

## Company Overview

Five Star Business Finance is an NBFC-ND-SI providing secured business loans to micro-entrepreneurs and self-employed individuals. The company is headquartered in Chennai and has a strong presence in south India comprising of an extensive network of 311 branches, as of June 30, 2022, spread across eight states and one union territory. The ticket size of the loans offered ranges between INR 0.1mn to 1mn with an average ticket size of 0.29mn for June 2022. The company's gross term loans are currently at 52,965mn as of June 2022 which is split into loans for business purposes (62.12% of gross term loans) and loans for asset creation and significant economic events (37.88% of gross term loans). Its targets customers in tier-2 to tier-6 cities who typically derive income from "everyday" cash and carry business with a typical focus on services. The company only provides secured loans where more than 95% of the collateral is a self-occupied residential property. The currently has a loan base of 230,175 customers and continues to increase this number while keeping the average ticket size stable. The company secures financing from various sources including term loans, proceeds from loans securitized, and loans from banks and financial institutions among others. The interest rate ranges from 24% to 26% and between tenure of five to seven years.

## Objects of the issue

The IPO proceeds will be used towards the following purposes:

- ⇒ To carry out Offer for Sale.
- ⇒ Achieve the benefits of listing equity shares in the stock exchanges.

## Investment Rationale

### Robust Customer Evaluation Process

The company has developed a robust customer credit evaluation method which is a four-layered process; two within the business and collections team and two layers within the credit team. It conducts an in-depth analysis of its potential customer by considering the 'three C's' viz Character, Cash-Flow, and Collateral to ensure that the customer has adequate ability to repay the loan amount. Also, sourcing of potential customers is 100% done in-house by the company, not depending on any intermediaries allowing better control over the files. Approximately 80% of the files logged in are sanctioned due to strict pre-login practices followed by the company.

### Under-penetrated market with large opportunities

The credit market for MSMEs and self-employed individuals is largely in the unorganised sector. According to industry reports, less than 15% of approx 70 million MSMEs in India have access to formal credit in any form. The company has calibrated a strategy for contiguous expansion to penetrate the market by enabling its customers to move into the organised credit market while maintaining strong asset quality. The GNPA of the company is approx 1.12% of the gross term loans as of June 2022.

## Valuation and Outlook

The general growth in the organised credit market for MSMEs and robust risk management and collections framework provide Five Star with a huge opportunity to expand further. The company's approach to sanction only fully secured loans with SORP as collateral coupled with a focus on strong pre-login assessment minimizes the risk of frequent defaults. Also low cost of borrowings and significant plans to invest in technology and data analytics to improve operational efficiency help the company in the long run. However, disruptions in the sources of capital and default by borrowers remain key risks. On the upper end of the price band, the issue is valued at a P/E of 29.6x and a P/B of 1.2x based on FY22 earnings which we feel is fairly priced and recommend investors to "SUBSCRIBE" to the IPO for the benefit of listing gains.

## Issue Details

|                                  |   |
|----------------------------------|---|
| Offer Period                     | 9 <sup>th</sup> Nov– 11 <sup>th</sup> Nov, 2022 |
| Price Band                       | INR.450 to INR.474                              |
| Bid Lot                          | 31  |
| Listing                          | BSE&NSE   |
| Issue Size (no. of shares in mn) | 43.56/41.36                                     |
| Issue Size (INR. in bn)          | 19.6  |
| Face Value                       | 1   |

## Issue Structure

|           |  |
|-----------|--|
| QIB       | 50%  |
| NIB       | 15%  |
| Retail    | 35%  |
|           | ICICI Securities Limited   |
|           | Edelweiss Financial Services Limited                             |
| BRLM      | Kotak Mahindra Capital Company Limited                           |
|           | Nomura Financial Advisory and Securities (India) Private Limited |
| Registrar | KFin Technologies Ltd  |

| Particulars    | Pre Issue % | Post Issue % |
|----------------|-------------|--------------|
| Promoter       | 39.10%      | 32.68%       |
| Promoter Group | 0.97%       | 0.97%        |
| Public         | 59.93       | 66.35%       |
| <b>Total</b>   | <b>100%</b> | <b>100%</b>  |

(Assuming issue subscribed at higher band)

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# Five Star Business Finance Ltd.

## Income Statement (Rs in millions)

| Particulars(Rs in thousands)          | Q1FY23       | FY22          | FY21          | FY20         |
|---------------------------------------|--------------|---------------|---------------|--------------|
| <b>Income</b>                         |              |               |               |              |
| Revenue from Operations               | 3,380        | 12,541        | 10,497        | 7,867        |
| <b>Total Revenue</b>                  | <b>3,380</b> | <b>12,541</b> | <b>10,497</b> | <b>7,867</b> |
| Fee expenses                          | -            | -             | 27            | 4            |
| Finance costs                         | 648          | 3,006         | 3,252         | 2,169        |
| Impairment on Financial Instruments   | (4)          | 455           | 352           | 493          |
| Employee benefit expenses             | 719          | 2,361         | 1,637         | 1,271        |
| Other expenses                        | 130          | 575           | 367           | 342          |
| <b>Total Operating Expenses</b>       | <b>1,493</b> | <b>6,397</b>  | <b>5,634</b>  | <b>4,280</b> |
| <b>Total Operating Profit</b>         | <b>1,887</b> | <b>6,143</b>  | <b>4,863</b>  | <b>3,587</b> |
| Depreciation and amortisation expense | 36           | 122           | 114           | 101          |
| Other income                          | 11           | 21            | 15            | 6            |
| <b>PBT</b>                            | <b>1,862</b> | <b>6,042</b>  | <b>4,764</b>  | <b>3,493</b> |
| Current tax                           | 469          | 1,596         | 1,259         | 1,006        |
| Deferred Tax charge                   | (2)          | (89)          | (85)          | (132)        |
| MAT Credit reversed/(availed)         | -            | -             | -             | -            |
| <b>Total tax</b>                      | <b>467</b>   | <b>1,507</b>  | <b>1,174</b>  | <b>874</b>   |
| <b>PAT</b>                            | <b>1,394</b> | <b>4,535</b>  | <b>3,590</b>  | <b>2,620</b> |
| <b>Diluted EPS</b>                    | <b>5</b>     | <b>16</b>     | <b>14</b>     | <b>10</b>    |

