BFI Finance

Version 8 | Bloomberg: BFIN IJ | Reuters: BFIN.JK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

4 Jan 2018

BUY

Last Traded Price (3 Jan 2018): Rp680 (JCI : 6,251.50)
Price Target 12-mth: Rp840 (24% upside) (Prev Rp700)

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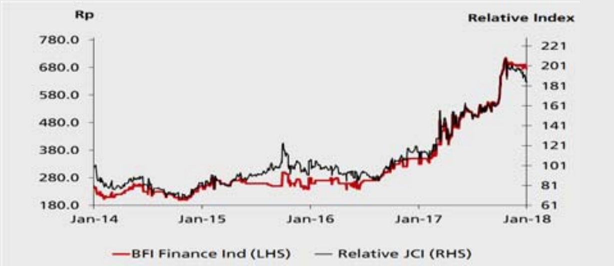
What's New

- Sustained growth traction to pave the way for growth
- Strong new booking growth is associated with margin expansion supported by strong refinancing business
- Our calculation suggests that current market valuation implies c.19% ROE, a disconnect with the strong ROE achievement of 25% in 9M17
- Maintain BUY with higher TP at 840/share; Earnings revised up by 18%/14% for FY17E/18F

Price Relative



Forecasts and Valuation

FY Dec (Rpbn)	2016A	2017F	2018F	2019F
Pre-prov. Profit	1,298	1,766	1,959	2,118
Net Profit	798	1,133	1,259	1,361
Net Pft (Pre Ex.)	798	1,133	1,259	1,361
Net Pft Gth (Pre-ex) (%)	22.8	41.9	11.1	8.1
EPS (Rp)	53.3	75.7	84.1	90.9
EPS Pre Ex. (Rp)	53.3	75.7	84.1	90.9
EPS Gth Pre Ex (%)	(32)	42	11	8
Diluted EPS (Rp)	53.3	75.7	84.1	90.9
PE Pre Ex. (X)	12.7	9.0	8.1	7.5
Net DPS (Rp)	22.1	26.7	37.8	42.1
Div Yield (%)	3.3	3.9	5.6	6.2
ROAE Pre Ex. (%)	19.3	24.5	23.6	22.5
ROAE (%)	19.3	24.5	23.6	22.5
ROA (%)	6.6	7.9	7.3	7.0
BV Per Share (Rp)	284	333	380	428
P/Book Value (x)	2.4	2.0	1.8	1.6
Earnings Rev (%):		18	14	9
Consensus EPS (Rp):		63.8	74.2	83.1
Other Broker Recs:		B: 2	S: 0	H: 0

Source of all data on this page: Company, DBS Bank, DBSVI, Bloomberg Finance L.P.

Staying exciting

Maintain BUY on exciting prospects. We maintain our bullish view on BFI Finance (BFIN)'s outlook on the back of: (1) better than expected growth traction, especially in the refinancing business, (2) structural NIM improvement due to higher yields, lower cost of funds post corporate bond rating upgrade, and (3) proven ability to maintain asset quality. These factors resulted in 25% ROE in 9M17, even with a low gearing ratio of c.2x (much lower than the industry and regulatory levels). BFIN's superior profitability and room for growth should justify its premium valuation, in our view. Its high dividend yield of c.5% is an added bonus. We also note that its heavy equipment leasing business has picked up strongly due to the improving commodity-related sector; this could add more upside to its current business portfolio and hence, earnings. We raised FY17E/18F earnings by 18%/14% for higher receivables growth and NIM to reflect better prospects. The stock has doubled in value in 2017 but strong prospects should continue to drive valuations higher.

Where we differ. We have the highest target price and earnings forecast on the street.

Potential catalyst. We believe the current market valuation only implies 19% ROE which is a disconnect with 25% ROE in 9M17. If the company can sustain this high ROE level by maintaining high growth and keeping asset quality in check, valuation should re-rate further. A higher payout could also drive up the stock price. BFIN is also expected to maintain a generous dividend payout policy of around 50%, thus implying an attractive dividend yield of c.5%.

Valuation:

Maintain BUY with higher TP. We raise our TP to Rp840, based on the Gordon Growth Model (assuming 21% ROE, 9% growth and 14% cost of equity), which implies 2.2x FY18 BV.

Key Risks to Our View:

Higher-than-expected inflation could hit customers' fixed income. An adverse economic cycle could also hit non-fixed income customers.

