

Edelweiss Financial Services Ltd

January 05, 2021

Ratings

Instruments	Amount (Rs. crore)	Ratings ¹	Rating Action
Non-Convertible debenture	200 (Rs. Two hundred crore only)	CARE A+; Stable (Single A Plus; Outlook: Stable)	Assigned

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating based on the consolidated financials of Edelweiss Financial Services Ltd (EFSL) continues to take into account the stress on the wholesale loan book, particularly the real estate exposures and the subsequent deterioration in asset quality of the group as on March 31, 2020 compared to previous year. The Group has sold substantial portion of wholesale loan assets to Asset Reconstruction Companies (ARC) and Alternative Investment Funds (AIF) including Edelweiss Asset Reconstruction Company (at arm's length basis) during FY20. In spite of sell down, the participation in the form of security receipts continues to reflect its exposure to the wholesale loan assets till resolution.

The group has shown ability to sell down the wholesale loan assets over the years, with further sell down of wholesale assets during FY21 to reduce the overall wholesale credit exposure.

On account of the above, the group made higher provisions on the credit book which has heavily impacted the profitability with the group booking loss of Rs. 2,045 crore in FY20 on consolidated basis (post minority interest) as compared to profit after tax (post minority interest) of Rs. 995 crore in FY19. The group has conservatively made provisions higher than the expected credit loss estimated as per study undertaken by an international consulting firm for its wholesale loan book, and it continues to make further provisions during FY21.

The rating takes into account the diversified business profile of Edelweiss group with experienced management team. CARE further factors in the adequate capitalization and the group's ability to raise capital as witnessed during the last few quarters with investment from Caisse de dépôt et placement du Québec (CDPQ), KORA Management and Sanaka Growth SPV I Ltd (part of Sanaka Capital) aggregating to Rs.1334 crore in the form of compulsorily convertible debenture and compulsorily convertible preference shares. Recently, the group has announced an agreement with PAGAC Ecstasy Pte. Ltd. for stake sale of 51% in the wealth management arm of the group at a post-money valuation of Rs.4,400 crore. The said transaction is expected to be closed in the next ~6 months. Further, the group is in talks with marquee investors for stake sale in the asset management arm and is also looking for a strategic partner for its General Insurance business. The group's ability to raise capital during the current environment will further bolster capital base of the group.

The ratings are, however, constrained on account of weak operating performance of the credit book with continuing but reduced exposure to the wholesale book. It continues to take into account the client concentration and credit risk in its wholesale credit book and the risk associated with distressed assets. The concentration in the wholesale book is evident though slightly reduced as the top 50 exposures form 111% of the tangible net worth (excluding minority interest) as on March 31, 2020 as compared to 137% as on March 31, 2019. The client concentration has improved since the last year, however, remains high. Further, the slowdown in the real estate sector owing to the current economic environment might continue to put some pressure on the assets that are still under moratorium which may ultimately have near to medium term impact on the asset quality. However, as stated above the group strives to reduce the wholesale loan book with shifting of the book into a fund-based model.

The rating also factors in some improvement in resource mobilization in the NBFC sector post May 2020. CARE takes note of approx. Rs.12,343 crore of resource mobilisation by EFSL and its subsidiaries during FY20 (including roll over of working capital demand loan) which included retail/private/market linked NCD, bank loans and short-term money market as compared to Rs.15,050 crore in FY19, though at a relatively increased cost of borrowings due to increased risk perception of the lenders towards entities operating in NBFC/HFC segment. Also, the yields in the secondary market continue to remain relatively higher than the retail NCDs. During Q1FY21, the group mobilized resources to the tune of Rs.4,091 crore through the TLTRO route, commercial paper and term loans and has further raised Rs.1,757 crore during July 2020 and August 2020.

