May 28, 2021 Revised

PNB Housing Finance Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible debentures	1,475.00	1,475.00	[ICRA]AA (Negative); Reaffirmed
Tier II bonds programme	200.00	200.00	[ICRA]AA (Negative); Reaffirmed
Total	**1,675.00**	**1,675.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation factors in PNB Housing Finance Limited's (PNBHFL) established track record in the mortgage finance industry, its experienced management team, and diverse funding profile. ICRA also notes that PNBHFL continues to reduce its wholesale exposure, which declined by ~34% in last two years and its proportion in its assets under management (AUM) declined to ~16% as on March 31, 2021 from ~18% as on March 31, 2020. This was supported by sell-down and accelerated prepayments of around Rs. 1,880 crore in the corporate book in FY2021. Further, ICRA expects that the company will continue to benefit from the shared brand name with its promoter, i.e. Punjab National Bank (PNB; rated [ICRA]AA (Stable)), which helps PNBHFL leverage its franchise and raise funds, thereby supporting its financial flexibility.

On the other hand, the rating factors in the significant increase in PNBHFL's gross non-performing assets (GNPAs) to 4.4% as on March 31, 2021 from 2.8% as on March 31, 2020, given the Covid-19 induced disruptions. The deterioration in the asset quality was witnessed in the retail as well as the corporate book. In addition, the company restructured certain accounts (2.28% of its AUM) under the one-time Covid-19 restructuring package announced by the Reserve Bank of India (RBI). ICRA notes that PNBHFL did manage to see some recoveries without any losses in its corporate book in FY2021. ICRA also notes that the company was not able to initiate legal proceedings due to asset classification standstill as per the honourable Supreme Court's order, which also caused low recoveries. With the lifting of the asset classification standstill, PNBHFL has started such proceedings and expects to witness an increase in recoveries. Nevertheless, the impact of the recent surge in Covid-19 infections and the resultant regional lockdowns/restrictions on operations and borrowers' cash flows remains to be seen. The risks are partly mitigated by the good collateral cover maintained by the company for such exposures and the healthy increase in its provision coverage ratio (PCR) in FY2021. Its overall provision to total assets increased to 4.1% as on March 31, 2021 from 2.6% as on March 31, 2020. Though this provides comfort and the cushion to absorb further losses, it has adversely impacted the profitability, which remains moderate despite improving from FY2020.

ICRA notes that with the decline in its scale of operations, PNBHFL's gearing declined to 6.7 times as on March 31, 2021 from 8.6 times as on March 31, 2020 (9.8 times as on March 31, 2019[1]), though it remains moderate. PNBHFL had been in the process of raising equity to reduce its leverage, however, there has been a significant delay in the same, given the challenging environment. In February 2021, PNBHFL stated that PNB would not be participating in the equity raise round. Nevertheless, PNBHFL is committed to raise further equity and expects the process to get completed in FY2022, which would further reduce its leverage and support its growth plans.

[1] *all ratios as per ICRA's calculations*

The operating environment for non-banking financial companies (NBFCs) and housing finance companies (HFCs) with sizeable real estate exposure and self-employed borrowers in the housing loans (HL) and loan against property (LAP) segments continues to be challenging.

The Negative outlook reflects ICRA's expectations that managing the asset quality metrics will remain challenging in the current environment wherein HFCs with sizeable real estate exposures and self-employed borrower segments have witnessed increased portfolio vulnerability. Thus, the company's ability to prevent further slippages and/or manage recoveries from delinquent accounts will be critical from a credit perspective.

Key rating drivers and their description

Credit strengths

Established player in mortgage lending market – PNBHFL has an established presence and a long track record of operations in the housing finance industry. It has a presence in 18 states/Union Territories (UTs) in India and it witnessed healthy growth in its scale of operations till September 2019. Post that, it increased its focus on the retail segment and started reducing its wholesale exposure. This led to degrowth of 10.65% in the AUM to Rs. 74,469 crore as on March 31, 2021 from Rs. 83,346 crore as on March 31, 2020. On its on-book portfolio, PNBHFL has registered degrowth of ~8% to Rs. 62,254 crore as on March 31, 2021 from Rs. 67,571 crore as on March 31, 2020. As on March 31, 2021, 56% of its on-book portfolio was towards individual housing loans, ~19% towards retail LAP, ~5% towards retail non-residential premises loans (NRPLs), ~1% towards retail lease rental discounting (LRD), ~14% towards construction finance, ~4% towards corporate term loans (CTLs) and ~1% towards corporate LRD. It also reported an off-book portfolio of Rs. 12,215 crore as on March 31, 2021 as against Rs. 15,775 crore as on March 31, 2020.

Experienced management and good systems – PNBHFL has a seasoned management team with sound knowledge of the mortgage industry and its board has prior experience in banking, insurance, retail lending, technology and economic policy. With support from the risk management and internal systems, PNBHFL's experienced management team has a track record of profitably scaling up businesses and has adequate experience in the retail and corporate lending segments of the housing finance industry.

