"Magma Fincorp Limited
Q3 FY2019 Earnings Conference Call"

January 31, 2019

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Moderator: Ladies and gentlemen, good day and welcome to the Magma Fincorp Limited Q3 FY2019 Earnings Conference Call hosted by IIFL Securities Limited. As a reminder 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, 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. Abhishek Murarka from IIFL Securities Limited. Thank you, and over to you, sir.

Abhishek Murarka: Hello, everyone, and welcome to the Q3 FY2019 conference call for Magma. We thank the company for allowing us the opportunity to host the call. From the management, we have Mr. Sanjay Chamria, Vice Chairman and Managing Director; Mr. Kaushik Banerjee, President and CEO, Asset Backed Finance Business; Mr. Manish Jaiswal, MD and CEO, Magma Housing Finance and CEO, SME Business; Mr. Rajive Kumaraswami, MD and CEO, Magma HDI General Insurance; and Mr. Kailash Baheti, Group CFO. We will start with an opening statement from the management and then proceed to Q&A. Over to you, Sir!

Sanjay Chamria: Thank you, Abhishek. Good evening, ladies and gentlemen. I thank you all for joining us this evening for the third quarter earnings call of Magma Fincorp. As you are all aware, the last quarter was one of the most challenging quarters for the financial services sector. I am quite happy to inform that we were able to continue our disbursement as usual in all the three months. We have come across similar challenging situations in over 30 years of experience in retail financing and Magma has been able to successfully overcome each of these without much impact on the business. Broadly, three factors have helped us navigate through the current situation. First, our capital raised of Rs.500 Crores in the beginning of the year. We are now sitting on a very healthy capital adequacy of 22.6% as of now and a low leverage of 4.5x. Second, even during the liquidity squeeze, we were able to raise additional term loans of Rs.500 Crores for the banking system. We have always relied on the banking system for a large part for funding requirement and therefore, had adequate funding lines to take care of our immediate needs of repayment of short-term obligations and maintaining disbursals at the normal level and thirdly, Magma's long history and strong reputation in raising money through securitization both in the form of pass-through certificate and direct assignment.

Magma has till date turned securitization of over 200 pools with total underlying asset value of over Rs.40000 Crores. It is a matter of record that Magma's pools have been upgraded many a times, but have never been downgraded. During the quarter, we successfully raised more than Rs.1700 Crores by way of fresh securitization providing enough liquidity to continue business as usual. One question that has been repeatedly asked during my recent interactions with various stakeholders is, "What would drive new business of NBFCs and HFCs going forward?" In my view, the business model of the NBFCs and HFCs have been differentiated by the two key factors. First, the speed and the consistency in credit underwriting. We have taken a significant leap in the quality of credit underwriting with the implementation of Credit Engine for our asset finance business. Now we are able to provide on-the-spot decisioning and the credit underwriting standards are universal throughout our network of 300-plus branches. We are presently in the process of developing similar rule engines for our other businesses that is mortgage and SME and will implement the same by early next year. The other differentiator is to provide warm experience to the customers. We have implemented state-of-the-art CRM system and now we target to resolve close to 80% of the customer queries on call, resulting in customer delight. Further, with the help of the CRM automation, we are using the available customer database for customer retention and the strong cross-sell and up-sell.

I shall now move to the performance for the quarter. I am glad to share that despite external headwinds, we have registered another quarter of good performance. I would first like to speak about the complete transformation achieved in the portfolio quality. I am very happy to share that our GNPA ratio has dropped to 6.3% and NNPA to 4%. We achieved this in spite of overall AUM remaining flat. Our NPA numbers are, therefore, qualitatively superior as we have not got the benefit of a growing AUM, which we shall get eventually. Coming to the Asset Backed business. During the quarter under review, the ABF business recorded a significant improvement in the portfolio quality with a sharp improvement in the net credit loss and the NPA ratios. We also launched a Credit Engine for our vehicle finance business in October. This involved a learning curve from the front-end, as is usual with the implementation of any new platform. With the launch of the Credit Engine and the team getting back to business as usual, we foresee the ABF business driving an enhanced disbursement performance through improved efficiency and a consistent improvement in credit assessment and resulted quality going forward. In line with our guidance, the disbursal of CV and CE grew by 27% and Used Assets by 16% Y-o-Y. Contribution of passenger vehicles and tractors to the overall disbursals continues to correct within the overall disbursal mix. Mortgage business - we are happy to share that we have successfully transformed the housing business to an affordable home loan business, with significant part of the business being generated directly. During the course of this year, our HL disbursals have trebled, while the overall disbursals have grown by 88%, in line with our business philosophy of Go HL and Go Direct.

