

Baid Finserv Limited

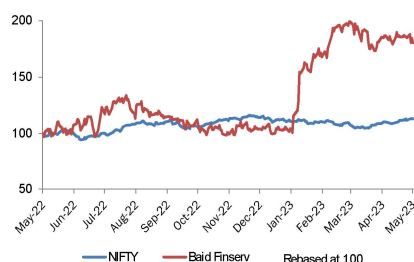
12 May 2023

Leveraging the credit gap in underserved markets

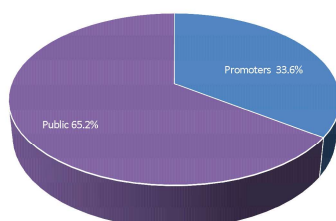
BUY

Sector	: Finance - NBFC
Target Price	: ₹48
Last Closing Price	: ₹35
Market Cap	: ₹420 crore
52-week High/Low	: ₹40/16
Daily Avg Vol (12M)	: 71,670
Face Value	: ₹2
Beta	: 0.42
Pledged Shares	: 0.0%
Year End	: March
BSE Scrip Code	: 511724
NSE Scrip Code	: BAIDFIN
Bloomberg Code	: BAIDFIN IN
Reuters Code	: BAID.BO
Nifty	: 18,297
BSE Sensex	: 61,905
Analyst	: Research Team

Price Performance



Shareholding Pattern



Initiating Coverage

Investment Summary

- Jaipur-headquartered Baid Finserv Limited is an NBFC offering LAP, vehicle financing, and SME loans. The company operates in the states of Rajasthan and Madhya Pradesh through 30 branches.
- Playing a critical role in the financial sector by extending credit to underserved segments, the NBFC sector's total asset is expected to grow by 18% CAGR from FY20 to FY25. Baid Finserv operates in markets having credit gaps with LAP being its predominant product.
- Despite the challenges posed by the Covid-19 pandemic, India's economy has shown remarkable resilience with businesses bouncing back strongly since the end of the third wave of Covid in early 2022. India's credit growth outlook is optimistic with credit offtake expected to remain healthy through FY24. The NBFC sector has been one of the key drivers of banks' credit growth in the recent past, suggesting strong demand for funds from NBFCs for on-lending.
- With RBI's benchmark policy rate closing in on its peak for this cycle and demand bouncing back with the resumption of normal business activities following 2 years of slump due to Covid, we expect credit offtake to be healthy, especially in the underserved segments and the unorganised sector.
- Baid Finserv targets a credit growth rate of 22% to 25% over the next 3 years to touch Rs 600 crore in loan assets by the end of FY26 as it looks to expand its distribution network to 75 branches by the end of FY25. As of December 2022, Baid Finserv reported healthy asset quality with a GNPA ratio of 2.68% and NNPA ratio of 0.40%.
- The Baid Finserv stock currently trades at an attractive forward P/B of 2.2x FY25E BVPS. Assigning a target multiple of 3.0x FY25E BVPS, our valuation informs a price target of Rs 48 with an upside potential of 37%, as we initiate coverage on Baid Finserv with a BUY rating.

Key Financial Metrics

₹ lakh	FY20A	FY21A	FY22A	FY23E	FY24E	FY25E
Interest income	6,204.7	5,329.7	4,959.2	5,307.2	6,451.5	7,986.8
Total income	6,278.7	5,410.9	5,005.3	5,518.1	6,690.1	8,268.9
Net interest income	3,100.0	2,924.0	2,999.2	3,460.8	4,114.1	4,924.3
Net interest margin	9.9%	10.0%	10.8%	11.4%	11.2%	10.7%
PPOP	1,429.7	1,359.2	1,652.4	1,846.6	2,240.9	2,623.5
Operating margin	22.8%	25.1%	33.0%	33.5%	33.5%	31.7%
PAT	760.8	748.0	878.7	1,018.7	1,278.0	1,462.3
PAT margin	12.1%	13.8%	17.6%	18.5%	19.1%	17.7%
Diluted EPS (₹)	6.34	6.23	7.32	0.85	1.06	1.22
BVPS (₹)	108.29	114.58	121.45	13.89	14.86	15.98

Note: FY23 onwards, EPS and BVPS are based on an increased number of outstanding shares following a 1:5 stock split and a 1:1 bonus issue

