ICRA Credit Perspective

UTKARSH MICRO FINANCE PRIVATE LIMITED

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GRADING

ICRA has reaffirmed the MFI grading of Utkarsh Microfinance Private Limited at M2+ (pronounced M 2 plus). The grading indicates that in ICRA's current opinion, the Graded MFI's ability to manage its microfinance activities in a sustainable manner is high

Website:
www.icra.in

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Grading Rationale

The grading factors in Utkarsh's ability to scale up operations (Portfolio of Rs 420 crore as on June 30, 2014 with 100% growth in 2013-14) while maintaining good asset quality indicators (Collection Efficiency of 99.9% as on June 30, 2014). The grading also factors in Utkarsh's ability to improve its profitability indicators supported by reduction in operating expenses and its improved financial flexibility as reflected by the fact that the company was able to raise around Rs 481 crore of funds in 2013-14 from 32 lenders including Rs 76 crore raised in the form of Non Convertible Debentures. The grading continues to factor in Utkarsh's experienced management team, strong investor profile, good loan monitoring and collection mechanisms supported by strong Management Information Systems (MIS) and risk management function. As for the company's business plan, the company intends to grow at a CAGR of over 64% over the next three years and in ICRA's view, ability of the company to manage growth, recruit and train personnel in line with the planned branch expansion and replacing existing employees especially at field level for the existing attrition rates of 24-25%. As for capital requirement, In ICRAs estimates, the company would require Rs 100-Rs 150 crore capital over the next two years to meet its growth plans and based on the track record of equity raising in the past, ICRA expects the company to be able to raise equity in a timely manner. It would also be important for the company to diversify its portfolio geographically further and maintain its asset quality indicators in the newer microenterprise loan product.

Company Background

Utkarsh Micro Finance Pvt. Ltd is registered with the Reserve Bank of India as an NBFC as Non Banking Finance Company (NBFC-MFI) with its registered and Corporate office in Varanasi (Uttar Pradesh). The Company is promoted by Mr. Govind Singh, the former Business Head for Microbanking at ICICI Bank. Besides the promoter and other individual shareholders (promoter's friends and associates), Aavishkaar Goodwell (AG) , International Finance Corporation (IFC) and Norwegian Microfinance Initiatives (NMI) have made equity investment in the company. The company is presently operating in 8 states, namely UP (constituting 58% of portfolio as on March 31, 2014), Bihar (28%), Uttarakhand(6%), Madhya Pradesh 4%, Delhi 3% , Himachal , Haryana and Maharashtra. Utkarsh reported a Profit After Tax of Rs 8.22 crore in 2013-14 on a managed asset base of Rs 531 crore vis-à-vis PAT of Rs 3.89 crore on a managed asset base of Rs 298 crore in 2012-13 . For the first quarter ended June 30, 2014, Utkarsh reported PAT of Rs. 2.26 crore on a managed asset base of Rs 526.70 crore.

Table 1: Highlights of Operations

	Mar-10	Mar-11	Mar-12	Mar-13	Mar-14	Jun-14
No of states	1	2	2	5	8	8
Total branches*	13	52	75	102	142	166
Total centers*	499	3,902	7,826	14,369	20,476	23,134
Total members*	8,719	58,623	110,886	200,066	337,543	381,096
Total active borrowers *	8,208	55,506	106,369	197,874	317,900	358,437
Total groups*	1753	12,456	25,816	49,087	80,181	85,844
Credit portfolio (Rs. Crore)	6	32	75	178	356	420
Growth (annualised %)	5106%	433%	134%	137%	100%	72%
No. of employees	114	325	408	623	1032	1,252
Growth in employee base		185%	26%	53%	66%	21%
Credit officers	73	195	216	341	575	705
Growth in credit officers		167%	11%	58%	69%	23%
Active borrowers per branch	631	1,067	1,418	1,940	2,239	2159
Active borrowers per credit officer	112	285	492	580	553	508
Portfolio per branch (Rs. Crore)	0.46	0.62	1	1.75	2.5	2.44
Growth		33%	63%	75%	44%	-2%
Loan outstanding per borrower(Rs.)	7310	5765	7051	8996	11187	11314
Growth		-21%	22%	28%	24%	1.13%

*For JLG Loans
Source: Company, ICRA analysis

Utkarsh utilizes a five-member group lending methodology under Joint Liability Group model, wherein the group members undertake the responsibility of forming the group, joint liability, and repayments. The borrowers are women from rural and semi-urban regions, with weak income backgrounds, and no access to organised credit. 2 to 6 groups form a centre. While this makes the lending risky (the loans being unsecured), the group dynamics, which has been historically tested and in varied markets, should be effective in curtailing shortfall in collections from any borrower. The borrowers typically are involved in animal husbandry projects, small trade, cottage industries, agricultural based projects and other textile related projects. For lending in these segments Utkarsh earns yields in the range of 25% apart from processing fees of 1%.

The company has also ventured into the Microenterprise loans (higher ticket size individual loans from Rs 30,000 onwards). The share of this portfolio would remain less than 10% of the total portfolio of Utkarsh in the medium term. The company contributes 2% of its PBT to Samutkarsh Welfare Services for credit plus activities.

