

Shriram Transport Finance Company Limited

April 05, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fixed Deposit Programme	-	-	MAA+ (Stable); Reaffirmed
Total	-	-	

*Instrument details are provided in Annexure-1

Rationale

The rating factors in Shriram Transport Finance Company Limited's (STFC) dominant market position, its extensive track record and strong customer outreach as well as its competitive position in the pre-owned commercial vehicle (CV) financing market. The rating also factors in STFC's adequate capitalisation levels (Tier I of 14.96% as on December 31, 2018), diversified borrowing mix, favourable liquidity profile and proven ability to maintain a good earnings profile through cycles (return on assets (RoA) of 2.46% in 9M FY2019).

These positives, however, are offset, to an extent, by the concentration of STFC's portfolio in the CV segment, which exposes it to industry-specific risks, and the resultant lack of diversity in its revenue stream. The rating is also constrained by the relatively weak asset quality indicators with gross stage 3 advances of 8.78% as on December 31, 2018 (9.53% as on March 31, 2018). The portfolio vulnerability is further augmented by the relatively higher yielding albeit riskier target borrower profile, largely consisting of first time users/buyers who could be more vulnerable to income shocks. Going forward, the company's ability to have a calibrated loan growth, while maintaining prudent capitalisation and, adequate profitability and improving the asset quality, will remain a key rating monitorable.

Outlook: Stable

ICRA believes STFC will continue to benefit from its franchise and will maintain its dominant market position in the pre-owned CV financing segment as well as its earnings profile. The outlook may be revised to Positive if there is a substantial improvement in the company's profitability and asset quality indicators. The outlook may be revised to Negative if there is a significant deterioration in STFC's asset quality and solvency profile.

Key rating drivers

Credit strengths

Extensive track record and dominant player in pre-owned CV financing segment – STFC is one of the largest CV financiers in the country with assets under management (AUM) of Rs. 1,03,818 crore as on December 31, 2018 (Rs. 90,019 crore as on December 31, 2017). As on December 31, 2018, pre-owned vehicle loans stood at Rs. 86,126 crore (83% of AUM), new vehicle loans at Rs. 12,719 crore (12% of AUM) and the balance was for equipment finance and working capital loans.

The company has an experienced management team with the senior level having an experience of nearly 40 years in CV financing. STFC's well laid-out branch network, credit appraisal and monitoring systems have enabled it to establish itself as a preferred lender in the CV financing sector.

Adequate capitalisation profile – STFC’s capitalisation profile is adequate for the current scale of operations with a net worth of Rs. 15,062 crore and CRAR of 19.72% (Tier I - 14.96%) as on December 31, 2018. The gearing increased marginally to 5.95 times as on December 31, 2018 from 5.21 times as on March 31, 2018. With the migration to IND-AS in Q1FY2019 wherein the company is required to make provisions on the basis of expected credit loss, there was a decline in the provisioning for gross stage 3 assets. This resulted in a write back and increased STFC’s net worth by Rs. 911 crore. At the same time, the reduced provision cover on stage 3 assets has led to a weaker solvency profile (net NPA in relation to net worth of 38.8% as on December 31, 2018 compared with 16.9% under iGAAP as on March 31, 2018). The company’s capitalisation is expected to remain adequate over the medium term, supported by healthy internal capital generation (return on equity (RoE) of 17.54% in 9M FY2019) and modest growth plans. The improvement in STFC’s solvency profile would also be a monitorable. However, if the company’s loan growth exceeds 15-20%, it would need external capital to maintain a prudent capitalisation profile.

Good profitability – STFC has been reporting good profitability with RoA and RoE of 2.46% and 17.54%, respectively in 9M FY2019 (RoA of 2.4% and RoE of 16.0% in 9M FY2018). The performance was supported by a 20% increase in net interest income and a decrease in credit costs to 2.47% (3.82% in FY2018).

Diversified borrowing profile – STFC has a well-diversified borrowing mix consisting of debentures (40%), banks/FIs (42%), fixed deposits (11%) and commercial papers (7%) including foreign borrowings, which constituted 5.5% of the total funding as on December 31, 2018. Further, the company is an active issuer in the securitisation/assignment market (17% of the total AUM as on December 31, 2018 was through securitisation, while 2% was through direct assignment), which provides an additional funding source. Nevertheless, STFC would need to raise funds for business growth, given the systemic tightening of liquidity, the cost of funds for the company could increase in the near term.

