Press Release

Village Financial Services Limited

June 12, 2020

Rating Reaffirmed and Assigned

Total Facilities Rated	**Rs. 520.00 Cr.**
Bank facilities Rated*	**Rs. 500.00 Cr.**
Long Term Rating	ACUITE A-/Stable
Total Facilities Rated*	**Rs. 20.00 Cr.**
Short Term Rating	ACUITE A2+

** Refer Annexure for details*

Erratum: In the original PR dated 27 November, 2019, the hyperlinks to the relevant rating criteria referred to an earlier version which have now been updated in this version, further the hyperlink to one of the relevant rating criteria was missing which has now been included in this version

Rating Rationale

Acuité has assigned the rating of '**ACUITE A-' (read as ACUITE A minus)** on the Rs. 50 Cr. bank facilities and reaffirmed the long-term rating of '**ACUITE A-' (read as ACUITE A minus)** on the Rs. 450.00 Cr. bank facilities of Village Financial Services Limited (VFSL). The outlook is **'Stable'**.

Acuité has also reaffirmed the short term rating of **'ACUITE A2+' (read as ACUITE A two plus)** to the Rs. 20.00 Cr. Commercial Paper Programme of VFSL.

About the company:

Village Financial Services Limited (VFSL) is a Kolkata based NBFC-MFI engaged in extending microfinance loans to woman borrowers organized in Joint Liability Groups. The company is promoted by Mr. Ajit Kumar Maity (Chairman) and his son, Dr. Kuldip Maity (Managing Director) who have over two decades of experience in the microfinance segment.

VFSL commenced its lending operations in 2006 and operates through a branch network of 240 branches as on June 30, 2019 across 11 states.

The promoters operate Village Welfare Society (VWS) and Village Micro Credit Services (VMCS- Section 25 Company) since 1982 and 2004 respectively. VMCS was engaged in lending activities, however, it has been discontinued since 2017 and all fresh disbursements are carried only in VFSL.

Analytical Approach

Acuité has adopted a standalone approach on VFSL's business and financial risk profile for arriving at the rating.

Key Rating Drivers

Strengths

- **Established track record in microfinance lending:**

  VFSL, a Kolkata based NBFC-MFI is promoted by Mr. Ajit Kumar Maity (Non-executive Chairman) and Dr. Kuldip Maity (Managing Director and CEO). Dr. Kuldip Maity commenced his career as an Assistant Secretary of Village Welfare Society which is engaged in welfare activities. He is an ex-Board member of Sa-Dhan and Founder Member in AMFI West Bengal and has received various awards for his work in the microfinance industry. The company's board is chaired by Mr. Ajit Maity, Dr. Kuldip Maity in capacity of Managing Director along with five independent Directors as on November 15, 2019. The Directors have experience of over three decades in the field of banking and finance.

VFSL commenced microfinance lending to woman borrowers organized in Joint Liability Groups since 2006. The company has strengthened its operational presence over the years by diversifying its geographical penetration. Microfinance loans are usually disbursed in clusters and are lent to marginal borrowers with limited ability to absorb income shocks. The company's branch network has increased to 240 branches as on June 30, 2019 from 159 branches as on March 31, 2017. The management has judiciously improved its geographical penetration resulting in a diverse borrower base spread across 11 states and 76 districts. As on June 30, 2019, West Bengal and Bihar contributed 71 percent and 12 percent of VFSL portfolio, respectively. The balance portfolio was distributed across Assam, Odisha, Tripura, Chhattisgarh, Madhya Pradesh and Uttarakhand among others.

The established track record of promoters in microfinance lending has supported VFSL's growth strategy. The company's Asset under Management (AUM) has grown to Rs. 1057 Cr. as on March 31, 2019 as against from Rs. 413 Cr. as on March 31, 2017. As on September 30, 2019, the company's AUM stood at 1025.7 Cr. of which the owned portfolio comprised Rs. 676 Cr. and off book comprised Rs. 349 Cr. The growth is driven by increased presence in existing geographies.

Besides business growth, the promoters have demonstrated their ability to raise equity funding from IDFC First Bank (holds 7 percent as on June 30, 2019). The promoters have also been able to raise debt funding from a diverse mix of 51 lenders including Public as well as Private sectorbanks.

