

Bandhan Bank

Transformation towards a more predictable model

Diversification across products and regions are strategic priorities of Bandhan Bank. This would transform its business model to be more scalable and sustainable. For this, the bank reinforced its top management, hiring professionals from various private banks. A combination of deepening product penetration and branch penetration across states would drive a 21% loan CAGR over FY23-25. With asset quality issues likely to be peaked out in H2FY23 earnings are expected to normalize thereafter. We believe, on a sustainable basis, Bandhan would deliver 2.5%+ RoA and 25% RoE. We initiate coverage on Bandhan Bank with a BUY rating and a target of Rs 327, valuing the bank at 1.9x FY25e ABV.

Rating : Buy
Target Price : Rs 327
Share Price : Rs 240

Key data	BANDHAN IN
52-week high / low	Rs 350 / 209
Sensex / Nifty	61046 / 18165
3-m average volume	\$31.3m
Market cap	Rs 386bn / \$4756.4m
Shares outstanding	1611m

Shareholding (%)	Dec'22	Sep'22	Jun'22
Promoters	40.0	40.0	40.0
- of which, Pledged	-	-	-
Free float	60.0	60.0	60.0
- Foreign institutions	32.4	34.2	35.6
- Domestic institution	12.5	12.5	17.3
- Public	15.2	13.3	7.1

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Transformation to a diversified asset base

Diversification across consumer finance products and regions (beyond West Bengal and the North-east) are strategic priorities of Bandhan Bank. This would transform its business model to be more scalable and sustainable. (Its group loans business would drop to 28%, from 40% now.) For this, the bank reinforced its top management, hiring professionals from various private banks (slides 10 & 11). A combination of widening product penetration and branch penetration across states such as UP, Gujarat, AP, Telangana and Bihar would drive a 21% loan CAGR over FY23-25



Rural tailwinds, strong brand recall

With rural tailwinds in the offing, we build in high-teen growth for the MFI sector over the next couple of years. Despite little product differentiation and stiff competition among nearly 200 MFI lenders (incl. NBFCs-MFIs, banks and SFBs), our channel checks suggest that Bandhan Bank commands a very strong and recognizable brand name across wide regions. Non-Bandhan customers recognise the brand name and aspire for a loan from it on account of better service, greater ticket sizes and lower cost of interest



Asset quality issues to peak in H2 FY23

The highest Covid-related stress was seen in the contact-intense micro-finance segment, leading to elevated stress among MFIs. Bandhan was severely hit since its core MFI book (60%+ of overall loans) was concentrated in the East and North-East (65%+ of its MFI book). In Q2 FY23, it had ~8% of its EEB book in the SMA 30+ category, amounting to ~Rs45bn. We believe most of this stress from the EEB book would flow through in Q3 FY23 and slippages should start easing from Q4 FY23



On the path toward RoA normalization

The MFI segment overall, incl. Bandhan, is experiencing a strong turnaround with disbursement/collections normalising. With stress related to its EEB likely to be absorbed in the near term, its credit cost is expected to soften from FY24. Stable NIM (7%+), greater efficiencies and credit cost would translate to a 2.8% RoA by FY25, in the top quadrant of returns in the banking sector



Valuation

We pencil in a healthy ~21% loan CAGR over FY22-25 and expect profitability to normalise with the RoA at 2.5%+ and the RoE at 20%+. We initiate coverage on the stock with a Buy rating at a target price of Rs327. This implies a ~1.9x P/ABV multiple on its FY25e book, which has been arrived at using the two-stage Gordon Growth model



Key risks

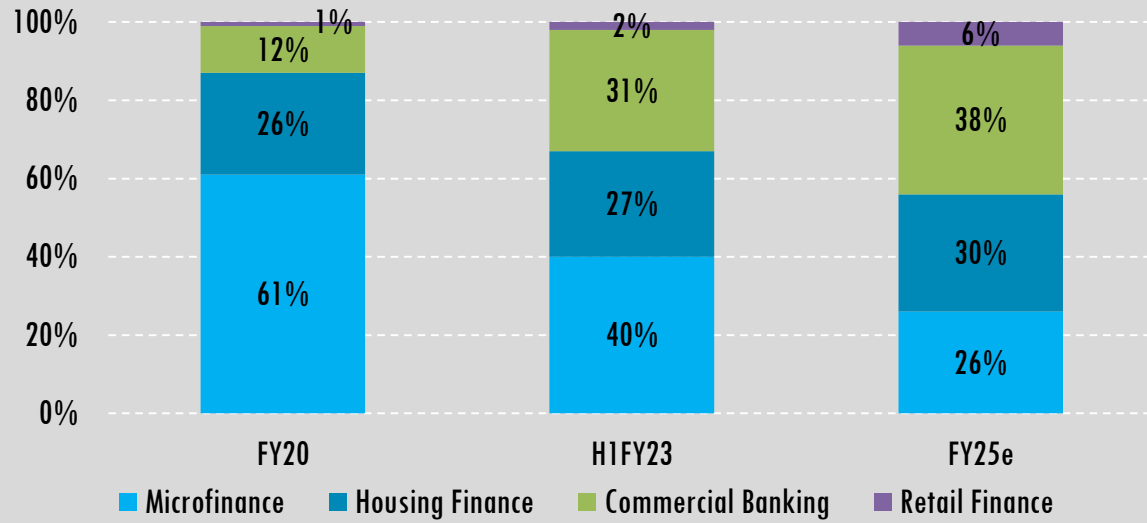
- More-than-expected stress arising from the EEB book
- Less-than-expected loan growth
- External shocks; further Covid waves could markedly hurt the bank's financials

