

Bread Financial Holdings Inc

4Q beats but outlook remains cloudy;
Neutral

Reiterate Rating: NEUTRAL | PO: 35.00 USD | Price: 30.50 USD

Too much uncertainty; Remain at Neutral

We are somewhat surprised that Bread Financial (BFH) shares are outperforming today following its 4Q print. While 4Q EPS of \$0.87 was ahead of BofAe/consensus at \$(0.82)/\$(0.70) on better-than-forecast revenues and credit, BFH's 2024 guide was below estimates and the impact from the CFPB's (Consumer Finance Protection Bureau) late fee rule was higher than we had anticipated. Core metrics like credit sales (down 23% y/y) and delinquencies (at a 5yr high) also remain pressured. Positively, BFH is tightening credit and prepping for the late fee rule implementation. Currently trading at 75% of tangible book value, shares are relatively cheap too. However, with credit metrics still weak and overhang from the late fee rule likely to last for some time, we think a Neutral rating is warranted.

'24 guide disappointing

For 2024, Bread expects revenue to be down low- to mid-single digits vs. 2023, a touch weaker than BofAe/consensus down 2.5%/2% y/y. NIM (net interest margin) is expected to be down y/y. For average loans, BFH expects balances to be down low-single digits vs. +4% for BofAe/ consensus. BFH did note that loan balances would be up low-single digits excluding the BJ's sale. BFH highlighted that it is tightening credit and higher credit losses would impact both revenue and loan growth. BFH expects net charge-offs in the low 8% range, a little weaker than BofAe/consensus at 8.03%/7.91%. BFH expects to deliver nominal operating leverage in 2024 and full-year operating expenses to be lower. Notably, the guide excludes any impact from the CFPB late fee rule.

Potential late fee rule impacts larger than anticipated

Assuming Oct 1 implementation of the late fee rule, BFH conservatively estimates it would reduce 4Q23 revenue by 25% y/y. This 25% reduction includes some mitigation actions that BFH is implementing ahead of the rule being introduced and suggests the late fee contribution is larger. BFH would not disclose the gross contribution from late fees. BFH did note that the longer the gap to the rule being implemented, the smaller the headwind. Assuming a 25% haircut to 4Q24 revs in addition to the low-single digits revs guide implies 2024 revenues could be down close to 10% y/y. We are concerned that BFH would struggle to achieve profitability with such a large revenue headwind.

Adjusting estimates – PO to \$35

We adjust our 2024/2025 EPS estimates to \$8.74/\$11.24 from \$8.33/\$12.03 prior as we account for 4Q results and new guidance. We tweak our PO to \$35 (\$34 prior) based on an unchanged 4x multiple to our 2024e forecast. Our PO also implies a 0.8x P/TBV (price /tangible book value) multiple, reflecting concern about profitability if the late fee rule is implemented.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	4.46	14.33	8.74	11.24	12.05
EPS Change (YoY)	-72.2%	221.3%	-39.0%	28.6%	7.2%
Consensus EPS (Bloomberg)			7.98	9.70	NA
DPS	0.84	0.84	0.84	0.84	0.84
Valuation (Dec)					
P/E	6.8x	2.1x	3.5x	2.7x	2.5x
Dividend Yield	2.8%	2.8%	2.8%	2.8%	2.8%

25 January 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	34.00	35.00

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Stock Data

Price	30.50 USD
Price Objective	35.00 USD
Date Established	25-Jan-2024
Investment Opinion	C-2-7
52-Week Range	23.19 USD -44.52 USD
Mrkt Val / Shares Out (mn)	1,505 USD / 49.3
Free Float	98.3%
Average Daily Value	23.53 USD
BofA Ticker / Exchange	BFH / NYS
Bloomberg / Reuters	BFH US / BFH.N
ROE (2024E)	0%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

