BANDHAN

RESULT UPDATE

nuvama institutional equities

KEY DATA

Rating	HOLD
Sector relative	Neutral
Price (INR)	237
12 month price target (INR)	265
Market cap (INR bn/USD bn)	382/4.7
Free float/Foreign ownership (%)	47/32.5

What's Changed

Target Price	↑
Rating/Risk Rating	–

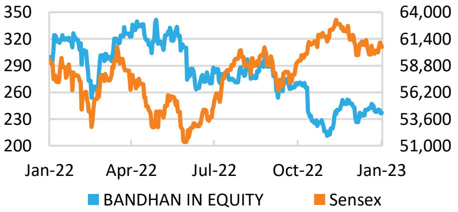
QUICK TAKE

	Above	In line	Below
Profit		●	
Margins			●
Revenue Growth			●
Overall		●	

FINANCIALS (INR mn)

Year to March	FY22A	FY23E	FY24E	FY25E
Revenue	115368	116217	145380	166944
PPoP	80134	71544	91772	102615
Adjusted profit	1258	24615	54059	59178
Diluted EPS (INR)	0.2	15.3	33.6	36.7
EPS growth (%)	(94.3)	9681.3	119.6	9.5
P/E (x)	1517.2	15.5	7.1	6.5
RoAE (%)	0.7	13.3	24.6	22.2

PRICE PERFORMANCE



Explore:

Financial model

Podcast

Corporate access

Video

Asset quality rebounds

Standard stress pool (1-90 DPD EEB loans) reduced sharply from 13.1% to 8.1% QoQ in Q3FY23, as guided. EEB slippage also fell from INR36bn to INR28.5bn with 90% from the disclosed stress pool. While NII growth missed estimates by a wide margin because of reversal and write-off, asset quality improvement is the overwhelming factor.

Earnings have bottomed out in Q3FY23 with a likely sharp recovery in NIM and credit cost in Q4FY23E. We are raising earnings by 18% for FY24E building in a higher NIM and lower credit cost. We are rolling forward the base to FY25E and thus revise the TP to INR265/1.5x BV FY25E (from 1.7x FY24E). Retain 'HOLD' as we believe Bandhan's business transformation reduces visibility on medium-term earnings.

Slippage and standard stress both decline substantially

EEB slippage slid from 27% to 20% QoQ and total slippage decreased from 19% to 15% QoQ. While slippage was elevated in Q3, the stress pool (1-90dpd) has reduced substantially, suggesting a substantially lower run-rate of slippage from Q4FY23. EEB stress pool has declined to 8% from 13% QoQ while, excluding-SMA0, stress had declined to 4.7% from 9.3% QoQ. The bank wrote off INR24bn/4% in EEB versus 7% QoQ. EEB NPL rose 1% QoQ. Total NPL rose 1.6% QoQ and stood at 7.2% of loans while the PCR improved to 72% from 71%. We expect EEB slippage to moderate to INR12bn/7.7% in Q4FY23E from INR29bn QoQ. Management guided that the normalized run rate of stress would settle at 1% higher than pre-covid, which implies normalized stress loans of 5–6% via-a-vis 4–5% pre-covid.

Miss on NII due to reversal on slippage

NII declined 2% QoQ/5% YoY due to write-offs/reversals. NIM in October fell to 6.75% from 7% in Q2FY23, but recovered to 7.3% in December. Other income ex-ARC sale grew 31% QoQ, but declined 12% YoY. The bank has not resumed sale of PSLC. Total other income, including ARC recovery of INR4.1bn, grew 46% QoQ/117% YoY. The entire ARC recovery included in PPOP was used towards higher provisions. Core PPOP dipped 3% QoQ/22% YoY.

Outlook and valuation: Earnings have bottomed, but retain 'HOLD'

We believe earnings and valuation have bottomed. While earnings will rebound in FY24E driven by below-normal credit cost and higher NIM and asset growth, long-term earnings visibility from the business transformation is low as Bandhan moves away from its core competency to intensely competitive segments. Retain **'HOLD'**.

