

ESAF Small Finance Bank Limited

September 02, 2025

Facilities/Instruments	Amount (₹ crore)	Rating ¹	Rating Action
Lower Tier II	150.00	CARE A-; Negative	Downgraded from CARE A; Negative
Lower Tier II	130.00	CARE A-; Negative	Downgraded from CARE A; Negative
Lower Tier II	500.00	CARE A-; Negative	Downgraded from CARE A; Negative
Tier II Bonds	20.00	CARE A-; Negative	Downgraded from CARE A; Negative
Tier II Bonds	-	-	Withdrawn
Certificate Of Deposit	500.00	CARE A1	Downgraded from CARE A1+

Details of instruments in Annexure-1.

Rationale and key rating drivers

Ratings downgrade to ESAF Small Finance Bank Limited's (ESFBL) debt instruments reflect the sustained weakening in asset quality and profitability in FY25 and Q1FY26, with the bank reporting net losses for four consecutive quarters. ESFBL posted a net loss of ₹521 crore in FY25 and ₹81 crore in Q1FY26, primarily considering elevated credit costs and interest income reversals, a trend which is expected to persist through FY26. The weakening is largely attributable to stress in the micro loans portfolio, which constituted 46% of total advances as on June 30, 2025, and was further exacerbated in Q1FY26 post the implementation of the new MFIN 2.0 regulatory framework.

ESFBL's slippages rose sharply to 10.29% in FY25 (from 6.50% in FY24) and further to 10.71% (annualised) in Q1FY26. Consequently, the gross non-performing assets (GNPA) ratio increased to 7.48% as on June 30, 2025, from 4.76% as on March 31, 2024. However, the reported GNPA ratio was partly contained through significant write-offs (₹1,225 crore) in FY25 and the sale of stressed assets (GNPA of ₹362 crore) to an asset reconstruction company in Q1FY26. This led to net non-performing assets (NNPA) to net worth ratio deteriorating sharply to 40.06% as on June 30, 2025, from 16.92% as on March 31, 2024. Considering heightened stress, the bank recalibrated its micro-banking disbursements and strategically pivoted to secured lending gold loans. Consequently, the share of micro-banking (including agri) declined from 75% as on March 31, 2024, to 51% as on June 30, 2025, owing to a 32% de-growth in this segment. In the same period, the share of secured loans increased from 23% to 59%, led by gold loans, which rose from 15% to 34%. While this shift is expected to improve portfolio quality, it is likely to exert pressure on profit margins given the relatively lower yields on secured lending products. On the liabilities front, while the bank has granular deposit base with 96% of deposits being retail, its current account savings account (CASA) ratio remains relatively moderate at 24.79% as on June 30, 2025.

CARE Ratings Limited (CareEdge Ratings) will closely monitor the bank's asset quality trends and profitability trajectory in FY26. The bank's ability to contain further slippages, infuse additional equity capital, improve collection efficiency, and earnings momentum while strengthening its secured lending base and maintaining adequate capitalisation will be key rating sensitivities going forward.

CareEdge Ratings has withdrawn the rating assigned to tier-II bonds (Basel III; ISIN No. INE818W08024 and INE818W08032) of ESFBL with immediate effect, as the bank has redeemed the instrument and there is no amount outstanding under the issue.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors: Factors that could individually or collectively lead to positive rating actions/upgrade:

- Profitable scale up in operations while maintaining adequate capitalisation levels.
- Sustained improvement in profitability and asset quality.

Negative factors: Factors that could individually or collectively lead to negative rating actions/downgrade:

- Deteriorating capitalisation with overall capital adequacy ratio (CAR) remaining below 18%.
- Inability to raise equity capital by Q3FY26.
- Weakening of earnings profile with continuation of losses.
- Gross stressed assets remaining above 7% of total advances.

¹Complete definition of ratings assigned are available at www.careratings.com and other CARE Ratings Limited's publications.

Analytical approach:

Standalone

Outlook: Negative

The negative outlook is on the expectation that the bank's profitability and asset quality will remain under pressure in the near-term. The outlook may be revised to 'Stable' if the company successfully raises substantial equity capital or demonstrates improved asset quality, characterised by a significant reduction in slippage while maintaining a comfortable capital adequacy buffer above regulatory requirements.

