December 17, 2024

Pahal Financial Services Pvt. Ltd.: Rating reaffirmed and outlook revised to Negative; Rating withdrawn for Rs. 40-crore NCD programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible debentures	60.90	60.90	[ICRA]BBB- (Negative); reaffirmed and outlook revised to Negative from Stable
Non-convertible debentures	40.00	0.00	[ICRA]BBB- (Negative); reaffirmed and outlook revised to Negative from Stable and withdrawn
Long-term fund based – Term loan	50.00	50.00	[ICRA]BBB- (Negative); reaffirmed and outlook revised to Negative from Stable
Total	**150.90**	**110.90**	

**Instrument details are provided in Annexure I*

Rationale

The revision in the outlook to Negative considers the delay in the capital infusion, which has led to Pahal Financial Services Pvt. Ltd.'s (PFSPL) managed gearing remaining above 7 times in the past few quarters, higher than the ICRA-stipulated negative rating sensitivity. ICRA takes note of PFSPL's plans to raise sizeable equity capital, in relation to its current net worth, in the near term. The timely raise of equity capital, in view of the asset quality stress, shall therefore remain a key rating monitorable. The company also reported a deterioration in its asset quality in H1 FY2025 with the gross non-performing assets (GNPAs) increasing to 4.3% as on September 30, 2024 from 2.5% as on March 31, 2024. This was due to various factors including, but not limited to, adverse climatic conditions, worsening of credit discipline and overleveraging of borrowers. Given the deterioration in the asset quality, PFSPL's credit costs increased to 2.6% (annualised) of average managed assets (AMA) in H1 FY2025 from 1.4% in FY2024. This, along with higher operating expenses, has adversely impacted the earnings profile, resulting in a decline in the net profit to Rs. 10 crore in H1 FY2025 (RoMA[1] of 0.8%; annualised) from Rs. 39 crore in FY2024 (RoMA of 1.9%).

The rating, however, factors in PFSPL's established track record of operations in the microfinance sector and its adequately diversified funding profile. The rating continues to consider the company's geographically concentrated operations and the risks associated with microfinance loans.

ICRA has reaffirmed the rating and revised the outlook to Negative while simultaneously withdrawing the rating for the Rs. 40-crore non-convertible debenture (NCD) programme as the instrument has been redeemed by the company with no amount outstanding against the same. The rating has been withdrawn in accordance with ICRA's policy on the withdrawal of credit ratings.

Key rating drivers and their description

Credit strengths

Established track record in microfinance sector – Since commencing operations in 2011 under microfinance lending, PFSPL has a track record of over a decade in the sector. As on September 30, 2024, the company was operating through a network of 361 branches spreads across 152 districts in 11 states/Union Territories (UTs) while managing a portfolio of Rs. 1,985 crore.

[1] Return on managed assets

It is promoted by Mr. Kartik Mehta and Ms. Purvi Bhavsar, who have experience in the banking and microfinance sectors. PFSPL's existing investors include Base of Pyramid Asia (BoPA) Pte. Ltd., Dia Vikas Capital Private Limited (an impact investor) and GAWA Capital Pte. Ltd.

Adequately diversified funding profile – PFSPL's funding mix is adequately diversified for its current scale. It has credit lines from various lenders including non-banking financial companies (NBFCs), financial institutions (FIs), public sector banks and private sector banks. The company's borrowing profile comprised loans from NCDs (36%), NBFCs/FIs (32%), banks (27%), and sub-debt (6%) as on September 30, 2024. It raised Rs. 625-crore debt funds (including securitisation) in H1 FY2025 and had a healthy pipeline of funding to support its near-term disbursement plans. Nevertheless, it is important for PFSPL to reduce its cost of funds and further diversify its funding profile as it continues to scale up its operations.

Credit challenges

High geographical concentration – PFSPL's portfolio has high geographical concentration with the top 3 states comprising 68% of the AUM as on September 30, 2024; Gujarat (31%) and Bihar (24%) account for a high share. ICRA, however, notes that the concentration in the top 3 states has declined from 75% as on March 31, 2023. Also, PFSPL commenced operations in Telangana in FY2025. ICRA expects the share of AUM in Gujarat and Bihar to remain relatively high in the near term with a gradual reduction as the company scales up its operations. Further, there is scope for improving the district-level diversification of the AUM.

