Dvara Kshetriya Gramin Financial Services Private Limited

May 26, 2020

Ratings

Facilities / Instruments	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Long-term Bank Facilities	236.57	**CARE BBB; Stable** (Triple B; Outlook: Stable)	Reaffirmed; Outlook revised from Positive to Stable
Long-term/Short-term Bank Facilities (Proposed)	65.43	**CARE BBB; Stable / CARE A3+** (Triple B; Outlook: Stable / CARE A Three Plus)	Reaffirmed; Outlook revised from Positive to Stable
Total Bank Facilities	**302.00 (Enhanced from 300) (Rs. Three hundred two crore only)**		
Non-convertible debenture issue-II	20	**CARE BBB; Stable** (Triple B; Outlook: Stable)	Reaffirmed; Outlook revised from Positive to Stable
Non-convertible debenture issue-III	50	**CARE BBB; Stable** (Triple B; Outlook: Stable)	Reaffirmed; Outlook revised from Positive to Stable
Total Instruments	**70 (Rs. Seventy crore only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities and debt instruments of Dvara Kshetriya Gramin Financial Services Pvt. Ltd. (Dvara KGFS) continue to factor in the experience of senior management team, commensurate loan appraisal, risk management & MIS System and adequate liquidity profile. The ratings also take note of the equity raise of Rs.127 crore in H1FY20 (refers to the period April 01 to September 30) from existing and new investors. The ratings are, however, constrained by geographical concentration of loan portfolio, product concentration, moderate profitability levels, moderate asset quality and inherent risks associated with its customer segment including sociopolitical intervention risk and regulatory risk.

Rating Sensitivities

Positive Factors - Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Improvement in scale of operations and profitability on a sustained basis
- Sustained improvement in geographical concentration and product concentration

Negative Factors - Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Deterioration in Asset Quality
- Weakening of capital adequacy levels
- Further moderation in profitability levels

Outlook: Stable

Earlier in the month of October 2019, CARE had revised the Outlook of Dvara KGFS from ‘Stable’ to ‘Positive’ based on the expectation that the recent equity raise is likely to aid Dvara KGFS to increase its scale of operations thereby achieving benefits of scale going forward. However, the lockdown due to outbreak of COVID-19 is likely to result in longer than expected time for improving its scale of operations and achieve scale benefits in terms of reducing opex/avg. assets, etc. Hence, CARE has revised the Outlook of Dvara KGFS from ‘Positive’ to ‘Stable’. Furthermore, Dvara KGFS is extending moratorium to its borrowers following Reserve Bank of India’s circular dated March 27, 2020, on the Covid-19 regulatory package. Going forward, impact of the moratorium on delinquency levels and bringing back the customers to regular repayments in the near term remains to be seen. The company has also applied to avail moratorium from its lenders and PTC/DA investors and most of them have approved for the same.

Credit Risk Assessment

Key Rating Strengths

Experienced management team and part of the Dvara group

Dvara KGFS is promoted by Dvara Trust (Formerly IFMR Trust) and the board consists of representatives from Holding Companies. The Board & Senior management Team of Dvara KGFS have significant experience in NBFC Sector & Rural Banking. Mr Joby CO, CEO of the company has 17 years of experience in Indian Microfinance Industry, Mr LVLN Murty,

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

Deputy CEO has 24 years of Diverse Experience and Vijayakumar G, CFO of Dvara KGFS has 29 years of experience in various financial institution sectors. The Dvara group provides support for the information technology through Dvara Solutions.

