HDFC securities
Click. Invest. Grow.
20 YEARS

Cross-Sector Series

VEHICLE FINANCING

Cross-Sector Series: Vehicle Financing

BFSI


Deepak Shinde


Krishnan ASV


Neelam Bhatia


Sahej Mittal

AUTOS


Aniket Mhatre


Sonaal Sharma

With green shoots in the underlying PV and CV segments, the Indian vehicle financing disbursals (FY22: ~US$ 42bn) is poised to ride a secular 15%+ CAGR over the next 4 years. New PV financing (US$ 20bn; +17% CAGR) is benefitting from rising premiumisation; yet remains thin on profitability due to elevated competitive intensity, especially in salaried class. Used car financing (US$ 4bn; +32% CAGR) is emerging as a sunrise sector, offering potential for high growth as well as high profitability (>2% ROA), benefitting from rising formalisation and increasing finance penetration. New CV financing is poised for a strong cyclical rebound, led by sustained recovery in fundamentals while the used CV financing market remains NBFC-dominated, translating into superior pricing power. We initiate coverage on SUF with BUY; we reiterate M&M among auto OEMs and CIFC among NBFCs as our top picks.

Vehicle Financing

Secular opportunity meets cyclical tailwinds

With green shoots in the underlying PV and CV segments, the Indian vehicle financing disbursals (FY22: ~US$ 42bn) is poised to ride a secular 15%+ CAGR over the next 4 years. New PV financing (US$ 20bn; +17% CAGR) is benefitting from rising premiumisation; yet remains thin on profitability due to elevated competitive intensity, especially in salaried class. Used car financing (US$ 4bn; +32% CAGR) is emerging as a sunrise sector, offering potential for high growth as well as high profitability (>2% ROA), benefitting from rising formalisation and increasing finance penetration. New CV financing is poised for a strong cyclical rebound, led by sustained recovery in fundamentals while the used CV financing market remains NBFC-dominated, translating into superior pricing power. We initiate coverage on SUF with BUY; we reiterate M&M among auto OEMs and CIFC among NBFCs as our top picks.

- **New PV financing - loss leader (AUM of US$ 64bn)**: New PV financing offers healthy growth (+17% CAGR) - however, the heightened competitive intensity continues to drive marginal spreads lower, resulting in loss leader pricing and dilutive unit economics for most lenders.
- **Used car financing - emerging sweet spot (AUM of US$ 8bn):** Riding on the back of increasing formalisation, rising finance penetration, and changing customer preference for used cars (1.3x-1.4x new car volumes), the used vehicle financing segment offers a combination of high growth (+32% CAGR) and high profitability.
- **CV financing - riding the cyclical recovery (AUM of US$ 53bn):** CV financing is poised to ride a strong cyclical rebound (~+15% CAGR) driven by multiple underlying catalysts. With the stress pool easing materially due to better utilisation and rising freight rates, the new CV financing segment is relatively heterogeneous with banks dominating the M&HCV segment and NBFCs leading other segments.
- **Used CV market remains buoyant; NBFCs best-placed:** Used CV financing is expected to witness fillip on the back of improving economic activity and utilisation levels. While new CV financing remains highly competitive from banks, used CV financing is likely to remain a stronghold for NBFCs with superior pricing power and customer stickiness.
- **OEMs poised for strong cyclical recovery:** We expect auto demand (across segments) to revive on a low base, led by a pick-up in economic growth and expected rural revival (17/16/18% volume CAGR for 2Ws/PVs/CVs over FY22-24E). We also expect strong recovery in earnings for all OEMs on the back of softening commodity prices and a gradual easing of supply constraints. Our top picks are TVS Motors (BUY: sustained outperformance), Hero Motocorp (BUY: volume revival + attractive valuation) and M&M (BUY: mojo back in UVs + value unlocking driving re-rating).
- **Initiate on Sundaram Finance (SUF) with BUY; CIFC remains top pick**: We initiate coverage on SUF with BUY (SoTP-based TP of INR 2,360). Our stance on SUF is anchored on the virtuous cycle that encompasses best-in-class funding costs, superior borrower profile and pristine asset quality. CIFC remains our top pick (BUY; TP: INR790) as the franchise is poised for strong growth with CV up-cycle and new growth avenues, along with superior RoE (~20%). We drop coverage on Indostar Capital Finance (previous rating: REDUCE) as the prospects of a turnaround of the franchise appear to be increasingly diminishing.

NBFCs

Company	Mcap (INR bn)	CMP (INR)	Reco.	TP (INR)
CIFC	563	685	BUY	790
SUF	221	1,989	BUY	2,360
SHTF	405	1,497	ADD	1,554
MMFS	257	208	ADD	215

Auto OEMs

Company	Mcap (INR bn)	CMP (INR)	Reco.	TP (INR)
MM	1,362	1,135	BUY	1,390
TVSL	414	871	BUY	988
HMCL	567	2,838	BUY	3,268
MSIL	2,601	8,613	ADD	8,957
EIM	843	3,083	ADD	3,118
BJAUT	1,163	4,017	REDUCE	3,677
TTMT	1,721	450	REDUCE	398
AL	432	147	SELL	102

BFSI
Deepak Shinde
deepak.shinde@hdfcsec.com
+91-22-6171-7323

Krishnan ASV
venkata.krishnan@hdfcsec.com
+91-22-6171-7314

Neelam Bhatia
neelam.bhatia@hdfcsec.com
+91-22-6171-7341

Sahej Mittal
sahej.mittal@hdfcsec.com
+91-22-6171-7325

AUTOS
Aniket Mhatre
aniket.mhatre@hdfcsec.com
+91-22-6171-7357

Sonaal Sharma
sonaal.sharma@hdfcsec.com
+91-22-6171-7308

Focus charts

Exhibit 1: New/Used cars financing market to grow at 17%/32% CAGR during FY22-FY26P

	Units	FY22E	FY26P	CAGR %
New car sales	mn	3.1	4.6	11%
Avg ticket size (loan)	INR mn	0.6	0.8	5%
Market size	**INR trn**	**1.5**	**2.8**	**17%**
Used car sales	mn	4.2	6.6	12%
Finance penetration	%	21%	34%	
Avg ticket size (loan)	INR mn	0.4	0.4	5%
Market size	**INR trn**	**0.3**	**1.0**	**32%**

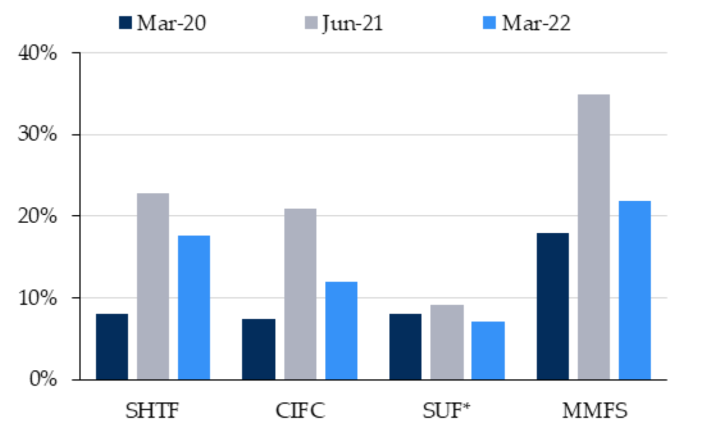
Source: SIAM, Industry, HSIE Research | *Market size in terms of disbursals*

Exhibit 2: Used cars financing more lucrative vs. new cars financing for Banks

(% of Advances)	New cars	Used cars
Interest Income	7.5%	11.5%
Interest Expenses	4.0%	4.0%
Net interest income	3.5%	7.5%
Fee income	0.3%	0.8%
Total Income	3.8%	8.3%
Operating expenses	1.4%	2.9%
PPOP	2.4%	5.4%
Provisions	0.7%	1.5%
Profit before Tax	1.7%	3.9%
PAT	1.3%	2.9%

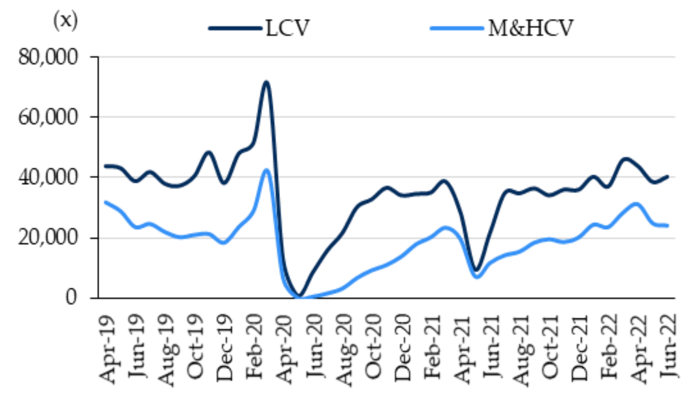
Note: Industry, Company, HSIE Research | *Assuming yield on advances, cost of funds similar to leading private banks*

Exhibit 3: CV financiers – reducing stress pool (GS-II + GS-III)



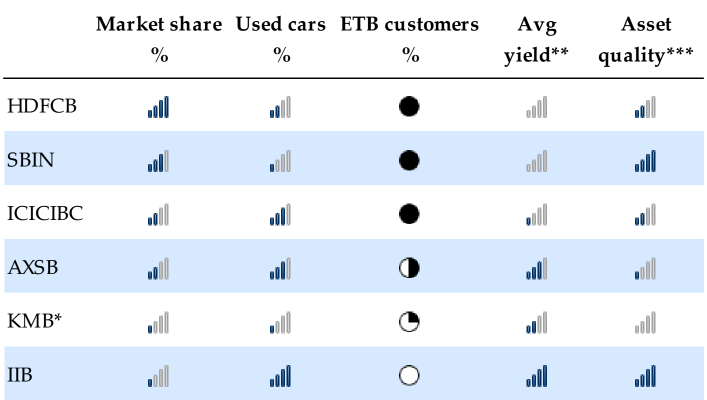
Source: Company, HSIE Research | *Note: *Restructured assets considered as GS-II for Jun-21*

Exhibit 4: CV sales witnessing pick up with replacement demand, capacity additions



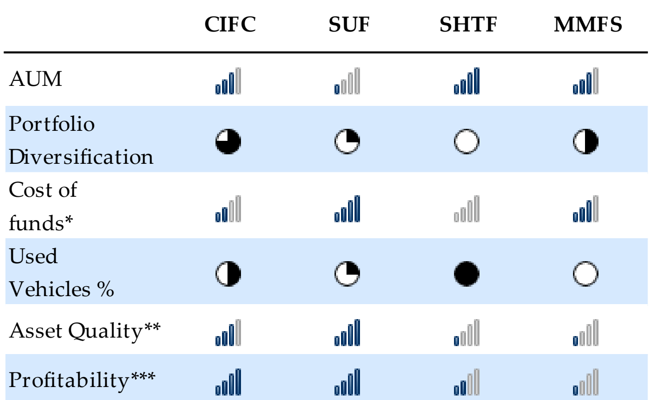
Source: FADA, HSIE Research

Exhibit 5: Banks dashboard (PVs)



Source: CRIF Highmark, Industry, Company, HSIE Research *Note: HDFC Securities is a subsidiary of HDFC Bank | On each parameter, a fuller bar indicates a superior franchise | * Kotak Mahindra Prime; ** Average yield based on mean interest rates for loans disbursed during Q4FY22; *** GNPA as on Mar-22 for vehicle loans portfolio, GNPA for ICICIBC and AXSB assumed similar to that of their retail portfolio*

Exhibit 6: Vehicle financing NBFCs dashboard (CVs)



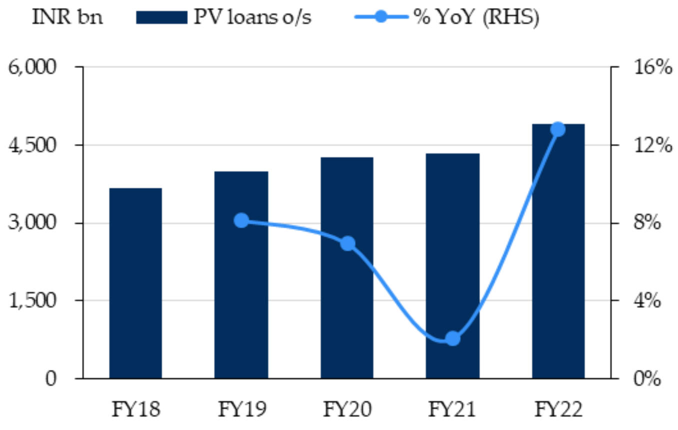
Source: Company, HSIE Research | *Note: On each parameter, a fuller bar indicates a superior franchise; AUM, portfolio diversification and used vehicles mix as on Mar-22; *Average cost of funds during FY13-FY22; **Average credit costs during FY13-FY22; *** Average RoE during FY13-FY22*

Contents

Passenger Vehicle (PV) Financing - at a new crossroad

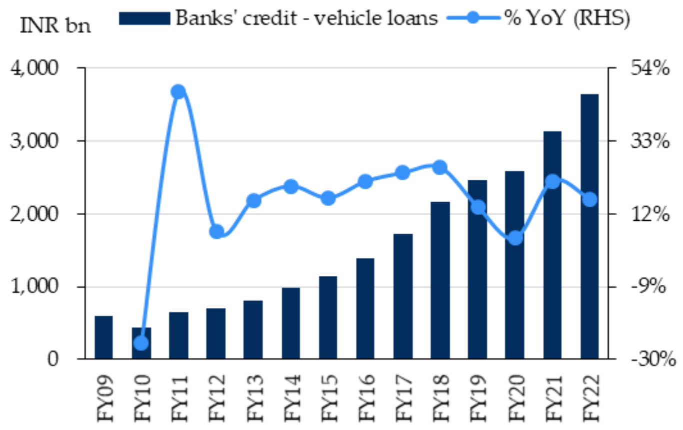
Driven by a combination of strong underlying demand, rising premiumisation, and improving finance penetration in the used/preowned vehicles segment, the passenger vehicle (PV) financing opportunity in India is poised to grow at ~20% CAGR to US$ 50 billion in terms of annual disbursements during FY22-FY26E.

Exhibit 7: Industry PV loans outstanding at ~INR 5trn



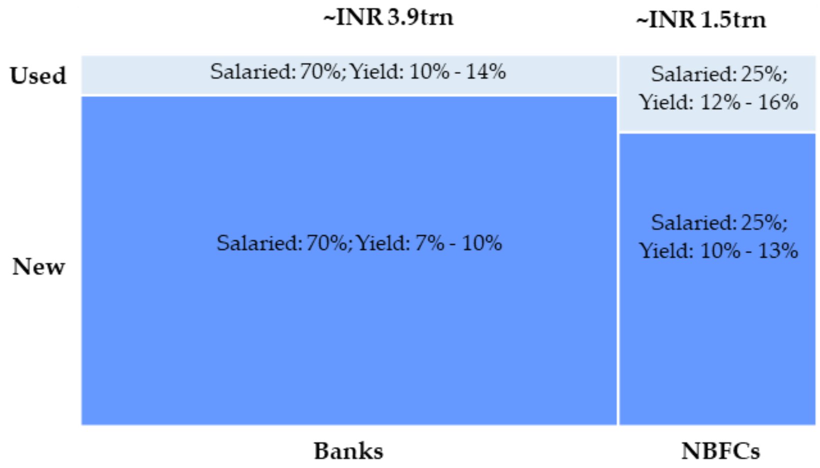
Source: CRIF HighMark, HSIE Research

Exhibit 8: Banks' credit - retail vehicle loans



Source: RBI, HSIE Research

Exhibit 9: PV financing landscape (Mar-22)



Source: CRIF HighMark, Industry, HSIE Research | Note: *Share of salaried customers and Yields on loans are indicative*

- **Underpenetrated market offers long runway for volume growth:** With a registered PV population of ~40mn, our analysis (Exhibit 10) suggests that ~40% of mid-income and above households in India own a passenger vehicle, compared to average PV ownership of 1.2-2x per household (all income households) in other economies. Given such massive under-penetration, we expect PV volumes to grow at a healthy pace in the medium term.

Exhibit 10: PV penetration per household estimated at ~40%

Indian PV market	
No. of registered LMVs (mn)*	39
Indian Population (mn)	1,380
Indian Households (mn)	289
# Households with annual income > 0.5mn per annum (mn)	95.0
Cars per household (x)	**0.4**

Source: VAAHAN, SIAM, BCG Report, Company, HSIE Research | *Note: * No. of registered LMVs taken as cumulative sum of PV sales for last 15 years*

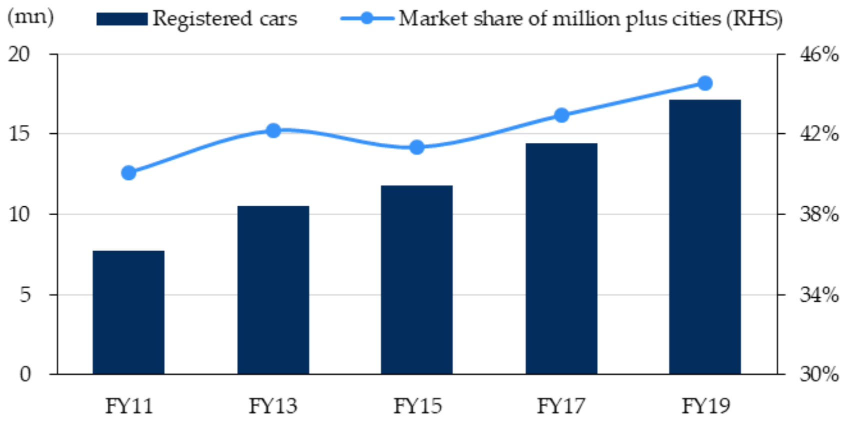
Exhibit 11: New-car financing market poised to grow at ~17% CAGR during FY22-FY26P

	Units	FY22E	FY26P	CAGR %
New car sales	mn	3.1	4.6	11%
Avg. selling price	INR mn	0.8	0.9	5%
Finance penetration	%	79%	80%	
LTV	%	82%	83%	
Market size (disbursal)	**INR trn**	1.5	2.8	17%

Source: SIAM, CRIF HighMark, Industry, HSIE Research

- **PV penetration skewed towards urban centres:** As of FY19, India was home to 51 "million plus cities (MPCs)". These centres, which together constituted ~13% of India's population, accounted for ~45% of the PV population (and rising every year), indicating significant under-penetration in the semi-urban/rural centres.

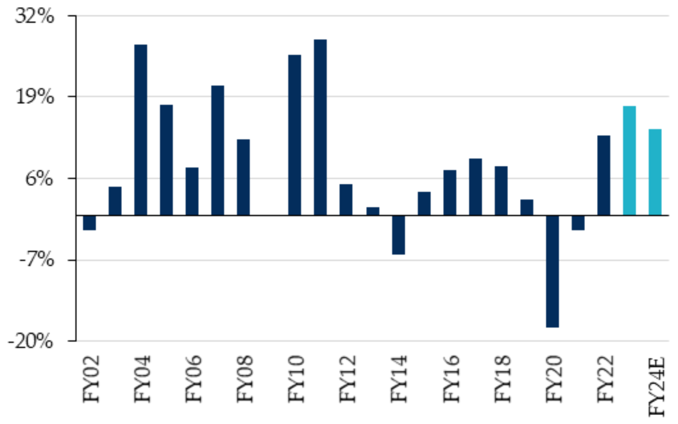
Exhibit 12: Contribution of "million plus cities" in registered PVs at >40%



Source: MoRTH, HSIE Research | *Note: No. of "million plus cities" in FY11, FY13, FY15, FY17 and FY19 at 35, 42, 48, 42 and 51 respectively*

- **Longer waiting periods to translate into strong volume growth catalysts**: Our auto sector analysts, Aniket and Sonaal, expect PV sales volumes to deliver ~16% CAGR during FY22-FY24E. Supply side constraints have resulted in record high waiting period across all major OEMs (**Exhibit 14**). Our discussions with stakeholders across the ecosystem suggest that supply side issues are gradually getting addressed.

Exhibit 13: PV sales volumes growth – poised for strong recovery



Source: SIAM, HSIE Research | *Note: Domestic sales volumes*

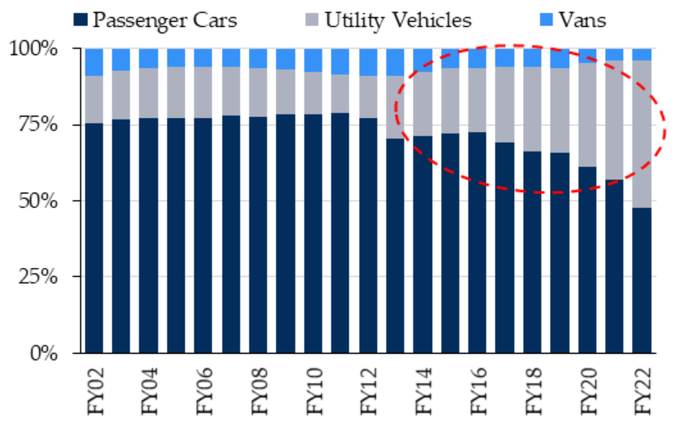
Exhibit 14: Waiting period for various models of OEMs

Company/Model	Waiting Period
Maruti Suzuki New Brezza	8-38 weeks
Maruti Suzuki New Baleno	6-8 weeks
Maruti Suzuki Ertiga (Petrol/CNG)	Up to 7 - 9 months
Mahindra XUV700	Up to 22 months
Mahindra Thar	Up to 12 months
Hyundai Venue	Up to 4 months
Hyundai Creta	Up to 7 months
Tata Nexon/ Nexon EV	Up to 4 - 5 months

Source: Company, HSIE Research

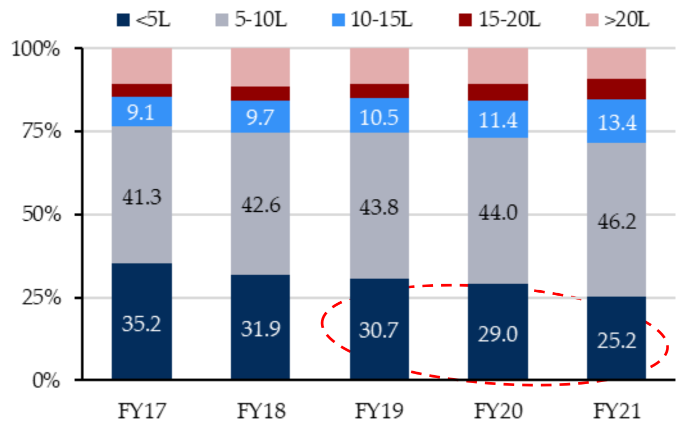
- **Premiumisation, regulatory norms drive higher average ticket size:** Driven by rising disposable incomes and changing consumer preferences, India's PV demand has been gradually shifting towards UVs, contributing to ~50% of total PV volumes. High compliance costs (stringent regulations such as transition to BS-VI, increase in number of compulsory airbags, and higher insurance premium for TP) are driving the cost curve higher, translating into higher ticket-sized vehicles and proportionally higher ticket size of auto loans (average ticket size of PV loans up by ~6% CAGR in the past three years).

Exhibit 15: PV sales mix - shifting towards UVs…



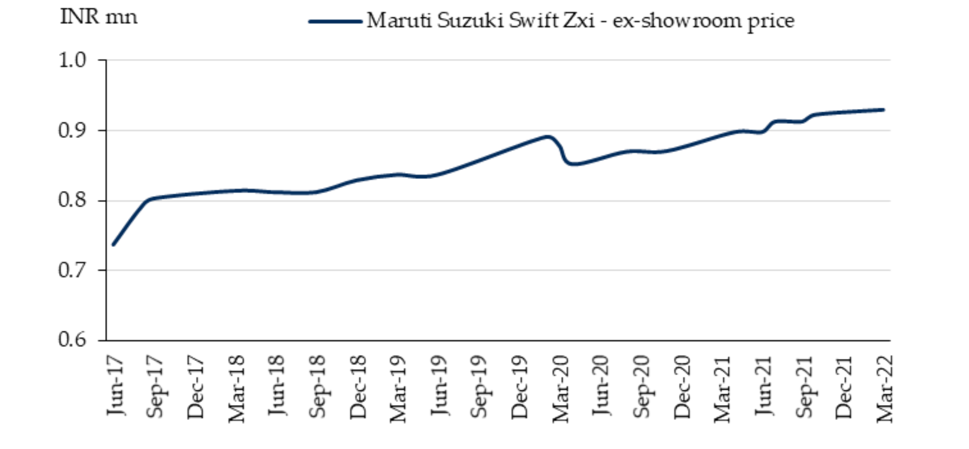
Source: SIAM, HSIE Research

Exhibit 16: …driving higher ticket-sized auto loans (average ticket size of originations – auto loans)



Source: CRIF Highmark, HSIE Research

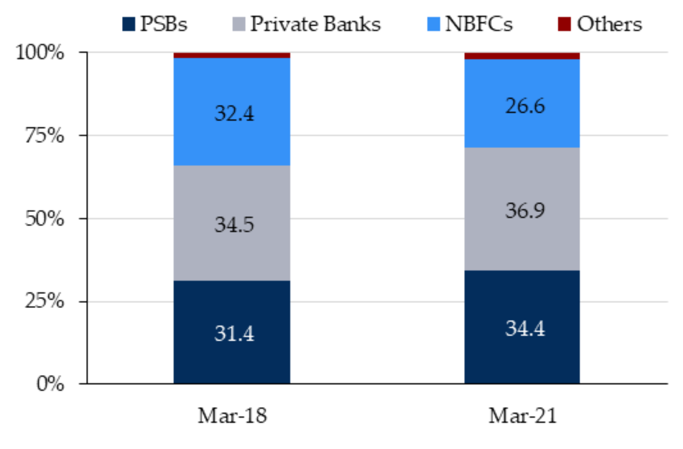
Exhibit 17: Maruti Suzuki Swift Zxi price has increased at ~6% CAGR since Jun-17 (ex of insurance, registration charges etc.)



Source: Company, HSIE Research

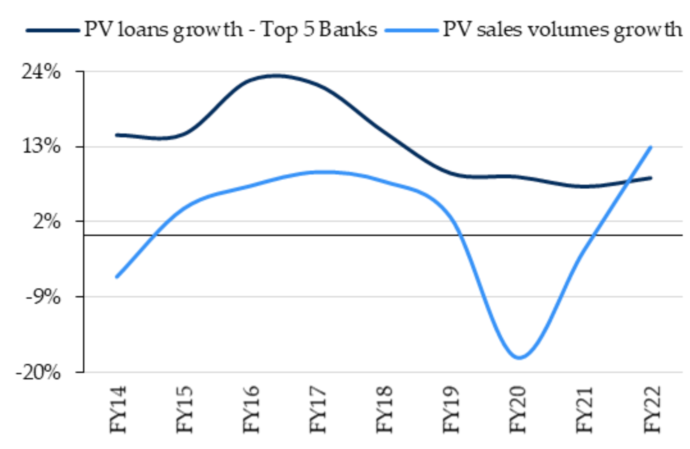
- **Market share consolidation amid rising competitive intensity:** The competitive intensity in PV financing has increased significantly, with leading private banks investing in digital initiatives to service NTB customers as well as pre-approved ETB customers with real-time disbursals. PSBs have also been growing their auto loans portfolio at a furious pace, albeit on a low base. The market microstructure is moving towards market share consolidation, which is already reflecting in the exit of captive financiers (Ford and Volkswagen) that constitute the long tail. We believe that the increasingly marginal role of NBFCs in this space reflects the underlying customer profile and the sub-par economics of the segment.

Exhibit 18: Banks have gained healthy market share during the past three years



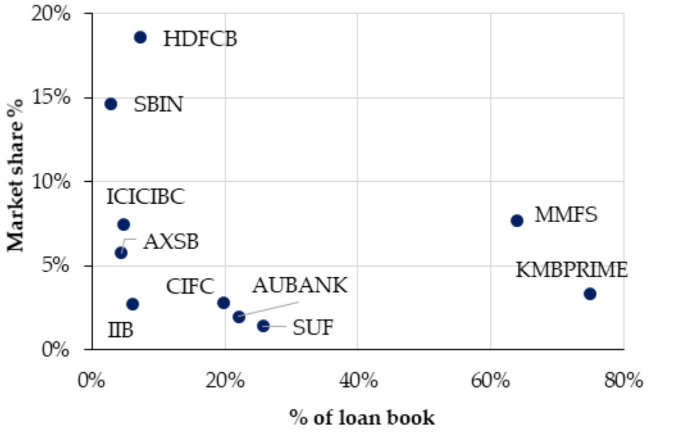
Source: CRIF Highmark, HSIE Research

Exhibit 19: Loan growth has come off with declining PV sales volumes



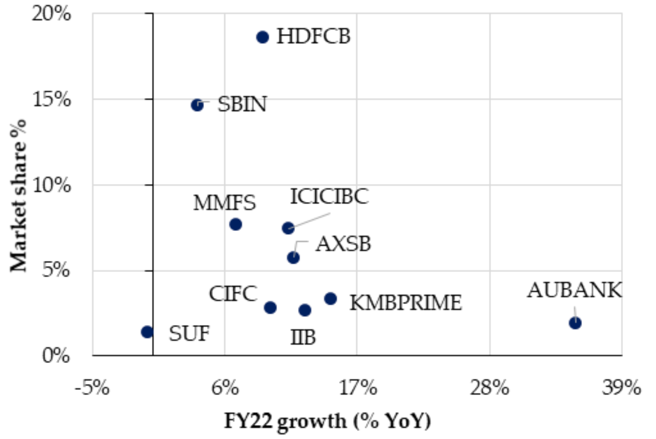
Source: RBI, Company, HSIE Research

Exhibit 20: PV loans share in loan book vs. market share in PV loans (Mar-22)



Source: CRIF Highmark, Company, HSIE Research | *Note: HDFC Securities is a subsidiary of HDFC Bank*

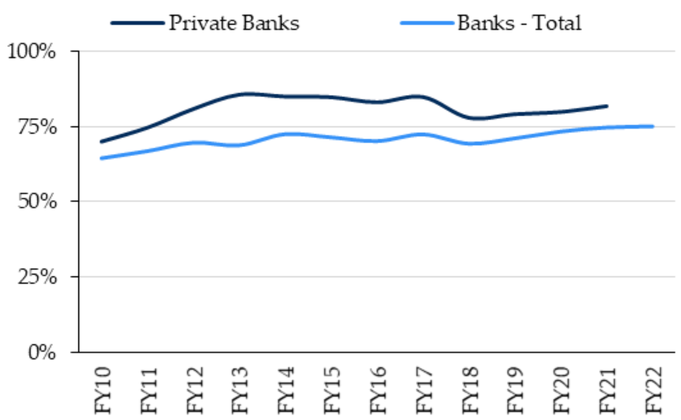
Exhibit 21: Market share vs. PV loans growth (Mar-22)



Source: CRIF Highmark Company, HSIE Research | *Note: HDFC Securities is a subsidiary of HDFC Bank*

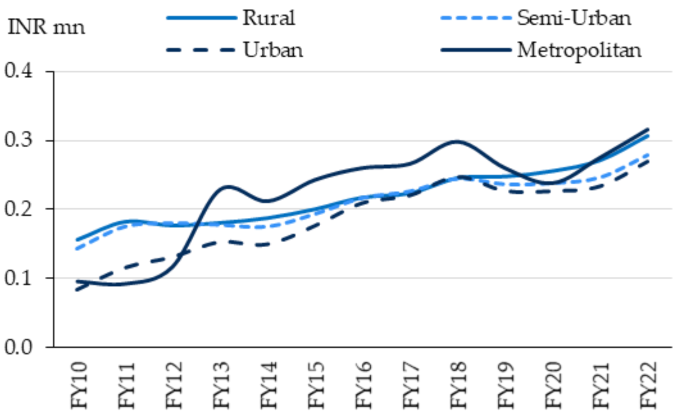
- **Highly competitive space favours banks:** Banks, especially the ones with a large captive SA base, have a dominant market share in new PV financing (~75%) as well as used PV financing (>60%). This segment remains highly competitive driving asset yields of ~7-9%, especially for new PVs. Given the combination of the geographical mix (largely urban centres), customer profile (predominantly salaried), and the consequent sub-par economics, NBFCs play a relatively more active role in used PV financing, with average portfolio yields at a little over 12%.
- **Highly skewed towards urban and metros:** Banks' auto loans portfolio remains skewed towards metros and urban centres contributing to ~3/4th of the vehicle loans outstanding (~45% contribution in PV sales from the top 51 "million plus cities"). While select banks are gradually seeking market share gains in semi-urban/rural segments, they are likely to face stiff competition from NBFCs with their well-established network and customer penetration.

