December 09, 2022

Fusion Micro Finance Limited: Rating upgraded; Rating upgraded and simultaneously withdrawn for Rs. 288-crore NCD programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
NCD programme	609.50	609.50	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
NCD programme	288.00	-	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable) and simultaneously withdrawn
Subordinated debt	55.00	55.00	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Total	**952.50**	**664.50**	

**Instrument details are provided in Annexure I*

Rationale

The rating revision factors in Fusion Micro Finance Limited's (Fusion) increased scale of operations and the improvement in its profitability indicators, driven by the increase in yields and the reduction in the credit costs in H1 FY2023. In addition, the rating action factors in the improvement in the company's capitalisation profile, given the recent capital raise via its initial public offer (IPO). Fusion reported assets under management (AUM) of Rs. 8,047 crore as on September 30, 2022 compared to Rs. 6,786 crore as on March 31, 2022. Its return on managed assets (RoMA) improved to 3.9% (annualised) in H1 FY2023 from 0.3% in FY2022. Further, Fusion raised Rs. 600 crore of equity in November 2022, which has resulted in a strong net worth base for its scale of operations and growth plans.

The rating also continues to factor in the company's healthy geographical diversification and its robust and integrated systems and processes, which aids in good credit appraisal and portfolio monitoring. ICRA notes that Fusion's profitability was impacted in FY2021 and FY2022 by higher credit costs because of the deterioration in the asset quality. However, as the incremental credit cost has declined in H1 FY2023 and net interest margins (NIMs) have increased, Fusion's profitability has improved and is expected to remain healthy. The rating also factors in Fusion's diversified borrowing profile, which mainly comprises funding from banks, followed by non-banking financial institutions (NBFCs) and financial institutions (FIs), non-convertible debentures (NCD) and subordinated debt, external commercial borrowing (ECB) and direct assignment (DA).

The rating is, however, constrained by Fusion's subdued, albeit improving asset quality, as it reported gross stage 3 (GS3) of 3.8% as on September 30, 2022, after writing off Rs. 156 crore of the portfolio in H1 FY2023. ICRA notes that the improvement in the GS3 from 5.7% as on March 31, 2022 was supported by write-offs and the growing loan book.

The rating also factors in the risks associated with the unsecured nature of microfinance loans, the marginal borrower profile, which is susceptible to income shocks, and the political and operational risks associated with microlending, which may lead to volatility in the asset quality indicators.

The Stable outlook on the [ICRA]A rating reflects ICRA's opinion that the company will be able to maintain its credit profile, while expanding its scale of operations, maintain healthy profitability and improve its asset quality.

ICRA has upgraded the rating with a Stable outlook while simultaneously withdrawing the rating outstanding for the Rs. 288-crore NCD programme as the instrument has been repaid by the company and there is no amount outstanding against the same. The rating has been withdrawn in accordance with ICRA's policy on the withdrawal of credit ratings.

Key rating drivers and their description

Credit strengths

Established track record and increased scale of operations with improvement in profitability – Incorporated in 1994, Fusion commenced its microfinance operations from 2010. It has an established track record of over a decade with consistent growth in its AUM. Its gross AUM stood at Rs. 8,047 crore as on September 30, 2022 compared to Rs. 6,786 crore as on March 31, 2022. Since March 2019, Fusion's AUM has increased at a compound annual growth rate (CAGR) of ~37% till September 2022.

The company also increased its branch network to more than 1,000 as on September 30, 2022, from around 500 as on March 31, 2019 to meet its growth plans and channelise incremental disbursements. As on September 30, 2022, Fusion's operations were well diversified across 19 states/Union Territories (UTs) with the top 3 states accounting for around 51% of the AUM.

