

Sept 22, 2023

**COMPANY UPDATE** | Sector: Financials

# Shriram Finance

## Growth and Asset Quality in good shape

### Used PV, MSME and Gold Loans to spearhead growth

Post-merger entity Shriram Finance is a multi-product play having synergistic growth spurt at disposal. Its stronger AUM growth of 4% qoq/18.6% yoy in Q1 FY24 surprised many. In our view, the growth momentum could likely continue through the year aided by 1) residual benefits of value growth in used CV/PV financing (50%/19% of AUM), 2) firm replacement demand for used PVs, 3) phased roll-out of MSME Loans (10% of AUM) in vehicle financing branches, 4) distribution of Gold Loans (3% of AUM) taken to substantial number of vehicle financing branches, and 5) sustained momentum in Personal Loans (4% of AUM).

In longer run, the growth levers would be 1) stronger volume growth in used CV/PV financing (co. has been gaining market share consistently), 2) availability/supply of used BS VI vehicles, 3) operational policy driven emphasis on realization of cross-sell/distribution synergies, 4) tapping of market outside Shriram ecosystem customers for erstwhile SCUF products and 5) conversion of rural centers into full-fledged branches. Management expects to deliver a 15% AUM CAGR over the next three years with a diversified product portfolio offering growth fungibility. The AUM mix is expected to move meaningfully towards Used PV, MSME and Gold Loans.

### Collections, portfolio construct and ECL coverage healthy

The improvement in operating environment for Vehicle Finance and MSME Loans customers has translated into healthy collection efficiency for the company. New delinquency creation and existing delinquency flow across buckets has come down and bucket corrections are happening. This is reflected in meaningful decline in absolute Stage-2 bucket over the past three quarters notwithstanding controlled fwd. flow into Stage-3. The Stage-3 assets have seen limited increase in recent quarters adjusted for the write-offs which have also nearly normalized. We believe that collection efficiency and stage-wise portfolio construct are in good shape and overall ECL coverage is adequate. Hence, we estimate credit cost to be around the guided level of 2%.

Micro factors which are supportive of asset quality include a) rising vehicle prices, b) shift within MSME portfolio towards secured loans (now almost 90% from below 80%), c) nearly 95% of PL portfolio comprising of erstwhile 2W customers or existing 2W customers who have repaid >80% of the loan, d) no longer tenor (>3 years) loans offered in Vehicle and MSME financing and e) loan eligibility (even during cross-sell) determined on assessed cash flows/income and FOIR.

### NIM to stabilize with transmission of hikes and product mix shift

NIM is likely to bottom out in the current quarter with further increase in CoF and lagged/slow benefit of the lending rate hikes taken (25-100 bps) across products. The co. has not raised rates in case of high-yielding products (>18-19% yield) such as PL, 2W and small-ticket (<Rs3 lakh) MSME loans which combined form 15-20% of AUM. Besides the transmission of rate hikes, the continued AUM mix shift towards better yielding products of MSME, Gold Loans and PLs should improve the blended portfolio yield in medium term and support stable margins (around 8.5%).

### Reasonable valuation for healthy growth and profitability

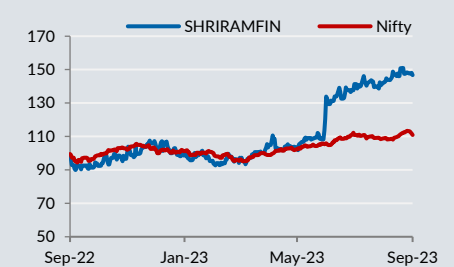
We expect 14-15% AUM CAGR and 18-19% earnings CAGR over FY23-25 with average RoA/RoE delivery of 3.3%/16%. For reviewing estimates, we would closely monitor a) pricing and volume growth in used CV/PV segment, b) distribution roll-out of GL and MSME Loans in vehicle financing branches and success in cross-sell, c) emerging signs of stress in PL and MSME Loan portfolios (Stage-2 coverage seems low in these products) and d) cost of funds. Even after a strong run-up in the past 3-4 months, the stock's valuation is reasonable at 1.4x P/ABV and 8.5x P/E on FY25 estimates. Retain BUY with an upgraded 12m PT of Rs2300.

Reco	: <b>BUY</b>
CMP	: Rs 1,900
Target Price	: Rs 2,300
Potential Return	: 21.1%

#### Stock data (as on Sept 21, 2023)

Nifty	19,742
52 Week h/l (Rs)	1972 / 1146
Market cap (Rs/USD mn)	719878 / 8660
Outstanding Shares (mn)	375
6m Avg t/o (Rs mn):	1,747
Div. yield (%):	1.9
Bloomberg code:	SHFL IN
NSE code:	SHRIRAMFIN

#### Stock performance



	1M	3M	1Y
Absolute return	3.1%	9.6%	49.3%

#### Shareholding pattern

Promoter	25.5%
FII+DII	70.0%
Others	4.5%

#### Δ in stance

(1-Yr)	New	Old
Rating	BUY	BUY
Target Price	2,300	2,110

#### Δ in earnings estimates

	FY23	FY24e	FY25e
EPS (New)	159.7	190.7	224.3
EPS (Old)	159.7	190.7	224.3
% Change	-	-	-

#### Financial Summary

(Rs mn)	FY23	FY24E	FY25E
Op. income	172,571	192,275	225,852
PPOP	123,441	134,583	161,656
Net profit	59,793	71,396	83,978
Growth (%)	120.8	19.4	17.6
EPS (Rs)	159.7	190.7	224.3
ABVPS (Rs)	1,005.0	1,146.7	1,317.3
P/E (x)	11.9	10.0	8.5
P/ABV (x)	1.9	1.7	1.4
ROAE (%)	17.3	15.5	16.0
ROAA (%)	3.5	3.3	3.5

