ANNUAL REPORT 2018

Private Equity

IL&FS Investment Managers Limited

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CORPORATE INFORMATION

BOARD OF DIRECTORS	**Mr S M Datta** Chairman **Mr Sunil Mehta** **Ms Shubhalakshmi Panse** **Mr Hari Sankaran** **Mr Vibhav Kapoor** **Mr Ramesh Bawa** Managing Director
CHIEF EXECUTIVE OFFICER	**Mr Krishna Kumar Gangadharan**
CHIEF FINANCIAL OFFICER	**Mr Manoj Borkar**
COMPANY SECRETARY	**Mr Sanjay Mitra**
BANKERS	**HDFC Bank Limited**
STATUTORY AUDITORS	**M/s B S R & Associates LLP** Chartered Accountants
INTERNAL AUDITORS	**M/s Patel & Deodhar** Chartered Accountants
SECRETARIAL AUDITORS	**M/s Mehta & Mehta** Company Secretaries
REGISTRARS & SHARE TRANSFER AGENTS	**Link Intime India Private Limited** C-101, 247 Park, L.B.S. Marg, Vikhroli (West), Mumbai 400 083, India Tel : +91 22 4918 6270 Fax : +91 22 4918 6060
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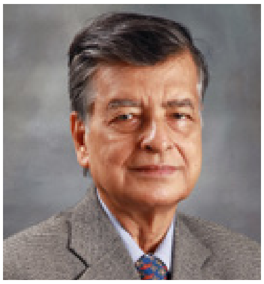

S M Datta
Chairman

CHAIRMAN'S STATEMENT

Dear Shareholders,

The global economy has been posting a strong growth of ~4% p.a. in the recent past, and the expectation has been that this growth trend would sustain. Risk to this growth are however tilted to the downside. Interest rate hikes by the US Federal Reserve and rising crude price is of concern. The rise of protectionism is evident from the tariff increases being enforced, citing unfair commercial practices and rising trade deficit. It is estimated that global gross domestic product growth could take a hit of around one percent if the tariff wars escalate. Needless to add, a global trade war would hit emerging markets the hardest as trade is a key factor in supporting developing economies

In India, growth in the first half of FY2018 was disappointing. The economy has recovered in the fourth quarter of FY2018 and has posted a 7.7% growth rate, enabling the country to retain its position as the fastest growing major economy. A faster pace of growth in manufacturing at 9.1%, compared with 6.1% a year ago, helped lift the overall economic growth during the quarter. The farm sector also grew at a healthy rate of 4.5%, while construction activity, powered by the government investments in the highways sector, clocked a double digit growth of 11.5% to give a fillip to the economy. The World Bank has forecast that the Indian economy will see a robust GDP growth of 7.3% in 2018-19 and 7.5% for the next two years

An environment of strong growth in the country is key to our ability in raising new funds. While we continuously strive to leverage the positive macro-economic conditions in our Fund raise, we also need to be cognizant of the various underlying risks. The banking sector is facing a significant challenge in terms of managing a large portfolio of non-performing loans. This may impact the bank's ability to grow the fresh loan book to the extent required to support the projected growth and investment in the country. In addition, a sustained rise in crude oil prices would curb the fiscal room available to the government to invest in key sectors like infrastructure. Furthermore, the resultant inflationary pressures, in turn, may adversely impact currency stability and also lead to upward movement in the interest rate curve. These factors would have a significant impact on investor and investment appetite

India is also heading into an election year. This will add to the complexity of decision making for the investors. The Private Equity Fund raise and investment environment for the coming year will reflect this uncertainty. The impact would vary across sectors. Certain sectors like consumer-tech, banking, insurance, Information Technology etc. may witness lower unpredictability. In other sectors like infrastructure and real estate, investors may adopt a wait and watch position – not just to see how the macro-economic and political situation pans out, but also to see how effectively the insolvency resolution is implemented across various stressed assets

In this context, your Company is seeking to work on products which either leverage on investor preferences or which effectively address their concerns. As regards the former, the next round expansion of your Company's infrastructure debt platform and the general purpose private equity fund is a case in point. As regards the latter, an infrastructure fund focused on operating assets or a real estate fund investing into yield generating properties can be considered as suitable product offerings

In parallel, your Company has also been focusing on de-risking its India centric business model. Some of the initiatives are beginning to bear fruit. We believe that by the end of this financial year, a meaningful component of revenues would begin to accrue from such offshore ventures of your Company

