"Mahindra Finance Q3 FY 2017 Results Conference Call"

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ANALYST: **MR. KARAN SINGH - JM FINANCIAL**

MANAGEMENT: **MR. RAMESH IYER - VICE CHAIRMAN AND MANAGING DIRECTOR – MAHINDRA FINANCE**

MR. V. RAVI - EXECUTIVE DIRECTOR & CFO - MAHINDRA FINANCE

MR. DINESH PRAJAPATI – SENIOR VICE PRESIDENT – TREASURY & CORPORATE AFFAIRS - MAHINDRA FINANCE

MR. VISHAL AGARWAL - SENIOR MANAGER, TREASURY AND INVESTOR RELATIONS - MAHINDRA FINANCE

Moderator: Ladies and gentlemen, good day and welcome to the Mahindra Finance Q3 FY2017 Results Conference Call, hosted by JM Financial. 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 call please signal an operator by pressing "*" and then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Karan Singh from JM Financial. Thank you and over to you Sir!

Karan Singh: Thank you. Good evening everybody and welcome to Mahindra & Mahindra Financials Services earnings call to discuss the third quarter results. To discuss the results we have on the call, Mr. Ramesh Iyer, who is the Vice Chairman and Managing Director, Mr. Ravi, who is the Executive Director and CFO, and Mr. Dinesh Prajapati, who is the Senior Vice President, Treasury & Corporate Affairs and Mr. Vishal Agarwal, who is Senior Manager, Treasury and Investor Relations. May I request Mr. Iyer to take us through the financial highlights subsequent to which we can open the floor for Q&A session? Over to you Sir!

Ramesh Iyer: Good afternoon. You must have seen the numbers that has already posted and release must have been complete already. So I do not want to go line-by-line in terms of the results, but let me kind of tell you what do we see from here and why we are, where we are and how do we propose to handle it going forward is what I would try to kind of cover in my initial address.

So if you kind of look at our disbursements, we have had decent quarter with the disbursement growth and that is some positive indication of how the rural market is turning out to be. I would like for this purpose to split the quarter into, honestly three months independently, so, October being one, November and then December.

October was extremely good from our point of view in the sense that after September, October with a good festival season, the demand picked up and the vehicle sales picked up, tractor sales went up and we were direct beneficiary of that growth and we actually registered a 20%, 22% plus growth in October standalone in terms of volumes are concerned.

And then comes there was a spillover benefit in November first week from October demand and then comes the demonetization of November 8, 2016 and we had one address in between after this and unfortunately the whole of November was, where people just did not know what was happening, how to handle this, what is the next thing coming in and therefore there was complete slowdown as far as rural market is concerned and the volumes also went down during the same period and the volumes went down for various reasons and one of them was the sentiments got weak straightaway, because people did not know how long will this situation really impact, therefore why is this is the right time to buy a new vehicle was the fundamental question.

It was also followed up by exchange programs were not happening well because one always feared the second hand vehicle normally is bought by people or brokers with a lot of cash etc., and therefore they were not readily available in the system and therefore exchange was another area where there was a pressure and third area of pressure was, customers who brought in margin money the 20%, 25% upfront normally people do bring it in cash, either out of sale of their old vehicle or from borrowing from friends, relatives or own money and that size of the money also was being much smaller, having the overall sales volumes got impacted and we also went through that impact of that volume and therefore November in itself did not show a mega growth.

Then came December where there was a pending enquiry available in the hands of the dealer and then the OEM supported the December sales by good discounts and various programs that they initiated because inventory levels had to be brought down by most of these OEMs. Considering all of that December once again registered a growth for us and therefore we ended up the quarter at a decent growth of 15%, 17% plus.

We believe that with a great monsoon, the November yields were extremely good and we were very, very happy when we actually in September sales were and we believe that this quarter will show some phenomenal change even in terms of our recoveries are concerned, and I must remind you that the rural cash flows are farm driven while it is also well supported by various infra cash flows, contracting segment cash flows etc., but fundamentally rural still remains upward of 80%, 85% cash driven economy and then transaction of this nature does put that tremendous extra pressure in the system of how do they handle their transaction going forward.

So we had a bit of problem in terms of our recoveries are concerned. October was exactly like last October because normally during this festival period and pre-harvest etc., there is normally an investment and people do get ready for the January cropping and therefore they do buy seeds, fertilizers etc., in October and that money normally gets invested for these items and October for us historically has been a month where the collection efficiencies remain between 85% and 90% and we saw that the same and we did not overreact to it and we felt things are going well and if November had not happened the way it went through we believe that the crop money would have come in and we would have seen a very, very different picture to what we are seeing.

So our belief was that crop being good in November and readiness for January crop was getting on way we thought rural is bouncing back to normalcy and the volumes reflected that kind of sentiment, but with this impact of demonetization that came in, November we had steep fall in our collection of upward of 20% and that really put tremendous pressure in terms of where the quarter is going to end for us, but the fact still remains that the customer were available to be met discussed, vehicles are available, we really understood the problem of the customer and as we mentioned in our first address, we took a very conscious view of how to deal with good customer and how to deal with not so good customer.

We also took a very conscious view some one who is not otherwise paying as even in the past, this is the right time to go and pickup their vehicle, because we did not believe their intention were fair and good that they would have come out of this even in demonetization had not happened, because demonetization brought this very clear spirit between good and not so good customer. So in this quarter we actually added about 70,000 contracts moved into NPA which otherwise would not have been just larger number but for demonetization, but against the 70,000 we are also seeing upward of 40,000 - 45,000 of the contracts have registered movement during this quarter while they have not been able to pay full enough to come out of the NPA, but that is the confidence which takes us to the next quarter as if these contracts continued to behave in the direction of positivity, it helps us to solve this as we go to the next quarter.

I think our own belief is the fastest to come out of this problem would be the farmer and therefore the tractor segment or the vehicle segment, which is normally used by the farming community or farm driven cash flow community. Why we are saying this, it is the November crop is out while the adatiya have not bought this crop, I think they have been sold to the Mandi's and Mandi's is not paying full payment immediately, they have paid some part payments, they are making cheque payments etc., and therefore as we sail through this last quarter of this year, we will see most of this money will come through, similarly we will see their January crop is also expected to be good with a good water level, the sowing was good and it is expected that the January yields will also be good.

