18 March 2024

Bajaj Finance

Rating: **Buy**
Target Price (12-mth): Rs.8,630
Share Price: Rs.6,485

Medium-term outlook intact; attractive entry point, reiterating a Buy

We met Bajaj Finance's management. The company is on track to achieve its medium-term targets and gain market share. Despite competition from other large corporate-backed NBFCs, we reckon that it is one of the fastest growing proxies for the Indian premiumisation theme. The recent correction of 22% from its 52W high is an attractive entry point. Reiterate Buy. At the CMP, the stock trades at 3.5x FY26e BV and 18x FY26 PE, with regulatory overhang priced in at this point.

Regulatory tightening positive; loan growth premium to endure. Risk-weighted changes for personal loans have reduced competition in CD loans, which could be extremely beneficial to the company. Management aims to follow all suggestions made by the RBI about EMI cards by the quarter's end. The recent clarification regarding credit-card partnerships should also be beneficial. Only three of the top 12 upper-layer NBFCs are to be listed, including Tata Sons. Keener competition would only spur innovation in the sector. The company's loan-growth premium to peers is likely to be high. This, and deep tech and product knowledge, leads us to believe that it is the best franchisee to play the Indian premiumisation theme.

Medium-term outlook unchanged; insignificant impact of the embargo. Despite the embargo on issuing new EMI cards, our channel checks suggest that growth has not been affected. Management maintains its medium-term outlook in terms of market-share gains and long-range profitability. We factor in a ~26.6% loan CAGR over FY24-26 and 4.5% RoA.

Valuation. At our 12-mth TP, the stock would trade at 4.7x FY26e BV and 23x FY26e EPS. It has traded at higher valuations in the past. **Risks:** Key-man risk, regulatory changes.

Key financials (YE Mar) (Rs m)	FY22	FY23	FY24e	FY25e	FY26e
Net interest income	213,820	273,314	344,134	434,828	540,947
PPoP	143,586	187,176	238,830	302,963	377,795
Provisions	48,548	31,897	42,912	58,123	67,921
PAT	70,282	115,078	144,588	180,692	228,687
EPS (Rs.)	116.5	190.4	234.0	291.4	367.7
NIM (%)	*11.4*	*11.4*	*11.0*	*11.0*	*11.0*
RoE (%)	*34.2*	*35.1*	*34.0*	*33.3*	*32.8*
RoA (%)	*17.4*	*23.5*	*22.0*	*21.2*	*21.9*
AUM growth (%)	*3.7*	*4.7*	*4.6*	*4.5*	*4.5*
GNPA (%)	*29.1*	*25.3*	*29.9*	*26.5*	*25.9*
CRAR	1.5	1.5	1.5	1.5	1.5
P/E (x)	27.2	26.5	26.9	25.4	24.8
P/BV (x)	55.0	33.7	27.4	22.0	17.4

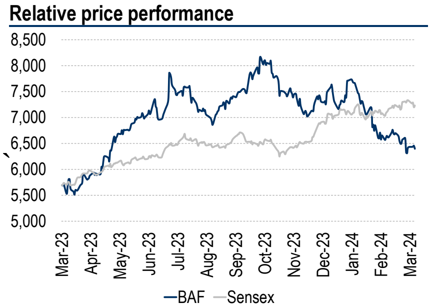
Source: Company, Anand Rathi Research

Key data	BAF IN / BJFN.BO
52-week high / low	Rs8192 / 5486
Sensex / Nifty	72643 / 22023
3-m average volume	$111.4m
Market cap	Rs3954bn / $47736.5m
Shares outstanding	618m

Shareholding pattern (%)	Dec'23	Sep'23	Jun'23
Promoters	54.8	55.9	55.9
- of which, Pledged	-	-	-
Free float	45.2	44	43.9
- Foreign institutions	20.9	20.1	20.1
- Domestic institutions	14.1	12.9	12.9
- Public	10.2	11.0	10.9

Estimates revision (%)	FY25e	FY26e
NII	(0.3)	(0.7)
PPOP	(0.8)	(1.6)
PAT	(1.0)	(4.9)

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (Rs m)

Year-end: Mar	FY22	FY23	FY24e	FY25e	FY26e
Net interest income	213,820	273,314	344,134	434,828	540,947
Growth (%)	*30.4*	*27.8*	*25.9*	*26.4*	*24.4*
Non-interest income	4,373	15,148	17,723	19,495	21,445
Total income	**218,193**	**288,462**	**361,857**	**454,323**	**562,392**
Growth (%)	*27.0*	*32.2*	*25.4*	*25.6*	*23.8*
Operating expenses	74,607	101,286	123,026	151,359	184,597
of which, emp. benefit exp.	35,897	50,494	63,117	79,528	99,410
PPoP	**143,586**	**187,176**	**238,830**	**302,963**	**377,795**
Growth (%)	*19.8*	*30.4*	*27.6*	*26.9*	*24.7*
Provisions	48,548	31,897	42,912	58,123	67,921
PBT	**95,038**	**155,279**	**195,918**	**244,840**	**309,874**
Tax	24,756	40,202	51,331	64,148	81,187
PAT	**70,282**	**115,078**	**144,588**	**180,692**	**228,687**
PAT growth (%)	*59.0*	*63.7*	*25.6*	*25.0*	*26.6*

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (Rs m)

