

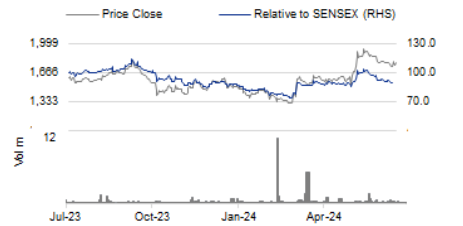
India

ADD (no change)

Consensus ratings*: Buy 17 Hold 4 Sell 2	
Current price:	Rs1,778
Target price:	Rs2,000
Previous target:	Rs2,000
Up/downside:	12.5%
InCred Research / Consensus:	6.8%
Reuters:	AVAS.NS
Bloomberg:	AAVAS IN
Market cap:	US\$1,681m Rs140,726m
Average daily turnover:	US\$8.4m Rs707.0m
Current shares o/s:	79.1m
Free float:	73.5%
*Source: Bloomberg	

Key changes in this note

➤ Aavas Financiers is a key beneficiary of improving rural housing demand. However, current performance is a cause of concern. Retain ADD rating with a TP of Rs2,000.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(4.9)	10.4	10.0
Relative (%)	(6.5)	1.7	(8.3)

Major shareholders	% held
Lake Districts	15.6
SBI MF	8.5
Partners Group	7.6

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Aavas Financiers Ltd

Weak performance across parameters

- Aavas Financiers posted a lower-than-expected 1Q PAT of Rs1.26bn (InCred est: Rs1.41bn) amid weak growth, declining margins & elevated credit costs.
- The fall in margins by ~60bp qoq is due to softer yields amid tight competition while there were elevated credit costs (+11bp qoq) amid a spurt in NPAs.
- It is a key beneficiary of improving rural housing demand. However, its current performance is a cause of concern. Retain ADD rating with a TP of Rs2,000.

Weak disbursements; company's improved presence is encouraging

Aavas Financiers (Aavas) reported disbursements amounting to Rs12.1bn (+13.4% yoy/-35.7% qoq) in 1QFY25 amid a lower sanction-to-disbursement ratio of ~77% against the company's historic average of ~83-85%. Management has indicated that sanctions during the quarter improved by ~25% yoy which, in turn, will aid disbursements in the coming quarters. The demand environment and new customer acquisitions continue to remain healthy. Aavas is improving its presence in new geographies like Karnataka and Uttar Pradesh as well as deepening its presence in existing stronghold states like Rajasthan, Gujarat, and Maharashtra. We are building in ~25% CAGR in disbursements over FY24-27F which will translate into ~23.6% CAGR in assets under management or AUM.

Spreads close to their bottom; recent rise in yields to aid margins

Aavas Financiers witnessed ~6bp decline in spreads sequentially to ~500bp amid a consistent rise in the cost of funds as well as stagnant yield on advances. However, the margin decline has been heavy at ~60bp amid lower AUM growth. Though margins may remain volatile in the near term, the recent hike of ~25bp in the prime lending rate (PLR) will support yields for ~60% of the variable loan book. Management has highlighted that during expansion into new geographies, the company prefers low risk/low yield customers. However, gradually with the rise in comfort, the company increases its dominance in superior yield products. Thus, the recent expansion in southern and eastern India will eventually generate better yields.

Operating leverage to boost profitability further

Post change in management, Aavas Financiers has witnessed a steep rise in operating expenses which were initially pertaining to employee costs amid higher attrition followed by elevated tech-driven expenses to improve the overall efficiency. We believe such tech investments will improve the overall efficiency at branch and employee levels. We expect cost-to-average assets for the company to improve to ~3.1% by FY27F vs. ~3.6% in FY24.

Outlook & valuation

We had upgraded Aavas Financiers' rating last quarter to ADD as the company was returning to a profitable growth trajectory with improving return ratios. The current quarter's performance has been disappointing, but we expect an improvement in the coming quarters. Retain ADD rating with a target price of Rs2,000, corresponding to ~3x FY26F BV. Downside risks: Attrition at the top management level and growth slowdown.

Financial Summary

	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Net Interest Income (Rsm)	7,971	9,063	10,946	13,530	16,679
Total Non-Interest Income (Rsm)	2,220	2,856	3,284	3,771	4,637
Operating Revenue (Rsm)	10,191	11,919	14,230	17,301	21,316
Total Provision Charges (Rsm)	(124)	(245)	(466)	(572)	(709)
Net Profit (Rsm)	4,301	4,907	5,774	7,028	8,900
Core EPS (Rs)	54.78	62.51	73.55	89.52	113.37
Core EPS Growth	21%	14%	18%	22%	27%
FD Core P/E (x)	32.46	28.45	24.18	19.86	15.69
DPS (Rs)	0.00	0.00	0.00	0.00	0.00
Dividend Yield	0.00%	0.00%	0.00%	0.00%	0.00%
BVPS (Rs)	416.5	480.6	560.6	656.5	776.2
P/BV (x)	4.27	3.70	3.17	2.71	2.29
ROE	14.2%	13.9%	14.1%	14.7%	15.8%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 1: Quarterly earnings summary

