

October 12, 2022^(Revised)

IIFL Wealth Distribution Services Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper programme	300	300	[ICRA]A1+; reaffirmed
Total	300	300	

*Instrument details are provided in Annexure I

Rationale

The rating for IIFL Wealth Distribution Services Limited (IWDSL) is based on a consolidated view of IIFL Wealth Management Limited (IWML; standalone) and its subsidiaries (referred to as IIFL Wealth/the Group/the company; consolidated), given the common senior management team and strong financial and operational synergies.

The rating factors in IIFL Wealth's leading market position in the wealth management business supported by its senior management team. Its assets under management and distribution stood at Rs. 2.52 lakh crore as on June 30, 2022. The franchisee, built over the years, has helped ensure low client attrition (loss of assets under management (AUM) due to client attrition of 1% in FY2022). To reduce the volatility in income on account of transaction/brokerage assets, the management has been focusing on increasing the share of assets with a recurring nature of income (57% as of June 30, 2022, 50% as on June 30, 2021 and 41% as on June 30, 2020). This, coupled with the increasing AUM, has also driven the healthy profitability. The return on equity (RoE) and return on assets (RoA) were healthy at 19.4% and 6.0%, respectively, in FY2022 compared to 13.1% and 3.4%, respectively, in FY2021, driving comfortable capitalisation despite the high dividend payout rate.

The Group's borrowing requirements are driven by the lending operations to its wealth clients with a loan book of Rs. 4,335 crore as on June 30, 2022 and are backed by the client's AUM. However, the top 20 exposures formed 39% of the total loans and 56% of the consolidated net worth as on June 30, 2022. The rating also factors in the funding concentration, through principal protected market linked debentures (PP-MLDs), though these are largely through its own client base. While the share of commercial papers (CP) increased to ~28-30% of the consolidated borrowings as on June 30, 2022, the short-term assets also increased correspondingly. This was driven by the short-term in-transit investment book for down-selling to clients and the margin funding book under IWDSL. ICRA expects the share of CPs in overall borrowings to decline with the corresponding short-term assets. Further, though the tenure of the loan book is ~1-2 years, the average maturity has remained ~8-9 months.

Bain Capital recently announced its intention to acquire a 24.98% stake in IIFL Wealth from General Atlantic and Fairfax, and has received approval from various regulatory authorities. In ICRA's opinion, this announcement and the proposed transaction are not expected to have an adverse impact on the company's credit profile. The outlook is Stable as IIFL Wealth is expected to maintain healthy profitability, driven by its strong position in wealth management, and is likely to maintain the gearing under 3.5x.

Key rating drivers and their description

Credit strengths

Strong market position in wealth management – IIFL Wealth offers advisory, asset management, broking and distribution services to high-net-worth individuals (HNIs) and ultra HNIs. Its leading market position is reflected in the assets under management and distribution of Rs. 2.52 lakh crore as on June 30, 2022 (YoY growth of 7.2% from Rs. 2.35 lakh crore as on June 30, 2021). It is also one of the largest managers of alternative investment funds (AIFs) with AUM of Rs. 32,374 crore as of June 30, 2022 (Rs. 27,090 crore as on June 30, 2021). The company has seen a transition with the increasing share of annual recurring assets and has a presence in wealth management across five geographies with 23 offices and 227 relationship managers as on March 31, 2022.

It has a subsidiary, IIFL Wealth Prime Limited (IWPL), which is a non-banking financial company (NBFC) that provides loans against securities to the clients of the wealth management business.

Experienced and stable management team – The company's senior management team has significant experience and expertise in the wealth management business, which has helped it grow into a leading player in the wealth management industry. Apart from the senior management, the relationship managers have average experience of over seven years in IIFL Wealth and overall experience of more than 12 years.

