Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Company Update

Cholamandalam Investment and Finance Company

Earnings trajectory to remain strong

NBFC	Sharekhan code: CHOLAFIN
Reco/View: Buy ↔	CMP: **Rs. 1,230** | Price Target: **Rs. 1,425** ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Cholamandalam Investment and Finance Company (CIFC) is well poised to clock healthy AUM growth across product segments led by strong disbursement momentum in its non-vehicle finance book.
- NIM is expected to remain at a healthy level (>7.0% over FY25-26E) aided by yield improvement on better product mix, re-pricing of fixed-rate vehicles loan book and likely peak-out of CoB.
- Management expects modest impact of the RBI's latest revised risk-weight norms. Capital adequacy impact would be contained at about 15-20 bps.
- We believe CIFC ability to deliver industry leading growth along with healthy NIM and contained cost to keep earnings trajectory upgraded. PAT is expected to grow at a CAGR of 31% over FY23-26E with would drive ~20 bps ROA expansion to ~ 2.9%. At CMP, the stock trades at P/BV 4.5x/3.6x to its FY2025E/FY2026E BV estimates. We maintain a Buy rating with an upgraded PT of Rs. 1,425.

Cholamandalam Investment and Finance (CIFC) has made a significant progress in its planned strategy for diversification of loan book across products such as home loans, LAP and new businesses (vehicle finance book share reduced by 10% in last 2.5 fiscals). We believe the strategy is not only margin supportive but also reduces cyclicality of book to core vehicles finance business, besides providing a boost to growth trajectory. While some stress was noted in the CSEL partnership business, its low share (~1.8% AUM) and corrective measures taken by management provides comfort. The management guided for contained credit cost of 1.1-1.2% for FY24. Strong growth along with healthy NIM and contained credit cost to sustain a strong expansion in earnings trajectory over the next two fiscals.

- **AUM growth to remain strong despite some near-term moderation in partnerships led CSEL book:** CIFC delivered 23% AUM CAGR over FY21-23 as strong disbursements in HL & new business helped it to offset slowdown in vehicle finance. Share of non-vehicles finance book rose to 40% of book as of H1FY24 (vs 28% in FY21). We expect near-term moderation in disbursements for CSEL partnership business because of assets quality risk & increase in risk weights, but momentum in other non-vehicle product segments to remain strong. As per the management, credit demand will also remain healthy for UVs and CVs, which will drive overall book's growth. We expect overall AUM to grow at a CAGR of 27% over FY23-26E.
- **NIM to stay healthy; expects limited impact of increase in risk weights:** Despite the higher share of fixed rate loan book, CIFC managed its margin well amidst rising interest rate scenario with better management of liabilities and increasing share of high yielding book. We expect margin to sustain at >7% over the forecasted fiscals as multiple drivers are in place. 1) Increasing share of high yielding new business book and pick-up in share of used vehicles finance book. 2) re-pricing of fixed rate vehicles finance book and 3) peak-out of CoB and limited impact of RBI's revised risk weights norms. As per the management, about 2% of the book would come under preview of RBI new risk-weighs and CRAR impact would be about 15-20 bps. While it expects 15-20 bps point increase in cost of funds (CoF).
- **Stable assets quality to keep credit cost contained:** Assets quality improved significantly as GS-3 ratio reduced to 3.0% by H1FY24 (versus 3.8% y-o-y). PCR improved to 47.3% (v/s 41.5% y-o-y) on lower slippages. The company has noted stress in its partnership led CSEL book as GS-3 ratio in this book rose to 4.7% (vs 0.82% in traditional channel sourced CSEL book). Over the last one and half year, the company expanded its new business book aggressively (book size increased to Rs. 133 bn from Rs16 bn as of FY22). Partnership (fintech + consumer tech) led CSEL accounted for 25% of Rs. 82 billion CSEL book. The management has already taken corrective actions in the CSEL book where NPAs levels are still within industry norms. We also take comfort from the company's past execution track record as it has managed well on the asset quality front during various cycles in the past. We expect contained credit cost ~1.0% over FY24-26E led by improvement in assets quality of vehicles finance and LAP portfolio.

