



L&T Finance Holdings

Investor/Analyst Conference Call Transcript

July 23, 2013

Shiv Muttoo: Good evening and welcome to L&T Finance Holdings Q1FY14 conference call. We have with us on the call Mr. N. Sivaraman - President and Whole-time Director and other members of the senior management team. We will initiate the call with opening remarks by Mr. Sivaraman followed by an interactive Q&A session. Kindly note that some of the statements made on today's call may be forward-looking in nature and a note to that effect is stated in the presentation sent to you earlier. I would now request Mr. Sivaraman to provide his views on the results this quarter and his thoughts going forward.

N. Sivaraman: Thanks for joining us on the call. I hope that you have had an opportunity to go through the press release, statutory advertisement copy and the presentation which have been uploaded on our website.

We begin with Slide #4 which gives the industry overview. I am sure that there is nothing on this slide which is not known to you, but this is more to set the context for explaining our overall performance and our outlook going forward.

On the positive side, the Government has been consistent in making announcements on getting various projects kick-started. There has been some action on the fuel supply agreements, which are expected to be signed by most of the power producers with Coal India. I also hear that the Coal India supplies have been of a fairly good volume, which augurs well for power projects that are on the verge of starting operations. The other development is that there are a few electricity boards which have agreed to participate in the debt restructuring program. It augurs well for power producers as some of them who are sitting on capacity and not able to find a buyer, would perhaps be able to get the power sold.

Monsoons have been good, so we expect the rural economy to continue to do well. Hopefully it is not excessive. The pattern of rains for the last 1.5 months has been pretty strong and widespread in terms of coverage.

On the other hand, we are concerned about the potential of the current account deficit remaining at elevated levels on account of crude oil prices moving up, though it may be mitigated to some extent by the reduction in both gold prices as well as in the quantum of gold imports. The volatility and the weak Rupee definitely causes concerns on what trajectory inflation would take going forward and the consequent monetary action that RBI could take.

While Food Security Bill could be beneficial in the longer term once it is rolled out fully in an efficient manner, in the shorter term it could have an impact of the fiscal deficit. We also need to be cautious about how the State Governments will react to this initiative and whether they also would resort to populist measures to win votes, which does cause concern to us.

In the near term the RBI intervention to help the Rupee and keep the rates high has definitely created a level of uncertainty on the interest rate. While there were concerns around liquidity to begin with, the liquidity situation seems to have improved. In fact it is working at a level which is well below the RBI limit of Rs. 75,000 crores. This should start influencing the short term interest rates sooner than later. They have come down by about a percentage or so, but if liquidity continues to remain as stable as this, then perhaps it could have an impact on the way short term interest rates could move.

Moving over to Slide #6 which captures the highlights of this quarter's financial performance - we have had a healthy 31% Y-o-Y growth on loan book, which is good. The fact that we have been able to grow the book in the segments and clients whom we chose to lend to, is a positive. The Investment Management business has started getting back to growth mode with the average AUM for the quarter having gone up by about 23% on Q-o-Q basis. This is one of the highest growths in the industry. We shall get into more details on this when we discuss the Investment Management business.

The Y-o-Y profits have grown by about 20%. This is on the back of margin improvements, offset by the increased credit costs to some extent. Part of the credit costs are against the NPAs and part of it is on basis of additional provisions we have taken as a precautionary step, based on our estimation on how the NPA situation would emerge over the next two quarters.

The heartening aspect is that the TTM ratios have shown an improvement over the last 12 month period i.e. FY 2013. We have added the TTM ratios to give a more comparable trend over a 12 month period, thereby removing the impact of seasonality and annualization of quarterly results on the overall performance.

Asset quality concerns have continued. We have had deterioration in the asset quality, seen in the elevated levels of both absolute NPAs and the NPA ratios. This has been primarily driven by the corporate segment, including some corporates engaged in the infrastructure segment and continued pressure in the CV & CE segments. The rest of the NPAs in the retail segment have been largely seasonal. As you would have observed the 3rd and 4th quarters generally end up being one of the best quarters for managing the retail NPAs.

Our outlook is that the NPAs could be elevated in the near-term, i.e. the next one to two quarters. Some of the steps taken by the government and an improvement in release of payment overdue by NHAI against the claims should help in containing further deterioration. The credit cost that will get charged to the P&L account is expected to remain at current levels for at least one more quarter and we could see a slow improvement coming in thereafter.

