FINANCIAL SERVICES SEGMENT

Consumer loans

Overview

L&T Finance Holdings Ltd. (LTFH), incorporated in 2008 and listed in 2011, domiciles the financial services aspirations of the Group. It is one of the India's leading NBFCs, having a strong presence across lending businesses.

LTFH embarked on the strategy of 'Lakshya 2026' to become a digitally-enabled retail finance company, moving from being 'product-focused' to 'customer-focused', thereby pivoting to become a FinTech@Scale. FY 2022-23 was characterised by the reshaping of businesses towards 'Retailisation' with the intent of creating sustainable, long-term value for all stakeholders in line with the Lakshya 2026 plan.

LTFH has a granular digital and data analytics-powered retail franchise pan-India, delivered through a network spanning 27,500+ employees, across more than 100 cities / towns and about 2 lakh villages with over 28,000 touch-points. This, in turn, caters to the requirements of more than 2 crore customers through a suite of customer-focused products.

Retail Finance

The Retail business comprises the following:

Rural business loans and Micro-loans

The Rural Business loans and Micro-loan products, backed by a strong rural presence and digitally-enabled processes, are committed to the financial inclusion of the unserved and underserved rural customer segment. During the year, the Business achieved a disbursement growth of 70% y-o-y to ₹ 16,910 crore, to over 30 lakh rural women customers. The loan portfolio in this segment stands at ₹ 18,693 crore as on March 2023, growing at 41% on a y-o-y basis.

Farm Equipment Finance

Domestic tractor volumes grew by 12% on a y-o-y basis to 9.4 lakh, on the back of a good monsoon, adequate reservoir levels, robust *mandi* arrivals of crops and a record *Rabi* sowing. Retail demand across key geographies continued to be strong on the back of positive customer sentiments led by finance availability, better price realisation of crops and favourable Minimum Support Prices (MSPs). LTFH, with its strong Original Equipment Manufacturer (OEM) and dealer relationships, continued to be a leading player in this space by financing more than 1 lakh new tractors.

LTFH's digital-assisted app proposition offers a seamless onboarding experience with an industry-best Turnaround Time (TAT) of less than 24 hours. This has resulted in disbursement growth of 25% y-o-y to ₹ 6,450 crore and a book growth of 13% y-o-y to ₹ 12,819 crore.

Urban Finance

- **Two-wheeler Finance**

  The two-wheeler industry grew 19% during the year, with domestic sales increasing by 14%. However, it is yet to reach the peak pre-COVID levels. Despite this, LTFH's performance has outperformed the sector, with

Farm finance

disbursements of ₹ 7,110 crore and a book size of ₹ 8,960 crore, increasing by about 20% y-o-y and resulting in about 8.45 lakh units being financed.

The underwriting process in this business is powered by an algorithm-driven engine which ensures quick processing and industry-best TAT. This acts as a catalyst for maintaining a leadership position in the market.

- **Home Loans and Loan Against Property (LAP)**

The mortgage market in India (industry size of ₹ 27.6 trillion for Home Loans and ₹ 6.24 trillion of LAP), coming out of the pandemic, witnessed steady growth in FY 2022-23 despite being faced with a rapidly rising interest rate cycle wherein RBI orchestrated a 250 basis points (bps) increase in Repo rate between May 2022 and February 2023.

LTFH has expanded its business with an increase of 97% in disbursements over the previous year reaching ₹ 4,730 crore and 26% growth in book reaching ₹ 13,410 crore. This has been achieved with the business changing the customer mix of Salaried and Self-Employed Non-Professional (SENP) customers for new disbursements.

To strengthen the distribution network, the Business has created a multi-directional distribution channel by sourcing Direct Selling Agents, Referral Agents, Developers and Digital business.

- **Consumer Loans**

The Personal Loan industry in India is witnessing consistent double-digit growth year after year, with a market size of ₹ 9.9 trillion. Despite the existence of several loan products in the market, online Personal Loans (PLs) have emerged as one of the most favoured loan options.

