Suryoday Small Finance Bank Limited Revised

May 07, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Certificate of Deposit Programme	30.00	130.00	[ICRA]A1; assigned/outstanding
Fixed Deposit Programme	500.00	500.00	MA (Stable); outstanding
Long Term Bank Lines	105.12	105.12	[ICRA]A- (Stable); outstanding
Non-Convertible Debenture	176.50	176.50	[ICRA]A- (Stable); outstanding
Subordinate Debt Programme	50.00	50.00	[ICRA]A- (Stable); outstanding
Non-Convertible Debenture	37.00	-	[ICRA]A- (Stable); withdrawn
Total	**898.62**	**961.62**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has assigned a rating of [ICRA]A1 (pronounced ICRA A one) to the Rs. 130 crore[1] (enhanced from Rs. 30 crore) certificate of deposit programme of Suryoday Small Finance Bank Limited (SSFB) [2]. ICRA has also withdrawn the rating of [ICRA]A- (pronounced ICRA A minus) with Stable outlook assigned to the Rs. 37 crore non-convertible debenture programme of SSFB. The rating has been withdrawn at the request of the bank as there is no amount outstanding against the rated instrument. The ratings have been withdrawn in accordance with ICRA's policy on withdrawal and suspension.

ICRA has the rating outstanding of [ICRA]A- (pronounced ICRA A minus) for the Rs. 105.12 crore long term bank lines programme, Rs. 176.50 crore non-convertible debenture programme and Rs. 50 crore subordinated debt programme of SSFB. ICRA also has the rating outstanding of MA (pronounced M A) on the Rs. 500 crore fixed deposit programme of SSFB. The outlook on the long-term and medium-term ratings is stable.

Rationale

The rating factors in SSFB's experienced board and management team and strong investor support, its comfortable capitalisation and liquidity profile of the bank supported by regular capital infusion by the investors and promoters. ICRA takes comfort from the capital infusion from the promoters and investors (Rs. 289.87 crore received in FY2017 and Rs. 25.93 crore in FY2018) which has helped SSFB meet the increased operating expenses owing to conversion to a small finance bank and elevated credit costs due to deterioration in asset quality. ICRA notes the deterioration in asset quality indicators owing to significant proportion of portfolio in affected areas post demonetisation with the bank reporting Gross NPA of 6.03% as on March 31, 2018. However, SSFB has made provisions amounting to 0.66% (% of average managed assets) for the same and net NPA% was lower at 1.84% (on provisional results). Further, SSFB's strong capitalisation and good collection efficiency in disbursement made post demonetisation provide comfort in this regard. The rating also factors in the geographically diversified portfolio of the bank with presence in eight states and a union territory.

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website (www.icra.in) or other ICRA rating publications*

SSFB commenced banking operations in 2017 and has introduced new products like home loans, loan against property, loans to micro, small and medium enterprises and deposits. Further SSFB has been able to mobilise Rs. 749 crore of deposits as on March 31, 2018. The rating is however constrained by SSFB's low profitability indicators (ROE of 4.33% in FY2017 and 1.96% in FY2018) and elevated credit costs. The rating factors in the risks associated with unsecured lending, political and operational risks arising out of cash handling and high attrition rates in the industry. Given the marginal profile of its borrowers and the risk of their overleveraging, the credit quality of micro-loan portfolios is fundamentally characterised by a high level of volatility. ICRA takes note of the transition to electronic mode for incremental disbursements which is expected to reduce operational risks to some extent. Going forward, the SSFB's ability to diversify its retail deposit base and product mix and improving the profitability indicators would remain key rating monitorables.

Outlook: Stable

ICRA believes SSFB will continue to benefit from the experienced board and strong management, comfortable capitalisation and liquidity position. The outlook may be revised to 'Negative' if asset quality or capitalisation indicators deteriorate sharply, or there is a stretch in the liquidity position of the bank.

Key rating drivers

Credit strengths

Geographically diversified portfolio – SSFB has presence in eight states and one union territory covering major regions in the southern, western and eastern parts of the country. Initially focused on Maharashtra, SSFB has actively brought down the share of Maharashtra from 77% of the portfolio as on March 31, 2012 to 32% of the portfolio as on March 31, 2018 while focusing on new states and geographies. Over the past three years, SSFB has ventured into the states of Chhattisgarh, Puducherry and Madhya Pradesh which together accounted for ~6% of the portfolio as on March 31, 2018. As on March 31, 2018, SSFB was operating through 219 microfinance outlets and 23 banking branches serving 9.3 lakh customers. Also, with commencement of banking operations, SSFB has introduced new products like home loans, loan against property, loans to micro, small and medium enterprises and deposits. Consequently, the share of joint liability group loans has come down from 98% as on March 31, 2017 to 89% as on March 31, 2018 of assets under management (AUM).

