"Cholamandalam Investment & Finance Company Limited Q1 FY2020 Earnings Conference Call"

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**Moderator**: Ladies and gentlemen, good day, and welcome to the Cholamandalam Investment and Finance Company Limited Q1 FY20 Earnings Conference Call, hosted by Kotak Securities 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, please signal an operator by pressing "*" then "0" on your touchtone phone. I now hand the conference over to Nischint from Kotak Securities. Thank you, and over to you, Sir!

**Nischint Chawathe**: Welcome to the Q1 FY20 earnings conference call of Cholamandalam Investment and Finance Company Limited. To discuss the financial performance of Chola and to address your queries, we have with us today Mr. Arun Alagappan, Executive Director; Mr. Arul Selvan, Executive Vice President and Chief Financial Officer; Mr. Ravindra Kundu, President and Business Head, Vehicle Finance; Mr. Rohit Phadke, President and Business Head, Housing Finance; and Mr. Rupinder Singh, Senior Vice President and Business Head, Home Equity.

I would now like to hand over the call to Arun Alagappan for his opening comments

**Arun Alagappan**: Good morning, ladies and gentlemen. I have great pleasure in presenting to you the quarter ending June 2019 performance of Chola finance for the financial year FY20.

At the outset, I am happy to state that we ended the quarter with a business asset base of Rs.57494 Crores, registering a growth of 27% over the last year. The company has adopted Ind AS 116 leases during the quarter and has recognized operating leases on balance sheet.

The following highlights from Q1 FY 20 performance reaffirms Chola's stedfast growth despite the prevailing adversities in the external market.

Aggregate disbursements for the quarter ended June 2019 were at Rs.8572 Crores as against Rs.7014 Crores in the same period over the previous year, registering a growth of 22%. PBT for the quarter ended June '19 was at INR 484 crores as against Rs.439 Crores last year, registering a growth of 10%.

Business assets under management stood at Rs.57494 Crores compared to Rs.45361 Crores last year, registering a growth of 27%.

Assets under management, including investments, grew 35% from Rs.46709 Crores to Rs.62827 Crores.

PAT stood at Rs.314 Crores for Q1 FY 20. The PBT-ROTA for Q1 FY20 was at 3.4%.

ROE was at 20% in Q1 FY20 and book value is up by 20% to Rs.83 per share as of Q1 FY20 from Rs.69 as at Q1 FY2019.

We have increased our branch network to 999 branches out of which 80% are in Tier 3, Tier 4, Tier 5, and Tier 6 cities. We are well on our way to reach 1200 branches by the end of this financial year.

We have maintained our continued focus on our efforts to reduce the nonperforming assets. As per Ind AS, our Stage 3 asset at the end of June 2019 was at Rs. 1671 Crores as compared to Rs.1617 Crores as on FY2018. Stage 3 percentage to total gross assets stood at 2.97% in June 2019 compared to 3.57% in June 2018.

Coverage ratio for the Stage 3 improved to 36.2% as of June 2019 from 34.3% in June 2018. We continue to hold Rs.50 Crores as micro provisions and as per I-GAAP GNPA at the end of the Q1 FY2019 was at 2.6% compared to 3.1% at the end of Q1 FY2018.

In absolute terms, the GNPA as of June 2019 were at Rs. 1517 Crores as compared to Rs.1448 Crores as of June 2018.

Provision coverage ratio was at 46.8% in Q1 FY20 as compared to 43.9% in Q1 FY2019.

Let me also share with you the business level performance of Vehicle Finance and Home Equity divisions.

Vehicle Finance has delivered a performance with an all-round improvement in disbursement, asset growth, profits and reduction in delinquencies. The vehicle business grew by 21% in terms of disbursements and 28% in terms of closing assets year-on-year. The business recorded a PBT of Rs.319 Crores as against Rs.275 Crores last year. ROA is at 3.1% level.

Over the years, the VF business has diversified its loan book to include products across the spectrum in the automotive sector. In the prevailing scenario of slowdown in the HCV and Car segment such diversification has helped maintain the asset growth by leveraging the product mix in other product segments and focusing on the Used Vehicle business. Adequate liquidity with your company shall continue to support its asset growth in Vehicle Finance throughout the financial year FY20.

Moving on to Home Equity business: the Home Equity business grew disbursements by 17% and PBT by 48% year-on-year. The business recorded a PBT of Rs.84 Crores for the year ended June 2019 as compared to Rs.57 Crores last year. Higher recoveries in NPAs supported in the growth.

The Home Equity business has been able to improve its ROA level to 2.8% for the quarter ended June 2019 as against 2.2% last year.

Recoveries continued to be good leveraging SARFAESI, resulting in higher profitability in this business.

The company's capital adequacy ratio as of end of Q1 FY20 was at 17.16% with Tier 1 at 12.86%.

