Bandhan Bank | BUY

Gruh merger : Look beyond the near-term

Bandhan Bank has seen a sharp correction in its market cap (INR 86bn, 15% fall) since the announcement of its merger with Gruh Finance, and we believe the impact of EPS / BVPS dilution (13% / 14% in FY20E) as a result of the rich price paid for the acquisition has been more than factored in. We factor in the merger in our estimates and looking ahead, we believe the current price offers an attractive entry point for the stock. Following the merger, Bandhan will remain India's most profitable banking franchise (RoA / RoE of 3.6% / 24% in FY21E), with top-notch asset quality and loan growth metrics. The secured nature of Gruh's book provides further comfort on Bandhan's asset quality, while diversifying the book geographically. Separately, the eastern Indian housing finance market is one of the most underpenetrated (Exhibit 5), and also houses India's 2 most populous states (WB and Bihar). Our mock-up analysis suggests that, armed with Gruh's systems and processes, Bandhan can scale up the housing finance business to c.INR 150bn by FY25E in its home market (Exhibit 11). Further, the bank's management has indicated that Gruh's mid and senior management will continue at the bank, which we believe is essential for integration efforts (with Mr. Choksey being appointed as Executive Director subject to RBI approval). We maintain BUY with a revised TP of INR 600, valuing the merged bank at 4.8x FY21E BVPS.

- **Still India's most profitable bank with top-notch asset quality:** The merged entity will continue to be India's most profitable bank (RoA / RoE of 3.6% / 24% in FY21E). Further, Gruh's top-notch asset quality (0.5% NNPLs), the completely granular and secured nature of its book (vs. Bandhan's almost completely unsecured) and the reduction in Bandhan's geographical concentration in the east provide further comfort on credit costs in our view. Despite the apparent differences in their business models, there are inherent similarities between the 2 businesses – a) Focus on similar target segments (from a purely economic perspective) – 65% of Gruh's customers have monthly family incomes below INR 25k. b) Both are inherently high RoE businesses and c) Structurally low opex ratios - while Bandhan has the leanest opex ratio among banks (cost to income of 33.7% in 9MFY19), Gruh's cost ratios are one of the best in the BFSI space (16% cost-to-income in 9MFY19).
- **Are the diversification benefits real?** Apart from getting Gruh's completely secured portfolio (vs. Bandhan's unsecured) and reduction in concentration risks, we believe that there is abundant opportunity for Bandhan to scale up Gruh's business in its home market. Since its conversion to a bank, Bandhan has scaled up its SEL (small enterprise loan) book to INR 16.4bn from c.86k customers (as of FY18 – 21 months since launch). SEL loans cater to a similar economic segment as that of Gruh's customer base, with disbursement ticket sizes in the range of INR 0.1-1mn, while 58% of Gruh's loans have ticket sizes <INR 0.5mn. We believe SEL distribution centres (137 as of FY18) offer the opportunity for Bandhan to quickly scale up Gruh's housing loan business in its home market. Our mock-up suggests that Bandhan could scale up the housing loan business to c.INR 150bn by FY25E.
- **Management continuity to aid integration:** Bandhan has indicated that senior / mid management at Gruh (including Mr. Choksey), are expected to continue at Bandhan. Bandhan expects RBI nod for the merger by end-Feb/early March 2019.

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Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	600
Upside/(Downside)	48.2%
Previous Price Target	650
Change	-7.7%

Key Data – BANDHAN IN

Current Market Price	INR405
Market cap (bn)	INR483.0/US$6.8
Free Float	13%
Shares in issue (mn)	1,192.8
Diluted share (mn)	
3-mon avg daily val (mn)	INR651.3/US$9.1
52-week range	742/368
Sensex/Nifty	36,469/10,894
INR/US$	71.3

Price Performance

%	1M	6M	12M
Absolute	-27.3	-42.7	0.0
Relative*	-27.7	-41.1	0.0

* To the BSE Sensex

Financial Summary *(Pro forma merged with Gruh from FY20E onwards)* (INR mn)

Y/E March	FY17A	FY18A	FY19E	FY20E	FY21E
Net Profit	11,119	13,456	18,443	34,085	44,094
Net Profit (YoY) (%)	304.0%	21.0%	37.1%	84.8%	29.4%
Assets (YoY) (%)	53.0%	46.5%	40.6%	73.9%	27.5%
ROA (%)	4.4%	3.6%	3.5%	3.6%	3.6%
ROE (%)	28.6%	19.5%	18.0%	23.7%	24.3%
EPS	10.2	11.3	15.5	21.2	27.4
EPS (YoY) (%)	304.0%	11.1%	37.1%	37.1%	29.4%
PE (x)	**39.9**	**35.9**	**26.2**	**19.1**	**14.8**
BV	41	79	93	100	126
BV (YoY) (%)	33.3%	93.7%	18.4%	6.9%	26.3%
P/BV (x)	**9.97**	**5.15**	**4.35**	**4.07**	**3.22**

Source: Company data, JM Financial. Note: Valuations as of 01/Feb/2019

1. What happens to the promoter shareholding?

Rich valuations of Gruh notwithstanding, we like the deal as it helps Bandhan move closer to attaining a reduction in promoter stake (BFHL currently owns 82.3% which it needs to bring down to 40%) while acquiring a top-notch franchise. BFHL's holding in the merged entity will come down to 61%. We believe that Bandhan is better off acquiring a high quality business that enables it to diversify into a low-risk product than buying a sub-par business (by paying a premium) just to ensure regulatory compliance.

