

Equitas Small Finance Bank

Refer to important disclosures at the end of this report

Lower LLP drives earning boost, but needs to shore-up PCR

- Equitas SFB reported a beat on PAT at Rs1.7bn (vs our est. of Rs1.2bn) mainly on account of lower provisions, partly offset by flattish margins and higher staff expenses as the bank adds headcount to bolster business growth. Headline NPA ratio moderated to 6.3%, while Bank used Rs0.4bn from the contingent buffer (now at Rs0.6bn/03% of loans).
- Bank has posted strong credit growth at 27% YoY/7% QoQ, largely driven by healthy traction in MFI, VF, SBL and the corporate portfolio. Bank remains confident of delivering growth of ~25%, as demand outlook remains good. It is expanding into newer geographies for growth and has accelerated hiring; although this should keep staff cost elevated in the near term, but will improve business growth/return ratios in the long run.
- The Equitas SFB's reverse merger with Equitas Holdings is nearing completion and Management expects the merged shares (swap ratio at 231:100) to be listed within the next 2 weeks. Further, Founder cum MD & CEO Mr. P N Vasudevan has decided to stay back with the bank and the Board has decided to renew his term for 3 years, from Jul-2023 (subject to RBI approval).
- Factoring-in the better growth/margins and lower LLP, we upgrade our earnings estimate for FY23/24/25 by 10%/3%/1%, respectively, leading to steady improvement in RoA/RoE to 1.7-2%/11-16% over FY23-25E. We retain BUY with revised TP of Rs72/share (up from Rs65 earlier), based on 1.5x Dec-24E ABV.
- Growth accelerates, but margins remain flat amid rising cost pressure:** Equitas SFB reported strong credit growth at 27% YoY/7% QoQ, led by healthy traction in MFI, VF, SBL and the corporate portfolio. The bank expects growth to remain healthy at 25% YoY for FY23, given strong underlying demand. Deposit growth has also been robust, at 31% YoY/8% QoQ, led by acceleration in TDs; this caused CASA to slip to 46%, which albeit remains better than peers. Margin remained flat at a healthy 9%, even amid rising cost pressure. That said, the bank's strategy to diversify its portfolio mix towards secured loans should keep margins in check in the mid-to-long term. We expect the bank to apply for a Universal Banking license post reverse merger of the holdco; this could hasten the portfolio diversification and simultaneously benefit the bank by mobilizing low-cost deposits.
- Slippages remain elevated; Bank needs to boost PCR:** Gross slippages remain elevated at Rs2.9bn/6.3% of loans (vs 7% in Q2 and 8.1% in Q1), mainly due to stress-flow from the restructured book. However, GNPA ratio declined 28bps QoQ to 3.6% due to higher upgrades and credit growth. The restructured pool, too, moderated, to Rs7.3bn/3.1% of loans from 4.5% in Q2. Bank has utilized Rs0.4bn in Q3 and the overall contingent buffer now stands at 0.6bn/0.3% of loans. Bank's PCR remains low at 50%, which it plans to raise to 60% within the next 4-5 quarters amid looming ECL norms.
- Outlook and Valuations:** Accounting for the better growth/margins and lower LLP, we upgrade our FY23E/24E/25E earnings by 10%/3%/1%, leading to steady improvement in RoA/RoE to 1.7-2%/11-16% over FY23-25E, respectively. We retain BUY, with revised TP of Rs72/sh (up from Rs65 earlier), based on 1.5x Dec-24E ABV. We welcome the decision of the Founder cum MD & CEO of revoking his resignation, but believe the bank needs to strengthen top-management bandwidth as part of the succession plan, to minimize Management-transition risk in future. **Key risks:** Higher-than-expected NPA formation; faster margin contraction; higher provisions in case of new ECL norms given lower PCR.

