

## Sakthi Finance Limited

February 21, 2019

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible Debentures (NCDs)	377.16	35.13 342.03	[ICRA]BBB (Stable); withdrawn [ICRA]BBB (Stable); Outstanding
Fund Based - Term Loan	48.81	48.81	[ICRA]BBB (Stable); Outstanding
Fund-based Long-term Facilities from Banks - Cash Credit (CC)	148.95	148.95	[ICRA]BBB (Stable); Outstanding
Fund based - Interchangeable <sup>1</sup>	28.95	28.95	[ICRA]BBB (Stable)/ [ICRA]A2; Outstanding
Fund-based Short-term Facilities from Banks (WCDL)	67.00	67.00	[ICRA]A2; Outstanding
Fixed Deposits	-	-	MA- (Stable); Outstanding
<b>Total</b>	<b>641.92</b>	<b>606.79</b>	

\*Instrument details are provided in Annexure-1; <sup>1</sup> Sub-limit of fund-based long-term facilities from banks - CC

### Rationale

ICRA has withdrawn the rating of [ICRA]BBB (pronounced ICRA triple B)<sup>1</sup> rating with a Stable outlook for the Rs.35.13 NCD programme, at the request of the company, as it was not issued and there is no outstanding against the same.

### Outlook: Stable

ICRA believes SFL will continue to benefit from its established market presence in Tamil Nadu and Kerala and its prudent loan origination policies. The outlook may be revised to Positive if SFL is able to grow at a steady pace and improve its capitalisation, liquidity and earnings profiles. The outlook may be revised to Negative if there is a significant weakening in its asset quality, capitalisation or earnings profile or, if SFL's financial flexibility weakens further.

### Key rating drivers

#### Credit strengths

**Established franchise and extensive presence in the regional market** - SFL has a track record of more than six decades in the vehicle finance segment, with operations across Tamil Nadu, Kerala, Andhra Pradesh and Karnataka. The company has a good understanding of the target segments, mainly the used commercial vehicle (CV) segment and it has established customer relationships, with about 55-60% of incremental business being from repeat customers.

**Effective origination, monitoring and collection systems** – SFL's extensive presence in vehicle finance along with the Group's presence in related businesses like automotive dealerships has aided in effective origination, prudent appraisal, good market responsiveness, monitoring and collections. The company has a branch-centric operating model with an inhouse origination team, which is responsible for collections, while credit sanctioning is centralised. The company conducts credit bureau checks to screen its customers, followed by field investigation and income assessment and

<sup>1</sup> For complete rating scale and definitions, please refer to ICRA's website ([www.icra.in](http://www.icra.in)) or other ICRA rating publications

viability analysis as part of its loan origination. Prior to loan disbursement, the company's internal risk control unit verifies the authenticity of the documents submitted. The company is implementing a workflow management system (expected to be completed by March 2019) which will enable management to monitor sourcing and collection activities on a real-time basis, thereby reducing the lead time for loan processing.

**Expected improvement in capital structure post the rights issue** – SFL has a moderate capitalization currently with gearing and capital adequacy of 6.5 times and 16.3% respectively as of September 2018 (6.4 times and 17.2% as of March 2018). The company plans to raise Rs. 50 crore through rights issue in H1FY2020, which is currently pending shareholder approval. The rights issue would enable the company to grow its portfolio at about 8-10% annually over the next three years (FY2020-FY2022), assuming internal generation to be in the range of 4-6% , while capping the gearing at about 5 times. Any higher than expected growth would however warrant incremental capital to maintain gearing at about 5 times.

## Credit challenges

**Stagnant portfolio; regionally concentrated operations** – SFL's portfolio has been stagnant over the past few years on account of modest disbursement growth, relatively high level of prepayments and its own moderate financial flexibility. The portfolio stood at Rs 925 crore as of September 2018 as compared to Rs. 903 crore as of March 2018 (Rs. 906 crore as of March 2017). The company has a regionally concentrated portfolio with Tamil Nadu and Kerala accounting for 89% of the total portfolio as in September 2018. ICRA expects the portfolio share to remain concentrated given the company's limited branch expansion plans in the medium term.

