

Recommendation	Subscribe
Price Band	Rs 57-60
Bidding Date	3 rd Nov-7 th Nov
Book Running Lead Manager	ICICI Securities, DAM Capital, Nuvama
Registrar	Link Intime India Pvt Ltd
Sector	SFB

Minimum Retail Application- Detail At Cut off Price

Number of Shares	250
Minimum Application Money	Rs. 15000
Discount to retail	0
Payment Mode	ASBA

Consolidated Financials (Rs Cr)	FY22	FY23
Total Income	1355	2124
Pre Prov. Profit	492	894
Adj PAT	55	302

Valuations (FY23 Post Issue)	Upper Band
Market Cap (Rs Cr)	3088
BVPS	40.9
EPS	5.9
P/B	1.5
P/E	10.2

Post Issue Shareholding Pattern	
Promoters	63.4%
Public	36.6%

Offer structure for different categories	
QIB (Including Mutual Fund)	50%
Non-Institutional	15%
Retail	35%
Post Issue Equity (Rs. in cr)	514.59
Issue Size (Rs in cr)	463
Face Value (Rs)	10

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BACKGROUND

ESAF, founded in 1992, is a Small Finance Bank focusing on rural and semi-urban lending. They offer micro, retail, MSME, financial institution, and agricultural loans. Their key strength lies in understanding the microloan segment. They are leveraging technology for underwriting and credit sanctioning for loan products which has resulted in healthy portfolio quality indicators with GNPA/NNPA at 2.5%/1.1% combined with NIMs of ~10.7% resulting in ROA/ROE of 1.6%/19.4% for FY23. The AUM has grown to Rs. 13,924 Cr as of FY23, from Rs. 8,168 Cr as of FY21, at a CAGR of 30.6% between FY21-FY23.

Objects and Details of the Issue:

The public issue consists of Offer For Sale of Rs. 72 Cr and Fresh Issue of Rs. 391 Cr aggregating to total issue size of Rs.463 Cr. The Net Proceeds will be used to boost the bank's Tier-I capital for future growth and regulatory compliance.

Investment Rationale:

- Huge opportunity to support growth over next three years (AUM)
- Focus on rural and semi-urban banking franchise
- Effective Loan Collection and Monitoring Process
- Growing Retail Deposits portfolio

Valuation and Recommendation:-

ESAF SFB has the best asset quality among compared peers. It is favorably placed with portfolio share of 63% from rural and semi-urban, which is the highest among the comparable. Further, it has managed to improve its Non MFI mix from 15% in FY21 to 25% in FY23 which has de-risked its business model. We expect this trend to continue. Over FY21-23 period, ESAF has reasonably done well on all fronts - loan growth, return ratios and asset quality. It's valuation on P/B basis is at a significant discount compared to peers, at 1.5x FY23 post issue BVPS. Considering that the micro finance industry has come out of severe crisis over 2020-22, with most of the bad loans having weeded out of the system, we expect growth and healthy profitability to resume for the sector as well as for ESAF. We recommend subscribing to the issue.

Financials (Cr)	FY21	FY22	FY23	Q1FY24
Total Income	1,049	1,355	2,124	678
Growth	NA	29%	57%	37%
Pre Prov Profit	417	492	894	301
Growth	NA	18%	82%	33%
PAT	105	55	302	130
Growth	NA	-48%	452%	23%
BVPS	30.1	31.4	40.9	41.0
EPS	2.0	1.1	5.9	2.5
ROA	1.0%	0.4%	1.6%	2.4%*
ROE	8.9%	4.1%	19.4%	29.2%*
P/E (Post IPO)	29.3	56.4	10.2	23.8 #
P/B (Post IPO)	2.0	1.9	1.5	1.5 #