Comfortable capitalisation; demonstrated ability to raise equity – The consolidated net worth stood at Rs. 2,990 crore as on June 30, 2022 with a reported gearing of 1.75x. On a standalone basis, IWPL reported a Tier I capital of 22.64% as of June 30, 2022 (25.33% as on June 30, 2021). The capitalisation has been supported by a regular equity infusion of Rs. 904 crore in FY2016 by General Atlantic and an equity infusion of Rs. 745.71 crore in Q1 FY2019 by Amansa, General Atlantic, HDFC Standard Life Insurance, Rimco, Steadview and Ward Ferry. The infused capital was partly utilised for the acquisition of Chennai-based wealth management company, Wealth Advisors India Pvt. Ltd., for Rs. 253.6 crore in cash in FY2018. Further, the company purchased the wealth business of L&T Finance for Rs. 230 crore in FY2020.

The profitability also remains strong. With the significant increase in the AUM, the operating revenues were higher in FY2022 at Rs. 2,024 crore (up 19% YoY) while the cost-to-income ratio declined to 58.6% (60.5% in FY2021). IIFL Wealth (consolidated basis) reported a profit after tax (PAT) of Rs. 582 crore in FY2022 (RoE of 19.4%) compared to Rs. 369 crore in FY2021 (RoE of 13.0%). The consolidated PAT remained strong at Rs. 160 crore in Q1 FY2023 (RoE of 21.4%).

With minimal additional sponsor investments in own manufactured AIFs, a low capital-intensive business and moderate growth plans for IWPL's loan book, the Group is currently comfortably capitalised. This has driven the high dividend payouts at ~75-80% during the last few years, which can be calibrated, if required, to support growth and maintain the leverage within the stated levels.

Comfortable asset quality – IWPL provides loans against securities (including AIF investments) to its clients in the wealth management business and the same is sourced by the wealth relationship managers. The loan book accounted for 1.7% of the wealth management AUM as of June 30, 2022.

IWPL reported gross non-performing advances (GNPAs) of Rs. 85 crore, comprising 2.1% of gross advances, with net NPAs of 1.5% as of December 31, 2021. The same was recovered in Q4 FY2022, leading to nil NPAs as on date. While the reported asset quality remains comfortable, the loan book, which is backed by financial assets, is susceptible to a decline in prices that may lead to an increase in the loan-to-value (LTV) ratios. While the collateral held by the company against most of its loans is liquid, a part of the same may not be liquid in a few instances, which could impact the asset quality. ICRA derives comfort from the fact that the portfolio largely comprises the clients of the wealth management business and the company does not have any aggressive plans to grow its portfolio.

Credit challenges

Funding profile remains concentrated – The funding profile remains concentrated with the company's borrowings largely comprising PP-MLDs (74% of overall borrowings as on June 30, 2022; 66% as of March 31, 2022). These PP-MLDs offer tax efficiency to the investors and funding from such instruments could be susceptible to changes in tax laws. However, most of these PP-MLDs are invested by its wealth management clients. The Group's funding requirements will be driven by the growth in the loan book and its contribution to the sponsor share in the AIFs.

The company increased its reliance on CP to 28% as on June 30, 2022 (30% as of March 31, 2022) to fund its short-term requirements (largely in-transit investment book and margin funding book under IWDSL). Overall, on a steady-state basis, the share of CPs is likely to reduce to ~20% in FY2023 and will largely be backed by short-term assets.

Earnings remain exposed to capital market movements and regulatory uncertainties – The company's net inflows are exposed to fluctuations in the capital markets. While the AUM is expected to support revenues, lower net inflows could impact revenue growth. The company's revenues were impacted in FY2020 by the change in the revenue recognition model, whereby the revenues on distribution were payable on trail basis even for the portfolio management services (PMS) and AIFs. To reduce the volatility in income, the management is also focusing on increasing the share of recurring assets instead of transaction/brokerage assets, which has helped reduce the volatility in income. With the growth in the AUM and the increase in the share of annual recurring revenue (ARR) assets, the revenues in FY2021 and FY2022 have improved substantially. The revenues are also susceptible to regulatory changes such as the regulations for the total expense ratio (TER). The company's strategy of moving to an advisory model from the broker model would help reduce the regulatory uncertainties associated with distribution fees from the manufacturer.