The bank expects to receive the Reserve Bank of India's (RBI) approval for the transaction by end-February/early-March 2019. Subsequently, the bank will approach the National Company Law Tribunal (NCLT) for the transaction approval which is likely to take another 6-8 months.

Having already completed a significant stake reduction to comply with regulatory directives, Bandhan intends to appeal to the RBI to lift restrictions (on automatic branch opening and MD's compensation) along with the next steps for reducing from 61% (post-transaction approval) to 40%.

Notably, the RBI itself has proposed that it will look to harmonise the prevalent differences in the corporate structure permissible to banks for setting up financial services entities (depending upon the timing of their licensing), Bandhan will remain watchful of the developments on this front, wherein clarity is expected to emerge by mid-FY20.

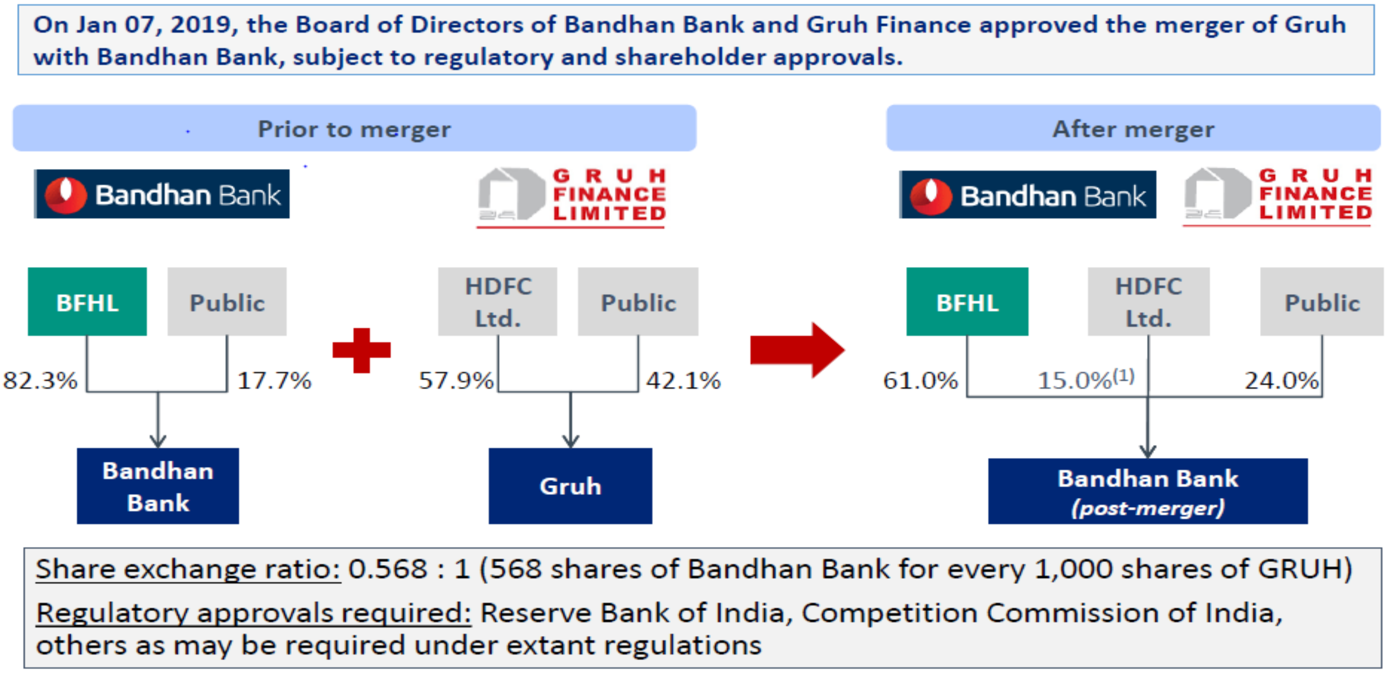
Bandhan remains committed to ensure that any further measures to comply with promoter shareholding requirements will not result in stake sell-down by the promoter in open market. This could be achieved in the following ways (subject to regulatory approval):

- Collapsing the existing 3-tier shareholding structure (Bandhan -> BFHL - > BFSL -> BFSL shareholders). This could allow Bandhan to nominate the trusts: FIT and NEFIT as the Promoter Group, who would then have 24.8% shares in the merged entity (based on current economic interest; 33.5% pre-merger).
- Extension in the timeline for further reduction of promoters' stake as is currently allowed to small finance banks. The RBI's guidelines for licensing of small finance banks (Nov-2014) allows them a period of 5 years from date of commencement of operations, to bring down the promoter's shareholding to 40%. In contrast, Bandhan had to bring down its promoters' shareholding to 40% within 3 years. If the RBI allows such an extension, Bandhan will have time till Aug-2020 (18 months from now), to achieve the desired reduction to 40%.

Separately, HDFC Ltd. has applied for permission from the RBI to hold 14.96% shares in the merged bank. The approval / disallowance for the same is expected along with the RBI's approval for the merger scheme in Feb19. If HDFC Ltd. is disallowed from holding 14.96% permanently in the bank, it will seek a timeline from the RBI to bring down its shareholding to 10% over a period of time. Management believes this could enable HDFC Ltd. to bring down its shareholding in tranches, without incurring large equity supply risks.

