Bajaj Finance

Accumulate

DART — DOLAT ANALYSIS & RESEARCH THEMES — IN-DEPTH•PRECISE•ACTIONABLE

Result Update

Asset quality lets down but otherwise another strong quarter with an AUM growth of 38% and benefits of operation leverage translating into earnings growth of 66% YoY. The negative was weakening asset quality, driven by slippages outpacing recoveries by 10bps QoQ, to 1.49% and reduced provisions cover. We remain confident on its ability to continue the growth momentum and increase market share as peers tighten their belts, ability to sustain NIMs and maintain customer acquisition and asset growth. Despite the increased volatility and regulatory overhang, it is well placed to weather the liquidity squeeze and risk aversion. Premium valuations and high beta coupled with sector aversion is likely to induce the volatility nevertheless premium valuations are likely to persist.

GNPA hurts but robust and steady asset growth, expect CAGR 35% in assets over FY18-20E: Assets grew 38% YoY, momentum guzzling across products. Operating leverage driven by optimising branch investment in the last fiscal aided exponential earnings growth. Asset quality continues to hurt, and the cover has been falling under the new ECL regime. We believe that the trend of robust asset growth and exponential earning growth is expected to continue after the benefits of physical and technological investments in previous year accrue. The demand momentum in its key product segment is unlikely to be adversely impacted in the near to medium term, though the GNPA are expected to inch up as its book season and pressure on rural book remain. The heartening part is the asset quality on relatively lumpy commercial finance book is nil and the risks in the other unsecured book is priced in.

Premium valuation + CAGR 40% in earning growth over FY18-20E = Accumulate at FY20E P/ABV: With robust asset growth and churning leverage benefits, we are healthy earning CAGR 40% and RoA expansion by 20 bps. With a short tenure assets and matched liability profile, it is well placed amidst the regulatory overhang and current adverse market sentiment. Despite narrowing, the relative premium valuations are likely to persist. At 5.5x FY20E P/ABV, Accumulate.

Q2FY19 Result (₹ Mn)

Particulars	Q2FY19	Q2FY18	YoY (%)	Q1FY19	QoQ (%)
Interest earned	42,559	30,862	37.9	39,365	8.1
Interest expended	15,673	11,438	37.0	13,636	14.9
Net interest income	26,886	19,425	38.4	25,728	4.5
Other income	404	161	-	49	-
Total Net Income	27,290	19,586	39.3	25,777	5.9
Operating expenses	9,799	8,752	12.0	9,536	2.8
Pre-provision profits	17,491	10,833	61.5	16,241	7.7
Provisions	3,146	2,278	38.1	3,268	(3.7)
Tax expense	5,110	3,005	70.1	4,634	10.3
Extraordinary gains	16	16		16	
Reported Net Profit	9,235	5,551	66.4	8,339	10.7
			(bps)		(bps)
AUM	37.9	38.9	(95)	35.5	244
NIM (%)	10.3	11.0	(70)	11.6	NM
RoA	4.0	3.2	80	4.8	(80)
RoE	21.6	17.6	400	24.0	(240)
Gross NPA (%)	1.4	1.7	(26)	1.4	(1)

CMP	₹ 2,083
Target / Upside	₹ 2,350 / 13%
BSE Sensex	33,847
NSE Nifty	10,147
Scrip Details	
Equity / FV	₹ 1,094mn / ₹ 2
Market Cap	₹ 1,201bn
	US$ 16bn
52-week High/Low	₹ 2,994/₹ 1,511
Avg. Volume (no)	2,735,200
NSE Symbol	BAJFINANCE
Bloomberg Code	BAF IN
Shareholding Pattern Sep'18(%)	
Promoters	55.2
MF/Banks/FIs	8.2
FIIs	20.1
Public / Others	16.1

Valuation (x)

	FY18A	FY19E	FY20E
P/E	44.8	30.5	22.6
P/ABV	7.5	6.2	4.9
ROAA	3.6	3.8	3.7
ROAE	20.7	21.7	23.6

Estimates (₹ mn)

