March 31, 2021

DMI Housing Finance Private Limited: [ICRA]AA- (Stable) assigned

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund Based	-	50.0	[ICRA]AA- (Stable); Assigned
Total Bank Facilities	**-**	**50.0**	

**Instrument details are provided in Annexure-1*

Rationale

To arrive at the rating, ICRA has taken a consolidated view of DMI Finance Private Limited (DFPL) and DMI Housing Finance Private Limited (DHFPL), referred to as the DMI Group, given the operational linkages between the two companies in addition to the common promoter, shared name and management oversight.

The assigned rating factors in the DMI Group's consistent track record of strong capitalisation, aided by regular equity infusions by the promoter i.e. DMI Limited. Following the equity infusion of about Rs. 2,700 crore during the five-year period ending December 2020, the Group's consolidated net worth stood at about Rs. 4,019 crore with a consolidated gearing of 0.6x as on December 31, 2020. Moreover, ICRA notes that over the longer term, the Group plans to maintain prudent capitalisation with a peak gearing of 2x. The assigned rating also draws comfort from the Group's track record of strong liquidity supported by low leverage and sizeable on-balance sheet liquidity. Moreover, a considerable proportion of the loan book has a residual tenor of up to 1 year. The available on-balance sheet liquidity of about Rs. 2,000 crore (as on December 31, 2020) is more than sufficient to take care of the debt-servicing obligations falling due in next one year.

While assigning the rating, ICRA has taken cognizance of the Group's moderate profitability indicators and the rising share of digital loans (small-ticket personal/consumption retail loans) in the overall portfolio mix. The foray into digital loans and affordable housing loans has led to improved granularity of the portfolio, which, in the past, was characterised by concentrated wholesale exposures primarily to real estate builders. As of December 31, 2020, digital loans constituted 50% of the total consolidated loan book of Rs. 4,640 crore, followed by wholesale loans (34%) and affordable housing finance loans (16%). While a higher proportion of digital/retail loans is a positive from a concentration risk perspective, the inherent vulnerability associated with the target borrower profile and unsecured nature of loans augments the portfolio vulnerability.

Nevertheless, ICRA draws comfort from the Group's systems and processes and expects it to report good risk-adjusted returns over the medium term. Further, while the Group has a relatively shorter track record of operations in the digital lending segment, it is improving with three years of operations and disbursements of over Rs. 9,500 crore. However, in this regard, it is noted that the Group's proforma asset quality indicators witnessed a deterioration in 9M FY2021. Asset quality pressure has primarily emerged in the digital lending segment wherein loans disbursed prior to April 2020 witnessed a spike in delinquencies. Nevertheless, comfort is drawn from the first loss default guarantee (FLDG) arrangements with the fintech partners wherein almost 2/3rd of the stressed pool is protected through FLDGs while the balance amount has already been provided for in 9M FY2021. Given the protection available in the form of FLDGs and provisions, an incremental impact on profitability is unlikely. Also, the originations done without FLDG protection have not witnessed a similar deterioration and fresh originations post April 2020 are performing satisfactorily with no uptick in delinquencies over the past two quarters.

Overall, the Group's ability to improve the profitability indicators from the current levels and grow the business while maintaining the underwriting standards and controlling the credit costs would be a key monitorable. At the same time, the ability to diversify the funding mix would be critical to grow the business. As for DHFPL, ICRA notes that on a standalone basis, the company's scale of operations is modest with assets under management of Rs. 746 crore as on December 31, 2020. Nonetheless, given the good market potential in affordable housing finance and the company's satisfactory, albeit short, track record of operations, ICRA expects it to grow as per the business plans with good asset quality and return indicators over the medium term.

Key rating drivers and their description

Credit strengths

Strong capitalisation with consolidated gearing of 0.6x on sizeable net worth – The Group's capitalisation has consistently remained strong, aided by regular equity infusions by the promoter i.e. DMI Limited. Following the equity infusion of over Rs. 1,800 crore during the four-year period ending March 2020, the Group's consolidated net worth stood at about Rs. 3,044 crore with a gearing of 1.0x and a total capital adequacy ratio of over 40% (for both DFPL and DHFPL) as on March 31, 2020. Further, the Group concluded the latest round of equity raise in April 2020, whereby about Rs. 942 crore was infused by South Korea's Nexon Co through DMI Limited. As a result, the Group's net worth, as of December 31, 2020, is estimated at Rs. 4,019 crore with a gearing of 0.6x. As for DHFPL at the standalone level, the net worth stood at Rs. 572 crore as of December 31, 2020 with a gearing of 0.9x.

