

August 04, 2022

Arohan Financial Services Limited: Provisional [ICRA]A(SO) assigned to Series A1 SNs backed by microfinance loan receivables issued by Aavishkaar July 2022 Trust I

Summary of rating action

Trust Name	Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Aavishkaar July 2022 Trust I	Series A1 SN	80.15	Provisional [ICRA]A(SO); Assigned

*Instrument details are provided in Annexure I

Rating in the absence of pending actions/documents	No rating would have been assigned as it would not be meaningful
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Rationale

ICRA has assigned a provisional rating to the securitisation notes (SNs) issued under a securitisation transaction originated by Arohan Financial Services Limited {Arohan/originator; [ICRA]A- (Negative)}. The SNs are backed by a pool of Rs. 86.18-crore (principal amount; receivables of Rs. 97.81 crore) microloan receivables originated by Arohan.

The provisional rating is based on the strength of the cash flows from the selected pool of contracts and the credit enhancement available in the form of (i) a cash collateral (CC) of 12.0% of the pool principal to be provided by the originator, (ii) over-collateralisation of 7.0% of the pool principal for Series A1 SN, and (iii) subordination of the entire excess interest spread (EIS) in the structure, as well as the integrity of the legal structure. The rating is subject to the fulfilment of all the conditions under the structure and the review of the documentation pertaining to the transaction by ICRA.

Key rating drivers

Credit strengths

- Availability of credit enhancement in the form of EIS, over-collateralisation and CC
- No overdue contracts in the pool as on the cut-off date

Credit challenges

- High geographical concentration with top 3 states contributing ~83%
- Pool's performance will remain exposed to any fresh disruptions that may arise due to the Covid-19 pandemic
- Performance of the pool would also remain exposed to natural calamities that may impact the income-generating capability of the borrower, given the marginal borrower profile; further, pool's performance would be exposed to political and communal risks

Description of key rating drivers highlighted above

According to the transaction structure, the loan pool receivables will be assigned at par to the SN investors. The monthly cash flow schedule comprises the promised interest payment to Series A1 SN at the predetermined interest rate on the principal outstanding and the entire principal on the final maturity date. The surplus EIS and over-collateralisation available after meeting the promised and expected payouts to the SNs will be passed on to the originator every month.

In the event of a shortfall in meeting the promised SN payouts during any month, the Trustee will utilise the CC to meet the shortfall. The principal amount collected upon the pre-termination of contracts will be paid to Series A1 SN. Following such prepayment, the future payment schedule for the SNs will be revised.

The first line of support for Series A1 SN in the transaction is in the form of over-collateralisation of 7.0% of the pool principal. Further credit support is available in the form of an EIS and a CC of 12.0% of the initial pool principal (i.e. Rs. 10.34 crore) to be provided by Arohan.

There are no overdues in the pool as on the cut-off date. It has high geographical concentration with the top 3 states (Bihar, West Bengal and Uttar Pradesh) contributing 83.2% to the initial pool principal amount. Concentration is modest at the district level with the top 5 districts accounting for 17.2% of the initial pool principal amount. The performance of the pool would be exposed to political and communal risks and natural calamities that may impact the income-generating capability of the borrower. It would also remain exposed to any fresh disruptions that may arise due to the pandemic.

Past rated pools: ICRA has ratings outstanding on 15 pass-through certificate (PTC) transactions originated by Arohan. Live pools have reported satisfactory collections with nil CC utilisation up to the June 2022 payouts.

Key rating assumptions

ICRA's cash flow modelling for rating asset-backed securitisation (ABS) transactions involves the simulation of potential delinquencies, losses (shortfall in principal collection during the tenor of the pool) and prepayments in the pool. The assumptions for the loss and coefficient of variation (CoV) are arrived at after taking into account the performance of the originator's portfolio as well as the characteristics of the specific pool being evaluated. Additionally, the assumptions may be adjusted to factor in the current operating environment and any industry-specific factors that ICRA believes could impact the performance of the underlying pool of contracts.

After making these adjustments, the expected mean shortfall in principal collection during the tenure of the pool is estimated at 4.25-5.25% of the initial pool principal, with certain variability around it. The prepayment rate for the underlying pool is estimated at 6.0-9.0% per annum.