In addition, the company witnessed an improvement in the NIM in H1 FY2023 driven by the increase in yields. This, along with the reduction in credit costs, helped the company report an improvement in its profitability in H1 FY2023. Fusion reported a net profit of Rs. 170 crore in H1 FY2023, translating into RoMA of 3.9% and a return on net worth (RoNW) of 23.9% compared to Rs. 22 crore, 0.3% and 1.7%, respectively, in FY2022.

Strong capitalisation profile supported by recent capital raise – Fusion had a capital to risk weighted assets ratio (CRAR) of 20.97%, a managed gearing[1] of 4.8 times and reported net worth of Rs. 1,514 crore as on September 30, 2022. The same is expected to have improved further after the capital raise of Rs. 600 crore in November 2022. This provides Fusion with sufficient cushion to absorb future losses, if any, and support for its growth plans. ICRA expects Fusion to maintain a healthy capitalisation level over the medium term as well.

Diversified funding profile – Fusion had a fairly diversified lenders' base as on September 30, 2022, with direct funding relationships with 56 distinct lenders, including public sector banks, private sector banks (including small finance banks (SFBs) and foreign banks), NBFCs, and development financial institutions (DFIs). In addition, the company had borrowings in the form of ECBs, NCD issuances, sub-debt and off-book funding. Going forward, the funding profile is expected to remain diversified with the increasing share of public sector banks. ICRA notes that the company was able to secure funding of around Rs. 3,450 crore in H1 FY2023 and has a strong funding pipeline of more than Rs. 4,500 crore as on date.

Experienced and professional management with good portfolio monitoring processes – Fusion has completed more than a decade in microfinance operations. It draws upon the experience of its promoters and management personnel, some of whom have remained with the company for long, and upon the instituted policies, operational infrastructure and guidance. Fusion has robust, digitally-enabled credit appraisal and monitoring processes such that detailed daily data at the last mile level is available through its management information system (MIS). It also has a strong recovery and internal audit team, which ensures checks and balances regularly through surprise visits, employee rotation and digital technology, affording accountability to all the employees.

Credit challenges

Subdued, albeit improving, asset quality metrics – Fusion's asset quality was impacted, like other microfinance institutions (MFIs), due to the Covid-19 pandemic. It reported GS3 of 5.7% as on March 31, 2022. However, with write-offs, recoveries and growth in the loan book in H1 FY2023, the GS3 declined to 3.8% in September 2022. ICRA notes that Fusion wrote off Rs. 156 crore of the portfolio in H1 FY2023.

ICRA also notes that Fusion had not restructured its loan book under the Reserve Bank of India's (RBI) Restructuring Framework 1.0, though it had restructured 2.5% of its AUM under Framework 2.0, which was relatively lower than the industry average.

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[1] *Managed gearing = (on-book debt + off-book portfolio) / net worth*

The standard restructured book declined to 0.5% of the AUM as on September 30, 2022, on the back of recoveries and slippages.

Ability to manage political, communal and other risks in the microfinance sector – The microfinance industry is prone to socio-political and operational risks, which could negatively impact its operations and financial position. However, a geographically diversified portfolio would mitigate these risks to some extent as these issues are largely region-specific, so far. Fusion's ability to onboard borrowers with a good credit history, recruit and retain employees and improve its geographical diversity further by penetrating in recently entered territories with nascent operations would be relevant for managing the high growth rates.

Marginal borrower profile with high susceptibility to income shocks – The rating factors in the risks associated with the marginal borrower profile, unsecured lending, increased risks from multiple lending and overleveraging, business and political risks, along with the challenges associated with a high pace of growth and attrition. While credit bureaus checks and the regulatory ceiling on borrower repayment capacity reduces concerns on overleveraging, issues related to the policy of MFIs, regarding their underwriting practices, borrowers' income and leverage assessment, multiple identity proof as well as gaps in the information available with the bureaus remain.

