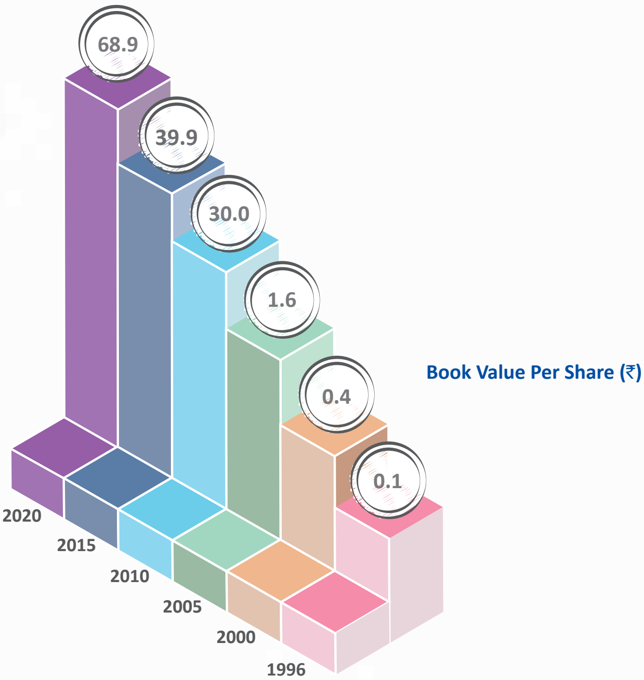
Chairman's Letter 2020

Edelweiss
Ideas create, values protect

Chairman's Letter



As I sit and pen down this letter, I have spent the best part of the last five months inside my house practising social distancing – undoubtedly the word of the year 2020. I do not think this is a sentence with which I expected to start the letter marking 25 years of Edelweiss. But there are many things which we did not expect but are the reality today. We're living in a very different world to what it was a few months back. Clearly, we live in unprecedented times.

Living and Working in Unprecedented Times

Covid-19 continues to grow rapidly in many parts of the world, including India. I do hope that we find a vaccine soon; there are positive indications emanating from multiple directions. Covid-19 is a reality which we must accept and move on and the sooner we find a way to cure it, the better it will be for mankind. In the meanwhile, I do hope that we can minimise the number of cases by adhering to the required precautions. At Edelweiss, we continue to pray for the quick and speedy recovery of all those afflicted by Covid-19.

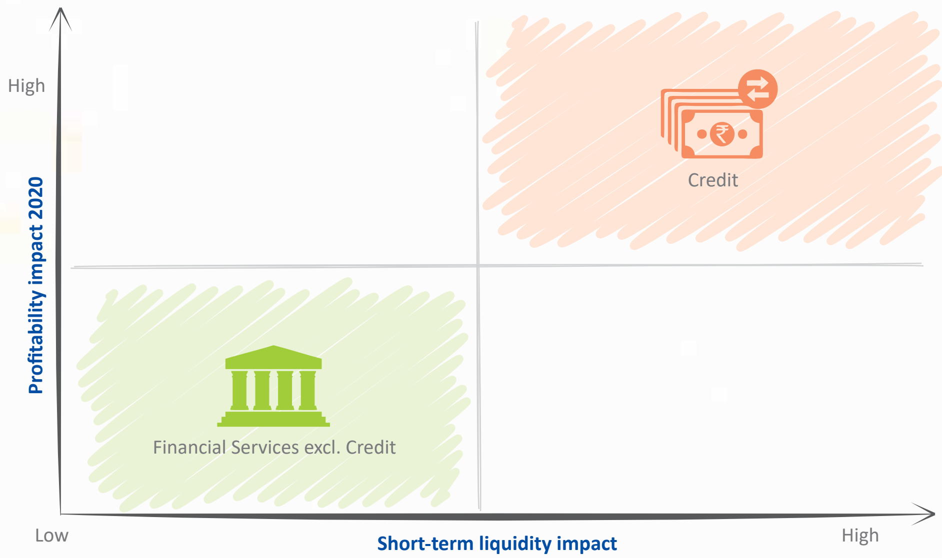
I also want to take a moment here to applaud the superheroes of this fight against Covid-19. All the doctors, nurses, medical staff, policemen, municipality workers, social workers and field staff of NGOs (and even our branch staff!), amongst others. They have been out there fighting so that the vast majority of us can stay safe and comfortable. Their actions are truly reflective of the resilience and determination of the human race – a spirit that shines through in the toughest of times.

It is under the greatest adversity that there exists the greatest potential for doing good, both for oneself and others

— His Holiness, The Dalai Lama

These unprecedented times have also created an unprecedented situation for businesses across the country. As we went into lockdown mode in the last week of March, the entire business machinery in the country came to a jarring halt, which continued through April. This was reflected in the numbers as well – zero car sales in April, Services PMI in single digits, capacity utilisation at historical lows, the examples are innumerable. This has impacted, in near term, both the profitability as well as the liquidity situation for businesses across sectors, irrespective of their size: small *kirana* shops, mid-sized enterprises or large conglomerates. Within Financial Services, except Credit, most businesses were impacted to a much lesser extent.

Financial Services (ex-Credit) unimpacted



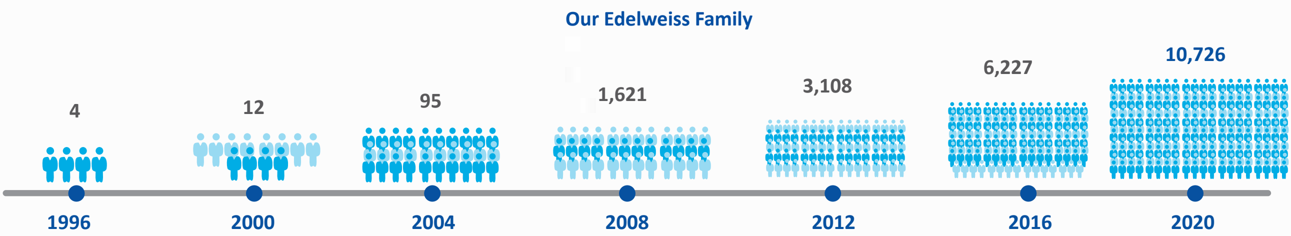
However, we have been in gradual unlock mode for a couple of months now and businesses are starting to inch bank to normalcy. Government and Regulators' relief measures have gone a long way in helping manage the liquidity crunch which was exacerbated by Covid-19. While it will take time for complete normalcy to return, we are now well and truly on the slow road to recovery which will be helped by the resilience that is unique to our country. In fact, our country's ability to recover from shocks and come back with twice the strength often reminds me one of my favourite quotes from the movie Rocky –

It ain't about how hard you hit. It's about how hard you can get hit and keep moving forward. That's how winning is done!