Moving to the next slide on Summary Financial Performance - the disbursement growth for the quarter on a Y-o-Y basis has been about 46%, which has resulted in the Loans and Advances growing by about 31%. The NIMs have grown by 37.6% which indicates that the margins have been improving. PAT growth is about 20% for the NBFC businesses. Gross NPAs as we discussed have moved up to 2.54%. ROE for the NBFC business has dropped to 11.26% as compared to the previous year. The computation of ROE and NIM are on an all-included basis. In order to exclude the effects of micro finance provisions we used to previously report adjusted ratios. Going forward the ratios would be on an all-in basis as some of the anomalies which existed in understanding the performance have disappeared.

Average AUM for the investment management business touched close to Rs. 14,000 crores, indicating that the closing AUM for June has been far better than the

opening AUM for this quarter. The PAT before exceptional items for the Investment Management business has dropped to loss of Rs 3.5 crores as compared to Rs.6.3 crores in Q1FY13 and more importantly as compared to Rs. 14.6 crores for Q4FY13.

Moving to Slide #8, the growth in PAT has been contributed as we mentioned because of the margin improvement, while being offset by credit costs to some extent. Drop in PAT as compared to Q4 of last year is primarily on account of lower fee income in L&T Infra and the higher credit costs. Accounting for the readjustment of the tax cost of L&T Infra for Q1FY13 which was about Rs.14 crores of improvement in PAT, the Q-o-Q growth in PAT is also quite consistent.

Slide#10 is on the market scenario and outlook for the Rural and Corporate Finance business. The rural products segment has done well on the back of a strong rural economy and the early arrival of good monsoons. From what we understand, the monsoon dispersal has been quite good. Additionally the short gap between the two phases of monsoon have given an opportunity for sowing, consequently the Kharif crop is expected to be good. All this has given a good fillip to the sales of tractors as well as the small commercial vehicles in the rural markets, contributing to healthy disbursement growth.

On CE and CV, the scenario is well known to all of you. The combination of mining-related issues, lack of construction opportunities in the infrastructure segment as well as the general increase in operating costs have resulted in a negative growth in both CE and CV segments.

Micro finance business is back into growth mode after all the issues that we had to face due the legislative/regulatory changes in the Andhra Pradesh. I can say that as of now the business is breaking even. We expect to see consistent growth in the disbursements and consequently the micro finance book should start catching up in terms of the overall book size.

The Corporate book continues to be under stress. There are very limited opportunities for new disbursements given the lack of investments. We have been very selective in lending. We have attempted to lend to really good quality corporates even if the margins are slightly less. We believe that this will enhance the quality of the book and also ensure that the overall ROE compromise, due to lower margins, would not be significant.

Slide#11 is on the market scenario and outlook for the Infrastructure Finance business, most of which you are aware of. With regards to thermal power some initiatives with regard to the pass through of coal price increase have been taken. Also as I mentioned earlier, some forward movement on the level of SEB restructuring options have come through. The fuel supply arrangements which are being entered into by Coal India and also approval of about 18 new mining projects should help in improving the overall environment for the thermal power segment. On renewable energy - tariff revision by Maharashtra and Madhya Pradesh reinforces confidence in the sector, while lending opportunities in this segment continue to exist.

With regard to the road sector, the reduction in traffic growth is putting some of the projects under pressure. Hopefully the commitment towards further project orders should provide some fillip to both the construction companies and some of the developers. While we have been talking about the slowdown in payment release by NHAI and other government agencies, at least the road segment has seen some movement coming through. NHAI payment seems to be starting to happen and definitely a few contractors have received payments of their pending claims from

NHAI. This, we believe, should help ease the cash flow of some of the construction companies. There are also new orders which the Government has been talking about. So these would provide an opportunity to the construction companies and help improve their overall profile and increase revenue generating opportunities.

Dinanath Dubhashi: The next slide (slide #12) talks about the disbursement trends and the numbers are more or less in line with what Mr. Sivaraman has been talking about. The growth has mainly come from rural product finance, which is primarily tractors and also cars to some extent. Though the car industry has not done so well, we have been able to do reasonably well primarily because of a lower base and also due to our concentration being on semi-urban and rural segments of the car industry.

The other segment which has grown of course is microfinance, once again on a lower base. What we would like to emphasize is that the business has been growing at a reasonably good level now in all the states where we are present leading to an overall growth of about 15%. The growth in capital markets has been primarily due to lending to very few select and handful top quality promoters, especially for promoter funding. If you really look at the growth of the other segments we have been very selective both in terms of credit as well as yields, which clearly is indicated by the negative growth.

