IL&FS | Private Equity

IL&FS Investment Managers Limited

ANNUAL REPORT 2013

THE NUCLEUS OF INFRASTRUCTURE

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CORPORATE INFORMATION

BOARD OF DIRECTORS

Mr S M Datta
Chairman

Mr Ravi Parthasarathy

Mr Bansi S Mehta

Mr Jitender Balakrishnan

Mr Siddharth Mehta

Mr Arun Saha

Mr Vibhav Kapoor

Mr Ramesh Bawa

Mr Shahzaad Dalal
Vice Chairman

Dr Archana Hingorani
Chief Executive Officer &
Executive Director

COMPANY SECRETARY

Mr Sanjay Mitra

BANKERS

HDFC Bank Limited

AUDITORS

M/s Deloitte Haskins & Sells
Chartered Accountants

INTERNAL AUDITORS

M/s Patel & Deodhar
Chartered Accountants

REGISTRARS & SHARE TRANSFER AGENTS

Link Intime India Private Limited
C-13, Pannalal Silk Mills Compound
L.B.S. Marg, Bhandup (West), Mumbai 400 078, India
Tel : +91 22 2596 3838 Fax : +91 22 2594 6969

REGISTERED OFFICE

The IL&FS Financial Centre, Plot No C-22, G Block
Bandra Kurla Complex, Bandra (East), Mumbai 400 051, India
Tel : +91 22 2659 3531 Fax : +91 22 2653 3056

Mr S M Datta
Chairman

Dear Shareholders,

The financial year 2013 has been a challenging one. The year began with a difficult outlook and at one point of time it seemed that India was headed towards a period of severe economic slowdown. Economic growth was clouded by a high inflationary environment and mounting fiscal imbalance on account of elevated commodity prices, primarily Oil and Gold. The year did, in the end, witness a decadal low in GDP growth. The recent depreciation in the Rupee may translate into further stress on the economy

However, I am pleased to note that some of the factors contributing to this growth de-acceleration have begun to turn around. Inflation is softening, interest rates are expected to fall and price of Oil and Gold have corrected. This has given room to both the Government and a judicious Central Bank to pursue a more lenient economic policy. The process of financial easing has begun as the Reserve Bank of India has cut interest rates. The difficult economic environment and fear of country rating downgrade also nudged the Government to bring in a slew of economic reforms and focus on balancing its books. These reforms, in my opinion, are steps in the right direction and should hold the economy in good stead in the long term

For a developing economy like ours, sustained growth is an imperative and one of the key requirements for the same is reigniting the investment cycle. Creating a conducive environment for investments is the responsibility of the Government and the Government, to its credit, has earnestly attempted to address some of the issues facing the Indian economy by embarking on the process of fiscal consolidation and ushering in reforms. Another key element of reigniting the investment cycle is infusion of risk capital. The Private Equity industry has been playing a stellar role in channelizing risk capital into the country, and has emerged as one of the largest sources of fresh risk capital for the economy

This year has, however, not been an easy one for the Private Equity industry as a whole. There were headwinds of uncertainty on the economic and on the tax front. International capital with a long term perspective needs an environment which has stability and unfortunately some of the earlier policy announcements created an uncertain scenario. This, coupled with weak global risk appetite, translated into risk aversion amongst long term global investors for India. India focussed fund management companies therefore had a difficult time raising money. New Fund raises fell 73% since 2008 and were, during year, at their lowest level since the Indian Private Equity industry opened up in earnest in 2005

However, Investors have not ignored India completely as evidenced by the record inflows in listed equities space in recent times. The economic outlook is also expected to improve in the near term. This, hopefully coupled with continued liquidity in the global markets, may result in the Private Equity space witnessing more activity on the fund raising and deployment front

During the past year, your Company worked towards consolidating its position as one of India's premier Private Equity fund house and as a thought leader in the business. It has focussed its efforts on bringing differentiated investment products which seek to generate quality, risk mitigated returns for its investors. The process of fund raise for these products is ongoing. Further your Company also worked towards enhancing returns from its existing investments by proactive asset management. As the business environment improves, and our investee companies start ramping up operations, your Company intends to take advantage of the expected improvement in equity markets and announce value accretive exits. I believe that a combination of both strategies, innovative products and a continued focus on generating returns thereby enhancing the already strong track record, will ensure that your Company is the preferred choice for institutional investors to manage their long term funds in India

