India Ratings Downgrades Ashv Finance’s NCDs to ‘IND BBB-’/Negative and CP to ‘IND A3’

Sep 30, 2024 | Non Banking Financial Company (NBFC)

India Ratings and Research (Ind-Ra) has downgraded Ashv Finance Limited’s (AFL) debt instruments as follows:

Details of Instruments

Instrument Type	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (million)	Rating Assigned along with Outlook/Watch	Rating Action
Principal protected market-linked debentures (PP-MLDs) *	-	-	-	-	INR200	IND PP-MLD BBB-/Negative	Downgraded
Non-convertible debentures (NCDs)*	-	-	-	-	INR262.5 (reduced from INR 700)	IND BBB-/Negative	Downgraded
Commercial paper (CP)^	-	-	-	-	INR500	IND A3	Downgraded
Bank loans	-	-	-	-	INR500	IND BBB-/Negative	Downgraded

*Details in Annexure
^ unutilised

Analytical Approach

Ind-Ra continues to take a standalone view of AFL to arrive at the ratings.

Detailed Rationale of the Rating Action

The downgrade and the Negative Outlook reflect AFL’s overall deteriorating financial metrics as visible in its weakened operating performance over FY24, challenges on asset quality and stretched funding condition. The culmination of these had resulted in a loss of INR1,101 million in FY24 on the back of the shrinking asset under management (AUM) and accelerated provisioning due to a write-off of assets worth INR1,138 million during the year. While the collection seems to have improved in 1QFY25 to around 91%, from the low of 87% seen in February 2024, it remained lower than AFL’s FY23 average of around 94%. There has also been high attrition at the senior management level, although the positions were filled in 1QFY25.

AFL had raised INR913 million in FY24 but all of it was consumed by its losses. Additionally, the capital raise was delayed and was lower than that expected by AFL earlier (INR1,400 million). AFL’s business momentum continues to struggle with its shrinking capital base. Although the tangible leverage was at 2.9x in 1QFY25, the headroom to achieve a disbursement run rate like in FY23 is limited, in the absence of a further capital raise; hence, it becomes pertinent for AFL to bring in a significant amount of fresh capital to get back on the growth trajectory.

List of Key Rating Drivers

Strengths

- Capital buffer adequate for a curtailed level of operation

- Liquidity adequate for short term

Weaknesses

- Funding constraints
- Profitability remains under pressure
- Elevated credit cost compressing asset quality

Detailed Description of Key Rating Drivers

Capital Buffer Adequate for a Curtailed Level of Operation: AFL raised INR913 million in FY24 as part of its INR1,400 million capital raise programme; however, deterioration in financial and operating performance deterred investors from committing the entire planned capital. Meanwhile, AFL's promoter group - Aavishkaar Group - has approved a capital infusion of USD1.25 million into AFL by end-3QFY25, which should help the company accelerate its disbursement over near term. However, to accelerate growth back to its run rate seen in FY23, the company will need further capital. The management is cognizant of the same and is in process to bring in fresh equity of another INR1,500 million by the next six-to-nine months. This equity will be over and above the capital commitment made last year, which is yet to be realise. The envisage capital infusion will provide a headroom to accelerate disbursement and fall back on growth trajectory and can be utilised to absorb asset-side shocks.

At end-1QFY25, AFL's Tier-1 capital stood at 26.9% (FY24: 26.7%; FY23: 19.9%; FY22: 27.7%), the tangible net worth was INR1,599 million (INR 1661 million; INR1,916 million; INR2,229 million) and leverage (debt/tangible net worth) was 2.9x (3.3; 3.7x; 2.7x). The management plans to operate below a threshold leverage of 4.0x on a steady-state basis. AFL has also utilised direct assignment in the past to manage its capitalisation and profitability; however, in FY24, thrust was on co-lending partnerships to grow its off book. Ind-Ra expects it to continue to utilise the same over the medium term and continue to source business by way of off-book financing.

Liquidity Adequate for Short Term: As per the latest asset-liability statement, AFL had a cumulative surplus as a percentage of total assets of 2.8% in the less than one-year bucket at end-June 2024. The management expects the surplus in the up to one-year bucket to be maintained on an ongoing basis and AFL's plans to maintain its on-balance sheet liquidity to meet repayments for the next two months even as the business scale continues to expand. At end-June 2024, AFL had debt obligations of INR461.7 million for the subsequent two months, as against the unencumbered cash and liquid investments of INR555 million, which, along with advances inflow provide adequate liquidity cover. Additionally, at end-1QFY25, AFL had an unutilised line of INR10 million in the form of cash credit and working capital loan, which, in the agency's view may not be adequate to meet the asset liability management (ALM) gaps if challenges on collection front resurface, making it a key monitorable.