Source: Company data, Khambatta Research

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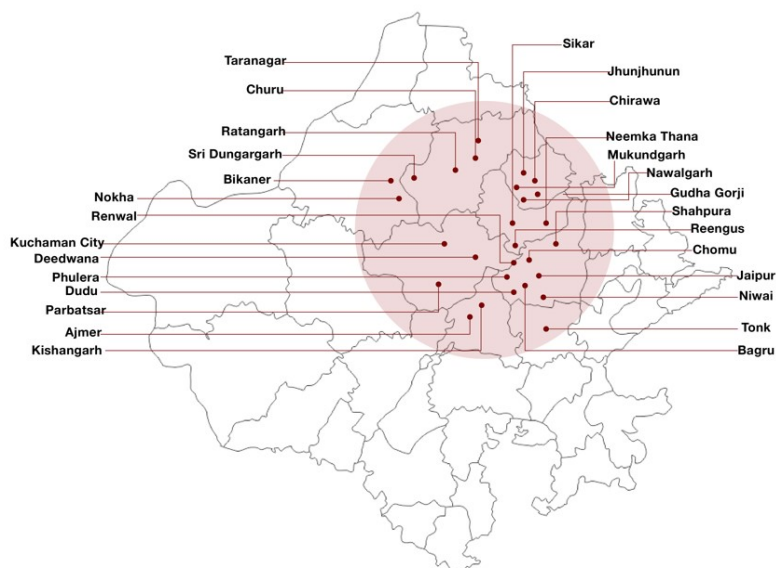
Baid Finserv operates in the states of Rajasthan and Madhya Pradesh via 30 branches

Company Profile

Baid Finserv Limited, formerly known as Baid Leasing and Finance Company Limited, was incorporated in 1991. The Jaipur-headquartered company changed its name in July 2022. Baid Finserv is a Non-Banking Finance Company (NBFC) registered with the Reserve Bank of India (RBI), offering loan against property (LAP), vehicle financing, and SME loans.

The company currently operates in the states of Rajasthan and Madhya Pradesh through 30 branches. With a plan to rapidly expand its touchpoints, Baid Finserv envisages to end FY25 with 75 branches. Management estimates to have finished the last financial year with a loan book size of Rs 320 crore as it targets to grow by a CAGR of 22%-25% in the next 3 years to reach Rs 600 crore in loans by the end of FY26.

Baid Finserv's branch network in Rajasthan



Source: Company website

When Baid Finserv launched its business 28 years ago, it primarily provided new vehicle finance. In 2015, the company added MSME loans and loans against property (LAP) to its product portfolio. The main products of the company include the following.

MSME Loan: Baid Finserv offers loans to businesses operating in the MSME segment for their various needs such as working capital financing and capital expenditure requirements in the trading, manufacturing and service sectors.

Loan against Property: Baid Finserv provides customized LAP products to salaried and self-employed individuals.

Vehicle Loan: Baid Finserv provides loan for both new and used vehicles. The company offers financing for most types of commercial vehicles (CVs)

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including buses, trucks, tankers, trailers, light commercial vehicles (LCVs) and small commercial vehicles (SCVs), whilst also providing balance transfer facilities and top-up loans.

The company's mortgage loan portfolio (LAP and MSME combined) comprises around 90% of its overall loan book.

Baid Finserv's branch network in Madhya Pradesh



Source: Company website

Investment Thesis

NBFCs have strong growth prospects as they exploit the credit gap in the market.

NBFCs play a critical role in the Indian financial sector, especially in providing credit to underserved segments of the economy. The NBFC sector's total asset size stood at Rs 36.6 lakh crore as of March 2020, growing to Rs 54 lakh crore by March 2022. It is expected to grow at a CAGR of 18% from FY20 to FY25. Baid Finserv operates in 3 market segments having significant credit gaps with mortgage loans being its predominant and most important product category.

MSME credit: A significant challenge faced by India's MSME sector is access to credit. NBFCs have been instrumental in addressing this challenge by reducing the credit gap in the segment. The credit disbursed to MSMEs by NBFCs stood at Rs 2.49 lakh crore as of March 2020, accounting for 17.6% of the total credit disbursed to the sector. The MSME sector's contribution to India's GDP is expected to grow from 31% in FY17 to 50% by FY25 with NBFCs expected to play a crucial role in financing this growth.

