Stock Idea Note - Fusion Finance Ltd.

Company Overview

Fusion Finance Limited, incorporated in 1994, is a Gurugram-headquartered NBFC-MFI that has evolved from a development-focused microfinance institution into one of India's larger regulated microfinance lenders. Backed by Creation Investments, the company has built its franchise primarily around providing small-ticket, unsecured credit to underserved women borrowers in rural and semi-urban India through the Joint Liability Group (JLG) model. As of Q1FY27, Fusion had an AUM of Rs. 7,702 crores, with microfinance remaining the dominant business at approximately Rs. 6,906 crores, or 89.7% of the portfolio. The core MFI business provides small-ticket loans to rural women entrepreneurs, with an average ticket size of around Rs. 61,000. The company has gradually expanded beyond its core MFI franchise into secured MSME lending, primarily through Loans Against Property, which stood at Rs. 796 crores and accounted for 10.3% of AUM, with typical ticket sizes of Rs. 7.5-8 lakhs, while the legacy personal and consumer loan book remains negligible. Fusion has also recently launched Individual Loans of around Rs. 1.5 lakhs for established MFI customers with stronger business and repayment track records, creating a pathway to address their evolving credit requirements beyond the traditional JLG model. The company operates through a large branch-led distribution network across 22 states, providing direct access to customers in rural and semi-urban markets while also allowing it to leverage its existing franchise for sourcing its newer lending products. Geographically, the portfolio has a meaningful concentration in North and East India, with Uttar Pradesh accounting for 26%, followed by Bihar at 19%, Madhya Pradesh at 9% and Odisha at 8%, while Tamil Nadu, Rajasthan and Jharkhand contribute around 5% each. Consequently, the top three states account for more than half of the portfolio, making local credit conditions and collection trends in these markets particularly important to the business. Fusion is therefore fundamentally a rural-focused credit franchise, with its strategy centered on strengthening its core MFI customer base while gradually diversifying into higher-ticket secured MSME and individual lending.

Investment Rationale

Portfolio repair and tighter underwriting provide the foundation for a sustainable MFI growth recovery

Fusion Finance appears to be moving beyond the portfolio repair phase, with the recovery in asset quality providing room to gradually restore growth in its core MFI franchise, which forms 90% of its book as on Q1FY27. The company has deliberately tightened customer selection and credit guardrails, with 85% of Q1FY27 disbursement customers having only one other lender, reducing exposure to highly leveraged borrowers. A crucial part of this recovery has been the strengthening of its underwriting architecture through the Portfolio Quality Management (PQM) framework. Under this model, dedicated quality and credit personnel independently assess borrowers and portfolio quality and report into the credit function rather than the sales hierarchy, helping create a clearer separation between growth targets and credit decisions. The framework is currently operational across 250 large MFI branches and provides greater branch-level oversight as the company prepares to scale disbursements again. These measures are already beginning to reflect in portfolio performance, with GNPA declining to 2.51% in Q1FY27 from 3.21% in Q4FY26, while collection efficiency improved to 99.76%. As collections stabilise and portfolio quality improves, management has begun gradually relaxing certain credit guardrails in stronger-performing branches, creating scope for higher disbursements from a significantly healthier base. The company's branch-led franchise across rural and semi-urban markets provides the distribution infrastructure to capture this recovery, while the existing customer base offers a relatively familiar pool for repeat lending. This should support Fusion's ambition to grow AUM towards Rs. 10,000 crores by FY27E, implying around 30% growth from Rs. 7,702 crores as of Q1FY27, although execution will remain dependent on maintaining the current discipline around borrower leverage and collections. In our view, is that the company is attempting to rebuild growth with a more institutionalised underwriting framework already in place, which should help contain credit costs as the MFI franchise returns to a stronger growth trajectory.

Stock Rating

BUY	HOLD	SELL
■		
> 15%	-5% to 15%	< -5%

Sector Outlook Positive

Stock

CMP (INR)	203
Target Price (INR)	238
NSE Symbol	FUSION
BSE Code	543652
Bloomberg	FUSION IN
Reuters	FUSION.BO

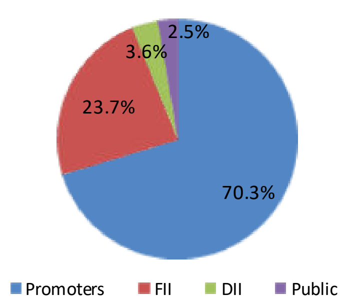
Key Data

Nifty	23,898
52WeekH/L(Rs.)	243/136
O/s Shares (Cr.)	16.2
Market Cap (Rs, Cr.)	3,290
Face Value (Rs.)	10

