NIRMAL BANG
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Institutional Equities

Bandhan Bank

18 December 2020

Reuters: BANH.BO; Bloomberg: BANDHAN IN

Initiating Coverage

High earnings visibility on back of continued MFI dominance

We initiate coverage on Bandhan Bank with a BUY rating and fair value estimate of Rs490 based on 3.5x 1HFY23E ABV. Bandhan Bank enjoys a dominant position in the Indian micro-finance industry. Having maintained 20% market share over the last 4 years, we believe that Bandhan Bank is strongly positioned to gain in an industry which is expected to grow at 15% CAGR over FY21-26E. Bandhan Bank's loans have grown at a 30% CAGR over FY17-20, backed by very high-quality and granular growth in deposits. While micro-finance is expected to continue on the strong growth trajectory for the bank, we expect non-micro-finance segments to grow at a higher rate given the management's vision 2025. We also expect Bandhan Bank to gain deposit market share, especially in West Bengal given that it offers relatively higher rate than frontline banks. The higher-rate strategy, even if it continues for longer, is not concerning as the high margins on the asset side shall be able to accommodate it. The bank has done a commendable job in terms of improving the opex ratios. – cost/income ratio has improved from 36.3% (FY17) to 30.8% (FY20). We are building in a cost/income ratio of 32% over FY22-23E. Given that micro-finance collections are now inching towards normalcy and in absence of any large-ticket/corporate NPAs or state-specific agitations (such as in Assam), we believe that the bank's balance sheet is sufficiently provided for in terms of addressing the asset quality impact due to Covid-19. We expect credit cost to start moderating FY22E onwards, which will be a major driver of ROE improvement. Overall, we expect the bank to deliver an ROE of 18.6-22.9% over FY21-23E. In our view, Bandhan Bank is one of the few banks which provide a high degree of overall growth and earnings visibility. This comfort comes partially from the bank's track record and its performance vis-à-vis peers. What strongly adds to our 'visibility' thesis is the specialized nature of the business i.e., micro-finance where the bank commands 20% market share.

Market dominance to continue: Bandhan Bank has maintained its Microfinance industry market share at 20% in last few years. Given the industry growth opportunity (15% CAGR FY21-26E) coupled with superior execution capability (as demonstrated so far), we expect Bandhan Bank to improve upon its market share (23.6% by FY25E).

Non-MFI to grow at a higher rate: Under the vision 2025, the non-MFI segments (housing, SME, personal/retail) are expected to see higher growth. Over FY20-23E, we expect Bandhan Bank's micro-finance portfolio to grow at ~21% CAGR, led by improving penetration in east/north-east India. Untapped states of West Bengal, Jharkhand and UP are expected to provide impetus for housing finance growth. We expect the non-micro-finance portfolio to grow at ~30% CAGR over FY20-23E.

Deposit scale up impressive; West Bengal market share to improve: The bank's deposits have grown at 35% CAGR over FY17-20. Compared to 71% as of FY17, retail deposits constituted ~78% of the total deposits as of 2QFY21. Over FY17-20, CASA deposits have grown at 45.4% CAGR and retail TDs have grown at 34.9% CAGR. We expect Bandhan Bank to gain further deposit market share in West Bengal given it currently holds only 3% (1QFY21) vis-a-vis ~70% held by PSBs despite Bandhan Bank offering higher rates.

Expect NIM to compress: Given that the share of micro-finance is expected to decline further, we expect blended NIM to compress. We expect 86bps compression in NIMs over FY20-23E.

Superior cost ratios: Over FY17-20, the C/I ratio has improved from 36.3% to 30.8%. Bandhan Bank's employee cost per head is about 50% lower and rent per banking outlet is 63% lower than the second-lowest bank in our coverage. Given the geographical spread of the business, majority of the workforce and banking outlets are based in east/north-east where wages and rents are generally lower than other parts of the country. We see scope for 17-18% improvement in micro-borrowers-per-DSC ratio.

Historical asset quality track record better than industry: During some of the recent events, which proved to be detrimental to the micro-finance industry's asset quality, Bandhan Bank's 90+ dpd numbers were 50-90% lower than the industry. Even in the current situation, Bandhan Bank has reported better-than-industry collections in the micro-finance portfolio. We expect credit cost to trend down FY22E onwards, which will be a major driver of ROE improvement.

Y/E March (Rsmn)	FY20	FY21E	FY22E	FY23E
NII	63,239	79,523	96,526	1,15,023
PPOP	54,466	67,240	79,459	94,525
PAT	30,237	30,568	43,138	54,828
Loans	6,66,299	7,85,272	9,54,764	11,71,101
RoA (%)	*3.9*	*3.0*	*3.5*	*3.7*
RoE (%)	*22.2*	*18.6*	*21.6*	*22.9*
P/ABV	2.2	3.8	3.2	2.7

Source: Company, Nirmal Bang Institutional Equities Research

BUY

Sector: Banks

CMP: Rs407

Target Price: Rs490

Upside: 20%

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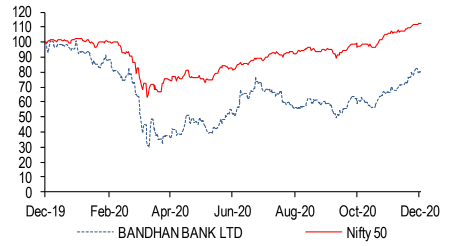
Key Data

Current Shares O/S (mn)	1,610.4
Mkt Cap (Rsbn/US$bn)	663.7/9.0
52 Wk H / L (Rs)	527/152
Daily Vol. (3M NSE Avg.)	11,207,660

Share holding (%)	4QFY20	1QFY21	2QFY21
Promoters	40.0	40.0	61.0
Public	60.0	60.0	39.0
Others	-	-	-

One Year Indexed Stock Performance



Price Performance (%)

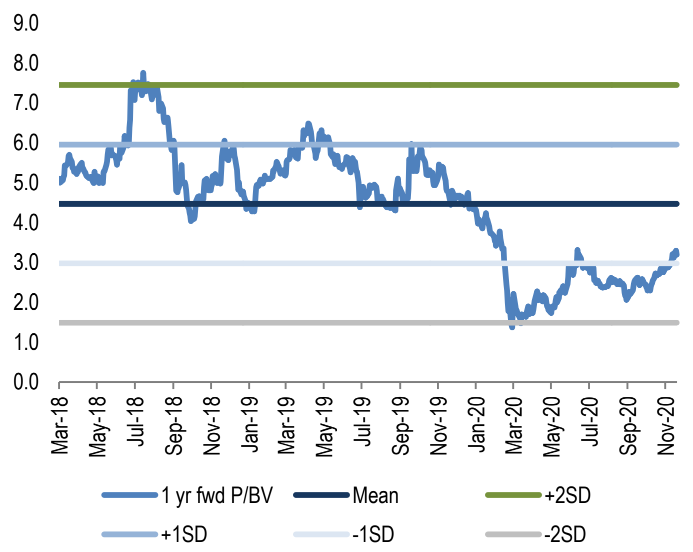
	1 M	6 M	1 Yr
Bandhan Bank.	20.0	53.8	(15.8)
Nifty Index	6.2	36.9	12.6

Source: Bloomberg

Outlook and valuation

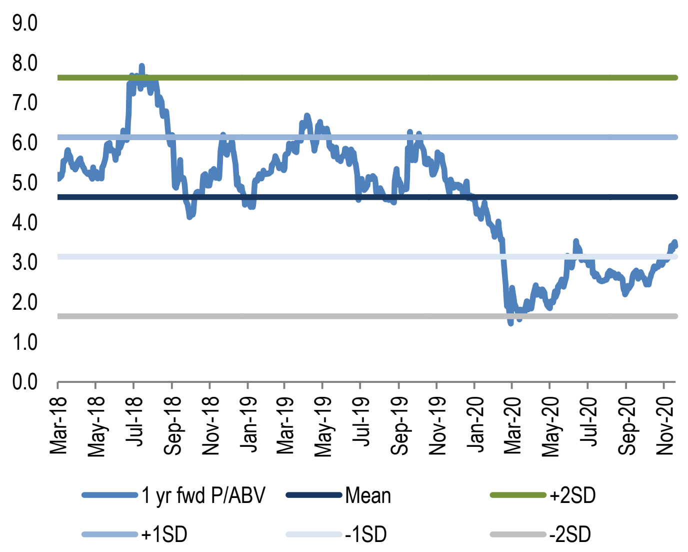
Bandhan Bank enjoys a dominant position in the Indian micro-finance industry. The bank has an overall industry market share of 20% (FY20) and a banking sector micro-finance market share of 50% (FY20). The bank has grown its loans at a CAGR of 30% over FY17-20, backed by very high-quality and granular growth in deposits. We expect industry-level micro-finance portfolio to grow at 15% CAGR over the next five years (FY21-26E) on the back of increasing target market penetration. We believe that the micro-finance industry has enormous room to grow. Having maintained 20% market share over the last 4 years, we believe that Bandhan Bank is strongly positioned to gain from this structural story. Post the GRUH merger, housing finance is also expected to contribute to overall growth strongly along with retail/personal and SME loans. While micro-finance is expected to continue on the strong growth trajectory for the bank, we expect the non-micro-finance segments to grow at a higher rate given the management's vision 2025. We expect overall advances to grow at ~21% CAGR over FY20-23E. The fact that public sector banks still hold ~70% of West Bengal's deposits provides huge opportunity for Bandhan Bank to gain further market share, which currently stands at 3%, especially given that the bank is offering higher deposit rates than most of the frontline large banks. The higher-rate strategy, even if it continues for longer, is not concerning given that the high-margins on the asset side shall be able to accommodate it. The bank has done a commendable job in terms of improving the opex ratios. Over FY17-20, the cost/income ratio has improved from 36.3% to 30.8%. As of 2QFY21, the cost/income ratio stood at 29.4%. A large part of the cost structure improvement has come through the non-staff line items. For instance, rent/income ratio has declined from 3.4% in FY17 to 2.5% in FY20. Rent per banking outlet for Bandhan Bank is 63% lower than the second-lowest bank in our coverage. In terms of the banking outlet infrastructure, Bandhan Bank's cost metrics are superior to peers. We also see scope for 17-18% improvement in micro-borrowers-per-DSC ratio, which currently stands at 3,063 as of 2QFY21. We are building in cost/income ratio of 32%. Given that micro-finance collections are now inching towards normalcy and in absence of any large-ticket/corporate NPAs or state-specific agitations (such as in Assam), we believe that the bank's balance sheet is sufficiently provided for in terms of addressing the asset quality impact due to Covid-19. We expect credit cost to trend downwards FY22E onwards, which will be a major driver of ROE improvement. Overall, we expect the bank to deliver an ROE of 18.6-22.9% over FY21-23E. In our view, Bandhan Bank is one of the few banks which provide a high degree of overall growth and earnings visibility. This comfort comes partially from the bank's track record and its performance vis-à-vis peers. What strongly adds to our 'visibility' thesis is the specialized nature of the business, i.e., micro-finance. The bank commands 20% market share in an industry where growth headroom is still plentiful as mentioned earlier. We value the stock at Rs490, based on 3.5x 1HFY23E ABV and initiate with a BUY rating.

Exhibit 1: P/BV (1-year forward)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: P/ABV (1-year forward)

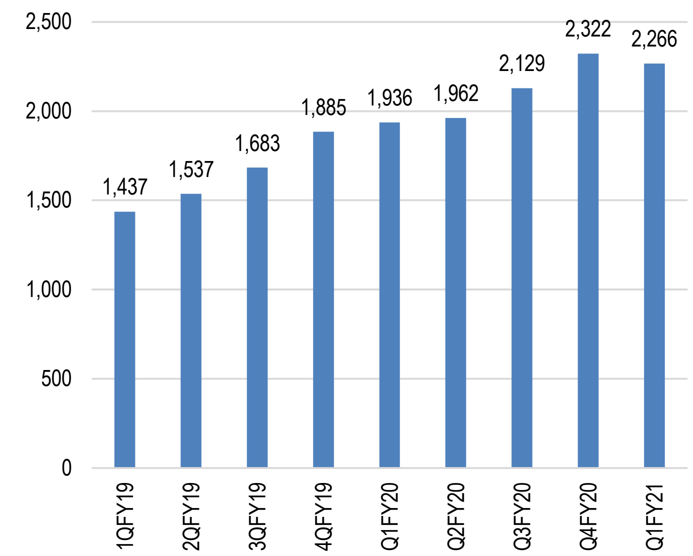


Source: Company, Nirmal Bang Institutional Equities Research

The micro-finance landscape – Bandhan is a dominant player

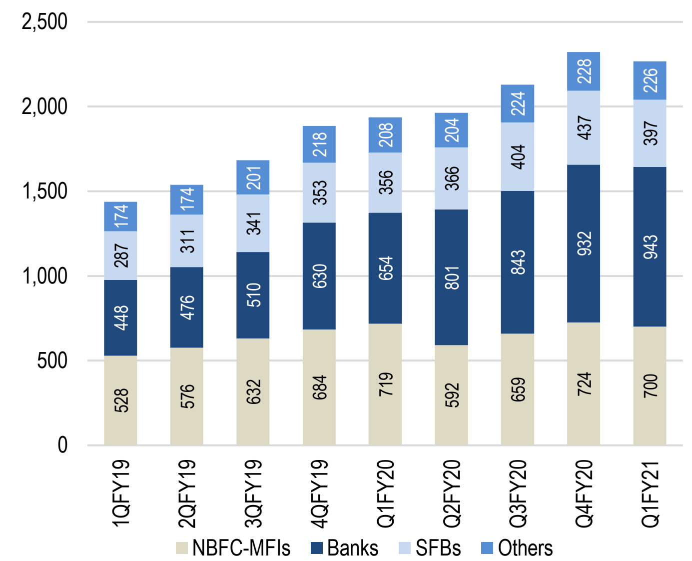
The total micro-finance portfolio in India stood at Rs2,322bn as of FY20, having grown at a 3-year CAGR of 30% (FY17-20). NBFC-MFIs account for 31.2% (Mar-20) of the total industry size while banks account for 40.2%. Banks' micro-finance portflio has grown at a CAGR of 42.4% over FY17-20 while NBFC-MFIs have grown at 31.2% over the same period (without adjusting for M&A). Bandhan Bank, which has the largest micro-finance portfolio (2QFY21: Rs498bn) has an overall industry market share of ~20% (FY20) and a banking sector micro-finance market share of 50% (FY20).

Exhibit 3: Total industry gross loans portfolio (Rsbn)



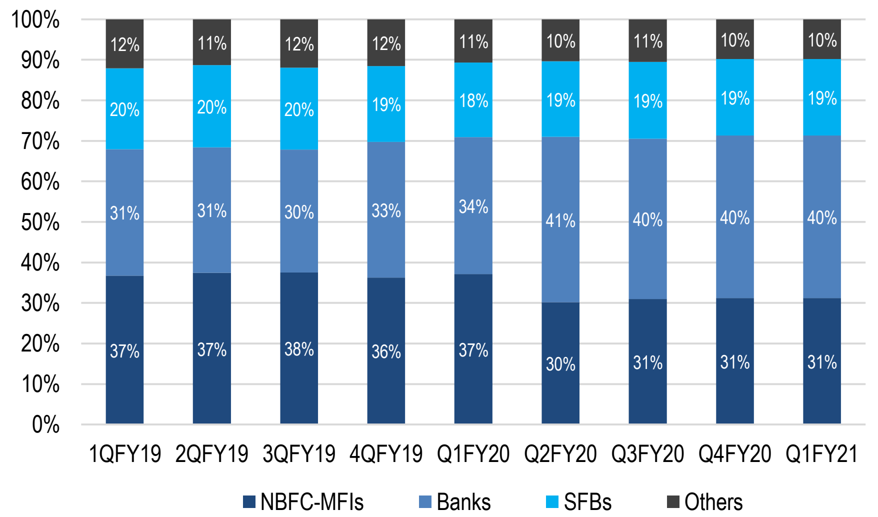
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 4: Industry gross loans portfolio mix (Rsbn)



Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 5: Industry gross loans portfolio mix (%)

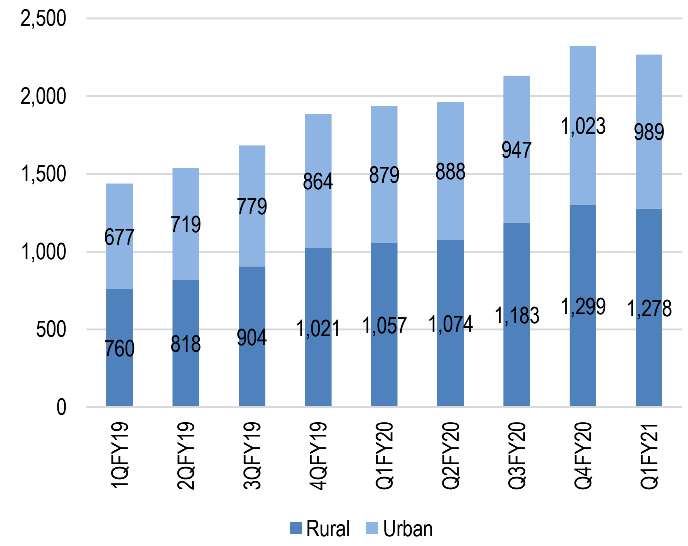


Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Rural orientation of the micro-finance industry has increased

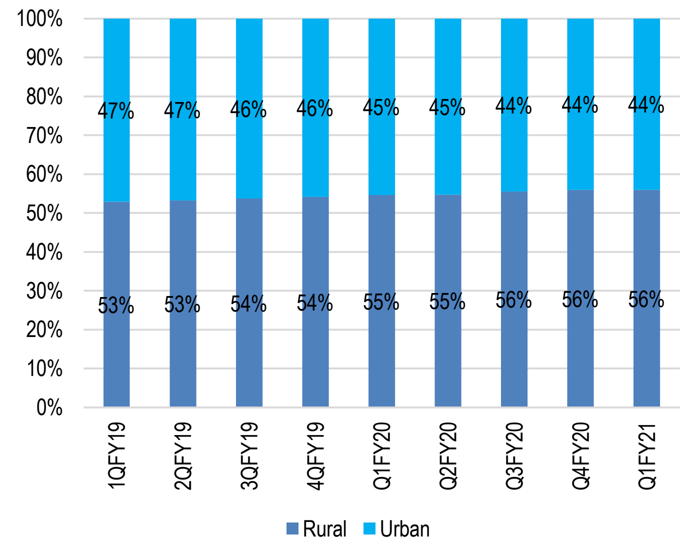
In terms of geographical segmentation, the rural micro-finance portfolio accounts for 56% (FY20) of the total industry compared to 49% in Mar-18. Tamil Nadu (TN) and West Bengal (WB) are the largest markets with a portfolio size of ~Rs330bn each (Mar-20). Micro-finance business is significantly concentrated, with top 10 states accounting for 83% of the total industry exposure. Over FY18-20, Tamil Nadu has witnessed the highest growth in average exposure (51%), exceeding ATS growth (27%), indicating increasing exposure per borrower. This is also supported by the fact that at 8.5%, Tamil Nadu has the highest share of customers borrowing from 4 or more lenders. For West Bengal, ATS stands at ~Rs44,500 (30% higher than national average) while average exposure stands at ~Rs46,360 (20% higher than national average). Despite higher exposure and ticket size per borrower, the percentage of customers having exposure to 4 or more lenders in WB is significantly lower at 1.3%. We estimate that Bandhan Bank has a customer market share of ~75% in WB.

Exhibit 6: Area-wise portfolio mix (Rsbn)



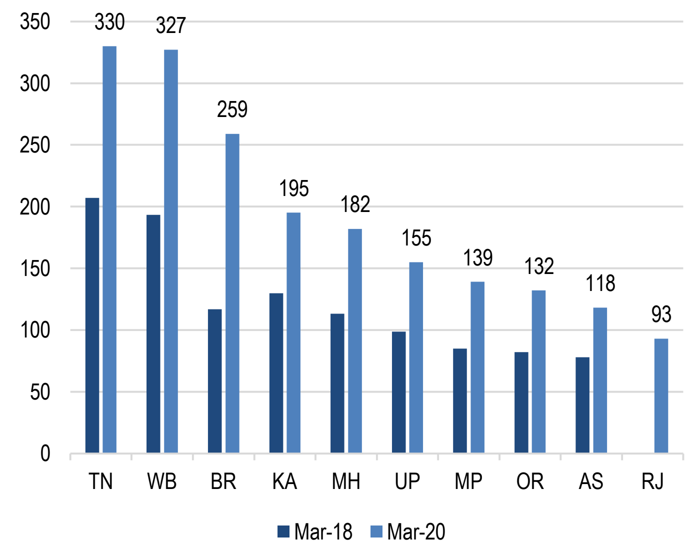
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 7: Geographical mix of the portfolio (%)



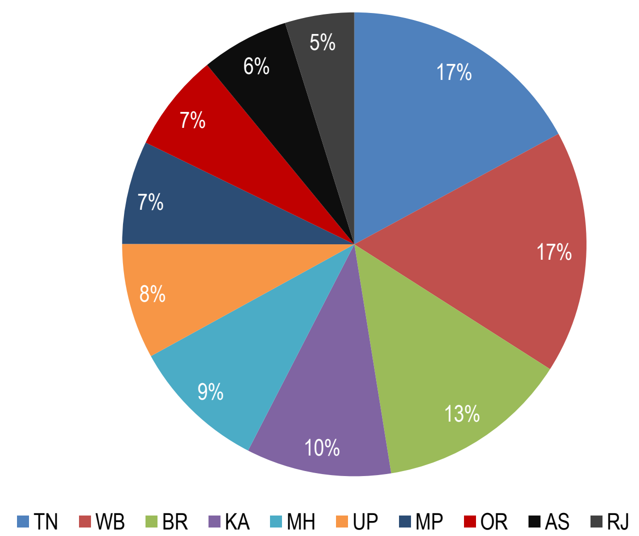
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 8: State-wise MFI exposure (Rsbn)



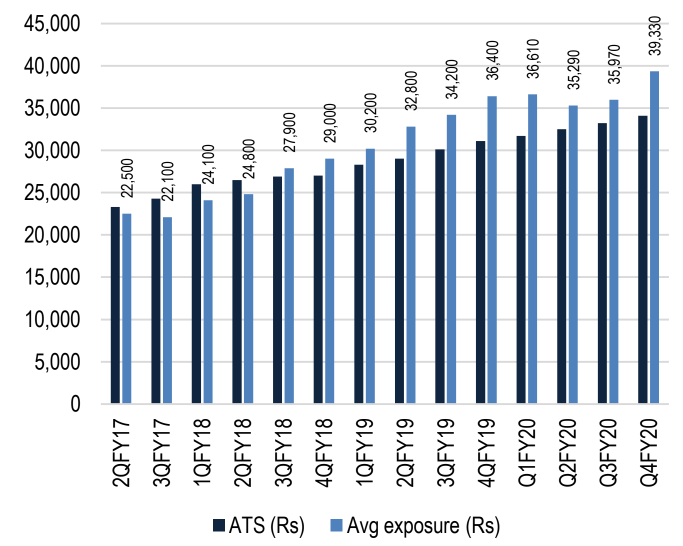
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 9: State-wise composition (%) (Mar-20)



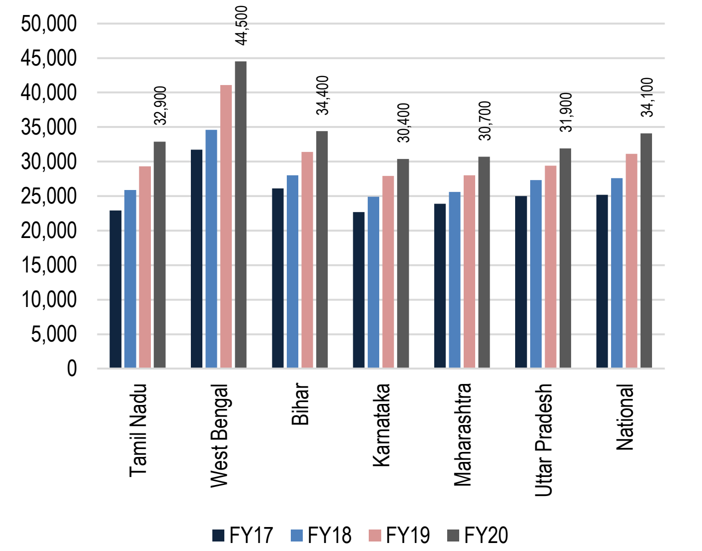
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 10: ATS and average exposure trends



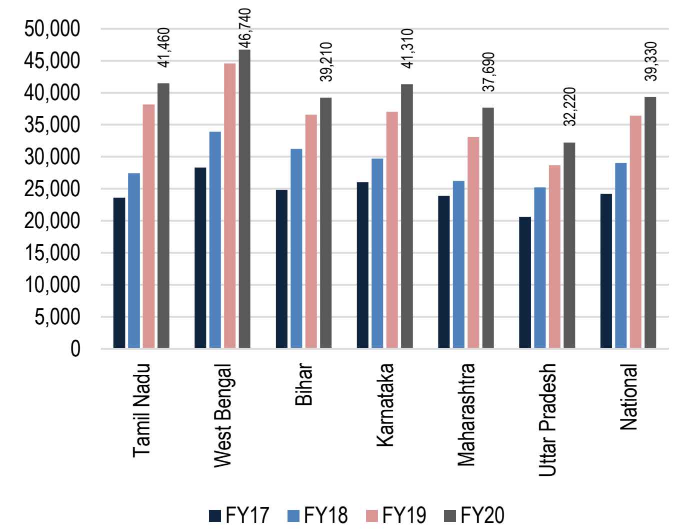
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 11: State-wise ATS (Rs)



