September 29, 2023

SBFC Finance Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term loan	3,500.00	3,500.00	[ICRA]A+ (Stable); reaffirmed
Non-convertible debentures	100.00	100.00	[ICRA]A+ (Stable); reaffirmed
Total	**3,600.00**	**3,600.00**	

**Instrument details are provided in Annexure I*

Rationale

The rating for SBFC Finance Limited (SBFC) factors in its good capitalisation profile, supported by the capital raise of Rs. 750 crore in H1 FY2024. With this improved capital base, the company is well placed to grow as per its business plans while maintaining prudent leverage levels. The rating also favourably factors in the SBFC's improving profitability metrics aided by the increasing share of the relatively higher-yielding lower-ticket small and medium enterprise (SME) loans in the overall portfolio mix. Also, with the entire loan book being at floating rates of interest, the company has been able to pass on the rate hikes to the end borrowers, thereby supporting its margins.

The rating also factors in the adequate liquidity profile and the fairly diversified borrowing profile, which is commensurate with the current scale of operations. The rating is, however, constrained by the relatively lower seasoning of the loan book as a large part of the current book was originated in the past two years compared with the asset tenure of up to 15 years. This exposes the company to volatility in the asset quality indicators as the portfolio seasons. Portfolio vulnerability is further augmented by the target borrower profile, which is more susceptible to economic shocks, given the lower income buffers. In this regard, the secured and granular nature of the loans provides comfort.

While the early delinquencies could remain volatile for the company, the ultimate loss given default is expected to remain limited, given the secured (largely backed by self-occupied residential property comprising ~83% of the loan book portfolio) nature of the loans. In the recent past, SBFC has been able to control its asset quality despite the tough macroeconomic environment. Its asset quality improved with a decline in the gross stage 3 (GS3) to 2.5% of gross advances as on June 30, 2023 from 3.4% as on March 31, 2021. This was driven by the improvement in the collection efficiency as well as some write-offs and the sale of impaired assets to an asset reconstruction company (ARC) in FY2022 and FY2023.

The Stable outlook factors in ICRA's expectation that SBFC will continue improving its scale while keeping its leverage under control.

Key rating drivers and their description

Credit strengths

Good capitalisation supported by recent capital raise – With SBFC concluding its initial public offering (IPO) in H1 FY2024, its tangible net worth increased to ~Rs. 2,357 crore as on August 31, 2023, leading to a lower gearing of 1.5x. ICRA expects that SBFC would be able to leverage this capital and grow as per its business plans while maintaining prudent leverage of 3-4x over the medium term.

Improving profitability metrics; enhanced operating efficiency key, going forward – The average yields on SBFC's portfolio improved following the change in the mix in favour of the relatively higher-yielding small and medium-sized enterprise (SME) and gold loans. Although the cost of funds increased with the rise in systemic interest rates, SBFC has been able to pass on the hike as the entire loan book is at floating rates of interest. Consequently, the net interest margin (NIM) improved to 7.2%[#] of average managed assets in FY2023 and 7.5%[#] in Q1 FY2024. During this period, the operating expenses remained stable at 4.2%[#] of average managed assets as the company continued to invest in expansion while credit costs remained range-bound at 0.5-0.6%[#]. The improvement in the margins led to an increase in the return on managed assets (RoMA) to 2.7%[#] in FY2023 and 2.9%[#] in Q1 FY2024 from 1.4%[#] in FY2022. Going forward, the margins are expected to remain stable and the operating efficiency is expected to improve with the increase in the scale, leading to a further improvement in the profitability, provided the company is able to maintain control on fresh slippages.

