

June 09, 2023

Five-Star Business Finance Limited: Ratings reaffirmed/assigned

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible debenture programme – Market linked debenture	20.00	20.00	PP-MLD[ICRA]AA- (Stable); reaffirmed
Non-convertible debenture programme	260.00	260.00	[ICRA]AA- (Stable); reaffirmed
	115.00	0.00	[ICRA]AA- (Stable); reaffirmed and withdrawn
	0.00	100.00	[ICRA]AA- (Stable); assigned
Long-term fund-based term loan	2,940.00	2,940.00	[ICRA]AA- (Stable); reaffirmed
Long-term fund-based cash credit	60.00	60.00	[ICRA]AA- (Stable); reaffirmed
Non-convertible debenture programme – Market linked debenture	150.00	150.00	PP-MLD[ICRA]AAA(CE) (Stable); outstanding
Total	3,545.00	3,530.00	

*Instrument details are provided in Annexure I; For the credit enhanced ratings of the entity, refer to the rationales given under the structured finance section [here](#)

The letters, PP-MLD, prefixed to a rating symbol stand for principal protected market linked debentures. According to the terms of the rated instrument, the amount invested, i.e. the principal, is protected against erosion while the returns on the investment could vary, being linked to movements in one or more variables such as equity indices, commodity prices, and/or foreign exchange rates. The assigned rating expresses ICRA's current opinion on the credit risk associated with the issuer concerned. The rating does not address the risks associated with variability in returns resulting from adverse movements in the variable(s) concerned

Rationale

The rating action factors in Five-Star Business Finance Limited's (FSBFL) strong capital and earnings profile. Sizeable capital infusions in the past (~Rs. 2,273 crore raised during FY2016-FY2022) have supported FSBFL's capital profile while it registered a high portfolio growth (compound annual growth rate (CAGR) of 66% over FY2017-FY2023), albeit on a smaller base. FSBFL's managed gearing stood modest at 1.0 times as of March 2023. The company reported a return on managed assets (RoMA) of 8.0% in FY2023 (7.5% in FY2022) while the return on average net worth stood at 15% (15% in FY2022). The company's existing capital structure and expected strong internal accruals would support the growth in its assets under management (AUM), which is expected to increase at a CAGR of 30-35% during FY2024-FY2026. The ratings continue to factor in FSBFL's adequate internal controls, its diversified board and experienced senior management team.

FSBFL's asset quality is characterised by gross stage 3 of 1.4% as of March 2023 (1.0% without considering the impact of the Reserve Bank of India's (RBI) circular dated November 12, 2021¹) compared to 1.1% as of March 2022. The small ticket size secured nature of lending (more than 95% of the loans were against self-occupied properties with a loan-to-value (LTV) of less than 50% for 97% of the AUM as of March 2023) and the high-yielding nature of its exposures provide comfort against the modest risk profile of the target borrower segment. While the asset quality performance, during the stages of scaling up, is a monitorable, FSBFL's healthy internal accruals and current capital structure support its overall risk profile. Control over the underwriting process would be crucial over the medium term, in view of its growth plan, which is expected to keep the portfolio seasoning at a low level. Geographically, the company is expected to focus on deeper penetration in the existing geographies and the portfolio is expected to remain regionally concentrated in southern India over the medium term. As of March 2023,

¹ On Prudential Norms on Income Recognition, Asset Classification and Provisioning

Tamil Nadu (TN), Karnataka, Andhra Pradesh (AP) and Telangana accounted for 94% of the overall portfolio (100% as of March 2018).

ICRA has reaffirmed and withdrawn the rating on the Rs. 115.00-crore non-convertible debentures (NCDs) as the same have been fully redeemed and there is no amount outstanding against the rated instrument. The rating was withdrawn as per ICRA's policy on the withdrawal of credit ratings.

