

## India

## ADD (no change)

Consensus ratings\*: Buy 22 Hold 6 Sell 6

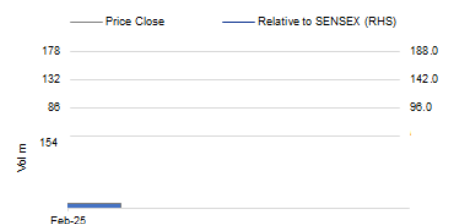
Current price: Rs795  
 Target price: ▲ Rs880  
 Previous target: Rs820  
 Up/downside: 10.7%  
 InCred Research / Consensus: 15.6%

Reuters:  
 Bloomberg: AUBANK IN  
 Market cap: US\$6,875m  
 Rs592,354m  
 Average daily turnover: US\$32.2m  
 Rs2778.4m  
 Current shares o/s: 879.9m  
 Free float: 77.1%

\*Source: Bloomberg

## Key changes in this note

- We have revised our earnings estimates based on the quarterly results.
- We tweak our sustainable RoE assumption and risk-free rate.

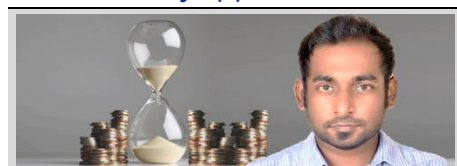


Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(0.1)	35.5	25.4
Relative (%)	0.7	31.6	23.7

Major shareholders	% held
Sanjay Agarwal	15.7
HDFC MF	5.7
Camas	3.6

## Research Analyst(s)



## Bhavik SHAH

T (91) 22 4161 1551

E bhavik.shah@incredresearch.com

## AU Small Finance Bank

## Weak margin; raises credit cost guidance

- Key negatives: Weak margin progression (down 44bp) & credit cost guidance increased by 10-15bp. Positives: Controlled costs & strong treasury gains.
- Though asset quality normalization is delayed, AU SFB has more headwinds than tailwinds, given its rural presence – in case the systemic growth improves.
- We raise our TP to Rs880 (~11% upside) as we trim our risk-free rate & revisit the earnings estimates. We assign a target multiple of 2.9x on FY27F BV.

## Weak margin progress aided by low opex delivers in-line core PPOp

AU Small Finance Bank or AU SFB posted 1QFY26 PAT of Rs5.8bn (+16% YoY; annualized RoA of 1.5%) which beat our estimate owing to strong treasury gains (Rs3bn vs. Rs1bn last quarter). Core PPOp was in line (+9% YoY) and credit costs, although moderate QoQ, remained elevated (200bp vs. 250bp). Margin declined by 44bp QoQ to 5.4% and NII grew by 6% YoY (down 2% QoQ; missed our estimate by 5%). Costs were contained (+4% YoY; 11% below our estimate) while core fee was weak (+4% YoY). Loans grew by 23% YoY (3% QoQ) and deposits were up 31% YoY (3% QoQ). The CET-1 ratio stood at 18.2% and the average LCR improved QoQ (123% vs. 116%).

## Asset quality normalization appears to take longer than expected

Gross slippage increased QoQ to Rs10.3bn (4.6% of trailing loans; annualized) vs. Rs8.9bn last quarter. Recovery/upgrades moderated QoQ (Rs2.9bn vs. Rs3.9bn) while write-offs increased QoQ (Rs4.3bn vs. Rs3.9bn). As a result, headline GNPA's increased by 12% QoQ to Rs27.5bn; the GNPA ratio increased QoQ by 19bp to 2.47%. PCR moderated QoQ (65% vs. 68%). The net NPA ratio inched up to 0.9% (vs. 0.7% last quarter). Credit costs stood at 200bp vs. 250bp last quarter. Management upped its credit cost guidance by 10-15bp to 100bp of average assets (i.e. 150bp of loans), given the higher stress formation from South India mortgage book (predominantly Fincare SFB's) and the delay in MFI asset quality normalization. Management indicated that most of the stress formation in the credit card portfolio has come from the identified pool and has peaked out.