While the existing capital base is sufficient to support the growth plans for the near to medium term, ICRA notes that the Group may need incremental capital to maintain a prudent capitalisation level over the longer term, especially given the growth plans for the digital lending and housing finance segments. Nevertheless, given the track record of the existing investors in extending support to the Group, ICRA expects support from the investors to be forthcoming as and when required. Further, ICRA notes that the Group plans to maintain prudent capitalisation over the longer term with a maximum gearing of 2x.

Strong liquidity profile – DFPL's asset liability maturity (ALM) profile is characterised by positive cumulative mismatches in the near-and-medium-term buckets, given the low leverage and sizeable proportion of the loan book with a residual tenor of up to 1 year. This, along with sizeable cash and liquid investments of about Rs. 1,660 crore at the standalone level, augurs well for the liquidity profile. Similarly, DHFPL's ALM profile is characterised by positive cumulative mismatches in the near-and-medium-term buckets, given the low leverage and sizeable on-balance sheet liquidity (about Rs. 338 crore as on December 31, 2020). Furthermore, the track record of regular support from the promoter, in terms of equity infusion, provides comfort. Moreover, while the Group is currently maintaining enhanced on-balance sheet liquidity given the challenging operating environment, it endeavours to maintain on-balance sheet liquidity equivalent to six months of the total outflows at all times.

ICRA, however, notes that the Group's dependence on external borrowings from banks, mutual funds and other domestic investors has remained limited compared to the current scale of operations, given the regular fund inflow (equity as well as debt) from the promoter group. Furthermore, the Group's comfortable liquidity position has not yet required it to test the securitisation markets. Going forward, it would be imperative for the Group to augment the lender base, diversify the borrowing profile and establish financial flexibility, given the growing scale. At the same time, the ability to borrow funds for a prudent tenure at competitive rates would be a key determinant of the profitability going forward.

Credit challenges

Rising share of digital retail loans; high portfolio vulnerability could keep asset quality indicators volatile – Till FY2018, the Group was mainly engaged in secured corporate lending, largely to real estate builders. However, it subsequently shifted its focus to the small-ticket personal/consumption retail loan and affordable housing finance segments with a sharp growth recorded since then. The Group's consolidated loan book, as on December 31, 2020, was about Rs. 4,640 crore with digital lending accounting for 50% and affordable housing loans for 16% with the balance 34% comprising wholesale/real estate loans. The digital lending business is completely technology-driven with API-based origination, underwriting and loan management systems. The underwriting is based on an algorithm, which uses certain data points for arriving at the loan eligibility with minimum manual intervention and deviations. While such algorithms are regularly updated based on the past performance of the loans with new variables added from time to time, the assumptions for parameters like default rates are critical for the underwriting of loans with expected credit losses, which, in turn, affect the asset quality, credit costs and profitability. Also, while a higher proportion of digital/retail loans is a positive from a concentration risk perspective, the inherent vulnerability associated with the target borrower profile and unsecured nature of loans augments the portfolio vulnerability. Nevertheless, ICRA draws comfort from the Group's systems and processes and expects it to grow the business volumes while maintaining control on the credit costs.

Going forward, the Group's ability to demonstrate the effectiveness of its credit underwriting policies and partnerships and keep the asset quality indicators under control through economic cycles will be imperative. In this regard, it is noted that while the reported GNPA stood at 3.0% as on December 31, 2020 compared to 3.8% as on March 31, 2020, the Group's proforma asset quality indicators witnessed a deterioration in 9M FY2021 with an elevated proforma GNPA %. The asset quality pressure has primarily emerged in the digital lending segment wherein loans disbursed prior to April 2020 witnessed a spike in delinquencies. Nevertheless, ICRA takes comfort from the FLDG-backed model for most of the existing partnerships (though the share of FLDG-backed originations is expected to decline considerably going forward) and the high granularity of this portfolio due to the smaller ticket sizes. This enables the diversification of the risk while the higher yields earned help mitigate the inherent risk in the target segment. Also, herein almost 2/3rd of the stressed pool is protected through FLDGs while the balance has already been provided for in 9M FY2021. Given the protection available in the form of FLDGs and provisions, an incremental impact on profitability is unlikely. ICRA also notes that the originations without FLDG protection have not witnessed a similar deterioration and fresh originations post April 2020 are performing satisfactorily with no uptick in delinquencies over the past two quarters.

As for DHFPL at the standalone level, the loan book stood at Rs. 746 crore as on December 31, 2020 with an average ticket size of about Rs. 12 lakh and a geographical footprint of about 39 branches across 9 states (though 3 states, i.e. Uttar Pradesh, Rajasthan and Madhya Pradesh, account for 2/3rd of the portfolio). While home loans account for 85% of the loan book with the salaried segment (including pensioners) accounting for 87% of this, the balance comprises loan against property (LAP; 12%) and corporate loans (3%). Herein, the reported GNPA% was comfortable at 0.2% as on December 31, 2020. However, while the Group has demonstrated good control over the asset quality in the affordable housing finance segment, this loan book remains relatively less seasoned and performance across economic cycles remains to be established.

