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SYSTEMATIX INSTITUTIONAL EQUITIES

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Institutional Equities

AAVAS Financiers Ltd

28 October 2023

Earnings inline; lower margin was a dampener

RESULT UPDATE

Sector: NBFCs Rating: BUY
CMP: 1,549 Target Price: Rs 2,000

Stock Info

Sensex/Nifty	63,782/19,047
Bloomberg	AAVAS IN
Equity shares	79 mn
52-wk High/Low	2077/1335
Face value	Rs 10
M-Cap	Rs 122bn/USD1.4bn
3-m Avg volume	USD 4.2mn

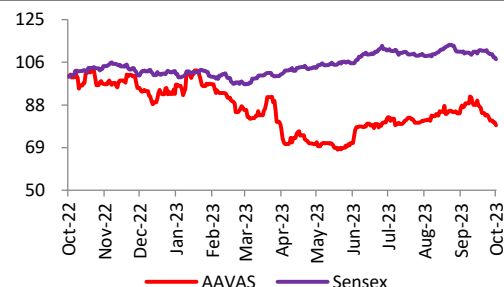
Financial Snapshot (Rs mn)

Y/E March	FY23	FY24E	FY25E
NII	7,976	9,649	11,749
PPP	5,608	6,797	8,323
PAT	4,296	5,138	6,290
EPS (Rs)	54.3	65.0	79.6
EPS Gr. (%)	21.0	19.6	22.4
BV/Sh (Rs)	414	472	544
Ratios			
NIM (%)	6.3	6.1	6.0
C/I ratio (%)	45.0	45.8	46.0
RoA (%)	3.5	3.4	3.5
RoE (%)	14.1	14.7	15.7
Payout (%)	0.0	10.0	10.0
Valuations			
P/E (x)	28.5	23.8	19.5
P/BV (x)	3.7	3.3	2.8
Div. Yield (%)	0.0	0.4	0.5

Shareholding pattern (%)

	Mar-22	Jun-23	Sep-23
Promoter	39.14	39.13	39.11
FII	38.83	35.01	35.49
DII	12.49	14.34	14.13
Others	9.53	11.51	11.24

Stock Performance (1-year)



AAVAS's Q2FY24 NII was marginally lower than expected at Rs2.2bn (vs. est. of Rs2.3bn) due to 35bps qoq contraction in NIMs, even as AUM growth remained steady at 22%. However, with higher other income and lower opex, operating profit/ PAT were inline at Rs1.6bn/ 1.2bn. Operating expenses declined 2% QoQ led by 13.6% QoQ decline in employee cost, on account of one off in Q1. Asset quality remained broadly stable, with GS3/NS3 marginally up by 4bp/ 3bp to 1.04%/0.76%. PCR on Stage 3 assets was slightly up from 26.9% in Q1 to 27.5% in Q2. 1+dpd improved by ~10bp QoQ to 3.6%. We estimate a 23% CAGR in AAVAS's AUM to deliver 21% CAGR in earnings over FY23-25E. We expect the RoA to remain stable at 3.5% and RoE to improve to 15.7% by FY25 (vs 14.1% in FY23) as the leverage builds up. Key risks: Inflation pressure might impact the demand for home loans.

Key result highlights

- AAVAS 2QFY24 operational performance was in line with our estimates. NII at Rs 2.22bn was marginally below our estimates mainly due to 35bps contraction in NIMs, even as the AUM growth was on expected lines at 22% YoY / 5% QoQ. HL AUM (70% of total loan portfolio) grew by 20.1% YoY (4.4% QoQ), while Mortgage AUM grew by 27.2% YoY (4.9% QoQ). Disbursement growth gathered pace and grew 18% QoQ (10% YoY).
- NIMs declined by 35bps QoQ to 5.9% mainly due to 11bps fall in yields and 18bps increase in cost of funds. OP/PAT at Rs 1.6bn / 1.2bn was in-line with our estimates. Provisions declined 2.5% QoQ at Rs 55mn resulting in credit cost of 0.15% vs 0.16% in Q1.
- Operating expenses declined 2% QoQ (moderated to 14% YoY vs avg 30% YoY in past few quarters) led by 13.6% QoQ decline in employee cost. Employee costs were lower on account of reversal of ESOP expenses. Thus, opex to AUM ratio also improved to 3.5% in Q2FY24 from 3.8% in Q2FY23 (3.7% in Q1FY24).
- Asset quality remained broadly stable, with GS3/NS3 marginally up by 4bp/ 3bp to 1.04%/0.76%. PCR on Stage 3 assets was slightly up from 26.9% in Q1 to 27.5% in Q2. 1+dpd improved by ~10bp QoQ to 3.6%. ECL/EAD was stable QoQ at 0.64%. Management guided that GS3 ratio in Non housing segment to be in the range of 1-1.25% while in housing segment it will continue to remain < 1%.

