

January 08, 2024

Aavas Financiers Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term bank lines – NHB refinance	2,765.60	3,248.91	[ICRA]AA (Stable); reaffirmed/assigned
Long-term bank lines – Term loan	265.40	134.09	[ICRA]AA (Stable); reaffirmed
Long-term bank lines – Cash credit	59.00	15.00	[ICRA]AA (Stable); reaffirmed
Non-convertible debenture programme	600.00	600.00	[ICRA]AA (Stable); reaffirmed
Commercial paper	50.00	50.00	[ICRA]A1+; reaffirmed
Total	3,740	4,048	

*Instrument details are provided in Annexure I

Rationale

The ratings factor in Aavas Financiers Limited's (Aavas) track record in the affordable housing finance space. The company's assets under management (AUM) increased at a compound annual growth rate (CAGR) of 28% during FY2018-FY2023 and stood at Rs. 15,319 crore as on September 30, 2023 (Rs. 14,167 crore as on March 31, 2023). ICRA favourably notes that Aavas' capitalisation level remains healthy along with a strong liquidity position and a diversified funding mix. Although the managed gearing¹ is expected to increase from 4.0x as on September 30, 2023 with incremental business being funded by fresh borrowings, ICRA expects the company to maintain a prudent capitalisation profile over the medium term. The ratings also factor in Aavas' satisfactory profitability trajectory, supported by healthy net interest margins (NIMs) and controlled credit costs.

The ratings also consider the company's portfolio vulnerability, given its target borrower profile. Aavas' operations remain focussed on low-and-middle-income self-employed borrowers (60% of the AUM as on September 30, 2023), who are relatively more vulnerable to economic cycles and have limited income buffers to absorb income shocks. Thus, delinquencies in the softer buckets could remain volatile.

ICRA, however, draws comfort from Aavas' good underwriting systems and collection infrastructure, which is reflected in the relatively low one days past due (1+ dpd) of 3.6% as on September 30, 2023 (3.3% as on March 31, 2023). Further, losses on default are expected to be limited, considering the secured nature of the portfolio with moderate loan-to-value (LTV) ratios and the low-ticket size. Moreover, the assets are largely self-occupied residential properties, thereby supporting asset quality. The gross stage 3 assets remained stable at 1.0% as on September 30, 2023 (0.9% as on March 31, 2023). The ratings also factor in the limited portfolio seasoning, given the high portfolio growth, and the geographical concentration of the portfolio, though the same is improving. While the company has expanded its geographical footprint, dependence on its home state of Rajasthan remains high, albeit declining.

The Stable outlook on the long-term rating reflects ICRA's expectation that the company will continue to grow its business volumes while retaining the healthy operational and financial metrics trajectory.

¹ Managed gearing = (Total borrowings + Off-book portfolio)/Net worth

Key rating drivers and their description

Credit strengths

Healthy capitalisation – Aavas is well capitalised with a managed gearing of 4.0x and a capital-to-risk weighted assets ratio (CRAR) of 48.2% as on September 30, 2023 (3.9x and 47.0%, respectively, as on March 31, 2023). While the leverage is expected to increase from the current level with fresh borrowings funding the incremental business, ICRA expects the company to maintain a prudent capitalisation profile with a peak managed gearing of 5-6x over the medium term. In ICRA's opinion, a prudent capitalisation level, the secured nature of the portfolio backed largely by self-occupied residential properties, and low ticket sizes would be the key mitigants against the inherent risks associated with the company's portfolio given the target borrower profile. Considering the calibrated growth plans, low leverage, and good internal capital generation, ICRA does not expect Aavas to need external capital infusions to meet its growth target. Also, the comfortable capitalisation level provides a buffer for absorbing unforeseen asset-side shocks, if any.

Track record of good asset quality, notwithstanding intermittent weakening during the pandemic – The gross and net stage 3 stood comfortable at 1.0% and 0.8%, respectively, as on September 30, 2023 (0.9% and 0.7%, respectively, as on March 31, 2023) compared to 1.0% and 0.7%, respectively, as on March 31, 2021, even with the implementation of the Reserve Bank of India's (RBI) notification on Income Recognition, Asset Classification, and Provisioning (IRACP) norms. Moreover, the gross stage 3, on a 1-year lagged basis, stood at 1.1% as on September 30, 2023 (1.2% as on March 31, 2023). ICRA, however, notes that the company's portfolio remains vulnerable, given its target borrower profile. Hence, delinquencies in the softer buckets could remain volatile. Although the delinquencies in the softer buckets had come under pressure during the Covid-19 pandemic, Aavas demonstrated good underwriting systems and collection infrastructure, which helped bring down the 1+ dpd to 3.6% as on September 30, 2023 (3.3% as on March 31, 2023) from the elevated level of 12.7% as on June 30, 2021. As on September 30, 2023, the entire restructured book was classified under stage 2 and was negligible at 0.5% of the AUM (0.8% as on March 31, 2023) with a provision cover of 14%.

