

January 15, 2024

## Spandana Sphoorty Financial Limited: Ratings reaffirmed; outlook revised to Positive

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund based – Term loan	2,105.00	2,105.00	[ICRA]A (Positive); reaffirmed and outlook revised to Positive from Stable
Non-convertible debentures	358.00	358.00	[ICRA]A (Positive); reaffirmed and outlook revised to Positive from Stable
Non-convertible debentures	21.50	0.00	[ICRA]A (Positive); reaffirmed, outlook revised to Positive from Stable and withdrawn
Market linked debentures	20.00	20.00	PP-MLD[ICRA]A (Positive); reaffirmed and outlook revised to Positive from Stable
Market linked debentures	100.00	0.00	PP-MLD[ICRA]A (Positive); reaffirmed, outlook revised to Positive from Stable and withdrawn
<b>Total</b>	<b>2,604.50</b>	<b>2,483.00</b>	

\*Instrument details are provided in Annexure I

### Rationale

The revision in the rating outlook factors in the steady improvement in Spandana Sphoorty Microfinance Limited's (SSFL) borrowing profile, characterised by a reduction in the marginal borrowing cost and the addition of new lenders. The company raised about Rs. 7,013 crore in 9M FY2024 (compared to about Rs. 5,775 crore in FY2023) from its existing as well as new lenders. The marginal cost of borrowing has reduced over the last four quarters, but is higher compared to some of the industry peers. Going forward, SSFL's ability to diversify its liability profile further and keep the borrowing rates under control would be crucial from a rating perspective.

ICRA takes notes of the steady improvement in SSFL's asset quality and earnings over the last few quarters. SSFL's gross stage 3 assets (standalone) improved to 1.3% as of September 2023 from 5.0% as of December 2022 (18.9% as of March 2022). On a consolidated basis, the gross stage 3 assets improved to 1.4% as of September 2023 from 15.0% as of March 2022. SSFL had undertaken significant loan write-offs of Rs. 886.1 crore in FY2023 (largely in Q1 FY2023) and sold Rs. 258.0 crore to an asset reconstruction company (ARC). This helped reduce its stressed exposures on account of the Covid-19 pandemic and the operational disruptions faced due to management changes in H2 FY2022. Write-offs remained low at Rs. 38.9 crore in H1 FY2024 as fresh loans originated in FY2023 have demonstrated good collections, contributing to the improved asset quality.

On a consolidated basis, SSFL's net profitability (return on average managed assets; RoMA) improved to 4.4% (annualised) in H1 FY2024 (from 0.1% in FY2023 and 0.8% in FY2022), supported by the moderation in credit costs (credit and provision costs stood at 0.8% (annualised) in H1 FY2024 compared to 5.5% in FY2023 and 5.3% in FY2022) and the improvement in the portfolio yields. The company had changed its lending rates in FY2023 following the revised regulatory framework for microfinance institutions (MFIs). The ratings also factor in SSFL's comfortable capitalisation profile with a capital adequacy ratio of 37.0% and a standalone managed gearing of 2.5x as of September 2023. The consolidated managed gearing also stood at 2.5x as of September 2023.

SSFL's consolidated assets under management (AUM) stood at Rs. 9,784 crore as of September 2023, catering to about 27 lakh borrowers through a network of 1,502 branches spread across 19 states. Its portfolio remains diversified with no state accounting for more than 20% of the portfolio. The ratings also consider the risks associated with the marginal borrower

profile, unsecured lending, business, and political risks along with the high pace of growth. SSFL's ability to manage such risks while expanding to new geographies would be crucial. ICRA takes note of the new management team and various initiatives for risk management, technology and operational improvements, which shall partly offset the impact of the above risks.

ICRA has reaffirmed the long-term ratings on the Rs. 21.50-crore non-convertible debenture (NCD) programme and the Rs. 100-crore market linked debenture (MLD) programme while revising the outlook to Positive from Stable and has simultaneously withdrawn the ratings as the instruments have been fully redeemed with no amount outstanding against the same. The ratings were withdrawn as per ICRA's policy on the withdrawal of credit ratings.

## Key rating drivers and their description

### Credit strengths

**Diversified geographical presence; expected to improve further with expansion in new states** – SSFL's consolidated AUM grew by 29.0% year-on-year (YoY) in FY2023 and 69% YoY in H1 FY2024 and stood at Rs. 9,784 crore as of September 2023. The company expects to reach a consolidated AUM of Rs. 15,000.0 crore by FY2025 (Rs. 28,000.0 crore by FY2028), which will be largely supported by borrower additions in new geographies and diversification into newer asset segments.