Our incremental disbursals have 70% contribution of the home loans and about 80% of this business is sourced directly. We are now present in 100 branches, which include 21 micro markets, in line with our strategy of deepening affordable housing presence in semi-rural and rural markets. We intend to expand our reach and distribution capabilities to over 120 branches and 36 micro markets next year. Our housing franchise has deepened its presence and established direct connect with its customers in nine key states, signifying distinguished and diversified national presence with 34%, 31%, 29% and 6% disbursals for the quarter coming in from West, North, South and East, respectively. This mitigates geographical concentration risk.

Coming to the SME business, the momentum has continued with a focus on upcountry locations. Our disbursal for the quarter grew 23% Y-o-Y. And for nine months, the disbursal grew 41% with 70% growth coming in from the upcountry market. Investment in data analytics have started giving returns. With the use of machine learning, we are able to pick up nuanced portfolio trends and tweak underwriting norms swiftly. We shall launch the Credit Engine in Q1 of FY2020. Once the new Credit Engine goes live, we would expect significant improvement in the customer approval time and productivity and improvement in the portfolio quality.

General insurance business. This business continues to register robust growth vis-à-vis the industry growth rates. Magma HDI have registered a growth of 115% in gross direct premium over third quarter last year and 83% in nine months on a Y-o-Y basis as against the industry growth rate of 14% and 13%, respectively. The growth is driven by strong momentum in the retail and commercial verticals with the continuous improvement in the quarter-on-quarter retail run rate. Motor continues to be the dominant portfolio of the company with the concentration being 38% of the portfolio versus 76% in the nine months. The company continues to enjoy one of the lowest Own Damage loss ratios in the industry. The company has successfully launched Health - Group Health in third quarter and has made modest beginning in underwriting business with focus on the smaller corporate customer.

During the quarter, the company has strengthened its reserves on historical TP liability portfolio due to which the combined ratio for the quarter normalized, is higher by 2.7% over the third quarter of last year. The combined ratio for third quarter stands at 124.7%. For nine months, there is an improvement in the combined ratio by 3.6% over the same period last year with it being 120.3% for nine months. The company is now reaping benefits of the scale with an improvement on the expense and the commission ratio. The company continues to make an endeavor to forge new tie-ups with the OEMs and banks, which is likely to result in a further improvement in quarterly retail run rate and financial performance.

Now coming to the highlights of the financial performance for the third quarter. These numbers are under Ind-AS. And the previous year figures have also been aligned with the

Ind-AS to make them comparable. The disbursals grew despite the severe liquidity crunch faced by the industry. For nine months, our disbursements grew by 22% compared to same period last year. And for third quarter, the disbursements grew by 10%. Our AUM grew by 6% Y-o-Y and is flat quarter-on-quarter. During the quarter, we wrote-off fully provisioned NPL of Rs.450 Crores in the higher buckets. If not for this write-off, our AUM would have grown by 2% on Q-o-Q basis. We are confident of continuing the growth trajectory in our disbursals and the AUM.

GNPA and NNPA. As mentioned earlier, we have been placing relentless focus on improving asset quality, which has resulted in rich dividends for the company. Our GNPA has reduced from a peak of 10% in third quarter last year to 6.3% in third quarter this year. And our NNPA has similarly reduced from 5.6% to 4%. The significant improvements seen in the early warning indicators from the new portfolio, we are on course to further reduce GNPA and NNPA next year. This will have cascading impact on credit losses and improve the profitability of the company. As a result, in line with our guidance, the credit cost has declined to 1.3% in the third quarter and we expect it to go down further in the seasonally strong fourth quarter. Our NIMs continues to be healthy at 8.4% in spite of steep increase in the cost of funds due to prevailing liquidity scenario during the quarter. It has peaked in the month of December, and we have seen some softening of the incremental borrowing rates in January 2019 and expect it to ease out further in the fourth quarter as the liquidity scenario returns to normalcy.

However, we expect an overall cost increase of about 50 basis points in fourth quarter compared to third quarter. We have been able to pass on the increase in the cost of funds on the entire mortgage book and for fresh disbursals in the other products. As a result of all of these, our PAT has grown significantly by 65% on Y-o-Y in spite of sharp increase in the cost of funds during the quarter. For nine months, the profits have grown by 39%. Overall, considering the current NBFC environment, I believe Magma has registered a strong performance on all parameters. I would like to once again affirm our commitment towards sustainable, long-term earnings and growth. So now myself and my team would be happy to take any questions that you all may have. Thank you.

