# "Mahindra Finance Q3 FY14 Earnings Conference Call"

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**MANAGEMENT:** **MR. RAMESH IYER – MANAGING DIRECTOR**
**MR. V. RAVI – CFO**
**MR. DINESH PRAJAPATI – SENIOR GM, TREASURY & CORPORATE AFFAIRS**
**MR. RAKESH BALDANI – SENIOR MANAGER, TREASURY**

**MODERATOR:** **MR. KARAN SINGH UBEROI – ANALYST, JM FINANCIAL**

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| **Moderator** | Ladies and gentlemen, good day and welcome to the Mahindra Finance Q3 FY14 Earnings Conference Call hosted by JM Financial Institutional Securities Private Limited. As a reminder, all participants' 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 touch-tone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Karan Singh Oberoi from JM Financial. Thank you and over to you sir. |
| **Karan Singh Uberoi** | Thank you. Good evening everybody and welcome to Mahindra & Mahindra Financial Services earnings call to discuss the third quarter results. To discuss the results, we have on the call Mr. Ramesh Iyer who is the Managing Director and member of group executive board, Mr. Ravi who is the CFO, Mr. Dinesh Prajapati who is the Vice President, Treasury and Corporate Affairs and Mr. Rakesh Baldani who is the Senior Manager, Treasury. Shall I request Mr. Ramesh Iyer to take us through the financial highlights subsequent to which we can open the floor for a Q&A session. Over to you, sir. |
| **Ramesh Iyer** | Good evening. I am sure that the results which is being seen by all of you is definitely not in expectations of what all of us thought would have been and when I say all of us, possibly even us to an extent. But I think more than anything else, we are pretty conscious of why this has happened or where has this happened and to what kind of product and profile has this happened and what are the corrective actions that we have put in place which would help us to be able to tide through this situation in the times to come.<br><br>Now, let me first lay out the overall fundamentals, the way it looks like from outside. Clearly, the expectations that all of us had and maybe in any communication that we have had so far was we have felt that the monsoons have been good. Therefore the expectations that the rural cash flows will definitely be much better from the times that we have been comparing it to the previous years. Our answers continue to be "yes". The monsoons are good. The cash flows will hold up. I will explain what has happened in this quarter and therefore, why do we still say that? Second is, we have always said that even though the auto market is not behaving too well in terms of overall volumes, but the rural market definitely seems to offer some growth. While it may not be able to offset the overall de-growth of the auto market, but split vertically between urban and rural, rural seems to continue to maintain growth and we think that that answer still holds good to be true. But what one has to understand is that there are differences between geographies and we have said it in the last 8-9 months that the Southern market is something that has not behaved well and it continues not to behave so very well.<br><br>Now, let us go to the first one which I started off with which is – the monsoon is good and therefore the yields are expected to be good and also the support price required to be. Let us take just three crops in hand. One is the soya from MP, cotton in Maharashtra and the paddy prices that got announced. What has happened in this quarter? Normally both soya or cotton or paddy prices do get announced sometime in October or maybe before middle of November and the entire cash flow comes into the market and we get the benefit of it in the third quarter itself |

and that has been historical. If we go into the past performances of the company, one would see that the third quarter starts showing the improvement. Unfortunately in this quarter, even though the sentiments were very positive and the yields were high, but because of elections in some of the states and the delay in announcement of the final price, the actual cash flow has not come into the hands in this quarter. And when I say it has not come into the hands, it just about started from somewhere middle of or end of December, almost the third week of December and to some extent the benefit of it would have come to us in the last week of December but not time enough to be able to take the corrections. If you look at that as one event which has happened which is against the normal practice and has delayed the whole collection process. That is one very clear thing.

The second thing is again if you look at our book, if you take a vertical split between Northwest and South as one pocket, if your NPAs are high initially, the correction will always happen in the third quarter because the harvest in North is in the third quarter. In this round, the book has undergone a change and the NPAs were high and as we have been saying all the time, from the Southern market. The Southern harvest happens only in January, which is after 14th January, from the Pongal time and we are already seeing some positive signals already coming from Tamil Nadu and Andhra. Clearly if you take this too as a rural cash flow event, then our belief is that what has got delayed in the third quarter, some benefit of it must flow into the fourth quarter and if the post Pongal harvest of Tamil Nadu and Andhra had to hold up, one would also see some correction happening from these two states. Karnataka, interestingly, has already shown some signs of improvement after some opening up of the mining activity, etc., and therefore clearly one would see South as a correction story but will it correct itself as much as it has got built up over the last 10 months, 12 months or more? The answer is “No”. But they are good enough and significant enough to show good positive trend in the times to come. The third is on the heavy commercial vehicle. Again this has been our view that the industry is not doing well and we do not expect that the industry will show any major signs of improvement, at least for the next 6-12 months, if not more and we have slowed down our disbursement to that segment substantially and we have taken a conscious view that instead of rescheduling contracts on any of the contract rescheduling just because the market is not doing well we have taken a view in a business line where we are wanting to come out, we rather repossess vehicles, sell them and book losses, if need be. So, we have taken that view and we have gone ahead and taken and repossessed some vehicles, sold and we have booked some of the losses also in this quarter.

There is one another product segment which is the low-end segment of the three-wheeler and the small four-wheeler which are local, commercial application products and there again the price is protecting the definite credit losses. But accepting that what happens is when you take a decision to even repossess and sell them, it may happen in one quarter whereas the income gets spread all through the period. Now, in this quarter, if we have repossessed some of such products and we have booked a loss and therefore the disposal losses would have gone up in this quarter, one does not expect that every quarter this event will repeat itself once the income of all the contracts will get spread over a period of time. So, the recovery and repossession may be a bunched activity in one particular quarter whereas the income is spread over a period of time and therefore they are a mismatch and one should not therefore imagine "Is the whole portfolio moving in this direction?" These are the very clear three or four events of the market which has resulted into a higher provision and our belief and expectation is that these are not in the same signs and format repetitive in times to come but the market conditions do continue to be highly pressurizing. We have taken very clear corrective actions on the market front.