Experienced board and management team and good systems have enabled the company to scale up operations profitably – SSFB has a seven-member board with good representation by independent directors. The bank has an experienced senior management team and the bank has developed strong second and third lines of management. SSFB has robust loan origination, monitoring and collection systems in place. Internal audits are conducted regularly, and the scope and coverage are in line with industry practices. The bank has a strong risk management team, which prepares the guidelines on credit risk, geographical concentration, cross sell products to be introduced, assessment of the various businesses and operating risks. The bank has also recruited key managerial personnel with experience in the banking sector, to further strengthen its team.

Comfortable capitalisation and gearing level; regular capital infusion – SSFB's capital adequacy remains comfortable with a Capital to Risk Weighted Assets Ratio (CRAR) of 36.37% (Tier I being 33.23%) as on March 31, 2018 as compared to regulatory requirement of 15% (Tier I being 7.5%). With regular equity infusion by promoters and investors (Rs. 289.87 crore in FY2017 and Rs. 25.93 crore in FY2018) the gearing level reduced to 2.72 times as on March 31, 2018 vis-a-vis 4.84 times as on March 31, 2016. ICRA's expects SSFB to maintain good capitalisation indicators going forward given the investor support and regular capital infusions.

Comfortable liquidity position and financial flexibility; strong ability to raise funding from diverse sources - SSFB's liquidity position remains comfortable owing to a conservative liquidity policy, high cash balances and continued funding from promoters and investors. Also, with commencement of banking operations, SSFB has started raising funds through deposits. However, it would take some time for SSFB to garner a sizeable retail depositor base. Nevertheless, lines from SIDBI, NABARD and other banks are likely to support its liquidity profile in the interim period.

Credit challenges

Ability to diversify product mix and garner retail deposits – With commencement of banking operations, SSFB has introduced new products like home loans, loan against property, micro, small and medium enterprise (MSME) loans and deposits. While the share of the new products on the asset side stood at 9% of the portfolio as on March 31, 2018, the company has been successful in raising deposits amounting to Rs. 749 crore against an AUM of Rs. 1,759 crore as on the date. However, majority of the deposits were of wholesale nature. Going forward, SSFB's ability to successfully diversify their product mix and garner retail deposits while growing its portfolio remains a key rating monitorable.

Deterioration in asset quality post demonetisation – Pursuant to the demonetisation action by the Government of India leading to inadequate currency supply, political interference in some states, and disruption in borrower cash flows which led to a decline in collection efficiencies and subsequent deterioration in asset quality with gross NPAs of 6.03% and net NPAs of 1.84% as on March 31, 2018. However, SSFB has made provisions amounting to 0.66% (% of average managed assets) for the same and net NPA% was lower at 1.84%. Further, SSFB's strong capitalisation and good collection efficiency in disbursement made post demonetisation provide comfort in this regard.

Profitability to be impacted by increasing operational costs, elevated credit costs and negative carry of regulatory reserve requirements – Since the bank is opening its SFB branches in stages, operating expenses are likely to remain elevated over the medium term which coupled with costs arising out of maintaining regulatory cash and liquidity reserves are likely to impact profitability indicators negatively. In ICRA's opinion, the bank's ability to maintain asset quality, offer diverse loan products and fee-based products while developing a strong deposit base would remain critical for its long-term profitability.

Marginal borrower profile with limited ability to absorb income shocks – The rating factors in the risks associated with marginal borrower profile, unsecured lending business, political risks, and operational risks arising out of cash handling, along with challenges associated with high pace of growth and high attrition rates.

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

Suryoday Small Finance Bank (SSFB) started as Suryoday Micro Finance Limited was set up in October 2008 as an NBFC with the concept of providing loans to women in urban and semi-urban areas under the Grameen Bank Joint Lending Model. During FY2016, SSFB received license from Reserve Bank of India to commence operations as a small finance bank. Subsequently, it commenced operations as a small finance bank on January 23, 2017.

As of March 2018, the SSFB had operations across eight states and one union territory catering to a client base of 9.3 lakh customers through 221 microfinance outlets and 23 banking branches. During FY2018 SSFB reported a net profit of Rs. 10.19 crore on a total income of Rs. 325.13 crore vis-a-vis a net profit of Rs. 15.06 crore on total income of Rs. 254.79 crore during FY2017. SSFB reported a return on managed assets (RoMA) of 0.50% FY2018 as compared to 1.01% during FY2017.

