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IPO Report

06th Feb'24

Snapshot

Capital Small Finance bank commenced operations as India's first small finance bank in 2016 pursuant to RBI's approval dated March 4, 2016. Bank offer a range of banking products on the asset and liability side, in all the states bank operate in, i.e., Punjab, Haryana, Delhi, Rajasthan, Himachal Pradesh and Union Territory of Chandigarh. SFB's asset products primarily include agriculture loans, MSME and trading loans (working capital, machinery loans etc.) and mortgages (housing loans and loans against property)

VALUATION

Company is bringing the issue at price band of Rs 445-468 per share at p/b multiple of 1.81x on post issue book value basis. Company's retail focused liability franchise with high Share of CASA & has secured and diversified advances portfolio. Company's streamlined credit assessment processes and risk management practices has customer centric approach and understanding of target customers. Company's Consistent track record of growth with constantly improving operational and profitability metrics & has professional and experienced leadership team. Hence ,looking after all above we recommend "Subscribe" on issue.

Price Band (Rs./Share)	445-468
Opening date of the issue	07th Feb '2024
Closing Date of the issue	09th Feb '2024
No of shares pre issue	35427136 Eq Shares
Issue Size	Rs 519-523 Cr
Fresh issue	Rs 450 Cr
Offer For Sale	1,561,329 Eq Shares
Face Value (Rs/ share)	Rs 10/share
Bid Lot	32

BIDDING DETAILS

QIBs (Including Anchor)	50% of the offer (Approx 5588356 Eq Shares)
Non-Institutional	15% of the offer (Approx 1676507 Eq Shares)
Retail	35 % of the offer (Approx 3911850 Eq Shares)
Employee Reservation	18,75,420 Equity Shares
Lead managers	Nuvama Wealth, DAM Capital, Equirus Capital
Registrar to the issue	Link Intime India Pvt Ltd

WHAT WE LIKE

Retail focused liability franchise with a high share of CASA

Bank have created a retail centric deposit franchise with a high share of CASA deposits with CASA ratio increasing from 40.08% in Fiscal 2021 to 41.88% in Fiscal 2023. Bank's experience of operating as a local area bank for over 16 years provides it a competitive edge with respect to its understanding on growing its deposit base. Bank's holistic suite of banking products, deeply relationship-based banking approach, entrenched branch network, single window service, customer friendly practices and brand equity has aided retail centric deposit profile

Consistent track record of growth with constantly improving operational and profitability metrics

Since its conversion into an SFB, bank have demonstrated consistent improvement in bank's financial metrics such as total advances growth, deposit growth, increasing C/D Ratio, improving cost to income ratio and profitability. Bank's CASA deposits as of the six months ended September 30, 2023 and Fiscals ended March 31, 2023, 2022 and 2021 were ₹ 26,433.61 million, ₹ 27,478.96 million, ₹ 25,494.01 million and ₹ 20,926.34 million, respectively. Bank's average credit to deposits ratio has also improved from 67.51% in Fiscal 2021 to 77.96% in Fiscal 2023 to 79.61% as on the six months ended September 30, 2023. Bank's efficiency ratios have also been continuously improving.

Secured and diversified advances portfolio

Bank have consciously focused on building a secured and granular loan book over the years with a focus on income generation. As on March 31, 2023 and September 30, 2023, 99.82% and 99.85% of bank's loan book, being ₹ 54,975.90 million and ₹ 58,571.93 million was secured with 85.16% and 84.26% respectively of the loans being secured with immovable properties. Bank have a welldiversified portfolio across products (agricultural, MSME and trading, mortgage lending and other products) which helps bank to mitigate risk and optimise its resources



COMPANY BACKGROUND

Bank have an experience of over two decades in the banking industry, having been incorporated in 1999. Company is regulated by RBI and are one out of the two non-NBFC microfinance entities to receive the SFB license in 2015. Bank's core strategy is to strengthen its retail focused banking franchise by enabling access to affordable credit in the states company operate in its well defined niche catering to middle income group segment with special emphasis on rural and semi-urban areas. As on date, bank do not have any subsidiaries. Bank focus primarily on the middle-income customer segments i.e., customers with an average annual income of ₹ 0.4 million to ₹ 5 million in semi-urban and rural areas with 41.62% of bank's branches in rural areas, 34.68% branches in semi-urban areas and 23.70% of its branches in urban areas as on September 30, 2023. Since bank focus primarily on the middle-income customer segments, bank's full suite of products and services on the asset and liability side will provide it an opportunity to serve more customers in the middle-income segment that have limited or no access to formal banking channels, spread across rural and semiurban areas.