We believe that through the acquisition Bandhan has made a substantial move towards regulatory compliance and now has a greater possibility of getting a relief from regulatory restrictions. Moreover, the bank has recently received permission from the regulator (link) to open 40 new branches, in Dec 2018, which were promptly opened in 3QFY19.

Exhibit 1. BFHL's holding in the merged entity comes down to 61% from 82.3% currently in Bandhan Bank



Source: Company

2. Are the diversification benefits real?

By merging with Gruh, Bandhan will acquire an almost entirely complimentary loan book profile. While both banks cater to the bottom of the pyramid, a) Gruh's loan book is completely secured (vs. Bandhan's almost completely unsecured micro and MSME loan book) and b) Gruh is dominant in western India, where Bandhan has a relatively lower presence.

Gruh gets access to Bandhan's ~4000 touchpoints:

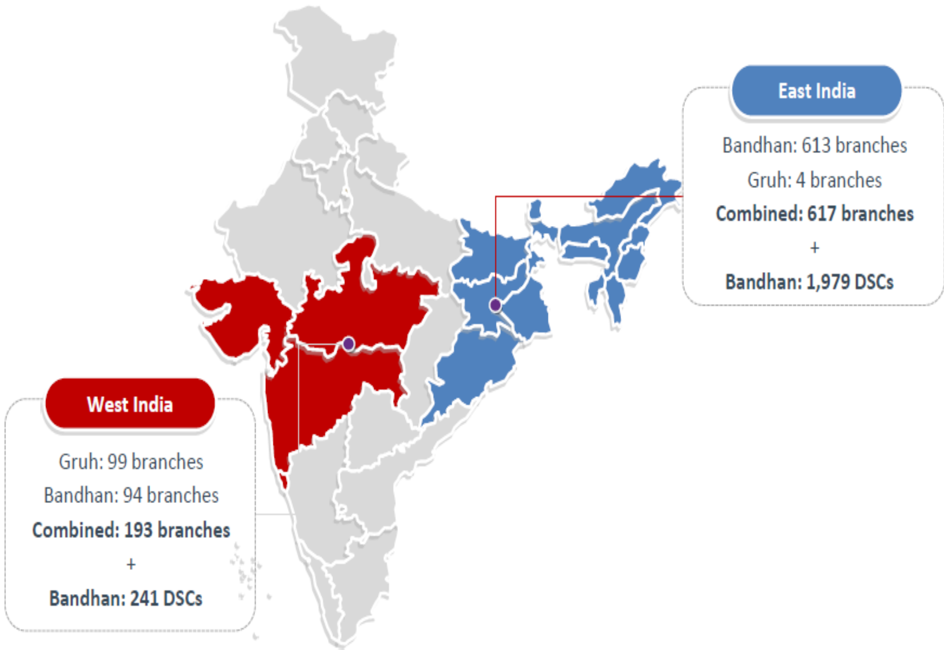
Currently, Gruh has 195 branches spread across 11 states. Its business is concentrated in western and central India (Gujarat, Maharashtra and Madhya Pradesh) with 68% of the branches and c. 80-85% of the portfolio in this region. Post-merger, Gruh will get access to Bandhan's large network of c.4,000 branches and DSCs which it can leverage to expand its footprint across other geographies, particularly east and north-east India. Further, Gruh will also gain access to the Bandhan's 15.3mn strong customer base, which can be targeted to fuel the incremental housing credit growth.

Exhibit 2. Region-wise branch-network of the merged entity (as of 1HFY19)

State	GRUH	Bandhan (incl. DSCs)	Total
East	4	2,012	2,016
Central	50	639	689
North Eastern	0	564	564
North	13	225	238
South	29	175	204
West	99	335	434
Total	195	3,950	4,145

Source: Company, JM Financial

Exhibit 3. Expansion of geographical presence (as of 1HFY19)



Source: Company

Exhibit 4. State-wise footprint of the merged entity (as of 1HFY19)