At A Glance

Issued Capital (m shrs)	15,967
Mkt. Cap (Rpbn/US$m)	10,858 / 805
Major Shareholders (%)	
Trinugraha Capital & Co (%)	43.7
Fil Ltd (%)	0.7
Commonwealth Bank (%)	0.2
Free Float (%)	55.4
3m Avg. Daily Val (US$m)	0.12
ICB Industry : Financials / General Financial	

WHAT'S NEW

Keeps on delivering

The current market valuation implies 19% ROE, much lower than 9M17's 25%. Our calculation suggests that the current market price implies c.19% sustainable ROE. This is a substantial disconnect to 9M17 ROE of 25%. We believe that the market is taking a conservative stance to assume that ROE will normalise lower. We agree in a way that 25% is a spectacular level and might not sustainable. But valuing the stock using 19% ROE - given the current strong growth traction and structural NIM improvement - also means throwing opportunity out the window.

What contributes to the current high ROE? Roll back 3 years to 2014 where BFIN recorded 17% ROE mainly due to lower interest spread. Dealer financing contributed 46% of its managed receivables while non-dealer financing was 42%. In September 2017, interest spread was 10.4% with non-dealer financing contributing 55% of the managed receivables. The shift towards non-dealer financing (refinancing) business is the main difference between the two periods. The lower cost of funds also helps, thanks to the bond rating upgrade and lower interest rate environment.

Stellar growth of refinancing business. New bookings growth in the non-dealer 4W and 2W space grew 31% y-o-y and 58% respectively in 9M17. Outlet expansion is also concentrated in Java area where the potential for the refinancing business is the highest.

How to sustain the growth traction? The growth in the refinancing business requires the company to handle more but smaller ticket loans. It requires operational excellence in terms of credit screening and collections. Outlets expansion to underpenetrated areas could also boost growth further. Effective implementation of an online application system is also helping improve efficiency, while cutting commissions for the external field agents.

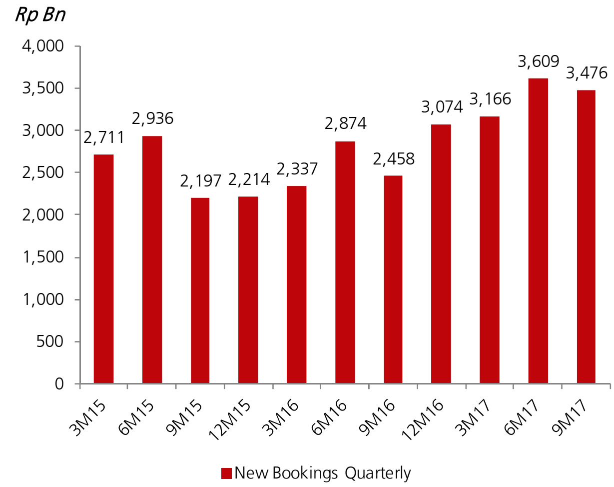
Higher spreads from higher asset yield and lower cost of funds; strong fee income. Interest spread increased 176bps y-o-y due to higher asset yields from a higher proportion of non-dealer financing and lower cost of funds. Fee income grew strongly at 30%, mainly driven by strong new bookings growth.

Operating costs and credit costs kept in check. Operating efficiencies improved with cost-to-income ratio declining 254bps y-o-y. Operating expenses growth of 22% is mainly due to higher business volume. Number of branches also rose 16 units to 321 during the year.

Credit costs headed lower to 1.7%, consistent with the improving asset quality trend. NPL improved to 1.1% from 1.8% a year ago while write off rate also improved to 1.52% in 9M17 from 1.67% in 9M16. This should indicate that asset quality is improving.

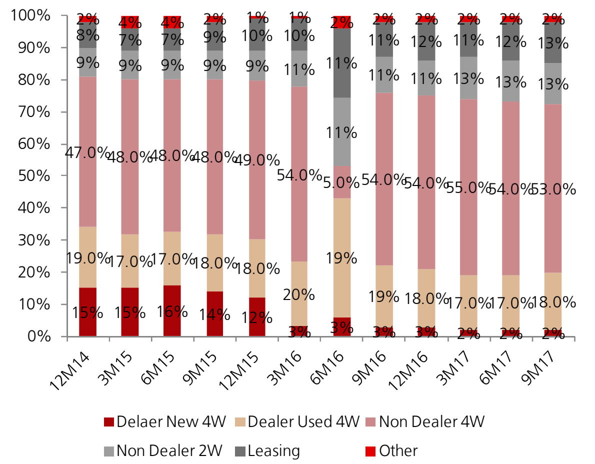
New bookings grew 34% y-o-y, driven by refinancing and leasing. New bookings grew strongly 34% y-o-y driven by refinancing business. The non-dealer 4W and 2W new bookings grew 31% and 58% respectively. New bookings in leasing, which was mainly dominated by heavy equipment leasing, also grew strongly by 58% due to high heavy equipment demand.

