

Cholamandalam Investment

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Earnings beat on stable margins and reduced credit costs

- **Result highlights:** Cholamandalam Investment and Finance Company (CIFIC) reported Q3FY23 standalone PAT of ~Rs6.8bn (+21.5% QoQ/+30.6% YoY), ~16%/~14% above ours/consensus estimates, primarily driven by lower provisioning in the current quarter. The highest-ever disbursements in the vehicle finance segment drove AUM growth of 8.9% QoQ/ 31.3% YoY. Within vehicle finance, portfolio growth was driven by MUV (+11% QoQ), cars (+8% QoQ), and CE (+9% QoQ). Contrary to our expectations, margins were broadly flat QoQ, with the rise in CoF offset by the NBFC passing on rate hikes on its floating rate loans, higher composition of new business loans coupled with income from treasury operations. Operating expenses continued to remain elevated on account of continued investments in new business verticals coupled with higher variable pay in line with heightened business volumes during the quarter. Asset quality improved QoQ with GS3 and NS3 declining by 33bps and 18bps QoQ to 3.51% and 2.07%, respectively. Credit costs came in at ~0.7%, resulting in earnings growth of 21.5% QoQ/30.6% YoY and quarterly RoA of ~2.8% translating into RoE of ~20.8%.
- We rollover our estimates to Mar-24E and retain our BUY rating with a Mar-24E TP of Rs950 (earlier Rs860), valuing the company using the excess return on equity (ERE) method. Our TP implies Mar-25E P/BVPS of 3.8x for FY25 RoA of ~2.6% and RoE of ~21.5%. **Key downside risks:** Asset-quality stress in the new business verticals.

- **What we liked:** 1) Highest-ever disbursements in vehicle finance (VF) and continued scale up of the SME/consumer business augur well for growth, 2) Margin stability sequentially coupled with guidance for higher NIM, 3) Management's guidance for lower credit costs in Q4FY23 vs. Q3FY23. **What we did not like:** Continued elevated operating expenses weighed down on profitability.
- **Margins pressure on VF portfolio negated via rate hikes:** During Q3FY23, margins were flat on account of higher cost of funds (60% of the borrowings are floating), offset by increased yields due to pass through of rate hikes in the floating rate book (~40% of the loans are floating). LAP/HL have been repriced by 160bps/130bps YTD. CIFIC is contemplating a further 40bps rate hike and will decide on the same after the February 2023 MPC meet. Management has also guided for higher margins as the proportion of new loans in the fixed-rate VF portfolio rises along with increased contribution of the new business verticals.
- **Lower provisioning drives earnings beat:** Asset quality improved sequentially, with GS3 at 3.51% (Q2: 3.84%) and NS3 at 2.07% (Q2: 2.25%). PCR on stage-3 assets stood at ~41% (Q2:41.5 %). Credit cost came at ~0.7% due to reversal of provision on standard assets and lower-than-expected write-offs during the quarter. The restructured book stood at ~Rs.28bn (2.9% of business AUM) vs. ~Rs.35bn (4% of business AUM) as of Q2FY23. CIFIC retains management overlay provisions of Rs5bn (Q2: Rs5.3bn).

Financial Snapshot (Standalone)

(Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net income	49,997	58,400	71,743	93,746	1,17,563
Net profit	15,141	21,467	25,704	31,984	40,325
EPS (Rs)	18.5	26.1	31.2	38.9	49.0
BV (Rs)	116.5	142.4	171.0	206.0	250.2
RoA (%)	2.2	2.7	2.6	2.5	2.6
RoE (%)	17.1	20.2	19.9	20.6	21.5
PE (x)	40.6	28.7	24.0	19.3	15.3
P/BV	6.4	5.3	4.4	3.6	3.0

Source: Company, Emkay Research. emkay@whitemarquesolutions.com use and downloaded at 02/03/2023 11:15 AM

CMP	Target Price
Rs 750 as of (February 1, 2023)	Rs 950 (▲) 12 months
Rating	Upside
BUY (■)	26.7 %