Detailed description of key rating drivers:

Key strengths

Established track record of the bank

ESFBL is promoted by K Paul Thomas, who is the promoter of the Kerala-based ESAF group, operating in the microfinance space since 1995 (ESAF Microfinance started its operations as an NGO as Evangelical Social Action Forum) and set up ESAF Microfinance & Investments Private Limited (EMFIL) in 2007. EMFIL subsequently received small finance bank (SFB) license and started its banking operations from March 2017. K Paul Thomas holds 6.05% stake in ESFBL as on June 30, 2025. He has over 35 years' industry experience, of which, over 25 years are in the microfinance sector. He is supported by a well-qualified and experienced management team, having rich experience in the banking and financial services sector. As on June 30, 2025, the bank's board consisted of 11 directors, including five independent directors, two nominee directors and one non-executive director apart from chairman (who is also an independent director), MD and one executive director, having extensive experience in the banking and financial services industry.

Adequate capitalisation levels

ESFBL reported comfortable capital adequacy with capital adequacy ratio (CAR) of 22.74% and a tier I CAR of 18.44% as on June 30, 2025. Despite the losses reported in FY25 and Q1FY26, the bank's capital adequacy remained comfortably above regulatory requirements. This was supported by the bank's strategic focus on expanding its gold loan portfolio with simultaneous reduction of micro-loans portfolio, which contributed to a reduction in risk-weighted assets. The bank also raised tier II capital of ₹115 crore in July 2025 and August 2025. Given the anticipated earnings pressure in the near-term, maintenance of a sufficient capital adequacy buffer by raising additional equity capital will be crucial in CareEdge Ratings' view.

Granular deposits; however, CASA proportion remains moderate

The bank's resource profile majorly consists of deposits (86% of total liabilities as on June 30, 2025) followed by borrowings. The bank's total deposits grew by 8.7% year-on-year (y-o-y) and stood at ₹22,698 crore as on June 30, 2025. The bank has a granular deposit profile with 96% of total deposits being retail consisting of less than ₹3 crore category as on June 30, 2025, with low dependence on bulk deposits for funding. However, the bank's CASA (as a percentage of total deposits) ratio remained relatively moderate at 24.79% as on June 30, 2025. The bank's ability to maintain granular deposit profile while improving its CASA base with meaningful reduction in cost of deposits remains a monitorable.

Key weaknesses

Weak profitability

The bank reported net loss of ₹521 crore for FY25 and ₹81 crore for Q1FY26 compared to profit after tax (PAT) of ₹426 crore in FY24. The decline in profitability was primarily driven by elevated credit costs and interest income reversals arising from asset quality deterioration in microfinance segment. Going forward, profitability is expected to remain under pressure in FY26 due to continued stress in the microfinance sector (resulting in interest reversals and high provisions) and change in product mix in favour of lower yielding secured loans which are repo linked. While this shift is expected to improve the bank's portfolio quality and reduce credit cost over time, the bank's ability to limit incremental slippages will be critical.

Deterioration in asset quality

ESFBL's asset quality deteriorated materially in FY25 and Q1FY26, with the GNPA rising to 7.48% as on June 30, 2025 (March 31, 2025: 6.87%), from 4.76% as on March 31, 2024. The slippage ratio stood elevated at 10.71% (annualised) for Q1FY26 and 10.29% for FY25. While high slippages persisted, the reported GNPA ratio was partly contained through significant write-offs in FY25 and the sale of stressed assets to an ARC in Q1FY26. However, the NNPA-to-net worth ratio increased sharply to 40.06% as on June 30, 2025 (31.18% as on March 31, 2025), from 16.92% as on March 31, 2024, remaining significantly higher than peers. Gross stressed assets to gross advances and net stressed assets to net worth remained elevated at 7.79% and 43.44%,

respectively, as on June 30, 2025 (March 31, 2024: 5.03% and 19.02%). This deterioration was largely driven by stress in the micro-loan segment, which was further exacerbated by the implementation of MFIN Guardrail 2.0 from April 01, 2025.

As on June 30, 2025, the bank's provision coverage ratio (PCR) excluding technical written off accounts (TWO) on GNPA's stood at 52%, which is comparatively lower than peer small finance banks. Gross stressed assets (as a percentage of gross advances) increased to 7.79% as on June 30, 2025, from 5.03% as on March 31, 2024. Given the ongoing stress in the microfinance (MFI) segment, slippages are expected to remain elevated in the near-term, posing continued pressure on the bank's profitability. The bank's ability to manage asset quality and credit costs remains critical for stability of its profitability and return ratios going forward.