Loan Against Property: LAP is an important product for NBFCs which has seen significant growth in recent years. As per a report by ICRA, LAP credit

The NBFC sector is expected to grow at a CAGR of 18% from FY20 to FY25

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in India is expected to grow at a CAGR of 22% from FY20 to FY25, driven by an increasing demand for affordable housing and growth in the mortgage market. LAP is a secured lending product and consequently has a lower risk profile compared to unsecured loans. As per RBI data, LAP credit disbursed by NBFCs stood at Rs 2.55 lakh crore as of March 2020, accounting for 21% of the total credit disbursed by the sector.

Commercial vehicle financing: The CV financing market has a positive outlook due to the government's infrastructure push and increasing demand for e-commerce and logistics services. The Indian government's focus on infrastructure development, especially the highway and road infrastructure development project Bharatmala Pariyojana, is expected to drive demand for CVs. According to a report by ICRA, the CV financing segment is expected to grow at a CAGR of 8-10% from FY20 to FY25. NBFCs have been instrumental in providing credit to the segment with the total credit disbursed to the CV segment by NBFCs standing at Rs 2.71 lakh crore as of March 2020, accounting for 22.6% of the overall credit disbursed by the sector.

Despite the growth potential, NBFCs face several challenges in sustaining their growth momentum. One of the significant challenges is asset-liability management, given the asset-liability mismatches that can arise due to a difference in the maturity periods of assets and liabilities. Liquidity risk is another challenge, given the dependence on short-term funding sources. A further challenge is credit risk, given the higher risk profile of the customers they cater to. NBFCs need to address these issues through effective risk management to sustain their growth momentum and continue to play a crucial role in the Indian financial sector.

India's economic and credit growth outlook

Despite the challenges posed by the Covid-19 pandemic, India's economy has shown remarkable resilience with businesses bouncing back strongly since the end of the third wave of Covid in early 2022. The World Bank estimates the Indian economy to have grown by 6.9% in FY23 whilst pegging FY24's growth forecast at 6.3%.

One of the key drivers of India's economic growth is its young workforce which is expected to remain a major advantage in the coming years. Additionally, the government's focus on initiatives such as Make in India and Digital India is expected to boost the manufacturing and technology sectors, respectively. Another area of focus for India's economic growth is its infrastructure development with the government investing heavily in roads, railways, airports and ports. This is expected to boost trade and commerce, create jobs, and further fuel economic growth.

However, like any growing economy, India faces its fair share of challenges. These include issues such as inflation, fiscal deficit, and non-performing assets at lending institutions. Addressing these challenges will be crucial in ensuring sustained GDP growth and macroeconomic stability.

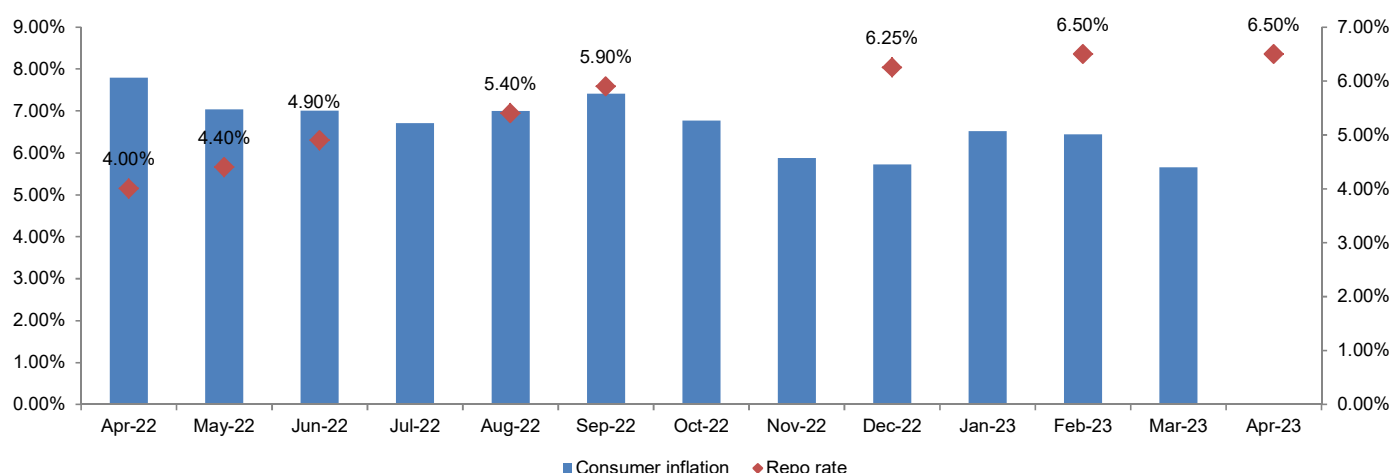
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India's credit growth outlook is optimistic with credit offtake expected to remain healthy through FY24. Moody's Investors Service maintains a stable outlook for India's banking sector in spite of concerns raised by a report on the Adani Group. The asset quality of banks is predicted to be stable with non-performing loan ratios declining modestly. The NBFC sector has been one of the key drivers of banks' credit growth in the recent past, suggesting strong demand for funds from NBFCs for on-lending. The credit growth was broad-based in FY23 with the retail (including vehicle loans) and MSME segments witnessing especially strong offtake. In spite of concerns over rising interest rates, inflationary pressures, and softness in the job market, Moody's expects capital, funding and liquidity at banks to remain stable, supporting credit growth.