New booking quarterly



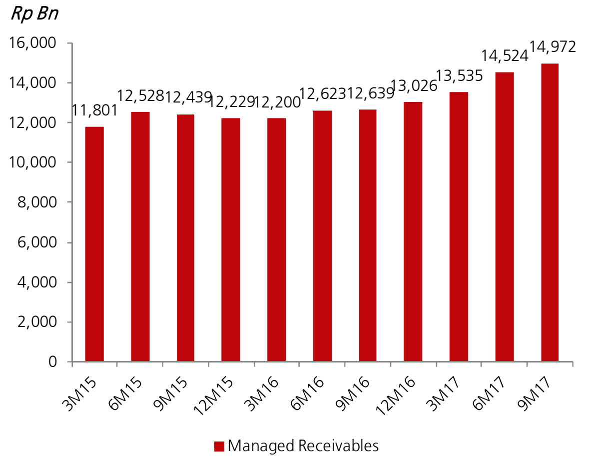
Source: Company, DBSVI, DBS Bank

New bookings composition



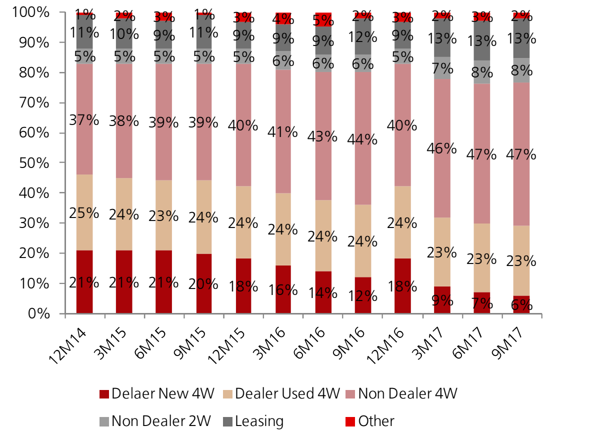
Source: Company, DBSVI, DBS Bank

Managed receivable growth



Source: Company, DBSVI, DBS Bank

Managed receivable composition



Source: Company, DBSVI, DBS Bank

Tax rate normalisation also helped bottom line on y-o-y basis. BFIN booked tax provisions last year to cushion against potential additional tax expenses from the undergoing tax investigation. It has stopped booking tax provisions this year and the effective tax rate has normalised to c.20% from 23% in the corresponding period a year ago.

Gearing ratio remained low at 2x. Gearing ratio is slightly higher at 2x from 1.7x in the previous year. But the gearing level is way below the regulated 10x level.

Outlook

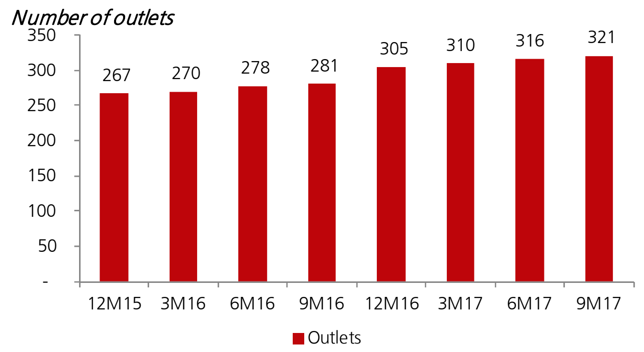
Maintain high growth mode next year. Management targets a modest 15%-20% new booking growth rate in 2018. However, we have to keep in mind that management has been very conservative in laying out targets. Earlier this year, new booking growth was targeted at 20%, while it achieved 34% in 9M17.

Outlet expansion to continue; most additions are in Java. Management targets to add 50 new outlets in 2018. We note that this target is more aggressive than the addition of 16 outlets in 2017. Management is planning to continue to add more outlets in Java, like they have always done since early 2014.

NIM expansion to continue. We expect yield to continue expanding in 2018 due to the company's shift to the high yielding refinancing business. Cost of funds, however, is expected to be lower as the company has moved more towards bonds financing to take advantage of improved pricing climate in the bond market.

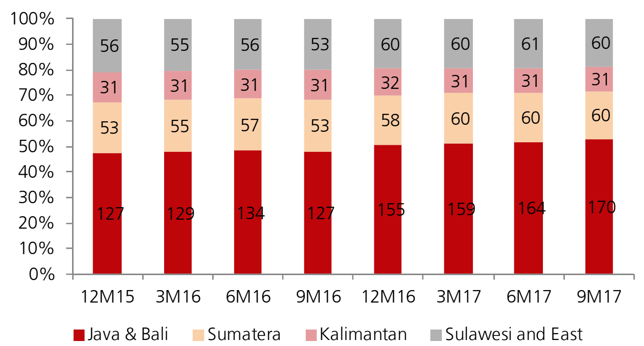
Expect asset quality to be stable. We expect asset quality to be stable at the current level. The management expects asset quality to stabilise towards the normal c.1.2% level (higher than last year's 0.93%), aided by improving commodity prices. Elsewhere, management has guided for credit cost to remain stable (with a maximum increase of 10bps). The change of write-off policy to 210 days overdue last quarter (from 270 days) should not affect its credit cost. By regulation, multi-finance companies have to set aside 100% provisions for loans that are 180 days overdue.

