

Q4FY20 results review  
and earnings revision

## Financials

Target price: Rs1,350

### Earnings revision

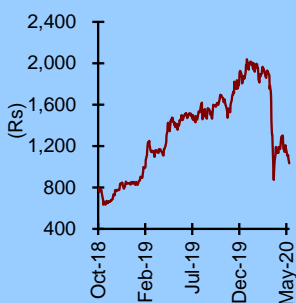
(%)	FY21E	FY22E
NII	↓ 0.7	↑ 1.0
PPoP	↓ 1.4	↑ 0.2
PAT	↓ 0.7	↑ 0.2

### Shareholding pattern

	Sep '19	Dec '19	Mar '20
Promoters	58.3	58.2	53.5
Institutional investors	26.7	33.0	37.1
MFs and others	8.1	5.2	4.5
Banks & FIs	0.0	6.4	6.4
Insurance Cos.	0.5	1.2	1.3
FPI	18.1	20.2	24.9
Others	15.0	8.8	9.4

Source: CMIE

### Price chart



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INDIA



## Aavas Financiers

**BUY**

Maintained

**Rs968**

### Strong outing on asset quality

Aavas Financiers (Aavas) yet again demonstrated why it commands a valuation premium. Important read-through from Q4FY20 results 1) Asset quality witnessed strong improvement with 1+dpd at 2.4%, down ~100bps YoY/QoQ. This could deteriorate in the coming quarters but we expect it to come down to normalized levels by end-FY21. Company made Covid-related provisions of Rs44.4mn (~24bps annualized of average AUM) 2) FY20 PAT at Rs2490mn (I-Sec: Rs2592mn) came in slightly lower because of lower securitization income in Q4FY20 3) NIM (Reported FY20: 8.2%) would continue to remain under pressure but can be offset by improvement in operating cost ratios 4) On liabilities, the company has gone from strength to strength (raised ~Rs11.8bn at 8.1% in Q4FY20) and has healthy liquidity of ~Rs25bn in cash/cash equivalents/undrawn lines. We have an unchanged target price of Rs1,350 (based on 3.9x FY22E P/BV). Reiterate BUY.

- ▶ **Extension of credit-linked subsidy scheme (CLSS) should benefit affordable housing players:** Government has extended the CLSS scheme until Mar'2021 and incentivized demand for affordable housing even in the post-COVID world order. This we see as a positive for the sector specially for sector leaders like Aavas.
- ▶ **Collection efficiencies would have held up well even during Covid times:** Collection efficiencies of Aavas in the month of April would have held up well. We estimate it to be between 60%-70%. This could very well taper off a little in the months of May and June but should not lead to very high provisioning. In-line with our 'HML credit cost framework', we have conservatively modelled credit costs of ~76bps in FY21E.
- ▶ **Asset quality – strong outing:** While reported AUM growth (up ~31% YoY) and disbursements (up ~10% YoY) were largely in line with expectations, Aavas reported strong numbers on asset quality. Importantly, NNPA stood at 0.34% and with this Aavas has improved the PCR from ~19% to ~26%, improvement of 680bps QoQ. Interestingly, other mortgage (including LAP) asset quality (FY20 GNPA: 0.27%) which had deteriorated in the first nine months of the year, improved 26bps QoQ – Aavas could have effected some write-offs here.
- ▶ **Valuations – premium for the quality and predictability in earnings:** We now model NII / PPoP / PAT CAGRs of 21% / 25% / 19% over FY20E-FY22E, respectively. Aavas trades at 2.8x FY22E P/BV. Aavas, we feel, can deliver sustainable RoAs of >3% in the medium term even as we factor in an asset quality deterioration leading to a more than doubling of credit costs. We have an unchanged **target price of Rs1,350**. Maintain **BUY**. Key risks to the thesis: 1. Covid-19 lockdowns can again lead to asset quality deterioration in the LAP book 2. Higher aggression from banks and SFBs in affordable housing space could lead to margin compressions. This can be offset by bringing in operating leverage at play and lowering cost ratios.

Market Cap	Rs76bn/US\$1bn	Year to Mar	FY19	FY20P	FY21E	FY22E
Reuters/Bloomberg	AVAS.BO/AAVAS IN	NII (Rs mn)	4,286	5,131	6,460	7,506
Shares Outstanding (mn)	78.3	Net Income (Rs mn)	1,759	2,490	2,744	3,515
52-week Range (Rs)	2040/875	EPS (fully diluted) (Rs)	22.1	31.3	34.5	44.2
Free Float (%)	46.5	% Chg YoY	76.4	41.5	10.2	28.0
FII (%)	24.9	P/E (x)	43.7	30.9	28.0	21.9
Daily Volume (US\$'000)	2,878	P/BV (x)	4.2	3.7	3.2	2.8
Absolute Return 3m (%)	(48.8)	Net NPA (%)	0.4	0.3	1.1	0.9
Absolute Return 12m (%)	(30.1)	Dividend Yield (%)	0.0	0.0	0.0	0.0
Sensex Return 3m (%)	(24.3)	RoA (%)	3.6	3.7	3.2	3.4
Sensex Return 12m (%)	(15.6)	RoE (%)	11.6	12.7	12.2	13.7

