

November 29, 2019

## Hinduja Leyland Finance Limited: Rating reaffirmed

### Summary of rating action

| Instrument*            | Previous Rated Amount<br>(Rs. crore) | Current Rated Amount<br>(Rs. crore) | Rating Action                 |
|------------------------|--------------------------------------|-------------------------------------|-------------------------------|
| Subordinated debenture | 205.00                               | 205.00                              | [ICRA]AA-(Stable); Reaffirmed |
| <b>Total</b>           | <b>205.00</b>                        | <b>205.00</b>                       |                               |

\*Instrument details are provided in Annexure-1

### Rationale

The rating reaffirmation factors in the expected support from the Hinduja Group, largely via Ashok Leyland Limited (ALL; rated [ICRA]AA+(Stable)/[ICRA]A1+), given Hinduja Leyland Finance Limited's (HLF) strategic significance. The Hinduja Group companies held a 92.4% stake in HLF as of September 2019, of which ALL held 61.8%. The rating also factors in the company's presence in diverse product segments (vehicle finance, construction equipment, mortgage and wholesale lending), wide geographical footprint and established funding relationships, which provide comfort on its financial flexibility. The Stable outlook on the [ICRA]AA- rating reflects ICRA's opinion that HLF will continue to benefit from the strong operational, financial and managerial support from the Hinduja Group.

The rating is, however, constrained by HLF's moderate asset quality profile and subdued profitability with profit after tax (PAT)/average managed assets<sup>1</sup> (AMA) of 1.1% in H1 FY2020 (1.3% in FY2019). ICRA also takes note of the limited capital buffer over the regulatory requirement with Tier I of 11.1% as of March 2019 (under Ind-AS). The Tier I capital ratio improved to 12.5% as of September 2019 due to the repayment of certain Group exposures. While the rating derives comfort from the track record of capital infusion by the Hinduja Group, ICRA expects HLF to maintain an adequate buffer over the regulatory Tier I requirement, going forward, which is crucial from a rating perspective.

### Key rating drivers and their description

#### Credit strengths

**Strategic importance to Hinduja Group** – HLF is a part of the Hinduja Group, a global conglomerate with diversified interests across various business verticals. ALL, which holds a 61.8% stake in HLF (as of September 2019), is the second largest original equipment manufacturer in the medium and heavy commercial vehicle (M&HCV) segment in the country with a domestic market share of 34% in FY2019 (33% in H1 FY2020). HLF derives significant operational support from ALL as it has access to the latter's pan-India dealership network. The company also derives benefits from the support services (including business sourcing, collection and asset recovery) provided by an associate entity (HLF Services Limited). In FY2019, the Group participated in HLF's rights issue and infused capital of about Rs. 201 crore, while the total capital infused since inception is about Rs. 1,430 crore. Given the strategic significance of HLF to ALL's operations, ICRA expects the Hinduja Group to provide need-based support to the company and for its growth plans, going forward.

<sup>1</sup> Includes total assets and assigned book  
[www.icra.in](http://www.icra.in)

**Diversified product profile and wide geographical presence** – At the standalone level, HLF’s assets under management<sup>2</sup> (AUM) grew at a compounded annual growth rate (CAGR) of 40% during FY2016-FY2019, driven by robust disbursement growth across the retail (vehicle finance, construction equipment and loan against property (LAP)) and wholesale segments. The company’s AUM stood at Rs. 25,417 crore as of March 2019 and grew to Rs. 26,312 crore as of September 2019. Within the retail segment, HLF financed a range of vehicles including M&HCVs, light commercial vehicles (LCVs), two-wheelers (2Ws), three-wheelers (3Ws), cars and tractors, which constituted about 65% of the AUM while construction equipment and LAP constituted about 11% each as of March 2019. HLF has a presence in the used/refinance segment (largely in M&HCVs and cars; totalling about 7-10% of the AUM), which lends some diversity to the overall portfolio. It extends loans to NBFCs and NBFC-MFIs and invests in securitisation transactions (pass-through certificates) and debentures of entities with a minimum investment grade rating. Such investments accounted for 12% of the AUM as of March 2019. These wholesale exposures are not expected to exceed 15% of the overall AUM going forward. HLF has a wholly-owned subsidiary, Hinduja Housing Finance Limited (HHFL), which provides affordable housing finance. HHFL’s portfolio stood at Rs. 1,272 crore as of March 2019.

