



SMC Ranking

★ ★ ☆ ☆ ☆ (2/5)

Issue Highlights

| Industry | Small Finance Bank |
|--|--------------------|
| Total Issue (Shares) - Offer for sale | 72,000,000 |
| Total Issue (Shares) - Fresh Issue | 84,848,485 |
| Net Offer to the Public | 156,848,485 |
| Employee Reservation Portion | 303,030 |
| EHL Shareholder Reservation Portion | 15,454,545 |
| Issue Size (Rs. Cr.) | 501-518 |
| Price Band (Rs.) | 32-33 |
| Offer Date | 20-Oct-20 |
| Close Date | 22-Oct-20 |
| Face Value | Rs.10 |
| Lot Size | 450 |

Issue Composition

| | In shares |
|-------------------------------------|-------------|
| Total Issue for Sale | 156,848,485 |
| QIB | 70,545,455 |
| NIB | 21,163,636 |
| Retail | 49,381,818 |
| Employee Reservation Portion | 303,030 |
| EHL Shareholder Reservation Portion | 15,454,545 |

About the Company

Incorporated in 1993, Equitas Small Finance Bank Ltd (ESFBL) is the largest small finance bank in India in Fiscal 2019 considering banking outlets and the 2nd largest small finance bank considering assets under management and total deposits. Unlike other microfinance companies, it has a diversified loan portfolio and less dependence on microfinance business. With the main focus on financially unserved and underserved customers, the bank offers a wide range of banking products and services. The company provides microfinance loans promoting financial inclusion, housing finance, vehicle finance, and MSE finance. Equitas Small Fin Bank offers financial products according to customers' income profile, type of security available and nature of business. Apart from this, the bank also provides current accounts, salary accounts, savings accounts, other deposit accounts, ATM-cum-debit cards, mutual fund products, third party insurance, and issuance of FASTags. ESFBL follows credit assessment procedures through a risk management framework which is analyzed by its Risk Management Committee. As on 30th Sep 2019, it has the largest distribution channel among Small Finance Banks (SFBs) including 853 Banking Outlets and 322 ATMs in India across 15 states and union territories.

Strength

Customer centric organization with a deep understanding of the unserved and underserved customer segments: Bank's strength lies in promoting financial inclusion within unserved and underserved customer segments, beginning from their operations in 2007 as an NBFC providing microfinance loans through EMFL. They have also been providing vehicle finance and MSE finance through the Erstwhile NBFC that received its asset finance license in 2012, primarily to economically disadvantaged households. ESFB has gained a deep understanding of the market over the years that enable them to meet the financing requirements of potential customers. ESFB disbursed "priority sector loans" to 93,196 customers as of June 30, 2020. Further, as of June 30, 2020, advances to the unserved and underserved segments represented 89.12% of their Gross Advances (including IBPC issued). Bank's engagement with its target customer segments and understanding of related socio-economic dynamics allows them to establish effective credit and operational procedures, identify potential market demand, and leverage their existing operating network to introduce new products, increase the customer base, and grow their product portfolio

Among the largest SFBs in India with a well-diversified asset portfolio: ESFB is the largest SFB in India in terms of number of banking outlets, as of March 31, 2019, and in Fiscal 2019 they recorded the 4 th lowest yields indicating their diversification away from microfinance. Their asset products include provision of small business loans comprising LAPs, housing loans, agriculture loans, microfinance to JLGs, used and new commercial vehicle loans, gold loans, MSE loans, and corporate loans. Within their credit portfolio, the small business loans (including housing loan) and vehicle finance product segments recorded significant growth with a CAGR of 53.34% and 29.62%, respectively, from March 31, 2018 to March 31, 2020.