Secured and retail nature of exposures – As of June 2023, the secured loan book comprised ~97% of the overall loan book, including MSME-loan against property (LAP) of ~79% and loan against gold jewellery (LAG; ~18%). The overall assets under management (AUM) accounted for ~89% (Rs. 4,767 crore) of the on-book portfolio and ~11% (Rs. 560 crore) of the off-book portfolio originating from the co-origination partnership with ICICI Bank as on June 30, 2023. SBFC's average ticket size declined to Rs. 9.7 lakh in Q1 FY2024 from Rs. 10 lakh in FY2023, reflecting a retail loan book. The share of loans with a ticket size of Rs. 25 lakh and below in the micro enterprise (ME) and SME portfolio increased significantly to 91% as on June 30, 2023 from 61% as on March 31, 2020. The company plans to maintain the share of the less-than-Rs. 25-lakh segment at more than 90% of the ME AUM in the near term, given its relatively better delinquency performance compared to higher ticket size loans. Going forward, the share of LAP and LAG is expected to be maintained at 80% and 20%, respectively, and the unsecured loan book would be completely run down.

Credit challenges

Moderate asset quality; portfolio yet to season, given the high pace of growth – SBFC's asset quality improved in FY2023 and Q1 FY2024 with the reported gross stage 3 declining to 2.5% as on June 30, 2023 from the high of 3.4% as on March 31, 2021. ICRA notes that the improvement was driven by the higher collection efficiency (97% on standard pool in Q1 FY2024) and controlled slippages. Further, the company reported a restructured loan book of Rs. 88.1 crore or 1.8% of advances as on June 30, 2023. ICRA notes that a significant proportion of the LAP book was originated in the last two years and is yet to season compared with the contractual tenure of ~15 years. Thus, there could be some build-up of delinquencies as the loan book seasons. In this regard, the secured and granular nature of loans provides comfort. Overall the company's ability to maintain the asset quality indicators, while growing as per plans, will remain a monitorable.

Portfolio vulnerability remains high, given the target borrower profile – SBFC predominantly provides small-to-medium-sized ticket loans to self-employed borrowers. Considering the borrowers' business and income profiles, their credit profiles are expected to be modest and vulnerable to income shocks induced by events such as the Covid-19 pandemic, the ongoing inflation and the increase in interest rates.

Environmental and social risks

While non-banking financial companies (NBFCs) like SBFC do not face material physical climate risks, they are exposed to environmental risks indirectly through their portfolio of assets. If the entities or businesses to which banks and financial institutions have an exposure face business disruption because of physical climate adversities or if such businesses face climate transition risks because of technological, regulatory or customer behaviour changes, the same could translate into credit risks for financial institutions. With regard to social risks, data security and customer privacy are among the key sources of vulnerability for financial institutions as material lapses could be detrimental to their reputation and invite regulatory censure.

[#] *All ratios as per ICRA's calculations*

As the majority of SBFC's services are digitally driven with high utilisation of information technology, it faces the risk of data breaches, cyberattacks and other operational risks, which could affect customer data. However, SBFC has faced no such instances in the past, which indicates that its risk management and processes are adequate. Further, the company's focus is towards providing access to finance to underserved customers in underbanked regions with female borrowers comprising 90.4% of the customer segment. It conducts several corporate social responsibility (CSR) activities in the fields of skill development, education and building livelihood for the underprivileged sections of society. Moreover, SBFC has started the assessment of environmental, social and governance (ESG) risks within the enterprise with the inception of ESG audit at its premises.

Liquidity position: Adequate

The company's liquidity profile is adequate. As on June 30, 2023, it had Rs. 645 crore of cash and liquid investments with positive cumulative mismatches across all buckets. Liquid investments are in mutual funds, Government securities and fixed deposits. Further, SBFC had undrawn bank lines of Rs. 40 crore as on March 31, 2023 and Rs. 100 crore as on June 30, 2023. Additionally, it has a diversified resource profile with the majority of the funding from public and private sector banks (~80% as on June 30, 2023) while securitisation and other financial institutions account for the balance.

Rating sensitivities

Positive factors – ICRA could upgrade the rating if the company shows a track record of profitable growth with a return on assets of more than 3.5% on a sustained basis.

