Bajaj Finance

BSE SENSEX	S&P CNX
31,643	9,252

Bloomberg	BAF IN
Equity Shares (m)	577
M.Cap.(INRb)/(USDb)	1218.3 / 16.4
52-Week Range (INR)	4923 / 1916
1, 6, 12 Rel. Per (%)	-19/-30/-14
12M Avg Val (INR M)	8654

Financials & Valuations (INR b)

Y/E March	2020E	2021E	2022E
Net Income	168.2	177.2	202.1
PPP	110.8	124.4	140.3
PAT	56.3	44.6	64.8
EPS (INR)	94.1	74.5	108.2
EPS Gr. (%)	35.8	-20.8	45.2
BV/Sh. (INR)	554	619	715
Ratios			
NIM (%)	10.4	10.1	10.3
C/I ratio (%)	34.1	29.8	30.6
RoA (%)	3.9	2.6	3.5
RoE (%)	21.3	12.7	16.2
Payout (%)	10.0	10.0	10.0
Valuations			
P/E (x)	21.5	27.2	18.7
P/BV (x)	3.7	3.3	2.8
Div. Yield (%)	0.5	0.4	0.6

Shareholding pattern (%)

As Of	Mar-20	Dec-19	Mar-19
Promoter	56.2	56.2	55.2
DII	10.9	10.5	8.5
FII	21.5	22.5	20.9
Others	11.5	10.9	15.5

FII Includes depository receipts

Please note all the calculation/assumptions in the note are based on our judgement on each product class related to a) Repayment rate b) Moratorium expected c) worst case expected LGDs under stress scenario – BAF does not disclose specifics regarding the same. Hence actuals may vary significantly to estimates/Assumptions

CMP: INR2,025 TP: INR 2,300 (+14%) Neutral

Macros to weigh on valuations; Long term outlook positive

Scenario analysis suggest credit cost of 5.3-8%

- **Over the past decade, Bajaj Finance (BAF) has had nothing but a dream run; the company delivered AUM/PAT/MCAP CAGR of 44%/55%/48% and GNPL ratio has declined from 8% to 1.6%. However, given the current environment, FY21 would be a year of consolidation. BAF would face real big challenges on (a) risk management, (b) trimming flab created in the upcycle, and (c) fine-tuning the business model.**
- **BAF is well placed amongst all large NBFCs to counter the near-term challenges of liquidity (sitting on 11-12% of AUM), ALM dislocation caused by moratorium and capitalization (CAR of ~27%, leverage of just ~4x). Even in case of ~50% AUM being under moratorium, the company would comfortably meet all its debt obligations for the next three months and still have liquidity of ~INR90b remaining on its balance sheet (refer Exhibit 3).**
- **We conducted a sensitivity analysis on credit costs in FY21 by factoring in different slippage rates based on expected moratorium across product segments, 20% relapse rate and 35% recovery/upgrades from relapse. According to our conservative calculations, in the base case/case 1, net slippages may spike to ~6.7% in FY21 (v/s run-rate of sub-2%), credit costs would jump to ~5.3%. While the situation is still evolving, we derive comfort from the company having 65% of its customers with 750+ CIBIL score.**
- **Considering the changed lockdown guidelines and extension of period, we have further increased credit cost by 25bp/10bp each to 4.3%/3.3% for FY21/22E and have built in gradual growth recovery (~12% in FY22E v/s ~20% earlier). We have cut earnings estimates by 6-7% for FY21/22E.**
- **While we remain convinced of the strength of BAF's business model to deliver better than sector returns over the medium-to-long term and get comfortable on multiples, an immediate significant re-rating is unlikely due to (a) near-term macro volatility caused by COVID-19, and (b) lack of any specific catalyst. We cut our TP to INR2,300 (3.2x FY22 BVPS) to factor in EPS cuts and moderation in growth. Maintain Neutral.**
- **Key Risks: (a) Extension of the lockdown and moratorium period, (b) Higher share of riskier/unsecured products in portfolio, (c) Competitive pressures from banks on housing loans, (d) Continued funding challenges for NBFCs, although we believe BAF would be less impacted.**

Well placed to counter near-term challenges

Apart from managing asset quality, key challenges for any lending institution in the near term would be (a) managing liquidity and ALM, and (b) maintaining adequate capital for comfort of the rating agencies as well as depositors. BAF scores well on all fronts with (a) **strong liquidity on the balance sheet** of INR160b (11-12% of AUM), and (b) **healthy ALM** situation – ~40% of its loans are of less than one year duration. Our 'adjusted' ALM analysis reveals that even if ~50% customers avail the moratorium, BAF would be able to meet its debt obligations (but not disburse any fresh loans) and sit on excess liquidity of ~INR90b (this does not factor in any new borrowings), (c) **capitalization –** BAF has the least leverage (~4x) among large NBFCs – it has recently raised INR85b (~40% of net worth), which stands it in good stead v/s other NBFCs.

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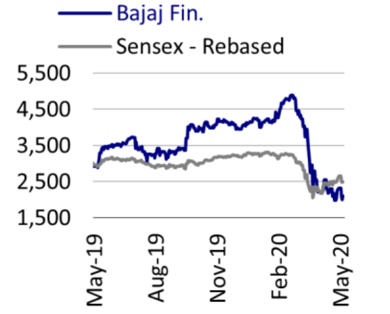
Stock Performance (1-year)



Building in adequate buffer for credit cost and growth

We conducted product-wise scenario analysis of credit costs depending on the net slippage ratio. We assume three scenarios with weighted average net slippages ratio ranging from 6.7% to 10% (run-rate is sub-2%) based on expected moratorium of each product class, 20% relapse rate and 35% recovery/upgrade from relapse. We also assume write-offs (benchmarking reported PCR to each product) based on each product class and keep PCR levels constant (for rest of the portfolio), which leads us to 5.3-8% credit cost under various scenarios. In our view, part of this is likely to be up-fronted in 4QFY20 earnings and a part would be deferred to FY22E. We have increased our credit cost by 25bp/10bp for FY21/22E to 4.3%/3.3% to factor in the revised lockdown scenario and have modelled in gradual growth recovery in FY22E (12.5% v/s 20% earlier). We must state that the situation remains extremely volatile and this is our best case judgement based on product /customer profile.

Liability diversification to gain traction

Post the IL&FS crisis, the company aggressively moved to ECB and deposit mobilization (share now at 20% v/s 14% pre-Sep'18) to diversify the liability side. Risk aversion by banks and volatile bond markets would continue to weigh on the funding cost of NBFCs in the near-to-medium term, but BAF is better placed than peers due to strong parentage, healthy capitalization and a proven business model. BAF has demonstrated strong execution on the deposit front too – starting from scratch in FY14, it has scaled up the deposit base to INR207b as of 9MFY20 with over 200k depositors. Performance on this front would be the key monitorable in the ensuing quarters. Note that public deposit rates are competitive with those of other NBFCs (Exhibit 16).

Long-term drivers in place; Macro uncertainty to weigh on valuations

We believe BAF's long-term thesis remains intact; the company has (a) strong customer acquisition helped by large distribution network, (b) an ability to create a profitable business model in an already crowded market, (c) created a niche in few product/customer segments, (d) a disciplined liability and ALM approach, (e) an ability to monetize customer base and improve asset-light income streams, and (f) high flexibility on opex. While multiples are getting comfortable, any significant re-rating is unlikely due to near/medium-term challenges caused by COVID-19 and lack of specific catalysts. Maintain **Neutral** with TP of INR2,300 (3.2x FY22E BVPS).

