September 26, 2023

Electronica Finance Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible debentures	33.75	33.75	[ICRA]A- (Stable); reaffirmed
Total	**33.75**	**33.75**	

**Instrument details are provided in Annexure I*

Rationale

The rating factors in Electronica Finance Limited's (EFL) established track record of more than three decades in the asset financing business and its experienced management team. The company has been able to scale up its portfolio consistently (5-year CAGR[1] of 21% till March 31, 2023) despite the disruptions caused by the Covid-19 pandemic and it reported assets under management (AUM) of Rs. 3,026 crore as on June 30, 2023 (Rs. 2,906 crore as on March 31, 2023). The growth has been aided by EFL's gradual expansion in the micro loan against property (LAP) segment and the rooftop solar loan segment. The share of these segments increased collectively to 23% as on June 30, 2023 from 3% as on March 31, 2020.

The company has a diversified borrowing profile comprising funding relationships with more than 30 lenders as on June 30, 2023 with a good mix of private sector banks, public sector banks, non-banking financial companies (NBFCs) and financial institutions (FIs). However, the managed gearing[2] has been increasing and was reported at 5.9 times as on March 31, 2023 (4.6 times as on March 31, 2022) due to the scaling up of the portfolio. In ICRA's opinion, EFL would require an equity infusion in the near term to support its envisaged growth while maintaining a prudent capitalisation profile. ICRA notes that the company is in the process of raising equity capital.

The rating is constrained by the inherent risks associated with the target borrower segment of small and medium industrial units that are susceptible to economic shocks. This can lead to asset quality challenges for the portfolio. However, with strong underwriting norms, the company has been able to navigate through various macro-economic events in the past, including the pandemic, and its asset quality indicators improved in FY2023 supported by recoveries and write-offs. Nevertheless, its ability to keep its asset quality under control, especially in the relatively newer product segments, namely micro LAP and rooftop solar loans, would be important. The rating also remains constrained by the company's moderate, albeit gradually improving, earnings profile. EFL's ability to improve its operating efficiency while managing the credit costs as its scales up the portfolio will be important from a credit perspective.

The Stable outlook on the [ICRA]A- rating reflects ICRA's opinion that EFL will continue to benefit from its experienced management team, adequate systems and processes and diversified borrowing profile, while increasing its scale of operations.

Key rating drivers and their description

Credit strengths

Established track record of operations in asset finance – EFL started its operations in machine financing in 1990, given the background of its parent group of equipment manufacturers. It draws competitive advantage, in terms of critical know-how of machine usage and resale, by leveraging the operational and management experience of its promoter group entities. Moreover, the company takes higher exposure only in case of repeat borrowers with a successful repayment track record or

[1] Compound annual growth rate

[2] Managed gearing = (Total borrowings + Off-book loan assets + Cash collateral from customers towards off-book loan assets)/(Net worth)

in case of adequate group entity comfort and/or with sufficient collateral to support the loan. Supported by the diverse experience of its senior management and its track record of over 30 years, EFL was managing an AUM of Rs. 2,906 crore (Rs. 3,026 crore as on June 30, 2023) spread across 16 states as on March 31, 2023.

Comfortable asset quality – Despite the pandemic, EFL witnessed an improvement in its asset quality indicators over the last three years. It reported gross non-performing advances (NPAs) of 1.7% as on June 30, 2023 (1.1% as on March 31, 2023) compared to 3.8% as on March 31, 2020. ICRA draws comfort from EFL's established track record in the asset financing business with demonstrated ability to manage the asset quality over cycles. Further, the portfolio remains granular in nature with the company catering to more than 15,000 clients with the top 20 borrowers comprising 3% of the total portfolio outstanding as on March 31, 2023 (5% as on March 31, 2022). Nevertheless, the company's ability to keep its asset quality under control while managing growth, especially in the relatively newer product segments, namely micro LAP and rooftop solar loans, would be important.

Fairly diversified borrowing profile – The company has a fairly diversified borrowing profile comprising funding relationships with more than 30 lenders as on June 30, 2023 and a good mix of private sector banks, public sector banks, NBFCs and FIs. The borrowing profile comprised bank facilities (61%), non-convertible debentures (NCDs; 6%), term loans from NBFCs/FIs (5%), and an off-book loan portfolio (19%) as on March 31, 2023. ICRA notes the company's plan to further diversify its borrowing profile while raising funds through NCDs from various investors, including funds from development finance institutions. EFL also takes a cash collateral as a security deposit from its clients (8%). Cash collateral from customers is a source of low-cost funds, wherein the company provides a loyalty bonus to its borrowers, contingent on meeting certain conditions. EFL raised Rs. 1,131 crore of debt funds in FY2023 from more than 20 different lenders followed by Rs. 219 crore of debt funds in Q1 FY2024 and continues to maintain a healthy pipeline of funds to support its growth plans.

Credit challenges

Moderate profitability profile – The net interest margin improved to 7.7% of average managed assets (AMA) in FY2023 from 6.3% in FY2022 owing to the improvement in yields with the increasing share of the relatively higher yielding micro-LAP portfolio. However, operating expenses increased to 5.1% of AMA in FY2023 from 4.4% in FY2022 due to increase in administrative and employee expenses, as the company increased its employee base and strengthened its senior management team considering the growth plans. EFL continues to open new branches and hire personnel to support its envisaged growth plans. Credit costs were low at 0.8% of AMA in FY2023 compared to 0.5% in FY2022, given the overall comfortable asset quality indicators. The company reported a net profit of Rs. 42 crore (Rs. 11 crore in Q1 FY2024), translating into a return of 1.8% on AMA and 12.2% on average net worth in FY2023 (Rs. 29 crore, 1.7% and 9.4%, respectively, in FY2022). EFL's ability to improve its operating efficiency while managing the credit costs as its scales up the portfolio will be important from a credit perspective.