Please refer to important disclosures at the end of this report

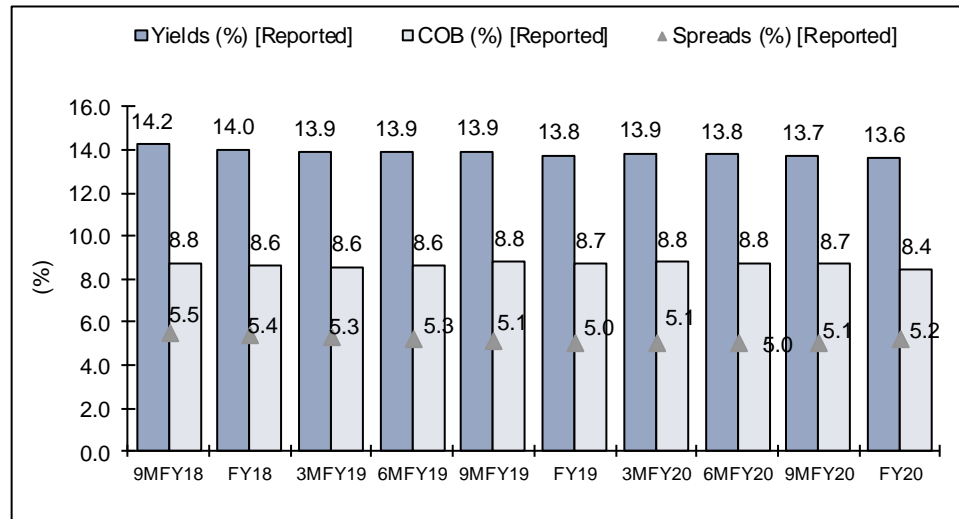
Table 1: Q4FY20 and full year FY20 result review

(Rs mn, year end March 31)

