Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Bajaj Finance

Prepared to navigate near-term challenges

Banks & Finance	Sharekhan code: BAJFINANCE	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 4,873**	
Price Target: **Rs. 6,000**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

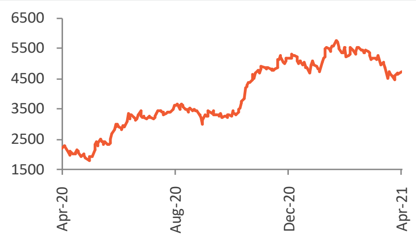
Company details

Market cap:	Rs. 293,667 cr
52-week high/low:	Rs. 5922/1783
NSE volume: (No of shares)	52.3 lakh
BSE code:	500034
NSE code:	BAJFINANCE
Free float: (No of shares)	26.4 cr

Shareholding (%)

Promoters	56.1
FII	24.1
DII	6.4
Others	13.4

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-8.7	-3.5	43.7	131.4
Relative to Sensex	-7.5	-3.6	23.1	78.9

Sharekhan Research, Bloomberg

Summary

- We maintain our Buy rating on the stock of Bajaj Finance Limited's (BFL) with an unchanged price target (PT) of Rs. 6,000.
- Q4FY2021 results were decent with most lead financial indicators normalizing to pre-COVID levels indicating a positive trend.
- Positive management commentary for FY2022; improved bounce rates, higher collection efficiency and overlay provisions make BFL well positioned to navigate challenges.
- BFL is available at 6.6x/5.5x its FY2022E/FY2023E BVPS and valuations are reasonable, backed by business strength, stock has corrected by ~18% from highs and risk reward is favorable for long term investors.

Bajaj Finance Limited's (BFL) Q4FY2021 results were good with most lead financial indicators normalizing to pre-COVID levels indicating a positive trend. Operational numbers were largely in line with estimates but sequentially lower provisions were positives. Asset quality improved on a sequential basis, with GNPA / NNPA at 1.79% / 0.75% which was much lower than proforma GNPA / NNPA of 2.86% / 1.22% which is significant positive. The company holds a management overlay and macro provision of Rs 840 crore as of 31 March 2021. Management commentary on growth and asset-quality outlook for the near term is now more confident and BFL is now looking more sure-footed on growth and credit costs for the medium term, which is encouraging. The management commentary was positive regarding growth and credit cost outlook for FY2022. With improved bounce rates, higher collection efficiency and overlay provisions, the company is well positioned to navigate any temporary stresses on account of second COVID wave. On the operational front, BFL saw NII (Calculated) stable on y-o-y basis, but up 8.4% q-o-q, while PPOP was down 5.5%% y-o-y and was in-line with expectations. The company's assets under management (AUM) were flat. We believe the business transformation steps that are underway for BFL, would not only be positive for business sustainability, scalability, but also position BFL to take advantage of a strong economic upturn expected in FY2022E. Business transformation, as well as relations with Banks partners will help diversify business channels. The drag on margins due to liquidity buffers continued in Q4 as well. We believe armed with factors such as a strong balance sheet, robust risk management, and prudent management, BFL is a strong franchise for the long term and is well placed to ride over medium-term challenges. We maintain our Buy rating on the stock with an unchanged price target (PT) of Rs. 6,000.

Key positives

- Lower Loan losses and provisions for Q4 FY21 was at Rs 1,231 crore as against Rs 1,954 crore in Q4 FY20 and Rs 1,352 crore for Q3 FY21.
- Customer franchise as of 31 March 2021 stood at 48.57 million, from 46.31 million in Q3 FY2021, indicating a strong customer traction. The Company acquired 6.20 million new customers in FY2021.

Key negatives

- Due to higher operating expenses in Q4 FY21 (Recovery commission higher by Rs 140 crore and employee costs higher by Rs 151 crore) the Opex to NIM came in at 34.5% against 31% in Q4 FY20.

Our Call

BFL is reasonable at 6.6x/5.5x its FY2022E/FY2023E BVPS backed by factors like business transition and stabilising growth outlook. BFL commentary indicated the company is today better prepared (compared to last year) to face near-term headwinds of the pandemic resurgence. The stock has corrected by ~18% from its highs and we believe that the risk reward is favorable for long term investors. We believe that with improvement in AUM growth, liquidity drag to reduce, will be positive for margins. Given BFL's strong balance sheet and business strengths, we believe the company is structurally a 20+% ROE business franchise in a normalised steady state basis. We believe BFL's stable leadership, well-capitalised balance sheet, robust risk management, and prudent management make it a strong franchise for the long term, which is well placed to ride over medium-term challenges. We maintain our Buy rating on the stock with an unchanged PT of Rs. 6,000.

