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INSTITUTIONAL EQUITIES

Shriram Transport Finance – Positive

A Mixed Bag

Tepid disbursements; but management commentary encouraging

While an earnings growth of 17% yoy in Q3 FY19 is healthy, that street may likely overreact to tepid disbursements during the quarter. However, it needs to be interpreted in the right context. Lower originations were not driven by liquidity challenges but by a transient moderation in new/used vehicle demand, purposeful calibration in new CV and business loans segments, increase in the lending rates and tightening of LTV and other underwriting processes across products and geographies. So, if the operating environment were to start improving, as is visible in the current month, then disbursements and asset growth will pick-up. Availability and cost of funding is not a material headwind for Shriram Transport (STFC) from an earnings perspective.

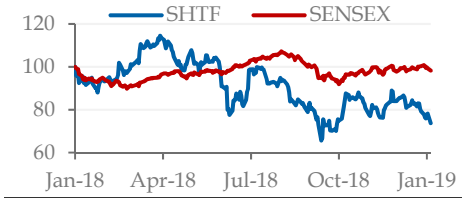
Believing that significant moderation in CV demand during Oct-Dec 2018 was a blip within a long-term upcycle, STFC expects an AUM growth of 15-18% in FY19 and 20%+ in FY20. Implementation of BS-VI norms will be a key growth trigger in the coming year, besides sustained strength in the rural economy and revival of infra and real estate activities. The company has deepened distribution in rural areas to capture market share.

CMP (Rs) 1,010

Stock data (As on Jan 29, 2019 - 11:00am) **Sector: Financials**

Sensex:	35,568
52 Week h/l (Rs)	1,671/904
Market cap (Rs mn)	229,624
Entp. value (Rs mn)	-
6m Avg t/o (Rs mn):	1,630
FV (Rs):	10
Div yield (%):	1.1
Bloomberg code:	SHTF IN
BSE code:	511218
NSE code:	SRTRANSFIN

Stock performance



Shareholding pattern (As of Dec'18 end)

Promoter	26.1%
FII+DII	53.8%
Others	20.1%

Exhibit 1: Result table

(Rs mn)	Q3 FY19	Q2 FY19	% qoq	Q3 FY18	% yoy
Operating Income	39,911	39,380	1.3	33,769	18.2
Interest Expended	(19,187)	(18,504)	3.7	(15,939)	20.4
Net Interest Income	**20,724**	**20,876**	**(0.7)**	**17,830**	**16.2**
Other income	23	98	(76.4)	11	106.3
Total Income	**20,747**	**20,974**	**(1.1)**	**17,841**	**16.3**
Operating expenses	(4,546)	(4,748)	(4.3)	(4,031)	12.8
Provisions/Impairment	(6,362)	(6,836)	(6.9)	(5,475)	16.2
PBT	9,839	9,390	4.8	8,335	18.1
Tax	(3,485)	(3,295)	5.8	(2,919)	19.4
PAT	**6,355**	**6,096**	**4.2**	**5,415**	**17.3**

Source: Company, YSL

COMPANY REPORT

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Exhibit 2: Key Ratios

	Q3 FY19	Q2 FY19	% qoq	Q3 FY18	% yoy
NIM (%)	**7.4**	**7.5**	**(0.1)**	**7.6**	**(0.1)**
Cost to Income (%)	**21.9**	**22.6**	**(0.7)**	**22.6**	**(0.7)**
BV (Rs)	663.9	641.7	3.5	534.2	24.3
RoE (%)	17.2	17.0	0.1	18.2	(1.0)
RoA (%)	2.2	2.2	0.0	2.3	(0.1)
CAR (%)	**19.7**	**16.7**	**3.0**	**15.7**	**4.1**
Gross NPA (%)	**9.0**	**8.8**	**0.2**	**8.0**	**1.0**
Net NPA (%)	2.8	2.8	0.0	2.5	0.3
PCR (%)	70.9	70.6	0.3	71.0	(0.1)

Source: Company, YSL

Exhibit 3: Business Information

Particulars (Rs mn)	Q3 FY19	Q2 FY19	% qoq	Q3 FY18	% yoy
AUM	**1,038,179**	**1,043,798**	**(0.5)**	**909,642**	**14.1**
New CVs	120,768	127,188	(5.0)	96,888	24.6
Used CVs	861,261	860,574	0.1	776,875	10.9
Business Loans	31,823	33,135	(4.0)	21,498	48.0
Working Capital Loans	23,650	21,709	8.9	13,482	75.4
Others	678	1,192	(43.1)	900	(24.7)
Urban AUM	667,500	677,400	(1.5)	627,400	6.4
Rural AUM	370,700	366,400	1.2	282,200	31.4
Loan Portfolio	845,332	878,147	(3.7)	752,337	12.4
Securitized Portfolio	192,848	165,651	16.4	157,305	22.6

