Hinduja Leyland Finance Limited

September 17, 2018

Summary of rated instruments

Instrument	Previously Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper	750.00	-	[ICRA]A1+; withdrawn
Subordinated debenture	205.00	205.00	[ICRA]AA-(Stable); outstanding
Total	**955.00**	**205.00**	

Rating action

ICRA has withdrawn the [ICRA]A1+ (pronounced ICRA A one plus) rating on the Rs.750.00 crore commercial paper programme of Hinduja Leyland Finance Limited (HLF), at the request of the company and there is no amount outstanding against the rated instrument.

ICRA has rating outstanding of [ICRA]AA- (pronounced ICRA double A minus) on the Rs.205.00 crore subordinated debenture programme of HLF. The outlook on the long-term rating is Stable.

Rationale

The rating factors in regular capital infusion by the Hinduja Group, which has supported HLF's business growth and capital profile in the past. ICRA expects continued support from the Hinduja Group, given the strategic significance of HLF's operations to the Group. The Hinduja Group companies held 92.4% stake in HLF as in June 2018, of which Ashok Leyland Limited (ALL, rated [ICRA]AA(Positive)/ [ICRA]A1+) held 61.8%. During the two years ended FY2018, HLF raised a cumulative capital of about Rs.700 crore, of which ALL's contribution was about Rs. 410 crore. The capital infusion led to an improvement in managed gearing[1] to 6.3 times as on March 31, 2018 from 6.8 times as on March 31, 2017, even as its assets under management (AUM)[2] expanded sharply by 37% during FY2018. The company has refiled a draft red herring prospectus (DRHP)[3] with Securities and Exchange Board of India in June 2018, and intends to raise about Rs.500 crore via a fresh issue by Q2/Q3 FY2019, besides an offer for sale of about three crore shares by existing investors. The initial public offering (IPO) would augment the capital base and support the company's growth plans in the near-to-medium term. The rating continues to factor in the company's experienced management team, presence across multiple product segments (vehicle finance, construction equipment, mortgage and wholesale lending) and its established funding relationships, which enhances its financial flexibility. The rating also factors in the company's diverse geographical profile with presence across 1550 locations in 24 States and Union Territories in India.

The rating is, however, constrained by HLF's moderate asset quality profile and subdued profitability with profit after tax (PAT)/average managed assets[4] (AMA) of 1.2% in FY2018 (1.5% for FY2017). Going forward, the company's ability to control delinquencies through strengthened collections and maintain an adequate margin in view of the increasing interest rate regime, would be critical to improve the risk adjusted return profile.

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[1] *Including securitisation book in the debt (excluding assignment transactions)*

[2] *Assets under management include retail advances, dealer advances and investment portfolio (debentures, pass-through certificates and funds), dealer balances and repossessed assets*

[3] *The company had previously a filed DRHP in June 2016 but the IPO plan was cancelled*

[4] *Total assets + securitized book + assigned book*

Outlook: Stable

ICRA believes that HLF will continue to benefit from the Hinduja Group support. The outlook on the long-term rating may be revised to Positive if there is a sustained improvement in the company's asset quality and earnings profile. The outlook may be revised to Negative if there is a significant deterioration in the company's asset quality, capitalisation or profitability indicators or if there is lower-than-expected support from the Hinduja Group.

Key rating drivers

Credit strengths

Strategic importance to the Hinduja Group – HLF is a part of Hinduja Group, a large global conglomerate with diversified holdings across several business verticals. ALL, which holds 61.8% stake in HLF, is the flagship company of the Group in India and the second largest M&HCV original equipment manufacturer with a domestic market share of 34% in FY2018. HLF derives significant operational support from ALL by virtue of its access to the pan-India dealership network. The company also derives benefits from the support services provided by the associate entity (HLF Services Limited). During the last two years, the Group participated in HLF's rights issue and infused capital of about Rs. 250 crore in FY2017 and Rs. 450 crore in FY2018, while the total capital infused since inception was about Rs.1,230 crore. Given the strategic significance of HLF to ALL's operations, ICRA expects Hinduja Group to provide need-based support for the company's growth, going forward.

Presence across multiple products segments – At a standalone level, HLF's retail advances constituted about 90% of the AUM as on March 31, 2018 and grew at a compounded annual growth rate (CAGR) of 40% during FY2015-FY2018 driven by healthy disbursements across segments such as vehicle finance, CE and LAP. Within the vehicle finance segment (64% of AUM), the company finances a range of vehicles including M&HCVs, LCV, two-wheelers, three-wheelers, cars and tractors; M&HCV is the key segment, where the company finances only ALL vehicles in the new vehicle category. The company is also increasingly focusing on the used vehicle segment to diversify its portfolio with this segment constituting 11% of portfolio as on March 31, 2018. The company also invests in securitisation, assignment, and debenture transactions of entities with a rating of BBB or above; such investments accounted for 6% of the AUM as on March 31, 2018. Further, the company extends finance to a few ALL dealers (dealer advances) which accounted for 4% of AUM as on March 31, 2018. HLF has a wholly-owned subsidiary, Hinduja Housing Finance Limited (HHFL), for providing affordable housing finance; HHFL's portfolio stood at Rs. 746.6 crore as on March 31, 2018.

