"Mahindra Finance Q1 FY16 Earnings Conference Call"

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MANAGEMENT: **MR. RAMESH IYER – MANAGING DIRECTOR, MAHINDRA FINANCE**
MR. V. RAVI – EXECUTIVE DIRECTOR & CFO, MAHINDRA FINANCE
MR. DINESH PRAJAPATI – VICE PRESIDENT, TREASURY & CORPORATE AFFAIRS, MAHINDRA FINANCE
MR. RAKESH BILDANI – SENIOR MANAGER, TREASURY, MAHINDRA FINANCE

MODERATOR: **MR. KARAN UBEROI – VICE PRESIDENT, RESEARCH - INDIAN BANKS AND FINANCIALS , JM FINANCIAL INSTITUTIONAL SECURITIES LIMITED**

Moderator: Ladies and gentlemen good day and welcome to the Mahindra Finance Q1 FY16 Earnings Conference Call hosted by JM Financials Institutional Securities Limited. As a reminder all participant 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, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Karan Uberoi of JM Financials. Thank you and over to you sir.

Karan Uberoi: Thank you, good morning everybody and welcome to Mahindra and Mahindra Finance's Earnings Call to discuss the first quarter FY16 Results. To discuss the results we have on the call Mr. Ramesh Iyer who is the Managing Director, Mr. Ravi who is the CFO, Mr. Dinesh Prajapati who is the Vice President – Treasury and Corporate Affairs and Mr. RakeshBildani who isSenior Manager, Treasury. May I request Mr. Iyer take us through the financial highlights subsequent to which we can open the floor for Q&A session, over to you sir.

Ramesh Iyer: Karan one quick input which is, Ravi has been elevated to the Board and he is now the Executive Director and CFO of the company and this was done on the Board Meeting that we had on Friday.

Karan Uberoi: Congratulations Mr. Ravi.

Ramesh Iyer: So we kind of get into the results and then of course the overview but instead of me going through really number by number I am sure everyone must have already seen it, read it and understood and therefore let me get into what is causing whatever that you are seeing as number.

As we have been talking about it for some time now and we would continue to believe that things on the ground is yet to pick up and things have to yet change and its reflected from the industry that we support whether it is the auto industry whether it is the tractor industry or for that matter if you go geographically whether it is the rural market. So one has to continue to look at what we do in light of what is happening out there and will have continued with our focus of not wanting at this stage to really get behind and drive business but rather focus on building a little more preparedness for future but more importantly ensure that we from here control whatever that we could really control. But we would also like to state here that it is not a stage where we are able to influence a change at that market because the fundamental cash flows of the customer continue to remain stressed.

If you look at the customer segment that we work with are almost all of them are earn and pay customer and therefore whenever there is a pressure on their cash flow that has to for sure and necessarily reflect on our activities and our performance. If some of you will recall that we have been saying how the cash flows are getting stretched and their multiple impact and they are one, their overall cash flow size has come down from their activity level and two, the frequency of their ability to collect and pay as a customer has also come down. Like if most of them who are contractors operating at the local level are not able to really service the loan because their own bills are outstanding, the work that they have completed is kind of yet to produce results for them and we are able to see the pressure of that on our customer front and when I say the overall activity, it also somewhat from it was, let us say one year back or one and half year back situation, the activity seems to have substantially come down and the activity on various fronts have come down. People who are attached to infra projects they are not able to see many major contract segments are still operating. When it comes to the farm you know we had this untimely rains in between that has further impacted the customers substantially and each of this is a little at bit which harms a company like us which are deep into the rural market.

It is also important to understand by geography and it is unfortunate that we're not seeing any major positive activity big-time in any state as of today. While every state is preparing for that little future to come about but if we speak about what is happening particularly at this stage we are not able to kind of say that things are changing big-time whether it is from the coal block activity, whether from the mining activity or for that matter from the road infra activity. But we are seeing some signs of preparedness at different levels when we talk to contractors, when we talk to major operators they do seem to be getting ready for it but are the ordering process already commenced, are the tenders out, are the people been given contracts to start execution? I think the answer is no. But also it is interesting when we look at it and I am more speaking from a collection perspective is that while the overall weakness is seen in the system in terms of people not able to earn enough to pay but we do see that intentionally that these customers are servicing the loans even from whatever that they are collecting or they are executing. So if you look at the movement of contracts, if you look at how much has the customer been able to pay? We do see that there is a movement in substantial portion of the customer account but once they have built a large overdue they are not able to earn enough to be able to pay and come out of that situation very quickly. So that is something that we are continuously monitoring very closely. These are all collateral based business and therefore what we also keep measuring almost all time is what is the level of outstanding and what is the value of the underlying collateral and therefore is it sensible to wait for things to change or we need to act faster and the sense that we get is that definitely the collateral is in a position to protect the principal outstanding while it may not be sensible at this stage to repossess the vehicle and try and transact on them because the second-hand prices are also going to remain subdued given the activities levels around there.