Financial Snapshot (Standalone)

(Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net income	22,160	25,761	30,988	37,321	45,999
Net profit	3,842	2,807	5,153	6,803	9,282
EPS (Rs)	3.5	2.3	4.1	5.4	7.4
ABV (Rs)	29.0	32.5	35.6	41.4	48.8
RoA (%)	1.7	1.1	1.7	1.8	2.0
RoE (%)	12.5	7.3	11.4	13.3	15.7
PE (x)	16.6	24.7	14.1	10.7	7.8
P/ABV	2.0	1.8	1.6	1.4	1.2

Source: Company, Emkay Research

CMP	Target Price
Rs 58 as of (February 9, 2023)	Rs 72 (▲) 12 months
Rating	Upside
BUY (■)	24.1 %

Change in Estimates

EPS Chg FY23E/FY24E (%)	10.3/ 2.5
Target Price change (%)	10.8
Target Period (Months)	12
Previous Reco	BUY

Emkay vs Consensus

EPS Estimates		
	FY23E	FY24E
Emkay	4.1	5.4
Consensus	4.2	5.9
Mean Consensus TP (12M)	Rs 69	

Stock Details

Bloomberg Code	EQUITASB IN
Face Value (Rs)	10
Shares outstanding (mn)	1,255
52 Week H/L	64 / 37
M Cap (Rs bn/USD bn)	73 / 0.88
Daily Avg Volume (nos.)	3,061,201
Daily Avg Turnover (USD mn)	2.1

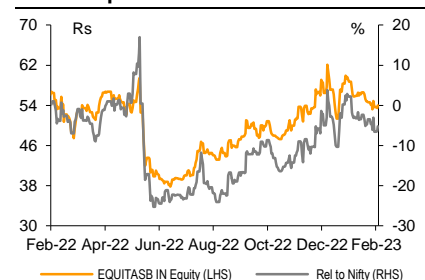
Shareholding Pattern Dec '22

Promoters	74.5%
FIIIs	4.1%
DIIIs	15.4%
Public and Others	6.1%

Price Performance

(%)	1M	3M	6M	12M
Absolute	1	13	32	3
Rel. to Nifty	3	14	29	1

Relative price trend



Source: Bloomberg

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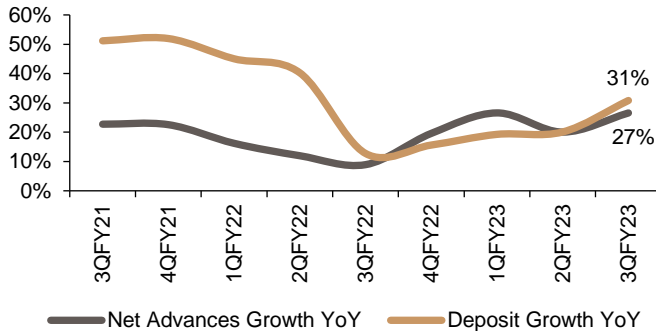
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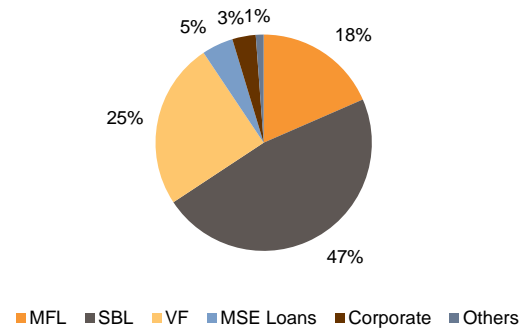
Story in Charts

Exhibit 1: Credit growth accelerates, led by healthy traction in MFI, VF, SBL and the Corporate portfolio



