L&T Finance Holdings

Investor/Analyst Conference Call Transcript
October 22, 2012

Moderator: Ladies and gentlemen, good day and welcome to the L&T Finance Holdings Q2 FY13 Earnings Conference Call. As a reminder, for the duration of this conference, all participants' lines will be in a listen-only mode, and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Shiv Muttoo. Thank you and over to you sir.

Shiv Muttoo: Good evening and welcome to L&T Finance Holdings Ltd's Q2 FY 2013 conference call. We have with us on the call today, Mr. N. Sivaraman - President and Whole time Director and other members of the senior management team. We will initiate the call with opening remarks by Mr. Sivaraman, followed by an interactive Q&A session. Kindly note that some of the statements made on this call today may be forward-looking in nature And a note to that effect is stated in the presentation sent to you earlier. I would now request Mr. Sivaraman to provide his views on the results this quarter and the strategy going forward. Thank you.

N. Sivaraman: Thank you for joining us on this call. I hope all of you have got a copy of the presentation in front of you. On Slide No. 4 which talks about the industry overview, there is hardly anything that I need to really be explaining or detailing to you, all of you are very well aware of it. While you have seen a level of interest rate reductions in the second quarter on the shorter end, again since the middle of September, the change in the liquidity situation seems to be little concerning and would impair any ability of the banks to really reduce the cost. Hopefully some RBI action around liquidity could help in really making sure that the interest rate regime remains more stable and predictable. We continue to be concerned about the fiscal and current account deficit, but hopefully the Government will stay by its statement that they will not exceed the budgetary levels of borrowing for the second half, which actually indicates some level of expenditure control at the Government's end and also in terms of relieving the floor for the corporates to really go up and raise their debt capital from the market. Though however that lack of government spending could have an impact on liquidity as well as the fillip to the market to some extent but I think, managed, well-balanced fiscal deficit or contained fiscal deficit would also help the situation.

In terms of business, what we have seen is a mixed experience across the sector, we have seen good demand continuing from the rural sector both for the HCV and LCV segments as well as the tractor piece, whereas we have seen concerns in terms of growth in the construction equipment as well as the corporate and infrastructure sector. Obviously, one doesn't have to look for the reason, the current environment is definitely contributing to it. The piece that would rather worry us will be the cash flows of many of the corporates and their ability to continue to keep their loans current. That's been one of the concerns and I think it will take some more time before that concern is really lifted out. Infrastructure sector, while I think the good part of the segment is that on the coal side, the 'two steps forward and three steps behind' kind of a resolution process is on but definitely it is working towards a resolution given the compulsion that we have on ground. Hopefully, with respect to CDR we have reached a peak, in terms of the number of applications which are coming up for CDR and you should start seeing some improvement from the third and fourth quarter onwards.

Moving on to the next slide, summary of the financial performance, we have continued to see growth in the Loans and Advances. As compared to the 31st March numbers, we have grown by about 8%, while on a year-on-year basis the loan book has grown by about 27%. This is contributed by, in one sense, Disbursements which are slightly lower than versus last year, about 10% lower. But on a quarter-on-quarter basis, we have seen an improvement of 20% in the Disbursements. The Disbursements have picked up in the month of August and September largely and we are seeing some level of traction coming by both on the infrastructure side as well as the retail asset financing side. The PAT has shown an 18% growth for the lending businesses. This could have definitely been better but for some additional provisioning which is reflected in the P&L. This also indicates that if you are able to bring down the credit cost, which is what our effort will be in the next two quarters, we can see a better improvement in the business. As you will see the margins have remained stable to improving, we will also discuss each individual business and how it has fared. While NPLs have remained more or less stable, but there are some accounts which gone out and some new accounts have come in. So at a broader level, we are confident that while there may be some spike in next two quarters, by 31st March we should end up seeing a stable to improved NPL situation. ROE has shown continued and healthy improvement right through this period. As compared to the first quarter we have shown an improvement.

Moving over to the Investment Management summary, the good piece is that we have improved the average assets under management as compared to the first quarter. PAT level again has been stable. Maybe slightly more than what we have had in the previous year, but definitely it is more because of the lower AUM and some of the integration costs that we have taken for the acquisition of Fidelity. At the holding company level the profits have moved up by 20% on a year-on-year basis for the half year, and 16% compared to the last quarter but on a quarter-on-quarter basis we have seen an improvement of close to 19% in the PAT.

Moving to Slide Number 7, most of it is familiar, it is just re-presented, but clearly we want to set new benchmarks in terms of what we want to represent to all the stakeholders. We want to be an admired inspirational financial institution by creating a sustainable value for all its stakeholders. The top circle indicates our spread of businesses. The Retail lending business has got a portfolio of close to around Rs. 9000 crore. The Supply Chain financing is around Rs. 7000 crore and the Infrastructure book has got about Rs. 12000 crore of loan assets.

Moving over to the next slide, we have always been asked a question about you are too diversified, I think this is basically trying to put together a set of fundamentals that we have used to build the business. There are basically four skills that we have put together to be the key players in the lending business. One is around the Asset backed businesses where we understand the asset, understand the cash flow that the assets give, understand the user of the asset and also when there is an event of default and we need to have a foreclosure we know how exactly to sell these businesses/ assets and then get our loan back. The construction equipment, commercial vehicles are both of that category where we use both the portfolio-based approach as well as the specific asset-based evaluations to be able to control risk in this business.