The monsoon which started off well in June did not show great promise as we moved into July but it has revived again and the news that we get from most of the states is the monsoon is likely to be average plus and that would be a good start point from a sentimental point of view while not every customer is farm dependent for their cash flow but ultimately the market that we service sentimentally definitely does depend on this. But the volumes out there are still low whether it is auto, tractors anyone of that and while we are protecting our market share we are not able to see a big time growth happening out of that.

So when you look at this quarter results in particular, after a great fourth quarter that we had and as I said with the stretched cash flow the customers are not able to service loans on a monthly basis so someone who has paid in March and will not surely be able to pay in the month of April may would have paid in June so it has got some kind of an internal regulatory correction that the customers have gone through in terms of their ability to pay and even if they are servicing it on a monthly basis sometimes they are not able to service the full loan, but there is a moment as I mentioned earlier.

From the volume perspective the discounts continue, the volumes are low and therefore you will see the impact of that happening to our growth story whether it comes to disbursement, whether it comes to asset growth or even for that matter more importantly when it comes to the income growth. In a business like ours every year you will have a set of contract maturing and a new set of contract coming in. But if the volume of contracts going out and coming in even though they are the same but if this is due to product mix change sometimes the income could be very different from these two set of contracts. And one of the impact of that is what one would see in this quarterly results of ours, that certain contracts which have matured and gone out had a different level of income that was being booked on those contracts when they were live and as against that when the new contracts have come in they are at a different level of income. So therefore the net income growth that should have happened has not substantially happened and that has happened to us almostto the first time over a period of time where there is a pressure that have seen from the income growth perspective coming in because of the lack of volumes that one is seeing in the market, but I personally think that that is temporary nature as our market starts correcting and the volumes starts coming in, this will also start getting corrected.

Strategically we continue to believe that there is room for growth as time opens up, we have added branches, we have added people, we have invested in training people, we have also invested in technology platforms as required and therefore we are ready to wait as and when the opportunity opens up we will be able to capitalize but we do not want to kind of move faster to say having built all this infrastructure should we now chase growth? The answer is no. I think the market is still not ready, we have the patience to wait for, it does not add substantial cost to us, we are utilizing this infrastructure that we have built more on the recovery front and therefore we believe that it is just a matter of time when it opens up that will be able to capitalize on it.

We very strongly think that what we miss in one quarter to some extent would get corrected in the following quarter like for example if you take Maharashtra as a story, even though sugarcane was good but the sugarcane prices were inadequate and the sugar mills did not pick up sugarcane, the cash flows does get impacted. Now, I would call this transactional, this is not fundamental. This would get corrected as and when the sugarcane gets picked up the cash flow will come in. The fundamentals I would say are there are equipment ready to be deployed but contracts have not been issued and therefore the underutilization of the asset happening.

In the improving states while we always talk about Southern states to be the most difficult ones and they continue to remain, but states like Andhra, Telangana, to some extent Tamil Nadu have started showing signs of improvement but they are still in the zone of attention that we need to have, they are still in the high zone. But the new States which have come in during this last 3-4 months which have been more impacted by the cash crop getting spoiled due to the untimely rains are states like Maharashtra and Madhya Pradesh. So when we have presence in this market and they go through this temporary phases we need to live this life with them and that we are not overly worried about, is things cracking, my answer would be while they are difficult at this stage we are not able to influence a decision on the customer but we are able to meet customer, we are able to inspect the asset and we are able to keep the cash flows going and therefore when things open up we would possibly be one of the strongest beneficiary of the change that can happen. But surely we continue with our strong practice of not to reschedule even a single contract even though there is a pressure from the customer end to ask for it. We continue to remain focused on our policy of not to increase LTVs to chase growth, we are still in the medium LTV zone 70-75% to the asset. We are not changing our terms in terms of dropping the rates etc. What you see as little margin pressure for us is not arising out of drop in interest rates of lending but it is also arising out of the product mix change. So if you less of tractor business or less of let’s say a UV business and that's replaced with car business and the car yields are always lower than the tractor yields. So you will always see on the net interest margin levels these kinds of pressures coming in due to product mix, but that's a new normal that we are getting adjusted to. Once the industry opens up then you will see many of these getting corrected. We have seen similar situations in the past where you see built up of NPA happening but the credit losses are not galloping the same way. The credit losses still remain in the zone of below 2% kind of a situation, the collateral do have its respective values. Decision to reposes or not is more internally driven policy and therefore we are willing to live this life, have patience and then once things open up I think we are all ready to capitalize on the emerging new opportunity.