Bank's background as a local area bank helped it in understanding needs of its target customers but restricted its geographical 204 outreach. Post conversion into a small finance bank, bank have been able to expand its operations into new and contiguous geographies which has enabled bank to widen its customer base and resulted in improved operational and business metrics.

The expansion of bank's business has been a major factor in the growth of its advances and deposits. Over the years, bank have expanded its operations strategically in the north Indian states of Punjab, Haryana, Rajasthan, Delhi, Himachal Pradesh and Union Territory, Chandigarh. As of September 30, 2023, bank was present in five States and one Union Territory with 173 branches and 175 ATMs with 76.30% of its branches located in rural and semi-urban areas covering 24 districts and 75.75% of bank's total customers (both credit and deposit). Bank plan to continue to expand its business.

Bank have diversified portfolio with sizeable book in multiple asset classes with proportion of secured lending of 99.85% as on September 30, 2023. Bank have average gross NPA ratio of 2.52% and average net NPA ratios of 1.30% with negligible write offs as a percentage of loan book for previous three Fiscals and first half of current fiscal year from Fiscal 2021 to six months period ended September 30, 2023. Bank also had consistent asset quality in the range of 2-3% from Fiscal 2021 to six months period ended September 30, 2023.

Bank have shown an increasing trend in profit after tax, RoA and RoE for both Fiscals 2022 and Fiscals 2023 depicting its consistent performance. Bank's retail deposits (as a % of total deposits), and CASA deposits stood at 97.90%, and 41.88%, as on March 31, 2023 and 93.59%, and 37.76%, as on September 30, 2023, respectively. Further, bank's percentage of gross NPAs to total advances have been 2.73% as on September 30, 2023 and 2.77%, 2.50% and 2.08% for the Fiscals ended March 31, 2023, 2022 and 2021, respectively. Bank target to be the primary banker to its customers and endeavour to achieve this objective through a mix of (i) suite of its product offerings; (ii) customer service orientation; (iii) deeply entrenched physical branch network; and (iv) evolving digital channels of service delivery. Bank generate fee income from products and services such as forex and money transfer, outward remittances, safe-deposit lockers, distribution of life insurance and general insurance products, 3-in-1 demat and trading account and other ancillary services.

As on September 30, 2023 and March 31, 2023 respectively, 99.85% and 99.82% of bank's loan book was secured with 84.26% and 85.16% of the loans secured by immovable properties. Further, bank have strategically focused on building a granular loan book. Since Fiscal 2021, bank's loans with ticket size of up to ₹ 2.5 million have increased from 62.88% of its total loan book to 67.80% in Fiscal 2023 and stood at 67.44% as on September 30, 2023. Bank's cost of funds was 5.11% and 5.68% for Fiscal 2023 and for the period ended September 30, 2023, respectively. It is the lowest interest paying SFB where-in rate of interest for retail term deposits inches up to only 7.60% whereas others offer a higher rate across some of the tenors in retail deposits.

Bank offer saving bank deposit rate of 3.50% irrespective of the amount of saving deposit as compared to other banks which have different saving bank deposit rates for various buckets. Further, bank have the lowest cost of deposit amongst comparable SFBs. As of March 31, 2023, bank had lowest cost of deposit (4.94%) followed by AU SFB (5.48%) and Ujjivan SFB (6.00%). (Source: CRISIL MI&A Report).



