Fusion Finance Limited

October 04, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	1,500.00	CARE A; Negative	Downgraded from CARE A+; Stable

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The downgrade of Fusion Finance Limited's (FFL) bank facilities reflects an unexpected sharp deterioration in the company's asset quality, which negatively impacted its profitability metrics. CARE Ratings Limited (CARE Ratings) observes that the overall microfinance industry is experiencing a significant rise in delinquencies, largely due to increasing borrower indebtedness and different contributing factors, including heatwaves, general elections, and political initiatives like the "Karja Mukti Abhiyan." Additionally, challenges such as the weakening of Joint Liability Group model, decreased centre attendance, and high staff turnover have severely affected collection efficiency. However, deterioration in FFL's asset quality is much higher than the other MFI players.

In light of these pressures, FFL reported a decline in asset quality, with gross non-performing assets (GNPA) ratio rising from 2.89% as on March 2024 to 5.46% as on June 2024. In Q1 FY25, the company also set aside an additional ₹208 crore (total provision as on Jun-24 is ₹348 crore) in provisions, resulting in a negative profit after tax (PAT) of ₹36 crore for the quarter. On September 21, 2024, FFL announced that it may need to create further provisions of ₹500-550 crore in Q2 FY25, leading CARE Ratings to anticipate significantly higher losses in the first half of FY25. Further, significant rise in the provisioning leading to deterioration of profitability will remain a key monitorable.

In their latest announcement, FFL stated that they will appoint a new CEO to strengthen the executive leadership team. Devesh Sachdev, the current Managing Director (MD) and Chief Executive Officer (CEO), will continue in his role as MD in a transitional period before becoming Chairman of the Board. Apart from this, the company has recently appointed Chief Collection Officer, and Chief Vigilance Officer. The company has also appointed new COO-MFI, Sunil Mundra in place of Tarun Mehndiratta (Previous COO-MFI). Furthermore, the company plans to raise an additional ₹550 crore in capital to enhance its balance sheet, with support from its promoters for this proposal. Timely execution of the expected equity infusion will remain a key monitorable.

However, ratings continue to derive strength from the company's strong market position with diversified geographical presence, well diversified resource profile with the ability to raise funds at competitive rates and adequate liquidity position.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors: Factors that could lead to positive rating action/upgrade:

- Significant scale-up of operations while maintaining asset quality.
- Improving profitability with return on total assets (RoTA) above 3% on a sustained basis.
- Continuous support from investors in form of capital infusion.

Negative factors: Factors that could lead to negative rating action/downgrade:

- Weakness in capitalisation profile with gearing rising above 4x
- Lack of capital infusion as envisaged in timely manner.

Analytical approach:

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

Standalone

Outlook: Negative

The negative outlook reflects CARE Ratings' concerns about rising delinquencies and deteriorating asset quality, which adversely impacted the company's profitability metrics. CARE Ratings will continue to monitor the impact of this stress on overall microfinance industry and individual company's performance. Additionally, the outlook may be revised back to stable if the company secures anticipated equity infusion and shows some improvement in profitability.

Detailed description of key rating drivers:

Key strengths

Established track record of operations of over a decade with experienced management team

Having started operations as micro finance institution in 2010, FFL completed over a decade in the microfinance industry. With average tenure of microfinance loans of two years, product profile is well seasoned. However, CARE Ratings notes the company has recently ventured in Micro, Small & Medium Enterprises (MSME) segment, whose share increased from 0.03% in FY20 to 4.68% as on June 30, 2024, and is expected to further rise in the medium term. The company's ability to successfully grow its MSME book while maintaining asset quality remain a key rating monitorable.

FFL's asset under management (AUM) stood at ₹11,476 crore as on March 31, 2024 with 23% Y-o-Y growth, and 35% three years compounded annual growth rate (CAGR). AUM further scaled up to ₹12,193 crore as on June 30, 2024. However, AUM growth is expected to remain muted for fiscal 2025 due to ongoing stress in MFI industry, as the company has slowed down their disbursements. Going forward, the portfolio's performance remains a key monitorable.

Comfortable capitalisation profile, supported by equity infusion and strong investor base

The company's capitalisation profile remains comfortable, with capital adequacy ratio (CAR) at 27.53% on March 31, 2024, and 25.86% on June 30, 2024. It has a tangible net worth of ₹2,754 crore as of March 31, 2024, up from ₹2,244 crore on March 31, 2023, supported by strong internal accruals. However, this figure slightly decreased to ₹2,649 crore as on June 30, 2024, due to losses reported in Q1 FY25. Net worth may further take a hit with expected losses in Q2FY25.

However, CARE Ratings notes that the company plans to raise ₹550 crore in equity to further bolster its balance sheet, with support from promoter for this initiative. Timely infusion of the planned equity infusion will be a key rating monitorable. CARE Ratings notes that without the anticipated capital infusion, continued losses could negatively affect the company's capitalisation profile.

Diversified resource base

FFL has diversified resource profile with availability of funds at competitive rates. Its resource profile has good mix of public sector banks, foreign banks, private sector banks, financial institutions (FIs), subordinate debt and non-convertible debentures (NCDs). Term loans from banks and FIs, constitute ~95.5% of its borrowings as on June 30, 2024, remaining being NCD (2.1%), subordinate debt (0.6%), external commercial borrowings (1.8%). Additionally, the company demonstrated strong capability in raising funds at competitive rates, with an average cost of funds of 10% in Q1FY25.

