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## Initial Public Offer of Five-Star Business Finance Limited

**Issue Opens on: November 09, 2022 | Issue Closes on: November 11, 2022**

**Price Band – ₹ 450 to ₹ 474 per equity share**

**The Floor Price is 450 times the face value of the Equity Shares and the Cap Price is 474 times the face value of the Equity Shares**

**Minimum Bid Lot of 31 shares; Bids in multiples of 31 shares thereafter**

Initial Public Offer of up to 4,13,50,316\* Equity shares of face value of ₹ 1 each (“Equity Shares”) of Five-Star Business Finance Limited (“Company” or “Issuer”) for cash at a price of ₹ [●] per equity share (including a share premium of ₹ [●] per equity share) (“Offer Price”) aggregating up to ₹ 19,600.05 million (The “Offer”) through an Offer for Sale of up to 4,13,50,316\* equity shares (the “Offer for Sale”), consisting of up to [●] equity shares aggregating up to ₹ 1,667.42 million by SCI Investments V, up to [●] equity shares aggregating up to ₹ 7,194.14 million by Matrix Partners India Investment Holdings II, LLC, up to [●] equity shares aggregating up to ₹ 120.87 million by Matrix Partners India Investments II Extension, LLC, up to [●] equity shares aggregating up to ₹ 3,614.47 million by Norwest Venture Partners X – Mauritius and up to [●] equity shares aggregating up to ₹ 7,003.15 million by TPG Asia VII SF PTE. Ltd. (collectively, the “Selling Shareholders”, and such equity shares, the “Offered Shares”). The offer shall constitute [●]% of the post-offer paid-up equity share capital of Company.

\*Assuming aggregate shares, amounts and/or percentage calculated at upper end of the Price Band of ₹ 474.

### Overview of the Company

#### Business Overview

- Five Star Business Finance Limited NBFC-ND-SI providing secured business loans to micro-entrepreneurs and self-employed individuals, each of whom are largely excluded by traditional financing institutions
- It is headquartered in Chennai, Tamil Nadu with a strong presence in south India and all of its loans are secured by borrowers’ property, predominantly being SORP.
- According to the CRISIL Report, among its compared peers (being NBFCs in India):
  - within a subset of large peers (with more than ₹30,000 million in Gross Term Loans), it had the fastest Gross Term Loans growth, with a compound annual growth rate (“CAGR”) of 65.0% (Financial Year 2017 to 2021)
  - within a subset of large peers (with more than ₹30,000 million in Gross Term Loans), it had the highest average return on Gross Term Loans of 7.5%, across the period covering Financial Years 2022, 2021 and 2020; and
  - it is among the three best for gross non-performing assets (being Stage 3 Gross Term Loans which are 90+ Days-Past-Due (“DPD”)) as a percentage of Gross Term Loans (it had Stage 3 Gross Term Loans as a percentage of Gross Term Loans of 1.05%) as of March 31, 2022, while it has the best asset quality among lenders identified by CRISIL as engaged in extending MSME business loans, with other lenders reporting 90+ DPD more than 2%
- It had an active loan base of 230,175 and 217,745 as of June 30, 2022 and March 31, 2022, respectively
- Its Gross Term Loans has grown to ₹52,965.35 million as of June 30, 2022 (₹50,670.78 million as of March 31, 2022), from ₹10,082.58 million as of March 31, 2018, at a CAGR of 49.73% between March 31, 2018 and March 31, 2022
- Five-Star primarily offers customers small loans for business purposes which accounted for ₹32,903.06 million (62.12% of Gross Term Loans), ₹28,769.34 million (62.85% of Gross Term Loans), ₹31,634.74 million (62.43% of Gross Term Loans), ₹27,934.54 million (62.84% of Gross Term Loans) and ₹24,477.65 million (62.89% of Gross Term Loans), as of June 30, 2022, June 30, 2021, March 31, 2022, March 31, 2021 and March 31, 2020; as well as loans for asset creation such as home renovation or improvement, or for meeting expenses for significant economic events such as marriage, healthcare and education, which accounted for ₹20,062.29 million (37.88% of Gross Term Loans), ₹17,005.77 million (37.15% of Gross Term Loans), ₹19,035.94 million (37.57% of Gross Term Loans), ₹16,519.27 million (37.16% of Gross Term Loans) and ₹14,444.64 million (37.11% of Gross Term Loans), as of the same dates
- Company targets customers:
  - in urban and semi-urban locations, as well as in the rural markets of India, where CRISIL expects faster growth in bank credit activity as financial awareness increases;
  - who typically derive income from “everyday” cash and carry businesses with a focus on services;

