Sharekhan by BNP PARIBAS

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Stock Update

Result Update

Bajaj Finance Ltd

Strong growth with NIMs compression in FY24

NBFC	Sharekhan code: BAJFINANCE
Reco/View: Buy ↔	CMP: Rs. 7,431
Price Target: Rs. 8,800 ↑	

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 18.79

Updated Jul 08, 2023

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

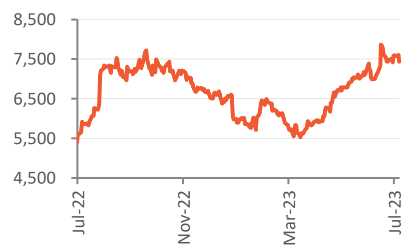
Company details

Market cap:	Rs. 4,50,261 cr
52-week high/low:	Rs. 8,000 / 5,487
NSE volume: (No of shares)	10.4 lakh
BSE code:	500034
NSE code:	BAJFINANCE
Free float: (No of shares)	26.7 cr

Shareholding (%)

Promoters	55.9
FII	20.1
DII	12.9
Others	11.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.2	22.7	28.2	18.6
Relative to Sensex	1.2	10.9	18.2	-1.2

Sharekhan Research, Bloomberg

Summary

- Bajaj Finance reported PAT of Rs. 3,437 crore up 32% y-o-y/ 9% q-o-q in line with our estimates. NII was up 27% y-o-y/ 7% q-o-q broadly in line, on the back of strong AUM growth (32% y-o-y/ 9% q-o-q) partly offset by lower NIMs down by 11 bps q-o-q to 10.4% (cal.).
- Outlook on NIMs remains negative. The company expects further 20-30 bps NIMs compression in the remaining quarters of FY24 on the back of liabilities getting repriced at higher rates assuming no repo rate hikes further.
- Asset quality was remarkable, as GS-3 ratio sequentially declined to 0.87% (vs. 0.94% q-o-q) lowest ever and GS2 ratio (incl. OTR) remained stable at 1.2% sequentially. It has improved the long-term guidance for GNPA at 1.2-1.4% vs 1.4-1.7% earlier and for NNPA at 0.4-0.5% vs 0.4-0.7% earlier.
- Loan growth outlook for FY24 has also been revised to 29-31% vs 25-27% earlier with asset mix expected to remain broadly stable. The company is now guiding for long term sustainable RoA/ RoE at ~4.6-4.8%/ ~21-23% respectively. We reiterate Buy on BAF with a revised PT of Rs. 8,800. At the CMP, the stock trades at 6.8x/5.3x FY2024E/FY2025E BV estimates.

Bajaj Finance (BAF) reported strong in line performance in Q1FY2024 despite margins compression and higher opex growth. Net interest income (NII) grew strongly by 27% y-o-y/ 7% q-o-q. NIM (calc. as a % of avg AUM) declined by 11 bps q-o-q at 10.4% as cost of funds increased by 22 bps q-o-q to ~7.6%. Outlook on NIMs remains negative. The company expects further 20-30 bps NIMs compression in the remaining quarters of FY24 on the back of liabilities getting repriced at higher rates assuming no repo rate hikes further. Customer acquisitions and the new loan booked trajectory remained strong. Fee and other income grew by 23% y-o-y/ 11% q-o-q. Total operating expenses were up 20% y-o-y/8% q-o-q. Opex growth is expected to moderate as company is near to exiting the investments cycle, which should aid operating leverage going forward. Net credit cost (calc.as a % of avg AUM) for the quarter stood at 154 bps vs 140 bps q-o-q. The company released Rs.120 crore from the contingent provisions during the quarter which was utilsed in creating additional standard asset provisioning and one-time provisions on Manipur portfolio due to deteriorating economic conditions. On full year basis, credit cost guidance now stands at 155-165 bps vs 140-150 bps earlier. The company also guided that there has been some signs of stress build up in rural B2C business, rest portfolio is behaving quite normal. PBT grew by 30% y-o-y/ 7% q-o-q. Tax rate was slightly lower due to the release of deffered tax liability provisions in BHFL made earlier related to temporary timing difference which is no longer required amounting Rs. 73 crore. AUM growth was strong at 32% y-o-y/ 9% q-o-q with asset mix broadly stable. Asset quality was remarkable, as GS-3 ratio sequentially declined to 0.87% (vs. 0.94% q-o-q) lowest ever and GS2 ratio (incl. OTR) remained stable at 1.2% sequentially. It has improved the long-term guidance for GNPA at 1.2-1.4% vs 1.4-1.7% earlier and for NNPA at 0.4-0.5% vs 0.4-0.7% earlier.PCR on GS3 assets was stable q-o-q at 65%. BAF holds contingent provisions of Rs. 840 crore (31 bps of AUM).

Key positives

- Strong growth in customer acquisitions and cross-sell franchise.
- Robust asset quality metrics.

