Aavas Financiers Limited

October 06, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	6752.00 (Enhanced from 6,552.00)	CARE AA; Stable	Reaffirmed
Long-term cash credit	110.00	CARE AA; Stable	Reaffirmed
LT – subordinated debt	50.00	CARE AA; Stable	Reaffirmed
LT – subordinated debt	50.00	CARE AA; Stable	Reaffirmed
LT – NCD	375.00	CARE AA; Stable	Reaffirmed
LT – NCD	420.00	CARE AA; Stable	Reaffirmed
LT – NCD	200.00	CARE AA; Stable	Reaffirmed
ST Instruments - Proposed commercial paper (CP)	100.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The rating reaffirmation for the various instruments of Aavas Financiers Limited (AFL) derives strength from its experienced management team, established track record of maintaining good asset quality along with portfolio growth, strong capitalisation and comfortable liquidity profile of the company with no negative cumulative mismatches across time buckets as per the asset liability maturity (ALM) statement dated June 30, 2023. While reaffirming the rating, CARE Ratings Limited (CARE Ratings) has considered the company's entire debt profile and the company's ability to raise funds from various sources at competitive rates.

The ratings also factor in the healthy profitability metrics, high portfolio granularity and adequate risk management and control systems put in place by the company as well as good growth opportunities in the affordable housing segment.

These rating strengths are, however, offset by relatively vulnerable target borrower profile of AFL with majority of customers being new to mortgage with having modest credit profile (self-employed borrowers comprising 60% of asset under management [AUM] as on June 30, 2023), which makes AFL susceptible to the inherent asset quality risks. However, owing to granularity of loan book with low loan to value ratio (average LTV-54%), 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.

Furthermore, AFL continues to have geographically-concentrated portfolio, with Rajasthan accounting for about 37% of AUM as on June 30, 2023, though reduced from 47% as on June 30, 2018.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors – Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Significant scale-up of operations in a sustainable and profitable manner.
- Significant improvement in geographical diversification.
- Comfortable asset quality with credit cost under control on a sustained basis.

Negative factors – Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Weakness in profitability of AFL with return on total assets (RoTA) below 2.5% on a continuous basis.
- Any sharp variation in portfolio mix.
- Weakness in capitalisation profile with gearing rising above 7x.

Analytical approach: Standalone

Outlook: Stable

The Stable outlook reflects CARE Ratings' expectation that Aavas financiers Limited will continue to grow the loan book while maintaining the asset quality under control.

Detailed description of the key rating drivers:

Key strengths

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Experienced board of directors and management team: AFL is majority owned by two private equity (PE) investors, Kedaara Capital and Partners Group, who cumulatively held 39.74% shareholding as on June 30, 2023. The board of AFL includes representatives from both the private equity (PE) investors and three independent directors. The management team is headed by Sachinder Bhinder, Managing Director & CEO, (earlier with the company as CEO of Aavas Fin Serv, heading micro, small & medium enterprises (MSME) and Government-led affordable housing business for the last three years) and Ghanshyam Rawat, President and CFO, who are supported by an experienced second line of management with vast experience in the finance and housing finance industry. Previously, the role of MD and CEO was carried on by Sushil Agarwal, who moved out of the organisation on May 03, 2023.

Going forward, with the growing scale of operations, the Board plans on horizontally expanding the management strength and as of now 10+ CXOs are there in the company.

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 (TNW) of AFL stood at ₹3,245 crore as on March 31, 2023, up from ₹2,803 crore as on March 31, 2022 which further increased to ₹3,389 crore as on June 30, 2023, on account of positive internal accruals. The company's gearing also stood comfortable at 2.8x as on March 31, 2022, 3x as on March 31, 2023 and 3.16x as on June 30, 2023. While the gearing is expected to increase with incremental business being funded with fresh borrowings, CARE Ratings expects gearing to remain below 6x in the medium to long term.

