

March 22, 2022

## Sakthi Finance Limited: Ratings reaffirmed; rated amount enhanced

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible Debentures (NCDs)	497.80	497.80	[ICRA]BBB (Stable); reaffirmed
	19.91	0.00	[ICRA]BBB (Stable); reaffirmed and withdrawn
	0.00	100.00	[ICRA]BBB (Stable); assigned
Fixed Deposits	-	-	MA- (Stable); reaffirmed
Fund Based - Term Loans	83.10	83.10	[ICRA]BBB (Stable); reaffirmed
Fund-based Long-term Facilities from Banks	131.66	131.66	[ICRA]BBB (Stable); reaffirmed
Fund Based – Interchangeable <sup>#</sup>	(60.66)	(68.66)	[ICRA]BBB (Stable)/[ICRA]A2; reaffirmed
Fund-based Short-term Facilities from Banks	100.00	100.00	[ICRA]A2; reaffirmed
<b>Total</b>	<b>832.47</b>	<b>912.56</b>	

\*Instrument details are provided in Annexure-1; <sup>#</sup>Sub-limit of fund-based long-term facilities from banks

### Rationale

The reaffirmation of the ratings takes into consideration Sakthi Finance Limited's (SFL) experience in the retail financing business and its established franchise, which has evolved over the last six decades of its operations. The ratings are, however, constrained by SFL's geographically concentrated operations, the highly competitive business environment, and its subdued profitability indicators. SFL's capitalisation profile is adequate with a gearing of 6.3 times as of December 2021 (provisional; 6.2 times as of March 2021). ICRA notes that the company has deferred its previously stated plan of raising Rs. 25 crore of equity, given the modest portfolio growth and adequate liquidity in the near term.

SFL's 90+ days past due (dpd) stood at 5.0% (provisional) as of December 2021 similar to March 2021 levels. Its liquidity profile is currently adequate; however, it would be crucial for the company to diversify its funding profile to support portfolio growth while maintaining its liquidity profile.

ICRA notes that the sub-debt raised by the company up to FY2020 via a private placement to retail/high-net-worth individual (HNI) investors (Rs. 234 crore outstanding as of December 2021) was not in adherence to the Reserve Bank of India's (RBI) guidelines<sup>1</sup>. While SFL has made its representation to the RBI on this matter and has also requested forbearance, it has stopped taking fresh deposits since H2 FY2021 and stopped renewals since April 2021. SFL's capital adequacy stood at 20.2% (provisional) as of December 2021 without considering the aforementioned sub-debt as Tier II capital. Further, if the outstanding sub-debt is treated as public deposits, the company would be in breach of the cap on deposits at 1.5 times of the net owned funds (NOF) and would also have to augment its statutory liquid assets. Any adverse development regarding the above, including the requirement to increase liquid assets, etc, could impact the company's liquidity. SFL is planning to raise about Rs. 50 crore through the public issuance of debentures (with a greenshoe option of an additional Rs. 50 crore) in May 2022, which is expected to support its liquidity position. The promoters are also expected to provide support, if required, by infusing liquidity or equity.

<sup>1</sup> RBI guidelines on raising money via private placement by a non-banking financial company (NBFC)

ICRA has reaffirmed and withdrawn the rating of [ICRA]BBB (Stable) on the Rs. 19.91-crore non-convertible debenture (NCD) of SFL. These instruments were fully redeemed and there is no amount outstanding against the rated instruments. The rating was withdrawn in accordance with the policy on withdrawal of credit ratings.

## Key rating drivers and their description

### Credit strengths

**Established franchise and presence in regional market** – SFL has a track record of more than six decades in the vehicle finance segment, with operations across Tamil Nadu, Kerala, Andhra Pradesh and Karnataka. It has a good understanding of the target segments, mainly the used commercial vehicle (CV) segment, and has established customer relationships, with repeat customers accounting for about 55-60% of the incremental business.

