

NOVEMBER 20, 2019

IPO Note

**CSB BANK LTD****NOT RATED****Background**

CSB Bank is one of the oldest private sector banks in India with a history of over 98 years and has a strong base in Kerala along with significant presence in Tamil Nadu, Karnataka, and Maharashtra. It offers a wide range of products and services to its overall customer base of 1.3 million as on September 30, 2019, with particular focus on SME, Retail, and NRI customers. It delivers its products and services through multiple channels, including 412 branches (excluding three service branches and three asset recovery branches) and 290 ATMs spread across 16 states and four union territories as on September 30, 2019, and various alternate channels such as micro ATMs, debit cards, internet banking, mobile banking, point of sale services and UPI.

It has four principal business areas, namely, (a) SME banking, (b) retail banking, (c) wholesale banking, and (d) treasury operations.

Under its SME banking business, it caters to financial institutions, agriculture and allied businesses, and vendors and dealers of corporates. Under its retail banking business, it offers a wide range of loan and deposit products to its retail and NRI customers. Under its wholesale banking business, it caters to large and mid-size corporates and other business entities (with credit requirement of Rs. 250 million and above). As a percentage of its total gross advances, loans to SME customers, retail loans (including gold loans) and wholesale banking advances accounted for 29.47%, 46.23% and 24.30% as on September 30, 2019, respectively. Its treasury operations primarily consist of statutory reserves management, asset liability management, liquidity management, investment and trading of securities, and money market and foreign exchange activities.

**Details of Offer**

Particulars	Details
Price band (Rs/share)	193-195
Opening date of the Issue	22nd November, 2019
Closing date of the issue	26th November, 2019
No. of shares pre-issue (nos. mn)	172
No. of shares post-issue (nos. mn)*	173
Fresh Issue (nos. mn)*	1.23
Offer for sale (nos. mn)	19.78
Issue size (Rs bn)*	4.1
Bid Lot	75 Equity share & multiple of 75 Equity share thereafter
<b>Book Building</b>	
QIBs	75%
Non-Institutional	15%
Retail	10%
Lead managers	Axis Capital, IIFL Securities
Registrar to the issue	Link Intime

Source: Company RHP, \* Based on upper price band

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### Shareholding pattern

	Pre issue	Post issue
Promoter holding (%)	50.1	49.7
Public shareholding (%)	49.9	50.3
Total (%)	100	100

Source: Company RHP

### Objects of the offer

	Utilization of proceeds (Rs Mn)
Augment Bank's Tire-I capital base	N.A
Ensure compliance with Basel III and other RBI guidelines	N.A

Source: Company RHP

### Management Background

Name	Age	Designation	Background
Rajendran Chinna Veerappan	64	Managing Director and Chief Executive Officer	He holds a bachelor's degree and a master's degree in commerce from Madurai Kamaraj University and is an associate of the Indian Institute of Bankers. He previously served as the chief executive of the Association of Mutual Funds in India and is currently responsible for overall management and expansion of our Bank. He has over 40 years of experience in banking and finance sector and was previously associated with Corporation Bank, Andhra Bank and Bank of Maharashtra. He has been on Board since November 24, 2016.
Madhavan Karunakaran Menon	64	Part – time Chairman and Non–executive Director	He holds a bachelor's degree and a master's degree in business administration from the George Washington University. He is also qualified for the award of "Indian School Certificate" in division two issued by the University of Cambridge. He has over 30 years of experience in the finance and banking sector. He has previously worked with ANZ Grindlays Bank Limited, Citibank N.A., Emirates Bank International, Birla Capital International AMC Limited in the past. He is currently on the chairman and managing director of Thomas Cook (India) Limited and has been on Board since September 3, 2018.
Sumit Maheshwari	50	Non – executive Director	He holds a bachelor's and a master's degree in commerce from the University of Mumbai. He is a certified associate member of the Institute of Chartered Accountants of India. He has completed the post graduate programme in management from the Indian School of Business. He has over 10 years of experience in finance sector. Previously, he has worked with KPMG and is currently the managing director and chief executive officer of Fairbridge Capital Private Limited. He has been on Board since September 3, 2018.