Liquidity position: Strong

As per the transaction structure, only the interest amount is promised to the SN holders on a monthly basis while the principal amount is promised on the scheduled maturity date of the transaction. Overall, the cash flows from the pool and the available credit enhancement are expected to be comfortable to meet the payouts to the Series A1 SN investors.

Rating sensitivities

Positive factors – The sustained strong collection performance of the underlying pool of contracts (monthly collection efficiency >95%), leading to lower-than-expected delinquency levels, and an increase in the cover available for future investor payouts from the credit enhancement would result in a rating upgrade.

Negative factors – The sustained weak collection performance of the underlying pool (monthly collection efficiency <90%), leading to higher-than-expected delinquency levels and higher credit enhancement utilisation levels, would result in a rating downgrade.

Analytical approach

The rating action is based on the analysis of the performance of Arohan's portfolio till March 2022, the key characteristics and composition of the current pool, the performance expected over the balance tenure of the pool, and the credit enhancement cover available in the transaction.

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Securitisation Transactions
Parent/Group support	Not Applicable

Consolidation/Standalone

Not Applicable

Pending actions/documents required to be completed for conversion of the provisional rating into final

The assigned rating is provisional and would be converted into final upon the execution of:

1. Trust deed
2. Assignment agreement
3. Legal opinion
4. Trustee letter
5. Chartered Accountant's know your customer (KYC) certificate
6. Any other documents executed for the transaction

Validity of the provisional rating

The Trust is expected to complete the pending actions/execute the pending documents in the near term. However, in case of continued pendency of the actions/documents beyond one year of this publication, the provisional rating would be withdrawn for the transaction even if the instrument has been issued.

Risks associated with the provisional rating

In case the issuance is completed, but the pending actions/documents are not completed for the transaction within one year (validity period) from the assignment of the rating, the provisional rating will be withdrawn in accordance with ICRA's Policy on Provisional Ratings available at www.icra.in.

About the company

Arohan Financial Services Limited is a Kolkata-headquartered non-banking financial company-microfinance institution (NBFC-MFI). It was incorporated on September 27, 1991. Arohan is engaged in the business of microlending mainly to women borrowers and operates on the joint liability group (JLG) model. It was set up through the acquisition of an existing NBFC, ANG Resources Ltd, with the support of Bellwether Microfinance Fund. The company's name was changed to Arohan Financial Services Limited in March 2008. Arohan became a part of the Aavishkar Group in September 2012. As on March 31, 2022, it was catering to 18.6 lakh borrowers through a network of 749 branches spread across 224 districts and 14 states while managing a portfolio of Rs. 4,122 crore.

Key financial indicators (audited)

	FY2020	FY2021	FY2022
Total income	935	1,014	920
Profit after tax	127	(160)	61
Gross loan portfolio	4,854	4,648	4,122
Gross non-performing assets (NPA)	2.3%	11.2%	4.5%
Net NPA	-	4.0%	1.4%

Source: Company data, 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

Trust Name	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years		
	Instrument	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
				Aug 04, 2022			
Aavishkaar July 2022 Trust I	Series A1 SN	80.15	80.15	Provisional [ICRA]A(SO)	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Series A1 SN	Moderately Complex

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 I: Instrument details

Trust Name	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating
Aavishkaar July 2022 Trust I	Series A1 SN	July 2022	9.55%	April 2024*	80.15	Provisional [ICRA]A(SO)

* Scheduled PTC maturity date at transaction initiation; may change on account of prepayments

Source: Company

Annexure II: List of entities considered for consolidated analysis

Not applicable

ANALYST CONTACTS

Abhishek Dafria

+91 22 6114 3440

abhishek.dafria@icraindia.com

Sachin Joglekar

+91 22 6114 3470

sachin.joglekar@icraindia.com

Rushabh Gohel

+91 22 6114 3420

rushabh.gohel@icraindia.com

Diptajyoti Banik

+91 22 6114 3412

diptajyoti.banik@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee

+91 80 4332 6401

jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani

Tel: +91 124 4545 860

communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited



Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45



Branches



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