"IIFL Finance Limited
Q2 FY2022 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to IIFL Finance Limited, Q2 FY2022 Earnings Conference Call. As a reminder all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to the Management. Thank you and over to you, Sir!

Rajesh Rajak: Good afternoon, everyone. On behalf of team IIFL Finance, I thank all of you for joining us on this call. I am Rajesh Rajak – Chief Financial Officer accompanied by Mr. Nirmal Jain, our Chairman, Mr. Monu Ratra – IIFL Home Finance CEO, and Mr. Venkatesh. N – Managing Director IIFL Samasta Finance Limited. I will hand over to our Chairman to briefly comment on the economy and the Group's strategy and plans. Over to you Mr. Jain!

Nirmal Jain: Thank you Rajesh and good afternoon, to everybody and welcome to this call. After a long time, we are very excited and very happy talking about the economy. Economy seems to be firing in all cylinders as we know consumption is picking up. I mean anecdotally we will find that restaurants and planes are full but also jewellery stores and retail malls are seeing very high footfalls. Also all the numbers and leading indicators show a very strong recovery. But what is more important, and heartening is that we are seeing a very strong recovery in the capex cycle, primarily because the commodity companies have got strong cash flows so that many of them are able to deleverage and even announce expansion plans with internal accruals.

As we know that the large ticket capex comes from commodity companies and not from the other companies and this has happened after a long-time gap. If you would have heard the commentary of many capital goods companies, they are sharing that the order inflow is significantly higher than what it was even a quarter or a year ago.

Also, we are seeing that exports have picked up- technology software exports and also others are doing much better, and all this has been helped by the policy framework which Government has been working on. As we know that the bigger problems such as the issues of telecom are resolved, PLI scheme has taken off, tax rate for new manufacturing is 15%, GST has stabilized. So all these factors put together with the infusion of money that happens during any crisis, is showing strong recovery.

We believe that such recovery has a cascading impact because when you see capex in one large sector it goes on over a year creating demand and jobs and that income is spent on other sectors and we see the cycle at least for the next three to five years should remain strong.

Now, coming to NBFC sector, from IL&FS crisis to COVID, the sector has seen many upheavals and trial by fire, but as is the universal law that survivor emerges stronger and the survivors in the sector seem to be emerging stronger. But there are few more interesting developments that have taken place in the sector primarily caused by COVID and the crisis that we have seen in the last few years.

One is that credit market has always been underpenetrated, but now the demand is becoming visible as well as addressable. It is become addressable with technology because with digital technology, widespread expansion and use of UPI and digital payments, availability of data and lot of alliances that are taking place, this market access is getting easier, and many finance companies are doing lot of innovations which will open up the market and maybe reduce the cost of doing small ticket retail loans in a way that was not possible or not thinkable even sometime back.

Also, the bank partnership in terms of direct assignment, securitization as well as co-lending is now becoming much stronger. In fact, when we are talking to banks what we are hearing is much stronger and much more positive than even what we would have expected or thought about. Even the Finance Minister, RBI and everyone else seems to be in consensus that the best way to penetrate credit to the underserved segment of the society as well as underpenetrated geographies seems to be a partnership model of banks and NBFCs, because what NBFCs can deliver in a small credit niche segments, the small ticket loans or even microfinance loans is far more efficient than what banks can do and these are the areas where the banks are not able to reach. Banks are flushed with liquidity as they are getting deposits and they are not able to lend significantly.

The large ticket private sector capex that I talked about, large corporates are able to tap the market directly, either the foreign market or local market and therefore going forward probably we will see large and larger part of their balance sheet credit being shown by the retail borrowers and that is where the partnership will make lot more sense. Now, when the economy is doing well, the NBFC sector is very well placed and liquidity has also eased for the survivor, for these well established companies very well. Now even our liquidity is higher by Rs. 1,885 Crores than what it was a quarter ago. So, this is the great time to bet on growth and that is what we are doing.

Branches are core to our growth strategy because our gold loan and microfinance businesses, the fulcrum is branch from where in case of gold loan, we can store the gold and for the other product it becomes the face to the customer and it becomes a very efficient mechanism for collection, and of course we use technology as much as possible, but branches cannot be missed away.

In case of gold loan in particular customer wants borrow in five minutes and also take back their jewellery in five minutes in case when they are paying the money back. Technology and the innovation is the key. I will just take one example of WhatsApp loans that we launched, so there are many players who are generating leads on WhatsApp but what we are doing is little different. We are not generating leads but we are doing entire credit underwriting process as well as disbursements on WhatsApp. In the first ten days without any advertisement or promotion we got more than 60,000 leads and what is interesting is that quite a few fraud cases also that we have been able to catch. Basically this technology is very different from what many other people or other fintechs are trying because when they put an app in your mobile phone the app is able to access lot of confidential data including where the customer is moving around physically, all the contact list and that basically is intrusion in privacy lot more than what is required. Many customers sooner or later will reject when they understand the issues with that.

