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India Ratings Affirms Navi Finserv's Debt Instruments at 'IND A'/Stable

Aug 18, 2023 | Non Banking Financial Company (NBFC)

India Ratings and Research (Ind-Ra) has taken the following rating actions on Navi Finserv Limited's (NFL) debt instruments:

Instrument	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
Commercial papers (CPs)	-	-	7 to 365 days	INR10,000	IND A1	Affirmed
Non-convertible debentures (NCDs)$,****	-	-	-	INR20,000	IND A/Stable	Affirmed
NCDs$	-	-	-	INR6,000	IND A/Stable	Affirmed
Principal protected market linked debentures (PP-MLDs)$,***	-	-	-	INR3,000	IND PP-MLD A/Stable	Affirmed
PP-MLDs$	-	-	-	INR2,000	WD	Withdrawn (paid in full)
NCDs*,$	-	-	-	INR1,950 (reduced from INR5,000)	IND A/Stable	Affirmed
NCDs**,#	-	-	-	INR31	IND A/Stable	Affirmed

* The limits are for NCDs and are fungible with MLDs, and the amount to be considered is INR1,950 million.
** The limits are for NCDs and are fungible with MLDs, and the amount to be considered is INR31 million.
*** The total PP-MLDs limit of INR3,000 million stands fungible between NCDs and PP-MLDs.
**** The total NCDs limit of INR20,000 million stands fungible between NCDs and PP-MLDs. INR5,000 million stands for public NCDs.
#Yet to be issued
$Details in Annexure

Analytical Approach: Ind-Ra continues to take a consolidated view of NFL (100% owned by Navi Technologies Limited; NTL; formerly known as Navi Technologies Private Limited), Chaitanya India Fin Credit Private Limited (CIFCPL; 'IND A'/Rating Watch with Developing Implications); 75% owned by NFL and 25% by NTL. Ind-Ra believes that the group would support CIFCPL till the completion of its acquisition by Svatantra Microfin Pvt Ltd), Navi General Insurance, broking and investment advisory units and NTL Asset Management Company, collectively referred to as the Navi group, to arrive at the ratings. NTL provides technological backbone and support to the subsidiaries.

Key Rating Drivers

Group's Capital Mostly Earmarked for Lending Services: NFL is a lending subsidiary of NTL, which was set up to invest in and provide technological platforms to the financial companies of the group. The company was set up by the founder and ex-promoter of Flipkart, Sachin Bansal, who infused INR40 billion into various financial ventures of the group in FY20. Apart from the lending business, the group owns a general insurance company (Navi General Insurance), broking and investment advisory units and asset management business.

As of June 2023, NTL infused equity of INR20.5 billion in NFL, INR4.87 billion in the insurance vertical and INR1.5 billion in the asset management company. The group does not expect the group entities other than NFL to require material equity and liquidity access from the group resources if required. The group decided to sell its microfinance vertical, CIFCPL, to Svatantra Microfin for INR15 billion which is expected to be completed by end-2023. The transaction is expected to provide additional capital to the group.

CIFCPL had applied for banking licence which was rejected by RBI in 2023; subsequently, the group decided to sell the microfinance subsidiary and focus on its app-based personal and housing loan segment. The sale of CIFCPL was also aligned with the Navi Group's strategic plan to focus on its technological synergies in digital financial offerings.

Franchise Continues to Expand; Product Proposition to Develop Further: After revamping its underwriting model from initial rule basis engine to machine learning model, NFL grew its personal loan book almost 2x in June 2023 to INR78 billion in the past 12 months, while home loan portfolio increased to about INR8 billion since its inception. This growth was fuelled by an increase in marketing and advertising efforts over FY22-FY23. However, the cost of acquisition reduced significantly during the period, on account of the scale achieved. The company has now adopted a co-lending strategy in home loans given that its current cost structure would not be supportive for a significant expansion in this segment. Unsecured personal loans are receiving a significant traction across players and NFL has also benefited from the same. Over the past two years, the product's scope has also expanded significantly. The sourcing algorithms, credit, monitoring and collection models, and other models that help operations across the loan life-cycle have also undergone an evolution and become mature and sharper.

