

AU Small Finance Bank Ltd

Sector: Banks/Mid Cap | Earnings Update – 4QFY20

BUY

19 May 2020

Background: AU SFB, initially incorporated as a vehicle finance company in 1996, was transformed into a Small Finance Bank in April 2017. The bank has presence in 11 states and 1 union territory, with 528 branches, 356 ATMs, 31 asset centers and ~6,59,904 loan accounts. The bank offers a comprehensive and tailor made range of products (both asset and liability) and services to cater to the needs of various businessmen (SME and MSME) and other middle and low income customers. Loan book of the bank grew at a CAGR of 36% over FY12 to FY20 and stood at ₹308.9bn as of 4QFY20 with a deposit base of ₹261.6bn.

Sensex	30,703
Nifty	9,024
Price	₹ 403
Target Price (12 months)	₹ 479
Recommendation	BUY

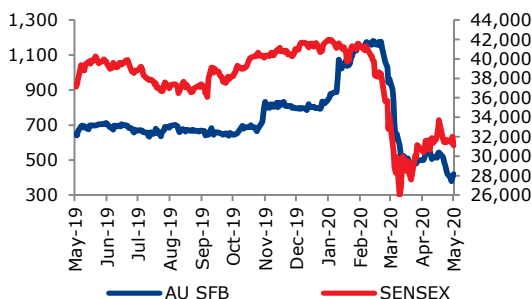
52 Week High/Low	₹ 1,217.7/379.9
Bloomberg / Reuters	AUBANK.IN/ AUFI.NS
Equity (shares in mn)	304.1
Mkt. Cap in bn	₹ 122.5/ \$ 1.6
Avg. Daily Vol. ('000)	814.3
Avg. Daily Vol. (mn)	₹ 328.1 / \$ 4.3

Shareholding	Mar-19	Dec-19	Mar-20
Promoters (%)	32.19	30.99	30.95
FII (%)	23.76	26.75	28.69
DII (%)	14.41	15.54	15.42
Others (%)	29.64	26.72	24.94
Pledge (% of promoter holding)	6.56	7.04	7.04

Valuation Summary (₹ bn)

Y/E March	FY20	FY21E	FY22E
Net Interest Inc	19.1	23.3	27.9
Other Inc	7.1	7.9	9.4
Pre Prov Profit	12.0	14.4	17.2
PAT	6.7	7.5	9.1
EPS (₹)	22.2	24.5	30.0
EPS growth (%)	68.6	10.6	22.4
PE (X)	18.2	16.4	13.4
P / ABV (X)	2.9	2.5	2.1
Div Yield (%)	-	0.2	0.2
ROA (%)	1.6	1.7	1.7
ROE (%)	15.8	15.8	16.5
CAR (%)	22.0	19.4	19.4

Performance(%)	1M	3M	12M
AU SFB	-16.1	-63.4	-35.3
SENSEX	1.4	-24.6	-16.6



Muted quarter due to higher Covid related provisioning, asset quality though stable, near term concerns remain on account of, NBFC, Wheels & Real estate portfolios. Despite challenges we believe risk reward seems favorable & upgrade the stock to buy on compelling valuations.

- The bank's loan AUM increased by 27.4% YoY (3.4 % QoQ) to ₹308.9bn driven by strong growth in Retail segment, up 37.6% YoY. Within retail segment Housing loans increased by 4.9x, coupled with wheels and SBL-MSME segment which registered 27% YoY and 43.5% YoY, growth respectively.
- During the year, disbursements witnessed growth of 16% YoY and stood at ₹186.3bn. This growth was led by retail assets (up 27% YoY in FY20) and stood at ₹150.4bn despite de-growth in Small and Mid-Corporate Segment (-16% YoY). The support for retail segment growth came from SBL-MSME (up 32% YoY) and Wheels (up 16% YoY) in FY20.
- Despite a challenging quarter, the deposits growth maintained up trend to reach ₹261.6bn compared to ₹194.2bn in 4QFY19 (up 35% YoY & 8% QoQ). The bank is focused on building deposits through non-callable TDs from senior citizens, which currently constitute 60% of the bulk TDs. This resulted in decline of CASA ratio to 16% from 17% in 4QFY20. Additionally, the bank has opened 13,000 accounts in April 2020, increasing Retail (CASA + Term) deposits by ₹0.8mn.
- On a sequential basis, NIMs remain stable at 5.5% (up 5 bps QoQ) due to 10bps QoQ decline in Cost of funds to 7.7% in 4Q20. The bank expects cost of funds to improve in next 6-9 months and restrict operating costs in absence of new expansion plans.
- The bank reported its lowest GNPA (%) in the last nine quarters at 1.68% (up 32bps YoY) in 4QFY20. This was on account of lower slippages at ₹810mn (vs ₹1.5bn in 4QFY19), despite weak macros.
- The C/I ratio increased to 57.9% (470bps QoQ) in 4QFY20 on account of employee hires and CSR expenses. The bank's 65% of expenses are fixed in nature, which provides further scope for cost reduction. The bank is targeting to reduce the fixed proportion of the bank's total expenses (~60% excluding depreciation) through efficiency improvements.
- The 5% provisioning requirement from RBI resulted in the bank setting aside ₹1.38bn for Covid (as its SMA stood at ₹27bn). This resulted in 3.8x increase in total provisions QoQ to ₹1.5bn leading to muted earnings of ₹1.2bn (3.4% YoY).
- Despite the lockdown, in April 2020, the bank received collections from ~75% of its customers, 94% of the NBFC customers paid their EMIs and 93% of working capital loan customers serviced their interest payments. Given the experienced management, diversified loan mix/geographies and collection efficiency the bank remains well positioned to sail the current storm stirred by the pandemic.

Valuation: Contracting cost of funds coupled with moderate loan book growth should support NIMs in the short term. Despite the possible increase in provisions in the coming quarters the high spread should support earnings for FY21E. The stock is currently trading at 2.1X P/ABV and 13X P/E of FY22E, compared to trailing 5.1x multiple at IPO and 6.8x average in LTM, implying a steep discount of 60% and 68% respectively. Assigning a P/ABV of 2.5x for FY22E, we arrive at a target of ₹479, and hence upgrade our rating on the stock from MARKET PERFORMER to BUY.

Risks: Rising competition may put pressure on yields; asset quality deterioration owing to higher share of riskier segments; state specific issues may have greater impact owing to regional concentration.

Results Summary 4QFY20

Y/E March (₹ bn)	4QFY20	4QFY19	YoY Growth	3QFY20	QoQ Growth
Net Interest Income	5.5	3.9	43.4%	5.1	9.5%
Other Income	1.8	1.3	40.3%	1.6	13.6%
Pre Provisioning Profit	3.2	2.2	46.4%	3.1	0.9%
PAT	1.2	1.2	3.4%	1.9	-35.7%
Cost / Income (%)	57.9	58.3		53.2	
Gross NPA (%)	1.7	2.0		1.9	
Net NPA (%)	0.8	1.3		1.0	
Prov Coverage ratio(%)	52.5	37.4		46.8	
CAR (%)	22.0	19.3		19.3	

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