

## Annexure I

### Rationale

#### IL & FS Financial Services Ltd.

#### Ratings

Instrument/Facilities	Amount (Rs. crore)	Ratings <sup>1</sup>	Remarks
Subordinated Debt	100	CARE AAA (Triple A)	Assigned
Non Convertible Debentures	500	CARE AAA (Triple A)	Assigned

#### Rating Rationale

*The ratings factor in IFIN's strong parentage as well as operational, managerial and financial support from IL&FS. The ratings also factor in healthy capitalisation levels, moderate gearing, reduced exposure to the promoter financing segment, strong risk management systems which draw linkage to its parent, comfortable liquidity position and comfortable asset quality. Continued support from the parent IL&FS, asset quality and profitability are the key rating sensitivities.*

#### Background

Incorporated in September 1995, IL&FS Financial Services Ltd. (IFIN) is a 100% subsidiary of IL&FS Ltd. IFIN's business profile is broadly divided into investment banking business (asset and structured finance), Project debt syndication business, Corporate advisory services business and project finance advisory. As on June 30, 2012, IFIN had a balance sheet size of Rs.11,885 crore with a networth of Rs.1,646 crore.

IFIN has an international presence through its fully-owned subsidiaries in Singapore, United Kingdom and Dubai. These subsidiaries were set up mainly to assist corporates for their overseas borrowing, through private equity syndication and advisory services. During FY12 (refers to the period April 2011 to March 2012), IFIN has set up a wholly-owned subsidiary in Hong Kong, IL&FS Global Financial Services (HK) Ltd.

<sup>1</sup> Complete definitions of the ratings assigned are available at [www.careratings.com](http://www.careratings.com) and in other CARE publications

## Credit Risk Assessment

### ***Strong parentage***

IFIN is the wholly-owned subsidiary of IL&FS, one of India's leading infrastructure development companies and rated CARE AAA. By virtue of being the wholly-owned subsidiary of IL&FS, IFIN enjoys high financial flexibility in addition to benefits arising from group synergies. The rating further derives strength from the operational and managerial support extended to it by IL&FS.

### ***Robust capitalisation levels***

IFIN continues to have robust capitalisation levels, with overall CAR being 21.33% [Tier I CAR: 14.71%] as on June 30, 2012. Higher Tier I capital will provide sufficient headroom to IFIN for raising Tier II capital which shall enable it to fund the asset book growth. As on June 30, 2012, IFIN's overall gearing stood at moderate 5.82x.

### ***Reduced exposure to the promoter financing (PF) segment***

In continuation to the trend witnessed since the last few years, IFIN has been consciously curtailing its exposure to promoter funding segment and has instead been focusing on infrastructure lending. Although the composition of real estate backed loans in the total lending mix has remained stable, the promoter funding exposure has steadily declined from 46% as on March 31, 2010, to 30% as on March 31, 2012. On the other hand, proportion of infrastructure loans has significantly increased from 15% as on March 31, 2010, to 37% as on March 31, 2012.

### ***Comfortable liquidity position***

IFIN's liquidity profile is characterized by negative cumulative mismatches in short to medium time buckets on account of rise in the proportion of medium to long-term infrastructure loans over the past few years as well as rise in the medium-long-term investments/ credit substitutes (in the form of equity shares and NCDs). However, in order to match the medium-term nature of lending, IFIN has been consciously trying to reduce reliance on the short-term borrowings. During FY12, the proportion of long-term borrowings (comprising bank loans and subordinated debt) in the resources profile increased to 83% as on March 31, 2012 [P.Y.: 77%]. Besides, parent support, moderate gearing as well as strong resource raising ability will enable it to contain any temporary mismatches.

### ***Repricing risk***

The interest rate sensitivity statement of the company exhibits cumulative gaps in one-year time frame. Despite the significant rise in the proportion of loan book on floating rates to 73% as on March 31, 2012 [P.Y.:53%], the repricing risk in one-year time frame has risen

primarily on account of significant rise in the infrastructure lending. In case of infrastructure loans, loan resets on fresh disbursements happen only after the completion of the initial year and a significant portion of the loan book built up has taken place in H2FY12. In addition, considering that further rise in interest rates seems to be unlikely, declining interest rates coupled with repricing of infrastructure loans in Q3 FY13 is expected to have a positive impact on IFIN's margins.

