

August 23, 2022

## Five-Star Business Finance Limited: Ratings upgraded for PTCs issued under five small business loan securitisation transactions

### Summary of rating action

Trust Name <sup>^</sup>	Instrument <sup>*</sup>	Initial Rated Amount (Rs. crore)	Amount O/s after Last Surveillance (Rs. crore)	Amount O/s after Jul-22 Payout (Rs. crore)	Rating Action
Northern Arc 2019 SBL Medici	PTC Series A1	99.05	25.39	14.10	[ICRA]AAA(SO); upgraded from [ICRA]AA-(SO)
Dhruva-III Northern Arc SBL 08 2020	PTC Series A	89.57	55.56	30.02	[ICRA]AAA(SO); upgraded from [ICRA]AA(SO)
Dhruva-IV 10 2020	PTC Series A1	85.91	63.51	37.77	[ICRA]AA(SO); upgraded from [ICRA]AA-(SO)
Dhruva V Vivriti 12 2020	PTC Series A1	46.02	34.40	17.84	[ICRA]AA(SO); upgraded from [ICRA]AA-(SO)
Dhruva-VIII AK 12 2020	PTC Series A1	25.00	19.14	9.90	[ICRA]AA+(SO); upgraded from [ICRA]AA-(SO)

<sup>^</sup> The transactions have been referred to as Medici, Dhruva-III, Dhruva-IV, Dhruva V and Dhruva-VIII in this release

<sup>\*</sup> Instrument details are provided in Annexure I; Instrument name of all transactions has been referred to as PTC Series A1 in this release

### Rationale

ICRA has upgraded the ratings for the pass-through certificates (PTCs) issued under five small business loan securitisation transactions originated by Five-Star Business Finance Limited {FSBFL; rated [ICRA]A+ (Stable)}, as tabulated above. The rating action factors in the sustained healthy collections and low delinquencies witnessed in all the pools. Due to the high amortisation in all the transactions, there has been a build-up of credit enhancement cover over the future PTC payouts. The breakeven collection efficiency is also comfortable compared to the actual collection level observed in the pools. Nonetheless, the ratings would remain exposed to any fresh disruptions that may arise due to the Covid-19 pandemic, leading to lower-than-expected collections.

A summary of the performance of the pools after the July 2022 payouts has been provided below.

Parameter	Medici	Dhruva-III	Dhruva-IV	Dhruva V	Dhruva-VIII
Months post securitisation	35	24	21	19	19
Pool amortisation	69.5%	47.4%	48.8%	53.9%	51.3%
Cumulative collection efficiency	97.9%	99.1%	97.6%	97.5%	98.7%
Average monthly collection efficiency for last three months <sup>1</sup>	101.2%	99.5%	99.5%	99.6%	99.8%
Cumulative prepayment rate	39.6%	36.9%	30.8%	19.4%	19.8%
Average monthly prepayment rate	1.4%	1.9%	1.7%	1.1%	1.2%
Loss-cum-30+ (% of initial pool principal) <sup>2</sup>	8.9%	4.1%	12.6%	10.8%	5.1%
Loss-cum-90+ (% of initial pool principal) <sup>3</sup>	0.5%	0.1%	0.8%	0.2%	0.0%
Breakeven collection efficiency <sup>4</sup>	16.0%	34.3%	59.8%	57.3%	53.4%
Cumulative cash collateral (CC) utilisation	0.0%	0.0%	0.0%	0.0%	0.0%
CC available (as % of balance pool)	23.0%	13.3%	6.9%	6.5%	6.2%

<sup>1</sup> Average of (Total Current and Overdue collections for the month as a % of Total Billing for the month) for three months

<sup>2</sup> Unbilled and Overdue Principal portion of contracts delinquent for more than 30 days, as a % of Initial Pool Principal

<sup>3</sup> Unbilled and Overdue Principal portion of contracts delinquent for more than 90 days, as a % of Initial Pool Principal

<sup>4</sup> (Balance Cash flows payable to investor – CC available) / Balance Pool Cash flows

Parameter	Medici	Dhruva-III	Dhruva-IV	Dhruva V	Dhruva-VIII
Excess interest spread (EIS) over balance tenure (as % of balance pool) <sup>5</sup>	32.9%	40.4%	39.4%	22.4%	22.8%
Principal subordination (% of balance pool)	58.0%	42.7%	NA	26.0%	30.8%

## Key rating drivers

### Credit strengths

- Healthy amortisation of PTCs resulting in build-up of cash collateral (CC), principal subordination (except for Dhruva-IV) and excess interest spread (EIS) cover available for the balance PTC payouts
- Low delinquency build-up in the harder buckets across all the pools

### Credit challenges

- Moderate to high geographical concentration of the contracts in the pools at the state level
- Performance of the pools would be exposed to fresh disruptions caused by the pandemic

## Description of key rating drivers highlighted above

As per the transaction structure for all the pools (except Dhruva-IV), the monthly cash flow schedule comprises the promised interest payment to PTC Series A1 at the predetermined interest rate on the principal outstanding. The principal repayment to PTC Series A1 is promised on the last payout date. During the tenure of PTC Series A1, the collections from the pool, after making the promised interest payouts, will be used to make the expected principal payouts to PTC Series A1. This principal payout is not promised and any shortfall in making the expected principal payment to PTC Series A1 would be carried forward to the subsequent payout.

