

November 18, 2022

SK Finance Limited (erstwhile Ess Kay Fincorp Limited): Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible Debentures	104.17	30.06	[ICRA]AA+(CE) (Stable); reaffirmed
Principal Protected Market Linked Debentures (PP-MLD)	125.00	125.00	PP-MLD [ICRA]AA+(CE) (Stable); Outstanding
PP-MLD	50.90	50.90	PP-MLD [ICRA]AA+(CE) (Stable); Outstanding
Non-convertible Debentures	35.00	35.00	[ICRA]A+ (Stable); Outstanding
LT – Market Linked Debentures	150.00	150.00	PP-MLD [ICRA]A+ (Stable); Outstanding
Long-term Fund-based Term Loan	275.00	275.00	[ICRA]A+ (Stable); Outstanding
Total	740.07	665.96	

Rating Without Explicit Credit Enhancement	[ICRA]A+
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*Instrument details are provided in Annexure I

Note: The (CE) suffix mentioned alongside the rating symbol indicates that the rated instrument/facility is backed by some form of explicit credit enhancement. This rating is specific to the rated instrument/facility, its terms and structure and does not represent ICRA's opinion on the general credit quality of the entity concerned. The last row in the table above also captures ICRA's opinion on the rating without factoring in the explicit credit enhancement

Rationale

The reaffirmation of ratings considers the structural features available in the transaction such that in the event of non-payment by SK Finance Limited (SKFL) of its expected repayments, the cover pool along with the cash collateral (CC) would be utilised to support the servicing of the rated instruments. The key structural features of the rated instruments are summarised below.

Instrument	Trust Name	Security Cover	Structural Feature
Rs. 104.17-crore NCDs	Vivriti Omega Trust II 2020	1.21x cover pool [^] and Rs. 6-crore CC	Pool has been assigned upfront to the trust; post trigger events, all collections from the cover pool along with the CC will be used to transfer to the Debenture Trustee of the NCDs

[^] The cover pool requirement is calculated on the outstanding principal

The ratings draw comfort from SKFL's established presence in the used vehicle financing space and its demonstrated ability to scale up its business, while maintaining healthy capitalisation and controlling slippages, despite the challenging operating environment. Nonetheless, post any trigger event, the performance of the cover pool would be exposed to macro-economic/business disruptions, if any.

Structure details, adequacy of credit enhancement and salient features of rated instruments

The non-convertible debentures (NCDs) issued in November 2020, have a final legal maturity of 48 months and were likely to be fully repaid in 36 months, as SKFL is required to service the NCD payments on a monthly basis as per an expected payment schedule. In November 2021, SKFL, with consent from the investor, had made following changes to the terms of these NCDs:

- No further assignment of loan contracts to the cover pool;

- As the cover pool would not be replenished with new contracts, SKFL will prepay such an amount on the NCDs every month to maintain the stipulated cover on the outstanding amount;
- Also, the prepayment will not impact the amortisation schedule of the NCDs, i.e. prepayments will be adjusted against last repayments.

Hence the cover pool is now static in nature due to the above changes and are expected to amortise in less than 36 months from the date of issuance.

Details on the structure, adequacy of the credit enhancement and salient features of the rated instrument are available in ICRA's previous rating rationale.

Key rating drivers and their description

Credit strengths

Presence of cover pool to support servicing of the rated facility in the event of non-payment by entity – The primary obligation of meeting the NCD payments is on SKFL. However, if SKFL does not meet the expected payment on the NCDs, the collections from the cover pool and CC (Rs. 6 crore) will be available to the Debenture Trustee. The principal as well as the interest on the NCDs are promised to the NCD investors on the legal maturity date.

Stringent eligibility criteria for cover pool – The eligibility criteria for the cover pool is stringent. The proportion of contracts in the pool which are delinquent, but less than 30 days, should be less than 5% of the pool principal outstanding and exclusion of all greater than 60 days delinquent contracts.

Credit challenges

Portfolio remains exposed to high geographical concentration mix – Notwithstanding the strong scale-up achieved by SKFL over the past few years, its scale of operations remains modest. Further, it has, over the years, expanded its reach to 10 states in India through a network of about 435 branches as on September 30, 2022. However, it remains a regional player with Rajasthan accounting for 58% of the portfolio as on September 30, 2022, which has moderated from 94% as of March 2014. The balance lending portfolio is primarily in Chhattisgarh, Gujarat, Maharashtra, Madhya Pradesh, Punjab and Haryana.

Pool's performance will remain exposed to macro-economic shocks/business disruptions, if any, post trigger event – The ratings factors in the risks associated with macro-economic shocks (if any) faced by the borrowers, which could affect the continuity of business operations and the possible adverse impact on the asset quality if the cash flows and economic activity slows down, post a trigger event.

