

Dvara Kshetriya Gramin Financial Services Private Limited

November 06, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings ¹	Remarks
Non-Convertible Debenture (Proposed)	50.00 (Rupees Fifty crore only)	CARE BBB; Positive (Triple B; Outlook: Positive)	Assigned

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the proposed non-convertible debenture issue of Dvara Kshetriya Gramin Financial Services Pvt. Ltd. (Dvara KGFS) continues to factor in the experience of senior management team, commensurate loan appraisal, risk management & MIS System and adequate liquidity profile. The rating also takes note of the equity raise of Rs.10 crore in Q4FY19 (refers to the period January 01 to March 31) and 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 and inherent risks associated with its customer segment including sociopolitical intervention risk and regulatory risk.

In light of growth plans envisaged by the company in the medium term, ability of Dvara KGFS to improve its asset quality & profitability while diversifying in terms of geography and effectively manage its growing scale of operations would be the key rating sensitivities.

Outlook: Positive

The outlook is '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. The outlook, however, may be revised to 'Stable' if the company is not able to improve its asset quality and profitability indicators while increasing the scale of operations.

Rating Sensitivities

Positive Factors

- Improvement in scale of operations and profitability on a sustained basis
- Sustained improvement in Geographical concentration and Product Concentration

Negative Factors

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

Credit Risk Assessment

Key Rating Strengths

Experienced management team and part of Dvara group

Dvara KGFS is promoted by Dvara Trust (Formerly IFMR Trust) and the board comprises 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, Deputy CEO has 24 years of Diverse Experience and Vijayakumar G, CFO of Dvara KGFS has 29 years of Experience in various financial institution sector. 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

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

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 7 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.

Comfortable capitalisation levels

Loan Portfolio of Dvara KGFS has seen a marginal growth of 15% from Rs.529 crore as on March 31, 2018 to Rs. 609 crore as on March 31, 2019. The reason for the slowdown in the disbursement in Q3FY19 is mainly due to the impact of Gaja Cyclone in Tamil Nadu.

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 CAR further improved to 30.16% as on June 30, 2019.

Apart from equity raise of Rs.30 crore during September 2018 by way of rights issue, DKFGS has also raised equity of Rs.10 crore in March 2019 and Rs.45 crore in April, 2019 from Dvara Trust, Leapfrog Financial Inclusion India (II) Ltd and Stakeboat Capital Fund-I. The company also raised equity of Rs.82 crore during September 2019 of which Rs.12 crore from Leapfrog and the remaining from 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 90% of the total borrowing as on March 31, 2019 of which banks constitute about 31% as on March 31, 2019.

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.662 crore as on June 30, 2019. During Q1FY20, Dvara KGFS reported a PAT of Rs.3 crore on a total income of Rs.46 crore.

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 Total Portfolio (On Book + Securitized) in Tamilnadu followed by 5.55% (PY: 0.44%) in Odisha. Dvara KGFS has entered Karnataka in FY19 by making Mysuru as KGFS. The proportion of Tamilnadu further reduced to 86% as on June 30, 2019. The improvement in geographical concentration is due to growth in Odisha and Karnataka. With the acquisition of Varam Capital Private Limited, Dvara KGFS also entered Chattisgarh during April 2019.

Product concentration

As on June 30, 2019, JLG Loans constituted 93% 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 SME loans.

Dvara KGFS also sells products such as insurance, pension plans, remittance products from its branches and plans to start selling mutual funds (money market funds) during FY20.

Moderate asset quality; However, Net NPA continues to be Nil

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 Tamilnadu. 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. During Q1FY20, GNPA & NNPA moderated to 2.57% & 0.00% respectively majorly due to the impact of Gaja Cyclone in Tamilnadu.

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, on account of various events post demonetization, collection efficiency of the MFIs had deteriorated during FY17. This has impacted the asset quality of the MFIs leading to increase in credit costs during FY17 and FY18. However with improvement in the scenarios during FY18, the overall industry had grown by around 47% during FY19 in terms of AUM and collection efficiency of the overall industry improved during FY18 with 30+dpd improved to 1.73% as on March 31, 2019 from 4.03% as on March 31, 2018 (source: MFIN). 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 comfortable with no cumulative mismatches in any of the time brackets upto 1 year as on September 30, 2019. 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 stood at Rs. 153 crore as on September 30, 2019.

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](#)

Background

Dvara Kshetriya Gramin Financial Services Private Limited (Dvara KGFS) formerly Pudhuaaru financial services Pvt. Ltd. (PFSP) 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 micro finance loans through JLG model. Apart from JLG loans, the company also provides jewel loans, SME loans, consumer durable loans, etc. and liability products including various insurance products and foreign inward remittances.

As on March 31, 2019, Dvara KGFS was operating in 4 States – Karnataka, Odisha, Tamilnadu & Uttarkhand through 5 KGFS ((Pudhuaaru and Thenpennaiaaru in Tamil Nadu; Keonjhar in Odisha, Sahastradhara in Uttarkhand & Mysuru in Karnataka) through 221 Branches.

Dvara KGFS has entered into a Business Transfer Agreement (slump sale agreement) with Varam Capital Private Limited. After the acquisition, Dvara KGFS has presence in 5 states through 7 KGFS and has 258 Branches as on June 30, 2019.

(Rs. crore)

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)	FY19 (A)
	IRCS (Consol.)	IRCS (Consol.)	Dvara KGFS (standalone)
Total 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

Note: a). A - Audited

b). Ratios have been computed based on average of annual opening and closing balances

c). NIM has been calculated as net interest income/ average annual total 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 Number	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Debentures-Non Convertible Debentures	-	-	13.50%	-	50.00	CARE BBB; Positive

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.	Fund-based - LT-Term Loan	LT	184.71	CARE BBB; Positive	1)CARE BBB; Positive (04-Oct-19)	1)CARE BBB; Stable (05-Oct-18)	1)CARE BBB; Stable (22-Jan-18)	1)CARE BBB- (27-Oct-16)
2.	Fund-based-LT/ST	LT/ST	115.29	CARE BBB; Positive / 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)	1)CARE BBB- / CARE A3 (27-Oct-16)
3.	Debentures-Non Convertible Debentures	LT	-	-	1)Withdrawn (04-Oct-19)	1)CARE BBB; Stable (28-Nov-18)	-	-
4.	Debentures-Non Convertible Debentures	LT	20.00	CARE BBB; Positive	1)CARE BBB; Positive (04-Oct-19) 2)CARE BBB; Stable (03-Jun-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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