Product and regional concentration

In FY25 and Q1FY26, ESFBL's advances remained largely stagnant as the bank moderated its micro-loan disbursements in response to stricter regulatory guardrails and persistent sectoral stress. At the same time, it recorded healthy growth in gold loans and other secured retail segments, gradually improving the overall advances mix to a more secured portfolio. To diversify its portfolio, the bank focussed on non-micro-loan segments, including gold loans, loans against property (LAP), business loans, and corporate loans among others. Micro-loans (including agri) continue to remain the largest segment of ESFBL's portfolio; however, its share declined sharply from 75% as on March 31, 2024, to 51% as on June 30, 2025, owing to a 32% de-growth in this segment. While the bank will continue to grow micro-banking loans, it is focusing on increasing secured segments whose share increased from 23% as on March 31, 2024, to 59% as on June 30, 2025, led by gold loans, the share of which rose from 15% to 34% in the same period.

Going forward, secured retail verticals (being smaller in size) are expected to grow even faster than micro-loans business and hence the share of micro-loans in overall loan book is expected to reduce even further.

ESFBL's operations are primarily concentrated in Kerala and Tamil Nadu, with Kerala alone accounting for 40% of branches, 35% of advances, and 79% of deposits as on June 30, 2025. Collectively, the two states contributed 59% to total branches, 59% to total advances, and 84% to total deposits as on March 31, 2025. While the bank has significantly reduced its state concentration over the last three years and intends to continue this trend going forward, the relatively high dependence on these states exposes it to region-specific risks such as natural calamities, political developments, and regulatory changes.

The bank's ability to reduce its product and geographical concentration remain a key rating monitorable.

Liquidity: Adequate

Per the structural liquidity statement as on June 30, 2025, there were no negative cumulative mismatches for time buckets up to one year. In addition, the bank consistently maintains excess statutory liquidity ratio (SLR) investments and non-SLR investments, which provides cushion to its liquidity. Excess SLR and non-SLR liquidity stood at ₹1,647 crore and ₹506 crore, respectively, as on June 30, 2025. In addition, the bank has access to borrowing from Reserve Bank of India's (RBI's) liquidity adjustment facility (LAF) and marginal standing facility (MSF) and option to refinance from Small Industries Development Bank of India (SIDBI), National Housing Bank (NHB), and National Bank for Agriculture and Rural Development (NABARD) among others, and access to call money markets. The bank's liquidity coverage ratio was comfortable at 150% as on June 30, 2025, against the minimum regulatory requirement of 100%.

Environment, social, and governance (ESG) risks

Not applicable

Applicable criteria

[Definition of Default](#)

[Rating Outlook and Rating Watch](#)

[Banks](#)

[Financial Ratios - Financial Sector](#)

[Rating Basel III - Hybrid Capital Instruments issued by Banks](#)

[Short Term Instruments](#)

[Withdrawal Policy](#)

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Financial services	Financial services	Banks	Other bank

ESFBL is a Kerala-based small finance bank (SFB), which has commenced its banking operations on March 10, 2017. The bank was promoted by K Paul Thomas who is a part of the Kerala-based ESAF group operating in microfinance space from 1995 (ESAF Microfinance started its operations as an NGO as Evangelical Social Action Forum) and set up ESAF Microfinance & investments Pvt. Limited (EMFIL) in 2007. EMFIL subsequently got SFB license and started its banking operations from March 2017. ESFBL is currently focused on retail banking business with presence in micro-finance, housing finance, business loans, loan against property (LAP), gold loans and providing financing solutions for marginal customers who lack access to the formal banking and financing channels while providing a comprehensive banking and digital platform for all. The bank received scheduled status from RBI on December 27, 2018.

