October 18, 2024

Muthoot Capital Services Limited: Provisional [ICRA]AAA(SO) assigned to PTC Series A1a and Provisional [ICRA]A(SO) assigned to PTC Series A1b issued by Azalea 2024, backed by a pool of two-wheeler loans

Summary of rating action

Trust Name	Instrument*	Rated Amount (Rs. crore)	Rating Action
Azalea 2024	PTC Series A1a	35.40	Provisional [ICRA]AAA(SO); Assigned
	PTC Series A1b	35.40	Provisional [ICRA]A(SO); Assigned

**Instrument details are provided in Annexure I*

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

Rationale

The pass-through certificates (PTCs) are backed by a pool of two-wheeler loan receivables originated by Muthoot Capital Services Limited (MCSL/Originator) with an aggregate principal outstanding of Rs. 78.68 crore (pool receivables of Rs. 96.64 crore).

The provisional ratings are based on the strength of the cash flows from the selected pool of contracts along with the eligibility criteria for follow-on pools, the credit enhancement available in the structure as well as the integrity of the legal structure. The provisional 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

As per the transaction structure, the tenure of the pool shall be divided into two periods – replenishment period and amortisation period. MCSL will be the Servicer for the transaction.

Replenishment period

The replenishment period will be for 6 months from the transaction commencement date. During this period, both PTC Series A1a and PTC Series A1b investors will receive only the promised interest payouts each month on pari-passu basis. The balance pool collections will be used by the trust to purchase fresh loan receivables from MCSL as per the pre-defined selection criteria which would result in build-up of the pool principal during this period and thus increase the subordination for the rated instruments.

The transaction also entails certain trigger events for early amortisation. A breach of any of these trigger events would lead to the end of the replenishment period and the start of the amortisation period. If a trigger event occurs at any time during the replenishment period, then the tenure of the PTCs shall be reduced and be co-terminus with the remaining tenure of the pool of receivables assigned to the trust.

Amortisation period

Post the replenishment period, both PTC Series A1a and PTC Series A1b investors will receive the promised interest payouts each month on pari-passu basis. All the principal collections including prepayments would be passed on to PTC Series A1a on an expected basis till the 'attachment month'. The 'attachment month' is defined as the month till which the pool principal billing would be 1.6 times the PTC Series A1a principal. Post the attachment month, all principal collections including prepayments would be passed on to both series of PTCs on a pari-passu basis. The principal is promised to the investors for both series of PTCs on the legal final maturity date of the transaction.

The credit enhancement for PTC Series A1a is available in the form of pool principal cover of 1.6 times over the PTC Series A1a principal and pool cashflow cover of ~2.0 times over the PTC Series A1a cashflows till the attachment month. For PTC Series A1b the credit enhancement is available in the form of subordination of 10% of the initial pool principal and entire excess interest spread (EIS) in the structure. Additional credit enhancement is available in the structure in the form of a CC of 5.00% of the initial pool principal, amounting to Rs. 3.93 crore, to be provided by the Originator (MCSL). The CC will be used to meet shortfalls in promised payouts to PTC investors.

Key eligibility criteria for the receivables

The eligibility criteria shall be met on commencement of the transaction and also at each replenishment event for all the new assets being added as well as for the updated pool (as applicable).

The key eligibility criteria that have to be met are mentioned below.

- The facility is a loan to an individual, partnership, sole proprietorship
- No facility is classified as a non-performing asset for the purposes of the directions and guidelines of the RBI.
- The pool should comply with the Minimum Holding Period requirements prescribed by the RBI.
- None of the loans in the pool have residual maturity of less than 365 days
- No facility is/shall be overdue as on the respective pool cutoff date
- All loans to be self-originated by the Originator and not under any co-lending partnership
- At least 75% of the pool to have seasoning of 9 months or higher
- No loans to have peak DPD during the seasoning period of more than 30 days
- All loans should have Original LTV less than 90%. In case LTV is between 90-100% all such loans should have minimum seasoning of 9 months
- Identified OEMs to constitute at least 85% of the pool
- Loans where the underlying cost of the vehicle is less than Rs. 1.5 Lakhs should comprise at least 90% of the pool. No loans to be taken where underlying cost of vehicle is greater than Rs. 2.0 Lakhs
- Weighted average interest rate of replenished pool should not be less than weighted average interest rate of initial pool less 2% and
- Maturity date of the underlying loans of replenished pool should not be more than May 31, 2028

Trigger events for early amortisation

The key early amortisation triggers which will lead to end of amortisation period are mentioned below.

- The Originator does not have sufficient loans (which meet the eligibility criteria)
- Utilisation of cash collateral to service PTC interest
- Rating downgrade of originator/servicer by two notches from date of transaction
- 30+ PAR on the outstanding pool breaches 10%
- Satisfaction of conditions that will trigger turbo amortisation trigger as defined in the legal documents

Key rating drivers and their description

Credit strengths

Granular pool supported by presence of credit enhancement – The current pool is granular (no obligor has more than 0.02% share in the initial pool) and the follow-on pools are also expected to be granular thereby reducing the exposure to any single borrower. Further, the credit enhancement available in the form of CC, subordination and EIS would absorb some amount of the losses in the pool and provide support in meeting the PTC payouts. Basis the utilisation of EIS during the replenishing period to purchase fresh receivables subject to eligibility criteria the subordination for both series of PTCs would increase during the replenishment period. Further as per the transaction structure, PTC Series A1a would receive principal collections till the attachment month and thus the pool cashflow cover over PTC Series A1a payouts is significantly high that supports the rating assigned to PTC Series A1a.

