Dip in MSME, tractor and micro loan pool collections in November 2016, collections in other asset classes relatively stable

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Contents

Executive summary

Following the Government of India's (GoI) demonetisation decision on November 8, 2016, there has been a temporary disruption in the liquidity available in the hands of people, which in turn has impacted economic activity in the near term. NBFCs' inability to accept repayments in old currency, shortage of valid currency among borrowers, and disruption in borrowers' regular business, especially the cash-intensive ones, resulted in an adverse impact on the collection efficiency in the various retail loan pools securitised by NBFCs. The extent of impact has varied across asset classes.

ICRA's analysis of 182 live securitisation transactions[1] across various asset classes like Commercial Vehicle (CV), Tractor, Micro Small and Medium Enterprises (MSME), Micro loans, Home Loans (HL) and Loan against Property (LAP) reveals that:

- Micro Loan, MSME loan and Tractor loan pools witnessed a sharp decline in collections. While collection in micro loan sector is almost entirely in cash, collections in case of MSME loans of smaller ticket size and tractor loans also largely happens in cash.
  - Median monthly collections[2] of micro loan pools declined to ~91% from 99.8% till September 2016. Collections of some pools declined to 50%-70% levels. The 0+ dpd[3] level in micro loan pools that was sub 0.5% until October 2016 spiked to 9% in November 2016.
  - The collection efficiency in ten pools dipped to less than 70%, nine of which belonged to a single Originator. All these pools had sizable share of contracts originated in Uttar Pradesh and Madhya Pradesh, where the collections were adversely impacted following political intervention by some local leaders and rumours of loan waivers.
  - High collection efficiency was reported in pools with weekly repayment cycles or for pools where collections were mostly completed prior to the announcement on demonetisation.
- Collections in MSME loan pools also witnessed a sharp decline to 83% from 95% in the previous month. Here again, some pools saw collections declining to 40%-70% levels from 70%- 90% levels earlier. Though the average 0+ dpd level increased to 11% in November 2016 from 5.3% in October 2016, the increase in 30+ dpd level was very low.
  - All seven pools with collections below 70% in November 2016 had a high share of loans with ticket size of less than Rs. 3 lakh, a sub-segment where a sizable portion of the collections are in cash.
- Median collections across tractor loan pools declined to 84% in November 2016 from around 95% in the previous month. 0+ dpd level increased to 16.5% from 14.5% in October 2016, while the 30+ dpd level remained largely stable. Due to currency shortage, farmers either faced a loss of income due to reduced off-take (for perishable food items like fruits and vegetables) or delayed realisations (many farmers were forced to deposit their produce with the mandis on credit).
- LAP collections declined to a small extent
  - Collections in LAP pools declined from 97% in October 2016 to 94.6% in November 2016. While the 0+ dpd level increased slightly, other delinquency buckets did not get impacted much. However, the monthly prepayment level declined to an average of 1.3% from a level of 2.1% seen till September 2016.

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[1] Data was available for the month of November 2016 for 182 pools out of a total of 248 live pools
[2] Calculated as (collections during the month including collections from overdue contracts) / (billing for the month)
[3] Calculated as (principal outstanding for contracts that are overdue) / (balance pool principal)

- Collections in CV and HL pools were not much affected
    - Collections in HL pools remained largely unaffected. Similarly, collections in CV loan pools remained resilient. However, softer delinquencies inched up a bit in these asset classes as well.
    - Prepayment in November 2016 declined.

In November, some of the retail loan pools were not impacted much either because the borrower(s) paid the installment from the earnings of the previous month/ savings or because the installment date fell before or very close to the date of demonetisation announcement. Also, acceptance of old currency notes in petrol pumps and waiver of toll charges benefitted the CV operators in the month of November. Nevertheless, the impact on performance of these operators in the next few months, in absence of these short-term allowances remains to be seen.

In ICRA's opinion, the performance of the retail loan pools in November 2016 is not a full reflection of the extent of disruption pursuant to the demonitisation exercise. The performance of the ICRA rated pools going ahead will depend primarily on the restoration of currency supply in the system, the degree of impact on the borrower's business volumes and cashflows over the medium to long term. Therefore, the performance of these pools over the next three months i.e. from December 2016 to February 2017 will be crucial. ICRA will continue to closely monitor the collections and delinquency profile of the underlying loans in the pool together with the adequacy of credit enhancement in these transactions to take appropriate rating actions, as may be warranted.

