Research

CRISIL IER
Independent Equity Research

Enhancing investment decisions

JM Financial Ltd

Detailed Report

Explanation of CRISIL Fundamental and Valuation (CFV) matrix

The CFV Matrix (CRISIL Fundamental and Valuation Matrix) addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through Fundamental Grade) and Analysis of Returns (Valuation Grade) The fundamental grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals) The valuation grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP).

CRISIL Fundamental Grade	Assessment	CRISIL Valuation Grade	Assessment
5/5	Excellent fundamentals	5/5	Strong upside (>25% from CMP)
4/5	Superior fundamentals	4/5	Upside (10-25% from CMP)
3/5	Good fundamentals	3/5	Align (+-10% from CMP)
2/5	Moderate fundamentals	2/5	Downside (negative 10-25% from CMP)
1/5	Poor fundamentals	1/5	Strong downside (<-25% from CMP)

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JM Financial Ltd

October 03, 2017

Another stellar year; fund-based business to help sustain growth momentum

Fundamental Grade: 4/5 (Superior fundamentals) **Valuation Grade: 3/5 (CMP is aligned)**

Industry: Capital Markets and Diversified finance **Fair Value: ₹150** **CMP: ₹143**

Mirroring the growth streak of the past four years, leading financial services provider JM Financial Ltd (JM) recorded healthy performance in FY17 led by the fund-based and investment banking, wealth management & securities (IWS) businesses. Driven primarily by real estate, the fund-based business (the group's mainstay) delivered robust performance with loan book growth of 58% in FY17, while maintaining gross non-performing assets (GNPAs) at ~0.1%. The company is well positioned in the ARC business as well, with focus on asset resolution while cautiously acquiring stressed assets. In the IWS business, the company has benefitted from robust activities in the capital markets and has strengthened its competitive position as a leading M&A advisory firm by executing several marquee deals. JM's 1) proven track record of risk management in the lending business along with improving prospects in the real estate sector, 2) foray into affordable housing finance and SME lending towards the end of 2017, and 3) sustained buoyancy in the capital markets are a good augury for medium-term growth. We, thus, maintain our fundamental grade of 4/5.

Fund-based business characterised by sustainable growth and robust asset quality

The fund-based business, having posted ~30% CAGR over FY11-17, has become the key driver for the company in terms of revenue (63% share in FY17) and profits (80% PBT share). While real estate continues to dominate the loan book (~71%), corporate lending and capital market book grew 163% and 69%, respectively, in FY17. Despite high growth, the company has been able to maintain its asset quality (GNPA below 1% in the past five years) owing to prudent risk management policies, which include 1) lending to reputed developers with track record of having completed a project at least 10 years ago, 2) cash flow-backed lending, and 3) focus on tier-I metros and repeat clients. However, increasing leverage and growing pressure on yields, owing to lending to low-risk projects and intensifying competition in the space, led to ~30 bps contraction in NIM in FY17. We expect the company's FY18 book to grow ~45% thanks to exploring opportunities in new geographies and addition of new clients (6-10) every year.

IWS business driven by buoyant capital markets, though volatility is an inherent risk

The IWS business recorded a stellar year attributable to increased activities in the capital markets. The business' revenue increased 29% in FY17 driven by strong competitive position in the IB space coupled with traction in capital markets across primary and secondary segments. JM's expertise and strong corporate relationships led to it brokering key transactions during the year. We expect the segment's revenue to increase a healthy ~17% in FY18 based on sustained capital market activities.

Fair value raised to ₹150 per share

We value JM by the sum of the parts (SoTP) method and our fair value estimate as on FY18 is raised to ₹150 per share. We value the lending business at a price-to-book (P/B) multiple of 3x FY18E book value and the IWS business at a price-to-earnings (P/E) multiple of 15x FY18E earnings. At the current market price of ₹143 per share, our valuation grade is 3/5.

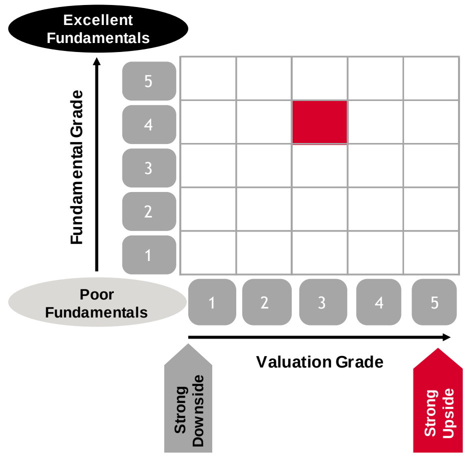
KEY FORECAST (CONSOLIDATED)

(₹ mn)	FY14	FY15	FY16	FY17	FY18E
Operating income	10,020	13,984	16,847	23,593	29,175
EBITDA	6,050	9,554	12,254	17,995	23,038
Adj PAT	2,116	3,312	4,006	4,898	6,013
Adj EPS-₹	2.8	4.2	5.1	5.9	7.5
Dividend yield	4.0	2.8	3.8	1.2	1.3
RoCE (%)	10.0	14.1	13.3	13.9	13.1
RoE (%)	9.8	13.9	14.7	15.1	16.9
PE (x)	9.0	11.3	7.5	21.1	16.6
P/BV (x)	0.8	1.2	0.8	2.2	2.0

Source: Company, CRISIL Research estimates

CMP: Current market price

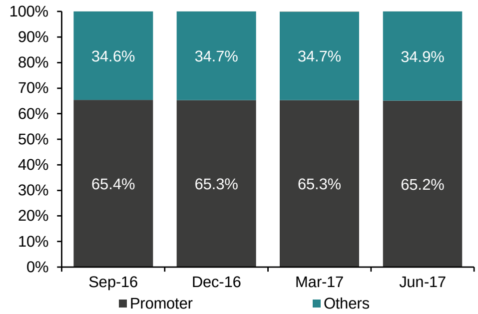
CFV MATRIX



KEY STOCK STATISTICS

Nifty/Sensex	9860/31497
NSE ticker	JMFINANCIL/JMFINAN
Face Value (₹ per share)	1
Shares outstanding (mn)	796.8
Market cap (₹ mn)/(US$ mn)	113,942/1738
Enterprise value (₹ mn)/(US$ mn)	217,948/3325
52-week range (₹)(H/L)	131/47
Beta	1.3
Free float (%)	34.9%
Avg daily volumes (30-days)	2,170,043
Avg daily value (30-days) (₹ mn)	308.1

SHAREHOLDING PATTERN



PERFORMANCE VIS-À-VIS MARKET

	Returns			
	1-m	3-m	6-m	12-m
JM Financial	1%	23%	59%	97%
NIFTY 500	-1%	3%	8%	15%

For detailed initiating coverage report please visit: www.crisil.com

CRISIL Independent Equity Research reports are also available on Bloomberg (CRI <go>) and Thomson Reuters.

Table 1: JM Financial - business environment

Parameters	Fund-based activities	Fee-based activities		
	Lending and ARC^	IWS	Asset management	Others
Segment offerings	• Real estate lending • Capital market lending: loan against securities, margin funding, IPO financing, broker funding, ESOP funding • Corporate lending - promoter funding, bridge loans, corporate loans, structured loans, acquisition financing • Asset reconstruction company (ARC) - acquisition of NPAs, their resolution and recovery	• Investment banking services – M&A advisory, corporate finance advisory, PE syndication, equity and debt markets oriented services • Equity research, sales & trading • Wealth management • Financial products distribution	• Mutual funds – equity and debt	• Alternative asset management – real estate fund, private equity fund
Revenue contribution* FY17 FY18E	63% 66%	25% 24%	3% 3%	9% 7%
Revenue growth (FY18E)	28%	17%	7%	0%
Key competitors	• Lending business - Edelweiss Capital, IIFL, HDFC, Indiabulls Housing Finance, Piramal Enterprises; Altico Capital • ARC - Edelweiss ARC, ARCIL	• Investment banking - Citi, Edelweiss, HSBC, ICICI securities, Axis bank, among others • Securities business - IIFL, Motilal Oswal, Edelweiss capital	• HDFC AMC, ICICI Prudential AMC, LIC MF, Invesco MF, Sundaram MF, DHFL Pramerica	NA

* Total revenue, including inter-segment sales, is used to calculate revenue contribution of segments

^ ARC figures in the statement of profit and loss are consolidated on a line by line basis from October 1, 2016. The ARC was an “associate” of JM Financial until September 30, 2016.

Source: Company, CRISIL Research

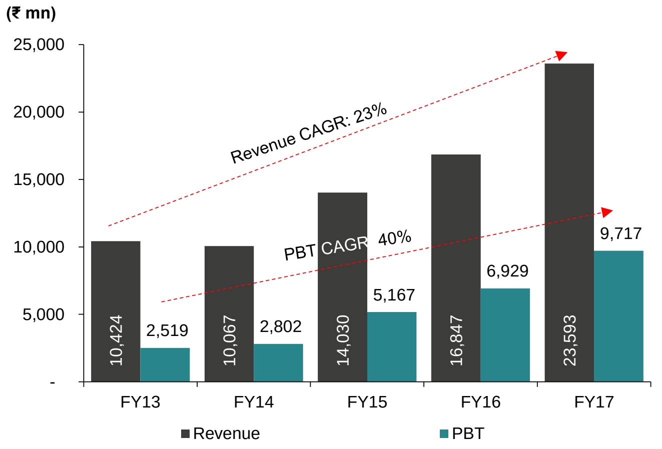
Grading Rationale

Successive years of robust performance driven by fund-based and IWS businesses

As estimated in our previous detailed report (dated June 26, 2016) JM marked another year of solid performance, registering consolidated revenue and adjusted PAT growth of 40% and 22% on-year, respectively, in FY17. The fund-based and IWS businesses are key revenue and profit drivers, accounting for ~88% of revenue and ~95% of PBT in FY17. The company's loan book grew a robust 58% to ~₹114 bn in FY17 from ₹72 bn in FY16 driven by traction across segments. The year also saw the IB and securities business post revenue and PBT growth of 29% and 81%, respectively, driven by buoyant capital markets (primary as well as secondary) and M&A activities.

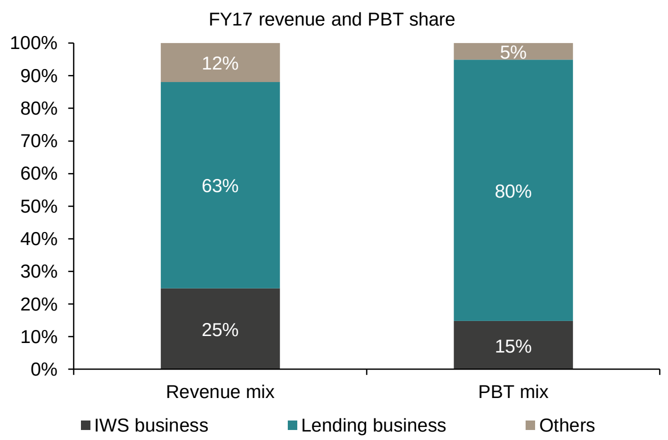
40% revenue growth in FY17 driven by fund-based and IWS segments

Figure 1: Revenue growth of 40% in FY17...



Source: Company, CRISIL Research

Figure 2:...driven by fund-based and IWS businesses



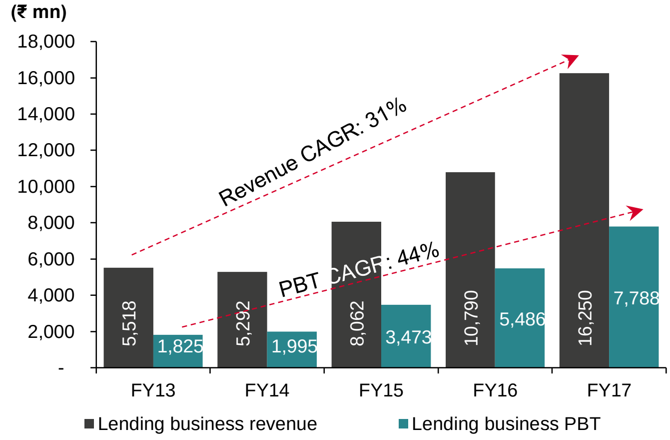
Source: Company, CRISIL Research

Fund-based business: The engine for sustainable growth

The company's fund-based business witnessed robust revenue growth of 51% and PBT growth of 42% in FY17. The lending book increased 58% on-year driven by growth across real estate, capital market and corporate lending. Real estate book, accounting for ~72% of the total loan book as of FY17, grew 45% on-year, while the capital market and corporate lending book grew 69% and 163%, respectively.