High leverage – PFSPL's gearing increased owing to the high pace of growth in the last two years, the subdued profitability and the delay in the equity infusion. The on-book gearing and managed gearing increased to 5.9 times and 7.4 times, respectively, as on September 30, 2024, from 5.1 times and 6.5 times, respectively, as on March 31, 2023. The reported capital adequacy ratio stood at 18.6%, as on September 30, 2024, above the regulatory requirement of 15%. PFSPL has been in breach of the ICRA-stipulated rating sensitivity for the managed gearing over the past few quarters. ICRA takes note of the company's plans to raise sizeable equity capital in the coming months to improve its capitalisation profile and support its growth plans. The timely raise of equity capital and improvement in the capitalisation profile shall remain key near-term rating factors, considering the asset quality stress.

Deterioration in asset quality and profitability – The company reported a deterioration in its asset quality in H1 FY2025 with the GNPAs increasing to 4.3% as on September 30, 2024 from 2.5% as on March 31, 2024. This was due to various factors including, but not limited to, adverse climatic conditions, worsening of credit discipline and overleveraging of borrowers. Given the deterioration in the asset quality, the credit costs increased to 2.6% (annualised) of AMA in H1 FY2025 from 1.4% in FY2024. This, along with higher operating expenses, has adversely impacted the earnings profile, resulting in a net profit of Rs. 10 crore in H1 FY2025 (RoMA of 0.8%; annualised) vis-à-vis Rs. 39 crore in FY2024 (RoMA of 1.9%). ICRA expects the asset quality and profitability to remain under pressure in FY2025 and PFSPL's ability to arrest further slippages and recover from delinquent customers is critical.

Political, communal and other risks in microfinance sector, given the marginal borrower profile – Microfinance remains susceptible to the risks associated with unsecured lending to marginal borrowers with limited ability to absorb income shocks and the rising borrower leverage levels owing to an increase in multiple lending in the areas of operations. Further, political and operational risks associated with microfinance may result in high volatility in the asset quality indicators. The microfinance industry is prone to socio-political, climatic and operational risks, which could negatively impact its operations. PFSPL's ability to onboard borrowers with a good credit history, recruit and retain employees as well as improve the geographical diversity of its operations would be key for managing high growth rates while maintaining its credit profile.

Liquidity position: Adequate

As on September 30, 2024, the company had a free cash and bank balance of Rs. 186 crore and scheduled inflows from advances of Rs. 972 crore against scheduled debt repayments of Rs. 595 crore during October 1, 2024 to September 30, 2025.

Factoring in the expected collections from advances, the liquidity profile is expected to remain adequate to meet the debt obligations in a timely manner.

Rating sensitivities

Positive factors – ICRA could revise the outlook if there is timely equity infusion, resulting in an improvement in the capitalisation profile. PFSPL's ability to keep the asset quality under control would also be a credit positive.

Negative factors – The rating could be downgraded if the proposed capital infusion is delayed, leading to the managed gearing remaining above 7 times on a sustained basis. Further, deterioration in the asset quality or profitability could exert pressure on the rating.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Non-banking Finance Companies ICRA Policy on Withdrawal of Credit Ratings
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

About the company

PFSPL is an Ahmedabad-based non-banking financial company-microfinance institution (NBFC-MFI) registered with the Reserve Bank of India. It commenced operations in March 2011 by acquiring the existing operations of Lok Vikas Nidhi, a trust operational in Gujarat for over 25 years. The current promoters acquired the portfolio of Rs. 2.6 crore spread over 15 branches, along with the field staff of Lok Vikas, and subsequently transferred the acquired portfolio to an NBFC along with an equity contribution of Rs. 2 crore. The NBFC was renamed Pahal Financial Services Pvt. Ltd.

PFSPL lends to poor women primarily in the rural and semi-urban areas of Gujarat, Rajasthan, Madhya Pradesh, Bihar, Uttar Pradesh, Chhattisgarh, Haryana, Maharashtra, Tamil Nadu, Puducherry and Telangana. It reported a profit after tax (PAT) of Rs. 10 crore in H1 FY2025 with an AUM of ~Rs. 1,985 crore as on September 30, 2024 compared to Rs. 39 crore in FY2024 with an AUM of Rs. 2,094 crore as on March 31, 2024.