1. Micro Loan Pools

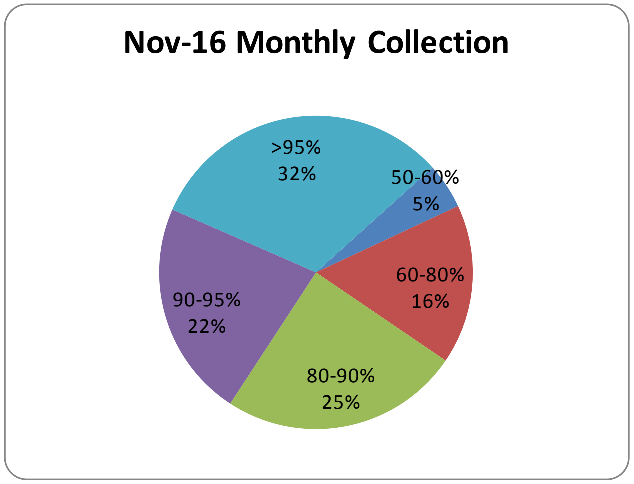
Asset class	Joint Liability Group (JLG) based micro loans originated by NBFC-MFIs
Ticket size	Rs. 10,000 to Rs. 60,000
Security	Unsecured
Borrower profile	All-women groups of small and marginal micro-entrepreneurs, daily wage workers, vegetable vendors, et al
Repayment mode	Almost entirely in cash
Nov-16 analysis based on	85 pools across 22 Originators (out of 111 live pools)

Exhibit 1: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*99.8%*	99.9%	99.7%	91.3%
Prepayment Rates	*0.1%*	0.1%	0.4%	0.1%

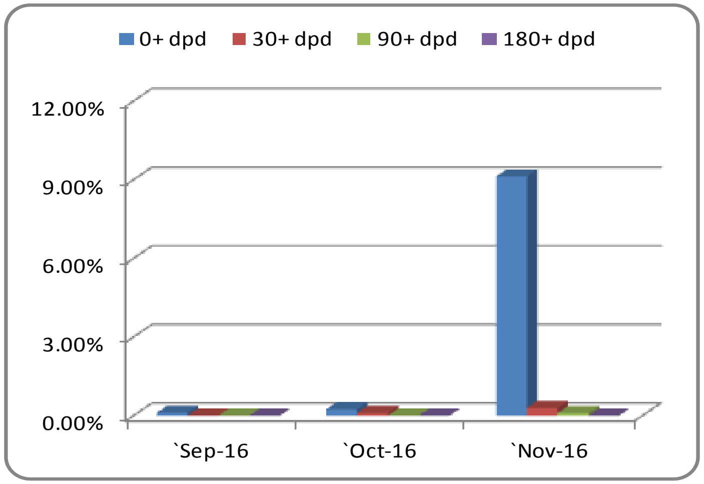
Source: ICRA Research

Exhibit 2: Distribution of pools based on Nov-16 monthly collection



Source: ICRA Research

Exhibit 3: Month-wise Delinquency profile



Collection efficiency in Micro Loan pools dips to ~91% in November 2016; spike in softer delinquency buckets

The median monthly collection efficiency for the month of November 2016 declined to 91.3%, from the near 100% cumulative collection efficiency till October 2016. In case of micro loans, the underlying borrowers are typically micro-entrepreneurs, daily wage workers or small vendors engaged in cash-intensive businesses. These borrowers, more often than not, either do not have a bank account or are not adequately familiar and comfortable in transacting through banking channels. Immediately after the demonetisation announcement on November 8, 2016, most of these borrowers were stuck with the old currency notes that couldn't be accepted by the MFIs. and were unable to get these notes exchanged from the bank branches quickly.

However, some MFIs that had monthly instalments falling due in the first week of month reported strong performance. Most MFIs actively helped their customers in exchanging old currency notes and also in opening bank accounts and transacting through them. The MFIs with a weekly billing cycle and consequently a smaller EWI (equated weekly instalments) amount also reported better collection levels (more than 95% collection efficiency), as borrowers found it easier to repay smaller weekly instalment compared with larger monthly instalments. As exhibit 2 above, one-third of the pools analysed had collection efficiency of more than 95% in November 2016 (around 80% in October, 2016).

In November 2016, collection efficiency of ten pools dipped to less than 70%, nine of which belonged to a single Originator. All these ten pools have a sizable share of contracts originated in Uttar Pradesh and Madhya Pradesh, where the collections were adversely impacted following political intervention by some local leaders and rumours of loan waivers.