Number of outlets



Source: Company, DBSVI, DBS Bank

Outlet distribution by regions



Source: Company, DBSVI, DBS Bank

Valuation and recommendation

Maintain BUY with higher TP. We raise our TP to Rp840, which is based on the Gordon Growth Model (21% ROE, 9% growth and 14% cost of equity) and implies 2.2x FY18 BV. The stock has doubled in value in 2017 but strong prospects should continue to drive valuations higher. BFIN's superior profitability and room for growth should justify its premium valuation, in our view. Its high dividend yield of c.5% is an added bonus.

Quarterly / Interim Income Statement (Rpbn)

FY Dec	3Q2016	2Q2017	3Q2017	% chg yoy	% chg qoq
Net Interest Income	413	501	1,214	193.9	142.1
Non-Interest Income	193	261	(412)	(313.2)	nm
Operating Income	606	762	802	32.3	5.3
Operating Expenses	(268)	(314)	(358)	33.4	14.0
Pre-Provision Profit	338	448	444	31.5	(0.8)
Provisions	(81.2)	(109)	(47.7)	(41.3)	(56.1)
Associates	0.0	0.0	0.0	nm	nm
Exceptionals	0.0	0.0	0.0	nm	nm
Pretax Profit	257	340	397	54.5	16.8
Taxation	(43.4)	(68.1)	(80.4)	85.3	18.0
Minority Interests	0.0	0.0	0.0	nm	nm
Net Profit	213	271	316	48.3	16.5
Growth (%)					
Net Interest Income Gth	3.5	6.6	142.1		
Net Profit Gth	18.2	6.7	16.5		
Key ratio (%)					
NIM	15.5	16.2	44.3		
NPL ratio	1.4	0.9	1.4		
Cost-to-income	44.2	41.2	44.6		

Source of all data: Company, DBS Bank, DBSVI

CRITICAL DATA POINTS TO WATCH

Critical Factors

Strong growth of non-dealer financing. Managed receivables is expected to continue to book double digit growth. Looking at the continuing improvement in asset quality, management indicated that it is comfortable to take on more risk this year and has guided for c.20% increase in new bookings. We expect the strong growth momentum in the non-dealer business, along with the improvement in the commodity-related business, to support a sustainable 15% receivable growth going forward.

Diverse products. BFIN offers a variety of products including dealer new/used 4W financing, as well as non-dealer 4W and 2W financing. There is also heavy equipment and machinery leasing. However, management will continue to focus on the non-dealer financing business, with the portfolio targeted to be maintained at the current 50% level.

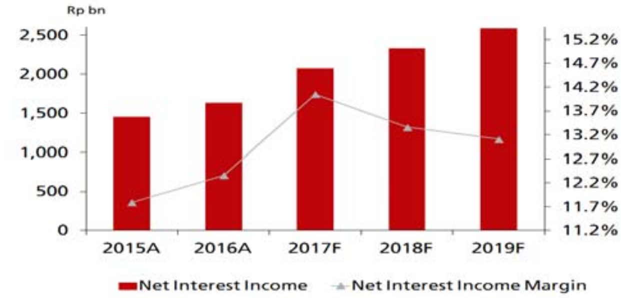
Possible NIM improvement. Further expansion in the non-dealer business can increase asset yield further. The yields from non-dealer 4W and 2W financing can be up to 20% and 40%, respectively, much higher than dealer financing yields of 15-16%. Elsewhere, the bond rating upgrade from Fitch and lower interest-rate environment may enable BFIN to lower its cost of funds further.

Non-interest income supported by financing growth. About 60% of BFIN's non-interest income is upfront fees worth 2-3% of loan size, while 40% are other fees such as late and transaction penalty charges.

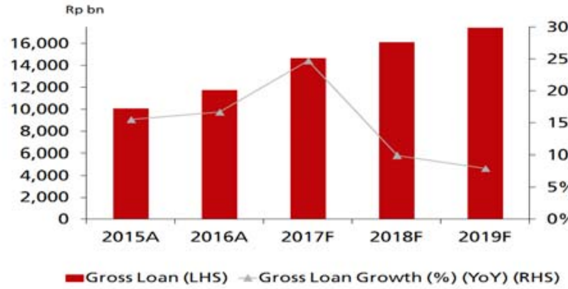
NPL and credit cost to stabilise. We believe NPL and credit cost can be maintained at current levels, as the economy and automotive market should stabilise this year. We expect NPL to hover around 1.2%, while credit cost should be flattish.