Well placed to face near-term challenges

Adequate liquidity| Healthy ALM | Best capitalization amongst large NBFCs

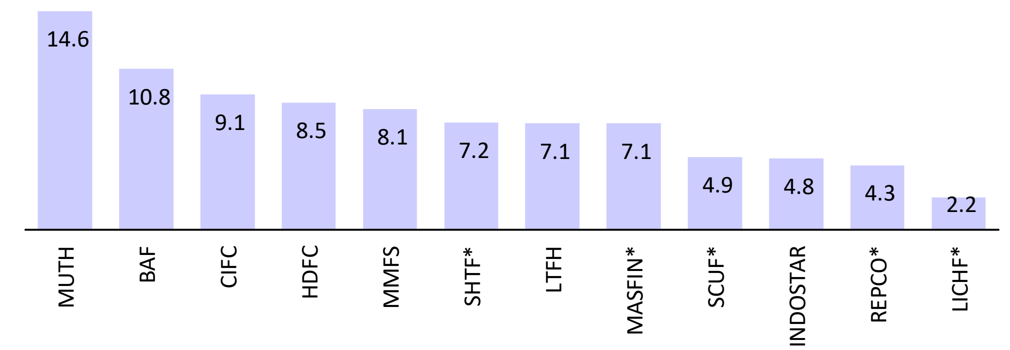
- **BAF has strong liquidity on the balance sheet of INR160b (11-12% of AUM).**
- **The company also has healthy ALM – ~40% of loans are of less than one year duration. Our 'adjusted' ALM analysis reveals that even in case ~50% customers avail the moratorium, BAF would be able to meet its debt obligations (but not disburse any fresh loans) and sit on excess liquidity of ~INR90b (this does not factor in any new borrowings).**
- **Best capitalization – BAF has the least leverage (~4x) amongst large NBFCs. Recently, the company has raised INR85b (40% of then outstanding net worth), which stands it in good stead v/s other NBFCs.**

Cash and Cash Equivalent at 11-12% of outstanding AUM

- BAF, in a recent conference call, revealed that it has cash and cash equivalent of INR160b as of Mar'20. This works out to ~11-12% of AUM and ~13% of the outstanding borrowings.
- Outstanding liquidity on the balance sheet is among the best in the sector and in our coverage universe.

Amongst large NBFCs, BAF has the highest outstanding cash on balance sheet v/s peers

Exhibit 1: Outstanding liquidity on the balance sheet (% of AUM)



Source: Company, MOFSL,*1HFY20, Note: BAF data as of FY20

Looking at adjusted ALM, factoring in moratorium across products

Expect ~50% loan moratorium on weighted-average basis. These are conservative assumptions in our view

- For our 'adjusted' ALM analysis, we assume varied rates of loan moratorium availed by customers depending on the product. **According to our assumptions, share of customers availing moratorium would vary from nil in case of Loan Against Shares (LAS) to 75% in case of the auto financing division.**
- At the same time, loan repayment rates (annualized) vary from 20% in case of mortgages to 100% in case of LAS and CD financing.
- Given the above assumptions, we arrive at loan repayments of ~INR85b for the quarter.

Exhibit 2: Expect ~INR85b loan repayments in 1QFY21 after adjusting for loan moratorium

	AUM (INR B)	Moratorium (%)	Repayment rate (%)	1QFY21 Repay. – Actual (INR B)	Adjusted inflow (INR B)
Auto Finance	134	75	60	20	5
Sales Finance	142	50	100	36	18
Consumer Finance (B2C)	299	60	50	37	15
Rural B2B Sales Finance	28	50	100	7	3
Rural B2C Business	101	50	50	13	6
SME Business	190	70	35	17	5
LAS	66	0	100	17	17
Commercial (Ex LAS)	66	40	25	4	2
Mortgages	450	40	20	22	13
Total	**1,476**	**51**	**47**	**172**	**85**

Note: We have assumed similar AUM mix for 4QFY20 as that of 3QFY20; Source: MOFSL, Company

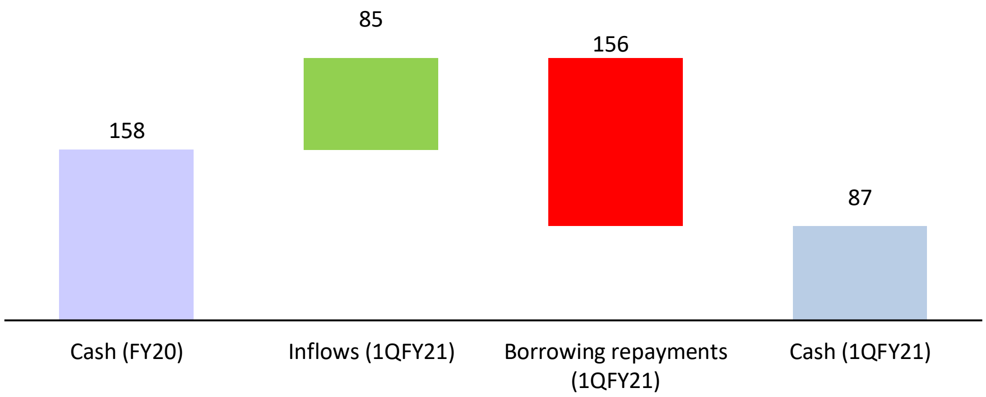
INR160b liquidity on the balance sheet adequate to meet debt obligations over the next quarter

Liquidity cushion of INR160b provides comfort

- As of 9MFY20, BAF had ~INR450b of borrowings maturing in a year. We conservatively assume that 35% of these borrowings (i.e. ~INR150b) are likely to mature in a quarter.
- With INR160b liquidity on the balance sheet, it would be able to meet its debt obligations and yet have ~INR90b of cash on the balance sheet.
- Our analysis does not factor in new inflows from banks/debt markets. Recently, BAF raised INR2b from the debt markets at 7.06% for a 3-year tenure. Total issue size was INR25b (INR100m base issue and rest green-shoe option). In our view, the company was trying to test the market's appetite for its paper at the set rate.
- Last fortnight, HDFC raised 3-year paper at ~7.4% with an issue size of INR50b (INR12.5b base issue and INR37.5b green-shoe). Our market interactions suggest that HDFC managed to garner only the base issue.

Exhibit 3: Adequate cash to meet debt obligations and disburse loans (INR b)

Despite taking care of all liability obligations in 1Q, BAF would sit with excess liquidity of INR87b



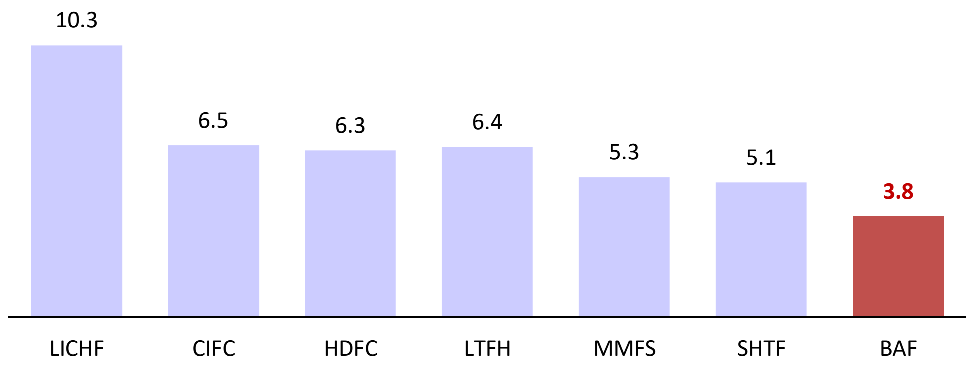
Source: MOFSL, Company

Best capitalization amongst large NBFCs

- BAF recently raised INR85b (40% of the then outstanding net worth), taking its overall CAR to ~27% with strong Tier I ratio of ~23%. Debt to equity of the company is at a low of ~4x, which should provide comfort to rating agencies and lenders.
- Since 2008, the company has never breached debt to equity of 6x. Also, ability of the management to raise capital as and when the need arises with improving profitability is a comforting factor.
- Amongst our coverage universe, BAF has the least leverage with strong parentage and a proven business model. As and when risk appetite for NBFCs improve, BAF would be the first to benefit in our view.

