June 25, 2019

Piramal Capital & Housing Finance Limited: Long-term Rating downgraded to [ICRA]AA (Negative); short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible Debentures	6,545	6,545	[ICRA]AA (Negative); downgraded from [ICRA]AA+ (Negative)
Subordinated (Tier-II) Bonds	1,500	1,500	[ICRA]AA (Negative); downgraded from [ICRA]AA+ (Negative)
Long-term Fund-based Limits	2,875	2,875	[ICRA]AA (Negative); downgraded from [ICRA]AA+ (Negative)
Long-term Term Loans	9,947	9,947	[ICRA]AA (Negative); downgraded from [ICRA]AA+ (Negative)
Commercial Paper (CP) programme	9,000	9,000	[ICRA]A1+; reaffirmed
Total	**29,867**	**29,867**	

**Instrument details are provided in Annexure-1*

Rationale

The rating revision factors in the increasing challenges in resource mobilisation for non-banking financial companies (NBFC) and housing finance companies (HFC), including Piramal Capital & Housing Finance Limited (PCHFL), thereby impacting their financial flexibility. These challenges stem from the current operating environment and the risk averse sentiment of investors towards non-banks, particularly wholesale-oriented financiers. PCHFL has witnessed increase in its cost of borrowings, in line with the trend observed in the sector, during recent months, along with shortening of tenor for its commercial paper (CP) borrowings. The resilience of PCHFL's business model to such external shocks will depend on its ability to raise long term funding and infusion of fresh equity. The outlook on the long-term rating continues to remain negative given its predominantly wholesale book, with large sized exposures particularly in real estate and infrastructure segment. While PCHFL has hitherto demonstrated its ability to maintain adequate asset quality, a prolonged slowdown in the real estate industry, coupled with the liquidity crunch in the overall market, could have an adverse impact on the same. ICRA notes that the Piramal Group (the Group) has taken several measures to shore up long-term funding for the financial services business[1] having raised long-term funds in excess of Rs. 23,700 crore over the past nine months and significantly reduced the share of commercial paper in the overall borrowings. The Group continues to explore fresh funding avenues and is in the process of tying up sizeable amount of funds to support liquidity and future growth.

The ratings favourably factor in PCHFL's established position and track record in the real estate lending segment, the promoter group's domain experience given its presence across the industry value chain, the company's leadership team and the strong systems and processes. The ratings also consider the company's currently adequate capitalisation, with a tangible net worth of Rs. 9,274 crore as of March 31, 2019, supported by capital infusion by the promoter group and a diversified resource profile.

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[1] *Financial services business of the Group refers to PCHFL, PHL Fininvest Limited (PHL FIN, wholly owned subsidiary of Piramal Enterprises Limited or PEL) as well as the residual loan-book held by PEL*

The rating also factors in the credit and concentration risks (although reducing) associated with the wholesale funding business model. These risks are mitigated to some extent through the collateral cover maintained by the Group on such exposures, the promoter group's expertise in the real estate segment and the company's risk management and monitoring processes, which enhance its ability to proactively manage the portfolio as demonstrated in the past. ICRA has taken note of the early stage of operations in the retail lending segment, the sizeable growth targets and the limited experience of the Group in retail lending. PCHFL's strong senior management team and the Group's track record of successfully scaling up businesses and generating adequate returns also provides comfort. PCHFL's ability to maintain its capitalisation profile, while following a measured growth strategy, would remain critical from a credit perspective.

ICRA has also taken note of the high, albeit declining, share of short term sources of funding in the company's resource profile (~16% of total debt as on March 31, 2019 compared to ~36% as on September 30, 2018). However, the company's demonstrated ability to mobilise long-term debt funds provides comfort. Following the liquidity issues in the industry in H2 FY2019, the financial services business of the Group has raised ~Rs. 16,500 crore of long-term funds to enhance the maturity profile of debt and reduce reliance on short-term sources of funding to some extent.

