

Correction: India Ratings Assigns Sindhuja Microcredit's Bank Loans 'IND BBB-' / Stable

28

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By Ruhi Pabari

This announcement rectifies the version published on 27 February 2020 to correctly state the assets under management at FYE19. The amended version is as follows: India Ratings and Research (Ind-Ra) has rated Sindhuja Microcredit Private Limited's (Sindhuja Microcredit) bank loans at 'IND BBB-' with a Stable Outlook. The detailed rating action is as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
Bank loans	-	-	-	INR500	IND BBB-/Stable	Assigned

KEY RATING DRIVERS

Experienced Management: Sindhuja Microcredit's management has over a decade-long microfinance experience with both the promoter directors having worked previously with Utkarsh Microfinance, steering it through demonetisation and being an integral part of the team during its conversion to a small finance bank. Ind-Ra factors into the rating this management expertise and expects Sindhuja Microcredit to continue to benefit from it in the medium term.

Adequate Capitalisation and Reasonable Leverage: At end-9MFY20, Sindhuja Microcredit's Tier-1 capital improved to 25.88% from 12.72% at FYE19, mainly on a fresh equity infusion of INR190 million by the private equity investor Carpediem Capital and the conversion of INR60 million compulsory convertible debentures (CCDs) issued to Carpediem Capital into equity in FY19. The company is expecting an equity infusion of INR650 million, of which the first tranche of INR300 million is likely to be received from a new prospective investor by FYE20 and the balance INR350 million will be infused by the existing and new investor after acquiring the Reserve Bank of India's approval in 1HFY21. Ind-Ra factors in at least a part of the aforementioned infusion to materialise by 1QFY21.

At end-9MFY20, the company's assets under management (AUM; including business correspondent) grew over 2x to INR1,293.2 million from INR613.9 million at FYE19. As part of its near-term strategy, Sindhuja Microcredit plans to grow its AUM to INR5,000 million by FYE21 with owned portfolio accounting for around 75%. Most of this growth would consume equity (internal accruals are likely to remain marginal between 5% and 10%) and hence, the plans to

raise further equity are important. The leverage (debt/equity) at end-9MFY20 was 2.4x. However, Ind-Ra expects it to be under 5.0x in the medium term, supported by the company's demonstrated ability to raise both equity and debt, to achieve the targeted AUM. Ind-Ra expects Sindhuja Microcredit to maintain higher capital buffers and lower leverage levels, given the geographical concentration risk, which is expected to exist at least over the medium term.

Comfortable Asset Quality, though Book is Unseasoned: Ind-Ra opines the company's asset quality is superior to its peers' with gross non-performing assets (90 days past due) at 0.04% at end-9MFY20. However, the loan book is yet to be seasoned as FY20 is its second year of operations. According to the industry track record, the gross non-performing assets (NPAs) may settle at higher levels once Sindhuja Microcredit achieves scale and its portfolio seasons. Ind-Ra also expects the company to continue to diversify its geographical and sectoral presence so as to reduce the adverse impact of sectoral events on its asset quality. However, the microfinance sector continues to face systemic and idiosyncratic risks, given the vulnerable socio-economic profiles of its borrowers.

Liquidity Indicator – Adequate: At end-December 2019, the company maintained a cumulative surplus of around 32% of its total assets in up to one year bucket. Also, based on Ind-Ra's stress test, the company has adequate liquidity buffers in up to one year bucket. The company also had INR495 million of unutilised bank lines at end-December 2019. As part of its asset liability management (ALM) gap, Sindhuja Microcredit had INR166.2 million of cash on its balance sheet (13.43% of total average assets; of which encumbered cash is around 96%) at end-December 2019. Considering the unsecured nature of lending and high geographic concentration risk, the agency views the company maintaining adequate liquidity buffers to be crucial.

Short Track Record of Operations; Evolving Corporate Governance Structure: Sindhuja Microcredit commenced its operations on 30 April 2018. While its AUM grew to INR1,293.2 million at end-December 2019, the company is yet to establish a proven track record. Considering the current scale of operations, the company has adequate systems and processes in place. However, the same would need to be enhanced in terms of corporate governance standards with the formation of additional board committees and the appointment of additional independent members on the board; the company has informed Ind-Ra that the same would be achieved before FY21.

High Geographic Concentration: Sindhuja Microcredit's book remains concentrated towards Bihar, with 57.4% of its AUM at end-December 2019, followed by Jharkhand (22.7%).

The company plans to diversify its portfolio with expansion in some of the existing states and exploration of new geographies (Punjab and Haryana) in FY21. Ind-Ra is of the view that contiguous expansion is better; non-contiguous expansion may present operational and control-related challenges that could impact the asset quality.

Funding Source Concentration: Sindhuja Microcredit's funding profile remains almost fully concentrated with the majority of its loans being sourced from non-financial banking companies (NBFCs) at end-3QFY20. This has led to high cost of funds, contributing to modest profitability levels.

While the company is exposed to funding risk, it has been able to renew or raise its majority funding lines on a continual basis and source funding from existing as well as new NBFCs. The company was able to secure INR340 million funding lines in December 2019-January 2020.

RATING SENSITIVITIES

Positive: A positive rating action could result from the company's ability to raise significant capital (second tranche of proposed capital infusion), expand and diversify the franchise, scale-up operations while maintaining stable asset quality levels, modest funding diversification and adequate short-term liquidity.

Negative: Deterioration in the profitability and capital impairment arising from deterioration in asset quality, an inability to secure planned equity infusions or adequate funding and refinance from financial institutions, an increase in the leverage levels above 5.0x and the inability to maintain adequate capital buffers could result in a negative rating action.

COMPANY PROFILE

Sindhujha Microcredit was incorporated under the provisions of the Companies Act and has its registered office at Noida, Uttar Pradesh, India. The company is registered as an NBFC-micro finance institution with the Reserve Bank of India since 11 September 2018. It primarily provides micro finance services to women in the rural areas of India who are enrolled as members and organised as joint liability groups.

FINANCIAL SUMMARY

Particulars	April 2019-January 2020 (Provisional)	FY19
Total assets (INR million)	1,337.6	592.1
Total equity (INR million)	345.9	77.7
Net income (INR million)	27.2	-27.0
Return on average assets (%)	3.4	-8.0
Return on average equity (%)	15.2	-33.9
Equity/Asset (%)	25.9	13.1
Source: Sindhujha Microcredit, Ind-Ra		

COMPLEXITY LEVEL OF INSTRUMENTS

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Applicable Criteria

Financial Institutions Rating Criteria
Non-Bank Finance Companies Criteria

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