BAF's debt/equity levels are just ~4x – significantly lower than other NBFCs

Exhibit 4: Least levered among large NBFCs in our coverage (Debt/Equity, x)



Source: MOFSL, Company

Building in buffer for credit cost and slower growth

Sensitivity analysis factoring in worst case credit cost of ~8%

- **We conducted product-wise scenario analysis of credit costs depending on the net slippage ratio. We assume three scenarios with weighted average net slippages ratio ranging from 6.7% to 10% (run-rate is sub -2%) based on expected moratorium of each product class, 20% relapse rate and 35% recovery/upgrade from relapse.**
- **We also assume write-offs based on each product class and keep PCR levels constant, which leads us to 5.3-8% credit cost under various scenarios. In our view, part of this is likely to be up-fronted in 4QFY20 earnings and a part would be deferred to FY22.**
- **We increase our credit cost by 25bp/10bp each for FY21/22E to factor in the revised lockdown scenario. We also model in gradual growth recovery for FY22E (12.5% v/s 20% earlier). Accordingly we cut earnings by 6-7% for FY21/22E. As we are conservative, we believe a positive surprise is likely.**

Expect 8%/13% YoY growth in FY21/FY22E

Factoring in gradual recovery in loan growth

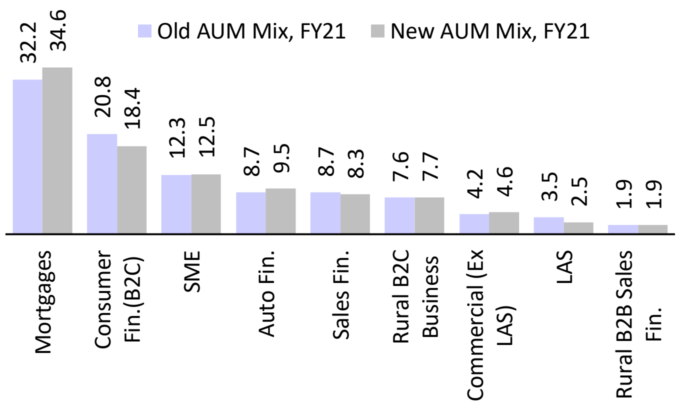
- We have attempted bottom-up growth estimates for BAF depending on the product's tenure and assumption on moratorium granted across product segments.
- We have also juxtaposed revised estimates as against the pre COVID-19 period.
- Under our revised estimates, overall disbursements (back of the envelope calculations) in absolute terms are likely to be 35%/30% lower for FY21/22E v/s earlier estimates. While we factor in 18-20% decline in disbursement for FY21, post this, disbursement should grow 25-30% in FY22E.
- Note that few products like Auto and sales finance in both urban/rural segments are of very short duration and could see sudden rebound with the change in sentiments. Other focused and longer duration segments like mortgages have seen sizable reduction in competitive intensity amongst NBFCs/HFCs. In the revised scenario with stability returning, BAF could accelerate efforts in such products.
- On the other hand, BAF would take longer to get its risk appetite back in SME lending.

Exhibit 5: Bake in moderate recovery in FY22E as well; short duration products could surprise positively

	AUM (INR b)				Earlier Est. (INR b)		AUM Abs. Chg (%)	
Product	**FY19**	**FY20**	**FY21**	**FY22**	**FY21**	**FY22**	**FY21**	**FY22**
Auto Finance	97	134	151	163	163	189	-8	-14
Sales Finance	123	142	132	149	163	192	-19	-22
Consumer Finance (B2C)	230	299	291	301	389	489	-25	-38
Rural B2B Sales Finance	21	28	30	38	36	44	-15	-15
Rural B2C Business	71	101	121	151	143	190	-15	-20
SME Business	158	190	199	199	229	272	-13	-27
LAS	64	66	40	40	66	66	-40	-40
Commercial (Ex LAS)	57	66	73	80	78	92	-7	-13
Mortgages	339	450	550	666	601	785	-9	-15
Total	**1,159**	**1,476**	**1,587**	**1,786**	**1,868**	**2,318**	**-15**	**-23**
Growth %		27.4	7.5	12.5	26.5	24.1		

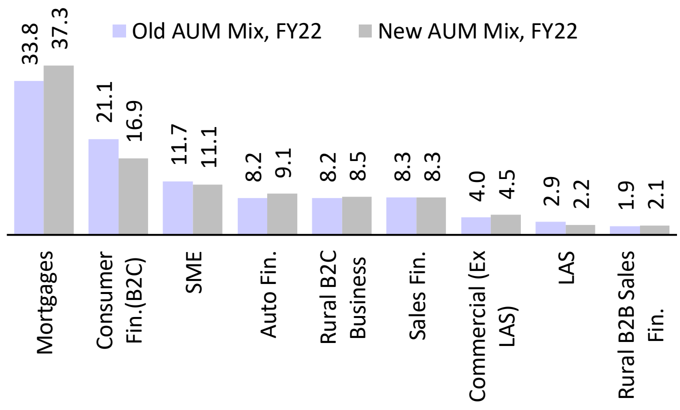
For FY20 we have assumed same AUM mix as of 9MFY20; Please note these our back of the envelope calculations – BAF does not disclose disbursement/repayment data; Source: MOFSL

Exhibit 6: Changes in product mix for FY21, %



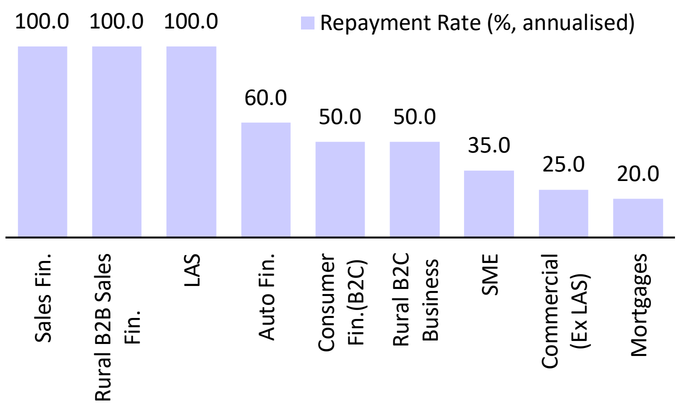
Source: MOFSL. % of AUM. *Fin-Finance

Exhibit 7: Changes in product mix for FY22, %



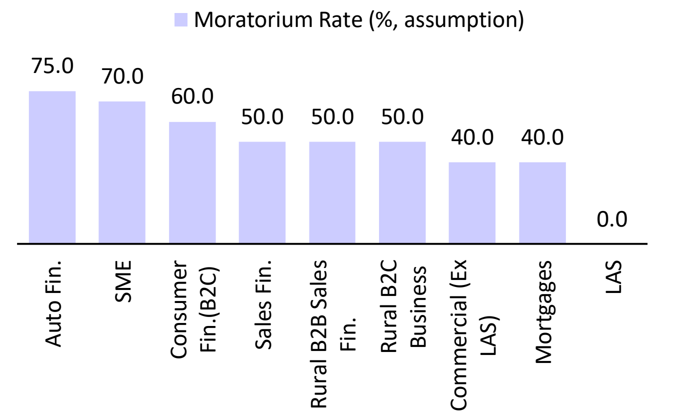
Source: MOFSL. % OF AUM, *Fin-Finance

Exhibit 8: Key assumptions for Repayment rate across product class (Annualised, %)