Around 96.6% of the portfolio as on March 31, 2014 was towards Joint liability group loans and the balance being microenterprise loans. As for geographical spread, the company expanded its presence from 24 districts as on March 31, 2013 to 40 districts as on March 31, 2014 districts across 8 states(UP, Bihar, Uttarakhand, MP, Delhi, Maharashtra, Haryana and Himachal Pradesh) which has resulted in reduction in geographical concentration of its portfolio in UP from 69% as on Mar-13 to 58% as on Mar-14 and is expected to decline further going forward. Nevertheless, Utkarsh's portfolio would continue to remain concentrated in UP and Bihar in the medium term. As for borrower vintage, owing to the high growth of Utkarsh around 50% of the portfolio as on March 31, 2014 was against first cycle loans though reduced from 54% as on March 31, 2013.This ratio is expected to remain high in the medium term, owing to the high growth plans of the company. Utkarsh's credit policies are relatively conservative; all incremental sanctions are processed post checking with Credit Bureau. The company does not offer Mid

Term Loans. As for the company's business plan, the company intends to grow at a CAGR of over 64% over the next three years and scale up the Micro-enterprise loan portfolio to around 5-7% of portfolio by Mar-15. In ICRA's view, ability of the company to manage growth while expanding into newer states as well as establish a track record of sustainable operations in the newer micro-enterprise loan product would be critical from a grading perspective

Chart 1: Monthly Disbursement Trends

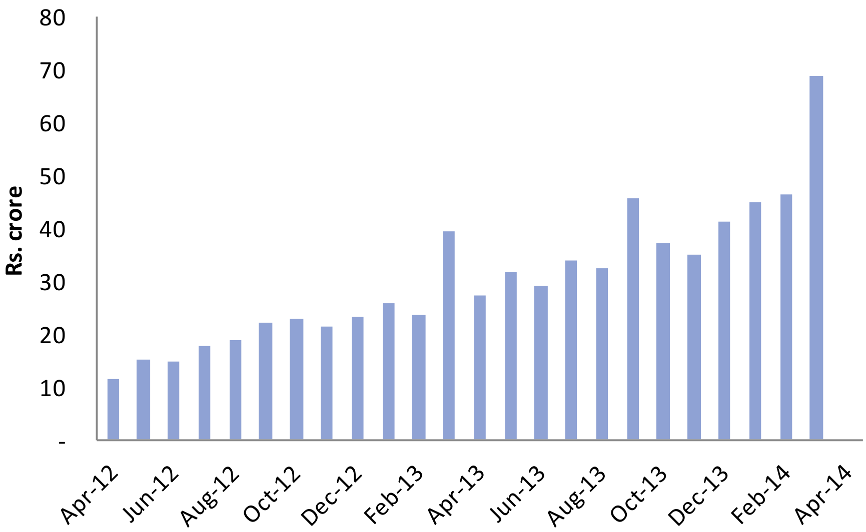


Table 2: Key Financials

	Mar-12	Mar-13	Mar-14
Equity Capital	10	24	26
Net Worth	33	64	74
Net Hire Purchase/ Loan/ Lease Assets	40	139	292
Total Assets	94	257	466
Managed Assets (incl. off balance sheet receivables)	131	298	537
Total Income	13	31	70
Net Interest Income (Net of BO Costs & Profits from Securitization)	6	15	29
Profit Before Tax (PBT)	2	6	14
Profit After Tax (PAT)	1	4	8
Yield on Average Earning Assets (%)	16.6%	16.7%	18.5%
Yield on Advances (%)	27.90%	26.42%	26.28%
Cost of average interest bearing funds (%)	9.4%	10.9%	12.6%
Gross Interest Spread (%)	7.2%	5.8%	5.9%
Net Interest Margin (%)	9.5%	7.8%	7.0%
Operating Expenses /Average Managed Assets	8.1%	5.5%	4.7%
Operating Expenses /Average Managed Portfolio	13.05%	9.38%	7.32%
Provisions & Write offs / Average Managed Assets (%)	0.3%	0.3%	0.5%
Cost to Income Ratio (%)	74.7%	64.5%	55.4%
PBT (excluding extraordinary items) / Average Managed (%)	2.5%	2.8%	2.7%
PAT / Average Managed Assets	1.6%	1.8%	1.9%
Return on Average Networth(%)	6.3%	8.0%	11.7%
Equity Dividend / Profit After Tax	0.0%	0.0%	0.0%
Equity Dividend rate(%)	0.0%	0.0%	0.0%
Total Debt / Net worth	1.72	2.81	5.04
Net Worth/Managed Advances	42.77%	35.69%	20.47%

Note: Amounts in Rs. Crore, AMA- Average Managed Assets

Managed Assets- Total Assets + Off Balance Sheet book
Managed Advances- Total Portfolio + off Balance Sheet Portfolio
Earning Assets Loan Portfolio + Cash and Bank Balances