Exhibit 3 above shows the movement in 0+ dpd, 30+ dpd, 90+ dpd and 180+ dpd levels on an average across all the pools rated by ICRA. Till Sep-16[4], while most transactions had nil delinquency, no micro loan transaction reported a loss cum 0+ dpd level of more than 3.8% and loss-cum-30+ dpd of more than 2.0%. However, post demonetisation, there has been a sharp rise in the average 0+ dpd level from sub 0.5% in October 2016 to around 9% in November 2016. The real impact of the cash shortage on the livelihoods of the underlying borrowers will be known only over the next few months. Thus, the performance of the micro loan pools going ahead will depend on several factors like replenishment of currency supply in the system, improvement in the livelihood situation of the borrowers, and the quality of customer engagement by the MFIs. The degree of recovery from the payments missed in November 2016 will also be a key monitorable.

Though the prepayments have conventionally been low for this asset class, most originators saw a further reduction in the monthly prepayment rate in November 2016 compared with the preceding month. In November 2016, nine pools had prepayment rate in excess of 2% in comparison with 25 pools in October 2016. Five of these pools belonged to two MFIs that have historically observed relatively higher prepayment rates.

[4] As per ABS Pool Performance Note, released by ICRA in December 2016

2. Micro, Small and Medium Enterprises Pools Loan Pools

Asset class	Business loans to MSMEs
Ticket size	Largely in the range of Rs. 50,000 to Rs. 15 lakhs
Security	Largely secured through charge on property (primarily residential) or machinery; small share of unsecured loans as well
Borrower profile	Micro, small and medium enterprises (mostly Tier II and Tier III ancillary units) engaged mainly in engineering, auto ancillary, power loom, dairy, services and plastic industries
Repayment mode	Pre-dominantly PDC or EC; cash to a small extent in smaller ticket loans
Nov-16 analysis based on	23 pools across 8 Originators (out of 27 live pools)

Exhibit 4: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*98.5%*	95.2%	94.6%	83.4%
Prepayment Rates	*0.8%*	1.8%	1.1%	1.1%

Source: ICRA Research

Exhibit 5: Bucket–wise monthly collection efficiency

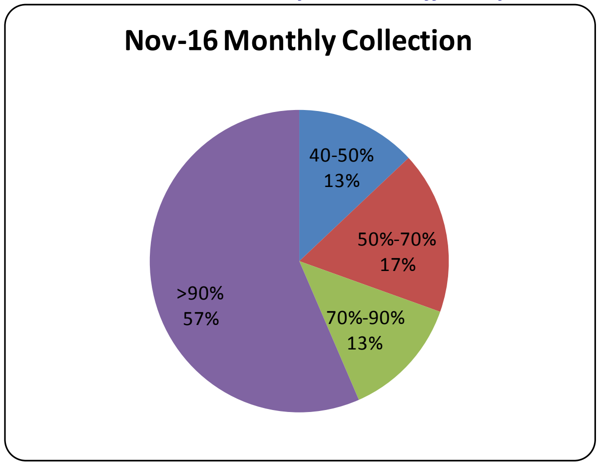
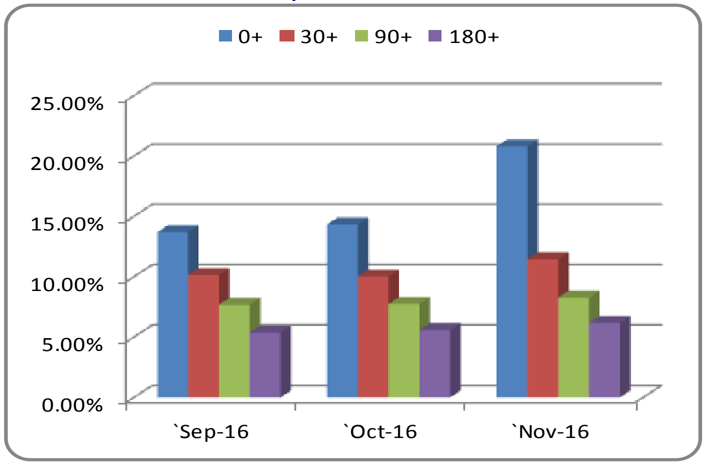


Exhibit 6: Bucket-wise delinquencies



Source: ICRA Research

Collection efficiency in MSME pools dips to ~83%; sharp build-up in delinquency

The average monthly collection efficiency for the MSME asset class declined to 83% in November 2016 from 95% in the previous month. In November 2016, 57% of the pools (compared with 70% in October 2016) reported collection efficiency of more than 90%. While no pool reported collection efficiency of less than 70% in October 2016, the share of such pools was around 30% in November 2016. Three pools witnessed collection efficiency of less than 50% in November 2016. These pools had a high share of loans with ticket size of less than Rs. 3 lakh, a sub-segment where a sizable portion of the collections happen in cash.