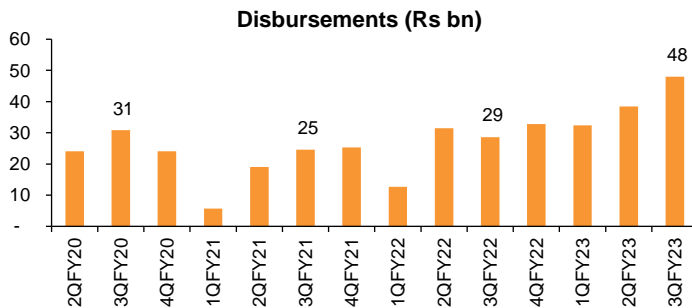
Source: Company, Emkay Research

Exhibit 2: Bank has gradually diversified its portfolio towards non-MFI



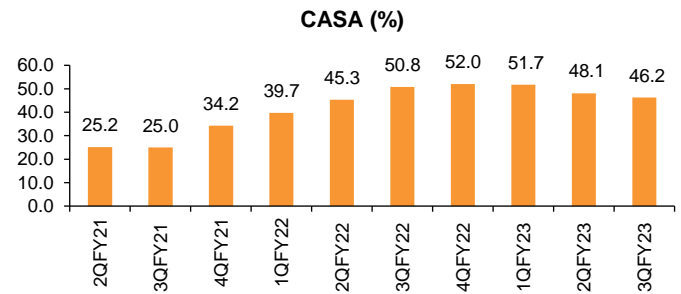
Source: Company, Emkay Research

Exhibit 3: Bank achieved its highest-ever quarterly disbursements



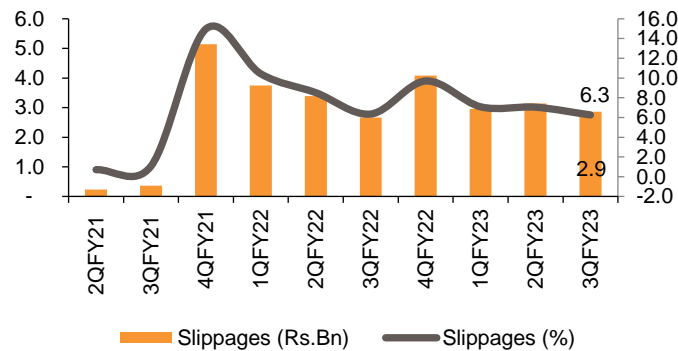
Source: Company, Emkay Research

Exhibit 4: CASA cannibalization led to moderation in CASA ratio



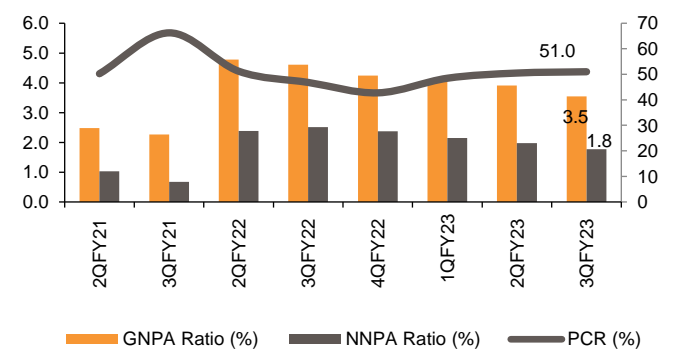
Source: Company, Emkay Research

Exhibit 5: Slippages remain elevated due to stress flow from the restructured book



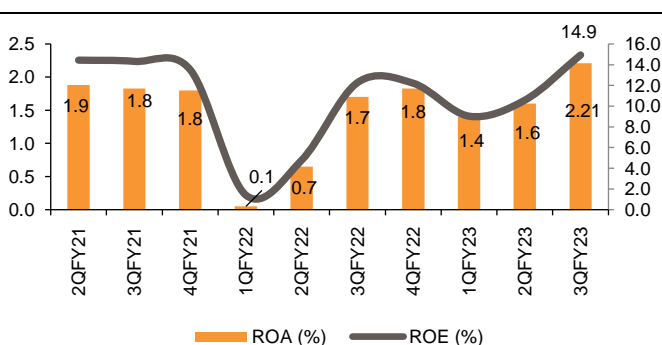
Source: Company, Emkay Research

Exhibit 6: Overall GNPA ratio declined 28bps QoQ to 3.6% due to strong upgrades and healthy growth



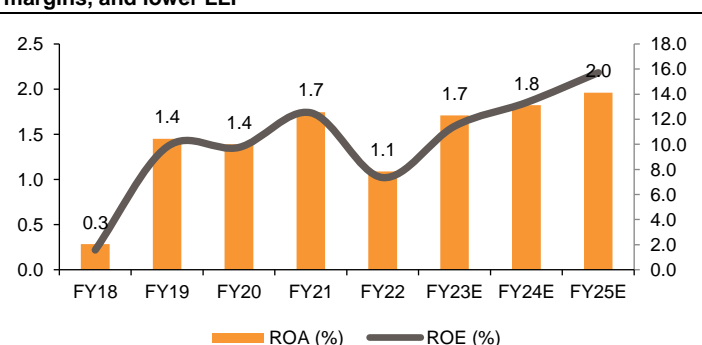
Source: Company, Emkay Research

Exhibit 7: Lower provisions led to higher RoA



Source: Company, Emkay Research

Exhibit 8: RoA/RoE improvement to be led by better growth, margins, and lower LLP