Valuation & recommendation

AAVAS reported in-line earnings aided by steady AUM growth and asset quality, even as there was slight disappointment on the margins front. Nevertheless, we maintain our earnings estimates for FY24/25 as Disbursement pick up pace from Q3 onwards and margins expected to be maintained at current levels. We continue to remain positive on AAVAS's robust business model and underwriting practices, which has demonstrated healthy earnings growth and asset quality. AUM growth guidance maintained at 20-25% YoY for FY24. We have a buy rating on the stock with a target price of Rs. 2000 valuing the company at 3.7x FY25E book value.

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Investors are advised to refer disclosures made at the end of the research report.

Management commentary

Business:

- Disbursement growth was moderate due to lag effect between sanctions and disbursements. Sanctions / disbursement ratio declined from 90% to 80%. Management expects disbursements to pick up in next couple of quarters.
- BT out run rate was steady QoQ at 0.5% of AUM per month.
- Avg. ticket size in non-housing loan was steady while in housing loans the avg. ticket size increased by 10% due to inflation and increase in property prices.

NIM/COF/Yields:

- Incremental borrowings were Rs 30.8bn raised at 8.1% in H1FY24.
- Yields declined by 10bps QoQ partly due to rate reduction for holding good customers and competitive environment.
- Un-availed sanctions from NHB to the tune of Rs 10bn.
- Share of borrowings from development financial institutions to be 10-15% in total borrowings.

Asset quality:

- As per RBI resolution framework 2.0, Rs 779 mn classified as stage 2 during the quarter of which Rs 575 mn under 0-30dpd. Total ECL provisions stood at Rs 797 mn.
- GS3 asset ratio stood at 1.04% of which 0.13% were upto 90dpd assets.
- Write-offs were Rs 20mn in H1.
- GS3 ratio guidance - Non housing loans: 1-1.25%, housing loans: <1%. Overall GNPA to be <1% and 1+dpd to be <5%.

Opex:

- Employee cost was down 13.6% QoQ as there was one time cost in Q1.
- Employee count and live accounts were 5731 and 1,98,947 at the end of Q2. Total sales force count was 3200.
- Added 4 branches in Q2. ~20-25 more branches to be added in H2.

Guidance:

- Spreads to be maintained at 5%+ levels. Incremental cost of borrowings to be 8-8.1%
- AUM growth guidance maintained at 20-25% YoY.

Exhibit 1: Quarterly performance

(Rs mn)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)
Net Interest Income	1,878	2,083	2,213	2,263	2,225	18.5	-1.7
Other Income	664	534	641	540	716	7.8	32.4
Net Income	2,542	2,617	2,854	2,804	2,940	15.7	4.9
Total Operating Expenses	1,150	1,204	1,204	1,339	1,311	14.0	-2.1
<i>As % Of Net Income</i>	<i>45.2</i>	<i>46.0</i>	<i>42.2</i>	<i>47.7</i>	<i>44.6</i>	(65bps)	(315bps)
Employee Expenses	775	806	756	949	820	5.8	-13.6
<i>As % Of Net Income</i>	<i>30.5</i>	<i>30.8</i>	<i>26.5</i>	<i>33.8</i>	<i>27.9</i>	(261bps)	(595bps)
Other Expenses	374	399	447	390	491	31.1	26.0
<i>As % Of Net Income</i>	<i>14.7</i>	<i>15.2</i>	<i>15.7</i>	<i>13.9</i>	<i>16.7</i>	196bps	280bps
Operating Profit	1,392	1,413	1,650	1,465	1,629	17.1	11.2
<i>As % Of Net Income</i>	<i>54.8</i>	<i>54.0</i>	<i>57.8</i>	<i>52.3</i>	<i>55.4</i>	65bps	315bps
Provisions	16	35	64	57	55	243.2	-2.5
PBT	1,376	1,378	1,587	1,408	1,574	14.4	11.7
Total Tax	309	306	318	310	357	15.5	15.1
Reported PAT	1,066	1,071	1,268	1,098	1,217	14.1	10.8
Adjusted PAT	1,066	1,071	1,268	1,098	1,217	14.1	10.8

