"Mahindra & Mahindra Financial Services 1QFY15 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Mahindra & Mahindra Financial Services Limited 1QFY15 Earnings Conference Call, hosted by Ambit Capital Private Limited. As a reminder, all participants' lines will be in the listen-only mode. 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. Aadesh Mehta from Ambit Capital. Thank you and over to you Mr. Mehta!

Aadesh Mehta: Good morning everyone. This is Aadesh Mehta from Ambit Capital. I welcome you all on the first quarter FY2015 Earnings Conference Call of Mahindra & Mahindra Financial Services. The officials who are representing the company on this call are Mr. Ramesh Iyer, Managing Director; Mr. V. Ravi, the CFO; Mr. Dinesh Prajapati, Vice President Treasury and Corporate Affairs; and Mr. Rakesh Bildani, Senior Manager, Treasury. Thank you gentlemen for joining this call and over to you Mr. Iyer!

Ramesh Iyer: Good morning. This has been one of our toughest quarters from the time we have been running this business model and right upfront I would like to state that the few events, which have caused the outcome of this quarter and will be interesting for you to know lot of them and how do we think we are going to handle it going forward.

One of course is the overall fundamental, still remains muted and that can be very clearly seen from the overall business volumes of various auto products and also coupled with that is the discounting of the vehicles continues to keep happening and at least the product-lines that we are in like the small car segment are available today at possibly the highest discount ratios and therefore even if the volumes were to be the same, I think the disbursements were expected to be lower with the price point being 10%, 12% lower than normal due to discounts.

Secondly, of course the volumes itself have also been lower. So these two clearly are the impacts that are causing the disbursement degrowth for us and as we have been saying regularly that this is not the time where we would like to chase market share growth. We would rather stay with a little lower disbursement but would not want to chase a market share growth clearly because we do not yet see that the fundamentals at the ground level are changing rapidly. It is yet not. That is not what we are witnessing. It is also important to bifurcate between commercial application and personal segment application and what was originally impacting just the heavy commercial vehicle segment has slowly percolated down even to the LCVs and sub-0.5 tonne vehicle and that is purely caused again by no increase in freight rates possibly lower volumes there whereas another cost of operations like diesel prices going up even their own little labour whatever that they engage with whether it is driver, cleaners that pricing going up and therefore the overall cash flows of even this segment has got impacted.

So given this background, we are very clear that this is not the time that we would like to chase disbursement. We are maintaining market share but one good news along with that is many more players and this we have been seeing it for some time and we are seeing it now in action on the ground is whether it is Toyota, whether it is Ford, whether it is Nissan whether it is Hyundai, all of them are really put in place now a very strong rural programme with more dealers out there using our services for reach and we do expect that even if overall volumes do not change but we get benefit of new product launches there, the benefit of no price increase we believe that another one quarter the discounts will continue if at all the change one can only see from the festival season. So once that correction also happens is the only time that one can start seeing some improvement to the disbursements happening but I think apart from all of this one another major event that has caused, the quality of asset in terms of overall collections and therefore increase in the gross NPA is the event of election.

It is very important to understand that our business is completely on the street business model and every time this is not something new that we are seeing but at this time the elections spread over two months virtually has had one of its major impact and the impact is we are not as much comfortable and allowed to really collect and carry cash from customer to branches. There are some administrative restrictions, the vehicles do get inspected and if cash is carried we need to surrender them and we have had some examples of needing to surrender them and therefore we have taken a very, very cautious view of how much do we really want to reach out and really collect cash during this period.

Also, on the other side, simultaneously the customers who deploy their vehicles and collect cash against their billing also have been simultaneously impacted. So, the overall impact comes from low collection or low activity in these two months and this result has to be definitely seen from the perspective of out of the 90 days and effective working of about 35, 40 days is what is available for us to be able to do what we have done and in a model like this where people earn and repay, what they do not earn for at least 30, 40 days, it is impossible for them to earn in the next 15, 20 days and start paying that and that is what has got really cumulated and therefore the increase in NPL number per se if you see they have all happened in the first bucket of NPL which means new contracts move into it and we have analysed them to see and most of these contracts are not contracts which have been just transacted. They are customers who have been with us for 12 months, 18 months and repaid over a period of time; two installments, three installments outstanding is what has jumped into the NPL by two installments not pay and we therefore kind of comfortable to believe that this event having already over, this is not repetitive in nature, but the fundamental has to substantially correct for all of this to get corrected in a shorter time.

So will this get corrected? My answer would be yes, of course it will be corrected, but when it corrected in 30 days, 60 days time? I would answer no, we will think that it may take may be two quarters to get this correction in place because people do not earn that kind of money to repay immediately the whole installments. There is also another factor to it that during this period administratively we are not even able to repossess vehicles or even get vehicle surrender from customers because you do not get the necessary administrative support either from the police or the court or whatever if necessary because they are discouraging this kind of activity during election periods. Now, for once we are not ascribing to the view that we need to repossess all these vehicles or we would have repossessed all these vehicles, the answer is no, but clearly high bucket provisioning items if there was an opportunity to take back the vehicles, put pressure on the customer to ask them to surrender vehicles even those activities come to much, much slower and lower levels as compared to what normally happens in every month. So I would largely think that the major event which has caused the delay of collection and therefore built up of such an NPA would be one of course the fundamentals are yet to show major correction but more importantly also the election because if you look at year-by-year, every time the first and the second quarter is always a build-up and therefore if everything was normal, we would have still seen a growth of NPL based on the overall base number of contracts that we have transacted in the one year period but that has further jumped to a level which has been caused by the events that I just explained.