Strong retail liability portfolio with a strategic distribution network: The bank offers a variety of demand deposits and savings bank account options including deposits and other services through which its customers can realize their savings goals. Its retail deposit base has grown at a CAGR of 143.53% from ₹642.63 crore as of March 31, 2018 to ₹4,377.12 crore as of June 30, 2020. The ratio of its retail deposits to total deposits for the 3 months ended June 30, 2020 was 46.40. Demand deposits, savings account and term deposits represented 2.80%, 17.17%, and 80.03% of the total deposits, respectively, as of June 30, 2020. As of June 30, 2020, ESFB had 856 Banking Outlets and 322 ATMs spread across 17

Shareholding Pattern (%)

| Particulars | Pre-issue | Post-issue |
|-------------------------------------|----------------|----------------|
| Promoters & promoters group | 95.49% | 82.05% |
| QIB | 4.51% | 10.37% |
| NIB | 0.00% | 1.86% |
| Retail | 0.00% | 4.34% |
| Employee Reservation Portion | | 0.03% |
| EHL Shareholder Reservation Portion | | 1.36% |
| Total | 100.00% | 100.00% |

*calculated on the upper price band

Objects of the Issue

The bank proposes to utilize the Net Proceeds from the fresh issue offer towards augmenting the Bank's Tier I capital base to meet the future capital requirement.

Book Running Lead Manager

- JM Financial Limited
- Edelweiss Financial Services Limited
- IIFL Securities Limited

Name of the registrar

- KFin Technologies Private Limited

states and union territories in India. In the 3 months ended June 30, 2020, the bank has recorded an average of 1,146 transactions per month per ATM, and an average of 78% of such transactions were by customers of other banks. In Fiscal 2019, 2020 and the 3 months ended June 30, 2020, the average debit card spend was ₹271.89 crore, ₹112.02 crore and ₹51.39 crore, respectively.

Customized credit assessment procedures for effective credit risk management: ESFB applies different credit assessment procedures based on the products they offer. It also has a risk management framework to identify, measure, monitor and manage credit, market and operational risks including IT security risk. Its risk management and credit evaluation processes, together with their ability to evaluate risk, have enabled them to contain their level of NPAs, restructured standard asset and special mention accounts category 2 levels. As of June 30, 2020, the Gross NPAs were ₹416.67 crore, or 2.68% of the Gross Advances (including IBPC issued), and Net NPAs were ₹213.37 crore, or 1.48% of the net Advances.

Technology as an enabler to drive operating procedures: ESFB has created a paperless onboarding process for originating microfinance loans, opening savings bank accounts and fixed deposits. The bank has also deployed API integration software to increase operating efficiencies between their various applications. As a result, it has been able to collaborate with fintech companies to enable them to provide their services by monetizing the digital assets and back-end operations.

Strategy

Leveraging on the existing network for deepening penetration and driving operational efficiency: ESFB intends to leverage the functions to further grow their banking operations. In order to achieve this, it intends to further cross-sell its liability products such as recurring deposits to its asset side customers primarily comprising microfinance customers. It also intends to increase distribution of third party products by offering and marketing them across all their channels, including Banking Outlets and digital channels. Its aim is to reduce the Cost to Income ratio which was 66.38% and 67.27% as of March 31, 2020 and June 30, 2020, respectively, by leveraging their existing infrastructure of Banking Outlets and large customer base to crosssell their range of products.

Strengthen liability franchise and focus on increasing their retail base to further improve cost of funds: As of June 30, 2020, ESFB had a liability customer base of 0.90 million customers. It intends to further strengthen its liability franchise with a focus on growing its retail deposit and CASA deposit base to provide them with a stable and low-cost source of funding. ESFB aims to achieve this by attracting greater retail deposits from their customer segments, and particularly the mass and mass-affluent customer segments. The bank has recently launched differentiated CASA products for various types of customers, such as the 'Wings Account' for mass-affluent depositors, 'Namma Account' for retail informal and semiformal customers, and 'Elite Programme' for higher income households. As of June 30, 2020, its deposit base of ₹11,787.13 crore represented 68.08% of its overall funding profile. ESFB introduced an online account called 'Selfie Digital Savings Account', which enables potential customers to open a bank account online.

