BUY

TP: Rs 9,105 | ⮝ 29%

BAJAJ FINANCE | NBFC | 01 September 2023

From strength to strength – initiate with BUY

- **Momentum across consumer, commercial, SME and mortgage lending to propel a 28% AUM CAGR over FY23-FY25E**
- **Stellar record on asset quality (10Y GNPA at 1.1-1.8%); expect comfortable GNPA of 1.3%, credit cost of 1.7% over 2Y**
- **Seasoned management, solid execution to help fend off rivals; valuations have moderated as well – initiate with BUY, TP Rs 9,105**

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Diverse, high-growth portfolio: BAF has delivered a robust 25% AUM CAGR to Rs 2.5tn over FY18-FY23, scaling up to 69mn customer accounts from 26mn. In line with guidance of 29-31% growth in FY24 and 25-27% long term, we forecast a 28% AUM CAGR to Rs 4tn over FY23-FY25, lifted by buoyancy across consumer loans (42% of AUM), mortgage (31%), SME (14%) and commercial lending (13%). Mortgages, having risen 28% on average over five quarters, will be a key factor to growth. BAF continues to enrich its slate, entering new car financing in Q1FY24 and aiming for microfinance in Q4FY24 and tractor financing the following year.

Best-in-class asset quality: For the past decade, BAF has contained GNPA between 1.1% and 1.8%, achieving sub-1% levels in FY23. Considering its seasoned management team and disciplined record, we expect comfortable GNPA at 1%/1.3% and NNPA at 0.4%/0.5% for FY24/FY25 despite the planned entry into higher risk segments. Credit cost too has held below peers at 1.5% on average for FY13-FY19, though the Covid years were outliers before the company returned to form in FY23. We conservatively bake in a creeping rise in cost to 1.6%/1.7% for FY24/FY25.

Return ratios buoyant despite slim margins: Barring the turbulent Covid period, the company has delivered a consistent step up in return ratios over the past 10 years. Accounting for a rising cost of funds in a high rate environment, we project a 40bps fall in NIM from 10.6% in FY23 to 10.2% in FY25. Even so, ROAE is forecast to rise from 23.5% to 24.8% over the same period as rapid business expansion and cost control likely improve operating leverage and lower C/I ratio from 35.1% to 33.1%.

Valuations have moderated; BUY: BAF's veteran leadership team, diversified business model and effective execution should enable it to weather rising competition and fend off asset quality risks in proposed businesses such as microfinance. We, therefore, value the standalone business at 6.6x FY25E ABV – a 20% premium to the long-term average – for a value of Rs 8,619/sh. The addition of Rs 482/sh for housing arm BHFL (2x FY25E BV) and Rs 4/sh for securities subsidiary BFSL (15x FY25E EPS) yields an SOTP-based TP of Rs 9,105. We initiate coverage on BAF with a BUY rating for 29% upside from the current price.

Ticker/Price	BAF IN/Rs 7,163
Market cap	US$ 16.5bn
Free float	44%
3M ADV	US$ 84.3mn
52wk high/low	Rs 8,000/Rs 5,486
Promoter/FPI/DII	56%/20%/13%

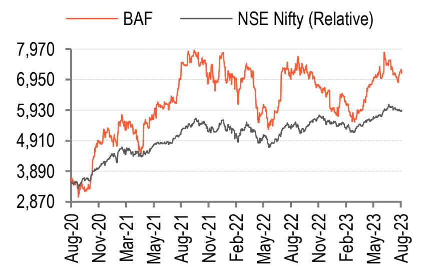
Source: NSE | Price as of 31 Aug 2023

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
NII (Rs mn)	2,29,903	2,85,451	3,63,124
NII growth (%)	31.2	24.2	27.2
Adj. net profit (Rs mn)	1,15,077	1,44,966	1,85,079
EPS (Rs)	189.6	238.7	304.8
Consensus EPS (Rs)	189.6	233.0	290.0
P/E (x)	37.8	30.0	23.5
P/BV (x)	8.0	6.5	5.3
ROA (%)	4.7	4.6	4.6
ROE (%)	23.5	23.9	24.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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Focus charts

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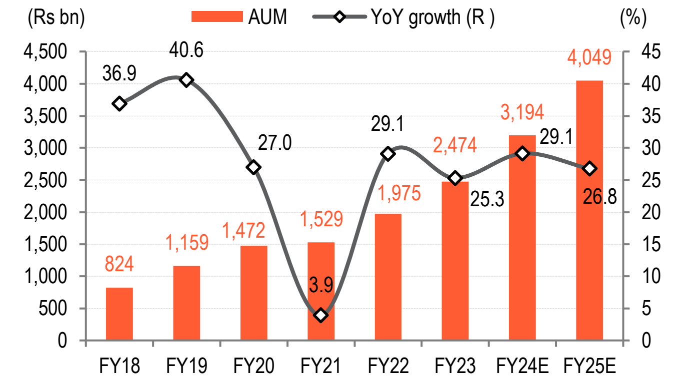
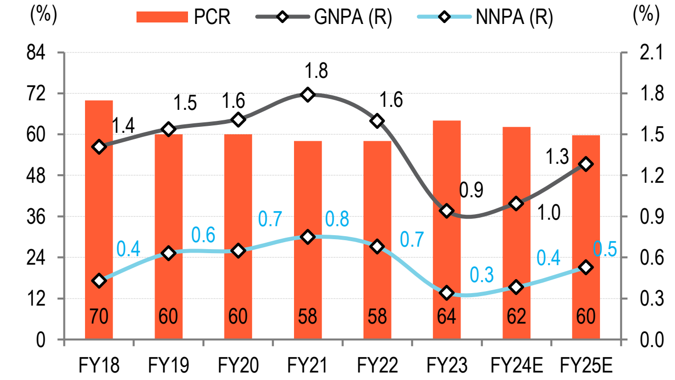


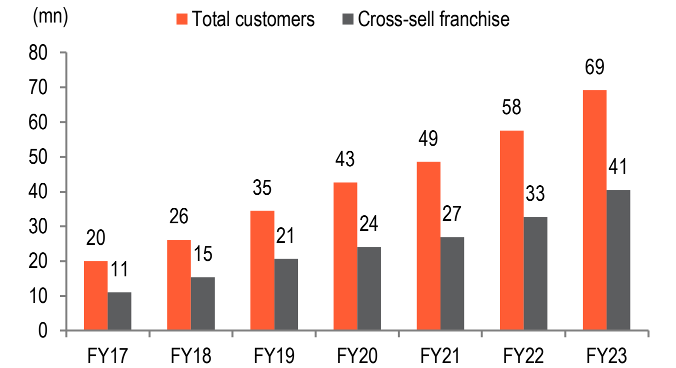
Source: Company, BOBCAPS Research

Fig 2 – …without compromising on asset quality



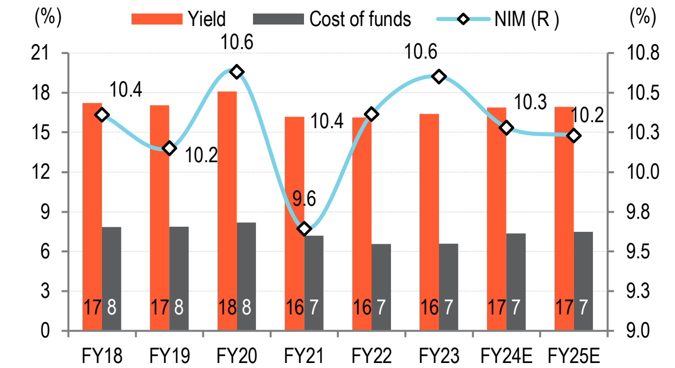
Source: Company, BOBCAPS Research

Fig 3 – Strong customer franchise



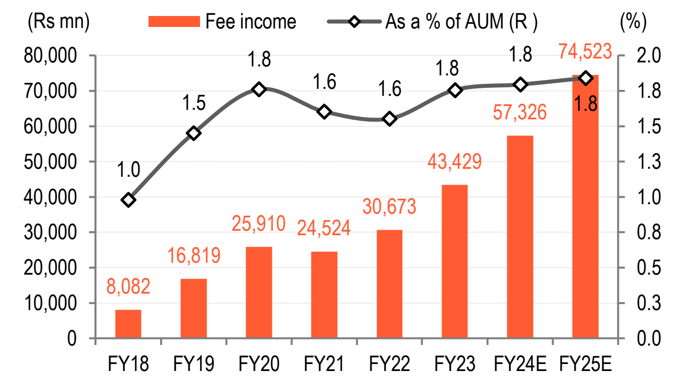
Source: Company, BOBCAPS Research

Fig 4 – Rising cost of funds to constrain NIM



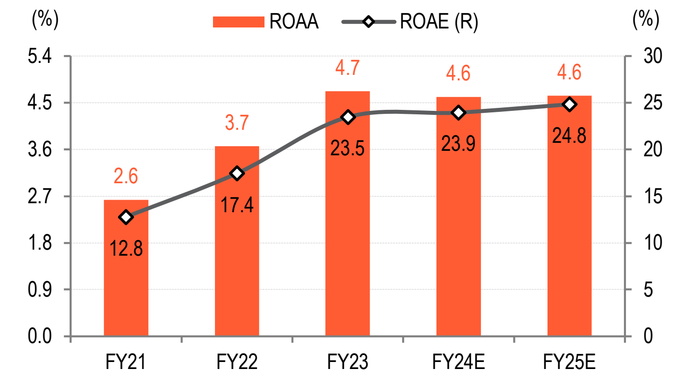
Source: Company, BOBCAPS Research

Fig 5 – High fee income led by credit card distribution and selling life insurance products



Source: Company, BOBCAPS Research

Fig 6 – …but business expansion, cost control to boost ROAE



Source: Company, BOBCAPS Research

Investment rationale

Diverse, fast-growing business model

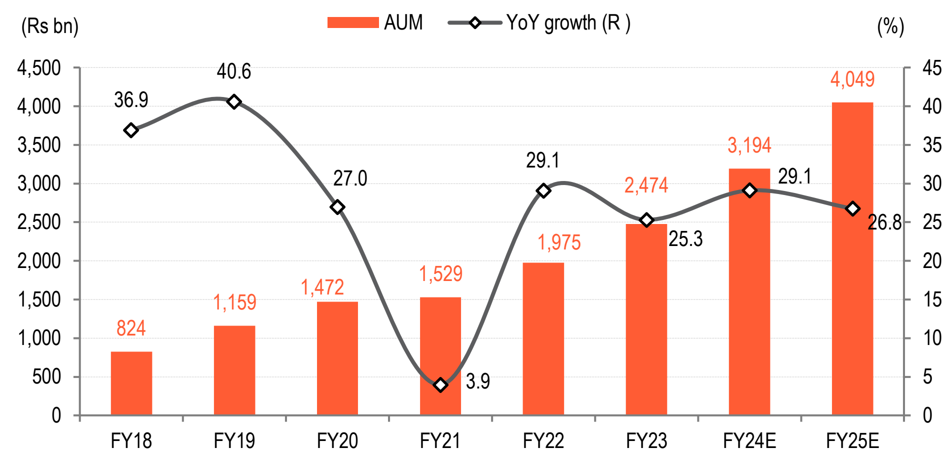
BAF, India's largest non-banking finance company, has clocked an impressive 30% AUM CAGR over the past decade (FY13-FY23) to Rs 2.5tn, accompanied by an even higher net profit CAGR of 35% to Rs 115bn. ROAE for the 10Y period has averaged 20% and GNPA has held under 2%, illustrating that asset quality has not been sacrificed at the altar of growth. Management has guided for a 29-31% rise in AUM during FY24 and a 25-27% increase in the long run. Considering BAF's diverse lending portfolio, solid execution record across businesses and headroom for market share gains in newer products, we model for a 28% AUM CAGR over FY23-FY25 to Rs 4tn.

Fig 7 – Solid growth metrics

Particulars	FY13	FY23	FY13-FY23 CAGR (%)
AUM (Rs bn)	175	2,473	30
Total income (Rs mn)	19,040	2,88,458	31
PPOP (Rs mn)	10,534	1,87,158	33
Net profit (Rs mn)	5,913	115,077	35

Source: Company, BOBCAPS Research | PPOP: Pre-Provision Operating Profit

Fig 8 – Robust AUM growth prospects

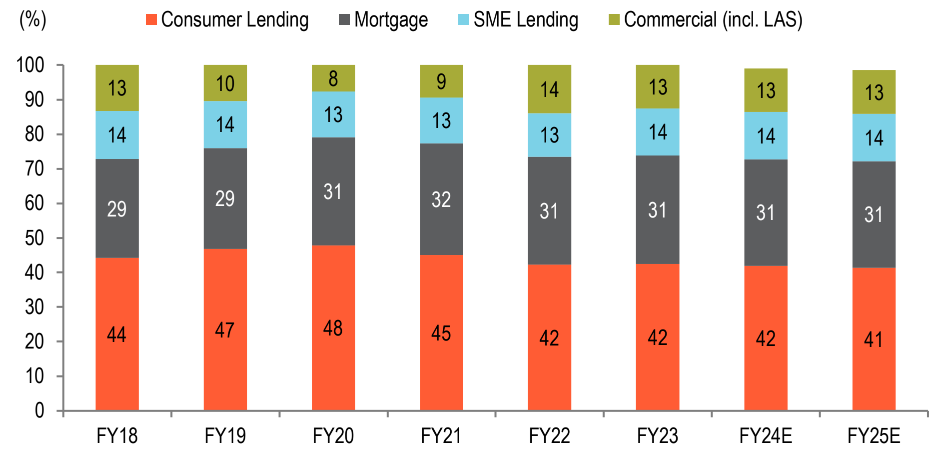


Source: Company, BOBCAPS Research

Broad product slate

BAF's AUM is diversified across the consumer, small & medium enterprise (SME), commercial and mortgage businesses. Consumer lending forms the largest chunk of the loan book at 42% of AUM in FY23 and is composed of the two-wheeler (2W) and three-wheeler (3W) finance that forms 5% of total AUM, B2B (9%) and B2C (28%) segments. Notably, rural loans in both the B2B and B2C categories make up 10% of the company's total AUM. The mortgage business is another pillar of growth at 31% of AUM, followed by SME (14%) and commercial (13%) lending.

