

AU Small Finance Bank



BSE SENSEX

62,411

S&P CNX

18,053



Stock Info

	AUBANK IN
Bloomberg	AUBANK IN
Equity Shares (m)	1,331
M.Cap.(INRb)/(USD b)	447.7 / 5.4
52-Week Range (INR)	733 / 468
1, 6, 12 Rel. Per (%)	7/-8/11
12M Avg Val (INR M)	1581
Free float (%)	74.4

Financials Snapshot (INR b)

Y/E March	FY22	FY23E	FY24E
NII	32.3	43.9	55.1
PPoP	18.2	21.2	27.3
PAT	11.3	14.1	17.5
NIM (%)	5.4	5.6	5.6
EPS (INR)	18.0	21.8	26.4
EPS Gr (%)	-5.1	21.0	21.1
BV/Sh. (INR)	118.7	163.8	190.2
ABV/Sh. (INR)	116.7	161.2	186.3

Ratios

RoE (%)	16.6	15.4	14.9
RoA (%)	1.9	1.8	1.8

Valuations

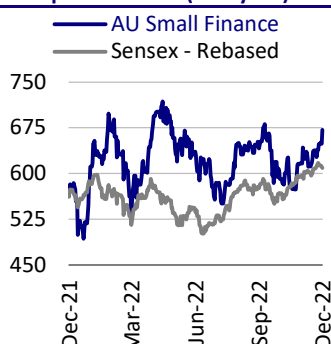
P/E (x)	37.3	30.8	25.5
P/BV (x)	5.7	4.1	3.5
P/ABV (x)	5.8	4.2	3.6

Shareholding pattern (%)

As On	Sep-22	Jun-22	Sep-21
Promoter	25.6	28.2	28.4
DII	21.3	18.4	20.9
FII	38.5	35.1	32.5
Others	14.6	18.3	18.3

FII Includes depository receipts

Stock's performance (one-year)



CMP: INR672

TP: INR750 (+12%)

Buy

Robust growth potential in SBL and Commercial Banking

Prudent underwriting to enable strong asset quality

We attended the fourth session of AUBANK's virtual Insights Day. The management dwelled upon its two SBUs: Secured Business loans and Commercial Banking. As these businesses provide significant growth opportunities, the management aims to grow this book at a healthy pace. It intends to offer superior digital capabilities and cross-sell its wide bouquet of services, which will enhance its fee income. Here are the key takeaways from that session:

Secured Business loans (SBL) – Mr. Amar Bahl, Head SBL

- It has made a segment-wide and profile-wise questionnaire to assess cash flow and the income profile of borrowers for the purpose of underwriting. It has put in place a robust mechanism and has an in-house team to assess the property and the collateral offered.
- The bank has created a sustainable model for a deep understanding of the business and to assess each factor in greater detail.
- MSMEs constitute 30% to India's GDP, 50% of its exports, and employs ~110m.
- Around 75% of AUBANK's exposure is to borrowers (average exposure of up to INR2.5m) with lower capex and OPEX requirements. Rajasthan and Madhya Pradesh are home to ~2.6m MSMEs, which offers it significant growth opportunities. Over 30% of the book is outside Rajasthan and Madhya Pradesh. It has increased the number of branches under SBL lending to 450.
- It offers collateral-backed loans of INR0.2m-10m with a tenure up to 15 years.
- Snapshot:** Average tenure stands at 101 months, with an ATS of ~INR1m and a LTV of ~46%. Around 75% of its customers are NTB, with a GNPA of 2.69%. About 70% of its customers make payments without any follow up. Even customers that availed of the moratorium have started to make payments.
- About 63% of its book sports a RoI of 14-18% and a ticket size of sub-INR1.5m. The bank is witnessing good opportunities in the Mid segment as well.
- Sourcing mix:** Direct sourcing (73%), AU Connect – local city referral (21%), cross-sell (3.5%), digital (1.5%), and BC (1%). Sourcing via alternate channels are gaining scale and growing at a faster pace.
- Credit score mix:** New to credit (16%), 700 and above (68%), 650-699 (12%), 600-649 (3%), and less than 600 (1%).
- To assess the collateral, the bank follows a dual legal check and an in-house technical team. Around 85% of collateral are self-occupied properties, with 75% being residential and 98% fully constructed.
- The underwriting process has been made more stringent, with a reduction in portfolio concentration to COVID-impacted sectors.
- Portfolio concentration in the Education/Hospitality/Daily and Allied sector has fallen to 1.5%/1.3%/0.7% from 6.3%/2.2%/1.8% earlier.

