

Press Release

Edelweiss Retail Finance Limited

February 06, 2020

Rating Downgraded



Total Facilities Rated*	Rs. 100.00 Cr.
Facilities Rated	Rs. 100.00 Cr.
Long Term Rating	ACUITE AA-/ Negative (Rating downgraded from ACUITE AA/Negative)

* Refer Annexure for details

Rating Rationale

Acuité has downgraded the long term rating to '**ACUITE AA-**' (**read as ACUITE double A minus**) from '**ACUITE AA**' (**read as ACUITE double A**) on the Rs. 100.00 Cr. Unsecured Subordinated Perpetual Non-Convertible Debenture of Edelweiss Retail Finance Limited (ERFL). The outlook continues to be '**Negative**'.

The revision in rating is primarily driven by Acuité's expectation of a significant increase in credit costs due to asset quality pressures, attributable to the overall tepid operating environment, and the moderation in the profitability metrics of the Edelweiss Group, during FY2020. The Net NPAs increased from Rs. 300 Cr. as on March 31, 2019 to Rs. 493 Cr. as on September 30, 2019. The Net NPA ratio as on September 30, 2019 has increased to 1.7 percent from 0.8 percent as on March 31, 2019. Besides the stress in its wholesale lending segment, Acuité also notes asset quality pressure building up in the retail portfolio of the Group during H12020. The Net NPAs of the retail segment increased from Rs. 150 Cr. as on March 31, 2019 to Rs. 181 Cr. as on Sept 30, 2019.

The Return on Average Assets (ROAA) has contracted from 1.7 percent during FY2019 to 0.6 percent (annualized) in H12020. Acuité expects these asset quality and profitability pressures to be sustained over the near to medium. Edelweiss Group has also exhibited a decline in its loan book from Rs. 36,129 Cr. as on March 31, 2019 to Rs. 31,289 Cr. (including Rs. 1565 Cr. assets held for sale) as on Sept 30, 2019. The contraction in loan book is primarily driven by management's strategic decision to consciously scale down the exposure to the wholesale segment coupled with subdued disbursements in the retail segment.

Acuité believes that while the group has been facing asset quality and profitability pressures, the credit profile is significantly supported by the group's demonstrated ability to attract funds in the form of debt or equity from diverse sources. The Group has completed four rounds of equity raising from global institutions indicating acceptability amongst domestic and overseas investors.

Analytical approach:

Acuité has taken a consolidated view on Edelweiss Financial Services Limited along with its 59 subsidiaries and 2 associates (as on March 31, 2019), collectively referred to as 'Edelweiss group'. This is on the back of common promoters, shared brand name, significant operational and financial synergies between the companies.

Acuité rates Unsecured Subordinated Non-Convertible Debenture (Perpetual NCDs) at a lower level vis. a. Vis. the other debt instruments of the same issuer, in view of the significant loss absorption characteristics associated with these perpetual NCDs. The issuer may be required to skip/defer the coupon/interest payment in case of certain events such as decline in CAR below regulatory thresholds.

Extent of consolidation: Full.

About the Group:

Edelweiss Financial Services Limited (EFSL), the holding company of Edelweiss Group, was incorporated in 1995 and has diversified its line of operations across various fund based and non-fund based businesses. Edelweiss offers a bouquet of financial services, to a diversified client base across domestic and global geographies. Its key line of business includes; credit (retail, corporate and distressed), advisory (wealth management, asset management and capital markets) and insurance (life and general).

The Edelweiss Group comprises Edelweiss Financial Services Limited, 59 subsidiaries and 2 associate companies (as on March 31, 2019). Edelweiss group has a pan India presence with a global footprint extending across geographies with offices in New York, Mauritius, Dubai, Singapore, Hong Kong and UK.

About the company: ERFL

Edelweiss Retail Finance Limited (erstwhile Affluent Dealcom Private Limited) was incorporated in 1997 as a Private limited company. The company was acquired by Edelcap Securities Limited (ESL; stepdown subsidiary of Edelweiss Financial Services Limited) and converted to a public limited company. Subsequently, the name was changed to Edelweiss Retail Finance Limited in 2014.

ERFL's key product offerings include SME Finance, loan against property, loan against shares, construction finance and rural finance.

