

AU Small Finance Bank

Conservatism brings growth-margin trade-off into play

AUBANK posted its highest-ever quarterly earnings on the back of lower-than-expected credit costs (30bps annualised), partly offset by elevated operating expenses. The bank calibrated its loan growth (+38% YoY) to mirror the growth in deposits (~400bps QoQ rundown in CASA), resulting in moderation across segments such as wheels, home loans, and commercial banking. In a rising interest rate environment, AUBANK has chosen to remain conservative in order to protect its margins and asset quality. However, continued investments in franchise-building and new businesses are likely to be a drag on medium-term profitability vectors. We continue to watch out for signs of operating leverage and the impact of incremental rate transmission on margins. We tweak our FY23E/FY24E estimates by +6% each for better risk-adjusted margins; maintain REDUCE, with a TP of INR610 (3.1x Sep-24 ABVPS).

- **Calibrated deceleration in loan growth leads to PPOP miss:** Sequential moderation in loans (+38% YoY), stable margins (~6.2%) and elevated opex from continued investments in people, tech and distribution led to a miss on PPOP (+11% YoY). With limited lending rate transmission, reflecting intense competition for high-grade assets, the rise in incremental funding costs, despite the focus on SA and retail TD, is likely to keep margins under check.
- **Healthy collections cushion asset quality:** GNPA improved marginally to 1.8%, led by steady recoveries on the back of organic collections (collection efficiency at 107%). The restructured book declined 30bps QoQ (1.4% of loans). With sufficient buffers in place (PCR at 72%), the management remains confident of a soft landing in the restructured portfolio.
- **Conservative outlook displays growth-margin trade-off:** Management's strategy to prioritise margins and quality of business over growth augurs well. Consistent with our thesis, the visible signs of softer NIMs coupled with a sustained high opex from franchise-building efforts are likely to keep return ratios in check.

Financial summary

(INR bn)	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	FY22	FY23E	FY24E	FY25E
NII	11.5	8.2	40.5%	10.8	6.4%	32.3	44.0	52.1	65.1
PPOP	5.6	4.6	21.2%	5.0	11.4%	18.2	20.4	26.9	33.6
PAT	3.9	3.0	30.1%	3.4	14.7%	11.3	13.9	17.0	20.9
EPS (INR)	5.9	9.5	-38.5%	5.2	12.0%	35.9	20.9	25.5	31.4
ROAE (%)						16.4	15.1	14.4	15.3
ROAA (%)						1.9	1.8	1.7	1.7
ABVPS (INR)						229.9	158.1	181.7	212.7
P/ABV (x)						2.7	3.9	3.4	2.9
P/E (x)						17.3	29.7	24.4	19.8

Change in estimates

(INR bn)	FY23E			FY24E			FY25E		
	Old	New	Δ	Old	New	Δ	Old	New	Δ
Net advances	576	585	1.5%	719	729	1.5%	898	910	1.4%
NIM (%)	6.0	6.1	15 bps	5.9	5.9	-3 bps	5.9	5.9	3 bps
NII	42.6	44.0	3.2%	51.7	52.1	0.7%	64.0	65.1	1.8%
PPOP	22.5	20.4	-9.3%	27.4	26.9	-1.6%	34.3	33.6	-2.2%
PAT	13.1	13.9	6.5%	15.9	17.0	6.8%	19.8	20.9	5.6%
Adj. BVPS (INR)	158.4	158.1	-0.2%	179.3	181.7	1.3%	206.0	212.7	3.2%

Source: Company, HSIE Research

REDUCE

CMP (as on 19 Jan 2023)	INR 621
Target Price	INR 610
NIFTY	18,108

KEY CHANGES	OLD	NEW
Rating	REDUCE	REDUCE
Price Target	INR 594	INR 610
	FY23E	FY24E
EPS %	6.5%	6.8%

KEY STOCK DATA

Bloomberg code	AUBANK IN
No. of Shares (mn)	667
MCap (INR bn) / (\$ mn)	414/5,089
6m avg traded value (INR mn)	1,172
52 Week high / low	INR 733/525

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	(0.8)	9.7	(1.7)
Relative (%)	(3.7)	(1.4)	(3.0)

SHAREHOLDING PATTERN (%)

