



**IPO NOTE**

**ESAF Small Finance Bank  
Ltd**

**02<sup>nd</sup> November 2023**

## Company Overview

Incorporated in 1995, the promoter group ESAF Financial Holdings Private Ltd. was granted the RBI In-Principle Approval to establish a Small Finance Bank (SFB) on October 7, 2015. Later, the bank was incorporated as 'ESAF Small Finance Bank Limited' on May 5, 2016, in Thrissur, Kerala. Subsequently, it commenced business as a small finance bank on March 10, 2017. It is included in the second schedule to the RBI Act, pursuant to a notification dated November 12, 2018, issued by the RBI. ESAF is an SFB focusing on unbanked and under-banked customer segments, especially in rural and semi-urban centres. The bank's advances comprise (a) Micro Loans, which comprise Microfinance Loans and Other Micro Loans; (b) retail loans, which include gold loans, mortgages, personal loans, and vehicle loans; (c) MSME loans; (d) loans to financial institutions; and (e) agricultural loans. Its liability products comprise current accounts, savings accounts, term deposits and recurring deposits. It has a network of 700 banking outlets (including 59 business correspondent-operated banking outlets), 767 customer service centres (which are operated by its 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 the bank's operations are spread across India, its business is concentrated in South India, particularly in Kerala and Tamil Nadu. As at June 30, 2023, 62.4% of its banking outlets are located in South India (including 43.4% in Kerala and 13.9% in Tamil Nadu), 73.1% of its gross advances are from customers in South India (including 43.5% from Kerala and 22.1% from Tamil Nadu), and 86.9% of its deposits are from banking outlets in South India (including 80.0% from Kerala and 3.4% from Tamil Nadu). The SFB use business correspondent entities to source and service customers for Micro Loans. Its business correspondents also source customers for mortgage loans, vehicle loans, MSME loans, agricultural loans and select deposit products. In addition, their business correspondents are responsible for sourcing and servicing their banking agents. Its business model focuses on the principles of responsible banking, providing customer-centric products and services through the innovative application of technology.

## Objects of the issue

The net proceeds from the fresh issue will be used towards the following purposes:

- To augment the Bank's Tier-1 capital base to meet future capital requirements.

## Investment Rationale

### Primary focus on rural and semi-urban banking franchise

ESAF SFB mainly focuses on providing loans to customers in rural and semi-urban centres. Its customers in rural and semi-urban centres (combined) have increased from 3.0 million as at March 31, 2021, to 3.9 million as at March 31, 2023, and further increased to 4.1 million as at June 30, 2023. As at June 30, 2023, its gross advances in rural and semi-urban centres (combined) were Rs. 90,951.76 million, representing 63.0% of the gross advances. As at June 30, 2023, 4.1 million of the customers were in rural and semi-urban centres (combined), representing 56.9% of the total customers, and the number of banking outlets in rural and semi-urban centres (combined) was 502, representing 71.7% of its entire banking outlets. Since April 2020, the bank has considerably expanded the number of states and territories of operations. In FY21, they expanded their operations to Meghalaya, Uttar Pradesh, Haryana, Tripura and Chandigarh by opening banking outlets and/or appointing business correspondents for these states/union territories. In FY22, the bank expanded its operations to Uttarakhand by establishing a business correspondent for that state. In FY23, they opened branches in Tripura and Uttarakhand for the first time. The SFB intends to deepen its distribution within the states and union territories it operates by opening additional branches, having business correspondents open more customer service centres, entering into relationships with new business correspondent entities and business facilitators and adding ATMs.

Issue Details	
Offer Period	3 <sup>rd</sup> Nov, 2023 - 07 <sup>th</sup> Nov, 2023
Price Band	Rs. 57 to Rs. 60
Bid Lot	250
Listing	BSE & NSE
Issue Size (no. of shares in mn)	77.4
Issue Size (Rs. in bn)	4.63
Face Value (Rs.)	10
Issue Structure	
QIB	50%
NIB	15%
Retail	35%
BRLM	ICICI Sec, DAM Capital, Nuvama Wealth Management
Registrar	Link Intime India Pvt. Ltd.

