

Ref: STEC NSE/BSE 206/2020

December 9, 2020

The Secretary,
BSE Ltd
P J Towers,
Dalal St,
Mumbai 400 001

The Manager
National Stock Exchange of India Ltd
Exchange Plaza, 5th Floor
Plot No.C/1, G Block
Bandra- Kurla Complex Bandra (E)
Mumbai 400 051

Sir,

Ref: ISIN – INE722A01011
Scrip Code: BSE – 532498 and NSE - SHRIRAMCIT

This is to inform you that India Ratings and Research Limited has affirmed the Company's Long term Issuer rating of 'IND AA' and resolved the Rating Watch Negative (RWN) and affirmed Short-Term Issuer Rating at 'IND A1+'. The outlook was stable. The instrument-wise rating actions are given below

Sl. No.	Instrument Type	Amount (₹ in billion)	Rating/ Outlook	Rating Action
1	Bank Loan	150	IND AA/Stable	Affirmed; Off RWN
2	Long-term debt programme	0.05	IND AA/Stable	Affirmed; Off RWN
3	Non-convertible debentures (NCDs)	10	IND AA/Stable	Affirmed; Off RWN
4	Fixed deposit programme	-	IND tAA/Stable	Affirmed; Off RWN

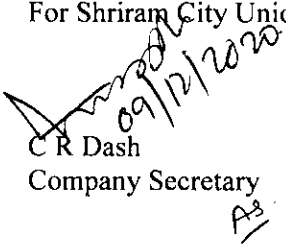
The rationale by India Ratings and Research Limited dated December 8, 2020 is enclosed

This is an intimation under Regulation 30 read with Schedule III (Part A) (3) of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements), Regulations, 2015 as amended from time to time.

We request you to kindly take the above information on record.

Thanking you,
Yours faithfully,

For Shriram City Union Finance Limited,


C R Dash
Company Secretary

Shriram City Union Finance Limited

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Corporate Identification Number (CIN) L65191TN1986PLC012840

India Ratings Affirms Shriram City Union Finance at 'IND AA'/Stable; Off RWN

08

DEC 2020

By **Amit Rane**

India Ratings and Research (Ind-Ra) has affirmed Shriram City Union Finance Limited's (SCUF) Long-Term Issuer Rating at 'IND AA' while resolving the Rating Watch Negative (RWN). The Outlook is Stable. The agency has also affirmed SCUF's Short-Term Issuer Rating at 'IND A1+'. The instrument-wise rating actions are as follows:

Instrument Type	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Bank loan	-	-	-	INR150	IND AA/Stable	Affirmed; Off RWN
Long-term debt programme*				INR0.05	IND AA/Stable	Affirmed; Off RWN
Non-convertible debentures (NCDs)*	-	-	-	INR10	IND AA/Stable	Affirmed; Off RWN
Fixed deposit programme	-	-	-	-	IND tAA/Stable	Affirmed; Off RWN

* Details in Annexure

Analytical Approach: Ind-Ra has taken a consolidated view of SCUF (34% owned by Shriram Capital & Shriram Ventures) and Shriram Housing Finance Ltd (SHFL; 77.25% owned by SCUF; debt rated at 'IND AA/Stable'), to arrive at the ratings. While SCUF mainly provides business loans, SHFL provides housing loans across segments and plans to leverage the Shriram Group's ecosystem.

SCUF's ratings were placed on RWN post the measures taken by the authorities to contain the spread of the COVID-19 leading to limited visibility on the impact of the same on SCUF's asset quality and credit costs. Furthermore, the agency took a cautious stance towards the tightening market conditions, which could impact the funding sources and funding costs for SCUF that have already been elevated since the onset of the liquidity crisis for non-banking financial companies in September 2018.

The rating affirmation and the resolution of the RWN reflect the improving trend in SCUF's collections over April-October 2020, with the company reporting collections efficiency of 93% in October 2020 (compared to 34% in April 2020). On the provisioning front, SCUF has already created a buffer of INR7.1 billion (2.6% of assets under management (AUM) as of 2QFY21) and the coverage for Stage 3 assets has been ramped up to 54.4% in 2QFY21. Moreover, the agency believes the company has sufficient pre-provision operating profit (PPOP) buffer and COVID-19-related provisions to cover the credit costs that it could incur in FY21 and FY22 without facing capital erosion. With the now improved overall collections efficiency as compared to that during the complete lockdown phase, SCUF has been able to mobilise funds at competitive rates from various sources including banks and retail fixed deposits despite the pandemic-led disruptions. The company has been able to diversify the sources of funding with higher contribution from retail fixed deposits at reasonable cost. Given the Shriram Group's parentage, Ind-Ra does not foresee any major challenge for SCUF to raise funds incrementally. That said, the company's ability to grow in its core segment of small and medium enterprises (SME) remains a rating monitorable over the near term.