Fig 9 – Diversified AUM



Source: Company, BOBCAPS Research | LAS: Loans Against Securities

Over the years, BAF has continually refreshed its product slate to service evolving demand, enabling a broadening of revenue streams and consumer reach. In Q1FY24, the company launched new car financing in 80 locations across India, building on its robust presence in the used car loan segment. Per management, the new car business could close FY24 at disbursements of Rs 2bn-2.5bn per month.

In FY23, the company introduced merchant QR code payments and in FY22, it forged strategic tie-ups with online vehicle marketplace Cars24 for end-to-end digital financing and with DBS Bank for co-branded credit card distribution, besides rolling out online payments interface 'Bajaj Pay'. A roadmap unveiled during Q3FY23 highlights management's plans to launch an array of products over the next two years, including microfinance in Q4FY24 and tractor financing in Q1FY25, along with new touchpoints.

Fig 10 – New business guidance put out in Q3FY23

Launch date	Planned product launches
Q2FY24	New auto loans (Launched in Q1FY24)
Q3FY24	Emerging corporate business
Q4FY24	Microfinance; B2B on QR and EDC; Flexi loans on QR; Insta PL card; Rewards as a platform
Q1FY25	Tractor financing
Q2FY25	Social as a platform
FY24-FY25	Open 100 locations in Uttar Pradesh, Bihar and North East in FY24 and another 100 locations in FY25

Source: Company, BOBCAPS Research | LAP: Loans Against Property; EDC: Electronic Data Capture; MSME: Micro, Small and Medium Enterprises; PL: Personal Loan

BAF offers both standard loans with predetermined repayment terms via equated monthly instalments and flexi loans with a credit line to borrowers allowing them to request funds as needed and pay interest only on the amount used. Per management, the latter product enjoys strong demand due to the twin benefits of affordability and flexibility. The company executed as many as 4.9mn flexi loans on its mobile app in FY23, up from 3.4mn in FY22.

Fig 11 – Product launches over the years stack up into a comprehensive product suite

Legacy	Two- and three-wheeler financing	Consumer durable financing					
FY08	Personal loan cross-sell	Life insurance distribution					
FY09, FY10	Loans against property	Loans against shares	Business loans	Vendor financing	Extended warranty cross-sell		
FY11	Home loans – self-employed	Loans against securities – Retail	Construction equipment financing				
FY12	SME cross-sell	Loans to professionals	Infrastructure financing	Co-branded credit card (Standard Chartered)	EMI card	Salaried personal loans	
FY13	Home loans – salaried	Lease rental discounting	Lifestyle product financing				
FY14	General insurance distribution	Crisil SME rating	Financial fitness report	Rural lending			
FY15	Digital finance	Property fitness report	MSME rural lending				
FY16	Urban gold loans	SME financial fitness report	Financial institutions lending business	Light engineering financing	Corporate finance	E-commerce- seller finance	
FY17	Co-branded card (RBL Bank)	Developer finance	Warehouse receipt financing				
FY18	Digital EMI card						
FY19	Used car financing	Secured enterprise loans	Specialty chemicals lending				
FY20	Health EMI card	IPO financing	ESOP financing				
FY21	Medical equipment financing	Digital deposit sourcing platform					
FY22	Strategic tie-up with Cars24 for end-to-end digital financing	Co-branded credit card (DBS Bank)	Bajaj Pay (PPI, UPI and BBPS)				
FY23	Merchant QR						
FY24 YTD	New car financing						

Source: Company, BOBCAPS Research | BBPS: Bharat Bill Payment System; EMI: Existing Member Identification; PPI: Prepaid Instruments; UPI: United Payments Interface

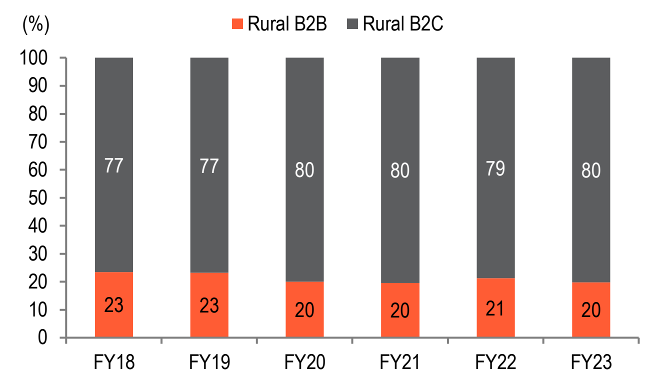
LEGEND	Retail / Consumer	Fee products	Commercial	SME	Rural	Payments	Closed

Consumer lending – steady growth trajectory

Consumer lending is BAF's biggest business, having logged a 24% CAGR between FY18 and FY23 to Rs 1tn, equating to 42% of AUM. The segment consists of two-wheeler (2W) and three-wheeler (3W) finance that forms 5% of total AUM, B2B sales finance both rural and urban (9%), and B2C finance both rural and urban (28%). BAF is seeing sustained momentum in urban and rural business led by its established position in the B2B sales finance category and growth in auto finance. We, thus, pencil in a 26% CAGR for the consumer lending business over FY23-FY25 to Rs 1.7tn (41% of AUM).

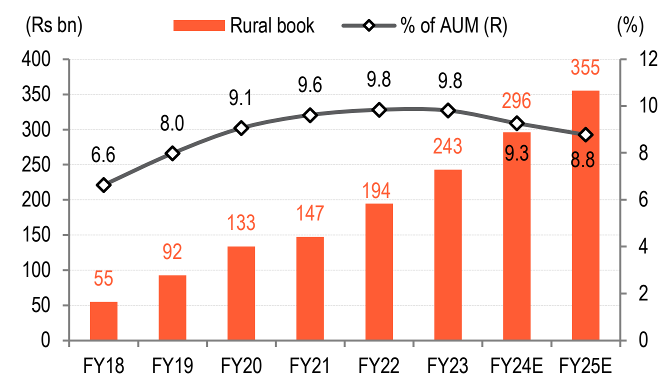
- **Urban business – strong brand recall:** BAF's urban business can be divided into two categories – (a) B2B lending (sales finance), which finances consumer durables, digital equipment and furniture, among other lifestyle goods; and (b) B2C lending, which provides loans to salaried, self-employed, professional and gold loan borrowers. Urban business recorded a 22% CAGR between FY18 and FY23, making up 27% of total AUM. Considering the company's strong brand recall and wide reach in major cities across the country along with India's growing young demographic, we bake in a 27% CAGR over FY23-FY25 to Rs 1.1tn.
- **Rural business – small but growing:** The rural business, which can also be split into the B2B sales finance and B2C segments, clocked a high 35% CAGR between FY18 and FY23, rising to 10% of total AUM. Growth was underpinned by BAF's presence in over 2,400 locations across 22 states and union territories, along with the addition of 2W finance to its portfolio in FY23. Weighing in these positives against the negatives of growing leverage in the B2C business and a Rs 2bn-2.5bn slowdown in monthly disbursals in Q1FY24, we project a 21% CAGR in rural lending AUM over FY23-FY25 to Rs 355bn.
- **B2B sales finance – a key client acquisition tool:** BAF has a longstanding position in the B2B sales finance category, where zero-cost EMI loans for gadgets such as smartphones serve as a significant client acquisition strategy. The company collaborates with retailers, who then give it discounted prices on goods in order to increase sales. BAF pays the discounted prices (compensates for loss in interest income) while offering the zero-cost installment payment option to buyers. Additionally, consumers pay processing costs to BAF. This strategy allows the company to expand its customer franchise and cross-sell other products, such as personal loans, through retailers.

Fig 12 – Rural AUM mix: B2C growth outpaces B2B



Source: Company, BOBCAPS Research

Fig 13 – Strong growth in rural AUM – a focus area



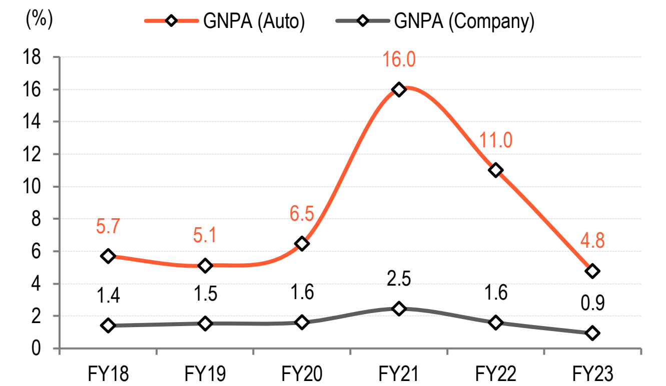
Source: Company, BOBCAPS Research

- **Auto finance – risky loans pared, shift to open architecture:** BAF's vehicle finance business has slashed GNPA from a peak of 16% in FY21 to 4.8% in FY23 by way of: (i) paring auto finance in total AUM from 8% to 5% over FY21-FY23; and (ii) established an open architecture model in 2W finance during FY23, against its earlier policy of funding vehicles manufactured only by parent Bajaj Auto (BJAUT).

  The company financed 57,500 non-BJAUT 2Ws in FY23 and expects to ramp up to 250,000-300,000 vehicles in FY24. It currently services 350 locations via 2,300 dealers largely in two states and aims to expand to 20 large cities and 227 small cities in India by the end of FY24, enrolling ~2,500 more dealers.

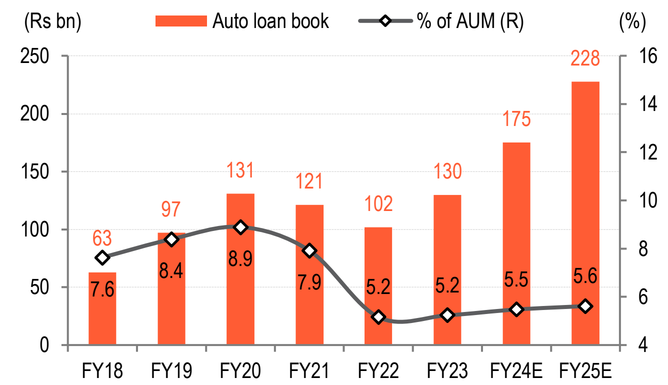
  We expect the switch to an open architecture model in tandem with network expansion to bolster growth prospects for the business. Following a 16% CAGR between FY18 and FY23, we model for 32% growth in auto finance over FY23-FY25 to Rs 228bn (5.6% of AUM). Although BJAUT has applied for an NBFC licence, we do not foresee a major reduction in business over the next couple of years as the proposed business will likely take a while to find its feet.

Fig 14 – Asset quality issues addressed in auto finance, albeit still higher than other businesses



Source: Company, BOBCAPS Research

Fig 15 – Auto loan book to grow at a fast pace, but a lower focus area for BAF



Source: Company, BOBCAPS Research

Mortgage business – the growth engine

BAF's mortgage business, which includes home loans, loans against property (LAP), developer financing and lease rental discounting (LRD), posted a strong 27% CAGR over FY18-FY23 to Rs 777bn, or 31% of total AUM. Barring FY21 when AUM dipped 7% YoY, the mortgage division has achieved consistent growth over five years backed by a well-diversified loan book.

In our view, the high-rate environment and climbing inflation are unlikely to constrict loan demand, due to low industry-level housing inventory and sustained offtake in the upper premium segment. At end-FY23, we estimate that BAF held ~2% market share in the mortgage business with an increasing trend and, thus, has sufficient headroom to expand operations even if growth is slow. We pencil in a 27% CAGR for the mortgage business to Rs 1.3tn over FY23-FY25.

In FY15, BAF established a housing finance subsidiary, Bajaj Housing Finance (BHFL), to house its mortgage business. By the end of FY23, BHFL was home to 87% of the company's mortgage activity.

Major components of the business include:

- **Home loans:** BHFL offers home loans to salaried customers for both ready and under-construction homes, with an average ticket size of Rs 5mn as of Q1FY24. The business is present in 59 locations across India.

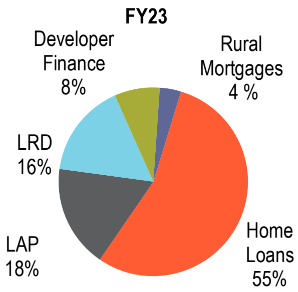
- **Loans against property:** SMEs, MSMEs (micro, small and medium enterprises), the self-employed and professionals can avail of LAP in exchange for the mortgage on their residential and commercial properties. The business is active in 27 locations in India, with loans averaging Rs.7mn as of Q1.

- **Lease rental discounting:** LRD loans range from Rs 100mn to Rs 5.5bn and are offered to high-net-worth individuals (HNI) and developers in 12 locations against rental income from commercial property leased to corporate lessees.

- **Developer loans:** Small and midsized developers with a track record of prompt project delivery and loan payback are eligible for construction and inventory financing from BHFL to the tune of Rs 50mn-5bn. The housing arm has a presence in 14 locations across the nation and leverages relationships with borrowers to also draw retail customers to its home loan product.

- **Rural mortgage:** BHFL provides loans secured by real estate to the salaried and self-employed across 109 rural Indian towns, with ticket size averaging Rs 1.7mn.

Home loans constitute a majority of mortgages



Source: Company, BOBCAPS Research

Fig 16 – BHFL houses 87% of the company's mortgage lending…

BHFL – Key metrics (Rs mn)	FY21	FY22	FY23
NII	11,890	16,120	24,540
Total operating expenses	3,290	4,710	6,300
Impairment on financial instruments	2,470	1,810	1,240
PAT	4,530	7,096	12,578
AUM	**3,88,710**	**5,33,220**	**6,92,280**
Housing loans (including top ups)	2,39,430	3,35,150	4,10,370
Loan against property	47,530	61,810	65,380
Lease rental discounting	48,380	72,240	1,12,600
Developer finance	20,570	28,750	60,260
Rural mortgage loans	19,800	19,230	25,920
Other loans	13,000	16,040	17,750

Source: Company, BOBCAPS Research

Fig 17 – …and enjoys low delinquencies

BHFL's segments	FY23			
	AUM (Rs mn)	GNPA (%)	NNPA (%)	PCR (%)
Home Loans	4,10,370	0.20	0.07	65
Loan against property	65,380	0.56	0.23	59
Lease rental discounting	1,12,600	-	-	-
Developer Finance	60,260	-	-	-
Rural Mortgages	25,920	1.15	0.43	62
Other loans	17,750	0.50	0.15	70
Total	**6,92,280**	**0.22**	**0.08**	**64**

Source: Company, BOBCAPS Research

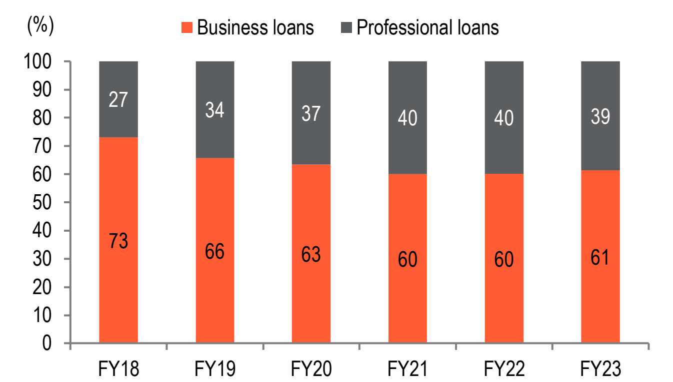
SME lending – focus on professionals paying off

SME lending, which predominantly caters to small firms, recorded a 24% CAGR to Rs 338bn over FY18-FY23, accounting for 14% of BAF's total AUM. A distinctive feature of this business is that it also provides secured and unsecured loans to professionals, including chartered accountants and doctors, in over 1,800 locations across India. Products consist mainly of working capital loans and term loan facilities.