In the WhatsApp model we ask upfront to the customer for the documents that we need and the model that we have been working on seems to be now stabilized and working well. This is what a customer appreciates and that is why the strong word of mouth referral and organic leads flow stronger than what we would have expected. So, when we plan growth strategy for next two to three years based on our assumptions about the economy sector and liquidity other than technology and branches, we are also investing in people. Since last year we have added 6,000 people and in last quarter alone we have added 2,700 people which is net addition. So, number of hiring would be this plus whatever people have left us. So, this is something which is again unprecedented, and these are enticed that people are talking about job losses and problems inflicted by COVID, but we are seeing a great opportunity and we have been able to hire good quality people as well.

So, we invest in branding also along with that and our campaigns are there nationally as well as regionally. So when we look at our last quarter's result there are two things that I would like to bring to your notice, one is that our operating cost obviously has gone up significantly on a year-on-year comparison it has gone up by almost Rs.Rs.94 Crores, significant part of it is the new people that we have hired like 6,000 people since last year and also salary increases that have taken place during this time period. Over and above that, the branch set up cost and new branch initial cost are also there, along with very aggressive investment in technology.

Liquidity as you have seen that we almost increased our cash on the balance sheet by Rs. 1,800 Crores, liquidity is up by almost Rs. 1,885 Crores that obviously has a negative carry in the cost and there has slight deterring impact on our NII or the net interest income, but this is a small cost to pay to make sure that liquidity is comfortable, and we are prepared for growth. But broadly we have been able to maintain our margins and ROE. With this I hand over to Rajesh and I will come back for the Q&A session later. Thank you.

Rajesh Rajak: Thank you, Mr. Jain. I will just take all of you through the key financial highlights for the quarter. So, IIFL Finance's profit after tax was Rs.292 Crores in Q2 FY2022, up 37% year-on-year and at 10% quarter-on-quarter driven by volume growth and lower credit cost.

We recorded pre-provision operating profit at Rs.582 Crores during the quarter. We have significantly expanded our distribution network by adding approximately 350 branches and 4,000 employees during the current financial year.

Our loan AUM grew by 8% year-on-year and 3% quarter-on-quarter to Rs. 44,249 Crores. Our core segments grew at 15% year-on-year to Rs. 40,851 Crores. The CRE portfolio has reduced in line with our retail strategy, 94% of our loans are now retail compared to 89% as of September 2020. 69% of our retail loans are PSL compliant excluding gold loans which are not classified as PSL loans as per RBI.

The large share of retail and PSL compliant loans are of significant value where we can sell down these loans to raise long-term resources. In line with our capital optimizing strategy, 35% of our AUM is assigned or securitized as of September 2021.

Accordingly, our non-fund-based income comprises 37% of the total income for the quarter up from 32% during the corresponding quarter in the previous year. During the quarter we also tied up with Central Bank of India, Punjab National Bank, DCB Bank and Shivalik Small Finance Bank for co-lending of gold loans, home loans and secured business loans.

Our cost to income ratio rose marginally to 40% due to expansion in our physical and digital footprint. Annualized return on equity for the quarter stood at 20.5% driven by an annualized return on asset of 2.8%.

Capital adequacy ratio was 25.9% and tier-1 stood at 18.3% they are well above the strategic requirement of 10% and 15% respectively. Total capital ratio of home finance was at 30.7% and for microfinance stood at 21.9% respectively.

Our average cost of borrowing declined 33 basis points year-on-year to 8.7%. Our GNPA stands at 2.3% and NNPA at 1.1% as of the quarter end.

Collection efficiency has improved significantly. Impact of the second wave has been much milder and as compared to the same in the first wave. As per IND-AS accounting provision coverage of NPA stood at 175%. During the quarter IIFL Finance and IIFL Home Finance's long-term credit rating from both ICRA and CARE were upgraded from AA (Outlook: Negative) to AA (Outlook: Stable). The credit rating from CRISIL was already at AA (Outlook: Stable).

IIFL Samasta Finance Limited's long-term credit rating also got upgraded from CRISIL A+ (Outlook: Stable) to AA- (Outlook: Stable) and from ICRA from A to A+ (Outlook: Stable).

During the quarter we raised Rs. 3,717 Crores through term loans and refinance and in addition loans of Rs. 3,655 Crores is securitized/ assigned during the quarter. Our cash and cash equivalence and committed credit lines from banks and institutions i.e., total liquidity was Rs. 6,379 Crores as of September 30, 2021. We have a positive ALM whereby inflows cover or exceed expected outflows across all buckets.

Additionally, we raised Rs.843 Crores by way of public issue of long-term secured bonds in the month of October 2021. IIFL Home Finance had also had a subordinate debt of public issue and it raised Rs.656 Crores in the month of July.

