L&T Finance Holdings Limited

September 29, 2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Preference Share	2,836.00	CARE AAA; Stable (Triple A; Outlook: Stable)	Reaffirmed
Non-convertible debentures	1,000.00	CARE AAA; Stable (Triple A; Outlook: Stable)	Reaffirmed
Total long-term instruments	**3,836.00 (₹ Three thousand eight hundred thirty-six crore only)**		
Commercial paper	2,500.00	CARE A1+ (A One Plus)	Reaffirmed
Total short-term instruments	**2,500.00 (₹ Two thousand five hundred crore only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

The reaffirmation of the ratings of L&T Finance Holdings Limited (LTFHL) is based on the consolidated business and financial risk profile of LTFHL, the holding company of the group's financial services businesses. The ratings continue to factor in the strong linkages of LTFHL with the ultimate parent, Larsen & Toubro Limited (L&T), strategic importance of financial services business to the group, demonstrated track record of financial support from L&T Group as and when required, shared brand name and managerial support in the form of representation of L&T executives on LTFHL's Board and its presence in some of the key committees.

The ratings further factor in LTFHL's diversified product profile with rising share of granular retail assets, experienced management team, diversified funding profile with strong resources raising ability, comfortable capital structure, and strong liquidity position.

The above strengths are partially offset by moderate asset quality and high credit costs, and the resultant impact on the profitability. However, this credit cost is also including the macro prudential and additional provisions (including OTR provisions) amounting to 1.73% of the standard book as on June 30, 2022, which is expected to provide some cushion to absorb asset side shocks.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade: Not applicable

Negative factors – Factors that could individually or collectively lead to negative rating action/downgrade:

- Weakening of the parent's (L&T Limited) credit profile.
- Material dilution in the shareholding of L&T Ltd. in LTFHL or reduction of strategic importance of LTFHL.
- Material deterioration in asset quality for LTFHL (Consolidated), with Net Stage 3/net worth remaining above 20% on a sustained basis.
- Consolidated gearing rising above 8x on a sustained basis.

Detailed description of the key rating drivers

Key rating strengths

Strong parentage and strategic importance for the parent company/Group: LTFHL is held 66.23% by L&T Limited as on June 30, 2022. The financial services business is strategic and an integral part of the overall L&T Group's business objectives, which is evident through L&T's support on operational, managerial, and financial front to LTFHL. On the capital front, L&T Ltd. has demonstrated capital support to LTFHL at regular intervals in the form of equity infusion. In addition to strong liquidity at the LTFHL (Consolidated) level and credit line from L&T (₹1,800 crore), LTFHL also benefits from financial flexibility due to its association with the L&T Group.

On managerial front, MD & CEO of L&T Ltd is the Chairman and Non-Executive Director of LTFHL. L&T Ltd provides strategic oversight with representations on the Board and crucial committees, such as Risk Management Committee, Audit Committee, Asset Liability Management Committee, etc. Furthermore, L&T Ltd being major technology, engineering, construction and manufacturing conglomerate with global operations and decades of experience, immensely benefits the financial services business especially the infrastructure and real estate underwriting. Thus, LTFHL's ratings derive significant strength from L&T Ltd and any material weakening in L&T's credit profile or dilution of LTFHL's strategic linkages with L&T or material reduction in

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

L&T's support to LTFHL will be considered as a credit negative. For FY22 (refers to the period April 1 to March 31), at a consolidated level, L&T Ltd clocked a revenue of ₹158,788 crore with a profit after tax (PAT) of ₹10,419 crore.