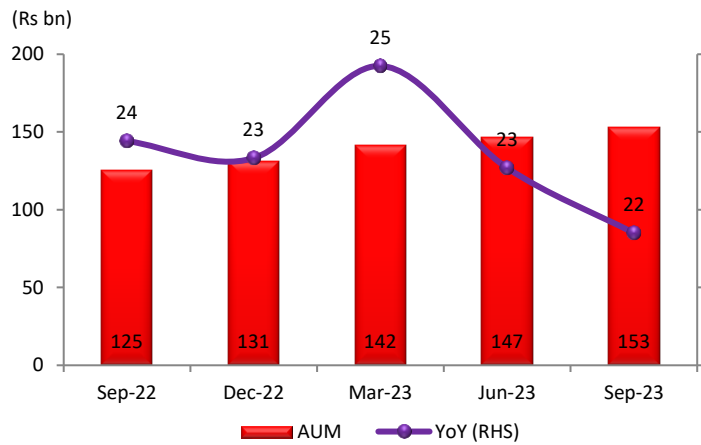
Yield Analysis (%)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)
Yield on AUM	10.8	11.2	11.3	11.5	11.4	61bps	(9bps)
Yield on Advances	13.4	13.9	14.0	14.1	14.0	62bps	(11bps)
Cost of funds	4.6	4.7	4.8	5.2	5.4	82bps	25bps
Cost of borrowing	6.7	6.8	7.0	7.3	7.5	83bps	18bps
NIMs on AUM	6.1	6.5	6.5	6.3	5.9	(21bps)	(35bps)

Asset quality (IndAs)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)
Gross Stage 3	1,113	1,204	1,067	1,193	1,295	16.3	8.5
Net Stage 3	848	917	780	872	939	10.7	7.7
Gross Stage 3 (%)	1.10	1.13	0.92	1.00	1.0	(6bps)	4bps
Net Stage 3 (%)	0.84	0.87	0.68	0.73	0.75	(8bps)	3bps
Net NPAs/Net worth (%)	2.8	2.9	2.4	2.6	2.7	(13bps)	10bps
Provision cover (%)	23.8	23.9	26.9	26.9	27.5	372bps	55bps

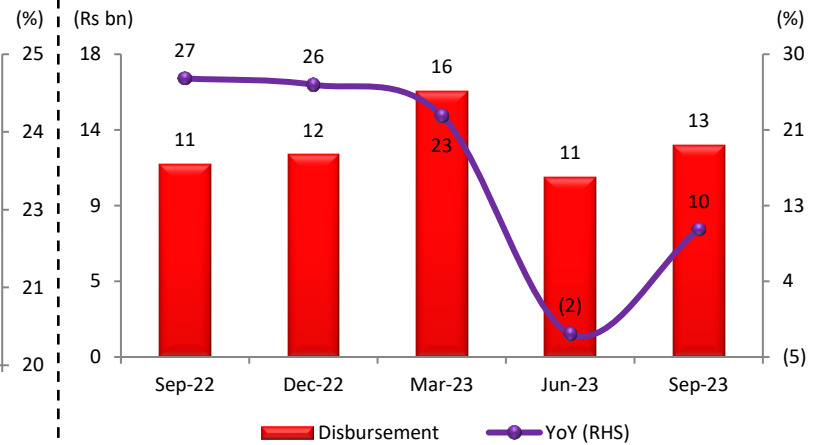
AUM (Rs bn)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)	% of total
Home loan	88,935	91,752	99,025	102,257	106,777	20.1	4.4	70
Mortgage loan	36,502	39,135	42,642	44,243	46,418	27.2	4.9	30
Total	125,437	130,887	141,667	146,500	153,195	22.1	4.6	100

(Rs mn)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24
Borrowing	109,711	116,648	125,209	133,816	140,844
Break up %					
Term loans from Banks/FI	42	42	45	47	50
Securitization/Direct Assignment	23	22	22	21	21
NHB Refinancing	21	22	21	21	18
Debt capital market	15	14	12	11	11