Key weaknesses

Deteriorating asset quality

The company's asset quality worsened with GNPA ratio increasing from 2.89% on March 31, 2024, to 5.46% on June 30, 2024. This change follows the identification of 55,000 customers previously classified as stage-1 for Fusion, who are now considered NPAs by other lenders. As a result, Fusion has reclassified these accounts to stage-3 and made additional provisions accordingly. Furthermore, in its announcement on September 21, 2024, the company indicated it anticipates an additional provision of ₹500-550 crore in Q2 FY25 (subject to limited review of the financials by the Statutory Auditors).

Additionally, the company's collection efficiency declined from 97.3% in Q4 FY24 to 96.3% in Q1 FY25 and is expected to decrease further in Q2 FY25. Moving forward, the performance of their portfolio will be a critical area to monitor, especially as it serves a customer base with a weaker credit profile that is more vulnerable to economic and socio-political risks.

Decline in profitability

The company's operating profitability has shown significant decline in Q1FY25 as the company reported negative profit after tax (PAT) of ₹36 crore as compared to positive PAT of ₹505 crore in FY24. This loss is primarily due to high provisioning, with an additional provision of ₹208 crore (total provision is ₹348 crore as on Jun-24) created in Q1FY25. Furthermore, the company expects to create an additional provision of ₹500-550 crore in Q2FY25, which will further increase its losses for H1FY25.

CARE Ratings calculated net interest margins (NIMs) stood at 12.41% in fiscal 2024 and 13.39% in Q1FY25 as compared to 11.61% in fiscal 2023. Improved NIMs are backed by increase in yields by 250 bps in fiscal 2023, as the company implemented risk-based pricing model. However, credit cost increased significantly to 11.73% (annualised) in Q1FY25, resulting in negative RoTA of 1.2%.

CARE Ratings note that the the company's profitability is expected to remain negative for fiscal 2025 considering ongoing stress in MFI industry.

Inherent industry risks

Microfinance sector continues to be impacted by the inherent risk involved, such as socio-political intervention risk and regulatory uncertainty and risks emanating from unsecured lending and marginal profile of borrowers who are vulnerable to economic downturns besides operational risks related to cash-based transaction.

Liquidity: Adequate

The company has an adequate liquidity position given most borrowings are for longer tenure repayable over 2-8 years as against shorter tenure of its advances, including microfinance loans of 17-25 months. As per asset liability mismatch statement as on June 30, 2024, FFL has no negative cumulative mismatches in time bucket.

Environment, social, and governance (ESG) risks

FFL has implemented Corporate Social Responsibility (CSR) programs that are designed to create a positive impact on communities where company operates. For this, the company distributed bicycle to 7,000 people in rural areas, which promoted eco-friendly modes of transportation thus, contributing to reduction in carbon emission and also distributed inverter bulbs to rural households.

Applicable criteria

Definition of Default
Rating Outlook and Rating Watch
Financial Ratios - Financial Sector
Non Banking Financial Companies

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Financial services	Financial services	Finance	Microfinance institutions

FFL was originally incorporated as Ambience Fincap Private Limited (AFPL) on September 05, 1994. The company is registered with Reserve Bank of India (RBI) as a non-deposit accepting, systemically important non-banking financial company in 2010. In July 2021, the company registered itself again as FFL as it converted itself to public company from private company. FFL provides loans to female individual members in a group (joint liability group [JLG]), with each group consisting of five to seven members. Loans provided to individuals are based on mutual guarantee from members. It lends to JLG borrowers at 19.15%-23.40% interest rate (on a reducing balance) for 17 to 25 months with a repayment frequency of 14/28 days. As on June 30, 2024, the company operates in 22 states with AUM of ₹ 12,193 crore. The company has also started providing MSME loans. Currently, MSME book stands at ₹570 crore (4.7% of total AUM) as on June 30, 2024.

Brief Financials (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)	Q1FY25 (UA)
Total operating income	1,799.97	2,412.42	706.68
PAT	387.15	505.29	-35.62
Interest coverage (times)	1.80	1.84	0.77
Total Assets	9,286.43	11,680.43	12,084.20
Net NPA (%)	0.87	0.60	1.25
ROTA (%)	4.70	4.82	-1.20

A: Audited UA: Unaudited; Note: these are latest available financial results

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of 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 and Rating Outlook
Fund-based - LT-Term Loan		-	-	27-09-2025	1500.00	CARE A; Negative

Annexure-2: Rating history for 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 2024-2025	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
1	Fund-based - LT-Term Loan	LT	1500.00	CARE A; Negative	1)CARE A+; Stable (17-Apr-24)	1)CARE A+; Stable (27-Dec-23)	1)CARE A; Stable (28-Dec-22)	1)CARE A-; Stable (21-Jan-22) 2)CARE A-; Stable (03-Sep-21)
2	Fund-based - LT-Cash Credit	LT	-	-	-	-	-	1)Withdrawn (03-Sep-21)
3	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (21-Jan-22)
4	Debt-Subordinate Debt	LT	-	-	-	1)Withdrawn (27-Dec-23)	1)CARE A; Stable (28-Dec-22)	1)CARE A-; Stable (21-Jan-22)

LT: Long term; ST: Short term; LT/ST: Long term/Short term

Annexure-3: Detailed explanation of covenants of rated instruments/facilities: Not applicable

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Term Loan	Simple

Annexure-5: Lender details

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

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