



KEY HIGHLIGHTS

1. RESULTS OVERVIEW:

- AU reported PAT in Q1FY24 that grew 45% YoY and declined 9% QoQ.
- CASA deposits increased by 15% YoY, gross advances/deposits increased by 29%/7%/YoY.
- As the bank continues to spend in developing the technological platform, operating expenses increased 37% YoY. Consequently, the C/I ratio rose by 200bp QoQ to 65%.

2. MANAGEMENT COMMENTARY:

- NIM saw a 38bp QoQ significant drop. This is a result of deposit repricing being frontloaded, according to management. The management advised that the increase in deposit costs will be gradual going forward. In comparison to NIM of 5.7% in Q1, it confirmed NIM guidance of 5.5–5.7%.
- Management expects to grow deposits and advances in the range of 20-25%.
- The bank plans to open an additional 50+ branches and touchpoints in FY24.
- The bank expects GNPA to be 1.5%-1.75% and NNPA to be 0.5%-0.6%.

3. BUSINESS OVERVIEW:

- AU Small Finance Bank is a small finance bank (SFB) that has recently transitioned from a prominent, retail focused NBFC, which primarily served low and middle-income individuals and businesses that have limited or no access to formal banking and finance channels. It received a license from the Reserve Bank of India to set up an SFB on December 20, 2016 and it was the only NBFC categorized as an asset finance company to obtain such license.

4. MANAGEMENT GUIDANCE

- In comparison to the repo rate's 250 bps increase over the same period, the cost of deposits has increased by 86 basis points (bps) year over year. The management indicated that the impact of deposit repricing would be limited moving ahead and that the majority of the impact has already been taken into account in NIM.
- Loans with fixed rates to those with fluctuating rates are divided 66%:34%. Once the interest rate cycle changes, it is anticipated that the fixed rate book will have a favorable effect on margins.
- Bank stated that it is improving its liability-side product proposition in order to attract new clients and strengthen relationships with current ones.
- Over 6 lakh active credit cards have been issued by the bank, 69% of which have been provided to NTB clients.
- The bank has made a substantial move towards an end-to-end digital transformation for its wheels business, which is anticipated to result in future cost reductions.

5. BANKING INDUSTRY

- The RBI has granted SFB licenses to 12 players as of FY23 in keeping with the government's emphasis on inclusive banking and financial inclusion. The four main directives for SFBs are: a minimum CRAR of 15%; a minimum of 25% of their total branches in unbanked rural areas; a minimum of 50% of their loan portfolio made up of loans and advances of up to Rs2.5 million; and a minimum of 75% of their ANBC designated for PSL.

6. VALUATION AND OUTLOOK:

- Among India's publicly traded banks, AU BANK stands out as one of the institutions with the quickest growth. The bank has continually increased its AUM, on average at a stunning +32% growth rate, during the previous 10 years. Even in the difficult year of FY21, which was impacted by the COVID-19 epidemic, AUBANK was able to keep up a respectable YoY growth rate of 22%. Retail asset account for 89% of the advances and 91% of the advances are secured in nature. The bank has successfully diversified its asset book, lowering its reliance on a particular industry and broadening its client base.
- We value the company at 32.5x FY24 EPS to arrive at the target of 840.

RECOMMENDATION - BUY

CMP - 725

TARGET - 840 (16%)

Industry	Bank - Private
NSE CODE	AUBANK
BSE CODE	540611
Market Cap (₹ Cr)	48645.43
Shares Outstanding (in Cr)	66.70
52 wk High/Low (₹)	795 / 548
P/E	31.45
P/BV	4.30
Face Value (₹)	10.00
Book Value (₹)	169.72
EPS (FY22) (₹)	21.42
Dividend Yield (%)	0.17

SHAREHOLDING PATTERN

	Jun'23	Mar'23	Dec'22
Promoters	25.53	25.54	25.55
Mutual Funds	10.29	11.53	11.63
FII/FPI	41.61	39.74	39.61
Non-Institutions	13.61	14.09	14.20
Promoter Pledging	0.00	0.00	0.00

FINANCIAL SNAPSHOT (₹ Cr)

Y/E March	2022A	2023A	2024E
Core			
Interest Earned	5921	8205	10666
Other Income	993	1034	1328
Total Income	6915	9239	11994
Interest Expense	2687	3780	5095
Profit from Ordinary Activity	1454	1864	2312
PAT	1130	1427	1734
EPS	17.94	21.42	26
Ratios			
ROE (%)	16.56	15.52	14.8
ROA (%)	1.87	1.79	1.6
Valuation			
P/E (x)	34.72	27.03	32.5
P/BV (x)	5.25	3.53	4.3

