

April 30, 2016

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Rating	<b>BUY</b>
Price	Rs943
Target Price	Rs1,025
Implied Upside	8.7%
Sensex	25,607
Nifty	7,850

(Prices as on April 29, 2016)

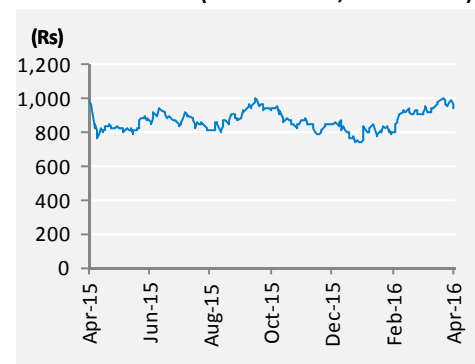
Trading data	
Market Cap. (Rs bn)	213.9
Shares o/s (m)	226.9
3M Avg. Daily value (Rs m)	458.7

Major shareholders	
Promoters	26.05%
Foreign	53.65%
Domestic Inst.	1.97%
Public & Other	18.33%

Stock Performance			
(%)	1M	6M	12M
Absolute	2.1	0.1	(4.2)
Relative	(0.7)	4.7	1.7

How we differ from Consensus			
EPS (Rs)	PL	Cons.	% Diff.
2017	73.9	73.0	1.2
2018	88.0	88.4	-0.4

Price Performance (RIC: SRTTR.BO, BB: SHTF IN)



Source: Bloomberg

**SHTF reported sharp 54.6% YoY decline in reported net earnings as it merged the equipment finance subsidiary with itself, while, migration to 150dpd further necessitated Rs3.0bn increase in provisions. However on standalone basis, SHTF reported 26.3% YoY growth in net profits to Rs4bn. AUMs grew 23% YoY (20% YoY adjusted for the merger) while reported NIMs expanded by 20bp QoQ. Post merger GNPL ratio increased by 200bp QoQ to 6.2% (better than estimates) while coverage ratio declined to 70%. We tweak our earnings to factor improving growth outlook and keep credit cost high as SHTF move towards 120dpd in FY17. We retain BUY with PT of 1,025 based on 2.3x Sep-2017E ABV.**

- **AUM growth picks up to 23% YoY:** AUM growth picked up to 23% YoY in a seasonally strong quarter - 20% YoY growth adjusted for the merger. SHTF has also witnessed continued growth in the demand for new vehicles share of which in total AUMs increased by 207bp QoQ to 10.4%. SHTF suggested that rural demand appears to be picking up while shortage of vehicles in the harvest season will further drive demand and guided for 15% AUM growth for FY17E.
- **Asset quality deteriorates on merger / migration to 150dpd; coverage ratio declines to 70%:** GNPA's increased by 52% QoQ to Rs38.7bn as SHTF migrated to 150dpd and merged its construction equipment subsidiary. SHTF drew down upon its provisioning cover resulting in 970bp decline in coverage ratio to 70.4%. SHTF indicated that movement to 150dpd (from 180dpd) resulted in ~50-70bp increase in GNPLs and further movement to 120dpd during FY17E could further dent GNPL ratio by 100-150bp. SHTF intends to bring down the book in CE business to Rs10bn by FY17E (Rs16bn currently).
- **SHTF has announced a management change:** SHTF has appointed Mr. JS Gujral as MD & CEO of the company and elevated Mr. Umesh Revankar into Shriram Capital - the Group's holding company. Mr. JS Gujral has been with the Shriram Group since 1988 and was the CEO of Shriram Overseas Finance where he was responsible for growing the commercial vehicle financing business in North India. We have tweaked our business growth estimates and factor in higher margins, while keep credit cost high at 250-280bps of loans.

