

IL&FS Securities Services Limited

October 19, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper programme	1,200.00	1,200.00	[ICRA]A1+&; placed under watch with developing implications
Short-term bank lines	350.00	350.00	[ICRA]A1+&; placed under watch with developing implications
Total	1,550.00	1,550.00	

&under rating watch with developing implications

*Instrument details are provided in Annexure-1

Rating action

ICRA has placed the rating of [ICRA]A1+ (pronounced ICRA A one plus) to the Rs. 1,200 crore¹ commercial paper programme and Rs. 350 crore short-term bank lines of IL&FS Securities Services Limited (ISSL)² under watch with developing implications.

Rationale

The short-term rating has been placed under watch with developing implications awaiting further clarity regarding the acquisition of ISSL by IndusInd Bank (IndusInd) Limited. On June 26, 2018, IndusInd announced that it had signed a definitive share purchase agreement (SPA) with Infrastructure Leasing and Financial Services Limited (IL&FS), the promoter of ISSL and other minority shareholders to acquire entire 100% shareholding in of ISSL. The transaction was subject to the receipt of certain regulatory approvals, which were received in the following months. On September 26, 2018, IndusInd informed the stock exchanges that all regulatory approvals for the acquisition were in place and the transaction was underway subject to fulfilment of all conditions precedent specified in the SPA. Given the developments at IL&FS, for instance the filing under the National Company Law Tribunal (NCLT) and the change in its board, the timelines for closure of the transaction remain uncertain. ICRA would continue to monitor the developments and take an appropriate rating action, when required.

The rating continues to factor in ISSL's its diversified revenue profile, strong market position and, its adequate capitalisation levels and liquidity profile. While the company remains exposed to volatility in the capital markets, the risk is partly mitigated by its diversified revenue streams within capital markets related services. The rating also takes into account the company's exposure to operational risks, albeit to a limited extent, its robust risk management systems and technology infrastructure provide comfort.

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

Key rating drivers

Credit strengths

Diversified revenue streams with professional clearing (PC), depository, custodian, credit portfolio management and interest income - ISSL provides a bouquet of capital market related offerings including depository, custodial, PC, credit portfolio management and back office services for small and mid-sized brokers and financial institutions. As on date, ISSL has more than 400 institutional clients. The company's fee income remains fairly diversified across functions with PCM services contributing 61% of total revenues in FY2018 followed by depository services (16%), custodial services (10%), credit portfolio management services (6%) and others (6%).

Transaction based nature of operations with limited exposure to credit risk - ISSL is engaged in various capital market related activities such as depository services, custodial services, professional clearing member and handling brokers' back office operations. These services are transactional in nature, with ISSL earning fee or commission income for the services rendered, which thus shields the company from credit risk. In addition to the fee-based income from transaction based business, ISSL also earns interest income on the deployment of margins received from the various trading members with ISSL. After placing the funds with the Exchange Houses (National Stock Exchange, Bombay Stock Exchange, Multi Commodity Exchange, MCX - SX, NCDEX and National Multi Commodity Exchange) for the margin requirement of the respective trading members, ISSL deploys excess funds in liquid mutual funds and as inter-corporate deposits to IL&FS group companies. The inter-corporate deposits to IL&FS group companies as on October 11, 2018 was Rs. 121 crore compared to Rs. 750 crore as on March 31, 2018.

Robust risk management and IT systems - ISSL has deployed robust risk management systems and technology infrastructure. It has well documented events of process / service failure and a process of regularly monitoring compliance. While most of ISSL's business operations are transaction-based with limited credit risk, its PCM operations are exposed to some element of credit risk which however, is adequately mitigated by ISSL's stringent upfront margin requirement and real time monitoring.