Policy rate action vis-à-vis consumer inflation in India



Source: tradingeconomics.com, RBI

With interest rates seen nearing peak as credit offtake, especially in underserved markets expected to remain buoyant

The RBI has raised the repo rate by 250 bps cumulatively to 6.5% over six consecutive rate actions since May 2022

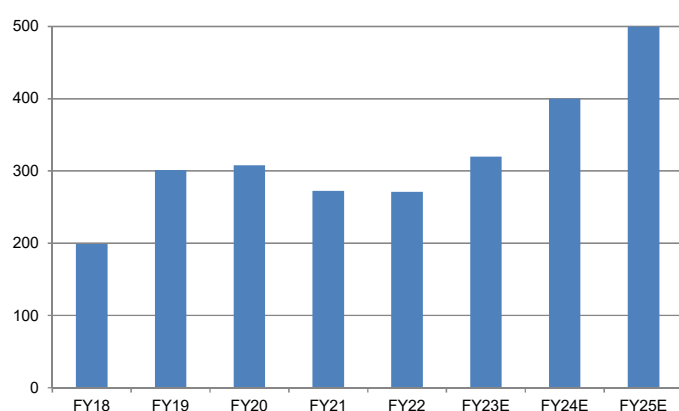
The current rate-hike cycle began in May 2022. The RBI has since raised the repo rate by 250 bps cumulatively over six consecutive rate actions, from 4.0% to 6.5%. The central bank decided to take a pause when its monetary policy body met in April this year. Between May 2020 and May 2022, the RBI kept the repo rate constant at 4%. Before that, between January 2015 and May 2020, the money market saw a rate-cut cycle during which the repo was cut to half from 8% to 4% over around 5 years. Between January and October 2022, the consumer inflation rate did not go below 6% with the period between March and October it remaining above or just under 7%. Whilst the inflation rate eased to 5.66% in March 2023 from 6.44% the month before, it is too early to assume that the trajectory of price rise has changed course with inflation dropping to 5.88% and 5.72% in November and December of last year, respectively to shoot past 6% again in January

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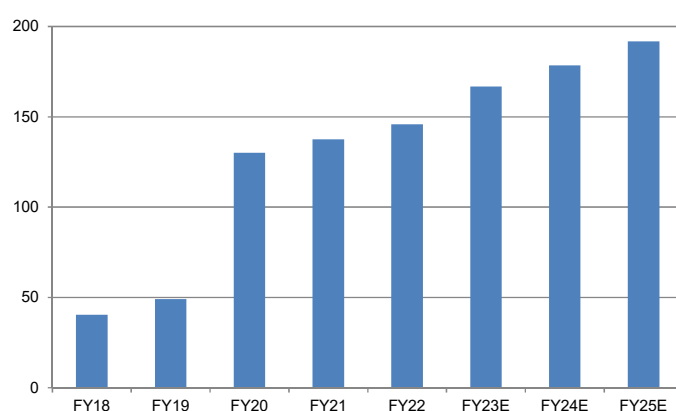
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2023. If inflation rises further or remains sticky at current levels, we say see more rate hikes to the tune of 25-50 bps before the policy rate peaks out. Consequently, lending rates are not expected to fall in FY24 whilst remaining steady or falling marginally in FY25. That said, with the policy rate closing in on its peak for this cycle and demand bouncing back with the resumption of normal business activities following 2 years of slump due to Covid, we expect credit offtake to be healthy, especially in the underserved segments and the unorganised sector.