Subdued profitability trajectory – As the Group's digital lending and affordable housing finance operations are in the ramp-up phase, the operating expenses remain high. The Group's operating cost (including sizeable commissions paid to fintech partners) as a proportion of average total assets (ATA) increased to over 4.5% in FY2020 from less than 3% till FY2017. Further, the emergence of asset quality pressures increased the credit cost to 3% of ATA in FY2020 and 1.8% of ATA in FY2019 from less than 1% in prior years. As a result, while the Group's lending spread has increased to about 9%, the consolidated return on assets and return on equity remained subdued at 2.30%[1] and 4.25%[2], respectively. In 9M FY2021 as well, the reported profitability remained subdued with a return on assets and return on equity of 1.1% and 2.2%, respectively, due to elevated credit costs of 3.2% and operating costs (including sizeable commissions paid to fintech partners) of 4.5%. Nevertheless, as the operating expenses stabilise with economies of scale and the outgo on account of commissions declines with the increased share of cross selling, the profitability is expected to improve, provided funds are raised at competitive rates and good control is maintained on slippages by demonstrating the effectiveness of the credit underwriting policies.

DHFPL reported a profit after tax (PAT) of Rs. 23.1 crore at the standalone level in FY2020 on a gross asset base of Rs. 1,119 crore. It is estimated to have achieved a PAT of Rs. 22.1 crore in 9M FY2021 on an asset base of Rs. 1,127 crore as on December 31, 2020. The profitability, however, remains subdued with a return on assets and return on equity of 2.6% and 5.2%, respectively, in 9M FY2021. Nonetheless, given the good market potential in affordable housing finance and the satisfactory, albeit short, track record of the company's operations, ICRA expects it to grow as per the business plans with good asset quality and return indicators over the medium term.

[1] *Would be higher if adjusted for timing of fund raise, especially the sizeable debt raised in February 2020*

[2] *Also gets constrained by low financial leverage*

Liquidity position: Strong

DFPL's ALM profile is characterised by positive cumulative mismatches in the near-and-medium-term buckets, given the low leverage and sizeable proportion of the loan book with a residual tenor of up to 1 year. As on September 30, 2020, the company's ALM reflected debt maturities of Rs. 75 crore for the 12-month period ending September 30, 2021, against which its scheduled inflows were Rs. 2,169 crore. This, along with sizeable cash and liquid investments of over Rs. 1,660 crore at the standalone level (equivalent to ~85% of borrowings as on December 31, 2020), augurs well for the liquidity profile. Further, the track record of regular support from the promoter, in terms of equity infusions, provides comfort.

Similarly, DHFPL's ALM profile is characterised by positive cumulative mismatches in the near-and-medium-term buckets, given the low leverage and sizeable on-balance sheet liquidity. As on September 30, 2020, the company's ALM reflected debt maturities of Rs. 38 crore for the 12-month period ending September 30, 2021, against which its scheduled inflows were Rs. 35 crore (performing advances). This, along with sizeable cash and liquid investments of about Rs. 338 crore (equivalent to 66% of borrowings as on December 31, 2020), augurs well for the liquidity profile.

Rating sensitivities

Positive factors – A well-established track record of strong profitability led by good control on the asset quality and operating efficiencies, while sustaining the current approach towards leverage and liquidity, will remain imperative for a rating upgrade in the medium to long term.

Negative factors – The rating could come under pressure if the leverage increases beyond a gearing of 2x or asset quality pressures adversely impact the company's earnings profile on a sustained basis. Pressure on the rating could also emerge if the liquidity profile weakens.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA's Credit Rating Methodology for Non-Banking Finance Companies ICRA's Credit Rating Methodology for Housing Finance Companies Financial Consolidation and Rating Approach
Parent/Group Support	-
Consolidation/Standalone	Consolidation; To arrive at the rating, ICRA has taken a consolidated view of DFPL and DHFPL, referred to as the DMI Group, given the operational linkages between the two companies in addition to the common promoter, shared name and management oversight.

About the company

DMI Housing Finance Private Limited (DHFPL), incorporated in 2011, is a private financial services company registered as a housing finance company (HFC). It started lending operations in FY2014 and primarily focusses on providing home loans and loan against property (LAP) to borrowers seeking affordable housing. The company's loan book stood at Rs. 746 crore as on December 31, 2020 with an average ticket size of about Rs. 12 lakh and a geographical footprint of about 39 branches across 9 states (though 3 states, i.e. Uttar Pradesh, Rajasthan and Madhya Pradesh, account for 2/3rd of the portfolio). While home loans account for 85% of the loan book with the salaried segment (including pensioners) accounting for 87% of this, the balance comprises LAP (12%) and corporate loans (3%). While DHFPL used to be a subsidiary of DFPL (till FY2018), DMI Limited, Mauritius now directly holds an 86.5% stake in the company (as of December 31, 2020).