	Q4FY19	Q3FY20	Q4FY20	% YoY	% QoQ	FY20	FY19	% YoY
<b>Income statement</b>								
Interest income	1,965	2,301	2,247	14.4	(2.4)	8,692	6,839	27.1
Interest expenses	723	949	974	34.7	2.6	3,561	2,554	39.4
<b>Net interest income</b>	<b>1,242</b>	<b>1,352</b>	<b>1,273</b>	<b>2.5</b>	<b>(5.8)</b>	<b>5,131</b>	<b>4,286</b>	<b>19.7</b>
Non-interest Income	87	92	104	19.3	12.1	341	270	26.1
<b>Total Income (net of interest expenses)</b>	<b>1,329</b>	<b>1,445</b>	<b>1,377</b>	<b>3.6</b>	<b>(4.7)</b>	<b>5,472</b>	<b>4,556</b>	<b>20.1</b>
Employee expenses	334	389	428	28.3	10.2	1,474	1,172	25.7
Depreciation and amortisation	28	54	56	96.9	3.5	196	97	101.2
Fees and Commission expenses	12	15	1	(91.9)	(93.3)	49	49	(0.4)
Other operating expenses	153	170	168	10.3	(1.1)	581	571	1.7
<b>Total Operating Expense</b>	<b>527</b>	<b>627</b>	<b>653</b>	<b>24.0</b>	<b>4.2</b>	<b>2,300</b>	<b>1,890</b>	<b>21.7</b>
<b>Pre-provisioning profit (PPOP)</b>	<b>802</b>	<b>818</b>	<b>724</b>	<b>(9.8)</b>	<b>(11.5)</b>	<b>3,172</b>	<b>2,666</b>	<b>19.0</b>
Provisions and write offs	34	13	63	84.1	367.4	153	89	72.4
<b>PBT</b>	<b>768</b>	<b>804</b>	<b>661</b>	<b>(13.9)</b>	<b>(17.8)</b>	<b>3,018</b>	<b>2,577</b>	<b>17.1</b>
Tax expenses	225	125	64	(71.7)	(49.1)	529	818	(35.4)
<b>PAT</b>	<b>543</b>	<b>679</b>	<b>597</b>	<b>10.0</b>	<b>(12.1)</b>	<b>2,490</b>	<b>1,759</b>	<b>41.5</b>
<b>EPS (Rs)</b>	<b>7.0</b>	<b>8.7</b>	<b>7.6</b>	<b>9.7</b>	<b>(12.1)</b>	<b>31.7</b>	<b>23.7</b>	<b>34.0</b>
<b>Balance Sheet</b>								
Share capital	781	783	783	0.3	0.0	783	781	0.3
Reserves & surplus	17,589	19,573	20,196	14.8	3.2	20,196	17,589	14.8
<b>Shareholders' funds</b>	<b>18,370</b>	<b>20,356</b>	<b>20,979</b>	<b>14.2</b>	<b>3.1</b>	<b>20,979</b>	<b>18,370</b>	<b>14.2</b>
<b>Borrowings</b>	<b>36,533</b>	<b>45,587</b>	<b>52,524</b>	<b>43.8</b>	<b>15.2</b>	<b>52,524</b>	<b>36,533</b>	<b>43.8</b>
Deferred tax liabilities (net)	428	380	317	(25.9)	(16.6)	317	428	(25.9)
Other Liabilities and provisions	939	2,009	2,761	194.1	37.4	2,761	939	194.1
<b>Total Liabilities and SHE</b>	<b>56,268</b>	<b>68,331</b>	<b>76,580</b>	<b>36.1</b>	<b>12.1</b>	<b>76,580</b>	<b>56,268</b>	<b>36.1</b>
Fixed assets	229	302	319	39.1	5.5	319	229	39.1
<b>Loans</b>	<b>47,245</b>	<b>56,246</b>	<b>61,808</b>	<b>30.8</b>	<b>9.9</b>	<b>61,808</b>	<b>47,245</b>	<b>30.8</b>
Cash & bank balances	6,792	9,204	11,967	76.2	30.0	11,967	6,792	76.2
Investments	45	45	45	0.0	0.0	45	45	0.0
Other Assets	1,958	2,534	2,441	24.7	(3.7)	2,441	1,958	24.7
<b>Total Assets</b>	<b>56,268</b>	<b>68,331</b>	<b>76,580</b>	<b>36.1</b>	<b>12.1</b>	<b>76,580</b>	<b>56,268</b>	<b>36.1</b>
<b>Key ratios</b>								
<b>AUM (Rs mn)</b>	<b>59,416</b>	<b>71,951</b>	<b>77,961</b>	<b>31.2</b>	<b>8.4</b>	<b>77,961</b>	<b>59,416</b>	<b>31.2</b>
-Home Loans (Rs mn)	44,878	53,172	57,301	27.7	7.8	57,301	44,878	27.7
-Other mortgage loans (Rs mn)	14,538	18,779	20,660	42.1	10.0	20,660	14,538	42.1
<b>Disbursements (Rs mn)</b>	<b>8,730</b>	<b>7,531</b>	<b>8,622</b>	<b>-1.2</b>	<b>14.5</b>	<b>29,304</b>	<b>26,724</b>	<b>9.7</b>
Yields (%) [Reported-YTD]	13.8	13.7	13.6	-12 bps	-11 bps	13.6	13.8	-12 bps
Borrowing costs (%) [Reported-YTD]	8.7	8.7	8.4	-31 bps	-24 bps	8.4	8.7	-31 bps
Spreads (%)	5.0	5.1	5.2	18 bps	13 bps	5.2	5.0	18 bps
<b>NIM (%) [Reported-YTD]</b>	<b>9.3</b>	<b>8.7</b>	<b>8.2</b>	<b>-116 bps</b>	<b>-50 bps</b>	<b>8.2</b>	<b>9.3</b>	<b>-116 bps</b>
<b>Op cost as % of avg assets</b>	<b>3.9</b>	<b>3.8</b>	<b>3.6</b>	<b>-35 bps</b>	<b>-18 bps</b>	<b>3.5</b>	<b>3.9</b>	<b>-45 bps</b>
Cost to income (%)	39.6	43.4	47.4	779 bps	404 bps	42.0	41.5	54 bps
1+ dpd (%)	3.4	3.4	2.4	-97 bps	-96 bps	2.4	3.4	-97 bps
<b>GNPL (% of on-book loans)</b>	<b>0.47</b>	<b>0.57</b>	<b>0.46</b>	<b>-1 bps</b>	<b>-11 bps</b>	<b>0.46</b>	<b>0.47</b>	<b>-1 bps</b>
<b>NNPL (% of on-book loans)</b>	<b>0.37</b>	<b>0.46</b>	<b>0.34</b>	<b>-3 bps</b>	<b>-12 bps</b>	<b>0.34</b>	<b>0.37</b>	<b>-3 bps</b>
<b>Provision coverage ratio (%)</b>	<b>21.3</b>	<b>19.3</b>	<b>26.1</b>	<b>481 bps</b>	<b>678 bps</b>	<b>26.1</b>	<b>21.3</b>	<b>481 bps</b>
Credit cost as a % of avg AUM [annualised]	0.24	0.08	0.33	9 bps	25 bps	0.28	0.22	6 bps