Going forward, the company's ability to scale up its retail operations and materially improve the diversification and granularity of the asset profile, while maintaining a healthy asset quality and capitalisation profile, remains crucial from a credit perspective. Moreover, the Group's ability to continue to raise capital (equity and debt) and diversify its borrowing profile and maintain a comfortable liquidity profile would be a credit sensitive factor.

Outlook: Negative

The outlook on the long-term rating is Negative on account of the increased risk profile of its predominantly wholesale lending business, which could impact the asset quality going forward. The outlook may be revised to Stable if the company is able to further de-risk the portfolio and improve the granularity while maintaining a healthy asset quality and capitalisation profile. The ratings may be downgraded in case of slower-than-expected progress in its de-risking plans, deterioration in the asset quality of the credit book and profitability indicators or an increase in the leverage indicators.

Key rating drivers

Credit strengths

Established position in real estate lending; gradual diversification of overall loan book – As on March 31, 2019, the Group's financial services business had a consolidated loan book of Rs. 56,624 crore, up from Rs. 41,657 crore as on March 31, 2018. Of this, Rs. 38,518 crore is attributable to PCHFL while the balance is housed under PEL (standalone) and PHL FIN. As a strategic decision, the Group has gradually been diversifying its loan book, as demonstrated by its foray into new segments like housing finance, CFG and the emerging corporate lending (ECL) segment. Consequently, the proportion of the real estate segment decreased to 71% of the overall loan book as of March 31, 2019 from 87% as on March 31, 2017.

Within the real estate segment, PCHFL has been increasingly looking at construction finance (~64% of the total real estate portfolio as on March 31, 2019) against funding at the land or pre-approval stage. It has also stepped up its focus on corporate lending, housed under the CFG segment, and is looking to diversify the portfolio in terms of sector and clients in this segment. The segment accounted for 17% of the overall loan book as of March 31, 2019. Following its strategy of diversifying the asset base, PCHFL forayed into lending to small and emerging corporates (ticket size of up to Rs. 100 crore) under the ECL segment and housing finance in FY2018. The existing relationships with developers, built through the lending, equity funding and real estate advisory services of the Group, are expected to support the housing finance business. The ramp-up of the housing finance business is expected to improve the granularity of the portfolio over the medium to longer term. The company's ability to successfully scale up the business while maintaining the asset quality remains crucial. ICRA notes that while the new businesses would help diversify the portfolio, given PCHFL's large real estate exposure, the concentration and credit risks will remain over the near term.

Domain expertise and enhanced financial flexibility as a part of Piramal Group – PCHFL draws strength from the Group's technical expertise, given its experience in real estate based private equity investment, advisory services and the development space. Further, given the long-standing experience of the Group in the real estate segment, the company also leverages the large network of developers with relationships built over a period of time. The Group's demonstrated ability to incubate and scale up new ventures also provides comfort. ICRA takes into account the emergence of PCHFL as the flagship financial services vehicle for the Piramal Group, following the amalgamation of Piramal Finance Limited (PFL) and Piramal Capital Limited (PCL) with itself with effect from March 31, 2018.

Experienced management team – PCHFL has taken on board seasoned industry professionals with prior experience in retail lending to leverage their experience to ramp up the retail loan book, maintain strong underwriting practices and adopt technologies. ICRA also draws comfort from the strong and experienced management team of the Piramal Group, which has a track record of successfully scaling up businesses (other than retail) and generating adequate returns. The company has also engaged reputed and experienced external consultants for framing its credit policies and credit appraisal systems, expansion strategy and operational policies.

Adequate capitalisation supported by capital infusion from the parent – PCHFL's capitalisation has been supported by regular capital infusions from the parent. The promoter group had infused Rs. 3,500-crore equity in the company in FY2018 and Rs. 1,500 crore in PHL FIN in FY2019. These funds are a part of the ~Rs. 5,000-crore qualified institutional placement (QIP) of compulsorily convertible debentures (CCDs) in October 2017 and the rights issue of ~Rs. 2,000 crore, which was concluded in March 2018. PCHFL's tangible net worth stood at a comfortable Rs. 9,274 crore (net of goodwill on amalgamation) and the capitalisation ratios remained adequate at 29.57% (Tier I of 26.87%) as on March 31, 2019.