Brief Financials (₹ crore)	31-03-2024 (A)	31-03-2025 (A)	Q1FY26 (UA)
Total income	4,260	4,329	1,023
PAT	426	-521	-81
Total assets	26,040	26,960	26,485
Net NPA (%)	2.26	2.99	3.77
ROTA (%)	1.84	-1.97	-1.22

A: Audited; UA: Unaudited; Note: these are latest available financial results

All calculations per CareEdge Ratings.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned and Rating Outlook
Tier II Bonds (Basel III)	INE818W08024	28-Mar-2018	11.50%	28-Mar-2025	-	Withdrawn
Tier II Bonds (Basel III)	INE818W08032	01-Jun-2018	11.50%	01-Jun-2025	-	Withdrawn
Tier II Bonds (Basel III)	INE818W08081	31-Mar-2022	11.25%	30-Apr-2032	20.00	CARE A-; Negative
Lower Tier-II bonds (Basel II)	INE818W08099	04-Sep-2023	11.25%	04-May-2029	85.00	CARE A-; Negative
Lower Tier-II bonds (Basel II)	INE818W08107	29-Feb-2024	11.10%	28-Feb-2034	60.00	CARE A-; Negative

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned and Rating Outlook
Lower Tier-II bonds (Basel II)	INE818W08123	20-Mar-2024	11.00%	20-Apr-2030	85.00	CARE A-; Negative
Lower Tier-II bonds (Basel II)	INE818W08115	20-Mar-2024	11.10%	20-Apr-2031	50.00	CARE A-; Negative
Lower Tier-II bonds (Basel II)	INE818W08131	17-Jul-2025	11.10%	17-Jul-2031	65.00	CARE A-; Negative
Lower Tier-II bonds (Basel II)	INE818W08149	14-Aug-2025	11.30%	14-May-2031	50.00	CARE A-; Negative
Lower Tier-II bonds (Basel II)	Proposed	-	-	-	385.00	CARE A-; Negative
Certificate Of Deposit	Proposed	-	-	-	500.00	CARE A1

Annexure-2: Rating history for last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2025-2026	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023
1	Bonds-Tier II Bonds	LT	-	-	-	1)CARE A; Negative (28-Mar-25) 2)CARE A; Negative (17-Mar-25) 3)CARE A; Stable (04-Jul-24)	1)CARE A; Stable (22-Feb-24) 2)CARE A; Stable (01-Aug-23) 3)CARE A; Stable (04-Jul-23)	1)CARE A; Negative (27-Dec-22)
2	Certificate Of Deposit	ST	500.00	CARE A1	-	1)CARE A1+ (28-Mar-25) 2)CARE A1+ (17-Mar-25)	1)CARE A1+ (22-Feb-24) 2)CARE A1+ (01-Aug-23)	1)CARE A1+ (27-Dec-22)

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2025-2026	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023
						3)CARE A1+ (04-Jul-24)	3)CARE A1+ (04-Jul-23)	
3	Bonds-Tier II Bonds	LT	20.00	CARE A- ; Negative	-	1)CARE A; Negative (28-Mar-25) 2)CARE A; Negative (17-Mar-25) 3)CARE A; Stable (04-Jul-24)	1)CARE A; Stable (22-Feb-24) 2)CARE A; Stable (01-Aug-23) 3)CARE A; Stable (04-Jul-23)	1)CARE A; Negative (27-Dec-22)
4	Bonds-Lower Tier II	LT	150.00	CARE A- ; Negative	-	1)CARE A; Negative (28-Mar-25) 2)CARE A; Negative (17-Mar-25) 3)CARE A; Stable (04-Jul-24)	1)CARE A; Stable (22-Feb-24) 2)CARE A; Stable (01-Aug-23)	-
5	Bonds-Lower Tier II	LT	130.00	CARE A- ; Negative	-	1)CARE A; Negative (28-Mar-25) 2)CARE A; Negative (17-Mar-25) 3)CARE A; Stable (04-Jul-24)	1)CARE A; Stable (22-Feb-24)	-

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2025-2026	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023
6	Bonds-Lower Tier II	LT	500.00	CARE A- ; Negative	-	1)CARE A; Negative (28-Mar-25)	-	-

LT: Long term; ST: Short term

Annexure-3: Detailed explanation of covenants of rated instruments/facilities: Not applicable

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1.	Bonds-Tier-II Bonds	Complex
2.	Bonds-Lower Tier II	Simple
3.	Certificate of deposit	Simple

Annexure-5: Lender details: Not applicable

Note on complexity levels of rated instruments: CareEdge Ratings has classified instruments rated by it based on complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for clarifications.

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