We have increased our reach in the Southern market to go more closer to customer. We have added more people, we have strengthened our legal team and there are, if you look at our expenses, overheads, etc., there has been some increases that have happened and they have also come from a very conscious decision to increase certain level of operations in the legal front. So, there are some four or five crores which has come through the legal expenses, benefits of which will only flow over a period of time. They are not immediate benefit items but they are required resources to be created. Yes, there is one major expense of about 9 crores of advertisement which we incur during this quarter, which was not there any time in the past and nor do we want to go ahead and do the same in future but that was required to build our direct marketing initiative that we have put in place and that is a one-time expense which has come in. So there are some one-time expenses like advertisement, legal expenses and in Madhya Pradesh, some stamp duty got introduced for which we have made a provision of about 3-4 crores. So, these things have happened in this quarter but they are one-time and we do not see them repeat.

At the same time, as I explained to you, on the recovery front our expectations clearly is that MP and Maharashtra are two great turn around stories of the quarter which if you look at last one year, Maharashtra would have been in the top of NPA list because of poor monsoon, absolute poor crop, no cash flow and they are completely a turnaround story. But as it all got corrected, the answer is clearly "No". They would start happening in December-mid onwards. There is a correction and it will spillover to January and going forward, one would see that correction. Commercial vehicle segment, as I have explained, is a sad story and therefore we pulled out of that business in a big way. Whatever portfolio we have, we think recovery is difficult. We rather repossess and cut loss and dispose-off those vehicles. So, each of these actions must have happened also in this quarter in a larger way and that in a way helps not to have too much of pressure going forward but at the same time, one should not forget that the market conditions are not substantially improving. Southern market has not shown some great improvement signs while they are very positive signs as against what we saw, maybe in the last 12 months and 18 months. So, that is some good story to look at there. All of this put together and with the operational decisions of increasing our reach, increasing legal penetration, increasing field level of people, will definitely push up the recovery and this one-time expenditure that we saw that is getting incurred or even one-time provisioning that has happened.

There is one another account that I may want to explain. There was an SME account that we had and there was a fire in the factory and they wanted a reschedule to this. We have taken a view that we will not reschedule any contract irrespective of which category of customer it belongs to and the reasons for which the reschedule is called for and therefore we had to make a 10 crores provision arising out of that account. Now that is also not repetitive in nature to say "Oh, again will in next quarter will the same thing repeat?' The answer is clearly "No". But each of these therefore, certain things are one-time, certain things are market, delayed cash flows and delayed activity out there and some of them are just about improving. As I said, South will always be post January harvest improvement which we have never witnessed in our books in the past. We have always seen correction in the third quarter because the improvements are from North and west. This is the first time that the Southern market is going through this cycle, which as a company we have always only the Northern market which has gone through this cycle. So, the expectation was that third quarter will start showing the improvement whereas since the Southern market has to improve, it will only show in the fourth quarter. Now, I am not believing that all of this will get corrected in the fourth quarter but we are surely believing that the pressure in the fourth quarter would not be possibly as high as we see it in the third quarter and our corrective actions will also guide us towards the same direction. In as much as disbursement is concerned, inspite of the fact that the overall market has been a very submissive market, auto market has not grown. Tractor has shown some signs of growth. The second-hand market is holding up decently for us but we still registered a disbursement growth of close to about 10% as against the previous quarters which were even lower. But our focus will continue to be ensuring that we take benefit of the emerging cash flow situation, go closer to customer, opening more branches and ensuring that when the cash flow in the market is available, to pick up the money rather than over-focus on growth. So, the growth by itself will happen at certain percentages based on the volumes that are available from the manufacturer's penetration and growth story. But I think the focus for the quarter would definitely be and this I have said in the past, that given a choice between business and collection, where will the effort and focus be? We have always felt that the efforts will be towards more collection and correction of quality because when the cash flows are available, we would like to take the complete advantage. I think that is the way we will look at things going forward. There is absolutely no pressure in as far as the lending rates are concerned. I do not think there is any need for us to bring down the lending rates, even if for any reason, the borrowing cost had to come down. So, there is no pressure on that kind of a margin front in terms of volumes or in terms of pressure on margins to get some volumes. Absolutely there is no pressure. We are conscious of what products will we want to do and what we will not. Given what we see in the market, I do not think we will open up financing of commercial vehicle for at least next 6-12 months. That does not seem to be the indications of the market. Even if market was to open up, projects were to come in play, I think there is enough corrections from the existing portfolios that have to happen before one can start getting into new purchases. One last thing is repossessions have always been an answer to a business like this, which is collateral based. But looking at the market conditions, even the resale prices are not very favorable. Therefore, our view is instead of repossessing and cutting loss from every product line, yes – a product which we do not see any improvement for next 6-12 months – we do not want to delay, as I so told you about commercial vehicle but in every other product, there is a pressure. We do not want to repossess vehicle but we are not able to cut loss by simply repossessing. After all, we have to select in the same market. So, it does not make sense to repossess vehicle when the overall market condition is not favourable. We have exactly taken the same decision four or five years back when the gross NPAs were high. There was a choice in front of us to either repossess, then cut loss or stay put and delay the decision. Market conditions improve, recover the money. I think we are very clearly seeing the signals that the market conditions would improve for product lines of this nature and therefore there is no urgency or hurry to repossess. We are able to see the vehicle make the customer. Wherever we think that the collateral depreciation is higher or the product line is not holding up like commercial vehicle, we will still take the view going forward. But today is not the time when we want to get into any repossessions and work on the basis that book losses because, after all, you need to sell it in the same market. So, we will kind of participate, partner the customer, not reschedule any contract but take benefit of the emerging scenario, as and when the cash flows come into the market, like we will see lot of action in MP And Maharashtra, maybe during even this month. We will start seeing actions clearly in Tamil Nadu, Andhra from this month onwards. And our expectation therefore that if these cash flows do happen the way we look at it, we do see corrections happening but they will not be large enough to bring about all corrections that have got accumulated over the last 12 months to all get done in the next three months.

I think that is the way I would put in to the summary. But then through Q&A we can answer the more specific. And if you have any specific data explanation requirement, we have the whole team here. We can provide that to you as well. Thank you.

**Moderator** Thank you very much. We will now begin the question and answer session. The first question is from the line of Kunal Shah from Edelweiss. Please go ahead.

**Kunal Shah** Sir, thanks for the entire explanation. Sir, when out to a year, maybe in terms of the pricing, since we really saw that this other market is giving some kind of a pain and some product segments are say, showing a higher stress, are we passing it on by way of say, higher lending rates, so that maybe at the overall return levels, it does not get impacted? So, how would we see it, in terms of say, higher credit cost? How are we seeing it in terms of the pricing of the product?

