

July 31, 2022

## Q1FY23 Result Update

☑ Change in Estimates | ■ Target | ☑ Reco

### Change in Estimates

	Current		Previous	
	FY23E	FY24E	FY23E	FY24E
<b>Rating</b>	<b>HOLD</b>		<b>ACCUMULATE</b>	
<b>Target Price</b>	<b>2,300</b>		<b>2,300</b>	
NII (Rs.)	8,971	10,898	9,162	10,692
% Chng.	(2.1)	1.9		
PPoP (Rs.)	5,690	7,340	5,995	7,261
% Chng.	(5.1)	1.1		
EPS (Rs.)	52.8	68.4	55.8	67.7
% Chng.	(5.4)	1.0		

### Key Financials - Standalone

Y/e Mar	FY21	FY22	FY23E	FY24E
Net Int.Inc. (Rs m)	5,182	7,753	8,971	10,898
Growth (%)	20.4	49.6	15.7	21.5
Op. Profit (Rs m)	3,905	4,775	5,690	7,340
PAT (Rs m)	2,895	3,568	4,170	5,402
EPS (Rs.)	36.9	45.2	52.8	68.4
Gr. (%)	15.9	22.6	16.9	29.5
DPS (Rs.)	-	7.5	2.6	4.1
Yield (%)	-	0.3	0.1	0.2
Margin (%)	5.3	6.6	6.3	6.4
RoAE (%)	12.9	13.7	14.1	16.1
RoAA (%)	3.5	3.6	3.5	3.8
PE (x)	64.6	52.7	45.1	34.8
P/BV (x)	7.8	6.7	6.1	5.2
P/ABV (x)	8.0	6.9	6.2	5.3

### Key Data

### AVAS.BO | AAVAS IN

52-W High / Low	Rs.3,340 / Rs.1,815
Sensex / Nifty	57,570 / 17,158
Market Cap	Rs.188bn/ \$ 2,374m
Shares Outstanding	79m
3M Avg. Daily Value	Rs.198.43m

### Shareholding Pattern (%)

Promoter's	39.20
Foreign	39.91
Domestic Institution	9.89
Public & Others	11.00
Promoter Pledge (Rs bn)	-

### Stock Performance (%)

	1M	6M	12M
Absolute	14.7	(17.2)	(7.5)
Relative	5.6	(17.7)	(15.4)

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## NII softer, upside capped

### Quick Pointers:

- Maintained spreads, opex efficiency and lower prov. to lead ROA expansion.
- Growth to be sustainable while target is to improve opex efficiency.

**Aavas Financiers (Aavas) PAT was largely in-line at Rs0.9bn (PLe Rs.0.93bn) even as miss on NII was partially offset by lower provisions. AuM growth at 23.7% YoY came in as expected and management suggested that AuM could grow by 20-25% consistently as demand exists, however asset quality would be preferred over growth. Opex intensity would remain elevated for 12 to 18 months owing to ramp up in distribution network and tech spends, however C/I is targeted to reduce by 2.0-2.5% over the medium term. ROE expansion would be driven by sustained spreads, opex efficiency, lower provisioning and higher leverage. While we increase AuM growth and opex expectations by 2%, we trim our NII estimates by 2%, which would impact PAT for FY23/24 by -5%/+1%. We maintain our multiple at 5.0x FY24 ABV and TP at Rs2300 as valuation at 5.3x is steep. Change rating from ACCUMULATE to HOLD.**