Technology: Cornerstone in Navi's Operational and Business Strategy: Navi leverages technology across various functions of its businesses. It has a single app for the end-user where it offers its insurance, personal loans and asset management services. It has a large tech team of over 600 engineers to develop, maintain and iterate its systems and for analytics across various functions of lending vertical as well as other businesses (which are currently fairly small by vintage and scale). Their systems enable them to monitor the selection of important variables on a real time basis and provide a quick basis for interventions if required across various functions in the lending business. In addition, as Navi builds its own collection team, it expects that running such analytics and collections would help it improve recoveries better than the agency-led collection model. Even in the new businesses that Navi would venture in, technology would be a key part of the process and the company shall remain branchless and would deliver credit in a non-traditional manner to the middle class for their personal and business needs. Ind-Ra expects such use of technology to in the long run show sustained improvements in the asset quality over multiple cycles and improve other operating metrics but also caveats that under conditions of fast growth, certain operational errors may leave a higher than usual impact if they creep in.

Undeployed Resources and CIFCPL Sales Proceeds to Support Business Requirements: Of the INR40 billion corpus and additional INR5billion raised through pledged investments of Sachin Bansal outside the Navi Group in personal capacity as of June 2023, the key fund utilisation comprises the infusion of around INR29 billion in operating entities, with 78% of it mainly infused in the lending businesses as of June 2023; funding of losses; INR8.8 billion of liquidity across the group; and INR3 billion inter corporate deposits in the lending vertical. Most of the incremental funding requirements in the group will mostly emanate from NFL if at all. Overall, the group had committed to maintaining maximum leverage of 3.75x, but with the exit of CIFCPL (relatively higher leverage lending entity in the group), Ind-Ra expects the group to maintain leverage of lower than 3.75x. The promoter's fund-raising track record in his previous role provides the group with substantial experience in the same. Given the pace of capital consumption and growth plans, and the delay in its initial public offering, the group will plan for private equity in the medium term, while maintaining the leverage commitments. In the meanwhile, the proceeds of the sale transaction will support the capital and liquidity requirements across the group, mainly for the lending entity.

High Churning Book; New Product Development to Pan Out in Near- to Medium Term: NFL offers digital personal loans up to a ticket size of INR2 million; in the agency's opinion, this is the easiest product to build through purely digital means. NFL also introduced home loans (up to INR50 million) in December 2020. In 1QFY24, NFL disbursed INR32.3 billion, resulting in disbursements/outstanding assets under management of 42% for NFL. Annually, this ratio has remained 40%-70% for smaller ticket loans in the similar rated category. NFL has almost reached a monthly run rate of INR11 billion disbursements, which could increase further in the near term. Over FY24, as its customer acquisition eases, the focus will now be on other adjacency products, such as cross-selling, new product rollouts among others. However, the agency expects its digital personal loans to pan out as much digital as possible over the medium term in a material manner.

Asset Quality and Credit Cost likely to be Manageable: NFL's gross non-performing assets (NPAs) reduced to 2.5% in 1QFY24 from the peak of 7% during the COVID-19 period. Its net NPAs stood at 0.3% as of 1QFY24 (FY23: 0.2%). A combination of strong growth in assets under management and write-offs by the company led to the reduction in consolidated gross NPAs. The company incurred credit costs of 6.8% in FY23. NFL has substantially increased its focus on collections over the past year and is taking various measures such as enhancing its in-house collection team over the near- to medium term. In its models, static pool indicates peak gross NPAs of 4%-4.5% for post COVID-19 monthly cohorts. The agency expects 5% credit loss on a steady state on personal loans.

Profitability Expectations Building up with Ramp up in Scale: On a standalone basis, NFL reported a profit of INR1,720 million in FY23 (including INR911 million of income from the sale of a 25% stake in CIFCPL to NTL in FY23) and INR260 million in 1QFY24 compared to a loss of INR669 million in FY22. At a consolidated level, the group's profit after tax stood at INR155 million in FY23 (FY22: loss of INR3.7 billion). The group has spent heavily on advertising and its marketing expenses declined in 2HFY23 and are likely to be lower in FY24. With continued ramp up in operations, Ind-Ra expects the economies of scale to lead to a decline in operating costs. From unit economics point of view, on the overall portfolio, the company may have a return on assets of 2%-2.5% (NFL and NTL together) despite the absence of its profitable microfinance operations.

Liquidity Indicator – Adequate: Until INR40 billion is fully deployed as equity, the undeployed proportion is available for liquidity support, while the undeployed portion has declined to about INR8.8 billion across the group as of June 2023, supporting its liquidity requirements. The excess has mostly been deployed in treasury investments in NFL and NTL and can be mobilised quickly for its liquidity support. As on 30 June 2023, out of the total NFL borrowings of INR69 billion, INR3 billion was sourced from the parent (unsecured interest free inter corporate deposits). In addition, the average maturity of NFL's liability tenors exceeds average assets tenor as majority of its book is in unsecured personal loans with an average tenor of six months, leading to asset-liability mismatch. On a standalone basis, the cumulative surplus of up-to-one-year bucket (excess of short-term assets over liabilities) to total assets for NFL stood at about 0.3% at end-June 2023.

