April 11, 2023

PNB Housing Finance Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible debentures	600.0	600.0	[ICRA]AA (Stable); reaffirmed
Tier II bonds	200.0	200.0	[ICRA]AA (Stable); reaffirmed
Total	**800.0**	**800.0**	

**Instrument details are provided in Annexure I*

Rationale

The rating reaffirmation factors in PNB Housing Finance Limited's (PNBHFL) established track record in the mortgage finance industry, its diverse funding profile and the improvement in its leverage profile. Its managed gearing[1] declined to 5.6 times as on December 31, 2022 from 6.3 times as on March 31, 2022. Further, PNBHFL is in the process of raising equity of up to Rs. 2,500 crore via a rights issue, which is expected to conclude in Q1 FY2024. The rights issue, if fully subscribed, will help the company reduce its managed gearing further and support its envisaged growth while maintaining prudent capitalisation.

PNBHFL also has a well-diversified funding profile comprising funding from banks, National Housing Bank (NHB), non-convertible debentures (NCDs) & bonds, deposits and external commercial borrowings (ECBs). ICRA also expects that the company will continue to benefit from its experienced management team and the shared brand name with its promoter, i.e. Punjab National Bank (PNB; rated [ICRA]AA+ (Stable)/[ICRA]A1+, [ICRA]AA (Stable) for Basel III Tier I Bonds), which helps it leverage its franchise and raise funds, thereby supporting its financial flexibility.

ICRA also notes that PNBHFL continues to reduce its wholesale exposure, which has declined materially in the past few years. Wholesale exposures declined to ~7% of the assets under management (AUM) as on December 31, 2022 from ~11% in March 2022 (~21% as on March 31, 2019). This was supported by write-offs, resolutions, rundown and accelerated prepayments in the corporate book.

The rating is, however, constrained by the weak, albeit improving, asset quality indicators and the moderate profitability metrics. PNBHFL reported gross non-performing assets (GNPAs) of 4.9% as on December 31, 2022 against 8.1% as on March 31, 2022 (8.2% as on December 31, 2021). Net recoveries via the legal route and one-time settlements (OTS), along with write-offs, has helped the company reduce its stressed book. Though the profitability improved in 9M FY2023, it remains moderate due to the relatively higher credit costs.

ICRA notes that the risks are partly mitigated by the good collateral cover maintained by the company and the adequate provision coverage ratio (PCR) as on December 31, 2022. The overall PCR, with the reduction in NPAs, declined in 9M FY2023 and stood at 3.0% of total assets against 4.4% in March 2022. The PCR on GNPAs stood at 35% as on December 31, 2022 vis-à-vis 38% in March 2022.

The Stable outlook reflects ICRA's expectation that the company will be able to arrest any major slippages and recover from its stressed book. Moreover, it is expected to maintain and improve its credit profile, aided by its experienced board and management.

[1] Managed gearing = (on-book debt + off-book portfolio)/ net worth

Key rating drivers and their description

Credit strengths

Established player in mortgage lending market – PNBHFL has an established presence and a long track record of operations in the housing finance industry with a presence in 19 states/Union Territories (UTs) in India. It also has a seasoned management team with sound knowledge of the mortgage industry and its board has prior experience in banking, insurance, retail lending, technology and economic policy. For the last few years, it increased its focus on the retail segment and started reducing its wholesale exposure, which led to a decline in its AUM since FY2020. Its AUM stood at Rs. 64,685 crore as on December 31, 2022 compared to Rs. 65,977 crore as on March 31, 2022 (Rs. 74,469 crore as on March 31, 2021). PNBHFL registered a degrowth of ~3% (annualised) in its AUM in 9M FY2023, given the decline in the wholesale book, whereas its retail book grew 7% (annualised) during this period.

As on December 31, 2022, ~65% of the on-book portfolio was towards individual housing loans (HL), ~21% towards retail loan against property (LAP), ~5% towards retail non-residential premises loans (NRPLs), ~9% towards corporate book (which includes construction finance, corporate term loans and corporate lease rental discounts). The company also reported an off-book portfolio of Rs. 7,554 crore as on December 31, 2022 against Rs. 9,088 crore as on March 31, 2022. With focus on the retail book including the affordable segment – Roshni, PNBHFL opened 60 branches (including Roshni) in 9M FY2023. It plans to open more locations to cater to the affordable housing finance segment.

