

April 13, 2020

Magma Fincorp Limited: Rating withdrawn for non-convertible debenture programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans (bank)	2,056.67	2,056.67	[ICRA]AA- (Negative); Outstanding
Non-convertible Debenture Programme	335.00	0.00	[ICRA]AA- (Negative); Withdrawn
Total	2,391.67	2,056.67	

*Instrument details are provided in Annexure-1

Rationale

ICRA has withdrawn the rating of [ICRA]AA- (pronounced ICRA double A minus) assigned earlier to the Rs. 335-crore non-convertible debenture (NCD) programme of Magma Fincorp Limited (MFL) as there is no amount outstanding against the rated instrument. The withdrawal is at the request of the company. ICRA also has a rating outstanding of [ICRA]AA- for the Rs. 2,056.67-crore term loans of MFL. The outlook on the long-term rating is Negative.

To arrive at MFL's rating, ICRA has taken a consolidated view of the credit profiles of MFL and Magma Housing Finance Limited (MHFL; together referred to as the Magma Group) owing to their common management and shared infrastructure.

The rating factors in the Group's strong presence in the retail asset finance business with a wide geographical presence through 326 branches across 21 states. The rating also factors in the Group's comfortable capitalisation levels (CRAR – 26.9% for MFL as on December 31, 2019), well-diversified portfolio mix and adequate liquidity buffer in the form of unutilised drawable bank lines and unencumbered cash and liquid investments. In ICRA's opinion, prudent capitalisation is a key mitigant against delinquencies and other credit risks associated with the Group's business. The Group's retail loan book supports its asset liability management (ALM) profile and since a sizeable part of its loan book qualifies for priority sector lending, down-selling is an important funding option for the Group.

The Negative outlook on the Group's rating factors in the deterioration in the asset quality indicators following the reduced collection efficiencies in certain geographies and loan segments (commercial vehicles - CVs and construction equipment - CE). Consequently, the credit costs were high and adversely impacted the profitability metrics of the Group. Moreover, ICRA expects the Group to continue having relatively weak asset quality indicators. Given the relatively moderate borrower credit profiles (first-time buyers, small entrepreneurs, self-employed and non-income proof category), the Group's ability to profitably grow its business while improving the asset quality from the current levels and maintaining prudent capitalisation would be a key rating sensitivity.

Key rating drivers and their description

Credit strengths

Established player in retail asset finance business – Incorporated in 1988, the Magma Group is a significant player in the retail asset finance space with an experienced management team and a wide geographical presence through 326 branches across 21 states, mostly in semi-urban and rural areas. The Group's managed assets under management (AUM) stood stable at Rs. 16,574 crore as on December 31, 2019 on a consolidated basis. It has a well-diversified managed portfolio mix comprising cars and utility vehicles (18%), CVs & CE (15%), used assets (23%), tractors (9%), SME (12%) and mortgage (23%) as on December 31, 2019. The Group's retail loan book supports its ALM profile. Moreover, as a large part of the portfolio qualifies for priority sector lending, the ability to down-sell loans remains high.

Adequate capitalisation profile – The Group's capitalisation profile is adequate for the current scale of operations with a CRAR of 26.9% and a net worth of Rs. 2,775 crore as on December 31, 2019. The managed gearing remained stable at 4.7 times as on December 31, 2019 (4.8 times as on March 31, 2019). Despite the muted internal capital generation, the capitalisation has remained adequate due to modest business growth with the disbursements declining by 17% in 9M FY2020 on a YoY basis. On a consolidated basis, the solvency ratio (net NPA/net worth) increased marginally to 23.32% (as per Ind-AS) as on December 31, 2019 from 21.98% as on December 31, 2018, supported by significant loan write-offs (~Rs. 323 crore in 9M FY2020). According to ICRA, prudent capitalisation is a key mitigant against delinquencies and other credit risks associated with Magma's business and ICRA expects the Group to maintain prudent capitalisation going forward as well.

Credit challenges

Modest asset quality indicators – The Group's asset quality indicators deteriorated with the gross stage 3% and net stage 3% rising to 6.7% and 4.5%, respectively, as on December 31, 2019 from 4.8% and 3.1%, respectively, as on March 31, 2019 (as per Ind-AS), despite loan write-offs worth ~Rs. 323 crore in 9M FY2020. The rise in delinquencies was majorly attributable to reduced collections in the CV and CE segments in Q2 FY2020 (accounted for ~70% of the increase in slippages) and in certain geographies such as Uttar Pradesh, West Bengal, Andhra Pradesh and Bihar (accounted for ~60% of the increase in slippages). Though the collection efficiencies improved to an extent from October onwards, the vulnerability of the portfolio remains high. The asset quality indicators remain weak and the Group's ability to control fresh slippages and recover from delinquent accounts, especially in a challenging operating environment, would be a key monitorable.

