

Rating Rationale

October 19, 2022 | Mumbai

Muthoot Capital Services Limited

Ratings upgraded to 'CRISIL A+/CRISIL PPMLD A+ r/Stable/CRISIL A1+'

Rating Action

Total Bank Loan Facilities Rated	Rs.2500 Crore
Long Term Rating	CRISIL A+/Stable (Upgraded from 'CRISIL A/Stable')

Rs.100 Crore Long Term Principal Protected Market Linked Debentures	CRISIL PPMLD A+ r /Stable (Upgraded from 'CRISIL PPMLD A r /Stable')
Rs.100 Crore Long Term Principal Protected Market Linked Debentures	CRISIL PPMLD A+ r /Stable (Upgraded from 'CRISIL PPMLD A r /Stable')
Fixed Deposits	CRISIL A+/Stable (Upgraded from 'CRISIL A/Stable')
Rs.150 Crore Non Convertible Debentures	CRISIL A+/Stable (Upgraded from 'CRISIL A/Stable')
Rs.250 Crore Commercial Paper	CRISIL A1+ (Upgraded from 'CRISIL A1')

1 crore = 10 million

Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has upgraded its long-term rating on the bank facilities and debt instruments of Muthoot Capital Services Limited (MCSL; part of Muthoot Pappachan Group [MPG]) to '**CRISIL A+/CRISIL PPMLD A+ r/Stable/CRISIL A1+**' from '**CRISIL A/CRISIL PPMLD Ar/Stable/CRISIL A1**'.

The rating action is driven by upgrade in the rating of flagship-company of the Muthoot Pappachan Group (MPG) - Muthoot Fincorp Ltd (MFL; '**CRISIL AA-/CRISIL PP-MLD AA-r/CRISIL A/Stable**') from '**CRISIL A+/CRISIL PP-MLD A+r /CRISIL A-/Stable**'

The ratings on the bank loan facilities and debt instruments continue to reflect the company's adequate capital position and continued financial, operational, and managerial support from Muthoot Pappachan Group (MPG), considering the strong operational linkages of MCSL with the group. These strengths are partially offset by weak asset quality, moderation in earnings profile and the company's continued, although reducing, geographical concentration in the south Indian states.

MCSL's AUM improved to Rs 2,088 crore as of June 30, 2022 from Rs 2056 crore as of March 31, 2022. Post the slowdown induced by the wave-II of the pandemic, disbursements have picked up from August 2021 onwards with average monthly disbursements of around Rs 110 crore till August 2022. The management has indicated that the company intends to continue with current disbursement levels to achieve a target AUM of around Rs 2700 crore for fiscal 2023.

Collection efficiency (including overdues but excluding prepayments) have increased to over 100% collections on monthly basis, marked by higher overdue payments. Nevertheless, NPAs in terms of gross stage 3, continued to be high at 19.3% as of June 30, 2022 (18.9% as of March 31, 2022) against 11.7% as of March 2021. Furthermore, reported GNPA (gross non-performing asset) stood at 25.3% as of June 30, 2022 (25.9% as of March 31, 2022) due to the impact of the Reserve Bank of India (RBI) clarification released in November 2021 with respect to single day NPA recognition and upgradation of NPA accounts only after all dues are cleared. While the revised RBI clarification had allowed deferring implementation of upgradation norms till September 30, 2022, the company did not avail this relaxation and made additional provisions (including write-offs) of Rs 236 crore during Q4 of fiscal 2022, thereby reducing their NNPA to 5.7% as on March 31, 2022. The NNPA stood at 5.2% as of June 30, 2022.

With MCSL carrying a high provision buffer of Rs 472.7 crore (22.6% of the total portfolio as of June 30, 2022), write backs are also expected in the current fiscal in addition to the improving profitability on account of expected growth. Therefore, profitability of the company is also expected to improve steadily over the medium term.

Nevertheless, the ability of the company to manage collections from the harder delinquency buckets will be a key monitorable. CRISIL Ratings also notes that the company had restructured Rs 130 crore as on June 30, 2021 and the billing for the entire restructured book started in August 2021 itself (company did not undertake any restructuring during July 2021 - September 2021). The collection performance of the restructured book will also be a key monitorable.

The overall rating continues to factor in expectation of timely financial support from MPG in case of any exigency.

