



“Shriram Transport Finance Company Limited Q2FY15 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Shriram Transport Finance Company Limited Q2FY15 earnings conference call. As a remainder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing * then 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Umesh Revankar – Managing Director, Shriram Transport Finance. Thank you and over to you Mr. Revankar.

Umesh Revankar: Hello everyone. Good evening and good morning to the people from US. I am with Sanjay, Sundar, Parag and Kelkar here. The Q2 results is always a difficult one and an unpredictable one especially if you are in India mainly because the monsoon has a lot of weightage on the way performance comes and this time we had little uncertainty in the beginning of the quarter with monsoon being very weak in the first month that is starting from June. Then, slowly it has picked up and relatively it has ended up well with only 12% deficiency which was at (-)46 in the beginning of the quarter. The performance in this unpredictable quarter is quite decent I should say, the numbers are with you. I will come to that little later. There is some pickup in the vehicle demand in the last month of the quarter that is in the month of September and we expect the demand to go up in the next quarter. Utilization levels have also gone up decently in the month of September. Overall, the collections also improved in the month of September but not sufficient enough. The other numbers which affects the economy where the GDP numbers are looking better in the Q2, the CPI and inflation rates both are showing the improvement. Only the industrial production is yet to pickup and we expect that to happen in this quarter. Overall, I should say the numbers are decent with net interest income going up. The higher provisions and higher interest cost reduced our numbers to some extent. Since the numbers are with you, I will not read it out and I will throw the session open for question and answers.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin the question and answer session. We have first question from the line of Ahmed Durrani from Deutsche Bank. Please go ahead.

Ahmed Durrani: Sir I had one question on your new CV assets. At least in the Q2, we saw a significant growth on the heavy CV side, on the new CV side, but your AUM in that segment seems to have degrown significantly. So any particular reason why that would have happened sir?

Umesh Revankar: See, heavy segment is one segment where we are not really growing big way and also if you look at the movement of the heavy vehicles across India has come down and that is one of the reasons we are growing more in mid and smaller vehicle segment, and we also expanded more into semi urban rural markets where the heavy vehicles do not play a major role. It is mostly in the industrial goods movement and mining activity heavy vehicles ply and these are the segment right now is in their downward trend at least for last one year. This is one of the reasons that our portfolio in heavy is not growing.

Ahmed Durrani: Okay sir, fair enough and just can you give some outlook on what is the kind of delinquency that you are facing. Are you still taking trucks from the delinquent owners and has the pace of these delinquencies been coming off for you?

Umesh Revankar: The repositions are definitely coming down. We have not seen much of the reposition in the last quarter and generally as a practice, we do not really believe in reposition but even then some of the people they surrender and some vehicles need to be re-pulled here and there, that also has come down significantly in the last quarter. So that is the signaling that the overall delinquencies are slowly coming down, but already existing delinquency will continue till it gets matured, loan gets matured.

Ahmed Durrani: Okay, fair enough sir and can you just remind us of the loan to value ratio which is there currently for you and has that changed over the last 1-2 quarters?

Umesh Revankar: Last 1-2 quarters not changed. In fact the last year, we tightened the LTV and reduced the LTVs by around 5%-10% across all segment and that is still continuing. I still would like to wait for sometime before rethinking on that.

Ahmed Durrani: Sir and lastly what we are hearing from the truck operators and OEMs is that even though the overall market is soft, lot of fleet operators who have older vehicles of say 3-4 years, they are just buying a new vehicle to replace a 3-4 year old vehicle because otherwise the secondhand market prices would fall for them. So are you seeing increased activity in the 3-4 year used vehicle market for you?

Umesh Revankar: We have not seen big change as it is because we have been in this segment of 3-5 years in the last two years. There is no significant change there and we also did not see big change in used vehicle market. For us, the market is very steady between 3-12 years and we are seeing reasonably good traction there.

Moderator: Thank you. We have next question from the line of Amit Ganatra from Religare Invesco. Please go ahead.

