IndoStar Capital Finance Limited (Revised)
May 16,2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term Instruments	9,700.00	CARE AA- (CWD) (Double A Minus) (Under Credit watch with Developing Implications)	Placed on Credit watch with Developing Implications
Market Linked Debentures	100.00	CARE PP-MLD AA- (CWD) (Principal Protected-Market Linked Debentures Double A Minus) (Under Credit watch with Developing Implications)	Placed on Credit watch with Developing Implications
Market Linked Debentures	200.00	CARE PP-MLD AA- (CWD) (Principal Protected-Market Linked Debentures Double A Minus) (Under Credit watch with Developing Implications)	Placed on Credit watch with Developing Implications
Total Long-term Instruments	**10,000.00 (₹ Ten thousand crore only)**		
Commercial Paper	1,000.00	CARE A1+ (CWD) (A One Plus) (Under Credit watch with Developing Implications)	Placed on Credit watch with Developing Implications
Commercial Paper	1,000.00	CARE A1+ (CWD) (A One Plus) (Under Credit watch with Developing Implications)	Placed on Credit watch with Developing Implications
Total Short-term Instruments	**2,000.00 (₹ Two thousand crore only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE Ratings Limited (CARE Ratings) has placed the ratings assigned to the various debt instruments of IndoStar Capital Finance Limited (ICFL) on 'Rating Watch with Developing Implications'. The rating action follows the company's disclosure in its exchange filings that certain control deficiencies with respect to sanctioning of loans to existing customers, loan documentation and policy implementation gaps were primarily observed in a part of the commercial vehicle (CV) loan portfolio.

Based on the preliminary findings, E&Y; the independent consultant appointed by the Audit Committee of ICFL) has estimated an additional estimated credit loss (ECL) provisioning between ₹557 crore and ₹677 crore. The loan portfolio review is ongoing and the assessment of the potential additional provisioning and relevant issues may undergo changes. The exercise is expected to be completed by the time of finalisation of the audited financial statements of the company for the year ended March 31, 2022.

The ratings factor ICFL's strong capitalisation levels, healthy net-worth base and comfortable gearing levels. The ratings also factor the company's strong institutional sponsor(s), experienced management and increasing proportion of retail advances bringing granularity to the book.

While the concentration risk is in the wholesale book has been declining, the ratings remain constrained by deterioration in the asset quality, weak financial performance in the retail segments.

Rating Sensitivities

Positive Factors – Factors that could lead to positive rating action/upgrade:

- Growth in the scale of business operations with sustained improvement in profitability (return on total assets [ROTA] above 3%).
- Improvement in the asset quality on a sustainable basis with growth in the market size.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Negative Factors – Factors that could lead to negative rating action/downgrade:

- Sustained deterioration in asset quality metrics impacting profitability.
- Significant deterioration in gearing levels above 5x.
- Material weakening of liquidity parameters.

Detailed description of the key rating drivers

Key Rating Strengths

Strong institutional support with experienced management team: Brookfield is the largest shareholder of the company, with around 57% shareholding as on March 31, 2022. Listed on the New York Stock Exchange (NYSE: BAM) and the Toronto Stock Exchange (TSX: BAM.A), Brookfield is a global alternative asset manager offering investment strategies in property, infrastructure, renewable energy, private equity and public securities to institutional investors. Brookfield is one of the largest global managers of real estate assets and has significant funding capacity, with approximately US$725 billion in assets under management (AUM). There have been series of changes in the top management team recently. Mr Deep Jaggi, who had joined ICFL in October 2020 as the Chief Business Officer, was appointed as the CEO in January 2022, after the Vice Chairman, Mr R. Sridhar, decided to step down on completion of his five-year tenure. Prior to joining ICFL, Mr Jaggi was the head of asset finance in HDB Financial Services. Recently, Mr Kapish Jain has joined in the role of CFOSeveral new appointments have being made in the areas of Risk and Operations. Over the past few years, the management has been transitioning from a corporate lending business to a granular retail business. As on December 31, 2021, the retail book stood at about 82% of the overall AUM. The company, under the leadership of the new team, intends to become a 100% retail finance company.

Strong capitalisation with healthy net worth base and low overall gearing: The tangible net worth of ICFL improved from ₹3,251 crore as on March 31, 2021 to ₹3,678 crore, primarily owing to conversion of optionally convertible loans to equity. As a result, gearing improved from 1.85x as on March 31, 2021 to 1.78x as on December 31, 2021, although it is expected to rise to around 2x after factoring the impact of the estimated additional provisioning. The capital adequacy ratio (CAR) remained relatively stable at 35.1%. As stated by the management, assuming the higher end of the range of potential additional provisioning owing to the recently uncovered control deficiencies, the revised CAR as on December 31, 2021, would be approximately above 25%, which still presents cushion over the regulatory requirement. However, the same is subject to finalisation of the audited financial statements of the company for the year ended March 31, 2022.

