CRISIL Ratings

Rating Rationale

June 23, 2022 | Mumbai

Fincare Small Finance Bank Limited

Rating reaffirmed at 'CRISIL A1+ '

Rating Action

Rs.250 Crore Certificate of Deposits	**CRISIL A1+ (Reaffirmed)**

1 crore = 10 million
Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale
CRISIL Ratings has reaffirmed its **'CRISIL A1+'** rating on the certificate of deposits programme of Fincare Small Finance Bank Ltd (Fincare SFB).

The rating continues to reflect the bank's adequate capital position, experienced board and leadership team, sound risk management systems and practices bolstered by increasing digitisation, and rising share of retail deposits. These strengths are partially offset by moderation in asset quality, modest credit risk profile of the borrowers and limited seasoning in the non-microfinance portfolio.

Over the years, Fincare SFB has ramped up its deposit franchise to reach a deposit base of Rs 6,456 crore as on March 31, 2022, up 21.4% on-year and constituting 69% of external borrowings. Commensurate to this growth, the share of retail deposits (current account and savings account [CASA] and retail term deposits) was at 82.2% as on March 31, 2022, compared with 87.6% a year earlier. The share of CASA deposits in the overall deposit base saw robust growth in fiscal 2022 and stood at 36.3% as on March 31, 2022, compared with 23.7% a year earlier. In terms of external liabilities, CASA stood at 18.8%, which is comparable with most other small finance banks (SFBs) but lower than banks.

Assets under management (AUM) grew 24% in fiscal 2022 to Rs 7,541 crore, driven by 19% growth in microfinance loans, which have the largest share (about 76%) in the AUM followed by LAP (12%) and loans against gold (6%). Despite gradual expansion into non-microfinance products in recent years, their share in the AUM remains small and ability to profitably scale up this portfolio will remain a rating sensitivity factor.

Gross non-performing assets (NPAs) surged to 6.4% as on March 31, 2021, after having remained below 1% pre-Covid. Furthermore, collection efficiency declined to 72% in May 2021 from 92% in March 2021 because of the second Covid wave. Post the second quarter of fiscal 2022, with improvement in cash flows of borrowers, collection efficiency improved and stood at 97% in March 2022. Gross NPAs were at 7.8% and net NPAs at 3.6% as on March 31, 2022. Additionally, the bank has a restructured portfolio of Rs 370 crore (4.9% of the AUM as on March 31, 2022), billing for which is expected to start from July 2022. The ability to sustain collection and eventually reach the pre-pandemic level of over 99% on a steady-state basis remains a key monitorable.

Higher provisioning in fiscal 2022 led to net profit of Rs 8.9 crore translating to return on assets of 0.1% (Rs 113 crore and 1.5%, respectively, in the previous fiscal). Pre-provisioning profit was Rs 431 crore in fiscal 2022 as against Rs 365 crore in fiscal 2021.

Analytical Approach
CRISIL Ratings has assessed the standalone credit risk profile of Fincare SFB.

Key Rating Drivers & Detailed Description
Strengths:
*** Adequate capital position, supported by a diverse investor base**
The bank is adequately capitalised despite volatility in asset quality owing to socio-political issues. In fiscal 2022, the bank raised Rs 169.7 crore through issuance of rights to shareholders. This, in addition to a stable cash accrual, resulted in networth of Rs 1,202 crore, and tier I capital adequacy ratio (CAR) of 19.5% and overall CAR of 22.3% as on March 31, 2022. On a steady state basis, the bank intends to maintain overall CAR of over 20%. Gearing was moderate at 7.8 times as on March 31, 2022.

CRISIL Ratings believes Fincare SFB enjoys strong flexibility to raise equity, whenever required, given its diverse group of investors with high pedigree, some of whom have been associated with the bank since 2010.

