

IL&FS Financial Services Limited

September 08, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper programme	4,000.00	4,000.00	[ICRA]A4&; downgraded from [ICRA]A1+ and placed under watch with developing implications
Total	4,000.00	4,000.00	

& - Under rating watch with developing implications; *Instrument details are provided in Annexure-1;

Rating action

ICRA has revised the short term rating for the Rs. 4,000 crore¹ commercial paper programme of IL&FS Financial Services Limited (IFIN)² to [ICRA]A4 (pronounced ICRA A four) from [ICRA]A1+ (pronounced ICRA one plus). The rating of [ICRA]A4 is placed under rating watch with developing implications.

Rationale

The rating revision is driven by the material weakening of the company's liquidity profile in light of the sizeable debt servicing obligations coupled with the diminishing expectation of funding support from the promoter, namely, IL&FS. While ICRA has taken note of IL&FS' plans of raising Rs. 8,000 crore of funds from the promoter group (through a mix of rights issue and long-term line of credit), greater clarity is awaited on the timing of the inflows given the sizeable repayment of the group's debt, and this remains a key rating sensitivity in the near term. In compliance with the Reserve Bank Commercial Paper Directions, 2017, the company will withhold from accessing commercial paper (CP) market till February 28, 2019, which further constrains the avenues of liquidity available with the company. The rating also takes into account the credit and concentration risks associated with IFIN's wholesale funding business model, deterioration in IFIN's asset quality, consequently subdued profitability indicators and recent rise in leverage levels. The rating, however, continues to factor in IFIN's strategic importance to the IL&FS group, and the group's established track-record in development of infrastructure projects. The rating is placed under watch with developing implications taking into cognizance the group's ongoing strategic initiatives for deleveraging its balance sheet and streamlining the portfolio. The progress achieved on these endeavours, and the consequent impact on the group's financial profile would remain critical from a credit perspective.

Key rating drivers

Credit strengths

Group's track record in infrastructure-related project development - The IL&FS Group, which refers to IL&FS along with its subsidiaries, associates and joint ventures, is a diversified infrastructure developer with presence across sectors like surface transportation, urban infrastructure, energy (thermal and renewable), education, and maritime and ports. The IL&FS Group has a long history of business operations, spanning over three decades, and has been able to establish a

¹ 100 lakh = 1 crore = 10 million

² For complete rating scale and definitions, please refer to ICRA's website (www.icra.in) or other ICRA rating publications

strong brand name within this space supported by its demonstrated track record as well as domain expertise of its senior management.

Strategic importance to overall IL&FS portfolio - IL&FS considers the financial services operations to be crucial for its business and thus considers IFIN as strategically important to the Group. Given the Group's presence in the infrastructure segment, involving long-gestation capital-intensive projects, IFIN's support to the Group, in its capacity as a lender and advisor, remains critical. Additionally, IFIN remains a major source of dividend income to IL&FS. The presence of key senior executives and directors of IL&FS on the board of IFIN further underscores its relevance to the group.

Credit challenges

Deteriorations in the credit profile of the parent – The ratings of IL&FS have been revised from [ICRA]AA+&/[ICRA]A1+& to [ICRA]BB&/[ICRA]A4& driven by the rise in liquidity pressure at the group level owing to the sizeable repayment obligations. IL&FS is in the process of raising Rs. 8,000 crore of funds from its promoter group (through a mix of rights issue and long-term line of credit). ICRA notes that timely receipt of the same remains important to improve the overall liquidity profile of the company.

Relatively risky wholesale lending model with high concentration in loan-book - The company largely caters to corporates (including Group companies) operating in the infrastructure and real estate space in its lending business. IFIN's loan-portfolio increased 24% YoY to Rs. 15,398 crore as on March 31, 2018, from Rs. 12,415 crore as of March 31, 2017, driven by disbursements in the infrastructure segment. The infrastructure, promoter funding, real-estate and other segments attributed to 41%, 13% 16% and 30% respectively (share of 39%, 20%, 17% and 23% respectively as on March 31, 2017). The client concentration in the loan-book remains high with the top 10 Group exposures (excluding related party lending) attributing to 26% of the loan-book as of March 31, 2018 (28% as of March 31, 2017 and 25% of loan book as of March 31, 2016).

Deterioration in asset quality of the portfolio - The company's gross non-performing assets (NPAs) increased to Rs. 816 crore as on March 31, 2018 (5.3% of gross advances) from Rs. 410 crore as on March 31, 2017 (3.30% of gross advances) driven by certain large-sized slippages. The NPAs, after adjusting for write-off and restructured assets, however, remained largely stable assets, at 8.1% as of March 31, 2018 as compared to 7.8% as of March 31, 2017. ICRA notes that the company has created a provision for general contingency (Rs. 275 crore as on March 31, 2018 after utilizing Rs. 175 crore of the general contingency provision for making specific provisions during FY2018) in addition to the specific provision and standard asset provisions as required under RBI regulations. Given the high-risk profile of these segments, the large ticket size nature of advances and the high concentration in the portfolio, the company is more vulnerable to a lumpy deterioration in asset quality in case of any slippages.