The liquidity of the group is adequate. According to the COVID relief package announced by RBI, the company has provided moratorium to the customers with ~25% of the retail customers under moratorium as on August 31, 2020 and ~50% of the wholesale customers under moratorium. The collection efficiency of the group stood at ~50% during Q1FY21 in the retail segment. As a part of the same scheme, the group was eligible for applying for moratorium on its bank loans and thus, three entities of the group viz. ECL Finance Ltd, Edelweiss Retail Finance Ltd and Edelweiss Housing Finance Ltd have been granted moratorium of Rs.795 crore from 5 lenders for the months of June 2020, July 2020 and August 2020. The company has raised resources through the TLTRO route and regular borrowings as stated above.

¹ Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications

The ability of the company in maintaining adequate liquidity, continuous resource mobilization, improvement in the asset quality with further sell down in the wholesale loan book, improvement in the profitability levels amongst the current economic environment would remain key rating monitorable.

Rating Sensitivities

Negative Fact or - Factors that could lead to negative rating action/downgrade

- Increase in the gearing levels [Debt (excluding CBLO)/ Tangible Net worth (excluding minority interest)] above 7x on a consolidated basis.
- Further deterioration in asset quality on consolidated basis.
- Lower than expected scale down of the wholesale loan portfolio
- Depletion in the liquidity buffer maintained by the Group

Positive Factors- Factors that could lead to positive rating action/upgrade

- Improvement in the consolidated profitability parameters on a sustained basis
- Increase in the mobilization of resources on a steady basis at improved rates
- Increase in the granularity of the overall credit book with decline in the wholesale book along with maintaining of asset quality and profitability

Detailed description of the key rating drivers

Key Rating Strengths

Diversified business profile of the group

EFSL is a diversified financial services company with presence in various business segments related to credit in retail credit including mortgage finance (housing loans, loans against property) and SME credit, corporate credit and distressed assets credit including asset reconstruction. Its Advisory businesses include wealth management, asset management, and capital market businesses which include equity broking (both institutional and retail) and investment banking. Its insurance business includes both life and general insurance businesses. The share of the group's total interest income accounted for 57% of the total income in FY20 on consolidated basis. (FY19: 60%). The share of broking and fee based income has remained at 22% of total income in FY20 same as FY19. The share of the insurance premium increased marginally from 7% of total income in FY19 to 11% of total income in FY20.

Established institutional equity broking business and good retail distribution network

EFSL on group basis has established institutional equity business comprising institutional equity sales and research. It provides services to a large and diversified base of Foreign Institutional Investors (FIIs) and domestic institutional investors. Its clients include large pension funds, long only funds, Exchange Traded Funds (ETFs) and hedge funds. It is one of the largest domestic institutional broking houses in India with around 700 foreign and domestic institutional investors. The institutional equity business is supported by a strong equity sales team and relevant and timely research. EFSL manages an AUM of Rs. 2,07,700 crore of customer assets as on March 31, 2020 which comprises of Assets under advice (Wealth Management), Distressed Credit (ARC Assets) and Funds under Management (Asset Management) .

Experienced management team

EFSL has a strong management team with a rich experience in the financial sector. The senior management team of Edelweiss has been quite stable over the last few years and most of the senior management has been with Edelweiss for a long period.

Adequate capitalization levels

On a consolidated basis, the tangible net worth (including minority interest, CDPQ, Kora and Sanaka investment) stood at Rs. 7257 crore as on March 31, 2020 compared to Rs. 7822 crore as on March 31, 2019. The group maintained the Capital Adequacy levels (as per company) at 21% as on March 31, 2020. (18.1% as on March 31, 2019). In March 2019, the company has signed an agreement with CDPQ (Canadian Pension Fund) for investment in the NBFC arm ECL Finance Limited of ~Rs. 1800 crore in a span of 2 years. Out of the said investment, Rs. 1040 crore was received in May 2019 in the form of compulsorily convertible debenture. During FY20, the company announced capital infusion plans in the advisory arm of the group i.e. EGIA to the tune of Rs. 883 crore from two foreign investor viz. Kora Management Limited and Sanaka Capital. Out of the said investment, Rs. 177 crore was received in November 2019 from KORA Management and the company received Rs. 117 crore from Sanaka Capital during Q3FY20 in the form of compulsorily convertible preference shares.