**Ramesh Iyer** I think, at this stage, it may not be very advisable to cover losses through pricing on these products. So, we would rather put more efforts on timely recovery or more frequent recovery. I would not even call it as "timely", more frequent recovery. And from whichever account we are recovering for sure, we are trying to build pressure to collect the penal charges for delay and protect the returns rather than charging a new customer a new price. Because there is already pressure in the market on volumes which is also a part played by the rate pressure. And there is no point in over-pressurising that situation. And as I explained, even in the last two quarters, we are in continuous dialogue with manufacturers for subventions, both in terms of cost of subvention, wherever possible. And now with this kind of delinquency in terms of three-wheeler losses or a Maxximo loss or a Tata ACE loss or whatever, we would re-dialogue with all these people. We do not want to take a credit support for future lending but we are in a position to negotiate for the actual loss book and get it subvented to some extent and of course, delay payment charges charged to the customer to protect the returns rather than charging a new customer a new price.

**Kunal Shah** And sir, would it be possible to quantify to some extent as to how much would have been the stress in the Southern market and how much would have been say, on account of the commercial vehicle repossession, which he has done in terms of how much of the numbers? Last time I think the repossession, what he highlighted, was like 1500-2000 odd vehicles. So, has that trend moved up significantly?

**Ramesh Iyer** The number of vehicles repossessed or sold?

**Kunal Shah** Yeah, repossessed and disposed-off.

**Ramesh Iyer** Repossessed numbers would be same in the range of 1500-2000 kind of a number. But I think, more importantly the first one that you asked, "how much will be from the Southern market?", I think, out of our total NPAs, say gross NPA of Rs. X, at least about 40-45% will be from the Southern market because South for us as a volume has been a large market, in any case. As far as disposal of vehicle is concerned, please understand that it is commercial vehicle and I said the low-end vehicle like the three-wheeler, Maxximo, Tata ES, those kind of vehicles as well. Repossession typically per month is anywhere between 1500-2000 vehicle. But just since you asked the question, let me also give you one more clarification. Earlier, when we used to repossess, take back a vehicle, let us say in some markets like Southern markets, or even west, etc., many times the customer used to come for a settlement in certain range. Given the market conditions today, he is not in a hurry to come back and take because he is not able to settle the full account immediately. Therefore, we have to be cautious not only just in repossession, but also in selling of those vehicles because the market prices do not hold up. Which is why, we are cautious on even though our NPA may grow, we are willing to stay with that new NPA number because we know they are temporary market conditions and they are not a failure of appraisal or over-lending parameter like high LTVs or anything. NPAs are not built because of poor quality of assets in terms of lending conditions or they are not built because of very high LTV. They are not market-share-bought NPLs. They are market condition NPL and therefore the behaviour of the financial has to be market-like. There is no point in repossessing a vehicle where the collections are suffering. The resale price will be half the price. We want to stay with the market. We are seeing it on the ground what is the reality. We are penetrating deeper to say, as much as you can, you keep collecting. And one correction that will happen maybe during the quarter will start, showing signs of substantial improvement. And we have gone through this in the past. It is not a new phenomenon to us except that his phenomena earlier used to be in the North. It has now shifted to South. That is all is the difference.

**Kunal Shah** Sir, what we talked about, say the stress in tractor, which you mentioned, should correct seasonally?

**Ramesh Iyer** Not Tractor, sorry. I did not say "tractor".

**Kunal Shah** No, last time you highlighted that there was some stress in sectors which should seasonally correct as we move into October. So, has that come in line with expectations? Or on account of that also..?

**Ramesh Iyer** Tractor, if you see even the business growth, is an outcome of the market correcting itself and therefore, recovery has also shown the same. But please read it with the delayed cash flow which has happened in Maharashtra and Madhya Pradesh. To that extent, the correction would not have fully come in, in this quarter.

**Moderator** Thank you. The next question is from the line of Anand Vasudevan. Please go ahead.

**Anand Vasudevan** Sir, you mentioned that you are seeing crop cash flow related stress on your portfolio. Just to understand, is this on the tractor portfolio or is this the reason for the stress on your CV portfolio as well?

**Ramesh Iyer** No, it is a rural portfolio. One, even though the vehicle may not be for harvest or it may not be for direct agri application, but the fundamental cash flow does come from harvest, as one of the important contributor in the rural market and therefore the sentiments. Even though they may have the money, they will like to hold on until they see a fresh cash flow coming in.

**Anand Vasudevan** Are you seeing stress on the tractor portfolio as well as on the CV portfolio?

**Ramesh Iyer** If you take Madhya Pradesh and Maharashtra as one geography where the cash flows got delayed, we would have definitely seen the tractor correction is not as much as it should have happened in the third quarter. As far as CV is concerned, they have no relation whatsoever with the crop price or harvest. They are purely economic conditions, whether it is project related, whether it is container movement related or whether they are goods movement related. So, the overall rural cash flow impact that we see, let us say in Maharashtra, MP or even parts of South which will correct after the 15$^{th}$ Pongal festival at the harvest time, would all be related to individual owners of vehicle like small pick-up, three-wheeler, small three-wheeler, commercial application vehicle, those kind of products and of course, tractor being a part of that trailer.

**Anand Vasudevan** And what is the customer profile in where you are seeing stress? I am trying to understand first of all the vintage of these loans and also if the proportion of new customers is higher among the stress portfolio.

**Ramesh Iyer** In a way, if you look at our coverage, if it is 55-56% coverage which means the NPAs are in the first bucket. But not necessarily they are from one year old customer. The customer could also be paid for 12 months but not able to pay the next five months. So, it is not that all new customers who we have entered into a loan this year have all become NPL. We look at all the NPL number by number. Last December (December '12) we had about 48000 customers, let us say, in the NPL out of the total of two million. In the one year space between last December to this December, we have done close to half a million customer as new business. Whereas the overall increase in NPL number of customer is only about 9000 customers, which means that some of the customers who are already in NPL is also moving up in the age, which is purely market related and some of course, the new ones which have paid maybe five months, six months, seven months and not able to pay the next few months. So, you will have a mix of everything. It is not a pattern that is emerging to say "Okay, this type of customer or this period of customer is getting bad". It is more market geography oriented rather than any particular profile or any particular age or any particular period. That is why I said it is not arising out of poor appraisal or high LTV. It is not "dosh" of the customer. It is purely arising out of the economic conditions of the market which is delaying the whole repayment.