Moderator: Thank you very much Sir. Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Aarsh Desai from Vallum Capital. Please go ahead.

Aarsh Desai: Yes. My question was actually with regards to your NPA. I mean, there has been a sharp improvement. So I was wondering what has led to that sharp recovery because the AUM has not per se grown. That was my first question. And my second question was, to what extent do we plan to rundown our agriculture book and our passenger vehicle book? And how do we see our portfolio shaping up?

Sanjay Chamria: So let me answer the first question, and the second one will be answered by Kaushik. There are two reasons, which has led to the sharp improvement in the NPA ratios. So it is consistent with the commentary that we have been sharing over the last several quarters that the focus on relentless improvement in the portfolio quality. And as a result of that, the new origination has been distinctly superior and measured by the early warning indicators. When we look at the noncurrent customers on 0 plus after 60 days and the customers having more than two installments default across various periods starting from 6 months to 18 months. And what we have seen and this is something we have shared in the investors presentation, which has been uploaded on our site, that there has been more than 60%, 70% improvement over the last three years in terms of the early warning indicators. And on this new portfolio accounts for more than 85% of our total AUM. As a result of that, the credit cost has been steadily coming down and the standard portfolio has been growing in size. The second region is the portfolio, which went into NPA, which is 90-plus. Due to the better cash flows prevailing in the markets, we have been able to clawback some of these gross NPAs and adjusted even for the write-off of the fully provided NPAs, there has been reduction because there has been more recoveries in the NPAs than what has been the fresh accretion. When that happens, that also leads to a lower credit loss. So as a result of these two factors, the NCL, which is a factor of the portfolio distribution, the total credit cost has come down from well over 2.3%, 2.4% to 1.3% in the third quarter. So hope that satisfies your first question and now over to Kaushik for your second question.

Kaushik Banerjee: Yes. Could you just repeat the question regard on cars and tractors? The line was slightly bad.

Aarsh Desai: Yes, Kaushik. No, so what I was trying to ask you is where do you eventually see your portfolio construct in the sense what do you plan to run down your passenger vehicle to and your Agri Finance book to? I mean, what is an ideal AUM mix that you're personally looking at?

Kaushik Banerjee: Okay. So there are two significant changes, right? So one is basically your overall composition of portfolio from a disbursement perspective and the resulted impact of this in terms of your AUM. So just to give you a comparative Y-o-Y, last year, for example, 40%, just Q3 FY2018, 40% of our disbursement came from Agri and UV. And 60% came from other products. Used is about 34%, CE was about 8% and CV is about 15%. This year, in Q3, basically, 70% of our overall disbursements come from Used, CE and CV, and about 29% has come from Agri and cars. However, if I look at my AUM composition, we still have about 49% close to 50% of the portfolio in Agri and UV, which is corrected from 26%

in Agri and it was about 33% in cars. So in all our previous interactions, what I have indicated is that no single product, barring Used, which is a composite of multiple products, should have a share of more than 20% in the overall AUM. So it is not contraction and volume. That could be an outcome in terms of the fact that you are focusing on other products. But yes, so, today, we are at about 49%. And with severe growth across all asset categories, including cars and tractors, it should still be within 20% for each of these categories of assets. So the larger contribution of Used, CV and selectively CE. So does that answer your question?

Aarsh Desai: Yes, it does. And just one more thing on with regards to what Sanjay just said, with regard to the cash flows that have gotten better which has led to the upgrades in terms of the asset quality. So what has led to this per se in this quarter? I mean, there would be cash flows have gotten better or the collection efforts have changed? Or I am still not getting, like, the operational part where there has been such a big jump in our asset quality.

Sanjay Chamria: So you see it is very difficult to sort of distinguish and create a silo of the improved cash flows and reflected in the collection efficiency, is it a function of the improved great underwriting or better collection efforts or the superior cash flows in the hands of the customers? But actually, it is a combination of all three. So what, therefore, we do is measure the collection efficiency in the various buckets that we have. And again, I do not know if we have shared that slide in this PPT. But we do look at internally that collection efficiency across buckets has improved during the third quarter, in fact, the entire nine months. And therefore, we think that there is an improvement in terms of the cash flows coming in from the customers resulting in better bucketing and, therefore, lesser credit losses. Now what happens under Ind-AS, you need to make a provision for every single bucket as against only the provision in the LTA bucket.

Aarsh Desai: Alright, got it. That is it from my side. Thank you.