- **Unsecured loans:** In FY23, the AUM of unsecured loans to professionals increased by 27% YoY to Rs 119bn. Medical equipment financing that was launched in FY21 began to take off last fiscal thanks to field distribution and buildup of a medical OEM and dealer network. The company now has 19 OEMs for sourcing and more than 450 empanelled dealers. This business provides a support function for professional loans that saw AUM surge 124% to Rs 3.1bn in FY23.
- **Secured loans:** BAF accepts home property, business property and used four-wheelers as collateral for the secured loans it offers to SME and MSME customers. AUM of loans secured against real estate, whether residential or commercial, swelled 80% YoY to Rs 33bn in FY23, whereas used auto finance assets soared 136% YoY to Rs 28bn, thanks to the subsidiary's expanded presence across 50 locations from 28 in FY22.

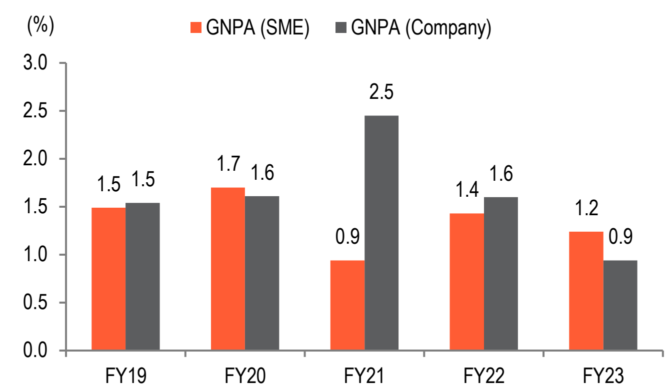
At the end of FY23, BAF had ~1% market share in the SME business as per our estimates. We forecast a 28% CAGR for the company's SME financing segment over FY23-FY25 to Rs 555bn (13.7% of AUM), owing to strong growth trends and pristine asset quality. In addition to cross-sell opportunities, we see sizeable potential for growth in the professional category which has held at ~40% of the lending mix for the past three years vs. 27% at the end of FY18. Further, the company's flexi loan offering, where customers can avail of funds only as needed and thus save on interest, should continue to draw business.

Fig 18 – Professional loans a sizeable chunk of SME mix



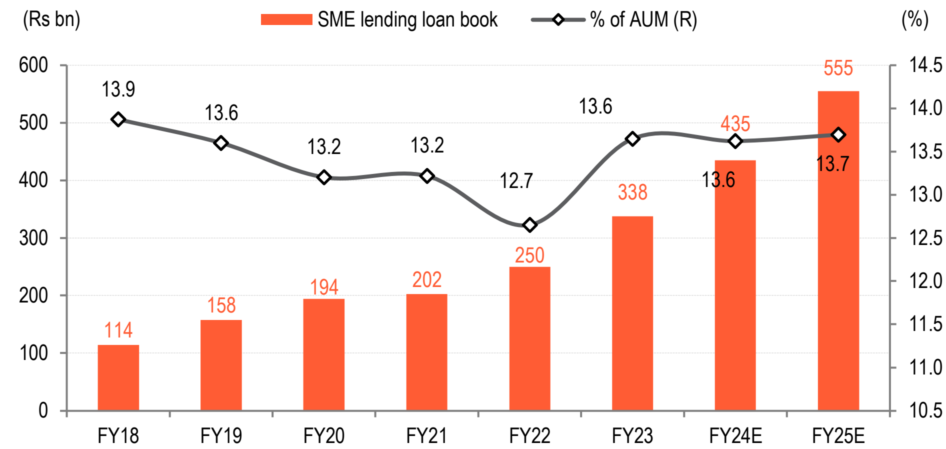
Source: Company, BOBCAPS Research

Fig 19 – SME business enjoys strong asset quality



Source: Company, BOBCAPS Research

Fig 20 – Strong momentum in SME lending to continue



Source: Company, BOBCAPS Research

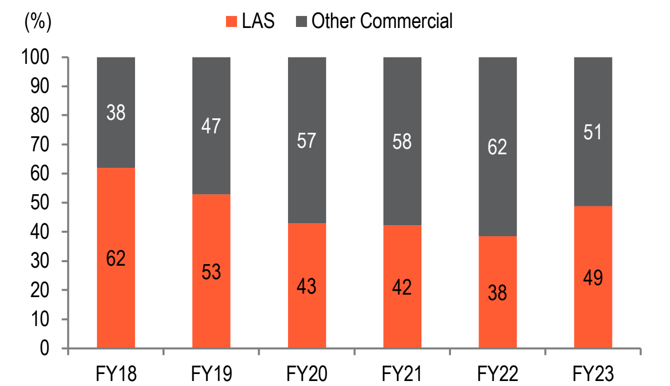
Commercial lending – LAS propelling growth

The commercial lending business comprises high-ticket loans to prime-rated borrowers with GNPA less than 0.3% and NNPA less than 0.2%. Borrowers include financial institutions, specialty chemical and pharmaceutical industries, car component manufacturers, the light engineering industry, and other midmarket businesses. This apart, customers in the retail, HNI and promoter categories are offered medium- and short-term financing against shares, bonds, mutual funds and insurance policies, as well as deposits by the company's loans against securities (LAS) segment.

LAS contributed 49% of segmental AUM in FY23 vs. 38% in FY22. While the AUM contribution from commercial lending tends to fluctuate, we believe the LAS segment will support a 28% CAGR for the business over FY23-FY25 from Rs 309bn to Rs 511bn (vs. a 23% CAGR for FY18-FY23), continuing to form 13% of AUM.

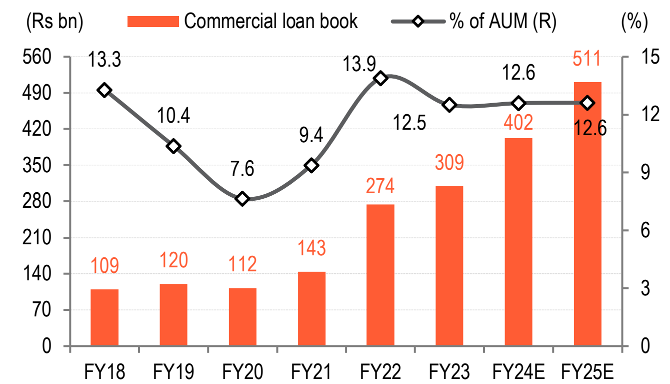
BAF operates physical branches in 22 locations and provides financing through digital channels as well. In addition to its own lending operations, 100% subsidiary, Bajaj Financial Securities (BFSL), provides a broad range of products to HNI and retail clients, including demat services, brokerage and margin trade financing.

Fig 21 – LAS formed higher share of commercial book during FY23



Source: Company, BOBCAPS Research

Fig 22 – Commercial loan book growing but volatile as a proportion of AUM



Source: Company, BOBCAPS Research

Customer base ramping up

BAF has ramped up to 69mn customer accounts (end-FY23) compared to 20mn serviced in FY17, backed by distribution network expansion and productive cross-selling initiatives. Management expects to add 12-13mn new customers during FY24. Although the company faces intensifying competition from banks, NBFCs and new entrants (such as Jio Financial Services), we anticipate limited headwinds considering its strong brand image, innovative product lineup and impressive record on growth and asset quality.

Strong cross-selling franchise

BAF emphasises cross-sales of loans to credit-worthy customers who have a history of on-time payback in any of its verticals. To this end, it has created a data analytics platform that evaluates client data and assists in the creation of new loan products and the sales of existing ones across users. Already, 41mn customer accounts (59% of total) formed part of the company's cross-sell franchise at end-FY23. The number of new loans booked has thus been rising at a steady pace, tripling to 30mn as compared to 10mn at end-FY17.

Fig 23 – Cross-sell initiatives yielding results

Particulars	FY17	FY18	FY19	FY20	FY21	FY22	FY23
Total customers (mn)	20	26	35	43	49	58	69
- Cross-sell franchise (mn)	11	15	21	24	27	33	41
AUM per cross-sell franchise (Rs)	54,722	53,417	56,066	60,983	56,879	58,617	60,991
PAT per cross-sell franchise (Rs)	1,670	1,618	1,933	2,182	1,644	2,145	2,837
New loans booked (mn)	10.1	15.3	23.5	27.4	16.9	24.7	29.6
New customer addition (mn)	4.1	6.1	8.3	8.1	6	9	11.6
Existing customer mix (%)	59.8	60.3	64.8	70.4	64.6	63.5	60.9

Source: Company, BOBCAPS Research | Note: For the existing customer mix, we have divided New Customer Addition by New Loans Booked and subtracted the result from 100%

Wide distribution

At end-FY23, BAF's geographical footprint stood at 3,700+ locations and more than 154,000 distribution points across India. The company added ~230 branches in FY23 (95 in Q1FY24) and has guided for the opening of 100 more in Uttar Pradesh, Bihar and the northeast in FY24 and another 100 locations in FY25.

Fig 24 – Expanding distribution network

Particulars	FY21	FY22	FY23
Consumer durable stores - Urban	26,400+	30,600+	33,950+
Consumer durable stores - Rural	24.000+	29,800+	37,000+
Digital product stores	23,800+	29,500+	33,000+
Lifestyle retail stores	9,800+	11,000+	13,200+
EMI card - retail spends stores	14,300+	18,800+	22,200+
BJAUT dealers, sub-dealers & associates	5,900+	6,000+	5,150+
Non-captive 2W dealers, sub-dealers & associates	-	-	2,650+
(DSA)/Independent financial agents	6,100+	7,500+	7,500+
Overall active distribution network	**1,10,300+**	**1,33,200+**	**1,54,650+**
Net addition in the period	(4,100)	22,900	10,750

Source: Company, BOBCAPS Research | DSA: Direct Selling Agent

Omnichannel strategy to spur growth

The company drafted an omnichannel strategy in FY20 to spur sustainable growth. Major initiatives over the past two years include:

- Revamp of the customer-facing **mobile app** with a new interface, in-app programs, rewards and offers, along with the provision of services via parent Bajaj Finserv's app that saw 58mn statements of account read, shared and downloaded in FY23
- Buildout of a full-service **payments** business, comprising a robust payments stack that encompasses wallets, united payments interface (UPI), a bill pay service and a single payment checkout gateway
- Transformation of the customer **web experience** to offer a consistent experience across app and web that will drive traffic, business volumes and customer service
- Launch of the **Sales One app** (to equip sales teams with capabilities such as lead management and customer service) and the **Debt Management One app** (to equip debt management teams with features like mobile receipting and settlement workflow)
- Introduction of a **customer data platform** that enables multi-channel customer communication, call governance and a multi-lingual architecture.

Fig 25 – Omnipresence metrics: Momentum across geographies & digital channels

Particulars	Q1FY23	Q4FY23	Q1FY24	YoY (%)
Geography*				
New locations added (Nos.)	82	19	95	NA
Locations - Cumulative (Nos.)	3,586	3,733	3,828	242
Gold loan branches - Cumulative (Nos.)	155	181	424	269
App Metrics				
Downloads (mn)	11.0	13.4	15.1	37
Net Installs - Cumulative (mn)	23.0	35.5	40.2	75
In App programs - Cumulative	62	104	118	90
Ranking in financial domain in Playstore	6	5	5	↑
Service requests initiated on app (% of total)	15	26	34	↑
App Payments Metrics				
UPI handles - Cumulative (mn)	3.6	13.0	15.5	329
Bill pay transactions (mn)	2.1	5.3	5.4	164
QRs at merchant PoS - Cumulative (mn)	0.02	0.6	1.1	NA
Rewards issued (mn)	4.8	13.5	18.1	277
App business metrics				
EMI cards acquired on App ('000)	69	99	123	78
Personal loans disbursed on App (Rs bn)	21	26	28	31
Credit card acquisition on App ('000)	30	72	77	157
Flexi loan transactions on App (mn)	0.9	1.6	1.7	95
DMS receipts on App ('000)	644	972	982	52
Marketplace metrics				
Bajaj Mall visits (mn)	31.8	47.1	49.0	54
Bajaj Mall loans ('000)	645	607	826	28
Insurance Bazaar policies ('000)	9.5	107.6	112.0	1,079
Investments Bazaar MF A/C ('000)	10.0	23.6	25.4	154
Digital EMI card metrics				
EMI cards acquired digitally ('000)	522	598	665	27
EMI cards acquired digitally - CIF (mn)	2.3	3.6	3.8	65
B2B loans from digital EMI cards ('000)	227	291	416	83

Source: Company | CIF: Cards in Force; DMS: Debt Management Services; EMI: Existing Member Identification; PoS: Point of Sale; UPI: Unified Payment Service

Jio Finance unlikely to erode customer base

After spinning off from behemoth Reliance Industries, Jio Financial Services (JFS) listed on the exchanges on 21 Aug 2023. The business seeks to offer a variety of financial services, such as loans, payment services, payment banking, insurance brokerage, and asset management.

In the initial stages, JFS plans to offer financing solutions for consumer durables and electronics, later adding secured loans. Financing options for retailers in the food, digital, fashion, and pharma industries will be included in the merchant loan category, whereas the MSME category would provide working capital funding.