Key Financials (Y/e March)	2015	2016E	2017E	2018E
Net interest income (Rs m)	30,572	40,989	52,218	62,698
Growth (%)	41.6	34.1	27.4	20.1
Non-interest income (Rs m)	4,279	4,329	4,546	5,136
Operating Profit (Rs m)	31,315	38,400	49,254	58,805
PAT (Rs m)	12,378	11,782	16,762	19,968
EPS (Rs)	54.6	51.9	73.9	88.0
Growth (%)	1.1	5.7	42.4	19.1
Net DPS (Rs)	8.5	10.0	11.0	12.0

Profitability & valuation	2015	2016E	2017E	2018E
Spreads / Margins (%)	6.3	7.2	8.0	8.0
RoAE (%)	14.1	12.2	15.2	15.6
RoAA (%)	2.5	2.1	2.6	2.6
P/E (x)	17.3	18.2	12.8	10.7
P/BV (x)	2.3	2.1	1.8	1.5
P/ABV (x)	2.4	2.4	2.2	2.0
Net dividend yield (%)	0.9	1.1	1.2	1.3

Source: Company Data; PL Research

**Exhibit 1: Q4FY16 Financials: Merger with CE impacted reported earnings**

(Rs m)	Q4FY16	Q4FY15	YoY gr. (%)	Q4FY16	QoQ gr. (%)
Interest income	27,207	21,364	27.3	23,675	14.9
Interest expenses	14,474	11,886	21.8	12,239	18.3
<b>Net Interest Income</b>	<b>12,733</b>	<b>9,478</b>	<b>34.3</b>	<b>11,436</b>	<b>11.3</b>
Securitisation income	1,705	1,376	23.9	1,567	8.8
<b>Total Net Interest Income</b>	<b>14,438</b>	<b>10,854</b>	<b>33.0</b>	<b>13,002</b>	<b>11.0</b>
Operating & Other Income	197	160	23.2	193	2.2
<b>Net revenue</b>	<b>14,635</b>	<b>11,014</b>	<b>32.9</b>	<b>13,195</b>	<b>10.9</b>
Operating expenses	3,896	2,991	30.2	3,287	18.5
<b>Operating profit</b>	<b>10,739</b>	<b>8,023</b>	<b>33.9</b>	<b>9,909</b>	<b>8.4</b>
Provision for bad debts	8,567	3,241	164.4	4,199	104.0
<b>Profit before tax</b>	<b>2,172</b>	<b>4,782</b>	<b>(54.6)</b>	<b>5,710</b>	<b>(62.0)</b>
Tax	733	1,615	(54.6)	1,959	(62.6)
<b>Profit after tax</b>	<b>1,439</b>	<b>3,167</b>	<b>(54.6)</b>	<b>3,751</b>	<b>(61.6)</b>
<b>PAT - SHTF S'lone</b>	<b>4,000</b>	<b>3,167</b>	<b>26.3</b>	<b>3,751</b>	<b>6.6</b>
<b>Busines mix</b>					
<b>Total AUM</b>	<b>727,606.0</b>	<b>591,082.8</b>	<b>23.1</b>	<b>665,383.5</b>	<b>9.4</b>
on book	618,783.7	492,271.4	25.7	583,926.6	6.0
off book	108,822.3	98,811.4	10.1	81,456.9	33.6
Used CV book	6,09,462.3	5,16,148.0	18.1	5,82,744.0	4.6
New CV book	55,435.1	47,845.0	15.9	49,426.0	12.2
Used CV book share	92%	90%	1.2	92%	(0.5)
<b>Disbursement</b>	<b>1,04,790.0</b>	<b>89,970.0</b>	<b>16.5</b>	<b>95,061.9</b>	<b>10.2</b>
Used CVs	91,780.0	83,690.0	9.7	85,383.9	7.5
New CVs	13,010.0	6,280.0	107.2	9,678.0	34.4
<b>Asset quality</b>					
Gross NPA (mn)	38,702.4	18,941.4	104.3	25,357.3	52.6
Net NPA (mn)	11,437.0	3,791.2	201.7	5,022.8	127.7
Gross NPA (%)	6.25%	3.80%	2.5	4.29%	2.0
Net NPA (%)	1.85%	0.79%	1.1	0.88%	1.0
Coverage ratio (%)	70%	80%	(9.5)	80%	(9.7)
Credit Cost (%)	4.92%	2.23%	2.7	2.59%	2.3
<b>Ratios</b>					
<b>Gross Spread (on book)</b>	<b>5.70%</b>	<b>6.13%</b>	<b>(43)</b>	<b>5.76%</b>	<b>(6)</b>
<b>NIM/AUM</b>	<b>8.29%</b>	<b>7.47%</b>	<b>82</b>	<b>8.01%</b>	<b>28</b>
<b>NIM/AUM - Reported</b>	<b>7.73%</b>	<b>6.67%</b>	<b>106</b>	<b>7.47%</b>	<b>26</b>
<b>CRAR</b>	<b>17.55%</b>	<b>20.52%</b>	<b>(297)</b>	<b>18.47%</b>	<b>(92)</b>

