Spandana Sphoorty Financial Limited

December 27, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	1,500.00	CARE A+; Negative	Reaffirmed; Outlook revised from Stable
Non Convertible Debentures	500.00	CARE A+; Negative	Reaffirmed; Outlook revised from Stable
Non Convertible Debentures	200.00	CARE A+; Negative	Reaffirmed; Outlook revised from Stable
Commercial Paper	100.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The reaffirmation of the rating of the commercial paper (CP), non-convertible debentures (NCD) and bank term loans of Spandana Sphoorty Financial Limited (SSFL) is based on the company's healthy liquidity profile, comfortable capitalisation position with low gearing levels as compared to peers, diversified resource profile with increasing share of bank borrowings, though slightly moderated in H1FY25 and geographically diversified AUM as on September 30, 2024.

However, CARE Ratings Limited (CARE Ratings) has revised its outlook on the long-term bank facilities and NCD of SSFL to 'Negative' from 'Stable' owing to weakening of profitability and asset quality metrics in H1FY25 and expectation of further rise in delinquencies and consequent uptick in the credit costs and overall weak profitability of the company in near term. Rating constraints also factors in inherent risks involved in the microfinance industry, including unsecured lending, marginal profile of borrowers, socio-political intervention risk, and regulatory uncertainty. The assets under management (AUM) of SSFL (on a consolidated basis) have shrinked from Rs. 11,973 crore in FY24 to Rs. 10,537 crore in H1FY25 owing to muted disbursements in H1FY25.

CARE Ratings notes that the microfinance industry is currently experiencing significant stress, primarily due to increasing borrower indebtedness, as larger ticket sizes and multiple loans taken by low-income individuals have led to over-leverage and difficulties in repayment. Compounding this issue is the dilution of the joint liability group (JLG) model, with declining centre attendance, high attrition rates among field staff and natural calamities that has significantly affected the collection efficiency of the microfinance institutions (MFIs). SSFL is currently dealing with significant attrition and operational difficulties amidst its plan to shift to a weekly collection model. However, the company has decelerated this transition in light of the challenges faced within the sector. Further, the company has stopped acquiring new-to-credit customers and also stopped new customer acquisition in 46% of the branches amidst stress in MFI sector.

Owing to rise in delinquencies in H1FY25, there has been an sharp uptick in the annualized credit costs (as a percentage of average total assets) of the company from 2.32% in FY24 to 11.76% in H1FY25 and deterioration in its Gross Stage III assets to 5.31% and Net Stage III assets to 1.13% (consolidated GNPA% of 4.86%) as on September 30, 2024 (compared to Gross Stage III assets of 1.68% and Net Stage III assets of 0.34% as on March 31, 2024). This has negatively impacted the profitability of SSFL with decline in annualized Return on Total Assets (RoTA) from 4.47% in FY24 to -2.62% in H1FY25.

CARE Ratings also note that as on September'24, the company has breached certain financial covenants in respect of borrowings amounting to ₹ 867.74 crore (this comprises of ₹ 732.88 crore of non-convertible debentures (NCDs) and ₹ 134.86 crore of term loans outstanding), resulting in these borrowings becoming repayable on demand subject to fulfilment of the terms of debenture trust deed. Till date, debenture holders of NCDs worth ₹ 198.32 crore have exercised early redemption, while it has received waivers from 2 lenders for all the term loans. These covenant breaches were reported by the company as a part of declaration of financial results for the quarter ended September 30, 2024. Going Forward, CARE Ratings expects continued lender support and does not anticipate requests for sizeable recall or accelerated repayments. Any deviation from the lender's current stance will be a critical factor for ongoing monitoring.

Going forward, CARE Ratings anticipates a moderation in loan book growth considering the ongoing MFI stress. Additionally, with rising credit costs expected to exert further pressure on profitability, Company's ability to maintain its financial flexibility in the current environment will remain key rating monitorable.

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

Rating sensitivities

Positive factors

- Improving profitability profile with return on total assets (RoTA) of more than 3% on a sustained basis
- Significant scale-up of operations while maintaining credit costs below 4%
- Substantially diversifying lender mix with the company able to raise funds at competitive rates

Negative factors

- Significant reduction in borrowings owing to sizeable recalls/ repayments, adversely impacting liquidity profile
- Weakness in capitalisation profile with asset under management (AUM) to net worth rising 5x.
- Rise in gearing level above 4x

Analytical approach: Consolidated. CARE Ratings Limited (CARE Ratings) has adopted a Consolidated approach for SSFL. Please refer Annexure 6.