**Anand Vasudevan** You mentioned that you are pulling out of the market in the CV business. I want to understand which markets are you pulling out of?

**Ramesh Iyer** No. First of all, when we got into it, about 18 months or 2 years around that period, we never became a significant player. By the time the market started showing signs of crack where the demands from the customers were very erratic. They wanted almost 100% finance, five year loans, seven year loans. Then the discount on the products started coming in. So, we kind of already rolled back from participating in that segment in a big way.

**Anand Vasudevan** Are you talking about the M&HCV market?

**Ramesh Iyer** Yeah. Medium and Heavy Commercial Vehicle. Not the LCV. LCV is still holding up. The pressure is not high. While their numbers have also come down, they are not badly behaving as as the M&HCVs.

**Anand Vasudevan** Have you taken a decision to exit the M&HCV market?

**Ramesh Iyer** Exit is not the right answer because we were never a significant player. But, yes, we are not participating in that segment that is never going to be growth driver for us at least for next 12 months. And M&HCV for us in a book now will be not more than 2% is my guess. Because our entire LCV, M&HCV and small construction equipment together itself is only about 5-7% and M&HCV will not be more than 2% because we have not grown the book at all after that.

**Anand Vasudevan** In the Northern markets like UP, there is a law and order situation. So, is that in any way affecting collections or have you had to make any adjustments to the way you do business to deal with this issue?

**Ramesh Iyer** Actually, those law and order situations that we see in a state sometimes get projected in a certain period of time but those states, in at least the last 20 years that we have worked there, have been no different. And in fact, as we speak today, UP is one of our best state in terms of collections, low NPA and a better business.

**Anand Vasudevan** You are not seeing any worsening of behaviour out of this?

**Ramesh Iyer** No. These kind of states always have certain group of people and certain group of activities in which they are busy. You will never see U.P's businesses coming to an end as there is some problem out there. They co-exist actually.

**Anand Vasudevan** And a final question is I would like to understand what will be the structural cost impact of the corrective actions that you have taken. You have said that you wanted to be closer to the customers. So, more field staff, perhaps more branches, more support staff. What will be the impact?

**Ramesh Iyer** As far as support staff is concerned, I think we have already incurred it and you will see some cost of it already reflected in the third quarter. Nothing new is going to come in. As far as more branches are concerned, this are typically three people, four people sitting in one small office of 300-400 square feet. As a matter of fact, my understanding is the conveyance that we will save as a cost should offset the rent that we will pay for those branches. And beyond that, there is no new cost because the same set of people who are otherwise sitting in a branch 50-70 kms away will now move to a 25 kms away. So, there is no substantial increase in number of people. There is no new facilities provided to them. It is just that a new infrastructure in the form of a branch gets opened. We just have a rent of about Rs. 4000-5000 a month and the conveyance that we would save is in fact normally better than this but at least equal to this.

**Moderator** Thank you. The next question is from the line of Hardik Shah from Birla Sun Life Insurance. Please go ahead.

**Hardik Shah** Sir, I would like to find out about the write-off that was there in this quarter?

**V. Ravi** Write-off includes the termination losses which is around 39 crores.

**Hardik Shah** And what was the figure last year, in the previous quarter?

**V. Ravi** Previous quarter includes bad debt. We have a policy every September and March. We provide for bad debt also which was 106 crores.

**Hardik Shah** In the previous quarter? Okay.

**Dinesh Prajapati** These figures are not technically comparable, uh.

**Hardik Shah** Okay, got it, sir. Secondly, sir, what would be your portfolio mix be like as of now? And how would you see it in next say, one year?

**Ramesh Iyer** When you say portfolio, I am assuming M&M, non-M&M would be kind of 47-48 M&M and 50-52 non-M&M. One minute, Dinesh is just pulling out a sheet. Is that right?

**Dinesh Prajapati** Yeah.

**Ramesh Iyer** And within that 45-47 that I said, 30 odd would be the auto sector portfolio and about 16-17% would be the tractor portfolio. On the other, either the 50-53, above 35 would be cars. You will have about 5-7% or 10% coming from the commercial vehicle construction equipment, including LCV, etc., and 8-9% will be from second-hand vehicle segment.

**Hardik Shah** Sir, lastly what would be the LTV that you have right now?

**Ramesh Iyer** 71%, I think.

**Dinesh Prajapati** Yeah. 72%.

**Ramesh Iyer** 71-72.

**Hardik Shah** Sir, lastly what is the average cost of funds?

**V. Ravi** 10.18

**Dinesh Prajapati** 10.2

**Hardik Shah** Sir, in a geography-wise focus are you doing any change or you will continue having a similar focus in all the geographies?

**Ramesh Iyer** I think the business growth will come from non-Southern states largely and collection efforts will be much higher on the Southern states as against the other geography.

**Moderator** Thank you. The next question is from the line of Ashwini Agrawal from Baroda Pioneer Mutual Fund. Please go ahead.

**Ashwini Agrawal** Sir, just wanted to know how do you see your gross NPAs behaving because from 4.1 it has jumped to 5% in the quarter. Do you see it going down in the next quarter to around a 4.5% or will try to maintain this level?

**Ramesh Iyer** Last quarter when we were asked this question, we did say that the worst it could go is up to five and we have had very worst experiences maybe 5-7 years back when it had gone to 10 and 11and we said we do not see that they were coming back.

**Ashwini Agrawal** Sir, I am talking about little recovery. Is it possible? Have you for Q4?

**Ramesh Iyer** Clearly, the answer is "yes" for the simple reason that all this lending is backed up by collateral and as I repeatedly say, "they are not market-share purchases". The LTV is only 70% and they are not accounts where there are absolutely no movements. It is just that the delay in recovery arising out of the current market conditions. We do not want to be in a hurry to say, "Okay, we want to make all these corrections in this quarter", and therefore collect money or repossess vehicle will not be our approach. We are very clear that this will need patience and time because the cash flows have just about started coming. The market conditions are just about improving. We will put in our best efforts through various resources that we have created in these three months. Repossessions will only be done in extreme cases where we think customer has absolutely no ability to repay or the asset is getting misused as otherwise, we will partner and collect the money. But we will not reschedule a single contract, even if we have to explain this level of an NPA at any point of time.