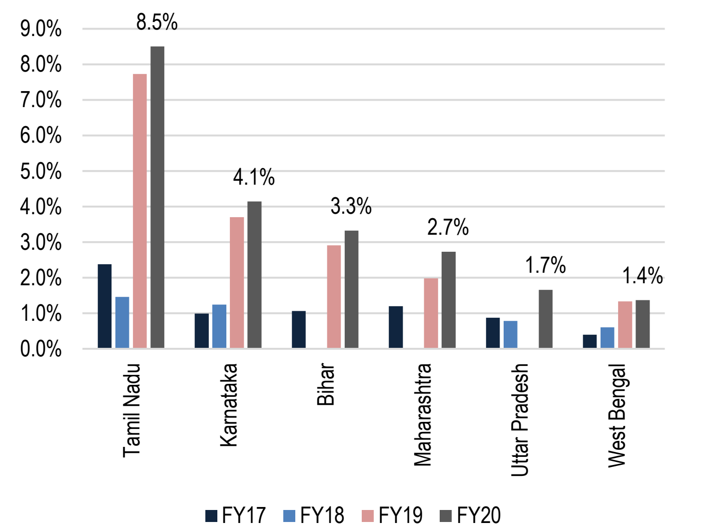
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 12: State-wise average exposure (Rs)



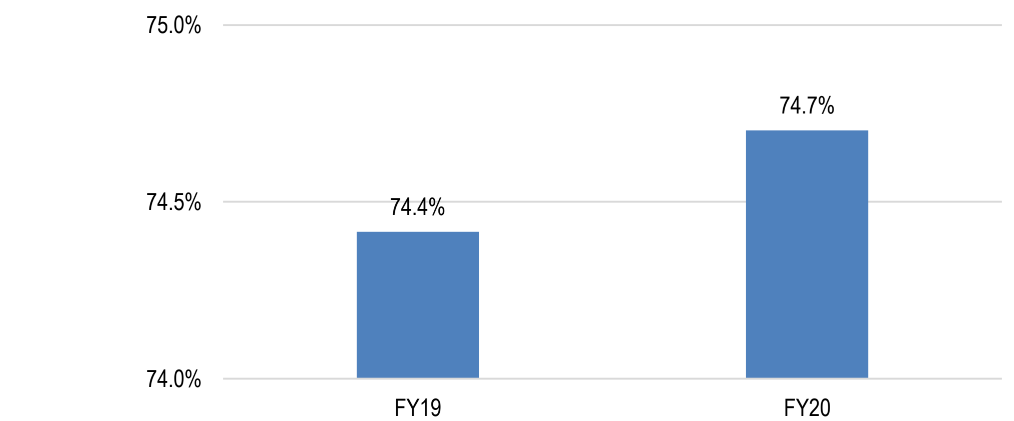
Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 13: Borrowers associated with 4 or more lenders (%)



Source: CRIF High Mark, Nirmal Bang Institutional Equities Research

Exhibit 14: Bandhan's customer market share in WB (%)*



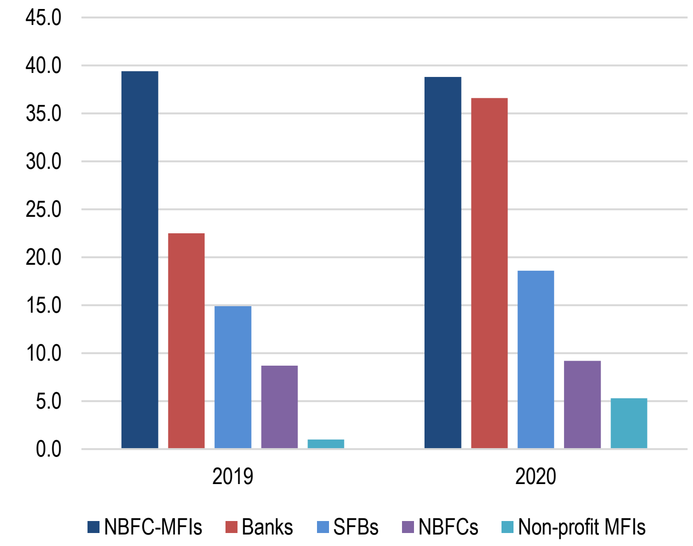
Source: Company, Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

*Bandhan's MFI customers in WB divided by unique number of MFI customers in WB.

Banks account for 18% of overall active micro-finance loans but 39% of the overall industry exposure

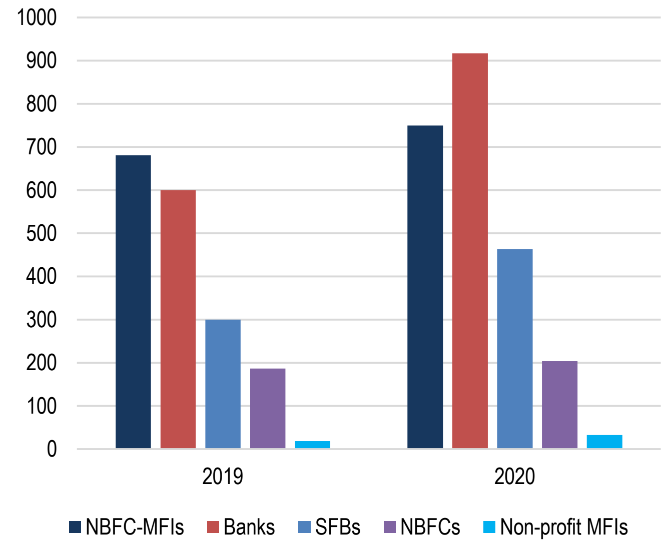
Average exposure per loan for banks is 30% higher than for NBFC-MFIs. Bandhan Bank has 50% share in the banking sector's micro-finance loan book.

Exhibit 15: No. of active loans (mn) (lender-type wise)



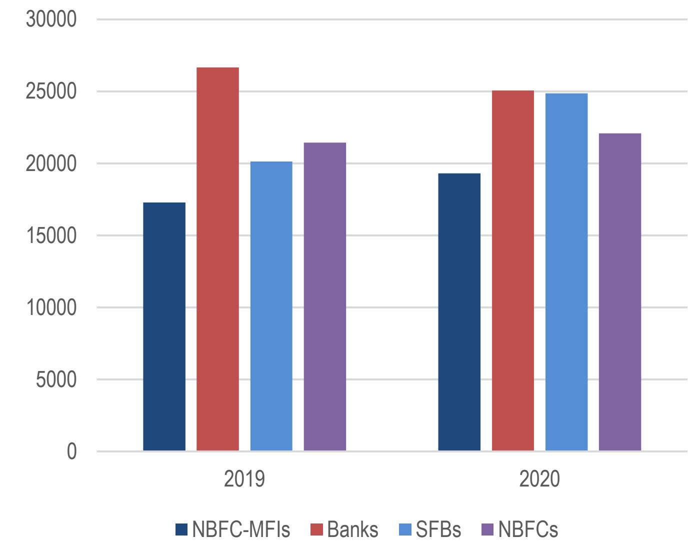
Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

Exhibit 16: Loans o/s (Rsbn) (lender-type wise)



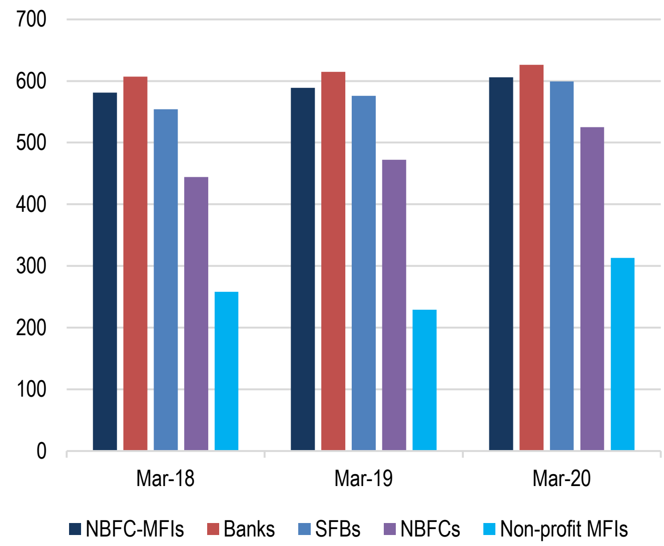
Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

Exhibit 17: Loan o/s per active loan (Rs) (lender-type wise)



Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

Exhibit 18: Lender wise number of districts covered



Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

Exhibit 19: Delinquency trends across states

30+ delinquency by value	FY20						FY19
States	**Industry**	**NBFC-MFIs**	**Banks**	**SFBs**	**NBFCs**	**NFPs**	**Industry**
Andhra Pradesh	0.53%	0.41%	2.66%	0.11%	0.47%	0.00%	0.69%
Arunachal Pradesh	1.32%	0.10%	6.22%	1.11%	NA	NA	2.65%
Assam	13.90%	21.21%	9.76%	15.43%	31.20%	NA	0.37%
Bihar	0.30%	0.30%	0.31%	0.31%	0.27%	0.02%	0.25%
Chandigarh	2.83%	0.85%	2.21%	0.28%	24.95%	NA	0.31%
Chhattisgarh	1.37%	1.18%	0.98%	1.80%	2.87%	0.27%	0.67%
Delhi	1.30%	1.98%	1.15%	1.08%	3.92%	NA	1.86%
Gujarat	1.64%	1.32%	1.56%	1.52%	2.98%	1.84%	1.20%
Haryana	0.75%	0.55%	0.61%	0.48%	2.98%	0.23%	0.87%
Himachal Pradesh	1.32%	0.59%	2.55%	0.08%	6.64%	0.00%	0.96%
Jammu & Kashmir	2.24%	0.65%	26.14%	0.00%	0.00%	NA	1.45%
Jharkhand	0.83%	0.79%	0.76%	0.58%	3.01%	0.01%	0.70%
Karnataka	3.16%	3.51%	3.45%	1.18%	4.07%	0.00%	0.63%
Kerala	1.28%	2.19%	1.41%	0.36%	2.16%	0.00%	2.20%
Madhya Pradesh	1.41%	1.24%	0.91%	1.73%	3.41%	1.43%	1.34%
Maharashtra	1.15%	0.93%	0.74%	1.98%	1.96%	1.05%	0.89%
Manipur	0.87%	0.11%	0.38%	8.70%	0.00%	NA	0.17%
Meghalaya	1.50%	2.06%	0.66%	3.27%	NA	NA	0.86%
Mizoram	1.19%	1.47%	0.55%	4.43%	NA	NA	0.27%
Nagaland	1.69%	0.01%	2.02%	0.03%	NA	0.00%	0.29%
Odisha	1.38%	1.21%	1.27%	1.44%	3.27%	0.00%	2.89%
Pondicherry	0.69%	1.23%	0.33%	0.48%	0.99%	0.00%	0.56%
Punjab	0.95%	0.39%	0.69%	0.55%	6.01%	0.00%	0.80%
Rajasthan	0.59%	0.61%	0.34%	0.58%	1.66%	0.01%	0.57%
Sikkim	2.70%	0.27%	2.73%	3.39%	NA	NA	1.71%
Tamil Nadu	1.19%	1.25%	0.56%	1.06%	2.04%	1.64%	1.51%
Telangana	0.54%	1.80%	0.31%	0.01%	1.09%	NA	1.86%
Tripura	0.85%	1.00%	0.66%	0.37%	8.62%	0.00%	0.28%
Uttar Pradesh	0.73%	0.84%	0.56%	0.69%	2.07%	0.12%	1.18%
Uttarakhand	0.98%	1.23%	0.57%	1.00%	2.79%	0.00%	2.16%
West Bengal	0.70%	0.80%	0.68%	0.68%	0.77%	0.23%	0.45%

Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

We estimate the micro-finance industry to grow at 15% CAGR over FY21-26E

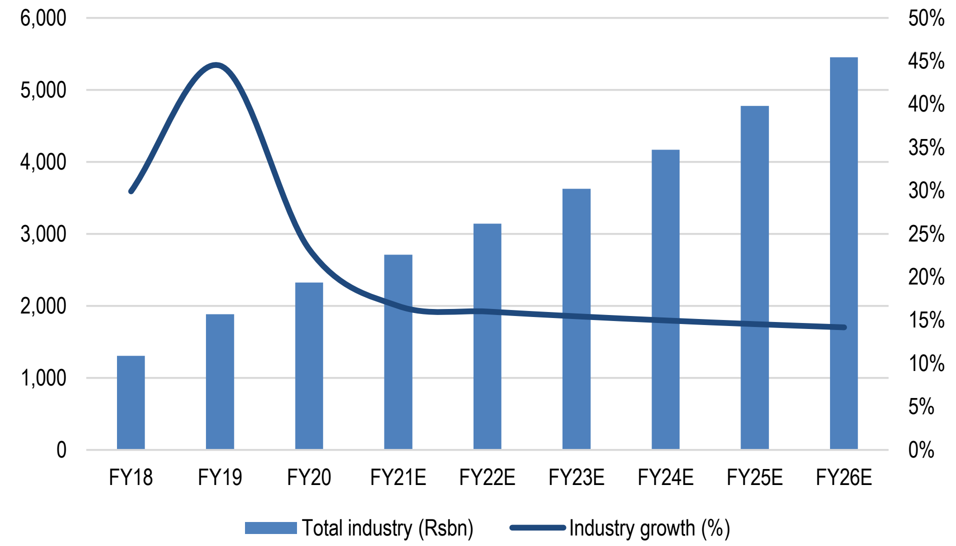
Based on our micro-finance demand-supply model, we estimate the industry-level portfolio to grow at 15% CAGR over the next 5 years (FY21-26E) to Rs5,452bn. Our projections assume target market penetration of 28% by FY26E and a CAGR of 8% over FY21-26E in exposure per borrower.

Exhibit 20: Demand forecast model

MFI demand forecast	FY19	FY20	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E
Urban target market (no. of households) (mn)	55.6	55.6	55.6	55.6	55.6	55.6	55.6	55.6
Rural target market (no. of households) (mn)	112.3	112.3	112.3	112.3	112.3	112.3	112.3	112.3
Total target market (no. of households) (mn)	167.9	167.9	167.9	167.9	167.9	167.9	167.9	167.9
No. of potential borrowers per household	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Total no. of target individuals (mn)	335.8	335.8	335.8	335.8	335.8	335.8	335.8	335.8
Live customer base (mn) (source: Crif)	56.0	63.0	68.0	73.1	78.1	83.1	88.2	93.2
Live customer base penetration (as % of target market)	17%	19%	20%	22%	23%	25%	26%	28%
Change in penetration (%)	-	2.1%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%
Exposure per borrower (Rs)	33,661	36,857	39,806	42,990	46,429	50,144	54,155	58,488
Growth p.a. in exposure per borrower (%)	-	9.5%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
GLP (Rsbn)	**1,885**	**2,322**	**2,708**	**3,141**	**3,627**	**4,169**	**4,776**	**5,452**
Growth in MFI GLP (%)	**-**	**23.2%**	**16.6%**	**16.0%**	**15.4%**	**15.0%**	**14.5%**	**14.2%**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 21: Industry micro-finance portfolio growth forecast

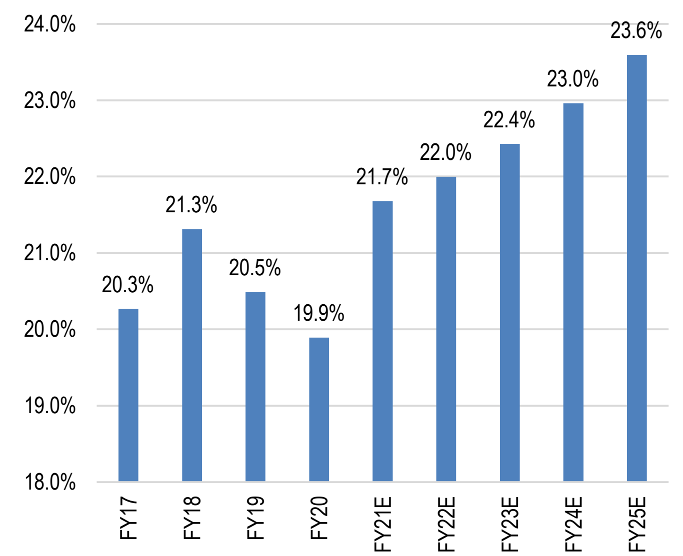


Source: Nirmal Bang Institutional Equities Research

Bandhan Bank – the micro-finance behemoth

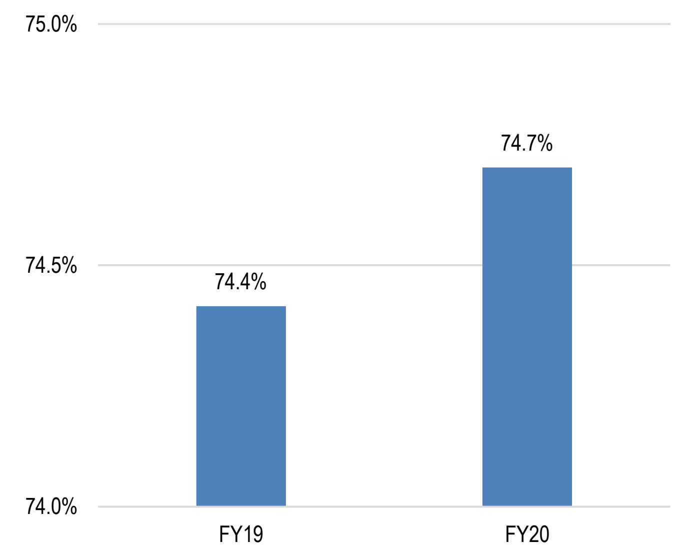
Bandhan Bank has the largest micro-finance portfolio in the country with a total loan book of Rs498bn as of 2QFY21. Over FY17-20, the bank has maintained its micro-finance loan book market share at an average of 20%. Over FY16-20, the bank's micro-finance book has grown at a CAGR of 31.5%, driven by 15% CAGR in active micro-borrower base and 14.3% CAGR in exposure size (per customer). Based on our demand model, we estimate industry loan book to grow at 15% CAGR over FY21-26E; we estimate an industry loan book size of Rs5,452bn by FY26E. Given Bandhan Bank's market positioning, we expect it to grow at above the industry rate. We are modelling (1) active micro-borrower base growth of 10-13% per annum (p.a.) over FY21-23E and (2) exposure size growth 7-12% over FY21-23E. Overall, we expect Bandhan Bank's micro-finance book to grow at a CAGR of 20.8% over FY20-23E.

Exhibit 22: Bandhan Bank – micro-finance market share (%)



Source: Company, Nirmal Bang Institutional Equities Research

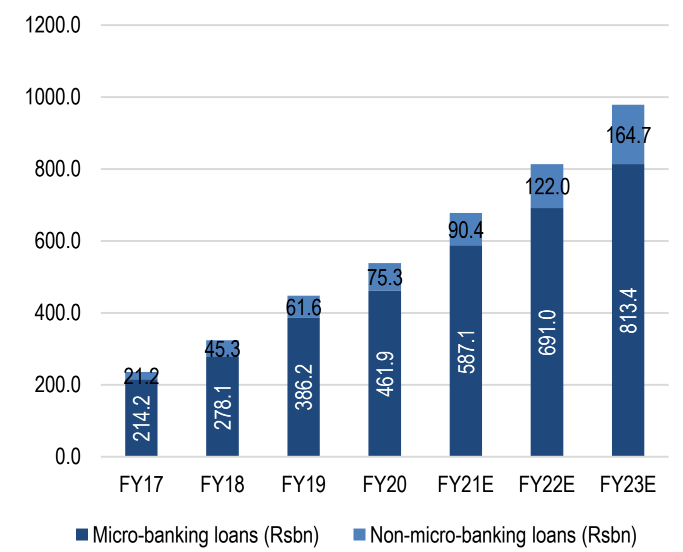
Exhibit 23: Bandhan's customer market share (%)*



Source: Company, Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

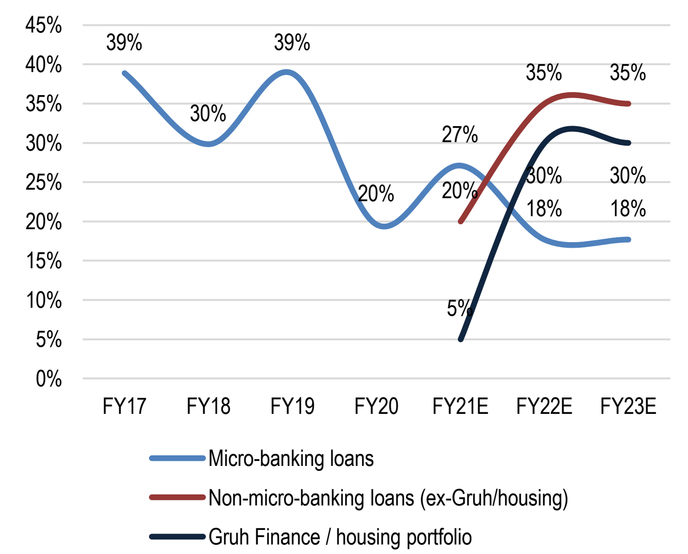
*Bandhan's MFI customers in WB divided by unique number of MFI customers in WB.

Exhibit 24: Segment wise loan book (Rsbn) – focus shifting towards non-MFI



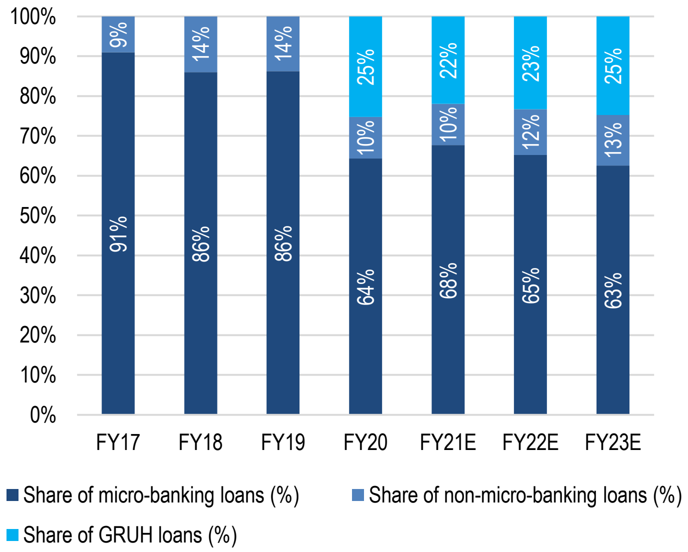
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 25: Segment wise advances growth rate (yoy, %) – non-MFI to grow at a higher rate



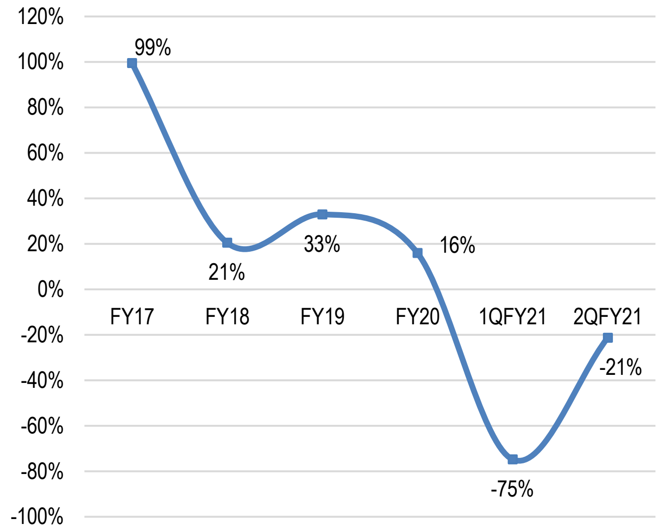
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 26: Segment wise advances mix (%)



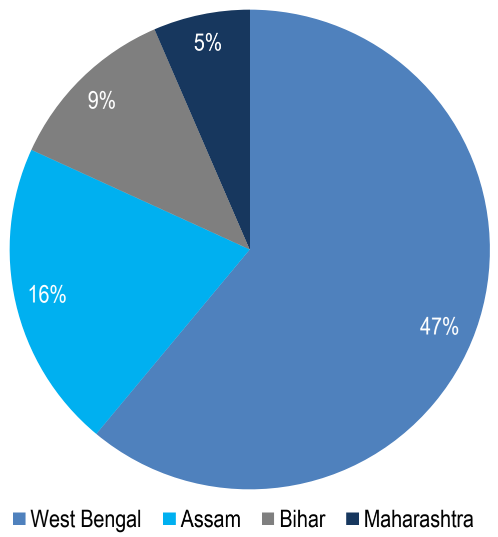
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 27: Growth in micro-banking disbursements (yoy, %)