Although a few of these segments would be in direct competition with BAF, and RIL's plan to tap its 450mn Jio telecom subscribers and ~20,000 Reliance Digital outlets to build its own NBFC is a good one, we believe the scope to supercharge growth at JFS will be constrained by tough competition and high collection costs. Further, the high-growth unsecured loan business could prove challenging for a new NBFC entrant owing to the poor credit history of customers in the segment.

Fig 26 – JFS: Consolidated P&L

(Rs mn)	FY23
Interest income	383.4
Dividend income	2.7
Net gain on fair value changes	30.2
Total revenue from operations	**416.3**
Other Income	32.1
Total Income	**448.4**
Other expenditure	55.6
Operating profit	**392.8**
Reversal of ECL & contingent provision on standard assets	100.6
Profit before tax	493.4
Total Tax expense	180.9
PAT	**312.5**

Source: Company, BOBCAPS Research | ECL: Expected Credit Loss

Fig 27 – JFS: Consolidated balance sheet

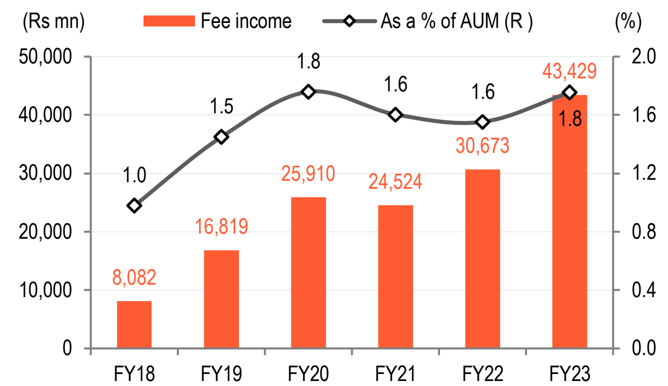
(Rs mn)	FY23
Loans	411
Investments	10,81,409
Goodwill and Intangible assets	1,565
Other assets	65,910
Total Assets	**11,49,296**
Total Equity	11,41,203
Borrowings	7,428
Other Liabilities	665
Total Liabilities and Equity	**11,49,296**

Source: Company, BOBCAPS Research

Fees a core component of growth

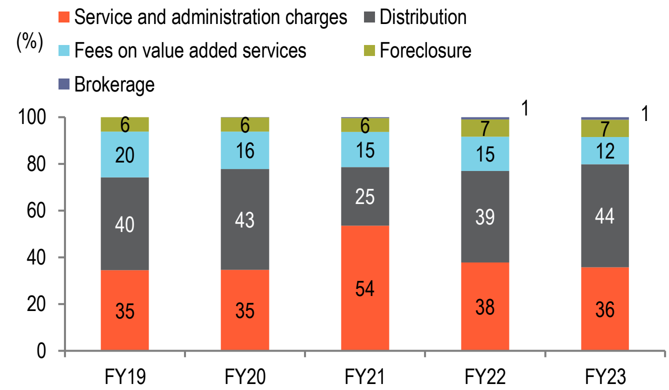
Fee income is a key component of BAF's strategy and has increased at a 40% CAGR over FY18-FY23, outpacing the company's 25% AUM CAGR for this period and climbing from 1% of AUM to 1.8% at Rs 43.4bn. We note that not all fee income components are correlated with an increase in AUM – for instance, annual fees from BAF's existing member identification (EMI) card and distribution fees from co-branded credit cards, both of which are based on consumer spending. Indeed, our analysis shows that credit card cross-sales have been among the key growth drivers of fees.

Fig 28 – Fee income growth higher than AUM growth



Source: Company, BOBCAPS Research

Fig 29 – Constituents of fee income



Source: Company, BOBCAPS Research

Credit card and life insurance cross-selling a money-spinner

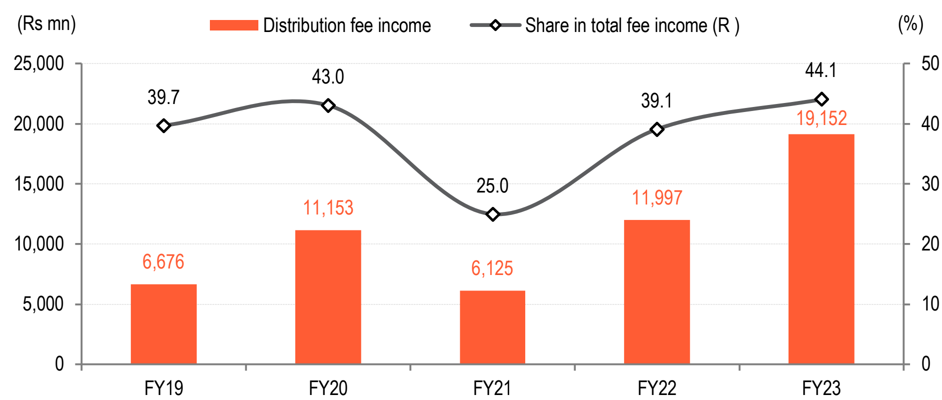
BAF has partnered with RBL Bank to offer co-branded credit cards for which it receives fee income. Although the company does not disclose its commercial agreements, we believe fee income depends on this arrangement as, barring a dip in FY21, distribution income has accounted for ~40% of fee income over the past five years. The company has recently partnered with DBS Bank to sell its co-branded credit cards as well. Selling cards and distributing life insurance products generate most of its distribution income.

Fig 30 – Credit card sales gaining pace

Particulars	FY17	FY18	FY19	FY20	FY21	FY22	FY23
Co-branded credit cards sold (mn)	0.03	0.39	0.81	1.12	0.70	1.36	1.92

Source: Company, BOBCAPS Research

Fig 31 – Distribution income an important constituent of fee income

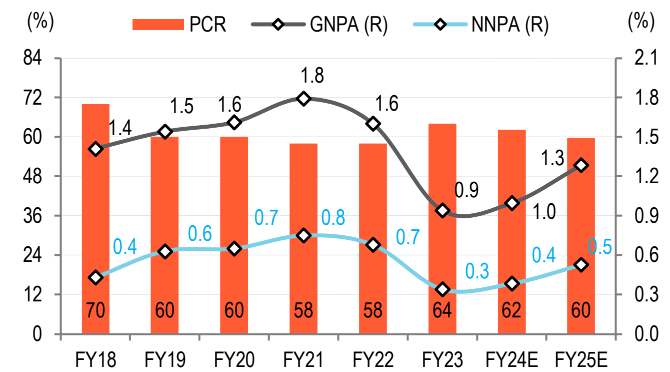


Source: Company, BOBCAPS Research

Asset quality robust

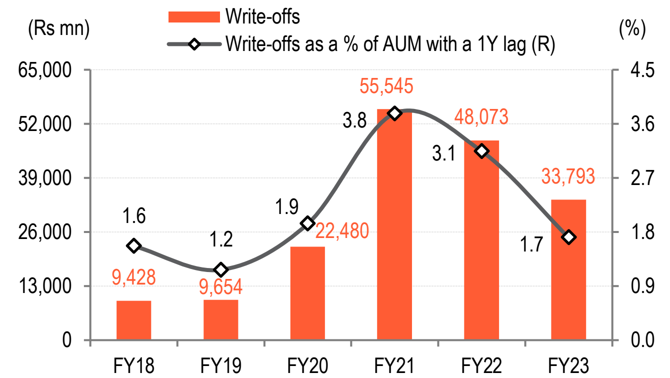
BAF has maintained impeccable asset quality, with GNPA ranging from 1.1% to 1.8% of advances over the past 10 years and dropping below 1% in FY23, indicating a robust operational ecosystem with stringent risk management. A rising share of mortgage lending has helped pare asset quality risk. For FY24/FY25, we forecast comfortable levels of 1%/1.3% for GNPA and 0.4%/0.5% for NNPA.

Fig 32 – Strong asset quality



Source: Company, BOBCAPS Research

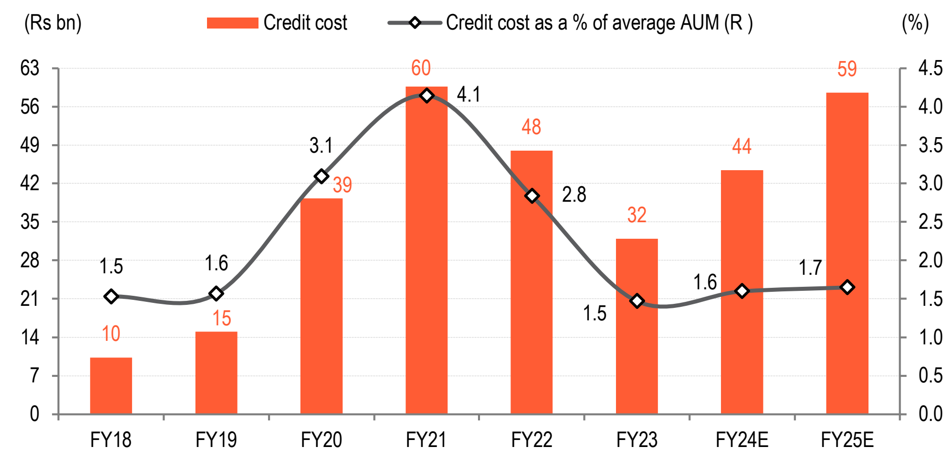
Fig 33 – Write-offs normalising after Covid-led spike



Source: Company, BOBCAPS Research

After spiking to 3.1% in FY20 and 4.1% in FY21, the company's credit cost has normalised at 1.5% of advances in FY23, in line with the long-term average. On a conservative basis, we model for credit cost of 1.6% for FY24 – in keeping with management guidance of 155bps-165bps – and 1.7% for FY25.

Fig 34 – Credit cost returning to historical levels



Source: Company, BOBCAPS Research

We acknowledge that BAF's new product lineup, including plans to introduce microfinance loans in the last quarter of FY24, entails risks to asset quality but do not foresee a serious threat over the medium term considering the company's robust risk management record and nascent share of new businesses in total AUM.

Fig 35 – Portfolio credit quality – Stage-2 assets (where loan credit risk has risen significantly since initial recognition) the highest in 2W and 3W financing

Particulars	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24
Stage 1									
Consumer Durables & Lifestyle	99.1	99.6	99.7	97.9	99.7	99.6	99.6	99.6	99.6
Two & three-wheelers	71.1	77.8	82.9	85.2	86.0	89.3	91.7	93.3	94.3
Digital products	98.7	99.6	99.7	99.7	99.5	99.5	99.6	99.5	99.5
Urban B2C	95.2	97.4	98.2	98.5	98.6	98.8	98.7	98.8	98.7
Business & professional loans	97.3	98.5	98.7	98.9	99.0	99.1	99.1	99.3	99.3
Rural B2B	98.9	99.6	99.8	99.8	99.7	99.6	99.7	99.6	99.7
Rural B2C	95.5	94.5	95.8	97.8	98.1	97.9	98.0	98.1	98.0
Loans against property	97.9	96.2	97.2	98.6	98.4	98.6	98.8	98.8	98.9
Home loans	98.3	99.1	99.1	99.6	99.4	99.4	99.5	99.6	99.4
Stage 2									
Consumer Durables & Lifestyle	0.7	0.3	0.2	0.3	0.3	0.3	0.3	0.3	0.4
Two & three-wheelers	16.4	12.7	11.0	8.7	8.4	6.3	5.2	4.2	3.7
Digital products	1.0	0.3	0.2	0.3	0.5	0.4	0.3	0.4	0.5
Urban B2C	3.8	2.1	1.4	1.3	1.2	1.0	1.0	1.0	1.0
Business & professional loans	2.0	1.0	0.9	0.7	0.6	0.6	0.4	0.4	0.4
Rural B2B	0.8	0.2	0.1	0.2	0.2	0.3	0.2	0.3	0.3
Rural B2C	3.6	4.2	2.7	1.8	1.7	1.7	1.6	1.6	1.7
Loans against property	1.3	2.7	1.8	0.8	1.0	0.9	0.7	0.7	0.7
Home loans	1.4	0.7	0.6	0.2	0.4	0.4	0.3	0.3	0.4

Source: Company, BOBCAPS Research

Fig 36 – Stage-wise expected credit loss (ECL) provisioning

Consolidated (Rs bn)	Gross Assets Receivable			ECL Provision			Provision Coverage Ratio (PCR) (%)		
	Stage 1	Stage 2	Stage 3	Stage 1	Stage 2	Stage 3	Stage 1	Stage 2	Stage 3
Two & three-wheeler finance	122	7	6	1	1	3	1.0	19.7	50.5
Urban sales finance	176	1	1	1	1	1	0.6	46.5	77.3
Urban B2C	485	8	5	6	3	3	1.3	39.5	74.6
Rural sales finance	48	0	0	0	0	0	0.4	51.0	77.6
Rural B2C	194	4	2	3	1	1	1.4	31.3	71.3
SME lending	338	3	4	4	1	3	1.1	46.6	75.0
Loan against securities	151	0	0	0	-	-	0.1	4.5	11.0
Commercial lending	158	0	0	0	-	0	0.2	0.1	47.7
Mortgages	741	7	5	4	2	3	0.6	22.4	57.4
Total as of 31 Mar 2023	**2,413**	**30**	**23**	**20**	**9**	**15**	**0.8**	**30.8**	**63.8**

Source: Company, BOBCAPS Research

High, sustainable return ratios; sturdy balance sheet

Except for the Covid-hit years of FY21-FY22, the company has consistently improved return ratios over the past decade, crossing 20% in FY23 while maintaining leverage well below peers. We model for a further increase in ROAE from 23.5% in FY23 to 24.8% in FY25 as rapid business expansion and cost control likely offsets a higher cost of funds.

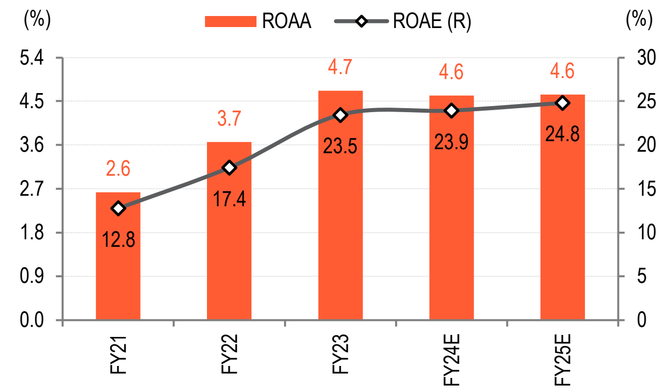
BAF's balance sheet has logged a high 31% CAGR between FY13 and FY23, but the company has demonstrated fiscal prudence, maintaining an average assets-to-equity leverage ratio of 5.7x, marked by a high of 6.8x and a low of 4.6x. This disciplined approach also enabled it to weather the turbulent Covid period. This apart, it remains well capitalised and has no pressing need to raise funds to meet regulatory requirements.

