



IPO Report

02nd Aug '23

Snapshot

SBFC Finance a systemically important, non-deposit taking non-banking finance company ("NBFC-ND-SI") offering Secured MSME Loans and Loans against Gold, with a majority of company's borrowers being entrepreneurs, small business owners, self-employed individuals, salaried and working class individuals. Among MSME-focused NBFCs in India, company have one of the highest assets under management ("AUM") growth, at a CAGR of 44% in the period from Fiscal 2019 to Fiscal 2023. Company have also witnessed healthy disbursement growth, at a CAGR of 40% between Fiscal 2021 and Fiscal 2023.

VALUATION

SBFC Finance is bringing the issue at price band of Rs 54-57 per share at p/b multiple of 2.5x.

Company has diversified pan-India presence with an extensive network to cater to target customer segment. Due to 100% in-house sourcing in turn leading to superior business outcomes. Company has Comprehensive credit assessment, underwriting and risk management framework with extensive on-ground collections infrastructure leading to maintenance of robust asset quality. Company has healthy liability franchise with low cost of funds. Company has shown consistent financial performance backed by profitable growth and experienced, cycle-tested and professional management team with good corporate governance backed by marquee investors.

Hence we recommend to "Subscribe" issue

Price Band (Rs./Share)	54-57
Opening date of the issue	03 rd Aug 2023
Closing Date of the issue	07 th Aug 2023
No of shares pre issue	958908906 Eq Shares
Issue Size(In Rs)	Rs 1025 Cr
Issue Size (in No of Shares)	189887816-179889950 Eq Shares
Fresh issue	Rs 600 Cr
Offer For Sale	Rs 425 Cr
Face Value (Rs/ share)	Rs 10/share
Employee Discount	Rs 2/share
Bid Lot	260

BIDDING DETAILS

QIBs (Including Anchor)	50% of the offer (Approx 89013156 Eq Shares)
Non-Institutional	15% of the offer (Approx 26703948 Eq Shares)
Retail	35% of the offer (Approx 62309210 Eq Shares)
Employee Reservation	Rs 10.25 Cr
Pre Issue Promoter & Group Holding	80.48%
Post Issue Promoter & Group Holding	65.51%
Lead managers	ICICI Securities, Kotak Mahindra Capital, Axis Capital
Registrar to the issue	KFin Technologies Ltd.

KEY HIGHLIGHTS

Diversified pan-India presence with an extensive network to cater to company's target customer segment

As of March 31, 2023, company have an expansive footprint in 120 cities, spanning 16 Indian states and two union territories, with 152 branches. Company have lowered its geographic concentration risk and its extensive, geographically diverse distribution network allows company to penetrate underbanked populations in tier II and tier III cities in India. As of March 2022, less than 15% of the approximate 70 million MSMEs in India have access to formal credit in any form.

Consistent financial performance backed by profitable growth

As of March 31, 2023, company's average yield on Gross Loan Book was 15.91%, with Secured MSME Loans and Loans against Gold accounting for 15.89% and 15.64%, respectively. Company's Loan against Gold portfolio has grown from 36,813 customers as of March 31, 2021 to 59,437 customers, as of March 31, 2023 at a CAGR of 27.07%. Company's AUM has grown from ₹ 22,213.23 million as of March 31, 2021, to ₹ 49,428.23 million as of March 31, 2023, at a CAGR of 49.17%.

Experienced, cycle-tested and professional management team with good corporate governance backed by marquee investors

Company's CEO, Aseem Dhru, has more than 25 years of experience, and was previously Group Head - Business Banking, Working Capital and Retail Agri business at HDFC Bank. He has also been the Managing Director and CEO of HDFC Securities Limited and was a director on the board of HDB Financial Services Limited. Company is backed by marquee institutional investors such as the Clermont Group, Arpwood Group, and Malabar Group, who provide their expertise to company's operations, including through their representatives on company's Board.



COMPANY BACKGROUND

As of March 31, 2023, the average ticket size (“ATS”) of company’s Secured MSME Loans, Loans against Gold and other unsecured loans, on the basis of disbursed amounts was ₹ 0.99 million, ₹ 0.09 million and ₹ 0.69 million, respectively. Among NBFCs, the Gross NPA for Secured MSME Loans for ticket sizes between ₹ 0.50 million and ₹ 3.00 million was 4.2% in March 2023. As of March 31, 2023, company’s Gross NPA to AUM ratio for ticket sizes between ₹ 0.50 million and ₹ 3.00 million was 1.97%. Company’s total AUM as of March 31, 2021, March 31, 2022 and March 31, 2023 was ₹ 22,213.23 million, ₹ 31,921.81 million and ₹ 49,428.23 million, respectively. As of March 31, 2021, March 31, 2022 and March 31, 2023, company had provided loans to 56,587, 72,816 and 102,722 customers, respectively.