Source: Company Data, PL Research

## STFC Q4FY16 Concall Highlights

### Business & Management Commentary:

- Economic conditions have started improving slightly but monsoon remains key. Heavy vehicle demand remains robust. Management is optimistic on government spending and improving infrastructure will improve outlook.
- **AUM growth** – HCVs & PVs continue to add to growth mainly from urban markets. Passenger vehicles and tractors also saw good growth as SHTF has been mainly financing used tractors and has been gaining market share. **Outlook** - Growth will be above 15% for FY17 with high tilt of growth in H2FY16.
- **Margins** – Margins have improved on reducing cost of funds on better cash management & reduction in base rate. MCLR regime will not help much to lower bank funding rates as 1YR MCLR rates are more than base rate, will benefit only short tenure loans.
- **Borrowings** – Have been able to do good securitization of Rs48bn during the quarter.

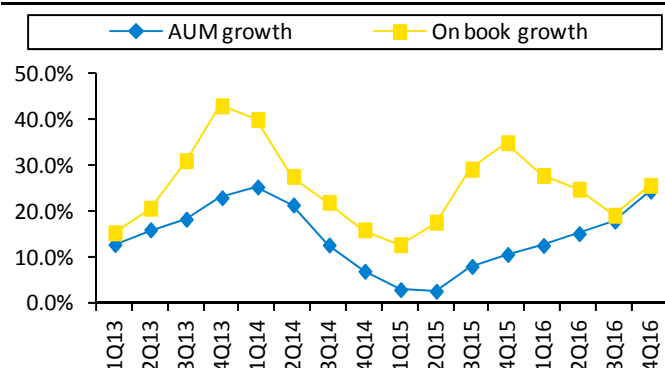
### Asset Quality:

- SHTF moved to 150dpd from 180dpd and hence GNPA's moved to 4.9% from 4.2% (70bps) in Q3FY16 and made a provision of Rs3bn for this movement to keep PCR at 70%. If SHTF would have not moved GNPA's would have been flattish.
- SHTF merged the equipment finance business which added 1.3% of loans (Rs8.94bn) to GNPA's taking overall GNPA to 6.2%.
- **Outlook** – On moving to 120/90dpd asset quality will deteriorate by 1.5% of loans on each movement. Credit cost will remain at similar levels of 200-250bps of loans in FY17.

### Subsidiaries:

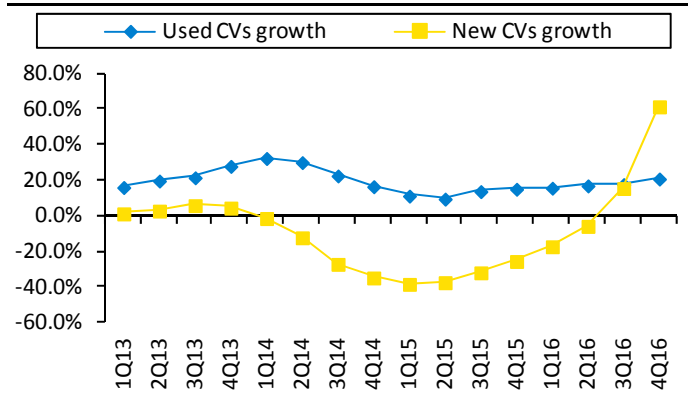
- Shriram Equipment Merger –
  - **Asset Quality** – Collections have been has 80-110crs/month based on 150dpd, while at 40-50crs/month at 150dpd. GNPA's have come down from Rs10.5bn to Rs8.94Rs on 150dpd.
  - **Equipment AUM** – Currently, AUM at Rs16bn or 2.2% of consolidated AUM, which has come off from Rs22.5bn or 3.2% of loans.

