EQUITAS SMALL FINANCE BANK LIMITED

20-Oct-20

Subscribe (Long Term)

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Issue Details

Issue Details	
Issue Size (Value in ` crore, Upper Band)	517.60
Fresh Issue (No. of Shares in Lakhs)	848.48
Offer for Sale (No. of Shares in Lakhs)	720.00
Employee Reservation Portion (Value in crore)	1.00
Bid/Issue opens on	20-Oct-20
Bid/Issue closes on	22-Oct-20
Face Value	Rs. 10
Price Band	32-33
Minimum Lot	450

Note: *The EHL shareholder reservation is 10% of the offer size.*

Objects of the Issue

The Fresh Issue (₹280 Cr)

The company proposes to utilize the Net Proceeds towards augmenting its Tier – 1 capital base to meet future capital requirements.

Offer for Sale (₹237.60 Cr)

The company will not receive any proceeds from the Offer for Sale.

Book Running Lead Manager
JM Financial Limited
Edelweiss Financial Services Limited
IIFL Securities Limited
Registrar to the Offer
KFin Technologies Private Limited

Capital Structure (₹ Crore, at Upper Band)	Aggregate Value
Authorized share Capital	1700.00
Subscribed paid up Capital (Pre-Offer)	1053.40
Paid up capital (Post - Offer)	1138.25

Share Holding Pattern %	Pre Issue	Post Issue
Promoters & Promoter group	95.5%	82.1%
Public	4.5%	17.9%
Total	**100%**	**100%**

Financials

Particulars (₹ Cr)	Q1-FY21	FY20	FY19	FY18
Interest Earned	721.3	2645.4	2111.9	1531.7
Interest Expended	317.0	1150.1	960.2	671.1
Net Interest Income	404.3	1495.3	1151.7	860.5
Other Income	29.7	282.4	282.9	241.2
Total Income	433.9	1777.7	1434.6	1101.8
Operating Expenses	291.9	1180.1	1008.5	881.1
Pre Provision Profit	142.0	597.6	426.1	220.6
Provisions & Contingencies	68.3	246.6	102.4	172.5
PBT	73.7	350.9	323.7	48.1
Tax	16.0	107.3	113.2	16.3
PAT	57.7	243.6	210.6	31.8
EPS	0.5	2.3	2.0	0.3

Company Description

Equitas Small Finance Bank Limited (Equitas SFB) is one of the leading players in the small finance bank (SFB) space in India, catering the mass market focused on "financially unserved and underserved segments" and committed to promoting financial inclusion in the country. During FY19, Equitas SFB ranked as the largest SFB in India in terms of number of banking outlets, and the second largest SFB in terms of assets under management (AUM) and total deposits. Notably, the company had a market share of 16% in terms of AUM in FY19. The company offers a diversified portfolio of products comprising small business loans, micro finance, vehicle finance, MSE finance, corporates and others.

Equitas SFB was incorporated as V.A.P. Finance Private Limited on June 21, 1993 at Madras, Tamil Nadu. The company commenced operations as an SFB on Sep 5, 2016, post receipt of the Reserve Bank of India (RBI) approval. Prior to this, the company operated as an NBFC – asset finance company carrying out vehicle finance and MSE finance business as a wholly-owned subsidiary of its Promoter Equitas Holdings Ltd. (EHL). Complying with regulatory requirement to operate as an SFB, the other two erstwhile subsidiaries of EHL, namely Equitas Micro Finance Ltd. (EMFL) and Equitas Housing Finance Ltd. (EHFL), were merged with the erstwhile NBFC to form Equitas SFB.

The IPO of Equitas SFB comes primarily as an effort by the management to meet with the listing norm of the RBI that calls for mandatory listing of SFBs within three years from the date of reaching a net worth of ₹500 crores. For Equitas EFB, it was three years from the date of commencement of operations as an SFB, i.e., on or prior to Sep 4, 2019, as the combined net worth of the erstwhile NBFC, EMFL and EHFL was in excess of ₹500 crores. The company was unable to meet the timeline and upon request to the RBI, the timeline was extend to first week of Nov 2020. Also, promoter EHL is required to reduce its shareholding in Equitas SFB to 40% of its paid-up equity share capital within a period of five years from the date of commencement of its business as an SFB, and further reduce to 30% and 26% within a period of 10 years and 12 years, respectively, from the date of commencement of business. Notably, post IPO, the promoter's stake will reduce to 82.1% from its current 95.5% stake.

