



TM

SYSTEMATIX INSTITUTIONAL EQUITIES

Systematix

Institutional Equities

## Shriram Finance

27 July 2023

## Result a mixed bag; Strong on growth, weak on margins

## RESULT UPDATE

Sector: NBFCs

Rating: BUY

CMP: Rs 1,831

Target Price: Rs 2,175

## Stock Info

|                |                    |
|----------------|--------------------|
| Sensex/Nifty   | 66,266/19,699      |
| Bloomberg      | SHFL IN            |
| Equity shares  | 271mn              |
| 52-wk High/Low | 1,868/1,147        |
| Face value     | Rs 10              |
| M-Cap          | Rs 682bn/ Rs 8.3bn |
| 3-m Avg volume | USD 29.9mn         |

## Financial Snapshot (Rs bn)

| Y/E March   | FY23  | FY24E | FY25E |
|-------------|-------|-------|-------|
| NII         | 161   | 187   | 214   |
| PPP         | 123   | 138   | 160   |
| PAT         | 60    | 69    | 80    |
| EPS (Rs)    | 160   | 183   | 213   |
| EPS Gr. (%) | 58    | 15    | 17    |
| BV/Sh (Rs)  | 1,157 | 1,275 | 1,450 |

## Ratios

|               |      |      |      |
|---------------|------|------|------|
| NIM (%)       | 9.3  | 9.3  | 9.3  |
| C/I ratio (%) | 28.5 | 30.4 | 29.5 |
| RoA (%)       | 3.1  | 3.1  | 3.1  |
| RoE (%)       | 15.3 | 14.9 | 15.4 |
| Payout (%)    | 21.9 | 22.0 | 22.0 |

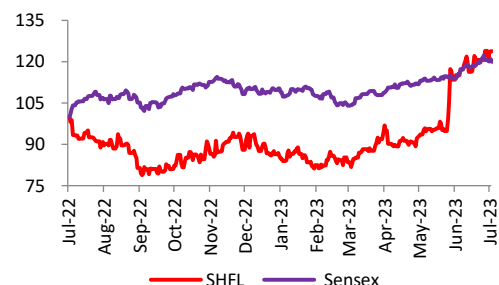
## Valuations

|                |      |      |     |
|----------------|------|------|-----|
| P/E (x)        | 11.5 | 10.0 | 8.6 |
| P/BV (x)       | 1.6  | 1.4  | 1.3 |
| Div. Yield (%) | 1.9  | 2.2  | 2.6 |

## Shareholding pattern (%)

|          | Jun'23 | Mar'23 | Dec'22 |
|----------|--------|--------|--------|
| Promoter | 25.5   | 25.3   | 25.3   |
| -Pledged |        |        |        |
| FII      | 55.4   | 49.8   | 42.9   |
| DII      | 14.7   | 11.8   | 11.1   |
| Others   | 4.5    | 12.9   | 20.7   |

## Stock Performance (1-year)



Shriram Finance (SHFL) Q1FY24 earnings were marginally lower than expected due to higher-than-expected NIM contraction and higher opex, even as AUM growth remain healthy at 18.5%yoy. NIM contracted 34Bps qoq due to a 22bps increase in cost of funds and 12bps reduction in yields. Asset quality improved marginally with Gross stage 3/2 improving by 17/23bps to 6.0%/ 3.0%, with credit cost also normalizing to 1.9% from 2.6% in Q4. Even as the opex was higher than expected, Opex/ Income ratio declined by 110bps qoq to 30.8% from 31.9% in Q4, due to higher base in Q4 on account of few one offs. Nevertheless, we remain positive on growth and asset quality. Moreover, with Piramal stake sale behind, the supply risk in the stock is no longer there, warranting the discount to historical valuation multiple to narrow. We reiterate our BUY rating on SHFL, with a target price of Rs 2,175 (Rs 1,850 earlier), valuing it at 1.5x FY25BV.

