September 25, 2023

Unity Small Finance Bank Limited: Rating confirmed as final for PTCs backed by secured LAP receivables issued by Marathon

Summary of rating action

Trust Name	Instrument*	Initial Rated Amount (Rs. crore)	Current Rated Amount ^ (Rs. crore)	Rating Action
Marathon	Series A1 PTC	81.10	78.62	[ICRA]AA-(SO); provisional rating confirmed as final

*^ Provisional rating amount was Rs. 81.10 crore for Series A1 PTC. Actual PTC issuance was lower. *Instrument details are provided in Annexure I*

Rationale

In July 2023, ICRA had assigned a Provisional [ICRA]AA-(SO) rating to the pass-through certificates (PTCs) issued under a securitisation transaction originated by Unity Small Finance Bank Limited {Unity SFB; rated [ICRA]A- (Stable)}. The PTCs are backed by a pool of Rs. 158.67-crore secured loan against property (LAP) receivables (underlying pool principal of Rs. 84.54 crore). During the provisional rating assignment, the pool principal was Rs. 87.21 crore while the pool receivables were Rs. 163.50 crore. However, the pool underwent a downward revision of 3.07% of the original principal outstanding due to deletion of certain contracts. There has been no addition of contracts in the pool or change in the transaction structure or other terms and conditions. Since the executed transaction documents are in line with the rating conditions and the legal opinion for the transaction has been provided to ICRA, the said ratings have now been confirmed as final.

Update on pool performance

The pool performance post August 2023 payout month for the pool is captured in the table below.

Exhibit 1: Key pool summary till August 2023 payout month

Parameter	Marathon
Months post securitisation	2
Number of PTC payouts made to PTC investors	1
Pool amortisation	2.89%
Scheduled pool amortisation	0.46%
Series A1 PTC Amortisation	3.10%
Cumulative prepayment rate	2.42%
Cumulative collection efficiency	99.54%
Loss-cum-0+ dpd	0.46%
Loss cum 30+ dpd	0.00%
Loss cum 90+ dpd	0.00%
Cumulative cash collateral (CC) utilisation	0.00%

Key rating drivers

Credit strengths

- Availability of CE in the form of EIS, principal subordination and CC
- Absence of overdue contracts as on pool cut-off date; ~97% of the contracts in the initial pool have never been delinquent
- Average seasoning of ~14 months

Credit challenges

- High geographical concentration with top 3 property states accounting for ~76% of the contracts in the initial pool
- While the pool yield is fixed, the interest rate on the PTCs is linked to the repo rate, leading to interest rate risk in the structure
- Performance of the pool would remain exposed to macro-economic shocks/business disruptions/natural calamities, which may impact the income-generating capability of the borrower

Description of key rating drivers highlighted above

The first line of support for Series A1 PTCs in the transaction is in the form of a subordination of 7.0% of the initial pool principal, which will be in the form of an equity tranche (Series A2 PTCs). The EIS available after meeting the promised payouts (as per the waterfall mechanism) to Series A1 PTCs will be passed on as the expected yield to Series A2 PTC. Series A2 PTC payouts are completely subordinated to Series A1 PTC and the EIS will be available as support for principal payment to Series A2 PTC only after Series A1 PTC has been fully paid. A CC of 3.00% of the initial pool principal (Rs. 2.54 crore), have been provided by Unity SFB, would act as further CE in the transaction. Further, the transaction has a liquidity facility amounting to 2.00% of the initial pool principal outstanding, i.e. Rs. 1.69 crore, maintained in the form of a fixed deposit. In the event of a shortfall in meeting the promised PTC payouts during any month, the trustee will utilise the liquidity facility first followed by the CC to meet the shortfall.

As per the transaction structure, the monthly promised cash flows for Series A1 PTC will comprise the scheduled principal amount (which is 93% of the billed pool principal) and the interest payment to Series A1 PTC at the predetermined interest rate on the principal outstanding. The surplus, in relation to the principal portion of the pool's receivables along with any prepayment amount, would be used for the payment of Series A1 for faster amortisation. Following the payment of Series A1 PTC in full, the principal for Series A2 PTC is to be paid monthly on expected basis (to the extent of billing). Further, the yield on Series A2 PTC is in the form of the EIS in the structure.