Increased granularity of loan book owing to retail focus, albeit low seasoning: The overall portfolio of ICFL is divided into retail advances (which includes CV segment, small and medium enterprises [SME] segment and housing segment) and wholesale advances (which consists of corporate loans). The corporate lending book, which formed 73% as on March 31, 2018, has been consciously run down in a span of three years, to 18% of AUM as on December 31, 2021, as part of the long-term retailisation strategy for the group. As on December 31, 2021, out of the total AUM of ₹9,215 crore, loans in CV segment stood at 49%, followed by 20% in SME segment and 13% in affordable housing finance. The proportion of CV financing substantially increased on account of acquisition of the CV portfolio from IIFL in FY20 (refers to the period April 1 to March 31). The overall retail disbursements have been on the rise increasing to ₹1,456.3 crore in Q3FY22 in comparison to ₹476.9 crore in Q3FY21 and ₹1,107.5 crore in Q2FY22 with maximum share being in the CV financing space. Going ahead, ICFL intends to focus on growing its book in the used CV and affordable housing finance segment. On the SME portfolio, focus would be more on the high-yield loan against property (LAP) segment. While granularity of the book has increased given the retail focus, portfolio seasoning would remain low on the newly originated book. Moreover, asset quality would remain the key monitorable especially in the CV segment considering the current developments.

Key Rating Weaknesses

Moderation in asset quality metrics due to weakening economic environment: In FY21, the pandemic-induced disruptions led to significant uptick in ICFL's Gross Stage-2 (GS2) assets, while Gross Stage-3 (GS3) improved from 4.8% as on March 31, 2020 to 4.4% as on March 31, 2021. GS3 assets increased to 4.3% as on December 31, 2021, owing to the second wave of Covid disruptions due to the lockdown. The CV portfolio continues to remain the major contributor to GS3 assets with GS3 at 6%. As indicated by the management, the stage-wise bucketing for the part of the CV portfolio where control deficiencies were uncovered is yet to be finalised by the statutory auditors and will be a key rating monitorable. We also understand that the management has instituted an action plan, which includes revamping and strengthening of the underwriting criteria for existing customers, stepping up of collection efforts, undertaking no new restructuring of loans, among others, to guard against any asset quality issues in the future.

Low profitability levels: The company had returned to profitability in 9MFY22 with PAT of ₹17 crore after two consecutive years of losses. In FY20, ICFL undertook some accelerated provisioning and aggressive write-offs in its legacy corporate book and in its acquired CV book. In FY21, the earnings were impacted due to lower interest income from reduction in wholesale loans and lower disbursement in the retail segment. With the recent announcement of additional estimated provisioning, the company is expected to post a loss in FY22, the quantum of which is yet to be established. Furthermore, clarity is also expected on whether the additional provisioning estimated to be undertaken by the company would eventually result in actual losses.

Concentration in the wholesale book; albeit declining The corporate lending book stood at ₹1,622 crore as on December 31, 2021, and constitutes 18% of the overall AUM. The asset quality for this segment remains vulnerable to current challenging economic scenario and concentration risks of chunkier real estate loans, which continues to remain a key monitorable. During 9MFY22, there was a slippage of ₹19 crore in the corporate loan book. Out of the outstanding corporate portfolio, real estate portfolio constitutes 88% as on March 31, 2022. Top five exposures account for 57% of the Corporate Loan book. The management does not expect any additional losses in the corporate loan segment.

Liquidity: Adequate
Generally, the company's strategy is to keep around two to three months of liquidity in liquid cash and mutual funds. As on April 30, 2022. At standalone level, ICFL had liquidity to the tune of ₹1,123 crore, which comprises cash and liquid investments of ₹559 crore and undrawn committed lines of ₹564 crore.

Analytical approach: CARE Ratings has taken a consolidated view of ICFL and its subsidiary, IndoStar Home Finance Pvt Ltd (IHFPL), together referred to as the IndoStar Group. This is because of 100% ownership, shared brand name, strong operational, management and financial linkages and growing size and strategic importance of IHFPL to the group.

Applicable criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Financial ratios – Financial sector
Rating Methodology: Consolidation
CARE's Criteria for Market Linked Notes/Debentures
Criteria for Short Term Instruments
Rating Methodology – Non-Banking Finance Companies

About the company
IndoStar Capital Finance Ltd. (ICFL) is registered with the Reserve Bank of India (RBI) as a systemically important non-deposit-taking non-banking financial company (NBFC). The company started off with corporate lending in 2011, ventured into SME financing from 2015 and CV financing from May 2017, to have a diversified and a granular portfolio. ICFL also diversified into retail home financing from FY18 through its subsidiary, IndoStar Home Finance Private Limited (IHFPL). ICFL co-lends for CV financing (new vehicles) with ICICI Bank. In this, the origination is done by ICFL, and the entire disbursement is then carried out by ICICI Bank. ICFL also plans to tie up with smaller NBFCs, which have a reach in Tier-III and Tier-IV cities to further its penetration and presence in the used vehicle business. ICFL operates through 343 branches across 19 states as on December 31, 2021.

