

# IPO Report

Choice

“Subscribe with Caution” to  
**Five-Star Business Finance Ltd.**



**Salient features of the IPO:**

- **Five-Star Business Finance Ltd. (FBFL)** is an NBFC-ND-SI providing secured business loans to micro-entrepreneurs and self-employed individuals.
- As of Jun'22', AUM stood at Rs5,297 cr which grew at a CAGR of ~48% from FY18.
- Total issue size stood at Rs1,960 cr which is purely offer for sale.

**Key competitive strengths:**

- Fastest gross term loans growth among its compared peers
- Ability to successfully expand to new underpenetrated geographies through a calibrated expansion strategy
- Strong on-ground collections infrastructure leading to ability to maintain a robust asset quality;
- 100% in-house sourcing, comprehensive credit assessment and robust risk management and collections framework, leading to good asset quality;

**Valuation:** At the higher price band of Rs474, the issue is valued at P/BV 3.6x (on post issue BVPS) which seems expensive.

**Below are few key observations of the issue:**

- Five Star Business Limited (FBFL) was incorporated on May 7, 1984. FBFL is an NBFC-ND-SI providing secured business loans to micro-entrepreneurs and self-employed individuals, each of whom is largely excluded by traditional financing institutions. Based in Chennai Tamil Nadu, the company has a strong presence in south India.
- With a CAGR of 65% (FY17 to FY21), FBFL has the fastest Gross Term Loans among large peers (with more than Rs3,000 cr in Gross Term Loans). Over 95% of the loan portfolio comprises loans from between 1 lakh to 10 lakh in principal amount, with an average ticket size (ATS) of 2.9 Lakh as of June 30, 2022.
- FBFL had an extensive network of 311 branches, as of June' 2022, spread across approximately 150 districts, eight states and one union territory, with Tamil Nadu Andhra Pradesh, Telangana and Karnataka being key states. Such key states collectively accounted for approximately 85% of the branch network by number, as of June' 2022. Approximately 95% of the branches were located in cities and towns with populations up to one million as of June' 2022.
- FBFL primarily offers the customers small loans for business purposes which accounts for Rs3,290 cr (62.1% of Gross Term Loans) as of June, 2022. They also provide loans for asset creation such as home renovation or improvement, or for meeting expenses for significant economic events such as marriage, healthcare and education, which accounted for Rs 2,006 cr (37.9% of Gross Term loans) as of June 30, 2022.

Recommendation	Subscribe with Caution	
Price Band	Rs450-474 per share	
Face Value	Rs1 per share	
Fresh Issue Size	-	
Shares for Fresh Issue	-	
OFS Issue Size	Rs.1,960 cr	
Total Issue Size	Rs1,960 cr	
Bidding Date	Nov 09 ' 2022 - Nov 11 ' 2022	
MCAP at Higher Price Band	Rs13,811 cr	
Book Running Lead Manager	ICICI Securities Ltd., Edelweiss Financial Services Ltd., Kotak Mahindra Capital Company Ltd. and Nomura Financial Advisory and Securities (India) Pvt. Ltd.	
Registrar	KFin Technologies Ltd.	
Industry	Non-Banking Finance	
<b>Retail application money at higher cut-off price per lot</b>		
Number of shares per lot	31	
Application Money	Rs14,694 per lot	
<b>Allocation Detail</b>		
Qualified Institutional Buyers (QIB)	50%	
Non-Institutional Investors (NII)	15%	
Retail Individual Investors (RIIs)	35%	
<b>Shareholding Pattern</b>		
	<b>Pre-Issue</b>	<b>Post Issue</b>
Promoters & promoters group	40.1%	33.7%
Public	59.9%	66.3%
Total	100.0%	100.0%