Personal Vehicle Finance which is Family Credit shows a big growth because it was not there with us in Q1FY13, but if you take a like-to-like comparison the business disbursement shows around 20% growth. The good thing is even though the TTM growth in disbursements is just about 5%; this has translated to a Y-o-Y growth in the book by around 24%. That gives us a good fillip to our overall NIMs.

Moving to the next slide (slide#13), which is on the summary financials for the retail and corporate finance business. You would see that Y-o-Y growth in interest income has kept pace with the loan book growth, indicating that we have maintained yields at more or less similar levels. Interest expenses have been controlled and have not been entirely passed on to the borrowers, resulting in NIM growth that is higher than the loan book growth. We continue to focus on controlling operating expenses by focusing on increasing productivity. There has been a good increase of around 45% in contribution before credit cost and the credit cost increase of 72% is basically in line with what Mr. Sivaraman has talked about on the corporate portfolio and some parts of the construction equipment portfolio witnessing stress.

Even though the number of new NPA additions from the corporate portfolio in this quarter has been fairly limited, but the credit costs have gone up mainly because of non resolution of previous NPAs in this quarter and our policy of providing what we believe would be needed based on the notional asset value, which is more than what RBI requires. The footnote provided below indicates that we carry about Rs. 148 crores of additional provisions for this business, in addition to about Rs. 21 crores of repossessed assets. As mentioned by Mr. Sivaraman we do not see credit costs coming down immediately from the next quarter, but we believe that it may not go up further from this point of time.

Slide#14 indicates in ratio format what we have discussed till now. The TTM numbers validate the fact that NIMs are increasing steadily and fee income has more or less been stable. Operating expenses have gone up slightly but it is more an indication of FamilyCredit coming into the fold. On a like-to-like basis, the expenses have been controlled pretty well. The increase in credit costs as indicated earlier has resulted in the RoA being just about 1.6% and RoE to be around 11%. On a steady state basis, if the corporate NPAs or corporate credit

costs were at levels which normally this business warrants, I would say that RoA will be at least 0.6% to 0.7% more.

The next slide (slide#15) talks about the housing finance business. Though we have indicated a positive PAT for this quarter, we would like to concentrate more on the organization building that we are undertaking. All the products that are needed for a good housing finance company are now in place. We have put in additional equity into the company and have obtained AA rating for the senior debt of this company. 13 markets have been operationalized, out of which 9 markets have stabilized. GNPA levels as you see are mainly from the legacy portfolio as it is too short a period for the new portfolio, but there is no stress in the new portfolio. Disbursements are in line with our expectations. To summarize, the building blocks of housing finance business are being put in place as per what we had envisaged.

Suneet Maheshwari: If you see Slide#16 on Infrastructure Finance, you can see some sectoral growth which is reflective of the growth that we have seen from our portfolio. The growth in the case of projects has really come in from past exposures that we had taken, so there are disbursements from previous sanctions coming in. In some of the other cases, these are more refinancing that has happened. One significant area of growth seems to be Power (Corporate + T&D) where we have given corporate loans to a very good utility in the transmission sector, which we thought was good opportunistic business.

In roads, I would say disbursements have been largely in the area of refinancing. Transportation which has been the large area has not seen too many fresh projects because the developers and the construction businesses are under stress or rather could be stressed. So it has been just old projects being refinanced. In telecom, for Q1, there was not much of activity. I think till the spectrum issue sort of settles down, we are not going to see much activity in this space. Again, if you look at the disbursements on a year-on-year basis, you can see where this growth is coming from.

So again to summarize, Thermal Power is more in terms of old projects where some movement is happening in disbursements. Renewable power has been a major area of growth, except maybe in the more recent times, but otherwise on a steady state basis I think it has been a decent part of our portfolio and will continue to remain so. I also mentioned about Transportation and some corporate financing we have done.

So now if you look at our portfolio breakup, Corporate at 38% and Projects at 58% of which 28% are operating and under construction is around 30%, also there is a small equity asset of about 4%. So that kind of totals up to 100 and I think our perspective would be to keep the operating portfolio at about 30%. Since we are talking about floating an IDF, at an Infra platform level, we would want to increase our operating asset exposure gradually over a period of time. I reckon that by the end of this year it could be somewhere around 35% or so if things go smoothly and I think that it is a decent number to sort of stay at going forward. Top ten borrowers represent 21% of our outstanding, top ten borrower groups comprise 28% of our outstanding. So I think the point that comes out of this is that emerging entrepreneurs still form a fair amount of our portfolio.