ICRA notes that the Sakthi Group's presence in related businesses like automotive dealerships has aided in effective origination, prudent appraisal, good market responsiveness, monitoring and collections. The company has a branch-centric operating model with an in-house origination team, which is responsible for collections, while the credit sanctions are centralised. SFL conducts credit bureau checks to screen its customers, followed by field investigation and income assessment and viability analysis as a part of its loan origination process. It has implemented a workflow management system in the majority of its branches, which enables the management to monitor the sourcing and collection activities on a real-time basis.

**Adequate near-term capitalisation structure** – SFL has an adequate capitalisation profile with a gearing<sup>2</sup> of 6.3 times as of December 2021 (provisional; 6.2 times as of March 2021). The company had raised Rs. 25.00 crore through a preferential placement in March 2020, which resulted in an improvement in the gearing level in FY2020 to 6.3 times from 6.8 times in March 2019. The company was expected to raise about Rs. 25 crore from its promoters in H2 FY2022; however, the plan was deferred as the liquidity is adequate and portfolio growth expectation is limited. ICRA notes that the company's modest near-term portfolio growth expectations would keep its capital structure under control. However, as SFL envisages to reduce its gearing to 5.0-6.0 times and improve its growth over the medium to long term, it may require capital infusion for the same.

SFL's total capital adequacy, adjusted for the sub-debt raised via private placement to retail investors, stood at 20.2% (provisional; Tier I at 13.4%) as of December 2021. The company would have to augment its capital to comply with the ceiling on the quantum of deposits (1.5 times of NOF) for NBFCs if the sub-debt were to be treated as public deposits. SFL has made a representation to the RBI and has applied for forbearance in this regard.

### Credit challenges

**Modest portfolio growth; regionally concentrated operations** – SFL's portfolio increased at a modest compound annual growth rate (CAGR) of about 4% during FY2017-FY2021. The portfolio grew by a modest 3.9% in FY2021 to Rs. 1,126 crore and declined by 1.8% in 9M FY2022 to Rs. 1,106 crore as disbursements were adversely impacted due to the Covid-19 pandemic. SFL has a regionally concentrated portfolio with Tamil Nadu and Kerala accounting for 96% of the total portfolio as of December 2021. ICRA expects the portfolio share to remain concentrated, given the company's limited branch expansion plans in the medium term.

**Subdued profitability indicators** – SFL's net interest margin reduced to 5.2% in FY2021 from 5.6% in FY2020 due to slowing demand and low business volumes due to the pandemic. For 9M FY2022 it stood at 5.5% (annualised; provisional) supported by improvement in yields. Its operating cost ratio remained high at 4.0% in 9M FY2022 (3.9% in FY2021 and 4.2% in FY2020) and the credit cost increased to 0.9% in 9M FY2022 from 0.4-0.6% in the prior 5 years. SFL's profit after tax (PAT), as a proportion of total assets, stood at 1.0%, 0.8% and 0.7% (provisional) in FY2020, FY2021 and 9M FY2022, respectively. The

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<sup>2</sup> Net worth (Ind-AS) adjusted for revaluation reserve

company's ability to improve its business margins and operating efficiency further and keep the credit costs under control would be critical for improving its profitability going forward.

**Moderate asset quality** – The 90+dpd was largely stable at 5.0% in December 2021 (provisional) similar to March 2021 levels. The softer bucket overdues (30+dpd) stood at 14.2% in December 2021 and 14.1% in March 2021 (19.4% in March 2020). The company's credit cost stood at 0.9% in 9M FY2022 and 0.6% in FY2021 (0.4-0.6% in FY2018-FY2021) and the provision coverage on gross stage 3 assets improved to 64.2% as of December 2021 from 54.9% in March 2021. SFL has a restructured book outstanding at 0.5% of the loan portfolio as of December 2021. ICRA notes that it would be critical for the company to undertake effective recoveries to keep the asset quality and credit costs under control.