## Margin dips by 44bp QoQ to 5.4%; full-year average likely at 5.5%

The margin decline of 44bp QoQ to 5.4% was mainly led by the repo rate cut impact on yields, lower share of the MFI book, lower investment yields, and higher liquidity. The decline in yields (~30bp QoQ) was partly offset by funding cost benefit (down 6bp). Management stated that there will be some impact on 2QFY26F margin owing to residual pass-through of repo rate cuts but that should be the trough, and margin should improve from there on. We have built in average margin of 5.5%/5.6% for FY26F/27F, respectively.

## Stock is not cheap at 2.6x FY27F BV but a strong compounder

AUF SFB has posted RoA of 1.5% & RoE of ~13% in 1QFY26. We expect RoA to improve to 1.5%/1.7% in FY27F/28F, respectively, and RoE to improve to 15.5%/17.5% in FY27F/28F, respectively, as the asset quality normalizes. We revisit our earnings estimates, tweak our sustainable RoE assumptions and trim our risk-free rate because of which our target price rises to Rs880 (~11% upside) vs. Rs820 earlier. We assign a target multiple of 2.9x on FY27F BV. Downside risks: Lower-than-expected growth/margin, worsening asset quality trend, and higher-than-expected opex growth.

Financial Summary	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Net Interest Income (Rsm)	51,571	80,116	88,678	109,446	133,366
Total Non-Interest Income (Rsm)	17,459	25,263	30,739	34,124	41,767
Operating Revenue (Rsm)	69,030	105,379	119,416	143,569	175,133
Total Provision Charges (Rsm)	(4,307)	(17,926)	(18,600)	(19,288)	(19,518)
Net Profit (Rsm)	16,195	21,059	25,582	32,704	43,436
Core EPS (Rs)	2.42	2.83	3.44	4.39	5.83
Core EPS Growth	17%	17%	21%	28%	33%
FD Core P/E (x)	328.44	281.03	231.35	180.96	136.25
DPS (Rs)	1.08	1.00	1.60	2.05	2.72
Dividend Yield	0.14%	0.13%	0.20%	0.26%	0.34%
BVPS (Rs)	18.8	23.1	26.4	30.7	36.3
P/BV (x)	42.35	34.48	30.07	25.92	21.90
ROE	13.8%	14.2%	13.9%	15.4%	17.4%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 1: Quarterly earnings summary

Rs M	1QFY25	4QFY25	1QFY26	YoY (%)	QoQ (%)
<b>Net Interest Income</b>	<b>19,206</b>	<b>20,939</b>	<b>20,447</b>	<b>6%</b>	<b>-2%</b>
Other Income	5,093	7,607	8,106	59%	7%
--Core Fee	4,903	6,580	5,106	4%	-22%
--Treasury Income	190	1,020	3,000	1479%	194%
--Misc. Income	0	7	0	NA	-100%
<b>Total income</b>	<b>24,299</b>	<b>28,546</b>	<b>28,553</b>	<b>18%</b>	<b>0%</b>
--Core Revenues	24,109	27,519	25,553	6%	-7%
<b>Operating Expenses</b>	<b>14,781</b>	<b>15,623</b>	<b>15,431</b>	<b>4%</b>	<b>-1%</b>
--Staff Expenses	7,901	8,175	8,655	10%	6%
--Other Operating Expenses	6,880	7,449	6,775	-2%	-9%
<b>Operating Profit</b>	<b>9,517</b>	<b>12,923</b>	<b>13,122</b>	<b>38%</b>	<b>2%</b>
--Core PPOp	9,327	11,896	10,122	9%	-15%
<b>Provisions</b>	<b>2,828</b>	<b>6,351</b>	<b>5,333</b>	<b>89%</b>	<b>-16%</b>
<b>PBT</b>	<b>6,689</b>	<b>6,571</b>	<b>7,789</b>	<b>16%</b>	<b>19%</b>
Tax	1,663	1,535	1,980	19%	29%
<b>PAT</b>	<b>5,026</b>	<b>5,037</b>	<b>5,809</b>	<b>16%</b>	<b>15%</b>
EPS	7	7	8		
Advances	896,520	1,070,925	1,098,340	23%	3%
Deposits	972,900	1,242,685	1,276,960	31%	3%
LD Ratio	92%	86%	86%		
CASA Ratio	33%	29%	29%		
Margins (%)	6.00	5.84	5.40	-0.60	-0.44
Overall provisions (in bps)	139	246	197		
---Credit cost (in bps)	139	246	197		
-----NPA provisions	142	273	214		
GNPA	16,132	24,470	27,513	71%	12%
GNPA Ratio (%)	1.78%	2.28%	2.47%		
NNPA	5,626	7,913	9,713	73%	23%
NNPA Ratio (%)	0.63	0.74	0.88		
PCR	10,506	16,557	17,800	69%	8%
PCR Ratio (%)	65%	68%	65%		
Slippages	5,430	8,940	10,270	89%	15%
--% of trailing loans	3.7%	4.9%	4.6%		
CET-1 Ratio (%)	19.5%	18.1%	18.2%		
RoA	1.6%	1.4%	1.5%		
RoE	13.2%	11.9%	13.3%		