Our own belief is therefore January-March quarter we will see cash flows from two crops. One which already over in November, the money for which will come in this quarter and the January crop which should be out or somewhere it is out and somewhere it will be out in the next one week or so, this money should also come in between February and March. So, we would see substantial correction to some overdues and NPLs that we have built in this quarter and we would definitely see them come out.

While we have definitely taken the little benefit of the RBI circular on demonetization, but we have restricted ourselves only about 30,000 odd contracts where we would directly establish that these were the once who were hugely and directly impacted by demonetization. While the entire cash flow of rural is very cash dependent and one could take a view that all contracts should have been gone through this demonetization impact, but we do believe somewhere that like a car or other segment, are not necessarily only cash flow dependent and therefore we provided on those contracts and therefore even though we know the reasons for why that they have not paid we have not resorted to the demonetization benefit.

So, while the impact of provision on account of demonetization could be upward of Rs.200 - Rs.250 Crores, but what we would have taken as a benefit is only about Rs.152 Crores. So, to that extent we have limited ourselves to deciding on which contract will do this or will not do this. Same thing we have done this with high delinquent account like customers who are 10 plus into 50% provision bucket etc., we have resorted to repossession as one answer.

If you recall our past addresses we have always said that we are going close to customer, we are opening more branches, we are remaining closer to the customer and we are deciding as to how to handle this collection, give more time to customers who are circumstantially hit and act on customer who are otherwise people are intentionally hit and we have deferred our repossessions in the past, but in this round post November we have repossessed at least 8000, 10000 vehicles more than normally we would have repossessed like on an average if we repossess 3000 to 4000 vehicle, I think we are currently having stock close to about 14000- 15000 vehicle and we do know for the fact that these are highly provided items and therefore when we transact on them, we would not bring in a big loss, but at least we will solve a lot of delinquent account and therefore you will see our coverage ratio has moved up from 51% odd to 56% odd and that is an outcome of the higher delinquent account either settled or highly provided remaining there.

So net-net we have not changed any our fundamental approach to this business. We do believe where customers are not able to pay, but where they are circumstantial I think we have taken a very clear view as to how do we give them more time, but if they are intentional we have kind gone ahead and done what is good to be done. We believe that going forward the fourth quarter has lot of promises in store for us, we do see that the rural cash flow improving, we do see the flow of money is better and all of that considered together, the demand for the vehicle was good as we talked about in October and December and we do expect that the sentiments are returning to normal. We do see the transactions are getting little better.

I do not want to sound like everything has gone normal now, but definitely the situation is far far better than where it was. Taking all of this into consideration I think we have resourced ourselves well. We have enough people in the system. We have enough locations where we are present and I think we would definitely be benefitted out of the actions that we have taken. Most of the time we have seen also in the past, fourth quarter is one of our best quarters and we continue to stay with that sentiment that even in this around, fourth quarter will definitely show us the direction of what it has shown us in the past with an added benefit if at all of the flow of the money happening during this fourth quarter, which will help us to recover better from where we are.

As I said we have this higher coverage which is continuing to be there and we also see that while there are NPA account numbers are higher, but the accounts which have registered movement are also equally high and cash flow of rural market dependent on farm cash flow has had its impact on because of the delayed cash flow coming from this market, but there are some very clear signals of also certain contracting segment recommencing activity and all that and if parallely along with form cash flow if the contract segment does begin again, I think we would see bounce back of rural in a much better position from where they are today.

So net-net I would think that while this quarter we have seen some unique and different levels of pressure, but I think this pressure is not making our belief and our fundamental any weaker. We think that the problems have rural is a little behind and things are seeming to be improving unless something at the marketplace changes substantially in the fourth quarter which we do not forecast that there is anything more to happen out there.

Put all of this together, we believe that we will pursue our growth story vehemently, we will pursue our penetration and we will pursue our focus on collections and concentration and make sure that we get the maximum benefit of the changes that we think are likely to happen in the fourth quarter.

I think this is our thought process. As far as the subsidiaries are concerned I think that it is not much to really talk of them in terms of geography that they work is a similar geography, so not that they have had any new problem except that the insurance business does not have to worry about the collections etc., and therefore their impact is only to the extent that the volumes have been lower they have been impacted, as otherwise they have registered a growth of 14% plus and as far as the rural housing is concerned they had similar impact that we had in terms of collection because it represented the same geography, but their own at approach also is the same, stay close to the customer as the flow starts improving, I think they would also get the benefit of their collections and that will help them do better.

So that is the visibility that we have about all of our businesses. I think just to add one final sentence. I think the states where we went through major problem during this period, which are very agreed dependent are Maharashtra, MP, UP, Bihar are the kind of states that we saw in Karnataka and Andhra Pradesh, as against states like in the past we used to have problems coming from Tamil Nadu, Kerala, Punjab, West Bengal etc., they do not have seem to have gone through same pressure as much as the states that I mentioned went through, but the good news is the crop in this states have all been good and therefore no sooner they have sold and cash flow comes in we should be one of the beneficiary of that flow. I think that is all from my side and let me check with Ravi, Dinesh anyone wants to add anything otherwise we can open it up for Q&A.

V Ravi: I just to supplement what Ramesh Iyer said there is notional item of Rs.26 Crores which is provided for derivative mark-to-market which is a transitory entry, there is no gain or loss, it is just notional entry as per the new accounting guidance and these underlying contracts are fully provided for this Rs.26 Crores mark-to-market is a very notional entry and this is not going to be actually incurred, so you can say this Rs.26 Crores is nothing but the deferred profit to Q4.

Dinesh Prajapati: I think we can move onto Q&A based on this.

Karan Singh: Let us open it for Q&A.

Moderator: Thank you very much. We will now begin with the question and answer session. We will take the first question from the line of Chandra Govindaraju from IDFC Securities. Please go ahead.

Mahrukh Adajania: This is Mahrukh. I just had few data points and then had a few more questions. Firstly, what was the interest reversal during the quarter in terms of what is actually reversed and on the dispensation portion?

Ramesh Iyer: As you ask your next question in the meanwhile they will pull the data out.

Mahrukh Adajania: The other is that if I am just trying to judge the core profitability during the quarter, so you have a net loss of Rs.15.6 Crores, you can add back the derivative MTM of Rs.26 Crores, but you would also have to deduct the provision that you saved on dispensation right, so it would still be a very weak quarter, your comments on how profitability will improve?