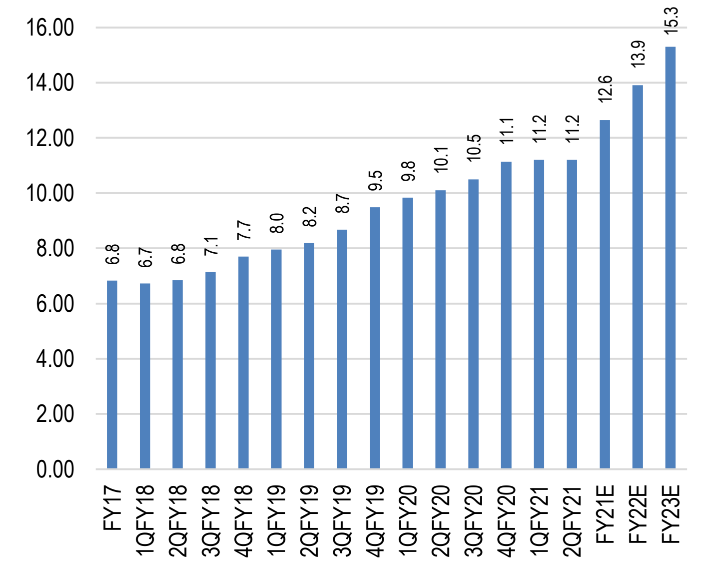
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 28: Micro-finance portfolio mix by state (%) (Q2FY21)



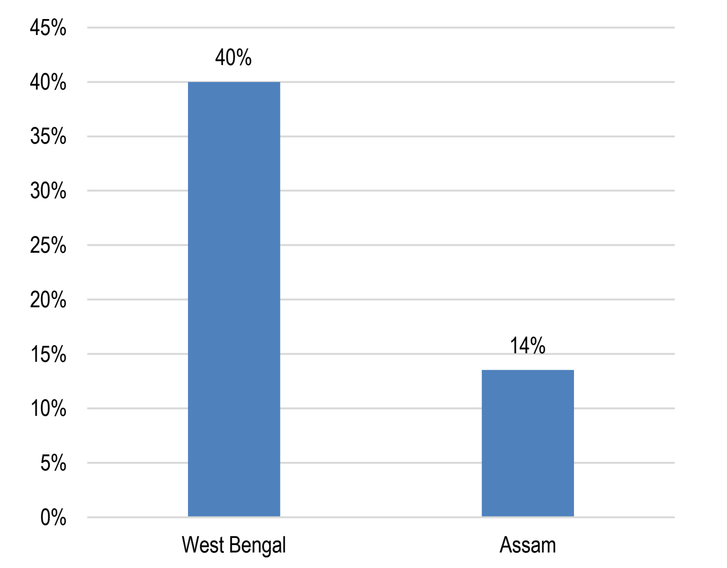
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 29: No. of active micro borrowers (mn)



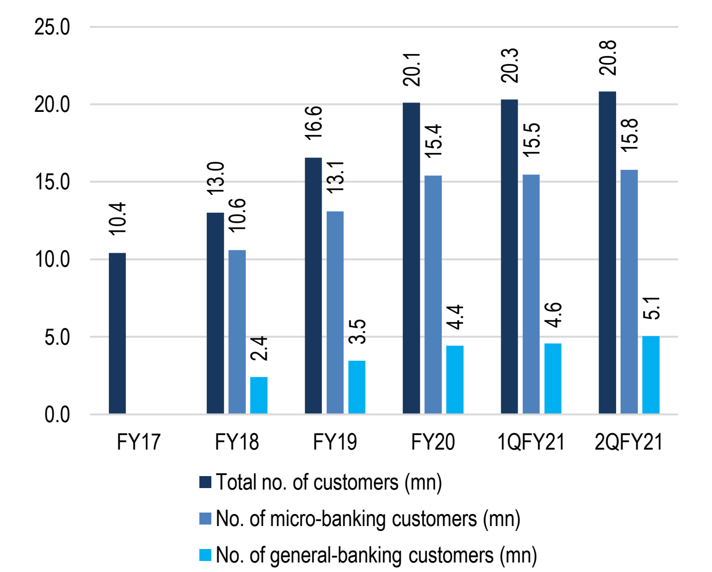
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 30: State wise share of total active micro-borrower (Q3FY20)



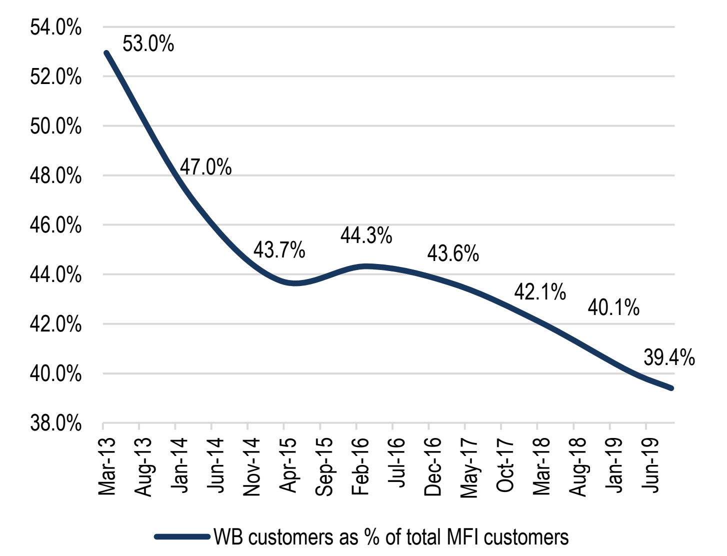
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 31: Customer statistics



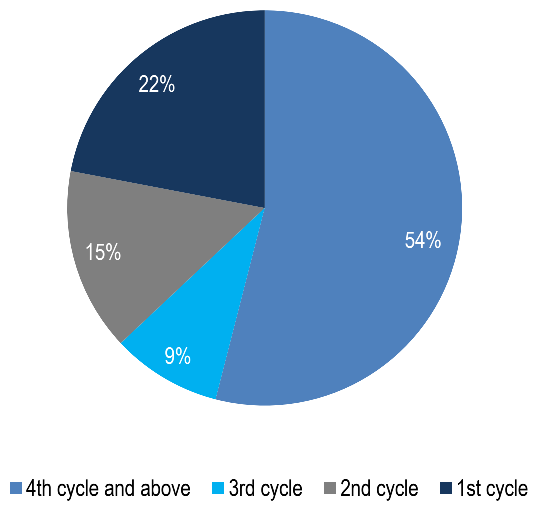
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 32: WB customers as % of total MFI customers



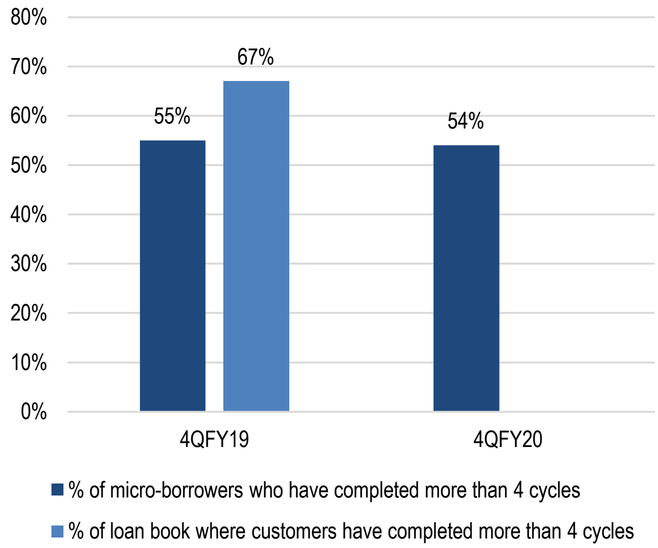
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 33: Bandhan's customer vintage is higher than the industry



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 34: Customer and loan book vintage

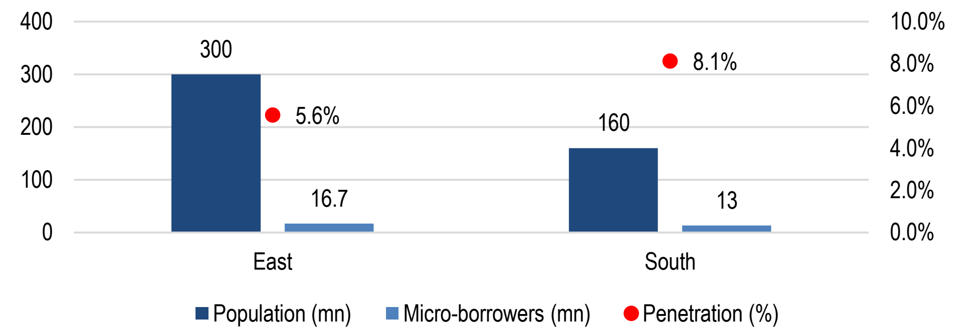


Source: Company, Nirmal Bang Institutional Equities Research

See scope for further micro-borrower penetration in East/NE

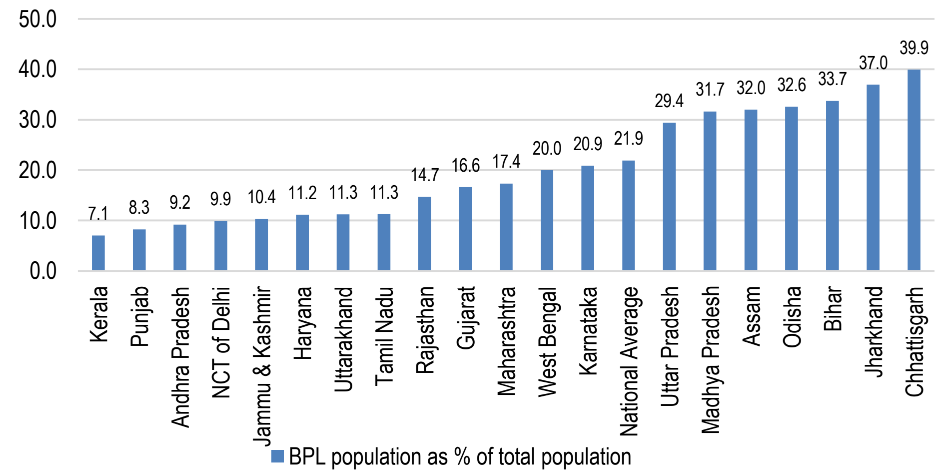
Our key reason behind modelling 10-13% growth (p.a.) in micro-borrower customer base is due to the lower micro-borrower penetration in the East/NE vis-à-vis South. Total population in east India is 300mn, out of which micro-borrowers are only 16.7mn. In south India, micro-borrower population is 13mn out of a total population of 160mn. Further, we have also looked at the ratio of number of unique micro-finance customers to total below-the-poverty-line (BPL) population, based on which we believe there is enough opportunity for the industry as well as Bandhan Bank to sustain the current growth rate in the medium term.

Exhibit 35: Micro-borrower penetration (as % of total population)



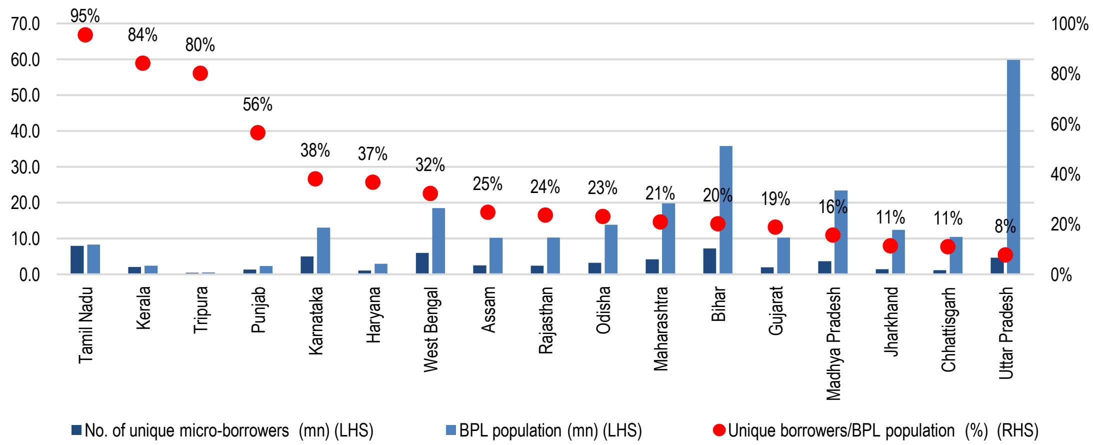
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 36: States with higher economic backwardness provide better growth opportunities



Source: RBI, GoI, Nirmal Bang Institutional Equities Research

Exhibit 37: Penetration, given the economic backwardness, is high in Tamil Nadu, reasonable in WB, low in UP and central

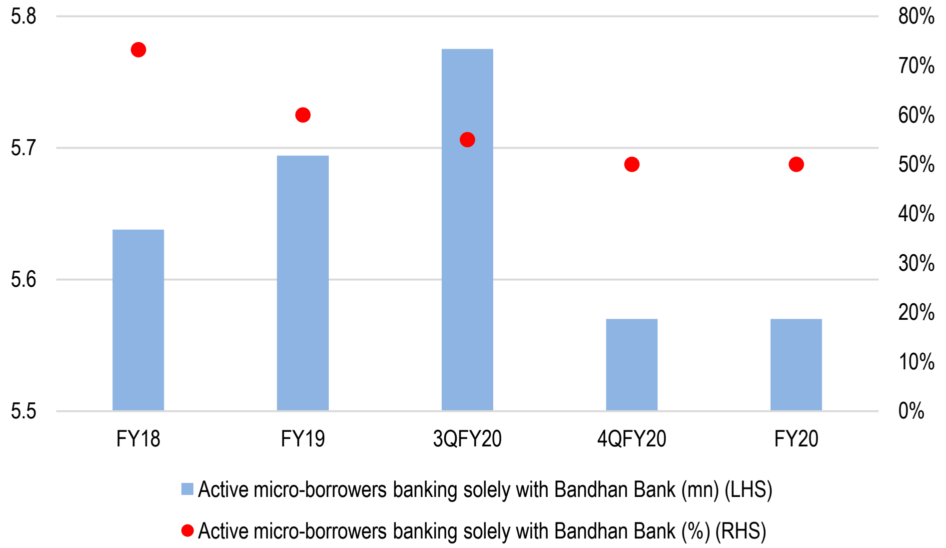


Source: Bharat Microfinance Report 2020, RBI, Nirmal Bang Institutional Equities Research

Part of MFI growth to come from regaining sole lender market share

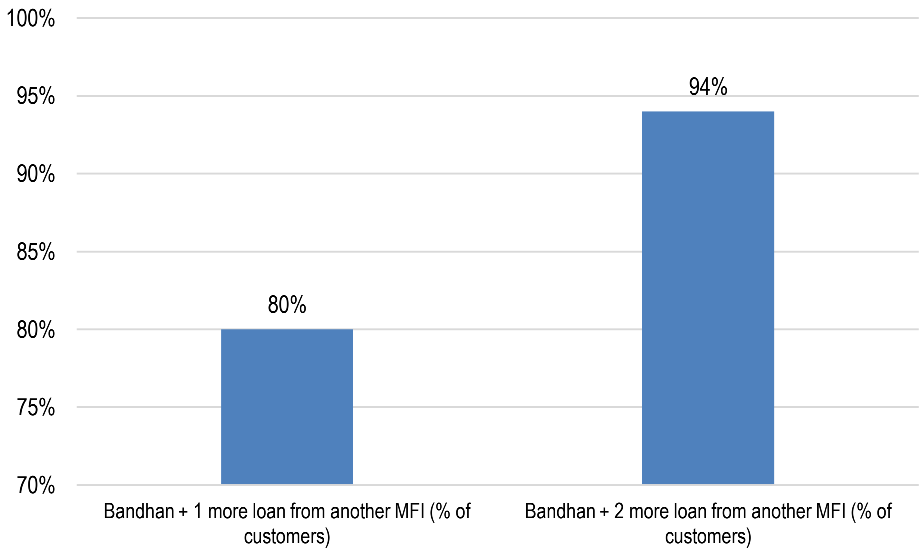
Three years ago, the share of micro-finance customers, where bank was the sole lender (to the customer), was 70%. This figure/number has now fallen to 50% as competition has started giving top-up loans. As a result of stressing more on liability management (due to the moratorium given to micro-finance customers), some NBFC-MFIs have significantly scaled back new disbursements. Considering this as an opportunity, the bank plans to scale back its share of exclusive customers by taking higher exposures. As of 2QFY21, top-up loans constituted 7.6% of the micro-finance loan book and 12% of the micro-borrowers. Average ticket size of top-up loans is Rs35,000.

Exhibit 38: Active micro-borrowers banking solely with Bandhan Bank



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 39: Bandhan is looking to regain some of the sole-lender status



Source: Company, Nirmal Bang Institutional Equities Research

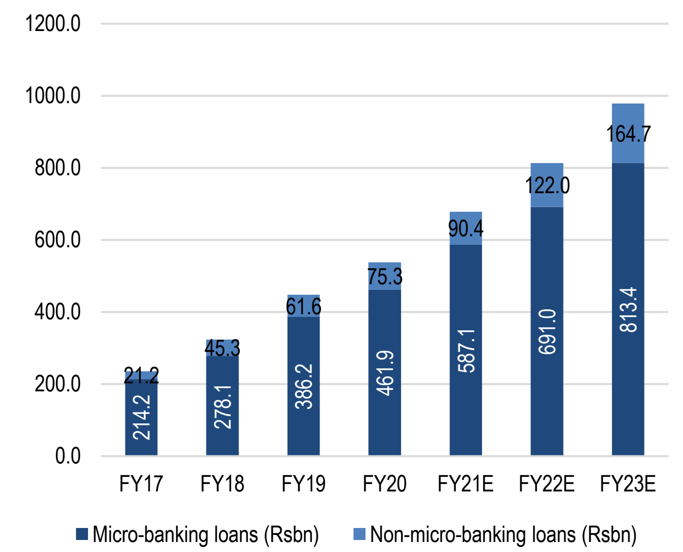
Looking to diversify exposures – Non-MFI to grow at a higher rate (Vision 2025)

Our estimate of the bank's micro-finance portfolio growth is lower than historical standards. Recently, the bank articulated its vision 2025 to reduce the share of micro-finance loans to 30% from 65% presently and simultaneously increase the share of commercial/MSME lending to 30%, housing to 30% and retail/personal loans to 10% in 5 years. A key part of executing this diversified growth strategy would be to cross-sell non-micro-finance loan products to existing (as well as new) micro-finance borrowers as they graduate in their needs/demands and overall income levels. The bank has stated that there is already good demand for these products from its existing and new customers. In the MSME segment, the bank is looking to tap high vintage micro-finance customers for growth.

Housing finance growth strategy is expected to be two-legged with one vertical focusing on micro-housing loans, which would be undertaken by the micro-finance vertical and another vertical focusing on prime housing loans with a higher-ticket size compared to Rs0.9-0.95mn currently. Untapped states of West Bengal, Jharkhand and UP are expected to provide impetus for growth in the housing finance portfolio. In line with the management's growth strategy, we expect the non-micro-finance portfolio to grow at 29.8% CAGR over FY20-23E.

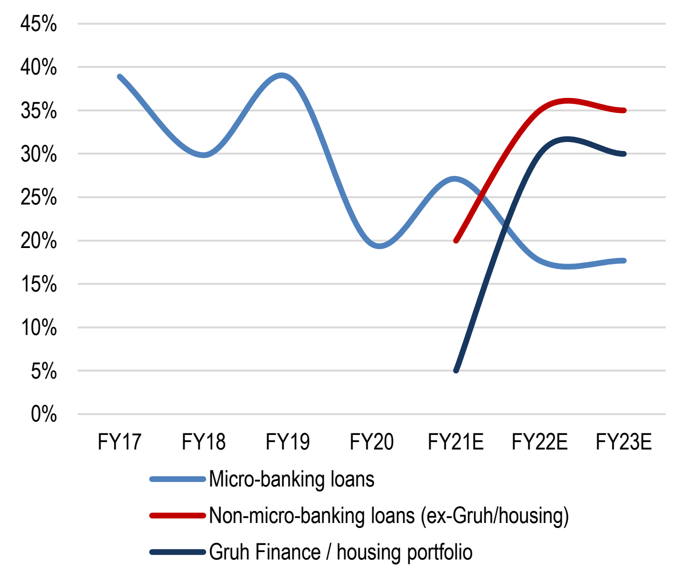
In the retail/personal segment, the management's strategy is to grow through the bank branch network. For instance, gold loan distribution has now been scaled up to 500+ branches compared to 100 branches a year ago.

Exhibit 40: Segment loan book (Rsbn) – focus shifting towards non-MFI



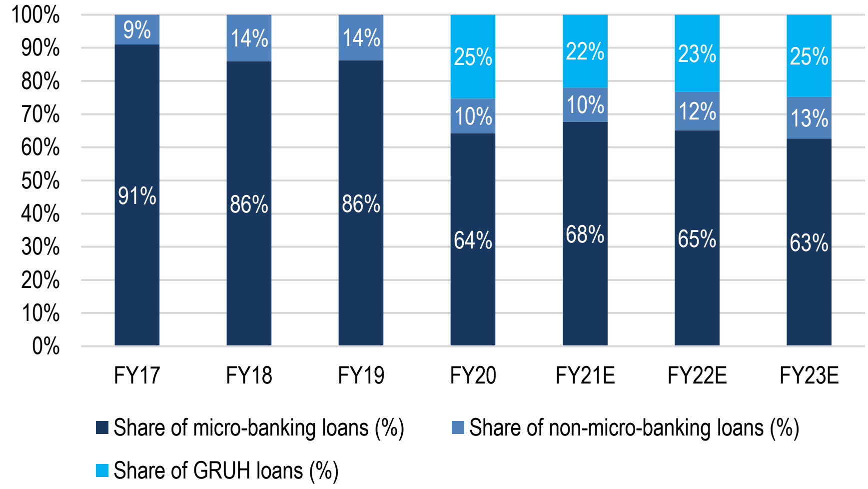
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 41: Segment wise advances growth rate (yoy, %) - non-MFI to grow at a higher rate



Source: Company, Nirmal Bang Institutional Equities Research

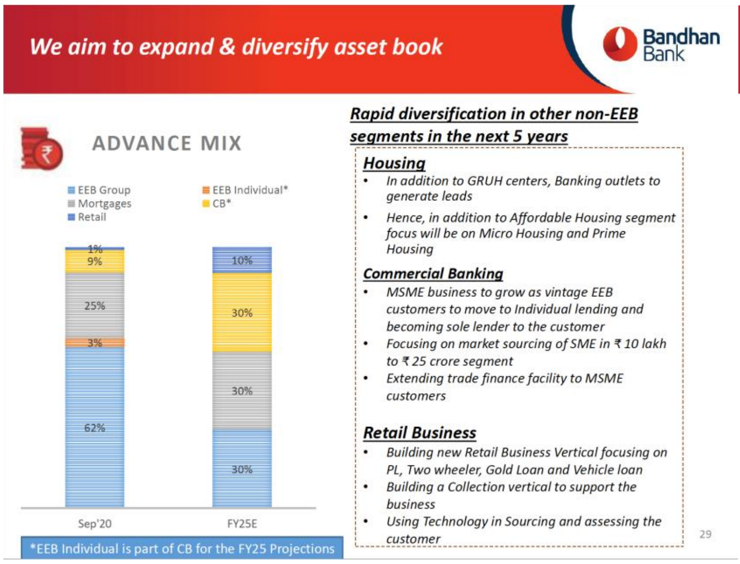
Exhibit 42: Segment wise advances mix (%)



Source: Company, Nirmal Bang Institutional Equities Research

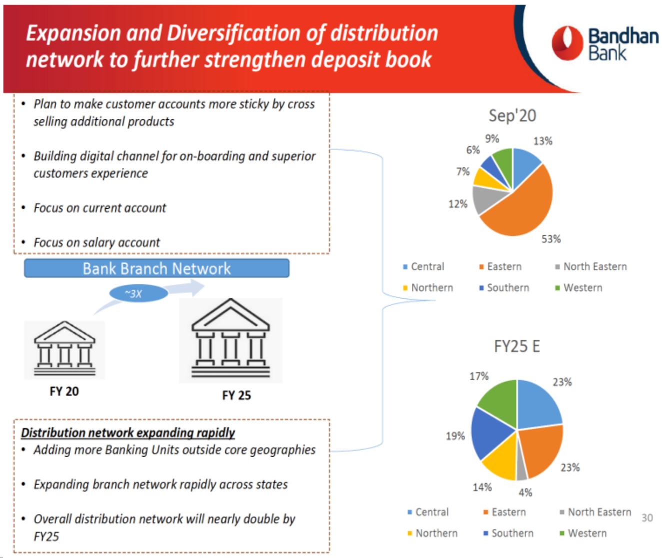
Vision 2025 – Key highlights

Exhibit 43: To reduce loan book concentration



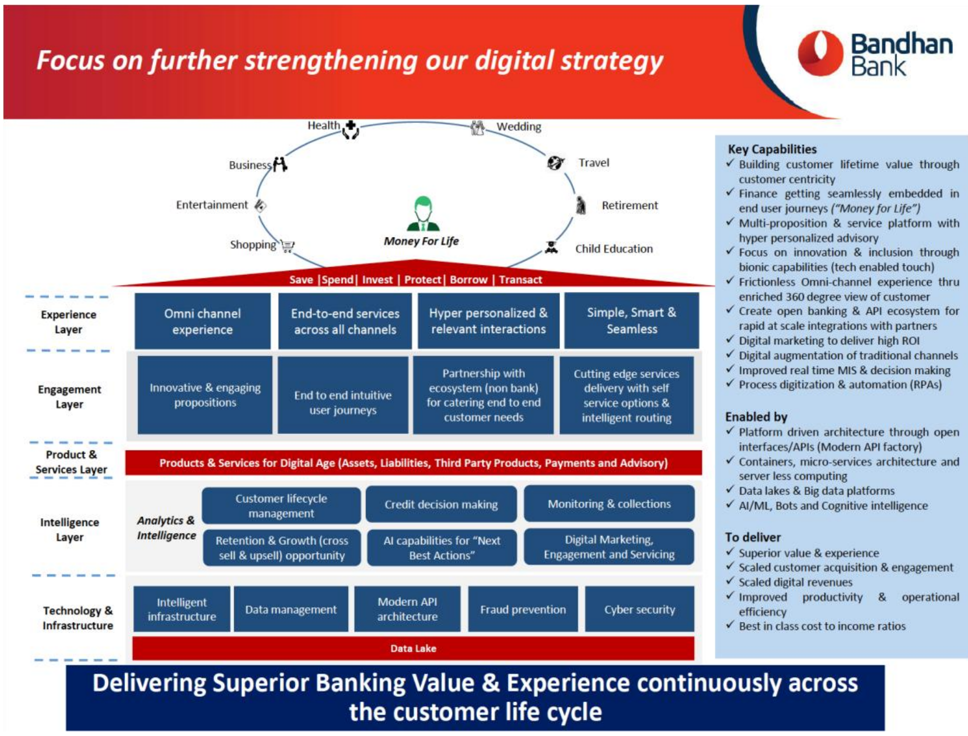
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 44: To reduce geographic concentration