ICRA notes that the overall provision cover against the loan book stood at 0.6% as on September 30, 2023 (0.6% as on March 31, 2023). Losses, in case of default, are expected to be limited, as most of the properties are self-occupied, the company is covered under the SARFAESI Act, and the nature of lending is secured with moderate LTV ratio at origination.

Satisfactory profitability trajectory – Aavas' blended lending yield moderated to 12.5% in FY2023 from 12.7%. The cost of funds remained stable at 6.6% in FY2023 because of the company's ability to raise funds at competitive rates, including refinance from National Housing Bank (NHB). Consequently, the lending spread moderated marginally to 5.9% in FY2023 from 6.1% in FY2022 but remained commensurate with the underlying portfolio risk. The NIMs remained stable at 6.4% in FY2023 (and in line with historical NIMs of 6-7%), supported by securitisation-related income. While the operating expenses increased to 3.1% in FY2023 from 2.9% in FY2022 because of investments in digital upscaling, the credit cost remained low at 0.1% in FY2023 compared to 0.2% in FY2022. Overall, the profitability indicators remained stable with a return on managed assets (RoMA)² and a return on net worth (RoNW) of 2.9% and 14.2%, respectively, in FY2023 compared to 2.9% and 13.7%, respectively, in FY2022.

While Aavas was able to pass on the rate hike to its customers in H1 FY2024, resulting in a rise in the blended yields to 13.0%, the cost of funds increased sharply to 7.4% because of the higher systemic interest rates. This led to further moderation in the lending spreads and NIMs to 5.6% and 6.2%, respectively, in H1 FY2024 despite stable operating expenses and credit costs of 3.1% and 0.1%, respectively. This resulted in a slight moderation in the profitability with RoMA³ and RoNW of 2.7% and 13.6%, respectively, in H1 FY2024. Going forward, the NIMs are likely to be under some pressure on account of increase in gearing. The company's ability to grow the loan book profitably while maintaining the credit quality will be a key monitorable.

² Return on assets (RoA) stood at 3.5% in FY2023 compared to 3.6% in FY2022.

³ RoA stood at 3.2% in H1 FY2024.

Strong liquidity profile with diversified funding mix – Aavas’ liquidity profile is strong with sizeable on-balance sheet liquidity in the form of cash and liquid investments and long-tenor liabilities raised by it with no dependence on short-term commercial paper funding since inception. Further, the company’s financial flexibility is good, given its relationships with all the leading banks of the country. It also has funding support from various multilateral agencies like International Finance Corporation (IFC), British International Investment (BII, Formerly known as Commonwealth Development Corporation) and Asian Development Bank (ADB).

Aavas’ funding profile remains diversified with sources including borrowings from banks and other financial institutions (FIs; 46%), non-convertible debentures (NCDs; 11%), NHB refinance (18%), securitisation and assignment (24%; significant proportion of the portfolio qualifies for priority sector lending, thereby providing an additional funding source) and others (including lease liability and interest accrued but not due; 1%). The company’s incremental borrowing cost has increased due to the rise in systemic interest rates. It raised Rs. 3,076 crore in H1 FY2024 (Rs. 4,763 crore in FY2023) at a weighted average rate of 8.2% (7.3% in FY2023) for a weighted average maturity of 135 months (128 months in FY2023).

Demonstrated ability to grow retail business volumes – Aavas’ portfolio has grown over the past five years, driven by the increase in the customer base and its foray into new regions and deeper penetration in existing geographies, thereby leading to a CAGR of 28% during FY2018-FY2023. The AUM increased to Rs. 14,167 crore as on March 31, 2023 from Rs. 4,073 crore as on March 31, 2017. The AUM growth moderated to 16% on an annualised basis in H1 FY2024 to Rs. 15,319 crore as on September 30, 2023 because of the calibrated approach adopted by the company. As far as the portfolio mix is concerned, the share of individual home loans remained high at about 70% as on September 30, 2023 with other mortgage loans accounting for the balance. The share of the salaried customer segment stood at 40% as on September 30, 2023.

