Janalakshmi Financial Services Limited

December 18, 2017

Janalakshmi Financial Services Limited: Ratings downgraded to [ICRA]A- (Negative)/[ICRA]A2+

Summary of rated instruments

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-Term Bank Facilities	1,300.00	1,300.00	[ICRA]A- (negative); revised from [ICRA]A (negative)
Non-Convertible Debentures	3,716.00	3,716.00	[ICRA]A- (negative); revised from [ICRA]A (negative)
Subordinated Debt	751.00	751.00	[ICRA]A- (negative); revised from [ICRA]A (negative)
Commercial Paper	900.00	900.00	[ICRA]A2+; revised from [ICRA]A1
Total	**6,667.00**	**6,667.00**	

Rating action

ICRA has revised the long-term rating outstanding on the Rs. 1,300.00 crore[1] long-term bank facilities, Rs. 3,716.00 crore non-convertible debenture (NCD) programme and Rs. 751.00 crore subordinated debt programme of Janalakshmi Financial Services Limited (JFSL) from [ICRA]A (pronounced ICRA A)[2] to [ICRA]A- (pronounced ICRA A minus). The outlook on the long-term rating has been retained at Negative. ICRA has also revised the short-term rating outstanding on the Rs. 900.00 crore commercial paper programme of JFSL from [ICRA]A1 (pronounced ICRA A one) to [ICRA]A2+ (pronounced ICRA A two plus).

Rationale

The revision in ratings take into account the weakening of JFSL's credit profile following the higher than expected credit costs, as the collection efficiency in the harder buckets (90+dpd) stabilised at a lower level of about 22-23% in the small batch (SB) loans segment over the period Aug-Nov 2017; SB loans accounted for 80% of JFSL's overall portfolio as on November 30, 2017. ICRA expects JFSL's incremental provision and write-offs to be in the range of Rs. 1,300-1,400 crore, sizeable portion of which is expected during H2FY2018; the gross NPA and provisions stood at Rs.2,966 crore and Rs. 1,210 crore respectively as on September 30, 2017. The sharp increase in provisions along with the slowdown in incremental disbursements has impacted the company's overall profitability profile and would lead to a higher than expected erosion in networth during the current fiscal, notwithstanding the fresh capital infusion of Rs. 1,030 crore during 8MFY2018 and the proposed Rs. 770 crore in Dec-Jan 2018. ICRA expects JFSL's networth to moderate to about Rs. 1,200 - 1,300 crore by March 2018 (unadjusted for tax reversals) as compared with about Rs. 2,400 crore as in March 31, 2017. Consequently, the managed gearing[3] is expected to increase to about 6.5-7.0 times by March 31, 2018 (5.0 times as on March 31, 2017).

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[1] 100 lakh = 1 crore = 10 million

[2] For complete rating scale and definitions, please refer to ICRA's website (www.icra.in) or other ICRA rating publications

[3] Includes borrowings, securitized book and public deposits

The ratings nevertheless take note of the company's initiatives to improve its collections by augmenting the field strength, ramping up tele-calling capacity and initiating legal actions via Lok Adalats against delinquent borrowers. JFSL has also strengthened its sourcing norms including improved field verification of borrowers, stricter eligibility criteria and reduction in loan size and tenure for new customers. The company has also stopped disbursements in troubled regions and limited its sourcing to certain geographies. The impact of these steps is however yet to be fully manifested on the ground. On the other hand, the slow-down in incremental disbursements (Rs.90 crore during Aug-Nov 2017) and other uncertainties at the field level are expected to increase customer attrition and have a medium-term impact on business growth and operational performance even after JFSL's conversion to a small finance bank (SFB). The company is likely to commence SFB operations during Q4FY2018.

