Aavas Financiers Limited
January 06, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	2662.00 (Rs. Two Thousand and six 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

**of which Rs.345 crore is utilized and remaining Rs.450 crore is unutilized*
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 company's robust financial metrics with healthy disbursements, strong growth in assets under management (AUM) and high portfolio granularity with average ticket size of Rs 8.4 lacs. Also, the company has comfortable capitalization profile supported by positive internal accruals and few rounds of equity infusion particularly via equity raising of Rs.115 crore from management and employees and through IPO of Rs 360 crore in FY19. As a result, the company's gearing has improved to below 2.5 times. The resource profile of AFL remains well diversified with company raising funds from various sources such as banks, financial institutions, NHB (National Housing Bank) and development financial institutions and via market borrowings at competitive rates. The rating also derives strength from healthy profitability metrics with RoTA (Return on total assets) at 4.03% in H1FY20, 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 March 31, 2019 and September 30, 2019.

These rating strengths, are however, partially offset by the limited track record of operations and improving albeit still relatively low seasoning of loan portfolio. Also, AFL continues to be geographically concentrated with Rajasthan accounting for 43.6% of Assets under Management (AUM) as on September 30, 2019 and 78% of portfolio in top three states. Additionally, the exposure to the relatively vulnerable borrower customers who are new to credit and have modest credit profile (self-employed borrowers comprising 65% of AUM as on September 30, 2019) makes AFL susceptible to inherent asset quality risks. 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 maintain high collections efficiency (~99%) and keep its asset quality under control with GNPA and NNPA at 0.62% and 0.49% respectively as on September 30, 2019. 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-
- Scale up of operations in a sustainable and profitable manner
- Comfortable asset quality with GNPA on a sustainable basis below 1%
- Comfortable capitalization profile with gearing below 5 times on a sustainable basis

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

Negative Factors-

- 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: The company was promoted by AU Small Finance Bank (AUSFB) (rated currently at **CARE AA-; Stable**); however in June 2016, when in order to comply with RBI guidelines for conversion into (SFB) Small Finance Bank, AUSFB divested majority stake in AFL to two private equity (PE) investors – Kedaara Capital and Partners Group, who cumulatively held 58.25% equity as on September 30, 2019. The company's board 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 capital adequacy ratio (CAR) of the company remains strong with Tier 1 and overall CAR of 60.4% and 63.6% respectively as on Sep 30, 2019 (64.25% and 67.77% respectively as on March 31, 2019) led by healthy internal accruals and regular equity infusion by the promoters and investors in recent years. Also, the capitalization is supported by lower risk weights assigned on smaller ticket home loans. The company raised fresh equity of Rs.441 crore during FY18 and Rs.475 crore in FY19 (including Rs 360 crore of equity raised through IPO). As a result, the tangible net worth of the company increased to Rs.1,833 cr as on March 31, 2019 and further to Rs.1,958 crore as on September 30, 2019. The overall gearing of the company stood at 2.15 times as on September 30, 2019 and 1.9 times as on March 31, 2019 vs. 2.3 times as on March 31, 2018. However, adjusted for securitization book at Rs.1,463 crore; gearing stood at 2.9 times as on September 30, 2019. On a steady-state basis, the company expects to maintain gearing below 6 times.

Diversified Resource Profile: The borrowing profile of AFL remains well diversified with funding from banks/FIs (through term loans / working capital (41.5% of total borrowings as on September 30, 2019) as well as direct assignment lines (27.7%), National Housing Bank (15.2%) and through NCDs and Rupee Dominated Masala Bonds (15.2%). Company has been able to raise funds at competitive rates from a diverse set of lenders including insurance companies and development financial institutions (DFIs). The weighted average borrowing cost of the company stood at 8.74% (including securitization/Assignment) as on March 31, 2019 as against 8.63% as on March 31, 2018. During the quarter ended September 30, 2019, AFL borrowed Rs.953 crores with average maturity of around 10 years at 8.67%, of which Rs.345 crores was raised in the form of non-convertible debentures (NCDs) from IFC, Rs.258 crores from assignment and Rs.350 crores as term loans from the bank. The company did not have any exposure to commercial paper borrowings as on September 30, 2019.

Adequate risk management and control systems*:* 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.

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 72% from fiscal 2014 till fiscal 2019 primarily driven by denominator effect amid lower base. End fiscal 2019, the AUM of the company stood at Rs.5,942 crore, up 46% Y-o-Y and further to Rs.6,753 crore as on September 30, 2019. During FY19, the housing loan portfolio (forming 79% of the total portfolio mix) grew by 41% Y-o-Y to Rs.4,674 crore; while the non-housing loan portfolio forming the remaining 21% of portfolio, grew by 66.8% Y-o-Y to Rs.1,267 crore. The non-housing loan comprises top-up loans against residential property (5.8% as on March 31, 2019) as well as LAP with average ticket size of 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 of the company remains healthy with AFL reporting net interest margin (NIM) and return on tangible assets (ROTA) of 7.0% and 3.6% respectively in FY19, up from 6.2% and 2.8% respectively in FY18. The operating expense of the company (as a % of average total assets) reduced to 3.91% end fiscal 2019 as against 4.98% in FY18 as the company is achieving economies of scale. Also, credit cost for the company, though rising, has remained controlled at 0.18% as on March 31, 2019 on the back of good asset quality. For the half year ending September 30, 2019, the company reported profit after tax (PAT) of Rs.121.3 crore on net interest income of Rs.205.9 crore as against PAT of Rs.65.3 crore as against net interest income of Rs.149.8 crore for the corresponding period last year. The company reported NIM and RoTA at 6.8% and 4.0%

respectively as on September 30, 2019.