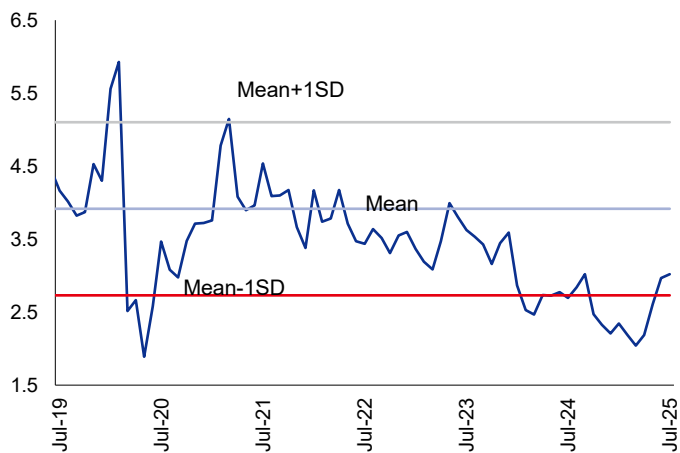
SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 2: Our revised earnings estimates**

Rs Bn	New Estimates				Old Estimates			Change		
	FY25	FY26F	FY27F	FY28F	FY26F	FY27F	FY28F	FY26F	FY27F	FY28F
Net Interest Income	80	89	109	133	93	116	138	-5%	-5%	-4%
--Growth YoY	55%	11%	23%	22%	17%	24%	20%			
Non Interest Income	25	31	34	42	29	35	43	7%	-3%	-3%
--Growth YoY	45%	22%	11%	22%	14%	22%	22%			
Total Income	105	119	144	175	122	151	181	-2%	-5%	-3%
--Growth YoY	53%	13%	20%	22%	16%	24%	20%			
Opex	60	67	81	98	71	86	104	-6%	-6%	-6%
--Growth YoY	36%	12%	21%	21%	19%	21%	21%			
PPOP	46	53	63	78	52	65	78	2%	-4%	0%
--Growth YoY	82%	15%	19%	23%	13%	27%	19%			
Provision	18	19	19	20	19	20	20	0%	-2%	-1%
--as % of avg. loans	199	158	137	116	157	138	116			
PBT	28	34	44	58	33	46	58	4%	-5%	0%
Tax	7	9	11	15	8	12	15	-4%	5%	0%
PAT	21	26	33	43	25	34	43	4%	-5%	0%
--Growth YoY	30%	21%	28%	33%	17%	39%	27%			
Advances	1,071	1,278	1,531	1,835	1,288	1,547	1,857	-1%	-1%	-1%
--Growth YoY	46%	19%	20%	20%	20%	20%	20%			
Deposits	1,243	1,541	1,880	2,294	1,541	1,880	2,294	0%	0%	0%
--Growth YoY	43%	24%	22%	22%	24%	22%	22%			
Book Value	231	264	307	363	287	329	381	-8%	-7%	-5%
--Growth YoY	23%	15%	16%	18%	24%	15%	16%			
EPS	29	34	44	58	33	43	55	4%	2%	7%
--Growth YoY	24%	20%	28%	33%	15%	31%	27%			
ROA	1.5%	1.5%	1.6%	1.8%	1.5%	1.7%	1.7%	5	-6	2
ROE	13.1%	14.0%	15.5%	17.5%	13.1%	14.1%	15.5%	82	140	205