Year-end: Mar	FY22	FY23	FY24e	FY25e	FY26e
Share capital	1,207	1,209	1,236	1,240	1,244
Other equity	435,920	542,511	770,267	934,839	1,147,354
Net worth	**437,127**	**543,720**	**771,503**	**936,079**	**1,148,598**
Borrowings	1,652,319	2,173,357	2,780,933	3,491,651	4,348,912
Growth (%)	*25.5*	*31.5*	*28.0*	*25.6*	*24.6*
Other liabilities	35,608	35,210	45,773	59,505	77,357
Total liabilities	**2,125,054**	**2,752,287**	**3,598,209**	**4,487,235**	**5,574,866**
Cash & equivalents	36,803	43,045	161,904	193,484	228,492
Investments	122,455	229,007	206,106	195,801	186,011
Loans	1,914,233	2,430,886	3,160,151	4,013,392	5,056,874
Growth (%)	*30.5*	*27.0*	*30.0*	*27.0*	*26.0*
Other assets	51,563	49,349	70,047	84,558	103,489
Total assets	**2,125,054**	**2,752,287**	**3,598,209**	**4,487,235**	**5,574,866**
AUM	**1,974,520**	**2,473,790**	**3,213,125**	**4,065,752**	**5,117,978**
RWA	**1,588,032**	**2,309,341**	**3,223,354**	**4,173,928**	**5,259,149**

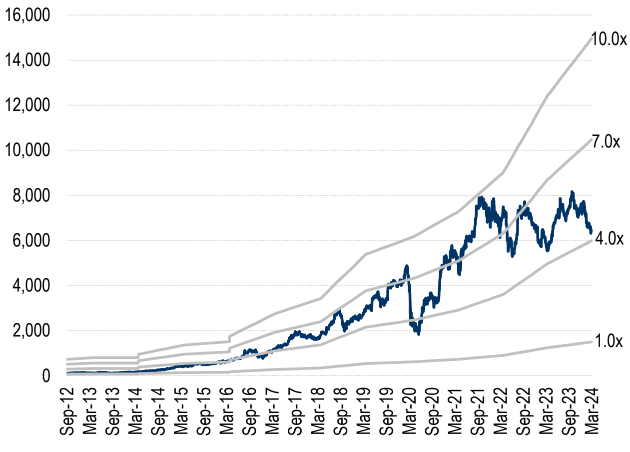
Source: Company, Anand Rathi Research

Fig 3 – Ratio analysis (%)

Year-end: Mar	FY22	FY23	FY24e	FY25e	FY26e
NIMs	11.4	11.4	11.0	11.0	11.0
Cost-to-income	34.2	35.1	34.0	33.3	32.8
Credit cost	2.9	1.5	1.5	1.6	1.5
RoA	3.7	4.7	4.6	4.5	4.5
RoE	17.4	23.5	22.0	21.2	21.9
GNPA	1.5	1.5	1.5	1.5	1.5
NNPA	0.7	0.7	0.7	0.7	0.7
RWA / Assets	74.7	83.9	89.6	93.0	94.3
CRAR	27.2	26.5	26.9	25.4	24.8
Tier 1	24.7	23.5	23.9	22.4	21.8
EPS (Rs)	116	190	234	291	368
BVPS (Rs)	725	900	1,248	1,510	1,847
ABVPS (Rs)	714	886	1,231	1,488	1,818
Dividend yield	0.3	0.3	0.4	0.4	0.4
P/E (x)	55.0	33.7	27.4	22.0	17.4
P/B (x)	8.8	7.1	5.1	4.2	3.5
P / ABV (x)	9.0	7.2	5.2	4.3	3.5

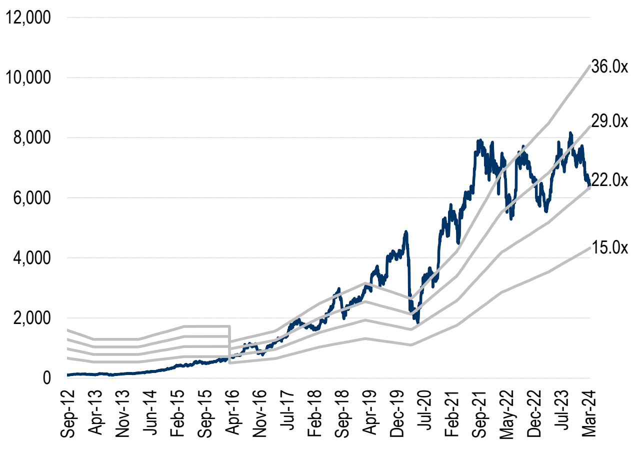
Source: Company, Anand Rathi Research

Fig 4 – 1-yr-fwd price-to-book band



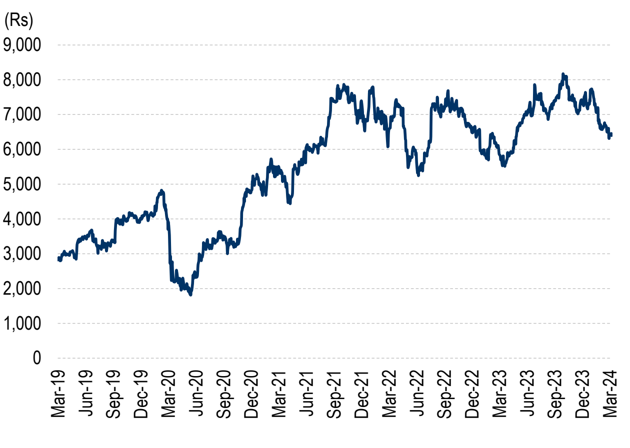
Source: Bloomberg

Fig 5 – 1 yr-fwd price-to-earnings band



Source: Bloomberg

Fig 6 – Price movement



Source: Bloomberg

Regulatory tightening positive

Risk-weighted changes for personal loans have reduced competition in consumer durables, which could significantly benefit the company. Management aims to fulfil all the suggestions made by the RBI regarding EMI cards by the quarter's end. The recent clarification about credit-card partnerships should also benefit the company. Even the entry of a large corporate group in financial services would ensure innovation and best practices. Pre-Covid, the NBFC commanded premium valuations on scarcity. With increasing choice of NBFCs, this has however contracted. We believe that the company is the best franchisee to play the Indian premiumisation theme.

