



IL&FS Investment Managers Limited

“IL&FS Investment Managers Limited Q3 FY12 Conference Call”

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Moderator:

Ladies and gentlemen good day and welcome to the IL&FS Investment Managers Q3 FY12 Analyst Conference Call hosted by Genesis Burson-Marsteller. As a reminder, for the duration of this conference, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference please signal an operator by pressing "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. At this time I would now like to hand the conference over to Dr. Archana Hingorani. Thank you. And over to you ma'am.

Dr. Archana Hingorani:

Good afternoon, everybody, and thank you joining us. We here today to discuss the Q3 December end numbers for IL&FS Investment Managers Limited. For the quarter we have booked Income of Rs. 57.2 crores with a PBT of Rs. 22.3 crores and a PAT of Rs. 18.6 crores. The PAT is 13.5% higher than like period last year. Primarily, the income has remained stable vis-à-vis similar period last year. Four or five factors despite known fund raises, the plus factors are the fact that our joint ventures and subsidiaries are performing a whole lot better. We have controlled employee cost for the year. We also have had some foreign exchange positive impact due to the fluctuation in the Rupee-Dollar. On the minus side, we are on the road to raise funds so there are costs linked to that, we have also been exiting some of our investments on few funds and the management fees have been coming down and this is also important because it creates track record, but overall net-net because of both pluses and minuses on the Revenue and Expense side. We are pretty much at the same level in terms of Revenue as last year, but have a 13.5% improvement in profit, that is on the numbers.

In terms of the funds that we manage as you all know, we are in three verticals; Growth, Real Estate and Infrastructure. In Growth, we have two funds; the Leverage India Fund which is in exit mode and is expected to harvest five exits in the next two quarters. We have the Tara India Fund which is fully deployed and is right now in monitoring mode, and the Tara portfolio is not yet matured to start talking about exits, but probably end of FY13 onwards we would also see exits in that portfolio. There are two Real Estate Funds; Fund I which is 2005 Vintage which is in construction and exit mode. In fact, during the last quarter, we have had overall in the Real Estate portfolio one full exit and four partial exits. And in the Real Estate Fund II which is in deployment mode we are fully committed. All our investments have been committed, we are right now investing that amount. There is no fresh money available in the Real Estate category or in the Growth Private Equity space.

In the Infrastructure space, we have one small fund which is in exit mode and we expect a couple of exits in the next two quarters. We also have a large fund which is an Asia focused fund is currently in investment mode and approximately \$200 million is yet to be invested other than that everything has been committed. As a result of this you will notice that we need to raise fresh capital which we have been on the road last year for Growth and in the next fiscal we would be planning to raise fresh money both in the Real Estate as well as the Infrastructure space. That is all from my end. If there are any questions we will be happy to start with that.

- Moderator:** Thank you very much. We will now begin with the question-and-answer session. Our first question is from the line of P Sachdev from Aadhar Securities, please go ahead.
- P Sachdev:** Hi, could you throw some light on the recent Real Estate deals particularly the Indiabulls Real Estate one and also the potential exits going forward?
- Dr. Archana Hingorani:** I will talk about potential exits, I will not talk about individual transactions as we are bound by our contractual obligations to each of the investee companies, but as you can see, we are in deployment mode. In terms of exits as I mentioned earlier, again here I can't mention all the details because they are all partial exits. In our Fund I portfolio there are some mature assets, they have started throwing cash, we have started to see some reverse capital coming from them and therefore there have been three partial exits in Fund I. Similarly in Fund II, we have been able to partially exit two of our investments, and in this coming fiscal we should be able to do another 3 or 4 in the Real Estate space. So we are going to see a spate of exits, but because of the way our portfolio is largely residential in nature, the cash flow determines the amounts that come in and it will always been in trickles it won't have one full exit happening at one shot. So this quarter as well as next fiscal we expect a similar pattern.
- P Sachdev:** And any idea of the quantum of exits in Fiscal '13?
- Dr. Archana Hingorani:** It is difficult to say, but I would expect that we would have exit from the Real Estate space to the tune of about \$100 million.
- P Sachdev:** Okay, coming back to the first question, I understand that you are bound by certain obligations regarding deals, but are these purely Equity deals or you have some minimum guarantee or buyback from the promoters as well?
- Dr. Archana Hingorani:** No. Please understand that we are in the space of Equity, so our deals are Equity structured. We don't have any mezzanine kind of structures in our Fund.
- Moderator:** Thank you. Our next question is from the line of Ashi Anand from Kotak India Focus Fund, please go ahead.
- Ashi Anand:** Archana, I have a few questions, first of all, if you just look at the cost side, Legal and Professional Expenses and Other Expenditures have gone up quite significantly. I understand this is probably linked to the new fund getting raised. If you could just give some more color on why these costs have gone up so significantly and are these likely to sustain or are these more transitory in nature?
- Manoj Borkar:** Actually, if you look at the QoQ thing there is a slight increase in Legal and Professional Expenses mainly because we have couple of funds which are currently in the market, mainly the Tara India-IV as well as the PIPE fund. So all the legal documentation including setting up of the offshore vehicles and all is a one-time process which goes on, and as we go along getting investors we will get into the documentation mode and there will be certain costs which will be incurred. However, the understanding always in a fund is as and when these funds are raised and