## Key observations of the issue...conti...

- With a deeper presence in urban and semi-urban as well as in the rural areas, the company generates ~24% yield on its loans, while the CoB is double digit at over 10.5% which translates to NIM ranging from 16-17% over the last three fiscals. The credit rating of FBFL is 'A+' and with the rising interest rate, the company has managed to maintain its NIM and going forward we think that it is likely to remain stable.
- FBFL has recorded good financial numbers in the last three fiscals, with profitability showing a good trend. During Q1FY23, FBFL reported PAT of Rs139 cr (vs. Rs454 cr in FY22 and Rs359 cr in FY21). As a result of better cost management and all loans being secured by the property of the borrowers, predominantly SORP, the company drove the strong profitability during the quarter. The overall asset quality of the book has also improved. GNPA remained stable to 1.1% in Q1FY23 from 1.1% in FY22.
- *FBFL enjoys a better position among South Indian financiers due to its dominant position in the South. Business growth has been remained strong as AUM grew by a CAGR of 65% over the period of FY17-FY21, while annual disbursements has gone down to Rs1,756 cr in FY22 from Rs2,409 cr in FY20. The company strategized its payment by seeing its customers character, collateral and cash flow (3Cs).*
- *At the higher price band of Rs474, the issue is valued at P/BV 3.6x on post issue BVPS of Rs132. At demanded valuation, market cap of the firm is stood at Rs13,811 cr. Return ratios of the firm remained stable (at avg. RoE of 15.1% over FY20-22). Micro finance, the sector that caters to small customers, is becoming increasingly competitive due to the number of competitors in the market and also high inflation are impacting more the low income people in rural regions. However, considering the company's recent performances in the Covid scenario where they continue to posted growth in both top and bottom line, we believe that the company can maintain its growing performances in the future. Financial performance of the company has been remain strong with healthy return ratios, though the valuation at P/BV of 3.6x seems fully priced considering the prevailing valuation of regional small lenders. Industry peer given by the company include Aavas Financer is currently trading at P/BV of 4.9x, Aptus Value Housing is trading at P/BV of 5.6x, and AU Small Bank at P/BV of 4.0x. Though, these peer are not truly comparable on apple-to-apple basis.*

Considering the business profile of the company, intense competition and mounting risk around micro finance sector, we assign 'Subscribe with Caution' rating to the issue.

Companies (Rs cr)	CMP (Rs/sh)	6M R%	12M R%	M Cap	P/BV (x)	NIM (%)	GNPA (%)	NNPA (%)
Five-Star Business Finance Ltd.	474	-	-	13,811	3.6	17.7%	1.1%	0.7%
AAVAS Financer	1,914	-11.8%	-31.4%	15,127	4.9	7.7%	1.1%	0.8%
Aptus Value Housing Finance	317	3.4%	-8.1%	15,794	5.6	14.3%	1.8%	1.3%
AU Small Finance Bank	616	-6.4%	0.8%	41,068	4.0	5.9%	2.0%	0.6%

Companies	P/BV (x)	P/E (x)	BVPS (Rs/sh)	EPS (Rs/sh)	RoE (%)	RoA (%)	CAR (%)	C/I (%)
Five-Star Business Finance Ltd.	3.6	30.5	127	15.6	15.0%	7.5%	69.9%	36.9%
AAVAS Financer	4.9	37.8	383	50.6	13.2%	3.6%	51.9%	30.9%
Aptus Value Housing Finance	5.6	38.0	59	8.3	14.2%	7.3%	83.3%	18.6%
AU Small Finance Bank	4.0	32.6	152	18.9	12.4%	1.8%	21.0%	62.0%

Companies (Rs cr)	RoE (%)	TTM PAT	AUM	Net Worth	Total Assets	D/Ex	Share capital	Face value (Rs/sh)
Five-Star Business Finance Ltd.	15.0%	454	5,297	3,710	6,343	0.7	29	1
AAVAS Financer	13.2%	400	11,894	3,029	11,020	2.8	79	10
Aptus Value Housing Finance	14.2%	415	5,519	2,916	5,684	0.9	99	2
AU Small Finance Bank	12.4%	1259	50,161	10,144	69,078	7.8	315	10

