

SHRIRAM CITY UNION FINANCE

Bracing for near-term challenges

India Equity Research | Banking and Financial Services



Shriram City Union Finance (SCUF) reported below estimated Q1FY21 PAT of INR1.9bn on higher provisions (covid-19 related) even as core performance came in line with estimate (albeit, softer). Headline asset quality held up on lower slippages--a natural and wholly expected corollary of the moratorium option. Collection efficiency (>70% in June) and moratorium (at 25%) have been steadily improving, but sustenance is key. Further, scope of application of the restructuring scheme and eligibility under the ECLGS scheme will be critical to fortunes. As anticipated, business momentum decelerated with >6% YoY dip in AUM. This, combined with lower NIM (down 13bps QoQ), led to tepid core. That said, valuations at 0.6x FY21E P/BV render comfort. Maintain 'BUY' with TP of INR1,080. Target multiple of 1.0x FY22E P/BV accounts for higher uncertainty around its key operating segment (SME) and possibility of a less-than-favourable merger ratio in the three-way merger envisaged in Shriram Group restructuring.

Asset quality holding up; outlook uncertain

Asset quality improved with stage-3 assets declining to 7.3% (from 7.9%) with improvement across segments (ex-personal loans), partially a reflection of moratorium at play. Going forward, we remain cautious in one of its key operating segments (SME), which though improving from the early Q1FY21 trough, needs monitoring. This segment, we believe, will shape the company's asset quality outcomes.

Core metrics continue to be soft

Growth remains soft with disbursements at INR13.3bn, which led to AUM falling 6% YoY/2% QoQ to INR284bn (broadly in line with estimate). Within segments, growth was largely supported by gold loans and used 2W segment as other segments remained relatively tepid. Given weak growth and limited levers for NIM improvement, we expect core momentum to remain weak in the near term.

Outlook and valuation: Valuation comfort; maintain 'BUY'

Events over the past two years have tested SCUF's resilience, particularly given its reliance on the self-employed segment. The company responded by going slow on growth and recalibrating collection strategies to navigate the challenging environment. Covid-19 additionally renders the near-term outlook challenging. Post a deep correction, the stock trades at 0.6x FY21E P/BV, rendering comfort. We maintain 'BUY/SP'.

Financials

(INR mn)

Year to March	Q1FY21	Q1FY20	Growth (%)	Q4FY20	Growth (%)	FY20	FY21E	FY22E
Net revenue	8,771	9,557	(8.2)	9,038	(3.0)	37,890	38,731	40,976
Net profit	1,923	2,532	(24.1)	1,531	25.6	10,159	9,091	9,287
Dil. EPS (INR)	29.1	38.4	(24.1)	23.2	25.6	153.8	137.6	140.6
Adj. BV (INR)						964.6	1,009.4	1,076.1
Price/ Adj book (x)						0.7	0.7	0.6
Price/ Earnings (x)						4.5	5.0	4.9

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Overweight

MARKET DATA (R: SHCU.BO, B: SCUF IN)

CMP	: INR 662
Target Price	: INR 1,080
52-week range (INR)	: 1,572 / 617
Share in issue (mn)	: 66.0
M cap (INR bn/USD mn)	: 44 / 2,273
Avg. Daily Vol.BSE/NSE('000)	: 16.9

SHARE HOLDING PATTERN (%)

	Current	Q4FY20	Q3FY20
Promoters *	33.9	33.9	33.9
MF's, FI's & BK's	5.6	5.9	5.9
FII's	26.8	27.4	27.4
Others	33.6	32.8	32.7
* Promoters pledged shares (% of share in issue)	:		NIL

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Banks and Financial Services Index
1 month	(2.1)	2.7	(3.5)
3 months	(9.6)	10.5	(3.2)
12 months	(53.1)	(1.0)	(25.0)

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Table 1: Q1FY21 earnings snapshot....

