L&T Finance Holdings Limited

August 21, 2020

Ratings

Instruments	Amount (Rs. crore)	Ratings	Rating Action
Non-Convertible Debentures	1,000 (Rupees One Thousand Crore only)	CARE AAA; Stable [Triple A; Outlook: Stable]	Reaffirmed
Preference Shares	2,836 (Rupees Two thousand Eight Hundred and Thirty Six Crore only)	CARE AAA(RPS); Stable [Triple A (RPS); Outlook: Stable]	Reaffirmed
Commercial Paper	2,500 (Rupees Two Thousand and Five Hundred Crore only)	CARE A1+ (A One Plus)	Reaffirmed

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings continue to factor in the strategic importance of L&T Finance Holdings Limited (LTFHL) to the L&T Group as the flagship holding company of the Group's financial services business. The same is reflected through maintaining of ownership, sharing of the L&T brand name along with continued financial and management support.

Furthermore, the ratings continue to draw comfort from experienced management and LTFHL's strong resource raising ability coupled with comfortable liquidity position. CARE has also taken into account the diversified revenue streams through various subsidiaries in the wholesale and retail lending segment, with increasing proportion of retail portfolio, though at present the wholesale portfolio constitutes a larger share.

The ratings further take into account moderate but improving asset quality and growth trend in lending portfolio and profitability albeit some moderation in FY20. On a consolidated basis, the high concentration in the wholesale portfolio along with the exposure in the relatively riskier asset classes including micro loans, two wheelers and real estate, will remain a key rating monitorable. The ratings also take into account relatively high gearing levels on a consolidated basis, which have shown an improvement during FY20. Lockdown/restrictions imposed by the Government to contain spread of COVID-19 have impacted collections and disbursements of banks and NBFCs including LTFHL. Company's ability to maintain asset quality at reasonable levels during this period of lockdown/restriction and weak macroeconomic environment will remain key rating monitorable.

CARE takes note of the recent announcement of the Scheme of Amalgamation by way of merger by absorption involving amalgamation of L&T Housing Finance Limited (LTHF) and L&T Infrastructure Finance Company Limited (L&T Infra) with L&T Finance Limited (LTFL) (Scheme of Amalgamation). This Scheme of Amalgamation is subject to approval from NCLT and other approvals, as may be required. CARE's analytical approach on the LTFHL Group is on a consolidated basis, however it will still monitor the progress of the said merger in terms of LTFHL Group's expectation of creating a single unified entity to achieve operational efficiencies and have a simplified organizational structure. As per the LTFHL's management, there will be no change in the LTFHL Group's business approach; none of the business lending products will be discontinued on account of this Scheme of Amalgamation.

Continued support from L&T, maintaining profitability and asset quality considering the change in the product-mix are the key rating sensitivities.

Rating sensitivities

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

- Weakening of parent's credit profile
- Material deterioration in asset quality for LTFHL Group
- Increase in gearing (Debt/Net-worth) beyond 9x levels at LTFHL Group level
- Any prolonged and significant deterioration in asset quality on account of COVID-19 outbreak

Detailed description of the key rating drivers

Key Rating Strengths

Strong parentage and strategic importance for the parent company/Group

L&T is a major technology, engineering, construction, manufacturing and financial services conglomerate, with global operations. L&T operates in sectors like hydrocarbon, infrastructure, power, process industries and defence for customers in over 30 Countries around the World. L&T's total consolidated debt stands at Rs.1,410 billion as on March 31, 2020 with a market capitalization of approx. Rs.1,135 billion. LTFHL is in the financial service space and Group's flagship holding company. L&T Group considers LTFHL Group strategically important, which is reflected through brand linkages and financial and managerial support. Besides LTFHL also benefits from the expertise of L&T Limited in infrastructure segment, however LTFHL does not lend against any infrastructure projects of L&T. In terms of representation from L&T, Mr. R. Shankar Raman (currently serving a whole-time director and CFO at L&T Limited) is on LTFHL board as a non-executive director and he is also a member of Nomination and Remuneration Committee, Audit Committee, CSR Committee and Risk Management Committee. Further there has been instances of equity infusion in the past & extension of credit line of Rs. 2,000 crore which indicate continuous support from the parent. L&T Limited had infused equity capital of Rs. 2,000 crore in FY18.

