Veritas Finance Private Limited

March 07, 2018

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Remarks
Proposed Non-convertible Debentures	100.00 (Rupees One hundred crore)	**CARE BBB-; Stable (Triple B Minus; Outlook: Stable)**	**Assigned**
Proposed Non-convertible Debentures	50.00 (Rupees Fifty crore)	**CARE BBB-; Stable (Triple B Minus; Outlook: Stable)**	**Reaffirmed**
Total	150.00 (Rupees One hundred and fifty crore only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the debt instrument of Veritas Finance Private Limited (VFPL) factor in experience of the promoter and senior management team in lending business, robust business growth, presence of well managed in-house appraisal, origination & collection team, adequate risk management & MIS systems and good asset quality. The ratings also take note of fresh equity infusion of Rs.105 crore in Q3FY18 and consequent improvement in capitalization levels.

The ratings are however constrained by limited seasoning of its portfolio, geographical concentration amidst the efforts taken for diversification, presence in the MSME segment which is relatively risky, moderately diversified resource profile and moderate profitability profile on account of growing nature of operations.

In light of high growth plans envisaged by the company in the medium term, ability of VFPL to maintain its asset quality & profitability while geographically diversifying its portfolio and effectively manage its growing scale of operations would be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strength

Experienced promoter and senior management: VFPL is promoted by Mr. D. Arulmany, who is MD and CEO of VFPL. Mr. D. Arulmany has overall experience of about 25 years most of which is in financial services industry and has held various positions in the companies under the Murugappa group and CEO of an affordable housing finance company. VFPL's board has five directors including three independent directors and one nominee director representing the Private Equity firm Sarva Capital LLC, who have infused equity capital in the company. Mr. D. Arulmany is assisted by experienced senior management team who were closely associated with him in earlier organizations and have significant experience in the lending business.

Well managed in-house processes along with good MIS system: VFPL is engaged in lending small business loans to catering to borrowers in MSME segment (completely secured by collateral), for which the ticket size is in the range of Rs.1-15 lakhs, as against other NBFCs who lend at a higher ticket size. VFPL's target segment includes MSME enterprises where the business is on cash and carry basis especially in the rural and semi urban areas with tenure upto 7 years, which however is characterized by marginal credit profile of the borrowers. The senior management team of the company has drafted credit policy based on its experience and knowledge of the target customer segment gathered in the past.

VFPL provides loans with LTV ratio of less than 50% of the tech value arrived by the company which gives them considerable cushion, in case of any delinquencies. With respect to the credit appraisal of the borrowers, upto 45% of the applicant's income is considered as EMI to the company's loans.

VFPL has is its in-house team covering all the facets starting from business sourcing, recovery and collection, technical and legal. The selection of customers runs through several levels of checks including sales executive visiting business premises of the customer for income assessment, LTV assessment, KYC norms, etc. All the appraisals are done at the branch level and for final approval reports sent to head office. The collections are done through ECS/ACH and the sales team holds the

[1] *Complete definition of the ratings assigned are available at www.careratings.com and in other CARE publications*

responsibility to follow up with the customers to recover the loan in case of delays. VFPL uses third party vendor software for its MIS systems which has been used by many banks and leading NBFCs. This system provides solutions for the business starting from loan origination and up to NPA management. This system enables to automate the entire processes thereby improving the efficiency. With such strong appraisal and collection mechanism, VFPL has been able to grow their business, without any significant strain on the asset quality.

Improvement in the capitalization profile supported by fresh equity infusion: During November 2017, VFPL mobilized fresh equity of Rs. 105 crore which resulted in improvement in networth to Rs.164.4 crore as on January 31, 2018 (Prov.) from Rs.39.7 crore as on March 31, 2017. The gearing improved to 0.9 times as on January 31, 2018 from 1.8 times as on March 31, 2017. The total capital adequacy ratio as on January 31, 2018 was 54.73% and Tier-I CAR during the same period was 53.81%

Robust business growth: The company's loan portfolio grew from Rs.6.1 crore as on March 31, 2016 to Rs. 92.3 crore as on March 31, 2017 further to Rs. 280.5 crore as on January 31, 2018 which was supported by periodical infusion of fresh equity and borrowed funds. The company operates in 61 districts with 16 regional offices, 68 branches and 104 micro centers as on January 31, 2018. The ability of the company to manage growing scale of operations and operational efficiencies as it opens new branches/ enters new geographies to grow the portfolio remains critical for its growth prospects.

Good Asset quality however limited seasoning of portfolio: The company recognizes NPA on 90 days overdue basis as against the regulatory requirement of 180 days. The Gross NPA and Net NPA (90 dpd) of the company as on January 31, 2018 was 0.95% and 0.62% as against 0.97% and 0.71% as on March 31, 2017 (FY16: nil) respectively. The company continues to provide 1% as standard assets provision against the RBI requirement of 0.25%. VFPL commenced lending operations in April 2015 and has relatively limited track record and limited seasoning of the loan portfolio. As a result, its asset quality performance through different economic cycles and geographies is yet to be established. Moreover, with increased number of branches and growth in portfolio in the recent past, ability of the company to manage its asset quality would remain critical.

