BUY Cholamandalam Investment

Staying on course

BFSI - NBFCs ▸ Result Update ▸ **August 2, 2023**

TARGET PRICE (Rs): 1,215

In Q1FY24, CIFC continued its strong disbursements and AUM growth, despite a seasonally weak quarter; however, profitability missed our estimates on some pressure on NIM and increased credit cost. Going ahead, margins are likely to improve, with easing cost of funds and higher yielding fixed rate new loans aiding loan book yields and improving credit cost helping overall profitability. Overall, the CIFC's profitable growth story, powered by its strength in core vehicle finance and accelerated growth in newer segments, stays on course. The planned ~Rs40bn capital raise should improve the capital adequacy by ~4ppts and support stronger growth for 2-3 years. To reflect Q1 developments, we have tweaked our FY24-26 estimates (~3% downgrade in EPS) and reiterate our BUY rating with Jun-24 TP of Rs1,215 (implied FY25E P/BV: 4.7x)

Cholamandalam Investment: Financial Snapshot (Standalone)

Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net profits	21,467	26,662	34,453	42,173	52,752
AUM growths (%)	9.9	38.5	28.9	24.3	24.9
NII growths (%)	13.3	20.2	38.6	28.1	26.4
NIMs + Fees (%)	8.0	7.9	8.1	8.1	8.1
PPOP growth (%)	10.4	18.0	36.9	24.5	25.0
Adj. EPS (Rs)	26.1	32.4	41.8	51.2	64.0
Adj. EPS growth (%)	41.5	24.0	29.1	22.4	25.1
Adj. BV (INR)	142.4	173.7	211.2	257.3	314.9
Adj. BVPS growth (%)	22.3	21.9	21.6	21.8	22.4
RoA (%)	2.7	2.7	2.7	2.6	2.6
RoE (%)	20.2	20.5	21.7	21.9	22.4
P/E (x)	42.1	33.9	26.3	21.5	17.2
P/ABV (x)	7.7	6.3	5.2	4.3	3.5

Source: Company, Emkay Research

Multiple moving parts drive lower NII and higher credit cost leading to earnings miss

CIFC continued its strong growth, with both vehicle finance and non-vehicle disbursements growing strongly (total disbursement +50% YoY to Rs200bn), driving 40% YoY growth in loan AUM to Rs1.15trn. On the profitability front, increased cost of funds and some pressure on yields (owing to increased new vehicles in the mix) affected Q1 NIM and higher credit cost sequentially on account of seasonality, revision in PD and LGD norms, and some prudent reserving in newer business segments, leading to Q1 PAT at Rs7.3bn (+28%YoY), 11% lower than our estimate of Rs8.2bn.

Medium-term story remains intact

CIFC's operating and financial performance in Q1 was robust and management provided credible explanations for the minor aberrations. Notwithstanding the minor deviations this quarter, the medium-term story of CIFC's profitable growth, powered by its core strength in vehicle finance and supported by accelerated growth and growing size of the non-vehicle finance book, remains intact. The board has approved the capital raise of up to Rs40bn via QIP, and this capital raise (of Rs40bn) should increase Tier-1 CAR of the company by ~4ppts from 15.17% currently. This capital should be sufficient to support stronger growth over the next 2-3 years.

Minor cut in estimates, reiterate BUY

To reflect Q1 developments, we have tweaked FY24-26 estimates, leading to ~3% cut in EPS. We have not incorporated capital raise impact in our forecast as the exact quantum, price and instrument of capital raise is not confirmed. Beyond this minor change in earnings, our AUM, disbursement and credit cost estimates remain broadly unchanged. We reiterate our BUY rating on the stock with our Jun-24E target price of Rs1,215.(implied FY25E P/BV: 4.7x)

Target Price – 12M	Jun-24
Change in TP (%)	**(1.6)**
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	10.5
CMP (02-Aug-23) (Rs)	1,099.4

Stock Data	Ticker
52-week High (Rs)	1,215
52-week Low (Rs)	658
Shares outstanding (mn)	822.3
Market-cap (Rs bn)	904
Market-cap (USD mn)	10,946
Net-debt, FY24E (Rs mn)	21,988
ADTV-3M (mn shares)	2
ADTV-3M (Rs mn)	1,941.9
ADTV-3M (USD mn)	23.5
Free float (%)	-
Nifty-50	19,527
INR/USD	82.6
Shareholding, Jun-23	
Promoters (%)	51.5
FPIs/MFs (%)	20.9/20.4

Price Performance

(%)	1M	3M	12M
Absolute	(3.7)	25.7	47.2
Rel. to Nifty	(5.4)	16.8	30.8

1-Year share price trend (Rs)