Company have a diversified pan-India presence, with an extensive network in its target customer segment. As of March 31, 2023, company have an expansive footprint in 120 cities, spanning 16 Indian states and two union territories, with 152 branches. Company’s geographically diverse distribution network, spread across the North, South, East and West zones, allows it to penetrate underbanked populations in tier II and tier III cities in India. Company’s AUM is diversified across India, with 30.84%, being ₹ 15,242.41 million, in the North (in the states of Chandigarh, Delhi, Haryana, Punjab, Rajasthan, Uttar Pradesh and Uttarakhand), 38.53%, being ₹ 19,047.97 million, in the South (in the states of Karnataka, Andhra Pradesh, Telangana, Tamil Nadu and Puducherry), and 30.63%, being ₹ 15,137.85 million, in the West and East (in the states of Gujarat, Madhya Pradesh, Maharashtra, West Bengal, Assam and Bihar) collectively, as of March 31, 2023. Company primarily focus on small enterprise borrowers, whose monthly income is up to ₹ 0.15 million, with a demonstrable track record of servicing loans such as gold loans, loans for two-wheeler vehicles and have a CIBIL score above 700 at the time of origination. Company source customers directly through its sales team of 1,911 employees as of March 31, 2023, and have adopted a direct sourcing model through branch-led local marketing efforts, repeat customers or through walk-ins, which has helped company maintain contact with its customers and establish strong relationships with them, high levels of customer satisfaction and increased loyalty.

As of March 31, 2023, approximately 89.49% of company’s Secured MSME Loan collections and 90.92% of its unsecured loan collections were non-cash based EMI collections, thus reducing company’s cash management risk, and enabling customers to receive real-time payment receipts through SMS.



INVESTMENT RATIONALE

<p><i>100% in-house sourcing, leading to favourable business outcomes</i></p>	<p>Company acknowledge the complexities of underwriting such loans, and to ensure positive business outcomes, 100% of company's loan portfolio has in-house origination, limiting company's reliance on direct selling agents or connectors in order to ensure a more direct, thorough understanding of the customer's profile. Company source customers directly through its sales team of 1,911 personnel as of March 31, 2023, and have adopted a direct sourcing model through branch-led local marketing efforts, repeat customers or through walk-ins, which has helped company maintain contact with its customers and establish close relationships with them, high levels of customer satisfaction and increased loyalty. Company's AUM per employee has also increased from ₹ 15.10 million as of March 31, 2021, to ₹ 15.59 million as of March 31, 2022 and further to ₹ 17.52 million as of March 31, 2023.</p>
<p><i>Comprehensive credit assessment, underwriting and risk management framework</i></p>	<p>Company have a credit assessment and risk management framework to identify, monitor and manage risks inherent in its operations. Credit management is crucial to company's business since a significant number of company's customers are from the underserved financial segment. Company have a core focus area of small enterprise borrowers, whose monthly income is up to ₹ 0.15 million, with a demonstrable track record of servicing loans such as gold loans, loans for two-wheeler vehicles, among others. High risk perception and prohibitive cost of delivering services physically have constrained formal lending to MSMEs. Company focus on the profile of the borrower, and as of March 31, 2023, 82.32% of company's Secured MSME Loan customers have a CIBIL score above 700 at the time of origination, while 7.90% of company's customers are new to the formal secured lending ecosystem. Company serve customers in tier II and tier III markets who have a strong credit history but may lack formal proof of income documents. Company focus on collateral-backed lending and as of March 31, 2023, 96.44% of company's loan portfolio was secured. Property which is provided as collateral is largely self-occupied residential or commercial property, and as of March 31, 2023, 82.75% of Secured MSME Loans were with self-occupied residential property as collateral and 11.01% were with self-occupied commercial property as collateral. The remaining collateral provided is either rented or mixed use property. As of March 31, 2023, company's Secured MSME Loans have an average LTV ratio of 42.51% and Loans against Gold having an average LTV ratio of 68.51%</p>
<p><i>Healthy liability franchise with low cost of funds</i></p>	<p>Company's average cost of borrowing was 8.11%, 7.65% and 8.22% for Fiscal 2021, 2022 and 2023, respectively and its Incremental Cost of Borrowings (which represents weighted average rate of interest on fresh borrowings in the relevant period) was 8.76% for Fiscal 2023. As of March 31, 2023, company's outstanding borrowings included ₹ 29,121.73 million from public and private sector banks and ₹ 3,672.49 million from NBFCs and other financial institutions. As of March 31, 2023, company's total borrowings aggregated to ₹ 37,458.33 million, comprising primarily of term loans of ₹ 32,794.22 million, working capital demand loans from banks of ₹ 600.00 million, non-convertible debentures of ₹ 430.00 million and other collateralized borrowings of ₹ 3,634.11 million. Company have received a credit rating upgrade of [ICRA] A+ (Stable) in October 2022 from [ICRA] A (Positive) in October 2021. Company have received a rating of CARE A+; Stable for its long term bank facilities in April 2023.</p>



OBJECTS OF OFFER

Company proposes to utilize the Net Proceeds towards augmenting its capital base to meet future capital requirements arising out of the growth of company's business and assets.

