"IIFL Holdings Limited Q1FY15 Results Conference Call"

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MANAGEMENT: **MR. NIRMAL JAIN – CHAIRMAN, IIFL HOLDINGS LIMITED.**
MR. R. VENKATARAMAN – MANAGING DIRECTOR, IIFL HOLDINGS LIMITED.
MR. PARAG SHAH – CHIEF FINANCIAL OFFICER, IIFL HOLDINGS LIMITED
MR. AMIT MEHENDALE – CHIEF FINANCIAL OFFICER, INDIA INFOLINE FINANCE LIMITED

Moderator: Ladies and Gentlemen, Good Day and Welcome to the IIFL Holdings Limited Results Conference Call. We have with us on the call today, Mr. Nirmal Jain – Chairman, IIFL Holdings Limited; Mr. R. Venkataraman – Managing Director IIFL Holdings Limited; Mr. Parag Shah – CFO, IIFL Holdings Limited; and Mr. Amit Mehendale – CFO for India Infoline Finance Ltd.

As a reminder, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. R. Venkataraman. Thank you. And over to you, sir.

R. Venkataraman: Thank you, and Good Afternoon. On behalf of team IIFL I thank all of you for joining us on this call. I am Venkataraman accompanied by Nirmal Jain – our Group Chairman; Parag Shah – CFO for IIFL Holdings Limited and Amit Mehendale – CFO for India Infoline Finance Ltd.

As you are aware we are a diversified financial services company and have multiple businesses which are carried on in our various subsidiaries. In today's call we will be referring to our consolidated numbers unless otherwise specifically stated, as they give a true and fair representation of our performance.

Further, any of us in today's call may make some forward-looking statements based on our current expectations. Actual results may vary. The accuracy or completeness of these expectations therefore cannot be guaranteed.

Post the historic verdict of May 2014 we expect India's business cycle to turnaround. A strong political outcome has already had a positive impact on business sentiment. For the first time in nearly 3 decades India has a political mandate to take forward policy measures including implementation of GST, overhaul of plan acquisition and labor laws and other fiscal and banking sector reforms. Focus on addressing supply side bottlenecks including natural resources like coal, agriculture can help mitigate inflationary pressures. If these are tackled then this will give RBI some leg room to shift its monetary policy stance from combating inflation to supporting growth by lowering interest rates. We believe that Indian equities are in a sweet spot. A conducive policy environment and improving macroeconomic outlook, a positive momentum in earnings growth, rising capital efficiency and falling cost of capital will drive a more sustained valuation rerating. Needless to say, there are risks on the horizon, namely the progress of monsoon and geopolitical tension in the Middle East.

The medium-to-long term improvement in India's economic recovery has a direct linkage to our prospect of our lending business, both in terms of credit growth and asset quality. After a slump over last 2-3 quarters capital market is showing signs of a cyclical recovery, whereas commodities and currency-related broking business continue to face headwind. Our Wealth business continues to grow and we are amongst the leading wealth managers in the country with assets crossing Rs.66,000 crores.

Among other updates – India Infoline Finance Ltd has appointed career banker Ms. Rajashree Nambiar as the Chief Executive officer. Prior to joining IIFL Ms. Nambiar was a part of Standard Chartered Group, Grindlays for over last 2 decades. At the bank she held several key positions in India and South Asia and across multiple functions including sales, credit, product, customer service, distribution, marketing, and operations. She is an MBA from Jamnalal Bajaj Institute of Management Studies.

ICRA announced the upgradation of IIFL's long term debt instruments from earlier (AA-) Stable Outlook to now (AA) with Stable Outlook. Post the performance of our asset revival fund, IIFL Wealth has extended its offerings under the AIF platform. During the quarter we launched a new fund under the AIF platform, namely IIFL National Development Agenda Fund. The fund will be investing in companies and sectors that are going to benefit from the policies of a new government and the cyclical recovery of the economy. We have collected over Rs.500 crores of committed client capital in the funds. IIFL Private Wealth has been recognized as the 'Best Performing National Financial Advisor Wealth Distributor – 2014' at the CNBC TV18 Financial Advisor Award. These awards recognize the best financial advisor across the country and acknowledge the contribution they have made to creating and preserving wealth and distributing expert and productive financial advice. Thomson Reuters announced the winners of the 2014 StarMine Analysts Award for India. Avi Mehta of IIFL won Overall Stock Pickers Award at the same.

