

## Ind-Ra Assigns I-Fin's and IL&FS' Proposed NCDs 'IND AAA'/Stable

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India Ratings and Research (Ind-Ra) has assigned IL&FS Financial Services Ltd's (I-Fin) additional proposed INR3bn non-convertible debentures (NCDs) an 'IND AAA' rating with a Stable Outlook. The agency has also assigned Infrastructure Leasing & Financial Services Ltd's (IL&FS) additional proposed INR10bn NCDs an 'IND AAA' rating with a Stable Outlook and its additional proposed INR5bn short-term debt an 'IND A1+' rating. I-Fin is 100% owned by IL&FS. A list of IL&FS' and I-Fin's outstanding ratings is at the end of this commentary.

### Key Rating Drivers

I-Fin's rating is equated with that of IL&FS as it is considered core to IL&FS' business. I-Fin, which was a division of IL&FS till 2008, has strong operational and management linkages with its parent, and its treasury and risk management are centralised at IL&FS. Its debt syndication desk provides critical support to the groups' project development business. I-Fin accounted for about 60% of the group company dividends received by the parent in FY14 and FY15, accounting for about 27% of IL&FS's revenue (net of interest expense and preference dividend) in FY15 (FY14: 20%); IL&FS expects to continue holding 100% shareholding in I-Fin.

IL&FS' ratings reflect its steady competitiveness, established franchise, proven operating track record, management strength and its unique positioning in the infrastructure space in India. The IL&FS group's competencies encompass project advisory, sponsoring and development in initial phases as well as funding and operating projects, which enhance its competitiveness. IL&FS' financial leverage, though has increased, compares favourably with that of traditional financial companies as the regulation caps financial leverage at moderate levels for core investment companies (CICs). The regulation also mandates 90% of assets of a CIC to be as investments in group companies in the form of equity or loans.

Nevertheless, IL&FS being a CIC carries a concentrated asset portfolio with high single name exposures. Also, a significant part (around three-fourths) of its equity investments is in the development stage. The harsh operating environment over last few years has impeded divestments, resulting in a continuous deferral in the planned deleveraging of the balance sheet, and impacted profitability. These delayed divestments together with current slide in the valuation of its listed investments - 50% of the excess of an increase in market value over invested amount is allowed by CIC regulation to be included in net worth in leverage calculation - have resulted in high regulatory leverage.

The current leverage levels are now likely to be close to the regulatory ceilings. The company has reported that it has completed a part stake sale in its renewable business which was critical to bring down its FY16 year-end regulatory leverage levels. The company has also provided a roadmap to continue the process of deleveraging in FY17 through equity infusion and divestments. The company's contingent loss reserves at 3.7% of assets at end-September 2015, though reduced (FY15: 4.1%, FY14: 4.8%) provide some cushion for unforeseen losses on its exposures.

IL&FS' derives its revenue primarily from interest income from loans to its group companies and dividend income (primarily from I-Fin and IL&FS Transportation Networks Ltd ('IND A'/Stable)), while intermittent divestments boost its profitability. Nevertheless, the profitability of the company has suffered as divestment income squeezed. Most of the reported profit of FY15 was accrued through the sale of one of its investments in a power venture (arrived at a fair price) to its subsidiary in the energy vertical.

IL&FS predominantly relies on institutional funding from diversified domestic sources. The company manages its liquidity judiciously with largely long-ended debt resulting in matched assets and liability tenures. The company's liquidity is comfortable as gaps in less than one-year buckets of structural liquidity statement (committed inflows less committed outflows) are

manageable. The refinancing risk on account of disruptions in the institutional bond market is reduced by maintaining reasonable liquidity to meet contingent repayment obligations in the short term.

## Rating Sensitivities

I-Fin: Any dilution in the ownership together with a re-evaluation of I-Fin's importance to IL&FS could lead to the de-linking of the long-term ratings of the two companies.

IL&FS: Continued pressure on the leverage ratios together with an assessment by the agency of the ability of the company to maintain improved capital ratios on a sustained basis could result in a downward rating movement.

The lower Tier 2 subordinated bonds have been rated at the same level as the long-term ratings based on Ind-Ra rating criteria 'Rating of Bank Legacy Hybrids and Sub-Debt'.

## Company Profile

IL&FS is one of the leading companies operating in the infrastructure development space in India. The company has a strong investor profile with Life Insurance Corporation of India and ORIX Corporation, Japan together holding a 49% stake. The company restructured its business in FY08 and converted itself into a holding company after demerging its loan against shares and advisory business to its subsidiary I-Fin. The company received its CIC licence in September 2012.

I-Fin's ratings (including the above) are as follows:

- Long-Term Issuer Rating: 'IND AAA'/Stable
- Short-Term Issuer Rating: 'IND A1+'
- INR20bn (increased from INR17bn) long-term debt: 'IND AAA'/Stable
- INR9bn lower Tier 2 subordinated debt: 'IND AAA'/Stable
- INR7bn short-term debt: 'IND A1+'

IL&FS' ratings (including the above) are as follows:

- Long-Term Issuer Rating: 'IND AAA'/Stable
- Short-Term Issuer Rating: 'IND A1+'
- INR62.25bn (increased from INR52.25bn) long-term debt: 'IND AAA'/Stable
- INR1bn lower Tier 2 subordinated debt: 'IND AAA'/Stable
- INR12.25bn (increased from INR7.25bn) short-term debt: 'IND A1+'

## APPLICABLE CRITERIA

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### Financial Institutions Rating Criteria

### Non-Bank Finance Companies Criteria

### Rating FI Subsidiaries and Holding Companies

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