



**LONG TERM SUBSCRIBE**

**IPO Report**

02<sup>nd</sup> Nov' 23

**Snapshot**

ESAF Small Finance Bank is a small finance bank with a focus on unbanked and under-banked customer segments, especially in rural and semiurban centres. As at June 30, 2023, company's gross advances to its customers in rural and semi-urban centres (combined) accounted for 62.97% of company's gross advances and 71.71% of company's banking outlets were located in rural and semi-urban centres (combined). Company's primary products are its advances (asset products) and deposits (liability products). Company's advances comprise: (a) Micro Loans, which comprises Microfinance Loans and Other Micro Loans; (b) retail loans, which includes gold loans, mortgages, personal loans, and vehicle loans; (c) MSME loans; (d) loans to financial institutions; and (e) agricultural loans.

**VALUATION**

Company is bringing the issue at price band of Rs 57-60 per share at p/b multiple of 1.4x on FY23 basis.

Company's understanding of the micro loan segment, has enabled it to grow its business outside of Kerala, company's home state. Company's main focus on rural and semi-urban banking franchise along with growing retail deposits portfolio & customer connections driven by its customer-centric products and processes and other non-financial services for Micro Loan customers.

Looking after all above, we recommend "Long Term Subscribe" on issue.

<b>Price Band (Rs./Share)</b>	<b>57-60</b>
<b>Opening date of the issue</b>	<b>03<sup>rd</sup> Nov'2023</b>
<b>Closing Date of the issue</b>	<b>07<sup>th</sup> Nov'2022</b>
<b>No of shares pre issue</b>	449,473,798 Eq Shares
<b>Issue Size</b>	Rs 463 Cr
<b>Offer For Sale</b>	Rs 72.30 Cr
<b>Face Value (Rs/ share)</b>	Rs 10/share
<b>Bid Lot</b>	250

**BIDDING DETAILS**

<b>QIBs (Including Anchor)</b>	50% of the offer (Approx 37,541,665 Eq Shares)
<b>Non-Institutional</b>	15% of the offer ( Approx 11,262,500 Eq Shares)
<b>Retail</b>	35 % of the offer ( Approx 26279167 Eq Shares)
<b>Employee Reservation</b>	2272727 Eq Shares
<b>Lead managers</b>	ICICI Securities, DAM Capital, Nuvama Wealth Management
<b>Registrar to the issue</b>	Link Intime India Pvt. Ltd

**WHAT WE LIKE**

**Growing Retail Deposits portfolio**

Company's total deposits increased from ₹89,994.26 million as at March 31 2021 to ₹146,656.25 million as at March 31, 2023, representing a CAGR of 27.66%, and further increased to ₹156,558.54 million as at June 30, 2023, an increase of 6.75%. Company's Retail Deposits increased from ₹87,963.84 million as at March 31, 2021 to ₹133,230.03 million as at March 31, 2023, representing a CAGR of 23.07%, and further increased to ₹139,772.67 million as at June 30, 2023, an increase of 4.91%. Company's CASA increased from ₹17,476.45 million as at March 31, 2021 to ₹31,374.47 million as at March 31, 2023, representing a CAGR of 33.99%, and decreased to ₹28,519.70 million as at June 30, 2023, a decrease of 9.10%

**Main focus on rural and semi-urban banking franchise**

Company's main focus is on providing loans to customers in rural and semi-urban centres. Company's customers in rural and semi-urban centres (combined) have increased from 3.00 million as at March 31, 2021 to 3.93 million as at March 31, 2023 and further increased to 4.07 million as at June 30, 2023. As at June 30, 2023, company's gross advances to customers in rural and semi-urban centres (combined) were ₹90,951.76 million, representing 62.97% of company's gross advances. As at June 30, 2023, 4.07 million of company's customers were in rural and semi-urban centres (combined), representing 56.92% of its total customers, and the number of banking outlets in rural and semi-urban centres (combined) was 502, representing 71.71% of company's total banking outlets

**Experienced Board and Key Managerial Personnel and Senior Management Personnel**

Mr. Kadambelil Paul Thomas, company's Managing Director and Chief Executive Officer and one of its Promoters, was previously a senior field representative at Indian Farmers Fertilizers Cooperative Limited and since 2013 he has been the president of the Kerala Association of Micro Institutional Entrepreneurs. Members of company's Senior Management Personnel and Key Managerial Personnel have been working in the banking and financial services sector for more than 27 years.