NFL's board has approved a policy to maintain its liquidity coverage ratio (high quality liquid assets net cash outflow over the next 30 calendar days) at 150%; Ind-Ra believes this is critical given the low seasoning of the asset book, given its focus on unsecured loans and the pace of disbursements. The agency expects further support in its liquidity through the securitisation of its portfolio. NFS is also scaling up its off-book portfolio with direct assignments and co-lending book to INR5.5 billion and INR7.7 billion, respectively, as of 1QFY24. The share of off-book in the portfolio is likely to increase in the near- to medium-term as the company will further add its co-lending partners which currently stands at five. The company is likely to do home loan portfolio mostly through co-lending partners. Also, the company has diversified its borrowing profile with over 50 lenders and on-balance sheet funding mix of NCDs/PP-MLDs (32% as of June 2023), PTC

(28%), term loan (33%) and CP (7%) with an average cost of borrowings of 10.55% as of June 2023 (March 2023: 10.92%).

Moderate Leverage Critical Given Unsecured Loan Franchise: NFL's standalone leverage (debt/ equity) including internal debt of INR3 billion stood at 2.6x (excluding internal debt of INR3 billion, leverage stood at 2.4x) in FY23, supported by the INR9.5 billion equity infusion by parent. However, with the sale of CIFCPL (which operates at higher leverage than NFL) and subsequent receipt of sales proceeds, the leverage levels are likely to reduce, before it starts building up again as it builds scale. The consolidated leverage of the lending business including internal debt at end-March 2023 stood at 3.5x (December 2021: 3.47x). The company is likely to contain it below 3.75x until the transaction is completed. The group infused INR0.75 billion of equity into CIFCPL in 1QFY24. At a consolidated level, the group had a leverage of 2.74x as of March 2023.

Rating Sensitivities

Positive: A continuous increase in the scale of the group's financial services business with the material group level and standalone profitability, the widening of its product portfolio and sufficient seasoning, while keeping the capital levels materially higher than its peers, on a sustained basis, could lead to a positive rating action.

Negative: The inability to scale up as planned, consistently weak operating parameters, the lending business leverage exceeding 3.75x, consistent losses in the lending business or the gross stage 3 deteriorating over 5%, on a sustained basis, could lead to a negative rating action.

ESG Issues

ESG Factors Minimally Relevant to Rating: Unless otherwise disclosed in this section, the ESG issues are credit neutral or have only a minimal credit impact on NFL, due to either their nature or the way in which they are being managed by the entity. For more information on Ind-Ra's ESG Relevance Disclosures, please click here. For answers to frequently asked questions regarding ESG Relevance Disclosures and their impact on ratings, please click here.

Company Profile

NFL, a wholly owned subsidiary of the Navi group (main holding company is NTL), holds 100% stake in CIFCPL, which has been in operations since 2009. The consolidated AUM of the lending vertical stood at INR85 billion at end-June 2023. NTL plans to foray into financial services business targeted at the middle class using technology as its core competency and developing innovative products.

STANDALONE FINANCIAL SUMMARY

Particulars	FY23	FY22
Total assets (INR million)	84,495	40,933
Total equity (INR million)*	21,965	11,382
Net profit (INR million)	1,720	-669
Return on average assets (%)	2.74	-1.81
Equity/assets (%)	26.0	29.0

Capital adequacy ratio (%)	28.4	28.0
Source: Company Data, Ind-Ra analysis *Total equity is net of deferred tax assets and intangibles		

CONSOLIDATED FINANCIAL SUMMARY (NTL)

Particulars (INR million)	FY23	FY22
Total assets	1,45,017	85,997
Total equity	36,546	35,898
Net profit	141.9	-3,620.9
Source: Company Data, Ind-Ra analysis		

Non-Cooperation with previous rating agency

Not applicable

Solicitation Disclosures

Additional information is available at www.indiaratings.co.in. The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