Exhibit 22: Banks' Auto loan book – skewed towards metro & urban centres (% of Auto loans)



Source: RBI, HSIE Research

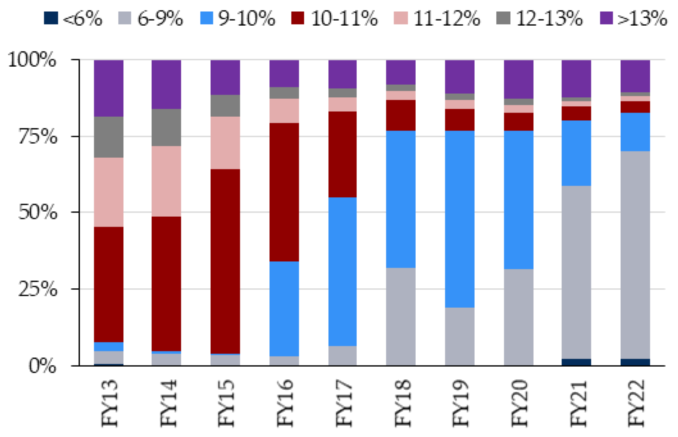
Exhibit 23: Average Auto loans outstanding per borrower – region agnostic



Source: RBI, HSIE Research

- **Sub-optimal returns in new PV financing:** High competitive intensity has driven yields for new PV loans as low as 6.75-7% for banks on incremental loans disbursed in H2FY22, thereby driving diminishing returns at a product level. Our analysis (Exhibit 26) suggests that incremental loans disbursed at sub-optimal yields are likely to be RoA-dilutive for leading banks, although cross-sell opportunities in the form of third-party products and liabilities up-sell offer fillip to customer-level profitability and also helps in completing the product bouquet for customers. Despite such fierce competition, our discussion with bureaus suggests that asset quality trends have remained fairly steady, reflecting the quality of the underlying customer profile.

Exhibit 24: Banks – ~70% of Auto loan book yielding sub-9%



Source: RBI, HSIE Research

Exhibit 25: Yields on new car loans disbursed in Q4FY22

	Min	Max	Mean
AXSB*	6.65%	17.75%	9.99%
HDFCB	6.70%	10.00%	7.31%
ICICIBC	6.75%	13.50%	7.65%
SBIN	NA	NA	8.25%

Source: Company, HSIE Research | ** Includes used car loans as well | Note: HDFC Securities is a subsidiary of HDFC Bank | Zero processing fees for SBIN*

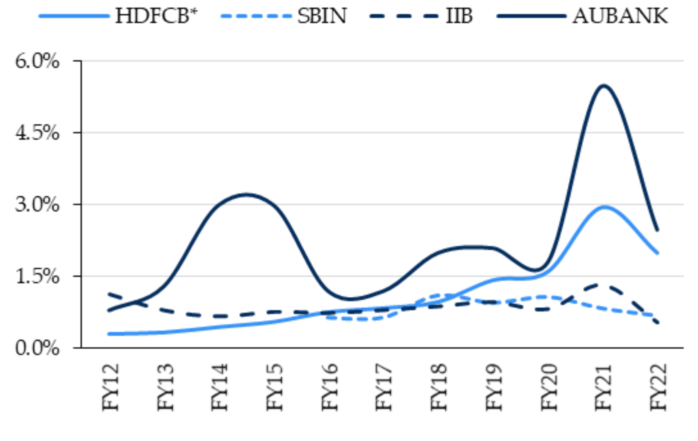
Exhibit 26: NBFCs' RoAs more accretive vs. banks in new car financing

(% of advances)	Bank	NBFC	Comments
Interest Income	7.5%	12.0%	NBFCs cater largely to high yielding customer segment (self-employed)
Interest Expenses	4.0%	7.0%	Cost of funds advantage for leading Banks
Net interest income	**3.5%**	**5.0%**	
Fee income	0.4%	0.4%	
Total Income	3.9%	5.4%	
Operating expenses	1.4%	1.3%	
Pre-provisioning profit	2.5%	4.1%	
Total Provisions	0.7%	1.3%	Delinquencies for NBFCs significantly higher compared to Banks due to different customer profile
Profit before Tax	1.8%	2.8%	
Provision for Taxation	0.5%	0.7%	
PAT	**1.3%**	**2.1%**	NBFCs portfolio more profitable at RoA level

Source: Industry, Company, HSIE Research

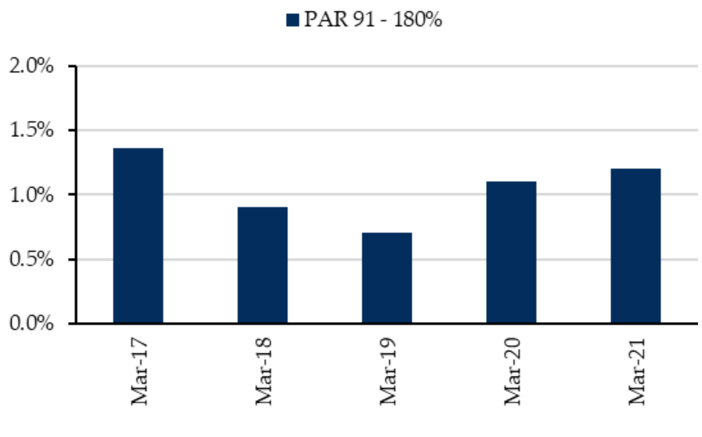
1. Assumed accounting for Banks and NBFCs under GAAP for like-to-like comparison
2. Loan of ticket size of INR 0.5 mn with a tenure of 4 years; Processing fees and origination costs amortised over the tenure of the loan
3. Cost of funds assumed similar to that of leading banks and NBFCs
4. Impact of SLR and CRR requirements not considered in case of Banks

Exhibit 27: GNPA ratio of select banks for auto loans portfolio



Source: Company, HSIE Research | * For Consolidated auto loans portfolio;| Note: HDFC Securities is a subsidiary of HDFC Bank

Exhibit 28: PAR 91 -180 bucket has been declining for the industry (PV loans)



Source: CRIF HighMark, HSIE Research

Exhibit 29: RoA profile of Kotak Mahindra Prime (Vehicle loans at ~75% of AUM)

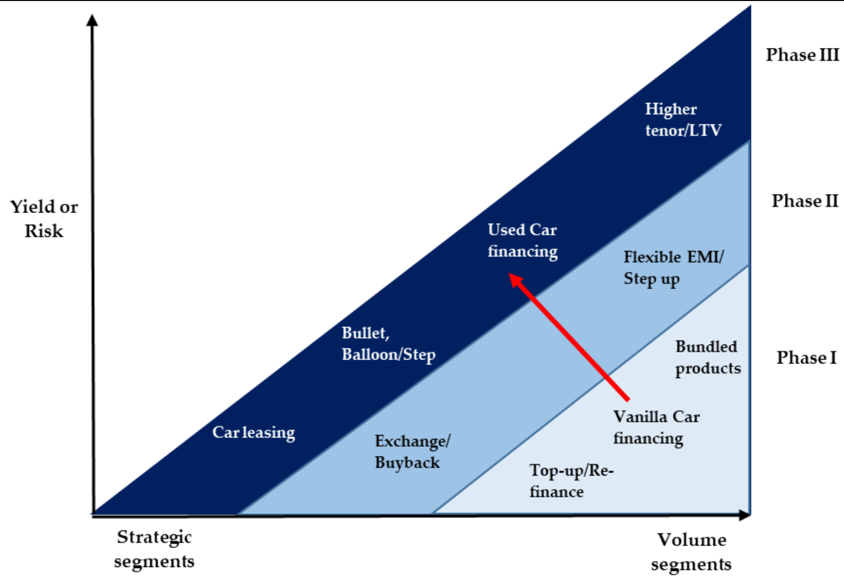
DuPont (% of avg assets)	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Interest Income	11.4%	10.6%	10.2%	9.7%	9.7%	8.5%	8.5%
Interest Expenses	7.1%	6.6%	6.3%	6.1%	5.8%	4.4%	3.5%
Net interest income	4.3%	4.0%	3.9%	3.7%	3.9%	4.2%	5.0%
Total Non-Interest Income	1.0%	0.9%	0.9%	0.5%	0.6%	0.6%	0.7%
Total Income	**5.3%**	**4.9%**	**4.8%**	**4.2%**	**4.5%**	**4.7%**	**5.7%**
Total Operating Expenses	1.5%	1.4%	1.4%	0.9%	1.0%	1.2%	1.5%
PPP	**3.8%**	**3.4%**	**3.4%**	**3.2%**	**3.5%**	**3.5%**	**4.2%**
Total Provisions	0.3%	0.4%	0.3%	0.4%	0.9%	1.1%	-0.4%
Profit before Tax	3.5%	3.1%	3.1%	2.9%	2.6%	2.5%	4.6%
Provision for Taxation	2.3%	2.0%	2.1%	1.9%	1.9%	1.8%	1.1%
RoA	**2.3%**	**2.0%**	**2.1%**	**1.9%**	**1.9%**	**1.8%**	**3.4%**
Avg Assets/Avg Net worth	6.2	6.3	6.4	5.5	4.4	3.7	3.3
RoE	**14%**	**13%**	**13%**	**10%**	**8%**	**7%**	**11%**

Source: Company, HSIE Research | Note: IND AS accounting from FY19 and hence not directly comparable to prior years as well as Exhibit 26

- **Current dealer economics favourable; future imperfect:** With minimal inventory levels (low working capital), high waiting periods for new vehicle sales (Exhibit 14), and low discounts, new PV dealers are currently in a very sweet spot in terms of profitability. However, increasing digitisation of new PV financing by major OEMs (the Maruti Suzuki Smart Finance Program contributes to ~15% of Maruti's financing volumes) and leading lenders (preapproved offers by SBI YONO, HDFC Bank Xpress Digital and ICICI Bank Insta Car loans) are likely to shift the decision of choice of financing partner away from dealers, denting dealer margins.

- **Beyond plain-vanilla new PV financing:** While new PV financing remains fiercely competitive, there are several opportunities for auto financiers to move up the yield curve with product diversification. As demonstrated in Exhibit 30, our discussions with mobility experts suggests that auto financiers can gradually migrate towards higher value-add, higher-yielding products such as exchange/buyback programs (particularly for captive financiers), car leasing (for corporates) and used car financing.

Exhibit 30: PV financiers - need for further cross-sell beyond plain-vanilla financing



Source: E&Y report, HSIE Research

Pre-owned/used car financing – emerging sunrise sector

The used car financing business, currently with annual disbursements of ~INR 0.3trn, is poised for ~32% CAGR to INR 1trn by FY26. The growth is likely to be driven by improving financing penetration, higher LTV and increase in ticket size with entry of SUVs in the used cars market. Rising competitive intensity in new PV financing, an improving ecosystem for used PV financing, and changing customer preferences are driving used PV financing as the next big opportunity for lenders to tap into.

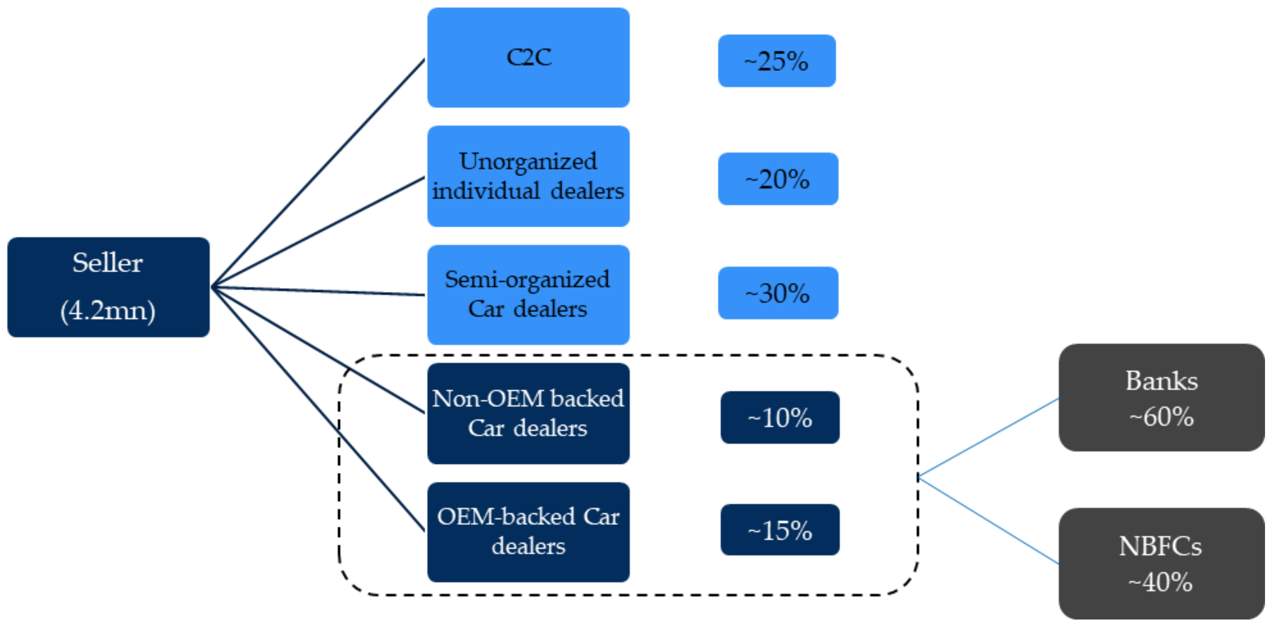
Exhibit 31: Used PV financing market poised to grow at ~32% CAGR to ~INR 1trn by FY26

	Units	FY22E	FY26P	CAGR %
Annual Used Car Sales	mn	4.2	6.6	12%
Average selling price	INR mn	0.55	0.64	4%
Finance penetration	%	21%	34%	
LTV	%	65%	67%	
Avg ticket size - loan	INR mn	0.4	0.4	5%
Market size	**INR trn**	**0.3**	**1.0**	**32%**

Source: SIAM, Industry, HSIE Research

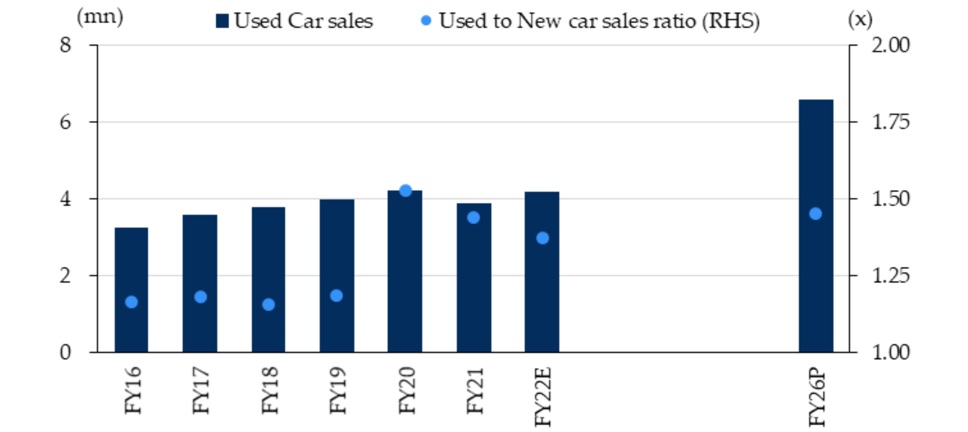
Banks typically finance used PVs largely through the organised segment, while select NBFCs finance used PVs in the unorganised segment as well. Basis our interaction with industry experts, HDFC Bank is the market leader in the used PV financing segment, followed by Mahindra Finance and ICICI Bank, with a negligible market share for PSBs.

Exhibit 32: Used cars dealer landscape



Source: Praxis Global Alliance Report March 2022, Industry, HSIE Research

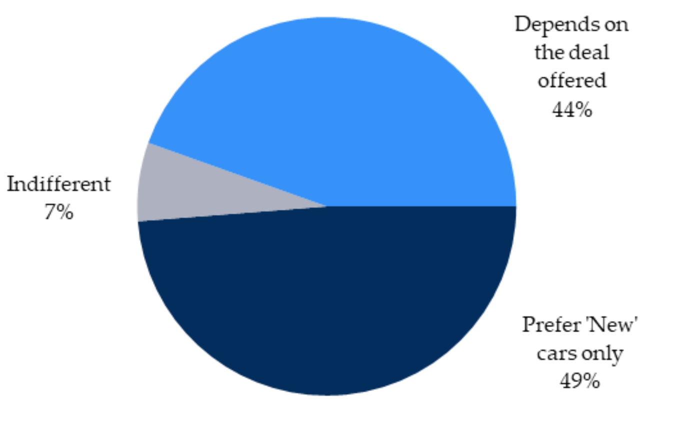
Exhibit 33: Used PV sales volumes at ~1.3-1.4x new PV sales volumes



Source: CRIF Highmark, SIAM, HSIE Research

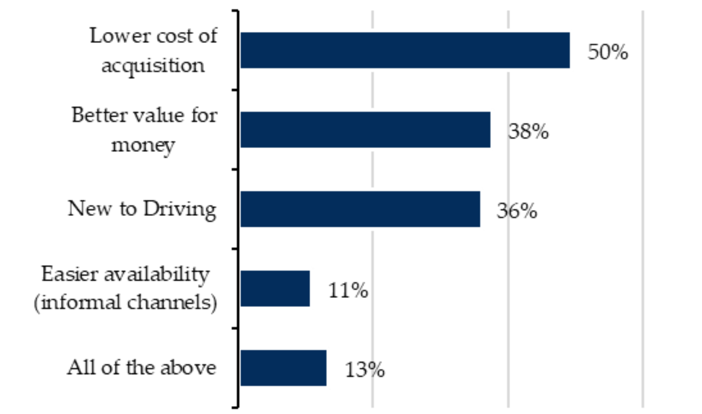
- **Demand for used cars on an upward trajectory:** Volumes in used PVs have been steadily increasing, led by customer preference of owning a car, rapidly escalating cost of ownership of new PVs and an improving used car sales ecosystem. Our proprietary survey with >200 respondents on pre-owned cars financing indicates a high customer inclination towards used cars for several reasons such as value for money, low cost, etc.

Exhibit 34: ~50% of respondents were open to purchase a used car



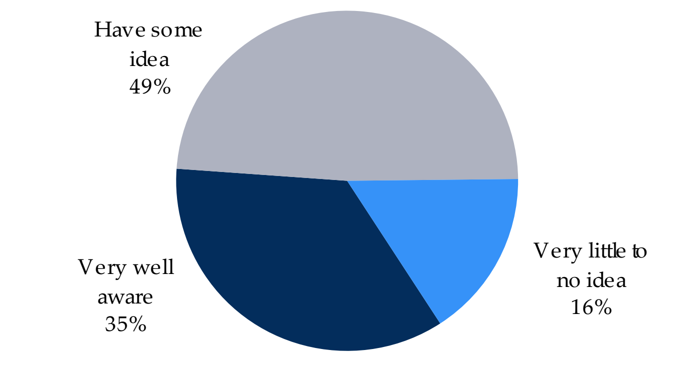
Source: HSIE Proprietary Survey

Exhibit 35: Multiple reasons to opt for a used car among respondents



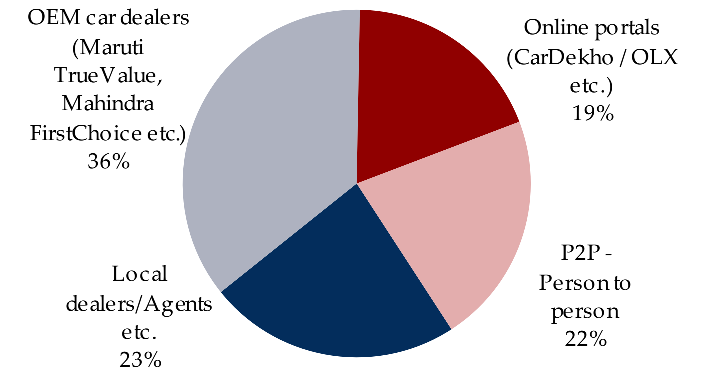
Source: HSIE Proprietary Survey

Exhibit 36: ~84% of the respondents had 'some' to 'very good' awareness of online auto portals



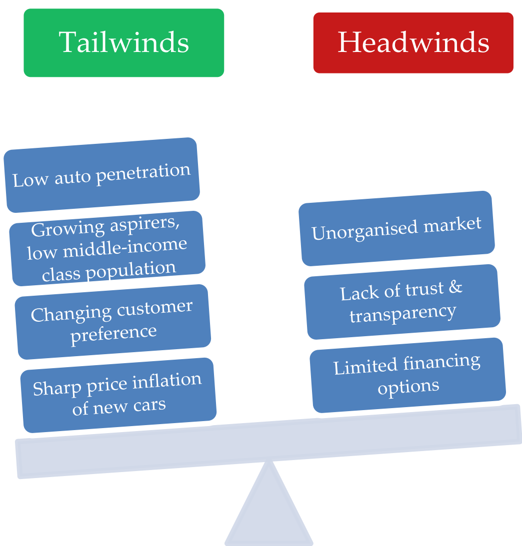
Source: HSIE Proprietary Survey

Exhibit 37: ~55% of respondents prefered to purchase a car from organised used car dealers



Source: HSIE Proprietary Survey

Exhibit 38: Enablers and barriers to used car financing



Source: HSIE Research

- **Rising formalisation to improve "bankability":** Used cars financing remains highly underpenetrated at ~20-21% as bulk of the transactions take place either through C2C (~1/4th) or through unorganised dealers/brokers. Roughly 20-25% of used car transactions take place through large organised used car dealers (Maruti TrueValue/Mahindra FirstChoice/Cars24/Spinny, non-OEM dealers, etc.) who provide additional services such as inspection checks, refurbishment, certification and warranty and, hence, drive more trust and transparency for the customers as well as lenders. The increasing share of these organised players is likely to improve the finance penetration in the used car segment.

Exhibit 39: Used car dealer landscape

	Unorganised		Organised	
	Unorganised/independent	Semi-organised	non-OEM backed	OEM-backed
Volume share %	15 - 20%	25 - 30%	5 - 10%	10 - 15%
Description	Individual brokers/commission agents without a physical outlet/showroom; uncertified cars w/o warranty	Dealers operating out of garage/mechanic shop etc.	Dealers operating out of showrooms, provide warranty, inspection checks etc.	OEM-backed, operating out of showrooms, provide warranty, inspection checks etc.
# Dealers	High	Medium to High	Low	Very Low
Cars sold per dealer per month	Low	Medium	High	High

Source: Praxis Global Alliance Report March 2022, Industry, HSIE Research

Exhibit 40: Organised used car dealers

FY21	Tech/Non-OEM backed				OEM-backed		
	CarDekho	Cars24	CarTrade (CarWale)	Spinny	Maruti TrueValue	Mahindra FirstChoice	Hyundai H Promise
Founded in	2007	2015	2009	2015	2001	2008	2009
Branches/Outlets (x)	60	205+	47	36	1143	1100	485
Cities (x)	88	182	32	22	868	350	300
Vehicles sold till date (mn)	NA	<0.1	NA	<0.05	4.3	2.0	0.2
OEM	All	All	All	All	Captive	All	Captive
Revenues - FY21 (INR bn)	8.8	27.5	2.5	0.3	NA	4.1	NA
PAT – FY21 (INR bn)	(3.5)	(1.9)	(1.0)	(1.1)	NA	(0.0)	NA

Source: VCCEdge, Industry, Company, HSIE Research

Co-Founders

CarDekho:

- Mr. Amit Jain
- Mr. Anurag Jain

Rupyy:

- Mr. Namit Jain

Company Description

CarDekho: Auto portal for buying and selling of used cars with ancillary services such as financing, insurance etc.

Rupyy: Digital lending platform for financing of used and new cars

Statistics

Rupyy:

- Cars sold on platform: 75K+
- Loans disbursed: INR 85bn
- Service locations: 132

CarDekho & Rupyy | Pre-owned Car platforms

Company Profile:

- **CarDekho** is a leading auto portal providing end-to-end services for buying and selling of used cars with presence in 88 cities with over 60 branches and 1,750 channel partners as of Oct-21. It primarily purchases cars from the end users with quality checks etc., re-furbishes them and sells it to buyers as well as other dealers.
- **Rupyy** (CarDekho Financial Services) is a digital lending platform, providing financing solutions through tie-up with multiple lenders as well as their in-house NBFC. The platform is seller-agnostic i.e. cars sold through non-CarDekho platforms could also avail financing through Rupyy.

Key Takeaways/Insights:

- Used cars market remains largely unorganised through small dealer/brokers, semi-organized dealers etc., as the new-age auto portals are yet to gain scale in context of used car market potential and OEM-backed dealers such as Maruti TrueValue/Mahindra FirstChoice etc. remain focused primarily on driving new car sales of the captive OEMs.
- Cars24, CarDekho etc. are incrementally focusing on retailing of cars and investing in re-furbishment centres, showrooms etc. to provide superior experience to buyers along with high trust (warranty etc.).
- Used cars financing market is currently at ~INR 0.3trn as finance penetration has improved to 20% from sub-10% a few years back and has a lot of room for further improvement.
- Interest rates for used cars financing is higher (~300-400bps) compared to new cars financing due to high opex (re-furbishing, valuation etc.) and marginally higher credit costs.

- **Used car financing—RoA accretive for lenders:** Our analysis indicates that used PV financing is relatively more RoA accretive compared to new PV financing, particularly for banks where the margins for new car financing are very thin.

  Increasing formalisation of the used car segment is addressing one of the key pain points—assessing the fair value of the vehicle—although entailing high opex on sourcing. Our interactions with lenders as well as bureaus indicate that NBFCs typically experience similar credit costs across both asset classes (new and used PVs). On the other hand, bank lending to used PVs entails higher credit costs relative to new PVs.

Exhibit 41: Banks' unit economics for used car financing at par with that of NBFCs

(% of Advances)	Banks	NBFCs	Comments
Interest Income	11.5%	15.0%	Higher yields compared to new Cars (~300bps+)
Interest Expenses	4.0%	7.0%	
Net interest income	**7.5%**	**8.0%**	
Fee income	0.8%	0.6%	
Total Income	8.3%	8.6%	
Operating expenses	2.9%	2.9%	Higher opex due to valuation, re-furbishing etc.
Pre-provisioning profit	5.4%	5.7%	
Total Provisions	1.5%	1.6%	Sharp jump when compared to new car financing for Banks compared to NBFCs
Profit before Tax	3.9%	4.1%	
Provision for Taxation	1.0%	1.0%	
PAT	**2.9%**	**3.0%**	

Source: Industry, Company, HSIE Research

1. Assumed accounting for Banks and NBFCs under GAAP for like-to-like comparison
2. Loan of ticket size of INR 0.4 mn with tenure of 3 years; processing fees and origination costs amortised
3. Cost of funds assumed similar to that of leading banks and NBFCs
4. Impact of SLR and CRR requirements not considered in case of Banks

Exhibit 42: Interest rates on used car loans disbursed in Q4FY22

Used Cars	Min	Max	Mean
AXSB*	6.65%	17.75%	9.99%
HDFCB	6.90%	14.00%	12.14%
ICICIBC	9.00%	17.01%	13.51%
ICICIBC**	9.25%	22.51%	14.07%

Source: Company, HSIE Research | ** Blended for New and Used car loans; ** For Q3FY22* | *Note: HDFC Securities is a subsidiary of HDFC Bank*

Exhibit 43: Comparison of used car financing economics vs. new cars

	Used cars	Comments
Interest Income	↑	Higher yields (~300bps+)
Fee income	↑	Higher processing fees charged
Operating expenses	↑	Transaction costs, refurbishment etc.
Total Provisions	↑	Higher delinquencies, LGDs

Source: Industry, HSIE Research

- **FinTechs—more of enablers rather than challengers:** FinTechs/tech companies focused on auto financing are more of enablers rather than a threat to the incumbents, in our view. Being a secured asset class with relatively higher ticket sizes and completely different lending dynamics, the segment has witnessed very few FinTech entrants, particularly on the lending side, as compared to unsecured personal loans/BNPL/payments, etc.

  Lending by FinTechs through own balance sheet is unlikely to become viable due to high cost of capital for these FinTechs (NBFCs), while the underlying asset class has relatively low IRR (12%-14%) compared to BNPL/unsecured personal loans where the yields are much higher.