Moderator: Thank you. The next question is from the line of Ankit Choudhary from Equirus Securities. Please go ahead.

Ankit Choudhary: My first question is related to the SME segment. So currently, in the current environment, it has been understood that the SME segment is facing some issues with respect to the cash flows and the business sentiment being down. And also, if we see the asset quality in the SME segment, if you measure by ID & ED, so one of those has increased on a quarter-on-quarter basis **(inaudible) 21:31** 1.4% to 1.6%. So how do we see the strength in the segment right now?

Sanjay Chamria: Yes. So you are right. In general in industry, there is certainly a perception that certain MSMEs are under stress. And the way we have run this business is very different. I think our customer selection criteria and risk management kind of virtually makes it a very tight process on our on-boarding process. So we essentially have fairly strong and robust process, which has stood us almost for last decade or so. Despite being a GST event or a demonetisation event, our performance of portfolio, by and large, has withstood the rigors of the economy. So to that extent, we believe that the intrinsic model with the organization has evolved, is holding us on good stead. Our ED ID ratios are actually stable. A 0.1% or 0.2% on ID of late has largely been on account of auto debit and NACH because we have seen 20%, 25% initial bounces in a couple of months, but then they get restored. So to that extent, we largely see that happening. But it kind of is bearing well and stable. There is no cost worry or angst as far as we see. We are holding on to our post-tax ROA which the business delivered in the range of 2.5% to 3%. And it has delivered in the past. It is delivering currently. And we are pretty sanguine about the performance of SME business in the current year to be kind of really growing at the rate of 28% to 30% at the top line level and also at the bottom line level.

Ankit Choudhary: Okay, understood. The second question was related to the vehicle finance segment. So in the call, in the Q2 FY2019 call, we have mentioned the focused products will be CVs, mostly light and small commercial vehicle, along with the Used segment. And in the current PPTs, so I understand that right now we are trying to manage the portfolio such a way that every product will be like 20% around. But then all of a sudden, in this quarter, we have suddenly started our focusing on construction equipment as well, so which I assume to be a lower yielding product. So in that case, how are we going to manage the leads going ahead? So vehicle finance will be able to sort of declining the Agri part, the tractor segment and focusing more on the construction equipment to make it - the portfolio a balanced one?

Kaushik Banerjee: Good point. So there are two things. One is yield management. The other is basically risk-adjusted return on your book, which is the return on assets. So when I talk about co-products, CE is a part of that. And our portfolio tough - portfolio quality in CE is excellent and, as a result of which, our return on assets in CE is extremely healthy. So we would focus on asset categories that give us an appropriate and necessary return on asset. So Used, clearly, has the highest return on assets. And CV and CE today are pretty much equal in terms of risk-adjusted return on assets. And if you realize, in Q3, the industry has grown about 20%, 28% or 28% in the CE business. And CV has actually degrown in the same quarter. So as a result of the overall buoyancy in the market for CE and given the returns that we get on the CE book post - in terms of our ROA, it is on an indifference curve in terms of your CV and CE. So the main focus has actually been to kind of reduce the overall AUM contribution of cars and tractors, I said earlier, is what 49% of the overall book.

Sanjay Chamria: Just to supplement what Kaushik has said. We have also taken an approach that the overall yield in the vehicle finance business we would like to keep in the range of about 15.5% to 16%. And there, of course, would be temporal shift that in certain quarters you may see the contribution of a particular product go up or go down. But it will be more range-bound. From that standpoint, as we have shared consistent with our product philosophy that we wanted to degrow our focus on the tractor given the cyclicality that it has in terms of the collections and significantly grow our exposure in the used efforts. And passenger vehicle is something that we do across all the three unit branches, so in terms of the top line, that is the second largest. And between CV and CE, we will do as and when we get the deals, which should meet with our risk-and-return expectations. So in CV particularly, we focus on light and small commercial vehicle, but that does not mean we don't do the heavy commercial vehicle. But we restrict ourselves to the first-time buyers or to one or two vehicle owner in commercial vehicles for heavy commercial vehicles. And similarly, in case of CE, there are two categories. One is the plant hirer and the other is one equipment owner. So these are the typical customer classes that we would be financing to. So what we have seen in the third quarter that there has been somewhat higher offtake by the plant hirers and one or two equipment owners. And as a result of that, because we specialize in financing, you have gotten some more business. But uppermost in the mind is: one, the portfolio quality, which has been showing steady improvement; and second, that our yield expectation for every month is not less than 15.5% and range-bound between 15.5% to 16%.