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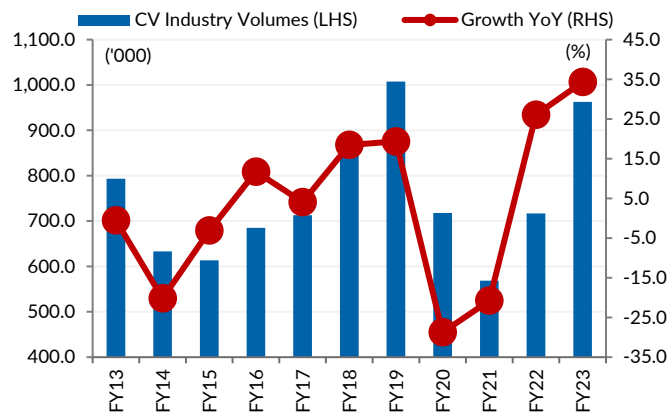
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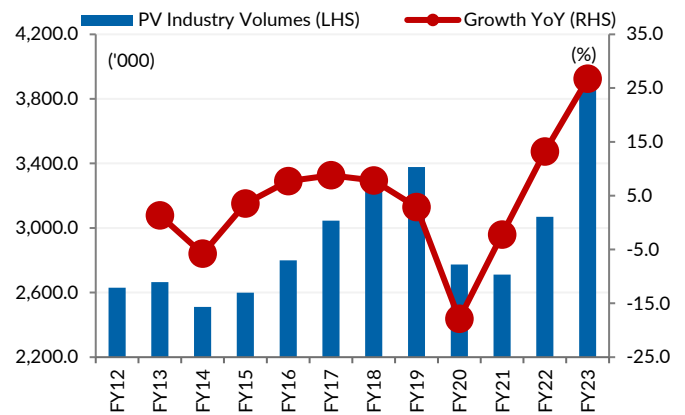
## STORY IN CHARTS