We continue to believe that the NPLs will in this business will never go below 3 even if everything had to normalise and we would have expected that we would never cross the threshold of 5 bearing this one event that I explained in detail if you were to kind of put a number to it not that we are able to quantify it absolutely, but I would still think that if we were to put a number to an event how much delay would have been because of that we would think we would still have ended up with an NPL number of 4.8% or 5% kind of region and that something is during the year as we close we believe can be the range that we would like to look at.

We are not in a position today to forecast with what is happening at the ground level that we will go below 4% as a gross NPA unless everything substantially normalises. Our own take is that we do not expect any event of normalisation before the festival season and one last thing would be the monsoon sentiments. It is not right to say that the first quarter impact is anything big on account of monsoon. Yes, middle of June there was an announcement that the monsoon is likely to be low and it had its own sentimental impact, too little in terms of quantifying that but I think the trend of that announcement is that this will be lower to the quarter.

The good news as we speak is at least slowly averaging it out. It is not as low as it was even a couple of days back or a couple of weeks back, but it may with this it will only end up at an average level of monsoon and it is not yet widespread so there will be some states which may have a little more impact than some other but it will only average out as we move along but for a business like our where direct farm dependent is now as low as may be 10% or so whilst tractors could be 16%, 18%, tractors do continue to be deployed in the contracting segment, but direct farm exposure could be 10%, 12% and those 10%, 12% in some pockets will have some impact of delay, but monsoon is an issue of sentiment that we would like to very closely watch and we believe that no sooner monsoon is declared even average, it could be a good news for us going forward but one needs to wait for one more month to get to that.

Technically if you look at it the sowing has been delayed and with the delayed sowing the time between sowing and harvest gets shrunk unless the season itself gets extended further but if the season was not to get extended and if you were to take closing of monsoon at the normal time then the time between sowing and harvest would get shrunk which would mean that there is going to be some impact on yields, which is what I am talking of a little cash flow impact that can have on the direct farm exposure. We are yet not seeing any major infrastructural announcement which is going to build excitement in improvement at the ground level, which is why the commercial vehicle segment continues to be under pressure. One did see some positives in the commercial vehicle segment but more driven by oil tanker application because the oil company announcing some tender but still the goods or container or tipper segment is still not showing any major upward trend and therefore we do not think the infrastructure story is still up but there are a lot of discussions, talks; the budget gives some direction about it but even if they make some announcements of the projects now for them to start becoming a reality 3-6 months before activity can commence, so our take for the year would be continuing to focus more on collections, our talk of the year will be go more deeper in the first quarter we have added close to 100 branches and we believe that those branch infrastructure that we are creating are going to for sure help us do better recovery but more importantly when market conditions are improving we already are in locations from where we can even start commencing some business over a period of time.

In this period, we have also tried and curtailed the expenditure to the extent that is possible to be, we do not want to be over-curtailing expenditure and building a new pressure on the people front and on the execution front but we have been able to register some curtailment of expenditure as well on this front. No pressures on margin even as we speak. The lending rates still hold up. The borrowing cost is not going up for us but what you see as a little shrinkage to the margin there is on account of the income reversals that would have happened on account of NPL, but they are not surely on account of lending rate dip or borrowing cost increase.

During this period we have been rated AAA by two rating agencies and we believe going forward that would help us at least improve our borrowing cost to an extent possible but our approach is going to be cautious; we are going to be more inclined towards quality controls, more inclined towards better collection and take advantage in this three months, six months where even the business levels are low to be able to correct whatever has happened in the first quarter due to the delayed cash flows at the customer end. June as I explained itself showed improvement and we think going forward we will see such improvements but not large enough to get all correction in the shortest time that has happened in the first quarter.

We do not expect credit losses to substantially dip unless we decide to repossess all vehicles that are in the segment and that is not our direction at all. Our LTVs are still at 71% and therefore we think the credit losses from here are not likely to further increase. The resale prices surely are under pressure because the discounts on the new vehicles are continuing but if no further discounts are to be offered and if one sees some correction to the price in the next two quarters one can in fact be benefited out of it but not taking that into account, we do not forecast that there is going to be any major credit loss shift happening whilst the NPL numbers be where it is.