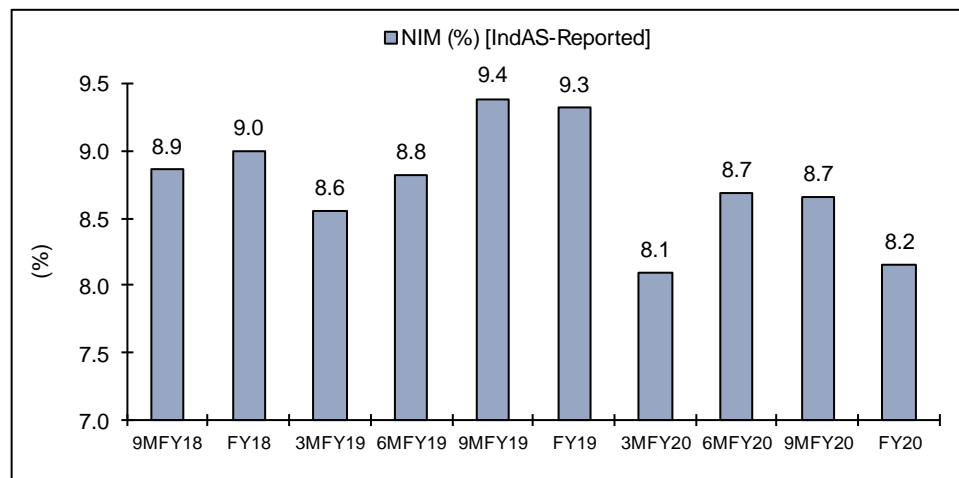
Source: Company data, I-Sec research

**Chart 1: Spreads have been maintained above 5%**



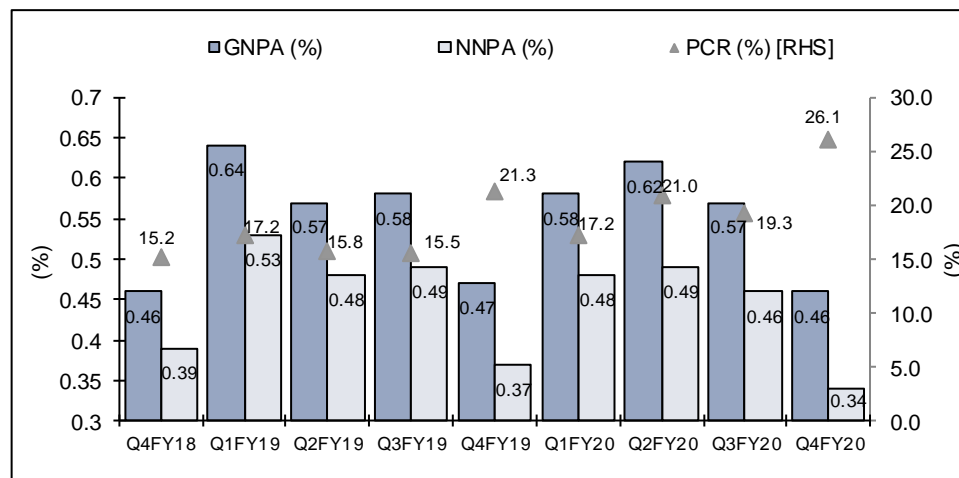
Source: Company data, I-Sec research

**Chart 2: Reported NIM at 8.2% deteriorated ~110bps YoY and we expect pressure on NIM in FY21 as well**



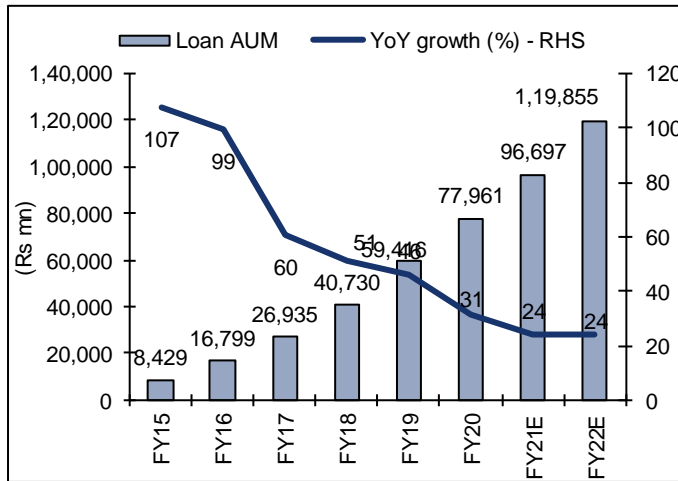
Source: Company data, I-Sec research

**Chart 3: Asset quality has remained benign with GNPA at 0.46%**



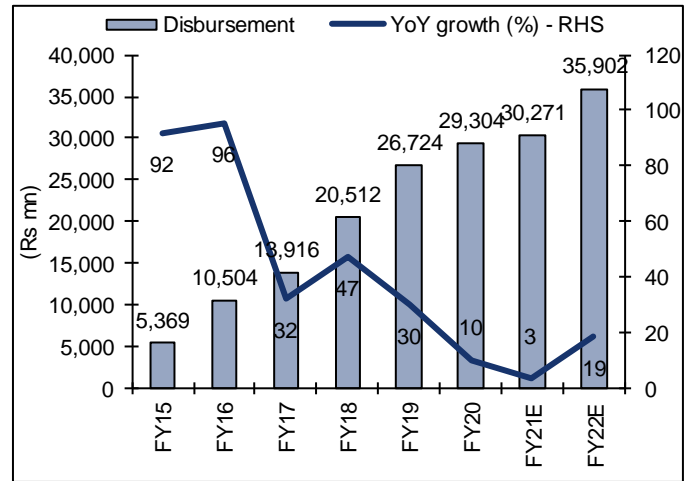
Source: Company data, I-Sec research

**Chart 4: Estimate AUM CAGR of 24% between FY20-FY22E...**



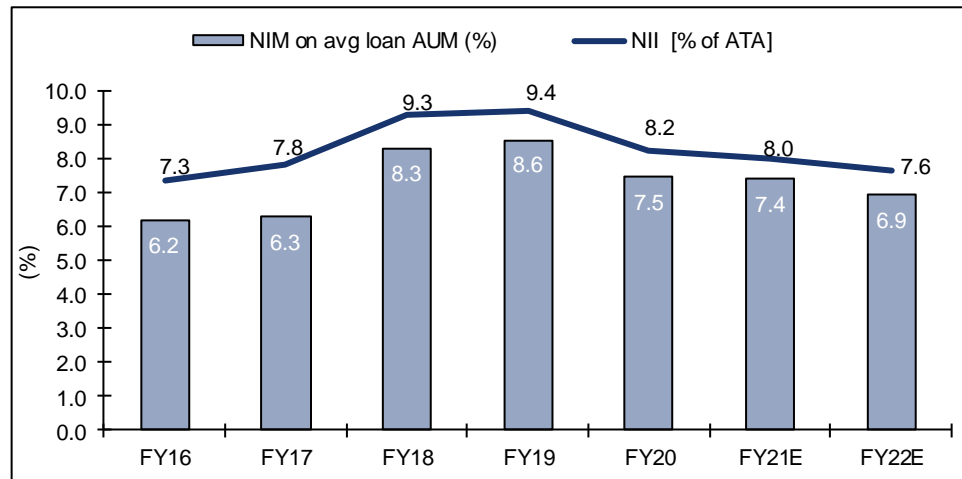