Our Call

View & Valuation: We maintain a Buy with an upgraded price target of Rs. 1,425: At CMP, the stock trades at P/ BV 4.5x/3.6x to its FY2025E/FY2026E. We are optimistic on CIFC's ability to deliver industry-leading growth aided by focus on diversification in product mix and steadily gaining market share. We believe margin has broadly bottomed out along with strong AUM growth >25%, moderation in opex growth and controlled credit costs, it should translate into a healthy earnings trajectory. PAT is expected to grow at a CAGR of 31% over FY23-26E. We believe CIFC would continue to sustain premium valuation relative to its peers given its ability to deliver industry leading growth, low credit cost and healthy RoE >20%.

Key Risks

Economic slowdown can result in slower loan growth, higher-than-anticipated credit cost, lower than-expected margin and emerging stress in partnerships led new business.

Valuation (standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E	FY26E
NII	5,268	6,334	8,204	10,779	13,695
Gr.	3.7%	26.3%	40.2%	28.7%	24.2%
NIM	7.5%	7.1%	6.9%	7.0%	7.1%
PPOP	3,750	4,450	5,889	8,033	10,152
PAT	2,147	2,666	3,405	4,786	6,050
AUM	76,908	1,06,498	1,37,079	1,76,069	2,19,397
RoE	20.2%	20.5%	21.4%	24.2%	24.3%
RoA	2.7%	2.7%	2.6%	2.9%	2.9%
C/I	35.6%	38.5%	38.3%	35.0%	35.2%
P/E (x)	47.2	37.9	29.4	20.9	16.5
P/BV (x)	8.6	7.0	5.7	4.5	3.6

Source: Company; Sharekhan estimates

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 24.83

Updated Aug 08, 2023

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

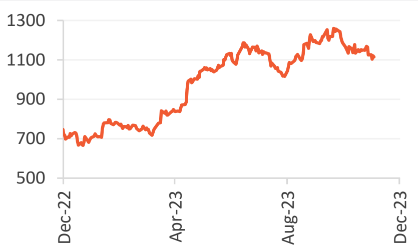
Company details

Market cap:	Rs. 1,02,869 cr
52-week high/low:	Rs. 1284 / 658
NSE volume: (No of shares)	16.3 lakh
BSE code:	511243
NSE code:	CHOLAFIN
Free float: (No of shares)	40.3 cr

Shareholding (%)