Moderate profitability – In 9M FY2020, the Group's profitability was significantly impacted (RoA of 0.37% and RoE of 2.28%) by higher credit costs of Rs. 372 crore (2.88% of average total assets) compared to Rs. 224 crore (1.84% of average total assets) in 9M FY2019. The increase in credit costs was mostly attributable to the incremental provisions on loan write offs and the loss on the sale of repossessed assets. ICRA notes that though the Group's focus on product segments such as CVs, used assets, SME finance and mortgage (combined share of ~68% of the overall portfolio as on December 31, 2019 compared to 53% as on March 31, 2018) could improve its risk-adjusted returns, its profitability is expected to remain subdued in the medium term due to elevated credit costs. The Group's ability to control fresh slippages and recover from delinquent accounts and hence report an improvement in the profitability indicators would be a key rating sensitivity.

Moderate portfolio vulnerability – The Group’s portfolio remains vulnerable given the high proportion of borrowers with relatively moderate credit profiles (first-time buyers, small entrepreneurs, self-employed and non-income proof category). The customer segment includes small fleet operators, farmers, small traders, factory owners, shop owners and other borrowers with informal income wherein ~68% of the Group’s portfolio was spread across semi-urban and rural areas as on December 31, 2019. The Group also provides unsecured loans to business enterprises as a part of its SME loan book. As on December 31, 2019, about two-third of the mortgage (including loan against property (LAP) and home loans) portfolio exposure was towards the self-employed borrower category (28% formal and 40% informal), while the rest was towards the salaried segment. The Group’s ability to control fresh slippages and maintain a high collection efficiency in the near term would remain a key rating monitorable.

Liquidity position: Adequate

The Group’s liquidity profile is adequate on a consolidated basis, supported by unencumbered cash and liquid investments of Rs. 831 crore and positive cumulative mismatches across all maturity buckets of the ALM for MFL, on a standalone basis, as on December 31, 2019. For MHFL, a positive mismatch in the 6-12-month bucket would depend on the timely renewal of the working capital lines.

The Group expects inflows of Rs. 3,127 crore compared to repayments of Rs. 2,173 crore in the next 6 months on a consolidated basis as on December 31, 2019. Moreover, the Group had Rs. 1,883 crore of unutilised sanctioned bank lines as on December 31, 2019, which support its liquidity profile. Also, a large part of its portfolio is eligible for securitisation, which provides an additional source of funding for the Group and hence supports the overall liquidity.

Rating sensitivities

Positive triggers – The Group’s ability to improve its asset quality with a reduction in the 90+ dpd (including write-offs) to less than 6.5% of AUM on a sustained basis, while maintaining the gearing at the current level on a sustained basis, would lead to a revision in the rating outlook. Given the Negative outlook, a credit rating upgrade is unlikely in the near term.

Negative triggers – The Group’s inability to improve its asset quality by reducing the 90+ dpd (including write-offs) to less than 6.5% of AUM along with its inability to maintain profitability with a return on average managed assets of over 1.5% on a sustained basis would lead to a revision in the credit ratings.

Analytical approach

Analytical Approach		Comments
Applicable Methodologies	Rating	ICRA’s Credit Rating Methodology for Non-Banking Finance Companies
Parent/Group Support		Not applicable
Consolidation/Standalone		Consolidated view of the credit profiles of MFL and MHFL (together referred to as the Magma Group) owing to their common management and shared infrastructure

About the company

Magma Fincorp Limited (formerly MFL Leasing Limited and MFL Shrachi Finance Limited) was incorporated in 1988 and is registered with the Reserve Bank of India (RBI) as an asset-financing NBFC. The portfolio growth remained stagnant in 9MFY2020 with the managed AUM at Rs. 16,574 crore as on December 31, 2019 compared to Rs.

16,396 crore as on December 31, 2018. The portfolio mix remained largely stable, with vehicle financing, SME and mortgage constituting 65%, 12% and 23%, respectively, of the portfolio. There has been an increased focus on the financing of used assets, SME and mortgage, the total share of which increased to ~58% of the portfolio as on December 31, 2019 from ~50% as on December 31, 2018. While MFL has a long track record in asset-based product financing (CVs, CE, cars, tractors), its SME business gained volume only from FY2014. The company entered mortgage financing in February 2013 and general insurance through a joint venture in October 2012.

In FY2019, MFL recorded a consolidated profit after tax of Rs. 304 crore on a total consolidated asset base of Rs. 16,789 crore compared with a consolidated profit after tax of Rs. 237 crore on a total consolidated asset base of Rs. 14,894 crore in FY2018. On a standalone basis, MFL reported a profit after tax of Rs. 275 crore on an asset base of Rs. 14,991 crore in FY2019 compared to a profit after tax of Rs. 202 crore on an asset base of Rs. 13,568 crore in FY2018.