(INR mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Comments
Interest income	14,117	14,864	(5.0)	14,495	(2.6)	
Interest expense	5,375	5,316	1.1	5,463	(1.6)	
Net interest income	8,742	9,548	(8.4)	9,032	(3.2)	Revenue momentum soft owing to >40bps QoQ NIM dip and softer AUM growth
Non-interest income	29	9	231.8	6	363.5	
Net revenues	8,771	9,557	(8.2)	9,038	(3.0)	
Operating expenses	3,105	3,695	(16.0)	3,882	(20.0)	
Operating profit	5,666	5,862	(3.3)	5,157	9.9	
Provisions	3,102	2,021	53.5	3,127	(0.8)	Provisioning remained elevated as company made iNR4bn towards COVID
Profit before tax	2,564	3,841	(33.2)	2,029	26.4	
Tax expense	642	1,309	(51.0)	498	28.7	
Profit after tax	1,923	2,532	(24.1)	1,531	25.6	
EPS (INR)	29.1	38.4	(24.1)	23.2	25.6	
Key Metrics						
AUM	2,95,470	2,86,460	3.1	2,97,220	(0.6)	AUM growth was softer - a trend expected to sustain in near to medium term
Non-gold	2,66,880	2,58,820	3.1	2,67,930	(0.4)	
Gold	28,590	27,640	3.4	29,290	(2.4)	
Disbursements	58,220	45,830	27.0	52,010	11.9	
Non-gold	39,780	32,750	21.5	35,510	12.0	
Gold	18,440	13,080	41.0	16,500	11.8	
Gross Stage-3 (%)	8.5	9.1		8.7		Headline asset quality came in lower but sustainability is question
NNPA (%)	5.0	5.2		5.1		
Shriram Housing Finance						
AUM	21,000	17,210	22.0	18,750	12.0	
Disbursements	3,860	110	NA	980	293.9	
GNPA (%)	2.7	3.2		3.0		
NNPA (%)	2.1	2.4		2.4		

Source: Company, Edelweiss research

Financial snapshot

(INR mn)

Year to March	Q1FY21	Q1FY20	Growth (%)	Q4FY20	Growth (%)	FY20	FY21E	FY22E
Operating income	14,117	14,864	(5.0)	14,495	(2.6)	56,626	56,263	58,333
Interest expended	(5,375)	(5,316)	1.1	(5,463)	(1.6)	(20,456)	(19,447)	(19,683)
Net operating income	8,742	9,548	(8.4)	9,032	(3.2)	36,170	36,815	38,651
Other income	29	9	231.8	6	363.5	1,720	1,915	2,325
Net revenues	8,771	9,557	(8.2)	9,038	(3.0)	37,890	38,731	40,976
Operating expenses	(2,904)	(3,492)	(16.8)	(3,679)	(21.1)	(14,290)	(14,874)	(16,026)
Pre-provision profit	5,867	6,065	(3.3)	5,360	9.5	23,600	23,857	24,950
Provisions and write off	(3,102)	(2,021)	53.5	(3,127)	(0.8)	(9,010)	(11,041)	(11,865)
Operating profit	2,765	4,044	(31.6)	2,233	23.9	14,590	12,816	13,085
Depreciation	(201)	(203)	(1.0)	(203)	(1.2)	(824)	(695)	(702)
Profit before tax	2,564	3,841	(33.2)	2,029	26.4	13,765	12,121	12,383
Tax	(642)	(1,309)	(51.0)	(498)	28.7	(3,607)	(3,030)	(3,096)
Profit after tax	1,923	2,532	(24.1)	1,531	25.6	10,159	9,091	9,287
Diluted EPS (INR)	29.1	38.4	(24.1)	23.2	25.6	153.8	137.6	140.6

Ratios (%)

Cost/income	35.4	38.7	42.9	39.9	40.2	40.8
Tax rate	25.0	34.1	24.6	26.2	25.0	25.0

Valuation metrics

Book value per share (INR)	1,088.8	1,194.9	1,303.9
Adjusted book value/share (INR)	964.6	1,009.4	1,076.1
Price/ BV (x)	0.6	0.6	0.5
Price/Earnings (x)	4.5	5.0	4.9