In order to mitigate the tight liquidity conditions, Chola has been carrying high levels of liquid cash from the second quarter of last financial year and has continued to do so during the current quarter as well. The liquid assets as of June 2019 were held in fixed deposits were Rs.4753 Crores and balance of Rs.591 Crores in cash and current account balances with banks. Though this resulted in a negative carry and had adversely affected the net income margins during the quarter, we had pursued this action as a conservative measure.

In the upcoming quarters for FY20, we look forward to continue on our growth trajectory and ensure value creation for the shareholders. Thank you all for attending the call. My colleagues and me, would be happy to answer any queries now.

**Moderator**: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Kunal Shah from Edelweiss. Please go ahead.

**Kunal Shah**: Congratulations for a good set of numbers. Firstly in terms of the overall growth, if you can highlight in terms of definitely this quarter has been better for us, but looking at the underlying auto sales, if you can give some colour in terms of what is the outlook are with respect to the overall disbursement growth and any particular pockets wherein we are concerned about and we are seeing some maybe the competitive dynamics coming up and we are going to benefit in any of the product segments?

**Ravindra Kundu**: Good morning to all of you. See, we have already mentioned in the last earnings call in the Q4 itself that we will be trying for 15% disbursement growth and luckily we have achieved 21%. The disbursement growth has come because we have got the benefit from the used vehicles more and we will continue to expand the product which we have been continuously feeding for quite some time like two-wheeler, three-wheeler, and tractor and construction equipment. And their market share is in nascent stage and if you increase little bit disbursement growth can come. So we are hoping that we will maintain this growth trajectory in the coming quarter as well.

**Kunal Shah**: Sir in terms of this kind of a mix you said towards the used vehicle, do we see overall yields also to be relatively better off?

**Ravindra Kundu**: Come again.

**Kunal Shah**: Should we see the yield improvement as well given the mix shift towards the used vehicle, tractors and all of that?

**Ravindra Kundu**: That is the objective. If you see that our NIM is still lower than last year Q1 which is 10bps at yield level and 20 bps at the cost of fund level. So we want to basically give the gap of that 10

BPS and hopefully by Q4 our yield will be higher, book yield will be higher than the previous corresponding quarter of the previous year.

**Kunal Shah**: Lastly in terms of the branch expansion, it is still quite significant in this particular quarter. So any locations I think may be broadly the spread across the regions have been maintained and even between the rural and semi-urban areas have been maintained. So first is maybe why we are looking at this kind of an expansion in the branches. Are we too positive or maybe we are seeing the competition coming down and that is the reason we are expanding. So what is the entire rationale behind certain aggressive branch expansion?

**Ravindra Kundu**: We have mentioned in the past also that we have a concept of putting up resident location and once the resident locations start delivering, say, Rs.40 lakhs, Rs.50 lakhs, we give them small premises, which is nothing but by putting up the infrastructure of worth Rs.5 lakh and the person who basically working as Location Resident Executive, he might become a Branch Manager or we shift somebody from the hub. It is like moving from the district level to taluka level or taluka level to block level. We are opening these branches within the area where we are operating mostly, because across the country we are present over there. There are few states we are not present over there. Otherwise, the branches are getting into the deeper location. And if you open up the branches, then it is better to do the collection, we can collect the money by traveling 20, 30 kilometers from the branch to customer place and that helps us to collect money. Second important is that customer service improves. Customer can actually come to our office so both put together without increasing much of opex, we are putting up our branches and these branches are being opened up only after getting the result.

**Kunal Shah**: So these are mostly in the existing locations?

**Ravindra Kundu**: Existing hub, the expansion of hub to Spoke locations

**Kunal Shah**: This would be both vehicle and Home Equity. So there is no specification in terms of where the concentration is more with respect to the new branches getting added?

**Ravindra Kundu**: So we open up first, then they come later because they are in 250-odd places. So they are going based on their strategy. Definitely, all the branches are co-located.

**Kunal Shah**: Thank you.

**Moderator**: Thank you. The next question is from the line of Sanjay Shah from ASA Securities. Please go ahead.

**Sanjay Shah**: Good morning gentlemen. Congratulations on good numbers and really maintaining the asset quality too, Sir. Sir, I read one very nice quote in your presentation. The fundamental principle of economic activity is that no man you transact with will lose then you shall not. Sir, can you highlight because we see the economy in such a doldrum and we have been growing in a segment where the OEs are bleeding. So what has gone so well? Sir, I will put this question to Mr. Kundu, Ravindra Kundu, Sir. Can you highlight have we gained some wallet share? Or would we get a good business and what went so well for us?

**Ravindra Kundu:** See in the country, we believe that more than financing, it is collection is the main business for us. So our 80% time is spent on collecting and understanding the market where we should fund, which customer we should actually focus on, what make-models we should focus on and how many manpower required for collection. Our collection is done by in-house team and we have more manpower in collection than sales because we are also operating into the rural market. Therefore, we have been focusing this as one of the important aspect of our business. So starting from origination to doing underwriting to infant delinquency management as a collection mechanism, we have been fairly using lot of analytics, lot of manpower and also using lot of our effort and time to ensure that our collection is actually on top. And that has helped us to ensure our NPA at this level. And we are expecting that we have started this year much better and if we continue to do this kind of collection, our portfolio will further improve by the year-end.

