

India Ratings Upgrades Muthoottu Mini Financiers' Debt Instruments to 'IND BBB+' /Stable

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India Ratings and Research (Ind-Ra) has upgraded the ratings of Muthoottu Mini Financiers Limited's (MMFL) debt instruments as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
Bank loans	-	-	-	INR15,000	IND BBB+/Stable	Upgraded
Non-convertible debentures (NCDs*)	-	-	-	INR11,011	IND BBB+/Stable	Upgraded

*details in annexure

The upgrade reflects MMFL's ability to manage the franchisee amidst the challenging operating environment as reflected in a profitable growth in assets under management (AUM), improved operational efficiency, as reflected in the AUM per branch, tight control over credit costs, and better cost of funding, leading to improved margins in FY21. The ratings also factor in MMFL's extensive experience in the gold-loan financing business, and its adequate liquidity and capital buffers.

KEY RATING DRIVERS

Stable Asset Quality Despite Pandemic-led Challenges: The gold loan segment has displayed considerable resilience in face of COVID-19-related disruptions, and has reported stable asset quality. MMFL's gross non-performing assets (NPAs) improved to 0.86% in FY21 (FY20: 1.89%; FY19: 2.16%). The collection efficiency numbers have also shown an improvement sequentially as the economy is opening up. Although the borrower class is vulnerable, the ultimate credit loss is capped due to better loan-to-value and the liquid nature of the collateral. Being in the gold loan business, MMFL's credit cost has always been modest and less volatile through the cycle, leading to better operating profit buffers. Given the softening in gold prices post December 2020, MMFL moved to shorter tenor loans of up-to-three months and three-to-six months. This has had an impact on the yields since MMFL cannot earn incremental yield for a longer period in cases wherein the interest is not serviced on a monthly basis; however, it has shielded the company from the volatility in gold prices. MMFL maintains a risk filter, wherein resolution is initiated if the principal-plus-interest reaches 95% of the loan-to-value, leading to the closing of the loan by the borrower, or in case of a delay, conducting of auctions after providing an intimation about the same to the borrower. Gold prices have corrected in the past few months, and any significant downward movement in the prices in the near term could lead to an increased auction risk. In FY21, MMFL auctioned loans outstanding worth INR450 million; the recovered amount stood at INR470 million.

Improved Profitability, Backed by Better Operational Efficiency: MMFL's net interest margin increased to 9.33% in FY21 (FY20: 8.69%) on account of lower borrowing costs (FY21:11.86%; FY20:13.95%). MMFL's profit before tax rose to INR532 million in FY21 (FY20: INR323 million) supported by the growth in AUM; improving operational efficiency and controlled credit cost. Its pre-provision operating buffer improved to 2.84% of the total average earning assets in FY21 (FY20: 1.3%; FY19: 1.39%) on account of moderation in the cost of funds and improved operational efficiency. The incremental funding for 1QFY22 was mobilised at lower interest rates of 9%-9.5% against earlier levels of 12%. MMFL's cost-to-income ratio improved to 67.8% in FY21 (FY20: 78.5%; FY19: 77.8%); the agency believes the company's operating expense will only moderate further with the rise in the loan book over the medium term. Improved branch productivity, as evident from the AUM / branch, has helped the company derive some operating leverage out of the business model. Ind-Ra believes MMFL is progressing towards improving its operational cost matrix.

Adequate Capital Buffers: MMFL's capitalisation remained stable in FY21, with a tier-1 capital ratio of 22.38% (FY20: 24.57%; FY19: 25.11%) and capital adequacy ratio of 25.75% (FY20:29.65; FY19:34.85%). The portion of equity capital locked in fixed assets reduced to 37% at end-FY21 (end-FY20: 41%). MMFL had leverage (debt/equity; debt excluding interest accrued) of 3.7x in FY21 (FY20: 2.91x; FY19: 2.31x). The leverage levels increased marginally in FY21 due to the availing of additional borrowings during the year to support growth. However, the loan book is granular with good asset quality, and hence, this level of gearing seems reasonable. On a steady state basis, MMFL plans to operate at a leverage of 4x.

Long Track Record of Operations: MMFL has over two decades of experience in the gold finance business in the highly-competitive markets of Kerala and Tamil Nadu. The company has managed multiple cycles in this business, which has seen fluctuations in the gold prices. MMFL has been expanding its franchisee in the core gold finance business, with its AUM growing by 18% yoy to INR19.9 billion at end-FY21 (FY20: growth of 22% yoy). The growth in the AUM has brought in better operational efficiencies (the AUM per branch improved to INR24 million in FY21 from INR21 million in FY20 for gold loans). Furthermore, MMFL's branch network has improved over the last few years; with the addition of 23 new branches in FY21, the branch network expanded to 807 in March 2021 (March 2019: 767 branches) and is looking to expand deeper into south Indian states.