the fund announces its 'First Close' you are eligible to recover certain Legal and Professional Expenses and other costs from the fund. So as an accounting policy the expenses are first written off as and when it is incurred and the 'First Close' of the fund we can recoup these expenses back.

Ashi Anand: Okay, so you have some of an exceptional income also in line with these costs as and when the closure happens?

Manoj Borkar: Yes.

Ashi Anand: And how about on the 'Other Expenditure' side that we have also seen a reasonable ramp-up?

Manoj Borkar: The 'Other Expenditure' on a QoQ may not be fully comparable because if you recollect in the last year of December 2010, we had completed the acquisition of Saffron, and accordingly in that quarter impact of five month had actually been reflected, because it was effective from August 1st and the five-year impact was recorded in the expenses also for Saffron in December 2010 quarter.

Ashi Anand: Sure, but if I don't look at the December 2010 quarter, I look at the second quarter the current financial year, even compared to that this is kind of quite a sharp increase it was as in the 45 crores last quarter has become 63.8 crores in this quarter. Just trying to understand, this is something should be modeling going forward or is this again something which is linked to what could possibly be the one-time cost linked to the raising of the new funds?

Manoj Borkar: Like-to-like QoQ basis it is mainly because of the travel cost on account of the new funds and subsequent impact is again more of an accounting through the consolidation of the joint venture, mainly the offshore joint ventures that we have with Standard Chartered will get consolidated. So that impact of grossing up happens on both the Income side as well as in the Expense side.

Ashi Anand: Okay. If you could just move to the second question, just wanted to understand how our fund raising is going given the environment which is fairly difficult. So can you just go through, I think you were talking about three funds you were looking at Tara-IV, Milestone JV and the PIPE Fund?

Dr. Archana Hingorani: Milestone JV, as you know, because of the equivalent of a force majeure event given the passing away of Mr. Arya that fund raising has been stopped obviously because he was part of the key man, we have garnered \$70 million approximately, which is higher than the numbers that we had let's say prior to that event. So we have closed all discussions on future money. So \$70 million has come in and that is being deployed. So that is on the Milestone side. On the Tara side as we had mentioned the last time we have 'first close' investors available to the tune of \$42 million. It includes international as well as domestic investors. We have started discussion and we are coming to a closure with local banks and institution, so we expect to be able to increase that but as of date that number stands at \$43 million is what we have actually garnered vis-à-vis the plan. So our expectation is that in this quarter we will be able to get some more domestic institutions

and once that happens, it is very important that the domestic institutions come in because they are old investors and all international investors even though they are sitting on the fence because of may be the Europe issue or the India related issues, you know there are so many of them. It is very important to get the Indian investors also so that it gives greater confidence. So that is where we are on Tara-IV. PIPE Fund has started relatively later in terms of its marketing and we are currently in active marketing mode and that results of even first \$50 million closing probably will happen around the first quarter of next fiscal.

Ashi Anand: Okay, but just given the environment what we are hearing from your LPs, are you confident of being able to achieve a second close and what could be the targets in Tara Fund-IV and PIPE Fund --?

Dr. Archana Hingorani: As of now we have not pulled down targets of either fund. I expect once you have the first close for Tara, especially because we are now trying to also showcase potential investment which is an added criteria that investors have brought into their evaluation exercise and they would like to see what kind of assets are being funded. We do expect to be able to meet that target of \$300 million. On the PIPE side our expectations are anywhere between \$200-300 million and again based on what the investors who want to come in, into the second close, not the first close but the investors who are ready for the second close, one would expect that we should be able to meet the \$200 million number.

Ashi Anand: Okay, and just in terms of are we getting any pushback from the cost structure and are we moving away from the 2-20 towards the lower fixed or any other such changes on the cost structure?

Dr. Archana Hingorani: I think more than pushback, according to our analysis, it is more of opportunistic negotiation at this point in time, and there are a lot of investors who are willing to put in money at a fee that is not sustainable. Now, of course, those kind of transactions are available and one could take those up and close the fund but that is not what we want to do. So, we, as of now the investors that we are talking to, the ones that who have already committed and the ones that are planning to commit, there is definitely no pushback on the 20 model, there may be some pushback on the fee, but again it is a function of what is the amount. If he is a \$5-10 million investor he is not negotiating on the fee. My expectation is that if he is a \$30-40 million investor, then yes, like we have in the Infrastructure and Real Estate funds already that trend has already been established that if you are larger you will be charged a lower fee. You are seeing a similar trend on the Growth side also.

