February 26, 2025

Fedbank Financial Services Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous rated amount (Rs. crore)	Current rated amount (Rs. crore)	Rating action
Commercial paper programme	1,000.00	1,000.00	[ICRA]A1+; reaffirmed
Total	**1,000.00**	**1,000.00**	

**Instrument details are provided in Annexure I*

Rationale

The rating action factors in the strong parentage of Fedbank Financial Services Limited (FFSL) with Federal Bank Limited (FBL) holding a 61.00% stake in the company. FFSL is expected to remain FBL's subsidiary and shall continue to draw managerial, operational and financial support from the bank, when required. The rating factors in FFSL's comfortable capitalisation profile with a gearing[1] of 4.0 times and a capital-to-risk weighted assets ratio (CRAR) of 21.6% as of December 2024 vis-à-vis 3.7 times and 23.5%, respectively, as of March 2024.

The rating also considers the decline in FFSL's profitability in 9M FY2025 due to the significant increase in credit costs. ICRA notes that the company has faced an increase in delinquencies recently, especially in the business loans, housing loans and small-ticket loan against property (LAP) segments, which led to higher provisioning and credit costs in the current fiscal. FFSL is expected to go slow on disbursements in these segments in the near term as the asset quality is brought under control.

FFSL's product mix is fairly diversified, comprising gold loans, medium-ticket LAP, small-ticket LAP, unsecured business loans, and housing loans. The company's assets under management (AUM) increased at a compound annual growth rate (CAGR) of 33% during March 2020 to March 2024, supported by branch additions. FFSL caters to customers with moderate credit profiles, mostly self-employed non-professional borrowers. ICRA notes that the portfolio seasoning is low, especially in the long-tenured product segments.

Key rating drivers and their description

Credit strengths

Strong parentage with Federal Bank holding a 61% stake – FFSL was promoted by FBL in 1995 and is a subsidiary of the bank, which held 61.00% as of December 2024 (61.6% as of March 2024). FBL is expected to maintain its majority stake in the company over the medium term. Further, FFSL derives benefits from the shared brand name and draws managerial and operational support from the bank. The Managing Director (MD) & Chief Executive Officer (CEO) as well as an executive director of FBL are on FFSL's board. The company is also engaged in distribution activities for the parent, for which it earns fee income.

FFSL has received financial support from FBL in the form of regular capital infusions (Rs. 471 crore since inception). FBL also provides credit lines {working capital facilities, term loans and non-convertible debentures (NCDs)}; the outstanding amount was Rs. 903.3 crore (9.3% of the overall borrowings) as of December 2024.

Comfortable capitalisation profile – FFSL's capital profile is comfortable, with a gearing of 4.0 times and a CRAR of 21.6% as of December 2024 (3.7 times and 23.5%, respectively, as of March 2024). Over the last few years, the company has received

[1] *Managed gearing was 5.4 times as of December 2024 vis-à-vis 4.7 times as of March 2024*

regular capital infusions, including the latest via its initial public offering (IPO) on November 30, 2023, which has helped it maintain strong growth. ICRA expects FFSL to operate with a gearing of less than 5.0[2] times over the medium term.

Credit challenges

Moderate portfolio seasoning and borrower profile – FFSL's AUM increased at a robust CAGR of 40.4% over the past two years to Rs. 12,192 crore as of March 2024 (Rs. 6,187 crore as of March 2022) and further to Rs. 14,922 crore as of December 2024. The AUM comprises gold loans (35%), LAP (27%), small/medium-ticket LAP (18%), business loans (13%), housing loans (6%) and other loans (1%). Over the last few years, FFSL has increased portfolio diversification by foraying into retail products like housing loans, personal loans, and unsecured business loans. Further, in the LAP segment, it has forayed into small-ticket LAP and lowered the average ticket size for medium-ticket LAP. The mix between the secured and unsecured portfolio was ~87:13 as of December 2024. In the near term, the company is expected to increase its focus on the secured retail segments, viz. mortgage and gold loans. Consequently, the share of the unsecured portfolio is expected to decline.

However, ICRA notes that the portfolio seasoning is low, especially for long-tenured product segments such as small-ticket LAP, housing finance, business loans and personal loans, which accounted for 24.2% of the AUM as of December 2024. FFSL typically caters to borrowers with a moderate credit profile, mostly self-employed non-professional borrowers in urban and semi-urban locations. Around 15% of the portfolio, as of December 2024, was to borrowers with a credit bureau score of less than 700. The company faced an increase in delinquencies in 9M FY2025, especially in the business loans, housing loans and small-ticket LAP segments. It is expected to go slow on disbursements in these segments in the near term while the asset quality is brought under control. ICRA notes that the company increased its stage 3 provision coverage to 45.2% as of December 2024 from 19.9% as of March 2024. Further, it has created additional management overlays, resulting in the overall provision cover increasing to 2.2% of the loan book (on-balance sheet; b/s) as of December 2024 from 1.2% as of March 2024.

Higher credit costs impacted profitability in 9M FY2025 – FFSL's profitability has witnessed a decline in the current fiscal, with its return on managed assets (RoMA) reducing to 1.4% in 9M FY2025 from 2.1% in FY2024 due to higher credit costs. Credit costs (provisions and write-offs/average managed assets) increased to 1.7% in 9M FY2025 from 0.6% in FY2024 on account of weaker asset quality in some of the segments such as small-ticket LAP and business loans. However, the net interest margin remained healthy at 7.1% in 9M FY2025 (6.7% in FY2024), supported by better yields and upfront gains from direct assignment transactions. In the near term, FFSL's profitability would be dependent on its ability to stabilise margins as it reduces the share of business loans and small-ticket LAP and keeps incremental credit costs under control.