Amit Ganatra: I had a question on credit cost. You mentioned that incrementally the trends are improving, but the existing delinquent portfolio basically will continue to basically hit, but considering that you have this 180 days NPA recognition norms, ideally incrementally if trends are improving, then by two quarters from now your credit cost should start coming down right?

Umesh Revankar: Definitely, it should start coming down, that is what we also believe. But we have to see how the next two quarters will turn out if the diesel price decreases if it becomes advantage for the transporters and if they can earn little more, definitely we can see better trends in the coming days.

Amit Ganatra: But that should definitely be a tailwind because...

- Umesh Revankar:** Definitely, but we have to see how it pans out which is definitely a positive signal for all the operators.
- Amit Ganatra:** So in that sense basically for next two more quarters, you would say that credit cost can continue to hit you because of the current level, I mean the past delinquencies that I already asked.
- Umesh Revankar:** Up to some extent, yes. But there is always a big effort from our side to reduce it.
- Amit Ganatra:** No, agreed. It is just that, it is just the accounting thing right because you provide also 80%, your coverage ratio is very high, so to that extent it continues to hit the P&L.
- Umesh Revankar:** Yes.
- Amit Ganatra:** And any comment that you could make on the RBI, there is this expectation that RBI circular will soon be out which will require NBFCs to recognize NPAs on 90-day norm.
- Umesh Revankar:** We have no clue as such and there are no rumors in the market also. So we are not able to make any assessment out of it. So I think we can comment after getting it.
- Amit Ganatra:** No, but suppose if that happens then what is the hit or the impact that you would have?
- Umesh Revankar:** In the earlier draft itself RBI said 2-3 years timeline they will give. So there is nothing to really jump and provide for it. So even if it comes, there will be some timelines for us to provide and then organization also will look into that in a very different way. We will tighten our way we operate and collect money. So probably the way we operate can go for a change and we used to normally allow customer to have 1 or 2 installment outstanding to manage his other requirement, working capital requirement. That is something we can tighten further. So we will be able to get along with it if it comes. However, we wish that on behalf of customer that RBI do not bring it.
- Amit Ganatra:** And can you also comment on the cost of funds in the sense that has the incremental cost of funds being coming down for you now as compared to what it was say 6 months ago or 1 year ago?
- Umesh Revankar:** I will ask Parag to answer.
- Parag Sharma:** Liquidity continues to be good and bond yields have come off slightly. We are able to borrow bonds at much lower rate and that would have definitely helped and that would continue to help in whatever borrowings we have done in the coming quarters also.
- Amit Ganatra:** But just an observation, why is it that you also do lot of public issuances and not much rely on the private placements whereas the wholesale markets, liquidity is quite abundant. So any specific reason?

- Management:** It is only diversity of liability, retail being very good source of long term and continuous flow of funds. We have been tapping it every year.
- Amit Ganatra:** I know, but I mean, is it also more expensive in the current market context?
- Umesh Revankar:** Yes, it is slightly expensive yes, but diversity always helps.
- Moderator:** Thank you. We have next question from the line of Sneha Kothari from Subhkam Ventures. Please go ahead.
- Sneha Kothari:** Sir how do you see the growth outlook in the second half?
- Umesh Revankar:** See from the way it is panning out, it looks to be quite good. One is the diesel price coming down, which is likely to give better margin and more people would be enthused to get into this business and the existing capacity also is likely to be better utilized because of now the festival period is going on and the next month will be the agri output coming into the market. So reasonably good, capacity utilization would be there in this quarter that should make people to go in for more transaction on buying and selling of used vehicle and also on new vehicle. So overall we feel that demand will pick up. But there are two major things which we are expecting that is likely to make bigger demand that is one is on mining with there are some announcements by the government yesterday and which has appeared in the newspaper today. But I think a more clarity is required on that policy and that may probably start giving some more demand in especially heavy vehicle sales and probably as soon as government comes out with it, there will be demand picking up for that. And other activity is the infra activity which again there is some pickup in the road construction in certain pockets. So these two things should bring in more demand for vehicle sales adding to the agri and festive demand.
- Sneha Kothari:** And how do you see the margins?
- Umesh Revankar:** Margins should remain same. Margin will be more dependent on decrease in the cost of funds, not much on the yield increase. So yield increase may not be possible till we are very comfortable with our customer ability to really service the loans.
- Sneha Kothari:** How do you see the freight rates moving in?
- Umesh Revankar:** Freight rates have been good in the month of September and it is likely to, but if it remains same with decreased diesel, then probably people will have better margin. So we have to see how the freight rate move up or down in the next couple of weeks.
- Sneha Kothari:** And sir if suppose if RBI comes out with the NBFC guidelines for 90 days How do you see the asset quality?