LTFH embarked on launching this product two years ago by tapping into its two-wheeler customer base, harvesting a database of over 65 lakh customers as of March 2023. This year, based on the success of this product, the Business expanded the sourcing channel to e-aggregators comprising partnerships with over 15 FinTech players, aggregators and BFSI companies. As a result of these efforts, the Business has disbursed ₹ 4,886 crore in FY 2022-23, translating to a book size of ₹ 5,471 crore.

Small and Medium Enterprise (SME) Finance

LTFH forayed into the financing of professionals and small businesses through a new vertical – SME Finance in FY 2021-22. Post an initial pilot project to establish and firm up its proposition, LTFH launched it as a full-fledged proposition in FY 2022-23. The franchise, which started with 2 locations, has now expanded to 19 in FY 2022-23 with disbursements of ₹ 1,473 crore, leading to a book size of ₹ 1,378 crore and a customer base of more than 6,000. LTFH has created its distribution framework through its 130+ channel partners pan-India.

SME loans

The USP that LTFH is endeavouring to create is a direct-to-channel journey, digitally simplified processes and a strong value proposition to the customer – through term loan and drop-line Overdraft (OD) assistance.

Wholesale Finance

The Wholesale business comprises Infrastructure Finance and Real Estate Finance.

LTFH is in the process of transforming itself into a retail finance company. This process of Retailisation is expected to be completed through a two-pronged approach of growing the Retail book as well as reducing the Wholesale book through accelerated sell-down.

During the year, the Wholesale Finance book (including De-focused) reduced from ₹ 43,257 crore to ₹ 19,840 crore, a 54% reduction y-o-y through a calibrated reduction of Infrastructure Finance and Real Estate Finance books.

Business Environment

Non-Banking Financial Companies (NBFCs) have been an integral part of India's financial ecosystem, complementing the banking system in many ways. They provide a wide range of financial services like loans, credit facilities, investments and other financial offerings. NBFCs have played a significant role in the Indian economy's growth and financial inclusion story, especially in the rural and semi-urban areas. One of the major factors that have contributed to the growth of NBFCs is the rising aspiration level amongst the masses which has translated into growing demand for credit in the Indian economy, across all categories. Another factor that has contributed to the growth of NBFCs is the Government's initiatives to promote financial inclusion. The Government has launched a number of schemes like Pradhan Mantri Jan Dhan Yojana (PMJDY), Mudra Yojana and Stand-Up India to extend financial services to the unbanked and underbanked population.

As the economy revives post-pandemic, NBFC sector prospects have improved due to robust infrastructure spending by the Government, increased consumer spending, credit uptake in industrial and agriculture sectors and low transaction costs. Further, the rural segment is also thriving due to an increase in crop prices, healthy *Rabi* sowing season, strong water reservoir levels and reasonable export demand. Rising digital penetration in the country driven by FinTechs is also supporting the growth of NBFCs.

There have been some headwinds during the year due to aggressive rate hikes by the US Federal Reserve impacting the flow of foreign funds into the country. The financial conditions turned tighter during the second half of FY 2022-23 following monetary policy tightening by the RBI, which somewhat impacted the lending growth in the country. Liquidity in the banking system turned into a deficit intermittently due to transient factors like advance tax outflows, GST outflows, State Bond auctions, etc. However, the RBI injected liquidity through variable repo auctions with higher Government spending to protect the positive credit sentiment.

Major Achievements

FinTech@Scale:

LTFH launched – PLANET, a D2C app in March 2022. Within a year of its launch, PLANET crossed 30 lakh downloads,

Two-wheeler loans

with over 2.8 lakh customers from the rural sector. LTFH sourced over ₹ 1,650 crore, collected more than ₹ 240 crore and serviced over 48 lakh customers during the year. The app is rated 4.5 (on a scale of 5) on the Google Play store.

The app aims to deepen customer engagement and features over 130 functions. It is evolving continuously and adding new features to provide a differentiated customer proposition.