- PPoP miss led by lower NII:** NII was a miss at Rs2bn (PLe Rs2.16bn) led by declining NIM and AUM growth came in as expected at 23.7% YoY. NIM was lower at 7.5% (PLe 8.7%) as yields came off by 93bps while CoF increased 38bps. Other income was higher at Rs1.6bn as fee income sustained and there was gain in FV changes. Opex spiked by 52.6% YoY to Rs1bn in-line with PLe. PPOP fell short by 11% at Rs1.1bn (PLe Rs1.3) due to lower NII and higher opex. Asset quality moderated than anticipated with GNPA/NNPA rising by 9/7bps QoQ to 1.08%/0.84%. There was a provision creation of Rs9mn. PAT was largely in-line at Rs.0.9bn (PLe Rs0.93bn).
- Business momentum steady:** Sequential AuM growth was strong at 6% QoQ that was led by non-HL segment which grew by 8.5% QoQ, while Home Loans grew by 3.3% QoQ. Non-HL portfolio has been seeing good traction (+8.5% QoQ) of which 40% is from MSME. HL: Non-HL AuM mix stood at 71:29 vs 73:27 in Q1FY22. Disbursement run-rate is about Rs3.7-3.8bn per month. Management suggested that it can sustainably grow by 20-25% per annum driven by technology, better understanding and deeper penetration in the geography and marginal cost differential with larger organizations. However, focus would remain on quality underwriting as asset quality would always take a precedence to growth. Repayments were steady sequentially. BT-out for the quarter was 1.5% of opening AuM.
- Opex continues to be elevated; asset quality sees slight moderation:** Opex remained elevated in Q1FY23 mainly on account of ramp-up in distribution network (continues to guide for addition of 35-40 branches per annum) and investments in digitization & technology, C/I came at 47% vs 43.8% in Q4FY22. C/I would remain elevated for 12-18 months; however, it may reduce by 20-25bps per year over the medium term. Credit quality in terms of GNPA deteriorated slightly QoQ due to slippages from restructured pool of Rs0.16bn. Management guided that 1+ DPD would be maintained <5%, Gross Stage-3 - <1% (+/- 10bps) and PCR at similar levels.

**Exhibit 1: Lower NII and higher opex lead to PPOP miss**

*NII growth was strong at 34% YoY led by AUM growth.*

*Other income was strong led by better fee income*

*Opex has been relatively elevated due to higher business volumes and expansion.*

*Lower provision than expected.*

*Disbursements have been decent despite seasonally weak quarter*

*NIMs come off due to rate hikes*

*Asset Quality slightly deteriorates, however PCR steady*

Financial Statement (Rs mn)	Q1FY23	Q1FY22	YoY gr. (%)	Q4FY22	QoQ gr. (%)
Interest Income	3,365	2,630	27.9	3,498	(3.8)
Interest Expense	1,347	1,128	19.4	1,237	8.9
<b>Net interest income (NII)</b>	<b>2,019</b>	<b>1,502</b>	<b>34.4</b>	<b>2,261</b>	<b>(10.7)</b>
Other income	163	90	82.6	155	5.8
<b>Total income</b>	<b>2,182</b>	<b>1,592</b>	<b>37.1</b>	<b>2,416</b>	<b>(9.7)</b>
Operating expenses	1,026	673	52.6	1,059	(3.1)
<b>Operating profit</b>	<b>1,156</b>	<b>919</b>	<b>25.7</b>	<b>1,357</b>	<b>(14.8)</b>
Total provisions	9	170	(94.6)	(104)	(108.8)
<b>Profit before tax</b>	<b>1,147</b>	<b>749</b>	<b>53.1</b>	<b>1,461</b>	<b>(21.5)</b>
Tax	254	150	69.3	304	(16.3)
<b>Profit after tax</b>	<b>892</b>	<b>599</b>	<b>49.0</b>	<b>1,157</b>	<b>(22.9)</b>
AUM (Rs mn)	118,936	96,156	23.7	113,502	4.8
Disbursements (Rs mn)	10,936	4,625	136.5	12,872	(15.0)
<b>Profitability ratios</b>					
<b>NIM</b>	<b>7.7</b>	<b>6.9</b>	<b>74</b>	<b>8.2</b>	<b>(56)</b>
RoAA	3.2	2.6	53	3.6	(41)
RoAE	12.5	9.8	265	13.7	(123)
<b>Asset Quality ratios</b>					
Gross NPL (Rs m)	1,130	894	26.4	904	25.0
Net NPL (Rs m)	847	670	26.4	146	482.0
Gross NPL ratio	<b>1.1</b>	<b>1.1</b>	<b>(6)</b>	<b>1.0</b>	<b>9</b>
Net NPL ratio	<b>0.8</b>	<b>0.9</b>	<b>(2)</b>	<b>0.8</b>	<b>7</b>
Coverage ratio	25.0	25.0	(2)	23.1	194
<b>Business &amp; Other Ratios</b>					
Yield on Loans (%)	12.7	13.0	(32)	12.7	2
Cost of Borrowings (%)	6.9	7.3	(39)	6.9	(2)
Spread (%)	5.8	5.7	7	5.8	4
Cost/Income Ratio	47.0	42.3	477	43.8	318