Umesh Revankar: See, I already replied once just now. Last time in the draft guidelines itself, RBI gave 2-3 years timeline. So we have a timeline to manage moving from 180 days to 90 days and we also expect RBI not to come out with 90 days guidelines.

Moderator: Thank you. We have next question from the line of Ashish Sharma from Enam Asset Management. Please go ahead.

Ashish Sharma: Sir just on the growth part. Sorry, I sort of joined in the call little late. Just wanted to check with you, I mean outlook in the near term may not be as good. We expect some improvement in second half, but from a longer term perspective where do you see FY16 in terms of growth. Could it sort of be substantially better than FY15 sir?

Umesh Revankar: Definitely, there is a huge order. Demand is likely to come in the year 16 mainly because most of the infra and mining activity would kick start by next year and adding to that many of the additional manufacturing activity which is likely to be invested with lot of government initiative coming make in India. So we expect lot of Sops would be given for manufacturing activity in the next budget and that should really make a lot of difference in the demand. Especially as inflation cools down, there will be more income in the hand of people. So expenditure and the purchasing power are likely to go up. So this will make more consumer durables, consumer items and the other related buying activities will continue. So similarly the manufacturing activity also will expand. So there will be definitely a bigger vehicular movement due to more goods being transported across India and the other one is the GST. If GST comes, I think it will be a very big bonus for all the manufacturers including the small manufacturers. They would be able to sell it across India unlike now where many of the small manufacturers are forced to sell within the state because they do not have that capability of managing interstate tax issue. So that is going to be a big change if GST comes. One is they will be able to sell it across India and also the ability to go beyond the country because they will be able to get a scale to manufacturing. So once you get a scale, then you are able to sell across the country also.

Ashish Sharma: And if you have to just sort of put a number if you are looking at around 10%-12% FY15, 16 number could be closer to 15%-18%. Would it be fair to assume sir?

Umesh Revankar: The vehicle sales number if you are asking me, I would put it between 12-15 in heavy especially if all the heavy activities like mining and infra moves up because last 3 years, heavy sales have been down. But smaller vehicles probably may not grow to that extent immediately, but with one year lag, small vehicles also start selling more. So I think the action will be for 2 years from 16 to 17, not just one year.

Ashish Sharma: And just one more on the credit cost sir. What is your outlook at least in the near term? Do you think the credit cost would sort of a trend down or would sort of remain stable?

Umesh Revankar: The trend seems to be we have arrested the gross NPLs to some extent. So credit cost is something which we will not be able to predict immediately because the diesel price of the

vehicle and our customer's ability to really pay even when things become better is something which you need to really look into. So I cannot comment on that, but we will be able to definitely control the credit cost at present level and bring it to lesser levels maybe in two quarters.

Moderator: Thank you. We have next question from the line of Jyoti Kumar from Spark Capital. Please go ahead.

Jyoti Kumar: Just a couple of questions. First on headcount, I see your headcount has decreased sharply from 18,000 odd employees at the end of last year to 16,500. What explains this decrease?

Umesh Revankar: We made some kind of restructuring of our business and the way we are processing each of the customers' proposal that gave scope for some reduction. However, we did not retrench anyone. It is more of a natural attrition which allowed to happen and without recruiting. Last one year we have not recruited any fresh people. So there may not be further reduction now because we are seeing trend of credit growth. We should be able to maintain at this level and grow a little more as the business grows.

Jyoti Kumar: But is the attrition more at the brands level or at regional and head office, how should.

