

“Mahindra & Mahindra Financial Services Limited
Q4 FY18 Results Conference Call”

April 25, 2018



MANAGEMENT:

MR. RAMESH IYER

VICE CHAIRMAN AND MANAGING DIRECTOR

MR. V. RAVI

**EXECUTIVE DIRECTOR AND
CHIEF FINANCIAL OFFICER**

MR. DINESH PRAJAPATI

**SENIOR VICE PRESIDENT,
TREASURY AND CORPORATE AFFAIRS**

MR. VISHAL AGARWAL

**DEPUTY GENERAL MANAGER,
TREASURY & INVESTOR RELATIONS**

MODERATOR:

MR. ABHISHEK MURARKA

IIFL CAPITAL LIMITED

Moderator: Ladies and Gentlemen, Good Day and Welcome to Mahindra & Mahindra Financial Services Limited Q4 FY '18 results conference call hosted by IIFL Capital Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference 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. Abhishek Murarka from IIFL Capital Limited. Thank you and over to you, Sir.

Abhishek Murarka: Thank you. Hello and Welcome everyone to the 4Q FY '18 earnings conference call for Mahindra Finance. The management team on the call consists of Mr. Ramesh Iyer – Vice Chairman and Managing Director; Mr. V. Ravi – Executive Director and CFO; Mr. Dinesh Prajapati – Senior Vice President (Treasury and Corporate Affairs); and Mr. Vishal Agarwal – Deputy General Manager (Treasury & Investor Relations).

We congratulate the Management on a great quarterly performance and thank them for allowing us to host the conference call. We request them to take us through the quarter's performance and then we shall open the call to Q&A. Thank you and over to you, Sir.

Ramesh Iyer: Good Evening everyone, extremely sorry that we had to reschedule this call by about half an hour or so because the Board got a little extended with all the other committee meetings etc. and therefore by the time we could reach the results to you, it was a little late. Thank you so much for joining us on this call and to start with, I will kind of like to take you back to what we have been saying couple of quarters over the last one year plus that the rural is showing uptick in terms of positive sentiments and we also said about how we have reorganized our organization to be able to capitalize on this changing environment and the benefit arising out of that as well as our continuing strategy to penetrate deeper and build strong relationship with multiproduct OEMs, and therefore, help us grow from there. Our focus of how we are kind of gone towards attacking the pre-owned vehicle segment and therefore maintain growth coming out of that, as well as also the commercial vehicle segment that we had vacated about three-four years back or little earlier than that when we saw the industries isn't doing well and we continue to kind of focus on that with a special vertical created, but not really going behind the fleet operators, but looking at load operators like five vehicles, 10 vehicle users etc., etc.

When we now speak to you about what we think and why and what has caused this results to be what it is, so I am not spending time on any particular number, but very clearly we do continue to believe that rural sentiments are positive at the back of the past monsoons which were favorable and then the Government focused on ensuring that the support prices are maintained to ensure the farmers are adequately compensated and also with the projections that have already started coming in on the monsoons likely to be good going forward, we are very clear that we would be one of the beneficiaries of all that is happening out in that market and we believe that whatever that we have done in terms of the verticalization which is creating product verticals and recovery verticals will get us the benefit very clearly and as we speak in this quarter itself, we

have added about 100 odd branch getting ready for tomorrow. We have also had our Dealer Council meeting very recently where it was reaffirmed to us the importance of Mahindra Finance when it comes to providing credit at the rural end. We do see in different pockets, banks going slow, we do see some of the NBFCs going slow and that is clearly an opportunity for us to therefore increase our volumes and market share.

As the year passed by, we have increased market share almost for every product that we participated in and that is the reconfirmation of an importance of a model like this. Our direct marketing initiative that we have been talking for quite some time now is now reached a situation of getting us business upward of 15% - 16%, which is a business self generated directly by us, which means going into the villages where we have our customers and through them generating more business in that village. We had one of the initiative that I had talked about in the past that is adding another 100,000 village to where we were, then we were around 3,00,000, 3,25,000 plus village and we said we want to add about 100,000 village in the next 12 to 18 months, I think we have already added another 30,000 - 40,000 villages to where we were earlier, so therefore the penetration strategy also is going well. We do not see any margin pressure in terms of our lending rates and we do recognize the fact that borrowing cost is inching up and we have taken a conscious decision also to increase our lending rates in select product in select geography while we may not want to do it across the board.

We have always said this in the past that even though our NPLs remain a little high, but there are sufficient movement in the NPL contracts and we have seen upward of 50% of the contract which always registers a movement while they continue to remain in NPA. As of now, I think, even the number of customers were in NPA are equal to what we had one year back after moving to 90 days, so I think it is a big, big shift from the base that we were into the base where we have reached now and I would also think out of this a lakh and 30,000-odd customers who are in NPA, at least 40% of them would be registering a clear movement, and therefore, going forward one would see. We are working on a target that we would like to reach at least 7% gross NPA levels with 60 odd percent coverage maintained, which would therefore be a definite much higher level of comfort level that we would be in and given the sentiments of the market, expected rainfall to be average plus, our deeper penetration, strong verticalisation and our employees present across all this together, we do believe that is clearly doable.