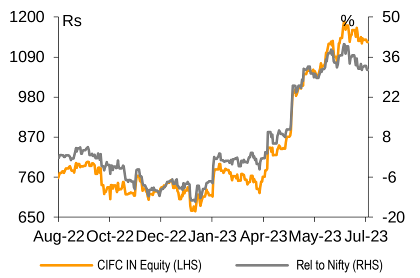

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Exhibit 1: Actual vs. Estimate

(Rs mn)	Actual Q1FY24	Estimate (Emkay)	Variation Emkay (%)	Comments
Disbursement	2,00,160	2,24,914	-11%	Disbursements were lower due to weak Q1.
AUM	11,47,960	11,34,783	1%	
NII	18,421	19,396	-5%	NII miss on account of a higher mix of new VF and increased cost of borrowings.
PPOP	13,399	13,279	1%	Cost-to-income improved, led by lower employee expenses.
PAT	7,260	8,186	-11%	Miss was primarily on account of provisioning on standard assets and revised PD and LGD norms.

Source: Company, Emkay Research

Exhibit 2: Revision in estimates

Y/E March (Rs mn)	FY24E			FY25E			FY26E		
	Earlier	Revised	Change (%)	Earlier	Revised	Change (%)	Earlier	Revised	Change (%)
Disbursement	8,24,297	8,24,297	0.0%	10,17,560	10,17,560	0.0%	12,66,545	12,66,545	0.0%
AUM	13,72,861	13,72,861	0.0%	17,06,677	17,06,677	0.0%	21,31,599	21,31,599	0.0%
Net interest income	91,210	87,765	-3.8%	1,14,798	1,12,398	-2.1%	1,44,938	1,42,027	-2.0%
PPOP	62,702	60,899	-2.9%	77,796	75,833	-2.5%	97,702	94,791	-3.0%
PAT	35,793	34,453	-3.7%	43,632	42,173	-3.3%	54,915	52,752	-3.9%
EPS (Rs)	43.5	41.8	-3.7%	53.0	51.2	-3.3%	66.7	64.0	-3.9%
BV (Rs)	213	211	-0.7%	260	257	-1.2%	320	315	-1.7%
NIM + Fees (%)	8.34%	8.06%	-28bps	8.25%	8.09%	-16bps	8.29%	8.14%	-15bps
Cost-to-income ratio (%)	38.3%	38.0%	-33bps	38.8%	39.2%	40bps	38.6%	39.3%	72bps
Opex-to-AUM (%)	3.2%	3.1%	-13bps	3.2%	3.2%	-3bps	3.2%	3.2%	0bps
Disbursement growth (%)	23.9%	23.9%	0bps	23.4%	23.4%	0bps	24.5%	24.5%	0bps
AUM growth (%)	28.9%	28.9%	0bps	24.3%	24.3%	0bps	24.9%	24.9%	0bps
Credit costs (%)	1.2%	1.2%	0bps	1.2%	1.2%	0bps	1.24%	1.24%	0bps

Source: Company, Emkay Research

Exhibit 3: AUM Trend

AUM trend (Rs bn)	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24
Vehicle Finance	484	493	507	529	554	576	613	669	711
Home loans (and Business Finance)	44	49	50	56	59	65	73	85	95
Home Equity (LAP)	145	153	162	168	177	188	200	216	229
Others	5	6	8	16	29	48	69	95	113
Total	678	700	727	769	819	877	955	1065	1148

Source: Company, Emkay Research

Exhibit 4: Disbursement trend

Disbursement trend (Rs bn)	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24
Vehicle Finance	28	62	76	88	86	85	104	122	113
Home loans (and Business Finance)	2	5	4	5	6	7	11	14	15
Home Equity (LAP)	4	16	18	19	20	22	23	28	27
Others	2	4	6	15	21	31	38	47	46
Total	36	87	104	127	133	146	176	210	200

