AU Small Finance Bank Limited

October 22, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Lower Tier-II Bonds	-	-	Withdrawn
Tier-II Bonds	250.00	CARE AA; Stable	Reaffirmed
Tier-II Bonds	650.00	CARE AA; Stable	Reaffirmed
Certificate of deposit	2,400.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Reaffirmation of ratings assigned to debt instruments of AU Small Finance Bank Limited (AUSFB), factors in continuous growth momentum in business and asset size over the last seven years post-conversion in small finance bank (SFB) in April 2017, making it the largest SFB in India. The scale is improved with the merger of Fincare Small Finance Bank (Fincare). Ratings also consider a growing deposit franchise and a diversified retail focused portfolio which largely consists of secured lending. AUSFB's product lines diversified further with addition of Fincare's segments such as microfinance and gold loans. Ratings also take into cognisance comfortable capitalisation levels supported with periodic equity capital raise, stable asset quality parameters, and healthy profitability.

However, ratings are constrained by regional concentration of advances and deposits although this improved to an extent with the merger, comparatively lower current account-saving account (CASA) proportion, and relatively moderate size as compared to mid-sized private sector banks.

Further, CARE Ratings Limited (CARE Ratings) has taken cognisance of the fact that AUSFB applied to RBI for transition to a Universal Bank.

CARE Ratings has withdrawn ratings on Lower Tier II bonds due to redemption.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Sustainably improving scale of operations with improving product and geographical diversification.
- Scaling up deposits with increasing CASA and retail deposits base, becoming more comparable to mid-sized private sector banking peers.

Negative factors

- Deteriorating asset quality, with gross non-performing assets (GNPA) increasing to over 4% on a sustained basis.
- Deteriorating capital adequacy parameters, with capital adequacy ratio (CAR) falling below 17% on a sustained basis.
- Moderating profitability parameters, with return on total assets (ROTA) falling below 1% on a sustained basis.

Analytical approach: Standalone

Outlook: Stable

CARE Ratings believes that AUSFB will continue maintaining its steady growth in advances, deposits, and healthy profitability profile over the medium term while maintaining stable asset quality and comfortable capitalisation levels.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications.

Detailed description of key rating drivers:

Key strengths

Continuous growth momentum in business

The company commenced operations as an SFB from April 2017 and got the status of scheduled commercial bank (SCB) in November 2017. Merger of Fincare with AUSFB is complete effective from April 01, 2024. Over seven years of operations as an SFB, the bank has been able to ramp up operations from 474 touchpoints as on March 31, 2018, to 2414 touchpoints (new and converted including branches of Fincare) across 21 states and four Union Territories, with over 46,500 employees as on June 30, 2024. AUSFB, the largest SFB in India in terms of asset size, has seen steady growth in total assets increasing from ₹18,833 crore as on March 31, 2018, to ₹1,09,426 crore as on March 31, 2024. Post the merger, the bank's total asset base stood at ₹1,25,942 crore as on June 30, 2024. The bank expects its advances and deposits to grow at 23-25% CAGR by FY27.

Comfortable capitalisation

Despite significant growth in loan book, AUSFB continues to be sufficiently capitalised, helped by regular capital infusions through qualified institutional placement (QIP), the latest being ₹2,000 crore in August 2022, and steady healthy internal accruals. It reported a capital adequacy ratio (CAR) of 20.06% (March 31, 2023: 23.59%, March 31, 2022: 20.99%) and Tier-I CAR of 18.80% (March 31, 2023: 21.78% and March 31, 2022: 19.69%) as on March 30, 2024, well above the minimum regulatory requirement of 15% and 7.5%, respectively. Post the merger with Fincare, AUSFB reported a capital adequacy ratio (CAR) and Tier-I of 20.11% and 18.88% as on June 30, 2024. Going forward, CARE Ratings expects AUSFB to maintain sufficient cushion over minimum regulatory requirements.

Consistent track record of healthy earnings performance

Post-conversion to SFB and access to deposits, cost of funds declined between FY20 and FY22, as it increased proportion of CASA and retail term deposits, further helped by lowering of systemic interest rates. However, cost of funds stayed constant in FY23 as against FY22, even when there was an increase in systemic interest rates due to rate hikes by the RBI. As majority advances comprise small business customers from Tier-II and Tier-III cities that have lower banking penetration, AUSFB is able to enjoy relatively higher yields. Hence, net interest margin (NIM) is higher than universal banks, ranging between 5% and 6%.

