Aavas Financiers Limited

Jan 05, 2021

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	3762.00 (Rs. Three Thousand and seven hundred sixty two crore only)	CARE AA-; Stable [Double A Minus; Outlook: Stable]	Reaffirmed
Long Term sub-ordinated debt	100.00 (Rs. One Hundred crore only)	CARE AA-; Stable [Double A Minus; Outlook: Stable]	Reaffirmed
Proposed Commercial Paper	100.00 (Rs. One Hundred crore only)	CARE A1+	Reaffirmed
Long term Non-Convertible Debentures	795.00 (Rs. Seven hundred and ninety five crore only)	CARE AA-; Stable [Double A Minus; Outlook: Stable]	Reaffirmed

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating reaffirmation of the long-term bank facilities, sub-ordinated debt and non-convertible debentures of Aavas Financiers Limited (AFL) at CARE AA-/Stable and of commercial paper at CARE A1+ factors in strong growth in assets under management (AUM) marked by healthy disbursements with outstanding amount at Rs.8,367 crore as on Sep 30, 2020, high portfolio granularity with average ticket size of Rs 8.4 lacs and healthy profitability metrics with annualized RoTA (Return on total assets) at 2.9% in H1FY21. Also, AFL has comfortable capitalization profile with overall gearing at 2.7 times as on Sep-20. The rating also derives strength from well diversified resource profile of the company as the company raises funds from various sources such as banks, financial institutions, National Housing Bank (NHB) and development financial institutions and via market borrowings at competitive rates, adequate risk management & control systems put in place by the company as well as good growth opportunities in the affordable housing segment. Liquidity remains adequate with no negative cumulative mismatches across the time buckets as on September 30, 2020

These rating strengths, are however, partially offset by the limited, albeit improving, track record of operations and relatively low seasoning of loan portfolio. Also, AFL continues to be geographically concentrated with Rajasthan accounting for 42% of Assets under Management (AUM) as on September 30, 2020 and 75% of portfolio in top three states. Additionally, the exposure to the relatively vulnerable borrowers who are new to credit and have modest credit profile (self-employed borrowers comprising 65% of AUM as on September 30, 2020) makes AFL susceptible to inherent asset quality risks and the asset quality risk is further augmented in the current environment. However, owing to its strong credit appraisal mechanisms, prudent and proactive risk management and control system coupled with enhanced use of technology and analytics, AFL has been able to keep its asset quality under control with GNPA and NNPA at 0.46% and 0.32% respectively as on September 30, 2020. Also, the granular nature of AFL's loan book with more than 99% loans to retail individuals mitigates the credit risk to some extent.

Key rating sensitivities:

Going forward, the ability of the company to grow its loan portfolio, while maintaining asset quality as the book seasons, improving geographical diversification of the portfolio and maintaining healthy profitability and capitalization profile would be key rating sensitivities.

Positive Factors- *Factors that could lead to positive rating action/upgrade*

- Scale up of operations in a sustainable and profitable manner

[1]*Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

- Comfortable asset quality with GNPA on a sustainable basis below 1%
- Comfortable capitalization profile with gearing below 5 times on a sustainable basis

Negative Factors- *Factors that could lead to negative rating action/downgrade*

- Weakness in profitability and/or capitalization profile of AFL with RoTA below 1% and/or steady state gearing rising above 7 times
- Decline in asset quality with GNPA above 3%

Detailed description of the key rating drivers

Key Rating Strengths

Experienced board of directors and management team: AFL is majorly owned by two private equity (PE) investors, post divestment of stake by AU Small Finance Bank (rated CARE AA-; Stable/A1+) in 2016, in order to comply with RBI guidelines for conversion into SFB. The two PE investors – Kedaara Capital and Partners Group, cumulatively held 50.94% shareholding as on September 30, 2020. The board of AFL comprises qualified and experienced personnel who possess strong knowledge in the housing finance domain and includes representatives from both the private equity investors and three independent directors. The management team is headed by Mr Sushil Kumar Agarwal, Founder and Managing Director and Mr. Ghanshyam Rawat, Co-founder and CFO, who are supported by an experienced second line of management with vast experience in the finance and housing finance industry.