Exhibit 44: FinTechs/tech companies in auto financing

Auto Portals	Digital Lending platforms	EV Lending platforms	Used Car leasing
•Cars24, CarDekho, Spinny etc. •Enable buying and selling of used cars through their platform •Value-add services such as inspection checks, valuation, refurbishment, warranty/ certification, financing through lenders etc.	•OTO Capital, Rupyy, Kuwy, AutoFin etc. •Digital platform/ marketplace for lenders and used car/2wheeler buyers/ sellers •Little balance sheet exposure due to high cost of capital and not commensurable yields on assets	•Revfin, Welectric etc. •Provide end-to-end solutions for owning an EV	•Pumpumpum, Mychoize (ORIX) •Used car leasing with subscription models •Asset light/asset heavy

Source: Industry, HSIE Research

EV financing—nascent market in making

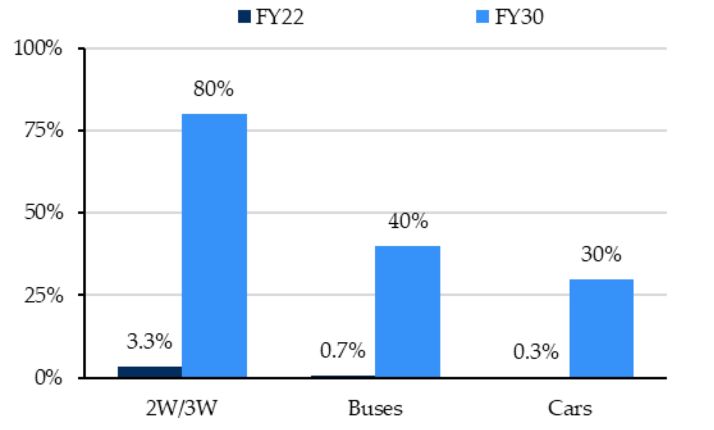
Electric vehicle (EVs) sales are gradually taking off in India, aided by the incentives for manufacturing and charging infrastructure through FAME-I/II and PLI schemes. NITI Aayog has an ambitious electrification target of 30% in PV sales and 40% in bus sales volumes by FY30E, providing a large opportunity for the lenders to tap into.

Exhibit 45: Gradual improvement in EV penetration, 3Ws already well penetrated

EV as % of total sales	FY20	FY21	FY22
2W	0.1%	0.4%	1.9%
3W	19.5%	34.2%	45.8%
PV	0.1%	0.2%	0.7%
CV	0.1%	0.1%	0.3%
Total	**0.8%**	**0.9%**	**2.7%**

Source: FADA, SIAM, HSIE Research

Exhibit 46: Expected EV penetration by 2030 by NITI Aayog



Source: NITI Aayog, HSIE Research

- **Unchartered territories, testing waters:** EV financing across vehicle categories is currently in unchartered territories as the underlying asset, which is the collateral, has limited resale market for repossession and recovery of dues and there are little branded players in the market which raises questions on the quality of the underlying asset to be financed. While the ecosystem will take time to develop the used EV market, lenders are broadly approaching this segment from cash flow perspective (for 3-wheelers) and based on the creditworthiness of the borrower (retail) rather than the traditional asset-based lending.

Exhibit 47: Leading EV OEMs and their tie-ups for auto financing

OEMs	Recent Financing Tie-ups
Ola Electric	HDFCB, ICICIBC, AXSB, KMBPrime, BOB, IIB, IDFCBK, Tata Capital
Ather Energy	HDFCB, IDFCBK, SBIN
Hero Electric	AXSB, HDB, RevFin, CIFC

Source: Industry, HSIE Research | Note: HDFC Securities is a subsidiary of HDFC Bank

- **Electric PVs—largely "bankable" category at present:** As per our interaction with lenders, EV financing for PVs is currently dominated by banks, largely due to the underlying customer profile. Most of the customers for EV financing are not first-time car buyers and have credit worthiness higher than the average ICE car borrower.
- **Electric 3Ws—sweet spot for NBFCs:** The 3W space has witnessed the highest EV penetration, contributing to nearly half of the total sales volumes in FY22. Given that the underlying customer segment remains largely self-employed and informal, NBFCs are better placed to tap into this opportunity while also exercising pricing power.

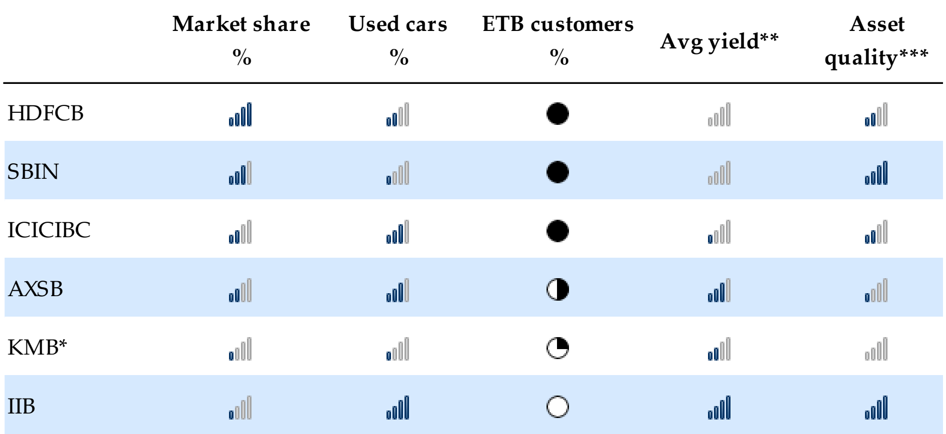
Exhibit 48: Challenges and opportunities in EV financing

Headwinds	Tailwinds
Limited discovery of salvage value – Low resale market	Exponential growth in EV sales going ahead
Rapid depreciation of asset (Battery costs)	Customer segment (in 2W and 4W) – prime and prime plus

Source: Industry, HSIE Research

- **Large banks dominant in the space:** Leading private banks, along with SBI and Bank of Baroda have dominant market share in the segment. Banks with large customer base such as SBI, ICICI Bank etc. tap into their existing customers for auto loans cross-sell at very competitive interest rates. Banks such as IndusInd Bank, on the other hand, have higher share of NTB customers, along with a healthy share of used car financing driving higher yields.

Exhibit 49: PV financing dashboard (Banks)

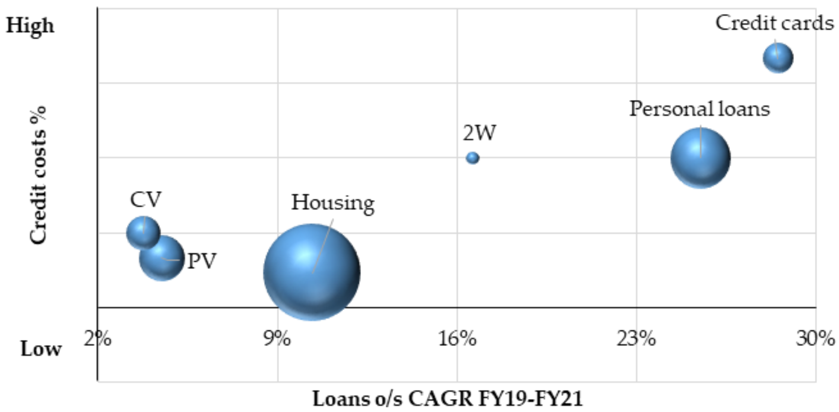


	Market share %	Used cars %	ETB customers %	Avg yield**	Asset quality***
HDFCB			●		
SBIN			●		
ICICIBC			●		
AXSB			◑		
KMB*			◔		
IIB			○		

Source: Company, Industry, HSIE Research I *Note: HDFC Securities is a subsidiary of HDFC Bank I On each parameter, a fuller bar indicates a superior franchise I * Kotak Mahindra Prime; ** Average yield based on mean interest rates for loans disbursed during Q4FY22; *** GNPA as on Mar-22 for vehicle loans portfolio, GNPA for ICICIBC and AXSB assumed similar to that of their retail portfolio*

- **Auto loans – portfolio approach, rather than product approach:** Auto loans, with ~3% market share in banking system loans and low profitability in the large new PV financing segment, has modest contribution to the overall profit pool. However, the increasing competitive intensity in the retail prime segment (affluent/salaried class) amongst leading banks is one of the major drivers of the auto loans portfolio becoming a must-have in the portfolio. Moreover, the ecosystem provides sufficient opportunities for adding profit pools such as dealer funding, used cars financing, re-finance etc.

Exhibit 50: Banks' various retail asset classes (Mar-22)

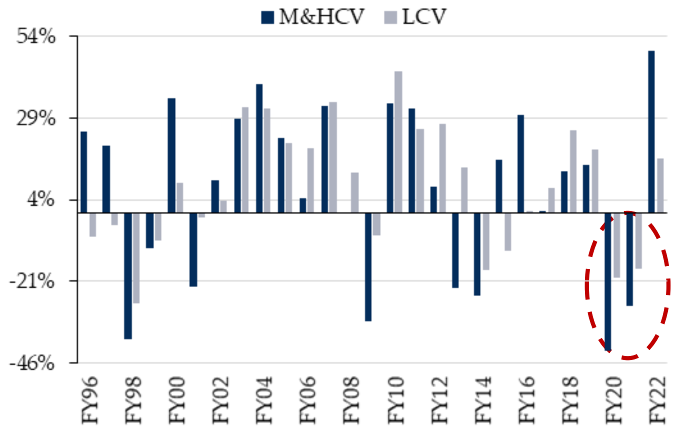


Source: CRIF Highmark, HSIE Research I Note: *Loans CAGR for the industry; Size of the balloon denotes loans outstanding for Banks as on Mar-22*

CVs–cyclical recovery on the cards

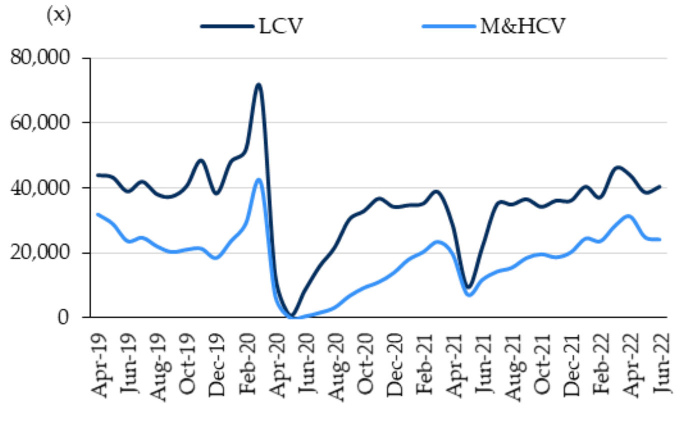
- **Strong up-cycle on the cards:** CV financing is poised to grow at ~13-15% CAGR, from US$ 53bn in FY22 to ~US$ 68-70bn in FY24 in terms of loans outstanding on the back of increasing off-take in CV sales, driven by improving economic activity, replacement demand, and scrappage policy. CV industry is poised to witness a strong up-cycle, having emerged out of one of the worst down-cycles of the last three decades, induced by the COVID pandemic.
- **Healthy uptick in sales volumes, improving utilisation levels:** New CV sales volumes have gradually picked up after the COVID pandemic; however, they are well below the pre-COVID peak during FY18-FY19. As per our interactions with dealers and lenders, the bulk of the new CV demand is driven by replacement demand, rather than fresh capacity additions, as fleet utilisation levels are a tad below pre-COVID levels. According to the forecast published by our auto analysts Aniket and Sonaal, M&HCV volumes are likely to witness a two-year CAGR of 18% while LCV volumes are expected to deliver a two-year CAGR of 13% over FY22-FY24E.

Exhibit 51: CV sales volume growth–uptick after a strong down cycle



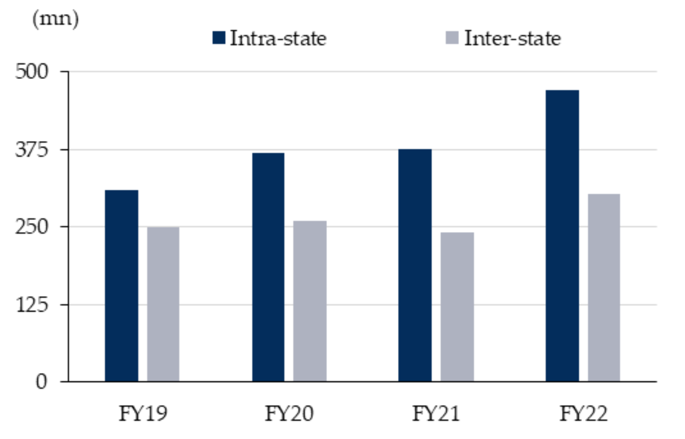
Source: SIAM, HSIE Research

Exhibit 52: Steady pick-up in CV sales volumes post COVID



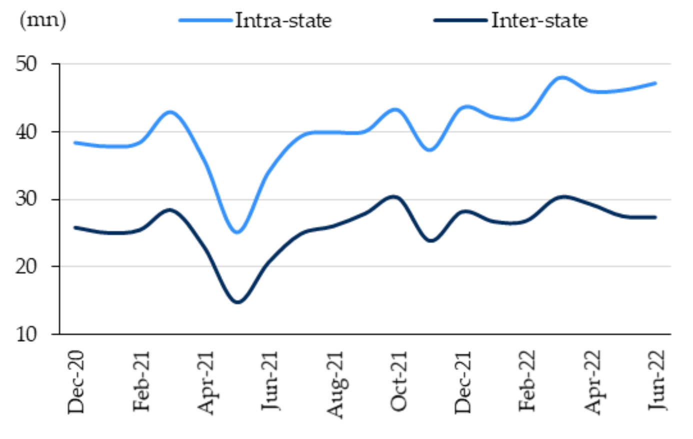
Source: FADA, HSIE Research

Exhibit 53: e-way bills generated: well above pre-COVID levels



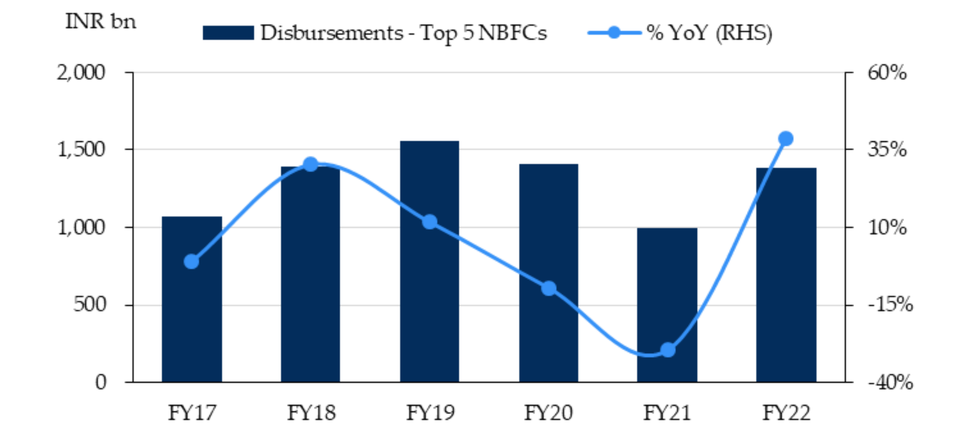
Source: GSTN, HSIE Research

Exhibit 54: Sustained monthly momentum in e-way bills generated



Source: GSTN, HSIE Research

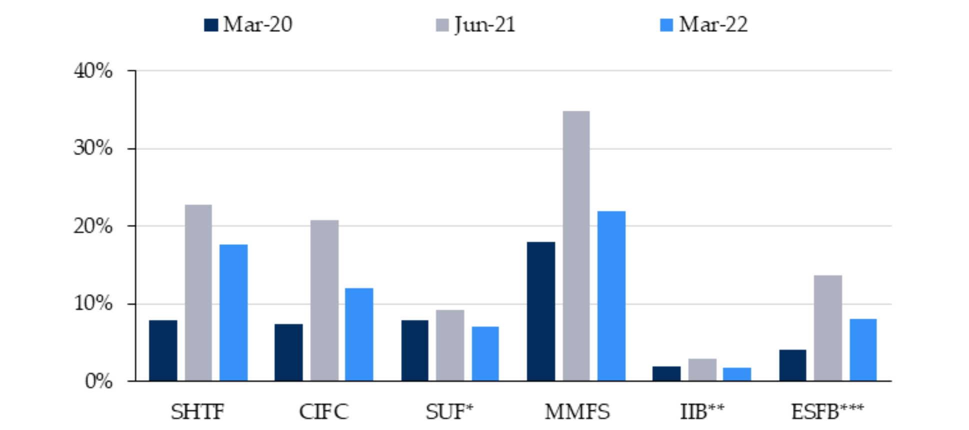
Exhibit 55: Strong pick-up in disbursements, nearing pre-COVID levels



Source: Company, HSIE Research | *NBFCs: SHTF, CIFC, MMFS, SUF and TMFL; Disbursements for CIFC include only vehicle finance segment*

- **Strong rebound in collection efficiencies driving lower stressed pool:** There has been a sharp rebound in collection efficiencies, led by improving economic activity and subsequently improving cash flows for fleet operators during CY22 (discussed in a subsequent section on pages 31 through 33). This has led to substantial improvement in the asset quality of CV financiers. The stressed pool (GS II + GS III) has reduced materially for most lenders and it is expected to reduce further in FY23.

Exhibit 56: Stressed pool for leading CV financiers (GS-II + GS-III) – material improvement



Source: Company, HSIE Research | *Note: *Restructured assets considered as GS-II for Jun-21; ** Includes only GNPA; *** Restructured book considered as GS-II, only GNPA available for Mar-20*

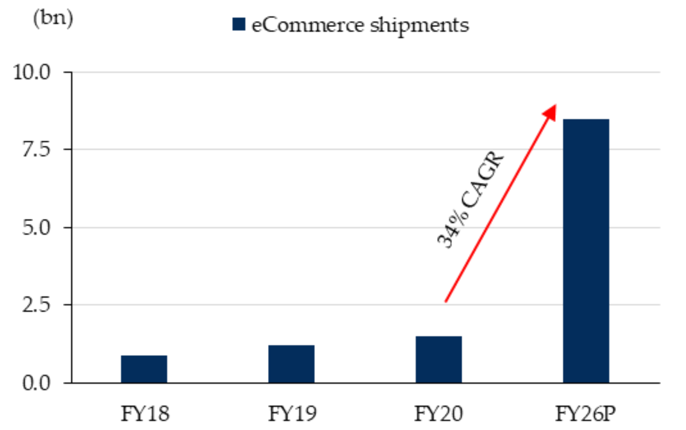
- **Improving pan-India consumption drives demand for last-mile logistics:** Categories such as auto sales, FMCG, consumer durables, etc. through offline and online channels have witnessed sharp uptick in growth along with pick-up in rural economy. Increasing consumption in urban as well as rural centres is boosting the road freight demand for last-mile delivery, which is likely to translate into higher SCV and ICV sales volumes.

Exhibit 57: Key indicators point towards strong revival in consumption post the pandemic

% YoY	PV sales	FMCG	Credit card spends
Q1FY21	-78.4%	-24.3%	-45.4%
Q2FY21	17.0%	-1.7%	-18.3%
Q3FY21	14.4%	5.5%	-3.5%
Q4FY21	42.5%	20.3%	9.5%
Q1FY22	320.4%	43.0%	84.2%
Q2FY22	2.1%	17.7%	59.5%
Q3FY22	-15.2%	14.1%	49.0%
Q4FY22	-2.3%	10.4%	42.4%
Q1FY23*	NA	NA	92.3%

Source: CMIE, RBI, Company, HSIE Research | *FMCG – volume growth for various key categories for listed FMCG firms; * Credit card spends data for Apr-May'22*

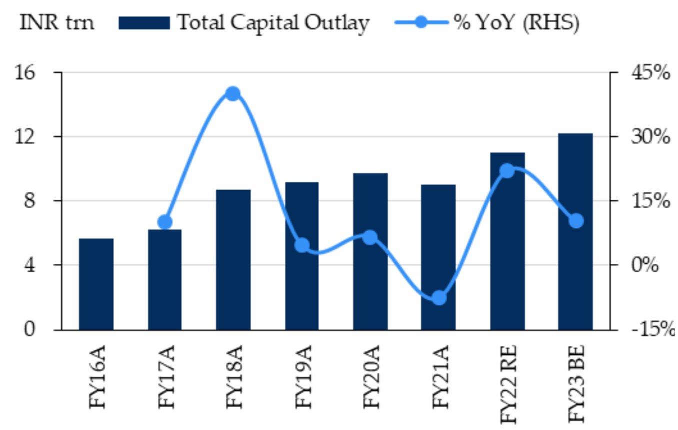
Exhibit 58: e-commerce shipments expected to grow at 34% CAGR during FY20-FY26P



Source: Delhivery RHP, HSIE Research

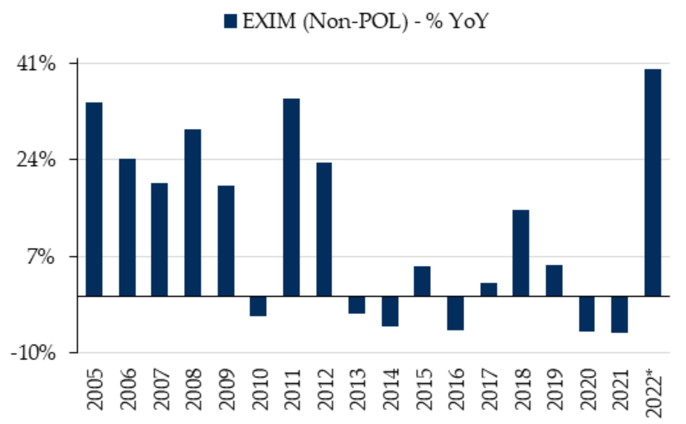
- **Surging government capex and improved economic activity to drive M&HCVs:** The strong revival in our M&HCV volume forecasts is premised on a sharp pick-up in economic activity (construction, mining, etc.) post the pandemic. Government capex continues to remain robust (~INR 12.2trn for FY23, +10% YoY), while private capex is expected to revive gradually. EXIM trade has also picked up sharply in FY22.

Exhibit 59: Government capex continues to grow in double digits



Source: Union Budget, HSIE Research | *Includes IEBR as well*

Exhibit 60: Sharp uptick in trade in FY22 after muted FY20 and FY21

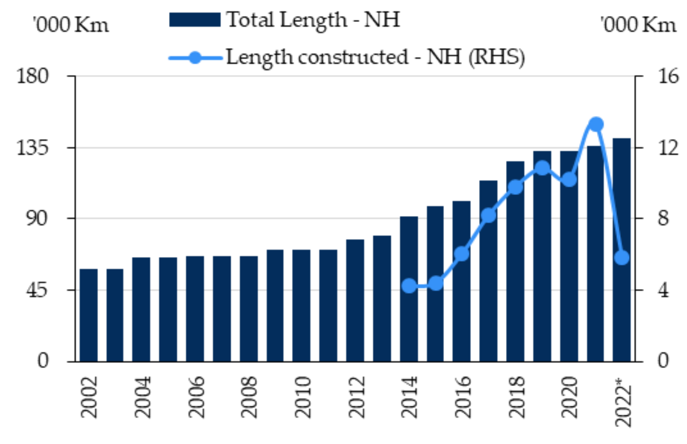


Source: CMIE, HSIE Research | Note: In US$

- **Investments in roads infra improving competitiveness:** Government's significant ramp-up in investments in road infrastructure, along with GST and e-way bill implementation, is aiding higher operating efficiencies for fleet operators (lower commute time, higher mileage, lower wear and tear, etc.), narrowing the gap further with rail freight rates.

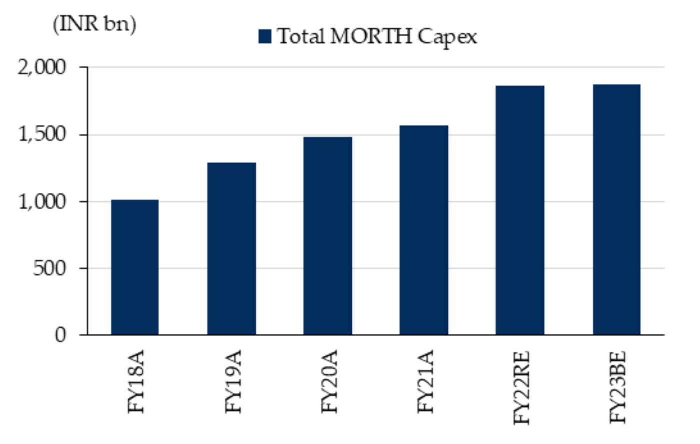
  Rail freight traffic, pre-dominantly bulk commodities, has remained muted during the decade (~1% CAGR), with road freight continuing to gain market share (~68% in freight with lead distance >300Km in 2019, as per Draft National Rail Plan 2020). While the commencement of DFCs (complete stretch) could be a near-term headwind for road freight, particularly for bulk commodities and containers, the improving unit economics for road freight, along with the advantage of last-mile connectivity, could arrest the market share losses, if any.

Exhibit 61: Significant pace of road infra in the last eight years – national highways



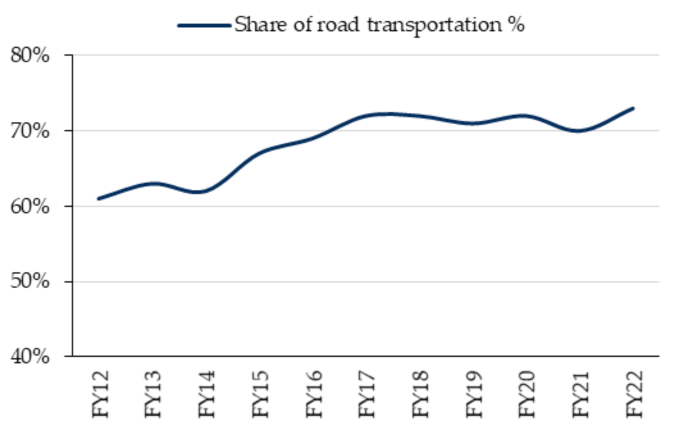
Source: MoRTH, CMIE, HSIE Research *Note: * Data for length constructed for Apr-Dec'21*

Exhibit 62: Road capex outlay for FY23



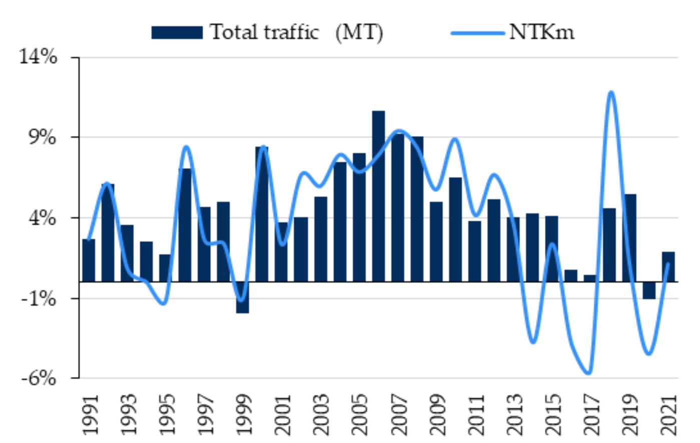
Source: Union Budget, HSIE Research | *Includes IEBR as well*

Exhibit 63: Share of road in freight mix has been steadily increasing for India's largest cement producer



Source: Company, HSIE Research

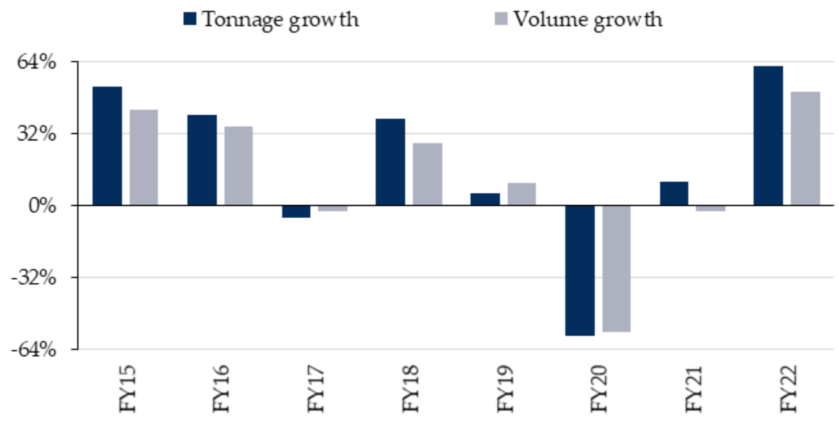
Exhibit 64: Rail freight traffic (tonnage) and tonnage km – muted during the past decade



Source: CMIE, HSIE Research

- **Tonnage growth to outpace volume growth:** Revised axle load norms alongside a shift towards higher tonnage vehicles in the HCV segment to drive economies of scale are leading to tonnage growth outpacing volume growth. Subsequently, while the volumes are likely to remain below FY19 levels until FY24, the fleet capacity in terms of tonnage is likely to be much higher.

Exhibit 65: Tonnage growth vs. volume growth for HCVs (% YoY)



Source: SIAM, HSIE Research

- **Replacement demand at play; could drive used CV sales too:** As per our interactions with dealers, lenders and fleet operators, the current uptick in CV volumes is largely driven by replacement demand, which was deferred during the pandemic. This is further driving the used CV volumes, which had witnessed high demand during the pandemic.

- **Scrappage policy unlikely to be a major volume driver:** The recently notified scrappage policy is fraught with several challenges in the near term for meaningful off-take such as low incentives (and disincentives) for scrapping old vehicles, contingency on state governments and OEMs to provide discounts/rebates, execution challenges such as investments in testing centres and scrappage centres, ensuring incentives provided induce new vehicle sales, etc. Near-term off-take of scrappage policy is likely to emerge from SRTOs, defence and other government departments.

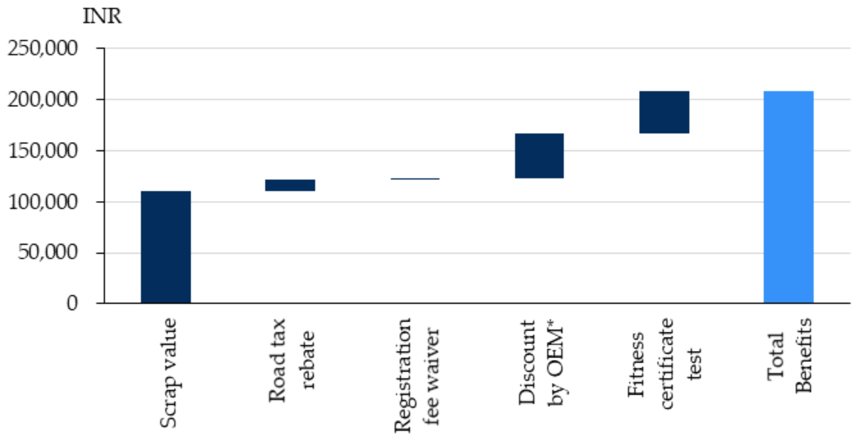
  The bulk of the estimated ~1mn CVs more than 15 years old are with small fleet operators/individual truck-owners that ply on short-haulage routes where enforcing the policy is likely to be a challenge. Further, their unit economics get stretched with replacement of the vehicle and sharp increase in new and used vehicle prices. Hence, given such low level of incentives, very few small fleet operators, may be incentivised to scrap their fleet and replace them, under the current policy.