Historical & Industrial Val Ratios

Historical P/E	31.45
Industry P/E	22.76
Historical P/B	4.30
Industry P/B	3.07



Liability Trends	Q1FY24	Q4FY23	Q3FY23	Q2FY23	Q1FY23	Q4FY22	Q3FY22
Total Deposit	69315	69365	61101	58335	54631	52585	44278
Current Account	3240	3680	2819	2867	2211	2569	1784
Saving Account	21046	22980	20652	21807	19006	17039	15595
CASA Ratio (%)	35	38	38	42	39	37	39

QUARTERLY PERFORMANCE (STANDALONE)

(₹ Cr)

Y/E March	FY22			FY23			FY24	FY24E*	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3		Q1
Interest Earned	1404.75	1496.45	1667.03	1820.20	1992.29	2118.07	2274.85	2458.34	10666
YoY change (%)	15.86%	18.66%	28.99%	34.48%	41.83%	41.54%	36.46%	35.06%	35%
Other Income	191.92	275.65	311.37	159.15	247.36	294.89	333.06	315.12	1328
Total Income	1596.68	1772.10	1978.41	1979.35	2239.65	2412.96	2607.91	2773.46	11994
Interest Expense	651.62	676.03	730.47	844.20	908.94	965.34	1061.65	1212.13	5095
Operating Expenses	552.58	637.63	765.60	741.08	831.92	891.92	975.35	1015.29	4324
Operating Profit	392.47	458.43	482.33	394.07	498.78	555.71	570.92	546.04	2575
Provision	4.63	55.97	93.23	38.37	42.96	32.64	40.88	32.98	263
Profit Before Tax	387.84	402.46	389.11	355.70	455.83	523.07	530.04	513.06	2312
Tax	109.33	100.42	43.03	87.83	113.23	130.24	105.41	126.16	578
Net Profit After Tax	278.51	302.05	346.08	267.87	342.60	392.83	424.63	386.90	1734
YoY change (%)	-13.47%	-36.94%	104.81%	31.83%	23.01%	30.05%	22.70%	44.44%	21.5

Source: Company, Hem Securities Research.

EWS*Insights into the assumptions:

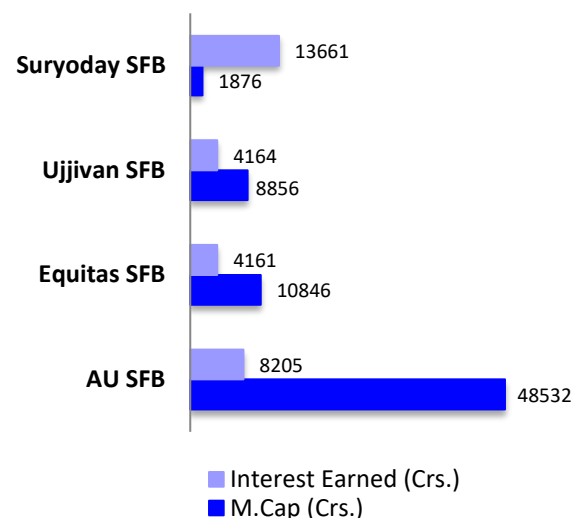
- 1> Bank credit growth is likely to increase up, Credit growth has started showing signs of recovery.
- 2> Asset quality improved as lower slippages and better recoveries helped the overall performance.
- 3> Banks are preparing to expand their digital offerings through partnerships with fintech companies or in-house development.
- 4> The rise in home demand, combined with lenders initial concentration on secured lending, resulted in considerable growth in housing loans across banks and HFCs.
- 5> Improvement in collection.
- 6> Given the economy's return to normalcy, the forecast for company growth and credit costs remains positive.