Umesh Revankar: It is at both level. We cannot say it is only at branch level, but mostly at field officer level where we organized our businesses. We found there was some additional manpower which was not immediately utilized. But even though it was more of an attrition rather than retrenchment.

Jyoti Kumar: Sure sir. The other question I had was on the prices of the secondhand vehicle if you can just comment on prices of secondhand vehicles in the market that is the new CV market and also would the change in economics because of diesel rate decrease make secondhand vehicles far more affordable and far more economical for the end user or for your customer?

Umesh Revankar: Yes. The second part, you are right. The reduction in diesel price will make comfortable like for used vehicle. That does not mean that people will not like to upgrade. People who would like to upgrade to new vehicle because of so many other comfort and technological improvement that is available in the new vehicle. So there will be aspiration to move into newer vehicle for all the people, but for the used vehicle operator where the fuel efficiency was the question mark. Now it is a little relief for them so that they can still operate on used vehicle and make a good earning.

Jyoti Kumar: And on the pricing part sir?

Umesh Revankar: Pricing, there is not much change. The diesel price have not really changed much, but now we have to really see with post diesel price decrease whether diesel price of used vehicle will go up, but there is some likelihood of going up because people who would definitely prefer used vehicle if it is available at reasonable rate and if they can make economical trip out of it. So we have to wait and watch for at least a month before commenting on that.

- Jyoti Kumar:** Sure. Finally on liability side, how is the demand for the securitization paper in the last couple of quarters generally at an industry level, not necessarily at Shriram level?
- Parag Sharma:** Securitization not much has happened, not from our end or in the industry as such. Normally it is during the last 2 quarters only, the banks come for priority sector and for securitization paper, already that taxation issue has still not resolved. So only the priority sector requirement as and when it comes up, there will be some requirement from the bank. As of now, it is not there much.
- Moderator:** Thank you. We have next question from the line of Saurabh Das from Franklin Templeton. Please go ahead.
- Saurabh Das:** Sir my first question is if I just look at the heavy vehicle book, what proportion of that would be largely less than 4-year-old trucks?
- Umesh Revankar:** We do not have that number immediately. Sanjay would help you to get that number.
- Saurabh Das:** But directionally in terms of growth, how has that segment been vis-à-vis your overall loan book. Has the proportion increased?
- Umesh Revankar:** We have been growing little slowly on the heavy. In fact in some markets we have also degrown because last 2 years the manufacturing activities were very low. It did not really increase substantially. So the requirement of heavy vehicle was less and therefore the growth opportunity on heavy vehicle also has come down significantly. It is more in smaller vehicles and passenger vehicles and tractors we have grown in the last 1 or 2 years.
- Saurabh Das:** Sir because if I have been looking at your segmental numbers and HCV in proportion over the last 4 quarters is broadly flat at 40%. So I was wondering if less than 4-year segment has been higher in our book than what it was a year back or it is almost same because it might have yield implications for us right because..
- Umesh Revankar:** Yes, but we are virtually not present in new vehicle financing of heavy.
- Saurabh Das:** I was talking about the used newer UCVs?
- Umesh Revankar:** Agreed, but I will not be able to give you a number immediately on the same.
- Saurabh Das:** And typically how is the yield difference between the two segments, the newer used and the older used?
- Umesh Revankar:** You are talking about heavy or?
- Saurabh Das:** Heavy, yes sir.

Umesh Revankar: Heavy, it will be around 200-300 basis points because it will be 16-18 in the newer used and 18-20 in the used.

Saurabh Das: And let us say going forward economy revives and you see strong demand coming back, what is your expectation of the mix that you would see lower proportion of these newer UCV trucks and you would have higher proportion of older or there is a structural change in the market that because of fuel efficiency and other reasons, you would see now your overall UCV book getting younger in age.

Umesh Revankar: Vehicles will definitely become younger over the period because efficiency and also technological advances in the new CV will make people go for newer CV, newer UCV. So that is going to be the way it is going forward. That is definitely going to happen, but the vehicle prices also we have to really watch and see. Except for last year, the vehicle prices have steeply gone up in the past 3 years and only last year the prices did not rise and there were discounts being offered. So to that extent, the diesel prices also were subdued or come down and once the discounts go off from the market, then only we will be able to really see how the trend is changing whether people prefer to go for newer used or a new.

