Subscribe-Long Term

Research Team

Issue Details

Issue Details	
Issue Size (Value in Rs. million, Upper Band)	8,316
Fresh Issue (No. of Shares in Lakhs)	158.40
Offer for Sale (No. of Shares in Lakhs)	Nil
Bid/Issue opens on	5-Sep-22
Bid/Issue closes on	7-Sep-22
Face Value	Rs. 10
Price Band	500-525
Minimum Lot	28

Objects of the Issue

Fresh Issue: Rs. 8,316 Million

- Augmentation of Bank's Tier-I capital base to meet their Bank's future capital requirements.
- Meeting the expenses in relation to the Offer.
- Receive the benefits of listing the Equity Shares on the Stock Exchanges.

Book Running Lead Managers
Axis Capital Limited
Motilal Oswal Investment Advisors Limited
SBI Capital Markets Limited
Registrar to the Offer
Link Intime India Private Limited

Capital Structure (` Million)	Aggregate Value
Authorised share Capital	2800.0
Subscribed paid up Capital (Pre-Offer)	1425.1
Paid up capital (Post - Offer)	1583.5

Share Holding Pattern %	Pre Issue	Post Issue
Promoters & Promoter group	0	0
Public	100	100
Total	**100**	**100**

Financials

Particulars (Rs. In Million)	FY22	FY21	FY20
Interest Earned	38,338.6	36,090.5	34,661.1
Interest Expended	20,186.3	20,715.3	21,465.9
NII	**18,152.3**	**15,375.3**	**13,195.2**
Other Income	8,225.8	6,443.5	5,264.2
Total Income	**26,378.0**	**21,818.8**	**18,459.4**
Operating Expenses	11,110.4	9,796.5	8,509.1
Profit Before Provision	**15,267.7**	**12,022.2**	**9,950.3**
Provisions & Contingencies	4,021.6	4,038.7	4,101.3
PBT	**11,246.1**	**7,983.6**	**5,849.0**
Tax	3,027.0	1,950.3	1,772.0
Net Profit	**8,219.1**	**6,033.3**	**4,076.9**

Company Description

Tamilnad Mercantile Bank Ltd is one of the oldest and leading old private sector banks in India with a history of almost 100 years. They offer a wide range of banking and financial services primarily to micro, small and medium enterprises ("MSME"), agricultural and retail customers ("RAM").

Since their incorporation, having head quartered at Thoothukudi, Tamil Nadu, India, they have built a strong presence in the state of Tamil Nadu, with 369 branches and 949 automated teller machines ("ATMs") and 255 cash recycler machines ("CRMs") as of March 31, 2022. The Bank also focus on diversifying their growth in other high growth regions of India which will help increase their network and client base. Other than Tamil Nadu, they are present in 15 other states and 4 union territories of India. Apart from Tamil Nadu, they have sizable presence in the states of Maharashtra, Gujarat, Karnataka, and Andhra Pradesh with presence across 90 branches and 125 ATMs and 18 CRMs as of March 31, 2022.

The Bank have also been consistently growing its customer base from approximately, approximately 4.66 million as of March 31, 2020 to approximately 5.08 million as of March 31, 2022 at the CAGR of 4.36% from Fiscal 2020 to 2022. Out of 5.08 million customers as of March 31, 2022, 4.05 million or 79.78% of their customers have been associated with them for a period of more than five years and have contributed to ₹ 350,142.39 million or 77.93% to their deposits and ₹ 219,022.26 million or 64.90% to company's advances portfolios as of March 2022.

TMB's gross non-performing assets ("GNPA") have reduced from ₹ 10,209.77 million or 3.62% in Fiscal 2020 to ₹ 5,709.23 million or 1.69% in Fiscal 2022. The net non-performing assets ("NNPA") have increased from ₹ 4,974.66 million or 1.80% in Fiscal 2020 to ₹ 6,138.26 million or 1.98% in Fiscal 2021 and subsequently reduced to ₹3,175.84 million or 0.95% in Fiscal 2022. The total income increased at a CAGR of 7.99% from ₹39,925.29 million in 2020 to ₹46,564.35 million in 2022. The NIM has consistently grown over the years with an increase from 3.64% to 4.10% from Fiscal 2020 to Fiscal 2022 at a CAGR of 6.13%. The cost to income percentage has reduced from 46.10% in Fiscal 2020 to 42.12% in 2022 at a CAGR of (4.41)%. The Bank had the second highest Net Profit for Fiscal 2022 amongst its Peers, and their Return on Assets was also higher at 1.66% compared to a median 0.80% for their Peers for Fiscal 2022. In terms of a Return on Equity, their Bank had a ratio of 16.58% in Fiscal 2022, as compared to its Peers who reported a median of 8.30%.

Valuation

Tamilnad Mercantile Bank Ltd (TMB) is one of the oldest and leading old private sector banks in India with a history of almost 100 years. It has loyal customer base as 79.78% of their customers have been associated with them for a period of more than five years. It has strong presence in Tamil Nadu and has focus to increase presence in other strategic regions. The Bank focuses on advances to MSME, agricultural and retail segment which have grown at CAGR of 12.94% between FY20-22. The Bank have shown consistent financial performance, NIM have grown over the years with an increase from 3.64% to 4.10% from FY20 to FY22 at a CAGR of 6.13%.

TMB is available at the upper end of the IPO price band at 9.1x its FY22 earnings demanding a market cap of Rs. 83,134.5 million. At the upper end of the IPO price band, the issue is priced at a P/BV of 1.4x based on its NAV of Rs. 374.4 as of March 31, 2022. The ROE/ROA for FY22 is 16.58%/1.66%.

TMB is demanding a slight higher valuation when compared to its peers given that TMB is outperforming its peers in majority of financial parameters. Given the consistency in its performance over past periods and healthy return ratio, we recommend a "**Subscribe-Long Term**" rating to this IPO.