Moving to the next slide (slide#17), which is on the Summary Financials. The growth that has happened in this particular quarter indicates that we are just staying on course on a Y-o-Y basis. There is of course some growth that is happening, but if we look at it from a Q-o-Q basis it has been a little even, in the sense that not too much of a growth has been there. The first quarter generally has

been a little sluggish in terms of the disbursements. We reckon that this will go on for another one quarter before there is an upswing.

Some of the steps taken by the Central Government entities and the initiatives on projects by the Cabinet Committee on Investments will yield results hopefully by second or the third quarter of this year, which is when we will see significant movement going forward. Looking at the credit costs where we made additional provisions in view of the stress we see in our portfolio, it is a part of our policy to be on the safer side, to be more on the conservative side. Where we see stress, we make voluntary or additional provisions over and above whatever RBI stipulates and as things start to improve, we could unwind some of these.

I think the more important point for us to make is that with whatever stress we have seen in the past, we had seen this in 2009 and we are seeing it now, we have not had a complete write-off case. There are delays and we make provisions, but post 2009-2010 we had significant level of unwinding that had taken place. Looking at the way things are, I am hopeful that the same kind of trend would continue for us and things would improve hopefully, by the end of third quarter.

If we look at Slide #18, it gives us a flavor of the key ratios. They are by and large consistent if you look at them on a TTM basis, there has not been too much of change. The difference that has been really is in the credit costs which signifies the additional provisioning that we have been doing over and above the normal provisions. Return on Equity for this quarter seems to be a little modest mainly because of credit costs, but on a trailing basis I think we are steady at about 16% and we would likely continue to be at these levels.

Gross NPAs are at 1.54%, so that has not changed so much and Net NPAs has also risen to 1.25%. What has definitely added on is the credit costs which are on account of voluntary provisions that we have been talking about.

N. Sivaraman:

Slide#19 is on the investment management business. All in all, it has been a quarter of consolidation and growth during Q1. The asset growth has been impressive and we have focused on the opportunistic area of fixed income. We have worked more on the duration products than the liquid products, as indicated by the bottom right table. Equity and hybrid have remained more or less consistent, cash and ultra short term has also remained at about 36%. It is basically the FMP and other Fixed Income products which have really shown a significant growth. We believe that these would be margin-accretive and would help us in our goal towards achieving breakeven sooner than later.

If you look at the summary financials, at a Net Margin of (-10) basis points on the assets, we are clearly as close to breakeven as it can be. I believe that the breakeven goals are very much in sight, given the level of upswing that we will see due to a high asset base.

The other important aspect is opex, which has moved up to Rs. 24.4 crores in Q1FY14 as compared to Rs. 8.5 crores on the erstwhile L&T Mutual Fund (which was without Fidelity MF) in Q1FY13. In the fourth quarter operating expenses were about Rs. 36.5 crores. Clearly the efforts that we have taken towards optimizing costs have shown results. They have led to improving the net margin to about 10 bps even though the revenue has remained more or less flat as compared to the fourth quarter. We continue to see outflows in the equity side, primarily because of the market environment and an aversion to equity from investors.

Moving to the next slide (slide #20), which gives a broad outlook for the investment management business. We see opportunities to grow the Fixed Income category.

The broader business space that the group has got does help bring innovative products to the market and create value for our investors. This is one of the reasons we have been able to see good accretion to our assets. We will drive revenue growth through strong focus on retail and by maintaining a balanced product mix that would be more interesting to the retail segment. We continue to maintain focus on the fund performance. Since the time of the takeover and after the transition period, today we are very much able to see the consistent improvement in performance on both equity as well as the debt sides.

We are setting up focused 'Investor Education Programs' and also trying to reach out to the Tier-2 and Tier-3 cities, which is what SEBI calls as beyond the top 15 cities. This is something which we are working on.

Slide# 21 is on the Wealth Management business – It is progressing well. We have seen assets growing further to about Rs. 3,000 crores as compared to about Rs. 2,200 crores at the end of March. We do see this business really catching up. We have been able to establish both processes and service benchmarks to make our customers happy and thereby achieve growth over here.

There are two other updates that we wanted to provide. Slide#23 is on the IDF. We are making good progress. As of now, it is awaiting regulatory approval. We hope to see this entity being operational before the end of September; of course it is subject to the RBI approval coming through by that time. We have got our strategy ready to build assets with this balance sheet.

Slide# 24 is on the Banking License. I am sure all of you are aware that we have submitted an application for grant of a bank license. We see this as the next logical step in our evolution to be a comprehensive financial services player in the country.