Key Rating Drivers:

Strengths:

- Strong parentage and diversified product offerings:**

Edelweiss Group is promoted by Mr. Rakesh Shah and Mr. Venkat Ramaswamy, who are seasoned professionals in the financial services industry with over two decades of experience. The promoters are supported by experienced professionals who are into financing, wealth, and asset management businesses. The group has a diverse business profile in financial services with presence in segments such as retail credit (including agri-finance), wholesale lending, warehousing services, asset reconstruction, wealth management, asset management, capital market including stock broking and insurance business. The various verticals of the group as mentioned above are now proposed to be organized under three broad categories i.e. Credit (Wholesale and retail lending), Insurance and Advisory (Wealth management, Capital market, Asset management and Asset reconstruction).

The Group had loan book of Rs. 31,289, Cr. as on September 30, 2019, of which Retail credit extended was Rs. 15, 111 Cr. and wholesale credit was Rs. 16,178 Cr. The wholesale segment comprised loans to realtors and structured credit. The Group has been attempting to gradually increase its exposure to retail segment and low to mid ticket lending. It proposes to reduce its exposure to the wholesale segment and reorient the portfolio towards small and mid-corporate lending segments. To increase the penetration under smaller ticket lending to mid corporates, Edelweiss Group has started co-origination of loans along with banks as per recent RBI guidelines. This would result into a co lending structure where Company would hold only a part of the loan on its books and the rest by the banks. So far it has signed Co-lending agreement with 4 Public Sector Banks.

Besides the fund based activities, Edelweiss Group also has an established franchise in the capital market related business across corporate finance and advisory domains including broking, investment banking, wealth management, and asset management. As on September 30, 2019, the group had customer assets AUM of Rs. 1,65,200 Cr. under the advisory vertical. Most of the businesses of the group present significant synergies amongst themselves and growth potential both on the assets and liabilities side. The access to a pool of HNIs can be leveraged to create fund based structures which can be utilised to support the AUM growth of the group.

Acuité believes Edelweiss group's established position in financial services and diversified range of fee and fund based product offerings will continue to support its business risk profile.

- Diversified funding profile:**

Edelweiss group has always demonstrated healthy resource raising ability from diverse lenders and investors. The Group's Net worth stood at Rs. 7773 Cr. as on September 30, 2019 (Rs. 7674 Cr. as on March 31, 2019). The Group has demonstrated its ability to attract investments from reputed international investors such as CDPQ (Caisse de dépôt et placement du Québec), KORA Management and Sanaka Capital. CDPQ has committed US\$ 250 Million (~Rs. 1800 Cr.) to the group, of which Rs. 1039.5 Cr. has already been received by ECL Finance Limited in May 2019, the balance tranches are expected to be received in FY2020 and FY2021. Similarly, Kora Management and Sanaka

Capital have committed US\$75 mln (Rs 525 Crs) and US\$ 44 mln (Rs 308 Cr.) respectively to the group. Edelweiss Financial Services Limited, the flagship company of Edelweiss Group is listed on the stock exchanges (Market capitalisation of Rs. 8188.7 Cr. on Feb 03, 2020) and its public shareholding includes institutional investors like Mutual funds, and Foreign Portfolio investors. The Group's Capital adequacy stood at 21.1 percent as on September 30, 2019 as against 18 percent as on March 31, 2019, of which Tier I capital adequacy stood at 16.2 percent and 15.1 percent respectively.

The Group has reduced its borrowings levels from Rs. 43,201 Cr. as on March 31, 2019 to Rs. 38,695 Cr. as on September 30, 2019. Of the total borrowings as on September 30, 2019, ~49 percent is being funded through banks, 27 percent through retail investors, 10 percent by mutual funds, and the balance 14 percent mainly through corporates, PFs, and insurance. The Group's NCD issuances targeted at the retail investor have been well accepted in the markets, which has helped the Group in increasing its retail funding to Rs. 10448 Cr. (27 percent) as on September 30, 2019 as against Rs. 5371 Cr. as on March 31, 2018. The strong patronage of the Group amongst retail investors augurs well from a future funding standpoint, since retail investors are expected to be more stable than wholesale investors.

Most of the bank borrowings and NCDs are long tenured with tenures beyond 3 years. The Group has significantly reduced its dependence on short term borrowings like Commercial Paper. In view of the tight liquidity situation caused by these events, the Group focused on conserving its liquidity rather than going in for asset growth. The Group is also exploring options like securitization and Partial Guarantee based structures to support its financing requirements.