**Sanjay Shah**: That is great, Sir. Sir, can you highlight on construction equipment business? How it is growing? What is the size right now? And what is your expectation on that?

**Ravindra Kundu**: Construction equipment, we are doing it selectively. We are not doing it across all application and across all make model, there are selective make model, we have selected out of the application. Construction equipments is a vast product actually, if you see that it has got excavator, back-hole loader, compacter, road builder. So we have selected top of each application, one item on one, one brand and we are focusing that. As of now our closing asset of construction equipment is Rs.2394 Crores and we are doing very well with respect to that, but we are not growing aggresively. We are growing slowly in terms of our construction equipment, if you see that, our disbursement growth has been 10%.

**Sanjay Shah**: How much Sir?

**Ravindra Kundu**: 10%. Construction equipment disbursement has been 10%, our disbursement growth has been 10% over the same quarter last year.

**Sanjay Shah**: And how do you see the future of that.

**Ravindra Kundu**: As of now, if you see, in the month of, in the Q1 the construction equipment number has come down significantly in terms of our overall industry side and it will pick up only when there is a mining activity improves. As of now it is actually down, but hopefully from Q4 onwards we can see some improvement, but the overall correction will come only after 1 year.

**Sanjay Shah**: Thank you and good luck to you Sir.

**Moderator**: Thank you. The next question is from the line of Shubhranshu Mishra from Bank of Baroda Capital Markets. Please go ahead.

**Shubhranshu Mishra**: Good morning. Thanks for the opportunity. My first question is with regards to your employee increase that's roughly around 3,000 on a Q-o-Q basis. How do I read into that and what is the split of incremental employees into sales collections and operations?

**Arul Selvan**: We have increased our branch network in this quarter by around 100 branches. There we needed to put people also we have strengthened our collection and sales team especially in the context that we are going into low ticket items which is like two wheeler etc. We need to put more the manpower behind this. So we have reshuffled our teams both on the sales side and the collection side and we have done. The predominant part of this increase is in the vehicle finance business more focused on the north and the east side of the geographies.

**Shubhranshu Mishra**: The second question is with regards to your Slide #64 where you are defining LGD and PD according to various categories? So I just wanted to understand your LGD and PD assumptions for the Home Equity business for Delhi, Tamil Nadu and Gujarat if you can give it to me?

**Arul Selvan**: See what will happen with LGD across these segments which are kept constant because actually we do not have any crystallized losses in any of these regions. What we are trying to do with this segmentation is only to arrive at the PD. The PDs are different for each of these because the way how it moves on into 90 plus is different. And, of course, as you know, the north side is slightly higher and that is why we have made this segment separate. But LGD we are following the 20% norm, which is given when you do not have LGD practically then you need to adopt the 20% norm. This is as per one of the guidelines given by us in last quarter. So that is what it is.

**Shubhranshu Mishra**: So what is the PD assumption for Delhi, Tamil Nadu and Gujarat Sir?

**Arul Selvan**: I will not be able to share individual numbers because I think these are not shared by anybody in the industry also so I think right now we would refrain from it.

**Shubhranshu Mishra**: One last question with regards to a data point Sir. Your result update PDF that says an AUM of 62000 Crores versus the investor presentation which is that on 57000 Crores so what am I missing here?

**Arul Selvan**: See the 62000 Crores is including the cash balance, which is because that also forms part of the investment. The 62000 cr has got cash and bank into it, whereas the 57000 Cr does not include the cash and bank. The cash and bank is 5000 Crores. **Shubhranshu Mishra**: Thank you for the opportunity Sir. Best of luck.

**Moderator**: Thank you. The next question is from the line of Utsav Gogirwar from Investec. Please go ahead.

**Utsav Gogirwar**: Thanks for the opportunity Sir. Just couple of questions from my side. Can you just, let me know if we have increase yields under home equity and vehicle finance segment in this quarter and if yes, that then how much?

**Arul Selvan** : The Home Equity yield have been increased across the bookearlier and right now it is trending in the range of around 11.7% overall. The Vehicle Finance we have selectively increased yields in different product segments, in the high yield product segments, the increase has been moderate and then the low yield segments we have increased, and increased the rates to the extent of anywhere between 30 and 70 basis points across various products, but in the Vehicle Finance segment the impact of these will be reflected in the March quarter because the existing book continues with that rates at which they were disbursed because this is a fixed rate book.

**Utsav Gogirwar**: Sir my second question is on the employee expenses, so we have done lot of branch addition and employee addition this quarter but if I look at year-on-year growth is just 3%. So what am I missing here, why it is 3%? Is there any one off element?

