

AU Small Finance Bank
(formerly known as AU Financiers (India) Ltd)

November 09, 2018

Ratings

Facilities	Amount (Rs. crore)	Rating ¹	Rating Action
Certificate of Deposit (CD)	500 (Rs. Five Hundred Crore only)	CARE A1+ (Care A One Plus)	Assigned

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to debt instruments of AU Small Finance Bank's (AUSFB) continues to factor in growth momentum post conversion into Small Finance Bank in April, 2017 and ability to mobilize considerable amount of deposits in a short span of time. The rating also takes into account the improvement in financial flexibility of the company post its listing of its equity shares on stock exchanges in July, 2017 and grant of status of schedule commercial bank in November, 2017. The rating continues to factor in experienced management team, presence of strong institutional investors, comfortable capitalization levels, comfortable liquidity profile, good resource profile, moderate profitability parameters and average asset quality.

The ratings are constrained by AUSFB's low seasoning of the non-vehicle finance portfolio and regional concentration. Growing scale of operations while maintaining asset quality & profitability, diversification of the liability profile and maintaining capital adequacy are key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Transition to small finance bank (SFB) and status of a scheduled commercial bank

The company commenced operations as SFB from April 2017 and has completed more than two years of operation. During this period of operations, the company has been able to ramp up its operations. As on September 30, 2018, AUSFB has geographical distribution across 11 states and a UT with 395 branches (new & converted) (March 31, 2018: 377 branches), 88 asset centers, 16 business correspondent agents, 12,109 employees, 16 offices, and 292 ATMs. It has also been able to mobilize deposits to the extent of Rs.12,869 crore as on September 30, 2018. The company continued its growth momentum after the transition period with asset size increasing from Rs.20,942 crore as on March 31, 2018 to Rs.24,780 crore as on September 30, 2018 (growth – 18%). The bank also got the status of a scheduled commercial bank from RBI from November 1, 2017 which has increased the financial flexibility of the bank.

Experienced management

AU SFB is professionally managed under the overall guidance of the bank's Board of Directors (BoD) which includes individuals with wide experience in the financial services. The BoD of the bank is headed by Mr. M Venugopalan (Independent Non-Executive Chairman) who has over 48 years of experience in the banking industry and was associated with Bank of India as Chairman and Managing Director and was also designated CEO & MD of Federal Bank in May 2005 and has served as Executive Director of Union Bank of India.

The operations of the bank are led Mr. Sanjay Agarwal (Promoter & Managing Director), a Chartered Accountant by qualification with over 2 decades of experience in the fields of finance and credit. He is assisted by senior management team members who are experienced in their respective fields.

Presence of strong institutional investors

The company has presence of strong institutional investors like Warburg Pincus, International Finance Corporation, Ouera Holdings, Chrys Capital and Motilal Oswal PE etc. As on September 30, 2018, the domestic to foreign shareholding stood in the ratio of 62:28 with promoters owning 31.3% equity stake in the company. During H1FY19 (refers to period April 01 to September 30), Temasek Holdings acquired 4.80% in the bank through its wholly owned investment arm – Camas Investments Pte. Ltd.

Comfortable capitalization

AUSFB has been reporting comfortable capital adequacy over the last two years. The bank has proposed capital infusion of Rs.1,000 crore from Temasek Holdings (through its indirectly wholly owned subsidiary Camas Investments Pte Ltd.) out of which Rs.300 crore as equity capital and Rs.175 crore by way of convertible warrants was infused into the bank during H1FY19. The balance Rs.525 crore would be infused over a period of 18 months (i.e. up to December 31, 2019) which will help the bank maintain comfortable capitalization levels while scaling up its operations.

²Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.

AUSFB reported Capital Adequacy Ratio (CAR) of 17.80% (Tier I CAR: 17.20%) as on September 30, 2018 (against minimum regulatory requirement of 15%) [March 31, 2018: CAR of 19.30% (Tier I CAR: 18.40%)].

Good resource profile

Post conversion into SFB, AUSFB has been able to raise low cost deposits as compared to earlier reliance on only borrowings by way of bank facilities and market borrowings. This will reduce its cost of borrowing and further diversify its resource profile. As on September 30, 2018, the bank's funding profile constituted deposits (62.2%), refinance from FIs (23.2%), Non-Convertible Debentures (NCD) (9.6%), borrowing through CBLO/LC/Others (2.2%) and loans from Banks & NBFC (1.7%). The bank's Current Accounts Savings Account (CASA) deposits as proportion of total deposits was 26% as on September 30, 2018 (March 31, 2018: 32%).

Comfortable liquidity profile

The bank has negative cumulative mismatches up to one year time bucket as on September 30, 2018 on account of deposit maturity. However, the mismatches were within the limits set by the board. The peak mismatch up to 6 months stood at Rs.1,267 crore. As on September 30, 2018, it has SLR investment of Rs.3,308 crore as against regulatory requirement of Rs.2,932 crore and Non SLR investment of Rs.1,597 crore. The liquidity coverage ratio was 95.2% as against regulatory requirement of 70% for SFBs as on September 30, 2018.