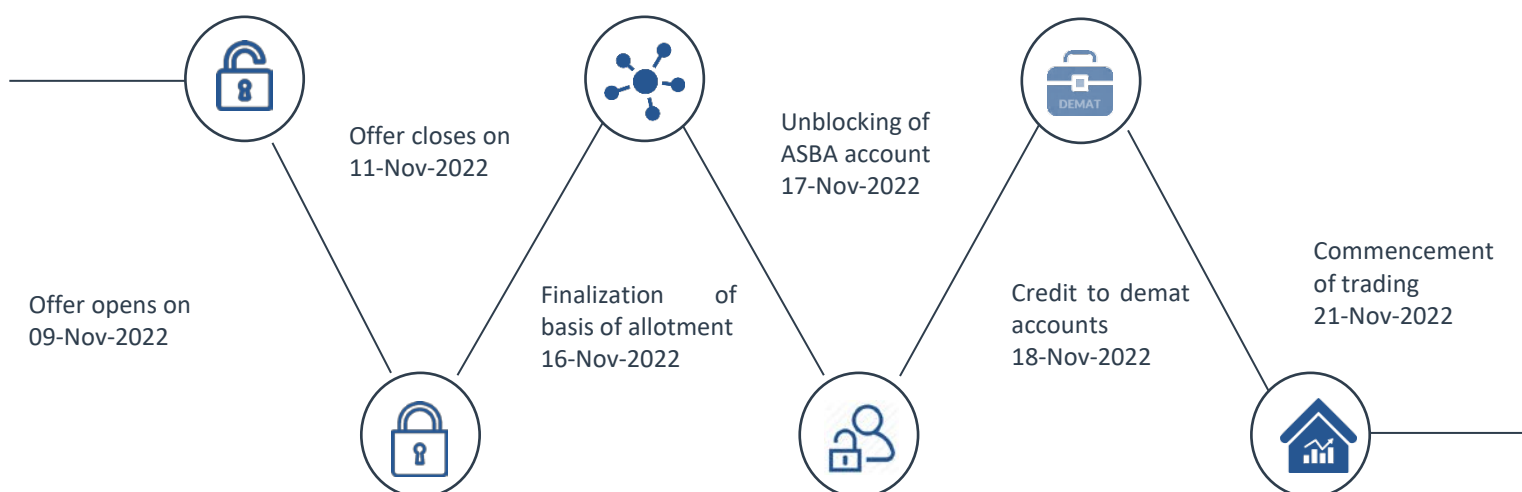
\*- Five-Star Business Finance - PAT, NIM, EPS, return ratios for FY22, Post issue BV

Source: CEBPL

## About the issue:

- Five-Star Business Finance Ltd.(FBFL) is coming out with Initial Public Offering of Rs1,960 cr.
- The issue includes only the offer for sale (OFS) of 4.14 cr shares and no fresh equity shares are being issued.
- The IPO price is fixed at Rs450-Rs474 per share.
- As the higher price band of Rs474, the issue size is stood at Rs1,960 cr.
- The size of the OFS stands at Rs1,960 cr at the higher price band.
- As the Offer is an offer for sale (OFS), FBFL will not receive any proceeds from the Offer.
- The issue will open for subscription on November 09' 2022 and close on November 11' 2022.
- Not more than 50% of the net offer shall be available for allocation on a proportional basis to qualified institutional Investors (QIIs).
- Further not less than 15% shall be available for allocation on a proportional to non-institutional investors (NIIs) and not less than 35% of net offer shall be available for allocation to Retail Institutional Investors (RIIs).
- Anchor book allocation will be placed on November 07' 2022.
- Promoters are selling 4.14 cr of shares through the IPO. Post issue, promoter stake will reduce to 33.65% from the pre-issue of 40.07%.
- PE player namely SCI Investments V is participating in the OFS and are selling 0.35cr shares. SCI Investments V (categories as promoter) held 8.81% stake (pre-issue) in the company.
- Another PE player namely M atrix Partners India Investment Holdings II, LLC (categories as promoter) is selling 1.52cr shares. The said PE player held 12.5% stake on pre-IPO offer basis. Three other PE shareholders Matrix Partners India Investments II Extension, LLC, Norwest Venture Partners X- Mauritius and TPG Asia VII SF Pte. Ltd.Funds are cumulatively fully exiting the company by selling 2.27 cr of shares.