The capital adequacy ratio (CAR) of AFL also remains strong with Tier-1 and overall CAR of 47.02% and 47.32%, respectively, as on June 30, 2023, which is well above the regulatory requirement. The capitalization profile is also supported by lower risk weights assigned on smaller ticket home loans and secured nature of portfolio. CARE Ratings expects that comfortable capitalization profile of AFL will provide buffer against asset quality related shocks, if any.

Diversified resource profile: AFL's funding profile remains diversified over the past few years with funding from banks/financial institutions (FIs) (through term loans amounting to 46.6% of the total borrowings as on June 30, 2023), refinance from National Housing Bank (NHB; 21.1%) and through non-convertible debentures (NCDs) (11.1%). Furthermore, AFL's funding position remains adequate due to strong relationship with all the leading banks of the country such as Punjab National Bank (PNB), State Bank of India (SBI), HDFC Bank Ltd. and funding support from various international agencies, such as Asian Development Bank (ADB), International Finance Corporation (IFC), and British International Investment (Erstwhile known as CDC) as on June 30, 2023.

The average borrowing cost of AFL (reported) stood at 6.64% as on March 31, 2023, and 7.28% as on June 30, 2023. Furthermore, AFL has no dependency on short-term commercial paper funding. The company borrowed funds at an interest rate of around 8.01% in Q1FY24.

Healthy financial risk profile: Engaged in providing affordable housing finance, AFL has registered strong growth with assets under management (AUM) growing at a five-year compounded annual growth rate (CAGR) of 28% from fiscal 2018 till fiscal 2023 primarily driven by low base. The housing loan portfolio comprises 70% of the total AUM while the remaining 30% belongs to mortgage-backed non-housing portfolio, primarily Loan Against Properties (LAP) and MSME loans with average ticket size of ₹7.4 lakh as on June 30, 2023. Furthermore, although the non-housing loan portfolio increased to 30% as on June 30, 2023, it is in compliance with the Reserve Bank of India (RBI) guidelines for maintaining the minimum proportion between housing and non-housing loan to 60:40. The management aims to keep non-housing loans at around the similar level of the total loan book in the medium term.

The profitability remains healthy with the net interest margins (NIMs) of 6.5% in FY23 and Q1FY24. However, operating expenses to average assets ratio increased to 3.75% in FY23 vs. 3.5% in FY22 and further increased to 3.85% in Q1FY24, due to digital and analytical upscaling. This, coupled with low credit cost of 0.1% in FY23 and 0.16% in Q1FY24, the company has reported a RoTA of 3.53% in FY23 and 3.16% in Q1FY24. Going forward, CARE Ratings expects NIMs to decline from the current levels on account of rising interest rate scenario which is expected to lead to higher cost of borrowing and increase in gearing.

Asset quality under control: AFL has continued to report healthy asset quality metrics with gross non-performing asset (GNPA) ratio of 0.92% and net non-performing assets (NNPA) ratio of 0.68% as of March 31, 2023, as compared to gross non-performing asset (GNPA) ratio of 0.99% and net non-performing asset (NNPA) ratio of 0.76% as on March 31, 2022, respectively. As on June 30, 2023, the GNPA ratio has moderately increased to 1% and net non-performing assets (NNPA) ratio of 0.73%, however it remains under control.

Furthermore, with improved collection and underwriting system, delinquency level of AFL in softer buckets (1+dpd) also stands comfortable with 1+dpd of 3.68% as on June 30, 2023 and 3.30% end-March 31, 2023, down from the level of 4.5% as on March 31, 2022. The provision coverage ratio (PCR) on GNPA stood at 27% March 31, 2023.

The asset quality profile of the company is, supported by strong control systems and low LTV ratios, with average LTV at about 54% end-March 31, 2023. Also, given the secured nature of the lending with comfortable LTV ratio at origination, most of the properties being self-occupied, and the company being covered under the SARFAESI Act., losses, in case of defaults, are expected to be limited.

Key weaknesses

Exposure to relatively vulnerable borrower segment: AFL's portfolio size remains moderate compared to large, rated players in the housing finance industry. As an affordable housing finance company, AFL is focused on providing secured retail home loans to low- and middle-income borrowers in semiurban and rural regions, with majority of them having lack of formal income documents. The customers of AFL are a mix of self-employed (60% of AUM as on June 30, 2023) and the remaining 40% as salaried borrowers with majority of them in Tier-2 to Tier-5 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. The company has put in place adequate credit appraisal mechanisms and integrated MIS systems.