**Exhibit 1: CV Industry volumes**



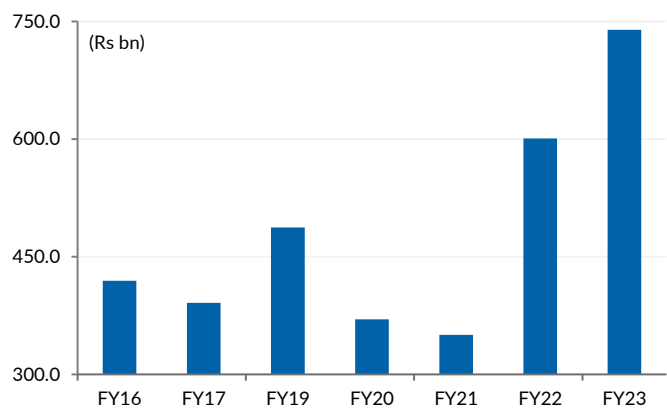
Source: Company, YES Sec

**Exhibit 2: PV Industry volumes**



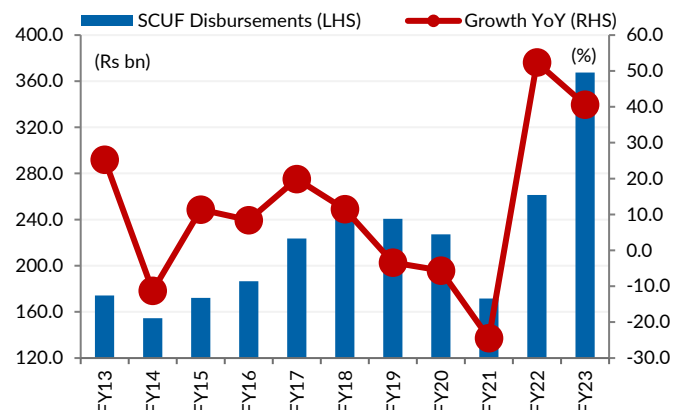
Source: Company, YES Sec

**Exhibit 3: Erstwhile SHTF Disbursement Trend**



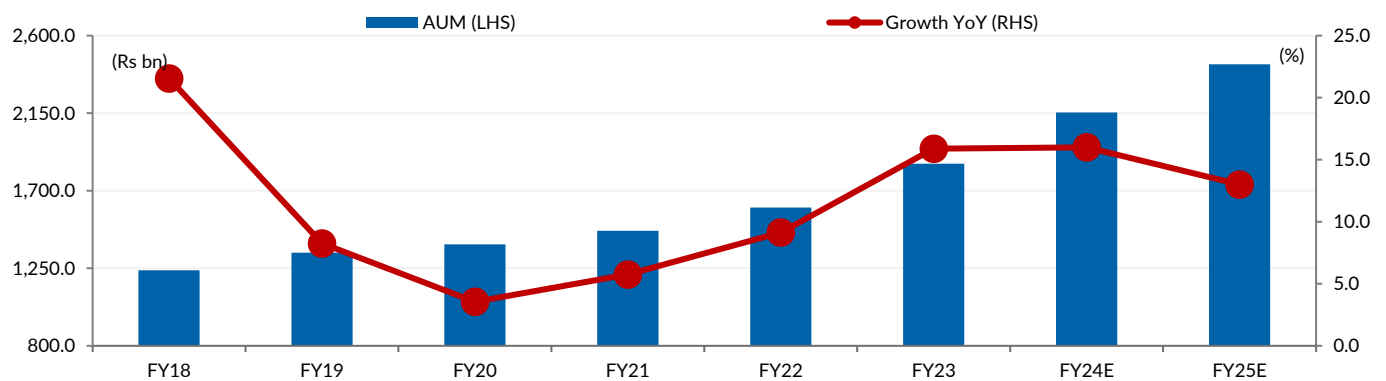
Source: Company, YES Sec

**Exhibit 4: Erstwhile SCUF Disbursement Trend**



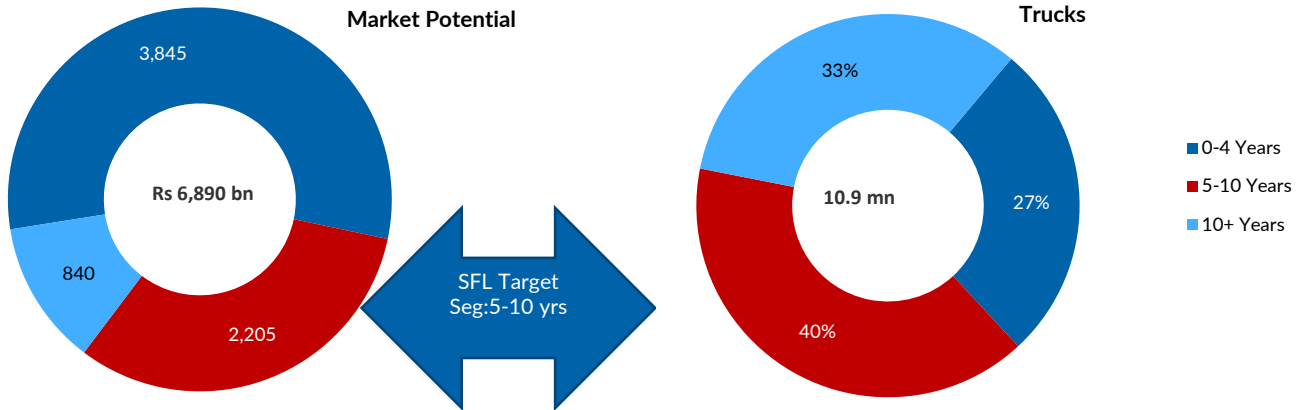
Source: Company, YES Sec

**Exhibit 5: Merged entity's AUM growth to remain firm**



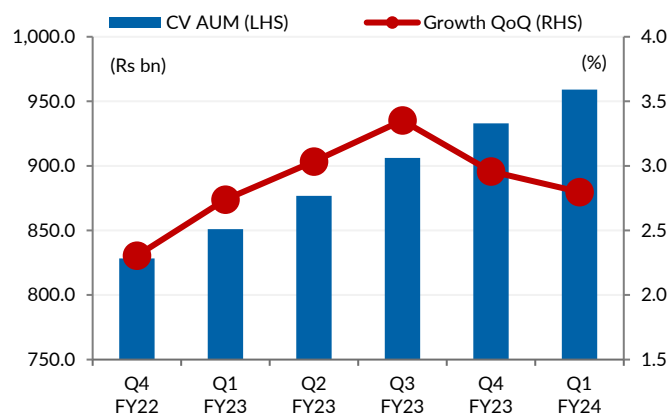
Source: Company, YES Sec, \*AUM from FY18-FY21 pertains to Erstwhile Shriram Transport and SCUF Combined