- with household net cash-flows of approximately ₹25,000 to ₹40,000 per month;
- who can provide collateral (typically land and building of approximately ₹1.0 million in value; and
- whose family will act as co-applicants on the loan.
- Extensive network of 311 branches, as of June 30, 2022, spread across approximately 150 districts, eight states and one union territory, with Tamil Nadu, Andhra Pradesh, Telangana and Karnataka being its key states
- Such key states collectively accounted for approximately 85% of branch network by number, as of June 30, 2022
- As of June 30, 2022, approximately 95% of branches were located in cities and towns with populations up to one million
- Long-term ratings from ICRA and CARE is A+ (a significant improvement from its rating of BBB-, from CARE in Financial Year 2015), its short-term borrowings are rated A1+ by CARE

The following table sets forth certain key operational and financial metrics as of and for the periods/years indicated

Metric	As of and for the						
	Three months ended June 30,		Financial Year				
	2022	2021	2022	2021	2020	2019*	2018*
<b>OPERATIONAL METRICS</b>							
Live Accounts <sup>(1)</sup>	230,175	184,479	217,745	176,467	143,079	72,890	33,157
Branches <sup>(2)</sup>	311	263	300	262	252	173	130
Number of Loans Disbursed <sup>(3)</sup>	19,793	12,236	63,633	48,111	76,634	43,988	19,257
Disbursements <sup>(4)</sup> (₹ in millions)	5,684.33	3,331.60	17,562.40	12,450.54	24,086.69	14,814.62	6,837.99
Gross Term Loans (₹ in millions)	52,965.35	45,775.11	50,670.78	44,453.81	38,922.28	21,128.06	10,082.58
Gross Term Loans Growth <sup>(5)</sup> (%)	4.53	2.97	13.99	14.21	84.22	109.55	104.27
Stage 3 Gross Term Loans to Gross Term Loans (%)	1.12	1.64	1.05	1.02	1.37	0.88	1.45
Stage 3 Gross Term Loans (net) to Gross Term Loans (%)	0.68	1.03	0.68	0.83	1.13	0.68	0.96
Gross Term Loans per Business Officer <sup>(17)</sup> (₹ in millions)	20.77	22.37	20.54	22.14	21.22	20.94	14.61
Average number of Business Officers per branch <sup>(23)</sup>	8.20	7.78	8.22	7.66	7.28	5.83	5.31
Average Ticket Size <sup>(8)</sup> (₹ in millions)	0.29	0.27	0.28	0.26	0.31	0.34	0.36

Metric	As of and for the				
	Three months ended June 30,		Financial Year		
	2022	2021	2022	2021	2020
<b>FINANCIAL METRICS</b>					
Average Yield on Gross Term Loans (%)	24.15	24.20	24.05	24.17	24.18
Average Cost of Borrowing (%)	10.53	10.68	10.51	11.48	12.07
Net Interest Margin (%)	19.17	16.63	17.68	16.00	16.69
Operating Expenses to Average Total Assets (%)	5.51	4.07	4.86	4.16	4.85
Impairment loss allowance to Average Total Assets (%)	(0.03)	1.07	0.72	0.69	1.38
Cost to Income Ratio (%)	32.25	36.99	36.91	34.30	38.97
Profit for the period / year after tax (₹ in millions)	1,394.33	1,015.71	4,535.45	3,589.94	2,619.51
Net Worth <sup>(15)</sup> (₹ in millions)	38,569.75	29,444.13	37,103.51	23,181.72	19,445.80
Total Borrowings <sup>(16)</sup> (₹ in millions)	25,203.19	31,212.18	25,588.31	34,251.97	23,636.93
Return on Average Net Worth (%)	3.69 <sup>^</sup>	3.67 <sup>^</sup>	13.86	16.85	15.35
Basic EPS (in ₹)	4.79 <sup>^</sup>	3.80 <sup>^</sup>	16.09	14.01	10.32
Diluted EPS (in ₹)	4.74 <sup>^</sup>	3.66 <sup>^</sup>	15.92	13.61	10.07
Net Asset Value Per Share	132.38	102.73	127.35	85.26	71.68

<sup>^</sup> Not Annualised

Select list of shareholders:

S. No.	Name of the Shareholder	Number of Equity Shares	Percentage of the pre-Offer Equity Share capital a fully diluted basis (%)*
1.	TPG Asia VII SF Pte. Ltd.	62,726,964	21.45
2.	Matrix Partners India Investment Holdings II, LLC	36,447,465	12.46
3.	Lakshmi pathy Deenadayalan	30,690,678	10.49

4.	Norwest Venture Partners X – Mauritius	29,748,060	10.17%
5.	SCI Investments V	25,696,500	8.79%
6.	Hema Lakshmipathy	20,890,600	7.14%
7.	Sirius II Pte Ltd	17,593,990	6.02%

**Fastest Gross Term Loans growth among its compared peers with more than ₹30,000 million in Gross Term Loans, with strong return and growth metrics and a significant potential addressable market; (CRISIL Report)**