Source: Company, PL

## Q1FY23 Concall Highlights

### Assets/Liabilities

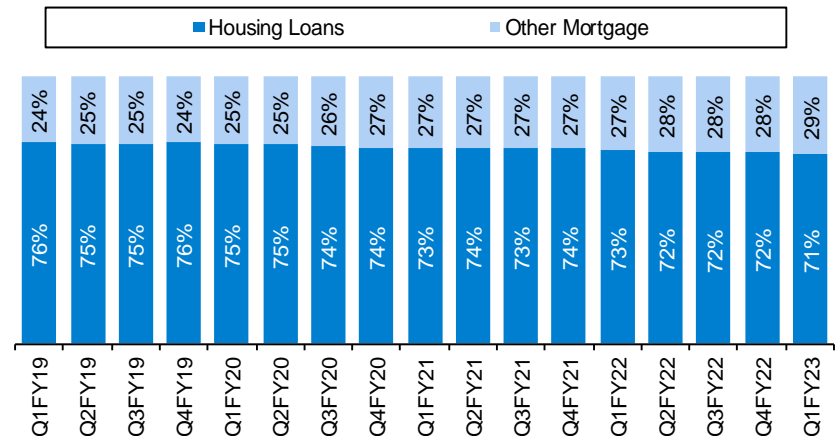
- Management expects the affordable housing segment to growth sustainable over the next 15 years, this in addition to the technology and geography awareness would continue to benefit the company as cost differential with larger companies would be 20-25bps.
- Disbursements in the quarter were Rs.10.9bn leading to an AUM growth of 23.7% YoY/4.8% QoQ. Average monthly disbursements have been in the range of Rs3,7-3.8bn. Management guided for 23-25% YoY growth while maintaining asset quality and sustainable operating metrics.
- Repayment rate remained steady sequentially at 22.9%(annualized) of the opening AUM. While BT-out for the quarter has been 1.5% of the opening AUM i.e. 6% (annualised).
- Rate hikes are passed on to the customers as per the decision of ALCO, even in Fixed Rate loans, reset is permitted every 3 years, hence risk is minimized to that extent. During the quarter, 25bps hike has already been taken, while another 50bps would be increased from August'22.
- Focus would be on maintaining spreads at this level, realizing cost efficiencies driven by technology and lower provisioning would lead to ROA in the range of 2.5-3%. This along with increase in leverage would lead to ROE improvement in sustainable manner of 3 to 5 years.

### Fees/NIMs/Branches

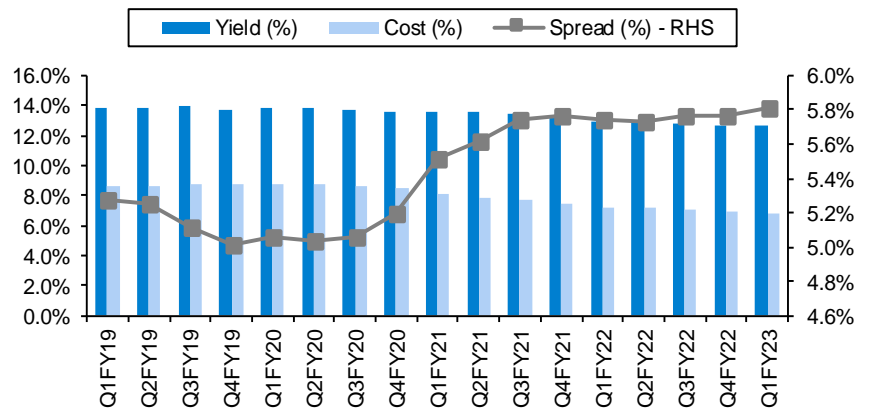
- NIM came to 7.5% vs 8.7% in Q4FY22. Margin compression was majorly due to faster rise Cost of Funds than yields. Management guided that spreads would normalize in 5% range over the course of time.
- Yields on Home loans was 11% while non-home loans was 14%. Incremental Cost of Borrowings were at 5.65% due to refinance from NHB.
- Opex was elevated during the year mainly on account of ramp up in distribution network, investments in digitization and technology. For FY23, C/I is expected to remain elevated, however over the 3-5 year the same is expected to reduce by 20-25bps every year.
- Every year 30-40 branches would be added for 1-2 years. Usually, new branches turn ROE positive in span of 12months.

