Small Business Fincredit India Private Limited

December 19, 2017

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term Bank Lines Programme	0.00	200.00	[ICRA]A (stable); Assigned
Non Convertible Debenture programme	400.00	400.00	[ICRA]A (stable); Outstanding
Total	**400.00**	**600.00**	

Rating action

ICRA has assigned a long term rating of [ICRA]A (pronounced ICRA A) to the Rs. 200 crore long term bank lines programme of Small Business Fincredit India Private Limited (SBFC). ICRA also has a long term rating of [ICRA]A outstanding for the Rs. 400 crore non convertible debenture programme of SBFC. The outlook on the long term rating is stable.

Rationale

The rating derives significant strength from the transaction structure (completed in September 2017) whereby SBFC acquired the retail lending book along with the existing infrastructure, branch network and employee team from Karvy Financial Services Limited (KFSL). Retail lending portfolio consists of Small ticket micro enterprise (ME) loans, medium ticket small and medium enterprise (SME) loans, loan against gold (LAG) and small commercial vehicle (SCV) loans. The rating also factors in the moderate seasoning and stable asset quality of the ME and SME loans which has been acquired as part of the deal. The rating takes comfort from the significant upfront equity infusion of Rs. 845 crore by Lyra Partners and Arpwood Partners Investment Advisors LLP into the company. This equity infusion and the Rs. 400 crore non-convertible debentures have helped the acquisition of the Rs. 807 crore of loan assets from KFSL. The rating also takes into account the senior management team who has significant experience in retail lending business in India. The rating is however constrained by the transition related challenges and the possible employee attrition in the near term. The company's ability to manage asset quality as the portfolio seasons would be a key rating sensitivity in the near to medium term. Going forward, the company's ability to improve its profitability by borrowing at competitive rates from banks and by containing operating expenses would also be a key rating monitorable.

Outlook: Stable

ICRA believes that Small Business Fincredit India Private Limited will continue to benefit from the upfront equity infusion along with the experienced senior management team and the acquired infrastructure (from KFSL). The outlook may be revised to 'Positive' if there is a healthy ramp up in the loan book along with healthy interest spreads, leading to an improvement in its financial risk profile. The outlook may be revised to 'Negative' if there is deterioration in the asset quality of the loan book, impacting the profitability of the company.

Key rating drivers

Credit strengths

Moderately seasoned loan book with a track record of seven years; majority of the portfolio have never been more than 30 days delinquent – SBFC has completed the acquisition of the retail assets in September 2017. The acquired loan book predominantly comprises of ME and SME loans (~76%) and LAG (~21%). The ME and SME loan book is moderately seasoned as these loans have been disbursed over the past seven years by KFSL. The portfolio acquired as part of transaction is moderately seasoned with delinquencies in the 30+dpd bucket being low (<1%) in the key segments like ME and SME. The gold loan book has been acquired on account of the extensive branch network (6 regional offices and 80 branches) of KFSL which comes along with it. ICRA notes that the market risk associated with gold prices is mitigated by the adequate loan to value (LTV) cover and the company's ability to auction the assets in case the LTV reaches a threshold level. SBFC also has a credit enhancement from KFSL for any future non-performing assets (NPAs) up to Rs. 50 crore for a period of 12 months.

Granular book with retail focus and low average ticket size – The existing ME and SME loan books have average ticket sizes of ~Rs. 12 lakh and ~Rs. 40 lakh respectively, which imparts granularity to the portfolio. For incremental disbursements, the company plans to focus on low ticket sizes micro enterprise loans upto Rs. 50 lakh. The average ticket size for the company is expected to be ~Rs. 25 lakh. With the managements focus on establishing adequate systems and processes initially, the disbursements have been restricted to only the LAG segment.

Comfortable Capitalisation profile after equity infusion by new shareholders – Lyra Partners and Arpwood Partners Investment Advisors LLP infused Rs. 845 crore upfront into the company which along with the non-convertible debenture borrowings have helped the company in acquiring retail assets of ~Rs. 807 crore from KFSL. SBFC's gearing is ~0.69 time at the closing of the deal with an adjusted net worth of Rs. 584 crore (adjusted for goodwill of Rs. 261 crore). Supported by the upfront capital infusion, the company's capital structure is expected to be comfortable and enable it to meet its growth targets for the next three years.

Experienced senior management team – SBFC has brought on board Mr. Aseem Dhru (as Chief Executive Officer) and Mr. Mahesh Dayani (as Chief Business Officer) from leading private sector banks who have significant experience in retail lending. The company has also brought in other senior managers from leading banks and NBFCs who have experience in the credit business. The company would leverage their experience in ramping up the retail loan book, maintaining strong underwriting practices and in technology adoption.

Credit weaknesses

Ensure smooth transition of operations and contain employee attrition – With the transaction in the pipeline for over a year, and no incremental disbursements during the period, there has been an increase in employee attrition in the last year. The company's ability to start disbursements soon would be critical for retaining key resources.

Manage asset quality as portfolio seasons – SBFC's asset quality at the time of closing of the deal was healthy with the company largely acquiring only performing loan assets. The delinquencies in the ME and SME segment were low as on the acquisition date (30+ dpd was 0.73% in ME and 0.00% in SME). However, LAG has slightly higher delinquencies but the adequate security cover and the liquid nature of the collateral minimizes the credit risk to an extent. As the company ramps up its loan book and the existing loan book seasons, its ability to maintain asset quality would remain a key rating monitorable. The company's ability to ensure strong underwriting practices in segments like ME loans would be critical driver of overall asset quality.

Improve profitability by borrowing at attractive cost of funds and containing operating expenses – With the company expecting to ramp up its loan book going forward, its ability to borrow funds from banks at competitive rates would be important for improving its net interest margins. SBFC's ability to contain operating expenses while investing in the required technology and infrastructure would also be a key rating monitorable.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:
ICRA's Credit Rating Methodology for Non-Banking Finance Companies

About the company

Small Business Fincredit India Private Limited (SBFC) is a non-banking finance company, which has acquired the retail assets of Karvy Financial Services Limited (KFSL). As a part of the transaction, the entire infrastructure, branches and employee team of KFSL has been transferred to SBFC. At the time of the closing of the deal, the company had a net worth of ~Rs. 590 crore (net of goodwill) and a loan book of Rs. 807 crore. Going forward, SBFC plans to focus the low ticket size business loans (secured by property) and loans against gold.

Key Financial Indicators (Audited)

	As on September 28, 2017
Borrowings	402.00
Equity Share Capital	676.00
Net worth	844.97
Current Assets	180.00
Loan Book	807.29
Goodwill	261.00
Total assets	1,247.02
Gearing	0.48
Gearing (on adjusted net worth)	0.67

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2018)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)		FY2018	FY2017	FY2016	FY2015
					Dec-17	Sep-17	-	-	-
1	Bank Lines Programme	Long Term	200.00	50.00	[ICRA]A (stable)	-	-	-	-
2	Non Convertible Debenture programme	Long Term	400.00	400.00	[ICRA]A (stable)	[ICRA]A (stable)	-	-	-

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE423Y07013	Non Convertible Debenture	28-Sep-17	9.40%	28-Sep-20	400.00	[ICRA]A (stable)
NA	Long term Bank Lines	Sep-17	NA	Sep-22	75.00	[ICRA]A (stable)
NA	Long term Bank Lines - Proposed	NA	NA	NA	125.00	[ICRA]A (stable)

Source: Small Business Fincredit India Private Limited

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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.

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