Ankit Choudhary: Okay. And lastly, on the asset quality, could you just provide me the breakup of the Gross Stage 3? As in what were the slippages and recoveries and write-offs? So I thought you mentioned about Rs.450 Crores, but the other part?

Sanjay Chamria: Sorry, can you just clarify your question?

Ankit Choudhary: So I wanted to know the breakup of Gross Stage 3 as in the moment? So what were the slippages and other recoveries during the quarter?

Sanjay Chamria: So I think that there is slide #41, I do not know if you have downloaded the investors PPT in which we have shared the stage 1 and 2, what is the provisioning ratio and what is the provisioning ratio in this stage 3. So in the stage 1 and 2, it has actually improved marginally from 2.5% to 2.4% from Q2 to Q3, whereas it was 2.9% in March. So between March and December, it has improved by 0.5%. And that is a function of the bucket mix. That means the 0 bucket has a higher percentage in December compared to March. And similarly, 61-90, which is the stage 2 higher bucket, the contribution is lower. And so far as the stage 3 is concerned, there, the provisioning has dropped from 54.5% to 38%. And that is, as I mentioned in my address, that during the quarter, we wrote-off Rs.450 Crores worth of gross NPAs, which were fully provided for, which means that there was 100% provisioning on that. And as a result of that, the provisioning on the balance NPA has reduced to 38%. So if you look at in slide #41, the Gross Stage 3 was Rs.1452 Crores, out of which Rs.450 Crores we sold. That makes it Rs.1000 Crores and still, in December, it is Rs.946 Crores. So that means in absolute amount, there is a reduction of more than Rs.50 Crores in the gross NPA in the third quarter.

Ankit Choudhary: No, my main question was more relevant to this, so, let us say, the Gross Stage 3 is right now Rs.946 million. So just wanted to know, what were the fresh slippages during the quarter? And what were the recoveries?

Sanjay Chamria: So we do not have that detail as of now. Maybe later on you can connect with Jinesh and he can provide you.

Ankit Choudhary: Okay. And finally, on the write-off, as you mentioned, Rs.450 Crores, could you just give some color on what was the write-offs on the vehicle side and if any on the LAP segment?

Sanjay Chamria: It would be mostly in the ABF portfolio. Because in the mortgage given the nature of the collateral, the recovery is a lot higher and therefore, the write-off would be much lower. And in SME, any ways, which is unsecured, here, like, for example, we do 100% provisioning at 730, in case of SME we do it at 450 itself.

Ankit Choudhary: Okay. So when we talk about when the Indian portfolio, so it is more of a tractor, the holder portfolio, which is running down?

Sanjay Chamria: So it will be a mix of tractor and passenger vehicles because these are the two largest verticals within ABF.

Ankit Choudhary: Thank you.

Moderator: Thank you. The next question is from the line of Kunal Shah from Edelweiss. Please go ahead.

Kunal Shah: Yes. So in terms of the write-offs, are there other portfolio as well, which would be 100% provided for and there is still further question to write it off over a period? Or we are largely done in terms of the write-off of the entire portfolio?

Kaushik Banerjee: So we are largely done in terms of write-off of the 730 plus portfolio. There could be some marginal amount.

Kunal Shah: Okay. And overall, in terms of the business momentum, so, definitely, liquidity was a challenge. But had this environment not been there, then what would be the kind of disbursements, which we would have looked at? So just wanted to understand in terms of - now maybe the steady disbursements, so how much was because of the weak underlying demand trends? And how much would have been on account of the supply-side constraints?

Sanjay Chamria: That is really a hypothetical question that we do a what-if scenario analysis and then try and answer. So I would rather not hazard a guess about this. What I can definitely share is that because of the liquidity constraints, even the demand side kind of compressed. And that if you look at the vehicle sales numbers, third quarter has probably seen the steepest decline over the last many, many years. So that when the liquidity side tightened up, the demand side also slackened. So it is very difficult to say as to which one happened due to whom. Similarly, in case of the fresh home loans, because there was a liquidity squeeze and which was felt more so on the housing finance industry, the sale of homes also took a beating. And therefore, it is very difficult to ascribe as to what occasioned which one and how much would have been there if this was not for this scenario.

Kunal Shah: But looking at the trends, how do we see it going forward? So when we look at generally in terms of a Q4 and so what could be like the average disbursement run rate, which we can look at?

Sanjay Chamria: Of course, we have seen that with the interest rate softening from beginning of January. And typically, that the Q4 distribution pattern is that it accounts for about 35% of the annual disbursals. That it should be higher than third quarter and much more than third quarter because third quarter was muted from overall industry perspective. Now how much would that be would be difficult to predict. But of course, we expect it to be far superior to third quarter.