RISKS

The quality of company's portfolio may be impacted due to higher levels of NPAs and company's business may be adversely affected if company is unable to provide for such higher levels of NPAs..

Source:RHP

INDUSTRY OVERVIEW

GROWTH DRIVERS

High credit gap in the MSME segment

Less than 15% of approximately 70 million odd MSMEs have access to formal credit in any manner as of March 2022. High risk perception and the prohibitive cost of delivering services physically have constrained traditional institutions' ability to provide credit to underserved or unserved MSMEs and self-employed individuals historically. As a result, they resort to credit from informal sources. This untapped market offers huge growth potential for financial institutions. As stated earlier, the credit gap was estimated at around ₹ 58.4 trillion as of 2017 (Source: IFC report named Financing India's MSMEs released in November 2018) and is estimated to have widened further to around ₹ 92 trillion as of Fiscal 2023.

Increased data availability and transparency

With increased digital initiatives by the MSMEs, the shift towards their formalisation and digitisation has created a plethora of data points for lenders that would help improve the efficacy of credit assessment and gradually enable provision of credit to hitherto underserved customer segments. For example, the quantum of retail digital payments has catapulted from ₹ 140 trillion in Fiscal 2017 to ₹ 606 trillion in Fiscal 2023. Within UPI, the quantum of person-to-merchant payments has zoomed from ₹ 6.2 trillion in Fiscal 2021 to ₹ 30.7 trillion in Fiscal 2023. UPI has increased banking transactions materially, impacting significant increase in tax compliance. This increase has created a digital footprint of customers, which can be potentially used for credit decision making, along with other relevant parameters such as customer demographics, business details, credit score, and personal situation of the borrower. Demonetisation and GST have further accelerated formalization of the Indian economy.

Growth in branch network of players in MSME segment

Over past few years, players offering MSME loans have expanded their branch network with the intent to serve a larger customer base. In the future also, CRISIL MI&A expects lenders with a strong focus on MSME lending and healthy competitive positioning to continue to invest in branch expansion. With increasing branch network, customer acquisition and credit penetration, share of MSME loans is also expected to increase.

Reduction in risk premiums due to information asymmetry In the absence of reliable information about small businesses, it becomes difficult for lenders to assess the creditworthiness of the borrower. Hence, lenders often charge a credit risk premium from these customers, leading to higher interest rates. By leveraging technology and using a combination of traditional data (bureau data, financial statements, credit score), non-traditional data (payments, telecom, provident fund contribution and psychometric data), and government data (Aadhaar, GST), lenders would be able to gain greater insight into their customers' data, thereby increasing the accuracy of customer assessments. This would reduce the level of asymmetry in information and could lower the credit risk premium over a period.

Increasing competition with entry of new players and partnerships between them

More players in consumer-facing businesses with a repository of data (such as e-commerce companies and payment service providers) are expected to enter the lending business, intensifying competition. For example, In June 2018, Amazon India launched a platform for lenders and sellers, wherein sellers can choose loan offers from various lenders at competitive rates. In August 2021, Meta (earlier known as Facebook) partnered with Indifi Technologies to provide loans to small businesses that advertise on its platform. Incumbent traditional lenders will increasingly leverage the network of their partners and/or digital ecosystem to cross-sell products to existing customers, tap customers of other lenders, and also cater to new-to-credit customers. This will expand the market for MSME loans.

Reduction in TAT and increased use of technology

With the availability of multiple data points and technological advancement, TAT for lending to MSMEs has been continuously declining. This too will drive the demand for MSME loans.


Consolidated Financials

(Rs in Mn)

Financials	FY21	FY22	FY23
Total Revenue From Operations (A)	5115.33	5307.02	7403.61
Total Operating Expenditure (B)	3974.68	4440.06	5389.95
PBT	1140.65	866.96	2013.66
Tax	290.55	221.75	516.30
PAT	850.10	645.21	1497.36
EPS	1.1	0.8	1.7
Eq Cap	7966.74	8068.00	8895.72
Net Worth	12051.08	12871.67	17272.68
ROE%	7.67	5.18	9.93
ROTA%	2.01	1.48	2.92
GNPA%	3.16	2.74	2.43
NNPA%	1.95	1.63	1.41
PCR%	38.25	40.44	42.04
Credit Cost %	0.85	1.14	0.66
NIM%	11.73	9.39	9.32

(Source: RHP)

Peer Comparison

Bank Name	Total Income (₹ in million)	Face Value (₹)	P/B	ROE(%)	NAV per share
SBFC Finance	7403.61	10		9.93	19.26
Listed Peers					
Aavas Financiers (Consolidated)	16106.08	10	3.78	13.14	413.58
Home First Finance Company India (Standalone)	7955.98	10	1.97	9.93	19.26
Aptus Value Housing Finance India Ltd (Consolidated)	11289.99	2	3.73	15.06	67.05
AU Small Finance Bank Ltd (Standalone)	92398.73	10	4.62	13.01	164.64
Five Star Business Finance Limited (Standalone)	15289.28	1	4.47	13.91	148.94

(Source: RHP)



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