Summary Grading Rationale

	Parameters	Overall Comments
A	**Business Risk**	
1	Operating Environment	MFIs reported over 40% annualized growth during the two years ended March 2014 after the period of stress post-AP crisis when funding sources had dried up. The growth was supported by better availability of funds, strong branch expansion, and increase in ticket size. Significantly, even after the impressive growth during the last two years, the untapped potential remains large. This, along with the expansion plans of MFIs and the expected fund availability, is likely to enable a 30-35% annualized rate of growth over the next three years. Further, the RBI, in June 2014, has allowed non deposit accepting NBFC-ND to be business correspondents (BC), which is likely to provide a fillip to financial inclusion and to the business prospects of MFIs. However, while the growth prospects for MFIs are favourable, recruitment, employee-training and employee-retention are likely to remain critical performance-determining factors, given that the employee attrition rate in the industry remains high at an annual 30-40% even as most MFIs are into a significant expansion drive. As for the regulatory environment, RBI has put in margin caps in place, which have forced MFIs to take several initiatives to cut operating costs including optimization of branch costs and manpower, increase in loan sizes and automation of processes, among others. Managing costs has become even more important as the net interest margins for MFIs has been capped from April 2014 at 10% for MFIs with a loan portfolio of more than Rs. 100 crore and at 12% for MFIs with a loan portfolio of less than Rs. 100 crore. Further mandatory use of credit bureaus and debt ceilings have restricted overleveraging for borrowers and are a positive for the sector in the long term. Since these regulatory changes were introduced, almost all the NBFC-MFIs have started contributing data to the credit bureaus. This has helped in checking the number of loans, quantum of loans and credit track record of a borrower. These checks have helped in reducing incidence of overleveraging as well as filtering of delinquent borrowers-these measures are likely to have a good long term impact on credit quality of the MFIs. However some banks which have ventured into microfinance and most of the SHGs still donot contribute the data to credit bureaus. RBI's circular of July 2013 clarifying that the priority sector benefit to MFIs continues, acts as a positive for the sector over the medium term as it points to the prospect of continued bank funding for the sector. However "The Micro Finance Institutions (Development and Regulation) Bill, 2012" is still awaiting which was awaiting the parliament approval, which leaves the sector exposed to the risk of AP-like state-level intervention. Though the overall operating environment is improving, some MFIs are venturing into relatively riskier individual loans and other secured and unsecured loan products, while remaining focused on politically and communally sensitive borrower groups. The external factors such as occurrence of political or communal issues may also have a long-term impact if they affect the credit culture of the borrowers at large. Though the potential remains huge, maintaining control over asset quality by building strong systems without compromise on internal audit and controls and building adequate cushions to absorb event risks would be important for NBFC-MFI's credit profile.
2	Governance Structure, Management and Systems	Transparent shareholding pattern; shareholders have a good representation on the Board. Utkarsh has a five member board with all the directors experienced in their respective area of expertise. The board has one investor director (representatives from Aavishkaar), two independent directors of who have finance/Microfinance expertise and

	Parameters	Overall Comments
		two executive directors. The board meets on a quarterly basis and if required it may meet more often. The Utkarsh Board is actively involved in strategy formulation and also approves the company's business plan. The Board is also involved in areas related to HR and Training, Social Performance Initiatives as well as introduction of new products. The company has an experienced and professional second and third line of management and is working on developing this team as well as standardising of training modules and procedures for managing the planned growth. As for Management Information System, Utkarsh has moved to mobile based collections and disbursements. The Internal Audit Process of the company is robust with each branch being audited once a quarter. The company has a formal Risk policy, branch risk rating model and grievance redressal mechanism in place.
3	Scalability (in relation to business plans)	The company intends to grow at a CAGR of around 60-65% over the next three years while diversifying into the newer states ventured into and in ICRA's view, ability of the company to manage growth, recruit and train personnel in line with the planned branch expansion and replacing existing employees especially at field level for the existing attrition rates of 24-25% would be important. To mitigate this risk the company has scaled up its training facilities and has also engaged an external consultant for Upgradation of training modules. The recruitment process has also been decentralized As for capital requirement, In ICRAs estimates, the company would require Rs 100-Rs 150 crore capital over the next two years to meet its growth plans and based on the track record of equity raising in the past, ICRA expects the company to be able to raise equity in a timely manner.
4	Asset Quality	Though Utkarsh is in growth phase and its track record is moderate, it has been able to maintain sound asset quality with 99.9% repayment rates till June 2014. Further, Utkarsh has good origination processes, all incremental sanctions are processed post credit bureau checks; rigorous supervision by operations team & regular follow up audits by Internal Audit Department have also helped the company to maintain asset quality indicators. So far, Utkarsh has not been affected by any political or external environmental issues. Utkarsh's geographical concentration in the state of Uttar Pradesh though declining continues to remain high at 58% as on March 31, 2014. Though the company is diversifying into newer geographies and newer products, ability of the company to maintain the same level of asset quality while growing and diversifying the portfolio at a higher asset base would be the key grading sensitivity going forward as well.

B	**Financial Risk**	
1	Liquidity and Funding Profile	Utkarsh's financial flexibility improved further in 2013-14 .The lender base consists of eleven Public sector banks/DFIs, ten private sector banks and seven NBFCs and three investors for NCD. The company has also started operating as a Business Correspondent and with NBFC-ND allowed to be Business Correspondents, these lines could increase going forward The company has a comfortable liquidity profile with the tenor of assets being shorter than that of liabilities. Based on the current sanctions in hand, the company would be able to meet incremental planned disbursements for about 3 months, however regular flow of funds would be crucial to maintain as well as grow business operations over longer term
2	Capitalisation	While the current capitalisation levels of Utkarsh were comfortable (Net Worth in Relation to Managed advances of 18% as on June 30, 2014), supported by regular capital infusions despite high portfolio growth in the past ,the company would require regular capital infusions to meet it growth plans. In ICRA's view the company would require around Rs 100-Rs 150 crore capital to meet its growth plans and based on the track record of equity raising in the past, ICRA expects the company to be able to raise equity in a timely manner. As for reported Capital adequacy Ratio, the company reported regulatory CRAR of 22.64% against the required level of 15%
3	Profitability	As for earning profile, the profitability indicators of Utkarsh improved from 1.81% in 2012-13 to 1.98% in 2013-14 and declined marginally in Q12014-15 owing to some rise in financial cost due to cash holding in March supported primarily by moderation in operating expenses in relation to managed advances from 9.38% in 2012-13 to 7.32% in 2013-14(7.94% in Q12014-15) owing to economies of scale, increase in ticket sizes and portfolio per branch) and low credit costs (0.52% in 2013-14). This coupled with increased in gearing levels helped the company to increase the Return on Equity from 8% in 2012-13 to 12% in 2013-14. (12% in 2014-15). As for incremental profitability, though portfolio yields are expected to decline owing to the reduction in the interest rate charged to customers by 1% to 25% from April 2014 onwards however a commensurate decline in cost of funds owing to improvement in credit profile and increased funding from banks is likely to help Utkarsh in maintaining the interest spreads. Additionally, some further moderation in operating expenses and fee based income initiatives such as opening of NPS accounts as well as the recent RBI notification allowing NBFC-ND to act as Business Correspondents could help the company to maintain ROE of 13-18%.