HLF has a wide geographical presence with semi-urban/rural areas contributing to 60% of the AUM and no single state constituting more than 20% of the AUM as of September 2019. The company has more than 1,500 branches (of which around 1,100 are in dealer locations) spread across 24 states and Union Territories. At the consolidated level, HLF is expected to grow its AUM by about 15-18% over the next three years (FY2020-2022).

## Credit challenges

**Moderate asset quality and exposure to vulnerable borrower profile** – On a standalone basis, HLF’s gross stage 3 (excluding repossessed asset) /AUM stood at 4.5% as of September 2019 (4.7% as of March 2019) compared to 5.1% as of March 2018. Gross stage 3 including repossessed remains at elevated levels; repossessed assets/AUM stood at 3.6% in September 2019 (2.5% as of March 2019). Its reported provision coverage under stage 3 remained stable at 38% as of September 2019 (37% as of March 2019). HLF’s target customer segment includes first-time buyers/users (FTBs/FTUs), who have a limited income profile, and self-employed borrowers. About 70-75% of the borrowers in the commercial vehicle segment (about 44% of the AUM as of March 2019) are FTBs/FTUs, while the majority of the 2W and 3W borrowers have limited banking history. Further, borrowers in the LAP segment, where the ticket size is typically high (above Rs. 50 lakh), comprise self-employed borrowers who are vulnerable to economic shocks.

While ICRA takes cognisance of the company’s steps to strengthen its underwriting norms (such as tighter loan-to-value (LTV) norms) and realign the incentive mechanism in line with the portfolio behaviour, the currently subdued macroeconomic conditions may continue to pose asset quality challenges in the near term. Going forward, its ability to strengthen its monitoring systems and improve recoveries will remain critical from a rating perspective.

**High credit provisions continue to impact net profitability** – On a standalone basis, HLF’s pre-provision operating profitability was 4.6% in FY2019 under Ind-AS (5.0% in FY2018 under Ind-AS) compared to the prior three-year average of 4.7% (FY2015-2017; under IGAAP) supported by gains from assignment transactions, fee income and low operating expenses (Opex/AMA of 1.2% in FY2019). Gains from the sale of the direct assignment portfolio contributed to 40% of the profit before tax in FY2019 (28% in FY2018). The company’s credit cost/AMA remained high at 2.7% in FY2019 (3.4% in FY2018) due to subdued recoveries and high write-offs. Overall, PAT/AMA remained subdued at 1.3% in FY2019 (1.2% in FY2018) and low at 1.1% in H1 FY2020. The company’s ability to control credit costs and maintain adequate margins would be critical to improve profitability going forward.

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<sup>2</sup> Includes a) loans, b) investments, c) dealer trade advances, d) loans sanctioned and pending disbursements, and e) direct assignment portfolio

**Critical to maintain adequate cushion above regulatory capital requirement while pursuing growth** – HLF’s capitalisation profile is marked by a Tier I ratio of 11.1% and total capital adequacy of 17.0% in March 2019 (12.0% and 17.0% in March 2018, respectively), under Ind-AS. The reported gearing stood at 6.4x and 6.7x on a standalone and consolidated basis, respectively, as of March 2019 (6.8x and 7.2x, respectively, as of March 2018). The capital adequacy and gearing improved to 17.6% and 5.9x as of September 2019, due to moderation in portfolio growth and repayment of certain Group exposures. Given its target of achieving a CAGR of 15-18% over the next three years, the company would require about Rs. 300-400 crore per annum to maintain an adequate buffer of 200 bps over the regulatory Tier I capital requirement. ICRA expects the company to limit its exposure to Group companies to less than 10% of the net worth (16% as of March 2019) going forward. While the capital raise through an initial public offering was deferred in FY2019, the Hinduja Group had supported HLF through a capital infusion of Rs. 201 crore via a rights issue. ICRA draws comfort from the demonstrated track record of capital support from the Hinduja Group, given HLF’s strategic significance to the Group’s overall plans.