Higher opex due to expansion. We expect higher operating expenses to stem from its aggressive expansion plan. Management targets to add up to 50 new outlets in 2018.

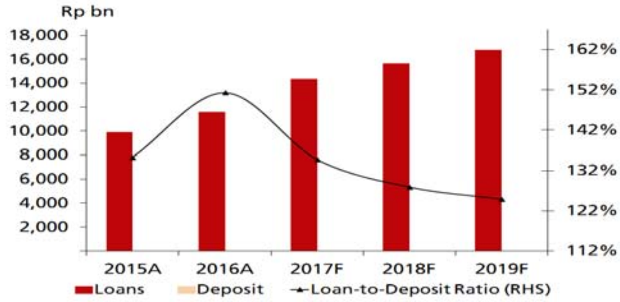
Margin Trends



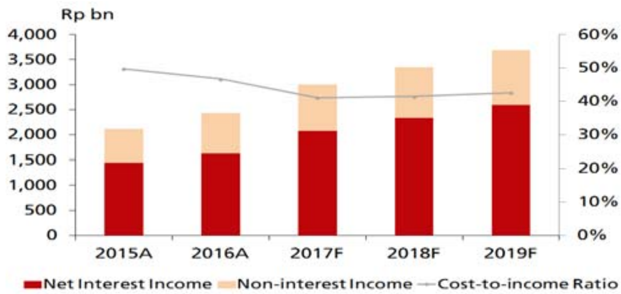
Gross Loan& Growth



Loan-to-Deposit Ratio Trend



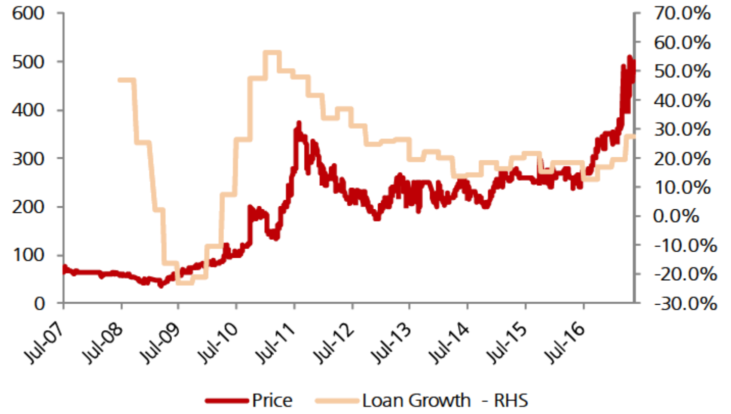
Cost & Income Structure



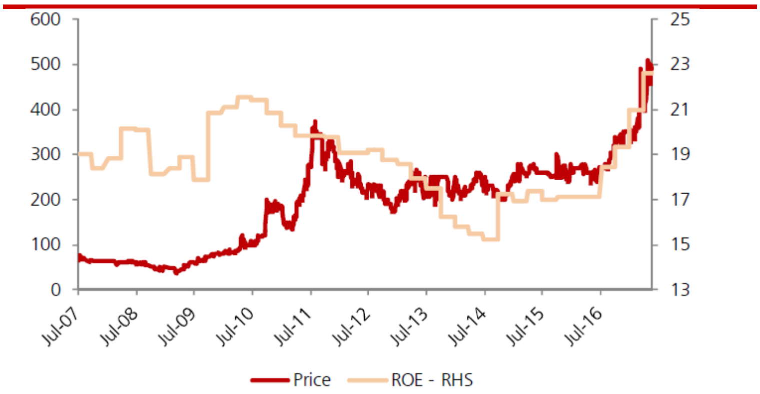
Source: Company, DBS Bank, DBSVI

Appendix 1: A look at Company's listed history – what drives its share price?