Source: Company, Emkay Research

Management Commentary

Business Commentary

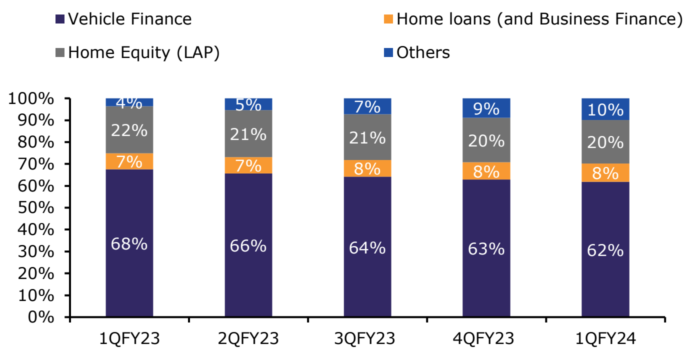
- The retail industry (NBFC) is expected to grow at 18-20%, with secured lending (including VF and other secured products) growth expectation at 14-16%.
- CIFC holds a strong liquidity position, with Rs70.69bn as cash balance as of June-23, including Rs15bn worth of investment in G-sec and T-bill. Total liquidity position, including undrawn sanctioned credit line, stood at Rs94.79bn.
- The board has approved fund raising of Rs40bn thorough QIP or preferential convertible debt, subjected to shareholders' approval. Price at which the fund will be raised is yet to be determined.
- Credit cost for Q1 has increased on account of revised PD and LGD norms and increased NCL in the new segment, which seems inflated due to the accounting treatment of FLDG reimbursement, which forms part of the income rather being netted off in credit cost. FLDG receipt was close to ~Rs350mn. Credit cost shown in the new business is majorly due to provision on standard assets. Provision on standard assets accounts for 60% of the NCL. Collection efficiency stood at 99.5%.
- The impact on VF margin can be explained by four factors: 1) Incremental book yield was 1% higher than book yield, but book yield was lower by 15bps; the same was impacted by the rundown of the high-yielding book, which was built in FY18-20. 2) On the other income (mainly debt recoveries) front, which was also lower in Q1 by ~15bps, the same can be attributed to seasonal effect. Q1 is a lean season for collections and recoveries. 3) The mix of new vehicles was higher in the overall mix; used business is doing well; but car sales were up by 10% at industry levels, and CIFC gained a bit of market share – so CIFC will continue to participate in this segment. 4) CoFs increased sequentially, which are expected to stabilize in the coming quarters.
- The new segment business is growing well and yields are similar to that of peers in the market and have a lower bounce rate. CIFC is not being very aggressing in growing this segment (not compromising on credit parameter).
- In the partnership business, which is a small ticket and small tenure loan, CIFC targets customers with 720+ CIBIL score. In BL (customer segment – self-employed professional and non-professional), it has 96% of the customers, with CIBIL score of 720+, and the remaining 4% customers are with a CIBIL score in the range of 700-720. For the personal loan segment, the company has not done business as it has lower yield compared to BL and CAT A, B and C kind of salaried profile are funded by banks and CAT D and E are targeted NBFCs, which are a high-risk profile. PL will be done through direct channels and to existing customers only.
- AHL is expected to grow at a much higher rate, as the company is looking to serve the underserved market segment in Northern states – the current mix is at 40% for non-south and 60% for south. Whereas LAP business is being operated from ~600 branches now and expects it to increase to 1200-1300 branches. Micro LAP is doing better in terms of yield and delinquency with a lower bounce rate.
- Digital App – Gaadi Bazzar – Re-possessed sale of ~3000 units per month (via ~1150 branches and 500 resilient locations), which are being sold online (customers quote their prices). This helps to realise the best value and increases transparency. Dealing with ~5000 dealers with disbursement of ~Rs16bn towards trade finance is being registered per month. Almost 1.5bn collection is done using this platform. CIFC has also created a market place with close to 10,000 used vehicle dealers, whose products are getting listed and helping it to generate revenue and leads from the platform.
- Restructured assets stood at Rs22bn, of which Rs3bn are in Stage-1, Rs15bn in stage-2 and the balance in Stage-3
- Employee expenses in Q4 are generally higher due to incentives and full performance of employees are accounted for, which was absent in Q1. In Q2, it can see some increment, although quite insignificant.

Guidance:

- Overall disbursements are likely to grow for all product segments. Affordable HL, LAP and new segment are expected to grow at a faster rate, with VF expected to grow at ~20%.
- Credit cost is expected to see improvement, with overall credit cost to be in an acceptable range. Management expects some increase in the new segment, given the nature of products, with the segment still growing. Currently, it is following a stringent policy for the new segment business till the company starts using the ECL model.
- Cost of borrowings is not expected to increase given no action from the regulator. Bank borrowings stand at 55-60% of the total borrowings, of which 10% is fixed. On the floating side, CIFC is in negation with banks and has built-in clause to repay if the negotiation fails at the time of reset.
- Margin improvement is expected, given improved yields on other products and increasing share of incremental disbursement at new rate of the VF book, which is generally lent at a fixed rate. The company is also increasing its focus on used VF Finance, which comes at a higher yield.
- NCL on new book is expected to increase since the book is still in a building process and the current credit cost is not sustainable at that level. The NCL should remain range bound at 1.2-1.5% levels.
- ROE of VF book is likely to catch-up in the coming quarters. The same was down due to lower yields and increasing cost with some support from reduced opex. (ROE gap of 60bps is expected to see sequential reduction).