Financial Summary (Rs m)	FY21	FY22	FY23e	FY24e	FY25e
Net interest income (Rs m)	75,634	87,140	95,606	115,644	141,752
Pre-provisioning profit (Rs m)	67,687	80,134	70,623	86,115	108,010
PAT (Rs m)	22,055	1,258	19,501	43,827	57,961
EPS (Rs)	13.7	0.8	12.1	27.2	36.0
NIM (%)	7.8	7.4	6.9	7.2	7.4
Cost-income (%)	29.4	30.5	40.2	39.9	38.4
RoE (%)	13.5	0.7	10.7	20.8	22.6
RoA (%)	2.1	0.1	1.3	2.5	2.8
Advances growth (%)	22.5	15.1	20.0	22.0	22.0
GNPA (%)	6.8	6.5	6.4	4.9	4.2
CAR (%)	23.5	20.1	18.8	19.1	19.6
P / E (x)	17.5	306.0	19.7	8.8	6.6
P / BV (x)	2.2	2.2	2.0	1.7	1.4
P / ABV (x)	2.5	2.4	2.2	1.8	1.4

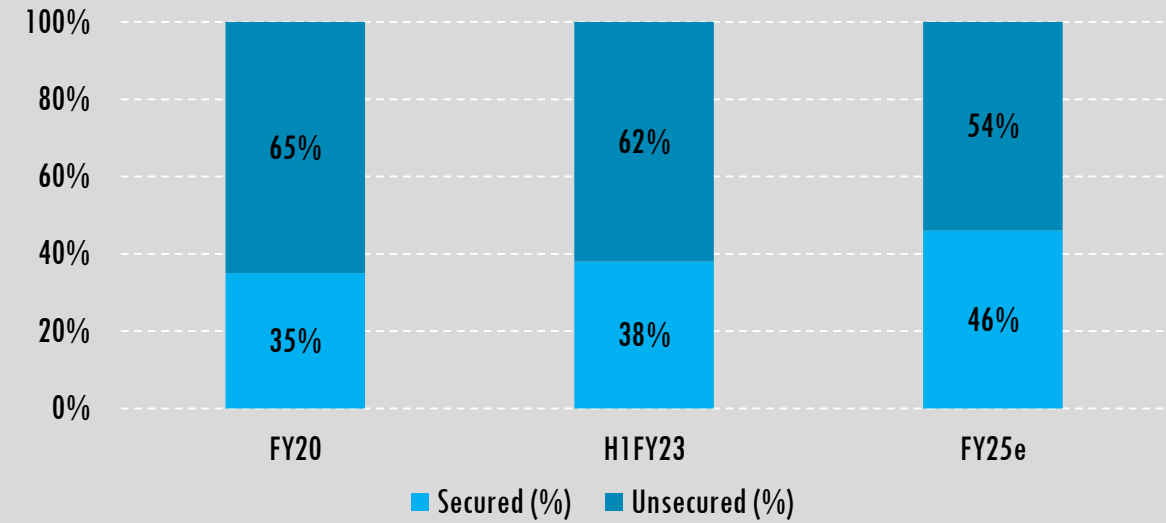
FY25e	Bear Case	Base Case	Bull case
Advances CAGR (FY22-25e), %	16	21	25
BVPS (FY25e), Rs	160	176	196
PBV (multiple)	1.3x	1.9x	3.0x
Catalyst	Higher delinquencies, lower loan growth		Benign asset quality, strong credit demand