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Timestamp: 25 January 2024 04:14PM EST

iQprofileSM Bread Financial Holdings Inc

Key Income Statement Data (Dec)	2022A	2023A	2024E	2025E	2026E
(US\$ Millions)	US GAAP	US GAAP	US GAAP	US GAAP	US GAAP
Net Interest Income	4,182	4,266	4,125	4,240	4,482
Net Fee Income	NA	NA	NA	NA	NA
Securities Gains / (Losses)	NA	NA	NA	NA	NA
Other Income	0	0	0	0	0
Total Non-Interest Income	(356)	23.0	(166)	(181)	(197)
Total Operating Income	3,826	4,289	3,959	4,059	4,285
Operating Expenses	(1,933)	(2,092)	(2,008)	(2,035)	(2,148)
Pre-Provision Profit	1,893	2,197	1,950	2,024	2,137
Provisions Expense	(1,593)	(1,229)	(1,368)	(1,276)	(1,335)
Operating Profit	300	968	582	748	802
Non-Operating Items	NA	NA	NA	NA	NA
Pre-Tax Income	300	968	582	748	802
Net Income to sh/holders	223	737	434	557	598
Adjusted Cash Earnings	223	737	434	557	598

Key Balance Sheet Data

Total Assets	25,407	23,141	22,416	23,049	24,324
Average Interest Earning Assets	21,659	21,806	21,201	21,790	22,745
Risk Weighted Assets	NA	NA	NA	NA	NA
Total Gross Customer Loans	21,365	19,333	18,488	18,801	19,916
Total Customer Deposits	13,826	13,620	12,649	12,662	13,116
Tier 1 Capital	NA	NA	NA	NA	NA
Tangible Equity	NA	NA	NA	NA	NA
Common Shareholders' Equity	2,265	2,931	3,364	3,922	4,520

Key Metrics

Net Interest Margin	19.3%	19.6%	19.5%	19.5%	19.7%
Tier 1 Ratio	NA	NA	NA	NA	NA
Effective Tax Rate	25.7%	23.9%	25.5%	25.5%	25.5%
Loan / Assets Ratio	84.1%	83.5%	82.5%	81.6%	81.9%
Loan / Deposit Ratio	155%	142%	146%	148%	152%
Oper Leverage (Inc Growth - Cost Growth)	2.12%	3.88%	-3.70%	1.20%	0.03%
Gearing (Assets / Equity)	11.2x	7.90x	6.66x	5.88x	5.38x
Tangible Equity / Assets	0%	0%	0%	0%	0%
Tangible Equity / RWAs	NA	NA	NA	NA	NA

Business Performance

Revenue Growth	16.9%	12.1%	-7.70%	2.54%	5.58%
Operating Expense Growth	14.8%	8.23%	-4.00%	1.33%	5.55%
Provisions Expense Growth	193%	-22.8%	11.3%	-6.76%	4.65%
Operating Revenue / Average Assets	NA	NA	NA	NA	NA
Operating Expenses / Average Assets	NA	NA	NA	NA	NA
Pre-Provision ROA	NA	NA	NA	NA	NA
ROA	NA	NA	NA	NA	NA
Pre-Provision ROE	NA	NA	NA	NA	NA
ROE	NA	NA	NA	NA	NA
RoTE	NA	NA	NA	NA	NA
RoRWAs	NA	NA	NA	NA	NA
Dividend Payout Ratio	18.8%	5.68%	9.55%	7.43%	6.93%
Efficiency Ratio (Cost / Income Ratio)	NA	NA	NA	NA	NA

Quality of Earnings

Total Non-Interest Inc / Operating Inc	NA	NA	NA	NA	NA
Market-Related Revenue / Total Revenues	0%	0%	0%	0%	0%
Provisioning Burden as % of PPP	84.2%	55.9%	70.1%	63.0%	62.5%
NPLs plus Foreclosed Real Estate / Loans	NA	NA	NA	NA	NA
Loan Loss Reserves / NPLs	11.5%	12.0%	12.0%	11.6%	11.5%
Loan Loss Reserves / Total Loans	13.0%	13.7%	13.6%	13.2%	13.1%
Provisions Expense / Average Loans	NA	NA	NA	NA	NA

Company Sector

Financial Services-Consumer/Commercial

Company Description

Headquartered in Columbus, Ohio, Bread Financial is a financial services company providing simple, personalized payment, lending and saving solutions. Bread offers a comprehensive product suite of products including private label and co-brand credit cards, installment lending and buy now, pay later (split-pay).

Investment Rationale

We rate BFH a Neutral. Bread's customer base skews more subprime and we believe they will be most pressured by inflation and the resumption of student loan payments. Additionally, the CFPB's late fee proposal is a major risk for BFH earnings, in our view. That said, these risks appear priced in given it is trading at a deep discount to book value.