Fig 37 – Peer comparison (FY23): BAF generated high ROE of >20% with significantly lower leverage than peers

Particulars	BAF	POONAWAL	CIFC	SHTF	MMFS	HDFC	MGFL
Loan book* (Rs bn)	2,423	152	1,048	1,787	865	6,246	342
NII/Average assets* (%)	9.4	6.2	6.5	9.2	7.3	2.0	11.6
GNPA (%)	0.9	1.4	4.6	6.2	4.5	1.2	1.3
NNPA (%)	0.3	0.8	3.1	3.2	1.9	0.7	1.1
Leverage (Total assets/Total equity)* (x)	5.1	3.4	7.9	4.8	5.6	5.1	4.1
CAR (%)	25.0	38.9	17.1	22.6	22.5	24.3	32.0
ROAE* (%)	23.5	8.8	20.4	17.3	11.7	13.6	16.7

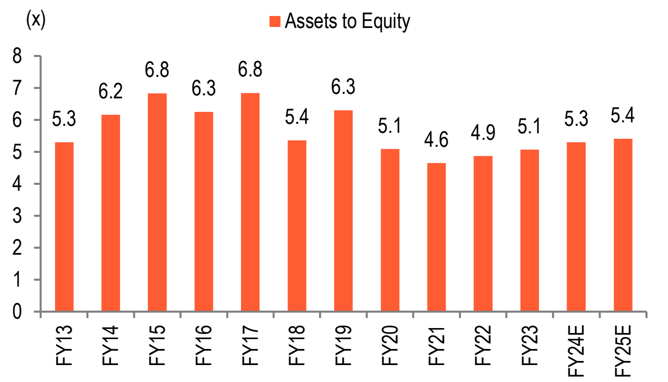
Source: Company, BOBCAPS Research | *Consolidated data | Note: HDFC has been merged with HDFC Bank with effect from 1 Jul 2023

Fig 38 – Return ratios likely to improve further



Source: Company, BOBCAPS Research

Fig 39 – Stable leverage



Source: Company, BOBCAPS Research

Strong parent, seasoned management

Financial services conglomerate Bajaj Finserv holds a 52.5% stake in BAF, giving the latter access to the parent's financial and operational support as well as brand equity. Additionally, BAF is one of the key players in the group's financial services businesses, and its recognized history of profitable growth increases the strategic significance of the company. Founded in 1926, the Bajaj group is a respected brand across India, in turn contributing to the recognition and growth of BAF's business.

Fig 40 – Strong parentage

Stake held (%)	Mar-23	Mar-22	Mar-21
Bajaj Finserv	52.5	52.5	52.7
Other promoters	3.4	3.4	3.4
Total promoters	**55.9**	**55.9**	**56.1**
FIIs	19.2	21.4	24.1
DII	12.9	11.2	9.1
Others	12.0	11.5	10.7

Source: Company, BOBCAPS Research

BAF's management team stands out for both its quality and longevity. Rajeev Jain has been MD and CEO since 2007, helming the company's swift expansion, and the senior management team includes several longstanding members, which helps ensure business stability. As part of the announced succession plan, Anup Saha and Rakesh Bhatt have been appointed as executive directors of the company. It has been indicated that Mr Jain will assume larger responsibilities within the organisation after handing over the reins in a few years. For key management team details, see Annexure A.

Fig 41 – Top management snapshot

Name	Designation	Joined BAF	Total experience (years)
Rajeev Jain	MD & CEO	2007	~30
Sandeep Jain	CFO	2008	~17
Anup Saha	Executive Director	2017	~30
Rakesh Bhatt	Executive Director	2009	~30
Fakhari Sarjan	Chief Risk Officer	2018	~30
Anupam Sirbhaiya	Chief Human Resources & Administrative Officer	2019	~29
Deepak Bagati	President - Debt management	2008	~30
Anand Bagri	Treasurer	2022	~22

Source: Company, BOBCAPS Research

Financial review

Robust AUM growth momentum

BAF delivered a strong 25% AUM CAGR to Rs 2.5tn over FY18-FY23 (32% YoY in Q1FY24). We expect broad-based business growth to spur a 28% AUM CAGR to Rs 4tn over FY23-FY25 vs. management guidance of 25-27% long term.

As discussed earlier, we forecast a 26% CAGR to Rs 1.7tn in the consumer lending business, within which the auto finance/rural/urban segments are likely grow at 32%/ 21%/27%. SME financing is anticipated to post a 28% CAGR to Rs 555bn backed by professional loans and the flexi scheme. Similarly, commercial lending, which is a big-ticket business with strong asset quality credentials, is projected to rise at 28% to Rs 511bn. In mortgages, low industry inventories and demand from the upper premium segment are likely to support a 27% run-rate to Rs 1.3tn.

Fig 42 – Growth expected to be spread across segments

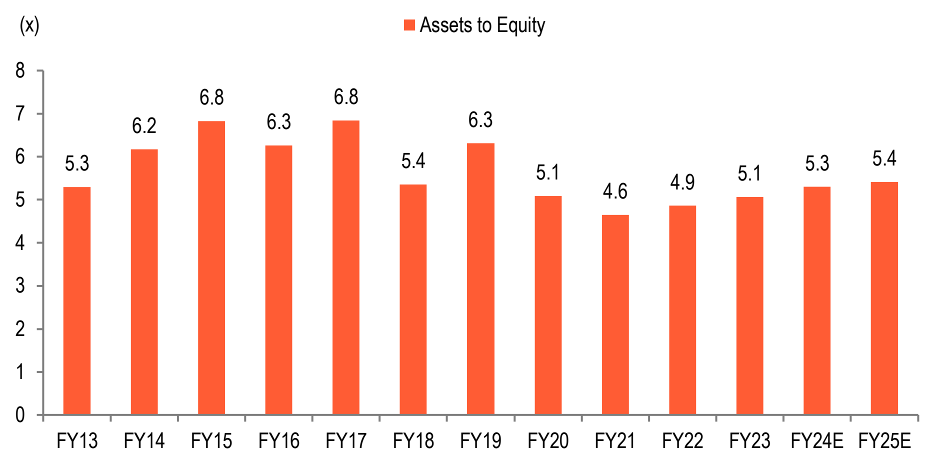
Business segment (Rs bn)	FY23	FY25E	FY23-FY25E CAGR (%)
Consumer Lending	1,050	1,674	26.3
SME Lending	338	555	28.2
Commercial (incl LAS)	309	511	28.5
Mortgage	777	1,251	26.9
New segments	-	60	NA
Total	**2,474**	**4,049**	**27.9**

Source: Company, BOBCAPS Research

Stable leverage

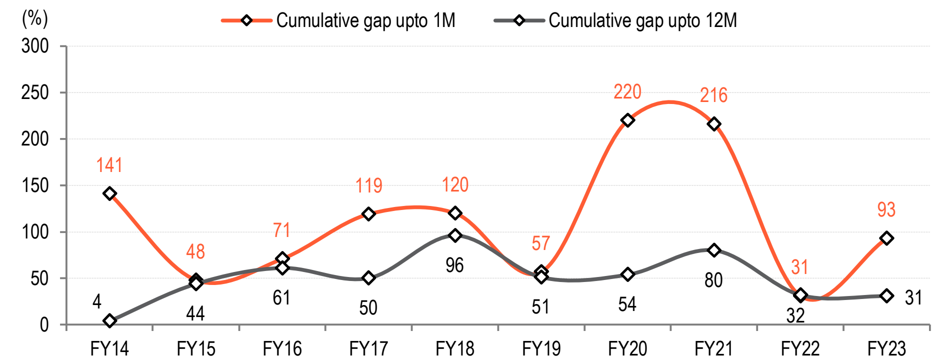
Despite a 31% CAGR in balance sheet size between FY13 and FY23, BAF has confined its leverage below 7x with an average assets-to-equity ratio of 5.7x. Moreover, the company practices careful asset liability management (ALM) and remains well capitalised. The business has received long-term rating of AAA/Stable from CRISIL, India Ratings, CARE and ICRA.

Fig 43 – Steady leverage ratio



Source: Company, BOBCAPS Research

Fig 44 – Disciplined ALM



Source: Company, BOBCAPS Research

Fig 45 – ALM, FY23

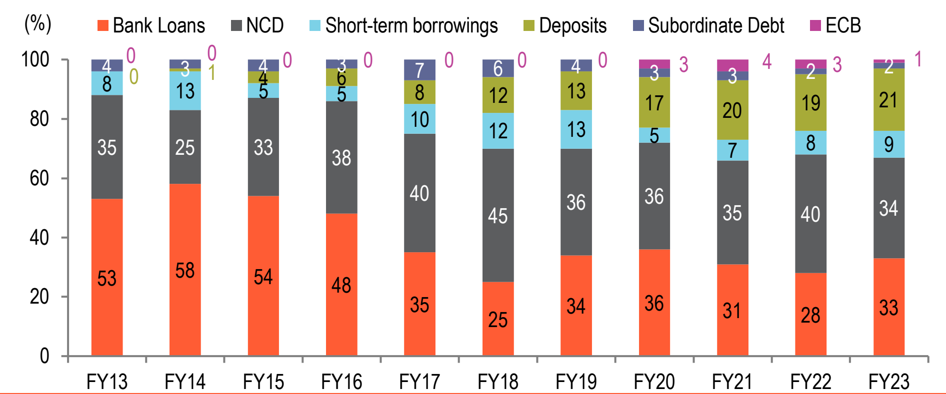
Particulars (Rs bn)	1-7D	8-14D	15-30D	>1-2M	>2-3M	>3-6M	>6M-1Y	>1-3Y	>3-5Y	>5Y	Total
Cash & Investments	66.5	93.7	16.8	0.1	0.4	2.3	3.1	32.8	12.5	92.3	320.4
Advances	60.0	19.6	44.4	82.2	76.0	190.5	286.2	673.5	238.1	158.8	1,829.3
Other inflows	51.0	1.3	1.7	5.1	4.9	1.5	1.8	7.3	6.2	35.2	116.1
Total Inflows (A)	**177.5**	**114.6**	**62.9**	**87.3**	**81.3**	**194.3**	**291.1**	**713.6**	**256.9**	**286.3**	**0.0**
Cumulative Total Inflows (B)	**177.5**	**292.1**	**355.0**	**442.4**	**523.6**	**717.9**	**1,009.0**	**1,722.7**	**1,979.5**	**2,265.8**	**2,265.8**
Borrowings	102.0	21.4	18.6	67.8	84.5	114.3	298.0	571.4	216.5	184.2	1,678.6
Capital Reserves and Surplus	0.0	-	-	-	-	-	-	-	-	514.9	514.9
Other Outflows	22.1	3.4	17.0	16.0	1.0	0.4	3.4	2.6	3.0	3.5	72.3
Total Outflows (C)	**124.1**	**24.7**	**35.6**	**83.8**	**85.5**	**114.7**	**301.4**	**574.0**	**219.5**	**702.6**	**2,265.8**
Cumulative Total Outflows (D)	**124.1**	**148.8**	**184.4**	**268.2**	**353.6**	**468.3**	**769.7**	**1,343.7**	**1,563.2**	**2,265.8**	**0.0**
Mismatch (E = A-C)	53.4	89.9	27.4	3.6	(4.2)	79.6	(10.3)	139.6	37.4	(416.4)	0.0
Cumulative mismatch (F = B-D)	53.4	143.3	170.6	174.2	170.0	249.6	239.4	379.0	416.4	-	0.0
Cumulative mismatch as % (F/D)	43.0	96.3	92.6	65.0	48.1	53.3	31.1	28.2	26.6	0.0	-

Source: Company, BOBCAPS Research

Diversified borrowing mix

Despite focusing on deposits and non-convertible debentures (NCD) to raise funds, BAF has a well-diversified borrowing mix. Bank loans stood at 33% of liabilities at the end of FY23 as opposed to 58% in FY14. Deposits account for 21% of the mix, up from 1% a decade ago, demonstrating the benefits of being an AAA-rated NBFC. The proportion of NCDs in the liability mix has averaged at 36% over the last five years.

Fig 46 – NCD and bank loans combined constitute two-thirds of liability mix

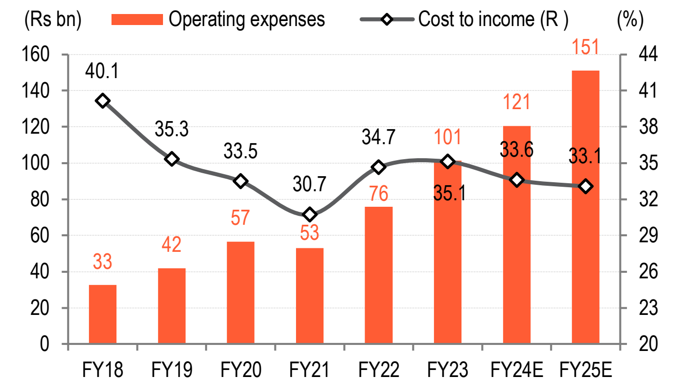


Source: Company, BOBCAPS Research

Cost-to-income ratio to moderate

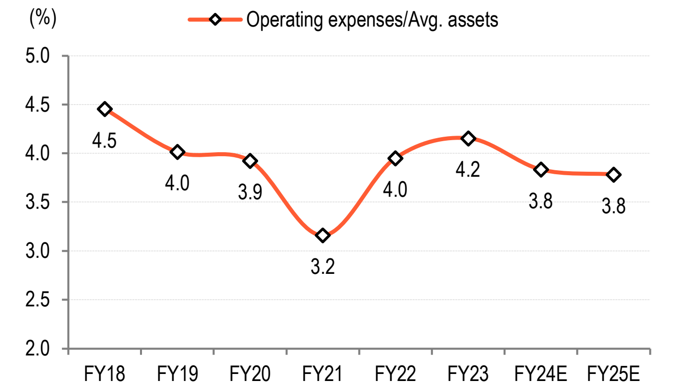
BAF's C/I ratio stood at 35.1% in FY23 after averaging at 34.9% over FY18-FY23. We expect a decline to 33.6%/33.1% in FY24/FY25 as operating leverage kicks in. For our model, we bake in a CAGR of 23% in employee expenses to Rs 76bn (rising to 51% of total expenses), 22% in other expenses to Rs 40bn (26% of total), and 17% in fees and commissions to Rs 26bn (17% of total).