The company has a target to invest substantially in improving and advancing technology. Although, this has led to higher operational expenses, the use of technology and analytics will result in better operating efficiencies, standardisation of process across all geographies and effective monitoring of assets quality geography and enhance their risk management system. With the transition in technology, the company has implemented Salesforce platform, which earlier started as a pilot project in March 2023, and then launched in April 2023. The company has also added tools like Mule soft which is then blended with their analytical models. AFL has made transformations in its middle office systems by implementing Oracle Flex Cube and Oracle Fusion on Oracle Cloud to create their system more robust. With these implementations, the company plans to see the significant reduction in turnaround time (TAT). Going forward, its ability to scale up the loan book while maintaining asset quality remains key monitorable.

High geographical concentration, though improving: While the company has presence in 13 states, the state-wise geographic concentration remains high with Rajasthan alone accounting for 37% of the AUM as on June 30, 2023, and top three states (Rajasthan, Maharashtra, and Gujarat) together accounting for 68% of AUM as on June 30, 2023, reduced from 47% concentration in Rajasthan and 83% concentration in top three states as of June 30, 2018. However, the company has been deepening its presence in the 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. The company plans on growing Karnataka, Odisha, and Uttar Pradesh and will continue to grow deeper into their existing geographies.
As on June 30, 2023, the company has presence in 13 states with 348 branches and has added 32 new branches in the last 12 months.

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 June 30, 2023. The liquidity stands strong with cash equivalents of ₹2,034 crore and sanctioned but un-availed bank lines to the tune of ₹1,160 crore as on June 30, 2023 against the debt liability of ₹1,196 crore for the next six months.

Environment, social, and governance (ESG) risks
AFL intends to build a strategic approach where environment, social and governance fundamentals are embedded into the business. For this, company has entered into a partnership with International Finance Corporation (IFC), a member of the World Bank Group, to promote the affordable 'green homes' in India with the help of environmental-friendly architecture of individual homes. Around 5,000+ customers have shown their interest for building a Green Home and willingly committed to use one or more green and sustainable measures in their homes.

Furthermore, the company has aligned their corporate social responsibility (CSR) strategy with sustainable development goals of the 2030- Global Agenda for Sustainable Development adopted by all UN Member States, with extensive initiatives in the areas of public healthcare, climate action, rural development, sport and quality education.

Applicable criteria

Policy on default recognition
Financial Ratios - Financial Sector
Rating Outlook and Credit Watch
Short Term Instruments
Housing Finance Companies
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro Economic Indicator	Sector	Industry	Basic Industry
Financial Services	Financial Services	Finance	Housing Finance Company

AFL, a housing finance company, was incorporated in February 2011 as a subsidiary of AU Small Finance Bank (rated 'CARE AA; Stable'). It received the NHB License – Certificate of Registration on August 04, 2011 and commenced operations from March 2012. In June 2016, to comply with the RBI guidelines, AU SFB divested majority of its shareholding to two private equity players – Kedaara Group and Partners Group. As on June 30, 2023, the Kedaara group holds 23.61% stake in AFL, the Partners Group holds 16.13% stake, and the remaining 60.26% is held by the public, including management team of AFL and marquee investors. AFL is engaged in providing retail home loans with focus on affordable housing segment to customers in semi-urban and rural regions. As on June 30, 2023, the company operates through a network of 348 branches in 13 states – Rajasthan, Maharashtra, Gujarat, Madhya Pradesh, Delhi, Haryana, Punjab, Chhattisgarh, Uttar Pradesh, Uttarakhand, Himachal Pradesh, Odisha and Karnataka.