The second business is the Portfolio-based lending, which is more of a scorecard and wanting to understand the business in the context of larger portfolio using definitely the averages, to be able to do that business very well, both in the management of price and risk. These are the tractors, commercial vehicles, construction equipment and also the micro finance businesses. So clearly these are two businesses were the underlying asset, understanding the asset, and how it will generate cash flow is extremely important and that's what we have built.

The other two sectors of business which is around logistics and lending to corporate, is around understanding the balance sheet as well as the cash flow from project. So when we have built the business around these four critical skills, we have also built the necessary team to bring the skills to us very clearly. In each one of this business we have got people who have more than 15-20 years of experience and know this business and we also have a critical size in our balance sheet today under each one of these businesses to offer meaningful opportunities to senior leaders in the business.

Moving over to the next slide, I think this slide will be very familiar to all of you. The two points that I want to highlight is the shareholding pattern, the retail, which is around 8%, continues to hold a very strong shareholding in the overall shareholding of the company. The other piece that the investments in the Federal Bank and City Union Bank are today valued at more than Rs. 500 crore as compared to our investment of about Rs. 151 crore. You would also see a new addition of the Indo-Pacific Housing Finance. It will of course get renamed as we go along, the acquisition has been completed as of 10th of October, 2012, and we`ll see some details on this company as we move along in the presentation.

On Page #11 we have the overview of L&T Finance and Fincorp. We continue to present it as one entity for the simple reason that year-on-year comparison becomes easier for us. You will see from the loan portfolio statement clearly the Construction Equipment and CLL (Corporate Loans and Leases) book having dropped as compared to both Q1 of this year as well as last year comparable numbers. The reason is obvious because the disbursement in this segment have been lower whereas the Rural Products Finance business have actually gained a percentage point as compared to the Q1 levels. You will also see that Capital Markets business has moved up a percentage point as compared to the previous quarter. This is as a result of opportunities available for quality promoters who want to continue to invest in their business or would like to enhance their levels of shareholding in their businesses using this opportunity of low valuation. So consequently it has offered us some good opportunities to build our portfolio in this business.

Moving over to Page #12, the risk management, the point that I want to highlight is that at the operational risk level, we have created a centralized loan authorization and a disbursement segment, so it clearly improves the kind of quality of data entry, quality of approval, and the quality of credit as a result. We are also moving into receipting on a centralized basis to make sure that the local level frauds are eliminated. As you will know that this is a business where there is a significant cash collection that happens both in the Commercial Vehicles as well as in the Tractor businesses and Rural Products Finance. So clearly the controls are extremely important, so this is another method that we have tried to use to make sure that the frauds on the grounds are reduced. As we keep repeating we are supported by an extremely strong analytics team to analyze and monitor the retail portfolio. They help in making sure that the origination quality continues to remain strong. The credit parameters are validated against the portfolio performance and appropriate modifications are done. So, on the whole, we have a credit department which is independent of the businesses and consequently makes sure the credit quality remains very good. As you will see from the table below, we are independent of the kind of movements or stress that is there in the system, the gross NPA levels have remained pretty steady, and these have been steady without any significant write-offs from the gross level. So we continue to carry a fair amount of provision. So it is creditable that the credit quality has to be seen in the context of the kind of write-offs we do and consequently the origination quality. As you see on the line - provision over RBI norms, we are quite comfortably placed to make sure that all potential foreclosure losses, whenever the loan account gets closed is fully provided for. The question that we have always come around is what is the level of coverage. I want to talk about it in two points. One is that in arriving at the net NPA level, we have always excluded the value of the repo assets in our balance sheet. We have given a line which increases the value of the repossessed assets that's in our hands, that's about Rs. 20 crore. So the effective net NPA is about Rs. 120-odd crore as compared to a gross NPA of Rs. 240 crore, which means that we have a provision coverage of about 50%. And over here, one important point that you all need to understand is that this is largely asset backed financing. We have recourse to the asset in case of a default and can exercise this right immediately after 180 days and frequently also, we do it earlier than even they becoming a NPA. So consequently our losses and the time it takes to really foreclose the loan with a repossessed asset is much shorter. As a result the losses underlying in the balance sheet are far lower than what happens in a corporate account. So in that context we do believe that our provision coverage levels are adequate and fairly good levels.

As far as the asset/liability management level is concerned, given the average level of maturity of L&T Finance portfolio of about roughly 2-2.5 years, it doesn't pose a major challenge, but frequently we run into this difficulty of basis mismatch, as you would have seen in the last about 18 months where we have had a margin drop as a result of this basis mismatch. We continue to look at rather as it is with any other NBFCs, most of the liability side is coming from the bank. So that's something which is a challenge which we will have to manage on an ongoing basis.

