CARE Ratings
Professional Risk Opinion
20 PLUS YEARS Analytical Excellence

No. CARE/HO/RR/2016-17/1271

Mr. Pankaj Thapar,
Chief Financial Officer,
IndoStar Capital Finance Ltd.
One Indiabulls Center, 17th Floor, Tower 2A,
Jupiter Mills Compound, Senapati Bapat Marg,
Mumbai- 400013.

June 30, 2016

Dear Sir,

Credit rating of various debt instruments/ facilities

Please refer to our letter dated June 17, 2016 on the above subject.

2. The final rationale for the ratings is attached as an Annexure - I. Kindly note that the rationale would be published in the forthcoming issue of our monthly journal, 'CAREVIEW'.

3. A write-up (brief rationale) on the above ratings is proposed to be issued to the press shortly. A final version of this is enclosed for your perusal as Annexure - II.

If you have any further clarifications, you are welcome to approach us.

Thanking you,

Yours faithfully,

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Encl: As above

Annexure I
Rating Rationale
INDOSTAR CAPITAL FINANCE LTD. (ICF)

Ratings

Instrument / Facility	Amt Rated (Rs crore)	Rating[1]	Remarks
Long term debt programme	3,750 (enhanced from Rs.3,000 crore)	**CARE AA- (Double A Minus)**	Reaffirmed
Commercial Paper	750	**CARE A1+ (A One Plus)**	Reaffirmed
Total	**4,500 (Rupees Four Thousand Five Hundred Crore only)**		

Rating rationale

The ratings factor in ICF's strong institutional sponsors as well as their capital, operational and management support. The rating further takes into account the company's experienced management, good risk management processes, strong capitalisation levels as well as comfortable gearing, healthy financial performance, comfortable asset quality & liquidity position. The rating is, however, constrained due to the limited track record of operations, client concentration risk and exposure to real estate segment which is a relatively riskier asset class. Continued sponsor support, profitability, business diversification, client concentration and asset quality are its key rating sensitivities.

Company Profile

IndoStar Capital Finance Ltd. (ICF) is registered with the Reserve Bank of India (RBI) as a systemically important non-deposit taking NBFC. It was originally incorporated as R. V.Vyapar Pvt. Ltd. on July 21, 2009 and the company was renamed as 'IndoStar Capital Finance Pvt. Ltd.' on November 15, 2010. The company however started disbursements from Q1FY12. (refers to the period April 01 to June 30). The company was converted into a public limited company on May 28, 2014 and consequently its name was changed to 'IndoStar Capital Finance Limited'.

ICF had been established by global financial institutions including Goldman Sachs, Ashmore group PLC, Everstone Capital, Baer Capital Partners and ACP Investments with the objective of developing an independent wholesale lending institution in India. During FY15, Ashmore

[1] *Complete definitions of the ratings assigned are available at www.careratings.com*

Group PLC exited ICF with its stake being acquired by Everstone and ACP Investments. The sponsors hold their stake in ICF through IndoStar Capital, Mauritius which holds 97.30% stake in the company.

ICF is engaged mainly into wholesale lending with products ranging from corporate finance, developer financing, working capital financing, acquisition financing & loan against shares. With a view to diversify its operations, the company has ventured into SME financing wherein Small and Medium Enterprises are financed business loans against security of the property. ICF's loan portfolio and networth stood at Rs.4,265 crore and Rs.1,531 crore respectively as on March 31, 2016.

Credit Risk Assessment

Strong sponsors

ICF had been established by global financial institutions including Goldman Sachs, Ashmore group PLC, Everstone Capital, Baer Capital Partners and ACP Investments. During FY15, Ashmore Group PLC exited ICF with its stake being acquired by Everstone and ACP Investments. The sponsors hold their stake in ICF through IndoStar Capital, Mauritius which holds 97.30% stake [P.Y.:87.61%] in the company. IndoStar Capital, Mauritius is held by Everstone (49.45%), ACP Investments (16.35%), Goldman Sachs (18.75%), Baer Capital (10.79%) and CDIB Investment (4.66%). ICF's credit profile derives comfort from management and financial support of sponsor investors at regular intervals. Besides, the rich experience of the sponsor investors in Indian and global financial markets are expected continue to help ICF in strengthening its business opportunities.