Strategy ahead

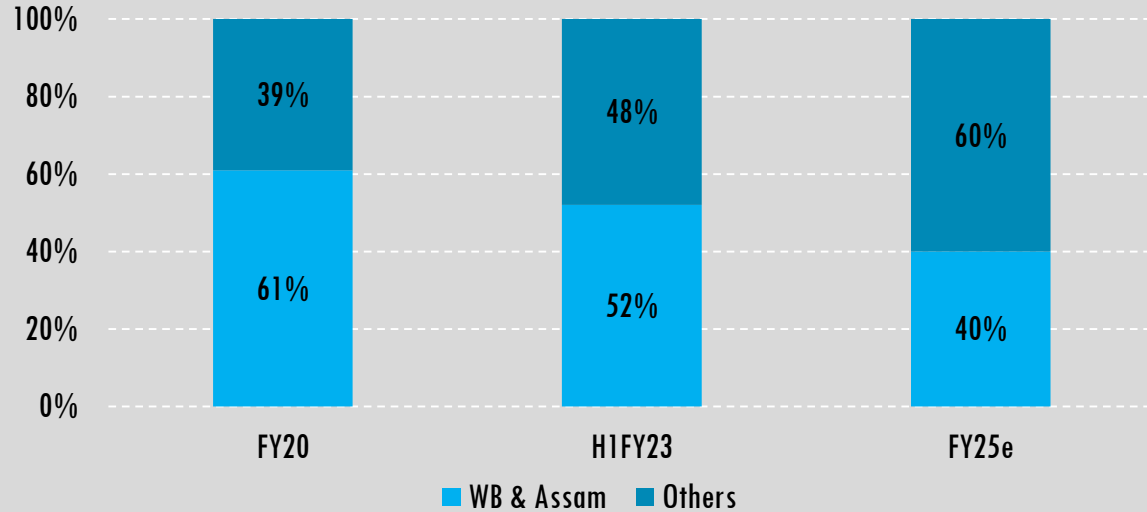
Portfolio-diversification strategy



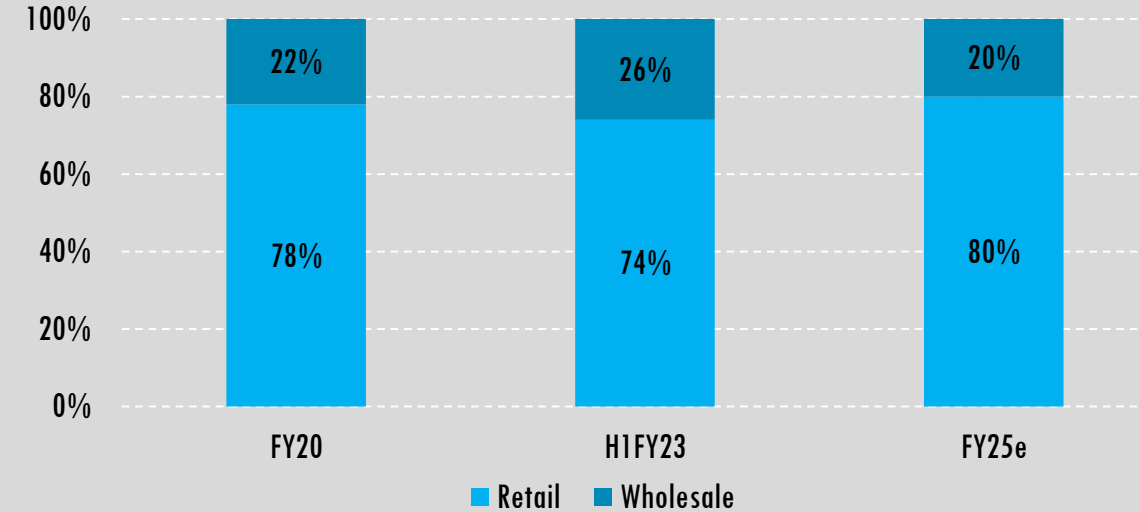
Secured products to be a focus area



Geographically-diversified strategy



Towards a book with more secured assets

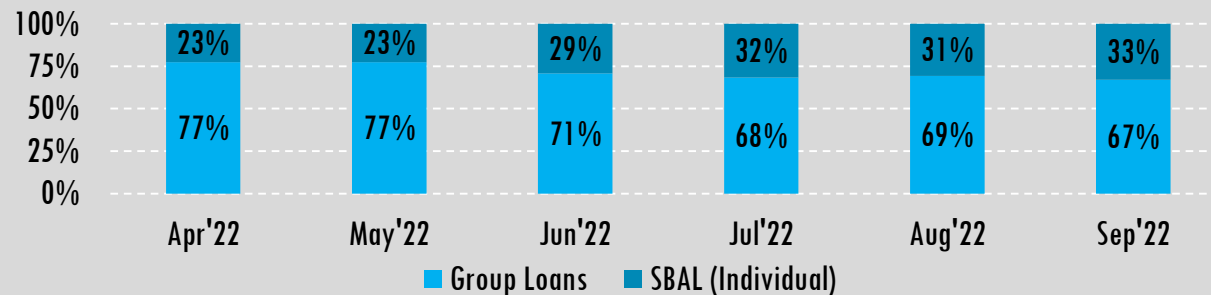


EEB portfolio - sharper focus on individual loans

Particulars	Group loans			SBAL (individual)		
	Mar-22	Jun-22	Sep-22	Mar-22	Jun-22	Sep-22
AUM (Rs bn)	465	429	382	159	152	157
Borrowers (m)	11	11	11.1	1.6	1.7	1.9
Avg. AUM (Rs'000 per borrower)	42	39	35	99	89	83
GNPA (Rs bn)	44	49	45	4	5	6
NNPA (Rs bn)	9.2	10	7.6	0.7	0.9	1.5
GNPA, %	10	11	12	3	3	4
NNPA, %	2.1	2.6	2.2	0.5	0.6	1
Yield, %	17	18	17	17	19	18
Sourcing yields, %	19.45	19.95	19.95	19.45	19.95	19.95

* Sourcing yield on 14th Nov, 2022 was 21.95% for group loans and 21.45% for individual loans

Rising share of individual loans disbursed



