

**CMP: INR 629**

**Rating: BUY**

**Target Price: INR 720**

**Stock Info**

BSE	540611
NSE	AUBANK
Bloomberg	AUBANK IN
Reuters	AUFI.BO
Sector	Banks
Face Value (INR)	10
Equity Capital (INR Cr)	669
Mkt Cap (INR Cr)	46,894
52w H/L (INR)	813/ 554
Avg Yearly Vol (in 000')	2,962

**Shareholding Pattern %**

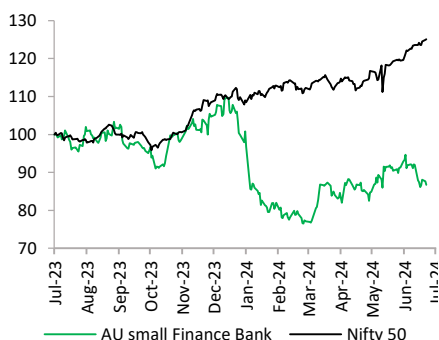
(As on June, 2024)

Promoters	22.92
Public & Others	77.08

**Stock Performance (%)**

	1m	6m	12m
AU Small Finance Bank	-5.06	-8.48	-11.4
Nifty 50	2.6	13.98	23.67

**AU Small Finance Bank Vs Nifty 50**



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AU Small Finance Bank reported profit of INR 5.03 bn (up 30% YoY/ up 36% QoQ), driven by increase in NII. NII improved by 54% YoY/ 44% QoQ, at INR 19.21 bn, mainly due to the impact of merger of AU SFB with Fincare Small Finance Bank. Other income grew by 73% YoY and -2% QoQ at INR 5.46 bn and provisions by 868% YoY at INR 3.19 bn. NIM of the bank is at 6%, which is up by 90 bps QoQ and 30 bps YoY, owing to the reduction in cost of funds, increase in portfolio yield and margin expansion due to merger. Operating profit increased by 81% YoY/ 49% QoQ to INR 9.88 bn.

**Other income grew by 52% YoY, led by increasing credit card business, banking fee and recovery from bad debts:** The other income during the quarter stood at INR 5.46 bn v/s INR 3.15 bn in the Q1FY24 (up 72% YoY, up -2% QoQ). This YoY increase in other income was driven by the increase in credit card business, cross sell and processing fees. Credit card income came at INR 1.01 bn (up 84% YoY, up 15% QoQ), cross sell and deposit related fee was up by 157% YoY at INR 1.42 bn during the quarter, loan asset processing fee was up by 39% YoY to INR 2.3 bn and Miscellaneous income increased from INR 0.35 bn in Q4FY24 to INR 0.54 bn (up 140% YoY/ up 55% QoQ).

**Deterioration in asset quality, partly impacted due to merger impact and seasonality:** The asset quality for the bank deteriorated as GNPA and NNPA ratio were up by 11 bps and 8 bps on QoQ basis to 1.78% and 0.63%, respectively. Asset quality degraded due to the seasonality and merger impact. Bad debts recovery came at INR 0.36 bn v/s INR 0.15 bn in Q4FY24 v/s 0.08 bn in Q1FY24. Further, slippages came in at INR 5.43 bn as compared to INR 2.96 bn in Q4FY24.

**NIMs expansion driven by reduction in cost of funds, increase in portfolio yield and margin expansion due to merger:** NIMs during the quarter was at 6% v/s 5.1% in Q4FY24 v/s 5.7% in Q1FY24 (up 90bps QoQ/ up 30 bps YoY). NIMs are expected to moderate in FY25 and remain within the guided range. Cost of funds reduced by 7 bps QoQ at 7.03%. Full year cost of funds is now expected to be in the range of 35-40 bps over cost of Fund of FY24, instead of earlier guidance of 40-45 bps.

**Transition to universal bank:** The board has given the approval for applying to transition into a universal bank. We believe this is positive for the bank as some of the restrictions/guidelines under SFB will be removed - a) reduction in the PSL requirement from 75% to 40%, b) removal of the stipulation that 50% of the portfolio must be in ticket size of INR 0.25 million or less, and c) decrease in the CRAR requirement from 15% to 12%, widening the target market and increase trust within depositors.

**Valuation & View:** AU Small Finance Bank experienced an improvement NII, aided by reduction in cost of funds, increase in portfolio yield and margin expansion due to merger. Asset quality was impacted due to merger impact and seasonality. Despite these challenges, loan growth remained robust. NIMs are likely to moderate going forward. The bank has completed the merger with Fincare Small Finance Bank with effect from 1st April 2024. The management is focused on improving its RoA for the next 3 years by disbursing loans in high yielding business verticals. We maintain our BUY rating on the stock with target price of INR 720, based on 2.6x FY27E P/ABV. Our target price is upside of 15% from the current levels.