Negative factors – Pressure on SBFC's rating could arise if there is a continued deterioration in the asset quality, with the 90+ days past due (dpd) increasing beyond 4.0% (on loan book), or if the gearing crosses 4 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA's Credit Rating Methodology for Non-banking Finance Companies
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

SBFC Finance Limited (SBFC) is a non-banking financial company that provides loan against property, and gold loans. Backed by the Clermont Group and the Arpwood Group, the company commenced operations in September 2017 after acquiring the performing loans in Karvy Financial Services Limited's (KFSL) retail portfolio. Following the acquisition, SBFC focussed on building adequate systems and processes and on the onboarding of experienced professionals in the management team before rebooting the lending business. It leverages technology and analytics to provide customers with easy access to credit and to assess their credit behaviour through their digital footprint.

SBFC reported a profit after tax (PAT) of Rs. 47 crore on total assets of Rs. 6,116 crore in Q1 FY2024 compared to Rs. 32.1 crore and Rs. 4,661 crore, respectively, in Q1 FY2023. In FY2023, it reported a PAT of Rs. 149.8 crore on total assets of Rs. 5,746 crore compared to Rs. 64.5 crore and Rs. 4,515 crore, respectively, in FY2022. As on June 30, 2023, the total AUM stood at Rs. 5,327 crore, consisting ~89% (Rs. 4,767 crore) of the on-book portfolio and ~11% (Rs. 560 crore) of the off-book portfolio as on June 30, 2023.

Key financial indicators (audited)

SBFC Finance Limited (Consolidated)	FY2021	FY2022	FY2023	Q1 FY2024
Total income	511	533	740	230
Profit after tax	85	64	150	47
Net worth	1,205	1,287	1,727	1,927
Loan book (Net)	2,107	2,982	4,415	4,713
Total assets	4,266	4,515	5,746	6,116
Return on managed assets	2.0%	1.4%	2.7%	2.9%
Return on net worth	7.7%	5.2%	9.9%	10.3%
Gross gearing (reported; times)	2.3	2.4	2.3	2.0
Gross stage 3 (Ind AS)	3.4%	2.9%	2.6%	2.5%
Net stage 3 (Ind AS)	2.2%	1.8%	1.6%	1.6%
Solvency (Net stage 3/Adjusted net worth)	4.4%	5.4%	4.8%	4.4%
CRAR	26.3%	26.2%	31.9%	33.6%

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Current Rating (FY2024)			Chronology of Rating History for the Past 3 Years		
			Amount Rated (Rs. crore)	Amount Outstanding as of Aug 31, 2023 (Rs. crore)	Date & Rating in FY2024 Sep-29-23	Date & Rating in FY2023 Oct-03-22	Date & Rating in FY2022 Oct-08-21	Date & Rating in FY2021 Oct-16-20
1	**Term loan**	Long term	3,500.00	3,500.00	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**	**[ICRA]A (Positive)**	**[ICRA]A (Stable)**
2	**Non-convertible debenture programme**	Long term	100	100	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**	**[ICRA]A (Positive)**	**[ICRA]A (Stable)**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term loan programme	Simple
Non-convertible debenture programme	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 as at September 25, 2023

