

Northern Arc Capital Limited

January 03, 2019

Summary of rated instruments

Trust Name	Instrument*	Initial Issued Amount (Rs. Crore)	Amount Outstanding as on previous rating exercise (Rs. Crore)	Amount Outstanding as on Nov-18 payouts (Rs. Crore)	Rating Action
Solstice Trust Series I 2017	PTC Series A1	101.57	38.50	26.97	Ratings reaffirmed at [ICRA]AA-(SO)
	PTC Series A2	6.85	6.85	6.85	Ratings reaffirmed at [ICRA]A+(SO)

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the ratings to PTCs issued under securitisation transaction originated by Northern Arc Capital Limited (Northern Arc). The PTCs are backed by term loan receivables originated by Northern Arc. The receivables have been assigned to the trust at par and each trust has issued PTCs backed by the same.

Rationale

The reaffirmation in the ratings is on account of high amortisation (>65%) of the Pool and PTC payouts under this transaction. The amortisation has led to a healthy build-up of the credit enhancement cover over the future PTC payouts. Also, the break-even collection efficiencies are comfortable when compared to the actual collection levels in this pool.

A summary of the performance of the pool till November 2018 collection month has been tabulated below.

Parameter	Solstice Trust Series I 2017
Number of Live underlying term loans	13
Pool Amortization (%)	65.37%
Cumulative collection efficiency (%) ¹	100.00%
Cumulative Prepayment Rate (%)	8.60%
Loss cum 90+ (% of initial pool principal) ²	0.00%
Cumulative CC utilization	0.00%
CC available (as % of balance pool)	23.10%
Principal subordination available (PTC A1) (as % of balance pool)	31.76%
Breakeven collection efficiency for - PTC Series A1	44.02%
Breakeven collection efficiency for - PTC Series A2	61.96%

¹ Cumulative collections till date / cumulative billings till date plus opening overdues

² POS on underlying term loans at 0+ dpd + overdues / Initial POS on the pool

Key rating drivers

Credit strengths

- Availability of credit enhancement in the form of First Loss Credit Enhancement (FLCE), Principal Subordination, over-collateral and EIS;
- Diversity amongst the borrower entities in terms of the varied nature of businesses, ranging from Microfinance entities to NBFCs catering to small business loans as well as consumer durable loans.
- Significant amortization of the pool leading to lower uncertainty around performance of the balance pool contracts;

Credit challenges

- Weak to moderate stand-alone credit quality of the Borrowers in long-term
- High obligor concentration of the loan contracts in the pool.

Description of key rating drivers highlighted above:

During the fresh rating exercise carried out in Sep-17, the underlying pool comprised of 16 term loans given by Northern Arc to 4 borrower entities (viz. Annapurna Finance Pvt. Ltd. (AFPL), CapFloat Financial Services Private Limited (Capital Float), Essel Finance Business Loans Ltd. (Essel), Home Credit India Finance Pvt. Ltd. (Home Credit)). The borrowers are diversified across varied nature of businesses, ranging from Microfinance entities to NBFCs catering to small business loans as well as consumer durable loans.

In the February 2018 payout month, one borrower entity (CapFloat) prepaid its entire debt obligation pertaining to this transaction. This led to faster actual amortisation of the pool as compared to the scheduled amortisation. After the August 2018 payout month, there were 7 live term loans, pertaining to the remaining three borrowers that continue to be part of the underlying pool. The same term loans were live as after November 2018 payouts. The obligor concentration of the pool is high with the top borrower constituting ~42.5% of the balance pool principal. The performance of the pool has been good with cumulative collection efficiency at 100.00% till October 2018 collection or November 2018 payouts. There has been no shortfall in collections with all the borrowers repaying the instalments on time. As on November 2018 payouts, there has not been CC utilisation in the transaction. The pool has amortised by ~65%, due to which the CC (as % of balance PTC payouts) has built up in the transaction.

The first line of support for Series A1 PTCs in the transaction is in the form of subordination of the pool principal (includes principal payable to PTC A2 and over collateralization). After PTC A1 has been fully paid, subordination of the pool principal will be available for PTC A2. An important feature of the structure in this transaction is that any collection in excess of the promised interest payouts to PTC A1 would be first utilised for payment of scheduled principal of PTC A1 and then for expected interest payouts to PTC A2. After PTC A1 is completely amortised the same would be utilised for payment of promised interest and scheduled principal to PTC A2.