On the NPL to conclude I would say that the range will still be 3-5%. We believe as we close the year we may be close to that 5% range because we do not see any major negative event going forward from here unless the monsoon substantially ends up disastrous and absolutely no infrastructure story begins and no fundamental correction happens to the market then that is a different communication we may have 3-6 months from today but the way it is forecasted from now if monsoon ends average if the infrastructure story does begin at the ground level and if corrections to the discounts on the vehicles do happen, I think we still want to put that it is an effort job. What is built will take two quarters to correct and therefore we may end up at a 5% level of an NPA which is what our forecast even at the beginning was and we think this business model will continue. If everything normalises till the disbursement possibly could be only in the vicinity of a single digit to a little upward of that because we already lost three months and we do not think the next three months are going to register disbursement growth and therefore festival to March may not be good enough to drive substantially large volumes and we are not wanting to gain market share in this would actually be the summary of our call.

We have added people and we are getting future ready both for collection and recovery is the way we will drive this business model. As far as the other subsidiaries are concerned, I think they are on a good news wicket. So far the MRHF and that the rural housing venture is concerned, they are continuing to double their balance sheet. They are growing at a very aggressive rate. Their margins are also not under pressure. They are able to raise funds and we would continue to kind of move forward with the dream that we projected that by 2015 can we look at a balance sheet of Rs3,500, Rs4,000 Crores, looks doable, but again since they are operating in the same rural market they also had their share of collection issues in some of these pockets but I think the kind of base numbers being pretty low, one would see that they are able to register growth.

As far as insurance broking is concerned again they have a direct strategy connection so if our volumes are less, their volumes are expected to be less and we are yet not providing insurance in an open market to many more agencies; so they are still supporting many of our existing customers or rural housing or a dealer community and therefore they have also had a volume impact, but profitability has been maintained by them. Whilst overall we think that all products, all geographies have had this election and fundamental issues but the southern market continues to be slow and within the southern market Tamil Nadu has yet not shown any signs of improvement and the immediate reaction of low monsoon, we think is more felt in states like Maharashtra, Madhya Pradesh, and Rajasthan as compared to any other state and these are the places where initial announcement of low monsoon has come about and they are the ones who normally go for early sowing and they have delayed that and therefore it is interesting to watch these states as to how they pan out from the monsoon point of view, at least end of July or first week of August.

Things have improved but not substantial enough to feel very happy and comfortable about. So I think those are my initial remarks and anything on the particular number part of it Dinesh is here, Ravi is here, Rakesh is here and if you open it up to questions then one of us will take it and answer on whatever other questions. So thank you so much and that we thought is the summary from our side on where we are and where we want to go.

Moderator: Thank you very much Sir. Ladies and gentlemen, we will now begin the question and answer session. First question is from the line of Sunil Thirumalai from Credit Suisse. Please go ahead.

Sunil Thirumalai: Thank you for the opportunity. I just want to know going back three months when we had the analyst meet in Mumbai and I remember it was I think a day before the election in Mumbai, we had the kind of sense we got on the situation on the ground was a lot more optimistic than what it eventually turned out to be and we had already seen a couple of weeks of elections nationwide and then various places before that. I am just wondering was there anything which significantly changed after that event in the subsequent phases of elections that caused the actual result for the quarter to deviate so much from the kind of indication we got.

Ramesh Iyer: That was in April kind of third week or something like that. So that is the time we met but I think the states that had gone through then were not so very significant in terms of the event but I think more importantly I would not want to say is it an announcement for us to do something or not do something. I think it is just our experience of ground reality. When we started seeing in some of these markets clearly we being stopped, cash need to be surrendered to the police if you carry cash from a location-to-location. Customers not therefore handling cash, these are the events which is dynamic and one needs to take a call as you move along. So clearly it is difficult for one to forecast that this is how it would be.

At the same time it is also very difficult to say at what stage in which state when will you do what but as things change from then to the end of May the answer is yes we were extremely, extremely cautious on what we want to do and definitely not repossess and get into any major issues out there, but as I explained look at June for us we looked at June independent of the three months and we are very comfortable to feel that to what extent the event is impacted and to what extent the fundamentals are weak.

Sunil Thirumalai: Also, you have been saying for some time that the NPAs will not grow beyond 5% but this quarter we accept it is because of some events it crossed 6% but I am surprised that you are saying that the NPA by end of the year will probably get back to only 5%. So where are the range above 5% now versus range below 5%, is that my right understanding?

Ramesh Iyer: Unless the fundamentals at the ground level get corrected, we do not want to even if you look at the previous year we were also hovering around 4.2-4.8% and has anything changed from then to now fundamentally at the ground level at least our understanding is it is not. Sentiments must have, expectations must have turned positive but actions are not yet. The inflation is still up there, interest rates are not coming down, freight rates are not increasing, volumes are not there, fuel price is still high and so I do not want to at this stage take a view that six months from today everything is going to be very good and we can definitely correct, but surely these models are when things starting correcting, you will get the benefit from day one, and when things go bad it starts going bad from day one. These are event-by-event, transaction-by-transaction, state-by-state, day-by-day. So suddenly you see volumes pick up, infrastructure projects get announced, mobilisation advances start coming in to the market. You will see volumes pick up overnight. It may not give you opportunity to prepare, so that is why we are saying create branch, add people, use them for collection now but be ready when that opportunity opens do not miss it.