**Exhibit 1: Financial Performance**

Y/E Mar (Rs Bn)	FY22	FY23	FY24	FY25E	FY26E	FY27E
NII	32	44	52	67	89	112
PAT	11	14	15	18	25	32
Networth	75	110	126	142	166	197
Adj BVPS (Rs)	231	160	181	203	235	277
EPS (Rs)	36	21	23	26	38	48
P/E (x)	18	29	27	24	17	13
P/Adj BV (x)	2.7	3.9	3.5	3.1	2.7	2.3

Source: Arihant Research, Company Filings

## Q1FY25 - Quarterly Performance (Standalone)

P&L (Rs Bn)	Q1FY25	Q1FY24	Q4FY24	YoY	QoQ
Interest Earned	37.69	24.58	28.29	53%	33%
Interest Expended	18.48	12.12	14.92	52%	24%
<b>NII</b>	<b>19.21</b>	<b>12.46</b>	<b>13.37</b>	<b>54%</b>	<b>44%</b>
Other Income	5.46	3.15	5.56	73%	-2%
<b>Net Income</b>	<b>24.66</b>	<b>15.61</b>	<b>18.93</b>	<b>58%</b>	<b>30%</b>
Opex	14.78	11.80	12.28	25%	20%
<b>PPOP</b>	<b>9.88</b>	<b>5.46</b>	<b>6.64</b>	<b>81%</b>	<b>49%</b>
Provisions	3.19	0.33	1.33	868%	141%
<b>PBT</b>	<b>6.69</b>	<b>5.13</b>	<b>4.55</b>	<b>30%</b>	<b>47%</b>
Tax	1.66	1.26	0.84	32%	98%
<b>PAT</b>	<b>5.03</b>	<b>3.87</b>	<b>3.71</b>	<b>30%</b>	<b>36%</b>

Asset Quality					
GNPA	16.13	11.21	12.37	44%	30%
NNPA	5.63	3.47	4.01	62%	40%
GNPA (%)	1.78%	1.76%	1.67%	2bps	11bps
NNPA (%)	0.63%	0.55%	0.55%	8bps	8bps

Source: Arianth Research, Company Filings

## Key Concall Highlights

## Guidance for FY25

- The bank targets over INR 600 bn worth disbursements for FY25.
- Credit cost is expected to be around 1.1% mark.
- Micro finance book mix in total loans to be at around 10% of total loans
- Total deposit growth is expected to be around 25%.
- Cost of fund is expected to increase in coming quarters.
- NIMs are expected to be around 5.7 to 5.8% range.
- Cost-to-income ratio is targeted at 63% in FY25.
- The bank expects ROA to be around 1.6% mark in FY25.

## Highlights

- The Net interest income on reported basis was up 54.1% YoY/ 43.6% QoQ at INR 19.21 bn, mainly due to merger impact.
- Net interest margin increased by 90 bps QoQ to 6.0% in Q1FY25, driven by higher disbursements towards better yielding products and reducing cost of funds by consumption of surplus liquidity.
- Provisions increased from INR 1.33 bn in Q4FY24 to INR 3.19 bn (Q1FY24: INR 0.33bn). Provisions were higher due to additional provisions towards micro finance and merger on reported basis.
- Net profit thus was up 29.9% YoY/ 36% QoQ to INR 5.03 bn in Q1FY25.
- Asset quality was partly impacted due to merger impact and seasonality.
- In Q1FY25, the asset quality marginally deteriorated as GNPA and NNPA ratio were up by 11 bps and 8 bps on QoQ basis to 1.78% and 0.63%, respectively.
- Slippages for the quarter stood at INR 5.43 bn versus INR 2.96 bn QoQ and INR 3.17 bn YoY.
- In Q1FY25, AU SFB posted advances growth of 42% YoY/ 22.5% QoQ to INR 896.52 bn, due to merger. On proforma merged basis advances were up 5% sequentially.
- Wheels (vehicle finance) business saw a growth of 7.8% QoQ while small business loans were up 14.6% QoQ.
- Home loans jumped by 38.7% QoQ, due to merger, while business banking growth was at 3% QoQ.
- Disbursement yields for the quarter stood at 15.8% with 82% of disbursements done towards high ROA business. On merged basis yield on gross loans were up 3 bps QoQ.
- Disbursement yield on standalone basis for the bank were up by 33 bps for wheels, 41 bps for micro banking and 113 bps towards housing.
- **The bank board has decided to file for "Universal Banking license" and it will be done soon.**
- **AU Small finance bank has done tie-ups with Bajaj life and Star health for insurance distribution.**

