

March 02, 2020

## Spandana Sphoorty Financial Limited: ICRA assigns provisional ratings to pass through certificates (PTCs) issued under a micro loan securitization transaction Kartikeya 02 2020

### Summary of rating action

Trust Name	Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Kartikeya 02 2020	PTC Series A	147.05	Provisional [ICRA]A(SO) assigned

\*Instrument details are provided in Annexure-1

### Rationale

ICRA has assigned Provisional [ICRA]A(SO) rating to PTC Series A under a securitisation transaction originated by Spandana Sphoorty Financial Limited (Spandana). The PTCs are backed by a pool of Rs. 191.39 crore micro loan receivables (underlying pool principal of Rs. 165.23 crore).

The provisional ratings are based on the strength of cash flows from the selected pools of contracts; the credit enhancement available in the form of (i) Cash collateral of 5.50% of the pool principal to be provided by the Originator, (ii) subordination of 11.00% of the pool principal for PTC Series A, and, (iii) subordination of entire Excess Interest Spread (EIS) in the structure; and the integrity of the legal structure. The ratings are subject to fulfillment of all conditions under the structure and the review of documentation pertaining to the transaction by ICRA.

### Key rating drivers

#### Credit strengths

- The first line of support is available for the transaction through subordination of the excess interest spread (EIS) amounting to around 11.3% of the pool principal amount for PTC Series A
- Further credit support in the transaction is available through subordination of 11.00% of pool principal for PTC Series A followed by a proposed Cash Collateral (CC) equivalent to 5.50% of the initial pool principal amount
- Absence of overdue contracts as on pool cut-off date and moderate seasoning at 23.6 weeks compared to balance pool tenure of 92 weeks

#### Credit challenges

- Moderate geographical concentration with top 3 states contributing to 54.58% of the initial pool principal amount
- Presence of moderate share of first loan cycle borrowers at 39.43%

#### Description of key rating drivers highlighted above

The first line of support for PTC Series A in the transaction is in the form of subordination of 11.00% of the pool principal (includes over collateralization). An important feature of the structure in this transaction is that any collection in excess of the promised interest payouts to PTC Series 1 would be first utilised for payment of expected principal of PTC Series A1 and the remaining would be passed on to the originator on a monthly basis.

Cash collateral of 5.50% of the initial pool principal provided by Spandana acts as further credit enhancement in the transaction. In the event of shortfall in meeting the promised PTC payouts during any month, the Trustee will utilize the cash collateral to meet the shortfall. Additionally, EIS available in the structure will also provide credit enhancement support.

There are no overdues in the pool as on the cut-off date. The pool consists of loans that are moderately seasoned with weighted average seasoning of 23.6 weeks and the door to door residual tenure of the contracts is moderate at 92 weeks. The geographical concentration of the loan contracts in the current pool is moderate with top 3 states constituting 54.58% of the pool principal.

**Performance of past rated pools:** In the past, ICRA has rated 22 micro loan receivable pools originated by SSFL with the last pool being rated in December 2019. The performance of the live pools (which have completed at least two payouts) has been good with the cumulative collection efficiency exceeding 98% and low delinquencies after the January 2020 payouts.

### Key rating assumptions

ICRA's cash flow modelling for rating Asset backed securities (ABS) transactions involves simulation of potential delinquencies, losses and prepayments in the pool. The assumptions for mean shortfall and the Co-efficient of Variation (CoV) are arrived on the basis of the values observed in the analysis of the Originator's loan portfolio. 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 pool contracts.

After making the aforementioned adjustments, the expected mean shortfall in principal collection during the tenure of the pool is estimated to be about 4.0% - 5.0%, with certain variability around it. The prepayment rate for the underlying pool is estimated to be in the range of 4% - 8% per annum.

### Liquidity position: Strong

The principal amount on the rated PTCs is promised on the scheduled maturity date. Only the interest amount is promised on a monthly basis. 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 promised PTC payouts.

Additionally, there is cash collateral available in the transaction amounting to 5.50% of the pool principal amount. The cash collateral is adequate to cover promised interest payouts due for six months to the PTC Series A investors even in an unlikely scenario of no collections in the pool.

### Rating sensitivities

**Positive triggers** – Sustained strong collection performance of the underlying pool contracts (>95%), leading to lower than expected delinquency levels, and on an increase in the cover available for future investor payouts from the credit enhancements.

**Negative triggers** – Sustained weak collection performance of the underlying pool (Monthly collection efficiency <90%) leading to higher than expected delinquency levels and CE utilization levels

## Analytical approach

The rating action is based on the analysis of the performance of SSFL's portfolio till December 2019, the performance of the previously rated ICRA pools, the key characteristics and composition of the current pool, the performance expected over the balance tenure of the pool, and the credit enhancement cover available in the transaction.

