June 05, 2023

Shriram Finance Limited (erstwhile Shriram Transport Finance Company Limited): Provisional ratings assigned to PTCs backed by vehicle loan receivables issued by Sansar Trust May 2023 III and second loss facility

Summary of rating action

Trust Name	Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Sansar Trust May 2023 III	PTC Series A	609.39	Provisional [ICRA]AAA(SO); Assigned
	Second Loss Facility	36.56	Provisional [ICRA]A-(SO); Assigned

Instrument details are provided in Annexure I

Rating in the absence of pending actions/documents	No rating would have been assigned as it would not be meaningful

Rationale

ICRA has assigned provisional ratings to the pass-through certificates (PTCs) and second loss facility (SLF) issued under a securitisation transaction originated by Shriram Finance Limited {SFL (erstwhile Shriram Transport Finance Company Limited)/originator; rated [ICRA]AA+ (Stable)}. The PTCs are backed by a pool of Rs. 609.39 crore (pool principal; receivables of Rs. 765.85 crore) of vehicle loan receivables.

The provisional ratings are based on the strength of the cash flows from the selected pool of contracts, SFL's track record in the vehicle loan business and the credit enhancement available in the form of (i) a credit collateral (CC) of 11.00% of the initial pool principal, (ii) excess interest spread (EIS) of 12.20% of the initial pool principal, and (iii) the integrity of the legal structure. The ratings are subject to the fulfilment of all the conditions under the structure and the review of the documentation pertaining to the transaction by ICRA.

Key rating drivers

Credit strengths

- Proven track record in pre-owned commercial vehicle (CV) financing segment along with a well-established franchise
- Availability of EIS and CC in the transaction
- Low obligor concentration with top 10 obligors accounting for only 0.8% of the overall pool principal amount

Credit challenges

- High share (i.e., ~57%) of contracts with internal rate of return (IRR) of more than 17%
- Performance of the pool would remain exposed to macro-economic shocks/business disruptions

Description of key rating drivers highlighted above

According to the transaction structure, the loan pool receivables will be assigned at par to the PTC investors. The promised cash flow schedule for PTC Series A on a monthly basis will comprise the interest (at the predetermined yield) on the outstanding PTC principal and the principal to the extent of 100% of the billed pool principal on each payout date. The excess available after meeting the promised and expected payouts to the PTCs will be passed on to the originator every month.

The first line of support for meeting the scheduled PTC payouts is the subordination of the EIS (amounting to 12.20% of the total initial pool principal, as per initial cash flows) in the structure. Further credit support is available through a CC of 11.00% of the pool principal amount (Rs. 67.03 crore). The CC will be split into a first loss facility (FLF) of 5.00% of the initial pool principal, amounting to Rs. 30.47 crore, and a second loss facility (SLF) of 6.00% of the initial pool principal amounting to Rs. 36.56 crore.

There are no overdues in the pool as on the cut-off date. The pool is well diversified with low obligor concentration and a weighted average seasoning of ~7 months. It comprises new and used commercial vehicle (new CV: ~13% and used CV: ~32%), new and used passenger vehicle (new PV: ~10% and used PV: ~37%), new and used construction equipment (new CE: ~2% and used CE: ~5%) and new and used tractor (new tractors: 0.1% and used tractors: ~2%) loan contracts. The pool has moderate geographical concentration with the top 3 states (Tamil Nadu, Andhra Pradesh and Karnataka) contributing ~35% to the initial pool principal amount. Contracts with an original tenure of more than 48 months account for ~22% of the pool. The pool has a high share of contracts (~57%) with IRR of more than 17%. Further, its performance would remain exposed to macro-economic shocks/business disruptions.

Past rated pools: ICRA has rated over 50 pools so far, backed by new & used CV, new & used PV, new & used CE and tractor loans originated by SFL. Overall, the performance of all live pools (which have completed at least two payouts) has remained healthy till the April 2023 payouts with good collections and loss-cum-180+ days past due (dpd) levels of sub-1.7%.

Key rating assumptions

ICRA's cash flow modelling for rating asset-backed securitisation (ABS) transactions involves the simulation of potential delinquencies, losses (shortfall in principal collection during the tenor of the pool) and prepayments in the pool. The assumptions for the loss and coefficient of variation (CoV) are arrived at after considering the performance of the originator's portfolio as well as the characteristics of the specific pool being evaluated. Additionally, the assumptions may be adjusted to factor in the current operating environment and any industry-specific factors that ICRA believes could impact the performance of the underlying pool of contracts.

After making these adjustments, the expected mean shortfall in principal collection during the tenure of the pool is estimated at 4.00-5.00% of the initial pool principal, with certain variability around it. The prepayment rate for the underlying pool is estimated at 18.0-24.0% per annum.