	FY18A	FY19E	FY20E
NII	77,022	107,143	142,925
PPOP	51,415	73,549	95,508
PAT	26,742	39,333	53,001
Adj BV	279.4	338.5	422.7

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DOLAT CAPITAL

Exhibit 1: Quarterly Data

Particulars	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
AUM	**726,690**	**779,700**	**840,330**	**933,140**	**1,002,170**
YoY (%)	38.9	35.4	39.6	35.5	37.9
AUM mix (%)					
Consumer Finance	38.5	47.9	46.6	39.1	38.7
SME Finance	43.8	31.5	31.4	40.9	42.1
Commercial Finance	11.7	13.5	14.7	12.9	11.7
Rural Finance	6.0	7.1	7.3	7.2	7.4
Borrowing mix YoY (%)					
Banks	30.0	32.0	31.0	30.0	34.0
NCDs	47.0	46.0	43.0	36.0	35.0
Tier II Debt	7.0	7.0	6.0	6.0	5.0
FDs	10.0	11.0	12.0	14.0	15.0
CPs	5.0	3.0	6.0	12.0	9.0
CBLO	1.0	1.0	2.0	2.0	2.0
Contribution Margins (%)					
Yield on assets	17.4	19.1	17.8	17.8	16.1
Cost of Funds	8.6	8.5	8.3	8.5	8.9
Spreads	8.8	10.7	9.5	9.3	7.2
Cost to Income	45.1	39.1	41.9	37.1	36.4
NIMs	11.0	12.9	11.7	11.6	10.2
Asset Quality and capital ratios (%)					
GNPA (Stage 3 assets)	1.7	1.7	1.5	1.4	1.4
NNPA	0.5	0.5	0.4	-	0.5
ROE	17.6	20.0	20.5	24.0	21.6
ROA	3.2	4.4	3.9	4.8	4.0
Credit quality composition					
CD portfolio					
Bkt 0	98.58	98.83	98.91	99.04	98.91
30+	0.83	0.69	0.65	0.53	0.62
2W/3W					
Bkt 0	85.82	87.85	88.76	87.6	88.32
30+	7.14	6.21	5.51	5.96	5.69
Lifestyle					
Bkt 0	98.35	98.63	98.66	98.59	98.73
30+	0.94	0.75	0.77	0.8	0.67
Digital product finance					
Bkt 0	98.68	98.86	98.49	98.47	98.72
30+	0.74	0.6	0.88	0.89	0.74
Personal loan cross sell					
Bkt 0	97.26	97.46	97.62	97.64	97.69
30+	1.45	1.36	1.27	0.84	1.22
Salaried personal loans					
Bkt 0	99.57	99.63	99.7	99.66	99.68
30+	0.3	0.27	0.22	0.22	0.24
Business loan					
Bkt 0	98.6	98.55	98.68	98.76	98.76
30+	0.94	0.98	0.95	0.84	0.85
LAP					
Bkt 0	98.55	98.27	99.16	99.27	99.16
30+	1.41	1.57	0.8	0.66	0.81
Home loans					
Bkt 0	98.82	98.96	99.48	99.49	99.4
30+	0.93	0.8	0.21	0.47	0.43
Rural lending					
Bkt 0	99.21	99.17	99.11	99.07	98.97
30+	0.53	0.57	0.59	0.61	0.66

Source: DART

Concall Highlights

- **View on the Liquidity Crisis: Transient and has various options**
  - Liquidity squeeze is a part of the game and it happens every five years.
  - Learning from the previous squeeze, we maintain liquidity buffer of 4-6% of borrowing and have increased granularity in liabilities
  - Positive ALM in 1M and 1 year's bucket and product tenor create natural liquidity in every bucket.
  - Even if the regulation changes to disallow 15% mismatch in early bucket, yet is well placed and can borrow ₹ 72 bn. It expects the 15% rule to reduce to 5%.
  - No chase for rapid growth, ₹ 15Bn is monthly acquisition and comfortable with growth currently.
  - Granularity in liability: Expects deposits to form 20-22% of book. Currently has deposits acquisition in 15 cities.
  - CP to remain between 5-10%.
  - Housing finance sides in increasing funding options.
  - Marginal CoF higher but it is a transient time, current levels may not remain. Expect normalization in another 30 days, likely like previous times but must wait and watch.
- **No belt tightening:** At the moment there is no belt tightening in any business. But if things were come to that pass, it would reduce the share of lumpy business. Won't slow B2B and B2C, may slow SME, LAS and commercial lending. Currently comfortable with the credit view. Open for all business and ensure no lumpy business for 1-2 quarter to avoid the concentration risk in a tight market with a further stronger focus on credit quality management.
- **Create credit separation:** The crisis will create credit separation with strong business models surviving. The best way to deal is to reduce business models based on cost of funds.
- **Exposure to IIL&FS (₹ 2250 mn):** LAP towards a commercial space in GIFT city, LTV based on MV 60-62% exclusive charge. Have received the confirmation from trustee and the company and see no risk to exposure. Toward prudence and ageing (the long wait for resolution), have currently charged 10% provisions.
- **Demand Scenario:**
  - Festive season demand, flows are exciting. Some argue it is in patches but the first 15 days have been strong. In discretionary and captive, the demand is strong.
  - SME is expected to pick up post the cautious slowdown during the demo and GST phase between November 16 - March 18. Since the last 2 quarters, SME has been growing good with healthy credit profile.
  - Growth at ambitious 38-39% is a monitorable but it is a benchmark
  - 45% of book is repriceable.
- Operating leverage and better optimization improves C/I.

- **Developer financing:** Exposure granular in ₹ 200-400mn mid-size developers with 1-3 projects and a cap of ₹ 500 mn per develop (average ₹ 110 mn), expect 12-14% of book in overall mortgage with 15-16 RoE without increasing risk
- **Gradual price increase:** Incremental new acquisition higher by 20-50 bps.
- Credit risk profile not a problem, conserve liquidity and look for no lumpy exposure.
- Increase of 10-20 bps embedded in pricing. Expect CoF at 8.8-8.7 in 1Q20.

