Midland Microfin Ltd

November 28, 2018

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	210.00 (Rs. Two Hundred Ten Crore Only)	CARE BBB; Stable (Triple B; Outlook: Stable)	Reaffirmed
Non-Convertible Debentures	25.00 (Rs. Twenty Five crore only)	CARE BBB; Stable (Triple B); Outlook: Stable	Reaffirmed

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, diversified resource base and adequate liquidity position. The ratings continue to factor in the good loan origination, appraisal and portfolio management systems in place and company's ability to maintain good asset quality profile over the years. The ratings also take into consideration scaling up of loan book to Rs.448 cr as on September 30, 2018. However, the rating is constrained by increasing gearing levels, moderate profitability during FY18 although improvement seen in H1FY19, high albeit reducing geographical concentration of operations, increased borrower concentration risk and inherent risks involved in the microfinance industry including unsecured lending, marginal profile of borrowers, socio-political intervention risk and regulatory uncertainty.

The company intends to raise equity capital of Rs.30 crore in H2, FY19 to reduce gearing levels. The ability of MML to raise the proposed equity capital of Rs.30 crore in timely manner and improve its overall gearing, grow its portfolio and improve profitability, diversify its operations geographically while maintaining good asset quality 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 lending business. The management of MML is headed by Mr Amardeep Samra, Promoter and Managing Director, who has extensive experience of nearly two decades in the field of finance, hire-purchase, leasing, commercial real estate development and management of Agri based co-operative societies. The overall operations of MML are governed by a 7 member Board including 3 independent directors. 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. MML has created separate departments with clearly demarcated roles and responsibilities for handling different functions.

MML has been carrying out microfinance lending activities since January 2011 and has gained experience in the group lending business and is one of the medium size NBFC-MFI in the country in terms of scale. MML had Assets under Management (AUM) of Rs.448 crore as on Sept-18 (growing significantly from Rs.113 crore since Mar-17).

Good loan origination, appraisal & portfolio management systems in place

MML has good internal controls and procedures from group formation, loan appraisal and sanction to disbursement, 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 adequate IT infrastructure and management information systems in place for monitoring of its operations.

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. The overall collection efficiency of MML post demonetization was better than peers. GNPA and NNPA stood at 0.56% and Nil as on Sept 30, 2018 as against GNPA and NNPA of 2.10% and 0.20% respectively as on September 30, 2017.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.

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

Scaling up of loan book

MML has seen nearly 210% growth in its AUM in FY18 from Rs.113 crore as on Mar-17 to Rs.351 cr as on Mar-18. The AUM have further grown by 28% during H1FY19 to Rs.448 cr as on Sept-18. MML has expanded its operations in Rajasthan and Haryana while also entering into newer geographies over the last 1.5 years.

Diversified Resource Profile and Comfortable Liquidity

The major source of external funding for MML has been term loan from banks/FIs. MML has associations with over 20 Banks/FIs as on June 30, 2018. MML has also accessed securitization route for tapping funds and raised funds through issue of long term NCDs and Preference Shares. Term loans from Banks and SIDBI constituted 18% of the borrowings of MML, loans from FIs/NBFCs constituted 50%, Debentures/ Tier-II Bonds (17%), Preference Shares (8%), Securitization (8%) of the overall funding sources of MML (as on Sept-18).

The company has a favorable liquidity position given the longer tenure borrowings repayable over 2-10 years as against shorter tenure of MFI loans of upto 2 years as also reflected by a well matched ALM as on Sept 30, 2018. Company's expected inflows in up to one year bucket (including bank balance and liquid assets) were 2.1 times of expected outflows. The company maintains sufficient liquidity buffer at all times to meet its immediate disbursement requirements and any emergent payments.

As on Oct 29, 2018, MML had free cash and bank balance of Rs.68.62 crore (including liquid investment of Rs.12.70 crore) and had un-availed sanctioned funding lines of Rs.5 crore.

Industry Prospects

On account of various events post demonetization, collection efficiency of the Micro Finance Institutions (MFIs) and Small Finance Banks (SFBs) had deteriorated. This has impacted the asset quality of the MFIs/SFBs leading to increase in credit costs. Consequently, the profitability of the MFIs/SFBs took a severe hit in FY18 on account of higher provisioning costs. However, the MFI Industry saw a growth of around 50% in terms of AUM during FY18 and asset quality of the MFI's has improved during FY18 as reflected 30+DPD of 4.44% as on March 31, 2018 (as against 11.05% as on March 31, 2017) (source: MFIN).

Key Rating Weaknesses

Increasing gearing levels; albeit comfortable capital adequacy for current level of operations

MML's capital adequacy ratio (CAR) and Tier-I CAR stood at 21.92% and 14.37% as against CAR and Tier-I CAR of 25.52% and 15.22% respectively as on Sept 30, 2017. The capital adequacy of MML is above the regulatory capital requirement due to significant capital raised through issue of preference shares during FY18 (65% of it is repayable after 5 years). MML has also raised equity capital of Rs.10 crore during H1FY19.