PCHFL also has a fairly-diversified resource profile with bank loans accounting for ~60% of its borrowings and long-term capital market instruments accounting for ~20% as on March 31, 2019. However, share of short term sources of funding, albeit declining, remains high at ~20% of total debt as on March 31, 2019 compared to ~36% as on September 30, 2018. The Group has further fund raising plans (including and not limited to sale of PEL's stake in Shriram Group; while PEL sold its 9.96% stake in Shriram Transport Finance Corporation Limited for Rs. 2,260 crore in June 2019, aggregate value of its investments in Shriram City Union Finance Limited and Shriram Capital Limited amounts to ~Rs. 5,000 crore) to further reduce its short-term borrowings. PCHFL's management has announced to put in place a liquidity policy wherein it will maintain liquidity to the tune of at least two months' repayments and net disbursements. As per the asset-liability statement as on March 31, 2019, PCHFL has no cumulative asset-liability mismatches in the near-term buckets.

Strong systems and processes – The company has strong risk management systems and adequate compliance processes, which have kept pace with the increase in the scale of operations, thereby providing comfort. It follows a multi-level evaluation process and has employed reputed independent third-party agencies for financial, technical-cum-valuation, legal and commercial due diligence. PCHFL also has a dedicated asset monitoring team for monitoring and managing the post-disbursement performance of the loans and the overall portfolio quality.

Credit challenges

Ability to raise funding while maintaining a healthy asset liability profile – Despite raising significant quantum of long-term funding over the past nine months, PCHFL still has high exposure to short-term borrowings (~16% of borrowings as on March 31, 2019). With increasing challenges in resource mobilisation stemming from the current operating environment and the risk averse sentiment of domestic investors particularly towards wholesale-oriented entities, PCHFL has witnessed increase in its cost of borrowings, in line with the trend observed in the sector, during recent months, along with shortening of tenor for its CP borrowings.

High sectoral and client concentration with predominant share of real estate lending – The loan book is concentrated towards the inherently risky real estate sector, albeit with a declining trend (71% of the overall loan book as on March 31, 2019 from 87% as on March 31, 2017). The risk is further increased by the ongoing downturn in the Indian real estate industry with a slowdown in sales across geographies. The risks in the portfolio are highlighted by the early stages of development of some of the underlying projects. Moreover, the top group exposures form a sizeable proportion of the company's overall loan book. PCHFL has, however, funded a bouquet of projects in some of these exposures, including projects with healthy sales tie-ups and finished stock, which provides comfort. Additionally, the company has been receiving sizeable prepayments from its loan portfolio over the years. In FY2019, it has received prepayments amounting to Rs. 8,602 crore (~25% of loan book as on March 31, 2018), providing comfort on the asset quality. The management has stated its intent to reduce its top 10 group exposure to ~22% over the near-term, compared to ~32% as on March 31, 2019. Nonetheless, despite the declining real estate concentration, the inherent riskiness of real estate exposures makes the portfolio highly vulnerable to any borrower or industry-specific event, which could result in a steep deterioration in the asset quality indicators.

Ability to sustain asset quality and growth – The overall asset quality, at a consolidated level, is comfortable, with reported gross non-performing assets (NPA) of 0.9% as on March 31, 2019. While the company has demonstrated its ability to maintain adequate asset quality, a prolonged slowdown in the real estate industry coupled with a liquidity crunch in the overall market could have an adverse impact on the same. Moreover, the high concentration in the loan book could result in deterioration in the asset quality in case of slippages and could consequently impact PCHFL's financial profile. The risks are, however, mitigated to some extent by the collateral cover maintained by the Group on such exposures, the promoter group's expertise in the real estate segment and the company's risk management and monitoring processes, which enhance its ability to proactively manage the portfolio.