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 45: Higher engagement with the customer beyond plain-vanilla banking likely to increase switching costs



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 46: Product suite

Loan	Sub Category	Description	Tenure	Amount	Interest Rate range
Micro Loans	**Suchana**	Income generation loan.	Upto 1 yr	Rs1,000-Rs25,000	17.95%
	Srishti	Income generation loan.	Upto 2 yrs	Rs26,000-Rs1,50,000	17.95%
	Su-Briddhi	Existing MFI borrowers with 1 Primary loan. Disbursed after 10th week of disbursement of running Primary loan. Monthly repayment.	Upto 3yrs	Upto 50% of disbursement of Primary loan	18.95%
	Samadhaan	Income generation loan for current MFI borrowers to tide over covid impact. Repayment Weekly/fortnightly for Saturday groups.	Upto 2 yrs	Rs5,000 (1st cycle) to Rs15,000 (completed 1st cycle)	17.95%
Small Enterprise loans		Unsecured loans for min 2yrs of vintage in same line of business.	Rs1Lakh-10Lakhs	TL-Tenure upto 3 yrs/WC repayable on demand.	17.00%-19.5%
MSME Loans	**WC Loan**	Repayable on Demand. Margin - Inventories (25%), Receivables (30%), LC&BG (25%)			10.06%-16.72%
	Term Loan	Max morat of 3 months. 25% Margin.	Upto 7yrs		10.06%-16.72%
	Micro Enterprise Loan	Borrower should have completed min 4 cycles of Suchana/Srishti.	Upto 2 yrs	Rs 151,000 to Rs3,00,000	17.95%
	Samriddhi Loans	Existing MB borrowers who have completed min 2 cycles can apply as co-applicant and her close relative will be the applicant. Repayment through EMI.	Upto 2 yrs	Rs 75,000 to Rs3,00,000	17.95%
	Micro Bazaar Loans	Facility for existing deposit holders who themselves and their spouse are not existing borrowers of Suchana/Srishti/Micro enterprise loans for WC needs.	Upto 2 yrs	Rs26,000-Rs1,50,000	17.95%
Gruh Home Loans	**Suraksha**	Home loan for Purchase/Construction/Extension of house. Offered to Individuals with formal income proofs (Salary slip with PF deduction/IT returns).	Upto 30yrs	Upto 75-90% of cost of property.	8.50%-11.5%
	Suvidha	Home loan for Purchase/Construction/Extension of house. Offered to Individuals without formal income proofs (income assessed based on CF).	Upto 30yrs	Upto 75-90% of cost of property.	8.75%-11.75%
	Repair loans	Offered to individuals for repair/renovation of house.	Upto 15yrs	Upto 75-80% of cost of repair work.	9.25%-11.75%
	LAP		Upto 30yrs	upto 60% of cost of the residential property or 50% of the cost of commercial property.	10.00%-13.50%
2 Wheeler Loans		Can be availed by Salaried/SEP/SENP of 21-57yrs age.	Upto 3 yrs	Rs10,000 to Rs1,50,000 (Upto 85% of on road price)	15.50%-19.07%
Loan against TD			Upto 3 yrs	Upto 90% of TD	Deposit Rate + 1.5%-2.0%
Personal Loan			Upto 3 yrs	Rs50,000 to Rs5,00,000	14%-16.26%
Gold Loans		Disbursement within 45mins. Eligible age 18-70yrs.	Upto 3 yrs		10.99%-18%
Agri Loans	**Kisan Credit Card**	Locations : MP/Punjab/Haryana	Upto 5yrs	Rs25,001 to Rs1,00,00,000	

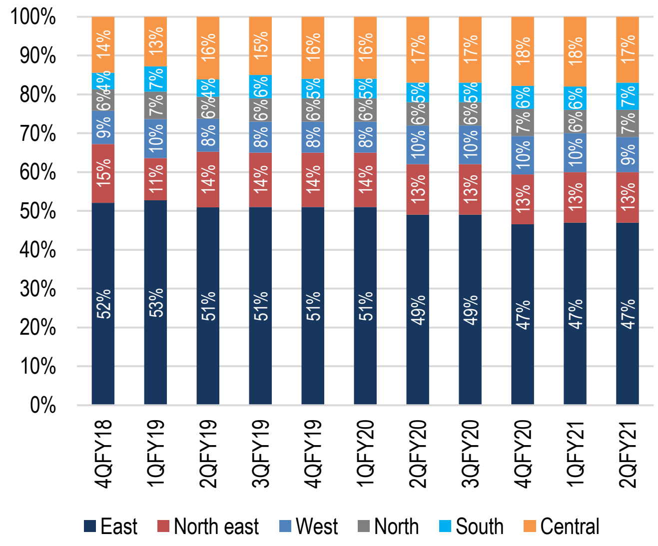
Source: Company, Nirmal Bang Institutional Equities Research

Predominantly focused on east/north east with a rural/semi-urban orientation

Bandhan Bank started its operations from the village of Bagnan near Kolkata. Over the years, while the organisation has shifted forms from being an NGO to an NBFC-MFI to a universal bank, expanded its range of offerings both on the assets and liabilities side and branched out operations across other states of the country, it has continued to derive a major chunk of its business from the east and north east regions, primarily West Bengal. Out of the total advances, West Bengal and Assam together account for ~60%. In terms of the micro-finance book, the two states account for 63% collectively. 40% of Bandhan Bank's micro-finance customers are from West Bengal while Assam accounts for 14% of the total (Dec'19).

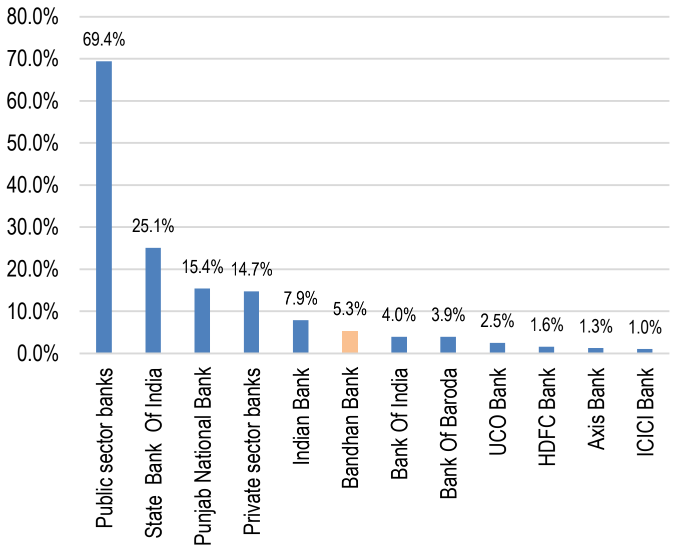
As of 2QFY21, out of the total banking outlet network, east and north east accounted for 47% and 13%, respectively. Though still high, the share of east and north east banking outlets has declined from 52.1% and 15.1%, respectively, as of FY18, implying Bandhan Bank's growing focus outside its home markets. Over the same period, the share of central India banking outlets has increased from 14.4% to 17%. Banking outlet share of south and north has also increased significantly while the share of west is up marginally since FY18.

Exhibit 47: Region wise banking outlet mix (%)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 48: Banking outlet market share in West Bengal (%)



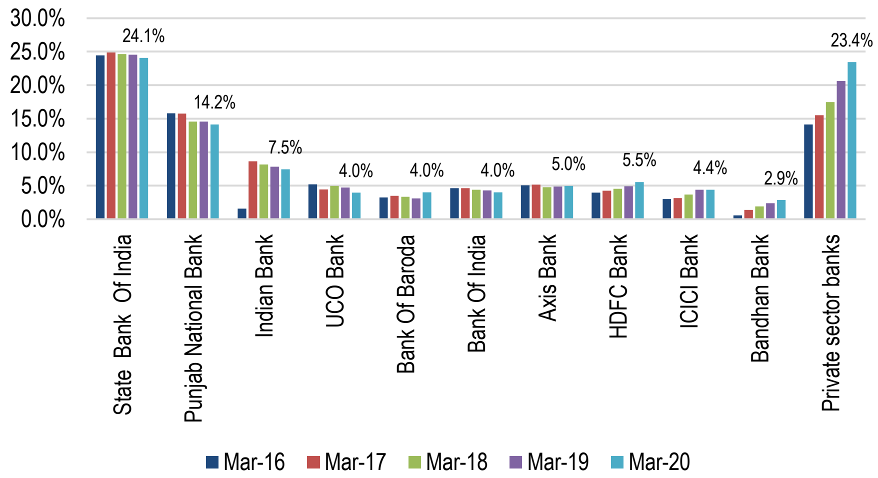
Source: SLBC, Nirmal Bang Institutional Equities Research

Poised for market share gains in WB on the deposits side

On the deposits front, Bandhan Bank has seen its WB market share improve from 1.4% in FY17 to 3% in 1QFY21. Bandhan Bank's WB deposits have grown at a CAGR of 38.1% over FY17-20. We attribute such strong growth and market share gains to Bandhan Bank's higher deposit rate offerings compared to peer banks in the state. Given the high margins on the asset side of the balance sheet, we think that Bandhan Bank can comfortably accommodate relatively higher deposit rates as a key strategy for building its deposit profile.

Private sector banks have seen their deposit market share increase from 14.1% in FY16 to 23.4% in FY20. This means that public sector banks still account for ~70% of the total state deposits. As the market share shifts further towards private sector banks, given Bandhan Bank's market positioning in WB and its higher-rate strategy, we expect the bank to gain further market share. Therefore, we believe that there is enough deposit growth opportunity for Bandhan Bank in WB.

Exhibit 49: Deposits market share in West Bengal (%)

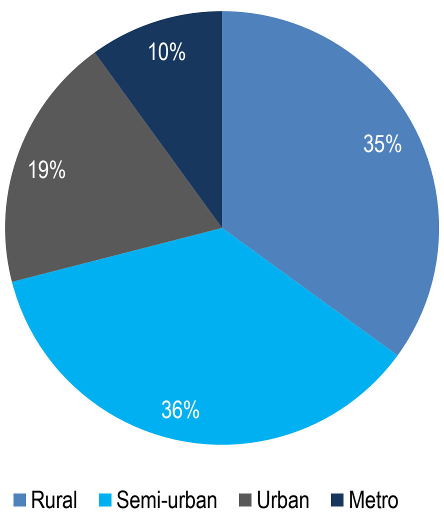


Source: SLBC, Nirmal Bang Institutional Equities Research.

Distribution network is rural and semi-urban oriented

As of FY20, 35% of Bandhan Bank's banking outlets were located in rural areas and 36% in semi-urban areas. Banking outlet exposure to metro area is relatively much lower at 10%. Given that metro and urban areas have been well exploited by banks and are therefore highly competitive, it is a reasonably sound strategy to focus on rural and semi-urban India, where growth opportunities are higher.

Exhibit 50: Area wise banking outlet mix (%) (Q2FY21)



Source: Company, Nirmal Bang Institutional Equities Research

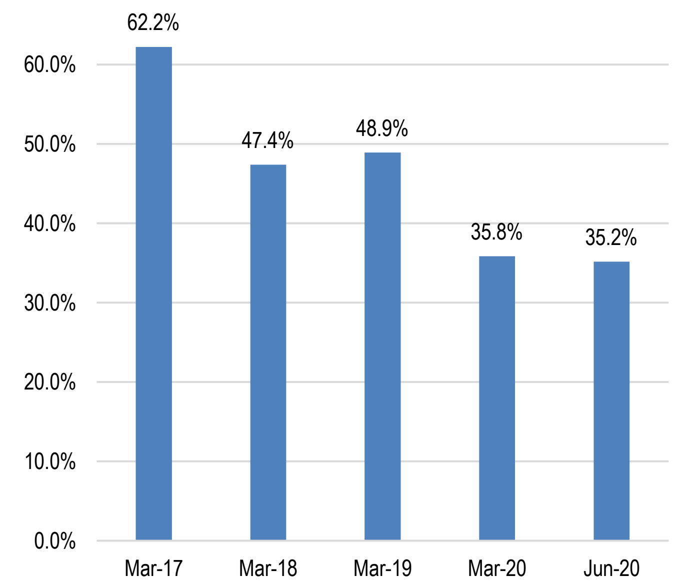
Lower C/D ratio in east and north east presents enough opportunity for credit growth

A lower C/D ratio in east (~41%) and north east (~42%) compared to the national average of 72% implies lower credit penetration in east and north east. C/D ratio for WB stands at 46%. An overall improving credit penetration in these regions bodes well from a credit growth standpoint. One of our key growth assumptions for Bandhan Bank is 10-13% growth per annum in micro-borrowers – this implicitly assumes an improving C/D ratio (improving credit penetration) going forward.

West Bengal accounts for >40% of the total business

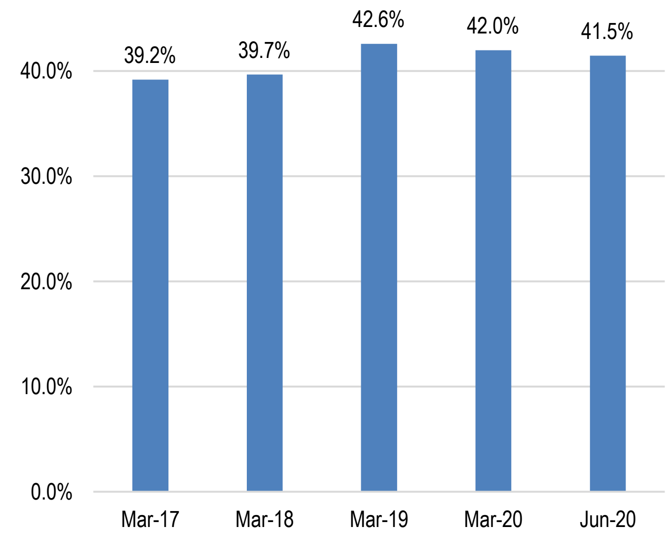
Bandhan Bank's deposit exposure to West Bengal (WB) is 41.5% (Jun-20) while market share in total state deposits is 3% (Jun-20). In terms of MFI exposure, WB accounts for 47% of the micro-credit advances (Sep-20). Therefore, there is a case for geographic concentration risk. Post GRUH acquisition, this risk has been addressed to some extent. However, the bank still remains susceptible to the state-specific vagaries. Any major adverse development or disruption in the state could have negative implications for Bandhan Bank.

Exhibit 51: Bandhan's share of loans from WB (% of total advances)



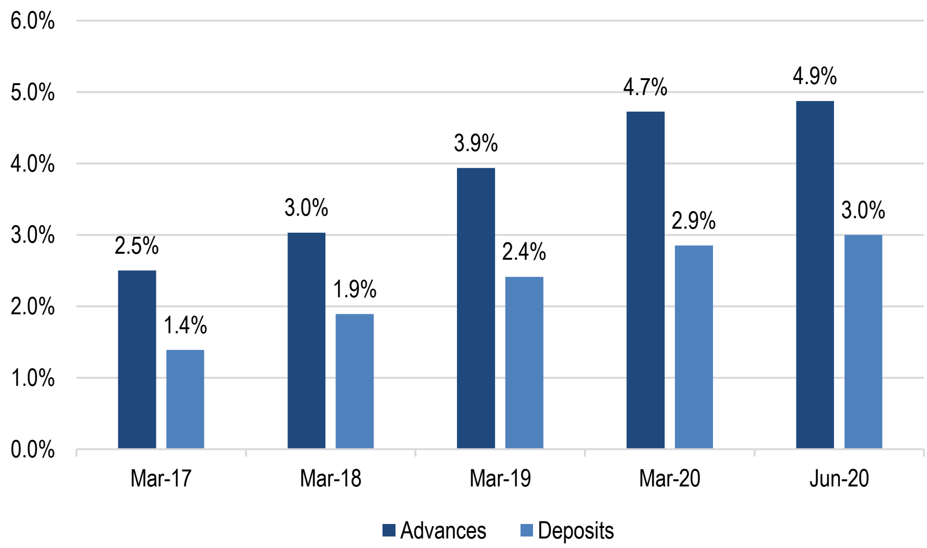
Source: SLBC, Nirmal Bang Institutional Equities Research

Exhibit 52: Bandhan's share of deposits from WB (%)



Source: SLBC, Nirmal Bang Institutional Equities Research

Exhibit 53: Bandhan's WB market share (%)

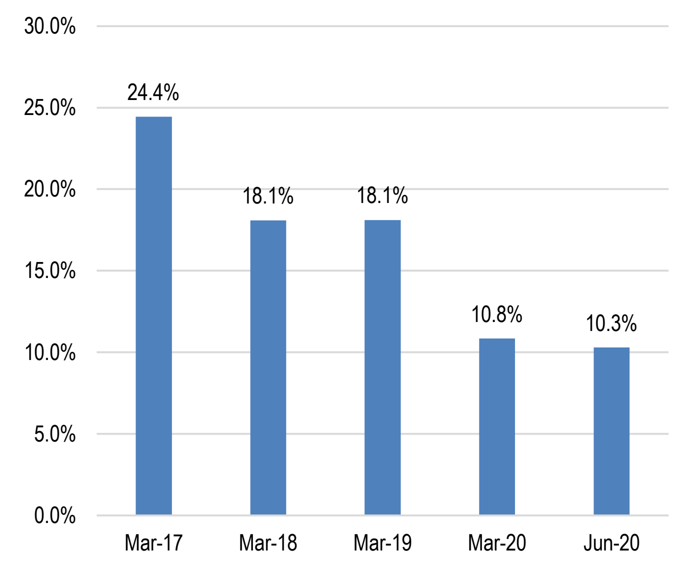


Source: SLBC, Nirmal Bang Institutional Equities Research

Slowed down on Assam owing to increasing risks

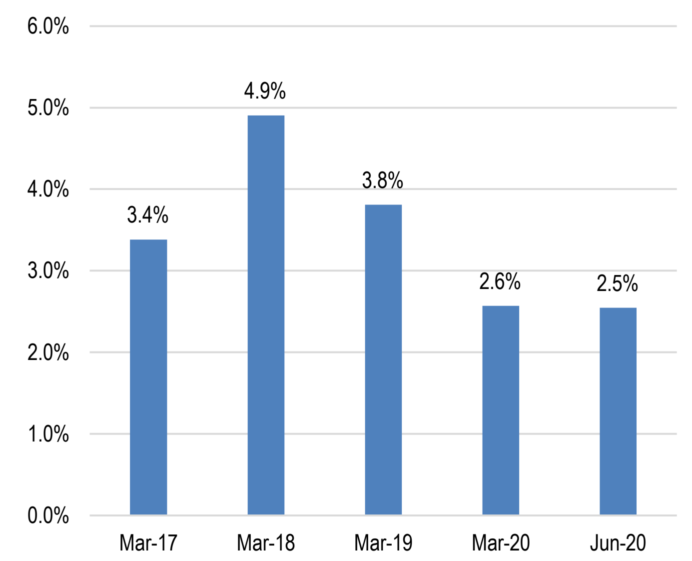
Assam is another very large market for Bandhan Bank, accounting for 10.3% of the overall advances (Jun-20). In terms of micro-finance exposure, Assam accounts for 16%. In FY20, the bank slowed down growth in Assam owing to heightened credit and overall business risks due to protests/agitation. In 3QFY20, almost the entire increase in 30+ DPD for Bandhan Bank came from Assam as collection rates dipped to 93-94%.

Exhibit 54: Bandhan's credit exposure to Assam



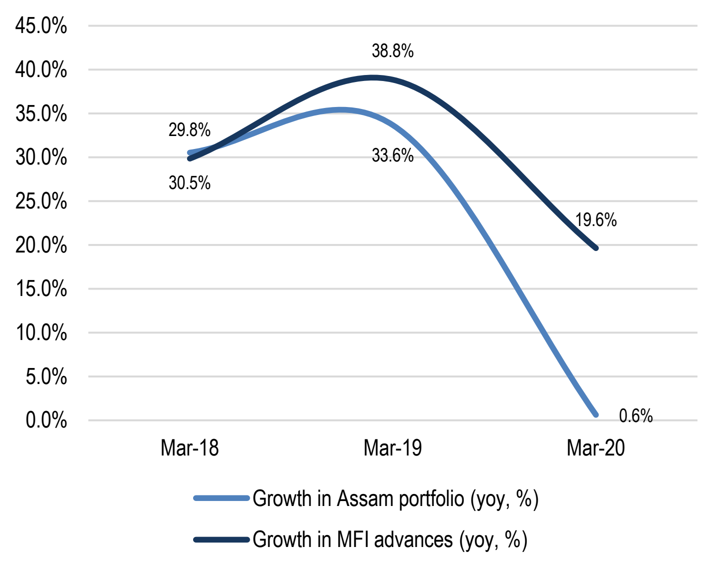
Source: SLBC, Nirmal Bang Institutional Equities Research

Exhibit 55: Share of deposits from Assam (%)



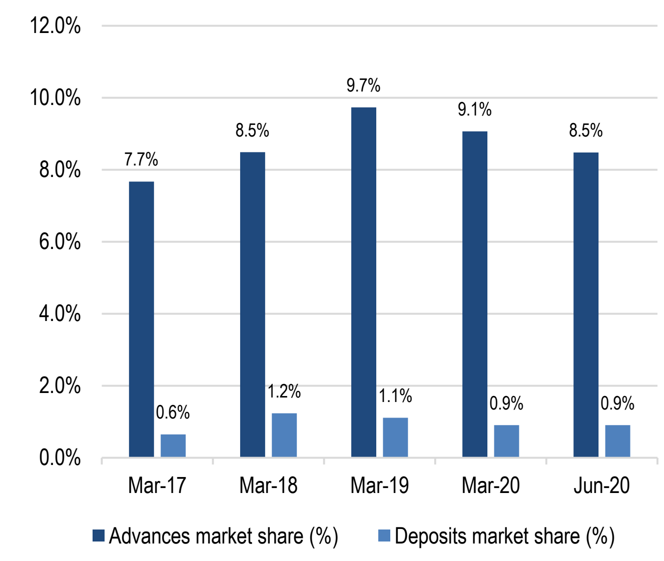
Source: SLBC, Nirmal Bang Institutional Equities Research

Exhibit 56: Bandhan slowed down growth in Assam due to heightened business risks



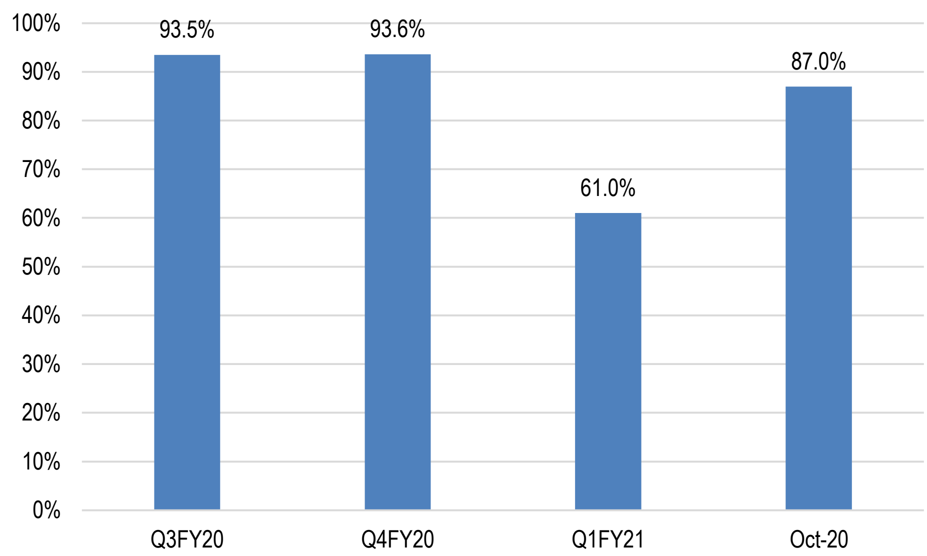
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 57: Stronger credit market share in Assam



Source: SLBC, Nirmal Bang Institutional Equities Research

Exhibit 58: Assam collections trend (%) – impacted due to protests, lockdown and floods

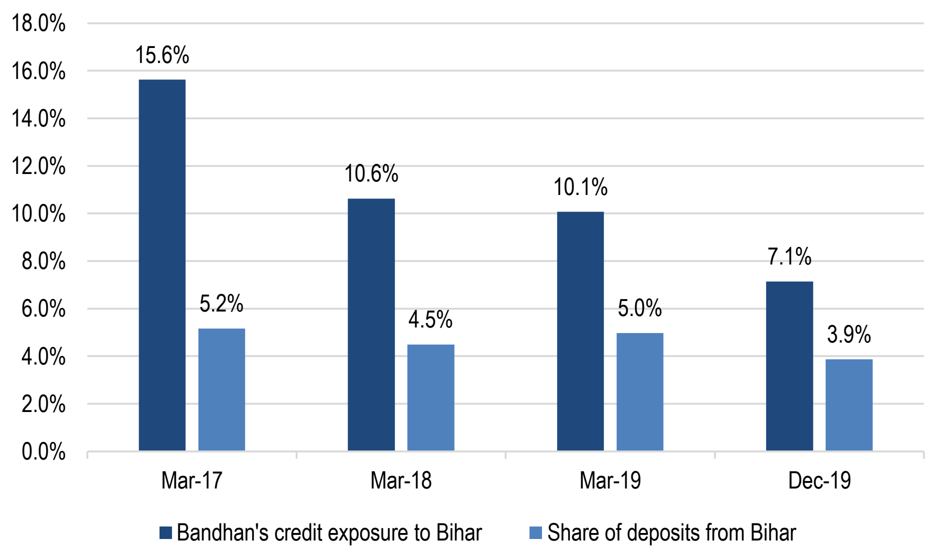


Source: Company, Nirmal Bang Institutional Equities Research

Concentration in Bihar is coming down too

The share of advances from Bihar has declined from 15.6% in Mar-17 to 7.1% in Dec-19 while the share of deposits from the state has declined from 5.2% in Mar-17 to 3.9% in Dec-19.