### Liquidity position: Adequate

As of September 2019, HLF’s asset liability maturity was characterised by a modest positive cumulative gap in the less-than- one-year bucket. The company raised about Rs. 6,700 crore via term loans and Rs. 3,810 crore via sell-downs through the direct assignment route in FY2019, and about Rs. 1,570 crore via term loans in H1 FY2020. It has marginally reduced its exposure to the commercial paper (CP) programme, which stood at 4% as of September 2019. The CP limit, as a share of overall borrowings, is expected to be in the range of 4-5% in the near term. ICRA also takes comfort from the available bank sanction lines (including undrawn cash credit facilities) of about Rs. 1,350 crore as of September 2019, and expects timely support from the Hinduja Group, if required.

As of September 2019, HLF’s borrowing profile comprised bank loans (62.0%), non-convertible debentures (NCDs) and subordinated debt (10.6%), portfolio sell-downs (22.6%; direct assignment) and CPs (4.8%). The company has relationships with 24 banks and domestic financial institutions, which provide adequate comfort on financial flexibility.

### Rating sensitivities

**Positive triggers** – A sustained improvement in the asset quality, profitability and capitalisation profile from the current levels, over the medium term, would be a trigger for a change in the outlook to Positive or a rating upgrade.

**Negative triggers** – ICRA could revise the outlook to Negative or downgrade the rating if there is a further weakening in the asset quality with the reported gross stage 3/AUM exceeding 6% or the net profitability falling below 1% on a sustained basis. The rating could also be under pressure if the cushion of the Tier I capital over the regulatory norm falls below 1% on a sustained basis, or if there is a significant stake dilution by the Hinduja Group or ALL. Weakening in ALL’s credit profile would also be a negative trigger.

### Analytical approach

| Analytical Approach             | Comments   |
|---------------------------------|--|
| Applicable Rating Methodologies | <a href="#">ICRA’s Credit Rating Methodology for Non-Banking Finance Companies</a><br><a href="#">Impact of Parent or Group Support on an Issuer’s Credit Rating</a>   |
| Parent/Group Support            | The assigned rating factors in the high likelihood of support from the Hinduja Group, led by ALL, because of HLF’ strategic importance.  |
| Consolidation/Standalone        | While arriving at the rating, ICRA has considered the consolidated financials of HLF. HLF has a wholly-owned subsidiary, HHFL, and an associate entity, HLF Services Limited, in which it holds a 45.9% stake. |

## About the company

HLF is a systemically important non-deposit accepting non-banking finance company (NBFC) incorporated in 2008. The company received an NBFC licence in 2010 and commenced operations from 2011. As of September 2019, Ashok Leyland Limited (ALL) and other Hinduja Group entities held a stake of 92.4% in HLF while Everfin Holdings (private equity) held a stake of 7.0%. HLF offers financing for ALL and non-ALL vehicles apart from construction equipment, LAP and wholesale financing. The financing of ALL vehicles accounted for 37% of AUM as of June 2019. The company also invests in securitisation, assignment and debenture transactions as a part of its overall growth strategy.

On a standalone basis, the company reported a net profit of Rs. 276 crore on a total income of Rs. 2,561 crore in FY2019 compared to a net profit of Rs. 182 crore on a total income of Rs. 1,961 crore in the previous year.