Limited track record of the Group in retail lending – While the Group has long-standing experience and expertise in wholesale lending and real estate, its experience in the retail customer segment is limited. PCHFL marks the Group's foray into the retail segment. ICRA takes comfort from the seasoned industry professionals with prior experience in retail lending, who have been taken on board by the company.

Liquidity position

PCHFL maintained liquidity of ~Rs. 5,240 crore including undrawn bank lines (including sanctioned external commercial borrowings of Rs. 1,050 crore) as on May 31, 2019. As per the asset-liability statement as on March 31, 2019, PCHFL has debt repayments aggregating to ~Rs. 10,300 crore due in the 6-month bucket, whereas it has inflows of ~Rs. 10,200 crore in the same bucket, including current liquidity (cash balance and unutilised bank lines) of ~Rs. 5,200 crore and collections due from its loan book of ~Rs. 5,000 crore. ICRA expects PCHFL to tie up additional bank lines in the near future, while also generating liquidity through strategic asset sale. ICRA also favourably notes the company's stated intention to maintain liquidity equivalent to at least two months' debt repayments and net disbursements. ICRA expects the company to achieve the same by the end of FY2020.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA's Credit Rating Methodology for Housing Finance Companies
Parent/Group Support	Not applicable
Consolidation/Standalone	To arrive at the ratings, ICRA has considered the standalone financial profile of PCHFL, and has factored in the financial flexibility available to PCHFL by being part of the Piramal Group.

About the company

Piramal Capital & Housing Finance Limited (PCHFL; erstwhile Piramal Housing Finance Limited or PHFL) was incorporated in February 2017 as a subsidiary of Piramal Finance Limited and received its housing finance licence in September 2017. With effect from March 31, 2018, Piramal Finance Limited and Piramal Capital Limited merged with PHFL (subsequently name changed to PCHFL), which became a direct subsidiary of Piramal Enterprises Limited. Following the merger, the entire financial services business including real estate lending, housing finance, corporate finance lending and small and emerging corporate lending of the Piramal Group will be housed under PCHFL. In FY2019, PCHFL reported a net profit of Rs. 1,443 crore on a total income of Rs. 5,572 crore.

Key financial indicators - PCHFL

PCHFL (Standalone)	FY2018* Ind AS	FY2019 Ind AS
Net interest income	25.44	2,670.40
Profit before tax	2.69	2,211.91
Profit after tax	44.75	1,442.58
Portfolio (PCHFL standalone)	32,507	38,518
Total assets# (adj)	34,554	41,866
% Tier I	26.88%	26.87%
% CRAR	30.89%	29.57%
Gearing (gross)	3.29	3.48
Gearing (net of cash)	3.10	3.44
% Net profit/Average total assets	NA	3.78%
% Return on net worth	NA	16.82%
% Gross NPAs	0.37%	0.37%
% Net NPAs	0.29%	0.14%
Net NPA/Net worth	1.28%	0.57%

Amount in Rs. crore; Source: PCHFL and ICRA research; All ratios are as per ICRA calculations

**Merger of PFL with PHFL (renamed as PCHFL) effective from March 31, 2018; PHFL reported a total income of Rs. 3,739 crore and profit after tax of Rs. 983 crore during April 01, 2017 to March 30, 2018*

