June 27, 2024

Veritas Finance Private Limited: Provisional ratings assigned to PTCs backed by small business loan and home construction loan receivables issued by Vajra 009 Trust

Summary of rating action

Trust Name	Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Vajra 009 Trust	Series A1 PTC	200.00	Provisional [ICRA]AAA(SO); Assigned
	Series A2 PTC	100.00	Provisional [ICRA]AA(SO); Assigned

**Instrument details are provided in Annexure I*

Rating in the absence of pending actions/documents	No rating would have been assigned as it would not be meaningful

Rationale

The pass-through certificates (PTCs) are backed by a pool of small business loan (SBL) and home construction loan (HCL) receivables originated by Veritas Finance Private Limited (Veritas/Originator) with an aggregate principal outstanding of Rs. 334.03 crore (pool receivables of Rs. 519.16 crore).

The provisional ratings are based on the strength of the cash flows from the selected pool of contracts, the credit enhancement available in the structure as well as the integrity of the legal structure. The ratings are subject to the fulfilment of all the conditions under the structure and ICRA's review of the documentation pertaining to the transaction.

Transaction structure

The transaction has a three-tranche structure with Series A1 PTC comprising 59.87% of the pool principal, followed by Series A2 PTC (29.94%) and the equity tranche (10.19%).

As per the transaction structure, the monthly cash flow schedule comprises the promised interest payout (on pari-passu basis to the holders of Series A1 PTC and Series A2 PTC on the outstanding PTC principal) and principal payout (59.87% of the pool principal billed) to Series A1 PTC. The balance principal (40.13% of the pool principal billed), after the replenishment of the credit enhancement, is expected to be paid on a monthly basis until the maturity of Series A1 PTC. A part of the residual cash flow from the pool (35%), after meeting the promised and expected payouts, will be used for the prepayment of the Series A1 PTC principal while the balance (65%) would be used for the payment of the equity tranche. Any prepayment in the pool would be used for the prepayment of the Series A1 PTC principal.

After the maturity of Series A1 PTC, the monthly cash flow schedule to Series A2 PTC comprises the promised interest payout and principal payout (89.81% of the pool principal billed). The balance principal (10.19% of the pool principal billed), after the replenishment of the credit enhancement, is expected to be paid on a monthly basis until the maturity of Series A2 PTC. A structure similar to the one used for Series A1 PTC would be followed to make the residual cash flow and prepayment payouts to Series A2 PTC. Further, ICRA notes that in case of a shortfall in collections at the end of the scheduled maturity date of the PTCs, the cash collateral (CC) will be utilised first for paying the dues towards Series A1 PTC and then for the dues towards Series A2 PTC.

The credit enhancement available in the structure is in the form of (i) a CC of 4.50% of the initial pool principal, amounting to Rs. 15.03 crore, to be provided by the Originator, (ii) subordination of 40.13% of the initial pool principal for Series A1 PTC and 10.19% of the initial pool principal for Series A2 PTC, and (iii) the excess interest spread (EIS) of 39.70% of the initial pool principal for Series A1 PTC and Series A2 PTC.

Key rating drivers and their description

Credit strengths

Availability of credit enhancement – The pool is granular, consisting of 9,021 contracts, with no contract exceeding 1% of the pool principal, thereby reducing the exposure to any single borrower. Further, the credit enhancement available in the form of the CC, subordination and EIS would absorb a part of the losses in the pool and provide support in meeting the PTC payouts.

No overdue contracts in the pool – The pool has been filtered in such a manner that there are no overdue contracts as on the cut-off date. Further, none of the contracts in the pool have ever been delinquent, which is a credit positive.

Seasoned contracts in the pool – The pool had amortised by almost 15% as on the cut-off date with no delinquencies seen in any of the contracts, post loan disbursement, thereby reflecting the borrowers' relatively better credit profile.

Contracts backed by self-occupied residential properties – A major part of the pool (~95% of the contracts in terms of the principal amount outstanding on the cut-off date) is backed by self-occupied residential properties. This is expected to support the quality of the pool as it has been observed that borrowers tend to prioritise repayments towards such loans even during financial stress.

Credit challenges

Significant geographical concentration – The pool has high geographical concentration with the top 3 states, viz. Tamil Nadu, Andhra Pradesh and West Bengal, contributing ~70% to the initial pool principal amount. The pool's performance would thus be exposed to any state-wide disruption that may occur due to natural calamities, political events, etc.

Risks associated with lending business – The pool's performance would remain exposed to macro-economic shocks, business disruptions and natural calamities that may impact the income-generating capability of the borrowers and their ability to make timely repayments of their loans.

Key rating assumptions

ICRA's cash flow modelling for rating securitisation transactions 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 assumptions for the losses and the coefficient of variation are considered on the basis of the values observed from the analysis of the past performance of the Originator's loan portfolio as well as the characteristics of the specific pool being evaluated. The resulting collections from the pool, after incorporating the impact of the losses and prepayments, are accounted for in ICRA's cash flow model, in accordance with the cash flow waterfall of the transaction.

For the current pool, ICRA has estimated the shortfall in the pool principal collection during its tenure at 4.75% with certain variability around it. The average prepayment rate for the underlying pool is modelled in the range of 7.2% to 27.0% per annum. Various possible scenarios have been simulated at stressed loss levels and prepayment rates and the incidences of default to the investor as well as the extent of losses are measured after factoring in the credit enhancement to arrive at the final rating for the instrument.