### Asset Quality

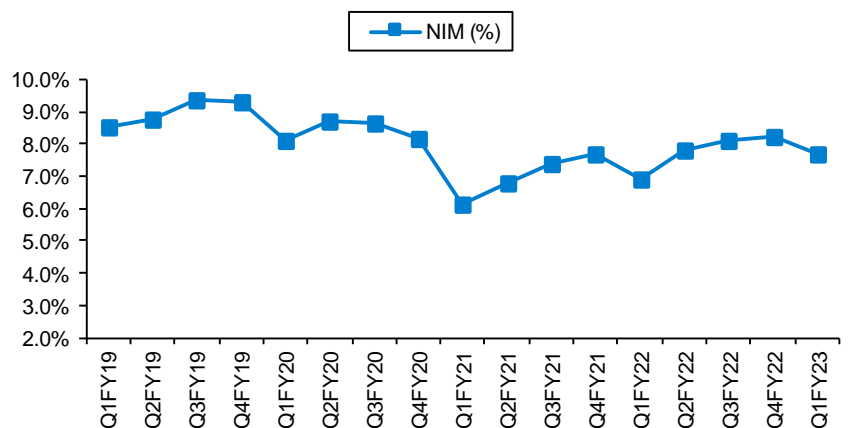
- Restructuring:** O/s as on June 30, 2022 was Rs. From the restructured book Rs0.16bn have slipped into Stage 3 which led to increase in Stage 3 assets this quarter
- Management guided that 1+ DPD book would <5%, while 90+ DPD would be maintained in ~1% range