- In respect of its EEB portfolio, Bandhan is seeking to diversify outside its core regions of WB and the NE, with most of new distribution planned outside these states through a sharper focus on 'SBAL' (33% of EEB monthly disbursements for Sep'22 vs 23% for Apr'22)
- Target audience for 'SBAL' would be: a) maturing customers from 'group'; and b) NTB customers, whereas, focus for 'group' would be NTB customers. GNPA of individual loans is 4% whereas for group it was 12% in Sep'22, which supports the bank's shift of focus from 'group' to 'SBAL'. Management aims to bring down the EEB group portfolio from 71% in Sep'22 to 53% by FY25

EEB portfolio composition ahead

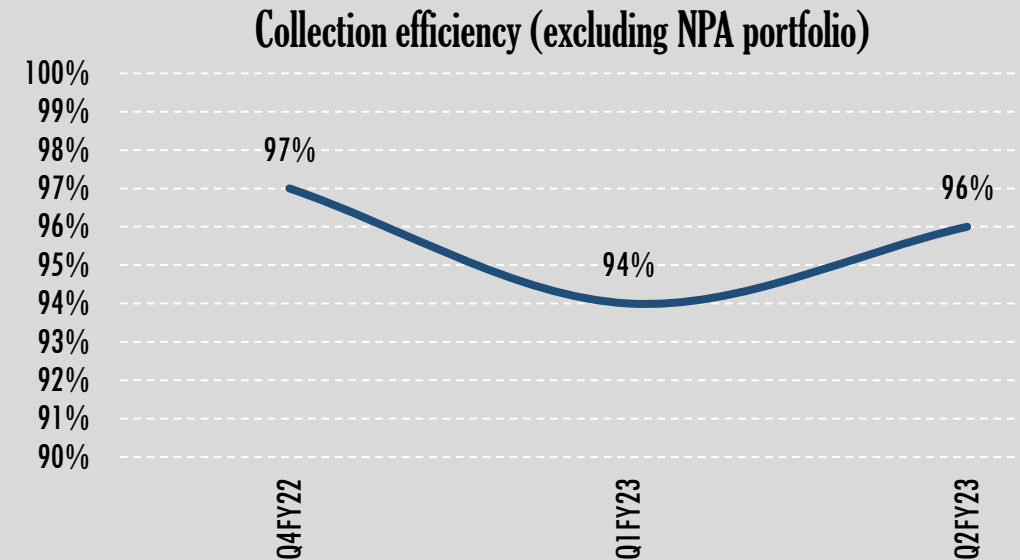
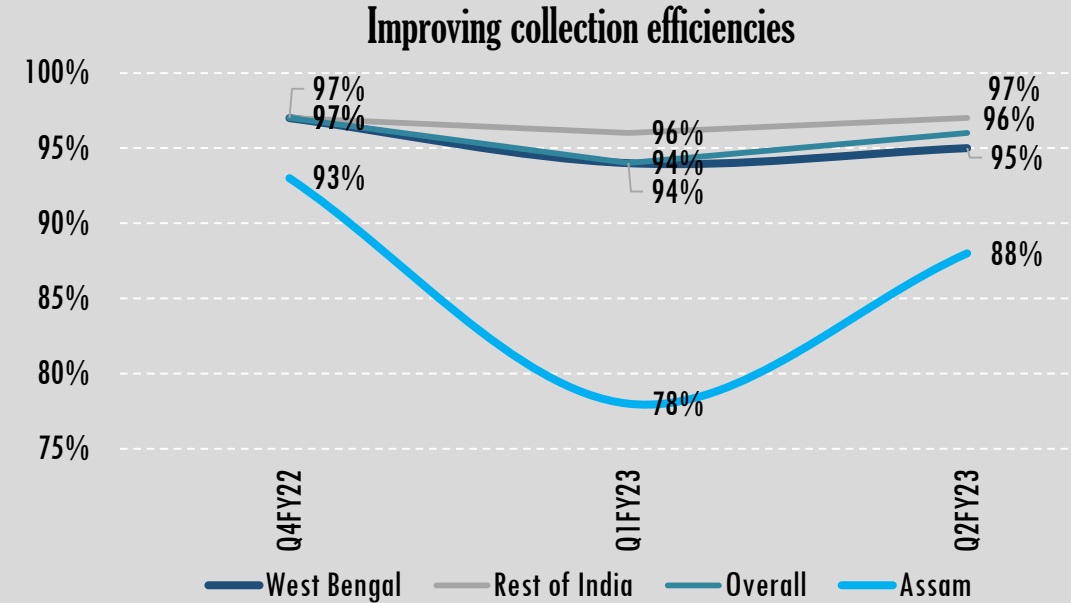
Particulars, %	FY23e	FY24e	FY25e
Group-based	62	56	53
SBAL (Individual-based)	38	44	47
EEB	100	100	100