Fig 7 – Recent regulatory actions on NBFCs

Subject	Action	Date of notification
BAF	Extension of 1 year for co-branded credit card with RBL, against five requested	13-10-2023
BAF	Suspension of sanctions and disbursals of e-com and insta EMI card	15-11-2023
Bank credit to NBFCs	Increase in risk weights by 25 percentage points, leading to increase in cost of funds obtained from banks	16-11-2023
One97 Communications (PayTM)	Suspension of licence of PayTM Payments Bank	31-01-2024
IIFL Finance	Cease and desist order on business of gold finance	04-03-2024
JM Financial	Cease and desist order on business of financing against shares and debentures	05-03-2024
Amendment to the master direction (credit and debit card issuance and conduct directions), 2022	No prior approval of the regulator required to become a partner in co-branded credit cards	07-03-2024

Source: RBI, Company, Anand Rathi Research

Will this impact the company in any way?

While only cross-selling is impacted in a limited manner due to the embargo on EMI cards, management said that by the quarter's end, it will submit a revised plan. Besides, clarity on non-banking credit card tie-ups is positive for the company. No further action augurs well for the NBFC.

Competition personal loans is easing as the regulator has tightened norms; capital is being allocated to more prudent companies in the space.

Is the scarcity premium component in its valuation eroding?

Of the 12 upper-layer NBFCs, only three are to be listed: Tata Sons (CIC), Tata Capital and HDB Financial Services. The others have already been listed, and performances aptly analysed. With Jio Financial also having been listed, almost all major competitors sport a fair price discovery.

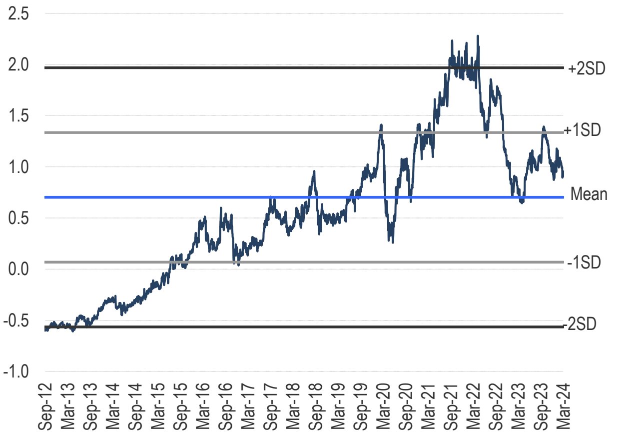
Will the RBI tighten norms, which would slow the company's growth?

The RBI has never intervened in the growth rate of companies. If it is not comfortable with growth, risk-weighted changes are more probable than loan-growth constraints. Besides, at the system level, BAF is still under 2% and has visibility left for longer periods of growth.

An alternative view to premium valuations

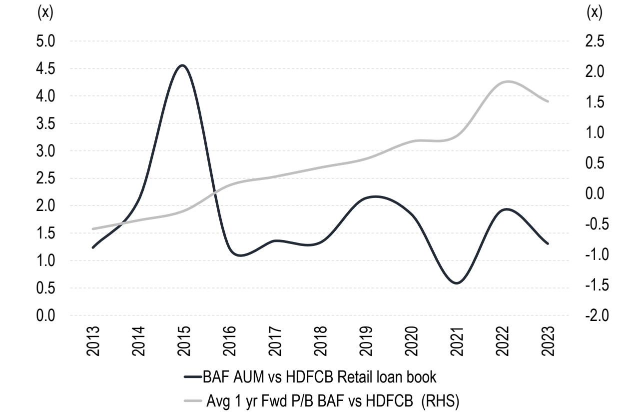
The company's premium valuation has decreased over the last two years. We offer an alternative viewpoint to look at its valuations. We compare its premium valuations to its AUM growth, outshining those of its peers.

Fig 8 – BAF vs. HDFC one-year-forward P/B



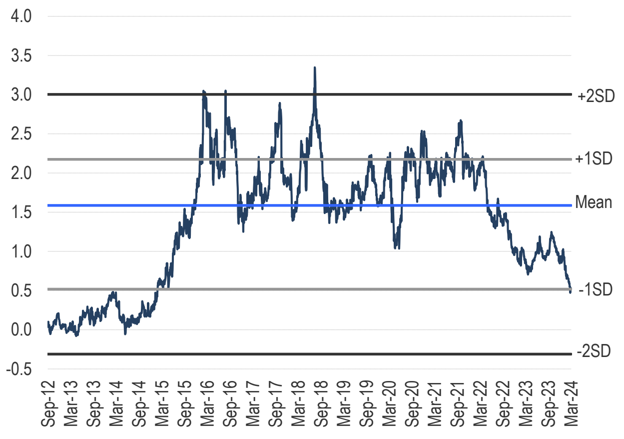
Source: Company, Anand Rathi Research

Fig 9 – BAF over HDFC Bank (growth vs. average one-year-forward P/B)