## Key financial indicators (audited)

| HLF (standalone)        | FY2018 | FY2019 |
|-------------------------|--------|--------|
|                         | Ind-AS | Ind-AS |
| Total Income            | 1,961  | 2,561  |
| Profit after Tax (PAT)  | 182    | 276    |
| Net Worth               | 2,020  | 2,723  |
| Managed Portfolio (AUM) | 19,170 | 25,417 |
| Total Managed Assets    | 18,305 | 24,335 |
| PAT/AMA                 | 1.2%   | 1.3%   |
| Return on Net Worth     | 10.7%  | 11.6%  |
| Gearing                 | 6.8    | 6.4    |
| Gross Stage 3% #        | 5.1%   | 4.7%   |
| Net Stage 3% #          | 3.1%   | 3.0%   |
| Net Stage 3/Net Worth   | 28.5%  | 27.9%  |
| CRAR %                  | 17.0%  | 17.0%  |

Amount in Rs. crore; # As a proportion of standalone AUM

| HLF (consolidated)      | FY2018 | FY2019 |
|-------------------------|--------|--------|
|                         | Ind-AS | Ind-AS |
| Total Income            | 2,073  | 2,712  |
| Profit after Tax (PAT)  | 198    | 300    |
| Net Worth               | 2,039  | 2,767  |
| Managed Portfolio (AUM) | 19,910 | 26,689 |
| Total Managed Assets    | 19,181 | 25,569 |
| PAT/AMA                 | 1.3%   | 1.3%   |
| Return on Net Worth     | 11.6%  | 12.5%  |
| Gearing                 | 7.2    | 6.7    |
| Gross Stage 3%          | NA     | NA     |
| Net Stage 3%            | NA     | NA     |
| Net NPA/Net Worth       | NA     | NA     |
| CRAR %                  | NA     | NA     |

Amount in Rs. crore

**Status of non-cooperation with previous CRA: Not applicable**

**Any other information: None**

**Rating history for past three years**

|   | Instrument        | Current Rating (FY2020) |              |                    | Rating History for the Past 3 Years |                      |                   |                    |                    |
|---|-------------------|-------------------------|--------------|--------------------|-------------------------------------|----------------------|-------------------|--------------------|--------------------|
|   |                   | Type                    | Amount Rated | Amount Outstanding | Rating                              | FY2019               |                   | FY2018             | FY2017             |
|   |                   |                         |              |                    | 29-Nov-2019                         | 17-Sep-2018          | 14-Aug-2018       | 4-Oct-2017         | 8-Sep-2016         |
| 1 | Subordinated debt | Long Term               | 205.0        | 205.0              | [ICRA]AA-(Stable)                   | [ICRA]AA-(Stable)    | [ICRA]AA-(Stable) | [ICRA]A+(Positive) | [ICRA]A+(Positive) |
| 2 | Commercial paper  | Short Term              | -            | -                  | -                                   | [ICRA]A1+; withdrawn | [ICRA]A1+         | [ICRA]A1+          | -                  |

*Amount in Rs. crore*

**Complexity level of the rated instrument**

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://www.icra.in)

### Annexure-1: Instrument details

| ISIN         | Instrument Name        | Date of Issuance / Sanction | Coupon Rate | Maturity Date | Amount Rated (Rs. crore) | Current Rating and Outlook |
|--------------|------------------------|-----------------------------|-------------|---------------|--------------------------|----------------------------|
| INE146O08068 | Subordinated debenture | 30-Nov-15                   | 11.50%      | 31-May-21     | 85.00                    | [ICRA]AA- (Stable)         |
| INE146O08076 | Subordinated debenture | 15-Dec-15                   | 11.40%      | 15-Jun-21     | 35.00                    | [ICRA]AA- (Stable)         |
| INE146O08084 | Subordinated debenture | 20-Jan-16                   | 11.30%      | 21-Jul-21     | 85.00                    | [ICRA]AA- (Stable)         |

Source: HLF

### Annexure-2: List of entities considered for consolidated analysis

| Company Name                    | Ownership | Consolidation Approach |
|---------------------------------|-----------|------------------------|
| Hinduja Housing Finance Limited | 100.00%   | Full Consolidation     |
| HLF Services Limited            | 45.90%    | Equity Method          |

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