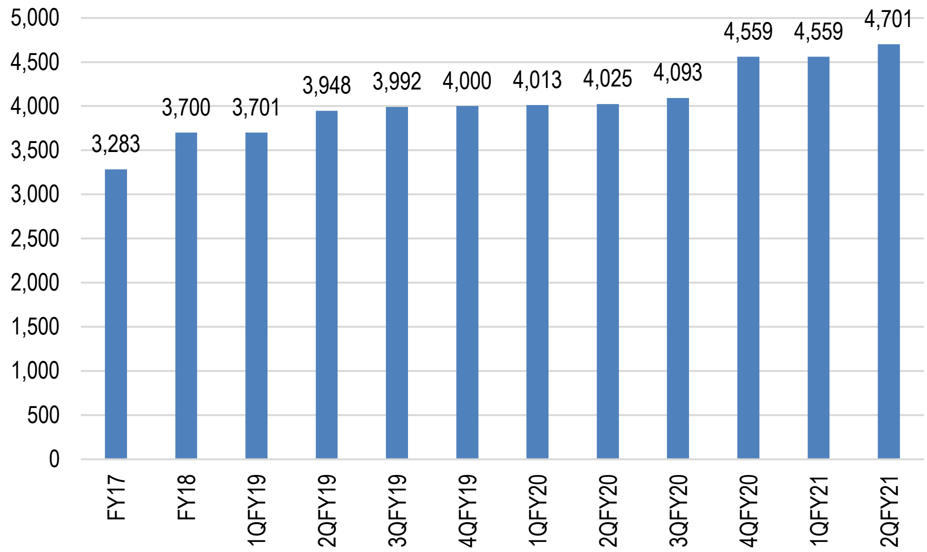
Exhibit 59: Bihar as % of Bandhan's advances and deposits



Source: SLBC, Nirmal Bang Institutional Equities Research

Distribution network

Exhibit 60: Total banking outlets (nos.)



Source: Company, Nirmal Bang Institutional Equities Research

Bandhan Bank follows a hub-and-spoke distribution strategy whereby, on average, 3-4 DSCs are linked to a bank branch. Customers of these DSCs automatically become customers of the associated bank branch, allowing them to open accounts and conduct their banking needs. The hub-and-spoke model provides the bank with low-cost means to extend its distribution network deep into underbanked areas. DSC overheads, compared to a full-fledged bank branch, are lower. For instance, IT/tech requirements of a DSC comprise of internet-enabled handheld devices while a bank branch requires full-fledged computer terminals. As a result of the bank's extensive yet low-cost distribution network, coupled with its focus on tech initiatives, the cost/income ratio has come down from 36.3% in FY17 to 30.8% in FY20.

Deposit scale up impressive, liability franchise comparable with best-in-class

The bank's deposit base has grown at 35% CAGR over FY17-20. YTD (1HFY21), total deposits are up 15.8% YoY. The bank's deposit growth strategy has been a retail-led one. Compared to 71% as of FY17, retail deposits constituted ~78% of the total deposits as of 2QFY21. Over FY17-20, retail deposits have grown at a CAGR of 39.5% (higher than overall deposits growth). Over the same period (FY17-20), CASA deposits have grown at a CAGR of 45.4% and retail TDs have grown at CAGR of 34.9%. Given the granularity, we believe the deposit growth has been a quality one.

Despite being relatively young, the bank's CASA ratio is enviable at 38.2% as of 2QFY21, up from 29.4% as of FY17. Improvement in CASA ratio has primarily come from the SA front. Among the new-age and mid-cap banks, Bandhan Bank's CASA scale up has been more impressive given that the liability-side granularity has not been diluted for the sake of growth.

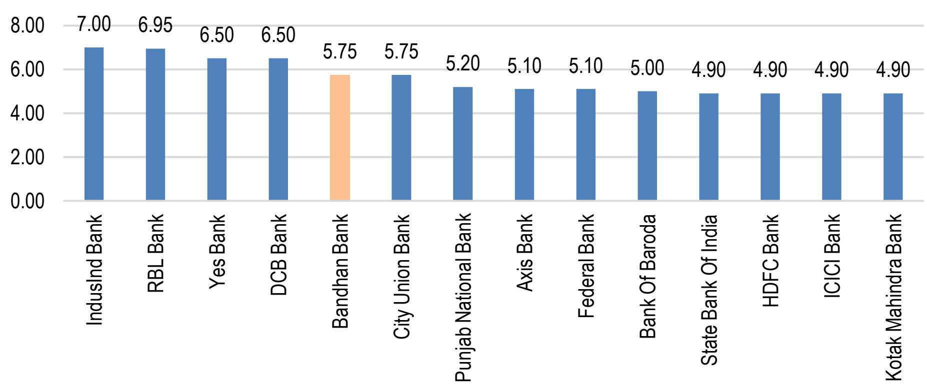
The bank is not aggressive in pushing deposit products to its micro-borrowers as the focus is primarily on credit, which explains the low share of deposits from the micro-banking customers at 5% as of 1QFY21. Typically, when MFI EMIs are collected, the bank ends up collecting Rs30-50 extra as deposits, but during the pandemic, the bank has emphasized only on EMI collection. As a result, average SA balance for micro-banking customers has fallen by 22% YTD.

Exhibit 61: Deposit profile comparison across coverage banks

Banks	Total deposits (Rsbn)			CASA ratio (%)			Deposit market share (%)		
	FY18	FY19	FY20	FY18	FY19	FY20	FY18	FY19	FY20
State Bank Of India	27,063	29,114	32,416	44.5%	44.6%	45.2%	23.7%	23.2%	23.9%
HDFC Bank	7,888	9,231	11,475	43.5%	42.4%	42.2%	6.9%	7.3%	8.5%
Bank Of Baroda	5,913	6,387	9,460	35.8%	35.0%	35.3%	5.2%	5.1%	7.0%
ICICI Bank	5,610	6,529	7,710	51.7%	49.6%	45.1%	4.9%	5.2%	5.7%
Punjab National Bank	6,422	6,760	7,038	41.0%	42.2%	43.0%	5.6%	5.4%	5.2%
Axis Bank	4,536	5,485	6,401	53.8%	44.4%	41.2%	4.0%	4.4%	4.7%
Kotak Mahindra Bank	1,926	2,259	2,628	50.8%	52.5%	56.2%	1.7%	1.8%	1.9%
IndusInd Bank	1,516	1,949	2,020	44.0%	43.1%	40.4%	1.3%	1.5%	1.5%
Federal Bank	1,120	1,350	1,523	33.7%	32.4%	30.7%	1.0%	1.1%	1.1%
Yes Bank	2,007	2,276	1,054	36.5%	33.1%	26.6%	1.8%	1.8%	0.8%
RBL Bank	439	584	578	24.3%	25.0%	29.6%	0.4%	0.5%	0.4%
Bandhan Bank	339	432	571	34.3%	40.8%	36.8%	0.3%	0.3%	0.4%
City Union Bank	329	384	408	24.2%	25.2%	25.0%	0.3%	0.3%	0.3%
DCB Bank	240	284	304	24.3%	23.9%	21.5%	0.2%	0.2%	0.2%

Source: Company, Nirmal Bang Institutional Equities Research

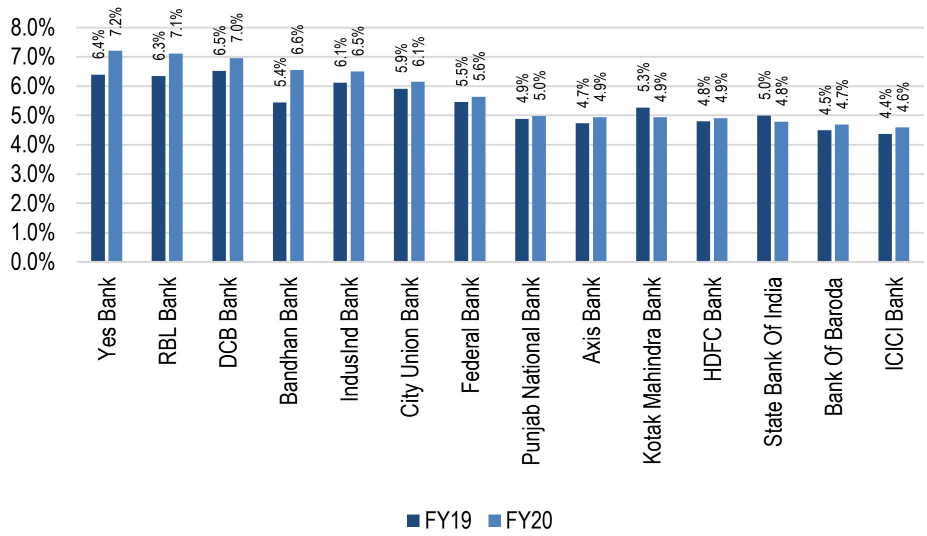
Exhibit 62: Deposit rate (%)*



Source: Company, Nirmal Bang Institutional Equities Research

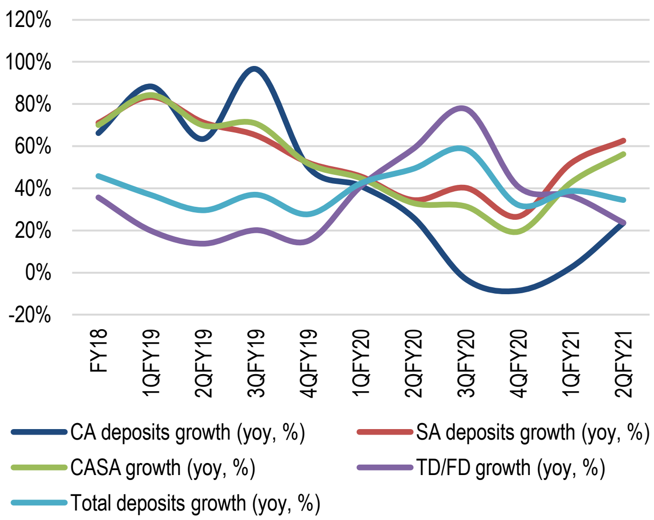
* for deposits less than Rs20mn as on 10th Dec 2020; maturity 1-2 years

Exhibit 63: Cost of deposits comparison with peers (%)



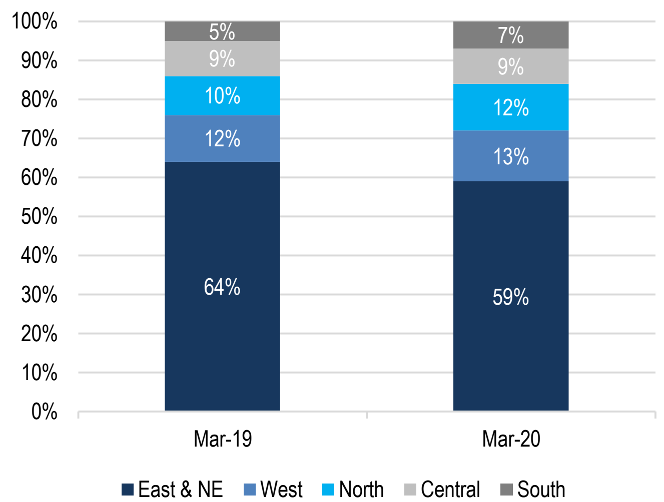
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 64: Liabilities growth



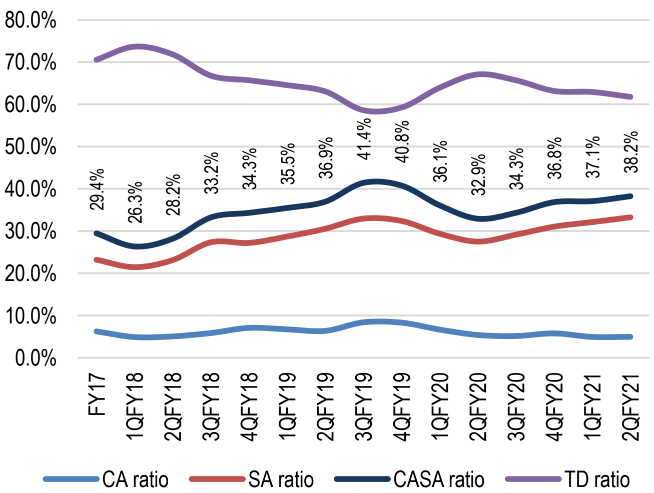
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 65: Customer deposit break-up by region (%)



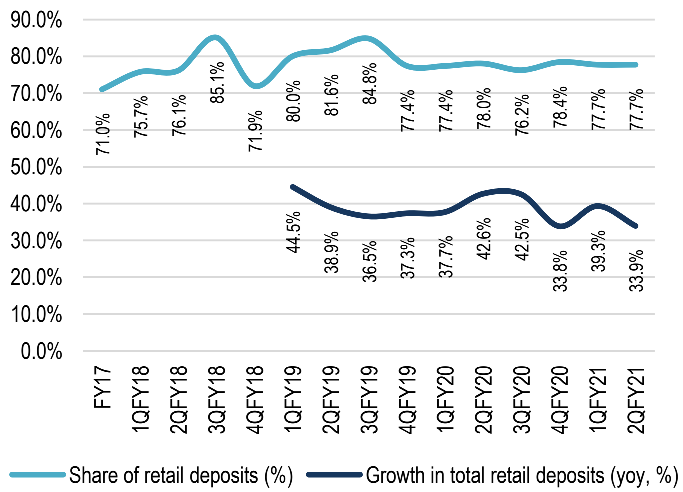
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 66: Strong CASA franchise for a relatively young bank



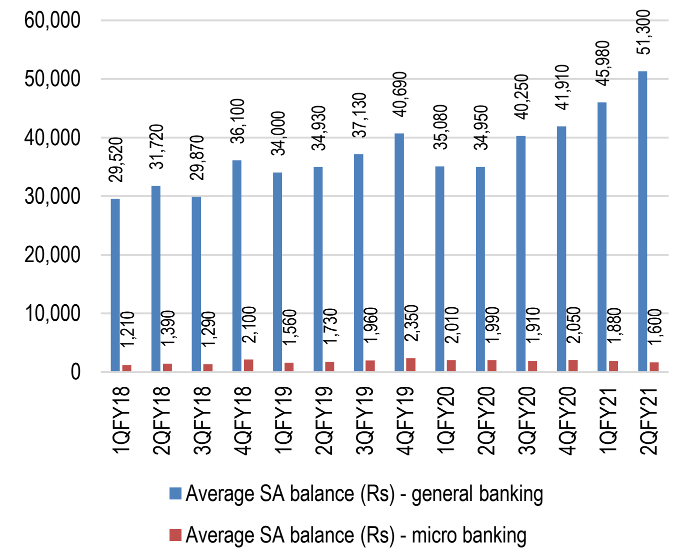
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 67: Ramp up in retail deposits has been impressive



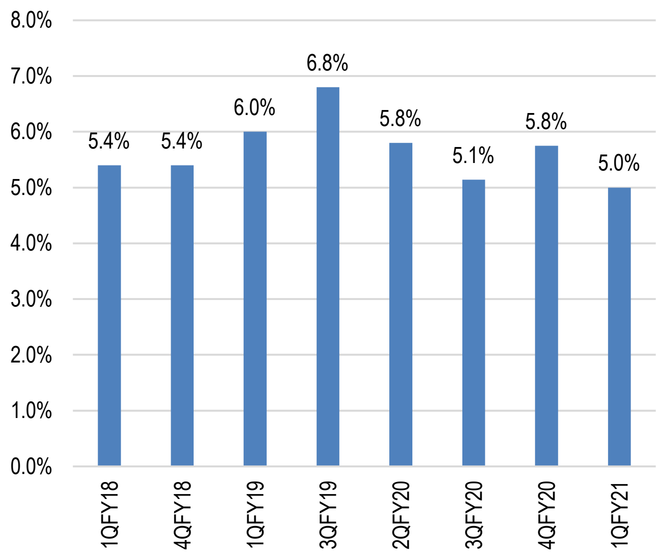
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 68: Average SA balance



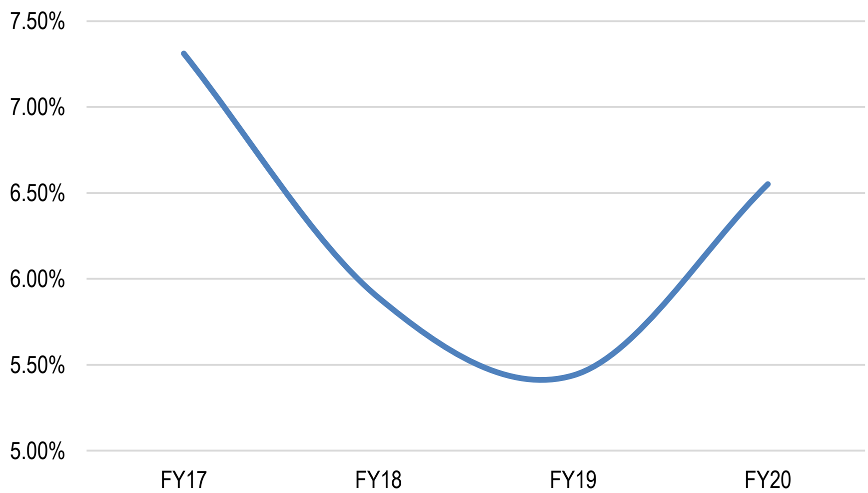
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 69: Micro-banking contribution to total deposits (%)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 70: Cost of deposits (%)

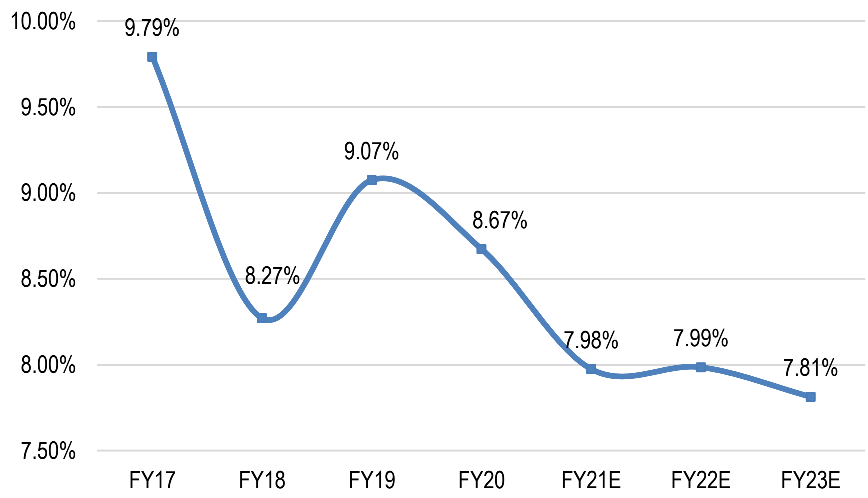


Source: Company, Nirmal Bang Institutional Equities Research

Higher growth in non-MFI to lead to NIM compression

Over FY17-20, the NII has grown at a CAGR of 38% compared to a CAGR of 58% in overall loans. As of FY17, the share of high-margin micro-finance business was 91% but has since declined to 64% as of FY20. Accordingly, over the same period, NIMs have declined by 112bps. Despite a sharp decline in the share of micro-finance loans, NIM compression has to some extent been cushioned by the decline in cost of deposits. Given that the share of micro-finance is expected to decline further, we expect blended NIM to compress going forward. We expect 86bps compression in NIMs over FY20-23E and 116bps over the next 5 years (by FY25E). Even though we expect the overall cost of funds to improve over our forecast period, yield compression is likely to be higher on account of higher growth in the bank's non-micro finance portfolio.

Exhibit 71: NIM (%)



Source: Company, Nirmal Bang Institutional Equities Research

Low-cost operations and PSL self-sufficiency producing superior cost ratios

The bank has done a commendable job in terms of improving the opex ratios. Over FY17-20, the cost/income ratio has improved from 36.3% to 30.8%. As of 2QFY21, the cost/income ratio stood at 29.4%. A large part of the cost structure improvement has come through the non-staff line items. For instance, rent/income has declined from 3.4% in FY17 to 2.5% in FY20.

At the same time, the PSL self-sufficiency has provided significant boost to other income. PSLC income, forming 20-30% of total non-interest revenue, has grown at 104.7% YoY and 46.9% YoY in FY19 and FY20, respectively.

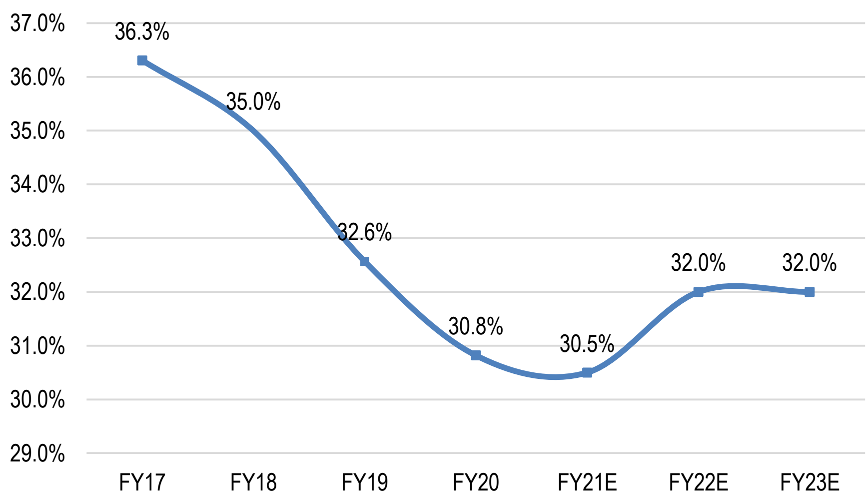
Due to micro-finance being a relationship-based business, the business models are usually people-heavy. In cases where collections are on a weekly basis, such as Bandhan Bank, we believe the manpower requirement would be relatively higher. What compensate for the higher manpower dependence are (1) higher NIMs (2) lower salaries as technical skill requirement is lower in micro-finance. Bandhan Bank's employee cost per head is about 50% lower than the second-lowest bank in our coverage.

In terms of the banking outlet infrastructure, Bandhan Bank's cost metrics are superior to peers. Rent per banking outlet for Bandhan Bank is 63% lower than the second-lowest bank in our coverage. This is partly because the share of rural and semi-urban banking outlets is 71% (Mar-20), where rents are lower than urban and metro centres. Also, due to a higher share of micro-finance loans, which is a highly field-oriented segment, the requirement for full-fledged branches is relatively low. DSCs (low-cost micro-finance centres) account for 78% of the total banking outlets (Sep-20) for Bandhan Bank.

Are the cost advantages durable in nature?