**Exhibit 2: AUM growth was led by traction in HCVs and passenger vehicles**



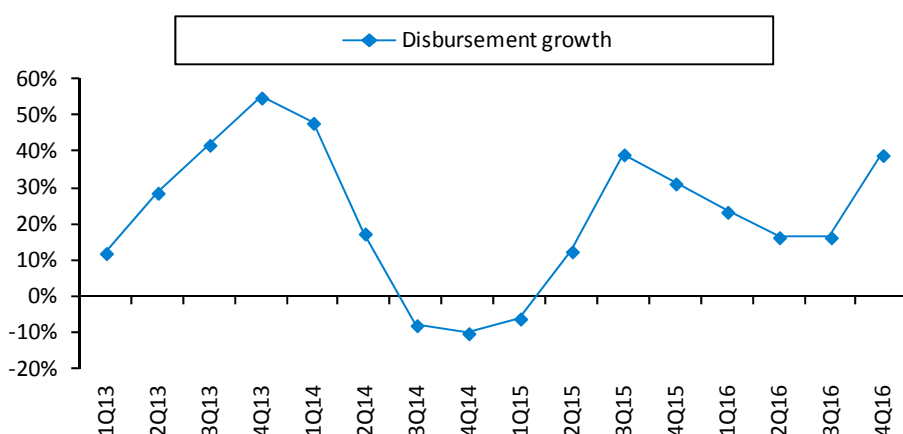
Source: Company Data, PL Research

**Exhibit 3: New CV growth remains strong**



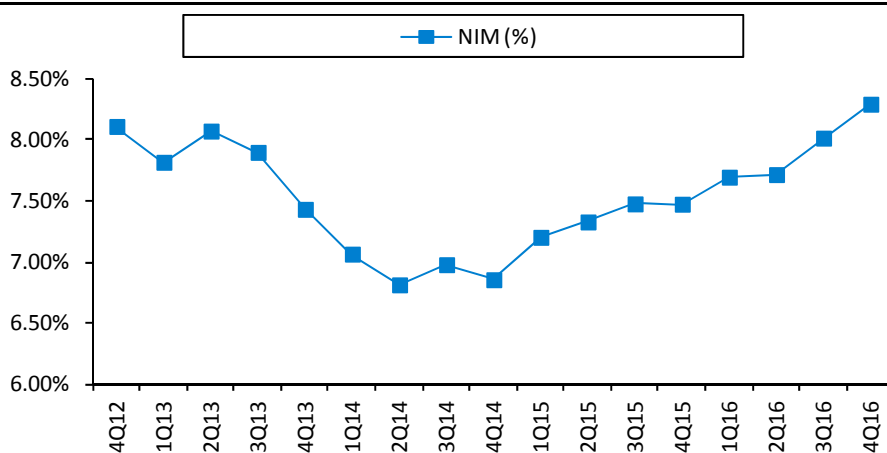
Source: Company Data, PL Research

**Exhibit 4: Strong disbursements were seen in New CVs, while used CVs grow steadily**

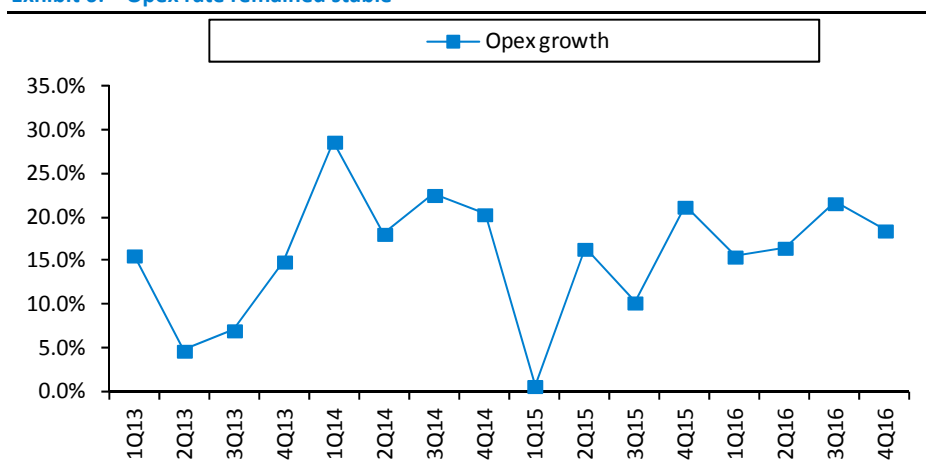


Source: Company Data, PL Research

