November 26, 2024

Fusion Finance Limited: Rating downgraded and Outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
NCD programme	180.00	180.00	[ICRA]A (Negative); rating downgraded from [ICRA]A+ and outlook revised to Negative from Stable
Subordinated debt	55.00	55.00	[ICRA]A (Negative); rating downgraded from [ICRA]A+ and outlook revised to Negative from Stable
Total	**235.00**	**235.00**	

**Instrument details are provided in Annexure I; NCD – Non-convertible debenture*

Rationale

Fusion Finance Limited (Fusion) announced its Q2/H1 FY2025 results on November 15, 2024, wherein it reported a higher-than-expected deterioration in its asset quality and profitability. The company's gross stage 3 assets increased to 9.4% as of September 2024 from 2.9% as of March 2024. Consequently, the earnings profile was adversely impacted, resulting in a net loss of Rs. 341 crore in H1 FY2025 vis-à-vis a net profit of Rs. 505 crore in FY2024. The deterioration in the asset quality was attributed to various factors including, but not limited to, adverse climatic conditions, attrition at the field level, worsening of credit discipline and overleveraging of borrowers.

Further, given the deterioration in the asset quality and profitability, Fusion was in breach of various financial covenants (in respect of borrowings amounting to Rs. 5,618 crore) as on September 30, 2024, thus making these borrowings repayable on demand. As a result, the statutory auditor highlighted material uncertainty regarding the company's ability to continue as a going concern as the lenders had not waived their right to demand immediate repayment from the company. The amount of borrowings with breach in covenant had reduced to ~Rs. 5,169 crore as on November 20, 2024. ICRA notes that Fusion is in the process of obtaining requisite waivers from its lenders and the same remains a key monitorable. While the current liquidity profile is adequate, the inability to obtain the requisite waivers could lead to pressure on the liquidity profile.

The rating continues to factor in Fusion's established track record of operations with a presence across 22 states/Union Territories (UTs) as of September 2024. The company remains comfortably capitalised with a net worth of Rs. 2,523 crore and a gearing (managed) of 3.9 times as on September 30, 2024. It is in the process of raising equity capital via a rights issue of up to Rs. 550 crore, which shall help it maintain a prudent capitalisation profile while providing for the deterioration in the asset quality and the consequent losses.

The Negative outlook on the rating reflects ICRA's expectation that the company's asset quality and profitability shall remain under pressure in the near term.

Key rating drivers and their description

Credit strengths

Established track record of operations – Commencing operations in 2010, Fusion is one of the largest microfinance companies in India with a presence in 22 states/UTs, catering to more than 38 lakh borrowers as on September 30, 2024. The company was operating through a network of 1,463 branches with assets under management (AUM) Rs. 11,571 crore as on September 30, 2024. ICRA notes that disbursements declined in H1 FY2025 amid asset quality challenges and the implementation of tighter customer selection criteria. ICRA expects AUM growth to remain under pressure in FY2025. ICRA takes comfort from Fusion's track record of operations and expects a gradual improvement in disbursements. Apart from microfinance, the company has a small share of micro, small and medium enterprise (MSME) loans, comprising ~5% of the AUM as on September 30, 2024.

Comfortable capitalisation profile – Fusion remains comfortably capitalised with a net worth of Rs. 2,523 crore and a gearing (managed) of 3.9 times as on September 30, 2024. The company's capital-to-risk weighted assets ratio (CRAR) of 24.4%, as on September 30, 2024, was well above the regulatory requirement of 15%. Fusion is in the process of raising equity capital via a rights issue of up to Rs. 550 crore, which shall help it maintain a prudent capitalisation profile while providing for the deterioration in the asset quality and the consequent losses. ICRA takes note of the majority shareholder and the promoter's intent to continue supporting the company by participating in the upcoming round of equity infusion. Going forward, ICRA expects Fusion's capitalisation profile to remain comfortable with the gearing (managed) remaining below 5 times on a sustained basis.

