August 20, 2020

JM Financial Limited: [ICRA]A1+ reaffirmed for CP programme; rated limits revised

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper (CP) Programme	1,000.00	300.00	[ICRA]A1+; reaffirmed
Non-convertible Debenture (NCD) Programme	100.00	100.00	[ICRA]AA (stable); outstanding
Long-term Bank Lines – Unallocated	100.00	100.00	[ICRA]AA (stable); outstanding
Total	**1,200.00**	**500.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings factor in the demonstrated track record and established franchise of the JM Financial Group (the Group) in the domestic financial services industry, its diversified revenue stream and healthy financial profile with steady profitability and an adequate capitalisation level. While assigning the ratings, ICRA has taken a consolidated view of the Group (i.e. JM Financial Limited (JMFL) on a consolidated basis) due to the close linkages between the Group entities, given the common promoters and senior management team, shared brand name, and strong financial and operational synergies. Moreover, ICRA expects the financial, managerial and operational support from the Group to continue to be available to all key Group companies.

The strengths are partially offset by the exposure to the volatility in capital markets, the inherent risk profile of key segments like real estate and promoter funding, and the portfolio concentration in the wholesale lending segment (~90% of the total book as on March 31, 2020), which could result in a sharp deterioration in the asset quality in case of slippages. The real estate sector has been facing a prolonged slowdown due to subdued sales and lack of funding access. The spread of the Covid-19 pandemic and the resulting nationwide lockdown further impacted the real estate sector. While the near-term pressure on the developers has been mitigated due to the moratorium offered for their loan instalments under the Covid-19-related regulatory package announced by the Reserve Bank of India (RBI), a slow pickup in sales will impact the cash flows of the developers over the medium term. This could pose challenges in maintaining the asset quality. The asset quality, though healthy at present, moderated in recent quarters with the gross non-performing assets (GNPAs) increasing to 1.65% of the loan book as on March 31, 2020 from 1.27% as on September 30, 2019 and 0.68% as on March 31, 2019 (partly also due to the base effect of a declining loan book). The SMA 2 accounts also increased to 2.64% of the loan book as on March 31, 2020 from 2.40% as on September 30, 2019 and 1.25% as on March 31, 2019. The presence of adequate collateral along with the Group's conservative underwriting norms, adequate risk management systems and proactive monitoring and resolution process provide comfort.

ICRA has also favourably factored in the Group's healthy capitalisation profile, with the leverage being lower than that of its peers, which provides it with financial flexibility as well as the ability to absorb losses, if needed. JMFL raised equity capital of Rs. 770 crore in June 2020 to shield itself from the uncertainties surrounding the Covid-19 pandemic and its impact on the economy. Supported by the capital raise, the Group's net gearing improved to 0.79 times as on June 30, 2020 from 1.04 times as on March 31, 2020. The capital raise is also expected to support the near-term liquidity, given the moratorium extended to customers and the stress in the underlying borrower groups. As on June 30, 2020, the Group had cash and cash equivalents of Rs. 3,394 crore (~33% of gross debt) and unutilised credit lines of Rs. 399 crore, covering the short-term debt repayments. The Group made additional provisions (including a fair value loss) of Rs. 175.21 crore in Q4 FY2020 and Rs. 66 crore in Q1 FY2021 towards the potential impact of the pandemic, as assessed by the management, on the Group's business. Going forward, the Group's ability to manage its asset quality and liquidity profile over the near-to-medium-term would remain critical. The ratings also take into account the risks associated with the distressed assets business, given the nature of the underlying assets, the focus on large ticket exposures, the protracted resolution process and the uncertainty associated with the same.

While assigning the ratings, ICRA has also noted the increased challenges in resource mobilisation stemming from the current operating environment and the risk-averse sentiment of investors towards non-banks, particularly wholesale-oriented entities. This has resulted in an increase in the Group's cost of funds (~80 bps YoY increase in FY2020) and the same is expected to limit its growth potential in the lending business in the near-to-medium-term. However, ICRA notes that the Group raised ~Rs. 450 crore from banks in Q1 FY2021 under the targeted long-term repo operations (TLTRO) of the RBI. Following the onset of the liquidity crisis for non-banking financial companies (NBFCs), there has been a change in the Group's debt maturity profile with the share of short-term debt declining to ~9% as on March 31, 2020 from ~27% as on March 31, 2019.

Given the prominence of the lending business in the Group's revenue profile, its ability to manage its asset and liability profile, particularly considering the current operating environment, would remain critical. ICRA takes comfort from the Group's adequate liquid assets and its ability to raise funds from the market when required, as demonstrated in the past. Going forward, the Group's ability to scale up its operations, while keeping the asset quality under check, maintaining healthy profitability and capitalisation and managing its asset liability profile, would remain critical from a credit perspective.