Exhibit 66: Scrappage policy – incentives and disincentives

	Commercial vehicle	Passenger vehicle
Incentives		
Salvage value	Depending on vehicle condition (~4-5%)	Depending on vehicle condition (~4-5%)
Registration fees waiver	100% waiver	
Road tax rebate	15% rebate for 8 years on new vehicle	25% rebate for 15 years on new vehicle
Disincentives		
Fitness test and certification charges	INR 1,500 for conducting test; INR 12.5K for renewal of fitness certificate	INR 1,000 after 15 years (currently INR 600)
Renewal of RC	None	INR 5,000 on renewal (currently at INR 600)

Source: MoRTH, HSIE Research

Exhibit 67: Benefits for a MCV (16 tonne) for scrapping 15 year old truck at ~9% of new truck price

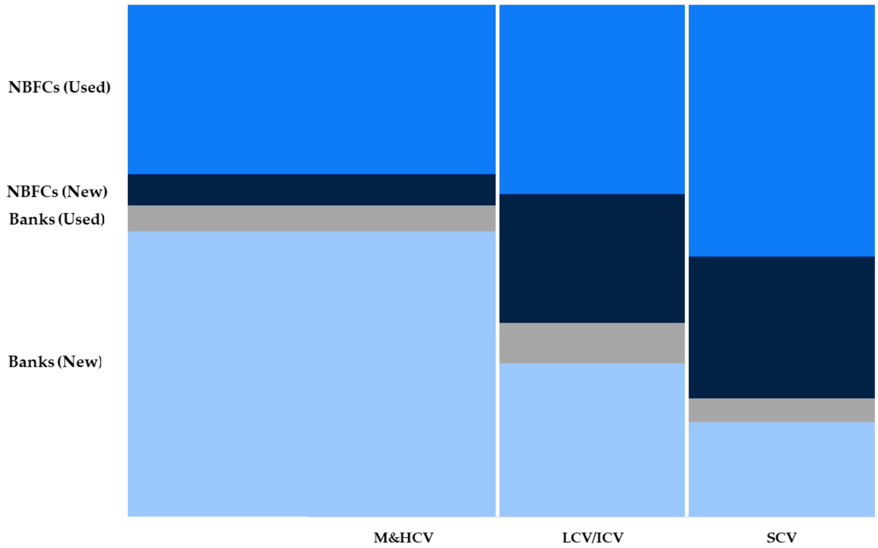


Source: MoRTH, HSIE Research | **Assuming OEM discount at 2%, scrap value at ~5% and waiver of registration fee*

Heterogeneous market; multiple forces at play

- **Heterogeneous market with multiple pockets of opportunity for lenders:** CV financing is relatively highly fragmented vs. PV financing, with different competitive positioning of banks and NBFCs based on vehicle type (M&HCV, LCV/ICV, SCV, etc.), customer profile (large/mid-size/small fleet operators and individual truck owners) and vehicle vintage (new/used). NBFCs have a dominant market share in used CV financing across categories as well as in new vehicles financing in the smaller CVs segment. Banks relatively have a higher market share in new CV financing for large and mid-size fleet operators.

Exhibit 68: CV financing - market landscaping



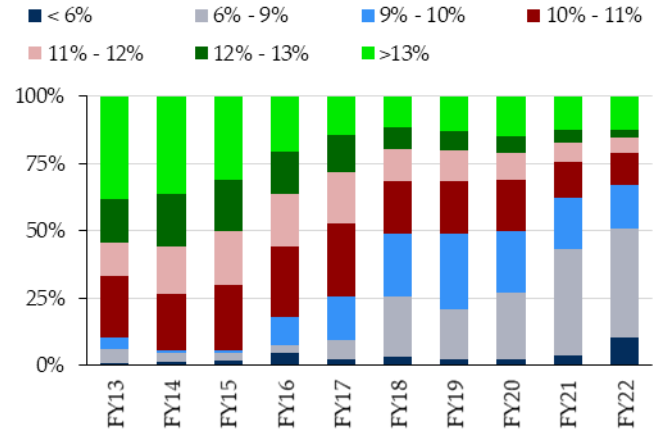
Source: CRIF Highmark, Industry, HSIE Research | *Loans outstanding*

- **Banks skewed towards metro-based operators with high ticket-size exposures:** Banks' credit to road transporters (CV financing) remains skewed towards urban and metro-based fleet operators, with ~40% of outstanding exposure over INR 50mn (~26% above INR 1bn) and ~85% exposure in metros and urban centres. The segment remains highly competitive with relatively low bargaining power (~2/3rd of the book yielding sub-10%); however, the segment provides huge cross-sell opportunities (working capital financing, overdraft, etc.), particularly for banks.

  In terms of volumes, **~72% of loan accounts** have exposure **below INR 0.5mn**, while **~54% of outstanding** accounts have **interest rate higher than 13%**, indicating a long tail of high yielding small-ticket size exposure to small fleet operators.

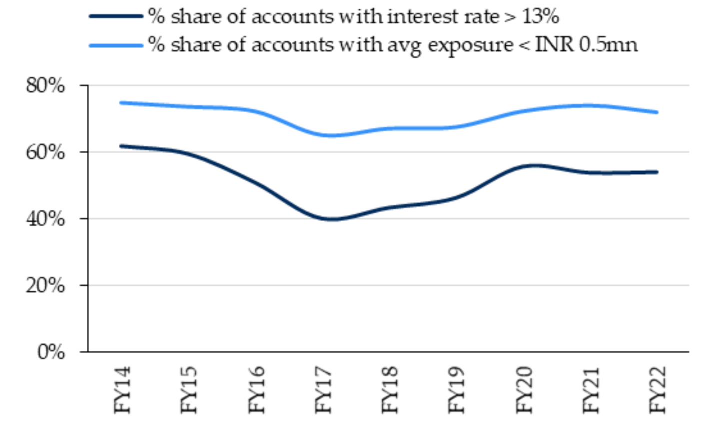
  Leading private banks such as HDFC Bank, ICICI Bank, IndusInd Bank, etc., are the major players in this segment, with select NBFCs such as captive financiers (Tata Motors Finance) and Sundaram Finance in the small/mid-size fleet segment.

Exhibit 69: Banks' credit to transport operators - ~2/3rd of book yielding sub-10%



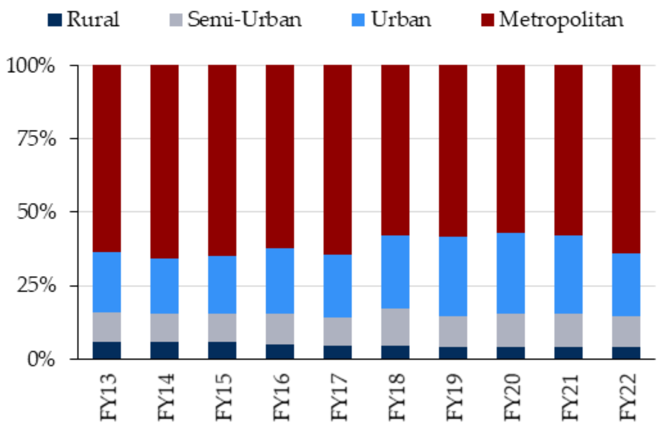
Source: RBI, HSIE Research

Exhibit 70: Banks' credit to transport operators by volume



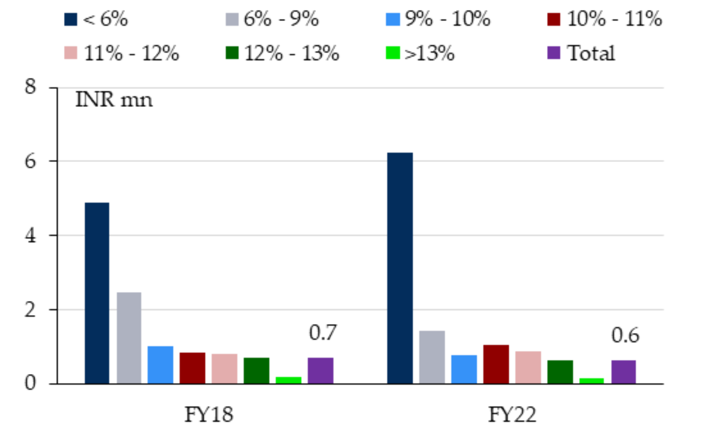
Source: RBI, HSIE Research

Exhibit 71: ~85% of bank credit to transport operators' (by value) from metro and urban centres



Source: RBI, HSIE Research

Exhibit 72: Banks' credit to road transporters - average loans outstanding based on interest rate range



Source: RBI, HSIE Research

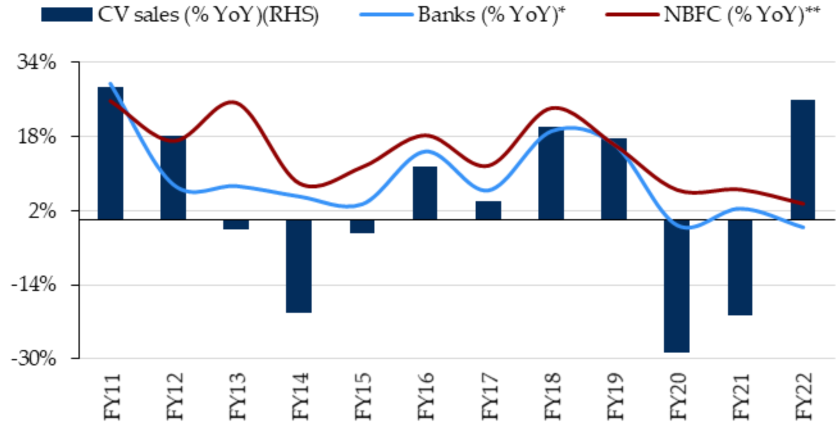
Exhibit 73: Banks' CV loans – interest rates for loans disbursed during Q4FY22

	Min	Max	Mean
HDFCB	6.5%	14.0%	8.2%
ICICIBC	7.3%	20.0%	9.7%
AXSB	6.5%	16.0%	8.6%
SBIN	8.0%	10.5%	NA

Source: Company, HSIE Research | Note: HDFC Securities is a subsidiary of HDFC Bank

- **Banks seeking market share; intense competition ahead:** Banks, having receded market share to NBFCs, are increasingly seeking market share gains during CY22 as collection efficiencies have rebounded strongly, based on our interactions with various lenders and market participants. We expect banks to gain market share in the new CV segment and grow in double-digits over the next couple of years.

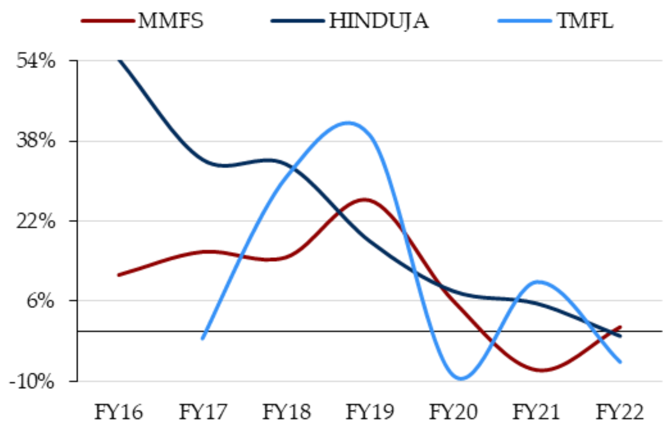
Exhibit 74: Banks' credit to road transporters lagged AUM growth of top-4 vehicle NBFCs



Source: RBI, Company, HSIE Research | *Note: *Banks' credit to road transporters; **NBFCs: AUM of SHTF, CIFC (Vehicle finance), SUF and MMFS (CV)*

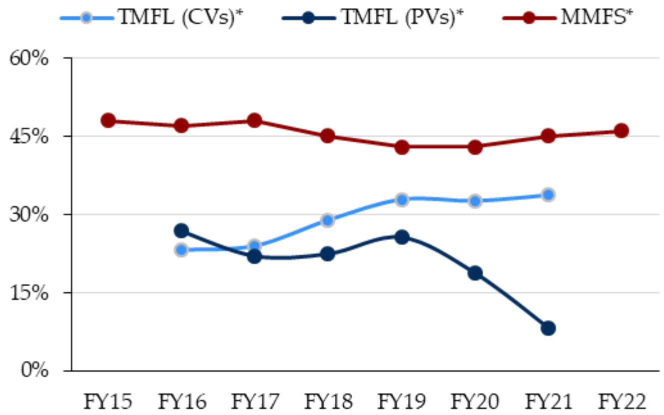
- **Captive NBFCs ceding market share on asset quality woes:** Competitive intensity had softened in the new CV financing segment with the ceding of market share by captive NBFCs such as Tata Motors Finance, Hinduja Leyland Finance, Mahindra Finance, etc. Most captive NBFCs had witnessed astronomical growth during FY17-FY19, driven by strong volume growth of the captive OEMs, followed by ballooning of the stressed pool during the pandemic. As the asset quality challenges subside, we expect captive NBFCs to intensify the competition during H2FY23 or FY24.

Exhibit 75: Loan growth of captive NBFCs



Source: Company, HSIE Research | IND AS from FY18 onwards

Exhibit 76: Contribution of captive NBFCs to OEMs' sales

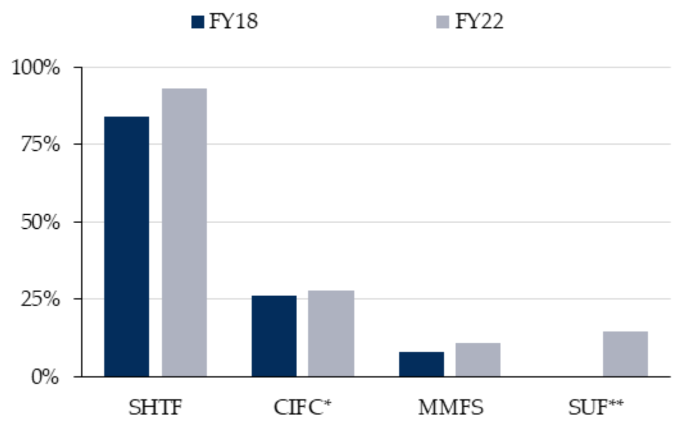


Source: Company, HSIE Research | *Note: *volume market share for TMFL in Tata Motors sales volumes;** M&M vehicles contribution to MMFS' AUM*

- **Used CV financing likely to remain NBFC forte:** Used CV financing is likely to continue to be dominated by NBFCs despite banks making inroads in semi-urban/rural areas and MSME segment. A relatively less-competitive market comprising mostly small fleet operators/individual vehicle owners, it provides superior yields (~12-20%) based on the vehicle vintage (1-5yr/5-10yr/10-14yr), partially offset by high opex intensity in sourcing and collections & recoveries as the underlying customer segment remains most vulnerable to economic shocks.

  Given the investments in distribution network (for sourcing and collections), little formal documentation of underlying borrowers and high volatility in their cash flows, banks are expected to continue to have relatively low direct presence in this segment and are likely to opt for co-lending/direct assignment with the NBFCs.

Exhibit 77: Share of used vehicles in total AUM



Source: Company, HSIE Research | *Note: * % of vehicle finance AUM; ** Data for Mar-18 not available*

Exhibit 78: AUM mix – vehicle financiers

as % of AUM (Mar-22)	M&HCV	LCV/SCV	PVs
CIFC	8.8%	25.8%	19.3%
SHTF	47.3%	27.2%	20.6%
SUF	45.6%		25.7%
MMFS	12.0%		65.0%
IIB	9.7%	1.3%	6.1%
KOGTA	6.2%	35.5%	25.2%
SKFIN	49.0%		17.3%

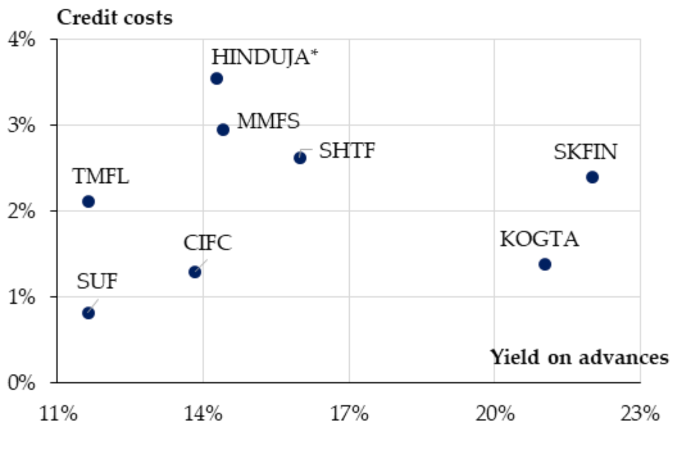
Source: Company, HSIE Research

Exhibit 79: Used CV vs. new CV financing for NBFCs

% of advances	New CV	Used CV
Interest income	11% - 14%	14% - 20%
Interest expense	~7%	~7%
Net interest income	4% - 7%	8% - 12%
Other income	~0.5%	~0.5%
Total income	5% - 8%	9% - 13%
Operating expenses	2.2% - 2.6%	2.6% - 3%
Pre-provisioning profit	2.8% - 5.4%	6.4% - 10%
Credit costs	1% - 2%	3% - 5%
Profit Before Tax	1.8% - 3.4%	3.4% - 5%
Profit After Tax	1.4% - 2.6%	2.7% - 4%

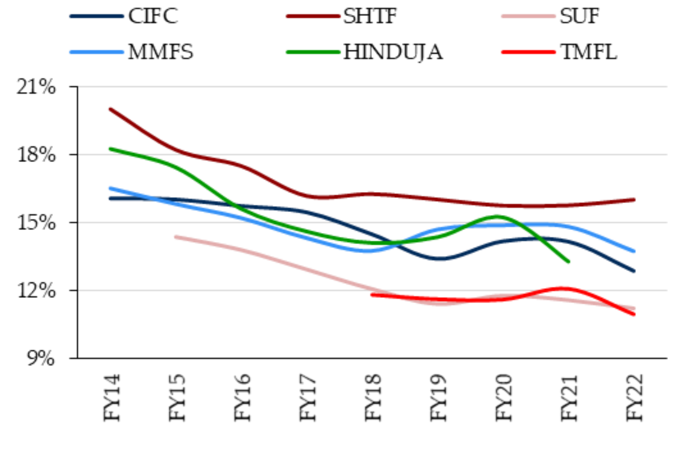
Source: Industry, HSIE Research | *Note: RoA tree is indicative and may vary from one NBFC to another depending upon opex and risk management*

Exhibit 80: Yields vs. credit costs for NBFCs (average of FY18-FY22)



Source: Company, HSIE Research | *Note: *FY18-FY21 for Hinduja Leyland Finance*

Exhibit 81: Yield on advances – steady over the last few years



Source: Company, HSIE Research | IND AS from FY18 onwards

- **Small niche lenders shaping up well; scalability to be seen:** Select small-sized NBFCs such as Kogta Finance and SKFin have been growing at a fairly healthy pace over the past several years. Both these NBFCs are concentrated in the north-western belt (Rajasthan, Gujarat and Maharashtra) and have diversified their loan book to cars, tractors, MSME lending, etc. While their financial performance has been exemplary, particularly in a stressed environment, the same needs to be seen as they achieve scale and diversify outside of their core geographies.

Exhibit 82: Snapshot of financial performance – Kogta and SKFin

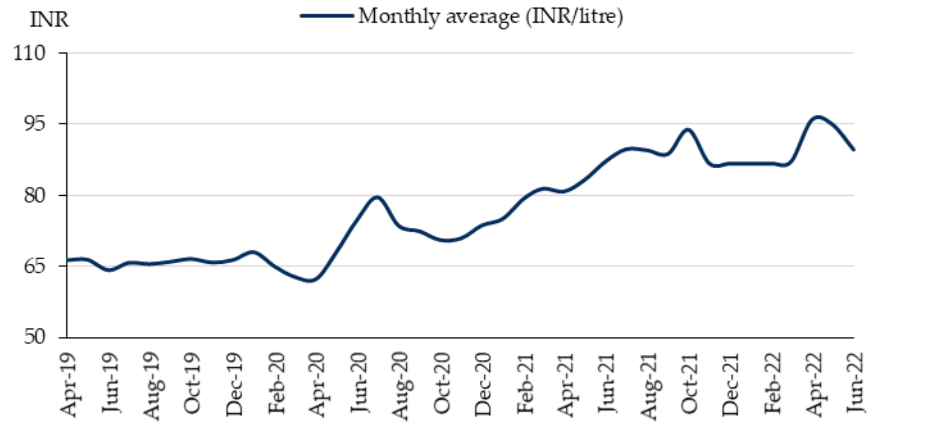
FY22	Units	Kogta	SKFin
AUM	INR bn	21.8	47.1
AUM CAGR: FY19 – FY22	%	45.3%	33.1%
Yield on Advances	%	20.4%	19.6%
ROA	%	2.4%	2.7%
ROE	%	8.4%	11.1%
Tier I	%	28.5%	30.4%
GS II	%	8.0%	7.2%
GS III	%	3.6%	2.8%

Source: Company, HSIE Research

CV financing–profitability nears trough

- **Rising input cost pressures for fleet operators:** The increasing cost pressures for fleet operators such as fuel prices, vehicle prices (new and used; due to emission norms), commodity prices, and insurance charges are gradually increasing their opex.

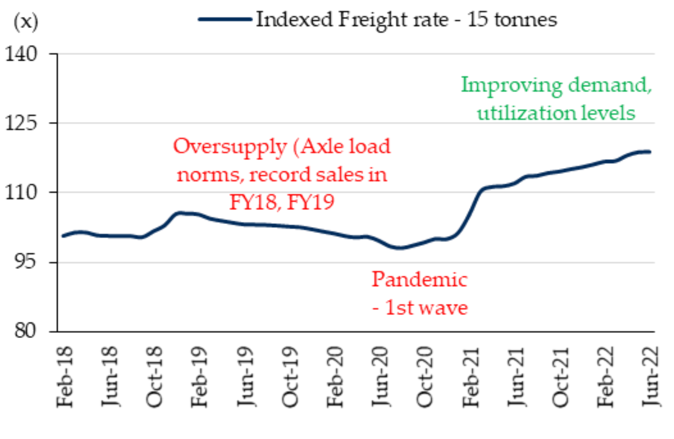
Exhibit 83: Diesel prices have increased by ~20% during the last two years



Source: Bloomberg, HSIE Research | *Retail diesel prices in Delhi*

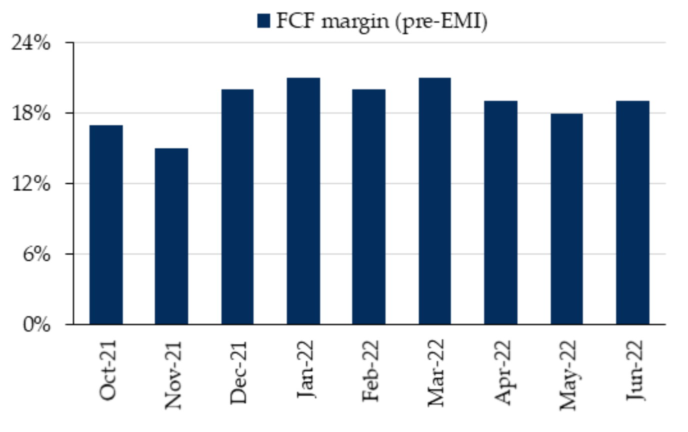
- **Improving demand driving the unit profitability of fleet operators:** Freight rates have been steadily inching up with improving utilisation levels, providing support to the unit profitability of the fleet operators. While input cost pass-through varies from segment to segment (contractual/spot, large/small fleet operator, nature of commodities transported, etc.), the current freight rates broadly indicate a healthy level of profitability for most fleet operators, although below pre-COVID levels.

Exhibit 84: Freight rates have continued to inch up



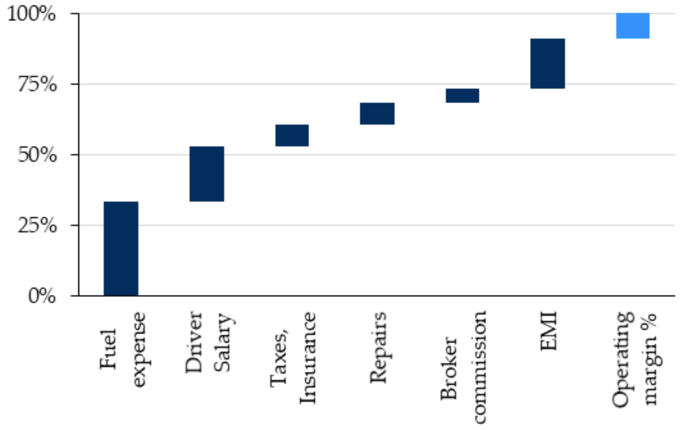
Source: CMIE, HSIE Research | *Average freight rate from Delhi to 16 different locations (long haulage) for 15 tonne haulage truck; indexed to 100 for Jan-18*

Exhibit 85: FCF (pre-EMI) of fleet operators as per CRISIL estimates



Source: CRISIL, HSIE Research

Exhibit 86: Operating cost structure for a used 12 tonne truck for a long haulage trip



Source: Industry, HSIE Research

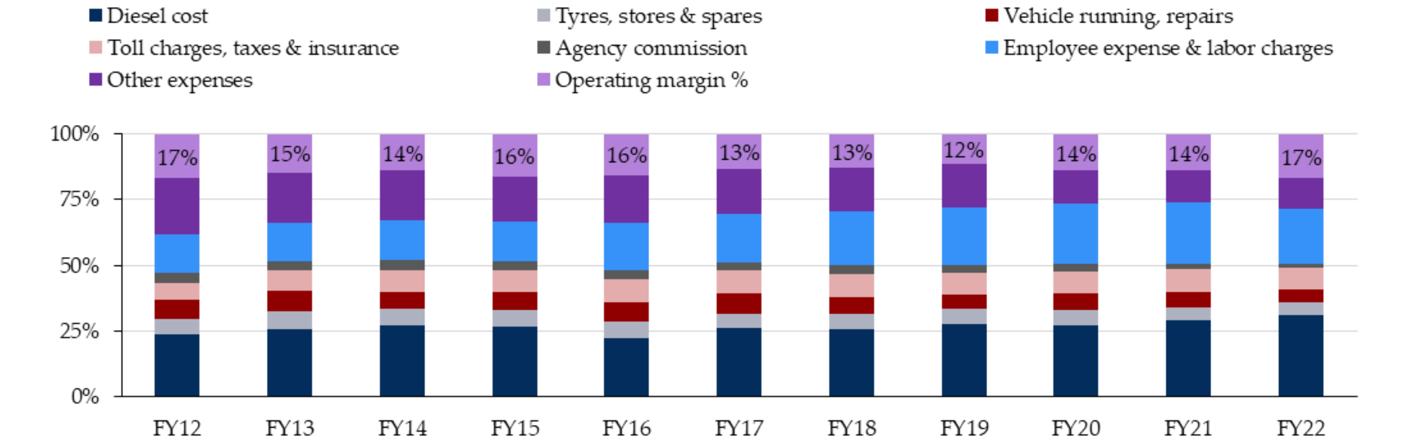
1. *Distance traveled: 650 Km; Diesel cost at INR 90/litre, Mileage at 7 per litre*
2. *Ticket size of INR 11 lakh; Interest rate of 16%; Tenure: 5 years*

Exhibit 87: Impact of change in diesel prices and freight rates on operating margin (pre-EMI) (bps)

	(bps)	Freight rate hike (%)					
	0	**0%**	**1%**	**2%**	**3%**	**4%**	**5%**
Fuel price hike (INR)	**2**	(78)	(17)	44	103	161	218
	4	(156)	(94)	(33)	27	86	144
	6	(235)	(171)	(109)	(49)	11	69
	8	(313)	(249)	(186)	(125)	(64)	(5)
	10	(391)	(326)	(263)	(201)	(140)	(80)

Source: Industry, HSIE Research | *Note: Assumptions similar to Exhibit 86*

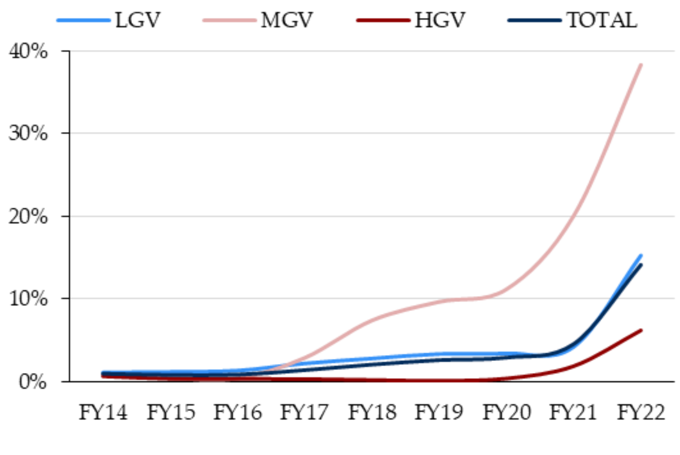
Exhibit 88: Operating margin for VRL Logistics improved during FY22 (% of revenues)



Source: Company, HSIE Research

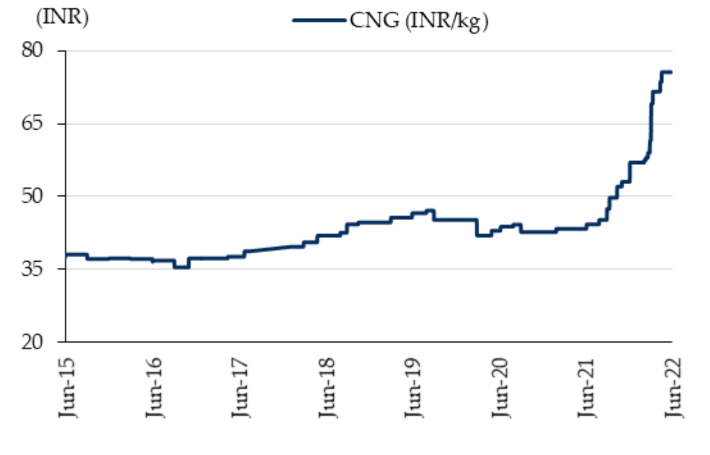
- **Shift towards CNG in LCV/SCV segment improving unit economics, but..:** Better unit economics, along with concession on green tax and improving distribution of fuel pumps in select geographies, has been driving the increasing share of CNG vehicles in new CV sales, particularly LCV (~15% penetration in new vehicle sales) and MCVs (~39% penetration). However, CNG prices have surged by ~74% in the last twelve months, impacting their unit economics as well. Having said that, we expect share of CNG in LCV and MCV segment to continue to improve with expanding distribution network in the country.

Exhibit 89: Share of CNG vehicles in total sales volumes



Source: VAAHAN, HSIE Research I *LGV: Light Goods vehicle; MGV: Medium goods vehicle; HGV: Heavy Goods vehicle*

Exhibit 90: CNG prices have shot up sharply by 43% during CY22



Source: Company, HSIE Research

- **Asset quality challenges largely mirror utilisation levels:** The asset quality of the CV portfolio remains largely contingent on the industry utilisation levels which affects the pass-through of cost pressures on freight rates. Utilisation level is impacted by various factors such as monsoon for agri transporters, industry oversupply with heavy push from OEMs towards new vehicles sales, decline in underlying demand with muted economic activity, etc.