Funding Constraints: Owing to the multiple uncertainties, AFL is facing funding constraint as reflected by only one fresh term loan sanction of INR50 million during 1QFY25. The funding mix has weakened with the share of cheaper term loans from banks declining to 21.0% as of 1QFY25 (1HFY24: 23%; FY23: 22.3%; FY22: 13%) and the share of loans from non-bank financial companies increasing to 39% (31%; 36%; 36%); the share of NCDs reduced to 30% of the total borrowing mix (37%; 31%, 29%). Despite challenges on the operating front, AFL's average cost of borrowing largely remained stable at around 12% (excluding process, legal and other charges), though incremental cost was higher at 13% in FY24. That said, the borrowing reduced to INR4,693 million in 1QFY25 (INR5,529 million; INR7,567 million; INR6,219 million).

Profitability Remains Under Pressure: AFL incurred losses of INR1,101 million in FY24 due to accelerated provisioning for write-offs amounting to INR1,138 million. The AUM declined to INR7,918 million in FY24 (FY23: INR10,700 million), primarily because of delays in equity infusion which slowed down disbursement growth, resulting in a negative yoy growth rate of 57.5%. The losses narrowed to INR53 million in 1QFY25, despite a management overlay provision of INR100 million; without this provision, the company would have reported a positive profit after tax (PAT). However, AFL's profitability continues to be impacted by the higher opex, alongside its declining net interest income and a shrinking asset base. The key opex metrics, such as opex to income and opex to AUM, deteriorated to 78.9% and 8.5%, respectively, in 1QFY25 (FY24: 95.4% and 7.6%; FY23: 60.3% and 8.1%). Furthermore, the disbursement run rate in 1QFY25 remained subdued at INR306.2 million per month (FY24: INR303.9 million; FY23: INR715.3 million). Consequently, AUM growth further declined to INR7,256 million.

To expand its portfolio in an asset-light manner, AFL plans to grow its off-book segment, particularly the co-lending segment, where it has three partnerships. The agency believes off-book growth, in addition to being less strenuous on capital buffers, will provide a steady source of income for AFL. Additionally, as a risk-mitigating strategy, AFL has outlined a plan to focus on secured assets, aiming to increase their share to around 35% of the total AUM over the medium term. This move is likely to lower credit costs and smoothen the credit cost curve.

Elevated Credit Cost Compressing Asset Quality: During FY24, AFL's asset quality metrics saw sharp deterioration with its gross non-performing assets (GNPA) of 10.9% at end-9MFY24. However, the company took a write-off of INR605.4 million in 4QFY24, which helped it to end FY24 with GNPA and NNPA of 4.4% and 2.0% (FY23: 5.32% and 2.58%; FY22: 4.55% and 2.0%). The asset quality improved further in 1QFY25 as the GNPA/NNPA stood at 3%/1.2%; the improvement was on account the sale of accounts worth INR1,470 million to ARC. Moreover, with the management's overlay provision of INR100 million, the stage 3 provision increased to 69% and the provision on gross advances stood at 6.1%. That said, the subdued profitability has impacted the pre-provision operating profit to credit cost (PPOP/CC) buffer which shrunk to 0.48x in 1QFY25 (FY24: 0.03x; FY23: 1.03x; FY22: 1.13x). The credit cost continues to be high, partially exaggerated by the shrinking asset base (1QFY25: 6.5%; FY24: 16.6%; FY23: 6.2%).

Moreover, the collection efficiency has improve to around 91% in 1QFY25 from the low of 87.5% seen in February 2024 but still below the average of around 94% in FY23. AFL has recalibrated its collection strategy and has doubled the size of its collection team. It also had a dedicated team for recovery in the write-off account. Considering the borrower profile in business loans, Ind-Ra opines focus and thrust on collections and initial assessment of the borrower's credit profile remain paramount for controlling credit risk in the medium-to-long term.

Liquidity

Adequate: As per the latest asset-liability statement, AFL had a cumulative surplus as a percentage of total assets of 2.8% in the less than one-year bucket at end-June 2024. The management expects the surplus in the up to one-year bucket to be maintained on an ongoing basis and AFL's plans to maintain its on-balance sheet liquidity to meet repayments for the next two months even as the business scale continues to expand. At end-June 2024, AFL had debt obligations of INR461.7 million for the subsequent two months, as against the unencumbered cash and liquid investments of INR555 million, which, along with advances inflow provide adequate liquidity cover. Additionally, at end-1QFY25, AFL had an unutilised line of INR10 million in the form of cash credit and working capital loan, which, in the agency's view may not be adequate to meet the ALM gaps if challenges on collection front resurface, making it a key monitorable.