Leverage data for analytics to drive operational efficiency: ESFB intends to continue to invest in technology as a means of improving its customers' banking experience and offer them a range of products tailored to their financial needs. ESFB intends to develop such tailored products with the help of data analytics. The bank is in the process of building data driven crossselling models to identify and tap into opportunities within its existing customer base. ESFB also propose to capitalize on the opportunity it presents, in terms of aggregating data to derive business intelligence including banking trends in various communities, and leverage this to monitor business performance at a unit level with limited manual intervention.

Continue to focus on digital products and technology to grow operations: ESFB intends to leverage its technological capabilities to access greater number of mass and mass-affluent customers for retail deposits through their mobile banking application. It also proposes to develop products that will be available only on its digital platforms, specifically designed for the younger and technologically advanced customer base. These products will be customized in terms of the user interface to deliver specialized experiences.

Continue to diversify product offerings and leverage cross-selling opportunities: ESFB's primary focus is to diversify its product offerings while growing its secured loan portfolio, comprising vehicle finance, agriculture loans, gold loans, microloans against property, working capital loans, and affordable housing loans. It intends to continue to develop and offer a comprehensive range of products anchored around the unserved and underserved customer segments, that will help them attract new customers and deepen their relationship with their existing customer base. In addition to expanding its product portfolio, ESFB intends to strengthen its alternate delivery channels and increase its adoption by encouraging customers to move from less cash to a cashless environment. It intends to achieve this by focusing on its existing internet banking system and mobile banking platform.

Increasingly focus on non-interest income sources: An important strategic focus for ESFB is to diversify its fee and non-fund based revenues. Its intends to achieve this by further cross-selling existing fee income products like distribution of mutual funds and insurance products, and introducing newer products and services. It has engaged with car dealers for issuance of 'FASTag', a selfservice application for toll booths. It intends to build on this income source and engage with more number of car dealers across India for issuance of similar products.

Risk Factor

- The business of the bank is subject to stringent regulatory requirements and prudential norms and its inability to comply with such laws, regulations and norms may have an adverse effect on its business, results of operations, financial condition and cash flows.
- Any adverse developments in the segments it operates in, including small business loans, microfinance and vehicle finance could adversely affect its business and results of operations.
- The bank has a continuous requirement of funds and its inability to access sources of funds in an acceptable and timely manner or any disruption in the access to funds would adversely impact its results of operations, financial condition and cash flows.
- A significant portion of its advances are towards customers located in the State of Tamil Nadu and any adverse changes in the conditions affecting the region can adversely impact our business, financial condition, results of operations and cash flows.
- The deposits of banks are depended on a limited number of customers and a loss of such customers could materially and adversely affect its deposit portfolio, funding sources, financial condition, results of operations and cash flows.