Fig 47 – C/I ratio to decline…



Source: Company, BOBCAPS Research

Fig 48 – …which is reflected in other cost ratios too

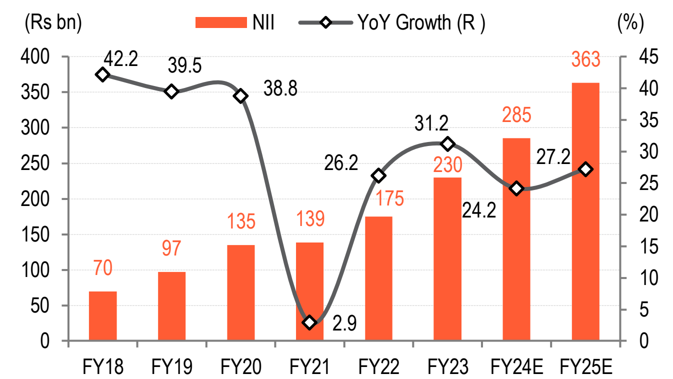


Source: Company, BOBCAPS Research

NIM to remain under pressure…

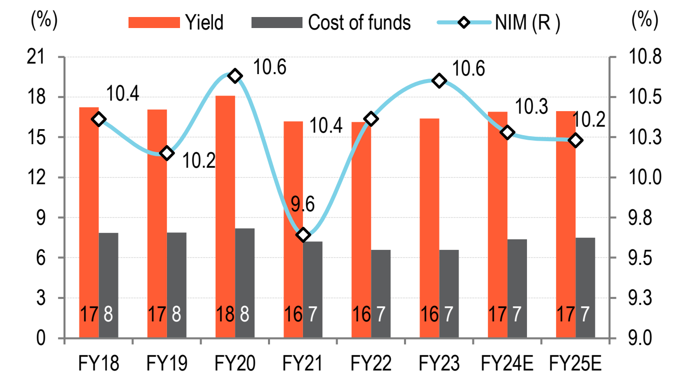
Given the diversity of business operations, BAF generates a blended yield of 16-18%. The SME and consumer businesses deliver strong yields whereas mortgage is on the relatively lower side. The company has been able to maintain NIM in the range of 10-10.5% for the past 10 years. Due to interest reversals and slower AUM growth in FY21, NIM fell to 9.6% but recovered in FY22 (10.4%) and FY23 (10.6%). We expect some compression to 10.3%/10.2% in FY24/FY25 as a result of a higher cost of capital in a rising rate environment. NII is forecast to clock a 26% CAGR over FY23-FY25 to Rs 363bn.

Fig 49 – Expect a 26% NII CAGR



Source: Company, BOBCAPS Research

Fig 50 – Margin forecast reflects higher cost of capital

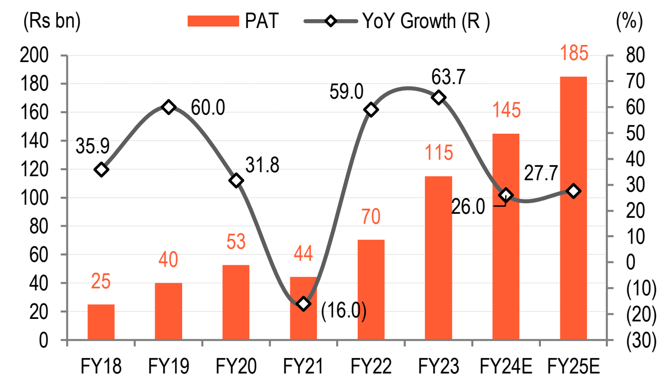


Source: Company, BOBCAPS Research

…but return ratios sustainable

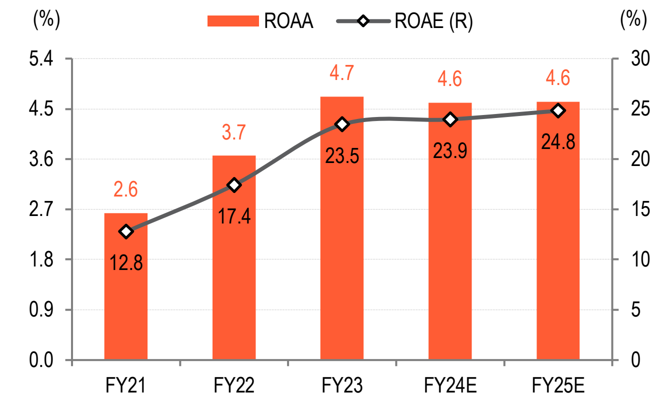
Rapid business expansion and cost control should enable BAF to improve its return ratios. Baking in the normalising credit cost, we project ROE of 23.9%/24.8% for FY24/FY25 vs. 23.5% in FY23. We bake in a PAT CAGR of 27% over FY23-FY25 to Rs 185bn as compared to the 36% run-rate over FY18-FY23 that came off a lower base.

Fig 51 – PAT projected to clock a 27% CAGR



Source: Company, BOBCAPS Research

Fig 52 – Return ratios to improve further



Source: Company, BOBCAPS Research

Q1FY24 commentary upbeat

During BAF's Q1FY24 earnings call, management raised full-year AUM growth guidance from a band of 27-29% to 29-31% and estimated that 12-13mn customers would be added during the year. AUM is guided to increase 25-27% long term, and management highlighted an upbeat outlook on the new car financing and gold loan businesses. BAF expects cost of funds to rise gradually in FY24 before easing in FY25, and credit cost, which stood at 168bps in Q1, to clock in at 155-165bps for FY24.

On the asset quality front, a management overlay provision of Rs 1.2bn was released in Q1 due to higher ECL provisioning of Rs 350mn; a one-time provision of Rs 150mn towards the Manipur portfolio, which is under moratorium due to social unrest in the state; and ECL model redevelopment costs of Rs 500mn. Management further indicated that personal loans and rural B2C loans were exhibiting high leverage and preemptive actions were underway to remedy the situation.

Potential conversion to a bank – Key implications

Our estimates indicate that BAF's AUM of Rs 2.5tn (FY23) will reach Rs 4tn by FY25. In order to bring large NBFCs such as BAF into compliance with some of the stricter regulations covering banks, the RBI classified the company along with 15 others as an "upper layer (UL)" NBFC effective Oct'22, from among four layers of base, middle, upper and top. This means BAF must now function within a new, stringent regulatory framework, much like a bank. Moreover, being the country's largest NBFC, it is possible the central bank will encourage BAF to convert to a bank in future, inviting even stricter oversight. While management has refuted such speculation, we outline the regulatory implications below.

Upper layer NBFCs attract stricter regulation

Key regulations applying to NBFC-UL and above:

- Exposure to a single counterparty must not exceed 20% of the NBFC-UL's available capital base at all times, though the board may allow an additional 5% exposure subject to some conditions. Exposure to a group of connected counterparties shall not be higher than 25%.
- To enhance the quality of regulatory capital, common equity tier-1 capital must be at least 9% of risk weighted assets.
- Differential provisioning must be held for different classes of standard assets.
- Stipulations prescribed for NBFC-UL must be implemented within 24 months of classification in the upper layer. The enhanced regulatory provisions will continue for at least five years from such classification, even if the company does not meet the criteria in subsequent years.

Stricter regulations that cover banks (but do not apply to NBFC-UL):

- **Statutory requirements:** A bank must maintain a 4.5% cash reserve ratio (CRR: cash reserves parked with the RBI) and an 18% statutory liquidity ratio (SLR: reserves of liquid assets, which include cash, government securities and gold). CRR does not earn any interest, whereas SLR earns 6-7%.
- **Priority sector lending (PSL):** The RBI requires that PSL form at least 40% of a bank's adjusted net bank credit (ANBC). The objective is enable access to credit to certain sections that are otherwise unable to tap the formal financial/banking system. These sectors, however, aren't always economically lucrative.
- **Internal systems:** A bank must have a core banking system and other compliance controls in place, which entails additional expenses in terms of IT systems and manpower costs.

We believe conversion to a bank could prove detrimental to profitability and, hence, BAF is better placed in its current form as a large NBFC.

Valuation

Initiate with BUY, TP Rs 9,105

BAF continues to derive benefits from a diverse product basket, wide distribution network, effective execution and seasoned management team. With the exception of FY21 and FY22, when operations were affected by transient Covid-related concerns, the company has routinely earned ROE of 20% or higher, alongside impressive asset quality. Businesses such as retail finance continue to enjoy structural drivers, such as a young population and rising per capita income in India, and we project a robust 28% CAGR in loans for the company over FY23-FY25.

Over the last decade, the stock has traded at an average of 5.5x one-year forward ABV on a standalone basis and 4.8x on a consolidated basis. Considering BAF's solid fundamentals and robust growth prospects, we value the standalone business at 6.6x (16% below it's 5-year mean) FY25E ABV – a 20% premium to its long-term average – yielding a value of Rs 8,619/sh. The addition of Rs 482/sh for housing arm BHFL (2x FY25E BV) and Rs 4/sh for securities subsidiary BFSL (15x FY25E EPS) yields an SOTP-based TP of Rs 9,105. We find current valuations compelling and initiate coverage on BAF with a BUY rating for a 29% upside from the current price.

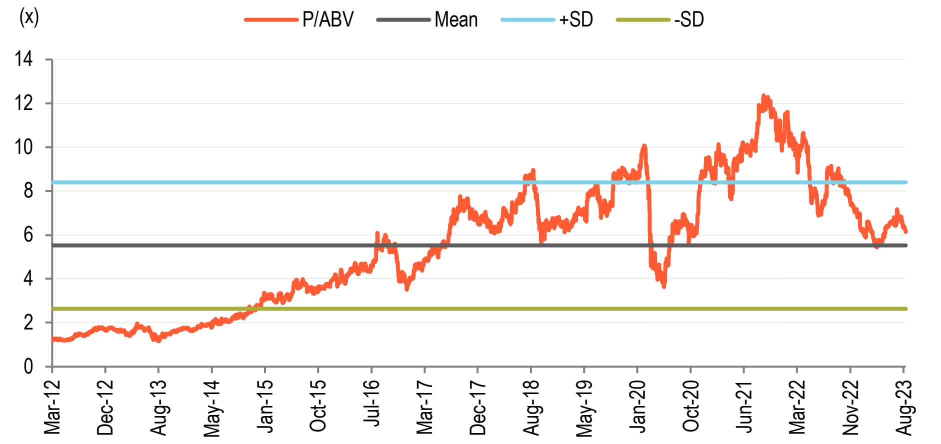
While we acknowledge recent investor concerns about potential risks to BAF's growth and asset quality in the face of intense competition (from both banks and NBFCs) and new business forays, these worries appear unfounded given management's established risk credentials and deep expertise in allied lending segments. We would look for new product rollout and business developments before revisiting our estimates.

Fig 53 – SOTP valuation

FY25E	Stake (%)	(Rs bn)	(Rs/share)	Valuation basis
Value of Bajaj Finance (Standalone)	**-**	**5,372**	**8,619**	6.6x P/ABV FY25E
Subsidiaries valuation	-	**295**	**486**	-
Bajaj Housing Finance (BHFL)	100	293	482	2x P/BV FY25E
Bajaj Financial Securities (BFSL)	100	2	4	15x P/E FY25E
Value of Bajaj Finance (Consolidated)	**-**	**5,667**	**9,105**	-
Final value (consolidated)	-	-	9,105	-
Current Market Price	-	-	7,163	-
Upside/(Downside) (%)	-	-	29%	-

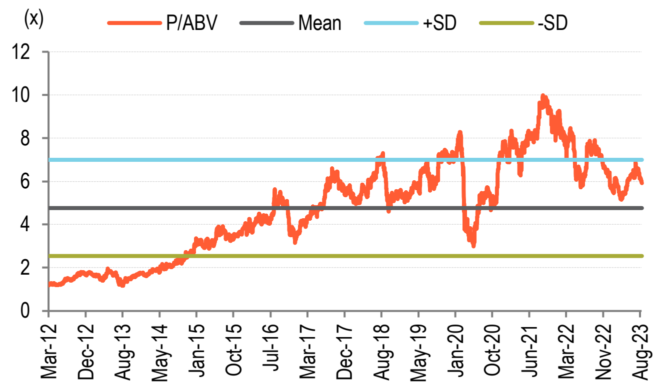
Source: BOBCAPS Research

Fig 54 – P/ABV 1Y fwd: Stock trading close to mean (standalone)



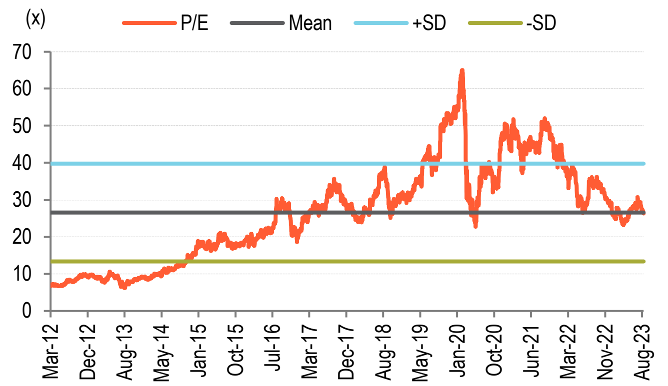
Source: Bloomberg, BOBCAPS Research

Fig 55 – P/ABV 1Y fwd: Stock trading at +1SD (consolidated)



Source: Bloomberg, BOBCAPS Research

Fig 56 – P/E 1Y fwd: Stock trading close to mean (consolidated)



Source: Bloomberg, BOBCAPS Research

Scenario analysis

We have conducted a scenario analysis to assess the impact of changes in AUM vis-à-vis our estimates. Our valuation model (base case) assumes a 27.9% AUM CAGR over FY23-FY25 to Rs 4tn, with a 25.7%/26.8% NII/PAT CAGR. For our bull and bear scenarios, we assume a 20% increase and decrease in AUM respectively from the base.