Source: Company RHP

## Strengths

### **Strong channel network and trusted brand in South India**

Bank provides its products and services primarily through an extensive physical network of branches and ATMs. It operates in 16 States and four Union Territories in India, reaching 1.3 million customers through 412 branches (excluding three service branches and three asset recovery branches) and 290 ATMs, as on September 30, 2019. In addition to its physical network, it has made investments in development of alternate channels from time to time. Its alternate channel network comprises of ATM debit cards, internet banking, mobile banking, point of sales ("POS"), QR payments, UPI, 24\*7 phone banking, ePassbook, micro ATMs, prepaid (co-branded) cards, and payment gateway services through tie ups. Its deposit renewal rate was 97.86% as on September 30, 2019.

### **Strong capital base for growth**

Bank's capital position has been significantly strengthened post FIHMs investment in the bank. As per the Basel III Norms, the CRAR, as assessed by the Bank as on March 31, 2019 and September 30, 2019, was 16.70% and 22.77% (including capital conservation buffer), respectively. This is above the minimum prescribed CRAR of 10.875% (including capital conservation buffer of 1.875%) stipulated by the RBI in the Basel III Norms. Capital augmentation post infusion of funds by FIHM helped vitalize the Bank's growth engine. As on September 30, 2019, Tier 1 CRAR (including capital conservation buffer) and common equity Tier 1 CRAR (including capital conservation buffer) stood at 22.11% and 22.11%, respectively, well above the minimum prescribed requirements of 7% and 5.5%, respectively, which would enable the long term growth.

### **Well established SME business**

Bank focuses on meeting the funding and banking requirements of its SME customers. As a percentage of its total advances, loans to SME customers accounted for 43%, 37%, 32% and 29.47% as on March 31, 2017, March 31, 2018, March 31, 2019 and September 30, 2019, respectively. It believes that lending to SMEs enables it to diversify the credit risk profile due to relatively smaller individual exposures. As on March 31, 2019 and September 30, 2019, its advances to SME customers aggregated to Rs. 34,733 million and Rs. 33,605 million, respectively, spread across 7,529 accounts and 7,534 accounts, respectively, implying an average ticket size of approximately Rs. 4.61 million and Rs. 4.46 million, respectively.

### **Retail offering driven by strong gold loan portfolio**

Gold loans constituted a major portion of the bank's advances, contributing 24%, 26%, 31% and 33.17% of its total advances as on March 31, 2017, March 31, 2018, March 31, 2019, and September 30, 2019, respectively. As on March 31, 2019 and September 30, 2019, bank had 522,248 and 595,121 gold loan accounts, with advances aggregating to Rs. 33,331 million and Rs. 37,818 million, implying an average ticket size of approximately Rs. 0.06 million and Rs. 0.06 million, respectively. It has a dedicated team within its retail banking business to focus on the gold loan product offerings and have established internal processes towards origination, valuation of gold being pledged as security, and subsequent monitoring and collection from customers towards loan repayment, including timely disposal of pledged gold to realize the receivables in the event of default.

### **Professional and experienced management with strong and independent Board.**

Key Managerial Personnel bring substantial experience and in-depth knowledge of banking operations and management. While some of the Key Managerial Personnel have been with the Bank for more than 35 years, it has also brought in other experienced professionals from the banking industry. Bank believes that the management's capabilities, strong reputation, extensive network of industry relationships, and wide-ranging experience in the finance and banking industry will continue to help them grow, modernize, and develop further.

### **Streamlined risk management controls, policies and procedures**

Bank has instituted prudent risk management controls, policies, and procedures that are critical for the long-term sustainable development of the business. It has implemented risk management procedures for its credit exposures, including credit evaluation, credit scoring, risk-based pricing models and risk monitoring and control mechanisms. It has also developed its own credit risk rating framework in terms of which all exposures of Rs. 2.5 million and above are brought within a rating mechanism. It periodically conducts audits/inspections to ensure that the risks on its portfolios are within acceptable parameters.

## **Strategies**

### **Accelerate transformation as new age private bank.**

It has designed a new organizational set up which it believes makes it more capable of attaining the long-term targets for the business growth and successfully evolve into a new age private sector bank. In the past, its organizational set-up was branch centric, wherein its branches were main drivers of its business, taking care of everything from deposits to lending and customer servicing. This typically had inherent conflict of interest as origination and sanction of loans were with the same branch and branch head. Pursuant to its new organizational set-up and infusion of capital by FIHM, which has given it a strong balance sheet to focus on growth, it will continue to recruit, retain, motivate, and develop talented and experienced professionals, and introduce variable pay, including employee stock option plans, to align compensation with employee performance.