- According to CRISIL, the potential market for residential property-backed secured MSME lending in India is approximately ₹22 trillion, with Uttar Pradesh, West Bengal, Maharashtra, Rajasthan and Tamil Nadu collectively accounting for over half of such potential market
- Five-Star has the fastest Gross Term Loans growth among its compared peers (being NBFCs in India) with more than ₹30,000 million in Gross Term Loans, with a CAGR of 65.0% (Financial Year 2017 to six months ended September 30, 2021) (CRISIL Report), catering to the small business finance needs of unserved and underserved customers.
- While its Gross Term Loans has grown to ₹50,670.78 million as of March 31, 2022 from ₹10,082.58 million as of March 31, 2018, at a CAGR of 49.73% (between March 31, 2018 and March 31, 2022), its growth has primarily been volume led with consistent ATS and steady yields
- As per the CRISIL Report, it had the highest average return on Gross Term Loans of 7.5% among its compared peers with more than ₹30,000 million in Gross Term Loans, across the period covering Financial Years 2022, 2021 and 2020; and for each of those Financial Years, its return on Gross Term Loans as calculated by CRISIL was 7.5%, 7.1% and 7.8%, respectively
- Such returns are as a result of its ability to lend to customers at consistently superior yields and then control costs through initiatives including:
  - reduction in cost of borrowings (its Average Cost of Borrowings was 12.07% as of March 31, 2020, 11.48% as of March 31, 2021, 10.51% as of March 31, 2022, 10.68% as of June 30, 2021 and 10.53% as of June 30, 2022);
  - use of technological advancements to drive improvement in productivity and bring down operational costs,
  - robust collections infrastructure; and
  - effective risk containment and continuous monitoring leading to low credit costs, low branch costs and efficiency in hiring through local talent pools
- Among compared peers, Company is among the three best for for Stage 3 Gross Term Loans as a percentage of Gross Term Loans (it had a Stage 3 Gross Term Loans to Gross Term Loans of 1.05%) as of March 31, 2022, while they have the best asset quality among lenders identified by CRISIL as engaged in extending MSME business loans, with other lenders reporting 90+ DPD more than 2%. (CRISIL Report)
- According to CRISIL, it had the lowest credit cost of 0.7% among the compared peers engaged in extending MSME business loans in Financial Year 2021 (Financial Year 2022: 0.8%; Financial Year 2020: 1.5%), due to its asset quality. (CRISIL Report)

**Strengths**

**Among the select institutions to develop an underwriting model that evaluates the cash-flows of small business owners and self-employed individuals in the absence of traditional documentary proofs of income (CRISIL Report)**

- Five-Star has an underwriting model to provide secured financial solutions to small business owners and self-employed individuals and over the last two decades of operation in this particular product, are among the select institutions to have developed such model in India. (CRISIL Report)
- The model is customer centric and is underpinned by underwriting practices that triangulate the character, cash-flow, and collateral of potential customers
- Underwriting practices are characterized by a multi-level evaluation process for each loan, where the sourcing team is responsible for conducting the preliminary assessment of each potential borrower, which is then independently evaluated by Field Credit Team, before File Credit Team reviews and approves the loan proposal
- Company has evolved this underwriting model over time and through economic cycles to ensure that it remains relevant and captures all key elements that it view as critical to maintain a robust asset quality

**Strong on-ground collections infrastructure leading to its ability to maintain a robust asset quality**

- Company has also created a strong “on-ground” collections infrastructure to ensure that it maintains a high asset quality
- Collections process involves high-touch engagement between Business Officers and customers and to optimize this interaction, it ensures that each Relationship Officer is responsible for no more than 120 customers on an average and it adds Business Officers as business grows
- For accounts in the 90+ DPD category, there is a coordinated effort between the corporate office and the branch to bring the account to a lower category
- Incentives for each individual at the branch are linked to the branch adhering to such Stage 3 Gross Term Loans target

**Ability to successfully expand to new underpenetrated geographies through a calibrated expansion strategy**

- According to the CRISIL Report, as of March 31, 2022, less than 15% of approximately 70 million MSMEs in India have access to formal credit in any form.
- Since starting as a Chennai based NBFC, it has demonstrated ability to grow beyond local market.
  - Its first growth phase was between Financial Year 2010 and Financial Year 2015 where it increased from six branches in Chennai to 39 branches across Tamil Nadu.
  - Between Financial Year 2015 and Financial Year 2018, it started to expand in the states of Andhra Pradesh, Telangana and Karnataka, growing from three branches to 72 branches during this period.
  - Since then, it has further expanded to 165 branches across Andhra Pradesh, Telangana and Karnataka, as of June 30, 2022.
- In addition, from March 31, 2017 to June 30, 2022, its Gross Term Loans in Tamil Nadu (including Pondicherry) grew from