All growth economies and markets do witness intermittent periods of slow down only to recover and perform better. I have strong belief in the intrinsic potential of India and there is conviction that, despite recent setbacks, growth in India will play out in the long term. Similarly, or rather more so, in the Private Equity business, growth is a step function. The recent past has indeed been challenging but your Company has not only demonstrated the strength of its business model by maintaining profitability levels, but it also laid strong foundations for future growth

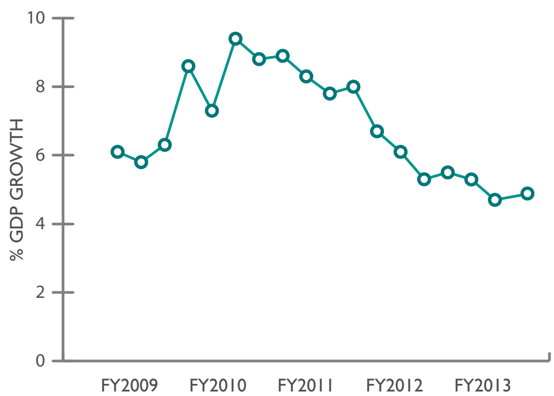
We continue to focus on improving business efficiency with the intent of enhancing shareholder value and in creating a sustainable and growth oriented business. The management and the team have been working relentlessly towards this goal and I would like to thank the shareholders for their continued support and belief in your Company

With Regards

Mr. S M Datta
Chairman

June 10, 2013

Moderating Growth



Led by Weak and Volatile Industrial Output

But Reforms underway to reignite growth

Policy Action / Reform Measures Undertaken
FDI limits relaxed in • Single/Multi Brand Retail • Teleports, Mobile TV Sky Broadcasting Services • Power Exchanges • Scheduled and Non-Scheduled Air Transport Services
Continued Divestment of Public Sector Undertakings
Restucturing of State Electricity Board loans
Fuel Price hike & hike in Railway fares

Policy Action Awaited
Implementation of Goods and Services Tax (GST)
Implementation of Direct Taxes Code (DTC)
Passing of Land Acquisition Bill
Hike in FDI limits in Pension and Insurance Sector

"...Investors have not ignored India completely as evidenced by the record inflows in listed equities space in recent times. The economic outlook is also expected to improve in the near term. This, hopefully coupled with continued liquidity in the global markets, may result in the Private Equity space witnessing more activity on the fund raising and deployment front"

Dr. Archana Hingorani
Chief Executive Officer & Executive Director

Dear Shareholder

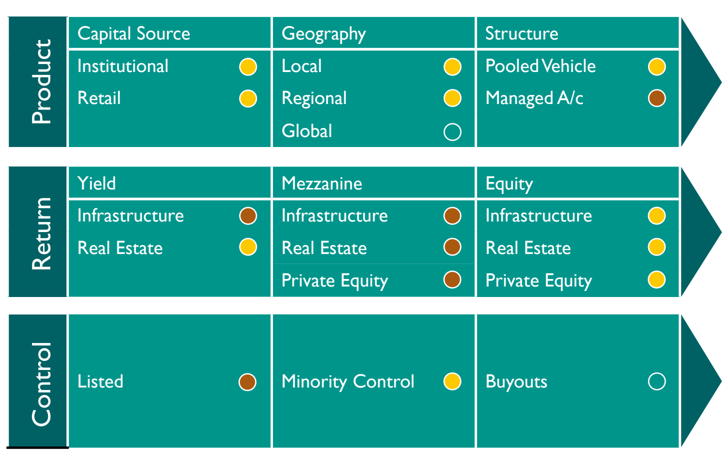
It has been the end of another 'mixed bag' year. The Global economy has vacillated between a mix of fear, trepidation, unease and disquiet at one end; ambivalence and cautious optimism at the other. The Cyprus banking crisis falls in the former category. The ability of policy makers to stave off two of the biggest short-term threats to the recovery - the threat of a euro area breakup and a sharp fiscal contraction in the United States caused by a plunge off the "fiscal cliff" gives rise to the latter. In all, the global economic score card can be termed encouraging. As succinctly put by the International Monetary Fund in its April 2013 World Economic Outlook and Global Financial Stability Report - Financial stability has improved and the ensuing financial market rally has been helping economic recovery by improving funding conditions and supporting confidence