Liquidity Indicator - Adequate: As per the structural liquidity statement dated 31 March 2021, there is adequate surplus in each of the buckets, typically because of shorter tenor loans of three-to-six months on the asset side and long liability tenor of four years. At end-July 2021, MMFL had unencumbered cash of INR443 million and unutilised bank lines of INR2,081 million, which along with steady inflows of loan receivables provide adequate cover to the repayments of borrowings. The total amount of debt that would be matured during the next three months stands at INR2,030 million. In addition to the surplus asset liability mismatch, the liquid nature of the underlying collateral offers support to the liquidity profile. MMFL has reasonable access to funding. It raised INR9.05 billion through the issuance of public and private NCDs and bank borrowings in FY21.

Funding Mix Yet to Be Diversified: Funds mobilised through the NCD route from Kerala formed 79% of MMFL's borrowing mix in FY21; bank funding through working capital and term loans constituted the balance. Historically, the company has shown the ability to mobilise funds from local high net worth individuals and retail borrowers through its branch network in Kerala, where a large part of investors in NCDs are repeat investors. Also, MMFL witnessed an improvement in banking relationships in FY21, as the total number of banks providing funding to MMFL increased to 10 from 7 in FY20. As per the management, the number of new NCD investors is expanding by 35%-40% every year. However, this excessive dependence on one geography for mobilisation of liabilities is fraught with risk.

Overhaul of Technological Systems In Progress: MMFL is reviewing its internal processes and has appointed an external information technology firm to revamp its entire legacy systems. The ongoing upgradation of MMFL's internal information systems would help in better information management and consolidation of information across several zones. Ind-Ra would closely monitor the company's efforts in improving its record-keeping and management information systems. MMFL plans to transition to the new operating system from December 2021; the transition was scheduled to happen earlier but was delayed due to the pandemic-led disruptions.

Geographically Concentrated Portfolio: MMFL portfolio is concentrated in southern India, with Tamil Nadu constituting around 43% (FY20: 41%) of the gold loan portfolio. Tamil Nadu, Kerala, Karnataka, Andhra Pradesh and Telangana constituted around 96% of the gold loan portfolio as on 31 March 2021. The portfolio is likely to remain concentrated in south India over the medium term.

RATING SENSITIVITIES

Positive: Profitable growth in the franchisee with geographical diversification, diversification of funding avenues, improvement in the operational efficiency, leading to better profitability, along with maintaining of capital buffers, and further strengthening of systems and processes could lead to a positive rating action.

Negative: The inability to raise funds at competitive rates, sharp rise in the delinquencies (gross non-performing assets more than 3% on a sustained basis) or credit costs, causing a material depletion in the capital buffers, and adverse regulatory actions, which could materially affect the operating performance, could result in a negative rating action.

COMPANY PROFILE

MMFL, a Kerala-based non-deposit taking non-banking finance company, lends against high-yielding gold jewellery, which forms around 97% of the total loans. It also has around 3% portion of its AUM as micro finance loans. Incrementally, MMFL plans to grow in the western geographies of Gujarat and Maharashtra in the gold loans segment.

FINANCIAL SUMMARY

Particulars	FY21	FY20
Total assets (INR million)	25,192	20,099
Total tangible equity (INR million)	5,091	4,659
Net profit (INR million)	319	336
Return on assets (%)	1.41	1.8
Equity/Asset (%)	20.21	23.2
Tier 1 capital (%)	22.38	24.57
GNPA (%)	0.86	1.89
Source: MMFL; Ind-Ra		

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook				
	Rating Type	Rated Limits (million)	Rating	5 March 2021	24 December 2020	14 August 2020	7 August 2019	14 August 2018
Bank loans	Long term	INR15,000	IND BBB+/Stable	IND BBB/Stable	IND BBB/Stable	IND BBB/Stable	IND BBB-/Stable	IND BBB-/Stable
NCDs	Long-term	INR11,011.1	IND BBB+/Stable	IND BBB/Stable	IND BBB/Stable	IND BBB/Stable	IND BBB-/Stable	IND BBB-/Stable

