Rationale for Investment

L&T Finance Limited (LTF) is wholly owned subsidiary of L&T Capital Holdings Limited, which is in turn a 99.99% subsidiary company of Larsen & Toubro Limited (L&T). LTF was incorporated as a Non Banking Finance Company (NBFC) in November 1994. LTF offers a spectrum of financial products and services for trade, industry and agriculture and has evolved into a multi product finance company with a diversified corporate and retail portfolio. LTF enters the debt capital market on 09 February 2010 with a public issue of Non Convertible Debentures (NCDs) aggregating up to Rs. 250 cr with an option to retain over-subscription of upto Rs. 250 cr for issuance of additional NCDs. aggregating to a total of up to Rs. 500 Crores

In the current market scenario, there are limited direct debt options for the retail investor in the fixed income market. LTF offers one more opportunity to the investor. It offers a better interest rate than other alternatives with no significantly higher risk. Further, given its established track record, decent financial history, high credit rating, strong parental backing, attractive returns compared to other fixed income options, medium liquidity and safety (NCDs are 100% secured by assets of the company), we feel that risk averse investors willing to hold for between 5-10 years can participate in this issue (low to medium risk, long term investment).

Given below is a table, which compares the NCD issue with other debt options available in the market.

Parameter	Company FD	Bank FD	Post office instruments like NSC, FIP, MIS	Liquid fund	Income fund	Tata Capital NCD **	STFC NCD **	L&T Finance NCD **
Returns/YTM p.a (%)	7.5-9	6.0-7.0	7.5-9.0	3.5-5.0	4.5-6.0	8.2 *	8.7*	8.8*
Volatility in returns	Low	Low	Low	Low	High	Low	Low	Low
Safety	Medium	High	High	High	High	Medium	Medium	Medium
Liquidity	Low	High	Low	High	High	Medium	Low	Low
Service Issues	No	No	Yes	No	No	No	No	No
Tax exemption on interest/investmen	No	Partial	Partial	Partial	Partial	No	No	No

**= calculated based on CMP on NSE, * = YTM based on secondary market rates, one year option chosen for NCD, except L7T (N2) (Source: HDFC Securities)

Investors in Tata Capital NCD issue (Feb 2009), STFC NCD issue (July 2009) and L&T Finance NCD issue (August 2009) have so far earned handsome returns due to yields falling in the meanwhile. All these issues (except STFC) were oversubscribed by a wide margin.

Investors should evaluate the NCD issue in the light of the fact that they allow locking into a yield between 8.40% - 8.50% for a 3 year period, even as returns on most other fixed-income options have declined sharply in the recent past.

The issue is attractive for investors who are concerned about the brand / management credibility of the issuer company and one who feels that interest rates in India are not going to rise significantly for 3 year corporate papers and hence is a good idea to lock into these rates at this point.

We feel that in an economy that is growing fast, where Consumer price inflation continues to remain high and when the Govt borrowing program is aggressive; interest rates may not fall below a level.

If convinced about the merits of the issue, the investor needs to apply at the earliest as allotment is to be made on first come first serve basis.

The **attractiveness of the issue** is summed up by the Credit Rating agencies; an extract of their comments is reproduced hereunder:

CARE: *'"The rating factors in the strength of the ultimate parent – Larsen and Toubro Ltd. (L&T) and its continued demonstrated support to LTF, by way of capital support as well as provision of additional business opportunities. The brand equity of L&T also benefits LTF. LTF's board comprises of senior executives of L&T. The rating is also supported by the established track record of LTF, comfortable profitability, well diversified revenue streams and financial flexibility. LTF's ability to scale up operations in a highly competitive business scenario while maintaining control over asset quality, effectively managing its liquidity position, ability to raise resources at competitive cost and continued support from L&T would be the key rating sensitivities*

Issue Details

LTF expects to raise a minimum amount of Rs 250 cr under this offer, with the option of retaining an additional Rs. 250 cr. The funds raised after meeting the expenditures of and related to the issue, will be used for LTF's various financing activities including lending and investments, to repay existing loans and business operations including for capital expenditure and working capital requirements as well as for any other uses permitted by applicable law.