Experienced Management

ICF has management with rich experience in the financial sector. Some of the key management personnel include Mr. Vimal Bhandari, MD & CEO of ICF (former Country Head at AEGON NV and has more than 17 years of experience with IL&FS), Mr Pankaj Thapar, CFO (Former Managing Director in the Private Equity business of Everstone Capital Advisors, has more than 25 years of experience in the financial and corporate sector) and Mr. Shailesh Shirali, Managing Director & Head- Corporate Lending & Markets (former CEO- Corporate lending at Future Capital Holdings Ltd.). The Board of Directors and management team at all levels have been drawn from leading players in the financial services space.

Strong solvency parameters and comfortable liquidity position

The company continues to maintain robust capitalization levels supported by regular equity infusions by sponsors. As on March 31, 2016, ICF's CAR stood at 34.15% [P.Y.: 32.64%] while Tier I CAR stood at 33.77% [P.Y.: 32.29%]. High proportion of Tier I capital provides considerable headroom for raising Tier II capital to support future business growth. Further, the company had comfortable gearing levels of 1.97x as on March 31, 2016 [P.Y.: 2.02x].

As on March 31, 2016, the liquidity profile of ICF was comfortable with positive cumulative mismatches across most time buckets. While the average loan book tenure is 4 years, the company has tapped similar tenure bank/ market borrowings. Further, as per company's prudent liquidity policy, ICF maintains cash/ cash equivalents and unutilized lines of credit to the tune of 15% of networth due to which its liquidity profile is comfortable.

Well defined risk management processes & secured lending

ICF draws experience from its global investors for creating its risk management framework. It has well-defined credit criteria for sanction of loan including assessing track record & borrowing capacity of borrower, credit history of borrower, quality of collaterals.

Over the last few quarters with a view to diversify the portfolio risk, the company has started SME financing. As on March 31, 2016, ICF's gross loan portfolio stood at Rs.4,272 crore of which real estate developer funding comprised 40.2% [P.Y.: 30.0%], corporate financing- 48.9% [P.Y.: 66.5%], loans against shares- 5.5% [P.Y.: 2.9%] with the remaining 5.4% being SME financing (SME loans against property). Going forward, the share of retail SME financing is expected to grow further which shall enable the company in diversifying its business operations.

Financial performance

During FY16, the company reported 21.5% y-o-y growth in total income vis a vis 33.1% growth in the previous year which was primarily on account of deceleration in portfolio growth owing to economic factors. Despite slowdown in portfolio growth, the company continued to witness improved margins due to reduction in cost of borrowings. While cost of borrowings declined by roughly 30-40bps during FY16, its cost of lending reduced by 10-15bps during the same period since a majority of its loans (~63% as on March 31, 2016) are on fixed rates. Consequently, ICFs NIM improved by 50bps to 6.35% during FY16. Operating expenses increased by 38.8% y-o-y during FY16 [P.Y.: 20.1%] led by company's foray in SME financing and the resultant rise in branch and manpower expenses. During FY16, the

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company set up 4 branches to cater to SME financing business in Mumbai, Pune, Bangalore and Delhi. The company's operating costs are expected to rise in near to medium term given the company plans to foray into newer geographies for tapping SME financing business. Improved margins and rise in fee income have offset rise in operating expenses thereby resulting into an improvement in overall profitability. ICF reported PAT of Rs. 191 crore during FY16 [P.Y.: Rs.149 crore] on total income of Rs.641 crore [P.Y.: Rs.528 crore]. ICF's ROTA stood at 4.41% during FY16 [P.Y.: 4.18%].