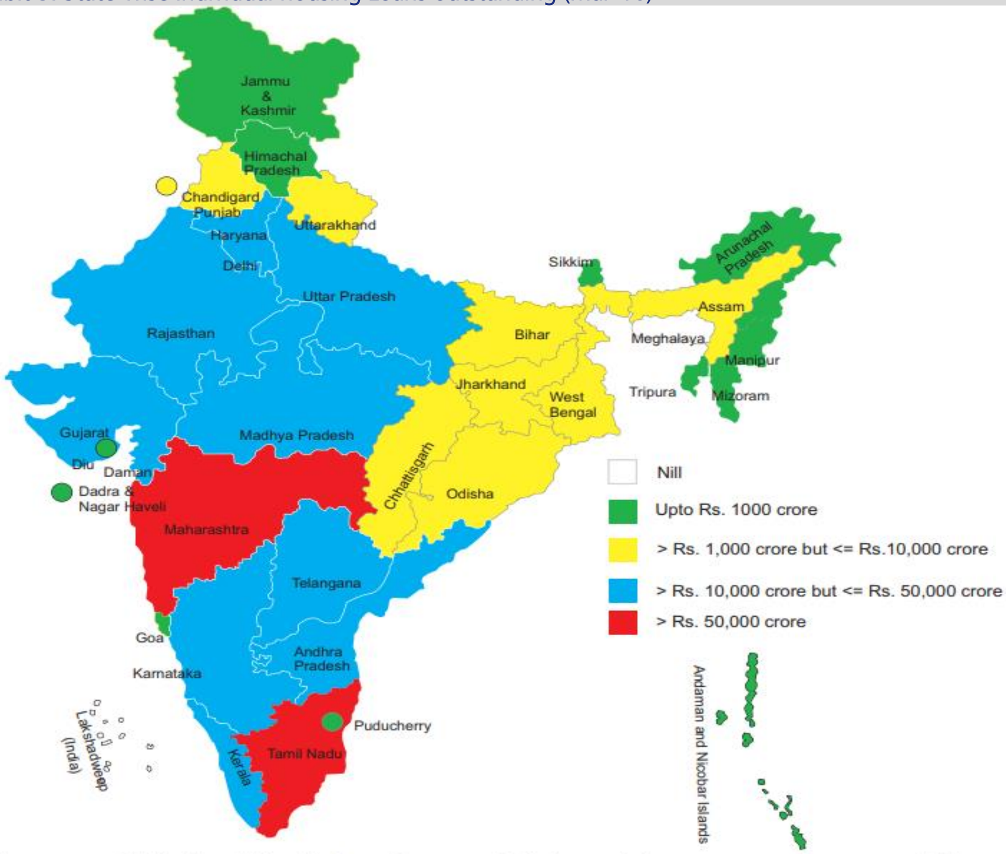
State	GRUH	Bandhan (incl. DSCs)	Total
West Bengal	2	1,286	1,288
Bihar	1	451	452
Assam	0	418	418
Uttar Pradesh	5	328	333
Maharashtra	51	206	257
Madhya Pradesh	33	201	234
Gujarat	48	121	169
Odisha	0	158	158
Rajasthan	13	99	112
Tripura	0	112	112
Jharkhand	1	109	110
Karnataka	17	76	93
Chhattisgarh	12	76	88
Others	12	309	321
Total	195	3,950	4,145

Source: Company, JM Financial

Penetration in the Eastern and North-eastern housing finance market

According to NHB data (dated as of FY16), the Eastern and North-eastern regions rank among the lowest in terms of the total individual housing loans outstanding. These states have very little HFC presence, and the banks of the region have been riddled with asset quality and capital adequacy woes (PCA banks like UCO, Allahabad, United Bank etc.)

Exhibit 5. State-wise Individual housing Loans outstanding (Mar-16)



Source: NHB

Not only is the amount of housing loans outstanding among the lowest for the eastern and north-eastern states, 2 of these states (WB , Bihar) also rank among the top 5 most populous states in India. This implies that the housing loan penetration per-capita is among the lowest for WB and Bihar.

Exhibit 6. Top 5 most populous states in India (Census 2011) – the 2 highlighted states account for c.44% of Bandhan's branch and DSC network

S. no.	State	Population (INR mn)
1	Uttar Pradesh	199.8
2	Maharashtra	112.4
3	Bihar	104.1
4	West Bengal	91.3
5	Andhra Pradesh	84.6

Source: Census 2011, JM Financial

The 2 states of West Bengal and Bihar account for c.44% of Bandhan's branch and DSC network. We believe the significantly underpenetrated housing finance markets of eastern and north-eastern India, offer immense opportunity for Bandhan to scale up Gruh's business in the region.

3. How can Bandhan scale up Gruh's business in its own geographies?

Although Gruh and Bandhan's loan books are largely complementary (west vs. east, secured vs. unsecured), we believe there is a substantial overlap in terms of their target customer segments (on an economic basis). Specifically, Bandhan's small enterprise loan (SEL) customer base could have a similar profile to Gruh's customers.

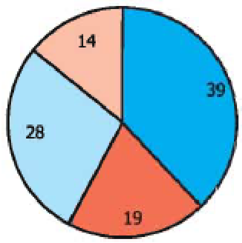
According to Gruh's FY18 annual report (as shown below), 58% of Gruh's loans disbursed till-date were below INR 0.5mn in ticket size. Also, 65% of Gruh's customers earn less than INR 25k per month.

Gruh has financed 0.42 mn customer properties till date, of which 50k (12%) were disbursed in FY18.

Exhibit 7. Gruh's customer profile – based on all loans disbursed till FY18 (Disbursement ticket sizes)

Properties Financed - Loan Amount Wise Distribution

Loan Amount (₹)	No.	%
Up to 3,00,000	1,62,488	39
> 3,00,000 to 5,00,000	81,830	19
> 5,00,000 to 10,00,000	1,17,647	28
> 10,00,000	60,966	14
	4,22,931	100

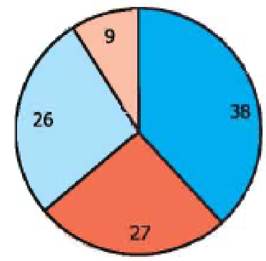


Source: Company

Exhibit 8. Gruh's customer profile – based on all loans disbursed till FY18 (Monthly family incomes)

Property Financed - Family Income Wise Distribution

Family Income (₹)	No.	%
Up to 15,000	1,61,327	38
> 15,000 to 25,000	1,13,641	27
> 25,000 to 50,000	1,09,178	26
> 50,000	38,785	9
	4,22,931	100



Source: Company

An analysis of Gruh's unit economics (below) with respect to disbursements shows that, on average Gruh disburses c.238 loans per branch at an average ticket size of c.INR 1mn. Moreover, the average repayment rate (i.e. repayments / opening loans) over the last 10 years has averaged at c.19% (with minimal variation across years).