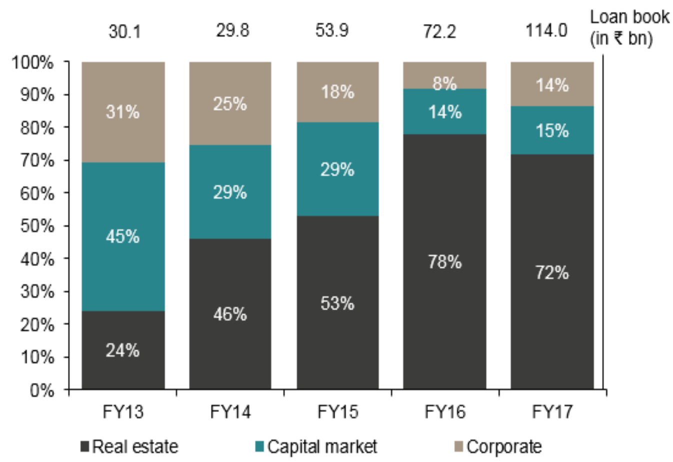
The fund-based business contributed ~63% of revenue and ~80% of PBT in FY17

Figure 3: Fund-based business posted robust revenue and PBT growth



Source: Company, CRISIL Research

Figure 4: Real estate lending book accounted for 72% in FY17



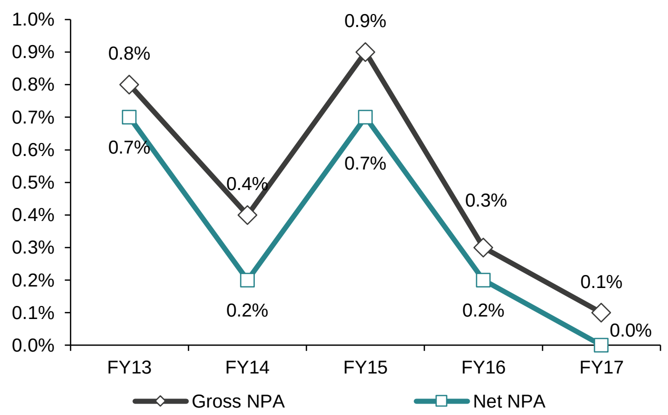
Source: Company, CRISIL Research

Asset quality maintained, but NIM and yield contracted

Historically, the asset quality of the lending book has remained healthy (GNPAs <1% over the past five years) and improved further in the past seven quarters (GNPAs <0.5% since Q3FY16), driven mainly by the company's policy of lending to developers having completed a project at least 10 years ago. The company has been able to maintain robust asset quality based on its risk assessment expertise and experience in real estate and capital markets, focus on lending to reputed builders in tier-I markets as well as practice of cash flow-backed lending. However, as the lending book has grown rapidly while keeping its asset quality intact, yields and NIM contracted slightly owing to competitive pressures in the low-risk lending space. We expect the spreads to contract by 40-50 bps in FY18.

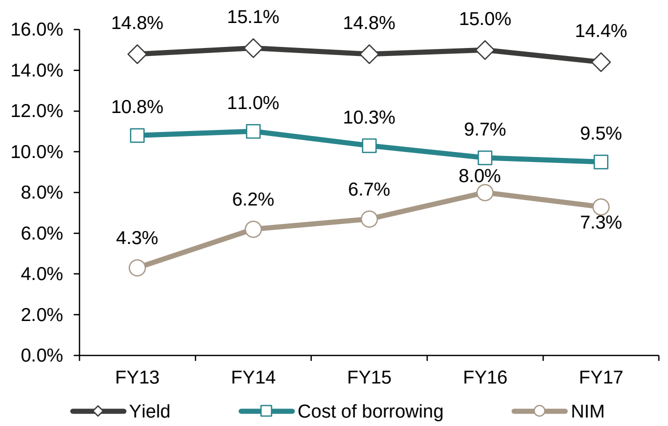
~0.1% GNPA reflects robust risk management practices

Figure 5: JM's expertise and disciplined approach helped asset quality improve further, but…



Source: Company, CRISIL Research

Figure 6: …yield and NIM receded from high levels of FY16

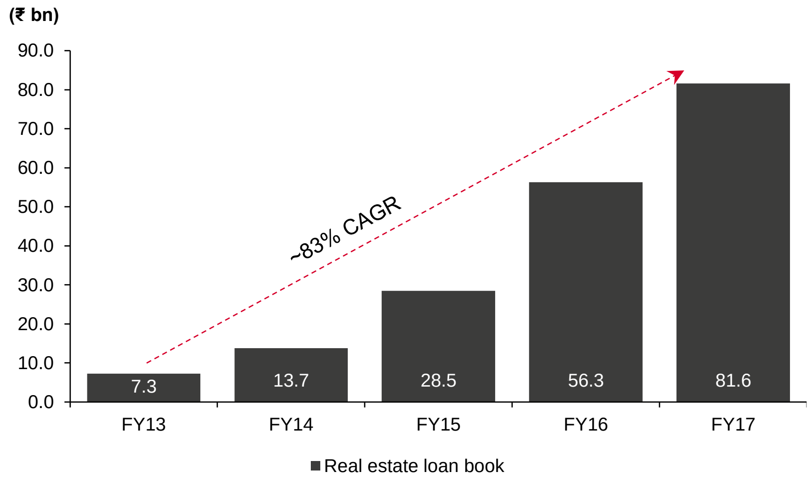


Source: Company, CRISIL Research

Growth in real estate lending book driven by existing relationships and …

JMs real estate lending business accounts for ~72% of the total loan book. It grew at more than 80% CAGR over FY13-17. The company currently lends to about 59 clients with significant focus on repeat business. It majorly provides real estate project financing backed by cash flows and ~80% of the book is against residential projects. Some of its prominent clients are Kalpataru, RMZ, Embassy, Kanakia, Peninsula, Adarsh Developers, Goel Ganga, Rajesh Lifespace and Lodha Group. The company primarily lends to reputed and established developers; most have an experience of more than 25 years in the industry.

Figure 7: Real estate loan book grew at a phenomenal rate



Source: Company, CRISIL Research

Real estate lending book accounts for ~72% of the loan book

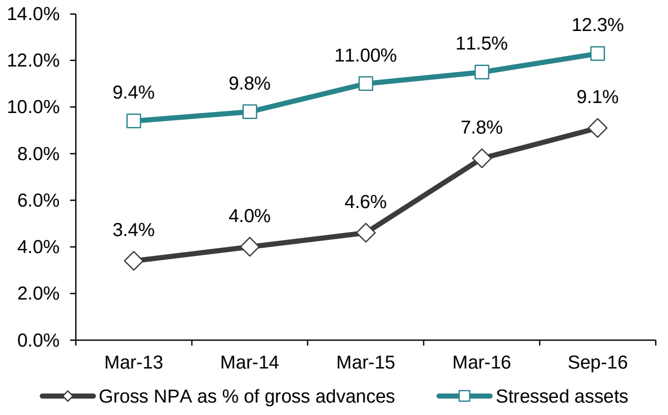
…foray into newer geographies amid…

Most of JM's real estate lending is linked to projects in tier-I markets of Mumbai, Pune and Bengaluru. The company entered Hyderabad in FY17 and Kolkata this year. It also plans to enter NCR in FY18. It plans to initially cater to existing clients in these markets. The company has been adding six to seven new clients every year; which it plans to ramp up to 10. In FY17, majority of disbursements were in Mumbai, Pune, Bengaluru and Chennai.

…opportunity arising from slowing of bank credit towards real estate

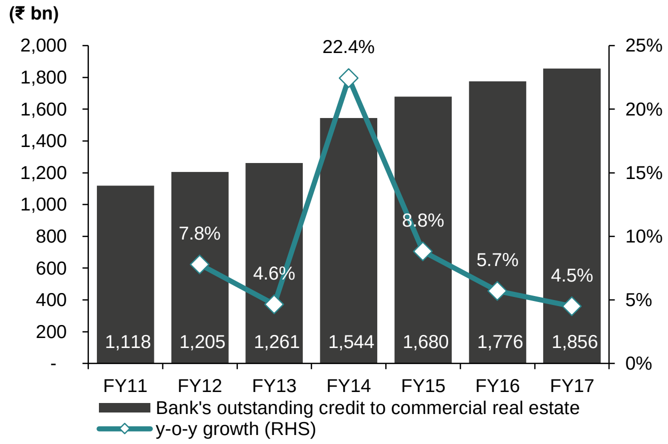
Banks have become moderately averse to lending to real estate developers because of high risk perception and bank's struggling with significant stressed assets. This has led to non-banking financial companies (NBFCs) gaining market share as they increasingly cater to the sector.

Figure 8: Banks grapple with asset quality issues…



Source: Reserve Bank of India (RBI), CRISIL Research

Figure 9: …as lending to real estate slows down



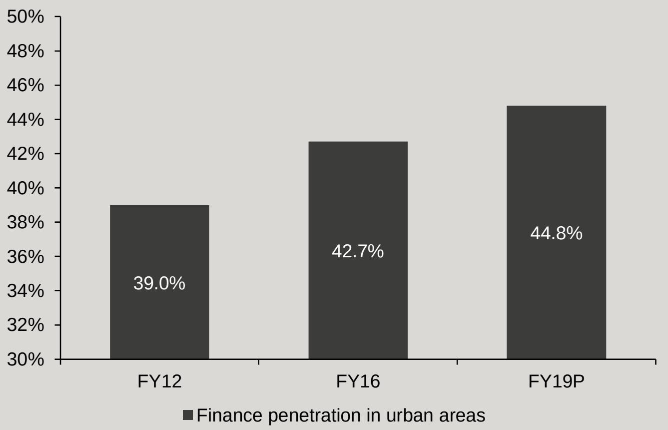
Source: RBI, CRISIL Research

Tailwinds for recovery in real estate sector in a challenging environment

RERA and lower cost of borrowing are near-term triggers for the sector

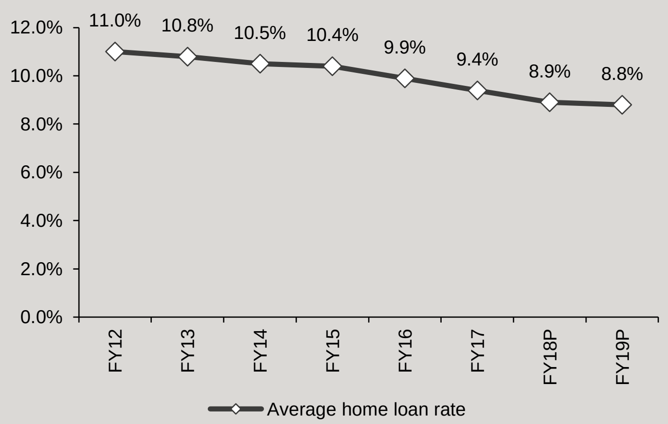
Despite a challenging environment, we expect the key near-term triggers such as Real Estate Regulatory Authority (RERA) Act and lower cost of financing along with increasing finance penetration to facilitate recovery of the real estate sector. RERA is expected to create confidence among buyers by bringing in transparency, while lower cost of borrowing and increasing penetration of housing finance are expected to boost demand.

Figure a: Increase in finance penetration in urban areas to induce housing demand…



Source: Industry, CRISIL Research

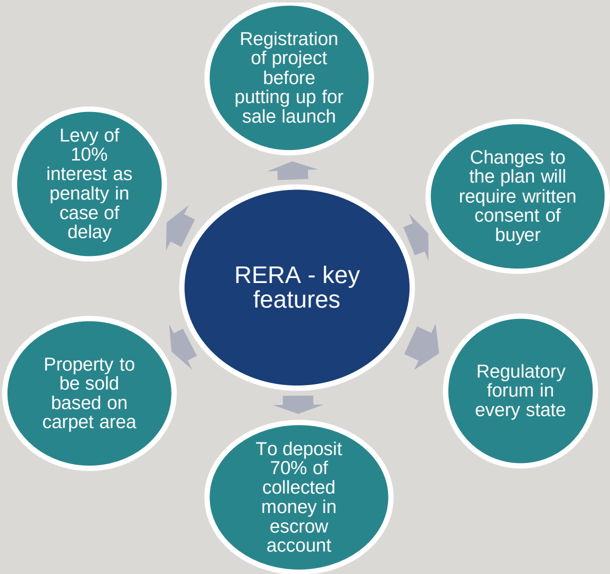
Figure b: …along with decrease in cost of borrowing



Source: Industry, CRISIL Research

We expect RERA to be positive for the organised developers as supply declines and demand recovery is facilitated by increased transparency. This is expected to benefit organised players to gain market share.