Acuité believes that VFSL's business profile will continue to benefit from the established presence in microfinance lending backed by strong managerial support and their resource raising ability.

- **Healthy asset quality and earning profile:**

VFSL on the back of its established presence in the microfinance segment along with strong foothold in its key operating geographies, has demonstrated a track record of healthy asset quality. The company is engaged in unsecured lending to marginal borrower with limited ability to absorb income shocks. The company extends micro credit through Joint Liability Group model and extends loans for income generation purpose. The company generally follows a practice of collecting its dues on fortnightly basis.

The company reported Gross NPA of 0.8 percent as on September 30, 2019 as against 0.4 percent as on March 31, 2019 and 0.5 percent as on March 31, 2018. The company's collection efficiency has been impacted post June 30, 2019 due to natural calamities. The company has demonstrated average collection efficiency (opening Overdue + current month due) of ~96 percent in 6 months ended September 30, 2019. Of the overall AUM, the overdues stood at Rs. 5.4 Cr. as on September 30, 2019 as against Rs. 3.9 Cr. as on June 30, 2019. Based on the track record of lending and collections, the company has been able to grow off book exposures through business correspondent relationships and securitization deals. VFSL's ability to maintain healthy collection efficiency along with its prudent lending policies have supported the company's ability to maintain its asset quality at healthy levels.

The company's earning profile is supported by healthy profitability on an increasing scale of operations. Net Interest Margins (NIMs) improved to 9.8 percent in FY2019 as against 7.8 percent in FY2018, primarily on account of the equity funded growth in loan book during FY2019. The company's Return on Average Assets (ROAA) improved to 3.4 percent in FY2019 from 1.6 percent in FY2018. This is primarily on account of Rs. 6.9 Cr. of excess interest spread on securitization transaction. The company's annualized NIMs and ROAA for H12020 was 9.3 percent and 4.2 percent respectively. The company's operating expense to on book earning asset ratio has increased to 7.9 percent in H12020 from 6.9 percent in FY2019.

Acuité believes that VFSL's ability to maintain its collection efficiency at healthy levels and sustain its profitability metrics will be a key monitorable.

Weaknesses

- **Leveraged capital structure; challenges in raising fresh debt could impeded growth trajectory:**

VFSL is engaged in microfinance lending with loan tenure ranging from 12 to 24 months. The company is in expansion stage, wherein the management plans to grow its AUM by increasing its presence in the existing geographies. The company's AUM stood at Rs. 1025 Cr. as on September 30, 2019 as against Rs.

413 Cr. as on March 31, 2017.

The company's Capital Adequacy ratio stood at 21.1 percent as on September 30, 2019 (18.8 percent as on March 31, 2019). The Tier II capital is by way of subordinated debt from IDFC First Bank Limited. The company's gearing stood at 4.7 times as on September 30, 2019 as against 6.2 times as on March 31, 2019 (including sub debt as part of debt) as against 7.7 times as on March 31, 2018. The improvement in gearing is primarily on the back of healthy plough back of profits in H12020.

The debt comprises Term loans from Banks/FIs, and subordinated debt. Most of the term debt is for a tenure ranging from two to three years. The leveraged capital structure may impact future leveraging initiative of VFSL. Acuité observes that generally MFIs opt for shorter tenured borrowings which is consistent with their asset portfolio i.e. Microfinance loans upto 2 years. The premise behind this funding philosophy is that the company will be able to raise fresh short to medium term debt from time to time. Consequent to the recent NBFC crises banks and FIs have become more selective in lending to NBFCs. Hence, already leveraged NBFC/MFIs such as VFSL could face challenges in raising fresh debt to support their on book growth. VFSL may have to raise additional equity to support the on book growth as envisaged.

Acuité believes that VFSL's ability to raise adequate equity capital in a timely manner to support the business growth will be key rating sensitivity.

- **Susceptibility of operating performance to inherent nature of microfinance segment**

VFSL primarily extends unsecured loans to economically challenged borrowers who have limited ability to absorb income shocks. Since the microfinance sector operates in a segment dealing with the lower economic strata of the society, the regulatory environment is stringent. This renders the MFIs like VFSL to regulatory risks. Besides the regulatory risks, the inherent nature of the business renders the portfolios vulnerable to event risks such as natural calamities in the area of operations.