As far as the business and business growth is concerned, I think with our market share for the Mahindra products remaining at 30% to 35% kind of a level, in Maruti we continue to be about 8% - 10% market share, we have increased our market share in every other LMV segment. I think we have become a decent player in terms of our commercial vehicle segment is concerned. We have become a significant player when it comes to pre-owned vehicle. Our SME segment is registered substantial growth during this period, I think all this put together we were kind of earlier believing that a 15% growth is possible, I think we ourselves have recalibrated to say that going up to a 20 and a little higher in the second half of the year is also possible, so when we talk of 20 plus percent growth in the first half and then taking it to a level much above that in the second half given all the sentiments that we are talking is definitely doable and likewise normally our first and second quarter always pushes up our NPA substantially high, we do not

see that happen this year, it will still grow a little over what it was in 31st March, but it will still be in a very range bound and a curtailed situation, so we believe that after two year hard work in the rural market and having stay put there and continue to invest in people, technology, training, penetration, branch, etc., I think we are getting the benefit of it and we saw the benefit of it very clearly.

In this year, right from the first quarter, every quarter was an improvement over the previous quarter and I think we ended the year exactly the way we scripted that we will go that direction, so net net I would kind of want to leave you with the thought that rural sentiments have turned positive, our strategy continues to remain to be focusing rural. I think the state elections are a big booster when it comes to the rural cash flows and given that there will be four or five or six states which will go for state elections in the next two years starting this May from Karnataka, will all be a positive run up into the national election which will be a benefit and this will be true for all our businesses and not just Mahindra Finance, but when you talk of a rural housing business which also has registered phenomenal growth and correction of quality over what it was the previous quarter. The insurance business has registered growth in spite of a changing regulation, they have registered substantial growth, and therefore, I think they are very direct proxy to the changing sentiments in the rural market. We will not come back to the urban market which has been our approach always. We believe rural and semi-urban has substantial potential and we yet do not see competition which forces us to take a knee-jerk reaction. I think we continue to lead the market, we continue to design product and services, and therefore, we would remain a leader taking the market head on and going forward, and national presence is our advantage as I said, and penetration will be our strategy.

I was just reminded that in this quarter we have added 100 odd branch which is where I started, so we currently cover every state and we are deeply penetrated and we worked with all the OEMs and I think we work with close to about 5000 odd dealers across the country including their additional outlets, so put all this together, I think we changed our stance from being extra cautious to be kind of selectively optimist to now telling you that we think we come out of the deep trouble that we were in and we are able to forecast a trend, which we believe is achievable. So that is it from my side and we can open up for the questions. As I said, subsidiary I did cover where housing I said has registered phenomenal growth as well as corrections to their quality registering a 70% plus growth in their PAT. MIBL which is our insurance subsidiary even though they had this regulatory pressure and there is a one-time provision for a long-term incentive of about 20 odd crores and which is the reason you see their profit flat as otherwise even they have registered a 30% odd growth in their bottom line, so net-net I think both this businesses contribute substantially to our profit growth and we believe all our businesses have sufficient potential and pricing power to ensure growth as well as margin protection and therefore the profitability, so I now open it up to questions.

Moderator:

Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. The first question is from the line of Kunal Shah from Edelweiss Securities. Please go ahead.

Kunal Shah: Sir, firstly in terms of GNPL if we look at it, it has come from 15,000 to 11,500, so how much would have been actually say something which would have been sold off and written off in this particular quarter which is leading to this kind of a GNPL decline?

Ramesh Iyer: First and foremost is we took a very strong view this year that if there is so much cash flow in the market, repossession is not the answer, rather follow up and collect as well as go for settlement rather than repossessing and selling and which is why the stock levels have been curtailed to almost at the same level that we had at the March closing time number maybe 500 to 600 vehicle here or there, so it is on the lower side, so I do not think the GNPL has come down by repossession and disposal, it is purely by recovery and settlement and closure of accounts because as I said there is enough money as we see in the market. I think it is important to know in rural at any point of time they have enough money. If they see the going forward is positive, they pull out the money and spend. If they do not see the onset of the next season to be positive, they will hold back so we saw them holding back for two years, now we are seeing them spend this two years because the monsoon has already declared to be likely to be at least average plus and there are some local level infrastructure story whether from the local Municipality or from the local State Government, and therefore, there is a cash flow and that brings the positivity for them to be able to settling their liability and going forward.

Kunal Shah: It is largely recovery and not the write-off, but what would be the overall write-off amount in this particular quarter vis-a-vis last quarter and Q4?

Dinesh Prajapati: We have a bad debt policy of every half yearly contracts which are matured and six-month expired, we will transfer into bad debt, so in this half, that is, this quarter, 324 crores were transferred from NPL bucket to bad debt on account of matured and 100% provided item, and on account of disposal and foreclosure, there is 257 crores of loss write-off in the P&L for the quarter.

Ramesh Iyer: I think pure disposal, I do not have an exact number, but I would think it will be about 150 crores or so out of this 260 crores.