Some of the basic rationale that we see for ourselves is that straightaway we will be able to address a larger revenue pool, be it in terms of the scope of services one can offer or the customers that we can address. Even though our cost of money on an all-in basis is as competitive as the banks, we have not been able to service the higher-rated corporate as we need to provide a relatively higher capital adequacy as an NBFC than what a bank needs to provide. So becoming a bank will definitely enable us to expand the customer segment more easily. These will result in our ability to participate in a larger revenue pool.

Retail liabilities provide both stability as well as some level of predictability to the liability segment. If one is rolling out a set of branches to acquire assets, I am sure that these branches can be better utilized as well for procurement of liabilities. The leverage that a bank can enjoy is far higher than that of an NBFC. We have seen that most banks have leverage in excess of 12 to 15 times, even after excluding the CRR and SLR assets. So that definitely provides us with a better opportunity to price our services competitively, while targeting a decent RoE on the balance sheet.

The regulatory framework as you all know has been moving more towards convergence, resulting in the so-called regulatory arbitrages (for NBFCs) also slowly disappearing.

Slide#25 has few details on the impact of converting into a bank. The Non Operative Financial Holding Company (NOFHC) will be promoted by LTFH, which will in turn house all the financial services companies as well as the bank. If and when we get a license and we take the next step to become a bank, all the financial services NBFCs will have to be merged under one umbrella.

On the regulatory side, we need to meet with the CRR-SLR norms as well as the priority sector norms on day zero. As per the priority sector guidelines that currently apply to the banks, you need to meet with the priority sector obligation as of the previous year's closing assets. This means that the 31st March 2014 balance sheet will become the base for meeting with the priority sector requirement during the period 2014-15.

We do believe that there will be some impact of CRR-SLR because of the negative carry that one might have between the cost of deposits and the yield available on the SLR assets. If one factors this and looks at the general deposit rates that are prevailing today along with the yields available on SLR, one can assess a loss i.e. a negative carry of anywhere between 40 to 70 basis points. These will get optimized as we substitute the term deposits or the bulk deposits with CASA as we build our branch network and customer base.

In our assessment, the mandatory 25% rural branches will not pose a significant obligation or cost escalation because these branches do not cost much. They may cost anywhere between Rs 12 to 15 lakhs on an annualized basis. Even if one were to have close to 200 branches, the 50 branches in the rural areas are not going to cost a significant amount of money.

All in all, while there could be a dip in ROE in the first year, we should start catching up from there onwards as the deposit composition improves and the rural branches start producing some revenue. This is what we would like to say and clearly from a long term perspective, we see it as a very important strategic opportunity available, which we should not ignore.

On the summary level, we do see the margins being stable to improving going forward. Our coverage ratio for NPL, based on our assessment is definitely adequate and represents what could be the maximum amount of loss that we could suffer on these books. The Investment Management business should be approaching breakeven sooner than later. So while the asset quality concerns could be a dampener for our performance, we should consistently be seeing improvement on the rest of the operating parameters. With that I would conclude and move to the Q&A session.

Moderator: Thank you very much Sir. Ladies and gentlemen, we will now begin the question-and-answer session. We have the first question from Lakshmi Ahuja of MSFL. Please go ahead.

Lakshmi Ahuja: On Slide#17 for the infrastructure finance business, when we look at the borrowings on a sequential basis they have increased by 4% and the cost of fund on a sequential basis has risen by around 33 basis points. For a substantial part of the time in this quarter the rates were pretty subdued. So what explains this rise in cost of funds?

N. Sivaraman: I would draw your attention to slide #18. One of the reasons why we have put the TTM numbers is actually to eliminate events which end up skewing the figures. If there was a large disbursement or a large borrowing that had been made in the last week of a month, they tend to skew the averages. So in this context, it is not necessarily on account of borrowing costs going up. If you really look at FY13 borrowing cost was at 9.42% and TTM it is 9.38%, then you can see that we have been able to exploit the benefit of lower interest rate regime. One other aspect that you need to consider is that the average gearing levels have gone up, which also results in the borrowing quantum being higher than the asset growth.

Lakshmi Ahuja: Another question was on the NPA movement in this particular segment. It has been said that it is a movement on account of one NPA in Q1. Is it from any particular sector? Could you share some details on that?

N. Sivaraman: There are no new sectors which are emerging as NPAs very clearly.

Lakshmi Ahuja: So there is no big chunky account as such?

N. Sivaraman: No, it is a very small account. The important point is that, if you have seen the number of accounts becoming NPAs as well as the volume of CDR cases that have happened, it has been increasing and there is enough in the pipeline as well. So that definitely is something which we need to factor in while looking at the performance of the next two quarters.

