

March 31, 2021

Shriram Transport Finance Company Limited: Provisional [ICRA]AAA(CE) (Stable) assigned to non-convertible debentures

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible Debentures (NCDs)	-	1000.00	Provisional [ICRA]AAA(CE) (Stable); assigned
Fixed Deposit Programme	-	-	MAA+(Stable); Outstanding
Total	-	1000.00	

Rating Without Explicit Credit Enhancement	[ICRA]AA
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*Instrument details are provided in Annexure-1

Note: The (CE) suffix mentioned alongside the rating symbol indicates that the rated instrument/facility is backed by some form of explicit credit enhancement. This rating is specific to the rated instrument/facility, its terms and structure and does not represent ICRA's opinion on the general credit quality of the entity concerned. The last row in the table above also captures ICRA's opinion on the rating without factoring in the explicit credit enhancement

Rationale

The rating of the NCDs is based on the strength of the presence of a cover pool (25% over-collateralisation as a percentage of the NCD principal outstanding) and 5% cash collateral (as a percentage of NCD issuance amount), to support the servicing of the NCDs in the event of non-payment by Shriram Transport Finance Company Limited (STFC/ Issuer). STFC shall execute an Agreement for Assignment and a power of attorney wherein it would agree to assign the cover pool assets and cash collateral to a special purpose vehicle in the form of a Trust (SPV/ Trust) set up for this purpose on the occurrence of a predefined trigger event (details given in the salient covenants of the rated facility section) during the tenure of the rated facility. On the occurrence of a trigger event, there would not be any requirement of any further deed or action for the assignment by STFC. Post the assignment, the Trust shall become the legal owner of the assigned receivables (i.e. the cover pool assets shall be bankruptcy remote from the other creditors of STFC). In turn, the Trust will provide an unconditional and irrevocable guarantee to the Debenture Trustee of the rated NCDs and would transfer all collections from the cover pool to the collection & payout account¹ under its guarantee obligation.

The legal final maturity of the transaction is 10 years from the deemed date of allotment. Interest payments on the NCDs is promised on a quarterly basis (prior to occurrence of the trigger event) and on a monthly basis post the trigger event. Principal payments on the NCDs are promised only on legal final maturity. However, STFC is expected to make principal repayment at the end of fifth, sixth and seventh year (one third of the initial amount every year). Failure on the part of STFC to meet any scheduled interest or expected principal repayment would be a trigger event. Cash collateral will be used by the Trustee to meet any shortfall in promised payment on the respective due date.

Adequacy of credit enhancement

The guarantee provided by the Trust is unconditional and irrevocable. Further, a Trustee-monitored payment mechanism is in place to ensure payments on the rated debt as given below:

- The primary obligation of meeting the NCD payments is on STFC. Hence, STFC shall fund the designated account to the extent of the principal and interest payable on two business days prior to the due date (T).

¹ Account maintained and operated by the Debenture Trustee

Key predefined trigger events, the occurrence of which would lead to the invocation of the Trust guarantee, are given below:

- Failure to meet the 1.25x security cover requirement
- Failure by the Issuer to meet the prefunding requirement, i.e., credit of amounts in the designated account by T-2 day of the each coupon payment date or the expected principal repayment date
- Cross-default/ insolvency proceedings (not withdrawn in 10 business days)/ any legal or regulatory proceedings commenced against the Issuer, with a material adverse effect
- Any default by the Issuer in relation to its servicing obligations under any securitisation transaction
- The gross Stage 3 assets on the books of the Issuer crossing 12%
- Capital adequacy ratio of the Issuer falling below 15%
- Rating of the issuer is downgraded to or below AA-
- Cumulative asset liability mismatch for the issuer for the next 12 months
- Failure of the issuer to comply with any of the covenants (not remedied within 30 days)

On the occurrence of a trigger event, the cover pool assets and cash collateral shall be immediately assigned to the Trust. The Trust shall appoint STFC as the servicer for the cover pool assets transferred. The collections from the cover pool will be used for payments to the debenture holders as per the defined payment mechanism.

The above attributes led to an enhancement in the rating of the said instrument to [ICRA]AAA(CE) (Stable) against the unsupported rating of [ICRA]AA.

