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AU Small Finance Bank Ltd

UNDER PERFORMER

Sector: Banks/Mid Cap | Earnings Update – 1QFY21

27 July 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 12 states and 1 union territory, with 594 branches, 359 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 ₹300.3bn as of 1QFY21 with a deposit base of ₹266.2bn.

Sensex	38,038
Nifty	11,165
Price	₹ 790
Target Price (12 months)	₹ 711
Recommendation	UNDER PERFORMER

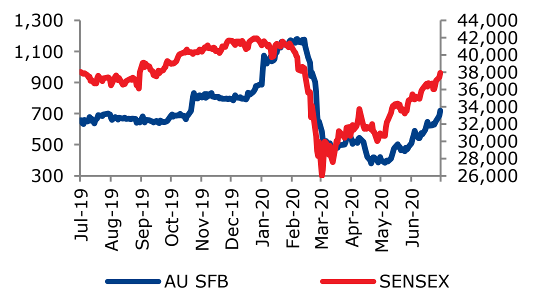
52 Week High/Low	₹ 1,217.7/366.2
Bloomberg / Reuters	AUBANK.IN/ AUFI.NS
Equity (shares in mn)	306.4
Mkt. Cap in bn	₹ 242.3/ $ 3.2
Avg. Daily Vol. ('000)	1,009.3
Avg. Daily Vol. (mn)	₹ 798.3 /$ 10.6

Shareholding	Jun-19	Mar-20	Jun-20
Promoters (%)	32.2	31.0	29.0
FII (%)	24.7	28.7	30.0
DII (%)	13.7	15.4	13.5
Others (%)	29.4	24.9	27.5
Pledge (% of promoter holding)	7.0	7.0	0.0

Valuation Summary (₹ bn)

Y/E March	2020	2021E	2022E
Net Interest Inc	19.1	21.4	26.2
Other Inc	7.1	8.2	9.9
Pre Prov Profit	12.0	18.2	22.2
PAT	6.7	6.9	10.0
EPS (₹)	22.2	22.5	32.7
EPS growth (%)	68.6	1.5	45.4
PE (X)	35.6	35.1	24.1
P /ABV (X)	5.8	5.1	4.4
Div Yield (%)	-	0.1	0.1
ROA (%)	1.6	1.5	1.8
ROE (%)	15.8	14.6	18.1
CAR (%)	22.0	19.4	19.4

Performance(%)	1M	3M	12M
AU SFB	48.2	29.3	9.4
SENSEX	9.2	23.8	-1.1



Robust quarter buoyed by decline in Opex; Management's focus on improving collections efficiency and maintaining asset quality will limit credit growth in FY21, higher covid provisioning though provide comfort on potential slippages warrants caution

- The bank's loan AUM increased by 17.3% YoY (down 2.8% QoQ) to ₹300.3bn driven by growth in Retail segment, up 25.1% YoY (constituting 83.8% of book). Within retail segment Housing loans increased by 2.7x, coupled with wheels and SBL-MSME segment which registered 15% YoY and 32.3% YoY, growth respectively. The management is focused on maintaining a retail book with granular focus.
- During the quarter, disbursements witnessed a steep decline of 70% YoY and stood at ₹11.8bn. This decline in growth was on account of the lockdown and slow opening up of the economy in parts of the country. The disbursement includes ₹2.4bn under TLTRO 2.0.
- Despite lockdown, 1QFY21 witnessed steady deposits growth to reach ₹266.2bn compared to ₹198.4bn in 1QFY21 (up 34% YoY & 2% QoQ). The bank continues to focus 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 19% in 1QFY20.
- On a sequential basis, NIMs declined to 4.8% (down 70 bps QoQ) despite a 30bps QoQ decline in Cost of funds to 7.2% in 1Q21 on account of moratorium. The incremental cost of funds in 1QFY21 stood at 6% indicating a downward trajectory in the quarters ahead. On asset quality, the bank continued to maintain low GNPA (%) at 1.7% (down 40bps YoY, muted QoQ) in 1QFY21. This was on account of lower slippages at ₹50mn (vs ₹1.4bn in 1QFY20). As on 30th June, ~11% of borrowers by value availed the moratorium. Post moratorium period ending in August will provide a clear picture of the asset quality.
- The C/I ratio declined to 41.4% (1650bps QoQ) in 1QFY21 in line with broad management guidance for cost reduction in FY21E. This was driven by 10% QoQ decline in Other opex and 4% QoQ decline in Employee costs.
- The bank set aside provisions ₹1.4bn for Covid (apart from ₹1.38bn in 4QFY20). This resulted in ₹2.7bn for Covid provisions constituting 1%/10% of Gross Advances/Moratorium book respectively.
- On the back of gradual opening up of the economy in 1QFY21, the bank has shown improvement in collections from ~54% in April to 90% in June. In addition, ~67% of customers are active (average in normal period ~80%). Indicating the bank is moving towards normality owing to its robust underwriting and quality assets. 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. However, the recent run-up in the stock price has factored in the positives. The stock is currently trading at 4.4x P/ABV of FY22E. Assigning a P/ABV of 4x for FY22E, we arrive at a target of ₹711, and hence downgrade our rating on the stock from BUY to UNDER PERFORMER.

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 1QFY21

Y/E March (₹ bn)	1QFY21	1QFY20	YoY Growth	4QFY20	QoQ Growth
Net Interest Income	5.2	4.0	30.4%	5.5	-7.0%
Other Income	2.3	2.1	7.0%	1.8	23.3%
Pre Provisioning Profit	4.5	2.9	53.2%	3.2	41.1%
PAT	2.0	1.9	5.5%	1.2	64.2%
Cost / Income (%)	41.4	59.6		57.9	
Gross NPA (%)	1.7	2.1		1.7	
Net NPA (%)	0.6	1.3		0.8	
Prov Coverage Ratio (%)	63.7	40.5		52.5	
CAR (%)	21.7	18.6		22.0	

Arjun Prasad Pasumarthi +91-44-40047363 arjunpp@chola.murugappa.com

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RESEARCH			
Kedar S Kadam	DGM & Head of Research	+91-44 - 4004 7361	kedarsk@chola.murugappa.com
Mugilan K	Technical Analyst	+91-44 - 4004 7353	mugilank@chola.murugappa.com
Arjun Prasad Pasumarthi	Fundamental Analyst	+91-44 - 4004 7363	arjunpp@chola.murugappa.com
Ammar Haider	Associate	+91-44 - 4004 7360	amarh@chola.murugappa.com
INSTITUTIONAL SALES			
Venkat Chidambaram	Head of FII Business & Corporate Finance*	+91-44 - 24473310	venkatc@chola.murugappa.com
Kishore K Ganti	Mumbai	+91-22-26597239	kishorekg@chola.murugappa.com
Bhavesh Katariya	Mumbai	+91-9860297739	bhaveshgk@chola.murugappa.com
Balaji H	Compliance Officer	044 - 30007226	balajih@chola.murugappa.com

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