**Ashwini Agrawal** Sir, as you had mentioned earlier, election time is not a very good time for a financial. So, do we see some decline in the loan growth as compared to what you have done over LTV?

**Ramesh Iyer** The elections would naturally spill over to next year, sometime in May or so and they are not going to be kind of more than a month phenomenon. I think it is not right to take a view on the whole year based on one election. But who knows? The outcome of the election will decide the direction for the country and therefore direction for the people who participate in that.

**Ashwini Agrawal** Another question. Is there any kind of a feeling in the rural area that the government might come with a loan waiver or something like that which can hamper your operations and others too?

**Ramesh Iyer** No, but loan waiver, even if they come, that has not hampered us ever because that is a very low-end financing like micro-finance kind of equivalent. Loan waivers are never given to people who bring in 25% margin money and margin money values are about Rs. 1-1.5 lakhs. These are all collateral assets worth Rs. 4 lakhs and Rs. 5 lakhs; they are not the loan waiver farmers or customer. They are marginal farmers the small micro finance borrowers who borrowed Rs. 10,000-20,000.

**Ashwini Agarwal** Sir another thing, can I know what was their interest income right back because of slippages?

**Ramesh Iyer** 40-odd crores.

**Moderator** The next question is from the line of Shrey Loonker from Reliance Mutual Fund. Please go ahead.

**Shrey Loonker** Just wanted to understand, you mentioned that there was some geographical misbalance because of which there was a timing issue in Q3, but within the same geographies where you had a cash flow pressure there were not any other product lines where you see some pressure because in your opening remarks you did mention, except M&HCV

**Ramesh Iyer** M&HCV and 3 wheelers and the small sub after.

**Shrey Loonker** But they would not essentially be part of the same rural cash flow chain right because the LCVs and the small 3 wheelers and all….

**Ramesh Iyer** No, I thought I clarified it, M&HCV has nothing to do with rural cash flows. Everything is to do with the current economic condition. As far as the 3 wheeler and the small sub after products are concerned, they are like tractors, like pick up related to the rural cash flows.

**Shrey Loonker** But Sir is there anything that leads you to suggest that this customer segment by itself is coming into a somewhere the retail end of the rural that seems to be kind of slowing down?

**Ramesh Iyer** Let us look at it like this, we have 2.7-3 million customers and we are talking of 50,000 cases delinquent, so I think it is not judgmentally correct to say that one segment is going into that direction. Okay, that is one and I also said that it is largely the pressure is in South and it is not all India phenomenon. And we had similar situation in the past where it is from North and not from South, so it is by historically one can see different geography at different point of times have behaved this way and they are purely related to market conditions because these products are need based products, they are not aspirational product. What is the alternative in rural India but for a 3 wheeler, but for a small vehicle in which people will travel? What is the alternative in rural India for transporting these loose goods from a point-to-point other than these vehicles? What is the alternative to tractors in the farm? What is the alternative to farm output being carried not by a tractor, trailer but by anything else. Our railways or our, the public transport systems do not support that there is an alternative, only when that happens one can see that this is an issue. In the current scenario, the acquisition cost on these goods are also very high. The operating costs have gone up, for them the fuel price is going up, interest cost has gone up and possibly the economy is not supporting the income side of that customer to that extent, therefore this temporary pressure.

**Shrey Loonker** And Sir any particular reason why North did not behave the way it supposed to in Q3?

**Ramesh Iyer** North behaved extremely well, the way it was expected, except MP and Maharashtra, the soya price and cotton price, even though yields are out, the price did not get announced and even after the price got announced the cash flows were made only now. Like if you look at MP, the mandis were closed post-election and they just opened about a week back. As far as Maharashtra is concerned, cotton price was announced only yesterday but the good news is as last two three rounds the price was Rs. 2000, this time it is Rs. 4000, in spite of yield being higher. So, it is just a delay of cash coming into the hands of the farmer, from normally one would see this happen before mid-November and money starts coming in sometime end November to get the situation corrected. It has got delayed; obviously the delay would have been negotiating for a better price in Maharashtra and election in Madhya Pradesh.

**Shrey Loonker** Sir just two more questions. One was except the food chain which is part of strictly the cash crop cycle; apart from that you are not seeing any significant slowdown in any of these geographical pockets?

**Ramesh Iyer** No, as I told you in fact North has been a turnaround, so UP today is one of the best behaving state for us in terms of business and collection is concerned. Rajasthan is a great change that we are seeing. Bihar continues to hold well. It is the Southern state and it is not just this quarter, we have been saying this for the last 12 months that South is not behaving the way one would expect it to behave and we do see that unless that correction happens it will built up and now we are seeing at least Karnataka is opened up sometime from December. Andhra minus Telangana has behaving well with better crop. Tamil Nadu has started showing signs of improvement in January. So, we have to see how much more does this happen and how quickly does this happen.

**Shrey Loonker** Sir this mining opening up in Karnataka at a margin, are you seeing some optic increase, some inch up in second hand asset prices or anything of that sort?

**Ramesh Iyer** I think I will immediately we will only see a better cash flow at least the existing vehicles will get deployed better, therefore some collections will start happening and maybe some outstanding bills of this contractors may get cleared but it will not immediately result into a big new business because see you must understand even the contractors will be a little vary of investing in capital goods at this stage, unless this mining really opens up like before in a very big way. Because who knows when will again it get shut after 3 or 6 months. So, new asset purchasers are not able to over project and that is the reading I get from Ashok Leyland or Tata whenever they speak as well but existing operators or the contractors would feel better because at least the cash flows will start happening in the next couple of months.

**Shrey Loonker** And Sir on the pricing front of the eventual asset, could you just give us some price trend that you would have seen over the last 3 months in the first hand and in the second hand market? How have they moved directionally?

**Ramesh Iyer** Actually January the prices have gone up from anywhere from 2.5-5% to even up to 9-10% for different product range. Pre-January it was a discounting market, the discounts were as high as 8-10% on certain products and even up to 5% on certain products. My personal opinion though is that even though the prices have gone up, if they see the volume pressure, it will come back in the form of a discount.

**Shrey Loonker** And Sir would the prognosis of second hand asset prices correcting a little more than the first hand still true? The asset price deflation that we have seen in the first hand is it mimicking exactly the same, in a very linear fashion even in the second hand asset market?