Diversified product profile and revenue streams, with rising share of retail asset classes: LTFHL has three major businesses verticals, i.e., Rural Finance (comprising Farm Equipment Finance, Rural Business Loans & Micro Finance loans), Urban Finance (comprising 2W loans, SME, consumer loans, home loans and loan against property [LAP]) and Wholesale Finance (comprising Real Estate Finance and Infrastructure Project Finance). Rural and Urban Finance collectively known as retail finance comprised 54% share in the total loan book as on June 30, 2022, while wholesale business comprised 45% (Retail: Wholesale share stood at 51:49 as on March 31, 2022). In sync with the company's strategy to move towards retail lending; the share of granular retail assets has been growing. The share of retail loans in the overall disbursements increased to 86% during Q1FY23 from 59% during FY22, which demonstrates the company's focus on its retail strategy.
The company also has investment management services business, which is conducted through L&T Investment Management Limited (LTIML), a wholly owned subsidiary of LTFHL. LTFHL has entered into definitive agreement with HSBC Asset Management (India) Private Limited ('HSBC AMC') on December 23, 2021, to sell 100% equity shares of L&T Investment Management Limited, subject to regulatory approvals**.** As on quarter ended March 31, 2022, AMC had an average asset under management (AUM) of ₹75,592 crore. The transaction is on track and is expected to be completed in near time. The purchase consideration is around USD 425 million (subject to adjustments as set out in the definitive agreement).
With rising share of granular retail assets, CARE Ratings expects credit concentration risks to be mitigated in the medium term.

Adequate capital position with back-up from the parent: The consolidated capital adequacy ratio (CAR) and Tier-I CAR of LTFHL stood at 22.88% and 19.70%, respectively, as on March 31, 2022, compared with 23.80% and 18.79% as on March 31, 2021, respectively. Furthermore, LTFHL benefits from demonstrated capital support from the parent. So far, L&T has infused ₹5,686 crore since inception into LTFHL. In sync with decline in the company's portfolio, gearing levels have been coming down and stood at 4.60x as on March 31, 2022, and is expected to remain at similar levels in the near future.
Considering the management's stated intent to reduce share of wholesale assets, macro prudential and additional provisions (including OTR provisions) of ₹1,450 crore as on June 30, 2022, and expected proceeds from stake sale in LTIML, LTFHL has adequate capital levers in CARE Ratings Limited's opinion for funding retail assets growth in the near to medium term.

Diversified funding avenues with strong resource raising ability: The company has a well-diversified resource profile base which comprises bank loans (43%), NCD- nonretail (42%), retail NCD (3%), commercial papers (8%), ECB (4%) and others (1%) as on June 30, 2022. Being part of the L&T Group provides financial flexibility and enables the company in raising resources at competitive rates of interest. In line with benign interest rate environment, weighted average cost of capital (WAC) (consolidated) for LTFHL reduced from 7.65% during Q4FY21 to 7.34% in Q4FY22 and 7.27% in Q1FY23. The company had also raised low-cost Priority Sector lending loans (PSL) amounting to around ₹1,800 crore in Q4FY22. With its focus on ESG assessment, the company was also able to raise low-cost sustainability linked rupee loans of ₹200 crore in Q4FY22.
The company has historically demonstrated its ability to raise long-term funding from broad-based sources and the same is expected to continue in the long term as well.
Going forward, LTFHL's continued ability to augment the resource profile at cost-effective rates will be key to its profitability. Given the continued focus on augmenting retail loans in general and rural financing in particular, the low cost PSL and sustainability funding will continue to be important funding sources.

Key rating weakness
Moderate asset quality: Gross Stage-3 and Net Stage-3 assets have improved on account of recovery and write-offs in the loan book and sale of assets done through ARC. Gross stage 3 (GS3) and Net Stage 3 (NS3) has improved from 6.67% and 2.26%, respectively as on June 30, 2021, to 4.08% and 1.87%, respectively, as on June 30, 2022. (As on March 31, 2022, GS3 and NS3 stood at 4.08% and 1.98%, respectively). The company also has a conservative provisioning policy for unsecured retail loans based on ECL assumptions and strong in-house collection teams, which also supported improvement in overall asset quality parameters. The provision coverage ratio stood at 53% as on March 31, 2022, compared with 71% as on March 31, 2021.
OTR book of the company has reduced from ₹3,040 crore as on March 31, 2022, to ₹2,019 crore as on June 30, 2022. The reduction in OTR is on account of assets worth ₹548 crore, which has been closed, ₹205 crore, which is written-off and ₹268 crore, which has been rolled over to GS3. LTFH continues to carry macro prudential and additional provisions (including OTR provisions) of ₹1,450 crore (₹1,727 crore as on March 31, 2022), which translates to 1.73% of standard book as on June 30, 2022, which are over and above the ECL on GS3 assets and standard assets provisions, which could be utilised for any future uncertainties.
With respect to some of the legacy stressed exposures in LTFHL's wholesale book, the company is trying to reduce these exposures through various resolution mechanisms. Security receipts at a consolidated level stood at 4,886 crore as on March 31, 2022, which are mainly consisting of wholesale assets.
Thus, considering its majority of its portfolio under unsecured and wholesale portion, asset quality continues to remain anchored on the vulnerability of income profiles of the borrowers in rural segment and resolution of stressed assets in the wholesale book. However, considering the quantum and reliance of digitisation, we expect that the company shall take prudent and proactive decisions on the back of heavy investments in data analytics and its accelerated provisioning policy should cushion the profitability and balance sheet from asset side risks in the near term.