Growth trend in lending portfolio and profitability albeit some moderation in FY20
The lending portfolio has grown at a 3 year CAGR of 15% as on March 31, 2020. The lending portfolio remained at similar level at Rs.96,308 crore as on March 31, 2020 (PY: Rs.96,076 crore). Overall disbursements during FY20 at Rs.37,160 crore were lower compared to Rs.58,224 crore in previous year. Company has maintained similar level of disbursements in rural finance segment compared to previous year; whereas disbursements in the real estate and infrastructure sector were lower. During FY20, the LTFHL consolidated PAT stood at Rs. 1,700 crore as against Rs. 2,232 crore compared to FY19. Post adjusting for DTA impact of Rs.473 crore, PAT stood at Rs.2,174 crore for FY20. For FY20, NIM (Net Interest Income to Average advances) stood at 6.13% as against 5.67% for FY19. Operating expenses as a percentage of total assets has reduced from 1.93% in FY19 to 1.78% in FY20. During FY20, LTFHL has done incremental provisions and macro-prudential provisions to take care of any additional volatility in asset performance going forward. Credit cost (provisions and write offs/average total assets) has increased to 1.87% during FY20 compared to 0.83% during FY19. For FY20, ROTA and RONW stood at 1.59% and 13.57% respectively, as against 2.29% and 21.01% in FY19. ROTA if adjusted for the one time impact of DTA will be at 2.04% for FY20.

Strong resource raising ability and capital position
The consolidated capital adequacy ratio (CAR) and tier I CAR stands at 21.60% and 17.70% respectively as on March 31, 2020 compared to 17.85% and 14.56% respectively as on March 31, 2019. Thus, there is sufficient headroom to raise Tier II capital. As on March 31, 2020, Tangible networth stood at Rs. 12,532 crore. In terms of resource mobilization, company has been able to raise Rs. 3,908 crore through retail NCD's in three tranches during the FY20. It has also raised Rs. 1,152 crore from IFC. The company has demonstrated its ability to raise long-term funding from broad based sources. Going forward, it has plans to further diversify its borrowings.

Comfortable liquidity profile
The consolidated ALM profile as on June 30, 2020 had cumulative positive mismatches upto 1 year bucket. It includes liquid assets in the form of cash, FD's and liquid investments of Rs. 9,082 crore as at June 30, 2020. Apart from the above, company has undrawn bank lines of Rs. 5,587 crore and backup line of Rs. 2,000 crore from L&T.

Diversified revenue streams with presence in the high yielding segments and relatively riskier asset class
LTFHL has presence across various financial services like corporate and retail finance and infrastructure through its subsidiaries and investment management services. In retail finance, company primarily deals in two wheeler, micro loans, farm equipment and housing loans, whereas in wholesale, it primarily does infrastructure finance and real estate finance. The remaining wholesale book (DCM and Structured Corporate Finance book) has been classified as defocused book which stands at Rs. 5,230 crore as on March 31, 2020 compared to Rs.9,403 crore as on June 30, 2019. As on March 31, 2020, total loan portfolio comprises of two wheeler (6%), micro loans (13%), farm equipment (8%), housing loans/LAP (12%), real estate (15%), infrastructure finance (40%) and defocused book (5%). Disbursements for FY20 stood at Rs.37,162 crore, out of which 50% were in rural finance followed by 28% in infrastructure segment, 13% in real estate and 9% in home loans/LAP.
In the micro loans, the customer profile is from lower socio-economic background; hence this segment is prone to event risks such as political, socio-economic and natural calamities. The asset quality is highly volatile during occurrence of such event risks. In the farm equipment financing, cashflows are subjected to volatilities in the rainfall conditions in any geographies. The real estate sector is witnessing slowdown and experiencing heightened refinancing risk, and therefore the asset quality in this segment is a key monitorable. To mitigate, the risks in the real estate book, exposure are taken on the basis of evaluation of the project, developer, location and stage of construction, sales velocity etc. Further it has control over cashflows through creation of escrow accounts, control over vendor payment and focussed & continuous monitoring of the project.