**Access to adequate funding critical to meet long-term growth plans** – SFL has limited financial flexibility as the continued weakness in the performance of the Group entities constrains its ability to secure incremental funding from some banks. However, ICRA notes that SFL has increased its dependence in the recent past on retail/HNI sources and especially via public issuance of debentures. As of December 2021, loans from banks and financial institutions, deposits, NCDs (public issue), NCDs (private placement), preference shares, sub-debt (public issue) and sub-debt (private placement) accounted for 14%, 9%, 39%, 11%, 1%, 3% and 22% respectively, of the total debt. The increase in the share of public NCDs over the recent past, which has led to chunky outflows and the company manages the same at present with a fresh public issuance of NCDs. SFL is in the process of raising about Rs. 100 crore through the public issuance of debentures (including greenshoe option of Rs. 50 crore) by May 2022, which is expected to support its NCD redemptions in May 2022 and help it maintain an adequate liquidity profile. The company's track record of raising monies via public issuance in the past provides comfort. The promoters are also expected to provide support, if required, by infusing liquidity or equity. SFL's ability to diversify its lender base to achieve its long-term growth plans and to maintain adequate liquidity will be a key monitorable.

ICRA notes that the sub-debt raised by the company from retail investors upto FY2020, with an outstanding of Rs. 234 crore as of December 2021, was not in adherence to the RBI's guidelines on raising money via private placement by an NBFC. Accordingly, if the total outstanding sub-debt is treated as public deposits, the company would have to augment investments in liquid assets. While SFL has made its representation to the RBI on the above matter and has also requested forbearance, it has stopped taking fresh deposits since H2 FY2021 and stopped the renewal of existing deposits since April 2021. The requirement to increase investment in liquid assets, etc, could impact the company's liquidity.

## Liquidity position: Adequate

SFL has unencumbered cash and liquid investments of Rs. 39.5 crore and undrawn bank lines of Rs.53.0 crore as on February 28, 2022 with payment obligation of Rs. 129.5 crore for March 2022 - May 2022. Asset Liability Maturity (ALM) profile as on December 31, 2021 does not reflect cumulative negative mismatches upto 12 months. ICRA notes that the company's collections have reached pre-covid levels in Q4 FY2021 by making average monthly collections of Rs.60 crore. The proposed public issuance of NCDs by May 2022 is expected to further bolster its liquidity position. In view of the observations pertaining to the sub-debt, it would be crucial for SFL to ensure the successful placement of its proposed NCDs; this would be important from liquidity perspective in the near term.

## Rating sensitivities

**Positive factors** – ICRA could change the outlook or upgrade the ratings if SFL steadily improves its funding, asset quality and earnings profiles.

**Negative factors** – ICRA could change the outlook or downgrade SFL's ratings in case of a deterioration in its liquidity profile or an increase in the gearing beyond 7.0 times on a sustained basis or a significant weakening in the asset quality, which could adversely impact its earnings.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">ICRA's Credit Rating Methodology for Non-Banking Finance Companies</a> <a href="#">Policy on Withdrawal of Credit Ratings</a>
Parent/Group Support	Not Applicable
Consolidation/Standalone	The ratings are based on the standalone financial statements of SFL

## About the company

Sakthi Finance Limited (SFL), incorporated in 1955, is a part of the Sakthi Group, which has a presence across sectors such as sugar, beverages, automobile and transport dealerships, auto components and textiles. SFL primarily finances CVs, which constituted 90% of its total portfolio as of December 2021. The remaining portfolio consisted of loans towards the purchase of cars, construction equipment and other machinery. SFL primarily operates in Tamil Nadu and Kerala, which together accounted for about 96% of the total portfolio.

In FY2021, SFL reported a net profit of Rs. 9.4 crore on a managed asset base of Rs. 1,214.9 crore compared to a net profit of Rs. 11.1 crore on a managed asset base of Rs. 1,194.1 crore in FY2020. As per the provisional financials for 9M FY2022, the company reported a net profit of Rs. 7.2 crore on a managed asset base of Rs. 1,251.5 crore.

