SBFC Finance Limited

April 05, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	200.00	CARE A+; Stable	Assigned

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The rating assigned to the bank facilities of SBFC Finance Limited (SBFC) factors in the comfortable capital structure along with improved gearing and improving earnings profile and experience of the senior management team. The rating further takes into account the retail-focused approach of the company along with the lending segments being secured in nature with lower loan-to-value (LTV) and adequate seasoning. However, the rating remains constrained by the credit profile of the borrower segment dealt by the company, which may lead to asset quality issues.

The company's ability to maintain comfortable leverage and scaling up of operations along with maintaining the asset quality will remain a key monitorable.

Rating sensitivities: Factors likely to lead to rating actions.

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

- Scaling up of loan book along with maintaining leverage at 3x.
- Sustained improvement in profitability metrics with return on total assets (ROTA) above 4% while maintaining asset quality with gross non-performing assets (GNPA) of less than 3%.

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

- Deterioration in the overall asset quality with GNPA above 5% on a sustained basis.
- Moderation in capitalisation with leverage beyond 4x.
- Deterioration in profitability on sustained basis with ROTA below 2%.

Analytical approach: Standalone

CARE Ratings Limited (CARE Ratings) has considered the standalone profile of SBFC.

Outlook: Stable

The Stable outlook reflects expectation of continued operational and financial position along with comfortable capitalisation levels.

Key strengths

Experienced management team; with retail lending experience.

SBFC has an experienced management team with rich experience in the finance industry. The company is headed by Mr. Aseem Dhru, Managing Director (MD) & Chief Executive Officer (CEO), who has 28 years of experience in the financial services industry. Prior to joining the company, he was associated with HDFC bank for 20 years and served as Group head- Business banking and agriculture finance before his current stint in SBFC. He also served as Ex MD & CEO of HDFC Securities Ltd and Nominee Director in HDB Finance Ltd. Furthermore, SBFC has appointed seasoned professionals from the banking and non-banking financial (NBFC) sectors having rich retail experience across all major functions and product segments. The Clermont (73.25%) and Arpwood group (19.67%) have also strong representation on the board.

Focused secured book with adequate seasoning and lower LTV in retail segment.

SBFC strategy revolves around better quality customers (CIBIL Score 700+), lower LTV (45% in micro enterprise and 70% in gold loans) majorly secured by way of self-occupied property and gold in tier-2 and tier-3 cities. The assets under management (AUM) for SBFC comprises owned originated book (80.53%), co-originated on book (2.09%), co-originated off book (8.34%), and portfolio acquired from Karvy (2.45%). Furthermore, there are DHFL PTC investments of ₹316.10 crore as on December 31, 2022. SBFC operates in the secured retail segment (96% of loan portfolio) basically lending to micro enterprises (ME) secured majorly

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications.

by self-occupied residential and commercial properties (around 90% of ME loan portfolio) and loan against gold (20% of loan portfolio). Unsecured lending book comprise 4% of the loan portfolio; however, this segment has been discontinued by the company since September 2022. SBFC had introduced ticket size of less than ₹30 lakh from January 2019 in ME portfolio. Thus, as on September 30, 2022, the share of less than ₹30 lakh ticket size is 87% of the portfolio, which has increased from 54% in FY20. The loan against gold segment has an average ticket size of ₹1.00 lakh and tenor of up to 12 months.
In addition to the on-book loans, the company had made investment in PTC issued by DHFL (Home loan and Loan against property) in June 2019. Original investment from SBFC was ₹2,365 crore (on the book of ₹2,957 crore) on this book and SBFC acts as a servicer to ensure collection efficiency. The structure initially had a first loss cover of 25%, which subsequently increased to 274% as of February 2023. As the underlying loans are performing good, and also given the high first loss cover, there is no credit loss provision for these investments. Furthermore, the total pool balance has been run down to ₹1,138 crore in February 2023. Given the monthly collection of around ₹25 crore, this portfolio will run down in the next few months.

Improving earnings profile

SBFC's profitability profile is consistently on an improving trend since FY18, where the profit after tax (PAT) improved from ₹3 crore in FY18 to ₹85 crore in FY21 driven by the growth in the loan book from ₹778 crore as on March 31, 2018, to ₹2,148 crore as on March 31, 2021. However, in FY22, due to higher opex (branch expansion, employee expenses) of ₹177 crore and higher credit cost (provisions and write-offs) of ₹49 crore, profitability of the company declined from ₹85 crore in FY21 to ₹64 crore in FY22 leading to decline in ROTA to 1.56% in FY22 from 2.14% in FY21. This increase in the credit cost was due to the loss incurred in sales to ARC and write-offs of loans affected due to COVID-19.
However, the 9MFY23 profitability has surpassed the FY22 PAT at ₹107 crore leading to a ROTA of 3.06%. The profitability levels are expected to be above average for SBFC for FY23 given the performance of 9MFY23, which has already surpassed the FY22 profitability. Furthermore, the DHFL portfolio has a floating interest rate of 11%, which is lower than the average yield of 15.7% of SBFC on book loan portfolio. Post the running down of this portfolio in the next few months, SBFC will be able to originate in higher yields, thus improving the profitability levels.