The group's financial flexibility is supported by their demonstrated ability to mobilise resources from diversified set of investors across domestic banks, Institutional investors and lenders, foreign investors and domestic retail investors amongst others. The Group also has large institutional client base in its various funds such as distressed credit fund, Real estate Credit Fund, Structured debt fund and Infrastructure Fund. The aggregate size of all these funds is Rs. 19,700 Cr. of which Rs. 10,000 Cr. is already deployed as on September 30, 2019. The group has also demonstrated its ability to support chunky real estate projects with a need for completion funding by setting up an AIF with South Korea based Meritz Group with a corpus of USD 425 million.

Acuité expects the Group to continue to benefit from diversified funding mix across domestic banks, Institutional investors and lenders, foreign investors and domestic retail investors amongst others.

Weaknesses:

- **Increased pressures on asset quality and profitability metrics:**

Edelweiss Group's key product offerings are spread across two segments i.e. retail segments and wholesale segments. The retail segment (48 percent of the loan book as on Sept 30, 2019) comprises housing finance, Loan against Property, Construction finance, SME loans, Loan against Shares while the wholesale segment (52 percent) comprises structured Credit and wholesale mortgage. The group's loan book has declined from Rs. 36,1293 Cr. as on March 31, 2019 to Rs. 31,289 Cr. as on September 30, 2019. The decline in the loan book is primarily driven by the management's strategic decision to consciously scale down the exposure to the wholesale segment, coupled with subdued disbursements in the retail segment. While the loan book has witnessed a decline, The Group's Net NPA assets over the said period have spiked from Rs. 300 Cr. (0.8% of loan assets) as on March 31, 2019 to Rs. 493 Cr. (1.7 percent of loan assets) as on September 30, 2019. Of the overall NNPA as on September 30, 2019, 63 percent was contributed by wholesale segment. As on September 30, 2019, top 25 exposures accounted for 41 percent pf the overall loan book. The group's wholesale segment mostly comprises exposures to real estate developers for their projects. The cash flows of these realtors and the quality of these exposures is linked to the revival in the real estate cycle.

The group has already initiated steps to prune its exposure to the wholesale segment through various initiatives such as slowing down fresh sanctions and sell down of existing assets to dedicated funds. In Q3 FY20 the group launched a USD 425 mn corpus last mile Real Estate Financing AIF in partnership with South Korean financial conglomerate Meritz Financial Group. The first tranche of the USD 240 million corpus is completed. Edelweiss holds 30 percent stake in this fund and the remaining 70 percent is held by Meritz. Meritz Financial Group, the Seoul headquartered conglomerate.

Since the group has decided to curtail its exposure to wholesale segment, the retail products like retail mortgage, SME lending, LAS along with smaller ticket lending to mid corporates under the co-

origination model with banks are expected to be the drivers of future growth. The group's retail strategy is evident from the fact that of the total disbursements of Rs. 1990 Cr. during the period April to Sept 2019, Rs. 1369 Cr. (~69 percent) comprised the retail disbursements. As regards the retail segment, SME loans and retail mortgage comprise the key products contributing to ~40 percent of the overall loan book as on Sept 30, 2019. The retail portfolio is relatively more granular with a median ticket size of ~1 Cr. for secured SME loan, Rs. 15 lakhs for housing loan and 19 lakhs for LAP.

The sharp spike in NPAs has resulted in an increase in provisions during H12020. The credit costs increased from Rs. 456 Cr. for FY2019 to Rs. 446 Cr. for H12020. The group expects the credit costs for H2FY2020 to be at levels similar to the first half. As per the discussions with Edelweiss group's management, they intend to maintain high liquidity buffers to support the business requirements. Higher credit costs, borrowing costs and costs of managing higher liquidity cushion leading to lower Net Interest Income (NII) is likely to have a major bearing on the profitability of the group for FY2020. The future trend in credit costs will be linked to the fresh slippages in both the segments i.e. retail as well as wholesale segments. With the increasing focus on relatively less risky retail segment, the portfolio is expected to be more granular going forward. However the group may face further profitability pressures in view of the relatively moderate margins in the 'commoditised' retail segment. The cost to income ratios (ex-insurance) has spiked from 50 percent for FY2019 and Q1FY2020 to 56 percent for Q2FY2020.

Acuité believes that Edelweiss Group's ability to attain any significant improvement in asset quality and profitability parameters over the near term will be impeded by the tepid economic environment coupled with the intense competition especially in the retail segment.