— Rocky Balboa

Last 25 vs Next 25 – Our journey

Someone recently asked me to put my Edelweiss journey of 25 years into one word and the first thought that came to my mind was 'fulfilling'. It has been a rollercoaster ride but I have thoroughly enjoyed every moment of it. We started out by creating a business which could help companies raise money but along the way, metamorphosed into a family which is helping fulfil the dreams and aspiration of millions of Indians, be it the small entrepreneur looking for SME loans, the homebuyer looking for home loans, the aspirational Indian looking for wealth and asset management services or the risk-conscious Indian looking to buy life and general insurance policies for himself and his family. But most importantly, we focused on fulfilling and help achieving the dreams and aspirations of the 10,000+ members of the Edelweiss family. They are the ones who have helped create the Edelweiss Group as it stands today, and it is to them that we owe everything that we have achieved in our 25-year journey.



Over this journey, our sole focus was on building quality. As Rajesh Khanna's character says in the 1971 film Anand,

Babu moshai... zindagi badi honi chahiye, lambi nahi...

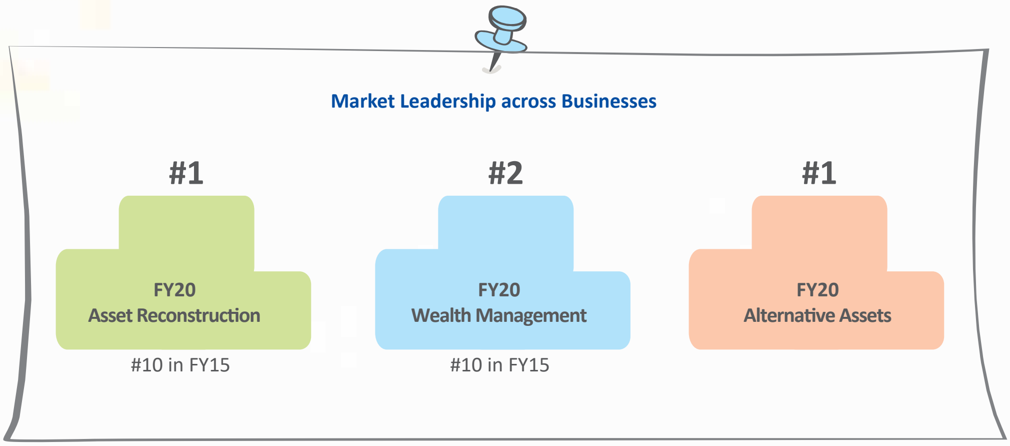
So, we focus on building quality in everything we do. That we have finished 25 years and are still going strong is purely incidental. In this journey, we have together achieved some truly remarkable things which give me immense pride –

- Starting from a capital base of only ₹10 million, created value of more than ₹80 billion
- Created an organisation which built its own unique ethos and principles centred around creating value for employees, customers and shareholders
- Created from scratch, multiple businesses, which we will touch upon in the subsequent section and built each of them to scale and even market leadership in their segments. Each of these businesses today have significant value unto themselves which will get truly reflected as these businesses chart their journey of independence – Edelweiss Wealth Management (EWM) has already launched into this journey with the partnership we have announced with PAG recently for an investment of ~₹22 billion for 51% stake in EWM
- Nurtured a family of more than 10,000 people supporting almost 2,000,000 clients in its journey with the sole focus on providing maximum satisfaction to both these employees and clients
- Established EdelGive Foundation in 2008, which has touched the lives of innumerable Indians in its 12-year journey, culminating in winning the National CSR Award last year

Did we achieve everything we set out to? In a way, yes and in a way, no. When we started out, we could never have imagined that 25 years hence we would be an organisation with more than 10,000 members spanning across the country. What our people have helped us achieve is far more than we could have ever envisaged. There is a lot more that we could have potentially achieved and which we will continue to work towards – this is what we intend to make our target for the next 25 years.

- **Market Leadership**

  Businesses like Wealth Management and Asset Management are the ones where we have built up market leadership over time. As we look at the next 25 years, not only do we want to maintain this leadership, we will look to incrementally capture market share and enhance our lead at the top of the pile. Global partners like PAG will play a significant role in this journey with their experience, expertise and ability to open new doors of opportunity. In our experience, in these businesses especially, size begets size and we do believe that with our strong platform, we can create an everlasting legacy.



- **Sizeable Presence**

  Businesses like Retail Credit, Life Insurance and General Insurance are the ones where the incumbents are significantly big and we are late to the party, so to say. But being late to the party has one advantage, which is going to be even more relevant in the post Covid-19 world.

  Newer retail businesses like ours have found it easier and more convenient to adapt to new technologies that are going to be the foundation for the future. Businesses like General Insurance, in fact, are meant to be pure-play tech businesses, our in-house Fintech businesses, so to speak!

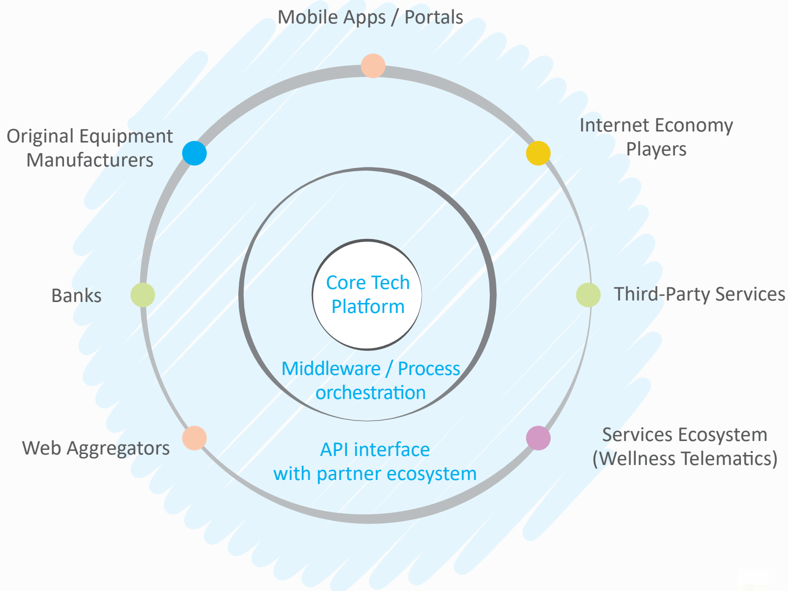
  With technology as the backbone, we expect to scale up these businesses substantially and reach a larger section of the population in the years to come. So while twenty five years down the line, we might not be market leaders in these businesses (or we could be, disruption is real!), we do hope to be amongst the bigger players in the industry, building on technology as a base to innovate and simultaneously putting customer experience at the forefront of all our endeavours.

