Investor/Analyst Conference Call Transcript
October 23, 2013

Moderator: Ladies and Gentlemen, good day and welcome to the Q2 FY14 Earnings Conference Call of L&T Finance Holdings. As a reminder for the duration of this conference, all participants' line will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need any assistance during this conference call please signal the operator by pressing '*' followed by '0' on your touchtone phone. Please note that this conference is being recorded. I now hand over the conference to Mr. Shiv Muttoo of CDR India. Thank you. Over to you sir.

Shiv Muttoo: Thank you. Good evening and welcome to L&T Finance Holdings' H1 FY14 Earnings 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 in today's call may be forward-looking in nature and a note to that effect is stated in the presentation sent to you earlier. I would now like to request Mr. Sivaraman to provide his views on the results during the half year and his thoughts going forward. Thanks.

N. Sivaraman: Good evening. Thanks for joining the call. I hope you have had an opportunity to see the press release as well as the advertisement and the presentation which we have uploaded on our website. I would be using the presentation to cover the salient aspects of performance for the first half of the current year.

Starting with Slide # 4: 'Industry Overview', which I would quickly summarize: There have been a few positive points – the monetary situation seems to be coming under control and improving; the monsoons have been good, as a consequence of which the rural segment could continue to see robust consumption growth. The government has been making efforts to give a push to investments by clearing some of the large projects in both the infrastructure (especially power sector) and non-infrastructure segments.

These should perhaps help us see some traction on investments in about two quarters or so is our belief, but we will have to wait and watch. Some of these actions have been taken almost about a quarter and a half back, while the impact is yet to be seen in the economy.

On the challenges side, the continuing high inflation and consequent impact on the interest cost could be a dampener and impact industry performance going forward. The fiscal deficit seems to be at a precarious level, with the government having consumed most of their available budget within the first seven months of the financial year. My fear is also that government spending, which is one of the important liquidity and opportunity provider for the economy, seems to be under a cloud. Consequently, new projects and capital expenditure continue to get delayed. Thus these challenges balance out the positives. While there is a fairly optimistic outlook on the current account deficit, we need to wait and see how it all pans out and how successful the government would be in controlling the fiscal deficit.

Moving over to slide # 6: 'Highlights – Q2FY14', which is a quick snap shot of our focus areas and performance over the half year. Given the current environment, we have clearly focused on the B2C segment as a way of building our business and disbursements in the retail business. While not necessarily taking our eyes off the B2B segment, we definitely continued to remain cautious about lending to this segment. In the wholesale business, asset management or managing the stressed accounts has been one of the key focus areas along with looking for opportunities to further build operational assets in our portfolio.

The environment that prevailed in the last quarter was perhaps what we have not witnessed for a long time in terms of the liquidity stress and the cost of borrowing changing almost overnight. Our preference was towards maintaining a high level of liquidity, even if it meant that we have to incur some negative carry. Thankfully the negative carry was very marginal and has not impacted our performance in Q2FY14.

In the mutual fund business, it is heartening that the business volumes or assets under management have increased during the quarter. We are amongst the four-odd players who have increased the assets under management as compared to a reduction in overall AUM of most other players. In addition to that we have continued to maintain control over operating costs, and that helped improve financial performance. The ranking of our AMC moved up, from 16th to 13th. This improvement has been on account of the growth of our business even while others de-grew.

On the lending side, while the GNPAs continue to pose a challenge, the level of restructuring that is being sought to be undertaken by the consortium of lenders is also of concern. It leaves us with limited opportunity, but to work to ensure that these borrowers survive for the future and repay the loans. Year-on-year the growth in the loan book at 28.2% has been quite good, but you would have also observed that it has slowed down as compared to Q1FY14. This is a reflection of the cautious and selective approach that we are following on disbursements.

On the PAT side, despite increase in borrowing cost we saw an improvement in the margins in the Retail and Corporate segment while in the Wholesale segment it remained more or less flat. The credit cost did go up. However the TTM ratios other than the credit costs have shown consistent improvement, indicating that the business fundamentals continue to be improving despite a difficult environment.

Moving to slide # 7 which is an overview of the financial performance. The loans and advances grew by 28.2% to close to Rs. 35,500 crores. The disbursements have shown a healthy growth as compared to first half of last year. The NIMs as I was mentioning have actually shown a marginal improvement as compared to the first quarter and a good improvement as compared to the last year as a whole. PAT growth is about 21% for the lending businesses. Gross NPAs did move up primarily due to slippage of one account. The ROE has shown improvement as compared to the first quarter though it is marginally lower than the same period of last year. I would attribute all of this to an elevated level of credit cost that we have incurred during the year.