Environmental and social risks

Environmental considerations: Given the service-oriented business of FFSL, its direct exposure to environmental risks/material physical climate risks is not significant. Lending institutions can be exposed to environmental risks indirectly through their portfolio of assets, though such risks are not material for FFSL as its lending operations primarily encompass gold loans and loan against property. Nevertheless, there is increasing interest from policymakers towards identifying the exposure of financing companies to carbon emissions through their financing activities. This process is, however, in an early stage and ICRA expects any adverse implications to manifest only over a longer time horizon, giving financing companies adequate time to adapt and minimise the credit implications.

Social considerations: With regard to social risks, data security and customer privacy are among the key sources of vulnerability for lending institutions as material lapses could be detrimental to their reputation and invite regulatory censure. FFSL has not faced any significant lapses in this regard. It serves the financing needs of a relatively underserved category of borrowers, which supports social inclusion and economic development.

[2] *Managed gearing of less than 6.5 times*

Liquidity position: Strong

FFSL's asset-liability maturity (ALM) profile reflects positive cumulative mismatches across the near-and-medium-term maturity buckets, supported by the favourable matching of the average tenor of the assets and liabilities and comfortable on-b/s liquidity. The company had on-b/s liquidity (cash and bank balances and investments) of Rs. 1,011.0 crore and unutilised bank lines of Rs. 1,526.5 crore, as on December 31, 2024, compared to principal repayments (including working capital demand loans) of Rs. 1,454.5 crore falling due in the subsequent three months. In addition, a sizeable share of the short-term product segment (gold loan; 35% of AUM as of December 2024) and average contractual monthly collections of Rs. 277.0 crore (between January-March 2025) support the liquidity profile. Further, ICRA notes that FFSL has good financial flexibility as it is a subsidiary of FBL. This, coupled with the high likelihood of support from the parent, augurs well for the company's liquidity profile.

Rating sensitivities

Positive factors – Not applicable

Negative factors – Pressure on the rating could arise in case of a change in the credit profile of the parent or a significant change in the shareholding or a major decline in the linkages with the parent. Pressure will also arise on a deterioration in the earnings profile and asset quality on a sustained basis.

Analytical approach

Analytical approach	Comments
Applicable rating methodologies	[Rating methodology for non-banking finance companies]
Parent/Group support	The rating factors in FFSL's strong parentage, as it is a subsidiary of FBL, and the well-demonstrated track record of support. It draws managerial, operational and financial support from FBL, as evident from the common board members, regular capital infusions, credit lines, business sourcing arrangements and shared brand name
Consolidation/Standalone	Standalone

About the company

Fedbank Financial Services Limited (FFSL) is registered with the Reserve Bank of India (RBI) as a non-deposit taking non-banking financial company (NBFC). It was incorporated in 1995 and received a licence to operate as an NBFC in 2010. FFSL is a subsidiary of Federal Bank Limited (FBL), which had held a 100% stake in the company until FY2018. In FY2019, TrueNorth LLP acquired a 17% stake in FFSL and another 9% (total 26%) in FY2020. The company concluded its IPO and offer for sale (OFS) in November 2023, which resulted in a decline in FBL and TrueNorth LLP's shareholding to 61.7% and 8.8%, respectively, as of December 2023 and 61.0% and 8.7%, respectively, as of December 2024.

The company primarily provides gold loans, LAP, business loans, personal loans, and housing loans. FFSL also engaged in sourcing loans (housing loans, auto loans, personal loans, small and medium-sized enterprise (SME) loans) for its parent. As on December 31, 2024, it had a presence in 18 states/Union Territories with a 693-branch network including 484 gold loan branches and 209 micro, small and medium enterprise (MSME) hubs. The AUM stood at Rs. 14,922 crore as on December 31, 2024 (Rs. 12,192 crore as on March 31, 2024). The operations are divided into three categories: retail lending (gold loans, LAP, business loans, personal loans, housing loans), wholesale lending (loans to NBFCs and construction loans) and distribution business (sourcing housing loans, auto loans, personal loans, SME loans for the parent company). While retail loans and wholesale loans generate interest income and fee income for the company, the distribution business contributes to its fee and commission income.

Key financial indicators

FFSL	FY2023	FY2024	9M FY2025^
Total income	1,215	1,623	1,553
PAT	180	245	154
Total managed assets	10,143	13,507	16,305
Return on managed assets	2.1%	2.1%	1.4%
Managed gearing (times)	6.1	4.7	5.4
Gross stage 3	2.0%	1.7%	1.9%
CRAR	17.9%	23.5%	21.6%

Source: Company, ICRA Research; ^B/S as per investor presentation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current (FY2025)			Chronology of rating history for the past 3 years					
	FY2025			FY2024		FY2023		FY2022	
	Type	Amount rated (Rs. crore)	Feb 26, 2025	Date	Rating	Date	Rating	Date	Rating
Commercial paper	Short term	1000.00	[ICRA]A1+	Feb 26, 2024	[ICRA]A1+	Feb 01, 2023	[ICRA]A1+	Feb 11, 2022	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity indicator
Commercial paper	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	Coupon rate	Maturity	Amount rated (Rs. crore)	Current rating and outlook
NA	**Commercial paper programme – Unutilised**	NA	NA	NA	1,000.00	[ICRA]A1+

Source: Company

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.

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