Particulars (Rs m)	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	4QFY24	1QFY25	YoY (%)	QoQ (%)
Net interest income	1,802	1,877	2,082	2,213	2,262	2,223	2,208	2,371	2,446	8.1%	3.2%
<i>NIM (% of AUM)</i>	<i>7.7%</i>	<i>8.2%</i>	<i>8.2%</i>	<i>8.3%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>7.9%</i>	<i>7.9%</i>	<i>7.3%</i>		
Other income	143	140	149	155	174	201	206	285	261	49.8%	-8.3%
Operating expenses	1,026	1,147	1,201	1,204	1,339	1,308	1,349	1,434	1,379	3.0%	-3.9%
Operating profit	1,156	1,394	1,415	1,650	1,464	1,631	1,577	1,818	1,695	15.8%	-6.8%
Provisions	9	16	35	64	57	65	80	43	86	51.2%	98.9%
Exceptional items											
PBT	1,147	1,378	1,380	1,587	1,407	1,565	1,497	1,775	1,609	14.4%	-9.3%
Tax	254	310	307	318	310	348	331	349	348	12.5%	-0.1%
PAT	892	1,068	1,073	1,268	1,097	1,217	1,167	1,426	1,261	14.9%	-11.6%
AUM (Rsbn)	118.9	125.4	130.9	141.7	146.5	153.2	160.8	173.1	178.4	21.8%	3.1%
Disbursements (Rsbn)	10.9	11.5	12.0	15.8	10.7	12.6	13.7	18.8	12.1	13.4%	-35.7%

SOURCE: INCRED RESEARCH

Figure 2: InCred BFSI coverage universe

Y/E Mar (Rs m)	FY25F			FY26F			FY27F		
	Earlier	Revised	% change	Earlier	Revised	% change	Earlier	Revised	% change
Net interest income	10,703	10,946	2.3%	13,827	13,530	-2.1%	16,827	16,679	-0.9%
PPOP	7,700	7,916	2.8%	9,799	9,640	-1.6%	12,199	12,193	0.0%
PAT	5,576	5,774	3.5%	6,788	7,028	3.5%	8,788	8,900	1.3%
EPS (Rs)	71	74	3.5%	86	90	3.5%	115	113	-1.2%
BV (Rs)	563	561	-0.4%	657	656	0.0%	777	776	-0.1%
AUM(Rsbn)	209	213	2.1%	254	264	3.7%	324	327	1.0%

SOURCES: INCRED RESEARCH

Earnings conference-call highlights

- Management maintains its AUM growth target of 20-25% and disbursement target of 25%.
- Management believes that borrowing costs have peaked out, in line with the benchmarks.
- The focus on innovation, technological development and cost optimization will bring in efficiency and improve opex, which is visible in a better cost-to-asset ratio, eventually improving the RoA. Opex, excluding ESOP reversal, is at 3.95%. The long-term guidance for the coming years is 3% opex cost.
- Muted loan growth was attributed to the lower sanction-to-disbursement rate, despite a 25% growth in sanctions. The momentum is expected to come back in the coming quarters with the sanction-to-disbursement ratio coming to the normal level of 85-87%.
- The end use of micro MSME loan is towards meeting working capital needs as these loans are unsecured in nature. Other mortgage loans have their end use for captive purpose.
- Management maintains its guidance of 5% spreads, despite the blended cost of funds inching towards the marginal cost of funds and falling yields. The transmission of higher marginal cost of funds was not possible to existing set of disbursement customers, leading to yields falling. It is expected to improve in the coming quarters as the additional cost is passed on to the customers.
- Despite the rate hike taken in 4QFY24, the yield did not improve on a computed level in the published numbers, as interest reversal as per an RBI circular, offsets the incremental yield.
- Balance transfer cases in the industry, on an average basis, is 5.6%. Management factors in 6% of balance transfer cases, which is well within control at 5-5.5%. The repayment to AUM ratio is well within control at 16% for the quarter.
- Employee costs on a YoY basis declined due to reversal of ESOP expenses.
- Tech spending done is going to benefit for the next 10 years due to which these expenses have been capitalized.
- Urban housing scheme from the Central government will not impact Aavas Financiers as it is not a segment where the company operates. The company operates in tier-3 to tier-5 cities with a major focus on rural self-constructed properties.

- Home loan and MSME loans put together witnessed a 6-8% rise in average ticket size.
- Home loans with a ticket size of more than Rs 2.5m accounted for 5-6% of AUM.