INDUSTRY OVERVIEW

- The remarkable credit CAGR of 40% for SFBs from FY18 to FY23, in contrast to the 10% growth of outstanding credit for Scheduled Commercial Banks (SCBs) and 15% for private sector banks, illustrates their capacity to penetrate underserved sectors by providing specialized financial products and services.
- The RBI changed its accommodative stance and raised the repo rate by a total of 225 basis points over the previous five monetary policy meetings, which led to an increase in interest rates. Banks may gain in the short run on the margin front because the majority of loans are made on a floating rate basis and higher deposit costs may take some time to take impact.
- This remarkable CAGR demonstrates the SFBs' prowess in spotting untapped markets and offering tailored financial goods and services to fit those markets' unique demands.
- The four main directives for SFBs are: a minimum CRAR of 15%; a minimum of 25% of their total branches in unbanked rural areas; a minimum of 50% of their loan portfolio made up of loans and advances of up to Rs2.5 million; and a minimum of 75% of their ANBC designated for PSL.
- The CASA deposits for SFBs are predicted to have increased at a pace of 66% CAGR between FY18 and FY23, giving them an edge over NBFCs and allowing them to build up their asset books.

KEY PLAYERS



PEER PERFORMANCE

(₹ Cr)

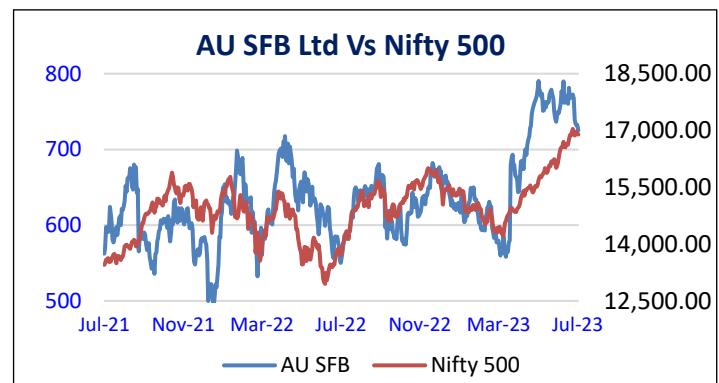
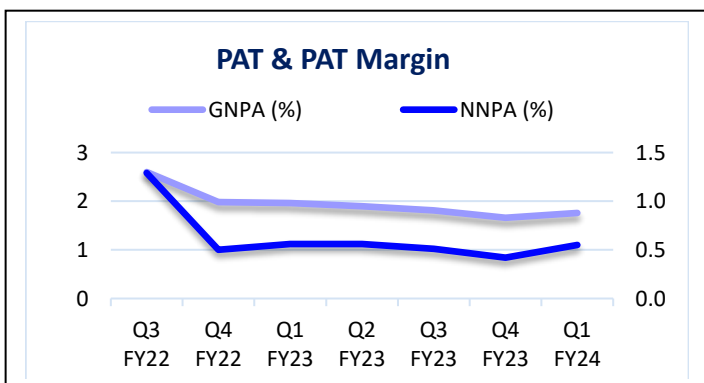
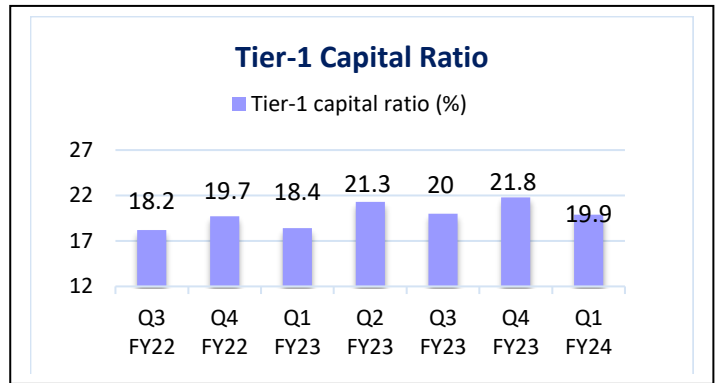
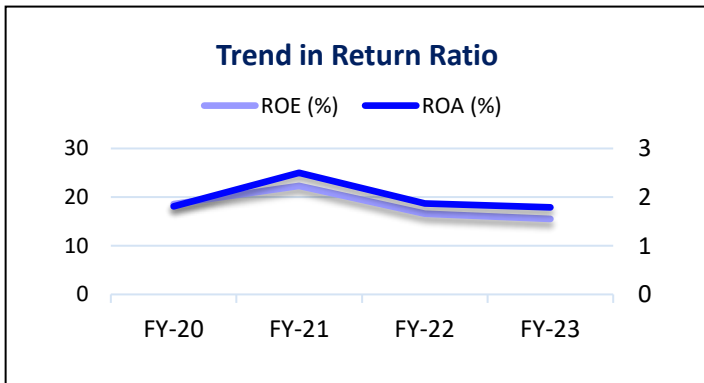
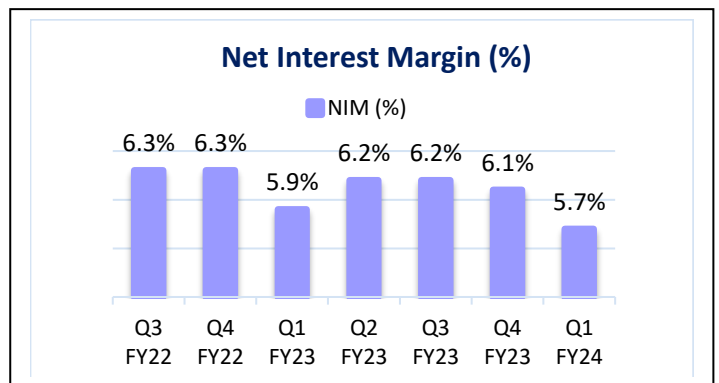
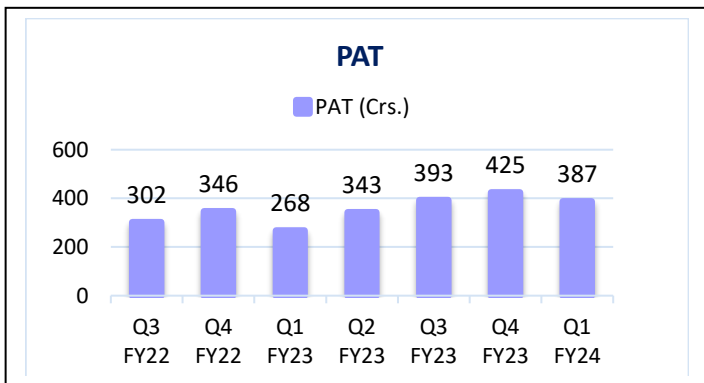
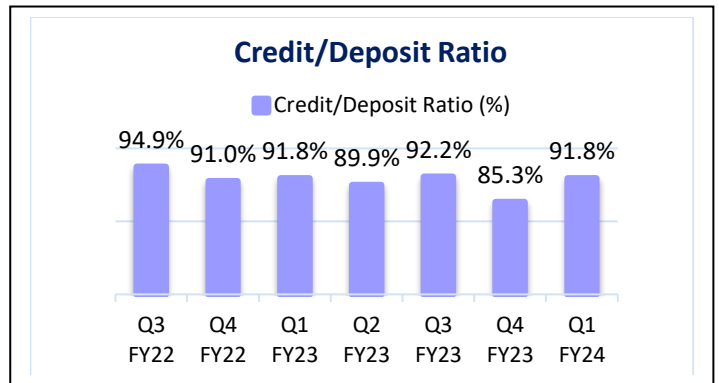
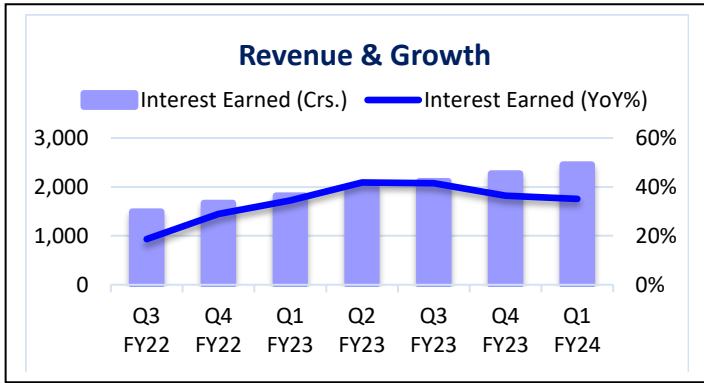
Particulars	AU SFB	Equitas SFB*	Ujjivan SFB	Suryoday SFB*
Market Cap	48532	10846	8856	1876
Interest Earned (FY-23)	8205	4161	4164	1183
Profit from Ordinary Activities	1864	768	1467	100
PAT	1428	573	1100	78
EPS(Rs)	21.86	4.71	5.82	7.32
Total Deposit	69315	25381	26660	5167
CASA Ratio	35	42	24.6	21.7
Net Interest Income	1246	707	793	210
NIM	5.7	9.10	9.2	10.4
Total Advances	63635	27861	25326	6114
Gross NPA (%)	1.76	2.6	2.4	3.1
Net NPA (%)	0.55	1.14	0.06	1.5
Provision Coverage Ratio	73	56.9	97.6	51.5
Capital Adequacy Ratio	21.5	23.8	26.7	33.72

Source: Company, Hem Securities Research.