Collection trends: underlying trends improve

Payment profile of borrowers (Excluding NPA portfolio)

Payment Profile	% of receivables		
	Jun'22	Sep'22	Oct'22
Not paid	3%	3%	1%
Up to 25%	1%	1%	2%
>25% to 50%	1%	1%	1%
>50% to 75%	1%	1%	2%
>75% to <100%	3%	2%	2%
Fully paid	91%	92%	93%

Payment percentage	% of AUM		
	Jun'22	Sep'22	Oct'22
Not paid	6%	5%	2%
Up to 25%	1%	1%	2%
>25% to 50%	1%	2%	1%
>50% to 75%	2%	2%	2%
>75% to <100%	3%	2%	2%
Fully paid	87%	88%	91%



Stress test on the EEB portfolio suggests peaking in H2 FY23

EEB stress book	%	Rs m
Overall EEB book in Q2 FY23		539,200
1-30 days	4.8	25,882
31-60 days	2.6	14,019
61-90 days	5.7	30,734
Overall DPD	13.1	70,635

Expected slippages in Q3 FY23 (Rs m)	Slippages	Provisions*
Expected stress from EEB book		
Bull case		
@ 25% slippages from EEB Overdue book	17,659	14,127
Base case		
@ 50% slippages from EEB Overdue book	35,318	28,254
Bear case		
@ 75% slippages from EEB Overdue book	52,976	42,381
* Assumption of 80% PCR		

Expected provisions (P&L) in H2 FY23 (Rs m)	
EEB provisions Q3 FY23 (<i>base case</i>)	28,254
Non-EEB provisions Q3 FY23 (<i>1.8% credit cost</i>)	1,886
CGFMU recovery	-9,166
Provisions Q4 FY23 (<i>1.8% credit cost on overall loans</i>)	4,364
Total provisions in H2 FY23	25,338
Provisions already in H1 FY23	19,221
Total provisions in FY23	44,559
Credit cost guided to by management (<i>3%-3.15%</i>)	35,523

- We ran a stress test on Bandhan's published figures to arrive at further slippages under various scenarios
- In the base case, we assume slippages of 50% from the EEB overdue (1+ dpd) book
- Based on the scenario shown above, we have built in higher provisions than management guidance

Housing Finance

Driven by growth in Gruh's traditional Western regions, Bandhan aims to expand its housing book and lever its strong presence in the East

- The bank aims to grow its housing book 25%+ in FY23
- The bulk (~80%) of the sourcing for the book is driven by indirect channels (connectors/ DSAs, etc.). These the bank plans to reduce over time as it levers its branch-banking channels
- Yields for this book have crossed pre-Covid'19 levels and are now 10.85%; 98% of the book is floating, of which 68% are linked to repo, which enables faster transmission of rates in a rising interest-rate scenario.

Pillars of Growth			
Expand market reach	Enhance customer value proposition	Evolve platforms	Engage partnerships
<ul style="list-style-type: none"> • Expand in underpenetrated potential regions such as UP, NCR, WB and southern India 	<ul style="list-style-type: none"> • Focus on higher-end affordable segment (Rs0.75m-5m) and expand to the prime segment (Rs5m-50m) with a dedicated channel for sourcing prime mortgages 	<ul style="list-style-type: none"> • Scorecard-based pricing model 	<ul style="list-style-type: none"> • Partner with all stakeholders
<ul style="list-style-type: none"> • Leverage the branch model through hubs & spokes 	<ul style="list-style-type: none"> • Re-launch construction finance in identified markets 	<ul style="list-style-type: none"> • Digital push to offer ease of delivery and quick solutions 	<ul style="list-style-type: none"> • Tie-ups for co-lending
<ul style="list-style-type: none"> • Single-point contact for all products 	<ul style="list-style-type: none"> • Expand range of LAP products; target ETB for value adds 	<ul style="list-style-type: none"> • Enhance data mining and analytics 	<ul style="list-style-type: none"> • Collaborate with builders and aggregators
<ul style="list-style-type: none"> • Strengthen the indirect channel 			
<ul style="list-style-type: none"> • Expand to 600+ branches by FY23, from 350+ now 			