With regard to the investment management business, the average AUM for the quarter grew by about 10.0% to reach Rs.15,000 crores. The PAT before exceptional items has shown a profit for the second quarter while for the half year we reported a loss of about Rs. 1.8 crores. This is remarkably different from the first half of last year when we had a Rs.16 crores loss without including the Fidelity operations.

Slide # 8 is on the financial performance of LTFH at consolidated level. PAT without exceptional items for the half year was about Rs. 300 crores, which is a 13.7% increase over the same period of the previous year and for the quarter the growth was about 8.0%.

Moving over to Slide # 10, the key areas that I would like to highlight on the positive side - rural products continued to show extremely good growth, tractor volumes increased by about 21.0% and the microfinance segment continues to show robust behavior outside of Andhra Pradesh. We have been able to build our business and grow in this segment. Consequently the business did turn around to achieve marginal profits in the current year.

On the negative side, construction equipment volume growth for the industry was negative to the extent of 20.0%. It must be noted that it is an additional 20.0% reduction from the previous year. So for two successive years we have seen a volume dip of 20.0%. The commercial vehicle segment has seen a negative growth, while two-wheelers showed a positive growth for the second quarter. Overall, the environment in the commercial vehicle, auto and transportation sectors continued to be negative. This has been contributed to a large extent because of the freight volumes being lower, operational cost for individual operators have been higher; without them being able to pass on the cost increases to their clients. Added to these, inflation has also eaten into the disposable income. All of this has contributed to limited investment from small operators in adding assets to their balance sheet.

With regards to the Corporates – no surprises, scenario continues to be difficult with no significant capital expenditure and very few good financing opportunities coming our way. In light of this, the Retail and Corporate business focused on the B2C segments, while being cautious about the B2B segments - which is largely corporate, commercial vehicle and construction equipment financing.

On the Wholesale finance side, again at the broader level new capital expenditure has been extremely low. Some of the developments in the thermal power sector have been a silver lining in this segment. This includes forward movement in fuel availability, improving financial capability of the electricity boards, which definitely helps in creating demand for purchase of generated power and augurs well for the power producers. As you would all appreciate, even though there is inherent demand for power from the consumers, many electricity boards have been unable to buy power due to the significantly higher prices which has resulted in the capacity of some of the power plants remaining unutilized.

In renewable energy, most states seem to have reached their statutory requirement for buying renewable power while there are some murmurs around the current tariff for solar energy. But the regulators have been making sure that the original contracts are honored. So we see a reasonable level of stability in the tariff for solar power. Road sector has not seen much action - lack of land acquisition and to some extent the lack of bidding power with the developers have limited the opportunity for new road contracts. Telecom sector seems to be coming out of the challenges, but it will be sometime before we really see a full-fledged roll out of 4G. Even in 3G, the investments have been limited.

Moving to slide # 12 – 'Retail and Corporate Finance', the disbursements for the half year have grown by 14.0%.To some extent this has been supported by the addition of Personal Vehicle finance through the acquisition of FamilyCredit and consequently new product lines have been added. A few good corporate accounts, where we could put large volume of money to work, did help us in the first quarter. More importantly, the rural product finance which consists of tractors and other farm equipment has shown extremely healthy growth. As I mentioned in the previous section, while the tractor volumes in the industry grew by 20.0%, the volume of tractors we financed went up by 47.0%, which shows that we have gained market share. Similarly, in Personal Vehicle finance our volume growth has been very good. We ended up achieving a larger market share for financing in this segment. These I think, will continue to grow on the back of healthy monsoon as well as our expansion of network. This will help us improve market share in the future. You would have also observed that the volume of construction equipment and transportation equipment that we have financed has seen a decrease, more than the reduction in industry volume. This reflects our choice of being cautious and selective in lending to this segment.

On the book size, you will notice that the rural products finance on the back of strong disbursements has grown by about 43.0%.The overall book volume has gone up by 21.0% in the Retail and Corporate Finance segment.