**Exhibit 2: Loan Book mix sees slight uptick in other mortgage**


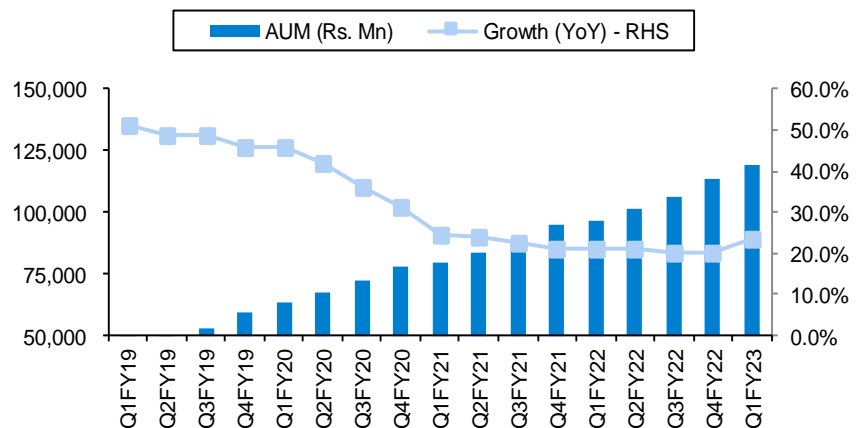
Source: Company, PL Research

**Exhibit 3: Spreads maintained at 5.8% levels**


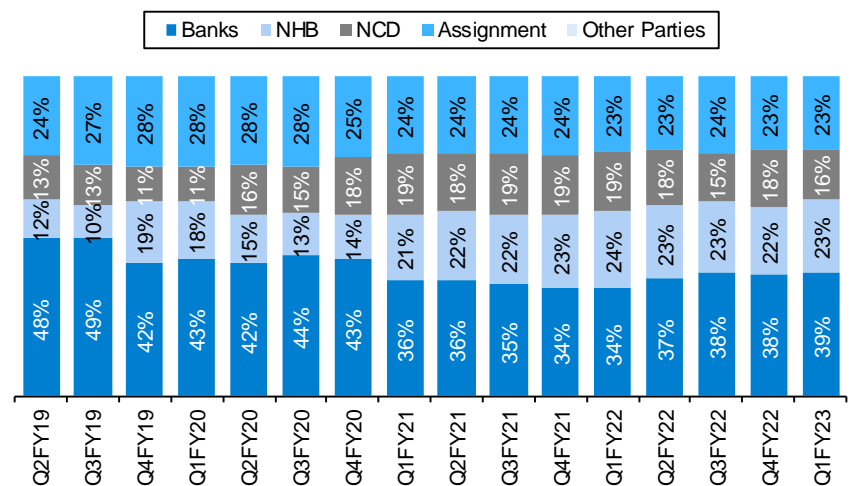
Source: Company, PL Research

**Exhibit 4: NIM expansion led by rate hikes**


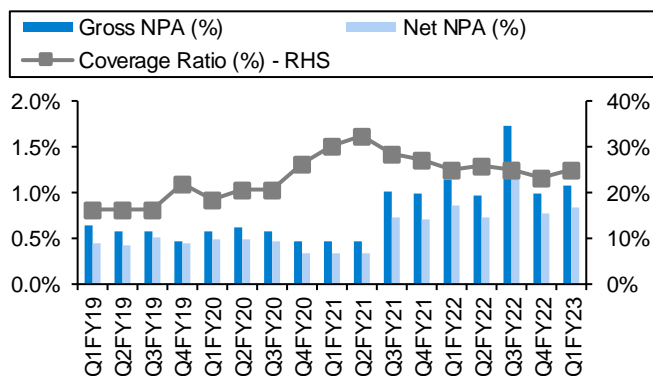
Source: Company, PL

**Exhibit 5: AUM growth was decent on lower base**


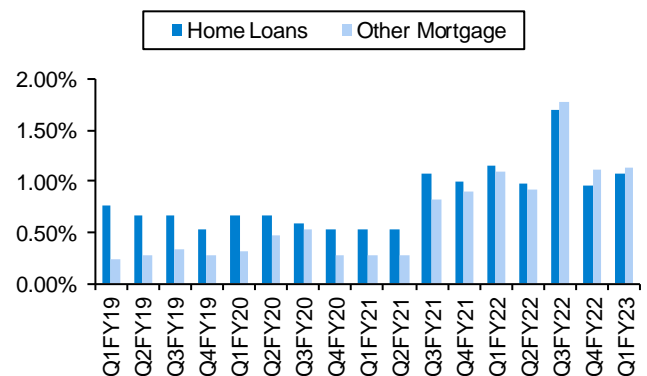
Source: Company, PL

**Exhibit 6: Borrowing Mix mainly from Banks and NHB refinance**


Source: Company, PL Research

**Exhibit 7: Asset quality sees slight deterioration**


Source: Company, PL

**Exhibit 8: Segmental GNPA break-up**


Source: Company, PL

Exhibit 9: ROEs to improve on lower provision

RoE decomposition (%)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest income	10.2	10.3	9.8	9.7	10.4	10.9	11.2
Interest expenses	5.0	4.4	4.4	4.6	4.0	4.8	5.1
<b>Net interest income</b>	5.2	5.9	5.4	5.2	6.4	6.1	6.1
Other Inc. from operations	2.6	2.0	1.5	1.3	0.4	0.6	0.7
<b>Total income</b>	7.8	7.9	6.8	6.4	6.9	6.7	6.9
Employee expenses	2.9	2.0	1.8	1.7	1.9	1.9	1.9
Other operating expenses	1.4	1.2	1.0	0.8	1.0	1.0	1.0
<b>Operating profit</b>	3.5	4.6	3.9	3.9	4.0	3.8	4.0
Tax	1.1	1.4	0.7	0.6	0.8	0.8	0.9
Loan loss provisions	0.1	0.2	0.2	0.4	0.2	0.2	0.2
<b>RoAA</b>	2.4	3.0	3.1	2.9	3.0	2.8	3.0
<b>RoAE</b>	11.2	11.9	12.7	12.9	13.7	13.8	15.2

