March 31, 2021

Higher Education Financing Agency: Rating reaffirmed; Outlook revised to Positive from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Bank facilities	2,500.00	2,500.00	[ICRA]AA-(Positive); rating reaffirmed and outlook revised to Positive from Stable
Issuer rating	NA	NA	[ICRA]AA-(Positive); rating reaffirmed and outlook revised to Positive from Stable
Total	**2,500.00**	**2,500.00**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in Higher Education Financing Agency's (HEFA) outlook factors in its portfolio scale-up and its comfortable capitalisation profile, which is supported by regular infusions from its shareholders – the Government of India (GoI; 90.9% equity stake) and Canara Bank [9.1% stake; rated [ICRA]AA+(Stable)]. ICRA expects the capital profile to remain comfortable over the medium term considering the current net worth (Rs. 6,045.6 crore, provisional, as of December 2020) and the expected growth plans. HEFA's risk profile is further supported by its exposure to GoI-funded/controlled educational institutions. Financing to these institutions are under five windows, depending on their vintage. The company also ensures the setting up of an escrow mechanism with these borrowing institutions, which provides some comfort regarding the collection of instalments (escrow quantum, to the extent of 5% of the sanctioned amount, six months in advance). While the servicing of interest by the institutions would be through the GoI grants received by them, the principal repayment would be either by the institution (via their fee receipts) or through the GoI grants or both, depending on the financing window.

The rating factors in HEFA's experienced board and the operational support from Canara Bank. The company's board of directors (BoD) is diverse with representation from various fields like education, banking and the GoI. Canara Bank supports HEFA in the loan appraisal process and its senior management team consists of personnel on deputation (for a period of three years) from Canara Bank. While this would limit the operating costs, the lending spreads are expected to remain lean, given the company's 'not-for-profit' nature of operations. HEFA is currently incorporated under Section 8 of the Companies Act, 2013 and is registered as a non-banking financial company (NBFC) with the Reserve Bank of India (RBI). It has a limited track record of operations having commenced operations in 2018. Its liquidity profile is strong at present, supported by its low leverage, expected inflows from advances and sizeable undrawn funding lines from banks. HEFA would, however, have to diversify its funding profile to support its growth and secure funding at competitive rates.

The company has received regular capital infusions from its shareholders, the most recent being Rs. 220 crore in the current fiscal (Rs. 2,310 crore in FY2020). While HEFA's track record is limited, its portfolio has more than tripled since March 2019 (Rs. 2,496.7 crore) to Rs. 7,966.2 crore in December 2020. However, the asset quality remains good with NIL non-performing assets (NPAs) as of February 2020, though there have been some delays by institutes for which a penal charge is imposed on the latter. Focus on financing the capital expenditure of Central Government funded/controlled educational institutes, along with an escrow mechanism for principal and interest collection, supports the asset quality.

Key rating drivers and their description

Credit strengths

Majority GoI holding; regular capital infusions from stakeholders – HEFA has been set up by the GoI as a joint venture with Canara Bank. As on December 31, 2020, the GoI held a 90.9% equity stake in the company with Canara Bank holding 9.1%. Till 9M FY2021, the company had received a capital infusion of Rs. 220 crore and its net worth stood at Rs. 6,045.6 crore as on December 31, 2020. The equity infusion in the current fiscal was lower than expected. As of December 2020, the gearing stood at 0.3 times and ICRA expects the same to remain at about 3 times over the next two years. ICRA expects HEFA to continue to receive timely and adequate capital support from the stakeholders, when required, and notes that the shareholding is likely to remain with the GoI and Canara Bank and in the current proportion in the near to medium term.

Experienced board and operational support from Canara Bank – The company's 10-member BoD comprises experienced personnel from the fields of education and banking while the Chairman of the BoD is the Secretary, Ministry of Education. A sub-committee of the board monitors the progress of the projects funded by HEFA on a quarterly basis and interacts with the institutes at least once annually to review the progress. HEFA receives operational support from Canara Bank with the latter's project appraisal team involved in the credit appraisal process of the loan sanctions. Canara Bank also deputes experienced personnel as senior management to HEFA for a period of three years. Currently, the company has a lean management team consisting of personnel with established banking and credit experience in Canara Bank. Canara Bank receives a management fee of 1% of the annual disbursements from HEFA.