The pool comprises 397 secured LAP contracts with future receivables of Rs. 158.67 crore (underlying principal of Rs. 84.54 crore). While the weighted average seasoning of the pool remains moderate at ~14 months, the adequate borrower profile, with a substantial share of the loan contracts (~60%) having a CIBIL score of more than 750, provides comfort. There were no overdue contracts in the pool as on the cut-off date. Also, 97% of the contracts (calculated on principal amount) have never been delinquent in the past.

The pool has high geographical concentration with the top 3 states (Telangana, Gujarat and Uttar Pradesh) contributing ~76% to the initial pool principal amount. It also has moderate obligor concentration with the top borrower accounting for 4.5% of the initial pool principal. Further, the pool comprises fixed rate loans, while the PTC yield is floating. Hence, the transaction is exposed to interest rate risk. Furthermore, the performance of the pool would remain exposed to macro-economic shocks/business disruptions/natural calamities that may impact the income-generating capability of the borrower.

Past rated pools: This is the first transaction of Unity SFB to be rated by ICRA.

Key rating assumptions

The pool comprises 397 secured LAP contracts, amounting to Rs. 84.54 crore. All the contracts in the pool are current as of the cut-off date while around 60% of the pool had a CIBIL score of more than 750. Nearly 97% of the contracts in the pool have never been delinquent in the past. The pool has high geographical concentration with the share of the top 3 states (Telangana, Gujarat and Uttar Pradesh) at ~76% of the initial pool.

The obligor concentration in the pool is moderate (top obligor accounting for 4.5% of the pool). Thus, the pool's performance is likely to get influenced by the performance of the top contract. The average ticket size is Rs. 22.55 Lakhs and weighted average original LTV is 38.93%. The variability of loss in case of a concentrated pool would be slightly higher than that of a regular granular pool. All loans pertaining to a borrower have been clubbed as one because if an entity defaults, it would most likely default on all its loans to a lender. ICRA's rating/credit assessment of the entities, along with the balance tenure of the loans given to these entities, has been considered to estimate the default probability for each loan. ICRA has also built in the assumptions on the quantum and timing of recovery post default. Further, a certain loss given default (LGD) has been assumed by factoring in the repossession and sale of the underlying assets. We have assumed that the recovery, post the default by a borrower, would happen with a lag. Various possible scenarios are simulated and the incidences of default to the investor as well as the extent of losses are measured.

Further, for the granular portion of the pool (95.5% of the pool), the portfolio loss has been adjusted for the pool's composition depending on whether the pool deviates positively or negatively from the portfolio on various parameters that might have a bearing on the eventual loss level. For the current pool, we have incorporated the above arguments and adjusted for various pool features like seasoning, overdues, peak days past due (dpd), loan-to-value (LTV), geography, property type, internal rate of return (IRR), and ticket size.

ICRA's cash flow modelling for the rating of PTCs backed by secured LAP receivables involves the simulation of potential losses, delinquencies and prepayments in the pool. The losses and prepayments are assumed to follow a log-normal distribution. The mean and the coefficient of variation (CoV) are calibrated on the basis of the values observed in the analysis of the past performance of the originator's loan portfolio. ICRA has also considered the credit quality experience of other established players in the mortgage business.

The resulting collections from the pool – after incorporating the impact of losses and prepayments as above – are accounted for in ICRA's cash flow model, in accordance with the cash flow waterfall of the transaction. Various possible scenarios are simulated and the incidences of default to the investor as well as the extent of losses are measured. These are then compared with ICRA's internal benchmarks to arrive at the assigned rating.

Upon modelling the cash flows and after considering the various above-mentioned factors, ICRA estimates the shortfall in the pool principal collection within the pool's tenure at 4.75-5.75%, with certain variability around it. The prepayment rate in the pool is assumed to be 6.0-20.0% p.a. (with a mean of 16.0%).