**Exhibit 6: SFL target segment is huge due to under-penetration of used CV financing**



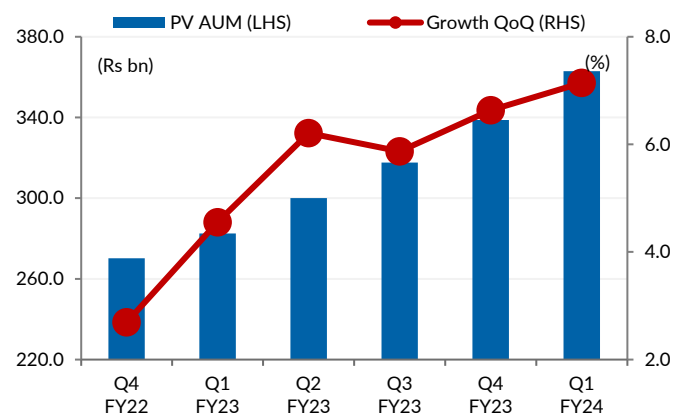
Source: Company, YES Sec

**Exhibit 7: Used CV growth momentum moderate**



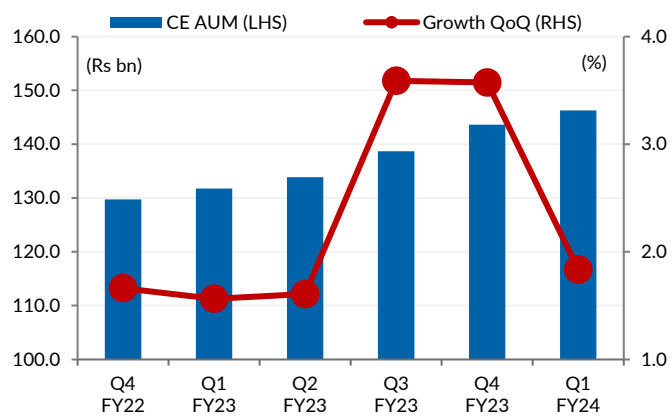
Source: Company, YES Sec

**Exhibit 8: Used PV growth has been strong**



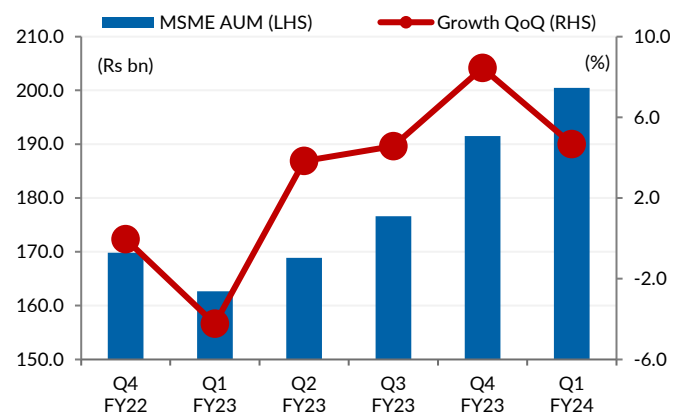
Source: Company, YES Sec

**Exhibit 9: Used CE growth has been modest**



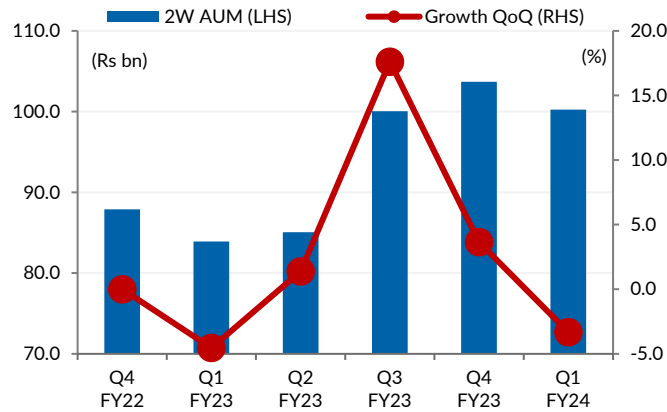
Source: Company, YES Sec

**Exhibit 10: MSME growth momentum has improved**



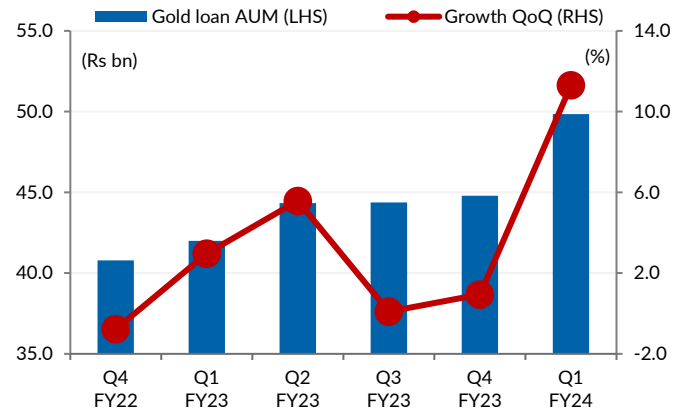
Source: Company, YES Sec

**Exhibit 11: 2W growth has been chequered**



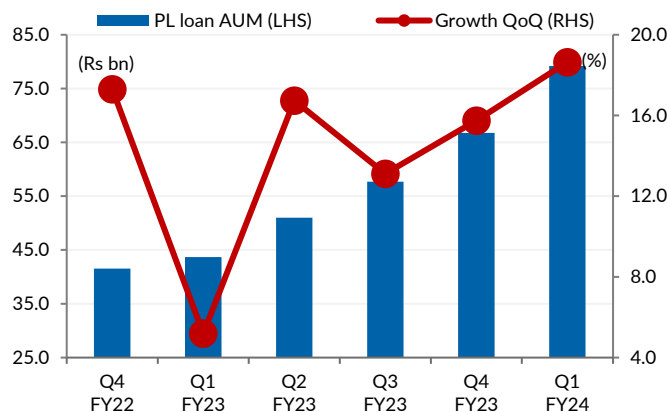
Source: Company, YES Sec

**Exhibit 12: GL growth has accelerated**



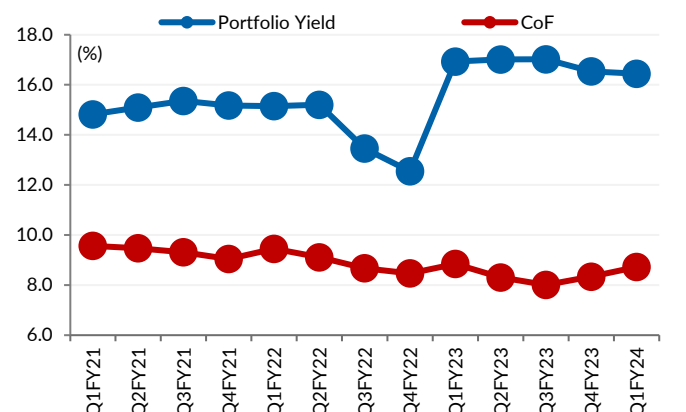
Source: Company, YES Sec

**Exhibit 13: PL growth happening at substantial pace**



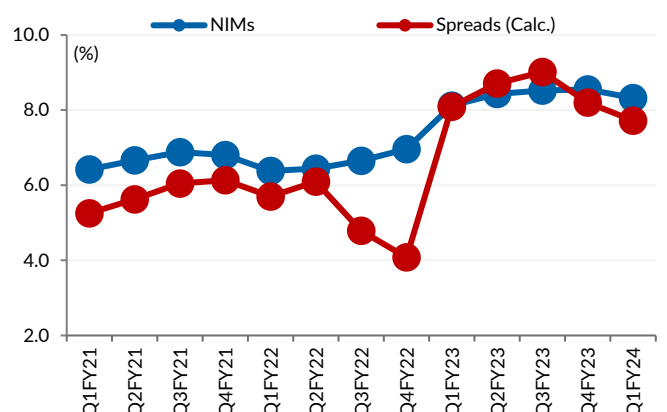
Source: Company, YES Sec