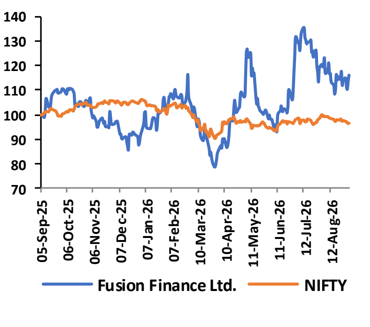
Average volume

3 months	9,94,678
6 months	7,64,736
1 year	5,94,442

Share Holding Pattern (%)



Relative Price Chart



Leveraging Fusion's existing customer and branch franchise can unlock a more diversified growth opportunity

While the recovery of the core MFI business remains essential, Fusion's longer-term opportunity lies in using its existing customer relationships and branch infrastructure to build a more diversified lending franchise. The company has gradually created a progression from small-ticket MFI loans to Individual Loans and eventually larger-ticket secured MSME lending, allowing it to retain customers as their businesses and financing requirements expand rather than losing them to banks, SFBs or other lenders. The opportunity is particularly attractive because Fusion does not need to build an entirely new distribution franchise to scale these businesses. Its MSME vertical already uses around 200 existing MFI branches through a hub-and-spoke model, enabling the company to leverage its established presence in Tier 3 and Tier 4 markets while maintaining separate underwriting for larger-ticket secured loans. MSME AUM stood at Rs. 796 crores, or around 10.3% of total AUM as of Q1FY27 and management is targeting the segment to reach 15% of the portfolio next year and around 20% within two years. This would gradually reduce the company's dependence on unsecured microfinance while increasing the contribution from secured lending. The newly launched Individual Loan product in Q1FY27 further strengthens this strategy by creating an intermediate step for established MFI customers with stronger repayment records and business vintage. With an average ticket size of around Rs. 1.5 lakhs, compared with approximately Rs. 61,000 in the core MFI business, Fusion can increase its share of the customer's financing requirements while relying on repayment behaviour and customer knowledge developed through the existing MFI relationship. Management sees potential for Individual Loans to eventually reach 10% of MFI disbursements, although the product is being scaled gradually with tighter underwriting and MSME credit-team oversight for larger exposures. The diversification strategy also comes at a favourable point in the earnings recovery. NIM expanded by 49 bps QoQ to 11.93% in Q1 FY27, supported by a 250 bps YoY reduction in marginal borrowing costs to 10.1% and the repricing of the loan book, with management expecting a further 15-25 bps improvement by FY27-end as these benefits continue to flow through. Combined with lower credit costs, this provides scope for a meaningful improvement in profitability as the business scales. Fusion also has sufficient balance-sheet capacity to support this expansion, with CRAR of 36.95% and leverage of 2.3x. The Rs. 290 crores of unrecognised DTA over the next 24-26 months further supports PAT conversion. We therefore see Fusion's investment case evolving from a pure MFI recovery story into a broader franchise-building opportunity.

Valuation and Outlook

We expect Fusion Finance Ltd. to deliver a strong earnings recovery over FY26-FY28E, supported by the normalisation of credit costs, improving funding costs and a gradual return to growth in its core MFI franchise. The company has already demonstrated meaningful progress in Q1FY27, with GNPA declining to 2.51%, collection efficiency improving to 99.76% and credit costs continuing to fall for the seventh consecutive quarter, providing a substantially healthier base for growth. We expect AUM growth to accelerate towards management's Rs. 10,000 crores FY27 target, supported by the recovery in MFI disbursements and the gradual scaling of MSME and Individual Loans. While MFI will remain the dominant contributor in the near term, the expansion of secured MSME lending towards management's targeted 15-20% share of the portfolio should gradually diversify the book and reduce dependence on a single lending segment. We expect NIM to improve to around 11.9% in FY27E and 12.2% in FY28E, supported by the sharp reduction in marginal borrowing costs to 10.1%, continued repricing benefits and access to lower-cost funding under the Credit Guarantee Scheme. Management has indicated scope for a further 15-25 bps improvement in margins by the end of FY27, providing support to our estimates. As the loan book scales, improving spreads should combine with lower credit costs and operating leverage to drive RoA from 0.2% in FY26 to 3.5% in FY27E and 4.2% in FY28E, while RoE is expected to improve to 12.1% and 15.6%, respectively. The strong capital position also provides sufficient headroom to fund this growth, allowing the company to improve returns through a combination of earnings recovery and a gradual increase in financial leverage rather than requiring an immediate capital raise. The key risk to this recovery depends on the sustainability of the growth, without renewed deterioration in asset quality, collections or credit costs. The Portfolio Quality Management (PQM) framework and tighter borrower-selection criteria are therefore particularly important as the company moves from stabilisation towards growth. **We thus value the stock at 1.4x FY27E book value of Rs. 171 per share, arriving at a target price of Rs. 238, implying an upside of around 17% from the current price.**