Analytical Approach

For arriving at the ratings, CRISIL Ratings has taken a standalone view of MCSL and has factored in support from MPG, whose flagship company is Muthoot Fincorp Ltd (MFL; 'CRISIL AA-/CRISIL PPMLD AA- r/CRISIL A/Stable/CRISIL A1+').

Key Rating Drivers & Detailed Description

Strengths:

- **Strong support from MPG**

MCSL is an integral part of MPG, whose flagship company is MFL. MCSL derives significant benefits from its linkages with the group. The group diversified its operations into vehicle financing through MCSL. The company has common promoters and promoter directors with the other MPG companies. Mr Thomas John Muthoot is the chairman of MCSL and other Muthoot Pappachan group companies. The company also has strong operational linkages with other group companies. It has the third largest portfolio in the group and has been leveraging on the branch network of the group to grow its book. Besides its own sales force, MCSL has access to the wide branch network and large clientele of MFL for origination of new loans and collection. MCSL, being an integral part of the group, will continue to receive operational and managerial support from MPG on an ongoing basis and timely financial support in case of any exigencies.

- **Adequate capitalisation**

Capitalisation had improved significantly in the past few years, with the company raising Rs 165 crore through qualified institutional placement in November 2017. The gearing had reduced to 3.2 times as on December 31, 2021 with disbursements being temporarily stopped on account of Covid-19, and hence the company's borrowing requirements were lower during fiscal 2021 and 2022. However, with the company reporting a net loss of Rs 154 crore during Q4 of fiscal 2022, the gearing increased to 4.2 times as on March 31, 2022. Nevertheless, with company returning to profitability and recording a muted growth, the gearing reduced to 3.8 times as of June 30, 2022. The company's philosophy is to maintain gearing at 5-6 times on a steady-state basis.

- **Extensive experience of the promoters and management in the vehicle finance sector**

Each of the three promoter directors have more than three decades of experience in the business of lending, beginning with gold loans, and have forayed into two-wheeler financing, microfinance, and housing finance over the years. The group ventured into two-wheeler financing in 1998 and since then has expanded into financing used cars, consumer durables and small-ticket business loans. The company also has a strong management with rich experience in similar businesses. The team has strengthened the systems and processes of the company, which will support the planned

scale-up. The group has established a strong reputation and brand in India, particularly in South India and has an appropriate assessment and underwriting methodology, which is being constantly refined.

Weaknesses:

- **Modest asset quality**

Amidst the challenging pandemic-induced economic environment during fiscal 2022, delinquencies had gone up and the company reported GNPA of 27.8% as on December 31, 2021 due to the impact of RBI clarification released in November 2021, with respect to single day NPA recognition and upgradation of NPA accounts only post all dues being cleared. While the revised RBI clarification had allowed deferring implementation of upgradation norms till September 30, 2022, the company did not avail this relaxation and made additional provisions (including writeoffs) of Rs 236 crore during Q4 of fiscal 2022, thereby reducing their NNPA to 5.7% as on March 31, 2022. As of June 30, 2022, the GNPA was at 25.3% (90+ dpd excluding the impact of IRACP norms was 19.3% as of June 30, 2022 as compared to 20.7% as of December 2021), while the NNPA stood at 5.2%. Nevertheless, the ability of the company to manage collections from the harder delinquency buckets will be a key monitorable. CRISIL Ratings also notes that the company had restructured Rs 130 crore as on June 30, 2021 and the billing for the entire restructured book started in August 2021 itself (company did not undertake any restructuring during July 2021 - September 2021). The collection performance of the restructured book will also be a key monitorable.