Liquidity position

For PTC Series A: Superior

The liquidity of the rated transaction is expected to be superior, supported by the healthy collections expected from the pool of contracts and the presence of a CC amounting to 11.00% of the pool principal amount. Even assuming a monthly collection efficiency of only 50% in the underlying pool of contracts in a stress scenario, the CC would cover the shortfalls in the scheduled PTC payouts for a period of six months.

For SLF: Strong

The cash flows from the pool and the available FLF are comfortable for the top-up of the SLF, if needed, as per the defined waterfall mechanism.

Rating sensitivities

Positive factors – Not applicable for the PTCs; the rating for the SLF can be upgraded on the sustained strong collection performance of the underlying pool of contracts, resulting in an increase in the credit enhancement cover available for the SLF.

Negative factors – Pressure on the ratings could emerge on the weakening collection performance of the underlying pool (monthly collection efficiency < 90% on a sustained basis).

Analytical approach

The rating action is based on the analysis of the performance of SFL's portfolio till December 2022, the key characteristics and composition of the current pool, the performance expected over the balance tenure of the pool, and the credit enhancement cover available in the transaction.

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Securitisation Transactions
Parent/Group support	Not Applicable
Consolidation/Standalone	Not Applicable

Pending actions/documents required to be completed for conversion of the provisional rating into final

The assigned ratings are provisional and would be converted into final upon the execution of:

1. Trust deed
2. Assignment agreement
3. Legal opinion
4. Trustee compliance letter
5. Chartered Accountant's know your customer (KYC) certificate
6. Any other documents executed for the transaction

Validity of the provisional rating

The Trust is expected to complete the pending actions/execute the pending documents in the near term. However, in case of continued pendency of the actions/documents beyond one year of this publication, the provisional ratings would be withdrawn for the transaction even if the instrument has been issued.

Risks associated with the provisional rating

In case the issuance is completed, but the pending actions/documents are not completed for the transaction within one year (validity period) from the assignment of the ratings, the provisional ratings will be withdrawn in accordance with ICRA's Policy on Provisional Ratings available at www.icra.in.

About the company

Shriram Finance Limited [SFL; erstwhile Shriram Transport Finance Company Limited (STFC)], incorporated in 1979, is a part of the Shriram Group of companies and is a top-layer non-banking financial company (NBFC). Based on the National Company Law Tribunal (NCLT) order dated November 14, 2022, the operations of Shriram City Union Finance Company Limited (SCUF) and Shriram Capital Limited were merged with STFC and the resultant entity was rechristened Shriram Finance Limited on November 30, 2022.

SFL enjoys a leadership position in pre-owned commercial vehicle finance and has a pan-India presence with 2,910 branches. As of December 31, 2022, its consolidated assets under management (AUM) was Rs. 1.8 lakh crore, comprising pre-owned commercial vehicle finance (76%), small and medium-sized enterprise (SME) lending (10%), personal loans (3%), gold loans (2%), two-wheeler loans (5%) and housing finance (4%; through its subsidiary – Shriram Housing Financing Limited).

In 9M FY2023, on a consolidated basis, SFL reported a net profit of Rs. 4,726 crore on AUM of Rs. 1,84,678 crore and its net worth was Rs. 41,140 crore[#]. On a standalone level, the company reported a profit after tax (PAT) of Rs. 4,671 crore on AUM of Rs. 1,77,498 crore. Its reported capital adequacy stood at 22.99% as of December 31, 2022.

Key financial indicators

	FY2021*	FY2022*	9M FY2023^
Particulars	**Audited**	**Audited**	**Provisional**
Net worth	21,568	25,932	41,140#
Profit after tax	2,487	2,708	4,726
Assets under management (AUM)	1,17,243	1,27,041	1,84,678
Gross stage 3	7.1%	7.1%	6.1%
Net stage 3	4.2%	3.7%	3.2%

Source: Company, ICRA Research; All ratios are as per ICRA's calculations; Amount in Rs. crore
**For SFL, prior to the merger with SCUF and SCL; ^Consolidated, post-merger*
#Adjusted for goodwill of Rs. 1,408.6 crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Trust Name	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years		
		Instrument	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					June 05, 2023	-	-	-
1	Sansar Trust May 2023 III	PTC Series A	609.39	609.39	Provisional [ICRA]AAA(SO)	-	-	-
		Second Loss Facility	36.56	36.56	Provisional [ICRA]A-(SO)	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
PTC Series A	Simple
Second Loss Facility	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

Trust Name	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date*	Amount Rated (Rs. crore)	Rating
Sansar Trust May 2023 III	PTC Series A	May 2023	8.75%	June 2028	609.39	Provisional [ICRA]AAA(SO)
	Second Loss Facility	May 2023	NA	June 2028	36.56	Provisional [ICRA]A-(SO)

** Scheduled PTC maturity date at transaction initiation; may change on account of prepayments*
Source: Company

Annexure II: List of entities considered for consolidated analysis

Not Applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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