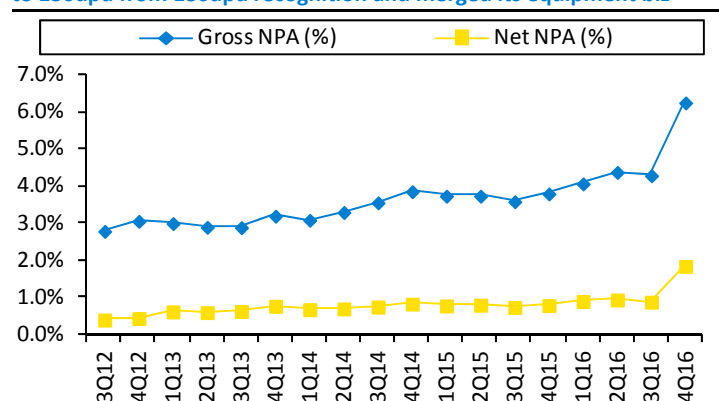
**Exhibit 5: Margins improve sharply on back of effective cash management, strong AUM growth and benefit from lower base rate**



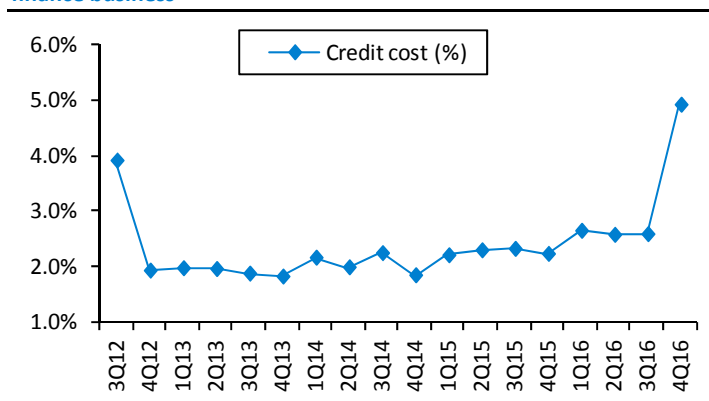
Source: Company Data, PL Research

**Exhibit 6: Opex rate remained stable**


Source: Company Data, PL Research

**Exhibit 7: Asset quality moves in-line with guidance as SHTF moved to 150dpd from 180dpd recognition and merged its equipment biz**