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- As most of the impacted sectors have either recovered or are in the last phase of a recovery, the management believes it is well placed to capture this growth opportunity and is likely to grow at a healthy pace.
- As SBL is a low OPEX and a high margin business, it aids overall profitability of the bank.

Commercial Banking – Mr. Vivek Tripathi, Head Commercial Banking

- Commercial Banking includes Business Banking, Agri Banking, NBFC lending, Real Estate lending, and Transaction Banking services. Business and Agri Banking constitute 70% of the total business.
- **Business mix:** ~55% is working capital and 45% is term loans.
- Commercial Banking customers have a deposit balance of INR52.7b.
- The business has a C/I ratio of 35%. The recurring fee income profile stands at 28% of NIM, with a RoA of over 2.5% and very low credit cost. Around 98% of its book sports a GNPA of 0.48%.
- A large part of the book (barring Real Estate) is at a floating rate, which is linked to the repo rate and is reset on a quarterly basis.
- AUBANK's market share in Commercial Banking stands at 0.2%, with the share of Private Banks constantly rising, providing a significant growth opportunity.
- **Business Banking:** ATS stands at INR8.5m, with working capital constituting 70% of total loans. WIRR stands at 10.15%, with GNPA at 0.17%.
- **Sourcing mix:** Branch (32%), self-sourced via referrals (29%), and channel partner (39%). Urban areas account for 58% of the book, while 42% is from its core region, with 80% being PSL compliant. Around 63% of the book has a ticket size of less than INR50m.
- **Agri Banking:** ATS stands at INR9.8m, with working capital constituting 60% of total loans. WIRR stands at 10.11%, with GNPA at 0.74%.
- **Sourcing mix:** Branch (19%), self-sourced via referrals (34%), and AU Value (47%). Urban areas account for 54% of the book, while 46% is from its core regions, with 93% being PSL compliant. Around 64% of the book has a ticket size of less than INR50m.
- **NBFC lending:** It has an exposure to 146 NBFCs, with 90% of the book sporting an investment grade. ATS stands at INR130m, with secured lending constituting 78%. Average residual tenure stands at 21 months. This floating rate book is linked to the repo rate, with an IRR of 10.8% (up 110bp since Mar'22). GNPA stands at a mere 0.01%.
- **REG book:** The focus remains on growing the cash flow backed business in Tier I cities, while reducing the mix in the LAP business. AUBANK is focusing on loans with an ATS of less than INR150m and Affordable Housing projects.
- Affordable Housing constitutes 42% of the book. RERA projects constitute 92% of the portfolio, with an average loan cycle of 30 months. ATS stands at INR142m, with average Retail ticket size of INR9m.
- GNPA ratio stands at 1.85%, with 97% of the book being current. Only three customers are 90+dpd. No customer loans disseminated after Apr'17 have turned into an NPA. GNPA is 100% provided for and the book has a security/receivable cover of 1-5-2x/2-2.5x.

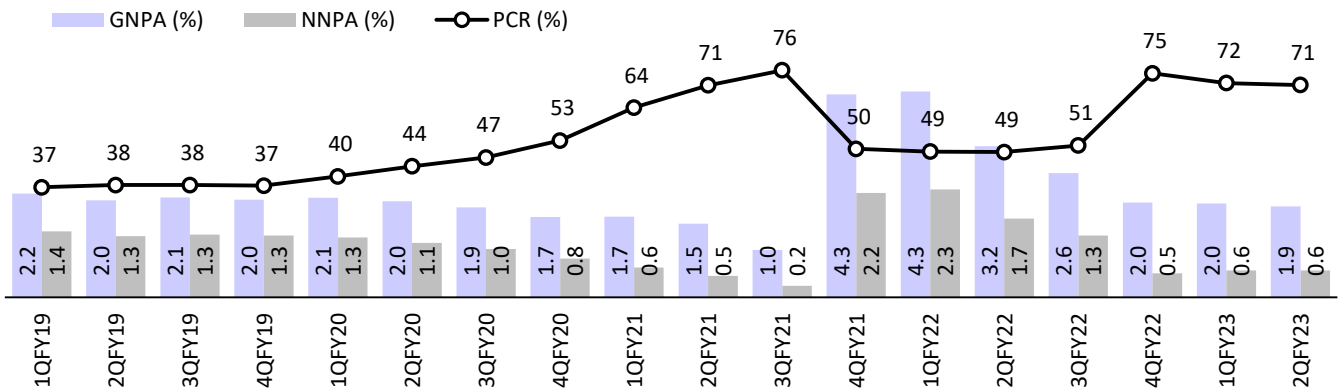
- **Transaction banking:** The number of customers on-boarded have grown 4x in the past few years. The management aims to build the CASA business and expand the bank's product suite.
- Overall, its focus remains on expanding digital adoption of internal processes and digital channels for a superior customer experience.