Credit challenges

Significant deterioration in asset quality and profitability – The company reported a significant deterioration in its asset quality in H1 FY2025 with the gross stage 3 assets increasing to 9.4% as of September 2024 from 2.9% as of March 2024. This was attributed to various factors including, but not limited to, adverse climatic conditions, attrition at the field level, worsening of credit discipline and overleveraging of borrowers. Fusion has taken certain corrective measures such as tightening of customer selection criteria and strengthening of the collections, tele-calling and senior management teams. Nevertheless, its ability to arrest further slippages and recover from delinquent customers remains important.

Given the deterioration in the asset quality, the company's credit costs increased significantly to 15.2% (annualised) of average managed assets (AMA) in H1 FY2025 from 2.8% in FY2024. This, along with the increase in operating expenses, has adversely impacted the earnings profile, resulting in a net loss of Rs. 341 crore in H1 FY2025 vis-à-vis a net profit of Rs. 505 crore in FY2024. ICRA expects the asset quality and profitability to remain under pressure in FY2025.

Political, communal and other risks in microfinance sector, given the marginal borrower profile – The microfinance industry is prone to socio-political and operational risks, which could negatively impact its operations and financial position. However, a geographically diversified portfolio would mitigate these risks partially as these issues are largely region-specific, so far. Fusion's ability to onboard borrowers with a good credit history, recruit and retain employees and improve its geographical diversity further by penetrating in recently entered territories with nascent operations would be relevant for managing the high growth rates.

The rating also factors in the risks associated with the marginal borrower profile, unsecured lending, increased risks from multiple lending and overleveraging, business and political risks, along with the challenges associated with a high pace of growth and attrition. 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 microfinance institutions (MFIs), regarding their underwriting practices, borrowers' income and leverage assessment, multiple identity proof as well as gaps in the information available with the bureaus remain.

Environment and social risks

Environmental – While MFIs like Fusion do not face material physical climate risks, they are exposed to environmental risks indirectly through their portfolio of assets. If the borrowers, to whom such MFIs have an exposure, face livelihood disruption because of physical climate adversities, it could translate into credit risks for them. However, such risk is not material for Fusion as it benefits from adequate geographical diversification of its portfolio. Further, the lending is for loans with a tenure of around two years, which will allow it to adapt and take incremental exposure to borrowers facing relatively fewer downside environmental risks.

Social – With regard to social risks, data security and customer privacy are among the key sources of vulnerability for MFIs as a material lapse could be detrimental to their reputation and invite regulatory censure. Fusion has not faced such lapses over the years, which highlights its sensitivity to such risks.

Liquidity position: Adequate

As on September 30, 2024, the company held free cash, bank balances and liquid investments of Rs. 1,793 crore. This, along with the scheduled collections (principal) of Rs. 6,305 crore, is sufficient to meet the scheduled debt repayments of Rs. 5,630 crore over the next 12 months, i.e. until September 30, 2025. Factoring in the estimated collections from advances, the liquidity profile is expected to remain adequate to meet the scheduled debt obligations in a timely manner. Nevertheless, the company faces prepayment risk, given the possibility of debt acceleration due to the breach of covenants, including financial, operating and rating-linked covenants, which may result in a stressed liquidity profile. ICRA notes that Fusion is in the process of obtaining the requisite waivers from its lenders and the same remains a key monitorable.

Rating sensitivities

Positive factors – ICRA could revise the outlook if the company demonstrates a sustained improvement in its asset quality and profitability indicators while maintaining a prudent capitalisation profile.

Negative factors – The rating could be downgraded if there is no material improvement in the asset quality or profitability.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA's Rating Methodology for Non-banking Finance Companies
Parent/Group support	Not applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company

About the company

Incorporated in 1994, Fusion Finance Limited started microfinance operations in 2010 and became a registered non-banking financial company-microfinance institution (NBFC-MFI) in 2014. It is engaged in microfinance lending, providing financial services (and educating borrowers on financial literacy) to poor women in India, who are organised as joint liability groups (JLGs). Fusion also uses its distribution channels to provide other financial products and services to members, primarily for the purchase of productivity-enhancing products such as mobile phones, mixer grinders/bicycles, emergency loans, etc. It also has a small portfolio in the micro, small and medium enterprise (MSME) segment, accounting for 5.4% of the total assets under management (AUM) as on September 30, 2024.