Source: Company Data, PL Research

**Exhibit 8: Credit cost remained high as SHTF merged equipment finance business**


Source: Company Data, PL Research

**Exhibit 9: ROE Decomposition (on Assets)**

ROA Decomposition (on Assets)	FY12	FY13	FY14	FY15	FY16E	FY17E	FY18E
Interest income	17.19	15.87	15.80	15.14	15.38	15.80	15.57
Interest expenses	7.30	7.12	8.36	8.09	7.97	7.68	7.44
<b>Net interest income</b>	<b>9.88</b>	<b>8.75</b>	<b>7.43</b>	<b>7.05</b>	<b>7.41</b>	<b>8.12</b>	<b>8.14</b>
Income from securitization	6.21	4.65	2.84	1.42	0.97	1.05	0.98
Other Inc. from operations	0.30	0.42	0.98	0.79	0.68	0.61	0.59
<b>Total income</b>	<b>10.19</b>	<b>9.16</b>	<b>8.41</b>	<b>7.84</b>	<b>8.09</b>	<b>8.73</b>	<b>8.72</b>
Employee expenses	1.10	0.95	0.87	0.79	0.93	0.91	0.88
Other operating expenses	1.23	1.10	1.21	1.28	1.13	1.16	1.13
<b>Operating profit</b>	<b>7.86</b>	<b>7.11</b>	<b>6.33</b>	<b>5.77</b>	<b>6.03</b>	<b>6.66</b>	<b>6.71</b>
Tax	1.85	1.63	1.20	1.11	0.95	1.17	1.17
Loan loss provisions	2.28	2.11	2.44	2.38	3.23	3.23	3.26
<b>Net profit</b>	<b>3.73</b>	<b>3.38</b>	<b>2.69</b>	<b>2.28</b>	<b>1.85</b>	<b>2.27</b>	<b>2.28</b>

Source: Company Data, PL Research

**Exhibit 10: Earnings estimate change table – We tweak our earnings on improving business performance and increase credit cost to factor in for 120dpd by FY17 end**

Rs mn	Old		Revised		% Change	
	FY17E	FY18E	FY17E	FY18E	FY17E	FY18E
Net Interest Income	51,433	60,956	59,999	71,257	16.7	16.9
Operating Profit	41,712	49,676	49,254	58,805	18.1	18.4
Net Profit	16,190	19,383	16,762	19,968	3.5	3.0
EPS (Rs)	71.4	85.4	73.9	88.0	3.5	3.0
ABVPS (Rs)	435.0	472.2	428.3	464.9	(1.6)	(1.6)
<b>Price Target (Rs)</b>	<b>1025</b>		<b>1025</b>		<b>-</b>	
<b>Reco</b>	<b>BUY</b>		<b>BUY</b>			

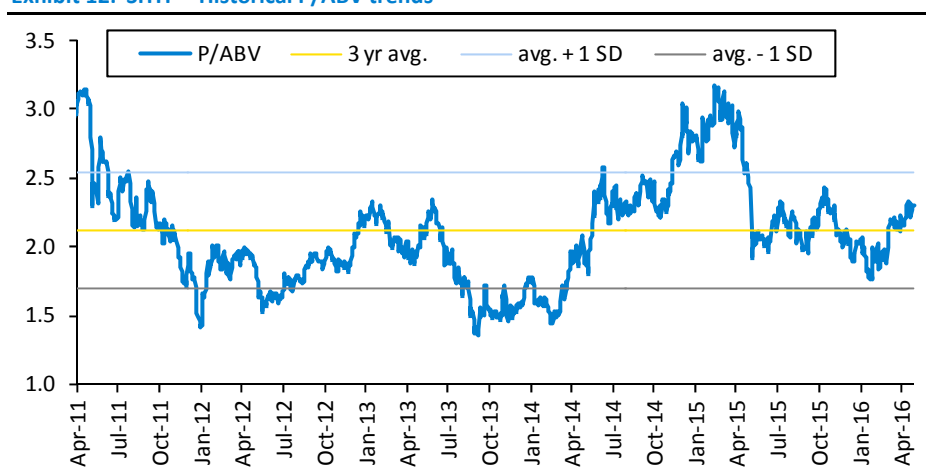
Source: Company Data, PL Research

**Exhibit 11: We retain our TP to Rs1,025 based on 2.3x Sep-17 ABV**

Fair price - EVA	1,062
Fair price - P/ABV	989
<b>Average of the two</b>	<b>1,025</b>
Target P/ABV	<b>2.3</b>
Target P/E	<b>12.7</b>
Current price, Rs	942.85
<b>Upside (%)</b>	<b>9%</b>
Dividend yield (%)	1%
<b>Total return (%)</b>	<b>10%</b>