Kunal Shah: Okay. And in terms of commercial vehicle and commercial equipment, are we seeing slight contradictory trend? Or this is largely on account of maybe few - maybe you highlighted there were like two order dealers wherein the demand was slightly, one-off kind or maybe concentrated? Or maybe only because when you look at the construction equipment, that is going pretty strong even quarter-on-quarter as well as year-on-year as compared to that of CV. So may be at the ground level, any differentiated trends you are seeing between these two segments?

Sanjay Chamria: So I would not really read too much into it based on one or two quarters development. As we shared that from a medium to longer term, our focus is to grow our franchise in the Used Assets and then light and small commercial vehicles. So these two, definitely, would be the focus products and followed by then passenger vehicles and finally, we will have medium and heavy and construction equipments and that trend will not change.

Kunal Shah: Okay. And lastly, in terms of looking at the early warning signals and maybe the other indicators, which you've highlighted, how comfortable are we with the credit cost, which was reported in this particular quarter? So we had seen overall quite, I think, significant reduction on the credit cost side. So are we getting back to the normalizing trend given that now it is like more a better graded branches, which are contributing to the incremental business?

Sanjay Chamria: On an overall basis, there has been very significant improvement in terms of the credit losses. I would expect this to decline a little bit further and then stabilize because as we expect our gross NPAs to moderate further. So now it is about 6.3% and the net NPAs are at about 4%. And we expect this to decline further in the fourth quarter and then further go down next year. So as it happens, we will definitely see the credit cost moderating down, but I certainly do not expect it to be lower than 1%.

Kunal Shah: Okay. And no need to increase the coverage now. Maybe because of the write-offs, it has again come down to sub-40%, but would we be looking at in terms of the stage 3 provisioning when we look at it. So given the loss, given default, would there be a need to further inch it up? Or maybe it should stabilize at 38% to 40% level?

Sanjay Chamria: So now it is very scientific that based on the long-term moving average of the LGD, you create a provisioning which is called ECL. So it is true representative of the likely losses that you are expected to incur in the NPA in the stage 3. And therefore, now depending upon the tenure or the aging of the NPA, the coverage ratio will go change. So for example, till September, it was 56%. And now, it is 38%. That is because, now, due to the write-off that we did in the third quarter, the average tenure has become much younger and, therefore, the provisioning is lessened. But then in terms of the percentage that we provide for remains the same and that is based on the long-term moving average of the LGDs.

Kunal Shah: Thanks a lot.

Moderator: Thank you. The next question is from the line of Antariksha Banerjee from ICICI Prudential Asset Management. Please go ahead.

Antariksha Banerjee: Good evening people. My question is separately to Kaushik and Manish. So last time we had met, you had told us about...So last time when we met, you had told us that you are reassessing your targets of three year or five years both transitioning to Ind-AS that you had set on the ROAs and ROEs. So are we done with that? And if you could guide me, business-wide, separately, at where we are now and how we would get to those targets?

Kaushik Banerjee: Sorry. I do not think we had a discussion in terms of reassessment or targets based on Ind-AS. Neither Manish nor I recall this particular conversation.

Antariksha Banerjee: Okay, so let us go with what are the targets now and how we will get there.

Kaushik Banerjee: The targets do not change. So it is a pretty elaborate process of budgeting. And what Ind-AS has succeeded in doing is basically there is a significant focus on each bucket.

Sanjay Chamria: Let me answer this question more at an organizational level. We have given the guidance that we wanted to first cross 1.5% ROA and 12% ROE, which we have already crossed. And now the next milestone for us would be to touch 2% ROA and 15% ROE and which is what all the three businesses are collectively gunning toward. So there are some businesses which do more than 15%. There are some that start doing less. So the idea now is that how, at a consolidated level, they can cross 2% ROA and 15% ROE.

Antariksha Banerjee: And this looking at from a one year perspective from now?

Sanjay Chamria: Well, let us see how it happens because it all depends upon the two things. One is the net interest spreads, in which it is dependent upon the cost of fund, which has been pretty volatile. But till now, we have maintained the NIMs which are in excess of 8% and which is pretty much the top border. And the credit losses, which were more than 2%, have now come down to 1.3%. But still on nine months basis, it is close to 2%. We want to further bring it down in the fourth quarter. So ideally, we would like to have this settled anywhere between 1% to 1.5% on an annualized basis and the other point that we had shared that the AUM, the growth which has trailed the disbursal growth, like until September, our disbursal growth was 27%, but our AUM growth was 5% and we said that from second half of the year, the AUM growth will follow the disbursal growth. But unfortunately, due to this liquidity scenario that panned out, the disbursal growth itself was just about 5%. So as that normalizes, we will see the opex ratio also improving. So both the NCL and the opex will start contributing to the ROA and therefore, we should be seeing a quarter-on-quarter improvement. So therefore, it will be more sustainable in nature.