- **Digital Financial Services Organisation**

  The world today is changing faster than it ever has. The impact of technology has been multiplied manifold in the Covid-19 era and has accelerated trends which were anyway gravitating towards a digital world. Organisations have three options – adapt to this change with time, react too slowly or not change at all. History has not been too kind to the last two categories, and it is imperative that we not only adapt to this change but become part of the change itself.

As mentioned earlier, our retail businesses will use technology as the backbone to what will eventually be a digital financial services organisation. In fact, some businesses like General Insurance, owing to their recency, are far ahead of the curve. Our General Insurance business has already established a fully integrated digital operating platform which has outperformed peers in the lockdown period (fastest growing private General Insurance player in Q1FY21!), as the lower dependency on physical interactions and higher use of technology helped ensure uninterrupted business flow. Our General Insurance business, in fact, is the first cloud native platform in this business, as well as the first to implement a SAP insurance suite in India. Going forward, our vision is to replicate the General Insurance model across all our retail businesses and to become a tech-first organisation, rather than only a tech-enabled one.

Fully integrated digital platform in General Insurance



While we hold these three objectives to core as we focus on our businesses going forward, the foremost objectives, as they remain today, will be to delight and enable our customers, ensure that we continue to support and grow our employees and continually enhance and unlock value for our stakeholders.

Diversified FS Organisation – Building Quality Mono-lines

We started Edelweiss in 1995 – a journey of 25 years with its fair share of ups and downs, thankfully more ups than downs. All through this ride, the intention was always the same, to start businesses in adjacent lines, nurture them in their initial years to build a solid foundation and then scale up once their foundations were established, helping create long-term value for shareholders. Edelweiss is like a family and even within a family, you take care of your kids when they are young, provide them with the right education and values till they are ready to go out and conquer the world. Our businesses are like our children. We have nurtured and strengthened them over the years, so that they are ready to face the world when the time comes. This has been core to our philosophy over the years and will continue to be key to how we operate going forward as well – build a diversified financial services business with quality mono-lines within it, each with the intention of creating shareholder value in the long-term.

Each of our businesses has charted its own journey since the beginning. We have, of course, provided the necessary resources and guidance, where required. But, as and when the need has arisen, we have also taken the decision to enlist people who can take the business to the next level. Take a daughter who excels in basketball, for example. The first lessons begin at home but there will eventually come a time where you might need to engage special coaches to take her skill to the next level. Similarly, we have also engaged and enlisted help from capable partners, as and when required.

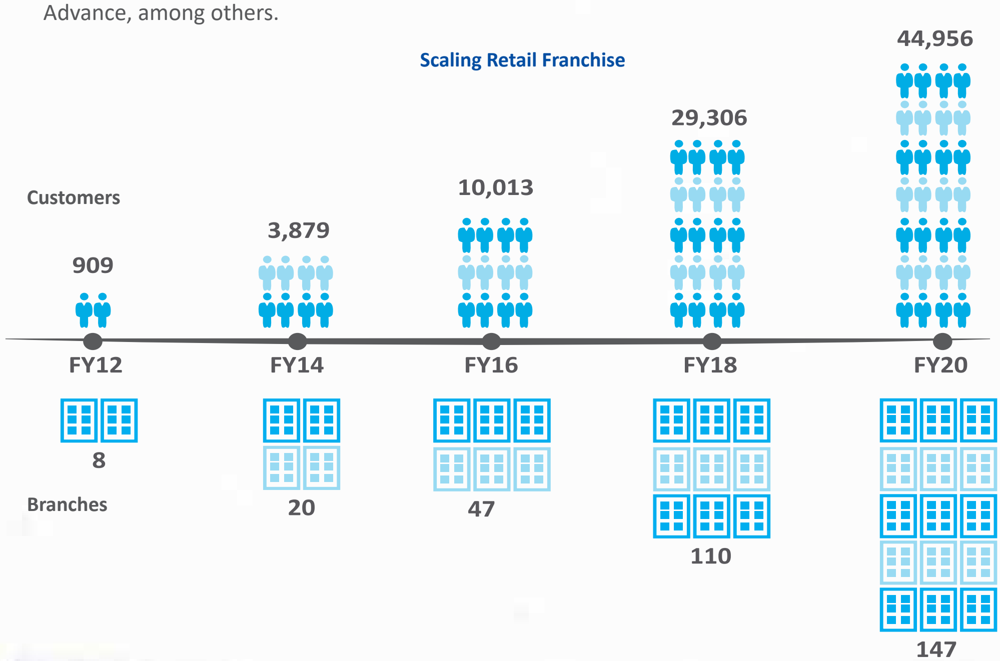
Each business is unique and has therefore seen this need arise at different points in its lifecycle. In Life Insurance, for example, we partnered with Tokio Marine early on in our journey – while the opportunity in the life insurance sector in India was obvious, we were also cognisant of the long gestation period of the business and hence the need to have a partner who can help accelerate the learning curve and our ability to create a strong, sustainable business. On the other hand, a business like Asset Reconstruction Company (ARC) had been fairly self-sufficient in its initial years and it was only after we had established a strong vintage and track record that we partnered with CDPQ, which helped open new vistas for the ARC business.

Similarly, our wealth management business today is at an inflection point. Being one of the largest wealth managers in India, our quality, pedigree and business acumen is well-established. The runway for the wealth management business in India is incredible and the recent disruption is an opportunity to capture even higher market share. We feel that we will be able to better capture this opportunity with a partner who will not only bring in the experience of global markets, where the industry is much more well-developed, but also provide a brand name which can open up windows which were hitherto restricted. To this effect, we have partnered with PAG, who will be buying 51% stake in our wealth management business, marking the onset of a new era in our wealth management journey. Most importantly, as we eventually undertake demerger and listing of the business, it will help us truly unlock shareholder value which will be more accretive than what it has been before.