A similar mix of emotions is also at play in India as well. The sub five percent growth during fiscal 2013 is disconcerting, but in the perspective of the paralysis in capital investments which had been plaguing Corporate India for some time now, this growth number is not something which was totally unexpected. Further, on closer examination, there are certain positive factors which are beginning to take shape, laying the foundation for reversing the slowing growth. End of the fiscal has brought relief with lower than expected deficit. The Reserve Bank of India, whilst continuing to maintain its hawkish stance, has relaxed the monetary policy. The Government has also taken some pro-reform measures though on the ground implementation will be instrumental in continuing the positive trends. Growth expectation for fiscal 2014 is being pegged at around 6%. While this is lower than the earlier expectations, it would still reflect a marked improvement over the 2013 growth levels

However, slowing growth and listless primary public markets during the last year have taken a toll on the operating performance and exit expectations of Private Equity (PE) portfolio companies. This coupled with the volatility in the currency has impacted the returns. As of 2013, India has returned $30 billion of the nearly $85 billion total capital invested since 2000. By comparison, China has returned $375 billion out of the $561 billion invested since 2002, a significantly higher proportion. The impact of local factors is felt more strongly on the PE industry, compared to any other sector of the economy, as these factors not only impact portfolio performance, but also impact fund raising. Investor perception for India has been dented and global institutional investors have held back increasing commitments. As a result, fund raising in India is down 73% since 2008, significantly higher than the fall in fund raising of 40% faced by emerging markets during the same period

Strategic Intent : Diversify Across Product Categories

> *"The new funds sought to be raised break new ground for the Company and are steps towards our ambition to build a more global fund house. Developing a diversity of product profile targeting disparate risk appetites, and geographies, has been our focus during 2013"*



Within this dynamic business environment, we continue to be focussed on, and have invested significant time, resources and senior management bandwidth, in raising new funds. With the improvement in business environment, these efforts are expected to fructify during the year. More importantly, the new funds sought to be raised break new ground for the Company and are steps towards our ambition to build a more global fund house. Developing a diversity of product profile - targeting disparate risk appetites, and geographies, has been our focus during 2013

The outcomes have been positive. The Middle East Infrastructure Fund has received encouraging investor response, and the Fund's First Close is expected in the near term. Replication of the Pan Asian investment strategy by way of a follow-on Fund is underway. The underlying strategic intent is to move beyond the Company's positioning as an India-centric fund manager and to take a larger share of the global private investment flows; to work like a global company implementing internationally accepted investment practices but operate locally, with strong on the ground teams. This approach allows us to de-risk our business model and to navigate through these dynamic and difficult markets

On the operational front, during the year, IIML completed investing all its funds. While we will continue to undertake follow-on funding, the teams are largely focussed on working the partners in optimizing value of our investments. During the year the company has invested ₹7.7 billion. These investments have been made with significant levels of due diligence and with quality underwriting. We are confident that in the years to come these will generate exciting returns and add to the strong track record of the company

We also continue to work with a single minded focus on ensuring that assets achieve optimal valuations and time bound exits. Aggregate divestments during fiscal 2013 stood at ₹5.4 billion, and would have been higher had it not been for difficult market situations. Many of our portfolio investments have attained maturity on the back of noteworthy efforts put in by the team in developing these businesses and I believe that this work should come to fruition as markets improve during the year. Getting the timing right and being proactive will be of prime importance as the team continues to ensure quality exits

Private Equity Fund management is a complex fiduciary business which is impacted by a host of extraneous factors. These factors are more ably dealt with, especially in challenging times, by players with a long track record of an on the ground experience. We have, for instance, posted growth in profits during a year, which in fact saw some of our peers shut shop in India. Growth in profits has been also despite our regimented divestment schedule, which in fact reduces our asset under management, and therefore our fees. Our efforts to enhance the product profile continue unabated. We have, in the past, raised and exited funds successfully, despite market conditions. The road ahead to fulfilling our strategic intent is backed by the same capable team, which has, over these years, developed a significant fund management experience. Coupled with your support, we are confident of fulfilling our shared vision