Valuation and view

AUBANK has been reporting a healthy performance, led by an expansion in margin and controlled credit cost. On the business front, growth in advances remains strong. The traction in deposits, particularly Retail deposits, remains healthy. It carries contingent reserves of INR1.29b (25bp of loans), which, coupled with a 17% coverage on restructured assets, provides comfort. We expect 25% earnings CAGR over FY22-24, with a RoA/RoE of 1.8%/14.9% in FY24. **We maintain our Buy rating, with a TP of INR750 (premised on 3.6x Sep'24E BV).**

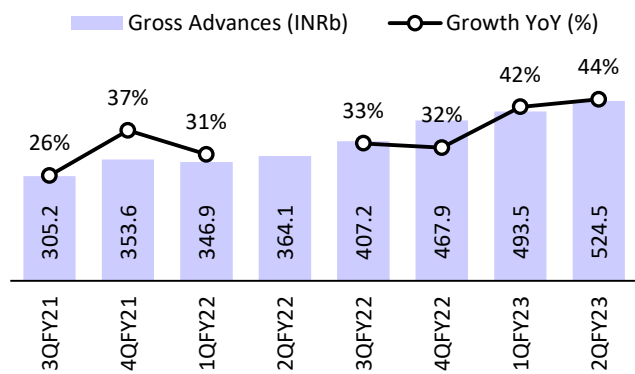
Story in charts

Exhibit 1: PCR stands healthy ~71%; the GNPA/NNPA ratio improves to 1.9%/0.6% in Sep'22



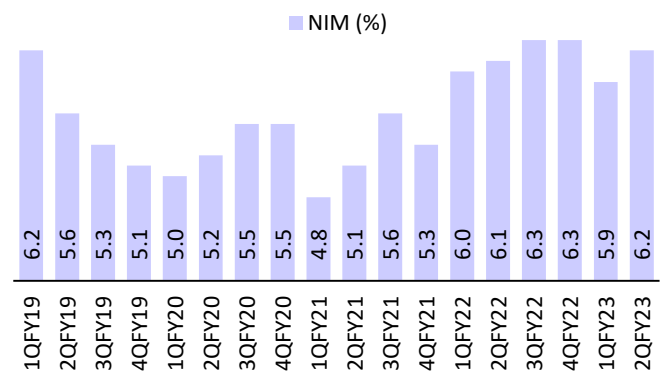
Source: Company, MOFSL

Exhibit 2: Gross advances grew 44% YoY and 6.3% QoQ in 2QFY23



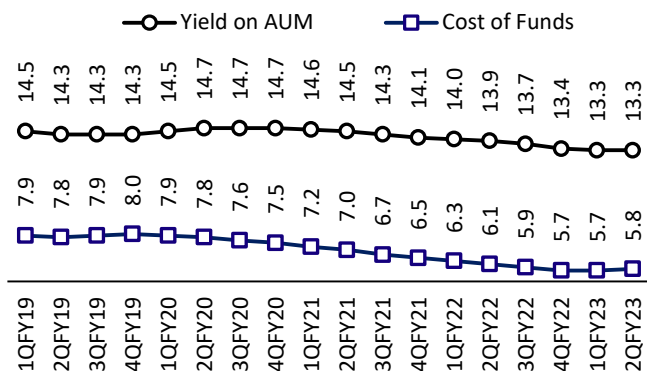
Source: Company, MOFSL

Exhibit 3: Margin improves by 30bp QoQ to 6.2% in 2QFY23



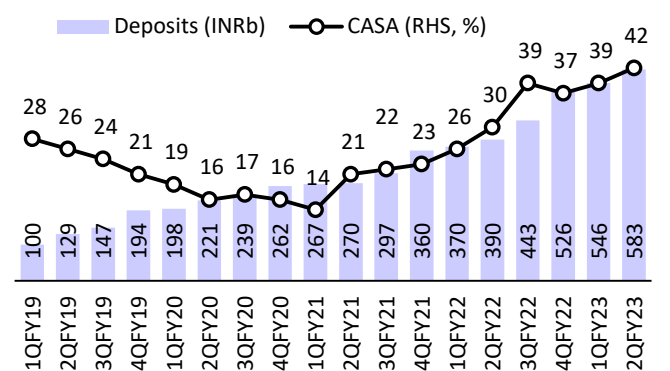
Source: Company, MOFSL

Exhibit 4: Yields on gross advances stood flat QoQ, while cost of funds increases by 10bp in 2QFY23



