

Fitch Ratings

IL&FS Affirmed at 'Fitch AAA(ind)'/Stable Ratings

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Fitch Ratings-Mumbai/Singapore-21 November 2011: Fitch Ratings has affirmed India-based Infrastructure Leasing & Financial Services Limited's (IL&FS) National Long-Term rating at 'Fitch AAA(ind)' with a Stable Outlook and its National Short-Term rating at 'Fitch A1+(ind)'. The agency has also affirmed the National Short-Term rating of IL&FS Financial Services Ltd. (I-Fin, 100% owned by IL&FS) at 'Fitch A1+(ind)'. A list of additional rating actions is provided at the end of this commentary.

IL&FS's ratings reflect its strong financial profile based on an established franchise and management expertise in India's infrastructure sector. The company's above-average profitability is supported by the group's established track record of sponsoring projects in the road, power and port sectors and subsequent divestments of some of its holdings, along with a diversified fee income. Fitch expects IL&FS's growing leverage to fall by March 2012 due to expected sizeable divestments in the power business. The company historically had high asset quality, and its specific and contingency reserves should cushion any possible stress on its asset portfolio from the current economic downturn.

IL&FS's equity/assets ratio, though on a declining trend since FY08, was high at 28.6% at end-March 2011. Fitch notes while IL&FS predominantly relies on institutional funds, it has progressively diversified its funding sources and maintained a better asset-liability framework by extending the tenor of its borrowings. This helps in mitigating the risks for such wholesale-funded institutions.

IL&FS's high but distinct exposures to various infrastructure sectors and its divestment-led business model expose the company to concentration risks that are not typically associated with a 'Fitch AAA(ind)'-rated entity. In recognition of this, Fitch expects IL&FS to continue to manage its capital and liquidity conservatively. Negative rating action may result if Fitch assesses these risks or the level of complexity in the business becomes inconsistent with the existing rating level. Weaker economic conditions having a relatively greater negative impact on IL&FS compared to similarly rated entities would also be negative for the ratings.

Over the years, the IL&FS group has morphed from a non-banking financial company to a predominantly infrastructure company, and periodic divestments have formed the principal part of its earnings in recent years. As a result, IL&FS has transformed into a quasi-holding company and has applied to the Reserve Bank of India to be classified as a 'core investment company'.

I-Fin's rating is equalised with that of IL&FS to reflect its strong operational and management linkages with its parent, of which it was a division till FY08. I-Fin's treasury and risk management are centralised at IL&FS, and its debt syndication desk provides critical support to the parent's project development business. In FY11, I-Fin was IL&FS's most profitable subsidiary and accounted for 60% of group company dividends received by the parent; IL&FS expects to continue holding 100% shareholding in future. Any dilution in ownership together with a re-evaluation of I-Fin's strategic importance to IL&FS may lead to the de-linking of the long-term ratings of the two companies.

IL&FS's lower tier 2 subordinated bonds have been rated at the same level as its National Long-Term rating based on Fitch's "Criteria for Indian National Ratings of Bank Hybrids and Subordinated Debt", dated 18 January 2010.

IL&FS' issue ratings affirmed by Fitch:

- INR16.45bn long-term debt: 'Fitch AAA(ind)'
- INR2.2bn lower tier 2 subordinated debt: 'Fitch AAA(ind)'
- INR7.2bn short-term debt: 'Fitch A1+(ind)'

I-Fin's issue rated by Fitch:

- INR7bn short-term debt: affirmed at 'Fitch A1+(ind)'
- INR2bn long-term debt: assigned at 'Fitch AAA(ind)'

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Note to editors: Fitch's National ratings provide a relative measure of creditworthiness for rated entities in countries with relatively low international sovereign ratings and where there is demand for such ratings. The best risk within a country is rated 'AAA' and other credits are rated only relative to this risk. National ratings are designed for use mainly by local investors in local markets and are signified by the addition of an identifier for the country concerned, such as 'Fitch AAA (ind)' for National ratings in India. Specific letter grades are not therefore internationally comparable.

In accordance with Fitch's policies the issuer appealed and provided additional information to Fitch that resulted in a rating action that is different than the original rating committee outcome.

Additional information is available at www.fitchratings.com. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable criteria, "Global Financial Institutions Rating Criteria," dated 16 August 2011; "National Ratings Criteria," dated 19 January 2011 and "Criteria for Indian National Ratings of Bank Hybrids and Subordinated Debt," dated 18 January 2010, are available at www.fitchratings.com.

Applicable Criteria and Related Research:
Global Financial Institutions Rating Criteria
National Ratings Criteria
Criteria for Indian National Ratings of Bank Hybrids and Subordinated Debt

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