Key Financials						
YE March (Rs. Cr.)	**FY23**	**FY24**	**FY25**	**FY26**	**FY27E**	**FY28E**
Net Interest Income	**1,600**	**2,092**	**2,134**	**1,533**	**1,760**	**2,273**
Growth (Y-o-Y)	*50.3%*	*30.7%*	*2.0%*	*-28.2%*	*14.8%*	*29.1%*
Operating Profit	**1,097**	**1,028**	**-338**	**362**	**501**	**737**
PPOP Growth (Y-o-Y)	*133.2%*	*-6.3%*	*-132.9%*	*-207.1%*	*38.2%*	*47.3%*
Net Profit	**387**	**505**	**-1,225**	**14**	**308**	**468**
Growth (Y-o-Y)	*1679.6%*	*30.5%*	*-342.3%*	*-101.1%*	*2123.0%*	*52.0%*
EPS	**23.9**	**31.2**	**-75.6**	**0.9**	**19.0**	**28.9**
Key Ratios						
NIM (%)	10.2%	11.2%	10.2%	10.8%	11.9%	12.2%
RoA (%)	**4.7%**	**4.8%**	**-12.2%**	**0.2%**	**3.5%**	**4.2%**
RoE (%)	21.2%	19.6%	-54.5%	0.7%	12.1%	15.6%
CASA (%)	**4.6**	**4.1**	**4.5**	**4.1**	**3.5**	**3.7**
BV per share (Rs.)	143.3	175.8	101.4	151.6	171.2	200.5
Valuation Ratios						
P/E (x)	8.5x	6.5x	-2.7x	237.4x	10.7x	7.0x
P/BV (x)	**1.4x**	**1.2x**	**2.0x**	**1.3x**	**1.2x**	**1.0x**

Source: Bloomberg, BP Equities Research

Understanding the FY25-FY26 financial volatility: From an industry-wide credit shock to portfolio repair

Fusion Finance's FY25-FY26 financial performance was materially impacted by the MFI credit cycle, with elevated credit costs and asset-quality stress resulting in a sharp deterioration in reported profitability. In FY25, weaker collections and significant borrower overleveraging across the industry resulted in a sharp increase in delinquencies and expected credit loss provisions. Fusion consequently reported impairment charges of around Rs. 1,869 crores, which drove the company to a net loss of Rs. 1,225 crores. The deterioration also resulted in elevated NPAs and pressure on the company's capital and leverage metrics, making FY25 an exceptional year rather than a sustainable earnings base.

FY26 was therefore primarily a year of stabilisation and portfolio repair rather than growth. Fusion deliberately reduced its exposure to highly leveraged borrowers, shrinking its active customer base by over 30% and allowing AUM to contract as it prioritised portfolio quality over disbursement growth. At the same time, the company strengthened its capital base through an approximately Rs. 800 crores rights issue, redesigned its underwriting architecture through tighter credit guardrails and the Portfolio Quality Management (PQM) framework, and strengthened collections by bringing harder-bucket recoveries increasingly in-house. As a result, credit costs declined sharply and asset quality progressively stabilised, although the benefits were only beginning to flow through the full-year FY26 earnings.

The stronger performance in Q1 FY27 therefore represents the early outcome of this repair process. The newer book originated under tighter underwriting standards has become increasingly dominant, while improved collections and lower incremental stress helped GNPA decline to 2.51%, collection efficiency reach 99.76%, and credit costs continue their multi-quarter moderation. With provisioning pressure reducing, the improvement in margins and operating profitability is now flowing through more clearly to earnings. We therefore view FY25 as the stress year and FY26 as the rebuilding year, with FY27E marking the beginning of a more normalised growth and profitability trajectory.

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Disclaimer Appendix

Analyst (s) holding in the Stock : Nil

Analyst (s) Certification:

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