Kunal Shah: How would this number be in Q4 of last year?

Dinesh Prajapati: Last year, it was around 310 crores, last quarter F '17.

Kunal Shah: Overall in terms of growth anything particularly with respect to the region or locations or maybe it is all across if we look at it and across may be in terms of the product category, so definitely SME something which is inching up in terms of the proportion, so how we look at that particular segment in terms of the overall growth so that has been driving on a lower base, but what would be the outlook out there?

Ramesh Iyer: Overall growth as I said if we were to talk about 20% plus growth, I think clearly the Mahindra Auto, Mahindra Tractor since we have a very matured market share will grow in line with the volumes of the OEMs, so we would expect that those businesses for sure will grow for us

anywhere between 12% to 15% kind of a thing, if there number changes obviously our number will further change. As well as Maruti is concerned, it is almost the same story, while Maruti is talking of maybe 8% to 10% growth or 12% growth, we should get the benefit if market share maintains which is currently our market share, so the growth engine from a growth rate perspective, while these three products will offer substantial value in terms of overall disbursement, the growth rate if you really look at will come from pre-owned vehicle growth, it will come from commercial vehicle, construction equipment growth. It will come from non-Maruti car growth and it will come from the SME growth.

Kunal Shah: Largely in terms of the yields, so obviously this would be a relatively higher yielding segment ex of tractors, so there also in terms of overall yield we see an improvement because of this kind of mixed change?

Ramesh Iyer: Clearly, our average yield will always be in the vicinity of anywhere between 15%-17% kind of a story, and as we see the borrowing cost moving up, we will push also our lending rate, but cautiously not across all geography, all product but we would kind of price ourselves for the price increase that we have to incur for our borrowing and which will therefore lead to our net interest margins not getting impacted.

Kunal Shah: But ex of funding cost if we look at the yields because of the portfolio shift that might not be there, you are saying in terms of?

Ramesh Iyer: May not be big time because at the end of the day 8% to 10% or 12% of the portfolio is pre-owned vehicle, so to some extent they will improve but at the same time car is a low yield segment or commercial vehicle is a low yield segment, so therefore, the net yield will not show substantial change from 16%-17% range or 15%-17% range that we are talking of.

Kunal Shah: Largely, in pre-owned it will be CVs or it will be all the vehicles in the incremental growth?

Ramesh Iyer: Pre-owned will be other than CVs, we are talking about UV, tractors, cars.

Moderator: Thank you. The next question is from the line of Manish Ostwal from Nirmal Bang Securities Private Limited. Please go ahead.

Manish Ostwal: My question on the operating expenses growth this year, we have been investing very heavily in terms of distribution network expansion last couple of years and again this year the overall full-year basis employee cost growth is 25% whereas OPEX growth is 15%, so how do you see this operating expenses growth going ahead given the large investment already done in terms of distribution network?

Ramesh Iyer: First is on the employee growth, I think it is important to understand that the gratuity provision, we have kind of revalued it and then actuarial valuation has been done and there we have factored certain increment for the balance life of the employees etc., and that is brought in an additional provision of I think about 14 or 15 crores or something like that, so that is not a repetitive nature expense. Second is, we had certain incentive programs for employees that if you

were to cross certain milestones, they would be given an additional incentive and that has been provided, again that is performance based. If the performance is good, the incentive will come, so these two are not repetitive in nature item and they will also be I think almost in the range of 20 odd crores or little more, so if you take off these two then the employee cost growth also will be the same 13%-14% kind of a situation and the OPEX of 13%-14% again is, you are right, more branches getting opened, so they are variable in nature and they will actually start contributing to business in this year and that cost therefore will get restated.

Manish Ostwal: Second question in terms of our growth rate, last year we grew our AUM 18% and now given the commentary of Mahindra & Mahindra and Maruti and based on our distribution network, what kind of AUM growth we can foresee for FY '19?

Ramesh Iyer: We are saying first half will be upward of 20 plus percent, second half if the monsoon is good then it will inch towards 25% plus in terms of our disbursement and I think therefore the AUM growth range will be instead of 18% may go to 22% kind of situation.

Manish Ostwal: Secondly, Sir in terms of last year at the beginning of the year you said the credit cost for the full year will be closer to 2%, so this year what is our assessment now most of the pain is out, now we are moving from the down cycle to up cycle, so what is your assessment of credit cost for the next year?

Ramesh Iyer: Let me restate, even when the gross NPA was 4%-5%, our credit cost was always in the vicinity of around 2%. In the best that we had possibly was about 1% when the gross NPAs were 3% or below that. Given the market conditions, given the discounts that are available in new vehicle, all of this factor considered even though the gross NPA has now climbed down from 13-14 to 8 point something to go down further to 7 and odd, but I think the credit losses will hover around this 1.75% - 1.8% kind of a situation and they are fully priced.

Manish Ostwal: Lastly, do we have any legacy liability bonds which can re-price at lower rate and that will have some positive impact overall net interest income?