Source: Company, Emkay Research

Exhibit 9: Actuals vs. Estimates (Q3FY23)

Rs mn	Actuals	Estimates		Variation		Comments
		Emkay	Consensus	Emkay	Consensus	
Net income	8,001	7,816	8,183	2%	-2%	Better than expected margins led to a beat
PPOP	2791	2548	2,777	10%	1%	Higher Net income led to a beat
PAT	1,701	1,220	1,476	39%	15%	Lower provisions led to a beat

Source: Company, Emkay Research

Exhibit 10: Quarterly Summary

Rs mn	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	FY22	FY23E	YoY (%)
Interest Earned	9,009	8,958	9,404	10,024	10,634	18	6	34,597	41,456	20
Interest Exp	3,601	3,434	3,598	3,927	4,159	15	6	14,211	16,295	15
Net Interest Income	5,408	5,525	5,806	6,097	6,475	20	6	20,385	25,161	23
Global NIMs (reported)	9.1	9.1	9.1	9.0	9.0	-8bps	1bps	8.3	8.8	48bps
Non-interest Income	1,341	1,481	1,332	1,450	1,526	14	5	5,376	5,827	8
Operating Expenses	4,502	4,167	4,456	5,124	5,210	16	2	17,041	20,270	19
Pre Provisioning Profit	2,247	2,839	2,682	2,423	2,791	24	15	8,719	10,719	23
Provision & Contingencies	784	1,232	1,416	901	499	-36	-45	4,938	3,832	-22
PBT	1,463	1,607	1,266	1,522	2,292	57	51	3,781	6,886	82
Income Tax Expense (Gain)	382	412	296	358	591	55	65	974	1,733	78
Net Profit/(Loss)	1,081	1,195	970	1,164	1,701	57	46	2,807	5,153	84
Gross NPA (%)	4.6	4.2	4.1	3.9	3.6	-98bps	-28bps	4.24	3.29	-95bps
Net NPA (%)	2.5	2.4	2.2	2.0	1.8	-69bps	-15bps	2.47	1.67	-80bps
Deposits (Rs bn)	179	190	204	217	234	31	8	190	247	30
Net Advances (Rs bn)	187	197	209	223	237	27	6	194	243	25

Source: Company, Emkay Research

Exhibit 11: Revision in estimates

Y/E Mar (Rs mn)	FY23E			FY24E			FY25E		
	Earlier	Revised	Change	Earlier	Revised	Change	Earlier	Revised	Change
Net income	30,610	30,988	1.2%	37,139	37,321	0.5%	45,917	45,999	0.2%
PPOP	10,403	10,719	3.0%	13,228	13,405	1.3%	17,851	17,824	-0.2%
PAT	4,673	5,153	10.3%	6,635	6,803	2.5%	9,170	9,282	1.2%
EPS (Rs)	3.7	4.1	10.3%	5.3	5.4	2.5%	7.3	7.4	1.2%
BV (Rs)	38	38	0.9%	43	43	1.1%	50	51	1.1%

Source: Company, Emkay Research

Exhibit 12: Key Assumptions

(%)	FY22A	FY23E	FY24E	FY25E
Loan Growth	15.0	25.2	25.0	30.1
Deposit Growth	15.6	30.2	29.9	32.4
NIM	8.3	8.8	8.6	8.4
GNPA	4.2	3.3	2.8	2.4
Credit Cost	2.7	2.3	1.8	1.5