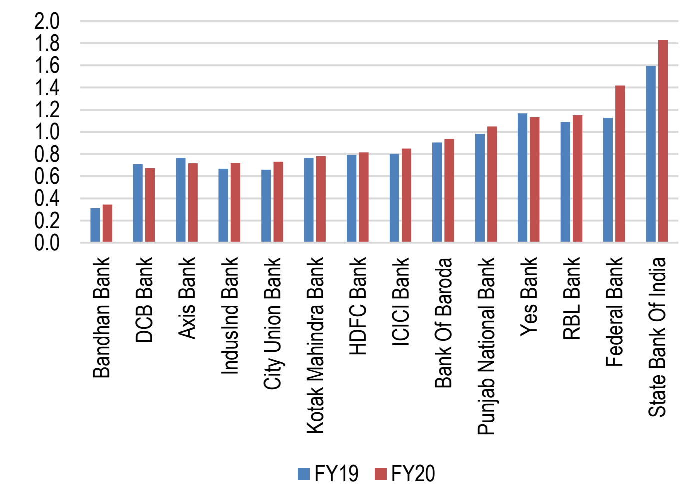
One caveat in case of Bandhan Bank, given the geographical spread of the business, is that majority of its workforce and banking outlets are based in east/north-east where wages and rents are generally lower than other parts of the country. As of Mar-20, east and north-east accounted for 60% of the bank's total banking outlets. As per Knight Frank data, rentals in Kolkata (WB) are 36-68% lower than other metro cities (ex-central India). Also, as a proxy for wage differential across states, per capita income in WB is 20% lower than the national average. Aggressive growth pursuit outside home markets could present material risk to the current opex profile and our cost assumptions.

Exhibit 72: Cost/income (%)



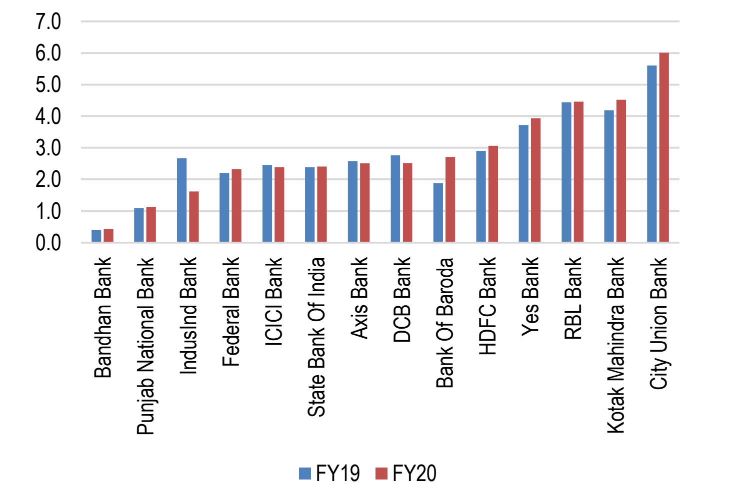
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 73: Employee cost per head (Rsmn)



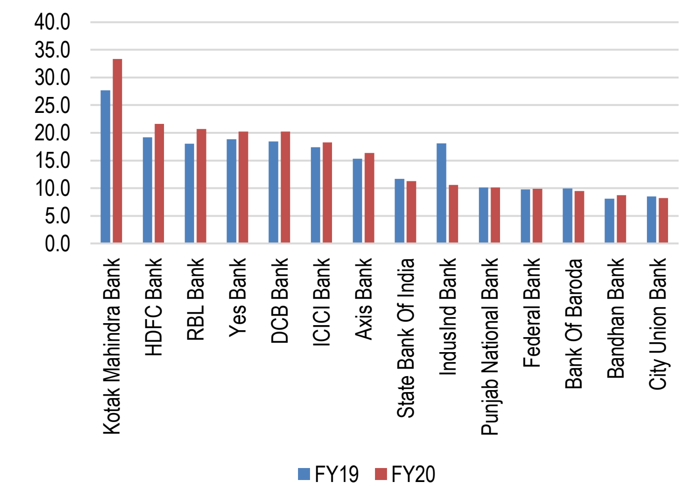
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 74: Rent per banking outlet (Rsmn)



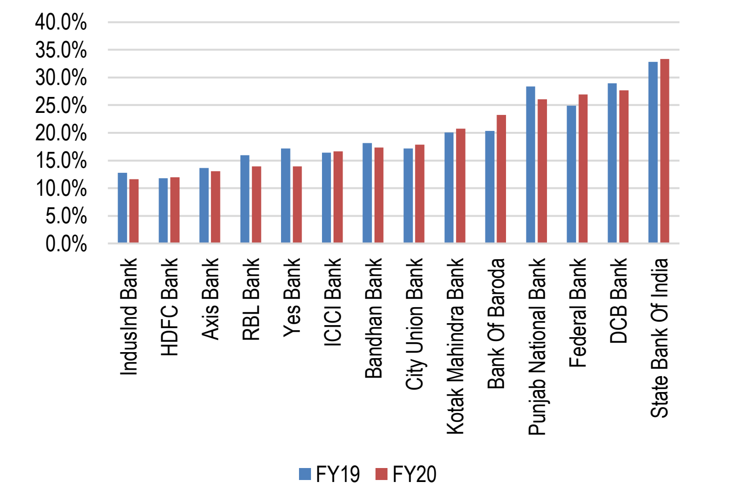
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 75: Employees/banking outlet (nos.)



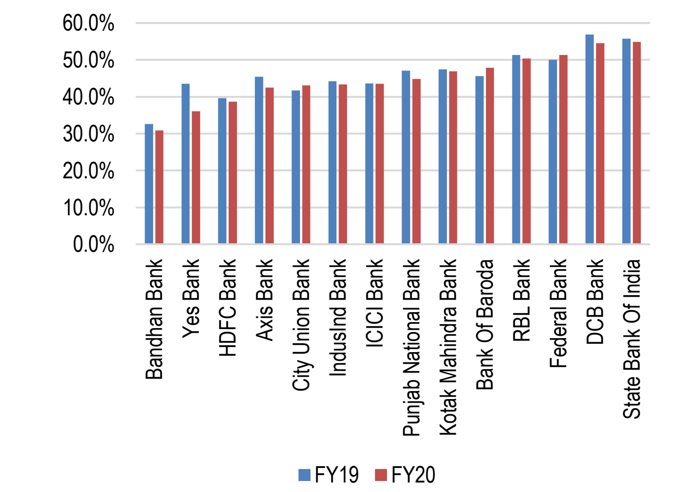
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 76: Employee cost/income (%)



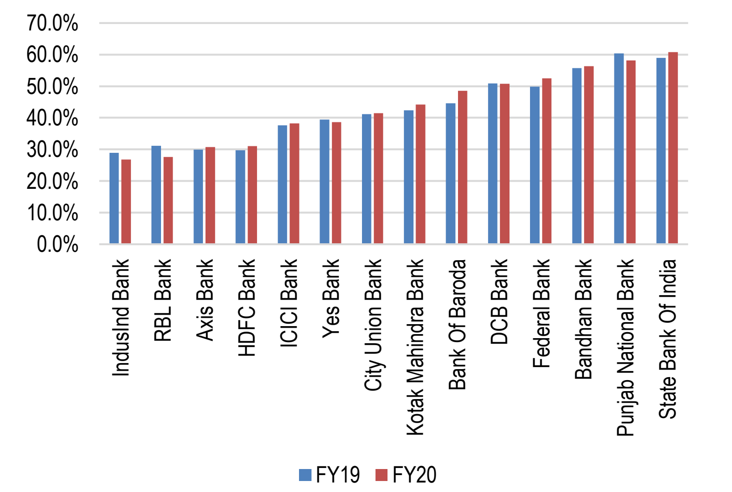
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 77: Overall cost/income (%)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 78: Employee cost as % of total opex

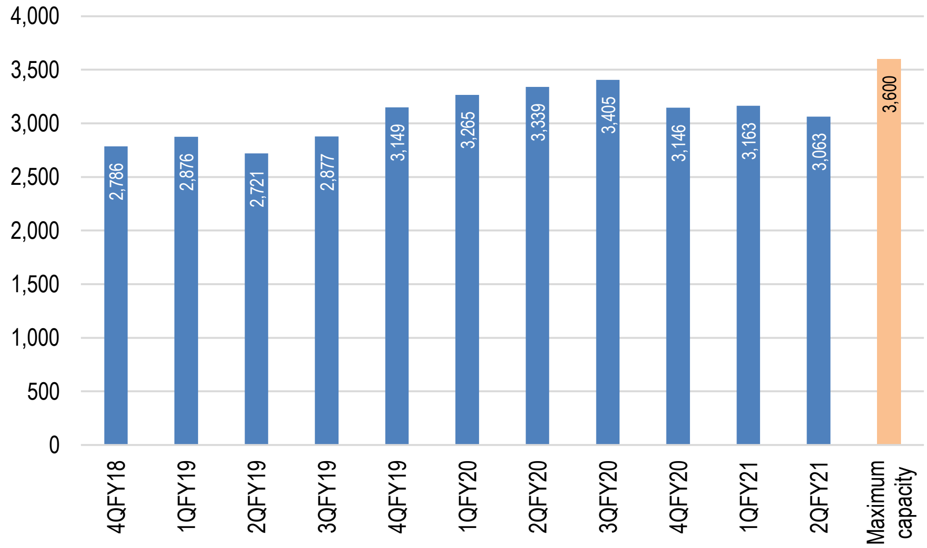


Source: Company, Nirmal Bang Institutional Equities Research

We see scope for improvement in micro-borrowers-per-DSC ratio

In the past, the bank has stated that each DSC has the capacity to handle 3,600 micro-borrowers. Since Mar-20, the bank has added 115 new DSCs (3.2% growth YTD), taking the total DSCs to 3,656 as of Sep-20. We see scope for 17-18% improvement in micro-borrowers-per-DSC ratio given that it stands at 3,063 as of 2QFY21. This would be led by improvement in new customer acquisition, which has been negligible in 1HFY21. Should this scenario materialize, it would lead to downward revision in our cost/income ratio assumptions, implying better-than-expected operational profitability. We are currently building in cost/income ratio of 32% over FY22-23E.

Exhibit 79: No. of active micro-borrowers per DSC

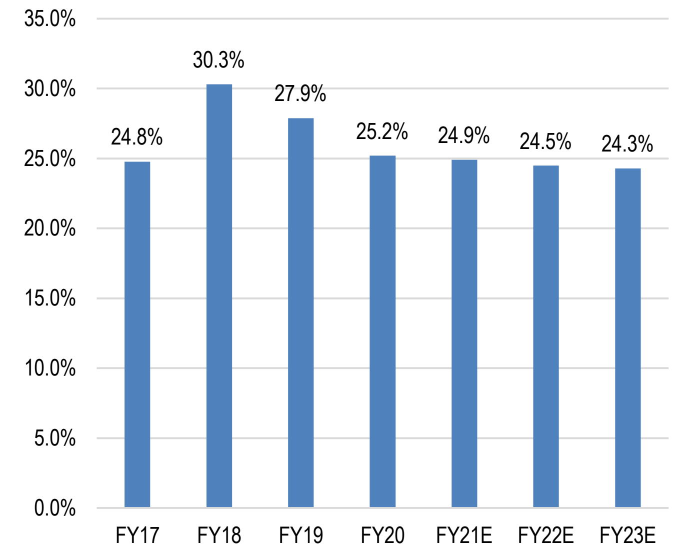


Source: Company, Nirmal Bang Institutional Equities Research

Supernormal ROEs moderate net capital consumption despite high loan growth

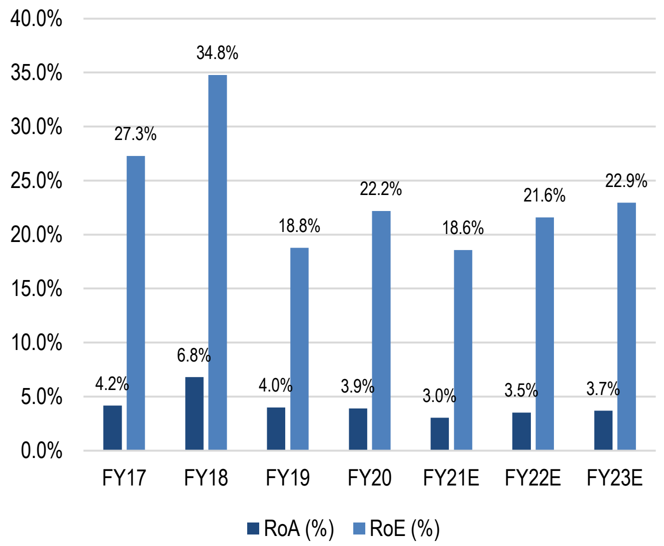
As of 2QFY21, Bandhan Bank had a CRAR of 27.8% (incl. 1HFY21 profit), which we find fairly comfortable given the minimum requirements. Bandhan Bank's CET-1 is highest amongst our banking coverage at 24.3% (Sep-20). Given the supernormal growth in loan book, the growth in RWAs has also been very high. Over FY16-20, loan book has grown at a CAGR of 52.1%. Over the same period, RWAs have grown at a CAGR of 47.7%, but the high ROEs have moderated the net capital consumption. We expect this trend to continue. Given our industry-demand forecast, we expect micro-finance growth for Bandhan Bank to remain higher. Also, we expect the non-micro-finance segments to grow at a higher rate given the management's strategy to reduce the share of micro-finance from current levels (Vision 2025). Against a 20.7% CAGR in loans and 21.9% CAGR in RWAs over FY20-23E, we expect shareholders' funds to grow at 19.7% CAGR supported by sustenance of high ROEs. We expect Bandhan Bank to remain comfortably placed from a capital standpoint.

Exhibit 80: CET- 1 (%)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 81: Profitability ratios (%)



Source: Company, Nirmal Bang Institutional Equities Research

From a stockholder's perspective: can a lower dividend payout and higher reinvestment of profit in a high-ROE business lead to better shareholder value creation?

While the RBI has restricted banks from declaring any dividend for FY20, we are building in a 20% dividend payout going forward. We think that a higher rate of reinvestment of profit (back into Bandhan Bank), implying lower dividend payout, would lead to better shareholder value creation as the bank's current/projected ROEs are in excess of its cost of capital and possibly higher than investors' opportunity cost of capital. While we understand investors' needs for dividend payouts, we are of the view that ploughing back earnings in a 21%+ ROE business makes for a better capital allocation decision that would lead to higher shareholder value creation than otherwise.

Bank is profitable enough to self-sustain

On the basis of our current growth projections and capital consumption patterns, we think that a dividend payout of sub-15% would enable the bank to fuel growth entirely through internal accruals.

Industry-leading profitability

Bandhan Bank has grown its net profit at a CAGR of 39.6% over FY17-20, supported by a high-margin loan book growth and improving cost ratios. The bank makes one of the highest NIMs in the banking sector due to the high share of micro-finance in the overall advances. As of FY20, micro-finance accounted for 64% of the bank's total advances. NII has grown at a 3-year CAGR of 38.1% (FY17-20) while operating profit has grown at 44.8% CAGR over the same period due to better cost control and improving productivity. For instance, the number of active micro-borrowers managed per DSC has improved by ~13% since FY18. Given that a single DSC can handle about 3,600 micro-borrowers, we see room for further improvement. Given the manpower-heavy nature of the business model, the number of employees per banking outlet has also increased from 7.6 in FY18 to 8.7 in FY20 and 9.7 in 2QFY21. The bank's PPOP-to-average total assets ratio is higher than other banks under our coverage universe. Such a strong operational profitability has also provided the bank room to absorb credit costs quite comfortably while ensuring a high ROE.

A host of regulatory factors place Bandhan at an advantage

Bank status, absence of margin cap, low PSL, provisioning and CAR requirement place Bandhan Bank at a competitive advantage compared to NBFC-MFIs.

Key regulatory differences	Banks	NBFC-MFIs
PSL/qualifying assets	Atleast 40% of the ANBC towards priority sector	Not less than 85% of the qualifying assets should be micro-finance loans; loans towards income generation should not be less than 50%
Margin	There is no margin cap	For large MFIs (loan portfolios >Rs1bn), margins cannot exceed 10%; for others, margin cap is 12%.
CRAR	Minimum CAR 9%	Minimum CAR 15%
Provisioning norms	Standard asset provisioning: 0.4%; 15% for secured and 25% for unsecured on recognition of NPA	Atleast 1% of aggregate loans or 50% of loan instalments which are 90+ dpd, whichever is higher

Source: RBI, Nirmal Bang Institutional Equities Research

Different micro-finance lending models

Metrics	JLG	SHG
Group Size	5-10 members	~20 members
Gestation period for loan approval	Upon formation of Groups	Upon demonstrating a savings track record for 3-6 months
Loan sanction and disbursal	Loans sanctioned and disbursed to individual borrowers	Loans sanctioned and disbursed to the SHG; subsequently split among group members.
Borrower identification (KYC)	KYC verification undertaken for all members of the JLG	KYC verification of office bearers mandatory; Not mandatory for other members.
Mandatory savings account	No	Yes; Savings culture is an integral part of the SHG model
In-lending within the group	No	Yes; Group savings can be utilized for lending to SHG members
Repayment frequency	Weekly / Fortnightly / Monthly	Typically monthly

Source: ICRA Research, Spandana Sphoorty RHP

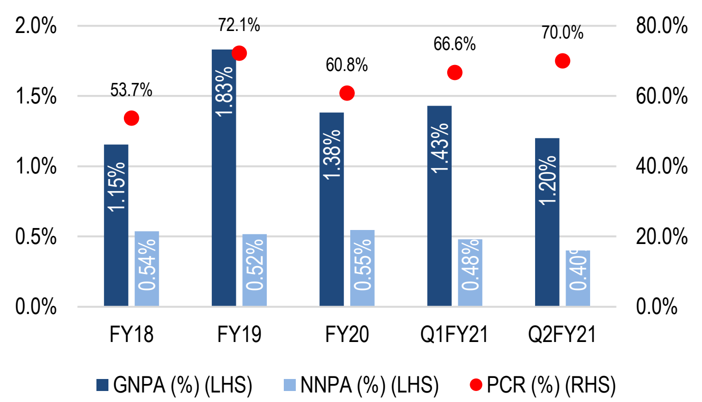
Bandhan Bank's better-than-industry asset quality performance provides comfort

As of 2QFY21, the bank had reported pro-forma GNPA of 1.50% compared to 1.38% as of FY20. Recently, the bank's asset quality has been under pressure due to a variety of reasons. In 3QFY19, the bank had reported an exposure of Rs3.85bn towards NPA-turned IL&FS. Post this recognition, the GNPAs increased by 110bps QoQ to 2.33%. Subsequently, the bank has seen another spurt of slippages in 3QFY20, which led to 29bps QoQ increase in GNPAs, partly because of slippages in the GRUH portfolio. Assam has also been a problem area for the bank recently, where early bucket asset quality and collection trends have seen deterioration owing to the protests. In 2HFY20, Bandhan Bank reported collection efficiency of 93.5-93.6% in Assam. With the onset of covid-induced lockdown and floods, the collection rates in Assam deteriorated further to 61% in 1QFY21 before recovering to 87% in Oct-20. The overall collection efficiency for the bank was on an upward trajectory in 2QFY21. Micro-finance collections (by value) have improved from 68% in 1QFY21 to 89% in 2QFY21 and further to 91% in Oct-20. In terms of number of micro-finance customers, 95% are paying as of Oct-20 compared to 75% in 1QFY21 and 99% in 2QFY21. In the non-micro-finance segments too, the collections have improved to nearly pre-covid levels.

Due to size restrictions on gatherings on account of covid, the bank has added to its on-field manpower strength. Group meetings have been small and collections have been happening mostly door-to-door. As the current situation normalizes, the extra field officers are expected to be absorbed in the normal course of the business as it grows.

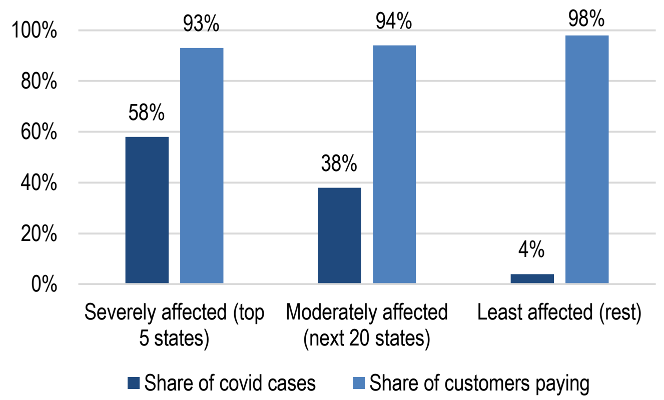
WB, which is the largest exposure state for the bank, reported collections of 90% (by value) and 96% (by customer) in 2QFY21. Complete normalization of local train services, used as transport by micro-borrowers for their commute, will be a positive development. High exposure concentration to WB and Assam can pose significant asset quality risks.

Exhibit 82: Asset quality metrics



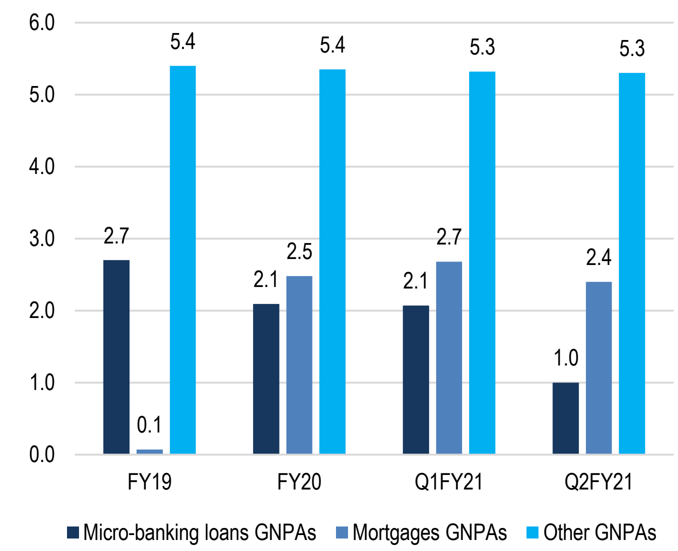
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 83: Collection trends across covid-affected areas for Bandhan



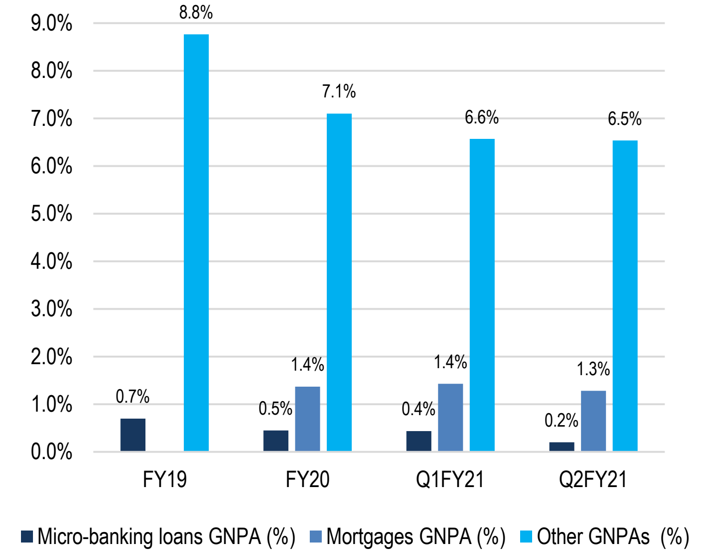
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 84: Segmental asset quality (Rsbn)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 85: Segmental asset quality (%)



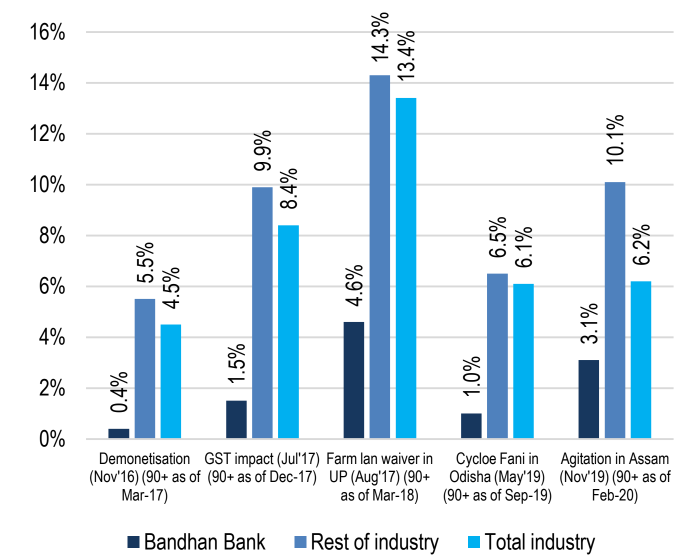
Source: Company, Nirmal Bang Institutional Equities Research

Historical asset quality track record better than industry

Historically, the bank's asset quality (90+ dpd) has held up in a much better shape vis-à-vis peers/overall industry, especially during extremely adverse events. During some of the recent events, which proved to be detrimental to the micro-finance industry's asset quality, Bandhan Bank's 90+ dpd numbers were 50-90% lower than the industry. During demonetisation, Bandhan Bank's early bucket collections reverted to normalcy within 3-4 months. Even in the current situation, Bandhan Bank has reported better-than-industry collections in the micro-finance portfolio.

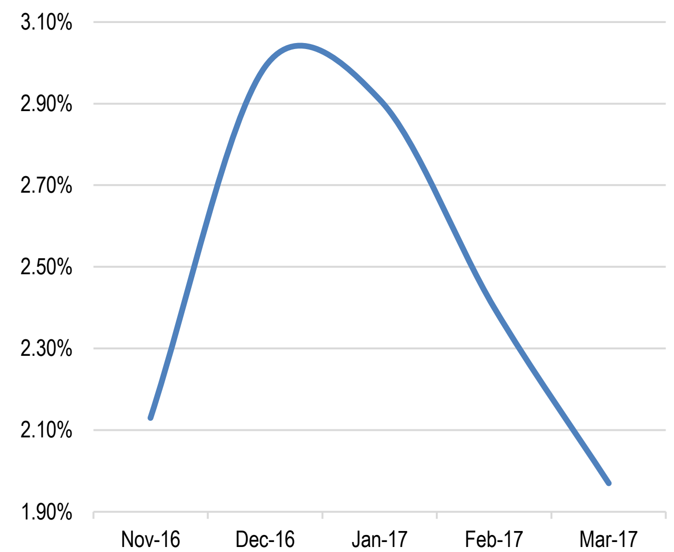
We also understand that in situations where the customers' willingness to repay is impacted (Assam agitation, UP farm loan waiver), the ultimate credit losses have been higher than in cases where the ability is affected due to impact on (customers') businesses.