Each of our mono-lines has had their own unique growth journey -

1. Retail Credit

Our retail credit journey started in 2011 with the launch of our Home Loan product. We gradually scaled this up to build a mortgages portfolio consisting of home loans (both prime and affordable) as well as Loan against Property (LAP). In addition, we also started our journey in SME Finance the year after and have since expanded to multiple products including Business Loans, SME LAP and Salary Advance, among others.



The retail portfolio has remained largely flat over the last two years, owing to the slowdown after September 2018 and a conscious focus on preserving liquidity and not scaling the book in such volatile times. Today, we are well-capitalised with Capital Adequacy ratio in excess of 25% and ready to scale, once the environment stabilises. In parallel, we are focused on further improving our business backbone and making it ready for growth. To this effect, our main priorities are –

- Use lockdown experience to improve cost efficiencies and productivity
- Focus on completing buildout of tech and analytics led platform
- Collaboration with Banks – Co-lending, On-lending and Securitisation

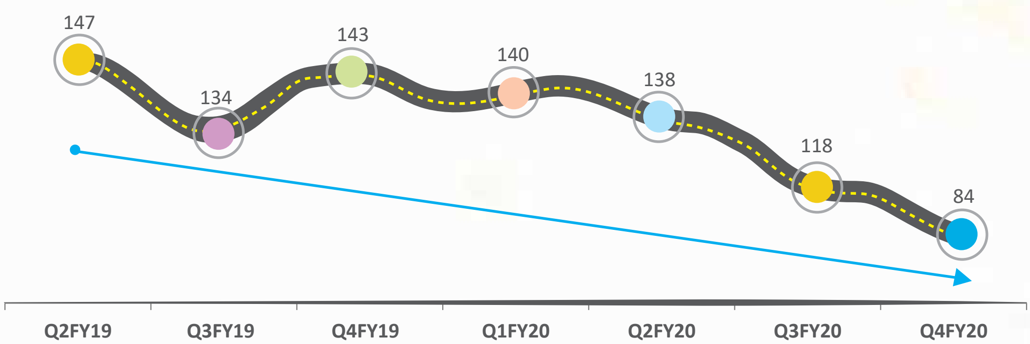
Bottomline – Well-capitalised, focused on technology and ready to scale once the environment stabilises.

2. Wholesale Credit

We launched our Wholesale Credit business in 2007. As luck would have it, this was right before the Lehman event happened and the Global Financial Crisis struck. It was a tough time for everyone, but we managed to navigate the challenges. We expanded into both Structured Credit as well as Real Estate Finance, once the market started normalising. Over the next few years, we gradually scaled up the book on both Structured Credit and Real Estate Credit side. However, one of our key learnings from running this business has been the uncertainty and vagaries associated with bespoke credit. This meant that, while it will continue to be a profitable business, the volatility in timing of cash flows, owing to short-term market dislocations, meant that this business is not well-suited to run within an NBFC structure.

With this learning and a strong asset management franchise, we have actively focused on reducing our on-balance Wholesale Credit portfolio worked towards moving this into the Asset Management structure. As we expedite the sell-down to release equity, we will continue to focus on preserving asset quality, going forward.

ECLF Wholesale Credit book (₹ billion)

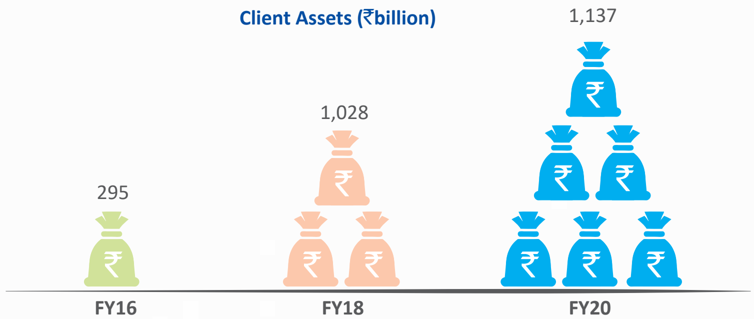


Bottomline – Focused on rapidly scaling down the book through organic repayments and movement into fund management structure to release equity and liquidity.

3. Wealth Management

We started our wealth management business, for all practical purposes, with the acquisition of Rooshnil Securities for only ₹80 million in the early 2000s. Since then, it has been a journey of inorganic growth burnished by the acquisition of Anagram in 2011. We were always focused on building a business which was not reliant solely on broking income, but was focused on creating an all-encompassing wealth management platform, be it broking, advisory services, distribution or funding in the form of Loan Against Securities (LAS) and ESOP. The business has seen strong growth in the last five years and today, we are one of India's leading wealth management players.

As we announced a few days back, we have entered into a partnership with PAG under which they will invest ~₹22 billion for 51% stake in EWM. The wealth management business is at an inflection point and we feel that with the immense scope for growth going forward, a marquee name like PAG would help elevate the business to the next level. This is also in line with our business strategy of building businesses to scale and then taking the requisite steps to help them achieve the next level in their growth, while unlocking shareholder value

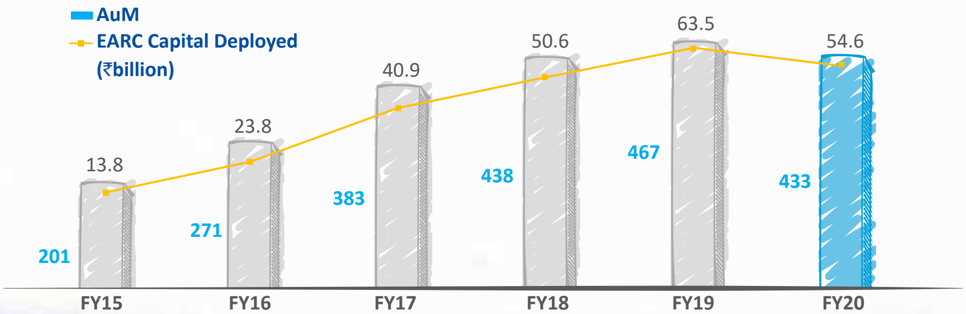


Bottomline – Commencement of a new phase in growth trajectory to create India's leading wealth management player.