Net interest income (NII) is growing consistently, in trend with growing advances and deposits. For the year-ended March 31, 2024, AUSFB continued to grow in NII, with interest income growing at 29% y-o-y, following gross advances growing at 25% y-o-y. Further, non-interest income also grew significantly by 69% y-o-y in FY24. The bank's operating cost increased by 30% as it is actively spending on business expansion, capacity building and investments in digital initiatives, which resulted in pre-provision operating profit (PPOP) growing by 21% for FY24 as compared to FY23. However, credit costs grew significantly in FY24 due to increased slippages and additional provisions created by AUSFB. Further, profit after tax (PAT) reported a marginal increase in PAT by 7% for FY24 post exceptional item. AUSFB reported ROTA of 1.54% for FY24 post exceptional item (FY23: 1.80%).

Post merger, AUSFB reported a net profit of ₹503 crore on a total income of ₹4,315 crore in Q1FY25. Further, it reported a ROTA of 1.71% (annualised) for Q1FY25. CARE Ratings expects NIMs to increase due to integration of high yielding microfinance business, however, it will also impact credit cost going forward. CARE Ratings expects AUSFB to continue maintaining healthy profitability over the medium term.

Stable asset quality

Historically, AUSFB has been able to manage its asset quality at comfortable levels, despite having significant exposure to segments that are more vulnerable to economic downturns. The bank's GNPA levels hovered ~1.7-2.1% between FY18 and FY20, rising to peak levels of 4.3% as on March 31, 2021, in COVID-19 with wheels and micro business loans (MBL) – two biggest segments for AUSFB saw higher slippages. Asset quality improved since Covid and the bank reported GNPA ratio at 1.67% as on March 31, 2024. In Q1FY24, the asset quality saw marginal deterioration across segments especially unsecured loans (credit card, micro finance and personal loan) with AUSFB reporting GNPA of 1.78% as on June 30, 2024, aligned with industry trend and is monitorable. Post merger, micro finance which is a relatively risky segment has become an important segment for AUSFB contributing 8% advances as on June 30, 2024. However, per the management the proportion of unsecured book will be limited to 15-20% with microfinance book capped at 10% of loan portfolio (including securitisation), limiting the impact on asset quality.

Key weaknesses

Relatively lower CASA proportion

AUSFB transformed its liabilities profile by developing deposit base since becoming a Small Finance Bank in FY18. Deposit franchise has consistently increased, with deposits increasing from ₹7,923 crore as on March 31, 2018, to ₹87,812 crore as on March 31, 2024.

The bank's CASA stood at 33.41% March 31, 2024 (March 31, 2023: 38.43%). It continues to granularise deposit book with a focus on increasing retail deposits. Post merger, AUSFB reported a total deposit of ₹97,290 crore as on June 30, 2024, of which CASA was at 32.93%. CASA plus retail term deposits stood at 70% as on June 30, 2024.

While in absolute terms CASA is increasing, CASA ratio has shown a declining trend and this is relatively lower in comparison to a few mid-sized private sector banks. The scaling-up of CASA over next few years will be a key rating sensitivity.

Regional concentration and relatively moderate size

There is regional concentration as top three states account for over 54% of gross advances and 55% deposits of AUSFB as on June 30, 2024. However, concentration of advances exposure to Rajasthan, which is largest state, reduced from 52% as on March 31, 2018, to 27% as on June 30, 2024. The merger enabled AUSFB to diversify geographically in the southern states of India, the scale up is yet to materialise. Although AUSFB has seen strong growth in past few years, its merged asset size continues to be relatively smaller as compared to private sector universal banks in India.

Liquidity: Adequate

AUSFB's asset liabilities maturity (ALM) profile as on June 30, 2024, had no negative cumulative mismatches per the structural liquidity statement in time buckets up to one month. To manage gaps in an optimum manner, the bank has been focusing on increasing granular deposit, where retail term deposits and CASA contributed 70% of total deposits. Post merger, AUSFB's average liquidity coverage ratio (LCR) stood at 117% for the quarter-ended June 30, 2024, as against the regulatory requirement of 100%. The bank maintained sufficient excess statutory liquidity ratio (SLR) and high-quality non-SLR instruments, which can be readily used for repo or liquidated in the secondary market. It can also resort to Rupee borrowing as corporate deposits (CDs), term money, portfolio securitisation, and re-finance from domestic financial institutions such as NABARD, SIDBI, MUDRA, NHB, and others, in case of liquidity need. The bank has access to facilities such as liquidity adjustment facility (LAF), marginal standing facility (MSF), and call money market to meet liquidity requirements.