Liquidity position: Adequate

As on September 30, 2022, Fusion had a free cash and liquid balance of Rs. 866 crore with debt obligations (including interest) of Rs. 1,894 crore over the six-month period ending March 2023 and collections (including interest) of Rs. 2,307 crore during this period. Additionally, it had sanctions in the pipeline of more than Rs. 2,000 crore, which will support its debt servicing and growth plans. Further, Fusion has raised Rs. 600 crore of primary capital via an IPO in November 2022.

Rating sensitivities

Positive factors – ICRA could change the outlook to Positive or upgrade the rating if the company demonstrates sustained profitable growth (RoMA>3%) while maintaining comfortable capitalisation (managed gearing below 4 times) and healthy asset quality indicators.

Negative factors – ICRA could change the outlook to Negative or downgrade the rating if the company's managed gearing increases to more than 5 times on a sustained basis or there is a significant deterioration in the asset quality or weakening of the profitability (RoMA<2%) on a sustainable basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Non-banking Finance Companies ICRA Policy on Withdrawal of Credit Ratings
Parent/Group support	Not applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company

About the company

Incorporated in 1994, Fusion Micro Finance Limited started microfinance operations in 2010 and became a registered NBFC-MFI in 2014. The company is engaged in microfinance lending, providing financial services (and educating borrowers on financial literacy) to poor women in India who are organised as joint liability groups (JLGs). In addition to the core business of providing microcredit, Fusion uses its distribution channels to provide other financial products and services to members, primarily the purchase of productivity enhancing products such as mobile phones, mixer grinders/ bicycles, emergency loans, etc. Fusion also has a small portfolio in the micro, small and medium enterprise (MSME) segment as well, accounting for 2% of the total AUM as on September 30, 2022.

As on September 30, 2022, Fusion had a presence in 390 districts across 19 states/UTs through 1,031 MFI branches. It reported a profit after tax (PAT) of Rs. 170 crore in H1 FY2023 (limited review) on gross AUM of Rs. 8,047 crore as on September 30, 2022 vis-à-vis a PAT of Rs. 22 crore in FY2022 on gross AUM of Rs. 6,786 crore as on March 31, 2022.

Key financial indicators (audited)

Fusion Micro Finance Limited	FY2020	FY2021	FY2022	H1 FY2023*
Accounting as per	Ind AS	Ind AS	Ind AS	Ind AS
Net interest income	329	452	568	429
Profit after tax	70	44	22	170
Net worth	1,199	1,246	1,338	1,514
Assets under management	3,608	4,638	6,786	8,047
PAT / Average managed assets	1.7%	0.8%	0.3%	3.9%
PAT / Average net worth	7.6%	3.6%	1.7%	23.9%
Gross stage 3	1.1%	5.5%	5.7%	3.8%
Net stage 3	0.4%	2.3%	1.7%	1.1%
Capital adequacy ratio	35.8%	27.3%	21.9%	21.0%
Gearing (reported; times)	2.5	3.6	4.3	4.3
Gearing (managed; times)	2.7	3.7	4.9	4.8

*Source: Company, ICRA Research; All ratios as per ICRA's calculations; *Limited review; Amount in Rs. crore*
Managed gearing = (on-book debt + off-book portfolio) / net worth