Source: NBRR

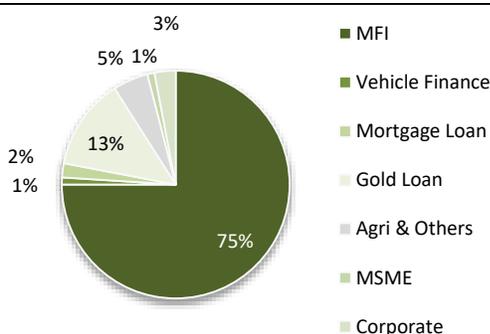
denotes: on post IPO basis

*Annualized figures

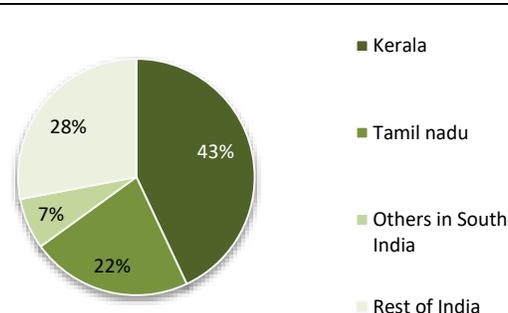
Company Background

ESAF, founded in 1992, is a Small Finance Bank focusing on rural and semi-urban lending. They offer micro, retail, MSME, financial institution, and agricultural loans. It has 700 branches, 767 service centers, 22 correspondents, 2116 banking agents and 525 facilitators, 559 ATMs spread across 21 Indian states & 2 UT. Their key strength is understanding the microloan segment. Its services includes safety deposit lockers, foreign currency exchange, giving customers access to the Bharat Bill Payment System, money transfer services and Aadhaar Seva Kendra services. It also distributes third-party life and general insurance policies and Government pension products.

AUM Mix (Segmental)



State Wise Advances



Source: Company, NBRR

Investment Rationale

Huge opportunity to support growth over next three years (AUM)

As of June 30, 2023, SFB industry AUM is estimated to have crossed Rs 1,900 bn. CRISIL MI&A expects SFB's AUM to grow at ~22-24% CAGR between FY 24-25.

Growth in SFB AUM will be driven by following factors:

- Huge market opportunity in the rural segment
- Presence of informal credit channels
- Geographic diversification
- Access to low-cost funds & huge cross sell opportunity

SFB industry AUM is expected to grow 22-24% CAGR over FY24-25

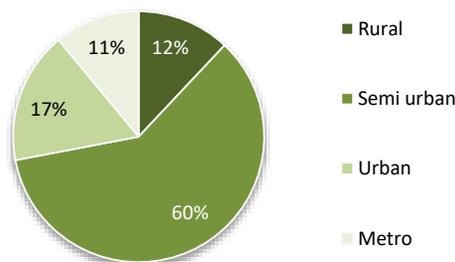


Source: Companies, NBRR

Focus on rural and semi-urban banking franchise

There are growth opportunities in rural centres in India as rural centres have lower financial inclusion compared with urban areas and there is thus less competition for banking services in rural centres compared with urban centres. As at March 31,2023, rural centres, which accounted for 47% of GDP, received just 8% of the overall banking credit, which shows the vast market opportunity for banks and NBFCs to lend in these areas. With increasing focus of the government towards financial inclusion, rising financial awareness, increasing smartphone and internet penetration, the delivery of credit services in rural area is expected to increase. Hence, ESAF’s main focus is on providing loans to customers in rural and semi-urban centres. Its portfolio share of 63% from rural and semi-urban is the highest among the comparable SFBs as on June 30, 2023. ESAF SFB has 72% branches present in rural and semi-urban region as on June 30, 2023, which will enable it to take advantage of this growth opportunity.