Q1FY21 Concall takeaway

On the current environment

- Will not be aggressive in lending for some time and fresh disbursements will be done after meeting customers and assessing their cash flow mechanics
- June saw decent momentum in disbursements – 2Wheeler and gold loans; Hopeful of sustaining the same
- Marginally improved cost; As a result, Cost/Income ratio improved to 35.4% in Q1FY21 as compared to 38.4% in Q1FY20
- Manpower rationalization will continue for at least 2 more quarters
- Comfortable with the current liquidity position
 - Raised fresh resources of INR10.5bn in current quarter
 - Fixed Deposit subscriptions continued to grow stronger
 - Focused on raising long term liquidity
- Recently obtained license from IRDAI to cross sell insurance products; Fee received from this line of business in Q1FY21 was INR 50mn
- Housing subsidiary also getting back to normalcy in terms of business momentum; Other operating metrics improving
- Management prefers to give extra time to customers to pay rather than restructure existing loans and make things look good optically; However, approach will depend on guidelines of RBI
- No clarity on merger as of now
- Recently started branches in East India and hence it will take some time for penetration
- North India is fairly more penetrated –
 - Idea of the company is to start with a small ticket size and then expand as they learn local nuances
 - Share of North India in overall AUM will go up eventually

On asset quality and provisioning

- Collection efficiency continued to improve month on month and stands at 71% for June, 2020 (vs. 52% for May, 2020)
 - According to the management, this is a better indicator of the health of the loan book – as it illustrates the percentage of people getting back to normal business activity levels
- Collections were as follows
 - In the month of April INR5.6bn was collected o/w collection against gold loan was zero
 - In the month of May INR10bn was collected o/w collection against gold loan was INR3bn
 - In the month of June INR14bn was collected o/w collection against gold loan was INR4bn
- A COVID specific provision of INR1.8bn was made in Q1FY21; Aggregate COVID-related provisioning now is INR6.1bn (2.13% of AUM)

Company Description

SCUF was incorporated in 1986 as a deposit accepting NBFC. Prior to 2002, it was exclusively engaged in transport finance with special emphasis on financing pre-owned commercial vehicles to small road transport operators. In 2002, it extended its product lines to include small-ticket retail financing, viz., consumer durables, two wheelers, personal, and enterprise loans. It deliberately went slow on disbursements in the CV segment, which has become a key area of its group company Shriram Transport Finance. The company's operations are largely concentrated in the southern states like Andhra Pradesh, Tamil Nadu, and Karnataka and the western region (particularly Maharashtra).

Investment Theme

SCUF follows a unique and sound business model with presence in high-yielding, high growth, small-ticket retail finance segment (auto loans, personal loans, business finance, and retail gold loans), and RoA of 3.5-% plus. Events over the past couple of years (demonetisation and GST) had put to test SCUF's resilience, particularly given its dependence on the self-employed segment. The company has not been aggressive on the growth front and maintained a well-matched ALM, which should help it sail through the currently challenging operating environment. Covid-19, additionally renders the near-term outlook for the company challenging, especially the all-important SME segment. Post-crisis, we expect operating leverage and credit cost containment (sub-3%) to support RoA of 3.5% and RoE of 17%-plus. At CMP, the stock trades at 0.6x FY21E P/ABV. We maintain 'BUY/SO'.

Key Risks

SCUF operates in the small-ticket retail finance segment in semi-urban and rural areas and may face stiff competition from banks, other financial institutions, and multinational players, which have access to cheap funds. Our earnings estimates may not fructify if the company is unable to maintain its spreads at expected levels due to inability to maintain yields amidst stiff competition.