SSFL's portfolio remains fairly diversified with no state accounting for more than 20% of the portfolio. The concentration of the top 3 states in the company's portfolio (on a standalone basis) was 41.6% as on September 30, 2023 (50% as on March 31, 2021). As on September 30, 2023, its largest state, Odisha, accounted for 15.5% of the standalone portfolio, followed by Madhya Pradesh (15.4%), Karnataka (10.8%) and Andhra Pradesh (10.8%). The company has identified seven states for scaling up and diversifying its AUM, which would bring down its geographical concentration further.

**Improving asset quality and earnings** – SSFL's gross stage 3 assets (standalone) improved to 1.3% as of September 2023 and 1.9% as of March 2023 from 18.9% as of March 2022. This was driven by the significant write-off of Rs. 886.1 crore in FY2023. SSFL also sold Rs. 258.0 crore of its stressed portfolio to an ARC in FY2023. Incremental write-offs made by the company in H1 FY2024 remained lower at Rs. 38.9 crore. On a consolidated basis, the gross stage 3 assets improved to 1.4% as of September 2023 from 15.0% as of March 2022. ICRA takes note of the steady improvement in collections with the monthly collection efficiency (collections against only the current month's demand) at 97.5% as of September 2023 (90.7% as of September 2022 and 91.9% as of June 2022). As of September 2023, SSFL was carrying provisions of Rs. 195.2 crore, representing 2.2% of the overall AUM (stage 3 provisions stood at Rs. 75.6 crore; 70% of provision coverage ratio).

SSFL reported a consolidated profit after tax (PAT) of Rs. 244.6 crore, translating into a RoMA of 4.4% (annualised) as of September 2023 (Rs. 12.4 crore and 0.1%, respectively, as of March 2023). As the company had addressed the legacy stress on its loan portfolio in FY2023, its credit costs moderated to 0.8% (annualised) in H1 FY2024 from 5.5% in FY2023. Further, following the revised regulatory framework, SSFL increased its lending rate in July 2022 to 24.0% from 21.0% and is currently lending at 25.0%. Consequently, the net interest margin improved to 11.3% in H1 FY2024 from 9.5% in FY2023 and 9.2% in FY2022. ICRA expects SSFL's net profitability to remain at around 4% over the medium term, supported by the moderation in credit costs and the improvement in the interest margins.

**Comfortable capitalisation profile** – SSFL's capital adequacy ratio remains well above the regulatory requirement of 15% and the leverage has been comfortable, supported by regular equity infusions. On a consolidated basis, the managed gearing was comfortable at 2.5x as of September 2023 and 2.1x as of March 2023 (1.4x as of March 2022). SSFL's standalone managed gearing stood at 2.5x as of September 2023. Its capitalisation profile provides it with a comfortable runway for scaling up its operations over the medium term. Going forward, given the robust growth plans envisaged by the management, the gearing is expected to increase with incremental business being funded through fresh borrowings. However, ICRA expects SSFL to maintain its consolidated managed gearing below 4.5x over the next two years.

## Credit challenges

**Ability to strengthen funding profile further** – SSFL's borrowing profile has improved steadily in the last 3-4 quarters, characterised by a reduction in the marginal borrowing cost and the addition of new lenders. The company raised about Rs. 7,013 crore in 9M FY2024 (compared to about Rs. 5,775 crore in FY2023) from its existing as well as new lenders. The marginal cost of borrowing has reduced over the last four quarters and stood at 12.3% in Q2 FY2024 compared to 12.7% in Q3 FY2023. However, SSFL's cost of borrowing is higher compared to some of the industry peers. ICRA notes that the share of bank borrowings (as a percentage of the total consolidated borrowings) declined to 44.0% as of September 2023 from 68.0% as of March 2021 while its reliance on high-cost funding from non-banking financial companies (NBFCs), external commercial borrowings and other capital market sources has increased, with their combined share jumping to 56.0% as of September 2023 from 32.0% as of March 2021. As of September 2023, the company was in breach of some covenants on NCDs amounting to Rs. 264.9 crore. Going forward, it is critical for SSFL to strengthen its funding profile, secure funding at competitive rates and achieve the targeted AUM over the next two years.