## Indicative IPO process time line:



## Company Introduction & Business Overview:

Five Star Business Limited (FBFL) was incorporated on May 7, 1984. FBFL is an NBFC-ND-SI providing secured business loans to micro-entrepreneurs and self-employed individuals, each of whom is largely excluded by traditional financing institutions. The headquarter is in Chennai, Tamil Nadu with a strong presence in south India, and all of FBFL loans are secured by their borrowers' property, predominantly being SORP. As of June'2022, AUM stood at Rs. 5,296.5cr. FBFL has 230,175 active loan accounts through 311 branches across approximately 150 district, eight states and one union territory, with Tamil Nadu, Andhra Pradesh, Telangana and Karnataka their key states. Such key states collectively accounts for approximately 85% of total branches network as of June'22. With a CAGR of 65% (FY17 to FY21), FBFL has the fastest Gross Term Loans among large peers (with more than Rs. 3,000cr in Gross Term Loans).

FBFL targets customers in Tier 3 and Tier 6 cities as well as in the rural India where they generate income from "everyday" cash and carry business with household net cash flow of approximately Rs. 25K to 40K per month and who can provide collateral. They offer the customers small loans for business purposes which accounts for Rs. 3,290cr (62.12% of Gross Term Loans) as of June 30,2022. They also provide loans for asset creation such as home renovation or improvement, or for meeting expenses for significant economic events such as marriage, healthcare and education, which accounted for Rs. 2,006cr (37.88% of Gross Term loans) as of June 30, 2022. As of Jun'22, effective costs of borrowing (CoB) stood at 10.5% and hold a credit rating of 'A+'. Gross NPA/Net NPA stood at 1.1%/0.7% as of Jun'22.

The company is in its growth phase which we can see in its number where the Interest income has grown by 18.6% in FY22 to Rs. 1,204cr and its profitability has grown by 26.3% to Rs. 454cr. FBFL profitability remained stable and growing because of the optimizing of the cost. As of FY22, FBFL's made disbursement of Rs1,756 cr as compared to Rs1,245 cr in FY21 and Rs2,409 cr in FY20. AUM has rose to Rs5,297 cr in FY22 from Rs. 3,892cr in FY20. In Q1FY23, the company reported PAT of Rs139 cr as compared to Rs454 cr in FY22 and Rs359 cr in FY20. In its latest fiscal , FBFL has reported a RoE of 15% and RoA of 7.5%.

### Key Financials

Particulars (Rs cr)	FY20	FY21	FY22	Q1FY23
Net Interest Income	530	690	903	270
Net Interest Margin	16.7%	16.0%	17.7%	
Total Income	570	726	956	274
Growth (%)		27.3%	31.6%	
Pre-Prov. Operating Profit	399	514	650	186
Adjusted PAT	262	359	454	139
Growth (%)		37.0%	26.3%	
AUM	3,892	4,445	5,067	5,297
RoA		7.1%	7.5%	
RoE	13.5%	16.8%	15.0%	

Source: CEBPL



### Competitive strengths:

- Fastest gross term loans growth among its compared peers
- Maintained a robust asset growth
- Ability to successfully expand to new underpenetrated geographies through a calibrated expansion strategy
- Strong on-ground collections infrastructure leading to our ability to maintain a robust asset quality;
- 100% in-house sourcing, comprehensive credit assessment and robust risk management and collections framework, leading to good asset quality;

### Business strategy:

- Increasing branch networks in existing geographies
- Continue to focus on small business owners and self-employed individuals in Tier 3 and Tier 6 cities in India
- Improve operational efficiency and optimize costs through technology investment
- Focus on Enhancing the Risk Management Framework
- Diversifying borrowing sources to reduce operating expenses and optimize borrowing costs



### Risk and concerns:

- Changing legal and regulatory environment
- Competitive intensity with entrance of the new competitors in the industry
- Geographical & concentration risks.