ICRA takes note of JFSL's adequate liquidity position, supported by on-book liquidity of about Rs.3,600 crore as on date and the proposed equity of Rs.770 crore in the near term. The company however would need a substantial portion (Rs. 1,500 crore) of the liquid funds to meet the cash reserve ratio (CRR) and statutory liquidity ratio (SLR) requirements following the commencement of the SFB operations; it would also need to maintain sufficient liquidity for a steady ramp up in disbursements of Rs.1,500 – 2,000 crore over the next four-six months, as envisaged and for pre-payment of any debt obligations. It would therefore be crucial for JFSL to maintain sufficient liquidity till it obtains the scheduled commercial bank status, post which, it would have access to inter-bank borrowings/ liquidity adjustment facility/ marginal standing facilities.

The ratings continue to factor in JFSL's geographically diversified portfolio, strong management team and board composition, and adequate systems and monitoring processes. The ratings also factor in the monoline nature of JFSL's business, its marginal borrower profile, high inherent operational risk, and lack of diversity in earnings. ICRA notes that conversion to an SFB would address some of these issues including greater diversity of earnings and reduced political risk with better regulatory supervision and liquidity.

Outlook: Negative

The negative outlook factors in the subdued credit risk profile expected over the near term as low business volumes of FY2018 would have a cascading impact on the operational and financial parameters, notwithstanding the sizeable capital infusion and the operational initiatives taken by the company. The ratings would be downgraded if the company's collection efficiency remains subdued or if the capitalization, earnings and liquidity profile deteriorates from the currently envisaged levels. The outlook would be revised to stable in case of a steady improvement in the asset quality and profitability indicators and substantially higher than expected capital infusion.

Key rating drivers

Credit strengths

Geographically diversified across 18 states and two union territories in India - JFSL has a diversified portfolio with presence across 18 states and two union territories across India. The company had a member base of 51 lakhs and a portfolio of Rs. 9,158 crore consisting mostly (about 80%) of SB loans, as on November 30, 2017. Apart from group loans, the company also offers individual loans like small business loans (nano and super-nano) enterprise loans and housing loans, which together constituted 19% of the portfolio as on November 30, 2017. The company also extends loans to corporates which comprised about 1% of the portfolio. Post the SFB conversion, JFSL intends to scale up its exposure to micro, small, and medium enterprises, gold loans and housing finance which would support portfolio diversification over the medium term.

Experienced senior management team with good board representation from private equity (PE) investors - JFSL is supported by a strong and diverse board of directors. The company has a 15-member Board of which seven representatives are from the PE investors and five independent directors. It also has an experienced senior management team with expertise in banking and other financial services.

SFB transition to support the development of a retail franchise and lower the cost of funds - JFSL intends to commence SFB operations during Q4FY2018. The company has made progress towards the transition into an SFB, including upgrading existing branch infrastructure and its IT systems and processes. In ICRA's opinion, JFSL would be able to offer additional loan products, increase its fee-based income and develop a retail deposit franchise over the medium term given its large active customer base which would support its liability profile and funding costs going forward.

Credit weaknesses

Deterioration in asset quality – JFSL's overall collection efficiency has been in the range of 78%-82% during Aug-Nov 2017. ICRA notes that regular collection efficiency has been in the range of 98%-99% during this period, but stagnant overall collections coupled with the shrinking loan book (from Rs. 10,929 crore as on August 31, 2017 to Rs. 9,159 crore as on November 30, 2017) led to increase in 90+ dpd and 180+ dpd from 30.1% and 21.5% as August 31, 2017 to 36.8% and 29.5% as in November 30, 2017. On an absolute basis, the 90+ stood at Rs.3,372 crore as in November 30, 2017. ICRA estimates the company's expected loss from the harder buckets to be in the range of Rs. 2,400 - Rs. 2,500 crore given the 22%-23% collection efficiency (90+ bucket) witnessed in recent months. ICRA takes note of the company's ongoing efforts to improve collections through various measures including augmenting its field force, ramping up its tele-calling capacity and taking actions via the legal route (lok-adalats) against delinquent borrowers have led to some recoveries in the deep delinquent buckets; however, the recoverability of sizeable overdues, considering the marginal borrower profile and unsecured nature of loans, remains to be seen.