*Represents Q4FY22 Data



STORY IN CHARTS





INVESTMENT RATIONALE:

- The bank has proven it is capable of managing asset quality in the Post-Covid environment and keeping non-performing assets (NPAs) at a level below peers. Following Covid-19, the GNPA's peaked at 4.3% as of March 31, 2021, and since the second wave of the pandemic was disrupted, they continued to be elevated. However, the asset quality of AU SFB has significantly improved as a result of the gradual relaxation of lockdown restrictions and the recovery of client cash flows. The bank reported an improved GNPA of 1.66% as of March 31, 2023, while the NNPA was at 0.42%, both of which are anticipated to be sustained over the next several years.
- Apart from the bank's track record of raising need-based capital, continuous internal accruals support capitalization, which is appropriate relative to the volume of activities of the bank. The bank's stated net value as of March 31, 2023, as compared to March 31, 2022, was Rs 10,977 crore as opposed to Rs 7,514 crore. This increase was the result of a capital raising of Rs 2500 crore during the year (Rs 2000 crore by QIP and Rs 500 crore by Tier II bonds). As of March 31, 2023, the bank's stated overall and tier 1 capital adequacy ratios (CAR) were comfortable at 23.6% and 21.8%, respectively, and both of these indicators had typically maintained over 15%. With CAR at above 18% on a steady state basis, the bank is anticipated to have adequate capitalization.
- The average cost of funding decreased as more money was obtained through refinancing from financial institutions and low cost deposits. Cost of funds was 9.6% in the 2017 fiscal year before falling to 8.43% in 2018 and then to 5.9% in 2022. It did, however, slightly increase in fiscal 2023 and Q1FY24. 6.6% was the value in Q1FY24.
- Bank has a proven track record of consistent execution over past few years. Further, the bank keeps investing for future to build a sustainable, scalable and long term business model.
- As of FY23, the bank asset book's composition has changed, with the categories of car finance and small business loans making up 32% and 31%, respectively, of its AUM. With this diversification, AUBANK shows its dedication to meeting a wider range of client demands while minimizing reliance on a single market.

RISK FACTORS:

- Despite progress, CASA's share of total liabilities is still modest compared to larger private banks.
- AU SFB's portfolio is concentrated across the four states to the extent of 76%, with Rajasthan alone accounting for 35% of the advances
- Any new Regulatory framework by RBI might impact the industry.
- The success and delinquencies of the Bank's aggressive product launches need to be tracked.
- Slippage ratio rose sharply to 2.6%, from 1.6% QoQ due to seasonality in SBL and wheels.
- NIM declined sharply by 38bp QoQ. Management attributes this to frontloading of deposit repricing.

COMPANY RECAP

- AU Small Finance Bank is a small finance bank (SFB) that has recently transitioned from a prominent, retail focused NBFC, which primarily served low and middle-income individuals and businesses that have limited or no access to formal banking and finance channels. It received a license from the Reserve Bank of India to set up an SFB on December 20, 2016 and it was the only NBFC categorized as an asset finance company to obtain such license. It commenced its SFB operations with effect from April 19, 2017. Prior to such date, the company was categorized as a 'Systemically Important, Non-Deposit Accepting Asset Finance Company' (NBFCND- AFC) by the RBI. As an NBFC, it operated in three business lines: vehicle finance; micro, small and medium enterprises (MSMEs) loans; and small and medium enterprises (SMEs) loans.
- SFBs were created with an objective to extend financial services to the informal segment of the society and support financial inclusion at grass root level. SFBs still form a small part of the banking sector with little over 1% market share in advances and deposits. As of March 2022. SFBs, albeit on a smaller base, have outperformed commercial banks in deposit and advances growth.
- Mr. Sanjay Agarwal is the promoter and Managing Director & CEO of AU Small Finance Bank and has over 28 years of strategic executive experience. He is a Commerce graduate from Government College, Ajmer and all-India rank holder Chartered Accountant. He possesses extensive experience in Accountancy, Agriculture and Rural Economy, Banking, Economics, Finance & Treasury, Small Scale Industry, Human Resource, Risk Management and Business Management.