Moving over to the financial performance slide, which is page 13, the average growth in the Interest Income as well as the Operating Expenses have been in line with the book growth whereas Interest Expenses have moved up by about 8% higher than the income growth which is as a result of the changes that have happened in interest rate environment.. Some of the lower cost loans have been replaced during the current year with the slightly higher cost loans, all of these have impacted the overall interest expenses level. The one that has really bothered us is the credit cost. As you will notice from the bullet below, that our credit cost has been higher by about Rs. 21 crore without including the MFI losses, which has had an impact in terms of our overall PAT numbers. I wouldn't call them all losses, as we roll back the account in a normal account, and especially in the case of some of the corporate loans which has caused the increase in the overall NPA levels as well as the credit costs, we do believe that there is an opportunity lying here to improve our performance going forward.

As far as the Gross Loans and Advances are concerned, as compared to the end of FY12, our loans have grown about 6% or so as compared to the first half of last year the loan book has grown by about 24%. Gross NPAs have remained steady except for some increases in the corporate books, which has pushed up the overall gross NPAs by about Rs. 38 crore or so as compared to the end of 31st March 2012.

Coming to the ratios, you will see that the Net Interest Margin without MTM on one time is at 5.79% as compared to 6.03% in the first quarter. The two points that you need to note which will be there in the box below is that there has been an increase in the gearing level and also we had some lumpy disbursements in the last week of September. If you really take out these two effects then the margins are about 6.1% which is in line with what we had estimated as an improvement that should come through sooner.

The other important point is that if I look at the portfolio margin, as of a particular date, that is more like telling us what is the one day interest that we can earn. As of 30th September 2012, it has improved by about 20 basis points as compared to 30th June, 2012. This is again in line with our expectation and outlook. We see this improving as we go along hoping that the interest rate environment will not worsen from here. There will be some steps which RBI will take to improve the liquidity situation. So clearly we are looking to see a continuous improvement in the margins till the fourth quarter.

The other piece is that if you look at the Operating Expenses, we have continued to show improvement in line with our overall goal to make sure that we are one of the most competitive in terms of delivery of credit in the market. Credit costs have been elevated. Obvious reasons have been around the quality of the corporate book. We do see these things reversing in the fourth quarter to help us improve the overall numbers. And you will also notice there is a handsome increase in the ROE on the back of both improving margins as well as improving gearing levels.

Coming to the capital adequacy, we are at about 15.5% as of September 2012. We are very deliberately making sure that we do not overcapitalize the subsidiaries, while the financial flexibility is kept at the holding company level, so that the ratios are more consistent at the operating entity level. I would now request Mr. Suneet Maheshwari, Managing Director and Chief Executive of L&T infrastructure Finance to kindly give us an update on the Infra business.

Suneet Maheshwari: On L&T Infra, we can talk about the business really comprising loan assets which are distributed to corporate projects, and a little flavor of equity. Of the projects about 1/3rd are operating, the rest are under construction. So essentially we are saying that 50% of the projects are already operating and therefore the completion risk is lower. If you look at our loan portfolio, we have tried to divide the power under 3-4 different heads, rather than look at it as just one head. We have looked at thermal power, renewable, transmission and distribution and we have some corporate loans in power. And our focus in the last 12 months has been really on trying to grow renewable power, which really comprises solar, wind and small hybrid projects and the advantage is that the renewable power except for the hybrid project, they come to the market or the completion risk is over much faster, in fact, all the solar projects which we have done, which would comprise may be about 9% out of the 21 are all operating at the moment with a few months of track record, so we have a satisfactory working. We believe that having almost a third of our portfolio as operating reduces the risk in terms of the portfolio because we have been able to see the seasoning of the portfolio over the completion risk period. If you see the growth in our assets which have been there over the period, it's of the order of about 15%, and we have been able to maintain this growth, while of course our focus this year has been more on not really chasing growth but more in terms of looking at good quality assets. Not missing out on any good opportunity, but really not chasing purely numbers, but we have had some marginal growth and what we see in terms of our order book pipeline is that we see a small revival, it's too early to say but we see a small revival in the pipeline. So we believe that augurs well going forward. Typically, our H1 to H2 ratio would be 40:-60. But this year since we were conservative our H1 would be about 32% over what we have targeted to achieve which is about the same as say last year. We are happy to remain at about similar levels in terms of disbursements, but in terms of assets we would of course grow because these are long-term assets.

Going over to our Risk Management, so if you look at the gross Non-Performing Assets, there is a small growth but if you look at over the March numbers, we are probably at the same level. If you look at the percentages at March we were at 1.69%, at present we are at 1.54%. Not a major achievement but what we see is we are still staying on course with respect to those levels. We are not seeing any major increase coming into this. It is too early to say whether this reduction or marginal reduction is the kind of trend to say because we still see stress in the economy continuing in this quarter but what we can also say is that since we are starting to see some investment cycle coming back, we hope and believe that the worst in the infrastructure sector maybe over by the end of this quarter.

So the other point that we may like to highlight is the fact that over and above the provisioning norms that RBI requires, we have provided an additional provisioning, which in September 2012, is of the order of Rs. 72 crore, and in March 2012 it was Rs 33.7 crore and this comprises that there is a standard provisioning and then we provide an additional provisioning over the standard provisioning that is required. The standard provisioning is at 0.25%, we provide on an average I would say 0.35-0.38% of our portfolio and we also in respect to those assets, though our provisioning requirements are beyond 180 days - we need to make provisioning as per RBI requirements. But in respect of those assets as they grow beyond the four months threshold, we do a case-by-case analysis and make an additional, if I may use the word, 'contingency provision.' based on our judgment in terms of how the things would go forward and the basic strategy is that we will get in line with the Usha Thorat Committee requirements and we come up to almost as much as about 7-7.5% of those requirements. So the contingency provision in the past has had of course some trend of reversals also happening if the case improves and if the worst in the economy is over by Q4, we in the next year could see some abatement in this or even some reversals.