Source: Company data, I-SEC research

**Chart 5: ...and disbursement CAGR of 11% during the same period**



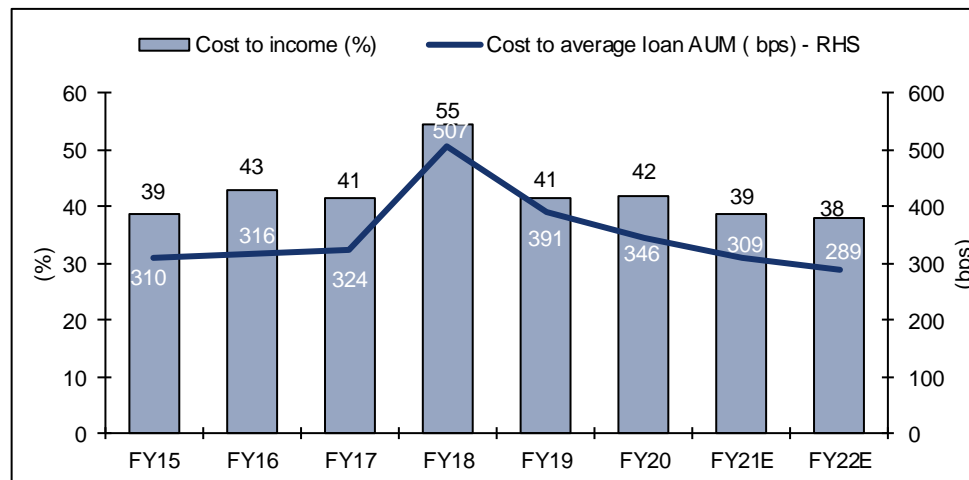
Source: Company data, I-SEC research

**Chart 6: Expect NIMs to remain under pressure in FY21E and FY22E**



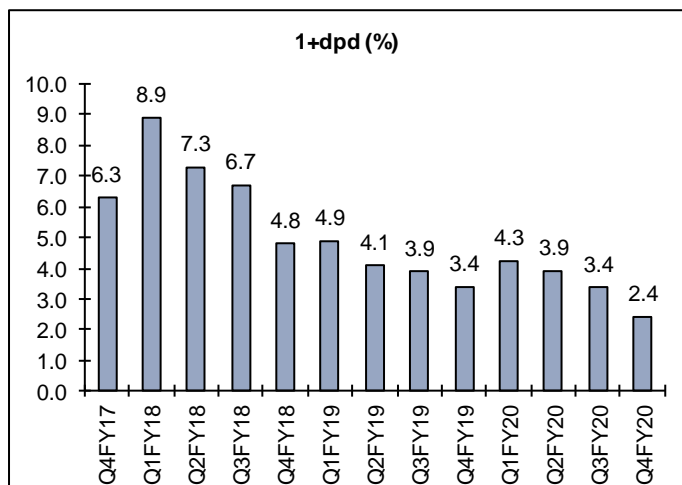
Source: Company data, I-Sec research

**Chart 7: With operating leverage kicking in, expect improvement in cost ratios**



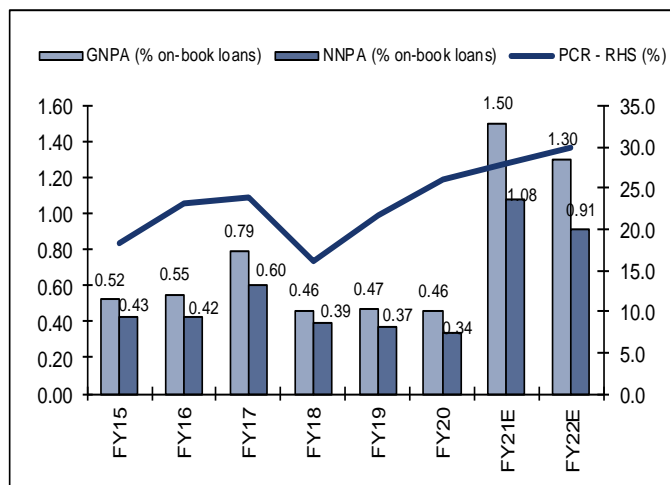
Source: Company data, I-Sec research

**Chart 8: 1+dpd was at historical best of 2.4%**



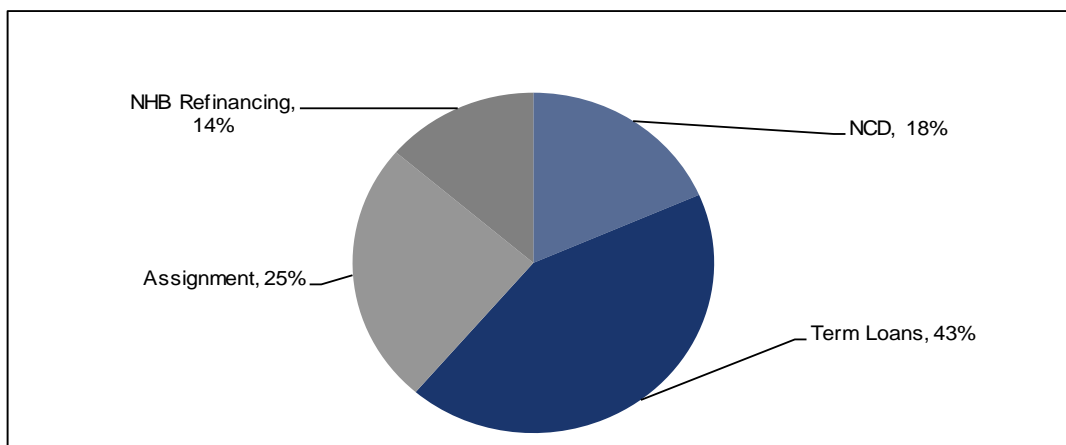