Weak profitability; critical to control costs and improve operating efficiency - JFSL reported pre-provisioning loss of Rs.568 crore during H1FY2018 as against Rs.320 crore profit during H1FY2017, largely because of one off interest reversals, lower operating efficiency on account of reduction in performing loan book. Besides, company made provisions of Rs 1,000 crore in H1FY2018. In view of the slowdown in sourcing, the company has taken steps to control its operating costs and has drawn a medium term plan to reduce annual operating costs by about Rs. 400 crore by FY2019-FY2020. This includes closure/consolidation of about 25% of the current branch network and rationalization of the manpower, which are at various levels of implementation. Nevertheless, the current year operating expenses are expected to be higher than in FY2017, which along with moderation in the portfolio and steep credit costs, are expected to result in overall losses (including provisions/write-offs) of about Rs. 2,900-3,000 crore (before tax) for FY2018. ICRA would closely monitor the effects of the various cost control initiatives taken by JFSL on its operating efficiency.

Gearing likely to increase in the near term - JFSL's capital profile is characterised by a networth and gearing of Rs. 1,747 crore and 6.1 times respectively as on September 30, 2017. During 8MFY2018, JFSL raised capital of Rs. 1030 crore through compulsorily convertible preference shares (CCPS), of which Rs.499 crore was raised via Jana Holdings Limited (holds 47.2% equity stake in JFSL). The company is expected to raise Rs. 770 crore of fresh equity during Dec-Jan 2018 from existing and new investors. Notwithstanding the sizeable capital infusion, the company's networth is expected to moderate to Rs. 1,200-Rs. 1,300 crore because of the sizeable losses anticipated for FY2018. Consequently, the gearing is expected to increase to about 6.5-7.0 times by March 31,2018 from 5.0 times as on March 31, 2017 even as the overall debt levels are expected to decline over the near term.

Critical to tap funds in a timely manner to tide over the near-term concerns - JFSL has a diverse lender base, with funding from banks and financial institutions, long-term debentures, portfolio sell-down and commercial paper accounting for 53%, 39%, 6% and 2% respectively of the total borrowings as of October 31, 2017. ICRA notes that, most of the long-term debentures carry certain restrictive financial and operational covenants and a few lenders exercised their scheduled put-option in the past. ICRA notes that the company has been maintaining adequate liquidity position (Rs.3,600 crore as on date) to meet the CRR/SLR requirements, debt repayment obligations and for its incremental disbursements (Rs. 300 – 400 crore per month during Dec-Mar 2018). Ability of the company to secure adequate funding lines to support business growth and debt redemption pressures, if any, would be crucial from a rating perspective.

Monoline nature of business and lack of diversity in earnings - The ratings continue to factor in the monoline nature of JFSL's business, its marginal borrower profile, high inherent operational risk, and lack of diversity in earnings. ICRA notes that conversion to an SFB would address some of these issues including greater diversity of earnings and reduced political risk with better regulatory supervision.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:

ICRA's Credit Rating Methodology for Non-Banking Finance Companies

About the company:

Janalakshmi Financial Services Ltd (JFSL) is a Bangalore-based NBFC-MFI catering to the financial needs of urban poor women through the joint liability mechanism. The company was founded in 2006 by Mr. Ramesh Ramanathan as Janalakshmi Social Services (JSS), whose portfolio was taken over by JFSL in 2008. The promoter shareholding continues to be in JSS (now called Jana Urban Foundation or JUF); the corpus funds in JUF are used for social activities.

JFSL has a diversified presence across 18 states and 2 union territories in India with a portfolio of Rs.9,158 crore as on November 30, 2017; the share of the top 3 states of Tamil Nadu, Karnataka and Maharashtra being about 49% as on November 30, 2017. JFSL registered a high compounded growth of 110% over the last four years ended FY2017. The company raised Rs. 1,030 crore equity during Apr-Nov 2017 from existing and new investors and expects to raise further Rs. 770 crore during Dec-Jan 2018.