Ashi Anand: Okay, but so the reduction in fee that on an overall fund basis would remain within the 25-40 bps kind of impact?

Dr. Archana Hingorani: I would expect that should be maintained because Growth funds are not of a very large size. So in order to be able to make it cost effective, you can't really go down significantly on the fee piece.

- Ashi Anand:** Sure. Just a final question from my side. You have spoken about exits in both LIF and Real Estate Fund I and that continues right now and going to next year also. But if you really just looking at the carry coming through given the environment right now would it be fair to say that unlikely to see any large carries from LIF until FY14 and RE Fund I for FY15, are those good kind of benchmarks you think?
- Dr. Archana Hingorani:** I think fair to say that on RE Fund I FY15, but I think on LIF we are going to start getting into carry somewhere around June/July of this Calendar Year. So my expectation is that we should start seeing consistent carry QoQ once we reach that June/July benchmark.
- Ashi Anand:** Okay, RE will fully start seeing trickling in 2015.
- Dr. Archana Hingorani:** The significant amount. Your question was will it be significant? So I am going with that word.
- Moderator:** Thank you very much. Our next question is from the line of Arpit Ranka from Tactica Capital Management, please go ahead.
- Arpit Ranka:** Hi, ma'am, this is Arpit from Tactica. Just a couple of questions; just trying to understand the life of the key funds that we have. One, being for example, Real Estate Fund II which we raised in 2007, if you could just throw some light on when you will probably enter the exit phase on this Fund?
- Dr. Archana Hingorani:** Fund II is actually right now in deployment mode but because we started 2007-08 in terms of investments there are some transactions that are already showing exit capacity. So therefore in the last quarter there are two on the Real Estate Fund II side where we have had partial exit. I can see in Real Estate because we are predominantly in the residential space, it is all a function of sales and excess cash flow. So we are starting to see exit start in Fund II even today, but bulk of the exit should be starting probably sometime in FY14.
- Arpit Ranka:** And typically we have a period of 2-3 years in which we are sort of try to run through the exit, is that correct?
- Dr. Archana Hingorani:** Yes, as this Fund ends somewhere in December 2015, so we have another 3-1/2 years of life to be able to exit out these investments.
- Arpit Ranka:** So when we say it comes to an end in 2015 what you mean to say is the fee that is accruable to our company sort of stops around that time and it is not necessary that all the exits would happen and we will be able to close the fund by then?
- Dr. Archana Hingorani:** The answer is 'yes,' fees will start trickling down to whatever is left, but the fund life is still December 2015, and if one is unable to exit all our investments by then we do get two extension period. So we can go up till December 2017.

- Arpit Ranka:** Okay, and in terms of JV we have with Standard Chartered where we have reached about \$650 million in 2008. What would be the timeline for that? Just trying to understand the cash flow visibility for the management company there.
- Dr. Archana Hingorani:** It is a 8-year fund was raised in September of 2008 so it goes till 2016.
- Arpit Ranka:** Okay and coming to exit you said that in the recent quarter we have had one full exit. If you can sort of share this info, what would be the IRR on the exit be? We are just trying to get a sense as to how conducive is the environment for the exit at this point in time?
- Dr. Archana Hingorani:** While you know the environment is not conducive at all, but again it shows a residential project invested in early 2006, this was a joint venture with AIPL Ambuja where we have been able to completely exit post starting phase and completing three years of investment, etc. the return has been 17.5%.
- Arpit Ranka:** Okay, just one final question in terms of portfolio structure typically, how concentrated are the bets that we end up making for each fund? For example, what would be the largest investment for any even fund and one particular investment and how?
- Dr. Archana Hingorani:** Typically, all funds will have requirements that we cannot invest in more than 10% of Fund size and by exception maybe one investment can be 15% of Fund size. In most Funds you will see that we don't normally cross the 10% threshold.
- Arpit Ranka:** From the risk management perspective just trying to understand across the Funds, the top five investments, what would be the portfolio concentration in terms of total assets being deployed in those five opportunities --?
- Dr. Archana Hingorani:** It will not go beyond 35-40%.
- Moderator:** Thank you very much. Our next question is from the line of Anuj Anandwala from PPFAS, please go ahead.
- Anuj Anandwala:** Firstly, could you just provide me with breakup of the Saffron top-line, bottom-line for the current quarter or nine months?
- Manoj Borkar:** The Saffron, top-line for the quarter is around 9.8 crores and after all the amortization and other costs we have had a profit of around 2.6 crores.
- Anuj Anandwala:** Secondly, you have been making partial exits in the first quarter of the current fiscal. How does this affect earning AUM? I guess it was 2.4. What would be the net earning AUM after this quarter?
- Manoj Borkar:** This has marginally gone down because the way the fees are earned or on the capital that is invested in today's particular company's divestment it would have gone down by \$0.4 million.