## Key Financials

P&L (INR Bn)	FY22	FY23	FY24A	FY25E	FY26E	FY27E
Interest income	59.2	82.1	105.5	133.6	177.8	232.9
Interest expense	26.9	37.8	54.0	66.2	89.0	120.6
<b>NII</b>	<b>32.3</b>	<b>44.3</b>	<b>51.6</b>	<b>67.4</b>	<b>88.8</b>	<b>112.3</b>
Non-interest income	9.9	10.3	17.5	18.4	22.0	25.7
<b>Net revenues</b>	<b>42.3</b>	<b>54.6</b>	<b>69.0</b>	<b>85.8</b>	<b>110.8</b>	<b>138.0</b>
Operating expenses	24.1	34.4	43.9	53.7	65.8	80.5
<b>PPOP</b>	<b>18.2</b>	<b>20.2</b>	<b>25.2</b>	<b>32.1</b>	<b>45.0</b>	<b>57.5</b>
Provisions	3.6	1.5	4.4	8.4	11.2	14.8
Exceptional Items	0.0	0.0	0.8	0.0	0.0	0.0
<b>PBT</b>	<b>14.5</b>	<b>18.6</b>	<b>20.0</b>	<b>23.6</b>	<b>33.8</b>	<b>42.7</b>
Tax	3.2	4.4	4.6	6.0	8.5	10.8
<b>PAT</b>	<b>11.3</b>	<b>14.3</b>	<b>15.3</b>	<b>17.7</b>	<b>25.3</b>	<b>31.9</b>

Balance sheet	FY22	FY23	FY24A	FY25E	FY26E	FY27E
Share capital	3	7	7	7	7	7
Reserves & surplus	72	103	119	136	160	190
<b>Net worth</b>	<b>75</b>	<b>110</b>	<b>126</b>	<b>142</b>	<b>166</b>	<b>197</b>
Deposits	526	694	872	1247	1686	2295
Borrowings	60	63	55	60	65	71
Other liability	30	36	42	22	21	18
<b>Total liabilities</b>	<b>691</b>	<b>902</b>	<b>1094</b>	<b>1472</b>	<b>1939</b>	<b>2581</b>
Fixed assets	6	7	9	9	10	10
Investments	153	201	271	364	526	761
Loans	461	584	732	938	1174	1471
Cash	59	94	64	147	215	323
Other assets	11	16	19	14	15	15
<b>Total assets</b>	<b>691</b>	<b>902</b>	<b>1094</b>	<b>1472</b>	<b>1939</b>	<b>2581</b>

Source: Arianth Research, Company Filings

Ratios	FY22	FY23	FY24A	FY25E	FY26E	FY27E
<b>Growth (%)</b>						
NII	37	37	17	31	32	26
PPOP	-15	11	25	28	40	28
PAT	-3	26	7	15	43	26
Advances	33	27	25	28	25	25
Deposits	46	32	26	43	35	36
<b>Spread (%)</b>						
Yield on Funds	10.1	10.6	10.8	10.6	10.6	10.4
Cost of Funds	5.3	5.6	6.4	5.9	5.8	5.9
Spread	4.8	4.9	4.4	4.7	4.8	4.6
NIM	5.5	5.7	5.3	5.4	5.3	5.0
<b>Asset quality (%)</b>						
Gross NPAs	2.0	1.9	2.0	2.0	2.2	2.2
Net NPAs	0.5	0.6	0.6	0.7	0.8	0.8
Provisions	75	70	69	65	64	66
<b>Return ratios (%)</b>						
RoE	16.4	15.4	13.0	13.2	16.4	17.6
RoA	1.9	1.8	1.5	1.4	1.5	1.4
<b>Per share (Rs)</b>						
EPS	36	21	23	26	38	48
BV	239	165	188	213	249	294
ABV	231	160	181	203	235	277
<b>Valuation (x)</b>						
P/E	17.5	29.3	27.4	23.8	16.6	13.2
P/BV	2.6	3.8	3.3	3.0	2.5	2.1
P/ABV	2.7	3.9	3.5	3.1	2.7	2.3

Source: Arianth Research, Company Filings

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Stock Rating Scale	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	-5% to -12%
SELL	<-12%

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