Summary of Issue Details	
Issuer	L&T Finance Limited
Issue opens on	09 February, 2010
Issue closes on	22 February, 2010 (with an option to close issue early)
Stock Exchanges proposed for listing of the NCDs	NSE & BSE

Issuance and Trading	Compulsorily in dematerialised form
Trading Lot	1 (one) NCD of Rs.1, 000 each
Depositories	NSDL and CDSL
Security	Security will be created for the purpose of this Issue as per the Debenture Trust - cum - Mortgage Deed.
Rating	'CARE AA+' by CARE and 'LAA' by ICRA
Lead Managers	JM Financial, Citigroup Global Markets India Pvt Ltd, Kotak Mahindra Capital Company Ltd
Registrar	Sharepro Services (India) Pvt Ltd
Debenture trustee	Bank of Maharashtra

(Source: Prospectus)

Applications cannot be made by NRIs, Minors without guardian name, FIIs, OCBs and non-residents.

Specific terms of each instrument

Options	I	II
Frequency of interest payment	Semi –annual	Annual
Minimum application (Rs.)	10,000 (Retail), 1,01,000 (NIIs & QIBs)	10,000 (Retail), 1,01,000 (NIIs & QIBs)
In multiples of (Rs.)	1,000	1,000
Face value (Rs/NCD)	1,000	1,000
Issue price (Rs/NCD)	1,000	1,000
Mode of interest payment	Through various options available*	Through various options available*
Coupon (%) p.a.	8.40% p.a	8.50% p.a
Yield on redemption	8.58%	8.50%
Tenor	36 months from the date of Allotment	36 months from the date of Allotment
Redemption Amount	Applicable face value plus any accrued interest	Applicable face value plus any accrued interest

* Interest payment could be via various options such as ECS, NEFT, and RTGS etc (Source: Prospectus)

Liquidity and Exit Options

- Secondary market exit – Listing on the NSE & BSE to provide tradability
- Buy back of NCDs – Company to consider buyback of NCDs from time to time

Interest on application money

Interest on application monies received which are used towards allotment of NCDs
LTF shall pay interest on the application money on the amount allotted, subject to deduction of income tax under the provisions of the I.T. Act or other statutory modification or re-enactment thereof, as applicable, if it exceeds the prescribed limit of Rs. 5,000/- in any financial year to any investor from the date of realization of the cheque(s) / demand draft(s) upto the Deemed Date of Allotment, at the rate of 7% per annum. The Application Interest shall be paid one day prior to the Deemed Date of Allotment. In the event the Company / Registrar is not able to determine the date of realization of application money, pursuant to application, the interest on application money shall be calculated from date of application upto the Deemed Date of Allotment.

Interest on application monies received which are liable to be refunded
LTF shall pay interest on refund of application monies on the amount not allotted from the date of realization of the cheque / demand draft upto the Deemed Date of Allotment, at the rate of 2.5% per annum on the amount refunded.

Basis for Allotment

Separate investor categories shall be maintained as under:
- Retail – 30% of issue size
- Non-institutional investor – 40% of issue size out of which 15% of issue size including the over subscription amount is reserved for-resident individuals and HUF's
- Qualified Institutional Buyer – 30% of issue size

On closure of the issue, all the valid applications would be segregated among the aforesaid 3 categories within which allotment on a **first come first serve basis** to the extent of the specified percentages would be done. However, with respect to applications which cannot be distinguished on first come first serve basis on the basis of such applications being filed on the same date, such applicants will be allotted NCDs based in proportion to their respective application size, rounded off to the nearest integer.

Company Background

LTF, promoted by L&T, was incorporated in November 1994, to provide a range of financial services. LTF began by financing the small and medium enterprises and later synergised with the opportunities provided by L&T ecosystem consisting of its subsidiaries and associates along with its large network of dealers, vendors, suppliers, clients etc. LTF has now evolved into a multi product asset backed finance company with a diversified corporate and retail portfolio. LTF is a wholly owned subsidiary of L&T Capital Holding Ltd, which is in turn a 99.99% subsidiary company of L&T.

LTF is headquartered in Mumbai and has a presence in major cities in India. As on September 30, 2009, LTF had 77 Branches and 355 points of presence. The network has been built to cater to the growing business needs and provide satisfactory customer services. Being a subsidiary of L&T, LTF has leveraged the knowledge, experience and businesses of L&T, while continuing to grow and expand independently.