The Bank was incorporated as ‘Nadar Bank Limited’ in 1921 and their name was changed to ‘Tamilnad Mercantile Bank Limited’ in the year 1962. It received the license to carry on banking business from the Reserve Bank of India (the “RBI”) in 1962. Since their incorporation, having head quartered at Thoothukudi, Tamil Nadu, India, they have built a strong presence in the state of Tamil Nadu, with 369 branches and 949 automated teller machines (“ATMs”) and 255 cash recycler machines (“CRMs”) as of March 31, 2022. Tamil Nadu, the fourth largest state of India, is one of the fastest growing states, with continued focus on MSME and textile industry. Tamil Nadu’s gross state value added (“GSVA”) at current prices grew at a compounded annual growth rate (“CAGR”) of 11% between Fiscal 2017 and 2022 against the country wide growth of 9%. Tamil Nadu ranked second in terms of state-wise contribution to GDP and has also grown at a faster rate as compared to the national GDP growth rate. Tamil Nadu is under penetrated which presents an opportunity for further growth in GDP funded by bank loans. Its bank credit to GDP stood at 52% as compared with approximately 100% in case Maharashtra and 33% for Gujarat during Fiscal 2022. Bank’s deposits have grown at a healthy pace of 10.46% CAGR (compared to median of its peers: 7.90%), while its advances grew at 9.93% CAGR (compared to median of its peers: 8.00%). As of March 31, 2022, their deposits and advances portfolio in the state of Tamil Nadu has contributed 75.06% to its Total Business. The Company also focus on diversifying their growth in other high growth regions of India which will help increase their network and client base. Other than Tamil Nadu, they are present in 15 other states and 4 union territories of India. Apart from Tamil Nadu, they have sizable presence in the states of Maharashtra, Gujarat, Karnataka, and Andhra Pradesh with presence across 90 branches and 125 ATMs and 18 CRMs as of March 31, 2022. The Company have also been consistently growing its customer base from approximately, approximately 4.66 million as of March 31, 2020 to approximately 4.91 million as of March 31, 2021 to approximately 5.08 million as of March 31, 2022 at the CAGR of 4.36% from Fiscal 2020 to 2022. Their focus on quality of service and nurturing long term relationship with their customers has enabled them to develop a well-recognized and trusted brand in south India, particularly in Tamil Nadu, India

The Company have built a strong portfolio of advances and deposits across their customer base.

Advances: Their advances portfolio primarily consists of lending to (a) Retail customers; (b) agricultural customers and (c) MSMEs (“RAM”).

MSMEs: They primarily offer various loan products to their MSME customers operating in manufacturing, trading and services sector. During the Fiscals 2020, 2021 and 2022 MSMEs contributed 37.92%, 39.08% and 37.38% respectively to their total advances with a CAGR of 8.55% from March 31, 2020 to March 31, 2022.

Agricultural customers: The Company primarily offer loan products to individual farmers, group of farmers and agricultural corporates. During the Fiscals 2020, 2021 and 2022 agricultural customers contributed 24.77%, 27.41% and 29.70% respectively to their total advances with a CAGR of 19.70% from March 31, 2020 to March 31, 2022.

Retail customers: They primarily offer home loans, personal loans, auto loans, educational loans as well as security backed loans of various types to their retail customers. During the Fiscals 2020, 2021 and 2022 retail customers contributed 19.27%, 20.60% and 20.39% respectively to their total advances with a CAGR of 12.46% from March 31, 2020 to March 31, 2022.

Corporate customers: The Company offer various kinds of loans to corporates, in textiles and other industries, with their assortment of banking products and services including working capital, term financial, trade financial, structured finance services, foreign exchange business funding in domestic and foreign currencies. During the Fiscals 2020, 2021 and 2022 corporate customers contributed 18.04%, 12.92% and 12.53% respectively to their total advances with a CAGR of (8.89%) from March 31, 2020 to March 31, 2022. This is in line with their strategy to move focus away from corporate customers in favour of RAM.

From Fiscal 2020 to Fiscal 2022, their overall advances portfolio has increased at a CAGR of 9.33%.

- RAM portfolio: The Company’s lending products are primarily focussed on MSME, retail and agri-financing. Their RAM portfolio has increased at a CAGR of 12.94% from ₹ 231,427.36 million in Fiscal 2020 to ₹ 295,205.01 million in Fiscal 2022.

- Secured and un-secured lending: With focus on keeping risk relatively lower, in addition to their strong underwriting processes, they have consistently maintained and further increased their secured lending from 98.82% of their overall advances in Fiscal 2020 to 99.17% of their overall advances in Fiscal 2022. The Company’s un-secured lending portfolio’s contribution has declined from 1.18% or ₹ 3,327.70 million of overall advances as on March 31, 2020 to 0.69% or ₹ 2,172.40 million as on March 31, 2021 and increased to 0.83% or ₹ 2,798.50 million as on March 31, 2022.

- Average ticket size of advances: With an aim to manage risk of concentration, they have increased their focus on lower ticket size loans. The company’s average ticket size of loans in their overall advances portfolio has grown in the following manner:

Loan Category	Fiscal 2020	Fiscal 2022	CAGR
Up to ₹ 1 lac	38,436.1	32,089.5	-8.63%
Above ₹ 1 lac and up to ₹ 5 lacs	27,925.6	58,272.6	44.45%
Above ₹ 5 lacs and up to ₹ 10 lacs	18,492.5	24,727.4	15.64%
Above ₹ 10 lacs and up to ₹ 25 lacs	42,540.1	56,155.0	14.89%
Above ₹ 25 lacs	154,967.7	166,239.3	3.57%

Deposits: The Company’s deposits portfolio consists of term deposits, recurring deposits, savings bank and current bank accounts amongst others. Total deposits of their Bank have increased at a CAGR of 10.46% from ₹ 368,250.27 million in Fiscal 2020 to ₹ 449,331.14 million in Fiscal 2022. During the Fiscals 2020 and 2022, their current account savings accounts (“CASA”) contributed ₹ 95,180.50 million or 25.85%, and ₹ 137,051.64 million or 30.50% respectively to their total deposits and have grown with a CAGR of 20.00% from March 31, 2020 to March 31, 2022. Further, during the Fiscals 2020 and 2022, retail term deposits contributed ₹ 243,362.20 million or 89.12%, and ₹ 272,048.89 million or 87.12% respectively to their total term deposits and have grown with a CAGR of 10.46% from March 31, 2020 to March 31, 2022. They also have healthy renewal rates across their term deposit categories. Their deposit growth rate has been one of the top five amongst its Peers in the industry with a growth rate of 10.46% for Fiscals 2020-22.