Source: Company Data, PL Research

**Exhibit 12: SHTF – Historical P/ABV trends**



Source: Company Data, PL Research

### Income Statement (Rs m)

Y/e March	2015	2016E	2017E	2018E
Int. Inc. / Opt. Inc.	74,472	91,733	109,008	127,823
Interest Expenses	43,900	50,744	56,789	65,125
<b>Net interest income</b>	<b>30,572</b>	<b>40,989</b>	<b>52,218</b>	<b>62,698</b>
<i>Growth (%)</i>	41.6	34.1	27.4	20.1
Non interest income	4,279	4,329	4,546	5,136
<i>Growth (%)</i>	(6.9)	1.2	5.0	13.0
Net operating income	42,547	51,489	64,545	76,393
<b>Expenditure</b>				
Employees	4,296	5,891	6,716	7,723
Other expenses	6,531	6,835	8,065	9,275
Depreciation	405	363	510	590
Total expenditure	11,232	13,089	15,291	17,588
<b>PPP</b>	<b>31,315</b>	<b>38,400</b>	<b>49,254</b>	<b>58,805</b>
<i>Growth (%)</i>	5.2	22.6	28.3	19.4
Provision	12,892	20,586	23,857	28,550
Other income	—	—	—	—
Exchange Gain / (Loss)	—	—	—	—
<b>Profit before tax</b>	<b>18,424</b>	<b>17,815</b>	<b>25,397</b>	<b>30,255</b>
Tax	6,046	6,032	8,635	10,287
<i>Effective tax rate (%)</i>	32.8	33.9	34.0	34.0
<b>PAT</b>	<b>12,378</b>	<b>11,782</b>	<b>16,762</b>	<b>19,968</b>
<i>Growth (%)</i>	(2.1)	(4.8)	42.3	19.1

### Balance Sheet (Rs m)

Y/e March	2015	2016E	2017E	2018E
<b>Sources of funds</b>				
Equity	2,269	2,269	2,269	2,269
Reserves & Surplus	90,111	99,272	116,034	136,002
Networth	92,380	101,541	118,303	138,271
<i>Growth (%)</i>	11.7	9.9	16.5	16.9
Loan funds	442,758	497,806	590,176	711,000
<i>Growth (%)</i>	—	—	—	—
Others	—	—	—	—
Minority Interest	—	—	—	—
Deferred Tax Liability	—	—	—	—
<b>Total</b>	<b>535,138</b>	<b>599,347</b>	<b>708,479</b>	<b>849,272</b>
<b>Application of funds</b>				
Net fixed assets	1,007	1,011	1,066	1,119
Advances	507,638	637,701	754,267	910,668
<i>Growth (%)</i>	30.5	25.6	18.3	20.7
Net current assets	(10,275)	(56,142)	(65,151)	(82,779)
Investments	33,272	13,562	14,918	16,708
<i>Growth (%)</i>	22.1	(59.2)	10.0	12.0
Other Assets	3,496	3,216	3,379	3,556
<b>Total</b>	<b>535,138</b>	<b>599,347</b>	<b>708,479</b>	<b>849,272</b>

Source: Company Data, PL Research.

