

Initiation of Coverage for Bendigo and Adelaide Bank (ASX:BEN)

Executive Summary

We initiate coverage on Bendigo and Adelaide Bank with a BUY recommendation based on a 12-month price target of \$10.88 comprised of a discounted cashflow and dividend discount models. Our price target represents a 28% upside from the current share price of \$13.89 in alignment with other analyst recommendations. Despite a recent earning surprise shock post 1H25, we project that net interest earnings will expand as Bendigo leverages its existing base low cost demand deposit funding to expand business and household lending despite margin compression in current macroeconomic policy conditions.

Business Description:

Operating outside of the big-4 banking oligopoly, Bendigo and Adelaide bank have garnered a brand identity of retail service to predominantly rural areas, with recent expansion into the online neo-bank sector. The company's varied banking arms provide the company with defensible brand power and the ability to service a broader demographic of customers than other mid-sized institutions. The core Bendigo bank brand provides retail banking services, business and private banking, wealth management and other credit products writing \$60.4B and \$10.4B in new residential and business loans in FY24 respectively. The core banking arm currently serves 2.83% of the retail home loan market. Conversely, the recently spawned UP neo-bank caters to a young, digital-only demographic with greater focus on demand and term deposits with only recent addition of credit products and loans offered to select customers.

Investment Thesis: Upwards Swing in Lending Book Performance with UP

The funding mix of the core Bendigo and Adelaide bank brand is comprised predominantly of retail customer deposits (offering 3.4% p.a. interest) at 75.2%, with wholesale borrowing and loan capital low at 11.9% below competitors BOQ and ING. This represents a strong and low cost base primed for continued balance sheet and loan expansion. To cater towards top line growth, the emergence of UP bank lending products provide an opportunity to increase ROA without incurring large fixed costs due to the online nature of neo-banking infrastructure. Additionally, UP bank customers are more likely to access credit products with higher interest margin due to their focus on unsecured personal loans in conjunction with traditional residential mortgages.

Despite a slip in NIM of -0.21% and a rising cost base due to regulatory, compliance and digital infrastructure spending, Bendigo Bank justifies its current share price through a combination of a defensible economic moat in its mid-size rural brand, stable funding base and opportunity to grow interest income through the UP bank branch of operations.

Regulatory Environment

Bendigo and Adelaide Bank is positioned to perform well in adapting to the new APS230 prudential requirements surrounding outsourcing agreements and data security when considering a clean track record against cyberattacks prevalent in the sector across their over-150-year history. Additionally, their commitment to data privacy evident in their chairmans address provides evidence of strong organisational governance when tackling future issues of this scope

Fundamental Analysis

When looking beyond recent earnings surprise, BEN has provided consistent returns among recent RBA interest rate uncertainties, sitting among medium sized retail banking peers when considering a favourable P/E ratio valuation, reasonable return on assets for the sector and consistent dividend payout ratio.

Metric	Value
Valuation Date	2025-04-25 00:00:00
Share Price	\$10.88
Diluted Shares Outstanding	567m
Cost of Equity	8.69%
Terminal Growth Rate	2.50%
Share Price	\$10.88
Intrinsic Value	\$10.73
Discount/(Premium)	-1.39%

Cash earnings after tax \$265.2 million 1H24 \$268.2 million 1.1% 2H24 \$293.8 million 9.7%	Statutory NPAT \$216.8 million 1H24 \$282.3 million 23.2% 2H24 \$262.7 million 17.5%
Dividend per share 30 cents per share 1H24 30 cents per share 2H24 33 cents per share	Cash return on equity 7.55% 1H24 7.82% 27 bps 2H24 8.54% 99 bps

Metric	Value
Dividend Yield (%)	2.69
Earnings Per Share (EPS)	0.96
Price to Earnings (P/E)	11.6
Return on Assets (ROA %)	0.55
Return on Equity (ROE %)	7.68
Profit Margin (%)	27.03
Operating Margin (%)	33.38
Price to Book (P/B)	0.89
Dividend Payout Ratio (%)	31.19

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