4. Asset Management

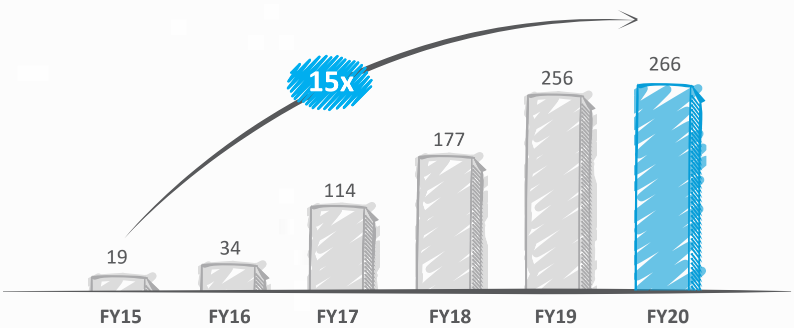
Our Asset Management (AM) business consists of Retail AM including our Asset Management Company (AMC), Public Market Alternatives and Institutional AM, including ARC and Private Credit funds. This business has also been a long vintage business for us, which marked its sunrise with the launch of Edelweiss Asset Reconstruction Company (EARC) in 2008 and the setting up of our AMC, as well as our Private Credit funds in quick succession.

EARC was set up with a view to create a specialised vehicle focused solely on stressed assets and in extracting value from them, be it through turnaround, restructuring or eventual liquidation. The real growth in Edelweiss ARC came from FY13 onwards, when it moved from an Assets under Management of only ₹3.7 billion to more than ₹90 billion by FY14 and then more than ₹200 billion by FY15. This growth trajectory has since continued, and we are today India's largest ARC with 50% market share. Significant resolutions and repayments in FY20 have led to some reduction in AuM and Capital Deployed.

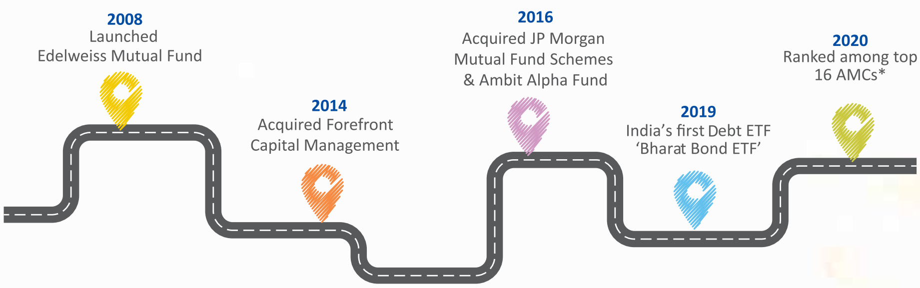


The Private Credit journey started at almost the same time with a small Special Opportunities fund nearly ten years ago, supported by a few Swedish pension funds. Today, we have Assets under Management of more than ₹210 billion across multiple private credit alternatives funds (and an additional ~₹50 billion in Public Market Alternatives), supported by marquee global investors. Along with our Retail Alternative funds, our total AuM in Alternatives is more than ₹260 billion. We have seen strong growth traction in our funds and are in the process of closing the third series of our Special Opportunities fund, which will significantly enhance this AuM by more than ₹60 billion very soon.

Edelweiss Alternatives AuM (₹billion)



Today, we run four key strategies across Special Opportunities, Real Estate, Infrastructure and Distressed Credit and have built a successful track record over a decade, including early success in the Infra fund. We will continue to make these four strategies the keystone of our Private Credit business going forward and continue to raise follow-on funds across these strategies. In parallel, we will also continue to gradually shift our on-book wholesale credit to a fund management structure, supported by the strength of our Institutional Asset Management business.



**Data as on June 30, 2020*

Our AMC was started in 2008 but started acquiring momentum from 2014, when we acquired Forefront. Not only did Forefront give a kickstart to our Retail Alternatives business, it also gave us the current CEO of our AMC! In that sense, the acquisition of Forefront was a turning point in our Retail AM journey. Today, we have grown by leaps and bounds and are the 16th largest (as on June 30, 2020) in the country. We have already closed two tranches of India's first Debt ETF, Bharat Bond, with considerable success, with more on the anvil. As it stands, we have Assets under Management of about ₹360 billion as of July. While this is a significant scale-up from where we were four years back (sub ₹50 billion), we feel that there is still room for a lot of growth with the growing financialisation that we are seeing in India and a growing focus on passives – both on the debt and equity side, which we hope to excel in. While the journey from rank 36 to rank 16 in four years has been a challenging one, the next stage of the journey will be even more challenging as we aspire to break into the top-10 of a hallowed club. However, we do believe that we have the right leadership and the right ethos in place to accelerate and move up another gear in this journey.

Bottomline – Focus on continued market leadership in Alternatives and building scale in our AMC through leadership in equity and debt passives.

5. Life Insurance

Our Life Insurance business was started in 2011. While we took some time establishing the business base, which has been our established strategy, our growth since 2016 has been nothing short of phenomenal. This has been on the back of strong strategic support from our partner, Tokio Marine, as well as the availability of resources to expand rapidly once a sustainable business model was established.

The focus in the business has been around building a quality, long-term franchise which can sustain not only any short-term internal hiccups, but also any interim slowdown in the overall market as well. This has been tested and validated, especially in the current Covid-19-induced lockdown, where our growth has far exceeded industry players (we were the second fastest growing player in the industry in Q1FY21!). This has been on the back of our technology backbone, as well as the strong connect we have built with our workforce as well as customers, which has helped sustain this phenomenal growth even today and for the foreseeable future.

Annualised Premium Equivalent

24% CAGR increase

₹3.23 billion

(₹1.38 billion FY16)

Gross Premium

36% CAGR increase

₹10.48 billion

(₹3.1 billion FY16)

Assets under Management

52% CAGR increase

₹27.07 billion

(₹5.11 billion FY16)

Value of New Business Margin

38%

(24% FY16)

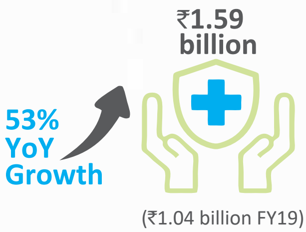
Bottomline – Focus on growth through digitisation and journey towards profitability leveraging support and experience of global partner.

6. General Insurance

Our General Insurance business is the newest business in our 25-year journey to building quality mono-lines within the Edelweiss fold. With General Insurance, we have taken a route which defines the need of the times. Edelweiss General Insurance is our in-house fintech business relying on technology as the core of the business and developing all other functions as adjunct to the core technology piece.

Similar to the Life Insurance business, the General Insurance business is based on a model which can withstand external shocks to the system, especially with its completely digital foundations and non-reliance on physical interactions. While the vintage for General Insurance is obviously much shorter compared to our other businesses, the performance chart is already reflecting the business potential. And this will only get burnished in the current year as shown in Q1FY21, where Edelweiss General Insurance was the fastest growing private general insurance company in India, truly a phenomenal achievement for a 2-year-old upstart!