INVESTMENT RATIONALE

<p><i>Secured and diversified advances portfolio</i></p>	<p>Bank have consciously focused on building a secured and granular loan book over the years with a focus on income generation. As on March 31, 2023 and September 30, 2023, 99.82% and 99.85% of bank's loan book, being ₹ 54,975.90 million and ₹ 58,571.93 million was secured with 85.16% and 84.26% respectively of the loans being secured with immovable properties. Bank have a well diversified portfolio across products (agricultural, MSME and trading, mortgage lending and other products) which helps bank to mitigate risk and optimise its resources. Bank focus on the middle-income group segment and aim to be the primary banker of its customers. With this endeavour, bank offer a full suite of products and services on the asset and liability side to address its customer needs. The average ticket size of bank's agriculture, MSME & trading and mortgage lending products was ₹ 1.23 million, ₹ 1.82 million and ₹ 1.16 million as of March 31, 2023 and the same stood at ₹1.24 million, ₹ 1.81 million and ₹ 1.15 million as on September 30 2023 respectively. Further, a well-diversified loan portfolio with focus on income generation, bank's continued focus on secured lending, continuous customer engagement and structured underwriting practices has contributed to bank's growth and superior asset quality as compared to other SFBs.</p>
<p><i>Streamlined credit assessment processes and risk management practices</i></p>	<p>Bank's credit assessment processes and risk management practices enables it to maintain good asset quality and low delinquencies. Bank's strategy of secured lending, primarily for productive purposes and conservative loan to value ratio contributes towards lower delinquencies and credit losses. Bank's positioning as the primary banker to most of its customers enables it to have a comprehensive view of and control over their cash flows contributing towards effective credit assessment. Bank's credit assessment involves multiple levels of independent review of information. Bank follow the principal of four eyes which involves a multi-level review of the credit exposures along with a well-defined matrix for credit assessment which is dependent on the risk profile of the borrower, including the mandatory checks of credit bureau verification, review of defaulters list and check on frauds. Further, bank have a credit sanctioning committee which oversees the exposures of an amount involving ₹ 12.50 million or above and a dedicated team to monitor the exposures granted by bank. Bank follow a principle of secured lending which has resulted in maintaining high asset quality. Bank's advances stood at ₹ 55,072.67 million, and ₹ 58,659.37 million with 99.82% and 99.85% of it being secured loans as of March 31, 2023 and as of September 30, 2023 with an average ticket size of ₹ 1.34 million and ₹ 1.37 million respectively. Bank have also had a consistent asset quality in the range of 2%-3% from Fiscal 2021 to the six months ended September 30, 2023 as compared other peers in the SFB space.</p>
<p><i>Customer centric approach and understanding of target customers</i></p>	<p>Bank's main focus is on providing its products and services to catering to middle income group segment with special emphasis on rural and semi-urban areas in bank's areas of operations. Bank is a one-stop financial hub for its customers where bank operate. As of March 31, 2023 and September 30, 2023, bank had 7,01,071 and 7,25,037 customers respectively (both credit and deposit). Further, as on September 30, 2023, bank had 173 branches and 175 ATMs with 76.30% bank's branches located in rural and semi-urban areas. As the majority of its customers are individuals from middle-income group segments, bank have designed its products in a manner such that they are simple to understand, which contributes to their popularity amongst customers. Bank strategically follow branch network driven business acquisition strategy which helps it to identify the customer needs effectively and respond with solutions.</p>



OBJECTS OF OFFER

Offer for Sale

Each of the Selling Shareholders will be entitled to their respective portion of the proceeds from the Offer for Sale in proportion of the Equity Shares offered by the respective Selling Shareholders as part of the Offer for Sale. Bank will not receive any proceeds from the Offer for Sale.

Objects of the Offer

In terms of the SFB Licensing Guidelines, Bank is required to maintain a minimum capital adequacy ratio of 15% of its risk weighted assets on a continuous basis, subject to any higher percentage as may be prescribed by RBI from time to time, and bank's Tier - I capital is required to be at least 7.5% of the risk weighted asset.

RISKS

Bank have certain contingent liabilities, including guarantees given by bank on behalf of its customers in India which constituted 81.14% of the total contingent liabilities of Bank as of September 30, 2023. If these contingent liabilities materialise, bank's financial condition, cash flows and results of operations may be adversely impacted.