*** Experienced board and senior management team**
Fincare SFB transitioned from a promoter-driven entity to an entity managed by a team of experienced professionals almost a decade ago, and benefits substantially from the presence of experienced professionals from across the financial sector. The leadership team, including Mr Rajeev Yadav, Mr Keyur Doshi, Mr Soham Shukla and Mr Mahendar Chawla, has been stable for many years now. Other top executives, such as Mr Pankaj Gulati and Mr Kishore Mangalvedhe, have also been with the entity for over eight years.

The board comprises eminent persons from the financial and allied sectors. They have rich domain expertise and extensive experience in the fields of microfinance and self-help groups, audit and accounts, banking, taxation, technology and strategy.

*** Sound risk management systems and practices, bolstered by digital initiatives undertaken by the bank**
Over its operational history, previously as an MFI and now as a bank, Fincare SFB has adjusted its systems and processes to match its scale and nature of business while keeping technology at the forefront. This has helped scale up the operationally intensive microfinance business and remains an anchor for the bank's retail portfolio. The bank has adequate audit and internal control mechanisms, which include a separate operational risk function. Since the amalgamation of Disha Microfin and Future Financial Services Ltd (FFSL), the board and senior management team have taken initiatives to enhance digitisation of operations. As part of its long-term strategy, the bank has launched '101 first account', a zero balance digital savings account with instant account opening feature. 'Kaizala', a secure employee communication and productivity application, has digitised field processes such as password resets, audits, UPI collection and branch control, providing greater visibility on the activities of the field staff. The bank has implemented DLite and M-Care process flows, which involve tablet-based loan application followed by real-time credit bureau check and instant credit decision.

*** Rising deposit base, driven by increasing share of retail deposits**
Fincare SFB had a deposit base of Rs 6,456 crore as on March 31, 2022, accounting for 69% of overall external borrowings. The share of retail deposits in the overall liability franchise has grown in tandem, anchored by the bank's ability to leverage its base of over 2.5 million retail borrowers on the asset side, of which majority are now deposit customers as well. The share of retail deposits (CASA and retail term deposits) stood at 82.2% as on March 31, 2022, as against 87.6% a year earlier. The traction in retail deposits imparts granularity to liabilities.

The CASA share rose to 36.3% of total deposits and 24.9% of total borrowings as on March 31, 2022, from 23.7% and 18.8%, respectively, a year earlier. This metric has improved gradually since Fincare SFB transitioned into a bank with incremental funds being in the form of low-cost deposits and refinance from financial institutions. Cost of funds declined from above 10% in fiscal 2017 to 6.8% in 2022 and is expected to reduce further. Ability to sustain growth in retail deposits in the overall deposit and liability base remains a key monitorable.

Weakness:
*** Modest credit risk profiles of borrowers**
A significant 76% of the portfolio comprises microfinance loans to clients with below-average credit risk profiles and lack of access to formal credit. These customers belong to the semi-skilled/self-employed category and their income may be volatile and dependent on the local economy. The slowdown in economic activity in the wake of the nationwide lockdown imposed in March 2020 to control the spread of Covid-19 affected the cash flows of such borrowers, thereby restricting their repayment capability. Moreover, this segment of borrowers remains exposed to idiosyncratic risks on account of socio-political factors. As economic growth is picking up, ability of the bank to reinstate repayment discipline among customers will be a key monitorable.

*** Moderation in asset quality**
The bank's asset quality has remained volatile since Covid-19 broke out in March 2020. As of March 2021, gross NPAs and net NPAs were 6.4% and 2.8%, respectively, against 0.8% and 0.4%, respectively, in March 2020. This was aggravated by the second wave of the pandemic, with gross NPAs and net NPAs rising to 7.8% and 3.6%, respectively, in fiscal 2022. Additionally, provisioning coverage ratio was 44% in fiscal 2022 and restructured portfolio stood at Rs 370 crore (4.9% of the AUM as on March 31, 2022). Billing for the restructured portfolio is expected to start from July 2022. While asset quality started improving in the third quarter of fiscal 2022, ability to expedite improvement to revive profitability remains a key rating sensitivity factor. As the bank's target market largely comprises customers with below-average credit risk profiles, ability to reinstate credit discipline among borrowers is critical.