The renewal rates of their term deposits have changed in the following manner across categories:

Category	Fiscal 2020	Fiscal 2021	Fiscal 2022
Up to ₹ 15 lacs	79.86%	78.31%	78.00%
Above ₹ 15 lacs below ₹ 100 lacs	78.26%	79.09%	78.87%
Above ₹ 100 lacs	32.96%	41.40%	31.96%

The Company's risk management processes are aimed at maximizing their Bank's risk adjusted rate of return by maintaining credit exposure within acceptable parameters. Their gross non-performing assets ("GNPA") have reduced from ₹ 10,209.77 million or 3.62% in Fiscal 2020 to ₹ 10,847.78 million or 3.44% in Fiscal 2021 to ₹ 5,709.23 million or 1.69% in Fiscal 2022. In Fiscal 2022, their Bank reported a low GNPA of 1.69% compared with 4.40% for its peers (median). Please see below a comparison with identified industry peers:

Parameters (FY22)	Tamilnad Mercantile Bank	City Union Bank	Catholic Syrian bank	DCB	Federal Bank	Karur Vysya Bank	Karnataka Bank	RBL Bank	South Indian Bank
GNPA (In ₹ million)	5,709.23	19,331.80	2,895.10	12,899.30	41,367.40	34,310.40	22,508.20	27,283.90	36,480.90
GNPA (%)	1.69%	4.70%	1.81%	4.32%	2.80%	5.96%	3.90%	4.40%	5.90%
NNPA (In ₹ million)	3,175.80	11,911.00	1,070.00	5,732.30	13,926.20	12,607.90	13,769.70	8,065.60	17,777.70
NNPA (%)	0.95%	2.95%	0.68%	1.97%	0.96%	2.28%	2.42%	1.34%	2.97%

Their net non-performing assets ("NNPA") have increased from ₹ 4,974.66 million or 1.80% in Fiscal 2020 to ₹ 6,138.26 million or 1.98% in Fiscal 2021 and subsequently reduced to ₹3,175.84 million or 0.95% in Fiscal 2022. In Fiscal 2022, its GNPA as a percentage of overall advances in RAM portfolio was ₹ 4,288.7 million or 1.45% and in corporate portfolio was ₹ 1,420.5 million or 3.36 % respectively. Further, the company have maintained a provision coverage ratio ("PCR") at 80.75%, 79.53% and 87.92% as of March 31, 2020, March 31, 2021 and March 31, 2022 respectively. As on March 31, 2022, they had a network of 509 branches, 12 administrative offices, 1,141 ATMs, 282 CRMs, and 101 E-lobbies. Out of these 509 branches, 76 branches are in metropolitan areas, 80 branches are in urban areas, 247 branches are in semi-urban areas, and 106 branches are in rural areas. They have wide presence in south India and further diversifying their branches in other states of India, with 90 branches located in the states of Maharashtra, Gujarat, Karnataka and Andhra Pradesh respectively. They are a professionally managed bank. Their Board of Directors and senior management consist of seasoned professionals with experience in banking, accounting and auditing. Its MD & CEO, K.V. Rama Moorthy, has more than 40 years of experience in the banking industry. Other members of the Board including their Independent Directors also have significant experience including experience in the banking and finance industry. Additionally, two Directors have been nominated to its board by the RBI. The experience of their Board and senior management team has enabled the company to develop a strong understanding of industry-specific aspects of their business and operations.

Metric	As of and for the years ended March 31,		
	2020	2021	2022
Total Business	650,612.1	725,114.5	786,812.5
Deposits	368,250.3	409,704.2	449,331.1
Credit to deposit ratio	75.26%	75.83%	74.54%
Cost of deposits	6.27%	5.49%	4.91%
Net advances	277,157.6	310,696.0	334,915.4
Yield on advances	10.19%	9.65%	9.45%
Credit cost (Average Advances)	1.51%	1.37%	0.63%
Net interest income	13,195.1	15,375.3	18,152.3
Net interest margin	3.64%	3.77%	4.10%
Operating profit	9,950.3	12,022.3	15,267.7
Net profit	4,076.9	6,033.3	8,219.1
et worth	39,796.5	45,799.8	53,357.1
Return on assets	0.99%	1.34%	1.66%
Return on equity	10.73%	14.10%	16.58%
CASA to total deposits ratio	25.85%	28.52%	30.50%
Cost to income ratio	46.10%	44.90%	42.12%
Gross NPA	3.62%	3.44%	1.69%
Net NPA	1.80%	1.98%	0.95%
PCR Ratio	80.75%	79.53%	87.92%

Strengths:

- **Strong legacy, loyal customer base and focus on improving servicing framework**

With almost 100 years of history, they have established themselves as a well-recognized scheduled commercial bank having a strong network of branches, ATMs and CRMs across several states of South India including Tamil Nadu being their home state, along with Maharashtra, Gujarat, Karnataka, and Andhra Pradesh, which has enabled them to maintain a strong customer base. As of March 31, 2020, 2021 and 2022, it had 4.66 million, 4.91 million and 5.08 million customers respectively with a CAGR of 4.36% from March 31, 2020 to March 31, 2022. The Company have consistently worked towards developing long-term relationships with their customers based on their knowledge of local needs and their experience in the sector, amongst other things. Their largest branch is located in Mandvi, Mumbai, contributing ₹ 20,341.30 million or 2.59% to their Total Business as of March 31, 2022. One of their oldest branches is in Sivakasi, Tamil Nadu, which was started in 1942 and contributes ₹ 14,026.70 million or 1.78% to their Total Business as of March 31, 2022.

With a focus on increasing their existing customer base, they have introduced various alternate banking channels such as ATMs, CRMs, internet banking, mobile banking, E-Lobbies, point of sales ("PoS"), banking and debit and credit cards. They introduced internet banking to their customers in 2008 through 'TMB-Econnect' and utility payment facility which enabled their customers to pay bills for cable operators/DTH operators, electricity services, mobile phone utility services, other utilities and tax services

- **Strong presence in Tamil Nadu with focus to increase presence in other strategic regions**

Since the company's incorporation, they have built a strong and trusted network of customers in the State of Tamil Nadu. As of March 31, 2020, 2021 and 2022 their deposits and advances in the state of Tamil Nadu contributed to 75.93%, 76.33% and 75.06%, respectively, of their Total Business. As of March 31, 2022, the company had 4.32 million customers, 85.03% of their overall customer base, contributing to their deposits and advances portfolios in the State of Tamil Nadu. The gross state domestic product ("GSDP") has been highest in the state of Maharashtra followed by the state of Tamil Nadu and Gujarat. GSDP of Tamil Nadu has grown at a CAGR of 11% over Fiscals 2017-22 higher than National gross domestic product ("GDP") which has grown at a CAGR of 9% between the same period. During the same period, Gujarat has reported highest growth of 11% and Maharashtra has displayed growth rate of 8%. Tamil Nadu is also one of the fastest growing states, with continued focus on MSME and textile industry with GSVA at current prices growing at a CAGR of 11% over Fiscals 2017-2022 against the country wide growth of 9%. Tamil Nadu is under penetrated which presents an opportunity for further growth in GDP funded by bank loans. Its bank credit to GDP stands at 52% as compared to ~100% in case Maharashtra and 33% for Gujarat during Fiscal 2020.