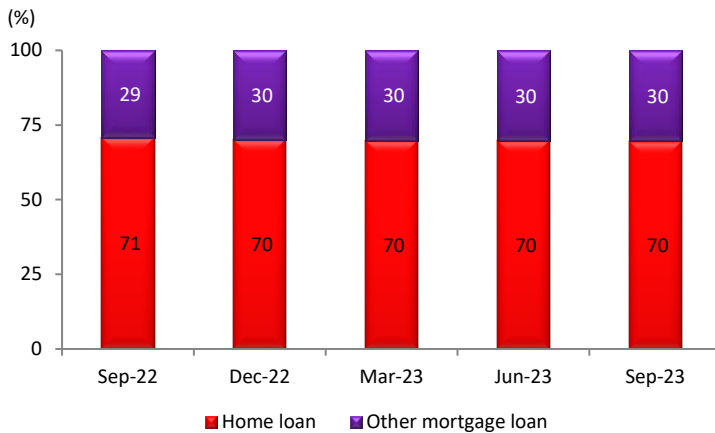
Source: Company, Systematix Institutional Research

Exhibit 2: AUM continue to grow in a range of 20-25%...

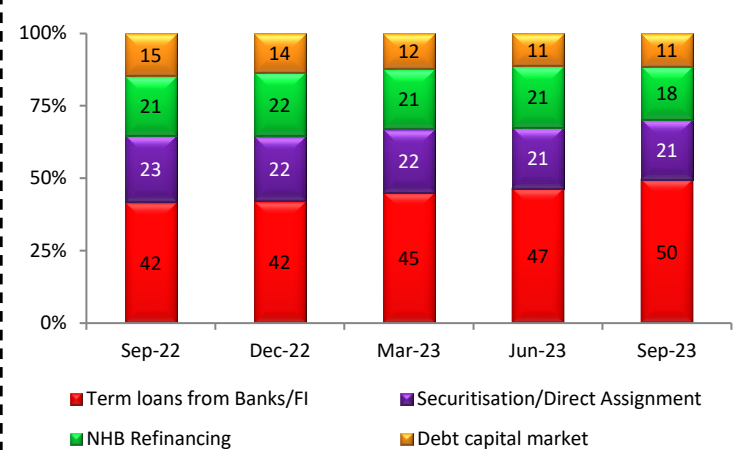
Source: Company, Systematix Institutional Research

Exhibit 3: ... with disbursement picking up in Q2

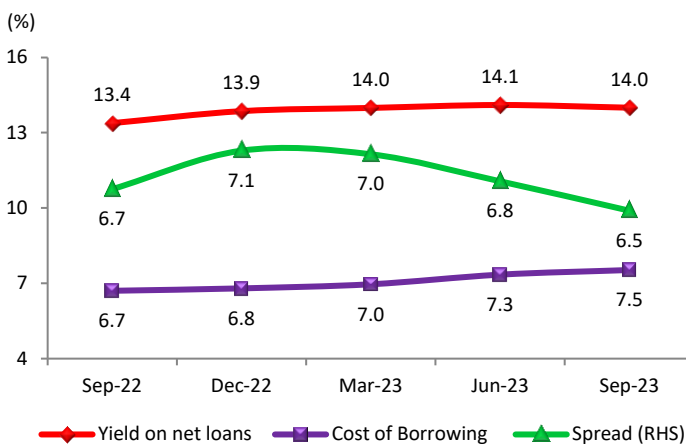
Source: Company, Systematix Institutional Research

Exhibit 4: Share of housing loans steady at ~70%

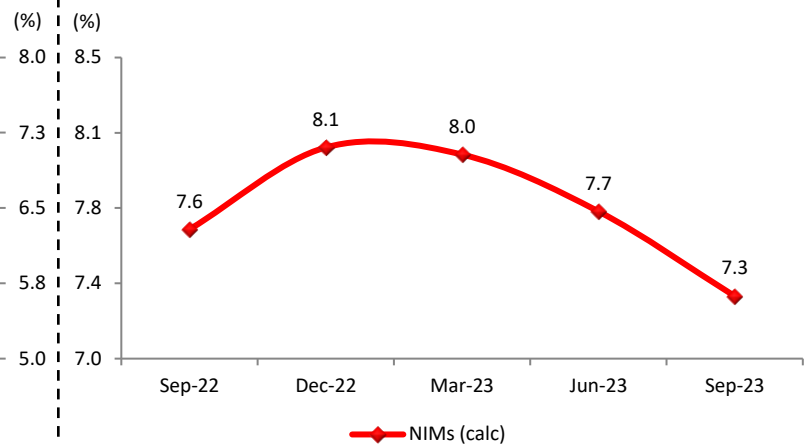
Source: Company, Systematix Institutional Research

