

## Small Business FinCredit India Private Limited

September 28, 2018

### Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Bank Lines Programme	200.00	200.00	[ICRA]A(stable); reaffirmed
Non-convertible Debenture Programme	400.00	400.00	[ICRA]A(stable); reaffirmed
<b>Total</b>	<b>600.00</b>	<b>600.00</b>	

\*Instrument details are provided in Annexure-1

### Rating action

ICRA has reaffirmed the long-term rating of [ICRA]A (pronounced ICRA A) on the Rs. 200-crore long-term bank lines programme and the Rs. 400-crore non-convertible debenture programme of Small Business FinCredit India Private Limited (SBFC)<sup>1</sup>. The outlook on the long-term rating is Stable.

### Rationale

The rating reaffirmation factors in the induction of the senior management team, with significant experience in the retail lending business, coupled with the revamping of the risk management systems and processes and the company's efforts to source leads and collect payments in-house, within the indicated timelines. The rating factors in the significant upfront equity infusion of Rs. 845 crore by Lyra Partners Limited (Lyra Partners) and Arpwood Partners Investment Advisors LLP (Arpwood Partners) for the acquisition of the retail lending book and the existing infrastructure, branch network and employee team from Karvy Financial Services Limited (KFSL). This equity infusion and the Rs. 400-crore non-convertible debentures have helped the acquisition of the Rs. 807-crore loan assets from KFSL.

The retail lending portfolio consists of small ticket micro enterprise (ME) loans, medium ticket small and medium enterprise (SME) loans, loan against gold (LAG) and small commercial vehicle (SCV) loans. The rating also factors in the moderate seasoning and stable asset quality of the ME and SME loans, which were acquired as a part of the KFSL deal. ICRA notes the near-zero delinquency levels of the portfolio originated by the new team under the new processes.

The company's ability to keep the asset quality in check, as the portfolio seasons, would be a key rating sensitivity in the near to medium term. Going forward, SBFC's ability to improve its profitability by borrowing at competitive rates from banks and by controlling operating expenses would also be a key rating monitorable.

<sup>1</sup> For complete rating scale and definitions, please refer to ICRA's website [www.icra.in](http://www.icra.in) or other ICRA Rating Publications

## Outlook: Stable

ICRA believes that Small Business FinCredit India Private Limited will continue to benefit from the upfront equity infusion along with the experienced senior management team and the acquired infrastructure from KFSL. The outlook may be revised to Positive if the entity is able to scale up while maintaining sound asset quality of the loan book. The outlook would be revised to Negative if there is material deterioration in the asset quality of the loan book, thereby impacting the company's profitability.

## Key rating drivers

### Credit strengths

**Granular book with retail focus; low average ticket size and LTV with adequate seasoning** – As of June 2018, the ME, SME, LAG, SCV and unsecured personal loans formed 59%, 17%, 22%, 1.7% and 0.3%, respectively, of the portfolio. Around 60% of the ME portfolio and 62% of the SME portfolio had a loan-to-value (LTV) ratio of less than 50%, indicating adequate collateral coverage, while 78% of the ME portfolio had a ticket size of less than Rs. 40 lakh. Meanwhile, 92% of the LAG portfolio had a ticket size of less than Rs. 5 lakh, which imparts granularity to the overall assets under management (AUM). SBFC completed the acquisition of the retail assets in September 2017, which included the management team, branch network, IT systems, employees, customers and Intellectual Property (IP) related to the retail business in order to ensure the continuity of the business. The entire branch network (80 branches and 6 regional offices) was renamed SBFC. The acquired loan book comprised ME loans (54%), SME loans (22%), LAG (21%) and SCV (3%) loans. ICRA takes comfort from the transaction structure, which ensured that only the seasoned portfolio was acquired with no new loan disbursements (except LAG) between June 2016 and September 2017 and average seasoning of over 25 months (except LAG). Only the performing portfolio (current and 0-30 for the ME book) was acquired. Gold loans, with mark-to-market LTV of less than 90%, were acquired. SBFC also has a credit enhancement from KFSL for any future non-performing assets (NPAs) up to Rs. 50 crore till September 2018.

**Comfortable capitalisation profile on equity infusion by new shareholders** – Arpwood Partners along with its investors (Clermont Group) infused Rs. 845 crore upfront into the company. This, along with the non-convertible debenture borrowings of Rs. 400 crore, helped the company in acquiring the retail assets worth ~Rs. 807 crore from KFSL. SBFC's gearing stood at a comfortable level of ~0.86 times as of June 2018, with an adjusted net worth of Rs. 5967 crore (adjusted for goodwill of Rs. 130 crore) and capital adequacy of 55%. In FY2020, another Rs. 100 crore will be infused by Arpwood Partners, on conversion of share warrants. Supported by the upfront capital infusion, the company's capital structure is expected to be adequate to meet its growth targets for the next three years.

