

India Ratings Downgrades Altico Capital India to 'IND A+'; Outlook Negative

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India Ratings and Research (Ind-Ra) has downgraded Altico Capital India Limited's (Altico) Long-Term Issuer Rating to 'IND A+' from 'IND AA-' and Short-Term Issuer Rating to 'IND A1' from 'IND A1+'. The Outlook is Negative. 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
NCDs*	-	-	-	INR30.5	IND A+/Negative	Downgraded
Bank loans	-	-	-	INR44	IND A+/ Negative	Downgraded
Commercial paper	-	-	Up to 1 year	INR8.5	IND A1	Downgraded
Principal protected market-linked debenture*	-	-	-	INR1	IND PP-MLD A+emr/Negative	Downgraded

* Details in Annexure

*The suffix emr denotes the exclusion of the embedded market risk from the rating. The rating of market-linked debentures is based on an ordinal assessment of the underlying credit risk of the instrument and does not factor in the market risk that investors in such instruments will assume. This market risk stems from the fact that the coupon payment on these instruments will be based on the performance of a reference index or equity share (detailed in the information memorandum of the issue).

PP-MLD refers to full principal protection in the equity-linked notes, wherein the issuer is obligated to pay the full principal upon maturity.

The revision takes into account the continued pressure on the real estate sector, which has resulted in a weakened operating environment for the construction lending business, the stretched working capital cycle for real estate borrowers, which has led to volatile delinquencies, tighter funding, which has resulted in wider spreads, and diluted on-balance sheet liquidity buffers. While the company is diversifying its portfolio both in terms of sectors and ticket size, it is likely to be reflected in the performance only gradually.

KEY RATING DRIVERS

Deterioration in Operating Environment Giving Rise to Asset-side Challenges: The operating environment for real estate players has become extremely challenging, with the tepid sales velocity of residential units, especially in the mid and higher ticket segments, and the funding crunch faced by the sector, given the heightened risk aversion of lenders. Dampening of sales has been higher for Tier II and Tier III developers (excluding the top 15 developers for the industry), who are the target customers for NBFCs. The tightened liquidity has also resulted in shrinkage of borrowing options for the developers, leading to lower portfolio churn, and hence, increased challenges on asset quality.

Altico's loan book (INR69 billion in June 2019) has exposure to real estate developers, many of whom have weak and stretched credit profiles. In terms of the lifecycle, 31% (FY18: 26%, 1HFY19: 28%) of Altico's loan book was attributable to early stage funding of projects as of July 2019, and about 70% of the loan book was under moratorium as of June 2019. Headline NPA numbers remained under control till March 2019 (GNPA: 1.8%), though incrementally pressure could build up as the loan book comes out of moratorium.

Dilution in Liquidity Buffers: Altico's board-approved liquidity policy stipulates the maintenance of a liquidity reserve (cash plus possible prepayments/refinancing) that would be sufficient to meet six months of obligations (debt repayment plus operating expenses and taxes) and three months of disbursements. However, at the end of June 2019, the liquidity reserve was sufficient to meet only four and a half months of obligations. Given the tight liquidity scenario, the probability of getting prepayments as envisaged would be low, which could exert further strain on the liquidity. However, Altico received prepayment of around INR1.9 billion in August 2019. The structural liquidity statement of July 2019 shows positive cumulative mismatches in all the buckets. Altico is in the process of mobilising long-term funds from various sources, which would further strengthen its long-term borrowings.

Concentrated Loan Book: Altico's loan book is concentrated, given the high single party exposures. The top ten individual exposures accounted for 39% of the loan book (90% of the net worth) and the top 10 group exposures accounted for 60% of the loan book (139% of net worth) at end-FY19. With this high concentration, the impact could be disproportionate in the event of any major defaults.

Short Operating Track Record: The ratings remain constrained by Altico's short operational track record compared with that of established non-banking financial companies, its unseasoned lending book, and moderate scale of operations.

Diversification of Loan Portfolio: Altico has been diversifying its loan portfolio by expanding into segments such as warehousing and logistics, and is likely to foray into hospitality, education, healthcare etc. as well. Additionally, it plans to expand into the housing finance business to increase the granularity of the loan book.

Diversified Funding Profile: Altico has credit limits from more than 25 lenders, comprising banks, NBFCs and mutual funds. It has reduced its commercial paper borrowings (3% of funding at end-1QFY20) in light of the challenging liquidity conditions to mitigate the refinancing risk.

Benefit from Strong Sponsors: The ratings continue to benefit from Ind-Ra's expectation of timely support from Altico's ultimate shareholders: Fiera Capital (erstwhile Clearwater Capital Partners LLC acquired by Fiera Capital), Abu Dhabi Investment Council, and Varde Partners, if required. In 4QFY19, Altico had to take a haircut on two of its exposures (around INR3 billion) while selling those loans to asset reconstruction companies. However, the losses were compensated by the capital infusion of INR3.6 billion by the sponsors in the last quarter of FY19.

Adequate Capital Buffers: Altico's leverage continues to be modest (equity to assets: 36% at FYE19), in line with its higher concentrated portfolio. Ind-Ra conducted a stress test on the company, factoring in the median credit rating of its borrowers and multiplying historical default experience for the rating category. The high single-name concentration risk was also tested by assuming additional defaults of the top two exposures, over and above the stress based on rating migration, which is consistent with the stress test that Ind-Ra conducts on lenders with concentrated exposures. The resultant equity, post the test, remains reasonable after absorbing losses.