In FY2017, JFSL reported a net profit of Rs. 170.0 crore on a total managed asset base of Rs. 15,729.8 crore as against a net profit of Rs. 160.3 crore on a total managed assets base of Rs. 13,345 crore during FY2016. During H1FY2018, JFSL reported a loss of Rs. 1,192 crore on a managed asset base of Rs. 10,332 crore.

Key Financial Indicators

	FY 2016	FY 2017	H1FY2018
Total Income	1,785	2,978	816
Profit after tax	160	170	-1,192
Net worth	1,228	2,397	1,747
Managed Portfolio	11,007	12,551	10,333
Total Managed Assets	13,345	15,730	14,452
Return on Managed Assets	1.7%	1.2%	NA
Return on Net worth	13.9%	9.4%	-57.2%
Gearing	7.95	4.97	6.1
Gross NPA%	0.2%	0.7%	29.9%
Net NPA%	0.1%	0.5%	20.2%
CAR%	17.4%	23.9%	26.6%

Amount in Rs. Crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2018)						Chronology of Rating History for the past 3 years		
								FY2017	FY2016	FY2015
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs crore)	Dec 2017	Jul 2017	Jun 2017	Mar 2017	Nov 2015	Dec 2014
1	Bank Facilities	Long-term	879.00	879.00	[ICRA]A- (Negative)	[ICRA] A (Negative)	[ICRA] A (Stable)	[ICRA] A+ (Negative)	[ICRA] A (Stable)	[ICRA] A- (Positive)
2	Unallocated Amount	Long-term	421.00	421.00	[ICRA]A- (Negative)	[ICRA] A (Negative)	[ICRA] A (Stable)	[ICRA] A+ (Negative)	[ICRA] A (Stable)	[ICRA] A- (Positive)
3	NCD	Long-term	3716.00	3716.00	[ICRA]A- (Negative)	[ICRA] A (Negative)	[ICRA] A (Stable)	[ICRA] A+ (Negative)	[ICRA] A (Stable)	[ICRA] A- (Positive)
4	Subordinated Debt	Long-term	751.00	751.00	[ICRA] A- (Negative)	[ICRA] A (Negative)	[ICRA] A (Stable)	[ICRA] A+ (Negative)	[ICRA]A (Stable)	-
5	Commercial Paper Programme	Short term	900.00	900.00	[ICRA] A2+	[ICRA] A1	[ICRA] A1+	[ICRA] A1+	[ICRA] A1	-