Shared brand name and benefits with PNB as the promoter – With PNB being its promoter and holding a stake of 32.5% as on December 31, 2022, PNBHFL has a competitive advantage. The common brand name supports its financial flexibility and deposit mobilisation. PNBHFL's board comprised two directors from PNB as on December 31, 2022. As per the revised trademark agreement between PNBHFL and PNB, entered in May 2021, PNBHFL is required to pay a royalty for the use of PNB's brand name if PNB's stake falls below 30%. Further, if PNB's shareholding falls below 20%, it would have the right to terminate the revised agreement. In case of such termination, PNBHFL shall be allowed a transition period of up to 24 months to change its brand name. ICRA notes that post the completion of the planned rights issue, given PNB's stated intent to invest up to Rs. 500 crore, PNB's shareholding in PNBHFL may decline to less than 30%, though it will remain above 26%. Further, PNB has stated that they will continue to be the promoter of the Company.

Diversified funding mix and demonstrated refinancing ability – PNBHFL has managed to maintain a healthy funding mix comprising NCDs (8.6% of the funding mix as on December 31, 2022), deposits (29.8%), bank borrowings (34.0%), NHB (5.5%), ECBs (9.6%) and off-book exposure (direct assignment and co-lending; 12.6%). The cost of average borrowings increased to 7.3% in 9M FY2023 from 7.2% in FY2022 owing to higher interest rates in 9M FY2023.

Credit challenges

Weak, albeit improving, asset quality – PNBHFL's overall asset quality metrics remain weak with reported gross and net NPAs of 4.9% and 3.2%, respectively, as on December 31, 2022. Although weak, the asset quality has improved over the past few quarters from GNPA and NNPA of 8.2% and 5.1%, respectively, as on December 31, 2021. The reduction in the GNPAs was on account of the resolution of a few large wholesale exposures (via sale to an ARC, project transfer to another developer, etc), write-offs of Rs. 1,267 crore in 9M FY2023, recoveries and OTS for some stressed exposures. ICRA notes that the management is committed to bring down the remaining stressed book. However, the same remains relatively high, with GNPA of 4.9%, restructured book of 3.1%, and security receipts (SRs) and repossessed assets outstanding as on December 31, 2022.

The risk is partly mitigated by the good collateral cover maintained by the company and the adequate PCR as on December 31, 2022. Its overall PCR declined in 9M FY2023, with the reduction in the NPAs, though it remains adequate at 3.0% of total assets. The PCR on GNPAs stood at 35% as on December 31, 2022 vis-à-vis 38% in March 2022. ICRA notes that the collateral cover maintained on corporate exposures and the loan-to-value (LTV) at origination for the retail segment (~71% in HL and ~49% in LAP) mitigate the risk to some extent. The management's ability to arrest further slippages and make healthy recoveries shall remain critical from a credit perspective.

Moderate profitability on account of elevated credit costs – PNBHFL reported a profit after tax (PAT) of Rs. 767 crore in 9M FY2023, translating into a return on average managed assets (RoMA) of 1.3% and a return on average net worth (RoNW) of 9.9% against Rs. 836 crore, 1.0% and 8.9%, respectively, in FY2022. The improvement was on account of the higher net interest margin (NIM) as the company was able to improve its yield while keeping the cost of borrowings under control. Though PNBHFL's operating profitability improved in 9M FY2023, the same was somewhat negated by the higher credit cost of 1.1% (annualised) with respect to average managed assets (AMA) against 0.7% in FY2022. ICRA expects the credit cost to decline, going forward, on account of the reduced stressed book and the expected recoveries from the written-off accounts, which should improve the overall profitability.

Environmental and social risks

Environmental – While housing finance companies (HFCs) like PNBHFL do not face material physical climate risks, they are exposed to environmental risks indirectly through their portfolio of assets. If the borrowers, to which such HFCs have an exposure, face livelihood disruption because of physical climate adversities, it could translate into credit risks for the HFCs. However, such risk is not material for PNBHFL as it benefits from portfolio diversification.

Social – With regard to social risks, data security and customer privacy are among the key sources of vulnerability for HFCs, as any material lapse could be detrimental to their reputation and invite regulatory censure.