Promoters	51.4
FII	21.5
DII	20.0
Others	7.0

Price chart

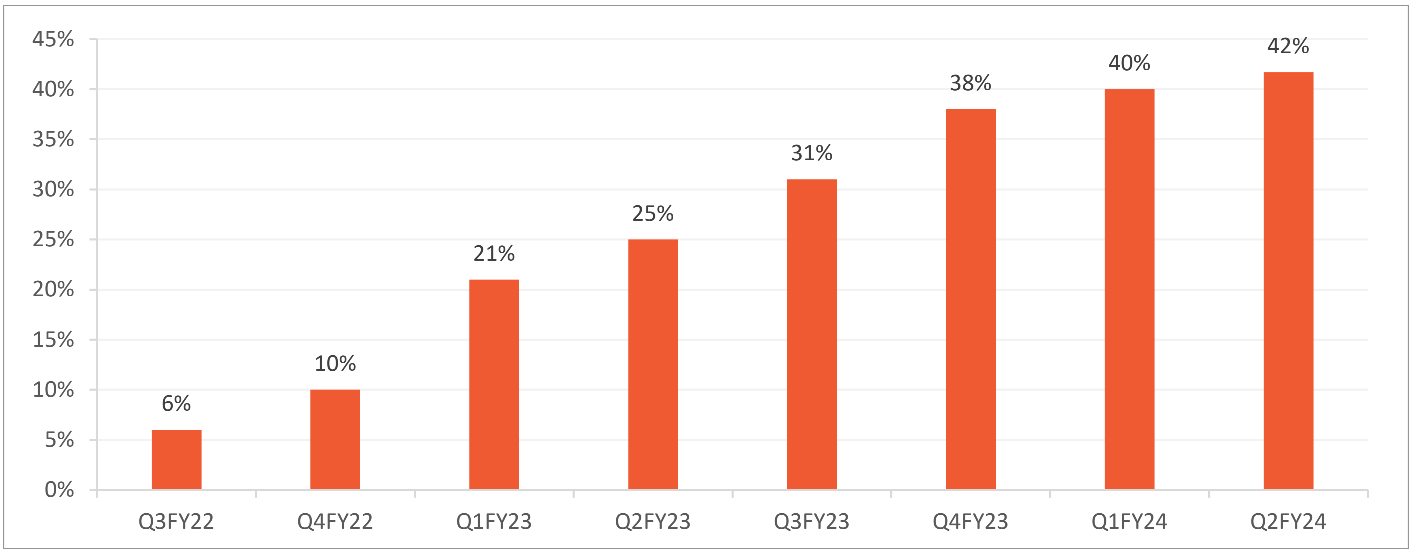


Price performance

(%)	1m	3m	6m	12m
Absolute	10.9	3.1	11.3	69.7
Relative to Sensex	3.5	-3.8	-0.6	53.7

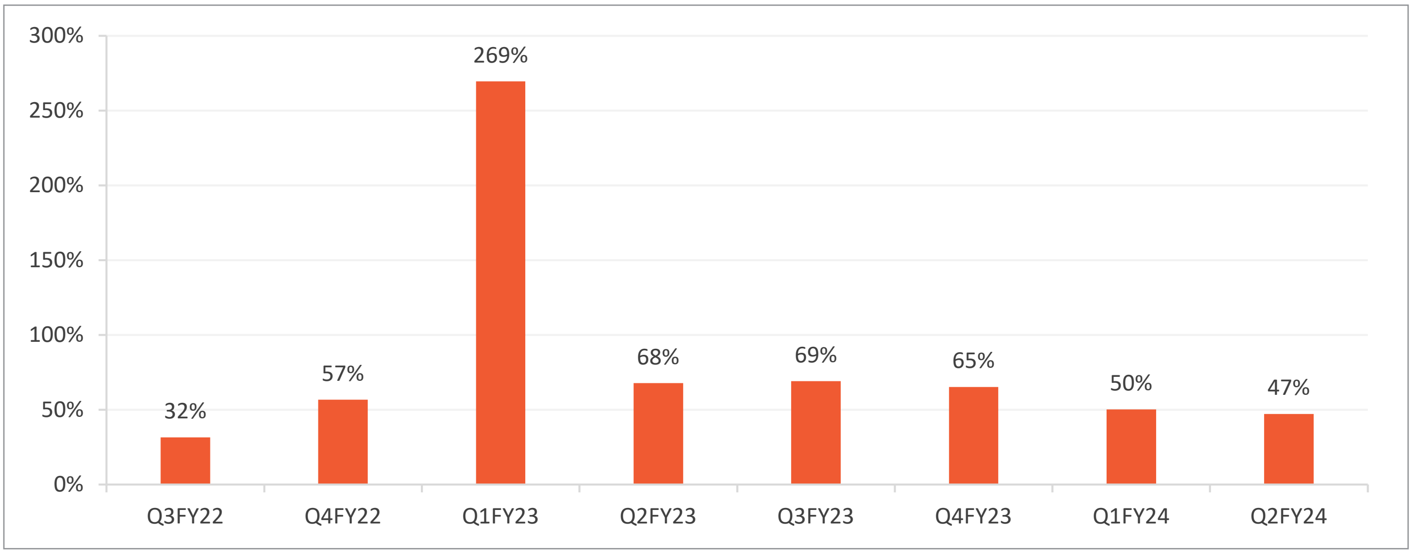
Sharekhan Research, Bloomberg

Trend in AUM growth (Y-o-Y)