Dinesh Prajapati: We have always matching ALM position and so to some extent there could be a couple of year back some liability which could be slightly higher, but relatively now the yields have gone up in the bond market which means that pricing gap is not wide enough, so we do not expect a margin benefit on account of liability re-pricing.

Moderator: Thank you. The next question is from the line of Adarsh Parasrampurua from Nomura Securities. Please go ahead.

Adarsh Parasrampurua: Sir, just couple of questions, one is pre-owned vehicles seemed to be suggesting good growth out there, so can you just talk about which product segments these are, what are the yields there, economics out there, and what is the head start that you got in this segment?

Ramesh Iyer: I will not go into too much of detail in terms of the segment by segment, but then if you look at our pre-owned vehicles as I said it is a good growth story for us and we are not in commercial

vehicle pre-owned vehicle, we are in cars, we are in tractors, we are in UVs, we are in pickup kind of range vehicles etc., those are our products in which we are and I think the yield range is anywhere between 18% to 20% going up to 22% to 24% kind of a situation. Again, they are geography based and not across the country and they are also period based, some of them take this for one year, some for two years, and therefore those ranges are there. In the pre-owned vehicle, we also have a segment where our existing customers who finished their loan completely until they sell that vehicle after another three to six months, they also take some kind of a working capital support on those vehicles which are free vehicle after all loan discharged by them. They also come under the same yield range and they are much shorter period product, which is less than 12 months kind of product and that is their advantage.

Adarsh Parasrampuria: Sir, what is the working capital component of this pre-owned vehicle, is that a large part of the pre-owned vehicle?

Ramesh Iyer: No, it will not be more than 10%-12% of the total because they are our existing good customer after they finish the full loan. Before they sell that vehicle, they may want to buy another new vehicle, so normally what happen is they sell the old vehicle and generate margin money for new vehicle, since they delay selling of this old vehicle, they take a top up loan, put it as margin to buy a new vehicle and then when they sell off this vehicle, they adjust it.

Adarsh Parasrampuria: Sir, you kind of given penetration levels of financing in different products in your presentation you know in the earlier, can you talk about what are these in rural areas in pre-owned vehicles and is that the larger driver that not much was happening in terms of pre-owned vehicle funding and that will be reasonably large in the next few years?

Ramesh Iyer: Pre-owned vehicle in rural was happening, but it used to be kind of customer to customer kind of a thing that somebody who had surplus money was to support someone who is wanting to sell the vehicle and all that, but those were never kind of supported big time by financiers. We got into it first time through our existing customers who wanted to transact on vehicle and now it has become a very institutionalized product with all the OEMs have got exchange programs now, whether True Value, Mahindra First Choice, My TVS, Tata Okay, all of them, and therefore some financiers have reached out to this market and with GST coming in, the broker system is managing so it is all the more becoming institutionalized so it becomes a very organized player game, so it is a very large opportunity and we have a definite early mover advantage and a deep penetration advantage with large customer base.

Adarsh Parasrampuria: The last question is, Sir, you did mention in your opening remarks about 7% NPA, is there a timeline, is it FY '19 or maybe like a couple of years expectation?

Ramesh Iyer: If you see that from 13 if you could come to 8.6 now, we are looking at a shorter cycle.

Moderator: Thank you. The next question is from the line of Gurpreet Arora from Quest Investment. Please go ahead.

Gurpreet Arora: Sir, in your opening remarks you had highlighted that some banks and NBFCs are going slow in select pockets and that is why you are getting some opportunity, can you elaborate that please?

Ramesh Iyer: You want the geography, or you want the company's name?

Gurpreet Arora: Whichever you are comfortable, both will be good.

Ramesh Iyer: We will be comfortable with geography not company's name. We definitely see them slow in states like UP, states like Rajasthan. We see them slow in states like MP, we see them in states like Karnataka. In East, we see them going a little slow and I must quickly tell you that it is not one company in all the geography, these are different companies in different geographies for different reasons, some of them are busy with collection, some of them have got mandate from their head office not to be after Retail, some of them have converted themselves into a bank and therefore are not as aggressive as they were before, so it is a mix of all these combination, now you can make names from all the explanation I gave that who could be where.

Gurpreet Arora: Sir, my second question is broadly any geography or region are you still worried about which has not recovered yet or where your suspicion continues?

Ramesh Iyer: I think suspicion continues, Tamil Nadu in between one or two years had become buoyant, it has become dormant because monsoon was not too good and politically still not very, very stable, but no major hiccups, but I think growth opportunity is restricted there. We do not have major recovery problem that is all-out, but growth is not happening big-time. Karnataka is the other story while it is on the election spree going forward etc., I think the mining has still not fully opened, the infra story had not fully ramped up, and therefore, Karnataka could not participate in growth as much as we saw maybe in other states, so Kerala is kind of anybody's guess, it is not growing nor is it declining. Other than that, we do not have any major, major problem but as much as UP is growing, did we see Maharashtra grow, the answer is no. As much as MP is growing, is Gujarat growing, I would say no, so comparative growth rates are lower, but they are not cause of concern. The cause of concern from a growth perspective it is only Karnataka, Tamil Nadu and to some extent Kerala. From a recovery perspective, I do not think we are left with any major pockets where we have an issue.