Strengths

- Company continues to focus on areas of moderate penetration in rural regions of UP, MP, Bihar and Uttarakhand . Management is well aware of negative areas within the target geographies, geographical diversification likely to improve going forward.
- Relatively prudent credit policies, as company does not offer midterm loans, lends to people staying for atleast 3 years at same location, performs borrower wise cash flow analysis , credit bureau checks mandatory
- Experienced and professional management team, good second and third line of management team as well
- Strong investor profile, with IFC , Norwegian Microfinance Initiative(NMI) and Aavishkaar Goodwell as the investors
- Good MIS, Risk Management and Internal Audit, systems
- Large & diversified funder base as well as funding instruments
- Incentives to loan officers capped beyond forming 80 members per month thus reducing the risks associated with high growth by compromising portfolio quality
- Good asset quality indicators with repayment rate of over 99.9% so far

Challenges

- To mobilise capital to meet the growth plans
- Ability to maintain the same level of asset quality while growing and diversifying the product profile as well as portfolio geographically
- Ability to recruit and train personnel to me the expansion plans and attrition rates especially at field level
- Ability to improve geographical diversification of operations further

Governance Structure, Management and Systems

Ownership Structure

Table 3: Shareholding Pattern as on March 31, 2014

	Mar-12	Mar-13	Mar-14
	% share	% share	% share
Aavishkaar Goodwell India Microfinance	31.03%	31.32%	30.75%
Norwegian Microfinance Initiative		27.38%	25.53%
International Finance corporation	16.69%	15.58%	14.53%
Individual shareholders	33.38%	14.20%	13.42%
Promoters	14.79%	6.40%	11.20%
Intellecash Microfinance Network	0.44%	0.19%	0.17%
ESOP	3.36%	4.85%	4.39%
Total	**100.00%**	100.00%	100.00%

Promoters' shareholding increased to 11.20% in 2013-14 owing to exercise of preference rights . Aavishkaar Goodwell India Microfinance and Norwegian Microfinance Initiative and IFC have are invested in the in the company through various equity infusion rounds. The company is in advanced stages of raising around Rs 120 crore of capital, and 2 new investors are expected to invest in Utkarsh by end of October 2014.

Board Structure and Processes

Table 4: Board of Directors as of March 31, 2014:

Name	Designation
Govind Singh	MD & CEO
Trilok Nath Shukla	Whole time Director
Ajay Maniar	Aavishkaar Goodwell Representative
Ramni Nirula	Independent Director
Vijayalakshmi Das	Independent Director

Utkarsh had a five member board with all the directors experienced in their respective area of expertise. The board has one investor directors (representatives from Aavishkaar),two independent directors of which two have finance/Microfinance expertise and two executive directors. The board meets on a quarterly basis and if required it may meet more often. The Utkarsh Board is actively involved in strategy formulation and also approves the company's business plan. The Board is also involved in areas related to HR and Training, Social Performance Initiatives as well as introduction of new products.

Management

Mr. Govind Singh is the promoter of the company and is holding the position of Managing Director and CEO. He started the company in August 2009 with an experienced management team acting as functional heads. Mr Govind Singh was the former business head for microbanking at ICICI Bank. He was responsible for Building ICICI Bank's microfinance funding portfolio (wholesale funding to MFIs), maintaining relationships with and developing the Business Correspondent Model. Mr Govind Singh is assisted by functional Heads (Core Team Members) who have been associated with the company since inception. All the functional heads have good experience in their relevant areas and the company has expanded the second and third line of management to meet the planned growth in the medium term

A hub structure has been created for managing operations. Three hubs have been created- Hub-1 which will focus on Eastern Uttar Pradesh and Bihar Hub-2 which will cater to NCR, Western Uttar Pradesh, Uttarakhand,Punjab, Haryana. Himachal Pradesh, and Hub-3, which will cater to Maharashtra & Madhya Pradesh.Two VP operations have been recruited, who have good local knowledge of the areas of operation. Further, the teams in all functions have been strengthened (treasury, finance, and audit). The company is also focusing on strengthening the training process and a dedicated training head has been recruited and an HR firm Global Talent also has been mandated by then to formalise the training modules.

Field officers who are on the rolls of the company handle entire operations. At the field level, the field officers report to the Branch Managers who in turn report to the Area Managers. Each Area Manager handles 3 branches and reports to Divisional Head who handles 3-4 areas. The Area Manager reports to a Divisional manager who in turn reports to the Regional Head.

The attrition rate of the company is 25% as a whole. For the trainee field officers, the attrition rate is higher about 40-45%. If we were to remove the staff who left within 6 month of joining, the attrition rate and that at the senior level is relatively low. (4-5%)

Systems and Processes

IT Systems

Utkarsh completely moved to mobile based collections in 2013-14 and is at present planning to migrate originations i.e. loan application, CGT and GRT as well through mobile based platform for which pilots are going on. The company is using a web based module implemented by by Craft Silicon, with an integrated Accounting module. This software is quite comprehensive, capturing all client details, loan purpose, client attendance, loan details and also the track record of the loan repayment and delinquency details, if any is appropriately maintained. The software is integrated with the mobile phones being carried by loan officers, which has helped in elimination of use of collections and disbursement sheet (CDS) used earlier by Loan officers

Some of the key features of the MIS systems of the company are

- Attendance Tracking at member level
- Portfolio cuts based on purpose, region, product, IRR, cycle of loan, religion
- Tracking Loan Utilisation Check in Collection and Disbursement Sheet

Benefits of Mobile Technology:

- • Real time updates of financial (like disbursement, collection, pre-closure) and non-financial transactions (like Attendance, Loan utilization Checks).
- • Reduced turnaround time.
- • Daily closures of business.
- • Real time tracking of collection and disbursement.
- • Efficient monitoring of Centre Meetings, LUC etc. by supervisors through use of mobile reports.
- • Reduction in operational errors due to close tracking.