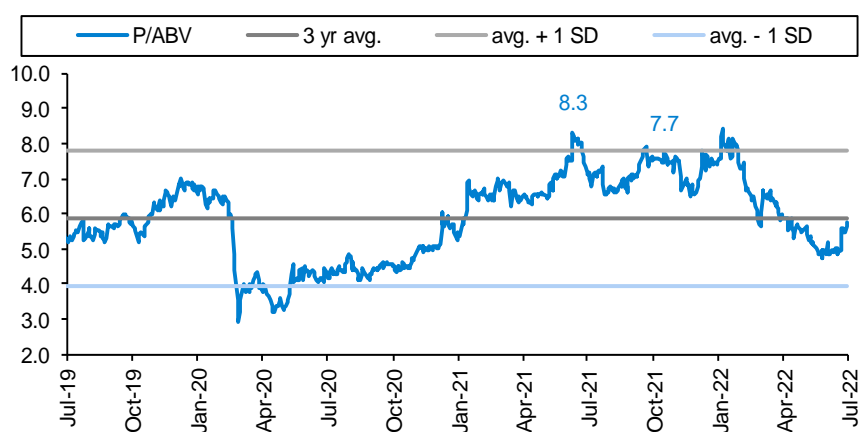
Source: Company, PL Research

Exhibit 10: We slightly tweak estimates and credit cost assumptions

Estimates Change Table Rs (mn)	Old		Revised		% Change	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Net interest income	9,196	10,753	8,971	10,898	(2.1)	1.9
Operating profit	6,029	7,322	5,690	7,340	(5.1)	1.1
Net profit	4,407	5,347	4,170	5,402	(5.4)	1.0
Loan Growth (%)	18.1	18.0	20.1	19.6	2.0	1.6
Credit Cost (bps)	22.0	21.7	22.0	21.7	-	-
EPS, Rs.	56.2	68.3	52.8	68.4	(5.4)	1.0
ABV per share, Rs.	398.3	457.4	382.8	446.5	(0.7)	(0.5)
<b>Price target, Rs.</b>	<b>2,300</b>		<b>2,300</b>		-	
<b>Recommendation</b>	<b>ACCUMULATE</b>		<b>ACCUMULATE</b>			

Source: Company, PL

Exhibit 11: One year forward P/ABV valuation chart



Source: Company, PL



## Income Statement (Rs. m)

Y/e Mar	FY21	FY22	FY23E	FY24E
Int. Inc. / Opt. Inc.	9,764	12,528	15,821	19,572
Interest Expenses	4,582	4,775	6,850	8,675
<b>Net interest income</b>	<b>5,182</b>	<b>7,753</b>	<b>8,971</b>	<b>10,898</b>
Growth(%)	20.4	49.6	15.7	21.5
Non-interest income	1,289	528	847	1,301
Growth(%)	10.5	(59.1)	60.5	53.7
Net operating income	6,471	8,281	9,818	12,199
<b>Expenditures</b>				
Employees	1,721	2,322	2,721	3,233
Other Expenses	639	946	1,124	1,299
Depreciation	206	238	282	326
Operating Expenses	2,566	3,506	4,128	4,858
<b>PPP</b>	<b>3,905</b>	<b>4,775</b>	<b>5,690</b>	<b>7,340</b>
Growth(%)	23.0	22.3	19.2	29.0
Provisions	371	226	275	325
<b>Profit Before Tax</b>	<b>3,533</b>	<b>4,549</b>	<b>5,416</b>	<b>7,016</b>
Tax	638	981	1,246	1,614
Effective Tax rate(%)	18.1	21.6	23.0	23.0
<b>PAT</b>	<b>2,895</b>	<b>3,568</b>	<b>4,170</b>	<b>5,402</b>
Growth(%)	16.2	23.2	16.9	29.5