Source: Emkay Research

Exhibit 13: Key ratios and trends

	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23
Loans (Rs bn)	168	168	167	178	183	194	205	218	233
-Growth (% YoY)	22.7	22.6	16.2	12.0	8.9	15.0	22.5	22.4	27.1
-Growth (% QoQ)	5.6	0.2	-0.8	6.7	2.7	5.8	5.7	6.6	6.6
Liability Profile									
Deposit	158,620	163,920	170,950	180,940	178,840	189,508	203,860	217,262	233,930
Deposit (Rs bn)	159	164	171	181	179	190	204	217	234
-Growth (% YoY)	51.2	51.9	45.0	40.3	12.7	15.6	19.3	20.1	30.8
-Growth (% QoQ)	23.0	3.3	4.3	5.8	-1.2	6.0	7.6	6.6	7.7
Asset Quality (%)									
GNPA	2.3	3.7	4.8	4.8	4.6	4.2	4.1	3.9	3.6
NNPA	0.7	1.6	2.4	2.5	2.5	2.4	2.2	2.0	1.8
PCR	66.2	58.6	51.2	50.1	46.8	42.7	48.5	50.5	50.8
Slippages (Rs mn)	365	5,146	3,749	3,391	2,668	4,086	3,380	3,140	2,865
Slippages - annualized (%)	1.1	15.0	10.4	8.5	6.3	9.7	8.1	7.0	6.3
ROE Decomposition (%)									
NII	8.0	7.2	7.4	7.6	8.5	8.5	8.4	8.4	8.4
Other Income	2.4	2.8	1.7	2.3	2.1	2.3	1.9	2.0	2.0
Opex	5.9	6.0	6.4	6.9	7.1	6.4	6.4	7.0	6.8
PPOP	4.6	4.0	2.6	3.1	3.5	4.3	3.9	3.3	3.6
Provisioning Cost	2.1	1.5	2.4	2.2	1.2	1.9	2.0	1.2	0.6
PBT	2.5	2.4	0.2	0.9	2.3	2.5	1.8	2.1	3.0
Tax	0.6	0.6	0.0	0.2	0.6	0.6	0.4	0.5	0.8
ROA	1.8	1.8	0.2	0.6	1.7	1.8	1.4	1.6	2.2
Leverage (x)	7.4	7.4	7.3	7.3	7.1	6.1	6.4	6.5	6.7
ROE	13.5	13.3	1.4	4.8	12.1	11.3	8.9	10.4	14.7

Source: Company, Emkay Research

Key Financials (Standalone)**Income Statement**

Y/E Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net interest income	17,980	20,385	25,161	30,625	38,293
Other income	4,181	5,376	5,827	6,696	7,706
Fee income	265	381	457	572	715
Net income	22,160	25,761	30,988	37,321	45,999
Operating expenses	13,294	17,041	20,270	23,915	28,175
Pre provision profit	8,866	8,719	10,719	13,405	17,824
PPP excl treasury	8,419	8,293	10,377	13,064	17,483
Provisions	3,753	4,938	3,832	4,314	5,420
Profit before tax	5,113	3,781	6,886	9,091	12,404
Tax	1,270	974	1,733	2,288	3,122
Tax rate	25	26	25	25	25
Profit after tax	3,842	2,807	5,153	6,803	9,282

Balance Sheet

Y/E Year End (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Equity	11,393	12,520	12,540	12,540	12,540
Reserves	22,571	29,941	35,094	41,897	51,179
Net worth	33,963	42,462	47,634	54,437	63,719
Deposits	163,920	189,508	246,647	320,375	424,229
Borrowings	41,653	26,164	26,687	25,353	24,085
Total liabilities	247,085	269,519	333,341	413,736	532,956
Cash and bank	5,148	9,570	10,048	10,551	11,078
Investments	37,052	44,498	57,773	73,013	94,597
Loans	168,482	193,742	242,587	303,205	394,491
Others	5,914	7,949	9,005	11,027	12,344
Total assets	247,085	269,519	333,341	413,736	533,056

Key Ratios (%)

Y/E Year End	FY21	FY22	FY23E	FY24E	FY25E
NIM	8.6	8.3	8.8	8.6	8.4
Non-II/avg assets	1.9	2.1	1.9	1.8	1.6
Fee income/avg assets	0.1	0.1	0.2	0.2	0.2
Opex/avg assets	6.0	6.6	6.7	6.4	6.0
Provisions/avg assets	1.7	1.9	1.3	1.2	1.1
PBT/avg assets	2.3	1.5	2.3	2.4	2.6
Tax/avg assets	0.6	0.4	0.6	0.6	0.7
RoA	1.7	1.1	1.7	1.8	2.0
RoAE	12.5	7.3	11.4	13.3	15.7
GNPA (%)	3.7	4.2	3.3	2.8	2.4
NNPA (%)	1.7	2.5	1.7	1.1	0.9