The list of subsidiary companies is as follows:
- Caspian Financial Services Limited
- Criss Financial Limited

Outlook: Negative

The outlook has been changed from stable to negative due to ongoing stress in the overall MFI industry, which is expected to lead to higher credit costs, and consequently moderation in profitability metrics in near term. Further, 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 shows some improvement in profitability and asset quality metrics.

Detailed description of the key rating drivers

Key strengths

Healthy capitalisation supported by equity infusion and strong investor base

SSFL is backed by marquee PE player i.e. Kedaara Capital which holds 48.13% stake in it (directly and indirectly through its special purpose vehicle (SPV) i.e. Kangchenjunga Limited) as on September 30, 2024. Further, SSFL has received an approval from the Stock Exchanges for reclassification of erstwhile promoters Padmaja Gangireddy and Vijaya Sivarami Reddy Vendidandi (holding 7.71% holding as on June 2024) to public shareholders.

The capitalization of SSFL remains comfortably well above regulatory benchmark, with improvement in Capital Adequacy Ratio (CAR)% in H1FY25 at 35.70% from 31.95% in FY24. In H1FY25, the gearing level of the company fell from 2.70x as on March 31, 2024 to 2.42x in H1FY25 owing to fall in borrowings despite the reduction in internal accruals on account of net losses in H1FY25. Further, the managed gearing (i.e. AUM/ Tangible Networth) fell from 3.43x in FY24 to 3.26x in H1FY25 owing to the decline in the AUM in H1FY25. Going forward, CARE Ratings expects the Company to maintain a gearing level below 4x level.

Diversified resource profile with increasing reliance on bank borrowings

SSFL (on a consolidated basis) has a diversified lender mix with lending relationships with 56 lenders including 29 NBFCs/ financial institutions, 22 private sector banks/ small finance banks, 4 public sector banks and 1 foreign private investor. Though the share of funding from banks (as a part of consolidated borrowings) has been increasing over years, the same moderated to 51.5% as on September 2024 as against 55.7% as on March 31, 2024. The share of NBFCs has increased from 8.7% in FY22 to 21.0% in H1FY25 while the share of NCDs (capital market exposure) has reduced from 39.0% as on March 31, 2023 to 25.4% as on September 2024, though increased from March 2024 i.e. 21.6%.

The company, on a consolidated level, raised an additional ₹ 3,138.01 crore in the form of term loans, NCD and PTCs in H1FY25 while, on a standalone level, the company raised funds amounting to ₹ 2,867 crore in H1FY25. The average cost of funds is 11.98% for H1FY25, comparatively higher than peers, however incremental cost of borrowing is around 10.38% for funds raised in H1FY25.
Going forward, SSFL's ability to raise funding at competitive rates while maintaining a stable funding profile would be monitorable.

Key weaknesses

Rising credit cost impacting profitability

The company's profitability (on a consolidated level) has been negatively impacted by rising credit costs amid ongoing challenges in the MFI industry. In H1FY25, the company incurred losses of ₹160.62 crore as compared to profit after tax (PAT) of ₹500.72 crores in FY24.

The company has made provisions worth ₹ 720.71 crore in H1FY25 vis-à-vis ₹ 259.41 crore in FY24 owing to higher delinquencies and worsening asset quality. With increased slippages and write offs in H1FY25 amidst stress in MFI sector, credit costs to average assets sharply increased to 11.76% (annualized) in H1FY25 (versus 2.32% in FY24).

The operating expenses (Opex) ratio slightly increased from 5.84% in FY24 to 6.71% (annualized) in H1FY25, driven by additional manpower expenses, high field attrition rate and expansion of LAP and Nano product lines under the company's subsidiary Criss Financial Ltd in H1FY25. The company opened 81 new branches in H1FY25, taking the total count to 1,723 branches, as on September 30, 2024. Operating expenses are expected to continue remaining high in the near term, with the company taking additional measures to control asset quality like hiring Branch Quality Managers and strengthening its collections/recovery teams. The company's profitability is partially supported by significant DA income, which stands at around 1.44% (as a % of average total assets) in H1FY25. Overall, driven by high credit and operating expenses, the profitability was negatively impacted leading to a decline in Return on Total Assets (RoTA) to -2.62% in H1FY25, down from 4.47% in FY24.

Going forward, the credit costs may further increase in H2FY25 and CARE Ratings expects a further moderation in profitability.

Moderation in asset quality

The microfinance industry is currently facing a significant rise in delinquencies, primarily driven by increasing borrower indebtedness and compounded by various factors, such as heatwaves, general elections, and political movements like the "Karja Mukti Abhiyan." This challenge is further aggravated by the weakening of the Joint Liability Group model, characterized by a notable decrease in centre attendance, diminished peer pressure and collective accountability, which have historically helped maintain low default rates. Due to these factors, the collections of SSFL were impacted in H1FY25 and continue to be impacted in Q3FY25.