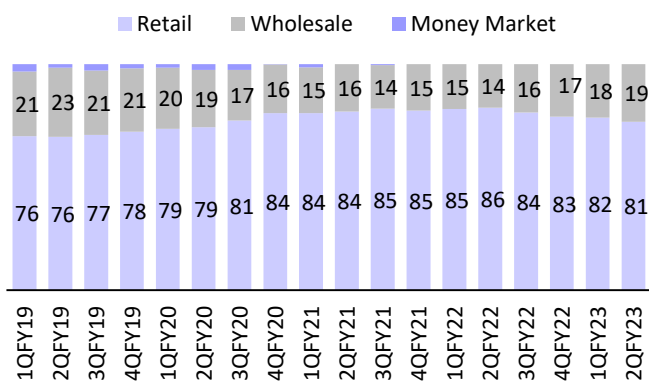
Source: Company, MOFSL

Exhibit 5: Robust traction in deposit mobilization (up ~49% YoY). The CASA ratio stands healthy ~42%



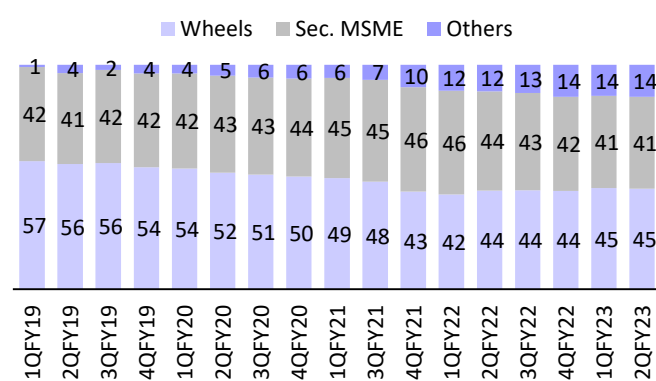
Source: Company, MOFSL

Exhibit 6: Retail mix dominates with a share of ~81%



Source: Company, MOFSL

Exhibit 7: Vehicles and MSME constitute ~86% of Retail loans



Source: Company, MOFSL

Valuation and view

- AUBANK continues to scale up its key business lines of Vehicle and MSME loans. The management aims to expand into new segments: Housing and Gold loans, Consumer Durable Financing, Credit Cards, among others. Growth has picked up over the last few quarters, with demand accruing across segments. We expect a 28% loan CAGR over FY22-24.
- The bank has shown strong progress in building a granular liability franchise, with the proportion of deposits in overall funding constantly improving. The proportion of Retail TD rose to 54%. CASA and Retail TD grew to 73% and are expected to grow further as the customer vintage increases. As the bank has raised deposit rates by 60bp in Oct’22, which can result in an increase in the cost of funds, its impact on margin will be a key monitorable going forward.
- GNPA ratio improved by 6bp to 1.9%, while the NNPA ratio stood stable at 0.5%. Collection efficiency remained healthy at 108% in 2QFY23. PCR was stable at 71%. The total restructuring book fell to INR8.95b (~1.7% of total loans v/s 2.1% in Jun’22) on which the management made provisions of INR1.5b. AUBANK carries additional contingent provisions of INR1.29b (0.25% of loans). We estimate credit costs at 05%/0.6% over FY23/FY24.
- **Maintain our Buy rating with a TP of INR750:** AUBANK has been reporting a healthy performance, led by an expansion in margin and controlled credit cost. On the business front, growth in advances remains strong, while a healthy traction in deposits, particularly Retail. It carries contingent reserves of INR1.29b (25bp of loans), which, coupled with a 17% coverage on restructured assets, provides comfort. We expect 25% earnings CAGR over FY22-24, with a RoA/RoE of 1.8%/14.9% in FY24. **We maintain our Buy rating, with a TP of INR750 (premised on 3.6x Sep’24E BV).**