**Ramesh Iyer** No, it will not. See, whatever be the discount of new vehicle, it is in terms of the price, it is double the price of a second hand vehicle and in an economic condition like this people would like to use second hand vehicle rather than buying a new vehicle when they are not sure of their recovery or their freight price, etc., on the other side. So, typically what happens is, when you see second hand vehicle price dropped, you would see them that their vehicles which have been used more than normal. So, the second hand pricing is not just purely on the basis of age-to-age, it is also on the application and the kilometer run. So, if a vehicle which is let us say sold after 3 years in a normal condition, it will be 60% of a new vehicle price. Now when the new vehicle is discounted by 10%, one would see in that situation a linear drop also in the second hand vehicle but if the second hand vehicle is now doing extra work because not too many new vehicles are being bought, when you then look at such a used vehicle the price will be little more dropped but it would have earned better.

**Shrey Loonker** And Sir on the subvention part, do you expect the negotiations to gain because I presume even the OEM s are facing severe margin pressures, how do you see that kind of play out?

**Ramesh Iyer** It will play out geography-by-geography and product-by-product. Like if I go to Maruti and negotiate with them for their cars like Alto, etc I will get nothing. Because they are reasonably sure that the vehicle is being sold on its own and they do not really need to offer any major sub venture to anybody. But vehicles in which we have lost money, including in M&M suppose a vehicle like a Maxximo or A, B, C, D vehicle, we go and negotiate to say “sorry! we would not be able to support the product unless there is a protection”; surely one would give, like Tata will give for some of their vehicles. So, we have to be very choosy about product and manufacturer and the location where our importance is higher for their growth.

**Shrey Loonker** So, this process would have always been on in the last 9 months right? We should not read it as the efforts are intensifying in Q3?

**Ramesh Iyer** No, nothing new and nothing substantially change has happened. It is just that the pressure from our side will be little more higher, having seen some factual figures to now go and tell them that it is as high or even higher than we expected, so we need this very urgently.

**Moderator** The next question is from the line of Anish Tawakely from Barclays. Pleased go ahead.

**Anish Tawakely** Sir I actually am a little bit confused about whether the stress is due to weak sentiment or actual weak cash flow? And if it is sentiment, I can understand consumers delaying purchases because of sentiment, I am a little confused as to why they should not make payments against because of sentiment?

**Ramesh Iyer** So, let us take Maharashtra and MP under the sentiment category. The crop is in hand, today we know even the cash will come because the price is also is announced but 15 days back crop was in hand, price was unknown. The sentiments were positive because yield was extremely good but willingness to pull out the money in pocket was not sure because he wanted to see at what price his crops is going to be sold and therefore how much more money he is going to have. That is what drives the cash flow out from the pocket when I say sentiments are positive but repayment is not happening because they want to see the actual cash flow.

**Anish Tawakely** And the other thing I mean how does this work, right? I mean these are MSPs so they are support price; they are actually not procurement prices. The sale is made to a private party, it is not really made to the Government?

**Ramesh Iyer** Yes but he may not be made to the Government but Government price is what he will also get when he sells to whomsoever. He is not going to sell it at lower than that.

**Anish Tawakely** So, he is just sitting on the goods?

**Ramesh Iyer** Yes this is what has happened. You take soya, only about a week back or so the mandis have opened.

**Anish Tawakely** See, actually the reason I am pushing on this is the following, we are saying that, “look we are not re possessing vehicles because the repossession would mean that you just repossessed them and their market price is lower”. How do we know that the customer is not being smart and saying “hey let them repossess it, the value of the vehicle is less than the loan”, do we really have that much visibility into their cash flows as to whether they have the cash or they do not have the cash, we would not really know right?

**Ramesh Iyer** Why we would not know? We are meeting him every month to collect our installments and we are in the local market. You ask me about any market more even into detail absolute district level, we will provide you information on particular information that you may want. Let me clarify just one more thing, first time in our 18 or 20 years of this business we are facing this. That is why I am making this debate.

**Anish Tawakely** So, you are absolutely confident that there could be no situations where the customer has sold his produce, have the cash and is not making the payment.

**Ramesh Iyer** Let us be clear. There is not just one customer who is in this business in that area, so if one person is selling and not paying, many more would have sold and somebody would have paid. I can understand if every customer is unique, then you will not know but it is a cluster. If you go to the soya belt of MP there will be thousands of farmers who are selling their soya, how can one person tell you that I have not still sold, when 999 have sold there.

**Anish Tawakely** And what would be sort of the pipeline of earlier stage delinquencies if you were to look at like because your NPL recognition is 5 months, what would be the delinquency levels at 120 days, 140 days or something like that, which could become NPL?

**Ramesh Iyer** We did some working when it becomes 90 days let us say. The gross NPL from a current 4.7, I mean that time it was 4 would have moved up to 6-6.5. Maybe, now 4.7 may go up to 7. So 2% increase one can look at when the delinquency drop from, see another thing one should also know that when somebody is putting in 25% money. Normally first 90 days he is not highly delinquent. Because he also needs to ensure that his margin money, recovery must happen in case he loses the vehicle. It is only from the $5^{th}$, $6^{th}$ or $7^{th}$ month when he is not able to hold on continuously through the cash flow that the delay starts. I think you will be surprised if you look at our NPL accounts, they are not absolute non-payment forever. They are not able to meet the installment obligation and we have taken a view not to reschedule any contract. Otherwise technically this 3 year contract that we give to somebody, his expectation is can you make it 48 months and bring down my EMI to some level. So that I service it fully and we will not have an NPL. But having contracted for 36 months we do not want to reschedule, we rather live with an NPL and collect as much as he can pay and come out of it as and when he pays it rather than rescheduling and getting into a mess.

**Anish Tawakely** In the past cycles have second hand prices dropped as much as they have this cycle or this particularly severe?

**Ramesh Iyer** We have had similar experiences at different point of time for different products. See even now the second hand prices have dropped for commercial vehicles substantially. Maybe the 3 wheeler, maybe the sub-0.5 tonne vehicle, it is not dropped for Boleros or pickups or cars. They have not dropped as badly

**Moderator** Thank you, the next question is from the line of Sudhanshu Asthana from Axis Mutual Fund. Please go ahead.

**Sudhanshu Asthana** Just wanted to get a sense, this gross slippages and NPAs plus the write-offs, how much of is CVs and how much of it is because of the other product lines? Can you give some sense on that?