Dinesh Prajapati: One was the during the period income reversal piece is Rs.65 Crores and the Rs.152 Crores which is the dispensation used if you breakup that Rs.152 Crores, Rs.92 Crores is the principal and Rs.60 Crores income reversal piece of that.

Mahrukh Adajania: That was my first question in term of core profitability and then how do we model aging provisions right because last quarter, the credit cost of Rs.3 billion would have some aging provisions and some provisions on slippage, now with the dispensation in the third quarter that slippage portion would be much less, so substantial portion of the provisions would be aging provision and the provision itself have gone up from 3 to 4.2 billion, so how do you model it going ahead in terms of aging, because what is reflected in Q3 if I am guessing it correctly as more of aging provisions and very little off fresh slippage provisions.

V. Ravi: There is no fresh provision except for that Rs.65 Crores of personal assets which are used, so if you remove the Rs.65 Crores in the increase between Q2 to Q3 as you correctly say almost 95% pertain to the bucket change, provision due to bucket change.

Ramesh Iyer: That bucket or moving forward that 6, 7, 8 whatever we would have.

V Ravi: Whichever way and that is how the coverage is also has gone up from

Ramesh Iyer: The only bit is look at the coverage has gone up from 51% to 57%.

Mahrukh Adajania: But the next quarter because fourth quarter always has better recoveries than other quarters, I am in the first quarter of 18, how would I model the aging provisions, because it has just gone up by a billion QOQ so that way?

Ramesh Iyer: You must also consider that next year 90 days kicks in, so I think it is going to be extremely difficult modeling proposition until 90 day also happens, so I think that is why it is much easier to look at will you be a 8% gross NPA company, will you be a 9% gross NPA company and if you were to have 51%, 52% coverage will you be a net 5.2% net NPA company.

Mahrukh Adajania: Got it and what would it be?

Ramesh Iyer: That is you have to model I only gave you a formula.

Mahrukh Adajania: What would your internal target is what my question was?

Ramesh Iyer: That is secret only in the ears of few people. I cannot disclose like this, we do not want to put out anything, I think it is important for you to understand that this quarter is a non-comparable quarter from any parameter at the market place and which is why I split it up into October, November and December to tell you how it went through. I think for us it will be extremely important to handle it in two phases. One, we want to handle the fourth quarter very independent of what normally our fourth quarter is, so we want to handle little fourth quarter as something that we have missed in third quarter plus something normally we can do in fourth quarter, so that is the way we would like to handle the fourth quarter and then it may be useful to have this discussion which we will do after our fourth quarter to say how do we develop a model from there with 90 day kicking in and if market conditions to stabilize. To develop a model on a very uneven market condition with a new regulatory framework coming in, it is going to be a task right, how we give you any magic for that.

Mahrukh Adajania: But the 90-day was kicking in March end or on from April 1, 2017?

Ramesh Iyer: It would kick in next March, but we always have been someone who believed in starting to do as early as we can instead of waiting for the last year, if you look at 120 days we actually moved in last year.

Mahrukh Adajania: Got it. Okay, makes sense thanks.

Moderator: Thank you. We will take the next question from the line of Kunal Shah from Edelweiss Securities. Please go ahead.

Kunal Shah: Firstly, just missed out if you highlighted in terms of how was the collection efficiency in the month of December. So you mentioned October and November, but how has been the recovery?

Ramesh Iyer: Collection efficiency December was I think 93%, 94% or so and November was something like 70% - 74%, so I think December was 94% odd it could not cover for what we lost in November.

Kunal Shah: Okay. And so when we look at this number of contracts, which moved into NPA, so today we would be standing somewhere around 2.50 lakh odd contracts?

Ramesh Iyer: ~ 219000 as of December 31, 2016.

Kunal Shah: 219000?

Ramesh Iyer: 2.19 lakh.

Kunal Shah: Okay and this 32000 borrower accounts so those are still extended when you are referring may be 40,000, 45,000 have registered movements, so most of it you will see outside of the 32000?

V. Ravi: 70000 is a total of which 44000, there is a movement, the remaining 26000 there are no movement, so off the 26000, 4400 and all had moved in January 2017, off the 44000 again, there is a movement up to 16000 contract in January 2017.

Kunal Shah: 32,000 what I was referring was in terms of where we have used this dispensation?

Ramesh Iyer: This 32,000 will be a part of 70,000. It is not independent of that.

V. Ravi: What Ramesh said is that if zero dispensation benefit we have taken 70,000 contracts would have gone to NPA instead of it we have less by 32,000 numbers say 38,000.

Kunal Shah: Out of this how many were less than 60-days DPD?

V. Ravi: In our case 120 days DPD only becomes NPL. You are right, sorry, just to supplement our personal loans, which I do not know it, are negligible part of our portfolio, two wheeler and personal loans.

Dinesh Prajapati: Kunal, what Ravi mentioned about personal, because RBI dispensation rule is that business loans will only be allowed for dispensation, so if the application of the asset which is passenger car or any other category of asset which does not serve the commercial purpose will be classified under different category.

Ramesh Iyer: We have not considered for dispensation in those contracts.

Dinesh Prajapati: That is how it is.

Kunal Shah: No, sir. When we finally look at in terms of the dispensation of 32000 borrower accounts, just wanted to get the sense wherein even without demonetization or with the demonetization, it would have slipped. So something which was already say 60 days or so as of October 31 and then maybe it would have fallen into NPL irrespective of demonetization and there we have used this dispensation?

Ramesh Iyer: No, if you normally look at say 100 contracts open as a projected NPA in a month, 90% of them anyway get solved by normal method whereas in this round what got solved was only 10% that is where the dispensation has been used and then within that also we removed all the vehicles which are not for business purposes, so that gets an impact anyway of that 10% normalcy, which would have remained there.

Kunal Shah: How much was written off during this quarter?

Ramesh Iyer: Write off meaning what do you mean?

Dinesh Prajapati: Termination loss.

Ramesh Iyer: Total termination law, disposal law, and bad debts all that kind of thing, which is a part of that Rs.400 Crores odd for the quarter, is about Rs.90 - 95 Crores.