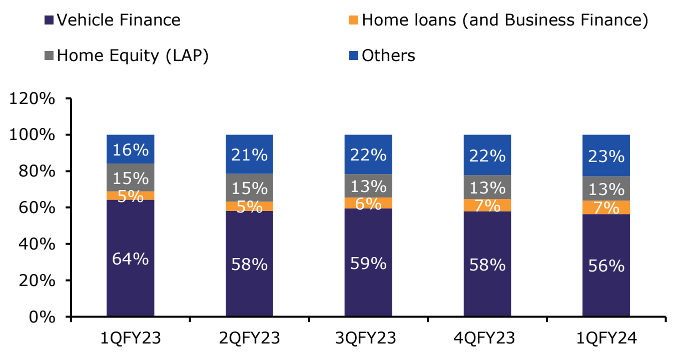
Result in Chart:

Exhibit 5: AUM mix: Increasing share of the non-vehicle portfolio



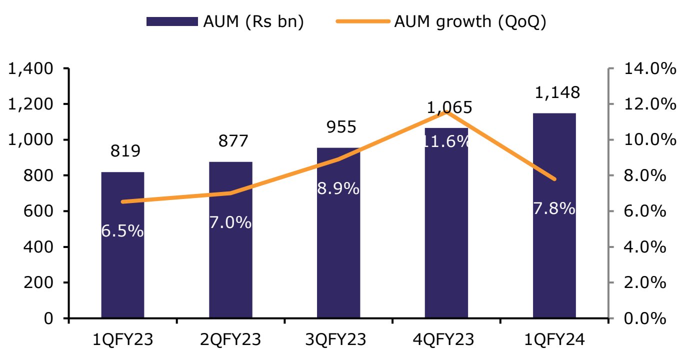
Source: Company, Emkay Research

Exhibit 6: Disbursement grew by ~50% YoY



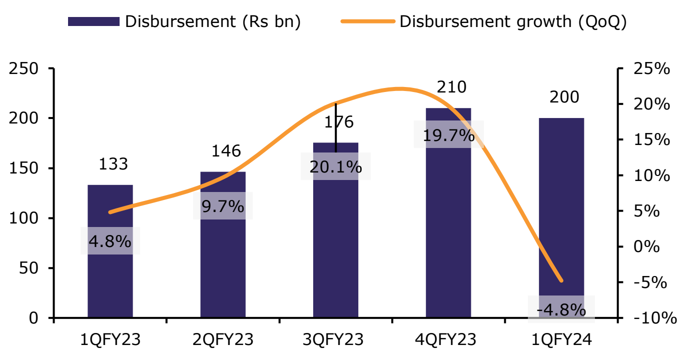
Source: Company, Emkay Research

Exhibit 7: AUM growth led by all product segments



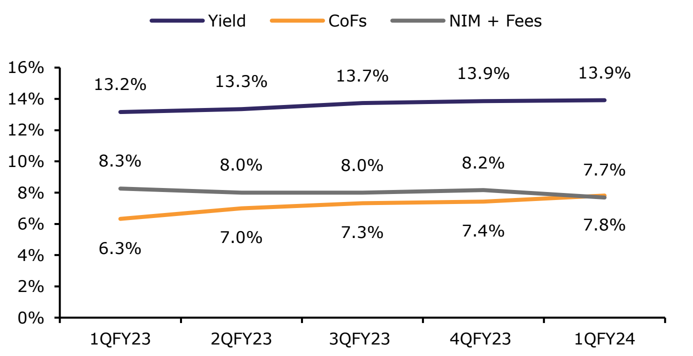
Source: Company, Emkay Research

Exhibit 8: Disbursements were low on account of weak Q1



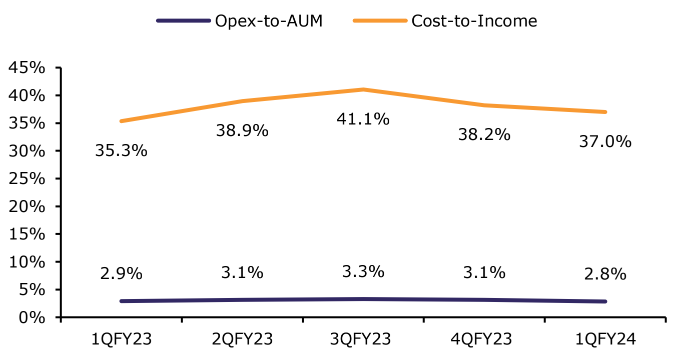
Source: Company, Emkay Research

Exhibit 9: NIM compression due to higher mix on new vehicles and increased cost of borrowings