Financials

Year to March	Q3FY23	Q3FY22	% Change	Q2FY23	% Change
NII	20,804	21,248	-2.1	21,930	-5.1
Pre-provisioning Profits	19,222	19,501	-1.4	15,529	23.8
Reported Profits	2,906	8,590	-66.2	2,093	38.9
EPS	1.81	5.33		1.3	

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Financial Statements

Income Statement (INR mn)

Year to March	FY22A	FY23E	FY24E	FY25E
Net interest income	87,140	91,741	1,13,286	1,29,189
Non interest income	28,228	24,476	32,093	37,755
Net revenues	1,15,368	1,16,217	1,45,380	1,66,944
Operating expense	35,234	44,673	53,608	64,329
Employee exp	21,349	26,900	32,279	38,735
Other opex	13,886	17,774	21,328	25,594
Preprovision profit	80,134	71,544	91,772	1,02,615
Provisions	78,848	38,636	19,500	23,500
PBT	1,286	32,908	72,272	79,115
Taxes	28	8,293	18,213	19,937
PAT	**1,258**	**24,615**	**54,059**	**59,178**
Extraordinaries	0	0	0	0
Reported PAT	1,258	24,615	54,059	59,178
Diluted EPS (INR)	0.2	15.3	33.6	36.7

Balance Sheet (INR mn)

Year to March	FY22A	FY23E	FY24E	FY25E
Equity capital	16,110	16,110	16,110	16,110
Reserves	1,57,704	1,80,921	2,26,558	2,73,892
Net worth	1,73,814	1,97,031	2,42,668	2,90,002
Deposits	9,63,300	10,78,896	12,73,097	15,27,717
Borrowings	1,99,216	1,90,251	2,13,082	2,38,651
Other liabilities	52,336	29,221	33,604	36,965
Total	**13,88,665**	**14,95,399**	**17,62,451**	**20,93,334**
Assets				
Loans	9,39,749	9,58,544	11,31,082	13,34,677
Investments	2,90,787	3,52,334	4,23,230	5,23,722
Cash & equi	93,214	89,774	98,751	1,08,627
Fixed assets	5,879	8,554	10,264	12,317
Other assets	59,037	86,194	99,123	1,13,991
Total	**13,88,665**	**14,95,399**	**17,62,451**	**20,93,334**
BV/share (INR)	21.6	122.3	150.6	180.0
ABV/share (INR)	107.9	122.1	150.7	180.1

Important Ratios (%)

Year to March	FY22A	FY23E	FY24E	FY25E
Net interest margins	7.4	7.0	7.8	7.4
Cost-income	30.5	38.4	36.9	38.5
Tax rate	2.2	25.2	25.2	25.2

Balance Sheet Ratios (%)

Year to March	FY22A	FY23E	FY24E	FY25E
Credit growth	15.1	2.0	18.0	18.0
Deposit growth	23.5	12.0	18.0	20.0
EA growth	17.2	5.8	18.0	19.0
Gross NPA ratio	6.8	7.0	6.4	5.5
Provision coverage	75.5	73.0	71.0	71.0

Valuation Metrics

Year to March	FY22A	FY23E	FY24E	FY25E
Diluted PE (x)	1517.2	15.5	7.1	6.5
Price/BV (x)	11.0	1.9	1.6	1.3
Price/ABV (x)	2.2	1.9	1.6	1.3

Source: Company and Nuvama estimates

ROA Decomposition (%)

Year to March	FY22A	FY23E	FY24E	FY25E
NII/Assets	7.4	7.0	7.8	7.4
Fees/Assets	2.1	1.9	2.0	2.0
Inv profits/Assets	9.8	8.9	10.0	9.6
Net revenues/assets	(3.0)	(3.4)	(3.7)	(3.7)
Opex/Assets	(6.7)	(3.0)	(1.3)	(1.4)
Provisions/Assets	(6.7)	(3.0)	(1.3)	(1.4)
Taxes/Assets	0	(0.6)	(1.2)	(1.1)
Total costs/Assets	(9.7)	(7.0)	(6.3)	(6.2)
RoA	0.1	1.9	3.7	3.4
Equity/Assets	14.8	14.2	15.1	15.4
RoAE	0.7	13.3	24.6	22.2

Valuation Drivers

Year to March	FY22A	FY23E	FY24E	FY25E
EPS growth (%)	(94.3)	9681.3	119.6	9.5
RoAE (%)	0.7	13.3	24.6	22.2

We revise earnings, but retain 'HOLD'

We are tweaking earnings for FY23 but increasing earnings in FY24E sharply by 18% as we believe Bandhan's credit cost will be substantially lower than the post-Covid normalized run rate of 1.8%. Margins will also rebound to 7.7% from the Q3FY23 low of 6.75% as FY24 will be free of the sharp reversal of interest income seen in 9MFY23 and the bank will reap the benefit of higher lending rates and lower conversion of SA into bulk term deposits leading to lower CoF.