	Jun-22	Sep-22
Promoters	28.2	25.6
FIs & Local MFs	19.5	19.8
FPIs	38.2	38.9
Public & Others	14.1	14.4
Pledged Shares	0.0	0.0

Source : BSE

Pledged shares as % of total shares

Krishnan ASV

venkata.krishnan@hdfcsec.com
+91-22-6171-7314

Deepak Shinde

deepak.shinde@hdfcsec.com
+91-22-6171-7323

Neelam Bhatia

neelam.bhatia@hdfcsec.com
+91-22-6171-7341

Disclosure:

Authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. SEBI conducted the inspection and based on their observations have issued advise/warning. The said observations have been complied with. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. Research Analyst or his/her relative or HDFC Securities Ltd. does have/ does not have any financial interest in the subject company. Also Research Analyst or his relative or HDFC Securities Ltd. or its Associate may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Further Research Analyst or his relative or HDFC Securities Ltd. or its associate does have/does not have any material conflict of interest.

HDFC Securities Limited (HSL) is a SEBI Registered Research Analyst having registration no. INH000002475.

Disclaimer:

This report has been prepared by HDFC Securities Ltd and is solely for information of the recipient only. The report must not be used as a singular basis of any investment decision. The views herein are of a general nature and do not consider the risk appetite or the particular circumstances of an individual investor; readers are requested to take professional advice before investing. Nothing in this document should be construed as investment advice. Each recipient of this document should make such investigations as they deem necessary to arrive at an independent evaluation of an investment in securities of the companies referred to in this document (including merits and risks) and should consult their own advisors to determine merits and risks of such investment. The information and opinions contained herein have been compiled or arrived at, based upon information obtained in good faith from sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. Descriptions of any company or companies or their securities mentioned herein are not intended to be complete. HSL is not obliged to update this report for such changes. HSL has the right to make changes and modifications at any time. This report is not directed to, or intended for display, downloading, printing, reproducing or for distribution to or use by, any person or entity who is a citizen or resident or located in any locality, state, country or other jurisdiction where such distribution, publication, reproduction, availability or use would be contrary to law or regulation or what would subject HSL or its affiliates to any registration or licensing requirement within such jurisdiction. If this report is inadvertently sent or has reached any person in such country, especially, United States of America, the same should be ignored and brought to the attention of the sender. This document may not be reproduced, distributed or published in whole or in part, directly or indirectly, for any purposes or in any manner.

Foreign currencies denominated securities, wherever mentioned, are subject to exchange rate fluctuations, which could have an adverse effect on their value or price, or the income derived from them. In addition, investors in securities such as ADRs, the values of which are influenced by foreign currencies effectively assume currency risk. It should not be considered to be taken as an offer to sell or a solicitation to buy any security.

This document is not, and should not, be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. This report should not be construed as an invitation or solicitation to do business with HSL. HSL may from time to time solicit from, or perform broking, or other services for, any company mentioned in this mail and/or its attachments.

HSL and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

HSL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

HSL and other group companies, its directors, associates, employees may have various positions in any of the stocks, securities and financial instruments dealt in the report, or may make sell or purchase or other deals in these securities from time to time or may deal in other securities of the companies / organizations described in this report.

HSL or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

HSL or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction in the normal course of business.

HSL or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither HSL nor Research Analysts have any material conflict of interest at the time of publication of this report. Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. HSL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Research entity has not been engaged in market making activity for the subject company. Research analyst has not served as an officer, director or employee of the subject company. We have not received any compensation/benefits from the subject company or third party in connection with the Research Report.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Murlu V Karkera Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

HDFC Securities Limited, SEBI Reg. No.: NSE, BSE, MSEI, MCX: INZ000186937; AMFI Reg. No. ARN: 13549; PFRDA Reg. No. POP: 11092018; IRDA Corporate Agent License No.: CA0062; SEBI Research Analyst Reg. No.: INH000002475; SEBI Investment Adviser Reg. No.: INA000011538; CIN - U67120MH2000PLC152193 Mutual Funds Investments are subject to market risk. Please read the offer and scheme related documents carefully before investing.

HDFC securities**Institutional Equities**

Unit No. 1602, 16th Floor, Tower A, Peninsula Business Park,

Senapati Bapat Marg, Lower Parel, Mumbai - 400 013

Board: +91-22-6171-7330 www.hdfcsec.com