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STRUCTURED FINANCE

Collection efficiency of securitised retail pools nears pre-second wave level; future Covid waves remain an event risk

SEPTEMBER 2021

Highlights

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The monthly collection efficiency increased by 8-17% in July over the May 2021 level across the asset classes in ICRA-rated securitised pools. Consequently, the incremental slippages in the softer and harder buckets have seen a decline.

The collections in August 2021 are likely to have shown further improvement as the operational activities are on the path of achieving near normalcy levels with the rising share of vaccinated population and eased restrictions.

- The average collection efficiency in ICRA-rated securitised retail pools originated by the NBFCs and the HFCs continue to improve following the easing of movement restrictions / lockdowns.
- The increase in monthly collection efficiencies in July 2021 was by 8-17% over the May 2021 level across the asset classes.
- While the Housing loans (HL) and Loan against property (LAP) remained the least impacted and were quick to recover to the March 2021 level, the monthly collections in commercial vehicle (CV) loans, SME and microfinance loans also rebounded quickly to >90% levels in July 2021 from the lows seen in May 2021.
- The collections in retail pools securitized, post the first wave (i.e. September 2020), especially for the unsecured SME and microfinance loan pools, continued to be better than the pools originated prior to the same period.
- The incremental slippages have reduced in July 2021 across asset classes, as the originators have reported lower bounce rates in their portfolio led by the improving collections, leading to subsiding asset quality concerns.
- ICRA does not foresee any immediate decline in the collection efficiencies of the retail pools. While the threat of another wave of Covid infections remains, ICRA expects that the past experience would make the State/Central Governments as well as the companies better equipped to handle such an event to ensure least disruption to economic activities.
- For ICRA-rated securitisation transactions, ICRA maintains a ‘Stable’ outlook as the credit enhancements are sufficient to meet investor payouts in case of lower collections for a few months.

Material recovery in collection efficiency across asset classes post May 2021

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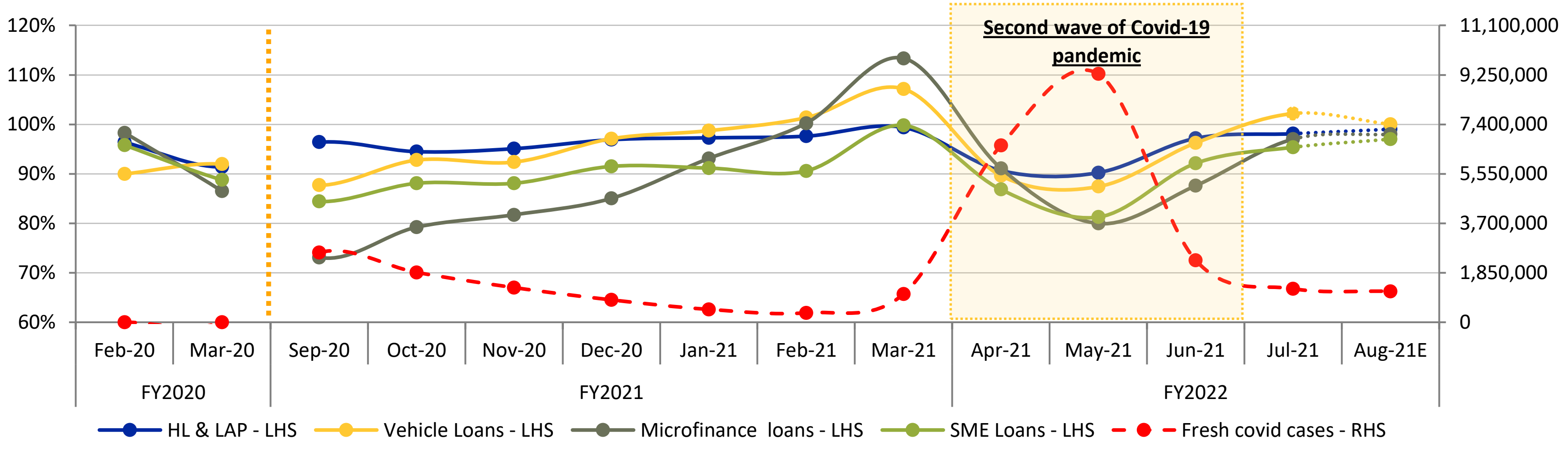
Exhibit: ICRA-rated pools' monthly collection efficiency and trend in fresh Covid cases