Figure 3: InCred BFSI coverage universe

Banks	Rating	CMP(Rs)	TP(Rs)	P/BV(x) (at TP)			ROA(%)			ROE(%)		
				FY25F	FY26F	FY27F	FY25F	FY26F	FY27F	FY25F	FY26F	FY27F
SBI **	ADD	848	1,000	2.1	1.8	1.6	1.0%	1.1%	1.1%	16.3%	17.2%	17.6%
HDFC Bank **	ADD	1,616	2,000	3.1	2.8	2.6	1.9%	2.0%	2.0%	15.4%	16.3%	16.9%
ICICI Bank	ADD	1,197	1,300	3.5	3.0	2.6	2.3%	2.2%	2.3%	17.7%	17.3%	17.7%
Axis Bank	HOLD	1,175	1,300	2.3	2.0	1.7	1.7%	1.7%	1.7%	16.8%	15.9%	16.3%
IndusInd Bank	HOLD	1,379	1,650	1.8	1.6	1.4	1.7%	1.7%	1.7%	14.1%	14.4%	14.8%

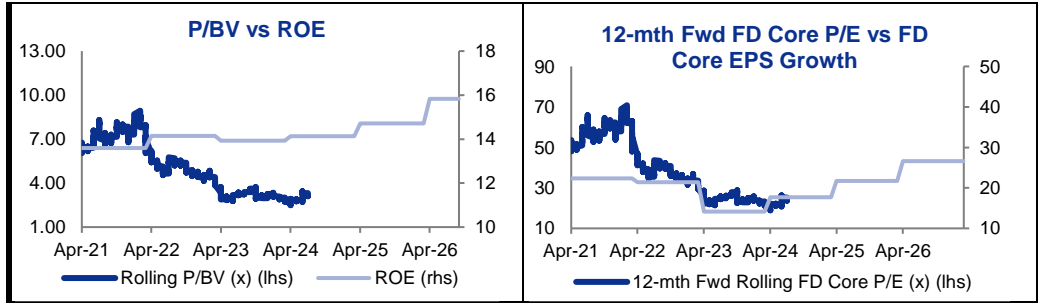
NBFCs	Rating	CMP(Rs)	TP(Rs)	P/BV(x) (at TP)			ROA(%)			ROE(%)		
				FY25F	FY26F	FY27F	FY25F	FY26F	FY27F	FY25F	FY26F	FY27F
Bajaj Finance	ADD	6,647	9,000	6.0	5.1	4.2	4.2%	4.4%	4.5%	21.0%	23.5%	25.4%
Cholamandalam Finance	ADD	1,363	1,400	5.0	4.1	3.4	2.5%	2.5%	2.5%	21.0%	21.8%	22.5%
MMFS **	ADD	289	370	2.4	2.2	2.0	1.8%	1.9%	2.0%	12.3%	14.0%	15.7%
Shriram Finance **	ADD	2,679	2,950	2.0	1.7	1.4	3.4%	3.5%	3.5%	16.9%	17.3%	17.9%
SBI Cards **	REDUCE	730	500	3.4	2.9	2.5	3.6%	3.2%	3.0%	17.8%	16.6%	16.3%
Aavas Financiers	ADD	1,778	2,000	3.6	3.0	2.6	3.1%	3.1%	3.1%	14.1%	14.7%	15.8%
Home First Finance	ADD	1,030	1,100	4.2	3.7	3.2	3.4%	3.4%	3.4%	16.2%	17.7%	19.3%
Spandana Spoorthy	ADD	699	1,300	2.1	1.8	1.5	4.4%	4.6%	4.6%	16.7%	17.9%	18.2%
Fusion Micro Finance	HOLD	438	580	1.7	1.4	1.1	4.7%	4.7%	4.7%	19.4%	19.6%	19.7%

AMCs	Rating	CMP(Rs)	TP(Rs)	P/E(x) (at TP)			ROAUM(%)			ROE(%)		
				FY25F	FY26F	FY27F	FY25F	FY26F	FY27F	FY25F	FY26F	FY27F
Nippon AMC	ADD	639	800	35.7	29.5	23.7	0.28%	0.26%	0.25%	35.2%	41.8%	50.7%
HDFC AMC	HOLD	4,058	4,250	33.5	29.9	25.3	0.37%	0.35%	0.35%	32.8%	34.2%	37.3%
UTI AMC	ADD	1,027	1,200	16.8	13.8	11.8	0.30%	0.30%	0.29%	19.5%	21.1%	22.0%
ABSL AMC**	ADD	697	950	26.9	22.0	18.2	0.27%	0.27%	0.27%	29.9%	32.0%	33.9%

