CARE Ratings
Professional Risk Opinion

CARE/ARO/RL/2018-19/1722

Mr. Jayendra Patel
Vice Chairman & Managing Director
Arman Financial Services Limited
502-503, Sakar III, Opp. Old High Court,
Off Ashram road, Ahmedabad,
Gujarat – 380 014

September 12, 2018

Confidential

Dear Sir,

Credit rating for proposed Non-Convertible Debenture issue

Please refer to your request for rating of proposed long-term non-convertible debenture (NCD) issue aggregating to Rs.28.00 crore of your company.

2. The following ratings have been assigned by our Rating Committee:

Instrument	Amount (Rs. crore)	Rating[1]	Rating Action
Proposed Non-Convertible Debenture issue	28.00 (Rupees Twenty Eight crore only)	**CARE BBB+; Stable [Triple B Plus; Outlook Stable]**	**Assigned**

3. Please arrange to get the rating revalidated, in case the proposed issue is not made within a period of **six months** from the date of our initial communication of rating to you (that is September 11, 2018).

4. In case there is any change in the size or terms of the proposed issue, please get the rating revalidated.

5. Please inform us the below-mentioned details of issue immediately, but not later than 7 days from the date of placing the instrument:

Instrument type	ISIN	Issue Size (Rs. crore)	Coupon Rate	Coupon Payment Dates	Terms of Redemption	Redemption date	Name and contact details of Debenture Trustee	Details of top 10 investors

[1] *Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

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6. Kindly arrange to submit to us a copy of each of the documents pertaining to the NCD issue, including the offer document and the trust deed.
7. The rationale for the rating will be communicated to you separately. A write-up (press release) on the above rating is proposed to be issued to the press shortly, a draft of which is enclosed for your perusal as Annexure II. We request you to peruse the annexed document and offer your comments if any. We are doing this as a matter of courtesy to our clients and with a view to ensure that no factual inaccuracies have inadvertently crept in. Kindly revert as early as possible. In any case, if we do not hear from you by September 13, 2018, we will proceed on the basis that you have no any comments to offer.
8. CARE reserves the right to undertake a surveillance/review of the rating from time to time, based on circumstances warranting such review, subject to at least one such review/surveillance every year.
9. CARE reserves the right to revise/reaffirm/withdraw the rating assigned as also revise the outlook, as a result of periodic review/surveillance, based on any event or information which in the opinion of CARE warrants such an action. In the event of failure on the part of the entity to furnish such information, material or clarifications as may be required by CARE so as to enable it to carry out continuous monitoring of the rating of the debt instrument, CARE shall carry out the review on the basis of best available information throughout the life time of such instrument. In such cases the credit rating symbol shall be accompanied by "ISSUER NOT COOPERATING". CARE shall also be entitled to publicize/disseminate all the afore-mentioned rating actions in any manner considered appropriate by it, without reference to you.
10. Users of this rating may kindly refer our website www.careratings.com for latest update on the outstanding rating.
11. CARE ratings are **not** recommendations to buy, sell or hold any securities.

If you need any clarification, you are welcome to approach us in this regard. We are indeed, grateful to you for entrusting this assignment to CARE.

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Thanking you,
Yours faithfully,

[Anuja Parikh]
Manager
anuja.parikh@careratings.com

[Harshveer Trivedi]
Sr. Manager
harshveer.trivedi@careratings.com

Encl.: As above

Disclaimer

CARE's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CARE has based its ratings/outlooks on information obtained from sources believed by it to be accurate and reliable. CARE does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CARE have paid a credit rating fee, based on the amount and type of bank facilities/instruments.
In case of partnership/proprietary concerns, the rating/outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

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Annexure I

Details of Rated Instrument

Particulars	Proposed terms of the issue
Issuer	Arman Financial Services Limited
Size of the issue	Rs.28 crore*
Mode of the issue	Private Placement
Proposed Subscriber	AAV Sarl, Luxemborg
Deemed date of allotment	August 3, 2018
Maturity date	February 3, 2022
Coupon	12.60% per annum; fixed
Frequency of interest payment	Semi-annually on February 17 and August 17 each year, for the first time on February 17, 2019, and on maturity date
Redemption	August 17, 2021: 50% of outstanding principal amount February 3, 2022: 100% of outstanding principal amount
Put Option	Nil

**INR equivalent of USD 4 million assuming currency rate of Rs.70 per USD*

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Annexure II

Draft Press Release

Arman Financial Services Limited

Ratings

Facilities/Instruments	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	39.00	**CARE BBB+; Stable [Triple B Plus; Outlook: Stable]**	Revised from CARE BBB; Stable [Triple B; Outlook: Stable]
Total	**39.00 (Rupees Thirty Nine crore only)**		
Proposed Non-Convertible Debenture Issue	28.00 (Rupees Twenty Eight crore only)	**CARE BBB+; Stable [Triple B Plus; Outlook: Stable]**	Assigned

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

For arriving at the rating, CARE has taken a consolidated view of Arman Financial Services Limited (AFSL), which includes its wholly owned subsidiary, Namra Finance Ltd. (NFL) engaged in micro finance lending, apart from the standalone financing business of AFSL. This is on account of the operational, managerial and financial linkages between the two entities.