Peer comparison

| Company | Total Income | PAT | EPS | P/E | P/BV | BV | FV | Price | Mcap |
|----------------------------------|--------------|---------|--------|-------|------|---------|----|---------|----------|
| AU Small Finance Bank Ltd | 5017.15 | 890.73 | 80.17 | 16.29 | 2.17 | 601.06 | 10 | 1306.05 | 14510.22 |
| Ujjivan Small Finance bank | 16759.76 | 2194.08 | 86.70 | 7.69 | 0.86 | 775.88 | 10 | 666.60 | 16869.08 |
| DCB Bank | 8792.97 | 1169.85 | 14.27 | 17.49 | 2.50 | 100.04 | 2 | 249.65 | 20462.57 |
| City Union Bank | 6169.00 | 961.22 | 145.63 | 5.88 | 0.76 | 1124.71 | 10 | 856.35 | 5652.28 |
| Bandhan Bank | 4865.97 | 444.71 | 6.02 | 23.56 | 1.98 | 71.72 | 1 | 141.85 | 10474.22 |
| Shriram City Union Finance Ltd | 3933.97 | 336.25 | 10.83 | 6.99 | 0.74 | 102.55 | 10 | 75.75 | 2351.78 |
| Shriram Transport Finance Ltd | 12501.30 | 1399.64 | 9.74 | 13.30 | 1.06 | 121.88 | 2 | 129.55 | 16006.29 |
| Cholamandalam Invest. & Fin. Ltd | 1491.60 | 317.10 | 49.30 | 11.38 | 1.37 | 408.29 | 10 | 561.05 | 3608.42 |
| M&M Fin. Services Limited | 5233.55 | 685.27 | 22.36 | 33.07 | 5.24 | 141.16 | 10 | 739.50 | 22668.29 |
| Sundaram Finance limited | 1948.65 | 309.72 | 19.93 | 34.23 | 3.00 | 227.39 | 10 | 682.30 | 10604.82 |
| CreditAccess Grameen limited | 12877.20 | 2769.94 | 17.20 | 18.65 | 3.40 | 94.36 | 10 | 320.70 | 51644.60 |
| Spandana Sphoorty Fin. Ltd. | 2365.94 | 217.46 | 1.26 | 24.80 | 1.82 | 17.16 | 10 | 31.25 | 5400.70 |
| Equitas Small Finance Bank Ltd* | 1495.30 | 243.65 | 2.14 | 15.42 | 1.22 | 27.08 | 10 | 33.00 | 3756.23 |

*FY20 financials are taken for valuation

Valuation

Considering the P/E valuation on the upper end of the price band of Rs. 33, the stock is priced at pre issue P/E of 14.27x on its FY20 EPS of Rs. 2.31. Post issue, the stock is priced at a P/E of 15.42x on its EPS of Rs. 2.14. Looking at the P/B ratio at Rs. 33 the stock is priced at P/B ratio of 1.24x on the pre issue book value of Rs.26.60 and on the post issue book value of Rs. 27.08 the P/B comes out to 1.22x.

On the lower end of the price band of Rs.32 the stock is priced at pre issue P/E of 13.84x on its FY20 EPS of Rs. 2.31. Post issue, the stock is priced at a P/E of 14.95x on its EPS of Rs. 2.14. Looking at the P/B ratio at Rs. 32, the stock is priced at P/B ratio of 1.20x on the pre issue book value of Rs. 26.60 and on the post issue book value of Rs. 27.08, the P/B comes out to 1.18x.

Industry overview

In order 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. Further, a few microfinance companies, local area banks and NBFCs have received permission to set up SFBs. SFBs are allowed to take deposits, which provide them an edge of having lower cost of funds in comparison with NBFCs. MFIs turned into SFBs are now diversifying their advances mix, and focusing on other retail and corporate lending business. It is expected that the loan portfolio of SFBs will grow at a CAGR of approximately 25% in the near term due to support from (i) significant market opportunities in the rural segment; (ii) new product offerings and cross-selling opportunities with the ability to cross-sell products on the liability side and asset side to improve customer stickiness and loyalty; (iii) higher presence of informal credit channels; (iv) geographic diversification; (v) ability to manage local stakeholders, (vi) access to low cost funds, and (vii) loan recovery and control on NPAs. Going forward, it is expected that deposits of SFBs will grow at a CAGR between 60% to 65% from Fiscal 2019 to Fiscal 2022, as players focus on promoting convenient banking habits in order to make it accessible to the last mile and enhance financial inclusion. In addition, few players are also contemplating capital injections to grow asset size and deepen their penetration in untapped geographies by expanding their network of branches/ banking outlets.

Outlook

Equitas SFB over the last few years has reduced its dependency on the Micro Finance Loans and has diversified into other products also. However, the benefit of the same still does not reflect in the financial performance, which is evident from its low ROA and ROE. Also the competitive intensity and asset quality issues are likely to persist in the medium term, in this scenario a significant improvement in the return ratios is very unlikely. In terms of valuations the issue is offered at a discount to other SFBs and that keeps the downside limited for the stock, however rerating in the stock will be a function in the improvement in asset quality and Return ratios going ahead.