**Exhibit 14: Port. Yield has softened while CoF has risen**



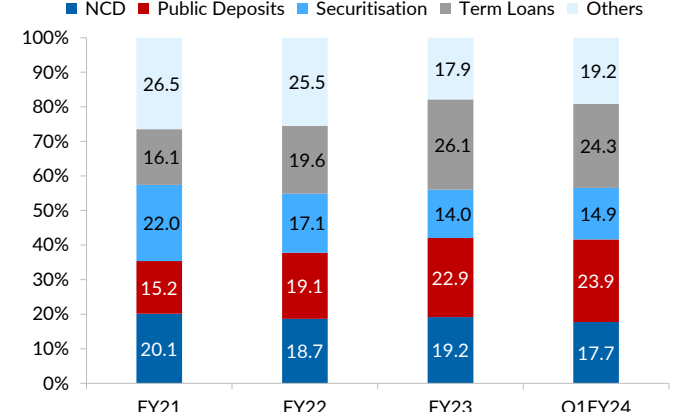
Source: Company, YES Sec, \*Data from Q1FY21-Q2FY22 pertains to Erstwhile Shriram Transport

**Exhibit 15: NIMs & Spreads to stabilize in future**



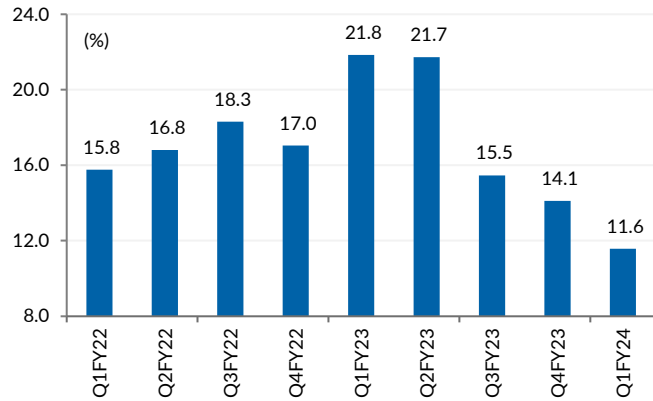
Source: Company, YES Sec, \*NIM Data from Q1FY21-Q4FY22 & Spreads data from Q1FY21-Q2FY22 pertains to Erstwhile Shriram Transport

**Exhibit 16: Borrowing mix diversified and stable**



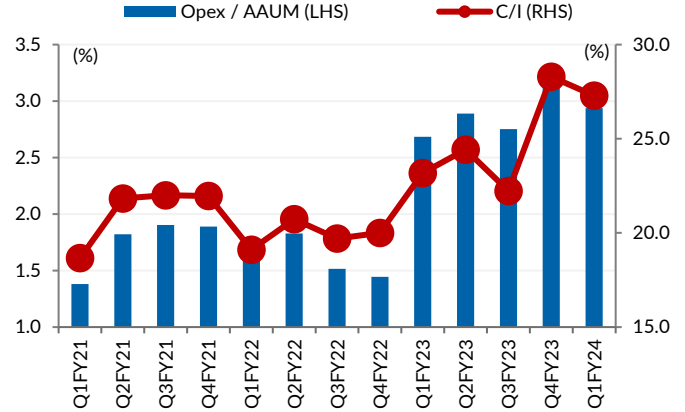
Source: Company, YES Sec, \*Data from FY21-FY22 pertains to Erstwhile Shriram Transport

**Exhibit 17: Liquidity levels on BS (% of TA) normalized**



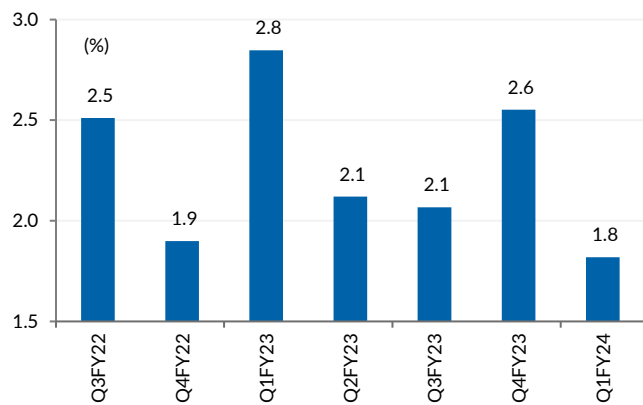
Source: Company, YES Sec, \*Data from Q1FY21-Q4FY22 pertains to Erstwhile Shriram Transport

**Exhibit 18: Opex adjustments are behind**



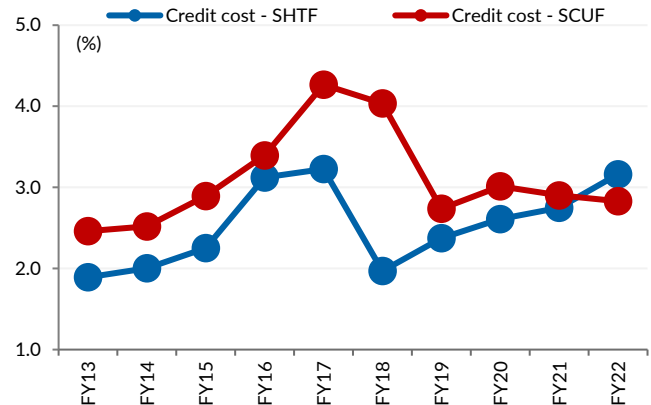
Source: Company, YES Sec, \*Data from Q1FY21-Q4FY22 pertains to Erstwhile Shriram Transport