Significant Initiatives

The business undertook the following strategic initiatives in FY 2022-23 towards fast-tracking Lakshya 2026 goals:

- **Sale of Mutual Fund business**

  The Mutual Fund business was sold to HSBC AMC in Q3 FY 2022-23 for a total consideration of ₹ 4,249 crore.

- **Accelerated pace of Retailisation**

  During the year, the Company increased the share of Retail from 51% to 75% and reduced the mix of Wholesale from 49% to 25%.

  The Retail portfolio grew 35% during the year through growth led by flagship products – Farm Equipment Finance, Two-Wheeler Finance and Micro-Loans; high growth in mature products such as Home Loans as well as a pick-up in new products such as Consumer Loans and SME loans.

- **Single Lending Entity Structure**

  In line with the 'Right Structure' strategy, LTFH, over the last 7 years, has merged 5 entities. This has led to a reduction in the number of lending entities from 7 to 2, i.e., L&T Finance Limited (LTF) and L&T Infra Credit Limited (LTICL), leading to simplification of the corporate structure along with enhanced governance and superior controls. It is now proposed to merge these subsidiary lending entities with the equity-listed holding company LTFH (subject to necessary statutory / regulatory approvals).

Risk Management Framework

LTFH has in place a Board-approved Enterprise-wide Risk Management Framework. This framework encompasses Risk Appetite Statement, Risk Limits Framework, Risk Dashboards and Early Warning Signals.

In addition to Enterprise-wide Risk Management Framework, the following emerging risks are being addressed in line with Lakshya 2026.

Credit Risk

A new-age portfolio management framework has been put in place as a part of the Lakshya 2026 journey. The focus is on strengthening the underwriting capabilities for existing as well as 'New-To-Credit' customers by investing further in building geo-agnostic underwriting capabilities and improving digital and analytical capabilities.

Micro-finance

The business has a provisioning policy which is cautious, conservative and prudent in nature. As part of the strategy of insulating it from event-based risks, LTFH has built macro-prudential provisions to strengthen the balance sheet. As at March 31, 2023, the company carried ₹ 1,171 crore of macro-prudential and other additional non-GS3 provisions in the Retail segment.

Liquidity Risk

The Business maintains a positive liquidity gap on a cumulative basis in all the time buckets up to 1 year (at LTFH consolidated level). A Contingency Funding Plan has also been put into practice for responding to severe disruptions, which might affect the ability to fund activities in a timely manner and at a reasonable cost.

IT Risk

The Business is undergoing a digital transformation with cyber security being a key deliverable to ensure the continuity of business. Accordingly, the Business has put in place the necessary security measures to shield its systems and data against cyberattacks. In addition, a detailed security assessment of all internet-facing applications is also carried out on a regular basis.

Outlook

Global growth is forecasted to slow down on account of sustained inflation in many economies, rising interest rates and negative global spillover effects from the war in Ukraine. India may see a slower GDP expansion in FY 2023-24 on the back of a likely slowdown in global economies, a high-interest rate environment amidst sustained inflationary pressures, subdued consumption demand and pressures on external balances.

Although there are a few definite positives for India such as sustained government capex, deleveraged corporates, low-stressed assets in the banking sector, Production-linked Incentive (PLI) schemes, etc., they are still not sufficient to take India's GDP growth to near potential levels.