## Balance Sheet (Rs. m)

Y/e Mar	FY21	FY22	FY23E	FY24E
<b>Source of funds</b>				
Equity	785	789	789	789
Reserves and Surplus	23,229	27,297	30,166	35,244
Networth	24,014	28,086	30,956	36,034
Growth (%)	14.5	17.0	10.2	16.4
Loan funds	63,777	80,120	96,790	1,15,129
Growth (%)	18.5	25.6	20.8	18.9
Deferred Tax Liability	-	-	-	-
Other Current Liabilities	1,690	1,957	1,515	1,453
Other Liabilities	119	40	50	60
<b>Total Liabilities</b>	<b>89,600</b>	<b>1,10,204</b>	<b>1,29,311</b>	<b>1,52,675</b>
<b>Application of funds</b>				
Net fixed assets	289	327	415	496
Advances	75,233	90,534	1,08,649	1,29,922
Growth (%)	21.7	20.3	20.0	19.6
Investments	45	675	818	978
Current Assets	11,210	15,302	17,719	21,188
<b>Net current assets</b>	<b>9,519</b>	<b>13,345</b>	<b>16,204</b>	<b>19,736</b>
Other Assets	2,824	3,365	4,083	4,883
<b>Total Assets</b>	<b>89,600</b>	<b>1,10,204</b>	<b>1,31,683</b>	<b>1,57,467</b>
Growth (%)	17.0	23.0	19.5	19.6
<b>Business Mix</b>				
AUM	94,543	1,13,502	1,36,298	1,62,988
Growth (%)	21.3	20.1	20.1	19.6
On Balance Sheet	94,543	1,13,502	1,36,298	1,62,988
% of AUM	100.00	100.00	100.00	100.00
Off Balance Sheet	-	-	-	-
% of AUM	-	-	-	-

## Profitability &amp; Capital (%)

Y/e Mar	FY21	FY22	FY23E	FY24E
NIM	5.3	6.6	6.3	6.4
ROAA	3.5	3.6	3.5	3.8
ROAE	12.9	13.7	14.1	16.1

Source: Company Data, PL Research

## Quarterly Financials (Rs. m)

Y/e Mar	Q2FY22	Q3FY22	Q4FY22	Q1FY23
Int. Inc. / Operating Inc.	3,118	3,282	3,498	3,365
Income from securitization	-	-	-	-
Interest Expenses	1,160	1,251	1,237	1,347
<b>Net Interest Income</b>	<b>1,958</b>	<b>2,031</b>	<b>2,261</b>	<b>2,019</b>
Growth (%)	33.1	12.0	42.9	34.4
Non-Interest Income	137	147	155	163
<b>Net Operating Income</b>	<b>2,095</b>	<b>2,178</b>	<b>2,416</b>	<b>2,182</b>
Growth (%)	34.2	12.8	37.9	37.1
Operating expenditure	864	910	1,059	1,026
<b>PPP</b>	<b>1,231</b>	<b>1,268</b>	<b>1,357</b>	<b>1,156</b>
Growth (%)	-	-	-	-
Provision	47	113	(104)	9
Exchange Gain / (Loss)	-	-	-	-
Profit before tax	1,183	1,155	1,461	1,147
Tax	262	264	304	254
Prov. for deferred tax liability	-	-	-	-
Effective Tax Rate	22.1	22.9	20.8	22.2
<b>PAT</b>	<b>921</b>	<b>891</b>	<b>1,157</b>	<b>892</b>
Growth	39	4	32	49
AUM	1,01,481	1,06,126	1,13,502	1,18,936
YoY growth (%)	21.3	20.3	20.1	23.7
Borrowing	69,055	72,291	79,725	82,909
YoY growth (%)	14.6	11.5	25.6	27.8