RATING SENSITIVITIES

Positive: The Outlook could be revised back to Stable as Altico grows its franchise while managing and diversifying the inherent risks in its business, while maintaining adequate liquidity and capitalisation buffers.

Negative: Continued diluted liquidity buffers, challenges on fund mobilisation, significant deterioration in the asset quality, leading to higher slippages, would trigger a negative rating action. Also, reduced expectation of support from the shareholders, which could be on account of weak operating performance or otherwise, could also be a negative rating trigger.

COMPANY PROFILE

Altico was established in 2004 by the funds managed by Clearwater Capital Partners as Clearwater Capital Partners India Private Limited for wholesale lending to capital-constrained Indian small and medium enterprises. It was registered as a non-deposit-accepting non-banking finance company with the Reserve Bank of India in January 2005. Its business strategy initially focused on special situation opportunities across capital structure. In FY15, the company was renamed Altico Capital India Limited, and its business strategy was changed. Altico is focused on high-yield asset-backed senior secured credit opportunities in the real estate sector.

FINANCIAL SUMMARY

Particulars	FY19	FY18
Total assets (INR million)*	83308	66807
Total equity (INR million)*	29586	24445
Profit after tax (INR million)	1467	2646
Return on average assets (%)	1.9	4.9
Tier 1 capital (%)	41.2	40.3
Source: Company, Ind-Ra analysis, *excluding deferred tax assets and intangible assets		

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook		
	Rating Type	Rated Limits (billion)	Rating	24 August 2018	27 February 2018	20 September 2016
Issuer rating	Long-/short-term	-	IND A+/-Negative /IND A1	IND AA-/Stable/IND A1+	IND AA-/Stable/IND A1+	IND AA-/Stable/IND A1+
NCDs	Long-term	INR 30.5	IND A+/-Negative	IND AA-/Stable	IND AA-/Stable	IND AA-/Stable
Bank loans	Long-term	INR44	IND A+/-Negative	IND AA-/Stable	IND AA-/Stable	IND AA-/Stable
Commercial paper	Short-term	INR8.5	IND A1	IND A1+	IND A1+	IND A1+
Principal protected market- linked debenture	Long-term	INR1	IND PP-MLD A+emr/Negative	IND PP-MLD AA-emr/Stable	IND PP-MLD AA-emr/Stable	-

ANNEXURE

Instrument Type	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Issue Subscribed/Outstanding (billion)	Rating Outlook	Rating Action
NCD	INE587007016	18 April 2016	9.95	28 May 2021	INR1.54	INR1.54	IND A+/-Negative	Downgrade
NCD	INE587007024	18 April 2016	9.95	28 May 2021	INR1.54	INR1.54	IND A+/-Negative	Downgrade
NCD	INE587007040	19 December 2016	9.11	28 May 2021	INR1.55	INR1.55	IND A+/-Negative	Downgrade
NCD	INE587007073	6 July 2017	10.25	2 September 2020	INR0.285	INR0.285	IND A+/-Negative	Downgrade
NCD	INE587007099	24 August 2017	10.5	23 August 2020	INR1.625	INR1.625	IND A+/-Negative	Downgrade
NCD	INE587007149	26 March 2018	10.5	26 September 2019	INR0.75	INR0.75	IND A+/- Negative	Downgrade
NCD	INE587007156	26 March 2018	10.5	26 March 2021	INR0.75	INR0.75	IND A+/- Negative	Downgrade

NCD	INE587O07164	29 June 2018	10.5	29 September 2019	INR0.20	INR0.20	IND A+/ Negative	Downgra
NCD	INE587O07172	29 June 2018	10.5	29 December 2019	INR0.30	INR0.30	IND A+/ Negative	Downgra
NCD	INE587O07180	29 June 2018	10.5	29 March 2020	INR0.20	INR0.20	IND A+/ Negative	Downgra
NCD	INE587O07198	29 June 2018	10.5	29 June 2020	INR0.30	INR0.30	IND A+/ Negative	Downgra
NCD	INE587O07214	20 July 2018	Zero Coupon	15 July 2021	INR0.382	INR0.382	IND A+/ Negative	Downgra
NCD	INE587O07222	20 July 2018	Zero Coupon	12 August 2021	INR0.262	INR0.262	IND A+/ Negative	Downgra
NCD	INE587O07230	16 August 2018	SBI 1 Yr. MCLR + 258 bps	16 August 2021	INR2.0	INR2.0	IND A+/ Negative	Downgra
NCD	INE587O07222#	4 September 2018	Zero Coupon	12 August 2021	INR1.00	INR0.265	IND A+/ Negative	Downgra
NCD	INE587O07222#	26 September 2018	Zero Coupon	12 August 2021	INR1.00	INR0.285	IND A+/ Negative	Downgra
NCD	INE587O07271	9 October 2018	Zero Coupon	10 May 2022	INR0.732	INR0.732	IND A+/ Negative	Downgra
NCD	INE587O07222#	31 October 2018	Zero Coupon	12 August 2021	INR1.00	INR0.115	IND A+/ Negative	Downgra
NCD	INE587O07297	18 February 2019	12.5	18 November 2020	INR2.5	INR2.5	IND A+/ Negative	Downgra
Total utilised						INR 15.581		
Total unutilised						INR 14.919		
Principal protected market- linked debenture	INE587O08030	10 April 2017	Zero coupon	9 April 2021	INR0.50	INR0.096	IND PP-MLD A+emr/ Negative	Downgra
Total utilised						INR0.096		
Total unutilised						INR0.904		

COMPLEXITY LEVEL OF INSTRUMENTS

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

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