As on September 30, 2009, LTF had an asset base of Rs. 6,016.7 cr. LTF has relationships with over 500 corporates, 8,000 contractors, 1,500 vendors, 900 dealers 10,000 transporters, 40,000 farmers and over 5,00,000 microfinance clients. LTF's revenues for the six month period ending September 30, 2009 stood at Rs. 421.8 cr. LTF has consistently made profits and generated return on assets of over 1.85% in the past 5 years.

Its core business is that of asset backed finance, covering a wide range of commercial and farm assets. As at September 30, 2009, Asset backed loans constituted 87.50% of its total loan assets. LTF also provides loans for meeting the working capital needs of small and medium enterprise (primarily to vendors and dealers of large corporate) and loans against capital market assets for corporate. It continues to strengthen its Micro Finance business furthering its commitment towards financial inclusion in the rural economy. Its client base for asset-backed loans includes large corporates, banks, multinational companies, small and medium enterprises, contractors, commercial vehicle operators and farmers.

Corporate Finance Group	Retail Finance Group
Asset Finance	Construction Equipment Finance
Capital Market Products	Transport Equipment Finance
Corporate Finance	Rural Financing And Distribution
Channel Finance	Micro Finance & Financial Products Distribution

(Source: Prospectus)

Corporate Finance Group accounts for 38% of total assets as on September 30, 2009 and Retail Finance Group accounted for the balance 62%.

Key Strengths of the company

Diversified and Balanced mix of businesses and customers

LTF provides services to clients in most of the growing sectors of the economy such as construction & ancillaries, rural finance and infrastructure, which are the focus areas for the Government of India. It offers a broad spectrum of financial products and services and cater to the needs of diverse customers which extends from construction contractors, truck owners, farmers, shopkeepers etc in the small segment, to medium sized vendors, dealers and contractors and also to large corporates including MNCs. LTF's presence in diversified businesses across asset classes and client segments reduces the risk of product and client concentration. Its diverse product range also allows it to offer innovative financial solutions.

Portfolio Quality

One of LTF's major strengths is its ability to maintain the quality of its asset portfolio. LTF derives significant benefits from the knowledge, experience and businesses of its promoter and group companies to understand corporate and small business clients and provide them with financial services and products that meet their requirements. Over a period of time, LTF has developed a mechanism for credit checking and valuation of assets that enables it to check the quality of its asset portfolio. This is reflected in a relatively lower level of delinquencies represented by the Gross NPA levels.

LTF's track record in maintaining Asset Quality has been consistent with net NPA's being continuously less than 1% between FY05 to FY08. The Net NPA as at March 31, 2005 March 31, 2006, March 31, 2007 and March 31, 2008 were 0.13%, 0.14%, 0.20% and 0.76% respectively. Its net NPAs stood at 2.04% of net advances as on March 31, 2009 and stood at 2.79% of net advances as on September 30, 2009. The rise was primarily on account of the overall economic downturn.

Respected brand arising out of strong parentage

L&T is one of the leading companies in infrastructure space and has received numerous awards and recognition from both domestic and international bodies over the years for its excellence and leadership. In 2009, L&T was ranked within the top 50 in a survey of the World's Most Reputable Companies. Being a subsidiary of L&T has provided LTF with a platform to reach out to potential customers and lenders. The reputation of the L&T brand has facilitated LTF's entry and consolidation in Construction Equipment. Furthermore, the background of L&T in the infrastructure sector has also provided LTF knowledge of the dynamics of the construction equipment industry.

Commitment from L&T

L&T has infused a total capital of Rs. 636.69 cr into LTF till date, including share premium of Rs. 424.51 cr. The financial services business is important for L&T in furthering its outreach, providing stable sources of income and participate in the growing opportunities thrown open by the financial sector.

Adequately Capitalized

LTF is subject to the capital adequacy requirements prescribed by the RBI. It is currently required to maintain a minimum ratio of 10% as prescribed under the Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007 (as amended from time to time) based on total capital to risk weighted assets. As per the RBI circular for NBFC-ND-SI, this limit would have to be increased to 12% by March 31, 2010. As a part of its governance policy, LTF ordinarily maintains capital adequacy higher than the statutorily prescribed CAR. Its CAR as on March 31, 2009 (audited) and as on September 30, 2009 (unaudited) was 16.41% and 15.60% respectively.