Kunal Shah: Just lastly in terms of the securitization income so that is in fact a loss out there of Rs.20 Crores odd during the quarter, so what is the reason, is that may be because of may be NPL issues on the securitized accounts?

V. Ravi: No, securitization we have to account on cash basis, so since we have not received the money from the customer, it is not an NPA. Normally securitized contracts are cherry pick contract, so it is not an NPA, if money is not received from the customer, I cannot book the income, and so in a way just Rs.20 Crores was deferred to the Q4, suppose we receive 80% of these contracts, installments in Q4, I will be in a position to account for so many Crores.

Ramesh Iyer: Even if one installment does income we have to reverse the income of that, we cannot do the income of that all for that installment.

Kunal Shah: Okay, but would it suggest that may be the collection efficiency in the securitized assets was relatively lower as compared?

Ramesh Iyer: Yes, it will. Let us be very clear where work has not changed whether it is securitized normal, abnormal, all contracts are in the same geography, so there behavior on account of the cash flow impact is going to be the same.

Dinesh Prajapati: See Kunal, major part of the securitization portfolio are agri related asset class and obviously agri were the highest impacted segment from the cash flow point of the liquidity challenge, so which is why these will be immediately felt even in the best class of customers.

Kunal Shah: Okay and may be to that extent there would have been expense, but no income and that is the reason it is showing, but here may be we expect this also may be do see some kind of recover in Q4 and normalize?

Ramesh Iyer: Pray with us jointly that nothing new should happen next quarter because the yields are out and the crop has gone to the Mandi, now the payments will come from Mandi unlike in the past it used to come from adatiya.

Kunal Shah: One last question is on disbursement? Only thing is in terms of disbursement, so you are pretty confident in terms of the growth may be collection efficiencies on one side, but otherwise when you look at December and say one half through January, how are we placed in terms of overall growth momentum or say the demand in the system?

Ramesh Iyer: It is as follows. I think the overall volumes have seen a dip at the retail level, but the good news is for us that the competition is also as low mainly from the banking system, so there is some volume available which otherwise the banks would have been doing because their own administrative activities keeping them busy, so that gives us some benefit of growth clearly. I think the second is we have been saying it for sometime, but almost every model is now reached to rural market and we do see some traction around these volumes as well, so our growth has come from non-Maruti segment to some extent. Our growth has come from Maruti doing well and therefore we get the benefit of Maruti retail to some extent. Our growth has come from tractor, which did well during this period, and our growth has come from non-Mahindra tractor, which we got into.

Kunal Shah: Okay, sure, I will come back in the queue.

Moderator: Thank you. We will take the next question from the line of Amit Premchandani from UTI Mutual Fund. Please go ahead.

Amit Premchandani: Good afternoon Sir. Sir, if you just recollect over the last three years if you just go over the calls whenever results are bad, we had the same story that results get impacted by one or other external factor, which is generally outside the control of the Company while during the same period many of the NBFCs have changed their business model, marched ahead, and they do not seem to go through the same cyclicity like Mahindra goes through. We appreciate that it's a very cyclical model. But generally has the Board ever considered this while evaluating how they frame strategies, how they give targets, what are the action to be taken to lower this dependence on external factors?

Ramesh Iyer: For anyone to review and give us revise strategy first, the fundamental change that we will have to agree and accept is to shift the geography where we work, which means we have to move from rural to urban, then only we can shift the strategic thought, otherwise in rural if you are going to be there, the limited shifts that is available as our strategy is to do more tractor, less car or more UVs and more tractor or used vehicle and less tractor, so there is no other scope there from a product perspective.

The second perspective that we look at it, are we missing out on any customer segment that we are not already working with, so there are only let us say largely three segments of customer very high end farmers or very high rich community, the midsize community or mid earning community and very lower end community. We have chosen to be in the mid community which is a large segment, because low end is very microfinance type community and very high end is a very banking community where we have no value proposition, when there is limited geographic choice and shift when there is a limited product choice and shift and there is a very limited segment shift from a customer perspective we think we will have to go through this problem, because we should not forget that 21 years we have run this model and we would have to had to explain the cyclic impact may be in the last two years or whatever.

Now this is not to mean that we do not have to revisit our strategy at any point of time or whatever, but it does mean that how do you get the benefit of having worked for 21 years ago is what we are trying to explore, so we are now trying to also expand and grow our preowned vehicle segment which could be a last segment possibly. We have moved into non-Mahindra tractor, which was a small portfolio, we believe that we can grow little bigger. We have moved into non-Maruti car which was so far not as actively present but we think they are penetrating and we can get a benefit of that very clearly, so to that extent the board reviews, looks at it and guides us to say how well and how best can we do.

The only other segment that we have looked at where we are participating is products like Ola, Uber, Zoom etc., where these driver driven segment these are and they are drivers from the remote rural areas who come to Mumbai to drive vehicle and therefore there are all types of customer segment where we get the rates that we are looking for and we have an advantage of doing the KYC in the villages from where they come and that is the strategic differentiator that we have built between us and someone else for us to get some volume benefit.

If you recall we also have gone into a little of SME financing but again that is very linked to the Mahindra supplier or Maruti supplier or Tata supplier kind of a thing on whose cash flow we have control over through the OEM and to that extent possibly we will try and derisk ourselves doing the SME segment, but just because we go through some cyclic pressure either caused by monsoon because we should not forget that the monsoon pressures that we face normally are never an all India pressure that every market faces. So even in the previous round sometimes it unfortunate the two or three major markets go through this pressure and therefore the problem size is larger than possible, but in this round that we are suffering from is not a cyclic pressure it is a very clear transactional impact arising out of a major decision and it is across the country, across the segment problem for us.

So I do not think this should be clubbed with a cyclic problem. The cyclic problem that we are faced in rural is on account of monsoon, drought or those kind of thing not as otherwise, but the last two years sufferings in rural market has got little more enhanced again not because of cyclic problem because of governmental action or economic slowdown arising out of infrastructure. So if you split the problem between cyclic which is very weather impacted and which is economically impacted due to infrastructure and other story going slow and the third due to demonetization, which is a very strong government action based. I think only one of the three qualifies as a cyclic front and normally the cyclic front is never beyond two months, three months in a year and never for all India and therefore we have never had problem of the size that we are currently actually handling to it.

Amit Premchandani: Okay, thank you, that is it from my side.