Our focus will of course will remain that people will be driven to focus more on collections, to maintain asset quality, we have formed internal teams and task forces which will look at different buckets, different products, different geography but those are operational decisions but in as far as strategic decision and fundamentals are concerned I think we are continuing to believe to go more deeper, capitalize on our existing customer relationship, tie up with various OEMs who are looking at rural as the geography for growth, remain focused on our internal processes and policy and not tamper with them at this stage for growth, but keep our eye more focused on collections and as and how the opportunity emerges we will ensure that we do not miss out on this emerging opportunity.

So net net I would think while this has been one of the most difficult quarters that we have gone through in terms of high effort low result situation but that is most driven by what is fundamentally happening at the marketplace. It is not an outcome of is the business model needing to be revisited. No, the business model is still the same,its same people with the same passion driven for the same segment of customer financing the same type of products and the geography that we are used to for the last 20 years, but that would not mean that we don't need to keep revisiting them and keep adjusting them to the changing environment, but it only means that the fundamentals of the business have not undergone any major change while temporarily there are pressures out in the market.

So I would therefore summarily say that while we are going through difficult times but it is not as though it is in our control, it is not as though we are not aware of what it is and it is something that which we can't influence and bring about quick change but surely these are opportunity.

That two subsidiaries have done extremely well from where they were but one must look at it from a small base that the rural housing had and therefore their growth is definitely from that base it is a much better base. They have been able to retain their margins but they do also have the same the pressure of collections because they are also in the same geography to almost the same profile of the customers that we operate in. But except that the collateral are very different and to the customers priority to service these loans could sometime be even more urgent than they service the vehicle loans. But this business has had tremendous promise of growth. We believe that these businesses will scale heights that we have targeted always and we do believe that in terms of their processes, in terms of their preparedness, in terms of their reach etc. they're all geared to capitalize on this growth and same is the penetration story as far as the insurance is concerned, insurance business or that distribution business of ours will grow faster than the growth rate of Mahindra Finance because they are increasing their penetration in terms of the volume of customers. So even though that we are not growing in terms of high volume in Mahindra Finance but since they have a lower penetration as they keep increasing penetration their volumes will keep going. So they also kind of maintaining a decent level of margins and profitability and as I told you their penetration is what their focus is and they would continue to maintain this growth and I think collectively we are waiting for some signals of improvement from the market. While there are some minor indications available but yet there are no major visible factors which we can say that things have started changing big time. But there are definite minor indicators. We are strategically looking at state-by-state and will prepare ourselves much better on the state basis of whichever state shows promising opportunity.

So I thought that’s from our side, definitely these are challenging times but I think these are also times where it's a test of a well-established business model with strong fundamentals and process practices and the team which has run it for longand therefore it is also a test for all of us to see how do we come out of these situations. The team’s confidence is that it is not very difficult to handle but one needs tremendous patience to live this life and then when and as things changes we will be able to capitalize and gain the benefit out of it.

So that is it from our side in terms of the initial input is concerned. If it is sensible will start getting into the Q&A where Dinesh, Rakesh, Ravi each one kind of can give you if there are any data point explanations that may be required. So this is where we are, thank you so much.

Moderator: Ladies and gentlemen, we will now being the question and answer session. The first question is from Mahrukh Adajania from IDFC. Please go ahead.

Mahrukh Adajania: You said that there is a lot of news flow on activity picking up but it is not translated into order flow, when do you see that picking up and what is your outlook on disbursement growth for the next few quarters?

Management: One is what is the outlook on disbursement growth for the next few quarters, other one is when a ground level pickup is expected?

Ramesh Iyer: At least the geography that we represent it's extremely important that we end the monsoon season more positive. I think that's the first direction of sentiment moving positive but in as far as the overall improvement is concerned it is less farm dependent, it is more infra dependent for us to really say things have started changing which means one has to start seeing more and more projects being announced whether it is coal excavation, whether it is mining, whether it is a road projects, telecom whatever they could be and we too believe that not before end of the third quarter and that therefore beginning of the fourth quarter is what we all can think that things have now started working in some particular format, but if the festival seasons have to be good at least the vehicle sales have to start picking up and tractor sales will have to start picking up, I think the sentiments of monsoon is extremely important. In as far as our own disbursement growth is concerned as I told you we are maintaining market share and we are not in a hurry to gain market share but I think the first time that one would start seeing some improvement to disbursement will be the discounts will have to discontinue. I still think that the dealership inventory levels are not low fordiscounts to vanish or the price increase to come in. So you don't see any OEM announcing price increase. So I think no sooner you see discounts vanish and price increases starts coming in at least we will see value growth happening to us automatically even though volume growth may not have kicked in even then. For the volume growth to happen in the inventory levels will have to go down which again will link to what are the overall sentiments and where things are going. So not before start of festival season and it could stretch one quarter after that, therefore we may want to look at fourth quarter from where we can start seeing as the things started moving upward, until then I think it is still going to be little flattish and wait and watch.