**Arul Selvan D**: The employee addition is more on the feet on street. The feet on street does not reflect in the cost as the salary because the feet on street actually are employed in a separate company which is the Chola Business Services, but we service only to Chola predominantly. So that comes under the outsourcing cost. It might have been in the group under Other Expenses that is where you see the increase. And the other factor is the incentive rate to them get amortized in line with the Ind AS norms. So only the fixed salary gets charged off fully, the incentives get amortized. As you know the fee income on the other side is getting amortized so these two generally net off. Earlier we being in the I-GAAP, we were charging the full expenses in the expenses and recognizing full fee. But now fee is also amortized on the income side and the expenses part on the incentive gets amortized and this incidentally is also netted off in the income line again as per Ind AS because Ind AS requires us to net it off with the income. So that is where the expenses may not reflect this increase.

**Utsav Gogirwar**: Sir just last question. If I look at the sale of services that has not grown compared to the disbursement growth this quarter?

**Arul Selvan D**: The sale of service is the one time sort of an income more like an advertisement income that we could get from some of the other companies who use our branches for selling their products, so this income when we entered into last year we had a small upfront income coming in to meet the initial cost of making some changeovers in the branches. So there was a small part of it as an upfront and the rest is like a five-year contract which they will use, our premises to advertise their product. So the rest of the period in last year as well as in the current year it is the monthly income that comes to us.

**Utsav Gogirwar**: Thank you Sir.

**Moderator**: Thank you. The next question is from the line of Piran Engineer from Motilal Oswal Securities. Please go ahead.

**Piran Engineer**: Congrats on the quarter. Just a couple of questions. Firstly on the macro front, can you comment on the trajectory of freight rates and fleet utilization? How that has been trending because it seems that, that has been on a downward trajectory in the last couple of months?

**Ravindra Kundu**: Yes. That is correct. That is the reason if you see that heavy commercial vehicle sales have come down significantly and that is one of the reasons for us not to participate in heavy commercial vehicles.

**Piran Engineer**: No I mean more in terms of cash flows for your customers?

**Ravindra Kundu**: Yes. I mean, what you are saying is applicable more to the heavy commercial vehicle, not the light commercial vehicle, those who are utilizing it within the state or operating it for vegetable transportation, autos or consumer goods transportation. The customers who are into the long haul, the customers who are transporting goods from Chennai to Manesar or Ahmedabad to Kolkata, because the IP has come down or the production is not happening. Therefore, obviously, load available for these customers are less than what it used to be one year back. And that is the reason heavy commercial vehicle, especially the medium fleet operators are under stress. The small road transport operator who can redeploy their vehicle from one route to other route, one product to other product they are able to manage their show. And we see that the heavy commercial vehicle as of now, the number of visits required for collecting EMI has significantly gone up. But in terms of light commercial vehicle and small commercial vehicle, still things are actually going on. Overall, economy is not doing well. That is the reason it is impacting even lights and small as well. And it is also across urban and rural. Therefore, there is a tight situation in terms of repayment of the customer. But we see that because we have taken utmost care in terms of sourcing such customers, going by make model, going by our historical data, we have been successfully collecting the money as of now. And therefore, we see that our target equity is still lower than the last year's Q1.

**Piran Engineer**: But in the past in previous cycles have we seen that this happens in HCVs with a lag it also happens in LCVs?

**Ravindra Kundu**: Provided agricultural growth also not there. It has happened in 2012-2013 when GDP was down for two years and then it was also supported with low agricultural growth for two years. And we saw that lights and small also had a problem in 2014 and 2015. This year at least in spite of monsoon is late, we are seeing that monsoon is picking up and the deficit is coming down and hopefully this will be better year also.

**Piran Engineer**: Okay. Sir secondly on cars. In our cars portfolio, we have grown disbursements 40%. If you could just talk a bit more on who are our key OEMs? What is our trajectory out there, the yield on that business? And how are we just really growing so much faster than the industry?

**Ravindra Kundu**: One is that because of the lower base. Base effect is important. For example, our Car MUV we put together we focus more mainly Maruti, Mahindra and to some extent Hyundai. So Car MUV put together, our market share was 2%. Now, it has gone up to 3%. So it is because of the base effect mainly and this entry level car or MUVs, which is mainly utilized in the rural market because of the branch network and because of our penetration in those markets, we are able to do it and we are focusing only Mahindra, Maruti and to some extent Hyundai.

**Piran Engineer**: And what is our yield in this business?

**Ravindra Kundu**: Yes, it is good actually.

**Piran Engineer**: How do I read good like 14%, 15% or is it…

**Ravindra Kundu**: No, no, no segmental we do not disclose but it is better than HCV which I can tell you.

**Moderator**: Thank you. The next question is from the line of Rohan Mandora from Equirus Securities. Please go ahead.

**Rohan Mandora:** Good morning Sir and thanks for the opportunity. Sir, given that there is some slowdown on economy we are adding new branches. Sir, I just wanted to understand like what kind of an opex to average assets we should expect from next 1 and 2 years that was one? And secondly, if you would share the Stage 2 and Stage 3 in used vehicles and also incremental yields on the new, used and Home Equity?