**Senior management team with experience in retail lending business; collection framework revamped** – SBFC has on-boarded Mr. Aseem Dhru (as Chief Executive Officer), Mr. Mahesh Dayani (as Chief Business Officer) and other officials with a proven track record in the banking/NBFC sector. The senior management team is supported by a strong zonal leadership team, with experience ranging from 11 to 18 years, that has been on-boarded over the last 12 months for business, credit and collection verticals. The company would leverage their experience in ramping up the retail loan book, maintaining strong underwriting practices and for technology adoption. The company has also acquired KFSL's junior and middle management team along with its various branches. SBFC has eliminated middle agencies for business sourcing and collections. The in-house debt management policy is expected to improve the monitoring of accounts, enable the triggering of pre-emptive measures and allow better follow-up of payment delays. It also educates customers about the implications of defaults on their credit history and other measures like loan recall, litigation, etc.

## Credit challenges

**Ability to manage asset quality as portfolio seasons** – SBFC’s asset quality, at the time of the closing of the deal, was healthy with the company largely acquiring only performing loan assets. However, the quality of the acquired book, which is also being run-down, has since deteriorated (gross NPA level<sup>2</sup> of 5.6% as of June 30, 2018). The first loss cover, up to Rs. 50 crore, which is available till September 28, 2018 effectively protects the company from any loss up to that level. Though still early, the freshly originated loans under the ME, SME and personal loan segments have nil delinquencies as of date. However, LAG, which has almost been churned completely over the last 12 months, has slightly higher delinquencies. The adequate security cover, the lender’s focus on margin call and the liquid nature of the collateral, however, minimises the credit risk to an extent. As the company ramps up its loan book and the existing loan book seasons, its ability to maintain the asset quality would remain a key rating monitorable. The ability to maintain strong underwriting practices in segments like ME loans would be a critical driver of the overall asset quality.

**Ability to improve profitability by borrowing at attractive cost of funds and containing operating expenses** – With the company expecting to ramp up its loan book going forward, its ability to borrow funds from banks at competitive rates would be important for improving its net interest margins. While the amortisation of goodwill, post the acquisition of KFSL’s retail assets, has dented the company’s profitability in FY2018, it is also expected to result in a net loss in FY2019. Pre-goodwill amortisation, the company earned a profit before tax of Rs. 2.05 crore in FY2018 and Rs. 9.98 crore in Q1 FY2019. SBFC’s ability to contain operating expenses, as it scales up its operations, would also be a key rating monitorable. The goodwill is expected to be completely amortised by the end of the current fiscal.

**Analytical approach:** For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

### Links to applicable criteria:

[ICRA’s Credit Rating Methodology for Non-Banking Finance Companies](#)

## About the company

Small Business FinCredit India Private Limited (SBFC) is a non-banking finance company that provides loans against property, gold loans and personal loans. Backed by Lyra Partners and Arpwood Partners Investment Advisors LLP, the company commenced operations in September 2017 after acquiring the performing loans in KFSL’s retail portfolio. At the time of closing the deal in September 2017, the company had a net worth of ~Rs. 590 crore (net of goodwill) and a loan book of Rs. 807 crore, which stand at Rs. 597 crore and Rs. 871 crore, respectively, as on June 30, 2018. Following the acquisition, SBFC focussed on building adequate systems and processes and on the on-boarding of experienced professionals in the management team before rebooting the lending business. It leverages technology and analytics to provide customers with easy access to credit and to assess their credit behaviour through their digital footprints. During Q1 FY2019, SBFC reported a net loss of Rs. 33.30 crore on total assets of Rs. 1,311.94 crore compared to a net loss of Rs. 84.75 crore on total assets of Rs. 1,303.29 crore in FY2018.

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<sup>2</sup> Gross NPA / Gross advances

## Key financial indicators (Audited)

	FY2018	Q1 FY2019
Net interest income	43.46	24.49
Operating income	53.55	31.42
Profit before tax	(84.75)	(33.30)
Profit after tax	(84.75)	(33.30)
Total portfolio	781.39	870.84
Net worth	760.22	726.91
Goodwill	173.59	130.31
Total assets	1,303.29	1,311.94
% Tier 1	55.46%	54.53%
% CRAR	55.95%	55.06%
Gearing (adjusted)	0.83	0.86
% Net profit/average total assets (annualised)	(12.91%)	(10.19%)
% Return on net worth	(22.22%)	(17.91%)
% Gross NPAs	1.41%	3.49%
% Net NPAs	1.17%	2.89%
Net NPA/Net worth	1.20%	3.44%

**Status of non-cooperation with previous CRA: Not applicable**

**Any other information: None**

## Rating history for last three years:

Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Sep-18	FY2018 Dec-17	Sep-17	FY2017	FY2016
1 Bank Lines Programme	Long Term	200.00	50.00	[ICRA]A (stable)	[ICRA]A (stable)	-	-	-
2 Non-convertible Debenture programme	Long Term	400.00	400.00	[ICRA]A (stable)	[ICRA]A (stable)	[ICRA]A (stable)	-	-

## Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://www.icra.in)

## Annexure-1: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE423Y07013	Non-convertible Debenture	28-Sep-17	9.40%	28-Sep-20	400.00	[ICRA]A (stable)
NA	Long-term Bank Lines	Sep-17	NA	Sep-22	50.00	[ICRA]A (stable)
NA	Long-term Bank Lines - Proposed	*	NA	*	150.00	[ICRA]A (stable)

Source: Small Business FinCredit India Private Limited

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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](http://www.icra.in)

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