The sustainability and a further improvement in the collection efficiency and the full impact of ongoing challenges on softer-bucket delinquencies and the transition of softer buckets to stage-3 delinquencies remain key monitorable over the near-to-medium term. This is because there is a standstill on asset quality movement due to an ongoing court case in the Supreme Court and availability of the Reserve Bank of India's one-time debt restructuring window till 31 December 2020. Having said that, the low leverage for the consolidated entity (1HFY21: 3.1x) provides some cushion, in case the credit costs were to spike.

KEY RATING DRIVERS

Well-established Track Record in High-yielding Segment: SCUF has an established track record of over three decades with expertise in low-ticket-size and high-yielding products such as SME (contributing 58% to the AUM) and two-wheeler (contributing 21% to the AUM) lending. The company has an AUM of INR275 billion, distributed across 22 states with a total network of 947 branches and over 25,000 employees at end-September 2020. SCUF's key strengths are its large customer base with long-term relationships directly or through the Shriram Group companies coupled with strong local knowledge and the ability to appraise businesses dealing in cash and robust collection infrastructure. This strength has been reflected in a sharp recovery in its collection efficiency in the current stressed environment.

Improvement in Collections Post Lockdown: SCUF's collection efficiency (calculated as total collections including all overdues, prepayments, pre-closures, etc/billing for the month) improved to 93% in October 2020 (April 2020: 34%; June 2020: 62%; August 2020: 76%, pre-COVID-19: 105%-110%). Notably, in the SME segment (wherein 67% of the AUM was under the Reserve Bank of India's moratorium at end-August 2020), the collection efficiency improved to 92% in October 2020 (April 2020: 18%; June 2020: 43%; August 2020: 65%). The collection to demand for the same month is still about 9% lower on an overall basis (11% for SME) compared to average pre-COVID-19 level and Ind-Ra expects these rates to improve in the medium term.

Adequate Capitalisation: The company's consolidated leverage improved to 3.1x at 1HFY21 (FY20: 3.4x, FY19: 3.7x) given its healthy internal accruals and muted AUM growth. SCUF (standalone) reported a Tier-I capital adequacy ratio of 30.1% in 1HFY21 (FY20: 27.7%, FY19: 22.75%). The agency expects SCUF to continue to hold significantly higher equity buffers than those of its peer non-banking financial companies to reflect its customers' weaker credit profile (implying operations at the higher end of the yield curve in the SME and two-wheeler portfolio, and the lack of seasoning in its housing subsidiary's portfolio). Ind-Ra believes SCUF is well capitalised to withstand credit costs that may exceed PPOP, which is unlikely over the near-to-medium term.

Liquidity Indicator – Adequate: According to the asset liability management statement (ALM) of end-September 2020, the company remains comfortable on the ALM of SCUF and SHFL (combined) with cumulative surplus (excess of short-term assets over short-term liabilities) up to 1 year (35% of total assets). Moreover, SCUF (combined with SHFL) had unencumbered cash and liquid investments of INR28.8 billion at end-October 2020 (INR23.7 billion at end-March 2020) and sanctioned but undrawn bank lines of about INR5.7 billion at end-October 2020. According to the agency, at end-October 2020, SCUF had adequate liquidity to cover its debt repayments (principal + interest) and operating expenses for about 2.5 months, assuming nil inflows.

For SCUF (standalone), bank loans constitute about half of its total borrowings in 1HFY21 (FY20: 45.6%; FY19: 54%; FY18: 58%), in line with most of its peers. The share of retail deposits in SCUF's overall funding continues to increase (1HFY21: 22.1%, FY20: 18.4%, FY19: 16%). The company has demonstrated its ability to mobilise funds with a fund raising of INR42.05 billion during 1HFY21 (1HFY20: INR56.1 billion), mainly contributed by INR26.1 billion through bank borrowings and INR13.7 billion from retail fixed deposits. The incremental cost of borrowing declined to 9.06% during 2QFY21 as against the on-book borrowing cost of 9.56%. The agency will monitor the company's ability to mobilise incremental funds at competitive rates in 2HFY21.

Buffers to absorb Incremental Credit Costs in Place: SCUF's gross stage-3 assets improved to 6.67% as of 2QFY21 (1QFY21: 7.28%; FY20: 7.90%; FY19: 8.9%). Notably, the reported gross stage-3 assets would have been much lower at 5.98% in 2QFY21 as per the Supreme Court order on the non-declaration of a regular account as non-performing after August 2020. The company's credit costs (as a percentage of average assets increased to 3.9% on an annualised basis in 1HFY21 (FY20: 3.2%; FY19: 2.9%) due to higher expected credit loss provisions (including COVID-19-related and higher stage 3 provisions). SCUF has improved its provision coverage ratio on stage-3 assets (2QFY21: 54.4%, FY20: 48.5%, FY19: 43.6%) in view of the current challenging environment. Consequently, the net stage-3 assets improved to 3.16% as of 2QFY21 (1QFY21: 3.8%; FY20: 4.2%; FY19: 5.2%). The consolidated return on average assets stood at 2.9% in 1HFY21 (FY20: 3.2%; FY19: 3.3%). Under Ind-Ra's stress tests, credit costs for FY21 and FY22 could be 5%-7% each (including COVID-19 provisions of 2.3%); with an increase in slippages and restructuring SCUF may see a decline in its PPOP to about 7% (1HFY21: 7.5%; FY20: 7.4%; FY19: 8.1%) and hence, operating buffers will be adequate to withstand credit costs and without capital erosion.