Exhibit 5: Borrowing from banks continue to remain a larger share

Source: Company, Systematix Institutional Research

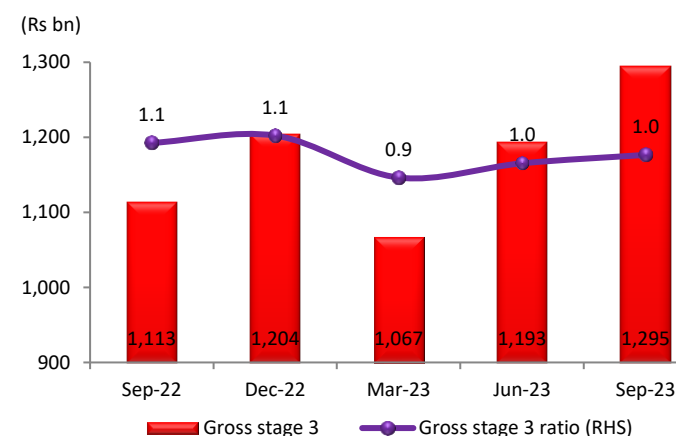
Exhibit 6: Sequentially spreads contracted by ~30bps

Source: Company, Systematix Institutional Research

Exhibit 7: ...similarly NIMs declined by 40bps

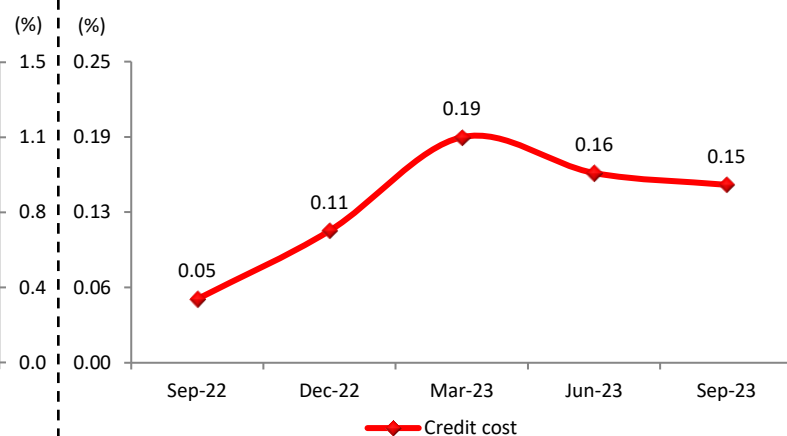
Source: Company, Systematix Institutional Research

Exhibit 8: Asset quality stood steady



Source: Company, Systematix Institutional Research

Exhibit 9: Credit cost broadly in range...



Source: Company, Systematix Institutional Research

Exhibit 10: Change in estimates

(Rs bn)	Old Estimates		New Estimates		% Change	
	FY24	FY25	FY24	FY25	FY24	FY25
NII	9.6	11.7	9.6	11.7	0.0	0.0
Operating Profit	6.8	8.3	6.8	8.3	0.0	0.0
PAT	5.1	6.3	5.1	6.3	0.0	0.0
BV	472	544	472	544	0.0	0.0
EPS	65	80	65	80	0.0	0.0

Source: Company, Systematix Institutional Research

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Profit & Loss Statement

YE: Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Net interest income	5,183	6,514	7,976	9,649	11,749
Other income	1,289	1,768	2,220	2,896	3,677
Net Income	6,473	8,281	10,196	12,545	15,425
Operating expenses	2,576	3,528	4,587	5,748	7,102
Preprovision profit	3,897	4,753	5,608	6,797	8,323
Provisions	371	226	124	239	295
Profit before tax	3,526	4,527	5,484	6,558	8,028
Tax	636	975	1,188	1,420	1,739
Tax rate	18.0	21.5	21.7	21.7	21.7
Reported Profit after tax	2,889	3,552	4,296	5,138	6,290