While earnings and valuation have bottomed out, we still believe that there is low visibility on longer term earnings because 1) Bandhan is moving away from its core competency into intensely competitive segments 2) While the bank is planning to reduce risky EEB group loans to 26% from 40% by FY25E, including individual EEB loans, total exposure to microfinance will remain high at ~49% (which means that Bandhan will still be exposed to the volatility of the microfinance business which has increased in the last 5 years.) 3) Bandhan's deposit franchise is weaker than large private banks exposing it to the risk of higher CoF in rising rate cycles. The proportion of savings deposits above INR 20M stands at 10% of total.

As such while the stock price has corrected sharply post Q2 earnings, we do not see strong core triggers to upgrade the stock to BUY. We retain HOLD.

We are rolling base to FY25E. Our target price for the stock stands revised to INR 265 based on 1.5x PBV FY25E from 1.8x PBV FY24E earlier.

Key earnings highlights:

- Core earnings were weak with a decline EEB loans and disbursals, a sharp decline in NIM and a higher proportion of bulk deposits. However, asset quality improved substantially as guided, which was the overwhelming highlight of Q3FY23.
- Net loans grew 2% QoQ / 15% YoY while gross loans grew 2% QoQ /11% YoY.
- EEB loans declined 8% YoY / 2% QoQ driven by a sharp decline in disbursements in micro loans and write-offs.
- Retail loans grew strongly at 133% YoY / 22% QoQ while mortgages grew 28% YoY / 4% QoQ. Growth in mortgages moderated because of a sharp rise in rates that hurt affordability. However, according to management, mortgage growth will pick up in Q4FY23.
- Deposits grew 21% YoY and 3% QoQ. There was a sharp decline in SA that declined 9% QoQ / 6% YoY as customers with SA balances of more than INR 20M moved to bulk term deposits. High value savings account for 10% of total. Due to this migration, there was a strong growth of 22% QoQ / 139% YoY in bulk term deposits. Proportion of bulk deposits rose sharply to 31% from 26% QoQ.
- Management believes that most of the migration from savings to term is through, as rate-sensitive high net worth clients do not wait for long to convert savings into term.
- NIM declined from 7% to 6.75% QoQ due to interest reversal on slippage and higher proportion of bulk deposits
- NII declined 5% QoQ and 2% YoY and was significantly below consensus.
- Other income ex ARC sale, grew 31% QoQ but declined 12% YoY. The bank has not resumed sale of PSLC. Total other income including ARC recovery of INR

4.1bn grew 46% QoQ / 117% YoY. The entire ARC recovery included in PPOP was used towards higher provisions.

- Core PPOP declined 3% QoQ and 22% YoY.
- Loan provisions stood at INR 15bn, up 21% QoQ rising from 5.7% to 6.6% of loans QoQ. The bank used the recovery from sale of ARC of INR 4bn to make higher provisions.
- PAT of INR 2.9bn declined 66% YoY and 39% QoQ
- The bank recovered INR 9.7bn from CGFMU. Of this INR 7.8bn went towards provisions and the remaining is part of other liabilities. The bank also sold assets of INR 8bn to an ARC. The recovery income of INR 4.1bn was part of other income while the portion of SR of INR 3.9bn is fully provided for.

Collection efficiency and asset quality

- Collection efficiency ex NPL improved from 95% in September to 98% in December.
- CE in WB improved to 98% in December from 96% in September while CE in Assam improved from 87% to 96%.
- EEB slippage declined from 27% to 20% QoQ while total slippage declined from 19% to 15% QoQ. While slippage was elevated in Q3, the stress pool (1-90dpd) has reduced substantially suggesting a substantially lower run-rate of slippage from Q4FY23. Stress pool has declined to 8% from 13% QoQ while excluding SMA0 stress had declined to 4.7% from 9.3% QoQ.
- Total slippage has declined from 19% to 15%. The bank wrote-off INR 24bn / 4% in EEB versus 7% QoQ. EEB NPL rose 1% QoQ.
- Total NPL rose 1.6% QoQ and stood at 7.2% of loans while PCR improved to 72% from 71%.
- We expect EEB slippage to moderate to INR 12bn / 7.7% in Q4FY23E from INR 29bn QoQ.
- Mgmt. guided that the normalized run rate of EEB stress would settle at 1% higher than pre-Covid, which implies normalized stress loans of 5-6% from 4-5% pre-Covid.