**Exhibit 19: Merged entity credit cost to stabilize at 2%**



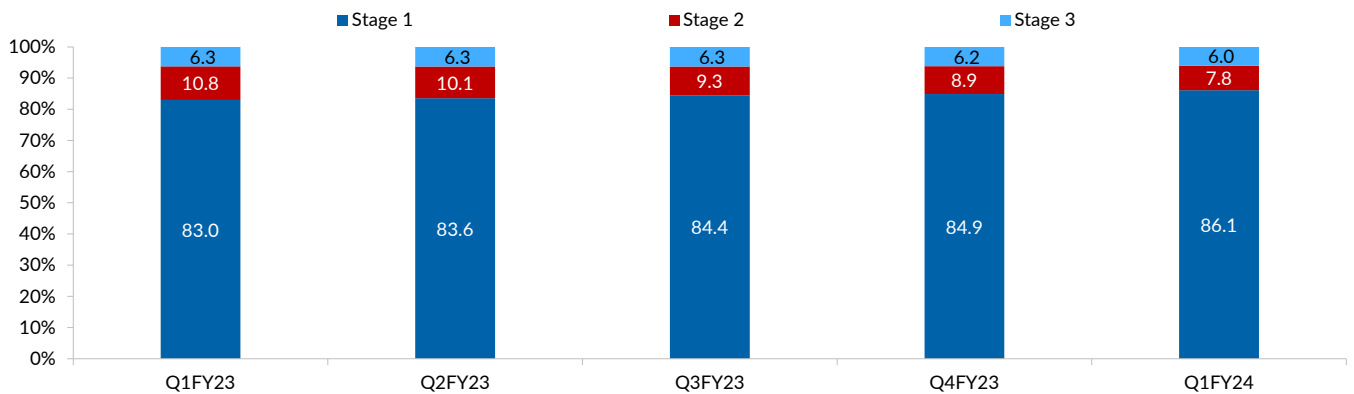
Source: Company, YES Sec

**Exhibit 20: Individual credit cost history of SHTF & SCUF**



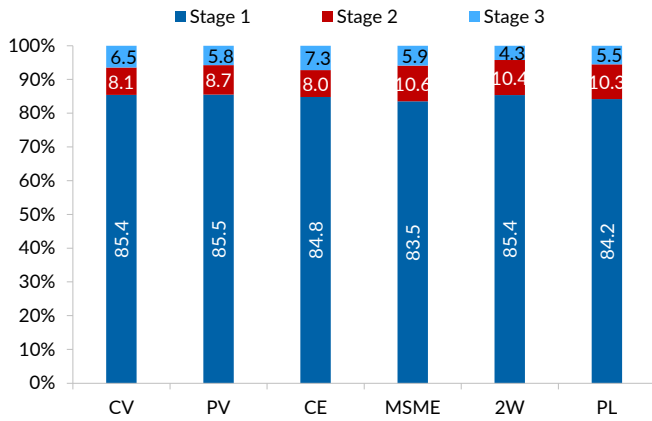
Source: Company, YES Sec

**Exhibit 21: Portfolio construct has improved meaningfully in recent quarters**



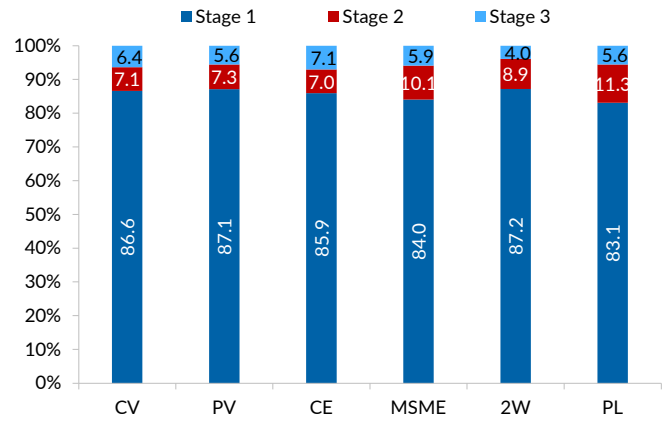
Source: Company, YES Sec

**Exhibit 22: Product-wise Portfolio Construct (Mar'23)**



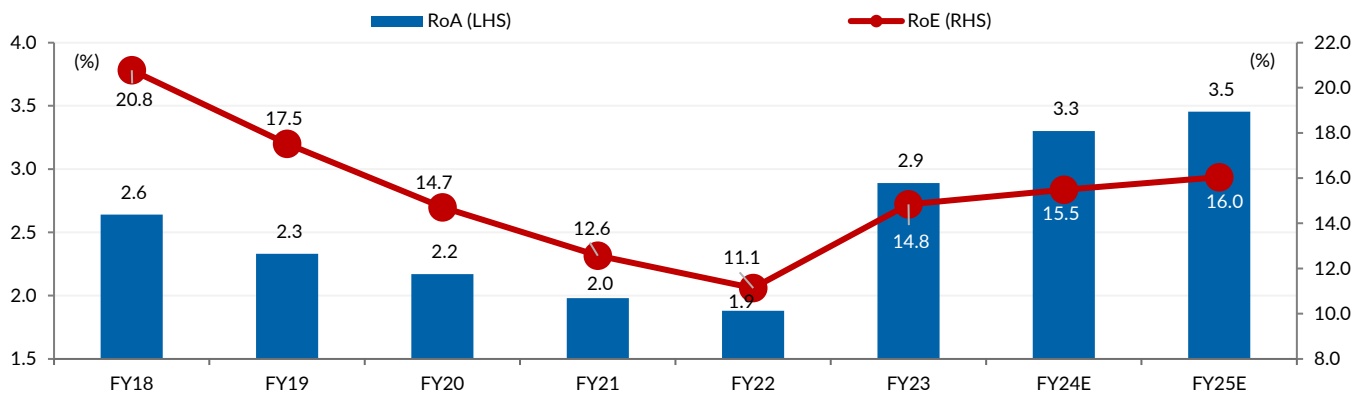
Source: Company, YES Sec

**Exhibit 23: Product-wise Portfolio Construct (June'23)**



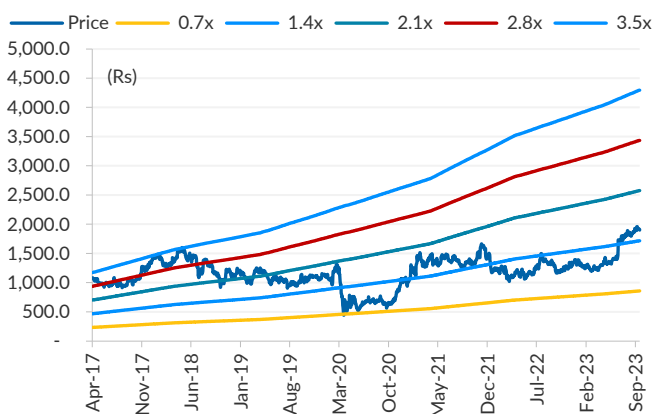
Source: Company, YES Sec

**Exhibit 24: Shriram Finance to deliver reasonably strong profitability over FY23-25**



Source: Company, YES Sec, \*Data from FY18-FY22 pertains to Erstwhile Shriram Transport

**Exhibit 25: 1-yr rolling P/ABV band**



Source: Company, YES Sec

**Exhibit 26: 1-year rolling P/ABV vis-a-vis the mean**



Source: Company, YES Sec

## FINANCIALS

### Exhibit 27: Balance Sheet

Y/e 31 Mar (Rs m)	FY21	FY22	FY23	FY24E	FY25E
Equity Share Capital	2,531	2,705	3,744	3,744	3,744
Other Equity	213,153	256,617	429,322	485,385	554,030
<b>Share-holders fund</b>	<b>215,684</b>	<b>259,322</b>	<b>433,066</b>	<b>489,129</b>	<b>557,774</b>
<b>Financial Liabilities</b>	<b>1,078,492</b>	<b>1,158,745</b>	<b>1,597,851</b>	<b>1,794,126</b>	<b>2,009,297</b>
Trade payables	1,534	1,687	2,947	0	0
Debt Securities	400,619	412,566	436,526	491,092	550,023
Borrowings (Excl. Debt Sec.)	452,814	466,769	735,900	827,888	927,234