Figure c: RERA to bring in greater transparency and increase buyer confidence

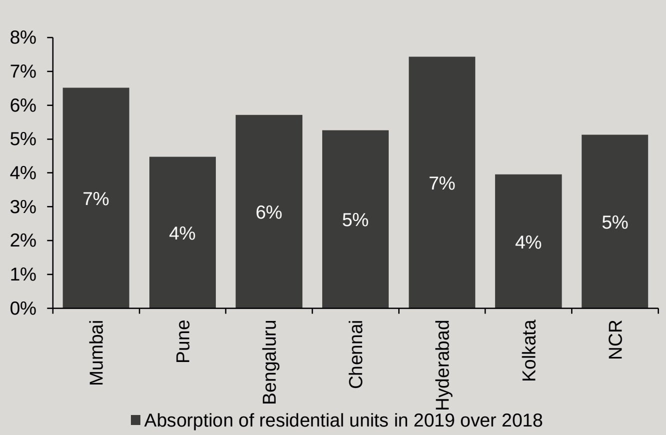


Source: Industry, CRISIL Research

Absorption expected to pick up in 2019

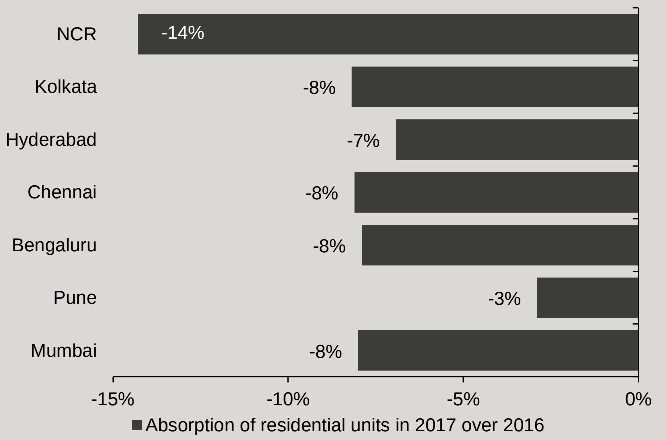
We expect gradual recovery in absorption from 2019 onwards as 2018 is still expected to witness sluggish growth in demand. However, we expect absorption in the residential segment to decline in 2017. The residential segment remained under pressure in 2016 in the key metros of Mumbai, Pune, Bengaluru, Chennai, Kolkata and NCR where absorption declined 4-5%. Only Hyderabad reported an increase in absorption. The near-term outlook for the real estate industry is muted. Pile-up in inventory and stagnant new launches have strained cash flows of most developers, especially smaller ones, in the past couple of years.

Figure d: Absorption expected to pick up in 2019…



Source: CRISIL Research

Figure e: …after decline in 2017 in most key markets



Source: CRISIL Research

Prudent risk management policies ensured healthy asset quality and successful exits in real estate book

The company has maintained healthy asset quality in real estate, despite riskier nature of the asset class. Management has indicated that there have been nil NPAs in its real estate loan book since inception. The company has been able to maintain healthy asset quality owing to-

- Fixed limit (as a percentage of book) on lending to a particular developer
- Focus on lending to reputed and quality developers who have completed project at least 10 years ago
- ~88% (Q1FY18) of the book is backed by cash flows
- ~84% (Q1FY18) of the lending book against residential projects (non-investor markets) and mostly in tier-I cities

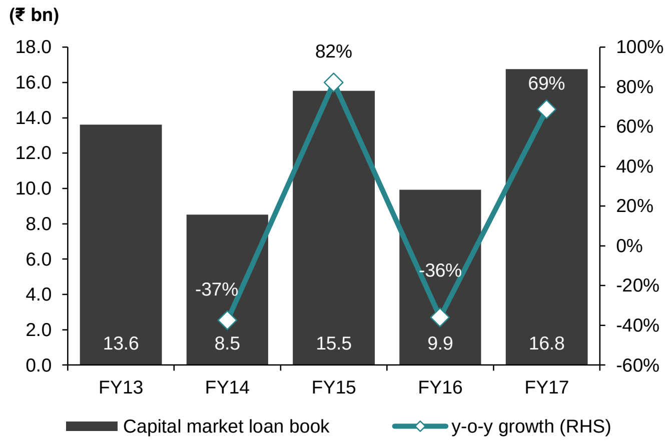
Secured lending to reputed and experienced developers in tier-I cities helps maintain asset quality

The company's loan book is seasoned as evident from its experience of six-seven years in the real estate lending space. Loan tenor of two-four years enabled it to log several successful exits in the past three-four years.

Notable growth in capital markets and corporate lending, albeit on a small base

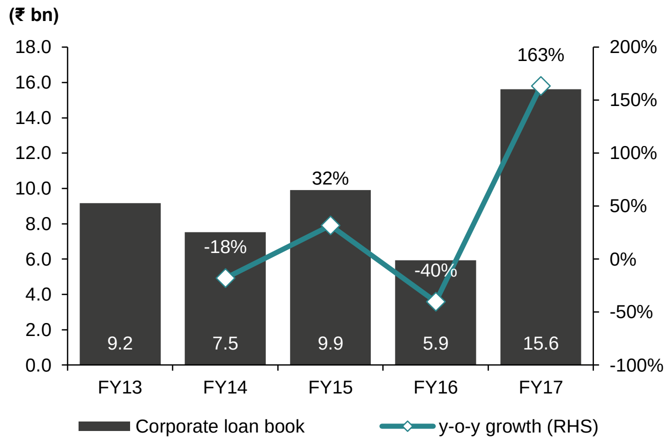
The company's capital market and corporate lending books, albeit on a small base, grew 69% and 163%, respectively, in FY17 on account of buoyant capital markets. The capital market loan book is more volatile as it witnessed de-growth in FY14 and FY16 on account of sluggish market activity. We expect the capital market loan book to grow in FY18 driven by robust capital markets and M&A activities.

Figure 10: Capital market loan book grew ~69% in FY17…



Source: Company, CRISIL Research

Figure 11: …while corporate loan book grew 163%

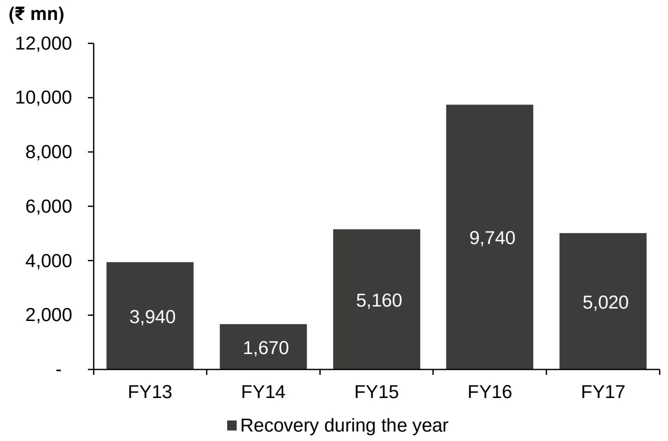


Source: Company, CRISIL Research

ARC business: Focus on resolution and cautious acquisition of appropriate NPAs

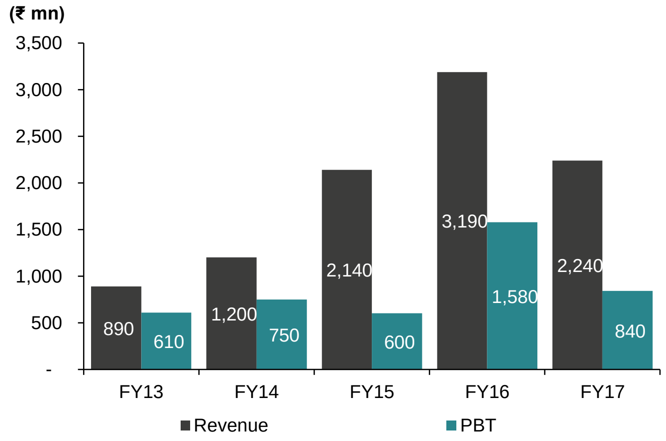
JM's ARC business' AUM increased 21% in FY17 as the company continued to pick up stressed assets. One major account it bought during the year was outstanding loan of ₹8.7 bn given to Unitech Group by HDFC. The ARC business is lumpy as profits are higher in the years of resolution. Therefore, owing to comparatively fewer resolutions, revenue declined ~30% in FY17 over FY16 (PBT down 47%). The company has recovered ~₹2,600 crore until FY17 with focus on restructuring and resolution. Going forward, we expect it to acquire assets cautiously, based on its expertise, and turn more focus towards resolution.

Figure 12: Focus on recovery with cumulative ~₹26 bn recovered until FY17



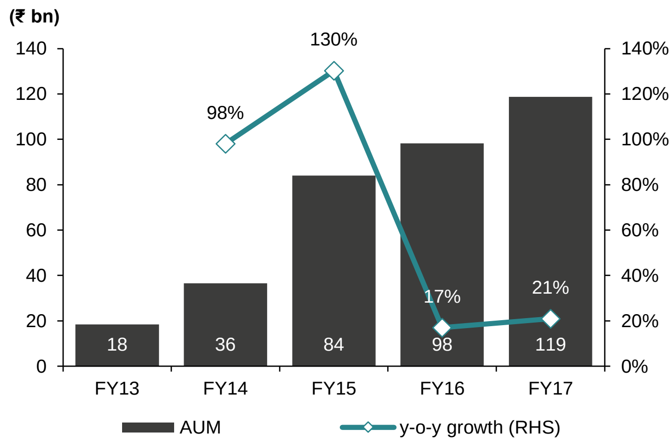
Source: Company, CRISIL Research

Figure 13: ARC revenue declined in FY17 as business is lumpy



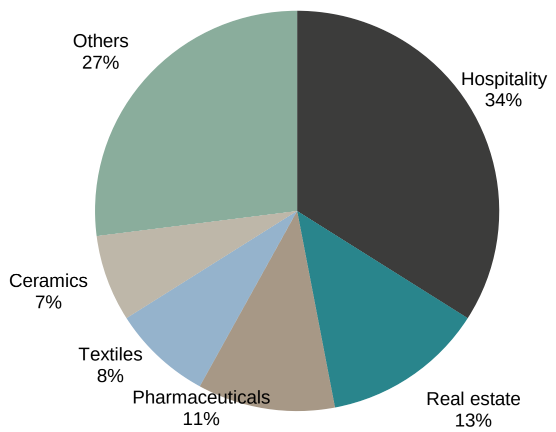
Source: Company, CRISIL Research

Figure 14: ARC AUM grew ~21% in FY17 as company continued to cautiously acquire assets



Source: Company, CRISIL Research

Figure 15: Hospitality accounted for 34% of outstanding AUM in FY17

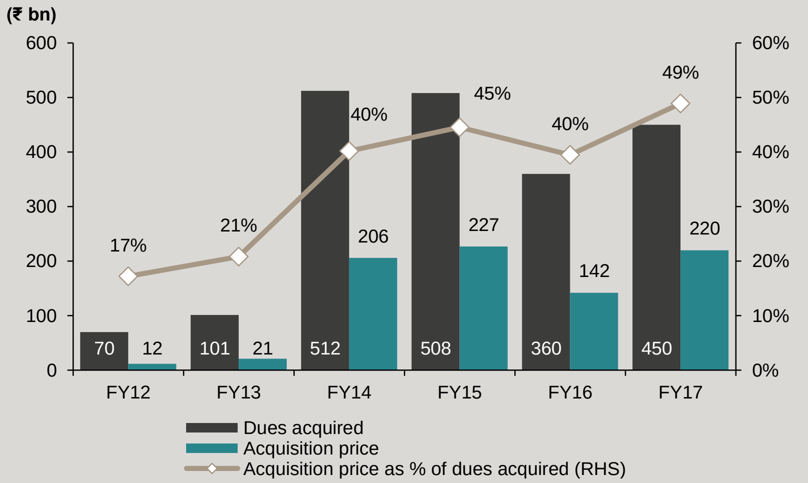


Source: Company, CRISIL Research

ARC business recovered in FY17 after slump in FY16

After a slump in FY16, sale of NPAs picked up in FY17 as banks attempted to clean their balance sheets. In August 2014, the RBI issued new guidelines, increasing the cash component to 15% from 5% and management fee linked to the net asset value (NAV) of security receipts. This led to ~30% fall in dues acquired in FY16.