CHAWLA ROADLINES
FLEET OWNERS & TRANSPORT CONTRACTORS

Founder & CEO

Family-owned Business currently headed by Mr. S.S. Chawla

Company Description

A logistics service provider providing end-to-end logistics solutions predominantly from Mumbai to Kolkata

Statistics

- 120 owned vehicles
- ~50 M&HCVs
- Avg. age of fleet: 3 – 4 years
- 68 national and multinational clients

Chawla Roadlines | Large Fleet operator

Company Profile:

- Chawla Roadlines is a large fleet operator with transportation and warehousing services with over 120 owned vehicles, plying primarily on the Mumbai-Kolkata route.
- Its large fleet of over 120 vehicles (~50 in the M&HCV segment) caters to a wide gamut of industries like plastic, steel, chemicals, paints, FMCG etc.

Key Takeaways:

- Freight rates by large corporate clients are gradually shifting from contract-based pricing to a mix of contract-based and spot-bidding pricing, leading to increasing competitive intensity among fleet operators.
- Pass-through of input cost pressures (diesel prices etc.) is largely a function of freight demand and capacity supply. During times of high freight demand (and high utilisation levels), pass-through is not a major challenge.
- Improving road connectivity, e-way bill implementation, FASTag etc. has reduced time to commute, improving truck availability as well as competitiveness with rail freight.
- While the vehicle prices have witnessed a steep increase during the last few years, increasing shift towards higher tonnage vehicles is driving economies of scale for fleet operators, leading to lower opex per tonnage.
- Muted business demand during Covid pandemic has witnessed the exit of a lot of fringe players, leading to reduction of capacity overhang and healthy utilisation levels for the industry. The new vehicle sales volumes is largely driven by existing mid and large-fleet operators, however aggressive lending rates typically attracts new players leading to capacity oversupply.

- **ROA poised to improve:** The earnings profile of CV financiers is poised for mean reversion during FY23-FY24E, driven by lower incremental provision on the stressed assets, partially offset by higher cost of funds. The improving pricing power with improving demand is likely to be offset with increasing competitive intensity by banks in select segments. We expect standalone NBFCs to revert to a steady state level, ahead of captive NBFCs.

Exhibit 91: RoA profile of CV financing NBFCs

% of Avg. assets (FY18 - FY22)	Standalone NBFCs			Captive NBFCs			Emerging players	
	CIFC	**SHTF**	**SUF**	**MMFS**	**HINDUJA***	**TMFL**	**KOGTA**	**SKFIN**
Interest Income	13.2%	14.6%	10.3%	13.6%	12.4%	10.3%	16.8%	18.1%
Interest Expenses	6.8%	7.4%	5.9%	6.2%	7.1%	6.9%	7.2%	8.0%
Net interest income	6.4%	7.2%	4.4%	7.3%	5.3%	3.4%	9.6%	10.0%
Non-Interest Income	0.7%	0.3%	1.7%	0.3%	1.4%	1.4%	1.3%	1.9%
Total Income	**7.1%**	**7.5%**	**6.1%**	**7.7%**	**6.7%**	**4.8%**	**10.9%**	**11.9%**
Operating Expenses	2.6%	1.8%	2.1%	2.7%	1.5%	2.6%	6.3%	6.3%
Pre-provisioning profit	**4.5%**	**5.7%**	**4.0%**	**4.9%**	**5.2%**	**2.2%**	**4.5%**	**5.7%**
Total Provisions	1.2%	2.5%	0.7%	2.6%	3.1%	1.8%	1.1%	2.0%
Profit before Tax	3.3%	3.3%	3.3%	2.3%	2.1%	0.4%	3.5%	3.7%
Provision for Taxation	1.0%	1.0%	0.9%	0.8%	0.7%	-0.2%	0.9%	1.0%
RoA	**2.3%**	**2.3%**	**2.3%**	**1.5%**	**1.4%**	**0.6%**	**2.5%**	**2.7%**
Avg Assets/Avg Networth	8.1	6.4	5.8	5.8	7.0	10.1	3.5	4.6
RoE	**18.5%**	**15.0%**	**13.4%**	**9.0%**	**10.3%**	**6.2%**	**8.7%**	**12.1%**
AUM: Mar-22 (INR bn)	**769**	**1,270**	**295**	**798**	**272***	**299****	**22**	**47**

Source: Company, HSIE Research | *Note: *For FY18 to FY21; ** Gross advances*

Exhibit 92: FY22 performance snapshot

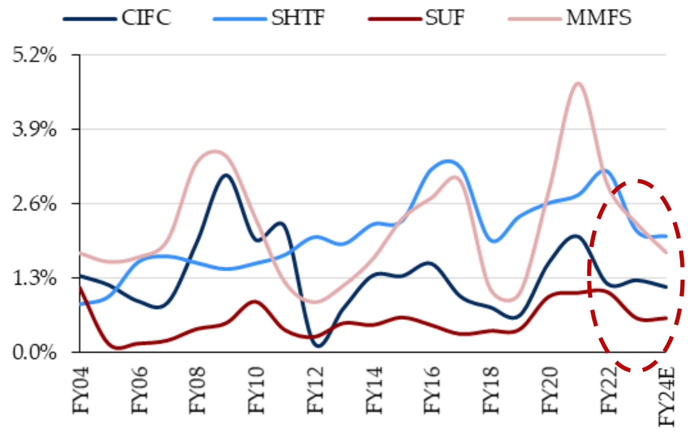
FY22	AUM growth	RoA	RoE	Credit costs	GS III
CIFC	10%	2.7%	20.2%	1.2%	4.4%
SHTF	8%	2.0%	11.4%	3.2%	7.1%
SUF	-4%	2.6%	13.8%	1.1%	2.3%
MMFS	1%	1.3%	6.5%	3.7%	7.7%
HINDUJA*	-1%	1.4%	8.4%	3.4%	6.4%
TMFL*	-6%	-0.1%	-1.4%	3.8%	10.3%
KOGTA	46%	2.4%	8.4%	1.0%	3.6%
SKFIN	42%	2.7%	11.1%	0.4%	2.8%

Source: Company, HSIE Research |* Loan growth

- **Impairment recognition largely over, expect credit costs to gradually come off:** Most lenders' CV portfolios have witnessed substantial reduction in their stressed pool and are expected to normalise further in FY23, with improving cash flows of the fleet operators. With healthy GS-III PCR at 40%-58% and overall PCR at ~2% - 7%, we expect the provisioning during FY23-FY24E to decline by ~20-120 bps, near to long-term trends.

- **RBI's revised IRAC norms unlikely to materially impact LGDs:** The RBI's revised IRAC norms for NBFCs to be implemented from Sep-22 are unlikely to impact the LGDs of the vehicle financing portfolio of NBFCs. Most NBFCs have made adequate provisioning for the stressed assets in the early delinquencies bucket (GS-II) as per their ECL norms under IND AS. With healthy provisioning and declining stressed pool, the incremental provisioning for the increase in GNPA is likely to be limited.

Exhibit 93: Credit costs to normalise during FY23-FY24E



Source: Company, HSIE Research | *Note: IND AS from FY18 onwards*

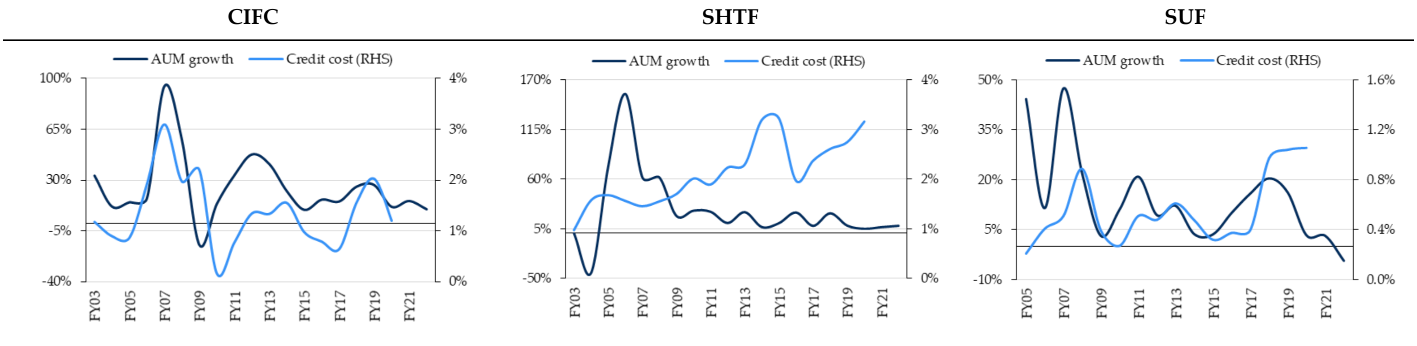
Exhibit 94: ECL provisions in various buckets (Mar-22)

ECL provisions %	GS-I %	GS-II %	GS-III %
CIFC	0.5%	11.3%	39.7%
SHTF	3.3%	9.1%	50.0%
SUF	0.4%	6.5%	52.0%
MMFS	2.3%	12.7%	58.1%
TMFL	0.4%	4.5%	44.3%

Source: Company, HSIE Research

- **Past trends indicate credit costs trail AUM growth with a lag:** Our analysis of the leading vehicle financing NBFCs over the past couple of decades indicates high correlation between strong loan growth and high credit costs in the subsequent couple of years (Exhibit 95). This could be attributed to muted economic activity after a strong up cycle leading to lower utilisation levels (double whammy of increased supply and decreased demand) and subsequently higher delinquencies.

Exhibit 95: AUM growth, along with a lagged (two-year) credit costs



Source: Company, HSIE Research

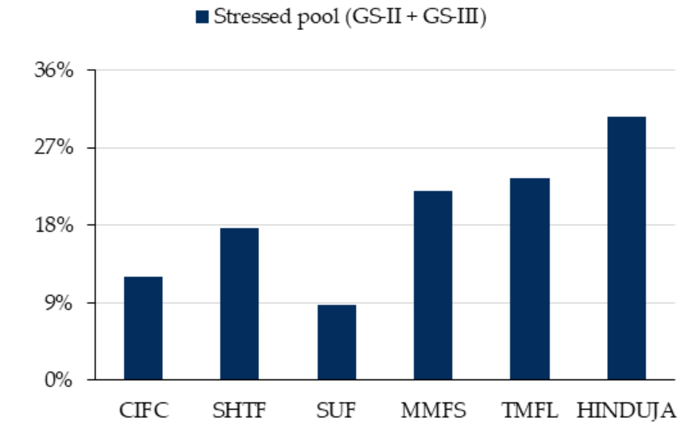
- **Captive NBFCs under higher stress:** Captive NBFCs such as Tata Motors Finance, Hinduja Leyland Finance, and Mahindra Finance have witnessed higher levels of stress compared to standalone NBFCs, driving elevated credit costs during FY20-FY22. While the overall economic environment has improved substantially after COVID, we expect the pace of normalisation in captive NBFCs to lag that of standalone NBFCs.

Exhibit 96: Credit costs jump sharply for Captive NBFCs

Provisioning %	FY18-FY19	FY20-FY22	FY23-FY24E
CIFC	0.7%	1.6%	1.2%
SHTF	2.2%	2.8%	2.1%
SUF	0.4%	1.0%	0.6%
MMFS	1.1%	3.5%	2.0%
TMFL	0.8%	3.0%	NA
HINDUJA	3.4%	3.6%	NA

Source: Company, HSIE Research

Exhibit 97: Aggregate stressed pool (GS-II + GS-III) as on Mar-22

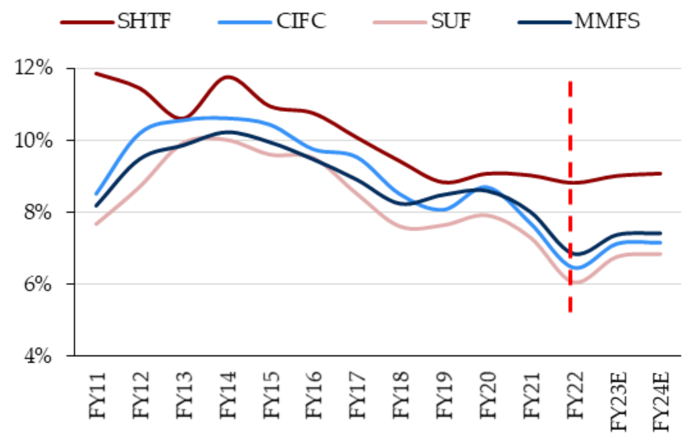


Source: Company, HSIE Research

- **Rising cost of funds to keep improving spreads under check:** The increasing interest rate environment with sharp repo rate hikes of 90bps (and expected further rate hikes) as well as increasing yields in the bond market are likely to drive cost of funds of vehicle NBFCs under coverage higher by ~50-70bps.

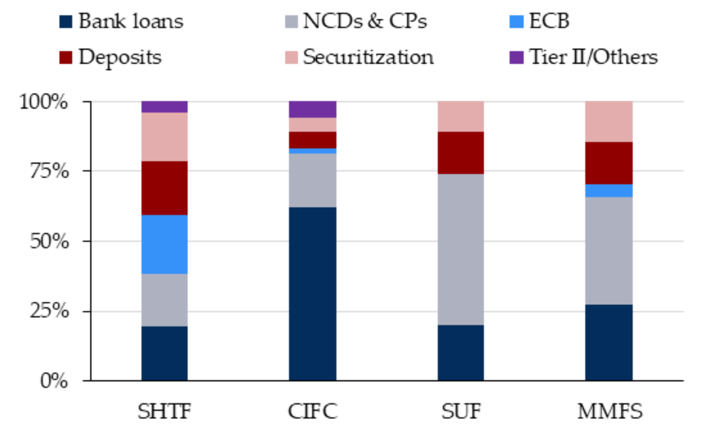
  NBFCs competing with banks such as Sundaram Finance are likely to witness higher pressure on NIM compared to NBFCs with relatively benign competitive intensity in their respective segments such as SHTF, CIFC, etc.

Exhibit 98: Cost of funds expected to inch up



Source: Company, HSIE Research

Exhibit 99: Funding mix (Mar-22)



Source: Company, HSIE Research

- **Increasing regulatory cost at the margin:** RBI's increasing enhanced regulations for NBFCs, post the IL&FS and DHFL crisis, is likely to impact the profitability at the margin. Scale-based regulations are likely to impact most NBFCs under coverage, although the impact is likely to be gradual.

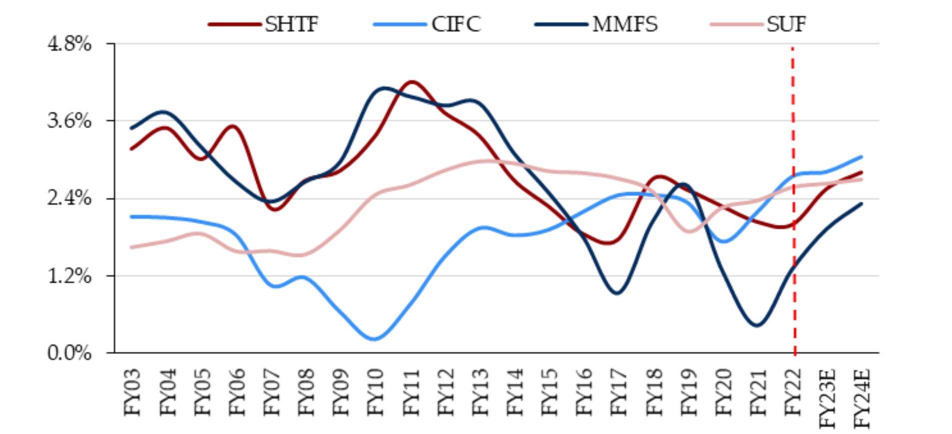
Exhibit 100: Revision in regulations for NBFCs bringing them gradually near par with banks

	NBFCs	Banks
Capital adequacy norms	Tier I of 12%; CRAR of 15%	CET I of 7.375%; CRAR of 10.875%
LCR norms	60% by Dec-21; 100% by Dec-24	100% for Universal Banks
PCA framework	Threshold I, II, III	Threshold I, II, III
CRAR	12 - 15%; 9 - 12%; < 12%	8.375 - 10.875%; 6.875 - 8.375%; <6.875%
Tier I/CET-I	8 - 10%; 6-8%; <6%	5.75% - 7.375%; 5.24% - 5.75%; < 5.24%
Net NPA	6-9%; 9-12%; >12%	6-9%; 9-12%; >12%
Leverage Ratio Shortfall	NA	< 50bps; 50-100bps; > 100bps
IRAC norms		
90dpd recognition	YES	YES
Daily tagging of NPA	YES	YES
NPA up gradation criteria	Full recoveries	Full recoveries
Investments in Technology		
Core-Banking Solution	For UL and ML NBFCs	For All
Customer protection		
Ombudsman Scheme	YES	YES

Source: RBI, HSIE Research

- **Healthy cross-cycle profitability, growth contingent on underlying asset growth:** CV financing NBFCs have delivered superior RoA over several cycles (~2.5% - 3%). However, the high cyclical coefficient of the underlying asset class has led to volatility in earnings as well as loan growth, particularly in used CV financing. As the COVID pandemic has largely subsided, we expect vehicle financing NBFCs to revert to steady-state profitability.

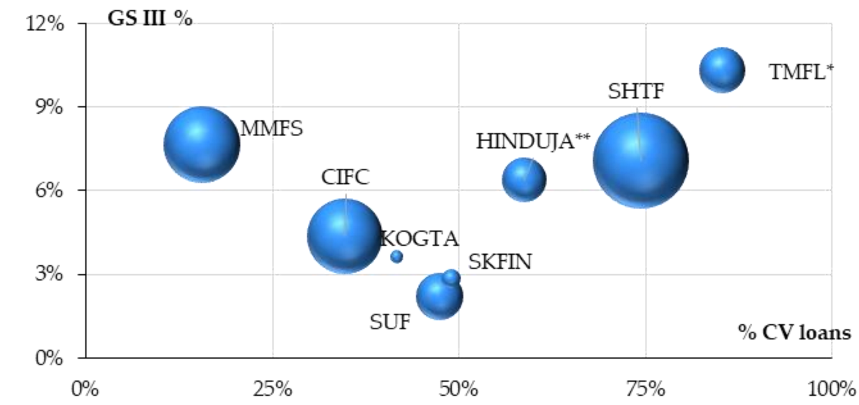
Exhibit 101: Cross-cycle ROA of leading vehicle NBFCs



Source: Company, HSIE Research

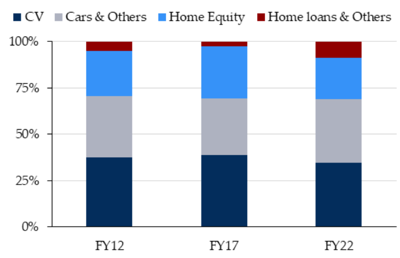
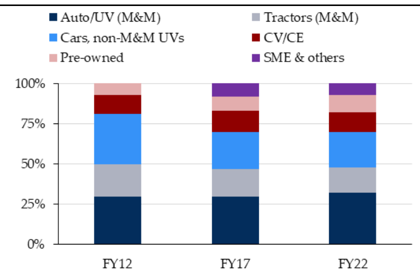
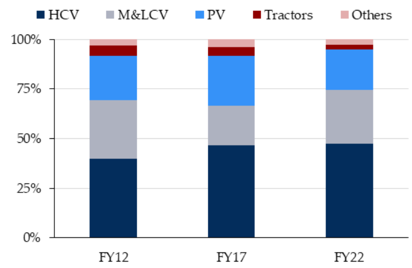
- **De-coupling the balance sheet with high cyclical coefficient of vehicle financing:** Leading CV financing NBFCs are increasingly seeking asset diversification towards non-vehicle portfolio in order to de-risk their portfolios from volatility in asset quality and portfolio growth. SHTF merger with its sister concern Shriram City Union Finance (MSME, 2W lending) has already received RBI approval. Chola Finance (CIFC) has introduced new categories of products targeted at retail and MSME segment – personal and business loans (secured and unsecured). Mahindra Finance (MMFS) is seeking to leverage its promoter strengths to increase MSME and supply chain financing and cross-sell non-vehicle loans to its customers.

Exhibit 102: CV financing NBFCs (Mar-22)



Source: Company, HSIE Research | *Note: Size of the balloon indicates total AUM; * % of disbursements; ** Share of CV loans as on Mar-21*

Exhibit 103: AUM mix

CIFC	MMFS	SHTF
		

Source: Company, HSIE Research

Exhibit 104: Diversification roadmap by various CV financiers

CIFC	MMFS	SHTF
Introduced 3 new lines of businesses: • SME loans • Secured Business loans (SBPL) • Personal loans & Business loans (unsecured) (CSEL)	• Focus on non-core business segments • Supply chain financing in collaboration with the parent entity • Personal and other loans for rural/semi-urban customers	• Merger with Shriram City Union Finance • SCUF loan mix (Mar-22): MSME: 26%; Gold loans: 26%; 2W: 21%; PL: 17%; Others: 5%

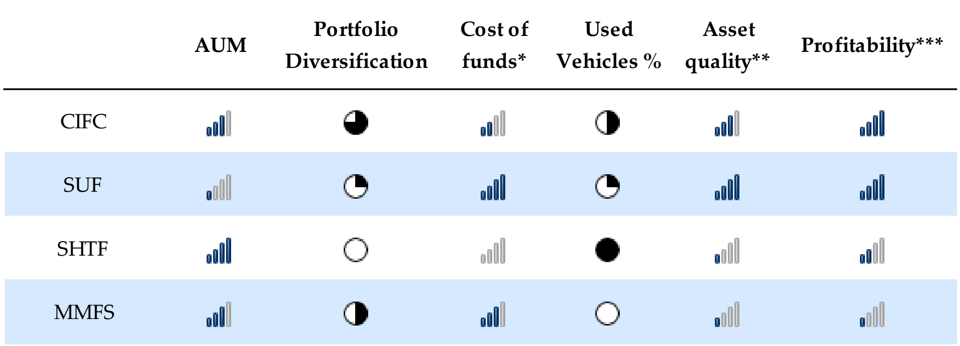
Source: Company, HSIE Research

- **Diversification—easier said than done:** Diversification into newer product/customer segments is likely to be fraught with several execution challenges, especially where the right-to-win is not explicitly visible. Further, the profitability of the new product categories is likely to take time to mature, leading to a drag on overall profitability.

  Bajaj Finance is one of the very few captive financiers that have been able to diversify their loan books across secured and unsecured lending; it has a sub-5% share of OEM in its loan book.

- **Initiate coverage on SUF with a BUY; CIFC remains our top pick:** We initiate coverage on Sundaram Finance (SUF) with a BUY rating and SoTP-based TP of INR 2,360 (standalone entity at 2.4x Mar-24 ABVPS). SUF remains a high-quality franchise with a prominent presence in the "bankable" new CV segment of fleet operators, along with pristine asset quality across cycles. Chola Finance (CIFC) remains our top pick, with a TP of INR790; the company is well-poised to accelerate on growth as profitability remains intact.

Exhibit 105: HSIE CV financing dashboard (NBFCs)



Source: Company, HSIE Research | *Note: On each parameter, a fuller bar indicates a superior franchise; AUM, portfolio diversification and used vehicles mix as on Mar-22; *Average cost of funds during FY13-FY22; **Average credit costs during FY13-FY22; *** Average RoE during FY13-FY22*

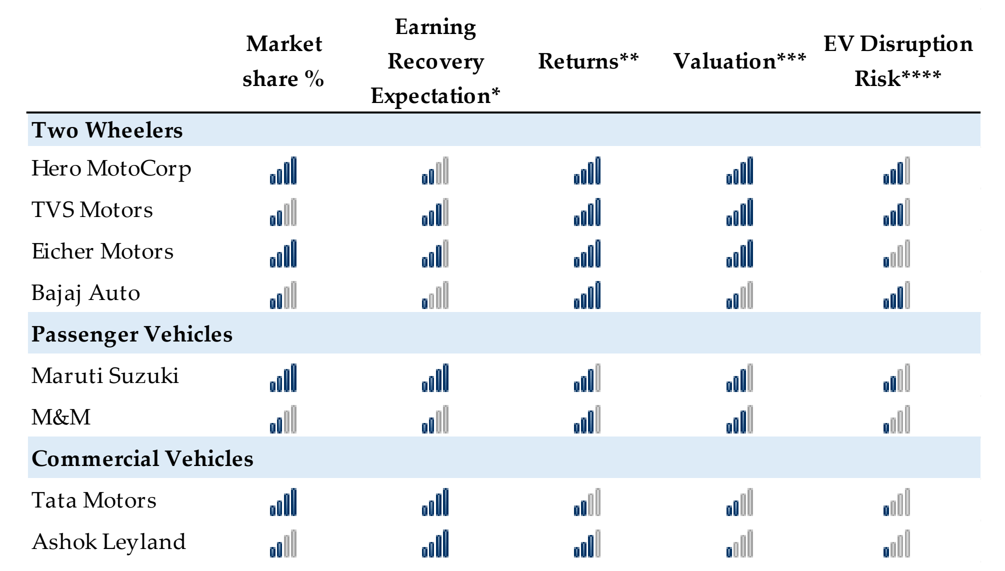
Exhibit 106: Vehicle financing NBFCs – Valuation summary

	Rating	TP (INR)	P/ABV (x)			RoAE (%)			RoAA (%)		
			FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
CIFC	BUY	790	5.8	4.6	3.8	20.2	19.5	20.5	2.7	2.8	3.0
MMFS	ADD	215	1.6	1.5	1.3	6.5	9.9	13.1	1.3	1.9	2.3
SHTF	ADD	1,554	1.9	1.6	1.5	11.4	13.7	14.5	2.0	2.6	2.8
SUF	BUY	2,360	3.4	3.0	2.7	13.8	13.6	14.2	2.6	2.6	2.7

Source: Company, HSIE Research; *CMP as on 25-July-2022*

- **Auto OEMs investment implications:** On India Autos, we expect auto demand (across segments) to revive on a low base relative to the peak of FY19, led by a pick-up in economic growth and expected rural revival. We factor in 17/16/18% volume CAGR for 2Ws/PVs/CVs over FY22-24E. We also expect strong recovery in earnings for all OEMs on the back of softening commodity prices and a gradual easing of supply constraints. Our top picks are TVS Motors (BUY: sustained outperformance), Hero MotoCorp (BUY: volume revival + attractive valuation) and M&M (BUY: mojo back in UVs + value unlocking driving re-rating). We also like Maruti Suzuki and Eicher Motors (both ADD; earnings growth to be driven by operating leverage). Our top SELL in the sector is Ashok Leyland (consensus earnings downgrade cycle likely to continue). We recommend trimming exposure on Tata Motors and Bajaj Auto (both REDUCE) as we believe most of the positives are already factored in.

Exhibit 107: HSIE Auto dashboard



Source: Company, Industry, HSIE Research | *Note: * PAT CAGR – FY22-FY24E; ** FY24 RoE; *** PEG ratio based on FY24 P/E and 2-year PAT CAGR; **** High implies more prone to EV transition*

Exhibit 108: Auto companies – Valuation summary

Company	Rating	TP	Mcap (INR bn)	EBITDA Margin %		EPS CAGR %	P/E (x)		EV/EBITDA (x)		ROE (%)	
				FY23E	FY24E	FY22-24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
AL	SELL	102	432	6.0	9.0	NA	86.0	31.9	24.4	14.3	6.5	15.6
BJAUT	REDUCE	3,677	1,163	17.0	17.5	17.7	21.0	18.2	14.5	12.5	20.6	22.5
EIM	ADD	3,118	843	23.0	25.0	39.6	34.4	25.8	23.7	18.0	16.9	19.1
HMCL	BUY	3,268	567	12.0	13.7	29.2	18.1	13.7	10.3	7.9	18.1	21.2
MM	BUY	1,390	1,362	13.1	13.5	21.4	20.3	18.1	11.3	9.7	15.2	15.0
MSIL	ADD	8,957	2,601	9.4	10.5	66.2	33.6	25.0	20.7	15.0	13.6	16.5
TTMT	REDUCE	398	1,721	12.8	14.5	NA	NA	27.4	6.3	4.8	NA	12.3
TVSL	BUY	988	414	9.8	11.2	34.7	32.5	24.7	14.9	11.5	21.8	23.4

Source: Company, HSIE Research | *CMP as on 25-July-2022*

Sundaram Finance

Virtuous cycle drives flywheel effect

On the back of a significant cost leadership advantage, Sundaram Finance (SUF) is a high-quality franchise with a stellar record on pristine cross-cycle asset quality and profitability (core RoE of ~18%). SUF has established a formidable "right-to-win" in the "bankable" new M&HCV segment in core geographies on the back of deep relationships with large fleet operators, reflecting in increasing proportion of repeat business and superior pricing power. SUF is poised to drive the strong CV upcycle, delivering ~14% loan CAGR through increased product and geographic diversification, although the rising rate cycle is likely to keep incremental spreads under check. The subsidiaries are gradually gaining scale and contribute ~24% to the SoTP. We initiate coverage on SUF with a BUY and SoTP-based TP of INR 2,360 (standalone entity at 2.4x Mar-24 ABVPS).

- **Disciplined underwriting drives pristine asset quality:** Sundaram Finance (SUF) has established a formidable "right-to-win" in the core CV segment (~46% of AUM), particularly in the "bankable" large fleet operators segment, reflected in over 2/3rd repeat customers (loyal borrower base). With its prudent approach to underwriting and consistent exercising of pricing power, SUF has delivered pristine asset quality even during cyclical downturns, ahead of its peers.
- **Poised to ride the CV upcycle; prudent on growth:** SUF is well-positioned for strong loan growth, with an imminent upcycle in its core new M&HCV financing segment (~18% industry growth expected during FY22-FY24E), coupled with a revival in the PV financing business. The geographical diversification beyond the core southern market (non-South at ~43% of AUM vs. 35% in Mar-18) is likely to provide further fillip to loan growth.
- **Best-in-class cost of funds:** SUF's stellar track record and parentage drives a superior credit rating (CRISIL AAA stable) and lowest cost of funds among peers (average of 7.3% during FY18-FY22), enabling the company to compete with banks and captive financiers in its core "Prime Plus" segment. However, the rising rate cycle is likely to drive incremental cost of funds higher for SUF, keeping the blended spreads under check.
- **Subsidiaries value unlocking**: SUF's subsidiaries, Sundaram Home Finance and Sundaram AMC, are gradually gaining scale with sustained profitability, while Royal Sundaram GI's combined ratio continues to hover over ~110%. The three subsidiaries contribute ~24% to the SoTP-based TP.
- **Best-in-class franchise; initiate with a BUY and TP at INR2,360:** SUF remains a high-quality franchise in our view with best-in-class asset quality and sustained profitability. We expect SUF to deliver AUM growth of ~14% during FY22-FY24E and average core RoE of ~18%.