Payments from borrowers making repayments through the banking channel also suffered. This is because the cashflows of some of the borrowers got adversely impacted given the cash intensive nature of their business or on account of subdued demand. Consequently, these borrowers had lower surplus for making the loan repayments. Nevertheless, large portion of these loans are backed by some asset and are highly seasoned. As a result, these loans would have a substantial equity build up by now and eventual losses to the financier should be low.

MSME pools have a high share of loans in 1-30 dpd bucket owing to some instances of cheque bounces (read insufficient money in the bank account owing to poor banking habits). Hence, this bucket is a soft delinquency bucket for this asset class, owing to high reversals. Nevertheless, ICRA has analysed movement in 0+ dpd level to study the immediate impact of demonetisation. It can be observed from Exhibit 6 above that there is a jump in average 0+ dpd level to around 21% in November 2016 from around 14% in the previous month. Slight increase in 30+ dpd level is also seen, as some borrowers that would have otherwise cleared their dues may not have been able to do so owing to liquidity issues and hence would have flowed forward from the 1-30 dpd bucket.

Only four pools out of 23 MSME pools analysed comprised of unsecured loans. However, the performance of these pools remained strong in November 2016 and was even better compared to the performance of secured pools. This is because there was low reliance on cash collections in all these pools.

The monthly prepayment rate was 1.1% in November 2016 (same as the prepayment level in October 2016).

3. HL Pools

Asset class	Home Loans
Ticket size	Largely in the range of Rs. 5 lakhs to Rs. 1 crore
Security	Mortgage on underlying security, primarily residential
Borrower profile	Individuals (salaried and self-employed) and small & medium enterprises
Repayment mode	Pre-dominantly PDC or ECS
Nov-16 analysis based on	22 pools across 7 Originators (out of 32 live pools)

Exhibit 7: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*99.2%*	101.5%	98.3%	98.1%
Prepayment Rates	*0.6%*	1.0%	1.0%	0.5%

Source: ICRA Research

Exhibit 8: Bucket–wise monthly collection efficiency

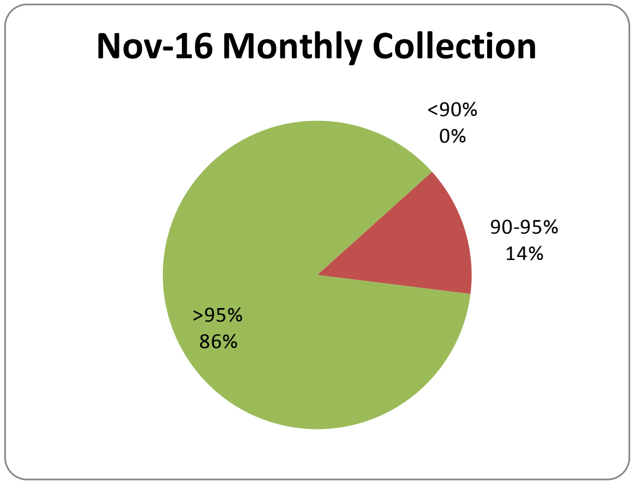
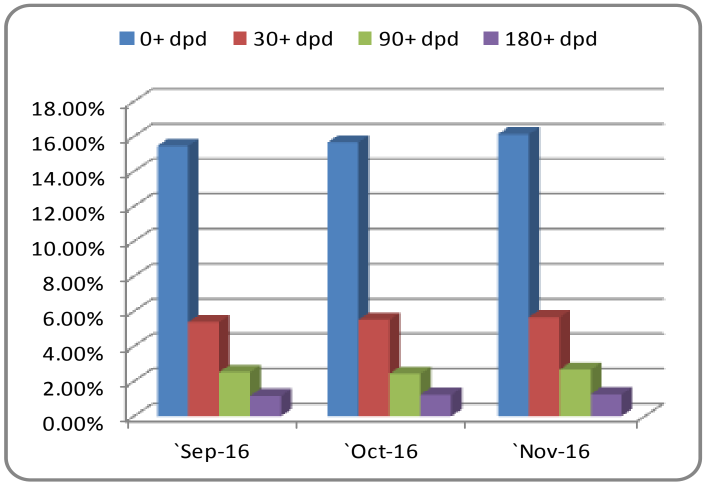


Exhibit 9: Bucket-wise delinquencies



Source: ICRA Research

No material impact in collection efficiencies; marginal build-up in delinquency

The average monthly collection efficiency for HL pools in November 2016 is largely comparable to the months prior to demonetization. For November 2016, 19 pools (compared with 21 in October 2016) had a collection efficiency of more than 95%. Only three pools had a collection efficiency of less than 95% while none of the pools had collection efficiency of less than 90% in November 2016. The pools impacted to some extent belonged to HFCs that cater to low income borrowers that may have limited cushion to meet unforeseen expenses, and hence potentially more impacted by the demonetization action.