Change in Estimates

EPS Chg FY23E/FY24E (%)	-/
Target Price change (%)	10.5
Target Period (Months)	12
Previous Reco	BUY

Emkay vs Consensus

EPS Estimates		
	FY23E	FY24E
Emkay	31.2	38.9
Consensus	29.7	36.5
Mean Consensus TP (12M)	Rs 832	

Stock Details

Bloomberg Code	CIFIC IN
Face Value (Rs)	2
Shares outstanding (mn)	822
52 Week H/L	818 / 594
M Cap (Rs bn/USD bn)	616 / 7.52
Daily Avg Volume (nos.)	15,67,934
Daily Avg Turnover (US\$ mn)	13.7

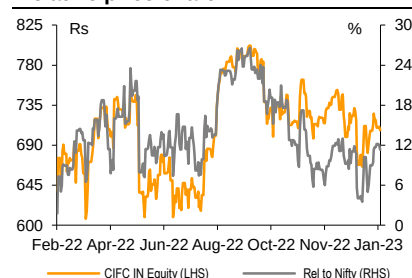
Shareholding Pattern Dec '22

Promoters	51.5%
FIIIs	19.4%
DIIIs	21.2%
Public and Others	7.9%

Price Performance

(%)	1M	3M	6M	12M
Absolute	4	6	2	15
Rel. to Nifty	7	9	1	14

Relative price chart



Source: Bloomberg

This report is solely produced by Emkay Global. The following person(s) are responsible for the production of the recommendation:

Manjith Nair
manjith.nair@emkayglobal.com
+91 22 661 21358

Rhave Shah
rhaveshah@emkayglobal.com
+91 22 6612 1284

Kishan Rungta
kishan.rungta@emkayglobal.com
+91 22 6624 2490

- **Management guidance:** Management has laid out the following targets going ahead – 1) business AUM growth of 27-30% for FY23E (20-22% earlier). YTD growth stood at ~24%. 2) While CoF are expected to increase by 40-50bps for FY23E, CIFIC is negotiating with banks for lower rates. 3) PBT-RoTA of more than ~3.5%. 4) Credit cost to be maintained at below 1% levels in the long term and 5) Securitization volumes to be higher in Q4.
- **Changes in estimates:** We have revised upwards our earnings estimates to account for the strong disbursement and business AUM growth reported in Q3FY23. This coupled with expected credit costs improvement in Q4FY23 results in our PAT estimates for FY23E to be revised upwards by ~11%. We now build in a 42% disbursement CAGR over FY22-25E, resulting in business AUM CAGR of 28% over the same period. While management has guided for credit costs of <100bps, we have broadly retained our credit cost estimates for FY24-25E at ~130bps to account for higher credit costs expected in the new business verticals of SME and consumer finance. We have revised downwards our operating expense estimates for FY24-25E to factor in the benefits of scale in the new businesses and management's guidance on the same.