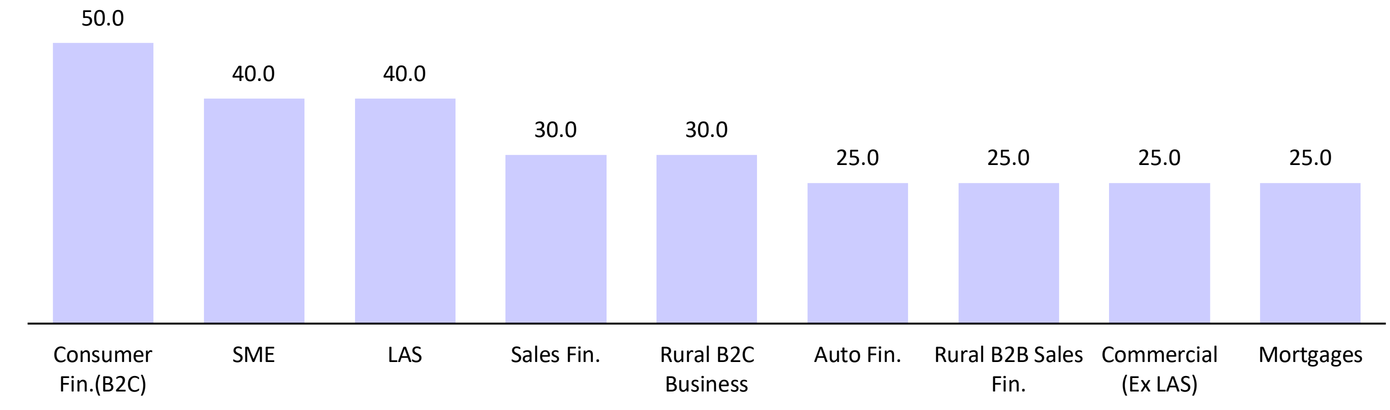
Source: MOFSL, Assumption

Exhibit 9: Key assumptions for Moratorium Rate under RBI scheme



Source: MOFSL, Assumptions

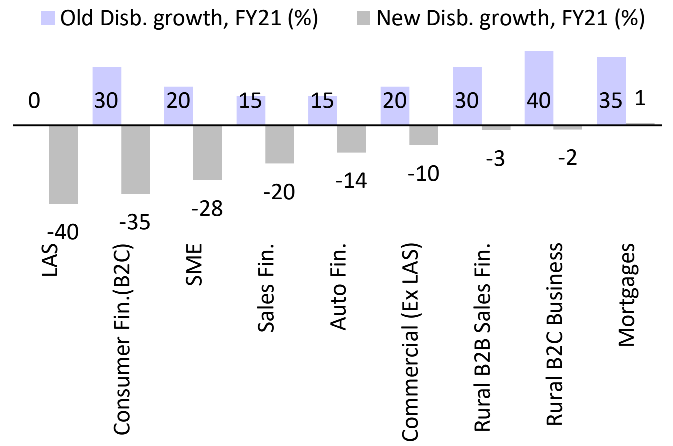
Exhibit 10: Assumption for loss of business in annual disbursement v/s Pre COVID-19 (% FY21 disbursement)



Source: MOFSL

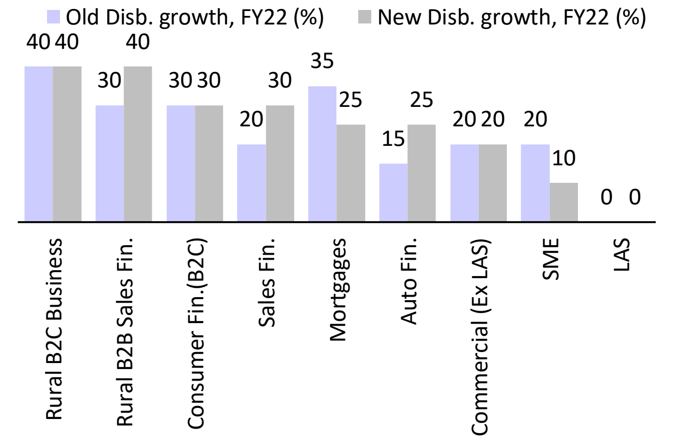
Revised disbursement growth likely to be significantly lower than earlier back of envelope calculation

Exhibit 11: Revised disbursement growth (FY21, %)



Source: MOFSL

Exhibit 12: Revised disbursement growth (FY22, %)



Source: MOFSL

Please note all the above calculation/assumptions are back of the envelope calculations based on our understanding of product repayment cycle – **BAF does not disclose disbursement/repayment data; hence, actuals may vary significantly than estimated/calculated above.**

Expect 7.5% cumulative credit costs over the next two years

7.5% cumulative credit costs over next two years in worst case

- We conducted product-wise analysis of credit costs across three scenarios. In the **base case (Case 1),** for the moratorium cases, we have assumed 20% relapse rate for NPAs. Of this, 35% is our estimate of recovery while the rest is estimated to slip into NPL. **Overall, in Case 1, net slippage ratio is likely to be 6.7%.**
- In **Case 2/3**, we have increased net slippage in individual asset class by 30%/50% v/s Case 1.
- In FY18/19, net slippage ratio (excluding write-offs) for the company stood at ~2% and for FY20, it is likely to be ~2.4% due to few lumpy corporate slippages.
- Further, we have kept PCR level constant v/s that reported in 3QFY20 and have assumed the Write offs (based on PCR reported for each product) depending on the product segment.

Exhibit 13: We have assumed 20% of the moratorium cases to slip into NPA, of this, 35% should be recovered/upgraded

	AUM Mix	Moratorium	Write offs	PCR	Net Slippages (% of Resp. product)		
	(9MFY20)	(%)	(%)	(9MFY20)	Case 1	Case 2	Case 3
Auto Finance	9.1	75.0	55.0	55.5	10.0	13.0	15.0
Sales Finance	9.6	50.0	80.0	80.8	6.5	8.5	9.8
Consumer Finance (B2C)	20.2	60.0	70.0	72.0	8.0	10.4	12.0
Rural B2B Sales Finance	1.9	50.0	80.0	82.4	6.5	8.5	9.8
Rural B2C Business	6.9	50.0	65.0	67.2	7.0	9.1	10.5
SME Business	12.9	70.0	75.0	74.9	9.0	11.7	13.5
LAS	4.5	0.0	0.0	0.0	0.0	0.0	0.0
Commercial (Ex LAS)	4.5	40.0	60.0	59.0	5.0	6.5	7.5
Mortgages	30.5	40.0	25.0	26.8	5.0	6.5	7.5
Total				**56.8**	**6.7**	**8.7**	**10.0**

Source: MOFSL

Exhibit 14: In our Base case, we have factored in 4%/3.25% credit cost for FY21/22, which in our view adequately covers risk

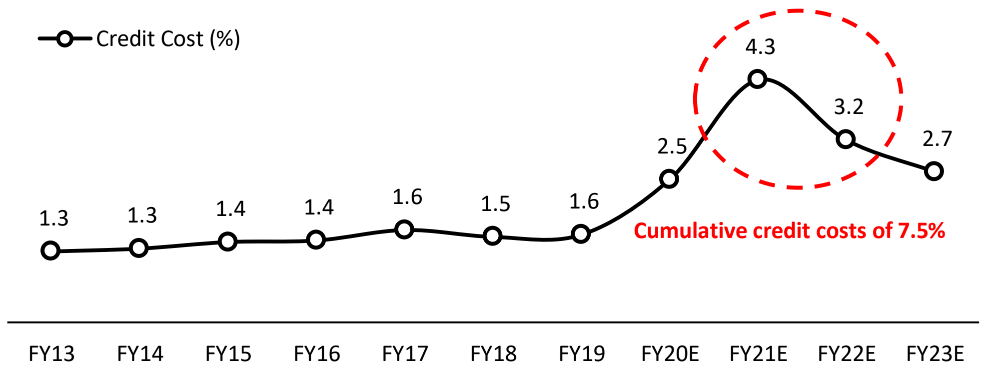
	Write offs (Net slippage*LGDs)			NPA Prov. ((Net slippage-Write offs)*PCR)			Provisions (Write offs+NPA)		
	Case 1	Case 2	Case 3	Case 1	Case 2	Case 3	Case 1	Case 2	Case 3
Auto Finance	5.5	7.2	8.3	2.5	3.2	3.7	8.0	10.4	12.0
Sales Finance	5.2	6.8	7.8	1.1	1.4	1.6	6.3	8.1	9.4
Consumer Finance (B2C)	5.6	7.3	8.4	1.7	2.2	2.6	7.3	9.5	11.0
Rural B2B Sales Finance	5.2	6.8	7.8	1.1	1.4	1.6	6.3	8.2	9.4
Rural B2C Business	4.6	5.9	6.8	1.6	2.1	2.5	6.2	8.1	9.3
SME Business	6.8	8.8	10.1	1.7	2.2	2.5	8.4	11.0	12.7
LAS	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial (Ex LAS)	3.0	3.9	4.5	1.2	1.5	1.8	4.2	5.4	6.3
Mortgages	1.3	1.6	1.9	1.0	1.3	1.5	2.3	2.9	3.4
Total	**3.9**	**5.1**	**5.9**	**1.4**	**1.8**	**2.1**	**5.3**	**6.9**	**8.0**
As %age of Net Slippages		**59.0**			**50.7^**			**79.8**	

Note: All the above numbers are % of respective loan class; ^on the net slippages ex write offs; Source: MOFSL

Please note all the above calculation/assumptions are based on our judgement on moratorium or expected write offs for each product class under stress scenario – BAF has not given disclosure regarding the same

- In **Case 3**, BAF is likely to incur credit cost of ~8%. The entire charge is unlikely to be incurred in FY21; even if we assume charge of 60%/40% in FY21/FY22E, then the provisioning requirement is likely to stand at 4.8%/3.2%.
- These are the calculations based on the outstanding portfolio as of FY20. Incremental credit is also likely to be of better quality due to mix shift and tightening risk standard considering the macro environment. Hence, we do not expect higher credit cost v/s FY17-19 level of ~1.6% on such loans.
- **As of now we have factored in credit cost of 4.3%/3.2% for FY21/FY22E.** In a recent conference call, management had mentioned that in the worst case scenario, credit cost for FY21 would likely be 80-90% higher of FY20 credit cost.

