December 29, 2023

Shriram Finance Limited: Provisional ratings assigned to PTCs backed by vehicle loan receivables issued by Sansar Trust Dec 2023 III and second loss facility

Summary of rating action

Trust Name	Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Sansar Trust Dec 2023 III	Series A PTCs	252.17	Provisional [ICRA]AAA(SO); Assigned
	Second loss facility	13.87	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) issued under a securitisation transaction originated by Shriram Finance Limited {SFL/originator; rated [ICRA]AA+ (Stable)}. The PTCs are backed by a pool of Rs. 252.17-crore (pool principal; receivables of Rs. 317.85 crore) 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 (CE) available in the form of (i) a credit collateral (CC) of 10.50% of the initial pool principal (Rs. 26.48 crore) and (ii) excess interest spread (EIS) of 12.54% of the initial pool principal in the structure (Rs. 31.61 crore), as well as 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 preowned commercial vehicle (CV) financing segment along with a well-established franchise
- Availability of CE in the form of EIS and CC in the transaction
- Low obligor concentration with the top 10 obligors accounting for 0.55% of the overall pool principal amount

Credit challenges

- Significant share of contracts with high IRR (internal rate of return) and loan-to-value (LTV) in the pool
- Performance of the pool would remain exposed to macroeconomic shocks/business disruptions

Description of key rating drivers highlighted above

As per the transaction structure, the scheduled cash flow promised to Series A PTCs on each payout date will comprise the interest payments to Series A PTCs at the predetermined interest rate on the principal outstanding while the monthly principal payments will be on expected basis and are promised on the final maturity date. The collections from the pool, after making the promised interest payouts to Series A PTCs, will be utilised to make the expected principal payments to Series A PTCs (100% of the pool principal billing). However, this principal payout is not promised and any shortfall in making the expected principal payment to Series A PTCs would be carried forward to the subsequent payout.

The loan pool receivables will be assigned at par to the PTC investors. The originator's claim in the EIS is subordinated to the PTC payouts. Thus, the EIS (amounting to 12.54% of the initial pool principal) acts as a source of CE in the transaction. After meeting the promised and expected payouts, the EIS will be passed on to the originator on a monthly basis. A CC equivalent to 10.50% of the initial pool principal also acts as CE in the transaction. The CC will be split into a first loss facility (FLF) of 5.00%

of the initial pool principal (Rs. 12.61 crore) and a second loss facility (SLF) of 5.50% of the initial pool principal amounting to Rs. 13.87 crore. The FLF and SLF would be in the form of a fixed deposit maintained with a designated bank acceptable to ICRA. However, SFL might replace the fixed deposit with a bank guarantee later, subject to the guarantor and the terms of the guarantee being acceptable to ICRA.

There are no overdues in the pool as on the cut-off date. The pool is well diversified with low obligator concentration and a weighted average seasoning of 8.3 months. It comprises new and used CV (new CV: 7.9% and used CV: 12.0%), new and used passenger vehicle (new PV: 19.5% and used PV: 25.9%), two-wheeler (34.7%) loan contracts. The pool has moderate geographical concentration with the top 3 states (Maharashtra, Uttar Pradesh and Andhra Pradesh) contributing 41.2% to the initial pool principal amount. It also has a significant share of contracts with high LTV and IRR. Further, the pool's performance would remain exposed to macroeconomic shocks/business disruptions.

Past rated pools: ICRA has rated over 50 pools so far, backed by new & used CV, new & used PV, new & used construction equipment 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 November 2023 payout, with a cumulative collection efficiency of more than 100%.

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 average prepayment rate for the underlying pool is estimated at 12.00% per annum.

Liquidity position:

For Series A PTCs: Superior

As per the transaction structure, only the interest amount is promised to Series A PTCs on a monthly basis while the principal amount is promised on the scheduled maturity date of the transaction. The cash flows from the pool and the available CE are expected to be comfortable to meet the promised payouts to the Series A PTCs investors.

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 CE cover available for the SLF.

Negative factors – The sustained weak collection performance of the underlying pool of contracts (monthly collection efficiency <90%), leading to higher-than-expected delinquency levels and higher CE utilisation levels, would result in a rating downgrade. Weakening in the credit profile of the servicer could also exert pressure on the ratings.

Analytical approach

The rating action is based on the analysis of the performance of SFL's portfolio till September 2023, the key characteristics and composition of the current pool, the performance expected over the balance tenure of the pool, and the CE 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 rating, the provisional ratings will be withdrawn in accordance with ICRA's Policy on Provisional Ratings available at www.icra.in.

About the originator

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, which was rechristened Shriram Finance Limited on November 30, 2022.

SFL enjoys a leadership position in preowned commercial vehicle finance and has a pan-India presence with 2,975 branches and 708 rural centres. As of September 30, 2023, SFL had consolidated assets under management (AUM) of Rs. 2,02,641 crore comprising preowned CV finance (49%), PV loans (19%), construction equipment (7%), farm equipment (2%), small and medium enterprise (SME) lending (11%), personal loans (4%), gold loans (3%) and two-wheeler loans (5%).

The company reported a profit after tax (PAT) of Rs. 3,426 crore on AUM of Rs. 2,02,641 crore in H1 FY2024. The gross stage 3 stood at 5.79% while the net stage 3 was 2.80% in Q2 FY2024. SFL reported a PAT of Rs. 1,675 crore and a net worth of Rs. 44,821 crore in Q1 FY2024. The company is adequately capitalised with a capital-to-risk weighted assets ratio (CRAR) of 22.15% in Q2 FY2024. Total outstanding borrowings stood at Rs. 1,653 billion with bank term loans and public deposits forming ~50% of the total borrowings as of September 30, 2023.

Key financial indicators (SFL)

Particulars	FY2022*	FY2023^	H1 FY2024^
	Audited	Audited	Audited
Net worth	25,932	43,306	46,035
Profit after tax	2,708	5,979	3,426
Assets under management (AUM)	1,27,041	1,85,683	2,02,641
Gross stage 3	7.1%	6.2%	5.8%
Net stage 3	3.7%	3.2%	2.8%

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*

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
					Dec 29, 2023	-	-	-
1	**Sansar Trust Dec 2023 III**	Series A PTCs	252.17	252.17	**Provisional [ICRA]AAA(SO)**	-	-	-
		Second loss facility	13.87	13.87	**Provisional [ICRA]A-(SO)**			

Complexity level of the rated instrument

Instrument	Complexity Indicator
Series A PTCs	Moderately Complex
Second loss facility	Moderately Complex

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)	Current Rating
Sansar Trust Dec 2023 III	Series A PTCs	Dec 2023	8.75%	May 2028	252.17	Provisional [ICRA]AAA(SO)
	Second loss facility		Residual	May 2028	13.87	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.

For more information, visit www.icra.in

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