

Rating Rationale

December 07, 2022 | Mumbai

Edelweiss Alternative Asset Advisors Limited

'CRISIL AA- / Negative' assigned to Non Convertible Debentures

Rating Action

Rs.200 Crore Non Convertible Debentures	CRISIL AA-/Negative (Assigned)
Rs.300 Crore Long Term Principal Protected Market Linked Debentures	CRISIL PPMLD AA- r /Negative (Reaffirmed)

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1 crore = 10 million

Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has assigned its **CRISIL AA-/Negative** rating on the Non Convertible Debentures of Edelweiss Alternative Asset Advisors Limited (EAAA; part of Edelweiss group). CRISIL Ratings has also reaffirmed the rating on the existing debt instruments of the company.

The ratings continue to reflect the adequate capitalisation of the Edelweiss group, supported by multiple rounds of capital raising; its diversified business profile, with presence across lending, asset management, asset reconstruction and insurance segments; and demonstrated ability to build competitive presence in multiple lines of businesses, which should also support improvement in earnings going ahead. The group also maintains adequate liquidity on an ongoing basis.

The continuation of the 'Negative' outlook reflects the challenges that group is facing in profitability and asset quality on account of its wholesale lending book. Although profitability has seen some improvement and the group is also taking concerted efforts to arrest asset quality stress, improvement in profitability and asset quality will be a key monitorable over the medium term.

The group has raised capital of Rs 4400 crore since 2016 by part or full stake sale in some of its businesses to marquee global investors such as Caisse de depot et placement du Quebec (CDPQ), Kora Management (Kora; a US-based investment firm), Sanaka Growth SPV I Ltd (part of Sanaka Capital), Pacific Alliance Group and Arthur Gallagher. Of this, Rs 2500 crore was raised through 61% stake sale in the wealth management business in fiscals 2020 and 2021, and Rs 400 crore from full stake sale in insurance broking business in fiscal 2022. The group plans to raise further capital through stake sales in its wealth, housing finance company and the life insurance businesses over the medium term.

Networth stood at Rs 8499 crore as on September 30, 2022 as against Rs 8,537 crore as on March 31, 2022 (Rs 8621 crore as on March 31, 2021). Gearing reduced to 2.4 times as on September 30, 2022 from 2.5 times as on March 31, 2022 (3.2 times as on March 31, 2021 and 4.3 times as on March 31, 2020). The debt reduction is on account of planned reduction in the wholesale loan book and shift towards an asset-light business model.

The group has diversified business interests in financial services domain and has demonstrated its ability to build competitive positions. Over the years, the group has significantly scaled up operations of its non-lending businesses, including the asset reconstruction company (ARC), asset management which houses mutual fund business and alternate assets businesses. The insurance businesses are in growth phase. The group has adopted an asset-light approach in the credit business and is looking at co-lending partnerships in the retail lending business; it is aiming for more than 80% of disbursements in the retail book (including housing) to be through the co-lending model. The group has been able to reduce its wholesale book through recoveries and sell-downs to alternative investment funds (AIFs) and ARCs.

Also, the group maintains adequate liquidity. The on-balance sheet liquidity (excluding Nuvama wealth; including cash, liquid investments, treasury assets and other liquidable assets) and unutilised bank lines stood at around Rs 2540 crore as on October 31, 2022. The group has raised Rs 4372 crore in fiscal 2023 till date as against Rs 8,569 crore in fiscal 2022 and Rs 7,565 crore in fiscal 2021, through bank loans, securitisation, structured non-convertible debentures (NCDs) and retail bonds.

As for asset quality, while further decline has been arrested, the stressed assets continue to be elevated. Overall reported gross stage III assets in the lending business stood at 944 crore (10%), as against Rs 930 crore (7.4%) as on March 31, 2022, and Rs 1182 crore (7.7%) as on March 31, 2021. Investments in securities receipts outstanding as on September 30, 2022, stood at Rs 5,621 crore (Rs 5,446 crore as on March 31, 2022). The group has adequate provisions on gross stage III assets, as a result, net stage III assets were lower at Rs 336 crore (4.0%), Rs 214 crore (1.7%) and Rs 627 crore (4.1%) respectively.