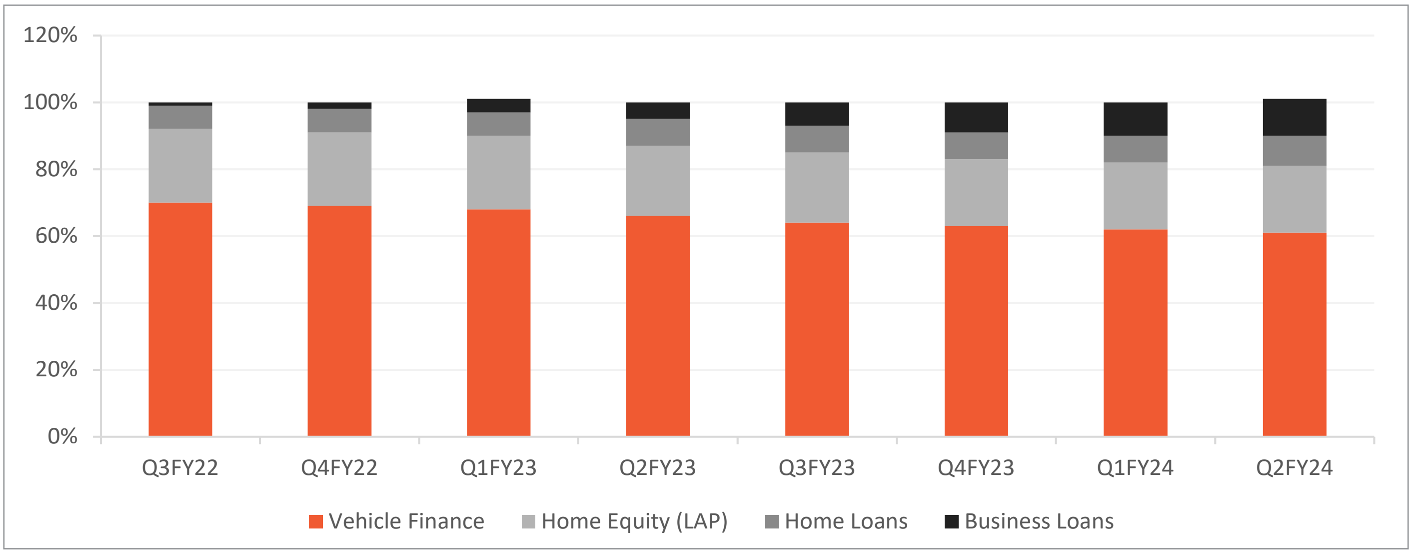
Source: Company, Sharekhan Research

Trend in disbursements growth (Y-o-Y)