Gross Written Premium



Bottomline – Establish a leading fin-tech business focused on cost efficiency – best of both worlds!

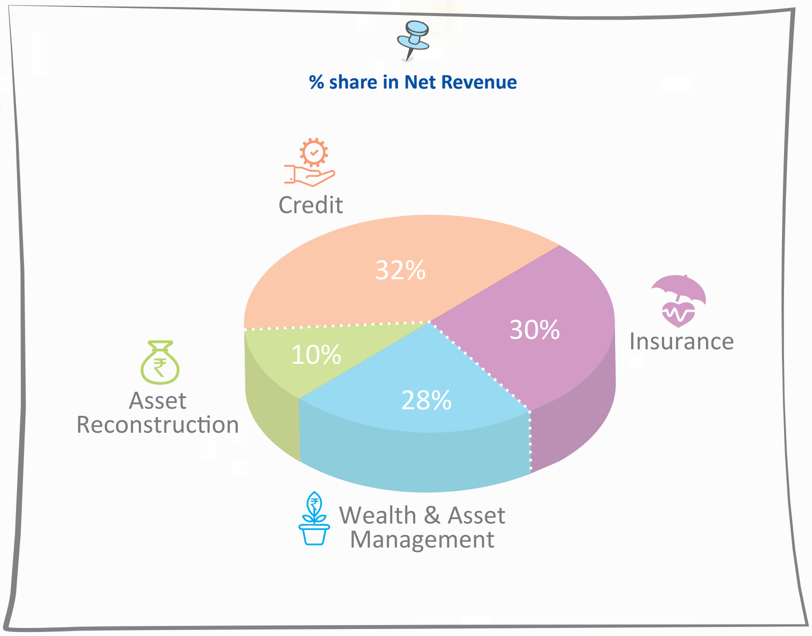
FY20 overview

A challenging time for the NBFC industry since September 2018 was further precipitated by the Covid-19 crisis. The last two years have seen the industry focus more and more on managing liquidity than on growth. As the overall economic environment took a turn for the worse, especially for Credit, even in the time preceding Covid-19, we initiated a detailed review of our Expected Credit Loss (ECL) model, both internally and with an independent international consulting firm. At the same time, the lockdown meant that business fundamentals were further impacted. With all these factors, we took the decision to be conservative on the Credit side and hence took a substantial impairment on our Credit portfolio. However, this was to some extent buffered by the diversified business model we have gradually built over the last decade, as businesses like Wealth Management, Asset Management and ARC continued to show good profitability and the Life Insurance and General Insurance businesses continued to focus on long-term value creation. These broadly were the key underlying themes of our results in FY20.

1. Diversified Business Model

One of the key tenets of the Edelweiss story has been the focus on building a diversified business model which straddles across the financial services sector. This not only helps us benefit from the various themes that drive India's growth story – financialisation of savings and democratisation of credit – but also helps us manage uncertainty and volatility in a specific part of the business.

While the overall environment has been challenging for the Credit business, other businesses have continued to outperform. As of FY20, our revenue streams are well-diversified with ~30% of the Net Revenue coming from Credit, Wealth & Asset Management and Insurance each.



2. Conservative Impairment

As mentioned before, we adopted a conservative stance on impairments overall. We took a total impairment of about ₹26.24 billion in Q4FY20 which was an outcome of three factors –

- Estimated impairment after revision of Expected Credit Loss model of ~₹12 billion
- Additional impairment taken to facilitate sell-down of ~₹5 billion
- Impairment taken on account of Covid-19 of ~₹9 billion

While the Covid-19 impact is playing out as we speak, we felt it was imperative that we took a pre-emptive provision on the same in Q4FY20 itself. The additional impairment of ~₹5 billion is to ensure that we can continue on the strong movement we have seen in the reduction of our wholesale credit exposure and quickly scale down the book to release equity.

3. Wholesale Book Reduction

As mentioned earlier, we continued to see good traction even in FY20 on our stated objective of reduction in our Wholesale Credit book. This was enabled by organic repayments as well as asset sell-down transactions like the Real Estate completion financing platform with Meritz. We have also finalised some more sell-down transactions which should lead to a further reduction in the wholesale book.

In fact, in the last eighteen months since ILFS, ECL Finance's wholesale loan book has come down by 43%, across both structured credit as well as real estate financing. We intend to take this number to zero by FY22.

4. Strengthening Capital Base

Through the year, we have focused on strengthening our capital base through both reduction in credit book as well as raising equity capital. We raised equity in both Credit and Wealth & Asset Management businesses with EWM being the most recent capital raise exercise. This has helped us maintain healthy capital adequacy across businesses, even after the impairments we have taken in Q4FY20.

Entity	Capital Adequacy Ratio
ECL Finance Ltd	21.0%
Edelweiss Retail Finance Ltd	29.4%
Edelweiss Housing Finance Ltd	28.6%
Edelweiss Asset Reconstruction Company Ltd	32.5%

Entity	Solvency Ratio
Edelweiss Tokio Life Insurance Ltd	232%
Edelweiss General Insurance Company Ltd	236%

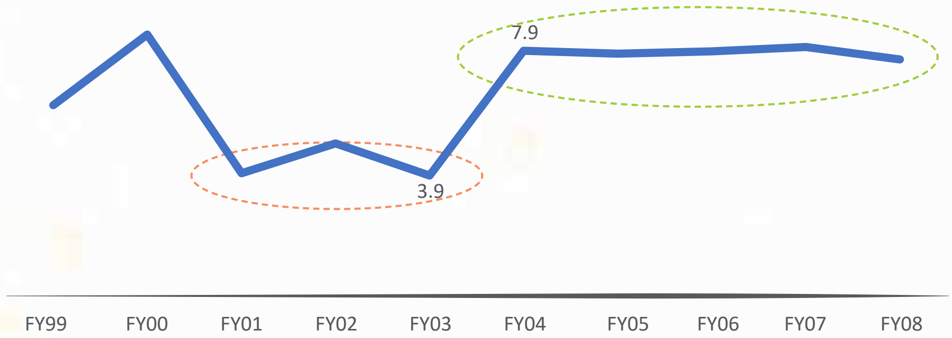
FY20 has been a year of consolidation as the overall economic environment and the Covid-19 onset meant that the focus was on strengthening the core rather than actively going for growth. FY21 will be similar with the focus on building on the successes in FY20 to further create an even stronger structural base. This will help us get back on the growth trajectory in FY22, once the economy is back on track and secular growth opportunities are available across all businesses.