Our concentration if I may talk about that is really the top borrowers represent about 21% of our exposures and the top 10 borrower groups represent about 30% of our exposures. So we are focused at the emerging clients group for the mid-market segment and that gives us also the option of distributing our asset portfolio over a larger number of clients or projects.

If you look at our Interest Income, again you see a growth, but on the other side if you see the Interest Expense that has also seen a large growth over the same period of last year, which is almost about 42.8% or 43% growth. Now that is reasonably well explained. There was a higher interest rate prevailing. We are seeing early signs of abatement, too early to say how fast this will go down. But we think that the worst in terms of higher interest rates may be over going forward and we should see an improvement here. Ultimately, when we look at our lending business, we don't focus only on the interest. We focus largely on our spread that is there and we don't really try and take a call on an interest rate regime. So I think that's the way we have tried to derisk our balance sheet from a point of view of interest rate risk.

There is a marginal drop on H1-to-H1 comparison on the Fee Income that's because these are linked to completion of the projects that are there and therefore tend to have lumpiness in terms of quarter booking. We are confident that the targets that we have kept for the year which is slightly over and above the last year`s achievement that we have done. We should be able to achieve as much Fee income as that.

If we look at our key ratios, the Yield is about 13.07, if we look at the Cost of funds, is at 9.72, so the Net Interest Margin is better than what it was at the end of the year which was 5.01. The Fee Income as we talked about is more or less on the same lines. Operating expenses also are more or less on the same line. So if there is one item that has changed, it is really credit cost of provisioning and that is reflected here already.

In terms of our Return on Equity, I think we are slightly lower but not too much. But if you look at our Return on Assets that has been a little lower primarily because of the higher interest cost and also the higher credit cost that was prevailing.

The Gearing ratios have slightly improved over the financial year end but more or less in line with the H1 and we would continue to operate within a 4.25 to 5.25 range. RBI allows us to go up to 5.5 but we would continue to operate in that kind of gearing levels going forward.

On our NPA, I have already mentioned to you that we are more or less on the same lines. We saw a marginal improvement in Q1, but it's too early to say, so we expect to remain at the same level as we go forward throughout the year but we hope to see an improvement in the next financial year.

N. Sivaraman: Just a few points of reinforcement, our portfolio in infra very clearly reflects our assessment of the credit outlook as well as the margin outlook. Our philosophy of creating contingency provisions even against the standard asset is basically from two perspectives; one is that we are able to even out the performance and second is that we are able to create a nature of a floating provision to make sure that if out of portfolio, one or two assets do slip into the final NPA levels, we have ability to absorb that without creating any additional provision. Also clearly our performance over the next two quarters from a credit cost perspective, we don't expect it to be really deteriorating in any further from here very clearly.

The other piece is that both the accounting treatment for our upfront fee as well as on the credit cost is in line with the international accounting standard, which is AS30 IFRS. So as and when some of these things become effective, we are already in line with what is we require to do, there will be no further impact on the P&L.

On Capital Adequacy, yes, as is the case with L&T Finance, we have kept it as based on requirement and the flexibility is available at the holding company level to make sure that we are able to put in the requisite capital as and when it is required.

The next page, Page #19 talks to you about the Debt Composition. Basically in L&T Finance Holdings, our effort has been to reduce the level of bank borrowing by using the opportunity to raise some 12 to 24 months borrowing from the market at a cheaper price than bank`s lending rate. Plus also it is in line with trying to reduce the level of basis miss-match that we carry in L&T Finance. Infra will continue to be in the region of about 65% in bank borrowing to make sure that it is in line with the asset profile which is carrying a floating rate. That's very important and it is also important that we carry about 30-40% of fixed rate loans to make sure that the shocks remaining interest rates volatility are minimized.

Moving over to Page #20, on Mutual Fund, as you may all be aware, currently all the approvals required from SEBI for taking control of Fidelity are available. The exit options to the investors are happening. Actually the exit option is available for both investors in the L&T Mutual Funds as well as Fidelity Mutual Fund to the extent that schemes are also being merged and they are becoming under one umbrella. We have put in place the entire integration plan; all positions have been identified, announced to people. I am happy to say that there are no major human resources issues over there. Some of them actually moved into a group level role to handle some key functions. So in the process we have been able to absorb almost all of them into over financial services organization. Fund Management team have been strengthened. Mr. Soumendra Nath Lahiri has joined from Canara Robeco to help the Equity Fund operations. So has Mr. Shriram Ramanathan, who is to be with Fidelity has joined us as Head of Fixed Income. Also, that very clearly the composition of the fund, the distribution reach will be that much more composite when Fidelity integration is complete.

At the summary financial levels, as I have explained already the PAT is about Rs. 8.4 crore for the quarter (negative) whereas the operating revenues as a percentage of AUM has slightly dropped as a result of the lower AUM plus also the composition mode in favor of the debt fund.