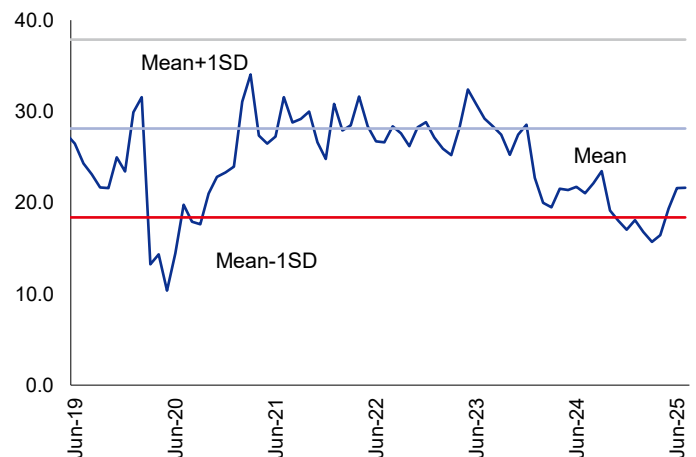
SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 3: One-year forward P/BV**



SOURCE: INCRED RESEARCH

**Figure 4: One-year forward P/E**



SOURCE: INCRED RESEARCH

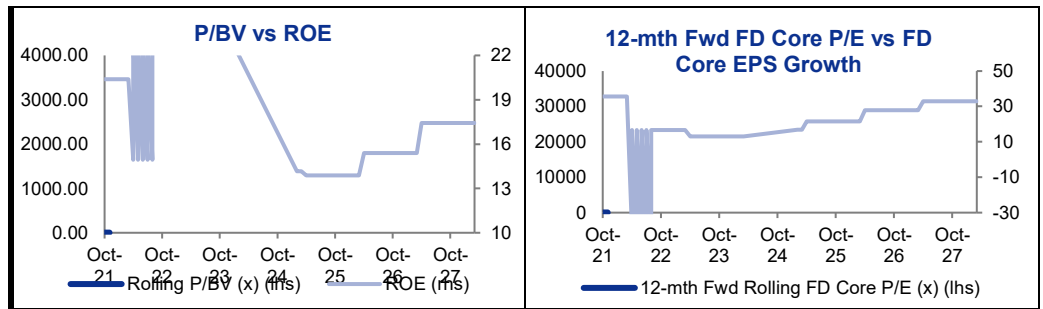
Figure 5: Financial summary

AU Small Finance Bank

Profit and Loss Statement					Per Share Data and Valuations				
Rs Bn (Year end-March)	FY25	FY26F	FY27F	FY28F	Year end-March	FY25	FY26F	FY27F	FY28F
Interest Income	160,637	187,881	226,012	272,754	EPS	28.67	34.36	43.93	58.34
Interest Expense	80,521	99,203	116,566	139,388	Book Value	231	264	307	363
<b>Net Interest Income (Incl. Securitization)</b>	<b>80,116</b>	<b>88,678</b>	<b>109,446</b>	<b>133,366</b>	Core PPOP	59	66	84	103
—Fee Income	22,900	27,193	33,399	41,038	DPS	1.0	1.6	2.1	2.7
—Capital Gains	2,350	3,525	700	700					
—Miscellaneous Inc.	13	21	25	30					
Total Non Interest Income	25,263	30,739	34,123	41,767	<b>Valuations</b>				
<b>Total Operating Income</b>	<b>105,379</b>	<b>119,416</b>	<b>143,569</b>	<b>175,133</b>	P/E	27.6	23.0	18.0	13.5
—Employee Exp	31,478	35,768	42,027	49,382	P/BV	3.4	3.0	2.6	2.2
—Other Expenses	28,095	30,825	38,531	48,164	P/Core PPOP	13.4	11.9	9.4	7.7
Total Operating Expenses	59,572	66,593	80,558	97,546	Dividend Yield	0.1%	0.2%	0.3%	0.3%
<b>Operating Profit</b>	<b>45,807</b>	<b>52,824</b>	<b>63,011</b>	<b>77,587</b>	<b>Ratio Analysis</b>				
Total provisions	17,926	18,600	19,288	19,518	<b>Year end-March</b>	<b>FY25</b>	<b>FY26F</b>	<b>FY27F</b>	<b>FY28F</b>
<b>Profit Before Tax</b>	<b>27,881</b>	<b>34,223</b>	<b>43,723</b>	<b>58,070</b>	<b>Margins</b>				
Provision for Tax	6,821	8,642	11,018	14,634	Net Interest Margin (NIM)	5.9%	5.5%	5.6%	5.6%
<b>Net Profit</b>	<b>21,059</b>	<b>25,582</b>	<b>32,704</b>	<b>43,436</b>	Average yield on assets	11.9%	11.3%	11.3%	11.2%
<b>Net Profit (Reported)</b>	<b>21,059</b>	<b>25,582</b>	<b>32,704</b>	<b>43,436</b>	Cost of earning assets	6.0%	6.0%	5.8%	5.7%