Financial summary

(INR bn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
NII	10.5	11.8	13.3	14.4	16.9	17.0	19.8
PPOP	9.4	10.0	12.3	13.7	15.0	15.1	17.5
PAT	5.6	5.3	7.2	8.1	9.0	9.9	11.5
EPS (INR)	50.7	48.1	65.2	72.8	81.3	89.1	103.4
ROAE (%)	14.3	11.6	13.7	13.8	13.8	13.6	14.2
ROAA (%)	2.5	1.9	2.3	2.4	2.6	2.6	2.7
ABVPS (INR)	359.0	433.4	457.6	520.1	587.7	656.9	737.7
P/ABV (x)	5.5	4.6	4.3	3.8	3.4	3.0	2.7
P/E (x)	39.2	41.3	30.5	27.3	24.4	22.3	19.2

Source: Company, HSIE Research

BUY

CMP *(as on 25 Jul 2022)*	INR 1,989
Target Price	INR 2,360
NIFTY	16,631

KEY STOCK DATA	
Bloomberg code	SUF IN
No. of Shares (mn)	111
MCap (INR bn) / ($ mn)	221/2,969
6m avg traded value (INR mn)	160
52 Week high / low	2,699/1,555

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	(1.9)	(10.7)	(22.9)
Relative (%)	(0.5)	(7.1)	(28.2)

SHAREHOLDING PATTERN (%)

	Dec-21	Mar-22
Promoters	35.9	38.5
FIs & Local MFs	11.8	14.3
FPIs	12.4	9.9
Public & Others	39.1	37.3
Pledged Shares	0	0

Source : BSE

Pledged shares as % of total shares

Deepak Shinde
deepak.shinde@hdfcsec.com
+91-22-6171-7323

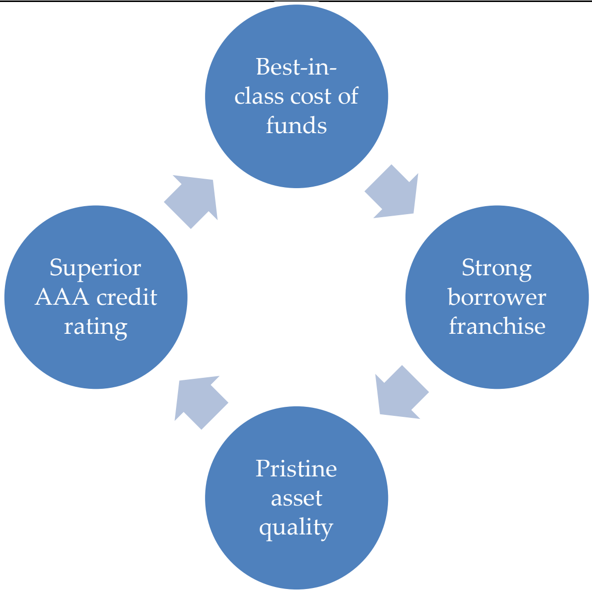
Krishnan ASV
venkata.krishnan@hdfcsec.com
+91-22-6171-7314

Neelam Bhatia
neelam.bhatia@hdfcsec.com
+91-22-6171-7341

Sahej Mittal
sahej.mittal@hdfcsec.com
+91-22-6171-7325

Cost leadership drives virtuous cycle

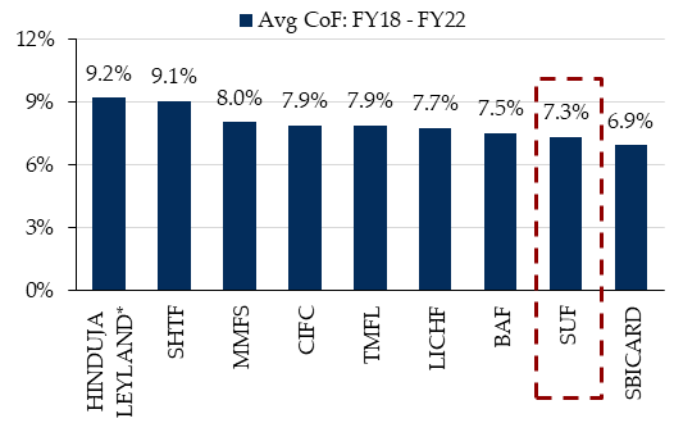
Exhibit 109: Virtuous cycle in play for Sundaram Finance



Source: Company, HSIE Research

- **Superior cost of funds amongst peers**: SUF's parentage alongside stellar long-term track record drives high creditworthiness rating from rating agencies (CRISIL: AAA stable), at par with the leading NBFCs such as Bajaj Finance and SBI Cards. This has led to SUF benefiting from one of the lowest funding costs in the industry, enabling the company to selectively compete with banks in target customer and product segments.

Exhibit 110: Cost of funds lowest after SBI Cards



Source: Company, HSIE Research | Note: * *average of FY18 to FY21*

Exhibit 111: Long-term ratings of select NBFCs

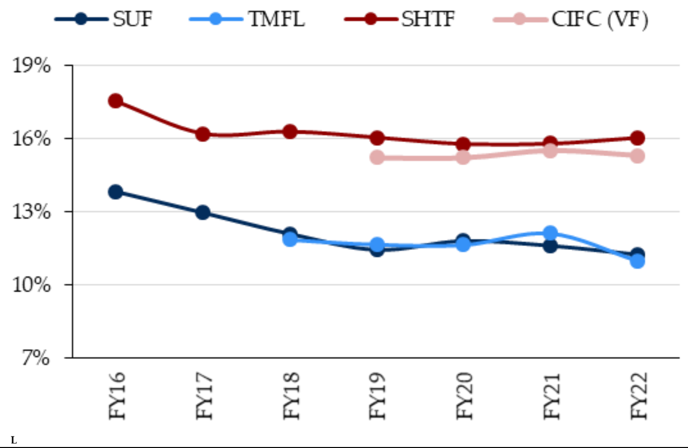
Company	Rating
SUF	**AAA Stable**
SHTF	AA+ Stable
CIFC	AA+ Stable
MMFS	AA+ Stable
TMFL	AA- Stable
HINDUJALEYLAND	AA- Stable
BAF	AAA Stable
LICHF	AAA Stable
SBICARD	AAA Stable

Source: CRISIL, HSIE Research | *As on 30-Jun-2022*

- **Maintaining pricing power in the core segment:** Sundaram Finance (SUF) has maintained its prominence and an established "right-to-win" in the core CV segment (~46% of AUM), particularly in the "bankable" fleet operators segment. SUF's deep understanding of its customers (fleet operators) has driven strong relationship leading to high customer stickiness over the years despite exercising of pricing power.

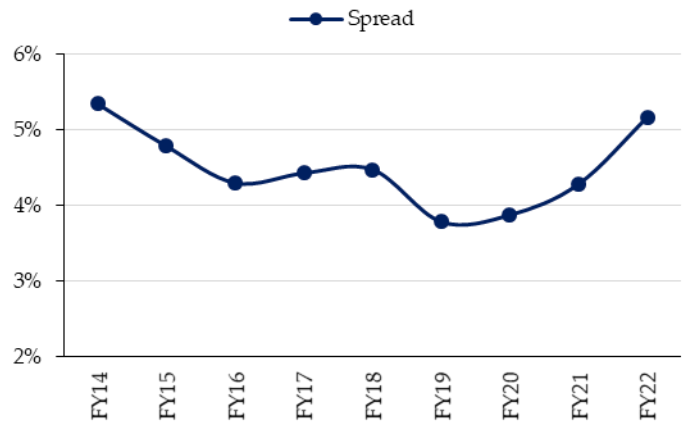
SUF competes primarily with banks and captive financiers such as Tata Motors Finance in the new CV financing segment. The yields have remained fairly steady with spreads of ~4-5%, far lower than the peers, CIFC and SHTF, due to customer segments of choice.

Exhibit 112: Asset yields for Sundaram Finance vs. peers



Source: Company, HSIE Research | *Note: Transition to IND AS from FY18 onwards*

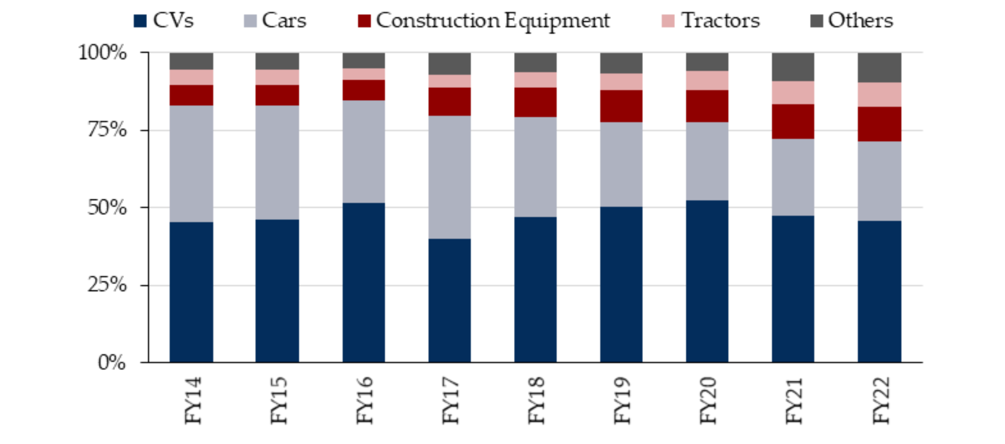
Exhibit 113: Core spreads have remained healthy in ~4-5% range



Source: Company, HSIE Research

SUF's product portfolio to fleet operators, apart from fleet financing, includes fuel and tyre financing, which are two of the highest variable expenses (after driver salary expenses). The company has gradually diversified from core M&HCV segment to ICV/LCV financing and car financing (~90% new vehicles) that aids loan growth during a cyclical downturn. Used vehicles comprise ~15% of AUM as on Mar-22.

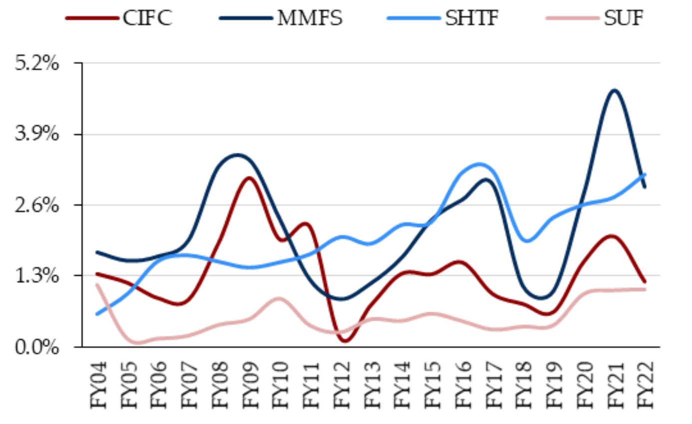
Exhibit 114: Loan mix has remained fairly steady



Source: Company, HSIE Research

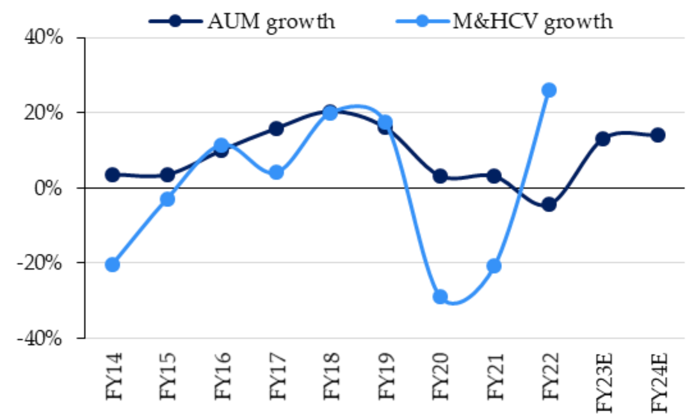
- **Pristine asset quality across cycles:** SUF's prudent approach towards growing its balance sheet in a calibrated manner has led to pristine asset quality compared to peers in an inherently volatile asset class. This is getting reflected in muted credit costs across cycles, driving superior profitability.

Exhibit 115: Credit costs have remained best-in-class across cycles



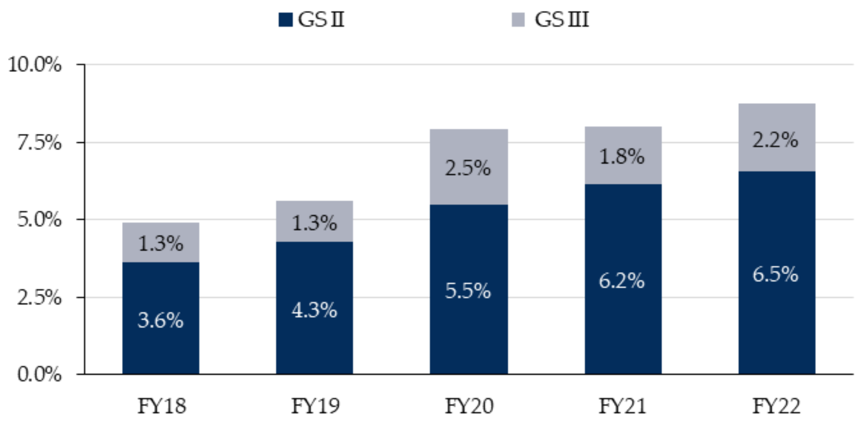
Source: Company, HSIE Research

Exhibit 116: Loan growth in line with industry M&HCV sales growth



Source: Company, HSIE Research | *Note: M&HCV growth – sales volumes growth for the industry*

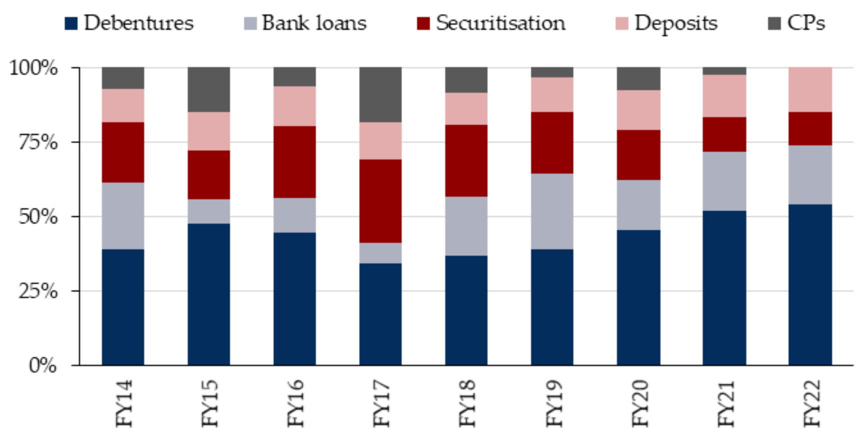
Exhibit 117: Early delinquencies inched up during the pandemic



Source: Company, HSIE Research

- **Rising cost of funds—near-term headwind:** The increasing interest rate environment with sharp repo rate hikes of 90bps (and expected further rate hikes) as well as increasing yields in the bond market are likely to drive cost of funds higher for SUF. With a large fixed-rate loan book and higher competitive intensity in customer segments, the spreads are likely to come under pressure in the near term.

Exhibit 118: Funding mix %



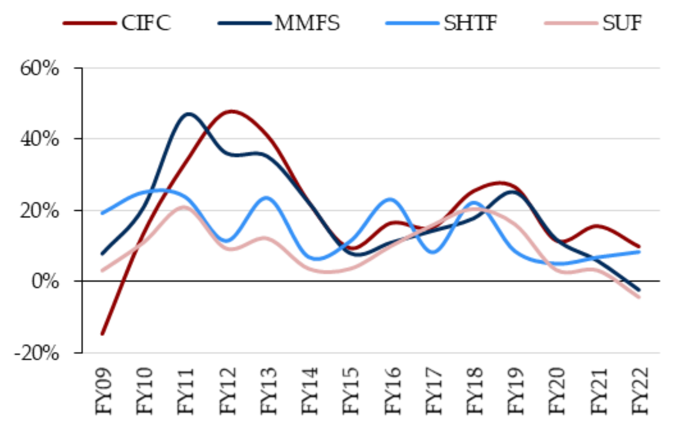
Source: Company, HSIE Research

Flywheel effect in place; initiate with a BUY

- **Demand on an upswing, geographic expansion to add more leg room for growth**: SUF is poised for strong loan growth with expected up cycle in the core M&HCV segment, along with revival in the PV segment. The geographical diversification beyond the core Southern market, is likely to provide further fillip to the loan growth.

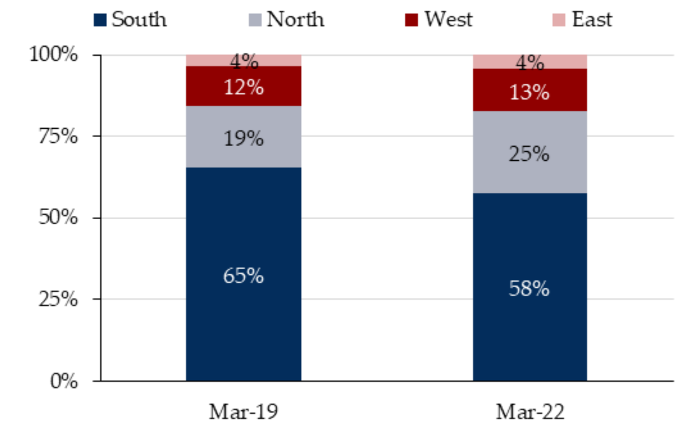
  However, SUF is likely to sustain its calibrated approach to growth in newer geographies riding on the back of select customer segments (for e.g., large and mid-size fleet operators).

Exhibit 119: Steady AUM growth over the years



Source: Company, HSIE Research

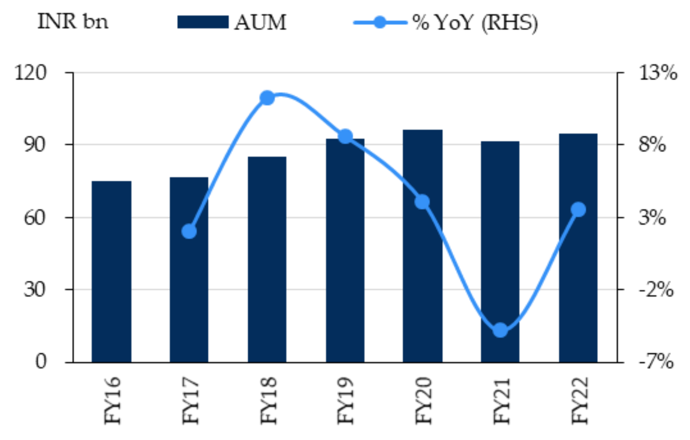
Exhibit 120: AUM mix: increasing non-South exposure



Source: Company, HSIE Research

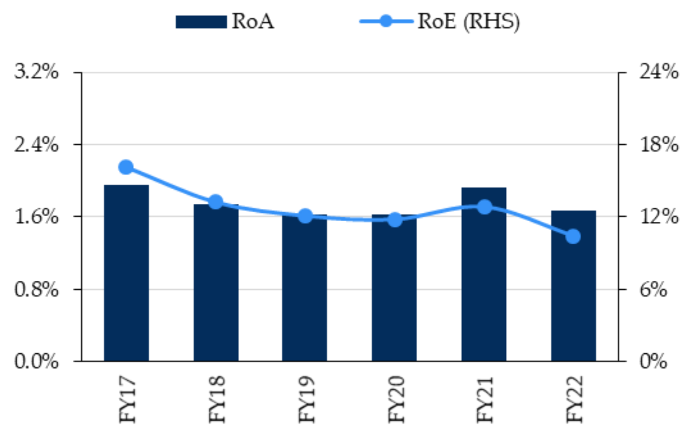
- **Housing finance subsidiary—steady profitability, muted on growth:** Sundaram Home Finance, a wholly-owned subsidiary of Sundaram Finance, continues to perform steadily in terms of profitability as it did even during the pandemic period. However, growth continues to remain tepid since FY19 and it's expected to witness some revival in FY23.

Exhibit 121: Muted AUM growth



Source: Company, HSIE Research

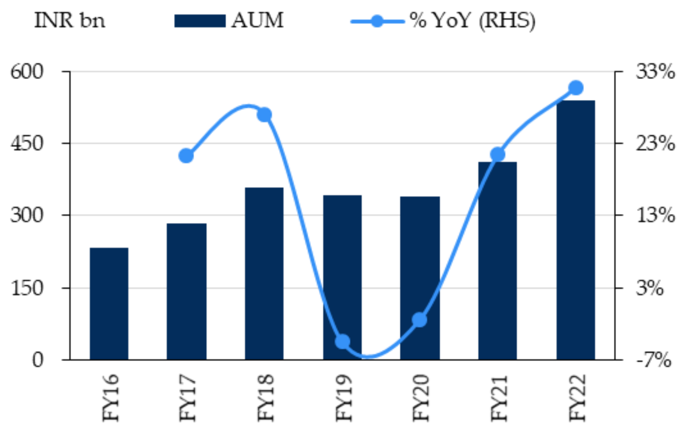
Exhibit 122: Steady profitability, even during Covid pandemic



Source: Company, HSIE Research

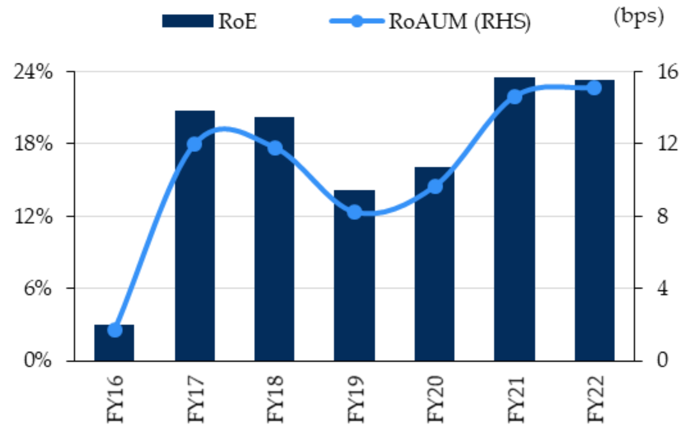
- **AMC business:** Sundaram Asset Management Company, another wholly-owned subsidiary of Sundaram Finance, witnessed a sharp uptick in AUM in FY21 and FY22, partly driven by the Principal AMC acquisition (AUM of ~INR100bn).

Exhibit 123: AUM growth gets a fillip with Principal AMC acquisition during FY22



Source: Company, HSIE Research

Exhibit 124: Healthy RoE; muted on return on AUM



Source: Company, HSIE Research

- **Initiate with BUY, SoTP-based TP at INR 2,360:** We initiate coverage on SUF with a BUY rating and SoTP-based TP of INR 2,360. Our implied multiple for the core NBFC is at 2.4x Mar-24 ABVPS, while the housing finance subsidiary Sundaram Home Finance is valued at 1.5x Mar-24 ABVPS.

Exhibit 125: SoTP-based valuation

	Value (INR mn)	% Stake	Per share (INR)	% of TP	Valuation Methodology
SUF (standalone, Mar-24 ABV)	195,665	100%	1,761	75%	RI-based
Sundaram Home Finance	27,506	100%	248	10%	1.5x Mar-24 ABVPS
Sundaram AMC	37,497	100%	337	14%	5% of Mar-24 AUM
Sundaram Finance Holdings	17,280	21.6%	34	1%	CMP
Royal Sundaram General Insurance	28,739	50%	129	5%	12x FY23 EPS
Total value of subsidiaries			**748**	**32%**	
Less: Holding company discount			150	6%	20% Hold co discount
Total SoTP valuation			**2,360**	100%	

Source: Company, HSIE Research

Financials

Income Statement

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest earned	23,937	29,379	34,064	34,713	33,945	37,129	42,969
Interest expended	13,460	17,625	20,720	20,307	17,001	20,120	23,152
Net interest income	**10,477**	**11,754**	**13,344**	**14,406**	**16,944**	**17,009**	**19,818**
Other income	4,617	4,803	5,205	5,429	4,960	5,450	5,830
Total income	15,094	16,557	18,549	19,835	21,904	22,459	25,647
Operating expenditure	5,742	6,531	6,234	6,111	6,949	7,347	8,159
Pre-provisioning operating profit	**9,352**	**10,026**	**12,315**	**13,724**	**14,954**	**15,112**	**17,488**
Non-tax provisions	855	1,073	2,864	3,161	3,185	1,878	2,133
Profit before tax	8,497	8,953	9,451	10,563	11,769	13,233	15,355
Tax expenditure	2,863	3,614	2,212	2,473	2,735	3,335	3,870
Profit after tax	5,634	5,339	7,239	8,090	9,034	9,898	11,486

Source: Company, HSIE Research

Balance Sheet

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share capital	1,111	1,111	1,111	1,111	1,111	1,111	1,111
Reserves and surplus	40,225	49,327	54,363	60,683	67,820	75,475	84,516
Net worth	41,359	50,467	55,498	61,795	68,931	76,586	85,627
Borrowings	211,092	250,058	273,367	282,134	278,353	316,133	360,201
Other liabilities and provisions	5,679	5,996	5,354	5,596	5,592	6,544	7,462
Total equity and liabilities	**258,107**	**306,492**	**334,195**	**349,525**	**352,875**	**399,263**	**453,290**
Cash and cash equivalents	9,821	8,386	6,298	6,932	6,171	8,283	11,395
Investments	22,068	18,663	39,377	40,524	53,187	51,281	54,944
Advances	220,030	272,715	280,447	294,039	284,002	329,713	375,937
Fixed assets	2,941	3,051	3,596	3,309	3,604	3,785	3,974
Other assets	3,247	3,676	4,477	4,721	5,911	6,202	7,041
Total assets	**258,107**	**306,492**	**334,195**	**349,525**	**352,875**	**399,263**	**453,290**

Source: Company, HSIE Research

Key Ratios

	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
VALUATION RATIOS							
EPS	50.7	48.1	65.2	72.8	81.3	89.1	103.4
Earnings Growth (%)	13.7%	-5.2%	35.6%	11.8%	11.7%	9.6%	16.0%
BVPS (ex reval.)	372	454	499	556	620	689	771
Adj. BVPS (ex reval. & 100% cover)	359	433	458	520	588	657	738
ROAA (%)	2.5%	1.9%	2.3%	2.4%	2.6%	2.6%	2.7%
ROAE (%)	14.3%	11.6%	13.7%	13.8%	13.8%	13.6%	14.2%
P/E (x)	39.2	41.3	30.5	27.3	24.4	22.3	19.2
P/ABV (x)	5.5	4.6	4.3	3.8	3.4	3.0	2.7
P/PPOP (x)	23.6	22.0	17.9	16.1	14.8	14.6	12.6
Dividend yield (%)	0.6%	0.9%	0.7%	0.9%	1.0%	1.0%	1.1%
PROFITABILITY (%)							
Yield on Advances (%)	12.1%	11.4%	11.8%	11.6%	11.2%	11.5%	11.6%
Cost of Funds (%)	7.6%	7.6%	7.9%	7.3%	6.1%	6.8%	6.8%
Core Spread (%)	4.5%	3.8%	3.9%	4.3%	5.2%	4.8%	4.7%
NIM (% of AUM)	4.6%	4.4%	4.5%	4.7%	5.6%	5.4%	5.5%
OPERATING EFFICIENCY							
Cost to average AUM ratio (%)	2.5%	2.4%	2.1%	2.0%	2.3%	2.3%	2.3%
Cost-income ratio (%)	38.0%	39.4%	33.6%	30.8%	31.7%	32.7%	31.8%
BALANCE SHEET STRUCTURE RATIOS							
Loan growth (%)	40.1%	23.9%	2.8%	4.8%	-3.4%	16.1%	14.0%
AUM growth (%)	20.4%	16.1%	3.3%	3.2%	-4.4%	13.1%	14.1%
Borrowing growth (%)	48.0%	18.5%	9.3%	3.2%	-1.3%	13.6%	13.9%
Debt/Equity (x)	5.7	5.6	5.6	5.2	4.7	4.7	4.8
Equity/Assets (%)	16.0%	16.5%	16.6%	17.7%	19.5%	19.2%	18.9%
Equity/Loans (%)	18.8%	18.5%	19.8%	21.0%	24.3%	23.2%	22.8%
Total Capital Adequacy Ratio (CAR) (%)	18.0%	19.5%	18.4%	22.1%	24.4%	23.8%	23.4%
Tier I CAR (%)	12.5%	14.7%	13.2%	15.2%	17.5%	17.7%	18.1%
ASSET QUALITY							
Gross NPL (INR mn)	2,830	3,666	7,013	6,831	7,035	6,943	7,406
Net NPL (INR mn)	1,454	2,285	4,636	4,009	3,636	3,600	3,666
Gross NPL (%)	1.3%	1.3%	2.5%	1.8%	2.2%	2.1%	2.0%
Net NPL (%)	0.7%	0.8%	1.7%	1.0%	1.1%	1.1%	1.0%
Coverage Ratio (%)	48.6%	37.7%	33.9%	45.7%	52.0%	48.1%	50.5%
Provision/Avg. AUM (%)	0.4%	0.4%	1.0%	1.0%	1.1%	0.6%	0.6%
DUPONT ANALYSIS							
Interest earned	10.6%	10.4%	10.6%	10.2%	9.7%	9.9%	10.1%
Interest expended	6.0%	6.2%	6.5%	5.9%	4.8%	5.4%	5.4%
Net interest income	**4.7%**	**4.2%**	**4.2%**	**4.2%**	**4.8%**	**4.5%**	**4.6%**
Non-interest income	2.1%	1.7%	1.6%	1.6%	1.4%	1.4%	1.4%
Operating expenses	2.6%	2.3%	1.9%	1.8%	2.0%	2.0%	1.9%
Pre-provisioning profit	4.2%	3.6%	3.8%	4.0%	4.3%	4.0%	4.1%
Provisions	0.4%	0.4%	0.9%	0.9%	0.9%	0.5%	0.5%
Tax	1.3%	1.3%	0.7%	0.7%	0.8%	0.9%	0.9%
ROAA	**2.5%**	**1.9%**	**2.3%**	**2.4%**	**2.6%**	**2.6%**	**2.7%**
Leverage (x)	5.7	6.1	6.0	5.8	5.4	5.2	5.3
ROAE	**14.3%**	**11.6%**	**13.7%**	**13.8%**	**13.8%**	**13.6%**	**14.2%**

Source: Company, HSIE Research

Cholamandalam Investment and Finance Company

Quality franchise poised for strong growth

Cholamandalam Investment and Finance Company (CIFC) is positioned as a high-quality franchise that combines strong growth with sustained profitability. With the CV and PV cycle poised for a strong up-cycle, CIFC is well-positioned for strong growth, while sustaining its profitability (RoA of ~2.7%). CIFC is further adding new growth engines to its non-vehicle book targeted at SMEs, small businesses and professionals, through its own distribution network as well as Fintech partnerships. While the management has indicated little change to existing RoA, we await evidence on CIFC's right-to-win and ability to deliver superior profitability in these segments. CIFC remains our top pick in the sector with its superior execution on profitability and calibrated loan growth and maintain a BUY with a TP of INR 790 (4.3x Mar-24 ABVPS).