Internal Audit Process

Utkarsh has developed a two tier Internal Audit System where all branches go through atleast one of the following types of audits every month The company has a ten member internal audit team and internal audit plan is prepared in advance and the team of auditors schedule the audits accordingly. All audits are surprise audits

- Short Audit – lasts for 2-3 days every branch with more than 500 clients to be covered monthly
- Comprehensive Audit -lasts for 6-8 days, every branch to be covered atleast quarterly

The company has developed a comprehensive checklist, with weightages for each parameter for the comprehensive audit. The checklist is comprehensive and covers the field operations, record keeping, statutory compliances, accuracy of Management Information Systems (MIS), monitoring mechanism and compliance with code of conduct.

The comprehensive audit process for each branch lasts for 6 days. The audit team stays in the respective branches for six days and verifies all the records and documents corresponding to that particular branch. The audit members also accompany the Loan officers to the centre meetings to verify the collection processes at the field level. Upon completion of audit detailed audit reports are prepared and submitted to the Head Internal Audit who consolidates all the audit reports and submits it to the Managing Director. An Audit report is not complete till the deficiencies observed in the previous audit are complied with.

The company has also introduced concurrent audit from current financial year. The concurrent audit is mainly focussed on treasury management, and audit the various non operation department.

Risk Management Systems

Apart from the regular branch audit , the company has also put in a Branch Risk Rating model in place, wherein apart from the feedback from the branch audit report, the status of credit risk and operational risk in the branches and is assessed based on Portfolio concentration, audit score, turnover of field staff, client acquisition and Portfolio at Risk. Scores are assigned in the category of critical, High, Moderate and low. Further, each new product and new area proposed would also need approval from the Risk Committee

Client Protection Practices

The company has developed a robust client protection practices in place, which is reflected in its relatively conservative credit policies. Some of the key highlights of the credit policies of Utkarsh are as follows.

- All sanctions are to take place post checking with Credit Bureau
- No Mid Term Loans
- Loan application captures family's outstanding loans
- Borrower wise cash flow analysis is part of the disbursement form

The company has also put in a good grievance redressal mechanism in place with a dedicated phone line for grievances and a grievance redressal committee which meets every month at Head office. Incentive structures for loan officers are also controlled and capped for new client acquisitions beyond 80 clients. Further, the company also contributes 2% of its Profit Before Tax to Samutkarsh Welfare Services a section 25 not for profit company, primarily to undertake credit plus activities.

Accounting Policies

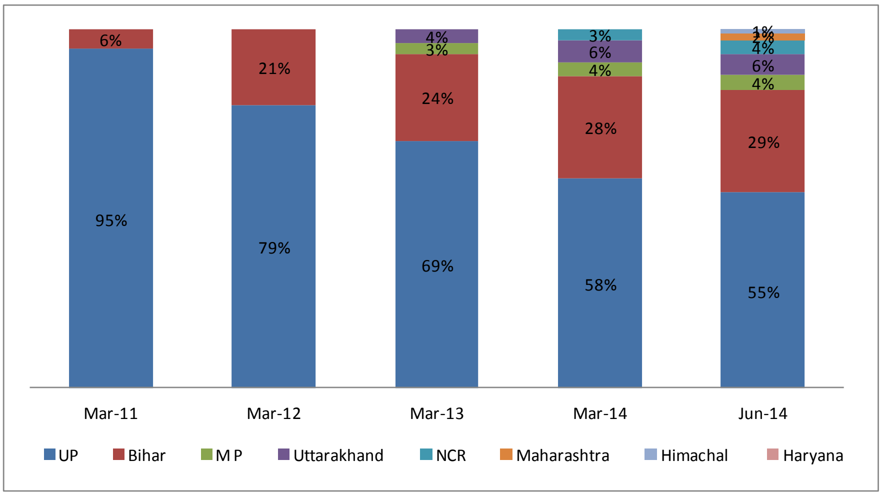
Utkarsh books interest income on the industry-accepted Internal Rate of Return (IRR) basis. Utkarsh's Provisioning policy is as per the RBI norms. As for the income recognition on assigned/securitised portfolio, the company amortises the profit on sale of loan portfolio over the tenure of the loan portfolio assigned /sold.

Scalability

Table 5: Operational Trends:

	MAR-10	MAR-11	MAR-12	MAR-13	MAR-14	JUN-14
NO OF STATES	1	2	2	5	8	8
TOTAL BRANCHES*	13	52	75	102	142	166
TOTAL CENTERS*	499	3,902	7,826	14,369	20,476	23,134
TOTAL MEMBERS*	8,719	58,623	110,886	200,066	337,543	381,096
TOTAL ACTIVE BORROWERS	8,208	55,506	106,369	197,874	317,900	358,437
TOTAL GROUPS*	1753	12,456	25,816	49,087	80,181	85,844
CREDIT PORTFOLIO	6	32	75	178	356	420
GROWTH (ANNUALISED %)	5106%	433%	134%	137%	100%	72%
NO. OF EMPLOYEES	114	325	408	623	1032	1,252
GROWTH IN EMPLOYEE BASE		185%	26%	53%	66%	21%
CREDIT OFFICERS	73	195	216	341	575	705
GROWTH IN CREDIT OFFICERS		167%	11%	58%	69%	23%
ACTIVE BORROWERS PER BRANCH	631	1,067	1,418	1,940	2,239	2159
ACTIVE BORROWERS	112	285	492	580	553	508
PORTFOLIO PER BRANCH	0.46	0.62	1	1.75	2.5	2.44
GROWTH		33%	63%	75%	44%	-2%
LOAN OUTSTANDING PER BORROWER	7310	5765	7051	8996	11187	11314
GROWTH		-21%	22%	28%	24%	1.13%