Healthy capitalisation and improved gearing levels

As on December 31, 2022, the CRAR of SBFC stood at 33.23% as against the regulatory requirement of 15% indicating a strong cushion over the regulatory requirement. The tangible net worth (TNW) of SBFC increased to ₹1,418 crore on December 31, 2022, from ₹1,023 crore on March 31, 2022. And the gearing improved to 2.40x as on December 31, 2022, from 2.88x as on March 31, 2022. The improvement was driven by the equity infusion of ₹250 crore in 9MFY23 and heathy internal accruals. SBFCs gearing philosophy is to maintain a leverage of 4.0x.

Key weaknesses

Moderate asset quality; albeit improvement

Historically, asset quality of SBFC was impacted due to legacy book acquired from Karvy along with unsecured segment. As on December 31, 2022, the GNPA of SBFC stood at 2.51% in the retail book, of which focused book is the ME segment and loan against gold segment. The loan against gold segment is secured in nature and the underlying assets on gold loans provides comfort on recoverability. The overall asset quality improved from 3.10% as on March 31, 2021, to 2.74% as on March 31, 2022. Given the improvement in the overall collections, write-offs and sale of loans to ARCs contributed towards improving the asset quality. The collection efficiency ME segment and co-origination was 98% in each segment during Q3FY23. Net NPA (NNPA) as on December 31, 2022, stood at 1.54% with PCR on NPAs of 38.67%. The restructured book stood at 2.34% of the on-loan book in 9MFY23.

Concentration of the loan portfolio in the ME segment

SBFC lends loans to the micro enterprise (ME) segment, which is characterised by the marginal credit profile of the borrowers. In order to mitigate the same, the company restricts the LTV, and as on March 31, 2022, the majority of the outstanding loan portfolio had an LTV of around 40-45%. However, given the relatively lower ticket size and value of collateral security (self-occupied properties) and higher credit score (+700) of the customer, CARE Ratings expects there will be negligible loss of income (without any principal loss).

Liquidity: Adequate

As on February 2023, SBFC had total liquidity of ₹440 crore by way of cash and bank balance of ₹75 crore and liquid investments worth ₹365 crore against debt obligation of ₹518 crore for the next 3 months. Also, as per the structural liquidity statement as on December 31, 2022, the are no mismatches in any of time bucket up to 1 year providing additional comfort. The company has successfully raised funds from numerous lenders, including PSU/Pvt banks/NBFCs.

Applicable criteria

Policy on default recognition
Financial Ratios - Financial Sector
Rating Outlook and Credit Watch
Rating Methodology-Non-Banking Financial Companies
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro-Economic Indicator	Sector	Industry	Basic Industry
Financial Services	Financial Services	Finance	Non-Banking Financial Company (NBFC)

SBFC Finance Limited is registered with the Reserve Bank of India (RBI) as a systematically important non-deposit taking non-banking financial company (NBFC-ND-SI). The company commenced its operations in September 2017 after acquiring the secured retail portfolio from Karvy Financial Service Ltd along with its branch infrastructure and staff. The company is into the lending business and offers products, such as secured MSME loans and loan against gold (LAG) with majority of the customers being low- and middle-income small business customers, salaried or working-class individuals and self-employed customers in urban and semi-urban areas in India, comprising Tier-2 and Tier-3 cities. Unsecured loans like personal loans and business/professional loans have been discontinued from September 2022. As on December 31, 2022, the operations of the company are spread across 16 states and two union territories with total 137 branches in 105 cities. The company is backed by the promoters, viz., SBFC Holdings Pte Ltd, Clermont Financial Pte Ltd, Arpwood Partners Investment Advisors LLP, Arp wood Capital Private Limited and Eight45 Services LLP.

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	9MFY23 (UA)
Total income	511	533	532
PAT	85	64	107
Overall gearing (times)	2.95	2.88	2.40
Total assets	4,226	4,515	5,335
Net NPA (%)	1.95	1.63	1.54
ROTA (%)	2.14	1.56	3.06
RONw (%)	10.05	6.53	11.69

A: Audited; UA: Unaudited; Note: 'the above results are latest financial results available'.
All ratios are as per CARE's calculation.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of the covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based-Long Term (Proposed)	-	-	-	-	200.00	CARE A+; Stable

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type*	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based-Long Term	LT	200.00	CARE A+; Stable	-	-	-	-

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities- Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based-Long Term	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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