Now this is not our guidance but I am saying if things really start becoming absolutely buoyant from festival we may go back to even two-year back-story of 3% NPA because infrastructurally we are ready, people-wise we are ready, the customers have the vehicle, resale markets are extremely good and if potential of earnings is there, people do not even want to surrender vehicle but I am just saying as we speak today we are not able to forecast a substantial change happening in such a short time and therefore we want to stay cautious.

Sunil Thirumalai: Sir one just last question. I just wanted to understand the problem in collections, was that specific to any particular asset segment or was it spread all across because that was one of the things that we have been talking about saying that the book is now quite diversified and so one particular segment getting under stress should not really impact the overall book. So I am just curious to know how each of the segments fair in terms of collection and NPAs?

Ramesh Iyer: I mean if you look at the overall book it is not product, I think we will have to start looking at it by application. So if you look at most of our asset, if they are earn and pay asset even cars for that matter which are in taxi application is the one which will get impacted. Personal segment has got least impacted. The commercial segment be it car, be it LCV, be it three-wheeler, be it pickup those are the ones which will get impacted. That is the way you will have to look at it. The second way to look at it is if the monsoon turns out to be weaker, it will impact the tractor farm exposure. So I think by geography I do not think new geography has got added for impact whereas what has got impacted would be by application and the commercial segment because of the cost of operations have gone up whereas the freight or the recovery of their pricing has not moved up substantially there is going to be this delay happening.

Sunil Thirumalai: Thank you very much. I will come back later for questions.

Moderator: Thank you. We move on to the next question that is from the line of Rishi Arya from Canara HSBC. Please go ahead.

Rishi Arya: Good afternoon. My question is a bit more general, when we talk to banks their asset quality cycle is kind of bottoming up. I mean they talk about that this year the things are going to get better and when all this whilst Mahindra Finance has been very robust and they did not see the NPA cycle, now when the bank cycle is getting over, we are seeing pressure here. So is it like the catch up is happening in the rural economy? So how do you explain this?

Ramesh Iyer: Historically first we will always have the first quarter NPA going up so you will neutralise it for the normal increase that happens. So let us say the election and things like that were not there, we would have still increased our overall NPA from where we closed clearly because if you do half a million contract in a year some of them even on a normal 2% basis become eligible in the NPA category because these are all those kind of profiles and customers and earning vehicle which will go through that cycle. So first is to normalise it for year-on-year event then come to the specific event of what happened in this quarter which takes away 30, 40 days of efficient working at the ground level. Therefore, I am saying what will get corrected is what is caused by this event and that may bring it down from a 6% to 5% level, for everything else to correct the fundamentals have to change, that is nothing to do with April or May particularly.

Rishi Arya: So in fundamental what are the leading indicators you look at it from your market point of view?

Ramesh Iyer: I do not personally think very clearly that if at least the overall volume of business at the local level needs to go up. Like supposing commercial vehicle segment starts performing decently well. The mining segment recommences because the entire economy of certain geography depends on certain activity of that type. Like in Tamil Nadu if you were to look at if the power situation improves, the SME segment, the textile segment starts improving, the labour community starts moving up and down, the three-wheeler segment starts improving, the small pickup vehicle starts improving.

Rishi Arya: Mining and everything has been down, commercial vehicle has been down for the last two, three years but Mahindra Finance was doing well?

Ramesh Iyer: Let us be very clear. We are not exposed to heavy commercial vehicle. The mining impact on the third level of operations will not happen as soon as mining starts. So heavy commercial vehicle or the tipper or the excavation equipment will first get impacted but dependent vehicle will always be affected subsequently and much more importantly if cost of operations increase whereas the customers are not able to increase their prices to their ultimate user; the overall cash surplus left in hand will come down, so they are not able to kind of pay. If suppose two installments are overdue earlier they used to pay off, today they are not able to service more than one installment, it is going to take that little increased time.

Rishi Arya: Sir over the next one year, couple of quarters how would the asset side change in terms of product mix, would there be any change in that? Would that happen should we expect some product mix change over next couple of quarter?

Ramesh Iyer: I mean not significant may be 1% or 2% up and there like maybe second-hand vehicle may move up from 14%, 15% to 16%, 17% levels. Tractor may possibly move up if they are talking of 8%, 10% growth possibility, tractor will move from 17% to 18%, 19%; cars may come down a little but on an overall basis we do not see a swing in product mix change.

Rishi Arya: Thank you.

Moderator: Thank you. The next question is from the line of Jonathan Prigoff from Equinox Partners. Please go ahead.

Jonathan Prigoff: It seems like you guys and the analyst community were surprised by the performance here given that as you said you guided kind of 5% was a weak in the past and it is obviously over that. Given that there have been numerous elections in the past, I am wondering why this was so surprising and more generally I think analysts might be saying that last year we had some asset quality issues which were attributed to one-time events, now we have got another round of asset quality issues that are one-time events, when do we get a period where there are not some of these one-time events?