Key financial indicators (Audited)

	FY2017	FY2018*
Total Income	254.79	325.13
Operating Profit	37.10	68.01
PAT (reported)	15.10	10.19
Yield on Average Loans	25.80%	23.35%
Cost of Average Interest-Bearing Funds	11.52%	9.81%
Net Interest Margin (adj. for BO costs) / AMA	8.70%	8.87%
Operating Profit / AMA	2.49%	0.66%
PAT / AMA	1.01%	0.50%
PAT / Average Net worth	4.33%	1.96%
Net worth	500.57	539.82
Gearing	2.08	2.72
CRAR	53.62%	36.73%
Gross NPA	6.15%	6.03%
Net NPA	3.80%	1.84%

**Provisional*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

S I No	Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years									
						FY2018		FY2017				FY2016			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	May 2018	Mar-18	Feb-18	Oct-16	Sep-16	Aug-16	May-16	Oct-15	Jun-15	May-15	Apr-15
1	Certificate of Deposit Programme	Short Term	130.00	NA	[ICRA] A1	[ICRA]A1	-	-	-	-	-	-	-	-	-
2	Fixed Deposit Programme	Medium Term	500.00	NA	MA (Stable)	MA (Stable)	MA (Stable)	-	-	-	-	-	-	-	-
3	Long Term Bank Lines	Long Term	105.12	105.12	[ICRA] A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable); reallocated to long term with rating upgraded;	[ICRA] BBB+ (Stable) / [ICRA] A2	[ICRA]BBB + (Stable) / [ICRA]A2; rating upgraded	[ICRA]BBB (Stable) / [ICRA]A3+	[ICRA]BBB (Stable) / [ICRA]A3+	[ICRA]BBB (Stable) / [ICRA]A3+
4	Non-Convertible Debenture	Long Term	176.50	176.50	[ICRA] A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable); rating upgraded	[ICRA] BBB+ (Stable)	[ICRA]BBB + (Stable); rating upgraded	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)
5	Subordinate Debt Programme (Previously rated as NCD)	Long Term	50	50	[ICRA] A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable); rating upgraded	[ICRA] BBB+ (Stable)	[ICRA]BBB + (Stable); rating upgraded	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable); assigned
6	Non-Convertible Debenture	Long Term	37	-	[ICRA] A- (Stable); withdrawn	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable); rating upgraded	[ICRA] BBB+ (Stable)	[ICRA]BBB + (Stable); rating upgraded	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (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
NA	Fixed Deposit Programme	NA	NA	NA	500.00	MA (Stable)
NA	Long Term Bank Lines	2015-2016	NA	2018-2019	105.12	[ICRA]A- (Stable)
INE428Q07059	Non-Convertible Debenture	6/23/2014	13.5 -14% P.A.	5/28/2019	35.00	[ICRA]A- (Stable)
INE428Q07075	Non-Convertible Debenture*	3/27/2015	14.00% P.A.	3/30/2019	37.00	[ICRA]A- (Stable); withdrawn
INE428Q07083	Non-Convertible Debenture	4/6/2015	14.90%P.A.	12/18/2020	5.00	[ICRA]A- (Stable)
INE428Q07091	Non-Convertible Debenture	5/11/2015	14.25% P.A.	5/13/2021	36.00	[ICRA]A- (Stable)
INE428Q07109	Non-Convertible Debenture	6/1/2015	14.10% P.A.	7/13/2018	41.50	[ICRA]A- (Stable)
INE428Q07117	Non-Convertible Debenture	9/30/2015	13.1011%P.A.	9/30/2020	39.00	[ICRA]A- (Stable)
INE428Q08040	Non-Convertible Debenture	10/27/2016	11.55% P.A.	10/28/2019	20.00	[ICRA]A- (Stable)
INE428Q08016	Subordinated Debt Programme	3/31/2015	17.50% P.A.	12/18/2020	10.00	[ICRA]A- (Stable)
INE428Q08024	Subordinated Debt Programme	9/22/2015	15.85% P.A.	4/23/2021	15.00	[ICRA]A- (Stable)
INE428Q08032	Subordinated Debt Programme	9/21/2016	12.70% P.A.	7/26/2022	25.00	[ICRA]A- (Stable)
NA	Certificate of Deposit Programme	NA	NA	7-365 days	130.00	[ICRA]A1

*Ratings withdrawn; Source: SSFB

Corrigendum:

Document dated May 07, 2018 has been corrected with revisions as detailed below:

- Current rated amount revised under summary of rated instruments on page 1
- Amount outstanding revised under rating history for last three years on page 5

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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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