- Anuj Anandwala:** So would it be around 2 Billion?
- Dr. Archana Hingorani:** No, it will be around \$2.4 Billion, it has only gone down by \$0.4 million.
- Moderator:** Thank you very much. Our next question is from the line of Arpit Ranka from Tactica Capital Management, please go ahead.
- Arpit Ranka:** Hi ma'am, just one more question in terms of understanding the outlook on earnings AUM. Because it used to be about 3 billion and a few quarters back it used to be 2.6 billion, now it is 2.4 billion. So given the difficulty everybody in the market is having sort of replenishing their funds what sort of sense you have in terms of trend for AUM going forward, if you could just sort of share some thoughts on that?
- Dr. Archana Hingorani:** Yes, you are right, you have been seeing last three quarters our early results were quite good, we got the \$40 plus million almost 4-5 months back, since then there has been no additional money is coming in. So, that is an indicator of how difficult it has been. It is not just because of the sector that we are in but also because we are dependent on international markets, largely for funding which they themselves are not doing well. And you have the India story which has been quite disheartening and you compare with the China which has been giving 22-23% return. The on a comparative basis people have been rethinking. If you see the kind of investors we are interacting where you find there are two buckets, where you can place investors; one, who want to invest but are being very, very cautious and would like to see other big investors coming before they put in their money. So, those are the cautious kind and the other investors are the ones who are saying that, "Okay, in this environment where the whole world in a particular situation, we are only interested in participating in distressed transactions." None of our funds are of that variety where we can rely on either of those sources of capital. So the LP base that would normally cater to something like what we do is obviously significantly cautious and therefore there has been slowness, but given the fact that in the next fiscal we do need to raise capital in all pockets, give or take, I don't think we can probably in the next six months or so you would see all funds would be out on the road. Our expectation is that during the fiscal at a minimum we should be raising about \$400-500 million.
- Arpit Ranka:** In the next six months you are saying?
- Dr. Archana Hingorani:** Six months.
- Arpit Ranka:** Okay, in that sense we don't expect the earning AUM sort of trickle down further from these levels provided we manage to be successful in raising some capital over the next few months.
- Dr. Archana Hingorani:** Correct.
- Arpit Ranka:** And following that in terms of line base if you are to sort of give a sense of how geographically diversified they are? For example, what percentage of total capital is coming from US, Europe, and India and things like that, if you could just sort of give us some...

Dr. Archana Hingorani: It is different across categories. For example, Real Estate is significantly the money come from the US markets, I would say, nearly 70-80% of capital would be US-based, remaining coming from Europe, Asia and the Middle East. On the Infrastructure side it is the reverse. Most of the money comes from Europe, Asia, and Middle East and a very little from the US. And on the Growth Private Equity side, it is mixed, they are all small amounts, so they come from various parts of the world; I think it is evenly spread across US, Europe, Japan, Middle East, Singapore, etc.

Arpit Ranka: So very little money coming in from domestic fund?

Dr. Archana Hingorani: Domestic, as you know, as a comparison even if how much ever you put in you are always going to be 1/50th of the international money, right because of the exchange rate. There is no institutional capital readily available. The only people who are allowed to invest into private equity without significant restrictions are insurance companies. Out of which there are only two; LIC and GIC who have cash flow to be able to participate. Other banks who used to participate, let us say in 2004-05 the trend was different. We saw significant contribution driven from banks but that has changed because of their own provisioning norms and requirements of RBI, which sort of discourages them from doing unlisted locked-in investments where they have to QoQ have a evaluation mechanism. So there are not too many banks that are happy to participate in private equity. They understand the need for it and therefore will give small amounts of capital but there is no concerted strategy by the banks to say that I would like to diversify my earning base to also include alternative asset.

Moderator: Thank you. I would now like to hand the floor over to Dr. Archana Hingorani for closing comments.

Dr. Archana Hingorani: Thank you all for joining the call. As you can see, while we have made a lot of progress on investments as well as divestments, fund raising continues to be a significant challenge and that is what is the focus of the company. Over the next 6-9 months, you are going to see significant amount of efforts being made to augment the AUM, and we will hopefully come back with greater insight as to how we can complete that in the next quarter. Thank you.

Moderator: Thank you very much. On behalf of Genesis Burson-Marsteller that concludes this conference call. Thank you for joining us and you may now disconnect your lines.