FIRST LIGHT

08 April 2021

RESEARCH

[Initiation] AU Small Finance Bank | Target: Rs 1,500 | +22% | BUY

A budding, high-quality franchise – initiate with BUY

BOB Economics Research | Monetary Policy Review

Growth remains centre point of monetary policy

Banking

Rising demand for used CV financing

SUMMARY

AU Small Finance Bank

We expect AU Small Finance Bank's (AUBANK) longstanding expertise in vehicle finance and successful extension into secured business loans to aid a 22% loan CAGR over FY20-FY23. The bank's provisioning buffer is healthy at 2% of AUM and collections of >100% suggest ebbing Covid headwinds, even as liabilities are tilting toward low-cost funds. We value the bank at 5.3x FY23E P/BV given its asset quality record, strong growth visibility and potential universal bank transition post FY22 – initiate with BUY, Mar'22 TP Rs 1,500.

Click here for the full report.

India Economics: Monetary Policy Review

MPC kept repo rate on hold but removed time specific stance guidance in favour of one contingent on reviving growth. RBI also announced Rs 1tn of asset purchase in Q1 (Rs 3.13tn in FY21). Growth forecast for FY22 was maintained at 10.5%. At the same time, inflation in FY22/ FY23 is projected at 5%/ 4.7%. With inflation estimated to remain above RBI's target of 4%, we believe RBI is likely to normalise monetary policy first by reducing rate corridor between repo and reverse repo rate in H2FY22 and second by raising repo rate in FY23.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	1,000
TCS	Buy	3,710
Tech Mahindra	Buy	1,130

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	3,750
Greenply Industries	Buy	195
Laurus Labs	Buy	480
Transport Corp	Buy	330

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.66	(4bps)	9bps	94bps
India 10Y yield (%)	6.12	0bps	(11bps)	(29bps)
USD/INR	73.42	(0.2)	(0.5)	2.9
Brent Crude (US$/bbl)	62.74	0.9	(9.5)	96.9
Dow	33,430	(0.3)	6.1	47.6
Shanghai	3,483	0	(0.5)	23.5
Sensex	49,201	0.1	(2.4)	63.6
India FII (US$ mn)	**5 Apr**	**MTD**	**CYTD**	**FYTD**
FII-D	(195.7)	(195.7)	(2,222.9)	(195.7)
FII-E	(89.9)	(89.9)	7,236.5	(89.9)

Source: Bank of Baroda Economics Research

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Banking

We recently interacted with industry players for a perspective on economic activity revival and potential fallout from the renewed lockdown in Maharashtra. Key takeaways: (1) Economic activity improving gradually, (2) Fleet utilisation back at pre-Covid levels, (3) Demand for used CVs gaining traction, (4) Taxis, school and private staff buses still under stress.

Click here for the full report.

BUY
TP: Rs 1,500 | ⮝ 22%

AU SMALL FINANCE BANK | Banking | 07 April 2021

A budding, high-quality franchise – initiate with BUY

We expect AU Small Finance Bank's (AUBANK) longstanding expertise in vehicle finance and successful extension into secured business loans to aid a 22% loan CAGR over FY20-FY23. The bank's provisioning buffer is healthy at 2% of AUM and collections of >100% suggest ebbing Covid headwinds, even as liabilities are tilting toward low-cost funds. We value the bank at 5.3x FY23E P/BV given its asset quality record, strong growth visibility and potential universal bank transition post FY22 – initiate with BUY, Mar'22 TP Rs 1,500.

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Asset quality indicators improving: We believe AUBANK's GNPAs have peaked and slippages should normalise hereon as collections have crossed 100% and the loan book paying full dues has touched pre-Covid levels of 84% in Dec'20. Further, our channel checks indicate that demand in the CV segment – a meaningful business for the bank – is gradually picking up. We model for credit cost of ~1% in FY22-FY23.

Liabilities scaling up well: Upon conversion from an NBFC to a bank in FY18, AUBANK has successfully transitioned to deposits as its primary source of funding and these now form ~64% of the balance sheet. A higher-yield asset portfolio enables attractive interest rates to customers and has boosted the share of retail deposits to 55% vs. 43% in FY20, indicating improved granularity.

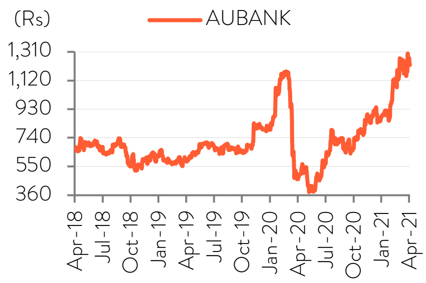
Core retail expertise to fuel growth: We expect a 22% CAGR in AUBANK's loan book over FY20-FY23 fuelled by the retail segment, especially vehicle finance and secured business loans. The recent ~Rs 6bn capital raise will support growth and also signals management's aspirations to become a universal bank.

Initiate with BUY: The stock is trading at 5.2x FY22E BV, ~10% premium to its 4Y average. Our Mar'22 TP of Rs 1,500 is set at 5.3x FY23E P/BV.