No overdue contracts in the pool – The initial pool has no overdue contracts as on pool cut-off date. Further any follow-on pool would also not include any overdue contracts on date of assignment to trust which is a credit positive.

Credit challenges

Moderate pool selection criteria – A potential concern pertaining to a replenishing structure is the uncertainty regarding the exact composition of the additional receivables. While the current transaction has a specified eligibility criteria, the follow-on pools may have a lower seasoning, lower interest rate contracts and contracts from weaker geographies. A higher presence of lower interest rates contracts would impact the excess interest spread adversely which acts as a credit enhancement in the structure.

Risks associated with lending business – The performance of both the initial and the follow-on pools 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. However, since the pool in the current transaction would be revised during the replenishment period, the characteristics of the pool would change unlike other PTC transactions where the pool is static. ICRA has used the defined eligibility criteria to arrive at a potential loss for the follow-on pools. The resulting collections from the current pool and follow on pools, 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 transaction, ICRA has estimated the shortfall in the principal of the pool crystalised at the end of replenishment period at 5.5% of the initial pool principal at end of its tenure with certain variability around it. The average prepayment rate for the underlying pool is modelled in the range of 3% to 9% 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 for PTC Series A1a and Strong for PTC Series A1b

The liquidity for PTC Series A1a is superior after factoring in the credit enhancement available to meet the promised payouts to the investor. The total credit enhancement would be more than 10 times the estimated loss in the pool.

The liquidity for PTC Series A1b is strong after factoring in the credit enhancement available to meet the promised payouts to the investor. The total credit enhancement would be ~4.0 times the estimated loss in the pool.

Rating sensitivities

Positive factors – Not applicable for PTC Series A1a. For PTC Series A1b, since the principal amortisation would begin on the crystallisation of the final pool, the ratings are unlikely to be upgraded till the final pool is crystallised. The rating could be upgraded basis the healthy collections observed in the final crystallised pool, leading to the build-up of the credit enhancement cover over the rated PTCs.

Negative factors – The ratings could be downgraded on the occurrence of a trigger event, non-adherence to the key transaction terms and deterioration in the performance of the follow-on pools such that the delinquencies during the amortisation period are higher than expected. Weakening in the credit profile of the servicer (MCSL) could also exert pressure on the ratings.

Analytical approach

The rating action is based on the analysis of the performance of MCSL's two-wheeler portfolio till June 2024, the key characteristics and composition of the current pool, the eligibility criteria for follow-on pools, the performance expected over the balance tenure of the pool, and the credit enhancement cover available in the transaction.

Analytical Approach	
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 rating is provisional and would be converted into final upon the execution of:

1. Trust deed
2. Assignment agreement
3. Legal opinion
4. Trustee letter
5. Auditor's 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

MCSL was incorporated in 1994 and is a deposit-taking non-banking financial company (NBFC). MCSL is a part of Muthoot Pappachan Group (MPG) and is based out of Kochi, Kerala. The company obtained NBFC license in 1998 and is primarily engaged in the two-wheeler financing business. The company also provides loans for purchase of used cars, light commercial vehicles (LCV) and three wheelers and also has a small corporate loan book. MCSL is a listed entity and has a presence in 21 states/union territories. In FY2024, MCSL reported a net profit of Rs. 122.7 crore with total assets of Rs. 2,314.2 crore compared with a net profit of Rs. 78.7 crore with total assets of Rs. 2,435.3 crore for FY2023. In Q1 FY2025, it reported a provisional net profit of Rs. 10.8 crore and total assets of Rs. 2,406.4 crore.

Key financial indicators

Muthoot Capital Services Limited (standalone)	FY2023	FY2024	Q1FY2025
Interest income	440.6	396.1	99.8
Profit after tax	78.7	122.7	10.8
Total assets	2,435.3	2,314.2	2,404.6
Gross stage 3	20.6%	10.2%	8.1%
CRAR	27.8%	31.3%	28.8%

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	Amount Rated (Rs. crore)	Date & Rating in FY2025	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022
			October 18, 2024	-	-	-
Azalea 2024	PTC Series A1a	35.40	**Provisional [ICRA]AAA(SO)**	-	-	-
	PTC Series A1b	35.40	**Provisional [ICRA]A(SO)**	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
PTC Series A1a	Moderately Complex
PTC Series A1b	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 Name	Date of Issuance / Sanction	Coupon Rate (p.a.p.m)	Maturity Date	Amount Rated (Rs. crore)	Current Rating
Azalea 2024	PTC Series A1a	October 11, 2024	9.25%	June 23, 2028	35.40	Provisional [ICRA]AAA(SO)
	PTC Series A1b		10.00%		35.40	Provisional [ICRA]A(SO)

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

Gaurav Mashalkar
+91 22 6114 3431
gaurav.mashalkar@icraindia.com

Mrugesh Trivedi
+91 22 6114 3436
mrugesh.trivedi@icraindia.com

Arijit Datta
+91 22 6114 3400
arijit.datta@icraindia.com

RELATIONSHIP CONTACT

Mr. L. Shivakumar
+91 22 6169 3304
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