Fedbank Financial Services Limited (Revised)

October 06, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term/Short-term bank facilities	7,500.00 (Enhanced from 3,000.00)	CARE AA; Stable / CARE A1+	Reaffirmed
Subordinate debt	350.00	CARE AA; Stable	Reaffirmed
Non-convertible debentures	250.00	CARE AA; Stable	Assigned
Non-convertible debentures	12.50 (Reduced from 200.00)	CARE AA; Stable	Reaffirmed
Non-convertible debentures	200.00	CARE AA; Stable	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

CARE Ratings Limited (CARE Ratings) has reaffirmed/assigned the ratings of Fedbank Financial Services Limited (Fedfina). The ratings factor Fedfina's stable operating performance along with its comfortable liquidity position. The ratings also factor in the company's demonstrated ability to raise funds at competitive rates and continued support from its, parent Federal Bank Limited (FBL, rated 'CARE AA+; Stable'). The company being a subsidiary of FBL enjoys the benefits of shared brand name along with financial and operational support from its parent. CARE Ratings also derives comfort from the high degree of management integration with senior management representation of FBL on the board of Fedfina. Nonetheless, the ratings remain constrained by the limited portfolio seasoning of the recently acquired portfolio, high leverage, and geographical concentration.

CARE Ratings notes that Fedfina's ability to scale up its operations while improving its profitability and maintaining resilient asset quality and ability to infuse additional equity will remain a key monitorable. Besides, any moderation in linkage with the parent, FBL, resulting in reduced intent and ability to support Fedfina in future also remains a key monitorable.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Significant scale-up of operations with maintenance of resilient asset quality and sound profitability.
- Significant improvement in credit profile of the parent.
- Comfortable leverage on a sustained basis.

Negative factors

- Any change in the ownership structure resulting in reduction in FBL's stake in Fedfina below 51% or moderation in Fedfina's linkage with FBL.
- Significant weakening of parent's credit profile.
- Gearing level above 6x on a sustained basis.
- Significant deterioration in the asset quality of Fedfina with gross non-performing assets (GNPA) exceeding 6% on a sustained basis.

Analytical approach:

CARE Ratings has analysed the standalone credit profile of Fedfina factoring operational and managerial linkages with its parent, FBL. Fedfina enjoys the benefits of a shared brand name besides operational and managerial linkages with the parent.

Outlook: Stable

Stable outlook has been assigned to Fedfina on account of stable operations and consistent earning profile of the company.

Detailed description of the key rating drivers:

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

Key strengths

Strong parentage and their continued support

Fedfina is a subsidiary of FBL which holds 73.22% ownership in the company as on June 30, 2023. True North, a private equity (PE) player, holds 25.72% stake acquired in two tranches in 2018 and 2019. The balance 1.06% is held by individuals. The parent, FBL, has been infusing growth capital in Fedfina from time-to-time. So far, it has infused capital of around ₹456 crore, and True North has infused capital of around ₹375 crore to support growth in the operations. CARE Ratings expects FBL to maintain majority shareholding in Fedfina over the medium term.

Fedfina not only enjoys the benefits of a shared brand name but also has operational and managerial linkages with its parent. The strategic importance of Fedfina to FBL is evident from the management integration, wherein the Managing Director and CEO as well as the Executive Director of FBL are on Fedfina's Board. In addition to capital support through equity infusion, Fedfina also enjoys financial flexibility in the form of funding lines from FBL. As on June 30, 2023, Fedfina has total sanctioned limits of ₹1,600 crore from FBL.

Improving profitability matrices

The overall profitability of the company improved in FY23 with profit after tax (PAT) margin increasing to 14.83% during FY23 from 11.71% in FY22. The improvement is on account of increase in net interest margin (NIM) which improved with increase in yield on advances, other income on account of net gain on sale of investments, and decreased credit cost. Opex as a percentage of average total assets increased by 40 bps to 5.68% in FY23 from 5.28% in FY22 owing to expansion of the branch network, hiring of new employees, technology upgradation, and strengthening the collections process. Going forward, the opex as a percentage of total assets will decline as the company will benefit from the operating leverage. The PAT margin remained rangebound at 14.65% in Q1FY24 against 14.83% in FY23 with some increase in the operating cost.

Sustenance of moderate asset quality

As on March 31, 2023, the asset quality metrics have improved with GNPA and net NPA (NNPA) of 2.03% (FY22: 2.23%) and 1.59% (FY22: 1.75%), respectively. The improvement in asset quality is on account of recoveries and write-offs. However, as of June 2023, on account of some slippages in the medium ticket size loan against property (LAP) book, GNPA and NNPA increased to 2.26% and 1.76%, respectively. The current NPA levels are not fully reflective of the asset quality due to limited seasoning of the overall loan portfolio.

Key weaknesses

Geographic concentration risk

While the company has presence in over 16 states, the state-wise geographic concentration remains high with 48% of the asset under management (AUM) vested in top three states Maharashtra, Karnataka, and Tamil Nadu, as on June 30, 2023. On similar lines, LAP as well as home loans are concentrated in southern India. Business loans have major concentration in the state of Maharashtra, Delhi, and southern India. CARE Ratings notes that the company has adequate monitoring mechanisms in place to review performance of each geography and manage and mitigate this risk in a timely manner.