Modest financial profile - The company's profitability, which has been reeling under pressure given the high credit costs and other provision, reported a further contraction in FY2018. The credit costs continued to remain high in FY2018 given the higher provisioning requirement due to further slippages (provision on NPA increased to Rs. 169 crore in FY2018 from Rs. 41 crore in FY2017) as well as write-off (Rs. 107 crore in FY2018). IFIN, however, utilized a part of the general contingency provision towards specific provisions during the year (of Rs. 450 crore of provision reserve as of Mar-17, Rs. 175 crore was used for making specific provisions during FY2018); should this be excluded the credit cost would have stood at 2.88% of ATA. IFIN's profit after tax (PAT) dipped to 0.48% of ATA in FY2018 from 1.1% of ATA in FY2017. On an absolute basis, IFIN reported profit after tax of Rs. 100 crore in FY2018 (4.63% of Return on equity or RoE) as against Rs. 209 crore in FY2017 (RoE of 9.91%).

Elevated debt Levels – IFIN's gearing remained elevated at 8.42 times as on March 31, 2018, (7.56 times as of March 31, 2017); the risks are aggravated considering the wholesale loan-book coupled with exposure to infrastructure sector. While the company had maintained a capital adequacy ratio of about 20% over the past few years, it declined to 17.25% as of March 31, 2018 owing to the increase in loan-book.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

[ICRA's Credit Rating Methodology for Non-Banking Finance Companies](#)

[ICRA's Approach for Rating Commercial Papers](#)

About the company

IL&FS Financial Services Limited

IL&FS Financial Services Ltd. (IFIN) is a wholly owned subsidiary of Infrastructure Leasing and Financial Services Limited (IL&FS) (rated [ICRA]BB& and [ICRA]A4&). IFIN was initially incorporated as IL&FS Asset Management Company (AMC) in 1997. After IL&FS sold the AMC business to UTI in 2004, the company obtained a NBFC license in 2005 and was renamed as IL&FS Finvest Ltd. In line with the overall strategy of the group to create distinct verticals for each business, the banking team from IL&FS and the syndication team from IL&FS Investsmart Ltd. were integrated under IL&FS Finvest Limited and subsequently the name of the integrated entity was changed to IL&FS Financial Services Ltd. IFIN commenced its new business activities in October 2006, in the various business lines like asset and structured finance business, syndication business, and corporate and project advisory business.

Key financial indicators (audited) – IL&FS Financial Services Limited

	FY2016	FY2017	FY2018
Total Income	1,921	2,346	2,294
Profit after tax (PAT)	192.78	208.78	99.66
Net Worth [^]	2,057	2,157	2,150
Total managed portfolio	12,523	12,415	15,398
Total managed assets	17,956	19,563	21,889
Return on managed assets (PAT/AMA)	1.14%	1.11%	0.48%
Return on average net worth (PAT/Avg. net worth)	9.43%	9.91%	4.63%
Gearing (times)	7.23	7.56	8.42
Gross NPA%	2.80%	3.30%	5.30%
Net NPA%	2.20%	2.36%	3.49%
Net NPA/Net worth	13.36%	13.47%	24.51%

[^]Net worth does not include preference share capital with premium; Total Debt = Borrowings + preference share capital + Interest accrued on borrowings

#AMA – average managed asset

Amounts in Rs. crore

Infrastructure Leasing and Financial Services Limited

IL&FS Limited was incorporated in 1987 with the objective of promoting infrastructure projects in the country. IL&FS was promoted by the Central Bank of India (CBI), Housing Development Finance Corporation Limited (HDFC) and Unit Trust of India (now, Specified Undertaking of Unit Trust of India - SUUTI). While SUUTI has largely exited (stake of 0.82% as on March 31, 2018), the shareholding has broadened over the years with the participation of many institutional shareholders. As on March 31, 2018, Life Insurance Corporation of India (LIC) and ORIX Corporation Japan were the largest shareholders in IL&FS with their stake holding at 25.34% and 23.54% respectively, while Abu Dhabi Investment Authority (ADIA), HDFC, CBI and SBI stake holding are at 12.56%, 9.02%, 7.67% and 6.42% respectively.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

Instrument	Type	Current Rating (FY2019)		Chronology of Rating History for the past 3 years									
		Rated amount (Rs. crore)	Amount Outstanding (Rs Crore)	FY2018			FY2017			FY2016			
				Sep-18	Sep-18	Aug-18	Mar-18	Feb-18	Nov-17	Apr-17	Apr-16	Jan-16	
1 Commercial Paper Programme	Short Term	4,000	NA	[ICRA]	[ICRA]	[ICRA]	[ICRA]	[ICRA]	[ICRA]	[ICRA]	[ICRA]	[ICRA]	[ICRA]
				A4&	A1+	A1+	A1+	A1+	A1+	A1+	A1+	A1+	A1+

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
-	Commercial Paper	NA	NA	7-365 days	4,000.00	[ICRA]A4&

Source: IL&FS Financial Services Limited

ANALYST CONTACTS

Karthik Srinivasan

+91 22 61143444

karthiks@icraindia.com

Samriddhi Chowdhary

+91 22 61143462

samriddhi.chowdhary@icraindia.com

Sainath Chandrasekaran

+91 22 61143439

sainath.chandrasekaran@icraindia.com

Parvathy S

+91 22 61143428

parvathy.s@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar

+91 22 6114 3406

shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani

Tel: +91 124 4545 860

communications@icraindia.com

Helpline for business queries:

+91-124-2866928 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 6606 9999

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