Financial Statements

Key Assumptions

Year to March	FY19	FY20	FY21E	FY22E
Macro				
GDP(Y-o-Y %)	6.8	5.0	5.8	6.5
Inflation (Avg)	3.4	4.3	4.8	5.0
Repo rate (exit rate)	6.3	5.2	4.5	5.0
USD/INR (Avg)	70.0	71.5	71.0	70.0
Sector				
Credit growth	14.0	11.0	13.0	15.0
Borrowings growth (%)	13.0	12.0	14.0	15.0
Bank's base rate (%)	9.0	8.7	8.5	8.5
Wholesale borr. cost (%)	8.5	8.5	8.3	8.1
G-sec yield	7.0	7.1	7.1	7.1
Company				
Balance sheet assumption (%)				
Op. metric assump. (%)				
Yield on advances	19.3	18.9	18.5	18.1
Cost of funds	9.3	9.6	9.5	9.4
Net interest margins	13.6	13.1	13.3	13.5
Dividend income	18	19	23	22
Employee cost growth	17.0	3.0	5.3	9.2
Other opex growth	2.8	(9.6)	2.3	5.5
Disbursement growth	(3.4)	(5.6)	5.7	11.4
Securit. during the yr	9,000.0	9,000.0	9,000.0	9,000.0
Bad debt written off	2.3	2.7	1.6	1.6
Gross NPLs	8.7	7.9	11.5	14.0
Prov Cov	69.1	49.0	50.0	53.0
Net NPLs	2.7	4.4	6.5	7.7

Income statement

(INR mn)

Year to March	FY19	FY20	FY21E	FY22E
Interest income	56,100	56,626	56,263	58,333
Interest expended	19,763	20,456	19,447	19,683
Net interest income	36,337	36,170	36,815	38,651
Other income	1,776.21	1,719.71	1,915.32	2,325.26
Net revenues	38,114	37,890	38,731	40,976
Operating expense	14,997	15,114	15,568	16,728
- Employee exp	8,227	8,475	8,923	9,747
- Depn /amortisation	340	824	695	702
- Other opex	6,430	5,815	5,950	6,279
Preprovision profit	23,116	22,775	23,163	24,248
Provisions	7,956	9,010	11,041	11,865
Profit Before Tax	15,161	13,765	12,121	12,383
Less: Provision for Tax	5,273	3,607	3,030	3,096
Profit After Tax	9,888	10,159	9,091	9,287
Shares o /s (mn)	66	66	66	66
Basic EPS (INR)	149.9	153.8	137.6	140.6
Diluted shares o/s (mn)	66	66	66	66
Adj. Diluted EPS (INR)	149.9	153.8	137.6	140.6
Dividend per share (DPS)	23.0	25.0	27.0	27.0
Dividend Payout Ratio(%)	18.0	19.0	22.9	22.5

Growth ratios (%)

Year to March	FY19	FY20	FY21E	FY22E
Operating income growth	11.0	(0.5)	1.8	5.0
Revenues	11.0	(0.6)	2.2	5.8
Opex growth	10.1	0.8	3.0	7.5
PPP growth	11.6	(1.5)	1.7	4.7
Adjusted Profit	48.8	2.7	(10.5)	2.2

Operating ratios

Year to March	FY19	FY20	FY21E	FY22E
Yield on assets	21.0	20.5	20.4	20.4
Cost of funds	9.3	9.6	9.5	9.4
Net interest margins	13.6	13.1	13.3	13.5
Spread	11.7	10.9	10.9	10.9
Cost-income	39.3	39.9	40.2	40.8
Tax rate	34.8	26.2	25.0	25.0

Balance sheet		(INR mn)			
As on 31st March	FY19	FY20	FY21E	FY22E	
LIABILITIES	-	-	-	-	
Share capital	659	660	660	660	
Reserves & Surplus	62,982	71,203	78,202	85,397	
Net worth	63,642	71,863	78,862	86,057	
Subordinate debt	15,307	16,307	17,307	18,307	
Secured loans	184,096	167,970	165,642	171,914	
Unsecured loans	21,623	21,723	21,823	21,923	
Def. Tax Liability (net)	(250)	-	-	-	
Total liabilities	284,417	277,863	283,633	298,201	
Loans	295,833	290,850	304,126	326,405	
Investments	730	730	730	730	
Total current assets	11,621	6,616	4,847	3,141	
Total Current Liab	28,755	25,067	30,600	36,400	
Net current assets	(17,134)	(18,451)	(25,753)	(33,259)	
Fixed assets	4,988	4,733	4,531	4,325	
Total assets	284,417	277,863	283,633	298,201	
Loan growth	8.1	(1.7)	4.6	7.3	
EA growth	9.8	(2.3)	2.2	5.3	
Provision coverage	69.1	49.0	50.0	53.0	
Gross NPA ratio	8.7	7.9	11.5	14.0	
Net NPA ratio	2.7	4.4	6.5	7.7	