- The collection efficiency in ICRA-rated securitised pools originated by the NBFCs and the HFCs continued to rebound in July, on account of focused collection activities of the lenders further supported by the receding movement restrictions / lockdowns in most states affected by the Covid-19 pandemic. Consequently, the incremental slippages in the softer and harder buckets have seen a decline.
- Basis our discussions and lower bounce rates being reported by several originators in their portfolio for August 2021 month, the collections in August 2021 would also have shown continued improvement as the operational activities are close to achieving normalcy levels with the rising share of vaccinated population and eased restrictions.
- ICRA does not foresee any material credit pressures on its rated securitisation transaction though any further rise in Covid infections would be an event risk. The presence of cash collateral and excess interest spread enhances liquidity in the pools and buffer to absorb the increase in losses.

Source: ICRA Research, CEIC, Aug-21E represents estimated collection numbers, Monthly collection efficiency = (current collections + overdue collections)/current billings

Lower infections and rising vaccinated population bode well for business activities

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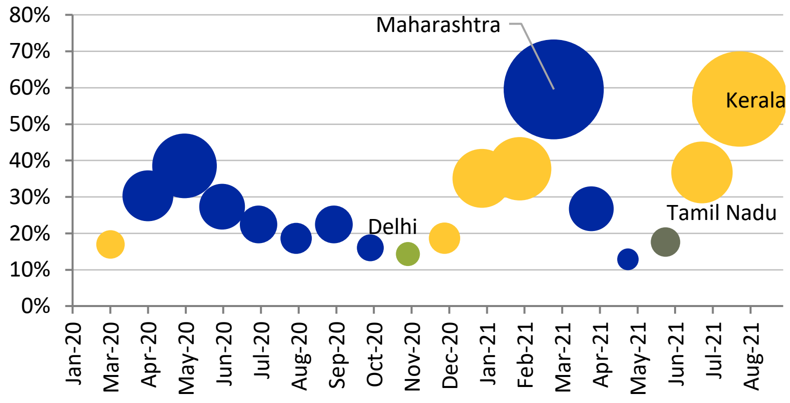
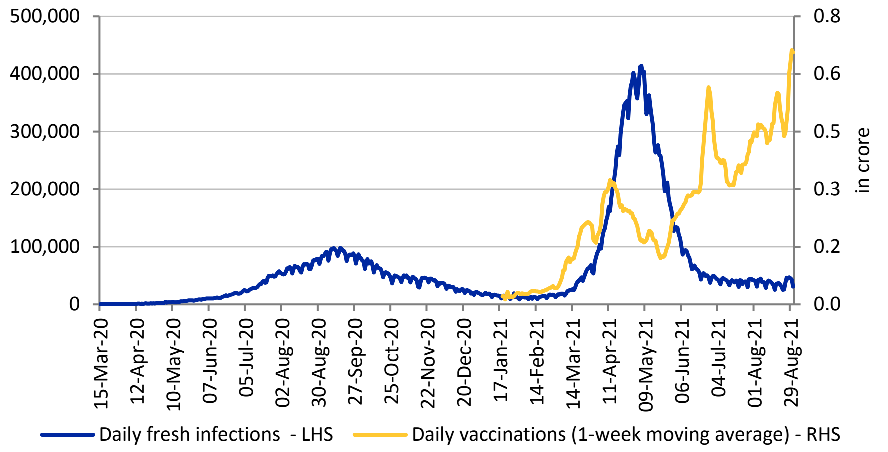
Exhibit: Top state contributing to fresh Covid-19 infections each month



Source: CEIC

- Kerala continues to be the top state contributing majority of fresh Covid infections in August 2021.
- The fresh infections outside of Kerala continue to remain low, post peaking in May 2021.

Exhibit: Fresh infections and daily vaccination in India



Source: CEIC

- With the eased restrictions and increased share of population (~60 crore) receiving vaccination (at least one dose) as of August 2021, the business and collection activities of lenders have achieved near normalcy levels. The high vaccination coverage could reduce the possibility of future rise in Covid infections.