Further credit support in the transaction is available through First Loss Credit Enhancement (FLCE) equivalent to 8.00% of the initial pool principal amount (Rs. 114.13 crore). The FLCE was envisaged to be in the form of an unconditional and irrevocable bank guarantee issued by any one of the scheduled commercial banks in favour of the Trustee. However, at present, the Originator has pledged units of fixed deposits with bank rated at least AA+ in favour of the Trustee to meet the payment obligations under the FLCE. In the event of shortfall in meeting the promised PTC payouts during any month, the Trustee can utilize the FLCE to meet the shortfall. Additionally, EIS available in the structure will also provide credit enhancement support.

In the transaction, interest is promised on a monthly basis while principal is promised at the final maturity date. Thus, there has been no instance of CC utilisation in the pool. Significant amortisation, adequate credit cushion available to service future investor payouts (including downward reset of credit collateral) and consequently lower breakeven collection efficiency when compared to cumulative collection efficiency has resulted in reaffirmation for both the tranches.

ICRA will continue to monitor the performance of the transaction. Any further rating action will be based on the performance of the pool and the availability of credit enhancement relative to ICRA's expectations.

Key Rating Assumptions

ICRA's cash flow modeling for surveillance of CLO transactions involves simulation of potential losses in the pool. ICRA's rating or rating view on the entities along with the balance tenure of the underlying loans given to obligor entities has been taken into account to estimate the default probability on each of the underlying loans. Additionally, a certain degree of correlation is assumed in the performance of the various obligor entities in the pool, by virtue of being in the same sector/ sub-sector. ICRA has also taken note of the originators' track record in lending to underlying entities and the past performance of their loan portfolio. Other variables that influence the amount of credit enhancement include the servicer's credit quality, the assumption on the build-up of delinquency/loss and the transaction structure.

Additionally, the assumptions may also be adjusted to account for the current macro-economic situation as well as any industry specific factors that ICRA believes could impact the performance of the underlying loan contracts.

After making the aforementioned adjustments, the expected mean shortfall in principal collection during the balance tenure of the transaction is estimated to be about 4.5% - 6.5% (of balance pool principal), with certain variability around the same.

Liquidity Position

In the pool, only the interest amount is promised on the PTCs on a monthly basis while the principal amount is promised on the scheduled maturity date. This structural feature imparts significant liquidity in the transaction, as even a small amount of collections in the underlying pool contracts would be sufficient to meet the scheduled PTC payouts.

Additionally, there is credit collateral available in the transaction amounting to 23.10% of the balance pool principal amount. The credit collateral remaining in the transaction is sufficient to cover all the interest payouts for the entities in the trusts. Analytical approach:

Analytical Approach

The rating action is based on the performance of the pool till October 2018 (collection month), the present delinquency profile of the pool contracts, performance expected over the balance pool tenure, and the credit enhancement available in the transactions.

Analytical Approach	Comments
Applicable Rating Methodologies	Rating Methodology for Securitisation Transactions
Parent/Group Support	Not Applicable
Consolidation / Standalone	Not Applicable

About the Issuer:

Northern Arc Capital Limited (Northern Arc)

Northern Arc Capital Limited (Northern Arc), a systemically important non-banking finance company, is based out of Chennai. The company was promoted by Dvara Trust. Northern Arc has raised equity of about Rs.310 crore during FY2014-FY2018 (till date) from IFHPL and other investors. IFHPL holds about 47.88% equity in the company, while Leapfrog Financial Inclusion India II Limited (Leapfrog), FIL Capital Investments (Mauritius) (II) Limited and Standard Chartered Bank (Singapore Branch) hold 28.02%, 14.20% and 9.90%, respectively, on a fully diluted basis, as on January 2018.

The company provides diverse financing solutions to entities providing microfinance, affordable housing finance, commercial vehicle finance, agri finance, small business loans and to corporates as well. Northern Arc provides loans and other structured debt products including guarantees to its clients. It also facilitates securitisation transactions for its clients and generally invests in subordinated tranches.