Moderator: Thank you. We will take the next question from the line of Hiren Dasani from Goldman Sachs Asset Management. Please go ahead.

Hiren Dasani: Thank you. Can you just briefly breakup again Rs.150 Crores which was the benefit due to dispensation in terms of interest reversal and the provisioning?

Ramesh Iyer: I think about 92 are principal and 60 is income reversal.

Hiren Dasani: Just to be clear, had you not used the dispensation your interest income would have been lower by Rs.60 Crores.

Ramesh Iyer: Lower by Rs.60 Crores if you use the dispensation to be reduced there.

Hiren Dasani: And provisioning would have been higher by Rs.92 Crores?

Ramesh Iyer: Absolutely.

Hiren Dasani: Okay and this Rs.92 Crores mean what Rs.900 Crores worth NPA?

Dinesh Prajapati: Rs.669 Crores.

Hiren Dasani: Rs.669 Crores NPA.

Dinesh Prajapati: Yes.

Hiren Dasani: Okay, because you typically go its 15% in the first?

Dinesh Prajapati: I agree but since again the same principal the tractor portfolio will be slightly higher proportion, so there could be possibility that there could be five month ageing, which could have been hit in the one stroke.

Hiren Dasani: Okay, so if I were to think of it had you not use the dispensation, your gross NPA would have been higher by Rs.669 Crores right?

Dinesh Prajapati: Correct.

Hiren Dasani: Okay, now if you think that the crop is good and the yields are good and all that, do you expect that by the end of March, we reach back to let say at least 8% of gross NPA level which was the last year of level or you think it will be very tall order?

Ramesh Iyer: I think genuine attempt will be that and our belief is that if the crop money, which is surely likely to come into the system of the November crop money, which will come into the system before end January, and the January crop money should come into the system by March. I think if this unfolds as a real action I think our belief will turnout to be that.

Hiren Dasani: Okay, great, thank you, that is it.

Moderator: Thank you. We will take the next question from the line of Sunil Tirumalai from Credit Suisse. Please go ahead.

Sunil Tirumalai: Again it's kind of a strategy question from where Amit dropped off. So basically we have seen a few years of tough asset quality situation and by the time we reach 90 days, we are probably talking in excess of 10%, 11% GNPA on the current business even for a good March quarter. In such a situation, what is the management and the Board's thought process in terms of disbursement growth being so high? Is not it an opportunity to actually step back and figure out if 10%, 12% of your loan assets are not performing and probably about 16%, 18% are probably 30-day plus in terms of delinquencies? That is a fairly large problem to have and in that context growing even if it is gaining share, banks are not there, others are not in the market so let me go and take the share; is that the right strategy to adopt when the stress is so high or would you rather take a slower approach and not grow the book so much and consolidate? That's my question. Thank you.

Ramesh Iyer: Let me clarity this to you. First is, I do not think we are sacrificing recovery for growth because we have different verticals which managers recovery which are 12 months after the business is done, so first 12 months from the time the business is done, it is handled by the business team with the recovery support and once the contract crosses 12 months of repayment after the business is done, it is taken over by a separate recovery team, so I think it is extremely important to understand that business and recovery is handled very independent. That is one. Second is, I do not think we are sacrificing on any appraisal norms to chase business and grow business? So if you look at it we have not grown market share. We are getting benefit of the available volume out there and may be temporarily 0.5%, 1% market share would have grown in certain products, so if you recall what I said we have grown in beyond Maruti which otherwise was a very low product for us. So now that Hyundai, Nissan, Toyota and Ford everyone is selling and Kwid Renault is selling in the market, we are getting a benefit of that.

I said we have grown in tractor because the tractor sales by itself has been higher. We have not grown market share big time there. Then I said we have grown in non-Mahindra tractor which we were not doing big time then I said we are growing in refinance that is preowned vehicle which was a low volume business for us, so please understand that the growth of disbursement is not coming at the cost of either sacrificing appraisal nor is at coming at the cost of gaining substantial market share nor is at coming at the cost of sacrificing recovery.

Now let us look at the gross NPA let us say when you said 90 day NPA becomes 10% plus, but if that is going to impact our credit loss eventually to go to 4% and 5%, I think board event does not have to interfere I think we are the management will take a decision not to do those businesses. The gross NPA by regulatory change if it moves up, it is just shifting up a goal post, because RBI might say 30-day delinquencies to be called as NPA, we may have 20% NPA, but the business model does not change, because the regulator has changed the norm. So we look at credit loss as one of the most important measurement for us and when the LTVs are pegged at 75%, 77% and if market condition is at least average plus, we do not see our credit losses to go beyond the 2.5%. So that is how we measured ourselves for sure.

Yes, in a product when we repossess and we make big loss, announced like two years back or three year back, we ourselves withdrew from heavy commercial vehicle financing when we saw the market dipping, so I think that is the conscious decision that we will take either by geography or by product or by certain segment of customer depending upon how things pan out there.

So far as the delinquency or the increased NPA is concerned, we also measure internally as to how much is due to intentional default and how much is due to circumstantial default. If we are in a business for a long term basis, I do not think we have the luxury of deciding when we will do business and when we will not do business, so in the business like this we will have to take a very conscious decision if you wind up, we need to wind up once for all from that market or from that product. I cannot say next two months, I am not going to do business from third month I will start doing business again.

So, we look at very clearly the impact of our recovery, our cost to what extent by circumstances and to what extent by intention. If it is cost by circumstances, it is an internal conscious view not to reschedule a contract as otherwise even in this round when we move to 120-day or it is the next round when we move to 90-days, RBI is allowing us one reschedulement to these contracts that we can do, but we have decided not to reschedule the contract and rather live with this high level of NPA, because we know that instead of 36 months somebody will pay you in 42 months and we know for a fact that out of 36 months contract if we can recover 18 months from customer or 12 months from customer, I think the asset has got the ability to protect the principal.

So credit loss becomes important for us, but having said that we will be conscious in terms of looking at where to grow, which product to grow, which geography to grow and which segment to grow and if there are certain segments, products or geography which does not support our vision going forward, we will withdraw from that market.

Sunil Tirumalai: Thank you Sir. Going forward as we stand given the whole set of information that you have from your market and your feet on street, so which are these areas which you feel would be key growth drivers for you among the segments that you are operating in?