The wholesale book has run down to Rs 4,710 crore as on September 30, 2022, from Rs 10,130 crore as on March 31, 2020. This is driven by recoveries and sell down to AIFs and ARCs; however, the group continues to retain some credit risk on part of these exposures. Therefore, the overall stressed assets remain elevated and the group's ability to recover from these assets in a timely manner will be a key monitorable.

Decline in credit book, lower margins as well as high credit costs have impacted the overall profitability of the group. Furthermore, the insurance businesses are in the growth phase and are expected to break-even in fiscal 2026. The group

reported ex-insurance profit of Rs 523 crore in fiscal 2022, as against Rs 552 crore in fiscal 2021 and an ex-insurance loss of Rs 705 crore in fiscal 2020. The net profit of the group was Rs 212 crore in fiscal 2022 as against Rs 254 crore and loss of Rs 2045 crore in fiscal 2021 and fiscal 2020. These include capital gains of Rs 306 crore and Rs 1406 crore in FY22 and FY21 respectively. For 1HFY23, the group reported ex insurance PAT of Rs 236 crore and overall PAT of Rs 112 crore.

Improvement in asset quality and profitability coupled with recoveries from wholesale exposure will be key rating monitorables.

Analytical Approach

CRISIL Ratings has combined the business and financial risk profiles of EFSL and its subsidiaries (including EAAA; excluding entities engaged in the wealth business). This is because these entities, collectively referred to as the Edelweiss group, have significant operational, financial and managerial linkages, and operate under a common brand, Edelweiss.

CRISIL Ratings has not consolidated entities in the wealth management business with the Edelweiss group because of the group's reduced shareholding, change in branding to Nuvama and fewer synergies.

Please refer Annexure - List of a Consolidated, which captures the list of entities considered and their analytical treatment of consolidation.

Key Rating Drivers & Detailed Description

Strengths:

- **Adequate capitalisation, supported by multiple capital raises**

The Edelweiss group has demonstrated its ability to raise capital from global investors across businesses, despite the tough macroeconomic environment. The group has raised Rs 4,400 crore since 2016 across lending, wealth management and asset management businesses. This has helped maintain the capital position, despite elevated credit cost and absorb the asset-side risks. The group's networth stood at Rs 8,499 crore as on September 30, 2022 (Rs 8,537 crore as on March 31, 2022).

Furthermore, gearing reduced to 2.6 times as on March 31, 2022, as against 3.2 times and 4.3 times as on March 31, 2021, and March 2020, respectively. The gearing stood at 2.4 times as on September 30, 2022. This is driven by the adoption of asset-light model, wherein the credit business operates through the co-lending model, and increased focus on fee-based businesses such as mutual funds and alternate assets.

The group's capitalisation position will remain supported by the asset-light model and increased focus on fee-based businesses. Also, it has the flexibility to raise capital through dilution of stake in group entities.

- **Diversified financial services player, with demonstrated ability to build significant competitive position**

The Edelweiss group is a diversified financial services player, with presence in four verticals i.e.; credit (wholesale and retail), insurance (life and general), asset management, and asset reconstruction. The group has attained competitive positions in the alternate asset business and asset reconstruction and is focusing on building market position in other businesses too, which should lend greater stability to earnings over a period of time.

The asset management business comprises mutual fund and alternate asset businesses. The group is a leading player in the alternate asset segment and its mutual fund assets under management (AUM) has been growing steadily. The asset management AUM has grown more than 3 times to Rs 1,32,000 crore as on September 30, 2022, as against Rs 37,100 crore as on March 31, 2019. Mutual fund AUM stood at Rs 92,000 crore and alternate asset AUM at Rs 40,000 crore as on September 30, 2022.

In the distressed assets segment, Edelweiss ARC is the largest ARC in India, with total securities receipts managed at Rs 38,000 crore as on September 30, 2022 (vis-à-vis Rs 40,200 crore as on March 31, 2022). From being largely corporate focused, the group has, in the recent past, started focusing on retail and micro, small and medium enterprises (MSME) segments. The share of retail is expected to grow, over the medium term, from 14% as on September 30, 2022.