Ticker/Price	AUBANK IN/Rs 1,233
Market cap	US$ 5.1bn
Shares o/s	307mn
3M ADV	US$ 16.3mn
52wk high/low	Rs 1,354/Rs 366
Promoter/FPI/DII	29%/33%/38%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Net interest income	13,425	19,089	23,656	29,425	37,221
NII growth (%)	42.7	42.2	23.9	24.4	26.5
Adj. net profit (Rs mn)	3,818	6,748	12,489	11,811	16,059
EPS (Rs)	13.2	22.6	40.5	37.8	51.5
P/E (x)	93.3	54.5	30.4	32.6	24.0
P/BV (x)	12.2	8.7	6.2	5.3	4.4
ROA (%)	1.5	1.8	2.7	2.1	2.3
ROE (%)	14.7	18.6	23.7	17.5	19.9

Source: Company, BOBCAPS Research

बैंक ऑफ़ बड़ौदा
Bank of Baroda

MONETARY POLICY REVIEW

07 April 2021

Growth remains centre point of monetary policy

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MPC kept repo rate on hold but removed time specific stance guidance in favour of one contingent on reviving growth. RBI also announced Rs 1tn of asset purchase in Q1 (Rs 3.13tn in FY21). Growth forecast for FY22 was maintained at 10.5%. At the same time, inflation in FY22/ FY23 is projected at 5%/ 4.7%. With inflation estimated to remain above RBI's target of 4%, we believe RBI is likely to normalise monetary policy first by reducing rate corridor between repo and reverse repo rate in H2FY22 and second by raising repo rate in FY23.

KEY HIGHLIGHTS

- Policy rate kept unchanged at 4%, accommodative stance to continue.
- CPI forecast for FY22 and FY23 at 5% and 4.7% respectively.
- GDP forecast for FY22 retained at 10.5%. In FY23, GDP to grow by 6.8%.

Status quo: MPC members voted to keep repo rate on hold. While accommodative stance has been retained, it is contingent on growth revival and mitigating the impact of the pandemic. Time based guidance has been removed.

GDP growth forecast retained in FY22: RBI retained its growth forecast for FY22 at 10.5%. However, second Covid-19 wave has brought uncertainty. While GDP growth for Q1 and Q2 has been retained at 26.2% and 8.3% respectively, for Q3 growth has been revised lower to 5.4%. In FY23, RBI expects GDP growth at 6.8%.

CPI forecasts remain above MPC's target: RBI has revised its CPI projection downward to 5% in Q4FY21 from 5.2% earlier. While inflation projection for Q1FY22 has been retained at 5.2%, for Q2 and Q3 it has been revised upward to 5.2% (5% earlier) and 4.4% (4.3% earlier) respectively. While inflation is estimated to drop from 6.2% in FY21 to 5% in FY22 and 4.7% in FY23, in all three years it will remain above RBI's target of 4%. Thus today's policy opens up room for normalisation contingent upon growth outlook.

Liquidity support and normalisation: While announcing withdrawal of time based guidance, RBI has announced liquidity support for long-end bonds by introducing G-Sec Acquisition Program (GSAP), an asset purchase program of Rs 1tn in Q1FY22. The first purchase under this window will be Rs 250bn on 15 April 2021. Notably, RBI did net purchases of Rs 3.13tn in FY21. With this, RBI has been able to strike a balance between liquidity guidance and opening up room for normalisation of monetary policy. RBI's inflation target is 4%. As a first step to normalisation, we believe RBI will reduce the corridor between repo and reverse repo rate in H2FY22 before raising repo rate in FY23.

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

BANKING

07 April 2021

Rising demand for used CV financing

Vikesh Mehta
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We recently interacted with industry players for a perspective on economic activity revival and potential fallout from the renewed lockdown in Maharashtra. Key takeaways:

Economic activity improving gradually: Our checks suggest that freight operator business has been picking up MoM. Consumption cargo remained flat in Q4FY21 as Q3 saw festive demand, but bulk cargo has picked up QoQ. Operators fear that the current lockdown in Maharashtra will affect last-mile delivery due to timing restrictions, though movement of goods originating from the state would be only marginally affected. Also, the adverse impact on business may not be as severe as the first lockdown initiated in Mar'20.

Fleet utilisation back at pre-Covid levels: Average fleet utilisation in Q4FY21 has reached the pre-Covid levels seen during Jan-Feb'20, as per one of the largest truck load companies in the country. The industry has taken a freight rate hike of ~20% in Q3 and 4-5% in Q4, thereby preserving margins in the face of higher fuel prices. However, operators' working capital is wearing thin due to delayed customer payments.

Demand for used CVs gaining traction: CV demand has been gradually improving, especially for used CVs, given the improvement in fleet utilisation and rise in economic activity. However, apprehensions over extension of the lockdown to other states amid a second wave of the pandemic have instilled a degree of uncertainty among vehicle buyers.

Taxis, school and private staff buses still under stress: Small fleet operators are facing a liquidity crunch but are collaborating with larger players to bring their fleet into use. However, if movement restrictions impede business activity in Q1 and Q2FY22, these operators could come under significant pressure. Lenders are currently taking a softer approach towards repossessing vehicles on profitable truck routes and are extending support if they find operator cash flows improving. Segments such as taxis, school and private staff buses continue to reel under stress as they await reopening of offices and schools.

Our view: Large banks are best placed in the current environment as they are well provisioned and adequately capitalised. **ICICI Bank** (TP: Rs 675, BUY), **HDFC Bank** (TP: Rs 1,800, BUY), and **State Bank of India** (TP: Rs 475, BUY) remain our top picks in the sector.

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BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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