Taking you over to the ‘Retail & Corporate Finance – Summary Financials’ on slide #13 - the interest income growth has been in line with the asset growth, whereas the NIMs have grown at a faster pace both at the half year level and also on a trailing 12-months basis. This basically indicates that our focus on improving margins has produced results. With regard to fee income, I would want to clarify a change in the presentation - since our dealer oriented businesses have picked up volumes, there is a payout or remuneration to the dealers which is partially compensated by the processing fee that we collect from our customers. Hence to appropriately represent the operating expenses, we have started adjusting the origination cost from the processing fee. So to that extent the numbers and ratios would be slightly different compared to those in the previous quarterly presentations.

Operating expenses, but for the addition of FamilyCredit have remained quite flat, again showing our commitment to control expenses. The credit costs have increased as a result of our foreclosure efforts and also due to stress in the corporate segment. So on a half year basis we have seen a 37.0% increase in credit costs. The credit cost in our case includes provision against NPAs, foreclosure losses, income reversals on NPA accounts and write-offs.

The PAT growth is about 27.7% for the Retail platform for the half year and on a trailing 12-months basis it is about 11.8%. The GNPAs have remained more or less steady from Q1 to Q2, giving us hope that this may perhaps be the peaking of GNPAs in the Retail and Corporate segment. But I would like to be cautious in guiding you to assume that the NPA situation has peaked out as the stress on the ground continues to exist.

Moving on to the ‘Retail & Corporate Finance – Key Ratios’ on slide # 14 – We have been able to pass through some part of the cost increase to our borrowers. The yields have moved up from about 14.33 to 14.55 over the two quarters. Net interest margin, despite the incremental cost of borrowing that we suffered in the second quarter, has actually improved by about 5 bps. But for the kind of the volatile environment, perhaps the margin improvement would have been better. For the next quarter we might see stable margins is what I would assume. I would not hazard a guess to say that the margins will actually expand for the next quarter, because some of the borrowings that we have done in the second half of the last quarter would perhaps continue in the third quarter and the effect of those increased cost will have an impact on our margin. The good thing is that the shorter end borrowing costs have actually come down. So if we are able to replace some of the borrowings that we have done in the second quarter with the CPs and NCDs, it is possible that we might still be able to see stable-to-improving margins. The fee income as I mentioned to you is after adjusting for the origination cost.

Operational expenses, again but for the addition of FamilyCredit which is a more retail business, have remained stable. Credit costs are about 1.57%, which shows a marginal reduction from the first quarter. But I would guess that the 4th quarter is perhaps when we will see some significant improvement in this. Till that time I would like to guide that the credit cost can remain flat. Again, in all our conversations in the past we have always indicated that while the NPAs might increase, the credit cost charge to the P&L account will remain more or less steady. ROE at about 9.63% is marginally lower than the first quarter, primarily on account of certain additional tax cost that we have had. I would see that improving in the next two quarters. Gross NPAs both on volume as well as on percentage terms have remained steady. We do have good capital coverage for all the businesses.

Slide #15 is on 'Housing Finance' - Since we are on an investment and growth mode at the moment, it may not be very relevant to talk about the ratios for this business. Suffice to say that we have seen good growth, we are expanding our network. The disbursement growth has been very strong and is across all the sectors - home loan, loan against property as well as construction finance. We do see construction finance providing us with a good traction to do origination of loan assets. The PAT is stable, but we still need to make investments in building the network. So I am not guiding you to anything on this front at the moment.

Moving over to 'Wholesale Finance' on slide # 16 – we have seen good growth on disbursements for the first half, a good part of it is on account of operational assets as well as some of the non-infra loans that we have originated during the quarter. You will observe that the share of operational projects in the total book has gone up to 33.0% from 28.0% of the previous quarter.

On the 'Wholesale Finance – Summary Financials' on slide # 17 – the interest income growth is about 29.0%, in line with the loans and advances growth. The NIM is slightly subdued for two reasons - one is that the debt-equity ratio has gone up and second is that we have added some high quality clients to our balance sheet. In addition to that, as I said we have been booking operational assets. Both of these have been at slightly lower yields. Consequently, there is a very sharp drop in the overall margins on year-on-year basis. Fee income - definitely the current environment does not encourage us to be in the market selling our services, but we consider this one of our focus areas going forward.

Other income of about Rs. 37 crores includes about Rs. 22 crores of capital gains on transfer of our seed assets that were originally booked on L&T Infra's balance sheet to the PE fund. I am happy to say that the PE fund has achieved a domestic close in the last quarter, after which we have been able to migrate two equity assets into the PE Fund. So we booked a gain of about Rs. 22 crores at a pre-agreed carry cost.

