

Reliance Capital Limited

April 26, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper programme	4,000.00	1,200.00	[ICRA]A4@; downgraded from [ICRA]A2@; Continues to be on Watch with Negative Implications
Total	4,000.00	1,200.00	

@On rating Watch with Negative Implications

*Instrument details are provided in Annexure-1

Rationale

ICRA has downgraded the short term -rating for various instruments of Reliance Capital Limited (RCL) and its subsidiaries to [ICRA]A4@ (pronounced ICRA A four) from [ICRA] A2@ (pronounced ICRA A two). The ratings continue to be on Watch with Negative Implications.

The rating downgrade reflects the slow pace of monetisation of RCL's non-core investments (non-financial services businesses), and consequently no improvement in liquidity. In addition, the liquidity of key operating subsidiaries, i.e. RCFL and RHFL also remains stretched as was earlier highlighted in rating rationale whereby the debt repayments in the next six months are higher than scheduled inflows.

In addition, the visibility of raising funds by the parent is lower than prior expectations. With weakening financial flexibility amidst large quantum of borrowings due for repayment in the near term, the timeliness of receipt of funds from divestments of some of its potentially core and non-core investments remains critical. At the same time, while the management remains confident, they have not provided clarity on the timely recoverability of funds extended to certain groups by RCFL and RHFL, and also the funds extended to the Reliance group by RCL, which now is critical to ensure timely repayment of debt obligations.

ICRA notes that while RCFL and RHFL have been able to raise funds in the securitisation market in the past six months, their respective current on-balance sheet liquidity is low in relation to the size of borrowings. RCL's key NBFC subsidiaries, RCFL and RHFL, have witnessed an increase in exposure towards higher ticket-size loans to some companies. The exposures are concentrated, and the top 10 exposures for RCFL contribute to ~21% of total AUM as of December 31,2018. The top 10 exposures for RHFL contribute to 11% of total AUM as of December 31,2018 ICRA also notes that Reliance Communications Limited (rated ICRA [D]) has filed for bankruptcy proceedings in the National Company Law Tribunal (NCLT) and overall, Reliance ADAG group companies have been under financial stress.

The rating continues to factor in RCL's status as a holding company for its financial services businesses, which have a presence across various verticals like asset management, life insurance, general insurance, commercial and home finance, broking and distribution of financial products and proprietary investments. The rating also takes into consideration RCL's experienced management profile with varied experience across financial services segments. ICRA notes that RCL has substantial exposure towards the ADAG group's various non-financial companies in the media, entertainment and infrastructure businesses. RCL has been making efforts to divest some of its core and non-core investments to reduce its debt. The divestment schedule was affected in CY2018 by the adverse capital market movements and the liquidity crunch faced by the NBFC sector post September 2018.

ICRA takes note of RCL's moderate profitability indicators. Going forward, RCL's ability to successfully and timely monetise some of its investment exposures in its media and entertainment businesses and shore up its liquidity profile would continue to be a key rating monitorable.

RCL's lending business entities, RCFL & RHFL reported a significant decline in its retail disbursements in Q3 FY2019 amid tightening liquidity for the company and significant debt repayments during September 2018 to February 2019. The liquidity position continues to be moderate going forward, given significant debt repayments due over the course of next six months, at standalone RCL level, as well at RCFL's & RHFL's standalone level. ICRA, however, notes that the company has been regular in meeting all its debt obligations and has raised funds through sizeable securitisation and assignment of loan assets ~Rs. 7200 crore since September 2018.

The ratings are on Rating Watch with Negative Implications due to the longer time frame taken to monetise non-core investments at RCL and reduction in financial flexibility at RCL and its lending subsidiaries. ICRA will closely monitor the progress in terms of divesting its core and non-core assets to improve upon its liquidity profile.

Outlook: Not applicable

Key rating drivers

Credit strengths

Diversified financial services group with presence in lending, asset management, insurance and capital market activities (broking and financial products distribution) – RCL has wholly owned subsidiaries which are into secured lending businesses –RHFL, a housing finance company under which home loans (including affordable housing loans), while construction finance, Loan against Property (LAP) loans and SME loans are booked at RCFL. Further, RCL's asset management, general and life insurance businesses continue to be leading players in their respective industries, which together with the lending businesses offer considerable financial flexibility and diversity of business streams to RCL.