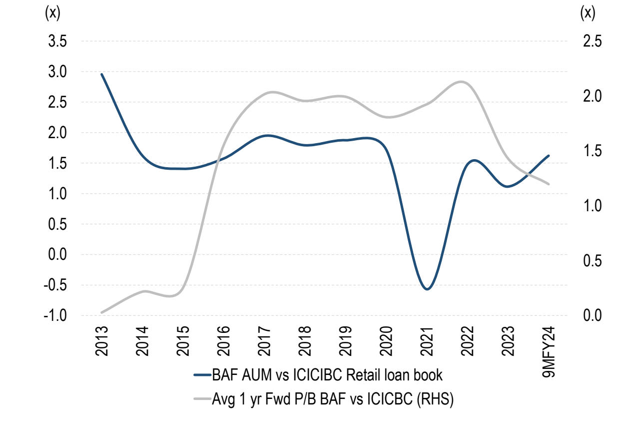
Source: Company, Anand Rathi Research

Fig 10 – BAF vs. ICICI one-year-forward P/B



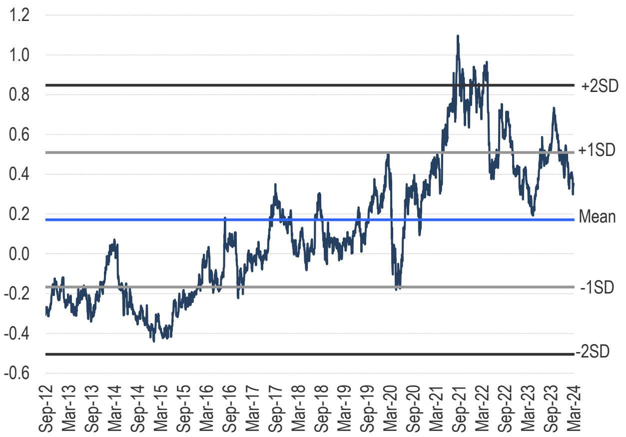
Source: Company, Anand Rathi Research

Fig 11 – BAF over ICICI Bank (growth vs. average one1-year-forward P/B)



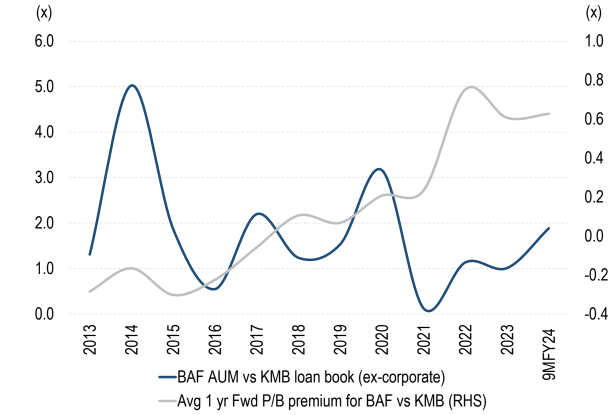
Source: Company, Anand Rathi Research

Fig 12 – BAF vs. KMB one-year-forward P/B



Source: Company, Anand Rathi Research

Fig 3 – BAF over KMB (growth vs. average one-year-forward P/B)



Source: Company, Anand Rathi Research

Fig 14 – BAF to continue its premium growth over Peers (%)

Growth premiums	FY24e	FY25e	FY26e
BAF vs. HDFC Bank	*1.8*	*1.7*	*1.6*
BAF vs. ICICIBC	*1.6*	*1.5*	*1.4*
BAF vs. KMB	*1.6*	*1.6*	*1.5*

Source: Company, Anand Rathi Research

3T and structural changes in consumer finance

Structural changes are underway in consumer finance, driving a realistic increase in the total addressable market (covered in our previous report **India - BFSI: Digitize or Die)**.

With the third highest number of unicorns in the world, capital is now shifting from payments to lending tech, insurtech and wealth-tech. Fintech could have $500bn AUM by FY30.

We believe that efficient utilisation of the Indian digital super-highway built on a combination of Jan-dhan Aadhar Mobile (JAM), a flexible regulator and NPCI is driving a realistic increase in TAM in retail and MSME credit. We explain the structural changes in what we call 'the 3T model'.

Ticket size

We believe smaller ticket sizes are catalysing financial diversification, with a whole set of the SENP category becoming eligible. Banks/NBFCs willing to experiment in the new-to-banking and under-served category would be able to tap the middle class and lower middle class more effectively. Also, this would drive faster penetration of credit in tier-3 towns and below. Our model suggests a potential Rs1.5trn pa rise in TAM due to smaller ticket sizes.

Tenure

On easy access to short-term personal loans and Buy-Now, Pay-Later and on superior customer experience, the velocity of loans taken by Gen Z would increase. We assume that a 25-year-old today would take 15 loans over his/her lifetime, against 3-4 for Gen X. Banks/NBFCs with sticky customers and an effective PPC strategy would win here. Our model suggests an Rs18trn increase in TAM due to shorter tenures.

Time to launch a new product

Open banking and APIs are driving faster turnaround time for financial products. Partnerships between banks, NBFCs and fintechs are occurring at an increasing pace. We would want to invest in banks/NBFCs which have an edge in technology and product innovation and robust execution abilities.

On track to achieving medium-term targets

The company reiterated that its medium-term FY27 targets are unchanged despite volatility. These include RoA, growth, NIM.

Market share

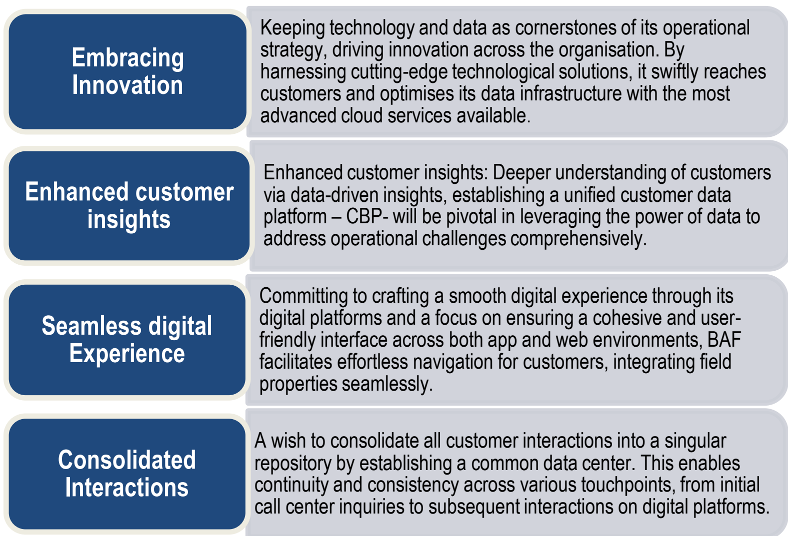
The company aims to broaden its customer base, setting a new 150m customer target, compared to the previous 100m goal. In 9M FY24, it onboarded 11.3m customers, marking 33% growth from the corresponding FY23 period. Besides, it aims at 25-27% AUM growth, with a 200bp y/y increase in RoA guidance (from 4–4.5% to 4.6–4.8%) in this financial year, which is also in line with our estimates. The aim is to reach a 3–3.5% market share in terms of GMV payments and 4–5% retail credit in India.