The credit cost in this segment has definitely been a matter of concern, but you can say that we have been more cautious than what the regulator requires. Consequently, our provisioning levels have been little higher than what the regulator expects. We do see that the rise in GNPA has been a result of one account which slipped into NPA status. I will also say that the overall restructured book has grown because of the stress in the environment and the need to enable the borrowers to become healthier over a period of time. The provision over the RBI norms is close to about Rs. 122 crores. This does not include the provision against NPAs or provisions against restructured assets. These are provisions against the overdue assets, assets which are overdue but have not become an NPA. This includes both provision against the principal and also the reversal of income that we have booked against these assets.

On the key ratios in slide # 18, you will see that most of the ratios are remaining stable both on a half year-to-half year basis and also on a TTM basis, except for credit cost which has jumped as compared to the last year. We continue to see that the provision for NPLs or stressed assets could increase over the third quarter. We might see some respite by the fourth quarter. The overall gearing levels have remained more or less stable over the last two quarters while it has gone up as compared to the previous year.

Moving over to slide # 19 – 'Investment Management': We did talk about it briefly in the opening remarks. While the average AUM growth for the industry was a negative 5%, we grew by about 9%. Average AUM composition has undergone a marginal change, but has remained very stable as compared to the first quarter. As compared to the short term (rather the overnight liquid) money, most of the growth has come in duration funds as well as some of the opportunistic debt funds where we have been able to grow some volume. Cost control has been one of the key focus areas and as a result of which you will see that the PAT for the second quarter is about Rs. 1.7 crores. If we compare it with the same period last year, it definitely has been a big improvement. But I will say that part of this has come through an accounting change which will help us book revenue as well as cost on a matching basis. As a result of this, the amount we have reversed is about Rs. 3.3 crores of expenditure that we had incurred in the first quarter. But if you take the half year as a whole there is no change and as such this can be representative of normal operational profit.

I will conclude this section by saying that we are well on our target to achieve a break even in this business for the current year. Our focus going forward for the current year will remain around the debt products which will be short term fixed income products as well as FMPs. This will be a key way of building our AUM, given that equity continues to suffer outflows and the lack of enthusiasm amongst our investors into putting money into equity schemes.

Slide # 21 is on Wealth Management – Suffice to say that we have seen good traction on the assets. We have built the average AUS from Rs. 2,800 crores as of Q1FY4 to about Rs. 3,600 crores as of the end of half year which is heartening. The client base has crossed 1000. Though it is a young business, it is definitely showing good buildup of assets and clients.

Slide # 22 is on 'Other updates': Banking License – Yes, we are engaging with RBI in providing clarifications to them. We will await their next steps. Infrastructure Debt Fund – we just about received the RBI approval to commence operations. We do have some level of seed assets already booked and sitting in the L&T Infra balance sheet. So we now have an opportunity to kick-start this business almost immediately, subject to some more compliances that we need to fulfill. The other aspect is that there has been some improvement in the economics of the IDF as NHAI has reduced the guarantee fee from 50 bps to 5 bps, government has allowed access to SARFAESI as a way of settling any NPAs and has also allowed filing shelf prospectus to speedup fund raising. With this I will now leave the floor open for questions.

Moderator: Thank you very much Sir. Participants, we will now begin with the question-and-answer session. We have the first question from the line of Parag Jariwala from Macquarie. Please go ahead.

Parag Jariwala: Your presentation says that the restructured asset has also gone up quarter-on-quarter. Can you give me what is the outstanding restructured asset as of September'13?

N. Sivaraman: As of September'13 it is 5.2% of the total outstanding book of the Infrastructure Finance business.

Parag Jariwala: What was it last quarter?

N. Sivaraman: 3.9%

Parag Jariwala: Can you bifurcate in terms of sector or number of accounts, any bulky accounts or CDR cases?

N. Sivaraman: 8 accounts have been part of the restructuring process. Let me say that we do see this rising in the next quarter given the number of proposals sitting before the CDR forum.

Parag Jariwala: And can you quantify the number of cases?

N. Sivaraman: It also depends on how quickly you are able to conclude this at the CDR forum.

Parag Jariwala: Yeah but can you quantify the restructuring pipeline similar to what banks do?

N. Sivaraman: For us?

Parag Jariwala: Yeah.

N. Sivaraman: I will refrain from doing that because; sometimes those who had filed the application for CDR have also dropped out later. But suffice to say, there will be an increase in the next quarter.