Ramesh Iyer: If you look at two years back we never had any event. So it was kind of maintaining and growing, the market conditions were positive, conducive to be able to handle it. So one-time event, it is unfortunate that it happens and we have to face it. It is just that the strength of the business model that we are able to accommodate this, go forward and get it corrected. So the models do not crack when you have one-time event but definite delays do happen. Like you touched upon even in the earlier round we had election, but it is important to know that five years back when we had the election the economic condition was substantially superior, so that event does not impact you so much, but when you have a situation where the ground fundamentals are weak you also have an event of this type coming together then the pressure start mounting and I do not think we have had such a large range of election period in the past; it used to be much shorter cycles and state elections do happen, but state elections impact you for three days kind of situation.

So we do not necessarily use them as one-time impact of the overall country, yes that particular state which goes through we will have an impact for about a week and then you get time to normalise it in the same month possibly, but now the basic fundamentals are also weak on top of that you have an event of this type and there are uncertainties around and I will not still say that the rural does not have cash. They definitely do have cash. They may sentimentally must have held back if the monsoon is declared to be little weaker that some other event until the monsoon is close and once unless it is declared the sowing is down, the yield is known to be what it is likely to be even if people have money they would delay it. So I think in a rural market it is important that we will have to build models which has its ability to observe this kind of a transactional impact which comes through, but it is a question of do you still want to continue in that geography then you have the partnership approach and the patience to continue, but if you decide everything is going wrong you want to vacate that market then we will approach it on a cut loss basis. So our approach today is that we are widespread across the country, we understand what is happening in that market, we are deep-rooted, we have added 100 more branches in this first quarter, so we are getting prepared to say yes things will change in a cycle and then get complete benefit of it, but this model is built to handle such events which will come through may be in a shorter time, it can come through and stay for a little longer than one can expect but the model is built to be able to handle this kind of transactional impact.

Jonathan Prigoff: I guess just a pushback on that a little bit I mean my understanding of the way the elections work and I am no expert on this, is the entire election across the entire country lasts two months but happens at different times in different places and as you said these are small rural markets so each market might be impacted for some period but there is no way that each market was impacted by the election for the entire two months?

Ramesh Iyer: Let me clarify, let us take only one market was impacted. Let us take elections in a place for 15 days or 10 days whatever is the period because pre-post election time has to be considered not just the election date, and so the election date may be for different dates announced in different places, but the election period is the same across the country and that is where they engage themselves with and ground activities do not really happen. So much of the administration is so active, our business model is on the street, we go and collect cash and there are instances where we are stopped when we carry cash in the vehicle because they want to stop cash movement for any purpose and which is where we have to take a cautious view to say is this the time we should reach out or is this the time to stay put and then get it corrected.

Now when the economic activity itself does not happen so much, the vehicles do not earn so much. These people do not have an ability that where the earning start that they can earn enough to pay immediately for two months on default. They will only neutralise it over a period but what they pay for is the penal interest for the delayed installment and that we have been able to collect and if you look at our NPL customer contract, there are people who have borrowed from us 12 months back, 18 months back and they are paying. They are billed two, three installments, this period another two installments got added, so they become an NPL but they are not kind of absolutely stuck, no movement contract. They are all contracts with movement and they are people who pay it back. We do not want to resort even today to repossession because the resale prices are not very favourable but whereas we believe that these customers are earning, they will continue to pay their installments and we will collect the overdue installments over a period of time that is the kind of approach that we are taking.

Jonathan Prigoff: I saw there was some management changes announced yesterday, could you clarify what is going on in the management of the company?

Ramesh Iyer: I think somewhere wrongly captured or whatever, we have actually nothing, but we have added one member to the board and he is the CFO of the group. Mr. S. V. Parthasarathy, who was the CFO of Mahindra & Mahindra has joined Mahindra Finance Board whereas I think I do not know from where the channels picked it up wrongly and announced this CFO inducted or something like that. We also got this message and then they have well subsequently corrected but if you see our stock exchange announcement, Mr. S. V. Parthasarathy who is the CFO of M & M is inducted into our board.

Jonathan Prigoff: Thank you.

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

Karthik Chellappa: Thank you for the opportunity. Firstly, given that June was by and large a month which did not have any election impact, can you share some amount of detail on how your collection efficiency was in June compared to say April and May, just wanted to get a sense?

Ramesh Iyer: I can give you some range but Dinesh or somebody will deal with it may be sometime later, he may not have it immediate, what I know for sure that at least 4%, 5% collection efficiency in June would have been higher than April and May.

Karthik Chellappa: My second question is on the impact of the monsoon, I know it is early days yet and probably by the end of the second quarter we can have better clarity but assuming monsoons turn out to be average, will it mean that our asset quality in terms of gross NPA will probably bottom out at that level and start to improve in the second half or will it still lead a substantial improvement in the second half for us to hit that 5% target assuming monsoons turnout to be average?