Figure f: 25% on-year increase in dues acquired in FY17



Source: Company

Key regulatory changes aimed at faster resolution of NPAs:

- The RBI has notified a minimum net owned fund (NOF) of ₹1,000 mn for ARCs - expected to discourage smaller and non-serious players in the ARC space and increase focus of ARCs towards recovery and resolution
- Allowed up to 100% foreign direct investment (FDI) in ARCs through the automatic route - can potentially enable greater infusion of capital in the sector, thus allowing ARCs to acquire more NPAs
- Amendment (2016) in SARFAESI Act which allows non-institutional investors to invest in Security Receipts (SR) - aimed at increasing investment in the space
- In September 2016, the RBI's guideline on sale of stressed assets specified stricter provisioning norms for banks subscribing to SRs on assets that earlier formed part of their own NPAs – expected to increase resolution of assets since ARCs would need to find serious investors for SRs which, in turn, would lead to higher focus on resolution

Along with the aforementioned key changes, the introduction of Insolvency and Bankruptcy Code (2016) facilitates faster resolution in liquidation and insolvency proceedings. This is expected to result in quicker receipt of resolution proceeds after the purchase of assets compared to six-seven years normally taken earlier.

IWS business: Performance driven by competitive position and buoyant capital markets; inherent risk of volatility

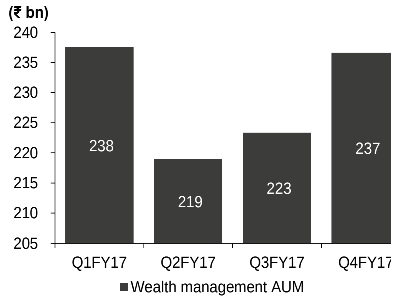
The IWS business is one of the oldest in the JM group. The segment recorded revenue growth of 29% on-year and PBT growth of 81% in FY17. The company was involved in several deals in FY17 and featured among top investment bankers in terms of the number and value of deals executed. It has been able to garner steady business based on strong relationships with Indian corporates and large business houses. The company was involved in some marquee deals in the M&A, private equity and capital markets space.

The securities business, comprising institutional equities and equity brokerage, also gained in FY17 driven by robust capital markets. The company's research covered around 169 companies and the business clocked average daily turnover at ₹2,987 crore in FY17 in cash and F&O segments compared to ₹2,137 crore in FY16.

The wealth management business' AUM, which caters to HNIs as well as corporates, tallied at ~₹23,664 crore in FY17 and had a team of 67 wealth advisors. The Independent Financial Distribution (IFD) division has a network of over 8,200 active distributors who distribute various financial products such as mutual funds, fixed deposits, IPOs and bonds. It is one of the leading companies in the fixed income and company fixed deposit distribution business.

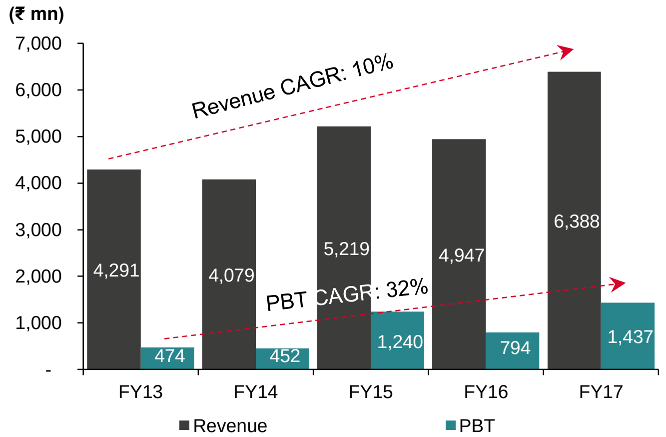
Healthy growth in IWS business driven by relatively heightened activities in capital markets

Assets under wealth management at a healthy ₹237 bn in FY17



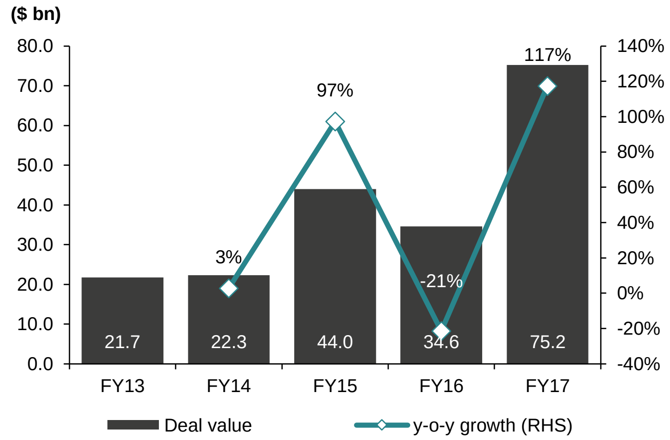
Source: Company, CRISIL Research

Figure 16: IWS recorded ~30% revenue growth…



Source: Company, CRISIL Research

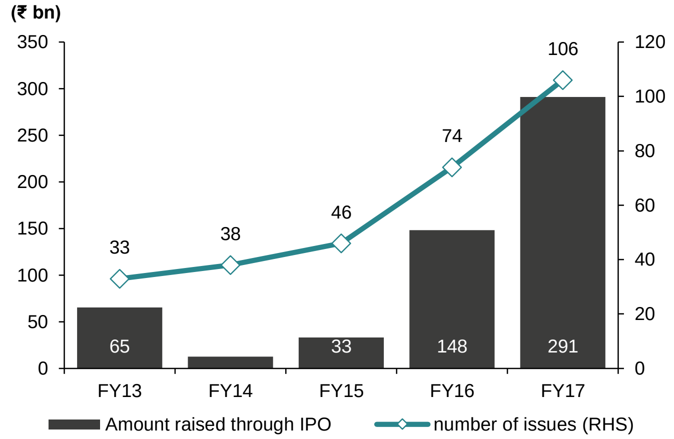
Figure 17: ...as M&A activities witnessed a remarkable year



Source: Industry, CRISIL Research

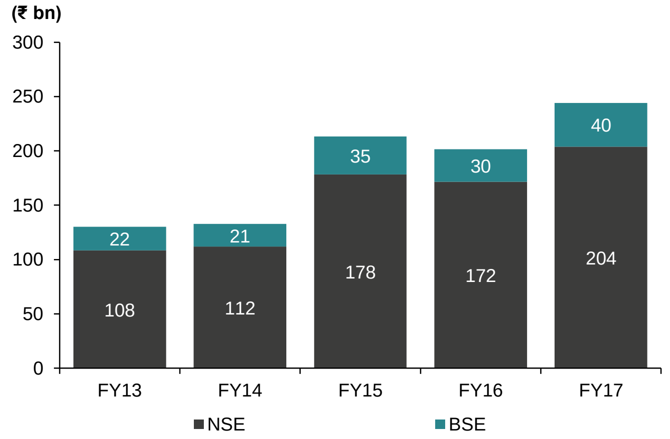
M&A activities more than doubled to $75 bn in FY17 from $35 bn in FY16 with domestic transactions contributing around 55% of the deal value. Private equity or PE deals recorded highest flows in 2015, and 2016 was the second highest year of PE investments after 2015. Deals worth $15.2 bn were inked in 2016 compared to $17.3 bn in 2015. Even the primary markets saw significant number of equity issues as the amount raised through IPO almost doubled in FY16. The secondary markets also witnessed increase in average daily turnover in NSE and BSE. We expect the capital market activities to remain strong in FY18 as well driven by strong cash inflows, especially in mutual funds, predominantly from domestic investors. However, inherent volatility is a risk and a key monitorable.

Figure 18: Primary markets recorded a notable year



Source: SEBI, NSE, BSE, CRISIL Research

Figure 19: Secondary markets saw average daily turnover rise

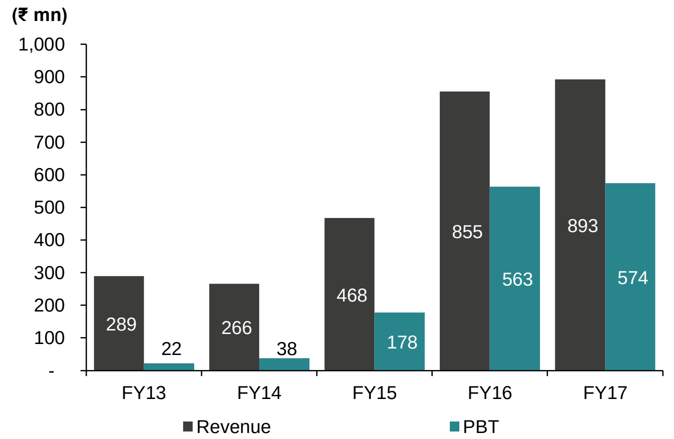


Source: SEBI, NSE, BSE, CRISIL Research

Asset management: Maintained high share of equity assets

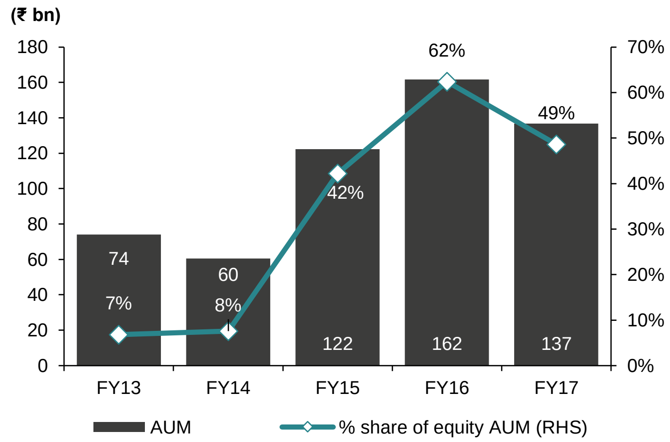
The AMC business (3% revenue share) saw tepid revenue and PBT growth of ~4% and ~2%, respectively. AUM de-grew 15% y-o-y in FY17 even as industry-wide AUM grew 35%, leading to a decline in market share from 1.2% in FY16 to 0.75% in FY17. Share of the high yielding equity assets declined to 49% in FY17 from 62% in FY16 even as it remained higher than 35% for the industry.

Figure 20: Tepid revenue growth of 4%...



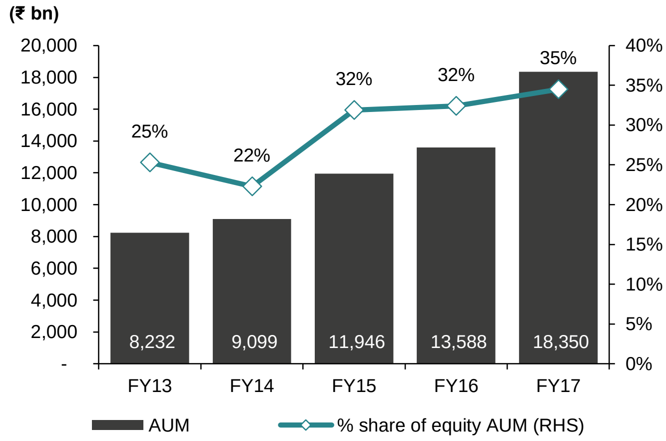
Source: Company, CRISIL Research

Figure 21: … as MF AUM de-grew 15%



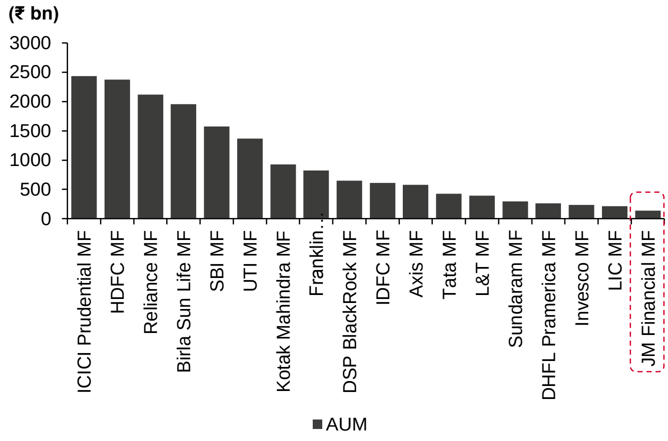
Source: Company, CRISIL Research

Figure 22: MF industry's AUM grew 35%



Source: Company, CRISIL Research, AMFI

Figure 23: JM continues to be a small player



Source: Company, CRISIL Research, AMFI

Alternate asset management: New PE fund in capital raising mode

The company's PE Fund II has received Sebi registration as Cat II – AIF and is in the process of raising capital. Similar to the first fund, which is now in exit mode, Fund II is an India-focused private equity fund, with the aim of providing growth capital to dynamic and fast growing mid-market companies.