Next page has been something which maybe it would have helped us if we had put it together earlier itself. As you will see in the slide it talks about Fidelity's own performance over the last two fiscal years where Fidelity has been able to improve its operating losses from Rs. 62.4 crore to about Rs. 20.8 crore and even as we absorb the current year run rate seems to be at a similar level even with a slightly lower AUM at the losses levels. The other piece you will see in the last column is actually a simple sum of the financial results of both L&T's AMC as well as Fidelity AMC. You will see that the operating profit is a loss of 35 basis points as a percentage of the

AUM. That is about Rs. 46 crore of an aggregate loss. This does not factor in any synergy benefit on network or in terms of the distribution reach and other pieces. And you are also aware that SEBI has recently changed the expense ratios both in terms of the fungibility of the expense ratio as well as additional expense ratio that is available to us. So a combination of increase in margins arising from the additional fee that we can charge on the funds and also an increase in the AUM level can easily bridge this Rs. 46 crore gap and then we can see a breakeven pretty soon. The whole purpose of this slide is to just communicate that this business will be value accretive to us and when the break-even is reached and it is a question of thereafter building the profitability. The other piece is that as of 30th September we had about close to Rs. 12,500 crore of total assets, it also puts us in a significant position to attract additional inflows both on the Fixed Income side and also on the Equity side.

You would have read in the media about the acquisition that we have announced of Family Credit Limited. This is an acquisition which we have acquired from Société Générale Consumer Finance. Their primary business is in financing the auto sectors, two-wheelers and car financing. They are present in about 16 states with 53 branches and customer base exceeding 400,000 customers. Out of these 53 branches, 42 branches are in same locations as L&T Finance, so it gives L&T Finance additional 11 branches reach in the country. They also have an existing OEM relationship as well as dealer locations of about 1500-odd where they are present already. For this business to be really successful both the OEM relationship as well as the presence at the distributor level is extremely important and that is what they bring. As you see at the bottom pie chart, the two-wheeler loans are about 53% of the total book of Rs. 1300 crore, new cars are about Rs. 250 crore and used cars are about Rs. 200-odd crore. So that gives us a very good pick-up to our own auto portfolio which is about Rs. 500 crore. So we are able to diversify our offering and also reach out to a much larger customer segment. This business has also shown a fairly significant improvement in the performance both on the disbursements side as well as in terms of its margins. The NIM even at a 16% capital adequacy is quite healthy at about 14%. The area that we really need to work on is the operating cost, as the volumes pick up and as it integrates with L&T Finance, there is a significant opportunity available to us to achieve that kind of efficiency. The PAT for the first quarter is about Rs. 5 crore which we can consider as a kind of run rate that one can hope to see in the current quarter. We have paid an acquisition cost of about Rs. 120 crore, which is of course, subject to adjustment changes to the net worth till the date of closing and you will also notice that it is in the context of a 16.5% capital adequacy, which means that there is sufficient value embedded in this acquisition for us. The Net worth of this company is about Rs. 190 crore as of 30th June. So it is clearly a very valuable acquisition for us. Now this value can only go up as we work on the branch rationalization which means 42 of the branches do get co-located with L&T Finance's own branch and they have a centralized back office or centralized back office which is being utilized to the extent of only 50% of the capacity, so clearly that is a great opportunity. We also believe that we can improve on the borrowing cost. So all of this has got an extremely positive impact on this acquisition and will help us improve our overall performance from where we are today.

On the Housing Finance, of course we have given some inputs quite early. The current loan book is of the order of about Rs. 182 crore with a Net worth of Rs. 125 crore, you all know that we paid about Rs. 110 crore for this acquisition. In the second quarter, the company has reported a PAT of about Rs. 5.6 crore. Of course, I have to say that we need to make some investments in expanding the network to be able to reach out to all the customer segments that we wish to serve. So this may not be a representative number, but clearly we believe that this is going to open up our ability to serve a set of new retail clients. Currently, this business serves self-employed low income group borrowers. Our desire will be to use our presence both in the rural areas, semi-urban areas to reinforce this segment of clients. In addition to that is what we will attempt to build in the urban areas with the salaried class. Our preference in the urban areas as well as L&T's role as a contractor to many developers and as a developer itself should help us establish the traction to the salaried class in the urban areas quite early. We would like to diversify the overall product portfolio from just being a mortgage financier to loan against property as well as builder financing in addition to doing lease rental discounting.

Some of the other two slides will be around trying to explain the balance sheet to some extent. One case is the consolidated network. Frequently, we end up saying price-to-book multiple at a holding company level. We wish to inform you that there are several components in this. So these need to be factored in valuing this company. There are three pieces that we need to understand: There is an investment in L&T Investment Management which is at about Rs. 180 crore as of now. The investments in the bank which is Rs. 152 crore, whose current market value is about Rs. 500 odd crore. There is also a perpetual debt which we have invested in L&T Finance of Rs. 200 crore, the balance is in the form of mutual fund investments. So these need to be factored in valuing this company.