- ₹3,429.84 million to ₹20,172.11 million, in Andhra Pradesh grew from ₹1,271.74 million to ₹15,770.01 million, and in Telangana grew from ₹114.98 million to ₹10,325.80 million
- Company adopts a calibrated strategy of contiguous expansion across geographies where there is substantial demand for its offering and which has allowed for the maintenance of robust asset quality

**100% in-house sourcing, comprehensive credit assessment and robust risk management and collections framework, leading to good asset quality**

- Five-Star's 100% in-house sourcing, comprehensive credit assessment and robust risk management and collections framework allows it to identify, monitor and manage risks inherent in its operations
- As of June 30, 2022, an estimated 95% of the loans that it disbursed were for single-unit, SORPs, that is, it has a high SORP focus
- Over the last three Financial Years and the three months ended June 30, 2022, it has provided loans to more than 205,000 customers
- To assist with credit assessment and risk management functions, it has created a four layered process for customer evaluation – two layers within the business and collections team and two layers within the credit team, in addition to independent legal checks
- It had a 4,381-member business and collections team including 3,424 Business Officers and Collection Officers catering to 230,175 loan accounts, as of June 30, 2022

**Access to diversified and cost-effective long-term financing with a conservative approach to asset liability and liquidity management**

- Average Cost of Borrowings on Average Total Borrowings was 10.53% as of June 30, 2022, 10.68% as of June 30, 2021, 10.51% as of March 31, 2022, 11.48% as of March 31, 2021 and 12.07% as of March 31, 2020
- Company's cost of incremental borrowings decreased from 11.37% in the Financial Year 2020 to 9.68% in the Financial Year 2021 and to 8.51% in the Financial Year 2022, and was nil and 8.42% in the three months ended June 30, 2021 and 2022
- It believes that it is able to access borrowings at a competitive costs due to its stable credit history, strong credit ratings, equity capital position and low leverage, and risk management policies
- As of June 30, 2022, it borrowed from 17 private sector banks, seven public sector banks, 13 NBFCs, one mutual fund, and 14 other entities; and its outstanding borrowings were ₹7,300.28 million from private sector banks, ₹5,852.95 million from public sector banks, ₹3,657.00 million from NBFCs, ₹1,501.27 million from mutual funds, and ₹6,891.70 million from other entities, as of the same date

**Experienced, cycle-tested leadership with an experienced longstanding promoter, and a professional management team and supported by marquee investors**

- Company is led by qualified and experienced management personnel, who are supported by a capable and motivated team of managers and other employees.
- Its management team has knowledge and understanding of the small business finance landscape in India and the expertise and vision to organically grow the business.
- They also have diverse experience in a range of financial products and functions related to its business and operations and are supported by qualified personnel who have an in-depth understanding of the geographic regions in which it operates, loan products and customer segment as a result of its focus on hiring local staff with strong local personal and professional networks
- Founder, Promoter, and Chairman and Managing Director, Lakshmi pathy Deenadayalan, has been associated with Five-Star for the past 20 years
- He has a deep understanding of customer behavior and the business and operations, and has been critical to developing and enhancing its business model and driving its total income and profitability
- Shareholders include marquee investors, including affiliates of TPG Capital, Sequoia Capital, Matrix Partners, Norwest Venture Partners, KKR and TVS Capital Funds Limited and we believe we have benefited significantly from their collective vision and experience

**Strategies**

- Increase penetration in existing markets through increasing branch staff numbers, increasing its branch network in the existing geographies and diversifying to contiguous markets;
- Continue to focus on small business owners and self-employed individuals primarily in the semi-urban and urban markets of India, as well as in rural markets where CRISIL expects faster growth in bank credit activity as financial awareness increases;
- Optimize its borrowing costs, reduce operating expenses further and continue to expand and diversify its lender base;
- Continue to invest in technology and data analytics to build a scalable and efficient operating model / to improve customer experience, increase productivity and decrease costs;
- Focus on enhancing its risk management framework; and
- Enhance its brand recall to attract new customers

**Objects of the Offer**

- The objects of the Offer are to
    - carry out the Offer for Sale; and
    - achieve the benefits of listing the Equity Shares on the Stock Exchanges.
- Company will not receive any proceeds from the Offer and all such proceeds (net of any Offer related expenses to be borne by the Selling Shareholders) will go to the Selling Shareholders

Investors are requested to refer to the Red Herring Prospectus (available at [https://www.icicisecurities.com/Upload/ArticleAttachments/Five\\_Star\\_Business\\_Finance\\_Limited\\_Red\\_Herring\\_Prospectus.pdf](https://www.icicisecurities.com/Upload/ArticleAttachments/Five_Star_Business_Finance_Limited_Red_Herring_Prospectus.pdf)) dated November 01, 2022 for details regarding the Offer, the Company and the risk factors before taking any investment decision.