Insurance	Rating	CMP(Rs)	TP(Rs)	P/EV (x) (at TP)			Return on EV (%)			ROE(%)		
				FY25F	FY26F	FY27F	FY25F	FY26F	FY27F	FY25F	FY26F	FY27F
SBI Life Insurance	HOLD	1695	1750	2.5	2.2	1.8	18.9%	18.5%	18.1%	15.4%	16.6%	16.2%

** HIGH CONVICTION
SOURCES: INCRED RESEARCH

BY THE NUMBERS



Profit & Loss

(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Net Interest Income	7,971	9,063	10,946	13,530	16,679
Total Non-Interest Income	2,220	2,856	3,284	3,771	4,637
Operating Revenue	10,191	11,919	14,230	17,301	21,316
Total Non-Interest Expenses	(4,577)	(5,430)	(6,313)	(7,661)	(9,123)
Pre-provision Operating Profit	5,614	6,489	7,916	9,640	12,193
Total Provision Charges	(124)	(245)	(466)	(572)	(709)
Operating Profit After Provisions	5,490	6,245	7,451	9,068	11,484
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	5,490	6,245	7,451	9,068	11,484
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	5,490	6,245	7,451	9,068	11,484
Exceptional Items					
Pre-tax Profit	5,490	6,245	7,451	9,068	11,484
Taxation	(1,189)	(1,337)	(1,676)	(2,040)	(2,584)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	4,301	4,907	5,774	7,028	8,900
Minority Interests					
Pref. & Special Div					
FX And Other Adj.					
Net Profit	4,301	4,907	5,774	7,028	8,900
Recurring Net Profit					

Balance Sheet Employment

(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Gross Loans/Cust Deposits					
Avg Loans/Avg Deposits					
Avg Liquid Assets/Avg Assets	96.0%	95.8%	95.8%	96.0%	96.2%
Avg Liquid Assets/Avg IEAs	114.4%	112.5%	114.4%	115.7%	116.6%
Net Cust Loans/Assets					
Net Cust Loans/Broad Deposits					
Equity & Provsns/Gross Cust Loans					
Asset Risk Weighting					
Provision Charge/Avg Cust Loans					
Provision Charge/Avg Assets					
Total Write Offs/Average Assets					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rsm)	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Total Gross Loans	114,763	140,044	170,399	210,831	261,836
Liquid Assets & Invst. (Current)					
Other Int. Earning Assets					
Total Gross Int. Earning Assets	114,763	140,044	170,399	210,831	261,836
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets	114,763	140,044	170,399	210,831	261,836
Intangible Assets					
Other Non-Interest Earning Assets	3,734	4,191	4,610	5,071	5,578
Total Non-Interest Earning Assets	4,295	5,351	6,002	6,742	7,583
Cash And Marketable Securities	13,816	17,978	26,575	33,464	44,882
Long-term Investments	1,231	1,822	2,550	3,315	4,144
Total Assets	134,105	165,195	205,526	254,352	318,445
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others	98,873	123,365	155,381	194,637	246,888
Total Interest-Bearing Liabilities	98,873	123,365	155,381	194,637	246,888
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	2,536	4,097	6,138	8,180	10,623
Total Liabilities	101,408	127,462	161,519	202,817	257,510
Shareholders Equity	32,697	37,732	44,007	51,535	60,935
Minority Interests					
Total Equity	32,697	37,732	44,007	51,535	60,935

Key Ratios					
	Mar-23A	Mar-24A	Mar-25F	Mar-26F	Mar-27F
Total Income Growth	22.9%	13.7%	20.8%	23.6%	23.3%
Operating Profit Growth	18.2%	15.6%	22.0%	21.8%	26.5%
Pretax Profit Growth	21%	14%	19%	22%	27%
Net Interest To Total Income	78.2%	76.0%	76.9%	78.2%	78.2%
Cost Of Funds	6.60%	7.45%	7.20%	6.80%	6.50%
Return On Interest Earning Assets	13.5%	13.6%	13.5%	13.3%	13.1%
Net Interest Spread	6.92%	6.16%	6.32%	6.54%	6.63%
Net Interest Margin (Avg Deposits)					
Net Interest Margin (Avg RWA)					
Provisions to Pre Prov. Operating Profit	2%	4%	6%	6%	6%
Interest Return On Average Assets	6.52%	6.06%	5.91%	5.88%	5.82%
Effective Tax Rate	21.7%	21.4%	22.5%	22.5%	22.5%
Net Dividend Payout Ratio					
Return On Average Assets	3.52%	3.28%	3.12%	3.06%	3.11%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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any other material conflict of interest at the time of publication of the research report or at the time of public appearance	NO	NO
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managed or co-managed public offering of securities for the subject company in the last twelve months	NO	NO
received any compensation or other benefits from the subject company or third party in connection with the research report	NO	NO
served as an officer, director or employee of the subject company	NO	NO
been engaged in market making activity for the subject company	NO	NO

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