September 12, 2024

Kinara Capital Private Limited: Ratings reaffirmed; outlook revised to Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
NCD programme	74.37	74.37	[ICRA]BBB (Stable); Reaffirmed and outlook revised to Stable from Positive
CP programme	60.00	60.00	[ICRA]A3+; Reaffirmed
Long-term fund based – Term loan	114.60	114.60	[ICRA]BBB (Stable); Reaffirmed and outlook revised to Stable from Positive
Short-term fund based – Term loan	25.00	25.00	[ICRA]A3+; Reaffirmed
Total	**273.97**	**273.97**	

**Instrument details are provided in Annexure I*

Rationale

The revision in the outlook to Stable factors in the weaker-than-expected asset quality and the consequent pressure on Kinara Capital Private Limited's (Kinara) earnings profile in FY2024 and Q1 FY2025. The capital profile is adequate at present. However, considering the near-term impact on earnings coupled with the envisaged growth in the assets under management (AUM), it would be critical to raise commensurate capital to maintain sufficient buffers. ICRA notes that the company's capital requirement is sizeable in relation to its current net worth. Kinara would need to raise capital in the next 12-18 months, considering the subdued internal capital generation expected in the near term.

Kinara has been observing higher stress in certain regions and segmental exposures in its AUM in recent quarters, with the 90+ days past due (dpd)[1] increasing to 6.9% as of June 30, 2024 (4.6% as of March 31, 2024) from 3.3% as of March 31, 2023 and the 0+dpd increasing to 15.0% as of June 30, 2024 (10.7% as of March 31, 2024) from 6.3% as of March 31, 2023. The company had also undertaken accelerated write-offs in Q1 FY2025, resulting in elevated credit costs. Consequently, it reported a loss of -0.6% (as percentage of average managed assets) in Q1 FY2025 vis-à-vis the net profit of 1.6% in FY2024 (net profit of 1.6% in FY2023). The company is cautious regarding disbursements in the impacted segments/regions and is focusing on bringing the asset quality under control over the next 1-2 quarters. In line with this, Kinara is strengthening its credit and portfolio monitoring framework and collections infrastructure further. Its ability to sustainably improve the performance of its portfolio quality would be a monitorable. ICRA, however, notes that close to 31% of the AUM in June 2024 is protected by a credit guarantee cover, up from 15% in June 2023.

The ratings also take into consideration Kinara's track record of operations in the micro, small, and medium enterprises (MSME)/small business lending segment. The ratings continue to take cognisance of the company's geographically concentrated operations with the top 3 states accounting for 71% of the portfolio as of June 30, 2024 (71% as of March 31, 2024).

[1] *Dpd numbers are reported net of CGTMSE claims received*

Key rating drivers and their description

Credit strengths

Track record of operations in MSME segment – Kinara has an established track record of around 12 years in the MSME segment, having commenced operations in FY2011. It provides loans to small businesses for asset purchase and working capital requirements. As of June 2024, Kinara had a presence in 6 states with 133 branches.

Kinara's AUM increased by 28% year-on-year (YoY) to Rs. 3,173 crore in FY2024, though it declined slightly in Q1 FY2025 to Rs. 3,189 crore as of June 2024, given the slowdown in disbursements. The off-balance sheet portfolio (includes co-lending and assigned exposures) accounted for 37% of the overall AUM. ICRA notes that Kinara envisages to reach an AUM of ~Rs. 4,000 crore by March 2025. The AUM is largely concentrated in the southern states with the top 3 states – Tamil Nadu, Karnataka, Andhra Pradesh – accounting for around 71% of the portfolio as of June 30, 2024 (71% as of March 31, 2024).

Kinara has an experienced management team[2], which has enabled it to continuously improve its lending and monitoring systems that are crucial for its AUM growth, given the borrower profile. The company, however, faces attrition at the field level, which has impacted collections and incremental disbursements in recent quarters. In view of the asset quality concerns, Kinara is tightening its underwriting criteria and is adding more guardrails on exposures to vulnerable sectors and geographies.

Adequate capital profile for the near term – Kinara, with a reported gearing of 2.9 times and a managed gearing of 4.5 times (adjusted gearing[3] of 3.4 times) as of March 2024, is adequately capitalised for its current scale of operations. In FY2023, the company had raised substantial equity of Rs. 405.8 crore in two tranches (Rs. 208.1 crore in April 2022 and Rs. 197.7 crore in September 2022), strengthening its capital profile. Accordingly, its net worth stood at Rs. 729.5 crore as of June 2024 (Rs. 736.4 crore as of March 2024) vis-à-vis Rs. 245.3 crore as of March 2022. The capital-to-risk weighted assets ratio (CRAR) was adequate at 27.0% as of June 2024 (27.6% as of March 2024). The company would be required to raise considerable capital over the next 12-18 months, in relation to its current net worth, to maintain adequate capital buffer considering its growth plans.