With strong presence across 17 states and union territories, Equitas SFB's distribution channels included 856 banking outlets and 322 ATMs, as of Jun 30, 2020.

Reflecting solid growth, the company's gross advances grew from ₹7,937 crore as of Mar 31, 2018 to ₹15,367 crore as of Mar 31, 2020 and stood at ₹15,573 crore as of Jun 30, 2020. Also, deposits increased from ₹5,604 crore as of Mar 31, 2018 to ₹ 10,788 crore as of Mar 31, 2020 and came in at ₹11,787 crore as of Jun 30, 2020. As of Jun 30, 2020, percentage of gross NPAs to gross advances was 2.68% and net NPAs to Net Advances was 1.48%, decreasing from 2.73% and 1.56%, respectively, in the previous year period.

Driven by decent loan growth, net interest income increased 29.8% yoy to ₹1,495 crore in FY20 while Net interest margin improved to 9.11% from 8.55% in the previous year. PAT increased 15.7% yoy to ₹244 crore in FY20. Among several strategies to drive growth, Equitas SFB is focused on diversifying its product portfolio, growing retail deposit base for low cost funding, deepening penetration in existing markets and leveraging technology to improve overall operational efficiencies.

Valuation

At upper price band of ₹33, the IPO is priced at 1.25 times post issue FY20 book value (BV). Valuation looks attractive when compared with peers like AU SFB (5.35x FY20 BV) and Ujjivan SFB (1.89x). While the operating environment remains challenging amid the COVID-19 pandemic, recent collection efficiency and moratorium position signals an improving trend. We remain positive on Equitas SFB given its diversified loan portfolio, well-managed asset quality, strong capital position, extensive distribution network and healthy growth prospects of the SFB industry. We recommend **Subscribe (Long Term horizon)** to this IPO.

Operating environment remains challenging amid pandemic, however, collection efficiency and moratorium position reflects an improving trend:

Owing to the COVID-19 induced nation-wide lockdown from March 25, 2020 to May 31, 2020 and various regulatory measures including moratorium, Equitas SFB witnessed a decline in collections, lower disbursements, reduced deposit mobilization and increased provisioning. The current environment remains challenging amid the pandemic and the asset quality and operations of the company might get impacted owing to any further extension of measures such as moratorium or restructuring of MSE loans without a downgrade in the asset classification. However, on a positive note, the latest information on the company's collection efficiency and moratorium reflects an improving trend.

Collection efficiency is calculated as the aggregate EMI amounts collected in the relevant period divided by the total amount due for collection in such period. In the below table, the company has taken into account aggregate collection in its micro finance business (including those relating to any micro finance loans disbursed subsequent to April 1, 2020) and has excluded any collection relating to any other loans for disbursements subsequent to April 1, 2020.

Asset Products	March	April	May	June	July	August
Small Business Loans	72.81%	17.03%	15.91%	60.55%	66.27%	105.02%
Micro Finance	77.41%	0.08%	6.57%	42.21%	61.23%	7.09%**
Vehicle Finance	80.52%	13.04%	14.11%	42.02%	48.40%	71.52%
MSE Finance*	34.50%	21.50%	20.50%	19.50%	21.00%	41.03%**
Corporate	99.25%	67.12%	33.33%	91.79%	88.07%	96.26%
Total	**78.13%**	**10.96%**	**12.30%**	**49.38%**	**60.50%**	**83.42%**

*****Excludes working capital loans (CC/OD) and loans classified as others, i.e. loan-against-gold, unsecured business loans, overdrafts against fixed deposits and staff loans*
***Excludes foreclosures*

Moratorium information for a particular month is calculated as the aggregate value of EMIs due in a particular month that have not been repaid, divided by Gross Advances (including IBPC (Inter-Bank Participation Certificate) issued) as of the dates indicated below. Moratorium option exercised by the company's customers are as follows:

Asset Products	Jun-20	Jul-20	Aug-20
	Value of EMIs due that have not been paid in the month of June 2020, as a % of Gross Advances (including IBPC issued) as of March 31,2020	Value of EMIs due that have not been paid in the month of July 2020, as a % of Gross Advances (including IBPC issued) as of June 30, 2020	Value of EMIs due that have not been paid in the month of August 2020, as a % of Gross Advances (including IBPC issued) as of June 30, 2020
Small Business Loans	42.06%	39.17%	39.25%
Micro Finance	58.00%	41.60%	24.65%
New Commercial Vehicle Finance	65.82%	53.52%	46.56%
Used Commercial Vehicle Finance	74.40%	58.90%	54.57%
MSE Finance (including Working Capital)*	48.25%	40.59%	18.60%
Corporate	12.42%	13.65%	13.69%
Total	**51.17%**	**42.40%**	**36.24%**

**Moratorium information for MSE Finance segment (excluding working capital) was 62.40%, 52.12% and 61.03%, for June 2020, July 2020 and August 2020, respectively.*

Key Metrics:

Key Metrics	Q1-FY21	FY20	FY19	FY18
Net Interest Margin	8.88%*	9.11%	8.55%	9.02%
Yield on Advances	18.63%*	18.90%	19.13%	20.47%
Cost of Funds	7.96%*	7.97%	8.13%	8.36%
Spread	10.67%*	10.93%	11.00%	12.11%
Cost to Income Ratio	67.27%	66.38%	70.30%	79.97%
GNPA Ratio	2.68%	2.72%	2.53%	2.68%
Net NPA to net Advance	1.48%	1.66%	1.44%	1.46%
Provision coverage ratio	48.79%	45.22%	43.38%	47.07%
Credit to Deposit ratio	189.23%	190.53%	174.98%	181.28%
CASA Ratio	24.49%	20.47%	25.25%	29.23%
CRAR	22.02%	23.61%	22.45%	29.60%
Common Equity Tier 1 Capital Ratio	21.04%	22.44%	20.93%	27.07%

**annualized*

Source: RHP, Anand Rathi Research

Business Highlights:

- ***One of the largest SFBs in India with a well-diversified portfolio***

During FY19, Equitas SFB ranked as the second largest SFB in terms of assets under management (AUM) and total deposits. Notably the company had a market share of 16% in terms of AUM in FY19. The company offers a diversified portfolio of products comprising small business loans, micro finance, vehicle finance, MSE finance, corporates and others. Notably, focusing on diversifying, the contribution from microfinance loan has reduced from 28% in March 2018 to 23% in June 2020.

Loan Mix as of Jun 30, 2020	(₹ Cr)	% of Total
Small Business Loans	**6,484**	**42%**
Small Business Loans	5,152	33%
Housing Finance	629	4%
Agriculture Loans	704	5%
Micro Finance	**3,618**	**23%**
Vehicle Finance	**3,776**	**24%**
Used Commercial Vehicles	2,628	17%
New Commercial Vehicles	1,149	7%
MSE Finance (Working Capital)	**712**	**5%**
Corporates	**772**	**5%**
Others*	**210**	**1%**
Gross Advances (including IBPC issued)	**15,573**	**100%**
Secured Advances (As % of Gross Advances, including IBPC issued)	**75.75%**	

**Others includes loan-against-gold, unsecured business loans, overdrafts against fixed deposits and staff loans.*

- ***Strong geographic footprint with extensive distribution network:***

Equitas SFB enjoys benefit from its strong geographic foot print through its multiplatform distribution network including banking outlets, ATMs, POS terminals, and various digital channels. During FY19, Equitas SFB ranked as the largest SFB in India in terms of number of banking outlets. As of Jun 30, 2020, the company had 856 banking outlets and 322 ATMs spread across 17 states and union territories in India. The company's rural banking outlets are used primarily for distribution of asset products while it distributes liability products through banking outlets located at urban and semi-urban areas. As the company's liability customers mainly belong to mass and mass-affluent segments, as of Jun 30, 2020, 54.23%, 33.79%, 9.88% and 2.10% of the total deposit were in metropolitan, urban, semi-urban and rural areas, respectively. While the loan portfolio of the company remains a bit concentrated in the South region, the deposit base is well diversified.