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument Details

ISIN	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Rated Amount	Current Rating and Outlook
NA	Term Loan 1	3-Aug-16	NA	3-Aug-18	43.00	[ICRA]A- (Negative)
NA	Term Loan 2	27-Oct-16	NA	27-Oct-18	72.00	[ICRA]A- (Negative)
NA	Term Loan 3	30-Dec-15	NA	30-Dec-17	14.00	[ICRA]A- (Negative)
NA	Term Loan 4	29-Feb-16	NA	28-Feb-18	17.00	[ICRA]A- (Negative)
NA	Term Loan 5	30-Nov-15	NA	28-Jan-18	7.00	[ICRA]A- (Negative)
NA	Term Loan 6	28-Oct-15	NA	10-Oct-17	1.00	[ICRA]A- (Negative)
NA	Term Loan 7	28-Jan-16	NA	10-Jan-18	9.00	[ICRA]A- (Negative)
NA	Term Loan 8	29-Feb-16	NA	10-Feb-18	9.00	[ICRA]A- (Negative)
NA	Term Loan 9	30-Mar-16	NA	10-Mar-18	10.00	[ICRA]A- (Negative)
NA	Term Loan 10	27-Nov-15	NA	28-Feb-19	25.00	[ICRA]A- (Negative)
NA	Term Loan 11	30-Mar-16	NA	20-Mar-18	60.00	[ICRA]A- (Negative)
NA	Term Loan 12	31-Dec-16	NA	31-Dec-18	50.00	[ICRA]A- (Negative)
NA	Term Loan 13	27-Nov-15	NA	31-Oct-18	138.00	[ICRA]A- (Negative)
NA	Term Loan 14	29-Sep-15	NA	29-Sep-17	3.00	[ICRA]A- (Negative)
NA	Term Loan 15	28-Dec-15	NA	28-Dec-17	25.00	[ICRA]A- (Negative)
NA	Term Loan 16	4-Jan-16	NA	4-Jan-18	25.00	[ICRA]A- (Negative)
NA	Term Loan 17	14-Jan-16	NA	13-Jan-18	5.00	[ICRA]A- (Negative)
NA	Term Loan 18	29-Jan-16	NA	29-Jan-18	33.00	[ICRA]A- (Negative)
NA	Term Loan 19	18-Feb-16	NA	17-Feb-18	43.00	[ICRA]A- (Negative)
NA	Term Loan 20	26-Jul-16	NA	26-Jul-18	9.00	[ICRA]A- (Negative)
NA	Term Loan 21	28-Jun-16	NA	28-Jun-18	86.00	[ICRA]A- (Negative)
NA	Term Loan 22	29-Aug-17	NA	29-Aug-20	195.00	[ICRA]A- (Negative)
NA	Unallocated Amount	-	-	-	421.00	[ICRA]A- (Negative)
INE953L07099	NCD	23-Jan-15	13.60%	23-Jan-19	200	[ICRA]A- (Negative)
INE953L07107	NCD	5-Feb-15	13.50%	5-Feb-18	125	[ICRA]A- (Negative)
INE953L07115	NCD	27-Feb-15	13.50%	27-Feb-18	100	[ICRA]A- (Negative)
INE953L07164	NCD	22-Jul-15	12.75%	22-Jul-17	50	[ICRA]A- (Negative)
INE953L07156	NCD	23-Jul-15	12.85%	23-Jul-21	76	[ICRA]A- (Negative)
INE953L07214	NCD	27-Jul-15	12.75%	27-Jul-17	100	[ICRA]A- (Negative)
INE953L08022	NCD	28-Aug-15	13.10%	28-Aug-17	75	[ICRA]A- (Negative)
INE953L07180	NCD	22-Jul-15	13.10%	22-Jul-19	50	[ICRA]A- (Negative)
INE953L07131	NCD	19-May-15	13.07%	19-May-18	75*	[ICRA]A- (Negative)
INE953L07172	NCD	22-Jul-15	12.85%	22-Jul-18	50	[ICRA]A- (Negative)
INE953L07198	NCD	24-Jul-15	12.85%	28-Jun-18	50	[ICRA]A- (Negative)
INE953L07206	NCD	24-Jul-15	12.85%	28-Jun-18	50	[ICRA]A- (Negative)
INE953L07222	NCD	28-Jul-15	12.85%	28-Jul-18	50	[ICRA]A- (Negative)
INE953L07248	NCD	31-Aug-15	12.85%	16-Aug-18	25	[ICRA]A- (Negative)
INE953L08089	NCD	2-May-16	12.78%	15-May-19	100	[ICRA]A- (Negative)
INE953L08071	NCD	21-Apr-16	12.78%	19-Apr-19	40	[ICRA]A- (Negative)
INE953L08204	NCD	28-Sep-16	Zero Coupon	28-Sep-18	15	[ICRA]A- (Negative)
INE953L08220	NCD	30-Nov-16	10.15%	30-Apr-20	25	[ICRA]A- (Negative)
INE953L07255	NCD	23-Sep-15	12.70%	23-Sep-21	98	[ICRA]A- (Negative)
INE953L07271	NCD	5-Feb-16	12.65%	8-Apr-19	100	[ICRA]A- (Negative)
INE953L07289	NCD	31-Mar-16	12.65%	30-Mar-19	100	[ICRA]A- (Negative)
INE953L08147	NCD	22-Jun-16	12.65%	22-Jun-19	25	[ICRA]A- (Negative)
INE953L07230	NCD	14-Aug-15	12.50%	14-Aug-18	100	[ICRA]A- (Negative)