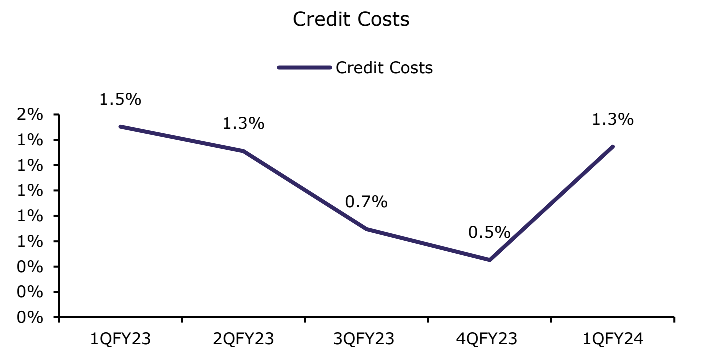
Source: Company, Emkay Research

Exhibit 10: Operating expenses improved on account of lower employee expenses



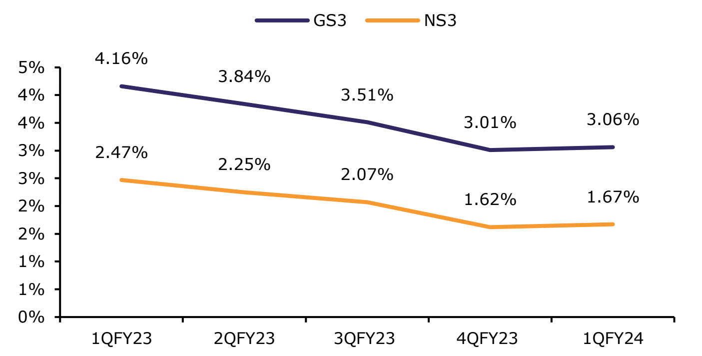
Source: Company, Emkay Research

Exhibit 11: Credit cost increased due to revised PD&LGD norms in addition to the stringent policy followed for the new segment



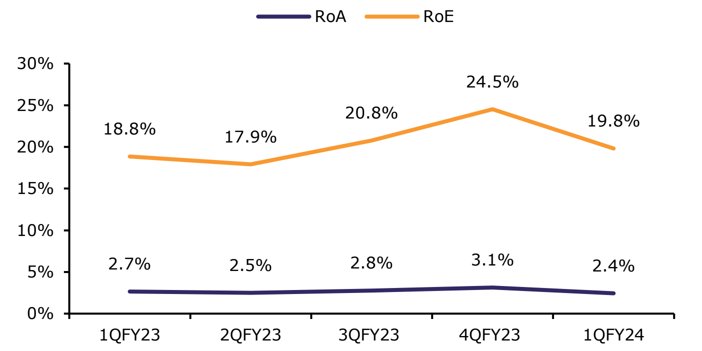
Source: Company, Emkay Research

Exhibit 12: GS3 and NS3 increased marginally.



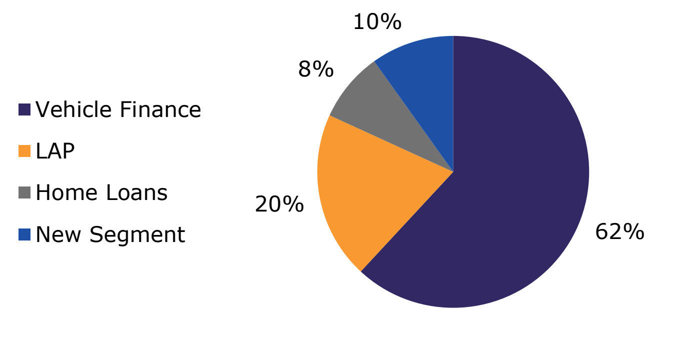
Source: Company, Emkay Research

Exhibit 13: RoE to improve with improving yields



Source: Company, Emkay Research

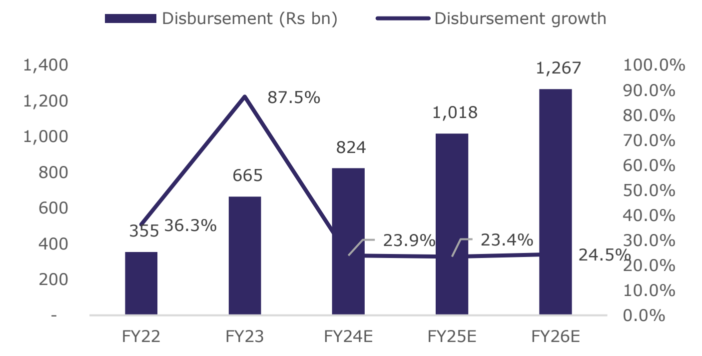
Exhibit 14: AUM Mix



Source: Company, Emkay Research

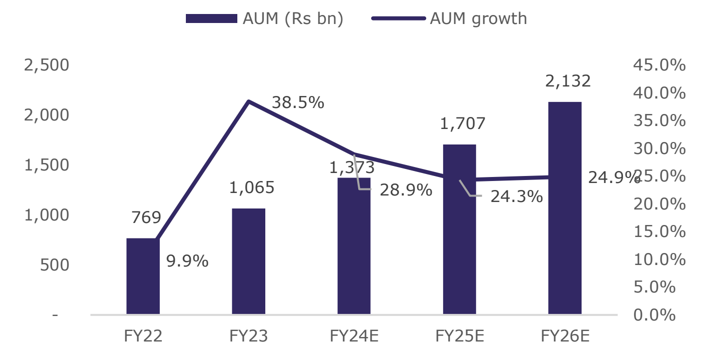
Story in charts:

Exhibit 15: Disbursement growth to remain strong, with the non-vehicle segment growing at a faster pace



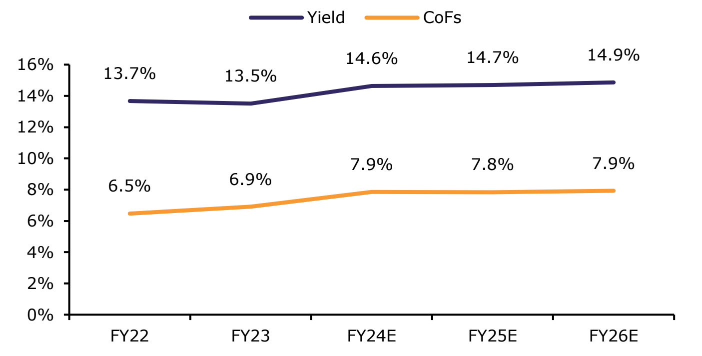
Source: Company, Emkay Research

Exhibit 16: AUM growth led by strong disbursement



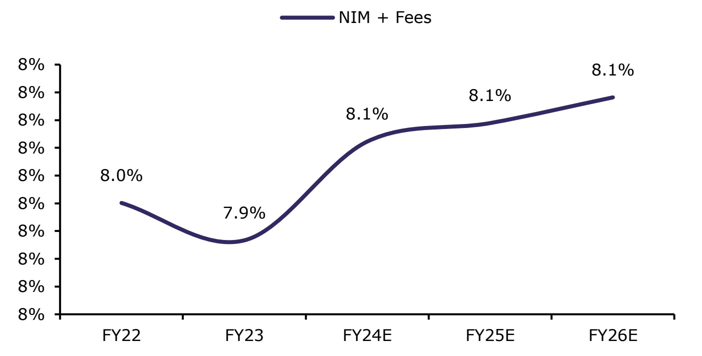
Source: Company, Emkay Research

Exhibit 17: Yields are expected to improve led by improving asset mix



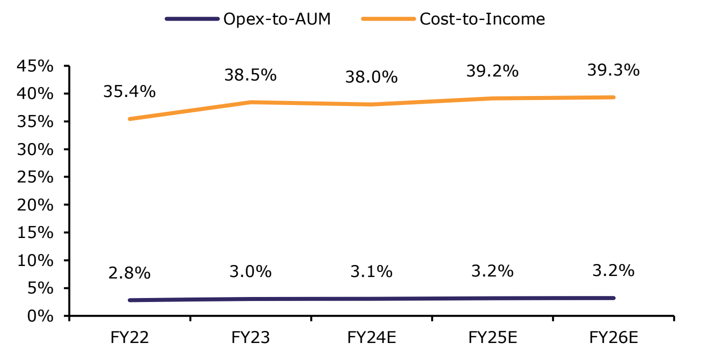
Source: Company, Emkay Research

Exhibit 18: NIM improvement led by improving yields and CoF moderation



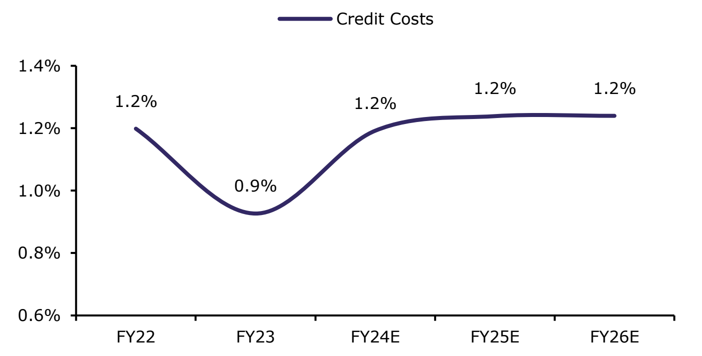
Source: Company, Emkay Research

Exhibit 19: Opex to remain at similar level



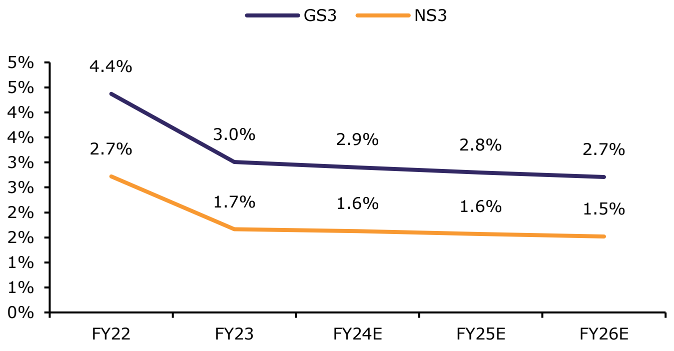
Source: Company, Emkay Research

Exhibit 20: Credit cost to remain stable at 1.2%



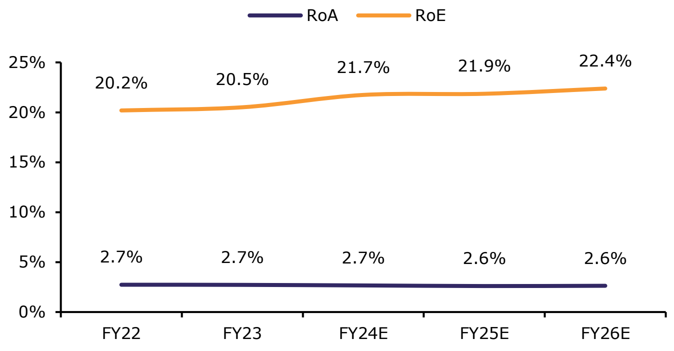
Source: Company, Emkay Research

Exhibit 21: GS3 and NS3 to see improvement



Source: Company, Emkay Research

Exhibit 22: RoA and RoE to expand on account of improved margins and profitability



Source: Company, Emkay Research

Cholamandalam Investment: Standalone Financials and Valuations

Profit and Loss

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	95,668	1,20,822	1,75,308	2,22,450	2,80,494
Interest Expense	42,988	57,488	87,543	1,10,052	1,38,468
Net interest income	**52,680**	**63,334**	**87,765**	**1,12,398**	**1,42,027**
NII growth (%)	13.3	20.2	38.6	28.1	26.4
Non interest income	5,720	8,958	10,495	12,241	14,209
Total income	**58,400**	**72,292**	**98,260**	**1,24,638**	**1,56,235**
Operating expenses	20,687	27,799	37,361	48,806	61,445
PPOP	**37,712**	**44,494**	**60,899**	**75,833**	**94,791**
PPOP growth (%)	10.4	18.0	36.9	24.5	25.0
Provisions & contingencies	8,803	8,497	14,529	19,073	23,792
PBT	**28,909**	**35,997**	**46,370**	**56,760**	**70,999**
Extraordinary items	0	0	0	0	0
Tax expense	7,442	9,335	11,917	14,587	18,247
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	**21,467**	**26,662**	**34,453**	**42,173**	**52,752**
PAT growth (%)	41.8	24.2	29.2	22.4	25.1
Adjusted PAT	**21,467**	**26,662**	**34,453**	**42,173**	**52,752**