Key rating drivers and their description

Credit strengths

Strong capital structure to support medium-term portfolio growth – FSBFL's capital profile is characterised by a net worth of Rs. 4,340 crore and a capital adequacy ratio of 67.2% as of March 31, 2023. The company had secured regular equity infusions in the past (~Rs. 2,273 crore raised during FY2016-FY2022), which supported its overall risk profile even as it registered a sharp AUM growth. In November 2022, the company's equity shares were listed on National Stock Exchange of India Limited (NSE) & BSE Limited. ICRA notes that while FSBFL is expected to increase its portfolio at a CAGR of ~30-35% during April 2023-March 2026, its leverage is not expected to exceed 4 times during this period.

Strong earnings profile – FSBFL's net profitability improved with profit after tax/average managed assets (PAT/AMA) at 8.0% in FY2023 vis-à-vis 7.5% in FY2022. The net interest margins improved to 16.6% in FY2023 from 15.4% in FY2022 largely due to the reduction in the cost of funds. Accordingly, the pre-provision operating profitability (PPOP) stood at 10.8% in FY2023 vis-à-vis 10.3% in FY2022. Also, the credit costs declined to 0.2% in FY2023 from 0.7% in FY2022 as the overall delinquency levels had improved in FY2023. Further, the company moderated its overall provisions, as a proportion of AUM, to 1.6% from 2.0% in March 2022.

FSBFL's ability to keep the credit costs under control and maintain optimal operating efficiency over the medium term, as it augments its branch network and geographically diversifies its portfolio, would be key from an earnings perspective. ICRA expects the net profitability to moderate from the current level as the leverage increases, though the same is expected to stabilise at 5.5-6.0% in the medium to long term.

Adequate internal control and risk management systems – FSBFL has a well-experienced board, consisting of eight members. Apart from the Chairman and Managing Director (promoter), the board consists of four independent directors, two non-executive nominee directors of the private equity (PE) investors, and one non-executive director. ICRA takes note of the experience of the promoter and the senior management team in retail lending and banking services. The senior management team has been steadily augmented over the past few years in view of the growth plans. The key business functions, including internal audit, business & collections, technology, credit, risk, treasury and human resources, are headed by personnel who have adequate experience in these fields.

FSBFL has maintained prudent underwriting policies with the LTV and the fixed obligations to income ratio (FOIR) capped at around 40-50%. As of March 2023, 55% of the portfolio had an LTV of less than 40%. AUM with LTV of more than 50% accounted for less than 3% of the portfolio as of March 2023 (1% as of March 2021). Considering the target segment, the tenors are relatively longer with 77% of the loans having a tenor of 7 years. This is expected to keep the loan instalment at manageable levels for the target customer segment. The loans are largely given for a ticket size below Rs. 5 lakh, which was 88% of the AUM as of March 31, 2023. All loans are sourced in-house – the company has a widely used loan origination system (LOS) and a dedicated collections team at the branch level, which also monitors collections, post 24 months of loan disbursement, apart from the business team. FSBFL relies on its internal assessment of cash flows to arrive at the borrower-level eligibility though it verifies the credit bureau report for all cases.

Credit challenges

Modest credit profile of target customer segment; asset quality has, however, remained under control – FSBFL’s borrowers are mainly small business owners & self-employed individuals with a focus on the services industry and with gross income levels in the range of Rs. 25,000-40,000 per month, largely without traditional income evidence. Reflecting this moderate credit profile, the softer bucket delinquencies, though improving in recent times, stood high with the 30+ days past due (dpd) at 10.5% as of March 2023 vis-à-vis 16.8% as of March 2022. However, the 90+ dpd was modest at 1.0% as of March 2023 (without considering the impact of the Reserve Bank of India’s (RBI) circular dated November 12, 2021²) vis-à-vis 1.1% as of March 2022 on account of the improving monthly collection efficiency (collections including arrears but excluding prepayments/total demand for the month). This stood at 100.5% in Q4 FY2023 while the company had collected at least one instalment in every month from 97.5% of the portfolio during this period. The restructured book stood at 0.9% of the AUM as of March 2023. ICRA, however, notes that the high envisaged portfolio growth exposes FSBFL to higher credit risk though this is likely to be partially mitigated by its prudent credit norms and policies.