Saurabh Das: And another question was on our ability to recover. So roughly you have close to 1,700 crores as a stock of gross NPLs. So what should as analyst or as a business manager you would be expecting in terms of recovery rates from this particular NPL book?

Umesh Revankar: This gross NPLs are the cases where it is above 180 days.

Saurabh Das: 180 days, not necessarily inactive accounts.

Umesh Revankar: They are not inactive accounts and as and when the loan matures, that particular loan expires, then probably we will give some more time for them to pay. So it may not be that all this cases will become repossess or it will be inactive and then not recoverable. It is not the case. So most of them will be still recoverable. So we will not be able to make a judgment immediately.

Saurabh Das: But historically you would have a sense of what proportion rather goes into loan losses?

Umesh Revankar: We have a historical credit cost of around 2% with around 20% on both sides. Right now, we are having a credit cost of around 2.35 this quarter. It is one of the peak. We believe that it is likely to come down over the period,

Saurabh Das: And within this slippage rate, is the LCV segment showing a higher slippage trend?

Umesh Revankar: Not exactly. The credit cost little higher for us and LCVs, the credit cost is little lower comparatively, but it will not have a big difference, but comparatively if I say LCVs are better for us because the likely chances of losses in LCVs will be lesser than the heavy because the ticket size will be bigger on heavy.

- Saurabh Das:** And just a small question on the quarterly results. If I am just looking at your fee and other income line item, I do not know if you have discussed it earlier. It shows a very sharp YoY and QoQ drop, what explains that if there any reclassification which has happened in the quarter.
- Sundar Shriram:** More on account of securitization income coming down.
- Saurabh Das:** Sir the securitization income is separately mentioned as net income on securitization that is 2,196 million. I was talking about the other line item, fee and other income which is 169 million in the quarter which was roughly 529 in the last year same quarter.
- Sundar Shriram:** It was investment income which was there in the previous year.
- Saurabh Das:** That is right. So it has been progressively coming off for the last 5 quarters. So is there any particular reason for that?
- Sundar Shriram:** No, in that particular year we had a surplus amount available for deployment in the short term investment which yielded certain income. There was one more transaction.
- Saurabh Das:** So I should broadly look at it as the trend in the fallen cash balances.
- Sundar Shriram:** Correct.
- Moderator:** Thank you. We have next question from the line of Lakshminarayanan from Catamaran. Please go ahead.
- Lakshminarayanan:** Sir I have one question on the tonnage of your HCV which is sizable part of your portfolio. What you have classified as HCVs and above which **(Inaudible)** this vehicle?
- Umesh Revankar:** We classify anything above the 17 tonne carrying capacity, that 25-tonne is a heavy and that is especially 10-wheel vehicle and all the 6-wheel vehicle, we classify as a medium and ICV.
- Lakshminarayanan:** You touched upon a important thing on technology advancers and what I understand is that ABS is becoming mandatory from sometime in 2015 where, correct me if I am wrong, more than I think 12 tons or 16 tons have been mandatorily fixed with antilock breaking system and then there is also you had talked about fewer emission norms getting revised forward. Now what kind of implication that we saw changes have on the secondhand portfolio of vehicles because at least for ABS what I understand retrofit of the vehicles cost almost between 50,000-75,000 per vehicle and failing which the vehicles cannot ply. So is this something which dealt earlier and how does investors are looking into these things from a portfolio health point of view?
- Umesh Revankar:** See typically when there is a new norm comes into implementation, they do it gradually and I am not really clear on what kind of regulations or changes they will bring in, but if you look at the past 10 or 15 years, all the regulations they bring it very gradually like euro norm or whatever it

is. First they will be implementing only in the cities, then it will be on the highways. Then only it will go to other places. And normally 7-8 years' time is given for this kind of a movement. So vehicles definitely will go in that case more into rural market. There is always a good demand for older vehicle in the rural market. So these vehicles will ultimately go into rural and slowly then get into very old category. So none of these vehicles will have overnight implication of not being run on either highways or in the cities.