JM Financial Property Fund is a real estate-focused private equity fund that has invested in residential, hospitality and mixed use development assets at individual projects or at the holding level in development companies. The fund continues to focus on exploring exit opportunities for its outstanding portfolio investments. During the year, the fund's domestic scheme received consent from investors to extend the tenure by two years.

Affordable housing finance and SME lending: Exploring new opportunities

JM is also exploring new opportunities in affordable housing and SME lending. It has floated a housing finance company (HFC) and has made an application to National Housing Bank (NHB) for a licence. In the affordable housing space, the company will lend to homebuyers whereas it will offer several products in the SME lending space. Though we believe there are significant opportunities in these segments, they entail a different set of expertise. We have not factored any meaningful revenue from these new businesses in our projections for FY18 as the company is expected to enter these businesses by the end of 2017.

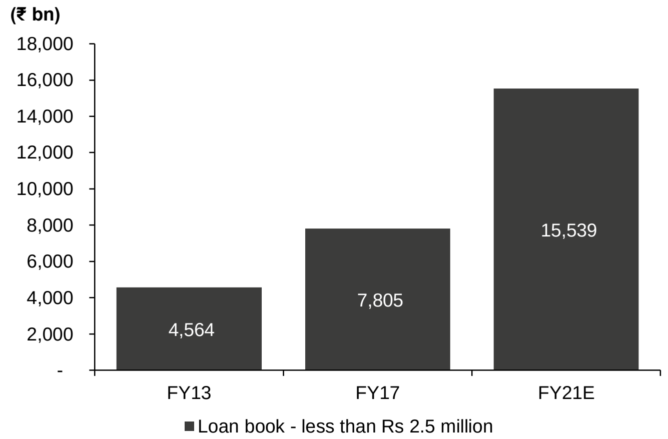
Focus on affordable housing finance and SME lending for growth opportunities

The company has started building the team for operating in the affordable housing segment by hiring people for senior to mid-level managerial positions. Its geographic target market will be outskirts of cities. The average ticket size is expected to be ₹1.5 mn to ₹2 mn. It plans to grow affordable housing book to ₹25 bn to ₹30 bn in the next three to four years.

Healthy growth expected in low ticket housing finance industry

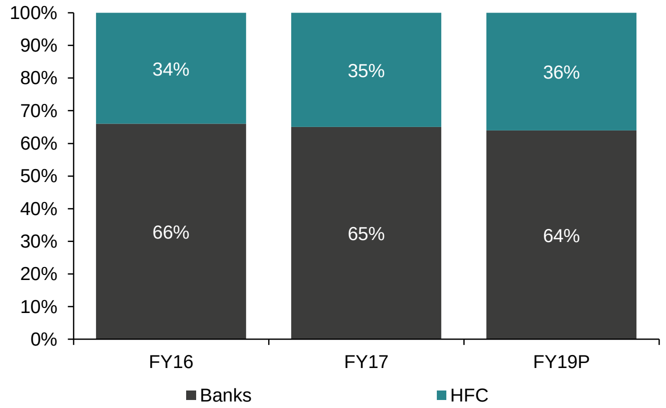
We expect low ticket housing loan book to grow at a healthy pace of 18-20% CAGR from FY17 to FY21. The recent push by the government to provide 'housing for all' by 2022 and various steps taken to implement the same are expected to boost sales of affordable, low-cost housing units and, consequently, financing for the same. Higher government support for the affordable housing segment (in terms of interest rate subsidy) as well as a low interest rate scenario will push up overall housing loan demand in the next two-three years.

Figure 24: Healthy growth in low ticket housing finance…



Source: RBI, NHB, CRISIL Research

Figure 25: …with HFC to increase market share



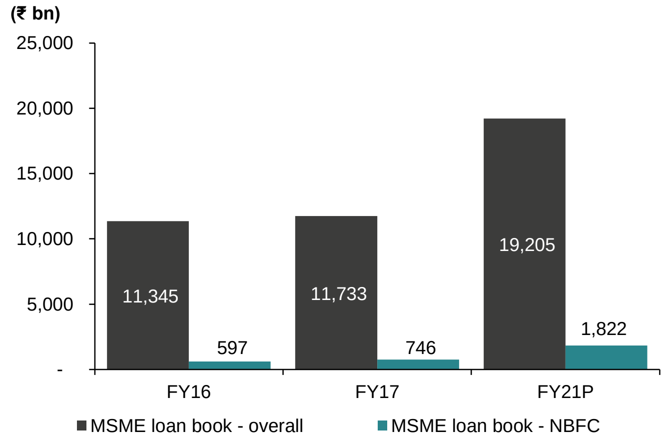
Source: RBI, NHB, CRISIL Research

The company is looking at entering SME lending via several products. The new areas are more retail-oriented and of smaller ticket size than its current expertise areas of real estate and corporate lending. Based on inputs from research teams, the company will focus on lending to SMEs in select sectors and regions. It plans to grow the SME lending book to ₹25 bn to ₹30 bn over the next three to four years.

NBFC to sustain impressive growth of 22-25% in SME lending

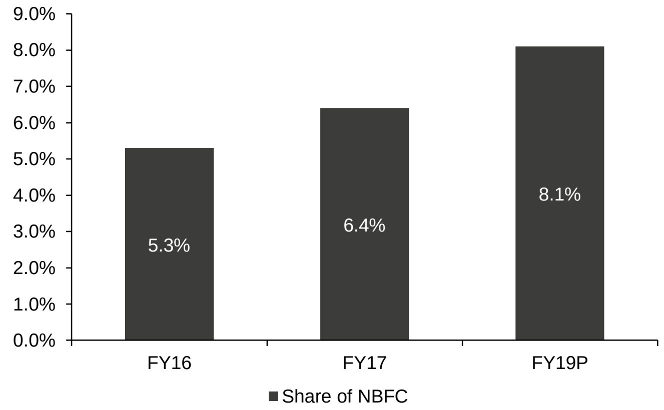
Lending to the SME sector is expected to increase 12-14% annually over the next four years. We expect the share of NBFCs to increase from the current 6.4% as growth is expected to be higher in non-metros. Growth will also be supported by better customer reach, greater focus, faster documentation process and higher risk appetite. NBFCs are gaining on money lenders as well as banks by offering higher loan amount, better service, faster turnaround time and lesser documentation.

Figure 26: NBFCs to sustain impressive growth…



Source: RBI, NHB, CRISIL Research

Figure 27: …leading to increase in market share



Source: RBI, NHB, CRISIL Research

Rationalising corporate structure for capital and operational efficiency

The company is looking to reorganise its business -- it plans to offer similar services under one vertical to drive operational efficiencies. For instance, financing needs of wealth customers shall now be served by its subsidiary (JM Financial Capital Ltd) of the IWS vertical (fig: 31 for details on corporate structure). This will enable it serve multiple needs of the client under one business vertical more efficiently.

Key Risks

Linkage with capital market

JM's IWS and capital market lending prospects are correlated with capital markets. Capital markets are inherently volatile, driven by economic and political factors as well as public sentiment. Any potential instability would also have a significant impact on the company's earnings potential.

Regulatory uncertainty

As in the case of banks, the RBI's regulations have deeply affected the business models of NBFCs and ARCs. Any adverse regulation or tightening of norms can further impact profitability and viability of the company's NBFC and ARC businesses.

Declining yields owing to competition in real estate lending

The real estate lending business constitutes ~72% of the company's lending portfolio. Real estate lending is primarily linked to the economic condition in tier-I cities such as Mumbai, Bengaluru, Chennai and Pune. Downturn in these cities could significantly impact growth and yields, and our estimates unfavourably.

Q1FY18 result update

Revenue and earnings in line with expectations

JM's Q1FY18 revenue increased 49% y-o-y (declined 2% q-o-q) to ₹7.1 bn driven by the fund-based business – which grew 53% y-o-y and 5% q-o-q. Adjusted PAT increased 49% y-o-y, but declined 15% q-o-q, to ₹1,282 mn. The lending book (60% revenue share) grew 65% y-o-y and 7% q-o-q to ₹121.1 bn.

Lending business continues to witness growth momentum

The real estate lending book remained flat compared to the last quarter and increased 42% over Q1FY17. The capital market book grew 24% q-o-q and 88% y-o-y to ₹20.7 bn, whereas the corporate lending book grew 25% q-o-q and 247% y-o-y to ₹19.6 bn. NIM was 7.1% (down 30 bps q-o-q). GNPA declined from 0.1% in Q4FY17 to 0.0%. Even as capital adequacy ratio declined to 22.7% from 27.6% in Q1FY17, there is still sufficient headroom for growth over the next two years.

Revenue traction in IWS segment remains healthy

The IWS business' revenue increased 44% y-o-y (down 21% q-o-q) to ₹1,768 mn. The company has a healthy pipeline of M&A and capital market-related deals. JM's equity market share on the NSE increased from 2.99% last quarter to 3.4%.

Q1FY18 Results Summary (Consolidated)

₹ mn	Q1FY18	Q4FY17	Q1FY17	q-o-q (%)	y-o-y (%)*
Income from operations	**7,091**	**7,250**	**4,765**	**-2%**	**49%**
Employee Cost	979	799	662	23%	48%
Other expenses	733	988	582	-26%	26%
EBITDA	**5,379**	**5,463**	**3,521**	**-2%**	**53%**
EBITDA margin	**76%**	**75%**	**74%**	**49 bps**	**197 bps**
Depreciation	64	63	53	1%	20%
EBIT	**5,315**	**5,401**	**3,468**	**-2%**	**53%**
Interest and finance charges	2,617	2,138	1,757	22%	49%
Operating PBT	**2,698**	**3,262**	**1,711**	**-17%**	**58%**
PBT	**2,698**	**3,262**	**1,711**	**-17%**	**58%**
Tax	917	1,160	588	-21%	56%
PAT	**1,781**	**2,103**	**1,123**	**-15%**	**59%**
Minority Interest	501	596	310	-16%	62%
Profit of Associates	2	2	48	12%	-95%
Adj PAT	**1,282**	**1,508**	**861**	**-15%**	**49%**
Adj PAT margin	**18%**	**21%**	**18%**	**-273 bps**	**1 bps**
No of equity shares (mn)	796.8	794.5	789.6	NM	NM
Adj EPS (₹)	**1.6**	**1.9**	**1.1**	**-15%**	**48%**

*Note: ARC figures in the statement of profit and loss are consolidated on line by line basis from October 1, 2016. The ARC was an "associate" of JM Financial until September 30, 2016. Therefore, Q1FY18 figures are not strictly comparable with Q1FY17 numbers.