Liquidity position: Superior

The liquidity for both PTC instruments is superior after factoring in the credit enhancement available to meet the promised payout to the investors. The total credit enhancement would be greater than 8 times the estimated loss in the pool.

Rating sensitivities

Positive factors – Not applicable for Series A1 PTC; the rating could be upgraded for Series A2 PTC if sustained strong collection performance is witnessed in the underlying pool, leading to low delinquency levels and build-up of the cover from the credit enhancement of the balance pool principal.

Negative factors – The sustained weak collection performance of the underlying pool, leading to higher-than-expected delinquency levels and higher credit enhancement utilisation levels, would result in a rating downgrade. Weakening in the credit profile of the servicer could also exert pressure on the ratings.

Analytical approach

The rating action is based on the analysis of the performance of Veritas' portfolio till March 2024, the key characteristics and composition of the current pool, the performance expected over the balance tenure of the pool, and the credit enhancement cover available in the transaction.

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

Pending actions/documents required to be completed for conversion of the provisional rating into final

The assigned ratings are provisional and would be converted into final upon the execution of:

1. Trust deed
2. Assignment agreement
3. Legal opinion
4. Trustee letter
5. Chartered Accountant's know your customer (KYC) certificate
6. Any other documents executed for the transaction

Validity of the provisional rating

The Trust is expected to complete the pending actions/execute the pending documents in the near term. However, in case of continued pendency of the actions/documents beyond one year of this publication, the provisional rating would be withdrawn for the transaction even if the instrument has been issued.

Risks associated with the provisional rating

In case the issuance is completed, but the pending actions/documents are not completed for the transaction within one year (validity period) from the assignment of the rating, the provisional rating will be withdrawn in accordance with ICRA's Policy on Provisional Ratings available at www.icra.in.

About the originator

Veritas Finance Private Limited (Veritas) is a non-banking financial company (NBFC) incorporated on April 30, 2015 and registered with the Reserve Bank of India (RBI). The company is promoted by Mr. D Arulmany and it lends to borrowers engaged in the micro, small and medium enterprise (MSME) sector with a primary focus on providing inclusive finance to self-employed borrowers for their businesses. As on March 31, 2024, it had 434 branches across 10 states, namely Tamil Nadu, West Bengal, Karnataka, Odisha, Andhra Pradesh, Telangana, Bihar, Jharkhand, Chhattisgarh and Madhya Pradesh, as well as the Union Territory (UT) of Puducherry.

Veritas had a gross loan portfolio of Rs. 5,724 crore as on March 31, 2024 (Rs. 3,534 crore as on March 31, 2023). It has divided the MSME loan product segment into two broad heads – MSME Rural and MSME Urban, apart from home loans (HLs). While the MSME Rural segment consists of SBLs and HCLs, MSME Urban is focused on unsecured business loans meant for working capital purposes. The HL segment focuses on affordable housing. These products are differentiated on the basis of the purpose of the loan, customer segment, etc.

MSME Rural is a secured loan product offered for business purposes with a ticket size of Rs. 1 lakh to Rs. 50 lakh. HCLs under this segment are given for home construction, home improvement or shop construction with a ticket size of Rs. 5 lakh to Rs. 25 lakh. HLs are given for purchase or self-construction with a ticket size in the range of Rs. 5 lakh to Rs. 30 lakh. MSME Urban is an unsecured product with a ticket size of Rs. 1 lakh to Rs. 5 lakh.

As on March 31, 2024, the promoter (Mr. Arulmany) and his relatives held 11.70% on a fully-diluted basis while other shareholders include Norwest Venture Partners X Mauritius (21.78%), Multiples PE and affiliates (16.38%), Kedaara Capital Fund II LLP (15.21%), Lok Capital and affiliates (11.33%), British International Investments Plc. (10.42%), Avendus Future Leaders Fund (2.34%), and Caspian Impact Investment Advisers Private Limited (0.19%). The balance is held by individual shareholders and employees and their relatives.

Key financial indicators

Veritas Finance Private Limited	FY2022	FY2023	FY2024
	Audited	Audited	Audited
Total income	443.65	682.21	1,123.80
PAT	75.85	174.70	245.49
Assets under management (AUM)	2,187.35	3,533.73	5,723.79
Gross NPA	3.94%	2.19%	1.79%
Net NPA	2.34%	1.26%	0.85%
CRAR	64.43%	45.00%	41.49%

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

Trust Name	Current Rating (FY2025)				Chronology of Rating History for the Past 3 Years		
	Instrument	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2025	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022
				Jun 27, 2024	-	-	-
Vajra 009 Trust	Series A1 PTC	200.00	200.00	**Provisional [ICRA]AAA(SO)**	-	-	-
	Series A2 PTC	100.00	100.00	**Provisional [ICRA]AA(SO)**	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Series A1 PTC	Moderately Complex
Series A2 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 Type	Date of Issuance / Sanction	Coupon Rate (p.a.p.m.)	Maturity Date	Amount Rated (Rs. crore)	Current Rating
Vajra 009 Trust	Series A1 PTC	June 26, 2024	9.25%	November 20, 2030	200.00	Provisional [ICRA]AAA(SO)
	Series A2 PTC	June 26, 2024	9.75%	November 20, 2030	100.00	Provisional [ICRA]AA(SO)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Not Applicable

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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

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