Exhibit 8: DuPont Analysis: Expect return ratios to remain healthy

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest Income	12.35	11.46	11.46	10.56	9.81	10.24	10.73
Interest Expense	5.78	6.24	6.36	5.51	4.45	4.65	5.18
Net Interest Income	6.57	5.22	5.11	5.05	5.36	5.59	5.56
Core Fee	2.45	1.71	1.43	1.21	1.41	1.19	1.15
Non-Interest income	2.71	1.80	1.89	3.10	1.65	1.33	1.37
Total Income	9.29	7.01	7.00	8.14	7.01	6.92	6.93
Operating Expenses	5.26	4.21	3.79	3.54	4.00	4.22	4.17
Employee cost	2.97	2.34	2.03	2.09	2.29	2.37	2.35
Others	2.29	1.87	1.76	1.45	1.71	1.85	1.83
Operating Profit	4.03	2.81	3.20	4.61	3.01	2.70	2.75
Core operating Profit	3.76	2.72	2.74	2.72	2.77	2.56	2.54
Provisions	0.93	0.55	0.76	1.49	0.60	0.30	0.39
NPA	0.39	0.29	0.17	1.08	0.19	0.25	0.34
Others	0.53	0.26	0.58	0.41	0.40	0.05	0.05
PBT	3.10	2.25	2.44	3.11	2.41	2.40	2.36
Tax	1.06	0.77	0.64	0.61	0.54	0.60	0.60
RoA	2.04	1.48	1.81	2.50	1.87	1.80	1.77
Leverage (x)	6.7	9.5	10.0	8.9	8.8	8.6	8.4
RoE	13.7	14.0	18.0	22.3	16.6	15.4	14.9

Source: MOFSL, Company

Financials and valuations

Income Statement							(INR m)	
Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	
Interest Income	17,672	29,488	42,859	49,501	59,217	80,414	106,450	
Interest Expense	8,267	16,064	23,769	25,846	26,876	36,491	51,320	
Net Interest income	9,405	13,425	19,089	23,654	32,341	43,923	55,130	
Growth (%)	20.0	42.7	42.2	23.9	36.7	35.8	25.5	
Other Income	3,881	4,620	7,061	14,209	9,937	10,434	13,564	
Total Income	13,285	18,045	26,150	37,864	42,278	54,356	68,694	
Growth (%)	-16.6	35.8	44.9	44.8	11.7	28.6	26.4	
Operating Expenses	7,526	10,826	14,179	16,584	24,128	33,154	41,374	
Growth (%)	113.3	43.8	31.0	17.0	45.5	37.4	24.8	
Operating Profit	5,759	7,219	11,972	21,279	18,150	21,203	27,320	
Growth (%)	-53.6	25.3	65.8	77.7	-14.7	16.8	28.8	
Core Operating Profit	5,377	6,998	10,246	12,737	16,721	20,079	25,163	
Growth (%)	-4.8	30.1	46.4	24.3	31.3	20.1	25.3	
Total Provisions	1,326	1,418	2,832	6,694	3,610	2,350	3,880	
PBT	4,433	5,801	9,140	14,585	14,541	18,853	23,440	
Tax	1,513	1,984	2,392	2,878	3,242	4,751	5,907	
Tax Rate (%)	34.1	34.2	26.2	19.7	22.3	25.2	25.2	
PAT	2,920	3,818	6,748	11,707	11,298	14,102	17,533	
Growth (%)	-64.5	30.7	76.8	73.5	-3.5	24.8	24.3	
Adj. PAT	2,920	3,818	5,962	6,002	11,298	14,102	17,533	
Growth (%)	-12.4	30.7	56.2	0.7	88.2	24.8	24.3	

Balance Sheet							
Y/E MARCH	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Equity Share Capital	5,714	5,847	6,082	6,244	6,298	6,643	6,643
Reserves and Surplus	17,098	25,782	37,164	55,477	68,429	102,186	119,719
Equity Net worth	22,812	31,629	43,247	61,721	74,727	108,829	126,362
Deposits	79,233	194,224	261,639	359,793	525,846	667,825	854,816
Growth (%)	NA	145%	35%	38%	46%	27.0%	28.0%
Borrowings	76,389	86,134	103,353	70,297	59,908	69,313	81,790
Other liabilities	9,894	14,241	12,670	23,071	29,884	33,769	39,847
Total Liabilities	188,328	326,228	421,431	515,913	690,778	880,149	1,103,228
Current Assets	17,612	17,402	33,697	47,813	59,285	63,830	66,478
Investments	30,506	71,617	106,682	108,154	153,065	198,985	254,700
Growth (%)	41.9	134.8	49.0	1.4	41.5	30.0	28.0
Loans	133,121	228,187	269,924	346,089	460,953	593,789	759,367
Growth (%)	103.2	71.4	18.3	28.2	33.2	28.8	27.9
Net Fixed Assets	3,861	4,470	4,480	4,824	6,226	7,160	8,234
Other assets	3,227	4,552	6,648	9,033	11,250	16,386	14,449
Total Assets	188,328	326,228	421,431	515,913	690,778	880,149	1,103,228
Total Assets (incl. off BS)	215,586	340,501	460,437	546,944	708,135	904,890	1,130,770