What we are attempting to do is looking at the way the accounts can potentially come up for CDR and provide in advance. If you look at the last 4 to 5 quarters, our provisioning numbers have not been very volatile. That actually tells you that we are conservative, we are anticipatory and do take care of potential stress cases in time, rather than leaving it to the date of occurrence. So that is why you will see that NPAs have gone up by only Rs. 20 odd crores while our provisioning is far higher than that.

Lakshmi Ahuja: What could be the CDR pipeline in next 2 quarters or so?

N. Sivaraman: Pipeline is difficult to define. I would not want to give any expectations on that front, but I am sure that you are keeping track of what is appearing in the newspapers. We could see elevated levels of restructuring for the industry as a whole and we as a participant may not be able to excuse ourselves out of that situation.

Lakshmi Ahuja: And primarily this could be from Infra?

N. Sivaraman: Yes, right, generally around the infrastructure players. It may not be the project as such, but it could be the players who are participating as a service provider or as a developer.

Moderator: Our next question is from Mayur Parkeria of Wealth Managers. Please go ahead.

Mayur Parkeria: Can you outline the broad profile in the renewable energy portfolio? In which sectors would it be and what would be the profile?

G Krishnamurthy: In our renewable energy portfolio we have a broad mix of solar, wind and hydro. If you would like to know the specific composition, as such it is more or less equal. I would say hydro is slightly higher. Hydro is typically small hydro which means projects which are of less than 100 MW, which comparatively carry lesser risk in terms of implementation. That is the kind of profile of projects which we have financed.

Mayur Parkeria: So you mean to say broadly one-third, one-third, one-third in all the three with hydro slightly higher?

G Krishnamurthy: Yes, slightly higher in hydro, otherwise it is almost one-third.

Mayur Parkeria: We have seen a lot of stress in thermal and other sectors of power, not to mention wind has also gone through its own cycle in the past. Do you believe that with overcapacity coming, there are some problems coming in solar? Do you see in the

medium term any stress that can come with more and more people going for solar, the way it happened with wind in the past?

G Krishnamurthy: In both solar and wind, we have been very selective and focused on the type of projects, equipment, geographies, counterparties, etc. So we can say that in every project that we have appraised in the last couple of years, our projects are doing much above or definitely above the appraised PLFs and there is no stress in these portfolios.

Moving forward also, we do not see any issues for us as far as solar and wind goes. This does not mean that the industry is going to remain the same, because there are specific pockets, particularly in wind, where counterparty risks exist or there are wind season issues. So it is more reflective of our pickings and our project selection than what the industry is undergoing as such.

Regarding thermal, definitely there is a pipeline of issues which could happen at the industry level. We are currently not seeing it because we have not been really big in thermal historically and our focus has been on mid-market clients and smaller projects. But at the industry level, definitely projects which are coming up for commissioning in the next 6 months to 1 year are likely to see issues on account of multiple points which all of us are aware of.

Mayur Parkeria: But similar to banks what would be our provision coverage ratio?

N. Sivaraman: Our provision coverage ratio on an overall basis is about 40%.

Mayur Parkeria: As I understand there is no particular norm for NBFC as of now for that?

N. Sivaraman: No, even for the banks these norms have been lifted. They are not applicable anymore.

Mayur Parkeria: There was an anchoring for 70-75% earlier?

N. Sivaraman: RBI has lifted it. I think you need to understand that our provisioning philosophy has been on the assessment of the underlying potential loss in a particular account or on the portfolio as a whole. Our experience in the past definitely has been that it has not exceeded whatever provisioning we make. I have just demonstrated to you that while NPLs have grown by Rs. 20 odd crores in infrastructure finance business, our credit provisioning is about Rs. 51 crores for the quarter. So we are quite anticipative in this area.

Mayur Parkeria: Though the RBI norms have been lifted for banks, but we see internal guidelines for many financial institutions in place where they have laid down internal guidelines for their provision coverage ratios. Do you have any internal guidelines and is there still a spread where you would like to reach or do you believe that they have reached an optimum level?

N. Sivaraman: This is exactly what we are doing, be it in the retail book or in the corporate book or infra book. We do have our own guidelines and policies for provisioning. If you read through our presentation in both the infrastructure segment as well as in the retail segment, our provision levels are far higher than what is mandated by RBI. This is on the basis of our own policy which has been in place.

Mayur Parkeria: I mean to say at an overall level, where do you see this 40%? Do you have a benchmark where you say "We want to increase this level to let us say slightly higher"?