## Q1FY24 Result key highlights:

- SHFL reported robust performance for 1QFY24 with AUM growth (18.6% YoY, 4.1% QoQ) and improved asset quality. However, reported OP/PAT at Rs. 31.3bn/16.7bn was lower than the estimate of Rs 33.9bn/18.0bn due to higher-than-expected NIM contraction and higher opex.
- NIM contraction in 1QFY24 was 34Bps due to an increase in cost of funds by 22Bps and reduction in yields by 12Bps. Increase in the proportion of new vehicles to the total AUM also contributed to reduction in NIM.
- Operating expenses increased by 28%yoy (-4%qoq) led by 33% yoy (14.4%qoq) increase in employee expenses and 22%yoy (-20.%qoq) increase in other expenses. Employee expenses increased due to increase in the head count as well as annual hikes given during the current quarter. However, we note that sequentially, there was a decline in opex due to a higher base in 4QFY23 and as a result the C/I reduced to 30.8% (vs. 31.9% in 4QFY23).
- AUM grew by a healthy 4.1%qoq (18.6%yoy) aided by healthy growth across the segments viz. personal loans (+18.6% QoQ), Gold loan (+11.3% QoQ), MSME loans (+4.9% QoQ), Passengers vehicles (+7.1% QoQ), and Commercial vehicles (2.8% QoQ). This was partially offset by degrowth in farm equipment (-1.7% QoQ), and two wheeler (-3.3%).
- Asset quality saw further improvement, with Gross/ Net stage 3 at 6.0%/ 2.9% (vs. 6.2%/ 3.1% in 4Q) with adequate provision coverage at 52.5% vs. 50.1% in 4Q. Credit cost for 1QFY24 also reduced to 1.9% (vs. 2.6% in 4QFY23).

## Valuation &amp; Recommendation

While the company's performance remains healthy on growth and asset quality front, lower than expected NIMs and higher opex came in as a negative surprise. We expect the AUM/ earnings to grow at a cagr of 15% over FY24/25. While we remain positive on the growth and asset quality front, there is risk to the margins in case of further hike in policy rates by RBI. At CMP, the stock trades at attractive valuation of 1.3x FY25E BV with RoA/RoE of 3.1%/ 15.4%. We reiterate BUY rating with a revised target price of Rs 2,175 (1,850 earlier). Any significant slowdown in the economy or sharp rise in fuel costs pose key risks.

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## Exhibit 1: Quarterly performance