With this I will now hand over to Amit Mehendale for an overview of our NBFC business. Thank you.

Amit Mehendale: Thanks. For Q1 FY15, income from fund-based activity was Rs.583 crores, of 9% quarter-on-quarter and 22% year-on-year. Interest cost was Rs.326 crores, up 7% quarter-on-quarter, 23% year-on-year. This segment constitutes 74% of total income for the quarter. Our quarterly loan book increased to Rs.12,439 crores, up 31% year-on-year. Our loan book comprises secured lending of mortgages, capital market products, gold loans, loans against medical equipment and commercial vehicles. Mortgage loan form 47% of total loan book and continue to grow steadily and remain our focus area. We continue to maintain high quality of assets. This is evident in low level of NPA. Our gross NPA and net NPA stood at 0.79% and 0.23% respectively as on June 30, 2014. Against gross NPA of Rs.98.8 crores we have non-standard asset provision of Rs.70.8 crores, and hence our net NPA stands at 0.23%. Besides this we have a provision of Rs.35.5 crores for standard assets as per statutory requirements. Our average cost of funds for the quarter was around 11.6%. Falling cost to income ratio indicates higher utilization of our branch network. I will now hand over to Parag for an overview of our other businesses.

Parag Shah: Thank you, Amit. For the quarter ended June 2014 our total income was Rs.791 crores, marginally up Q-o-Q and 17% Y-o-Y. Our profit before tax was Rs.145 crores, up 15% Q-o-Q and up 56% Y-o-Y, whereas net profit was Rs.94 crores, up 15% Q-o-Q and 48% Y-o-Y.

I will now present a review of each of our other business segment and cost. I start with Financial Product Distribution income. This segment primarily includes Distribution of Insurance, Mutual Funds, Alternate Asset Products, Bond, etc. In Life Insurance business our product portfolio is dominated by long term Endowment Fund product. Our income from this segment for the quarter was Rs.99 crores, down 42% Q-o-Q and up 9% Y-o-Y. Mutual Fund AUM mobilized by IIFL Group is over Rs.18,000 crores. IIFL Wealth has emerged as one of the leading players in this space with wealth management assets crossing Rs.66,000 crores.

I now move on to capital market activities income. Revenue for the quarter for this segment was Rs.107 crores, up 44% Q-o-Q, 83% Y-o-Y. Capital market activities comprise income from equities, commodities, currencies, investment banking, etc. Market volumes have picked up since March 2014 and therefore this segment can witness substantial growth.

Now I shall take up major cost sides. For the quarter our operating costs were Rs.77 crores, a decrease of 22% Q-o-Q and a decline of 14% Y-o-Y. Operating costs were 10% of revenue for the quarter. Employee cost for the quarter was Rs.136 crores, up 5% Q-o-Q and up 9% Y-o-Y. Other costs primarily including administration cost were Rs.93 crores for the quarter, down 19% Q-o-Q and up 8% Y-o-Y. Depreciation cost in the quarter was Rs.15 crores. Our consolidated net debt at the end of the quarter was Rs.10,075 crores and gross debt was Rs.12,060 crores. Of this secured long-term borrowings were Rs.6986 crores. Cash and cash equivalents including current investment position was Rs.1985 crores which includes fixed deposit of Rs.484 crores and mutual fund equity shares and bonds of Rs.833 crores. Our gross debt-to-equity ratio was 5.31x as of quarter end and net debt-to-equity ratio was 4.44x as of the quarter end. I now leave the floor open for any questions.

Moderator: Thank you very much, sir. We will now begin the question-and-answer session. We have the first question is from the line of Vinay Shah from Reliance Mutual Fund. Please go ahead.

Vinay Shah: There is interest cost component for the Wealth Management business in the presentation. So do we have any borrowing at the wealth management level, and for what purpose the borrowing would be there?

Nirmal Jain: There is some working capital requirement. Many a times they buy certain scrips or certain securities for clients, but it is a very negligible or small cost and funded for a few days before it is sold to them.

Vinay Shah: So largely for that requirement?