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	TL	Jan-28-2023	NA	Feb-03-2027	30.63	[ICRA]A+ (Stable)
-	TL	Mar-30-2022	NA	Apr-03-2025	23.33	[ICRA]A+ (Stable)
-	TL	Jun-21-2023	NA	Jun-21-2027	100.00	[ICRA]A+ (Stable)
-	TL	Jan-04-2021	NA	Jan-04-2026	13.16	[ICRA]A+ (Stable)
-	TL	Jan-04-2021	NA	Jul-04-2024	1.54	[ICRA]A+ (Stable)
-	TL	Dec-31-2021	NA	Dec-31-2025	16.49	[ICRA]A+ (Stable)
-	TL	Jan-31-2022	NA	Dec-31-2025	16.49	[ICRA]A+ (Stable)
-	TL	Mar-29-2022	NA	Mar-31-2032	44.81	[ICRA]A+ (Stable)
-	TL	Sep-01-2022	NA	Aug-31-2026	39.99	[ICRA]A+ (Stable)
-	TL	Dec-30-2022	NA	Dec-30-2026	46.67	[ICRA]A+ (Stable)
-	TL	Mar-29-2023	NA	Mar-31-2027	50.00	[ICRA]A+ (Stable)
-	TL	Jan-25-2022	NA	Jan-25-2025	12.12	[ICRA]A+ (Stable)
-	TL	Jan-31-2022	NA	Jan-25-2025	12.12	[ICRA]A+ (Stable)
-	TL	Sep-02-2021	NA	Sep-30-2025	12.50	[ICRA]A+ (Stable)
-	TL	Mar-31-2022	NA	Mar-31-2026	17.17	[ICRA]A+ (Stable)
-	TL	Aug-02-2021	NA	Aug-02-2025	26.67	[ICRA]A+ (Stable)
-	TL	Sep-19-2022	NA	Sep-19-2026	80.00	[ICRA]A+ (Stable)
-	TL	Jun-30-2023	NA	Jun-30-2026	150.00	[ICRA]A+ (Stable)
-	TL	Mar-22-2021	NA	Mar-22-2024	9.09	[ICRA]A+ (Stable)
-	TL	Jul-01-2022	NA	Jul-01-2025	33.33	[ICRA]A+ (Stable)
-	TL	Dec-31-2020	NA	Dec-31-2023	5.00	[ICRA]A+ (Stable)
-	TL	Feb-10-2022	NA	Feb-10-2025	150.00	[ICRA]A+ (Stable)
-	TL	May-22-2023	NA	May-22-2026	100.00	[ICRA]A+ (Stable)
-	TL	Mar-19-2021	NA	Mar-19-2024	10.00	[ICRA]A+ (Stable)
-	TL	Mar-08-2022	NA	Mar-08-2025	35.00	[ICRA]A+ (Stable)
-	TL	Mar-31-2023	NA	Mar-31-2026	100.00	[ICRA]A+ (Stable)
-	TL	Jun-26-2023	NA	Jun-26-2026	40.00	[ICRA]A+ (Stable)
-	TL	Dec-31-2021	NA	Dec-31-2024	13.64	[ICRA]A+ (Stable)
-	TL	Jan-12-2021	NA	Jan-12-2024	16.67	[ICRA]A+ (Stable)
-	TL	Mar-31-2022	NA	Mar-30-2025	29.17	[ICRA]A+ (Stable)
-	TL	Jun-21-2022	NA	Jun-21-2025	29.17	[ICRA]A+ (Stable)
-	TL	Nov-30-2022	NA	Nov-30-2026	40.63	[ICRA]A+ (Stable)
-	TL	Mar-31-2023	NA	Mar-31-2026	45.83	[ICRA]A+ (Stable)
-	TL	Nov-11-2022	NA	May-11-2025	52.50	[ICRA]A+ (Stable)
-	TL	Dec-20-2022	NA	Jun-20-2025	17.50	[ICRA]A+ (Stable)
-	TL	Jun-12-2019	NA	Jun-12-2027	1273.45	[ICRA]A+ (Stable)
-	TL	Apr-29-2023	NA	Oct-31-2025	45.00	[ICRA]A+ (Stable)

-	**TL**	Dec-31-2021	NA	Nov-30-2024	11.36	[ICRA]A+ (Stable)
-	**TL**	Feb-09-2022	NA	Nov-30-2024	11.36	[ICRA]A+ (Stable)
-	**TL**	Sep-26-2022	NA	Sep-26-2026	80.00	[ICRA]A+ (Stable)
-	**TL**	Aug-24-2023	NA	Aug-24-2027	5.00	[ICRA]A+ (Stable)
NA	**Unallocated**	NA	NA	NA	652.61	[ICRA]A+ (Stable)
INE423Y07062	**Non-convertible debentures**	Aug-21	NA	Aug-24	43.00	[ICRA]A+ (Stable)
-	**Non-convertible debentures***	-	-	-	57.00	[ICRA]A+ (Stable)

*Source: Company; *Proposed*

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis

Not Applicable

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