Robust capitalization: The capitalization profile of AFL is strong supported by healthy internal accruals and regular equity infusions in the past. The tangible net worth of AFL stood at Rs.2,093 crore and Rs.2,217 crore as on March 31, 2020 and Sep 30, 2020 respectively from Rs.1,833 crore as on March 31, 2019 on account of positive internal accruals. As a result, the overall gearing of AFL stood at 2.7 times as on September 30, 2019 and 2.6 times as on March 31, 2020. The gearing is expected to increase as AFL scales up its operations, although the management intends to maintain gearing below 6 times at all times on a medium to long term basis. The capital adequacy ratio (CAR) of AFL remains strong with Tier 1 and overall CAR of 50.84% and 53.08% respectively as on Sep 30, 2020 which is well above the regulatory requirement at 10% and 13% respectively. The capitalization profile is also supported by lower risk weights assigned on smaller ticket home loans.

Diversified resource profile: The borrowing profile of AFL remains well diversified with funding from banks/FIs (through term loans (36.3% of total borrowings as on September 30, 2020) as well as direct assignment/PTC (23.7%), National Housing Bank (21.7%) and through NCDs and Rupee Dominated Masala Bonds (18.3%). AFL has been able to raise funds at competitive rates from a diverse set of lenders including insurance companies and development financial institutions (DFIs). The average borrowing cost of AFL stood at 7.9% as on Sept 30, 2020 reduced from 8.4% as on March 31st, 2020 (8.7% as on March 31, 2019). During the quarter ended September 30, 2020, AFL borrowed Rs.520 crore with average maturity of around 167 months at 7.0%, of which Rs.194 crore was raised in the form of NHB refinance, Rs.175 crore as term loans from the bank and Rs.151 crore from assignment. Similar to fiscal 2020, AFL did not have any exposure to commercial paper borrowings as on September 30, 2020.

Healthy financial risk profile: Engaged in providing affordable housing finance, AFL has registered strong growth with AUM growing at a five year compounded annual growth rate (CAGR) of 56% from fiscal 2015 till fiscal 2020 primarily driven by denominator effect amid lower base. End fiscal 2020, the AUM of the company stood at Rs.7,796 crore, up 31% Y-o-Y and further to Rs.8,367 crore as on September 30, 2020. During FY20, the housing loan portfolio (forming 75% of the total AUM mix) grew 25% Y-o-Y to Rs.5,859 crore; while the non-housing loan portfolio forming the remaining 25% of portfolio, grew 53% Y-o-Y to Rs.1,937 crore as on March-20. The non-housing loan comprises top-up loans against residential property as well as LAP with average ticket size of about Rs 9 lacs (15.5%). The management aims to keep non-housing loans at around 25% of the total loan book in the medium term.

The profitability remains healthy with AFL reporting net interest margin (NIM) and RoTA of 6.5% and 3.7% respectively in FY20, broadly in line with profitability metrics at 7.0% and 3.6% respectively at the end of previous fiscal. The operating expense of the company (as a % of average total assets) marginally reduced to 3.5% end fiscal 2020 as against 3.9% in FY19 as the company is achieving economies of scale. Also, credit cost for the company, though rising on account of Covid 19 and its impact on the collections of the company, has remained controlled at 0.23% as on March 31, 2020 on the back of good asset quality. For the half year ending September 30, 2020, the company reported profit after tax (PAT) of Rs.116 crore on net interest income of Rs.246 crore as against PAT of Rs. 121 crore and net interest income of Rs.206 crore for the corresponding period last year. The company reported annualized NIM and RoTA at 6.1% and 2.9% respectively as on September 30, 2020.

Comfortable asset quality, though could be moderated in light of Covid-19: The asset quality ratios of AFL remains comfortable with GNPA and NNPA at 0.47% and 0.32% respectively as on Sep 30, 2020. While there has been some rise in absolute GNPA to Rs.31.27 as on Sep-20 (increased from Rs.28.41 crore as on March 31, 2020), the asset quality ratios are comfortable. The provision coverage ratio (PCR) improved to 32.4% as on Set 30, 2020 from 26% as on March-20, as the company made additional provisions on account of covid-19 impact on the collections.