Well-established IT and presence of risk management systems

Dvara KGFS has well-established structure to monitor the operations at different levels. It has a defined credit appraisal, collection and monitoring system and has also induced credit discipline amongst the borrowers through regular training programs. Dvara KGFS predominantly operates under the JLG lending model. Dvara KGFS also access reports regularly from High Mark to check the eligibility of the individual. The company does a two level appraisal for JLG loans, the first levels appraisal is done internally and second appraisal to done by third party. For Loans Raised for Business Correspondent (BC), Second appraisal is done by BC. Dvara KGFS has also formed risk function to take care of enterprise wide risk and credit function to take care of credit function in micro enterprise loans. Furthermore, Dvara KGFS had appointed head of internal audit wherein detailed, surprise and short audits are carried out to implement strict internal control systems. The internal audit team carries out risk scoring of branches based on a defined set of parameters covering different functional areas to assess the performance of the branch. All the branches are equipped with biometric recognition systems, which act as authorization for the transactions. The KGFS model leverages on the robust IT systems through the use of Core Banking System (CBS) and Customer Management System (CMS), which operate in a real-time basis. Such systems enable the company to monitor the portfolio performance on a real-time basis. The company has also formed an in-house IT and data analytics team headed by Chief Technology Officer.

Business model of KGFS

Dvara KGFS currently has 8 KGFS (Hub). Each of the KGFS has a network of brick and mortar branches which act as the front end distribution entities in their locality. This helps the KGFS to achieve the primary goal of being a local financial institution offering financial products and services in a focused geography. The core of the KGFS model consists of the village level branch which serves as a customer touch point, where the origination happens. These branches are fully supported by the Head Office (HO) through a series of hubs. Each branch covers a radius of 5-25 km depending on the terrain. Separate credit team is in place and credit appraisal will be done by the credit team at KGFS hubs for non-JLG products.
KGFS also distribute third-party products like Insurance and foreign inward remittances. Besides this, Dvara KGFS also acts as a Business Correspondent for Axis bank, MAS Financial Services and ESAF Small Finance Bank. Recently, Dvara KGFS has become Aadhaar-enabled payments partner by RBL Bank to enable cash withdrawal and balance enquiry for the customers.

Comfortable capitalisation levels

Overall Gearing stands at 3.64x as on March 31, 2019. CAR improved from 18.40% as on March 31, 2018 to 24.10% as on March 31, 2019, and CAR further improved to 29.82% as on March 31, 2020.
During FY20 (refers to the period April 1 to March 31), DKGFS has raised equity of Rs.127 crore from Dvara Trust, Leapfrog Financial Inclusion India (II) Ltd Stakeboat Capital Fund–I and Nordic Microfinance Initiative.

Key Rating Weaknesses

Moderate resource profile

Resource profile of Dvara KGFS is concentrated towards term loans from banks/financial institutions which constituted around 89% of the total borrowing as on March 31, 2020, of which banks constitute about 52%.

Profitability continues to be moderate during FY19

Loan portfolio grew at a marginal rate of 15% from Rs.528 crore as on March 31, 2018 to Rs.609 crore as on March 31, 2019. Disbursements grew by 2% from Rs.604 crore during FY18 to Rs.614 crore during FY19.
Net interest margin stood at 9.69% during FY19 as against 8.15% during FY18 mainly due to improvement in the capital structure during the year. Operating Expenses/Average Total Assets have increased from 7.86% as on March 31, 2018, to 8.92% as on March 31, 2019, whereas the credit cost have improved from 1.05% as on March 31, 2018 to 0.76% as on March 31, 2019. Pre-Tax ROTA stood at 2.67% during FY19 as against 2.39% during FY18. ROTA improved from 1.65% during FY18 to 4.65% during FY19 with tax write-back on account of accumulated losses in the books of IFMR Rural Channels and Services Private Limited (IRCS). Loan portfolio grew to Rs.844 crore (Ind-As) as on March 31, 2020. During FY20 (Prov.), Dvara KGFS reported a PAT of Rs.12.86 crore on a total income of Rs.196.77 crore (Ind-As). ROTA stood at 1.38% during FY20 (Prov.) primarily due to increase in Opex during the year.

Geographical concentration of loan portfolio

As on March 31, 2019, Dvara KGFS had presence in 33 districts spanning across 4 states with 90% (PY: 97%) of loan Portfolio in Tamil Nadu followed by 5.16% (PY: 0.44%) in Odisha. Dvara KGFS has entered Karnataka in FY19 and Jharkhand in FY20, respectively. The proportion of Tamil Nadu further reduced to 77% as on March 31, 2020. The improvement in geographical concentration is mainly due to two reasons, namely, higher growth in portfolio in the regions of Odisha & Karnataka and acquisition of Varam Capital Private Limited, which enabled Dvara KGFS to enter Chhattisgarh.