Liquidity position

For [ICRA]AA+(CE) (Stable) rating: Strong

Both the principal and the interest amount on the NCDs are promised to the lender on the legal final maturity date subject to the non-occurrence of a trigger event. The cash flows from the cover pool, along with the CC, are expected to be comfortable to meet the debt servicing in the event that the entity is unable to meet the scheduled payments on the NCDs.

For the [ICRA]A+ rating without explicit credit enhancement: Strong

SKFL's ALM profile, in the normal course of business, is characterised by positive cumulative mismatches in the buckets up to 1 year. As per the ALM profile as on September 30, 2022, the company has debt maturities of Rs. 2,368 crore for the 1-year period ending September 30, 2023, against which it has inflows of Rs. 2,012 crore from the performing advances. The on-balance sheet liquidity of Rs. 1,397 crore (cash and liquid investments), which is 24.3% of the total borrowings coupled with undrawn working capital lines of about Rs. 89 crore, further supports the company's liquidity profile.

Rating sensitivities

For [ICRA]AA+(CE) (Stable) rating

Positive factors – The ratings are unlikely to be upgraded in the near term.

Negative factors – The ratings could be downgraded on non-adherence to the key transaction terms envisaged at the time of assigning the same. The ratings could also come under pressure on a deterioration in SKFL's credit profile.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Non-banking Finance Companies Covered Bond Transactions
Parent/Group support	Not Applicable
Consolidation/Standalone	Not Applicable

About the company

Incorporated in 1994, SKFL is a Jaipur (Rajasthan) headquartered non-banking financial company (NBFC) registered with the Reserve Bank of India (RBI). It primarily finances used light commercial vehicles, multi-utility vehicles, cars, tractors and two-wheelers. It also advances small and medium enterprise (SME) loans. SKFL has a network across 10 states, namely Rajasthan, Gujarat, Maharashtra, Madhya Pradesh, Punjab, Haryana, Chhattisgarh, Uttarakhand, Himachal Pradesh and Delhi, though Rajasthan occupies a predominant share of ~58% in the portfolio as on September 30, 2022. As on September 30, 2022, the assets under management (AUM) stood at Rs. 5,960 crore.

The promoter group, viz. Mr. Rajendra Setia and his family members, held 38.7% equity share in the company as on September 30, 2022. Other key equity investors include Northwest Venture Partners, TPG Capital, Evolve and Baring India with equity shareholding of 24.5%, 19.0%, 5.6% and 4.7%, respectively, as on September 30, 2022.

Key financial indicators (audited)

SKFL	FY2021	FY2022	H1 FY2023
Total Income	683	821	591
Profit after tax	91	143	97
AUM	3,417	4,714	5,960
Gross NPAs	4.1%	2.8%	3.1%
Net NPAs	1.9%	2.0%	2.2%

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

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years									
		Type	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating		Date & Rating in FY2022		Date & Rating in FY2021						Date & Rating in FY2020
					Nov 18, 2022	Jul 29, 2022	Nov 19, 2021	Jul 30, 2021	Mar 18, 2021	Mar 10, 2021	Feb 4, 2021	Feb 1, 2021	Dec 2, 2020	Nov 19, 2020	-
1	NCD	Long term	150.00	30.06	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	[ICRA]AA+(CE) (Stable)	Provisional [ICRA]AA+(CE) (Stable)	-
2	PP-MLD	Long term	125.0	125.0	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	Provisional PP-MLD [ICRA]AA+(CE) (Stable)	-	-	-	-	-
3	PP-MLD	Long term	50.9	50.9	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	PP-MLD [ICRA]AA+(CE) (Stable)	Provisional PP-MLD [ICRA]AA+(CE) (Stable)	-	-	-

Complexity level of the rated instrument

Transaction Name	Instrument	Complexity Indicator
Vivriti Omega Trust II 2020	Non-convertible Debentures (NCDs)	Highly Complex
Elements 2021 CE MLD	Principal Protected Market Linked Debentures (PP-MLD)	Highly Complex
Northern Arc 2021 CE MLD Hemera	Principal Protected Market Linked Debentures (PP-MLD)	Highly 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: [Click Here](#)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE124N07507	NCD	Nov 19, 2020	9.80%	Nov 19, 2024	30.06	[ICRA]AA+(CE) (Stable)
INE124N07549	PP-MLD	Mar 09, 2021	8.90%*	Mar 09, 2026	125.0	PP-MLD [ICRA]AA+(CE) (Stable)
INE124N07523	PP-MLD	Jan 28, 2021	9.50%*	Jul 28, 2024	50.90	PP-MLD [ICRA]AA+(CE) (Stable)

* Additionally, step-up interest of 4.0% is applicable from the date of issuance in case of trigger event

Source: Company

Annexure II: List of entities considered for consolidated analysis

Not Applicable

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About ICRA Limited:

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