October 16, 2020

# SBFC Finance Private Limited: Rating reaffirmed

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Long-term fund-based bank lines | 2,865.60 | 2,865.60 | [ICRA]A(Stable); reaffirmed |
| Non-convertible debentures | 400 | 0.00 | [ICRA]A(Stable); reaffirmed and withdrawn |
| Non-convertible debentures | 50 | 50.00 | [ICRA]A(Stable); reaffirmed |
| Non-convertible debentures | 0 | 200.00 | [ICRA]A(Stable); assigned |
| **Total** | **3,315.60** | **3,115.60** | |

**Instrument details are provided in Annexure-1*

## Rationale

ICRA has reaffirmed the rating for SBFC Finance Private Limited's (SBFC) instruments at [ICRA]A. The outlook remains Stable. The rating factors in the integration of the collection process for the pass-through certificate (PTC) of Dewan Housing Finance Corporation Limited (DHFL) and the collection efficiency on the same. ICRA also notes the induction of SBFC's senior management team with significant experience in the retail lending business, post the acquisition of the lending business from Karvy Financial Services (KFSL). ICRA also notes the revamped risk management systems and processes and the company's efforts to source leads and collect payments in-house within the indicated timelines.

Moreover, ICRA notes the acquisition of a loan pool from DHFL, by way of a PTC transaction, which more than tripled the assets under management (AUM) in June 2019. The transaction was fully funded by long-term bank lines at competitive rates, which implies minimal impact on the company's asset-liability management profile and controlled cost of borrowings. SBFC has strengthened its collections team to manage the DHFL pool and was able to handle the operational issues post the acquisition of this pool. With good loan collections, regular repayments and foreclosures on the DHFL pool, over-collateralisation of the pool has increased and provides comfort. SBFC also provides loan management services (LMS) wherein it acts as a collections service provider for a special purpose vehicle (SPV), which renders adequate control over the collection of payments. This line of business has a very high operating margin and diversifies the revenue stream.

As on June 30, 2020, the KFSL portfolio had a gross non-performing assets (GNPA) ratio of 4.69%. SBFC's liquidity position is adequate, led by the cash and liquid investments on its books for meeting the debt repayments in the near term, the long-term nature of the borrowings and the equity infusions by the promoters, thereby providing comfort. The rating is constrained by the relatively lower vintage of the loans originated by SBFC, the relatively lower ability of the end borrowers to withstand local economic shocks, and the company's ability to ramp up its profitability on a sustained basis along with its operations.

The Covid-19-related lockdown led to a near-complete freeze on economic activities in April and May 2020. This would severely impact the repayment capacity of the unorganised sector, which forms the bulk of SBFC's customer base. SBFC's ability to maintain the collection efficiency at the pre-Covid levels and grow its loan book amid a tougher operating environment will remain a key monitorable.

ICRA has withdrawn the rating assigned to Rs. 400 crore Non-convertible debentures programme as it has been fully repaid. The rating withdrawal is in accordance with ICRA's policy on the withdrawal and suspension of credit ratings.

## Key rating drivers and their description

## Credit strengths

**Retail ME book; relatively low average ticket size and LTV with adequate seasoning** – As of June 2020, the loan book originated by SBFC and the portfolios acquired from KFSL and DHFL formed 39%, 7% and 54%, respectively, of the portfolio. Around 71% of the ME+SME portfolio has a loan-to-value (LTV) of less than below 60 and 61% of the portfolio has a ticket size of less than Rs. 25 lakh. Disbursements of high ticket size ME (ticket size above Rs. 50 lakh) and SME loans have stopped. The seasoning on the acquired portfolios from KFSL (except loan against gold( LAG)) and DHFL is around 64 months and 36 months, respectively. These factors impart adequate granularity to the portfolio. As of June 2020, over-collateralisation available on the Series A PTCs of Rs. 1,800.3 crore held by SBFC has increased to 33%[1] (over-collaterasation is available by way of collections on Series B PTCs of Rs. 591.4 crore). This provides comfort as any shortfall in collections from Series A PTCs can be recovered from the collections from Series B PTCs. The funds from Series B PTCs will be transferred to DHFL only after all the regulatory dues and collection fees have been recovered and the rundown of Series A PTCs is complete.