Deja 'View' – 1998:2003:: 2015:2021?

One of the key questions that is on everyone's mind right now is when can we expect the economy to regain its heydays of growth and glory. To make even a calculated estimate on this, we must realise that the Indian economy swings in cycles; we have seen this over multiple decades. Often, every slowdown cycle is followed by an exponential growth cycle and vice versa. It therefore makes sense to study the past as a guide towards the future. While all of it may not get replicated in its entirety, there are enough indications for a broad guidance into what the future could possibly look like. With that context, the period between 1998 and 2003 is an interesting study, especially because that phase is strikingly similar to what we have seen panning out in the last five-six years.

1997 saw the onset of the Asian Financial Crisis. While India was relatively unimpacted, the after-affects were showing up in the economy, eventually culminating in a sharp fall in Gross Domestic Product (GDP) in line with the global slowdown, post the tech bubble burst. GDP growth fell sharply and remained at those levels for a few years after which it again rose sharply, reiterating the cyclical growth story of the Indian economy!

GDP Growth (%)



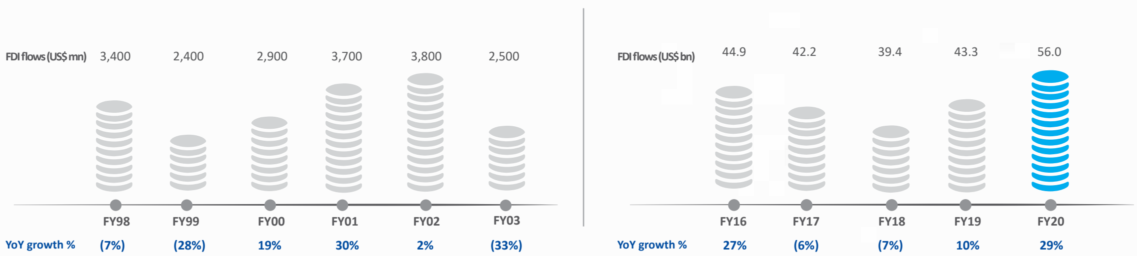
If we compare the period from 1998 to 2003 and then 2015 to 2020, there is an uncanny resemblance between the two periods –

Real Estate

Then	Now
Real Estate prices had fallen dramatically in India in the late 90s – by as much as 50%!	Real Estate prices have started seeing corrections and have already moved as much as 20% in the last one year

FDI flows

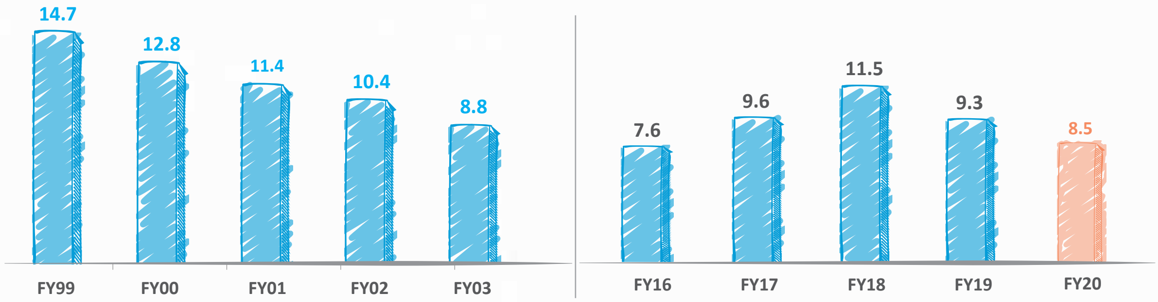
Then	Now
FDI flows de-grew in some interim years, especially after the global tech bubble burst	Even from 2016 onwards, flows into India have been trending mostly flattish with a minor spike in FY20



Gross NPAs

Then	Now
Gross NPAs were at very high levels but had started trending downwards	Gross NPAs were at record highs again but have started trending downwards

Gross NPAs for SCBs (%)



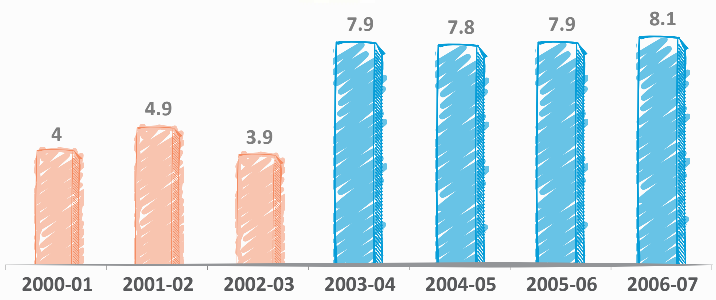
And the government response was also quite similar then as it is now...

- Sharp increase in Public Sector Undertaking (PSU) divestment at that time; is similar to government plans to divest significant stakes in PSU enterprises, be it the plan to sell Air India or to list LIC
- Significant rate cuts were effected then as have been done now
- Strong policy measures to infuse liquidity into the system were undertaken and the response this time has been even more robust since we have faced a double whammy due to Covid-19

All in all, we were facing similar changes in that period and the government response was also largely similar. Therefore, it might be useful to look at how the economy panned out once the bottom was hit.

1. Strong Growth post 2003 - best growth period in our history!

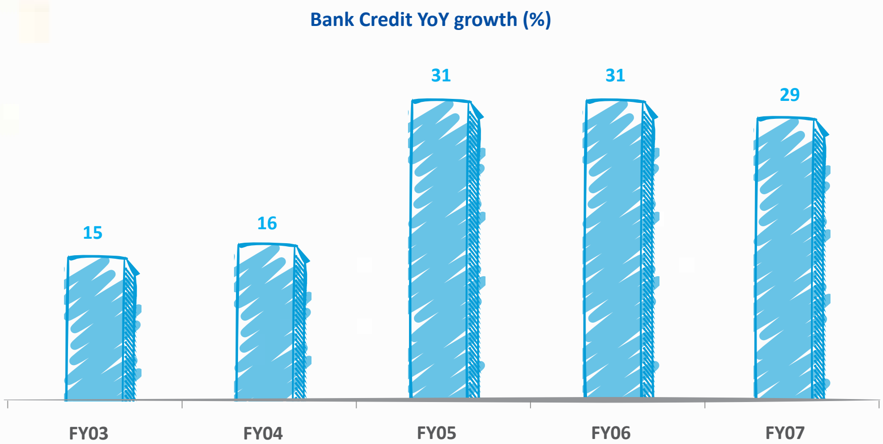
GDP Growth (%)



2. Strong increase in both government and private capex

	FY 97-03	FY 04-08
Government Capex Average *(as % of GDP)*	25%	35%
Pvt Sector Capex Average *(as % of GDP)*	17%	25%

3. Record credit uptake



Clearly, the economy has the potential to rebound rapidly and exponentially. While the situation has been compounded by Covid-19 today, we also think this is an excellent opportunity to undertake structural reforms, which can set the base for the future. Once the situation assumes normalcy, as we re-open the economy further, we do think 2021 onwards has the potential to be a 2004-2008 like growth trajectory.