Source: Company, Systematix Institutional Research

Dupont (as % of Average Assets)

YE: Mar	FY21	FY22	FY23	FY24E	FY25E
Interest Income	11.8	11.3	11.4	11.8	11.9
Interest Expense	5.5	4.8	4.8	5.3	5.4
Net Interest Income	6.2	6.5	6.5	6.5	6.5
Other income total	1.6	1.8	1.8	1.9	2.0
Net Income total	7.8	8.3	8.3	8.4	8.5
Operating expenses total	3.1	3.5	3.8	3.8	3.9
Preprovision profit	4.7	4.8	4.6	4.6	4.6
Provisions	0.4	0.2	0.1	0.2	0.2
Profit before tax and exce. items	4.2	4.5	4.5	4.4	4.4
Profit before tax	4.2	4.5	4.5	4.4	4.4
Tax total	0.8	1.0	1.0	1.0	1.0
Profit after tax	3.5	3.6	3.5	3.4	3.5

Source: Company, Systematix Institutional Research

Growth

YE: Mar (%)	FY21	FY22	FY23	FY24E	FY25E
Net interest income	20.4	25.7	22.5	21.0	21.8
Net Income total	18.3	27.9	23.1	23.0	23.0
Preprovision profit	22.8	22.0	18.0	21.2	22.5
Profit before tax	16.8	28.4	21.1	19.6	22.4
Profit after tax	16.0	22.9	21.0	19.6	22.4
Loan	21.7	20.3	26.8	22.4	19.5
Disbursement	-9.3	35.6	39.5	24.0	20.0
AUM	21.3	20.1	24.8	24.7	22.6

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Equity	785	789	791	791	791
Reserves	23,223	27,275	31,906	36,530	42,191
Net worth	24,008	28,064	32,697	37,320	42,981
Borrowings	63,454	79,725	98,407	1,22,742	1,50,496
Others	2,130	2,386	2,993	4,506	3,998
Total liabilities	89,593	1,10,175	1,34,096	1,64,568	1,97,475
Cash	11,252	15,457	13,928	17,373	21,301
Investments	-	525	1,107	1,381	1,693
Loans	75,233	90,534	1,14,763	1,40,454	1,67,908
Others	2,521	2,975	3,310	4,129	5,063
Total assets	89,593	1,10,175	1,34,096	1,64,568	1,97,475

Source: Company, Systematix Institutional Research

Key Ratios

YE: Mar	FY21	FY22	FY23	FY24E	FY25E
Yield on portfolio	14.3	13.6	13.5	13.8	14.0
cost of borrowings	7.8	6.7	6.6	7.2	7.2
Interest Spread	6.4	6.9	6.9	6.6	6.8
NIM (on AUM)	6.0	6.3	6.3	6.1	6.0
Cost/ Income (%)	39.8	42.6	45.0	45.8	46.0
Credit cost (%)	0.4	0.2	0.1	0.2	0.2
RoA(%)	3.5	3.6	3.5	3.4	3.5
RoE(%)	12.8	13.6	14.1	14.7	15.7
Leverage (x)	3.7	3.8	4.0	4.3	4.5
Tier I (%)	53.3	50.7	46.5	44.6	42.9
CAR (%)	54.5	51.4	46.9	44.9	43.2
Gross NPA (%)	1.0	1.0	0.9	1.0	1.0
Net NPA (%)	0.7	0.8	0.7	0.7	0.7
Provision coverage (%)	27.2	23.1	26.9	26.9	26.9

Source: Company, Systematix Institutional Research

Valuation ratios

YE: Mar	FY21	FY22	FY23	FY24E	FY25E
FDEPS (Rs)	36.5	44.9	54.3	65.0	79.6
PER (x)	42.4	34.5	28.5	23.8	19.5
Book value (Rs)	303.7	355.0	413.6	472.1	543.7
P/BV (Rs)	5.1	4.4	3.7	3.3	2.8
Adjusted book value (Rs)	296.9	346.2	403.7	459.0	528.0
P/ABV (Rs)	5.2	4.5	3.8	3.4	2.9
P/PPP (x)	31.4	25.8	21.8	18.0	14.7
Dividend yield (%)	0.0	0.0	0.0	0.4	0.5

Source: Company, Systematix Institutional Research

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