Midland Microfin Ltd

January 5, 2018

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	210 (Enhanced from Rs. 110 crore)	CARE BBB; Stable (Triple B; Outlook: Stable)	**Reaffirmed**
Total	210.00 (Rs. Two Hundred Ten Crore Only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale& Key Rating Drivers

The rating of Midland Microfin Limited (MML) continues to derive strength from the experience of the promoters and management team, MML's adequate track record, good loan origination, appraisal and portfolio management systems in place and company's ability to maintain good asset quality profile. The company has been able to ensure high collection efficiency post demonetization resulting in limited impact on asset quality. However, the rating is constrained by the small scale of operations, moderate earnings, increasing gearing levels, high geographical concentration of operations and inherent socio-political, regulatory and operational risks in micro finance business.

The ability of MML to grow its portfolio and improve profitability, while maintaining a good asset quality, diversifying its operations geographically and improve its overall gearing would be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters and management team

The promoters of MML belong to the Midland group of Punjab engaged into asset finance and banking business. The management of MML is headed by Mr Amardeep Samra, Managing Director, who has an experience of over 19 years in the field of finance, hire-purchase, leasing, commercial real estate development and management of Agri based co-operative societies. He is assisted by Mr Vijay Kumar Bhandari, Chairman of the Board of MML with over 34 years of experience in the banking industry and Mr Dinesh Gupta, who has over two decades of experience as a corporate advisor and investment consultant. MML has created separate departments with clearly demarcated roles and responsibilities for handling different functions. MML has formed different board committees for technically review and formulation of policies and procedure for the working of the MFI including audit committee, risk management committee, board management committee, and head office executive committee.

Strong loan origination, appraisal & portfolio management systems in place

MML has strong internal controls and procedures from group formation, loan appraisal and sanction to disbursement, loan utilization checks and collection with checks at multiple levels to ensure transparency of operations. MML also has a separate internal audit team conducting audit of the centre meetings, branches and head office at regular intervals. The MIS helps in monitoring disbursements, collection and cash reconciliation on a daily basis along with maintaining security of data and faster access to reports for day-to-day monitoring. MML has strengthened its IT infrastructure and software by migrating to a more flexible and structured software e-Fimo which is a complete ERP based Core Micro finance solution with automated functionalities.

Comfortable capital adequacy albeit increasing gearing levels

MML's capital adequacy ratio (CAR) and Tier-I CAR stood at 25.52% and 15.22% respectively as on Sept 30, 2017. MML has raised preference share capital of Rs. 25.50 crore (including Rs. 12.75 crore share premium) on Oct 11, 2017 which is likely to improve capital adequacy ratios further. Large part of these preference shares (around 80%) were longer tenure maturity (7-10 years). The overall gearing levels (excluding preference capital from debt as well as equity) increased to

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

6.21x as on Sept 30, 2017 as against 4.64x as on March 31, 2017 (P.Y. 4.21x). The ability of the company to raise equity capital and reduce its overall gearing going forward would be crucial for its credit profile.

Good asset quality

MML has been able to maintain good asset quality since 2011 when it started its operations. MML's asset quality is supported by rigorous supervision by operations team and regular checks and controls of finance and internal audit department. GNPA and NNPA stood at 2.10% and 0.20% respectively as on September 30, 2017. The overall collection efficiency since demonetization (Nov 2016-Nov 2017) has been 97%. However, the company's ability to maintain asset quality with further increase in scale of operations as it expands to new geographies is yet to be seen.

Key Rating Weaknesses

Moderation in earnings profile during H1FY18 due to impact on operations post demonetization

MML's total income had grown by 52% to Rs. Rs. 46.62 crore during FY17 on the back of disbursements upto October 2016 (prior to demonetization). However, de-growth of portfolio since demonetization has meant moderation in interest income earned and decline in Net Interest Margin during FY17 and H1FY18 to 9.04% and 4.47% respectively from 10.79% during FY16. Also, MML has had to provide for higher operating expenses due to deployment of staff towards recovery operations as against disbursements. Consequently, the operating cost ratio (OCR) increased to 12.90% for FY17 due to higher incidence of fixed costs (administrative and employee expenses) over a reduced asset base as at the end of FY17. The operational costs have been high during H1FY18 due to setting up of new regional offices (Chandigarh, Jaipur, Varanasi, Patna) and expansion of branch network in the new geographies (Bihar and Western UP) that MML is planning to enter. The operational costs of MML have also traditionally remained high due to emphasis on strict controls and practices which include supervision of operations at branch, cluster and headquarters level. With improving economies of scale, the operating expenses had been consistently declining since FY14 as reflected by operating cost ratio (OCR) which declined from 11.18% during FY14 to 7.12% during FY16. MML has also provided for higher contingent provision on standard assets of Rs. 1.66 crore during H1FY18 as against provision of Rs. 0.76 crore during FY17. Consequently, MML has reported net loss Rs. 2.08 on income of 21.33 crore for H1FY18 as against PAT of Rs. 4.31 crore for FY17. As the company expands its portfolio size in H2FY18 and consequently its NIMs and level of operating expenses improve, its profitability is likely to improve in H2, FY18.