Moderation in profitability: Despite growth in disbursements from ₹28,325 crore for FY21 to ₹37,140 crore for FY22, loan book of the company has declined from ₹94,013 crore as on March 31, 2021, to ₹88,341 crore as on March 31, 2022 [June 30, 2022: ₹88,078 crore]. This is mainly on account of high repayments / prepayments in wholesale segment and furthermore the company is consciously trying to augment retail portfolio while running down high-ticket wholesale book. Within the real estate portfolio, the company is only lending towards existing projects having committed disbursals, to ensure completion of projects. As part of the 'Lakshya 2026' strategy, the company shall continue to focus on growing granular retail loan book, while maintaining stable asset quality and profitability.
Consolidated NIM (net interest income, divided by average adjusted total assets) has marginally improved from 5.52% as on March 31, 2021, to 5.62% as on March 31, 2022, which is attributed towards reduction in borrowings and relatively flat asset base. In sync with the company's focus on ramping up its retail infrastructure and reach, retail finance Opex increased from 3.53% during FY21 to 4.27% during FY22. Consequently, consolidated Opex has increased from 1.75% during FY21 to 2.14% during FY22. The employee- head count increased from 22,532 as on March 31, 2021, to 24,643 as on March 31, 2022. The credit cost has declined majorly on a Y-o-Y from 2.78% to 1.61%, on account of lower incremental provisioning requirement on loan book.
The return on total assets (ROTA) has improved slightly from 0.89% as on March 31, 2021, to 1.0% as on March 31, 2022. During Q1FY23, the company has reported improvement in consolidated profit after tax (PAT) of ₹261 crore as against PAT of ₹177 crore for the corresponding period last year majorly driven by reduction in interest expense, on account of lower cost of borrowings and lower credit costs. The profitability is expected to improve in current financial year primarily on account of increase in the revenue from retail businesses and lower provisioning requirement given the quantum of the macro prudential provisions that has been created (1.73% of the standard book as on June 30, 2022).
Going forward, CARE Ratings expect the profitability to improve as retail book assumes scale and operating expenses associated with expansion stabilise. Furthermore, the credit risk associated management overlays are expected to enable the company in absorbing asset quality shocks if any.

Presence in relatively riskier asset class: On the rural loans side, the Micro Loans (ML) segment remain risky on account of the nature of the customer profile and vulnerability of the borrowers' cash flows to economic shocks, as majority of the rural borrowers belong to the lower socioeconomic background. In the Farm Loans (FL) segment, cash flows are subjected to volatilities in the climatic conditions in different geographies. Furthermore, the Two-Wheeler (2W) segment is highly susceptible to the downturns in the economy. However, LTFHL has managed to mitigate these risks by stringent underwriting policies and diligent collection mechanism, which is demonstrated in its healthy collection efficiency. On the wholesale side, the real estate sector while had witnessed strong upsurge in demand, the sector has also been experiencing heightened risk on account of delays in construction and cash flows. Therefore, the asset quality in this segment is a key monitorable. However, the fact that LTFHL has control over cash flows through creation of escrow accounts, control over vendor payment and focused and continuous monitoring of the project, with sole lending relationship in majority of the projects, partially mitigates the risk. The real estate loans are majorly sanctioned to Category A developers, which further add some comfort towards the project completion risk. Given large ticket size and hence exposure to asset quality shocks, inherent risk in infrastructure financing remains. However, the company's reducing exposure to wholesale assets as well as rising share of granular retail assets mitigates credit risk.