Low portfolio seasoning and geographically concentrated operations – FSBFL’s consolidated portfolio expanded at a CAGR of 66% during FY2017-FY2023 while it grew at a high pace of 37% (annualised) in FY2023 with disbursements at Rs. 3,391 crore vis-à-vis Rs. 1,756 crore in FY2022. The AUM stood at Rs. 6,915 crore as of March 31, 2023 (Rs. 5,067 crore as of March 31, 2022). The AUM is expected to increase at a CAGR of 30-35% during FY2024-FY2026. The steep growth in the past and the expected growth would result in low portfolio seasoning, considering the average tenor of the loans (about 5-7 years). Further, as FSBFL is expected to add more branches over the next few years, it would be crucial to keep the asset quality and operating costs under control. The four southern states, i.e. TN, Karnataka, AP and Telangana, continue to account for about 94% (100% as on March 31, 2018) of the overall portfolio. FSBFL is expected to remain a regional player with the southern states accounting for a sizeable share of the portfolio in the medium term.

Environmental and social risks

Given the service-oriented business of FSBFL, its direct exposure to environmental risks/material physical climate risks is not significant. While, in general, lending institutions can be exposed to environmental risks indirectly through their portfolio of assets, such risks are not material for FSBFL as its incremental lending operations encompass a well-diversified customer base.

With regard to social risks, data security and customer privacy are among the key sources of vulnerability for non-banking financial companies (NBFCs) as material lapses could be detrimental to their reputation and invite regulatory censure. FSBFL has not faced such lapses over the years, which highlights its sensitivity to such risks. Also, the disclosures made by the company outline the key policies, processes, and investments made by it to mitigate the occurrence of such instances. Customer preference is increasingly shifting towards digital banking, a phenomenon that provides an opportunity to reduce the operating costs. In this regard, FSBFL has been making investments to enhance its digital interface with its customers while continuing to maintain a personal touch point with them. While FSBFL contributes to promoting financial inclusion by lending to underserved segments, its lending practices remain prudent as reflected by the healthy asset quality numbers in this segment compared with its peers.

Liquidity position: Strong

The liquidity position is strong with free cash and liquid investments of ~Rs. 1,637 crore as of March 31, 2023 and sanctioned but unutilised bank lines of Rs. 140 crore against debt-servicing obligations of ~Rs. 898 crore during April-September 2023. The funding mix comprises bank term loans (56% of the total borrowings as of March 2023), securitisation (23%), non-convertible debentures (12%) and term loans from financial institutions & external commercial borrowings (ECB; the balance). Going forward, it would be crucial for FSBFL to secure adequate long-term funds at competitive rates, to achieve the envisaged business growth, while maintaining a strong liquidity profile.

² On Prudential Norms on Income Recognition, Asset Classification and Provisioning

Rating sensitivities

Positive factors – ICRA could revise the outlook to Positive or upgrade the ratings if the company is able to scale up its loan portfolio significantly while maintaining good asset quality and a strong earnings profile on a sustained basis.

Negative factors – Pressure on the ratings could arise in case of an increase in the leverage beyond 4.0 times or a deterioration in the asset quality indicators, leading to a decline in the RoMA to less than 4.0% on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA's credit rating methodology for non-banking finance companies Policy on Withdrawal of Credit Ratings
Parent/Group support	Not applicable
Consolidation/Standalone	The ratings are based on the standalone financials of the company

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, primarily 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 a typical loan ticket size of Rs. 2-10 lakh and an average ticket size of Rs. 3-3.5 lakh. Its loans are predominantly backed by self-occupied residential properties. As of March 31, 2023, the company had 373 branches across 8 states/Union Territories.

The company was listed on the NSE & BSE in November 2022. As of March 2023, the individual promoters & promoter group (Mr. Lakshmiopathy Deenadayalan and his family) held 18.5% of the stake in the company, being the single largest shareholders.