Exhibit 1: Quarterly Financials

Rs mn	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	FY23E	FY24E	YoY (%)
Net Interest Income	13,634	13,679	14,814	14,888	15,983	17.2%	7.4%	63,153	83,320	32%
Other Income	1,378	1,927	1,587	2,085	2,334	69.4%	11.9%	8,590	10,426	21%
Total Income	15,012	15,606	16,401	16,974	18,317	22.0%	7.9%	71,743	93,746	31%
Operating Expenses	5,317	6,486	5,797	6,611	7,520	41.4%	13.8%	28,024	35,885	28%
Operating Profit	9,696	9,120	10,604	10,363	10,797	11.4%	4.2%	43,719	57,861	32%
Provisions	2,653	(174)	2,986	2,782	1,589	-40.1%	-42.9%	9,125	14,814	62%
Credit costs (%)	1.5%	-0.1%	1.5%	1.3%	0.7%	-79bps	-62bps	1.0%	1.3%	25bps
PBT	7,043	9,294	7,617	7,581	9,208	30.7%	21.5%	34,594	43,047	24%
Tax	1,805	2,398	1,961	1,947	2,365	31.1%	21.5%	8,891	11,063	24%
Tax rate (%)	25.6%	25.8%	25.7%	25.7%	25.7%			25.7%	25.7%	
PAT	5,238	6,896	5,657	5,634	6,843	30.6%	21.5%	25,704	31,984	24%
Disbursements	1,04,300	1,27,180	1,33,300	1,46,230	1,75,600	68.4%	20.1%	6,39,117	8,05,648	26%
Business AUM	7,27,240	7,69,070	8,19,260	8,76,680	9,54,670	31.3%	8.9%	10,34,025	13,17,109	27%
GS3 (%)	5.9%	4.4%	4.2%	3.8%	3.5%	-234bps	-33bps	3.6%	3.5%	-9bps
NS3 (%)	3.6%	2.6%	2.5%	2.3%	2.1%	-151bps	-18bps	2.2%	2.2%	-5bps
PCR (%)	38.0%	39.7%	40.7%	41.5%	41.0%	296bps	-52bps	40.3%	40.0%	-25bps

Source: Company, Emkay Research

Exhibit 2: Actuals vs. Estimates (Q3FY23)

Rs mn	Actual	Estimate (Emkay)	% variation Emkay	Comments
Disbursement	1,75,600	1,57,095	11.8%	While we had built-in growth in VF disbursement, actual disbursements still came in higher.
Business AUM	9,54,670	9,34,538	2.2%	
NII	15,983	15,363	4.0%	While the VF segment margins were impacted by 40 bps sequentially, they were compensated by NIM improvement in the other segments.
PPOP	10,797	10,715	0.8%	Operating expenses were elevated due to investments and higher business momentum.
PAT	6,843	5,883	16.3%	Lower-than-expected provisions due to reversals and lower net write-offs.

Source: Company, Emkay Research

Exhibit 3: Revision in earnings estimates

Y/E March (Rs mn)	FY23E			FY24E			FY25E		
	Earlier	Revised	% change	Earlier	Revised	% change	Earlier	Revised	% change
Disbursement	5,82,791	6,39,117	9.7%	7,29,700	8,05,648	10.4%	8,74,379	10,11,265	15.7%
Business AUM	9,82,341	10,34,025	5.3%	12,22,700	13,17,109	7.7%	14,68,861	16,12,576	9.8%
Net interest income	62,822	63,153	0.5%	78,700	83,320	5.9%	96,717	1,05,198	8.8%
PPOP	43,884	43,719	-0.4%	53,934	57,861	7.3%	65,794	72,756	10.6%
PAT	23,202	25,704	10.8%	29,603	31,984	8.0%	35,859	40,325	12.5%
EPS (Rs)	28.2	31.2	10.8%	36.0	38.9	8.0%	43.6	49.0	12.5%
BV (Rs)	168	171	1.7%	201	206	2.7%	240	250	4.3%
NIM (%)	7.17%	7.00%	-17bps	7.14%	7.09%	-5bps	7.19%	7.18%	-1bps
Cost-to-income ratio (%)	37.8%	39.1%	128bps	38.6%	38.3%	-33bps	38.8%	38.1%	-64bps
Opex-to-AUM (%)	3.0%	3.1%	7bps	3.1%	3.1%	-2bps	3.1%	3.1%	-4bps
Disbursement growth (%)	64.2%	80.1%	1587bps	25.2%	26.1%	85bps	19.8%	25.5%	569bps
AUM growth (%)	27.7%	34.5%	672bps	24.5%	27.4%	291bps	20.1%	22.4%	230bps
Credit costs (%)	1.4%	1.0%	-43bps	1.3%	1.3%	-2bps	1.3%	1.3%	-4bps