The revision in AFSL's rating takes into account robust growth in its loan portfolio over the last one year with increased penetration in existing geographies & products along with addition of MSME loan product and increasing geographical diversification of operations with commencement of operations in Uttarakhand which however, still remains restricted to 5 states. The rating also takes cognizance of fund infusion of Rs.50 crore by a private equity player in April 2018 to further support the growth in its loan portfolio.

The rating continues to derive strength from AFSL's established track record of operations along-with experienced & professional management as well as diversified operations across three different loan segments, viz. vehicle finance, MSME lending and micro-finance. The rating further derives strength from AFSL's comfortable capital adequacy ratio (CAR), moderate profitability indicators (net interest margin and ROTA) which improved in Q1FY19 as well as its expanding resource base.

[1] *Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

The rating continues to be constrained on account of moderation in AFSL's asset quality as on FY18 end due to impact of demonetization, limited track record of operations in new geographies and products, risks associated with unsecured lending in microfinance and MSME loans, presence in a highly competitive industry and regulatory risk pertaining to the microfinance business.

AFSL's ability to further expand its loan portfolio through greater geographical and product diversification while improving its asset quality and profitability along with timely tie-up of envisaged funding from banks and financial institutions to support growth in business would be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Healthy growth in loan portfolio during FY18: AFSL's loan portfolio more than doubled during FY18 with healthy growth witnessed in all three segments with release of pent-up demand post wearing off of the impact of demonetization. Branch network and operational set-up created prior to demonetization also acted as catalyst for robust growth in loan portfolio during the year. Further, AFSL shifted its entire loan disbursement to cashless mechanism, which is expected to provide it with better control over the process.

Fund infusion in April 2018 from private equity player to enable further growth in loan portfolio: AFSL raised Rs.50 crore from a private equity player in April 2018 through issue of compulsory convertible debentures (CCDs). This fund infusion would provide it with the required equity capital to support the growth in its loan portfolio over the next couple of years, while it would be required to raise borrowings in line with its loan disbursements.

Diversified operations across three segments: AFSL on a standalone basis undertakes vehicle finance and MSME lending, while the microfinance lending is done through NFL, its wholly owned subsidiary. All these three segments witnessed healthy growth in disbursements during FY18. Microfinance lending continued to be the largest segment for AFSL constituting 68% of its total loan portfolio as on March 31, 2018.

Increasing geographical diversification: AFSL expanded its operations to Uttarakhand in FY18 while increasing its penetration in existing states of Madhya Pradesh, Uttar Pradesh and Maharashtra which resulted in reduced concentration of loan portfolio in Gujarat from 81% in

FY17 to 57% in FY18. As on March 31, 2018, AFSL had presence across 53 districts in these 5 states with a network of 107 branches.

Established track record of operations along-with experienced and professional management: AFSL is in the finance business since 1992 and has demonstrated a long track record of operations through various business cycles. The company is promoted by Mr. Jayendra Patel who has a wide industry experience of more than two decades. He is supported by Mr. Aalok Patel, son of Mr. Jayendra Patel, is also on the Board of the Directors of the company and is actively involved in the business. In August 2018, Mr. Alok Prasad joined as the Chairman on the Board of Directors of AFSL. Mr. Prasad has more than 35 years of experience in regulatory, banking and financial services.

Comfortable CAR with moderate profitability: AFSL's CAR stood comfortable at 23.49% as on March 31, 2018 and improved further to 28.02% as on June 30, 2018 with raising of funds through CCDs in April 2018. Though AFSL's ROTA moderated by around 93 bps y-o-y to 2.15% during FY18 (primarily due to higher provisioning as well as interest expense incurred during the year), it improved substantially to 3.77% in Q1FY19 with normalization of expenses as well as improvement in asset quality.