HL pools primarily consist of borrowers that make repayments through the banking channels. Many borrowers are salaried and receive salary credits in the bank account. The ability of these borrowers to pay remained largely unaffected on account of demonetisation. Historically, this asset class has shown resilience to stress in the operating environment, given that most of the houses purchased are for self-occupation.

Exhibit 9 above shows the movement in various delinquency buckets across the HL pools rated by ICRA. It can be observed that 0+ dpd level has seen only a marginal increase from around 15% in October 2016 to around 16% in November 2016. There has not been any material impact on the other delinquency buckets.

However, the rated pools have seen a decline in the monthly prepayment rate in November 2016 (to 0.5% from 1.0% in October 2016).

4. LAP Pools

Asset class	Loans against Property
Ticket size	Largely in the range of Rs. 10 lakhs to Rs. 2 crore
Security	Mortgage on underlying security, either residential or commercial
Borrower profile	Individuals (salaried and self-employed) and small & medium enterprises
Repayment mode	Pre-dominantly PDC or ECS
Nov-16 analysis based on	12 pools across 4 Originators (out of 17 live pools)

Exhibit 10: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*97.2%*	101.4%	96.9%	94.6%
Prepayment Rates	*2.1%*	2.1%	3.0%	1.3%

Source: ICRA Research

Exhibit 11: Bucket–wise monthly collection efficiency

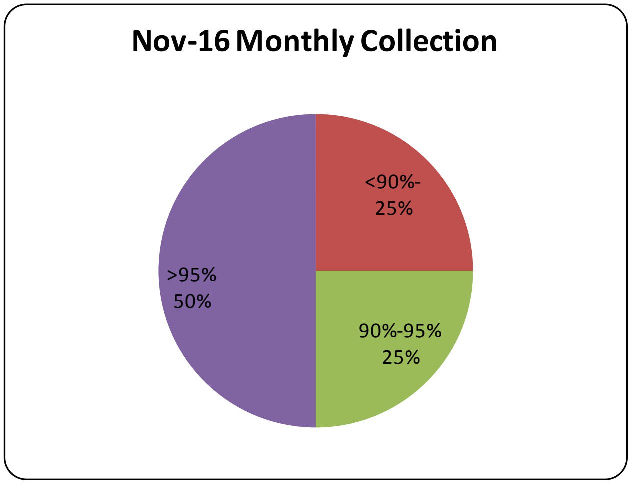
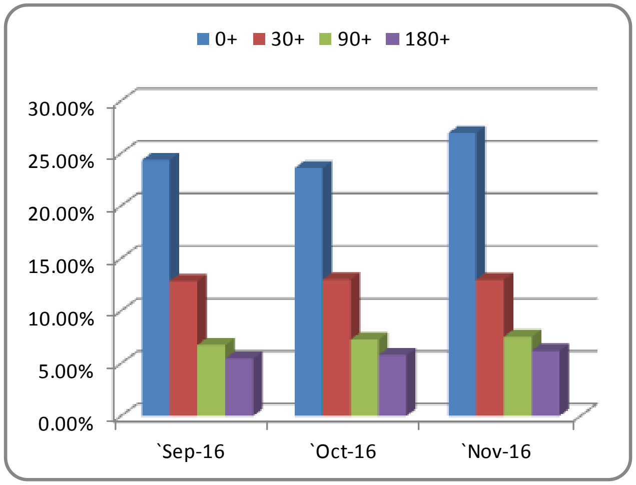


Exhibit 12: Bucket-wise delinquencies



Source: ICRA Research

Minor decline in collection efficiencies; moderate build-up in delinquency

The average monthly collection efficiency of LAP pools declined in to 95% November 2016 from 97% in the previous month. In November 2016, 50% of the pools (compared with 75% for October 2016) had collection efficiency of more than 95%. While only one pool had collection efficiency below 90% in October 2016, three pools reported collection efficiency below 90% in November 2016.