Brief Financials (₹ crore)	March 31, 2022 (A)	March 31,2023 (A)	Q1 FY2024 (UA)
Total operating income	1,305.56	1,610.15	466.85
PAT	356.8	430.07	109.71
Interest coverage (times)	1.95	1.93	1.75
Total assets*	11,014.59	13,386.00	14,399.20
Net NPA (%)	0.76	0.68	0.73
ROTA (%)	3.57	3.53	3.16

A: Audited UA: Unaudited; Note: 'the above results are latest financial results available'*excludes Deferred tax assets 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: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Cash credit		-	-	-	110.00	CARE AA; Stable
Fund-based - LT-Term loan		-	-	15-Feb-38	6752.00	CARE AA; Stable
Long-term subordinate debt	INE216P08017	22-Dec-2017	9.24%	22-Dec-23	100.00	CARE AA; Stable
Non-convertible debentures	INE216P07167	16-Sep-2019	NA	15-Sep-24	345.00	CARE AA; Stable
Non-convertible debentures	INE216P07175	30-Mar-2020	NA	30-Mar-28	444.40	CARE AA; Stable
Non-convertible debentures	INE216P07225	25-Mar-2022	Repo rate linked	25-Mar-27	100.00	CARE AA; Stable
Non-convertible debentures	INE216P07217	26-Nov-2021	Repo rate linked	26-Nov-26	99.00	CARE AA; Stable
Non-convertible debentures	Proposed	-	-	-	6.60	CARE AA; Stable
Commercial Paper (Standalone)	Proposed	-	-	-	100.00	CARE A1+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Commercial paper-Commercial paper (Standalone)	ST	100.00	CARE A1+	1)CARE A1+ (06-Jul-23)	1)CARE A1+ (21-Mar-23) 2)CARE A1+ (28-Dec-22) 3)CARE A1+ (13-Sep-22) 4)CARE A1+ (05-Apr-22)	1)CARE A1+ (05-Oct-21)	1)CARE A1+ (05-Jan-21)

2	Fund-based - LT-Term loan	LT	6752.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22) 3)CARE AA; Stable (13-Sep-22) 4)CARE AA-; Positive (05-Apr-22)	1)CARE AA-; Positive (05-Oct-21)	1)CARE AA-; Stable (05-Jan-21)
3	Debt-Subordinate debt	LT	50.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22) 3)CARE AA; Stable (13-Sep-22) 4)CARE AA-; Positive (05-Apr-22)	1)CARE AA-; Positive (05-Oct-21)	1)CARE AA-; Stable (05-Jan-21)
4	Debt-Subordinate debt	LT	50.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22) 3)CARE AA; Stable (13-Sep-22)	1)CARE AA-; Positive (05-Oct-21)	1)CARE AA-; Stable (05-Jan-21)

						4)CARE AA-; Positive (05-Apr-22)		
5	Debentures-Non-convertible debentures	LT	375.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22) 3)CARE AA; Stable (13-Sep-22) 4)CARE AA-; Positive (05-Apr-22)	1)CARE AA-; Positive (05-Oct-21)	1)CARE AA-; Stable (05-Jan-21)
6	Fund-based - LT-Cash credit	LT	110.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22) 3)CARE AA; Stable (13-Sep-22) 4)CARE AA-; Positive (05-Apr-22)	-	-
7	Debentures-Non-convertible debentures	LT	420.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22)	1)CARE AA-; Positive (05-Oct-21)	1)CARE AA-; Stable (05-Jan-21)

						3)CARE AA; Stable (13-Sep-22) 4)CARE AA-; Positive (05-Apr-22)		
8	Debentures-Non-convertible debentures	LT	200.00	CARE AA; Stable	1)CARE AA; Stable (06-Jul-23)	1)CARE AA; Stable (21-Mar-23) 2)CARE AA; Stable (28-Dec-22) 3)CARE AA; Stable (13-Sep-22) 4)CARE AA-; Positive (05-Apr-22)	1)CARE AA-; Positive (18-Nov-21)	-

*Long term/Short term.

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

Annexure-4: Complexity level of the various instruments rated

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-Cash credit	Simple
5	Fund-based - LT-Term loan	Simple

Annexure-5: Lender details

To view the lender-wise details of bank facilities please click here

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

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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