Source: Company, CRISIL Research

Q1FY18 segment-wise revenue summary (consolidated)

₹ mn	Q1FY18	Q4FY17	Q1FY17	q-o-q (%)	y-o-y (%)
IWS business	1,768	2,228	1,232	-21%	44%
Fund-based activities	5,020	4,782	3,276	5%	53%
Alternative asset management	81	10	18	742%	341%
Asset management	221	259	182	-15%	22%
Others	1,233	744	299	66%	313%
Total segment revenue	**8,324**	**8,022**	**5,006**	**4%**	**66%**
Less: Inter-segment revenue	1,233	773	241	60%	411%
Income from operations	**7,091**	**7,250**	**4,765**	**22%**	**52%**

Source: Company, CRISIL Research

Q1FY18 segment-wise profit before tax summary (consolidated)

₹ mn	Q1FY18	Q4FY17	Q1FY17	q-o-q (%)	y-o-y (%)
IWS business	363	691	205	-47%	77%
Fund-based activities	2,190	2,395	1,429	-9%	53%
Alternative asset management	(4)	(19)	(16)	-76%	-72%
Asset management	138	187	97	-26%	42%
Others	12	8	(4)	47%	-387%
Total	**2,698**	**3,262**	**1,711**	**-17%**	**58%**

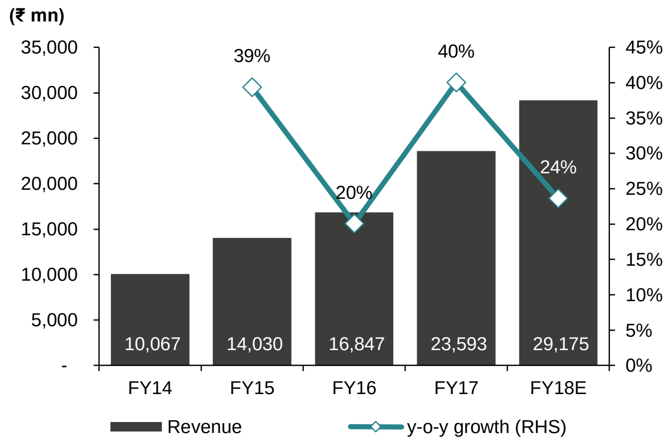
Source: Company, CRISIL Research

Financial Outlook

Expect revenue growth momentum to sustain

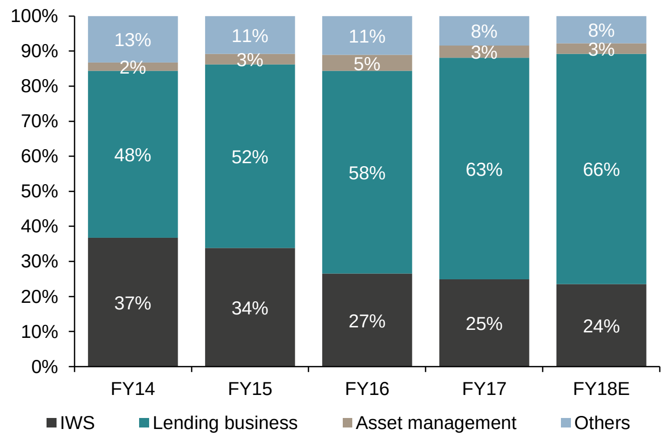
We expect revenue to increase 24% in FY18, driven by the lending business, aided by healthy capitalisation and capital market activity. We expect the IWS business to grow 17%, driven by JM's strong competitive positioning. The lending business' revenue rose 51% y-o-y in FY17, driven by healthy growth in real estate lending. We expect the lending business' revenue to increase ~28% y-o-y in FY18.

Figure 28: Revenue to record ~24% growth in FY18



Source: Company, CRISIL Research

Figure 29: Lending business to dominate revenue share

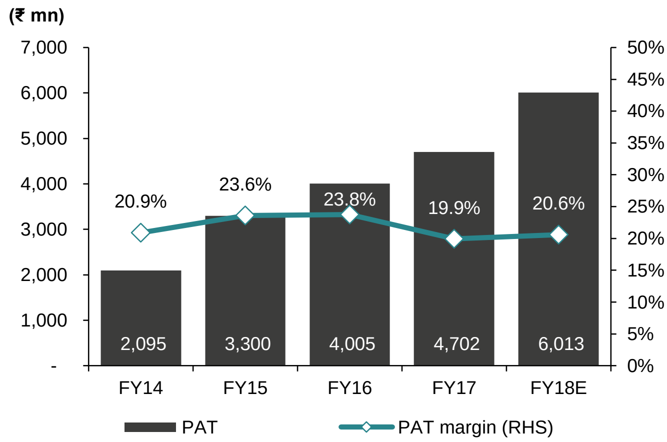


Source: Company, CRISIL Research

RoE to increase moderately

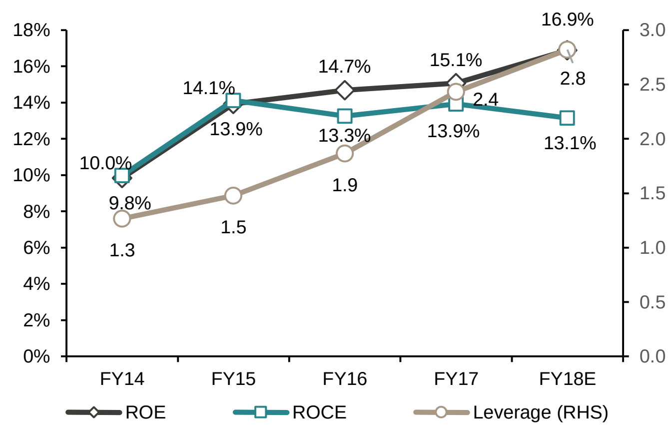
Though RoE is expected to increase to 16.9% in FY18 from 15.1% in FY17, we believe there is room for improvement considering the relatively low leverage of 2.4x. JM's leverage is lower than that of India Infoline and Edelweiss Financial owing to relatively low leverage in its lending business. With potential increase in leverage and upside in earnings from the ARC business, we expect RoE to improve.

Figure 30: Profitability expected to remain steady



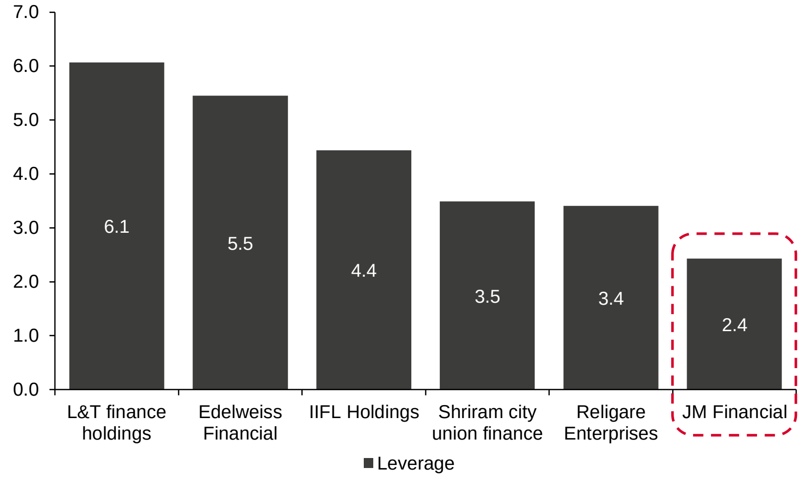
Source: Company, CRISIL Research

Figure 31: RoE expected to increase in FY18



Source: Company, CRISIL Research

Figure 32: JM's leverage is significantly lower than that of peers



Source: Company, CRISIL Research

Management Overview

CRISIL's fundamental grading methodology includes a broad assessment of management quality, apart from other key factors such as industry and business prospects, and financial performance.

Highly qualified and experienced management team

Led by Mr Nimesh Kampani, Group Chairman, JM Financial operates through subsidiaries, joint ventures and associate companies. Mr Kampani has over four decades of experience in the Indian capital markets and has played a pivotal role in not only making JM Financial an integrated player, but also fostered development of the financial market. Mr Vishal Kampani, Mr Nimesh Kampani's son, is the Managing Director of JM Financial - the group's flagship listed company. He joined the group in 1997 and has worked in different departments in various capacities.

Each business is headed by experienced professionals with in-depth understanding of financial markets and their relevant business segments.

- Manish Sheth is the Group Chief Financial Officer. He has over a decade of experience in financial consultancy, management consultancy, taxation, accounting and company laws. Mr Gagan Kothari is the CFO of JM Financial Credit Solutions Ltd – the primary real estate lending NBFC of the group.
- Dipti Neelakantan is the Group Chief Operating Officer with about four decades of experience in IB.

Decision making is decentralised

An experienced second line of management supports different businesses. Several members of the senior management, who lead various business segments and manage day-to-day operations, have been associated with the company for almost a decade. Our previous interaction with business heads (of ARC and NBFC) indicates that business units enjoy sufficient autonomy in decision making, which enhances operational flexibility.

Shown intent to grow the business

The top management's intent for diversified growth is apparent from the exploring of new opportunities. Management is looking at entering the affordable housing and SME lending space based on available opportunities. Also, as mentioned, JM's PE Fund II has received Sebi registration as Cat II – AIF, and is in the process of raising capital. The company has hired Mr Darius Pandole to head the PE division. He was partner at PE fund New Silk Route. Even in the existing real estate lending business, management is exploring entering new geographies.

Corporate Governance

CRISIL's fundamental grading methodology includes a broad assessment of corporate governance and management quality, apart from other key factors such as industry and business prospects, and financial performance. In this context, CRISIL Research analyses the shareholding structure, board composition, typical board processes, disclosure standards and related-party transactions. Any qualifications by regulators or auditors also serve as useful inputs while assessing a company's corporate governance.

Corporate governance at JM Financial is good. It is supported by a strong board and efficient board practices. It adheres to all regulatory requirements.

A well-structured board with diverse knowledge

JM has an eight-member board, six of whom are independent, which meets Clause 49 of Sebi's listing guidelines. The board is chaired by Nimesh Kampani. The independent directors are well qualified and bring significant diverse domain knowledge in consulting, corporate restructuring, project finance and strategic advisory. EA Kshirsagar is the independent director and chairman of the audit committee. He has three decades of experience in consulting and also serves on the board of other public listed companies in India. Independent directors have good understanding of the business. The company has all the necessary committees – audit, remuneration and investor grievance – in place. Board meetings are held at regular intervals. JM's board processes and systems seem satisfactory.

Consistent dividend payment policy

- **Consistent payment of dividends –** Over the past few years, the company has maintained a healthy dividend payout. The average dividend payout ratio over FY13-17 was around 32%.
- **Appointment of new auditors –** M/s. Khimji Kunverji & Co. has been the auditor for over a decade. The company has appointed Deloitte Haskins & Sells LLP as statutory auditor for a period of five years in its AGM held in July 2017.

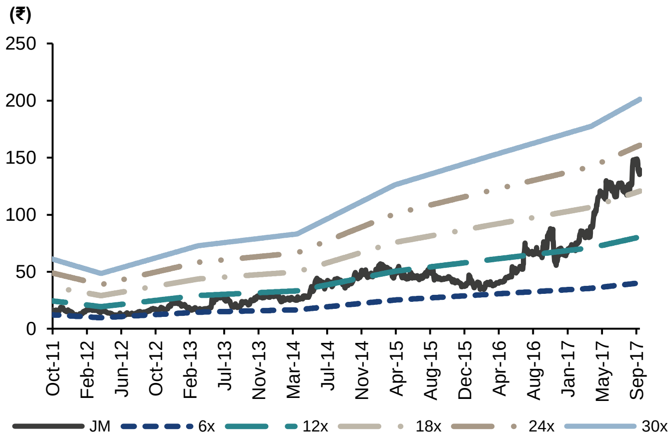
Valuation Grade: 3/5

We continue to use the SoTP method to value JM. The IWS business is valued at a P/E multiple of 15x FY18E EPS. The P/B multiple on FY18E book value for the fund-based business is raised to 3x. The ARC business is valued separately at a P/B multiple of 2.4x FY18E book value per share. We have raised our FY18 fair value estimate to ₹150 per share. At the current market price of ₹143 per share, our valuation grade is **3/5.**

SoTP Valuation

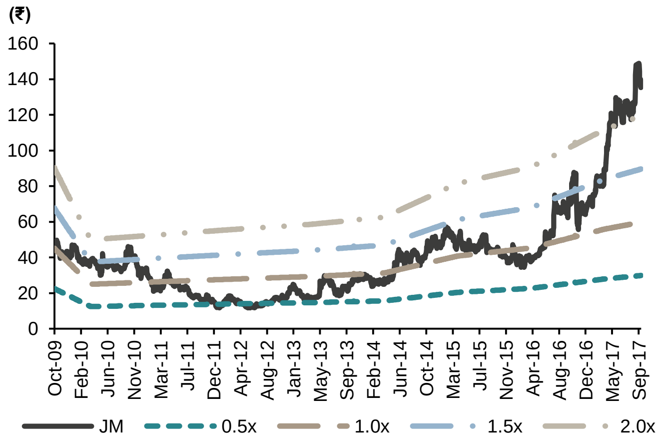
	Methodology	Multiple used	Parameter	Parameter value adjusted for JM's stake	Valuation (per share)
Lending business	P/B	3x	FY18E net worth	₹24,681 mn	₹92
IWS business	P/E	15x	FY18E earnings	₹1,380 mn	₹26
ARC business	P/B	2.4x	FY18E net worth	₹3,326 mn	₹10
AMC business	% of AUM	4%	FY18E AUM	₹85,523 mn	₹5
Alternative asset management and Excess cash and investments					₹17
Fair value as on FY18					₹ 150