With Regards

Dr. Archana Hingorani
Chief Executive Officer & Executive Director

May 29, 2013

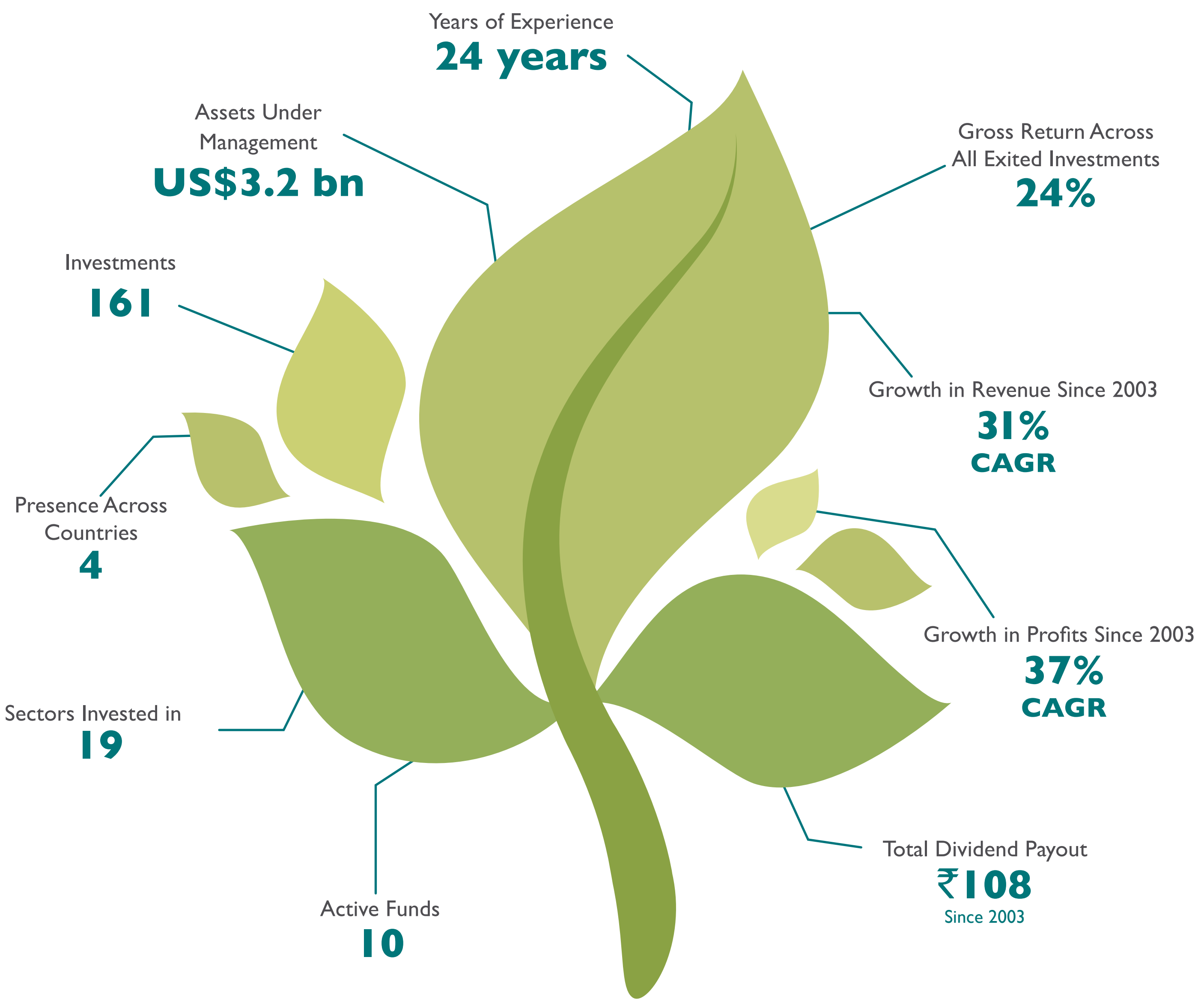
Our Past Experience & Present Offerings
Future Offerings

(₹mn)

	FY2009	FY2010	FY2011	FY2012	FY2013
Total Income	1,642	1,813	2,012	2,247	2,269
Total Operating Cost	578	680	830	1,022	1,258
PBT	846	957	905	953	1,011
PAT	622	738	690	735	767
PAT%	38	41	34	33	34
EPS * (₹)	3.1	3.7	3.4	3.6	3.7
Dividend%**	70	75	75	75	75