Rating Sensitivities

- Movement in Net NPA and ROAA
- Higher than expected decline in AUM

Material Covenants

Edelweiss Group is subject to covenants stipulated by its lenders/investors in respect of various parameters like capital structure, asset quality among others. As per confirmation from Edelweiss, they are compliant with covenants stipulated by lenders/investors.

Liquidity Position: Adequate

ERFL's liquidity profile is supported by the group's centralised treasury operations and adequate liquidity position. The group has demonstrated the ability to raise medium to long term funding from banks/capital markets which should support the Group's ability to plug any possible mismatches. The Group's liquidity profile is supported by funding from diversified base i.e. banks and financial institutions along with capital market instruments like CBLO borrowings, Commercial Papers and NCDs. The Group on a consolidated basis had maintained liquidity buffers of Rs. 10, 300 Cr. (includes short term loan book of Rs. 4150 Cr.) as on December 31, 2019. ERFL is supported by strong parentage of Edelweiss Group and can tap the excess liquidity available with the Group in case of future exigencies. Further, the group has received fresh sanction for securitization of Rs. 2930 Cr. during the period April to December 2019.

Outlook: Negative

Acuité believes that the Group's credit profile could face pressures over the near to medium term on account of increasing asset quality and profitability pressures on the back of a tepid operating environment. The outlook may be revised to Stable in case the Edelweiss Group is able to demonstrate a significant and sustainable improvement in its Net NPA levels (less than 1 percent) and profitability indicators (ROAA goes above 1.5 percent). Conversely, the rating will be downgraded in case of a further slippages in asset quality or significant challenges in achieving an improvement in profitability parameters.

EFSL- Key Financials (Consolidated)

	Unit	FY19 (Actual)	FY18 (Actual)
Total Assets	Rs. Cr.	64052.9	62892.2
Total Income*	Rs. Cr.	6159.2	5044.5

PAT	Rs. Cr.	995.17	863.18
Net Worth	Rs. Cr.	7674.5	6906.0
Return on Average Assets (RoAA)	(%)	1.65	1.55
Return on Average Net Worth(RoNW)	(%)	14.34	14.70
Total Debt/Tangible Net Worth (Gearing)	Times	6.06	7.09
Gross NPA	(%)	1.87	1.75
Net NPA	(%)	0.83	0.70

*Total income equals to Total Income net off interest expense

ERFL - Key Financials (Standalone)

	Unit	FY19 (Actual)	FY18 (Actual)
Total Assets	Rs. Cr.	2439.1	3323.1
Total Income*	Rs. Cr.	185.2	168.4
PAT	Rs. Cr.	33.9	27.7
Net Worth	Rs. Cr.	463.2	430.1
Return on Average Assets (RoAA)	(%)	1.2	1.1
Return on Average Net Worth(RoNW)	(%)	7.6	7.5
Total Debt/Tangible Net Worth (Gearing)	Times	4.2	6.6
Gross NPA	(%)	3.14	1.15
Net NPA	(%)	2.7	0.8

*Total income equals to Total Income net off interest expense

Applicable Criteria

- Non-Banking Financing Entities: <https://www.acuite.in/view-rating-criteria-10.htm>
- Consolidation of Companies: <https://www.acuite.in/view-rating-criteria-22.htm>
- Financial Ratios and Adjustments: <https://www.acuite.in/view-rating-criteria-20.htm>
- Default Recognition: <https://www.acuite.in/view-rating-criteria-17.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/criteria-complexity-levels.htm>

Rating History (Upto last three years)

Date	Name of Instrument / Facilities	Term	Amount (Rs. Cr)	Ratings/Outlook
1-August-2019	Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	20.00	ACUITE AA/Negative (Reaffirmed; Outlook revised to Negative from Stable)
	Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	25.00	ACUITE AA/Negative (Reaffirmed; Outlook revised to Negative from Stable)
	Proposed Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	55.00	ACUITE AA/Negative (Reaffirmed; Outlook revised to Negative from Stable)
03-August -2018	Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	20.00	ACUITE AA/ Stable (Reaffirmed)
	Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	25.00	ACUITE AA/ Stable (Reaffirmed)
	Proposed Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	55.00	ACUITE AA/ Stable (Reaffirmed)

02- December-2017	Proposed Unsecured Subordinated Perpetual Non-Convertible Debentures	Long Term	100.00	ACUITE AA/ Stable (Assigned)
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***Annexure – Details of instruments rated**

