

Fitch Assigns Muthoot Finance First-Time 'BB+' Rating; Outlook Stable

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Fitch Ratings has assigned India-based Muthoot Finance Limited (MFL) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDR) of 'BB+'. The Outlook is Stable.

KEY RATING DRIVERS

IDRS

MFL's Long-Term IDR is driven by the non-bank financial institution's (NBFIs) Standalone Credit Profile. The ratings take into account MFL's well-established franchise in the niche segment of gold-backed financing, its low credit losses and satisfactory leverage. These are counterbalanced by high exposure to operational risks in the business and MFL's moderate scale in comparison with other larger Indian NBFIs. However, the rating also factors in MFL's long record in its core business, strong profitability and stable funding and liquidity.

MFL caters mainly to borrowers in rural and semi-urban geographies, and has adequate pricing power despite the competitive dynamics. It has diversified operations across India while its branch network has the highest usage relative to peers. Its primary collateral is gold jewellery, which has a liquid market. Tighter regulations since 2013 have ensured propriety in loan-to-value standards as well as standardised auction processes. However, operational risk is high in gold-backed financing due to its decentralised branch-led disbursement and storage of gold jewellery stock in the company's branches.

The business model benefits from a high net interest margin (average 11.7% in last five years), which is reflected in high profitability as both operating costs and credit costs are low. Healthy internal capital generation results in a moderate debt/tangible equity ratio (2.7x at end-March 2019) while core capitalisation is commensurate with the risk. The company aims to maintain leverage at comfortable levels.

MFL's funding has become less concentrated. Bank loans form 49% of total borrowings while public non-convertible debentures constitute another 30% of total borrowings, of which a significant part is from MFL's retail customers in south-India states. MFL started accessing CP since financial year ended-March 2017 (FY17) on improved access to markets and lower interest rates, and increased its CP share to 18% by FYE19. A well-matched asset liability profile is supported by the low tenor of gold loans and high prepayments, while 36% of funding is long-term despite a mostly short-term asset profile. MFL's unused credit lines also provide an additional liquidity buffer against any unforeseen liquidity stress.

MFL has been diversifying into other segments, such as rural microfinance loans, low-cost rural housing, and auto loans, to benefit from a large customer database and branch infrastructure synergies. Fitch regards these as non-core to MFL, and could be a source of risk with higher growth implying a higher risk appetite in less familiar businesses. Non-gold loan products form 11% of the total assets under management, on a consolidated basis, which is likely to increase. Nevertheless, Fitch expects gold loans to remain the dominant business.

RATING SENSITIVITIES

IDRS

MFL's Long-Term IDR is at the higher-end of peers and any rating upside is improbable in the near term. The rating is likely to see downward pressure if losses stemming from operational risk are higher than Fitch's expectations or a sharp and sudden decline in gold prices were to materially affect earnings and capital buffers. The rating would also be sensitive to rising leverage (if debt/equity approached 4x) and a significant increase in exposure to non-core lending products or material losses arising from non-core lending products.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg.

ENTITY/DEBT	RATING
HIDE RATING ACTIONS	
Muthoot Finance Ltd	LT IDR
	BB+
	New Rating
	LC LT IDR
	BB+
	New Rating