Ramesh Iyer: The key growth driver as I told you is going to come from the tractor added with non-Mahindra tractor as one clear segment, because that is one segment which is showing prosperity of growth both from farm side and expected infra side. We very clearly see for ourselves growth coming from Maruti, because Maruti is continuing to drive rural with great focus and their volumes are registering higher volume growth and maintaining a market share will get a higher volume.

We do see growth coming to us from beyond Maruti whether it is Renault, Nissan, Ford, Toyota, Hyundai where we have very small 2%, 3%, 4% market share type situation, because we are not present in urban and semi-urban and they are pushing volumes into rural market will get some additional number. Preowned vehicle which is as a percentage to balance sheet was 7% to 8%, we do want to take it to a 12% to start with 14% to 15% over a period of time and we see that the scope of growth that is possible. But in the Mahindra UV segment, Maruti vehicle segment, we do not see market share growth for us happening, but to the extent of volume gets increased in that margin maintaining market share will get some volume which is why we are not willing to speak a growth beyond 15% because none of this promises a very high growth zone already. So if you have to get back to at 20%, 25%, and 30% kind of a growth story, their own volumes will have to register higher growth, discounts will have to discontinue and price increase will have to kick in if you have to see higher disbursement growth.

Sunil Tirumalai: Got it, thank you very much Sir, all the best.

Moderator: Thank you. We will take the next question from the line of Roshan Chutkey from ICICI Prudential Asset Management Company. Please go ahead.

Roshan Chutkey: Thanks for taking my question Sir. Just a quick question on what do you expect the elections backed on collection efficiency going forward in Q4, because I remember in 2014, you had election problem and you were attributed that the collection efficiency problem to elections at this point in time, do you see a similar…?

Ramesh Iyer: Two major states which go for election let look at UP and Punjab and UP is something fortunately it is from February to March and it is not concentrated all days in all the market, so I think it is different, different location on different, different dates, so I think UP will show some dip of about may be 5%, 7% kind of collection efficiency dip happening in UP, but pre and post election, the money in the market will always be very, very high, so for the election period one may see a dip, but if we can do good collection between now to election and if the election ends before March then in this quarter we would have recover for what you would have lost in between the quarter. And UP is the real indicator from the size perspective, Punjab is not a very large size from our point of view and I think it is a one-day election Punjab. It is not phased election. I think Punjab is a one day election item I think, anyway but in any case it is not a very major size for us at this stage, but UP something which is very large for us and the good news is that it spreads over a period and therefore whenever there is a election in a particular pocket we will have an impact for that period, but pre and post will show better collection, but everything gets over, starts before February and ends before March. We hope that in the same quarter correction will happen while that one can see a shift between month-to-month.

Roshan Chutkey: What is current thinking of the management on the repossession?

Ramesh Iyer: The thinking is very clear, anyone who is in high delinquency levels where they are moving from 10% provision bucket or 50% provision bucket we rather take back the vehicle sell and cut loss, reduce the burden of provision. So far as regular paying customer but delay the payments, because of their own cash flow impact I think will rather partner not repossess, so normally what used to be a repossession of 3000, 4000 in a month has gone up to may be 6000, 7000 in a month or 8000 in a month.

Roshan Chutkey: Thank you so much Sir. All the best.

Moderator: Thank you. We will take the next question from the line of Manish Ostwal from Nirmal Bang Securities. Please go ahead.

Manish Ostwal: Thank you for the opportunity. My question on the given the current collection efficiency trend in the disbursement, how do you see this yearly guidance of 8% gross NPA to be achieved in Q4?

Ramesh Iyer: Where did you get this 8% guidance? By the way somebody asked will you reach 8%? I said that is our expectation, belief and drive. So please do not put my name again it to say that we said 8%, but very clearly where does it come from if you ask me as I said the crop money expected November crop money has not yet come in so we expect that to come in this quarter as well as January crop money will come in this quarter, so is there going to be improved cash flow from farm, my answer is yes. All the transactions that went slow and got a little stopped between November and December will it come back to little normalcy with money flow in the market, my answer is yes. With so much of push that is happening on the road and other infrastructure if they all come in and activity do commence contracting segment money can start coming in, so put the three together I think is what gives us confidence to believe that they improved cash flow will improve our collection.

Manish Ostwal: Okay. And secondly, sir, at branch level when this November 8 announcement and then we thought there will be a meaningful impact on disbursement. The way the branches have played out, how do you see your initial reaction to the problem and the actual thing so what kind of the variance in terms of actual things could you throw some light on that?

Ramesh Iyer: I started off from there. I said it is important to look at this quarter as October, November and December. October actually did very well for us, because there was no demonetization, phenomenal festival positivity, good monsoon ended, so everyone expected that the yields will be good in November and December, so actually now at October saw a big growth of 20% for us in terms of disbursement is concerned. November was a disaster both for business and collection perspective. We had a 20% dip in collection. What we saw as an improved collection in December was just good enough to collect one installment of December; they could not cover up for November.

Manish Ostwal: And lastly, this disbursement growth of 16% so given the other segments we are targeting like non-Mahindra vehicles and non-Maruti vehicles also so overall disbursements pace, what level we can maintain?

Ramesh Iyer: So if October was a very good month and that is why we have ended by 17%, so between January to March if March is like October for some reason than one can expect some kind of 12%, 13%, 14% growth possibility, but if OEM flats out and they remain kind of subdued and constant I think we would have also be back to 8% to 10% kind of situation. We are enablers. I think for us what you need to understand is we are not losing market share while we are not very interested in substantially gaining market share.

Manish Ostwal: Okay. But we are targeting new segments where we may get better or increasing market share like this thing so in a way it is increasing the overall disbursement.

Ramesh Iyer: It is true, but you should also not forget that other volumes are remaining subdued or degrowing also, there we are losing right?

Manish Ostwal: And last question on the cost of funds movement because the interest rates are going down and when we see the impact on our financials to reflect that trend?

Ramesh Iyer: I think once the overdue levels come down, NPL levels come down, which means we do not need to borrow any money to protect the overdues that is use our own money for business and borrow only to the extent that the growth demands borrowing, then you will see the benefit of it. See currently, when the overdue levels also remain a little high right, so for lending we are borrowing so that means everything comes with some cost.

Manish Ostwal: Thank you.