| (Rs mn)                         | 1QFY23        | 2QFY23        | 3QFY23        | 4QFY23        | 1QFY24        | YoY (%)          | QoQ (%)          |
|---------------------------------|---------------|---------------|---------------|---------------|---------------|------------------|------------------|
| <b>Net Interest Income</b>      | <b>38,280</b> | <b>37,775</b> | <b>41,921</b> | <b>41,810</b> | <b>42,004</b> | 9.7              | 0.5              |
| Other Income                    | 2,237         | 4,162         | 3,022         | 3,460         | 3,167         | 41.6             | -8.5             |
| Net Income                      | 40,517        | 41,937        | 44,944        | 45,270        | 45,171        | 11.5             | -0.2             |
| <b>Total Operating Expenses</b> | <b>10,841</b> | <b>11,999</b> | <b>11,928</b> | <b>14,459</b> | <b>13,908</b> | 28.3             | -3.8             |
| <i>As % Of Net Income</i>       | <i>27%</i>    | <i>29%</i>    | <i>27%</i>    | <i>32%</i>    | <i>31%</i>    | 15.1             | -3.6             |
| Employee Expenses               | 5,932         | 5,831         | 6,391         | 6,907         | 7,904         | 33.2             | 14.4             |
| <i>As % Of Net Income</i>       | <i>15%</i>    | <i>14%</i>    | <i>14%</i>    | <i>15%</i>    | <i>17%</i>    | 19.5             | 14.7             |
| Other Expenses                  | 4,909         | 6,168         | 5,537         | 7,552         | 6,004         | 22.3             | -20.5            |
| <i>As % Of Net Income</i>       | <i>12%</i>    | <i>15%</i>    | <i>12%</i>    | <i>17%</i>    | <i>13%</i>    | 9.7              | -20.3            |
| <b>Operating Profit</b>         | <b>29,676</b> | <b>29,938</b> | <b>33,016</b> | <b>30,810</b> | <b>31,262</b> | 5.3              | 1.5              |
| <i>As % Of Net Income</i>       | <i>73%</i>    | <i>71%</i>    | <i>73%</i>    | <i>68%</i>    | <i>69%</i>    | -5.5             | 1.7              |
| Provisions                      | 11,597        | 8,976         | 9,173         | 11,846        | 8,786         | -24.2            | -25.8            |
| PBT                             | 18,079        | 20,962        | 23,844        | 18,964        | 22,476        | 24.3             | 18.5             |
| Total Tax                       | 4,690         | 5,411         | 6,074         | 5,881         | 5,722         | 22.0             | -2.7             |
| <b>Adjusted PAT</b>             | <b>13,390</b> | <b>15,551</b> | <b>17,770</b> | <b>13,083</b> | <b>16,754</b> | 25.1             | 28.1             |
|                                 |               |               |               |               |               |                  |                  |
| <b>Yield Analysis (%)</b>       | <b>1QFY23</b> | <b>2QFY23</b> | <b>3QFY23</b> | <b>4QFY23</b> | <b>1QFY24</b> | <b>YoY (bps)</b> | <b>QoQ (bps)</b> |
| Yield on portfolio              | 18.1          | 18.1          | 18.1          | 17.6          | 17.5          | (57bps)          | (9bps)           |
| cost of borrowings              | 7.9           | 8.3           | 8.0           | 8.3           | 8.7           | 79bps            | 39bps            |
| Spread                          | 10.2          | 9.8           | 10.1          | 9.3           | 8.8           | (136bps)         | (48bps)          |
| NIMs (Calculated)               | 9.5           | 9.1           | 9.7           | 9.2           | 8.9           | (61bps)          | (34bps)          |
| NIMs (Reported)                 | 8.1           | 8.4           | 8.5           | 8.6           | 8.3           | 20bps            | (23bps)          |
|                                 |               |               |               |               |               |                  |                  |
| <b>Asset quality (Rs bn)</b>    | <b>1QFY23</b> | <b>2QFY23</b> | <b>3QFY23</b> | <b>4QFY23</b> | <b>1QFY24</b> | <b>YoY (%)</b>   | <b>QoQ (%)</b>   |
| Gross NPAs                      | 101           | 106           | 111           | 114           | 115           | 13.6             | 1.1              |
| Net NPAs                        | 52            | 54            | 55            | 57            | 55            | 4.9              | -3.8             |
| Gross NPAs (%)                  | 6.3           | 6.3           | 6.3           | 6.2           | 6.0           | (24bps)          | (17bps)          |
| Net NPAs (%)                    | 3.2           | 3.2           | 3.1           | 3.1           | 2.9           | (36bps)          | (23bps)          |
| Provision cover (%)             | 48.6          | 49.1          | 50.7          | 50.1          | 52.5          | 393bps           | 240bps           |
|                                 |               |               |               |               |               |                  |                  |
| <b>AUM (Rs bn)</b>              | <b>1QFY23</b> | <b>2QFY23</b> | <b>3QFY23</b> | <b>4QFY23</b> | <b>1QFY24</b> | <b>YoY (%)</b>   | <b>QoQ (%)</b>   |
| Commercial vehicles             | 850.9         | 876.8         | 906.2         | 932.9         | 959.0         | 12.7             | 2.8              |
| Passenger vehicles              | 282.5         | 300.0         | 317.7         | 338.7         | 362.9         | 28.5             | 7.1              |
| Construction equipments         | 131.7         | 133.9         | 138.7         | 143.6         | 146.3         | 11.0             | 1.8              |
| Farm equipments                 | 32.3          | 33.0          | 33.3          | 34.8          | 34.2          | 5.9              | -1.7             |
| MSME                            | 161.8         | 168.9         | 176.6         | 191.0         | 200.4         | 23.9             | 4.9              |
| 2-Wheelers                      | 83.9          | 85.1          | 100.0         | 103.7         | 100.2         | 19.5             | -3.3             |
| Gold                            | 42.0          | 44.3          | 44.4          | 44.8          | 49.8          | 18.7             | 11.3             |
| Personal loans                  | 43.7          | 51.0          | 57.7          | 66.8          | 79.2          | 81.3             | 18.6             |
| <b>Total</b>                    | <b>1,630</b>  | <b>1,694</b>  | <b>1,775</b>  | <b>1,857</b>  | <b>1,932</b>  | <b>18.6</b>      | <b>4.1</b>       |
|                                 |               |               |               |               |               |                  |                  |
| <b>Other details</b>            | <b>1QFY23</b> | <b>2QFY23</b> | <b>3QFY23</b> | <b>4QFY23</b> | <b>1QFY24</b> | <b>YoY (%)</b>   | <b>QoQ (%)</b>   |
| Branches                        | 2,840         | 2,875         | 2,901         | 2,922         | 2,930         | 3.2              | 0.3              |
| Employees                       | 54,549        | 57,382        | 60,918        | 64,052        | 66,343        | 21.6             | 3.6              |