- **Moderation in earnings profile**

MCSL has been a steady contributor to the overall profitability of the group. Profitability was healthy until fiscal 2019 but moderated from fiscal 2020 onwards on account of higher provisions in relation to COVID 19 and toward other one-time provisions and increased cost of borrowing (during fiscal 2020), leading to decline in net interest margin (NIM) during the period. Consequently, return on managed assets (RoMA) moderated to 1.9% in fiscal 2021 (3.2% in fiscal 2019). For the first time in last 11 years, the company's profitability got significantly impacted and was constrained on account of lower disbursements impacting the growth and due to increase in delinquencies which led to rise in credit costs for the period. Credit costs rose to 13.9 % during fiscal 2022, as compared with 3.4% during fiscal 2021, on account of the Rs 324 crore provisioning (including write-offs of Rs 28.1 crore) done by the company during fiscal 2022. The operating expenses of the company also increased during the fiscal as the company employed dedicated collection teams to improve collections from across delinquency buckets. Consequently, it reported a net loss of Rs 171.9 crore for the fiscal 2022 while at a pre provisioning operating profit (PPoP) level it reported profit of Rs 152 crore compared to PPoP of Rs 146 crore in the previous fiscal. During the first quarter of fiscal 2023, the company reported a PAT of Rs 14.7 crore with a RoMA of 2.9% (annualised). The profitability of the company is expected to improve in the current fiscal with higher growth expectations for the current fiscal with the conditions returning to normalcy as well as expected write-backs from the high provisioning buffer carried by the company.

- **Geographically concentrated portfolio**

Although MCSL has sequentially reduced the concentration in its portfolio over the years, the company's operations continue to be largely concentrated in the southern states of the country. Concentration in the southern states reduced from 83% in March 2018 to 70% in March 2020 and further to 65% as on June 30, 2022. MCSL's operations are concentrated in Kerala, which accounted for 39.4% of hypothecation loans as on June 30, 2022, though it has declined from 42% as on March 31, 2019. However, MCSL has, over the past 4-5 years, entered the northern and eastern parts of India. The company plans to further reduce its dependence on the southern states over the medium term. CRISIL Ratings' believes the portfolio will continue to remain concentrated in the southern region, primarily because of MPG group's strong foothold in the south, and hence would be susceptible to geography-specific disruptions.

Liquidity: Adequate

MCSL's asset liability maturity profile is comfortable, with cumulative positive mismatches across all buckets up to 1 year as on June 30, 2022. As on June 30, 2022, MCSL had liquidity of around Rs 386.47 crore comprising Rs 171.8 crore of cash and equivalents and Rs 214.7 crore of unutilised bank lines (cash credit or working capital demand loan [CC/WCDL]). Its total debt obligation (including operating expense) was around Rs 276.6 crore for the next three months through September 2022. CC/WCDL of Rs 430 crore was due for renewal over the same period. The company has been able to rollover its CC/WCDL limit in the past and expects to be able to rollover the limit falling due during this period. Liquidity cover for three

INE296G07010	Non-Convertible Debentures	25-Jun-20	10.07%	21-Apr-23	50	Simple	CRISIL A+/Stable
NA	Non-Convertible Debentures*	NA	NA	NA	75	Simple	CRISIL A+/Stable
NA	Long term principal protected market linked debentures*	NA	NA	NA	100	Highly Complex	CRISIL PPMLD A+r/Stable
INE296G08018	Long term principal protected market linked debentures	06-Oct-22	G-Sec Linked	06-Oct-24	100	Highly Complex	CRISIL PPMLD A+r/Stable
NA	Commercial Paper	NA	NA	7-365 days	250	Simple	CRISIL A1+
NA	Fixed Deposits	NA	NA	NA	0	Simple	CRISIL A+/Stable
NA	Proposed Long Term Bank Loan Facility	NA	NA	NA	975	NA	CRISIL A+/Stable
NA	Cash Credit and Working Capital demand loan	NA	NA	NA	1065	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	23-Mar-24	35	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	26-Sep-22	100	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	18-May-24	175	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	18-Jun-23	75	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	24-Mar-24	25	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	28-Feb-23	25	NA	CRISIL A+/Stable
NA	Working Capital Term Loan	NA	NA	21-Jun-22	25	NA	CRISIL A+/Stable

*Yet to be issued

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
Fund Based Facilities	LT	2500.0	CRISIL A+/Stable	29-09-22	CRISIL A/Stable	30-12-21	CRISIL A/Stable	06-11-20	CRISIL A/Stable	05-04-19	CRISIL A/Stable	CRISIL A/Stable
			--	07-07-22	CRISIL A/Stable	18-03-21	CRISIL A/Stable	24-06-20	CRISIL A/Stable		--	CRISIL A/Stable
			--	22-06-22	CRISIL A/Stable		--	30-04-20	CRISIL A/Stable		--	--
			--	26-04-22	CRISIL A/Stable		--		--		--	--
			--	03-03-22	CRISIL A/Stable		--		--		--	--
Commercial Paper	ST	250.0	CRISIL A1+	29-09-22	CRISIL A1	30-12-21	CRISIL A1	06-11-20	CRISIL A1	05-04-19	CRISIL A1	CRISIL A1