Nirmal Jain: Yes, but it is a very small component and negligible amount.

Vinay Shah: In the profit and loss account there is some minority portion also. So…

Nirmal Jain: So the wealth management company, almost 20-21% is owned by employees.

Vinay Shah: This happened this quarter only?

Nirmal Jain: No, There is a greater increase in the stake based on ESOP exercise and this has been happening over the last few years. The structure of our wealth management company provides for employee ownership of almost up to 24-25% of the company.

Vinay Shah: Earlier, there was no minority interest ….?

Nirmal Jain: It has always been there for the last 4-5 years. Right from the day wealth management company started we have had this minority interest, it is simply the shareholding of employees' percentage has been increasing.

Vinay Shah: I was asking because in the presentation it was not reflecting in the report.

Nirmal Jain: This is the first time that we have given a wealth profit and loss account separately.

Vinay Shah: No, for the previous quarter and the corresponding quarter ….

Nirmal Jain: What you are saying now is a very valid point. May be there is a typographical error. What you are saying is absolutely right that it should be there in the Q4 also, so there is an error, we regret and we will get it corrected. It should be there in Q4 as well as Q1 last year.

Vinay Shah: In the opening remark it is mentioned that the focus would be more on mortgage loan. But there seems to be some degrowth in the Medical Equipment business in percentage as well as absolute terms also?

Nirmal Jain: There is not a degrowth but there is slow growth, and Amit will give the numbers of growth.

Amit Mehendale: For this quarter the loan book had Rs.438 crores Vs Rs.415 crores for the previous quarter, so it is a marginal growth.

Nirmal Jain: There is a slow growth and there percentage has declined, yes, but another thing is that this is a slack quarter for Medical Equipment. Typically, what happens the process equipment manufacturing companies they have a calendar year ending of December and they push most of their sales towards their yearend which is December quarter.

Vinay Shah: Any substantial growth we can expect in the Gold Loan segment?

Nirmal Jain: Unlikely. As you have seen that gold loan percentage in overall book has fallen and at least at this point in time we are not expecting significant growth in gold loan, percentage may decline further. But we are not expecting degrowth either, so it will be a slow growth or a growth which is slower than rest of the portfolio.

Vinay Shah: And there is a good amount of decline in the operating expense at the IIFL Group level and IIFL finance level. What would be the reason here for decline in the operating expenses because we are growing as an NBFC company?

Nirmal Jain: I will answer both questions. FPD business which is our Financial Product Distribution business peaks in March quarter and when the business volumes are higher, there are higher payouts of referral, sub-brokerage, incentives, and also there are a lot of schemes that happen in terms of what we call internally fly high where we take people on offsite as well as a reward, outside India. So that is all provided for in March quarter. Because FPD income is significantly higher, the concomitant cost is also higher in operating cost and other expenses. As far as our finance company is concerned which is IIFL Finance, there has been rationalization in branches and if you were there in our last call then we had mentioned about some reorganization and some branch shut down cost hit was taken in March quarter.

Vinay Shah: Primarily that would have driven the cost reduction?

Nirmal Jain: That is right. Somebody asked that time that is one-time, I think we had answered that, yes.

Vinay Shah: Any plan to infuse equity at the NBFC level because the overall capital adequacy is near to 16% as on June 2014?

Nirmal Jain: If you see our capital adequacy, then there are two aspects – One is tier-1 capital is 11.9% which is the equity component of capital where the threshold is 7.5%. So, at this point in time we are not under pressure but we can raise a bit of subordinate bonds/preference capital and boost our tier-2 capital. So if 11.9% or close to 12% is our tier-1, actually we can go up to 24% by raising non-equity resources, and second is, if you look at our housing finance there is a thrust for growth, there we have 47% capital adequacy. So we are under no pressure to raise equity at this point in time. But we will need to raise tier-2 capital, you are right.

Moderator: The next question is from the line of Rahul Vekaria from Axis Mutual Fund. Please go ahead.

Rahul Vekaria: I just wanted to know the number of total debt in the book of India Infoline Finance?

Amit Mehendale: The total debt consolidated is Rs.11,650 crores.

Rahul Vekaria: So, on the books of India Infoline Finance, what will be the standalone debt?