Exhibit 86: 90+ DPD trends



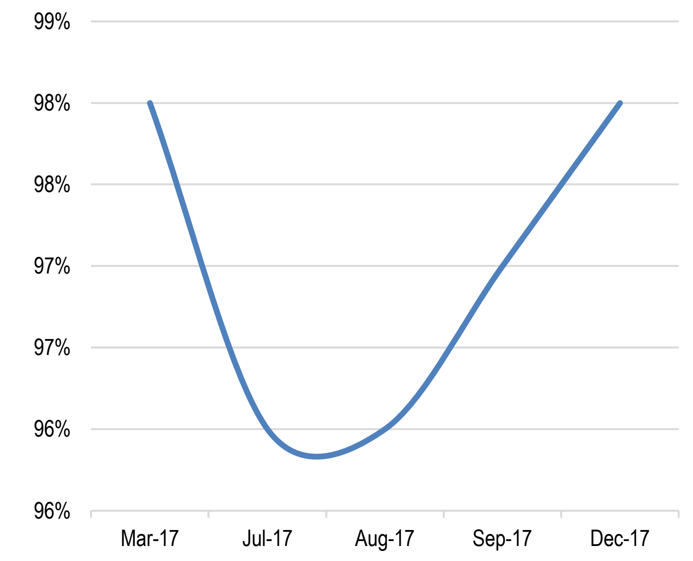
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 87: 7+ days overdue - Asset quality experience during demonetisation – Bandhan improved its delinquency numbers and came back to normalcy in the following 3 months.



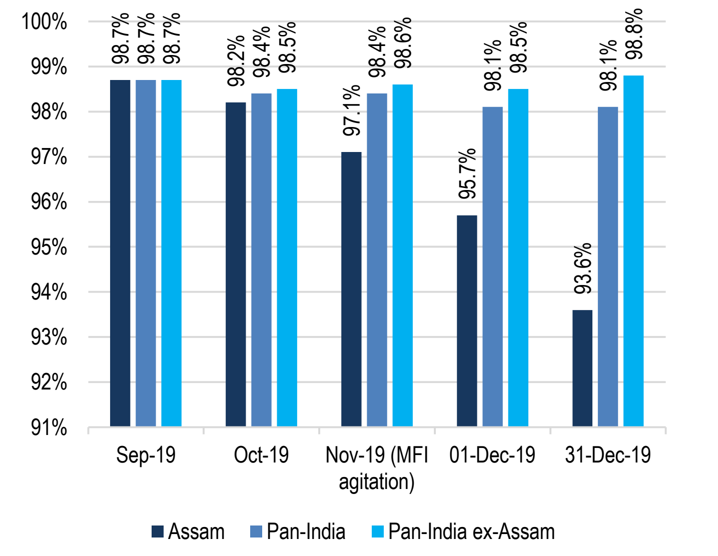
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 88: OTR behaviour during GST implementation



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 89: Bandhan's OTR behaviour during Q3FY20



Source: Company, Nirmal Bang Institutional Equities Research

Collections panning out better than expected

A major concern with regards to covid disruption was the impact on collections and consequently asset quality, which has been panning out better than earlier expected. While the general sense of the market is that borrowers' intent to repay remains intact, localised lockdowns, festivals etc. have hampered collections. As per Bharat Microfinance report FY20, repayments to MFIs dropped to near zero during the lockdown but recovered significantly in Oct-20 with cumulative repayments at 60-70%. Collections for Bandhan Bank in Oct-20 stood at 91% while that for Ujjivan SFB it was at 88%. For other players like Asirvad and Jana SFB, Oct-20 collections stood at 82% and 85%, respectively. Lenders have been quick to innovate and transition themselves towards digital operations due to restrictions on physical collections. For example, Ujjivan has tied up with Airtel Payments Bank for digital collections.

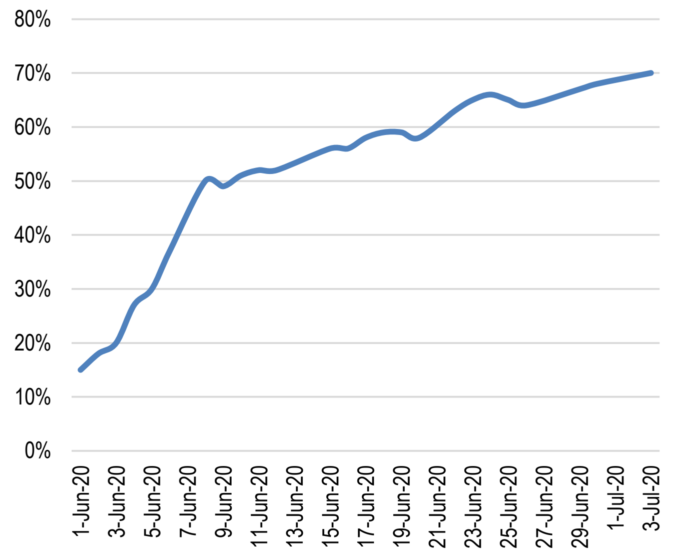
Exhibit 90: Collections data across the MFI industry

Collections data across the MFI industry	1QFY21	2QFY21	3QFY21
Bandhan Bank			
Bandhan Bank - no. of customers making payment (%)	75%	95%	-
Bandhan Bank - monthly collection by value (%)	June: 68%	Sept: 89%	Oct: 91%
Bandhan Bank - monthly collection by customers (%)	June: 67%	Sept: 94%	Oct: 95%
Asirvad Microfinance			
Asirvad - overall collection efficiency (incl. foreclosures) (%)	Apr: 2%, May: 17%, June: 55%	Jul: 69%, Aug: 75%, Sept: 90%	Oct: 90%
Asirvad - collection efficiency (current month billing) (%)	-	Jul: 68%, Aug: 71%, Sept: 82%, Overall: 74%	Oct: 82%
Asirvad - collection efficiency (current month billing + arrears) (%)	-	Jul: 68%, Aug: 71%, Sept: 87%, Overall: 75%	Oct: 87%
Asirvad - state-wise collection efficiency (%)			
Tamil Nadu (22%)	-	Jul: 66%, Aug: 80%, Sept: 95%	Oct: 98%
West Bengal (12%)	-	Jul: 56%, Aug: 61%, Sept: 75%	Oct: 75%
Bihar (10%)	-	Jul: 72%, Aug: 70%, Sept: 92%	Oct: 92%
Karnataka (9%)	-	Jul: 73%, Aug: 86%, Sept: 99%	Oct: 94%
Kerala (6%)	-	Jul: 66%, Aug: 71%, Sept: 91%	Oct: 90%
Madhya Pradesh (6%)	-	Jul: 80%, Aug: 79%, Sept: 89%	Oct: 93%
UP (6%)	-	Jul: 83%, Aug: 89%, Sept: 99%	Oct: 100%
Ujjivan SFB			
Ujjivan SFB - monthly collection efficiency (current month billing) (%)	Jun: 53%	Jul: 60%, Aug: 68%, Sept: 83%	Oct: 88%
Ujjivan SFB - monthly collection efficiency (incl. additional collection) (%)	Jun: 58%	Jul: 67%, Aug: 76%, Sept: 89%	Oct: 93%
IndusInd Bank (BHAFIN) - collection efficiency (%)		Sept: 91%	Oct: 93%
Spandana Spoorthy			
Absolute collections	-	Jul: 73%, Aug: 79%, Sep: 103%	Oct: 110%
Absolute collections (incl. prepayments)	-	Jul: 75%, Aug: 91%, Sep: 124%	Oct: 129%
CreditAccess Grameen			
CreditAccess Grameen - collection efficiency (excl. arrears, incl. morat) (%)	Jun: 74%	Jul: 76%, Aug: 82%, Sept: 88%	-
CreditAccess Grameen - state-wise collection efficiency (%)			
Karnataka	Jun: 78%	Jul: 78%, Aug: 86%, Sept: 91%	-
Maharashtra	Jun: 62%	Jul: 65%, Aug: 72%, Sept: 80%	-
Tamil Nadu	Jun: 75%	Jul: 79%, Aug: 86%, Sept: 94%	-
Madhya Pradesh	Jun: 81%	Jul: 88%, Aug: 88%, Sept: 91%	-
Madura Microfinance - collection efficiency (excl. arrears, incl. morat) (%)	Jun: 54%	Jul: 64%, Aug: 75%, Sept: 83%	-
Madura Microfinance - state-wise collection efficiency (%)			
Tamil Nadu	Jun: 54%	Jul: 66%, Aug: 77%, Sept: 83%	-
Maharashtra	Jun: 45%	Jul: 56%, Aug: 72%, Sept: 76%	-
Odisha	Jun: 43%	Jul: 43%, Aug: 63%, Sept: 81%	-
Bihar	Jun: 66%	Jul: 75%, Aug: 71%, Sept: 86%	-
Jana SFB - collection efficiency (%)	-	-	Oct: 85%

Source: Company, Nirmal Bang Institutional Equities Research

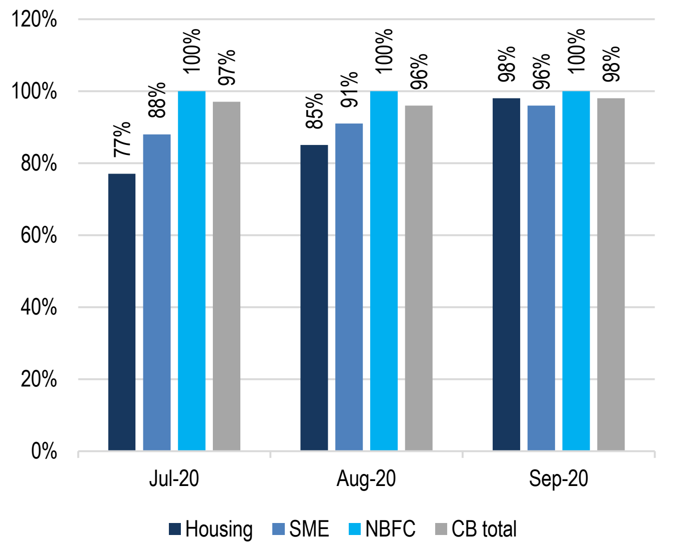
Collections across segments are up since Q1FY21 and are improving further

Exhibit 91: Daily collection efficiency for Jun-20



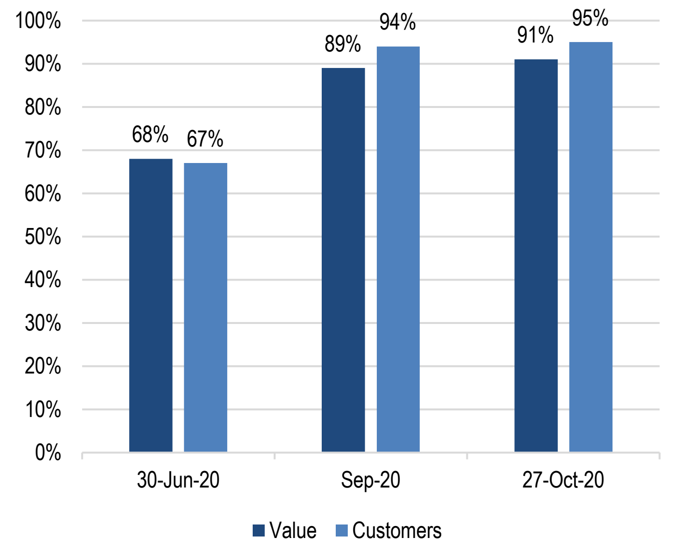
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 92: Collection trends in non-MFI segments



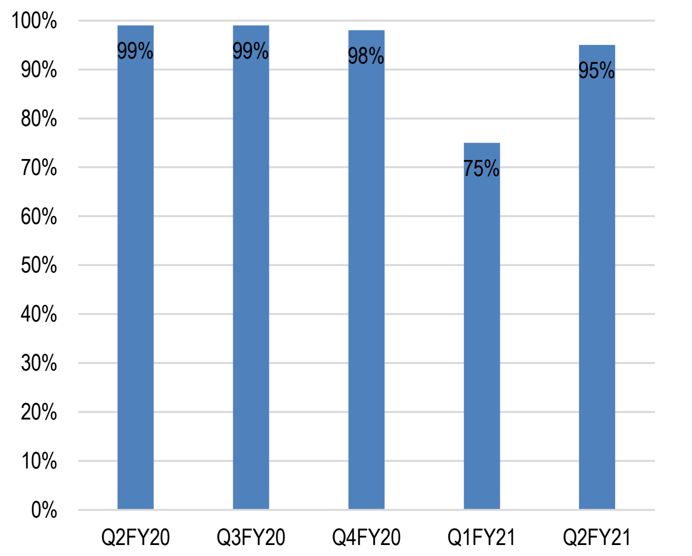
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 93: Micro-banking collection efficiency (excl. arrears)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 94: Proportion of micro-customers making payment



Source: Company, Nirmal Bang Institutional Equities Research

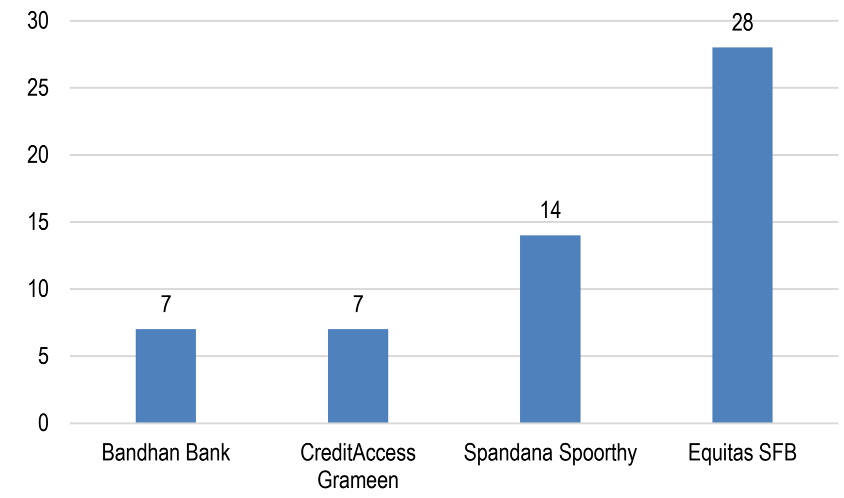
Moderation in credit cost FY22E onwards a major ROE driver

We note that credit cost in FY19 and FY20 was on the higher side due to one-off provisioning on account of IL&FS (Rs3.85bn), Assam agitation/protests and Covid-19. For FY21E, we are estimating credit cost of 3.62%. In 1HFY21, the bank has already made cumulative provisions of Rs12.4bn (90% of FY20 provisions) on account of covid. Given that micro-finance collections are now inching towards normalcy and in the absence of any large-ticket/corporate NPAs or state-specific agitations (such as in Assam), we believe that the bank's balance sheet is sufficiently provided for in terms of addressing the asset quality impact due to covid-19. The bank currently holds ~3% of advances in the form of non-NPA provisions. We expect credit cost to trend down FY22E onwards, which will be a major driver of ROE improvement. For FY21E, the bank's own credit cost guidance is 3.5%. Bank's expectation of steady state credit cost is 1-1.25%.

Higher customer engagement a key reason for better asset quality

Bandhan Bank follows a 7-day collection cycle, which means that the bank officer meets customers 52 times in a year. Compared to peers (Spandana and Equitas), Bandhan Bank's collection cycle indicates a higher degree/frequency of customer engagement. We believe this plays out favorably from an asset quality standpoint. A shorter EMI-collection cycle not only ensures more frequent interaction and relationship building opportunity with the customers but also helps the bank to monitor the repayment behaviour and credit default risk more closely. More frequent interactions reduce the chances of information asymmetry, especially in cases of adverse developments (at the borrowers' end). For CreditAccess Grameen, majority of the customers are on a 7-day collection policy. We also understand that Spandana used to follow a monthly collection model earlier.

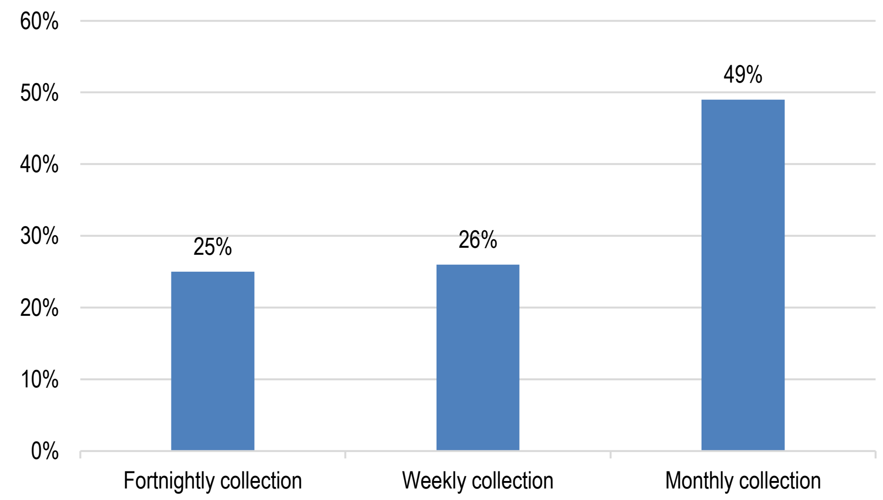
Exhibit 95: Collection policy (days) - shorter is better



Source: Company, Nirmal Bang Institutional Equities Research

Industry wide, nearly half of the loans are collected on a monthly basis (least preferred mode in our view) whereas weekly collections are 26%. Given this data, coupled with Bandhan Bank's strong asset quality performance relative to the broader MFI space, we believe that the bank's collection policies and systems are superior.

Exhibit 96: GLP composition in terms of collection mode (%) (FY20)



Source: Company, Nirmal Bang Institutional Equities Research

Loan appraisal process

Microloans

For microloans, bank's doorstep banking officers (DBOs) source loan applications, conduct the primary appraisal and customer visits and make loan recommendations to the head of the applicable DSC. The head of the DSC then visits the customer's house and checks the details entered in the loan applications and, if satisfied, sanctions the loan. The appraisal criteria for microloans are primarily qualitative, and include factors such as customer profile, age, current enterprise, income, surplus income and Credit Bureau report on past performance.

Retail loans

Personal loans are sourced by branch officials and are sanctioned by respective branch heads. Other retail loans are sourced by dedicated relationship managers, with loans up to Rs1mn sanctioned by the credit team and loans above Rs1mnn sanctioned by credit committees at the head office. Bank follows standard loan application and appraisal formats covering both qualitative as well as quantitative parameters.

SME loans

Bank sources SME loan proposals through bank branches and SME hubs, which are hubs with dedicated relationship managers that have been created within select branches with potential for SME business. The SME hubs also house SME credit managers who assess the creditworthiness of business proposals. This is to ensure close client interaction and timely service to customers. The appraisal is carried out by the credit team and sanctioning of all loans under SME is centralized and sanctioned by designated head office credit committees. There is a separate credit operations department to monitor and control post-sanction documentation and operations.

Small enterprise loans

Bank has a dedicated team of relationship managers who source and service the customers. The credit team for small enterprise loans has sanctioning powers and is independent of the small enterprise loan sourcing team. Bank uses a combined application-cum-appraisal form, with due diligence carried out by the credit managers based on the qualitative information available.

Brief on AP micro-finance crisis

In FY10, Andhra Pradesh was the largest MFI market with a share of ~28% (loans outstanding) and ~23% (client outreach). After multiple suicides by farmers due to pressure from MFI collection agents, the AP government, in Oct-10, passed the AP Microfinance Ordinance to put in place extremely strict operating guidelines. This resulted in a sharp drop in collection efficiencies of the AP based MFI portfolios (from ~99% to almost nil). This affected AP-based MFIs severely and out of the 7 MFIs with high concentration in AP, 6 were admitted to CDR. This resulted in a domino effect adversely affecting not just AP focussed MFIs, but other MFIs as well. AP focussed MFIs were affected due to adverse collection rates and other MFIs were impacted due to lack of fresh credit lines. The crisis led to a drop in investor confidence on the sector.

Bandhan Bank's ownership dilution

Bandhan Bank's IPO in Mar-18 resulted in Bandhan Financial Holding Limited's (BFHL) shareholding reducing to 82.28%. By regulation, BFHL was required to reduce its share to 40% by Aug-18. However, being unable to do so, the RBI, in Sep-18, froze the remuneration of MD and CEO Mr. Chandra Shekhar Ghosh and halted the bank's branch expansion. In Oct-19, post the successful merger with GRUH Finance, promoter shareholding in Bandhan Bank was brought down to 61%. This merger not only helped to address the stake dilution issue but also helped Bandhan Bank pursue high quality diversification. The second stage of stake dilution happened more recently (Aug-20) when Bandhan Bank's promoter entity sold its stake via block trade, which brought down promoter ownership to 40%. Going forward, as per regulatory guidelines, Bandhan Bank needs to further reduce promoter share to 15% by Aug-27 (12 years from commencement of operations). Despite the IWG's recommendations providing for relaxation of long-term ownership stakes in banks and collapse of NOFHCs (wherein banking is the only business), Bandhan Bank is likely to continue with the holdco structure given that it wants to be a full-service institution, providing customers other financial products such as insurance and mutual funds. We believe that the current holdco structure would be best suited in order to pursue a para-banking strategy. The bank plans to take the subsidiary route for its proposed insurance and mutual fund foray.

Key modelling assumptions

Bandhan Bank Ltd. - Key assumptions	FY21E	FY22E	FY23E
Growth in active micro borrowers (yoy, %)	13.5%	10.0%	10.0%
Growth in loan o/s per micro-borrower (yoy, %)	12.0%	7.0%	7.0%
Growth in non-micro-banking loans (ex-Gruh/housing) (yoy, %)	20.0%	35.0%	35.0%
Growth in Gruh Finance / housing portfolio (yoy, %)	5.0%	30.0%	30.0%
Investment-to-deposit ratio (%)	27.0%	26.0%	25.0%
CA deposits growth (yoy, %)	15.0%	15.0%	15.0%
SA deposits growth (yoy, %)	35.0%	32.0%	30.0%
TD growth (yoy, %)	23.0%	23.0%	20.0%
Yield on micro loans (%)	16.9%	16.8%	16.7%
Yield on housing loans (%)	10.0%	9.9%	9.8%
Yield on other loans (%)	8.0%	7.9%	7.9%
Yield on investments (%)	5.5%	5.5%	5.5%
Yield on cash/bank balances (%)	6.5%	6.5%	6.5%
Cost of deposits (%)	5.5%	5.5%	5.5%
Cost of funds (%)	6.2%	6.1%	6.1%
NIM (%)	8.0%	8.0%	7.8%
Employee cost/income (%)	17.5%	17.5%	17.5%
Non-employee cost/income (%)	13.0%	14.5%	14.5%
Credit costs (%)	3.6%	2.5%	2.0%
GNPAs (%)	2.9%	3.2%	3.0%
NNPAs (%)	1.4%	1.3%	1.1%
PCR (%)	52.8%	61.3%	63.6%
Micro-finance credit RWA density (%)	82.6%	82.6%	82.6%
Housing finance/mortgages credit RWA density (%)	56.7%	56.7%	56.7%
Non-micro, non-housing loans credit RWA density (%)	60.0%	60.0%	60.0%

What will drive shareholder value and stock returns?

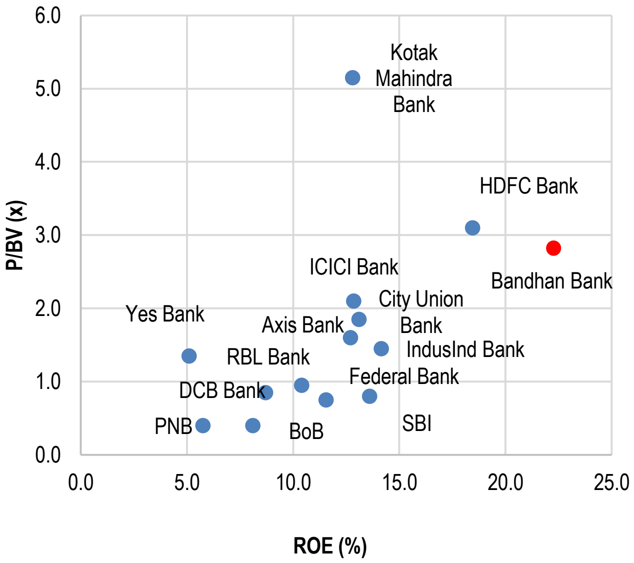
Returns in excess of bank's cost of capital as well as investors' opportunity cost

We expect Bandhan Bank to deliver ROE of nearly 19% in FY21, weighed down by higher credit cost in the near term due to covid-impact. We note that ROEs in FY19 and FY20 were affected due to one-off provisioning on account of IL&FS (Rs3.85bn), Assam agitation/protests and Covid-19. Given that micro-finance collections are now inching towards normalcy and the bank is sufficiently provided for and in absence of any large-ticket/corporate NPAs or state-specific agitations (such as in Assam), we forecast the bank to deliver ROEs of 22-23% over the medium-to-long-term.