Source:RHP

INDUSTRY OVERVIEW

Indian housing finance market

The Indian housing finance market clocked a healthy ~15% CAGR (growth in loans outstanding) over fiscals 2016-2023 on account of a rise in disposable income, healthy demand and a greater number of players entering the segment. Indian Housing Finance market witnessed low disbursements in the first quarter of Fiscal 2021 on account of pandemic, however the overall market grew by 14% in Fiscal 2022 due to improved affordability, pent-up demand and historically low interest rates. In Fiscal 2023, despite the aggressive rate hikes by RBI, the credit growth for Indian Housing Finance market stood at 18% year on year on account of pentup housing demand and focus on increase in housing penetration in Tier I and Tier II cities. Rise in disposable income: India's per capita income grew at a 10% CAGR between fiscal 2012 and 2020. Healthy demand emanating from smaller markets: Faster growth in smaller districts and relatively muted demand for high ticket housing in metros have led to increased share of smaller districts (tier-II and below cities) in housing loans over the last couple of years.

Housing finance (loans with ticket size between Rs 0.5 to 5 million) sector witnessing encouraging trends; to grow by 14-16% up to fiscal 2026 Housing loans (0.5 to 5 million) logged a CAGR of ~14% during fiscals 2016-2023. This was largely because of the government's increased focus on the housing loans (up to Rs. 5.0 mn) segment. Housing loan portfolio of ticket size (Rs. 0.5 – 5.0 million) grew by 13.9% in Fiscal 2023 due to pent up demand in housing as affordability, though deteriorating, continues to be favourable. CRISIL MI&A forecasts housing credit market for ticket size Rs 0.5 to 5 million to grow at 14-16% between fiscal 2023 and 2026 on account of increase in capital values and incremental construction under PMAY. The outstanding portfolio of housing loans of ticket size Rs 0.5 to 5 million constitutes 66% of the overall housing market as of fiscal 2023, hence CRISIL expects this ticket size segment to support growth of overall housing segment.



Consolidated Financials

(Rs in Mn)

Financials (Mn)	FY21	FY22	FY23	H1FY24
Total Income	2444.45	3094.65	3714.58	2002.08
Total Expenses	1729.59	1962.53	2227.54	1248.24
Pre Provision Profit	714.86	1132.12	1487.04	753.84
Provisions	307.02	506.45	551.08	209.93
PBT	407.84	625.67	935.96	543.91
Tax	0.00	0.00	0.00	0.00
PAT	407.84	625.67	935.96	543.91
Eq Cap	339.10	340.44	342.52	353.51
Net Worth	4,507.90	5,157.81	6,106.10	4,507.90
EPS	12.0	18.4	27.3	15.4
Book value	132.94	151.50	178.27	201.34
NIM %	3.36	3.74	4.19	4.04
Cost of Funds	5.83	5.20	5.11	5.68
ROE%	9.04	12.13	15.33	7.64
ROA%	0.69	0.92	1.22	1.28
Credit Cost%	0.3	0.42	0.32	0.08

(Source: RHP)

Peer Comparison

Company Name	Face value	EPS	NAV	P/E	P/B	RONW %
<i>Capital Small Finance Bank Limited</i>	<i>10.00</i>	<i>27.21</i>	<i>178.27</i>	<i>--</i>	<i>--</i>	<i>15.33</i>
Peers						
AU Small Finance Bank Limited	10	21.74	164.64	35.47	4.71	13.00
Suryoday Small Finance Bank Limited	10	7.32	149.28	24.21	1.19	4.90
Credit Access Grameen Limited	10	52.04	326.89	32.66	5.20	16.18
Spandana Sphoorty Financial Limited	10	1.74	436.58	665.52	2.65	0.40
Bandhan Bank Limited	10	13.62	121.58	16.87	1.89	11.21
Ujjivan Small Finance Bank Limited	10	5.87	21.27	10.15	2.81	26.45
Equitas Small Finance Bank Limited	10	4.67	46.44	24.21	2.46	11.21
Fusion Micro Finance Limited	10	43.13	230.74	14.68	2.75	16.67
Utkarsh Small Finance Bank Limited	10	4.51	22.33	13.51	2.73	20.22



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