N. Sivaraman: No, there is no mandated percentage. It depends on the mix of the portfolio assets that we have and our experience at a point of time or the near future. It would depend on the way the losses are expected to move in the delinquent accounts or even stressed accounts.

Mayur Parkeria: My last question, our capital adequacy is around 15.5?

N. Sivaraman: You have to look at capital adequacy in the context of overall group level numbers. At the NBFC level, we try and keep it to the minimum requirements with targeted Tier-I of about 13-13.5% and the balance being funded by Tier-II. We keep the excess cash balances at the holding company level so that we can allocate capital based on the growth requirements of each of the companies.

Mayur Parkeria: So what I was trying to conclude is that we do not see any issue in terms of increasing the growth areas in any of the segments of the subsidiaries?

N. Sivaraman: If our growth is in the region of about 25% to 30% in the current year, there will be no need for any additional capital raise by the company.

Moderator: Our next question is from Devam Modi of Equirus Securities. Please go ahead.

Devam Modi: It is heartening to see the investment management division almost close to turning around. So could you give a sort of guidance of what you would expect to achieve in FY14?

N. Sivaraman: It is a function of the market, the liquidity in the system and also the investors own risk appetite. All of them are going to determine how the AUM will grow and how the mix will change. All that I have indicated to you is that at current levels of average AUM we have been able to bring down the losses to 10 bps on the AUM. So we are as close to the breakeven point as it can be. This is what I would like to leave you with.

I do not want to make an outlook statement at this point of time, given the current volatility in the markets. On the equity side there is risk aversion to investing in equities and even on the fixed income side we need to see some stability on the yields and liquidity in the near term. Till that time it is very difficult to make a projection. From our end we will continue to focus on the opportunistic areas of fixed income for the retail segment and FMPs, which have been one of the most active products that we have offered. Given the overall asset size of the AMC, the opportunity for larger corporates to place their funds with us will go up consequently and we do see an accelerated progress towards breakeven.

Devam Modi: What will be the total quantum of corporate debt restructuring that we seeing in our portfolio right now?

N. Sivaraman: Currently, it is about 4%.

Devam Modi: 4% of the total or that is the corporate book?

N. Sivaraman: 4% is in infrastructure. If you are looking at it in the context of impaired assets, then for L&T Finance all the restructured assets are reflected as NPAs, there is nothing beyond that.

Devam Modi: How do we do the provisioning on the account that we shift to CDR?

- Suneet Maheshwari:** It is done as per the RBI guidelines applicable for banks where we provide for any interest losses and for any future sacrifices based on NPV differential.
- Dinanath Dubhashi:** In L&T Finance, the RBI norms require us to classify it as substandard for one year, so it is classified as such and provided like how we provide for any substandard asset.
- Devam Modi:** This is with regard to the restructured assets with L&T Finance?
- Dinanath Dubhashi:** That is correct.
- Moderator:** Our next question is from Saurabh Kumar of JP Morgan. Please go ahead.
- Saurabh Kumar:** One is on the AMC business, it seems despite the growth in your AUM, your net revenues have not gone up too much and the breakeven is essentially coming due to operating costs. Can you just throw some light as to why the revenue is not going up? Is it just the mix issue between equity and fixed income?
- N. Sivaraman:** As you will see in the asset composition, the percentage of hybrid and equity assets has dropped from 47% to 36% for the first quarter. Definitely, equity is not one of the most favorite destinations for the investors currently. That is one of the main reasons. To some extent it has been substituted with the fixed income opportunities. So it is definitely not as high yielding as the equity assets.
- Saurabh Kumar:** Basically, in your banking license slide, you talk about some efficiency being available if you have to follow the CRR-SLR norms. So could you just throw some light on it as to what kind of efficiencies you will have?
- N. Sivaraman:** This is basically about managing the transition from an NBFC balance sheet to a bank balance sheet. It requires a level of planning to be made well in advance, so that the transition can be managed. There is also the opportunity available to keep the IDF as well as the lease and hire purchase assets out of the bank. So you can manage the portfolio in a manner that will help us bring down the burden of the transition from a balance sheet perspective.
- Saurabh Kumar:** Is it technically possible that let us say for the IDF you can sell down the existing operating portfolio which you have in L&T Infra into the IDF and also keep the hire purchase business out of the bank, is that what you are hinting at here?
- N. Sivaraman:** We already have an IDF and we plan to build a balance sheet around that. So the strategy can be either taking assets from the market or if there are good assets available in the infra balance sheet that can also be migrated in the normal course of building the IDF balance sheet. It need not be structured around becoming a bank. So the basic point is that you have the opportunity to distribute the balance sheet across the product range and then make sure the transition is efficient. It has to be managed on the liability side also and not just on the asset side.
- Saurabh Kumar:** One other question on the bank side again. As per your understanding if you were to become a bank, will a cross with the parent, i.e. L&T- targeting their savings account or targeting the IDPL portfolio, will that be allowed or not, because it will be a pretty big opportunity?
- N. Sivaraman:** There is a higher level of governance around the intra group lending. As far as procuring the liabilities from the group is concerned, so long as it is arm's length there is no problem on that front. So I can look at the group employees for the