Deposits	162,324	219,490	361,398	406,573	455,362
Subordinated Liabilities	46,208	46,143	45,239	50,893	57,001
Other Financial Liabilities	11,498	8,596	10,207	11,482	12,860
Non-Financial Liabilities	3,438	2,994	5,721	6,293	6,923
Current tax liabilities (net)	1,020	368	1,609	1,770	1,947
Provisions	1,425	1,382	2,115	2,326	2,559
<b>Other non-financial liabilities</b>	<b>993</b>	<b>1,244</b>	<b>1,998</b>	<b>2,197</b>	<b>2,417</b>
<b>Total Liabilities &amp; Equity</b>	<b>1,297,613</b>	<b>1,421,061</b>	<b>2,036,639</b>	<b>2,289,549</b>	<b>2,573,994</b>
<b>Financial Assets</b>	<b>1,282,198</b>	<b>1,402,782</b>	<b>1,973,857</b>	<b>2,226,179</b>	<b>2,509,678</b>
Cash and Cash Equivalents	110,509	106,624	95,053	121,455	129,706
Bank balances	53,909	56,927	63,121	0	0
Derivative financial instruments	1,693	2,014	6,688	7,357	8,093
Receivables	588	1,958	2,771	3,048	3,353
Loans	1,083,030	1,166,652	1,719,846	1,995,021	2,254,374
Investments	31,979	68,092	85,651	98,498	113,273
Other Financial Assets	490	515	727	800	880
<b>Non- Financial Assets</b>	<b>15,415</b>	<b>18,279</b>	<b>62,782</b>	<b>63,370</b>	<b>64,316</b>
Current tax assets (Net)	1,717	2,282	7,170	7,887	8,675
Deferred tax assets (Net)	6,391	8,694	17,439	19,183	21,101
Investment Property	20	20	26	29	32
Property, Plant and Equipment	1,244	1,106	2,095	2,304	2,535
Intangible assets	24	30	26,905	23,905	20,905
Other Non-Financial Assets	2,933	3,122	4,245	4,670	5,137
<b>Total Assets</b>	<b>1,297,613</b>	<b>1,421,061</b>	<b>2,036,639</b>	<b>2,289,549</b>	<b>2,573,994</b>

Source: Company, YES Sec.

