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India Ratings Upgrades Can Fin Homes to ‘IND AA+’; Outlook Stable

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India Ratings and Research (Ind-Ra) has upgraded Can Fin Homes Limited’s (CFHL) Long-Term Issuer Rating to ‘IND AA+’ from ‘IND AA’. The Outlook is Stable. The instrument-wise rating actions are as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Non-convertible debentures (NCDs)*	-	-	-	INR37.98 (reduced from INR 41.2)	IND AA+/Stable	Upgraded
Subordinated debt*	-	-	-	INR3.0	IND AA+/Stable	Upgraded
Commercial paper (CP)	-	-	7-365 days	INR45.0	IND A1+	Affirmed

*Details in Annexure

The upgrade reflects the resilient performance exhibited by CFHL despite the pandemic-led disruptions in the operating environment. Furthermore, the company managed to grow its franchisee in spite of the challenging scenario and simultaneously maintained a strong control over its asset quality. Ind-Ra has also factored in CHFL's operational track record of more than three decades and its ability to grow the franchisee in an improved operating environment. CFHL has displayed its strength in raising funds at competitive rates of interest, which helped in appropriate pricing of the loans to stay competitive amid competition from banks and other housing finance companies (HFCs). Ind-Ra has taken into consideration the moderation in the leverage due to lower growth in the loan book and has also factored in the healthy internal accruals, which could support further portfolio growth. CFHL's operating profit buffers have remained healthy across cycles. The return ratios have remained stable throughout due to steady net interest margin and optimum operational efficiency.

KEY RATING DRIVERS

Long Track Record of Operations; Well Positioned to Expand Franchisee: CFHL, which started operations in 1987, is a sizable player in the housing finance industry, with assets under management of INR236 billion as on 30 September 2021. The entity has displayed the ability to manage the asset quality and grow the business through various business cycles. It is a fairly well-established player in the southern states of the country and an important player in the low-ticket granular housing finance segment. It has a stable business model, with a consistent track record of profitability due to strong control on credit cost and achievement of optimum operational efficiency. CFHL is well positioned to take advantage of the improving operating environment to expand its franchisee through increased penetration in the existing geographies and diversifying into newer geographies.

Resilient Performance with Franchisee Growth despite Headwinds: CFHL was able to grow its book by 7% yoy in FY21, in line with the industry's performance. Moreover, as on 30 September 2021, the loan book growth stood at 13% yoy, much higher than the industry levels. Ind-Ra believes CFHL is well positioned to take advantage of the improving operating environment to expand its franchisee through enhancing its penetration in the existing geographies and also diversifying into newer geographies.

The headline NPA numbers have remained below 1% for the past few years. The access to the funding avenues remained intact and CFHL could raise at cost-effective rates from banks, capital markets and National Housing Bank (NHB; 'IND AAA'/Stable; 23% of funding). The competitive cost of funding helped in the appropriate pricing of its loans, which helped the company remain competitive in face of pressure from banks. CFHL's operating profit buffers have been strong enough to absorb any possible increase in credit cost. The profitability ratios have remained stable through the cycle for CFHL.

Strong Control over Asset Quality: The pandemic had led to widespread disruptions in the economy due to the national and regional lockdowns, leading to volatility in the cash flows of the borrowers. However, HFCs have shown remarkable resilience in managing the asset quality. In line with the industry, CFHL also displayed strong control over asset quality, with stage 3 assets at 0.8% at 2QFYE22 (FYE21: 0.9%, FYE20: 0.76%). The credit cost has always remained rangebound due to the higher proportion of the home loan book (90%), targeted towards salaried and professional borrowers (74%), in the overall portfolio. Furthermore, CFHL has negligible exposure to construction finance, which has been facing headwinds.

The management's strategy of continuing to focus on the home loan portfolio towards the salaried segment provides comfort. Around 3% of the book has been restructured, which is again in line with the housing finance industry. Even after assuming a material slippage from the restructured book, the incremental credit cost would not disproportionately impact the profitability. CFHL increased the provision coverage on stage 3 assets to 40% at end-2QFY22 (33% at FY21, 36% at end-

2QFY21). The recent Reserve Bank of India (RBI) circular on NPA recognition, which stipulates daily stamping of the loan accounts for NPA mapping and the requirement of clearance of all the past overdues for the NPA account to become standard, can increase the headline NPA numbers. However, the impact on provisioning is not likely to be disproportionately high.

Liquidity Indicator - Adequate: CFHL's structural liquidity statement (adjusted by removing pending disbursements of loans and also draw down of unutilized funding lines) for September 2021 shows negative cumulative mismatches in the one-year bucket. The peak negative cumulative gap stood at INR49 billion in the six-months-to-one-year bucket. The gaps are attributed to longer tenure (15-20 years) of assets (67% of loan book flows in beyond the five-year bucket) as compared to liabilities (8-10 years; just 12% of debt liabilities mature beyond the five-year bucket) and CP (22% of borrowings) maturities within the one-year period. CFHL prepares its asset liability management statement on a contractual basis, unlike other HFCs, which factor in prepayments.

Operationally, CFHL always maintains a backup for CP borrowings in the form of unutilised bank lines. As on 30 September 2021, CFHL has unutilised bank facilities of INR50 billion, which can cushion the gaps in the liquidity profile.

On an operational level, CFHL monitors liquidity on a daily basis and ensures that cash and bank balance, liquid investments, unutilised bank lines minus CP outstanding and advances inflows are sufficient to take care of debt and disbursement commitments for six months. The unutilised bank lines are those that have been sanctioned and documentation for the same has been completed but the funds have not been availed. Furthermore, CFHL can raise funds through the securitisation/assignment route though it has not tapped this avenue in the past. It also has a deposit mobilising license, but it has not relied on this source. CFHL has the ability to raise funds from the market at competitive rates.

