# JM Financial Asset Reconstruction Company Private Limited

| Instrument | Amount (in INR Crores) | Rating Action (April 2016) |
|---|---|---|
| Long Term Bank Lines | 650 | [ICRA]A+ reaffirmed; Outlook revised to Positive from Stable |
| Non Convertible Debenture Programme | 525 | [ICRA]A+ reaffirmed; Outlook revised to Positive from Stable |
| Commercial Paper programme | 750 | [ICRA]A1+ reaffirmed |

ICRA has reaffirmed the credit rating of [ICRA]A+ to the Rs. 525 crore of Non Convertible Debenture Programme and Rs. 650 crore of Long Term Bank Lines of JM Financial Asset Reconstruction Company Private Limited (JMFARC). The outlook on the long term programmes has been revised to Positive from Stable. ICRA has also reaffirmed the credit rating of [ICRA]A1+ to the Rs. 750 crore Commercial Paper Programme of the company.

The revision in outlook of JM Financial Asset Reconstruction Company Private Limited (JMFARC) factors in the expectation of increase in shareholding by JM Financial Limited (rated [ICRA]AA (stable)/[ICRA]A1+), its promoter and largest shareholder (with holding of 50% as on Mar-16), which will make JMFARC a subsidiary post the proposed changes in regulations announced in Union Budget 2016-17. ICRA may upgrade the long term rating from current level once JM Financial Group acquires majority stake in JMFARC thus making it a subsidiary, while maintaining healthy recoveries from its stressed assets. Conversely, ICRA might revise the rating outlook to stable if there is reduction in JM Financial Group's stake in the company or if the pace of recoveries decreases significantly. The rating, at current level, draws comfort from the strong parentage of JM Financial Ltd and factors in the strong positioning of the company in the asset reconstruction space, its sizeable assets under management and its experienced management team. ICRA notes that JMFARC is strategically important to the JM Financial group given the shared brand name and allocation of significant resources in the form of financial as well as management support. The rating is however constrained by  the higher perceived risk of the target asset class of the company - single large credit cases and the challenges faced by this industry in continuously acquiring assets at reasonable price especially when the operating environment has become challenging after the Aug-14 guidelines of RBI requiring higher initial capital outlay as well as accounting of management fee on NAV and not on AUM which has changed the pricing expectations of the players, as well as asset quality challenges inherent in the industry it operates.

JMFARC is one of the larger players in the ARC business with AUM at Rs 8,382 crore as at December 31, 2015. The company largely operates in the large single borrower segment, perceived to be risky on account of its complexity, higher ticket size as well as levels of high degree of engagement with promoters. The AUM of the company increased significantly in Q1FY15 to ~Rs. 8,290 crore on account of a large ticket transaction to the tune of Rs. 4,100 crore. The deal was funded in part by bank lines, commercial paper borrowings as well as ICDs from JM Financial Group and other Corporates and consequently, the leverage levels too increased substantially to 3.7 times as on Jun-14. With capital infusion of ~Rs. 50 crore during FY15 and with internal accruals, the company was able to bring down the gearing to ~1.1 times as on Dec-15. The AUM of the company has remained stable in the last 18 months due to limited acquisitions and challenging operating environment.

In ICRA's view, JMFARC faces asset-quality-related challenges given its exposure to stressed assets, despite its adequate asset acquisition and resolution policy framework in place. As the company's AUM has grown primarily in the past few years, the performance of the recently acquired portfolio remains to be seen. In the current economic scenario, marked by significant pressure on cash flows of borrowers, JMFARC's ability to recover money will remain a key monitorable. The resolution performance of the company till FY2014 was good and in the range of 32-33%. However, due to acquisition of a lumpy account during Q1FY15, the overall assets resolved till Mar-15 as a percentage of assets acquired reduced to 23-24%. During 9MFY2016, the recoveries improved and as per the management, additional recoveries from this stressed asset will happen over the next 12-18 months which will further improve the recovery track record.

During 9MFY2016, the income levels of the company increased considerably due to sizable profit on redemption/sale of SRs during the period. Over the years, the income profile of the company has remained dominated by Management Fees and Interest income from loans given for restructuring. Total Income of the company increased to Rs. 311.73 crore during 9MFY2016 from Rs. 214.35 crore during FY2015. Total borrowings of the company declined during 9MFY2016 and hence the interest expenses reduced during the period. The operating expenses of the company remained stable at Rs. 37.17 crore during 9MFY2016 vis-à-vis Rs. 31.75 crore during FY2015. With an increase in revenues and stable expenses, the net profit of the company increased to Rs. 98.93 crore during 9MFY2016 (RoE of 28.31%) from Rs. 36.20 crore in FY2015 (RoE of 9.69%).

**Company Profile**

JMFARC was incorporated in September 2007 by JM Financial Ltd which holds 50 per cent stake in JMFARC, with the balance held by Mr. Narotam Sekhsaria (15 per cent), Valiant Mauritius Partners FDI Ltd (8.42 per cent), four public sector banks (20.72 per cent) and Others (5.86 per cent). During FY2015, JMFARC reported a PAT of Rs. 36 crore on a total income base of Rs. 212 crore as compared to a PAT of Rs. 48 crore on a total income of Rs. 120 crore for FY2014. JMFARC reported PAT of Rs. 98.93 crore on a total income base of Rs. 311.73 crore for 9MFY2016.

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