Balance Sheet Data									
Rs Bn (YE March)	FY25	FY26F	FY27F	FY28F	<b>Growth Ratios</b>				
Shareholders' equity	171,663	196,790	228,300	270,209	Net Interest Income	55%	11%	23%	22%
Deposits	1,242,685	1,540,930	1,879,935	2,293,520	Non Interest Income	45%	22%	11%	22%
Borrowings	116,599	127,259	144,848	165,075	Operating expenses	36%	12%	21%	21%
Other Liabilities & Prov.	47,509	52,260	60,099	69,114	Core Operating Profit				
<b>Total Liabilities</b>	<b>1,578,457</b>	<b>1,917,239</b>	<b>2,313,181</b>	<b>2,797,918</b>	Net Profit	30%	21%	28%	33%
					EPS	18%	20%	28%	33%
Cash & Balances with RBI	94,664	102,615	124,550	151,235	Book Value	23%	15%	16%	34%
Investments	378,475	497,506	613,479	761,095	Deposits	43%	24%	22%	22%
Advances	1,070,925	1,278,022	1,530,694	1,835,013	Advances	46%	19%	20%	20%
<b>Total Assets</b>	<b>1,578,457</b>	<b>1,917,239</b>	<b>2,313,181</b>	<b>2,797,918</b>	Total Assets	44%	21%	21%	21%
<b>Gross AUM</b>	<b>1,171,989</b>	<b>1,405,082</b>	<b>1,700,646</b>	<b>2,032,649</b>	Gross AUM	43%	20%	21%	20%
Earning Assets, ex off-BS AUM	1,544,064	1,878,143	2,268,723	2,747,343	<b>Profitability Ratios</b>				
Average IEA, ex off-BS AUM	1,316,523	1,659,429	2,005,915	2,426,910	Return On Equity	13.1%	14.0%	15.5%	17.5%
					Return on Assets, including off-BS AUM	1.5%	1.4%	1.5%	1.7%
<b>Asset Quality</b>					<b>Efficiency Ratios</b>				
Credit Cost (bps)	171	148	126	106	Cost Income Ratio	57%	56%	56%	56%
Gross NPL	24,470	40,789	59,998	82,991	Expenses/Avg Assets, including off-BS AUM	4.1%	3.8%	3.7%	3.7%
Net NPL	7,913	14,344	21,304	33,214					
Reserve Coverage	16,557	26,446	38,694	49,777	<b>Capital Adequacy</b>				
Gross NPL Ratio	2.3%	3.1%	3.8%	4.4%	CET 1 Ratio	18.1%	16.9%	16.3%	16.0%
Net NPL Ratio	0.7%	1.1%	1.4%	1.8%	Tier 1 Ratio	18.1%	16.9%	16.3%	16.0%
Coverage Ratio	68%	65%	64%	60%	Capital Adequacy Ratio	20.1%	18.4%	17.6%	17.1%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