Increasing leverage, given high pace of growth – Given the high pace of growth, the managed gearing has been increasing and stood at 5.9 times as on March 31, 2023 (5.6 times as on June 30, 2023) compared to 4.6 times as on March 31, 2022. The capital adequacy remained adequate at 19.0% as on June 30, 2023 against the regulatory requirement of 15%. ICRA takes note of the company's plans to raise equity capital in the near term, which would improve its capitalisation profile. However, higher-than-anticipated growth and/or a delay in raising equity could impact its capitalisation profile in the interim and shall remain a monitorable.

Modest credit profile of target customer segment – The portfolio is prone to asset quality challenges on account of lending to small and medium industrial units that are susceptible to economic shocks. However, with strong underwriting norms, the company has been able to navigate through various macro-economic events in the past, including the pandemic. EFL has a stringent appraisal and risk management framework, which includes multiple site visits, know your customer (KYC) verification, credit bureau checks and financial due diligence wherein the focus remains on assessing the debt repaying ability of the borrower based on his existing scale of business. While the relationship managers remain responsible for the respective accounts, the company has a separate collection team for follow-ups/personal visits in case of delays.

Liquidity position: Adequate

EFL's liquidity profile is adequate given the on-book liquidity of Rs. 115 crore as on June 30, 2023, expected inflows from advances and the availability of sanctioned unutilised lines. As per the structural liquidity statement as on June 30, 2023, the company had scheduled inflows of Rs. 771 crore against scheduled outflows of Rs. 675 crore till June 30, 2024. The company maintains a healthy debt pipeline comprising sanctions for term loans, direct assignment and co-lending arrangements. However, given its growth plans, EFL would require additional funding to support the projected business growth.

Rating sensitivities

Positive factors – A sustainable increase in the scale of operations, while maintaining the asset quality, and an improvement in the capitalisation and earnings profile could positively impact the rating.

Negative factors – Pressure on the company's rating could arise if there is a deterioration in the asset quality, which could affect its profitability. The weakening of the capitalisation profile with the managed gearing exceeding 6 times on a sustained basis or a stretch in the liquidity could also exert pressure on the rating.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Non-Banking Finance Companies
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

About the company

Electronica Finance Limited (EFL), formerly known as Electronica Leasing and Finance Limited, is a non-banking financial company (NBFC) incorporated in 1990 and is a part of SRP Electronica Group (the Group). At present, EFL provides financial assistance to small-and-medium-sized industrial units (mostly tier II, tier III and tier IV ancillary units) engaged mainly in the engineering, auto ancillary and plastic industries. The company reported an AUM of Rs. 3,026 crore (Rs. 2,906 crore as on March 31, 2023) spread across 17 states/Union Territories as on June 30, 2023.

The origin of SRP Electronica Group goes back to a manufacturing company started by a group of first-generation technocrats. With the experience of starting a new business also came the realisation about the challenges, especially financing, that a typical small and medium-sized enterprise (SME) faces. Given its manufacturing background and understanding of machines and engineering equipment, EFL had a leverage in starting machine financing, which was a pioneering effort. This understanding was also used to start other innovative services like doorstep finance and assessment-based financing. Very soon, EFL started machine financing of other manufacturers in the machine tool as well as other industries. EFL's products, services and last mile connectivity were also recognised by Small Industries Development Bank of India (SIDBI), which resulted in a partnership of 15+ years.

Key financial indicators (audited)

Electronica Finance Limited	FY2021	FY2022	FY2023	Q1 FY2024*
As per	**Ind-AS**	**Ind-AS**	**Ind-AS**	**Ind-AS**
Total income	172	220	327	100
Profit after tax	22	29	42	11
Net worth (including CCPS)	293	321	364	375
Gross loan portfolio	1,591	1,990	2,906	3,026
Total managed assets	1,414	1,924	2,667	2,711
Return on average managed assets	1.7%	1.7%	1.8%	1.6%
Return on average net worth	7.9%	9.4%	12.2%	11.8%
Gearing (including cash collateral as borrowings; times)	2.5	3.4	4.8	4.5
Managed gearing (times)	3.5	4.6	5.9	5.6

Electronica Finance Limited	FY2021	FY2022	FY2023	Q1 FY2024*
As per	Ind-AS	Ind-AS	Ind-AS	Ind-AS
Gross stage 3 assets	2.8%	2.6%	1.1%	1.7%
Net stage 3 assets	1.3%	1.3%	0.6%	0.9%
Solvency (Net stage 3 assets /Net worth)	4.2%	5.2%	3.2%	5.2%
Capital to risk weighted assets ratio	24.2%	21.9%	19.2%	19.0%
Tier I capital to risk weighted assets ratio	23.2%	20.6%	16.9%	16.8%

*Total managed assets = (Total assets + Impairment allowance + Off-book loan assets); Managed gearing = (Total borrowings + Off-book loan assets + Cash collateral from customers towards off-book loan assets)/(Net worth); Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore; * Unaudited*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Aug-31-2023* (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021
					Sep-26-2023	Sep-27-2022	Sep-28-2021	Aug-09-2021	Aug-10-2020
1	Non-convertible debt programme	Long term	33.75	33.75	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-	-
2	Subordinated debt programme	Long term	-	-	-	[ICRA]A- (Stable); withdrawn	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]BBB+ (Positive)

**Source: Company*

Complexity level of the rated instruments

Instrument	Complexity Indicator
Non-convertible debentures	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 Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE612U07068	Non-convertible debentures	Sep-27-2021	10.30%	Mar-13-2026	33.75	[ICRA]A- (Stable)

Source: Company

Annexure II: List of entities considered for consolidated analysis – Not applicable

ICRA

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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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