Key rating drivers and their description

Credit strengths

Established position of the Group in financial services industry – The Group is a diversified financial services entity with a presence in investment banking, retail and institutional equity broking, wealth management, investment advisory services, portfolio management, asset management, commodity broking, securities-based lending, corporate lending, real estate lending, private equity, and asset reconstruction. It is one of the leading entities in capital markets and related businesses with a key focus on investment banking and merchant banking operations and has been a part of many marquee deals. On a consolidated basis, the Group's revenue stream remains well diversified with the investment banking, wealth management & securities (IWS) business, mortgage lending, distressed credit and asset management businesses contributing 47%, 39%, 12% and 2%, respectively, in FY2020.

Diversification in business profile – The Group, which forayed into the non-capital market lending business in 2008, subsequently diversified its lending portfolio to wholesale mortgage, retail mortgage, and corporate lending. It forayed into the small and medium enterprises (SME) segment in FY2017 and housing finance in FY2018. Currently, the lending business has emerged as a key contributor to revenues. On an overall basis, the Group's loan book contracted by ~18.3% YoY to Rs. 11,531 crore as on March 31, 2020 from Rs. 14,107 crore as on March 31, 2019 (peak level of Rs. 17,108 crore as on September 30, 2018) due to the liquidity issues prevailing in the industry over the past one and a half years. With the decline in the granular capital markets loan book exceeding the decline in the portfolio, the share of wholesale loans in the total portfolio increased further. As on March 31, 2020, wholesale mortgage, corporate lending, capital markets lending, and retail mortgage accounted for 70%, 20%, 4% and 6%, respectively, of the loan book. While lending has emerged as the largest business activity for the Group, the fee-based businesses continue to account for a sizeable share of the net operating income[1] (~43% in FY2020).

Adequate capitalisation and low leverage at Group level – The Group's capitalisation remains adequate with a consolidated net worth (including non-controlling interest of the Group and net of goodwill on consolidation) of Rs. 7,993 crore and a capital adequacy ratio (CRAR) of 38.7% as on March 31, 2020 (Rs. 7,229 crore and 31.5%, respectively, as of March 31, 2019). The total borrowings at the consolidated level declined to Rs. 11,756 crore as on March 31, 2020 from Rs. 13,991 crore as on March 31, 2019 (peak debt of Rs. 17,794 crore as on September 30, 2018).

The Group had raised equity capital of Rs. 1,380 crore from external investors during FY2018-FY2019, thereby supporting the overall capitalisation levels and helping it maintain a low leverage. JMFL raised Rs. 770-crore equity through the qualified institutional placement (QIP) route in Q1 FY2021, which further enhanced the Group's capitalisation profile. The consolidated gearing was low at 1.47 times as on March 31, 2020 (1.94 times as on March 31, 2019) compared to 2.54 times as on March 31, 2018. The Group's capitalisation profile remains healthy, with lower leverage compared to peers, and provides adequate cushion against losses, if required. With the Group planning to curtail wholesale lending in the near term and increase its focus on retail lending, the leverage is expected to remain low over the near term. Over the medium-to-longer-term, the management intends to cap the gearing at 3 times for the real estate lending business and 2 times for the distressed credit business.

Adequate profitability indicators – The Group's total income declined marginally to Rs. 3,454 crore in FY2020 from Rs. 3,499 crore in FY2019 owing to a moderation in the performance of the asset management business and the distressed assets business. The net interest margins (NIMs) remained stable at 6.6% in FY2020 with the transmission of the increase in the cost of funds to the borrowers. JMFL reported a consolidated net profit of Rs. 545 crore in FY2020 with adequate return on assets (RoA)[2] of 3.6% (3.7% in FY2019). The return on equity (RoE)[2] moderated to 10.2% in FY2020 from 12.8% in FY2019.

Credit challenges

Fund-raising challenges for non-bank financiers impacting business; ability to maintain asset and liability profile remains critical – The operating environment for NBFCs and housing finance companies (HFCs), especially for entities with sizeable real estate exposure, has remained challenging since September 2018. The risk-averse sentiment of lenders/investors towards real estate lenders has constrained the ability of NBFCs and HFCs, including JMFL, to mobilise long-term resources from diversified sources. The cost of funds increased by ~80 bps YoY in FY2020. This, coupled with the subdued macro-economic and operating environment, has impacted JMFL's ability to grow the lending business and the margins (even for the non-real estate lending businesses). While the Group raised long-term funds of ~Rs. 3,700 crore in FY2020, the same was largely used for meeting debt repayment obligations and reducing commercial paper (CP) borrowings. In Q1 FY2021, the Group raised ~Rs. 450 crore from banks under the TLTRO of the RBI.