In FY2018, NACL reported a consolidated net profit of Rs. 86.3 crore on a total managed asset base of Rs. 3,845.2 crore compared to a consolidated net profit of Rs. 63.8 crore on a total managed asset base of Rs. 3,037.8 crore for FY2017.

Key financial indicators (Audited)

	FY2017	FY2018
Total Income	369	475
Profit after Tax	64	86
Net Worth	502	640
Managed Portfolio	2,796	3,511
Total Managed Assets	3,038	3,845
Return on Managed Assets	2.6%	2.5%
Return on Net Worth	16.3%	15.1%
Gearing	4.7	4.5
Gross NPA%	0.03%	0.11%
Net NPA%	0.0%	0.08%
CAR%	16.9%	17.1%

Amount in Rs. crore

About the live underlying borrower entities (rated by ICRA):

Annapurna Finance Private Limited (AFPL)

Annapurna Finance Private Limited (AFPL), formerly known as Annapurna Microfinance Private Limited, is promoted by People's Forum (PF), a society registered in Odisha. PF has been engaged in various socio-economic development programmes, including microfinance, since 1990. In November 2009, PF acquired a non-banking financial company (NBFC), Gwalior Finance and Leasing Company Private Limited, which was renamed AFPL in February 2010.

AFPL largely uses the self-help group (SHG) model for lending and recently started disbursing individual loans as well. As on June 30, 2018, AFPL had a network of 451 branches spread across 199 districts in Odisha, Bihar, Chhattisgarh, Jharkhand, Madhya Pradesh, Maharashtra, Rajasthan, Assam, Meghalaya, Punjab, Tripura, West Bengal, Haryana and Gujarat. Its corporate and registered office is in Bhubaneswar, Odisha.

In Q1 FY2019, AFPL reported a net profit of Rs. 14.5 crore (Rs. 9.5 crore in FY2018) on a total managed asset base Rs. 2,486.3 crore as on June 30, 2018 (Rs. 2,378.3 crore as on March 31, 2018)

Key financial indicators (Audited)

Parameters	FY2017	FY2018	Q1FY2019 ¹
Net interest income	73.8	128.7	46.3
Profit before tax	29.0	13.8	22.0
Profit after tax	18.9	9.5	14.5
Portfolio size	1,238.6	1,919.5	2,035.2
Total assets	1,531.1	2,023.6	2,175.0
% CRAR	22.4%	17.9%	26.3%
Gearing	7.8	7.0	4.1
Gearing (including off book)	9.1	8.5	4.8
% Net profit/average total assets	1.3%	0.5%	2.4%
% Return on net worth	13.1%	4.6%	17.7%
% Gross NPAs	0.2%	3.7%	2.1%
% Net NPAs	0.0%	0.3%	0.1%
Net NPA/net worth	0.2%	2.0%	0.5%

Amount in Rs. Crore

¹Provisional

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	Initial Rated Amount (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating December 2018	Date & Rating in FY2019 September 2018	Date & Rating in FY2018 March 2018	Date & Rating in FY2018 January 2018	Date & Rating in FY2018 September 2017*
1 Solstice Trust Series I 2017	PTC Series A1	101.57	26.97	[ICRA]AA-(SO)	[ICRA]AA-(SO)	[ICRA]A+(SO)	[ICRA]A (SO)	Provisional [ICRA]A(SO)
	PTC Series A2	6.85	6.85	[ICRA]A+(SO)	[ICRA]A+(SO)	[ICRA]A (SO)	[ICRA]BBB+(SO)	Provisional [ICRA]BBB+(SO)

*Initial Rating done in Sept-17

Complexity level of the rated instrument: Highly Complex

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

Annexure-1: Instrument Details

Trust Name	Instrument Name	Date of Issuance	Coupon Rate [#]	Scheduled Maturity Date [*]	Rated Amount (Rs. crore)	Current Rating
Solstice Trust Series I 2017	PTC Series A1	Sep 2017	10.40%	Dec 2020	26.97	[ICRA]AA-(SO)
	PTC Series A2	Sep 2017	12.50%	Dec 2020	6.85	[ICRA]A+(SO)

[#] calculated on XIRR basis

^{*} Scheduled maturity and average life at transaction initiation; may change on account of prepayments in the underlying pool

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About ICRA Limited:

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