The gross non-performing assets (GNPAs) and Net non-performing assets (NNPA) of SSFL (on a consolidated level) has sharply increased from 1.68% and 0.34% respectively as on March 31, 2024 to 5.31% and 1.13% respectively as on September 30, 2024 owing to additional slippages in H1FY25. Further, 1+ dpd (on standalone basis) increased from 4.20% as on March 31, 2024 to 16.28% as on September 30, 2024. The slippage ratio (Addition in NPA/ Opening gross loan book) stood at 5.82% as on September 30, 2024 vis-à-vis 1.91% as on March 31, 2024.

Net stressed assets to net advances [(Net NPA+ Standard Restructured Assets (net off provisions) + Amount of securities received by ARC)/ (Total Gross Advances – Closing Provision on NPA– Provision on standard restructured assets - Provision for Impairment loss allowance)] hiked from 1.35% in FY24 to 2.30% as on September 30, 2024. The provision coverage on NPAs have increased from 69.06% in FY23 to 79.67% in Q1FY25, due to stress in MFI sector.

As on September 30, 2024, around 26.9% of the total borrowers (as a proportion to current AUM) have been classified as loans outstanding with more than 4 lenders including Spandana and loans outstanding with more than 5 lenders including Spandana. Owing to the new stricter guardrails by Micro Finance Institutions Network (MFIN) limiting the number of lenders per borrower with a maximum of three microfinance lenders including SSFL (effective from April 01, 2025), headwinds for the asset quality are expected to continue in the near term from such overleveraged borrowers due to restricted availability of incremental microfinance loans.

CARE Ratings expects SSFL's asset quality to encounter further challenges in near term due to the strain in the microfinance sector and the stricter lending regulations as directed by the MFI-SRO. As a result, disbursements are likely to remain subdued, with an emphasis on managing asset quality. Company's ability to maintain its asset quality amidst the ongoing stress remain key rating monitorable.

Inherent industry risks

The microfinance sector continues to be impacted by the inherent risk involved. These include 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 transactions.

Liquidity: Adequate

The company (on a standalone basis) has an adequate liquidity position given short tenure of its advances, viz., microfinance loans of 12-30 months, with cash and cash equivalents of Rs. 1385.55 crore as on March 2024.

According to asset liability management statement as on September 30, 2024, SSFL has no negative cumulative mismatches in any time bucket. As on September 30, 2024, it has liquidity of ₹1,331.47 crore in the form of free cash in hand. Also, as per the

ALM statement, the company has advances of up to six months of ₹ 3,606 crore as against debt of up to six months of ₹ 2,815 crore.

Environment, social, and governance (ESG) risks

SSFL has implemented corporate social responsibility (CSR) programmes that are designed to create a positive impact on the communities where company operates. For this, SSFL has established 65 tailoring training centres specifically for rural women and girls across 10 states. These centres offer a comprehensive 90-day skill development programme in tailoring along with Financial and Digital literacy module. Also, the company carries CSR activities on continuous basis, such as installing four community water centres, promoting clean and affordable energy, conducting digital and financial literacy (DFL) programmes, and comprehensive support to underprivileged citizens by ensuring access to various government welfare schemes.

Applicable criteria

Consolidation
Definition of Default
Rating Outlook and Rating Watch
Financial Ratios - Financial Sector
Short Term Instruments
Non Banking Financial Companies

About the company

Industry classification

Macroeconomic Indicator	Sector	Industry	Basic Industry
Financial services	Financial services	Finance	Financial Institution

SSFL was incorporated on March 10, 2003 under the provisions of the Companies Act, 1956 and was registered as on non-deposit accepting NBFC with the RBI and was classified as an NBFC-MFI effective April 13, 2015. The company is engaged in undertaking microfinance loans business in India in a joint liability group (JLG) and loan against property (LAP) lending model. The company provides micro loans with a tenure of 1-2 years to women borrowers from low-income households for income generation activities like agriculture, handlooms & handicrafts, cattle raring, cottage industries & micro entrepreneurial ventures like tailoring, grocery stores amongst others, education and healthcare. The company has two subsidiaries, Caspian Financial Services Limited (CFSL) and Criss Financial Limited (CFL). As on September 30, 2024, the company operates in 19 states and 1 union territory with consolidated AUM of ₹10,537 crores.