ISIN	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Rated Amount	Current Rating and Outlook
INE953L07297	NCD	20-Apr-16	12.50%	19-Apr-19	60	[ICRA]A- (Negative)
INE953L07305	NCD	3-May-16	12.50%	26-Apr-19	50	[ICRA]A- (Negative)
INE953L07321	NCD	11-May-16	12.50%	10-May-19	50	[ICRA]A- (Negative)
INE953L07313	NCD	3-May-16	12.50%	28-Mar-19	25	[ICRA]A- (Negative)
INE953L08014	NCD	11-Aug-15	12.43%	10-Aug-18	50	[ICRA]A- (Negative)
INE953L08154	NCD	8-Jul-16	12.40%	8-Jul-19	100	[ICRA]A- (Negative)
INE953L08139	NCD	22-Jun-16	12.33%	22-Dec-17	35	[ICRA]A- (Negative)
INE953L08162	NCD	19-Jul-16	12.25%	15-Mar-18	50	[ICRA]A- (Negative)
INE953L08170	NCD	20-Jul-16	12.25%	19-Jan-18	50	[ICRA]A- (Negative)
INE953L07263	NCD	31-Dec-15	12.00%	31-Dec-18	250	[ICRA]A- (Negative)
INE953L08188	NCD	26-Jul-16	11.95%	25-Jan-18	75	[ICRA]A- (Negative)
INE953L08196	NCD	5-Aug-16	11.95%	5-Feb-18	15	[ICRA]A- (Negative)
INE953L08212	NCD	28-Sep-16	10.50%	28-Sep-19	10	[ICRA]A- (Negative)
INE953L07339	NCD	23-May-16	1.25%	23-May-19	15	[ICRA]A- (Negative)
INE953L08238	NCD	30-Nov-16	10.15%	29-Nov-19	10	[ICRA]A- (Negative)
INE953L08121	NCD	14-Jun-16	Zero Coupon	15-Jul-19	50	[ICRA]A- (Negative)
INE953L08246	NCD	21-Dec-16	10.43%	20-Dec-19	328	[ICRA]A- (Negative)
INE953L08253	NCD	21-Dec-16	10.76%	21-Dec-20	338	[ICRA]A- (Negative)
INE953L08261	NCD	21-Dec-16	11.10%	21-Dec-21	338	[ICRA]A- (Negative)
INE953L08279	NCD	15-May-17	10.00%	15-May-19	25	[ICRA]A- (Negative)
INE953L08287	NCD	15-May-17	10.10%	15-May-20	25	[ICRA]A- (Negative)
Unallocated	NCD-Unallocated	-	-	-	88	[ICRA]A- (Negative)
INE953L08030	Sub debt	22-Dec-15	13.80%	22-Dec-22	330	[ICRA]A- (Negative)
INE953L08048	Sub debt	30-Dec-15	14.00%	30-Jun-21	40	[ICRA]A- (Negative)
INE953L08055	Sub debt	21-Mar-16	14.20%	19-May-23	80	[ICRA]A- (Negative)
INE953L08063	Sub debt	28-Mar-16	13.35%	27-May-22	26	[ICRA]A- (Negative)
INE953L08097	Sub debt	7-Jun-16	13.40%	7-Jun-22	50	[ICRA]A- (Negative)
INE953L08105	Sub debt	7-Jun-16	13.40%	7-Dec-22	50	[ICRA]A- (Negative)
INE953L08113	Sub debt	7-Jun-16	13.40%	7-Jun-23	50	[ICRA]A- (Negative)
NA	Sub debt	26-Aug-15	14.25%	25-Aug-22	50	[ICRA]A- (Negative)
NA	Sub debt	29-Dec-15	14.00%	29-Dec-22	75	[ICRA]A- (Negative)
NA	Commercial Paper	-	-	7-365 Days	900	[ICRA]A2+

* part redemption of Rs. 225 crore on May 19, 2017 through put option

Source: JFSL

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