DHFPL reported a PAT of Rs. 23.1 crore in FY2020 on a gross asset base of Rs. 1,119 crore as on March 31, 2020 against a PAT of Rs. 1.6 crore in FY2019 on a gross asset base of Rs. 621 crore. It is estimated to have achieved a PAT of Rs. 22.1 crore in 9M FY2021 on an asset base of Rs. 1,127 crore as on December 31, 2020. As on March 31, 2020, DHFPL's reported capital adequacy was 79.1%.

DMI Finance Private Limited

DFPL, incorporated in 2008, is a private financial services company registered as a non-banking financial company (NBFC) with the Reserve Bank of India (RBI). While it was mainly engaged in secured corporate lending (largely to real estate builders) till a few years ago, it has shifted focus to digital lending wherein it provides consumption loans, personal loans and MSME loans. This is a completely digital technology-driven business with API-based origination, underwriting and loan management systems. Herein, DFPL predominantly works through front-end partnerships with other fintech companies, original equipment manufacturers (OEMs) and technology-driven aggregators. As on December 31, 2020, consumer loans accounted for 59% (PY: 40%) of the Rs. 3,894-crore loan book with the wholesale real estate lending booking accounting for a 28% share and the non-real estate wholesale loan book accounting for the balance.

DMI Limited, Mauritius holds a 74.6% stake in DFPL (as of December 31, 2020). DMI Limited, Mauritius is, in turn, backed by New Investment Solution (NIS), a Zurich-based alternative asset manager with over $2 billion of deployed capital. NIS is led by Takashi Sato, who was Head of Private Wealth and Asset Management at Nomura Bank (Europe). The fund focusses on Japanese equities, US asset-backed debt and the emerging market debt.

DFPL reported a consolidated profit after tax (PAT) of Rs. 98.4 crore in FY2020 on a gross asset base of Rs. 5,355 crore as on March 31, 2020 against a PAT of Rs. 77.3 crore in FY2019 on a gross asset base of Rs. 3,368 crore. DFPL is estimated to have achieved a PAT of Rs. 35.6 crore in 9M FY2021 on an asset base of Rs. 5,829 crore as on December 31, 2020. As on December 31, 2020, DFPL's reported capital adequacy was 59.1% (44.0% as on March 31, 2020).

Key financial indicators

Amounts in Rs. crore	DHFPL			DFPL + DHFPL		
	FY2019	FY2020	9M FY2021	FY2019	FY2020	9M FY2021
	Audited	Audited	Provisional	Audited	Audited	Provisional
PAT	2	23	22	78.9	121.5	57.7
Net Worth	527	551	572	2713.8	3043.8	4018.9
Gross Loan Book	434	795	746	2,951.2	4,520.3	4,640.3
Total Gross Assets	621	1,119	1,127	3,962.0	6,474.1	6,956.3
Return on Avg. Net Worth (%)	0.5%	4.3%	5.2%	4.1%	4.2%	2.2%
Gearing (times)	0.1	1.0	0.9	0.4	1.0	0.6
CRAR (%)	132.3%	79.1%	NA	NA	NA	NA
Gross NPA (%)	0.1%	0.2%	0.2%	2.5%	3.8%	3.0%
Net NPA (%)	0.0%	0.0%	0.2%	1.1%	1.6%	1.1%
Net NPA/Net Worth	0.0%	0.0%	0.2%	1.2%	2.3%	1.2%

Source: *DFPL, DHFPL, ICRA research*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Mar 31, 2021	FY2020	FY2019	FY2018
						-	-	-
1	Long-term Fund Based	Long Term	50.0	-*	**[ICRA]AA- (Stable)**	-	-	-

Source: *ICRA research; *As of January 31, 2021*

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance/ Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund-based bank facility	Dec 2020	NA	Jan 2028*	50.0*	[ICRA]AA- (Stable)

Source: *ICRA research; *For Rs. 25 crore that stood disbursed up to March 25, 2021*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
DMI Housing Finance Private Limited (DHFPL)	Rated Entity	Full Consolidation
DMI Finance Private Limited (DFPL)	Fellow Subsidiary	Full Consolidation
DMI Management Services Private Limited (DMSPL)	100% Subsidiary of DFPL	Full Consolidation
DMI Capital Private Limited (DCPL)	100% Subsidiary of DFPL	Full Consolidation

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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