Region	Banking Outlets	Number of States/ Union Territories	% of Gross Advances	% of Total Deposits
North	210	10	15%	38%
West	204	2	17%	20%
South	442	5	68%	42%
East			0%	0%
Total	**856**	**17**	**100%**	**100%**

Northern region comprises Chandigarh, Chhattisgarh, Haryana, Himachal Pradesh, Madhya Pradesh, New Delhi, Punjab, Rajasthan, Uttar Pradesh and Uttarakhand
Western region comprises Gujarat and Maharashtra
Southern region comprises Goa, Karnataka, Kerala, Pondicherry, Andhra Pradesh, Telangana and Tamil Nadu
Eastern region comprises Assam, Bihar, Jharkhand, Meghalaya, Odisha, Tripura and West Bengal

- ***Continued increase in advances supports growth in interest income:***

In recent years, Equitas SFB has been able to consistently grow its advances on account of growth in most of its loan segments. While demonetization affected loan disbursements in FY17 and FY18, it significantly rebounded in FY19. Notably, driven by increase in advances, interest earned increased 37.9% and 25.3% in FY19 and FY20, respectively. According to the CRISIL Report, the loan portfolio of SFBs is expected to grow at a CAGR of 25% in the near term, largely supported by introducing new products and capitalizing on cross-selling opportunities. This signals for a healthy growth opportunity for players like Equitas SFB.

(₹ Cr)

Loan Category	FY18	FY19	FY20	Q1-FY20	Q1-FY21
Small Business Loans	2,671	4,577	6,279	4,926	6,484
Growth y/y		71%	37%		32%
Micro Finance	2,257	3,070	3,616	3,124	3,618
Growth y/y		36%	18%		16%
Vehicle Finance	2,238	2,951	3,760	3,055	3,776
Growth y/y		32%	27%		24%
MSE Finance (Working Capital)	8	181	669	280	712
Growth y/y		2273%	270%		154%
Corporates	250	456	818	526	772
Growth y/y		82%	79%		47%
Others	514	468	224	340	210
Growth y/y		-9%	-52%		-38%
Total Gross Advances (including IBPC issued)	**7,937**	**11,703**	**15,367**	**12,251**	**15,573**
Growth y/y		47%	31%		27%

Source: RHP, Anand Rathi Research

- ***Asset Quality remains well managed:***

  Equitas SFB's asset quality remains well managed on the back of its decent risk management and credit evaluation processes. As of Mar 31, 2018, 2019, 2020 and as of Jun 30, 2020, percentage of gross NPAs to its gross advances (including IBPC) was 2.68%, 2.53%, 2.72% and 2.68%, respectively, while percentage of net NPAs to net advances was 1.46%, 1.44%, 1.66% and 1.48%, respectively.

- ***Strong Capital position:***

  Equitas SFB has been able to maintain a strong capital position. As per SFB operating guideline, the company is required to maintain a minimum Capital-to-risk weighted asset ratio (CRAR) of 15.00%, including a minimum Tier I capital of at least 7.5%. As of Mar 31, 2018, 2019, 2020 and as of Jun 30, 2020, the company's capital to risk weighted asset ratio was 29.60%, 22.45%, 23.61%, and 22.02% respectively, while Tier I capital ratio was 27.07%, 20.93%, 22.44% and 21.04%, respectively, comfortably exceeding the regulatory requirement. Notably, the IPO should further boost its capital ratios as Equitas SFB intends to utilize the net proceeds towards augmenting its Tier – 1 capital base.

- ***Experienced Management team:***

  Equitas SFB's senior management team has significant experience in the financial services industry and has been instrumental in developing and implementing the company's business strategy. The company's Managing Director and CEO, Vasudevan Pathangi Narasimhan has over two decades of experience in the financial services sector in various capacities, including as head of consumer banking, and vice president and head of vehicle finance in different financial services entities. Further, the company's board consists of directors with a diverse mix of experience in various sectors, in particular, the financial services industry.

Key Strategies:

- ***Diversify product offerings and leverage cross-selling opportunities:***

  Equitas SFB remains focused on diversifying its product offerings while growing the secured loan portfolio, comprising vehicle finance, agriculture loans, gold-loans, microloans against property, working capital loans, and affordable housing loans. As the company's group loan customers are gradually meeting eligibility requirements for individual loan products, the company intends to capitalize on this development by diversifying its individual loan products. In particular, the company proposes to cross-sell its individual loans as well as liability products including current accounts, vendor accounts, cash management services, family accounts to MSE customers by targeting proprietors. Additionally, in effort to diversify its fee and non-fund based revenues, the company aims to further cross-selling existing fee income products like distribution of mutual funds and insurance products, and introducing newer products and services.