Environment, social, and governance (ESG) risks

Environmental

- Sourced 10291 fixed deposits amounting ₹703 crore raised.
- ~₹189 crore deployed in Green Assets Lending.
- Currently Lending in Solar and EV Infrastructure.
- AU's Tree Plantation drive conducted, and 550 saplings planted at 10 different locations.
- Sustainability Idea Contest conducted within AU and more that 1,000 responses received on ESG. Top 10 winners were awarded.

Social

- Skill development is the flagship project of the bank. Till Q1'FY25, 21,962 youth were trained, of which 78% were linked to employment across 16 centres of Rajasthan. Three trainees have also secured placement overseas.
- Rural Sports Initiative Project, aimed at holistic development of rural children, is live across 60 locations with over 8,100 children in the age group of 8-16 years getting trained by certified coaches. Two athletes of this initiative clinched medals at the 19th National Youth Athletics Championship 2024.
- The bank supports women entrepreneurs for livelihood generation and capacity building by providing support and access. To date, over 2,580 women are engaged and 872 are nurtured.

Governance

- The bank has 70% independent directors, 20% women directors.
- Board committee on sustainability driving the sustainability agenda.

Applicable criteria

Definition of Default
Rating Outlook and Rating Watch
Bank
Financial Ratios - Financial Sector
Rating Basel III - Hybrid Capital Instruments issued by Banks
Short Term Instruments
Withdrawal Policy

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Financial services	Financial services	Banks	Other bank

AUSFB

AUSFB (erstwhile AU Financiers [India] Limited) was incorporated in 1996 as an NBFC and started the CV lending business in 2003 as a franchisee originator for HDFC Bank under 'Channel Business' and later moved to lend on its own books since 2007. Over the years, the company forayed in MSME and SME, housing loans, and structured financing and other types of vehicle financing.

The company received the license of SFB from the RBI in December 2016 and commenced banking operations from April 2017; it received the status of SCB in November 2017. Post becoming an SFB, it expanded its product portfolio and geographical footprint.

Brief Financials (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)	June 30, 2024 (UA)
	12M (Standalone)	12M (Standalone)	3M (Merged)
Total income	9,240	12,301	4,315
PAT	1,428	1,535	503
Total assets#	90,123	1,09,310	1,25,689
Net NPA (%)	0.42	0.55	0.63
ROTA (%)	1.80	1.54	1.71

A: Audited; UA: Unaudited. Note: These are latest available financial results.
Note: All analytical ratios are per CARE Ratings' calculations.
#Total assets and net worth adjusted by DTA, revaluation reserve, and intangible assets.

CareEdge RATINGS

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Covenants of rated instruments/facilities: Annexure-3

Complexity level of instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Lower Tier-II bonds	INE519Q08137*	22-Mar-18	11.30%	22-Jun-24	-	Withdrawn
Lower Tier-II bonds	INE519Q08145*	20-Mar-18	11.30%	20-Jun-24	-	Withdrawn
Bonds- Tier-II bonds	INE519Q08152	30-Sep-19	12.87%	30-Sep-25	100	CARE AA; Stable
Bonds- Tier-II bonds	INE519Q08178	05-Jul-23	10.75%	05-Jan-29	75	CARE AA; Stable
Bonds- Tier-II bonds	INE519Q08186	09-Aug-23	10.75%	09-Feb-29	50	CARE AA; Stable
Bonds- Tier-II bonds	INE949L08442	03-Aug-22	9.30%	03-Aug-32	350	CARE AA; Stable
Bonds- Tier-II bonds	INE949L08434	03-Aug-22	9.30%	13-Aug-32	100	CARE AA; Stable
Bonds- Tier-II bonds	INE949L08426	03-Aug-22	9.30%	23-Aug-32	50	CARE AA; Stable
Bonds- Tier-II bonds	Proposed	-	-	-	175	CARE AA; Stable
Certificate of deposit	INE949L16CN4	31-Jul-24	7.82%	03-Feb-25	50	CARE A1+
Certificate of deposit	INE949L16CN4	31-Jul-24	7.82%	03-Feb-25	50	CARE A1+
Certificate of deposit	INE949L16CN4	31-Jul-24	7.82%	03-Feb-25	25	CARE A1+
Certificate of deposit	INE949L16CN4	31-Jul-24	7.82%	03-Feb-25	75	CARE A1+
Certificate of deposit	INE949L16CF0	06-Mar-24	8.17%	05-Mar-25	100	CARE A1+
Certificate of deposit	INE949L16CG8	07-Mar-24	8.17%	06-Mar-25	100	CARE A1+
Certificate of deposit	INE949L16CH6	11-Mar-24	8.15%	10-Mar-25	200	CARE A1+
Certificate of deposit	INE949L16CH6	11-Mar-24	8.15%	10-Mar-25	50	CARE A1+
Certificate of deposit	INE949L16CT1	29-Aug-24	8.15%	19-Aug-25	50	CARE A1+
Certificate of deposit	INE949L16CT1	29-Aug-24	8.15%	19-Aug-25	150	CARE A1+
Certificate of deposit	INE949L16CT1	29-Aug-24	8%	19-Aug-25	50	CARE A1+
Certificate of deposit	INE949L16CI4	13-Mar-24	8%	20-Feb-25	200	CARE A1+
Certificate of deposit	INE949L16CI4	13-Mar-24	7.43%	20-Feb-25	50	CARE A1+
Certificate of deposit	INE949L16CS3	29-Aug-24	7.43%	25-Aug-25	200	CARE A1+
Certificate of deposit	INE949L16CP9	31-Jul-24		28-Jan-25	100	CARE A1+
Certificate of deposit	INE949L16CP9	31-Jul-24		28-Jan-25	100	CARE A1+
Certificate of deposit	INE949L16CM6	31-Jul-24		28-Oct-24	100	CARE A1+
Certificate of deposit	INE949L16CM6	30-Jul-24		28-Oct-24	200	CARE A1+
Certificate of deposit	INE949L16CU9	29-Aug-24		28-Nov-24	200	CARE A1+
Certificate of deposit	INE949L16CU9	29-Aug-24		28-Nov-24	50	CARE A1+
Certificate of deposit	Proposed	-	-	Upto 364 days	300	CARE A1+