Credit challenges

Relatively high, albeit improving, geographical concentration – Aavas commenced lending operations in March 2012 with primary focus on the home state of Rajasthan. While it subsequently expanded its geographical footprint to 13 states/Union Territories (UTs), its dependence on Rajasthan remains relatively high at 36% as on September 30, 2023, albeit lower than 48% as on March 31, 2017. While the share of Rajasthan in the portfolio is not expected to reduce significantly in the medium term, the overall geographical diversity is likely to improve with the company gradually expanding and opening new branches in other states. Aavas had 350 branches as on September 30, 2023 spread across Rajasthan, Maharashtra, Gujarat, Madhya Pradesh, Delhi, Uttar Pradesh, Punjab, Haryana, Uttarakhand, Chhattisgarh, Himachal Pradesh, Odisha, and Karnataka.

Exposure to relatively vulnerable borrower profile – Aavas’ operations remain focussed on low-and-middle-income self-employed borrowers (60% of the AUM as on September 30, 2023), who are relatively more vulnerable to economic cycles and have limited income buffers to absorb income shocks. Hence, delinquencies in the softer buckets could remain volatile. Nevertheless, the losses on default are expected to be limited considering the secured nature of the portfolio, the moderate LTV (~62% of the portfolio had an LTV of less than 60% as on September 30, 2023) and the low ticket size. Moreover, the assets are largely self-occupied residential properties. Also, ICRA draws comfort from Aavas’ demonstrated ability to control the asset quality and credit cost, which reflects positively on its underwriting norms and collection infrastructure.

Environmental and social risks

While financial institutions like Aavas 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 these institutions have an exposure, face business disruption because of physical climate adversities or if they face climate transition risks because of technological, regulatory, or customer behaviour changes, the same could translate into credit risks for financial institutions. However, such risk is not material for Aavas as it benefits from a granular portfolio profile.

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. Aavas has not faced such lapses over the years, which highlights its sensitivity to such risks. Aavas is seen to be operating responsibly in terms of its business practices with no instances of fines being imposed by regulatory authorities.

Liquidity position: Strong

Aavas' liquidity profile is strong with sizeable on-balance sheet liquidity in the form of cash and liquid investments of about Rs. 1,989 crore as on September 30, 2023 (equivalent to ~18% of its on-balance sheet borrowings). This is sufficient compared to the total debt-servicing burden (principal and interest) of about Rs. 2,791 crore over the next one year, as per the ALM profile as on September 30, 2023. The company is also maintaining off-balance sheet liquidity in the form of undrawn cash credit limits of Rs. 110 crore and documented but unavailed sanctions of Rs. 1,000 crore from NHB and documented but unavailed sanctions of Rs. 1,905 crore from other banks. Furthermore, while the company is likely to carry relatively lower on-balance sheet liquidity, it is noted that the ALM remains well matched during the normal course of business, aided by the long-tenor liabilities raised by it with no dependence on short-term commercial paper funding since inception. As on September 30, 2023, Aavas' ALM reflected scheduled inflows (principal and interest) of Rs. 3,275 crore from performing advances during the next 12 months.

Rating sensitivities

Positive factors – A significant increase in the scale, while maintaining a healthy financial profile and good asset quality over the medium to long term and reducing the geographical concentration, would be a credit positive. Retaining the diversified funding profile with minimal asset-liability mismatches in the near-term buckets, as the company expands its portfolio, would also be crucial for maintaining the credit profile.

Negative factors – Pressure on the ratings could arise in case of a significant deterioration in the earnings profile (RoMA of less than 2.5% on sustained basis) or a sustained weakening of the asset quality (90 dpd above 2.0%). Also, a deterioration in the capitalisation profile on a sustained basis or an adverse change in the asset-liability maturity profile will be a credit negative.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA's Credit Rating Methodology for Non-banking Finance Companies⁴
Parent/Group support	-
Consolidation/Standalone	Standalone

About the company

Aavas is a Jaipur (Rajasthan) headquartered housing finance company, which primarily provides housing loans in rural and semi-urban areas. It is present in 12 states and 1 UT, with a network of 350 branches and AUM of Rs. 15,319 crore as on September 30, 2023.

Aavas was incorporated as a subsidiary of Au Financiers (India) Limited {now Au Small Finance Bank Limited (AuSFB)} in February 2011, and it formally began its operations in March 2012. Later, in June 2016, AuSFB sold its stake in Aavas to private

⁴ For rating an NBFC, ICRA evaluates its business risk, ownership, management risk and financial risk, and uses this to assess the level and stability of the NBFC's future financial performance in likely scenarios, as required. The ratings are determined on a going concern basis rather than on a mere assessment of the assets and debt levels on a particular date

equity (PE) investors – Kedaara Capital and Partners Group – to meet the Reserve Bank of India’s (RBI) criteria for conversion to a small finance bank. Thereafter, Aavas launched an initial public offering (IPO) in FY2019 and its equity shares got listed on the stock exchanges on October 8, 2018. The total issue size was Rs. 1,734 crore, of which ~Rs. 360 crore was raised for business operations while the rest was utilised to pay off the existing shareholders. The company’s shareholding as on September 30, 2023: Kedaara Capital (24%), Partners Group (16%), the management team (2%), domestic institutional investors (DIIs; 13.5%), foreign institutional investor (FIIs; 35.5%) and others (around 9%).