Mahrukh Adajania: In terms of the delinquency outlook given that things are not really changed and probably deteriorated at the margin there is really no reason to believe that that also would also improve in the next 2 to 3 quarters because the macros kind of deteriorated at the margin though the news flow is positive.

Ramesh Iyer: So let me state this again, even if we see some correction in this quarter one should not start looking that it is the fundamental change. You know what we must have missed in the previous quarter; some of the customers may come back and pay during this quarter etc. The overall correction announcement will happen, first of all the volumes will have to start picking up, that is the time when one can start knowing that the cash flows there is improving otherwise it is managed from the available business whatever cash flows they can and the available cash flow does not allow customer to pay on a month-to-month basis. So what gets missed in the previous quarter possibly would get some corrections during this quarter and that should not be misunderstood to be that the fundamentals starts to changing. So for us in a business like ours, business growth and collection improvement will almost happen at the same time, they are not going to be on lag or one behind the other with a wide gap.

Mahrukh Adajania: One last question on operating expenses, any guidance you could give on that? Are you now more or less done with the branch expansion in terms of better collection points or in terms of employee additions to have better collection points and better proximity to clients?

Ramesh Iyer: We do not see a big swing on that front. We are not going to add some 3000 employees or not going to add some 1000 odd branches. Those programs will continue the way it has been following year after year pattern and again as a percentage it may look to be a little more or little less on the basis of the asset growth or otherwise, but more or less our plan is, you know every year we add about 1000-1500 people and we don't see that number to be very different nor do we see that the branch opening will it be around 150 branches, possibly the answer is yes but it is not going to be 500 branches during the year. So we do not see any big swing so far as the operating cost is concerned both as an increase or as a reduction.

Moderator: The next question is from Amit Premchandani of UTI Mutual Fund. Please go ahead.

Amit Premchandani: Last quarter results you have mentioned that the number of contracts which are delinquent have not gone up and roughly if I recollect there were 60,000 contracts which were under NPL, around 40,000 of them were actually paying. How has this moved from last year's number?

Ramesh Iyer: So if you recall in the same call we also said that normally for us the third and fourth quarter are the best quarters for the quarter and therefore you would see that kind of a drop happening and then in the first quarter it does pick up, so we have added about 25,000 to 30,000 contracts to this but we still have 50-52% of the contract where there is a movement. So 56,000 or 60,000 whatever that number was would have moved up to the about 99,000+ number and I talk about this without the repossessed vehicle in stock which will be another 6000-7000 vehicles. So it is about is 98000- 99,000 contracts is what will be in the NPA range but we have seen that at least 52-53% of them have registered movement.

Amit Premchandani: What was the number last year same quarter for this?

Ramesh Iyer: In terms of NPA?

Amit Premchandani: In terms of number of contracts.

Ramesh Iyer: I think it will be about 75,000-77,000 or so. So it is about 20,000 odd we would have added whereas we have done half a million of customers during that one-year period. See what you need to keep in mind also is that even the new business that you do will have the same pattern so when you are 75,000 on a live contracts of xnumbers and then you add another 3-4 lakhs new case during the year, even if you assume 50% of them crossed six months period and therefore become eligible for some growth and therefore it is 15000-20,000 contracts that way.

Amit Premchandani: In terms of collection efficiency last year the March month was 109% while…

Ramesh Iyer: March it will come per quarter of… 90% range and I think last year first quarter and this year first quarter are exactly the same.

Amit Premchandani: So there is no change in that and July would be better than the first quarter/

Ramesh Iyer: Too much to kind of make that comment but as I told you even if July is better let us assume it is going to be because somebody did not pay in June, it is not because something has got corrected on its own.

Amit Premchandani: Last quarter you had mentioned that you were taking some decision terms of not lending for three months in one market if you are seeing any pressure, have you kind of taken a decision on that which states will not lend to?

Ramesh Iyer: I do not know, I don't think we have said that specific what have said is from any particular location we see that the business opportunities are leading to delinquency or the market conditions are not proper whether it is one month, two months, three months is not the criteria we will take a conscious decision through that branch not to lend. So there will be in 1200 branches there will be clearly some locations and branches or even for that matter some products in which we will not lend for example we moved out of commercial vehicle and a continued to remain away from it big time.

Moderator: Our next question is from Gaurav Agarwal of E&R Advisors. Please go ahead.

Gaurav Agarwal: One of the prime reasons why our PAT was down is because of higher provisions which was high on a higher base already, on an average asset it has moved up from 1.6-1.8% in 2012 to around 3.6% currently. Are we having any lower expectations on recovery and that is why this provision as a percentage of average assets is increasing? Are we having any lower expectation and that is why our provision cost as a percentage of average assets is increasing?