**Arul Selvan**: So the expense ratio will be at the same levels of around 3% and we expect it to improve in the sense, reduce as we grow the assets because of the expansion in most of the expenses in the branches we have incurred so far and the next date of branch increase is, I think, mostly at the fag end of the year.

On the Stage I, Stage II, I would not again want to give this. As you know, that many of the industry players also do not give. Right now, we would say that it has not changed. The composition between Stage I and Stage II has not changed drastically between what we have been reporting either for the past quarters as well as past year numbers. What was your last question, sorry I missed it?

**Rohan Mandora:** Incremental yields on new used and home equity?

**Arul Selvan**: The incremental yields on the Vehicle Finance have gone up by around 60 basis points as compared to last year. As per our internal workings, this will start showing up from Q3 onwards in our overall closing efforts. So that yield improvement you will see from Q3 onwards and if the cost of funds by then is either held at the same level or reduced, we will see a drastic improvement in NIM.

**Rohan Mandora:** Right. Sir, one of our competitors like  has also shown good numbers in vehicle finance disbursements. There the incremental yields have gone up by around 140, 150 basis points in the vehicle business and we have increased by around 60, 70 basis points. So just trying to understand like in order to gain market share we are keeping it lower? Or something else is that?

**Ravindra Kundu**: Q1 is typically a school bus season. And during this particular season, when we finance the school buses, school buses are funded at a finer rate because portfolio quality is also fine. And that is what always Q1 is lower. And then Q2 onwards, the yield will go up, Q2, Q3, it goes up and then Q4, it comes down. That is what is the trajectory, and therefore, we are in line with that. So our Q1, marginal yield minus fee has gone up by 62 basis points in this quarter. And in Q2, I think we will do much better than that, so it will go up by 80 basis points or 90 basis points, I'm expecting that.

**Moderator:** Thank you. The next question is from the line of Bunty Chawla from B&K Securities. Please go ahead.

**Bunty Chawla:** Congratulations on a great set of numbers Sir. Sir, on the asset quality front, we have seen slightly increase in the gross NPA per se, so can share how much was due to vehicle financing and how much was due to home equity, because previously what we were riding or what we were seeing there was a good amount of resolution in the home equity per se. On that also, the data point if you can share?

**Arul Selvan**: The asset quality in every Q1, it tends to be slightly moving up as compared to the Q4 numbers. And you can go through the past few years also and you will find the same trend happening and this is what is sort of typically in any year and that is what you are seeing here. As a matter of fact, the extent of spike that happens in Q1, normally, we have been able to control it to a much greater extent over the last year as well as this year. And as compared to earlier years, you will see that this spike or the bounce back on the NPA numbers have been much, much less. Then you need to also see that you would see the similar trends in others in the industry also and I'm sure if you compare the numbers, you will see that the same pattern happens with the rest of the players.

Between Vehicle Finance and Home Equity, the Home Equity numbers have come down actually because we still are leveraging the recoveries on whole of the SARFAESI and these numbers are coming down and that is why we have a reduction. Vehicle Finance has a little bit gone up and that is, as I said, basically seasonal demand. And this trend will start coming down from Q3 onwards. Q2, it will remain flattish or maybe marginal improvements from today. But Q3 and Q4, you will see drastic deductions. This is the trend you can go through the numbers from the past calls.

**Bunty Chawla:** On the data point, in the home equity part, out of 265 Crores under SARFAESI, we have got already 160 to 170 Crores of recovery, so any addition on that during Q1?

**Rupinder Singh**: So on SARFAESI particularly it is around 24 Crores, what we reduced in Q1, so this a trend and going forward, I think it will continue for a quarter or Q2 something like that in the same way.

**Moderator:** Thank you. The next question is from the line of Pranay Rajani from B&K Securities. Please go ahead.

**Pranay Rajani:** Congratulations on the good set of numbers. Just a small data keeping point, if you could just provide the gross NPA numbers for the vehicle finance and home equity segment, that would be great?

**Arul Selvan**: You want the gross NPA or the whole?

**Pranay Rajani:** As per Ind AS Sir?

**Arul Selvan**: As per Ind As the gross NPA numbers is around 2% for Vehicle Finance and around 5.5% for Home Equity.

**Pranay Rajani:** Sir, it is not audible, can u please repeat it Sir?

**Arul Selvan**: Vehicle Finance 2%, this 2% has come down from 2.55% of June 2018 and similarly 5.5% come from 6.7%. 6.7% was the last year same period, it has come down to 5.5%.

**Pranay Rajani:** Thank you so much Sir.

**Moderator:** Thank you. The next question is from the line of Nidhesh Jain from Investec. Please go ahead.

**Nidhesh Jain:** Thanks for the opportunity Sir. Sir, on the growth aspect, given your own commentary is slightly bit concerning on the concerns in the fleet operator and the transport segment and we continue to hear that there is a quite a bit of stress in the SME segment primarily focusing on your HE portfolio. So what gives you confidence of such strong growth of this quarter, given the environment is so volatile and concerning? So are we tracking any forward-looking data points, which give us confidence that the lending that we are doing right now is probably pretty good, the quality of the lending is good?