In the lending business, while the wholesale book is under run down, the group is focusing on growth in retail through the asset-light model. The group has entered into agreements with various co-lending partners, which are large domestic and foreign banks, for both the priority and non-priority sector portfolios. Going forward, the group targets over 80% of its disbursements through the co-lending route. The key product offerings in retail credit book would be mortgage and MSME loans. Furthermore, the life and general insurance businesses are gaining scale and are expected to break even over the medium term.

Weakness:

- **Asset quality remains vulnerable**

The overall gross stage III assets in the lending business stood at Rs 944 crore (10%) as on September 30, 2022 as against Rs 930 crore (7.4%) as on March 31, 2022, and Rs 1,182 crore (7.7%) as on March 31, 2021. Of the gross stage III assets, Rs 762 crore as on September 30, 2022, 748 crore and Rs 866 crore, respectively, are from wholesale credit book. The group's investments in securities receipts outstanding as on September 30, 2022 was Rs 5,621 crore (Rs 5,446 crore as March 31, 2022).

The retail book asset quality saw an uptick as on March 31, 2021, with gross stage III assets increasing to Rs 316 crore (Rs 134 crore a year earlier), however, supported by recoveries and write offs, the retail stage III assets reduced to Rs 186 crore and Rs 182 crore as on March 31, 2022 and September 30, 2022 respectively.

The group is carrying adequate provisions on gross stage III assets, as a result, the net stage III assets is lower at Rs 336 crore (4%), Rs 214 crore (1.7%) and Rs 627 crore (4.1%) respectively.

The wholesale credit book remains vulnerable owing to exposure to the real estate segment and stressed mid-tier borrowers in structured credit. This book has substantially run down to Rs 4,710 crore as on September 30, 2022, from Rs 10,130 crore as on March 2020; supported by recoveries and sell down to AIFs and ARCs; however, the group continues to retain some credit risk on part of these exposures. Therefore, ability to recover from these assets in a timely manner will be a key monitorable. Furthermore, the loan book remains concentrated with 10 largest loans constituting ~45% of the wholesale portfolio as on September 30, 2022. Nevertheless, the group has reasonable collateral cover for its wholesale loans.

Any sharp weakening of asset quality, specifically in the wholesale lending book, will impact profitability as well as capitalisation and remains a key rating monitorable.

- **Low profitability**

Edelweiss Group's profitability has been lower compared to other large, financial sector groups. However, most of the businesses have been reporting profit from the last quarter of fiscal 2021.

The group reported ex insurance profit of Rs 523 crore in fiscal 2022 as against Rs 552 crore in fiscal 2021 and an ex-insurance loss of Rs 705 crore in fiscal 2020.

Also, the group's profitability remains subdued owing to the lower net interest margin (NIM) and substantial credit cost in lending business. The net profit of the group was Rs 212 crore in fiscal 2022 as against Rs 254 crore and loss of Rs 2,045 crore in fiscal 2021 and fiscal 2020, respectively. These include capital gains of Rs 306 crore and Rs 1,406 crore in in fiscals 2022 and 2021, respectively. Further, the insurance businesses are expected to breakeven in fiscal 2026. The group reported ex insurance profit of Rs 133 crore and consolidated net profit of Rs 67 crore in first half of fiscal 2023.

With the asset-light model, the borrowing requirement and resultant cost are likely to reduce. Also, credit cost normalised to 0.2% in fiscal 2022 from 8.2% and 10.7% in fiscals 2021 and 2020, respectively.

Asset management, asset reconstruction and credit are key to driving the group's overall profitability. The group aims at increasing the fee-paying AUM in asset management business, which would enhance the overall revenues and thereby profitability. Asset reconstruction business is expected to continue to provide a regular income stream. However, in the credit business, ability to scale-up retail lending and recover from wholesale book as well as breakeven in the insurance businesses, will be a monitorable.

Liquidity: Adequate

As a policy, the group maintains liquidity cushion of 9-10% of the balance sheet. As on October 30, 2022, the group had on-balance sheet liquidity (excluding Nuvama wealth; including cash, liquid investments, treasury assets and other liquidable assets) and unutilised bank lines of Rs 2540 crore. This is sufficient to cover the debt maturing over the next three to four months.

Outlook Negative

The 'Negative' outlook factors in challenges faced by the Edelweiss group due to stressed assets in its credit business, especially in its wholesale lending book, and their impact on profitability.