Liquidity profile supported by sanctioned bank lines, margin deposit and securities from clients - ISSL remains adequately capitalised with a net worth of Rs 235.48 crore as on June 30, 2018. The company's gearing (excluding margin deposits placed by trading members) increased to 4.30 times as on June 30, 2018 from 4.14 times as on March 31, 2018 on account of an increase in short-term bank borrowings and commercial papers. The total borrowings as on October 11, 2018 was Rs. 219 crore (Commercial paper of Rs. 25 crore and fund based short term bank borrowings of Rs.194 crore) compared to Rs. 1,012 crore (Commercial Papers of Rs. 868 crore and bank borrowings of Rs. 144 crore) as of June 30, 2018. The liquidity profile of ISSL however remains supported by the availability of cash margins and security collateral which can be liquidated at short notice in case of requirement, and access to unutilised credit lines.

Credit challenges

Underlying business dependant on the performance of the capital markets – ISSL's business remains dependant on the performance of the capital markets; revenues from depository operations and PC services are dependent on the volumes of transactions undertaken by their respective trading members.

Increasing competition – The competition in the professional clearing, depository and custodian business has been increasing leading to liberal margins. Large brokerage houses are becoming self-clearing members and foreign brokers have also started offering custodial services which is further increasing competition in their domain.

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 Brokerage Houses](#)

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

About the company

IL&FS Securities Services Limited

ISSL is engaged in a range of capital market related activities such as depository, custodial, and professional clearing services. Small brokerage houses avail the services of ISSL to maintain a demat account of their broking clients and to also act as a professional clearing member on their behalf. As a professional clearing member, ISSL serves as an intermediary between the brokerage houses and the exchange houses for maintaining adequate margin cover with the exchange houses on behalf of the trading members. ISSL also provides smaller brokerage houses the convenience of interaction with a single point of contact as against transacting with multiple exchange houses. Also, through ISSL, brokerage houses have a liberty to place only a single pool of margin with ISSL for all trading segments (like equity, futures & derivatives, commodity and currency futures) rather than placing separate margins for each trading segment. This helps the small brokerage houses in efficient utilisation of their financial resources.

Infrastructure Leasing & Financial Services Limited

Infrastructure Leasing & Financial Services Limited (rated [ICRA]D) 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.

Over the years IL&FS' focus has steadily shifted from project sponsorship to that of project advisory and project facilitator for development and implementation of projects. IL&FS acts as the main holding company of the IL&FS Group with most business operations domiciled in separate companies. IL&FS's Group companies are currently involved in infrastructure related project sponsorship, development & advisory, investment banking, corporate advisory, asset management and advisory services in environmental and social management, with presence across sectors like surface transportation, urban infrastructure, energy (thermal and renewable), education, maritime & ports etc.

Key financial indicators- IL&FS Securities Services Limited

	FY 2017	FY 2018	Q1 FY2019
Fee income (other than broking)	76.19	92.99	23.13
Net interest income	56.97	37.93	15.27
Other non-interest income	12.32	5.82	0.57
Operating income	145.49	136.74	38.97
Profit before tax	77.40	70.40	21.70
Profit after tax	51.02	45.08	14.29
Net worth	289.30	221.19	234.48
Return on net worth	17.64%	20.38%	24.27%
Gearing Ratio (times)	1.74	4.14	4.30

Source: Company, ICRA Research. Amounts in Rs. crore

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						
		Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Oct-18	FY2018			FY2017		FY2016	
					Jan-18	Nov-17	Jul-17	Dec-16	Oct-15	Apr-15	
1	Commercial Paper Programme	Short Term	1,200	NA	[ICRA] A1+&	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA]A1+	[ICRA]A1+
2	Short-term Bank Lines	Short Term	350	NA	[ICRA] A1+&	[ICRA] A1+	[ICRA] A1+;	-	-	-	-

&under rating watch with developing implications

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 Programme	NA	NA	7-365 days	1,200	[ICRA]A1+&
-	Short-term Fund Based Bank Lines	NA	NA	NA	100	[ICRA]A1+&
-	Short-term Non-fund Based Bank Lines	NA	NA	NA	250	[ICRA]A1+&

&under rating watch with developing implications

Source: IL&FS Securities Services Limited

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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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