## COMPANY BACKGROUND

Company have a network of 700 banking outlets (including 59 business correspondent-operated banking outlets), 767 customer service centres (which are operated by company's business correspondents), 22 business correspondents, 2,116 banking agents, 525 business facilitators and 559 ATMs spread across 21 states and two union territories, serving 7.15 million customers as at June 30, 2023. While company's operations are spread out across India, company's business is concentrated in South India, particularly in the states of Kerala and Tamil Nadu. As at June 30, 2023, 62.43% of company's are from customers in South India (including 43.45% from Kerala and 22.14% from Tamil Nadu) and 86.90% of company's deposits are from banking outlets in South India (including 80.04% from Kerala and 3.36% from Tamil Nadu). Company commenced its business as a small finance bank on March 10, 2017 and company was included in the second schedule to the RBI Act pursuant to a notification dated November 12, 2018 issued by the RBI. Bank does not have any subsidiaries, associates or joint ventures or a holding company. Kadambelil Paul Thomas, its Managing Director and Chief Executive Officer and one of company's promoters, along with others, founded ESAF Foundation, a foundation focused on the development of microenterprises, community development, and community health development. ESAF Foundation is governed by the society registrar under the Travancore-Cochin Literary, Scientific and Charitable Societies Registration Act, 1955.

Company follow a social business strategy seeking a triple bottom line impact: people; planet; and prosperity. The social, environmental, and economic outcomes of company's business create synergies that have an amplified impact on company's stakeholders. The legacy of a mission, fighting the partiality of prosperity (i.e., the drive for inclusion of marginalised sections of society and the equity of opportunities) led to the formation of Bank. Company's vision is to be India's leading social bank that offers equal opportunities through universal financial access and inclusion and livelihood and economic development. Company have adopted various policies to implement company triple bottom line approach, including an Environmental, Social and Governance ("ESG") policy. Pursuant to the ESG policy, company is committed to (i) the protection of the environment and ensuring sustainable development, (ii) promoting financial inclusion and gender equality through specialised financial services; and (iii) establishing a governance framework to ensure accountability, transparency and compliance with internal and external ESG standards. In 2020 company won the "Global Sustainability Award 2020" for outstanding achievements in sustainability management by the Energy and Environment Foundation. Company's ESG Grading scores from CARE Advisory Research & Training Limited in its report titled "ESG Grading Report of ESAF Small Finance Bank" published in June 2023 were: (i) 62% for the Environmental pillar, with remarks including company's commitment to green finance and environment conscious operations; (ii) 68% for the Social pillar, with remarks including that company have demonstrated healthy labour management practices, including the implementation of various policies that embody international and national human rights standards; and (iii) 76% for the Governance pillar, with remarks including that company have aligned with leading governance practices, such as adequate independence of company's Board (66% independent members on the Board) and committee levels. Company received a rating of CareEdge ESG 3 (good), with an overall score of 71 compared with the industry average overall score of 59.8. CARE Advisory Research & Training Limited's ESG specialist team undertook the ESG Grading of company's Bank during May 2023.

Company focus on leveraging technology to deliver products and services and company continuously work towards improving its customers' experience through the use of technology. Company have crossed a technology milestone with the successful adoption of e-signatures for Micro Loan disbursals. In Fiscal 2023, company disbursed over 0.53 million loans using e-signatures. Company offer its customers various digital platforms, including an internet banking portal, a mobile banking platform, SMS alerts, bill payments and RuPay branded ATM cum debit cards. Company's customers are also able to register for its savings accounts on a unified payment interface based mobile applications. Company's account opening and loan underwriting processes have been digitalised by using tablets. Company have a digitalised central credit-processing unit for its Micro Loans. Company's customer on-boarding process has been predominantly digitalised for its Micro Loans. Company leverage technology for underwriting and credit sanctioning for its loan products based on inputs from credit bureaus and/or its customer data analytics. Company have implemented technology solutions that enable it to ensure cashless disbursement of loans and implemented electronic signing for Micro Loans, both of which have reduced paperwork. Company's collections mechanism has also been digitalised through the use of mobile applications and a payment gateway through which company's borrowers can repay their loans. Company have also implemented a customer relationship management solution to better handle customer requests.