Brief Financials (Rs. crore)	31-03-2020 (A)	31-03-2021 (A)	9MFY22 (UA)
Total income	1,599	1,287	842
PAT	-325	-214	17
Interest coverage (times)	0.49	0.69	1.06
Total assets	10,129	10,082	9,712
Net NPA (%)	3.8	2.1	2.3
ROTA (%)	-3.00	-2.22	0.24

A: Audited; UA: Unaudited

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: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure-4

Annexure-1: Details of Instruments / Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating assigned along with Rating Outlook
Non-Convertible Debentures (NCD)	INE896L07702	25-Nov-19	-	25-Oct-24	25.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L07769	29-Dec-20	-	29-Jun-22	25.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L08031	04-Jun-21	-	04-Jul-22	75.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L07793	03-Jan-22	-	03-Jan-24	50.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L07074	06-Jun-13	-	06-Jun-23	15.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L07561	02-May-18	-	02-May-23	500.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L08023	14-May-21	-	14-Jun-22	350.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L07710	21-May-20	-	21-Feb-23	100.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L08049	30-Jul-21	-	30-Aug-22	150.00	CARE AA- (CWD)
Non-Convertible Debentures (NCD)	INE896L07728	26-Jun-20	-	26-Jun-23	50.00	CARE AA- (CWD)
Debentures-Market Linked Debentures	INE896L07785	25-Aug-21	-	23-Feb-24	75.00	CARE PP-MLD AA- (CWD)
Debentures-Market Linked Debentures	INE896L07777	18-May-21	-	18-May-23	45.90	CARE PP-MLD AA- (CWD)
Debentures-Market Linked Debentures (Proposed)	-	-	-	-	179.10	CARE PP-MLD AA- (CWD)
Fund Based -LT -Term loan	-	-	-	31-Mar-26	3,117.00	CARE AA- (CWD)
Proposed facilities -LT	-	-	-	-	5,243.00	CARE AA- (CWD)
Commercial Paper-Commercial Paper (Standalone)	-	-	-	-	2,000.00	CARE A1+ (CWD)

Annexure-2: Rating history of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) & Rating(s) assigned in 2022-2023	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020
1	Commercial Paper-Commercial Paper (Standalone)	ST	1000.00	CARE A1+ (CWD)	-	1)CARE A1+ (20-Aug-21)	1)CARE A1+ (08-Oct-20) 2)CARE A1+ (17-Aug-20) 3)CARE A1+ (CWD) (17-Apr-20)	1)CARE A1+ (09-Oct-19)
2	Debt	LT	9700.00	CARE AA- (CWD)	-	1)CARE AA-; Stable (20-Aug-21)	1)CARE AA-; Stable (08-Oct-20)	1)CARE AA-; Stable (09-Oct-19)

							2)CARE AA-; Stable (17-Aug-20) 3)CARE AA- (CWD) (17-Apr-20)	2)CARE AA-; Positive (02-Apr-19)
3	Debentures-Market Linked Debentures	LT	100.00	CARE PP-MLD AA- (CWD)	-	1)CARE PP-MLD AA-; Stable (20-Aug-21)	1)CARE MLD AA-; Stable (08-Oct-20) 2)CARE MLD AA-; Stable (17-Aug-20) 3)CARE MLD AA- (CW) (17-Apr-20)	1)CARE PP-MLD AA-; Stable (09-Oct-19)
4	Commercial Paper-Commercial Paper (Standalone)	ST	1000.00	CARE A1+ (CWD)	-	1)CARE A1+ (20-Aug-21)	1)CARE A1+ (08-Oct-20) 2)CARE A1+ (17-Aug-20) 3)CARE A1+ (CWD) (17-Apr-20)	-
5	Debentures-Market Linked Debentures	LT	200.00	CARE PP-MLD AA- (CWD)	-	1)CARE PP-MLD AA-; Stable (20-Aug-21)	-	-

* Long term / Short term

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not Applicable

Annexure-4: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1	Commercial Paper	Simple
2	Debentures-Market Linked Debentures	Highly Complex
3	Debt	Simple

Annexure 5: Bank lender details for this company
To view the lender-wise details of bank facilities please [click here]

Annexure 6: List of entities considered for consolidation

Name of the companies/ Entities	% of holding
IndoStar Asset Advisory Private Limited	100.00
IndoStar Home Finance Private Limited	100.00

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

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About CARE Ratings Limited:

Established in 1993, CARE Ratings Ltd. is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India (SEBI), it has also been acknowledged as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). With an equitable position in the Indian capital market, CARE Ratings Limited provides a wide array of credit rating services that help corporates to raise capital and enable investors to make informed decisions backed by knowledge and assessment provided by the company.

With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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