Gurpreet Arora: One follow up on that was anything in the West Bengal region, are we comfortable there?

Ramesh Iyer: Yes, but in East other than West Bengal everything else is small also like even though Assam is a very aggressive growth story, but what is the total contribution of size. North-East like Arunachal, Meghalaya, Nagaland, all these places we are there but they are not something, let us say that none of them sell anything, still our growth rate would be 3%-4%, 5% here and there, and so East is not something that we ever have been overly worried about growth or no growth, but they contribute about 10%-12% or 15% I think of the total balance sheet.

Gurpreet Arora: Sir, my last question is if you can highlight our growth strategy in the SME, what sort of growth rates and what sort of economics are we working there?

Ramesh Iyer: I think our growth rate in SME comes from again three segments where you know the Mahindra ecosystem support to the supplier and dealers, so they will maintain the same 25%-30% kind of a growth opportunity, since the OEMs have started doing well looking at schedules differently, we do expect expansion programs of all the suppliers happening, so clearly that will be one growth story. I think the small trader financing that we started with the support of the OEMs and the dealers support, that will also maintain, our overall growth this year in SME has been around 50 odd percent and I think to maintain a 30% to 40% growth considering that we are not still a very significant player, I think that is doable but we are not chasing growth, we are growing with quality conscious in mind and taking the OEM support as one major support available for choosing to whom to lend to.

Moderator: Thank you. The next question is from the line of Mayur Perkeria from Wealth Managers. Please go ahead.

Mayur Perkeria: Sir, couple of questions from my side, you have added lot of cherries already in your opening remarks by the way of growth, NPAs, so if you can just highlight, in previous cycles we have seen ROAs upwards of 3.5 even touching 4%, where do you see in this cycle the ROAs can touch, can it reach 3% plus on a two to three year sustained basis?

Ramesh Iyer: I used to give this explanation in the past that we had reached 1% and I said it will reach 3%, when we collect 1% from the past provision and 1% going forward not required to provide so high, I think recovering from the past provision is started seeing and obviously therefore going forward will not be required so much, will be the natural thing to follow and if we talk of growth at 20%-25%, this is a very funny market where when growth comes recovery happens and when there is no growth, there is no recovery because it is a fundamental cash flow the customer which is what speaks, so we do think that going back to 3% in next two to three quarter kind of a cycle may be end of March kind of situation, is it visible, I would think the answer is yes and will it stay at that 3%, I would think, based on average plus monsoon, based on infrastructure story both from Central and State that will kick off if not already going forward, then the cash flows will hold up for us to feel comfortable to make that statement as doable.

Mayur Perkeria: Sir, a more specific question, what would be the average duration for our NCD book currently, because in the last three-year cycle, we have increased the proportion of NCD book upwards of 50% now and with rising interest rate you did add a small remark that borrowing change profile you are looking for, so if you can give us more specific as to what is the average duration of the NCD book and how do we see the rising interest scenario in mitigation strategy there?

Dinesh Prajapati: NCD book average duration is around 33 months, so effectively as I said our ALM is almost matched, which means that whatever, almost one third of our liability gets re-priced every year which is also true for the asset side. On our banking side, since most of the loans are MCLR linked and they are some of which will be quarterly re-priced, some of which will be half yearly and some are yearly basis, so to that extent the bank borrowing will be roughly 80% will be MCLR linked, around 20% of the bank borrowing is also in the form of fixed borrowing, so to that extent there is a re-pricing in the banking side, otherwise, liability is fixed borrowing.

- Mayur Perkeria:** We are already seeing our cost of funds starting to rise on because of the one third which will start getting matured now?
- Dinesh Prajapati:** As in earlier question somebody raised that is their previous liability which was three years back or two years back some of these bond we would have raised, it would be slightly closer to higher than even the present borrowing rate, so that will get re-priced at lower even at the current rate, but if supposedly one year back what I would have raised money, that will get re-priced of some borrowing we would have borrowed for two years or 1.5 years that will get re-priced at a higher level, so broadly if I see on a blended basis, it will still get, we will not get a benefit of it, however, on the bank borrowing side, the cost has gone up.
- Mayur Perkeria:** Sir, last question from my side is, will you be optimistic in saying that we can reach 85,000 crores AUM in three years' time?
- Ramesh Iyer:** Three years?
- Mayur Perkeria:** Yes or am I being too pessimistic?
- Ramesh Iyer:** No, you are neither optimistic nor pessimistic, you are like my boss, so I think 80,000 is doable in three years for sure. I will tell you three to four reasons why it should happen; first is discounts will vanish, for the same volume we will do more disbursement. Second is as the discounts vanish, the price increase will kick in from the OEM, so for the same value we will do further disbursements. Then whatever are the new segments that we are entering and gaining the market share, we will add additional growth and finally the volume growth of the market in three years will contribute.
- Mayur Perkeria:** Sir, did you say 7% NPA target for this year FY '19?
- Ramesh Iyer:** Yes.
- Moderator:** Thank you. The next question is from the line of Hemali from B&K Securities. Please go ahead.
- Hemali:** Sir, in the opening remarks you mentioned that you have increased your yields in select products in geography, could you elaborate on that?
- Ramesh Iyer:** It is a very elaborated statement.
- Hemali:** If you could specify the geography?
- Ramesh Iyer:** Geography is minus South, so it is North mainly, and it is also a larger market for us and followed by West, followed by East, and in South only select product not across.
- Hemali:** If you could mention the products?
- Ramesh Iyer:** Where we have increased the yield?