The group's debt levels have decreased from Rs.46,148 crore as on March 31, 2019 to Rs.35,553 (excluding the CCPS) crore as on March 31, 2020. Consequently, gearing levels (including minority interest) decreased from 5.9x as on March 31, 2019 to 4.8x (including the CCPS/CCD) as on March 31, 2020. The group's gearing excluding the liquid treasury assets maintained for liquidity management as on March 31, 2020 stood at 3.2x (based on reported net worth of the group). As on September 30,

2020, the gearing (including minority interest and CCPS/CCD) stood at 4.7x and the gearing excluding the liquid treasury assets stood at 3.1x.

The Group has demonstrated a track record of raising funds at regular intervals to take care of the leverage at the group level. However, the gearing levels are high as compared to larger wholesale NBFC's. Further, the Group has a strong track record of raising and deploying managed funds, which supports its overall business capabilities. The current trend of improvement in gearing level along with the planned equity infusions is expected to maintain gearing at adequate level. However, CARE will monitor on a continuous basis any potential stress that could lead to increase in the gearing levels which will remain as key rating sensitivity.

Adequate liquidity profile and diversified resource profile

At the group level, the company maintained liquidity to the tune of Rs.4650 crore as on March 31, 2020 which comprised of Rs. 3700 crore of cash/bank balance & fixed deposit, Rs.400 crore of investment in government securities and bonds, Rs off balance sheet liquidity in the form of undrawn bank lines amounted to Rs.550 crore. As per management, the liquidity stood at Rs. 8100 crore (including short term loan book in the form of Loan against securities and other short term loans) as on March 31, 2020. The liquidity (excluding short term loan book considered) is sufficient for ~ 6 months debt repayment without any inflow from advances and no fresh borrowings.

As on March 31, 2020, resource profile (excluding CBLO) is well diversified with NCDs / Sub debt / MLD - 62% (FY19: 53%), Bank borrowings- 37% (FY19: 34%), Commercial Paper- 1% (FY19: 2%) of total borrowings respectively. EFSL has reduced its dependence on the commercial paper in FY19 and continued to maintain the commercial paper dependence at negligible in FY20 as well. The group has reduced the dependence on commercial paper from 18% as on March 31, 2018 to 1% as on March 31, 2020.

Key Rating Weakness

Substantial proportion of revenue from the capital markets related activities

A significant proportion of EFSL's revenue is related to the capital markets led activities, which include equity broking, investment banking, capital market related loan portfolio, asset management. However with increase in size of the credit business, dependency on capital markets has been declining over past few years.

Moderation in asset quality

Overall asset quality of the group deteriorated as Gross Non-performing assets (GNPA) stood at 5.32% of total loan book as on March 31, 2020 as compared to 1.87% of GNPA as on March 31, 2019. The Gross NPA % of the wholesale book stood at 9.7% as on March 31, 2020 as compared to 2.74% as on March 31, 2019. Including the security receipts held in the credit book amounting to Rs. 4835 crore as on March 31, 2020 (three NBFC and one HFC in the group) and the write off done during FY20, the stressed assets on balance sheet is higher. The group has faced asset quality issues during the year in the wholesale book, however the company has been striving to reduce the wholesale exposure of the group and has been instrumental in reducing the wholesale book from Rs. 18055 crore as on March 31, 2019 to Rs. 10100 crore as on March 31, 2020. These has been through Sale of Assets to AIFs and to ARCs. Through the AIF route, the company has arranged for last mile funding required to complete the projects and has done 2 such transactions in the past 9 months amounting to Rs. 2500 crore of assets. The other assets are sold to ARCs on account of their capability to resolve such stressed assets. The GNPA stood at 5.46% and NNPA 3.87% stood at as on September 30, 2020. The management expects recovery in SR to begin from Q4 FY21 and also expects some reversal of mark downs once the recovery starts to pick up. The company's ability to further reduce the wholesale book with transfer of the risks and rewards will be a key rating monitorable.