Product concentration

As on March 31, 2020, JLG Loans constituted 92% of the outstanding loans as against 96% as on March 31, 2019. The company has taken initiatives to diversify the earnings profile and its focus will be on Micro Enterprise loans (MEL).
Dvara KGFS also sells products such as insurance, pension plans, remittance products from it branches.

Moderate asset quality

Dvara KGFS has reported a GNPA and NNPA of 1.97% and 0.00% as on March 2019 against 0.13% and 0.00% as on March 31, 2018. Credit cost also increased from 0.2% in FY18 to 0.76% in FY19. Addition to NPAs during FY19 is due to amalgamation of IRCS with Dvara KGFS. In the past, IRCS had provided FLDG to the loans that it originated for Dvara KGFS as per the loan origination agreement. These loans were on the books of IRCS and 100% provisions have been provided for these loans, subsequent to the merger with IRCS, the loans came on to the books of Dvara KGFS. However, Net NPA stands at NIL as on March 31, 2019. The increase in delinquencies in softer buckets is mainly on account of Gaja cyclone in Tamil Nadu. Monthly collection efficiency dropped to 92% in November 2018. However, from December, the collections started improving and monthly collection efficiency stood at 99% in March 2019. 1+ DPD stood relatively high at 6.7% as on March 31, 2019. On Own book portfolio, Gross Stage III assets % (Gross Stage III assets / Gross Advances) & Net Stage III assets % (Net Stage III assets / Net Advances) stood at 2.67% & 1.68% as on March 31, 2020 (Prov.) as against 1.58% and 0.79% as on March 31, 2019, respectively.
Gross Stage III assets (Own book) has moderated from 1.58% as on March 31, 2019 to 2.67% as on March 31, 2020 (prov.). However, 0+ and 90+ DPD (days past due) on AUM basis showed improvement from 7.77% and 2.62% as on March 31, 2019 to 3.50% and 2.39% as on March 31, 2020 (prov.) with majority of the growth in AUM comes from Business Correspondence.

Industry Outlook and Prospects

Post the AP crisis and regulatory intervention by RBI, the microfinance sector has seen strong growth in loan portfolio on account of improving funding profile, control over operating expenses, improving margins and moderate leverage levels. The sector has evolved with the advent of credit bureaus in the sector and subsequent control over asset quality. However, it remains exposed to event based risks and marginal profile of borrowers. The recent outbreak of Covid-19 is likely to impact asset quality and credit costs.
With further improvement expected in the overall MFI industry over the medium term, the ability to withstand event risks and avoid further deterioration in the asset quality leading to impact in the overall profitability will be the key considerations. The credit view will continue to factor in risks associated with unsecured lending, socio-political intervention, geographic concentration and operational risks related to cash-based transaction.

Liquidity: Adequate

ALM profile remains adequate with no cumulative mismatches in any of the time brackets upto 1 year as on March 31, 2020 (Prov.). With majority of the portfolio composition being JLG loans with tenure of 18-24 months and the borrowings remaining long term, ALM looks adequate. Cash & Bank balances as on March 31, 2020, stood at Rs.187 crore. DKGFS has contractual repayments of Rs.134 crore during Q1FY21. However, the company has applied to avail moratorium from its lenders and PTC/DA investors and most of them have accepted for the same. Excluding loans for which moratorium received, contractual repayments for Q1FY21 stood at Rs.77.27 crore. With cash balance of Rs.187 crore as on March 31, 2020 and undrawn limits of Rs.34.50 crore as on May 13, 2020, the company has adequate liquidity.