Industry Outlook and Prospect: Over the last few years, the NBFC sector has gained systemic importance with increase in share of NBFC total assets to bank total assets. The same has resulted in the Reserve Bank of India (RBI) taking various policy actions resulting in NBFCs attracting higher support and regulatory scrutiny. The RBI has revised the regulatory framework for NBFCs which broadly focuses on strengthening the structural profile of NBFC sector. Overall the revised regulations are positive for the NBFC sector making it structurally stronger, increase transparency and improve their ability to withstand asset quality shocks in the long run.

Due to subdued economic environment, last three years have been challenging period for the NBFCs with rising delinquencies resulting in higher provisioning thereby impacting profitability. However, comfortable capitalization levels and liquidity management continue to provide comfort to the credit profile of NBFCs in spite of impact on profitability. Also with the improvement in economic environment, asset quality pressures should ease.

Key Rating Weaknesses

Presence in the MSME segment which is relatively riskier: VFPL is primarily lending towards the business finance needs of the un-organised MSME segment in the rural and semi-urban areas which is characterized by marginal credit profile of the borrowers and are not serviced by the banking sector. Since this segment is highly susceptible to the impact of economic downturn and asset quality is a key monitorable. However, adequate collateral on the loans provided (secured by properties, most of them are Self-occupied residential) and the management team's good knowledge on this target customer segment provides comfort.

Geographical concentration of portfolio amidst efforts taken for diversification: The company started its operations in Tamil Nadu and during current financial year, the company expanded their business into newer states like Orissa, West Bengal and Karnataka. The proportion of Tamil Nadu in the portfolio declined from 100.00% as on March 31, 2016 to 78.90% as on January 31, 2018 and other states contributed the remaining (West Bengal: 13.65%, Karnataka: 5.97%, Puducherry:1.33% and Orissa:0.15%). VFPL plans to reduce the concentration of Tamil Nadu Portfolio further in the current financial year by expanding into newer geographies.

Moderate Resource profile: The company's source of funding was earlier skewed towards loans from Financial Institutions during the initial stage of operations. During FY17 and current financial year, the company has gained access into borrowings from banks which resulted in moderation in cost of funds. The proportion of Bank borrowings increased from nil as on March 31, 2016 to 5.20% as on March 31, 2017 and further to 36.29% as on January 31, 2018. Going forward, the ability of the company to diversify their resource profile by getting access towards market instruments and raise funds at competitive interest rates would remain critical for profitability of the company.

Moderate profitability characterized by high opex due to initial stage of operations: The company reported losses in FY16 & FY17 due to initial stage of operations and operating costs were in the range of 13-14% of their total assets during FY17. With increase in loan book and benefits of scale opex/avg. assets declined to 10.95% in 10MFY18 (refers to period from April 01 to January 31). NIM was around 14.43% in 10MFY18 as against 7.89% in FY17. The company reported profit of Rs.4.8 crore 10MFY18 due to improvement in scale of operations improvement in NIM.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
CARE's methodology for Non-Banking Financial Companies
Financial ratios – Financial sector

About the Company

Veritas Finance Private Limited (VFL) incorporated on April 30, 2015 is a non-deposit taking NBFC (loan company), registered with RBI. VFL is promoted by Mr. D. Arulmany. As at January 31, 2018, Promoter & related parties held 9.63% of the equity, Resident Individual investors held 14.26% of the stake, Employees & related parties held 7.42% and remaining 68.69% equity held by institutional investors, namely, CDC Group (26.93%), Sarva Capital LLC (advised by Lok Capital) (22.88%), GCP & affiliate (16.57%) and Caspian Impact Investment Adviser Private Limited (2.31%). VFL lends to entrepreneurs engaged in micro, small and medium enterprises (MSME) with limited access to formal financial services.
VFL currently operates in Tamil Nadu, Puducherry, West Bengal, Orissa & Karnataka out of 16 regional offices, 68 branch offices (including 4 branches exclusively for working capital vertical) and 104 Micro Centers. For mortgage-backed lending, there are typically 3-4 branches under each area office which also functions as a hub.
VFL offers three products based on the purpose such as Business expansion Loan (BEL), Working capital loan (WCL) and loan for Purchase of assets/inventory (Purchase) of which WCL is in pilot stage which is currently being tested in Chennai. VFPL had a loan portfolio of Rs.280.5 crore as on January 31, 2018 of which around 96.27% of the portfolio was constituted by mortgage backed loans (BEL & Purchase) and remaining 3.73% by WCL..