Other strengths include adequate controls, processes and risk management systems, experienced management team and high credit ratings.

LTF Strategy

- Expand the existing lines of business
- Increase presence in Infrastructure and Rural Finance
- Explore new business opportunities
- Pursue strategic alliances
- Attract and retain talented professionals
- Expand client base and geographical presence

Risks

- As an NBFC, the risk of defaults and non-payment by borrowers and other counterparties is one of the most significant risks which may affect LTF's profitability and asset quality. Its net NPAs were Rs.106.5 cr representing 2.04% of net advances as at March 31, 2009 as compared to Rs. 362.2 cr representing 0.76% of its net advances as on March 31, 2008.

- LTF may be exposed to the potential loss of lower recovery of value of assets financed/secured to it due to delays in their enforcement on defaults by the company's borrowers as well as a decline in their values. More than 90% of LTF's total gross loan portfolio (excluding inter-corporate deposits) is secured by assets, movable and immovable. The value of certain types of assets may decline due to adverse market and economic conditions (both global and domestic). This also includes equity shares offered as main security/collateral, as the case may be, which are inherently volatile in nature.

- LTF has ventured and are in the process of venturing into new lines of business and there can be no assurance that its ventures will be profitable in future. LTF has recently ventured into new lines of business such as Micro Finance and Distribution of Financial Products. There are inherent risks in entering a market for the first time or in expanding a particular product portfolio.

- LTF may not be able to access funds at competitive rates and such higher cost of borrowings could have significant impact on the scale of its operations and also profit margins.

- LTF may face asset-liability mismatches in the short term, which could affect its liquidity position. As is typically seen in several NBFCs, a portion of funding requirements is met through short-term funding sources, i.e. bank loans, working capital demand loans, cash credit, short-term loans, non-convertible debentures and commercial papers. However, a large portion of assets have medium to long-term maturities. In the event that the existing and committed credit facilities are withdrawn or are not available to the company, funding mismatches may widen and it could have an adverse effect on LTF's business and future financial performance.

- A large part of the Company's loans are disbursed at fixed rates for specific tenures which may differ from its funding sources and therefore interest rate fluctuations could impact the company's margins as well as profitability.

- A slowdown in economic growth could cause the company's business to suffer. The company's performance and the quality and growth of its assets are necessarily dependent on the health of the overall Indian as well as the global economy. An economic slowdown could adversely affect its business, including its ability to grow its asset portfolio, maintain quality of assets and ability to implement strategy. The domestic economy could be adversely affected by a variety of domestic as well as global factors.

- The company faces increasing competition from other established banks and other NBFCs. The success of its business depends on its ability to face the competition.

- Any downgrading in credit rating of LTF's NCDs may affect the value of NCDs and thus its ability to refinance debts.

- Though the NCDs are proposed to be listed on the NSE, it does not guarantee adequate trades/depth for investors wishing to exit on a particular day or at a particular price. In case the interest rates rise, these NCDs could quote at a discount to their face value.

- Changes in laws and regulations that apply to NBFCs in India, including laws that impact its lending rates and its ability to enforce its collateral.

- In an environment of rising interest rates, the NCDs may trade below their fair value and an investor may have to exit at lower prices. However, investors who hold until maturity will not face this problem.

Financial Summary

Leverage situation of the company pre-issue and post-issue:

(Rs in cr) as on 02 February 2010	Prior to the issue	Post the issue*
Secured loans	3772.3	4272.3
Unsecured loans	2462.6	2462.6
Total Debt	6234.9	6734.9
Share capital	212.2	212.2
Reserves	862.7	862.7
Total Shareholders funds	1074.9	1074.9
Debt equity ratio	5.8	6.3
*Based on Rs. 1000 cr inflow from the issue		

(Source: Prospectus)

Financial Snapshot:

(Rs in cr)	FY07	FY08	FY09	H1FY10
Asset	3096.7	5144.0	5538.5	6274.0
Revenue	275.4	606.1	830.3	421.8
PAT	77.2	161.4	145.4	86.8
Return on Assets (%)	2.8	2.8	1.9	2.0

(Source: Prospectus)

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