

Press Release

Fedbank Financial Services Limited

February 05, 2021



Rating Reaffirmed & Assigned

Instruments Rated*	Rs. 1000.00 Cr.
Facilities Rated	Rs.500.00 Cr.
Short Term Rating	ACUITE A1+ (Reaffirmed)
Facilities Rated	Rs.500.00 Cr.
Short Term Rating	ACUITE A1+ (Assigned)

* Refer Annexure for details

Rating Rationale

Acuite has reaffirmed the short-term rating of '**ACUITE A1+**' (read as **ACUITE A one plus**) on the Rs.500.00 crore commercial paper program of Fedbank Financial Services Limited (FFSL).

Acuite has assigned the short-term rating of '**ACUITE A1+**' (read as **ACUITE A one plus**) on the Rs.500.00 crore proposed commercial paper program of Fedbank Financial Services Limited (FFSL).

The rating factors in strong support and strategic alignment derived from the parentage of the Federal bank. The rating further factors in the healthy capitalization levels which is maintained through the regular capital infusion by the promoters. The rating also considers the well diversified portfolio, spread across 10 states and 2 Union Territory, with max concentration of ~28% in state of Karnataka. FFSL's total loan book grew by 16% i.e. Rs. 4317 Cr. as on Dec 31, 2020 over March 31, 2020 (Rs.3721 Cr). Gold Loan Segment is driving the major growth in loan book as 68% of the total disbursements made in 9MFY2021 were towards Gold Loan Segment.

The strengths are partially offset by the asset quality concerns depicted through the increase in 90+ DPD towards the developer financing segment remains elevated, as the 90+ DPD of the same deteriorated to 12.84% as on Dec 31, 2020 from 10.95% as on March 31, 2020. Though, the collection efficiency in retail lending month-on-month basis is recovering to the pre-covid levels of 98-99%, however there are significant overdue amount from the period of moratorium given to the borrowers, whose significant portion is expected to be recovered by the March, 2021.

About The Fedbank Financial Services Limited (FFSL)

FFSL, a non-deposit taking systemically important non-banking financial company (NBFC-ND-SI), is a subsidiary of Federal Bank Limited (FBL). As on Dec 30, 2020 Federal Bank Limited holds 74 percent of shareholding and True North Enterprise Private Limited holds 26 percent in FFSL. FFSL started its operations in August 2010 from an initial gold loan portfolio and has expanded its range of offerings to loan against property (LAP) (small and large ticket), Small and Medium Enterprises (SME) loans, loans to NBFC's and Micro Financial Institutions (MFI) amongst others. As on Dec 30, 2020, the operations of FFSL are spread across 359 branches in 10 states and 2 Union Territory namely Gujarat, Maharashtra, Tamil Nadu, Karnataka, Andhra Pradesh, Telangana, Rajasthan, Punjab, Uttar Pradesh, Madhya Pradesh, Haryana, Goa and Delhi.

About The Federal Bank Limited (FBL)

FBL is a Kerala based private sector bank founded in 1931. The bank has a network of 1272 branches in India and abroad and 1948 ATMs and cash recyclers as on December 31, 2020. It has a net worth of Rs. 15,645 Cr. as on December 31, 2020. The bank has aggregate deposits of Rs. 1.62 trillion and advances of Rs. 1.26 trillion as on December 31, 2020. It has a healthy level of CASA at ~34.48 percent as on December 31, 2020. FBL registered a net profit of Rs. 404 Cr. on a net interest income of Rs. 1,437 Cr for 9MFY2021

Analytical Approach

Acuite has considered the standalone financial and business risk profile of FFSL and has notched-up the standalone rating to factor in the likelihood of support from the parent FBL.