Focus on financing capital expenditure requirements of Central Government funded/controlled educational institutions – HEFA has been set up with the primary objective of lending to GoI-controlled/funded educational institutions to meet their capital expenditure/infrastructure requirements. The company's target borrower profile includes premier educational institutions such as Indian Institute of Management (IIM), Indian Institute of Technology (IIT), National Institute of Technology (NIT), Indian Institute of Science Education and Research (IISER) and other Central universities. The established brand of these institutions along with steady student inflows offers strong growth prospects for HEFA, given the growing infrastructure needs of these institutions. Financing to these institutions is provided under five windows with varying levels of dependence on GoI grants for servicing the principal portion of the loan depending on the vintage and type of institution *(Window I – institutions established before 2008, Window II – institutions established between 2008 and 2014, Window III – Central universities established before 2014, Window IV – institutions established after 2014 and Window V – other institutions including the entities of the Ministry of Health).* Interest servicing of these loans would, however, be entirely through the GoI grants to such institutions. For loans extended under Window IV/V, the GoI was servicing both the principal and the interest. Sanctions under Window IV/V accounted for 52% of the total sanctions (~Rs. 31,400 crore till December 2020) and 49% of the pending disbursements (~Rs. 20,550 crore as of December 2020). Going forward, incremental disbursements to institutions, which got loan sanctions under Window IV/V, would be directly provided as grants from the GoI. As of December 2020, the company's portfolio stood at Rs. 7,966.2 crore.

Credit challenges

Limited track record of operations – HEFA started lending in FY2019 and the loan book increased to Rs. 7,966 crore in December 2020 from Rs. 2,497 crore in March 2019 (Rs. 6,334 crore in March 2020). ICRA also takes note of the escrow mechanism wherein the borrowing institution is required to maintain one half-yearly instalment of the principal in the escrow account at the time of first disbursement (about 5% of the loan amount) and replenish the same on a half-yearly basis post drawdown. Another escrow mechanism is in place for interest servicing from the grants receivable account of the institutes. Although the escrow mechanism for the repayment of the principal and interest provides some comfort, ICRA notes that the effectiveness of the same would depend on the timely availability of funds in the escrow accounts which would depend on the receipt of fees and/or GoI grants. Generally, the servicing of the loans extended by HEFA has been as per the terms, though there were marginal delays (up to 3-5 days) in some cases due to operational reasons. There was one instance in FY2020 where the delay was longer (about 50 days), again because of operational issues. Considering the target borrower profile, which comprises GoI-funded/controlled higher educational institutions, ICRA expects adequate and timely support from the GoI to these institutions in the event of stress.

Lending spread expected to remain lean – HEFA's lending spreads are expected to remain lean (in the range of 100-125 basis points) as it was formed to support GoI-funded/controlled institutes in raising funds. Further, the operating expenses largely comprise the management fee of 1% paid to Canara Bank for services received. In 9M FY2021, the company reported a provisional net profit of Rs. 367.0 crore (Rs. 315.8 crore in FY2020) with a return on assets (RoA) of 6.7% (6.7% in FY2020). As it is a Section 8 not-for-profit company, HEFA's profitability would moderate, given the lean lending spread and as the leverage increases.

Diversity in funding profile crucial for future growth – As on December 31, 2020, the company had borrowings from two banks and sanctioned and unutilised bank lines of ~Rs. 1,775 crore. However, given the sizeable loan sanctions, which are yet to be disbursed of over Rs. 10,500 crore (under Window I/II/III) as on December 31, 2020 and the incremental proposals under consideration, ICRA notes that the company would have significant funding requirements. Accordingly, it would be crucial for HEFA to diversify its funding profile to secure low-cost funds to maintain a comfortable liquidity profile and meet the envisaged portfolio growth.

Liquidity position: Strong

HEFA had an unencumbered cash and bank balance of Rs. 86 crore as on February 28, 2021 with a debt obligation of Rs. 221 crore during March – August 2021. Collections from advances of Rs. 1,477 crore during March – August 2021 are sufficient to cover the repayments during this period. Further, it had sanctioned and undrawn bank facilities of Rs. 1,775 crore as on February 28, 2021, which support its liquidity profile. HEFA reported 100% collection efficiency during April 2020 to February 2021.