Exhibit 15: Conservatively modelling credit costs over the next two years



Source: MOFSL, Company

Liability diversification to gain traction

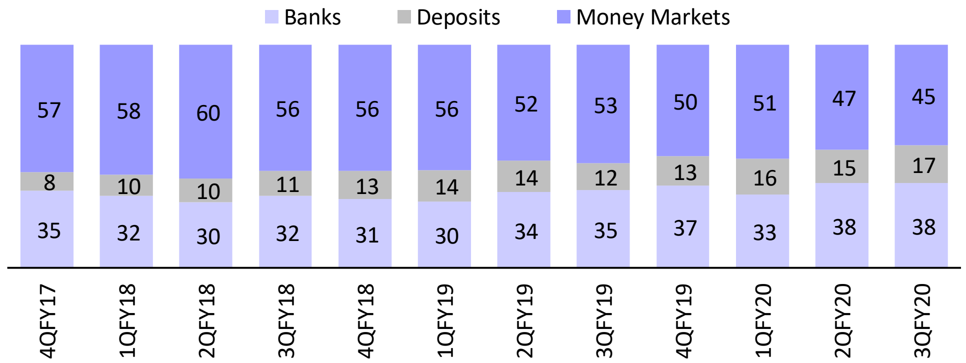
Best performance on deposit mobilization so far

- **Post the IL&FS crisis, BAF has aggressively moved to ECB and deposit mobilization (share now at 20% v/s 14% pre Sep'18) to diversify its liability side.**
- **In the near term, funding cost is likely to be elevated for NBFCs due to risk aversion from banks and issues in the bond market. However, BAF would be relatively better off than peers due to strong parentage, healthy capitalization and a proven business model.**
- **BAF has demonstrated strong execution on the deposit front, starting from scratch in FY14, it scaled up the deposit base to INR207b as of 9MFY20 with over 200k depositors. Performance on the deposits front is a key monitorable in the near term.**

Sharp improvement in liability mix

- One clear trend that has been witnessed is the reduction in dependence on market borrowings, even prior to the IL&FS crisis. Such a strategy should help the company in times of turmoil in the debt capital markets.
- However, note that with its AAA-rating and strong parentage, the company could increase the share of market borrowings if the rates are favorable.

Exhibit 16: Strong growth in volume and value of deposits



Source: MOFSL, Company

86% YoY growth in deposit base

Strong deposit traction

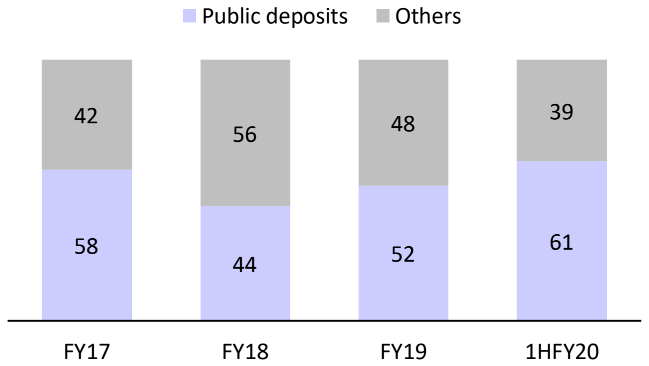
- In FY19, BAF overtook MMFS in terms of number of depositors (190k v/s 186k). It ranks second to HDFC (2m+ depositors).
- The mix has been moving toward higher share of public deposits.

Exhibit 17: Strong growth in volume and value of deposits

	FY17	FY18	FY19	9MFY20
Number of depositors ('000)	**71**	**101**	**190**	
Growth (%)		43	88	
Total deposits (INR b)	**43**	**78**	**132**	**207**
Growth (%)		82	69	86

Source: MOFSL, Company

Exhibit 18: Increasing share of public deposits (%)



Source: MOFSL, Company; Note: 1HFY20 number based on management interaction

Exhibit 19: Interest rate on public deposits offered (%)

Company	1-2 years	2-3 years	3-4 years
HDFC	7.10	7.10	7.10
PNBHF	7.50	7.65	7.65
BAF	**7.60**	**7.65**	**7.70**
SHTF	7.6-7.9	8.1-8.8	9.0-9.5
MMFS	7.4-7.6	8.0-8.25	8.55

Source: MOFSL, Company

Long-term growth story unchanged

Volume-driven growth| Focus on fee income |Superior return ratios

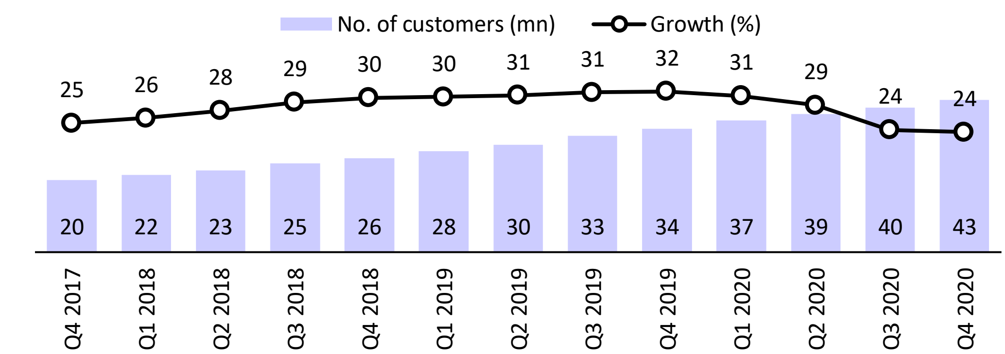
- **We believe long-term thesis for BAF remains intact. The company has (a) strong customer acquisition helped by its large distribution network, (b) an ability to create profitable business model in an already crowded market, (c) created a niche in few product/customer segments, (d) disciplined liability and ALM approach, (e) an ability to monetize the customer base and improve asset-light income stream, and (f) high flexibility on opex.**
- **While multiples are getting comfortable, any immediate significant re-rating is unlikely due to near/medium-term challenges caused by COVID-19 and lack of specific catalysts. Maintain Neutral with TP of INR2,300 (3.2x FY22E BVPS) changed from INR2,625 earlier (3.6x PBV) to factor in lower growth and cut in EPS.**

Consistent 25-30% customer base CAGR over the past several quarters

Customer base growing at ~25% YoY; FY21 to be a year of consolidation

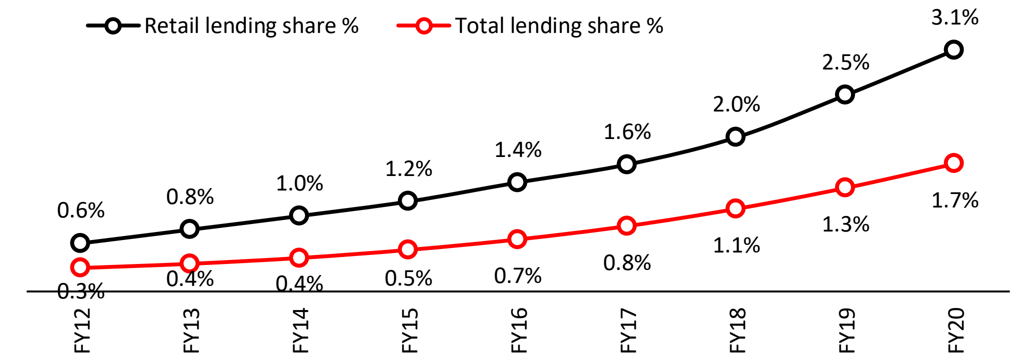
- Overall customer base growth has been steady at ~25% YoY although incremental addition slowed down in 1HFY20.
- Despite strong loan growth over the past 5 years, BAF's retail market share has increased from 1.2% to only 3.1%. Note that we have excluded mid/large corporate lending, agri finance and NBFC lending to calculate retail lending market share.