Loan book (Rs crore)



Net worth (Rs crore)



Source: Company data, Khambatta Research

Baid Finserv targets a credit growth rate of 22% to 25% over the next 3 years to touch Rs 600 crore in loan assets by the end of FY26

Growth strategy, capital, risk management and asset quality

With an estimated Rs 320 crore loan book at the end of FY23, Baid Finserv targets a credit growth rate of 22% to 25% over the next 3 years to touch Rs 600 crore in loan assets by the end of FY26. The company plans to achieve this target by sourcing business via its distribution network comprising sales agents and expansion of its branch network to 75 branches by the end of FY25. Baid Finserv recently tied up with certain banks for co-lending which is expected to add to its growth in the coming years with an annual target of Rs 50-60 crore in loans. The company generates a spread of 7%-8% over a blended borrowing cost in the range of 11.50%-11.75%. Approximately 65% of borrowings are procured from banks (with a significant share from PSBs) whilst most of the remainder is raised from impact investment funds. Baid Finserv reported a robust capital adequacy ratio of 51.3% as of December 2022, providing it ample elbow room to exponentially grow its loan book. A secured loan book with a loan-to-value (LTV) ratio of 45%-50% for MSME loans and LAP, and 75%-80% for vehicle finance contributes positively to risk management, with approximately 80% of vehicles financed being Mahindra and Tata products. The company uses a proprietary credit scoring mechanism/tool developed by its team for credit evaluation and risk management. As of December 2022, Baid Finserv reported healthy asset quality with a GNPA ratio of 2.68% and NNPA ratio of 0.40% (vs 3.34% and 1.02% in March 2022).

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The Baid Finserv stock currently trades at an attractive forward P/B multiple of 2.2x FY25E BVPS

Valuation

At 3.0x FY25E BVPS, we initiate Baid Finserv with a BUY rating, based on a price target of Rs 48 and an upside potential of 37%. We have modelled an average credit growth rate of 25% and interest income (gross) growth of above 17% over FY24E and FY25E for Baid Finserv. The strong top-line growth is expected to drive a solid expansion in earnings and net worth. The Baid Finserv stock currently trades at an attractive forward Price-to-Book Value (P/B) of 2.2 FY25E Book Value Per Share (BVPS). Backed by robust asset quality and solid earnings growth (~20% over the next 2 years and potential to grow faster subsequently driven by the planned expansion of business), translating into a healthy long-term growth rate of net worth, we assign a target multiple of 3.0x FY25E BVPS to arrive at a price target of Rs 48 with an upside potential of 37%, as we initiate coverage on Baid Finserv with a BUY rating.

Profit & Loss Account

₹ lakh	FY20A	FY21A	FY22A	FY23E	FY24E	FY25E
Interest income	6,204.7	5,329.7	4,959.2	5,307.2	6,451.5	7,986.8
Total income	6,278.7	5,410.9	5,005.3	5,518.1	6,690.1	8,268.9
Interest expense	3,104.7	2,405.7	1,960.1	1,846.4	2,337.4	3,062.5
Net interest income	3,100.0	2,924.0	2,999.2	3,460.8	4,114.1	4,924.3
Net interest margin	9.9%	10.0%	10.8%	11.4%	11.2%	10.7%
Non-interest income	74.1	81.1	46.0	210.8	238.6	282.1
Operating expenses	1,744.4	1,645.9	1,392.8	1,825.1	2,111.8	2,582.9
Pre-provision operating profit	1,429.7	1,359.2	1,652.4	1,846.6	2,240.9	2,623.5
Operating margin	22.8%	25.1%	33.0%	33.5%	33.5%	31.7%
Impairment on financial instruments	393.5	330.3	437.1	458.2	533.0	667.3
PBT	1,036.1	1,028.9	1,215.3	1,388.3	1,707.9	1,954.1
Tax expense	275.2	281.0	336.5	369.6	429.9	491.9
PAT	760.8	748.0	878.7	1,018.7	1,278.0	1,462.3
PAT margin	12.1%	13.8%	17.6%	18.5%	19.1%	17.7%
Diluted EPS (₹)	6.34	6.23	7.32	0.85	1.06	1.22