Widening product mix in commercial banking and retail assets

Commercial Banking Products

Institutional lending

SME — MMG (Rs150m-5,000m)

SME — BBG (Rs50m-1,000m)

SME — LAP (Rs2.5m-50m)

Small enterprise loans (up to Rs2.5m)

Retail Asset Products

Gold Loan

Personal Loan

Two wheeler loan

Car Loan (New & Used)

Loan/Overdraft against Term Deposit

CV/CE

Key Management Team

MD & CEO

**Chandra
Shekhar
Ghosh**

MD & CEO

Founder of BFSL; 30 years' experience in the microfinance & development

M.Sc. in statistics; attended the HBS-ACCION course on strategic leadership at Harvard Business School

CFO

**Sunil
Samdani**

CFO

23+ years' experience in the financial sector

Previously, head of business analytics & strategy at Development Credit Bank, and CFO at Karvy

CRO

Biswajit Das

CRO

28+ years' experience in the banking sector

Previously Head-RBS and regulatory reporting at ICICI Bank

Chief Compliance Officer

**Sudheer
Reddy
Govula**

Chief Compliance Officer

27+ years' experience in compliance and policy formulation with SBI and HDFC Bk

Previously handled RBI inspections of HDFC Bk and was member, internal RBS team

EEB Head

**Satyajit
Ghosh**

EEB Head

26+ years' experience in microfinance

Has been a key contributor to the growth of the organisation from an NGO to an NBFC and, finally, to Bandhan Bank

Retail Banking Head

**Shantanu
Sengupta**

Retail Banking Head

27+ years' experience in consumer & commercial banking, retail broking, wealth management, etc.

Previously MD and head, consumer banking at DBS Bank

Key Management Team

Housing Finance Head

Suresh Srinivasan Iyer

Housing Finance Head

23+ years' experience in the mortgage segment

Started at Gruh Finance, then moved to Bandhan as the head of housing finance vertical

Branch Banking Head

Sujoy Roy

Branch Banking Head

22+ years' experience in the banking sector

Previously leadership roles in retail liabilities, branch banking and channels at Axis Bank

Also responsible for the product portfolios of liabilities and NRI banking

Banking ops & Customer Service Head

Nand Kumar Singh

Banking ops & Customer Service Head

26+ years' rich banking experience across various functions

Previously with SBI and Axis Bank

Leads operations, customer service and collections

CTO

Manoj Kumar Mauni

CTO

27+ years' experience in banking, insurance, shipping and the financial sector

Previously Executive Vice President, IT at Kotak Mahindra Bank

Treasury Head

Arvind Kanagasabai

Treasury Head

32+ years' experience in leadership roles in Treasury

Previously CFO of SBI DFHI and member on the board of FIMMDA for four years

Chief Information Officer

Ronti Kar

Chief Information Officer

26+ years' experience in IT

Previously with Cognizant and TCS in various responsibilities and roles

Income statement (Rs m)	FY21	FY22	FY23e	FY24e	FY25e
Net interest income	75,634	87,140	95,606	115,644	141,752
<i>NII growth (%)</i>	<i>19.6</i>	<i>15.2</i>	<i>9.7</i>	<i>21.0</i>	<i>22.6</i>
Non-interest income	20,223	28,228	22,583	27,551	33,612
Total income	95,856	115,368	118,189	143,195	175,364
<i>Total income growth (%)</i>	<i>21.8</i>	<i>20.4</i>	<i>2.4</i>	<i>21.2</i>	<i>22.5</i>
Operating expenses	28,169	35,234	47,566	57,080	67,354
PPOP	67,687	80,134	70,623	86,115	108,010
<i>PPOP growth (%)</i>	<i>24.3</i>	<i>18.4</i>	<i>(11.9)</i>	<i>21.9</i>	<i>25.4</i>
Provisions	38,201	78,848	44,559	27,538	30,543
PBT	29,487	1,286	26,063	58,577	77,468
Tax	7,432	28	6,563	14,750	19,506
PAT	22,055	1,258	19,501	43,827	57,961
<i>PAT growth (%)</i>	<i>(27.3)</i>	<i>(94.3)</i>	<i>1,450.2</i>	<i>124.7</i>	<i>32.2</i>
EPS (Rs)	13.7	0.8	12.1	27.2	36.0