**Senior management team with experience in retail lending business; collection framework revamped** – SBFC has on-boarded a senior management team comprising officials with a proven track record in the banking/non-banking financial company (NBFC) sector. The senior management team is supported by a zonal leadership team with experience ranging from 11 to 18 years. This team was on-boarded over the last 24 months for the business, credit, finance and collection verticals. SBFC will leverage the team's experience in ramping up the retail loan book, maintaining adequate underwriting practices and for technology adoption. It has also added KFSL's junior and middle management team along with the various branches of KFSL. The in-house debt management policy is expected to improve the monitoring of accounts, enable the triggering of pre-emptive measures and allow the better follow-up of payment delays.

## Credit challenges

**Ability to manage asset quality as portfolio seasons** – SBFC's asset quality, at the time of acquisition of KFSL book (the deal) in 2017, was healthy with the company largely acquiring only the performing loan assets. In March 2019, the first loss cover, up to Rs. 44.2 crore, was utilised and settled by KFSL. Although the initial bad loans on the acquired book were settled in this transaction, the asset quality of the remaining loans in the acquired book (about Rs. 248 crore as on June 30, 2020) weakened in FY2021 on seasoning. The freshly originated loans under the ME loan segment are also witnessing higher slippages. These are attributable to the underlying stress in the operating

[1] *POS of series B PTCs / POS of series A PTCs*

environment of the borrowers. Delinquencies have increased across the days past due (dpd) buckets for unsecured personal loans but are still at a comfortable level. As of March 2020, around 33% of the outstanding loans were towards government employees while 22% of the loans are covered by SIDBI under credit insurance. Delinquencies (30+ and 60+ dpd buckets) in the LAG segment have improved as of June 2020 compared to December 2019. The adequate security cover, the lender's focus on margin calls and the liquid nature of the collateral minimise the credit risk to an extent. The pool acquired from DHFL, which forms more than half of the overall portfolio, has a loss cover of up to 33%[1], which can be recovered from the Series B PTCs held by DHFL. Hence, SBFC's losses on account of the acquired pool are expected to be limited. The monthly collection efficiency on this pool of assets exceeded 98% during June 2019 – March 2020. The company's solvency[2] level was at 3.79% in March 2020 increased from 0.73% in March 2019 due to higher NPAs in FY2020. In June 2020, the solvency decreased to 2.59% due to the Rs. 100-crore equity infusion by the promoters.

The Covid-19-related lockdown resulted in a near-complete freeze on economic activities in April and May 2020. This would severely impact the repayment capacity of the unorganised sector, which forms the bulk of the customer base for SBFC. The company has been in contact with a large section of its customer base and has educated them on the moratorium and its effect. Around 37% of the customers (portfolio excluding the DHFL pool) had availed the first moratorium in April 2020, which decreased to 16% in August 2020. About 5% of these customers had not paid a single EMI as of August end. SBFC's collection efficiency (excluding prepayment and foreclosures) also improved to ~80% in August 2020 from ~64% in April 2020. ICRA notes that the pandemic will affect the business growth plans for FY2021 and elevate the credit costs. The collection efficiency in Q3 and Q4 would be a key monitorable.

**Ability to improve profitability while maintaining the credit costs** – SBFC reported a profit of Rs. 35 crore in FY2020 compared to Rs. 24 crore in FY2019 though the return on average total assets declined to 1.2% in FY2020 from 1.5% in FY2019 as the size of the portfolio increased multifold in FY2020. The higher credit costs (including a Rs. 15-crore Covid-19 provision) and borrowing costs in FY2020 have affected the profitability . SBFC reported a profit after tax (PAT) of Rs. 24 crore in Q1 FY2021, a significant improvement due to the fee income from the LMS business, though the company made a provision of Rs. 1 crore. Going forward, SBFC's ability to improve its return on managed assets while growing its operations will be a key point to monitor.