Aavas reported a profit after tax (PAT) of Rs. 430 crore in FY2023 on a managed asset base⁵ Rs. 16,182 crore as on March 31, 2023 compared to a PAT of Rs. 357 crore in FY2022 on a managed asset base of Rs. 13,420 crore as on March 31, 2022. The company had a net worth of Rs. 3,270 crore and a CRAR of 47.0% as on March 31, 2023 compared to Rs. 2,809 crore and 51.9%, respectively, as on March 31, 2022. The gross and net stage 3 stood at 0.9% and 0.7%, respectively, as on March 31, 2023 compared to 1.0% and 0.8%, respectively, as on March 31, 2022.

Aavas reported a PAT of Rs. 231 crore in H1 FY2024 on a managed asset base Rs. 18,045 crore as on September 30, 2023. It had a net worth of Rs. 3,514 crore and a CRAR of 48.2% as on September 30, 2023. The gross and net stage 3 stood at 1.0% and 0.8%, respectively, as on September 30, 2023.

Key financial indicators

	FY2021	FY2022	FY2023	H1 FY2024
	Audited	Audited	Audited	Limited Review
Total income	1,105	1,306	1,610	964
PAT	289	357	430	231
Total managed assets	10,925	13,420	16,182	18,045
Return on average managed assets	2.9%	2.9%	2.9%	2.7%
Managed gearing (times)	3.5	3.7	3.9	4.0
Gross stage 3	1.0%	1.0%	0.9%	1.0%
CRAR	54.4%	51.9%	47.0%	48.2%

Source: Aavas’ financial results, ICRA Research; Note: Amount in Rs. crore; All figures and ratios are as per ICRA’s calculations/adjustments

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

⁵ Managed assets = Gross assets (including credit provisions on loans) + Off-book portfolio

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 (Rs. crore)^	Date and Rating	Date and Rating in FY2023			Date & Rating in FY2022			Date & Rating in FY2021		
					Jan 08, 2024	Feb 24, 2023	Sep 06, 2022	Aug 22, 2022	Jun 29, 2022	Dec 08, 2021		Dec 24, 2020	Oct 30, 2020
1 CP	ST	50.0	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2 Fund-based NHB refinance	LT	3,248.91	2,656.80	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	-	-	-	-	-	-	-
3 Fund-based term loan	LT	134.09	134.09	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Positive)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
4 Fund-based cash credit	LT	15.00	15.00	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
5 NCD	LT	600.0	187.5	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)

Source: ICRA Research; Note: LT: Long term, ST: Short term; ^ As on November 30, 2023

Complexity level of the rated instruments

Instrument	Complexity Indicator
NCD programme	Simple
Commercial paper	Very Simple
Fund-based NHB refinance	Simple
Fund-based term loan	Simple
Fund-based cash credit	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 on November 30, 2023

ISIN	Instrument Name	Date of Issuance/ Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA^	Commercial paper	NA	NA	NA	50	[ICRA]A1+
INE216P07209	NCD	Dec-31-2020	Repo Rate Linked	Dec-31-2025	100	[ICRA]AA (Stable)
INE216P07233	NCD	Jul-20-2023	Repo Rate Linked	Jul-20-2028	150	[ICRA]AA (Stable)
NA^	NCD	NA	NA	NA	350	[ICRA]AA (Stable)
NA	Cash credit 1	Aug-04-2014	NA	NA	10.0	[ICRA]AA (Stable)
NA	Cash credit 2	Sep-05-2014	NA	NA	5.0	[ICRA]AA (Stable)
NA	Term loan 1	Dec-13-2016	NA	Jan-07-2025	3.71	[ICRA]AA (Stable)
NA	Term loan 2	Nov-03-2015	NA	Jan-31-2026	4.03	[ICRA]AA (Stable)
NA	Term loan 3	Sep-27-2018	NA	Nov-01-2028	21.28	[ICRA]AA (Stable)
NA	Term loan 4	Sep-17-2015	NA	Jul-30-2025	0.30	[ICRA]AA (Stable)
NA	Term loan 5	Jul-04-2017	NA	Jun-04-2027	15.62	[ICRA]AA (Stable)
NA	Term loan 6	Jul-31-2018	NA	Jun-30-2028	6.15	[ICRA]AA (Stable)
NA	Term loan 7	Jul-31-2018	NA	Sep-30-2028	39.55	[ICRA]AA (Stable)
NA	Term loan 8	Aug-03-2017	NA	Sep-03-2027	13.55	[ICRA]AA (Stable)
NA	Term loan 9	Sep-24-2015	NA	Feb-28-2026	0.33	[ICRA]AA (Stable)
NA	Term loan 10	Sep-25-2017	NA	Mar-01-2028	29.57	[ICRA]AA (Stable)
NA	NHB refinance	2015-2023	NA	NA	2,656.80	[ICRA]AA (Stable)
NA^	NHB refinance	NA	NA	NA	592.11	[ICRA]AA (Stable)