Moderator: Thank you. Next question is from the line of Alpesh Mehta from Motilal Oswal. Please go ahead.

Alpesh Mehta: First of all, regarding the movement of the contracts into the NPLs, I believe last quarter we had around 175000 contracts, which has increased to around 220000 and you mentioned around 70000 got added, right. Is this calculation right?

Ramesh Iyer: Sorry, I missed your question can you repeat sorry?

Alpesh Mehta: The movement of contracts at the end of second quarter into NPL category, at the end of second quarter there were around 1.75 lakh contracts?

Ramesh Iyer: It has become 219 as of December.

Alpesh Mehta: Which is 2.19 lakh and during the quarter we added 70000.

Ramesh Iyer: That is right.

Alpesh Mehta: Okay. So what is moved out of the NPL category are around 26,000 contracts during the quarter?

Ramesh Iyer: Correct.

Alpesh Mehta: Okay. And these 70,000 contracts include the RBI dispensation?

Ramesh Iyer: Yes, it includes everything and about 44000 to 45000 contracts are registering moment demand in the same quarter while they have moved out.

Alpesh Mehta: Okay. So, the 70,000 contracts would include that 40000 to 45000?

Ramesh Iyer: That is right.

Alpesh Mehta: Okay. And when I look at this 70,000 contracts average ticket size, should I be taking around Rs.3 lakhs per round?

Ramesh Iyer: One should take about 3 to 3.5 lakhs.

Alpesh Mehta: So around Rs.2000 Crores of gross addition during the quarter to the NPL category, including the demonetization dispensation?

Dinesh Prajapati: That is 3.5 that is a ticket size at the original stage of beginning. It will not be necessarily that at the time of getting into NPL there is zero repayment.

Ramesh Iyer: Somebody would have given pay 12 months, 14 months before which they came into NPL also, so from that point of view if you want to take you can take about 2 lakhs odd figure.

Alpesh Mehta: Around Rs.1500 Crores of gross addition during the quarter to be NPA?

Ramesh Iyer: Should be there.

Alpesh Mehta: Of that, around Rs.650 Crores is related to demonetization.

Ramesh Iyer: That is right.

Alpesh Mehta: And secondly, how many contracts repossessed vehicle that we would have sold during the quarter?

Ramesh Iyer: How many we would have sold during this quarter is about 6700 vehicles or something we sold.

Alpesh Mehta: And normally we are now repossessing around 7000 to 8000 vehicles a month?

Ramesh Iyer: Yes, we used to earlier repossess about 3000 vehicles that have gone up to 4000 to 5000 type numbers now.

Alpesh Mehta: Because I believe last quarter you mentioned the number of around 10000 vehicles?

Dinesh Prajapati: Yes, that is stock.

Ramesh Iyer: That is stock, now it has moved to 15000.

Alpesh Mehta: The stock has moved to 15000 vehicles?

Ramesh Iyer: Yes, so we have opening stock of 10000 assume that we repossess something like 15000-odd vehicles during this period and sold about 7000 to 8000 vehicle, which ended up as 15000 odd thousand vehicles as of December 31[corrected].

Alpesh Mehta: Just one technical clarification if during due to this demonetization 650 Crores worth of accounts which were not paid as of paid December 31, would they have been categorized as NPL as of January 1, as per RBI regulation?

Dinesh Prajapati: As per RBI regulation 90 days he has given dispensation, but technically it does not make sense because we would have anyway, it does not matter because our disclosure will happen only on March 31.

V. Ravi: If it is not collected it will be NPA by March 31, 2017?

Alpesh Mehta: My question over here is assuming that I had the account, which was standard as of July 31, we have 120 days so till we recognize NPA after 120 days right, till November 30th that account would have remained as standard account and on December 1, it would have been categorized as the NPL account?

Ramesh Iyer: Correct.

Alpesh Mehta: Now there is a RBI dispensation for two months and during those months if the account which was standard and turning into to NPL category you can keep that account as a standard and on January 1, you have to recognize to the original movement levels, is that?

V. Ravi: Yes some of the contracts may become as of January 1, that the contract which would have become NPA on November 2, because we have considered all contract as November 1 as standard if on November 2, if some contract would have become NPA that was deferred to January 1, otherwise generally speaking it will start kicking from this month end, next month ultimately ending in March.

Ramesh Iyer: But can you simplify this whole problem more certainly we can put it this way that whatever dispensation we have taken, if we do not collect between February and March they will all become NPA.

Alpesh Mehta: And whatever the demonetization related specific NPA may be because of the inability to repay after the demonetization that NPL will hit us in 1Q of next year?

V. Ravi: Everything will be in March. March only, that thing will defer to the next financial year.

Ramesh Iyer: 152 Crores which we have taken as differentiation if no money is collected in the quarter this 152 Crores we will provide.

Dinesh Prajapati: Even if we collect and it remains in the same

Ramesh Iyer: If we collect and if they remain in NPL we will provide, we have to bring them out of NPA. That means they have to go below four EMIs.

Alpesh Mehta: No. My question over here is assuming that I had the account, which was standard as of July 31. We have 120 days till we recognize NPA after 120 days, right? It works out to till November 30 that account would have remained as a standard account and on December 1 it would have been categorized as the NPL account.

Ramesh Iyer: Can I simplify your problem? On 31st March whichever contract is four EMI outstanding will be NPA, whether they are November, December, dispensation, no dispensation forget all category, March 31, whichever account is four EMI outstanding will be NPA.

Alpesh Mehta: Thank you so much. That is it. Thank you.

Moderator: Thank you. Next question is from the line of Karthik Chellappa from Buena Vista Fund Management. Please go ahead.

Karthik Chellappa: Thank you very much for the opportunity Sir. A few questions given that high notes have been demonetized in future are we thinking about alternative collection mechanisms and if so how feasible is it?