Per Share Data (Rs)	FY21	FY22	FY23E	FY24E	FY25E
EPS	3.5	2.3	4.1	5.4	7.4
BVPS	29.8	33.9	38.0	43.4	50.8
ABVPS	29.0	32.5	35.6	41.4	48.8
DPS	0.0	0.0	0.0	0.0	0.0

Valuations (x)	FY21	FY22	FY23E	FY24E	FY25E
PER	16.6	24.7	14.1	10.7	7.8
P/BV	2.0	1.7	1.5	1.3	1.1
P/ABV	2.0	1.8	1.6	1.4	1.2
P/PPOP	7.5	8.3	6.8	5.4	4.1
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0

Source: Company, Emkay Research

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Growth (%)	FY21	FY22	FY23E	FY24E	FY25E
NII	20.2	13.4	23.4	21.7	25.0
PPOP	48.3	(1.7)	22.9	25.1	33.0
PAT	57.6	(26.9)	83.6	32.0	36.4
Loans	22.6	15.0	25.2	25.0	30.1

Quarterly (Rs mn)	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23
NII	5,408	5,525	5,806	6,097	6,475
NIM (%)	9.1	9.1	9.1	9.0	9.0
PPOP	2,247	2,839	2,682	2,423	2,791
PAT	1,081	1,195	970	1,164	1,701
EPS (Rs)	0.94	0.95	0.77	0.93	1.36

Source: Company, Emkay Research

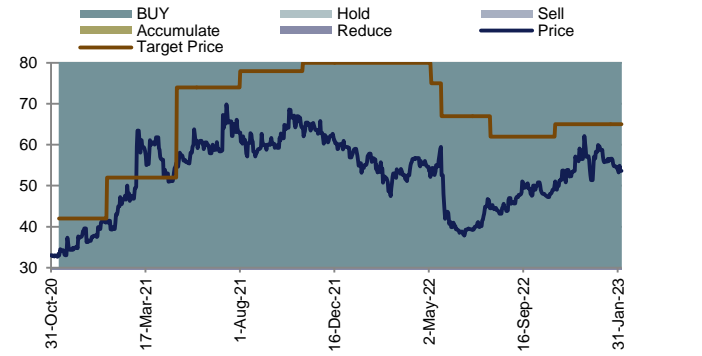
Shareholding Pattern (%)	Feb-22	Mar-22	Jun-22	Sep-22	Dec-22
Promoters	74.6	74.6	74.5	74.5	74.5
FIIIs	3.6	3.6	4.1	4.3	4.1
DIIIs	17.0	16.7	15.6	15.4	15.4
Public and Others	4.8	5.1	5.8	5.9	6.1

Source: Capitaline

RECOMMENDATION HISTORY (Rs/share)

Date	Closing Price	TP	Period (months)	Rating	Analyst
1-Nov-22	51	65	12m	Buy	Anand Dama
30-Jul-22	45	62	12m	Buy	Anand Dama
20-May-22	53	67	12m	Buy	Anand Dama
5-May-22	54	75	12m	Buy	Anand Dama
22-Mar-22	54	80	12m	Buy	Anand Dama
1-Feb-22	56	80	12m	Buy	Anand Dama
31-Oct-21	64	80	12m	Buy	Anand Dama
1-Aug-21	63	78	12m	Buy	Anand Dama
1-May-21	56	74	12m	Buy	Anand Dama
29-Jan-21	39	52	12m	Buy	Anand Dama
20-Jan-21	41	52	12m	Buy	Anand Dama
11-Nov-20	33	42	12m	Buy	Anand Dama

Source: Company, Emkay Research

RECOMMENDATION HISTORY (Rs/share)

Source: Bloomberg, Company, Emkay Research

Emkay Rating Distribution

Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

Completed Date: 09 Feb 2023 23:13:31 (SGT)
Dissemination Date: 09 Feb 2023 23:14:31 (SGT)

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