Exhibit 20: Customer base has crossed 40m



Source: MOFSL, Company

Exhibit 21: BAF's market share in retail and SME lending in the system stands at ~3%



Source: MOFSL, Company; Note: Assuming stable retail:commercial mix in FY20

Two of three new loans are to existing customers

Significant improvement in cross sell

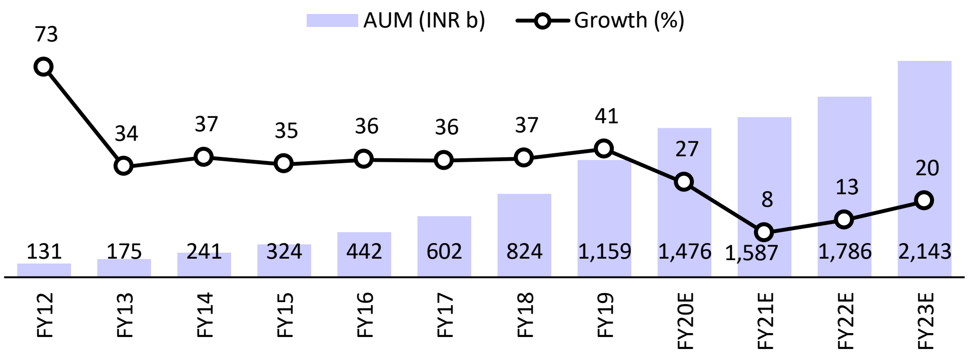
- Existing customers comprise over two-thirds of all new loans booked incrementally compared to three-fifths two years ago.
- This is beneficial to BAF due to lower opex and credit costs for existing customers.

Exhibit 22: Increasing share of new loans disbursed to existing customers

New loans booked ('000)	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020
Existing customers	2,722	2,369	3,559	3,490	4,255	3,913	4,814	4,549	5,209
New customers	1,814	1,411	2,071	1,770	2,515	1,917	2,456	1,921	2,461
Total	**4,536**	**3,780**	**5,630**	**5,260**	**6,770**	**5,830**	**7,270**	**6,470**	**7,670**
% from existing customers	60%	63%	63%	66%	63%	67%	66%	70%	68%

Source: MOFSL, Company

Exhibit 23: AUM growth to decline to 8% in FY21 and to pick up gradually in FY22E



Source: MOFSL, Company

Fee income at 1.7-1.9% of AUM is higher than that for most peers, including banks

Fee income traction robust but head-winds expected in FY21

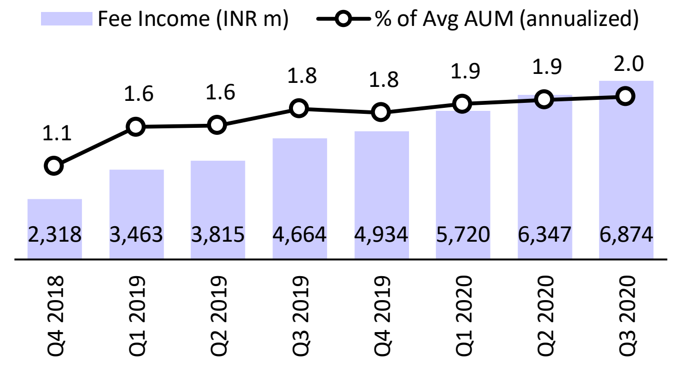
- Fee income growth has been strong and was largely driven by distribution fees (in our view, a large contributor to this is the tie-up with RBL Bank). **While that has been strong so far, we expect 25% decline in FY21 from lower referral fees, reduced card spends and less new card issuances.**
- However, some of this could be offset from increased overdue charges/late payment penalties in this environment. In addition, higher liquidity on the balance sheet (INR160b currently v/s FY20 average of INR100-120b) would result in higher interest income on liquid investment.
- **Note that at 1.7-1.9% of AUM, fee income for BAF is higher than that for most peers (including banks) and has been one of the key drivers of profitability improvement so far.**

Exhibit 24: Sharp growth in distribution fees

INR m	FY18	FY19
Service & admin charges	3,434	5,806
Fee on value added products	1,972	3,285
Foreclosure income	247	1,052
Distribution income	**2,428**	**6,676**
Total	**8,082**	**16,819**

Source: MOFSL, Company

Exhibit 25: Fee income trend



Source: MOFSL, Company

Exhibit 26: Fee income traction v/s peers

	Fee Income to Avg. Assets (%)
BAF	**1.7-1.9**
HDFCB	1.2-1.3
AXSB	1.3-1.4
IIB	2.0-2.1
LTFH	0.9-1.0

Source: MOFSL, Company

Expense ratio of 1.4% for the HFC is elevated as compared to peers

HFC on the right track; Risk aversion in other segments – share to increase

- BAF's HFC segment has witnessed steady improvement in profitability (RoA at 1.9% in 3QFY20 v/s 1.2% YoY); however, expense ratio remains higher than peers (25-75bp).
- BAF's share of mortgage is likely increase in AUM due to (a) slower growth in unsecured lending due to lower risk appetite, and (b) slower growth in underlying products for Auto/sales finance segments.

Exhibit 27: DuPont analysis of the HFC subsidiary

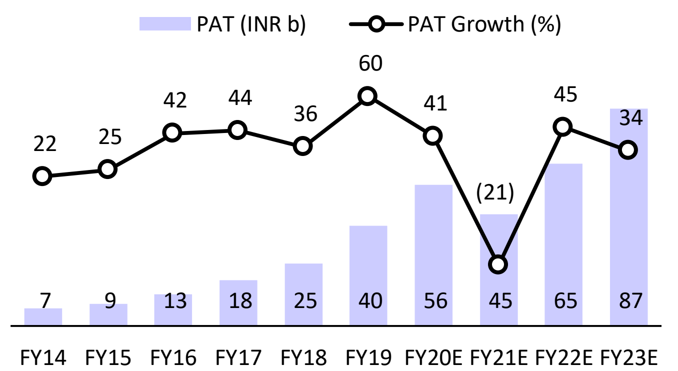
%	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020
Interest & fee income	10.9	11.0	10.9	10.5	10.7	10.4
Interest expense	6.3	6.7	6.8	6.4	6.3	6.3
NII	**4.6**	**4.3**	**4.1**	**4.0**	**4.5**	**4.1**
Opex	3.8	2.5	1.7	1.7	1.5	1.4
PPoP	**0.8**	**1.8**	**2.4**	**2.4**	**3.0**	**2.7**
Provisions	0.2	0.2	0.2	0.2	0.2	0.2
PBT	**0.5**	**1.6**	**2.2**	**2.2**	**2.7**	**2.5**
Tax	0.1	0.5	0.6	0.8	0.6	0.6
PAT	**0.4**	**1.2**	**1.6**	**1.4**	**2.2**	**1.9**

Source: MOFSL, Company

Superior RoA/RoE delivered across cycles

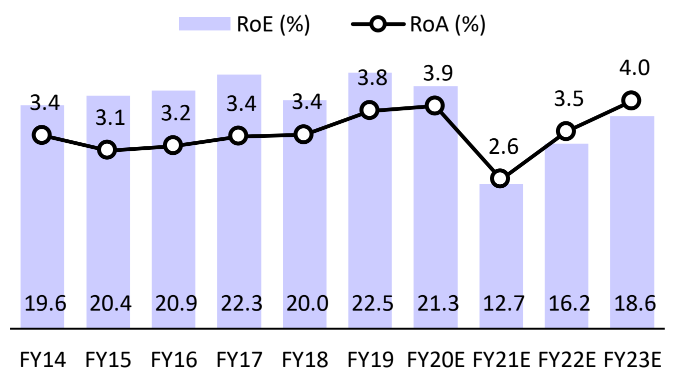
- Despite elevated credit costs, we believe BAF would deliver ~16% RoE in FY22E. We expect it to revert to run-rate levels of 18-20% in FY23E.