**Ramesh Iyer** You want to know byproducts of…..

**Sudhanshu Asthana** I just want to see that whatever accrual of NPAs has happened, see you have taken some amount of write offs and there is some amount of gross NPAs so write-offs are getting knocked off from the NPA gross.

**Ramesh Iyer** I can give you some flavor on it. Let us say, if Rs. 100 is written-off totally, I would estimate that 3 wheeler than that sub-0.5 tonne vehicle which I said Maxximo and ACE kind of a vehicle and the heavy commercial vehicle which contribute to at least 60-70% of that write-offs.

**Sudhanshu Asthana** And what about the accruals of gross NPAs which has happened?

**Ramesh Iyer** It will again, you will have CV as one of the highest because if you have not reposes all of that portfolio as I said so even though the portfolio is coming down, we have not kind of corrected the whole portfolio either by repossession or say.

**Sudhanshu Asthana** I just wanted to understand write offs plus gross NPAs, if you are saying CVs or something like that?

**Ramesh Iyer** See after all the sector if you kind of put, I mean all geography taken together. Let me first give you by geography. I think four South states contributes to about 45% of our total NPA at this stage because of the current conditions being there for the last 10-12 months which is now some signs of improvement is visible. Now within this if you see, CV by value itself they will be the highest, therefore they may be 10-12% of the total NPA. You may have within auto sector product; people have everything from pick up going up to 3 wheeler will be 8-10%. The tractors are showing signs of improvement may be 5-6%, would be tractor of this. And you will have cars which are also in the same range of about 7-8%, but within cars if you look at commercial application v/s personal cars segment, there could be a different percentage.

**Sudhanshu Asthana** I think idea which we were trying to get was that if you look at the delta of the NPA formation, just wanted to get a sense that the recognition of cash flow was not there and CTO more on the CV and may be on the ACE type of vehicles. So let us understand that going over the next 2, 3, 4 quarters, the accrual which will happen on the NPA.

**Ramesh Iyer** According to me if we do not get into heavy commercial business, the decision that we have taken, one would see correction there because we do not expect next 12 months any change in the commercial vehicle behavior. And therefore one would see drop of NPA, absolute value because they are heavy priced products and we are not into that in a big way. So far as the other products are concerned whether it is car, whether it is pick up, whether it is AS type vehicle, the geography in which we work, sentimentally will be driven by what is been the monsoon, what has been the crop output, and what is been the economic activity which uses these products. They are not historically very different except geographically they will keep switching.

**Sudhanshu Asthana** So what I was trying to understand is the CV market is bad, so most of your CV, loans are in a segment where the system itself is bad. Just trying to get a sense that as an accrual of 300 crores plus of gross slippages plus your write-offs, how much is the onetime kind of an impact because if you are not going to disburse more CVs and because you have recognized more CVs, how much is that onetime impact? You will recover money later on but from a cash flow perspective all the things just slipped in to gross NPA, they should be recovered if the cash flows come back.

**Ramesh Iyer** According to me, 70% of this will see correction in the next 3 months, 6 months kind of a thing as Southern markets starts improving. The 30% of it will see improvement only if the overall economy improves which is commercial vehicle based.

**Moderator** Thank you. The next question is from the line of Manish Chaudhary from IDFC Securities. Please go ahead.

**Pramod** Sir this is Pramod here. My first question pertains to the tractor segment. This as a user segment has grown by more than 25% YTD and how do you see this segment growth? And because your financing will also depend to a great extent on the underlying industry growth, what is your view on the 4th quarter and probably for even the next fiscal?

**Ramesh Iyer** See the tractor sales, I am just talking about the sales even in the 3rd quarter, the registered sales was good of tractor. And that is coming from a good harvest therefore better use and local application. Even though no major projects, etc., are announced, the tractor in terms of its application at the haulage local is still continuing to happen which is why even I said in our tractor portfolio we have seen an improvement in terms of overall collection and reduction of an NPA is concerned. But again it is very important to understand. I am repeating this over and over that a geographical split is a must to understand that even in South, even the tractor sales have not been as attractive as the overall country's sales have been. And like wise, therefore the collections are also reflective of the same by geography. But will it forever remain like this? No because if you look at 18 months back, may be the North did not show so much signs of demand as well as collection from those segments. And South was doing well. So I think cyclically, when things do not go well, in different geographies you have different behavior at different point of time. In our case at least it is after very long that South has behaved this way. And it has behaved for a longer time, this time you can see every company which is South based business or South based recovery you will see this issue being faced by them. I was just looking at Ashok Leyland's number, for the last three quarters they have not done well because they are so very South based in terms of their market share. So the market seems to be not still improving for showing corrections. The visibility at least from mid-December and then after Pongal the clear visibility is positive on South. At least Karnataka surely because some mining activities are recommenced, rains were kind of average plus. So I think Karnataka is the first to show the correction. Andhra is the second to show the correction minus the political belt. Andhra has shown correction. Kerala had something very unique at least what we saw was from our profile of customer, that people, the Gulf money of salaried people which got impacted about 12-18 months back. And all resorted possibly to pledge gold and borrow. Unlike other states, where people take from money lender, Kerala people pledge gold and borrow for their needs. And they have first repaid those installments when the money flow started. And which has what has created over due in the books of people who are in asset financing in Kerala and we have already started seeing correcting those. No sooner they have finished that loan, they have started repaying this loan. So there are different phenomenon installed which is working. Tamil Nadu is the last to react positive because if they had problems of farmer, they had drought in 30-40 districts. At this time around Cauvery water flow is good. The monsoons have been average. I will not say very good but I have told the paddy prices is good, sugarcane is expected to be good, so Tamil Nadu will also show signs of correction and the sentiments are positive.

**Pramod** So, in a way, next year South may play part in terms of demand recovery and help the tractor growth.

**Ramesh Iyer** I would think so but from commercial vehicles side, South is a big market and they will not play a part because overall economy has to improve for commercial vehicles to do well.

**Pramod** And how would you look at the second hand tractor market because you talked about second hand prices for commercial vehicles and everything as a trend but in tractors any signs of price trends what you are looking in the second hand tractor market at this point of time.