Key Rating Weaknesses

Deterioration in asset quality due to impact of demonetization, but normalization witnessed during recent months: AFSL's asset quality deteriorated in FY18 with gross NPA increasing to 1.69% as on March 31, 2018 from 1.44% as on March 31, 2017, reflecting the impact of demonetization on its borrowers, which are primarily engaged in cash based economy. Transition in NPA recognition norms from 120 days in FY17 to 90 days in FY18 for its two-wheeler business also contributed to the higher reported delinquency levels. However, the portfolio quality started stabilizing and even improving, with around 0.50% of gross NPA for MFI loans disbursed post demonetization (from April 2017) as on June 30, 2018 and reduction in PAR > 90 days for other businesses from 6.00% as on March 31, 2017 to 4.60% as on March 31, 2018.

Limited track record of operations in its new geographies and products: AFSL commenced microfinance lending operations in Uttar Pradesh, Maharashtra and Uttarakhand during the last two years. A good understanding of the local economy and its dynamics is required for engaging in a successful microfinance business, given the unsecured nature of lending as well as the target borrower set. Further, AFSL commenced unsecured MSME lending in Gujarat and

Madhya Pradesh during end FY17 which scaled up sizably in FY18 and Q1FY19. Collectively, both these translated into limited track record for AFSL in its new geographies & products and its performance in terms of profitability and asset quality is yet to be established.

Risks associated with unsecured lending: Around 79% of the outstanding loan portfolio of AFSL as on June 30, 2018 was contributed by microfinance and MSME lending. The loans in both these business segments are unsecured in nature translating into losses in case of any delinquency, as there is no asset which can be sold to recover the pending loan amounts.

Presence in a competitive and highly regulated industry albeit healthy growth prospects: The SHG - Bank Linkage Program (SBLP) which was launched in 1992 on a pilot basis has grown significantly. SHGs have enabled millions of poor household access to sustainable financial services from the banking system. Apart from MFIs, other models of microfinance like non-governmental organizations (NGOs), co-operatives, trusts etc. have also grown significantly in recent years. AFSL also faces competition from unorganized sector lending. However, growth prospect of micro-finance business in India continues to remain good given the market potential.

Analytical Approach: Consolidated

A consolidated approach has been considered for analysis for Arman Financial Services Ltd. (AFSL) and Namra Finance Ltd. (NFL) due to the following:

- NFL is a wholly owned subsidiary of AFSL
- Both entities are engaged in similar line of business (lending)
- Both entities operate under common management

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology: Factoring Linkages in Ratings
Rating Methodology - Non Banking Financial Companies
Financial Ratios-Financial Sector

About the Company

Promoted by Mr. Jayendra Patel, AFSL is a Non-Deposit taking Non-Banking Financial Company (NBFC) registered with Reserve Bank of India. Initially, AFSL was engaged in the business of two-wheeler financing and microfinance lending business through Joint Liability Group (JLG) model. In compliance with RBI directions, AFSL promoted NFL as its wholly owned subsidiary to carry

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out microfinance lending. NFL received NBFC – Micro Finance Institution (MFI) license from RBI on February 14, 2013 and from May 2013, entire new microfinance lending was carried out by NFL. In March 2017, AFSL also commenced MSME lending business.

AFSL, on a consolidated basis, operates across 5 states i.e. Gujarat, Madhya Pradesh, Maharashtra, Uttar Pradesh and Uttarakhand covering 53 districts through a network 127 branches as on March 31, 2018. Microfinance lending is presently the largest business segment for AFSL constituting 68% of the outstanding loan portfolio while the balance was from two-wheeler loans (21%) and MSME loans (11%)

Brief consolidated financials of AFSL are tabulated below:

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	53.59	80.03
PAT	6.32	7.30
Interest coverage (times)	1.44	1.27
Total Assets	214.64	462.71
Net NPA (%)	1.31	1.60
ROTA (%)	3.09	2.15

A: Audited;

During Q1FY19, on a consolidated basis, AFSL reported a total income of Rs.29.15 crore with a PAT of Rs.4.61 crore as against a total income of Rs.13.97 crore and a PAT of Rs.0.94 crore during Q1FY18.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History (Last three years): Please refer Annexure-2

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Analyst Contact
Name: Mr. Harshveer Trivedi
Tel: 079 – 4026 5610
Cell: 85111 90020
Email: harshveer.trivedi@careratings.com

About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over nearly two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	39.00	CARE BBB+; Stable
Debentures-Non Convertible Debentures (Proposed)	NA	12.60% p.a. fixed	NA	28.00	CARE BBB+; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Cash Credit	LT	39.00	CARE BBB+; Stable	-	1)CARE BBB; Stable (05-Oct-17)	1)CARE BBB (29-Aug-16)	1)CARE BBB- (18-Sep-15)
2.	Debentures-Non Convertible Debentures	LT	28.00	CARE BBB+; Stable	-	-	-	-

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