Source: Company, Systematix Institutional Research

## Earnings call highlights

### Business:

- The management remains optimistic about demand on the back of revival of the rural economy, good monsoon, good crop production, robust GST collection. Further, the automobile industry is also doing good.
- Fintech partnerships should contribute ~5% to the AUM.
- Mix in Shriram housing finance, HL-60/65%, LAP- 30/35%
- 6-7% growth in the number of vehicles financed, and the remaining growth has come from an increase in vehicle prices.
- Investment in the subsidiary increased to 1500Cr vs. 690Cr, on account of the valuation done during the merger.
- The majority of the customers are in the rural and semi-urban regions. 70% of the customers are new to credit for unsecured loans, so to leverage more loans outside is difficult. Further, they offer it to their existing 2-Wheeler customers, and the EMI for personal loans does not exceed the EMI for the 2/3wheeler.

### Asset Quality:

- Credit cost guidance of 2% on a lot of macro factors – increase in the operating levels (demand for vehicles), higher utilization rate of the vehicles as well as increase in prices of vehicles (+25/30%). Digital payments have also improved the efficiency of the customers as well as the employees as a lot of effort is saved.
- No impact of floods on the portfolio.

### Margins:

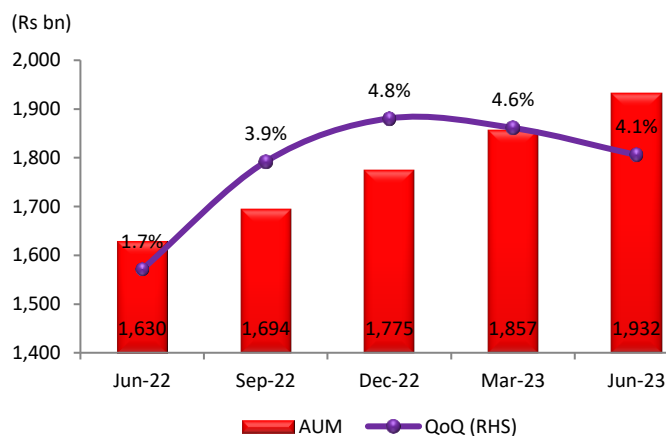
- Interest cost has gone up by 7Bps and yields has come down by 8Bps. In 1QFY23, the share of new vehicle/ CV has gone up, which has led to contraction of yield. Further, a lot of their customers shifted to new vehicles in March'23 which also resulted in lower yields (Used vehicles are high yielding).
- The repo rate is expected to be maintained at the current level.
- There will be a shift in the portfolio towards high yielding products. They are aiming to reach 8.5% by 4QFY24.
- LCR is 202%, and they will continue to maintain 3 months liability. The ideal LCR will be 150-200%.

