Aavas Financiers Limited

December 13, 2019

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Proposed Non-Convertible Debentures	420.00 (Rs. Four hundred and twenty crore only)	CARE AA-; Stable [Double A Minus; Outlook: Stable	Assigned

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating assigned to the non-convertible debentures of Aavas Financiers Limited(AFL) factors in company's experienced management team, comfortable capitalization profile supported by bolstered net worth base on account of capital raising in recent years leading to gearing below 2.5 times, adequate liquidity and diversified resource profile with company raising funds from various sources such as banks, financial institutions, NHB (National Housing Bank) and development finance institutions and via market borrowings. The rating also derives strength from healthy profitability metrics with RoTA (Return on total assets) at 3.64% in FY19, adequate risk management & control systems put in place by the company as well as good growth opportunities in the affordable housing segment.

These rating strengths, are however, partially offset by the limited track record of operations and improving albeit still relatively low seasoning of loan portfolio along with geographical concentration of its loan book with Rajasthan accounting for 43.6% of Assets under Management (AUM) as on September 30, 2019. Additionally, the exposure to the relatively vulnerable borrower segment (self-employed borrowers comprising 65% of AUM as on September 30, 2019) makes AFL susceptible to asset quality risks. However, owing to its strong credit appraisal mechanisms, AFL has been able to 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 woul d be key rating sensitivities.

Positive Factors-

- Scale up of operations in sustainable and profitable manner
- Comfortable asset quality with GNPA on a sustainable basis below 1%
- Comfortable capitalization profile with gearing below 4 times on a sustainable basis

Negative Factors-

- Weakness in profitability and/or capitalization profile of AFL with gearing rising above 5-6 times
- Decline in asset quality (GNPA above 2.2%).

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**) till June 2016, however 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 hold 58.25% equity as on September 30, 2019. The company has an experienced Board comprising of nine experienced professionals including 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 led by regular equity infusion by the promoters and investors in recent years. Overall CAR and Tier 1 CAR stood at 67.77% and 64.25% respectively as on March 31, 2019 and 63.6% and 60.4% respectively as on Sep 30, 2019. 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). On account of regular equity infusions coupled with positive accruals, the tangible net worth of the company has increased to Rs.1,833 cr as on March 31, 2019 and further to Rs.1958 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.

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

Diversified Resource Profile: The borrowing profile of AFL is well diversified with funding from banking channel (through term loans / working capital as well as direct assignment lines), National Housing Bank, other financial institutions and through NCDs and Rupee Dominated Masala Bonds. Company has been able to raise funds at competitive rates from a diverse set of lenders including insurance companies and development finance institutions (DFIs). The company did not have any 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 an improving trend of asset quality.

Healthy financial risk profile: The AUM of the company grew by 46% from Rs.4,073 crore as on March 31, 2018 to Rs.5,942 crore as on March 31, 2019 and further to Rs.6,753 crore as on September 30, 2019. Company's loan book comprised housing loans (77% as on September 30, 2019) and non-housing loans (23%). The profitability of the company is healthy with AFL reporting NIM and ROTA of 7.0% and 3.6% respectively in FY19 vs. 6.2% and 2.8% respectively in FY18. 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.

Key Rating Weaknesses

Low seasoning of loan portfolio with exposure to relatively vulnerable borrower segment; however asset quality under control: AFL started its operations in March 2012. The seasoning of the loan portfolio is low; however improving with time and the company has also witnessed significant portfolio growth in the recent past. AFL is focused on providing secured retail home loans to low income borrowers in semi-urban and rural regions, who have irregular cash flows 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 workers thereby exposing the company to the riskier borrower segment. However, AFL maintains low LTV ratio on its loan book (with about 64.5% of loan book at LTVs of <60% and only 4.5% of loan book at >80% LTV as on Sep 30, 2019), mitigating this risk to some extent. Also, AFL is able to maintain its asset quality despite demonetization, RERA and GST implementation. As on September 30, 2019, the Gross NPA% and Net NPA% stood at 0.62% and 0.49% respectively. The asset quality performance through different economic cycles and geographies is yet to be established.

Geographical concentration: The company has presence in 9 states with Rajasthan alone accounting for 43.6% of the AUM as on September 30, 2019, concentration to Rajasthan has declined marginally over last few years (49.49% as on March 31, 2016) and is likely to decline further as 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 the borrowings, rendering the 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. As on September 30, 2019, the company had liquidity in the form of cash and cash equivalents of Rs.1,050 crore.

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	494.44	710.97
PAT	93.09	175.91
Interest coverage (times)	1.70	2.01
Total Assets*	4,037.10	5,623.15
Net NPA (%)	0.39	0.37
ROTA (%)	2.87	3.64

*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	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Proposed Debentures-Non Convertible Debentures	December 10, 2019	-	-	420.00	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)	-	-	-

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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