ICRA takes comfort from Hinduja Group's strong track record in vehicle financing and its relationships with the target customer base, which would support the company's growth. At a consolidated level, HLF intends to grow by about 20-25% during FY2019.

Diversified geographical profile – HLF has a geographically diversified portfolio with 1,550 branches (of which around 1,100 are in dealer locations) spread across 24 states. Tamil Nadu, Rajasthan and Maharashtra contributed 46% to the overall portfolio as on March 31, 2018.

Adequate liquidity and funding profile – HLF's funding and liquidity profile remains comfortable. Its borrowing profile comprises bank loans (53.6% as on March 31, 2018), non-convertible debentures (NCDs) and subordinated debt (21.8%), portfolio sell-down (19.9%) and commercial paper (4.8%). The company has funding relationships with 23 banks, and has a well-matched asset liability position.

Credit challenges

Moderate asset quality profile – On a standalone basis, HLF's asset quality is characterized by gross NPAs (90+ dpd) of 3.9% as on March 31, 2018 compared to 120+ dpd of 4.2% as on March 31, 2017. ICRA notes that HLF's write-offs and loss on repossessed assets[5] stood high at 2.3% in FY2018 (0.9% in FY2017) while its provision coverage remained low at 25% as on March 31, 2018 (27% as on March 31, 2017). The asset quality in the M&HCV (comprised 36% of AUM as on March 31, 2018) improved during FY2018, while 90+ dpd in the two-wheeler, three-wheeler and car segments (together constituting 14% of portfolio as on March 31, 2018) remained at elevated levels. The company's CE and LAP segments (which together constituted 26% of AUM) are relatively less seasoned and therefore reported better asset quality. HHFL's asset quality was comfortable with 90+dpd at 0.7% as on March 31, 2018. Given the expansion plans, it would be important for the company to further strengthen its risk management systems and collections to improve its asset quality.

Subdued profitability owing to high credit costs – HLF's net margin[6] remained broadly stable at 4.9% in FY2018 (4.8% in FY2017) due to a systemic decline in the cost of funds even as the share of the low-yielding segments (new M&HCV, CE and LAP) increased during the year while its income from other services (other income/ AMA) stood at 0.5% in FY2018 (0.4% in FY2017). The company's operating expenses remained low while the credit cost/AMA remained high at 2.7% in FY2018 (1.8% in FY2017) due to write-offs and loss on repossessed assets. Consequently, PAT/AMA declined to 1.2% in FY2018 from 1.5% in FY2017. The company's ability to control credit cost and maintain adequate margins in view of the increasing interest rate regime would be critical to improve profitability, going forward.

Regular capital infusion required going forward – HLF's capitalisation profile is marked by a tier I ratio of 12.4% and total capital adequacy of 17.2% in March 2018. The company raised Rs. 700.0 crore during FY2017-FY2018 through rights issues. Given its growth target of 20-25% CAGR over the next three years, the company would require about Rs. 250-300 crore per annum to maintain managed gearing at about 7 times. The company is expected to raise capital via an IPO in Q2FY2019, which would support its growth needs over the next 1-2 years. ICRA draws comfort from the demonstrated track record of capital support from Hinduja Group, given HLF's strategic significance to the Group's overall plans.

Analytical approach: The ratings take into account the consolidated performance of HLF with its wholly-owned subsidiary, HHFL. The ratings factor in the support from Hinduja Group, considering HLF' strategic importance to the Group.

Links to applicable criteria:

ICRA Policy on Withdrawal and Suspension of Credit Rating

ICRA's Credit Rating Methodology for Non-Banking Finance Companies

About the company:

HLF is a systemically important non-deposit accepting non-banking finance company (NBFC) incorporated in 2008. The company received the NBFC licence in 2010 and commenced operations from 2011. As on June 9, 2018, Ashok Leyland Limited (ALL) and the other Hinduja Group entities held a 92.4% stake in HLF while Everstone PE held a 7.0% stake in the company. The company offers various vehicle financing products for ALL and other vehicles manufacturers. Financing of ALL vehicles accounted for 39% of the total portfolio as on March 31, 2018. The company also invests in securitisation, assignment and debenture transactions as a part of its portfolio growth strategy.

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[5] *On AUM basis*

[6] *(Interest on loans and deposits + income from pass through certificate and debenture + processing fee - Finance cost -business sourcing expense) / average managed assets*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019)					Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	September 2018	Aug 2018	FY2018 Oct 2017	FY2017 Sep 2016	FY2017 Apr 2016	FY2016 -
1	Subordinated debenture	Long Term	205.00	205.00	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	-
2	Commercial paper	Short Term	750.00	-	[ICRA]A1+; withdrawn	[ICRA]A1+	[ICRA]A1+	-	-	-

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

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)
NA	Commercial paper	NA	NA	NA	-	[ICRA]A1+; withdrawn

Source: HLF

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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