Antariksha Banerjee: Okay. Just two things. One is opex. So currently, from where we are, if you assume a steady-state growth rate, how much could be improved? And the second is something I would be asking you. In the vehicle finance portfolio itself, we were having a huge runoff from the old portfolio for the last few quarters. So has that run down completed? Or is there some more remaining?

Sanjay Chamria: So on the opex, we are at 4 plus, and our idea would be - so we are looking at various initiatives that have been undertaken. The combined effect of this would be to look at an improvement in the productivity by about 20%, 25%. With the 20%, 25% improvement in the productivity, the opex improvement should be about 15% because the productive to nonproductive would be about 65:35 ratio. So next year, our endeavor would be to go below 4%. And with that, that improvement is what we would expect. Now we know that there are some place in the industry which are even below 3%, but then that is the catch up that we need to do.

Antariksha Banerjee: So what you are saying is on your numerator, you expect a 15% reduction, whereas your denominator will be a function of how much you grow, right?

Sanjay Chamria: The denominator would grow, as I said, because from third quarter onwards with the disbursal growth, the AUM growth will also follow. And typically, if your disbursal would grow by 25%, your AUM should also grow by 15% to 17%, which, until September, in our case, it did not happen. Because the older portfolio was running off quicker and we had a degrowth in the portfolio earlier. But now that has stopped. So therefore, we should also get a tailwind on account of the growth in the denominator. So therefore, optically, the opex to AUM should look superior.

Antariksha Banerjee: Okay. And on the runoff?

Sanjay Chamria: Sorry, what was your question on the runoff?

Antariksha Banerjee: The last few quarters, specifically in the ABF portfolio, we were seeing a lot of the old portfolios running off. That run rate was very high. So has that stabilized now? Is that completely done?

Sanjay Chamria: Yes, that is exactly what we said that, till September, we had this legacy and the baggage. But from October onwards, it is normal curve.

Antariksha Banerjee: So we can expect this run rate to remain, right?

Sanjay Chamria: Yes. So for example, if we grow our disbursal by 20% in ABF, our AUM growth should be more than 10%, which was not the case until September.

Antariksha Banerjee: Thank you.

Moderator: Thank you. The next question is from the line of Deepak Poddar from Sapphire Capital. Please go ahead.

Deepak Poddar: Thank you very much Sir for the opportunity. Sir, just wanted to understand that given the hiccups that we saw in the last quarter, are we still maintaining kind of 15% kind of AUM growth this year and any outlook for next year as well would be helpful?

Kailash Baheti: So the AUM growth has not been 15% this year. There are two reasons. One is that we have return of this Rs.450 Crores of portfolio which was in 730 plus. So that is up roughly about 3%. We should be more looking at a growth of above 10%. What was your second question?

Deepak Poddar: Was a similar outlook for FY2020, if that is possible?

Kailash Baheti: I think the next year we should again be targeting what we had targeted current year at the beginning of the year.

Deepak Poddar: 15% to 18%, right?

Kailash Baheti: Yes.

Deepak Poddar: Okay, thank you very much.

Moderator: Thank you. The next question is from the line of Anirban Sarkar from Principal Asset Management. Please go ahead.

Anirban Sarkar: Thank you Sir for the opportunity. Most of my questions have been answered. Just one question on your general insurance piece. If you could help me understand the sharp increase in combined ratio between the two quarters, between Q2 and Q3. There is 740 basis points increase in the combined ratio and if you could help us understand that part.

Sanjay Chamria: Rajive, go ahead.

Rajive Kumaraswami: Sorry. I actually got disconnected. Can you repeat your question, Anirban?

Anirban Sarkar: Yes, sure. Sir, my question is on the sharp increase in combined ratio between the two quarters, between Q2 and Q3, for your general insurance piece, so...