### **Grow its asset business with focus on SME, agricultural and retail customers by leveraging its capital position.**

Bank has established a specialized SME team to strengthen its marketing in order to source additional SME business and drive further penetration. As of September 30, 2019, out of the total 388 SME cluster areas spread across India, as identified by UNIDO, it has presence in 166 such clusters and it intends to expand its SME business in the remaining clusters. It has also established a separate vertical for its agriculture based business to provide a variety of agriculture based banking products. In order to further grow its retail loan portfolio and diversify its loan portfolio mix, it intends to mainly focus on gold loans, two wheeler loans, loans against property, and personal loans.

### **Continue to leverage strong deposits franchise**

The share of CASA deposits in banks total deposits increased from 24.78% in Fiscal 2017 to 27.84% in Fiscal 2019. Further, the share of CASA deposits in its total deposits was 28.19% for the six month period ended September 30, 2019. To improve its wholesale deposit base, it intends to leverage its relationships

with various institutions like educational institutions, temple trusts, and churches. It also intends to leverage its corporate and SME relationships by cross selling salary accounts for employees. It intends to continue to focus on increasing its NRI deposit base, which has been one of its key growth engines on the deposits side and has also proved to be a stable source of funding for the Bank.

**Maximizing non-interest income by widening products and services for corporates as well as retail customers.**

Besides banks focus on increasing interest income, it also intends to focus on increasing its non-interest income from various conventional and non-conventional sources. Its fee and non-fund based revenues constituted 4.37%, 6.01%, 6.12% and 5.57% of its total revenue for Fiscals 2017, 2018, 2019, and for the six month period ended September 30, 2019, respectively. In order to grow its non-interest income, it distributes third-party investment products, such as life insurance and general insurance products.

**Strengthening risk management**

Bank believes that effective risk management is essential for its growth, strategic planning, and long-term sustainable development. It plans to continuously focus on strengthening its risk management and internal control capabilities by improving its policies and procedures and introducing advanced risk management tools. It has also implemented some of the recommendations provided in Fiscal 2016 by CRISIL Risk Solutions, a division of CRISIL Risk and Infrastructure Solutions Limited, to revamp its credit framework.

**Focus on NPA recovery and improve asset quality.**

Bank intends to establish separate teams for retail, SME, and corporate segments dedicated towards recovery of provisioned portfolio and also managing and monitoring of ongoing stressed portfolios. Its gross NPAs decreased to 4.87% as of March 31, 2019 from 7.25% as of March 31, 2017. Further, its gross NPAs was 2.86% as on September 30, 2019. The net NPAs decreased to 2.27% as of March 31, 2019 from 4.12% as of March 31, 2017. Further, its net NPAs was 1.96% as on September 30, 2019, while its provisioning coverage ratio was 65.50%, 75.83%, 78.16% and 79.45% in respect of NPAs (including technical write-offs) as of March 31, 2017, March 31, 2018, March 31, 2019, and September 30, 2019, respectively.

## Financials

### Balance sheet (Rs mn)

Rs. mn	2017	2018	2019	H1FY20
<b>ASSETS</b>				
Cash in Hand	506	549	584	549
Balance with RBI	7,058	6,229	6,670	6,513
Balance with Banks	768	463	232	1,099
Money at Call & Short Notice	3,780	4,910	2,250	-
Investments	57,292	40,833	40,276	43,141
Advances	80,008	91,849	106,152	112,978
Net Fixed Assets	513	567	599	585
Other Assets	9,712	10,583	10,770	11,118
Less : Intangible Assets and Deferred Tax Asset	1,936	2,635	2,999	2,751
Other Assets	7,776	7,947	7,771	8,367
<b>TOTAL (A)</b>	<b>157,700</b>	<b>153,347</b>	<b>164,535</b>	<b>173,233</b>
<b>LIABILITIES</b>				
<b>DEPOSITS</b>				
Demand Deposit	6,078	6,281	6,171	6,594
Saving Deposits	30,868	33,425	35,935	37,125
Term Deposits from Banks	183	59	1,901	1,830
Term Deposits from others	111,986	107,141	107,232	109,549
Borrowings	418	418	-	-
Other Liabilities & Provisions	2,705	2,486	3,556	2,774
<b>TOTAL (B)</b>	<b>152,239</b>	<b>149,810</b>	<b>154,795</b>	<b>157,873</b>
<b>NET WORTH (A-B)</b>	<b>5,461</b>	<b>3,536</b>	<b>9,740</b>	<b>15,360</b>
<b>Share Capital</b>				
Equity Share Capital	810	810	860	1,723
Share Warrant	0	0	6,513	0
<b>TOTAL (D)</b>	<b>810</b>	<b>810</b>	<b>7,373</b>	<b>1,723</b>
<b>RESERVE &amp; SURPLUS</b>				
Statutory Reserve	1,468	1,468	1,468	1,468
Capital Reserve	717	717	717	720
Revaluation Reserve	1,640	1,595	1,578	1,571
Share Premium	6,475	6,475	7,120	17,689
Revenue & Other Reserve	1,139	1,184	1,201	1,208
<b>TOTAL</b>	<b>11,439</b>	<b>11,439</b>	<b>12,083</b>	<b>22,656</b>
Less : Revaluation Reserve	1,640	1,595	1,578	1,571
Less : Intangible Assets and Deferred Tax Asset	1,936	2,635	2,999	2,751
Less: Profit & Loss (Dr.)	3,212	4,483	5,140	4,697
<b>TOTAL (E)</b>	<b>4,651</b>	<b>2,726</b>	<b>2,367</b>	<b>13,637</b>
<b>NET WORTH (D+E)</b>	<b>5,461</b>	<b>3,536</b>	<b>9,740</b>	<b>15,360</b>