Liquidity position: Strong

While the company remains exposed to asset-liability related risks given the longer tenor of the assets, its liquidity is supported by a good share of long-term and short-term borrowings and its plans to keep adequate liquid investments and unutilised lines to meet the gaps. It had cash and cash equivalents of Rs. 3,877 crore as on December 31, 2022 and collections due (as per behavioural analysis of asset liability management statement (ALM)) of Rs. 6,535 crore (excluding NPAs and including restructured book) against debt repayments of Rs. 9,014 crore till June 30, 2023. Further, PNBHFL had unavailed sanctions and working capital lines of Rs. 3,350 crore as on December 31, 2022 and pending committed disbursements of Rs. 3,676 crore. The cumulative mismatch up to the 6-month bucket, as per the provisional structured liquidity statement (SLS) for December 2022, is nil without factoring in the net interest income and committed disbursements and sanction lines. The company maintained a healthy liquidity coverage ratio (LCR) of 117%, as on December 31, 2022, against the regulatory requirement of 60%.

Rating sensitivities

Positive factors – PNBHFL's rating could be upgraded or the outlook could be revised to Positive if it is able to grow its scale of operations, while improving its overall asset quality and profitability profile, and maintain a prudent capitalisation profile.

Negative factors – Pressure on the rating would arise in case of a further deterioration in PNBHFL's asset quality and/or its inability to make a meaningful recovery out of its stressed assets. Pressure on its profitability (with RoMA <1% on sustained basis), a material decline in the scale of operations, higher gearing and challenges in fund raising, restricting PNBHFL's ability to lend or leading to a deterioration in its liquidity profile, could also exert pressure on the rating.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Rating Methodology for Non-banking Finance Companies (NBFCs)] [Rating approach - Consolidation]
Parent/Group support	Not applicable
Consolidation/Standalone	The rating is based on the consolidated financial profile of the company

About the company

Incorporated in 1988, PNBHFL is a deposit-accepting housing finance company. PNB and the Carlyle Group had a stake of 32.5% and 32.1%, respectively, as on December 31, 2022. The company offers home loans, LAP, builder loans and LRD. PNBHFL is geographically diversified with its portfolio spread across 19 states/UTs. As on December 31, 2022, PNBHFL reported an AUM of Rs. 64,685 crore (IndAS valuation at Rs. 65,753 crore) against Rs. 65,977 crore in March 2022.

Key financial indicators (audited)

PNBHFL	FY2021	FY2022	9M FY2023*
Accounting as per	**IndAS**	**IndAS**	**IndAS**
Total income	7,624	6,201	4,892
Profit after tax	930	836	767
Net worth	8,923	9,872	10,707
Loan book	62,254	57,895	58,033
Total managed assets	86,150	77,377	74,428
Return on average managed assets	1.0%	1.0%	1.3%
Return on average net worth	11.0%	8.9%	9.9%
Managed gearing (times)	8.1	6.3	5.6
Gross stage 3	4.4%	8.1%	4.9%
Net stage 3	2.4%	5.1%	3.2%
Solvency (Net stage 3/Net worth)	17.0%	29.7%	17.2%
CRAR	18.7%	23.4%	24.6%

*Source: Company, ICRA Research; * Limited review numbers; All ratios as per ICRA's calculations; Amount in Rs. crore*

Total managed assets includes ECL provision and off-book portfolio

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31, 2023 (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					Apr 11, 2023	Apr 12, 2022	May 28, 2021	Apr 3, 2020
1	NCD programme	Long term	600	450	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Negative)	[ICRA]AA (Negative)
2	Tier II bonds	Long term	200	200	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Negative)	[ICRA]AA (Negative)
3	NCD programme	Long term	-	-	-	[ICRA]AA (Stable); withdrawn	[ICRA]AA (Negative)	[ICRA]AA (Negative)

Complexity level of the rated instruments

Instrument	Complexity Indicator
NCD programme	Very simple
Tier II bonds	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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE572E09239	**NCD**	Jan-31-2014	9.48%	Jan-31-2024	300	[ICRA]AA (Stable)
INE572E07092	**NCD**	Mar-17-2023	8.70%	Sep-17-2024	150	[ICRA]AA (Stable)
Not issued	**NCD**	NA	NA	NA	150	[ICRA]AA (Stable)
INE572E09262	**Tier II bonds**	Nov-24-2014	8.70%	Nov-24-2024	200	[ICRA]AA (Stable)

Source: Company, ICRA Research

Annexure II: List of entities considered for consolidated analysis

Company Name	PNBHFL Ownership	Consolidation Approach
PHFL Home Loans and Services Ltd.	100.00%	Full Consolidation

Source: PNBHFL's Annual Report

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