Many of the above products are being developed in partnership with marquee Institutions. We value these partnerships, and have been investing significant time and resources in nurturing these relationships. Likewise, we value the support and encouragement which you as shareholders have extended to us. We hope for success in building sustainable value for our partners, and foremost our shareholders, during the coming year

With Regards,

S M Datta
Chairman

July 5, 2018

"India is also heading into an election year. This will add to the complexity of decision making for the investors. The Private Equity Fund raise and investment environment for the coming year will reflect this uncertainty. The impact would vary across sectors"

Ramesh Bawa
Managing Director

FROM THE OFFICE OF THE MANAGING DIRECTOR

Dear Shareholders,

The economic deceleration during the first half of FY2018 had generated worried commentaries about India's growth potential. However, the Indian economy has reclaimed the status of the fastest growing major economy, shedding concerns over disruptive reforms such as Demonetisation and the Goods and Services Tax. Despite fluctuations in the GDP growth, India's long-term trend shows a stable, resilient and diverse economic growth. Economic indicators such as Fiscal Deficit, Current Account Deficit and Inflation remain within acceptable limits. Further, continued reforms led to India's improved rank in the World Bank's 'ease of doing business' category. India moved up 30 places in this ranking, and is now among the top 100 countries. The improvement in the overall economic environment resulted in Moody's upgrade of India's sovereign rating for the first time in 14 years

However, there are global headwinds from rising crude prices and potential fallout of the recent tariff wars. These developments may impact our currency stability and inflation targeting. Consequent adverse impact on interest rates and investments could therefore pose challenges to improving on the current growth levels

As we move forward into FY2019, sustaining growth levels of ~7.5% would depend on a host of factors. The growth would need to be broad-based, covering agriculture and industrial sectors. Measures to reversing the slowdown in investment, credit supply and exports would be key to achieving this year's growth target. To this end, the issues facing the banking sector would need to get addressed expeditiously

From a private equity perspective, investor interest in India was one of cautious optimism. Alternative Investment Funds (AIFs) have more than doubled in the last couple of years. There are now ~350 AIFs registered with the Securities and Exchange Board of India. These AIFs have raised ~US$ 5 bn in 2017, reflecting a significant growth over the previous year. Investments into distressed assets also gained momentum. Institutionalisation of the Insolvency and Bankruptcy Code has streamlined resolution of distressed assets

The Private Equity funds in India have a significant amount of deployable capital or 'dry powder' at their disposal, estimated at US$ 9 billion. However, the investment preference for this available capital is skewed in terms of target sectors. Consumer tech and Banking, Financial Services and Insurance segments were the largest sources of investment in India during 2017, aggregating to more than 50% of the entire deal value for the year. Deals in the manufacturing sector witnessed a decline during 2017. While both the infrastructure and real estate sectors attracted capital, the same was focused on operating and yield generating assets. Capital for new asset creation was largely targeted at the renewable energy sector, where shorter project development cycle and strong payment security mechanisms provide comfort to investors

Given these strong investor preferences, we have accordingly fine-tuned our product strategy. For instance, in the infrastructure space, we are defined in greater detail the sector which we would be targeting and the stage of such investments. Keeping in mind the preference for stable, visible yield income, we have pressed ahead in expanding our infrastructure debt funds. Consumer tech and other socially relevant sectors are already being targeted by our 4th generation private equity fund. We plan to fully deploy this fund during the course of the current year and thereafter start the process of raising a fresh fund

During the financial year 2018, we were successful in cementing a new and complementary aspect of our strategy. In January 2018 we signed a joint venture agreement with the Islamic Corporation for the Development of the Private Sector (ICD) for establishing a US$ 1 billion fund focused on providing shariah compliant infrastructure debt finance to projects in Africa. ICD is a multilateral development financial institution and is part of the Islamic Development Bank Group. This partnership provides a unique positioning to the Fund in targeting investments in this new frontier for your Company. The Fund has already raised over US$ 200 million and is expected to attain First Close shortly. Another interesting strategic development has been the establishment of a joint venture with Government of Andhra Pradesh to set-up an urban infrastructure fund. The Government has committed ₹ 1 billion to this Fund. Fund raise from domestic and international investor is now underway