**Risks associated with microfinance business** – The ratings factor in the risks associated with the marginal borrower profile, unsecured lending, business, and political risks, along with the challenges associated with a high pace of growth. SSFL's ability to manage such risks while expanding in new geographies would be crucial. The company's ability to onboard borrowers with a good credit history, recruit and retain employees and maintain a geographically diversified portfolio would be key for managing high growth rates. While credit bureau checks and the regulatory ceiling on the borrower's fixed obligation to income ratio reduce concerns on overleveraging, issues related to the policy of MFIs, regarding their underwriting practices, borrowers' income and leverage assessment remain. The revised guidelines for the microfinance industry are expected to provide the players, including SSFL, with better pricing ability in view of the underlying risks.

## Environmental and social risks

Given the service-oriented business of SSFL, its direct exposure to environmental risks as well as those emanating from regulations or policy changes is not material. While lending institutions can be exposed to environmental risks indirectly through their portfolio of assets, SSFL's exposure to environmentally sensitive segments remains moderate. However, most of its borrowers are in small businesses, with the majority engaged in essential commodity related activities, primarily dependent on local demand-supply forces. If such borrowers face livelihood disruptions because of physical climate adversities, the same could translate into credit risks for entities such as SSFL.

Regarding social risks, data security and customer privacy are among the key sources of vulnerability for lending institutions as material lapses could be detrimental to their reputation and could invite regulatory censure. In FY2022, SSFL had faced such a lapse following a dispute with its erstwhile promoter and information technology (IT) vendor, whereby it lost access to its old systems and servers, resulting in significant operational constraints. However, it was able to largely restore/rebuild the same, following the resolution of the dispute. Going forward, it would be critical for the company to maintain failsafe policies and processes to mitigate the occurrence of such instances. ICRA notes that SSFL has recently upgraded its loan management system software and is making further investments to create a stable infrastructure to minimise data breaches and safeguard stakeholder data.

## Liquidity position: Adequate

The company's unencumbered cash and liquid investment balance stood at Rs. 1,854.5 crore as on November 30, 2023. SSFL's total debt obligation during December 2023-February 2024 is Rs. 2,396.7 crore. The on-book liquidity is sufficient to cover approximately two months of debt repayment obligations. The monthly average collection over the next few months is expected to be about Rs. 600-650 crore, providing support to the liquidity profile.

As of September 2023, SSFL had lending relationships with 49 lenders including 27 NBFCs/financial institutions (FIs), 19 private sector banks/small finance banks, 2 public sector banks and 1 foreign private investor. Its funding profile (on a consolidated

basis) comprised borrowings from banks (44.0%), FIs/NBFCs (21.0%), development financial institutions (5%), NCDs and MLDs (28.0%) and external commercial borrowings (2.0%).

## Rating sensitivities

**Positive factors** – Improvement in funding profile, sustained asset quality and earnings profile with return on average managed assets (RoMA) of more than 3.0%, as the company scales up.

**Negative factors** – Pressure on the ratings or outlook could arise if the managed gearing exceeds 5x on a sustained basis or there is a weakening of the profitability (RoMA of less than 2%) on a sustained basis.

## Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Rating Methodology for Non-banking Finance Companies</a> <a href="#">Policy on Withdrawal of Credit Ratings</a>
Parent/Group support	Not applicable
Consolidation/Standalone	The ratings are based on SSFL's consolidated financial statements (Annexure II)

## About the company

Spandana Sphoorty Financial Limited (SSFL) was incorporated in 2003 as a non-banking financial company (NBFC) and it took over the microfinance operations of Spandana, a non-governmental organisation, which was started in 1998. The company was classified as an NBFC-microfinance institution (NBFC-MFI) in 2015. Following the microfinance crisis in Andhra Pradesh (AP), the company entered into a master restructuring agreement (MRA) as a part of the corporate debt restructuring (CDR) with its lenders in September 2011. It exited the CDR in April 2017 after an equity investment led by Kedaara Capital Investment Managers Limited (Kedaara Capital) and fresh funding from three banks. SSFL completed its initial public offering (IPO) in August 2019. The current leadership team is led by Mr. Shalabh Saxena (Managing Director & Chief Executive Officer) and Mr. Ashish Damani (President & Chief Financial Officer). The company has a 10-member board of directors, including 5 independent directors.