- In the **bull case**, a 33.5% AUM CAGR over FY23-FY25 will lead to a 31.3% PAT CAGR to Rs 199bn and a 31.2% CAGR in NII, with a 150bps rise in ROE to 26.3% from the base case. Here, we assume that both C/I ratio and loan loss provisions are identical to the base case.
- In the **bear case**, a 22.4% AUM CAGR over FY23-FY25 will lead to a 22.5% PAT CAGR to Rs 173bn and a 130bps drop in ROAE to 23.5% from the base case. Assuming NIM is constant in both base and bear scenarios, NII will grow at a rate of 20.2% for our forecast years vs. the base case rate of 25.7%.

Fig 57 – Scenario analysis

FY23-FY25E CAGR (%)	Base	Bear	Bull
AUM growth	27.9	22.4	33.5
NII growth	25.7	20.2	31.2
Total income growth	25.9	21.5	30.3
Total opex growth	22.2	18.0	26.4
Loan loss provision growth	35.5	30.6	39.8
PAT growth	26.8	22.5	31.3

Source: BOBCAPS Research

Key risks

- **Intensifying competition:** Based on a wide product suite, solid execution capabilities, and robust demand for credit in its target industries, we expect BAF to achieve 20%+ loan growth in the medium term. Above-expected competition, particularly from banks and other financial institutions, could weigh on the company's performance, affecting our earnings, margin and valuation assumptions.
- **Deteriorating asset quality:** Between FY19 and FY23, BAF's GNPA and NNPA averaged just 1.5% and 0.6% respectively. Asset quality may decline as a result of slow economic growth or the recurrence of a pandemic (such as Covid).
- **Higher delinquency in new segments:** The company has announced plans to enter the higher risk microfinance and tractor financing markets in Q4FY24 and Q1FY25 respectively. These businesses could pose risks to asset quality.
- **Regulatory headwinds:** According to the RBI's scale-based NBFC framework published in 2022, BAF (along with 15 others) has been classed as an upper layer NBFC that must adhere to enhanced regulation. It cannot, for instance, lend more than 20% to one entity and more than 25% to a group of entities. In future, the RBI may even direct the company to transition from an NBFC into a bank, which would entail maintaining CRR, SLR and PSL – strictures that NBFCs aren't subject to and which would impact profitability.

Annexure

A: Key management personnel

- **Sanjiv Bajaj** is the Chairman of BAF and is also on the board of group operating companies. He is a member of the board of the Indian School of Business (ISB); the International Advisory Board (IAB); Allianz SE; the International Technology Advisory Panel (ITAP) of Monetary Authority of Singapore (MAS); and the Regional Stewardship Board for India and South Asia 2019- 2020 of the World Economic Forum. He was President of the Confederation of Indian Industry (2022-23) and a member of the steering committee appointed by the Indian government for B20 as part of India's G20 presidency.

  Sanjiv has a bachelor's degree in Mechanical Engineering from the University of Pune, a master's in Manufacturing Systems Engineering from the University of Warwick, UK, and a master's in Business Administration from Harvard Business School, US.

- **Rajeev Jain** is Managing Director and CEO, helming BAF's executive management team. He joined the company in 2007 as Chief Executive Officer and has over three decades of experience managing diverse consumer lending businesses, including auto loans, durable loans, personal loans and credit cards.

  Prior to BAF, he was associated with GE, American Express and the American International Group (AIG). Rajeev is a management graduate from the T.A. Pai Management Institute, Manipal with a bachelor's degree in Commerce from the American College, Madurai.

- **Anup Saha** is an Executive Director of BAF and a member of its executive management team. He joined the company in 2017 and leads its consumer finance portfolio business. He heads all the retail business lines, including urban consumer durable loans, personal loans, co-branded credit cards, SME, rural loans, fixed deposits, insurance, and payments.

  Prior to BAF, Anup was with ICICI Bank as Senior General Manager and Group Product Head of retail home loans, vehicle loans, developer funding, and retail and rural collections. He worked with ICICI Bank for 14 years across different roles and also served on the board of the bank's HFC and TU CIBIL and its Sales CRM and Big Data transformation projects. In his earlier stints, he worked with GE Capital International Services (GECIS), SBI Cards, Blow Past and BHEL. He is an alumnus of IIT Kharagpur and IIM Lucknow.

- **Rakesh Bhatt** is an Executive Director of BAF and a member of the executive management team. He joined the company in 2009 and was Chief Operating Officer until 2018, leading a large portfolio of critical functions, including technology, analytics, credit operations, customer experience and quality.

  Rakesh was the CEO of Bajaj Finserv Direct for four years and spearheaded the launch of a diversified digital marketplace business (Bajaj Markets) in financial services and e-commerce. In his earlier assignments, Rakesh has held leadership positions in AIG Consumer Finance, GE Money, Reliance Industries and 3i Infotech. He has a master's degree in Computer Applications (M.Sc.)

- **Sandeep Jain** is BAF's Chief Financial Officer and joined the company in 2008 to set up the management accounting practice. Over the years, he has held multiple roles across strategic planning, CEO's office, and financial planning & analysis, besides heading the business reengineering and investor relations functions. He started his professional journey in the internal audit function of BJAUT, handling audits in the areas of materials, system, finance, and indirect taxation.

  At BAF, he currently oversees finance, treasury, financial planning and analysis. Sandeep is a Chartered Accountant from ICAI with a bachelor's degree in Commerce from Nagpur University.

- **Madhur Bajaj** is a Director and Non-Executive Vice-Chairman of BJAUT – recently declared the world's most valuable two-wheeler company. He is also involved with other Bajaj group companies (BAF, Bajaj Finserv, Bajaj Electricals, BHIL) as a director on the board. After obtaining his bachelor's degree in Commerce, he earned his MBA at the International Institute of Management Development (IMD), Lausanne, Switzerland.

  In the past, Madhur has served as President of the Chamber of Marathwada Industries and Agriculture, Mahratta Chamber of Commerce, Industries and Agriculture, the apex chamber of Pune, Society of Indian Automobile Manufacturers, and Confederation of Indian Industry (western region). He is a National Council Member of the Confederation of Indian Industry (CII).

- **Rajiv Bajaj** is a Director of BAF and Managing Director of BJAUT. He has worked at BJAUT in the areas of manufacturing, supply chain (1990-95), R&D and engineering (1995-2000), and marketing and sales (2000-05), and has been the Managing Director since Apr'05 and a board member since Mar'02.

  Rajiv graduated in Mechanical Engineering from the University of Pune and went on to a master's in Manufacturing Systems Engineering from the University of Warwick.

- **Radhika Haribhakti** is an Independent Director with over three decades of experience in commercial and investment banking with Bank of America, JM Morgan Stanley and DSP Merrill Lynch. She offers advisory services at RH Financial but primarily serves as an independent director on multiple corporate boards. She is on the board of directors of ICRA, EIH Associated Hotels, Navin Fluorine International, Pipeline Infrastructure, Rain Industries and Torrent Power.

  Radhika is the former Chair of Friends of Women's World Banking (FWWB) and Swadhaar Finaccess. She has also served on the Governing Council of Citigroup Micro Enterprise Award and CII's National Committee on Women Empowerment. She is a graduate in Commerce from Gujarat University and a post graduate in Management from IIM, Ahmedabad.

B: Company profile

Bajaj Auto Finance, a deposit-taking NBFC established in 1987, was rechristened Bajaj Finance (BAF) in 2010 and is a fully owned subsidiary of financial services conglomerate Bajaj Finserv. BAF has an AUM of Rs 2.5tn at end-FY23, serves more than 69mn clients and offers a wide range of lending services to retail, SME and commercial customers across urban and rural India. BAF has two wholly owned subsidiaries: Bajaj Housing Finance (BHFL) and Bajaj Financial Securities (BSFL).

Business lines

BAF offers consumer, mortgage, SME and commercial loans; deposits; and partnerships and services, as outlined below:

a) The **consumer lending** vertical provides financing to salaried and self-employed individuals for the following products:

- **2W (motorcycle) and 3W (auto-rickshaw) loans** for vehicles manufactured by BJAUT (recently began financing other brands as well)
- **Consumer durable loans** for television sets, air conditioners, refrigerators, washing machines and other household electronic appliances
- **Lifestyle product loans** for products such as furniture, modular kitchens and luxury watches
- **Digital product loans** for mobile phones, laptops and other electronic devices
- **EMI cards** for existing customers that have a durables loan, lifestyle product loan or digital product loan, enabling them to avail of incremental loans in these segments
- **Personal loans** to existing customers with timely repayment track records for their short- and medium-term requirements
- **Salaried personal loans** to affluent salaried customers and **salaried home loans** for financing the purchase of residential property

b) **SME lending** offers secured and unsecured loans (working capital and term facilities) to small businesses such as SMEs, MSMEs and professionals. Secured loans to SME and MSME customers are offered against their residential property, commercial property or used four-wheelers. The company has also entered a tie-up with online car marketplace Cars24 to provide an end-to-end digital financing experience for customers transacting on the Cars24 platform.

c) **Commercial lending** consists of lending to auto component manufacturers and the light engineering industry, loans to financial institutions, the specialty chemical and pharmaceutical industry, and other midmarket companies.

d) **Rural lending** includes consumer B2B lending, personal loans, gold loans, and retail deposits in small towns and villages. This vertical was launched in 2013.

e) **Deposits:** BAF accepts deposits from retail and corporate clients and continues to raise funds in a calibrated manner.

f) **Partnerships and services:** The company offers a variety of products to customers, such as life insurance, health insurance, extended warranty, comprehensive asset care, co-branded credit cards and financial fitness reports.

- BAF is registered with Insurance Regulatory and Development Authority (IRDA) as a corporate agent for the distribution of life, health and general insurance products across nine insurance partners. Together with various insurance companies, it has developed a small-ticket insurance product called ‘pocket insurance’ for specific customer needs.
- The company also distributes comprehensive asset care products to its B2B customers, providing features such as extended warranty, theft cover, breakage cover and replacement cover of their purchased products.
- Co-branded credit cards are offered in partnership with RBL Bank and DBS Bank.

Collateral

BAF offers both unsecured loans and loans secured by collateral. Although collateral is an important mitigant of credit risk, the company’s practice is to lend based on an assessment of the customer’s ability to repay rather than placing primary reliance on collateral.

Fig 58 – Collateral data

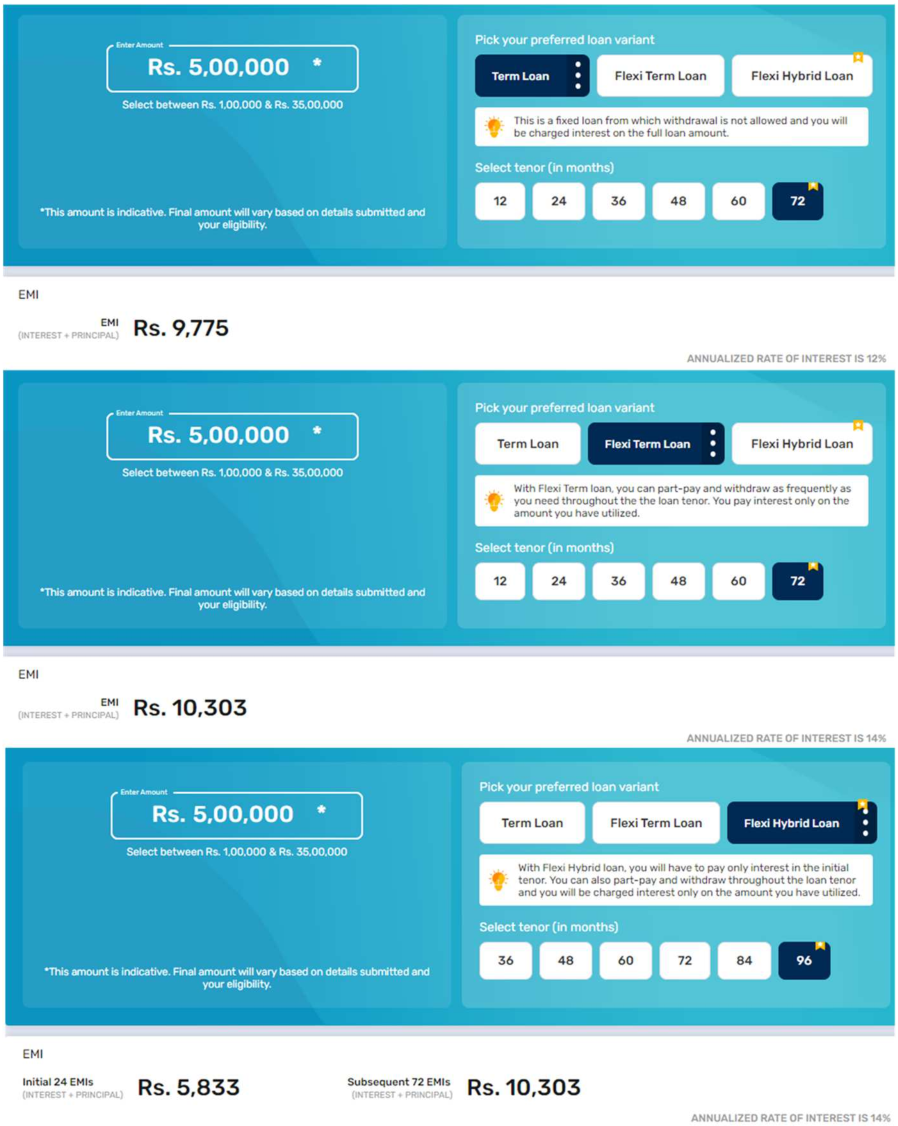
Product group	Nature of securities
Urban sales finance	Hypothecation of underlying product financed (e.g. consumer durables, furniture, digital products)
Two- and three-wheeler finance	Hypothecation of underlying 2W and 3W
Rural sales finance	Hypothecation of underlying product financed (e.g. consumer durables, furniture, digital products)
Rural B2C - Gold loans	Pledge of gold jewellery
SME lending (Secured)	Hypothecation of underlying product (e.g. used car, medical equipment)
Mortgages	Equitable mortgage of residential and commercial properties
Loan against securities	Pledge of equity shares and mutual funds and lien on deposits and insurance policies
Commercial lending	Plant and machinery, book debt, etc.