**Ravindra Kundu**: Yes. See, Vehicle Finance, if you see that, I have mentioned that the capacity utilization and the freight and all is more towards the heavy commercial vehicle, where we are not growing or we degrow by 32% in heavy commercial vehicle as against the industry degrowth of 30%. Our growth has come from the used and as we mentioned that, we have rural branches wherein car financings are also happening; there also we got the growth. And our core product like commercial vehicle, small commercial vehicle, there also we are doing better. In addition to that, we have also improved our market share little lately in tractor, two-wheeler and construction equipment, there is slight amount of improvement. These are happening based on our underwriting models that we are using it and we are tightening our underwriting models time to time. Our early default, infant delinquency is the biggest indicator of how the portfolio is behaving. We are seeing that those parameter like early default nonstarters are actually continuing to coming down. So therefore, we are quite comfortable with this in terms of Vehicle Finance. And if I talk about Home Equity particularly, it has been observed through analytics also that more into the retail size, smaller ticket size, it behaved much better than the bigger ticket size. So focus going forward is more on the retail side as well as moving to the new markets like Tier 2, Tier 3, where the impact of these things are comparatively less. And obviously to track this for future, the important piece around here is again an early default and how the Stage II is behaving, so both of these 2 categories are in control. And it looks like the couple of quarter is where we will be able to maintain the budget what we planned at the start of the year.

**Moderator:** Thank you. The next question is from the line of Antariksha Banerjee from ICICI Prudential Asset Management. Please go ahead.

**Antariksha Banerjee:** Good morning people. Two quick questions. One is on the liquidity front. Can you please help me with what is incremental cost of borrowing you are deploying each instrument at? And this cash balance of Rs.2000 Crores which is increased in this quarter, if the situation prevails the way it is today, how do you see that balancing it out? I mean, are you keeping it as a percentage of your disbursement of your assets? What is the thinking there?

**Arul Selvan:** See, the incremental cost is in the range of around 50 to 60 basis points and primarily this is from the bank lending, where we borrow from the bank. The cash balance the way we keep it is, we try and keep two months of maturity as cash balance or two months of maturities primarily. We are also, on the other hand, evaluating the new guideline, which is given by RBI on the liquid cover ratio and trying to say that in that scenario, how much to keep the adequate cash. While the provisions of that draft guidelines is little onerous, but we feel that RBI will go forward with the same features of what they have asked for because primarily it reflects the Basel III norms. And as they are bridging India's seasoned banks, these MCR conditions may not be changed too much. So we need to build that, and accordingly, we need building this liquid cover ratio by maintaining these high quality liquid assets, so which we do not want to play with various G-Sec, etc., and we want to keep it as simple fixed deposits and cash in hand.

**Antariksha Banerjee:** Okay Sir, so this will remain is broadly what you are saying?

**Arul Selvan:** This will remain more or less at similar level.

**Antariksha Banerjee:** Okay. And the second question is for Mr. Kundu, you said construction equipment growth is 10%, is that right??

**Ravindra Kundu:** Our disbursement growth is what I said.

**Antariksha Banerjee:** In construction equipment?

**Ravindra Kundu:** Yes, t, our overall disbursement growth is 21%, in that Construction Equipment growth has been 10%.

**Antariksha Banerjee:** But in the share of the disbursement growth, that number is mentioned as 5%, so can you help with the absolute number if that is possible?

**Ravindra Kundu:** This is the share of the total disbursement. This is growth over previous year versus current year.

**Antariksha Banerjee:** If the share is 5% and that is unchanged and the total disbursement has grown by 21%, ideally Construction Equipment also has grown by 21%, right?

**Arul Selvan:** It would be very marginal because the rest of the portfolio is growing, other products are also growing.

**Antariksha Banerjee:** If you have the absolute number, it would be great, I will take?

**Arul Selvan:** Construction Equipment?

**Antariksha Banerjee:** Absolute disbursement number if you have it?

**Arul Selvan:** Of Construction Equipment?

**Antariksha Banerjee:** Yes.

**Arul Selvan:** I think this is, I presume you are not auditing us.

**Antariksha Banerjee:** Sorry.

**Arul Selvan:** You need to understand that you take the numbers as we are presenting, it is not like, I mean I am really surprised that you want exact numbers, we do not give those numbers.

**Antariksha Banerjee:** Okay fine and how is the collection efficiency going on in HCV, the early warning indicators that you have?

**Ravindra Kundu:** Collection efficiency, as I mentioned our earlier default nonstarters are coming down and it has improved over the previous quarter Q1, Q1 to Q1 if you see that our 30, 60 and 90 everything has come down and collection efficiency has improved.

**Moderator:** Thank you. The next question is from the line of Shweta Daptardar from Prabhudas Lilladher. Please go ahead.

