

IL&FS Financial Services Limited

Instrument	Amount in INR Crores	Rating Action (<i>March 2016</i>)
Short Term Debt Programme	1,250 (Enhanced from 750)	[ICRA]A1+ Assigned

The rating of [ICRA] A1+ (pronounced ICRA A one plus) has been assigned to the Rs. ,1250 Crore (Enhanced from Rs. 750 crore) Short Term Debt Programme of IL&FS Financial Services Limited (IFIN). The rating draws support from IFIN's status as a wholly owned subsidiary of Infrastructure Leasing and Financial Services Limited (IL&FS) and consequently from the expected operational and financial support from the parent. The rating takes into account the group's substantial experience in the execution and funding of infrastructure projects, adequate risk mitigation measures, comfortable capitalisation and liquidity profile. ICRA has noted the shift in IFIN's asset profile with the company increasing the infrastructure lending book while moderating the loan against shares (LAS) book (LAS has greater linkages with the vagaries of capital markets space). ICRA has also factored in the high levels of general provisioning levels maintained by IFIN which partly alleviates concerns on the asset quality deterioration in the last two years. Going forward, IFIN's rating would be sensitive to its ability to maintain adequate margin cover and healthy asset quality indicators while scaling up its business operations.

Infrastructure lending has been the main drivers for the growth in IFIN's credit book since FY2011, with exposure to infrastructure lending increasing over years from ~23% of total customer assets (advances + investments) as on March 2011 to that of ~42% as on September 2015. While the portfolio witnessed a robust growth of 17% during FY2013, it has broadly remained static over past 2.5 years, on account of conscious curtailment by the company, given the challenging operating environment. The overall customer assets stood at Rs. 9,870 crore as on September 30, 2015. The cumulative exposure under infrastructure financing and real estate constituted more than one-half of the total customer assets of IFIN as on September 2015. The loan against shares book continued a progressive proportional decline. These loans carry 1-3 year tenure (or with put/call option at the end of 1 year). Going forward, IFIN has indicated that the scale of operations would witness a moderate growth over the medium term.

With greater lending to infrastructure segment in the last few years and the rise in general economic stress, the average internal rating of the portfolio has declined over the last 1-2 years. This combined with stagnancy in over portfolio has led to increase in the Gross NPA in percentage terms, from 1.1% as on March 2013 to 2.6% as on March 2015. While in H1 FY2016, there has been a further in the gross NPA to 3.6% as on September 2015, the management expects the asset quality indicators to improve during the latter part of the fiscal. The Net NPA for IFIN stood at 2.8% as on September 2015 post accounting for provisions against NPAs. Nevertheless, IFIN conservatively makes general contingency provision (Rs. 275 crore as on September 2015), which provide cushion against asset quality pressures (Net NPA post accounting for general contingency provisions stood at 0.02% as on September 2015).

IFIN's investment portfolio comprises its equity trading book, Private Equity (PE) investments and strategic equity investments. IFIN maintains the combined exposure to unquoted equity shares, quoted equity shares of non-group companies and units of PE funds within levels referenced to its networth.

IFIN's regulatory capital adequacy stood at an adequate 22.0% (Unaudited) (Tier 1 of 14.8%) as on September 2015 as compared to 21.6% (Tier I of 14.4%) as on March 31, 2015, primarily supported by moderate balance sheet growth. The gearing stood at 5.56 times as on September 30, 2015. The management has indicated that IFIN would maintain an overall capital adequacy of at least 20% (with significant proportion of Tier 1) as compared to the minimum regulatory requirement of 15%. In ICRA's view, with moderate growth targets and strong parentage, capital would not be a constraint for growth over near to medium term.

IFIN has a comfortable ALM profile with a positive cumulative mismatch in less than one year bucket as on September 30, 2015. IFIN maintains comfortable short term liquidity profile with large part of the loan book with residual maturity of less than one year, adequate proportion of long term borrowings and unutilised bank lines. The liquidity profile is further enhanced with IFIN having access to the surplus liquidity at the group level as the treasury operations are centrally managed.