Comfortable Asset quality

The company has comfortable asset quality parameters. During FY15 and FY16, there were no incremental asset quality slippages and the company continued to have one account in the NPA category. As on March 31, 2016, GNPA and NNPA stood at 0.23% [P.Y.: 0.57%] and 0.19% [P.Y.: 0.52%] while net NPA to networth stood at 0.52 % [P.Y.: 1.37%].

Relatively low track record and portfolio seasoning

ICF has a relatively short operating track record as it started its wholesale lending operations in April 2011 and SME financing in March 2015. Though a significant portion of its wholesale portfolio has witnessed churn (given the average tenure of the portfolio at around 4 years), its SME financing portfolio is fairly nascent. Going forward, the company's ability to maintain asset quality in newer lending products while expanding business operations is a key monitorable.

High customer concentration risk

Given the bulky nature of its lending operations (around 95% of ICFs portfolio is wholesale in nature); ICF is exposed to concentration risk. Although the company has recently ventured into SME financing which is expected to reduce concentration levels going forward, the portfolio is at nascent stage and constituted roughly 5% of its total portfolio as on March 31, 2016. On the wholesale lending front, top 10 exposures as on March 31, 2016 constituted 32.4% of total portfolio [P.Y.: 39.8%] and 90.4% of networth [P.Y.: 107.1%].

Further considering the higher ticket sizes of its wholesale loan book, slippages in few large accounts can have an adverse impact on asset quality. As on March 31, 2016, around 81.6% of ICF's corporate loan book had ticket size of Rs.50 crore or above.

Exposure to real estate segment

ICF continues to have high exposure to relatively riskier real estate developer funding segment. Although the company has started diversifying its operations by venturing into SME financing, its real estate portfolio continued to be on higher side and constituted 40% of total portfolio outstanding as on March 31, 2016 [P.Y.: 30%].

Prospects

Over the last few years, the NBFC sector has gained systemic importance with increase in share of NBFC total assets to bank total assets. The same has resulted in the Reserve Bank of India (RBI) taking various policy actions resulting in NBFCs attracting higher support and regulatory scrutiny. The RBI has revised the regulatory framework for NBFCs which broadly focuses on strengthening the structural profile of NBFC sector, wherein focus is more on safeguarding depositors' money and regulating NBFCs which have increased their asset-size over time and gained systemic importance. On the asset quality front, gradual change in the NPA recognition norms would lead to deterioration in asset quality parameters during the transition phase. Overall the revised regulations are positive for the NBFC sector making it structurally stronger, increase transparency and improve their ability to withstand asset quality shocks in the long run.

Due to subdued economic environment, last three years have been challenging period for the NBFCs with moderation in growth and rising delinquencies resulting in higher provisioning thereby impacting profitability. However, comfortable capitalization levels and liquidity management continue to provide comfort to the credit profile of NBFCs in spite of impact on profitability. Also with the improvement in economic environment, asset quality pressures should ease which will partially offset the impact of migration towards 150 day NPA recognition norm.

For IndoStar, continued sponsors support, profitability, business diversification, client concentration and asset quality are its key rating sensitivities.

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Financial Results

			(Rs. Crore)
As on / Year ended March 31,	**FY14**	**FY15**	**FY16**
	A	**A**	**A**
Interest Income	362	467	564
Other Operational Income	31	60	77
Other Income	4	1	0
Total Income	397	528	641
Operating Expenses	34	40	56
Total Provision / Write offs	1	3	3
Depreciation	1	1	1
Interest Expenditure	192	258	289
PBT	169	226	292
Tax	57	77	101
PAT	112	149	191
Net Fixed Assets	1	1	3
Total Loan Portfolio	2,572	3,375	4,265
Investments	61	55	10
Tangible Net worth	1,127	1,276	1,531
Total borrowings	1,898	2,574	3,019
Total Assets	3,153	3,983	4,682
GNPA	19	19	10
NNPA	17	17	8
Key Ratios (%)			
Total Gearing (times)	1.68	2.02	1.97
Interest Coverage (times)	1.88	1.88	2.01
Interest Income/ Avg. Interest earning assets	14.10	13.58	13.42
Interest / Avg. Borrowed Funds	12.78	11.54	10.34
Interest Spread	1.31	2.05	3.08
Net Interest Margin	6.36	5.85	6.35
CAR	41.45	32.64	34.15
Tier I CAR	41.05	32.29	33.77
ROTA	4.19	4.18	4.41
RONW	10.44	12.40	13.61
Gross NPA Ratio (%)	0.75	0.57	0.23
Net NPA Ratio (%)	0.68	0.52	0.19
Net NPA to Net worth (%)	1.55	1.37	0.52