Following the onset of the liquidity crisis for NBFCs, there has been a change in JMFL's debt maturity profile. As on March 31, 2020, the share of short-term debt in the total borrowings was ~9% compared to ~27% as on March 31, 2019. ICRA also notes that these short-term liabilities, predominantly in the form of CP, are largely matched by assets of similar maturity such as capital market assets. Given the rising prominence of the lending business, the Group's ability to

[1] *Net operating income = Revenue from operations (excludes net gain on derecognition of financial assets and investments carried at fair value) less finance cost and sub-brokerage, fee and commission expense*

[2] *RoA and RoE are as per ICRA calculations*

manage its asset and liability profile would remain critical. ICRA takes comfort from the Group's adequate liquid assets (cash and liquid investments) of Rs. 3,412 crore and undrawn bank lines of Rs. 442 crore as on March 31, 2020, and its ability to raise funds from the market when required, as demonstrated in the past.

High concentration and inherent credit risk in wholesale segment; moderation in asset quality in current fiscal, though it remains healthy – The Group's loan portfolio largely comprises wholesale lending (~90% of the total book as on March 31, 2020), which includes real estate, promoter funding and corporate loans. The concentration in the wholesale segment could result in a sharp deterioration in the asset quality in case of slippages. The risks are further aggravated by the pandemic-induced stress on the operating environment, which was already facing challenges due to the continued slowdown in the real estate sector and the liquidity squeeze faced by developers and financiers.

The Group's asset quality, which remained stable over the last few years, witnessed some deterioration in FY2020 due to a few lumpy slippages in the real estate lending segment. This, coupled with a decline in the loan book, resulted in a moderation in the asset quality indicators, as reflected by the increase in the GNPAs and the NNPAs to 1.65% and 1.13%, respectively, as on March 31, 2020 from 0.68% and 0.55%, respectively, as on March 31, 2019. Similarly, the SMA 2 assets increased to 2.64% of the loan book as on March 31, 2020 from 1.25% as on March 31, 2019.

In ICRA's view, despite the moderation in recent quarters, the Group's asset quality indicators remain comfortable. The Group's ability to maintain a healthy asset quality once the moratorium offered to the customers as per the RBI's Covid-19 regulatory package ends, given the currently challenging operating environment for the real estate sector, will be critical from a credit perspective. The presence of adequate collateral along with the Group's conservative underwriting norms, adequate risk management systems, and proactive monitoring and resolution process provide comfort. ICRA also draws comfort from the Group's leverage being lower than that of its peers, which provides it with the ability to absorb losses, if needed.

Risks associated with distressed assets business, given the nature of underlying assets, uncertainty associated with resolution process and large ticket exposures – The Group, through JM Financial Asset Reconstruction Company Limited (JMFARCL), is one of the prominent players in the asset reconstruction business, with distressed credit assets under management (AUM) of Rs. 11,489 crore as on March 31, 2020. JMFARCL focusses on the large single borrower corporate segment, which is riskier than the retail segment on account of the larger ticket size, higher complexity involved in the transactions and the resolution process, and the high degree of engagement required with the promoters. This, along with JMFARCL's strategy of focussing on resolution through the revival of operations and debt restrictions and the inherent risks in the industry, given the nature of the underlying asset class, can result in a protracted process and lumpy cashflows. The presence in the corporate and SME portfolios consisting of multiple borrowers provides some diversification to the AUM.

Liquidity position: Adequate

As on June 30, 2020, JMFL had cash and cash equivalents of Rs. 3,394 crore. The Group's liquidity profile is adequate in comparison to its near-term maturities. The Group used the liquidity buffer to buy back its bonds from the secondary market in Q1 FY2021. JMFL also raised equity funds of Rs. 770 crore in June 2020, which strengthened its liquidity profile. While the Group offered moratorium benefits to its customers, it did not avail a moratorium for any of its bank borrowings. As per the asset-liability statements for the key lending entities in the Group as on June 30, 2020, the cumulative cashflow position remains comfortable for the near term.

Rating sensitivities

Positive triggers – ICRA could upgrade the ratings if the Group posts a substantial and sustained improvement in its business performance, characterised by well-diversified growth in the lending portfolio with an increase in granularity, healthy growth in fee-based income and improvement in profitability while maintaining the current capital structure profile and asset quality.

Negative triggers – The ratings or the outlook could be revised if the asset quality deteriorates significantly with the reported GNPAs increasing above 5% on a sustained basis or if there is an increase in the vulnerability of the wholesale loan book/asset reconstruction business. Pressure on the ratings could also emerge if the funding access challenges continue for NBFCs for a prolonged period with the Group not being able to maintain its current scale of lending operations. A significant deterioration in the profitability, a reduction in the fee-based income and weakening of the capitalisation profile would also be credit negatives.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA's Credit Rating Methodology for Non-Banking Finance Companies Consolidation and rating approach
Parent/Group Support	Not applicable; while assigning the ratings, ICRA has taken a consolidated view of the Group (JMFL - Consolidated), given the high operational and managerial linkages between the Group companies and the shared brand name.
Consolidation / Standalone	To arrive at the ratings, ICRA has considered the consolidated financial profile of JMFL. As on March 31, 2020, JMFL had nine subsidiaries, six stepdown subsidiaries, one partnership firm (with two of JMFL's subsidiaries as partners) and one associate company. Details of these companies are provided in Annexure-2.