Exhibit 28: Expect sharp drop in PAT in FY21 led by higher credit cost



Source: MOFSL, Company

Exhibit 29: Expect RoA/RoE to decline to ~2.6%/13% in FY21 and pick up thereafter



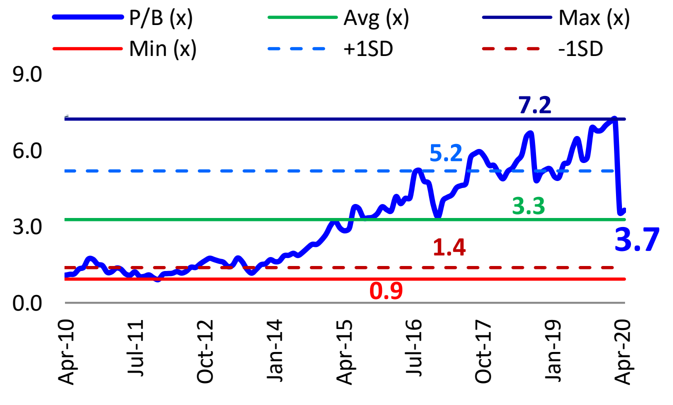
Source: MOFSL, Company

Exhibit 30: DuPont analysis (%) – Higher share of variable expenses; Opex can surprise positively

Y/E MARCH	2013	2014	2015	2016	2017	2018	2019	2020E	2021E	2022E	2023E
Interest Income	18.5	17.1	17.0	16.4	16.0	15.8	15.6	15.8	15.1	15.1	15.2
Interest Expended	7.8	7.4	7.8	7.3	7.0	6.3	6.3	6.4	6.2	6.0	6.0
Net Interest Income	**10.7**	**9.7**	**9.2**	**9.1**	**9.0**	**9.5**	**9.3**	**9.3**	**8.9**	**9.1**	**9.2**
Other Operating Income	1.6	1.9	1.7	1.9	2.3	1.6	2.0	2.3	1.4	1.7	1.9
Net Income	**12.4**	**11.8**	**11.0**	**11.0**	**11.4**	**11.1**	**11.4**	**11.7**	**10.4**	**10.8**	**11.1**
Operating Expenses	5.5	5.4	5.0	4.8	4.7	4.5	4.0	4.0	3.1	3.3	3.3
Operating Income	**6.9**	**6.4**	**6.1**	**6.3**	**6.7**	**6.6**	**7.3**	**7.7**	**7.3**	**7.5**	**7.7**
Provisions/write offs	1.2	1.2	1.3	1.4	1.5	1.4	1.4	2.3	3.8	2.8	2.4
PBT	**5.7**	**5.1**	**4.7**	**4.9**	**5.2**	**5.2**	**5.9**	**5.4**	**3.5**	**4.6**	**5.4**
Tax	1.8	1.8	1.6	1.7	1.8	1.8	2.1	1.5	0.9	1.2	1.4
Reported PAT	**3.8**	**3.4**	**3.1**	**3.2**	**3.4**	**3.4**	**3.8**	**3.9**	**2.6**	**3.5**	**4.0**
Leverage	5.7	5.8	6.5	6.5	6.6	5.9	5.9	5.5	4.8	4.7	4.7
RoE	**22.0**	**19.6**	**20.4**	**20.9**	**22.3**	**20.0**	**22.5**	**21.3**	**12.7**	**16.2**	**18.6**

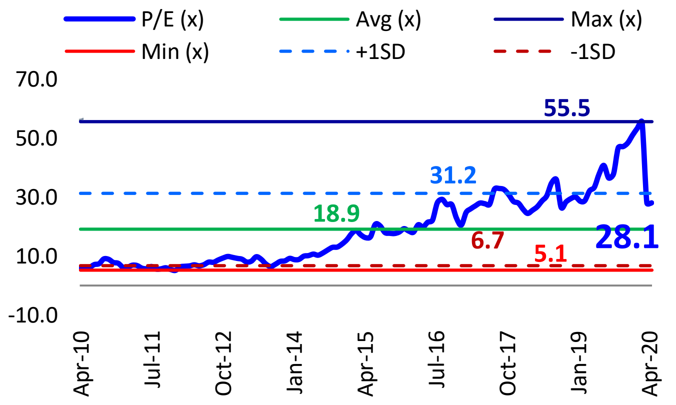
Source: MOFSL, Company

Exhibit 31: P/B chart (1-year forward)



Source: MOFSL, Company

Exhibit 32: P/E chart (1-year forward)



Source: MOFSL, Company

Key Risks

Lockdown extension – a key threat to portfolio

Extension of the lockdown or more zones getting converted to 'Red' from 'Orange' and 'Green' could have serious implications for growth and collections, especially in the self-employed and MSME segments. SME (13% of AUM) and non-salaried PL (~10% of AUM) contribute ~22% of the AUM. Our base assumes 8-9% slippage ratio in each product; anything higher than that would pose downside risk to estimates and affect investor sentiment for the stock.

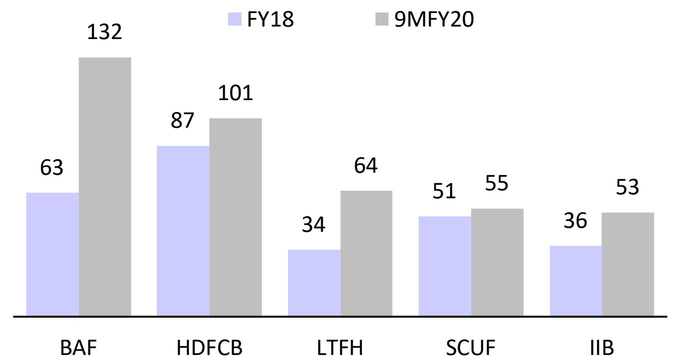
COVID-19 first crisis to test resilience of asset side on balance sheet

While India has faced multiple challenges (the global financial crisis (GFC), Taper Tantrum, Demonetization, GST and IL&FS crisis), BAF's asset side was less impacted (except during the GFC as it was early days for BAF) across crises. The company performed exceptionally well on mobilising liquidity, managing ALM and getting capital in place. However, the COVID-19 crisis is likely to pose a bigger challenge on the asset side due to loss of income/fear of job losses. BAF has aggressively grown its portfolio in the last three years (although a large part of it is short duration), but asset-side risk management is likely to be tested now.

Increasing 2W penetration a concern

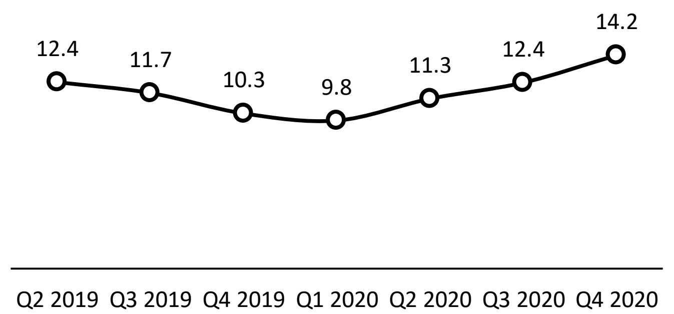
BAF's 2W/3W loan book has more than doubled over FY18-9MFY20 to INR132b. Its loan book is now larger than that of HDFCB. This segment had higher share of delinquencies at the time of demonetization. Even stress had increased pre COVID-19 with Zero+ Dpd increasing to ~14% v/s ~10% a year back.

Exhibit 33: Trend in loan book (INR b)



Source: MOFSL, Company

Exhibit 34: 0dpd+ trend in 2W/3W financing for BAF (%)



Source: MOFSL, Company

Sharp cut in home loan rates by SBI a key competitive threat

In Mar'20, SBI cut its 1-year MCLR by 75bp and is now offering home loans starting at 7.2%. Due to this, there could be increased balance transfers from BAF's book leading to margins declining gradually in this business.