Ramesh Iyer: See its a truth of the market, it is not what we expect or otherwise. We are working in a segment which is earn and pay segment and as I repeatedly keep saying the reflection of what you see in the demand side of vehicle and tractor will automatically reflect also in the collection side which means that the local cash flows that the customer is currently going through is inadequate to service the loan on a continuous basis. The cost of operations for them have also gone up whereas the freight rates or per passenger fare has not substantial gone up the overall volume has come down and that is impacting us but they are servicing the loan, not able to service the loan completely once they build up an overdue and they are not able to pay off completely. So it would wait for some fundamental corrections to happen where their volumes starts picking up, which is why we track the service ability of the customer whether he's at least available to be met, is he paying, is he paying the interest, is he keeping the loan serviced then the answer is yes, but we have taken a view not to reschedule. Typically these are contracts which qualifies for a re-schedulement and give them more extra time but we do not want to do that. We allow the customer to pay as he earns rather than rescheduling it and making it look alright internally and currently they are undergoing that pressure but it is important to understand that x percentage of customers is not able to service the whole loan when they are built over dues. It is not across the board all customers no vehicles in no geography is paying. The percentages to some extent are an effect of the denominator, so if we were to grow the book at 20-25% the same 8% may look like a 5% thing. That is why we track the number of customers who are not able to service rather than the percentage.

Amit Premchandani: Is there any change in buckets that number of customers in the safer bucket has moved to a bit of unsafe bucket?

Ramesh Iyer: Yesit would, like for example higher buckets if somebody is in a 11 month zone even though RBI wants us to provide only on the 18thmonth, internally we provide no sooner they reach12 months we make 50% provision, this is why you see the coverage ratio has gone up from last June which was 51-50% odd now close to 57%, so in the first quarter itself if we have moved up to 57 and if we continue to keep pace like this then last March we were I think 61% or odd and possibly we will cross that percentage as well.

Amit Premchandani: What was the interest reversal amount in this quarter in Q1?

Ramesh Iyer: It is about 100 crores.

Amit Premchandani: Are there any reduction in yields, you said in the call that there were not any reductions but because the base rate has come down?

Ramesh Iyer: Let me tell you, yield reduction product by product it will not be a major reduction but product mix is causing that.

Amit Premchandani: So there have been no yield cuts.

Ramesh Iyer: Tractor sales are 20% low, our tractor volumes are low, and tractor is the high yield item. On our own have we announced some major interest drop for customer, the answer is no.

Moderator: Our next question is from Piyush Chaddha from Ocean Dial. Please go ahead

Piyush Chaddha: In terms of delinquencies and the charge, our credit cost at around about 3.6-3.7% of assets are pretty close to the last down cycle in 2008-2009. Do you see the situation on the ground as severe as it was during that time that these credit costs of matching that period? That is number one. And second in terms of the delinquencies going forward given that we have a 150 day recognition norms the impact of unseasonal rains in February and the last 4-5 months event would it yet to be reflected in the NPA profile in that case could we expect further accretion to the NPA?

Ramesh Iyer: As far as five months is concerned we don't see that impacting us big time, because we were kind of almost prepared for it at 5.1 day and then we have to just to make a one-day adjustment kind of thing, but what we plan to do going forward clearly is to start preparing for 120 day.

Piyush Chaddha: Is that likely to increase the NPA level?

Ramesh Iyer: It will because when you move from 150 day to 120 day one month additional contracts come into this but that again is only preparedness from a regulatory needs for future that will not change the overall credit loss but we would like to prepare ourselves going forward to be ready for 120 days as much as we can.

Piyush Chaddha: In terms of the first question your credit losses are very similar to what they were in the 2008-2009 period. Is the situation on the ground also somewhat similar to that period?

Ramesh Iyer: The point is that the reasons what is causing this could be different while the effects are same. The reason what is causing this now is lack of work at the ground level and if the ground level work starts the corrections this time could be much faster and it could be much aggressive.

Moderator: Our next question is from the line of Karthik Chellapa from Buena Vista Fund Management. Please go ahead.

Karthik Chellapa: Firstly you mentioned at the outset that as far as repossession is concerned you are not repossessing at this point of time but to the collateral value is sufficient to cover the losses, can you give us some sense on how much cushion do we have, in the sense that how much more does it need to drop before it starts to impact our actual credit loss amount? That is my first question. My second question is if we look at our Others segment which we classify under Pre-owned vehicles and Others that also includes I believe SME financing to M&M vendors, etc., that has grown at about 28-29% odd this quarter. Can you give some sense of what is driving this demand and how was the asset quality behaving on this particular segment?

Ramesh Iyer: On the first question I may not have product by product statistics, etc., but one thing on a very large macro picture basis I can tell you is that if we have 2300 crores or whatever of NPA, gross NPA and if 57% we have covered the other 43% means another 1000 crores to cover and we have close to 100,000 customers and therefore if you value the assets underlying that it will be much more than that. I don't know specific to tractor how much will it be or how much will it be vehicles, etc., that is a more detailing of each customer each product but clearly let's say all customers surrender their asset today and we need to sell all of them, I think that on a principal basis we would be covered, yes. As a matter of accounting if interest is booked first principal outstanding is little more than the total to that extent, that is how you book loss but I think on a large picture basis the customer underlying asset for the value unprovided for as of today it is adequate to protect that.