Salient covenants of the rated facility

- » Minimum security cover of 1.25x is to be maintained on the NCD principal outstanding and the asset cover should consist of loans given for personal vehicle and commercial vehicle loans originated by STFC. Further, the cover pool assets need to be maintained/replenished by STFC as per the eligibility criteria mentioned in the transaction documents.
- » For computing the minimum security cover, only the principal amount of receivables that fall due prior to the legal final maturity of the NCDs will be considered. Further, contracts that are delinquent by more than 60 days would be excluded. Delinquent contracts should not constitute more than 15% of the pool principal amount.

Key rating drivers and their description

Credit strengths

Presence of cover pool and cash collateral to support servicing of NCD facility in case of non-payment by entity – The primary obligation of meeting the NCD payments is on STFC. However, if STFC does not meet the payment obligations on the NCDs, the collections from the cover pool will be available to the Debenture Trustee. The cover pool to be maintained would be 1.25x of the NCD's principal outstanding. The principal amount on the NCDs is promised to the NCD investors on the legal final maturity. A cash collateral of 5% of the NCD issuance amount would be used by the Trustee to meet any shortfall in promised payments.

Stringent eligibility criteria for cover pool – Contracts at the time of assignment should not be more than 30 days overdue and contracts that are delinquent by more than 60 days would be excluded from the cover computation. Even the proportion of contracts, which are delinquent, should be less than 15% of the pool at any point of time. Additionally, eligibility criteria related to LTV, seasoning, geographical concentration, IRR, loan size and asset-class wise concentration has been specified to ensure robust quality of the pool.

Credit challenges

Interest rate risk as pool yield could be lower in subsequent cover pool – The benefit available on account of the difference between the pool yield and the NCD yield (fixed rate) may shrink in case the pool, at the time of the occurrence of the trigger event, consists of contracts which have a lower IRR. However, this is mitigated as the major part of STFC's portfolio comprises loans with an IRR of more than 14%.

Liquidity position

For the Provisional [ICRA]AAA(CE) (Stable) rated NCDs: Superior

The principal amount on the NCD is promised to the lender only on the legal final maturity. The scheduled interest is payable on a quarterly (pre-trigger) and monthly (post-trigger) basis. The cash collateral of 5% (of the NCD issue size) is a part of the transaction to meet any shortfall in the promised repayment. These impart significant liquidity support to the instrument. The cash flows from the cover pool along with the cash collateral are expected to be comfortable to meet the debt servicing if the entity cannot meet the payments on the NCDs.

For MAA+(Stable) rating: Adequate

STFC's liquidity position remains adequate with positive cumulative mismatches across all the near-term buckets. As on December 31, 2020, the company's on-balance sheet and off-balance sheet liquidity buffer aggregated over Rs. 13,000 crore, which comfortably covered the scheduled outflows (including principal and interest repayments) over the next three months.

Rating sensitivities

Positive factors – Not Applicable

Negative factors – The rating could be downgraded due to either of the following events:

- Non-adherence to the key transaction terms envisaged at the time of the rating
- Material deterioration in the credit profile of STFC

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Non-Banking Finance Companies Covered Bond Transactions
Parent/Group Support	Not Applicable
Consolidation/Standalone	Not Applicable

About the company

STFC, incorporated in 1979, is a deposit-accepting non-banking financial company and a part of the Shriram Group of companies. It is the market leader in the used-CV financing space with a pan-India presence encompassing 1,799 branches and 808 rural centres as on December 31, 2020. STFC primarily provides financing for vehicles such as CVs (both pre-owned and new), tractors, and passenger vehicles. Assets under STFC's management aggregated Rs. 1,14,932 crore as on December 31, 2020.

In FY2020, STFC reported a net profit of Rs. 2,502 crore on an AUM of Rs. 109,749 crore compared to a net profit of Rs. 2,564 crore on a AUM of Rs. 104,482 crore in FY2019. Subsequently, in 9M FY2021, STFC achieved a net profit of Rs. 1,732 crore compared to a net profit of Rs. 2,278 crore in 9M FY2020.

