

Bread Financial Holdings Inc

BofA Securities 2024 Financials Conference: Takeaways

Reiterate Rating: NEUTRAL | PO: 40.00 USD | Price: 36.61 USD

Controlling the controllables in the current backdrop

Bread Financial's (BFH) CEO, Ralph Andretta, and CFO, Perry Beberman stuck a positive tone and highlighted that the progress the company has made in executing its strategic plan. BFH acknowledged the backdrop has presented some challenges – regulatory overhang from the CFPB being the biggest but also high inflation and a softer macro pressuring credit. Still BFH was confident that it can deliver on its short-term targets, and navigate the potential headwinds from lower late fees long-term. Reiterate Neutral.

Preemptively putting late fee mitigants in place

Bread is already proactively implementing mitigants to recoup lower fees from the expected late fee rule. Initially, this involves increasing APRs on new loans. This is prudent, in our view. It will take some time for new higher APR loans to replace existing loans (back book), so getting out in front of the rule should mitigate the impact of the rule. BFH did note that it has additional actions it will take (fees, underwriting changes) but brand partners generally want to wait for the rule to be finalized before implementing these changes. Consistent with industry and our expectation, Bread expects a final rule to come out before the State of the Union (3/7).

Higher near-term losses, early stage DQs are encouraging

Credit losses will likely inflect sharply higher in February / March, as despite January loss rate being 85, BFH reaffirmed mid-to-high 8% loss rates in 1Q and 2Q. BFH expects loss rates to decline in 2H and is encouraged by the early stage delinquency formations which are improving. It also expects macro and lower interest rates to be a tailwind. BFH noted it's underwriting posture remains tight which should also help losses and it is confident that longer-term it can bring losses below 6%.

QTD: weaker big-ticket spending = lower MDR

Management detailed that cardholders are continuing to self-regulate on spending, which is most visible in soft spending on big ticket spend and other verticals dominated by PLCCs. The weakness in big ticket will lead to lower MDRs and consensus appears too high given current spending trends. BFH also noted that roll rates are quite high which is leading to the high near-term losses in 1Q/2Q. That said, categories like Jewelry continue to perform solidly and deposit balances are approaching \$6.7B (up 20% y/y). We adjust our 2024/2025E EPS estimates to \$8.25/\$10.70 (\$8.60/\$11.18 prior) as we account the update. We maintain our \$40 price objective.

See inside for other key takeaways

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	4.46	14.33	8.25	10.70	11.62
EPS Change (YoY)	-72.2%	221.3%	-42.4%	29.7%	8.6%
Consensus EPS (Bloomberg)			7.23	9.02	7.05
DPS	0.84	0.84	0.84	0.84	0.84
Valuation (Dec)					
P/E	8.2x	2.6x	4.4x	3.4x	3.2x
Dividend Yield	2.3%	2.3%	2.3%	2.3%	2.3%

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Stock Data

Price	36.61 USD
Price Objective	40.00 USD
Date Established	15-Feb-2024
Investment Opinion	C-2-7
52-Week Range	23.19 USD -41.89 USD
Mrkt Val / Shares Out (mn)	1,809 USD / 49.4
Free Float	97.6%
Average Daily Value	29.86 USD
BofA Ticker / Exchange	BFH / NYS
Bloomberg / Reuters	BFH US / BFH.N
ROE (2024E)	0%
ESGMeter™	High

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CECL: Current Expected Credit Losses Methodology

CFPB: Consumer Financial Protection Bureau

DQs: Delinquencies

MDRs: Merchant Discount Rate

APR: Annual percentage rate

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	4,062	4,207	4,474
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	(229)	(231)	(249)
Total Operating Income	3,826	4,289	3,832	3,976	4,225
Operating Expenses	(1,933)	(2,092)	(1,945)	(1,994)	(2,118)
Pre-Provision Profit	1,893	2,197	1,888	1,982	2,107
Provisions Expense	(1,593)	(1,229)	(1,339)	(1,270)	(1,333)
Operating Profit	300	968	549	713	774
Non-Operating Items	NA	NA	NA	NA	NA
Pre-Tax Income	300	968	549	713	774
Net Income to sh/holders	223	737	409	531	577
Adjusted Cash Earnings	223	737	409	531	577

Key Balance Sheet Data

Total Assets	25,407	23,141	22,232	23,003	24,317
Average Interest Earning Assets	21,659	21,806	20,904	21,695	22,719
Risk Weighted Assets	NA	NA	NA	NA	NA
Total Gross Customer Loans	21,365	19,333	18,337	18,758	19,903
Total Customer Deposits	13,826	13,620	12,520	12,675	13,184
Tier 1 Capital	NA	NA	NA	NA	NA
Tangible Equity	NA	NA	NA	NA	NA
Common Shareholders' Equity	2,265	2,918	3,340	3,871	4,447