 # (adj) on account of goodwill

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

		Current Rating (FY2020)				Chronology of Rating History for the Past 3 Years							
						FY2020		FY2019			FY2018		
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Jun-19	May-19	Apr-19	Sep-18	Jul-18	May-18	Mar-18	Dec-17	Sep-17
1	Non-convertible Debentures	Long Term	6,545	4,845	[ICRA]AA (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)	[ICRA]AA (Positive)	-	-	-	-
2	Subordinated (Tier-II) Bonds	Long Term	1,500	1,500	[ICRA]AA (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)	[ICRA]AA (Positive)	-	-	-	-
3	Long-term Fund-based Limits	Long Term	2,875	2261	[ICRA]AA (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)	[ICRA]AA (Positive)	-	-	-	-
4	Long-term Term Loans	Long Term	9,947	9,947	[ICRA]AA (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)	[ICRA]AA (Positive)	-	-	-	-
5	Commercial Paper	Short Term	9,000	NA	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[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 No.	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE140A07146	NCDs	10-Jun-16	9.57%	08-Mar-19	300	[ICRA]AA (Negative)
INE140A07245	NCDs	21-Jul-16	9.35%	19-Jul-19 (Put: 21-Feb-18)	1,000	[ICRA]AA (Negative)
INE641O07136	NCDs	11-Aug-16	9.05%	09-Aug-19	1,500	[ICRA]AA (Negative)
INE140A07286	NCDs	12-Aug-16	9.25%	10-Aug-18	350	[ICRA]AA (Negative)
INE641O07029	NCDs	24-Nov-16	8.50%	22-Nov-19	25	[ICRA]AA (Negative)
INE641O07037	NCDs	10-Mar-17	8.95%	08-Mar-24	5	[ICRA]AA (Negative)
INE641O07052	NCDs	30-Mar-17	8.85%	25-May-20	200	[ICRA]AA (Negative)
INE641O07060	NCDs	06-Apr-17	8.85%	03-Jun-20	440	[ICRA]AA (Negative)
INE641O07078	NCDs	20-Apr-17	8.50%	19-Apr-19	50	[ICRA]AA (Negative)
INE641O07086	NCDs	04-May-17	8.75%	03-May-24	25	[ICRA]AA (Negative)
INE641O07094	NCDs	08-Jun-17	8.50%	07-Jun-19	140	[ICRA]AA (Negative)
INE641O07102	NCDs	16-Jun-17	8.50%	14-June-19 (Put: semi-annually)	50	[ICRA]AA (Negative)
INE641O07110	NCDs	14-Jul-17	8.35%	14-Jul-20	95	[ICRA]AA (Negative)
INE641O07128	NCDs	04-Aug-17	8.35%	04-Aug-20	125	[ICRA]AA (Negative)
INE641O07144	NCDs	20-Sep-17	7.96% (monthly)	19-Sep-25	167	[ICRA]AA (Negative)
INE641O07144	NCDs	20-Sep-17	7.96% (monthly)	18-Sep-26	167	[ICRA]AA (Negative)
INE641O07144	NCDs	20-Sep-17	7.96% (monthly)	20-Sep-27	166	[ICRA]AA (Negative)
INE641O07151	NCDs	25-Sep-17	8.07%	25-Sep-20	500	[ICRA]AA (Negative)
INE641O07169	NCDs	29-Sep-17	8.10%	29-Sep-20	125	[ICRA]AA (Negative)
INE641O07177	NCDs	08-Nov-17	7.96%	06-Nov-20	115	[ICRA]AA (Negative)
NA	NCDs (proposed)	-	-	-	1,000	[ICRA]AA (Negative)
INE641O08035	Subordinated Bond(Tier II)	08-Mar-17	9.55%	08-Mar-27	500	[ICRA]AA (Negative)
NA	Subordinated Bond(Tier II) (proposed)	-	-	-	1,000	[ICRA]AA (Negative)
NA	Long-term Bank Facilities – Line of Credit/Cash Credit	NA	NA	NA	2,875	[ICRA]AA (Negative)
NA	Long-term Bank Facilities – Term Loans	FY2014-FY2020	NA	FY2020-FY2024	9,947	[ICRA]AA (Negative)
NA	Commercial Paper Programme	NA	NA	7-365 days	9,000	[ICRA]A1+

Source: PCHFL

Annexure-2: List of entities considered for consolidated analysis

Not applicable

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