For the Dhruva-IV transaction, as per the transaction structure, the promised cash flow schedule on a monthly basis comprises the interest to PTC Series A1 (at the predetermined yield) on the outstanding PTC principal on each payout date. The principal repayment to PTC Series A1 is promised on each payout date to the extent of 100% of the billed principal amount for each month. An initial principal subordination of 15% is also available (PTC Series A1 principal was 85% of the pool principal). However, since 100% of the billed pool principal is promised every month to the PTC investor, the maturity date of the PTCs is co-terminus with 85% of the pool principal billing.

All the transactions had reported healthy collections since Q4 FY2021, except during April to June 2021, when the collections were impacted by the pandemic-induced restrictions. The pools had also reported a spike in delinquencies in the softer buckets. However, with improving collection efficiency, the delinquencies have reduced and were sub-1% for the 90+ days past due (dpd) after the July 2022 payout month. However, the pools have high geographical concentration with the share of the top state in the balance pool in the range of 34-58% and the share of the top 3 states exceeding 89% of the balance pool principal. All the pools have witnessed high amortisation. Consequently, the breakeven collection efficiency for the transactions is low.

ICRA will continue to monitor the performance of these transactions. Any further rating action will be based on the performance of the pools and the availability of credit enhancement relative to ICRA's expectations. Notwithstanding the improvement in collections in recent months, ICRA notes that the performance of the pools would remain exposed to any fresh disruptions that may arise due to the pandemic, leading to lower-than-expected collections.

<sup>5</sup>  $(\text{Pool Interest} - \text{PTC Interest}) / \text{Pool Principal outstanding}$

## Key rating assumptions

ICRA's cash flow modelling for the surveillance of asset-backed securitisation (ABS) transactions involves the simulation of potential delinquencies, losses (shortfall in principal collection during the balance tenor of the pool) and prepayments in the pool. The assumptions for the loss and coefficient of variation (CoV) are arrived at after taking into account the past performance of the originator's portfolio and the rated pools as well as the performance and characteristics of the specific pool being evaluated. Additionally, the assumptions may be adjusted to factor in the current operating environment and any industry-specific factors that ICRA believes could impact the performance of the underlying pool of contracts.

After making these adjustments, the expected mean shortfall in principal collection and prepayments during the balance tenure of the pools are provided in the following table.

S. No.	Transaction Name	Expected Loss (% of initial pool principal)	Prepayment
1	Medici	2.0-3.0%	12-18% p.a.
2	Dhruva-III	2.0-3.0%	12-18% p.a.
3	Dhruva-IV	2.5-3.5%	12-18% p.a.
4	Dhruva V	2.5-3.5%	12-18% p.a.
5	Dhruva-VIII	2.0-3.0%	12-18% p.a.

## Liquidity position

### Superior for Medici, Dhruva-III

As per the transaction structure, only the interest amount is promised to the PTC holders on a monthly basis while the principal amount is promised on the scheduled maturity date of the transaction. This imparts significant liquidity to the transaction in the interim period. The cash flows from the pool and the available credit enhancement are expected to be highly comfortable to meet the promised payouts to the PTC investors.

### Strong for Dhruva-IV

The liquidity of the PTCs is expected to be strong, supported by the healthy collections expected from the pool of contracts and the presence of a CC. Even assuming a monthly collection efficiency of only 50% in the underlying pool of contracts in a stress scenario, the CC would cover the shortfalls in the promised cash flows to the senior PTCs for a period of eight months.

### Strong for Dhruva V and Dhruva-VIII

As per the transaction structure, only the interest amount is promised to the PTC holders on a monthly basis while the principal amount is promised on the scheduled maturity date of the transaction. The cash flows from the pool and the available credit enhancement are expected to be comfortable to meet the promised payouts to the PTC investors.

## Rating sensitivities

**Positive factors** – Not applicable for Medici and Dhruva-III transactions

For the other transactions, the ratings can be upgraded on the sustained strong collection performance of the underlying pool of contracts, resulting in an increase in the credit enhancement cover available for the rated instrument.

**Negative factors** – The sustained weak collection performance of the underlying pools (monthly collection efficiency <80%), leading to higher-than-expected delinquency levels and credit enhancement utilisation levels

## Analytical approach

The rating action is based on the analysis of the performance of FSBFL's portfolio till June 2022, the key characteristics and composition of the current pools, the performance expected over the balance tenure of the pools, and the credit enhancement cover available in the transactions.

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Rating Methodology for Securitisation Transactions</a>
Parent/Group support	Not Applicable
Consolidation/Standalone	Not Applicable

## About the company

Five-Star Business Finance Limited (FSBFL) is a Chennai-headquartered non-banking financial company (NBFC) extending secured loans to micro entrepreneurs and self-employed individuals, predominantly in semi-urban markets. The company commenced operations in 1984, with a focus on consumer loans and vehicle finance. In 2005, it shifted its focus to small business loans with typical loan tickets of Rs. 2-10 lakh and an average ticket size of Rs. 3.5 lakh. The loans are predominantly backed by self-occupied residential properties and FSBFL had 300 branches as of March 31, 2022.