### Quarterly Financials (Rs m)

Y/e March	Q1FY16	Q2FY16	Q3FY16	Q4FY16
Int. Inc. / Operating Inc.	22,015	22,402	23,675	27,207
Income from securitization	1,464	1,595	1,567	1,705
Interest Expenses	11,972	12,059	12,239	14,474
<b>Net Interest Income</b>	<b>10,043</b>	<b>10,343</b>	<b>11,436</b>	<b>12,733</b>
<i>Growth</i>	39.3	31.4	24.5	34.3
Non interest income	148	190	193	197
<b>Net operating income</b>	<b>11,655</b>	<b>12,128</b>	<b>13,195</b>	<b>14,635</b>
<i>Growth</i>	17.6	18.5	23.6	32.9
Operating expenditure	2,905	3,001	3,287	3,896
<b>PPP</b>	<b>8,749</b>	<b>9,127</b>	<b>9,909</b>	<b>10,739</b>
<i>Growth</i>	18.3	19.1	24.3	33.9
Provision	3,959	3,984	4,199	8,567
Exchange Gain / (Loss)	—	—	—	—
Profit before tax	3,959	3,984	4,199	8,567
Tax	1,579	1,761	1,959	733
Prov. for deferred tax liability	—	—	—	—
<i>Effective tax rate (%)</i>	39.9	44.2	46.7	8.6
<b>PAT</b>	<b>3,211</b>	<b>3,382</b>	<b>3,751</b>	<b>1,439</b>
<i>Growth</i>	4.8	11.9	20.0	(54.6)

### Key Ratios

Y/e March	2015	2016E	2017E	2018E
CMP (Rs)	943	943	943	943
Eq. Shrs. O/s. (m)	227	227	227	227
Market Cap (Rs m)	213,939	213,942	213,942	213,942
Market Cap to AUM (%)	40.0	35.7	30.2	25.2
EPS (Rs)	54.6	51.9	73.9	88.0
Book Value (Rs)	407.1	447.5	521.4	609.4
Adjusted Book Value (Rs)	390.4	397.1	428.3	464.9
P/E (x)	17.3	18.2	12.8	10.7
P/BV (x)	2.3	2.1	1.8	1.5
P/ABV (x)	2.4	2.4	2.2	2.0
DPS (Rs)	8.5	10.0	11.0	12.0
Dividend Yield (%)	0.9	1.1	1.2	1.3

### Asset Quality

Y/e March	2015	2016E	2017E	2018E
Gross NPAs (Rs m)	18,941	38,702	52,799	72,853
Net NPAs (Rs m)	3,791	11,437	21,119	32,784
Gross NPAs to Gross Adv. (%)	3.7	6.1	7.0	8.0
Net NPAs to Net Adv. (%)	0.8	1.9	2.8	3.6
NPA Coverage (%)	80.0	70.4	60.0	55.0

### Profitability (%)

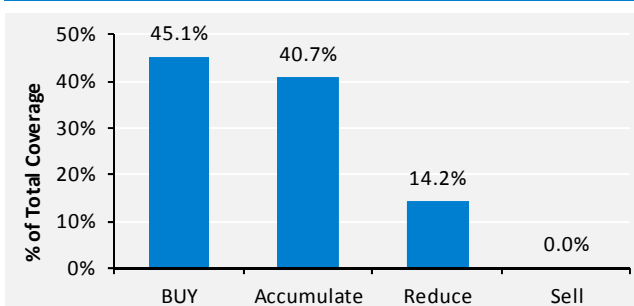
Y/e March	2015	2016E	2017E	2018E
NIM	6.3	7.2	8.0	8.0
RoAA	2.5	2.1	2.6	2.6
RoAE	14.1	12.2	15.2	15.6

Source: Company Data, PL Research.

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**Rating Distribution of Research Coverage****PL's Recommendation Nomenclature**

<b>BUY</b>	: Over 15% Outperformance to Sensex over 12-months
<b>Accumulate</b>	: Outperformance to Sensex over 12-months
<b>Reduce</b>	: Underperformance to Sensex over 12-months
<b>Sell</b>	: Over 15% underperformance to Sensex over 12-months
<b>Trading Buy</b>	: Over 10% absolute upside in 1-month
<b>Trading Sell</b>	: Over 10% absolute decline in 1-month
<b>Not Rated (NR)</b>	: No specific call on the stock
<b>Under Review (UR)</b>	: Rating likely to change shortly

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