Now, for some digital updates, we continue to focus on digitization and analytics to improve customer experience and enable a convenient one stop shop for customer's credit and investment needs. We are the first NBFC in the country to launch end-to-end instant unsecured business loans on WhatsApp right from customer on-boarding to disbursement. Within ten days of launch we have disbursed over Rs.4.5 Crores under this initiative.

Our investment in digital innovation has started giving results. Till date they have also disbursed Rs.43 Crores of secured business loans via My Money App. We also went live on the account aggregator model to help customers and a better underwrite small enterprises securely.

For home loans we integrated with WhatsApp for better customer engagements on post disbursement customer queries. Under gold loans we launched a co-branded prepaid card with ICICI Bank. We also tied up with GooglePay for lead generation during the quarter.

IIFL Loans app continues to be increasingly used for various transactions by customers. We have two lakh average monthly active users on the App for the month of June. That brings an end to the update. We can now open the floor for any questions, please. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Yash Agarwal from JM Financial Service. Please go ahead.

Yash Agarwal: Good afternoon, Sir. Congratulations on a good set of numbers. Few questions from my side, in your assigned book and securitized book what percentage credit risk is left on our balance sheet or the whole credit lies on the banks' balance sheet?

Nirmal Jain: In case of assigned book the whole credit risk lies in the bank balance sheet, in case of securitized book there is typically 5% to 7% of credit enhancement given by way of bank fixed deposit. So that much of credit risk lies on our books because bank can dip into that if your losses are more than what were agreed upon.

Yash Agarwal: Got it. So, assigned book completely it is on the bank balance sheet?

Nirmal Jain: That is right and for securitized assets our liability is limited to the bank FD that we have given to them for guarantee which is typically about 5% or 10% of the portfolio.

Yash Agarwal: Sure Sir, also I was just looking at the standalone and consolidated numbers, so I believe we did a standalone of profit before tax of Rs.244 Crores, whereas in IIFL Home Finance, I think as per the paper disclosures it is Rs.197 Crores so if I add that, that would Rs.440 Crores profit before tax. So, where did we lose the Rs.70 Crores, did we lose it in Samasta Microfinance completely?

Nirmal Jain: What happens here is that there is securitization which is done through a trust and that actually when the trust closes that money gets transferred as an assignment income and actually there was one trust of securitization that we closed in the last quarter. That is the adjustment that has come. So, what is happening is that we have done this as a one-off transaction done about two to three years back where the bond was issued through a trust. We have wound it up now and we have closed the trust. But that is only contra entry, because that income gets recorded here.

Yash Agarwal: Sure, I understood. Got it and my last question is in terms of incremental disbursements what is the run rate currently and what sort of loan growth incrementally are we looking at for the rest of the financial year?

Nirmal Jain: If you look at disbursement then last quarter gold loan, we did about Rs. 5,000 Crores disbursement but there are quite a few prepayments also so the loan growth has been 2% to 3% in gold loan. I think this part will accelerate. In case of home loan, we did disbursement of about Rs. 1,600 Crores which I think will grow significantly in this quarter again. The peak in the last year was about close to Rs. 1,800 Crores. I think we should be near peak across that. Business loan mostly is digital now and there also our disbursements were Rs.500 Crores odd in last quarter, that should also grow well. Microfinance also disbursement in the Q1 had in all sorts of hit the crux but now they have recovered from around Rs.236 Crores to Rs. 1,073 Crores. So four times growth in disbursement in microfinance in last quarter and that momentum seems to be continuing.

Yash Agarwal: So, can we see like 10% to 12% growth for the residual part of the year?

Nirmal Jain: Yes, easily I think the loan book should grow by that much in next six months for sure.

Yash Agarwal: Thank you, Sir. Best of luck.

Moderator: Thank you. The next question is from the line of Saptarshree Chatterjee from Centrum Portfolio Management. Please go ahead.

Saptarshree Chatterjee: Thank you for the opportunity. Sir, my question is on the business loans if I see the stage-2 assets it has come around Rs. 1,000 Crores last quarter to around Rs. 1,500 Crores and provision coverage is close to around 9%. So, just wanted to understand how comfortable we are on this business loan's part and secondly on an overall asset quality, is it like the peaks have been there and now going forward slippages are going to come down, just wanted to know your views?

Nirmal Jain: In business loans stage-2 has gone up marginally. It is Rs. 1,152 Crores now compared to Rs. 1,059 Crores last quarter.

Saptarshree Chatterjee: Yes, and if you are on that book how comfortable you are?

Nirmal Jain: The provision coverage is quite comfortable. I think we have been providing aggressively for likely losses or whatever. So if you see our restructuring initial movement then we have taken a significant provision in this quarter also and actually business loans are impacted by the economic activity. So what had happened is first quarter if you know that April–May was almost complete shutdown and then those people after three months or after two months will get into stage-2, stage-3, but things are now recovering. So, as we speak, we should see a very strong recovery in next six months in the business loan segment.