Collection efficiencies and delinquencies | HL & LAP pool performance

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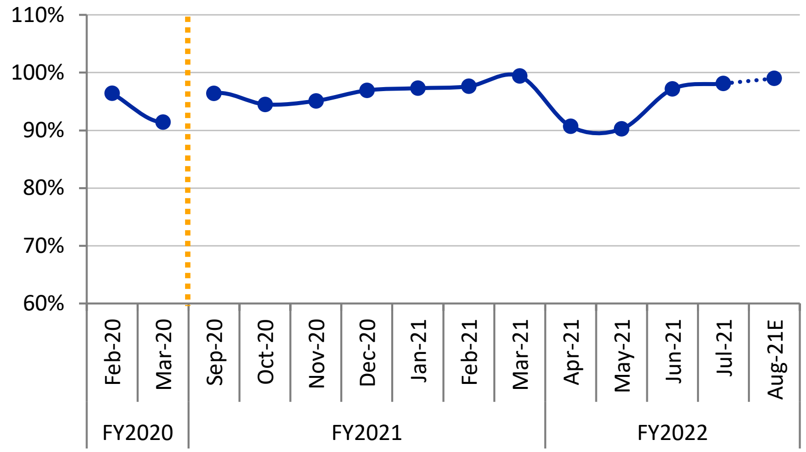
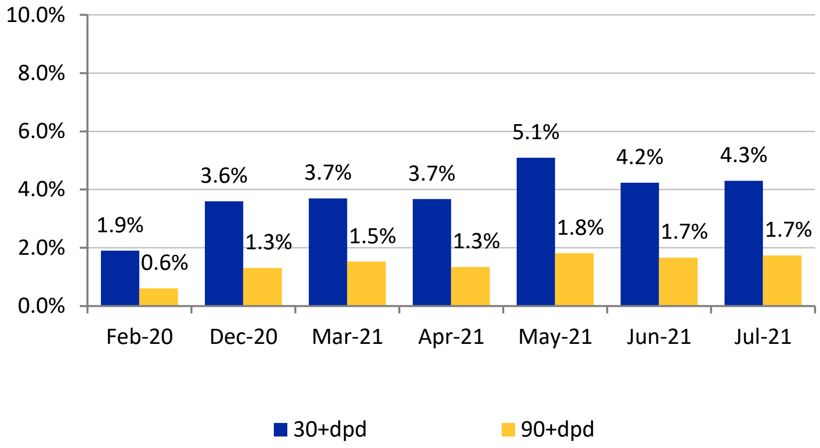
Exhibit: Monthly collection efficiency trend in ICRA-rated HL & LAP pools



Source: ICRA Research, Aug-21E represents estimated numbers,
Monthly collection efficiency = (current collections + overdue collections)/current billings

- Housing loans (HL) and loans against property (LAP) pools have demonstrated robust performance as the collections witnessed the swiftest recovery in June 2021 and remained sturdy in July 2021 post seeing a drop in May.
- Presence of online collection practices, association of the borrower with the underlying collateral and the priority given by the borrowers to repay such loans are the key drivers of the recovery in collections.

Exhibit: Delinquencies in ICRA-rated HL & LAP pools

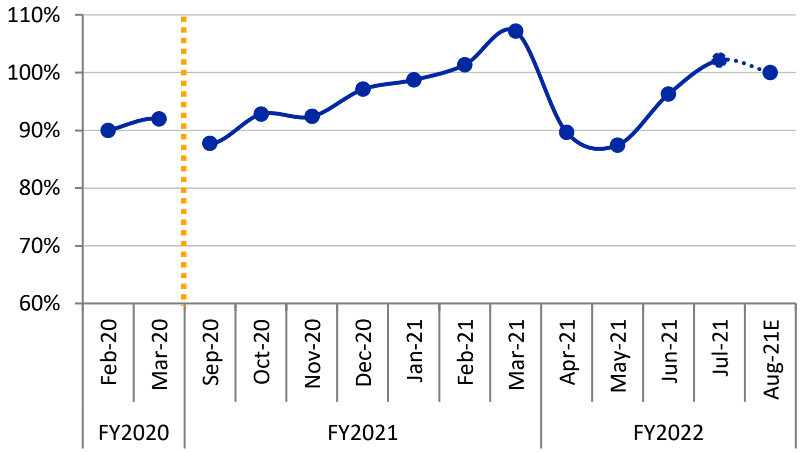


Source: ICRA Research, dpd – days past due

- With the collections returning to normal levels in July 2021, the delinquencies have witnessed marginal reduction. ICRA believes that HL & LAP pools are expected to remain healthy in near term provided there are no immediate widespread restrictions / lockdowns.

