Ratings

CRISIL
An S&P Global Company

Pursuant to SEBI notifications, CRISIL Limited (CRISIL) has transferred its Ratings business to its wholly owned subsidiary, CRISIL Ratings Limited (CRISIL Ratings), with effect from December 31st 2020. Any reference to CRISIL in the documents published by the Ratings division of CRISIL, such as Rating Rationales, Credit Rating Reports, Press Releases, Criteria, Methodology, FAQs, Policies and Disclosures, shall henceforth refer to CRISIL Ratings.

Rating Rationale

January 25, 2021 | Mumbai

Fedbank Financial Services Limited

Rated amount enhanced

Rating Action

Rs.1000 Crore (Enhanced from Rs.500 Crore) Commercial Paper	**CRISIL A1+ (Reaffirmed)**

1 crore = 10 million
Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has reaffirmed its 'CRISIL A1+' rating on the commercial paper of Fedbank Financial Services Limited (Fedfina).

The rating continues to be driven by the strategic importance to, and the strong support from, the parent, The Federal Bank Ltd (Federal Bank, rated 'CRISIL A1+'). The rating also factors in comfortable capitalisation. These rating strengths are partially offset by a small scale of operations and limited seasoning of the portfolios.

With nationwide lockdown restrictions being lifted steadily in a phased manner, the degree of relaxations vary across regions depending upon the severity of the Covid-19 pandemic. CRISIL believes that intermittent lockdowns and localised restrictions could delay collections returning to normalcy and put pressure on asset quality metrics.

Fedfina's ability to manage collections and asset quality given the weak macroeconomic environment is a key monitorable amidst the impact on the underlying borrower cash flows. As part of the measures for containing the pandemic, the Reserve Bank of India (RBI) had allowed a moratorium to borrowers with around 25% of them in terms of value availing of the facility as of August 31, 2020. While the collection efficiency was impacted during the initial months of the moratorium, collections have inched up since then. Nevertheless, given the potential challenges in the current environment, Fedfina has made additional provisioning of Rs 42 crore in the first half of fiscal 2021. However, any change in the behaviour of borrowers on payment discipline can affect delinquency levels and will be a key monitorable.

A one-time restructuring scheme announced by the RBI will provide necessary support to affected borrowers in the current environment. Fedfina has restructured aound 1.08% of its Gross advances as on December 31, 2020.

Analytical Approach

For arriving at the rating, CRISIL has assessed the standalone credit risk profile of Fedfina and continues to factor in strong managerial and financial support from the parent Federal Bank. CRISIL believes Federal Bank will continue to provide strong support to Fedfina, considering the strategic importance of the entity and also high moral obligation on account of majority shareholding and shared name.

Key Rating Drivers & Detailed Description

Strengths:

*** Strategic importance to, and strong expectation of support from, the parent**

Fedfina is a subsidiary of Federal Bank and an integral part of Federal Bank's business strategy and will therefore remain strategically important to the bank. Other than equity capital, Federal Bank has also extended a working capital facility of around Rs ~100 crore and term loan of around Rs ~854.3 crore as on December 31, 2020 to Fedfina. Federal Bank also has senior management representation on the board of Fedfina and extends treasury support to the company. The bank and Fedfina also has plans to start co-origination going forward which will further substantiate Fedfina's strategic importance. Benefits from the parent's funding, operational, and management support is expected to continue.

*** Comfortable capitalisation**

The Tier I and overall capital adequacy ratios were 16.81% and 24.06%, respectively, as on September 30, 2020. The parent has, so far, infused capital of Rs 307.8 crore, and held 74% stake as on December 31, 2020. During 2018 and 2019, private equity firm True North had acquired 26% stake in the company in two tranches, the first of which was in November 2018 when True North bought 17.4% stake for Rs 169 crore and the second was in September 30, 2019 for Rs 112 crore. In addition, True North infused equity of Rs 20 crore each in March 2020 and October 2020. Further, True North has the option to acquire upto 45% stake as per the agreement. However, Federal Bank is expected to maintain majority of shareholding over the medium term.

The gearing was at 5.2 times as on September 30, 2020, against 4.7 times as on March 31, 2020, and is expected to remain below 6-6.5 times over the medium term.

Weakness:

*** Small scale of operations**

The company remains a small player in the non-banking financial company (NBFC) sector with an asset base of Rs 4549 crore as on September 30, 2020. It primarily operates in the gold loan and loan against property (LAP) segments. As on September 30, 2020, these constituted 41% and 35% of the advances, respectively, while developer finance and Structured finance (7%), home loans (2%), business loans (7%) and microfinance and personal loans (4%) constitutes the rest. Management intends to focus on retail segments and gradually scale down the developer finance and structured finance portfolio. Over the last few years, it had started lending towards small ticket LAP, microfinance and unsecured business loans. The management's ability to scale up these businesses while maintaining healthy asset quality and profitability will be closely monitored.