ANNEXURE

Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/ Outlook
NCD	INE101Q08084	27 January 2016	10.5	27 July 2022	INR121.0	IND BBB+/Stable
NCD	INE101Q08092	27 January 2016	11.25*	27 July 2022	INR319.1	IND BBB+/Stable
NCD	INE101Q07375	24 April 2019	9.75	24 April 2022	INR153.5	IND BBB+/Stable
NCD	INE101Q07383	24 April 2019	10.22*	24 April 2022	INR193.4	IND BBB+/Stable
NCD	INE101Q07391	24 April 2019	10	24 April 2024	INR179.7	IND BBB+/Stable
NCD	INE101Q07409	24 April 2019	10.47*	24 April 2024	INR211.5	IND BBB+/Stable
NCD	INE101Q07722	30 September 2020	9.5	21 January 2022	INR336.0	IND BBB+/Stable
NCD	INE101Q07730	30 September 2020	9.75	29 September 2022	INR134.4	IND BBB+/Stable
NCD	INE101Q07748	30 September 2020	9.77*	29 September 2022	INR278.8	IND BBB+/Stable
NCD	INE101Q07755	30 September 2020	10	29 September 2023	INR204.7	IND BBB+/Stable
NCD	INE101Q07763	30 September 2020	10.22*	29 November 2024	INR75.0	IND BBB+/Stable
NCD	INE101Q07771	30 September 2020	10.5	29 September 2025	INR308.4	IND BBB+/Stable
NCD	INE101Q07789	30 September 2020	10.28*	29 October 2027	INR159.7	IND BBB+/Stable
NCD	INE101Q07797	24 November 2020	9.5	18 March 2022	INR242.3	IND BBB+/Stable
NCD	INE101Q07805	24 November 2020	9.75	23 November 2022	INR123.5	IND BBB+/Stable
NCD	INE101Q07813	24 November 2020	9.77*	23 November 2022	INR222.4	IND BBB+/Stable
NCD	INE101Q07821	24 November 2020	10	23 November 2023	INR212.3	IND BBB+/Stable
NCD	INE101Q07839	24 November 2020	10.22*	23 January 2025	INR86.5	IND BBB+/Stable
NCD	INE101Q07847	24 November 2020	10.5	21 November 2025	INR362.4	IND BBB+/Stable
NCD	INE101Q07854	24 November 2020	10.28*	23 December 2027	INR175.9	IND BBB+/Stable
NCD	INE101Q07862	15 February 2021	9.25	9 June 2022	INR319.9	IND BBB+/Stable

NCD	INE101Q07870	15 February 2021	9.5	14 February 2023	INR212.5	IND BBB+/Stable
NCD	INE101Q07888	15 February 2021	9.54*	14 February 2023	INR450.4	IND BBB+/Stable
NCD	INE101Q07896	15 February 2021	10	14 August 2024	INR472.7	IND BBB+/Stable
NCD	INE101Q07904	15 February 2021	10.71*	14 August 2026	INR218.2	IND BBB+/Stable
NCD	INE101Q08118	15 February 2021	10.25	13 March 2026	INR277.1	IND BBB+/Stable
NCD	INE101Q08126	15 February 2021	10.41*	14 February 2028	INR213.6	IND BBB+/Stable
NCD	INE101Q07912	03 May 2021	9.00	25 August 2022	INR226	IND BBB+/Stable
NCD	INE101Q07920	03 May 2021	9.25	02 May 2023	INR134.7	IND BBB+/Stable
NCD	INE101Q07938	03 May 2021	9.27	02 May 2023	INR224.8	IND BBB+/Stable
NCD	INE101Q07946	03 May 2021	9.75	02 November 2024	INR251.5	IND BBB+/Stable
NCD	INE101Q07953	03 May 2021	10.22	02 July 2025	INR128.1	IND BBB+/Stable
NCD	INE101Q08134	03 May 2021	10.25	02 June 2026	INR240.5	IND BBB+/Stable
NCD	INE101Q08142	03 May 2021	10.41	02 May 2028	INR134.9	IND BBB+/Stable
Utilised limit					INR7605.5	
Unutilised limit					INR3405.6	
Total					INR11011.1	

*Annualized yield

COMPLEXITY LEVEL OF INSTRUMENTS

Instrument Type Complexity Indicator NCDs Low Bank Loans Low For details on the complexity level of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

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Bank Loan

INR 15000 m

Non Convertible Debenture

INR 11011.1 m

Applicable Criteria

Financial Institutions Rating Criteria

Non-Bank Finance Companies Criteria

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