

Company Overview

Incorporated in 1999, Capital Small Finance Bank Ltd. (Capital SFB) received a license to operate as a small finance bank in 2016 before operating as a local area bank since its inception. The SFB offers a range of banking products on the asset and liability side. With an experience of over two decades in the banking industry, the SFB's strategy is to strengthen the retail-focused banking franchise by enabling access to affordable credit to middle-income group segments with special emphasis on rural and semi-urban areas. Capital SFB's business model primarily focuses on the middle-income customer segments i.e., customers with an average annual income of Rs. 0.4 million to Rs. 5 million in semi-urban and rural areas. The company has 41.6% of its branches in rural areas, 34.68% branches in semi-urban areas, and 23.70% of its branches in urban areas as on September 30, 2023. The SFB operates in states like Punjab, Haryana, Delhi, Rajasthan, Himachal Pradesh, and the Union Territory of Chandigarh where it offers products consisting of agriculture loans, MSME, and trading loans (working capital, machinery loans etc.) and mortgages (housing loans and loans against property). As on September 30, 2023, Capital SFB was present in five states and one Union Territory with 173 branches and 175 ATMs. Over the years, the bank has diversified its portfolio with a sizeable book in multiple asset classes with a proportion of secured lending at 99.85% as on September 30, 2023. Additionally, the lender generates fee income from products and services such as forex and money transfer, outward remittances, safe deposit lockers, distribution of life insurance and general insurance products, 3-in-1 demat and trading accounts, and other ancillary services. While most of the SFBs are pure MFI turned SFB and have huge concentration in MFI products, Capital SFB has about 19.7% of portfolio concentration towards MSME, agriculture accounts for 38.7% and mortgages accounts for 26.1% of the portfolio.

Objects of the issue

The offer comprises fresh issue and offer for sale. The net proceeds from the fresh issue will be used towards the following purposes:

- ⇒ Towards augmenting the bank's Tier-I capital base to meet the bank's future capital requirements; and
- ⇒ General corporate purposes.

Investment Rationale

Impressive business with retail focused liability alongside secured and diversified advances portfolio

With over 16 years of experience in operating as a local area bank, Capital SFB has deep understanding of growing its deposit base. This has helped the SFB to create a retail-centric deposit franchise with a high share of CASA deposits, with the CASA ratio increasing from 40.1% in FY21 to 41.9% in FY23. The lender offers a comprehensive suite of products of savings bank deposits, current deposits, term deposits, NRE and NRO deposits, and tax saver deposits to cater to the diverse needs of its customers. Due to high retail deposits, the bank has significant advantages including stability in deposits, greater customer retention, and enhanced cross-selling opportunities in addition to supporting the low cost of funds. Coming onto the Capital SFB's advances portfolio, it has consciously focused on building a secured and granular loan book over the years with a focus on income generation. As on March 31, 2023, and September 30, 2023, 99.82% and 99.85% of its loan books were secured. It has a well-diversified portfolio across agriculture, MSME and trading, mortgage lending, and other products which helps to mitigate risk and optimize resources. As on September 30, 2023, the average ticket size of agriculture, MSME & trading, and mortgage lending products stood at Rs. 1.24 million, Rs. 1.81 million and Rs. 1.15 million, respectively. Further, a well-diversified loan portfolio with a focus on income generation, continued focus on secured lending, continuous customer engagement, and structured underwriting practices has contributed to the lender's growth and superior asset quality as compared to other SFBs.

Streamlined credit assessment processes with customer centric approach

Capital SFB's strategy of secured lending, primarily for productive purposes and conservative loan-to-value ratio, contributes towards lower delinquencies and credit losses. The lender's positioning as the primary banker to most of its customers enables it to have a comprehensive view and control over cash flows, thereby contributing towards effective credit assessment. Further, its dedicated customer relationship team maintains healthy engagement with customers on an ongoing basis which has resulted in effective collection recoveries and consequently better asset quality. Through its

Issue Details

Offer Period	07 th Feb, 2024 - 09 th Feb, 2024
Price Band	Rs. 445 to Rs. 468
Bid Lot	32
Listing	BSE & NSE
Issue Size (no. of shares in mn)	11.2
Issue Size (Rs. in bn)	5.2
Face Value (Rs.)	10

Issue Structure

QIB	50%
NIB	15%
Retail	35%

BRLM	Nuvama Wealth, DAM Capital Advisors, Equirus Capital
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Registrar	Link Intime India Private Ltd.
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Particulars	Pre Issue %	Post Issue %
Promoter	22.39%	17.61%
Promoter Group	1.57%	1.24%
Public - Other S/S	14.21%	8.94%
Public - Others	61.83%	72.21%
Total	100.00	100.00

(Assuming issue subscribed at higher band)

Research Team - 022-61596138

Capital Small Finance Bank Ltd.

understanding of the market and customer base, the SFB offers a range of credit and non-credit products and services to address a variety of financing requirements of customers through its branch network. Capital SFB is a one-stop financial hub for its customers with 7,25,037 customers as on September 30, 2023. The bank targets customers across sectors with special attention to rural and semi-urban centers as borrowers in these regions tend to have lower credit penetration which helps the lender with less competition, and a lower risk of customer migration (leading to longer, more loyal customer relationships), better credit behaviours and, in turn, lower delinquency rates.