Asset Quality	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
GNPA (INR m)	2,697	4,701	4,578	15,028	9,244	10,825	14,276
NNPA (INR m)	1,693	2,945	2,173	7,555	2,308	3,104	4,283
GNPA Ratio	2.0	2.1	1.7	4.3	2.0	1.8	1.9
NNPA Ratio	1.3	1.3	0.8	2.2	0.5	0.5	0.6
Slippage Ratio	2.1	2.5	2.5	4.2	3.6	2.0	2.0
Credit Cost	1.0	0.6	1.0	2.0	0.7	0.4	0.5
PCR (Exc. Tech. write-off)	37.2	37.4	52.5	49.7	75.0	71.3	70.0

Financials and valuations

Ratios

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Yield and Cost Ratios (%)							
Avg. Yield - on IEA	13.1	12.1	12.1	11.2	10.4	10.9	11.3
Avg. Yield on loans	9.4	11.7	12.4	11.5	11.4	12.0	12.4
Avg. Cost of funds	7.3	7.4	7.4	6.5	5.3	5.5	6.1
NIM (On total assets)	6.6	5.2	5.1	5.0	5.4	5.6	5.6
NIM (On IEA)	7.0	5.5	5.4	5.3	5.7	5.9	5.9

Capitalization Ratios (%)

CAR	19.3	19.3	22.0	23.4	21.0	23.7	21.2
Tier I	18.4	16.0	18.4	21.5	19.7	22.8	20.6
Tier II	0.9	3.4	3.6	1.8	1.3	0.9	0.6

Business and Efficiency Ratios (%)

Loan/Deposit Ratio	168.0	117.5	103.2	96.2	87.7	88.9	88.8
CASA Ratio	26.9	18.5	14.5	23.0	37.3	34.3	35.4
Cost/Assets	5.3	4.2	3.8	3.5	4.0	4.2	4.2
Cost/Total Income ratio	56.7	60.0	54.2	43.8	57.1	61.0	60.2
Cost/Core Income ratio	58.3	60.7	58.1	56.6	59.1	62.3	62.2
Int. Expense/Int. Income ratio	46.8	54.5	55.5	52.2	45.4	45.4	48.2
Fee Income/Total Income ratio	26.3	24.4	20.4	15.0	20.1	17.1	16.6
Non-Int. Income/Total Income ratio	29.2	25.6	27.0	37.5	23.5	19.2	19.7
Investment/Deposit Ratio	38.5	36.9	40.8	30.1	29.1	29.8	29.8
Emp. Cost/Total Expense ratio	56.5	55.5	53.6	59.1	57.2	56.1	56.2

Profitability and Valuations

	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
RoE	13.7	14.0	18.0	22.3	16.6	15.4	14.9
RoA	2.0	1.5	1.8	2.5	1.9	1.8	1.8
RoRWA	2.5	2.0	3.0	4.2	3.1	3.0	2.9
Book Value (INR)	39.9	54.1	71.1	98.8	118.7	163.8	190.2
Growth (%)	14.2	35.5	31.4	39.0	20.0	38.1	16.1
Price-to-BV (x)	16.8	12.4	9.4	6.8	5.7	4.1	3.5
Adjusted BV (INR)	38.2	51.3	69.5	92.0	116.7	161.2	186.3
Growth (%)	12.0	34.5	35.4	32.5	26.9	38.1	15.6
Price-to-ABV (x)	17.6	13.1	9.7	7.3	5.8	4.2	3.6
EPS (INR)	5.1	6.6	11.3	19.0	18.0	21.8	26.4
Growth (%)	-79.5	28.9	71.3	67.9	-5.1	21.0	21.1
Price-to-Earnings (x)	131.1	101.7	59.4	35.4	37.3	30.8	25.5

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall be within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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