**Adequate capitalisation with relatively higher leverage** – Arpwood Partners Investment Advisors LLP and Lyra Partners infused Rs. 845 crore upfront in the company. This, along with the non-convertible debenture borrowings of Rs. 400 crore, helped SBFC acquire KFSL's retail assets worth ~Rs. 807 crore. In Q1 FY2020, the shares held by Lyra Partners were transferred to SBFC Holdings, which are both affiliates of the same investor group. SBFC's gearing (adjusted for goodwill of Rs. 260.39 crore) increased to 4.1 times in March 2020 from 1.4 times in March 2019, while the capital adequacy fell to 21.89% in March 2020 from 44.81% in March 2019. This was on account of the long-term borrowings that were used to finance the acquisition of the portfolio from DHFL. In June 2020, the company raised Rs. 100 crore, which improved its capital adequacy and gearing (26.52% and 3.5 times, respectively). ICRA notes that the current gearing level would increase once the company start growing its AUM. ICRA notes the promoters' commitment to maintain adequate capitalisation, which is necessary to support the envisaged growth.

---

[2] *Net NPA / Adjusted Net worth*

**Modest credit profile of target customer segment** – SBFC predominantly provides small-to-medium-size ticket loans to self-employed borrowers except for unsecured personal loans where around 33% of the borrowers were government employees. Considering the borrowers' business and income profiles, their credit profiles are expected to be modest and vulnerable to income shocks induced by events such as the Covid-19 pandemic. However, these risks are mitigated to an extent by the company's prudent underwriting norms. Most (93%) of the ME + SME loans are backed by self-occupied (residential or commercial) properties.

## Liquidity position: Adequate

SBFC's liquidity position is adequate. As on August 31, 2020, the company had Rs. 698 crore of cash and liquid investments, which is sufficient to cover the near-term debt obligations of Rs. 697 crore (principal + interest) till December 2020.

## Rating sensitivities

**Positive triggers** – ICRA could upgrade the rating if the company shows a track record of profitable growth with a return on managed assets of more than 3% on a sustained basis while improving the asset quality.

**Negative triggers** – Pressure on SBFC's rating could arise if there is a continued deterioration in the asset quality with the 90+dpd increasing beyond 5.0% (on loan book) or an increase in the adjusted gearing to over 5 times on a sustained basis.

## Analytical approach

| Analytical Approach | Comments |
|---|---|
| Applicable Rating Methodologies | ICRA's Credit Rating Methodology for Non-Banking Finance Companies<br>ICRA's Policy on Withdrawal and Suspension of Credit Rating |
| Parent/Group Support | Not applicable |
| Consolidation/Standalone | The rating is based on the standalone financial statements of the issuer |

## About the company

SBFC Finance Private Limited (SBFC) is a non-banking finance company that provides loans against property, gold loans and personal loans. Backed by the Clermont Group and the Arpwood Group, the company commenced operations in September 2017 after acquiring the performing loans in KFSL's retail portfolio. 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 footprint. In June 2019, the company acquired a pool of Rs. 2,365.6 crore via a PTC transaction. The total pool in the structure was Rs. 2,957.02 crore, of which Series A PTCs of Rs. 2,365.6 crore were issued to SBFC, wholly financed by long-term borrowings. DHFL holds the Series B PTCs of the remaining amount of Rs. 591.4 crore (20% of Series A PTCs; in line with the RBI's guidelines pertaining to minimum retention).

SBFC reported a PAT of Rs. 24 crore on total assets of Rs. 4,342 crore in Q1 FY2021 compared to a PAT of Rs. 4 crore on total assets of Rs. 4,141 crore in Q1 FY2020. In FY2020, the company posted a PAT of Rs. 35 crore on total assets of Rs. 4,208 crore compared to a PAT of Rs. 24 crore on total assets of Rs. 1,793 crore in FY2019.