Edelweiss group has outstanding exposure to real estate with financing to developers accounting for 30% of the total credit book as on September 30, 2020 as compared to 35% of the total credit book as on September 30, 2019. The current environment prevailing in the real estate sector owing to the pandemic coupled with higher inventory is expected to put pressure on the asset quality of the NBFCs including Edelweiss which has relatively higher exposure to real estate developers in the NBFC segment.

Thus, the ability of the group in maintaining the asset quality across the business cycles is a key rating sensitivity.

Client concentration and credit risk in its wholesale credit book

As on March 31, 2020, the total loan portfolio comprised of retail book of 52% (March 2018: 50%), wholesale book of 48% (March 2018: 50%). Wholesale credit book of EFSL comprises of the real estate financing and the structured collateralised credit book. The real estate financing accounted for 30% of the total credit book as on March 31, 2020 as compared to 32% of the total credit book as on March 31, 2018. Even though the company has demonstrated a reduction on the concentration in the wholesale book as compared to the last year, but the reduction in the Retail Credit book has also been steeper therefore the real estate segment continues to dominate the credit book. As on March 31, 2020, the top 50 exposures shared by the company accounted for 1.11 times of Tangible Net-worth (excl. MI) (March 2019: 1.37 times). The top 10 accounts accounted

for 44% of the tangible net-worth as on March 31, 2020. (March 2019: 45% of tangible net worth). As on June 30, 2020, the retail and wholesale proportion of the total loan portfolio stood at 55:45.

As on March 31, 2020, the real estate book which has high ticket concentration and higher proportion of the book (based on analysis of information provided for 14 top exposures in RE book) under principal moratorium is expected to impact the liquidity in the short to medium term given the prolonged slowdown in the real estate sector. However, the company tries to mitigate the risk associated with the real estate exposures by the adequate collateral cover of 2-3x maintained on each exposure and control over the cash flows of the projects through Escrow mechanism. The company undertakes regular monitoring of each projects by an in-house team which is engaged in fortnightly physical verification of the projects, marketing and controlling the construction if required. The group has also undertaken sell down through the AIF and ARC route during Q1FY21 and Q2FY21 also to reduce the exposure on the wholesale book.

Risk associated with distressed assets

As on March 31, 2020, asset under management of the Edelweiss Asset Reconstruction stood at Rs. 43012 crore as on March 31, 2020 as compared to Rs. 46423 crore as on March 31, 2019. Till date the ARC has redeemed Rs. 8330 crore of security receipts which account of approximately 19.04% of the issued security receipts. The ARC has made recoveries of Rs. 11257 crore during FY20 (FY19: Rs. 7019 crore) and Rs 1400 crore during H1 FY21 Edelweiss ARC reported a Profit after tax (PAT) of Rs.306 crore in FY20 (Rs.435.02 crore in FY19).

Even though the ARC business has demonstrated growth in the past year with steady recoveries and growth in profitability, the inherent high riskiness of business leads to uncertainty and credit risk. Furthermore, the group has acquired a large portfolio of distressed assets in the past few years and the resolution in such cases needs to be seen. At the same time, the implementation of IBC has improved the pace of resolution. The company's ability to demonstrate adequate and timely resolution performance is a key rating sensitivity.

Moderation in profitability growth

The group has reported loss during FY20 of Rs. 2045 crore as compared to profit after tax of Rs. 995 crore on account decline in the interest income due to de-growth in the loan portfolio, marginal decline in the advisory, increase in the loss in life insurance business coupled with the rise in the cost of borrowings of the group post H2FY19 on account of liquidity crunch in the market and also the lower dependence on the commercial paper borrowings. The Net interest margin stood at 1.96% of total assets in FY20 as compared to 3.31% of total assets in FY19. Credit cost stood at 6.13% of total assets in FY20 as compared to 1.12% of total assets in FY19. The major reasons for the rise in credit cost is mainly due to revision in the Expected credit loss model, COVID related provisions taken upfront in Q4FY20, marked down on the investment book and marked down on account of sell down of wholesale assets. The group has taken conservative approach in providing additional provisions over and above the ECL provisions thus impacting the profitability for strengthening the balance sheet. The operating expense stood at 6.38% of total assets in FY20 as compared to 6.25% of total assets in FY19. As a result of the above, the Return on total assets deteriorated from 1.66% in FY19 to -3.52% in FY20. Though the group has taken steps to lower down the cost and improve the profitability, which would be visible in the coming quarters.