Source: Company, YSL

Resilience in NIM and asset quality

Historically, STFC has demonstrated that sustaining NIM around 7.5%, even in adverse liquidity conditions, is not a big challenge. With its targeted customer segment being underserved by the formal financial system, the company's ability to raise lending rates is strong. In Q3 FY19, the increase in funding cost was transmitted instantly and the NIM was maintained despite a buffer of balance sheet liquidity (cash + investments up ~80% qoq). With collection efficiency trending well, the asset quality was stable. Management expects improvement in delinquencies and recoveries in FY20 which is reflected in its credit cost guidance of 2%.

Valuation is attractive considering earnings trajectory

With regulatory headwinds behind (90 dpd transition/Ind AS implementation) and cyclical tailwinds to stay, STFC's earnings should witness a linear progression with RoE remaining healthy over the next couple of years. We don't expect any meaningful increase in competition for the company, considering that its current business model is granular and is built on niche expertise. Post the steep price correction witnessed in the preceding months, the stock now trades at current valuation of <10x P/E and 1.8x P/ABV. Risk-reward appears attractive.

CONFERENCE CALL HIGHLIGHTS

- ✓ Management expects 2019 to be a good year for the economy as bottom-up growth drives are resilient and the election outcome is unlikely to have any durable impact. The government has announced higher MSPs and this will fuel growth in rural India.
- ✓ STFC had lower disbursements in Q3 FY19 due to a) higher lending rate, as the hike in funding cost was passed-on, b) reduction in LTV by 5-10% across products/geographies leading to higher down payment for customers, c) customers postponing vehicle purchase in reaction to the changed operating and financing environment and d) purposeful calibration of disbursements in new CV and business loans.
- ✓ The company also re-looked and strengthened its systems and processes. Macro factors like infra and RE activity slowed down and this coupled with state elections impacted CV demand. With existing vehicle utilization becoming stagnant, buying of the new vehicle was procrastinated.
- ✓ With vehicle demand improving in January, the management is confident about delivering 15-18% yoy AUM growth in the current fiscal. Asset growth in FY20 is expected to be even stronger, driven by BS-VI rollout (price increases of 10-15%) induced pre-buying. Resale prices of old vehicles will get a boost from price increases on new vehicles.
- ✓ While money supply to the real estate sector has not improved much, the housing demand seems to be reviving. Further, infra activity has picked-up in January. Better operating environment would also make STFC normalize its LTVs. FY20 AUM growth is expected to be 20%+.
- ✓ STFC's liquidity position remains strong to fund higher disbursements in Q4 FY19. The company is now keeping 3m liquidity buffer on its balance sheet as against 2m before the IL&FS issue. In comparison to most other NBFCs, STFC can raise money from various avenues comfortably.
- ✓ The company is not facing any constraints with regards to raising loans from Private Banks. Securitization/Assignments, Bonds/ ECBs, Retail NCDs and deposits remain active channels for financing. STFC plans to raise Rs100bn in FY20 through a retail NCD issue in FY20. It has headroom to raise ECB worth US$400mn. Thus, funding growth in FY20 will not be a challenge. As per the management, incremental cost of borrowing seems to have peaked.
- ✓ The collection efficiency has stayed strong in Q3 FY19 and GS-3 assets were stable. While some idling of vehicles (couple of days) was witnessed, it is expected to recover in the coming months with new vehicle additions having slowed down. The company is comfortable with current GS-3 levels as the customers have the intention and resilience to pay.
- ✓ STFC's customers are generally able to source business by going to neighboring areas and product segments. The company is facing some challenges in parts of Maharashtra and MP due to a drought-like situation, but it is likely to be transient. In Tamil Nadu, STFC's growth and asset quality remains heathy. Overall, the management expects credit cost to decline to 2% in FY20.
- ✓ Equity capital raise could take place in FY20, if 18-20% asset growth looks sustainable in the subsequent years.

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BUY > 15%

ADD 5% to 15%

HOLD -15% to +5%

SELL > - 15%

NOT RATED

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