Source: Company data, I-SEC research

**Chart 9: Conservatively built in asset quality deterioration and higher credit costs in FY21E**



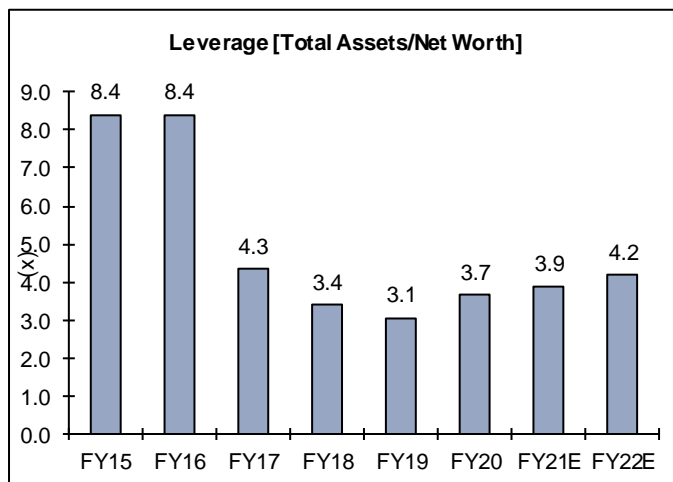
Source: Company data, I-SEC research

**Chart 10: Proportion of NCDs in the borrowing mix improved**



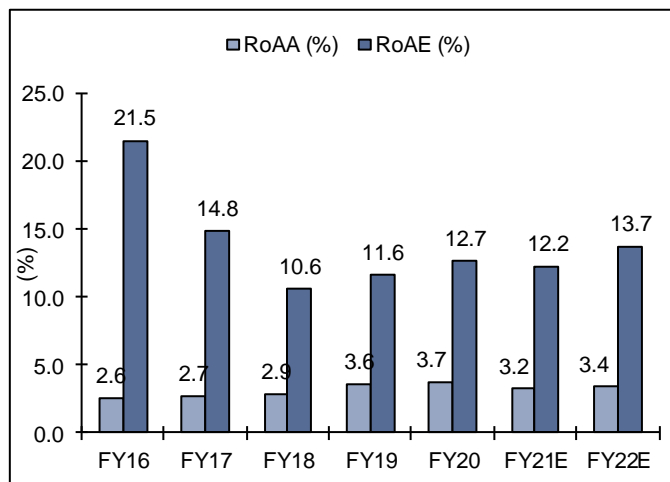
Source: Company data, I-Sec research

**Chart 11: Leverage will build up in due course...**



Source: Company data, I-SEC research

**Chart 12: ...with moderating RoA & improving RoE**



Source: Company data, I-SEC research

## Financial summary

**Table 2: Profit and loss statement**

(Rs mn, year ending Mar 31)