Amit Mehendale: I will just give the standalone number. The debt in the HFC is Rs.806 crores, which is funded through NCDs. So if you remove that number you will get a standalone number.

Nirmal Jain: Rs.10,000 odd crores in NBFC as a debt.

Rahul Vekaria: So, debt-to-equity for India Infoline Finance would be around 8.5x or something?

Nirmal Jain: 6.4, Rs.1,700 crores is the net worth, right, Rs.10,000 odd crores is the debt, this includes subordinate debt which is the nature of tier-2 capital.

Moderator: We have the next question from the line of Nishint Chawathe from Kotak Securities. Please go ahead.

Nischint Chawathe: Could you share the provisioning number for the quarter?

Amit Mehendale: Provisioning number for the quarter is Rs.16.93 crores.

Nischint Chawathe: Just trying to understand some of your peers who are engaged in gold loans have reported fairly high provisions during the quarter or higher NPLs during the quarter in this particular segment. So I just wanted to understand where do we stand on this?

Amit Mehendale: Our NPAs for the quarter have increased by about Rs.5.5 crores for gold loan.

Nischint Chawathe: And what would be the number like right row?

Amit Mehendale: The number is close to Rs.41 crores.

Nirmal Jain: The total provision we have on book is about Rs.106 crores, which includes Rs.17-18 crores which is provided in this quarter and in fact our gold loan book also has not grown very aggressively. So, we have been a little conservative in our LTV, and therefore may be that could be one reason, but of course I do not have precise information on our peers in this sector, but I think we have been little more conservative in growing the gold loan. As a strategy our focus is more on mortgages and home loans for growth. But I am surprised that if there is any extraordinary increase in gold provision this quarter, then 3there is a problem last year but I think this quarter if something has happened, I am a little bit surprised on that.

Nischint Chawathe: On the Broking side in the past you have been disclosing the breakup of the absolute broking income, I think in the previous year same quarter you disclosed the breakup between the Retail and Non-Retail segments as well.

Nirmal Jain: Broadly 60/40; 60 is Retail, 40 is Institutional.

Nischint Chawathe: In terms of revenue?

Nirmal Jain: Broking revenue vis-à-vis last year, there is a significant fall because of commodities and currencies actually, maybe the relative growth in equities is higher, but commodities contributed significant amount in the last year first quarter, dropped considerably from second quarter onwards.

Nischint Chawathe: But in terms of equity broking revenue where would you be in this quarter?

Nirmal Jain: Out of our total broking revenue 95% plus is actually equity. Our commodities revenue is just about less than 4% of our total brokerage.

Nischint Chawathe: When you refer to brokerage essentially you are talking about the Rs.107 odd crores?

Nirmal Jain: Of the capital market equities.

Nischint Chawathe: Okay 90-93% will be broking?

Nirmal Jain: The commodities and currency is around 4%.

Nischint Chawathe: In which you will have 60% Retail and 40% Institutional?

Nirmal Jain: The same percentage last year the commodities and currencies accounted for 18% to 20% of our capital market activities last year first quarter. That has fallen to around 4% this year first quarter.

Nischint Chawathe: And within the Broking side, Institutional Retail would be 60, Retail 40?

Nirmal Jain: That is right. And also Investment Banking revenue this quarter was zero whereas there are some positive contributions in the last year first quarter. So capital market activity is comprised investment banking as well as broking for equities, commodities and currencies.

Nischint Chawathe: The HFC is a part of IIFL Finance, right?

Nirmal Jain: That is a subsidiary of IIFL Finance. When you look at IIFL Finance consolidated HFC is included in that.

Nischint Chawathe: And incrementally the entire housing business is booked at the HFC or how does that work?

Nirmal Jain: Incrementally, entire home loan business is booked in HFC, that is right.

Nischint Chawathe: And outstanding basis also, there is any plan to transfer the book or it would just continue and run down?

Nirmal Jain: There will be implications in terms of not only stamp duty but also the age of the asset when you want to sell it down to bank. I do not think we will transfer it. When you want to securitize or sell it down it requires minimum one year holding or 18 months holding on the books, when we transfer it becomes a new asset for the HFC.

Nischint Chawathe: So you may not really want to do that?