Stable Profitability: CFHL has been consistently recording a net interest margin of over 3%. In FY21, CFHL reduced lending rates in order to stay competitive in face of competition from banks and an increased rate of foreclosures. However, the lower cost of funding helped it maintain the margins during the same period. It was able to raise funds from banks at 5.5% and higher amount of CP funding also helped in reducing funding cost. NHB lines (23% of borrowing) come at a competitive pricing, though there are caps on lending rates. It did, however, raised lending rates twice in 1HFY22. CFHL has always maintained a strong control on credit cost and its operating cost has been modest (operating cost to average assets: 0.56% in 1HFY22, 0.58% in FY21, 0.54% in FY20). Increased competition could put some pressure on the margins. The continued ability to raise funding at competitive pricing and manage asset quality will be essential for CFHL to maintain its profitability.

Adequate Capital Buffers: CFHL's leverage (1HFY22: 7.3x, FY20: 7.4x, FY20: 8.7x) has declined over the last one year due to tempered growth in the loan book. As the growth has been reviving, the leverage might inch up in the second half of FY22. However, due to reduced risk weights for small ticket home loans, tier 1 capitalisation (2QFY22: 23.5%) is significantly above the regulatory requirement. The internal accruals are sufficient to take care of growth requirements of 17%-18%, and hence, CFHL might not need external capital infusion to grow at this rate. However, CFHL plans to raise equity capital to grow the loan book by 18%-20%. The capital buffers are reasonable even under Ind-Ra's stress case scenario.

Moderately Diversified Resource Profile: CFHL has a larger proportion of borrowings from banks (banks accounted for 46% of the borrowings at end-September 2021) than other sources with concentration among two banks. Additionally, the company has a sizeable proportion of funding from NHB. Funding through CP increased in proportion (1HFY22: 22%, FY21: 19%), as it was mobilised to redeem some NCDs, and CP funding was available at very competitive rates. Sourcing through the debenture route is limited to 7% of the total funding. CFHL has a deposit-taking license; however, it has not tapped this source of funding to a large extent (only 2%). CFHL's access to funding remains adequate with large unutilised lines of INR50 billion at end-September 2021. CFHL mobilised INR41 billion through NHB, banks and NCDs in FY21.

RATING SENSITIVITIES

Positive: A substantial proportion of granular stable funding in the borrowing mix with diversification in the funding avenues, sizeable expansion in the franchisee, gaining market leadership, expanding presence across multiple geographies while maintaining credit costs will be positive for the ratings.

Negative: Future developments that could, individually or collectively, lead to a negative rating action include:

- significant deterioration in asset quality resulting in the operating buffers falling below 2.5x on a sustained basis
- sustained high leverage
- deterioration in the asset liability maturity profile creating sizeable asset liability tenor mismatch
- fall in competitiveness on account of challenges in raising cost effective funding or otherwise

COMPANY PROFILE

CFHL is a housing finance company started in 1987 by Canara Bank in association with Housing Development and Finance Corporation and Unit Trust of India. The company caters primarily to salaried borrowers in urban areas and 69% of its advances are sourced from southern states. At end-September 2021, CFHL had a loan book of INR235 billion and a network of 187 branches and affordable housing centres and 13 satellite offices.

FINANCIAL SUMMARY

Particulars	FY21	FY20
Total assets (INR million)	220,737	210436
Total equity (INR million)	26,098	21501
PAT (INR million)	4,561	3762
Return on average assets (%)	2.12	1.89
Tier 1 capital (%)	23.28	20.47
Source: CFHL, Ind-Ra		

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook		
	Rating Type	Rated Limits (billion)	Rating/ Outlook	17 December 2020	18 December 2019	7 December 2018
Issuer rating	Long-term	-	IND AA+/Stable	IND AA/Stable	IND AA/Stable	IND AAA/Negative

NCDs	Long-term	INR37.98	IND AA+/Stable	IND AA/Stable	IND AA/Stable	IND AAA/Negative
Subordinated debt	Long-term	INR3	IND AA+/Stable	IND AA/Stable	IND AA/Stable	IND AAA/Negative
CPs	Short-term	INR45	IND A1+	IND A1+	IND A1+	IND A1+

ANNEXURE

Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating
NCDs	INE477A07217	15 November 2016	7.77	15 November2021	INR1.22	WD (paid in full)
NCDs	INE477A07241	18 May 2017	7.89	18 May2022	INR6	IND AA+/Stable
NCDs**	INE477A08025	3 December 2014	8.94	3 December 2024	INR1	IND AA+/Stable
NCD	INE477A07266	17 October 2017	7.44	17 January 2021	INR2	WD (paid in full)
Limits utilised					**INR7.0**	
Limits unutilised ^			-	-	INR33.98	
Total					**INR40.98**	

**sub debt

^The unutilised limit for sub debt is INR2 billion.

COMPLEXITY LEVEL OF INSTRUMENTS

Instrument Type	Complexity Indicator
NCD	Low
Subordinated debt	Low

CP	Low

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

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Ind-Ra currently maintains coverage of corporate issuers, financial institutions (including banks and insurance companies), finance and leasing companies, managed funds, urban local bodies and project finance companies.

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Applicable Criteria

Financial Institutions Rating Criteria
Non-Bank Finance Companies Criteria
Rating Bank Subordinated and Hybrid Securities

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