Key Rating Drivers:

Strengths

• Strong parentage and Experienced Management:

FFSL is a subsidiary of FBL and holds 74 percent stake in FFSL with the balance 26 percent held by True North Enterprise Private Limited (True North), a private equity investor. The company raised ~Rs.79.19 Cr. by way of a right issue which was subscribed by the existing shareholders in proportion to their shareholding in October, 2020. Besides its majority stake, FBL has supported FFSL by way of debt of Rs. 1178 crore (term loan, cash credit, working capital demand loan, subordinate debt and Tier II) outstanding as on December 31, 2020. Debt from FBL comprised around 30 percent of FFSL's outstanding debt as on December 31, 2020.

The Board of Directors of FFSL has representations from FBL and True North. Mr. Shyam Srinivasan, Managing Director and CEO of FBL, Mr. Ashutosh Khajuria, Executive Director and CFO of FBL are on the board of FFSL. Mr. Maninder Juneja, is the Nominee Director of True North on FFSL board, he has over two decades experience in BFSI segment. Besides the nominee directors, FFSL benefits from its experienced management team headed by, Mr Anil Kothuri, Managing Director and CEO, who has over a decades experience in the BFSI sector, and has been associated with Edelweiss Group and Citibank in the past.

The board is supported by a senior management team comprising of experienced industry professionals having a strong background in the financial services and lending.

Acuite believes that FFSL will benefit from its experienced management team and business and operational linkages with its parent over the medium term, the continued association and a majority stake of FBL will be a key rating sensitivity.

• Diversified product Portfolio

FFSL, forayed into lending business with a focus on gold loans, and gradually diversified into other segments such as LAP (small and large ticket size), wholesale loans towards construction finance and NBFCs, unsecured business loans and affordable housing finance (AHF) loans. Besides LAP, Gold loans and AHF (a recently started segment) the company has business correspondent partnership with few NBFCs and MFIs. As on December 31, 2020 LAP loans comprises 41 percent of the total loan book, gold loans and wholesale finance loans comprised 40 percent and 5 percent, respectively, and balance 14 percent comprised of other categories. The company's loan book grew from Rs. 3721 Cr. as on March 31, 2020 to Rs. 4317 Cr. as on December 31, 2020 (16 percent growth), driven mainly by growth in gold loan segment. The company plans to gradually migrate towards the retail end of the segment. The ability to successfully prune down its big-ticket exposures (Big ticket LAP and wholesale finance) will be a key monitorable.

Geographically, the company's operations grew to 359 branches as on December 31, 2020 (302 branches as on March 31, 2020), spread across 10 states and 2 Union Territory namely Gujarat, Maharashtra, Karnataka, Andhra Pradesh, Telangana, Tamil Nadu, Rajasthan, Punjab, Uttar Pradesh, Madhya Pradesh, Haryana, Goa and Delhi. While the company's operations were well diversified across these states, ~62 percent of its operations are in the southern states of the country as on December 31, 2020.

Acuite expects further growth in the loan portfolio to be driven by an increase in the branch network, diversified product offerings and funding support from its shareholders.

Weaknesses

Marginal decline in asset quality due to slippages developer financing segments and other segments

FFSL's loan book of Rs. 4317 Cr. as on December 31, 2020 comprises a mix of small ticket loans like gold loans and LAP and wholesale lending (construction finance to developers and NBFCs). FFSL's Gross Non-Performing Assets (GNPA) ratio improved from 1.47 percent as on March 31, 2020 to 0.95 percent as on Dec 31, 2020. Mainly on account of improvement in asset quality in gold loan segment. Gross Non-Performing Assets (GNPAs) in Gold loan segment declined from 1.51 percent as on March 31, 2020 to 0.14 percent as on December 31, 2020.

The non-gold loans comprised of loans towards businessmen/traders/professionals in the form of LAP loans (41 percent of the loan book as on December 31, 2020) and construction loans and NBFC loans in the wholesale loan segment (5 percent of the loan book as on December 31, 2020) and Others (Affordable housing, loans to MFIs, Business correspondent exposures, other unsecured business loans) comprised 14 percent of the loan book. The LAP segment is the single largest contributor to the loan book, the GNPA of this segment stood at 1.09% as on December 31, 2020. FFSL's exposure is to real estate developers and NBFC's, with a ticket size ranging between Rs. 5 – 25 crore. The direct exposures to the real estate segment and NBFC reduced to 5 percent as on December 31, 2020 from 10 percent as on March 31, 2020.