Guidance

- The bank has hiked lending rates by 250bp in FY23, of which 50bp was in September and the remaining in November.
- NIM fell sharply to 6.75% in October and November but revived to 7.3% in December.
- Management expects NIM to improve to 7.75% over the next few quarters with higher lending rates, stabilization of deposit mix and lower slippage.
- Management retains guidance of GNPL of INR 80bn from EEB in Q3 versus INR 74bn (gross of write-off) in Q2.

CGFMU recovery of INR 17bn is expected in H1FY24E.

The normalized level of stress loans pre-Covid were 4-5%. Post Covid EEB CE will settle at 98% versus 99% pre-Covid. As such, the post Covid normalized level of stress loans will be 5-6%

Credit cost for Q4 will be INR 4-5bn versus INR 15bn in Q3FY23.

The bank has stopped lending to NPL accounts effective Q2FY23.

Loan growth will likely be 20% in FY24 with EEB growing 18% and faster growth in non-EEB segments

Exhibit 1: EEB stress

INR bn	Q3FY23	Q2FY23	Q1FY23
SMA0	17.9	25.9	27.3
SMA1	10.4	13.7	13.9
SMA2	14.2	30.6	32.7
Total SMA	42.5	70.2	73.9
as % of EEB Loans	8%	13%	13%
Restructured loans	-	-	21.4
Total standard stress	42.5	70.2	95.3
Standard stress as % of EEB	8%	13%	16%
Standard stress ex SMA0 as % of EEB	5%	8%	12%
NPLs	51.2	50.7	53.5
PCR on NPLs	38.0	41.5	
Write-off	24.0	35.0	
Total stress	117.7	155.9	148.8
as % of EEB Loans	22%	29%	26%
Totla stress ex write-offs as % of EEB loans	18%	22%	26%

Source: Company, Nuvama Research

Exhibit 2: Guidance on recovery stress pool

INR bn	Q3FY23	Q2FY23	Q1FY23
Total stress pool (A)	**76**	**95**	**121**
of which NPL	51	51	53
of which standard stress	25	44	68
Provisions	50	53	76
CGMFU recovery	17	25	25
Organic recovery	10	15	25
Assam relief	-	-	-
Total provisions + recovery (B)	**77**	**93**	**126**
Net stress © = A - B	**-1**	**2**	**-5**

Source: Company, Nuvama Research

Exhibit 3: Incremental stress

INR bn	Q3FY23	Q2FY23	Q1FY23
Slippage	32.65	40	11
as % of lagged loans	15%	19%	5.20%
Write-off	25.33	35	-
SMA1+2	24.6	44	47
Total incremental stress	82.58	119	58
as % of lagged loans	20.7%	26.6%	12.5%

Source: Company, Nuvama Research

Exhibit 4: Movement of EEB NPL

INR bn	Q2FY23	Q3FY23	Q4FY23E
Opening	53.5	50.54	51.3
Slippage	36.2	28.5	12.0
Recovery	3.8	4	7
write off	35.4	23.97	4
Closing	50.54	51.3	52.3
Slippage ratio, %	26.8%	19.8%	7.7%

Source: Company, Nuvama Research

Exhibit 5: Movement of total NPL

INR bn	Q2FY23	Q3FY23
Opening	69.7	68.5
Slippage	39.5	32.6
Recovery	5.3	6.22
write off	35.4	25.33
Closing	68.5	69.6
Slippage ratio, %	19.3%	14.8%

Source: Company, Nuvama Research

Exhibit 6: Movement of NIM

%	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23
NIM	7.8	8.7	8	7	6.5
Cost of funds	5.2	5.1	5.3	5.5	5.8
Yield	12.6	13.3	12.9	12.0	12.0

Source: Company, Nuvama Research

Exhibit 7: Asset book mix

INR bn	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23
Micro	575.6	624.0	581.3	539.2	527.6
Mortgages	209.4	235.6	246.2	258.0	267.3
Retail	11.3	16.6	18.2	21.6	26.3
SME, NBFC - MFI & NBFC - Others	83.7	117.2	120.9	139.5	156.7
Total	**880.0**	**993.4**	**966.6**	**958.3**	**977.9**