The next page 'Financial Flexibility' basically tries to address the question about what kind of liquidity is available at the holding company level to meet with the cost of acquisitions as well as meeting the capital requirements of the two companies. So we have the perpetual debt investment in L&T Finance which can be disposed off any time that we require. We are carrying about Rs. 290 crore of mutual fund investment and we talked about the market value of investments in the banks. While we have invested it from the point of view of participating in the entire value chain in financial services but this is flexibility available to us in the event that we require this capital. So all in all we have close to around Rs. 1000 crore of financial flexibility available at the holding company level.

Moving over to the outlook. The good piece is that the monsoon has caught up and reasonable level of rains have occurred across the country except may be in one or two states. So clearly the monsoon deficit has come down. We believe that this will provide a fillip to the rural market which continued to show robustness even when the rest of the country has suffered a bit of the slow down. The minimum support price as well as the continued transfer of income to the rural area should support the demand for both utility vehicles as well as small commercial vehicles.

Construction equipment, we hope in the second quarter with the lifting of mining bans in certain areas as well as the financial closure to be achieved for the road sector and may be with the real estate segment also showing some signs of growth, we will see some strong traction in construction equipment going forward. Our hope has been that the economic activities in the second half will be better which would support the auto sector, commercial vehicles as well as the cars and other auto segments. Corporate, we do believe that they are still not out of the woods, they continue to be in some level of cash flow stress. Hopefully, with the release of some funds by some of the public sector undertakings to these corporates and successful periods having been completed, these assets will return to help. While we may not see a significant increase in the disbursements in the corporate segment, we could expect to see some reduction in the stress in this sector.

Margins for L&T Finance Holdings will definitely improve with our outlook. We do not see any great spike in the interest rates going from here if anything we should see a reduction.

As far as the infrastructure is concerned the primary opportunity will be around renewable energy, roads and if the coal issues are resolved we may see opportunities in the thermal sector. We might also see some of the GAP financing as well as some quality re-financing opportunities as banks would like to reduce their exposure to the infrastructure sector available to us. The margin over here given that the basis mismatch is very limited, margin should remain stable to improving except when the project loans. Some of the re-finance loans might look for slightly lower rates of interest but it comes with a lower operating cost as well as improved credit quality.

On the asset management side you will all be familiar that the expense ratio changes are going to be very positive, and hopefully with some of the steps that the Government is taking the outlook towards the investment in the equity market will improve and consequently the industry and also we will start seeing some positive flows. From our perspective, it is also important that most of the distributors are at a neutral position at the moment. Once the empanelment process is completed we will start seeing active selling as well. So that should result in some improvement in our equity AUM as well. So consequently all in all, we expect that the AMC business should start looking up on the overall returns and valuation as well. With this, I leave the floor open for questions.

Moderator: Thank you very much Sir. Ladies and gentlemen, we will now begin the question-and-answer session. Our first question is from Mr. Parag Jariwala of Macquarie Securities, please go ahead.

Parag Jariwala: Regarding your acquisition of Family Credit I just wanted some details about this company. What was the profit made by the company in FY 2012 if you can give that number?

N. Sivaraman: FY 2012 it was Rs. 3 crore.

Parag Jariwala: What is the Net worth for the company?

N. Sivaraman: It is about Rs. 190 crore as of 30th June 2012.

Parag Jariwala: What was the reason for such low profits in FY 2012 because I see your presentation that first quarter was Rs. 5 crore, is it because of the higher write-offs they have taken?

N. Sivaraman: They had some legacy portfolio on personal loans which they have cleaned up in the last year plus they were also little slow in terms of disbursements in the last two years which they picked up only towards the end of third quarter of last year.

Parag Jariwala: Can you give me this amount of personal loan write-offs in FY 2012?

N. Sivaraman: At the moment we have certain confidentiality norms because their transaction is yet to close. But I can say that there is no legacy which is being carried forward.

Parag Jariwala: The NIM is very impressive at 13.6%. So can you just tell me what are the cost of funds there because I just wanted to know what extent L&T brand can bring the cost down?

N. Sivaraman: Their cost has been I think in the region of about 11% after borrowing, and it is also impacted by a fairly high level of operating cost given the low utilization of capacity. So typically one would look at 4-5% operating cost but they have been far higher than that.

Parag Jariwala: Regarding say operating cost or operating margins and etc. by what time you think that you can turn around to a reasonable NBFC which can generate anywhere between 18-20% kind of ROE?

N. Sivaraman: First is you need to see it in the context of our acquisition cost, while at the Net worth level it may take 3-4 quarters to reach up to that level of ROE but in the context of our acquisition we are almost close to the ROE target that we have set for ourselves. It does not need too much of an improvement from here to achieve 18-20% ROE.

Parag Jariwala: I think 5% kind of quarterly profits can be maintained here right?

N. Sivaraman: Yes, that is what the run rate looks like.

Parag Jariwala: Sir, your another acquisition in Housing Finance, I see that the profit has jumped from Rs. 1.6 crore to almost Rs. 5.6 crore. So what has actually led to this sharp improvement in profit?