**Increase in delinquencies during H1FY2019** - The company's 90+ dpd increased to 5.8% as of September 2018 from 4.9% as of March 2018 (5.0% as of March 2017), because of the impact of floods in several districts in Kerala. The economic disruption also affected the collections in adjoining districts in Tamil Nadu. This is reflected in the rise in 90+ dpd to 6.0% as of September 2018 from 5.0% as of March 2018 in the two states (Tamil Nadu and Kerala), which constituted bulk of SFL's portfolio. With some recovery in collections during Oct-Dec 2018, the company's overall 90+ dpd declined to 5.2% as of December 2018 vis-a-vis 4.8% as of December 2017, albeit remain higher than the March 2018 level. Going forward, it would be critical for the company to strengthen its collection and undertake overall effective recoveries to improve quality and keep credit cost under control.

**Moderate profitability** – SFL's margins (net interest margin/ average managed assets) remained stable at 5.6% in H1FY2019 in line with the three-year average (5.7% during FY2016-FY2018). The company's core profitability (Operating profit/ Average managed assets), however declined to 2.1% in H1FY2019 from 2.3% in FY2018 (2.3% in FY2017) as operating efficiencies were impacted by the weak portfolio expansion. Its net credit cost stood at 0.4% in H1FY2019 vis-a-vis 0.5% in FY2018, as provision cover remained stable at 37% in H1FY2019 (36% in FY2018) . Overall, the company's net profitability remained moderate at 1.3% in H1FY2019 in line with the prior three-year average (1.3%). SFL's ability to improve its operating efficiencies and keeping credit costs under control would be critical for incremental profitability.

**Diversification of funding profile critical to meet long-term growth plans** - SFL has limited financial flexibility as continued weaknesses in group entity performances limit its ability to secure incremental funding from some banks. ICRA however notes that, SFL, over the recent past has increased its dependence on retail deposits and debentures, largely via public issuance. Currently, the company envisages raising about Rs.150 crore through public issue of debentures and about Rs.70-80 crore via private placements to HNIs. Further, the proposed rights issue would bolster its ability to secure further retail deposits, which as in September 2018 stood at 1.3 times its net owned funds. SFL would need to diversify its lender' base to achieve long-term growth plans and for maintaining adequate liquidity.

### Liquidity position:

SFL's asset liability maturity (ALM) profile is well matched as of December 2018 with no cumulative negative mismatches in the less than one-year buckets. Over the period Jan'19 – Jun'19, the company has average monthly repayment obligation in the range of Rs. 30-35 crore which could be met with monthly loan collections of about Rs. 35 crore over the same period. The company also has unencumbered cash and liquid investments of about Rs. 35 crore and sanctioned undrawn bank lines of about Rs.20 crore as of December 2018.

The company proposes to raise about Rs.150 crore through public debenture issue and Rs.70-80 crore via private placement for its incremental business needs. Ability of the company to raise resources in a timely manner and at competitive rates would be crucial going forward.

### Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">ICRA's Credit Rating Methodology for Non-Banking Finance Companies</a>
Parent/Group Support	Not applicable
Consolidation / Standalone	The ratings are based on the standalone financial statements of SFL.

### About the company:

Sakthi Finance Limited (SFL), incorporated in 1955, is a part of Sakthi Group, which has a presence across sectors such as sugar, beverages, automobile and transport dealerships, auto components and textiles. SFL primarily finances CVs, which constituted 89% of its total portfolio as in September 2018. The remaining portfolio consisted of loans towards the purchase of cars, construction equipment and other machinery. SFL primarily operates in Tamil Nadu and Kerala, which together accounted for about 89% of the total portfolio.

In FY2018, SFL reported a net profit of Rs. 16.8 crore on a managed asset base of Rs. 1,075.7 crore, compared to a net profit of Rs. 11.9 crore on a managed asset base of Rs. 1,060.9 crore in FY2017.