The seven institutional investors (Matrix Partners, TPG Asia, Norwest Venture Partners, Sequoia Capital, Sirius II Pte. Ltd (KKR), Bay Capital and TVS Shriram Growth Fund) held a stake of 70.6% in the company as of December 31, 2021, with the promoters holding ~20% (fully diluted).

### Key financial indicators (Ind-AS; audited)

Five-Star Business Finance Limited	FY2020	FY2021	FY2022
Total income	787.3	1,051.3	1,256.2
PAT	261.9	359.0	453.5
Total managed assets	4,353.2	5,793.6	6,343.1
Gross NPA	1.4%	1.0%	1.1%
Net NPA	1.1%	0.8%	0.7%

Amount in Rs. crore

### Status of non-cooperation with previous CRA: Not applicable

### Any other information: None

## Rating history for past three years

Trust Name	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years					
	Instrument	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2022		Date & Rating in FY2021		Date & Rating in FY2020	
				Aug 23, 2022	Feb 21, 2022	Aug 27, 2021	Aug 14, 2020	Sep 20, 2019 <sup>^</sup>	Sep 06, 2019 <sup>*</sup>	
1 Northern Arc 2019 SBL Medici	PTC Series A1	99.05	14.10	[ICRA]AAA(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	Provisional [ICRA]AA-(SO)

	Trust Name	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years			
		Instrument	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2022	Date & Rating in FY2021		Date & Rating in FY2020
					Aug 23, 2022		Oct 28, 2020 <sup>^</sup>	Aug 07, 2020*	
2	Dhruva-III Northern Arc SBL 08 2020	PTC Series A	89.57	30.02	[ICRA]AAA(SO)	[ICRA]AA(SO)	[ICRA]AA(SO)	Provisional [ICRA]AA(SO)	-

	Trust Name	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years			
		Instrument	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2022	Date & Rating in FY2021		Date & Rating in FY2020
					Aug 23, 2022		Dec 08, 2020 <sup>^</sup>	Oct 28, 2020*	
3	Dhruva-IV 10 2020	PTC Series A1	85.91	37.77	[ICRA]AA(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	Provisional [ICRA]AA-(SO)	-

	Trust Name	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years			
		Instrument	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2022	Date & Rating in FY2021		Date & Rating in FY2020
					Aug 23, 2022		Feb 12, 2021 <sup>^</sup>	Dec 31, 2020*	
4	Dhruva V Vivriti 12 2020	PTC Series A1	46.02	17.84	[ICRA]AA(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	Provisional [ICRA]AA-(SO)	-

	Trust Name	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years			
		Instrument	Initial Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2022	Date & Rating in FY2021		Date & Rating in FY2020
					Aug 23, 2022		Feb 12, 2021 <sup>^</sup>	Dec 31, 2020*	
5	Dhruva-VIII AK 12 2020	PTC Series A1	25.00	9.90	[ICRA]AA+(SO)	[ICRA]AA-(SO)	[ICRA]AA-(SO)	Provisional [ICRA]AA-(SO)	-

\* Initial rating assigned

<sup>^</sup>Final rating assigned

### Complexity level of the rated instruments

Trust Name	Instrument	Complexity Indicator
Northern Arc 2019 SBL Medici	PTC Series A1	Moderately Complex
Dhruva-III Northern Arc SBL 08 2020	PTC Series A	Moderately Complex
Dhruva-IV 10 2020	PTC Series A1	Simple

<b>Dhruva V Vivriti 12 2020</b>	PTC Series A1	Moderately Complex
<b>Dhruva-VIII AK 12 2020</b>	PTC Series A1	Moderately Complex

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: [www.icra.in](http://www.icra.in)

### Annexure I: Instrument details

Trust Name	Instrument Type	Date of Issuance / Sanction	Coupon Rate	Maturity Date*	Amount Rated (Rs. crore)	Current Rating
<b>Northern Arc 2019 SBL Medici</b>	PTC Series A1	August 2019	11.00%	December 2025	14.10	[ICRA]AAA(SO)
<b>Dhruva-III Northern Arc SBL 08 2020</b>	PTC Series A	August 2020	10.00%	January 2026	30.02	[ICRA]AAA(SO)
<b>Dhruva-IV 10 2020</b>	PTC Series A1	October 2020	10.00%	April 2025	37.77	[ICRA]AA(SO)
<b>Dhruva V Vivriti 12 2020</b>	PTC Series A1	December 2020	10.15%	November 2025	17.84	[ICRA]AA(SO)
<b>Dhruva-VIII AK 12 2020</b>	PTC Series A1	December 2020	10.00%	December 2024	9.90	[ICRA]AA+(SO)

\*Scheduled maturity at transaction initiation; may change on account of prepayments in the underlying pools

Source: Company

### Annexure II: List of entities considered for consolidated analysis

Not Applicable

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