Source: Company, Sharekhan Research

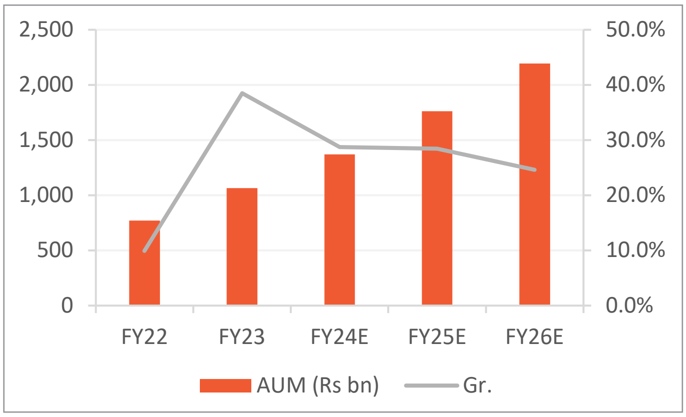
Trend in AUM mix



Source: Company, Sharekhan Research

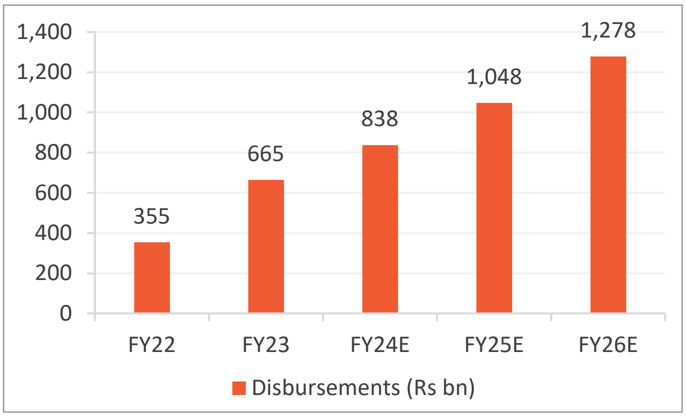
Financials in charts

Trend in AUM



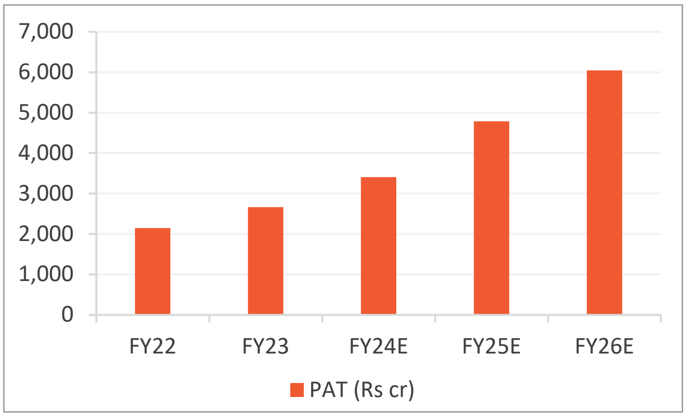
Source: Company, Sharekhan Research

Trend in Disbursements



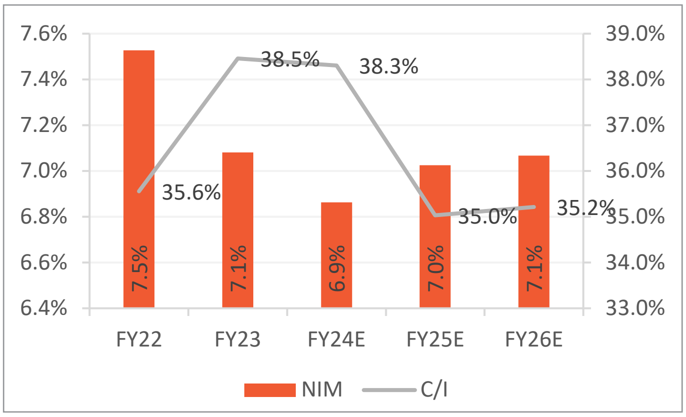
Source: Company, Sharekhan Research

Trend in Profitability



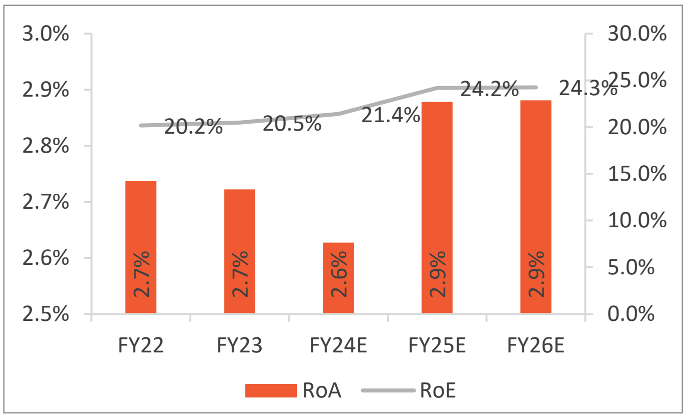
Source: Company, Sharekhan Research

Trend in NIM, C/I ratio



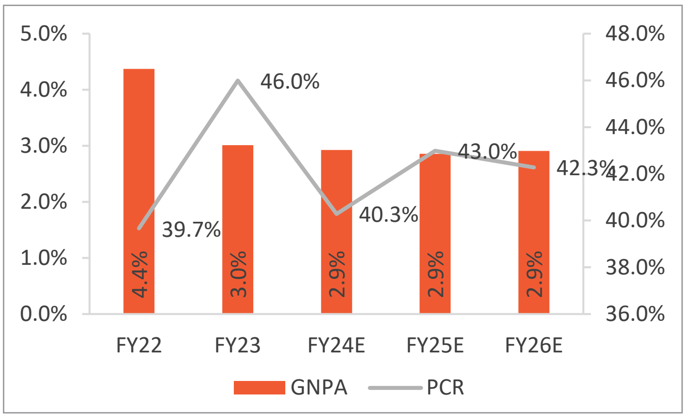
Source: Company, Sharekhan Research

Trend in Return Ratios



Source: Company, Sharekhan Research

Trend in Assets Quality



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Growth prospects look encouraging

The growing importance of NBFCs is reflected in the consistent rise of their credit as a proportion to GDP as well as in relation to credit extended by SCBs to the NBFC sector. Retail credit demand continues to remain robust, driven by strong macro tailwinds. Volumes continue to see an uptick. Urban demand has been strong and recovered fully from pandemic-induced disruptions. There are some green shoots related to improvement in rural demand. Asset-quality trends are encouraging. NBFCs with a diverse product offering strategy, strong asset-liability management, robust liquidity buffers, strong risk management framework, and healthy liability franchise have ample growth opportunities and are well placed.