*** Limited seasoning of the non-microfinance portfolio**
Fincare SFB has a limited track record in the non-microfinance segment, which accounts for 24% of AUM, with vintage of just over three years in affordable housing loans, loans against property, loans against gold and institutional finance. Other products such as two-wheeler loans were introduced only in fiscal 2019. Loans against property and gold loans form the bulk of the non-microfinance portfolio, and stood at 12% and 6% of the AUM, respectively, as of March 2022. As the bank intends to increase share of the non-microfinance segments, ability to maintain sound asset quality while managing growth and profitability across economic cycles will be a key monitorable.

Liquidity : Strong

The bank had excess statutory liquidity requirement of Rs 1,050 crore and liquidity coverage ratio (LCR) of 206% as on March 31, 2022. Based on its structural liquidity statement dated March 31, 2022, there were no material negative gaps in buckets for up to one year. Liquidity is supported by access to refinance limits from financial institutions. As a scheduled commercial bank, Fincare SFB has access to liquidity adjustment facility, marginal standing facility and interbank markets in addition to certificate of deposits.

Rating Sensitivity factors

Downside factors

- Moderation in asset quality and growth in non-microfinance segment, weakening the profitability and capital position
- Inability to garner retail deposits, leading to Reduction in share in the total deposit base below 30% for a prolonged period

About the Bank

Incorporated in June 2017, Fincare SFB is an amalgamation of Disha Microfin and FFSL. Promoted by Mr Sameer Nanavati, Mr Keyur Doshi, Mr Vivek Kothari and Mr Soham Shukla, Disha Microfin was engaged in the microfinance business since February 2009 in Gujarat. FFSL, promoted by Mr Dasaratha Reddy and his family members, was in the same business since 2007 in Tamil Nadu, Karnataka and Andhra Pradesh. In October 2010, Indium IV (Mauritius) Holdings Ltd (Indium IV), advised by India Value Fund Managers (IVF), acquired stake in Disha Microfin and FFSL to integrate the entities. By mid-2012, the functional integration of Disha Microfin and FFSL was completed with both companies using the same software and technology, having common ground-level processes and similar organisation structure. The Fincare brand was established in 2014.

In September 2015, Disha Microfin received in-principle approval from the Reserve Bank of India (RBI) to set up a small finance bank with the objective of enhancing financial inclusion. The bank, Fincare SFB, commenced operations in July 2017. Through a gazette order dated April 13, 2019, the RBI directed the inclusion of the bank in the Second Schedule of Reserve Bank of India Act, 1934.

Key Financial Indicators

Particulars for the period-ended	Unit	Mar-2022	Mar-2021	Mar-2020	Mar-2019
Total assets	Rs Crore	10,906	7,966	7116	4172
Total income	Rs Crore	1,648	1,378	1216	675
PAT	Rs Crore	8.9	113	143	102
Overall CAR	%	22.3	29.6	29.3	23.6
Tier I CAR	%	19.5	24.9	23.5	21.5
Return on assets	%	0.1	1.5	2.5	3.2

Any other information: Not applicable

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Annexure - Details of Instrument(s)

ISIN	Nature of instrument	Date of allotment	Coupon rate (%)	Maturity date	Amount (Rs crore)	Complexity level	Rating assigned with outlook
NA	Certificate of deposits	NA	NA	7-365 days	250	Simple	CRISIL A1+

Annexure - Rating History for last 3 Years

	Current			2022 (History)		2021		2020		2019		Start of 2019
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Certificate of Deposits	ST	250.0	CRISIL A1+		--	29-06-21	CRISIL A1+	29-06-20	CRISIL A1+	13-06-19	CRISIL A1+	--

All amounts are in Rs.Cr.

Criteria Details

Links to related criteria
CRISILs Bank Loan Ratings - process, scale and default recognition

[Rating Criteria for Banks and Financial Institutions](#)
[CRISILs Criteria for rating short term debt](#)

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