	FY18	FY19	FY20P	FY21E	FY22E
Interest Income	4,743	6,839	8,692	11,336	13,625
Interest Expenses	1,931	2,554	3,561	4,875	6,119
<b>Net Interest Income (NII)</b>	<b>2,812</b>	<b>4,286</b>	<b>5,131</b>	<b>6,460</b>	<b>7,506</b>
Non-Interest Income	201	270	341	311	404
<b>Total Income (net of interest expenses)</b>	<b>3,014</b>	<b>4,556</b>	<b>5,472</b>	<b>6,771</b>	<b>7,909</b>
Employee benefit expenses	1,115	1,172	1,474	1,518	1,640
Depreciation and amortisation	56	97	196	235	305
Other operating expenses	473	621	630	857	1,048
<b>Total Operating Expense</b>	<b>1,645</b>	<b>1,890</b>	<b>2,300</b>	<b>2,610</b>	<b>2,993</b>
<b>Pre Provisioning Profits (PPoP)</b>	<b>1,369</b>	<b>2,666</b>	<b>3,172</b>	<b>4,162</b>	<b>4,916</b>
Provisions and write offs	26	89	153	666	438
<b>Profit before tax (PBT)</b>	<b>1,343</b>	<b>2,577</b>	<b>3,018</b>	<b>3,496</b>	<b>4,478</b>
Total tax expenses	412	818	529	752	963
<b>Profit after tax (PAT)</b>	<b>931</b>	<b>1,759</b>	<b>2,490</b>	<b>2,744</b>	<b>3,515</b>

Source: Company data, I-Sec research

Note: FY18 onwards numbers are as per Ind-AS

**Table 3: Balance sheet**

(Rs mn, year ending Mar 31)

	FY18	FY19	FY20P	FY21E	FY22E
Share capital	692	781	783	790	794
Reserves & surplus	11,207	17,589	20,196	23,037	26,649
<b>Shareholders' funds</b>	<b>11,899</b>	<b>18,370</b>	<b>20,979</b>	<b>23,826</b>	<b>27,443</b>
Borrowings	27,376	36,533	52,524	64,957	82,496
Provisions	32	44	83	99	119
Deferred tax liabilities (net)	114	427	317	336	353
Other Liabilities	981	894	2,678	3,268	4,050
<b>Total Liabilities and SHE</b>	<b>40,401</b>	<b>56,268</b>	<b>76,580</b>	<b>92,486</b>	<b>1,14,460</b>
Fixed assets	185	229	319	351	421
<b>Loans</b>	<b>33,334</b>	<b>47,245</b>	<b>61,808</b>	<b>75,424</b>	<b>93,487</b>
Cash & bank balances	5,650	6,791	11,967	13,000	15,000
Investments	45	45	45	50	59
Other Assets	1,188	1,958	2,441	3,662	5,493
<b>Total Assets</b>	<b>40,401</b>	<b>56,268</b>	<b>76,580</b>	<b>92,486</b>	<b>1,14,460</b>