Stock Data

Average Daily Volume 771,368

Quarterly Earnings Estimates

	2023	2024
Q1	9.08A	3.31E
Q2	0.95A	2.81E
Q3	3.42A	2.58E
Q4	0.87A	0.05E

4Q Key metrics and additional detail on 2024 guidance

PPNR (pre-provision net revenue) (+): came in at \$501M well above BofAe/consensus estimates at \$450M/\$464M primarily driven by higher net interest income.

Net interest income (+): Net interest income was \$1,075M above BofAe/consensus at \$1,036M/\$1,048M driven by higher yields on card loans. Higher yields drove a NIM (net interest margin) of 19.61%, up 32bps y/y, and above BofAe/consensus at 18.99%/18.89%.

The company expects a sequential decline of NIM in 1Q due to seasonality as well as pressure from higher credit losses and funding costs. NIM is also expected to decline on a y/y basis in 2024. For 2024, BFH also expects revenues down low- to mid-single digits from 2023 excluding gain on portfolio sale (\$4,059M base).

Credit / reserves (+): The net charge-off rate was 8.0%, better than our consensus-like 8.2% estimate. The company built \$121M reserves, below BofAe/consensus at \$131M/\$134M, which led to a reserve ratio of 12.04%, down 27bps q/q. The decrease in the reserve rate was driven by seasonally increased transactor balances.

The company expects a low 8% range net loss rate for full year 2024, peaking in the first half, with each of the first two quarters in the mid- to high-8% range. The company said it expects the 1Q24 reserve rate to be similar to 3Q23 levels (12.31%). BFH said it will remain conservative and likely hold reserves higher for the second quarter, after which the rate may begin to come down if the current economic outlook holds.

OpEx (+/-): Total expenses of \$516M were in line with BofAe/consensus at \$518M/\$516M, down 6% y/y. Higher employee compensation and benefit costs driven by higher headcount for digital and tech modernization roles was more than offset by lower card and processing, marketing and D&A costs. The efficiency ratio (total non-interest expense/non-interest income) was down 2% y/y.

BFH said total expenses will be lower in 2024 than 2023 assuming the economic outlook remains intact. BFH also guided to nominal positive operating leverage in 2024 (0-1%).

Exhibit 1: PPNR came in above consensus driven by higher NII

Variance table

(\$ in millions)	Actual	Estimate	Variance	Var per share	Consensus
	Dec-23-A	Dec-23-E	(Actual - Est)		
Income Statement					
Interest on fees and loans	1,264.0	1,219.1	45	\$2.14	1,229.6
Interest on cash and investment securities	48.0	47.5	0	\$0.02	46.5
Total interest income	1,312.0	1,266.6	45	\$2.17	1,284.3
y/y growth	-1%	-4%			-3%
Interest on deposits	154.0	153.0	1	(\$0.05)	158.4
Interest on borrowings	83.0	77.7	5	(\$0.25)	78.6
Total interest expense	237.0	230.7	6	(\$0.30)	237.6
Net interest income	1,075.0	1,035.9	39	\$1.87	1,047.5
y/y growth	-5%	-8%			-7%
Interchange revenue, net of RSAs	(91.0)	(101.7)	11	\$0.51	(102.2)
Other revenue	33.0	33.0	0	\$0.00	34.6
Total non-interest income	(58.0)	(68.7)	11	\$0.51	(67.7)
y/y growth	-40%	-29%			-30%
Provision for credit losses	482.0	503.6	(22)	\$1.03	514.9
y/y growth	-30%	-27%			-26%
Total non-interest expense	516.0	517.5	(1)	\$0.07	515.8
y/y growth	-6%	-6%			-6%
% of total revenue (excluding provisions)	50.7%	53.5%			52.6%
Income from continuing operations before income tax	19.0	(53.8)	73	\$3.48	(50.9)
y/y growth	-109%	-74%			-75%