Apart from their home state, Tamil Nadu, they focus on diversifying their reach in their already existing network including in the states of Gujarat, Maharashtra, Karnataka and Andhra Pradesh. As of March 31, 2022, their businesses, including the deposits and advances portfolios, in the state of Tamil Nadu, Maharashtra, Andhra Pradesh, Karnataka and Gujarat contributed 75.06%, 5.78%, 3.67%, 3.47% and 2.91% to their Total Business. The Company's focus to increase their markets share in these states more specifically in their home state where they are located across 369 branches, 949 ATMs, 255 CRMs, 91 E-Lobbies, 3,939 PoS as of March 31, 2022, has therefore, benefited them and will help them further enhance their customer base and increase their business operations.

- **Advances with focus on MSME, agricultural and retail segments.**

The Company have traditionally focused on small ticket size loan products to MSME customers, agricultural and retail customers for their growth. Their advances portfolio consists of a wide basket of retail finance and small ticket size MSME finance products. The focus is on understanding the needs and expectation of their customers, particularly in the RAM space and adopting strategies to target these customer segments for their growth. The Company have dedicated marketing managers and agri-officers across their regional offices who specifically focus on growing the network of their existing MSME and agricultural customers. The Company leverage their presence in semi-urban and rural regions where they are located to attract more customers in the RAM segment. They have dedicated branches at Thoothukudi and Chennai in Tamil Nadu, and at Surat, Gujarat to cater to the requirements of MSME customers in these regions. Further, these dedicated branches act as facilitators for their MSME customers with a focus on improving their loan processing timelines and faster disbursals to benefit their MSME customers.

- **Consistently growing deposit base with focus on low-cost retail CASA**

The Company have adopted a customer-first approach, with an emphasis on customer relationships. Apart from the individual segment, they have focused on account sourcing on value based CASA products, have started following segmental approach on CASA growth by introducing segment wise CASA products such as Trust, Association, Society, Colleges, Charities ("TASC") and CASA accounts of central and state government schemes under their "TMB Savings for Government Segments" account. During the last three Fiscals, their overall deposits base has increased from ₹ 368,250.27 million in Fiscal 2020 to ₹ 409,704.16 million in Fiscal 2021 to ₹ 449,331.14 million in Fiscal 2022, owing to an increase in both term deposits and CASA deposits. Their CASA deposits as a share of total deposits has increased from ₹ 95,180.50 million or 25.85 % in Fiscal 2020 to ₹ 116,852.65 million in Fiscal 2021 or 28.52% to ₹ 137,051.64 million in Fiscal 2022 or 30.50% with a CAGR of 20.00 % from Fiscal 2020 to Fiscal 2022. The Company's CASA portfolio is diversified and has low concentration with 2.91% of deposits from their top 20 deposit holders and 4.75% deposits from their top 50 depositors as of March 31, 2022.

The cost of deposits, calculated on average of fortnightly deposit balance, has been reduced from 6.27% in Fiscal 2020 to 5.49% in Fiscal 2021 to 4.91% in Fiscal 2022. However, as at March 31, 2020, 2021 and 2022 their CASA and retail term deposits contributed ₹ 338,542.67 million or 91.93%, ₹ 381,096.26 million or 93.01% and ₹ 409,100.53 million or 91.05% of their total deposits. Further, during Fiscals 2020-22, their deposits increased at a healthy CAGR of 10.46% compared with peer median of 7.90%.

They continuously strive to increase reliance for transactions on digital channels which are more cost effective than physical channels. Their digital banking channels enable a smooth transition from physical to digital usage and enhance customer experience, designed to grow their business and improve their margins.

- **Professionally managed Bank with experienced senior management team and board of directors**

The Company's Board of Directors comprises 11 directors and two nominee directors appointed by the RBI. The 11 directors include their Managing Director and Chief Executive Officer and ten Non-Executive directors, of whom six are Independent Directors, one of whom is a woman Director. They bring substantial experience and independent directors with diverse experience including sectors such as banking, law, business administration, other streams of finance such as accounting and auditing. Certain directors are also qualified in various stream of technology.

Their senior management team's capabilities, reputation, extensive network of industry relationships, and wideranging experience in the finance and banking industry is critical to their strategy to grow, modernise, and develop further. The senior management team consists of their Managing Director and Chief Executive Officer and various General Managers. Their Managing Director and Chief Executive Officer has been working with the company since September 4, 2017 and their General Manager heading the Human Resources Department has been working in the Bank for the last 34 years in various positions and subsequently, as the General Manager of the Human Resources Department from May 25, 2018. The General Manager of Recovery has been a part of the Bank for the last 37 years in various positions and as the General Manager of Recovery from May 25, 2018. Further, the General Manager of Credit has been working in the Bank since March 20, 2019, and he had previously worked as Chief General Manager in State Bank of India.

- **Strong asset quality, underwriting practices and risk management policies and procedures.**

The strong customer understanding, focus on secured granular loan products and strong under-writing and risk management framework has helped them to maintain and further improve asset quality and driving their growth with consistent profitability. This is particularly important to the company given their RAM portfolio focusing particularly on the MSME customers. They focus on selective lending and limit their exposure to certain industries and sectors as a part of their strategy to monitor concentration risk. The GNPA have reduced from 3.62% in Fiscal 2020 to 1.69% in Fiscal 2022. The Bank has reported a relatively lower GNPA of 1.69% as compared with 4.40% for their Peers (median) as of Fiscal 2022. The NNPA have reduced from 1.80% in Fiscal 2020 to 0.95% in Fiscal 2022. In Fiscal 2022, their GNPA as a percentage of advances in RAM portfolio is 1.45% and in corporate portfolio is 3.36 % respectively. They have a low customer concentration in terms of average ticket size. The average ticket size has remained in the range of 0.31 million to 0.34 million during the last three Fiscals. The Company have maintained their PCR at 87.92% as of March 31, 2022. They made total provisioning of ₹ 2,496.30 million and total write-offs including technical/prudential write offs of ₹ 20,571.40 million together amounting for ₹ 23,067.70 million as on March 31, 2022. Additionally, during the year they had made provisions for contingency provision for COVID-19 and other uncertainties as of March 31, 2022, they made total provisioning for ₹ 2500 million.