Since LAP are extended to self-employed individuals for business purposes and this segment contributes majorly to the loan book, the serviceability of these loans is directly dependent on the level of economic activity in the region. Since the cash flows of these borrowers are vulnerable to factors like level of economic activity in their area of operations, any slowdown in the level of activity can influence the credit profiles of these borrowers which in turn will impact the overall credit quality of this segment and may result in elevated credit costs over the near to medium term. Any sharp increase in Non-performing assets is likely to result in elevated credit costs and thereby impact its profitability and capitalisation levels.

Acuite believes that the company's ability to contain its asset quality pressures while maintaining its profitability parameters is a key rating monitorable.

Liquidity Position: Adequate

FFSL had adequately matched asset-liability profile as on December 31, 2020 with a cumulative surplus in all maturity buckets. The company's assets comprise short to medium term (average of 18 to 36 months) exposures depending on the asset class, against which the borrowings are in the form of two to three-year term loans and cash credit limits. The company has adequate liquidity buffers by way of unencumbered cash and bank balances, unutilised working capital limits and liquid investments as on December 31, 2020 stood at ~Rs. 777.15 Cr. The promoters has also infused funds of Rs.79.19 crore in October, 2020.

Rating Sensitivities:

- Significant change in ownership pattern , which brings down the Federal Banks stack below 51% in the FFSL
- Adverse Movement in asset quality
- Movement in leverage indicators

Material Covenants:

None

About the Rated Entity - Key Financials

	Unit	FY20 (Actual)	FY19 (Actual)
Total Assets	Rs. Cr.	4079.68	2145.32
Total Income (Net of Interest Expense)	Rs. Cr.	264.56	141.85
PAT	Rs. Cr.	39.14	36.13
Net Worth	Rs. Cr.	691.15	458.62
Return on Average Assets (RoAA)	(%)	1.26	1.99
Return on Average Net Worth (RoNW)	(%)	6.81	10.13
Total Debt/Net Worth (Gearing)	Times	4.67	3.53
Gross NPAs	(%)	1.47	2.30
Net NPAs	(%)	1.07	1.93

Status of non-cooperation with previous CRA (if applicable)

Not Applicable

Any other information

Not Applicable

Applicable Criteria

- Group and Parent support - <https://www.acuite.in/view-rating-criteria-47.htm>
- Default Recognition - <https://www.acuite.in/view-rating-criteria-52.htm>

- Non- Banking Financing Entities - <https://www.acuite.in/view-rating-criteria-44.htm>
- Financial Ratios and Adjustments - <https://www.acuite.in/view-rating-criteria-53.htm>
- Commercial Paper - <https://www.acuite.in/view-rating-criteria-54.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/view-rating-criteria-55.htm>

Rating History (Upto last three years)

Date	Name of Instrument/ Facilities	Term	Amount (Rs. Cr.)	Ratings/ Outlook
28 August 2020	Commercial Paper Program	Short Term	500.00	ACUITE A1+ (Reaffirmed)
20 September 2019	Commercial Paper Program	Short Term	500.00	ACUITE A1+ (Reaffirmed)
05 October 2018	Commercial Paper Program	Short Term	500.00	ACUITE A1+ (Reaffirmed)
29 September 2017	Commercial Paper Program	Short Term	500.00	ACUITE A1+ (Assigned)

***Annexure – Details of instruments rated**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Commercial Paper Program	Not Applicable	Not Applicable	Not Applicable	500.00	ACUITE A1+ (Reaffirmed)
Proposed Commercial Paper Program	Not Applicable	Not Applicable	Not Applicable	500.00	ACUITE A1+ (Assigned)

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About Acuite Ratings & Research:

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