Analytical approach: Standalone
Applicable Criteria
Criteria on assigning 'Outlook' and 'Credit Watch' to Credit Ratings
CARE Policy on Default Recognition
Rating Methodology- Non Banking Finance Companies
Financial ratios - Financial Sector

About the Company

Dvara Kshetriya Gramin Financial Services Private Limited (Dvara KGFS) formerly Pudhuaaru financial services Pvt. Ltd. (PFSPL) is a non-deposit taking NBFC engaged in providing financial services in remote areas. With the approval of Scheme of Arrangement from RBI & NCLT, Pudhuaaru Financial Services Pvt. Ltd. got amalgamated with the parent IRCS & renamed as Dvara KGFS on March 21, 2019. The services are provided through a network of branches ensuring that every individual and enterprise within a 5 - 25 km radius of his/her residence/place of business has access to financial services. The company is primarily engaged in lending loans through JLG model. Apart from JLG loans, the company also provides jewel loans, MEL loans, consumer durable loans, etc., and liability products including various insurance products and foreign inward remittances.

Dvara KGFS has entered into a Business Transfer Agreement (slump sale agreement) with Varam Capital Private Limited effecting April 01, 2019. After the acquisition, Dvara KGFS has presence in 6 states – Karnataka, Odisha, Tamil Nadu, Uttarakhand, Chhattisgarh and Jharkhand through 8 KGFS (Pudhuaaru, Thenpennaiaaru and Chennai in Tamil Nadu; Keonjhar in Odisha, Sahastradhara in Uttarkhand & Mysuru in Karnataka, Chhattisgarh and Jharkhand) and 299 branches as on March 31, 2020.

Brief Financials (Rs. crore)	FY17 (A) IRCS (Consol.)	FY18 (A) IRCS (Consol.)	FY19 (A) Dvara KGFS (Standalone)
Total operating income	88.89	124.68	162.47
PAT	1.54	9.06	33.20
Interest coverage (times)	1.07	1.23	1.24
Total Assets	453	689	754
Net NPA (%)	0.00	0.00	0.00
ROTA (%)	0.41	1.59	4.65

A: Audited

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	-	-	-	May 2024	236.57	CARE BBB; Stable
Fund-based-LT/ST	-	-	-	-	65.43	CARE BBB; Stable / CARE A3+
Debentures-Non Convertible Debentures-II	INE179P08033	May 30, 2019	13.713%	May 30, 2024	20.00	CARE BBB; Stable
Debentures-Non Convertible Debentures-III	INE179P07118	Dec 01, 2019	13.50%	Nov 30, 2022	0.34	CARE BBB; Stable
	-	Dec 01, 2019	13.50%	Nov 30, 2022	1.01	CARE BBB; Stable
	INE179P07126	Jan 01, 2020	13.50%	Dec 31, 2022	0.20	CARE BBB; Stable
	-	Jan 01, 2020	13.50%	Dec 31, 2022	2.27	CARE BBB; Stable
	-	Feb 25, 2020	13.50%	Feb 25, 2022	0.20	CARE BBB; Stable
	Proposed	-	-	-	45.98	CARE BBB; 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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Term Loan	LT	236.57	CARE BBB; Stable	-	1)CARE BBB; Positive (04-Oct-19)	1)CARE BBB; Stable (05-Oct-18)	1)CARE BBB-; Stable (22-Jan-18)
2.	Fund-based-LT/ST	LT/ST	65.43	CARE BBB; Stable / CARE A3+	-	1)CARE BBB; Positive / CARE A3+ (04-Oct-19)	1)CARE BBB; Stable / CARE A3+ (05-Oct-18)	1)CARE BBB-; Stable / CARE A3 (22-Jan-18)
3.	Debentures-Non Convertible Debentures-I	LT	-	-	-	1)Withdrawn (04-Oct-19)	1)CARE BBB; Stable (28-Nov-18)	-
4.	Debentures-Non Convertible Debentures-II	LT	20.00	CARE BBB; Stable	-	1)CARE BBB; Positive (04-Oct-19) 2)CARE BBB; Stable (03-Jun-19)	-	-
5.	Debentures-Non Convertible Debentures-III	LT	50.00	CARE BBB; Stable	-	1)CARE BBB; Positive (06-Nov-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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