Key Risks

Prolonged or intermittent lockdowns may result in slower growth and operational challenges, which along with worsening of economic parameters will pose a challenge.

Valuation Rs cr

Particulars	FY19	FY20	FY21	FY22E	FY23E
Net interest income (Rs cr)	11,762	16,901	17,254	21,455	26,318
Net profit (Rs cr)	3,995	5,264	4,420	8,217	10,005
EPS (Rs)	68.9	87.7	73.5	136.6	166.3
PE (x)	70.8	55.6	66.3	35.7	29.3
Book value (Rs/share)	342	499	614	734	881
P/BV (x)	14.3	9.0	7.9	6.6	5.5
RoE (%)	22.1	20.2	12.8	20.3	20.6
RoA (%)	3.7	3.6	2.5	3.9	3.7

Source: Company; Sharekhan estimates

Key Concall Highlights

Acquisition of customers: The focus of the company is on acquisitions and cross-selling to customers. The company will soon reach the 100 mn customer size. Hence omni- channel sales is what the technology platform brings to the company. Any customer that comes on Bajaj Finserv market belongs to company. And it's a new way to originate customers. The idea is to increase customer wallet share and the engagement. From Q4 onwards to the company will begin to publish the metrics.

Credit cost guidance: Prior to March 31st, the company expected 150-160 BPS for FY2022E. Due to the pandemic, the visibility is not clear. However, not carrying legacy NPAs, and have provision cushion augurs well for the company. Provided there are no further national lockdowns there are localized restrictions , and there is no moratoriums on credit, the company will be able to meet the long term guidance of 25-27% BS growth and 18-20% ROE and current GNPA/NNPA for FY22E.

Pandemic impact: Disruptions is expected to be less intense, and readiness of Bajaj Finance is also much better than last year. Hence the management is positive for the year. Barring a national lockdown, 3-4 large GDP contributing states going into simultaneous lockdown for 3-5 weeks and another moratorium on loan repayment, the company is confident of delivering its long term guidance metrics in FY22.

Better placed compared to last year: Having experienced the first wave, the company believes that a disruption in first quarter could be reasonably mitigated in the balance quarters.

Write-offs: The company has accelerated write off in the quarter of Rs 1,530 crore due to COVID related stress and advancement of its write-off policy and around Rs 500 crores for others. After this write-off, the Company still holds a management overlay and macro provision of Rs 840 crore. Based on the current risk estimates and available management overlay, the company is covered for loan losses and provisions

Growth: Sequential strong movement were seen across all of its 8 segments during Q4 FY2021, hence the Q4 growth was broadbased, and the growth will happen dependent on supporting data.

Banking: No plans shared as of now.

Opex to Income: Current Opex to Income is higher, due to lower growth. The digital initiatives will help to bring down the Opex to Income further down, as operating leverage kicks in the same will likely decline further.

Collection efficiency is higher than pre-COVID levels and is at at an all time high.

Business update: Despite significant disruptions during the second wave, the company remains open for business across geographies. As a high frequency indicator, in the last 7-10 days, the company has continued to originate 50-55% of daily volumes in B2B business, 80-85% in B2C and SME businesses and 40-50% in mortgages. It is confident that second wave would not have any major impact.

Liquidity & borrowing costs: The Company has a liquidity buffer of Rs 16,485 crore as of 31 March 2021. This represents 12.5% of its total borrowing. The Company has paid down over Rs 7,500 crore to various banks in last 2 quarters as part of its strategy to optimize cost of funds and benefit from lower interest rate environment.

Credit Cost: Credit cost came at Rs. 1231 Cr (3.2%) vs YoY Rs. 1953 Cr (5.3%), QoQ Rs. 1352 Cr (3.8%). Credit cost was in line with co's guidance of Rs. 1250 Cr in Q4FY21. FY22 onwards, the Co expects credit cost to revert to pre-COVID-19 levels of 150-170 bps as it does not carry any baggage of NPAs and infact possesses excess provisions of 0.55%. Thus we believe that the company is on track to reach ~19% ROE in FY22E.

Restructuring: Restructuring portfolio is at Rs. 1739 cr vs q-o-q Rs. 2040 Cr. Holding provision coverage for the same book of 20% at Rs 328 Crore.

Write-offs: The company has written off loans worth Rs. 1530 Cr during the quarter and correspondingly the interest outstanding of Rs. 328 Cr by utilizing the contingent provisions. Co holds contingent provision of Rs. 840 Cr (0.55% of AUM).