## Key financial indicators

| Parameters | FY2018 | FY2019 | FY2020 | Q1 FY2021 |
|---|---|---|---|---|
| Net interest income | 58 | 124 | 176 | 54 |
| Operating income | 58 | 126 | 200 | 59 |
| Profit before tax | 5 | 35 | 59 | 33 |
| Profit after tax | 3 | 24 | 35 | 24 |
| | | | | |
| Total AUM | 781 | 1,153 | 1,548 | 1,530 |
| Net worth | 848 | 880 | 1,012 | 1,138 |
| Goodwill | 260 | 260 | 260 | 260 |
| Total assets | 1,382 | 1,793 | 4,208 | 4,342 |
| | | | | |
| % Tier I | 55.46% | 44.26% | 21.36% | 26.07% |
| % CRAR | 55.95% | 44.81% | 21.89% | 26.52% |
| Gearing (adjusted)* | 0.82 | 1.43 | 4.06 | 3.51 |
| | | | | |
| % Net profit/average managed assets | 0.45% | 1.54% | 1.18% | 2.26% |
| | | | | |
| % Return on net worth | 0.74% | 2.83% | 3.74% | 8.97% |
| | | | | |
| % Gross NPAs | 1.37% | 0.44% | 2.28% | 2.24% |
| % Net NPAs | 0.40% | 0.12% | 0.71% | 0.79% |
| Net NPA/Net worth* | 1.29% | 0.59% | 3.28% | 2.59% |

*Amount in Rs. crore, *adjusted net worth i.e. (Net worth – Goodwill)*

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

## Any other information: None

## Rating history for last three years

| | Instrument | Current Rating (FY2021) | | | | Rating History for the Past 3 Years | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount Rated | Amount Outstanding* | 16-Oct-20 | FY2020 | | | FY2019 | FY2018 | |
| | | | | | | 14-Feb-20 | 29-Aug-19 | 22-Apr-19 | 28-Sep-18 | 19-Dec-17 | 15-Sep-17 |
| 1 | Bank Lines Programme | Long Term | 2,865.60 | 2,775.60 | [ICRA]A (stable); reaffirmed | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | - |
| 2 | Non-convertible Debenture Programme | Long Term | 400 | 0 | [ICRA]A (stable); withdrawn | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) |
| 3 | Non-convertible Debenture Programme | Long Term | 50 | 50 | [ICRA]A (stable); reaffirmed | [ICRA]A (stable) | - | - | - | - | - |
| 4 | Non-convertible Debenture Programme | Long Term | 200 | 100 | [ICRA]A (stable); assigned | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) | [ICRA]A (stable) |

**As on September 30, 2020; Source: Company; Amount in Rs. crore*

## 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 | Instrument Name | Date of Issuance / Sanction | Coupon Rate | Maturity Date | Amount Rated (Rs. crore) | Current Rating and Outlook |
|---|---|---|---|---|---|---|
| INE423Y07039 | Non-convertible Debentures | 11-Aug-20 | 9.25% | 11-Feb-22 | 50.00 | [ICRA]A (stable) |
| INE423Y07021 | Non-convertible Debentures | 03-Aug-20 | 9.25% | 03-Feb-22 | 25.00 | [ICRA]A (stable) |
| INE423Y07047 | Non-convertible Debentures | 17-Aug-20 | 9.30% | 17-Feb-22 | 25.00 | [ICRA]A (stable) |
| INE423Y07054 | Non-convertible Debentures | 14-Sep-20 | 9.25% | 14-Mar-22 | 50.00 | [ICRA]A (stable) |
| - | Non-convertible Debentures* | - | - | - | 100.00 | [ICRA]A (stable) |
| NA | Long-term Bank Lines | 2018-19 | NA | 2021-27 | 2,775.60 | [ICRA]A (stable) |
| NA | Long-term Bank Lines* | - | - | - | 90.00 | [ICRA]A (stable) |

**Proposed; Source: Company*

## Analyst Contacts


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

**Sahil Udani**
+91 22 6114 3429
sahil.udani@icraindia.com

**Sudam Shingade**
+91 22 6114 3425
sudam.shingade@icraindia.com

**Mayank Chheda**
+91 22 6114 3413
mayank.chheda@icraindia.com


## Relationship Contact


**Jayanta Chatterjee**
+91 80 4332 6401
jayantac@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


**Corporate Office**
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

**Registered Office**
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

**Branches**

| | |
|---|---|
| Mumbai | + (91 22) 24331046/53/62/74/86/87 |
| Chennai | + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294, |
| Kolkata | + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008, |
| Bangalore | + (91 80) 2559 7401/4049 |
| Ahmedabad | + (91 79) 2658 4924/5049/2008 |
| Hyderabad | + (91 40) 2373 5061/7251 |
| Pune | + (91 20) 2556 0194/ 6606 9999 |