Details of rated facilities as on May 31, 2016

1.A. Long term bank facilities

Bank Lines	Sanctioned Amounts			Current O/S
	Term loan	CC/WCDL	Total	
ICICI Bank	100.0	-	100.0	-
IndusInd Bank	30.0	-	30.0	5.0
State Bank of Patiala	100.0	-	100.0	-
Kotak Mahindra Bank	40.0	10.0	50.0	-
Corporation Bank	30.0	-	30.0	4.2
Punjab National Bank	100.0	-	100.0	11.7
State Bk of Hyderabad	50.0	-	50.0	8.3
State Bk of Bikaner and Jaipur	50.0	-	50.0	12.5
ING Vysya Bank	50.0	-	50.0	4.2
Kotak Mahindra Bank - II	50.0	-	50.0	8.3
Axis Bank - II	100.0	-	100.0	38.5
Canara Bank	100.0	-	100.0	25.0
Federal Bank	25.0	-	25.0	6.2
Bank of Baroda	100.0	-	100.0	50.0
Bank of India	150.0	-	150.0	65.6
Development Credit Bank	25.0	-	25.0	0.0
Indian Overseas Bank	100.0	-	100.0	66.7
IndusInd Bank - II	30.0	-	30.0	12.0
Federal Bank - II	10.0	-	10.0	5.8
State Bank of Mysore - II	75.0	-	75.0	58.3
Kotak Mahindra Bank - III	100.0	-	100.0	62.5
Axis Bank - III	40.0	-	40.0	36.9
Axis Bank CC	0.0	15.0	15.0	-
ING Vysya Bank - III	100.0	-	100.0	75.0
ICICI Bank - II	100.0	-	100.0	70.0
Bank of Baroda - II (taken over from ING Vysya)	100.0	-	100.0	65.0
Corporation Bank - II	30.0	-	30.0	26.7
South Indian Bank	25.0	-	25.0	22.2
State Bank of India - II	200.0	-	200.0	177.8
IDBI Bank	50.0	-	50.0	47.2
State Bank of Patiala - II	100.0	-	100.0	100.0
State Bank of Bikaner & Jaipur - II	75.0	-	75.0	75.0
Kotak Mahindra Bank- IV	100.0	-	100.0	100.0
South Indian Bank II	25.0	-	25.0	25.0
State Bank of Mysore III	50.0	-	50.0	50.0
State Bank Of Hyderabad	100.0	-	100.0	100.0
Punjab National Bank	55.0	-	55.0	55.0
State Bank of India CC	0.0	100.0	100.0	-
Dena Bank	100.0	-	100.0	15.0
Total	**2665.0**	**125.0**	**2790.0**	**1485.6**

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1.B. Outstanding NCD- Rs.1,036.5 crore

1.C. Proposed long term debt- Rs.1,102.9 crore

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Annexure II
Brief Rationale
CARE REAFFIRMS RATINGS ASSIGNEDTO VARIOUS DEBT INSTRUMENTS OF INDOSTAR CAPITAL FINANCE LTD.

Ratings

Instrument / Facility	Amt. Rated (Rs crore)	Rating[2]	Remarks
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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.

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In case of partnership/proprietary concerns, the rating assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.