Source: Company, Nuvama Research

Exhibit 8: Deposit mix

INR bn	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23
Current account	39.1	54.6	43.7	50.5	47.4
Saving account	346.2	346.2	358.2	354.7	324.7
Term deposit - Retail	329.1	343.6	327.6	331.4	338.4
Term deposit - Others	130.6	218.9	201.1	257.1	312.3
Total deposits	**845.0**	**963.3**	**930.6**	**993.7**	**1022.8**

Source: Company, Nuvama Research

Exhibit 9: Financial snapshot (INR mn)

Year to March	Q3FY23	Q3FY22	Growth (%)	Q2FY23	Growth (%)
Interest on advances	32,603	29,753	9.6	32,646	(0.1)
Interest on investments	4,864	3,944	23.3	4,555	6.8
Interest on other resources	141	387	(63.4)	138	2.1
Other interest income	468	3	14,038.0	395	18.7
Interest income	38,076	34,088	11.7	37,735	0.9
Interest expenses	17,272	12,840	34.5	15,805	9.3
Net interest income	**20,804**	**21,248**	**(2.1)**	**21,930**	**(5.1)**
Other income	10,333	7,090	45.7	4,764	116.9
Operating expenses	11,916	8,837	34.8	11,165	6.7
Staff expenses	6,867	5,279	30.1	6,663	3.1
Other opex	5,049	3,557	41.9	4,502	12.1
Pre prov Op profit (PPP)	**19,222**	**19,501**	**(1.4)**	**15,529**	**23.8**
Provisions	15,415	8,057	91.3	12,797	20.5
Profit before tax	3,807	11,444	(66.7)	2,732	39.3
Provision for tax	901	2,855	(68.4)	640	40.9
Profit after tax	**2,906**	**8,590**	**(66.2)**	**2,093**	**38.9**
EPS (INR)	1.8	5.3	n.a.	1.3	39.2
Ratios	0.1	0.1	0.1	0.1	0.1
NII / GII	54.6	62.3		58.1	
Cost - income	38.3	31.2		41.8	
Provisions / PPOP	80.2	41.3		82.4	
Tax rate	23.7	24.9		23.4	
Balance sheet (INR bn)		0.1	0.1	0.1	0.1
Advances	**921**	**803**	**14.7**	**902**	**2.1**
Deposits	**1,023**	**845**	**21.0**	**994**	**2.9**
CD Ratio (%)	90.0	95.0		90.8	

Source: Company, Nuvama Research

Exhibit 10: Change in estimates

	FY23E	FY24E	FY23E	FY24E	FY25E	FY23E	FY24E
		Old		**New**	**(Introduced)**		**% Change**
NII, INR M	97,439	1,17,597	91,741	1,13,286	1,29,189	-5.8%	-3.7%
PAT, INR M	24,255	45,642	24,615	54,059	59,178	1.5%	18.4%
EPS, INR	15.1	28.3	15.3	33.6	36.7	1.2%	18.6%
BVPS, INR	123.4	149.1	122.3	150.6	180.0	-0.9%	1.0%
Target price, INR	**250**		**265**			**6.0%**	

Source: Company, Nuvama Research

Company Description

Bandhan Bank started its journey as a not-for-profit entity in 2001, which became an NBFC in 2009 and then the first microfinance company to receive a banking licence from the RBI in August 2015. The company was established by Mr. Chandra Shekhar Ghosh to provide micro loans to women that are socially disadvantaged and economically exploited. It is a bank for all, but its focus remains on meeting financial needs of people that are overlooked by the formal banking system—economically disadvantaged sections of society—and acting as a vehicle-of-empowerment and creating better education, health care and self-employment opportunities.

In January 2019, Bandhan decided to merge with Gruh Finance. Gruh Finance is a housing finance company with a loan book of ~INR177bn (June 2019) engaged in retail home loans (95% are retail loans and 5% are developer loans). The synergies from this merger include geographical, loan book diversification, cross-sell opportunities, lower cost of funds for Gruh's liabilities, etc. The bank has a network of 1,107 branches, 4,090 banking units and 487 ATMs spread across 34 states/UTs.