Asset quality: Gross NPA (%) came at 1.79% vs q-o-q (proforma) 2.87%. Net NPA (%) came at 0.75% vs QoQ (proforma) 1.23%. It has already reached close to pre-Covid NNPA (0.7%) which it had earlier guided to reach by Q3FY22.

Digital: In the last one year, the company has significantly augmented its digital capabilities to remain fully functional for new origination, service, operations and collections in a work from home situation. It continues to remain well invested with 25-30% higher collections infrastructure. All the planned business transformation initiatives are expected to go live by August/September. This will help in accelerating market share as the economic momentum accelerates.

Outlook for FY2022E: Overall, the Company is entering FY22 on a strong footing. Barring a nationwide lockdown or extended lockdowns in large GDP contributing states, the Company is confident of delivering its long-term guidance metrics in FY22.

Results (Consolidated) Rs cr

Particulars	Q4FY21	Q4FY20	YoY %	Q3FY21	QoQ %
Interest Income & Fees	6850.6	7226.6	-5.2	6656.1	2.9
Interest and Other Charges	2195.6	2547.4	-13.8	2362.7	-7.1
Net Interest Income	4655.1	4679.2	-0.5	4293.4	8.4
Other Income	4.3	4.3	1.6	2.4	83.8
Total Operating Income	4659.4	4683.4	-0.5	4295.8	8.5
Employee Expense	768.3	618.1	24.3	678.4	13.3
Depreciation & Amortisation Expenses	89.9	85.3	5.4	79.6	12.9
Other Expenses	747.8	748.1	0.0	631.5	18.4
PPoP	3053.4	3231.9	-5.5	2906.2	5.1
Provisions and Loan losses	1230.8	1953.8	-37.0	1351.7	-8.9
PBT	1822.6	1278.2	42.6	1554.5	17.2
Tax Expense	476.0	330.1	44.2	408.5	16.5
Profit After Tax	1346.6	948.1	42.0	1146.0	17.5

Source: Company; Sharekhan Research

Outlook and Valuation

Sector view - Structural Tailwinds to support

We believe retail players have a large market to grow and recent credit growth of 6+% indicates a pickup in credit offtake, especially in retail and consumer segments. Leading indicators depict recovery in economic activity, which will be a positive. So far, risk metrics of new volumes originated across businesses are tracking better than pre-COVID-19 levels. We believe that retail and consumer lending segments have a long structural growth runway available to them, as India's credit delivery diversifies and penetration increases. In this backdrop, aided by a strong demographic advantage, we believe nimble NBFCs and private banks can co-exist and grow for the foreseeable future as the market expands.

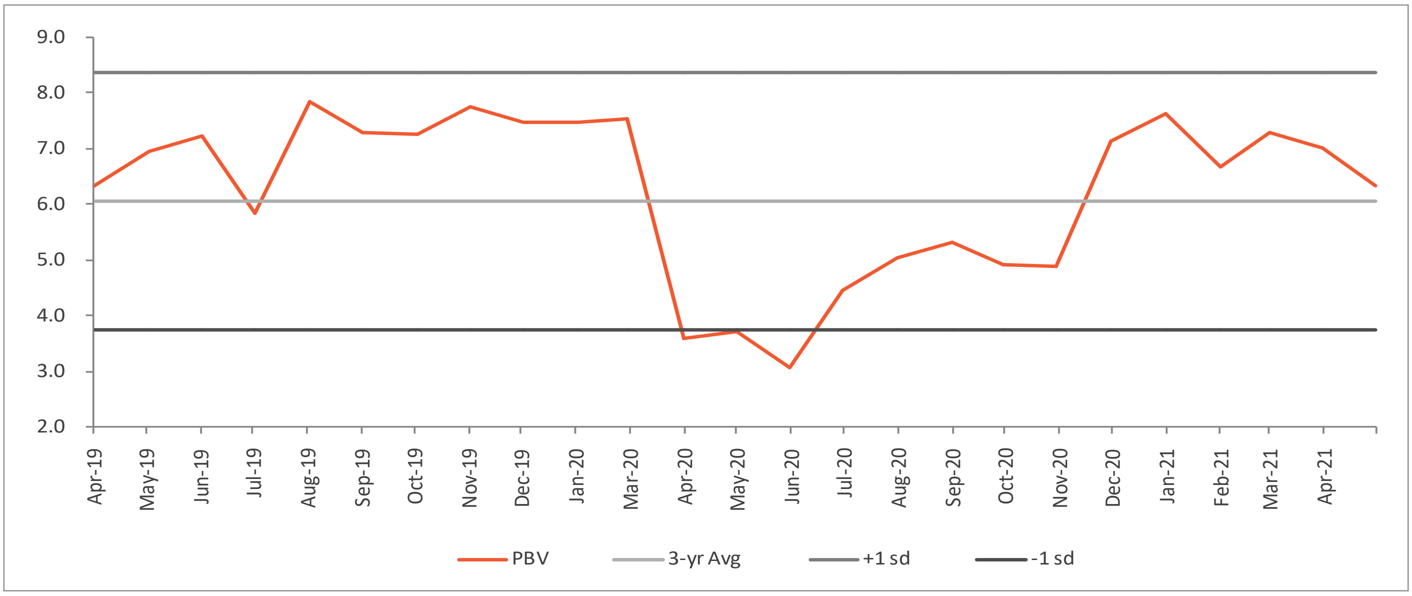
Company outlook - Strong and prudent management, company getting ready for future growth