- **Core vehicle financing portfolio poised for strong growth:** CIFC remains well positioned in its core vehicle financing segment (SRTOs/individual truck owners in LCV/ICV segment) to benefit from the strong up cycle in CVs and PVs. The pricing power is apparent with steady yield at ~15% in a declining interest rate environment with stable portfolio mix. The portfolio continues to deliver superior profitability (~3% RoA) and is expected to deliver AUM growth of ~18% CAGR during FY22-FY24E. The segment remains fairly diversified across products (highest exposure of LCVs at ~21% of vehicle finance AUM) in a cyclical asset class.
- **Non-vehicle finance book gaining traction:** The share of non-vehicle portfolio is gradually gaining traction with 31% of AUM vs. 25% in FY19, with relative acceleration in home loans. Going ahead, we expect the share of LAP and home loans to remain steady as vehicle finance growth picks up.
- **Adding new growth engines**: CIFC has sought to add multiple levers for growth with launch of three new segments during FY22 targeted at SME, small business enterprises and consumers (largely professionals). While the management has indicated negligible RoA dilution on a steady state basis, we await evidence of CIFC's "right-to-win" in terms of growth and superior RoA in these segments.
- **Asset quality mean reverting with steady-state credit costs**: Despite surging early delinquencies bucket (GS-II) in Q1FY22, CIFC's portfolio continued to deliver strong profitability (average RoA of 2.2% during FY20-FY22) with healthy provisioning. The revival in economic activity and CIFC's superior credit underwriting led to negligible surge in credit costs during the pandemic. We expect credit costs to remain at ~1.2% during FY23-FY24E.
- **Remains top pick among NBFCs:** We expect CIFC to deliver AUM growth CAGR of ~18% during FY22-FY24E and average RoE of ~20% during the same period. We maintain our BUY rating on CIFC, with a TP of INR 790 (4.3x Mar-24 ABVPS).

Financial summary

(INR bn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
NII	25.9	30.4	35.3	46.5	52.7	59.3	70.5
PPOP	17.1	21.3	24.8	33.6	37.7	44.1	53.6
PAT	9.2	11.9	10.5	15.1	21.5	25.1	31.7
EPS (INR)	58.7	75.8	12.8	18.5	26.1	30.6	38.6
ROAE (%)	19.5	21.0	14.7	17.1	20.2	19.5	20.5
ROAA (%)	2.5	2.3	1.7	2.2	2.7	2.8	3.0
ABVPS (INR)	283.1	337.8	84.2	98.2	117.9	148.1	182.3
P/ABV (x)	2.4	2.0	8.1	7.0	5.8	4.6	3.8
P/E (x)	11.7	9.0	53.4	37.1	26.3	22.5	17.8

Source: Company, HSIE Research

BUY

CMP *(as on 25 Jul 2022)*	INR 685
Target Price	INR 790
NIFTY	16,631

KEY STOCK DATA	
Bloomberg code	CIFC IN
No. of Shares (mn)	821
MCap (INR bn) / ($ mn)	563/7,560
6m avg traded value (INR mn)	1,685
52 Week high / low	770/469

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	(4.2)	6.4	37.2
Relative (%)	(2.8)	10.0	32.0

SHAREHOLDING PATTERN (%)

	Mar-22	Jun-22
Promoters	51.6	51.5
FIs & Local MFs	23.0	22.4
FPIs	17.6	18.0
Public & Others	7.8	8.1
Pledged Shares		0.0

Source : BSE

Pledged shares as % of total shares

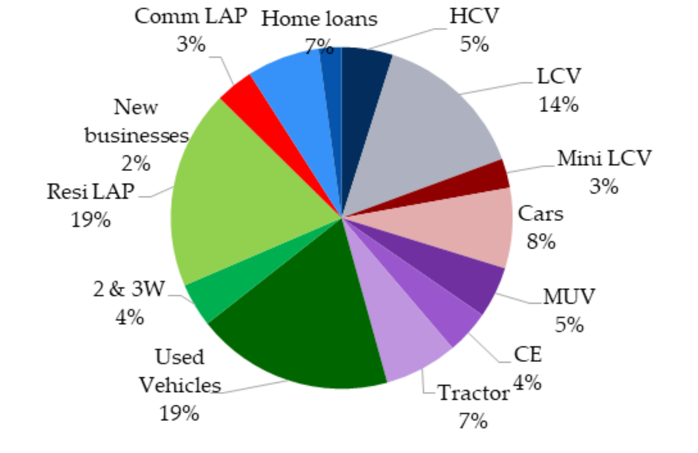
Deepak Shinde
deepak.shinde@hdfcsec.com
+91-22-6171-7323

Krishnan ASV
venkata.krishnan@hdfcsec.com
+91-22-6171-7314

Neelam Bhatia
neelam.bhatia@hdfcsec.com
+91-22-6171-7341

Sahej Mittal
sahej.mittal@hdfcsec.com
+91-22-6171-7325

Exhibit 126: AUM mix—fairly diversified (Mar-22)



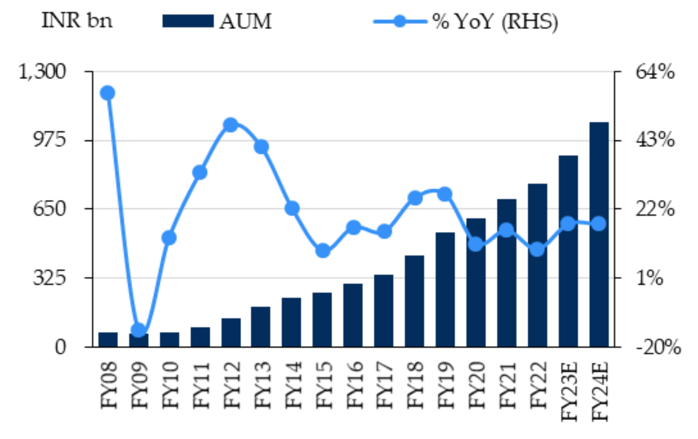
Source: Company, HSIE Research

Exhibit 127: Segmental RoA tree (average of FY21-FY22)

On AUM (avg of FY21-FY22)	Vehicle Finance	Home Equity	Home loans	Total
Total Income	15.4%	11.8%	14.2%	13.9%
Cost of Funds	7.1%	7.2%	6.9%	6.3%
NIM	8.3%	4.7%	7.3%	7.6%
Opex	3.0%	1.1%	2.3%	2.6%
Provisions	2.0%	0.9%	1.2%	1.6%
PBT	3.4%	2.7%	3.8%	3.5%
PAT	**2.5%**	**2.0%**	**2.8%**	**2.6%**

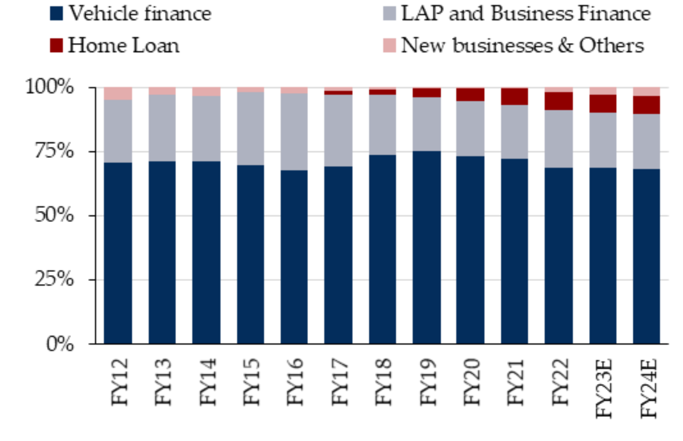
Source: Company, HSIE Research

Exhibit 128: Strong AUM growth over the years



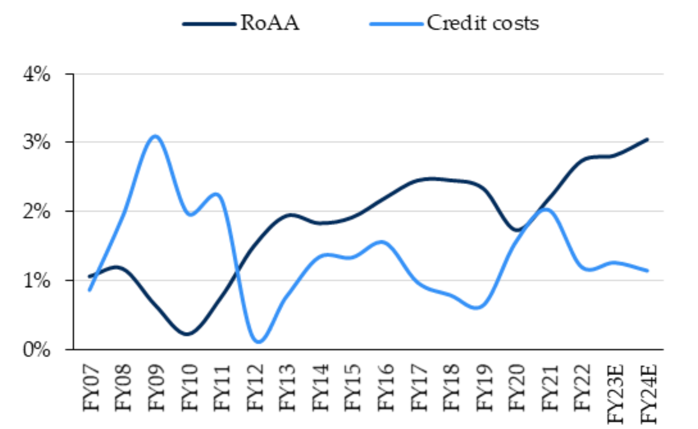
Source: Company, HSIE Research

Exhibit 129: Non-vehicle finance now constitutes ~31% of the AUM



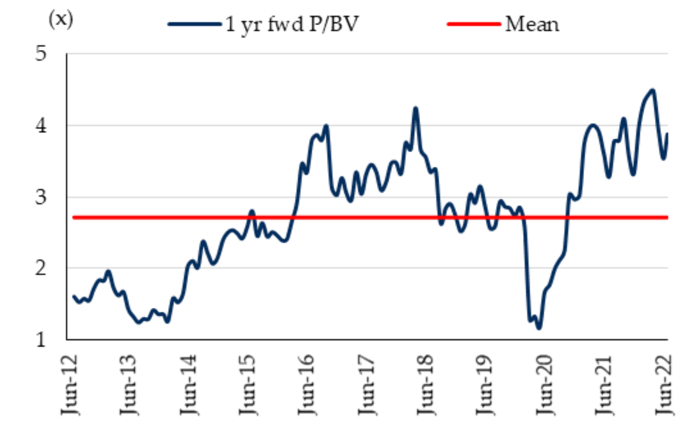
Source: Company, HSIE Research

Exhibit 130: Maintaining healthy RoA of 2%+



Source: Company, HSIE Research | *IND AS from FY18 onwards*

Exhibit 131: CIFC currently trades at ~40% above 10-year mean with improving earnings profile



Source: Bloomberg, HSIE Research

Income Statement

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest earned	52,457	66,285	81,242	92,242	95,668	112,587	132,640
Interest expended	26,593	35,887	45,922	45,759	42,988	53,288	62,140
Net interest income	**25,864**	**30,398**	**35,319**	**46,483**	**52,680**	**59,298**	**70,499**
Other income	2,339	3,641	5,287	2,955	5,720	6,851	8,370
Total income	28,203	34,039	40,607	49,437	58,400	66,149	78,870
Operating expenditure	11,153	12,696	15,776	15,834	20,687	22,035	25,233
Pre-provisioning operating profit	**17,051**	**21,344**	**24,831**	**33,603**	**37,712**	**44,115**	**53,636**
Non-tax provisions	3,037	3,112	8,973	13,218	8,803	10,548	11,240
Profit before tax	14,014	18,232	15,857	20,384	28,909	33,567	42,396
Tax expenditure	4,831	6,370	5,334	5,235	7,442	8,459	10,684
Profit after tax	**9,183**	**11,862**	**10,524**	**15,149**	**21,467**	**25,108**	**31,712**

Source: Company, HSIE Research

Balance Sheet

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share capital	1,564	1,564	1,640	1,640	1,643	1,643	1,643
Reserves and surplus	49,417	60,193	80,079	93,962	115,434	138,899	166,502
Net worth	50,981	61,757	81,718	95,602	117,077	140,542	168,145
Borrowings	383,303	505,667	550,054	637,300	691,735	802,863	933,125
Other liabilities and provisions	6,613	6,838	8,251	12,581	14,822	17,258	20,231
Total equity and liabilities	**440,897**	**574,263**	**640,024**	**745,484**	**823,634**	**960,663**	**1,121,501**
Cash and cash equivalents	8,880	36,749	69,591	52,319	42,201	47,669	54,901
Investments	729	729	729	16,188	20,761	21,070	21,385
Advances	422,532	526,223	554,027	658,393	741,492	869,504	1,019,258
Fixed assets	1,646	1,759	2,839	2,294	2,916	3,207	3,528
Other assets	7,110	8,804	12,838	16,290	16,264	19,213	22,430
Total assets	**440,897**	**574,263**	**640,024**	**745,484**	**823,634**	**960,663**	**1,121,501**

Source: Company, HSIE Research

Key Ratios

	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
VALUATION RATIOS							
EPS	58.7	75.8	12.8	18.5	26.1	30.6	38.6
Earnings Growth (%)	27.8%	29.2%	-11.3%	44.0%	41.7%	17.0%	26.3%
BVPS (ex reval.)	326	395	100	117	142	171	205
Adj. BVPS (ex reval. & 100% cover)	283	338	84	98	118	148	182
ROAA (%)	2.5%	2.3%	1.7%	2.2%	2.7%	2.8%	3.0%
ROAE (%)	19.5%	21.0%	14.7%	17.1%	20.2%	19.5%	20.5%
P/E (x)	11.7	9.0	53.4	37.1	26.3	22.5	17.8
P/ABV (x)	2.4	2.0	8.1	7.0	5.8	4.6	3.8
P/PPOP (x)	6.3	5.0	22.7	16.7	14.9	12.8	10.5
Dividend yield (%)	0.9%	0.9%	0.2%	0.3%	0.3%	0.7%	0.9%
PROFITABILITY (%)							
Yield on Advances (%)	14.5%	13.4%	14.20%	14.18%	12.88%	13.25%	13.35%
Cost of Funds (%)	8.5%	8.1%	8.70%	7.71%	6.47%	7.13%	7.16%
Core Spread (%)	6.0%	5.3%	5.50%	6.47%	6.41%	6.12%	6.19%
NIM (% of AUM)	6.7%	6.3%	6.15%	7.12%	7.17%	7.09%	7.17%
OPERATING EFFICIENCY							
Cost to average AUM ratio (%)	2.9%	2.6%	2.7%	2.4%	2.8%	2.6%	2.6%
Cost-income ratio (%)	39.5%	37.3%	38.9%	32.0%	35.4%	33.3%	32.0%
BALANCE SHEET STRUCTURE RATIOS							
Loan growth (%)	48.7%	24.5%	5.3%	18.8%	12.6%	17.3%	17.2%
AUM growth (%)	25.5%	26.6%	11.6%	15.6%	9.9%	17.5%	17.5%
Borrowing growth (%)	58.3%	31.9%	8.8%	15.9%	8.5%	16.1%	16.2%
Debt/Equity (x)	7.5	8.2	6.7	6.7	5.9	5.7	5.5
Equity/Assets (%)	11.6%	10.8%	12.8%	12.8%	14.2%	14.6%	15.0%
Equity/Loans (%)	12.1%	11.7%	14.7%	14.5%	15.8%	16.2%	16.5%
Total Capital Adequacy Ratio (CAR) (%)	18.2%	17.4%	20.7%	19.1%	19.6%	19.5%	19.5%
Tier I CAR (%)	13.1%	12.4%	15.3%	15.2%	16.5%	16.8%	17.1%
ASSET QUALITY							
Gross NPL (INR mn)	14,846	14,455	21,633	27,050	33,428	35,954	40,062
Net NPL (INR mn)	6,716	8,921	12,650	15,075	20,167	18,831	18,313
Gross NPL (%)	3.4%	2.7%	3.8%	4.0%	4.4%	4.1%	3.9%
Net NPL (%)	2.4%	1.8%	2.3%	2.3%	2.7%	2.2%	1.9%
Coverage Ratio (%)	30.8%	34.3%	41.5%	44.3%	39.7%	47.6%	54.3%
Provision/Avg. AUM (%)	0.8%	0.6%	1.6%	2.0%	1.2%	1.3%	1.1%
DUPONT ANALYSIS							
Interest earned	14.0%	13.1%	13.4%	13.3%	12.2%	12.6%	12.7%
Interest expended	7.1%	7.1%	7.6%	6.6%	5.5%	6.0%	6.0%
Net interest income	6.9%	6.0%	5.8%	6.7%	6.7%	6.6%	6.8%
Non-interest income	0.6%	0.7%	0.9%	0.4%	0.7%	0.8%	0.8%
Operating expenses	3.0%	2.5%	2.6%	2.3%	2.6%	2.5%	2.4%
Pre-provisioning profit	4.6%	4.2%	4.1%	4.9%	4.8%	4.9%	5.2%
Provisions	0.8%	0.6%	1.5%	1.9%	1.1%	1.2%	1.1%
Tax	1.3%	1.3%	0.9%	0.8%	0.9%	0.9%	1.0%
ROAA	**2.5%**	**2.3%**	**1.7%**	**2.2%**	**2.7%**	**2.8%**	**3.0%**
Leverage (x)	7.9	9.0	8.5	7.8	7.4	6.9	6.7
ROAE	**19.5%**	**21.0%**	**14.7%**	**17.1%**	**20.2%**	**19.5%**	**20.5%**

Source: Company, HSIE Research

INSTITUTIONAL RESEARCH

Shriram Transport Finance Company

Diversification could reduce cyclical coefficient

Shriram Transport Finance Company (SHTF)'s deep moats in the used vehicle financing segment enables it to exercise high pricing power, with low competitive intensity. However, the heavy dependence on the used vehicles segment (~93% of AUM) and gradual receding in new CV segment have muted AUM growth and caused high volatility in asset quality. The impending merger with SCUF offers portfolio diversification which is likely to help reduce the cyclicality in growth and earnings, although merger synergies are likely to remain limited. We maintain our ADD rating with a TP of INR 1,554 (1.5x Mar-24 ABVPS).

- **Core competencies remain intact:** SHTF's moats in the used vehicle financing remain largely intact with low competitive intensity. SHTF's strong in-house distribution network with a deep understanding of the used CV segment (largely SRTOs and individual truck owners) drives superior pricing power, reflected in high asset yields.
- **Growth rebound on the cards, likely to lag peers:** SHTF's disbursals growth momentum is likely to sustain with the current CV sales largely driven by replacement demand, driving used CV sales as well. However, SHTF's low presence in new vehicles segment (sub-5%), coupled with headwinds in the older vehicles segment (NGT ban, scrappage policy etc.), is likely to lead to lower AUM growth vs. peers. We expect AUM growth of ~13% CAGR during FY22-FY24E.
- **Diversification—a welcome move, synergies awaited:** RBI's approval for the proposed merger without qualification paves the way for the merger of SHTF and SCUF. The impending merger is likely to provide healthy diversification to SHTF's portfolio with lower volatility in asset quality. SHTF's exposure to used vehicle financing has increased from 75% in FY09 to 93% of AUM in FY22. The healthy profitability of SCUF (average RoA of 3.2% during FY19-FY22) implies little dilution to SHTF's current RoA, while the merger synergies are yet to be completely ascertained.
- **Asset quality near pre-COVID levels; maintain ADD:** We maintain ADD rating on STHF with a target price of INR 1,554. We value the company using RI-based model with medium-term RoE at ~16%, implying 1.5x Mar-24 ABVPS. Asset quality has held up fairly well compared to peers who had witnessed significant deterioration in early delinquencies. Better-than-expected rebound in collections and recoveries during Q4FY22 has brought the portfolio to near steady-state levels. Our FY23-FY24 estimates do not factor in merger with SCUF.

Financial summary

(INR bn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
NII	68.2	78.7	80.0	80.7	89.1	99.8	114.8
PPOP	53.8	61.6	62.3	64.0	74.1	79.0	91.3
PAT	23.2	25.6	25.0	24.9	27.1	37.7	45.3
EPS (INR)	102.3	113.0	110.3	98.3	100.1	139.4	167.4
ROAE (%)	18.7	17.4	14.8	12.6	11.4	13.7	14.5
ROAA (%)	2.7	2.5	2.3	2.0	2.0	2.6	2.8
ABVPS (INR)	340.9	449.1	529.5	662	794	907	1,018
P/ABV (x)	4.4	3.3	2.8	2.3	1.9	1.6	1.5
P/E (x)	14.6	13.2	13.6	15.2	14.9	10.7	8.9

Source: Company, HSIE Research

ADD

CMP *(as on 25 Jul 2022)*	INR 1,497
Target Price	INR 1,554
NIFTY	16,631

KEY STOCK DATA	
Bloomberg code	SHTF IN
No. of Shares (mn)	271
MCap (INR bn) / ($ mn)	405/5,440
6m avg traded value (INR mn)	1,451
52 Week high / low	1,696/1,002

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	36.5	28.3	8.0
Relative (%)	37.9	31.9	2.7

SHAREHOLDING PATTERN (%)

	Dec-21	Mar-22
Promoters	26.1	26.5
FIs & Local MFs	15.2	13.8
FPIs	53.2	53.9
Public & Others	5.6	5.7
Pledged Shares		0.0

Source : BSE

Pledged shares as % of total shares

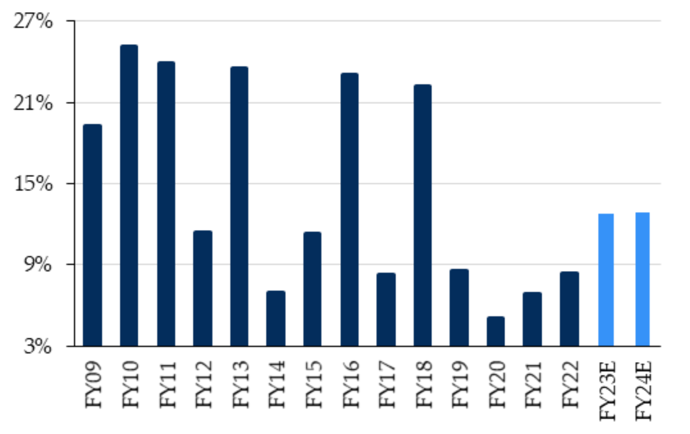
Deepak Shinde
deepak.shinde@hdfcsec.com
+91-22-6171-7323

Krishnan ASV
venkata.krishnan@hdfcsec.com
+91-22-6171-7314

Neelam Bhatia
neelam.bhatia@hdfcsec.com
+91-22-6171-7341

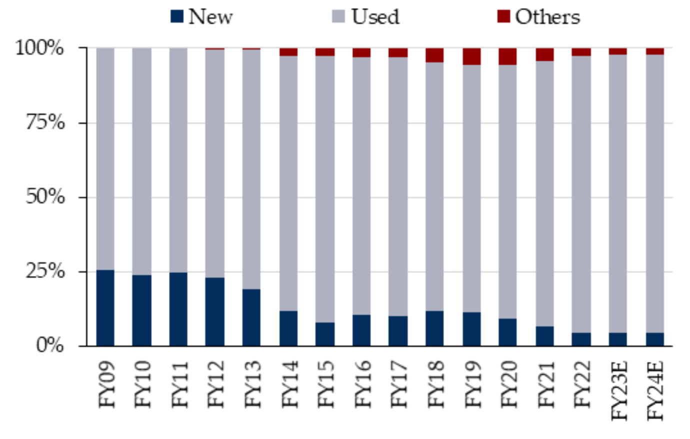
Sahej Mittal
sahej.mittal@hdfcsec.com
+91-22-6171-7325

Exhibit 132: AUM growth muted in the recent past, expected to revive going ahead



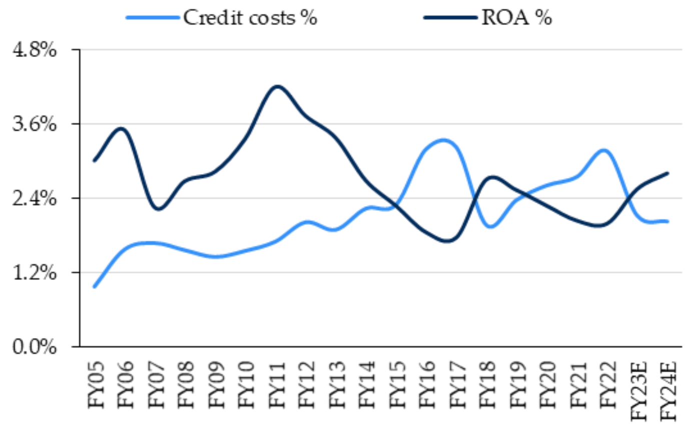
Source: Company, HSIE Research | IND AS from FY18 onwards

Exhibit 133: Portfolio is increasingly becoming predominantly used vehicle financing



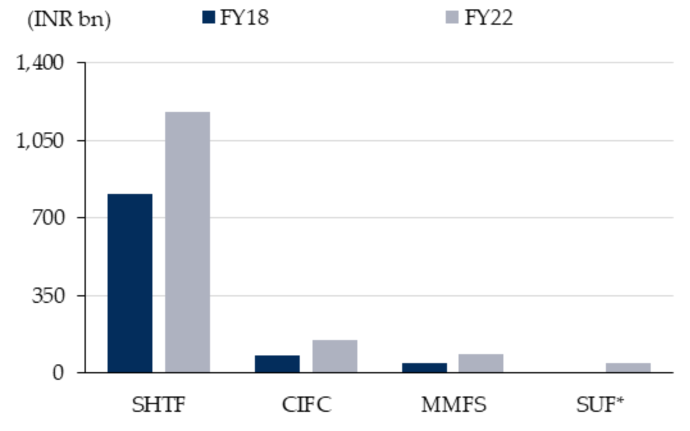
Source: Company, HSIE Research

Exhibit 134: Credit costs over cycles have hovered around ~2-3%



Source: Company, HSIE Research | *IND AS from FY18 onwards*

Exhibit 135: Dominant player in used vehicle financing (AUM)



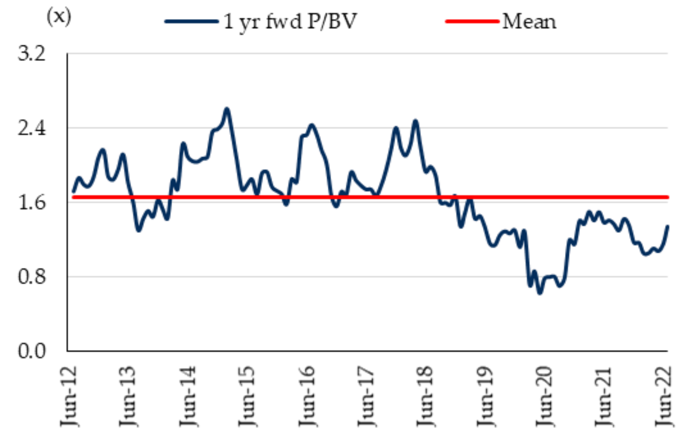
Source: Company, HSIE Research | *Note: * Data for FY18 not available*

Exhibit 136: ROA profile – expected to witness strong rebound during FY23-FY24

% of average assets	FY18 - FY19	FY20 - FY22	FY23-FY24E
Interest earned	15.3%	14.2%	14.1%
Interest expended	7.4%	7.4%	7.2%
Net interest income	7.9%	6.8%	6.9%
Non-interest income	0.2%	0.3%	0.3%
Operating expenses	1.9%	1.7%	1.7%
Pre-provisioning profit	6.2%	5.5%	5.5%
Provisions	2.2%	2.6%	1.9%
Tax	1.4%	0.7%	0.9%
ROAA	2.6%	2.1%	2.7%
Leverage (x)	6.9	6.1	5.3
ROAE	18.0%	12.9%	14.1%

Source: Company, HSIE Research

Exhibit 137: Trading below the 10-year mean – one-year fwd P/BV



Source: Bloomberg, HSIE Research

Financials

Income Statement

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest earned	131,935	153,843	162,675	171,281	186,463	206,418	230,747
Interest expended	63,688	75,113	82,703	90,543	97,343	106,642	115,978
Net interest income	**68,248**	**78,730**	**79,972**	**80,739**	**89,120**	**99,776**	**114,769**
Other income	1,506	1,588	3,083	3,083	6,280	4,154	4,247
Total income	69,754	80,319	83,055	83,821	95,399	103,929	119,016
Operating expenditure	15,910	18,713	20,720	19,857	21,298	24,971	27,720
Pre-provisioning operating profit	**53,844**	**61,605**	**62,336**	**63,964**	**74,101**	**78,958**	**91,296**
Non-tax provisions	17,223	23,823	27,949	31,184	38,609	28,681	30,927
Profit before tax	36,621	37,783	34,387	32,780	35,493	50,277	60,369
Tax expenditure	13,413	12,143	9,368	7,908	8,413	12,569	15,092
Profit after tax	23,209	25,640	25,018	24,873	27,079	37,708	45,277

Source: Company, HSIE Research

Balance Sheet

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share capital	2,269	2,269	2,269	2,531	2,705	2,705	2,705
Reserves and surplus	133,486	156,094	177,783	213,153	256,617	288,914	329,322
Net worth	135,755	158,363	180,052	215,684	259,322	291,619	332,027
Borrowings	821,308	879,144	943,718	1,061,964	1,144,967	1,221,184	1,334,338
Other liabilities and provisions	15,387	15,418	17,517	19,141	16,772	23,086	25,963
Total equity and liabilities	**972,451**	**1,052,925**	**1,141,286**	**1,296,789**	**1,421,061**	**1,535,889**	**1,692,328**
Cash and cash equivalents	36,746	39,815	73,149	164,418	163,552	162,895	149,155
Investments	23,414	39,991	27,985	31,979	68,092	48,106	53,935
Advances	907,456	967,515	1,022,316	1,083,030	1,166,652	1,306,392	1,469,206
Fixed assets	1,221	1,475	4,889	4,374	4,181	4,265	4,350
Other assets	3,615	4,130	12,947	12,988	18,585	14,232	15,682
Total assets	**972,451**	**1,052,925**	**1,141,286**	**1,296,789**	**1,421,061**	**1,535,889**	**1,692,328**

Source: Company, HSIE Research

Key Ratios

	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
VALUATION RATIOS							
EPS	102.3	113.0	110.3	98.3	100.1	139.4	167.4
Earnings Growth (%)	84.6%	10.5%	-2.4%	-0.6%	8.9%	39.2%	20.1%
BVPS (ex reval.)	598	698	794	852	959	1,078	1,227
Adj. BVPS (ex reval. & 100% cover)	341	449	530	662	794	907	1,018
ROAA (%)	2.7%	2.5%	2.3%	2.0%	2.0%	2.6%	2.8%
ROAE (%)	18.7%	17.4%	14.8%	12.6%	11.4%	13.7%	14.5%
P/E (x)	14.6	13.2	13.6	15.2	14.9	10.7	8.9
P/ABV (x)	4.4	3.3	2.8	2.3	1.9	1.6	1.5
P/PPOP (x)	6.3	5.5	5.4	5.9	5.5	5.1	4.4
Dividend yield (%)	0.7%	0.8%	0.0%	0.4%	1.3%	1.2%	1.2%
PROFITABILITY (%)							
Yield on Advances (%)	16.3%	16.0%	15.8%	15.8%	16.0%	16.1%	16.1%
Cost of Funds (%)	9.4%	8.8%	9.1%	9.0%	8.8%	9.0%	9.1%
Core Spread (%)	6.9%	7.2%	6.7%	6.8%	7.2%	7.1%	7.0%
NIM (% of AUM)	7.8%	7.8%	7.5%	7.1%	7.3%	7.4%	7.5%
OPERATING EFFICIENCY							
Cost to average AUM ratio (%)	1.8%	1.9%	1.9%	1.7%	1.7%	1.8%	1.8%
Cost-income ratio (%)	22.8%	23.3%	24.9%	23.7%	22.3%	24.0%	23.3%
BALANCE SHEET STRUCTURE RATIOS							
Loan growth (%)	34.1%	6.6%	5.7%	5.9%	7.7%	12.0%	12.5%
AUM growth (%)	22.2%	8.5%	5.0%	6.8%	8.4%	12.8%	12.9%
Borrowing growth (%)	54.6%	7.0%	7.3%	12.5%	7.8%	6.7%	9.3%
Debt/Equity (x)	6.7	6.2	5.9	5.7	5.3	5.0	4.8
Equity/Assets (%)	14.0%	15.0%	15.8%	16.6%	18.2%	19.0%	19.6%
Equity/Loans (%)	15.0%	16.4%	17.6%	19.9%	22.2%	22.3%	22.6%
Total Capital Adequacy Ratio (CAR) (%)	17.4%	20.3%	22.0%	22.5%	23.0%	25.0%	25.5%
Tier I CAR (%)	14.5%	15.6%	18.1%	19.9%	20.7%	22.8%	23.5%
ASSET QUALITY							
Gross NPL (INR mn)	89,345	86,163	91,771	82,928	88,875	106,346	137,486
Net NPL (INR mn)	58,401	56,465	59,911	48,067	44,460	46,144	56,618
Gross NPL (%)	9.3%	8.4%	8.5%	7.1%	7.1%	7.5%	8.6%
Net NPL (%)	6.4%	5.8%	5.9%	4.4%	3.8%	3.5%	3.9%
Coverage Ratio (%)	34.6%	34.5%	34.7%	42.0%	50.0%	56.6%	58.8%
Provision/Avg. AUM (%)	2.0%	2.4%	2.6%	2.7%	3.2%	2.1%	2.0%
DUPONT ANALYSIS							
Interest earned	15.4%	15.2%	14.8%	14.1%	13.7%	14.0%	14.3%
Interest expended	7.4%	7.4%	7.5%	7.4%	7.2%	7.2%	7.2%
Net interest income	8.0%	7.8%	7.3%	6.6%	6.6%	6.7%	7.1%
Non-interest income	0.2%	0.2%	0.3%	0.3%	0.5%	0.3%	0.3%
Operating expenses	1.9%	1.8%	1.9%	1.6%	1.6%	1.7%	1.7%
Pre-provisioning profit	6.3%	6.1%	5.7%	5.2%	5.5%	5.3%	5.7%
Provisions	2.0%	2.4%	2.5%	2.6%	2.8%	1.9%	1.9%
Tax	1.6%	1.2%	0.9%	0.6%	0.6%	0.9%	0.9%
ROAA	**2.7%**	**2.5%**	**2.3%**	**2.0%**	**2.0%**	**2.6%**	**2.8%**
Leverage (x)	6.9	6.9	6.5	6.2	5.7	5.4	5.2
ROAE	**18.7%**	**17.4%**	**14.8%**	**12.6%**	**11.4%**	**13.7%**	**14.5%**

Source: Company, HSIE Research

INSTITUTIONAL RESEARCH

Mahindra & Mahindra Financial Services

Course correction imperative for franchise stability

MMFS's newly laid out roadmap for FY25 is commendable and necessary. However, a predominantly rural and semi-urban customer franchise has delivered sub-par returns, couple with volatile asset quality for the past few years. While the company has recovered significantly after the Q1FY22 asset quality shock, the sharp spike in the delinquent portfolio and credit costs with every external shock is a concern. To that extent, its strategy of product and customer diversification and leveraging of inherent strengths of parentage and rural presence are welcome, although achieving superior financial metrics during FY22-FY25E is likely to remain a challenge, in our view. We maintain ADD with an SoTP-based TP of INR 215 (standalone entity at 1.4x Mar-24 ABVPS).