Saptarshree Chatterjee: Great and in the gold loan segment we see that the ticket size has increased around Rs. 50,000 - Rs. 55,000 to close around Rs. 70,000?

Nirmal Jain: Yes, Rs.50000 – Rs.55000 was last year, but last quarter it was around Rs.65000. So, with the gold prices going up, the ticket size has increased across the industry. Also the yield has fallen a little bit because we are also now focusing on a little larger value, i.e. customers from a higher income bracket. But when you say Rs. 59,000 that is last year's average, but if you see last quarter as well it was Rs. 59,000, which has gone up to about Rs. 70,000. So it has gone up marginally from there.

Saptarshree Chatterjee: So, incrementally generally also you are focusing even on the larger ticket size clients also for gold loan, right?

Nirmal Jain: As the gold prices in the last two years have gone up, so the same gold gets will more money also and incrementally you are right there as we open the new branches and the customer segment is also improving little bit.

Saptarshree Chatterjee: Sure, and any guidance you want to put for next two–three years on the credit cost side?

Nirmal Jain: It is difficult to put any guidance on that but under the circumstances if the economy improves then your credit cost and loan loss provisions should go down. Even the similar thing we spoke about in the first quarter in January – February but nobody knew at that point in time that in April – May Covid Wave-2 would be so brutal and quick. So, that again impacted our first quarter performance then the GNPA trending and all. So, unless there is something unforeseen like COVID or anything else things should improve significantly.

Saptarshree Chatterjee: Thank so much and congratulations on good set of numbers. Thank you.

Moderator: Thank you. The next question is from the line of Chirag Sureka from DSP Mutual Fund. Please go ahead.

Chirag Sureka: Good afternoon, Sir. This is Vivek Ramakrishnan. Congratulations on a solid performance. I was looking at the collection efficiency numbers, and I notice that microfinance is in fact actually done really well despite the fact that across industry it does not seem to have done well. So, just wanted to know is there any segment which has performed very well for you which is contradicted to the industry and just completing the question, in terms of SME business loans even there you have shown a strong pickup in collection efficiency, and you were optimistic. I just wanted to know given the state where things are as there are some businesses are completely shut down, are your customers in good shape and do you expect this 94% to go up in the next quarter?

Nirmal Jain: It is a good question. So, collection efficiency basically includes the billing for the month and the overdue amount as well. So, supposing in the last quarter we had 30 days overdue, 60 days overdue, that will also become part of the money to be collected or the money collected will be accounted as there in therefore you see collection efficiency being higher. But even then the GNPAs are trending up little bit. But in microfinance I just want to clarify one thing which is very important. We restructured significant amount of our portfolio i.e. 7% - 8% of our microfinance portfolio is restructured and customer have been given more time. Now, this is a call that one has to take that it is not to say GNPA primarily but more to make sure that these are small customers. Microfinance customers were taking Rs. 25,000 loan and they depend on small activities for their livelihood and when in April–May things were completely shut down, obviously they will be impacted now when you declare them GNPA, their credit score goes down, they find it difficult to borrow again and you will also have a problem. So, we took a conscious call and if you notice last quarter, we restructured around Rs.200 Crores of microfinance portfolio and this quarter we again restructured around Rs.176 Crores of portfolio. But unlike large ticket or other restructuring, here the customers are given three months to six months' moratorium and then we expect them to start paying from next quarter. So, microfinance industry across has been impacted but the only thing is that whether you give restructuring and more time to customers or not is a conscious call that every company can take differently.

Vivek Ramakrishnan: Then one follows up question, three months to six months you do not even collect interest is it or do you collect any interest or anything because people will be going to the collection centres and so on, right to keep in touch with the customer?

Nirmal Jain: Interest is not collected which is collected after the moratorium. The idea is that the income generating activity is completely disrupted, what happened in April – May then we do not expect them to have cash flow to pay their instalments, so we have restructured and given them more time.

Vivek Ramakrishnan: Absolutely, so you are just saying with the opening up they will bounce that is what you are saying, right?

Nirmal Jain: What happens that the instalments remain the same they are given more time, and this has been our experience last year also, last year after the COVID Wave-1 in August – September when things became normal most of these people they came back, and they started becoming good customers. So, what we thought is that rather than declaring them GNPA there we will do restructuring and our restructuring microfinance is relatively significant.

Vivek Ramakrishnan: Thank you, very much and good luck.

Moderator: Thank you. The next question is from the line of Deepak Poddar from Sapphire Capital Partners. Please go ahead.

Deepak Poddar: Thank you very much for the opportunity. I was just reading about as IIFL Finance now on their co-lending plan to more than double its loan book in next three years to about Rs.1 lakh Crores. So, can you throw some more light on it and what sort of matrix we are looking at in three years in terms of ROA and credit cost? So, that would be quite helpful.