### Opex:

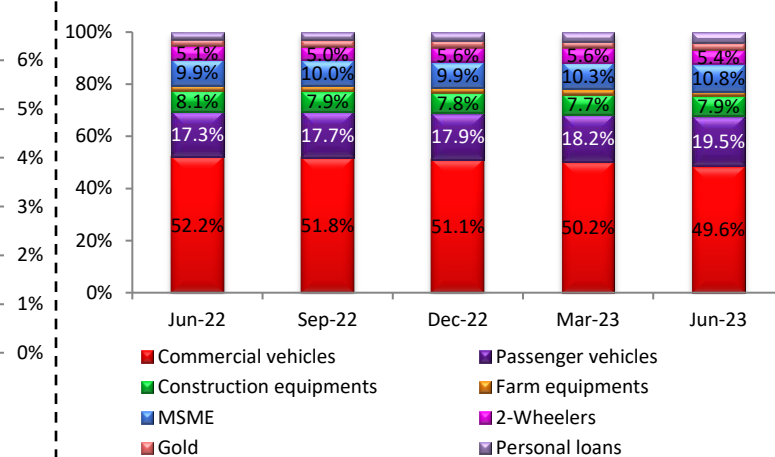
- Employee cost (Rs 100Cr) has gone up on account of increase in the head count (+2000 employees) and hike in salary which is expected to continue in the coming quarters.

### FY24 Guidance:

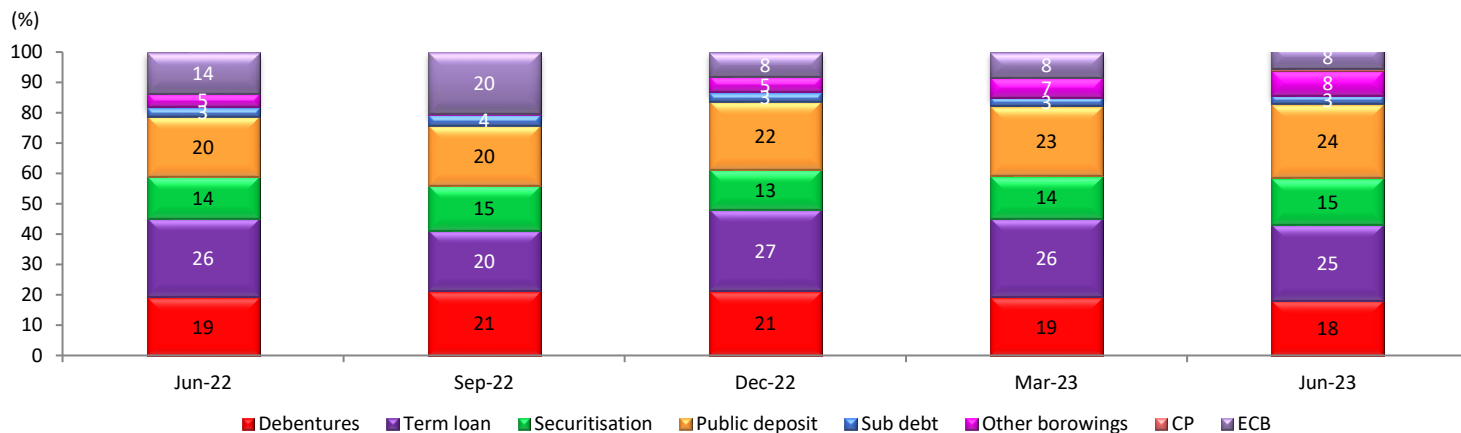
- AUM growth: 15%,
- CV portfolio- 12%, 2wheeler – 15%+ (OEM's are expecting a growth of 10%+),
- Credit cost: 2%
- NIM: 8.5%
- C/I – 27/28%.
- Shriram housing finance : RoA/RoE - 2.75-8% and 15.5%
- Shriram Finance (consolidated) RoE- 15/16% FY24.

**Exhibit 2: AUM growth remains steady**

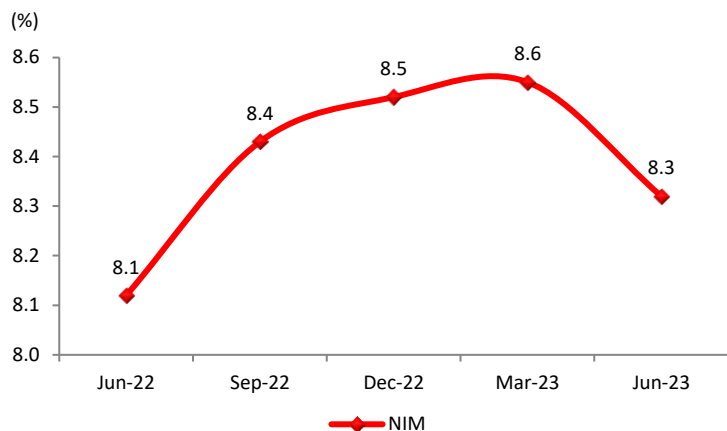
Source: Company, Systematix Institutional Research