Valuation and Outlook

With small finance banks and payments bank increasing their reach and expanding into rural areas and increasing financial awareness, faster growth in rural areas can be expected in future due to the huge untapped potential. Given the stronghold and experience of these entities in dealing with customers across these regions, the share of SFBs will go up against the public and private sector banks. The sector's loan portfolio is expected to see a strong growth of around 22-24% CAGR during FY2023-25 period as most of the SFBs have completed the transition phase and are likely to benefit from the operating leverage. Capital SFB already had its presence across the retail liability and asset side on account of operating as a local area bank before converting to a small finance bank. As a result, its retail franchise and reach has already been established across current and savings deposits as well as retail term deposits, thereby placing it in a good stead against other small finance banks. In comparison to other SFBs which are primarily focused on MFI lending and find it more difficult to penetrate into other products, Capital SFB has products, systems and processes in place to scale up operations across different products and geographies. Furthermore, Capital SFB has a CASA ratio which is similar to some of the leading private sector banks like HDFC Bank, Axis Bank, and ICICI Bank. Moreover, the lender's gross NPA of 2.73% and net NPA of 1.36% as on September 30, 2023 acts as a testament to its streamlined underwriting processes, credit assessment, efficient collections, and risk management. It is important to note that the lender's PPOP has grown from Rs. 714.86 million in FY21 to Rs. 1,487.04 million in FY23 and stood at Rs. 753.84 million as of six months ended September 30, 2023. **As the lender will utilize net proceeds of the fresh equity issue to augment its Tier-I capital base, its capital adequacy will enhance and lead to a stable leverage position. At the current P/BV multiple of 2.3x based on book value as on September 2023, we believe the company is reasonably valued and advise investors to "Subscribe" to the issue from a medium to long-term perspective.**

Key Risks

- ⇒ Capital SFB's business is concentrated in North India, with approximately 86.1% of the total branches located in Punjab as of September 30, 2023. Any adverse change in the economy of North India could have an adverse effect on its financial condition, results of operations, and cash flows.
- ⇒ Any downgrade in its credit rating could increase the borrowing costs, affect the ability to obtain financing, and adversely affect its business, results of operations, and financial condition.
- ⇒ The lender may be impacted by volatility in interest rates which could cause its Net Interest Margin to decline and adversely affect the results of operations and cash flows.



Capital Small Finance Bank Ltd.

Income Statement (Rs. in millions)

Particulars	FY21	FY22	FY23	H1FY24
INCOME				
Interest Earned	5,114	5,782	6,760	3,860
Other Income	458	542	495	292
Total	5,573	6,324	7,255	4,152
EXPENDITURE				
Interest Expended	3,128	3,229	3,540	2,150
Operating Expenses	1,730	1,963	2,228	1,248
Provisions and Contingencies	307	506	551	210
Total	5,165	5,698	6,319	3,608
PROFIT				
Net profit for the period	408	626	936	544
Profit brought forward	988	1,263	1,670	2,332
Total	1,396	1,889	2,606	2,876
APPROPRIATIONS				
Transfer to Statutory Reserves	102	156	234	0
Transfer to Special Reserve	7	18	35	0
Transfer (from)/to Investment Reserve Account	0	0	-8	0
Transfer (from)/to Investment Fluctuation Reserve	24	17	-21	0
Dividend	0	27	34	42
Balance carried over to Balance sheet	1,263	1,670	2,332	2,833
Total	1,396	1,889	2,606	2,876
EARNING PER SHARE				
Basic (Rs.)	347	224	680	729
Diluted (Rs.)	12.04	18.41	27.35	15.59
	11.98	18.22	27.21	15.49

Source: RHP, BP Equities Research

Cash Flow Statement (Rs. in millions)

Particulars	FY21	FY22	FY23	H1FY24
Cash Flow from operating activities	1743	(2,107)	(1,074)	1,885
Cash flow from investing activities	(124)	(132)	(197)	(67)
Cash flow from financing activities	1,968	(1,197)	2,215	1,031
Net increase/(decrease) in cash and cash equivalents	3,587	(3,436)	944	786
Cash and cash equivalents at the beginning of the period	3,824	7,411	3,975	4,919
Cash and cash equivalents at the end of the period	7,411	3,975	4,919	5,706

Source: RHP, BP Equities Research



Capital Small Finance Bank Ltd.

Balance Sheet (Rs. in millions)

Particulars	FY21	FY22	FY23	H1FY24
CAPITAL & LIABILITIES				
Capital	339	340	343	354
Reserve and Surplus	4,169	4,817	5,764	6,764
Deposits	52,211	60,464	65,606	70,003
Borrowings	6,167	4,984	7,214	5,728
Other Liabilities and provisions	827	934	982	1,059
Total	63,712	71,539	79,908	83,907
ASSETS				
Cash and Balances with Reserve Bank of India	7,217	3,640	4,627	5,025
Balances With banks and Money at call and Short Notice	5,687	6,551	4,182	3,501
Investments	12,123	13,571	14,886	15,495
Advances	37,269	46,348	54,287	57,842
Fixed assets	866	836	826	808
Other Assets	551	594	1,101	1,237
Total	63,712	71,539	79,908	83,907
Contingent Liabilities	384	456	565	529
Bills for Collection	0	0	0	0

Source: RHP, BP Equities Research

**Disclaimer Appendix****Analyst (s) holding in the Stock : Nil****Analyst (s) Certification:**

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