There has been moderation in the capital structure of MML over the last 12 months as reflected by increase in adjusted overall gearing levels (ratios of borrowings including preference capital and securitized portfolio /Tangible Net-worth) from 7.06x as on Sept-17 to 9.82x as on Sept 30, 2018. Net adjusted Gearing (debt reduced by for cash and bank balance and liquid investments of Rs.93.48 cr) stood at 7.9x as on Sept 30, 2018. This has been on account of largely debt funded growth and most of the capital being raised through issue of redeemable preference shares (Rs.28.20 crore raised during FY18).

MML is in the process of raising additional equity capital of Rs.30 crore during H2FY19. The ability of the company to raise the proposed equity capital in a timely manner and reduce its overall gearing going forward would be crucial for its credit profile.

Moderation in earnings profile during FY18 due to impact on operations post demonetization however improvement seen in H1, FY19

MML's operations were impacted post demonetization. Although, the AUM of MML grew by 210% from Rs.113 cr as on Mar-17 to Rs.351 cr as on Mar-18, the overall income grew only 22% from Rs.46.6 cr during FY17 to Rs.56.8 crore during FY18 as much of the growth in loan book was seen during H2FY18 (60% of the disbursements). This along with increase in gearing levels resulted in moderation in net interest margin from 9.04% during FY17 to 6.39% in FY18. Further, increasing in operating expenses owing to setting up nearly 50 additional branches and opening of new regional offices (Chandigarh, Jaipur, Varanasi, Patna) along with incurrence of higher operating expenses due to deployment of staff towards recovery operations as against disbursements uptil H1FY18 resulted in Adj. Opex/ATA increasing from 7.44% during FY17 to 8.32% during FY18. The operational costs of MML have traditionally remained high due to emphasis on greater controls and practices which include supervision of operations at branch, cluster and headquarters level.

Consequently, MML has reported PAT of Rs.1.18 crore during FY18 (after reporting losses of Rs.3.09 crore during H1FY18) as against PAT of Rs.4.31 crore during FY17 despite the considerable growth in loan book. MML has seen improvement in profitability with increase in NIMs and reduction in operating expenses over the period H1FY18-H1FY19 as against losses of Rs.2.08 cr in H1FY18 with expansion of portfolio. MML reported PAT of Rs.3.26 crore in H2FY18 and Rs.5.31 cr in H1FY19.

Geographical concentration of portfolio; albeit reducing; however borrower concentration risk emanating from few relatively higher ticket size corporate exposures

MML was operating in 69 districts across 5 states (viz. Punjab, Rajasthan, Haryana, UP and Bihar) as on Sept 30, 2018. The company being a Punjab based player has major portfolio concentrated in Punjab. However, with the new branches being opened in Haryana and Rajasthan and expansion of the footprint in new states of UP and Bihar, the concentration of portfolio of MML in Punjab has reduced from 72% as on March 31, 2017 to 48% as on Sept 30, 2018. As the company expands its presence in Bihar and Western UP in current fiscal, its portfolio concentration in single state is likely decline further. The Top State concentration to Net Worth has however, increased from 220% as on March 31, 2017 to 436% as on Sept 30, 2018 with the growth in loan book in Punjab.

MML has extended corporate loans to 3 entities over the last 12 months of ticket size of Rs.5-15 crore. MML's corporate loan book was Rs.22 crore which was 5% of the AUM as on Sept-18. Although, there are monthly amortizing loans, however, given their relatively larger ticket size as compared to MFI loans, the borrower concentration risk of MML has increased with buildup of wholesale book.

Inherent industry risks

The microfinance sector continues to be impacted by the inherent risk involved viz. socio-political intervention risk and regulatory uncertainty and risks emanating from unsecured lending and marginal profile of borrowers who are vulnerable to economic downturns besides 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 five states (i.e. Punjab, Rajasthan, Haryana, Bihar and Uttar Pradesh). The operations are managed through a network of 125 branches across 69 districts with total of 2.59 Lac active JLG borrowers and loan portfolio of 448 crore as on Sept 30, 2018.

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	46.62	56.80
PAT	4.31	1.18
Interest coverage (times)	1.33	1.14
Total Assets	230.74	387.32
Assets under Management	113.27	350.79
Net NPA (%)	0.00	0.00
Adj. ROTA (%)	2.11	0.37

A: Audited
@Adjusted Ratios: Adjusted for off-book portfolio

Status of non-cooperation with previous CRA: Not Applicable

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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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	-	-	*	210.00	CARE BBB; Stable
Debentures-Non Convertible Debentures	April 07, 2014	11-12%	April 1, 2024	25.00	CARE BBB; Stable

*including proposed

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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
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)
2.	Fund-based - LT-Term Loan	LT	210.00	CARE BBB; Stable	-	1)CARE BBB; Stable (05-Jan-18) 2)CARE BBB; Stable (05-Sep-17)	1)CARE BBB (15-Jul-16)	1)CARE BBB- (31-Jul-15)

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