BFL continues to remain well capitalised with CRAR of 28.3% with Tier-1 capital at a healthy 25.1%. The drag on margins due to liquidity buffers continued in Q4 as well, but as situation normalises, and with return of growth, is expected to wane, which will offer positive support for BFL's margins. Ot is in the middle of a business transformation, which aims to significantly strengthen its technology, data science, app design, and content design to result in a transformed customer experience model for it. We believe there are several business transformation steps that are underway for BFL, which would not only be positive for business sustainability and scalability, but would also position BFL to take advantage of a strong economic upturn expected in FY2022E. Once implemented, this transformation should lead to significantly higher velocity at a much lower cost.

Valuation - Maintained by with an unchanged PT of Rs. 6,000

BFL is reasonable at 6.6x/5.5x its FY2022E/FY2023E BVPS backed by factors like business transition and stabilising growth outlook. BFL commentary indicated the company is today better prepared (compared to last year) to face near-term headwinds of the pandemic resurgence. The stock has corrected by ~18% from its highs and we believe that the risk reward is favorable for long term investors. We believe that with improvement in AUM growth, liquidity drag to reduce, will be positive for margins. Given BFL's strong balance sheet and business strengths, we believe the company is structurally a 20+% ROE business franchise in a normalised steady state basis. We believe BFL's stable leadership, well-capitalised balance sheet, robust risk management, and prudent management make it a strong franchise for the long term, which is well placed to ride over medium-term challenges. We maintain our Buy rating on the stock with an unchanged PT of Rs. 6,000.

One-year forward P/BV (x) band



Source: Bloomberg, Sharekhan Research

Peer valuation

Particulars	CMP (Rs)	P/BV (x)		P/E (x)		RoA (%)		RoE (%)	
		FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Bajaj Finance	4,873	6.6	5.5	35.7	29.3	3.9	3.7	20.3	20.6
HDFC Ltd	2,518	4.5	4.2	39.9	34.1	1.8	1.8	10.4	11.3

Source: Bloomberg, Sharekhan Research

About company

BFL is one of India's largest NBFCs for consumer finance. The company provides loans for two-wheelers, consumer durables, housing, small businesses, construction equipment, and infrastructure finance. BFL undertook business and organisational restructuring in FY2008 and re-defined small business and consumer financing as its key niches. The company operates through 944 urban locations and 951 rural locations, with over 91,700 distribution points. BFL continues to be the largest consumer durables lenders in India. As a business entity, BFL continues to deliver steady performance with well-maintained margins and conservative asset-quality performance.

Investment theme

BFL enjoys a dominant position in the Indian consumer finance space with a strong presence in retail assets and liabilities. Its dominance in the market is seen in the consistent growth and margin performance maintained by the company across credit cycles and rate cycles. During the past few years, BFL has been posting consistently strong growth with high but stable NIMs along with excellent asset quality. The sequential improvement in asset quality is indicative of the company's high focus on risk management and robust credit underwriting capability. Despite the medium-term impact of the pandemic, we expect BFL to maintain its loan book trajectory as well as profitability and margin because of healthy franchise expansion and increasing customer base in the long term.

Key Risks

Prolonged or intermittent lockdowns may result in slower growth and operational challenges, which along with worsening of economic parameters will pose a challenge.

Additional Data

Key management personnel

Mr. Rahul Bajaj	Chairman
Mr. Rajeev Jain	Managing Director
Mr. Rakesh Bhatt	Chief Operating Officer
Mr. Sandeep Jain	Chief Financial Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Republic of Singapore	4.4
2	Maharashtra Scooters Ltd	3.2
3	Axis Asset Management Co Ltd/India	2.5
4	SBI Funds Management Pvt Ltd	1.6
5	BlackRock Inc	1.3
6	Capital Group Cos Inc/The	1.3
7	Vanguard Group Inc/The	1.3
8	FMR LLC	0.9
9	UTI Asset Management Co Ltd	0.7
10	Baron Capital Inc	0.5

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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