Key negatives

- Opex growth was higher (20% y-o-y/ 8% q-o-q). Opex to Avg. AUM was at 4.4%.
- Credit cost guidance has been increased marginally for FY24 (155-165 bps of advances vs 140-150 bps earlier).

Management Commentary

- Loan growth outlook for FY24 has also been revised to 29-31% vs 25-27% earlier with asset mix expected to remain broadly stable led by strong customer acquisition and cross sell.
- It has improved the long-term guidance for GNPA at 1.2-1.4% vs 1.4-1.7% earlier and for NNPA at 0.4-0.5% vs 0.4-0.7% earlier. However, in near term company guided that there have been some signs of stress build up in rural B2C business, rest portfolio is behaving quite normal.
- BAF expects moderation in margins by another 20-30 bps in the remaining quarters of FY24. This impact would be partly offset by operating leverage and strong AUM growth. Sustainable RoA/ RoE are expected at ~4.6-4.8%/ ~21-23% respectively.

Our Call

Valuation – We reiterate a Buy on Bajaj Finance with a revised PT of Rs. 8,800: At CMP, the company trades at 6.8x/ 5.3x its FY2024E/ FY2025 BV. We believe the company is poised to deliver sector-leading growth and return ratios. Diverse product offerings through omni channel presence along with new product lines, focus on new customer addition and ability to cross-sell is likely to support AUM growth. Digital transformation, omnichannel strategy is likely to bode well for its growth objectives along with operational efficiencies going ahead which would be partly offset by lower NIMs in FY24.

Key Risks

Economic slowdown due to which slower AUM growth and higher-than-anticipated credit cost; Increased competitive intensity could lead to market share loss and moderation in AUM growth.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
NII	17,524	22,990	28,155	33,697
PAT	7,028	11,508	13,514	15,855
EPS (Rs)	115.8	189.6	222.3	263.0
RoA (%)	4.2	5.3	4.7	4.7
RoE (%)	17.4	23.5	22.4	22.0
P/E (x)	64.5	39.2	33.5	29.4
P/BV (x)	10.3	8.2	6.8	5.3

Source: Company; Sharekhan estimates

Key result highlights

- **NIMs outlook negative in near term:** Net interest income (NII) grew strongly by 27% y-o-y/ 7% q-o-q. NIM (calc. as a % of avg AUM) declined by 11 bps q-o-q at 10.4% as cost of funds increased by 22 bps q-o-q to ~7.6%. Outlook on NIMs remains negative. The company expects further 20-30 bps NIMs compression in the remaining quarters of FY24 on the back of liabilities getting repriced at higher rates assuming no repo rate hikes further.
- **Operating leverage expected to kick in:** Total operating expenses were up 20% y-o-y/8% q-o-q. The company has guided that incremental tech-led investments have peaked out. Opex growth is expected to moderate as company is near to exiting the investments cycle, which should aid operating leverage going forward.
- **Credit cost guidance revised marginally upwards for FY24:** Net credit cost (calc.as a % of avg AUM) for the quarter stood at 154 bps vs 140 bps q-o-q. The company released Rs.120 crore from the contingent provisions during the quarter which was utilsed in creating additional standard asset provisioning and one-time provisions on Manipur portfolio due to deteriorating economic conditions. On full year basis, credit cost guidance now stands at 155-165 bps vs 140-150 bps earlier. The company also guided that there has been some signs of stress build up in rural B2C business, rest portfolio is behaving quite normal. The company holds contingent provisions of Rs. 840 crore (31 bps of AUM).
- **Strong asset quality:** Asset quality was remarkable, as GS-3 ratio sequentially declined to 0.87% (vs. 0.94% q-o-q) lowest ever and GS2 ratio (incl. OTR) remained stable at 1.2% sequentially. It has improved the long-term guidance for GNPA at 1.2-1.4% vs 1.4-1.7% earlier and for NNPA at 0.4-0.5% vs 0.4-0.7% earlier. PCR on GS3 assets was stable q-o-q at 65%. It has improved the long-term guidance for GNPA at 1.2-1.4% vs 1.4-1.7% earlier and for NNPA at 0.4-0.5% vs 0.4-0.7% earlier.
- **Strong loan growth outlook:** Customer franchise expanded to 73.0 mn (up 21% y-o-y) with cross-sell franchise at 44.3 million (up 28% y-o-y) in Q1FY2024. New loans booked were 9.94 mn, up 34% y-o-y and new customer addition were at 3.84 mn up 40% y-o-y during the quarter. AUM grew by 32% y-o-y/9% q-o-q with asset mix broadly stable. Growth moderation in rural B2C segment is likely to continue due to early warning signs of potential stress build up. The company articulated that its new customer additions are expected to be 12-13 million in FY2024 which should support AUM growth. Diverse product offerings through omnichannel, new customer addition, adding distribution network, and ability to cross-sell are likely to support strong AUM growth. Loan growth is expected to be at 29-31% for FY24. Capital adequacy remained strong at 24.61% as at June 2023 with Tier-1 capital at 23.01%.
- **Deposit growth strong:** Deposits rose by 46% y-o-y and contributed to 21% of consolidated borrowings. The company is on track to deliver its long-term goal of 25% of consolidated borrowings from deposits in the medium term.