## Key financial indicators (audited)

Sakthi Finance Limited	FY2020	FY2021	9M FY2022 (P)
	Ind-AS	Ind-AS	Ind-AS
Total income (Rs. crore)	168.7	171.0	135.1
Profit after tax (Rs. crore)	11.1	9.4	7.2
Net worth (Rs. crore) *	160.5	166.5	170.1
Total managed portfolio (Rs. crore)	1,083.6	1,126.4	1,106.3
Total managed assets (Rs. crore)	1,194.1	1,214.9	1,251.5
Return on managed assets (%)	1.0%	0.8%	0.7%
Return on net worth (%)	7.6%	5.7%	5.5%
Gearing (times)*	6.3	6.2	6.3
Gross stage 3 (%)	4.6%	5.0%	5.0%
Net stage 3 (%)	2.3%	2.2%	1.8%
Solvency (Net stage 3/Net worth)	15.2%	15.2%	11.5%
CRAR (%)**	19.0%	19.2%	20.2%

Source: Company, ICRA Research; \*Adjusted for revaluation reserve; \*\*Not considering sub-debt (private placement) as Tier II capital

## 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 (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2022		Date & Rating in FY2021		Date & Rating in FY2020	Date & Rating in FY2019	
				Mar 22, 2022	Apr 26, 2021	Aug 04, 2020	Apr 13, 2020	Feb 20, 2020	Apr 06, 2018/ Feb 14, 2019/ Feb 21, 2019	
1 NCDs	Long Term	497.80	497.80	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB&	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	
		19.91	0.00	[ICRA]BBB (Stable); withdrawn	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	
		100.00	0.00	[ICRA]BBB (Stable)	-	-	-	-	-	
2 Fixed Deposits	Medium Term	-	-	MA- (Stable)	MA- (Stable)	MA- (Stable)	MA-&	MA- (Stable)	MA- (Stable)	
3 Term Loans	Long Term	83.10	83.10	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB&	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	
4 Long-term Bank Facilities	Long Term	131.66	131.66	[ICRA] BBB (Stable)	[ICRA] BBB (Stable)	[ICRA] BBB (Stable)	[ICRA]BBB&	[ICRA] BBB (Stable)	[ICRA] BBB (Stable)	
5 Fund-based Interchangeable <sup>^</sup>	Long Term/ Short Term	(68.66)	(68.66)	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BBB&/ [ICRA]A2&	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BBB (Stable)/ [ICRA]A2	
6 Short-term Bank Facilities	Short Term	100.00	100.00	[ICRA] A2	[ICRA] A2	[ICRA] A2	[ICRA] A2&	[ICRA] A2	[ICRA] A2	