Source: Company, Emkay Research

Con-call Highlights

- Highest-ever disbursements, crossing ~Rs100bn for the VF segment in Q3FY23.
- Healthy liquidity position with cash and bank balance at ~Rs73.96bn and overall liquidity of ~Rs100bn. ALM is comfortable with no negative cumulative balance mismatch across all buckets.
- Higher operating expenses were due to increased disbursement and investment towards technology development. Benefits in terms of lower operating expenses are expected to be realized over the next one year.
- Home Equity Stage 3 was marginally higher and has been continuously declining. Over the past nine months, it has reduced from 7.93% to 4.76%, i.e., a ~300 bps reduction, which is reflected in the almost close-to-zero credit cost.
- Disbursement is flat on a QoQ basis mainly due to more granularity in the portfolio, lower ticket size while increasing the number of accounts – management is comfortable with this kind of expansion, and good growth can be expected next year.
- Consumer loan (PL/BL) market share is hardly 0.8-0.9%, and CIFIC wants to do this business and expand it like the VF business. Currently, BL/PL has only 50% the number of touchpoints as the VF business..
- Management is fundamentally maintaining a cautious approach towards PL/BL and not going to mini-markets where the bounce rate is on the higher side.
- PL/BL is 100% scorecard based. 96% of customers in the PL/BL/consumer business have been acquired over the past year, and have a credit score of 700+.
- Underwriting of PL/BL is fully digitalized. Credit score is strictly monitored with a minimum score of 700+. The existing efficiency is 99.72% in the current bucket and the bounce rate is sub-5%. The first EMI bounce is sub-3% with 100% clearance on MoM basis.
- CoF is expected to increase by 40-50bps on a YoY basis, but CIFIC will try to mitigate this by scaling up pricing in the floating rate book, which is LAP and HL. LAP and HL have been repriced by 160bps and 130bps YTD, respectively.
- Management is contemplating another 40bps increase. It is to be decided after the MPC meet of February 2023.
- The restructured book stood at Rs28bn (stage 1: ~Rs3bn, stage 2: ~Rs20bn, stage 3: ~Rs5bn.)
- LAP margin rose from 4.82% to 5.46% YTD. For HL, margins rose from 7.59% to 8.02%. This has been offset by VF margins declining from 8.67% to 8.48% YTD.

Key Financials (Standalone)**Income Statement**

Y/E March (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net interest income	46,483	52,680	63,153	83,320	1,05,198
Other income	3,514	5,720	8,590	10,426	12,364
Net income	49,997	58,400	71,743	93,746	1,17,563
Operating expenses	15,843	20,687	28,024	35,885	44,807
Pre provision profit	34,154	37,712	43,719	57,861	72,756
PPP excl treasury	34,154	37,712	43,719	57,861	72,756
Provisions	13,778	8,803	9,125	14,814	18,483
Profit before tax	20,376	28,909	34,594	43,047	54,273
Tax	5,235	7,442	8,891	11,063	13,948
Tax rate	26%	26%	26%	26%	26%
Profit after tax	15,141	21,467	25,704	31,984	40,325

Balance Sheet

Y/E March (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Equity	1,641	1,643	1,643	1,643	1,643
Reserves	93,962	1,15,434	1,39,085	1,67,875	2,04,174
Net worth	95,603	1,17,077	1,40,727	1,69,518	2,05,817
Other liabilities and provisions	12,581	14,822	16,279	17,881	19,640
Borrowings	6,37,300	6,91,735	9,61,695	12,24,977	14,99,776
Total liabilities	7,45,484	8,23,634	11,18,701	14,12,376	17,25,234
Cash and bank	52,319	42,201	75,634	87,685	1,06,416
Investments	16,188	20,762	9,617	12,250	14,998
Loans	6,58,393	7,41,492	10,12,310	12,89,449	15,78,712
Others	18,584	19,179	21,140	22,992	25,108
Total assets	7,45,484	8,23,634	11,18,701	14,12,376	17,25,234

Key Ratios (%)