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Rating Methodology for Securitisation Transactions</a>
Parent/Group Support	Not applicable
Consolidation / Standalone	Not applicable

## About the company

Spandana Sphoorty Financial Limited was incorporated in 2003 as a non-banking financial company (NBFC) and took over the microfinance operations of Spandana, a non-governmental organisation started by Ms. Padmaja Reddy in 1998. The company was classified as a non-banking financial company – microfinance institution (NBFC - MFI) in 2015. Following the microfinance crisis in Andhra Pradesh (AP), Spandana entered into a Master Restructuring Agreement (MRA) as a part of the corporate debt restructuring (CDR) with its lenders in September 2011. It exited the CDR in March 2017 after a fresh equity investment led by Kedaara Capital Investment Managers Limited<sup>1</sup> (Kedaara Capital) and fresh funding from three lenders. The key shareholders in the company as on August 16, 2019 are Kangchenjunga Limited (45.7%), Valiant Mauritius Partners FDI Limited (6.0%), JM Financial Ltd group (5.2%) and the company's promoter Ms. Reddy (17.1%), who continues to be the Managing Director. The company had come out with its IPO in August 2019.

As on June 30, 2019, Spandana had operations in 17 states and Union Territories spanning 268 districts with a total loan portfolio outstanding of Rs. 4,876 crore. The active member base and number of field staff stood at 24.43 lakh and 4,941 respectively as on June 30, 2019.

The company has a rating of [ICRA]A- with stable outlook on its long-term debt programmes.

<sup>1</sup> Through a special purpose vehicle called Kanchenjunga Limited

## Key financial indicators

	<b>FY2016 (audited)</b>	<b>FY2017 (audited)</b>	<b>FY2018 (audited)</b>	<b>H1 FY2019 (IndAS)</b>
Total Income	347.5	376.0	525.7	486.7
Profit after Tax	243.2	52.9	171.9	145.3
Net Worth	-606.9	537.2	984.2	1,675.2
Total Managed Portfolio <sup>^</sup>	2,018.8	2,094.6	4,013.9	4,535.2*
Total Managed Assets <sup>^</sup>	2,099.9	2,413.2	4,262.9	5,520.5*
Return on Average Managed Assets <sup>^</sup> (%)	10.9%	2.3%	5.1%	5.9%*
Return on Average Net Worth (%)	-33.5%	-152.0%	22.6%	21.9%
Gross NPA <sup>^</sup> (%)	39.7%	42.1%	25.9%	13.4%*
Net NPA <sup>^</sup> (%)	0.1%	2.9%	0.3%	0.1%*
Net NPA <sup>^</sup> / Net Worth	-0.2%	6.9%	0.7%	0.2%*
Managed Gearing (times)	-2.9	1.8	2.3	1.9
CRAR <sup>^</sup> (%)	-18.6%	49.0%	37.2%	38.8%

Note: Amounts in Rs. crore

<sup>^</sup>Includes non-yielding old AP portfolio of about Rs. 800 crore, which has 100% provision cover

\*Includes non-yielding old AP portfolio of about Rs. 615 crore, which has 100% provision cover

Source: Spandana, ICRA research

## Status of non-cooperation with previous CRA

### Non-cooperation by Issuer

CRISIL has been consistently following up with Spandana Sphoorty Financial Limited (SSFL) for obtaining information through letters dated August 20, 2018 and September 20, 2018 among others, apart from telephonic communication and emails. However, the issuer has remained non cooperative.

'The investors, lenders and all other market participants should exercise due caution while using the rating assigned/reviewed with the suffix 'ISSUER NOT COOPERATING'. These ratings lack a forward looking component as it is arrived at without any management interaction and is based on best available or limited or dated information on the company'.

### Detailed Rationale

Despite repeated attempts to engage with the management, CRISIL failed to receive adequate information on either the business performance or strategic intent of SSFL, which restricts CRISIL's ability to take a forward looking view on the entity's credit quality. CRISIL believes information available on SSFL is consistent with 'Scenario 2' outlined in the 'Framework for Assessing Consistency of Information with CRISIL BBB' rating category'. Therefore, CRISIL has migrated the rating on bank facilities of SSFL to 'CRISIL BBB-/Positive Issuer Not Cooperating'.

Subsequently, CRISIL has withdrawn the rating at the company's request and on receipt of no objection letters from respective banks. The withdrawal is in line with CRISIL's policy on withdrawal of bank loan ratings.

**Any other information: None**

**Rating history for last three years**

Instrument	Current Rating (FY2020)			Chronology of Rating History for the past 3 years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating	Date & Rating in FY2019	Date & Rating in FY2018	Date & Rating in FY2017
1 Kartikeya 02 2020	PTC Series A	147.05	147.05	02-Mar-20 Provisional [ICRA]A(SO)	-	-	-

**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

Trust Name	Instrument Name	Date of Issuance	Coupon Rate (p.a.p.m)	Scheduled Maturity Date*	Amount Rated (Rs. crore)	Current Rating
Kartikeya 02 2020	PTC Series A	February 2020	8.75%	December 2021	147.05	Provisional [ICRA]A(SO)

\* Scheduled maturity at transaction initiation; may change on account of prepayment

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### About ICRA Limited:

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For more information, visit [www.icra.in](http://www.icra.in)

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