  Currently the expenses in HFC are up fronted and income amortized, expect faster growth as share of NII increase. 6-8 months is the transition.
- Mix of HFC at 30-35% in the medium term.
- Coupon on deposits: 8.50% coupon now. Existing customers 8.75% coupon. Corporate is more of a market rate

Profit and Loss Account (₹ Mn)

Particulars	FY17A	FY18A	FY19E	FY20E
Interest Income	92,723	123,366	177,114	236,683
Interest expenses	38,034	46,343	69,971	93,758
Net interest income	**54,690**	**77,022**	**107,143**	**142,925**
Other incomes	7,310	11,294	13,869	16,253
Total expenses	25,642	36,901	47,463	63,670
- Employee cost	9,317	14,196	16,805	22,411
- Other	16,326	22,705	30,659	41,259
Pre provisioning profit	**36,357**	**51,415**	**73,549**	**95,508**
Provisions	8,182	10,452	12,904	14,546
Profit before taxes	28,175	40,963	60,644	80,962
Tax provision	**9,810**	**14,221**	**21,311**	**27,961**
Profit after tax	18,366	26,742	39,333	53,001
Share in JV associate	0	0	0	0
Minority interest	0	0	0	0
Extraordinary gains	0	0	0	0
Total comprehensive income	**18,366**	**26,742**	**39,333**	**53,001**
Adjusted profit	**18,366**	**26,742**	**39,333**	**53,001**

Balance Sheet (₹ Mn)

Particulars	FY17A	FY18A	FY19E	FY20E
Sources of Funds				
Equity Capital	1,094	1,150	1,156	1,156
Reserves & Surplus	94,909	161,523	197,983	248,210
Minority Interest	0	0	0	0
Net worth	**96,003**	**162,673**	**199,139**	**249,366**
Borrowings	492,497	644,814	920,261	1,297,370
Current liabilities & provisions	48,746	60,757	85,593	123,296
Total Liabilities	**637,246**	**868,243**	**1,204,993**	**1,670,032**
Cash and balances with RBI	3,565	3,395	4,259	129,179
Investments	40,747	31,460	53,098	55,175
Advances	576,827	816,001	1,127,911	1,463,491
Fixed assets	3,611	4,703	4,284	3,936
Other current assets, loans and advances	12,495	12,685	15,440	18,251
Total Assets	**637,246**	**868,243**	**1,204,993**	**1,670,032**

E – Estimates

Important Ratios

Particulars	FY17A	FY18A	FY19E	FY20E
(A) Margins (%)				
Yield on advances	17.8	17.1	17.5	17.4
Yields on interest earning assets	17.3	17.3	18.0	17.2
Costs of funds	8.8	8.1	8.9	8.5
NIMs	10.5	10.7	10.6	10.5
(B) Asset quality and capital ratios (%)				
GNPA	1.7	1.4	1.8	2.0
NNPA	0.4	0.4	0.5	0.5
PCR	74.0	74.5	74.6	74.3
Slippages	75.8	113.5	132.0	106.5
NNPA to NW	1.4	2.3	2.9	3.4
CAR	20.3	24.7	21.9	20.0
Tier 1	14.6	19.7	16.7	16.1
(C) Dupont as a percentage of average assets				
Interest income	16.8	16.4	17.1	16.5
Interest expenses	6.9	6.2	6.7	6.5
Net interest income	9.9	10.2	10.3	9.9
Non-interest Income	1.3	1.5	1.3	1.1
Total expenses	4.7	4.9	4.6	4.4
- cost to income (NII)	46.9	47.9	44.3	44.5
Provisions	1.5	1.4	1.2	1.0
Tax	1.8	1.9	2.1	1.9
RoA	3.3	3.6	3.8	3.8
Leverage	5.0	5.0	5.0	5.0
RoE	21.6	20.7	21.7	22.6
RoRwa	2.8	3.0	3.5	3.6
(D) Measures of investments				
EPS - adjusted	33.4	46.5	68.4	92.2
BV	175.6	282.8	344.6	431.5
ABV	174.1	279.4	338.5	422.7
DPS	3.6	4.0	4.0	4.0
Dividend payout ratio	13.3	10.6	7.1	5.3
(E) Growth Ratios (%)				
Net interest income	35.7	40.8	39.1	33.4
PPoP	45.0	41.4	43.1	29.9
Adj PAT	43.6	45.6	47.1	34.8
Advances	34.9	41.5	38.2	29.8
Total borrowings	33.0	30.9	42.7	41.0
Total assets	37.2	36.2	38.8	38.6
(F) Valuation ratios (%)				
Market Cap	1,200,947	1,200,947	1,200,947	1,200,947
CMP	2083	2083	2083	2083
P/E	62.4	44.8	30.5	22.6
P/BV	11.9	7.4	6.0	4.8
P/ABV	12.0	7.5	6.2	4.9
Div Yield	0.2	0.2	0.2	0.2

E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	**> 20%**
Accumulate	**10 to 20%**
Reduce	**0 to 10%**
Sell	**< 0%**

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