Particulars	Pre Issue %	Post Issue %
Promoter	74.43%	62.64%
Public	25.57%	37.36%
<b>Total</b>	<b>100.00</b>	<b>100.00</b>

(Assuming issue subscribed at higher band)

## Customer connections driven by its customer-centric products and servicing other non-financial services

ESAF SFB's products and services are designed to meet the various lifecycle needs of 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. An example of its customer-centric approach is that its Micro Loans can be repaid weekly, fortnightly or monthly based on customer preferences. As at June 30, 2023, 55.3% of its Micro Loan customers repaid their loans weekly. In addition to providing financial services, their business correspondents undertake various non-financial services, including conducting financial literacy programmes, livelihood programmes, entrepreneurship training programmes and community engagement programmes. The bank recently launched three new loan products to assist their customers during the COVID-19 pandemic: (1) Income Generation Loan Top Up, which is a pre-approved loan and a variant of the Income Generation Loan and is targeted at customers who have an existing Income Generation loan; (2) Utdhan Loan Series 3 – Covid Care Loan, which was tailor-made to support the financial needs of customers adversely affected by the COVID-19 pandemic; and (3) Pratheeksha Kiran Loan, which was mainly for the restoration of livelihoods and households of customers impacted by the pandemic. Due to its customer-centric products and processes, they have high customer retention rates.

## Valuation and Outlook

India's financial inclusion has improved significantly from 2014 to 2021 as the adult population with bank accounts increased from 53% to 78% (Source: Global Findex Database) due to the Indian government's efforts to promote financial inclusion and the proliferation of supporting institutions. 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 bank, an NBFC, and one urban co-operating bank have received permission to set up small finance banks. Despite its larger contribution to GDP of 47%, the rural segment's share in credit remains relatively low at around 8-9% of the overall credit outstanding as of March 31, 2023. This provides a vast market opportunity for SFBs and other players present in the segment. With their microfinance experience, SFBs can manage local stakeholders and maintain operational efficiency. SFBs' cost of funds is substantially low as they are allowed to raise CASA deposits. This will also help it to lend at more reasonable rates to its customers, enhancing its cross-sell opportunity in terms of asset products, insurance, etc. ESAF SFB was the fifth largest SFB in India in terms of AUM as of June 30, 2023. Amongst the SFBs, ESAF posted the fastest AUM CAGR of 39% over FY2021-23 period. The SFB's capital adequacy ratio, which is the ratio of capital to risk-weighted assets and current liabilities, as at June 30, 2023, was 20.6%, which is the best asset quality amongst comparable peers as of June 30, 2023. **As the lender will utilise the net proceeds of the fresh equity shares issue to augment its Tier-I capital base, its capital adequacy will enhance and lead to a stable leverage position. At the current P/BV multiple of 1.6x, we believe the company is attractively valued and advise investors to "Subscribe" from a medium to long-term perspective.**

## Key Risks

- ESAF SFB faces challenges in the rural-focused Microfinance Loan business, including the high cost of reaching customers, potential customers' lack of financial and product awareness and vulnerability of household's income to local developments, which could adversely affect the business and financial condition, results of operations and cash flows.
- The SFB does not have much of a presence in Bihar, Uttar Pradesh, West Bengal, Odisha or Rajasthan, which are among the top 10 states for Microfinance Loan advances under management for the industry as at June 30, 2023. They do not have any customers in Jammu and Kashmir, Himachal Pradesh, and Manipur, which are three of the top five most underpenetrated states as at June 30, 2023.
- If the lender cannot secure funding on acceptable terms and at competitive rates when needed, it could adversely affect the business, financial condition, results of operations and cash flows.