**Ramesh Iyer** See second hand, unlike in cars and pickups and all, application of second hand and new vehicle is to the same application. In tractors, the application is all different. So, therefore second hand tractor price will always be guided by the quick ability to recover that money through application. Like for example, normally people buy second hand tractor for hiring purposes or haulage purposes and less for farming purposes full time. And you will always see that is how the price pressure is. Even when we repossess and sell a tractor, if a tractor is bought by a farmer for his farming, the price is much better because he is willing to live with the tractor for 7 and 9 years because pure farm application life is 9 years. And no sooner is most to haulage application the life is 3 years. So, what he does is, he bargains for a shorter period loan of 1 year and 2 year, even in second hand financing of tractor and also prices it accordingly but extremely uses it and recovers all his money. So, the pricing of tractor unlike UV or whatever is not by product but it is by application.

**Moderator** The next question is from the line of Amit Ganatra from Religare Invesco. Please go ahead.

**Amit Ganatra** Just two questions from my end. One is that, in the past you have mentioned that whenever there is a drop in collection efficiency that is the time you will see slowdown in terms of growth, so now basically would you guide that there should be some sort of slowdown in at least in products whereby there has been drop in collection efficiency?

**Ramesh Iyer** No, clearly we are saying that commercial vehicle is anyway have come out and to that extent our book is not growing through that. And therefore if you have grown only 9% disbursement this quarter and it would have been another 4 or 5% if you have participated in commercial vehicle that is one. And between therefore minus South and others if you look at, I think South would actually be a de growth for us in terms of growth rate is concerned.

**Amit Ganatra** And the other question is that typically both quarters sees a very sharp reduction in gross NPA that has always been the trend in the past. Do you expect this trend to continue even for this quarter?

**Ramesh Iyer** Expectations and realities have to be two different states but see clearly, I will not say that we will see the same that we saw all the time in the past, the answer is clear no. Because the economic conditions are not as attractive as it was maybe last year and the year before, that is one. Second is, even though the NPLs have moved up, the high bucket NPLs are not very high, otherwise the coverage would have been very high. And therefore in the past if you have seen such corrections, they would have been out of solving high bucket NPLs as of a repossession or negotiation settlement. So, if you look at the current trends, the provisioning is 55% cover or whatever, so even if corrections happen you cannot see the same trend as that you saw in the past because it is only the 10% bucket correction which will happen.

**Moderator** The next question is from the line of Shantanu Chakravarthy from ICICI Securities. Please go ahead.

**Shantanu Chakravarthy** I would like to ask a couple of housekeeping questions and of course follow it up with something that is related more to the business. So the two housekeeping questions are essentially what happened on securitization, did you incrementally do any assignment of securitization this quarter and what is the securitization income for the quarter? And more importantly the question I would want to ask is, when I am looking through the assets you have financed in the quarter, given that you have faced so much assets stress in this quarter and so much incremental slippages, your growth is actually quite robust, even if I look at the CV and CE segment which will include your M&HCV the amount of assets that you have financed in the quarter is almost Rs. 860 crores which is by no means a small number, so could you explain is this because you were saying earlier that you also realized the full extent of the problem pretty late and that is why the course correction could not happen in the quarter, what can we expect on growth going forward, would you become more conservative, given what is happening to the asset quality situation?

**Dinesh Prajapati** This quarter we have not done a securitization or assignment transaction. We are in dialogue with the banks for doing a securitization. In principally we have received an approval from the couple of banks, so for around Rs. 600 crore portfolio sell down in this quarter. That is as far as the securitization part is concerned. As far as the securitization income for the quarter is Rs. 54 crore and for your question on the CV asset value finance for the quarter is Rs. 620 crore.

**Shantanu Chakravarthy** And that will include LC and all that?

**Ramesh Iyer** Yes it includes everything.

**Ramesh Iyer** And please understand that when we say we are out of M&HCV that is heavy commercial vehicle we are out. We are not out of LCV segment.

**Shantanu Chakravarthy** And in general if I look at your AUM that has grown at almost 5.4% QQ. The YoY growth is about, it is high around mid-20s, and I do not recollect the exact numbers right now.

**Ramesh Iyer** 27%.

**Shantanu Chakravarthy** Yes, it does look little bit on the high side. I mean you are obviously growing much faster but given the situation.

**Ramesh Iyer** I do not know whether you are able to hear answers to other's questions, I am not sure but I did explain that our business growth comes from North which is continuing to be buoyant. Our NPAs are getting down in North, North we are not doing well and I said South we have a degrowth. In business we have a de growth in South because the focus is collection, North is a growth story for us from business point of view because the collections and NPAs are also under very good control.

**Shantanu Chakravarthy** And what can we expect going forward?

**Ramesh Iyer** I think if the economy does not change, commercial vehicle segment will not improve and you will not see us participate in that segment for growth at all. So far as South is concerned, as I told you Karnataka first improved, then Andhra, then Kerala, now Tamil Nadu. We will still wait and watch to see how this quarter behaves in terms of our overall collection and correction of NPA, etc. before we can really jump into a business conclusion in these States.

**Shantanu Chakravarthy** You also have done quite a bit of CP financing in the quarter, any particular reason for that?

**Diensh Prajapati** Our strategy for short term financing always remains during the financial year, roughly around 8-10% of our borrowing from the short term bucket and in that short term bucket CP is one of the instruments and so we believe that it will continue to remain in 8-10% bucket. Yes, whenever we get an opportunity to replace these short term liability with the long term, we usually happens in the half-year ending or annual ending wherein you get an attractive long term papers or through securitization deal that we try and replace that short term paper with this long term papers.

**Shantanu Chakravarthy** Will that be an increased focus on NCD, how do you see this going forward from a strategy point of view in the next quarter or so given what the current situation is?

**Diensh Prajapati** That liability switching whether it will be more focused on the bank or bond market will depend on a market scenario. So, if the currently what we saw last few days, maybe a week, the bond market has rallied and there was a scope for participation so we have participated in some form in the last few days. Now if things continue in the same form, we will try and see whether we can replace the bank market with this bond market by around 2-3%.

**Moderator** Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the floor over to Mr. Karan Singh Uberoi for closing comments.

**Karan Singh Uberoi** On behalf of JM Financial I would like to thank Mr. Ramesh Iyer and at the same time the management team of Mahindra & Mahindra Financial Services and all the participants for joining us on the call today. Thank you and good bye.

**Moderator** Thank you. On behalf of JM Financial that concludes this conference. Thank you for joining us and you may now disconnect your lines.