- ***Strengthen liability franchise and focus on increasing retail base to improve cost of funds:***

  Equitas SFB intends to strengthen its liability franchise with strong focus on growing the retail deposit base as it would provide the company with a stable, low-cost source of funding. As of Jun 30, 2020, the company's deposit base of ₹11,787 crore comprised 68.08% of its overall funding profile. Retail deposits formed 16.20% of total deposits as of Mar 31, 2018 and have grown to 44.42% as of Mar 31, 2020 and were 46.40 % of total deposits as of Jun 30, 2020. As a result, the cost of funds has been witnessing a reducing trend with 8.36%, 8.13%, 7.97% and 7.63% (annualized)/ 1.91% (unannualized) as of Mar 31, 2018, 2019, 2020 and Jun 30, 2020, respectively. The company intends to meet a majority of its funding requirements through CASA deposits and recurring and fixed deposits by building a sticky deposit base and targeting new customers whose primary avenues of savings and capital building currently include the unorganized sector and other high risk savings schemes.

- ***Leveraging existing distribution network to increase customer penetration and lower cost to income ratio:***

  Equitas SFB, over the years, made significant investments in expanding its network of banking outlets and associated support structures, including network of ATMs, technology infrastructure, and employee training activities. The company now intends to leverage these functions to further grow its banking operations and improve productivity across all channels. Also, the company looks to increase distribution of third party products by offering and marketing them across its channels. Through cross selling and leveraging the existing network infrastructure the company not only aims to deepen penetration in existing markets but reduce the cost to income ratio as well.

- ***Boost technology capabilities:***

  Equitas SFB is thrusting on technology and data analytics to boost overall operational efficiency and product innovation. For instance, the company intends to develop digital dashboards and other tools to efficiently track loans and monitor customer history and potential opportunities. Also, it intends to leverage its front-end technology platforms to further improve customer acquisition and transaction management.

Key Risks:

- Equitas SFB may witness deterioration in the asset quality as its target borrower segment primarily comprises unserved and underserved customers, who are most impacted due to the economic downturn caused by COVID-19. Further slowdown in economic activity amid the pandemic and extension of measures such as moratorium or restructuring of MSE loans might impact profitability of the company.
- The company faces risks from high concentration of advances from customers located in the state of Tamil Nadu. As of Jun 30, 2030, the state represented 54.31% of gross advances. Any regional slowdown in economic activity, political unrest, disruption, etc. may adversely impact the company.
- The company is subject to stringent regulatory environment which may impact growth.

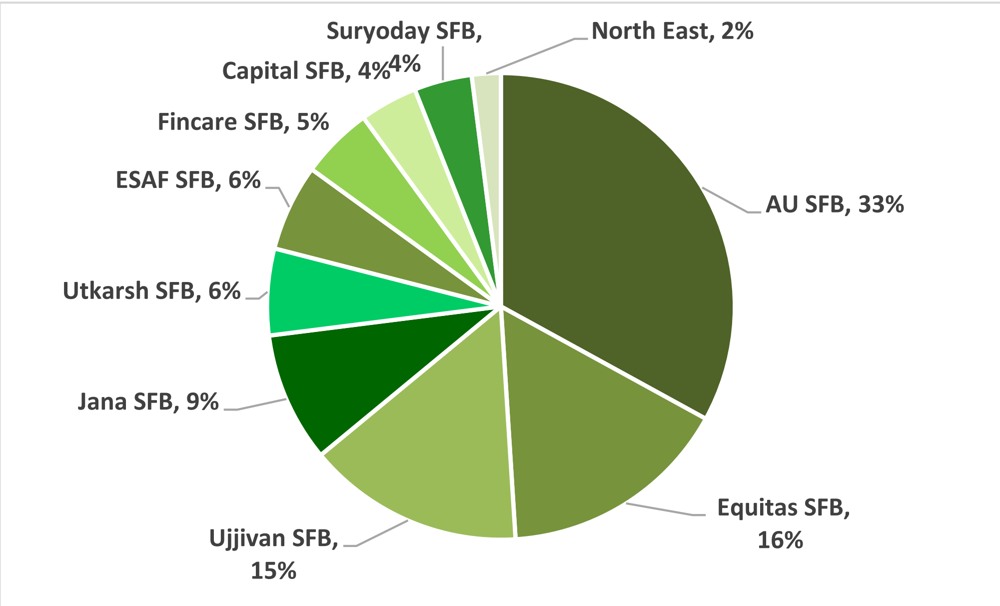
Source: RHP, Anand Rathi Research

Industry Snapshot:

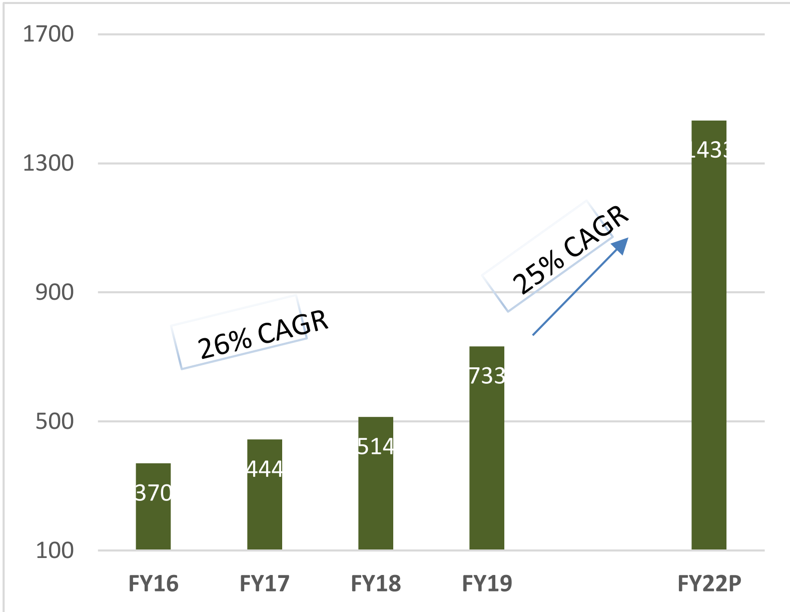
SFB's aim to cater to the low-income segment and have an opportunity to offer them with various products and services. Unlike NBFCs which expand horizontally with a special focus product, SFBs are likely to expand vertically and horizontally which would enable them to have a good range of medium and low value customers and as a result, help in increasing their business. SFBs have grown at a CAGR of 26% from FY16 to FY19, in terms of assets under management (AUM). Top three SFBs accounted for 64% of the total SFB AUM in FY2019, compared to 53% in Fiscal 2016. These top three SFBs recorded a CAGR of 34% from FY16 to Fiscal 2019.

Further, 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.

Top 3 players account for 64% of the market (FY19 AUM)



Huge opportunity for growth (AUM in ₹ billion)



Major growth drivers for SFBs:

i. Sizeable market opportunity and credit at affordable rates: Due to the size of India's population and the lack of formal banking services for significant section of India's population, driving financial inclusion has been a key priority for the government. Various initiatives have been undertaken by the government, which have been implemented by NABARD and through entities such as regional rural banks, cooperatives and commercial banks. However, despite the rapid expansion in the scale of the institutions, several households continued to face difficulties in accessing credit facilities. Notably, The size of the India market (in terms of financially excluded households), offers scope for sustainable credit to the poor at affordable rates to drive growth for SFBs in India.

ii. Customized products driven by technology and availability of information: Increase in the use of technology has enabled lenders to provide customized product offerings to their target customer segments with much lower turnaround times. Further, availability of multiple data points facilitates lending decisions by firms within a few minutes by using data-driven automated lending models. These models help in the supply of credit to small business units and the unorganized sector at low cost. The use of technology is expected to also help such players in expanding their reach to underserved population and areas at a lower operating cost.

iii. Availability of funds at cheaper rates: The ability to accept deposits through CASA and other retail deposits would provide SFBs a cheap source of funding which would help them in competing with NBFCs. Further, with the low cost of funds, SFBs would aim to expand their product portfolio and provide competitive rates in the market. In addition, with the further expansion of SFBs in underserved regions, the deposit base is expected to further increase and will help in expanding their asset side portfolio. Accordingly, SFBs will hold an advantage over NBFCs.

iv. Profitability of SFBs is expected to improve: Newly converted SFBs had a challenging beginning in Fiscal 2018, as many players experienced decline in profitability due to losses in the second half of the financial year on account of stressed microfinance accounts. The main reason for the sharp increase in non-performing assets in the microfinance portfolio of SFBs was the dual impact of demonetization and loan waivers. Profitability revived in FY19 as credit costs on newly originated loans disbursed post demonetization was much lower. Though the current environment remains challenging amid the COVID-19 pandemic, profitability is expected to improve moderately going forward on account of reduction in operating expenses as players gradually scale up their banking operations with the aid of digitization. However, the reduction in operating expenses may not be consistent across the board, as it depends on the ability of SFBs to keep branch establishment and employee costs at stable levels, and also scale up their deposit and income base from these branches. Additionally, ability to maintain sound asset quality in new segments while managing growth and profitability across economic cycles remains to be seen.