Incremental ratings in rural show a satisfactory performance, although not fully aligned with past performances

Sluggish retail B2C; B2B on track

Despite sluggish rural growth, the company is optimistic about penetrating deeper into India. States like UP, Bihar and the north-eastern ones offer substantial expansion opportunities. The company has expanded its operations, adding 139 locations. The plan is to penetrate these regions by launching all products across all locations in a sustained manner.

Fig 15 – Technological interventions will help enhance customer journey



Source: Company, Anand Rathi Research

Omnipresence strategy: Moving from digitisation to digitalisation

The heart of the company's strategy is dual commitment to establishing omnipresence in the market along with enhancing overall customer experience and pioneering seamless transactions that would transcend geographical and temporal boundaries. This weaves a strong tapestry across consumer landscapes, asserting brand presence in physical outlets and virtual interfaces. Moreover, efforts are being made to enhance the social space, with plans to introduce rewards in future. This also allows better utilisation of the existing customer base, with improved credit cost.

Fig 16 – App metrics trending well; could provide the next fillip

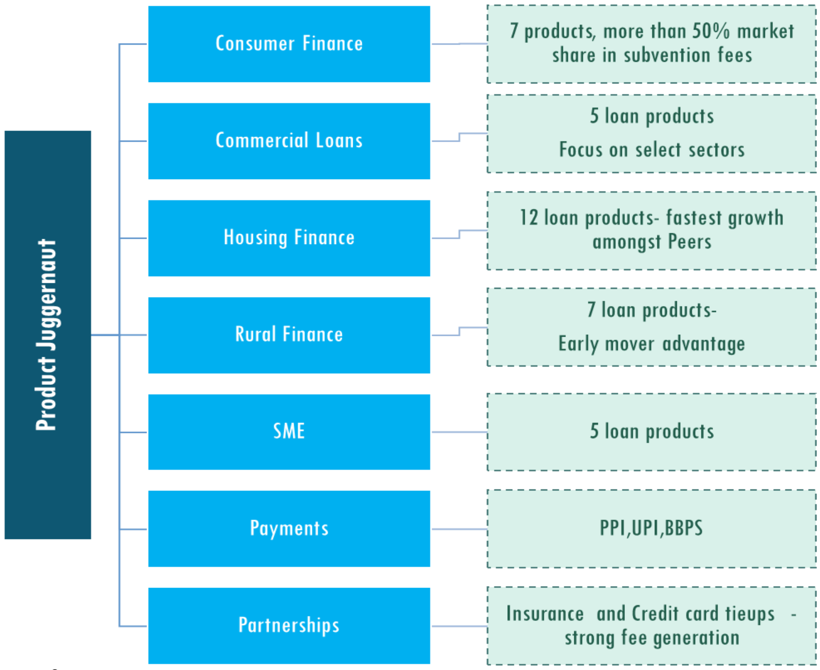
(Rs m)	Q3 FY23	Q4 FY23	Q1 FY24	Q2 FY24	Q3 FY24
Region					
Locations added - in the quarter	29	19	95	106	158
Location - cumulative	3,714	3,733	3,828	3,934	4,092
Standalone gold loan branches - cumulative	179	181	424	514	537
App parameters					
Downloads (m)	14.8	13.4	15.1	16.7	15.8
Net installs - cumulative (m)	31.5	35.5	40.2	44.7	49.2
App payment parameters					
UPI handles - cumulative (m)	10.4	13.0	15.5	18.6	21.5
Bill Pay, no. of transactions (m)	5.0	5.3	5.4	6.4	7.5
QRs at merchant PoS, cumulative ('000)	214.0	627.0	1,140.0	2,160.0	2,710.0
Reward issues (m)	17.3	13.5	18.1	22.1	25.4
App business parameters					
EMI cards acquired on app ('000)	100.0	99.0	123.0	130.0	89.0
Personal loans disbursed on app (m)	23,010.0	2,607.0	2,760.0	2,910.0	2,861.0
Credit card acquisitions on app ('000)	59.2	72.0	77.0	69.9	59.7
Flexi-loan transactions on app ('000)	1,481.0	1,554.0	1,700.0	1,990.0	2,190.0
DMS receipts on app ('000)	900.0	972.0	982.0	1,100.0	1,240.0
Marketplace parameters					
Bajaj Mall visits (m)	44.2	47.1	49.0	52.0	46.0
Bajaj Mall loans ('000)	619.0	607.0	826.0	589.0	491.0
Insurance Bazaar policies ('000)	153.7	107.6	112.0	106.0	149.1
Investments Bazaar MF A/C ('000)	19.5	23.6	25.4	38.5	55.0
Digital EMI card parameters					
EMI cards acquired digitally ('000)	637.0	598.0	665.0	678.0	439.0
EMI cards acquired digitally - CIF (m)	3.1	3.6	3.8	4.2	4.5
B2B loans from digital EMI cards ('000)	284.0	291.0	416.0	346.0	281.0