## Key financial indicators (audited)

Spandana Sphoorty Financial Limited (standalone)	FY2022	FY2023	H1 FY2024
Total income	1,350.8	1,355.8	1,105.1
Profit after tax	46.6	12.3	227.4
Total managed assets	7,985.5	9,933.3	11,862.1
Return on managed assets	0.5%	0.1%	4.2%
Managed gearing (times)	1.4	2.1	2.5
Gross stage 3 assets	18.9%	1.9%	1.3%
CRAR	50.7%	36.9%	37.0%

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

Spandana Sphoorty Financial Limited (consolidated)	FY2022	FY2023	H1 FY2024
<b>Total income</b>	1,479.9	1,438.3	1,154.9
<b>Profit after tax</b>	69.9	12.4	244.6
<b>Total managed assets</b>	8,214.2	10,159.5	12,229.9
<b>Return on managed assets</b>	0.8%	0.1%	4.4%
<b>Managed gearing (times)</b>	1.4	2.1	2.5
<b>Gross stage 3 assets</b>	15.0%	2.1%	1.4%
<b>CRAR</b>	NA	36.3%	36.6%

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	Type	Current Rating (FY2024)		Chronology of Rating History for the Past 3 Years									
			Amount Rated (Rs. crore)	Amount O/S (Rs. crore)	Date & Rating in FY2024		Date & Rating in FY2023			Date & Rating in FY2022	Date & Rating in FY2021			
					Jan-15-2024	Aug-18-2023	Mar-27-2023	Mar-01-2023	Sep-29-2022	Nov-10-2021	Nov-20-2020	Oct-12-2020	Jul-01-2020	Jun-19-2020
1	MLD	LT	20.00	20.00	PP-MLD[ICRA] A (Positive)	PP-MLD[ICRA] A (Stable)	PP-MLD[ICRA] A- (Positive)	PP-MLD[ICRA] A- (Positive)	PP-MLD[ICRA] A- (Stable)	PP-MLD[ICRA] A-&	PP-MLD[ICRA] A- (Stable)	PP-MLD[ICRA] A- (Stable)	-	-
2	MLD	LT	100.00	0.00	PP-MLD[ICRA] A (Positive); withdrawn	PP-MLD[ICRA] A (Stable)	PP-MLD[ICRA] A- (Positive)	PP-MLD[ICRA] A- (Positive)	PP-MLD[ICRA] A- (Stable)	PP-MLD[ICRA] A-&	PP-MLD[ICRA] A- (Stable)	PP-MLD[ICRA] A- (Stable)	-	-
3	NCD	LT	358.00	259.25*	[ICRA]A (Positive)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Positive)	[ICRA]A- (Stable)	[ICRA]A-&	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
4	NCD	LT	21.50	0.00	[ICRA]A (Positive); withdrawn	[ICRA]A (Stable); withdrawn	[ICRA]A- (Positive); Withdrawn	[ICRA]A- (Positive)	[ICRA]A-&	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
5	Term loan	LT	2,105.00	2,105.00	[ICRA]A (Positive)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Positive)	[ICRA]A- (Stable)	[ICRA]A-&	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)

\*Outstanding amount has declined on account of part payment against ISIN INE572J07315 (reduced to Rs. 10.00 crore from Rs. 100.00 crore) and ISIN INE572J07323 (reduced to Rs. 26.25 crore from Rs. 35.00 crore)  
&: Rating Watch with Developing Implications

## Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund based – Term loan	Simple
Non-convertible debentures	Simple
Market linked debentures	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**

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term fund based – Term loan	June-09-2017 to March-24-2023	NA	February-01-2024 to January-27-2026	812.56	[ICRA]A (Positive)
Unutilised	Term loan	NA	NA	NA	1,292.44	[ICRA]A (Positive)
INE572J07281	NCD programme	December 24, 2020	11.49%	December 22, 2023	21.50	[ICRA]A (Positive); withdrawn
INE572J07315	NCD programme	February 26, 2021	12.50%	February 26, 2024	100.00	[ICRA]A (Positive)
INE572J07323	NCD programme	March 12, 2021	11.49%	March 12, 2027	35.00	[ICRA]A (Positive)
INE572J07414	NCD programme	August 1, 2022	12.29%	August 1, 2028	23.00	[ICRA]A (Positive)
Unutilised	NCD programme	-	-	-	200.00	[ICRA]A (Positive)
INE572J07257	MLD programme	November 24, 2020	-	November 24, 2023	100.00	PP-MLD[ICRA]A (Positive); withdrawn
INE572J07208	MLD programme	October 28, 2020	-	June 27, 2024	20.00	PP-MLD[ICRA]A (Positive)