Y/E March	FY21	FY22	FY23E	FY24E	FY25E
NIM	7.1	7.2	7.0	7.1	7.2
RoA	2.2	2.7	2.6	2.5	2.6
RoAE	17.1	20.2	19.9	20.6	21.5
GNPA (%)	4.0	4.4	3.6	3.5	3.6
NNPA (%)	2.3	2.7	2.2	2.2	2.2

Per Share Data (Rs)	FY21	FY22	FY23E	FY24E	FY25E
EPS	18.5	26.1	31.2	38.9	49.0
BVPS	116.5	142.4	171.0	206.0	250.2
DPS	2.0	2.0	2.5	3.9	4.9

Valuations (x)	FY21	FY22	FY23E	FY24E	FY25E
PER	40.6	28.7	24.0	19.3	15.3
P/BV	6.4	5.3	4.4	3.6	3.0
Dividend Yield (%)	0.3	0.3	0.3	0.5	0.7

Source: Company, Emkay Research

Growth (%)	FY21	FY22	FY23E	FY24E	FY25E
NII	23.0	13.3	19.9	31.9	26.3
PPOP	37.5	10.4	15.9	32.3	25.7
PAT	43.9	41.8	19.7	24.4	26.1
Loans	18.8	12.6	36.5	27.4	22.4

Quarterly (Rs mn)	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23
NII	13,634	13,679	14,814	14,888	15,983
NIM (%)	7.6%	7.3%	7.5%	7.0%	7.0%
PPOP	9,696	9,120	10,604	10,363	10,797
PAT	5,238	6,896	5,657	5,634	6,843
EPS (Rs)	6.38	8.40	6.89	6.86	8.33

Source: Company, Emkay Research

Shareholding Pattern (%)	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Promoters	51.6	51.6	51.5	51.5	51.5
FIIIs	17.7	17.6	18.0	18.7	19.4
DIIIs	22.8	23.0	22.4	21.9	21.2
Public and Others	8.0	7.8	8.1	7.9	7.9

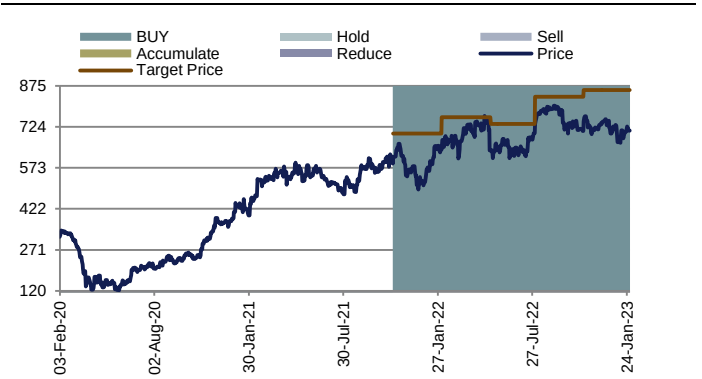
Source: Capitaline

RECOMMENDATION HISTORY TABLE

Date	Closing Price	TP	Period (months)	Rating	Analyst
02-Dec-22	732	860	12m	Buy	Manjith Nair
02-Nov-22	745	860	12m	Buy	Manjith Nair
01-Aug-22	734	835	12m	Buy	Manjith Nair
08-May-22	637	735	12m	Buy	Manjith Nair
03-Feb-22	643	760	12m	Buy	Manjith Nair
02-Nov-21	610	700	12m	Buy	Manjith Nair

Source: Company, Emkay Research

RECOMMENDATION HISTORY CHART



Source: Bloomberg, Company, Emkay Research

Emkay Rating Distribution

Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

Completed Date: 02 Feb 2023 01:12:56 (SGT)
Dissemination Date: 02 Feb 2023 01:13:56 (SGT)

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7th Floor, The Ruby, Senapati Bapat Marg, Dadar - West, Mumbai - 400028. India

Tel: +91 22 66121212 Fax: +91 22 66121299 Web: www.emkayglobal.com