## BY THE NUMBERS



### Profit & Loss

(Rsm)	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Net Interest Income	51,571	80,116	88,678	109,446	133,366
<b>Total Non-Interest Income</b>	<b>17,459</b>	<b>25,263</b>	<b>30,739</b>	<b>34,124</b>	<b>41,767</b>
Operating Revenue	69,030	105,379	119,416	143,569	175,133
<b>Total Non-Interest Expenses</b>	<b>(43,880)</b>	<b>(59,572)</b>	<b>(66,593)</b>	<b>(80,558)</b>	<b>(97,546)</b>
Pre-provision Operating Profit	25,150	45,807	52,824	63,011	77,587
<b>Total Provision Charges</b>	<b>(4,307)</b>	<b>(17,926)</b>	<b>(18,600)</b>	<b>(19,288)</b>	<b>(19,518)</b>
Operating Profit After Provisions	20,842	27,881	34,223	43,723	58,070
<b>Pretax Income/(Loss) from Assoc.</b>					
Operating EBIT (incl Associates)	20,842	27,881	34,223	43,723	58,070
<b>Non-Operating Income/(Expense)</b>					
Profit Before Tax (pre-EI)	20,842	27,881	34,223	43,723	58,070
<b>Exceptional Items</b>					
Pre-tax Profit	20,842	27,881	34,223	43,723	58,070
Taxation	(4,647)	(6,821)	(8,642)	(11,018)	(14,634)
Consolidation Adjustments & Others					
<b>Exceptional Income - post-tax</b>					
Profit After Tax	16,195	21,059	25,582	32,704	43,436
Minority Interests					
Pref. & Special Div					
<b>FX And Other Adj.</b>					
Net Profit	16,195	21,059	25,582	32,704	43,436
Recurring Net Profit					

### Balance Sheet Employment

(Rsm)	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Gross Loans/Cust Deposits					
Avg Loans/Avg Deposits	84.1%	85.2%	84.4%	82.1%	80.6%
Avg Liquid Assets/Avg Assets	97.5%	97.7%	97.9%	98.0%	98.1%
<b>Avg Liquid Assets/Avg IEAs</b>	<b>108.8%</b>	<b>106.5%</b>	<b>106.1%</b>	<b>105.8%</b>	<b>105.8%</b>
Net Cust Loans/Assets					
<b>Net Cust Loans/Broad Deposits</b>					
Equity & Provns/Gross Cust Loans					
Asset Risk Weighting					
<b>Provision Charge/Avg Cust Loans</b>	<b>0.65%</b>	<b>1.99%</b>	<b>1.58%</b>	<b>1.37%</b>	<b>1.16%</b>
<b>Provision Charge/Avg Assets</b>	<b>0.43%</b>	<b>1.34%</b>	<b>1.06%</b>	<b>0.91%</b>	<b>0.76%</b>
Total Write Offs/Average Assets					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