## INVESTMENT RATIONALE

<b><i>Company's understanding of the micro loan segment has enabled it to grow its business outside of Kerala, company's home state</i></b>	Company can trace its microfinance roots back to 1995. As at June 30, 2023, company had over 3.25 million customers with Micro Loans, the majority of whom were women. Company's understanding of the micro loan segment has enabled it to successfully expand its business outside of Kerala. As at June 30, 2023, company's products and services were offered in 21 states and two union territories. Company's gross Micro Loans to customers outside of Kerala were ₹43,305.24 million, representing 42.30% of company's total gross Micro Loans, as at June 30, 2023. As at June 30, 2023, company's top five states outside Kerala for gross Micro Loans were Tamil Nadu, Maharashtra, Madhya Pradesh, Karnataka and Chhattisgarh, with gross Micro Loans in those states (combined) being ₹50,437.31 million, which represented 49.27% of company's total gross Micro Loans.
<b><i>Main focus on company's rural and semi-urban banking franchise</i></b>	Company's main focus is on providing loans to customers in rural and semi-urban centres. Company's customers in rural and semi-urban centres (combined) have increased from 3.00 million as at March 31, 2021 to 3.93 million as at March 31, 2023 and further increased to 4.07 million as at June 30, 2023. As at June 30, 2023, company's gross advances to customers in rural and semi-urban centres (combined) were ₹90,951.76 million, representing 62.97% of company's gross advances. As at June 30, 2023, 4.07 million of its customers were in rural and semi-urban centres (combined), representing 56.92% of company's total customers, and the number of banking outlets in rural and semi-urban centres (combined) was 502, representing 71.71% of company's total banking outlets.
<b><i>Growing Retail Deposits portfolio</i></b>	Company's total deposits increased from ₹89,994.26 million as at March 31 2021 to ₹146,656.25 million as at March 31, 2023, representing a CAGR of 27.66%, and further increased to ₹156,558.54 million as at June 30, 2023, an increase of 6.75%. Company have placed an emphasis on increasing its Retail Deposits. Company's Retail Deposits increased from ₹87,963.84 million as at March 31, 2021 to ₹133,230.03 million as at March 31, 2023, representing a CAGR of 23.07%, and further increased to ₹139,772.67 million as at June 30, 2023, an increase of 4.91%. CASA tends to provide a stable and low-cost source of deposits compared to term deposits. Company's CASA increased from ₹17,476.45 million as at March 31, 2021 to ₹31,374.47 million as at March 31, 2023, representing a CAGR of 33.99%, and decreased to ₹28,519.70 million as at June 30, 2023, a decrease of 9.10%.
<b><i>Customer connections driven by its customer-centric products and processes and other non-financial services for Micro Loan customers</i></b>	Company aim to provide the best-in-class banking services to company's customers, as company's customers are the most important stakeholders in its business. Company's products and services are designed to meet the various lifecycle needs of its customers, such as home loans, clean energy product loans, loans for agricultural activities, loans against property, personal loans, education loans, gold loans and vehicle loans.
<b><i>Technology-driven model with a digital technology platform</i></b>	Company offer its customers various digital platforms, including an internet banking portal, a mobile banking platform, SMS alerts, bill payments and RuPay branded ATM cum debit cards. All banking and payment transactions, such as remittances and utility payments, can be completed through these platforms. Company's customers are also able to register its savings accounts on a unified payment interface based mobile applications.



## OBJECTS OF OFFER

Each of the Selling Shareholders will be entitled to their respective portion of the proceeds from the Offer for Sale in proportion of the Equity Shares offered by the respective Selling Shareholders as part of the Offer for Sale. Bank will not receive any proceeds from the Offer for Sale

## RISKS

As at June 30, 2023 and March 31, 2023, 2022 and 2021, 74.70%, 75.04%, 81.16% and 84.80%, respectively, of company's advances under management, which is gross advances plus advances originated and transferred under securitization, assignment and inter-bank participation certificates for which co continue to hold collection responsibilities ("Advances Under Management" or "AUM") were Micro Loans. As at June 30, 2023 and March 31, 2023, 56.52% and 63.66%, respectively, of company's AUM were Microfinance Loans and 18.18% and 11.38%, respectively, of company's AUM were Other Micro Loans. Any decrease in demand for its Micro Loans could adversely affect company's business, financial condition, results of operations and cash flows.

## INDUSTRY OVERVIEW

### Small finance banking industry

In order to promote financial inclusion, the Indian banking industry has seen several changes in recent years. NBFCs, such as Bandhan and IDFC, received permission to set up universal banks. Also, a few microfinance companies, a local area banks and an NBFC as well as one urban co-operating bank have received permission to set up small finance banks (SFBs). The RBI awarded SFB licences to 12 players keeping in with the government's focus on financial inclusion and inclusive banking.

### Growth drivers for small finance banks

- **Customized products aided by technology and information availability** Greater use of technology is enabling lenders to provide customised products, that too at much lower turnaround time. Multiple data points are available for lenders that is facilitating quick decision making. In fact, they can take lending decisions within minutes using data-driven automated models. These models would help in supply of credit to small business units and the unorganised sector at low cost. Technology also helps these players expand their reach to under penetrated population in remote centres at a lower operating cost.