Chart 2 : State Wise Break-up of Portfolio



Utkarsh reported a 100% growth in portfolio in FY2013, The no of active borrowers per branch and credit officer also improved with improvement in borrower penetration per branch and shifting towards fortnightly mode of repayment (from weekly) to enable more no of borrowers to be covered per credit officer. In FY13 the company expanded its presence from 5 states to 8 states, which resulted in decline in geographical concentration of its portfolio in UP from 68.5% as on Mar-13 to 58% as on Mar-14 and further to 55% in June 14. The company plans to further expand to the states of Bihar,MP and Uttarakhand , Haryana and Maharashtra in the current financial year. Nevertheless, UP and Bihar are likely to continue to have a majority share of the portfolio in the medium term being an area of moderate penetration and good potential . The company has been scaling up operations at a fast pace as it is still in growth phase However, the company has been following a contiguous expansion strategy (expansion in neighbouring districts within states) to monitor the portfolio more effectively. Further, extensive surveys are done before entering any village, covering poverty levels, literacy levels, population, various risks in the area, primary occupation of the villagers etc. Extensive community meetings are also conducted before members are admitted.

Access to capital

Table 6: Capitalisation Trends

Rs crore	Mar-12	Mar-13	Mar-14	Jun-14
Net Worth	33	64	74	77
Managed Advances	75	178	357	420
Net Worth/Managed Advances	43.30%	36.07%	20.82%	18.22%
Gearing (including off balance sheet book)	2.84	3.45	6.00	5.60
Gearing (excluding off balance sheet book)	1.72	2.81	5.04	4.83

Source : Company , ICRA Analysis

The company plans to grow at a CAGR of 65% for the next three years for which the external capital requirement would be around 120-150 crore. The company is in advance stages of raising equity from a consortium of existing and fresh investors and is expecting an infusion of $20-21 million by October 2014. Since the foreign shareholding of Utkarsh is likely to go beyond 75% post this infusion, the company would need to bring in another $20 million in 2 years time from the infusion i.e. by October 2016.

Table 7: Capital Requirement for next three years

Rs crore	3 Year CAGR in portfolio							
Internal Capital Generation	30%	40%	50%	60%	70%	80%	90%	100%
5%	44	81	123	171	225	284	350	422
7.00%	39	74	116	163	216	275	341	413
9.00%	33	67	109	156	208	267	332	403
11.00%	28	60	101	148	200	258	323	394
13.00%	23	53	94	140	192	250	314	384
15.00%	17	48	86	132	184	241	305	375
17.00%	12	42	79	124	175	232	295	365

Source : ICRA Analysis

Human Resources

With scaling up of business, Utkarsh would require a larger number of trained employees to support its operations. At the field officer level, the basic requirement is that the staff must have passed 12th Standard, with knowledge of the local language and good communication skills. The staff is trained at the company's training centres and the training procedures are standardised. Company has decentralised its training procedures and has 7 training centres. Every employee goes through 5 days of classroom training, followed by a test and 5 days of field training. After the field training, the employee is sent for 3 months of on the job training on the field. During this period they remain in 1 branch. In the first 1-1.5 months they work with an existing credit officer, post which they are permitted to form groups if they are found capable of doing so.

After confirmation a person is placed at a place which is 40-50 kms away from their home and in another district. The officers are rotated across branches atleast once in 6 months. Refresher trainings for new products, code of conduct, compliance are held once in three months at divisional offices. The company has kept alternate Saturdays exclusively for training purposes. The field officers report to the Branch Managers who in turn report to the Area Managers. Each area manager handles 3 branches and reports to divisional manager who handles 9 branches. The Area Manager reports to a Divisional Head, who reports to Regional Manager. The Regional Manager reports to Zonal Manager who in turn reports to the COO/Hub in Charge.

Utkarsh intends to grow at a fast pace in the medium term with plans of adding around 100 branches in FY2015. Owin**g** to large expansion plans coupled with relatively high attrition rates at field staff level given the tough nature of job and adverse climatic conditions in the main area of operations , the company would require to recruit and train personnel at a fast pace in the medium term. ICRA has noted company's efforts to scale up its training facilities and also engaging an external consultant for Upgradation of training modules. The recruitment process has also been decentralised. The company has issued ESOPs to retain senior and middle management.

Tie-up of funding sources

Table 8: Funding Profile

Rs crore	Mar-13		Mar-14		Jun-14	
Networth	64		74		77	
Term Loans from Banks	59	27%	244	55%	234	55%
Term Loan from FIs	122	55%	55	12%	37	9%
Debentures	-	0%	76	17%	100	23%
Off balance sheet	41	18%	71	16%	58	14%
Total Borrowings (incl Off B/s)	222	100%	446	100%	428	100%
Gearing (assuming assigned book as debt)	3.45		6.00	1%	5.60	1%