Loan growth as critical factor



Bond Yield as critical factor



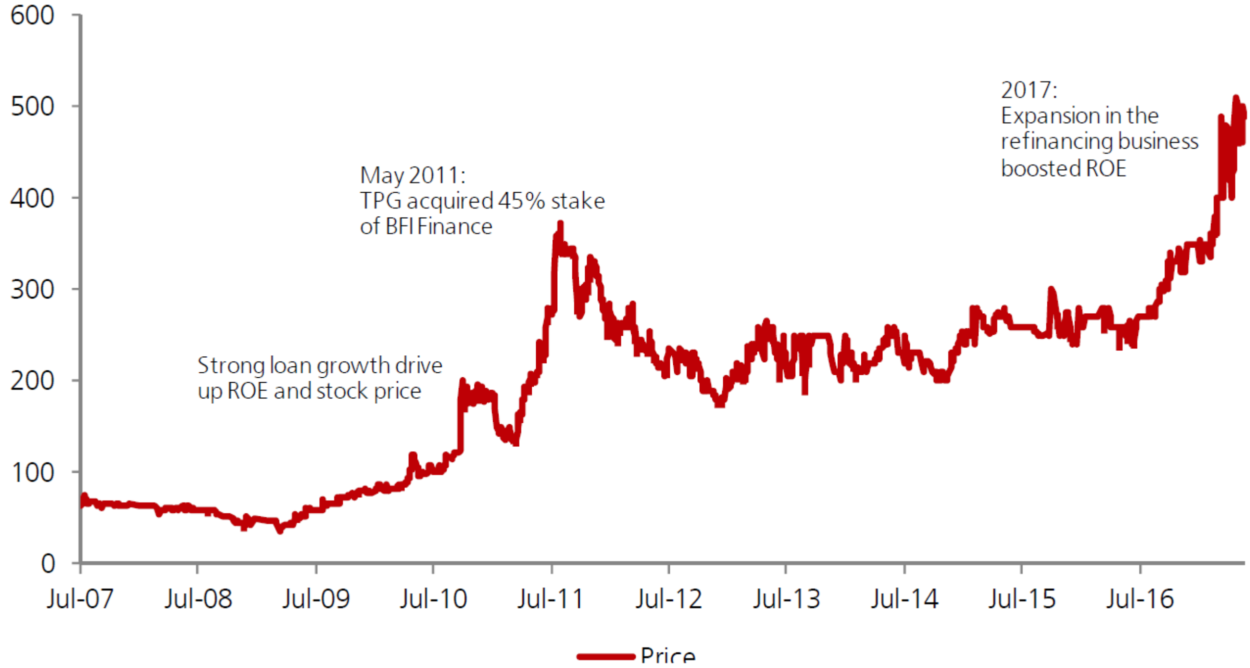
Remarks

Loan growth is the main driver of stock price. BFI is underleveraged and is known for its conservatism to maintain safe level of liquidity and leverage. BFI is a stand-alone multifinance company (unlike most multifinance companies which are backed by banks), and therefore has less access to financial help unlike most of its peers.

ROE in the past year has been improving significantly due to expansion in the refinancing business, which offers higher yield.

Source: Bloomberg Finance L.P, DBSVI, DBS Bank

Share price performance (10-year historical trend)



Source: Bloomberg Finance L.P, DBSVI, DBS Bank

Balance Sheet:

Funding is not an issue. Funding is not an issue this year as BFIN continues to utilise bond issuances and bank borrowings. Currently, bonds contribute c.40% of the funding and no significant change is expected. USD debt exposure is about 30% of its total debt and is fully hedged.

NPLs be maintained at low level. Management expects NPL to be stable at around c.1.2%. The company recently changed its write -off policy on its automotive loans to 210 days overdue from 270 days.

Gearing ratio remains low. The company's gearing ratio has below 2x historically. BFIN is well-capitalised and carries low solvency risk. Even with the currently strong growth momentum, management expects gearing to not exceed 3x in the near future.

Share Price Drivers:

Near-term resilience will support valuation; M&A will boost multiples over the long term. BFIN's diversified portfolio and unique direct financing business will continue to deliver sustainable earnings in the long term. BFIN is also an attractive M&A target given its cheap valuation, and also that it is one of the few sizeable multi-finance companies not directly backed by a bank.

Key Risks:

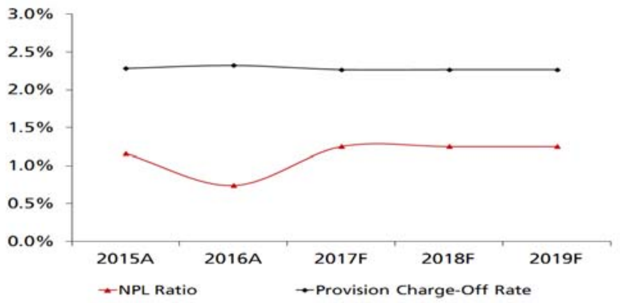
Slower-than-expected growth; more intense competition. The slower growth of consumer financing would be a downside risk to our forecast. Tougher competition can also lower yields and erode NIM.

Macro risk. Higher-than-expected inflation could hit customers earning fixed income. An adverse economic cycle could also hit the non-fixed income customers.