- **Availability of funds at cheaper rates** CASA and other retail deposits are a cheap source of funds for SFBs, which help them expand their product portfolio. They can provide lower rates in the market to compete with NBFCs. With SFBs expanding in the underserved regions further, their deposit base is expected to further widen. The CASA deposits for SFBs is estimated to have grown at 66% CAGR from Fiscal 2018 to Fiscal 2023. This will give them an advantage over NBFCs and help expand their asset book.

### Industry growth and outlook

The small finance banks' advances under management (which is gross advances plus off-balance sheet advances ("AUM")) is estimated to have clocked 29% CAGR from March 31, 2018 to June 30, 2023. CRISIL MI&A estimates that the top three SFBs accounted for ~60% of the aggregate AUM as of June 30, 2023, up from 55% as of March 31, 2017 indicating the rising concentration and expansion of players within the SFBs. CRISIL MI&A also estimates that the top six players accounted for ~85% of the market share as of June 30, 2023. In Fiscals 2021 and 2022, new loan origination remained low as SFBs turned cautious and selective in disbursements due to the pandemic. However, as economy revived and business operations normalised, SFBs' AUM witnessed strong growth post pandemic. As of June 30, 2023, SFB AUM is estimated to have crossed ₹1,900 billion. CRISIL MI&A expects SFB's AUM to grow at ~22-24% CAGR between June 30, 2023 and March 31, 2025, as most of the SFBs have completed the transition phase and are likely to benefit from their operating leverage.

### Growth in SFB AUM will be driven by following factors:

- **Huge market opportunity in the rural segment** – Despite its larger contribution to GDP of 47%, the rural segment's share in credit remains fairly low at ~8-9% of the overall credit outstanding as of March 31, 2023. This provides a huge market opportunity for SFBs and other players present in the segment
- **Presence of informal credit channels** – In remote centres, informal credit channels have a major presence. In other words, there is a huge section of unbanked population. SFBs have an opportunity to tap this market
- **Geographic diversification** – With increased focus on diversifying their portfolio and expanding their reach, SFBs are expected to log higher growth as they tap newer geographies
- **Loan recovery and control on aging NPAs** – SFBs are experienced in collection and monitoring of default risk. This will help them keep asset quality under check
- **Ability to manage local stakeholders** – With their microfinance experience, SFBs have the ability to manage local stakeholders and maintain operational efficiency
- **Access to low-cost funds & huge cross sell opportunity**– SFBs' cost of funds is low substantially as they are allowed to raise CASA deposits. This will also help them lend at more reasonable rates to its customers, hence enhancing their cross-sell opportunity in terms of asset products, insurance etc.



Financials (Mn)	FY21	FY22	FY23	Q1FY24
Net Income	10488.39	13547.22	21242.53	6784.82
Total Expenses	6318.55	8628.71	12305.41	3778.13
Pre Provision Profit	4169.84	4918.51	8937.12	3006.69
Provisions	3115.88	4371.19	5913.79	1707.05
PBT	1053.96	547.32	3023.33	1299.64
Tax	0.00	0.00	0.00	0.00
PAT	1053.96	547.32	3023.33	1299.64
Eq Cap	4494.74	4494.74	4494.74	4494.74
Net Worth	13,520.64	14,116.02	17,091.29	18,390.93
EPS	2.46	1.22	6.73	2.89
Book value	30.08	31.41	38.03	40.92
NIM %	8.98	8.64	10.67	3.08
Cost To Income ratio	60.24	63.69	57.93	55.69
ROE%	8.85	4.12	19.36	7.33
ROA%	0.96	0.38	1.63	0.63

(Source: RHP)

## Peer Comparison

Q1FY2024	ROA%	ROE%	NIM %	Yield on Advances %	GNPA%	NNPA%
<b>ESAF Small Finance Bank Limited*</b>	0.6%	7.3%	2.9%	5.8%	1.65%	0.81%
<b>Listed Peers</b>						
AU SFB	0.4%	3.5%	1.4%	3.3%	1.76%	0.55%
Equitas Small Finance Bank Limited	0.5%	3.6%	2.0%	4.3%	2.75%	1.18%
Ujjivan SFB	<b>1.0%</b>	<b>7.5%</b>	2.3%	5.2%	2.62%	0.06%
Jana SFB	<b>0.3%</b>	<b>4.3%</b>	1.8%	4.9%	2.90%	1.20%
Utkarsh SFB	0.6%	5.2%	2.2%	4.9%	3.13%	0.33%
Suryoday SFB	0.5%	3.0%	2.2%	5.1%	3.04%	1.63%

(Source: RHP)



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