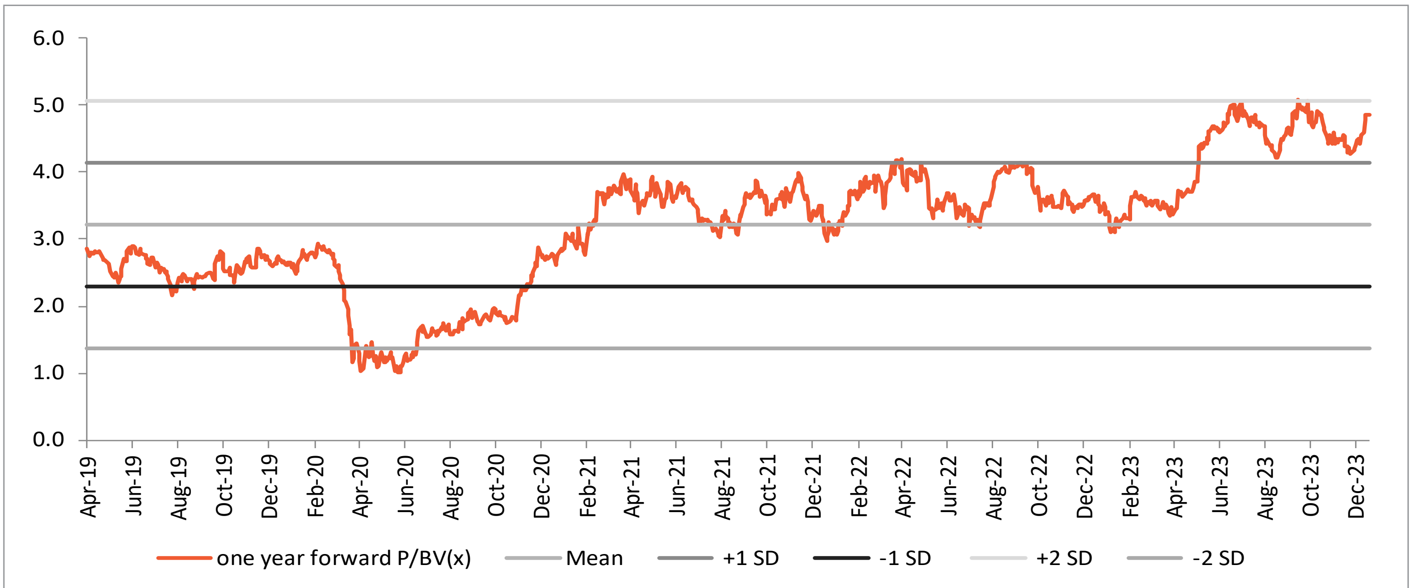
■ Company outlook - Attractive franchise

CIFC has a strong business model, demonstrated by superior performance across economic cycles. A robust collection mechanism aided by a strong credit risk assessment framework has helped it to navigate past business cycles and would enable it to navigate in the future also. Pristine asset quality has been the hallmark of the franchise. The company is likely to deliver a sustainable RoE of 18-20%. We are confident about the longevity of the franchise and best-in-class management in terms of execution capabilities and strong governance. The company is confident of sustaining strong business momentum by penetrating deeper into geographies.

■ Valuation - Maintain Buy rating with an upgraded price target of Rs. 1,425

At CMP, the stock trades at P/ BV 4.5x/3.6x to its FY2025E/FY2026E. We are optimistic on CIFC's ability to deliver industry-leading growth aided by focus on diversification in product mix and steadily gaining market share. We believe margin has broadly bottomed out along with strong AUM growth >25%, moderation in opex growth and controlled credit costs, it should translate into a healthy earnings trajectory. PAT is expected to grow at a CAGR of 31% over FY23-26E. We believe CIFC would continue to sustain premium valuation relative to its peers given its ability to deliver industry leading growth, low credit cost and healthy RoE >20%.

One-year forward P/BV trend



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs/ Share)	MCAP (Rs Cr)	P/E (x)		P/B (x)		RoE (%)		RoA (%)	
			FY24E	FY25E	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Cholamandalam	1,230	1,02,949	29.4	20.9	5.7	4.5	21.4	24.2	2.6	2.9
M&M Finance	270	33,501	19.8	12.7	1.9	1.7	9.9	14.5	1.6	2.1

Source: Company; Sharekhan Research

About company

CIFC was incorporated in 1978 as the financial services arm of the Murugappa Group. CIFC commenced business as an equipment financing company and today has emerged as a comprehensive financial services provider offering vehicle finance, home equity loans, home loans, consumer loans, SME loans, wealth management, stock broking, and a variety of other financial services to customers.