salary accounts, the vendors in terms of their current accounts and also providing some credit support to them, all those are feasible.

- Saurabh Kumar:** So IDPL may not be feasible, other things are feasible?
- N. Sivaraman:** IDPL is also feasible on an arm's length basis, but the current balance sheet is built with nil exposure to IDPL.
- Moderator:** The next question is a follow-up from Lakshmi Ahuja from MSFL. Please go ahead.
- Lakshmi Ahuja:** Just two questions on the conversion into a bank. Could we see some spike in the NPAs given that you will have to follow NPL recognition norms as that of a bank? Could you see that resulting in a higher NPA?
- N. Sivaraman:** Firstly, the transition to 90 days norm for NPA recognition is anyway getting mandated by formalizing the Usha Thorat Committee recommendation. It maybe one year plus or one year later, but I think we would definitely start slowly migrating towards it, more in terms of the conduct and collection behavior on the ground than necessarily changing our norms.
- Secondly, our provisioning norms as I mentioned to you are more conservative than what RBI mandates. So, one way to manage is to ensure that the calibration of the provisioning is in the right direction to manage this credit cost. It is possible that the NPAs could end up being slightly elevated. You have to understand that we have an opportunity to build high quality assets by lending to higher rated corporates. So from a ratio point of view we may be able to bring it down to normal level in a matter of 2 to 3 years.
- Lakshmi Ahuja:** In any of the segments, have we started recognizing 90 days kind of recognition?
- N. Sivaraman:** Housing Finance in any case is mandated at 90 days. For the Two-Wheeler portfolio we follow the 90-days norm.
- Lakshmi Ahuja:** Another question on the conversion was - given the 18 months time period, how many of branches would we be able to convert into bank branches? Is this a sufficient time?
- N. Sivaraman:** From a point of view of making it bank branch eligible it does not take too much time. We have got 18 months time which is more than enough to cover it.
- Lakshmi Ahuja:** Some of the peers who were pitching for the banking license had expressed concerns that 18 months time is not sufficient enough to convert their presence into bank branches, so that is where the question comes from. But given our network, would we be able to convert?
- N. Sivaraman:** Our current number of branches are about 120 odd. So we do not see a challenge in converting them into bank branches in the specified time frame of 18 months, assuming RBI approves conversion of all our existing branches into bank branches.
- Moderator:** Thank you. Actually, we have got one more question; it is from Avneesh Sukhija of BNP Paribas. Please go ahead.
- Avneesh Sukhija:** What is your view on the liability profile of the company especially given the recent RBI measures? Do you expect any compression in NIMs or are NIMs likely to stay stable?

- N. Sivaraman:** To the extent that we have undertaken replacement of borrowings over the last say two weeks, the costs have been slightly higher. But as I mentioned during my comments, this is something which all of us believe will be a temporary measure. The liquidity situation on the ground has been far better than the limit that RBI has put in place. So slowly the short term rates should stabilize and improve is what I would guess. But we will have to wait and see. I do not see this situation lasting for more than 4 to 6 weeks.
- Avneesh Sukhija:** On Slide #10 you actually mentioned that there could be a possibility of a rate cut in the second half?
- N. Sivaraman:** Yes, it is on the back of inflation expectations which should start improving in the second quarter. Given the growth rate as of today, it will have to happen sooner than later.
- Moderator:** Thank you. Ladies and gentlemen, that was the last question. I would now like to hand the conference back to the management for closing comments.
- N. Sivaraman:** Thank you for all the questions. I hope there is sufficient clarity on the results and also on some of the other strategic initiatives that we have put in place. Do feel free to write to us in case you have any other questions or contact our concerned people and they should be able to provide you with a quick response. Thank you for participating.
- Moderator:** Thank you very much members of the management team. Ladies and gentlemen, on behalf of L&T Finance Holdings, that concludes this conference.