Nirmal Jain: We do not want to do that because there is no pressure at this point in time. So we will hold it there, over a period of time we can securitize it from there itself.

Moderator: The next question is from the line of Rohit Shimpi from SBI Mutual Fund. Please go ahead.

Rohit Shimpi: My question is on the Capital Markets segment. This quarter we are reporting PBT margins of about 33% in that segment. Just wanted to get a sense that now that it seems we are close to the previous peaks that we had seen in FY08 to FY10 certainly at the bottom end of toes. Is there basically more operating leverage that is available in this business segment or do you think there is any increase in revenue hereon will have to certainly come with some cost increases?

Nirmal Jain: The increase in revenue will come with significantly less than proportionate cost increase, but of course there can be some cost increase because as the revenue increases, the incentive pay outs and everything also go up. This is also gross in which there are certain exchange and other costs and there are sub-broker pay outs. Operating leverage is still there which is significant in this business. Since there is an increase in revenue, there will be more than proportionate benefit at the bottom line. What has happened in this business, in last quarter….in fact there were some questions which were asked in last call also, we had also taken some reorganization hit where we had shut down and rationalized.

Rohit Shimpi: So if I compare it with last cycle say if we look at FY08 to FY10 numbers of IIFL on this segment, so there we had PBT margins of anywhere between 30% and 40% but at this point we were having higher number of branches which we have rationalized this time around. Is it that we should expect margins to be much higher in this cycle in an optimal quarter or optimal year, how do you look at that?

Nirmal Jain: I think so, in fact that is what our plan and our thought process has been. If the revenue pie increases from here significantly, then our margins should be better than the previous cycle. Now, with a lot more rationalized model focusing on cash market, delivery brokerage and also focusing more through call center and fewer branches, the whole business has undergone a complete transformation in last one year. That has been done with the objective and intent of improving margin and reducing vulnerability to certain down cycles in this segment.

Moderator: The next question is from the line of Vinay Shah from Reliance Mutual Fund. Please go ahead.

Vinay Shah: This is a book-keeping question; can you share the average daily turnover for this quarter, last quarter and the corresponding previous quarter for equity?

Amit Mehendale: Average daily turnover for the current quarter was Rs.6,058 crores, previous quarter was Rs.5,100 crores, and same quarter previous year was Rs.6,500 crores.

Vinay Shah: What would have been the brokerage yield for this quarter?

Amit Mehendale: 2.68.

Vinay Shah: And the two corresponding numbers if you can share?

Amit Mehendale: Previous quarter 2.11 and previous year 2.03.

Nirmal Jain: Our market share in cash segment has gone up by around 60 basis points whereas in F&O it has fallen by around 40 basis points and F&O being the largest part, so overall it seems to have fallen by 30 basis points on an aggregate basis. Obviously the focus on cash market share and market share growth there has helped us in improving our yield.

Vinay Shah: Earlier you used to give this market share and this information in the presentation itself, so...

Nirmal Jain: We can give it. So it has fallen from 3.2 to 2.9 but the cash market share has gone up about 60 basis points increase there.

Vinay Shah: As mentioned in the opening remark that our rating has been upgraded by ICRA, and one of the reasons mentioned in the release that because of the increased or expected increase retail participation in the equity market which may augur well for the players like us. So does it mean that again we will have more branches and there will be a new focus on the retail thing or how do you ….?

Nirmal Jain: It is a good question; our strategy would be to leverage and improve the productivity of existing branches because what we feel that the number of branches, after our complete revamp strategically we have all the locations across the country, are enough to tap the market, and of course they are supported through call center and sub-broker network. Even if there are new branches they will be few. It is not that we really need to ramp up the branch network the way we did it in 2007-08 for broking and insurance or we again did it for gold loan branches in 2010-11. We do not need to go back to that kind of rapid expansion of branches, but I think there is a significant room to improve the productivity and improve sales per branch or per person of the existing network itself.

Moderator Sir, there are no questions at this time.

R. Venkataraman: Thank you so much for joining us on the call today and if you have any other questions please feel free to contact any one of us including investorrelationships@indiainfoline.com.

Nirmal Jain: Good day to everybody.

Moderator Thank you. On behalf of IIFL Holdings Limited this concludes this conference. Thank you for joining us, and you may now disconnect your lines.