Further, with an aim to maintain and improve the asset quality, the company follow specific processes prior to loan approval and during the tenure of the loans depending on the ticket size of the loans. Their term loans are reviewed annually and higher value loans are reviewed periodically depending on the size of the loan products. This enables the company to escalate any defaults at their regional offices in a timely manner. They also have a dedicated credit audit monitoring department which monitors their advances and helps avoid any downgrading in asset classification. They also have recovery champions at specific branches, regional offices and their head office to enable them to maintain their asset quality. They also have early warning signals ("EWS") software to identify weaknesses in advances which is escalated to relevant officers and branches of their Bank. Their lending products are sanctioned basis standard operating procedures. Their advances with exposure of ₹ 250.00 million or more are monitored on a daily basis. These prudent risk management controls, policies, and procedures that the company currently have and continuously evaluate to improve, are critical for the long-term sustainable development of their business. They regularly assess and update these policies and procedures to align with statutory changes as well industry standards. They have implemented risk management procedures for their credit exposures, including credit scoring, risk based pricing models, risk monitoring and control mechanisms. As of March 31, 2022, they have 59.46% of their outstanding loan value with less than 12 month tenures including working capital facilities renewable annually, 17.45% of their outstanding loan value with a tenure of 12-60 months and 23.09% with a tenure of more than 60 months. As of March 31, 2022, their average loan outstanding per branch is ₹ 663.03 million

- **Consistent financial performance**

The Company's diversified portfolio, increasing market penetration across rural and semi-urban regions and focus on asset quality has enabled the company to ensure consistent financial performance over the years. They also focus on increasing their digital footprint which in turn has improved their operational processes that has reduced their costs and resulted in improving the profitability of the Bank. The total income increased at a CAGR of 7.99% from ₹39,925.29 million in 2020 to ₹ 42,534.02 million in Fiscal 2021 to ₹46,564.35 million in 2022. The NIM has consistently grown over the years with an increase from 3.64% to 4.10% from Fiscal 2020 to Fiscal 2022 at a CAGR of 6.13%. The cost to income percentage has reduced from 46.10% in Fiscal 2020 to 42.12% in 2022 at a CAGR of (4.41)%. The Company had the second highest Net Profit for Fiscal 2022 amongst its Peers, and their Return on Assets was also higher at 1.66% compared to a median 0.80% for their Peers for Fiscal 2022. In terms of a Return on Equity, their Bank had a ratio of 16.58% in Fiscal 2022, as compared to its Peers who reported a median of 8.30%.

Key Strategies:

- **Continue to strengthen its product portfolios across deposits and advances**

The Company's growth in the past few years has been driven by strong understanding of the needs and expectations of their RAM customers. Their RAM Portfolio has increased from ₹ 231,427.36 million in Fiscal 2020 to ₹ 295,205.01 million in Fiscal 2022 at a CAGR of 12.94%. The Company have higher growth potentials in geographies where they exist such as in the State of Tamil Nadu and Gujarat which have lower bank credit to GDP ratios that are indicative of opportunities for banks and with their presence in the rural and semi-urban markets, the company are well positioned to continue attracting higher proportion of RAM customers. Their long terms growth strategy is aligned to the RBI guidelines of Priority Sector Lending ("PSL") which encourages inclusive lending policies, targeted at retail customers from weaker sections, agriculture and MSME customers who are covered under priority sector. Therefore, their focus is on boosting the RAM loan book through SME loan, house loans, car loan, personal loan, Loan Against Property ("LAP") and pensioner's loans, jewel loan, agricultural loan and good quality mid-corporate segment loans on selective basis.

They will continuously focus on exploring and introducing new and customized fee-based products in connection with their centenary anniversary and strategies like TMB win-back campaign in addition to their existing products such as 'TMB Home Loan', 'TMB Affordable Home Loan', 'TMB Mahalir', and 'TMB Tractor'. The Company will also focus on improving experience of already available products as well as more tie ups with strategically identified third parties and leveraging their deep market expertise and relationships to leverage cross-selling opportunity, to grow deposits, improve advances sector wise and grow their fee-based income.

The Company also aim to expand the branch-wise targets by opening new Retail Assets Central Processing Centres ("RACPCs") with dedicated home loan sales teams posted at these locations to drive further home loan portfolio growth. As of March 31, 2022, the Bank has one RACPC located at Chennai, Tamil Nadu, to which 36 branches of their Bank are linked. The housing loan portfolio of these 36 branches grew from 1,463 accounts with an outstanding amount of ₹ 2,900.79 million as on March 31, 2020 to 1,634 accounts with an outstanding amount of ₹ 3,405.53 million as on March 31, 2022.

They are also focused on diversifying their product portfolio so as to gain more customers and increase their market share. They will continue to expand their relationship banking facilities to increase their network. The Company intend to focus more on fee based products such as issuing debit cards, credit cards, general insurance, life insurance, online bill payment services, depository services, government schemes, e-stamping and bill payments to their existing as well as new customers. They have introduced individual targets to increase income arising through cards, locker system, PoS machine and any third party products. They are also promoting investments in sovereign gold bonds floated by the RBI. The Company is also aiming to mobilise opening new accounts under the Atal Pension Yojana and National Pension Schemes. They aim to identify potential clients in the import/export industry to augment their bill collection and forex transaction turnover. They also focus on maximizing their revenue through their treasury operations to increase the profit on exchange, profit on sale of investments and income on investments.

- **Transformation through technology to improve efficiency and customer experience**

The Company believe that the increased availability of internet access and connectivity across India requires a comprehensive technology-driven strategy to proactively develop new methods of reaching their customers and running their businesses. The technology-driven strategy is focused on acquiring new customers by enhancing customer experience through their digital interfaces. Their technology focus is also intended to enhance the loan approval capabilities, reduce overall turnaround time, and facilitate maintaining and developing long-term customer relationships by allowing the customers to interact with them and access their accounts from the comfort of their personal space.

The Company invest in technology as a means of improving their customers' experience, offering them a range of products tailored to their financial needs and making it easier for them to interact with the company. While they have introduced internet and mobile banking to their customers around 10 years ago, the company continue to launch better interfaces and platforms for ease of their customers to access and use their varied product portfolio and services. They have approximately 0.28 million customers using their internet banking facilities who made 4.99 million transactions, and approximately 0.28 million customers using their new mobile banking facilities who made 8.12 million transactions, as of March 31, 2022.