Exhibit 9. Gruh's unit economics – On average Gruh has disbursed c.238 loans per branch with an average ticket size of c.INR 1mn

Gruh Finance	FY16	FY17	FY18	3-year average
No. of loans disbursed	40,084	42,525	50,164	44,258
Branches	179	185	194	186
No. of loans disbursed per branch	**224**	**230**	**259**	**238**
Total disbursements (INR mn)	38,566	41,253	52,590	44,136
Disbursement per loan (INR)	**9,62,125**	**9,70,083**	**10,48,361**	**9,97,255**

Source: Company, JM Financial

We believe Bandhan's SEL customers have a similar economic background as the lower end of Gruh's customer base. Bandhan's SEL loans are unsecured loans for income generating activities. These are in the form of working capital loans or short-term business loans. Small enterprise loans may vary from INR 0.1mn to INR 1mn in ticket size and have loan tenures from 1 to 3 years.

The SEL product was launched by Bandhan in FY17, following its conversion to a commercial bank. By the end of FY18, (within 21 months of launch) Bandhan had a loan book outstanding of INR 16.4bn from c.86k customers.

Exhibit 10. Bandhan's small enterprise loans (SEL) portfolio

Bandhan's SEL portfolio - Key parameters	FY17	FY18
Bandhan's SEL portfolio (INR mn)	10,545	16,390
Growth %		55%
No. of customers		86,089
Disbursement ticket sizes		INR 0.1mn to 1mn
Tenure		1 - 3 yrs
No. of credit centres		137

Source: Company, JM Financial

Can Bandhan scale up Gruh's business through its SEL branches?

In our mock-up below, we analyse how Bandhan can scale up Gruh's lending business through its own SEL centres. Bandhan had 137 centres (as of FY18) to disburse SEL loans. As SEL loans cater to a roughly similar economic segment as that for Gruh's housing loans (discussed above), we believe that it may be possible for Bandhan to scale up this business relatively quickly through its SEL centres.

We have assumed comparatively lower housing loan disbursement ticket sizes for Bandhan from its SEL branches. Disbursement ticket sizes are assumed at INR 500k-600k (compared to c. INR1mn for Gruh). This is because Bandhan's customer segment in SEL primarily caters to the lower end of Gruh's customer base (purely on economic criteria, as discussed above).

On the flip side, we have assumed higher number of loan disbursements per centre – going up to 350 per centre by FY25E (as opposed to c.238 per centre disbursed by Gruh on average over past 3 years). We believe Bandhan's ability to scale up faster, while maintaining asset quality, as well as the size and under-penetration of the eastern market could warrant such an assumption. Also, repayment rates (ie. repayment as a percentage of opening loans) have been assumed to be largely similar to that observed by Gruh in its business over the past 10 years (largely stable with minimal variations).

Exhibit 11. How Bandhan can scale up Gruh's business in the East through its own SEL centres

	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E
Opening loans o/s (INR mn)		-	15,000	34,010	57,514	87,029	1,19,156
Disbursements (INR mn)		15,000	21,875	30,000	40,500	48,750	57,750
Repayments (INR mn)		-	2,865	6,496	10,985	16,623	22,759
Loan book o/s (INR mn)	**0**	**15,000**	**34,010**	**57,514**	**87,029**	**1,19,156**	**1,54,148**
Loan Growth %			127%	69%	51%	37%	29%
Disbursement growth %			46%	37%	35%	20%	18%
No. of centres	137*	150	175	200	225	250	275
No. of loans disbursed per centre		200	250	300	300	325	350
Average ticket size of disbursement (INR)		5,00,000	5,00,000	5,00,000	6,00,000	6,00,000	6,00,000
Repayment as % opening loans	19.1%	(Avg. seen by Gruh in last 10 years)					

Source: Company, JM Financial *Assumed Bandhan's SEL centres are used to disburse housing loans

Based on our workings Bandhan could scale up the housing loan business in the Eastern market to **c.INR 154bn by FY25E** (implying a CAGR of c.59% over FY20-25E).

Separately, Bandhan can also replicate Gruh's business model in its own geographies by deploying, for example, a mortgage field officer to each of its c.4000+ touchpoints (branches + DSCs). Currently, Gruh averages 3.5 employees per branch in its existing network. This could enable Bandhan to scale up Gruh's business in its own geographies.

4. How much can extra PSLC income contribute?

Both Bandhan and Gruh have almost completely priority sector lending (PSL) compliant loan portfolios. While Bandhan's loan book is c.96% PSL compliant, Gruh's entire loan book (ex-developer book) is PSL compliant. As a result, the merged entity will continue to hold excess PSL compliant loans which could be used to generate higher PSLC income.

Exhibit 12. Extra PSLC income to accrue from Gruh's PSL compliant loan book

Extra income from PSLCs	INR bn
Bandhan PSL compliant loan book (96%) (1HFY19)	305
Gruh PSL compliant loan book (95%) (1HFY19)	159
PSL requirement of merged entity (@40% of combined loan book)	**194**
Extra loans available for PSLC sales	270
PSLC sales (based on 1.25% avg. yield)	3.37
Bandhan (standalone) PSLC income FY19	2.77
Potential extra income accrued (based on 1HFY19 numbers)	0.60

Source: Company, JM Financial

Based on our estimates (using 1HFY19 pro-forma numbers), the merged entity could generate INR 3.4bn in PSLC fees, as opposed to INR 2.8bn to be booked by Bandhan in FY19E. Hence, by our estimates an extra income of c.INR 600mn could accrue to the merged entity from the merger (based on 1HFY19 numbers).