Source: Company RHP

**Profit and Loss (Rs mn)**

Rs. mn	2017	2018	2019	H1FY20
<b>Interest Earned</b>	<b>13,363</b>	<b>12,968</b>	<b>13,475</b>	<b>7,323</b>
Interest & Discount on advance/bills	8,809	9,128	9,686	5,631
Income on Investment	4,126	3,362	3,474	1,534
Interest - Others	429	478	315	158
<b>OTHER INCOME</b>	<b>2,812</b>	<b>1,254</b>	<b>1,359</b>	<b>844</b>
Commission, Exchange & Brokerage	205	234	272	137
Profit on sale of Investments(Net)	1,959	27	80	130
Others	648	993	1,007	577
<b>Total Income</b>	<b>16,175</b>	<b>14,222</b>	<b>14,834</b>	<b>8,167</b>
<b>EXPENDITURE</b>				
<b>Interest Expended</b>	<b>10,227</b>	<b>9,120</b>	<b>9,076</b>	<b>4,528</b>
Interest on Deposits	10,041	8,973	8,618	4,483
Others	185	147	457	45
<b>Operating Expenses</b>	<b>4,431</b>	<b>4,359</b>	<b>5,625</b>	<b>2,604</b>
Payment to & provision for employees	2,936	2,869	3,844	1,681
Rent, Tax & Lighting	415	459	506	278
Depreciation on Banks Properties /Assets	149	156	165	100
Other Expenditure	931	875	1,110	544
<b>Total Expense</b>	<b>14,658</b>	<b>13,479</b>	<b>14,701</b>	<b>7,131</b>
<b>Operating Profit (before Extra Ordinary Items and Provision &amp; Contingencies)</b>				
	<b>1,517</b>	<b>743</b>	<b>134</b>	<b>1,036</b>
Less : Provisions and contingencies	2,522	2,692	1,110	346
<b>PBT</b>	<b>-1,004</b>	<b>-1,949</b>	<b>-976</b>	<b>689</b>
Provision for tax	-425	-678	-319	247
<b>PAT</b>	<b>-580</b>	<b>-1,271</b>	<b>-657</b>	<b>443</b>

Source: Company RHP

**Cash Flow statement (Rs mn)**

Rs. mn	2017	2018	2019	H1FY20
<b>Cash and cash equivalent at the beginning of the year</b>	<b>7,263</b>	<b>12,112</b>	<b>12,151</b>	<b>9,736</b>
Net cash from operating activity	3,954	268	-8,932	-6,410
Net cash from investing activity	-170	-178	-221	-84
Net cash from financing activity	1,064	-51	6,739	4,919
Net inc/(dec) in cash and cash equivalents	4,849	40	-2,415	-1,575
<b>Cash and cash equivalent at the end of the year</b>	<b>12,112</b>	<b>12,151</b>	<b>9,736</b>	<b>8,161</b>

Source: Company RHP

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<b>ADD</b>	–	We expect the stock to deliver 5% - 15% returns over the next 12 months
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<b>SELL</b>	–	We expect the stock to deliver < -5% returns over the next 12 months
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