The above mentioned initiatives have the potential of adding significant value to your Company going forward. As is the case with most strategic initiatives, the effect of these new products on the financial performance of your Company would only reflect with a lag. In the interim, the fund under management have been depleting on account of the divestments being undertaken from the existing funds. Consequently, fee income from these

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funds has fallen. In order to maintain profitability, we have sought to negate the fall in fee income by way of cost reductions, which have largely been implemented by way of manpower rationalization

As we move forward in reorienting our strategy and bringing into play new product themes, it would be important to nurture and encourage the management team in overcoming the various challenges which are a natural part of such an effort. In this, we have the strength of the IL&FS Group, more particularly that of the financial services group of IL&FS, to draw upon. With this strong institutional backing and your encouragement and support, we are confident that we will emerge at the forefront of industry thought leadership, product innovation and value creation in the coming time

With Regards,

Ramesh Bawa
Managing Director

July 6, 2018

CORPORATE SOCIAL

RESPONSIBILITY PROGRAMME

In FY2018, IL&FS Investment Managers (IIML) provided a grant of ₹ 10.7 mn towards a healthcare programme in rural Maharashtra, educational initiatives in and around Mumbai, a pan India Skill Development Programme and a mentorship programme for women entrepreneurs

Skill Development Programme : The objective of the skill development programme is to provide gainful employment to urban unemployed and population below the poverty line. IIML supported a pan India skill development programme providing training to beneficiaries in the 18-35 years age group. Eligible beneficiaries include minimally educated people in the age group of 18-35 years, urban poor, women, persons with disabilities, disaster/ project affected people and those not covered under any government schemes. In the current year 2,300 candidates were trained and 1,600 obtained employment upto April 2018. Top sectors for placements include automotive, construction, retail and apparels

Educational Initiatives - Masoom : Masoom works with 60 night schools across Mumbai to improve the quality of education. In the current year, IIML supported 2 educational institutes - Vidya Vikas Night School, Ghatkopar and Sharda Night School, Vikhroli. Around 150 students were supported by IIML in these schools. Support by IIML included infrastructure support (books, libraries, laboratories, audio visual learning, nutrition etc), capacity building (training of various stakeholders such as trustees, headmasters, teachers, students, parents and non-teaching staff). The Masoom programme aimed at improved attendance, enrolment and academic performance

Healthcare at Palghar - Mobile Medical Unit (Savali) : The mobile medical unit ("MMU") started operations in January 2016. In the current financial year, the MMU catered to 30 villages covering 10,000 patients - ~74% of diseases diagnosed comprised muscular pain, skin diseases, diarrhoea and common cold. ~50% of diseases were communicable in nature. The gender mix comprises women (44%), men (25%) and children (31%). A deeper analysis revealed that the root cause of most diseases were drinking water and nutrition issues. Consequently, Savali has installed water purifiers on a pilot basis in 4 locations. Additionally, discussions have been held with IIT Center for Technology Alternatives for Rural Areas to resolve these issues

Introduction to Basic Technology (IBT) – (Savali)
The IBT programme was initiated in FY2016 and is being implemented in 5 schools in Maharashtra (Jawhar, Kudal, Murbad, Pune and Sindhudurg) covering 760 students. Students are being trained in Engineering, Agriculture, Energy & Environment and Health & Home science. In FY2018, IIML continued its support of operating expenses in the 5 schools. The children participated in various activities during the year including preparing models of rainwater harvesting, cropping using coco-peat, cloth bag making, making stools for schools, repair of school infrastructure etc.

Entrepreneurship Programme : A mentorship programme was carried out with 30 high achieving women entrepreneurs. The key features included :

- Annual turnover enhanced from ₹ 6.5 mn to ₹ 16 mn
- Loans aggregating ₹ 1.4 mn were availed by the women in the current year
- These women contribute ~60% of the family income

These entrepreneurs will be monitored in FY2019 for further progress

FINANCIAL STATEMENTS

(₹ mn)

Particulars	FY2014	FY2015	FY2016	FY2017	FY2018
Total Income	2,229	2,087	1,908	1,151	1,226
Total Expenses	1,222	1,122	1,160	1,013	1,012
PBT	1,007	965	748	139	214
PAT after MI	725	730	561	61	66
PAT (%)	33	35	29	5	5
EPS * (INR)	2.3	2.3	1.8	0.2	0.2

* Face Value of ₹ 2 per share