Exhibit 1: PPNR came in above consensus driven by higher NII

Variance table

(\$ in millions)	Actual	Estimate	Variance	Var per share	Consensus
Provision for income taxes	(26.0)	(13.4)	(13)	\$0.60	(15.7)
tax rate	-137%	25%			31%
Income from continuing operations	45.0	(40.3)	85	\$1.72	(35.3)
y/y growth	-134%	-70%			-74%
Income from discontinued operations, net of tax	(2.0)	0.0	(2)	(\$0.04)	0.0
Net income	43.0	(40.3)	83	\$1.68	(35.0)
y/y growth	-132%	-70%			-74%
EPS from continuing operations	\$0.87	(\$0.82)	\$1.68		(\$0.70)
y/y growth	-132%	-70%			74%
Average diluted shares outstanding	49.6	49.4			49.8
Other Key Metrics					
Pre-Provision Net Revenue	\$501.0	\$449.8			\$464.0
ROE	5.95%	-5.68%			-4.96%
Net interest margin	19.61%	18.99%			18.89%
Credit card and loan receivables, gross	19,333	19,290			19,523
y/y growth	-9.51%	-9.71%			-8.62%
Average Loans	18,267	18,196			18,531
y/y growth	-7.84%	-8.20%			-6.51%
Deposits	13,620	13,936			14,303
y/y growth	-1.49%	0.79%			3.45%
Credit Sales	7,802	8,133			8,336
y/y growth	-23.25%	-20.00%			-18.00%
Net Principal loss rate (Calc)	7.90%	8.20%			8.15%
y/y increase (BPS)	160.8	190.3			
Reserve Ratio	12.04%	12.12%			12.00%
Reserve Build	121	131			134

Source: BofA Global Research estimates, company reports, Visible Alpha

BofA GLOBAL RESEARCH

Price objective basis & risk

Bread Financial Holdings Inc (BFH)

Our \$35 PO is based on a 4x PE multiple to '24e EPS. A 4x PE multiple is below peers currently trading at 7x and the typical range for card issuers (7-12x), reflecting the hostile macro backdrop and BFH's outsized exposure to the subprime consumer relative to peers.

Downside risks to our price objective are: an economic downturn, which could lead to elevated loan loss rates, increased defaults, higher credit costs and slower loan growth. Deteriorating economic conditions would likely hurt investor sentiment and drive valuations lower. Loss of retail partners also poses a risk to growth and the earnings outlook.

Analyst Certification

I, Mihir Bhatia, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Payments, Processors, Specialty Finance and IT services Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Accenture Plc	ACN	ACN US	Jason Kupferberg
	American Express Company	AXP	AXP US	Mihir Bhatia
	Block Inc	SQ	SQ US	Jason Kupferberg
	Capital One Financial	COF	COF US	Mihir Bhatia
	Discover Financial	DFS	DFS US	Mihir Bhatia
	Enact Holdings	ACT	ACT US	Mihir Bhatia
	Essent Group	ESNT	ESNT US	Mihir Bhatia
	Fidelity National Information Services	FIS	FIS US	Jason Kupferberg
	Fiserv Inc	FI	FI US	Jason Kupferberg
	FleetCor Technologies Inc.	FLT	FLT US	Mihir Bhatia
	Flywire	FLYW	FLYW US	Jason Kupferberg
	Global Payments Inc	GPN	GPN US	Jason Kupferberg
	Jack Henry & Associates	JKHY	JKHY US	Jason Kupferberg
	Mastercard Inc	MA	MA US	Jason Kupferberg
	MGIC Investment Corp.	MTG	MTG US	Mihir Bhatia
	NMI Holdings	NMIH	NMIH US	Mihir Bhatia
	Nuvei	NVEI	NVEI US	Jason Kupferberg
	Nuvei	YNVEI	NVEI CN	Jason Kupferberg
	OneMain Holdings, Inc.	OMF	OMF US	Mihir Bhatia
	Shift4 Payments, Inc	FOUR	FOUR US	Jason Kupferberg
	Telus International	TIXT	TIXT US	Cassie Chan
	Telus International	YTIXT	TIXT CN	Cassie Chan
	Visa Inc.	V	V US	Jason Kupferberg
	WEX Inc.	WEX	WEX US	Mihir Bhatia
NEUTRAL				
	ADP	ADP	ADP US	Jason Kupferberg
	Affirm Holdings	AFRM	AFRM US	Jason Kupferberg
	Bread Financial Holdings Inc	BFH	BFH US	Mihir Bhatia
	DLocal	DLO	DLO US	Jason Kupferberg
	Globant SA	GLOB	GLOB US	Jason Kupferberg
	Marqeta	MQ	MQ US	Jason Kupferberg
	PayPal Holdings Inc	PYPL	PYPL US	Jason Kupferberg
	SoFi Technologies Inc	SOFI	SOFI US	Mihir Bhatia
	Synchrony Financial	SYF	SYF US	Mihir Bhatia
	Thoughtworks	TWKS	TWKS US	Jason Kupferberg
	Toast	TOST	TOST US	Jason Kupferberg
	TTEC Holdings	TTEC	TTEC US	Cassie Chan