Liquidity position: Strong

The cash collections and the credit collateral available in the transaction are expected to be comfortable to meet the Series A1 PTC investor payouts. Assuming a monthly collection efficiency of even 50% in the underlying pool of contracts in a stress scenario, the recommended credit collateral would cover the shortfalls in the investor payouts for a period of 12 months.

Rating sensitivities

Positive factors – The sustained strong collection performance of the underlying pool (monthly collection efficiency >95%), leading to lower-than-expected delinquency levels and lower CE utilisation levels, 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 CE utilisation levels, would result in a rating downgrade.

Analytical approach

The rating action is based on the trustee confirming compliance with the terms of the transaction and the executed transaction documents being in line with the terms initially shared with ICRA

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

Originator profile

Unity SFB is the 12th small finance bank (SFB) in India, promoted by the consortium of Centrum Group and Resilient Innovations Private Limited (RIPL or BharatPe, a fintech company). The Reserve Bank of India (RBI) granted in-principle approval to Centrum Financial Services Limited (CFSL), to set up an SFB under the general guidelines for the on-tap licensing of SFBs in the private sector, as a part of the revival/reconstruction of PMC Bank in June 2021. The licence to set up the SFB was issued in October 2021.

BharatPe acquired a 49% stake in Unity SFB (for Rs. 745 crore) while CFSL holds 51%. Further, as a part of this transaction, the entire business (assets and liabilities) of CFSL and Centrum MicroCredit Limited (CML) was transferred to Unity SFB via a slump sale. CFSL serves as the holding company of Unity SFB with no other operations. Currently, Unity SFB primarily has the already existing small and medium-sized enterprise/micro, small and medium enterprise/supply chain/microfinance asset base of CFSL and CML. Unity SFB commenced active operations from November 1, 2021 with an upfront equity base of Rs. 1,105 crore. As the second leg of this transaction, PMC Bank was amalgamated with Unity SFB in accordance with the RBI's scheme for the recovery/resolution for the same. This was completed on January 24, 2022.

Key financial indicators (audited)

Unity SFB	Nov 1, FY2021	FY2022	FY2023
Total income	NA	154	803
Operating Profit	NA	17	148
Profit after tax	NA	(150)	35
Loan assets	1,264	2,419	4,468
Total assets	2,477	10,811	8,761
Gross NPA*	NA	3.37%	3.17%
Net NPA*	NA	8.14%	0.34%
CRAR	NA	63.71%	49.40%

** As on Mar 31, 2023, gross and net non-performing advances (NPAs) were 3.17% and 0.36%, respectively, excluding legacy NPAs of erstwhile PMC Bank*
Source: Unity SFB, ICRA Research; All ratios as per ICRA's calculations; NA – Not available
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 (FY2024)					Chronology of Rating History for the Past 3 Years		
		Instrument	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024		Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					Sep 25, 2023	July 18, 2023	-	-	-
1	**Marathon**	Series A1 PTC	81.10	78.62	**[ICRA]AA-(SO)**	**Provisional [ICRA]AA-(SO)**	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Series A1 PTC	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: Click Here

Annexure I: Instrument details

Trust Name	Instrument	Date of Issuance / Sanction	Coupon Rate**	Maturity Date*	Amount Rated (Rs. crore)	Current Rating
Marathon	Series A1 PTC	July 2023	8.75%	November 2037	78.62	[ICRA]AA-(SO)

*** Floating, linked to RBI Policy Repo Rate; *Scheduled 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

Anubhav Agrawal
+91 22 6114 3439
anubhav.agrawal@icraindia.com

Rushabh Gohel
+91 22 6114 3420
rushabh.gohel@icraindia.com

Priya Gounder
+91 22 6114 3454
priya.gounder@icraindia.com

RELATIONSHIP CONTACT

L Shivakumar
+91 22 6114 3406
shivakumar@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