Nirmal Jain: I think three years' time doubling is about 25% compounded growth broadly and that is what we are looking at. In terms of ROA, I think we will maintain our current levels and ROE can improve slightly. As the competition becomes intense there can be slight pressure on the yield, there can be upward pressure on cost of fund also. We should be able to make it up by better cost to income ratio as we stabilize our expansion plan and those new branches become productive.

So, there are so many damaging factors which should at play but broadly speaking I think we should be able to maintain and slightly improve return ratios.

Deepak Poddar: Okay, so you said maintain or 2.5% - 3% is the range we are looking at?

Nirmal Jain: Yes, return on assets should be around 2.5%, so it is bit 2.7% in the first half but broadly say around 2.5% or 2.7% is a good number to look at and ROE of about 20% that is what our targets are internally.

Deepak Poddar: So, even at the scale of Rs. 90,000 Crores kind of AUM and we are still looking at ROA 2.5% to 2.7% range?

Nirmal Jain: Yes, because our product mix will remain similar. So our ROA should remain at those level or may improve a little bit. But as I said that it is very difficult to make any forward-looking statement because there are so many divergent forces at play.

Deepak Poddar: Absolutely, that is quite fair and secondly you did mention that in the second half 10% to 12% loan book growth is one can envisage. So, that effective will mean that this year our AUM will grow by only 10% to 11%, right?

Nirmal Jain: Our AUM will grow by 10% to 12% this year, yes you are right broadly maybe in the next six months because the first half there has not been any growth. We should look at our core segment, so if you really look at last five years our total loan AUM has grown on CAGR of 16% but the core segment or the products that we really want to grow which we are focused on in the future has a CAGR of 22%. So, for the next six months 10% to 12% growth is a good number to look at.

Deepak Poddar: Understood, and Sir just a last query on the credit cost you did mention in the last quarter conference call that last quarter credit cost would be a good benchmark like 2% - 2.1% for the rest of the year. Do we still maintain that?

Nirmal Jain: Actually, this quarter again we were little bit hit by the rollover of the lockdown in the first quarter. Hopefully, always we have to maintain that, and our endeavour will be to improve it and reduce the credit cost. So, right now if you see our provisions to loan book is around 2.5% in second quarter which was around 2.2% in the six months if you really look at it. I think we should be able to maintain in that range or we should be able to improve it actually our internal target to bring it down further. Historically, before COVID the credit cost for ten years would have averaged around 1% or little less than that. I think in a steady state scenario once the impact of moratorium restructuring, DCCO is removed then we should be back to those levels, it might take another two three quarters at least.

Deepak Poddar: Steady state 1%, right in two quarter to three quarters?

Nirmal Jain: Yes, trying to reach steady state will be still little sometime away.

Deepak Poddar: Understood. That is, it from my side. All the very best. Thank you very much.

Moderator: Thank you. The next question is from the line of Navneet Bhaiya an Individual Investor. Please go ahead.

Navneet Bhaiya: Sir, congratulations for your results. I have two–three questions, first one is on slide-22 there is a provision release of Rs.173 Crores, I just wanted to understand how is this accounted for is it included in your operating profits?

Nirmal Jain: Recovery will add to the profit but that is a cycle actually you keep providing some part of that recovered more than that for which you have provided.

Navneet Bhaiya: So, Sir just to understand it correctly, in your P&L you provided for Rs.210 Crores, in your slide-22 you have written Rs.210 Crores is the provision and release is Rs.173 Crores, so the net increase is Rs.37 Crores. So, I just wanted to understand?

Nirmal Jain: What happens in many assets which reach very high level of provision then it is better we write them off but our right to recovery continues so, that is how the book is cleaned up.

Navneet Bhaiya: I understand when you recover it is good but how is it treated in your P&L?

Nirmal Jain: P&L gets the Rs.210 Crores hit. Rs.173 Crores adjustment gets into balance sheet actually. So, the provision carried forward is Rs. 1,347 Crores.

Navneet Bhaiya: Okay, so the Rs.173 Crores is not included in your PBT if I understood correctly?

Nirmal Jain: No, it is not included in PBT.

Navneet Bhaiya: Perfect that was my question. Second Sir, on your cost to income ratio with your increased focus on digitization and your investments over there, how do you see your cost to income ratio which is at 39% right now trending over the medium-term what is your aim to take it to?

Nirmal Jain: So, we have set up 350 branches in last six months and 230 branches in last quarter alone and added almost 4,000 people in six months. Now, we have further branch expansion plan, there has been slow down in terms of quarter-over-quarter and earlier branches started becoming productive. So, if you see then in the longer-term, we should be able to be around 33% to 35% as cost to income ratio and at steady state basis.

Navneet Bhaiya: Okay, so with increased digitization let us say over the next three–four years the lower end of 30s is what you would aim to get to?