#### ***Improving asset quality***

Over the last few years, IFIN has been able to maintain sound asset quality. Since FY08, the NPA levels of the company have largely remained stable in absolute terms. However, during FY11, there was rise in NPAs primarily on account of the slippage in one large account. Recovery in case of the aforementioned account has led to improvement in the asset quality. As on June 30, 2012, the GNPA and NNPA ratios improved to 0.58% and 0.42%, respectively; net NPA/ networth being 2.24%.

#### ***Risk management***

Risk management systems play a critical role since majority of IFIN's funding is towards big ticket loans. IFIN has concentration risk with top 15 individual borrowers constituting approximately 34.3% [P.Y.: 39.9%] of the total portfolio. However, the asset quality risk is somewhat mitigated given its parent's expertise in credit appraisal and execution of infrastructure projects. As a result, the company continues to report comfortable asset quality. In order to counter the risk arising from its borrower concentration in the promoter funding, the company maintains an average share cover of around 2x. As on March 31, 2012, IFIN had average cover of 2.74x [P.Y.: 2.38x] on its top 15 promoter funding clients.

#### ***Continued subdued financial performance***

During FY12, the company witnessed a strong 46% yoy growth during FY12, primarily on the back of robust loan portfolio growth at higher yields. Loan book (including credit substitutes) increased by 41.5% to Rs.8,470 crore as on March 31, 2012 [P.Y.: Rs.5,987 crore]. However, despite the healthy loan growth and higher portfolio yields, IFIN's margins declined by 93 bps to 3.11% during FY12 on account of the following: a) In case of infrastructure loans, loan resets on fresh disbursements happen only after the completion of the initial year and since a significant portion of the loan book built up has taken place in H2FY12, the company has been unable to pass on higher borrowing costs. The company expects such loans to reset during Q3 FY13. b) During the last two years, there has been a shift in the lending portfolio from high yielding real estate backed and the promoter funding

loans to infrastructure loans which carry relatively lower spreads and c) the company has consciously refrained from passing on higher borrowing costs partly to prevent asset quality concerns.

9 Higher borrowing costs have offset the robust fund-based income growth and operational efficiencies, thereby resulting into 21% yoy decline in profits to Rs.256 crore during FY12. On a sequential basis, annualized margins and other profitability parameters continued to slide, given the high borrowing costs and limited repricing ability. During Q1FY13, IFIN reported PAT of Rs.34 crore, down by 19% on y-o-y basis.



## Standalone Financials

(Rs. Crore)

Particulars as on / for the period ended	FY10	FY11	FY12
Interest Income	748	760	1165
Interest Expenses	412	455	860
<b>Net Interest Income</b>	<b>336</b>	<b>305</b>	<b>305</b>
Other Fund Based Income	128	83	65
<b>Total fund based income</b>	<b>876</b>	<b>843</b>	<b>1230</b>
Fee Income	155	258	194
Other income	3	5	3
<b>Total Income</b>	<b>1034</b>	<b>1106</b>	<b>1427</b>
Operating Expenses	108	108	118
Provisions	46	66	69
PBT	467	471	377
<b>PAT</b>	<b>315</b>	<b>326</b>	<b>256</b>
Total Assets	6694	8408	11230
Loans & advances	4093	4945	7424
Investments	1432	2517	3138
<b>Tangible Networth</b>	<b>1381</b>	<b>1529</b>	<b>1611</b>
<b>Borrowings</b>	<b>4660</b>	<b>6178</b>	<b>8855</b>
<b>Key Ratios (%)</b>			
Int. income/ avg. Int. earning assets	16.44	14.35	16.74
Int. expense/ avg. Int. bearing liabilities	8.67	8.40	11.44
<b>Interest Spread</b>	<b>7.77</b>	<b>5.95</b>	<b>5.30</b>
<b>NIM</b>	<b>5.05</b>	<b>4.04</b>	<b>3.11</b>
<b>ROTA</b>	<b>4.73</b>	<b>4.31</b>	<b>2.60</b>
Overall Debt / Networth (times)	3.37	4.04	5.50
<b>CAR</b>	<b>25.99</b>	<b>21.19</b>	<b>20.24</b>
<b>Tier I CAR</b>	<b>24.74</b>	<b>19.94</b>	<b>15.21</b>
Interest coverage (after provisions & tax)	1.76	1.72	1.30
Fee income / total income	14.95	23.39	13.58
Oper. Expns./Av.Total Assets	1.62	1.50	1.24
Gross NPA (%)	1.57	1.72	0.60
Net NPA (%)	0.74	1.44	0.44
Net NPA to Networth (%)	2.17	5.59	2.29

### Disclaimer

CARE's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CARE has based its ratings on information obtained from sources believed by it to be accurate and reliable. CARE does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CARE have paid a credit rating fee, based on the amount and type of bank facilities/instruments.