## BY THE NUMBERS...cont'd

### Balance Sheet

(Rsm)	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
<b>Total Gross Loans</b>	<b>731,627</b>	<b>1,070,925</b>	<b>1,278,022</b>	<b>1,530,694</b>	<b>1,835,013</b>
Liquid Assets & Invst. (Current)	271,334	378,475	497,506	613,479	761,095
Other Int. Earning Assets					
Total Gross Int. Earning Assets	1,002,960	1,449,400	1,775,528	2,144,173	2,596,108
<b>Total Provisions/Loan Loss Reserve</b>					
Total Net Interest Earning Assets	1,002,960	1,449,400	1,775,528	2,144,173	2,596,108
Intangible Assets					
<b>Other Non-Interest Earning Assets</b>	<b>19,017</b>	<b>25,268</b>	<b>29,059</b>	<b>33,417</b>	<b>38,430</b>
<b>Total Non-Interest Earning Assets</b>	<b>27,533</b>	<b>34,393</b>	<b>39,096</b>	<b>44,458</b>	<b>50,575</b>
Cash And Marketable Securities	63,763	94,664	102,615	124,550	151,235
<b>Long-term Investments</b>					
Total Assets	1,094,257	1,578,457	1,917,239	2,313,181	2,797,918
Customer Interest-Bearing Liabilities	871,821	1,242,686	1,540,930	1,879,935	2,293,520
Bank Deposits					
Interest Bearing Liabilities: Others					
Total Interest-Bearing Liabilities	916,615	1,349,285	1,658,189	2,014,782	2,448,595
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	42,047	47,509	52,260	60,099	69,114
Total Liabilities	958,661	1,396,794	1,710,449	2,074,882	2,517,709
Shareholders Equity	125,595	171,663	196,790	228,300	270,209
<b>Minority Interests</b>					
Total Equity	125,595	171,663	196,790	228,300	270,209

### Key Ratios

	Mar-24A	Mar-25A	Mar-26F	Mar-27F	Mar-28F
Total Income Growth	17.8%	55.4%	10.7%	23.4%	21.9%
Operating Profit Growth	27.5%	82.1%	15.3%	19.3%	23.1%
Pretax Profit Growth	15%	34%	23%	28%	33%
Net Interest To Total Income	74.7%	76.0%	74.3%	76.2%	76.2%
Cost Of Funds	6.49%	7.11%	6.60%	6.35%	6.25%
Return On Interest Earning Assets	11.8%	13.1%	11.7%	11.5%	11.5%
Net Interest Spread	5.32%	5.99%	5.05%	5.18%	5.26%
Net Interest Margin (Avg Deposits)	6.59%	7.58%	6.37%	6.40%	6.39%
Net Interest Margin (Avg RWA)					
Provisions to Pre Prov. Operating Profit	17%	39%	35%	31%	25%
Interest Return On Average Assets	5.17%	6.00%	5.07%	5.17%	5.22%
Effective Tax Rate	22.3%	24.5%	25.3%	25.2%	25.2%
Net Dividend Payout Ratio	4.4%	4.7%	4.7%	4.7%	4.7%
Return On Average Assets	1.62%	1.58%	1.46%	1.55%	1.70%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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#### **InCred Research Services Private Limited**

##### **Research Analyst SEBI Registration Number: INH000011024**

Registered Office: Unit No 1203, 12th Floor, B Wing, The Capital, C-70, G Block, BKC, Bandra (E), Mumbai – 400051

Phone: +91-22-6844-6100

Corporate Office: 05<sup>th</sup> floor, Laxmi Towers, Plot No. C-25, G Block, Bandra – Kurla Complex, Bandra (East), Mumbai – 400051

Phone: +91-22-4161-1500

Name of the Compliance Officer: Mr. Yogesh Kadam

Email ID: compliance@incredresearch.com, Phone No: +91-22-41611539

For any queries or grievances, you may contact the Grievance Officer.

Name of the Grievance Officer: Mr. Rajarshi Maitra

Phone no. +91-022-41611546

Email ID: rajarshi.maitra@incredresearch.com

CIN: U74999MH2016PTC287535



## Recommendation Framework

### Stock Ratings

Definition:

- Add** The stock's total return is expected to exceed 10% over the next 12 months.
- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
- Reduce** The stock's total return is expected to fall below 0% or more over the next 12 months.

*The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.*

### Sector Ratings

Definition:

- Overweight** An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

### Country Ratings

Definition:

- Overweight** An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral** A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight** An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.