Ramesh Iyer: So we are thinking we have the customer think, that we are introducing ECS, we are introducing PDC, we are introducing POS everything we are doing, but fundamentally his revenue stream has to change from cash to something else, then only he is going to use all this system. If he is selling and collecting cash his convenience is to pay us in cash. We should not forget that people were paying cash for two or three reasons, one it was very convenient for him to transfer his problem to us right, administratively that was the easiest one. Second is if he is paying in cash he chooses to pay whenever he wants. If he is giving an easiest instruction or PDC on the appointed day it will go into his bank and it has to be paid up, so that is the second problem that he has. The third problem he has is his inflow is a much unstructured inflow because of which he is not able to commit to you when and how he will pay. While taking a loan he knows that on 10th if he takes the loan, 10th of every months he has to repay, but his inflow does not support such a commitment and that is the facility we give and that is a premium we charge for that facility and therefore what is so far a strategic differentiator, we will not force ourselves to standardize it and make it difficult for us while we will attempt everywhere to provide that facility to make his and our life easy.

Karthik Chellappa: Okay got it and Sir with the increasing focus on formalizing the economy per se do you think some of the larger NBFCs who are hitherto focused in Tier 1 and Tier 2 towns can probably now start to get into your territory because their cash flow assessment at the margin become easier?

Ramesh Iyer: So our take is as follows. I think we have never feared of competition. We always have believed competition will expand the market. If all of us believe that another 10 NBFCs are going to come to rural market and the market will remain the same size then all 10 of us will kill each other. The 10 of us will have to come and expand the market. The market is so large that Mahindra Finance in spite of doing whatever it is doing is not cornering a very large market share, so the credit expansion will happen if more players come that is what the whole government push about financial inclusion and drive is all about. Government is not saying we want more NBFC or more finance company to come to rural because one company is making all the money or one company is doing all wrong things. They want more finance company and more banks so that more people can get the credit, so let us unnecessarily not pressurize ourselves by saying is more player going to make it more difficult for anyone to do any business my answer is no to that. The second thing is of course more players should come then what is the advantage of our player like us who has been there for 21 years with 4 million customers, 1100 branches, 24000 people and relationship with every OEM and every dealer. Unless we do everything wrong it is not so easy for someone to take over from us and why would we do anything wrong.

Karthik Chellappa: Got it. Sir on your observation of stepping up to the reposession rate this quarter now given that the second hand market would have virtually collapsed because of the cash crunch having such number of vehicles in stock 15000 would not you be in the way compounding the problem and do not you think the reprocess value will probably deteriorate further?

Ramesh Iyer: Okay, let us put it in three categories or rather two categories. Vehicle with us and vehicle with customer okay, customer is not paying and we are selling it at a low price, which better?

Karthik Chellappa: What I am trying to get at is the price at which you are selling?

Ramesh Iyer: No, no, I am saying. Let say customer owes me Rs.3 lakh of and he is not paying and I have got that vehicle with me and I get only Rs.225000 because the price has collapsed, I still think Rs.225000 is better?

Karthik Chellappa: But given the cash crunch instead of 225 how much do you think you will get now will it be like 2 lakhs?

Ramesh Iyer: I am talking cash crunch price of 225. I am saying 225 is what I get today for a vehicle suppose instead of 3 lakhs that the customer, see if the customer is able to pay regularly, I will not touch that vehicle that is why I explained saying we are repossessing from high delinquent account, people owe pay me in installment, 12 installment whose intension itself to repay is going to change, because he also sees a dip in his resale price, he is not earning enough, see why did we delay repossession first of all in the past, we delayed the repossession in the past when we saw the market conditions will improve due to infrastructure. We saw the market conditions will improve due to better crop, due to good monsoon. If those two events were to happen we thought there will be a better cash flow and many, many more people will repay and then at that stage whosever does not repay we can easily repossess then comes the demonetization which is making even borderline case becomes difficult to repay then we said, now do not delay at least repossess vehicles which are high delinquent even if we make a little loss. Now when we repossessed vehicle where we have met 50% provision, the book loss on vehicle will not be a high, because we have already provided 50% and our belief is that on a second hand market, however, the price drops at least 40%, 50% price can be recovered, yes we can recover the entire due of our customer, but at least in the book we may not have to incur a bigger loss on this vehicle. At the same time do not forget, 15000 on a standalone looks a large number compared to 6000 or 7000 vehicle that we had in the past or 10,000 in the past, but 15000 on a 2 million live customer and 15000 on a 2.5 lakh NPA case is not a very large number to worry about and 15000 spread over 1200 branches is not more than 8 to 10 vehicle per branch is again not a large number to worry about and all 15000 vehicles are not at the same type and therefore all of them will not in the same loss is the third thing is that we need not to worry about.

Karthik Chellappa: Okay and Sir lastly on this investigation proceeding which has been initiated by the sales tax department in Maharashtra, I thought the taxability on the sale of repossessed vehicle because we have been doing this in the normal course of business, should not give rise to any such claim, but it seems that they have initiated proceedings for the last five years and the amount is pretty sizeable almost like Rs.26 Crores odd, can you give a some color about this and what do you expect the outcome of this to be and can this set up precedent for sales tax department in other states to follow suite?

Ramesh Iyer: This is not the only state where we have a similar problem or we are not the only company who is having this problem, so one is collectively it is getting represented by the association with the sales tax authority who seem to appreciate what we say, but do not want to act, because it is a revenue stream, so that is the first level of basic understanding. Second is we do not capitalize this vehicle, it is held on trust on behalf of the defaulter and being sold out and out from the defaulter to another customer and therefore there is really no sale or no value add, so this all will have to go to the next level of tribunal or whatever you call it as where the documentary evidences will have to be proved. So this is the long drawn process, it will require RBI intervention, it will require association intervention, it will require legal interpretation, it will require continuous arguing of the case, at the end of the day, it can still happen they can tell you no story we do not understand all of this, we need revenue and therefore you have to pay.

Karthik Chellappa: Okay, right now, we have made the payment, but we have not made a provision.

Dinesh Prajapati: It is under protest.

Ramesh Iyer: It is under protest. It is a deposit.

V. Ravi: As of now we have treated it as an advance.

Karthik Chellappa: Thank you very much and wish you all the best.

Moderator: Thank you very much. Ladies and gentlemen as there are no further questions from the participants. I would now like to hand the conference over to Mr. Karan Singh from JM Financial for closing comments.

Karan Singh: On behalf of JM Financial, I would like to thank Mr. Iyer and the senior management team Mahindra and Mahindra Financial Services and all the participants who are joining us in the call today. Thank you and good-bye.

Moderator: Thank you very much. On behalf of JM Financial that concludes this conference. Thank you for joining us. You may now disconnect your lines.