Credit challenges

Asset quality under pressure – Kinara's gross stage 3 (GS3) assets increased to 6.6% as of June 30, 2024 (5.6% as of March 31, 2024) from 5.6% as of March 31, 2023. Softer bucket delinquencies also increased with the 0+dpd standing at 15.0% as of June 30, 2024 (10.7% as of March 31, 2023) vis-à-vis 6.3% as of March 31, 2023. ICRA notes that the company has been observing asset quality stress over the last few quarters in its exposures to certain segments/regions as well as in its higher ticket size portfolio. Impact on collections because of employee attrition is also being witnessed. As a result, Kinara had to undertake higher write-offs in FY2024 and Q1 FY2025. Overall, the write-offs increased to Rs. 123.3 crore in FY2024 {3.9% of the AUM and 6.1% of gross carrying asset (GCA)} from Rs. 74.2 crore in FY2023 (3.0% of the AUM and 4.5% of GCA); Kinara also wrote off around Rs. 46 crore in Q1 FY2025.

Kinara's customers are usually traders (62% in June 2024) and small manufacturers (34%), a largely underserved and unserved segment, which is susceptible to economic shocks. The company usually provides loans for asset purchase and working capital requirements, with tenures of 6 months to 72 months and ticket sizes in the range of Rs. 50,000 to Rs. 40 lakh. The share of borrowers who are new to credit is currently around 6%. Further, Kinara largely operates in the unsecured lending segment, with the share of unsecured loans at around 81% as of June 2024 (87% as of March 2023). ICRA notes the inherent risk in the

[2] The Chief Operating Officer (COO), Mr. Thirunavukkarasu, recently resigned from the company; at present, Kinara has appointed separate heads for sales and collections, who will report to the Chief Executive Officer

[3] Adjusted gearing = (On-book borrowing)/(Net worth – First loss given default extended for co-lending exposure)

portfolio given the unsecured nature of the loans, the moderate credit profile of the borrowers and the modest seasoning of the loans due to strong AUM growth.

ICRA notes that about 31% of Kinara's portfolio, as of June 30, 2024, was covered under various guarantee schemes of Credit Guarantee Fund for Micro Units (CGFMU), Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE), Emergency Credit Line Guarantee Scheme (ECLGS), etc. Adjusting for the portfolio covered under these schemes, the net non-performing advances (NPAs on AUM basis) stood at 3.9% as of June 2024 (2.9% as of March 2024 and 2.2% as of March 2023). The company had recovered Rs. 38.6 crore during FY2021-FY2024 from the guarantee schemes.

In view of the asset quality concerns and to expand its coverage under the CGFMU scheme, the company had reduced the average ticket size of the loans to Rs. 8 lakh (including partnerships) from Rs. 11 lakh as of March 2023. Further, it has taken steps to improve its collection processes by introducing new collection interventions, outsourcing harder bucket delinquencies to collection agencies, etc.

Subdued profitability – Kinara reported a modest loss in Q1 FY2025 vis-à-vis a profit of 1.6% (percentage of AMA) in FY2024 as well as FY2023, predominantly due to higher credit costs. The credit cost increased to 4.9% in Q1 FY2025 (4.8% in FY2024) from 3.5% in FY2023, owing to the elevated write-off of Rs. 123.3 crore in FY2024 (Rs. 46 crore in Q1 FY2025), given the stress observed in its portfolio. Kinara's operating cost remained elevated at 4.7% in FY2024, though it was lower than 6.2% in FY2023. Operating costs could witness some increase in the near term as incremental changes are being implemented for the sales and collections teams in response to the asset quality stress.

Kinara has been increasing the share of higher interest rate loans over the last two years. Loans with an interest rate of more than 30% accounted for 24.3% of the portfolio as of March 2024 compared to 17.8% as of March 2023 (2.7% as of March 2020), supporting its yields and interest margins. Further, the company has booked sizable gains from its co-lending portfolio, which has also supported the interest margins.

The steps taken by the company to enhance its portfolio quality and manage the operating efficiency, while focusing on smaller-ticket loans, would be key for improving its earnings profile. Further, Kinara's ability to improve its liability profile, through further diversification of its lenders, and obtain funds at competitive rates would remain crucial from an earnings perspective.

Liquidity position: Adequate

Kinara had unencumbered cash and liquid investments of ~Rs. 672.6 crore as of June 30, 2024. The company is also expected to have collections of Rs. 1,143.2 crore between July 2024 and December 2024. As such, its liquidity position is projected to be adequate for meeting the scheduled debt repayments (including interest) of Rs. 848 crore during July-December 2024.