Ramesh Iyer: I think the first collection to our gross NPL will happen in those contracts which are built up due to the April-May event. That is the first correction which will happen and that will take in my opinion two quarters to correct because they cannot earn so much to pay you immediately two or three installments so they will neutralise it over a period of time. As otherwise monsoon by itself if it is declared average it is not something to overtly worry except in market, average is still a very macro number. There will be some states which will have different monsoon levels, some could be good, and some could be bad as well. So to that extent we will be concerned only in those respective pockets but it is very, very important to understand that the basic economic activity has to pick up for the overall commercial segment or whether it is a small vehicle or heavy commercial vehicle to start performing well. Otherwise, they will be under pressure and they can only pay their monthly installments, it is difficult for them to correct the overdue that is built over a period of time immediately.

Karthik Chellappa: So if it reasonable for us to assume that this quarter the NPA very little of it is attributable to a poor start to the monsoon?

Ramesh Iyer: First quarter it is nothing to do with monsoon except some sentimental impact when 15 or 18 or some time when the department announced that the monsoon is likely to be weak this year so people just hold back some money saying let us wait but I do not think we can put any substantial value to the monsoon impact already.

Karthik Chellappa: So any impact if at all will probably manifest only in the second quarter?

Ramesh Iyer: I would think so that has been historic I mean it is too early the first quarter because even if monsoons were normal in June the sentiments would have been positive; some sowing would have happened, but it would still not have had major positive impact on collections or whatever.

Karthik Chellappa: Sir earlier in your opening remarks you have made a statement that you will be going slow on disbursement, so you are not keen on incremental market share and you will be looking to maintain your market share. In that context, how do you assess say some of your peers who are also operating in the same segment as you are let us say with reference to CVs or so, with respect to the discipline in the industry I mean what will happen if your peers continue to offer say a higher LTV product or so in which case you may have to lose some market share. If that is the case what will be the trade-off that you will be making? Do you think the industry right now is disciplined enough for everyone to grow slowly or there are still pockets of aggression from some of your peers?

Ramesh Iyer: Let me first clarify that I may not be able to speak for industry but one is to look at your own strength, your own capability and your own requirement and design. We believe this is not a time to compete what is happening at the market level. If somebody is offering 90%, 95% even 100% finance, they may have a method to handle it better than we believe we have. So we have ensured that our LTVs remain at the range of 70% to 75% and we do not want to overstretch that. Then come to products where such competition could emerge and where we could lose market share the point that you made. We have 30% market shares for Mahindra Auto and we have almost same number 29%, 30% for Mahindra Tractors and Swaraj. We have Maruti about 8% to 10%. Rest of the products our market share is anywhere 3-5% kind of a situation. So whenever we make a statement we do not want to really gain market share, it will be for at least those three major matured products, which is where if we have to really gain market share we will have to do something very different from normal.

Now wherever we have 3%, 5% market share it is more about how much more vehicles do those manufacturers want to sell in the rural market. If Hyundai has now said that 30%, 40% of the sales they want to come to rural from a current 15%, 20%. My market share will go up even if I do nothing and I just operate the normal way because they are selling more vehicles. If new products like a Nissan or a Toyota or a Ford talk of launching products for rural that is a new addition of LMV, which will come to me, so we will not want to change our product offerings. We do not want to cut on lending rates and gain market share as the statement. If more vehicles get sold off either same manufacturer in that market we may be benefited if new manufacturer comes and sells surely we will get some volume benefit. So to that extent the disbursement will move in one way but gaining market share is not something we want to do even if somebody comes and says they are offering 8% lending rate. I think we will wish them well. We may not want to participate.

Karthik Chellappa: My last question is on the provision coverage. I know in the past in the number of calls you have always highlighted that there is a cyclical element to the coverage when NPL spikes in the first half and it comes down in the second half, so more or less it evens out but recent quarters progressively we have been touching the 50-55% range whereas may be a year or two back we used to be comfortable in the 75-80% range. So what are your thoughts on this coverage ratio what seems to be kind of like falling let us say over the quarter?

Ramesh Iyer: Whether 50% or 75% is an outcome of the bucket of NPA, let us say if all this contracts which are in NPL now for the next three quarters do not get corrected and they move to the next bucket of provisioning which is 50% cover automatically you will see coverage going up. So when you get a bunch of new contracts, meaning contracts which are not in NPL, now move into NPL they are in the first bucket of coverage and therefore you see a dip. So two ways you will see coverage increase let us say all these contracts which moved into NPL in this quarter gets fully collected and what remains in NPL is high provided one, you will see the coverage looking very, very high. So it is not due to any corrections in our provisioning method or change of policy or looking at provisioning very differently, no those basics have remained the same. It is only by age of the contract which is in the NPL bucket which reflects the coverage.

Karthik Chellappa: Thank you. I will come back later in case if I have any further questions. Thank you.

Moderator: Thank you. We move on to the next question from the line of Anita Rangan from HSBC Asset Management. Please go ahead.

Anita Rangan: Good afternoon. Could you be able give us the segment-wise NPA in your various segment bucket so that we can understand like which sectors are seeing most stress and probably which will see like better recovery going forward?