## Complexity level of the rated instrument

Instrument	Complexity Indicator
Long-term Fund Based – Cash Credit	Simple
Short-term Fund Based – Working Capital Demand Loan	Simple
Long-term Fund Based – Term Loans	Simple
Fixed Deposit Programme	Very Simple
Non-convertible Debentures	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](http://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
INE302E07193	NCD	May-15-2019	9.75%	May-15-2022	5.92	[ICRA]BBB (Stable)
INE302E07201	NCD	May-15-2019	9.75%	May-15-2022	2.69	[ICRA]BBB (Stable)
INE302E07219	NCD	May-15-2019	-	May-15-2022	8.00	[ICRA]BBB (Stable)
INE302E07227	NCD	May-15-2019	10.00%	May-15-2023	19.09	[ICRA]BBB (Stable)
INE302E07235	NCD	May-15-2019	10.00%	May-15-2023	2.92	[ICRA]BBB (Stable)
INE302E07243	NCD	May-15-2019	-	May-15-2023	15.41	[ICRA]BBB (Stable)
INE302E07250	NCD	May-08-2020	9.50%	May-08-2022	16.91	[ICRA]BBB (Stable)
INE302E07268	NCD	May-08-2020	-	May-08-2022	19.73	[ICRA]BBB (Stable)
INE302E07276	NCD	May-08-2020	9.75%	Aug-08-2023	8.12	[ICRA]BBB (Stable)
INE302E07284	NCD	May-08-2020	9.75%	Aug-08-2023	1.42	[ICRA]BBB (Stable)
INE302E07292	NCD	May-08-2020	-	Aug-08-2023	7.94	[ICRA]BBB (Stable)
INE302E07300	NCD	May-08-2020	10.00%	Jun-08-2024	18.94	[ICRA]BBB (Stable)
INE302E07318	NCD	May-08-2020	10.00%	Jun-08-2024	2.49	[ICRA]BBB (Stable)
INE302E07326	NCD	May-08-2020	-	Jun-08-2024	11.29	[ICRA]BBB (Stable)
INE302E07334	NCD	Jul-29-2021	9.50%	Sep-29-2023	29.49	[ICRA]BBB (Stable)
INE302E07342	NCD	Jul-29-2021	-	Sep-29-2023	32.14	[ICRA]BBB (Stable)
INE302E07359	NCD	Jul-29-2021	9.75%	Oct-29-2024	16.63	[ICRA]BBB (Stable)
INE302E07367	NCD	Jul-29-2021	-	Oct-29-2024	15.95	[ICRA]BBB (Stable)
INE302E07375	NCD	Jul-29-2021	10.00%	Aug-29-2025	35.66	[ICRA]BBB (Stable)
INE302E07383	NCD	Jul-29-2021	-	Aug-29-2025	21.07	[ICRA]BBB (Stable)
INE302E08027	NCD	May-15-2019	10.25%	Jun-15-2024	20.85	[ICRA]BBB (Stable)
INE302E08035	NCD	May-15-2019	10.25%	Jun-15-2024	1.07	[ICRA]BBB (Stable)
INE302E08043	NCD	May-15-2019	-	Jun-15-2024	21.84	[ICRA]BBB (Stable)
INE302E08050	NCD	May-08-2020	10.25%	Jul-08-2025	7.39	[ICRA]BBB (Stable)
INE302E08068	NCD	May-08-2020	10.25%	Jul-08-2025	0.67	[ICRA]BBB (Stable)
INE302E08076	NCD	May-08-2020	-	Jul-08-2025	7.98	[ICRA]BBB (Stable)
INE302E08084	NCD	Jul-29-2021	10.50%	Aug-29-2026	30.89	[ICRA]BBB (Stable)
INE302E08092	NCD	Jul-29-2021	-	Aug-29-2026	16.71	[ICRA]BBB (Stable)
Unutilised	NCD	NA	NA	NA	98.61	[ICRA]BBB (Stable)
Unutilised	NCD – Fresh	NA	NA	NA	100.00	[ICRA]BBB (Stable)
INE302E07177	NCD	May-15-2019	9.50%	May-15-2021	6.47	[ICRA]BBB (Stable); withdrawn
INE302E07185	NCD	May-15-2019	9.50%	May-15-2021	13.44	[ICRA]BBB (Stable); withdrawn
NA	Fixed Deposits	NA	NA	NA	-	MA- (Stable)
NA	Term Loans	NA	NA	NA	83.10	[ICRA]BBB (Stable)
NA	Cash Credit	NA	NA	NA	131.66	[ICRA]BBB (Stable)
NA	Fund-based Interchangeable	NA	NA	NA	(68.66)^	[ICRA]BBB (Stable) /[ICRA]A2
NA	Working Capital Demand Loan	NA	NA	NA	100.00	[ICRA]A2

Source: Company; ^ Sub-limit of fund-based long-term facilities from banks

**Annexure-2: List of entities considered for consolidated analysis – Not Applicable**

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