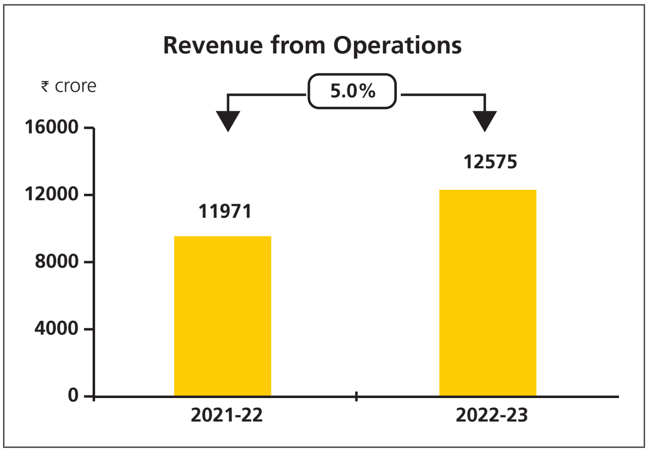
The Indian banking system's health continues to be at its best in decades. India Ratings expects the banking system credit growth to moderate to 13.5% (y-o-y) in FY 2023-24 from 15% in FY 2022-23. During FY 2023-24, bank credit growth would be driven by housing NBFCs catering to the credit needs in the services segment and large industry segment (especially working capital). However, loans to SMEs could pose risks to the banks' asset quality because this segment is the most vulnerable to elevated interest rates.

The overall loan book of the NBFC sector could reach about ₹ 50 trillion by March 2024 (from ₹ 40 trillion as of March 2022), as per estimates by ICRA Ratings. Various rating agencies have pegged the NBFC sector growth between 12-16% for FY 2023-24. This growth would be largely driven by NBFCs who have access to capital and cost-of-funding advantage. Credit costs are likely to remain benign, but a higher borrowing cost would compress spreads for NBFCs in FY 2023-24. Near-term growth for NBFC retail book is expected to be driven by the unsecured segments comprising personal credit and micro-finance.

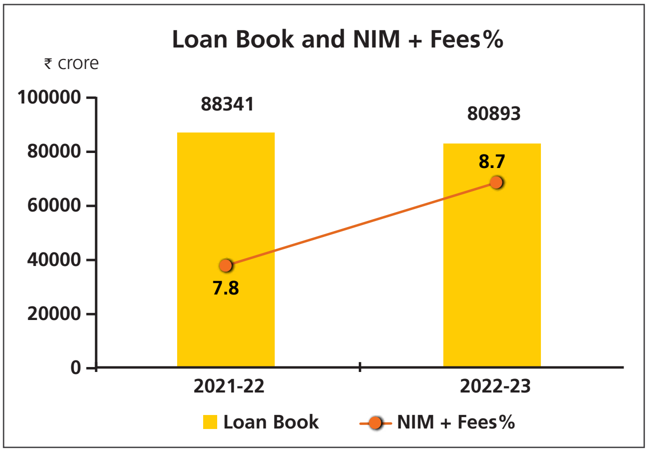
Home loans

The business will continue to pursue its stated strategy of a customer-focused FinTech@Scale growth in the Retail lending sector.

Financial performance of the segment



The segment's revenue improved by 5.0% y-o-y at ₹ 12,575 crore for FY 2022-23 due to higher disbursements on the back of the retailisation of book strategy. A revised business strategy is being implemented in line with the Lakshya 2026 strategic plan. The core strategy for the Financial Services business revolves around its transformation into a full-scale retail-oriented, digitally-enabled business. Several initiatives have been completed to exit the wholesale exposure, resulting in 75% of its loan book being retail credit as at March 31, 2023.



Disbursements of loans and advances at ₹ 46,975 crore for the year registered a growth of 26% on the y-o-y basis, reflective of a higher credit demand due to overall improvement in economic activity. The Loan Book stood at ₹ 80,893 crore as at March 31, 2023, registering a decline of 8% over the previous year, reflecting timely collections in Retail Finance, phased exit from Wholesale Finance and sell-downs to ARCs (in Wholesale Finance and de-focused book). The Net Interest Margin (NIM), including fee income, improved from 7.8% to 8.7%, mainly due to the increased share of the retail portfolio and higher fee income.

The Gross Non-Performing Asset (GNPA) ratio marginally moved up to 4.74% as at March 31, 2023, from 4.08% as at March 31, 2022. Net NPA ratio has improved to 1.51% as at March 31, 2023, against 1.98% as at March 31, 2022.

The Financial Services business has concluded the sale of the Mutual Fund business to HSBC AMC during the year.