Acuitè believes that regulatory and event risks will continue to have a major bearing on the credit profile of players like VFSL.

Rating Sensitivities

Positive sensitivities:
- Gearing improving to below 3x

Negative sensitivities:
- Gearing above 5.5x
- ROAA falling below 3 percent
- Net NPA crossing 1 percent

Material Covenants: The lenders have stipulated covenants pertaining to asset quality and Capitalisation levels.

Liquidity Position: Adequate

VFSL's overall liquidity profile remains adequate, given that its loans comprise relatively shorter-tenure microfinance loans compared to the tenure of borrowed funds. The company has demonstrated its ability to augment its liquidity profile through measures such as securitization of its portfolio by way of PTC transactions. The company's near term liquidity position is well managed based on ALM Statement as on September 30, 2019, with positive mismatches in individual buckets for upto one year. However, the company's ability to continue to maintain the pace of disbursements will depend on its ability to raise long term resources in the form of equity, long tenure loans or by securitizing its loan assets. In the event of excessive securitization, the expected growth in on book portfolio could be impacted.

In a nutshell, Acuité believes that VFSL's ability to maintain the tradeoff between liquidity and Growth (disbursements) will be linked to fresh equity infusion in current year and also its ability raise long term debt and securitize its asset pools.

Outlook: Stable

Acuité believes that VFSL will maintain a 'Stable' outlook over the near to medium owing to its established track record and resource raising ability of the promoters. The outlook may be revised to 'Positive' in case of significant and sustainable growth in its AUM while maintaining profitability, asset quality and leverage indicators. Conversely, the outlook may be revised to 'Negative' in case of any deterioration in asset quality, profitability, lower than expected growth in on book portfolio or in case of challenges faced in raising fresh capital.

About the Rated Entity – Key Financials

Parameters	Unit	FY19 (Actual)	FY18 (Actual)	FY17 (Actual)
Total Assets	Rs. Cr.	966.7	736.8	458.4
Total Income*	Rs. Cr.	92.2	52.1	33.6
PAT	Rs. Cr.	29.2	9.4	5.9
Net Worth	Rs. Cr.	126.0	81.8	47.4
Return on Average Assets (RoAA)	(%)	3.4	1.6	1.5
Return on Average Net Worth(RoNW)	(%)	28.1	14.5	13.2
Total Debt/Tangible Net Worth (Gearing)	Times	6.2	7.7	8.5
Gross NPA	(%)	0.4	0.5	0.3
Net NPA	(%)	0	0	0

* *Total income equals to Net interest income plus other income*

Status of non-cooperation with previous CRA (if applicable)

CARE wide its Press release dated January 07, 2019 has classified VFSL as issuer not cooperating. The rating has been denoted as 'CARE BBB-; Stable; ISSUER NOT COOPERATING'.

Any other information

None

Applicable Criteria

- Rating of Non-Banking Financing Entities – https://www.acuite.in/view-rating-criteria-44.htm
- Default Recognition – https://www.acuite.in/view-rating-criteria-52.htm
- Financial Ratios And Adjustments – https://www.acuite.in/view-rating-criteria-53.htm
- Criteria for rating Commercial paper - https://www.acuite.in/view-rating-criteria-54.htm

Note on complexity levels of the rated instrument

https://www.acuite.in/criteria-complexity-levels.htm

Rating History (Upto last three years)

Date	Name of Instrument /Facilities	Term	Amount (Rs. Cr.)	Ratings/Outlook
August 08, 2019	Proposed Long term Bank facility	Long Term	500.00	ACUITE A-/Stable (Assigned)
	Commercial Paper Programme	Short Term	20.00	ACUITE A2+ (Assigned)

***Annexure – Details of instruments rated**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Term Loan	NA	NA	NA	50.00	ACUITE A-/Stable (Assigned)
Proposed Long term Bank facility	NA	NA	NA	450.00	ACUITE A-/Stable (Reaffirmed)

Commercial Paper Programme	NA	NA	NA	20.00	ACUITE A2+ (Reaffirmed)

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About Acuité Ratings & Research:
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