**Exhibit 3: Product composition remain largely stable**

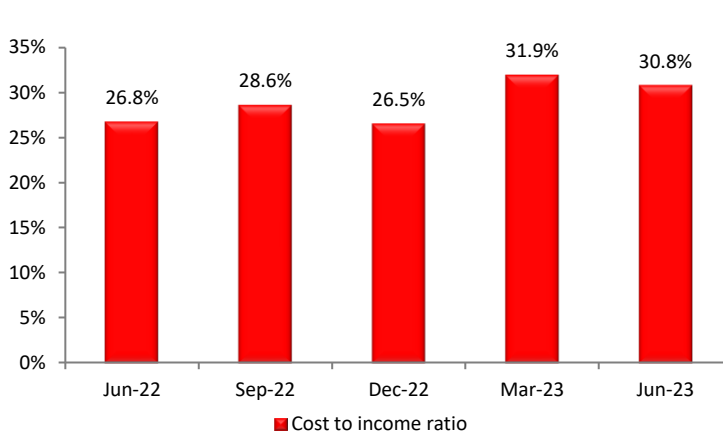
Source: Company, Systematix Institutional Research

**Exhibit 4: Diversified borrowing mix**

Source: Company, Systematix Institutional Research

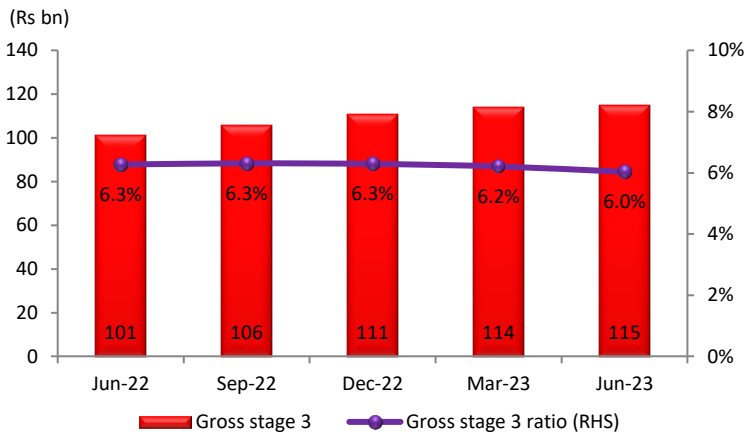
**Exhibit 5: NIMs contracted due to increase in cost of funds**

Source: Company, Systematix Institutional Research

**Exhibit 6: C/I ratio declined on higher base in Q4**

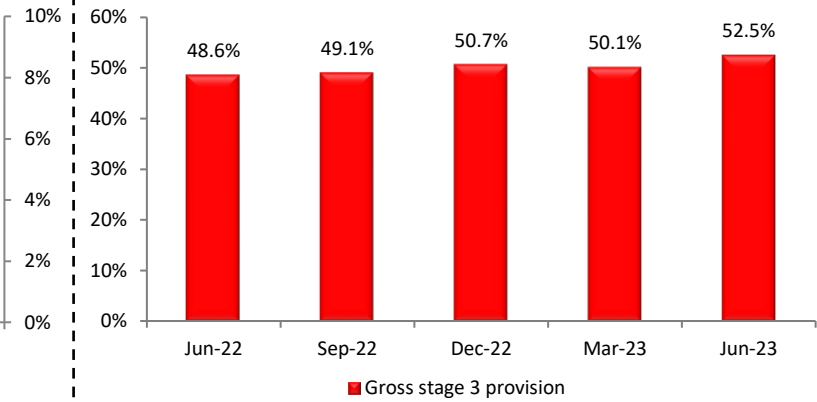
Source: Company, Systematix Institutional Research

Exhibit 7: Gross stage-3 remains steady



Source: Company, Systematix Institutional Research

Exhibit 8: Stage 3 is well provided for...