			--	07-07-22	CRISIL A1	18-03-21	CRISIL A1	24-06-20	CRISIL A1		--	--
			--	22-06-22	CRISIL A1		--	30-04-20	CRISIL A1		--	--
			--	26-04-22	CRISIL A1		--		--		--	--
			--	03-03-22	CRISIL A1		--		--		--	--
Fixed Deposits	LT	0.0	CRISIL A+/Stable	29-09-22	CRISIL A/Stable	30-12-21	F A+/Stable	06-11-20	F A+/Stable	05-04-19	F A+/Stable	F A+/Stable
			--	07-07-22	CRISIL A/Stable	18-03-21	F A+/Stable	24-06-20	F A+/Stable		--	--
			--	22-06-22	CRISIL A/Stable		--	30-04-20	F A+/Stable		--	--
			--	26-04-22	F A+/Stable		--		--		--	--
			--	03-03-22	F A+/Stable		--		--		--	--
Non Convertible Debentures	LT	150.0	CRISIL A+/Stable	29-09-22	CRISIL A/Stable	30-12-21	CRISIL A/Stable	06-11-20	CRISIL A/Stable	05-04-19	CRISIL A/Stable	CRISIL A/Stable
			--	07-07-22	CRISIL A/Stable	18-03-21	CRISIL A/Stable	24-06-20	CRISIL A/Stable		--	--
			--	22-06-22	CRISIL A/Stable		--	30-04-20	CRISIL A/Stable		--	--
			--	26-04-22	CRISIL A/Stable		--		--		--	--
			--	03-03-22	CRISIL A/Stable		--		--		--	--
Long Term Principal Protected Market Linked Debentures	LT	200.0	CRISIL PPMLD A+ r /Stable	29-09-22	CRISIL PPMLD A r /Stable		--		--		--	--
			--	07-07-22	CRISIL PPMLD A r /Stable		--		--		--	--

All amounts are in Rs.Cr.

Annexure - Details of Bank Lenders & Facilities

Facility	Amount (Rs.Crore)	Name of Lender	Rating
Cash Credit & Working Capital Demand Loan	180	Union Bank of India	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	50	Central Bank Of India	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	10	City Union Bank Limited	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	30	DCB Bank Limited	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	60	Dhanlaxmi Bank Limited	CRISIL A+/Stable
Cash Credit & Working	15	The Federal Bank Limited	CRISIL A+/Stable

Capital Demand Loan			
Cash Credit & Working Capital Demand Loan	200	HDFC Bank Limited	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	35	IDBI Bank Limited	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	50	Indian Bank	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	50	Indian Overseas Bank	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	50	IndusInd Bank Limited	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	200	Punjab National Bank	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	100	State Bank of India	CRISIL A+/Stable
Cash Credit & Working Capital Demand Loan	35	Tamilnad Mercantile Bank Limited	CRISIL A+/Stable
Proposed Term Loan	975	Not Applicable	CRISIL A+/Stable
Working Capital Term Loan	35	Axis Bank Limited	CRISIL A+/Stable
Working Capital Term Loan	100	State Bank of India	CRISIL A+/Stable
Working Capital Term Loan	175	Canara Bank	CRISIL A+/Stable
Working Capital Term Loan	75	Bank of Baroda	CRISIL A+/Stable
Working Capital Term Loan	25	CSB Bank Limited	CRISIL A+/Stable
Working Capital Term Loan	25	Punjab National Bank	CRISIL A+/Stable
Working Capital Term Loan	25	Tata Capital Limited	CRISIL A+/Stable

This Annexure has been updated on 19-Oct-22 in line with the lender-wise facility details as on 02-Aug-21 received from the rated entity.

Criteria Details

Links to related criteria
CRISILs Bank Loan Ratings - process, scale and default recognition
Rating Criteria for Finance Companies
CRISILs criteria for rating fixed deposit programmes
Criteria for Notching up Stand Alone Ratings of Companies based on Parent Support

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