- **Continue to improve asset quality**

The aim of the company is to continuously monitor and improve asset quality by focusing on secured advances, high loan to value ratio, diversification across loan book tenures, low concentration across branches and more stringent audit procedures for sanction of the loans specifically focusing on higher value loans. Their risk assessment, mitigation and management measures towards reducing NPAs and managing their stressed assets portfolio is particularly important to them, given their focus on their RAM portfolio.

Apart from continuously monitoring the loans during their tenure, they also conduct various audit processes such as stock audits on working capital facilities, with exposure of ₹ 30.00 million or above in both fund and non-fund based accounts. Further, they conduct credit audits on their loan accounts with exposure of ₹ 30.00 million or above. Their pre-disbursement approval procedure is also quite detailed with specific audits and procedures to be conducted in exposure of ₹ 30.00 million or above. The Company aim to introduce more follow ups for compliances of their existing and new loans and introduce peer review of their approved loans to ensure that their asset quality continues to maintain and improve further.

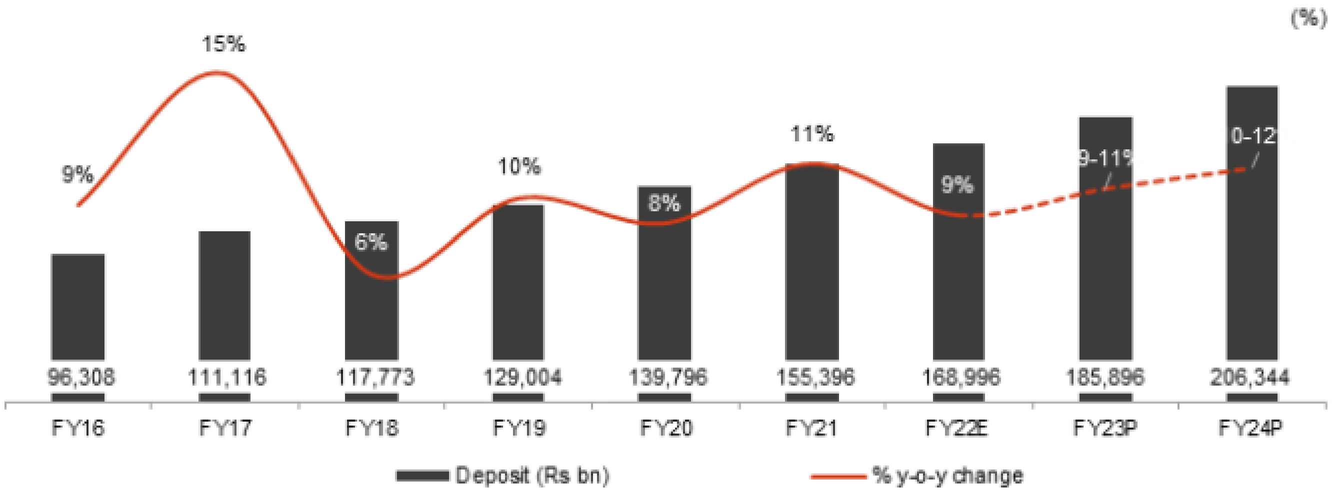
They also intend to reduce their NPAs by continuing to offer various schemes of settlement to address the issues specifically faced by small ticket borrowers. Further, they propose to boost NPA recovery through one-time settlements, and monitoring of small value NPA accounts. They will continue their focus on establishing and maintaining comprehensive strategies to achieve NPA targets by operating a dedicated credit recovery department and a region- wise cluster based oversight mechanism.

Industry Snapshot:

- **Deposits to grow at a healthy rate of 9-11% during fiscal 2023**

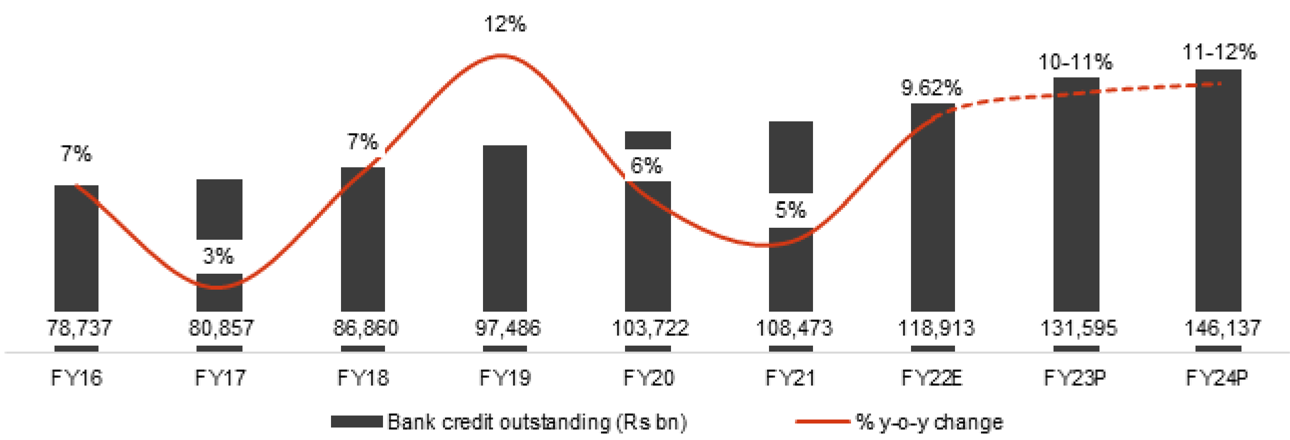
The banking sector enjoyed a healthy deposit compound annual growth rate (CAGR) of ~10% between fiscals 2016-21. With the outbreak of Covid-19 in fiscal 2021, conserving money became a priority and households reduced their private consumption, leading to 11% deposit growth in the fiscal. Further, the weighted-average domestic term deposit rate declined 80 basis points (bps) from 6.07% in April 2020 to 5.28% in March 2021. With the RBI keeping it stance accommodative and policy rates unchanged for the entire fiscal 2022, the weighted average term deposit rate declined a further 25 bps to 5.03% as of March 2022. During the monetary policy meeting in April 2022, the RBI signalled a gradual removal of the accommodative policy — it increased the policy repo rate by 40 bps in May 2022 and 50 bps in June 2022. The deposits are expected to grow 9-11% during fiscal 2023, driven by an expected hike in policy rates by an additional 75 bps the fiscal, pushing the repo rate 50 bps above the pre-pandemic level by fiscal-end, and banks, in turn, transmitting the hike by increasing deposit rates.