Parag Jariwala: In terms of percentage, what is the provisioning you follow for restructured assets?

N.Sivaraman: 5% is what we carry on principal, in addition to that carried for the income, in line with RBI requirements. We also provide for the NPV of the interest differential as a sacrifice right up front.

Parag Jariwala: Basically, NPV loss, right?

N.Sivaraman: Yes, which is actually positive for the future years because we will be drawing from this NPV provision in the future years.

Parag Jariwala: The increase in gross NPLs is only due to one account or is it majorly due to that one account?

N.Sivaraman: For infrastructure segment it is just one account.

Moderator: Thank you. The next question is from the line of Saurabh Kumar from JP Morgan. Please go ahead.

Saurabh Kumar: My question was basically on the banking application. You have said that the NOFHC will be promoted by L&T Finance Holdings and our understanding initially was that L&T Finance Holdings will be the NOFHC. So was there any compulsion for you adopt this structure?

N.Sivaraman: The guidelines require no external shareholders in the NOFHC.

Saurabh Kumar: And since the other businesses will be out, the bank will just have the wholesale business? Can we assume that the operating assets of your lending business will be part of IDF?

N.Sivaraman: Not all of it, because we have operating assets across various segments - roads, power, etc. Power sector is not covered by the Build-Own-Operate-Transfer regulations. An IDF-NBFC format can only be done where the concessionaire acquires back the asset at the end of the concession period. There are some seed assets we carry which are eligible for migration to IDF, but there is also some limitation around the taxation requirement where it says that single party exposure cannot be more than 20% of the corpus. So it will have to be progressively done considering whatever seed assets we have on our balance sheet. But suffice to say that we are on a good wicket to get started.

Saurabh Kumar: So when you hint that there is scope to effectively manage the transition from the existing business to the bank in terms of managing the CRR/SLR norms, it will be done via a combination of probably shifting some operating assets and securitizing some others?

N.Sivaraman: It is not necessarily to avoid the CRR/SLR obligation. It is more to do with the way the business can be done more efficiently, that will be the primary driver. CRR/SLR itself is not going to be a daunting task. I am not indicating that 20% of our corpus will be in the IDF and Hire Purchase segment. Even if that is done, it only reduces about Rs. 6,000 crores on the current balance sheet. For the remainder, we will have to still fund CRR/SLR. It is more of business economics and business efficiency, rather than purely driven to avoid certain regulatory preemptions.

Saurabh Kumar: And two final questions from my side - one is on the Asset Management business. So we have broken even this quarter. So for the third and fourth quarter can we assume at least a no loss situation?

N.Sivaraman: I think it will be as close to that.

Saurabh Kumar: And finally again back to banking - as per your understanding, will you be allowed to tap into let us say the parent L&T's employee pool for basically building up your savings?

N.Sivaraman: Liability side, there is absolutely no challenge.

Saurabh Kumar: On the asset side there will be right? For example, IDPL?

N.Sivaraman: Asset side, yes. It basically needs to be arm's length and will have to be approved at the board level. It is not a prohibition. The approval process will be stringent.

Moderator: Thank you. The next question is from the line of Amey Sathe from JM Financial. Please go ahead.

Amey Sathe: Three-four questions. One is on the disbursement growth. So how do you expect the disbursement growth trend to be in the second half?

N.Sivaraman: I will ask Mr. Dubhashi and Mr. G. Krishnamurthy to answer you.

Dinanath Dubhashi: In the Retail and Corporate business, the trends would continue in terms of the distribution. In that sense B2B businesses will continue to be negative. We do not see any reason why there should be a sudden pick up in construction equipment or commercial vehicles. In the corporate segment, it is not as if the demand is not there. But we are being extremely careful in lending loans for general corporate purposes. We are doing deals which are very tightly structured both in terms of security as well as cash flows. This would mean that we would see flat to very small single-digit growth in corporate as well.

For the farm as well as personal vehicle sector, some of the numbers that you see like 44.0% growth in farm or 3-digit growth in personal vehicle, they may be moderated as the industry itself moderates. So in farm, during the first half, growth was 21.0% in tractors. All industry experts expect it to be more between 10.0%-15.0% for the year. As we are gaining market share, you can put a premium over this and that would be more or less the growth in farm. Similarly in personal vehicle – two-wheelers growth especially of scooters has been robust in the industry. We expect that to continue. In cars, of course our market is very small, just about a per cent. So we are not very much dependent on the industry growth. So in personal vehicle we will see similar growth coming in H2 also. In tractors, it might be a little more moderated than the 44.0% that we have seen in H1.