- Hemali:** Yes.
- Ramesh Iyer:** That would be little difficult, but I can tell you that pre-owned vehicle we have moved it up a little. In tractor, we have not increased the yield but we have withdrawn some facilities that was being provided, and in as far as cars are concerned, in Maruti, we have not done, but the new segments that we have got into either we have directly increased or we have bargained a subvention from the OEM whom we are taking into that market, so these are different, different formats.
- Moderator:** Thank you. The next question is from the line of Marukh Adajania from IDFC. Please go ahead.
- Marukh Adajania:** I just had one question, Sir, how would you tackle NPLs in your rural housing sub?
- Ramesh Iyer:** It has already come down so much from 13% odd to it has come to 10% level.
- Marukh Adajania:** Is this the level it is going to stabilize at?
- Ramesh Iyer:** I think wait for another two quarters from here, because Maharashtra money is just coming in, it is largely contributed for rural housing from Maharashtra and as that money starts coming in, you will see a decent correction happening to this number very soon.
- Marukh Adajania:** What will be your normalized level, like say in two to three quarters?
- Ramesh Iyer:** Two to three quarters, I think it will kind of reach the MMFSL level, about 7 odd percent.
- Moderator:** Thank you. The next question is from the line of Harshit Toishniwal from Jefferies. Please go ahead.
- Harshit Toishniwal:** Firstly, if I look at the SME I just want to understand, we give interest-free loans to our dealers to a particular extent, is that also parked in with SME advances?
- Ramesh Iyer:** No, let me clarify it, to the dealer what we give as a trade advance which is nothing, but a retail linked loan, and therefore, the conversion of that amount happens in the retail level and it is not a part of the SME. What sits in the SME from a dealer side if any is an inventory financing, if it is done with some collateral or whatever or else it is all supplier financing, supplier bill discounting, or supplier expansion programs, small trader expansion programs and those kind of things.
- Harshit Toishniwal:** Sir, where are these then trade advances to the retail linked loans, where are they parked?
- Ramesh Iyer:** They must be in something called others, if you see this one item called SME and Others, so SME is independent, others are independent.
- Dinesh Prajapati:** SME is 9% which is also in the footnote mentioned.

- Harshit Toishniwal:** Sir, in these loans, we do not charge them interest up to a particular period of time, so can I know the?
- Ramesh Iyer:** SME and all we start from day 1. In this trade advance, there will be no interest but that is factored into our lending scheme, so that advance is equal to the retail levels that we do with dealer.
- Harshit Toishniwal:** Sir, another question on the housing finance, so clearly this quarter has been phenomenal both in terms of disbursal, AUM growth, asset quality improvement and all, but if I look at the yields they have come off a bit around 150 to 200 basis points for the quarter, is it that we are shifting the customer class a bit to which we used to serve?
- Ramesh Iyer:** There are two things here, I think one is the little product mix change here in terms of priority, affordable housing etc., but at the same time when you have an high NPA, you also have some income reversals which happen and that pressurizes the margin, so no sooner you see the NPA reversal starts happening, the collection, you will start seeing there is a jump in the margin that happens, so I must confirm to you that in the rural business there is no shrinkage of margin out of lending rate reduction, but the new segment of business that we have got into is at a lower rate than the rural businesses, and therefore, the book may look to have been a little lower.
- Harshit Toishniwal:** But the customer segment is broadly the same?
- Ramesh Iyer:** No, they are very different, one is the 1 lakh loan fellow, and another is the 5 to 7 lakh loan.
- Moderator:** Thank you. The next question is from the line of Alok Shah from Centrum Broking. Please go ahead.
- Alok Shah:** Sir, one specific thing I was trying to understand here is that when I look at the pre-owned and other space that book is now closer to 20% of AUM and it has kind of grown from 16% two years back, is there a number that we are looking at scaling this book to a particular level?
- Ramesh Iyer:** As I said pre-owned will go from a 10% to 12% - 13% on a growing book and SME also will go from 8% to may be 10% kind of a thing, so the two together will reach a level of maybe a 20% kind of a situation, 20% - 21% of situation in a growing book at 20%-22%.
- Alok Shah:** Sure, but we are already at 20% level, 9% is my pre-owned and other SMEs?
- Ramesh Iyer:** 17%, so therefore I am emphasizing in a growing book it will go to that 20%-odd.
- Alok Shah:** The point that I am trying to drive here is that when I kind of exclude this part of book from my overall AUM that number looks something less than 18% AUM growth that we talked about and then growing this book at 20% run rate?
- Ramesh Iyer:** In my one of the earlier question I answered this, where I said that please understand currently the vehicles, tractors, at least the vehicles and cars etc are available on discount, so for the same

volume there is a low priced product which is low disbursement. We do see in the next couple of quarters very quickly or may be another three months or four months, the discounts will vanish over a period, and therefore, even for the same volume, you will have a higher disbursement and then comes the volume kicker that takes you to the next number and then comes the price increase for it to go to a further number which is why I am saying even in cars and UVs, we do expect the growth rate of upward of 20%.