During H1FY21, the group reported loss post minority interest of Rs.293.58 crore as compared to profit after tax post minority interest of Rs.183.19 crore in H1FY20 on account of 16% reduction in the total income as compared to that during the same

Liquidity: Adequate

The liquidity of the group stands adequate. As on November 30, 2020, the liquidity stood at Rs. 6450 crore which comprised of overnight liquidable assets of Rs. 2950 crore, treasury assets of Rs. 1950 crore, Rs. 250 crore of undrawn bank lines and short term loan book of Rs. 1300 crore.

As on September 30, 2020, the overnight liquidity, treasury assets and undrawn bank lines aggregating to Rs. 5250 crore covers principal debt repayments of ~10 months. As a policy, the group maintains 15-20% of the borrowings as liquidity at all times.

Analytical approach:

EFSL (rated 'CARE A1+; CARE A+; Stable), the flagship company of the Edelweiss group, owns 100% in most of its subsidiaries and the management/line functions for these businesses is common with significant operational and financial integration among them. Accordingly, CARE has considered a consolidated view of EFSL for arriving at the rating. The list of the subsidiaries considered for consolidation is as per Annexure 4.

Applicable Criteria

[CARE's Criteria on assigning Outlook and Credit Watch to Credit Ratings](#)

[Policy of Default Recognition](#)

[Financial ratios – Financial Sector](#)

[Rating Methodology- Non Banking Finance Companies](#)

[Consolidation and Factor Linkages in Ratings](#)

About the Company

Previously known as Edelweiss Capital Limited, Edelweiss Financial Services Limited (EFSL) was incorporated in 1995 by Mr. Rashesh Shah and Mr. Venkat Ramaswamy. EFSL is registered as a Category I Merchant Banker with SEBI and is the parent company of the Edelweiss Group. The company on a standalone basis is primarily engaged in investment banking services and provides development, managerial and financial support to the businesses of the Edelweiss group entities. The Edelweiss Group offers a range of products and services, spanning varied asset classes and diversified consumer segments. The businesses of Edelweiss are organized around three broad lines – credit including housing finance, SME loans, Loans against Property, Loans against Securities, Rural finance, Agri credit, Structured collateralised credit to corporates and real estate developer finance, Advisory businesses (EGIA) including wealth management, asset management and capital markets and insurance including life and general insurance. In addition, the Balance-sheet Management Unit (BMU) attends to the balance sheet and liquidity management.

Brief Financials (Rs. crore) (IND AS)	FY19 (A)	FY20 (A)
Total income	11,161	9,603
PAT (after share of profit and minority interest)	995	(2,045)
Overall Gearing (excluding minority interest) (times)	6.53	6.09
Total Assets	63,630	54,280
Gross NPA (%)	1.87	5.32
ROTA (%)	1.65	(3.47)