About the company

JM Financial is an integrated and diversified financial services group. Its primary businesses include (a) IWS, including fee and fund-based activities for its clients, (b) mortgage lending, which includes both wholesale mortgage lending and retail mortgage lending (home loans, educational institution lending and loan against property), (c) distressed credit, which includes the asset reconstruction business, and (d) asset management, which includes the mutual fund business.

JMFL is the holding company for the operating companies in the Group and is also engaged in investment banking and the management of private equity funds. As on June 30, 2020, the consolidated loan book stood at Rs. 10,833 crore (Rs. 11,531 crore as on March 31, 2020), distressed credit business AUM at Rs. 11,441 crore (Rs. 11,489 crore as on March 31, 2020), wealth management AUM at Rs. 47,579 crore (Rs. 44,883 crore as on March 31, 2020) and mutual fund quarterly average AUM (QAAUM) at Rs. 4,049 crore (Rs. 6,109 crore as on March 31, 2020). The Group is headquartered in Mumbai and has a presence in 456 locations spread across 154 cities in India. JMFL's equity shares are listed in India on the BSE and the NSE.

In FY2020, JMFL reported a consolidated net profit (net of non-controlling interest) of Rs. 545 crore on a total income of Rs. 3,454 crore compared with a consolidated net profit of Rs. 572 crore on a total income of Rs. 3,499 crore in FY2019.

Key financial indicators of JMFL (consolidated)

	FY2018 Ind-AS	FY2019 Ind-AS	FY2020 Ind-AS
Total Income	3,033	3,499	3,454
PAT[3]	601	572	545
Tangible Net Worth[4]	4,502	5,079	5,586
Non-controlling Interests	1,395	2,150	2,407
Total Loan Book	14,772	14,107	11,531
Total Assets[4]	22,154	22,588	20,693
Return on Average Assets (RoA)	4.0%	3.7%	3.6%
PAT/ Average Net Worth (RoE)	15.0%	12.8%	10.2%
Gearing (times)	2.54	1.94	1.47

Source: JM Financial Limited and ICRA research; Amounts in Rs. crore; All ratios are as per ICRA calculations

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

		Rating (FY2021)					Rating History for the Past 3 Years			
	Instrument	Type	Amount Rated	Amount Outstanding	Current Rating	Earlier Rating	FY2020		FY2019	FY2018
					20-Aug-2020	13-Apr-2020	20-Jan-2020	1-Apr-2019	-	31-Jan-2018
1	NCD Programme	Long Term	100	0	[ICRA]AA (stable)	[ICRA]AA (stable)	[ICRA]AA (stable)	[ICRA]AA (stable)	-	[ICRA]AA (stable)
2	Bank Lines	Long Term	100	0	[ICRA]AA (stable)	[ICRA]AA (stable)	-	-	-	-
3	CP Programme	Short Term	300	0	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	[ICRA]A1+

Amount in Rs. crore

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

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[3] *Including share in profit of associates and net of minority interest*

[4] *Net of goodwill on consolidation*

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Bank Lines (Unallocated)*	-	-	-	100	[ICRA]AA (stable)
NA	NCD Programme*	-	-	-	100	[ICRA]AA (stable)
NA	CP Programme	-	-	7-365 days	300	[ICRA]A1+

** Proposed; Source: JM Financial Limited*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership as on March 31, 2020	Consolidation Approach
JM Financial Asset Management Limited	59.54%	ICRA has taken a consolidated view of the parent and its subsidiaries and an associate
CR Retail Malls (India) Limited	100%	
JM Financial Products Limited	99.35%	
JM Financial Capital Limited	100%	
JM Financial Services Limited	100%	
JM Financial Credit Solutions Limited	46.68%	
Astute Investments	100%	
JM Financial Asset Reconstruction Company Limited	59.25%	
JM Financial Home Loans Limited	98.36%	
JM Financial Institutional Securities Limited (formerly known as JM Financial Securities Limited)	100%	
Infinite India Investment Management Limited	100%	
JM Financial Trustee Company Private Limited	25%	
JM Financial Overseas Holding Private Limited	100%	
JM Financial Securities Inc.	100%	
JM Financial Singapore Pte Ltd	100%	
JM Financial Commtrade Limited	100%	
JM Financial Properties and Holdings Limited	100%	
J.M. Financial & Investment Consultancy Private Limited	Related Party *	

** Owned by the promoters of JMFL*

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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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