Investment Theme

Bandhan plans to diversify out of its core competency into highly competitive segments. With low visibility on long term earnings from the transformation, we maintain HOLD.

Key Risks

Asset quality risks in the microfinance portfolio

A sharper than expected rise in cost of funds if deposit competition intensified.

Additional Data

Management

MD & CEO	Chandra Shekhar Ghosh
Chairman	Anup Kumar Sinha
COO	Sunil Samdani
Director	Bhaskar Sen
Auditor	E&Y

Holdings – Top 10*

	% Holding		% Holding
HDFC	9.89	Societe General	1.19
Caladium Invst	7.79	Nomura	0.88
Blackrock	3.04	Touchstone Adv	0.54
LIC	2.11	Standard Life	0.43
Vanguard	1.78	Nippon Life	0.42

**Latest public data*

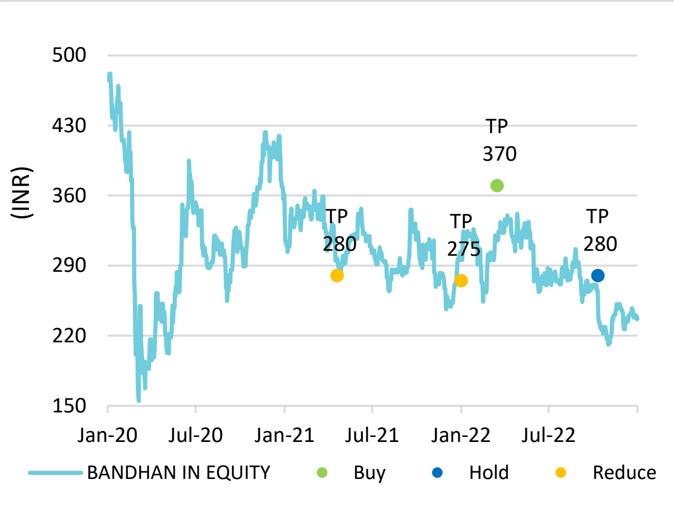
Recent Company Research

Date	Title	Price	Reco
01-Dec-22	Pain to persist in Q3FY23; no hurry to b; *Company Update*	271	Hold
30-Oct-22	Big miss; lofty slippage to persist in; *Result Update*	271	Hold
22-Jul-22	Quarter marked by one-offs; *Result Update*	317	Buy

Recent Sector Research

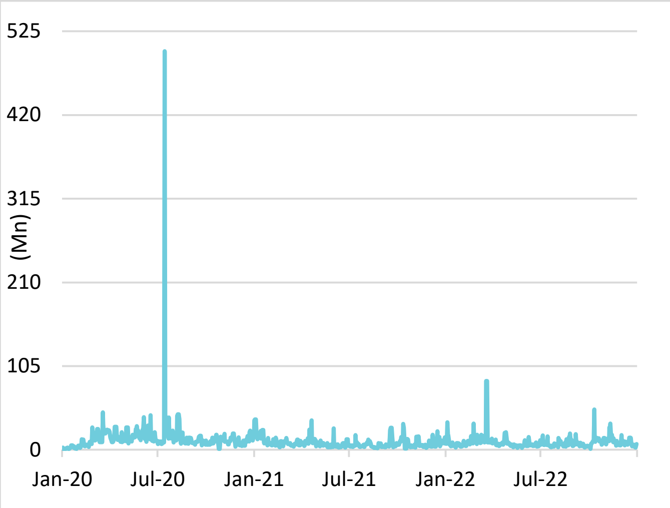
Date	Name of Co./Sector	Title
20-Sep-21	Banking	Reimagining credit; *Sector Update*
11-Feb-20	Union Bank (I)	Union Bank of India - Result Update Q3FY; *Result Update*
17-Jan-20	South Ind.Bank	South Indian Bank - Result Update Q3FY20; *Result Update*

Rating Interpretation



Source: Bloomberg, Nuvama research

Daily Volume



Source: Bloomberg

Rating Distribution: Nuvama Research Coverage

	Buy	Hold	Reduce	Total
Rating Distribution*	179	62	19	260
	>50bn	**>10bn and <50bn**	**<10bn**	**Total**
Market Cap (INR)	228	31	1	260

* *stocks under review*

Rating Rationale

Rating	Expected absolute returns over 12 months
Buy:	>15%
Hold:	>15% and <-5%
Reduce:	<-5%

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