The LAP pools primarily consist of borrowers making repayments through the banking channels. However, these loans are taken for business purpose by self-employed individuals/ small business units. Any adverse impact on cashflows/ business of these borrowers in the coming months could impact the performance of these pools going forward.

LAP pools also have a notable share of contracts in 1-30 dpd bucket owing to some cash flow mismatches in the borrower's business, or delay in receiving some payment. Hence, this bucket witnesses significant reversals and cannot be seen as a hard bucket for this asset class. Nonetheless, ICRA has analysed the movement in 0+ dpd bucket to assess the immediate impact of demonetisation. It can be observed that the average 0+ dpd level saw a moderate increase to 27% in November 2016 from 24% in October 2016.

As per the prepayment data available for November 2016, it can be observed that the monthly prepayment rates have reduced to almost half (1.3%) of the levels seen till September 2016 (2.1%). This could be due to the lower availability of surplus cash in the hands of borrowers post demonetization, and fewer instances of balance transfer cases. Business volumes for most lenders has come down significantly post demonitisation due to reduced demand and enhanced focus on collections till the time normalcy returns.

5. Commercial Vehicle Pools

Asset class	Commercial Vehicles[5]
Ticket size	Largely in the range of Rs. 2.0 lakhs to Rs. 50.0 lakhs
Security	Charge over the underlying vehicle financed
Borrower profile	Fleet operators, small truck operators, individuals
Repayment mode	Mix of both PDC or ECS and Cash
Nov-16 analysis based on	29 pools across 7 Originators (out of 46 live pools)

Exhibit 13: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*95.5%*	93.5%	93.0%	94.0%
Prepayment Rates	*0.5%*	1.2%	1.2%	0.9%

Source: ICRA Research

Exhibit 14: Bucket–wise monthly collection efficiency

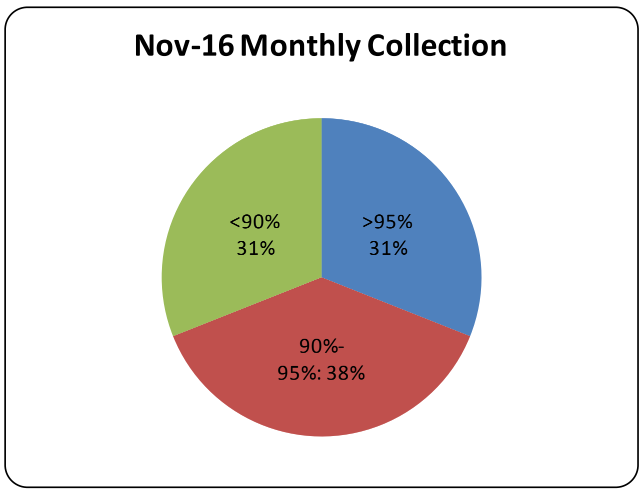
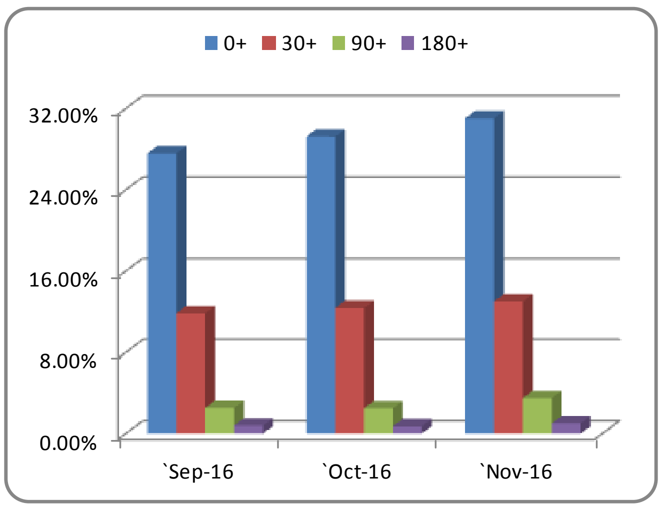


Exhibit 15: Bucket-wise delinquencies



Source: ICRA Research

[5] Some pools are mixed pools having a minority share of Construction Equipment (CE), Car and Tractor loans as well

No material impact on collection efficiencies; small build-up in delinquency

The performance of most CV loan pools in November 2016 has not been impacted much on account of demonetization. The median collection efficiency for the month of November 2016 was 94.0% compared to 93.0% in the previous month. In case of CV loans, the underlying borrowers are primarily from varied categories of small truck owners to large fleet operators. Businesses of some of the underlying borrowers, who transact and repay through the formal banking channels, was impacted to some extent in November 2016 but they were able to pay the November instalments on time from the earnings in the previous month.