Note: FY23 onwards, EPS is based on an increased number of outstanding shares following a 1:5 stock split and a 1:1 bonus issue

Source: Company data, Khambatta Research

Abridged Balance Sheet

₹ lakh	FY20A	FY21A	FY22A	FY23E	FY24E	FY25E
Loans	30,809.6	27,249.1	27,111.9	32,000.0	40,000.0	50,000.0
Investments	345.3	323.3	857.6	731.4	1,000.0	1,333.3
Other financial assets	762.1	998.3	650.3	640.0	720.0	850.0
Non-financial assets	907.6	714.8	893.8	1,019.7	1,120.0	1,264.7
Total assets	34,055.6	31,649.6	31,783.6	36,456.7	44,743.5	54,914.0
Borrowings	18,859.9	16,390.6	15,977.2	18,285.7	25,000.0	33,333.3
Other financial liabilities	1,572.2	1,000.6	659.6	824.5	1,071.8	1,393.3
Non-financial liabilities	73.7	54.2	61.7	74.1	88.9	106.7
Total equity	13,002.4	13,757.5	14,582.8	16,682.1	17,840.0	19,182.2
Total equity & liabilities	34,055.6	31,649.6	31,783.6	36,456.7	44,743.5	54,914.0

Source: Company data, Khambatta Research

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Key Ratios

	FY20A	FY21A	FY22A	FY23E	FY24E	FY25E
Net interest margin	9.9%	10.0%	10.8%	11.4%	11.2%	10.7%
Pre-provision operating margin	22.8%	25.1%	33.0%	33.5%	33.5%	31.7%
PAT margin	12.1%	13.8%	17.6%	18.5%	19.1%	17.7%
EPS (₹)	6.34	6.23	7.32	0.85	1.06	1.22
BVPS (₹)	108.29	114.58	121.45	13.89	14.86	15.98

Note: FY23 onwards, EPS and BVPS are based on an increased number of outstanding shares following a 1:5 stock split and a 1:1 bonus issue

Source: Company data, Khambatta Research

Key Risks

- Due to its relatively small scale of business and operating in an intensely competitive market with a large number of both formal and informal players, any significant loss of business or inability to grow in line with our expectations will lead to underperformance of our expectations.
- The market segment Baid Finserv operates in generally poses a higher risk of default.
- Being a small lender with limited geographical reach, Baid Finserv faces concentration risk.
- Baid Finserv operates in a rigorously regulated sector.

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Guide to Khambatta's research approach

Valuation methodologies

We apply the following absolute/relative valuation methodologies to derive the 'fair value' of the stock as a part of our fundamental research:

DCF: The Discounted Cash Flow (DCF) method values an estimated stream of future free cash flows discounted to the present day, using a company's WACC or cost of equity. This method is used to estimate the attractiveness of an investment opportunity and as such provides a good measure of the company's value in absolute terms. There are several approaches to discounted cash flow analysis, including Free Cash Flow to Firm (FCFF), Free Cash Flow to Equity (FCFE) and the Dividend Discount Model (DDM). The selection of a particular approach depends on the particular company being researched and valued.

ERE: The Excess Return to Equity (ERE) method takes into consideration the absolute value of a company's return to equity in excess of its cost of equity discounted to the present day using the cost of equity. This methodology is more appropriate for valuing banking stocks than FCFF or FCFE methodologies.

Relative valuation: In relative valuation, various comparative multiples or ratios including Price/Earnings, Price/Sales, EV/Sales, EV/EBITDA, Price/Book Value are used to assess the relative worth of companies which operate in the same industry/industries and are thereby in the same peer group. Generally our approach involves the use of two multiples to estimate the relative valuation of a stock.

Other methodologies such as DuPont Analysis, CFROI, NAV and Sum-of-the-Parts (SOTP) are applied where appropriate.

Stock ratings

Buy recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) by at least 15%.

Hold recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) between 5% and 15%.

Sell recommendations are expected to improve up to 5% or deteriorate, based on consideration of the fundamental view and the currency impact (where applicable).

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