V. Ravi: As far as the Others which is includingthe SME portfolio so roughly around the 500 crore is SME portfolio and there is additional 130 crore which is on working capital line to the dealer, so that extent there is a SME portfolio.

Karthik Chellapa: Can we assume that this growth that this particular segment has seen at least in the last two quarters is more to some extent financial accommodation to some of the dealers and your vendor partners given the financial stress that they are in?

Ramesh Iyer: Let me clarify to you we are not picking up their liability as a replacement. If somebody is owing money to a bank let us say 5 crores is he coming and taking from us and say please give me 5 crores I have to discharge the liability, the answer is no. It is purely their requirement and the growth is from a base. So it is still a very small portion of our total, so far as pre-owned vehicle is concerned whenever the new vehicle does not do well it is always the second-hand vehicle which will do well because people have need for vehicle but they are not able to invest such a large amount from their return perspective.

Karthik Chellapa: If you look at your parent M&M have a very aggressive pipeline of products this year they almost are talking about 9 to 10 launches across segments UVs, CVs, etc., given our focus on collections and given our view of the macro are we in a position to participate in this opportunity initially as and when they launch?

Ramesh Iyer: You look at my initial comment we are not losing market share while we are not chasing. If they launch one product and if it is sold in that geography they sell 100 vehicles I will continue to do 30 of them. So we have not moved away from financing of vehicle while we are not in a hurry to chase growth.

Moderator: Our next question is from the line of Lakshmi Narayanan of Catamaran Capital. Please go ahead.

Lakshmi Narayanan: I have a question related to the pre-owned and others which is almost 15% of your AUM, you mentioned that it comprises SME and working capital to dealers. When you say pre-owned what are the things it actually comprise, is this the commercial vehicles or is it cars what is the configuration like?

Ramesh Iyer: Largely it is a mix of UV, cars, and tractors, we are not into big-time heavy commercial vehicle pre-owned.

Lakshmi Narayanan: In terms of cars where we are 23% of our AUM is in cars, how much of these cars are actually used for? Is it for business purposes cars or is it for individual driving what is the mix, has it changed over the period of time?

Ramesh Iyer: It has not changed but in our case typically what happens is almost 90% of them will have multiple use even though they may be registered personally. Like for example in rural India typically what happens is even though a local teacher or a doctor buys a vehicle so it registered gets personal but it is used during wedding season, tourism on a hired basis.

Lakshmi Narayanan: Coming to tractor segment which is around 18% what is the market share with respect to the Mahindra and Swaraj brand?

Ramesh Iyer: There are about 26% or 27% as far as Swaraj is concerned and we are about 29% to 30% as far as Mahindra is concerned.

Lakshmi Narayanan: I see that you had mentioned it is in the single digit growth for the next 4-5 years and how has it been panning out at least till July for you in terms of tractor sales and hence the disbursements?

Ramesh Iyer: Single digit growth for us you are saying, right?

Lakshmi Narayanan: There is a projection which is mentioned in terms of the next 4-5 years what has been the projection for number of units of tractor getting sold in your presentation?

Ramesh Iyer: Tractor Sales?

Lakshmi Narayanan: I just wanted to check with you on your outlook because of the unseasonal rains, etc., and also the commentary on tractors at least till June has been quite bad so are you seeing some green shoots or what is your outlook for tractor industry?

Ramesh Iyer: Tractors at least my understanding is not pure farm product, it also has haulage application, so even though the monsoon may be good unless the infra project commences, replacement market pickup happens, commercial tractor purchases happen one would go with still the projections and the commentary that the growth rate is likely to be subdued. I think we'll have to live with that volume, I cannot influence the volume, if somebody sells 100 tractors I will do 30 of that but I have no means to make that 100 become 120.

Lakshmi Narayanan: Last thing on regional focus I believe that our regions where we are strong are Maharashtra, Madhya Pradesh, Uttar Pradesh and Bihar. And you also mentioned stress in particular states like Maharashtra when you talked about. Are we strategically looking at changing our state mix or trying to look at some other products in some other states if so what has been our change?

Ramesh Iyer: See, as far as our business is concerned we are pretty widespread across the country. The percentage of the product, the volume mix is on account of the size of the state, so if UP looks higher it's because UP by state is so large and by population it's so large the vehicle sales are higher there. So I don't think we are in any state less in terms of our penetration is concerned. The states where we see the stress currently other southern states, added to that is Maharashtra and West Bengal and MP. And Maharashtra and MP are phenomena of the untimely rains that came in at the beginning of this quarter and a continued pressure on monsoon, so I don't think we are going to kind of temporarily look at some new products and kind of a situation. I think we are pretty stable in terms of every state is concerned. We are increasing our reach and penetration in every state adding people in these locations to be ready, use them for recovery and once the business recommences we will also engage ourselves into business growth.