**Shweta Daptardar:** Sir, couple of questions. The ECL Stage 3 coverage ratio has come down. So is it the indication that the asset quality ahead will be stabilizing? So that's number one. Second, Sir, I am not pressing on you revealing the PD and LGD numbers, but how frequently are these assumptions reset? And lastly Sir in the Home Equity side, loan loss provisioning quarter-on-quarter and year-on-year has shown sharp improvement. But you also highlighted concerns in the PPT on the self-employed segment with elongated working capital cycles and liquidity crunch. So do you see risk to these loan loss provisions going forward? Thank you.

**Arul Selvan:** See what happens is, as you know, these provisions under the ECL methodology is calculated for different segments differently. That is even within the Vehicle Finance, the segmentation is based on the costs like heavy, light, etc. As you know, the last year, the growth in heavies was large and today, the movement into the Stage 3 is more from the heavies that are moving into the Stage 3. The loss ratio, the LGDs for heavies are lower as compared to other high-yield products, so that is where even though the NPAs have moved up, provision requirements has been lower and that is where the provision coverage is seemingly to be marginally down. So there is nothing like we are changing any assumptions in this. The methodology of ECL calculation is changed once in a year. We changed it in March 2019 and it will be changed again in March 2020 based on the previous 10 years of data. So these are the approaches.

**Rupinder Singh:** Yes. So in this Home Equity, when you talk about, yes, there was a lot of reduction. And when you talk about, there is always yes, there is a caution approach we took keep in mind. Please understand market is risky, we also understand, but what we need to do that is prudently keeping in mind the collections on which we are fortifying across there. Obviously, there will be a benefit of further SARFAESI support in terms of reduction, the already existing accounts and in case any new account comes into it. So that statement is all about that we are cautious about it how the market is operating and we are prepared and geared about it. Let us see how it takes up, but point is on both sides whether for the previous reduction, yes, there are a lot of scopes still and we are working on that. And secondly, if anything comes, we are prepared accordingly.

**Moderator:** Thank you. The next question is from the line of Jigdesh Shail from Emkay Global. Please go ahead.

**Jigdesh Shail:** Thanks for allowing me to have the questions. I had 2 specific questions here. Number one, we are seeing that overall securitization pool has been reducing for us if you see the borrowing patterns of debt. From 12% it is right now close to around 10%. So is there any specific reason behind that? Or are we seeing that particular pool to go back to 12% levels and that could support our cost of funds? That is number one. And number two, had been now we are almost in the bottom as far as margins are considered at 6.75%, that is my calculated number, so what kind of trajectory are we looking out to? Obviously I see the yield has been increased by 60 to 70 bps.

**Arul Selvan:** Your voice is slightly low, can you speak loudly please?

**Jigdesh Shail:** So first question was on securitization pool which has reduced. And number two, what is your view over the margin trajectory, which has already hit the low of 6.75%. So what is the trajectory you think margin should be looking like going forward? That is my 2 questions here.

**Arul Selvan:** So we plan doing a securitization more in the process of basis available of demand at the right price as well. And predominantly, we do securitization of priority sector as well to enable the better rates that are prevailing in the market for such assets. Normally, the demand for this peaks in the Q3 and Q4 and that is where you will see the trend happening more towards the later part of the year.

In the first quarter, we have done two deals of securitization and we have done three deals of assignment because the assignment does not show up here on the borrowings under the Ind AS. That is why you are not seeing the total number out here. But between assignment and securitization, we have been maintaining our cash flows for this sort of opportunity at similar levels.

The second question on the margin, yes, the margin will improve. As we said, there are multiple levers we are working on. One is the product mix, which Ravi spoke about and that would improve the yield. And from my end, I will also be working on further reducing the cost of funds, making more of external commercial borrowing than maybe leveraging a little bit more on securitization, etc. And opex will come down in the coming quarters, predominantly by way of a little bit more on the productivity side as well as the denominator effect of the assets growing in the coming quarters. So we fairly see the returns improving, but at this juncture, there are variables we need to be a little bit more assured over the next one or two quarters by which more clarity will emerge.

**Jigdesh Shail:** But do you think the margins can even dip further from current levels? Or you see that to be more or less to be stabilizing and then probably you can see an upward trajectory?

**Arul Selvan:** I do not see further reduction because I see costs of funds are not going up any further. So cost of funds has been the major drain on the margins. So in all probability, hopefully that should be some sort of an advice to the bank, etc., coming from the ministry or from RBI to pass on the cost of fund benefit to the ultimate borrowers, whether it is NBFCs or otherwise. Once it comes, and world over, the rates have been more on the softer side and I think even in India, we expect the rates to either come down or at best to stay where they are rather than increase further. So I do not see that impacting margins further.