Liquidity: Strong
Consolidated asset liability management (ALM) profile as on June 30, 2022, had cumulative positive mismatches in all buckets up-to 1-year tenor. The group had cash and cash equivalents in the form of cash, FD's, and liquid investments of ₹7,770 crore as on June 30, 2022. Apart from the above, the company has undrawn bank lines of ₹2,368 crore as on June 30, 2022, and backup line of ₹1,800 crore from L&T. All of this combined, the company maintains liquidity cover of 139.8% for scheduled debt repayments inclusive of interest for the next 3 months. Furthermore, the group's resource raising capability through integrated treasury also provides comfort.

Analytical approach: L&T Finance Holdings Limited (LTFHL), is the holding company for the financial services business of the L&T group, which owns (directly and indirectly) 100% in all of its lending subsidiaries. CARE Ratings has taken a consolidated approach for arriving at the rating given high business, operational and management linkages. CARE Ratings has also factored in the linkages with L&T Limited, which is the ultimate parent entity.

Applicable criteria
Policy on default recognition
Consolidation
Financial Ratios - Financial Sector
Rating Outlook and Credit Watch
Short Term Instruments
Non-Banking Financial Companies
Policy on Withdrawal of Ratings

About the company
LTFHL is RBI registered Non-Banking Finance Company - Core Investment Company (NBFC – CIC) and holding company for the financial services entities of the L&T Group. As on June 30, 2022, L&T held 66.23% equity stake in LTFHL. The group has three key business segments, namely, Rural Finance (comprising of Rural Business & Micro finance and Farm loans), Urban Finance (comprising of 2W loans, SME, consumer loans, HL/LAP) and (Wholesale Finance comprising of real estate and infra segment).

Consolidated financials:

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	Q1FY2023
Total operating income	13,753	12,324	3,136
PAT	949	1,049	261
Total Assets	1,06,563	1,05,306	1,02,106
Net Stage 3 (%)	1.57^	1.98	1.87
ROTA (%)	0.89	0.99	1.01

A: Audited #Adjusted Gearing is Total borrowings / Tangible Networth; UA: Unaudited; ^IND-AS (On Principal basis)
**adjusted total assets (net of intangible assets and deferred tax

Status of non-cooperation with previous CRA: NA

Any other information: NA

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: 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 (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Debentures-Non-Convertible Debentures	Proposed	-	NA	-	1000.00	CARE AAA; Stable
Preference Shares-Non-Convertible Redeemable Preference Share	INE498L04126	16-09-2019	--	16-12-2022	100.00	CARE AAA; Stable
Preference Shares-Non-Convertible Redeemable Preference Share	Proposed	-	NA	-	2736.00	CARE AAA; Stable
Commercial Paper-Commercial Paper (Standalone)	Proposed	-	NA	-	2500.00	CARE A1+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Debentures-Non-Convertible Debentures	LT	1000.00	CARE AAA; Stable	-	1)CARE AAA; Stable (30-Sep-21)	1)CARE AAA; Stable (08-Oct-20) 2)CARE AAA; Stable (21-Aug-20)	1)CARE AAA; Stable (21-Aug-19)
2	Commercial Paper-Commercial Paper (Standalone)	ST	2500.00	CARE A1+	-	1)CARE A1+ (30-Sep-21)	1)CARE A1+ (08-Oct-20) 2)CARE A1+ (21-Aug-20)	1)CARE A1+ (28-Mar-20) 2)CARE A1+ (21-Aug-19)
3	Preference Shares-Non-Convertible Redeemable Preference Share	LT	2836.00	CARE AAA; Stable	1)CARE AAA; Stable (15-Apr-22)	1)CARE AAA (RPS); Stable (30-Sep-21)	1)CARE AAA (RPS); Stable (08-Oct-20) 2)CARE AAA (RPS); Stable (21-Aug-20)	1)CARE AAA (RPS); Stable (04-Oct-19) 2)CARE AAA (RPS); Stable (21-Aug-19)

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities: NA

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

Sr. No.	Name of Instrument	Complexity Level
1	Commercial Paper-Commercial Paper (Standalone)	Simple
2	Debentures-Non-Convertible Debentures	Simple
3	Preference Shares-Non-Convertible Redeemable Preference Share	Highly Complex

Annexure-5: Bank lender details for this company

To view the lender wise details of bank facilities please click here

Note on complexity levels of the rated instruments: 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 us:
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