Some of the customers resorted to collecting full freight amounts in advance from their principals to meet their operating expenses. Lenders worked pro-actively to help their customers exchange old currency notes that helped curtail the damage to a large extent. Also, acceptance of old currency notes in petrol pumps and waiver of toll charges benefitted the CV operators in the month of November. The impact on performance of these operators in the next few months with these short term dispensations going away remains to be seen and would be a key monitorable.

Nine pools (31% of the analysed pools) had collection efficiency of more than 95% in November 2016 compared to 12 pools (41% of the analysed pools) in October 2016. The performance of CV pools going ahead will depend primarily on uptick in economic activity, and movement in freight rates and fuel prices over the next few months.

Exhibit 15 above shows the movement in average 0+ dpd, 30+ dpd, 90+ dpd and 180+ dpd levels across the pools rated by ICRA. It can be observed from the chart above that there has been a small rise in delinquencies across all buckets.

Though prepayment rates have conventionally been low in case of CV loans, most originators saw a further reduction in the monthly prepayment rate in November 2016 compared to the preceding month.

6. Car Pools

Asset class	Cars
Ticket size	Rs. 1 lakh – Rs. 10 lakh
Security	Charge over the underlying vehicle financed
Borrower profile	Self-employed
Repayment mode	Mix of both PDC/ ECS and Cash
Nov-16 analysis based on	3 pools across 1 Originator (out of 3 live pools)

Exhibit 16: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*93.0%*	97.0%	89.2%	84.3%
Prepayment Rates	*0.6%*	0.7%	0.6%	0.5%

Source: ICRA Research

Exhibit 17: Bucket–wise monthly collection efficiency

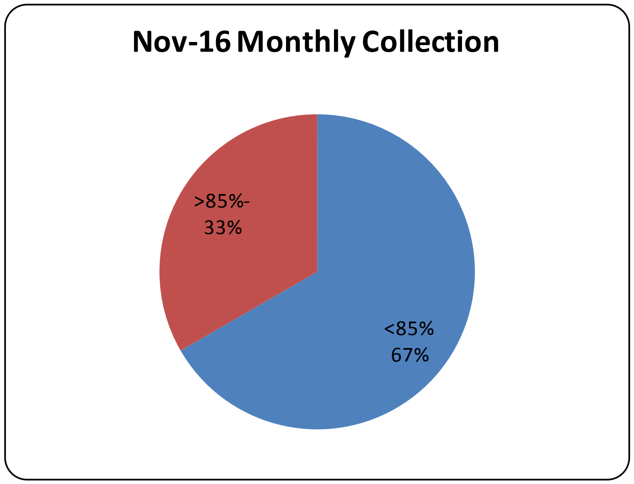
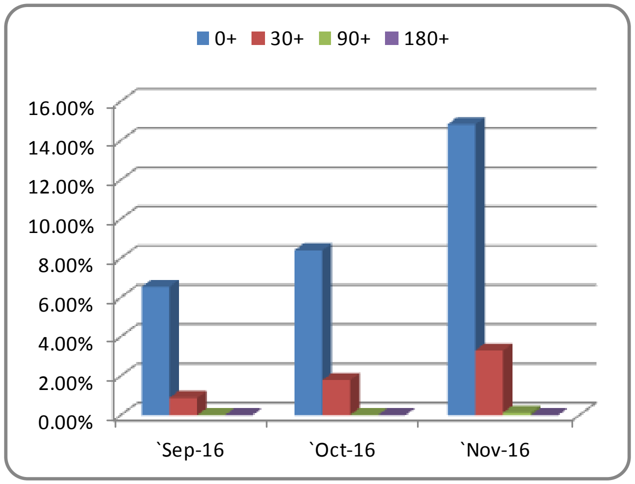


Exhibit 18: Bucket-wise delinquencies



Source: ICRA Research

Moderate decline in collection efficiencies; build-up in delinquency seen

The analysis presented above is based on performance of only three pools belonging to one originator and therefore may not be entirely reflective of industry trends. This particular financier has a high reliance on cash collections in its portfolio. Also, a pre-dominant portion of its portfolio comprises of self-employed borrowers. Also, it may be noted that all the pools have been rated recently and have amortised by less that 20%. Therefore, the delinquencies are still in the build-up stage.

