CARE Ratings
Professional Risk Opinion

Fedbank Financial Services Ltd.

July 31, 2019

Ratings

Instruments/facilities	Rated Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	2,000 (enhanced from 1,750) (Rs. Two thousand crore only)	**CARE AA-; Stable (Double A Minus; Outlook: Stable)**	**Reaffirmed**

Details of instruments/facilities in Anneuxre-1

Detailed Rationale & Key Rating Drivers

The rating continues to factor in the strong parentage of Fedbank Financial Services Ltd. (Fedfina), being a subsidiary of The Federal Bank Ltd. and the resultant financial and operational support from the parent. The rating also derives comfort from the high degree of management integration & brand linkage with FBL. The rating also factors in Fedfina's comfortable capitalization levels, adequate liquidity position and moderate profitability. The rating is however constrained by moderate asset quality, moderate scale of operations and limited portfolio seasoning, geographical concentration and market risk in gold loan portfolio. Continued parentage, diversification of business operations, profitability, capitalization and asset quality are the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Strong parentage and expected support with brand linkage and management integration: Fedfina is a subsidiary of The Federal Bank Ltd. (FBL; rated 'CARE AA; Stable'). The board of Federal Bank has approved 26% strategic investment by private equity player True North in FedFina. Further, True North has the option to acquire upto 45% stakes as per the agreement. During FY19, Fedfina received fresh equity infusion of around Rs. 168.60 crore from True North; as a result Federal Bank's stake in Fedina has been reduced to 82.6% as March 31, 2019.

Fedfina has high level of integration with FBL and shares its brand identity. The strategic importance of Fedfina to FBL is visible from the high degree of management integration wherein the MD and a director of FBL is on the board of Fedfina. Furthermore, Fedfina is also engaged in distribution of loan products for its parent. Fedfina also enjoys financial flexibility on account of its parentage.

Comfortable capitalization levels: Fedfina has adequate capitalization levels. As on March 31, 2019, Fedfina's CAR Ratio stood at 22.50% with Tier I CAR at 20.99% (FY18: CAR 17.22% and Tier I CAR 16.95%). The improvement in CAR ratio in FY19 was due to fresh capital infusion by True North. In addition, high levels of Tier I capital provides the company adequate headroom for raising Tier II capital for funding future business expansion. As on March 31, 2019, Fedfina's overall gearing level was comfortable at 3.82 times (4.62 times as on March 31, 2018).

Moderate Profitability: During FY19, PAT grew by 14% as compared to 31% growth in total income, mainly due to increase in borrowing and provision & write off costs. Decrease in proportion of relatively high yielding gold loan book coupled with increase in borrowing costs resulted in moderation in NIM to 6.92% in FY19 as compared with 8.51% in FY18. Decline in share of Gold loan portfolio also resulted in reduction in operating cost and the operating cost as percentage of total average assets reduced from 5.46% in FY18 to 5.11% in FY19. Moderation in NIM and credit costs resulted in decline in ROTA despite improvement in operating cost, ROTA (Return on Average Total Assets) stood at 1.95% in FY19 as against 2.48% in FY18.

Key Rating Weaknesses

Geographic concentration & market risk: The Company's scale of operations remained moderate and exhibits geographic concentration in its loan portfolio as 100% of its gold loan portfolio as on March 31, 2019 has been originated from Southern India. Besides geographic concentration, the company is exposed to market risk associated with gold prices since 22% of its portfolio constitutes gold loans. However, average LTV in gold loan segment stood at 65-75%.

Moderate scale of operations and limited portfolio seasoning: Fedfina has a relatively moderate scale of operations which can be witnessed from its loan portfolio size of Rs.2,004 crore as on March 31, 2019 (Rs.1,422 crore as on March 31, 2018) which includes 22% of Gold Loan, 39% of LAP, 19% of wholesale lending, 17% small ticket LAP with remaining 3% being others Fedfina started its LAP business in 2013 and Wholesale lending business in 2014, hence these portfolios are yet to be seasoned. Therefore, the company's ability to scale up its business operations besides maintaining asset quality is yet to be tested.

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

Moderate asset quality: Fedfina's asset quality remained comfortable with GNPA and NNPA ratios at 2.06% and 1.81% respectively as on March 31, 2019 (March 31, 2018: GNPA: 0.92% and NNPA: 0.80%).

Analytical approach:
CARE has analyzed standalone credit profile of Fedfina along with its operational and managerial linkages with its parent, Federal Bank Ltd.

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
CARE Policy on Default Recognition
Rating Methodology: Factoring Linkages in Ratings
Rating Methodology- Non Banking Finance Companies
Financial ratios - Financial Sector

Adequate Liquidity Position
The liquidity profile of the company as on March 31, 2019 exhibits positive cumulative mismatch (excluding unutilised working capital facilities) in upto one year time bucket. Furthermore, the company has sufficient unutilised working capital facilities worth Rs.382 crore of which around Rs.120 crore is from the parent, Federal Bank Ltd. As on March 31, 2019, borrowings from CP constituted 12% of the total borrowings. Further, given the rising LAP and wholesale loan portfolio, the company has started tapping long term bank loans which is expected to mitigate its future short term mismatches if any.

About the Company
Fedfina is a Non Deposit accepting Systematically Important Non-Banking Finance Company (NBFC-ND-SI) and a subsidiary of FBL. Incorporated in 1995, the company received the NBFC license from RBI in August 2010, post which the company has commenced the gold loan business. The company also ventured into the LAP segment in FY13 while wholesale lending was started in Q4FY14. The four states Andhra Pradesh, Telangana, Karnataka and Tamil Nadu cumulatively accounted for 100% of the gold loan portfolio as on March 31, 2019 while the LAP and wholesale portfolios are concentrated mainly in Maharashtra and Gujarat, Karnataka and Tamil Nadu. As on March 31, 2019, Fedfina had a tangible net-worth of Rs.458 crore and outstanding loan portfolio of Rs.2,004 crore.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total Income	197.66	258.92
PAT	30.80	35.08
Interest coverage (times)	1.64	1.44
Total Assets	1476.22	2123.93
Net NPA (%)	0.80	1.81
ROTA (%)	2.48	1.95

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	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Long Term Bank Facilities	-	-	Upto 5 years	2,000	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.	Fund-based-Long Term	LT	2000.00	CARE AA-; Stable	-	1) CARE AA-; Stable (31-Dec-18) 2)CARE AA-; Stable (21-Sept-18) 3)CARE AA-; Stable (10-Jul-18)	1)CARE AA-; Stable (5-Jan-18) 2)CARE AA-; Stable (11-Oct-17) 3)CARE AA-; Stable (12-Jul-17)	1)CARE AA-; Stable (10-Feb-17)
2.	Debentures-Non Convertible Debentures	LT	200.00	CARE AA-; Stable	-	1) CARE AA-; Stable (31-Dec-18)	1)CARE AA-; Stable (5-Jan-18)	1)CARE AA-; Stable (10-Feb-17)

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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About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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