Source: Company, Systematix Institutional Research

## FINANCIALS

### Profit & Loss Statement

| YE: Mar (Rs mn)           | FY21     | FY22     | FY23     | FY24E    | FY25E    |
|---------------------------|----------|----------|----------|----------|----------|
| Net interest income       | 1,15,116 | 1,25,937 | 1,60,616 | 1,86,778 | 2,14,097 |
| Other income              | 4,733    | 9,440    | 11,955   | 11,006   | 12,705   |
| Net Income                | 1,19,848 | 1,35,376 | 1,72,571 | 1,97,784 | 2,26,803 |
| Operating expenses        | 33,484   | 37,788   | 49,131   | 60,065   | 66,803   |
| Preprovision profit       | 86,364   | 97,589   | 1,23,441 | 1,37,720 | 1,60,000 |
| Provisions                | 39,693   | 47,485   | 41,592   | 44,986   | 51,841   |
| Profit before tax         | 46,672   | 50,103   | 81,849   | 92,734   | 1,08,158 |
| Tax                       | 11,692   | 12,164   | 22,056   | 24,204   | 28,229   |
| Tax rate                  | 25       | 24       | 27       | 26       | 26       |
| Reported Profit after tax | 34,980   | 37,940   | 59,793   | 68,531   | 79,929   |

Source: Company, Systematix Institutional Research

### Dupont (as % of Average Assets)

| YE: Mar                           | FY21 | FY22 | FY23 | FY24E | FY25E |
|-----------------------------------|------|------|------|-------|-------|
| Interest Income                   | 14.7 | 14.4 | 14.8 | 15.3  | 15.3  |
| Interest Expense                  | 7.2  | 7.1  | 6.5  | 6.8   | 6.9   |
| Net Interest Income               | 7.4  | 7.3  | 8.3  | 8.5   | 8.4   |
| Other income total                | 0.3  | 0.5  | 0.6  | 0.5   | 0.5   |
| Net Income total                  | 7.8  | 7.8  | 8.9  | 9.0   | 8.9   |
| Operating expenses total          | 2.2  | 2.2  | 2.5  | 2.7   | 2.6   |
| Preprovision profit               | 5.6  | 5.6  | 6.4  | 6.3   | 6.3   |
| Provisions                        | 2.6  | 2.7  | 2.2  | 2.0   | 2.0   |
| Profit before tax and exce. items | 3.0  | 2.9  | 4.2  | 4.2   | 4.3   |
| Profit before tax                 | 3.0  | 2.9  | 4.2  | 4.2   | 4.3   |
| Tax total                         | 0.8  | 0.7  | 1.1  | 1.1   | 1.1   |
| Profit after tax                  | 2.3  | 2.2  | 3.1  | 3.1   | 3.1   |

Source: Company, Systematix Institutional Research

### Growth

| YE: Mar (%)         | FY21  | FY22 | FY23 | FY24E | FY25E |
|---------------------|-------|------|------|-------|-------|
| Net interest income | -0.4  | 9.4  | 27.5 | 16.3  | 14.6  |
| Net Income total    | -0.6  | 13.0 | 27.5 | 14.6  | 14.7  |
| Preprovision profit | 1.9   | 13.0 | 26.5 | 11.6  | 16.2  |
| Profit before tax   | -2.6  | 7.4  | 63.4 | 13.3  | 16.6  |
| Profit after tax    | -0.1  | 8.5  | 57.6 | 14.6  | 16.6  |
| Loan                | 5.3   | 8.8  | 16.5 | 15.4  | 15.2  |
| Disbursement        | -25.9 | 65.2 | 29.7 | 15.0  | 15.0  |
| AUM                 | 5.7   | 9.1  | 15.9 | 15.4  | 15.1  |