Rating sensitivities

Positive factors – ICRA could upgrade the rating if the company is able to demonstrate sustained portfolio scale-up while maintaining comfortable capitalisation, good asset quality and diversification in its funding profile.

Negative factors – Pressure on the rating could arise if there is a material weakening in the asset quality impacting the earnings and capital profile or if there is an adverse change in the shareholding pattern with a significant reduction in the GoI holding or lower-than-expected support from the GoI or Canara Bank.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Rating Methodology for Non-Banking Finance Companies Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group Support	The rating considers the importance held by HEFA for the GoI as a vehicle for policy implementation and thus factors in timely support from the GoI
Consolidation/Standalone	Standalone

About the company

HEFA is a joint venture initiative between the Ministry of Education, the Government of India (GoI) and Canara Bank. It was established in 2017 with the objective of financing the capital asset creation of Central Government funded/controlled educational institutions. At present, the company has been constituted as not-for-profit under Section 8 of the Companies Act, 2013 and is registered as a non-banking financial company (NBFC) with the Reserve Bank of India (RBI). HEFA reported a profit after tax (PAT) of Rs. 367.0 crore (provisional) in 9M FY2021 on a loan book of Rs. 7,966.2 crore (provisional) as of December 2020. Its net worth stood at Rs. 6,045.6 crore (provisional) as of December 2020.

Key financial indicators (audited)

Higher Education Financing Agency	FY2019	FY2020	9M FY2021*
Total income (Rs. crore)	109.4	379.1	443.8
Profit after tax (Rs. crore)	72.1	315.8	367.0
Net worth (Rs. crore)	2,844.3	5,470.2	6,045.6
Loan book (Rs. crore)	2,496.7	6,334.1	7,966.2
Total managed assets (Rs. crore)	2,879.8	6,528.5	7,985.8
Return on managed assets (%)	4.5%	6.7%	6.7%
Return on net worth (%)	4.6%	7.6%	8.5%
Managed gearing (times)	0.0	0.2	0.3
Gross NPA (%)	0%	0%	0%
Net NPA (%)	0%	0%	0%
Net NPA / Net worth	0%	0%	0%
CRAR (%)	113.2%	85.8%	NA

Source: *Company, ICRA research; * Provisional numbers; All ratios as per ICRA calculations*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

<table>
<tr><th rowspan="3">Instrument</th><th colspan="4">Current Rating (FY2021)</th><th colspan="3">Chronology of Rating History for the past 3 years</th></tr>
<tr><th rowspan="2">Type</th><th rowspan="2">Amount Rated (Rs. crore)</th><th rowspan="2">Amount Outstanding (Rs. crore)</th><th>Date & Rating in FY2021</th><th>Date & Rating in FY2020</th><th>Date & Rating in FY2019</th><th>Date & Rating in FY2018</th></tr>
<tr><th>Mar 31, 2021</th><th>Dec 27, 2019
Feb 21, 2020</th><th>Dec 31, 2018</th><th>Sep 25, 2017</th></tr>
<tr><td>Issuer Rating</td><td>LT</td><td>NA</td><td>NA</td><td>[ICRA]AA- (Positive)</td><td>[ICRA]AA- (Stable)</td><td>[ICRA]AA- (Stable)</td><td>[ICRA]AA- (Stable)</td></tr>
<tr><td>Term Loans</td><td>LT</td><td>2,500.00</td><td>2,500.00</td><td>[ICRA]AA- (Positive)</td><td>[ICRA]AA- (Stable)</td><td>-</td><td>-</td></tr>
</table>

LT – Long term

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 No	Instrument Name	Date of Issuance / Sanction	Coupon Rate (%)	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Issuer Rating	NA	NA	NA	NA	[ICRA]AA-(Positive)
NA	Term Loan – 1	March 2020	-	March 2030	2,000.00	[ICRA]AA-(Positive)
NA	Term Loan – 2	August 2020	-	August 2025	300.00	[ICRA]AA-(Positive)
NA	Term Loan – Proposed	NA	NA	NA	200.00	[ICRA]AA-(Positive)

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Not applicable

ICRA

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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.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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