Source: RHP, Anand Rathi Research

Competition Scenario

Metrics FY19:

SFB Players	Yield on Advances (%)	NIM (%)	Other Income (% of avg. assets)	Cost of Funds (%)	Cost to Income Ratio (%)	PCR (%)	GNPA	ROE	Post Tax-ROA	Proportion of Deposits in total borrowing (%)	CASA (% of Deposits)
AU SFB	13.0	4.6	2.4	7.4	59.9	37.3	2.0	14.0	1.5	69.3	21.0
Equitas SFB	19.0	7.9	1.9	8.2	63.9	43.3	2.5	9.8	1.4	69.4	28.3
Ujjivan SFB	19.3	9.5	1.8	7.6	76.5	72	0.9	11.5	1.7	63.9	12.3
Jana SFB	20.4	4.6	1.2	10.2	204	NA	8.08	-177	-20.3	50.7	NA
Utkarsh SFB	22.6	9.2	1.1	8.3	58.6	91.3	1.39	15.9	1.7	72.6	10.0
ESAF SFB	26.8	9.7	1.9	9.0	66.4	30	1.61	14.6	1.5	71.7	13.6
Fincare SFB	27.5	11.7	2.2	8.9	66.4	23.5	1.3	20.3	3.2	61.4	5.09 (FY18)
Capital SFB	15.6	3.5	0.8	5.9	79.4	28.6	1.3	8.1	0.5	91.1	38.4
Suryoday SFB	24.7	11.4	2.3	9.1	48	58	1.81	12.2	2.9	58.6	11.2

NA- not available

- Equitas SFB is the second largest SFB in terms of AUM, behind AU SFB. Other players are relatively smaller when compared to the top three players. In terms of deposit, the company is the second largest with deposits of ₹ 90.1 billion, behind AU SFB with deposits of ₹ 194.2 billion.

- With a network of 991 banking outlets in FY19, Equitas SFB remained the leader among SFBs in terms of distribution network. This is followed by AU and Ujjivan SFB, with 558 and 524 outlets, respectively. However, Ujjivan SFB is present in 24 states/ union territories followed by Equitas SFB which is present in 15 states/ union territories.

- Among the SFBs, Capital SFB has the highest CASA ratio of 38.39% followed by the Bank with a CASA proportion of 28.34%. Equitas SFB has the third highest proportion of retail deposits in total deposits at 58.38%.

- Equitas SFB has the fourth lowest yields indicating its diversification away from micro finance. Fincare has the highest yield among SFBs, followed by ESAF. These players have high yields due to high share of microfinance loans in their portfolio. As these players diversify into other loan products, their yield is expected to decline.

Outlook

It is expected the loan portfolio of SFBs will grow at a CAGR of approximately 25% in the near term due to support from (i) significant market opportunity especially in the rural segment (ii) presence of high informal credit channels, (iii) geographic diversification, (iv) ability to understand local markets, (v) access to low cost funds, and (vi) loan recovery and control on NPAs. In the next couple of years, SFBs are expected to focus on gradually building up their banking business and complying with more stringent regulatory norms. On the other hand, access to stable and granular public deposits over the long run will bring down their cost of funds. However, SFBs are expected to face near-term challenges in increasing deposits amid intense competition and maintaining profitability in the initial few years after transformation.

Source: RHP, Anand Rathi Research

Our Take:

With favorable macro traits in the domestic SFB space, we believe Equitas is well positioned for continued growth. At upper price band of ₹33, the IPO is priced at 1.25 times post issue FY20 book value (BV). Valuation looks attractive when compared with peers like AU SFB (5.35x FY20 BV) and Ujjivan SFB (1.89x). While the operating environment remains challenging amid the COVID-19 pandemic, recent collection efficiency and moratorium position signals an improving trend. We remain positive on Equitas SFB given its diversified loan portfolio, well-managed asset quality, strong capital position, extensive distribution network and healthy growth prospects of the SFB industry. We recommend **Subscribe (Long Term horizon)** to this IPO.

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Ratings Guide (12 months)	Buy	Hold	Sell
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