Nirmal Jain: Absolutely, and once we stop the branch expansion, with the branches to have become productive then also cost to income ratio goes down.

Navneet Bhaiya: Okay, but as long as if you keep seeing growth you will always want to keep expanding your branches, right that would be matter to the factor?

Nirmal Jain: Yes, the pace of growth has been particularly faster in last quarter, which is there are lot of things in pipeline, so we just commissioned everything. But some bit of expansion will continue but it is just relative pace we have the organic growth.

Navneet Bhaiya: Understand Sir, and my last question is on your GNPA ratios while your collections and everything is improved across your various verticals quite drastically, but your GNPA ratios have moved up over last quarter, overall as well as within the various divisions. So, just wanted to understand why would that happen?

Nirmal Jain: I just said that the collection efficiency amounts collected will also include the 30 day, 60 day and all the overdue and GNPA has inched a little bit of more increase in microfinance which has gone up from 1.8% to 2.4%. As we discussed that microfinance has been one industry which has been more seriously impacted that is followed by business loans, only for the unsecured position. So, slight inching up has happened for two–three reasons, one is that last years' restructured cases or moratorium cases would go out of moratorium last quarter and of course the collection will happen there also but there can be slight few basis point increase because of that. Then the second wave impact which hits after 90 days because if the ample of people of who got disrupted in April-May they would have shut down and due to which they start missing their instalment than sooner or later that becomes GNPA, so these are the factors.

Navneet Bhaiya: Understand, so if nothing happens over the next three, four, five months we should again stabilize or maybe even reduce over the next couple of quarters, right if I understand correctly?

Nirmal Jain: Yes, exactly. That is how it should happen. So, if there are no surprises in terms of COVID or anything else or disruption in the economy then obviously this should come down.

Navneet Bhaiya: Understand, Sir. Thank you so much and all the best.

Moderator: Thank you. The next question is from the line of Mudita from Abakkus Asset Managers. Please go ahead.

Mudita: Sir, thanks for this opportunity. Just one question, what would be the quantum of business that would we expect from these branches and what would be the breakeven time for these branches?

Nirmal Jain: So, typically our breakeven branches have good breakeven of six to nine months or up to twelve months. The gold loan branches scale up over a period of time and our matured branch may have Rs.7 Crores – Rs.8 Crores – Rs.10 Crores of principal outstanding. But even if they reach about around Rs.2 Crores or so which is in less than a year then at least from the year around they start breaking even at the unit level without allocating the HO cost. So, our endeavour is to make them breakeven in less than a years' time but nine months to twelve months that is what we can take as good benchmark for their breakeven.

Mudita: Thank you. That is, it from my side.

Moderator: Thank you. The next question is from the line of Amit from 2.0 Capital Advisors. Please go ahead.

Amit: On the new branches you have added 300 plus branches in the first half so going forward what is the plan on branch expansion?

Nirmal Jain: As we said about couple of quarter ago in March, we got approval from RBI. So, our plan is to set up totally seven hundred new branches and I think half of it we have opened 350 branches. So, in next two quarter – three quarter we will set up another 350 branches.

Amit: Out of these 350 branches that you set up already how many of them are also gold loan branches and how many are microfinance?

Nirmal Jain: So, around 230 branches would be gold loan and 120 branches for microfinance.

Amit: Okay, and if you look at your gold loan growth is from the last few quarters so by the branch expansion has been very strong the gold loan growth has not been that strong. So, in fact the per branch gold loan AUM has been coming down, so what is the cost and where this number stabilizes?

Nirmal Jain: First quarter was disrupted, in the last quarter we saw that many people were waiting for their prepayments and the new branches will start delivering over a period of time. Last quarter there were some options of the old cases as well as some of the prepayment of some of the loans and I think the new branch contribution we have not seen yet. But as we go along that will happen over a period, I mean it is a slow process it will happen over a period of time quarter-after-quarter. So, last quarter we grew gold loan book by 3%, despite auctions and prepayment pending for a long time which customers got it done in this quarter. So, hopefully that growth that we talked about which is about 10% - 12% over six months is what we should look at.

Amit: Okay, and what was the quantum of auctions that have happened in Q2?

Nirmal Jain: They happened at local level actually at district level. amounting to around Rs.500 Crores.

Amit: Rs.500 Crores, okay. Thank you very much.

Moderator: Thank you. The next question is from the line of Tejas Mehta from Omkara Capital. Please go ahead.

Tejas Mehta: Nirmal, thanks for taking my question. Few questions, number one you raised a lot of liquidity in the second quarter which is lying on the balance sheet. What is the reason for raising so much liquidity, is it to make sure that the balance sheet remains pretty liquid, and solvent are you seeing a lot of growth coming in the second half?