Geographical concentration of portfolio base; concentration declining to some extent and likely to decline further

MML was operating in 80 districts across 3 states (viz. Punjab, Rajasthan and Haryana) as on Sept 30, 2017. The company being a Punjab based player has major portfolio concentrated in Punjab. However, the expansion and new branches being opened in Haryana and Rajasthan the concentration of portfolio of MML in Punjab has reduced to 62% as on Sept 30, 2017 as against 72% as on March 31, 2017. The Top State concentration/Net Worth however has increased to 431% as on Sept 30, 2017 (as against 208% as on March 31, 2017 and 363% as on March 31, 2016). As the company expands its presence to two more states (Bihar and Western UP) in current fiscal, its portfolio concentration is likely decline further.

Industry Prospects

On account of various events post demonetization, collection efficiency of the MFIs/newly converted SFBs has deteriorated. This has impacted the asset quality of the MFIs/SFBs leading to increase in credit costs. It is expected that the loss on account of this event is likely to be in the range of 5-10% of the total loan portfolio for the sector.

Given the current situation and any further deterioration in the situation from hereon, the profitability of the MFIs/SFBs are expected to take a severe hit in FY18 on account of higher provisioning costs. Overall FY18 is expected to be a challenging year for the sector with growth expected to moderate on the back of demonetization as the MFIs/SFBs will primarily concentrate on overhaul of entire operations to minimize future losses. The portfolio growth for the sector is expected to be around 25 to 30% y-o-yin FY18 as compared to 50-60% y-o-y growth achieved in the past few years. However given the market potential, the sector is likely to continue its high growth post normalization of situation with MFIs continuing to attract funds and improving operational efficiencies to maintain profitability.

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.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology for Non-Banking Financial Companies
Financial Sector Ratios

About the Company

Midland Microfin Ltd (MML) was originally incorporated as 'Sajan Hire Purchase Pvt Ltd (SHPPL)' on May 28, 1988. SHPPL was engaged in hire purchase business. In June 2010, the Midland group of Punjab promoted by Mr. Amardeep Samra and family acquired SHPPL with the aim of venturing into the microfinance business and the name of the company was changed to MML in January 2011. The hire purchase business was also discontinued at the same time. MML is registered with RBI as a NBFC-MFI (Non-Banking Financial Company-Microfinance Institute) since January 2015.

MML is currently operating in three states (i.e. Punjab, Rajasthan and Haryana). The operations are managed through a network of 580 branches with total of 1,33,481 JLG individual active borrowers and loan portfolio of Rs. 203.09 crore as on Sept 30, 2017.

Brief Financials (Rs. crore)	FY16 (A)	FY17 (A)
Total operating income	30.69	40.62
PAT	3.71	4.31
Interest coverage (times)	1.41	1.27
Total Assets	178.04	230.74
Net NPA (%)	Nil	Nil
ROTA (%)	2.85	2.11

A: Audited

Status of non-cooperation with previous CRA: Brickworks Ratings vide its Press Release dated December 31, 2016 has stated its inability to review the rating in the absence of information from the company to review the ratings.

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

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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In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

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
Fund-based - LT-Term Loan	-	-	Dec-2020	210.00	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 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015
1.	Debentures-Non Convertible Debentures	LT	25.00	CARE BBB; Stable	1)CARE BBB; Stable (05-Sep-17)	1)CARE BBB (15-Jul-16)	1)CARE BBB- (31-Jul-15)	1)CARE BBB- (30-Apr-14)
2.	Fund-based - LT-Term Loan	LT	210.00	CARE BBB; Stable	1)CARE BBB; Stable (05-Sep-17)	1)CARE BBB (15-Jul-16)	1)CARE BBB- (31-Jul-15)	-

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