RoE decomposition (%)		FY19	FY20	FY21E	FY22E
Year to March					
Op. income /Assets		14	13	13	13
Net int. income/assets		14.3	13.7	14.0	14.3
Other income/Assets		0.7	0.6	0.7	0.8
Operating expense/assets		(5.6)	(5.5)	(5.6)	(5.8)
Provisions/assets		(3.0)	(3.3)	(4.0)	(4.1)
Taxes/assets		(2.0)	(1.3)	(1.1)	(1.1)
Total costs/assets		(10.6)	(10.0)	(10.7)	(11.1)
ROA		3.7	3.7	3.3	3.2
Equity/assets		22.3	24.5	27.3	28.8
ROAE (%)		16.6	15.0	12.1	11.3

Valuation parameters		FY19	FY20	FY21E	FY22E
Year to March					
Adj. Diluted EPS (INR)		149.9	153.8	137.6	140.6
Y-o-Y growth (%)		48.8	2.6	(10.5)	2.2
BV per share (INR)		965.4	1,088.8	1,194.9	1,303.9
Adj. BV per share (INR)		886.8	964.6	1,009.4	1,076.1
Diluted P/E (x)		4.4	4.3	4.8	4.7
Price/ Adj. BV (x)		0.7	0.7	0.7	0.6
Dividend Yield (%)		3.5	3.8	4.1	4.1

Name	Diluted P/E (X)		P/B (X)		ROAE (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Shriram City Union Finance	4.8	4.7	0.6	0.5	12.1	11.3
HDFC	17.0	15.0	2.6	2.4	12.2	12.0
Indiabulls Housing Finance	4.9	3.8	0.6	0.6	12.9	15.5
LIC Housing Finance	4.8	4.2	0.7	0.6	14.9	15.3
Mahindra & Mahindra Financial Services	10.9	8.8	0.9	0.9	8.7	10.4
Manappuram Finance	8.9	7.7	2.2	1.9	26.8	26.9
Muthoot Finance	14.1	12.5	3.2	2.7	25.3	23.6
REC	-	-	-	-	15.7	17.6
Repco Home Finance	2.3	2.0	0.4	0.3	17.2	17.1
Shriram Transport Finance	4.4	3.9	0.8	0.6	18.6	17.9
Median	4.8	4.0	0.7	0.6	15.3	16.3
AVERAGE	5.5	4.7	1.1	1.0	16.4	16.7

Source: Edelweiss research

Additional Data

Directors Data

Debendranath Sarangi	Chairman	Yalamati Srinivasa Chakravarti	Managing Director & CEO
Diwakar Bhagwati Gandhi	Director	Duruvasan Ramachandra	Director
Maya Swaminathan Sinha	Director	Pranab Prakash Pattanayak	Director
Ramarao Muralidharan Coimbatore	Director	Ranvir Dewan	Director
Shashank Singh	Director	Venkataraman Murali	Director
Ignatius Michael Viljoen	Director		

Auditors - G.D. Apte & Co.

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Shriram capital ltd	33.89	Dynasty acq fpi ltd	20.34
Piramal enterprises	9.97	East bridge cap mast	5.89
East bridge capital	3.88	Matthews intl capita	2.63
East bridge capital	2.49	Ward ferry mangement	2.43
Wf asian smaller com	2.3	Aditya birla sun lif	1.97