Lakshminarayanan: Sir while I assess that the Euro norms are usually tough on that particular gradual manner of Euro x in cities and Euro x(-1) in the other cities. I think ABS what I understand is kind of slightly being made mandatory, I have not gone through it detail. So what is your thought on ABS?

Umesh Revankar: I do not have any clarity on that, but I have not heard of such thing. I really doubt because everyone in the government and stakeholder of the transporters are there. Without consulting them, government cannot come out with anything of such thing. So it will not happen because the transporters are now reasonably well organized. You cannot come with something where 40%-50% of the vehicles straight away unable to run the vehicle. That kind of law will not, even though there is a Supreme Court verdict on overloading from 2008, maybe 6 years now. No where it is strictly being implemented. There are lot of efforts from the government to really make it happen. So I do not really think such thing will happen.

Lakshminarayanan: Sir just one more question if I can squeeze in. In terms of delinquency/NPLs, which states actually contribute to the maximum if you can just help me with like states which would be like 70%-80% of the NPLs?

Umesh Revankar: See, it depends upon where we have big volume. Wherever we have big volume, it will contribute more. It is almost same across all the states and it will change every quarter. Till probably the April-May, we had a difficult time in Andhra Pradesh because lot of agitation and issues were there, but slowly it is coming off. Similarly we have some issues going on in some other state all the time like 2 years back we had Tamil Nadu delinquency going up because of draught condition there. So it will change. Now this year Tamil Nadu rains are good. So Tamil Nadu portfolio have started behaving a little better in the last one quarter. So it is keep changing. So it will not be one fixed area which that contribute more. So I will not be able to really comment on that straightforward.

Moderator: Thank you. We have next question from the line of Ahmed Durrani from Deutsche Bank. Please go ahead.

Ahmed Durrani: I just wanted a clarification, you said that on the LCV side, your credit costs are generally lower. So were you referring to the absolute level of losses or the overall asset quality because I would assume that an LCV owner would be slightly higher risk credit if I am not wrong?

- Umesh Revankar:** For us all the customers are owner, driver or small operator so whether he is having a bigger vehicle or smaller vehicle. So the level of commitment of the customer would be that he is owner, driver on the vehicle. So it will not differ, but only thing is if the LCVs, the loan sanction would be small amount. So the loss on that loans would be much smaller compared to heavier vehicle where the amount ticket size is bigger.
- Ahmed Durrani:** Fair enough. But the probability or the percentage of loans going bad on either one would be similar?
- Umesh Revankar:** Almost similar because one is local condition, second one is being owner, driver. He has this own livelihood to manage with the vehicle. Nobody would like to manage it badly and lose his vehicle.
- Ahmed Durrani:** Right. And I do not know if you can give this number. Generally is there a difference in the number of vehicles that your customer would have if he is an LCV customer or a HCV customer?
- Umesh Revankar:** Number of vehicles are normally restricted to 2-3, but some exceptional case where customer is with us for long, he may be having between 5-10 vehicles, but not many of the customers would be in that range.
- Moderator:** Thank you. As there are no further questions from participants, I would now like to hand over the floor back to Mr. Umesh Revankar for his closing remarks. Over to you sir.
- Umesh Revankar:** Thank you. We do really looking at the prospect of the credit demand going up in the commercial vehicle in the next 2 quarters because we do expect a lot of initiative of the government to come into action especially in the infra mining and various new CAPEX into the various segments and also expect a lot of infra activity coming up in the states like Andhra Pradesh and some of the states like Madhya Pradesh which is showing a lot of enthusiasm for manufacturing activity. So we have very bright prospect coming in the next 2 quarters and long term definitely a great growth story. With this comment, I thank everyone for participating and wish you a Happy Diwali to all. And also we have made this Diwali much sweeter by giving the highest dividend of 40%. So I wish you all the best.
- Moderator:** Thank you very much sir. Ladies and gentlemen, on behalf of Shriram Transport Finance Company that concludes today's conference. Thank you for joining us and you may now disconnect your lines.