Key financial indicators (Ind-AS; audited)

Five-Star Business Finance Limited	FY2021	FY2022	FY2023
Total income	1,051.3	1,256.2	1,528.9
Profit after tax	359.0	453.5	603.5
Net worth	2,318.2	3,710.4	4,339.5
Total managed portfolio	4,445.4	5,067.1	6,914.8
Total managed assets	5,793.6	6,343.1	8,702.8
Return on managed assets	7.1%	7.5%	8.0%
Return on net worth	16.8%	15.0%	15.0%
Gearing (reported; times)	1.5	0.7	1.0
Gearing (managed; times)	1.5	0.7	1.0
Gross stage 3	1.0%	1.1%	1.4%
Net stage 3	0.8%	0.7%	0.7%
CRAR	58.9%	75.2%	67.2%

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

S. No.	Instrument	Type	Current Rating (FY2024)		Chronology of Rating History for the Past 3 Years							
			Amount Rated	Amount Outstanding	Current Rating	Date & Rating in FY2023			Date & Rating in FY2022		Date & Rating in FY2021	
			(Rs. crore)	(Rs. crore)	Jun-09-2023	Mar-01-2023	Feb-23-2023	Mar-11-2022	Jun-29-2021	Dec-15-2020	Sep-25-2020	Sep-07-2020
1	Market linked debentures	Long term	20.00	20.00	PP-MLD[ICRA]AA- (Stable)	PP-MLD[ICRA]AA- (Stable)	PP-MLD[ICRA]AA- (Stable)	PP-MLD[ICRA]A+ (Stable)	PP-MLD[ICRA]A+ (Stable)	PP-MLD[ICRA]A (Stable)	PP-MLD[ICRA]A (Stable)	PP-MLD[ICRA]A (Stable)
2	Long-term fund-based term loan	Long term	2,940.00	2,647.20	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
3	Long-term fund-based cash credit	Long term	60.00	53.50	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	-	-	-	-	-	-
4	Long term – Unallocated	Long term	0.00	0.00	-	-	-	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
5	NCD	Long term	260.00	155.00	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
6	NCD	Long term	115.00	0.00	[ICRA]AA- (Stable); withdrawn	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
7	NCD	Long term	100.00	0.00	[ICRA]AA- (Stable)	-	-	-	-	-	-	-

For the credit enhanced ratings of the company, refer to the rationales given under the structured finance section [here](#)

Complexity level of the rated instrument

Instrument	Complexity Indicator
Non-convertible debenture – Market linked debenture	Moderately Complex
Non-convertible debenture	Simple
Long-term fund-based term loan	Simple
Long-term fund-based cash credit	Simple