It is to be noted that in addition to reported NPA levels, delinquency level of AFL in softer buckets (1+dpd) has remained relatively low at 2.4% March 31, 2020, partially due to dpd freeze arising out of moratorium on payments due to borrowers as announced by Reserve Bank of India. However, in the backdrop of Covid-19 pandemic-led economic slowdown and subsequent moratorium, there has been rise in 1+dpd to 6.2% as on Sep-20 underpinned by some concerns in Maharashtra that saw stricter lockdowns. However, since the slippage to 90+dpd is about 5.6% (of 1+dpd) as on Sep-20, the overall asset quality remains under control.

The asset quality profile of the company is further supported by strong control systems and low loan to value (LTV) ratios with about 63% of loan book at LTVs of less than 60% and only 5% of loan book greater than 80% LTV as on Sep 30, 2020. Also, about two thirds of the book had fixed obligation to income ratio (FOIR) below 50%. The average ticket size of both housing and non-housing products remain sub-Rs 10 lacs thereby imparting granularity. The company has so far demonstrated strong ability to recover its over-dues under demonetization, RERA and GST implementation, though asset quality performance through different economic cycles and geographies is yet to be established.

Key Rating Weaknesses

Low seasoning of loan portfolio; albeit improving and exposure to relatively vulnerable borrower segment: Since its inception in 2012, AFL has registered strong portfolio growth and the seasoning of loan portfolio, though low, has been on an improving trend. As an affordable housing finance company, AFL is focused on providing secured retail home loans to low income borrowers in semi-urban and rural regions, with majority of them having undocumented incomes. The customers of AFL are a mix of self-employed (65% of AUM as on September 30, 2020) and remaining 35% as salaried borrowers with majority of them in tier 2 to tier 6 cities; thereby exposing the company to the relatively economically vulnerable borrower segment. Since this segment is highly susceptible to the impact of economic downturn, maintaining good asset quality while increasing the scale of operations is a key sensitivity. However, the company has put in place adequate credit appraisal mechanisms and integrated MIS systems. The company has enhanced its risk management system with the use of technology and analytics; which has resulted in better operating efficiencies, effective monitoring of collections and better asset quality.

Geographical concentration: While the company has presence in eleven states, the state-wise geographic concentration remains high with Rajasthan alone accounting for 42% of the AUM as on September 30, 2020 (down from 44% as on Sep 30, 2019) and top three states (Rajasthan, Maharashtra and Gujarat) together accounting for 75% of AUM as on Sep-20. However to counter the concentration risk, the company has been deepening its presence in existing states with opening of new branches at district/tehsil level. The geographic concentration is expected to further come down as the company plans to expand its operations in other geographies. As of September 30, 2020, company has presence in 11 states with 259 branches covering around 215 districts and 1100 tehsils.

Liquidity: Strong

AFL has well matched the tenure of its housing loan book and that of its borrowings, rendering liquidity profile of the company very comfortable with no negative cumulative mismatches across the time buckets as on March 31, 2020. Over the next six months (Oct-20 to Mar-21), the company expects repayment from loan book of Rs.642 crore while its debt repayment will be around Rs.207 crore. Moreover, the company had liquidity in the form of cash and cash equivalents of Rs 1,575 crore and sanctioned but unutilized lines of Rs 1012 crore as on September 30, 2020.

Covid-19 impact

AFL has not requested for moratorium from any of its lenders and the company has provided moratorium to its customers on Opt-in basis. Company's exposure under moratorium was 24% as of April-20 and only 6.2% of AUM was at 1+DPD as of Sep-20. There has been an increase in the delinquencies in softer buckets and improvement of the same remains to be seen. The company made total disbursements of Rs.880 crore in H1FY21, down 33% Y-o-Y from corresponding period of last fiscal although in Q2 FY 21, the disbursements stood at Rs 667 crore, up 4% Y-o-Y thereby suggesting normalization in business to around pre-covid levels

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology - Non Banking Finance Companies (NBFCs)
Financial Ratios – Financial Sector
Criteria for Short Term Instruments
Rating Methodology - Housing Finance Companies (HFCs)