### Key financial indicators (audited)

	FY2017	FY2018
<i>NPA recognition norm</i>	<i>180+ dpd</i>	<i>90+ dpd</i>
Total Income	166.7	167.6
Profit after tax (reported)	16.8	11.9
Net Worth	135.1	140.1
Managed Portfolio	905.6	902.6
Total Managed Assets	1060.9	1075.7
Return on Managed Assets	1.5%	1.0%
Return on Net Worth	12.8%	7.8%
Gearing (reported)	6.6	6.4
Gross NPA%	4.4%	5.2%
Net NPA%	3.1%	3.3%
CAR%	19.7%	17.2%

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 (FY2019)				Chronology of Rating History for the past 3 years			
		Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating February 2019	April 2018	Date & Rating in FY2018 April 2017	Date & Rating in FY2017 March 2016	Date & Rating in FY2016 December 2014	
1 NCD	Long Term	342.03	342.03	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BB B (Stable)	[ICRA]BB B (Stable)	[ICRA]BBB (Stable)	
2 Term Loans	Long Term	48.81	48.81	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BB B (Stable)	[ICRA]BB B (Stable)	[ICRA]BBB (Stable)	
3 Long-term bank facilities - CC	Long Term	148.95	148.95	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BB B (Stable)	[ICRA]BB B (Stable)	[ICRA]BBB (Stable)	
4 CC / WCDL – Interchangeable	Long Term/ Short Term	28.95	28.95	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BB B (Stable)/ [ICRA]A2	[ICRA]BB B (Stable)/ [ICRA]A2	[ICRA]BBB (Stable)/ [ICRA]A2	
5 Short-term bank facilities - WCDL	Short Term	67.00	67.00	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A2	
6 Fixed deposits	Long Term	-	-	MA- (Stable)	MA- (Stable)	MA- (Stable)	MA- (Stable)	MA- (Stable)	
7 NCD	Long Term	35.13	-	[ICRA]BBB (Stable) withdrawn	[ICRA]BBB (Stable)	[ICRA]BB B (Stable)	-	-	

**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

ISIN No	Instrument	Date of Issuance /Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Unutilized	NCD	NA	NA	NA	150.00	[ICRA]BBB (Stable)
INE302E07060	NCD	1-Apr-15	11.50%	1-Apr-19	19.43	[ICRA]BBB (Stable)
INE302E07078	NCD	1-Apr-15	11.50%	1-Apr-19	2.72	[ICRA]BBB (Stable)
INE302E07086	NCD	1-Apr-15	-	1-Apr-19	14.33	[ICRA]BBB (Stable)
INE302E07110	NCD	18-May-16	10.50%	18-May-19	8.01	[ICRA]BBB (Stable)
INE302E07128	NCD	18-May-16	10.50%	18-May-19	3.34	[ICRA]BBB (Stable)
INE302E07136	NCD	18-May-16	10.92%	18-May-19	8.79	[ICRA]BBB (Stable)
INE302E07144	NCD	18-May-16	11.00%	18-May-20	60.50	[ICRA]BBB (Stable)
INE302E07151	NCD	18-May-16	11.00%	18-May-20	9.56	[ICRA]BBB (Stable)
INE302E07169	NCD	18-May-16	11.46%	18-May-20	40.34	[ICRA]BBB (Stable)
INE302E08019	NCD	29-Mar-16	13.50%	15-Apr-22	25.00	[ICRA]BBB (Stable)
NA	Term loan 1	21-Sep-16	-	30-Sep-19	7.60	[ICRA]BBB (Stable)
NA	Term loan 2	31-Oct-17	-	15-Dec-20	16.21	[ICRA]BBB (Stable)
Unutilized	Term loan	NA	-	NA	25.00	[ICRA]BBB (Stable)
NA	Fund based Long Term Facilities from Banks - CC	NA	-	NA	148.95	[ICRA]BBB (Stable)
NA	Fund based- Interchangeable (CC/ WCDL)	NA	-	NA	28.95	[ICRA]BBB (Stable) / [ICRA]A2
NA	Fund based Short Term Facilities from Banks (WCDL)	NA	-	NA	67.00	[ICRA]A2
NA	Fixed deposits	NA	-	NA	-	MA- (Stable)
Unutilized	NCD	NA	NA	NA	35.13	[ICRA]BBB (Stable); withdrawn

Source: SFL

## Annexure-2: List of entities considered for consolidated analysis: Not applicable

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