Financial performance

Post conversion to SFB and access to deposits, the cost of funds has declined over the last two years for AUSFB. However, with diversification in lending book, the yields have seen marginal reduction. The Net Interest Margin (NIM) for FY18 stood at 5.31% as compared to 7.89% for FY17. During FY18, the Net Interest Income increased by 26% from Rs.747 crore in FY17 to Rs.940 crore in FY18 (Rs.607 crore in H1FY19). The Profit After Tax (PAT) during FY18 increased by 92% during FY18 from Rs.152 crore (excluding exceptional item) in FY17 to Rs.252 crore in FY18.

During FY17 the Company sold its investment in subsidiary companies viz. Avas Financiers Limited and Index Money Ltd and other associate Companies. The profit on sale these investments was Rs.670 crore. The ROTA was 2.12% for FY18 as compared to 2.70% (after excluding exceptional item) for FY17. The operating cost/ average adjusted assets were 4.25% for FY18 as compared to 3.24% in FY17 on account of higher operating cost due to expansion of banking franchise. The profitability parameters were expected to moderate on account of conversion to bank.

Moderate asset quality

AUSFB started recognizing NPAs based on 90 days past due (DPD) from Q1FY18. As on September 30, 2018, GNPA and NNPA ratios were 2.03% [2.01% as on March 31, 2018] and 1.28% [1.27% as on March 31, 2018] respectively. The bank's Net NPA / Tangible Net worth ratio stood at 7.92% as on March 31, 2018 [March 31, 2018: 7.42%] as compared to 4.28% as on March 31, 2017.

Key Rating Weakness

Regional concentration

The bank's lending portfolio had regional concentration with top three states – Rajasthan, Gujarat and Maharashtra collectively constituted 69% of AUM as on September 30, 2018. The state of Rajasthan alone comprised 41% of AUM whereas Maharashtra constituted 17% and Gujarat constituted 12%.

Lower seasoning portfolio

AUSFB was initially into vehicle financing in its NBFC format. Post conversion into SFB, it has witnessed significant portfolio growth in the MSME / SME segments in the last few years. Post conversion of SFB it has started new products like Business Banking, Gold Loan, Agri Loan and consumer durables financing. The performance of its recently originated portfolio needs to be seen. Further, seasoning of the portfolio built up in new geographies is still low.

Analytical approach: Standalone

Applicable Criteria

[Criteria on assigning outlook to Credit Ratings](#)

[CARE's policy on default recognition](#)

[Financial Ratios-Financial Sector](#)

[CARE's Criteria for NBFC](#)

[CARE's Rating Methodology for Banks](#)

About AU Small Finance Bank

AU Small Finance Bank (erstwhile AU Financiers (India) Ltd) (AUSFB) was incorporated in 1996 as an NBFC by Mr. Sanjay Agarwal. The company started CV lending business in 2003 as a franchisee originator for HDFC Bank under 'Channel Business' and later moved to lending on its own books since 2007. Over the past few years, the company forayed into

MSME / SME & structured financing and other types of vehicle financing. The company received license of Small Finance Bank (SFB) from Reserve Bank of India (RBI) on December 20, 2016 and commenced the banking operation from April 19, 2017. The company got its shares listed on BSE and NSE on July 10, 2017. The company also received Schedule Commercial bank status in November, 2017. As part of the transition process to SFB, the company sold 90.10 % stake in AU Housing Finance (renamed as Avas Financiers Ltd) for Rs.828.35 crore. Post becoming SFB it has expanded its portfolio to Gold loans, Agri Loan and Consumer Durables. As on September 30, 2018, AUSFB had a tangible Net-worth of Rs.2,929 crore with Assets Under Management (AUM) of Rs.20,219 crore. As on September 30, 2018, Vehicle financing (including CV, CE and 3W and CARs) accounted for 53% of AUM, with MSME – 38% and SME - 5%. As on September 30, 2018, AUSFB has geographical distribution across 11 states and a UT with 395 branches, 88 asset centers, 16 business correspondent agents, 12,109 employees, 16 offices, and 292 ATMs. As on September 30, 2018, the top three states of Rajasthan (41%), Maharashtra (17%) and Gujrat (12%) collectively constituted 69% of AUM.

Brief Financials

(Rs. Cr)

	FY17 (A)	FY18 (A)
Total Income	1,387	2,155
PAT	822*	292
Total Assets [^]	9,706	18,833
Gross NPA (%)	1.89	2.01
ROTA (%)	10.28*	2.05

A: Audited; *: Including profit on sale of investment in subsidiaries/ associates; ^: Net of intangibles and deferred tax assets (DTA)

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr)	Rating assigned along with Rating Outlook
Certificate of Deposit (CD)	-	-	-	500	CARE A1+

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. Cr)	Rating	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015
1.	Fund-based - LT-Cash Credit	LT	-	-	1)CARE A+; Stable (03-Apr-17)	-	1)CARE A+ (20-Jan-16)	1)CARE A+ (17-Dec-14)
2.	Debt-Subordinate Debt	LT	-	-	1)Withdrawn (03-Apr-17)	-	1)CARE A+ (20-Jan-16)	1)CARE A (17-Dec-14)
3.	Debentures-Non Convertible Debentures	LT	-	-	-	-	1)Withdrawn (20-Jan-16)	1)CARE A+ (17-Dec-14)
4.	Fund-based - LT-Term Loan	LT	491.59	CARE AA-; Stable	1)CARE AA-; Stable (19-Mar-18) 2)CARE A+; Stable (03-Apr-17)	-	-	-
5.	Certificate of Deposit	ST	500	CARE A1+				

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CIN - L67190MH1993PLC071691