Source: RHP, BP Equities Research

## Cash Flow Statement (Rs in million)

| Particulars (Rs in thousands)                                   | Q1FY23         | FY22           | FY21          | FY20         |
|---|----------------|----------------|---------------|--------------|
| Cash Flow from operating activities                             | (1,746)        | (2,772)        | (1,573)       | (15,233)     |
| Cash flow from investing activities                             | 306            | (3,839)        | 1,021         | (1,319)      |
| Cash flow from financing activities                             | (597)          | 70             | 10,325        | 17,253       |
| <b>Net increase/(decrease) in cash and cash equivalents</b>     | <b>(2,036)</b> | <b>(6,540)</b> | <b>9,774</b>  | <b>701</b>   |
| <b>Cash and cash equivalents at the beginning of the period</b> | <b>6,132</b>   | <b>12,672</b>  | <b>2,898</b>  | <b>2,197</b> |
| <b>Cash and cash equivalents at the end of the period</b>       | <b>4,096</b>   | <b>6,132</b>   | <b>12,672</b> | <b>2,898</b> |

Source: RHP, BP Equities Research



## Five Star Business Finance Ltd.

## Balance Sheet (Rs in millions)

| Particulars  | Q1FY23        | FY22          | FY21          | FY20          |
|--|---------------|---------------|---------------|---------------|
| <b>Equity and Liabilities</b>  |               |               |               |               |
| Share Capital  | 291           | 291           | 256           | 256           |
| Other Equity   | 38,278        | 36,812        | 22,925        | 19,190        |
| <b>Net worth</b>   | <b>38,570</b> | <b>37,104</b> | <b>23,182</b> | <b>19,446</b> |
| <b>Financial Liabilities</b>   |               |               |               |               |
| Borrowings(other than debt securities)   | 15,729        | 15,503        | 21,214        | 12,848        |
| Debt Securities  | 9,474         | 10,085        | 13,038        | 10,789        |
| Other Financial Liabilities  | 535           | 415           | 172           | 157           |
| <b>Total Non Current Liabilities</b>   | <b>25,739</b> | <b>26,003</b> | <b>34,424</b> | <b>23,794</b> |
| <b>Current Liabilities</b>   |               |               |               |               |
| Derivative Financial Instrument  |               | 14            |               |               |
| Trade Payables   |               |               |               |               |
| (a) total outstanding dues of micro enterprises and small enterprises                      |               |               |               |               |
| (b) total outstanding dues of creditors other than micro enterprises and small enterprises | 109           | 130           | 87            | 66            |
| Short Term Provisions  | 135           | 90            | 72            | 58            |
| Other non financial liabilities  | 53            | 90            | 172           | 161           |
| Current tax liabilities  | 109           | 0             | 0             | 7             |
| <b>Total Current Liabilities</b>   | <b>407</b>    | <b>324</b>    | <b>331</b>    | <b>292</b>    |
| <b>Total liabilities</b>   | <b>26,146</b> | <b>26,327</b> | <b>34,754</b> | <b>24,086</b> |
| <b>Total Equity and Liabilities</b>  | <b>64,715</b> | <b>63,431</b> | <b>57,936</b> | <b>43,532</b> |
| <b>Assets</b>  |               |               |               |               |
| Property, plant and equipment  | 130           | 121           | 85            | 111           |
| Right-of-Use assets  | 208           | 198           | 145           | 149           |
| Other Intangible assets  | 10            | 9             | 19            | 19            |
| Investment property  | 0             | 0             | 0             | 0             |
| Other Financial Assets   | 187           | 180           | 47            | 52            |
| Deferred tax assets  | 471           | 467           | 370           | 282           |
| <b>Total Non current assets</b>  | <b>1,007</b>  | <b>975</b>    | <b>667</b>    | <b>614</b>    |
| Investments  | 1,892         | 2,482         | 0             | 0             |
| <b>Financial Assets</b>  |               |               |               |               |
| Loans  | 54,544        | 51,024        | 43,587        | 38,308        |
| Cash and cash equivalents  | 4,096         | 6,132         | 12,672        | 2,898         |
| Other Bank Balances  | 3,036         | 2,668         | 885           | 1,613         |
| Derivative Financial Instrument  | 4             | 0             | 0             | 0             |
| Other Non Financial Assets   | 106           | 128           | 45            | 55            |
| Current tax assets   | 32            | 22            | 80            | 44            |
| <b>Total Current Asset</b>   | <b>63,709</b> | <b>62,456</b> | <b>57,270</b> | <b>42,918</b> |
| <b>Total Assets</b>  | <b>64,715</b> | <b>63,431</b> | <b>57,936</b> | <b>43,532</b> |

Source: RHP, BP Equities Research

**Key Risks**

- ⇒ We require substantial capital for our business and any disruption in our sources of capital could have an adverse effect on our business, results of operations and financial condition.
- ⇒ The risk of non-payment or default by our borrowers may adversely affect our business, results of operations and financial condition.
- ⇒ Our inability to meet our obligations, including financial and other covenants under our debt financing arrangements, could adversely affect our business, results of operations and financial condition.

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