As on September 30, 2024, Fusion had a presence in 483 districts across 22 states/UTs through 1,463 MFI branches. It reported a net loss of Rs. 341 crore in H1 FY2025 on gross AUM of Rs. 11,571 crore as on September 30, 2024 vis-à-vis a net profit of Rs. 505 crore in FY2024 on gross AUM of Rs. 11,476 crore as on March 31, 2024.

Key financial indicators (audited)

Fusion	FY2023	FY2024	H1FY2025^
Total income	1,782	2,386	1,403
Proft after tax	387	505	(341)
Total managed assets	10,655	13,302	13,912
Return on average managed assets	4.1%	4.2%	-5.0%
Managed gearing (times)	3.4	3.4	3.9
Gross NPA/ stage 3	3.5%	2.9%	9.4%
CRAR	27.9%	27.5%	24.4%

Source: Company data, ICRA Research; all values and ratios are as per ICRA's calculations and estimates; Amounts in Rs crore; ^As per limited review financials and data

Status of non-cooperation with previous CRA: Not applicable

Any other information: Fusion faces prepayment risk, given the possibility of debt acceleration upon the breach of covenants, including financial, operating and rating-linked covenants. Upon failure to meet the covenants, if the company is unable to get waivers from the lenders/investors or the lenders/investors do not provide it with adequate time to arrange for alternative funding to pay off the accelerated loans, the rating would face pressure. The company was in breach of various financial covenants in respect of borrowings amounting to Rs. 5,618 crore as on September 30, 2024, thus making these borrowings repayable on demand. The amount of borrowings with breach in covenant had reduced to ~Rs. 5,169 crore as on November 20, 2024. Consequently, the statutory auditor highlighted material uncertainty regarding Fusion's ability to continue as a going concern as the lenders had not waived their right to demand immediate repayment from the company. ICRA notes that the company is in the process of obtaining the requisite waivers from its lenders and the same remains a key monitorable.

Rating history for past three years

Current (FY2025)						Chronology of rating history for the past 3 years					
				FY2025		FY2024		FY2023		FY2022	
Instrument	Type	Amount Rated (Rs Crore)	Nov-26-2024	Date	Rating	Date	Rating	Date	Rating	Date	Rating
NCD programme	Long Term	180.00	[ICRA]A (Negative)	16-May-2024	[ICRA]A+ (Stable)	19-July-2023	[ICRA]A (Positive)	07-APR-2022	[ICRA]A- (Stable)	21-SEP-2021	[ICRA]A- (Stable)
				-	-	12-Jan-2024	[ICRA]A+ (Stable)	26-APR-2022	[ICRA]A- (Stable)	-	-
				-	-	-	-	09-Dec-2022	[ICRA]A (Stable)	-	-
				-	-	-	-	27-Jan-2023	[ICRA]A (Stable)	-	-
Subordinated debt	Long Term	55.00	[ICRA]A (Negative)	16-May-2024	[ICRA]A+ (Stable)	19-July-2023	[ICRA]A (Positive)	07-Apr-2022	[ICRA]A- (Stable)	-	-
				-	-	12-Jan-2024	[ICRA]A+ (Stable)	26-Apr-2022	[ICRA]A- (Stable)	-	-
				-	-	-	-	09-Dec-2022	[ICRA]A (Stable)	-	-
				-	-	-	-	27-Jan-2023	[ICRA]A (Stable)	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Non-convertible debentures	Simple
Subordinated debt	Very 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

ISIN	Instrument	Date of Issuance	Coupon Rate	Maturity Date	Rated Amount (Rs. crore)	Rating
INE139R08116	**NCD**	Apr-19-2022	11.04%	Dec-31-2024	35.00	[ICRA]A (Negative)
INE139R07431	**NCD**	May-04-2022	10.35%	May-04-2027	145.00	[ICRA]A (Negative)
INE139R08108	**Subordinated debt**	Mar-31-2022	13.00%	Jun-30-2027	25.00	[ICRA]A (Negative)
INE139R08090	**Subordinated debt**	Mar-31-2022	12.11%	Sep-30-2027	30.00	[ICRA]A (Negative)

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.

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