Shared brand name and benefits with PNB as the promoter – With PNB being its promoter and holding a stake of 32.6% as on March 31, 2021, PNBHFL has a competitive advantage. The common brand name supports its financial flexibility and deposit mobilisation. Further, PNB's commitment to stay invested in the company and to provide liquidity support to meet PNBHFL's growth plans provides added comfort. PNBHFL's board comprises two directors from PNB.

Diversified funding mix – PNBHFL has managed to maintain a healthy funding mix comprising debt market instruments (non-convertible debentures (NCDs) and commercial paper (CP) formed 16.5% and 1.6%, respectively, of the funding mix as on March 31, 2021), deposits (23.7%), bank borrowings (22.2%), National Housing Bank (NHB; 10.9%), external commercial borrowings (ECBs; 8.3%) and direct assignments (16.9%). The cost of borrowings declined to 7.97% in FY2021 from 8.27% in FY2020 owing to low-rate incremental funding and the replacement of high-cost borrowings by low-cost borrowings in FY2021.

Credit challenges

Deterioration in asset quality metrics due to pandemic; impact of recent surge in Covid-19 infections remains monitorable – PNBHFL's overall asset quality has deteriorated with gross and net NPAs of 4.4% and 2.4%, respectively, as on March 31, 2021 (2.8% and 1.8%, respectively, as on March 31, 2020). In Q4 FY2021, PNBHFL reported further slippages of around Rs. 425 crore in the Stage 3 book and around Rs. 873 crore in Stage 2 accounts under significant-increase-in-credit-risk (SICR) classification. On the other hand, the management was able to resolve around Rs. 204 crore worth of accounts with NIL haircut and NIL credit loss. However, a large portion of the stressed exposure still stands unresolved as the resolution programmes were hampered by operational halts due to the Covid-19 pandemic. The management expects the resolution of these accounts to happen soon.

PNBHFL reported GNPAs of 12.70% with a Stage-3 PCR of 59.7% under the corporate book as on March 31, 2021 against 8.18% and 42.21%, respectively, as on March 31, 2020. The total provision to total asset for the corporate book stands at ~14% as on March 31, 2021. Given the typical maturity profile of the loans in the real estate sector and the significant prepayments/exits through refinance, the share of the loan book under moratorium remains high. While PNBHFL has been able to contain its asset quality in the past, the recent deterioration of the book due to the pandemic and stressed corporate exposures have increased the risk. The management's ability to manage the same remains critical from a credit perspective.

An increase in NPAs was witnessed in the retail book as well because of the pandemic. PNBHFL reported GNPAs of 2.5% with a Stage-3 PCR of 28.2% as on March 31, 2021 against 1.3% and ~25.4%, respectively, as on March 31, 2020. PNBHFL's ability to maintain its asset quality indicators in the current scenario will remain a monitorable. The risks are, however, mitigated to some extent by the collateral cover maintained by the company on such exposures. In addition, PNBHFL's various collection measures helped it achieve retail book collection efficiency ((current collections + overdue recoveries)/current demand) at 98.2% for the quarter ended March 2021.

Elevated credit costs keep profitability moderate – Given the increased stress in the asset quality, PNBHFL increased its provisioning requirement. It made sizeable provisions in Q4 FY2020 and FY2021, which impacted its profitability adversely, despite maintaining the lending spreads. It reported a profit after tax (PAT) of Rs. 930 crore, translating into a return on average managed assets of 1.02% and a return on average net worth of 10.99% in FY2021 (Rs. 646 crore, 0.68% and 8.32%, respectively, in FY2020)[2]. Going forward, the company's ability to manage the interest spreads and credit costs will be critical for maintaining the profitability indicators.

Moderate gearing level – PNBHFL reported an improvement in its leverage profile with a gearing of 6.7 times as on March 31, 2021 (8.6 times as on March 31, 2020). However, the same remains relatively high, given the macro environment and the high asset quality stress faced by the industry including PNBHFL. Supported by the decline in its scale of operations, internal accrual generation and the relatively lower risk weights prescribed by NHB for smaller ticket loans, which formed a part of its portfolio, the company improved its capital adequacy ratio (CRAR) to 18.73%[3] as on March 31, 2021 with a Tier I of 15.5% (CRAR stood at 17.98% with Tier I of 15.18% as on March 31, 2020[4]) against the regulatory requirement of CRAR of 15%.

Liquidity position: Strong

While the company remains exposed to asset-liability related risks given the longer tenor of the assets, its liquidity is supported by a good share of long-term and short-term borrowings and its plans to keep adequate liquid investments and unutilised lines to meet the gaps. It had cash and cash equivalents of Rs. 6,906 crore as on March 31, 2021 (as per provisional ALM, excluding investments) and collections due (as per behavioural analysis of ALM) of Rs. 5,654 crore (excluding NPAs, including restructured book) against debt repayments (including short-term overdraft (OD) facility) of Rs. 13,332 crore till September 30, 2021.