Credit challenges

Weak asset quality indicators – Given the target borrower profile of first time users/buyers who are relatively more vulnerable to income shocks, the company’s asset quality indicators remain weak. The cash flows of the borrowers were impacted by the slowdown in economic activity and hence their debt servicing ability was impacted. STFC’s reported asset quality numbers were also affected by the migration to IND-AS under which delinquent assets from the securitised portfolio as well as interest accrued on delinquent accounts were considered as on-balance sheet and included in the calculation of gross stage 3 assets. However, with some recovery and portfolio growth, the gross stage 3 assets NPA declined to 8.78% as on December 31, 2018 from 9.53% as on March 31, 2018. Under iGAAP, the company had a good provision coverage ratio (PCR) of over 70%. However, under IND-AS, the PCR for stage 3 assets was 35.28% as on December 31, 2018, while it was 2.82% (compared with a standard asset provisioning of 0.4% earlier) for stage 1 and 2 assets. Overall, the company’s ability to control fresh slippages and report an improvement in its asset quality indicators would be a key monitorable.

Liquidity position

The company has a comfortable liquidity profile which is supported by its unencumbered cash and liquid investments of Rs. 3132 crore and has no cumulative mismatches in any of the ALM buckets as on December 31, 2018. STFC has the ability to raise funds from a diverse base and had unutilised drawable bank lines of Rs. 3,880 crore as on December 31, 2018 which provides adequate liquidity support in the near term. Further, given its presence in the retail lending segment, a large portfolio of the company is eligible for sell-downs and can be used to raise funds through securitisation/assignment.

Analytical approach

Analytical Approach	Comments
Applicable Methodologies	Rating ICRA's Credit Rating Methodology for Non-Banking Finance Companies
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

About the company

STFC, a deposit-accepting asset financing non-banking financial company, was incorporated in 1979 and is a part of the Shriram Group of companies. It provides financing for vehicles such as CVs (both pre-owned and new), tractors, and passenger vehicles and is the market leader in used CV financing. It has a pan-India presence, with 1,348 branches and 885 rural centres as on December 31, 2018. STFC is also engaged in the construction equipment financing business through its erstwhile wholly-owned subsidiary, Shriram Equipment Finance Company that was merged with STFC with effect from April 1, 2015.

STFC reported a net profit of Rs. 1,568.04 crore in FY2018 on a total income base of Rs. 12,264.80 crore compared to a net profit of Rs. 1,257.34 crore on a total income base of Rs. 10,824.47 crore in FY2017. STFC reported a net profit of Rs. 1,817.92 crore in 9M FY2019 on a total income base of Rs. 11,610.42 crore.

Key financial indicators

	FY2017 iGAAP	FY2018 IND-AS	9M FY2019 IND-AS
Total Income	10,824	12,265	11,610
Profit after Tax	1,257	1,568	1,818
Net Worth	11,292	12,572	15,062
Total Assets	74,400	88,471	1,08,757
Return on Assets	1.77%	1.93%	2.46%
Return on Net Worth	11.61%	13.14%	17.54%
Gearing (times)	4.89	5.21	5.95
% Gross NPAs	8.16%	9.53%	8.78%
% Net NPAs	2.65%	6.08%	5.86%
% Net NPA/Net Worth	14.69%	46.13%	38.81%
Capital Adequacy Ratio	16.94%	16.87%	19.72%

Source: Company and ICRA research

CRAR: Capital to risk weighted assets ratio, NPA: Non-performing asset
Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Current Rating (FY2020)					Chronology of Rating History for the Past 3 Years			
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2018	Date & Rating in FY2018	Date & Rating in FY2015	
				April 2019	Mar 2018	Nov 2017	Apr 2014	
1	Fixed Deposit	NA	NA	Medium Term	MAA+ (Stable)	MAA+ (Stable)	MAA+ (Stable)	
2	Subordinate Debt Programme	50	0	Long Term	-	[ICRA]AA (Stable); Withdrawn	[ICRA]AA (Stable); Withdrawn	
							[ICRA]AA (Stable); Assigned	

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	Fixed Deposit Programme	NA	NA	NA	NA	MAA+ (Stable)

Source: ICRA

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