

RESEARCH
[Initiation] Bajaj Finance | Target: Rs 5,000 | +21% | BUY

BAF 2.0 – Revamped growth engine; initiate with BUY

SUMMARY
Bajaj Finance

We initiate coverage on Bajaj Finance (BAF) with BUY and a Mar'21 TP of Rs 5,000. Strong traction in consumer finance (~40% of loans) underpins a high-yield, high-churn book that aids faster repricing, while the SME and commercial lending businesses form sustainable scale builders. We estimate a 30% CAGR in NII over FY19-FY22, alongside non-linear fee income growth form a refined cross-sales engine. Higher fixed-rate borrowings and a prudent ALM strategy are expected to sustain spreads at ~9% and fuel a 37% earnings CAGR through FY22.

[Click here for the full report.](#)

TOP PICKS
LARGE-CAP IDEAS

| Company | Rating | Target |
|-------------------------------------|--------|--------|
| Cipla | Buy | 570 |
| Eicher Motors | Buy | 25,000 |
| Petronet LNG | Buy | 400 |
| Reliance Industries | Buy | 1,860 |
| TCS | Add | 2,390 |

MID-CAP IDEAS

| Company | Rating | Target |
|-------------------------------------|--------|--------|
| Alkem Labs | Buy | 2,290 |
| Future Supply | Buy | 680 |
| Greenply Industries | Buy | 210 |
| Laurus Labs | Buy | 480 |
| Ashok Leyland | Sell | 68 |

Source: BOBCAPS Research

DAILY MACRO INDICATORS

| Indicator | Current | 2D (%) | 1M (%) | 12M (%) |
|------------------------|---------|-----------|-----------|---------|
| US 10Y yield (%) | 1.77 | (1bps) | (16bps) | (97bps) |
| India 10Y yield (%) | 6.64 | 0bps | 7bps | (65bps) |
| USD/INR | 71.20 | 0 | 0 | 0.2 |
| Brent Crude (US\$/bbl) | 63.21 | (2.1) | (4.8) | 3.4 |
| Dow | 29,186 | 0 | 2.2 | 18.8 |
| Shanghai | 3,061 | 0.3 | 3.3 | 18.6 |
| Sensex | 41,115 | (0.5) | (1.3) | 13.9 |
| India FII (US\$ mn) | 21 Jan | MTD | CYTD | FYTD |
| FII-D | (163.5) | (1,721.6) | (1,721.6) | 1,222.6 |
| FII-E | 238.3 | 1,936.4 | 1,936.4 | 9,325.6 |

Source: Bank of Baroda Economics Research

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BUY

TP: Rs 5,000 | ▲ 21%

BAJAJ FINANCE

| NBFC

| 24 January 2020

BAF 2.0 – Revamped growth engine; initiate with BUY

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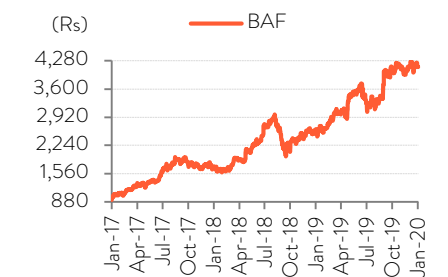
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Consumer finance, cross-sell to remain key moats: Consumer finance will remain the customer acquisition engine for BAF, driving cross-sales of credit and fee-based products to vetted clients. We expect non-linear fee income growth (~3x over FY19-FY22) from the cross-sell franchise to largely cover for operating cost (~2x). A bulk of NII will thus flow into operating profit which is estimated to log a 33% CAGR through to FY22 vs. a 27% CAGR in AUM.

| | |
|------------------|-------------------|
| Ticker/Price | BAF IN/Rs 4,126 |
| Market cap | US\$ 34.8bn |
| Shares o/s | 602mn |
| 3M ADV | US\$ 66.2mn |
| 52wk high/low | Rs 4,253/Rs 3,950 |
| Promoter/FPI/DII | 56%/22%/10% |

Source: NSE

Sustainable scale builders and stable spreads: SME and commercial lending (together 24% of AUM) offer profitable and opportunistic credit plays that mitigate BAF's concentration in the top-10 cities. We expect a prudent liability mix and rural lending to help sustain spreads at ~9% over FY19-FY22 and model for a 150bps decline in C/I ratio over this period led by technology investments.

STOCK PERFORMANCE

Source: NSE

Well managed asset quality to drive return ratios: The use of technology and data analytics for prudent product positioning and cross-sales has kept credit risk at bay. Credit cost is expected to remain stable at ~200bps over the next three years, thus driving healthy ROE of 22%+.

Initiate with BUY: We have a Mar'21 TP of Rs 5,000 for BAF using a residual income model, assuming 12.8% CoE, 7.75% risk-free rate and 5% terminal growth.

KEY FINANCIALS

| Y/E 31 Mar | FY18A | FY19A | FY20E | FY21E | FY22E |
|-------------------------|--------|--------|---------|---------|---------|
| Net interest income | 69,716 | 97,252 | 135,172 | 171,485 | 213,464 |
| NII growth (%) | 42.2 | 39.5 | 39.0 | 26.9 | 24.5 |
| Adj. net profit (Rs mn) | 24,964 | 39,950 | 61,728 | 82,232 | 102,432 |
| EPS (Rs) | 43.4 | 69.3 | 102.6 | 136.7 | 170.2 |
| P/E (x) | 95.1 | 59.6 | 40.2 | 30.2 | 24.2 |
| P/BV (x) | 15.0 | 12.1 | 7.4 | 6.1 | 5.0 |
| ROA (%) | 3.4 | 3.8 | 4.2 | 4.3 | 4.4 |
| ROE (%) | 20.1 | 22.5 | 23.2 | 22.1 | 22.6 |

Source: Company, BOBCAPS Research



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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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