Source: Aavas, ICRA Research; ^Proposed/yet to be placed; Note: Rate of interest not available for term loans

[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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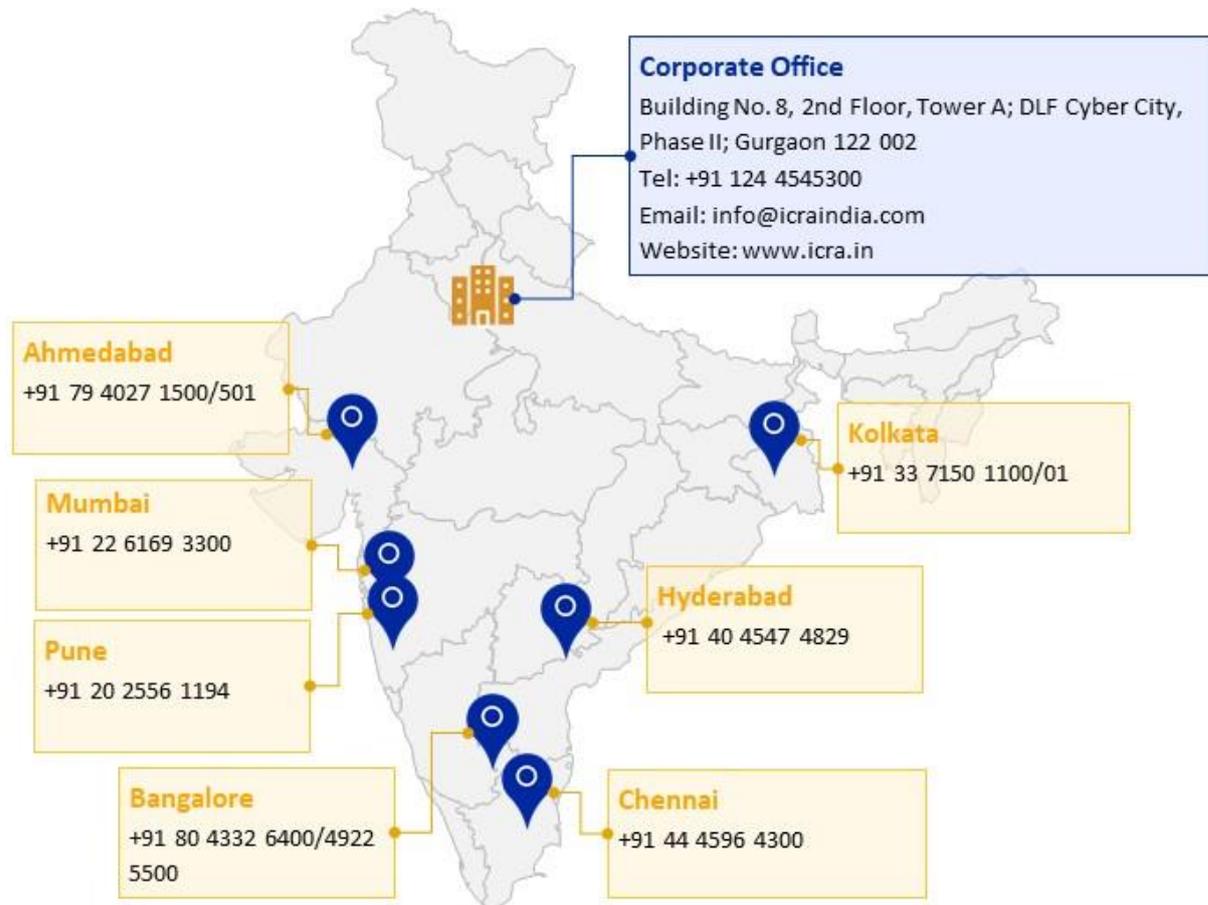
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