Rating Sensitivity factors

Upward factors

- Significant improvement in the group's asset quality with stage III assets ratio less than 3% on sustained basis and reduction in level of stressed assets
- Demonstration of profitability across businesses

Downward factors

- Continued pressure on profitability, with sustained losses (negative PAT excluding one-off gains)
- Deterioration in asset quality of the Edelweiss group
- Funding access challenges with limited fundraising by the group
- Lack of progress on planned scale-down of wholesale portfolio

About the Company

EAAA was incorporated in 2008 and is an investment manager. The company manages alternate assets business of the Edelweiss group and provides non-binding advisory services to certain offshore funds under the group. EAAA is 99% held by Edelweiss Securities and Investments Pvt Ltd including nominees of ESIP and its ultimate holding company is EFSL. As on September 30, 2022, the company's total assets stood at Rs 542.3 crore.

EAAA reported PAT of Rs 49 crore on total income of Rs 216 crore for fiscal 2022, against profit of Rs 15 crore on total income of Rs 144 crore for fiscal 2021. During the first half of fiscal 2023, the company reported net profit of Rs 39.8 crore on total income of Rs 127.9 crore.

About the Group

The Edelweiss group comprised 30 subsidiaries and associates as on March 31, 2022. The number of companies has come down from 74 as on March 31, 2016, because of multiple factors such as sale, windup and merger among others. The group had 293 offices (including 10 international offices in 6 locations) in around 136 cities as on March 31, 2022. Furthermore, as part of streamlining its operating structure, the group has restructured the businesses into four verticals namely credit, insurance, asset management and asset reconstruction.

The group is present across various financial services businesses, including loans to corporates and individuals, mortgage finance - loans against property and small-ticket housing loans, MSME finance, alternative and domestic asset management, and life and general insurance. In addition, the Balance sheet Management Unit (BMU) focuses on liquidity and asset-liability management.

On a consolidated basis, the group reported PAT of Rs 212 crore on a total income of Rs 4320 crore for fiscal 2022, as against Rs 254 crore on total income of Rs 7015 crore for fiscal 2021.

For the half year ended September 2022, the group reported net profit of Rs 112 crore on total income of Rs 2121 crore, compared to profit of Rs 91 crore and total income of Rs 1952 crore during corresponding period in previous fiscal.

Key Financial Indicators EFSL (consolidated)

As on/for the period ended		Sept 2022	March 2022	March 2021
Total assets	Rs crore	42521	43188	45975
Total income	Rs crore	2121	4320	7015
PAT (ex-Insurance)		236	523	552
PAT	Rs crore	112	212	254
Gross stage III assets	Rs crore	944	930	1182
Gross stage III assets	%	10.0	7.4	7.7
Net stage III assets	Rs crore	336	201	627
Net stage III assets	%	4.0	1.12	4.1
Gearing	Times	2.4	2.5	3.2
Return on assets (Ex-Ins)	%	0.6	1.2	1.1
Return on assets	%	0.5	0.5	0.4

Any other information: Not applicable

Note on complexity levels of the rated instrument:

CRISIL Ratings' complexity levels are assigned to various types of financial instruments and are included (where applicable) in the 'Annexure - Details of Instrument' in this Rating Rationale.

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Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Complexity level	Rating assigned
NA	Non-Convertible Debentures*	NA	NA	NA	200	Simple	CRISIL AA-/Negative
NA	Long-term principal-protected market-linked debentures*	NA	NA	NA	227.2	Highly complex	CRISIL PPMLD AA-r/Negative
INE528L07016	Long-term principal-protected market-linked debentures	18-May-22	NA	17-May-24	25	Highly complex	CRISIL PPMLD AA-r/Negative
INE528L07024	Long-term principal-protected market-linked debentures	16-Jun-22	NA	15-Jun-24	30	Highly complex	CRISIL PPMLD AA-r/Negative
INE528L07040	Long-term principal-protected market-linked debentures	22-Nov-22	NA	21-Aug-25	7.5	Highly complex	CRISIL PPMLD AA-r/Negative
INE528L07057	Long-term principal-protected market-linked debentures	22-Nov-22	NA	21-Jan-25	10.3	Highly complex	CRISIL PPMLD AA-r/Negative