*ISIN Matured.

Annexure-2: Rating history for last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022
1	Fund-based - LT-Term Loan	LT	-	-	-	-	-	1)Withdrawn (23-Mar-22)
2	Certificate Of Deposit	ST	2400.00	CARE A1+	1)CARE A1+ (14-Aug-24) 2)CARE A1+ (10-Apr-24)	1)CARE A1+ (15-Mar-24) 2)CARE A1+ (11-Mar-24) 3)CARE A1+ (03-Oct-23) 4)CARE A1+ (04-Apr-23)	1)CARE A1+ (27-Jul-22)	1)CARE A1+ (23-Mar-22)
3	Bonds-Tier II Bonds	LT	200.00	CARE AA; Stable	1)CARE AA; Stable (14-Aug-24) 2)CARE AA; Stable (10-Apr-24)	1)CARE AA; Stable (15-Mar-24) 2)CARE AA; Stable (11-Mar-24) 3)CARE AA; Stable (03-Oct-23) 4)CARE AA; Stable (04-Apr-23)	1)CARE AA; Stable (27-Jul-22)	1)CARE AA; Stable (23-Mar-22)
4	Bonds-Tier II Bonds	LT	300.00	CARE AA; Stable	1)CARE AA; Stable (14-Aug-24) 2)CARE AA; Stable	1)CARE AA; Stable (15-Mar-24) 2)CARE AA; Stable	1)CARE AA; Stable (27-Jul-22)	-

					(10-Apr-24)	(11-Mar-24) 3)CARE AA; Stable (03-Oct-23) 4)CARE AA; Stable (04-Apr-23)		
5	Bonds-Tier II Bonds	LT	150.00	CARE AA; Stable	1)CARE AA; Stable (14-Aug-24) 2)CARE AA; Stable (10-Apr-24)	1)CARE AA; Stable (15-Mar-24) 2)CARE AA; Stable (11-Mar-24) 3)CARE AA; Stable (03-Oct-23) 4)CARE AA; Stable (04-Apr-23)	1)CARE AA; Stable (27-Jul-22)	-
6	Bonds-Lower Tier II	LT	-	-	1)CARE AA; Stable (14-Aug-24) 2)CARE AA; Stable (10-Apr-24)	-	-	-
7	Bonds-Tier II Bonds	LT	150.00	CARE AA; Stable	1)CARE AA; Stable (14-Aug-24) 2)CARE AA; Stable (10-Apr-24)	-	-	-
8	Bonds-Tier II Bonds	LT	100.00	CARE AA; Stable	1)CARE AA; Stable (14-Aug-24) 2)CARE AA; Stable	-	-	-

					(10-Apr-24)			

LT: Long term; ST: Short term; LT/ST: Long term/Short term

Annexure-3: Detailed explanation of covenants of rated instruments/facilities: Not applicable

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Bonds-Lower Tier II	Complex
2	Bonds-Tier II Bonds	Complex
3	Certificate Of Deposit	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on complexity levels of rated instruments: CARE Ratings has classified instruments rated by it based on complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for clarifications.

Contact us

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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