## Key Ratios

Y/e Mar	FY21	FY22	FY23E	FY24E
CMP (Rs)	2,383	2,383	2,383	2,383
EPS (Rs)	36.9	45.2	52.8	68.4
Book value (Rs)	305.9	355.8	392.2	456.5
Adj. BV(Rs)	299.0	347.0	382.8	446.5
P/E(x)	64.6	52.7	45.1	34.8
P/BV(x)	7.8	6.7	6.1	5.2
P/ABV(x)	8.0	6.9	6.2	5.3
DPS (Rs)	-	7.5	2.6	4.1
Dividend Payout Ratio(%)	-	16.6	5.0	6.0
Dividend Yield(%)	-	0.3	0.1	0.2

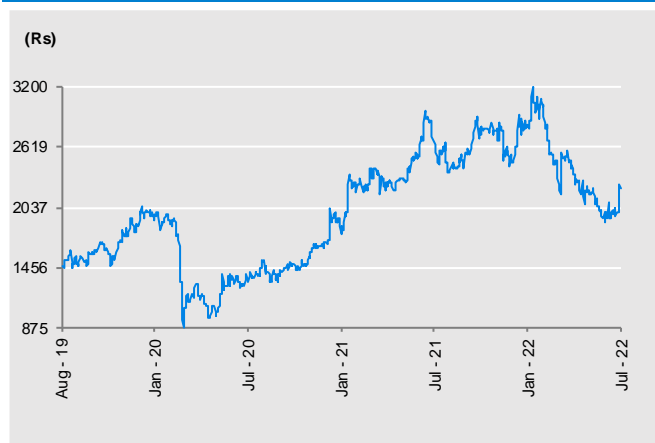
## Asset Quality

Y/e Mar	FY21	FY22	FY23E	FY24E
Gross NPAs(Rs m)	739	892	939	1,018
Net NPA(Rs m)	538	697	739	790
Gross NPAs to Gross Adv.(%)	1.0	1.0	0.9	0.8
Net NPAs to net Adv.(%)	0.7	0.8	0.7	0.6
NPA coverage(%)	27.2	21.9	21.3	22.4

## Du-Pont as a % of AUM

Y/e Mar	FY21	FY22	FY23E	FY24E
NII	5.2	6.4	6.2	6.3
NII INCI. Securitization	5.2	6.4	6.2	6.3
Total income	6.4	6.9	6.7	7.0
Operating Expenses	2.6	2.9	2.8	2.8
PPOP	3.9	4.0	3.9	4.2
Total Provisions	0.4	0.2	0.2	0.2
RoAA	2.9	3.0	2.9	3.1
Avg. Assets/Avg. net worth	4.5	4.6	4.9	5.2
RoAE	12.9	13.7	14.1	16.1

Source: Company Data, PL Research

**Price Chart**
**Recommendation History**


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	08-Jul-22	BUY	2,300	2,006
2	08-May-22	Accumulate	2,300	2,172
3	09-Apr-22	BUY	3,500	2,485
4	11-Jan-22	BUY	3,454	2,734
5	02-Dec-21	BUY	3,500	2,810

**Analyst Coverage Universe**

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	AAVAS Financiers	BUY	2,300	2,006
2	Axis Bank	BUY	940	727
3	Bank of Baroda	BUY	125	105
4	Can Fin Homes	BUY	675	538
5	City Union Bank	BUY	170	145
6	DCB Bank	Hold	120	81
7	Federal Bank	BUY	135	99
8	HDFC	BUY	2,900	2,378
9	HDFC Bank	BUY	1,740	1,362
10	ICICI Bank	BUY	950	800
11	IDFC First Bank	UR	-	34
12	IndusInd Bank	BUY	1,300	1,018
13	Kotak Mahindra Bank	Accumulate	1,950	1,827
14	LIC Housing Finance	Accumulate	435	351
15	Punjab National Bank	BUY	50	31
16	State Bank of India	BUY	600	487

**PL's Recommendation Nomenclature (Absolute Performance)**

<b>Buy</b>	: > 15%
<b>Accumulate</b>	: 5% to 15%
<b>Hold</b>	: +5% to -5%
<b>Reduce</b>	: -5% to -15%
<b>Sell</b>	: < -15%
<b>Not Rated (NR)</b>	: No specific call on the stock
<b>Under Review (UR)</b>	: Rating likely to change shortly



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