** Face Value of ₹2 per share. Adjusted for 1:2 Bonus Issuances in FY2007 and FY2009*

*** % of Face Value of share of ₹2 each*



SEEDING INFRASTRUCTURE INVESTMENTS

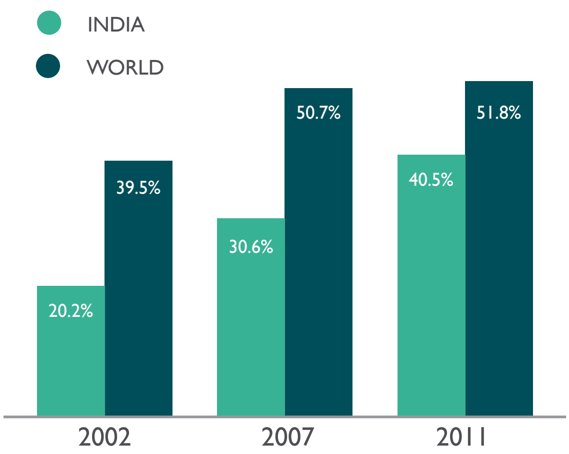
India has 13 major and 187 Minor/Private Ports along its more than 7,500 km long coastline. About 95% of the foreign trade by quantity and 70% by value takes place through these ports

Over the last few years, the Government has announced several policy initiatives to enhance private sector participation in ports

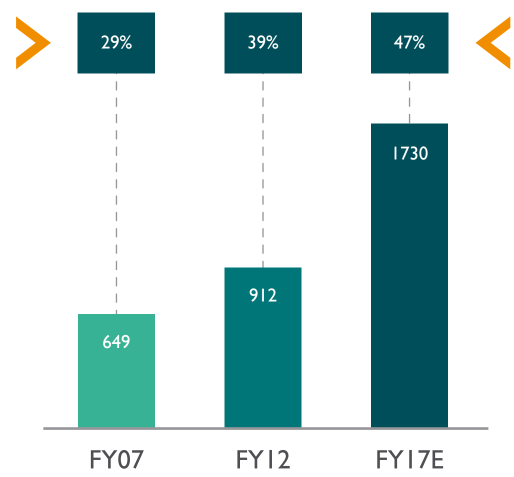
- 100% foreign investment under the automatic route
- Tax break under Section 80 IA
- Allowance to Major Port Trusts to form joint ventures with foreign port operators, Minor Ports and other companies
- Model Concession Agreement

The Maritime Agenda 2020 envisages an investment of ₹3 trillion by 2020 towards development, modernization and expansion of berths (₹1.3 trillion in Major Ports and ₹1.7 trillion in Minor Ports) in a target to develop an aggregate capacity of 3.2 billion tonnes. More than 80% of the investment in Major Ports and 96% of investment in Minor Ports is expected to be undertaken by the Private Sector

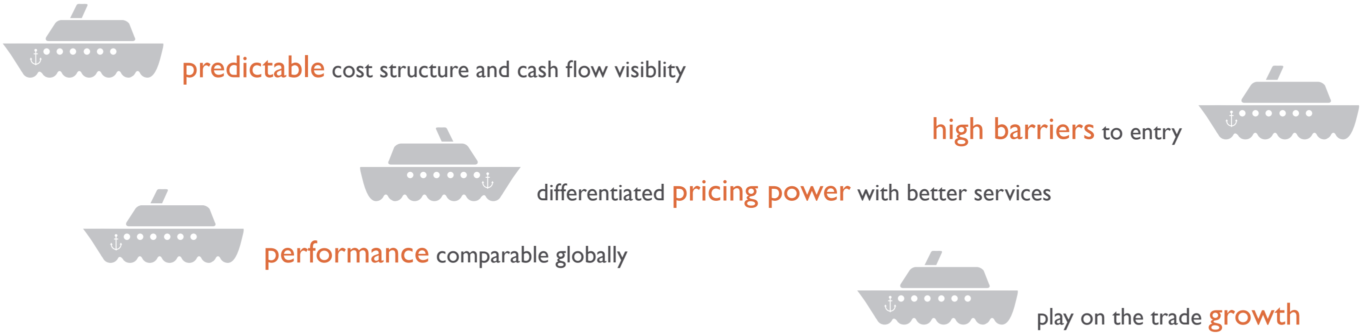
India's Increasing Trade as a % of GDP



Private Ports Capture a Larger Share



Ingredients in Place for an Attractive Asset Class



predictable cost structure and cash flow visiblity

high barriers to entry

differentiated pricing power with better services

performance comparable globally

play on the trade growth