Rajive Kumaraswami: Yes. So I mean I will probably address this more at a fundamental level. As you would be aware, in the initial years of a general insurance business, the business tends to consume fair amount of capital. Compare us to a lot of our peers, we have been very prudent in terms of the capital that we have consumed in this business. And till date, we have infused about Rs.308 Crores of capital, and our accumulated losses as on date are only to the tune of about Rs.23-odd Crores. Now what we have been doing, as you might be aware, given the accounting strain that a general insurance company has more so on the retail businesses, the more you grow on your retail businesses, the higher tends to be the accounting loss. Because the policy premium gets owned over 12 months, whereas the cost of acquisition and your operating expenses get charged in the month you acquire the business. So what we have been doing over the last, actually, 18 to 24 months is we use reinsurance fairly judiciously, one, to manage the accounting stream; and two, to manage our solvency requirements. What we have done in Q3 is to: one, take care of the accounting stream; and two, also to optimize our capital requirements. We have reinsured a part of our own damage portfolio, as a result of which the composition of the earnings, which is what is called the net earned premium, between OD, third-party liability and the nonmotor business has changed. The loss ratio per se has not changed. But because the commission earnings from the OD sessions takes care of the accounting charge, but, actively, what happens is because the NEP of OD goes down, you end up replacing a 50% loss ratio business with TP, based on your reserving at about 100% loss ratio. So effectively, that is about a 5% impact on loss ratio. So our OD composition was about 26%. Our TP composition was about 74%, which, in this quarter, has come down to 21% and 79%. As a result of this, the loss ratios have got elevated. But this has got compensated by an improvement in the commission and the operating expenses.

Anirban Sarkar: Fair enough Sir. Thank you that is very helpful. Thank you Sir and all the best.

Moderator: Thank you. The next question is from the line of Umang Shah from HSBC. Please go ahead.

Umang Shah: All my questions have been answered. Thank you.

Moderator: Thank you. The next question is from the line of Shubhranshu Mishra from Motilal Oswal Securities. Please go ahead.

Shubhranshu Mishra: Thank you for the opportunity. A few questions. What is the percentage of repeat customers? And what is the percentage of cross-sell that you have in your AUM, Sir? And how do we split this when we look at the growth going forward, Sir?

Kaushik Banerjee: So let me answer the second part first, which is that we have seen a 31% growth Y-o-Y in terms of our cross-sell volume, including tractors. So we have done about roughly what Rs.4200 Crores of disbursement, Rs.4150 Crores. And out of that, about Rs.509 Crores, so Rs.510 Crores is the volume of business that's coming from internal cross-sell. So about 12% of the overall disbursement in the current financial year has come from internal cross-sell and growth Y-o-Y 31%.

Shubhranshu Mishra: Okay. And how do we look at it going forward, Sir?

Kaushik Banerjee: Actually, the penetration level itself are – I am sure you will be either kind of comparing our peer group. So 31% plus at a 40% conversion ratio on – we have generated – we are probably pretty much out there in terms of the efficiency of conversion. And we also have a direct business. So direct business as a percentage of the overall business that we generate is about 40%. So I think it would be quite difficult to go beyond that in terms of the contribution of direct to overall. There may be a certain amount of scope to increase. There is, certainly, scope to increase the cross-sell percentage within the business. But I would say that we will be near peak. Probably we are at about 80%, 85% of where we could be.

Shubhranshu Mishra: Sure. And Sir, what is the opex difference and the credit loss difference for a repeat customer versus a new customer?

Kaushik Banerjee: I cannot do the figures offhand, but it is significantly lower. So basically, at a fundamental level, because we are doing cross-sell, your only payout is fundamentally to your internal team, to your front-end executive and the spotter. So you do not have any external payments to make. So you are very efficient in terms of origination costs. And in terms of credit cost is significantly lower than the overall portfolio because you are lending only to creditors and customers. So both from a perspective of origination cost and in terms of credit cost, the repeat book is a significant outperformer.

Shubhranshu Mishra: I am just trying to quantify, sir, if you can quantify it just in terms of percentage...

Kaushik Banerjee: We do not really track that way, because it is not the aggregate book level. So right now, we cannot really give a breakup in terms of quantification, specifically for this segment.

Shubhranshu Mishra: Thank you so much.

Moderator: Thank you. Ladies and gentlemen, this was the last question for today. I now hand the conference over to Abhishek Murarka for his closing comments. Over to you, Sir.

Abhishek Murarka: Yes. Thanks, everybody, for attending the call, and a big thank you to the management for allowing us to host this. All the best for the next quarter, and hope to be doing this again. Thanks.

Sanjay Chamria: Thank you.

Kailash Baheti: Thanks, Abhishek.

Moderator: Ladies and gentlemen, on behalf of IIFL Securities Limited, that concludes this conference call. Thank you for joining us. You may now disconnect your lines.