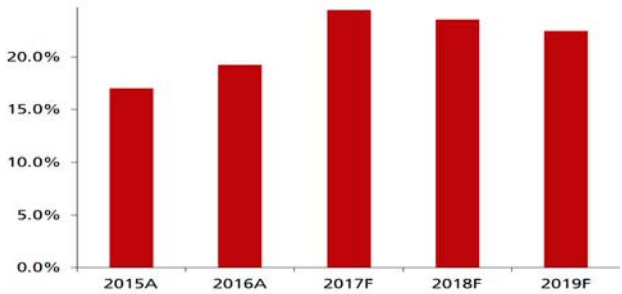
Company Background

BFI Finance (BFIN) is a financing company that focuses on consumer financing, both dealer generated and direct lending. The major shareholder with a 44.95% stake is a consortium comprising TPG Capital, Northstar Equity Partners and Boy Garibaldi Thohir.

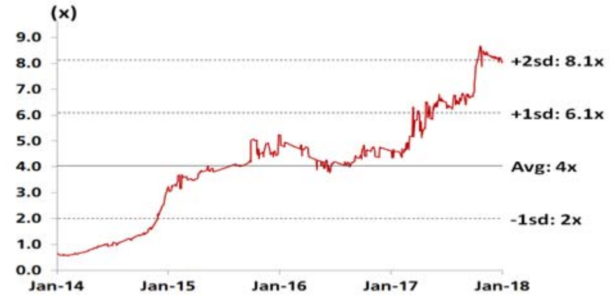
Asset Quality



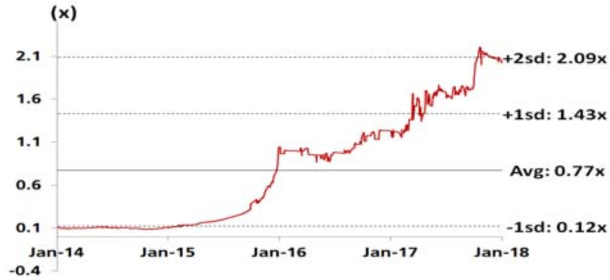
ROE (%)



Forward PE Band (x)



PB Band (x)



Source: Company, DBS Bank, DBSVI

Key Assumptions

FY Dec	2015A	2016A	2017F	2018F	2019F
Gross Loans Growth	15.6	16.8	24.7	10.0	8.0
Yld. On Earnings Assets	17.6	18.4	20.1	19.6	19.3
Avg Cost Of Funds	11.1	10.6	9.7	9.4	9.4

Income Statement (Rpbn)

FY Dec	2015A	2016A	2017F	2018F	2019F
Net Interest Income	1,448	1,630	2,074	2,329	2,590
Non-Interest Income	671	805	926	1,018	1,100
Operating Income	2,119	2,435	3,000	3,348	3,690
Operating Expenses	(1,053)	(1,137)	(1,233)	(1,388)	(1,572)
Pre-provision Profit	1,066	1,298	1,766	1,959	2,118
Provisions	(230)	(273)	(333)	(366)	(395)
Associates	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	836	1,025	1,434	1,593	1,722
Taxation	(185)	(227)	(301)	(335)	(362)
Minority Interests	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	650	798	1,133	1,259	1,361
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Growth (%)					
Net Interest Income Gth	12.1	12.6	27.3	12.3	11.2
Net Profit Gth	8.9	22.8	41.9	11.1	8.1
Margins, Costs & Efficiency (%)					
Spread	6.6	7.8	10.4	10.2	9.9
Net Interest Margin	11.8	12.4	14.1	13.4	13.1
Cost-to-Income Ratio	49.7	46.7	41.1	41.5	42.6
Business Mix (%)					
Net Int. Inc / Opg Inc.	68.3	66.9	69.1	69.6	70.2
Non-Int. Inc / Opg inc.	31.7	33.1	30.9	30.4	29.8
Fee Inc / Opg Income	25.6	29.2	27.3	26.9	26.3
Oth Non-Int Inc/Opg Inc	6.1	3.9	3.6	3.6	3.5
Profitability (%)					
ROAE Pre Ex.	17.0	19.3	24.5	23.6	22.5
ROAE	17.0	19.3	24.5	23.6	22.5
ROA Pre Ex.	6.1	6.6	7.9	7.3	7.0
ROA	6.1	6.6	7.9	7.3	7.0

Source: Company, DBS Bank, DBSVI

Quarterly / Interim Income Statement (Rpbn)