In 9M FY2020, MFL recorded a consolidated profit after tax of Rs. 63 crore on a total consolidated asset base of Rs. 16,432 crore compared with a consolidated profit after tax of Rs. 219 crore on a total consolidated asset base of Rs. 15,546 crore in 9M FY2019. On a standalone basis, MFL reported a profit after tax of Rs. 25 crore on an asset base of Rs. 14,021 crore in 9M FY2020 compared to a profit after tax of Rs. 189 crore on an asset base of Rs. 13,908 crore in 9M FY2019. On a consolidated basis, the company's borrowing mix consisted of working capital lines (25%), securitisation (34%), NCDs (6%), term loans (28%) and perpetual & subordinated debt (7%) as on December 31, 2019. About two-third of the funding was generated through banks.

Key financial indicators (consolidated)

	FY2018	FY2019	9M FY2020
	Ind-AS	Ind-AS	Ind-AS
Profit after tax	237	304	63
Net worth	1,972	2,744	2,775
AUM	15,801	17,029	16,574
On-book portfolio	14,644	15,645	14,776
Return on average assets	1.6%	1.8%	0.4%
Return on average equity	11.3%	12.9%	2.3%
Managed gearing (times)	6.1	4.8	4.7
% CRAR (MFL; standalone)	17.3%	24.9%	26.9%
% Gross stage 3 (on-book)	8.6%	4.8%	6.7%
% Net stage 3 (on-book)	4.5%	3.1%	4.5%
% Net stage 3/ Net worth	31.7%	17.2%	23.3%

Source: Magma, ICRA research; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Type	Current Rating (FY2021)		Chronology of Rating History for the Past 3 Years							
			Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2021	Date & Rating in FY2020				Date & FY2019	Rating in	Date & Rating in FY2018
					13-Apr-20	16-Dec-19	24-Oct-19	06-Aug-19	22-Jul-19	25-Jul-18	20-Apr-18	24-Jul-17
1	Term Loans (banks)	Long Term	2,056.67	2,056.67	[ICRA]AA-(Negative)	[ICRA]AA-(Negative)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Negative)
2	NCD	Long Term	335.00	0.00	Rating Withdrawn	[ICRA]AA-(Negative)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Negative)

Source: ICRA research, Magma

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

Annexure-1: Instrument details

ISIN	Instrument Name	Date Issuance Sanction	of / Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Outlook	Rating and
INE511C07607	Secured NCD	18-Aug-2017	8.99%	19-Aug-2019	60	[ICRA]AA- Withdrawn	(Negative);
NA	NCD (yet to be placed)	NA	NA	NA	275	[ICRA]AA- Withdrawn	(Negative);
NA	Term Loan 1	29-Dec-2015	9.40%	31-Dec-2020	75	[ICRA]AA-	(Negative)
NA	Term Loan 2	29-Dec-2015	9.10%	28-Dec-2020	63.75	[ICRA]AA-	(Negative)
NA	Term Loan 3	26-Feb-2016	9.45%	31-Dec-2020	37.5	[ICRA]AA-	(Negative)
NA	Term Loan 4	26-Sep-2017	9.90%	30-Sep-2022	162.5	[ICRA]AA-	(Negative)
NA	Term Loan 5	31-Oct-2017	8.95%	30-Sep-2022	65.63	[ICRA]AA-	(Negative)
NA	Term Loan 6	29-Jun-2016	10.60%	29-Jun-2021	35.29	[ICRA]AA-	(Negative)
NA	Term Loan 7	31-Dec-2018	10.00%	31-Dec-2023	500	[ICRA]AA-	(Negative)
NA	Term Loan 8	30-Mar-2019	10.50%	30-Mar-2024	150	[ICRA]AA-	(Negative)
NA	Term Loan 9	30-Mar-2019	9.75%	31-Mar-2024	100	[ICRA]AA-	(Negative)
NA	Term Loan 10	27-May-2019	9.80%	27-May-2023	392	[ICRA]AA-	(Negative)
NA	Term Loan 11	28-Jun-2019	9.15%	27-Jun-2024	75	[ICRA]AA-	(Negative)
NA	Term Loan 12	30-Mar-2019	12.50%	30-Mar-2026	100	[ICRA]AA-	(Negative)
NA	Term Loan 13	31-Dec-2019	9.35%	30-Mar-2024	200	[ICRA]AA-	(Negative)
NA	Term Loan 14	31-Dec-2019	10.00%	31-Dec-2024	100	[ICRA]AA-	(Negative)

Source: Magma

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