Nirmal Jain: Actually, what has happened is that in last two three years everybody had liquidity tied and last quarter actually many applications which were pending in the bank which started clearing. We do not want to say no, that is one. Secondly we thought that we have set up so many new branches and even that there is a little bit of negative and carry and cost to pay we used to feel comfortable even if slight accident in the economy or system you should not worry about it. So, that is how we have boosted our liquidity reserves.

Tejas Mehta: Got it and what is the cost at least the liquidity has come us to what is the cost?

Nirmal Jain: These are all coming at 8% - 8.5% -9% depending on the tenure. Again, what we get is about 2.5% - 3% on bank fixed deposit or liquid funds. So, it is about 5%-6% negative continued annualized basis. But what it does is that it gives you peace of mind in the sense that you want to expand, you do not want hold that branches that no the liquidity is tight so go through kind of a thing, you want to make sure that for next six months you should not worry about growth that is what the thought was.

Tejas Mehta: Right, Sir gold loans what is the kind of tonnage is that we hold against the loans that we have on our books?

Nirmal Jain: 43.3 tons of gold is there in our vault.

Tejas Mehta: Got it and the other question is quite intriguing that your gold book very well spread between south, north and west versus the traditional gold loan players which are south focused more or less. What sort of pockets are you identifying in these new geographies that is helping us to spread or going so fast in the new geographies I mean the behaviour of the customer or anything that you would like to highlight here?

Nirmal Jain: We are underpenetrated in south and secondly, we do a lot of research and there is a data analytics team and a Fintech that also works with us on identifying the areas which is bottom up from the district to small towns to villages. So, we do lot of modelling on that based on our historical experience, the current loan book of various products for whatever data we get and the pattern of growth over next two to three years. It is a process where there a team works on identifying locations for growth and that is why we can target to breakeven quicker. So, if you breakeven in six months to twelve months that is really to my mind a very good achievement.

Tejas Mehta: Yes, because operationally gold loan is a very tough business to do, we need a vault in every branch that we are operating and then ability of separately the pure gold from fake jewellery or many times we have heard of robberies stuff like that. So, there are lot of challenges in this business and getting into new geographies which may not be as trialled and tested can have business challenges later down the line. So, just trying to understand what sort of risk management in place do we have a very major accident?

Nirmal Jain: We have lot of internal system, process, and securities. Many a times most of the branches we newly set up are also in the vicinity of branches that we have, because we already have spread all over the country, so we have some understanding of geographical area. Based on that knowledge and understanding, we are not landing into any geography which is completely alien to us.

Tejas Mehta: Right, got it and just one last question on your strategy to reached Rs.1 lakh Crores, is that going to be like a bank relationship driven co-lending what kind of sell downs are looking to do, how will you manage capital to grow so fast over the next few years if you can just through some light on that?

Nirmal Jain: I think what you are saying is right that the bank co-lending model will be one of the key drivers for our growth and as we said the branches are core to our strategy because the businesses that we do they require physical presence and particularly the storage of gold and banks are also looking for retail assets particularly those that are backed high quality collateral like home loan or gold loan or those also priority sector and meet the social objective. So, we are working on that strategy, and I think our growth will be driven by that.

Tejas Mehta: But any bank ties up that you would like to highlight for this strategy?

Nirmal Jain: We have tied up with many banks viz. Central Bank of India, ICICI Bank, Standard Chartered even DCB Punjab National Bank. It will be very exciting.

Tejas Mehta: You originate and then just transfer the loan to the banks and you basically get a cut over the period of the loan is exactly the strategy?

Nirmal Jain: Yes, this is the strategy, but the way it works is that we sit down with the bank, go through the credit policies there and then originate the loans that are lying with their credit policies because they are going to have 80% on their books then you set up the work through all, then you set up the processes we check them, then you integrate the system, then you test it, pilot testing and then you stay there over a period of time.

Tejas Mehta: Sir, today we have about 35% of our loans as securitized and assignment when you hit a number of Rs. 90,000 Crores to Rs.1 lakh Crores what sort of number are we looking at given that co-lending will be a core?

Nirmal Jain: Around 50% of total book, ballpark.

Tejas Mehta: Thanks so much.

Moderator: Thank you. The next question is from the line of Tejas Mehta from Omkara Capital. Please go ahead.

Tejas Mehta: Nirmal, just a couple of more questions, one is on the residual book of commercial real estate that we have, what is the strategy over there now? Are we looking to grow that book again or we will continue to run it down?

Nirmal Jain: So, we do not want grow the book, so what happens with CRE book, there are two types of loans that happen; one loan which banks do, is construction finance where the money is given only for the purpose of construction and not any other purpose like land purchase or against the control of land for takeout for other projects or whatever. So, that is what many NBFCs including us are doing it somewhat in time that we have stopped completely but having said that when you see this portfolio then there are some projects which are synergistic or strategically good for our home loan business. Monu, maybe you can talk about that strategy that how do we look at CRE portfolio from here what kinds of loans you would like to take?