Ramesh Iyer: I think that is not the way we look at. We more look at what is the overall portfolio movement is and may be when you speak to Dinesh or Rakesh at some future date, they can give you some ballpark indication but that is not the way we will look at it at all, but I will personally though think that historically if you look at that percentage would not substantially change temporarily sometimes like during monsoon tractors could up and harvest tractor will come down and second-hand vehicle may possibly remain constant all through the period. Commercial vehicle when the economic turnaround is not good it will spike and it will fall. So I do not think that is a way we kind of look at this. We kind of look at by a branch, what are the movement and therefore what is the effort that is required so it is not by product and in this round I can tell you for sure that every product would have inched forward because of the overall situation being what it is. It is wrong to say that this geography or this product has done extremely well or this geography or this product has not done well. So I think it is overall otherwise it could never reach this level where it has reached.

Anita Rangan: You did mention that in June the collection efficiency actually improved by 4% to 5%, can you if possible tell us as we speak is there like any further improvement we are seeing in the collection efficiencies?

Ramesh Iyer: Will it be better than June and July the answer should be no because after all what if the June activity will continue in July. June has improved because April-May was be poor whereas June is not better because in June something new has happened out as an activity, so June and July will not be very different, but June will surely be better than April-May because the activity levels see fundamentally we must understand that what we are trying to explain is the overall activity level in the rural market because of the event was extremely low in April-May and that have got normalised to an extent in June that does not mean fundamental overall economy has improved.

Anita Rangan: Thank you.

Moderator: Thank you. The next question is from the line of Vikesh Gandhi from Bank of America Merrill Lynch. Please go ahead.

Vikesh Gandhi: Good afternoon, Sir. I had couple of questions, one is can you just give some more details around how much is the collection staff in your fold? How much it has moved up if you can give some indication around last one year, two years? How many of your current branches are solely and wholly focusing on just collections and leave aside the business part? The second question is just probably a shorter one, how much of your AUM would be linked around farm exposures?

Ramesh Iyer: If you talk of two three years, collection boys increased it would have doubled according to me because we add about 1,000 people every year, of which about 30% will go towards business and other activity and about 60%, 70% normally for collection and therefore if we were 1,500- 2,000 people or plus three years back we would at least be 4,000-5,000 people now in the collection front because collection boys whilst they do only collection, business people also do business plus collection. The first eight, nine months they are also responsible for the initial demand collections. So you will have a mix of two plus we have a set of people who are exclusively on NPA collection monitoring and there are people exclusively with the legal team for high bucket collections, but normally in three years time definitely the number would have doubled in terms of overall collection is concerned.

Exclusive collection branches would be around 200-250, of which 60%, 70% of them would have got added last year because otherwise earlier all our branches were district and village branches which had both activity. We added 200 branches specific for this purpose in deeper pockets and in this quarter we have added another 100 branches of which about 60%, 70% branches would exclusively handle collection until the overall market conditions improve for them to be able to handle both of this by adding more people there.

Vikesh Gandhi: Sir when you are saying 200, 250, are you including the 60%, 70% in that or is it outside of that?

Ramesh Iyer: Outside of that I am talking of this quarter because this quarter what we added May, June what we have added will really start functioning from now in a big way. Those people have to move from district headquarters, people are handling the contracts there will move out there, systems will get set up etc., etc. They are not fully functional let us say when they get opened immediately. On an overall basis one can say about 250, 275 branches will exclusively focus on collections whilst all other branches would do multiple activities. On the AUM front I think our total tractor is about 18-20% but within tractor one should know 30% 40% of cash flow is non-farm, so pure farm I do not know whether it is good to put a 60% to this 18% and say it is about 11%, 12% direct but tractor itself in the overall is about 18%, 20% and there would be some three wheelers and even pickup vehicles which has 10-20% farm dependent. So I would think on an AUM basis if you were to take a mix of all of this about 20% one can say is farm dependent.

Vikesh Gandhi: Sir just one more question I had was, you mentioned couple of times that your target for the NPLs year end would be around 5% and this is my understanding if I was to today your AUM growth is 16% for the quarter YoY but let us assume fiscal 2015 your AUM growth is somewhere around 15% if not more if not less, if I do some backward calculations, I come to a conclusion that the decline in absolute numbers from where you are today would be roughly not even more than 5% and if I put that on the 15% AUM growth and the outstanding AUM at the year end, the gross NPLs will be still somewhere around 5.6%-odd, so I am just not able to tie in the 5% part?

Ramesh Iyer: You are kind of saying if the asset is growing at 15% and your NPA remains where it is?

Vikesh Gandhi: Not where it is I mean…

Ramesh Iyer: Some marginal correction.

Vikesh Gandhi: Some marginal correction based on if I assume around that?

Ramesh Iyer: Let me clarify when I said that today we are at 6 point whatever I am saying 1% whilst we are not absolutely quantifying but I am saying 1% is on account of April-May event that by itself should have corrected and therefore we are putting up 5% and we are not taking any fundamental-based correction and if actually assets grow by 15% then it should be below 5% by that method. So the fundamental correction to this number, I am at this stage assuming only the impact which has happened due to delayed cash flow, delayed activity which was observed during April-May, will get corrected and I am not taking any correction to the fundamentals of the rural market or the economy turning around or better monsoon or none of those.