Amey Sathe: So is it fair to say the disbursement growth will be same as the second quarter?

Dinanath Dubhashi: Yes, similar. There may be a little more moderation in tractors. It may be slightly less than what we have shown in the first half, but otherwise, yes.

Amey Sathe: Because I think last year second half we had a pretty strong base?

Dinanath Dubhashi: Exactly. There is a higher base now for the second half.

G.Krishnamurthy: On the Wholesale side, there is a deceleration with no new capital expenditure in the economy. So typically we have done larger deals in renewable energy last year, but in the second half this year we expect to see a reduction in new project funding that we do in renewable. This is also because there are some regulatory changes happening, which means that there will be a smaller pipeline this year for H2 compared to last year. So having said that, our focus therefore will continue to be on operating assets across sectors, including thermal power, renewable power and transportation. In the non-infra segment, we have started project financing in a limited manner. So focus will again be on project finance rather than corporate finance and we should maintain the current pace of disbursements. There would not be any major upside.

Amey Sathe: So it will typically be?

G.Krishnamurthy: Flat with marginal improvement.

N.Sivaraman: What he is saying is that year-on-year it could remain marginally positive to remaining flat, that is the range of disbursement.

Amey Sathe: Another question on the personal vehicle finance. As per the first quarter presentation disbursement growth was shown as around Rs. 274 crores and as per the second quarter presentation for the same period it is shown as Rs.445 crores.

N.Sivaraman: We have reclassified the cars to form part of the personal vehicle segment for the sake of representing in a better manner. Cars used to be a part of the rural product finance during earlier reporting. We have reclassified it now as part of the personal vehicle finance segment.

Dinanath Dubhashi: The logic for that was that in car financing we were largely into rural areas. Now, as volumes increase we are getting into semi-urban and even urban areas. Hence we have moved cars from the rural products finance to personal vehicle segment.

Amey Sathe: At the consolidated level, our NIM growth is around 18% but our loan growth is around 28% and we have also reported around 10 bps margin improvement. So just wanted to understand why there is such anomaly that NIM growth is slower than the loan growth?

N.Sivaraman: As I said we chose to maintain liquidity by borrowing. To some extent if you add the other income, which is largely the income from mutual fund and dividend income (may have been around Rs. 40 crores or so in this quarter), to the net interest income then you would be able to match the growth numbers. I suggest you do not strictly go by the advertisement for this purpose. We have done appropriate reclassification in our presentation; do refer to it as it is far better represented. You would see that the NIM growth in retail is higher than the asset growth and the interest income growth even in the consolidated numbers.

Dinanath Dubhashi: Please have a look at Slide # 7.

Amey Sathe: And does this also explain the increase in other income which is of Rs. 87 crores?

N.Sivaraman: That is what I was referring to. As I mentioned there are two components of other income - there is the Rs. 40 odd crores of investment income plus another Rs 22 crores of income on transfer of assets. As I mentioned we transferred some seed assets which were sitting on L&T Infra balance sheet to the PE Fund on achieving our domestic first close of the fund.

Amey Sathe: On the banking aspect, LTFH will be having a NOFHC. So does the L&T parent need to dilute its stake?

N.Sivaraman: Yes, it has to dilute its stake. L&T is looking at options for the same. In any case before August 2014, L&T will have to bring it down to 75% and then they have close to around 12-18 months to achieve the rest of the dilution.

Amey Sathe: I think L&T needs to bring it down to 51%, right?

N.Sivaraman: 49% on voting equity.

Amey Sathe: Just a last question on the asset quality trend. Do you witness any stress especially in two-wheeler finance portfolio over the last 3-6 months kind of a period?

Dinanath Dubhashi: Not really. We track this portfolio on a bucket-to-bucket basis. Two-wheelers for example, we classify as GNPA post 180 DPDs, but things may start going wrong from the second or third bucket itself. We have been seeing very steady trends - neither have they improved tremendously nor have they gone worsened greatly.

Moderator: Thank you. The next question is from the line of Nischint Chawathe from Kotak Securities. Please go ahead.

Nischint Chawathe: Just trying to understand a little bit on the Housing Finance business. You do not give the detailed financials. If I look at the last year, I think this particular business reported profit of around Rs. 24-25 crores and in the first half there was hardly any profit. So just kind of trying to understand what is happening out there?