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Rating History

Instrument Type	Current Rating/Outlook						
	Rating Type	Rated Limits (million)	Rating/Outlook	12 September 2022	6 May 2022	12 April 2022	17 February 2022
PP-MLDs	Long-term	INR3,000	IND PP-MLD A/Stable	PP-MLD Aemr/stable	IND PP-MLD Aemr/Stable	IND PP-MLD Aemr/Stable	IND PP-MLD Aemr/Stable
NCDs	Long-term	INR27,981	IND A/Stable	IND A/Stable	IND A/Stable	IND A/Stable	IND A/Stable
CPs	Short-term	INR10,000	IND A1	IND A/Stable	IND A1	IND A1	IND A1

Annexure

Instrument Type	ISIN	Date of Issuance	Coupon Rate(%)	Maturity Date	Size of Issue (million)	Rating/Outlook
PP-MLD	INE342T07098	24 November 2021	8.60	24 May 2023	INR2,000	WD (Paid in full)

Utilised	INR2,000	
Unutilised	0	
Total	INR2,000	

Instrument Type	ISIN	Date of Issuance	Coupon Rate(%)	Maturity Date	Size of Issue (million)	Rating/Outlook
NCDs	INE342T07106	05 January 2022	9.18	5 April 2023	INR1,000	WD (Paid in full)
NCDs	INE342T07114	18 January 2022	9.50	31 December 2024	INR350	IND A/Stable
PP-MLD	INE342T07122	28 January 2022	9.25	31 July 2024	INR500	IND PP-MLD A/Stable
NCDs	INE342T07130	10 February 2022	9.15	10 May 2023	INR1,400	WD (Paid in Full)
NCDs	INE342T07056	25 August 2021	9.60	25 August 2023	INR300	IND A/Stable
NCDs	INE342T07080	30 September 2021	9.15	30 September 2023	INR800	IND A/Stable
PP-MLD	INE342T07064	21 September 2021	8.75	21 March 2023	INR650	WD (Paid in Full)
Utilised					INR 1,950	
Unutilised					0	
Total					INR1,950	

Instrument Type	ISIN	Date of Issuance	Coupon Rate(%)	Maturity Date	Size of Issue (million)	Rating/Outlook
PP-MLD	INE342T07148	23 February 2022	8.60	23 February 2024	INR1,000	IND PP-MLD A/Stable
PP-MLD	INE342T07155	15 March 2022	8.60	15 March 2024	INR1,500	IND PP-MLD A/Stable
PP-MLD	INE342T07163	31 March 2022	9.90	31 May 2025	INR300	IND PP-MLD A/Stable
Utilised					INR2,800	
Unutilised					INR200	
Total					INR3,000	

Instrument Type	ISIN	Date of Issuance	Coupon Rate(%)	Maturity Date	Size of Issue (million)	Rating/Outlook
NCDs	INE342T07189	8 June 2022	9.20	8 December 2023	INR3x,460	IND A/Stable
NCDs	INE342T07197	8 June 2022	9.50	8 December 2023	INR870	IND A/Stable
NCDs	INE342T07205	8 June 2022	9.40	8 December 2023	INR380	IND A/Stable
NCDs	INE342T07213	8 June 2022	9.75	6 September 2024	INR250	IND A/Stable
Utilised					INR4,960	
Unutilised					INR1,040	
Total					INR6,000	

Instrument Type	ISIN	Date of Issuance	Coupon Rate(%)	Maturity Date	Size of Issue (million)	Rating/Outlook
NCDs	INE342T07221	30 June 2022	9.50	4 July 2023	INR250	IND A/Stable
NCDs	INE342T07247	25 August 2022	9.50	30 September 2024	INR300	IND A/Stable

PP-MLD	INE342T07239	28 July 2022	8.65	28 February 2024	INR1,000	IND PP-MLD A/Stable
Utilised					INR1,550	
Unutilised					INR18,450	
Total					INR20,000	

Complexity Level of Instruments

Instrument Description	**Complexity Indicator**
NCDs	Low
PP-MLDs	High
CPs	Low

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

Contact

Primary Analyst
Aishwary Khandelwal
Senior Analyst
India Ratings and Research Pvt Ltd
Wockhardt Towers, 4th Floor, West Wing, Bandra Kurla Complex, Bandra East,Mumbai - 400051
+91 22 40001700
For queries, please contact: infogrp@indiaratings.co.in

Secondary Analyst
Jindal Haria
Director
+91 22 40001750

Chairperson
Jatin Nanaware
Senior Director
+91 22 40001761

Media Relation
Ameya Bodkhe
Marketing Manager
+91 22 40356121

APPLICABLE CRITERIA

Financial Institutions Rating Criteria

Non-Bank Finance Companies Criteria

Evaluating Corporate Governance

The Rating Process

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