Key Metrics

Net Interest Margin	19.3%	19.6%	19.4%	19.4%	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%	81.5%	81.8%
Loan / Deposit Ratio	155%	142%	146%	148%	151%
Oper Leverage (Inc Growth - Cost Growth)	2.12%	3.88%	-3.60%	1.23%	0.03%
Gearing (Assets / Equity)	11.2x	7.93x	6.66x	5.94x	5.47x
Tangible Equity / Assets	0%	0%	0%	0%	0%
Tangible Equity / RWAs	NA	NA	NA	NA	NA

Business Performance

Revenue Growth	16.9%	12.1%	-10.6%	3.75%	6.26%
Operating Expense Growth	14.8%	8.23%	-7.05%	2.52%	6.23%
Provisions Expense Growth	193%	-22.8%	8.92%	-5.14%	4.99%
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%	10.1%	7.80%	7.18%
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%	70.9%	64.1%	63.3%
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%	13.7%	13.2%	13.0%
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 815,661

Quarterly Earnings Estimates

	2023	2024
Q1	9.08A	3.44E
Q2	0.95A	2.21E
Q3	3.42A	2.39E
Q4	0.87A	0.21E

Other key takeaways

- While BFH is focused on delivering positive operating leverage in 2024, it still expects to invest in digital and technological capabilities to remain competitive in the market.
- Bread believes that its underwriting improvements and portfolio construction shift towards general-purpose cards could help drive the reserve rate lower in the long term, but noted that the CECL Day 1 number does not contemplate downside scenarios / include risk overlays.
- The \$30M buyback authorization is primarily to offset dilution associated with employee restricted stock unites. BFH still plans to paydown debt, reduce double leverage, and build capital levels.
- While some have pushed back on the ability for Bread to easily raise APRs, but the company noted it did not raise APRs on cards earlier because it wanted to remain competitive vs peers and its returns did not require this additional lift.



Price objective basis & risk

Bread Financial Holdings Inc (BFH)

Our \$40 PO is based on a 0.9x multiple to current book value. We believe more investors are looking at BFH through a book value lens given potential profitability challenges if the CFPB's late fee rule was to come into effect. We view a book value of <1.0 as appropriate in such a backdrop.

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
	Marqeta	MQ	MQ US	Cassie Chan
	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
	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
	Western Union	WU	WU US	Jason Kupferberg

iQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

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

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

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

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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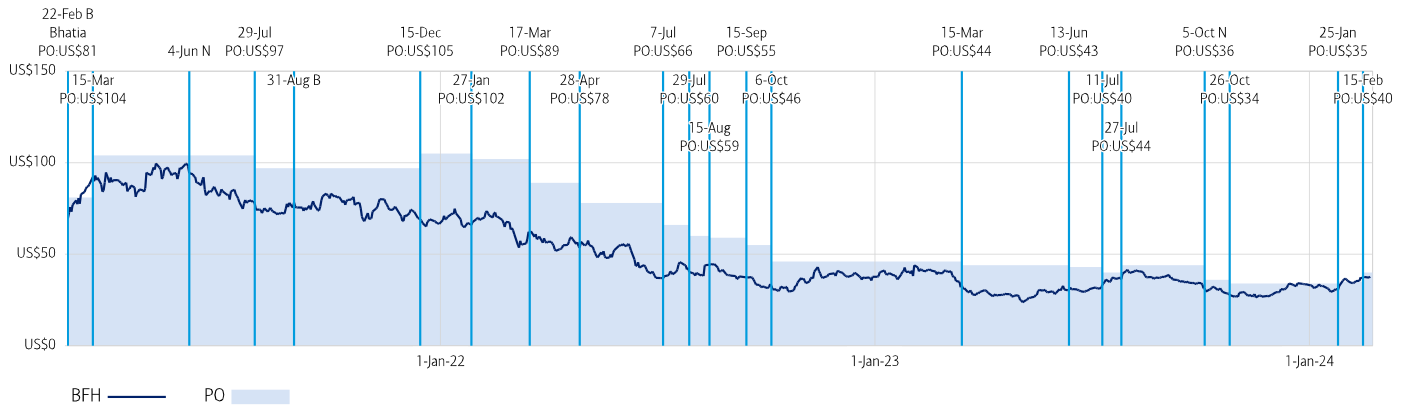
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Bread Financial (BFH) Price Chart



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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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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