## Exhibit 28: Income statement

Y/e 31 Mar (Rs m)	FY21	FY22	FY23	FY24E	FY25E
Income from Operations	174,205	192,552	297,722	339,610	387,455
Interest expense	(90,543)	(97,343)	(125,458)	(147,642)	(161,941)
<b>Net interest income</b>	<b>83,662</b>	<b>95,209</b>	<b>172,264</b>	<b>191,968</b>	<b>225,514</b>
Non-interest income	160	191	307	307	338
Total op income	83,821	95,399	172,571	192,275	225,852
Total op expenses	(19,857)	(21,298)	(49,131)	(57,693)	(64,196)
<b>PPoP</b>	<b>63,964</b>	<b>74,101</b>	<b>123,441</b>	<b>134,583</b>	<b>161,656</b>
Provisions	(31,184)	(38,609)	(41,592)	(38,102)	(48,172)
Profit before tax	32,780	35,493	81,849	96,481	113,483
Taxes	(7,908)	(8,413)	(22,056)	(25,085)	(29,506)
<b>Net profit</b>	<b>24,873</b>	<b>27,079</b>	<b>59,793</b>	<b>71,396</b>	<b>83,978</b>

Source: Company, YES Sec

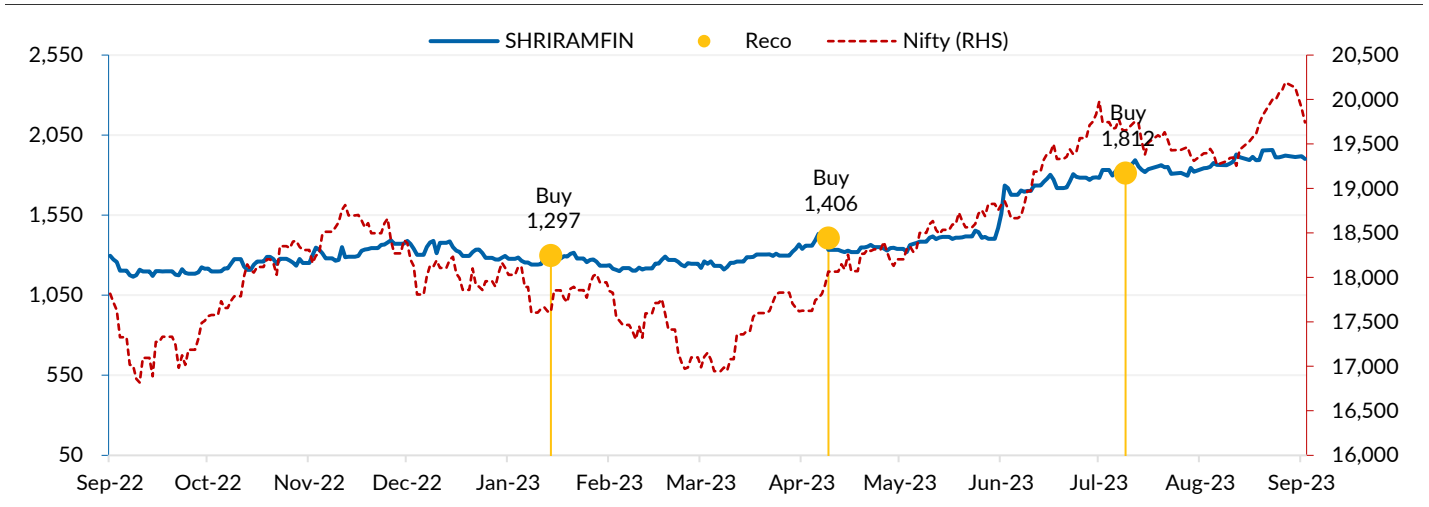
## Exhibit 29: Growth and Ratio matrix

Y/e 31 Mar	FY21	FY22	FY23	FY24E	FY25E
<b>Growth matrix (%)</b>					
Net interest income	0.9	13.8	80.9	11.4	17.5
Total op income	0.8	13.8	80.9	11.4	17.5
Op profit (pre-provision)	2.6	15.8	66.6	9.0	20.1
Net profit	(0.6)	8.9	120.8	19.4	17.6
Advances	5.9	7.7	47.4	16.0	13.0
Total Borrowings	12.5	7.8	37.9	12.5	12.0
Total assets	13.7	9.5	43.3	12.4	12.4
<b>Profitability Ratios (%)</b>					
NIM	7.4	6.9	10.0	9.6	9.8
Non-interest income /Total income	0.2	0.2	0.2	0.2	0.1
Return on Avg. Equity	12.6	11.4	17.3	15.5	16.0
Return on Avg. Assets	2.0	2.0	3.5	3.3	3.5
<b>Per share ratios (Rs)</b>					
EPS	98.3	100.1	159.7	190.7	224.3
Adj. BVPS	662.4	794.3	1005.0	1146.7	1317.3
DPS	6.0	20.0	35.0	35.0	35.0
<b>Other key ratios (%)</b>					
Cost/Income	23.7	22.3	28.5	30.0	28.4
Tier-I capital	19.9	29.9	23.3	21.4	21.7
Credit Cost	2.7	2.8	2.4	1.9	2.1
Stage 1 and 2 ECL Provision	4.1	3.9	3.3	0.0	0.0
Tax rate	24.1	23.7	26.9	26.0	26.0
Dividend yield	0.3	1.1	1.8	1.8	1.8

Source: Company, YES Sec



## Recommendation Tracker



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Name of the Research Analyst : Rajiv Mehta, Manuj Oberoi

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