IFIN has maintained its Net Interest Margins (NIMs) and reported Net Interest Income of Rs 406 crore during FY15, as compared to Rs 402 crore during FY14. The Profit Before Tax (PBT) of the company improved during

FY2015 to Rs. 400 crore from Rs. 355 crore in FY2014 supported by higher fee income and moderation in operating expenses despite an increase in the credit costs, while Net Profit for FY15 reported marginal decline to Rs. 249 crore (as against Rs. 265 crore for FY14) due to higher tax outflow. However, during H1 FY2016, the profitability remained subdued with reported PAT of Rs. 89 crore, on the back of decline in interest margins and increased credit costs. While IFIN's earning profile is largely dependent on a greater contribution from fee income and rise in interest income on increasing scale of operations, its operating expenses are expected to remain under control with no immediate requirement of infrastructure expansion. The profitability over the medium term will remain dependent on its ability to improve the fee income profile and to keep the credit costs under control

Company Profile

IL&FS Financial Services Ltd. (IFIN) is a wholly owned subsidiary of Infrastructure Leasing and Financial Services Limited (IL&FS) (rated [ICRA]AAA (stable) and [ICRA]A1+). 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. During FY15, IFIN booked a net profit after tax of Rs. 249 crore on a total income base of Rs 1,921 crore as compared to a net profit of Rs 265 crore on a total income base of Rs 1,815 crore in FY14. During H1 FY16, the company reported net profit of Rs. 89 crore on a total income of Rs. 909 crore.

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For further details please contact:

Analyst Contacts:

Mr. Karthik Srinivasan (Tel No +91 22 6114 3444)

karthiks@icraindia.com

Relationship Contacts:

Mr. L. Shivakumar, (Tel. No. +91 22 6114 3406)

shivakumar@icraindia.com

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**Registered Office****ICRA Limited**

1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office**Mr. Vivek Mathur**Mobile: **9871221122**Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai**Mr. L. Shivakumar**Mobile: **9821086490**Email: shivakumar@icraindia.com

3rd Floor, Electric Mansion
Appasaheb Marathe Marg, Prabhadevi
Mumbai—400025,
Board : +91-22-61796300; Fax: +91-22-24331390

Kolkata**Mr. Jayanta Roy**Mobile: **+91 9903394664**Email: jayanta@icraindia.com

A-10 & 11, 3rd Floor, FMC Fortuna
234/3A, A.J.C. Bose Road
Kolkata—700020
Tel +91-33-22876617/8839 22800008/22831411,
Fax +91-33-22870728

Chennai**Mr. Jayanta Chatterjee**Mobile: **9845022459**Email: jayantac@icraindia.com

5th Floor, Karumuttu Centre
634 Anna Salai, Nandanam
Chennai—600035
Tel: +91-44-45964300; Fax: +91-44 24343663

Bangalore**Bangalore****Mr. Jayanta Chatterjee**Mobile: **9845022459**Email: jayantac@icraindia.com

'The Millenia'
Tower B, Unit No. 1004, 10th Floor, Level 2 12-14, 1 & 2,
Murphy Road, Bangalore 560 008
Tel: +91-80-43326400; Fax: +91-80-43326409

Ahmedabad**Mr. L. Shivakumar**Mobile: **989986490**Email: shivakumar@icraindia.com

907 & 908 Sakar -II, Ellisbridge,
Ahmedabad- 380006
Tel: +91-79-26585049, 26585494, 26584924; Fax:
+91-79-25569231

Pune**Mr. L. Shivakumar**Mobile: **989986490**Email: shivakumar@icraindia.com

5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range
Hills Road, Shivajinagar, Pune-411 020
Tel: + 91-20-25561194-25560196; Fax: +91-20-
25561231

Hyderabad**Mr. Jayanta Chatterjee**Mobile: **9845022459**Email: jayantac@icraindia.com

4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj
Bhavan Road, Hyderabad—500083
Tel:- +91-40-40676500