Credit Analysis and Research Limited proposes, subject to receipt of requisite approvals, market conditions and other considerations, to make an initial public offer of its equity shares and has filed a draft red herring prospectus ("DRHP") with the Securities and Exchange Board of India (the "SEBI"). The DRHP is available on the website of SEBI at [www.sebi.gov.in](http://www.sebi.gov.in) as well as on the websites of the Book Running Lead Managers at [www.investmentbank.kotak.com](http://www.investmentbank.kotak.com), [www.dspml.com](http://www.dspml.com), [www.edelcap.com](http://www.edelcap.com), [www.icicisecurities.com](http://www.icicisecurities.com), [www.idbicapital.com](http://www.idbicapital.com), and [www.sbicaps.com](http://www.sbicaps.com). Investors should note that investment in equity shares involves a high degree of risk and for details relating to the same, see the section titled "Risk Factors" of the DRHP.

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## Annexure II

### Press Release

#### CARE assigns 'CARE AAA' to Long term debt instruments of IL&FS Financial Services Ltd.

#### Ratings

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During FY12, IFIN witnessed robust 50% y-o-y [P.Y.: 21%] loan book growth with major focus on infrastructure lending. IFIN's infrastructure lending has grown significantly in the

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past two years and comprised 37% of its loan portfolio as on March 31, 2012. Loan book (including credit substitutes) stood at Rs.8,470 crore as on March 31, 2012 [P.Y.: Rs.5987 crore]. During FY12, the company witnessed a strong 46% yoy growth in its fund-based income, primarily on the back of robust loan portfolio growth at higher yields. However, despite the healthy loan growth and higher portfolio yields, IFIN's margins declined during FY12 primarily due to the shift in the lending portfolio from high-yielding real estate backed loans and promoter funding loans to infrastructure loans which carry relatively lower spreads. Higher borrowing costs have offset the robust fund-based income growth, thereby resulting in 21% yoy decline in profits to Rs.256 crore during FY12.

During Q1FY13, IFIN reported PAT of Rs.34 crore, down by 19% on y-o-y basis. The company continued to report comfortable asset quality parameters. As on June 30, 2012, the GNPA and NNPA ratios improved to 0.58% and 0.42%, respectively; net NPA/ networth being 2.24%. IFIN reported healthy capitalisation levels with overall CAR being 21.33% [Tier I CAR: 14.71%] as on June 30, 2012. IFIN's overall gearing stood at moderate 5.82x as on June 30, 2012.

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*CARE has classified instruments rated by it on the basis of complexity. This classification is available at [www.careratings.com](http://www.careratings.com). Investors/market intermediaries/regulators or others are welcome to write to [care@careratings.com](mailto:care@careratings.com) for any clarifications.*

#### **Disclaimer**

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Credit Analysis and Research Limited proposes, subject to receipt of requisite approvals, market conditions and other considerations, to make an initial public offer of its equity shares and has filed a draft red herring prospectus ("DRHP") with the Securities and Exchange Board of India (the "SEBI"). The DRHP is available on the website of SEBI at [www.sebi.gov.in](http://www.sebi.gov.in) as well as on the websites of the Book Running Lead Managers at [www.investmentbank.kotak.com](http://www.investmentbank.kotak.com), [www.dspml.com](http://www.dspml.com), [www.edelcap.com](http://www.edelcap.com), [www.icicisecurities.com](http://www.icicisecurities.com), [www.idbicapital.com](http://www.idbicapital.com), and [www.sbicaps.com](http://www.sbicaps.com). Investors should note that investment in equity shares involves a high degree of risk and for details relating to the same, see the section titled "Risk Factors" of the DRHP.

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