5. What do the operating metrics for the merged entity look like?

Below, we look at what some of the metrics for the merged entity could look like:

A) NIMs:

The merged entity could have NIMs of c.8.5% (pro-forma based on 1HFY19 reported numbers). However, in the calculation below we have not considered i) the (negative) impact of CRR / SLR requirements against Gruh's borrowings and ii) the (positive) impact of refinancing Gruh's borrowings at Bandhan's lower CoF. This is discussed in the sections that follow.

Exhibit 13. NIM for merged entity (without considering CRR / SLR negative carry and lower CoF on merging Gruh into the bank) – (A)

Bandhan NIM (1HFY19)	10.3%
Gruh NIM (1HFY19)	4.1%
Blended NIM (without CRR / SLR impact or lower CoF)	8.5%

Source: Company, JM Financial

i) Impact on NIMs due to CRR /SLR requirement

As shown below, incremental CRR / SLR to be held against Gruh's borrowings (assuming it to be replaced by deposits) will have a negative impact of ~35bps on the blended NIMs.

Exhibit 14. NIM for merged entity after considering impact of negative carry on CRR / SLR (B)

Impact of CRR / SLR on NIM	
Total borrowings of Gruh (INR mn) (1HFY19)	1,66,434
SLR requirement	19.25%
CRR requirement	4.00%
SLR to be held (INR mn)	32,039
Yield on Gsecs	7.3%
Yield differential (between SLR and blended yield of merged entity)	8.0%
CRR to be held (INR mn)	6,657
Yield on CRR	0%
Yield differential (between CRR and blended yield of merged entity)	15.3%
Total cash already on books of Gruh (INR mn)	14,380
Net impact on P&L (INR mn)	1,956
Impact on NIM	-0.34%
Blended NIM (after impact of CRR / SLR)	8.15%

Source: Company, JM Financial

Bandhan currently holds c.33% SLR – well above the regulatory requirement of 19.25%. Moreover, Gruh also holds c.15% of its assets in liquid funds and bank deposits. As a result, we do not expect substantial incremental impact of CRR / SLR on NIMs.

We expect the negative impact on NIMs due to CRR / SLR to be sufficiently offset by a) refinancing of Gruh's borrowings at Bandhan's lower CoF and b) Positive impact from PSLC sales from Gruh's loans.

ii) Impact on NIMs on refinancing Gruh's borrowings at Bandhan's lower CoF

If Bandhan were to refinance Gruh's borrowings at Bandhan's CoF (1.2% lower as of 1HFY19), the negative carry on CRR / SLR would be almost completely offset. Pro-forma calculations are tabulated below:

Exhibit 15. NIM for merged entity after considering both a) CRR / SLR impact and b) lower CoF on merging Gruh into the bank

Impact of lower cost of funds on NIM	
Delta between Gruh and Bandhan CoF (based on 1HFY19 data)	1.2%
Total borrowings of Gruh (INR mn) (1HFY19)	1,66,434
P&L impact of refinancing at Bandhan CoF	1,997
Impact on NIM	0.34%
Blended NIM after taking impact of lower CoF and CRR/ SLR impact	8.5%

Source: Company, JM Financial

The difference in CoF between the 2 companies was around c.200 bps as of 3QFY19.

B) Opex ratios

Blended cost ratios for the merged entity will decline as Gruh is a cost leader in its space, just like Bandhan. In fact, Gruh runs a far tighter ship than even Bandhan, with cost to income at c.16% in 1HFY19.

Exhibit 16. Blended cost metrics for the merged entity

Bandhan - Cost to assets (1HFY19)	3.8%
Gruh - Cost to assets (1HFY19)	0.8%
Blended - cost to assets (1HFY19)	**3.0%**
Bandhan - Cost to income (1HFY19)	33.7%
Gruh - Cost to income (1HFY19)	15.9%
Blended - Cost to income (1HFY19)	**31.4%**

Source: Company, JM Financial

C) Credit cost

Similarly credit cost for the merged entity is also expected to decline. Gruh's completely secured loan book results in significantly lower credit costs.

Exhibit 17. Blended credit cost for the merged entity to be lower

Credit cost - Bandhan (1HFY19)	0.94%
Credit cost - Gruh (1HFY19)	0.15%
Credit cost - Blended (1HFY19)	**0.68%**

Source: Company, JM Financial

6. What do the merged return metrics look like?

The merger is BVPS and EPS dilutive to Bandhan, as Gruh traded at a significant premium to Bandhan on both P/E and P/BV basis. Below, we summarise the impact to Bandhan's return metrics as a result of the merger.

Exhibit 18. Return metrics of the merged entity

	Bandhan (pre-merger)		GRUH (pre-merger)		Merged Bandhan		
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY21E
EPS	15.5	24.3	5.9	7.1	15.5	21.2	27.4
BVPS	93.1	116.2	23.0	28.0	93.1	99.5	125.7
RoA	3.5%	3.9%	2.4%	2.4%	3.5%	3.6%	3.6%
RoE	18.0%	23.2%	28.1%	28.0%	18.0%	23.7%	24.3%

Source: Company, JM Financial

As seen above, the merger results in an EPS / BVPS dilution of 13% / 14% to Bandhan shareholders. However, even though the merged entity has lower RoAs than our estimates for Bandhan standalone (FY20E), we see that RoEs are, in fact, slightly higher. RoEs for the merged entity are bumped up by Gruh's significantly higher leverage. Gruh's leverage was at 11x as of 1HFY19, as compared to 4.5x for Bandhan.