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

**Annexure II: List of entities considered for consolidated analysis**

Company Name	Ownership	Consolidation Approach
Crisis Financial Holdings Limited	99.85%	Full Consolidation
Caspian Financial Services Limited	100.00%	Full consolidation

Source: Company

Note: ICRA has taken a consolidated view of the parent (SSFL), its subsidiaries and associates while assigning the ratings

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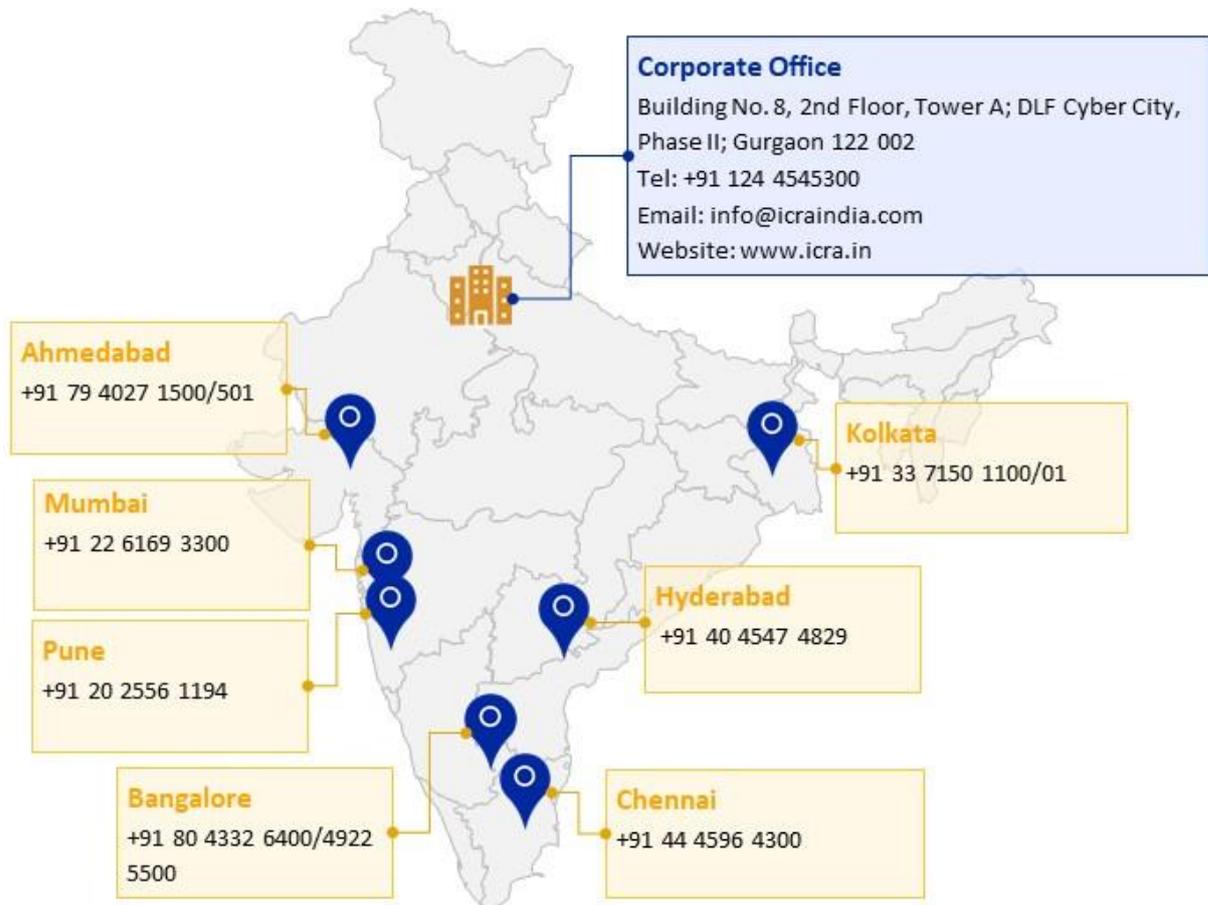
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