About the Company

Aavas Financiers Ltd, a housing finance company, was incorporated in February 2011 as a subsidiary of AU Small Finance Bank (rated CARE AA-; Stable). It got the NHB License – Certificate of Registration on Aug 04, 2011 and commenced operations from March 2012. In June 2016, to comply with RBI guidelines, AU SFB divested majority of its shareholding to two private equity players – Kedaara Group and Partners Group. As on September 30, 2020, Kedaara Group holds 30.31 % stake in AFL, Partners Group holds 20.63% stake, AU SFB held 4.57% and remaining 44.49% is held by public including management team of AFL. The tangible net-worth of the company improved to Rs.2,217 crore as on Sep 30, 2020 from Rs.1,833 crore as on March 31, 2019 on account of positive internal accruals.

AFL is engaged in providing retail home loans with focus on affordable housing segment to customers in semi-urban and rural regions. As on September 30, 2020, the company operates through a network of 259 branches in 11 states of Rajasthan, Gujarat, Madhya Pradesh, Maharashtra, Delhi, Uttar Pradesh, Haryana, Punjab, Chattisgarh, Uttrakhand and Himachal Pradesh.

Brief Financials (Rs. crore)	**FY19 (A)**	**FY20 (A)**
Total operating income	710.9	903.1
PAT	175.9	249.1
Interest coverage (times)	2.0	1.9
Total Assets*	5,623.1	7,653.5
Net NPA (%)	0.37	0.34
ROTA (%)	3.6	3.8

*A: Audited, *Total assets are adjusted for DTA and intangible assets*

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*
Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	-	March 2030	3762.00	CARE AA-; Stable
Debt-Subordinate Debt	INE216P08017	Dec-22-2017	9.74%	Dec-22-2023	100.00	CARE AA-; Stable
Debentures-Non Convertible Debentures	INE216P07167	Sep-16-2019	8.39%	Sep-15-2024	345.00	CARE AA-; Stable
Debentures-Non Convertible Debentures	INE216P07175	Mar-30-2020	8.65%	30-Mar-2028	444.40	CARE AA-; Stable
Debentures-Non Convertible Debentures	Proposed				5.60	CARE AA-; Stable
Commercial Paper-Commercial Paper (Standalone)	Proposed				100.00	CARE A1+

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Commercial Paper-Commercial Paper (Standalone)	ST	100.00	CARE A1+	-	1)CARE A1+ (06-Jan-20)	1)CARE A1+ (25-Mar-19)	1)CARE A1+ (29-Aug-17)
2.	Fund-based - LT-Term Loan	LT	3762.00	CARE AA-; Stable	-	1)CARE AA-; Stable (27-Mar-20) 2)CARE AA-; Stable (06-Jan-20) 3)CARE AA-; Stable (30-Jul-19) 4)CARE AA-; Stable (15-Jul-19)	1)CARE AA-; Stable (25-Mar-19) 2)CARE AA-; Stable (01-Mar-19)	1)CARE A+; Positive (22-Mar-18)
3.	Debt-Subordinate Debt	LT	50.00	CARE AA-;	-	1)CARE AA-; Stable	1)CARE AA-; Stable	1)CARE A+; Stable (29-Aug-17)

				Stable		(06-Jan-20)	(25-Mar-19)	
4.	Debt-Subordinate Debt	LT	50.00	CARE AA-; Stable	-	1)CARE AA-; Stable (06-Jan-20)	1)CARE AA-; Stable (25-Mar-19)	1)CARE A+; Stable (11-Dec-17)
5.	Debentures-Non Convertible Debentures	LT	375.00	CARE AA-; Stable	-	1)CARE AA-; Stable (06-Jan-20) 2)CARE AA-; Stable (31-May-19)	-	-
6.	Debentures-Non Convertible Debentures	LT	420.00	CARE AA-; Stable	-	1)CARE AA-; Stable (06-Jan-20) 2)CARE AA-; Stable (13-Dec-19)	-	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not Applicable

Annexure 4: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Commercial Paper-Commercial Paper (Standalone)	Simple
2.	Debentures-Non Convertible Debentures	Simple
3.	Debt-Subordinate Debt	Complex
4.	Fund-based - LT-Term Loan	Simple

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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About CARE Ratings:

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