Source: Company, Anand Rathi Research

Strong franchisee, deeper penetration

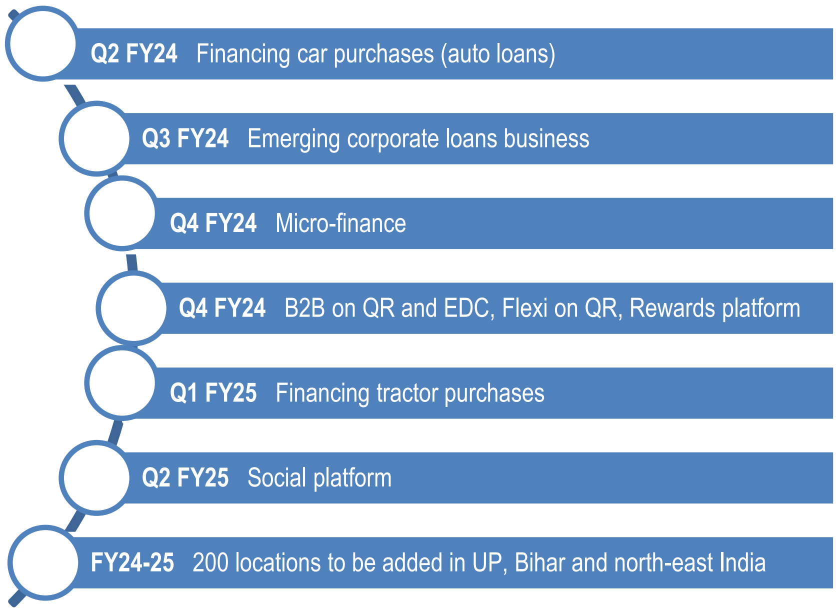
The company is financialising consumption in India. It has many firsts to its credit in lending, incl. short-duration EMIs, rural CDs, etc. Its strategy of localised proof-of-concept, then unveiling products at scale, has much steam left. At present, housing and gold loans are growing faster than other products. Deeper product penetration provides assurance of a longer runway of growth.

Fig 17 – Product portfolio



Source: Company

Fig 18 – Timeline for new products



Source: Company

The company's penetration and distribution have been consistently increasing.

Fig 19 – Penetration

Geographic presence	FY19	FY20	FY21	FY22	FY23	9M FY24
Urban	927	1,035	1,298	1,368	1,392	1,538
Rural	903	1,357	1,690	2,136	2,341	2,554
Total Bajaj Finance presence	**1,830**	**2,392**	**2,988**	**3,504**	**3,733**	**4,092**
Strong distribution reach						
Consumer durable stores, urban	20,400	24,200	26,400	30,600	33,950	40,150
Consumer durable stores, rural	14,500	19,600	24,000	29,800	37,000	46,300
Digital product stores	22,500	26,400	23,800	29,500	33,000	38,750
Lifestyle retail stores	7,700	9,500	9,800	11,000	13,200	16,050
EMI card retail spends stores	19,100	24,300	14,300	18,800	22,200	27,650
Bajaj Auto dealers, sub-dealerships and ASSC	4,600	5,500	5,900	6,000	5,150	5,550
Non captive 2W dealers, sub dealers & ASSC*	-	-	-	-	2,650	5,200
Direct sales agents	2,800	4,900	6,100	7,500	7,500	9,600
Overall active distribution network	**91,700**	**114,400**	**110,300**	**133,200**	**154,650**	**190,600**

Source: Company, Anand Rathi Research

Over the last five years, the portfolio mix has diversified substantially with the share of mortgages rising. Ahead, management believes this to be a stable proportion of loan mix and should not deviate much.

Fig 20 – Diversified portfolio mix

(Rs m)	Q3 FY23	Q4 FY23	Q1 FY24	Q2 FY24	Q3 FY24
Consumer B2B - auto finance	117,860	129,790	147,360	165,480	193,840
Consumer B2B - sales finance	167,120	176,270	223,210	229,730	244,850
Consumer B2C	467,330	501,080	548,450	581,780	617,050
Rural B2B sales finance	46,840	48,030	55,670	55,340	61,660
Rural B2C	184,580	194,570	202,720	208,800	214,260
SME	308,800	337,650	349,640	386,730	413,960
Securities lending	132,570	150,930	162,380	169,860	192,050
IPO financing	-	-	-	-	-
Commercial lending	148,480	158,340	180,640	195,580	206,720
Mortgages	734,840	777,130	830,900	909,340	965,290
Total AUM	**2,308,420**	**2,473,790**	**2,700,970**	**2,902,640**	**3,109,680**
Y/Y growth (%)	*27.4*	*25.3*	*32.4*	*32.9*	*34.7*

Source: Company, Anand Rathi Research

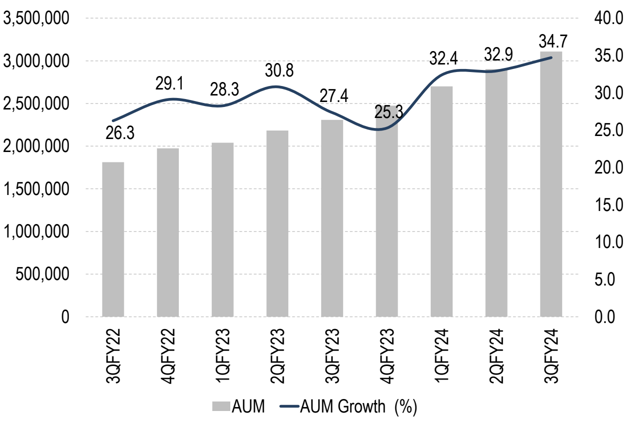
Management guided to a higher Rs100m-110m TAM of premium-segment customers. This has still some way to go. Besides, as more customers take loans frequently, we believe growth for the company would be buoyant.