Alok Shah: Two is how the LTV moving in this space, the pre-owned?

Ramesh Iyer: LTVs have remained constant over a period of time anywhere between 72 - 73 to about 76 odd percent.

Alok Shah: Finally, on this pre-owned space, you talked about this getting more institutionalized and kind of formalized in last one year or so, how is the competition, there would have been some other NBFCs or not so bigger names who would have been working in those markets, so is it kind of getting competitive or it is just that the space is so big enough for everyone to do business?

Ramesh Iyer: We are present across the country, we have not found another player to name who is present across the country, but if it is a little semi-urbanish, we do see HDFC, what is their finance outfit called HDB or whatever, we do see them in some pockets. We clearly see in different pocket like AU Finance used to do earlier and they continue to do small numbers in maybe Rajasthan, Maharashtra kind of a market. We do see Magma trying to do something in East. We do see Chola doing something in South, so there are different players, L&T Finance is doing in some markets in tractors, so I think you will find different players in different geography also for different products, so we do not see one player all product across the geography.

Moderator: Thank you. The next question is from the line of Bhaskar Basu from Jefferies. Please go ahead.

Bhaskar Basu: I just had one question on the yields, if I look at the calculated yield, there seems to be almost a 51 BPS decline on a YOY basis, I understand obviously last year 4Q there was additional income due to decline in GNPA, that would have been the case this year as well, so any reason for decline in yields per se on a YOY basis?

Ramesh Iyer: If you look at SME growth will always be at a lower yield, so one is if you kind of need to look at without SME in the auto segment what is the yield happening, so we have not seen any decline there, so it is a product mix change which would have cost that more than any pressure of margin.

Dinesh Prajapati: The borrowing has come down to that extent re-pricing.

Bhaskar Basu: What would have been the additional income recognition because of fall in GNPA during this quarter?

Ramesh Iyer: They can send it to you separately maybe.

- Bhaskar Basu:** Just to follow up there, regarding the product mix, so does it mean that with lot of growth actually going to come from SME, you see yield trending lower?
- Ramesh Iyer:** No, but please look at it at the margin levels you may see the margins coming down whatever, but operating and SME business is not at the same 3% overhead and it is not going to bring an NPA of the same level, so at the ROA level they actually tend to even improve the ROA as you get to this businesses with lower cost of operation and lower NPA.
- Bhaskar Basu:** Basically, the credit cost is where you think would be an offset in terms of ...?
- Ramesh Iyer:** Even cost of operation, these are who will operate through the banking system through ECS and all that, so there is no major recovery cost like a retail business.
- Bhaskar Basu:** In terms of cost to income, do you have any guidance because that is something which has remained elevated?
- Ramesh Iyer:** Somebody asked that question as well, if you kind of remove there are some one timers which have got provided, which is we have re-looked at our gratuity provision by an actuarial valuation and that has cost us some 15 to 17 crores and there were some performance-based incentives which were a part of our compensation announced and that has been fully provided for looking at the performance level and that is a one-time cost of another 20-25 crores. If you kind of were to neutralize them, there is no increase in the cost.
- Dinesh Prajapati:** I can share you the income reversal figure for the period for the year, last year it was 230 crores on account of income reversal, this year it is 135 crores.
- Moderator:** Thank you. The next question is from the line of Pankaj Jain from GCJ Finance. Please go ahead.
- Pankaj Jain:** Sir, your performance in rural housing has been strong in the quarter, so just give a qualitative comment on rural housing as well as insurance broking business?
- Ramesh Iyer:** It is a large potential business and I think we are still not completely been benefited of the potential available because we still are penetrating in each geography even more deeper and therefore if we have grown this year at upward of 40 odd percent and the profit at about 70 odd percent, I think that potential continues to be there while looking at the size of growth, we have also added to that vertical a low-cost housing and an affordable housing vertical which will be around 15% to 20% in the next couple of years that we speak, so when the book grows at 30%-40% one must consider that they will be contributed also by affordable and low-cost housing coming in and NPAs remained elevated, but they are correcting except in State of Maharashtra where the correction was low. We do expect that they will get corrected also in the next couple of quarters and that would contribute to the growth of profits the way they are today.
- Pankaj Jain:** In terms of benefit of the fundraising in equity regime, we have not seen much benefit in Q4, can you just guide us why there is not a benefit of either in interest saving or more come from interest?

Dinesh Prajapati: This is like 2000 crores of liability getting replaced because the growth rate was fast, at the same time if you see last quarter the short-term as well as long-term bond market which is money market as well as the long-term market was elevated. Effectively that to some extent got offset on account of that. The incremental book growth was much higher in the last quarter if you see, so the incremental borrowing is also equally high whereas income may not reflect fully in this quarter, because it is accrual.