Loan Growth to Remain Subdued in FY21: The company's loan growth over FY18-FY20 was low at a CAGR of 5.4% in AUM, reflecting the macroeconomic stress in the SME segment as well as competition. Moreover, post COVID-19, AUM declined 7.3% yoy in 2QFY21 as the company focused on collections while disbursing much lower amounts in gold and two-wheeler segments. According to the management, disbursements in 3QFY21 in the SME segment have shown significant traction and is likely to reach pre-COVID-19 quarterly disbursement run-rate by 4QFY21.

SCUF's average disbursement per SME loan account has remained INR1.2 million-1.3 million since FY18 and the company expects it to remain at similar levels over the medium term. According to the management, SCUF will continue to focus on its existing borrower segments (including used two wheeler product introduced in 1QFY21) and expects the overall SME loan segment to constitute 60%-65% of its aggregate loans under management over the medium term. While many competitors have remained absent from home loan financing, SHFL plans high growth; but at end-1HFY21, it constituted about 10% of the consolidated book.

RATING SENSITIVITIES

Positive: Sustained growth in SCUF's franchise and funding profile with higher capital market participation at competitive rates and asset quality while maintaining profitability and liquidity ratios could lead to positive rating action.

Negative: Significant deterioration in the asset liability profile and liquidity position, the gross stage-3 assets exceeding 10% and/or the net non-performing assets surpassing and sustaining above 6%, the tier 1 ratio falling below 20% and a higher-than-expected deterioration in return on assets could lead to a negative rating action.

COMPANY PROFILE

SCUF was established in 1986 as a commercial vehicle financier, part of the larger Shriram Group. In FY06, SCUF shifted focus to retail financing which includes small business loans, two-wheeler loans, auto loans, loans against gold, and personal loans. SCUF is one of the largest non-banking financial companies that lends to small businesses directly. It had 947 branches and total loans under management of INR275 billion at end-September 2020.

FINANCIAL SUMMARY (Consolidated)

Parameters	1HFY21	FY20	FY19
Total assets (INR billion)	327.5	332.3	313.6

Total equity (INR billion)	77.9	73.6	65.3
Net income (INR billion)	4.7	10.3	10.0
Return on average assets (%)	2.9	3.2	3.3
Debt/Equity (x)	3.1	3.4	3.7
Tier-I capital (%)*	30.1	27.69	22.75
Source: SCUF; *Standalone			

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook/Rating Watch		
	Rating Type	Rated Limits (billion)	Rating	4 May 2020	19 February 2020	7 March 2019
Issuer rating	Long-term/Short-term	-	IND AA/Stable/IND A1+	IND AA/RWN/IND A1+	IND AA/Stable/IND A1+	IND AA/Stable/IND A1+
Long-term debt programme	Long-term	INR0.05	IND AA/ Stable	IND AA/RWN	IND AA/Stable	IND AA/Stable
NCDs	Long-term	INR10.00	IND AA/ Stable	IND AA/RWN	IND AA/Stable	-
Bank loan	Long-term	INR150	IND AA/Stable	IND AA/RWN	IND AA/Stable	IND AA/Stable
Fixed deposit programme	Long-term	-	IND tAA/Stable	IND tAA/RWN	IND tAA/Stable	IND tAA/Stable

ANNEXURE

Instrument Type	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook
NCDs	INE722A07182	4 February 2011	10.75	4 February 2021	INR0.05	IND AA/Stable
NCDs	INE722A07AE0*	28 February 2020	9.25	28 May 2024	INR5.0	IND AA/Stable
NCDs	INE722A07AF7	28 February 2020	9.25	28 February 2023	INR5.0	IND AA/Stable
		Total			INR10.05	

*Partly paid NCD; debenture holders have subscribed for INR0.5 billion and they have right, but not obligation, to subscribe to an additional amount of INR4.5 billion on the completion of 15 months from initial deemed date of allotment.

COMPLEXITY LEVEL OF INSTRUMENTS

For details on the complexity level of the instruments please visit <https://www.indiaratings.co.in/complexity-indicators>.

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Ind-Ra currently maintains coverage of corporate issuers, financial institutions (including banks and insurance companies), finance and leasing companies, managed funds, urban local bodies and project finance companies.

Headquartered in Mumbai, Ind-Ra has seven branch offices located in Ahmedabad, Bengaluru, Chennai, Delhi, Hyderabad, Kolkata and Pune. Ind-Ra is recognised by the Securities and Exchange Board of India, the Reserve Bank of India and National Housing Bank.

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Applicable Criteria

[Financial Institutions Rating Criteria](#)

[Non-Bank Finance Companies Criteria](#)

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