N. Sivaraman: The overall reduction in the liabilities, largely funded by the Net worth as you will see on the balance sheet itself, from Rs. 117 crore , the Net worth has moved to Rs. 124 crore the retained earnings have helped them. The second is also that there have been good amount of recoveries from their provisioning in the past. One of the things is this company anything above 60 days is fully provided for. So that is a contrary reason why there is some recovery as well. I think you need to look at it as a platform rather than as a profit at the moment, because Rs. 180 crore is neither here nor there. It offers us a ready platform from where we can really build our mortgage business into big numbers. So at the moment the profit numbers are not so relevant, more importantly that it has got sufficient Net worth to build an overall volume close to around Rs. 800 crore to Rs. 900 crore, given the capital adequacy requirements in the mortgage business, and the second piece is that it has a ready platform and a deposit acceptance capability. So, all of these are going to be valuable to us.

Parag Jariwala: Sir, as regards to overall disbursement numbers, agreed that the market situation is not that great but still disbursement growth has been flat for L&T Finance and little compression is visible in L&T Infra. So what could be a fair outlook to assume reasonable numbers to look for in FY 2013? These numbers will get into the loan book at least in the next two to three quarters because currently although loan growth looks really impressive but as disbursement is slowing down or remaining flat that would directly get reflected in the next 2 -3 quarters in the loan growth as well right?

N. Sivaraman: Agreed, so we would like to achieve about 15-20% growth in the loan book on L&T Finance and L&T Infra the disbursements momentum continue will show about 30-35% kind of growth in balance sheet.

Parag Jariwala: So overall it could still be around 25%?

N. Sivaraman: Around 20-23%. In Infra most of the loan disbursements go and sit in the balance sheet because of the slow accretion of principal.

Parag Jariwala: Sir, the last question regarding Fidelity, so whatever was the proportion of debt-to-equity at the time you announced the acquisition, is there any substantial change say I mean 80 was equity and 20 was debt in the overall mutual fund of Fidelity, so is there any change in that mix as of now or as 30th September for Fidelity standalone?

N. Sivaraman: It was a 65:35 equity-debt mix in Fidelity. It may have marginally changed in favor of debt to some extent. But this is also because there is no active selling of the fund by the distributors, even the normal redemptions have also had an impact on the overall AUM level. But broadly I think the overall AUM level has improved and I think we should be seeing a positive value for it.

Parag Jariwala: Sir, I think almost all the approvals from SEBI and etc. as we read in the news paper are in place. So by what time can you announce the acquisition price or something?

N. Sivaraman: I think the closing of the transaction is scheduled for end of November. So we would definitely keep you informed.

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

Devam Modi: Firstly, we would like to know that which are the segments that have witnessed the maximum stress in terms of, there is definite rise in gross NPA number, so which particular segments have contributed to this?

N. Sivaraman: As far as Infra is concerned, there is no major discovery to be made except that construction companies are the ones which are causing some trouble, and some of the earlier cases where they were vendors to the PSU companies have continued to remain in the stress cases as of now. As far as L&T Finance is concerned we are not really doing business based on segment but more around specific corporates who we have liked. Some of them are in stress. So it is nothing to do with segment as such as of now for us.

Devam Modi: What would be the approximate amount of upfront interest fee that we would have currently apportioned of our future period?

N. Sivaraman: See, typically it improves our average margin by about quarter percent per annum.

Devam Modi: Sir, basically what I would be wanting to know is what would be the approximate amount of upfront fees that we would have postponed or apportioned to our future period?

N. Sivaraman: I understood your question but it is a static number but you can assume that about quarter percent improvement in the margin in the yields as a real representation of how much we are carrying.

Devam Modi: As per the RBI regulations as a core investment company, the standalone entity could go up to a leverage of 3:7. So what kind of leverage would we targeting at L&TFH standalone level?

N. Sivaraman: I think it is important to note that there are 2 issues: One is that we need to continue to keep the dividend flow to be able to service this loan and the second is that interest on these loans is not deductable under the tax law, which means if I borrow 12% effectively on a pre-tax basis, it amounts to roughly 18% kind of borrowing cost. So we need to be careful about borrowing at the holding company level unless it is for investing in the form of a debt in the downstream entities. At the moment as I have said that we have got sufficient financial flexibility. So we would not like to borrow at the holding company level at the moment.

Devam Modi: What would be the long-term strategy of L&T Finance Holdings per se with so many diverse and different businesses like obviously naming a few construction, transport, farm equipment, agriculture, rural products, so you really see all those pieces, not another NBFC that comes to my mind that has all this diversity at house within it. So what would be the long term strategy of our company per se?

N. Sivaraman: Devam, I think I took pains to explain that it is not diversification. It is around four key skills that we have built our business and whatever falls within those skill areas we would definitely like to add so that the skills are better exploited. Around asset management, around understanding small borrowers, around understanding project flows. This is what we will build our business to be.

Devam Modi: Just some housekeeping questions. What would be the investment figure and cash figure as of 30th September for L&T Finance and L&T Infra?

N. Sivaraman: I think I will request one of my guys to give you some of those specific details. You talk to Mr. Viraj or Nandi, they will be able to give you this.

Moderator: Thank you very much. Our next question is from Mr. Yogesh Hotwani of IndiaNivesh Securities. Please go ahead.

Yogesh Hotwani: I have a couple of questions on Infra. Firstly, I believe in Quarter 1 we had some disbursal of somewhere around Rs. 600 crore. Now in Quarter 2 we have disbursements of around Rs. 1260 crore. Just wanted to understand where we are seeing these incremental disbursements happening, like in which segment?