Fig 21 – Widening customer franchise - TAM increasing considerably

(Rs m)	Q3 FY23	Q4 FY23	Q1 FY24	Q2 FY24	Q3 FY24
Total franchise	66.1	69.1	73.0	76.6	80.4
Credit segment filter	51.3	53.6	56.9	59.7	62.9
Overall cross-sell franchise	49.7	52.0	55.2	57.9	61.1
Non-delinquent customers	43.9	45.9	48.9	51.3	54.1
Cross-sell franchise	38.6	40.6	44.3	46.7	49.3
Customer franchise addition	**3.1**	**3.1**	**3.8**	**3.6**	**3.9**

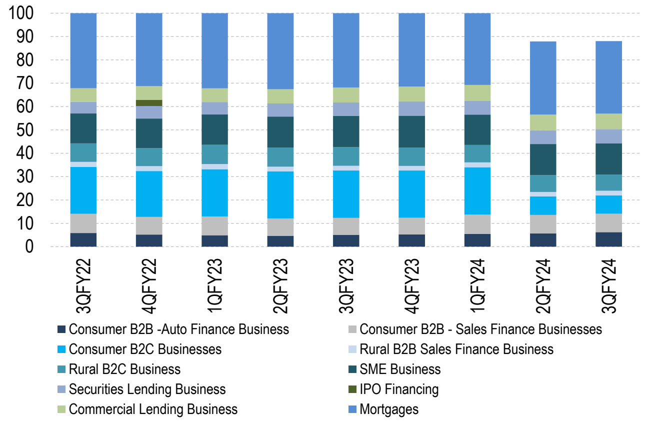
Source: Company, Anand Rathi Research

Fig 22 – AUM and y/y growth



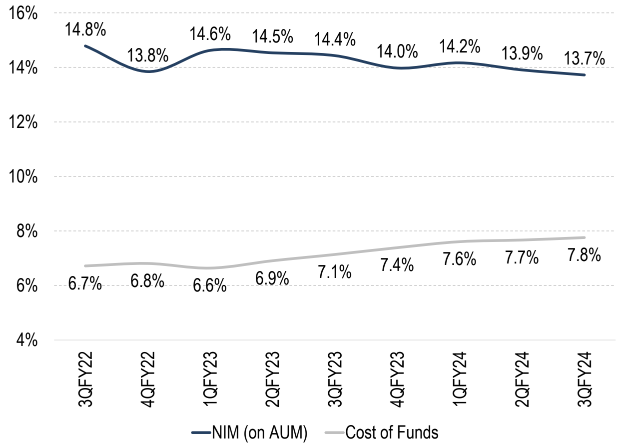
Source: Company, Anand Rathi Research

Fig 23 – AUM break-up



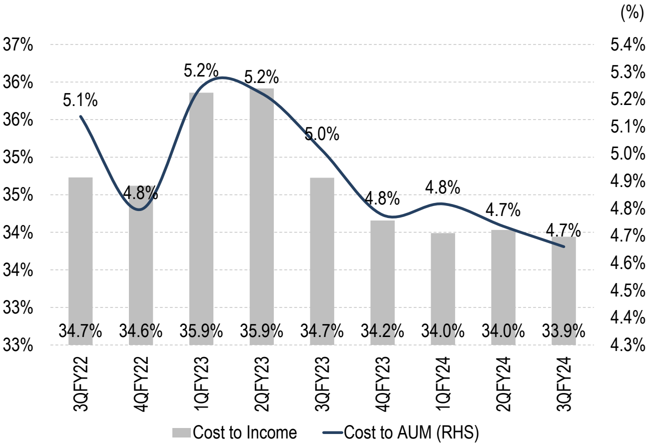
Source: Company, Anand Rathi Research

Fig 24 – NIM vs. Cost of funds



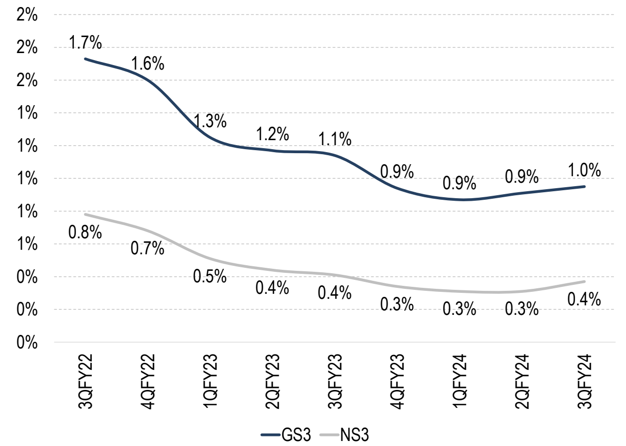
Source: Company, Anand Rathi Research

Fig 25 – C/I and Cost-to-assets



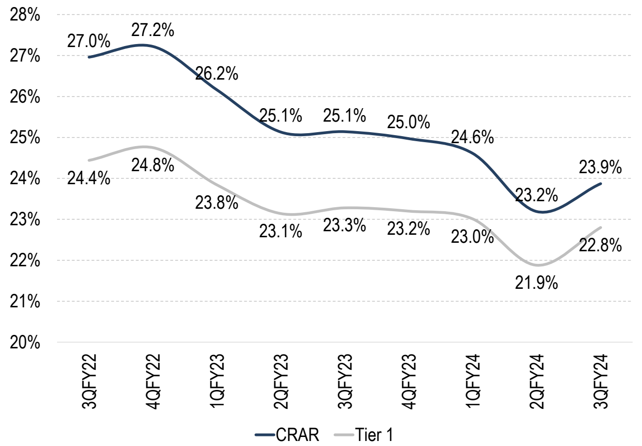
Source: Company, Anand Rathi Research

Fig 26 – GS3 and NS3 movement



Source: Company, Anand Rathi Research

Fig 27 – CRAR and Tier 1



Source: Company, Anand Rathi Research

Valuation

At our meeting with Bajaj Finance's management, we found the company is on track to achieving its medium-term targets and gaining market share, with high growth, deepening product penetration and unmatched execution skills. Despite competition from other large corporate-backed NBFCs, we consider that it is one of the fastest growing proxies for the Indian premiumisation theme.

