

Stock Update

Keeps getting better

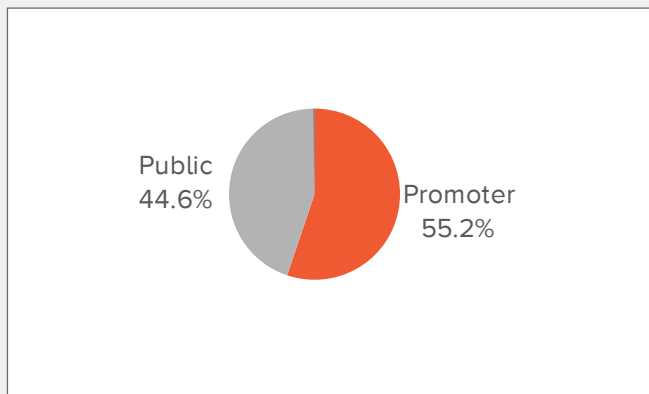
Bajaj Finance

Reco: Buy | CMP: Rs3,023

Company details

Price target:	Rs3,400
Market cap:	Rs174,683 cr
52-week high/low:	Rs3132 / 1819
NSE volume: (No of shares)	17.5 lakh
BSE code:	500034
NSE code:	BAJFINANCE
Sharekhan code:	BAJFINANCE
Free float: (No of shares)	25.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.3	19.7	31.5	56.2
Relative to Sensex	5.7	10.9	17.3	35.7

Key points

- ♦ **Men to be separated from boys:** The NBFC segment is undergoing a significant shift in market approach. Courtesy recent events such as defaults (and subsequent bankruptcy in several cases) of the debt paper of several top-rated corporates, we find that risk tolerance and appetite have been tempered across money markets. We believe this may lead to a possible shift in market approach, giving more importance to ratings and quality of borrower rather than merely chasing yields. As a result, cost of money may be unlike different-rated players, thereby widening the competitive chasm even further. Going forward, we believe high credit ratings will be a clear competitive advantage rather than just be a facilitator. Bajaj Finance Limited (BAF) has maintained its high ratings profile (AAA for its long term, A1+ for its short term and FAAA/stable for fixed deposits) by leading rating agencies in India. The company has also continued to manage its ALM/Cost of Funds (COF) and, thus, NIMs well across rate cycles and its liquidity scenario indicates its business model resilience, which we believe will be sustained if not accentuated going forward.
- ♦ **Growth capital may be another differentiator:** Another shift is that the days of secular high growth phase of NBFCs as a sector are over. Increasingly, due to various structural and environmental challenges, several NBFCs (having weaker business models/balance sheets etc.) are already paring down their growth outlook and margin forecasts. In this scenario, we believe NBFCs with a strong balance sheet/strong business model/backed by a strong parent will be able to buck the trend and would be able to maintain their growth trajectory and margins. Thus, BFL is likely to have ample availability of growth capital at attractive valuations to sustain its high-growth trajectory and further consolidate its leadership position in the retail finance segment.
- ♦ **Higher investment allocation, a tactical factor:** Given the edge BFL commands in the changing business environment, its sustainable high-growth trajectory and limited investment options in the financial space, the company is likely to continue to attract more than fair share of flows from institutional investors, both

domestic and international, despite heady valuations.

- ♦ **Well-diversified balance sheet and steady asset quality:** BAF has a well-diversified loan book with its consolidated AUM mix for consumer, rural, SME, commercial and mortgage at 40%, 8%, 13%, 11% and 28%, respectively (Q3FY2019). Consumer and rural loans continue to contribute a major share in incremental growth. While it has indicated to calibrate growth in segments where it sees risk building up, notably, BAF is also diversifying geographically, expanding its focus on rural business. The company's rural lending branches have increased to 341 (in December 2018), nearly doubled in a short time (from 177 in March 2017; and 50 in March 2015), indicating business diversification. While BAF today has 867 urban locations, it also has 869 rural locations with 13,100+ rural consumer durable stores (from 5,500+ in March 2017 and 1,500 in March 2015), indicating its deepening reach and business diversification. BAF's asset quality continues to remain under control despite the implementation of IND-AS (Indian Accounting Standards). As per expected credit loss method (ECL), its GNPA and NNPA stood at 1.55% and 0.62%, respectively, which we believe is attractive given its pace of growth and scale of book. We believe BAF's strong underwriting process should keep its NPA in
- ♦ **Outlook – Prefer to stick with high-quality business:** At present times, we prefer to stick with a selective stance in the NBFC space. BAF has a strong borrowing profile (high ratings and well-matched ALM profile) and has strong business and operational parameters. We expect the NBFC space is likely to see differentiated performers, with borrowing costs as per their balance sheet/business model strengths, thereby resulting in a differentiated margin play. Consequently, institutional growth capital is likely to favour the outperformers. Finding that BAF checks on the criteria, we believe going forward, its premium may be sustained or be even more accentuated. The ability of BAF to create new product categories, leveraging its large customer base and proactive risk management track record are key positives to support valuations.
- ♦ **Valuation:** BAF currently trades at 5.9x its FY2021E book value. When viewed in perspective of high growth and strong asset quality, we believe these premium valuations are sustainable. We introduce our estimates for FY2021E and rollover the price target (PT). We maintain our Buy rating with a revised PT of Rs. 3,400.

Valuations

	Rs cr				
Particulars	FY17	FY18	FY19E	FY20E	FY21E
Net interest income (Rs cr)	5,469	8,272	11,146	12,852	18,806
Net profit (Rs cr)	1,836	2,559	3,922	4,915	6,398
EPS (Rs)	33.6	44.4	68.0	85.2	111.0
EPS growth (%)	40.6	32.2	53.3	25.3	30.2
PE (x)	90.0	68.7	44.4	35.5	27.2
Book value (Rs/share)	176	284	344	419	517
P/BV (x)	17.2	10.7	8.9	7.3	5.9
RoAE (%)	21.6	19.7	21.7	22.3	23.7
RoAA (%)	3.3	3.3	3.8	3.6	3.5

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