Large core financial assets which are on book value in RCL's investment book in addition there is a sustained effort to monetise the non-core investments – There is a potential value unlocking in the core operating finance companies, but a critical aspect of the timing of inflows is uncertain. In addition, the quantum of recoveries from the non-core investments remain uncertain, especially in face of ~Rs. 6,700 crore provisioning done in Q2FY2019. RCL continues to have a sizeable investment book of ~Rs 23,120 crore as on December 31, 2018 primarily in the form of equity and compulsory convertible debentures in group companies. In addition, the company also has ~ Rs. 10,552 crore of loans to group companies. The company has indicated that the longer-term strategy would be to exit the non-core investments. The company expects proceeds from assets sale in the following businesses: sale of its Radio business, stake sale in Reliance Nippon Asset Management Company Limited (RNAM) to Nippon Life Insurance, monetisation of its stake in Reliance General Insurance Company Limited (RGICL) via an offer for sale to the extent of 49%, listing of the U.K. subsidiary of Prime Focus Limited

(held by Reliance Mediaworks) and monetising its remaining stake in Codemasters. However, despite the decrease in non-core investments in RCL portfolio, ICRA notes the increase in large ticket loans in the books of RCFL, and RHFL.

Credit challenges

High consolidated gearing level on account of networth write-off as part of Ind-AS transition – The entity has a moderate gearing level of 1.50 times at a standalone level as on September 30, 2018 vis-à-vis 1.52 times as on March 31, 2018. However, at a consolidated level, the gearing increased sharply to 5.10 as on September 30, 2018 vis-à-vis 2.26 as on March 31, 2018 as the company had fairly valued its investments and written off ~Rs. 6,700 crore of its consolidated networth as part of transitioning to Ind-AS.'s capital adequacy at the stand-alone level stood at 32% as on December 31, 2018. Given sizeable investments in non-core assets of group company in relation to its networth, it must be noted that the standalone net worth of RCL can adversely get impacted in case these investments could not be recovered at later date or are further marked down given the considerable delays in monetisation of these investments.

Profitability subject to gain on divestments on core/non-core assets; any write-offs because of non-recoverability of non-core investments leading to write-off remains a sensitivity – RCL's standalone income is driven by divestment income and interest income on investments/advances to group entities. Standalone Profit Before Taxes in FY2018 was supported by stake sale in Reliance Nippon Asset Management Limited. RCL got Rs. 378 crore from stake sale to Reliance Nippon Life and subsequently, ~Rs 273 crore from offer for sale in IPO, resulting in a total gain of Rs. 651 crore. Overall the company on standalone basis reported a PAT/ATA of 1.69% in H1FY2019 as compared to 2.37% in FY2018, on account of lower income from profit from sale of investments in H1FY2019.

RCL's reported a consolidated PAT of Rs. 246 crore in Q3FY2019, as against Rs. 309 crore in Q2FY2019, and Rs. 39 crore in Q3FY2018. For 9MFY2019, PAT stood at Rs. 850 crore, as against a loss of Rs. 478 crore in 9MFY2018 (Rs. 881 crore profit as per iGAAP) due to impact of ECL provisioning and fair valuation of investments as per Ind-AS.

Exposure to non-core group entities – RCL has total investments and advances of Rs 13,748 crore towards non-core group companies and exceeds the standalone net worth of RCL. RCL's continued equity, fund-based & non-fund based exposure towards the Reliance Group's various non-financial companies in the media, entertainment & infrastructure businesses, and a slow progress on the monetisation of these assets diminishes the financial flexibility of the company in raising fresh funds as well as its capability to service its near-term debt obligations. In addition, ICRA notes that the RCL had ~Rs. 1,584 crore of exposure to a group company, i.e. Reliance Communications Limited which has been recently referred for insolvency proceedings and the company has fully provisioned for this loan. In addition, the exposure to other group companies like Reliance Power is around ~Rs. 1,500 crore. The other investments in media and entertainment etc are also towards loss making entities. Recoverability of these exposures remain uncertain given the financial position of these companies.

Moderating liquidity profile and low funding flexibility- RCL's balance sheet liquidity is modest in relation to the size of its borrowings and quantum of maturing liabilities. However, ICRA notes that the company has been regular in meeting all its debt obligations and its subsidiaries have raised funds through sizeable securitisation and assignment of loan assets (~Rs. 7,200 crore raised since H1FY2019).

Apart from income from divestments, if any; RCL's income stream comprises of interest and dividend income up streamed by operating as well as non-operating group entities to which RCL has exposure via debt and equity investments, as well as direct loans and advances extended to them. its critical for the company to be able to realize the value of its core as well as non-core investments and remains one of the key rating sensitivities. Reliance Communications Limited (rated ICRA [D]) has filed for bankruptcy proceedings in the National Company Law Tribunal (NCLT) and the overall financial stress to

the Reliance group companies is weak. In addition, due to the adverse market environment for the wholesale borrowing market, RCL has limited avenues for raising funding (as being a NBFC-CIC, it cannot raise bank borrowings to fund equity investments), and the absence of raising any longer term debt in the last six months.