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
No Data Available			

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Aavas Financiers	REDUCE	SU	M	Aditya Birla Capital	BUY	SO	H
Axis Bank	HOLD	SO	M	Bajaj Finserv	REDUCE	SU	L
Bank of Baroda	BUY	SU	M	DCB Bank	BUY	SP	M
Equitas Holdings	BUY	SO	M	Federal Bank	BUY	SO	L
HDFC	BUY	SO	L	HDFC Bank	BUY	SO	L
ICICI Bank	BUY	SO	L	IDFC FIRST BANK	HOLD	SP	L
Indiabulls Housing Finance	HOLD	SU	M	IndusInd Bank	HOLD	SO	L
Kotak Mahindra Bank	BUY	SP	M	L&T Finance Holdings	HOLD	SP	M
LIC Housing Finance	BUY	SO	M	Magma Fincorp	BUY	SP	M
Mahindra & Mahindra Financial Services	BUY	SP	M	Manappuram Finance	HOLD	SU	H
Max Financial Services	BUY	SO	L	Multi Commodity Exchange of India	REDUCE	SP	M
Muthoot Finance	BUY	SO	M	Power Finance Corp	BUY	SP	M
Punjab National Bank	UNDER REVIEW	SU	M	REC	BUY	SP	M
Repco Home Finance	BUY	SP	M	Shriram City Union Finance	BUY	SP	M
Shriram Transport Finance	BUY	SO	M	South Indian Bank	BUY	SP	M
State Bank of India	BUY	SO	L	Union Bank Of India	HOLD	SU	M
Yes Bank	BUY	SP	M				

ABSOLUTE RATING

Ratings

Expected absolute returns over 12 months

Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings

Criteria

Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings

Criteria

Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings

Criteria

Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

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Coverage group(s) of stocks by primary analyst(s): Banking and Financial Services

Aavas Financiers, Aditya Birla Capital, AU Small Finance Bank Ltd, Axis Bank, Bajaj Finserv, Bank of Baroda, DCB Bank, Equitas Holdings, Federal Bank, HDFC, HDFC Bank, HDFC Life Insurance Company Ltd, ICICI Bank, ICICI Lombard General Insurance Company Ltd, IDFC FIRST BANK, Indiabulls Housing Finance, IndusInd Bank, ICICI Prudential Life Insurance Company Ltd, Kotak Mahindra Bank, LIC Housing Finance, L&T Finance Holdings, Max Financial Services, Multi Commodity Exchange of India, Manappuram Finance, Magma Fincorp, Mahindra & Mahindra Financial Services, Muthoot Finance, Punjab National Bank, Power Finance Corp, REC, Repco Home Finance, SBI Life Insurance Company Ltd, State Bank of India, Shriram City Union Finance, Shriram Transport Finance, South Indian Bank, Union Bank Of India, Yes Bank

Recent Research

Date	Company	Title	Price (INR)	Recos
10-Aug-20	Bank of Baroda	Long road ahead; valuation comfort; <i>Result Update</i>	49	Buy
10-Aug-20	DCB Bank	Steady quarter; evolution of moratorium pool is key; <i>Result Update</i>	83	Buy
07-Aug-20	REC	Steady quarter; forex drives earnings volatility; <i>Result Update</i>	107	Buy

Distribution of Ratings / Market Cap

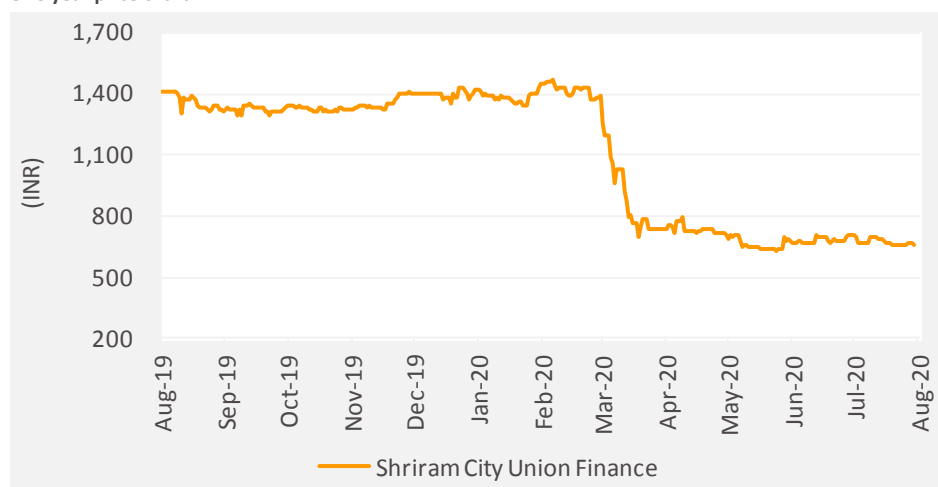
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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