Key Rating Weaknesses

Low seasoning of loan portfolio with exposure to relatively vulnerable borrower segment; however asset quality under control: 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, 2019) 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. However, AFL maintains low loan to value (average LTV 51% as on Sep-19) ratio on its loan book with about 65% of loan book at LTVs of less 60% and only 4.5% of loan book greater than 80% LTV as on Sep 30, 2019 thereby mitigating asset quality risk to some extent. About two thirds of the book had FOIR below 50%. The average ticket size of both housing and non-housing products remain sub-Rs 10 lacs thereby imparting granularity. Also, AFL is able to maintain its asset quality despite demonetization, RERA and GST implementation with GNPA and NNPA of 0.47% and 0.37% respectively (per Ind-AS) as on March 31, 2019. Company's softer delinquencies (30+ DPD) are under control at 2.2% as on Sep 30, 2019. As on September 30, 2019, the Gross NPA% and Net NPA% stood at 0.62% and 0.49% respectively while the provision coverage ratio (PCR) hovered around mid-20%. The asset quality performance through different economic cycles and geographies is yet to be established.

Geographical concentration: While the company has presence in nine states, the state-wise geographic concentration remains high with Rajasthan alone accounting for 44% of the AUM as on September 30, 2019 (down from 49.5% as on March 31, 2016) and top three states (Rajasthan, Maharashtra and Gujarat) together accounting for 78% of portfolio. 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, 2019, company has presence in 9 states with 216 branches covering around 125 districts and 900 tehsils.

Liquidity: Adequate

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 September 30, 2019. As per ALM statement dated September 30, 2019, over the next six months, the company expects repayment from loan book of Rs.747.21 crore while its debt repayment will be around Rs.508.27 crore. Moreover, the company had liquidity in the form of cash and cash equivalents of Rs 1,050 crore and sanctioned but unutilized lines of Rs 902 crore as on September 30, 2019. Also, as per management, the company maintains liquidity to meet net disbursement requirements coming in next three months.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Short Term Instruments
Financial Ratios – Financial Sector
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, 2019, Kedaara Group holds 34.3 % stake in AFL, Partners Group holds 24.0% stake, AU SFB held 6.40% and remaining 35.3% is held by public including management team of AFL. The tangible net-worth of the company improved to Rs.1,833 crore as on March 31, 2019 and further to Rs.1,958 crore as on September 30, 2019. Recently, equity shares of AFL got listed on BSE and NSE.

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, 2019, the company operates through a network of 216 branches in 9 states of Rajasthan, Gujarat, Madhya Pradesh, Maharashtra, Delhi, Uttar Pradesh, Haryana, Chattisgarh and Uttrakhand.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)

Total operating income	494.4	710.9
PAT	93.1	175.9
Interest coverage (times)	1.7	2.0
Total Assets*	4,037.1	5,623.1
Net NPA (%)	0.39	0.37
ROTA (%)	2.8	3.6

*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

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	-	-	-	June 2027	2662.00	CARE AA-; Stable
Commercial Paper	Proposed				100.00	CARE A1+
Subordinate Debt	INE216P08017	Dec-22-2017	9.74%	Dec-22-2023	100.00	CARE AA-; Stable
Non-Convertible Debentures	INE216P07167	Sep-16-2019	8.39%	Sep-15-2024	345.00	CARE AA-; Stable
Non-Convertible Debentures	Proposed				450.00	CARE AA-; Stable

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Commercial Paper	ST	100.00	CARE A1+	-	1)CARE A1+ (25-Mar-19)	1)CARE A1+ (29-Aug-17)	1)CARE A1+ (14-Mar-17)
2.	Fund-based - LT-Term Loan	LT	2662.00	CARE AA-; Stable	1)CARE AA-; Stable (30-Jul-19) 2)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)	1)CARE A+; Stable (14-Mar-17)
3.	Debt-Subordinate Debt	LT	50.00	CARE AA-; Stable	-	1)CARE AA-; Stable (25-Mar-19)	1)CARE A+; Stable (29-Aug-17)	-
4.	Debt-Subordinate Debt	LT	50.00	CARE AA-; Stable	-	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 (31-May-19)	-	-	-
6.	Debentures-Non Convertible Debentures	LT	420.00	CARE AA-; Stable	1)CARE AA-; Stable (13-Dec-19)	-	-	-

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

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