Moderate portfolio seasoning

Fedfina has expanded into newer products and geographies over the years and is currently in its growth phase with an AUM of ₹9,069.31 crore as on March 31, 2023, as against AUM of ₹6,187 crore as on March 31, 2022. Furthermore, AUM increased to ₹9,434.21 crore as on June 30, 2023. The new additions to the portfolio like medium-ticket LAP and small-ticket LAP have low seasoning with an average behavioural tenure of around four years and eight years, respectively. The operations in the small-ticket LAP and unsecured business loan segments, are yet to see complete lifecycle, thus, portfolio seasoning remains a key monitorable.

High leverage

Due to the increase in operations funded by additional borrowings, gearing increased to 5.36x in FY23 as against 4.48x in FY22. This happened mainly due to delay in additional equity infusion. Earlier, the company had planned to raise equity by way of IPO or fund raise from PE. It had also filed DRHP for IPO which was valid till May 13, 2023. However, considering the slowdown in capital market impacting the valuations, the company delayed the plan of equity infusion. The company has again filed a DRHP for IPO in July 2023 in view of better macro conditions, and is expected to receive the approval in October 2023, post which it plans to get listed by December 2023.

Currently, to reduce the overall capital requirement, the company is planning to do co-lending with banks for gold loan and LAP and resorting to securitisation of loans. Thus, by way of incremental co-lending, direct assignment, calibrated originations, and potential equity raise, the company will maintain leverage below 6x in the near term. CARE Ratings notes that increasing scale of operations while maintaining healthy gearing and timely equity infusion to support growth operations by the company will remain a key monitorable. Overall, the capital adequacy ratio (CAR) stood comfortable at 19.71% and Tier I CAR: 14.70%, well above regulatory requirement of 15% and 10%, respectively.

Liquidity: Adequate
As on June 30, 2023, the asset liability management (ALM) statement exhibits no negative cumulative mismatches. The company's cash, bank, and liquid investments amount to ₹844 crore as on June 30, 2023, with inflows for the next one year amounting to ₹3,974 crore. Additionally, the company has undrawn credit lines to the extent of ₹547 crore. Against this, the company has the debt obligations of ₹2,638 crore to be paid for the next one year, indicating the company is adequately funded to repay its debt.

Applicable criteria

Policy on default recognition
Factoring Linkages Parent Sub JV Group
Financial Ratios - Financial Sector
Rating Outlook and Credit Watch
Short Term Instruments
Non Banking Financial 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	Investment Company

Fedbank Financial Services Limited (Fedfina) is a non-deposit accepting, systemically important non-banking finance company (NBFC-ND-SI). The company was incorporated in the state of Kerala in April 1995 and commenced operations in August 2010 after receiving the NBFC license from RBI. It is primarily engaged in the lending business with a diversified portfolio consisting of gold loans, loan against property, home loans and business loans. Fedfina is a retail-focused NBFC promoted by Federal Bank Limited (FBL). FBL, a commercial bank with significant presence in the private sector holds 73.22% stake in Fedfina along with True North Fund, a renowned PE firm based in Mumbai, that holds the other 25.72% stake through its fund (True North Fund VI LLP) as of June 2023.

Brief Financials (₹ crore)	March 31, 2022 (A)	March 31, 2023 (A)	Q1FY24 (UA)
Total operating income	883.64	1,214.67	367.87
PAT	103.46	180.13	53.88
Interest coverage (times)	1.40	1.51	1.44
Total assets	6,401.45	8,934.03	NA
Net NPA (%)	1.75	1.59	1.76
ROTA (%)	1.75	2.35	NA

A: Audited UA: Unaudited NA: Not available; Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA:
None

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	Coupon Rate (%)	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Debentures-Non-convertible debentures	INE007N07041	26-Jun-2023	3M SBI MCLR	26-Jun-2027	200.00	CARE AA; Stable
Debentures-Non-convertible debentures (Proposed)	-	-	-	-	262.50	CARE AA; Stable
Debentures-Non-convertible debentures	INE007N07017	18-Jun-2020	9.00%	18- Jun-2023	0.00	Withdrawn
Debt-Subordinate debt	INE007N08023	26-May-2023	9.00%	26-Apr-2030	200.00	CARE AA; Stable
Debt-Subordinate debt (Proposed)	-	-	-	-	150.00	CARE AA; Stable
LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	-	-	-	-	2,950.63	CARE AA; Stable / CARE A1+
LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC (Proposed)	-	-	-	-	4,549.37	CARE AA; Stable / 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	Fund-based-Long term	LT	-	-	-	-	-	1)Withdrawn (31-Mar-21) 2)CARE AA-; Stable (31-Mar-21) 3)CARE AA-; Negative (29-Apr-20)
2	Debentures-Non-convertible debentures	LT	12.50	CARE AA; Stable	1)CARE AA; Stable (12-May-23)	1)CARE AA; Stable (27-Dec-22)	1)CARE AA-; Stable (20-Jan-22)	1)CARE AA-; Stable (31-Mar-21) 2)CARE AA-; Negative (29-Apr-20)
3	LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	LT/ST*	7500.00	CARE AA; Stable / CARE A1+	1)CARE AA; Stable / CARE A1+ (12-May-23)	1)CARE AA; Stable / CARE A1+ (27-Dec-22)	-	-
4	Debt-Subordinate debt	LT	350.00	CARE AA; Stable	1)CARE AA; Stable (12-May-23)	-	-	-
5	Debentures-Non-convertible debentures	LT	200.00	CARE AA; Stable	1)CARE AA; Stable (12-May-23)	-	-	-
6	Debentures-Non-convertible debentures	LT	250.00	CARE AA; Stable				

*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	Debentures-Non-convertible debentures	Simple
2	Debt-Subordinate debt	Complex

3	LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	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:
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