Franchisee risks – The company relies on its brand and the franchisee developed over a period for the retention and acquisition of clients. Any reputational damage could affect the business. The ability to retain the relationship manager base will also be critical to maintain low client attrition rates.

Modest scale of lending operations with concentration of top 20 exposures – IIFL Wealth's lending operations remain modest with a loan book of Rs. 4,335 crore as on June 30, 2022. Further, the portfolio is largely concentrated on a single product, i.e. loan against securities to HNI clients. ICRA also notes that the top 20 exposures formed 39% of the total loans and 56% of the consolidated net worth as of June 30, 2022.

Liquidity position: Adequate

As on August 31, 2022, the consolidated debt repayment for the Group stood at Rs. 1,763 crore till February 2023. Against this, the company has cash and liquid investments of Rs. 1,528 crore and sanctioned but unutilised bank lines of Rs. 200 crore. IWPL had positive cumulative mismatches in the less-than-1-year bucket as on August 31, 2022. While the contractual repayments on its loan book, as per the structural liquidity statement (SLS), are limited, the actual repayments received are much higher. IWML (standalone) had cash and liquid investments of Rs. 723 crore as of August 31, 2022 against repayments of Rs. 565 crore due by February 28, 2023.

Rating sensitivities

Positive factors – ICRA will upgrade the ratings/change the outlook to Positive if the company is able to increase the annual recurring assets to 75% of the AUM on a sustained basis while growing the AUM and maintaining healthy profitability.

Negative factors – ICRA will downgrade the rating if there is a material and prolonged erosion in the company's AUM with high client and advisor attrition. Increase in the consolidated gearing beyond 3.5x on a sustained basis remains a rating trigger.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Non-banking Finance Companies Rating Approach - Consolidation
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the rating, ICRA has considered the consolidated financials of IIFL Wealth Management Limited

About the company

IIFL Wealth Distribution Services Limited (IWDSL) is a public company incorporated under the provisions of the Companies Act, 1956. It is registered with the Securities and Exchange Board of India (SEBI) to engage in the retail broking and depository participant business. IWDSL also provides manpower services to its associate companies.

Earlier, the financial product distribution businesses of IIFL Wealth Management were carried out by three wholly-owned subsidiaries, viz. IIFL Wealth Capital Markets (IWCML) and IIFL Wealth Prime (IWPL) and IWDSL. To consolidate these distribution businesses under a single wholly-owned subsidiary, the distribution business will be demerged from IWPL and IWCML to IWDSL after getting regulatory approvals.

IWDSL's net worth stood at Rs. 45 crore as on March 31, 2022. It reported a net profit of Rs. 11 crore on total revenues of Rs. 80 crore in FY2022 compared to a net profit of Rs. 27 crore on total revenues of Rs. 86 crore in FY2021. For Q1 FY2023, the company reported a net loss of Rs. 7 crore on total revenues of Rs. 12 crore.

IIFL Wealth Management Limited

IIFL Wealth Management Limited (IIFL Wealth), founded in 2008, is one of the largest private wealth management firms in India. It was a part of the IIFL Group with IIFL Holdings Limited (renamed IIFL Finance) holding a majority stake of 53.3% as on March 31, 2019. After the scheme of arrangement (effective May 2019), the demerger of the wealth business undertaking of IIFL Finance Limited into IIFL Wealth became effective. It was listed on September 19, 2019.