Diluted EPS (Rs)	**26.1**	**32.4**	**41.8**	**51.2**	**64.0**
Diluted EPS growth (%)	41.5	24.0	29.1	22.4	25.1
DPS (Rs)	**2.0**	**2.1**	**4.2**	**5.1**	**6.4**
Dividend payout (%)	**7.7**	**6.5**	**10.0**	**10.0**	**10.0**
Effective tax rate (%)	25.7	25.9	25.7	25.7	25.7
Net interest margins (%)	8.0	7.9	8.1	8.1	8.1
Cost-income ratio (%)	35.4	38.5	38.0	39.2	39.3
PAT/PPOP (%)	56.9	59.9	56.6	55.6	55.7
Shares outstanding (mn)	821.4	822.4	822.4	822.4	822.4

Source: Company, Emkay Research

Balance Sheet

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	1,643	1,645	1,645	1,645	1,645
Reserves & surplus	1,15,434	1,41,316	1,72,329	2,10,291	2,57,776
Net worth	**1,17,077**	**1,42,961**	**1,73,974**	**2,11,936**	**2,59,421**
Borrowings	**6,91,735**	**9,73,561**	**12,55,636**	**15,52,557**	**19,39,107**
Other liabilities & prov.	**14,822**	**18,634**	**20,626**	**22,841**	**25,308**
Total liabilities & equity	**8,23,634**	**11,35,155**	**14,50,236**	**17,87,334**	**22,23,836**
Net loans	7,41,492	10,47,483	13,50,147	16,78,440	20,96,332
Investments	20,762	36,200	41,436	45,024	56,234
Cash, other balances	42,201	29,614	33,964	35,839	39,293
Interest earning assets	**8,04,455**	**11,13,298**	**14,25,547**	**17,59,303**	**21,91,859**
Fixed assets	2,916	4,589	5,507	6,609	7,930
Other assets	16,264	17,268	19,182	21,422	24,047
Total assets	**8,23,634**	**11,35,155**	**14,50,236**	**17,87,334**	**22,23,836**
BVPS (Rs)	142.4	173.7	211.2	257.3	314.9
Adj. BVPS (INR)	142.4	173.7	211.2	257.3	314.9
Gross loans	7,64,779	10,70,780	13,77,500	17,11,625	21,36,930
Total AUM	**7,69,080**	**10,64,980**	**13,72,861**	**17,06,677**	**21,31,599**
On balance sheet	7,41,420	10,47,360	13,50,147	16,78,440	20,96,332
Off balance sheet	27,660	17,620	22,714	28,237	35,267
Disbursements	3,54,890	6,65,330	8,24,297	10,17,560	12,66,545
Disbursements growth (%)	36.3	87.5	23.9	23.4	24.5
Loan growth (%)	12.6	41.3	28.9	24.3	24.9
AUM growth (%)	9.9	38.5	28.9	24.3	24.9
Borrowings growth (%)	8.5	40.7	29.0	23.6	24.9
Book value growth (%)	22.3	21.9	21.6	21.8	22.4