## Income Statement (Rs. in millions)

Particulars	FY21	FY22	FY23	Q1FY24
<b>(I) Income</b>				
Interest Earned	16,412	19,399	28,537	8,987
Other Income	1,272	2,076	2,879	930
<b>Total</b>	<b>17,684</b>	<b>21,475</b>	<b>31,416</b>	<b>9,918</b>
<b>(II) Expenditure</b>				
Interest Expended	7,196	7,928	10,173	3,133
Operating Expenses	6,319	8,629	12,305	3,778
Provisions and Contingencies	3,116	4,371	5,914	1,707
<b>Total</b>	<b>16,630</b>	<b>20,928</b>	<b>28,392</b>	<b>8,618</b>
<b>(III) Profit</b>				
<b>Net Profit for the year (I - II)</b>	<b>1,054</b>	<b>547</b>	<b>3,023</b>	<b>1,300</b>
Add: Balance in Restated Profit and Loss Account brought forward from Previous Year	2,272	3,062	3,215	5,420
<b>(IV) Appropriations</b>				
Transfer to Statutory Reserve	263	137	756	0
Transfer to Capital Reserve	0	37	3	0
Transfer to/(from) Investment Fluctuation Reserve Account	0	221	59	0
Balance carried over to Restated Statement of Assets and Liabilities	3,062	3,215	5,420	6,720
<b>Total</b>	<b>3,326</b>	<b>3,610</b>	<b>6,238</b>	<b>6,720</b>
<b>(V) Earnings per equity share (Face value ₹ 10/- per share)</b>				
Basic (Rs.)	2.46	1.22	6.73	2.89
Diluted (Rs.)	2.46	1.22	6.71	2.89

Source: RHP, StoxBox

## Cash Flow Statement (Rs in millions)

Particulars	FY21	FY22	FY23	Q1FY24
Cash flow from operating activities	11,274	-5,845	-5,730	7,058
Cash flow from investing activities	-6,380	-9,818	-5,732	290
Cash flow from financing activities	6,533	12,588	4,014	-6,151
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>11,428</b>	<b>-3,075</b>	<b>-7,449</b>	<b>1,198</b>
<b>Cash and cash equivalents at the beginning of the period</b>	<b>6,760</b>	<b>18,188</b>	<b>15,113</b>	<b>7,664</b>
<b>Cash and cash equivalents at the end of the period</b>	<b>18,188</b>	<b>15,113</b>	<b>7,664</b>	<b>8,862</b>

Source: RHP, StoxBox

## Balance Sheet (Rs. in millions)

Particulars	FY21	FY22	FY23	Q1FY24
<b>Capital and Liabilities</b>				
Capital	4,495	4,495	4,495	4,495
Employee Stock Options Outstanding	0	48	59	58
Reserves and Surplus	9,026	9,573	12,597	13,896
Deposits	89,994	1,28,151	1,46,656	1,56,559
Borrowings	16,940	29,528	33,542	27,391
Other Liabilities and Provisions	2,932	5,281	4,888	5,561
<b>Total</b>	<b>1,23,387</b>	<b>1,77,076</b>	<b>2,02,237</b>	<b>2,07,959</b>
<b>Assets</b>				
Cash and Balances with Reserve Bank of India	16,181	13,007	7,395	8,213
Balances with Banks and Money at Call and Short Notice	2,011	2,112	275	655
Investments	19,321	40,703	48,885	48,821
Advances	81,676	1,16,370	1,39,243	1,43,216
Fixed Assets	1,385	1,595	1,879	1,873
Other Assets	2,814	3,289	4,558	5,182
<b>Total</b>	<b>1,23,387</b>	<b>1,77,076</b>	<b>2,02,237</b>	<b>2,07,959</b>
<b>Contingent Liabilities</b>				
Bills for Collection	0	0	0	0

Source: RHP, StoxBox

## Disclaimer Appendix

Analyst (s) holding in the Stock : Nil

### Analyst (s) Certification :

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