

Shriram City Union Finance Ltd

Sector: NBFC /Small-Cap | Earnings Update – 3QFY19

BUY

29 January 2019

Background: Shriram City Union Finance (SCUF), the retail finance arm of the Shriram Group, offers diversified loan products ranging from low risk (loan against gold) to high risk segments (small business loans and two-wheeler financing). Strong group parentage (three decades expertise in the finance services space) is among the key positives. The company benefits from Shriram Chits' branch infrastructure and existing customers, deriving more than 85% of its business from Shriram Chits' network. Shriram City operates through a wide distribution network of ~969 branches, 600 of them are owned by Shriram City and the rest are shared with group companies.

Sensex	35,592
Nifty	10,652
Price	INR 1,716
Target Price	INR 1,950
Recommendation	BUY

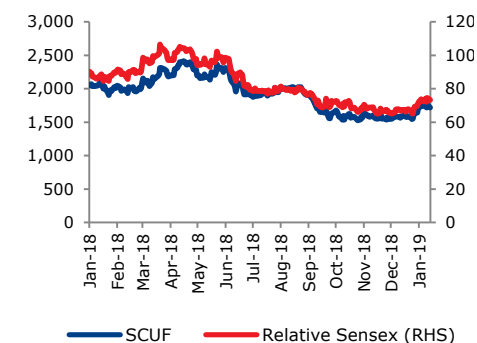
52 Week High/Low	INR 2,454/1,480
Bloomberg / Reuters	SCUF IN / SHCU.BO
Equity (shares in mn)	65.97
Mkt. Cap in bn	INR 113.20/ \$ 1.59
Avg. Daily Vol. ('000)	34.95
Avg. Daily Vol. (mn)	INR 59.98 / \$ 0.84

Shareholding	Dec 17	Sep 18	Dec 18
Promoters (%)	33.76	33.75	33.75
FII (%)	25.77	24.63	24.74
DII (%)	5.55	6.85	7.00
Others (%)	34.92	34.77	34.51
Pledge (% of promoter holding)	0.00	0.00	0.00

Valuation Summary (INR bn)

Y/E March	2019E	2020E	2021E
Net Interest Inc	39.0	46.6	55.2
Other Inc	1.0	1.3	1.5
Pre Prov Profit	24.0	29.6	32.7
PAT	10.0	12.4	13.8
EPS	151.6	187.6	208.4
EPS growth (%)	45.5	23.7	11.1
PE	11.3	9.1	8.2
P /ABV	1.8	1.6	1.3
Div Yield (%)	0.7	0.8	0.9
ROA (%)	3.3	3.5	3.5
ROE (%)	17.3	17.5	18.3
CAR (%)	23.0	22.6	22.1

Performance %	1M	3M	12M
SCUF	-1.7	-16.4	-25.7
Sensex	-1.2	6.9	-1.1



Muted disbursements, however improvements seen in credit costs and opex

- SCUF's, AUM grew by 9.6% YoY to INR 288bn in 3QFY19 (vs. CSEC estimate of 11% YoY) predominantly led by growth in SME (18.2%YoY), 2Ws segment (9.1%YoY), and Other Non-gold loans (4.4%YoY). Consequently the loan mix was noted at SME segment (59.7%), Two Wheeler (18.3%), Loan against gold (9.6%) and Others(12.4%). Management retains its growth guidance of 18-20% CAGR over FY19-20E, to be predominantly driven by SME and 2W segments.
- Overall disbursements de-grew by 28% YoY in 3QFY19 to INR 45.8bn, owing to the liquidity crunch witnessed in the NBFC space. During the quarter, disbursements were largely seen in SME and in 2W segment, constituting 39% and 23% respectively of the overall disbursements.
- Total Borrowings of the company stood at INR 224bn as at 3QFY19, growing at 12.9% YoY. Currently, bank borrowings constitute 54% of the overall borrowings and ~30% comprises of market borrowings. In 3QFY19 the average cost of funds spiked by 49bps YoY to 9.27%.
- Average yield on assets also plunged by 155bps YoY to 19.68% (due to INR 18.5bn held as undisbursed cash during the quarter), resulting in a 220bps YoY contraction in NIMs. The management highlighted that, in the coming quarters, cost of funds would continue to remain elevated.
- Asset quality improved sequentially, with the Gross Stage-3 (GS-3), equivalent of erstwhile GNPA, down by 39bps QoQ to 9.63%. In absolute numbers, GS-3 advances dropped by 8.3% QoQ and stood at INR 27bn during the quarter. Hence provisions this quarter were down by 47% QoQ and the coverage ratio for GS-3 assets inched up to 48.51% from 48.24% in 2QFY19.
- The Net Interest income de-grew by 3.1% YoY to INR 9.1bn (CSEC's estimate of INR 9.87bn), due to fall in yields and moderate growth in disbursements. Despite a 3.6% YoY drop in opex (due to lower disbursements in 2W segment and reduction in employee bench strength), operating profits were down by 5.3% YoY due to fall in other income (by 97% YoY). Cost to Income ratio was however, down by 20bps YoY to 41.1%.
- PAT for the quarter stood at INR 2.59bn up by 2%YoY (in line with CSEC estimate of INR 2.4bn), led by decline in provisioning costs (down by 27%YoY).
- In 1QFY19, the RoE dropped to 16.2%, due to the adoption of Ind- AS, and the management had guided to achieve a RoE of 18-20% over FY19-20E (as per IND-AS). In 3QFY19, however due to muted disbursement growth, ROE dipped by 7bps sequentially. Going ahead, with streamlining credit policies, and muted growth in opex, we expect the return ratios to improve.
- Shriram Housing Finance Ltd (Subsidiary) saw a 93% YoY de-growth in disbursements, which stood at INR 110mn for 3QFY19. Overall AUM was up by 7% YoY and is currently at INR 17.21bn. GNPA's as per Ind-AS fell by 341bps YoY to 3.22%. Cost to Income ratio (as per Ind-AS) also fell by 127bps to 65.96% from 67.23% in 3QFY18.

Valuation: With the credit quality expected to be maintained at current levels (aided by uniform underwriting practices) and cut down in opex by employee reduction, we expect the return ratios to improve going forward. However, due to increase in cost of funds, near term pressures remain on NIMs and disbursement growth. The stock is currently trading at 1.3X P/ABV of FY21E. We give the stock a BUY rating with a target price of INR 1,950, assigning a P/ABV of 1.5X on FY21E.

Risks: Slower ramp up in loan book and any stress in the SME segment might impact earnings.

Results Summary 3QFY19

Y/E March (INR mn)	3QFY19	3QFY18	YoY Growth	2QFY19	QoQ Growth
Net Interest Income	9,095.6	9,390.0	-3.1%	10,189.2	-10.7%
Other Income	4.4	151.7	-97.1%	8.4	-47.6%
Pre Provisioning Profit	5,360.0	5,661.7	-5.3%	6,227.6	-13.9%
PAT	2,590.0	2,540.0	2.0%	2,490.0	4.0%
Cost / Income (%)	41.1	41.3		38.9	
GS-3 (%)	9.6	9.6		10.0	
Net GS-3 (%)	5.0	5.2		5.2	
Coverage GS-3 (%)	48.5	46.2		48.2	
CAR (%)	23.0	22.8		20.8	

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