Vikesh Gandhi: Thank you.

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

Anand Vasudevan: Just like to get your take on the potential impact on funding costs due to the recent tax and regulatory changes, so the impact of long-term capital gains on debt mutual funds which might have been a source of funding for you and also the possibility that over time bank bond issuances will compete with NBFC bond issuances?

Ramesh Iyer: One is that this particular thing at this point of time of course yes debt mutual funds are the subscribers for both money market instruments, CP as well as for our NCD and it should be impacted in terms of the CP, which should inch up in case basically we are talking beyond October. I feel that probably from September 1 onwards people will try to revive in case no announcement in the budget is going to be made then during the budget passing session so somewhere from October, middle of September we are expecting something like about 25, 30 basis point hike in CP and of course correspondingly NCD and as far as the long-term money is concerned, we are roughly about 15% of our funds are coming from mutual fund both short term and long term; how much it will come down, how much the debt mutual fund is going to be impacted but one way to look at it is that there will be more certainty, what is happening is that in SMP money so far we are not able to say 18 months or 24 months is a kind of period they are giving in case probably people try to lock the money for three years whomever can afford to, we will expect some kind of term money from mutual fund.

Coming to fixed deposits since we have fixed deposit licence, we expect some kind of positive in fact last 10 days also we have been sort of feeling that and we are seeing it there are some high net worth individuals who are going to shift from SMP to good company fixed deposits since we have both long-term as well as short-term AAA. In fact our fixed deposit is rated AAA by

CRISIL. Our long-term bonds are also rated AAA by both Fitch and Brickworks. So we feel that many high net worth individuals, a portion of their money, how much of their portion it is too early to say, a portion of their money assuming that debt mutual fund will continue to be where it is if the budget is not going to be, they are not going to make any amendment to the suggestion which is put forward. I feel that some kind of money should come in the fixed deposit where we will be in a position to bring down the fixed deposit rate. So there is going to be a positive impact on our fixed deposit programme and there is going to be some kind of negative impact yes we will have to go to the bank treasury to get them subscribed to our bonds because bank treasury fortunately the base rate is not applicable, so we may have to go and convince the bank treasury to subscribe to our bonds.

Anand Vasudevan: So overall what sort of impact would you expect on your cost of funds everything else being the same?

Ramesh Iyer: As far as cost of funds since what we saw last couple of years if you see our exposure from the banking market has been on a higher side and we have seen some bond market opening up even though you may see the mutual fund industry may not be able to participate in the same manner but due to our AAA rating probably we will be able to get exposure from the other institutional market places like insurance companies and those type of institutions which will help us to average out the borrowing so I would say marginally if at all there is possibility whenever the rate correction is expected somewhere around December or January, you may start looking at the positive side as of then the negative part of it.

Anand Vasudevan: Thank you.

Moderator: Thank you. The next question is from the line of Sachin Bhardwaj from Birla Sunlife Insurance. Please go ahead.

Sachin Bhardwaj: I would just like to understand how do you track the productivity levels of loan origination staff? **S**o is it in terms of the number of disbursements or number of sanctions on a monthly basis and what are the levels currently?

Ramesh Iyer: It is by number of contracts with each one and what the benchmark that one business executive the best is about 20 vehicles, the lowest he should be actually doing 15 vehicles. Whenever the market conditions are not good they are better used for even recovery from the lower bucket customers because that is anywhere their prime responsibility between one EMI and 6-8 EMIs is they have to participate until the customer moves beyond that after he has paid six EMIs regularly then only he moves to the collection executive responsibility. So they have a dual responsibility which is why the business volumes are kept a little low. It is between 15 and 20 vehicle per month, per executive. So we have about 2,300-2,500 people apart from our direct marketing initiative people and which is why that 50,000-60,000 vehicles is what we normally average, with the current volume it is about 45,000-48,000 vehicles is what we are averaging.

Sachin Bhardwaj: Secondly you mentioned about also pinning the responsibility for collections so one obviously the fact that you have mentioned that till six EMIs they are responsible for collections but later on if there is any delinquency in the loans originated by them, do they have some repercussions?

Ramesh Iyer: Ultimately the repercussion is in their performance pay, because they are also based on branch pay profitability, performance pay, one is direct responsibility performance pay, second is branch profitability performance pay. So when there is future delinquency one is the collection executive gets negative for no collection and the profit gets impacted, therefore the business and branch manager also gets impacted.

Moderator: Thank you. Ladies and gentlemen, due to time constraints that was the last question. I would now like to hand over the floor back to Mr. Aadesh Mehta for his closing remarks. Over to you Sir!

Aadesh Mehta: On behalf of Ambit Capital, I would like to thank the management and the participants for joining us on the call today. Thank you all and have a good day.

Moderator: Thank you everybody, on behalf of Ambit Capital Private Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.