Rating Sensitivities

Positive: A sustainable recovery both in terms of operational as well financing condition along with significant equity infusion is required to re-instore profitability; and expand franchise, along with an improvement in the asset quality. This, along with a continued improvement in the diversification of the funding profile and maintenance of adequate liquidity could lead to a positive rating action.

Negative: A further weakening of the operating performance, funding challenges, and delays in the planned raising of equity capital beyond the timelines expected by Ind-Ra, a dilution in the liquidity buffers below two months on an ongoing basis, and sustained asset quality or operating buffers and the leverage (debt/tangible net worth) increasing above 4.0x on a sustained basis, will result in a negative rating action.

ESG Issues

ESG Factors Minimally Relevant to Rating: Unless otherwise disclosed in this section, the ESG issues are credit neutral or have only a minimal credit impact on AFL, due to either their nature or the way in which they are being managed by the entity. For more information on Ind-Ra's ESG Relevance Disclosures, please click here. For answers to frequently asked questions regarding ESG Relevance Disclosures and their impact on ratings, please click here.

About the Company

AFL is a non-bank financial company registered with the Reserve Bank of India. It started operations in 2012 as a venture debt financer and provides small ticket size loans to the micro, small and medium-sized enterprises.

Key Financial Indicators

Particulars	FY24	FY23
Total assets (INR million)	9,116	11,450
Total tangible equity (INR million)	1,661	1,966
Net income (INR million)	-1,101	60.7
Return on average assets (%)	-10.7	0.59
Tier-I capital adequacy ratio (%)	26.7	19.9

Tangible equity/assets (%)	18.2	16.7
Source: AFL, Ind-Ra		

Status of Non-Cooperation with previous rating agency

Not applicable

Rating History

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook				
	Rating Type	Rated Limits (million)	Rating	19 Jan 2024	29 May 2023	24 June 2022	25 June 2021	18 Ju
Bank loans	Long-term	INR500	IND BBB-/Negative	IND BBB/Negative	IND BBB/Positive	IND BBB/Positive	IND BBB/Stable	IND B
Principal protected market-linked debenture	Long-term	INR200	IND PP-MLD BBB-/Negative	IND PP-MLD BBB/Negative	IND PP-MLD BBB/Positive	IND PP-MLD BBBemr/Positive	IND PP-MLD BBBemr/Stable	IND PP- emı
Commercial Paper	Short-term	INR500	IND A3	IND A2	IND A2+	-	-	
Non-convertible debenture	Long-term	INR262.5	IND BBB-/Negative	IND BBB/Negative	IND BBB/Positive	-	-	

Bank wise Facilities Details

The details are as reported by the issuer as on (30 Sep 2024)

#	Bank Name	Instrument Description	Rated Amount (INR million)	Rating
1	HDFC Bank Limited	Term loan	100	IND BBB-/Negative
2	Utkarsh Small Finance Bank Limited	Term Loan	160	IND BBB-/Negative
3	NA	Term Loan	240	IND BBB-/Negative

Complexity Level of the Instruments

Instrument Type	Complexity Indicator
Bank loan	Low
Commercial paper	Low
Non-convertible debenture	Low
Principal protected market-linked debenture (PP-MLD)	High

For details on the complexity level of the instruments, please visit https://www.indiaratings.co.in/complexity- indicators.

Annexure

NCDs

ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Outlook
INE411R07202	24 May 2023	12.25	7 May 2026	INR200	WD (Paid in full)
INE411R07210	12 July 2023	12.25	31 December 2024	INR112.5	IND BBB-/Negative
INE411R07228	12 July 2023	12.25	30 June 2026	INR150	IND BBB-/Negative
			Total utilised	**INR262.5**	
			Total unutilised	**-**	
			Total	**INR262.5**	

Source: NSDL; AFL

PP-MLDs

ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Outlook
INE411R07087	29 June 2021	Variable - Index Linked	30 September 2024	INR200	IND PP-MLD BBB-/Negative

Source: NSDL; AFL

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APPLICABLE CRITERIA AND POLICIES

Non-Bank Finance Companies Criteria

Evaluating Corporate Governance

Financial Institutions Rating Criteria

The Rating Process

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