Key Financial Indicators

Parameter	FY2019 IND-AS	FY2020 IND-AS	9M FY2021 IND-AS
Total Income	15,457	16,519	12,939
Profit after Tax	2,564	2,502	1,732
Net Worth	15,836	18,005	20,947
Assets under Management	104,482	109,749	114,932
Return on Assets	2.3%	2.2%	1.9%
Return on Net Worth	17.5%	14.7%	12.0%
Gearing	5.6	5.2	4.6
Capital Adequacy Ratio	20.3%	22.0%	23.6%
% Gross Stage 3	8.4%	8.4%	7.1%
% Net Stage 3	5.7%	5.6%	4.3%
% Net Stage 3/Net Worth	36%	33%	23%

Source: STFC and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Sl	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018
					Mar 31, 2021	-	-	-
1	NCD	Long term	1000.00	1000.00	Provisional [ICRA]AAA(CE) (Stable)	-	-	-

For details of other ICRA-rated instruments of the company, refer the rationales given [here](#)

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	NCD	Yet to be issued	TBD	NA	1000.00	Provisional [ICRA]AAA(CE) (Stable)

Source: Company

For details of other ICRA rated instruments of the company, refer the rationales given [here](#)

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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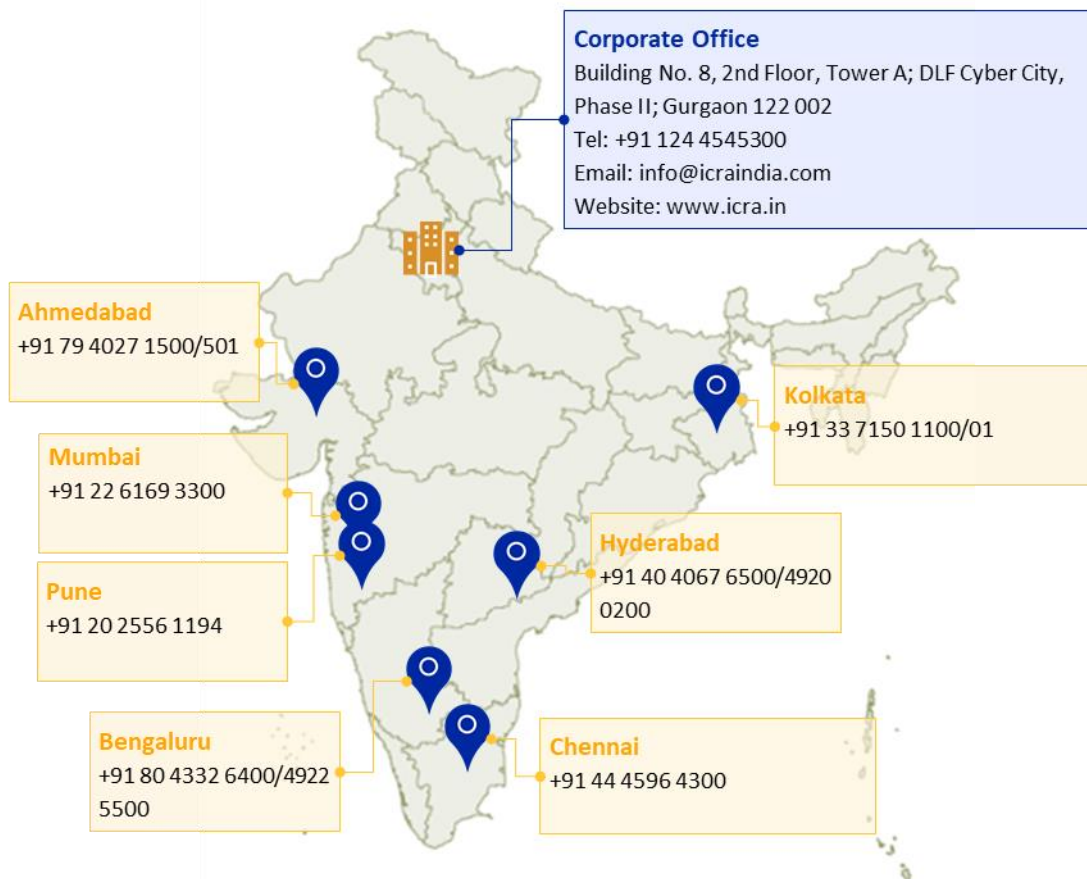


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