Source : Company, ICRA Analysis

The company has been able to diversify its resource profile , with increase in share of funding from banks and Non Convertible Debentures. With the increase in share of bank funding, the weighted average cost of funds also moderated by around 50 bps to around 14%. The lender base consists of eleven Public sector banks/DFIs, ten private sector banks and seven NBFCs and three investors for NCD. The company has also started operating as a Business Correspondent for IndusInd Bank, where Utkarsh is acting as a sourcing agent and servicer for the bank's microfinance portfolio with a first loss default guarantee provided by Utkarsh. The share of such lines could increase going forward with NBFC-ND allowed to work as Business Correspondents. The company has a comfortable liquidity profile with the tenor of assets being shorter than that of liabilities. Based on the current sanctions in hand, the company would be able to meet incremental planned disbursements for about 3 months, but would require additional funding for meeting planned, however regular flow of funds would be crucial to maintain as well as grow business operations

Financial Performance

Table 9 : Profitability Indicators

Key Ratios	Mar-12	Mar-13	Mar-14	Jun-14
Net Interest Margin)/AMA	9.5%	7.8%	7.6%	8.6%
Non Interest Income/AMA	1.44%	0.78%	0.94%	0.80%
Operating expenses (excl. royalty) / AMA	8.15%	5.54%	4.72%	5.81%
Operating Expenses/ Managed advances	13.05%	9.38%	7.32%	7.91%
Operating Profit / AMA	2.76%	3.05%	3.80%	3.57%
Credit Prov. & Write-offs / AMA	0.26%	0.26%	0.52%	0.66%
Operating Profits (net of credit provisions) / AMA	2.51%	2.79%	3.28%	3.68%
PBT/ AMA	2.51%	2.79%	3.28%	2.91%
PAT/ AMA	1.65%	1.81%	1.98%	1.71%
PAT/Average Net Worth	6.25%	8.03%	11.87%	11.97%

Source: Company Financials , ICRA Analysis

Utkarsh's earning profile improved in 2013-14 owing to reduction in operating expenses from 2012-13 levels owing to increase in scale of operations and ticket sizes and low credit costs. This coupled with increased in gearing levels helped the company to increase the Return on Equity from 8% in 2012-13 to 12% in 2013-14. (12% in 2014-15). As for incremental profitability, though portfolio yields are expected to decline owing to the reduction in the interest rate charged to customers by 1% to 25% from April 2014 onwards however a commensurate decline in cost of funds owing to improvement in credit profile and increased funding from banks is likely to help Utkarsh in maintaining the interest spreads. Additionally, some further moderation in operating expenses and fee based income initiatives such as opening of NPS accounts as well as the recent RBI notification allowing NBFC-ND to act as Business Correspondents could help the company to maintain ROE of 13-18%.

COMPANY PROFILE—Utkarsh Micro Finance Private Limited

Date of Incorporation	May,1990
Constitution	Non-Deposit Taking NBFC
Registered Office	S-2/639-56, Varuna Vihar colony, J.P Mehta Road, Cantt. Varanasi-221002 (U.P.) India
Corporate Office	S-2/639-56, Varuna Vihar colony, J.P Mehta Road, Cantt. Varanasi-221002 (U.P.) India
Net Worth (Mar-2014)	Rs. 74 crore
Number of Branches (Mar-14)	151
Number of active borrowers (Mar-14)	317,900
Number of field officers (Mar-14)	575

Managing Director	Mr Govind Singh	
Auditors	BSR and CO (KPMG)	
Shareholding Pattern (Mar-14)		Mar-14
		% share
	Promoters	11.20%
	Individual Shareholders	13.42%
	International Finance Corporation	14.53%
	Aavishkaar Goodwell	30.75%
	NMI (NMI Frontier Fund KS)	25.53%
	Intellcash Micro Fin. Network	0.17%
	Utkarsh ESOP Welfare Trust	4.39%
	Total	100.00%

Board of Directors	Name	Designation
	Govind Singh	MD & CEO
	Trilok Nath Shukla	Whole Time Director
	Ajay Maniar	Aavishkaar Goodwell Representative
	Ramni Nirula	Independent Director
	Vijayalakshmi Das	Independent Director

Key Financials

PROFIT & LOSS ACCOUNT	Mar-12	Mar-13	Mar-14
Interest Income (Net of Business Origination Costs and incl. processing fees)	10.0	27.4	64.0
Interest Expenses (including Preference Dividend)	3.5	12.9	35.0
Net Interest Income	6.5	14.5	29.0
Non Interest Income	1.2	1.7	3.9
Operating Income	7.7	16.2	32.9
Operating expenses	7.0	11.9	19.6
Operating Profits	0.7	4.3	13.4
Provisions including NPA provisions	0.2	0.6	2.2
Income from Securitization / Assignment	1.7	2.2	2.4
Net profit on sale of securities and assets	0.0	0.0	0.0
Profit Before Tax (before extraordinary items)	2.2	6.0	13.6
Extraordinary Items	0.0	0.0	0.0
Profit Before Tax (PBT)	2.2	6.0	13.6
Tax	0.7	2.1	5.4
Profit After Tax (PAT)	1.4	3.9	8.2
Equity dividend	0.0	0.0	0.0
Accretion to reserves	1.4	3.9	8.2
SUMMARY ASSETS			
Net Hire Purchase/ Loan/ Lease Assets	39.8	139.5	291.8
Investments - Strategic	0.0	0.0	0.0
Investments - Short Term Surpluses	0.1	0.1	0.0
Cash & Bank Balances	52.7	112.3	157.9
Advance Tax paid	0.1	0.2	0.3
Other Current Assets	1.3	4.7	14.2
Net Fixed Assets	0.5	0.7	1.6
Total Assets	94.4	257.5	465.9
Off-balance sheet receivables	36.5	40.7	71.0
Total Managed Assets	130.8	298.2	536.9
SUMMARY LIABILITIES			
Equity Share Capital	10.2	24.1	25.9
Reserves	22.4	40.2	48.4
Net Worth	32.6	64.3	74.3
Total Borrowings (including Preference Shares)	56.2	180.9	374.6
Other Current Liabilities & Provisions	5.5	12.3	17.0
Total Liabilities	94.3	257.5	465.9