Kinara's lender profile, as on June 30, 2024, comprised debentures from foreign portfolio investors (FPIs; 29% of the total borrowings), followed by external commercial borrowings (ECBs), non-banking financial companies (NBFCs)/financial institutions, term loans from banks, and alternative investment funds (AIFs) at 28%, 25%, 16% and 2%, respectively. ICRA notes that the company was in breach of some financial covenants with its lenders and has received temporary relaxation from a few lenders for the same.

Rating sensitivities

Positive factors – A sustained improvement in the profitability indicators and funding profile while scaling up the AUM would be a positive factor.

Negative factors – Pressure on the company's ratings could arise if there is further deterioration in its asset quality or earnings profile. Sustained weakening of the capitalisation metrics (managed gearing exceeding 5 times on a continued basis) would also exert pressure on the ratings.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Rating Methodology for Non-banking Finance Companies]
Parent/Group support	Not applicable
Consolidation/Standalone	The ratings are based on the standalone financial statements of the company

About the company

Kinara Capital Private Limited is a non-deposit taking NBFC, incorporated in 1996. The current promoters acquired the company in September 2011 and commenced lending operations in November 2011. It provides secured (hypothecation of machinery) and unsecured term loans as well as working capital facilities. Currently, the company operates in six states, namely Karnataka, Maharashtra, Gujarat, Tamil Nadu, Andhra Pradesh and Telangana, with its head office in Bengaluru. As on March 31, 2024, Kinara had 133 branches with an AUM of Rs. 3,173.24 crore (AUM of Rs. 3,189.3 crore as of June 30, 2024).

Key financial indicators (audited)

Kinara Capital Private Limited	FY2023	FY2024	Q1 FY2025
Total income	491.6	722.6	174.3
Profit after tax	41.2	62.2	(6.8)
Total managed assets	3,435.0	4,305.9	4,443.5
Return on managed assets	1.6%	1.6%	-0.6%
Adjusted gearing (times)	2.8	3.4	3.7
Managed gearing (times)	3.7	4.5	4.8
Gross stage 3	5.6%	5.6%	6.6%
CRAR	32.0%	27.6%	27.0%

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Current (FY2025)			Chronology of rating history for the past 3 years					
				FY2024		FY2023		FY2022	
Instrument	**Type**	**Amount Rated (Rs Crore)**	**12-Sep-2024**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**
Short term-term loan-fund based	Short Term	25.00	[ICRA]A3+	15-SEP-2023	[ICRA]A3+	22-JUL-2022	[ICRA]A3+	09-NOV-2021	[ICRA]A3
				-	-	28-SEP-2022	[ICRA]A3+	-	-
Long term-term loan-fund based	Long Term	114.60	[ICRA]BBB (Stable)	15-SEP-2023	[ICRA]BBB (Positive)	22-JUL-2022	[ICRA]BBB (Stable)	19-APR-2021	[ICRA]BBB- (Negative)
				-	-	28-SEP-2022	[ICRA]BBB (Stable)	06-JUL-2021	[ICRA]BBB- (Negative)
				-	-	-	-	09-NOV-2021	[ICRA]BBB- (Negative)
CP programme	Short Term	60.00	[ICRA]A3+	15-SEP-2023	[ICRA]A3+	22-JUL-2022	[ICRA]A3+	19-APR-2021	[ICRA]A3
				-	-	28-SEP-2022	[ICRA]A3+	06-JUL-2021	[ICRA]A3
				-	-	-	-	09-NOV-2021	[ICRA]A3
NCD programme	Long Term	74.37	[ICRA]BBB (Stable)	15-SEP-2023	[ICRA]BBB (Positive)	22-JUL-2022	[ICRA]BBB (Stable)	19-APR-2021	[ICRA]BBB- (Negative)
				-	-	28-SEP-2022	[ICRA]BBB (Stable)	06-JUL-2021	[ICRA]BBB- (Negative)
				-	-	-	-	09-NOV-2021	[ICRA]BBB- (Negative)

Complexity level of the rated instruments

Instrument	Complexity Indicator
NCD programme	Simple
CP programme	Very Simple
Long-term fund based – Term loan	Simple
Short-term fund based – Term loan	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

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE200W07290	**NCD programme**	Sep 07, 2022	11.75%	Mar 07, 2028	69.52	[ICRA]BBB (Stable)
Unallocated	**NCD programme**	NA	NA	NA	4.85	[ICRA]BBB (Stable)
Unallocated	**CP programme**	NA	NA	NA	60.00	[ICRA]A3+
-	**Long-term fund based – Term loan**	Jul 29, 2022 to Jun 30, 2023	NA	Feb 15, 2025 to Aug 31, 2025	43.89	[ICRA]BBB (Stable)
Unallocated	**Long-term fund based – Term loan**	NA	NA	NA	70.71	[ICRA]BBB (Stable)
Unallocated	**Short-term fund based – Term loan**	NA	NA	NA	25.00	[ICRA]A3+

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

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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