growth (48% YoY) is significantly outpacing bulk deposits.	□
Mgmt Guidance Track Record	Reliable	Consistent delivery on growth and return ratios over the last 8 quarters.	□
Key Vulnerability	Regional Stress	High geographical concentration in Bihar (42%) and UP (27%) for JLG remains the primary risk.	□
Management Tone	Cautiously Optimistic	Admitted operational "hiccups" in Q1 but remained firm on full-year targets.	□

Key Takeaways: * **Positives:** Loan growth remains robust at 31% YoY; the bank achieved its highest-ever quarterly operating profit (₹11 Cr); secured loan mix increased to 35% as part of the strategic shift away from pure microfinance. * **Negatives:** Asset quality showed seasonal/operational deterioration with SMA 1 & 2 reaching 2.6% (vs 1.9% QoQ); NIM compressed by 50 bps QoQ to 9.4% due to a massive liquidity buffer that acted as a drag. * **Street's Main Concern:** Analysts are skeptical that credit costs will return to the 2% guided range given the lack of immediate reversal in July. Management maintains that this was a connectivity issue (heatwave/elections) rather than a financial stress issue. * **Forward Watchpoint:** Monitor the "reversal of trend" in SMA buckets in Q2; if slippages do not cool off, the 2% credit cost guidance for FY25 will become mathematically improbable.

2. BUSINESS PERFORMANCE

2A. KEY METRICS

PPT not available — numbers from concall for specific slippage figures; PPT used for all other primary metrics.

Metric	Current Qtr	YoY Change	QoQ Change	Trend	Mgmt Commentary
NII Growth (%)	36.3%	↑	↑	↑	Driven by 31% loan growth and stable Cost of Funds.
NIM (AUM basis %)	9.4%	↓ (9.7% PY)	↓ (9.9% PQ)	↓	Impacted by ₹3,000 Cr+ surplus liquidity and interest reversals on NPAs.
Cost of Funds %	8.0%	↑ (7.6% PY)	→ (8.0% PQ)	→	Stable despite elevated interest rate environment; IBPC route helps keep it at 7.9%.
Cost of Deposits %	8.6% (TD)	↑	↑	↓	Focus on Retail Term Deposits (RTD) which are pricier but more stable.
CASA Ratio (period end %)	18.0%	↓ (21.0% PY)	↓ (20.0% PQ)	↓	Depositor preference shifting to Term Deposits due to high rates.
Credit-Deposit Ratio %	92.7%	↓ (93.9% PY)	↓ (93.7% PQ)	↑	Strategic reduction as deposit growth (30% YoY) meets loan growth.
Loans Growth (% YoY)	30.6%	↑	→	→	Gross Loan Portfolio reached ₹18,798 Cr.
Deposits Growth (% YoY)	30.0%	↑	→	→	Total Deposits reached ₹18,163 Cr; RTD grew 48% YoY.
GNPA %	2.8%	↑ (3.13% PY)	↓ (2.5% PQ)	↓	QoQ increase (2.5% to 2.8%) due to micro-banking slippages.
NNPA %	0.3%	→ (0.33% PY)	↓ (0.0% PQ)	↓	Increase from nil in March due to seasonal stress.
Slippage Ratio %	3.8% (annualized)	N/A	↑	↓	Total slippages of ₹180 Cr (₹125 Cr from JLG).
Credit Cost (% funded assets)	2.7%	↑ (2.1% PY)	↑ (1.7% PQ)	↓	Includes ₹20 Cr floating provision; core credit cost at 2.2%.
Collection Efficiency %	96.0%	↓ (97.0% PY)	↓ (98.0% PQ)	↓	Impacted by heatwave and elections in core geographies.
Capital Adequacy %	23.18%	↑ (19.8% PY)	↑ (22.6% PQ)	↑	Strong buffer; Tier 1 at 20.39%.
PAT (₹Cr)	137	↑ 28%	↓ 14%	□	Seasonal Q1 weakness in other income and higher provisions.
Fee Income Growth %	14.1%	↑	↓	□	Processing fees lower QoQ due to seasonal disbursement trends.

2B. SEGMENT BREAKDOWN

Segment	Portfolio (₹ Cr)	Share (%)	Yield	Trend	vs Company Avg	Key Development
JLG (Micro-banking)	10,672	57%	~25-26%	↓	High Yield	Implementating MFIN norms; stress in Bihar/UP pockets.
MBBL (Micro-biz)	706	4%	~26%	↑	High Yield	Scaling fast (+83% YoY); healthy asset quality (1% NPA).
MSME (Retail)	2,745	15%	12.1%	↑	Low Yield	Disbursement yields up 70 bps; 95% secured.
Housing Loans	1,010	5%	10.7%	↑	Low Yield	Growing 38% YoY; average ticket size ₹20-25 Lakh.
CE & CV	759	4%	12.3%	↑	Low Yield	Focused on small fleet operators; yields up 30 bps.
Wholesale Lending	1,872	10%	10.8%	→	Low Yield	70% of FI book is A-rated or higher.