Moderate but improving asset quality
From FY19 onwards, company adopted Expected Credit Loss (ECL) model for classification of advances in Stage I, Stage II and Stage III and consequent provisioning on the same. Gross stage 3 and Net Stage 3 stood at 5.36% and 2.28% respectively as on March 31, 2020 compared to 5.90% and 2.40% respectively as on March 31, 2019. The provision coverage ratio has stood

at 59% as on March 31, 2020 compared to 61% as on March 31, 2019. As on June 30, 2020, Gross Stage 3 and Net Stage 3 stood at 5.24% and 1.71% respectively.

Relatively high gearing but capitalization is supported by timely equity infusion from parent
As on March 31, 2020, gearing (debt to tangible networth) at consolidated levels stood at 7.49x compared to 7.87x as on March 31, 2019. As per the LTFHL management, the gearing levels are not expected to significantly increase from the existing levels on account of healthy internal accruals and lower growth in the loan portfolio. The Interest coverage (PBT + Finance costs/ Finance costs) has shown a marginal decrease from 1.44x times as on March 31, 2019 to 1.36x as on March 31, 2020.

Concentration in wholesale book
The lending activity of LTFHL Group can be divided primarily into 2 broad classes:

- Retail Finance which comprises of Rural Finance (farm equipment, two wheelers, micro loans and consumer loans) and Housing Finance (Home loans and Loan against Property); and
- Wholesale book which comprises of Real Estate and Infrastructure Finance.

The company has classified DCM and Structured Corporate Finance as a defocused book, which constitute 5% of the outstanding lending business as on March 31, 2020. Wholesale book occupies 55% of the outstanding book as on March 31, 2020. Wholesale book (including defocused book) stood at 64% as on March 31, 2019. Given the company's plans to increase its retail book going forward, the proportion of wholesale book continues to decline but still remains a larger part of the outstanding portfolio.

Liquidity Profile- Strong: The consolidated ALM profile as on June 30, 2020 had cumulative positive mismatches upto 1 year bucket. It includes liquid assets in the form of cash, FD's and liquid investments of Rs. 9,082 crore as at June 30, 2020. Apart from the above, company has undrawn bank lines of Rs. 5,587 crore and backup line of Rs. 2,000 crore from L&T. RBI has permitted lenders to grant moratorium (as a part of regulatory measures under the Covid-19 Regulatory Package) till August 31, 2020. 44% of customers on retail side and 40% on wholesale side are under moratorium as on June 30, 2020. However, the Group has not sought moratorium from its lenders. The Group's resource raising capability through integrated treasury also provides comfort.

Analytical approach:
L&T Finance Holdings Limited (LTFHL), the flagship holding company for the financial services business of L&T Group, which owns (directly and indirectly) 100% in all 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 for arriving at the rating. The list of the subsidiaries considered for consolidation is as per Annexure 3.

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Financial ratios – Financial sector
CARE's criteria for Housing Finance Companies
Consolidation and Factor Linkages in Ratings
CARE's Criteria for Market Linked Notes/Debentures
Rating Methodology- Non Banking Finance Companies

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, 2020, L&T held 63.72% equity stake in LTFHL. The Group has three key business segments, namely rural finance (comprising farm equipment, two wheeler, micro loans and consumer loans), housing finance (comprising home loans and LAP) and wholesale lending (comprising infra finance and real estate finance).