IIFL Wealth Management (Consolidated – referred to as IIFL Wealth) net worth stood at Rs. 2,990 crore as on June 30, 2022. It earned a net profit of Rs. 582 crore on total operating revenues of Rs. 2,024 crore in FY2022 compared to a net profit of Rs. 369 crore on total operating revenue of Rs. 1,634 crore in FY2021. The profit for Q1 FY23 was Rs. 160 crore on a total income of Rs. 469 crore

IIFL Wealth Management Limited (IIFL Wealth), founded in 2008, is one of the largest private wealth management firms in India. It was a part of the IIFL Group with IIFL Holdings Limited (renamed IIFL Finance) holding a majority stake of 53.3% as on March 31, 2019. After the scheme of arrangement (effective May 2019), the demerger of the wealth business undertaking of IIFL Finance Limited into IIFL Wealth became effective. It was listed on September 19, 2019.

IIFL Wealth Management's (consolidated – referred to as IIFL Wealth) net worth stood at Rs. 2,990 crore as on June 30, 2022. It earned a net profit of Rs. 582 crore on total operating revenue of Rs. 2,024 crore in FY2022 compared to a net profit of Rs. 369 crore on total revenue of Rs. 1,634 crore in FY2021. The profit for Q1 FY2023 was Rs. 160 crore on total income of Rs. 469 crore.

Key financial indicators (audited)

IIFL Wealth Management Limited (consolidated)	FY2021	FY2022	Q1 FY2023
Total operating revenues	1,634	2,024	469
Profit after tax	369	582	160
Net worth	2,828	2,998	2,990
Loan book	3,620	4,384	4,335
Total AUM	2,07,044	2,61,745	2,52,038
Total assets	8,740	10,740	9,650
Return on assets	3.39%	5.97%	6.28%
Return on net worth	13.06%	19.41%	21.40%
Gross gearing (times)	1.80	1.94	1.75
Gross NPA	2.2%	-	-
Net NPA	1.8%	-	-
Gross stage 3	-	-	-
Net stage 3	-	-	-
Solvency (Net stage 3/Net worth)	-	-	-
CRAR	23.11%	23.61%	22.97%

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Sep 30, 2022 (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					Oct 12, 2022	Jan 18, 2022	-	-
1	Commercial paper programme	Short term	300	-	[ICRA]A1+	[ICRA]A1+	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Commercial paper programme	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: [Click Here](#)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
Not placed	Commercial paper programme	-	-	7-365 days	300	[ICRA]A1+

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	IIFL Wealth Ownership	Consolidation Approach
IIFL Distribution Services Limited (formerly IIFL Distribution Services Limited)	100%	Full Consolidation
IIFL Investment Adviser and Trustee Services Limited	100%	Full Consolidation
IIFL Wealth Portfolio Managers Limited	100%	Full Consolidation
IIFL Asset Management Limited	100%	Full Consolidation
IIFLW CSR Foundation	100%	Full Consolidation
IIFL Trustee Limited	100%	Full Consolidation
IIFL Wealth Prime Limited	100%	Full Consolidation
IIFL Wealth Securities IFSC Limited (w.e.f. June 22, 2018)	100%	Full Consolidation
IIFL Altire Advisors Private Limited (w.e.f. November 05, 2018) (Formerly known as Altire Advisors Private Limited)	100%	Full Consolidation
IIFL Asset Management (Mauritius) Limited (formerly known as IIFL Private Wealth (Mauritius) Limited)	100%	Full Consolidation
IIFL Inc.	100%	Full Consolidation
IIFL Capital Pte. Limited	100%	Full Consolidation
IIFL Private Wealth Management (Dubai) Limited	100%	Full Consolidation
IIFL Capital (Canada) Limited (w.e.f. November 3, 2018)	100%	Full Consolidation

Source: IIFL Wealth annual report FY2022

Note: ICRA has taken a consolidated view of the parent (IIFL Wealth), its subsidiaries and associates while assigning the rating

Corrigendum

Document dated October 12, 2022, has been corrected with revisions as detailed below:

- The link for 'Rating Approach – Consolidation' is added to the Applicable rating methodologies of the Analytical approach section on Page No. 4 of the document.

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