ANNUAL PERFORMANCE

Financials & Valuations						
Income Statement	(₹ Cr)					
	2019	2020	2021	2022	2023	2024E
Interest Earned	2949.13	4285.88	4950.05	5921.73	8205.41	10666
YoY change (%)	66.88%	45.33%	15.50%	19.63%	38.56%	35%
Other Income	461.91	706.09	1420.93	993.69	1034.46	1328
Total Income	3411.04	4991.98	6370.98	6915.43	9239.87	11994
Interest Expense	1606.53	2376.94	2584.61	2687.61	3780.13	5095
Operating Expense	1082.61	1417.86	1658.43	2412.77	3440.27	4324
Provision	141.78	283.20	669.44	360.97	154.83	263
Profit from Ordinary Activities Before Tax	580.13	913.97	1458.50	1454.07	1864.65	2312
YoY change (%)	30.85%	57.55%	59.58%	-0.30%	28.24%	24%
Tax	198.32	239.19	287.82	324.24	436.72	578
Net Profit After Tax	381.81	674.78	1170.68	1129.83	1427.93	1734
YoY change (%)	30.74%	76.73%	73.49%	-3.49%	26.38%	21.5%
EPS	6.53	11.09	18.75	17.94	21.42	26
YoY change (%)	27.76%	69.90%	68.99%	-4.31%	19.38%	21.5%

Source: Company, Hem Securities Research.

Balance Sheet					
Y/E March	(₹ Cr)				
	2019	2020	2021	2022	2023
Share Capital	292	304	312	315	667
Reserves	2,696	4,073	5,963	7,199	10,311
Borrowings	28,036	36,499	43,009	58,575	75,664
Other Liabilities	1,599	1,267	2,307	2,988	3,575
Total Liabilities & Equity	32,623	42,143	51,591	69,078	90,216
Fixed Assets	440	438	477	609	707
CWIP	7	10	5	14	33
Investments	7,162	10,668	10,815	15,306	20,072
Other Assets	25,014	31,027	40,294	53,149	69,404
Total Assets	32,623	42,143	51,591	69,078	90,216

Source: Company, Hem Securities Research.



Ratios				
Y/E March (Basic (INR))	2020	2021	2022	2023
Profit and Loss Account				
Net interest income	1909	2365	3234	4425
Employee expenses	759	980	1378	1793
ROE (%)	18.56	22.31	16.56	15.52
ROA (%)	1.81	2.50	1.87	1.79
EPS	11.09	18.75	17.94	21.42
Key Performance Indicator				
NIM (%)	4.65	4.71	4.80	5.03
CASA (%)	14.48	23	37.29	38.43
Yield on Assets (%)	15.58	14.30	12.85	14.05
Cost of Funds (%)	6.51	6.01	4.59	5
Cost-to-Income	54.22	43.80	57.07	63.01
GNPA (%)	1.70	4.30	2	1.66
NNPA (%)	0.81	2.20	0.50	0.42
Provision Coverage Ratio (%)	53	50	75	75
Credit/Deposit (%)	103.17	96.19	87.66	84.22
Capital Adequacy Ratio (%)	21.99	23.37	20.99	23.59
Tier I (%)	18.36	21.53	19.69	21.78
Valuations Ratios				
P/E (x)	22.93	32.70	34.72	27.03
P/BV (x)	3.58	6.20	5.25	3.53
Dividend Yield (%)	0	0	0.08	0.17
Growth (%)				
Advances	18.4	29.8	32.3	26.4
Deposit	34.7	37.5	46.1	31.9
Net Interest Income	42	23.8	36.7	36.8
Net Profit	76.73	73.49	-3.49	26.38

Source: Company, Hem Securities Research.



RATING CRITERIA

INVESTMENT RATING	EXPECTED RETURN
BUY	>=15%
ACCUMULATE	5% to 15%
HOLD	0 to 5%
REDUCE	-5% to 0
SELL	<-5%

RECOMMENDATION SUMMARY

DATE	RATING	TARGET
28-July-2023	BUY	840

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Name of the Research Analyst: Madhur Mandhana

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3.	Research Analyst or his/her relative or HSL has any other material conflict of interest at the time of publication of the Research Report	No
4.	Research Analyst has served as an officer, director or employee of the subject company(ies)	No
5.	HSL has received any compensation from the subject company in the past twelve months	No
6.	HSL has received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
7.	HSL has received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
8.	HSL has received any compensation or other benefits from the subject company or third party in connection with the research report	No
9.	HSL has managed or co-managed public offering of securities for the subject company in the past twelve months	No
10.	Research Analyst or HSL has been engaged in market making activity for the subject company(ies)	No

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