FY Dec	3Q2016	4Q2016	1Q2017	2Q2017	3Q2017
Net Interest Income	413	441	470	501	1,214
Non-Interest Income	193	228	230	261	(412)
Operating Income	606	669	700	762	802
Operating Expenses	(268)	(311)	(305)	(314)	(358)
Pre-Provision Profit	338	358	395	448	444
Provisions	(81.2)	(51.3)	(75.8)	(109)	(47.7)
Associates	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pretax Profit	257	306	319	340	397
Taxation	(43.4)	(61.6)	(64.5)	(68.1)	(80.4)
Minority Interests	0.0	0.0	0.0	0.0	0.0
Net Profit	213	245	254	271	316
Growth (%)					
Net Interest Income Gth	3.5	6.8	6.6	6.6	142.1
Net Profit Gth	18.2	14.7	4.0	6.7	16.5

Balance Sheet (Rpbn)

FY Dec	2015A	2016A	2017F	2018F	2019F
Cash/Bank Balance	777	165	1,031	2,007	2,811
Government Securities	0.0	0.0	0.0	0.0	0.0
Inter Bank Assets	0.0	0.0	0.0	0.0	0.0
Total Net Loans & Advs.	9,898	11,583	14,357	15,674	16,804
Investment	0.0	0.0	0.20	0.0	0.0
Associates	0.0	0.0	0.0	0.0	0.0
Fixed Assets	450	414	415	414	411
Goodwill	0.0	0.0	0.0	0.0	0.0
Other Assets	645	313	313	313	313
Total Assets	11,770	12,476	16,116	18,409	20,340
Customer Deposits	0.0	0.0	0.0	0.0	0.0
Inter Bank Deposits	0.0	0.0	0.0	0.0	0.0
Debts/Borrowings	7,318	7,656	10,656	12,256	13,456
Others	434	565	472	472	472
Minorities	0.0	0.0	0.0	0.0	0.0
Shareholders' Funds	4,019	4,255	4,988	5,680	6,412
Total Liab& S/H's Funds	11,770	12,476	16,116	18,408	20,340

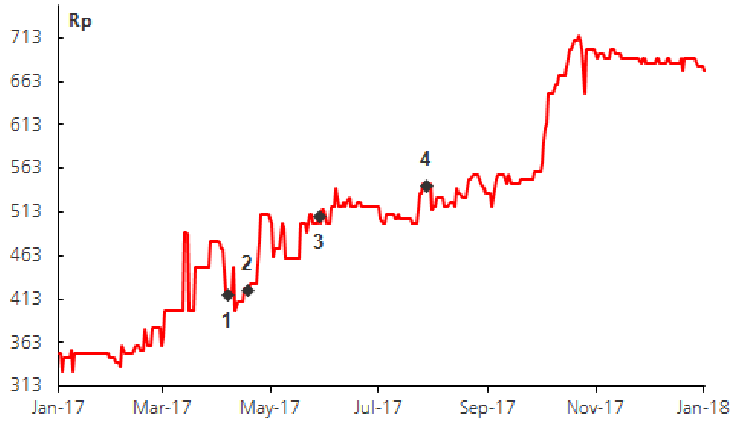
Source: Company, DBS Bank, DBSVI

Financial Stability Measures (%)

FY Dec	2015A	2016A	2017F	2018F	2019F
Balance Sheet Structure					
Loan-to-Deposit Ratio	135.3	151.3	134.7	127.9	124.9
Net Loans / Total Assets	84.1	92.8	89.1	85.1	82.6
Investment / Total Assets	0.0	0.0	0.0	0.0	0.0
Cust . Dep./Int. Bear. Liab.	0.0	0.0	0.0	0.0	0.0
Interbank Dep / Int. Bear.	0.0	0.0	0.0	0.0	0.0
Asset Quality					
NPL / Total Gross Loans	1.2	0.7	1.2	1.2	1.2
NPL / Total Assets	1.2	0.9	1.2	1.1	1.1
Loan Loss Reserve Coverage	126.6	154.4	168.8	225.5	280.8
Provision Charge-Off Rate	2.3	2.3	2.3	2.3	2.3
Capital Strength					
Total CAR	0.0	0.0	0.0	0.0	0.0
Tier-1 CAR	0.0	0.0	0.0	0.0	0.0

Source: Company, DBS Bank, DBSVI

Target Price & Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	07 Apr 17	420	500	BUY
2:	18 Apr 17	425	500	BUY
3:	29 May 17	510	500	HOLD
4:	28 Jul 17	545	700	BUY

***Note**: Share price and Target price are adjusted for corporate actions.*

Source: DBS Bank, DBSVI
Analyst: Benedictus Agung SWANDONO
Sue Lin LIM

DBS Bank, DBSVI recommendations are based an Absolute Total Return* Rating system, defined as follows:
STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)
BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return i.e. > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

Completed Date: 3 Jan 2018 21:28:26 (WIB)
Dissemination Date: 4 Jan 2018 16:33:16 (WIB)

Sources for all charts and tables are DBS Bank, DBSVI unless otherwise specified.

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