Monu Ratra: Here on as you know in home loans we are in the affordable category, so we would like to do construction, pure play construction finance where all the approvals are in place RERA registered, etc. which will complement our retail strategy, so these would be typical where you can expect 70% to 80% inventory of below say Rs.75 lakhs and this has a great potential to grow and that would supplement our retail home loan growth as well. So, those are the kind of loans we would like to do going forward.

Nirmal Jain: Essentially the book will remain small because large ticket loans will not be done and obviously this book will become relatively much less risky because when you are financing affordable construction you really do not run too much of project related risk. As a percentage our endeavour will be to bring it down to less than 5%.

Tejas Mehta: Got it and some more light on the home loan book, can you just throw some light on the profile of the customers the salaried versus self-employed, you have given the breakup of self-employed of 39%, salaried of 61% can we look at your book as in closer to some competitors?

Monu Ratra: As you can see our average ticket size about Rs.17 lakhs to Rs.18 lakhs and these would be the sense of people where people are buying properties typically ranging from Rs.15 lakhs to anything about Rs.35 lakhs to Rs.40 lakhs. So, the people from the salaried side would be people who would be working in the blue collared jobs or the ones who are working in the retail setups which are there and where the fair amount of our portfolio has a documented income coming because that is how the whole economy has grown. So, we also stress a lot on the subsidy so far, we have been able to give subsidy to nearly 50000 people worth nearly Rs.1200 Crores, so these are people who are buying first time homes and they are also fairly eligible by the subsidy as well. So, that is the kind of a segment we operate in home loans.

Tejas Mehta: So, you were typically operating on the outskirts of large cities?

Monu Ratra: Absolutely, very true.

Tejas Mehta: Got it and if you can take me through the ROA breakup for home loan book is that possible?

Monu Ratra: As far as the home loan is concerned ROA is typically, somewhere around 1.5 to 1.7 kind of an ROA for the standalone home loan book.

Tejas Mehta: The leverage on the book could be about 12 times or more than 12 times?

Monu Ratra: No, we are at about 6 times.

Nirmal Jain: Then we also do assignment, so the ROE multiplication will be not only from leverage but also from the securitized and assigned asset.

Tejas Mehta: Yes, correct.

Monu Ratra: 32% is assigned book.

Tejas Mehta: Okay, and the ROE would be what range then in that scenario?

Nirmal Jain: ROE is about 20% in home loan also separately.

Tejas Mehta: Okay, so you maintain ROE profile similar in most of the segments?

Nirmal Jain: Yes. Microfinance last two quarters was very badly impacted but other than that we have maintained, our target is still have ROA of 20%.

Tejas Mehta: Right, so one more question on the asset quality side, you mentioned that the presentation mentioned Rs.770 Crores is gross NPA and then another about Rs.1290 Crores odd is your restructured book, so if you add the two it is about close to 7% of the loan which are basically spread. While you have mentioned that you have made almost full provision on the entire piece. What sort of recoveries do you see so called do you see chances of more slippage in the next second half?

Nirmal Jain: All indications are that recoveries should be better than the slippages and as against Rs.768 Crores of GNPA, provisions is Rs. 1,347 Crores. The restructured book is about 3% so we are fairly covered, and the recovery till now have been passing through long period and things have been bad and things have been uncertain and volatile. Hopefully next few quarters we will more stable, and then I think our recovery should be very strong compared to the slippages.

Tejas Mehta: I know, my concern is more to do with something like a gold loan book or a microfinance book where usually the recovery is delayed by a couple of quarters and more or less a write off situation for these loans as leverage if you give a moratorium and everything still becomes tough?

Nirmal Jain: If you go by last years' experience when things recovered this was not the case, maybe exceptional cases, so under normal circumstances when people have not paid for a quarter obviously then that will be difficult to recover but when people have not paid because of disruption caused by COVID which is very clear and visible then obviously things are different. In case of gold loan what happens is that you have gold, so as you can auction and recover the money, your lost given default is almost negligible at zero.

Tejas Mehta: How much gold would you have sold in the last quarter in the first half?

Nirmal Jain: We sold about Rs.500 Crores. That was pent up and pending for a long time, so last quarter was about Rs.500 Crores.

Tejas Mehta: Got it, great. I am done with. Thanks a lot.

Moderator: Thank you very much. As there are no further questions, I will now hand the conference over to the management for closing comments.

Nirmal Jain: Thank you all the participants and I also take this opportunity to wish all of you, your families and loved ones a very, very Happy Diwali and a very Prosperous New Year ahead. Thank you so much and if there are any more questions or queries you can always be in touch with our Investor Relations or CFO's department. Thank you so much and have good day ahead.

Moderator: Thank you very much. On behalf of IIFL Finance Limited that concludes this conference. Thank you for joining us you may now disconnect your lines. Thank you.