Ramesh Iyer: One way to look at it is, it has been to have this 2000 crore capital for the same growth rate, we would have borrowed 2000 crore more and it would have actually pushed up our cost to an extent, you can consider that to be the steady because it is an overall kitty you are not specifically able to see it.

Dinesh Prajapati: On 2000 crore 2% type of for the quarter.

Pankaj Jain: In terms of our earning ratios, ROA and ROE, I think last time during Q4 we said we will lead 3% ROA from 1% last year, but this time we have reached around 1.9% and our ROE is around 11%, in good times we are reaching 11%, so when we expect Mahindra Finance to clock 20% ROE, how far are we from that level, Ramesh, qualitative comments from your side?

Ramesh Iyer: We said we will reach 3% ROA not in one quarter, right?

Pankaj Jain: You said last year this quarter.

Ramesh Iyer: Correct, so what did we say we said that 1% ROA improvement will come from corrections of previous NPA and then going forward when we do not need to make the same provision, but in the meanwhile we will have to move towards 90 day NPA as well, so we have moved to 90 day NPA and in spite of that we have come to this 2%, so I think this year you will see us move towards from two to three and then also the capital will get better geared, we are only four times geared or whatever, so once the capital also gets better geared to 5.5 odd times and move towards 3% ROA, I think we will touch the numbers that we are all looking for.

Pankaj Jain: You are saying we will reach 3% ROA in 2019?

Ramesh Iyer: I am saying we will put in our best effort to reach there, market has to support that, monsoon has to be good. We do not see reasons from the market as we speak that it will not allow us that opportunity.

Pankaj Jain: We are still having 11% ROE, I mean we are in a unique position, we have a strong rural presence, some of our competitor are clocking more than 18% ROE and for last six years we are having the same profitability...?

Ramesh Iyer: One thing I can tell you is that if you are comparing us to competition, I can tell you for a fact that they are not in the same business and they are not of the same size, and they have not raised the capital as of now, and therefore, their gearing is not at 4x, but at the same time I am telling

you that we have reached 2% and we would reach 3% by not requiring to provide NPA at that elevated level.

- Pankaj Jain:** Lastly, you said our credit demand guidance for this year would be around 20% to 22%?
- Ramesh Iyer:** That is right.
- Moderator:** Thank you. The next question is from the line of Saurabh Kumar from JP Morgan. Please go ahead.
- Saurabh Kumar:** I just wanted to know what is the write-off level for F '18 this year?
- Dinesh Prajapati:** Full-year bad debt is 547 crores and on account of pre-closure and foreclosure, it is 510 crores.
- Saurabh Kumar:** Sir, just additional thing on this cost income, cost to asset like you bottomed at about 3% is like the best you have done in Fiscal '14, so is that the number to keep in mind?
- Ramesh Iyer:** I think 2.85 is something that is doable with some one-timer that is already in this may not be required going forward and the branches will also start being more productive than they are today, so they will also rationalize the cost to an extent, so I think about 2.8%-2.85% is something that should happen.
- Saurabh Kumar:** This should be Fiscal '20 or?
- Ramesh Iyer:** I think we should start seeing correction of that this year for it to settle sometime in the mid of next year.
- Saurabh Kumar:** Just one more final question Sir, what will you think will be the normalized ROA for these rural housing businesses?
- Ramesh Iyer:** Normalized ROA for rural housing, I think anywhere close to 3% is what they should be able to, I think you must take a range anywhere between 2.2 to 2.5-2.6 kind of a thing. They will kind of keep switching because we are continuing to add business and the business has not stabilized. If I do not add geography, if I do not add new business then we can make a number to say like for example if I want to pick one state which is five-year-old, I can tell you that they will be upward of 3% but when I say that I am adding 40% new book and they will come with new expenses at 6%-7% etc. until they mature to start contributing it will not, but if you think the day we announce saying that rural housing is now fully matured across the state and the natural growth of 15% to 20% is what we are speaking then we would be able to make a statement of 3% plus. At 40% to 50% growth rate, one should imagine that the cost of setting up, cost of acquiring this businesses and stabilizing and running it will take away 1% ROA out of this.
- Saurabh Kumar:** Sir, just one final question, per Maruti your market share in the rural business will be pretty much intact, right?

Ramesh Iyer: Yes, in fact it has grown because now the NEXA products have also started entering that market, so if you were to take that denominator as only the vehicles of Maruti sold in rural, I think our market share anywhere between 14% to 16% kind of a situation will be there while our overall market share has remained at 7% to 8%.

Moderator: Thank you. Ladies and Gentlemen, that was the last question. I now hand the conference over to Mr. Abhishek Murarka for closing comments. Thank you and over to you.

Abhishek Murarka: Thanks everyone for being on the call and many thanks to the management for giving us the opportunity to host this call and wish them all the best for the year ahead. Have a Good Evening.

Moderator: Thank you very much. Ladies and Gentlemen, on behalf of IIFL Capital Limited that concludes today's conference. Thank you for joining us and you may now disconnect your lines.