At CMP, the business is yielding 8% at 1x 1HFY23E BV – better risk/reward than most frontline banks

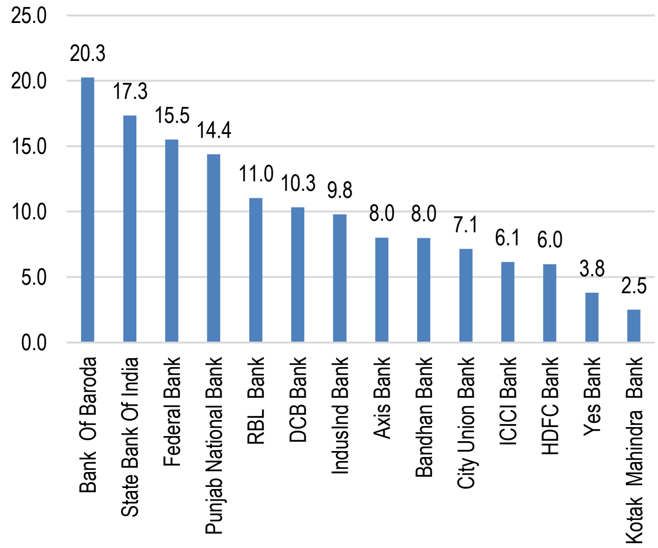
In our view, Bandhan Bank is one of the few banks which provide high degree of overall growth and earnings visibility. This comfort comes partially from the bank's track record and its performance vis-à-vis peers. What strongly adds to our 'visibility' thesis is the specialized nature of the business, i.e., micro-finance. The bank commands 20% market share in an industry where growth headroom is still plentiful given the current penetration levels (in terms of credit as well as population, especially east/north east India).

Exhibit 97: RoE and valuation scatter plot



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 98: Bandhan is yielding 8% at 1x 1HFY23E BV



Source: Company, Nirmal Bang Institutional Equities Research

Among the very few which can self-sustain

One of the key requirements for continuous growth in the lending space is the constant need for capital and especially so when growth rates are high (for example: Yes Bank, RBL Bank, Bajaj Finance). This comes with the risk of dilution for existing shareholders, especially when the stock is trading cheap. Given Bandhan Bank's business model, market positioning and profitability forecasts, we are of the view that the bank can rely solely on internal accruals to satisfy its capital requirements. There are only a handful of lenders in the Indian market which can boast of such a business characteristic.

From a stockholder's perspective: can a lower dividend payout and higher reinvestment of profit in a high-ROE business lead to better shareholder value creation?

While the RBI has restricted banks from declaring any dividend for FY20, we are building in a 20% dividend payout going forward. We think that a higher rate of reinvestment of profit (back into Bandhan Bank), implying lower dividend payout, would lead to better shareholder value creation as the bank's current/projected ROEs are in excess of its cost of capital and possibly higher than investors' opportunity cost of capital. While we understand investors' needs for dividend payouts, we are of the view that ploughing back earnings in a 21%+ ROE business makes for a better capital allocation decision that would lead to higher shareholder value creation than otherwise.

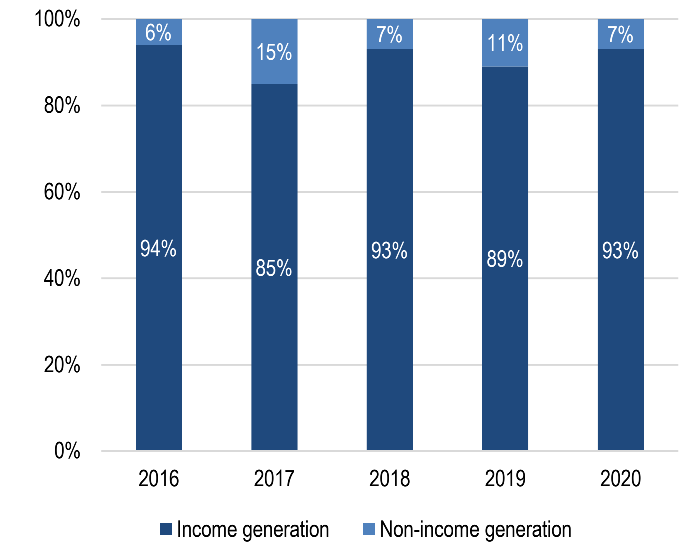
Bank is profitable enough to self-sustain

On the basis of our current growth projections and capital consumption patterns, we think that a dividend payout of sub-15% would enable the bank to fuel growth entirely through internal accruals.

The ESG perspective in investing

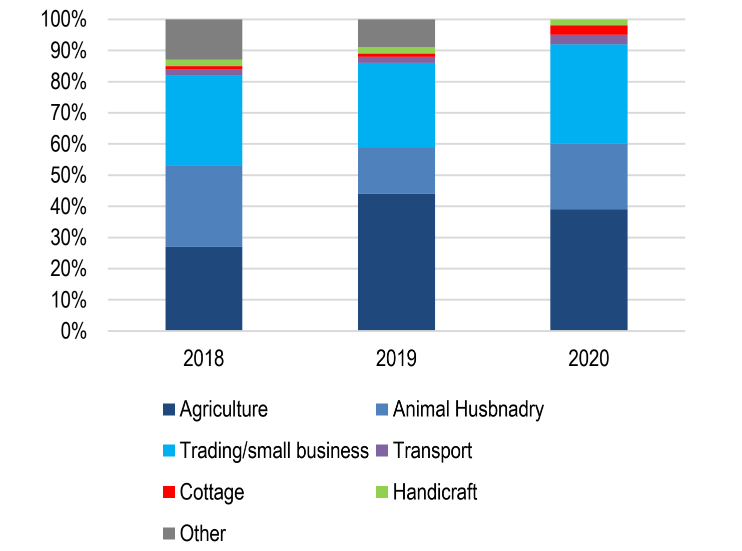
Micro-finance serves a social purpose: The main goal of micro-finance is to help the backward sections of the society to improve their financial situation (financial inclusion). Given this, we believe that the micro-finance industry serves a very important social purpose. In FY20, 98% of the micro-finance borrowers (through Sa-dhan network) were women. Majority of the loans (93%) were for income generation purposes. Even within the non-income generation segment, housing and education together constituted 72% of the end-use while consumption was only 9%.

Exhibit 99: Purpose of loan (by % share) - MFI loans are mostly meant for income generation Share of various income generation activities (%)



Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

Exhibit 100: Share of various income generation activities (%)



Source: Bharat Microfinance Report 2020, Nirmal Bang Institutional Equities Research

Exhibit 101: Bandhan's borrower profile is largely from industries which are resilient to the COVID 19 environment

In ₹ MN	Business Category	Micro Banking	Non Micro Banking	Total Advances	% of Total Advances
Resilient	Agriculture & Allied Activities	206,120	909	207,029	28.8%
	Affordable Housing	191	185,002	185,193	25.8%
	Food Processing & Retail	138,504	9,848	148,352	20.6%
	Personal & Healthcare	1,234	17,432	18,666	2.6%
	Rural Transportation (bullock carts / cycle)	11,701	-	11,701	1.6%
	Pharma and Medical	909	1,267	2,176	0.3%
	Computer, Cable / DTH Service Providers	379	21	400	0.1%
	Education	-	335	335	0.05%
	Chemicals	-	257	257	0.04%
	Total	359,039	215,070	574,109	80%
Low Impact	Manufacturing – Non-Essential	67,074	3,809	70,883	9.9%
	Financial Services (NBFCs ;NBFC-MFIs)	1,160	35,430	36,590	5.1%
	Wood / Metal Furniture , Building Material	9,111	-	9,111	1.3%
	Total	77,345	39,239	116,584	16%
Marginal Impact	Other Transportation	14,215	1,226	15,441	2.1%
	Wellness & Beauty Parlour	10,971	511	11,482	1.6%
	Logistics & Courier	322	387	709	0.1%
	Others- Services	-	133	133	0.02%
	Total	25,508	2,256	27,764	4%
	Total Portfolio	461,892	256,565	718,457	100%

Source: Company, Nirmal Bang Institutional Equities Research

Key risks

Geographic concentration: >40% of Bandhan Bank's business comes from WB. Any major adverse development or disruption in the state could have negative implications for Bandhan Bank.

Higher sensitivity to political commentary & campaigns and natural calamities: Over the years, farm loan waivers, which have become more frequent, have started to have knee-jerk reaction on micro-borrowers. The repayment culture in the micro-finance industry has become highly sensitive to political commentary (especially regarding poor/backward classes). Going forward, we expect such political announcements to recur but the asset quality impact will be short-lived. We also believe that large natural calamities tend to impact micro-borrowers more.

Non-MFI not seasoned enough: Bandhan Bank has articulated its vision to increase the share of non-micro-finance considerably by 2025. We have known Bandhan Bank for its dominance in the micro-finance industry. Foraying into untested waters (housing, SME, personal/retail loans) could prove to be disastrous if not executed properly (especially underwriting).

Deposit stickiness: Bandhan Bank currently offers higher rates than frontline large banks as a key strategy to acquire the liability business. Any reduction in deposit rates may lead to outflows.

Growth opex can hurt outside home markets: Bandhan Bank's current cost ratios are low due to majority of the business coming from east/NE. Aggressive growth in non-east/NE India, where costs are higher, could hurt cost ratios.

Key risk to profit forecast is credit cost: Higher than expected NPAs would result in higher credit cost, impacting profitability.

Management profile

Executives	Designation	Comments
Chandra Shekhar Ghosh	MD & CEO	Founder of BFSL, has 27 years of experience in the field of microfinance and development; awarded 'Entrepreneur of the Year' by Forbes and ET in 2014
Sudhin Bhagwandas Choksey	Head, Housing Finance	35+ years' experience in financial industry; previously served as Managing Director at GRUH Finance Limited.
Deepankar Bose	Head, Corporate Centre	36+ years' experience in banking industry; previously served as Chief General Manager and Head Of Wealth Management business, at SBI
Sanjeev Naryani	Head , Business	32+ years of experience in banking Industry; previously worked as Chief General Manager and Head of Real Estate and Housing Business Unit at SBI
Sunil Samdani	Chief Financial Officer	20+ years of experience in financial industry; previously served as Head of Business Analytics and Strategy at Development Credit Bank and as CFO at Karvy
Santanu Banerjee	Head, HR	27+ years of experience in the field of banking and finance; previously worked as Head of HR Business Relationship at Axis bank
Indranil Banerjee	Company Secretary	20+ years' experience in financial industry; previously served as Company Secretary at Energy Development Company
Biswajit Das	Chief Risk Officer	28 years of experience in banking industry; previously served as Head-RBS and regulatory reporting at ICICI Bank
Siddhartha Sanyal	Chief Economist and Head Research	20+ years of experience in the field of Macro Economic; previously served as Director and Chief India Economist at Barclays Bank PLC.
Nand Kumar Singh	Head, Banking Operations and Customer Services	27+ years' experience in banking industry; previously served as Retail Banking Head, Patna Circle, at Axis Bank
Kumar Ashish	Head , Emerging Entrepreneurs Business	26+ years' experience in the field of Banking and Finance; previously served as North Zone Head of ICICI Bank and as Group Director at Airtel Money.
Srinivasan Balachander	Chief Compliance Officer	20+ years' experience in banking industry; previously served as Chief Compliance Officer at Axis Bank Ltd.
Arvind Kanagasabai	Head, Treasury	30+ years of experience at a PSU Bank; previously served as CFO at SBI DFHI Limited, Mumbai
Rahul Dhanesh Parikh	Chief Marketing & Digital Officer	20+ years' experience in Financial Industry; previously served as Chief Executive Officer at Bajaj Capital Ltd.

Source: Company, Nirmal Bang Institutional Equities Research

Board profile

Executives	Designation	Comments
Dr. Anup Kumar Sinha	Non-executive Chairman	Economist with Ph.D from University of Southern California Served as Professor of Economics at IIM Calcutta for 25 years
Chandra Shekhar Ghosh	MD & CEO	Has significant experience in the field of microfinance Awarded 'Outstanding Leadership Award' by Dhaka University Having more than 30 years of experience in microfinance & development terrain
Bhaskar Sen	Director	Retired as Chairman & MD of United Bank of India Previously, Executive Director of Dena Bank Having significant experience in Banking.
Snehomoy Bhattacharya	Director	Significant experience in public and private banking sector Previously worked as Executive Director – Corporate Affairs Axis Bank
Sisir Kumar Chakrabarti	Director	Significant experience in public and private banking sector Previously worked as Executive Director – Corporate Affairs Axis Bank
T. S. Raji Gain	Director	Significant experience in the field of agricultural and rural development, Previously, she has worked with BIRD Currently, CCM & State in Charge – MP - NABARD
Ranodeb Roy	Non-Executive Director	Founder of RV Capital Management Private Limited, Singapore, he was earlier heading Fixed Income Asia Pacific in Morgan Stanley Asia) Singapore
Santanu Mukherjee	Director	Significant experience in Banking at various capacities in SBI Group Former MD of State Bank of Hyderabad
Dr. A S Ramasastri	Director	Director, Institute for Development & Research of Banking Technology; Chairman of IFTAS; company promoted by IDRBT to provide technology services in Banking & financial sectors
Harun Rashid Khan	Director	Retired as Deputy Governor of Reserve Bank of India Instrumental in formulation of Payments system Vision 2018 of RBI
Dr. Holger Dirk Michaelis	Nominee Director	Significant experience in private equity and as strategic advisor to financial services companies Currently, he is working with GIC
Vijay N Bhatt	Director	Significant experience in accounting, audit and assurance Former Sr. Independent Director of BSR & Co., Chartered Accountants
N V P Tendulkar	Director	Significant experience in finance, accounts and management Former Whole time Director – Finance of Hewlett Packard (India)

Source: Company, Nirmal Bang Institutional Equities Research

About Bandhan Bank

Bandhan Bank was incorporated on 23rd December 2014 and began operations on 23rd August 2015 when Bandhan Financial Services Limited, the ultimate parent company, transferred its entire microfinance business to Bandhan Bank. The institution started its journey as Bandhan Konnagar in 2001 as an NGO providing microfinance services to socially and economically disadvantaged women in rural West Bengal. Bandhan Bank received its banking license from the RBI on 17th June 2015. The bank is primarily focused on serving the underbanked and underpenetrated markets in India. Its strength lies in microfinance (65% of advances) which it conducts through a network of 3,656 DSCs. Bandhan currently has 11.2mn active micro-borrowers (Sep-20). Along with microfinance, the bank has also focused on creating strong general banking business. As of Sep-20, the bank had 5.05mn general banking customers and 1,045 general banking branches.

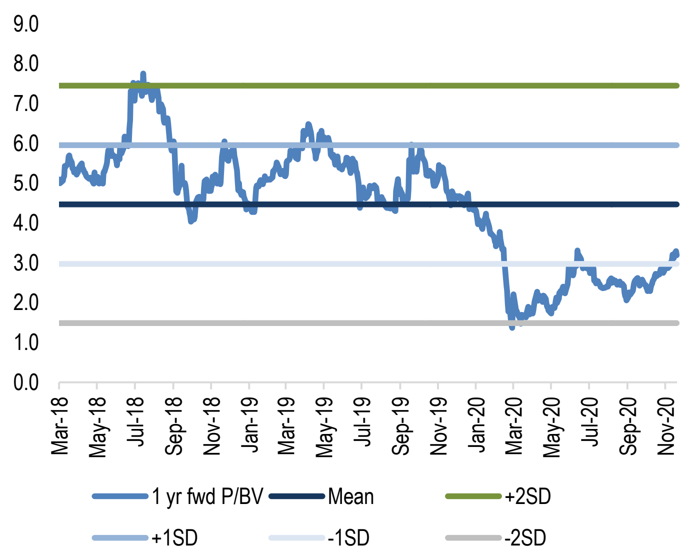
Top 20 investors' shareholding	%
BFHL (Promoter)	40.0
HDFC Ltd	9.9
Caladium Investments	7.8
BlackRock	2.5
Societe Generale	2.2
LIC of India	1.9
SBI Funds Management	1.9
Vanguard Group	1.7
BNP Paribas SA	1.5
International Finance Corp	1.3
Societe Generale SA	1.0
Amansa Holdings	1.02
Nomura Holdings Inc	0.88
Aditya Birla Sun Life AMC	0.8
Kotak Mahindra AMC	0.5
Touchstone Advisors Inc	0.47
Nippon Life India AMC	0.46
Credit Agricole Group	0.44
ICICI Prudential AMC	0.41
Standard Life Aberdeen PLC	0.37

Source: Bloomberg, Nirmal Bang Institutional Equities Research

Outlook and valuation

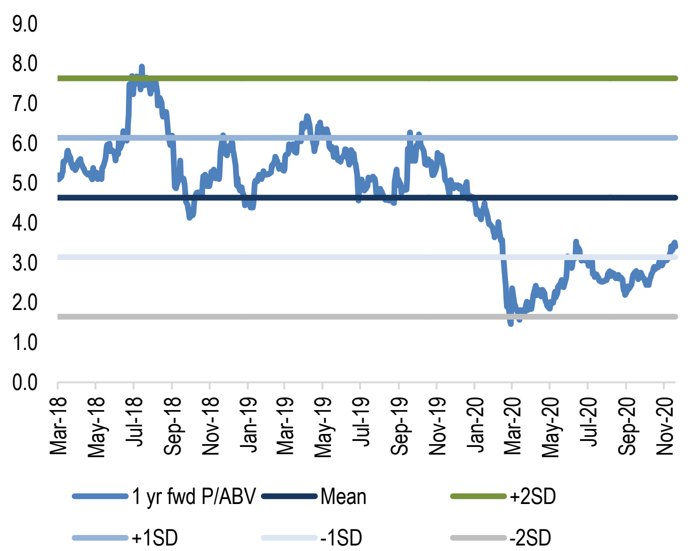
Bandhan Bank enjoys a dominant position in the Indian micro-finance industry. The bank has an overall industry market share of 20% (FY20) and a banking sector micro-finance market share of 50% (FY20). The bank has grown its loans at a CAGR of 30% over FY17-20, backed by very high-quality and granular growth in deposits. We expect industry-level micro-finance portfolio to grow at 15% CAGR over the next five years (FY21-26E) on the back of increasing target market penetration. We believe that the micro-finance industry has enormous room to grow. Having maintained 20% market share over the last 4 years, we believe that Bandhan Bank is strongly positioned to gain from this structural story. Post the GRUH merger, housing finance is also expected to contribute to overall growth strongly along with retail/personal and SME loans. While micro-finance is expected to continue on the strong growth trajectory for the bank, we expect the non-micro-finance segments to grow at a higher rate given the management's vision 2025. We expect overall advances to grow at ~21% CAGR over FY20-23E. The fact that public sector banks still hold ~70% of West Bengal's deposits provides huge opportunity for Bandhan Bank to gain further market share, which currently stands at 3%, especially given that the bank is offering higher deposit rates than most of the frontline large banks. The higher-rate strategy, even if it continues for longer, is not concerning given that the high-margins on the asset side shall be able to accommodate it. The bank has done a commendable job in terms of improving the opex ratios. Over FY17-20, the cost/income ratio has improved from 36.3% to 30.8%. As of 2QFY21, the cost/income ratio stood at 29.4%. A large part of the cost structure improvement has come through the non-staff line items. For instance, rent/income ratio has declined from 3.4% in FY17 to 2.5% in FY20 and rent per banking outlet for Bandhan Bank is 63% lower than the second-lowest bank in our coverage. In terms of the banking outlet infrastructure, Bandhan Bank's cost metrics are superior to peers. We also see scope for 17-18% improvement in micro-borrowers-per-DSC ratio, which currently stands at 3,063 as of 2QFY21. We are building in cost/income ratio of 32%. Given that micro-finance collections are now inching towards normalcy and in absence of any large-ticket/corporate NPAs or state-specific agitations (such as in Assam), we believe that the bank's balance sheet is sufficiently provided for in terms of addressing the asset quality impact due to Covid-19. We expect credit cost to trend downwards FY22E onwards, which will be a major driver of ROE improvement. Overall, we expect the bank to deliver an ROE of 18.6-22.9% over FY21-23E. In our view, Bandhan Bank is one of the few banks which provide a high degree of overall growth and earnings visibility. This comfort comes partially from the bank's track record and its performance vis-à-vis peers. What strongly adds to our 'visibility' thesis is the specialized nature of the business, i.e., micro-finance. The bank commands 20% market share in an industry where growth headroom is still plentiful as mentioned earlier. We value the stock at Rs490, based on 3.5x 1HFY23E ABV and initiate with a BUY rating.

Exhibit 102: P/BV (1-year forward)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 103: P/ABV (1-year forward)



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 104: Income statement

Y/E March (Rsmn)	FY19	FY20	FY21E	FY22E	FY23E
Interest Income	66,434	1,08,855	1,29,743	1,56,970	1,88,847
Interest expense	21,480	45,616	50,219	60,444	73,825
Net interest income	**44,954**	**63,239**	**79,523**	**96,526**	**1,15,023**
Non-interest income	10,630	15,492	17,226	20,326	23,985
Net Revenue	55,585	78,731	96,749	1,16,852	1,39,007
Operating Expense	18,103	24,265	29,508	37,393	44,482
Operating profit	**37,482**	**54,466**	**67,240**	**79,459**	**94,525**
Provisions	7,351	13,932	26,265	21,633	21,028
PBT	30,131	40,534	40,975	57,826	73,497
Taxes	10,616	10,297	10,408	14,688	18,668
PAT	**19,515**	**30,237**	**30,568**	**43,138**	**54,828**

Exhibit 106: Balance sheet

Y/E March (Rsmn)	FY19	FY20	FY21E	FY22E	FY23E
Share capital	11,931	16,102	16,104	16,104	16,104
Reserves & Surplus	1,00,087	1,35,852	1,66,420	2,00,930	2,44,793
Shareholder's Funds	**1,12,017**	**1,51,955**	**1,82,523**	**2,17,034**	**2,60,897**
Deposits	**4,32,316**	**5,70,815**	**7,20,734**	**9,05,003**	**11,15,410**
Borrowings	5,214	1,63,792	1,67,068	1,87,116	2,24,539
Other liabilities	14,870	30,617	36,186	34,977	36,367
Total liabilities	**5,64,417**	**9,17,178**	**11,06,510**	**13,44,130**	**16,37,213**
Cash/Equivalent	58,027	83,529	1,10,975	1,36,515	1,67,494
Advances	3,96,434	6,66,299	7,85,272	9,54,764	11,71,101
Investments	1,00,375	1,53,518	1,94,598	2,35,301	2,78,853
Fixed Assets	3,312	3,688	4,372	4,572	4,772
Other assets	6,270	10,144	11,292	12,979	14,993
Total assets	**5,64,417**	**9,17,178**	**11,06,510**	**13,44,130**	**16,37,213**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 105: Key ratios

Y/E March	FY19	FY20	FY21E	FY22E	FY23E
Growth (%)					
NII growth	48.3	40.7	25.8	21.4	19.2
Pre-provision profit growth	54.2	45.3	23.5	18.2	19.0
PAT growth	45.0	54.9	1.1	41.1	27.1
Business (%)					
Deposit growth	27.6	32.0	26.3	25.6	23.2
Advance growth	33.4	68.1	17.9	21.6	22.7
CD ratio	90.0	105.9	112.4	107.0	105.2
CASA ratio	40.8	36.8	38.5	39.7	41.3
Operating efficiency (%)					
Cost-to-income	32.6	30.8	30.5	32.0	32.0
Cost-to-assets	3.6	3.3	2.9	3.1	3.0
Spreads (%)					
Yield on advances	16.5	17.9	15.7	15.8	15.5
Yield on investments	6.7	6.6	5.5	5.5	5.5
Cost of deposits	5.4	6.6	5.5	5.5	5.5
Yield on assets	13.4	14.9	13.0	13.0	12.8
Cost of funds	5.5	7.8	6.2	6.1	6.1
NIMs	9.1	8.7	8.0	8.0	7.8
Capital adequacy (%)					
Tier I	27.9	25.2	24.9	24.5	24.3
Tier II	1.3	2.2	3.5	3.5	3.5
Total CAR	29.2	27.4	28.4	28.0	27.8
Asset Quality (%)					
Gross NPA	1.8	1.4	2.9	3.2	3.0
Net NPA	0.5	0.5	1.4	1.3	1.1
Provision coverage	72.1	60.8	52.8	61.3	63.6
Slippage	2.6	2.6	4.5	2.2	1.8
Credit cost	2.1	2.6	3.6	2.5	2.0
Return (%)					
ROE	18.8	22.2	18.6	21.6	22.9
ROA	4.0	3.9	3.0	3.5	3.7
RORWA	5.7	6.2	4.7	5.4	5.6
Per share					
EPS	16.4	18.8	19.0	26.8	34.0
BV	93.9	94.4	113.3	134.8	162.0
ABV	92.0	91.9	106.1	126.6	153.3
Valuation					
P/E	32.1	10.8	21.4	15.2	12.0
P/BV	5.6	2.2	3.6	3.0	2.5
P/ABV	5.7	2.2	3.8	3.2	2.7

Source: Company, Nirmal Bang Institutional Equities Research

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SELL < -5%

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