TTM P/E band



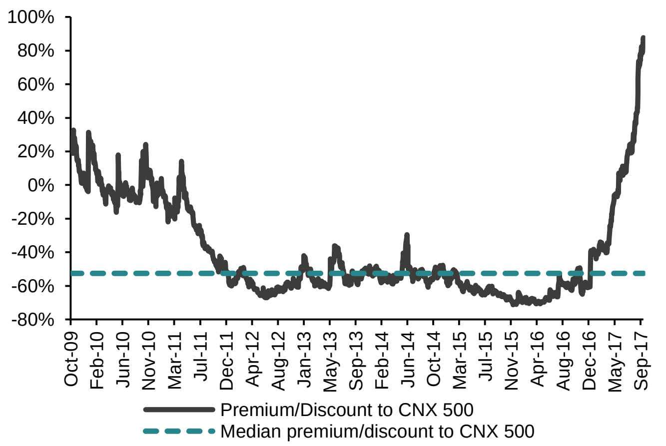
Source: NSE, CRISIL Research

TTM P/B band



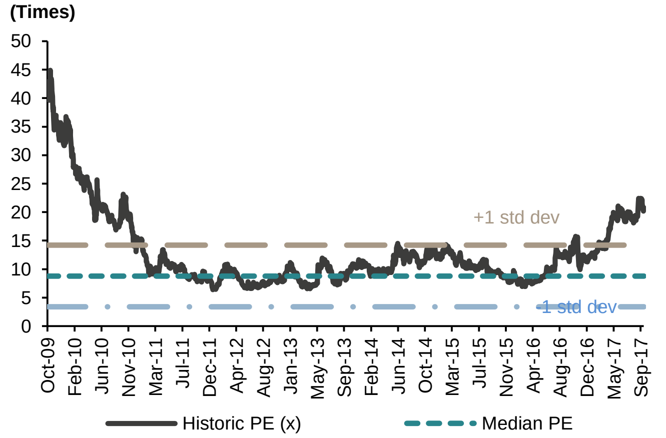
Source: NSE, CRISIL Research

P/E – premium / discount to CNX 500



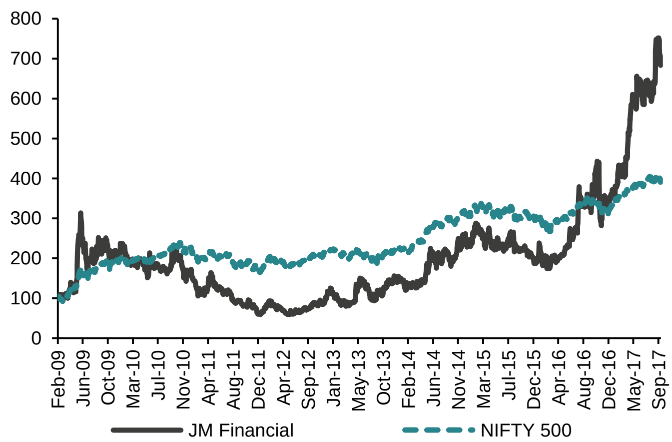
Source: NSE, CRISIL Research

P/E movement



Source: NSE, CRISIL Research

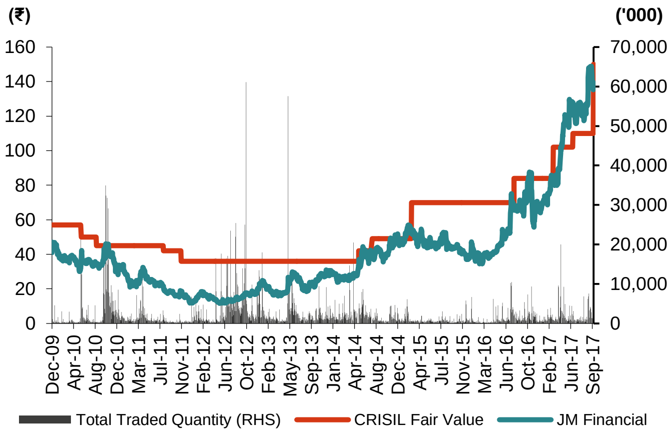
Share price movement



-Indexed to 100

Source: NSE, CRISIL Research

Fair value movement since initiation



Source: NSE, CRISIL Research

CRISIL
An S&P Global Company

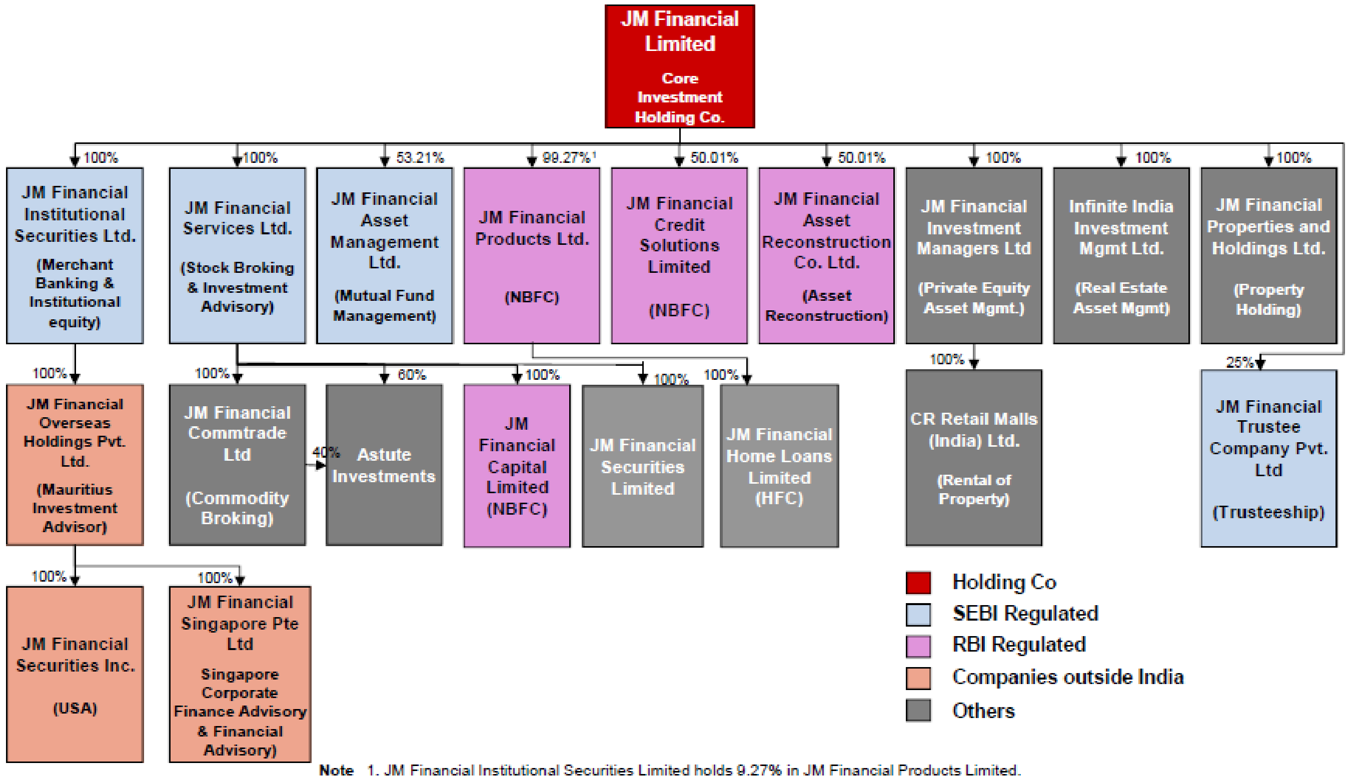
CRISIL IER reports released on JM Financial Ltd

Date	Nature of report	Fundamental grade	Fair value	Valuation grade	CMP (on the date of report)
28-Dec-09	Initiating coverage	4/5	₹57	5/5	₹41
02-Feb-10	Q3FY10 result update	4/5	₹57	5/5	₹41
01-Jun-10	Q4FY10 result update	4/5	₹50	5/5	₹38
19-Aug-10	Q1FY11 result update	4/5	₹45	5/5	₹34
03-Nov-10	Q2FY11 result update	4/5	₹45	4/5	₹40
27-Jan-11	Detailed Report	4/5	₹45	5/5	₹22
21-Feb-11	Q3FY11 result update	4/5	₹45	5/5	₹25
14-Jun-11	Q4FY11 result update	4/5	₹42	5/5	₹24
04-Aug-11	Q1FY12 result update	4/5	₹42	5/5	₹22
08-Nov-11	Q2FY12 result update	4/5	₹33	5/5	₹19
24-Nov-11	Detailed Report	4/5	₹36	5/5	₹15
20-Feb-12	Q3FY12 result update	4/5	₹36	5/5	₹18
27-June-12	Q4FY12 result update	4/5	₹36	5/5	₹12
29-Aug-12	Q1FY13 result update	4/5	₹36	5/5	₹14
28-Nov-12	Q2FY13 result update	4/5	₹36	5/5	₹17
06-Dec-12	Detailed Report	4/5	₹36	5/5	₹18
05-Mar-13	Q3FY13 result update	4/5	₹36	5/5	₹16
07-June-13	Q4FY13 result update	4/5	₹36	4/5	₹29
10-Sep-13	Q1FY14 result update	4/5	₹36	5/5	₹24
08-Nov-13	Q2FY14 result update	4/5	₹36	5/5	₹28
21-Feb-14	Q3FY14 result update	4/5	₹36	5/5	₹26
23-May-14	Q4FY14 result update	4/5	₹42	4/5	₹37
12-Aug-14	Q1FY15 result update	4/5	₹49	4/5	₹40
11-Nov-14	Q2FY15 result update	4/5	₹49	3/5	₹47
23-Feb-15	Q3FY15 result update	4/5	₹70	5/5	₹53
23-Jun-15	Detailed report	4/5	₹70	5/5	₹46
18-Aug-15	Q1FY16 result update	4/5	₹70	5/5	₹53
08-Dec-15	Q2FY16 result update	4/5	₹70	5/5	₹37
27-June-16	Detailed report	4/5	₹70	5/5	₹51
30-Aug-16	Q1FY17 result update	4/5	₹84	5/5	₹66
08-Dec-16	Q2FY17 result update	4/5	₹84	4/5	₹71
06-Mar-17	Q3FY17 result update	4/5	₹102	4/5	₹82
12-Jun-17	Q4FY17 result update	4/5	₹110	2/5	₹126
03-Oct-17	Detailed report	4/5	₹150	3/5	₹143

Company Overview

Established in 1973, JM Financial is an integrated financial services player, operating across varied business such as investment banking, equity, debt, commodity sales and trading, wealth management, portfolio management services, asset management, alternative asset management, financing and lending and distressed asset management. These businesses are managed as strategic business units and organised as separate companies headed by a team of professionals. The group caters to corporates, HNIs and retail investors through its subsidiaries / joint ventures / associate companies.