A: Audited

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Not Applicable

Complexity level of various instruments rated for this company: Annexure 3

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Non-convertible debenture (proposed)	-	-	-	-	200.00	CARE A+;Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (12-Sep-17)
2.	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1) Withdrawn (12-Sep-17)
3.	Debentures-Non Convertible Debentures	LT	-	-	1)Withdrawn (18-Jun-20) 2) CARE AA-; Negative (02-Jun-20) 3)CARE AA-; Negative (30-Apr-20) 3)CARE AA-; Stable (25-Mar-20)	1)CARE AA-; Stable (05-Jul-19)	1)CARE AA; Positive (06-Jul-18)	1) CARE AA; Stable (12-Sep-17)
4.	Commercial Paper	ST	1575.0	CARE A1+	1) CARE A1+ (05-Nov-20) 2) CARE A1+ (08-Oct-20) 3)CARE A1+ (02-Jun-20) 4)CARE A1+ (30-Apr-20) 5)CARE A1+ (25-Mar-20)	1)CARE A1+ (05-Jul-19)	1)CARE A1+; (06-Jul-18)	1)CARE A1+ (12-Sep-17)
5	Debentures-Non Convertible Debentures	LT	200.00	CARE A+; Stable	1)CARE A+; Stable (05-Nov-20)			
6	Debentures-Non Convertible Debentures	LT	200.00	CARE A+; Stable	-	-	-	-

Annexure 3: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Commercial Paper	Simple
2	Non-convertible debenture (Public Issue)	Complex
3	Non-convertible debenture	Complex

Annexure 4: List of subsidiaries taken for consolidation as on March 31, 2020

	Subsidiaries of Edelweiss Financial Services Limited	Shareholding by EFSL (directly/indirectly)
1	Edelweiss Securities Limited (ESL)	100%
2	Edelweiss Comtrade Ltd.	100%
3	Edelweiss Securities (Hong Kong) Private Limited	100%
4	Edelweiss Financial Services Inc., USA	100%
5	Edelweiss Custodial Services Limited	100%
6	Edelweiss Asset Reconstruction Company Limited	74.80%
7	Edelweiss Financial Services (UK) Limited	100%
8	Edelweiss Finance & Investments Limited	100%
9	EC Global Limited, Mauritius	100%
10	Edelweiss Rural & Corporate Services Limited (ERCSL) (Formerly Edelweiss Commodities Services Ltd. (ECSL))	100%
11	Edelweiss Housing Finance Limited (EHFL)	100%
12	Edelweiss Broking Limited (EBL)	100%
13	Edel Finance Company Ltd.	100%
14	Edelweiss Capital (Singapore) Pte. Limited (ECSPL)	100%
15	Edelweiss Alternative Asset Advisors Pte. Limited	100%
16	Edelweiss International (Singapore) Pte. Limited	100%
17	Edelweiss Investment Advisors Private Limited, Singapore	100%
18	EC International Limited, Mauritius (ECIL)	100%
19	Aster Commodities DMCC, Dubai	100%
20	EAAA LLC, Mauritius	100%
21	EW Special Opportunities Advisors LLC, Mauritius	67%
22	ECap Equities Limited	100%
23	Edelcap Securities Limited	100%
24	Edelweiss Finvest Private Limited (formerly Arum Investments Private Limited)	100%
25	Edelweiss Retail Finance Limited	100%
26	ECL Finance Limited	100%
27	Edelweiss Alternative Asset Advisors Limited	95%
28	Edelweiss Global Wealth Management Limited	100%
29	Edelweiss Gallagher Insurance Brokers Limited (Formerly known as Edelweiss Insurance Brokers Limited)	74%
30	EC Commodity Limited	100%
31	Edelweiss Investment Adviser Limited	100%
32	Edelweiss Tokio Life Insurance Company Limited	51%
33	Edel Investments Limited	100%
34	Edel Land Limited	100%
35	Edelweiss Trusteeship Company Limited	100%
36	Edelgive Foundation	100%
37	Edelweiss Asset Management Limited	100%
38	Edelweiss General Insurance Company Limited	100%
39	Edelweiss Securities (IFSC) Limited	100%
40	Allium Finance Private Limited	70%
41	Lichen Metals Private Limited	100%
42	Edelweiss Multi Strategy Fund Advisors LLP	100%
43	Edelweiss Resolution Advisors LLP	100%
44	Edelweiss Securities and Investments Pvt Ltd	100%
45	Edelweiss Private Equity Tech Fund	89%
46	Edelweiss Value and Growth Fund	89%
47	ESL Securities Ltd	100%

Note on complexity levels of the rated instrument: CARE has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.

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