ISIN	Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Rs. 100.00 Cr.						
INE528S08050	Unsecured Subordinated Perpetual Non-Convertible Debentures	26-Dec-17	9.75%	NA	20.00	ACUITE AA-/Negative (Rating Downgraded from ACUITE AA/Negative)
INE528S08068	Unsecured Subordinated Perpetual Non-Convertible Debentures	07-Feb-18	10.00%	NA	25.00	ACUITE AA-/Negative (Rating Downgraded from ACUITE AA/Negative)
-	Proposed Unsecured Subordinated Perpetual Non-Convertible Debentures	NA	NA	NA	55.00	ACUITE AA-/Negative (Rating Downgraded from ACUITE AA/Negative)

- The following Subsidiaries and Associates of EFSL have been considered for consolidation:**

Sr.No.	Name of Entity	Relationship with EFSL
1	Edelweiss Securities Limited	Subsidiary
2	Edelweiss Finance & Investments Limited	Subsidiary
3	ECL Finance Limited	Subsidiary
4	Edelweiss Global Wealth Management Limited	Subsidiary
5	Edelweiss Insurance Brokers Limited	Subsidiary
6	Edelweiss Trustee Services Limited	Subsidiary
7	Edelcap Securities Limited	Subsidiary
8	Edelweiss Asset Management Limited	Subsidiary
9	Ecap Equities Limited	Subsidiary
10	Edelweiss Broking Limited	Subsidiary
11	Edelweiss Trusteeship Company Limited	Subsidiary
12	Edelweiss Housing Finance Limited	Subsidiary
13	Edelweiss Investment Adviser Limited	Subsidiary
14	EC Commodity Limited	Subsidiary
15	Edel Land Limited	Subsidiary
16	Edelweiss Custodial Services Limited	Subsidiary
17	Edel Investments Limited	Subsidiary
18	Edelweiss Rural & Corporate Services Limited	Subsidiary
19	Edelweiss Comtrade Limited	Subsidiary
20	Edel Finance Company Limited	Subsidiary
21	Edelweiss Retail Finance Limited	Subsidiary
22	Edelweiss Multi Strategy Fund Advisors LLP	Subsidiary
23	Edelweiss Resolution Advisors LLP	Subsidiary
24	Edelweiss Holdings Limited	Subsidiary
25	Edelweiss General Insurance Company	Subsidiary
26	Edelweiss Finvest Private Limited	Subsidiary

27	Edelweiss Securities (IFSC) Limited	Subsidiary
28	Alternative Investment Market Advisors Private Limited	Subsidiary
29	Edelweiss Securities Trading and Management Private Limited	Subsidiary
30	Edelweiss Securities and Investment Private Limited	Subsidiary
31	Edelweiss Securities (Hong Kong) Private Limited	Subsidiary
32	EC Global Limited	Subsidiary
33	EC International Limited	Subsidiary
34	EAAA LLC	Subsidiary
35	EFSL International Limited	Subsidiary
36	Edelweiss Capital (Singapore) Pte. Limited	Subsidiary
37	Edelweiss Alternative Asset Advisors Pte. Limited	Subsidiary
38	Edelweiss International (Singapore) Pte. Limited	Subsidiary
39	Edelweiss Investment Advisors Private Limited	Subsidiary
40	Aster Commodities DMCC	Subsidiary
41	Edelweiss Financial Services (UK) Limited	Subsidiary
42	Edelweiss Financial Services Inc.	Subsidiary
43	Edelweiss Alternative Asset Advisors Limited	Subsidiary
44	EW Clover Scheme - 1	Subsidiary
45	Edelvalue Partners	Subsidiary
46	Edelgive Foundation	Subsidiary
47	Lichen Metals Private Limited	Subsidiary
48	EW India Special Assets Advisors LLC	Subsidiary
49	Edelweiss Private Equity Tech Fund	Subsidiary
50	Edelweiss Value and Growth Fund	Subsidiary
51	Edelweiss Asset Reconstruction Company Limited	Subsidiary
52	EW Special Opportunities Advisors LLC	Subsidiary
53	Edelweiss Tokio Life Insurance Company Limited	Subsidiary
54	Allium Finance Private Limited	Subsidiary
55	Retra Ventures Private Limited	Subsidiary
56	Edelweiss India Capital Management	Subsidiary
57	Cross Border Synergy Pte. Limited	Subsidiary
58	Edelweiss Tarim Urnleri Anonim Sirketi	Subsidiary
59	EW SBI Crossover Advisor LLC	Subsidiary
1	Allium Finance Private Limited	Associates
2	Aeon Credit Services India Private Limited	Associates