Figure 33: Organisational structure*



Source: Company, CRISIL Research

*Note: as on June 30, 2017

Milestones

1973	• Establishment of JM Financial & Investment Consultancy Services Pvt. Ltd
1986	• Ventured into stock broking and the securities broking business
1997	• Joint venture with Morgan Stanley to offer IB and securities broking services
2006	• Launch of PE fund, JM Financial India Fund, with US-based Old Lane Partners, LP
2007	• Termination of joint venture with Morgan Stanley • Acquired 60% stake in ASK Securities – specialised in institutional broking business • Launch of the real estate fund
2008-12	• Acquired the remaining 40% stake in ASK Securities and rechristened JM Financial Institutional Securities Pvt. Ltd • Strategic co-operation with Rand Merchant Bank of South Africa to offer M&A advisory services to Indian and African corporates • Expanded to international markets • Commenced asset reconstruction business
2012-till date	• Announced partnership in real estate NBFC, with an investment made by Vikram Pandit • Announced the appointment of Mr Vishal Kampani as MD of JM Financial Ltd. Mr Nimesh Kampani continues to be the non-executive chairman of the group and a director on the board of a few group companies • Floated HFC and applied to NHB for licence

Source: Company

Annexure: Financials (Consolidated)

Income statement

(₹ mn)	FY15	FY16	FY17	FY18E
Operating income	**13,984**	**16,847**	**23,593**	**29,175**
EBITDA	**9,554**	**12,254**	**17,995**	**23,038**
EBITDA margin	**68.3%**	**72.7%**	**76.3%**	**79.0%**
Depreciation	181	203	233	250
EBIT	**9,374**	**12,051**	**17,761**	**22,788**
Interest	4,202	5,121	7,820	10,875
Operating PBT	**5,172**	**6,930**	**9,942**	**11,913**
Other income	(2)	(1)	(24)	-
Exceptional inc/(exp)	(13)	(1)	(196)	-
PBT	**5,157**	**6,929**	**9,721**	**11,913**
Tax provision	1,557	2,225	3,353	4,050
Less: Minority interest/ Share of profit of associates	301	699	1,667	1,850
PAT (Reported)	**3,300**	**4,005**	**4,702**	**6,013**
Less: Exceptionals	(13)	(1)	(196)	-
Adjusted PAT	**3,312**	**4,006**	**4,898**	**6,013**

Balance Sheet

(₹ mn)	FY15	FY16	FY17	FY18E
Liabilities				
Equity share capital	784	789	795	799
Reserves	24,646	28,306	32,532	37,108
Minorities	6,546	6,686	11,092	12,942
Share w arrants	-	-	-	-
Net worth	**31,976**	**35,780**	**44,419**	**50,849**
Convertible debt	-	-	-	-
Other debt	47,239	66,729	108,032	143,412
Total debt	**47,239**	**66,729**	**108,032**	**143,412**
Deferred tax liability (net)	873	853	683	665
Total liabilities	**80,088**	**103,362**	**153,134**	**194,926**
Assets				
Net fixed assets	3,334	3,317	3,726	3,765
Capital WIP	25	86	38	113
Total fixed assets	**3,359**	**3,403**	**3,764**	**3,878**
Investments	**5,383**	**7,855**	**5,532**	**8,532**
Current assets				
Inventory (securities held as stock i	3,510	2,539	97	3,197
Sundry debtors	2,627	3,548	11,789	4,476
Loans and advances	59,397	77,684	131,292	177,965
Cash & bank balance	2,031	8,548	4,026	6,060
Marketable securities	7,311	5,515	7,471	5,071
Total current assets	**74,876**	**97,833**	**154,675**	**196,769**
Total current liabilities	**4,650**	**6,857**	**11,983**	**15,399**
Net current assets	**70,226**	**90,976**	**142,693**	**181,370**
Intangibles/Misc. expenditure	**1,120**	**1,128**	**1,145**	**1,145**
Total assets	**80,088**	**103,362**	**153,134**	**194,926**

Ratios

	FY15	FY16	FY17	FY18E
Growth				
Operating income (%)	39.6	20.5	40.0	23.7
EBITDA (%)	57.9	28.3	46.8	28.0
Adj PAT (%)	56.5	20.9	22.3	22.7
Adj EPS (%)	50.9	20.1	21.4	22.0
Profitability				
EBITDA margin (%)	68.3	72.7	76.3	79.0
Adj PAT Margin (%)	23.6	23.8	19.9	20.6
RoE (%)	13.9	14.7	15.1	16.9
RoCE (%)	14.1	13.3	13.9	13.1
RoIC (%)	13.4	12.4	12.5	11.6
Valuations				
Price-earnings (x)	11.3	7.5	21.1	16.6
Price-book (x)	1.2	0.8	2.2	2.0
EV/EBITDA (x)	8.6	7.3	11.5	10.6
EV/Sales (x)	6.3	5.6	9.2	8.4
Dividend payout ratio (%)	32.1	28.6	24.4	21.6
Dividend yield (%)	2.8	3.8	1.2	1.3
B/S ratios				
Current ratio (x)	16.1	14.3	12.9	12.8
Debt-equity (x)	1.5	1.9	2.4	2.8
Net debt/equity (x)	1.2	1.5	2.2	2.6
Interest coverage	2.2	2.4	2.3	2.1

Cash flow

(₹ mn)	FY15	FY16	FY17	FY18E
Pre-tax profit	5,170	6,930	9,918	11,913
Total tax paid	(1,590)	(2,245)	(3,522)	(4,068)
Depreciation	181	203	233	250
Working capital changes	(23,412)	(16,030)	(54,282)	(39,044)
Net cash from operations	**(19,651)**	**(11,142)**	**(47,653)**	**(30,950)**
Cash from investments				
Capital expenditure	(2,365)	(255)	(612)	(364)
Investments and others	(2,143)	(675)	366	(600)
Net cash from investments	**(4,508)**	**(931)**	**(245)**	**(964)**
Cash from financing				
Equity raised/(repaid)	557	152	192	115
Debt raised/(repaid)	17,309	19,490	41,303	35,380
Dividend (incl. tax)	(1,265)	(1,334)	(1,298)	(1,547)
Others (incl extraordinaries)	5,437	281	2,983	-
Net cash from financing	**22,039**	**18,588**	**43,180**	**33,948**
Change in cash position	(2,108)	6,517	(4,522)	2,033
Closing cash	2,031	8,548	4,026	6,059

Quarterly financials

(₹ mn)	Q2FY17	Q3FY17	Q4FY17	Q1FY18
Total operating income	**5,638**	**5,940**	**7,250**	**7,091**
Change (q-o-q)	18.3%	5.4%	22.1%	-2.2%
EBITDA	**4,281**	**4,505**	**5,463**	**5,379**
Change (q-o-q)	21.6%	5.2%	21.3%	-1.6%
EBITDA margin	**75.9%**	**75.9%**	**75.4%**	**75.9%**
Reported PAT	1,507	1,637	2,103	1,781
Adj PAT	**1,147**	**1,186**	**1,508**	**1,282**
Change (q-o-q)	33.2%	3.4%	27.2%	-15.0%
Adj PAT margin	**20.3%**	**20.0%**	**20.8%**	**18.1%**
Adj EPS	**1.4**	**1.5**	**1.9**	**1.6**

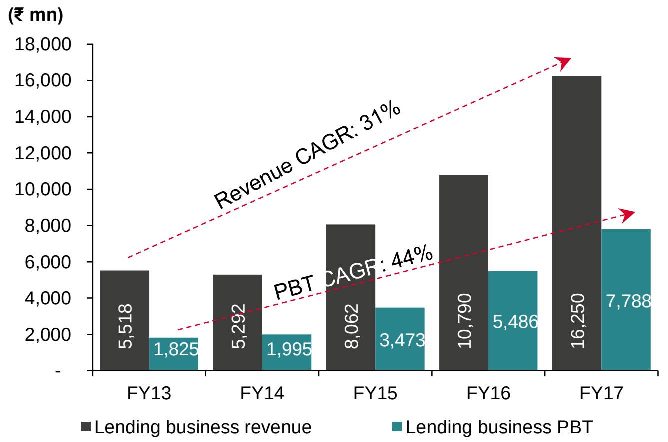
Per share

	FY15	FY16	FY17	FY18E
Adj. EPS (₹)	4.2	5.1	6.2	7.5
CEPS	4.4	5.3	6.2	7.8
Book value	40.8	45.3	55.9	63.6
Dividend (₹)	1.4	1.5	1.5	1.6
Actual o/s shares (mn)	784	789	795	799

Source: CRISIL Research

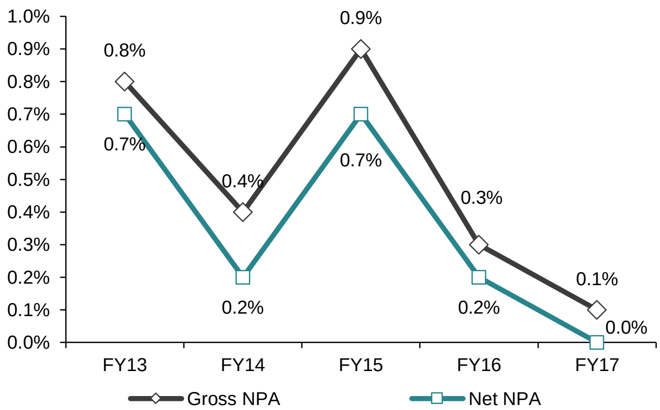
Focus charts

Fund-based business posted robust revenue and PBT growth



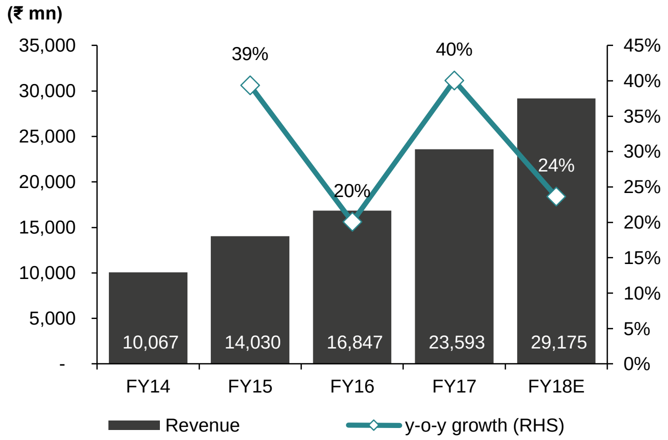
Source: Company, CRISIL Research

JM's expertise and disciplined approach helped improve asset quality



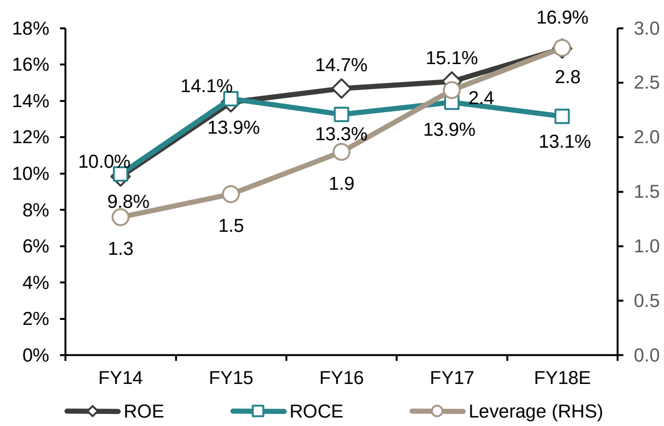
Source: Company, CRISIL Research

Revenue estimated to increase 24% in FY18



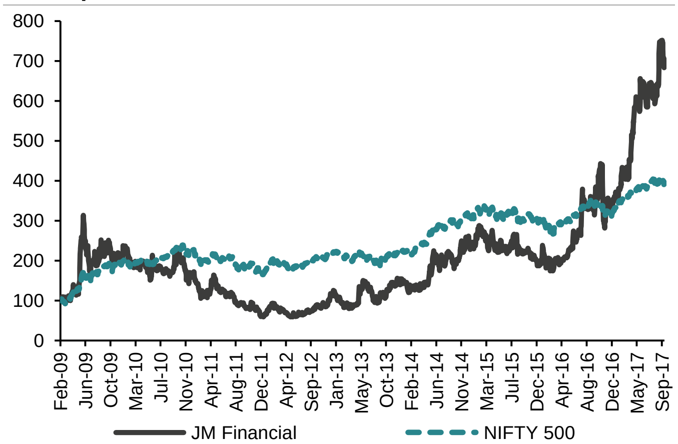
Source: Company, CRISIL Research

RoE expected to increase in FY18



Source: Company, CRISIL Research

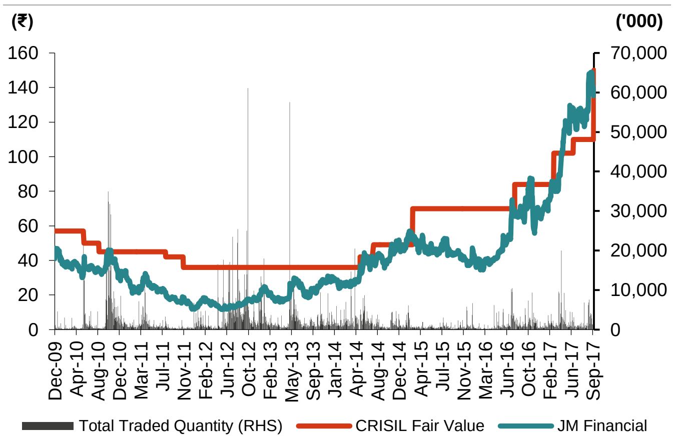
Share price movement



-Indexed to 100

Source: NSE, CRISIL Research

Fair value movement since initiation



Source: NSE, CRISIL Research

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Last updated: April 2016

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