Rating sensitivities

Positive factors – Given the Negative outlook, a rating upgrade is not likely in the near term. However, the outlook may be revised to Stable if the company witnesses an improvement in the asset quality in the corporate as well as retail book with an improvement in its profitability profile.

Negative factors – Pressure on the rating would arise if the company continues to face further deterioration in its asset quality and/or does not see a meaningful recovery from its stressed assets. Pressure on its profitability, increase in its gearing and challenges in fund raising, restricting PNBHFL's ability to lend or leading to a deterioration in its liquidity profile, could also exert pressure on the rating.

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[2] *all ratios as per ICRA's calculations*

[3] *CRAR has been adjusted for deposits made by PNBHFL with PNB; CRAR would have been 20.61% as on March 31, 2021 without factoring in these deposits with PNB*

[4] *CRAR of March 2020 is basis I GAAP accounting*

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Rating Methodology for Housing Finance Companies
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the consolidated financial profile of the company

About the company

Incorporated in 1988, PNBHFL is a deposit-accepting housing finance company. PNB and The Carlyle Group had a stake of 32.6% and 32.2%, respectively, as on March 31, 2021. The company offers home loans, LAP, builder loans and LRD. The on-book portfolio mix, as on March 31, 2021, included individual housing loans (~56% of on-book portfolio), retail LAP (~19%), retail NRPL (~5%), retail LRD (~1%) and wholesale loans including LRD (~19%) aggregating Rs. 62,254 crore. PNBHFL is geographically diversified with a portfolio spread across 18 states/Union Territories (UTs).

In FY2021, PNBHFL reported PAT of Rs. 930 crore on AUM of Rs. 74,469 crore as on March 31, 2021 vis-à-vis PAT of Rs. 646.2 crore in FY2020 (PAT of Rs. 1,191.5 crore in FY2019) on AUM of Rs. 83,346 crore as on March 31, 2020 (AUM of Rs. 84,722 crore as on March 31, 2019). The company reported a CRAR of 18.73% (Tier I capital of 15.50%) and a gearing of 6.7 times as on March 31, 2021 as compared to CRAR of 17.98% (Tier 1 capital of 15.18%) and gearing of 8.6 times as on March 31, 2020. It reported GNPAs and NNPAs of 4.4% and 2.4%, respectively, as on March 31, 2021 vis-à-vis 2.8% and 1.8%, respectively, as on March 31, 2020.

Key financial indicators (Ind AS; audited)

PNBHFL	FY2019	FY2020	FY2021*
Total income (Rs. crore)	7,683	8,490	7,624
Profit after tax (Rs. crore)	1,192	646	930
Net worth (Rs. crore)	7,544	7,998	8,923
Loan book (Rs. crore)	74,916	68,645	63,370
Total assets (Rs. crore)	84,328	80,695	73,936
Return on average managed assets (%)	1.5%	0.7%	1.0%
Return on average net worth (%)	16.9%	8.3%	11.0%
Gross gearing (times)	9.8	8.6	6.7
Gross stage 3 (%)	0.5%	2.8%	4.4%
Net stage 3 (%)	0.4%	1.8%	2.4%
Solvency (Net stage 3/Net worth)	3.7%	14.8%	17.0%
CRAR (%)	13.98%	17.98%	18.73%~

Source: *Company, ICRA Research; All ratios as per ICRA calculations*

** FY2021 numbers and ratios might change subject to notes to accounts*

~ Adjusted for deposits made with companies in same Group (parent), CRAR would have been 20.61% as on March 31, 2021

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	May-28-2021	FY2021	FY2020	FY2019
						Apr-03-2020	May-31-2019	Apr-06-2018
1	NCD programme	Long term	1,475	300	**[ICRA]AA (Negative)**	**[ICRA]AA (Negative)**	**[ICRA]AA+ (Negative)**	**[ICRA]AA+ (Stable)**
2	Tier II bonds programme	Long term	200	200	**[ICRA]AA (Negative)**	**[ICRA]AA (Negative)**	**[ICRA]AA+ (Negative)**	**[ICRA]AA+ (Stable)**

Complexity level of the rated instruments

Instrument	Complexity Indicator
NCD Instruments	Very Simple
Tier II Bonds	Very 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: www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE572E09239	NCD	Jan-31-2014	9.48%	Jan-31-2024	300.00	[ICRA]AA (Negative)
NA	NCD: Unutilised	NA	NA	NA	1,175.00	[ICRA]AA (Negative)
INE572E09262	Tier II Bonds	Nov-24-2014	8.70%	Nov-24-2024	200.00	[ICRA]AA (Negative)

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
PHFL Home Loans and Services Ltd.	100.00%	Full Consolidation

Corrigendum

Rationale dated May 28, 2021 has been corrected with revisions as detailed below:

Relationship contact details corrected from Jayanta Chatterjee to L Shivakumar on Page 8 of this document.

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