Source: Company, Emkay Research

Asset Quality and Other Metrics

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Asset quality					
GNPL - Stage 3	33,428	32,220	39,978	47,863	57,877
NNPL - Stage 3	20,170	17,400	21,988	26,325	31,832
GNPL ratio - Stage 3 (%)	4.4	3.0	2.9	2.8	2.7
NNPL ratio - Stage 3 (%)	2.7	1.7	1.6	1.6	1.5
ECL coverage - Stage 3 (%)	39.7	46.0	45.0	45.0	45.0
ECL coverage - 1 & 2 (%)	1.4	0.8	0.7	0.7	0.7
Gross slippage - Stage 3	0	0	0	0	0
Gross slippage ratio (%)	0.0	0.0	0.0	0.0	0.0
Write-off ratio (%)	10.0	8.2	7.7	7.9	8.0
Total credit costs (%)	1.2	0.9	1.2	1.2	1.2
NNPA to networth (%)	17.2	12.2	12.6	12.4	12.3
Capital adequacy					
Total CAR (%)	19.6	17.1	16.2	16.0	15.8
Tier-1 (%)	16.5	14.8	13.8	13.7	13.4
Miscellaneous					
Total income growth (%)	16.8	23.8	35.9	26.8	25.4
Opex growth (%)	30.6	34.4	34.4	30.6	25.9
PPOP margin (%)	5.1	4.9	5.0	4.9	4.9
Credit costs-to-PPOP (%)	23.3	19.1	23.9	25.2	25.1
Loan-to-Assets (%)	90.0	92.3	93.1	93.9	94.3
Yield on loans (%)	13.7	13.5	14.6	14.7	14.9
Cost of funds (%)	6.5	6.9	7.9	7.8	7.9
Spread (%)	7.2	6.6	6.8	6.9	6.9

Source: Company, Emkay Research

Valuations and Key Ratios

Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	42.1	33.9	26.3	21.5	17.2
P/B (x)	7.7	6.3	5.2	4.3	3.5
P/ABV (x)	7.7	6.3	5.2	4.3	3.5
P/PPOP (x)	23.9	20.3	14.8	11.9	9.5
Dividend yield (%)	0.2	0.2	0.4	0.5	0.6
Dupont-RoE split (%)					
NII/avg AUM	7.2	6.9	7.2	7.3	7.4
Other income	0.8	1.0	0.9	0.8	0.7
Securitization income	0.0	0.0	0.0	0.0	0.0
Opex	1.6	1.7	1.8	1.9	2.0
Employee expense	1.2	1.4	1.3	1.2	1.2
PPOP	**5.1**	**4.9**	**5.0**	**4.9**	**4.9**
Provisions	1.2	0.9	1.2	1.2	1.2
Tax expense	1.0	1.0	1.0	0.9	1.0
RoAUM (%)	**2.9**	**2.9**	**2.8**	**2.7**	**2.7**
Leverage ratio (x)	6.9	7.1	7.7	8.0	8.1
RoE (%)	**20.2**	**20.5**	**21.7**	**21.9**	**22.4**

Quarterly data

Rs mn, Y/E Mar	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24
NII	14,814	14,888	15,983	17,649	18,421
NIM + Fees (%)	8.3	8.0	8.0	8.2	7.7
PPOP	10,604	10,363	10,797	12,731	13,399
PAT	5,657	5,634	6,843	8,528	7,260
EPS (Rs)	6.89	6.86	8.33	10.38	8.84

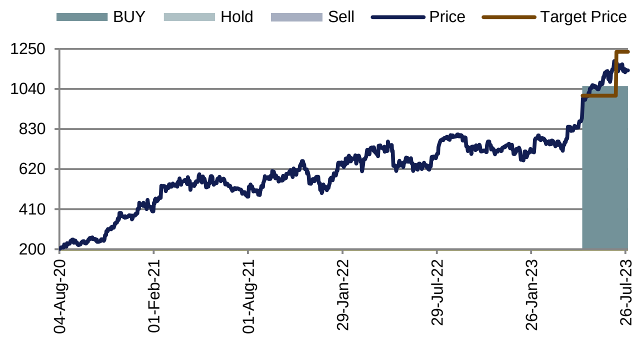
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	CMP (INR)	TP (INR)	Rating	Analyst
08-Jul-23	1,177	1,235	Buy	Avinash Singh
04-May-23	950	1,005	Buy	Avinash Singh

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Bloomberg, Company, Emkay Research

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