**Moderator:** Thank you. The next question is from the line of Nishant Rungta from Premji Invest. Please go ahead.

**Nishant Rungta**: Very good morning. Thank you so much for the opportunity. I have a couple of questions, Sir. First on the vehicle financing industry per se what we have seen over the last six, eight months is basically from various financial encounters that there has been an elongation in tenure on the vehicle financing loans to roughly about four years, while LTVs have remained pretty high. We are nowhere. Most of the players are operating at roughly 90%, 95% sort of an LTV and probably more in some cases. With most of the fleet operators plying at replacement tenure of about four years, is that not taking a high risk on the LTVs already for the industry? Will that not lead to asset quality challenges for the industry, and how will that impact for our company? Specifically in that context, I know you are cutting back on SUV disbursements a bit. You highlighted, but what happens to the back book generally in that context?

And my second question is, given the way in which we are seeing the regulatory arbitrage converging between NBFCs and banks and given the kind of goodwill and vintage that you have in the industry, is there not a growing case for you to look at on the banking license or a small finance bank license given the kind of liquidity issues that we have seen? Does it not make sense for the management to look at an opportunity like that, Sir? Thank you.

**Ravindra Kundu:** So this LTV which you mentioned about it and for the fleet operator, which is particularly applicable for heavy commercial vehicle. The heavy commercial vehicle comes with a chassis or cowl chassis. So therefore invariably all finance companies are financing 100% of the chassis. And since chassis cost is actually invoiced by the manufacturer that is actually the asset value we consider. So, therefore, there is no confusion as that we will fund less than 100%. It is 100% of the chassis. Body is built by the customer. I also mentioned that industry degrew 23% in terms of heavy commercial vehicle. We degrew by 32%. That is the reason because one is that LCVs are funded at much lower price, which is impacting our marginal book yield and book yield at the end. Second is that in the heavy commercial vehicles, as of now, the capacity utilization and other things are not that great. So, therefore, we find that lot of customers are in fairly liquidity and equity so that customers are not qualifying for that. But that we do not fund fleet operator and therefore, we have to focus on the small road transport operator only. And therefore, we are selectively identifying such customers who are good and who can actually build their body on their own and we can finance them 100% of the chassis.

In terms of the price of the vehicle, as of now in this BS IV era, the prices are at the same level. In fact, some discounts have gone up. So, therefore, we are considering the discounts at the time of giving the LTV. So we do not do gross of discount funding. We do net of discount funding and the discounts are also considered. So if MRP is, say, Rs.30 lakh and say, Rs.4 lakh, Rs.5 lakh or Rs.5 lakh is the discount, we consider asset value as Rs.25 lakh, and then on that, we provide 100% funding. And most of the finance companies are doing like that only. So therefore, there is no worry in terms of LTV offering to the customer. The important problem is that today the customers are not having freight or load available, therefore, they are not able to serve the loan every month and that is what is the challenge for us to how to get the money. And that is the reason we have been doing very less in terms of heavy commercial vehicle. Always, as a strategy, we have never increased our disbursement, which is actually helping us.

**Nishant Rungta**: Understood, Sir. On the other question, if you can elaborate?

**Arul Selvan:** On the other question, in order to convert into small finance bank, I think you have already seen our choice of not wanting to become payment bank. Ultimately you have seen vindicated by many of the other finance, small finance banks getting out of the system. I see the small finance bank also very tough, it is not that the deposits are attractive. The rates at which these deposits come are very expensive. Our borrowing costs are even cheaper than these things. We need to wait and watch and see how RBI looks at larger NBFCs and I think in the current context of the larger NBFCs, they will come with certain new regulations surrounding the larger NBFCs. We will wait for it. More importantly, as it stands now, the regulation does not allow us to become a bank. So there is no point in trying to become bank when the regulation does not permit you.

**Nishant Rungta**: Understood Arul. Thank you so much for the response.

**Moderator**: Thank you. We will be able to take one last question. The last question is from the line of Digant Haria from Antique Stock Broking. Please go ahead.

**Digant Haria**: Just one question that I have. So it was a very refreshing annual report where you talk about a phygital strategy, which is digital plus physical? So in line with that, I see a lot of initiatives have been taken to get closer to the customers and maybe to help customers grow their business. So in that context, where are we in terms of our cost-to-income cycle, like when do the benefits of all this starts flowing into it? We are looking at maybe growing more and not looking at cost benefits out of all these initiatives? That is the only question I have.

**Arul Selvan:** Digant that is an interesting question. While there will be cost benefits, what I have frankly experienced is the cost of obsolescence and the cost of keeping abreast of technology is a constant churn. So we need to keep investing more continuously in this endeavour. And it is like if you do not do this your survival itself could be challenged. So this is something you need to keep doing. And you need to keep doing this to keep yourself ahead of the rest of the players, so, while there will be cost benefits, I do not see that becoming a big game changer. I hope I am making myself clear.

**Digant Haria**: Yes, Sir. But anyhow it was a great annual report reading all these initiatives.

**Moderator:** Thank you very much. I would like to hand the conference back to Mr. Nischint Chawathe from Kotak Securities for closing comments.

**Nischint Chawathe:** Thank you.

**Moderator**: Thank you very much. On behalf of Kotak Securities that concludes this conference. Thank you for joining us. Ladies and gentlemen you may now disconnect your lines.