An Indicative timetable in respect of the Issue is set out below:

| EVENT | INDICATIVE DATE (On or about) |
|--|----------------------------------|
| Bid/Offer Opens Date | October 20, 2020 |
| Bid/Offer Closing Date | October 22, 2020 |
| Finalisation of Basis of Allotment with the Designated Stock Exchange | October 27, 2020 |
| Initiation of refunds (if any, for Anchor Investors)/unblocking of funds from ASBA Account | October 28, 2020 |
| Credit of Equity Shares to depository accounts of Allottees | October 29, 2020 |
| Commencement of trading of the Equity Shares on the Stock Exchanges | November 02, 2020 |

Annexure

Consolidated Financials

Profit & Loss

Rs. in Cr.

| Particulars | Period ended 30-Jun-20 (6 Months) | Period ended 31-Mar-20 (12 Months) | Period ended 31-Mar-19 (12 Months) |
|------------------------------|--------------------------------------|---------------------------------------|---------------------------------------|
| Interest Earned | 721.31 | 2,645.44 | 2,111.93 |
| Interest expended | 317.03 | 1,150.14 | 960.20 |
| Operating Income | 404.28 | 1,495.30 | 1,151.73 |
| Operating expenses | 291.92 | 1,180.08 | 1,008.49 |
| Operating Profit | 112.36 | 315.22 | 143.24 |
| OPM% | 15.58 | 11.92 | 6.78 |
| Other Income | 29.66 | 282.35 | 282.90 |
| PBDIT | 142.02 | 597.58 | 426.14 |
| Provisions and contingencies | 84.35 | 353.93 | 215.58 |
| PBT | 57.67 | 243.65 | 210.56 |
| Tax | 0.00 | 0.00 | 0.00 |
| Profit after tax | 57.67 | 243.65 | 210.56 |

Balance sheet is on next page

Balance Sheet

Rs. in Cr.

| Particulars | As on 30-Jun-20 | As on 31-Mar-20 | As on 31-Mar-19 |
|--|-----------------|-----------------|-----------------|
| Assets | | | |
| Cash and Balances with Reserve Bank of India | 429.02 | 380.86 | 402.70 |
| Balances with Banks and Money At Call and Short Notice | 1496.55 | 2155.98 | 857.91 |
| Investments | 3478.58 | 2342.51 | 2344.45 |
| Advances | 14388.62 | 13747.24 | 11593.57 |
| Fixed Assets | 197.66 | 212.77 | 237.34 |
| Other Assets | 901.71 | 475.19 | 326.72 |
| Total Assets | 20892.14 | 19314.55 | 15762.69 |
| Liabilities | | | |
| Deposits | 11787.13 | 10788.41 | 9006.74 |
| Borrowings | 5525.53 | 5134.87 | 3973.03 |
| Other Liabilities and Provisions | 777.66 | 647.12 | 528.61 |
| Total | 18090.32 | 16570.40 | 13508.37 |
| NET Worth | 2801.82 | 2744.15 | 2254.32 |
| Net worth represented by: | | | |
| Share capital | 1053.40 | 1053.40 | 1005.94 |
| Reserves and surplus | 1748.42 | 1690.75 | 1248.38 |
| Net Worth | 2801.82 | 2744.15 | 2254.32 |

RANKING METHODOLOGY

| | |
|-----------|-------|
| WEAK | ★ |
| NEUTRAL | ★★ |
| FAIR | ★★★ |
| GOOD | ★★★★ |
| EXCELLENT | ★★★★★ |

E-mail: smc.care@smcindiaonline.com



Moneywise. Be wise.