At Edelweiss, we believe that growth will return to normal next year for the broader economy, barring a few sectors. The market will present good growth opportunities and we must be ready for the same. The PAG transaction is one such step to unlocking shareholder value as well creating a war-chest amongst others, which will provide us ample ammunition to ensure that we enter the growth run of India ready to be a significant beneficiary of the same.

Learnings in last two years

Bill Gates famously said,

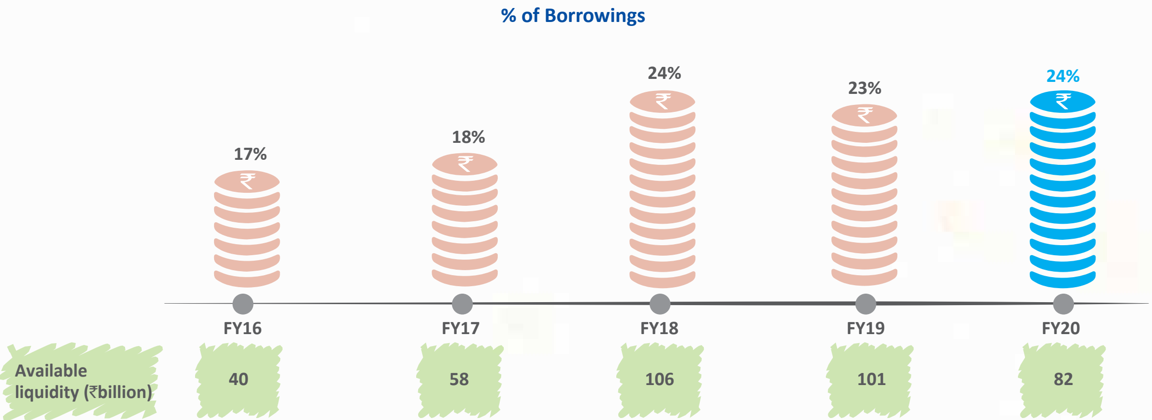
It's fine to celebrate success but it is more important to heed the lessons of failure

The last 24 months have been very challenging and while we would not describe them as a time of failure by any means, they have taught us some very useful lessons. These lessons have, in some instances, helped validate our hypothesis from our previous learnings, while in some other instances, they have provided some new insights.

On **liquidity**, for example, we have seen a validation of our decision to be conservative. We have always maintained a sizeable quantum of liquid assets on our balance sheet going way back to 2016. Even though this meant some amount of negative drag, it also meant that we felt comfortable at all points of time, even after ILFS when the liquidity squeeze was extreme. One thing we did not anticipate was the liquidity squeeze lasting so long.

We have been through recessions and financial crises before, but the current liquidity challenge has been unprecedented and quite surprising in its longevity, especially for a growing country like India. Events followed one after another since September 2018 and that meant that the market never had a chance to settle down and recover completely. There was extreme risk aversion in the bond markets and that meant that even when there was sufficient liquidity, the transmission was slow and subdued. Bond yields also remained elevated for a significant amount of time and the short-term funding market almost vanished. In such a backdrop, we have realised that you can never have enough liquidity!

Liquidity is largely comfortable for Edelweiss now but with the market still in a transition phase, it is important to be optimistic but with caution.



On **wholesale credit**, we had been working towards gradually moving our on-balance sheet book to the fund structure. However, we did not anticipate that a liquidity squeeze could have had such a significant impact on the sector. While this accelerated the movement of our wholesale book, it has also been a challenging time managing the overall impact on the wholesale portfolio. Clearly, a wholesale book needs a flexible financing structure, which is more conducive in the fund format rather than an NBFC format. This has been one of our major learnings from the last two years. While it has come at a cost, it has also clarified to us the long-term direction we want Edelweiss to gravitate towards – a retail, digital-led financial services organisation with wholesale businesses being run through the asset management vertical. We do remain positive on the wholesale credit sector overall through a fund structure and strongly believe that real estate, especially, will continue to present several opportunities, both in the near term as well as long term.

Another important reiteration during this phase has been on the **power of communication**. Mario Draghi, in 2012, famously vowed to do '*whatever it takes*' to preserve the Euro – a pledge that for many marked a turning point in the eurozone crisis. No one could have envisaged that a simple three-word phrase could have had such a profound impact on the global economy. Similarly, we have experienced that communication, both internal and external, is an extremely important part of any crisis management exercise and can often be the difference between success and failure.

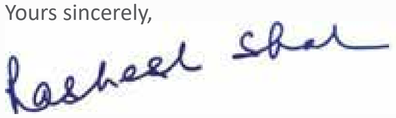
These are just few examples of what an insightful 24 months these have been. The learnings we have had are something which will form a guide for our next 25 years as well. Hence, I want to conclude this letter with a summarisation of these learnings –

1. There is nothing such as excess liquidity
2. The power of communication is unparalleled and is accentuated 100 times during a crisis
3. Wholesale Credit business is most conducive through a fund management structure
4. The worst of times brings out the best in people and the quality of human capital in an organisation really shines through – tough times build character
5. A strong organisational backbone in the form of enterprise functions not only enables growth during good times but even more importantly helps build agility and responsiveness to negative changes in the environment
6. There is no better teacher than history – history repeats itself in every cycle in different forms but with the same outcome

It has been a challenging year but there have been challenges before and there will be challenges in future too. We have faced and overcome these challenges in the past and we will continue to do so as we go forward. As an organisation, we have come a long way in the last 25 years but there is, yet, a long way to go. At Edelweiss, we feel fresh, energised, and raring to go as if we are starting Edelweiss today! There are a lot of targets to achieve in the next 25 years and we are all geared up to do so. In the words of Robert Frost...

We have promises to keep, and miles to go before we sleep, miles to go before we sleep...

Yours sincerely,



Rashesh Shah
Chairman & CEO