Deposits (Rs billion) and % on-year change in India



- **Credit growth to continue at 10-11% during fiscal 2023**

Bank credit outstanding and % on-year change



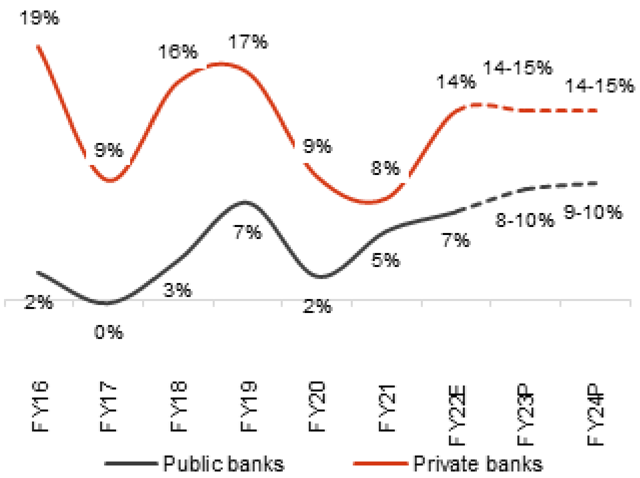
In fiscal 2021, the Indian economy witnessed the sharpest contraction since Independence, due to the onset of the pandemic and imposition of a nationwide lockdown. To help deal with the impact of the pandemic, the government and the RBI took several initiatives to provide relief to borrowers. While the impact was significant in the first half of fiscal 2021, faster-than-expected revival led to moderate credit growth of 4.6% in fiscal 2021. The most significant initiatives included the Rs 3,000,000 million (revised upwards to Rs 5,000,000 million) Emergency Credit Line Guarantee Scheme (ECLGS); provision of loan moratorium; and option of restructuring loans to corporates, micro, small and medium enterprises (MSMEs), and individual borrowers under the restructuring framework (One-time restructuring - OTR 1.0 and 2.0).

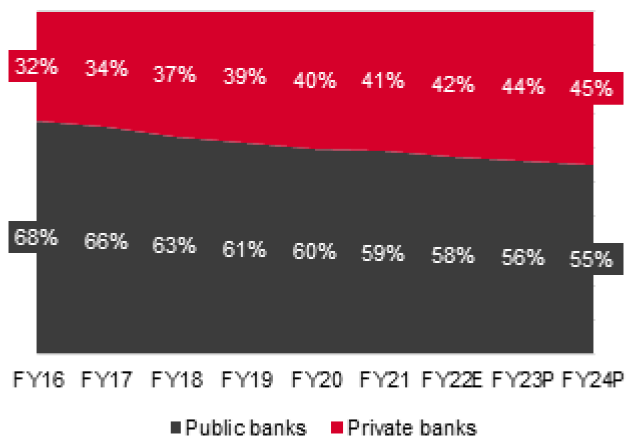
In the first half of fiscal 2022, the second wave of the pandemic forced both borrowers and lenders to tread cautiously, leading to muted growth in bank credit. Growth picked up in the third quarter of fiscal 2022, and with a mild third wave, the momentum continued in the fourth quarter supported by pent-up and festive season demand. Further, the amount sanctioned under the ECLGS aggregated to Rs 3,320,000 million and disbursement aggregated to Rs 2,590,000 million as of April 2022. The scheme has primarily aided the MSMEs to obtain credit from the banking sector and revive business activities. The bank credit is expected to grow 10-11% during fiscal 2023, driven by the retail and agriculture segments and supported by recovery in services and industrial credit.

- **Private banks to continue to outpace public banks in credit growth in the medium term**

Traditionally, public banks have accounted for the major proportion of the banking credit outstanding. However, low profitability, a weak capital position, low operational efficiency and an increase in stressed loans in the past few years led to slowdown in their loan growth. As a result, public banks gradually lost market share to private banks, which were relatively well capitalised and had a higher degree of operational efficiency. Public banks, which accounted for 71% share in credit outstanding in fiscal 2015, accounted for only 58% share in fiscal 2022.

A partial economic slowdown resulted in lower credit growth in fiscal 2020 for both public and private banks. In fiscal 2021, growth for public banks stood at 5%, while private banks were able to grow 8% due to better capital buffers and increased focus on retail segment. Therefore, the latter gained further market share. As merged banks focus on integration and banks placed under corrective action come out of the PCA framework, credit growth of public banks is expected to lag that of private banks in the medium term. In fiscal 2022, private banks' focus on credit growth, especially in the retail segments, aided them to grow at a healthy double-digit rate of 14%. Growth at public banks also picked up to 7%. The credit growth of 8-10% at public banks and 14- 15% at private banks is expected during fiscal 2023.





- **Peer Comparision**

  - **Peer comparison for advances and deposits**

Parameters (FY22)	Tamilnad Mercantile Bank	City Union Bank	Catholic Syrian bank	DCB	Federal Bank	Karur Vysya Bank	Karnataka Bank	RBL Bank	South Indian Bank
Deposits (Rs Million)	4,49,331	4,76,897	2,01,883	3,46,917	18,17,006	6,86,763	8,03,868	7,90,065	8,91,421
CASA/Total deposits	30.50%	32.56%	33.66%	26.75%	36.94%	34.81%	33.00%	35.29%	33.21%
Advances (Rs Million)	3,34,915	4,03,585	1,58,147	2,90,958	14,49,283	5,53,346	5,67,831	6,00,218	5,99,934
Deposits CAGR FY20-22	10.46%	8.07%	13.07%	6.88%	9.23%	7.82%	5.82%	16.90%	3.61%
Advances CAGR FY20-22	9.93%	9.07%	17.96%	7.14%	8.87%	9.56%	-0.20%	1.71%	-3.51%
Net profit (Rs Million)	8,219.09	7,601.65	4,584.90	2,875.10	18,898.20	6,732.70	5,086.10	-747.4	449.8
Net profit CAGR FY20-22	41.99%	26.30%	-	-7.76%	10.68%	69.25%	-6.62%	-	-34.42%