Brief Financials (₹ crore) (Consolidated)	March 31, 2022 (A)	March 31, 2023 (A)	March 31, 2024 (A)	H1FY25 (UA)
Total operating income	1,438.46	1,438.29	2,510.78	1,436.05
PAT	69.83	12.39	500.72	(160.62)
Interest coverage (times)	1.20	1.06	1.75	0.61
Total assets*	6,867.65	9,163.62	13,227.42	11,279.56
Net NPA^ (%)	11.38	0.70	0.34	1.13
ROTA (%)	0.91	0.15	4.47	(2.62)

A: Audited; UA: unaudited
*excludes deferred tax assets and intangible assets
^CARE Ratings calculated

Brief Financials (₹ crore) (Standalone)	March 31, 2022 (A)	March 31, 2023 (A)	March 31, 2024 (A)	H1FY25 (UA)
Total operating income	1,391.60	1,394.45	2,406.91	1,348.79
PAT	46.64	12.34	467.88	-152.65
Interest coverage (times)	1.14	1.06	1.72	0.60
Total assets*	6,675.37	8,992.03	12,743.05	10,697.77
Net NPA^ (%)	10.95	0.62	0.32	1.10
ROTA (%)	0.63	0.16	4.31	-2.60

A: Audited; UA: unaudited, NA: Not Available
*excludes deferred tax assets and intangible assets

^CARE Ratings calculated

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: 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 and Rating Outlook
Commercial Paper	Proposed	-	-	-	100.00	CARE A1+
Debentures-Non Convertible Debentures	INE572J07729	10-Jul-2024	10.75%	10-Jul-2026	55.00	CARE A+; Negative
Debentures-Non Convertible Debentures	INE572J07711	28-Jun-2024	9.84%	28-Jun-2026	75.00	CARE A+; Negative
Debentures-Non Convertible Debentures	Proposed	-	-	-	20.00	CARE A+; Negative
Debentures-Non Convertible Debentures	INE572J07711	02-Aug-2024	9.84%	28-Jun-2026	150.00	CARE A+; Negative
Debentures-Non Convertible Debentures	INE572J07737	14-Aug-2024	10.50%	14-Apr-2027	50.00	CARE A+; Negative
Debentures-Non Convertible Debentures	INE572J07752	05-Sep-2024	10.75%	15-Apr-2027	50.00	CARE A+; Negative
Debentures-Non Convertible Debentures	INE572J07711	12-Sep-2024	9.84%	28-Jun-2026	100.00	CARE A+; Negative
Debentures-Non Convertible Debentures	Proposed	-	-	-	200.00	CARE A+; Negative
Fund-based - LT-Term Loan		-	-	NA	1500.00	CARE A+; Negative

NA: Not Applicable

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	Commercial Paper-Commercial Paper	ST	100.00	CARE A1+	1)CARE A1+ (30-Sep-24)	1)CARE A1+ (21-Mar-24)	-	-
2	Debentures-Non Convertible Debentures	LT	500.00	CARE A+; Negative	1)CARE A+; Stable (30-Sep-24)	1)CARE A+; Stable (21-Mar-24)	-	-
3	Fund-based - LT-Term Loan	LT	1500.00	CARE A+; Negative	1)CARE A+; Stable (30-Sep-24)	1)CARE A+; Stable (21-Mar-24)	-	-
4	Debentures-Non Convertible Debentures	LT	200.00	CARE A+; Negative	1)CARE A+; Stable (30-Sep-24)	-	-	-

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

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

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Commercial Paper-Commercial Paper	Simple
2	Debentures-Non Convertible Debentures	Simple
3	Fund-based - LT-Term Loan	Simple

Annexure-5: Lender details

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

Annexure-6: List of entities consolidated

Sr No	Name of the entity	Extent of consolidation	Rationale for consolidation
1	Criss Financial Limited	Full	Subsidiary
2	Caspian Financial Services Limited	Full	Wholly owned Subsidiary

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.

Contact us

Media Contact	Analytical Contacts
Mradul Mishra Director **CARE Ratings Limited** Phone: +91-22-6754 3596 E-mail: mradul.mishra@careedge.in	Sanjay Kumar Agarwal Senior Director **CARE Ratings Limited** Phone: 912267543582 E-mail: sanjay.agarwal@careedge.in
Relationship Contact Pradeep Kumar V Senior Director **CARE Ratings Limited** Phone: 914428501001 E-mail: pradeep.kumar@careedge.in	Neha Kadiyan Director **CARE Ratings Limited** Phone: 91-120-4452022 E-mail: Neha.Kadiyan@careedge.in Kanika Aggarwal Lead Analyst **CARE Ratings Limited** E-mail: Kanika.aggarwal@careedge.in

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.

For detailed Rationale Report and subscription information, please visit www.careedge.in