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: [Click Here](#)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated	Current Rating and Outlook
					(Rs. crore)	
INE128S07366	NCD	Apr-11-19	11.40%	Apr-11-24	30.00	[ICRA]AA- (Stable)
INE128S07424	NCD	May-13-20	12.75%	May-13-26	15.00	[ICRA]AA- (Stable)
INE128S07432	NCD	May-28-20	10.50%	May-26-23	15.00	[ICRA]AA- (Stable)
INE128S07440	NCD	Jun-12-20	11.00%	Jun-12-23	25.00	[ICRA]AA- (Stable)
INE128S07457	NCD	Jun-24-20	11.00%	Apr-21-23	115.00	[ICRA]AA- (Stable); withdrawn
INE128S07507	NCD	Sep-30-20	NA	Sep-30-29	70.00	[ICRA]AA- (Stable)
Unallocated	NCD	-	-	-	205.00	[ICRA]AA- (Stable)
INE128S07523	NCD-MLD	Dec-15-20	10-yr G-Sec	Jun-15-23	20.00	PP-MLD[ICRA]AA- (Stable)
NA	Term loan - 1		NA		23.37	[ICRA]AA- (Stable)
NA	Term loan - 2		NA		106.68	[ICRA]AA- (Stable)
NA	Term loan - 3		NA		236.11	[ICRA]AA- (Stable)
NA	Term loan - 4		NA		12.44	[ICRA]AA- (Stable)
NA	Term loan - 5		NA		22.17	[ICRA]AA- (Stable)
NA	Term loan - 6		NA		100.00	[ICRA]AA- (Stable)
NA	Term loan - 7		NA		9.73	[ICRA]AA- (Stable)
NA	Term loan - 8		NA		13.13	[ICRA]AA- (Stable)
NA	Term loan - 9		NA		54.17	[ICRA]AA- (Stable)
NA	Term loan - 10		NA		40.83	[ICRA]AA- (Stable)
NA	Term loan - 11		NA		48.00	[ICRA]AA- (Stable)
NA	Term loan - 12		NA		63.75	[ICRA]AA- (Stable)
NA	Term loan - 13		NA		175.75	[ICRA]AA- (Stable)
NA	Term loan - 14		NA		11.68	[ICRA]AA- (Stable)
NA	Term loan - 15		NA		107.64	[ICRA]AA- (Stable)
NA	Term loan - 16		NA		47.27	[ICRA]AA- (Stable)
NA	Term loan - 17	Aug-2018 to Dec-2022	NA	Feb-2023 to Sep-2029	12.00	[ICRA]AA- (Stable)
NA	Term loan - 18		NA		70.44	[ICRA]AA- (Stable)
NA	Term loan - 19		NA		1.58	[ICRA]AA- (Stable)
NA	Term loan - 20		NA		223.02	[ICRA]AA- (Stable)
NA	Term loan - 21		NA		86.57	[ICRA]AA- (Stable)
NA	Term loan - 22		NA		50.00	[ICRA]AA- (Stable)
NA	Term loan - 23		NA		10.87	[ICRA]AA- (Stable)
NA	Term loan - 24		NA		75.00	[ICRA]AA- (Stable)
NA	Term loan - 25		NA		150.00	[ICRA]AA- (Stable)
NA	Term loan - 26		NA		70.00	[ICRA]AA- (Stable)
NA	Term loan - 27		NA		75.00	[ICRA]AA- (Stable)
NA	Term loan - 28		NA		100.00	[ICRA]AA- (Stable)
NA	Term loan - 29		NA		250.00	[ICRA]AA- (Stable)
NA	Term loan - 30		NA		100.00	[ICRA]AA- (Stable)
NA	Term loan - 31		NA		200.00	[ICRA]AA- (Stable)
NA	Term loan - 32		NA		100.00	[ICRA]AA- (Stable)
NA	Term loan - Unallocated		NA		292.80	[ICRA]AA- (Stable)
NA	Cash credit - 1	Nov-15-12	NA	NA	5.00	[ICRA]AA- (Stable)
NA	Cash credit - 2	Aug-06-13	NA	NA	5.00	[ICRA]AA- (Stable)
NA	Cash credit - 3	Jul-04-16	NA	NA	5.00	[ICRA]AA- (Stable)
NA	Cash credit - 4		NA	NA	10.00	[ICRA]AA- (Stable)
NA	Cash credit - 5	Oct-20-20	NA	NA	2.00	[ICRA]AA- (Stable)
NA	Cash credit - 6	Nov-17-21	NA	NA	5.00	[ICRA]AA- (Stable)
NA	Cash credit - 7	Dec-08-21	NA	NA	5.00	[ICRA]AA- (Stable)
NA	Cash credit - 8	Nov-23-22	NA	NA	2.00	[ICRA]AA- (Stable)

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated	Current Rating and Outlook
					(Rs. crore)	
NA	Cash credit - 9	Feb-22-22	NA	NA	5.00	[ICRA]AA- (Stable)
NA	Cash credit - 10	Feb-04-22	NA	NA	0.50	[ICRA]AA- (Stable)
NA	Cash credit - 11	Nov-08-21	NA	NA	9.00	[ICRA]AA- (Stable)
NA	Cash credit – Unallocated	NA	NA	NA	6.50	[ICRA]AA- (Stable)

Source: FSBFL

[Please click here to view details of lender-wise facilities rated by ICRA](#)

Annexure II: List of entities considered for consolidated analysis: Not applicable

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