Collection efficiencies and delinquencies | CV loan pool performance

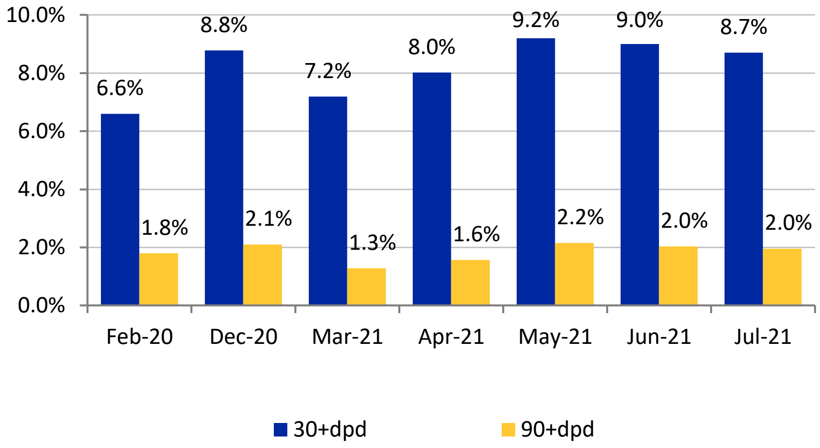
Exhibit: Monthly collection efficiency trend in ICRA-rated Vehicle loan pools



Source: ICRA Research, Aug-21E represents estimated numbers,
Monthly collection efficiency = (current collections + overdue collections)/current billings

- The ICRA-rated vehicle loan pools include tractor and construction equipment sub-pools as well. The collection efficiency of the vehicle loan pools rebounded in July 2021 led by eased movement restrictions enabling elevated collection efforts of the lenders. The repayment capability of the borrowers improved due to resumption in the business of the transport operators on the back of higher inter/intra-state movements.
- Also, the performance of our rated vehicle loan pools has remained healthy due to the minimal presence of highly affected passenger vehicle loans (such as buses).

Exhibit: Delinquencies in ICRA-rated Vehicle loan pools

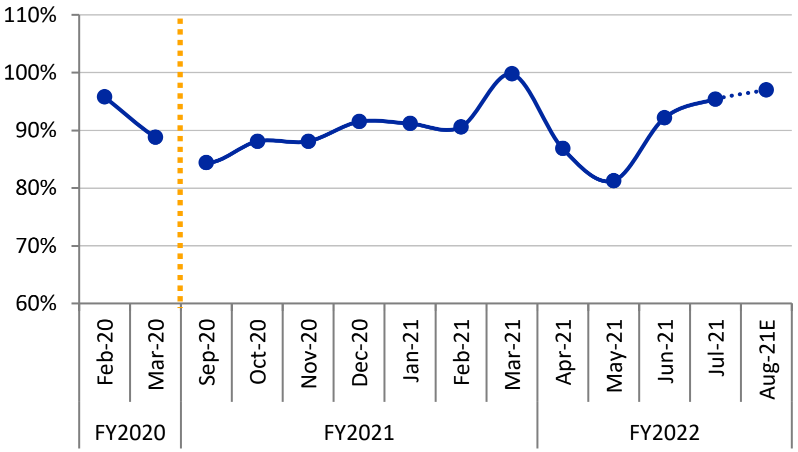


Source: ICRA Research, dpd – days past due

- Consequently, the slippages in softer and harder buckets have witnessed drop post May 2021. The recovery from the delinquent borrowers in CV loans can still be expected due to the presence of collateral with eventual losses being comparatively lower.

Collection efficiencies and delinquencies | SME loan pool performance

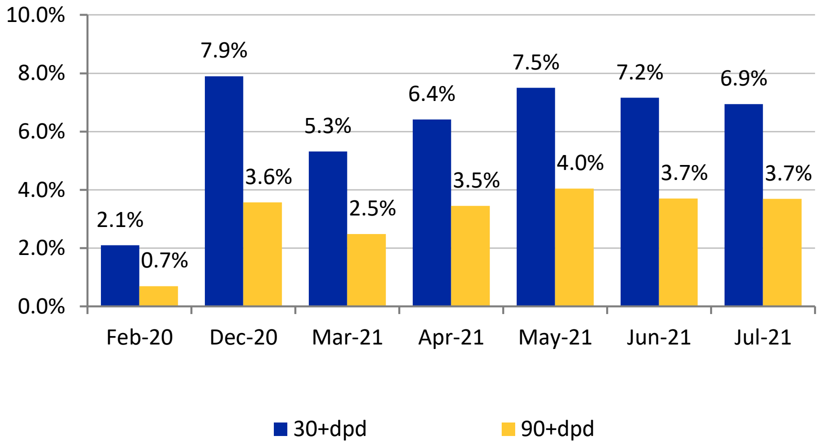
Exhibit: Monthly collection efficiency trend in ICRA-rated SME loan pools