Exhibit 19. Dupont analysis : Our Bandhan standalone estimates vs merged Bandhan estimates

	Bandhan (standalone)			Bandhan (merged)*		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
NII / Assets (%)	8.2%	8.4%	8.0%	8.2%	7.4%	7.2%
Core other income / Assets (%)	1.6%	1.5%	1.4%	1.6%	1.2%	1.2%
Other income / Assets (%)	1.7%	1.6%	1.4%	1.7%	1.3%	1.3%
Total Income / Assets (%)	10.0%	9.9%	9.5%	10.0%	8.7%	8.5%
Employee Cost to Assets (%)	1.8%	1.6%	1.4%	1.8%	1.3%	1.2%
Other Cost to Assets (%)	1.6%	1.5%	1.4%	1.6%	1.2%	1.2%
Cost to Assets (%)	3.3%	3.1%	2.9%	3.3%	2.6%	2.4%
PPP / Assets (%)	6.6%	6.8%	6.6%	6.6%	6.1%	6.1%
Provisions / Assets (%)	1.3%	0.8%	0.8%	1.3%	0.7%	0.7%
PBT / Assets (%)	5.3%	6.0%	5.8%	5.3%	5.5%	5.4%
ROA (%)	3.5%	3.9%	3.8%	3.5%	3.6%	3.6%

Source: Company, JM Financial * We have merged Bandhan with Gruh from FY20E onwards

Valuation and TP:

We value the merged entity using a 2-stage Gordon Growth model, with assumptions as shown below. We revise our TP to INR 600, valuing the merged entity at 4.8 x FY21E BVPS (22x FY21E EPS).

Exhibit 20. Bandhan Bank : Valuation and TP

Initial no of years	10
Growth rate for the first 10 years (%)	19.5%
Pay out ratio for the first 10 years (%)	20.0%
Perpetual growth rate (%)	4.0%
Perpetual payout ratio (%)	85.0%
K1	2.68
K2	15.44
FY21E BVPS (Rs)	125.7
Target P / Fully Adj BV (x)	4.8x
Fair value (rounded off)	**600**

Source: Company, JM Financial

Financial Tables (Pro-forma merged with Gruh from FY20E onwards)

Profit & Loss					(INR mn)
Y/E March	FY17A	FY18A	FY19E	FY20E	FY21E
Net Interest Income	24,035	30,322	43,885	70,380	88,912
Profit on Investments	217	463	463	463	463
Exchange Income	0	0	0	0	0
Fee & Other Income	3,897	6,598	8,757	11,825	15,322
Non-Interest Income	**4,114**	**7,062**	**9,220**	**12,289**	**15,785**
Total Income	**28,149**	**37,384**	**53,105**	**82,668**	**1,04,697**
Operating Expenses	10,220	13,083	17,783	24,367	30,017
Pre-provisioning Profits	**17,929**	**24,301**	**35,322**	**58,302**	**74,679**
Loan-Loss Provisions	802	3,331	7,442	5,823	7,970
Provisions on Investments	19	451	-300	0	0
Others Provisions	64	-40	0	400	100
Total Provisions	**884**	**3,742**	**7,142**	**6,223**	**8,070**
PBT	**17,045**	**20,559**	**28,179**	**52,079**	**66,609**
Tax	5,925	7,103	9,736	17,994	22,515
PAT (Pre-Extraordinaries)	**11,119**	**13,456**	**18,443**	**34,085**	**44,094**
Extra ordinaries (Net of Tax)	0	0	0	0	0
Reported Profits	**11,119**	**13,456**	**18,443**	**34,085**	**44,094**
Dividend paid	0	0	1,193	1,930	2,010
Retained Profits	**11,119**	**13,456**	**17,250**	**32,155**	**42,084**

Source: Company, JM Financial

Balance Sheet					(INR mn)
Y/E March	FY17A	FY18A	FY19E	FY20E	FY21E
Equity Capital	10,951	11,928	11,928	16,082	16,082
Reserves & Surplus	33,513	81,891	99,142	1,43,966	1,86,050
Deposits	2,32,287	3,38,690	4,91,101	6,82,630	11,19,513
Borrowings	10,289	2,850	12,850	2,23,043	38,216
Other Liabilities	15,320	7,741	8,128	18,164	21,797
Total Liabilities	**3,02,361**	**4,43,101**	**6,23,148**	**10,83,885**	**13,81,658**
Investments	55,165	83,719	1,06,455	1,56,330	2,12,072
Net Advances	1,68,391	2,97,130	4,56,060	8,38,391	10,60,524
Cash & Equivalents	73,650	55,106	55,788	82,974	98,321
Fixed Assets	2,518	2,381	3,162	4,279	6,182
Other Assets	2,637	4,764	1,683	1,911	4,560
Total Assets	**3,02,361**	**4,43,101**	**6,23,148**	**10,83,885**	**13,81,658**