Brief Financials (Rs. crore)	FY16 (A)	FY17 (A)
Total operating income	0.7	12.7
PAT	-1.9	-2.9
Interest coverage (times)	41.2	112.6
Total Assets	NA	0.1
Net NPA (%)	-9.3	-3.7
ROTA (%)	0.0	0.7

A: Audited;

Status of non-cooperation with previous CRA: NA

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Analyst Contact:
Name: Mr Sudhakar P
Tel: 044-2849 7812
Mobile :94422 28580
Email: p.sudhakar@careratings.com

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In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Debentures-Non Convertible Debentures (Proposed)	-	-	-	50.00	CARE BBB-; Stable
Debentures-Non Convertible Debentures (Proposed)	-	-	-	100.00	CARE BBB-; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015
1.	Fund-based - LT-Term Loan	LT	100.00	CARE BBB-; Stable	1)CARE BBB-; Stable (06-Oct-17)	-	-	-
2.	Debentures-Non Convertible Debentures	LT	50.00	CARE BBB-; Stable	1)CARE BBB-; Stable (06-Oct-17)	-	-	-
3.	Debentures-Non Convertible Debentures	LT	100.00	CARE BBB-; Stable	-	-	-	-

CONTACT

Head Office Mumbai

Ms. Meenal Sikchi
Cell: + 91 98190 09839
E-mail: meenal.sikchi@careratings.com

Mr. Ankur Sachdeva
Cell: + 91 98196 98985
E-mail: ankur.sachdeva@careratings.com

Ms. Rashmi Narvankar
Cell: + 91 99675 70636
E-mail: rashmi.narvankar@careratings.com

Mr. Saikat Roy
Cell: + 91 98209 98779
E-mail: saikat.roy@careratings.com

CARE Ratings Limited

(Formerly known as Credit Analysis & Research Ltd.)

Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022
Tel: +91-22-6754 3456 | Fax: +91-22-6754 3457 | E-mail: care@careratings.com

AHMEDABAD
Mr. Deepak Prajapati
32, Titanium, Prahaladnagar Corporate Road,
Satellite, Ahmedabad - 380 015
Cell: +91-9099028864
Tel: +91-79-4026 5656
E-mail: deepak.prajapati@careratings.com

BENGALURU
Mr. V Pradeep Kumar
Unit No. 1101-1102, 11th Floor, Prestige Meridian II,
No. 30, M.G. Road, Bangalore - 560 001.
Cell: +91 98407 54521
Tel: +91-80-4115 0445, 4165 4529
Email: pradeep.kumar@careratings.com

CHANDIGARH
Mr. Anand Jha
SCF No. 54-55,
First Floor, Phase 11,
Sector 65, Mohali - 160062
Chandigarh
Cell: +91 85111-53511/99251-42264
Tel: +91- 0172-490-4000/01
Email: anand.jha@careratings.com

CHENNAI
Mr. V Pradeep Kumar
Unit No. O-509/C, Spencer Plaza, 5th Floor,
No. 769, Anna Salai, Chennai - 600 002.
Cell: +91 98407 54521
Tel: +91-44-2849 7812 / 0811
Email: pradeep.kumar@careratings.com

COIMBATORE
Mr. V Pradeep Kumar
T-3, 3rd Floor, Manchester Square
Puliakulam Road, Coimbatore - 641 037.
Tel: +91-422-4332399 / 4502399
Email: pradeep.kumar@careratings.com

HYDERABAD
Mr. Ramesh Bob
401, Ashoka Scintilla, 3-6-502, Himayat Nagar,
Hyderabad - 500 029.
Cell : + 91 90520 00521
Tel: +91-40-4010 2030
E-mail: ramesh.bob@careratings.com

JAIPUR
Mr. Nikhil Soni
304, Pashupati Akshat Heights, Plot No. D-91,
Madho Singh Road, Near Collectorate Circle,
Bani Park, Jaipur - 302 016.
Cell: +91 – 95490 33222
Tel: +91-141-402 0213 / 14
E-mail: nikhil.soni@careratings.com

KOLKATA
Ms. Priti Agarwal
3rd Floor, Prasad Chambers, (Shagun Mall Bldg.)
10A, Shakespeare Sarani, Kolkata - 700 071.
Cell: +91-98319 67110
Tel: +91-33- 4018 1600
E-mail: priti.agarwal@careratings.com

NEW DELHI
Ms. Swati Agrawal
13th Floor, E-1 Block, Videocon Tower,
Jhandewalan Extension, New Delhi - 110 055.
Cell: +91-98117 45677
Tel: +91-11-4533 3200
E-mail: swati.agrawal@careratings.com

PUNE
Mr.Pratim Banerjee
9th Floor, Pride Kumar Senate,
Plot No. 970, Bhamburda, Senapati Bapat Road,
Shivaji Nagar, Pune - 411 015.
Cell: +91-98361 07331
Tel: +91-20- 4000 9000
E-mail: pratim.banerjee@careratings.com

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