Banking Outlets across India

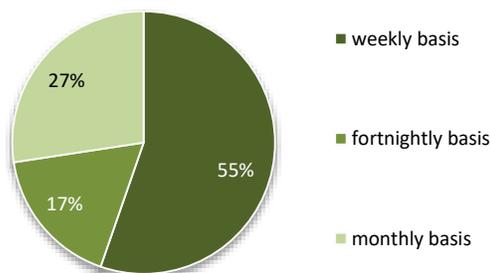


Source: Companies, NBRR

Effective Loan Collection and Monitoring Process

The target customers for Microfinance Loans and Other Micro Loans are women in unserved and underserved households in India. Business correspondent’s source and service customers for the Microfinance Loans and Other Micro Loans. With robust loan collection and effective monitoring process. The collection schedule is tailored to weekly, fortnightly or monthly repayments depending on the preference of customers. Weekly collections at 55% of total induces confidence.

Collection Schedule



Source: Companies, NBRR

Growing Retail Deposits portfolio

ESAF plans to continue to increase deposits, in particular Retail Deposits, in order to help grow business and reduce Cost of Funds. The total deposits increased from Rs. 8999 Cr in FY21 to Rs 15656 Cr in Q1FY24. The Retail Deposits increased from Rs. 8,796 Cr in FY21 to Rs. 13,977 Cr in Q1FY24. The business correspondent entities are the primary channel for sourcing deposits from Micro Loan customers. Hence ESAF plans to add more business correspondents, which will help to increase deposits. Furthermore, it intends to continue to target NRIs to scale up its deposit base and in particular its CASA base. ESAF also plans to establish relationships with more farmer producers' associations, co-operative societies, government departments, non-government organizations, and educational institutions in order to offer its products and services, including CASA, to their members/employees.

Key Risks

Economic slowdown can increase the risk of non-payment or default by borrowers

Micro Loans and some of the retail loans are unsecured and, as such, are at a higher credit risk than secured loans because they are not supported by collateral. Since these advances are unsecured, in the event of defaults by such customers, the ability to realise the amounts would be restricted to initiating legal proceedings for recovery. There can be no guarantee as to the amount of resources that would be utilised and the length of time it could take to conclude such legal proceedings.

Rising competition from NBFCs and SFBs in the longer term

The small finance bank industry in India is witnessing a gradual increase in competition from NBFCs and banks. Some of its competitors have more resources, a wider branch and distribution network, access to cheaper capital and superior technology. This may encourage competitors to expand and achieve economies of scale to a greater extent. Thus if the competition increases, ESAF's growth and margins would get impacted.

Valuation and Recommendation

ESAF is favorably placed with portfolio share of 63% from rural and semi-urban, which is the highest among the comparable. Further, it has managed to improve its Non MFI mix from 15% in FY21 to 25% in FY23 which has de-risked its business model. We expect this trend to continue. Over FY21-23 period, ESAF has reasonably done well on all fronts - loan growth, return ratios and asset quality. It's valuation on P/B basis is at a significant discount compared to peers, at 1.5x FY23 post issue BVPS. Considering that the micro finance industry has come out of severe crisis over 2020-22, with most of the bad loans having weeded out of the system, we expect growth and healthy profitability to resume for the sector as well as for ESAF. We recommend subscribing to the issue.

Listed Comparable Peers

FY23 Metrics	Ujjivan SFB	Credit Access	Spandana	Suryoday SFB	Fusion Micro	Avg.	ESAF
Loan Book (Rs Cr)	24085	17,561	8,511	6,114	9,296	13,113	13,924
CASA	26%	NA	NA	17%	NA	22%	21%
NIM	9.5%	10.8%	10.0%	8.3%	11.5%	10.0%	9.7%
Cost/Income	55%	37%	51%	60%	38%	48%	58%
ROA FY23	3.9%	4.2%	0.2%	0.9%	4.7%	2.7%	1.6%
ROE FY23	31.4%	17.8%	0.4%	5.0%	21.2%	15.2%	19.4%
GNPA	2.6%	1.2%	2.0%	3.1%	3.5%	2.5%	2.5%
NNPA	0.0%	0.4%	1.6%	1.5%	0.9%	0.9%	1.1%
Loan CAGR FY21-23	21%	24%	8%	21%	42%	23%	31%
P/BV Trailing (Post IPO)	2.0x	3.9x	1.6x	1.2x	2.6x	2.3x	1.5x