The recent 22% stock easing since the results offers an ideal entry point; we, therefore, reiterate BAF as our top NBFC idea and value it at 4.7x FY26e BV as per the multi-stage DDM. At the CMP, it trades at 3.5x FY26e BV and 18x FY26e EPS. We believe the regulatory overhang has been priced in at this point.

Fig 28 – Change in estimates

	FY25e			FY26e		
(Rs m)	New	Old	Chg %	New	Old	Chg %
Net interest income	434,828	436,185	*(0.3)*	540,947	544,582	*(0.7)*
Pre-provisioning profit	302,963	305,512	*(0.8)*	377,795	384,017	*(1.6)*
PAT	180,692	182,573	*(1.0)*	228,687	240,510	*(4.9)*

Source: Anand Rathi Research

Fig 29 – Key assumptions

(%)	FY25e	FY26e
Balance sheet assumptions		
AUM growth	26.5	25.9
Borrowings growth	25.6	24.6
Asset quality assumptions		
Credit cost	1.61	1.49
Provision coverage	54.1	53.3

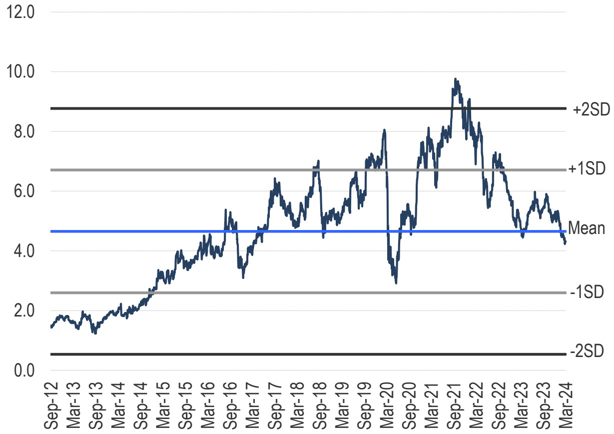
Source: Company, Anand Rathi Research

Fig 30 – du Pont analysis

(%)	FY22	FY23	FY24e	FY25e	FY26e
Operating income	16.3	16.4	16.1	16.0	16.0
Interest expense	5.1	5.2	5.3	5.2	5.3
Net interest income	**11.1**	**11.2**	**10.8**	**10.8**	**10.8**
Other income	0.2	0.6	0.6	0.5	0.4
Total income	**11.4**	**11.8**	**11.4**	**11.2**	**11.2**
Operating expenses	3.9	4.2	3.9	3.7	3.7
of which, salaries	1.9	2.1	2.0	2.0	2.0
PPoP	**7.5**	**7.7**	**7.5**	**7.5**	**7.5**
Provisions	2.5	1.3	1.4	1.4	1.4
PBT	**5.0**	**6.4**	**6.2**	**6.1**	**6.2**
Tax	1.3	1.6	1.6	1.6	1.6
RoA	**3.7**	**4.7**	**4.6**	**4.5**	**4.5**
Equity multiplier	4.8	5.0	4.8	4.7	4.8
RoE	**17.4**	**23.5**	**22.0**	**21.2**	**21.9**

Source: Company, Anand Rathi Research

Fig 31 – One-year-forward price-to-book value



Source: Company, Anand Rathi Research

Fig 32 – One-year-forward price-to-earnings

Source: Company, Anand Rathi Research

Risks

- Higher slippages.
- Less-than-expected loan growth.
- Key-man risk.

Appendix

Analyst Certification

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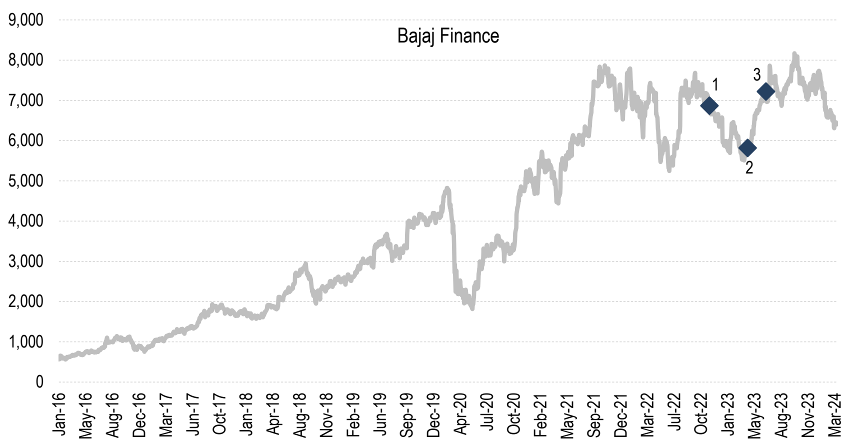
Rating and Target Price History (as of 16 March 2024)



	Date	Rating	TP (Rs)	Share Price (Rs)
1	5-Dec-22	**Buy**	8,959	6,674
2	26-Apr-23	**Buy**	8,123	6,056
3	10-Jul-23	**Buy**	9,650	7,622

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