- **Rural franchise drives high volatility in earnings and sub-par returns**: MMFS' predominant rural and semi-urban exposure leaves the company prone to high volatility during economic shocks (demonetization, COVID etc.). However, asset yields have not kept pace with increasing credit costs, thereby driving risk-adjusted spreads lower over the years.
- **In search of star businesses, beyond captive financing:** MMFS' diversification into non-M&M portfolio, despite having made healthy progress, remains WIP with M&M contribution to MMFS's AUM at ~44-45%. The other segments are yet to emerge as stars in the MMFS portfolio and scale up significantly, except cars portfolio. Like with other captive financiers, MMFS's asset quality woes escalated during H1FY22, although they tapered off materially in H2FY22.
- **Roadmap for sustained profitability— necessary but not sufficient:** MMFS's latest roadmap to achieve 25% AUM growth with opex to assets and RoA of 2.5% simultaneously seems a steep ask. However, the roadmap is much needed strategy to achieve earnings and portfolio stability. MMFS has certain advantages to achieve product and customer diversification such as strong parentage to provide support on SME, supply chain financing etc., along with a large dominant presence in the rural side. However, the migration from existing profile of customers towards more creditworthy customers and more wholesale credit exposure are likely to increase competitive intensity, particularly with banks, where the right-to-win is not evident.
- **Execution key monitorable, maintain ADD:** The execution of the latest roadmap remains key monitorable for MMFS for any rerating as the return ratios have remained subdued and below potential. We believe MMFS could gradually improve its portfolio mix towards more risk-adjusted profitable segments, although achieving the targeted financial metrics is likely to remain a challenge in the near term.

Financial summary

(INR bn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
NII	35.0	46.7	51.1	55.3	55.6	62.0	74.0
PPOP	21.7	30.2	34.0	41.5	37.3	41.1	49.4
PAT	10.1	15.6	9.1	3.3	9.9	16.0	23.2
EPS (INR)	16.5	25.3	14.7	2.7	8.0	12.9	18.8
ROAE (%)	12.6%	15.2%	8.1%	2.5%	6.5%	9.9%	13.1%
ROAA (%)	2.0%	2.6%	1.3%	0.4%	1.3%	1.9%	2.3%
ABVPS (INR)	102.7	123.9	120.2	99.6	109.8	115.7	127.6
P/ABV (x)	2.0	1.7	1.7	2.1	1.9	1.8	1.6
P/E (x)	12.6	8.2	14.1	77.9	25.9	16.1	11.1

Source: Company, HSIE Research

ADD

CMP *(as on 25 Jul 2022)*	INR 208
Target Price	INR 215
NIFTY	16,631

KEY STOCK DATA	
Bloomberg code	MMFS IN
No. of Shares (mn)	1,236
MCap (INR bn) / ($ mn)	257/3,456
6m avg traded value (INR mn)	919
52 Week high / low	213/128

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	18.2	34.3	35.0
Relative (%)	19.6	37.9	29.8

SHAREHOLDING PATTERN (%)

	Mar-22	Jun-22
Promoters	52.2	52.2
FIs & Local MFs	17.9	20.4
FPIs	18.7	17.6
Public & Others	11.1	9.7
Pledged Shares		0.0

Source : BSE

Pledged shares as % of total shares

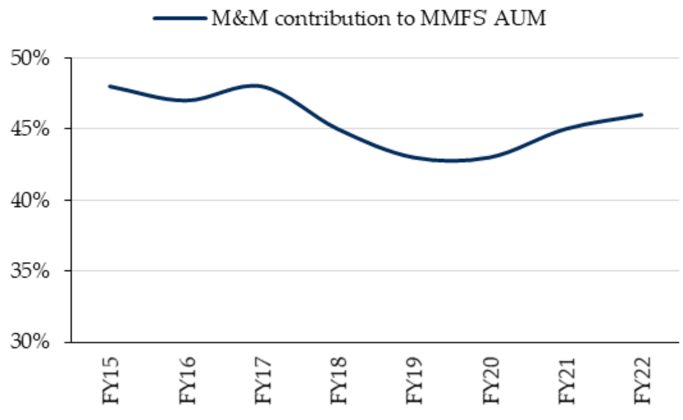
Deepak Shinde
deepak.shinde@hdfcsec.com
+91-22-6171-7323

Krishnan ASV
venkata.krishnan@hdfcsec.com
+91-22-6171-7314

Neelam Bhatia
neelam.bhatia@hdfcsec.com
+91-22-6171-7341

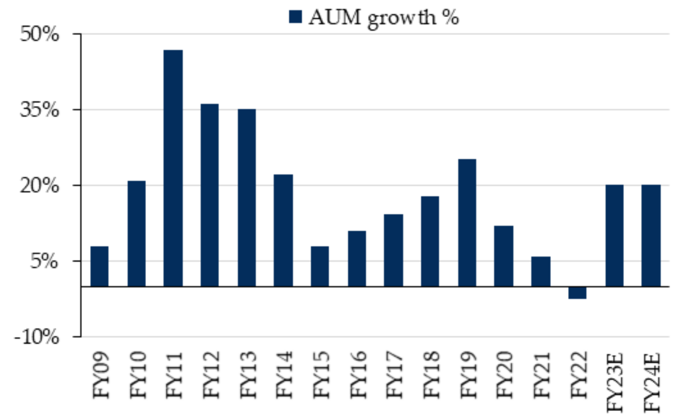
Sahej Mittal
sahej.mittal@hdfcsec.com
+91-22-6171-7325

Exhibit 138: M&M share in MMFS' AUM has remained fairly high at ~45%



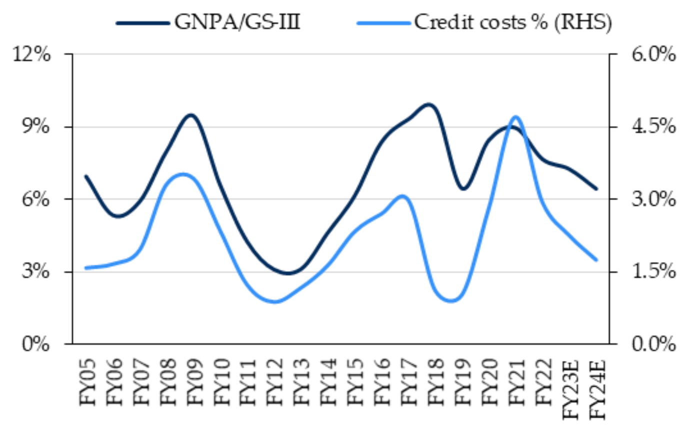
Source: Company, HSIE Research

Exhibit 139: Loan growth – expected to witness strong revival



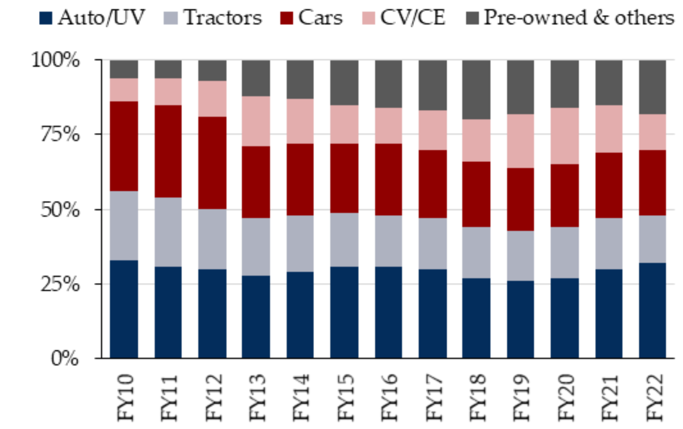
Source: Company, HSIE Research

Exhibit 140: Asset quality has remained fairly volatile



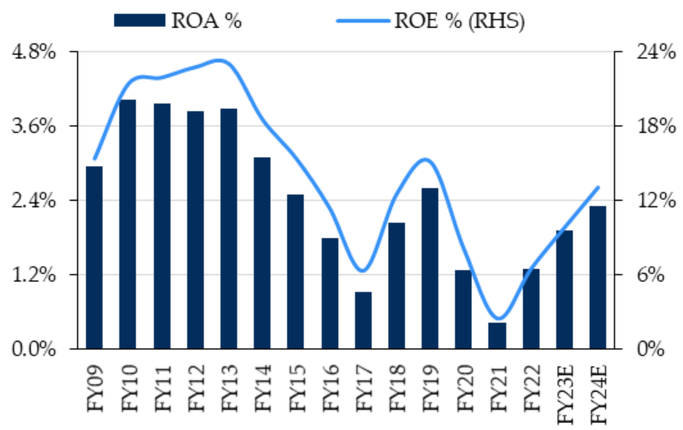
Source: Company, HSIE Research | *IND AS from FY18 onwards* | *Transition from 180dpd NPA recognition to 90dpd in a phased manner from FY13 to FY17*

Exhibit 141: Portfolio mix over the years



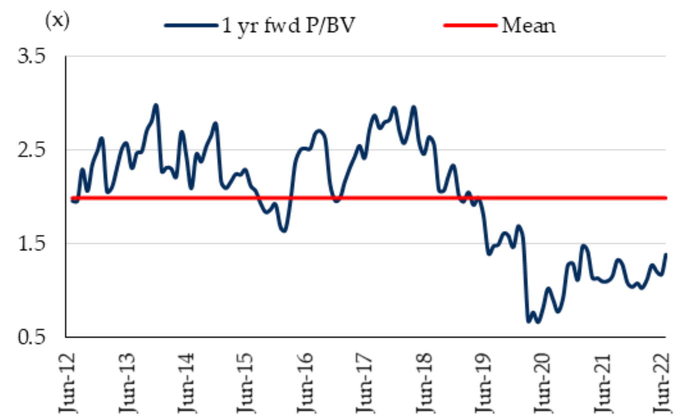
Source: Company, HSIE Research

Exhibit 142: Profitability has remained muted for the last few years



Source: Company, HSIE Research | *IND AS from FY18 onwards*

Exhibit 143: MMFS has witnessed significant de-rating in the recent years



Source: Bloomberg, HSIE Research

Financials

Income Statement

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest earned	65,842	86,146	99,417	102,670	94,756	108,191	131,464
Interest expended	30,816	39,446	48,288	47,332	39,202	46,199	57,483
Net interest income	**35,025**	**46,700**	**51,130**	**55,338**	**55,554**	**61,992**	**73,981**
Other income	1,010	1,953	3,034	2,498	2,432	3,643	4,480
Total income	36,036	48,653	54,164	57,835	57,986	65,635	78,461
Operating expenditure	14,336	18,476	20,182	16,325	20,734	24,552	29,059
Pre-provisioning operating profit	**21,700**	**30,177**	**33,982**	**41,510**	**37,252**	**41,083**	**49,403**
Non-tax provisions	5,681	6,352	20,545	37,348	23,683	19,754	18,408
Profit before tax	16,018	23,824	13,438	4,162	13,569	21,329	30,995
Tax expenditure	5,907	8,254	4,374	873	3,682	5,375	7,811
Profit after tax	**10,111**	**15,571**	**9,064**	**3,289**	**9,888**	**15,954**	**23,184**

Source: Company, HSIE Research

Balance Sheet

(INR mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share capital	1,229	1,230	1,231	2,464	2,466	2,466	2,466
Reserves and surplus	94,777	107,512	111,922	144,224	153,502	165,018	184,133
Net worth	96,219	109,080	113,639	147,115	156,281	167,484	186,599
Borrowings	400,932	528,469	594,623	585,767	558,139	694,334	855,160
Other liabilities and provisions	30,777	33,230	32,451	37,483	38,467	40,969	54,871
Total equity and liabilities	**527,927**	**670,780**	**740,712**	**770,364**	**752,887**	**902,786**	**1,096,630**
Cash and cash equivalents	4,111	9,585	14,258	32,696	41,507	37,068	45,994
Investments	27,341	37,917	59,110	116,073	84,403	98,459	110,533
Advances	485,470	612,496	649,935	599,474	604,446	744,882	914,515
Fixed assets	1,197	1,631	3,635	3,405	3,928	4,321	4,753
Other assets	9,808	9,151	13,775	18,717	18,603	18,056	20,836
Total assets	**527,927**	**670,780**	**740,712**	**770,364**	**752,887**	**902,786**	**1,096,630**

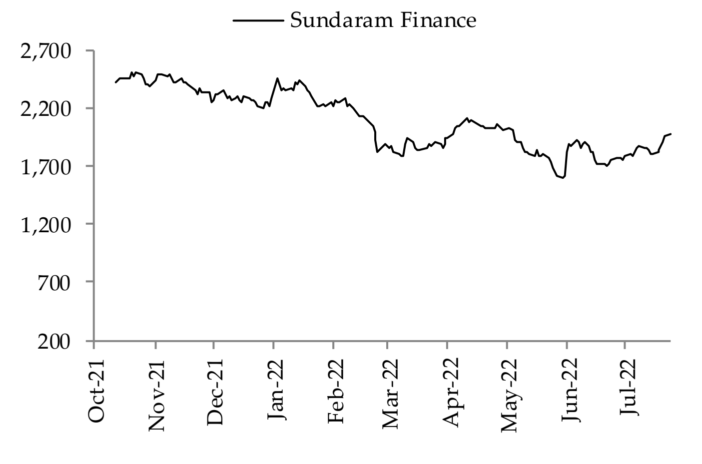
Source: Company, HSIE Research

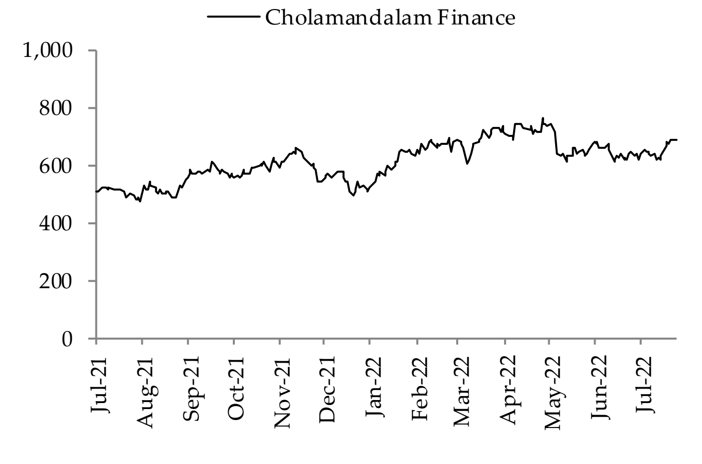
Key Ratios

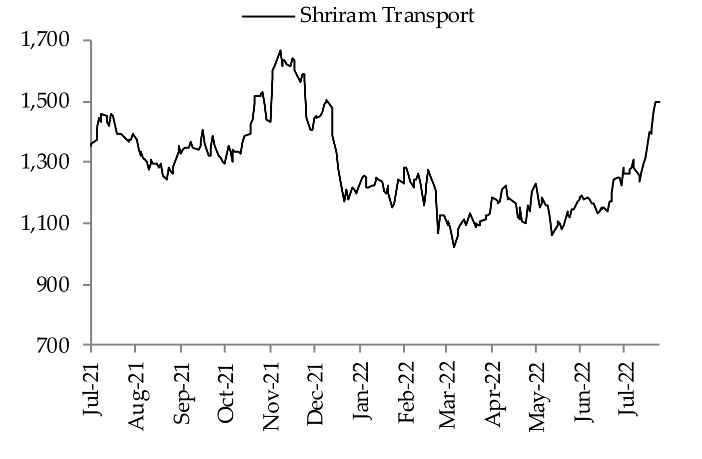
	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
VALUATION RATIOS							
EPS	16.5	25.3	14.7	2.7	8.0	12.9	18.8
Earnings Growth (%)	152.6%	54.0%	-41.8%	-63.7%	200.6%	61.4%	45.3%
BVPS (ex reval.)	157	177	185	119	127	136	151
Adj. BVPS (ex reval. & 100% cover)	103	124	120	100	109.8	115.7	127.6
ROAA (%)	2.0%	2.6%	1.3%	0.4%	1.3%	1.9%	2.3%
ROAE (%)	12.6%	15.2%	8.1%	2.5%	6.5%	9.9%	13.1%
P/E (x)	12.6	8.2	14.1	77.9	25.9	16.1	11.1
P/ABV (x)	2.0	1.7	1.7	2.1	1.9	1.8	1.6
P/PPOP (x)	5.9	4.2	3.8	6.2	6.9	6.2	5.2
Dividend yield (%)	1.9%	3.1%	0.0%	0.4%	1.7%	1.6%	2.2%
PROFITABILITY (%)							
Yield on Advances (%)	13.8%	14.7%	14.9%	14.8%	13.8%	14.4%	14.5%
Cost of Funds (%)	8.2%	8.5%	8.6%	8.0%	6.9%	7.4%	7.4%
Core Spread (%)	5.5%	6.2%	6.3%	6.8%	6.9%	7.0%	7.1%
NIM (% of AUM)	6.9%	7.5%	7.0%	7.0%	6.9%	7.1%	7.0%
OPERATING EFFICIENCY							
Cost to average AUM ratio (%)	2.8%	3.0%	2.8%	2.1%	2.6%	2.8%	2.8%
Cost-income ratio (%)	39.8%	38.0%	37.3%	28.2%	35.8%	37.4%	37.0%
BALANCE SHEET STRUCTURE RATIOS							
Loan growth (%)	14.8%	26.2%	6.1%	-7.8%	0.8%	23.2%	22.8%
AUM growth (%)	17.8%	25.1%	11.9%	5.9%	-2.3%	20.1%	20.1%
Borrowing growth (%)	15.6%	31.8%	12.5%	-1.5%	-4.7%	24.4%	23.2%
Debt/Equity (x)	4.5	5.4	6.0	4.6	4.1	4.7	5.2
Equity/Assets (%)	18.2%	16.3%	15.3%	19.1%	20.8%	18.6%	17.0%
Equity/Loans (%)	19.8%	17.8%	17.5%	24.5%	25.9%	22.5%	20.4%
Total Capital Adequacy Ratio (CAR) (%)	22.7%	20.3%	19.6%	26.0%	27.8%	24.9%	22.6%
Tier I CAR (%)	17.0%	15.5%	15.4%	22.2%	24.2%	22.0%	20.2%
ASSET QUALITY							
Gross NPL (INR mn)	50,270	40,706	57,468	57,911	49,814	57,387	62,023
Net NPL (INR mn)	33,109	32,907	39,666	24,391	20,914	24,865	29,217
Gross NPL (%)	9.8%	6.4%	8.4%	9.0%	7.7%	7.2%	6.4%
Net NPL (%)	6.8%	5.4%	6.1%	4.1%	3.5%	3.3%	3.2%
Coverage Ratio (%)	34.1%	19.2%	31.0%	57.9%	58.1%	56.7%	52.9%
Provision/Avg. AUM (%)	1.1%	1.0%	2.8%	4.7%	2.9%	2.2%	1.7%
DUPONT ANALYSIS							
Interest earned	13.3%	14.4%	14.1%	13.6%	12.4%	13.1%	13.2%
Interest expended	6.2%	6.6%	6.8%	6.3%	5.1%	5.6%	5.7%
Net interest income	**7.1%**	**7.8%**	**7.2%**	**7.3%**	**7.3%**	**7.5%**	**7.4%**
Non-interest income	0.2%	0.3%	0.4%	0.3%	0.3%	0.4%	0.4%
Operating expenses	2.9%	3.1%	2.9%	2.2%	2.7%	3.0%	2.9%
Pre-provisioning profit	4.4%	5.0%	4.8%	5.5%	4.9%	5.0%	4.9%
Provisions	1.2%	1.1%	2.9%	4.9%	3.1%	2.4%	1.8%
Tax	1.2%	1.4%	0.6%	0.1%	0.5%	0.6%	0.8%
ROAA	**2.0%**	**2.6%**	**1.3%**	**0.4%**	**1.3%**	**1.9%**	**2.3%**
Leverage (x)	6.1	5.8	6.3	5.8	5.0	5.1	5.6
ROAE	**12.6%**	**15.2%**	**8.1%**	**2.5%**	**6.5%**	**9.9%**	**13.1%**

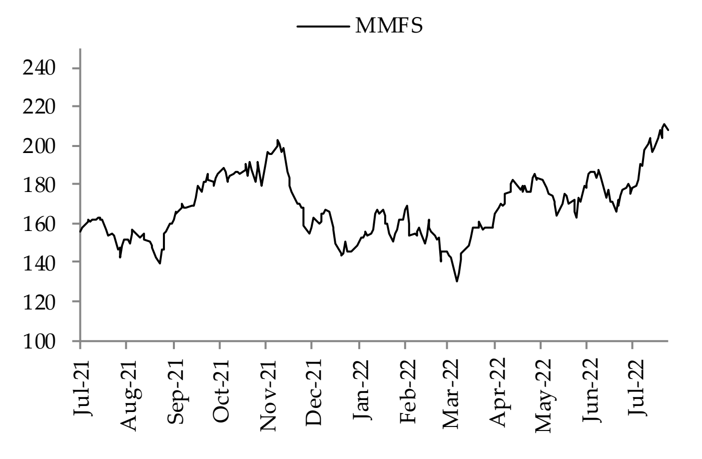
Source: Company, HSIE Research

1 Yr Price movement









Rating Criteria

BUY: >+15% return potential
ADD: +5% to +15% return potential
REDUCE: -10% to +5% return potential
SELL: > 10% Downside return potential

Thematic reports by HSIE

Cement: WHRS – A key cog in the flywheel | Autos: Where are we on "S" curve? | FMCG: Defensive businesses but not valuations | Autos: A changed landscape | Banks: Double whammy for some | India Equity Strategy: Atma Nirbhar Bharat | Indian IT: Demand recovery in sight

Life Insurance: Recovery may be swift with protection driving margins | Retail: Whole flywheel is broken? | Appliances: Looing beyond near-term disruption | Pharma: Chronic therapy – A portfolio prescription | Indian Gas: Looking beyond the pandemic | India Equity Strategy: Quarterly flipbook | Real Estate: Ripe for consumption

Indian IT: expanding centre of gravity | Indian Chemical: Evolution to revolution! | Life Insurance: ULIP vs. MF | Infrastructure: On the road to rerating | Cement: Spotting the sweet spot | Pharma: Cardiac: the heartbeat of domestic market | Life Insurance: Comparative annual report analysis

Indian microfinance: Should you look micro as macros disappoint? | India Equity Strategy: Quarterly flipbook | Autos: Divergent trends in PVs and 2Ws | India Internet: the stage is set | FMCG: Opportunity in adversity - A comparative scorecard | Logistics: Indian Railways - getting aggressive | Industrials: Triggering a new cycle

Indian IT: raising the bar | India Equity Strategy: Quarterly flipbook | FinTech Playbook: P2M Payments | Surging pool, dwindling yields | India Hospitals: capital discipline improving, sustenance is key | Autos: Will EVs impact the 'EV'? | Cement: Riding High | Power: Reforms essential for rennaissance

Fashion & Lifestyle: From a disruptor's lens II | India Equity Strategy: Quarterly flipbook | Indian Gas Sector: Resilience in the eye of the storm | Consumer Durables: Fans - a compounding story but underrated | Quarterly flipbook: Q2FY22–Demand environment improves but input cost inflation dents profitability | FinTech Playbook: Discount Brokers | Footwear: No bargains here!

Holdcos for portfolio diversification | Cement: A concrete road for net-zero emissions | FinTech Playbook: Buy Now Pay Later | De-mystifying the tablestakes | India Equity Strategy: PLI: Spearheading India's manufacturing push | Power: Shifting energy landscape: Grey to green gains pace | IT sector: Decoding signal from noise

Disclosure:

We, **Krishnan ASV, PGDM, Aniket Mhatre, MBA, Deepak Shinde, PGDM, Neelam Bhatia, PGDM , Sahej Mittal, ACA and Sonaal Sharma, MBA** authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. SEBI conducted the inspection and based on their observations have issued advise/warning. The said observations have been complied with. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

Research Analyst or his/her relative or HDFC Securities Ltd. does not have any financial interest in the subject company. Also Research Analyst or his relative or HDFC Securities Ltd. or its Associate may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Further Research Analyst or his relative or HDFC Securities Ltd. or its associate does not have any material conflict of interest.

Any holding in stock – **YES**

HDFC Securities Limited (HSL) is a SEBI Registered Research Analyst having registration no. INH000002475.

Disclaimer:

This report has been prepared by HDFC Securities Ltd and is solely for information of the recipient only. The report must not be used as a singular basis of any investment decision. The views herein are of a general nature and do not consider the risk appetite or the particular circumstances of an individual investor; readers are requested to take professional advice before investing. Nothing in this document should be construed as investment advice. Each recipient of this document should make such investigations as they deem necessary to arrive at an independent evaluation of an investment in securities of the companies referred to in this document (including merits and risks) and should consult their own advisors to determine merits and risks of such investment. The information and opinions contained herein have been compiled or arrived at, based upon information obtained in good faith from sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. Descriptions of any company or companies or their securities mentioned herein are not intended to be complete. HSL is not obliged to update this report for such changes. HSL has the right to make changes and modifications at any time.

This report is not directed to, or intended for display, downloading, printing, reproducing or for distribution to or use by, any person or entity who is a citizen or resident or located in any locality, state, country or other jurisdiction where such distribution, publication, reproduction, availability or use would be contrary to law or regulation or what would subject HSL or its affiliates to any registration or licensing requirement within such jurisdiction.

If this report is inadvertently sent or has reached any person in such country, especially, United States of America, the same should be ignored and brought to the attention of the sender. This document may not be reproduced, distributed or published in whole or in part, directly or indirectly, for any purposes or in any manner.

Foreign currencies denominated securities, wherever mentioned, are subject to exchange rate fluctuations, which could have an adverse effect on their value or price, or the income derived from them. In addition, investors in securities such as ADRs, the values of which are influenced by foreign currencies effectively assume currency risk. It should not be considered to be taken as an offer to sell or a solicitation to buy any security.

This document is not, and should not, be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. This report should not be construed as an invitation or solicitation to do business with HSL. HSL may from time to time solicit from, or perform broking, or other services for, any company mentioned in this mail and/or its attachments.

HSL and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

HSL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

HSL and other group companies, its directors, associates, employees may have various positions in any of the stocks, securities and financial instruments dealt in the report, or may make sell or purchase or other deals in these securities from time to time or may deal in other securities of the companies / organizations described in this report.

HSL or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

HSL or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from t date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction in the normal course of business.

HSL or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither HSL nor Research Analysts have any material conflict of interest at the time of publication of this report. Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. HSL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Research entity has not been engaged in market making activity for the subject company. Research analyst has not served as an officer, director or employee of the subject company. We have not received any compensation/benefits from the subject company or third party in connection with the Research Report.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

HDFC Securities Limited, SEBI Reg. No.: NSE, BSE, MSEI, MCX: INZ000186937; AMFI Reg. No. ARN: 13549; PFRDA Reg. No. POP: 11092018; IRDA Corporate Agent License No.: CA0062; SEBI Research Analyst Reg. No.: INH000002475; SEBI Investment Adviser Reg. No.: INA000011538; CIN - U67120MH2000PLC152193

Mutual Funds Investments are subject to market risk. Please read the offer and scheme related documents carefully before investing.

HDFC securities
Institutional Equities
Unit No. 1602, 16th Floor, Tower A, Peninsula Business Park,
Senapati Bapat Marg, Lower Parel, Mumbai - 400 013
Board: +91-22-6171-7330 www.hdfcsec.com