Source: ICRA Research, Aug-21E represents estimated numbers,
Monthly collection efficiency = (current collections + overdue collections)/current billings

- With the easing restrictions on the opening of local establishments coupled with the pick-up in consumer demand, the cash flows of the borrowers and businesses have improved post May 2021 and consequently the loan repayment ability of the SME borrowers has improved leading to recovery in collection efficiency.
- The SME borrowers from sectors such as hospitality, tourism, textile, food & entertainment etc. continued to log in weaker performance.

Exhibit: Delinquencies in ICRA-rated SME loan pools

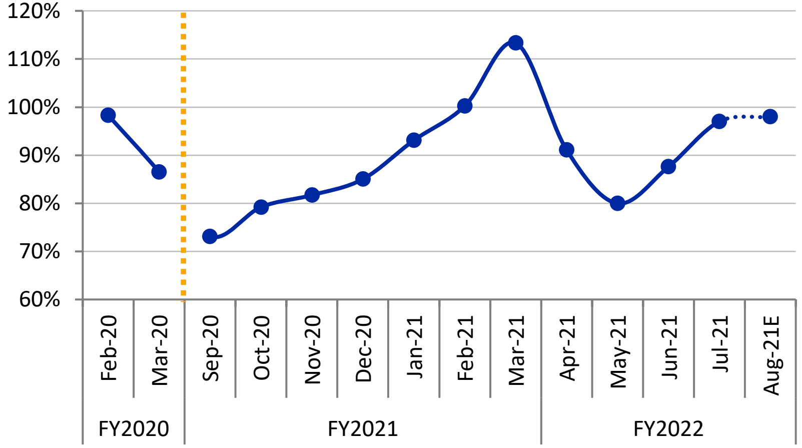


Source: ICRA Research, dpd – days past due

- The slippages in softer and harder buckets saw a decline from the May 2021 level as the resumption in the local business activities advanced the repayment ability of the self-employed borrowers in the segment.
- A material recovery may not be expected in the unsecured SME loan segment as recovery from harder buckets would be difficult and the losses may be higher than seen in the past due to the absence of a collateral.
- The limited share of restructured loan accounts in the pools is a source of comfort.

Collection efficiencies and delinquencies | Microfinance loan pool performance

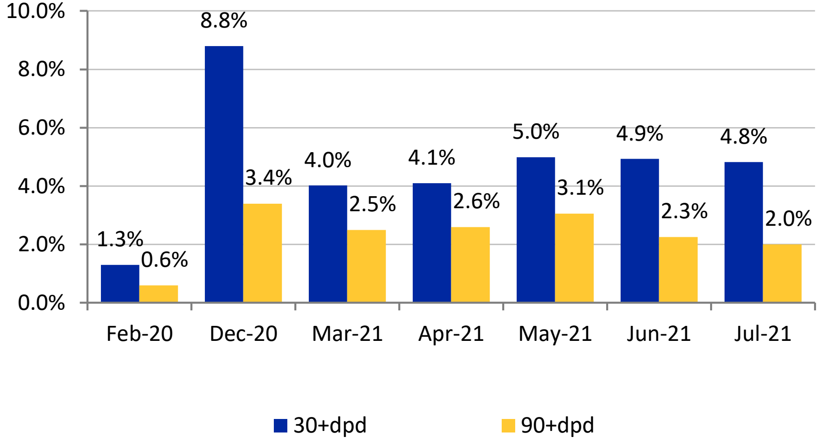
Exhibit: Monthly collection efficiency trend in ICRA-rated Microfinance loan pools



Source: ICRA Research, Aug-21E represents estimated numbers,
Monthly collection efficiency = (current collections + overdue collections)/current billings

- The average monthly collection efficiency of ICRA-rated microfinance loan pools continued to rebound in July 2021. Nonetheless, improvement to the pre-Covid level or March 2021 level may take some more time as the impact of second wave of pandemic has been more severe in rural and semi-urban areas.
- Certain states continued to report weak collections due to their own local issues.