US - Payments, Processors, Specialty Finance and IT services Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
UNDERPERFORM	CGI Inc.	GIB	GIB US	Jason Kupferberg
	CGI Inc.	YGIBA	GIB/A CN	Jason Kupferberg
	Cognizant Technology Solutions	CTSH	CTSH US	Jason Kupferberg
	Coinbase	COIN	COIN US	Jason Kupferberg
	DXC Technology	DXC	DXC US	Jason Kupferberg
	EPAM Systems	EPAM	EPAM US	Jason Kupferberg
	Paychex	PAYX	PAYX US	Jason Kupferberg
	Radian Group Inc	RDN	RDN US	Mihir Bhatia
	Rocket Companies, Inc.	RKT	RKT US	Mihir Bhatia
	TaskUs	TASK	TASK US	Cassie Chan
RSTR	Western Union	WU	WU US	Jason Kupferberg
	EngageSmart	ESMT	ESMT US	Jason Kupferberg

iQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity
Operating Margin
Earnings Growth
Free Cash Flow

Quality of Earnings

Cash Realization Ratio
Asset Replacement Ratio
Tax Rate
Net Debt-To-Equity Ratio
Interest Cover

Valuation Toolkit

Price / Earnings Ratio
Price / Book Value
Dividend Yield
Free Cash Flow Yield
Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income
Operating Profit
Expected 5 Year CAGR From Latest Actual
Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations
Capex
Tax Charge
Net Debt = Total Debt – Cash & Equivalents
EBIT

Numerator

Current Share Price
Current Share Price
Annualised Declared Cash Dividend
Cash Flow From Operations – Total Capex
EV = Current Share Price × Current Shares + Minority Equity + Net Debt + Other LT Liabilities
Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Amortization
Shareholders' Equity
Sales
N/A
N/A

Denominator

Net Income
Depreciation
Pre-Tax Income
Total Equity
Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)
Shareholders' Equity / Current Basic Shares
Current Share Price
Market Cap = Current Share Price × Current Basic Shares
Sales
Basic EBIT + Depreciation + Amortization

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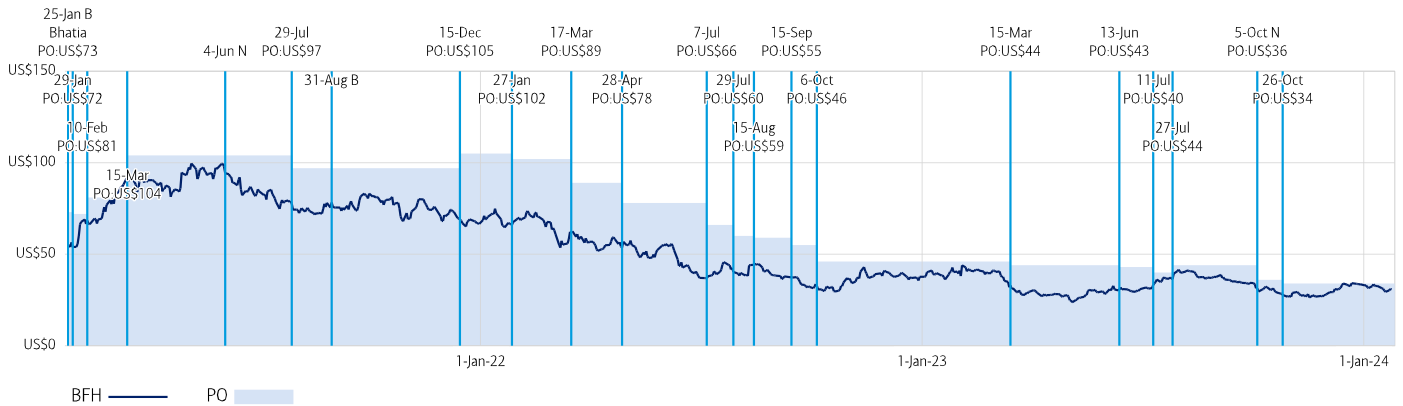
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Disclosures

Important Disclosures

Bread Financial (BFH) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	156	53.79%	Buy	94	60.26%
Hold	72	24.83%	Hold	48	66.67%
Sell	62	21.38%	Sell	35	56.45%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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