Key financial indicators

PFSPL	FY2023	FY2024	H1 FY2025
	Audited	Audited	Reviewed
	Ind-AS	Ind-AS	Ind-AS
Total income	279	461	252
PAT	15	39	10
Total managed assets	1,796	2,402	2,334
Return on managed assets	0.9%	1.9%	0.8%
Managed gearing (times)	6.5	7.7	7.4
GNPA	1.9%	2.5%	4.3%

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore
Managed gearing = (on-book debt + off-book portfolio) / net worth

Status of non-cooperation with previous CRA: Not applicable

Any other information:

PFSPL 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. Nevertheless, ICRA notes that PFSPL has been able to raise fresh funds despite covenant breaches in the last two to three years. The management has guided that the company has requested waivers from lenders/investors for such breaches.

Rating history for past three years

	Current (FY2025)			Chronology of rating history for the past 3 years					
				Date & Rating in FY2024		Date & Rating in FY2023		Date & Rating in FY2022	
Instrument	**Type**	**Amount rated (Rs. crore)**	**Dec-17-24**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**
Bank lines	Long term	50.00	[ICRA]BBB- (Negative)	08-MAR-2024	[ICRA]BBB- (Stable)	10-MAR-2023	[ICRA]BBB- (Stable)	17-MAR-2022	[ICRA]BBB- (Stable)
				28-MAR-2024	[ICRA]BBB- (Stable)	-	-	-	-
NCD	Long term	40.00	[ICRA]BBB- (Negative); withdrawn	08-MAR-2024	[ICRA]BBB- (Stable)	10-MAR-2023	[ICRA]BBB- (Stable)	17-MAR-2022	[ICRA]BBB- (Stable)
				08-MAR-2024	[ICRA]BBB- (Stable); withdrawn	-	-	-	-
				28-MAR-2024	[ICRA]BBB- (Stable)	-	-	-	-
				28-MAR-2024	[ICRA]BBB- (Stable)	-	-	-	-
NCD	Long term	60.90	[ICRA]BBB- (Negative)	08-MAR-2024	[ICRA]BBB- (Stable)	10-MAR-2023	[ICRA]BBB- (Stable)	17-MAR-2022	[ICRA]BBB- (Stable)
				08-MAR-2024	[ICRA]BBB- (Stable); withdrawn	-	-	-	-
				28-MAR-2024	[ICRA]BBB- (Stable)	-	-	-	-
				28-MAR-2024	[ICRA]BBB- (Stable)	-	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Non-convertible debentures	Simple
Bank facilities	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	Name of instrument	Date of Issuance	Coupon Rate	Maturity Date	Rated Amount (Rs. crore)	Current Rating and Outlook
INE514Q08021	**NCD**	Mar-16-2020	16.50%	Jun-16-2025	15.00	[ICRA]BBB- (Negative)
INE514Q07239	**NCD**	Apr-23-2021	12.30%	Apr-30-2025	37.50	[ICRA]BBB- (Negative)
INE514Q07288	**NCD**	Jun-02-2022	13.65%	Jun-30-2026	40.00	[ICRA]BBB- (Negative); withdrawn
Unallocated	**NCD**	-	-	-	8.40	[ICRA]BBB- (Negative)
NA	**Bank lines**	Mar 2023	MCLR + 2.85%	Mar 2026	50.00	[ICRA]BBB- (Negative)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Not applicable

ANALYST CONTACTS

Karthik Srinivasan
+91 22 6114 3444
karthiks@icraindia.com

A M Karthik
+91 44 4596 4308
a.karthik@icraindia.com

Prateek Mittal
+91 33 7150 1100
prateek.mittal@icraindia.com

Arpit Agarwal
+91 124 4545 873
arpit.agarwal@icraindia.com

Chandni
+91 124 4545 300
chandni@icraindia.com

RELATIONSHIP CONTACT

L Shivakumar
+91 22 2433 1084
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:

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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