Investment in Shriram Finance Limited, a Leading Non-Banking Financial Company in India

Main Q&A

Q. Will the size of share repurchases decrease going forward due to this investment? What is your view on future growth investment?

A. The basic policy on share repurchases remains unchanged. We will take flexible actions depending on our financial results, foreign exchange fluctuations, and capital ratios, while balancing shareholder returns and growth investments. Since the investment was still under discussion and not finalized when we announced our second-quarter results, its effects were not included in our second-half CET1 ratio outlook. However, we were considering possible increases in RWA and certain growth investments. Therefore, the expected negative impact on MUFG's CET1 ratio coming from this investment is about 60bps, but this does not mean a direct decline from our second-quarter outlook. We acknowledge concerns about the effect on share repurchases. With profits exceeding 2.0 trillion yen annually, we will reassess toward the end of the fiscal year. We remain committed to growth investments within our CET1 ratio target range.

Q. Why did you choose Shriram Finance as your partner?

A. Over four years, we evaluated various opportunities in India. We believe Shriram Finance can sustain growth due to its quality of management, competitive edge, talented staff, and corporate culture. This is evidenced by consistently achieving ROE above 15% for three consecutive years. The company's growth was previously constrained by capital constraints, as it is not part of a larger conglomerate or banking group. We anticipate that our investment will help overcome these constraints and boost its growth. As the global economy becomes more protectionist, entering the Indian market—known for its robust domestic demand—holds significant strategic value for us. Using our ASEAN investment experience, we will foster strong relationships to support its development.

Q. The timeline for contributing to the mid- to long-term ROE target of approximately 12% seems rather long. Could it be accelerated if the synergy effect increases?

A. Like our existing investments, we base our decisions on business plans with conservative assumptions. The timeline for contributing the ROE above 12% during the medium-term business plan after the next is also built on these cautious assumptions. If actual results surpass the plan, the timeline can be moved forward.

Q. What is the amount of goodwill and the amortization period? Which indicators can we reference to confirm the company's growth?

A. The goodwill amount is over ¥350 billion based on the current exchange rate, and we are assuming an amortization period of around 10 to 15 years. The company has a monoline business focused on a specific area and business growth can be verified by loan balances, NIM, and credit cost, among other factors. Its business operates in an area with high credit risk, but credit cost is reduced to a level comparable to its peers through systematic responses, such as data expansion in credit scoring.

Q. Is there a possibility of additional investment? Also, will there be a change to DMI Finance's investment policy due to this investment?

A. The regulatory restriction on investing more than 20% in a non-banking financial company (NBFC) in India was lifted with the regulatory revision earlier in December, although it still needs approval from the Reserve Bank of India (RBI). No decision has been made yet on increasing the investment ratio. We will proceed with this investment, focusing on business management through appointing directors and realizing potential synergy effects. Our emphasis will be on building "confidence" and "trust" in collaboration with the company. "Confidence" pertains to belief in a strong business platform that meets our expectations, while "trust" involves strengthening the relationship with the founder and management established through the process of discussions and negotiations for this investment. Once these are established, we may explore various investment options.

Our investment policy for DMI Finance remains unchanged. Shriram Finance and DMI Finance operate in different segments, with distinct models and channels. We do not plan to change our strategy towards DMI Finance due to this investment. Instead, we aim for the growth of both Shriram Finance and DMI Finance aligned with their respective business models.

Q. Enhancing funding capacity through improved creditworthiness was listed as one of the strategic rationales. What were the results of past investments?

A. In the past, some rating agencies upgraded the standalone ratings of Bank of Ayudhya and Bank Danamon by approximately two notches due to the potential support from their parent company. This upgrade helped lower the cost of funds for both banks. We anticipate that Shriram Finance's funding costs will also decline as its creditworthiness improves following the preferential allotment.

Q. Could Shriram Finance holding a deposit license while operating as an NBFC lead to any constraints not applicable to its peers?

A. Through due diligence, it has not been confirmed any disadvantages associated with holding a deposit license. Transactional deposits might necessitate infrastructure development, such as systems setup. However, Shriram Finance provides investment-type term deposits with longer durations, so we believe no additional constraints are applicable.

Q. How will the domestic economy in India affect Shriram Finance's business?

A. Micro, Small, and Medium Enterprises (MSME) and retail segments are the primary customer segments for the company, and the status of the Indian economy may influence them to some extent. However, because the company focuses on business finance rather than consumer finance, including support for last-mile land transport delivery, the impact would be limited. The logistics sector is experiencing steady growth due to increased domestic infrastructure investment in India, which has resulted in strong performance by Shriram Finance. We will continue to closely monitor the Indian economy and the demand for social infrastructure. This investment diversifies GCB's mid- to long-term business portfolio and is expected to stabilize MUFG's revenue.

Q. What is your opinion of the Shriram Finance management?

A. The founder still retains some influence over management, making this a key point to monitor. While our due diligence confirmed this, they also let us know they have a strong succession plan. Additionally, shares once owned by the founder are now held in custody by the Group trust corporation, which was set up to manage shares held by Group companies, with both current and former management serving as trustees. This demonstrates that the company operates without a single leader and has a collaborative management structure.

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