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India Ratings Assigns Virutcham Microfinance Limited's Bank Loans 'IND BB+'/Stable

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By Roshan Aryal

India Ratings and Research (Ind-Ra) has assigned Virutcham Microfinance Limited's (VML) 'IND BB+' 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	-	-	-	INR300	IND BB+/Stable	Assigned

KEY RATING DRIVERS

VML's rating reflects its small scale of operations and high geographic concentration. The company's loan book fell to INR500.4 million at end-9MFY21 (FY20: INR608.2 million; FY19: INR516.7 million) due to COVID-19 led lack of disbursements. The company loan book is skewed towards Tamil Nadu (accounted for 80% of its asset under management (AUM) at end-9MFY21), followed by Kerala (15%) and the rest by Puducherry (5%), exposing it to high geographical concentration risk. However, the management has informed the agency that it is looking to expand in neighbouring southern states. The agency believes that contiguous expansion is better, as non-contiguous expansion may present operational and control related challenges.

The rating, however, is supported by VML's diversified funding profile, as the company had equally sourced its loans from non-banking finance companies (NBFCs) as well as banks at end-9MFY21, demonstrating the company's funding flexibility. While the company's cost of funds was high at around 14.5% at end-9MFY21, the agency notes that the company is able to raise incremental funds at 8%-10%, which would contribute to a further rise in the profitability. The company has also been able to renew or raise its majority funding lines on a continual basis and source funding from existing as well as new lenders.

The rating is also supported by VML's adequate capitalisation level, as the entity received an equity capital of INR80 million from various investors over FY19-FY20. The same helped VML in maintaining a comfortable capital adequacy ratio of 23.8% at end-9MFY21 (FY20: 32.8%) and Tier-I capital at 20.9% (25.5%). Resultantly, the company's moderate leverage (debt/equity) stood at 2.6x at end-9MFY21(FY20: 3.06x, FY19: 4.62x; FY18: 4.27x). Its equity-to-assets ratio stood at 27% at end-9MFY21 (FY20: 24.1%) and equity-to-AUM was 32.4% (FY20: 26.4%). The agency believes the current capital level is adequate, given the funding situation and the company's plans to log over 100% growth rate for FY22 maintaining balance sheet leverage at 5x.

Liquidity Indicator – Adequate: At end-9MFY21, the company maintained a cumulative surplus of around 15% of its total assets even after stressing the inflows in up to one-year bucket. The company also had INR50 million of unutilised bank lines at January 2020. At end-9MFY21, VML had INR33.4 million of cash on balance sheet (5% of total average assets; all of which are unencumbered). Considering the company's unsecured nature of lending and high geographic concentration risk, the agency views the company's maintaining adequate liquidity buffers to be very crucial.

The rating also factors in VML's stable asset quality as gross non-performing assets stood at 0.3% at end-9MFY21 (FY20: 0.2%; FY19: 0.1%), which is similar to that of its peer entities with comparable portfolio size in the microfinance segment. The company's profitability was moderate with return on average assets at 2.76% at end-1HFY21 (FY20: 1.88%).. However, the agency believes a rise in the company's credit costs owing to delinquent loans could exert pressure on profitability.

RATING SENSITIVITIES

Positive: A positive rating action could result from the company's ability to raise significant capital, 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 (gross non-performing assets rising over 5%), an inability to secure planned equity infusions or adequate funding and refinance from financial institutions, the leverage exceeding 5x, and the inability to maintain adequate capital buffers could result in a negative rating action.

COMPANY PROFILE

VML was incorporated as a NBFC on 8 July 2008 and converted into NBFC-Microfinance Industry on 6 June 2014. VML started its microfinance operations in November 2008. The company is primarily engaged in providing 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 (INR million)	1HFY21	FY20
Total assets	628.1	667.5
Total equity	169.7	160.7
Net income	9.0	12.2
Return-on-average assets (%)	2.76	1.88
Return-on-average equity (%)	10.84	8.99
Equity/Asset (%)	27.0	24.1
Source: VML; Ind-Ra		

COMPLEXITY LEVEL OF INSTRUMENTS

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

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Applicable Criteria

Financial Institutions Rating Criteria
Non-Bank Finance Companies Criteria

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