Balance Sheet (Rs m)	FY21	FY22	FY23e	FY24e	FY25e
Share capital	16,106	16,108	16,108	16,108	16,108
Reserves & surplus	157,976	157,704	175,254	214,699	266,864
Net worth	779,722	963,306	1,155,967	1,387,161	1,664,593
Borrowings	169,604	199,212	219,134	241,047	265,152
Other liabilities	26,754	52,336	57,569	63,326	69,659
Total liabilities	1,150,162	1,388,665	1,624,033	1,922,341	2,282,375
Advances	816,129	939,749	1,127,699	1,375,793	1,678,467
Investments	251,554	290,787	319,866	351,852	387,038
Cash & bank balances	62,283	93,214	86,762	85,254	83,352
Fixed & other assets	20,196	64,916	89,706	109,441	133,518
Total assets	1,150,162	1,388,665	1,624,033	1,922,341	2,282,375
No. of shares (m)	1,611	1,611	1,611	1,611	1,611
Deposit growth (%)	<i>36.6</i>	<i>23.5</i>	<i>20.0</i>	<i>20.0</i>	<i>20.0</i>
Advances growth (%)	<i>22.5</i>	<i>15.1</i>	<i>20.0</i>	<i>22.0</i>	<i>22.0</i>

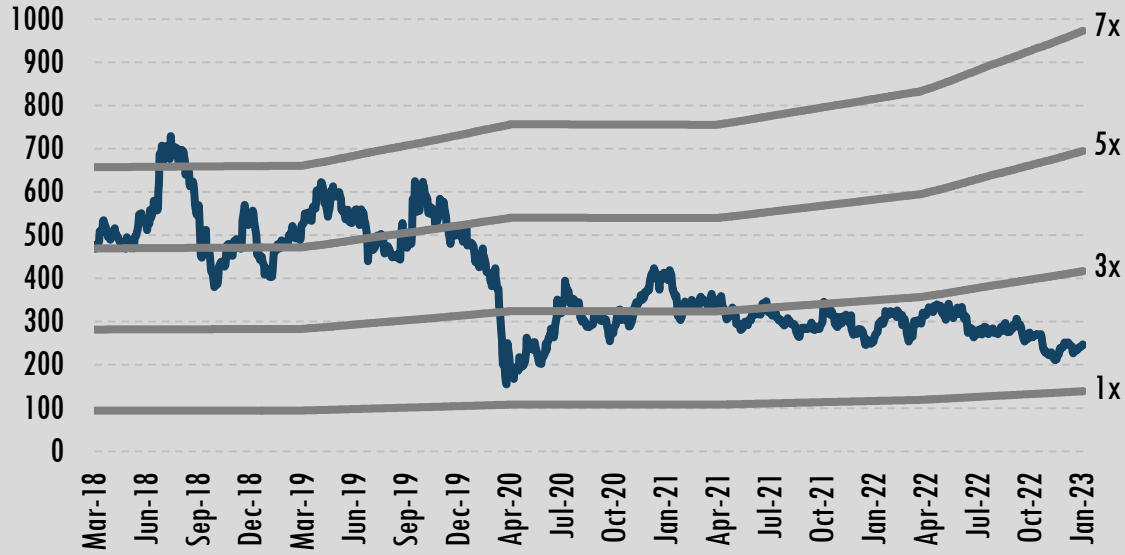
Key Ratios

Key Ratios, %	FY21	FY22	FY23e	FY24e	FY25e
NIM	7.8	7.4	6.9	7.2	7.4
Other inc. / total inc.	21.1	24.5	19.1	19.2	19.2
Opex/avg advances	3.8	4.0	4.6	4.6	4.4
Provisions/avg loans	5.8	5.9	4.3	2.2	2.0
Cost-income	29.4	30.5	40.2	39.9	38.4
DPS (Rs)	1.0	0.0	1.2	2.7	3.6
Credit-deposit	104.7	97.6	97.6	99.2	100.8
Investment-deposit	32.3	30.2	27.7	25.4	23.3
Gross NPA	6.8	6.5	6.4	4.9	4.2
Net NPA	3.5	1.7	1.6	1.2	1.1
Provision coverage	50.3	75.5	75.0	75.0	75.0
BV (Rs)	108.1	107.9	118.8	143.3	175.7
Adj. BV (Rs)	95.7	101.1	111.0	135.9	168.0
CAR	23.5	20.1	18.8	19.1	19.6
- Tier 1	22.5	18.9	17.8	18.2	18.9
RoE	13.5	0.7	10.7	20.8	22.6
RoA	2.1	0.1	1.3	2.5	2.8