  - **Operating profitability of TMB and its peers**

Parameters (FY22)	Tamilnad Mercantile Bank	City Union Bank	Catholic Syrian bank	DCB	Federal Bank	Karur Vysya Bank	Karnataka Bank	RBL Bank	South Indian Bank
Yield on advances	9.45%	9.36%	11.21%	10.71%	7.92%	8.47%	8.84%	12.22%	8.73%
Cost of deposits	4.91%	4.68%	4.31%	6.05%	4.28%	4.30%	4.66%	4.81%	4.75%
Net interest margins	4.10%	3.98%	5.27%	3.56%	3.16%	3.69%	3.18%	4.40%	2.62%
Cost-to-income	42.12%	40.37%	50.51%	55.40%	59.89%	53.20%	52.57%	56.90%	64.10%
Net profit margin	17.65%	15.62%	17.60%	7.30%	12.00%	10.60%	7.21%	-0.10%	0.10%

Key Risk:

- The Company have regional concentration in southern India, especially Tamil Nadu. Any adverse change in the economic, political, or geographical conditions of Tamil Nadu and other states in which they operate can impact their results of operations.
- The Bank is subject to stringent regulatory requirements and prudential norms and their inability to comply with such laws, regulations and norms may have an adverse effect on the business, results of operations, financial condition and cash flows.
- Their contingent liabilities exceed their net worth, which, if they materialize, may adversely affect the results of operations, financial condition and cash flows.

- The Company is subject to supervision and inspection by authorities such as the RBI. Any adverse observations from RBI or non-compliance with RBI inspection/ observations or other regulatory requirements could have an adverse effect on their business, financial condition, results of operation and cash flows.

- The majority of the bank's business premises are leased. Accordingly, they are exposed to risks typical to leasing of commercial real estate, including risk of being required to relocate certain of their premises from time to time.

- They are currently significantly dependent on Retail, MSME and Agri-financing, customers and any adverse developments in these segments could adversely affect their business, results of operations, financial condition and cash flows.

- The bank will be unable to open new branches unless they are listed and are also required to obtain prior permission from the RBI to open new branches.

- The Bank's business is vulnerable to interest rate related risks. Volatility in interest rates could adversely affect their net interest margin, the value of their fixed income portfolio, their security receipts, their income from treasury operations, the quality of their loan portfolio, and their financial performance.

Valuation:

Tamilnad Mercantile Bank Ltd (TMB) is one of the oldest and leading old private sector banks in India with a history of almost 100 years. It has loyal customer base as 79.78% of their customers have been associated with them for a period of more than five years. It has strong presence in Tamil Nadu and has focus to increase presence in other strategic regions. The Bank focuses on advances to MSME, agricultural and retail segment which have grown at CAGR of 12.94% between FY20-22. The Bank have shown consistent financial performance, NIM have grown over the years with an increase from 3.64% to 4.10% from FY20 to FY22 at a CAGR of 6.13%.

TMB is available at the upper end of the IPO price band at 9.1x its FY22 earnings demanding a market cap of Rs. 83,134.5 million. At the upper end of the IPO price band, the issue is priced at a P/BV of 1.4x based on its NAV of Rs. 374.4 as of March 31, 2022. The ROE/ROA for FY22 is 16.58%/1.66%.

TMB is demanding a slight higher valuation when compared to its peers given that TMB is outperforming its peers in majority of financial parameters. Given the consistency in its performance over past periods and healthy return ratio, we recommend a "**Subscribe-Long Term**" rating to this IPO.

Name of the Company	Total Revenue (₹ in million)	Face Value (₹)	P/E	EPS (Basic) (₹)	Return on Net Worth (%)	NAV per share (₹)	P/B
Tamilnad Mercantile Bank	46,564.4	10	9.1	57.67	15.40%	374.41	1.4
City Union Bank	48,638.6	1	13	10.29	11.54%	89.05	1.5
CSB bank Ltd	22,851.1	10	8	26.43	17.29%	152.78	1.4
DCB Bank Ltd	39,648.0	10	7.5	9.26	7.10%	130.15	0.5
Federal Bank Ltd	165,024.6	2	10	9.52	10.21%	91.58	1.1
Karur Vysya Bank Ltd	63,567.3	2	5.5	8.42	8.86%	94.95	0.5
Karnataka Bank Ltd	71,755.4	10	3.4	16.36	7.16%	227.98	0.2
RBL Bank Ltd	1,07,963.70	10	-	-2.77	-1.33%	209.01	0.6
South Indian Bank Ltd	76,204.3	1	36	0.21	0.77%	27.97	0.3

Parameters (FY22)	Tamilnad Mercantile Bank	City Union Bank	Catholic Syrian bank	DCB	Federal Bank	Karur Vysya Bank	Karnataka Bank	RBL Bank	South Indian Bank
GNPA (In ₹ million)	5,709.2	19,331.8	2,895.1	12,899.3	41,367.4	34,310.4	22,508.2	27,283.9	36,480.9
GNPA (%)	1.69%	4.70%	1.81%	4.32%	2.80%	5.96%	3.90%	4.40%	5.90%
NNPA (In ₹ million)	3,175.8	11,911.0	1,070.0	5,732.3	13,926.2	12,607.9	13,769.7	8,065.6	17,777.7
NNPA (%)	0.95%	2.95%	0.68%	1.97%	0.96%	2.28%	2.42%	1.34%	2.97%

Parameters (FY22)	Tamilnad Mercantile Bank	City Union Bank	Catholic Syrian bank	DCB	Federal Bank	Karur Vysya Bank	Karnataka Bank	RBL Bank	South Indian Bank
Credit costs/total assets	0.27%	1.00%	0.30%	0.91%	0.50%	0.90%	0.90%	2.70%	1.30%
Credit costs/total assets (FY20-22 avg)	0.68%	1.30%	0.60%	0.90%	0.70%	1.40%	1.30%	2.50%	1.50%
Return on assets	1.66%	1.32%	1.88%	0.68%	0.89%	0.87%	0.57%	-0.07%	0.05%
Return on assets (FY20-22 avg)	1.32%	1.16%	1.00%	0.82%	0.88%	0.57%	0.62%	0.35%	0.07%
Return on equity	16.58%	12.23%	18.98%	7.37%	10.82%	9.25%	7.40%	-0.59%	0.77%
Return on equity (FY20-22 avg)	13.17%	10.76%	10.28%	9.44%	10.79%	6.05%	9.05%	3.16%	1.33%
Tier-1 capital adequacy ratio	20.44%	19.80%	24.40%	15.8 %	14.40%	17.50%	12.70%	16.20%	13.20%

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Ratings Guide (12 months)	Buy	Hold	Sell
Large Caps (>₹300Bn.)	15%	5%-10%	Below 5%
Mid/Small Caps (<₹300 Bn.)	20%	10%-15%	Below 10%

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