Amounts in Rs. Crore, Source: Company, ICRA analysis

GROWTH RATES	Mar-12	Mar-13	Mar-14
PROFIT & LOSS ACCOUNT			
Interest Income (Net of Business Origination Costs and incl. processing fees)	36%	175%	134%
Interest Expenses (including Preference Dividend)	26%	266%	172%
Net Interest Income	41%	125%	100%
Non Interest Income	-22%	35%	133%
Operating Income	25%	111%	103%
Operating expenses	38%	70%	65%
Provisions including NPA provisions	72%	151%	293%
Income from Securitization / Assignment	2795%	32%	8%
Profit Before Tax (before extraordinary items)	108%	178%	127%
Profit Before Tax (PBT)	108%	178%	127%
Tax	498%	184%	155%
PAT (Reported)	55%	175%	109%
Accretion to reserves	55%	175%	111%
SUMMARY ASSETS			
Net Hire Purchase/ Loan/ Lease Assets	66%	251%	109%
Investments - Short Term Surpluses	106%	-51%	-11%
Cash & Bank Balances	681%	113%	41%
Advance Tax paid	102%	205%	50%
Other Current Assets	-16%	278%	201%
Net Fixed Assets	53%	56%	116%
Total Assets	190%	173%	81%
Off-balance sheet receivables	340%	11%	75%
Total Managed Assets	221%	128%	80%
SUMMARY LIABILITIES			
Equity Share Capital	0%	136%	7%
Reserves	833%	79%	20%
Net Worth	159%	97%	16%
Total Borrowings (including Preference Shares)	203%	222%	107%
Other Current Liabilities & Provisions	309%	122%	38%
Total Liabilities	190%	173%	81%

COMMON SIZE STATEMENTS	Mar-12	Mar-13	Mar-14
PROFIT & LOSS ACCOUNT (% of Operating Income)			
Net Interest Income	84%	90%	88%
Non Interest Income	16%	10%	12%
Operating Income	100%	100%	100%
Operating expenses	91%	73%	59%
Operating Profits	9%	27%	41%
Provisions including NPA provisions	3%	3%	7%
Income from Securitization / Assignment	22%	14%	7%
Net profit on sale of securities and assets	0%	0%	0%
Profit Before Tax (before extraordinary items)	28%	37%	41%
Extraordinary Items	0%	0%	0%
Profit Before Tax (PBT)	28%	37%	41%
Tax	10%	13%	16%
Profit After Tax (PAT)	18%	24%	25%
Equity dividend	0%	0%	0%
Accretion to reserves	18%	24%	25%
SUMMARY ASSETS (% of Total Assets)			
Net Hire Purchase/ Loan/ Lease Assets	42%	54%	63%
Investments - Strategic	0%	0%	0%
Investments - Short Term Surpluses	0%	0%	0%
Cash & Bank Balances	56%	44%	34%
Collaterals for Securitization	0%	0%	0%
Advance Tax paid	0%	0%	0%
Other Current Assets	1%	2%	3%
Net Fixed Assets	0%	0%	0%
Total Assets	100%	100%	100%
Off-balance sheet receivables	39%	16%	15%
Total Managed Assets	139%	116%	115%
SUMMARY LIABILITIES (% of Total Liabilities)			
Equity Share Capital	11%	9%	6%
Reserves	24%	16%	10%
Net Worth	35%	25%	16%
Total Borrowings (including Preference Shares)	60%	70%	80%
Interest Accrued but not due	0%	0%	0%
Provisions for Tax	0%	0%	0%
Other Current Liabilities & Provisions	6%	5%	4%
Deferred Tax Liability	0%	0%	0%
Total Liabilities	100%	100%	100%

KEY FINANCIAL RATIOS	Mar-12	Mar-13	Mar-14
OPERATING RATIOS			
Yield on Average Loans (Net of BO Costs)	27.6%	27.3%	26.4%
Yield on Average Investments	3.7%	3.7%	4.9%
Yield on Average Earning Assets (Net of BO Costs)	16.6%	16.7%	18.5%
Cost of Average Interest Bearing Funds	9.4%	10.9%	12.6%
Gross Interest Spread	7.2%	5.8%	5.9%
PROFITABILITY RATIOS			
Net Interest Margin/ Average Managed Assets	9.5%	7.8%	7.0%
Fee based Income/ Average Managed Assets	1.4%	0.8%	0.9%
Operating Expenses /Average Managed Assets	8.1%	5.5%	4.7%
Operating Expenses/Average Managed Advances	13.1%	9.4%	7.3%
Operating Profit / Average Managed Assets	2.8%	3.1%	3.2%
Provisions /Average Managed Assets	0.3%	0.3%	0.5%
Net profit on sale of securities and assets / Average Managed Assets	0.0%	0.0%	0.0%
Profit Before Tax (before extraordinary items)/ Average Managed Assets	2.5%	2.8%	3.2%
Tax / Profit Before Tax	34.3%	35.1%	39.7%
Profit After Tax / Average Managed Assets	1.6%	1.8%	1.9%
Profit After Tax / Average Net worth	6.3%	8.0%	11.7%
EFFICIENCY RATIOS			
Fee Based Income/Operating Expenses	17.7%	18.6%	20.9%
Operating Cost/Operating Income	74.7%	64.5%	55.4%
CAPITALISATION RATIOS			
Net Worth/ Total Assets	34.6%	25.0%	15.9%
Total Debt / Net worth(on book)	1.72	2.81	5.04
Net NPA/Net worth	0.0%	0.0%	0.0%
COVERAGE RATIOS			
PBIT/ Total Interest	1.61	1.47	1.39

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