Source: Company, Systematix Institutional Research

### Balance Sheet

| YE: Mar (Rs mn)          | FY21             | FY22             | FY23             | FY24E            | FY25E            |
|--------------------------|------------------|------------------|------------------|------------------|------------------|
| Equity                   | 3,191            | 3,371            | 3,744            | 3,744            | 3,744            |
| Reserves                 | 2,93,678         | 3,45,675         | 4,29,322         | 4,82,776         | 5,45,121         |
| Net worth                | 2,96,869         | 3,49,047         | 4,33,066         | 4,86,520         | 5,48,865         |
| Borrowings               | 13,17,617        | 14,51,285        | 15,79,063        | 18,44,028        | 21,44,860        |
| Others                   | 25,228           | 21,405           | 24,509           | 37,252           | 28,152           |
| <b>Total liabilities</b> | <b>16,39,714</b> | <b>18,21,737</b> | <b>20,36,639</b> | <b>23,67,800</b> | <b>27,21,876</b> |
| Cash                     | 2,16,562         | 2,29,679         | 1,58,174         | 1,82,062         | 2,09,628         |
| Investments              | 42,152           | 86,454           | 85,651           | 1,02,811         | 1,20,844         |
| Loans                    | 13,57,232        | 14,76,890        | 17,19,846        | 19,84,811        | 22,85,643        |
| Others                   | 17,169           | 22,246           | 39,040           | 66,807           | 76,922           |
| <b>Total assets</b>      | <b>16,39,714</b> | <b>18,21,737</b> | <b>20,36,639</b> | <b>23,67,800</b> | <b>27,21,876</b> |

Source: Company, Systematix Institutional Research

### Key Ratios

| YE: Mar                | FY21    | FY22 | FY23 | FY24E | FY25E |
|------------------------|---------|------|------|-------|-------|
| Yield on portfolio     | 17.2    | 17.5 | 17.9 | 18.2  | 18.2  |
| cost of borrowings     | 9.0     | 8.9  | 8.3  | 8.7   | 8.8   |
| Spread                 | 8.2     | 8.7  | 9.6  | 9.4   | 9.5   |
| NIM (on AUM)           | 8.1     | 8.2  | 9.3  | 9.3   | 9.3   |
| Cost/ Income (%)       | 27.9    | 27.9 | 28.5 | 30.4  | 29.5  |
| Credit cost (%)        | 2.6     | 2.7  | 2.2  | 2.0   | 2.0   |
| RoA(%)                 | 2.3     | 2.2  | 3.1  | 3.1   | 3.1   |
| RoE(%)                 | 1,274.3 | 11.7 | 15.3 | 14.9  | 15.4  |
| Leverage (x)           | 5.6     | 5.4  | 4.9  | 4.8   | 4.9   |
| Tier I (%)             | 21.8    | 22.0 | 21.2 | 21.0  | 21.1  |
| CAR (%)                | 23.8    | 23.8 | 22.6 | 22.2  | 22.1  |
| Gross NPA (%)          | 6.9     | 6.9  | 6.2  | 6.3   | 6.4   |
| Net NPA (%)            | 4.0     | 3.6  | 3.3  | 3.2   | 3.2   |
| Provision coverage (%) | 44.1    | 49.8 | 50.1 | 51.0  | 52.0  |

Source: Company, Systematix Institutional Research

### Valuation ratios

| YE: Mar                  | FY21 | FY22 | FY23  | FY24E | FY25E |
|--------------------------|------|------|-------|-------|-------|
| FDEPS (Rs)               | 93   | 101  | 160   | 183   | 213   |
| PER (x)                  | 20   | 18   | 11    | 10    | 9     |
| Book value (Rs)          | 793  | 932  | 1,157 | 1,275 | 1,450 |
| P/BV (Rs)                | 2.3  | 2.0  | 1.6   | 1.4   | 1.3   |
| Adjusted book value (Rs) | 793  | 932  | 1,157 | 1,299 | 1,466 |
| P/ABV (Rs)               | 2.3  | 2.0  | 1.6   | 1.4   | 1.2   |
| P/PPP (x)                | 6.8  | 6.3  | 5.6   | 5.0   | 4.3   |
| Dividend yield (%)       | 1.2  | 1.3  | 1.9   | 2.2   | 2.6   |

Source: Company, Systematix Institutional Research

## Institutional Equities Team

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