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument		Current Rating (FY2023)					Chronology of Rating History for the Past 3 Years						
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of November 30, 2022 (Rs. crore)	Date & Rating in FY2023			Date & Rating in FY2022	Date & Rating in FY2021					Date & Rating in FY2020
					Dec-09-22	Apr-26-22	Apr-7-22	Sep-21-21	Dec-14-20	Nov-11-20	Oct-5-20	Aug-24-20	May-11-20	Aug-30-19
1	Non-convertible debenture	Long term	609.50	483.00	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
2	Non-convertible debenture	Long term	288.00	-	[ICRA]A (Stable); withdrawn	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
3	Subordinated debt	Long term	55.00	55.00	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)							
4	Non-convertible debenture	Long term	129.00	-	-	-	-	-	-	-	-	-	[ICRA]A- (Stable); withdrawn	[ICRA]A- (Stable)
5	Non-convertible debenture	Long term	31.00	-	-	-	-	-	-	-	-	[ICRA]A- (Stable); withdrawn	[ICRA]A- (Stable)	[ICRA]A- (Stable)
6	Non-convertible debenture	Long term	81.00	-	-	-	-	[ICRA]A- (Stable); withdrawn	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
7	Non-convertible debenture	Long term	60.00	-	-	-	[ICRA]A- (Stable); withdrawn	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Non-convertible debentures	Simple
Subordinated debt	Very 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	Date of Issuance	Coupon Rate	Maturity Date	Rated Amount (Rs. crore)	Rating
INE139R08041^	**NCD**	Sep-10-2019	11.91%	Sep-9-2025	35.00	[ICRA]A (Stable)
INE139R07399[2]	**NCD**	Mar-16-2018	12.02%	Mar-16-2024	63.00	[ICRA]A (Stable)
INE139R08017	**NCD**	Mar-15-2017	13.85%	Mar-30-2023	50.00	[ICRA]A (Stable)
INE139R08058^	**NCD**	Sep-15-2016	13.25%	Sep-15-2025	55.00	[ICRA]A (Stable)
INE139R07258	**NCD**	Oct-6-2020	11.90%	Dec-6-2023	10.00	[ICRA]A (Stable)
INE139R07266	**NCD**	Jun-19-2020	11.40%	Jun-19-2023	30.00	[ICRA]A (Stable)
INE139R07274	**NCD**	Jun-30-2020	11.25%	Jun-30-2023	20.00	[ICRA]A (Stable)
INE139R07290	**NCD**	Jul-29-2020	11.50%	Jul-29-2023	20.00	[ICRA]A (Stable)
INE139R07282	**NCD**	Jul-31-2020	11.25%	Apr-21-2023	25.00	[ICRA]A (Stable)
INE139R08074[3]	**NCD**	Feb-11-2020	11.53%	Feb-11-2026	75.00	[ICRA]A (Stable)
INE139R08082	**NCD**	Dec-21-2021	10.50%	Dec-21-2023	45.00	[ICRA]A (Stable)
To be issued	**NCD**	NA	NA	NA	35.00	[ICRA]A (Stable)
To be issued	**NCD**	NA	NA	NA	145.00	[ICRA]A (Stable)
Unallocated	**NCD**	NA	NA	NA	1.50	[ICRA]A (Stable)
INE139R08108	**Subordinated debt**	Mar-31-2022	13.00%	Jun-30-2027	25.00	[ICRA]A (Stable)
INE139R08090	**Subordinated debt**	Mar-31-2022	13.00%	Sep-30-2027	30.00	[ICRA]A (Stable)
INE139R07233	**NCD**	Feb-6-2016	12.75%	May-16-2022	53.00	[ICRA]A (Stable); withdrawn
INE139R07308	**NCD**	Dec-8-2020	10.50%	Dec-2-2022	50.00	[ICRA]A (Stable); withdrawn
INE139R07324	**NCD**	Nov-13-2020	9.75%	May-13-2022	25.00	[ICRA]A (Stable); withdrawn
INE139R07332	**NCD**	Nov-13-2020	10.50%	May-13-2022	50.00	[ICRA]A (Stable); withdrawn
INE139R07340	**NCD**	Nov-13-2020	10.40%	May-13-2022	50.00	[ICRA]A (Stable); withdrawn
INE139R07357	**NCD**	Nov-19-2020	10.50%	May-19-2022	25.00	[ICRA]A (Stable); withdrawn
INE139R07365	**NCD**	Nov-13-2020	10.25%	May-13-2022	35.00	[ICRA]A (Stable); withdrawn

^ISINs have redeemed in October 2022

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

[2] *ISIN number has changed to INE139R07399 from INE139R07191*

[3] *ISIN number has changed to INE139R08074 from INE139R07316*

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