The monthly collection efficiency for Car pools declined from 89.2% in October 2016 to 84.3% in November 2016. During the same period, the 0+ dpd level increased from 8.4% to 14.8%. The monthly prepayment rate remained largely unchanged in November 2016.

7. Tractors

Asset class	Tractors
Ticket size	Rs. 1 lakh – Rs. 40 lakhs
Security	Charge over the underlying vehicle financed
Borrower profile	Farmers, individuals largely in rural/ semi-urban areas
Repayment mode	Large reliance on cash; PDC/ ECS to a small extent
Nov-16 analysis based on	11 pools across 3 Originators (out of 15 live pools)

Exhibit 19: Monthly collection efficiency and prepayment rates

	Cumulative till Sep-16	Month of Sep-16	Month of Oct-16	Month of Nov-16
Collection Efficiency	*93.8%*	103.6%	95.3%	83.8%
Prepayment Rates	*0.2%*	0.5%	0.6%	0.7%

Source: ICRA Research

Exhibit 20: Bucket–wise monthly collection efficiency

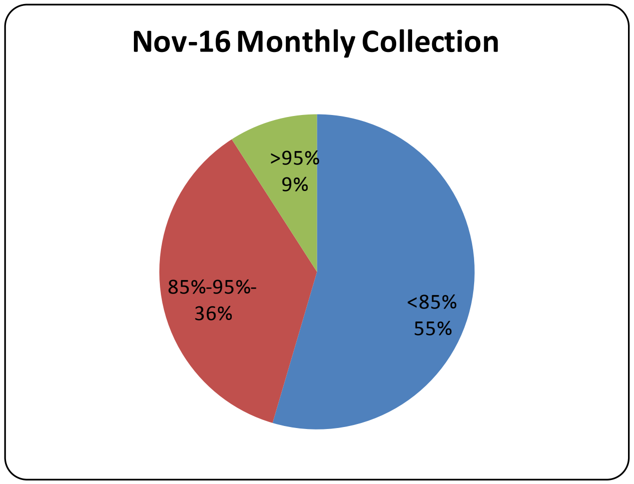
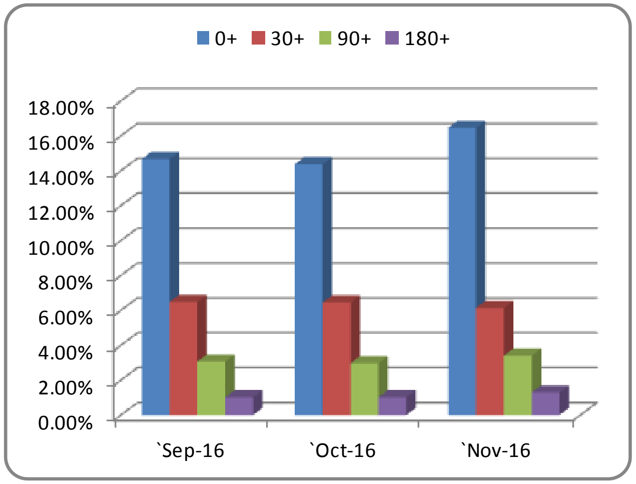


Exhibit 21: Bucket-wise delinquencies



Source: ICRA Research

Sharp decline in collection efficiencies seen; moderate delinquency build-up seen

The median monthly collection efficiency for Tractor pools declined sharply to 83.8% in November 2016 compared with 95.3% in the previous month. In case of tractor loans, the underlying borrowers are typically farmers engaged in agricultural activities. These borrowers either do not have a bank account or have poor banking habits. As a result, many borrowers were not able to pay due to unavailability of new currency resulting in decline in collection efficiency.

November-December period is the harvest season for the Kharif crop. The tractor loan instalments are often structured by some lenders to align with the income stream of the borrowers (with large chunky instalments falling due in the months of November and December). The benefits in this segment that were likely to accrue on account of good monsoon this year (after two years of successive deficient rainfall) were negated to a large extent on account of demonetisation. Due to currency shortage, farmers either faced a loss of income due to reduced off-take (for perishable food items like fruits and vegetables) or delayed realisations (many farmers were forced to deposit their produce with the mandis on credit). Thus, the revival in the rural economy should determine the performance of these pools over the next 2-3 months.

In November 2016, collection efficiency in six of the 11 pools dipped to less than 85%, as compared to 4 out of the 11 pools in the previous months. 0+ dpd level has seen a spike from 14.4% in October 2016 to 16.5% in November 2016.

The monthly prepayment rates have not been affected in month of November.

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