*Yet to be issued

Annexure - List of entities consolidated

Names of Entities Consolidated	Extent of Consolidation	Rationale for Consolidation
ECL Finance Ltd	Full	Subsidiary
Edelweiss Rural & Corporate Services Ltd	Full	Subsidiary
Edelweiss Asset Reconstruction Company Ltd	Full	Subsidiary
Edelweiss Housing Finance Ltd	Full	Subsidiary
Edelweiss Retail Finance Ltd	Full	Subsidiary
Edel Finance Company Ltd	Full	Subsidiary

Edelweiss Asset Management Ltd	Full	Subsidiary
EdelGive Foundation	Full	Subsidiary
Edelweiss Tokio Life Insurance Company Ltd	Full	Subsidiary
Edelweiss General Insurance Company Ltd	Full	Subsidiary
Allium Finance Private Ltd	Full	Subsidiary
Edelcap Securities Ltd	Full	Subsidiary
Edelweiss Securities and Investment Pvt Ltd	Full	Subsidiary
ECap Equities Ltd	Full	Subsidiary
Edel Investments Ltd	Full	Subsidiary
EC Commodity Ltd	Full	Subsidiary
Aster Commodities DMCC	Full	Subsidiary
EC International Ltd	Full	Subsidiary
Edel Land Ltd	Full	Subsidiary
Edelweiss Comtrade Ltd d	Full	Subsidiary
Edelweiss Multi Strategy Fund Advisors LLP	Full	Subsidiary
Edelweiss Gallagher Insurance Brokers Ltd	Full	Subsidiary
Edelweiss Private Equity Tech Fund	Full	Subsidiary
Edelweiss Value and Growth Fund	Full	Subsidiary
India Credit Investment Fund II	Full	Subsidiary
EAAA LLC	Full	Subsidiary
Edelweiss Alternative Asset Advisors Ltd	Full	Subsidiary
Edelweiss Alternative Asset Advisors Pte. Ltd	Full	Subsidiary
Edelweiss Investment Adviser Ltd	Full	Subsidiary
Edelweiss Resolution Advisors LLP	Full	Subsidiary
EW Special Opportunities Advisors LLC	Full	Subsidiary
Edelweiss Trusteeship Company Ltd	Full	Subsidiary
Edelweiss International (Singapore) Pte. Ltd	Full	Subsidiary
Edelweiss Capital Services Ltd	Full	Subsidiary
Edelweiss Real Assets Managers Limited	Full	Subsidiary
Sekura India Management Limited	Full	Subsidiary
Edelweiss Securities Limited	Proportionate	Associate
Edelweiss Finance & Investments Limited	Proportionate	Associate
Edelweiss Broking Limited	Proportionate	Associate
Edelweiss Custodial Services Limited	Proportionate	Associate
Edelweiss Financial Services Inc	Proportionate	Associate
Edelweiss Investment Advisors Private Limited	Proportionate	Associate
Edelweiss Securities (Hong Kong) Private Limited	Proportionate	Associate
Edelweiss Financial Services (UK) Limited	Proportionate	Associate
Edelweiss Securities (IFSC) Limited	Proportionate	Associate
ESL Securities Limited	Proportionate	Associate

Annexure - Rating History for last 3 Years

Instrument	Current			2022 (History)		2021		2020		2019		Start of 2019
	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Non Convertible Debentures	LT	200.0	CRISIL AA-/Negative		--		--		--		--	--
Long Term Principal Protected Market Linked Debentures	LT	300.0	CRISIL PPMLD AA-r /Negative	22-10-22	CRISIL PPMLD AA-r /Negative		--		--		--	--
			--	04-03-22	CRISIL PPMLD AA-r /Negative		--		--		--	--
			--	31-01-22	CRISIL PPMLD AA-r /Negative		--		--		--	--

All amounts are in Rs.Cr.

Criteria Details

Links to related criteria

[Rating Criteria for Finance Companies](#)

[CRISILs Criteria for rating short term debt](#)

[Criteria for Notching up Stand Alone Ratings of Companies based on Group Support](#)

CRISILs Criteria for Consolidation

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