Corporate Office:
11/6B, Shanti Chamber,
Pusa Road, New Delhi - 110005
Tel: +91-11-30111000
www.smcindiaonline.com

Mumbai Office:
Lotus Corporate Park, A Wing 401/402, 4th Floor,
Graham Firth Steel Compound, Off Western
Express Highway, Jay Coach Signal, Goreagon
(East) Mumbai - 400063
Tel: 91-22-67341600, Fax: 91-22-67341697

Kolkata Office:
18, Rabindra Sarani, Poddar Court, Gate No-4,
5th Floor, Kolkata - 700001
Tel.: 033 6612 7000/033 4058 7000
Fax: 033 6612 7004/033 4058 7004

SMC Global Securities Ltd. (hereinafter referred to as "SMC") is regulated by the Securities and Exchange Board of India ("SEBI") and is licensed to carry on the business of broking, depository services and related activities. SMC is a registered member of National Stock Exchange of India Limited, Bombay Stock Exchange Limited, MSEI (Metropolitan Stock Exchange of India Ltd) and M/s SMC Comtrade Ltd is a registered member of National Commodity and Derivative Exchange Limited and Multi Commodity Exchanges of India and other commodity exchanges in India. SMC is also registered as a Depository Participant with CDSL and NSDL. SMC's other associates are registered as Merchant Bankers, Portfolio Managers, NBFC with SEBI and Reserve Bank of India. It also has registration with AMFI as a Mutual Fund Distributor.

SMC is a SEBI registered Research Analyst having registration number INH100001849. SMC or its associates has not been debarred/ suspended by SEBI or any other regulatory authority for accessing /dealing in securities market. SMC or its associates or its Research Analyst or his relatives do not hold any financial interest in the subject company interest at the time of publication of this Report. SMC or its associates or its Research Analyst or his relatives do not hold any actual/beneficial ownership of more than 1% (one percent) in the subject company, at the end of the month immediately preceding the date of publication of this Report. SMC or its associates its Research Analyst or his relatives does not have any material conflict of interest at the time of publication of this Report.

SMC or its associates/analyst has not received any compensation from the subject company covered by the Research Analyst during the past twelve months. The subject company has not been a client of SMC during the past twelve months. SMC or its associates has not received any compensation or other benefits from the subject company covered by analyst or third party in connection with the present Research Report. The Research Analyst has not served as an officer, director or employee of the subject company covered by him/her and SMC has not been engaged in the market making activity for the subject company covered by the Research Analyst in this report.

The views expressed by the Research Analyst in this Report are based solely on information available publicly available/internal data/ other reliable sources believed to be true. SMC does not represent/ provide any warranty expressly or impliedly to the accuracy, contents or views expressed herein and investors are advised to independently evaluate the market conditions/risks involved before making any investment decision. The research analysts who have prepared this Report hereby certify that the views /opinions expressed in this Report are their personal independent views/opinions in respect of the subject company.

Disclaimer: This Research Report is for the personal information of the authorized recipient and doesn't construe to be any investment, legal or taxation advice to the investor. It is only for private circulation and use. The Research Report is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon as such. No action is solicited on the basis of the contents of this Research Report. The Research Report should not be reproduced or redistributed to any other person(s) in any form without prior written permission of the SMC. The contents of this material are general and are neither comprehensive nor inclusive. Neither SMC nor any of its affiliates, associates, representatives, directors or employees shall be responsible for any loss or damage that may arise to any person due to any action taken on the basis of this Research Report. It does not constitute personal recommendations or take into account the particular investment objectives, financial situations or needs of an individual client or a corporate/s or any entity/s. All investments involve risk and past performance doesn't guarantee future results. The value of, and income from investments may vary because of the changes in the macro and micro factors given at a certain period of time. The person should use his/her own judgment while taking investment decisions. Please note that SMC its affiliates, Research Analyst, officers, directors, and employees, including persons involved in the preparation or issuance of this Research Report: (a) from time to time, may have long or short positions in, and buy or sell the securities thereof, of the subject company(ies) mentioned here in; or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the subject company(ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender/borrower to such subject company(ies); or (c) may have any other potential conflict of interest with respect to any recommendation and related information and opinions. All disputes shall be subject to the exclusive jurisdiction of Delhi High court.