3. MANAGEMENT OUTLOOK & EXECUTION TRACKER

Dimension	Category	Management Target / Claim	Required Run-Rate / Mathematical Feasibility	Historical Delivery	Risk Flag
Guidance	Loan Growth	~30% for FY25	Needs ₹4,400 Cr net addition over Q2-Q4 (Q1 addition was ₹500 Cr).	Met (31% YoY)	Low
Guidance	Credit Cost	~2.0% for FY25	Needs ~1.7-1.8% over Q2-Q4 to offset Q1's 2.7%.	Missed in Q1	High
Guidance	ROA / ROE	>2% ROA / ~18% ROE	Currently at 2.3% and 18.1%; needs to maintain current trajectory.	Met	Low
Guidance	Cost-Income	54% - 57%	Currently at 54.1%; well within range despite salary hikes.	Met	Low
Strategy	Mix Shift	Decrease MB share by 3-4%	MB share was 62% in Mar-24; currently at 61%. On track.	On track	Low
Strategy	Reverse Merger	Complete in FY25	Swap ratio to be based on June-24 results; filing in Q2.	Ongoing	Medium

4. ANALYST Q&A

Q#	Relevance	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded	Credibility	Verdict
1	5.0	Rajiv Mehta / YES Sec	Asset Quality	Financials	"How is micro-banking collection efficiency in July, and will slippages be higher in Q2?"	Management admitted July hasn't seen a full reversal but claimed the stress is operational (heat/ elections) rather than financial stress on the customer. Investment Implication: Credit costs are likely to remain elevated in Q2, making the 2% year-end target highly dependent on a massive Q3/ Q4 recovery.	None	3.5	Directional but cautious
2	4.5	Rajiv Mehta / YES Sec	Growth Guardrails	Mgmt Outlook	"How will MFIN indebtedness limits impact growth in competitive markets like UP/Bihar?"	Management expects a "single-digit" percentage impact on disbursements but plans to offset this by acquiring new customers and leveraging their low ticket size (₹35k). Investment Implication: Volume growth may slow temporarily as the bank cleans the pipeline, but risk-adjusted returns should improve.	None	4.0	Specific & quantified

Q#	Relevance	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded	Credibility	Verdict
3	4.5	Rahil Shah / Crown Cap	Geography Stress	Financials	"What exactly is causing stress in pockets like Jharkhand, Odisha, and UP?"	Management cited heatwaves, elections, and temporary migration for cultivation/ monsoon as the primary drivers of the SMA spike. Investment Implication: This confirms the "seasonal" thesis; if these borrowers don't return to pay in Q2/Q3, it suggests structural over-leverage.	None	3.0	Qualitative
4	4.0	Rahil Shah / Crown Cap	Margins	Financials	"How will NIMs shape up for the rest of the year?"	Management expects NIMs to stay around 9.4%, supported by the deployment of ₹3,000 Cr surplus liquidity into higher-yielding assets. Investment Implication: NIM compression has likely bottomed out, but the shift to secured loans will prevent significant expansion.	None	4.0	Directional with data
5	4.0	Shailesh Kanani / Centrum	Opex Efficiency	Financials	"Why did opex not spike despite employee additions and	Management attributed it to lower performance bonus provisions in	None	4.5	Clear explanation

Q#	Relevance	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded	Credibility	Verdict
					salary increments?"	Q1 (which are higher in Q4) and natural efficiency gains. Investment Implication: Positive operating leverage is playing out, allowing the bank to invest in branches without hurting the bottom line.			
6	4.0	Shailesh Kanani / Centrum	Governance	Governance	"What is the update on the reverse merger with the promoter entity?"	Management confirmed that the swap ratio will be based on Q1 FY25 results and they expect to file applications this quarter. Investment Implication: The merger timeline is firm, which will simplify the holding structure and potentially unlock value.	None	5.0	Specific timeline
7	4.0	Gaurav Kochar / Mirae	Yields	Financials	"How big is the gap between disbursement yield and portfolio yield?"	Management noted that disbursement yields in non-microfinance segments are rising (MSME +70bps), which will catch up to the portfolio over 3-4 quarters. Investment Implication:	None	4.5	Quantified

Q#	Relevance	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded	Credibility	Verdict
						Future interest income growth will be realization-driven as the bank re-prices its retail book.			
8	4.5	Ashlesh Sonje / Kotak	Industry Norms	Mgmt Outlook	"Are other lenders following the MFIN guardrails, and how do you handle ineligible repeat borrowers?"	Management believes major SFBs are implementing the norms and that ineligible borrowers will naturally "regularize" their debt over 6-9 months by not getting new loans. Investment Implication: Industry-wide discipline is critical; Utkarsh's early adoption may hurt short-term growth but protects the long-term book.	None	3.5	Directional
9	3.5	Anirudh Gangahar	Net NPA	Financials	"Is the guidance of zero/nil Net NPA still intact?"	Management confirmed they are still aiming for "closer to zero" NNPA by year-end despite the Q1 spike. Investment Implication: This implies aggressive provisioning or write-offs in the back half of the year to clean the	None	3.0	Vague / Aspirational

Q#	Relevance	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded	Credibility	Verdict
						balance sheet.			

PATTERN FLAGS & SENTIMENT * **The "Heatwave/Election" Defense:** Management repeatedly attributed the asset quality dip to physical inability to connect with borrowers due to extreme weather and election duties. While plausible for a high-touch MFI model, analysts remain skeptical because July hasn't shown a sharp recovery. This remains a "live" concern for Q2. * **Yield Optimization:** There is a clear pattern of management pushing yields higher in secured segments (MSME, Housing) to offset the cost of funds. This indicates pricing power in their core geographies. * **Analyst Sentiment Verdict:** Analysts were generally satisfied with the growth and operating profit numbers but remained "on edge" regarding the credit cost guidance. The tone was professional but inquisitive, focusing heavily on the math of the 2% credit cost target. Management's credibility remains intact due to their transparency on floating provisions and surplus liquidity.

5. WHAT CHANGED vs PRIOR QUARTER

First entry — no prior quarter to compare.
STOP HERE.