Du Pont analysis (%)	FY21	FY22	FY23e	FY24e	FY25e
Interest Income/Assets	12.1	10.9	11.0	11.9	12.2
Interest Expense/Assets	4.8	4.1	4.6	5.4	5.4
Net interest income/Assets	7.3	6.9	6.3	6.5	6.7
Non interest income/Assets	2.0	2.2	1.5	1.6	1.6
Net revenues/Assets	9.3	9.1	7.8	8.1	8.3
Operating expense/Assets	2.7	2.8	3.2	3.2	3.2
PPOP/Assets	6.5	6.3	4.7	4.9	5.1
Provision/Assets	3.7	6.2	3.0	1.6	1.5
Taxes/Assets	0.7	0.0	0.4	0.8	0.9
ROA	2.1	0.1	1.3	2.5	2.8
ROAE	13.5	0.7	10.7	20.8	22.6

Valuation

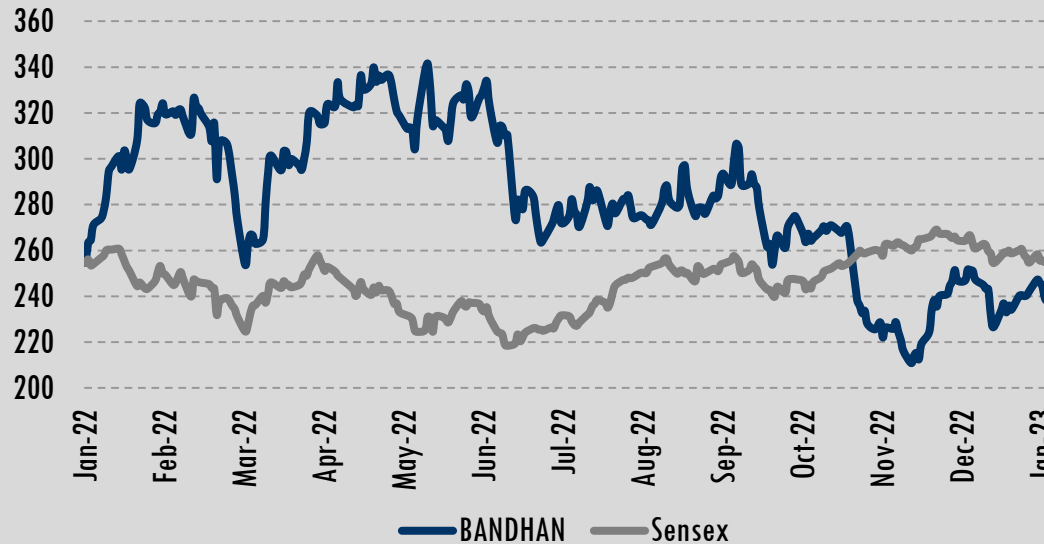
1-year forward P/B – currently at past low valuations



1-year forward S/D – trading below mean valuations



Relative price performance



Valuation - Peer comparison

	M.Cap	CMP	P/B				P/E				BV				EPS			
	(Rs m)	(Rs)	FY22	FY23e	FY24e	FY25e	FY22	FY23e	FY24e	FY25e	FY22	FY23e	FY24e	FY25e	FY22	FY23e	FY24e	FY25e
Bandhan	386,117	240	2.2	2.0	1.7	1.4	NM	19.8	8.8	6.7	107.9	118.8	143.3	175.7	0.8	12.1	27.2	36.0
SFBs																		
Ujivan SFB	56,388	29	1.9	1.5	1.2	1.0	NM	7.1	6.5	5.5	15.1	19.7	23.7	29.2	-2.4	4.1	4.5	5.3
Equitas SFB	70,743	56	1.7	1.5	1.3	1.1	23.2	13.2	9.4	7.4	33.9	37.7	43.2	51.0	2.4	4.3	6.0	7.6
MFIs																		
Credit Access	139,505	893	3.5	2.9	2.4	1.9	38.3	17.8	13.0	10.3	255.2	303.8	372.0	461.4	23.3	50.3	68.9	86.5
Fusion	41,093	408	2.5	1.9	1.6	1.4	NM	11.6	8.0	6.1	161.7	214.4	252.0	300.4	2.6	35.1	51.1	67.1
Spandana	40,879	576	1.3	1.3	1.1	1.0	57.3	43.7	10.9	6.9	446.9	453.9	508.6	585.9	10.1	13.2	52.9	83.6

Appendix

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The views expressed in this Research Report accurately reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this report. The research analysts are bound by stringent internal regulations and also legal and statutory requirements of the Securities and Exchange Board of India (hereinafter "SEBI") and the analysts' compensation are completely delinked from all the other companies and/or entities of Anand Rathi, and have no bearing whatsoever on any recommendation that they have given in the Research Report.

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Ratings Guide (12 months)	Buy	Hold	Sell
Large Caps (>US\$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US\$1bn)	>25%	5-25%	<5%

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