Results (Consolidated) Rs cr

Particulars	Q1FY24	Q1FY23	Q4FY23	Y-o-Y %	Q-o-Q %
Net Interest Income	6,719	5,275	6,255	27.4	7.4
Fee & Other Income	1,679	1,363	1,516	23.2	10.8
Total Income	8,398	6,638	7,771	26.5	8.1
Operating Expenses	2,854	2,380	2,652	19.9	7.6
Pre-Provisioning Profit (PPoP)	5,544	4,257	5,119	30.2	8.3
Provisions	995	755	859	31.9	15.8
PBT	4,551	3,503	4,261	29.9	6.8
Tax	1,114	907	1,103	22.9	1.0
PAT	3,437	2,596	3,158	32.4	8.8

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Large opportunity pool

NBFCs have become important constituents of India's financial sector and have been recording higher credit growth than scheduled commercial banks (SCBs) over the past few years. NBFCs continue to leverage their superior understanding of regional dynamics and customised products and services to expedite financial inclusion in India. Lower transaction costs, innovative products, quick decision making, customer orientation and prompt service standards have typically differentiated NBFCs from banks. Considering the reach and expanse of NBFCs, these are well-suited to bridge the financing gap in a large country like India. Systemically important NBFCs have demonstrated agility, innovation, and frugality to provide formal financial services to millions of Indians. The growing importance of NBFCs is reflected in the consistent rise of their credit as a proportion to GDP as well as in relation to credit extended by SCBs to the NBFC sector.

■ Company Outlook – Attractive franchise over the long term

The company has completed its business transformation, developing omnichannel presence to serve customers. BAF has significantly strengthened its technology, digital platforms, and product offering to improve customer experiences. We believe business transformation would enhance growth sustainability, improve the scalability of business, and would give competitive advantage against peers. Additionally, operating leverage is expected to kick in as the company is near to exiting the investment cycle. We are confident on strong sustainable earnings growth and longevity of the franchise.

■ **Valuation – We reiterate a Buy on Bajaj Finance with a revised PT of Rs. 8,800:** At CMP, the company trades at 6.8x/ 5.3x its FY2024E/ FY2025 BV. We believe the company is poised to deliver sector-leading growth and return ratios. Diverse product offerings through omni channel presence along with new product lines, focus on new customer addition and ability to cross-sell is likely to support AUM growth. Digital transformation, omnichannel strategy is likely to bode well for its growth objectives along with operational efficiencies going ahead which would be partly offset by lower NIMs in FY24.

Peer valuation

Particulars	CMP (Rs / Share)	MCAP (Rs Cr)	P/E(x)		P/BV(x)		RoA (%)		RoE (%)	
			FY24E	FY25E	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Bajaj Finance	7,431	4,50,261	33.5	29.4	6.8	5.3	4.7	4.7	22.4	22.0
Cholamandalam Investment and Finance Company	1,142	93,856	30.6	25.2	5.5	5.0	3.0	2.7	19.4	20.2

Source: Company, Sharekhan estimates

About company

BAF is one of India's largest and well-diversified NBFC. The company provides loans for two wheelers, consumer durables, housing, SME & MSME businesses etc. BAF undertook business and organisational restructuring in FY2008 and re-defined small business loans and consumer financing as its key niches. The company operates through 1,422 urban locations and 2,406 rural locations, with over 167,100 distribution points. BAF continues to be the largest consumer durables lenders in India. As a business entity, BAF continues to deliver steady performance and superior asset-quality performance.

Investment theme

BAF enjoys a dominant position in the retail finance space. BAF's dominance in the market is seen in its consistent growth and steady operational performance that has been maintained by the company across cycles. Superior asset quality is indicative of the company's high focus on risk management and robust credit underwriting capability and collections.

Key Risks

Economic slowdown due to which slower AUM growth and higher-than-anticipated credit cost; Increased competitive intensity could lead to market share loss and moderation in AUM growth.

Additional Data

Key management personnel

Mr. Sanjiv Bajaj	Chairman
Mr. Rajeev Jain	Managing Director
Mr. Sandeep Jain	Chief Financial Officer
Mr. Atul Jain	Chief Executive Officer (BHFL)

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	BAJAJ FINSERV LTD.	52.45
2	REPUBLIC OF SINGAPORE	3.42
3	MAHARASHTRA SCOOTERS LTD.	3.13
4	SBI FUNDS MANAGEMENT LTD.	2.91
5	AXIS ASSET MANAGEMENT CO. LTD.	2.36
6	BLACKROCK INC.	1.51
7	VANGUARD GROUP INC.	1.35
8	UTI ASSET MANAGEMENT CO. LTD.	0.98
9	CAPITAL GROUP COS INC.	0.91
10	FMR LLC	0.71

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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