## Financial statements :

## Profit And Loss Statement

Particulars (Rs cr)	FY20	FY21	FY22	Q1FY23
Interest Income	747	1,015	1,204	335
Growth (%)		35.9%	18.6%	
Interest Expended	217	325	301	65
Growth (%)		49.9%	-7.6%	
Net Interest Income	530	690	903	270
Net Interest Margin	16.7%	16.0%	17.7%	19.2%
Other Income	41	36	52	4
% of Interest Income	5.4%	3.6%	4.4%	1.1%
Total Income	570	726	956	274
Growth (%)		27.3%	31.6%	
Operating & Other expenses	171	212	306	89
Pre-Prov. Operating Profit	399	514	650	186
Provisions and contingencies	50	38	46	-0.4
Operating Profit before Tax	349	476	604	186
Growth (%)		36.4%	26.8%	
Pre-tax Margin %	61.2%	65.6%	63.2%	67.9%
Tax	87	117	151	47
% of PBT	25.0%	24.7%	24.9%	25.1%
Reported PAT	262	359	454	139
Net Profit Margin %	45.9%	49.4%	47.5%	50.8%
Extraordinary Income	0	0	0	0
Adjusted PAT	262	359	454	139
Growth (%)		37.0%	26.3%	

## Balance Sheet

Particulars (Rs cr)	FY20	FY21	FY22	Q1FY23
Cash and balance	451	1,356	880	713
Loans	3,831	4,359	5,102	5,454
Investment	-	-	248	190
Fixed assets	28	25	33	35
Other assets	43	54	80	80
<b>TOTAL ASSETS</b>	<b>4,353</b>	<b>5,794</b>	<b>6,343</b>	<b>6,472</b>
Capital	26	26	29	29
Reserves and Surplus	1,919	2,293	3,681	3,828
Provisions	6	7	9	13
Borrowings	2,364	3,425	2,559	2,520
Other financial liabilities	39	43	65	81
<b>TOTAL CAPITAL AND LIABILITIES</b>	<b>4,353</b>	<b>5,794</b>	<b>6,343</b>	<b>6,472</b>

Source: CEBPL

## Financial Ratios

Particulars	FY20	FY21	FY22	Q1FY23
<b>Return / Profitability Ratios (%)</b>				
Net interest margin (NIM)	16.7%	16.0%	17.7%	19.2%
Cost of borrowings	12.1%	11.5%	10.5%	10.5%
EPS (Diluted) (Rs)	9.0	12.3	15.6	4.8
RoA		7.1%	7.5%	
RoE	13.5%	16.8%	15.0%	
<b>Business Ratios (%)</b>				
AUM (Rs cr)	3,892	4,445	5,067	5,297
Disbursements (Rs cr)	2,409	1,245	1,756	568
CAR (Basel III)	52.9%	58.9%	75.2%	69.9%
Equity / Assets	44.7%	40.0%	58.5%	59.6%
AUM / Assets	89.4%	76.7%	79.9%	81.8%
Cost/Income	39.0%	34.3%	36.9%	32.3%
<b>Asset Quality ratios (%)</b>				
GNPA	1.4%	1.0%	1.1%	1.1%
NNPA	1.1%	0.8%	0.7%	0.7%
<b>Per Share Data (Rs)</b>				
EPS (Diluted)	9.0	12.3	15.6	
BVPS	66.7	79.6	127.3	132.4
<b>Valuation ratios (x)</b>				
P/E (x)	52.7	38.5	30.5	99
P/BV (x)	7.1	6.0	3.7	3.6
<b>Growth ratios (%)</b>				
AUM		14.2%	14.0%	
NII		-4.1%	10.5%	
PAT		37.0%	26.3	

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