Brief Financials* (Rs. crore)	FY19 (A)	FY20(A)
Total income	13,302	14,548
PAT	2,232	1,700
Interest coverage (times)	1.44	1.36
Total Tangible Assets	1,03,586	1,07,369
Net Stage 3 (%)	2.40	2.28
ROTA (%) (PAT/Average Total Assets)	2.29	1.59

A: Audited **Financials as per Ind-AS*
Status of non-cooperation with previous CRA: Not Applicable
Any other information: Not Applicable

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

Annexure-1: Details of Instruments/Facilities

ISIN	Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
INE498L04092	Redeemable Preference shares	12-Oct-18	-	12-Oct-21	250.0	CARE AAA (RPS); Stable
INE498L04100	Redeemable Preference shares	17-May-19	-	17-Nov-22	145.4	CARE AAA (RPS); Stable
INE498L04118	Redeemable Preference shares	03-Jun-19	-	02-Dec-22	63.7	CARE AAA (RPS); Stable
INE498L04126	Redeemable Preference shares	16-Sep-19	-	16-Dec-22	100.0	CARE AAA (RPS); Stable
INE498L04134	Redeemable Preference shares	20-Sep-19	-	20-Jan-23	150.0	CARE AAA (RPS); Stable
INE498L04142	Redeemable Preference shares	27-Sep-19	-	10-Feb-23	150.0	CARE AAA (RPS); Stable
NA	Redeemable Preference shares (proposed)	-	-	-	1,976.9	CARE AAA (RPS); Stable
NA	Non-Convertible Debentures (proposed)	-	-	-	1,000.0	CARE AAA; Stable
NA	Commercial Paper	-	-	7 days-1 year	2,500.0	CARE A1+

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	1000.00	CARE AAA; Stable	-	1)CARE AAA; Stable (21-Aug-19)	1)CARE AAA; Stable (08-Oct-18)	1)CARE AAA; Stable (26-Feb-18) 2)CARE AA+; Positive (09-Oct-17) 3)CARE AA+; Stable (13-Jul-17)
2.	Commercial Paper	ST	2500.00	CARE A1+	-	1)CARE A1+ (28-Mar-20) 2)CARE A1+ (21-Aug-19)	1)CARE A1+ (26-Jun-18) 2)CARE A1+ (08-Oct-18)	1)CARE A1+ (26-Feb-18) 2)CARE A1+ (14-Nov-17) 3)CARE A1+ (09-Oct-17)
3.	Preference Shares-Non Convertible Redeemable Preference Share	LT	2836.00	CARE AAA (RPS); Stable	-	1)CARE AAA(RPS); Stable (21-Aug-19) 2)CARE AAA(RPS); Stable (04-Oct-19)	1)CARE AAA(RPS); Stable (08-Oct-18)	1)CARE AAA (RPS); Stable (26-Feb-18) 2)CARE AA+ (RPS); Positive (09-Oct-17) 3)CARE AA+ (RPS); Stable (13-Jul-17)

Annexure 3: List of subsidiaries/associates considered for consolidation as on 31st March 2020

Sr. No	Name of Company
1	L&T Infrastructure Finance Company Limited
2	L&T Investment Management Limited
3	L&T Mutual Fund Trustee Limited
4	L&T Financial Consultants Limited
5	L&T Infra Investment Partners Advisory Private Limited
6	L&T Infra Investment Partners Trustee Private Limited
7	L&T Finance Limited
8	L&T Housing Finance Limited
9	L&T Capital Markets Limited (divestment of entire stake from April 24, 2020)
10	L&T Infra Debt Fund Limited
11	Mudit Cement Private Limited
12	L&T Infra Investment Partners Fund
13	L&T capital markets (middle east) Limited

Annexure 4: Complexity levels of the rated instrument

Sr. No.	Name of the Instrument	Complexity Level
1.	Debentures-Non Convertible Debentures	Simple
2.	Redeemable Preference shares	Highly Complex
3.	Commercial paper	Simple

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

Contact us

Analyst Contact 1
Name - Mr. Ravi Kumar
Contact no.- +91-22-6754 3421
Email ID - ravi.kumar@careratings.com

Analyst Contact 2
Name - Mr. Mitul Budhbhatti
Contact no.- +91-22-6754 3547
Email ID – mitul.budhbhatti@careratings.com

Business Development Contact
Name: Mr. Ankur Sachdeva
Contact no. : +91-22-6754 3495
Email ID - ankur.sachdeva@careratings.com

Media Contact
Name - Mr. Mradul Mishra
Contact no. – +91-22-6837 4424
Email ID – mradul.mishra@careratings.com

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(*For more details please refer to our rationale for the entity published on October 23, 2019*)

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