Lakshmi Narayanan: And you mentioned South and West Bengal are also in stress broadly. Can you elaborate more on those two?

Ramesh Iyer: I don't know what exactly the input you are looking for but South has been not in good shape for now more than 15 months and we have been talking about it every quarter on how Tamil Nadu went through a most difficult time. Some signs of improvement with power situation getting improved, etc., so some improvement is seen in that state. So far as Andhra and Telangana is concerned of the southern states they are the fastest registering growth as we see in terms of improvement. Karnataka, mining is one major issue still and therefore we don't see major activity. These are the situations. And as far as West Bengal is concerned, same problem, there are no major economic activities and then you had this one scam that went through there in terms of the Saradha scam or whatever and that puts everything to a backburner for sometime in terms of activity. East is not something that has been a great promising states for us anytime in any case but except that the pressures are little more than before.

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

Deepak Poddar: My first question is that you mentioned that you will start preparing for 120 days, so exactly when we will see the migration happening, like next one quarter, two quarters or from FY17 itself?

Ramesh Iyer: Too premature to comment but I think from this quarter itself we will try and see if it is possible. But not said 120. We will move towards 120, maybe we will move 10 days and then another 10 days and then another 10 days.

Deepak Poddar: Like 8% that we reported this quarter, gross NPA, how does it look like if we have to report on 3 months basis or a 4 months basis?

Ramesh Iyer: I don't know, I don't have a ready number. I would assume 2% it will look worst, but one should also assume the denominator effect. So if the business grows at 25%, this 8 would have looked like 6 and therefore that would look like 7 or 8.

Deepak Poddar: So basically by FY18 if we have to completely migrate to 3 months, so what would be your revised gross NPA target that you would be happy with?

Ramesh Iyer: Happiness would be 5% but what reality would be could be 10-12%. But I think it's important to understand that whether it is 8%, 6% or 10% does not change the credit loss situation.

Deepak Poddar: Credit loss situation in the sense because we will have to provide for that incremental loan, right?

Ramesh Iyer: That’s in the P&L, but if we were to repossess, sell, we won’t lose money. The book will have it provided early and then as the contract comes to an end we would have recovered that money, so it will be a timing situation but not really the money lost situation.

Deepak Poddar: My final question would be, like this year we are not targeting growth but any kind of growth outlook that you see what long term that this is the sustainable growth that we might look at next 2-3 years?

Ramesh Iyer: See I have said this in the past, our approach is we don't want to lose market. So the fundamental volumes will have to get corrected at the market place for us to register some growth. Importantly on a value front first we will have to discontinue, finance the new normal. Second is the price increase of the manufacturer; third is the volume impact of the manufacturer. There are no signs yet or there is no announcement yet from anywhere to say there is going to be a price increase or there is going to be a discount discontinuity or there is going to be volume increase witnessed. So even now people are talking very subdued number. People are saying singledigit growth possible, tractors is yet flattish, so I think it's too premature for us to say something that no we want to register x percentage growth. Yes, we do see pre-owned vehicle is one demand area where new vehicles don't do too well there is a demand for pre-owned vehicle and we are registering some growth there.

Deepak Poddar: So basically it's safe to assume that we might grow at industry rate assuming that you want maintain a market share, right?

Ramesh Iyer: We don’t see us taking an aggressive position and beating the market.

Moderator: Thank you. Our next question is from Deepen Shankar of Trust Line PMS. Please go ahead.

Deepen Shankar: Want to understand what are the key triggers you are looking at rural stress to get rid of?

Ramesh Iyer: I think first is monsoon to end favorable, so no sooner its declared that monsoon is favorable it ended up average we will see sentiments return. Second is I think we would see contractors getting engaged into more and more projects whether it is road, whether it is coal excavation whether its mining whatever they are. Means that we will first look for how well is the demand for new vehicles picking up at the dealerships. Is the walk-in improving, is the discounts discontinuing, is the demand for second-hand vehicle of our repossessed vehicle in terms of price starts moving up, is the customer coming to pay money on his own without us chasing for it, these are the very simple triggers which will say that the demand for vehicle at the ground level has gone up.

Moderator: Thank you. Our next question is from Piyush Chaddha of Ocean Dial. Please go ahead.

Piyush Chaddha: You just answered my question. I just wanted to know whether the move to 120 from 150 days past due would be staggered or in one shot.

Ramesh Iyer: Yes, so I said staggered, 10 days per quarter is what we will attempt to reach that level.

Moderator: Thank you. Our next question is from Manisha Porwal of Taurus Mutual Fund. Please go ahead.