Investment theme

CIFC is a leading vehicle financier diversifying its product segments. A strong collection mechanism and rigorous risk-management practices provide comfort, reflected in pristine asset quality. We believe while the vehicle financing business will continue to be the mainstay for the company, home equity (LAP) has also been a significant contributor to the company's growth. The home loans segment has great potential to be built into a solid portfolio, considering the expertise of the company in handling typical customer profiles along with new consumer and SME business.

Key Risks

Economic slowdown can result in slower loan growth, higher-than-anticipated credit cost and lower than-expected margin and emerging stress in partnership led new business

Additional Data

Key management personnel

Vellayan Subbiah	Chairman
Ravindra Kumar Kundu	ED
Arul Selvan	CFO

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	AXIS ASSET MANAGEMENT CO. LTD.	4.50
2	AMBADI INVESTMENTS LTD.	4.02
3	VANGUARD GROUP INC.	1.93
4	CAPITAL GROUP COS INC.	1.90
5	BLACKROCK INC.	1.66
6	SMALLCAP World Fund Inc/Fund Paren	1.55
7	SBI FUNDS MANAGEMENT LTD.	1.54
8	HDFC ASSET MANAGEMENT CO. LTD.	1.50
9	Motilal Oswal Assets Management	1.43
10	Norges Bank	1.25

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/ weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan
by BNP PARIBAS

DISCLAIMER

This information/document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This information/ document is subject to changes without prior notice.

Recommendation in reports based on technical and derivatives analysis is based on studying charts of a stock's price movement, trading volume, outstanding positions, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals. However, this would only apply for information/document focused on technical and derivatives research and shall not apply to reports/documents/ information focused on fundamental research.

This information/document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this information/report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved) and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other recommendations/ reports that are inconsistent with and reach different conclusions from the information presented in this recommendations/report.

This information/recommendation/report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst might have dealt or traded directly or indirectly in securities of the company and that all the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that either he or his relatives or Sharekhan associates might have direct or indirect financial interest or might have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report. The analyst and SHAREKHAN encourages independence in research report/ material preparation and strives to minimize conflict in preparation of research report. The analyst and SHAREKHAN does not have any material conflict of interest or has not served as officer, director or employee or engaged in market making activity of the company. The analyst and SHAREKHAN has not been a part of the team which has managed or co-managed the public offerings of the company, and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Ltd or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Forward-looking statements (if any) are provided to allow potential investors the opportunity to understand management's beliefs and opinions in respect of the future so that they may use such beliefs and opinions as one factor in evaluating an investment. These statements are not a guarantee of future performance and undue reliance should not be placed on them. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause actual performance and financial results in future periods to differ materially from any projections of future performance or result expressed or implied by such forward-looking statements. Sharekhan/its affiliates undertakes no obligation to update forward-looking statements if circumstances or management's estimates or opinions should change except as required by applicable securities laws. The reader/investors are cautioned not to place undue reliance on forward-looking statements and use their independent judgement before taking any investment decision.

Investment in securities market are subject to market risks, read all the related documents carefully before investing. The securities quoted are for illustration only and are not recommendatory. Registration granted by SEBI, and certification from NISM in no way guarantee performance of the intermediary or provide any assurance of returns to investors.

Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com

---

Registration and Contact Details: Name of Research Analyst - Sharekhan Limited, Research Analyst Regn No.: INH000006183. CIN): - U99999MH1995PLC087498. Registered Office: The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA. Tel: 022-6115000.

Correspondence/Administrative Office: Gigaplex IT Park, Unit No 1001, 10th Floor, Building No.9, TTC Industrial Area, Digha, Airoli-West, Navi Mumbai – 400 708. Tel: 022 61169000 / 61150000, Fax No. 61169699.

Other registrations of Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669.

Compliance Officer: Ms. Binkle Oza; Tel: 022-62263303; email id: complianceofficer@sharekhan.com

For any complaints/grievance, email us at igc@sharekhan.com or you may even call Customer Service desk on - 022- 41523200 / 022-69920600