Liquidity Position:

RCL Group’s lending companies, RCFL & RHFL, have been able to manage their liquidity position largely through the securitization market (Pass through certificates, and direct assignments of loans) apart from inflows from maturity of their advances. RCL has lent to its non-operating subsidiaries directly, or by way of Compulsorily Convertible Debentures (CCD), where some of the corporate loan exposures were transferred. The proceeds from these corporate loans are up streamed to RCL as dividends, and on direct loans RCL receives interest and principal repayments, which in turn it uses to meet its debt obligations. The corporate loan has been on a run-down mode over the past one year and supported RCL’s liquidity at a standalone level. However, going forward the role of asset monetization becomes even more critical for RCL to meet its debt obligations. With limited fresh business generation and sizeable securitization and assignment of loan assets, the pool eligible for sell down has also been declining, thereby reducing RHFL and RCFL’s ability to refinance through securitization.

As on March 31, 2019 RCL has a liquidity cushion of around Rs. 48 crore in the form of unencumbered cash and deposits, as well as estimated inflows of ~Rs. 1,584 crore in April 2019, Rs. 59 crore in April 2019 and Rs. 31 crore in June 2019 (largely interest repayments on the loans and debentures to the group companies). The liquidity profile is tight in relation to the near-term debt maturities (borrowings of ~Rs. 613 crore still due for maturity in April 2019, and ~Rs 1,800 crore maturing by June 2019).

RCL expects proceeds from sale of its Radio business, stake sale in Reliance Nippon Asset Management Company Limited (RNAM) to Nippon Life Insurance, monetisation of its stake in Reliance General Insurance Company Limited (RGICL) via an offer for sale to the extent of 49%, etc. These proceeds if completed in a timely manner will shore up RCL’s liquidity buffer and enable it to service its debt in a timely manner.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA’s Credit Rating Methodology for Non-Banking Finance Companies
Parent/Group Support	Parent / Investor: Not Applicable
Consolidation / Standalone	While arriving at the rating for Reliance Capital Limited (RCL), ICRA has considered the consolidated performance of RCL and its subsidiaries carrying businesses as finance companies (namely Reliance Commercial Finance Limited, Reliance Home Finance Limited, Reliance Financial Limited, Reliance Asset Reconstruction Company Limited, Reliance Commodities Limited & Reliance Securities Limited, collectively referred to RCL group) given the strong operational and financial synergies between the companies.

About the company

Reliance Capital Limited (RCL) is a part of the Reliance group. RCL’s subsidiaries have a significant presence across various financial services businesses like Asset Management, Life Insurance, General Insurance, Commercial & Home Finance,

Broking & Distribution of financial products and Proprietary Investments. RCL is a Core Investment Company with investments in group as well as non-group entities.

RCL's reported a consolidated PAT of Rs. 246 crore in Q3FY2019, as against Rs. 309 crore in Q2FY2019, and Rs 39 crore in Q3FY2018. For 9MFY2019, PAT stood at Rs. 850 crore, as against a loss of Rs. 478 crore (Rs. 881 crore profit as per iGAAP) due to impact of ECL provisioning and fair valuation of investments as per Ind-AS.

Key Financial Indicators

RCL (Standalone)	FY2017	FY2018	H1FY2019
Net Operating Income	202	467.00	308.00
Profit on sale on investments	253	774.00	0
Profit after tax	419	828.00	308.00
Networth	13,701	14,168	13,289
Investment Book	18,834	21,108	23,272
Total assets	33,266	36,352	36,697
Return on assets	1.20%	2.37%	1.69%
Return on equity	3.11%	5.94%	4.49%
Capital adequacy ratio	38.0%	47.00%	31.69%#
Gearing	1.41	1.52	1.75

Amounts in Rs. Crore, ratios as per ICRA calculations

**Annualised,*

as on December 31, 2019

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2020)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Apr-19	FY2019		FY2018	FY2017	
						Mar-19	Mar-19	Feb-18	Nov-16	Apr-16
1	Commercial Paper Programme	Short term	1,200.00	NA	[ICRA]A4@; downgraded from A2@	[ICRA]A2@	[ICRA]A1@	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

@On rating Watch with Negative 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
NA	Commercial Paper Programme	NA	NA	7-365 days	1,200.00	[ICRA]A4@

Source: Company Data

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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

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