Manisha Porwal: I just wanted a small clarification as to the rural stress is not allowing the organized to lend to them so aren't they resorting to the unorganized sector lending? Is there more of leverage which is getting generated and would this materially change the leverage position of the rural people?

Ramesh Iyer: Let's be clear, they never borrowed from moneylenders if you look at them as another sector for the purpose of asset acquisition. They are all hand loans. If somebody is resorting to a moneylender loan that is a temporary consumption loan that they go to. If I was in a big time personal look segment may be we would have been an alternative to a moneylender. We are in asset lending where customer brings in Rs. 1 lakh or Rs. 1.5 lakh as margin money, so the need for a new asset in terms of its opportunity to be deploying there is weak because these are all earn and pay assets. They have to earn from that asset to pay. So when they see the overall volume of work is less they don't want to acquire new asset, to the extent that they need this asset for any work therefore they are resorting to available vehicle on a hired basis because the supply side has been high in the past. So the basic answers to all growth will come from more work and much faster pace of work being announced.

Manisha Porwal: Secondly, is this stress on the rural side no actually translating on rural housing finance side, can you provide how the NPA has moved on the rural housing side?

Ramesh Iyer: They have also grown similar way in terms of NPA is concerned. So their growth is an outcome of low pace whereas their recovery is on outcome of the market behavior. It is just that they are not in every state of the country so therefore in some states their performance would be better and it's to an extent offset through the states where the performance is not as good. But their problems are no different. You look at Tamil Nadu, if you look at Karnataka or if you look at Maharashtra or MP for that matter their NPA also has substantially grown over March to base. Plus for them the first quarter and second quarter growth of NPA will be even higher than us because during this period no work activity also happens.

Manisha Porwal: So what could be the credit costs there?

Ramesh Iyer: They will be no different in terms of trend from these states are concerned. Sorry what was your follow-up question?

Manisha Porwal: Any indication on the credit costs and NPA levels there?

Ramesh Iyer: I think they are 90 days NPA though and therefore they will be in the zone of 8-9% gross NPA, they will not be less than that.

Moderator: Thank you. Our next question is from Pankaj Tibrewal of Kotak Mutual Fund. Please go ahead.

Pankaj Tibrewal: Two questions, one on the P&L interest you account it on an accrual basis or a cash basis?

Ramesh Iyer: Cash basis.

Pankaj Tibrewal: How much was the cash collection?

Ramesh Iyer: The number is about 38-40 crores must be this quarter. Rakesh will check up I will come back to you. But it will be around that range. It is normal like every quarter. It is nothing something very high or abnormal collection. Last year would have been 35 crores maybe it is 37 crores now or something like that.

Rakesh Bildani: It is 48 crores collection from **P&L51.20**interest, this vis-à-vis last year, we will tell you least year's also.

Ramesh Iyer: It will be around the 30-32 crores, it will not be very high. It's just that number of customers are high in delinquent so therefore the amount will be high.

Pankaj Tibrewal: Another question was when you look at your employee cost last year your profits have remained almost stagnant for almost 3 years but the employee cost has gone up substantially even in last year about by 50%. What's the outlook you are carrying on this?

Ramesh Iyer: No, that is reconstitution. We had an outsource company which was coming under legal expense or something like that, that moved up.

Pankaj Tibrewal: Can you give some more clarification?

Rakesh Bildani: Last year's P&L interest collection is 42 crores.

Ramesh Iyer: That's what I said, I will be almost same, it will not be very different. This is a normal practice or ours.

Pankaj Tibrewal: On the employee you were saying something?

Ramesh Iyer: On the employee, we had an outsource company where the collection executives and the business executives at the low end were all in that company and it was being classified under legal and professional fees, if I am not wrong. That has been merged into Mahindra Finance and therefore the employee cost seems to be gone up 50%. In terms of absolute number of people we added year-on-year it's about 1000 odd people, it will only marginal, a fractional point only it will move up the cost.

Pankaj Tibrewal: So this cost which was there whatever you said, for this year it should not be abnormal?

Ramesh Iyer: Yes, it should not be.

Pankaj Tibrewal: So the OPEX expense increase this year should be much more muted compared to what it was last year?

Ramesh Iyer: Look at 2-3 years the range will be between 2.9% to 3.2% kind of a situation. It's actually the affect due to asset decline. On an absolute basis we have not added substantial number of people or any new activity to push the cost up.

Pankaj Tibrewal: Because on absolute amount the employee expense was looking at….

Ramesh Iyer: That was what I told you category…professional into employee cost.

Moderator: Ladies and gentlemen, that was the last question. I now hand the floor back to Mr. Karan Oberoi for closing comments.

Karan Uberoi: On behalf of JM Financials I would like to thank Mr. Ramesh Iyer and the senior management team of MMFS and all the participants for joining us on the call today. Thank you and good bye.

Moderator: Thank you. Ladies and gentlemen on behalf of JM Financial Institutional Securities Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.