Source: NBRR

Financials

P&L (Rs. Crs)	FY21	FY22	FY23	Q1FY24	Bal. Sheet (Rs. Crs)	FY21	FY22	FY23	Q1FY24
Interest earned	1,641	1,940	2,854	899	Equity capital	449	449	449	449
Interest expended	720	793	1,017	313	ESOP	0	5	6	6
NII	922	1,147	1,836	585	Reserves & surplus	903	957	1,260	1,390
Non interest income	127	208	288	93	Net worth	1,352	1,412	1,715	1,845
Total income	1,049	1,355	2,124	678	Deposits	8,999	12,815	14,666	15,656
<i>Growth</i>	NA	29%	57%	37%	<i>Growth</i>	NA	42%	14%	16%
Operating expenses	632	863	1,231	378	Borrowings	1,694	2,953	3,354	2,739
<i>Growth</i>		37%	43%	39%	Other liab and prov	293	528	489	556
Staff costs	188	232	278	80	Total liabilities	10,987	16,296	18,509	18,951
Other Op Exp	444	631	953	298	Total liab and equity	12,339	17,708	20,224	20,796
Profit before prov	417	492	894	301	Cash and bank bal	1,819	1,512	767	887
<i>Growth</i>	NA	18%	82%	33%	Investments	1,932	4,070	4,889	4,882
Provisions	276	418	488	127	Net Advances	8,168	11,637	13,924	14,322
<i>Growth</i>	NA	51%	17%	52%	<i>Growth</i>	NA	42%	20%	23%
Exceptional items	0	0	0	0	Other assets	281	329	456	518
Profit before tax	141	74	406	174	Fixed Assets	139	159	188	187
Taxes	36	19	104	44	Total assets	12,339	17,708	20,224	20,796
Net profit	105	55	302	130	<i>Growth</i>	NA	44%	14%	15%
<i>Growth</i>	NA	-48%	452%	23%					

Key Ratios	FY21	FY22	FY23	Q1FY24*	Asset Quality	FY21	FY22	FY23	Q1FY24
Yield on Advances	20.0%	17.4%	19.8%	23.2%	GNPA	564	950	352	238
Cost of Funds	7.6%	6.3%	6.2%	6.9%	GNPA ratio	6.7%	7.8%	2.5%	1.7%
Spread	12.5%	11.1%	13.6%	16.4%	NNPA	317	456	158	116
NIM	8.5%	7.6%	9.7%	11.4%	NNPA ratio	3.9%	3.9%	1.1%	0.8%
					PCR	53%	59%	57%	74%
					Credit Cost	3.8%	4.2%	3.8%	1.0%

Profitability Ratios	FY21	FY22	FY23	Q1FY24*	Balance Sheet Ratios	FY21	FY22	FY23	Q1FY24
Cost / Income	60.2%	63.7%	57.9%	55.7%	CASA	19.4%	22.8%	21.4%	18.2%
ROA	1.0%	0.4%	1.6%	2.4%	CAR	24.2%	18.6%	19.8%	20.6%
ROE	8.9%	4.1%	19.4%	29.2%	Tier - 1	21.5%	16.2%	18.1%	19.0%

Per Share Data	FY21	FY22	FY23	Q1FY24*	Valuation Ratios	FY21	FY22	FY23	Q1FY24
EPS	2.0	1.1	5.9	10.1	P/E	29.3	56.4	10.2	5.9
BVPS	30.1	31.4	40.9	41.0	P/BV	2.0	1.9	1.5	1.5
Adjusted BVPS	20.1	18.6	30.3	33.6	P/ABV	3.0	3.2	2.0	1.8

Source: Company data, NBRR

*Annualised figures

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