Source: Company, JM Financial

Key Ratios					
Y/E March	FY17A	FY18A	FY19E	FY20E	FY21E
Growth (YoY) (%)					
Deposits	92.2%	45.8%	45.0%	39.0%	64.0%
Advances	35.4%	76.5%	53.5%	83.8%	26.5%
Total Assets	53.0%	46.5%	40.6%	73.9%	27.5%
NII	157.7%	26.2%	44.7%	60.4%	26.3%
Non-interest Income	174.5%	71.6%	30.6%	33.3%	28.5%
Operating Expenses	65.9%	28.0%	35.9%	37.0%	23.2%
Operating Profits	284.1%	35.5%	45.4%	65.1%	28.1%
Core Operating profit	281.1%	34.6%	46.2%	65.9%	28.3%
Provisions	65.9%	323.1%	90.9%	-12.9%	29.7%
Reported PAT	304.0%	21.0%	37.1%	84.8%	29.4%
Yields / Margins (%)					
Interest Spread	8.28%	7.04%	7.11%	7.02%	6.28%
NIM	9.79%	8.27%	8.33%	8.30%	7.26%
Profitability (%)					
Non-IR to Income	14.6%	18.9%	17.4%	14.9%	15.1%
Cost to Income	36.3%	35.0%	33.5%	29.5%	28.7%
ROA	4.45%	3.61%	3.46%	3.58%	3.58%
ROE	28.6%	19.5%	18.0%	23.7%	24.3%
Assets Quality (%)					
Slippages	0.83%	2.10%	2.95%	1.10%	1.20%
Gross NPA	0.51%	1.25%	2.36%	1.40%	1.43%
Net NPAs	0.36%	0.58%	0.72%	0.41%	0.42%
Provision Coverage	29.1%	53.7%	70.0%	71.3%	71.0%
Specific LLP	0.33%	0.97%	1.60%	0.57%	0.63%
Net NPAs / Networth	1.4%	1.8%	3.0%	2.1%	2.2%
Capital Adequacy (%)					
Tier I	24.77%	30.30%	27.82%	24.27%	23.90%
CAR	26.36%	31.48%	28.73%	24.82%	24.73%

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY17A	FY18A	FY19E	FY20E	FY21E
NII / Assets	9.62%	8.14%	8.23%	7.40%	7.21%
Other Income / Assets	1.65%	1.89%	1.73%	1.29%	1.28%
Total Income / Assets	11.26%	10.03%	9.96%	8.69%	8.49%
Cost / Assets	4.09%	3.51%	3.34%	2.56%	2.43%
PBP / Assets	7.17%	6.52%	6.63%	6.13%	6.06%
Provisions / Assets	0.35%	1.00%	1.34%	0.65%	0.65%
PBT / Assets	6.82%	5.52%	5.29%	5.48%	5.40%
Tax rate	34.8%	34.6%	34.6%	34.6%	33.8%
ROA	4.45%	3.61%	3.46%	3.58%	3.58%
RoRWAs	7.49%	5.57%	5.28%	6.51%	5.91%
Leverage	6.8	4.7	5.6	6.8	6.8
ROE	28.6%	19.5%	18.0%	23.7%	24.3%

Source: Company, JM Financial

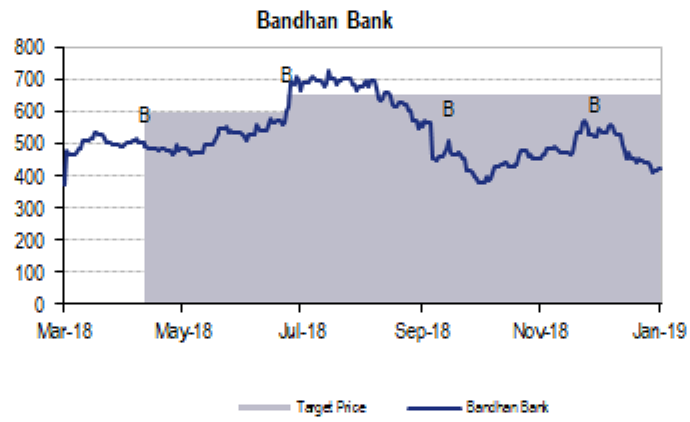
Valuations					
Y/E March	FY17A	FY18A	FY19E	FY20E	FY21E
Shares in Issue	1,095.1	1,192.8	1,192.8	1,608.2	1,608.2
EPS (INR)	10.2	11.3	15.5	21.2	27.4
EPS (YoY) (%)	304.0%	11.1%	37.1%	37.1%	29.4%
PER (x)	39.9	35.9	26.2	19.1	14.8
BV (INR)	41	79	93	100	126
BV (YoY) (%)	33.3%	93.7%	18.4%	6.9%	26.3%
ABV (INR)	40	78	93	100	126
ABV (YoY) (%)	32.5%	94.0%	19.2%	7.0%	26.3%
P/BV (x)	9.97	5.15	4.35	4.07	3.22
P/ABV (x)	10.05	5.18	4.35	4.07	3.22
DPS (INR)	0.0	0.0	1.0	1.2	1.3
Div. yield (%)	0.0%	0.0%	0.2%	0.3%	0.3%

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	Recommendation	Target Price	% Chg.
7-May-18	Buy	595	
19-Jul-18	Buy	650	9.2
10-Oct-18	Buy	650	0.0
24-Dec-18	Buy	650	0.0

Recommendation History



APPENDIX I

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