Exhibit: Delinquencies in ICRA-rated Microfinance loan pools

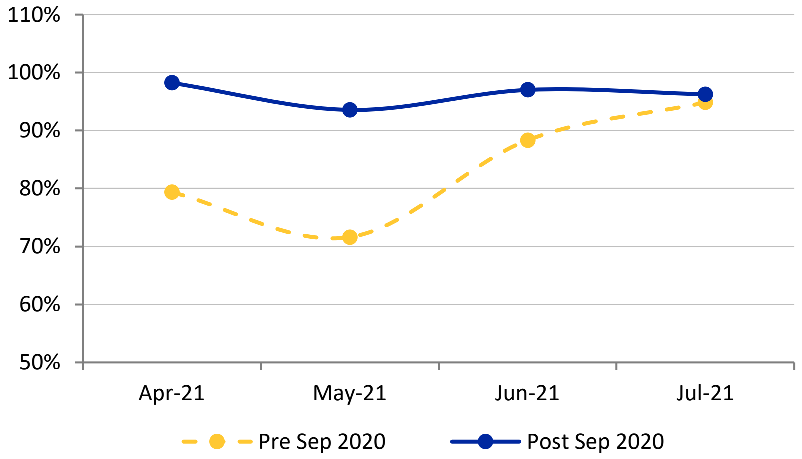


Source: ICRA Research, dpd – days past due

- The incremental slippages and delinquencies in July 2021 dropped in ICRA-rated microfinance pools. The asset quality is expected to improve further in near term on account of the presence of better-quality contracts in the pools. Like SME loans, a substantial recovery from harder bucket (i.e. 90+dpd) would continue to remain a challenge.

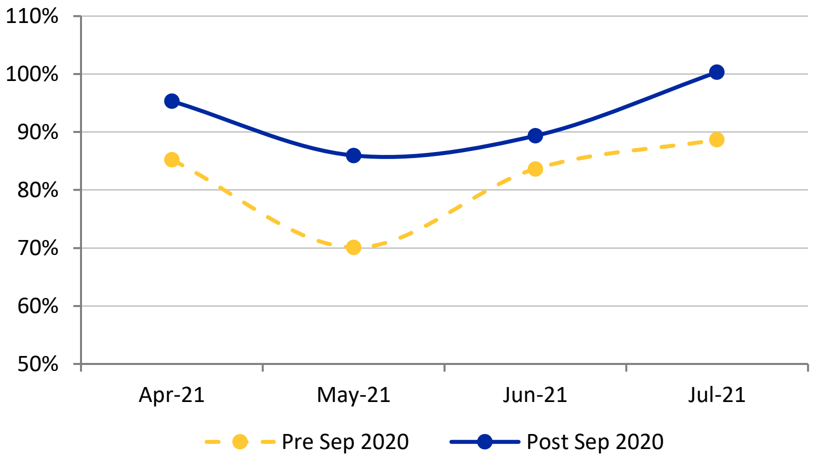
Better collection efficiency for unsecured loan pools securitised post Sep-20

Exhibit: Monthly collection efficiency trend in ICRA-rated SME loan pools



Source: ICRA Research,
Monthly collection efficiency = (current collections + overdue collections)/current billings

Exhibit: Delinquencies in ICRA-rated Microfinance loan pools



Source: ICRA Research,
Monthly collection efficiency = (current collections + overdue collections)/current billings

- ICRA observes that the collections in retail pools securitised post the first wave (i.e. September 2020), especially for the more affected unsecured loans segment i.e. SME loans and microfinance loans, have fared better than the pools originated prior to the same.
- This is on account of tightening of the prevailing credit appraisal processes and parameters by the lenders to ensure addition of better-quality loans in the portfolio coupled with stringent loan selection criteria espoused by the investors in the pools such as high bureau scores, high seasoning, non-moratorium, exposure to least infected states/districts etc.
- Specific to the unsecured SME loan pools, with the improving business activities and resultantly the cash flows, the gap in collection performance has narrowed substantially. ICRA expects a similar trend in Microfinance loan pools only post the borrowers in rural / semi-urban areas recover significantly from the impact of second wave.

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Thank You!