Valuation matrix

	Rating	CMP	Mcap	P/E (x)		P/BV (x)		RoA (%)		RoE (%)	
		(INR)	(USDb)	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
HFCs											
HDFC*	Buy	1,690	38.8	13.7	9.7	1.7	1.2	1.7	1.7	13.1	13.2
LICHF	Buy	263	1.7	5.8	4.8	0.7	0.6	1.0	1.1	12.0	13.0
PNBHF	Neutral	179	0.4	3.5	2.7	0.3	0.3	1.1	1.4	9.6	11.5
REPCO	Buy	121	0.1	2.7	2.5	0.4	0.3	2.3	2.4	14.4	13.6
Vehicle fin.											
SHTF	Buy	744	2.3	9.9	6.3	0.9	0.8	1.6	2.4	9.0	12.7
MMFS	Buy	165	1.4	16.1	11.1	0.9	0.8	0.8	1.2	5.5	7.6
CIFC	Buy	144	1.6	9.2	7.7	1.2	1.1	2.0	2.2	14.1	14.9
Diversified											
BAF	Neutral	2,025	16.4	27.2	18.7	3.3	2.8	2.6	3.5	12.7	16.2
SCUF	Buy	719	0.6	5.4	4.7	0.6	0.5	3.0	3.4	11.4	11.8
LTFH	Buy	57	1.5	5.5	4.5	0.7	0.6	1.9	2.2	13.1	14.3
MUTH	Neutral	810	4.4	10.1	9.0	2.4	2.0	7.1	7.2	25.8	24.4
MAS	Buy	563	0.4	18.3	15.1	2.8	2.4	4.2	4.7	16.2	17.2

Financials and Valuations

Income Statement									(INR M)
Y/E MARCH	**2015**	**2016**	**2017**	**2018**	**2019**	**2020E**	**2021E**	**2022E**	**2023E**
Interest Income	48,923	65,479	87,067	115,855	163,488	227,294	257,339	283,305	329,967
Interest Expended	22,483	29,269	38,034	46,139	66,236	92,775	105,191	113,035	130,936
Net Interest Income	**26,440**	**36,211**	**49,033**	**69,716**	**97,252**	**134,519**	**152,148**	**170,270**	**199,031**
Change (%)	28.4	37.0	35.4	42.2	39.5	38.3	13.1	11.9	16.9
Other Operating Income	4,895	7,456	12,707	11,589	21,363	33,303	24,621	31,347	40,606
Other Income	364	398	260	124	167	350	420	504	605
Net Income	**31,699**	**44,065**	**61,999**	**81,429**	**118,782**	**168,172**	**177,189**	**202,121**	**240,242**
Change (%)	26.7	39.0	40.7	31.3	45.9	41.6	5.4	14.1	18.9
Operating Expenses	14,284	18,991	25,642	32,690	41,977	57,339	52,837	61,847	72,421
Operating Profits	**17,415**	**25,074**	**36,357**	**48,739**	**76,805**	**110,833**	**124,352**	**140,274**	**167,821**
Change (%)	29.0	44.0	45.0	34.1	57.6	44.3	12.2	12.8	19.6
Provisions and W/Offs	3,846	5,429	8,182	10,305	15,014	32,702	64,502	53,346	51,330
PBT	**13,569**	**19,646**	**28,175**	**38,434**	**61,792**	**78,132**	**59,851**	**86,928**	**116,491**
Tax	4,591	6,861	9,810	13,471	21,842	21,824	15,262	22,167	29,705
Tax Rate (%)	33.8	34.9	34.8	35.0	35.3	27.9	25.5	25.5	25.5
PAT	**8,979**	**12,785**	**18,366**	**24,964**	**39,950**	**56,308**	**44,589**	**64,762**	**86,786**
Change (%)	24.9	42.4	43.6	35.9	60.0	40.9	-20.8	45.2	34.0
Proposed Dividend	1,087	1,621	2,485	2,769	4,310	6,757	5,351	7,771	10,414

Balance Sheet									(INR M)
Y/E MARCH	**2015**	**2016**	**2017**	**2018**	**2019**	**2020E**	**2021E**	**2022E**	**2023E**
Capital	500	536	1,094	1,150	1,154	1,197	1,197	1,197	1,197
Reserves & Surplus (Ex OCI)	47,497	73,731	89,409	157,427	195,809	330,317	369,555	426,545	502,916
Net Worth	**47,997**	**74,266**	**90,503**	**158,577**	**196,963**	**331,514**	**370,752**	**427,742**	**504,114**
OCI	0	0	26	-98	7	7	7	7	7
Net Worth (Including OCI)	**47,997**	**74,266**	**90,528**	**158,478**	**196,970**	**331,521**	**370,759**	**427,750**	**504,121**
Change (%)	20.3	54.7	21.9	75.1	24.3	68.3	11.8	15.4	17.9
Borrowings	**266,908**	**370,247**	**508,931**	**665,573**	**1,015,879**	**1,274,864**	**1,354,906**	**1,506,749**	**1,808,098**
Change (%)	35.1	38.7	37.5	30.8	52.6	25.5	6.3	11.2	20.0
Other liabilities	13,207	25,216	19,944	23,932	29,476	33,897	38,981	44,829	51,553
Total Liabilities	**328,112**	**469,730**	**619,403**	**847,983**	**1,242,325**	**1,640,283**	**1,764,647**	**1,979,327**	**2,363,772**
Investments	**3,323**	**10,341**	**41,312**	**31,394**	**85,990**	**98,889**	**113,722**	**130,780**	**150,398**
Change (%)	1,077.9	211.2	299.5	-24.0	173.9	15.0	15.0	15.0	15.0
Loans	**311,995**	**438,309**	**564,000**	**800,001**	**1,137,135**	**1,448,710**	**1,557,363**	**1,752,033**	**2,102,440**
Change (%)	35.8	40.5	28.7	41.8	42.1	27.4	7.5	12.5	20.0
Other assets	12,795	21,080	14,091	16,587	19,200	92,684	93,562	96,513	110,935
Total Assets	**328,112**	**469,730**	**619,403**	**847,983**	**1,242,325**	**1,640,283**	**1,764,647**	**1,979,327**	**2,363,772**

E: MOFSL Estimates

Financials and Valuations

Ratios									(%)
Y/E MARCH	**2015**	**2016**	**2017**	**2018**	**2019E**	**2020E**	**2021E**	**2022E**	**2022E**
Spreads Analysis (%)									
Yield on Advances	18.1	17.5	17.4	17.0	16.9	17.3	16.8	16.8	16.8
Cost of borrowings	9.7	9.2	8.7	7.9	7.9	8.1	8.0	7.9	7.9
Interest Spread	8.4	8.3	8.7	9.1	9.0	9.2	8.8	8.9	8.9
Net Interest Margin	9.8	9.7	9.8	10.2	10.0	10.4	10.1	10.3	10.3
Profitability Ratios (%)									
Cost/Income	45.1	43.1	41.4	40.1	35.3	34.1	29.8	30.6	30.1
Empl. Cost/Op. Exps.	31.6	33.2	36.3	43.9	46.2	45.7	45.9	45.1	44.3
RoE	20.4	20.9	22.3	20.0	22.5	21.3	12.7	16.2	18.6
RoA	3.1	3.2	3.4	3.4	3.8	3.9	2.6	3.5	4.0
Asset Quality (%)									
GNPA	4,844	5,386	9,824	11,638	17,941	27,901	46,514	59,697	76,538
NNPA	1,425	1,229	2,554	3,535	7,207	8,370	20,931	26,864	34,442
GNPA %	1.6	1.2	1.7	1.4	1.5	1.9	2.9	3.3	3.5
NNPA %	0.5	0.3	0.5	0.4	0.6	0.6	1.3	1.5	1.6
PCR %	70.6	77.2	74.0	69.6	59.8	70.0	55.0	55.0	55.0
Capitalisation (%)									
CAR	18.0	19.5	19.5	24.0	20.7	19.1	20.3	21.4	21.5
Tier I	14.2	16.1	13.3	18.4	16.3	16.0	17.5	19.0	19.6
Tier II	3.8	3.4	6.2	5.5	4.4	3.2	2.8	2.4	1.9
Average Leverage on Assets (x)	6.5	6.5	6.6	5.9	5.9	5.5	4.8	4.7	4.7

Valuation	**2015**	**2016**	**2017**	**2018**	**2019E**	**2020E**	**2021E**	**2022E**	**2022E**
Book Value (INR)	96.0	138.7	165.5	275.7	341.4	553.8	619.3	714.5	842.1
Price-BV (x)					5.9	3.7	3.3	2.8	2.4
EPS (INR)	18.0	23.9	33.6	43.4	69.3	94.1	74.5	108.2	145.0
EPS Growth (%)	24.2	33.0	40.7	29.2	59.6	35.8	-20.8	45.2	34.0
Price-Earnings (x)					29.2	21.5	27.2	18.7	14.0
Dividend per Share (INR)	1.8	2.5	3.6	4.0	6.0	9.8	7.7	11.2	15.0
Dividend Yield (%)					0.3	0.5	0.4	0.6	0.7

E: MOFSL Estimates

NOTES

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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