Suneet Maheshwari: I think the two things that you must understand that the project disbursements happen based on project completion cycles. We have a fair amount of disbursements which are sort of built in with the prior sanctions or prior approvals that we have done. And the project implementation is happening over a period of three years. So, disbursements happen as the project completions are getting over. In the last, I would say 7 or 8 months ending till June, we did see some slowing of projects because the corporate sector was under some stress and they have been able to arrange or alliance to get some liquidity in their books plus they have decided to go ahead with some of their projects. So we have started to see the disbursements of their earlier projects actually starting to happen. So I think the reason why you see this increase is may be some incremental new business and some of the older projects queuing in for disbursements.

Yogesh Hotwani: So these projects are mainly into power or it is well diversed into other segments as well?

Suneet Maheshwari: They are all across our portfolio which we mentioned about. So they are spread across all our portfolios and it would be largely in the proportion of our portfolio distribution.

Yogesh Hotwani: I am referring to your slide number 18. You have mentioned that there is one account in Infra segment which has turned NPA. So can you throw some light on that account?

N. Sivaraman: We cannot really mention what the name of that client is but what we are trying to say is there is just one slippage that has happened which is not too large an amount.

Yogesh Hotwani: Talking about the gearing, I believe we are at 5.07 currently. Now the way we are growing the asset in L&T Finance at least we will get closer to a regulatory requirement which we have mentioned from 5.5.

N. Sivaraman: No, there are two entities. Which one are you talking about? L&T Infra Finance or L&T Finance?

Yogesh Hotwani: L&T Infra

N. Sivaraman: I think we have committed that the moment we start crossing the threshold of 5.25 we will add some capital.

Yogesh Hotwani: One thing about the provisioning, how much excess provisioning we are holding as of now in L&T Infra?

N. Sivaraman: If you see it on our Page #Number 16, the provision over RBI norms that they are holding is about Rs. 72 crore.

Yogesh Hotwani: I was just looking for the outstanding number.

N. Sivaraman: About Rs.100 crore roughly.

Moderator: Our next question is from Mr. Nischint Chawathe of Kotak, please go ahead.

Nischint Chawathe: Can we talk a little bit about what are the plans on any further acquisitions or how the excess capital that you have shown in the slide what exactly we utilize?

N. Sivaraman: These are the same questions got asked to me, what are the acquisitions plans are there for you. We are really not running around the city with a bag in our hand. I think if you look at it, it has been with a very specific goal and strategy and some of these, we may not have started by ourselves in a hurry but clearly these are business lines which were of interest to us and when these opportunities just present themselves we did look at it seriously to consummate them. As of now I can only say that there is nothing on the table for us to consider. I continue to maintain that where we are already present we would be reluctant to really acquire any company. If there is going to be complementary products definitely we will consider them. And we are not going to pay out any large sum of money to acquire in any case. That is the way we will look at.

Nischint Chawathe: On L&T Finance bit, I just wanted to understand if you could give some color on how the NPLs have played out and what could be the reason, some outlook on that front?

N. Sivaraman: On the L&T Finance side the increase in NPL is actually on account of a few corporate account slippages. In fact the retail NPLs have actually dropped as compared to 30th June number. We believe that these are reversible as we go along and while one or two might take slightly longer, some of this can actually be reversed before 31st March, 2014. But definitely by 31st March we should see a clearly stabilized number. This is what we are hoping and from there on improving.

Nischint Chawathe: Based on current delinquencies, do you see that, is it something that we are already close to the peak or how do we see in terms of the trending happening given the fact that you would have some sense on the current delinquency?

N. Sivaraman: There may be an increase of some 10-15% but that does not really stress us because we know the kind of accounts which are under stress, and even if they slip there will be a period of time by which they will recover. But we will continue to see an improvement in the retail book to some extent that will mitigate the increase in the gross NPA level.

Nischint Chawathe: Is that the reason why you would kind of slow down the business or that has nothing to really do with each other?

N. Sivaraman: NPAs cannot scare the lender because that is its business very clearly. But I think our selection criteria is definitely far stricter, we are looking to see it in the context of what we really need to look at on the ground. The kind of proposals that are on the table, either they are too good and very competitively priced or we have a challenge in terms of quality of the asset. So these are the two reasons why we will not be, if at all we do, not rather than any fear.

Nischint Chawathe: I guess you are referring to the corporate book.

N. Sivaraman: That is correct. On the retail book it is a question of opportunity like Construction Equipment we have seen a degrowth at the manufacturing level. So it will be not appropriate for me to expect but having said that the opening up some mines should give a fillip to the construction.

Moderator: As there are no further questions from the participants I would now like to hand the floor back to the management team for closing comments.

N. Sivaraman: It has been a period of stress for all of us. Hopefully, the outlook represented by the stock markets do tell us that things can be better from here and we also do see that with the amount of work that we have put in and also the response that we are getting from the market perhaps we are in a period of time when things will slowly start improving, we look forward to a better period from here on. Thank you.

Moderator: Thank you very much. Ladies and gentlemen on behalf of L&T Finance Holdings Ltd, that concludes this conference call.