Source: Company data, I-Sec research

Note: FY18 onward numbers are as per Ind-AS

**Table 4: Key metrics***(Year ending Mar 31)*

	FY18	FY19	FY20P	FY21E	FY22E
<b>AUM and Disbursements (in Rs mn)</b>					
AUM	40,730	59,416	77,961	96,697	1,19,855
On-book Loans	33,334	47,245	61,808	75,424	93,487
Off-book Loans	7,396	12,171	16,153	21,273	26,368
Disbursements	20,512	26,724	29,304	30,271	35,902
<b>Growth (%):</b>					
AUM	51.2	45.9	31.2	24.0	23.9
Disbursements	47.4	30.3	9.7	3.3	18.6
Loan book (on balance sheet)	56.3	41.7	30.8	22.0	23.9
Total Assets	64.9	39.3	36.1	20.8	23.8
Interest Income	69.2	44.2	27.1	30.4	20.2
Interest Expenses	35.2	32.3	39.4	36.9	25.5
Net Interest Income (NII)	104.5	52.4	19.7	25.9	16.2
Non-interest income	-19.9	34.3	26.1	-8.7	29.8
Total Income (net of interest expenses)	85.3	51.2	20.1	23.8	16.8
Total Non-Interest Expenses	144.2	14.9	21.7	13.5	14.7
Pre provisioning operating profits (PPoP)	43.6	94.7	19.0	31.2	18.1
PAT	62.9	89.0	41.5	10.2	28.1
EPS	43.2	48.7	34.0	9.6	27.4
<b>Yields, interest costs and spreads (%)</b>					
NIM on avg. loan AUM	8.3	8.6	7.5	7.4	6.9
NIM on ATA	9.3	9.4	8.2	8.0	7.6
Yield on interest-earning assets	12.5	12.1	11.1	11.4	11.1
Yield on on-book loans	14.4	14.7	14.4	14.2	13.8
Average cost of funds	8.5	8.0	8.0	8.3	8.3
Interest Spread on loan assets [on-book]	5.8	6.7	6.4	5.9	5.5
<b>Operating efficiencies</b>					
Non-interest income as % of Total income	6.7	5.9	6.2	4.6	5.1
Cost to income ratio (%)	54.6	41.5	42.0	38.5	37.8
Op. costs/avg AUM (%)	4.9	3.8	3.3	3.0	2.8
No of employees	1,862	2,384	2,734	3,084	3,434
Average annual salary (Rs '000)	599	492	539	492	478
Salaries as % of non-int. costs (%)	67.8	62.0	64.1	58.2	54.8
AUM/employee(Rs mn)	22	25	29	31	35
AUM/asset branch(Rs mn)	247	283	312	345	400
<b>Capital Structure</b>					
Debt-Equity ratio	2.3	2.0	2.5	2.7	3.0
Leverage [AUM/Net Worth] (x)	3.4	3.2	3.7	4.1	4.4
Leverage [Assets/Net Worth] (x)	3.4	3.1	3.7	3.9	4.2
Tier 1 CAR (%)	55.9	65.4	53.9	48.6	43.8
Tier 2 CAR (%)	5.6	3.1	2.2	2.2	2.2
CAR (%)	61.6	68.5	56.0	50.8	46.0
Tier I Capital	10,955	18,370	20,979	23,826	27,443
Tier II Capital	1,099	871	849	1,079	1,378
Total RWA	19,582	28,111	38,939	49,026	62,636
<b>Asset quality and provisioning</b>					
GNPL (Rs mn)	155	223	284	1,131	1,215
GNPL (%)	0.46	0.47	0.46	1.50	1.30
NNPL (Rs mn)	130	174	210	815	851
NNPL (%)	0.39	0.37	0.34	1.08	0.91
Coverage ratio (%)	16.0	21.8	26.0	28.0	30.0
Credit costs as % of average AUM (bps)	8	18	22	76	40
<b>Return ratios</b>					
RoAAUM (%)	2.8	3.5	3.6	3.1	3.2
RoA (%)	2.9	3.6	3.7	3.2	3.4
RoAE (%)	10.6	11.6	12.7	12.2	13.7
Payout ratio (%)	0.0	0.0	0.0	0.0	0.0

	FY18	FY19	FY20P	FY21E	FY22E
<b>Valuation Ratios</b>					
No. of shares (mn)	70.0	78.1	78.5	79.0	79.4
No. of shares - fully diluted (mn)	74.2	79.5	79.5	79.5	79.5
ESOPs outstanding	4.2	1.4	0.9	0.5	0.2
EPS (Rs)	13.3	22.5	31.7	34.8	44.3
EPS fully diluted (Rs)	12.5	22.1	31.3	34.5	44.2
Price to Earnings (x)	72.7	43.0	30.5	27.9	21.9
Price to Earnings (fully diluted) (Rs)	77.1	43.7	30.9	28.0	21.9
BVPS (fully diluted) (Rs)	160.4	231.2	264.0	299.8	345.0
Adjusted BVPS (fully diluted) (Rs)	159.1	229.5	262.1	292.3	337.1
Price to Book (x)	6.0	4.2	3.7	3.2	2.8
Price to Adjusted Book (x)	6.1	4.2	3.7	3.3	2.9
DPS	0.0	0.0	0.0	0.0	0.0
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0

Source: Company data, I-Sec research

**Table 5: DuPont analysis (on average assets)***(Rs mn, year ending Mar 31)*

	FY18	FY19	FY20P	FY21E	FY22E
Interest earned	14.6	14.2	13.1	13.4	13.2
Interest expended	5.9	5.3	5.4	5.8	5.9
<b>Gross Interest Spread</b>	8.7	8.9	7.7	7.6	7.3
Credit cost	0.1	0.2	0.2	0.8	0.4
<b>Net Interest Spread</b>	8.6	8.7	7.5	6.9	6.8
Operating cost	5.1	3.9	3.5	3.1	2.9
<b>Lending spread</b>	3.5	4.8	4.0	3.8	3.9
Non-interest income	0.6	0.6	0.5	0.4	0.4
<b>Final Spread</b>	4.1	5.3	4.5	4.1	4.3
<i>Tax rate (%)</i>	30.7	31.7	17.5	21.5	21.5
<b>RoA</b>	2.9	3.6	3.7	3.2	3.4
Effective leverage (AA/ AE)	3.7	3.2	3.4	3.8	4.0
<b>RoAE</b>	10.6	11.6	12.7	12.2	13.7

Source: Company data, I-Sec research



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