*** Limited portfolio seasoning**

Operations in the small ticket LAP, microfinance and unsecured business loan segments commenced only in recent years and the portfolios are yet to season. Gross non-performing assets (NPAs) reduced to 1.13% as on September 30, 2020 from 1.47% in March 31, 2020 primarily on account of improvement in delinquencies in the gold loan portfolio which also partially offset the higher delinquencies in the developer financing segment. Net NPAs were at 0.73% as on September 30, 2020. Performance across asset classes will remain a key monitorable as they gain scale.

Liquidity: Strong

The asset-liability management profile was comfortable, with positive cumulative mismatches in the maturity bucket of up to one year as on December 31, 2020. As on this date, the company had Rs 493 crore debt maturing till March 31, 2021 for which Rs 777 crore liquidity buffer available in terms of unutilized bank line (Rs 310 crore), mutual fund investments (Rs 205 crore), Fixed deposits (Rs 169 crore) and cash & bank balances (Rs 94 crore). The liquidity profile is also supported by the short-term nature of gold loans (around six months) which was 35% of the total portfolio as on September 30, 2020. Liquidity is further cushioned by funding support from the parent Federal Bank.

Rating Sensitivity factors

Downward factors

* Decline in support from Federal Bank, either by way of decline in Federal Bank's ownership in the company below 51% or in the strategic importance of Fedbank Financial Services Ltd to Federal Bank
* Significant and continuous increase in delinquency impacting profitability

About the Company

Fedfina is a subsidiary of Federal Bank, which held 74% stake as on December 31, 2020. During 2018 and 2019, private equity firm True North has acquired 26% stake in the company in two tranches, first tranche of which happened in November 2018 when True North bought 17.4% stake for Rs 169 crore and second tranche which happened in September 30, 2020 for Rs 112 crore. Further, True North has the option to acquire upto 45% stakes in the company as per the agreement.

Fedfina, started as a wholly-owned subsidiary of FBL, is engaged in the distribution of auto and home loans for FBL. It received a non-bank finance company license in 2010, post which, it started gold finance in 2011, LAP finance in 2012 and construction finance in 2014.

In 2019, company has also started microfinance and unsecured business loans. However, management intends to focus on retail segments going ahead and continue to gradually scale down the developer finance and structured finance portfolio. The Company has 359 branches in 12 states all over India as on December 31, 2020; it had a loan portfolio of Rs 4072 crore as on Setpember 30, 2020.

Net profit was Rs 39 crore on total income (net of interest expense) of Rs 265 crore in fiscal 2020 against net profit of Rs 36 crore on total income (net of interest expense) of Rs 142 crore in fiscal 2019. For the six months ended September 30, 2020, net profit stood at Rs 22 crore.

Key Financial Indicators

As on / for the fiscal year ended September 30,	Unit	2020	2019
Total Assets	Rs. crore	4549	2881
Total income (net of interest expense)	Rs. crore	170	100
Profit after tax	Rs. crore	22	17
Gross NPA	%	1.13	1.60*
Overall capital adequacy ratio	%	24.06	21.9*

**As per Indian GAAP*

Any other information: Not applicable

Note on complexity levels of the rated instrument:

CRISIL complexity levels are assigned to various types of financial instruments. The CRISIL complexity levels are available on www.crisil.com/complexity-levels. Users are advised to refer to the CRISIL complexity levels for instruments that they consider for investment. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Annexure - Details of Instrument(s)

ISIN	Name of Instrument	Date of Allotment	Coupon Rate (%)	Maturity Date	Issue Size (Rs.Cr)	Complexity	Rating Assigned with Outlook
NA	Commercial Paper	NA	NA	7-365 days	1000	Simple	CRISIL A1+

Annexure - Rating History for last 3 Years

	Current			2021 (History)		2020		2019		2018		Start of 2018
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Commercial Paper	ST	1000.0	CRISIL A1+		--	23-11-20	CRISIL A1+	15-11-19	CRISIL A1+		--	--
			--		--		--	28-03-19	CRISIL A1+		--	--
Short Term Debt	ST		--		--		--		--	29-03-18	CRISIL A1+	CRISIL A1+

All amounts are in Rs.Cr.

Annexure - Details of various bank facilities

Current facilities			Previous facilities		
Facility	Amount (Rs.Crore)	Rating	Facility	Amount (Rs.Crore)	Rating

Links to related criteria
Rating Criteria for Finance Companies
CRISILs Criteria for rating short term debt
Criteria for Notching up Stand Alone Ratings of Companies based on Parent Support

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