Source: Company, BOBCAPS Research | Note: The above data is from BAF’s FY23 Annual Report

Loan repayment variants

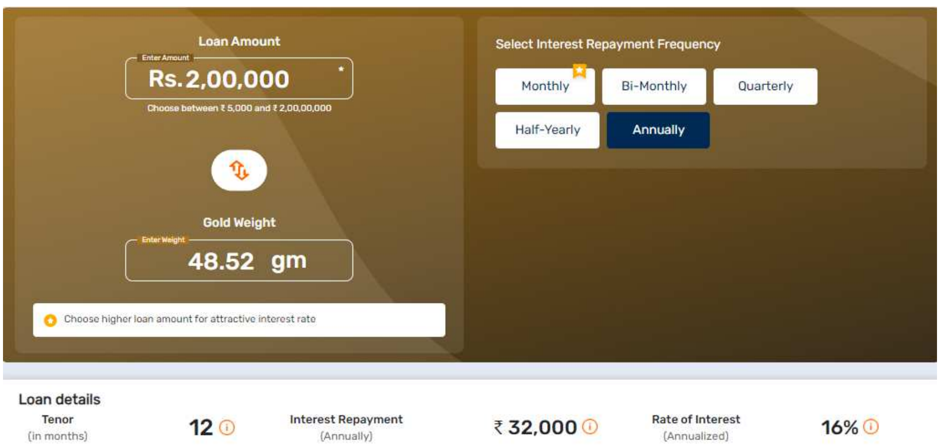
BAF offers loans in three variants – flexi hybrid, flexi term and term loan – which offer customers the flexibility to repay as convenient. These features are available across personal, professional and business loans. If a salaried person earning Rs 50,000 per month were to apply for a Rs 0.5mn personal loan, he/she could avail of any of the three variants below, as per the company’s website. In the subsequent illustration, we conducted a similar exercise for a gold loan of Rs 0.2mn.

Fig 59 – Personal loans



Source: Company website, BOBCAPS Research

Fig 60 – Gold loans



Source: Company website, BOBCAPS Research

Subsidiaries

BAF has two subsidiaries – Bajaj Housing Finance (BHFL) and Bajaj Financial Securities (BFSL).

BHFL – the housing story

BHFL, a 100% subsidiary of BAF with a focus on the mortgage industry, was set up in 2015 (operations started in 2017) and currently houses 87% of the parent's mortgage assets. About 62% of the subsidiary's portfolio is made up of individual home loans, a low-risk sector. Within this, ~95% of AUM is composed of loans to salaried employees and self-employed professionals for new home purchases.

BHFL offers the following products: (i) home loans to salaried (90% of segmental AUM), self-employed and professional customers, with average ticket size of Rs 5mn, offered in 59 locations across India; (ii) LAP to mass-to-affluent self-employed customers, with average size of Rs 7mn, offered in 27 locations; (iii) LRD to HNIs and developers against commercial property leased to corporate lessees, with ticket size of Rs 100mn to Rs 5.5bn, offered in 12 locations; and (iv) developer financing mainly to category A and A+ developers, with ticket size of Rs 50mn to Rs 5bn, offered in 14 locations. It also has a vertical that provides LAP and housing loans to MSMEs and the rural sector.

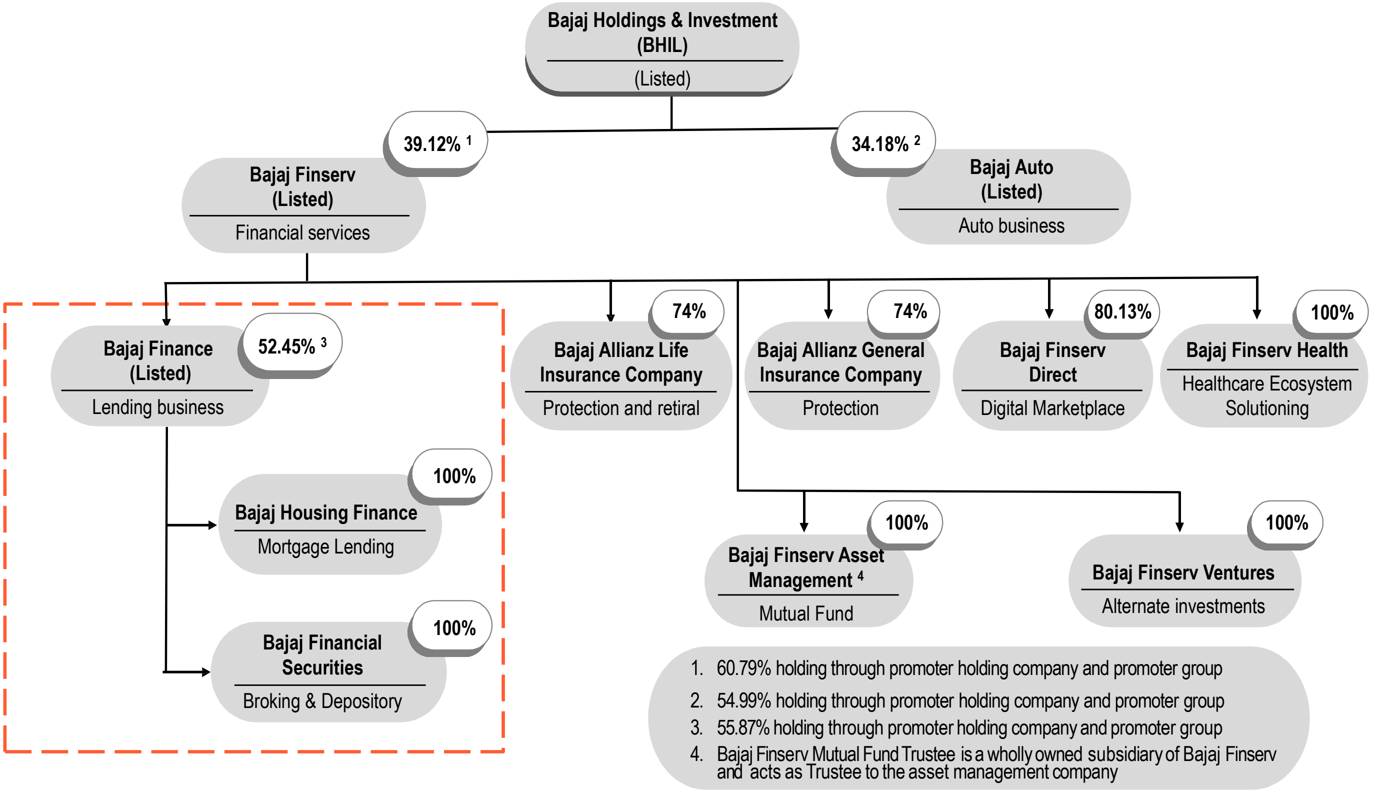
BFSL – the upcoming story

BFSL, a wholly owned subsidiary, began operating in 2019 to cross-sell a range of investment products and services to BAF's LAS customers. For retail and HNI clients, it provides demat, broking, margin trading finance, and financing for offers for sale. It also offers spread financing through BAF, including financing for new equity listing (IPO finance) and ESOP finance. BFSL has a base of ~0.6mn customers and generated total income of Rs 2bn and PAT of Rs 80mn in FY23. The year prior, BAF had infused Rs 4bn of additional share capital to fund near-term growth plans in the securities business.

Business activities can be broadly classified into:

- **HNI demat and broking:** BFSL offers demat and broking services to HNI clients, who have the option of call-in-trade service through dedicated traders. Such clients can avail of customised brokerage plans based on their trading needs. HNI clients with high trading volumes are given the option of a trading terminal. As on 31 Mar 2023, BFSL had over 22,500 HNI clients.
- **Retail demat and broking:** The company offers demat and broking services to retail clients through a set of customised discount broking plans. As on 31 Mar 2023, customer strength stood at 542,600.
- **Margin trade financing (MTF):** Under the MTF facility, both HNI and retail clients can purchase approved securities by paying the required margin while the balance is funded by BFSL. As on 31 Mar 2023, MTF AUM stood at Rs 10.6bn.

Fig 61 – Bajaj Group: Organisational structure



Source: Company, BOBCAPS Research | Note: Data as of 30 June 2023

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Net interest income	**1,38,894**	**1,75,235**	**2,29,903**	**2,85,451**	**3,63,124**
NII growth (%)	2.9	26.2	31.2	24.2	27.2
Non-interest income	33,797	43,708	58,555	73,289	94,063
Total income	1,72,691	2,18,944	2,88,458	3,58,740	4,57,187
Operating expenses	53,082	75,872	1,01,300	1,20,512	1,51,193
PPOP	1,19,608	1,43,072	1,87,158	2,38,228	3,05,995
PPOP growth (%)	6.3	19.6	30.8	27.3	28.4
Provisions	59,686	48,034	31,897	44,424	58,564
PBT	59,923	95,038	1,55,262	1,93,804	2,47,431
Tax	15,724	24,756	40,202	48,839	62,353
Reported net profit	**44,198**	**70,282**	**1,15,077**	**1,44,966**	**1,85,079**
Adjustments	0	0	0	0	0
Adjusted net profit	**44,198**	**70,282**	**1,15,077**	**1,44,966**	**1,85,079**

Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Equity capital	1,203	1,207	1,209	1,209	1,209
Reserves & surplus	3,67,981	4,35,920	5,42,511	6,65,732	8,23,048
Net worth	3,69,184	4,37,127	5,43,720	6,66,940	8,24,257
Debt securities	5,45,021	7,62,231	8,68,452	11,26,056	14,27,511
Borrowings	7,71,314	8,90,089	12,98,453	16,83,604	21,34,320
Other liab. & provisions	29,185	35,618	41,662	57,060	71,989
Total liab. & equities	**17,14,704**	**21,25,064**	**27,52,287**	**35,33,661**	**44,58,077**
Cash & bank balance	21,643	36,803	43,045	40,282	33,790
Investments	1,83,969	1,22,455	2,27,518	2,93,775	3,72,421
Advances	14,66,869	19,14,233	24,22,689	31,30,306	39,68,317
Fixed & Other assets	42,223	51,573	59,034	69,298	83,549
Total assets	**17,14,704**	**21,25,064**	**27,52,287**	**35,33,661**	**44,58,077**
Total debt growth (%)	10.0	39.9	13.9	29.7	26.8
Advances growth (%)	3.8	30.5	26.6	29.2	26.8

Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23A	FY24E	FY25E
EPS	73.7	116.8	189.6	238.7	304.8
Dividend per share	10.0	20.0	30.0	35.8	45.7
Book value per share	615.4	726.6	895.7	1,098.3	1,357.4

Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23A	FY24E	FY25E
P/E	97.2	61.3	37.8	30.0	23.5
P/BV	11.6	9.9	8.0	6.5	5.3
Dividend yield (%)	0.1	0.3	0.4	0.5	0.6

DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23A	FY24E	FY25E
Net interest income	8.3	9.1	9.4	9.1	9.1
Non-interest income	2.0	2.3	2.4	2.3	2.4
Operating expenses	3.2	4.0	4.2	3.8	3.8
Provisions	3.6	2.5	1.3	1.4	1.5
ROA	2.6	3.7	4.7	4.6	4.6
Leverage (x)	4.9	4.8	5.0	5.2	5.4
ROE	12.8	17.4	23.5	23.9	24.8

Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23A	FY24E	FY25E
YoY growth (%)					
Net interest income	2.9	26.2	31.2	24.2	27.2
Pre-provisioning profit	6.3	19.6	30.8	27.3	28.4
EPS	(15.8)	58.6	62.3	25.9	27.7
Profitability & Return ratios (%)					
Net interest margin	9.6	10.4	10.6	10.3	10.2
Fees / Avg. assets	1.5	1.6	1.8	1.8	1.9
Cost-Income	30.7	34.7	35.1	33.6	33.1
ROE	12.8	17.4	23.5	23.9	24.8
ROA	2.6	3.7	4.7	4.6	4.6
Asset quality (%)					
GNPA	1.8	1.6	0.9	1.0	1.3
NNPA	0.8	0.7	0.3	0.4	0.5
Slippage ratio	5.3	4.1	1.9	2.4	2.5
Credit cost	4.1	2.8	1.5	1.6	1.7
Provision coverage	58.0	58.0	64.0	62.2	59.7
Ratios (%)					
Loans to Total debt	111.1	115.5	111.5	111.1	111.1
CAR	28.3	27.2	25.0	24.5	24.8
Tier-1	25.1	24.8	23.2	22.6	23.0

Source: Company, BOBCAPS Research

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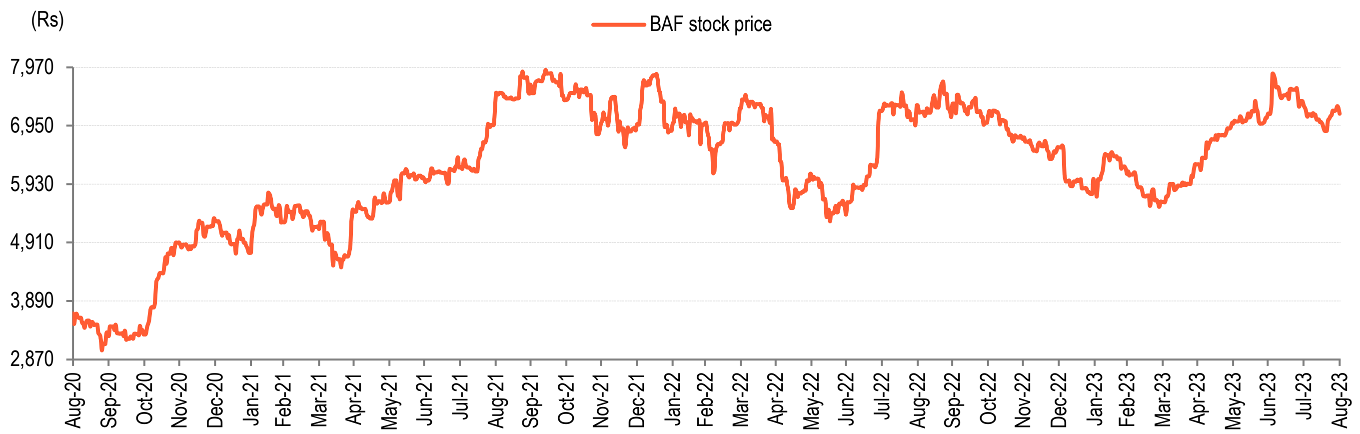

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