N.Sivaraman: At the outset let me say that to give you very fine details of financial performance at this point of time maybe not very relevant. If you look at the capital adequacy, it is so high as compared to the asset base. So if I talk about NIM, it will be quite high and it may not be the sustainable NIM for the future. The second important aspect is that operational expenses will also be high relative to the assets because we are still building traction and we have to use the capacity fully. This is the reason we are saying that this is the business which is in the build mode, we need to focus on the key areas of network expansion and asset growth.

This is the only reason. There is no other intent behind that. As far as this performance is concerned the previous year the portfolio got readjusted on acquisition. So some of these were the provisions released on cleaning up of the balance sheet. That is why you would have seen a slightly higher PAT. But if you look at Q4FY13 and Q1FY14, they are very representative numbers for you to really understand the performance of this business.

Dinanath Dubhashi: We have listed debentures and the results are published in public domain, Nischint. So you can definitely get more details from that.

Nischint Chawathe: On the Retail business you basically mentioned that there was a reclassification of the fee income and fee basically gets adjusted with the operational expenses line item.

N Sivaraman: It is other way around, Nischint. The dealer payout gets adjusted from the fee.

Nischint Chawathe: If I optically look at the numbers I can see the fee going down but somehow the operational expenses have remained flat. I am looking at quarter-on-quarter numbers.

N Sivaraman: Last quarter has also been adjusted.

Nischint Chawathe: If I look at the fee income I think there is a sharp drop between the first and the second quarter.

N.Sivaraman: In absolute terms in the first quarter fee income was Rs. 9.9 crores, in the second quarter it is Rs. 10 crores.

Nischint Chawathe: In the Infra business on the other income, I think you said you booked income of around Rs. 22-odd crores. This is at a pre-agreed price and what is the yield that you get on this?

N.Sivaraman: This for us is a normal PE operation. Yes, this was at a pre-agreed cost of carry with the LPs as they joined us.

Nischint Chawathe: Cost of carrying would be like what percentage if you could give?

N.Sivaraman: It is around our borrowing cost.

Nischint Chawathe: So this is basically a funding cost that could have been accrued?

N.Sivaraman: Yes, there is no valuation here.

Moderator: Thank you. The next question is from the line of Devam Modi from Equirus Securities. Please go ahead.

Devam Modi: Just wanted some more color on two segments. One is the Supply Chain segment wherein you have grown quite strongly in the Retail business and also the Transport segment in the Infra business wherein we got a strong growth in this quarter?

G.Krishnamurthy: In the transport segment we have lent to the operating assets, some of which are seed assets for the IDF. So focus has been on financing operational, annuity and toll projects.

Dinanath Dubhashi: With regards to supply chain, I hope you are looking at the same numbers. Slide # 12 shows disbursement growth is -8.0% for supply chain.

N.Sivaraman: This is half year to half-year.

Devam Modi: I am looking at the second quarter number; I am looking at the quarter more than the half year.

Dinanath Dubhashi: Second quarter is Rs. 1,251 crores as against Rs.1,335 crores in Q1.

Devam Modi: A large part of the disbursements that we have done is dominated by supply chain, so in this context could you provide more color on this particular component?

Dinanath Dubhashi: Disbursements in supply chain have always been a large part of the overall disbursement composition. This is because every supply chain disbursement is for 60 days. All other disbursements are for 3-5 years. So you cannot put it in the same bucket as other products. What you will see is that even H1-to-H1 or Q-o-Q the growth has been slightly negative. It is mainly on account of yield management, as in the second quarter we increased the yield on supply chain which perhaps led to flight of business to some other banks from the main anchor company. So we have been very steady on our yields here – increased the yields as the cost increased and that has led to the drop. We expect that further drop may not continue, but at best it will be a flat growth.

Devam Modi: What will be the yield in the supply chain business?

Dinanath Dubhashi: It will be around 12.5 % to 13.5 % depending on the customer.

Devam Modi: You just mentioned that the transport sector assets are mainly operational assets for the IDF. So is there any sort of cost of carry that has been pre-agreed over here?

G.Krishnamurthy: No, there is no cost of carry which has been pre-agreed, it will be based upon a transfer pricing policy which we have that is dependent upon the prevalent bond yields at the point of transfer.

Devam Modi: So basically in this business what will happen is that the capital deployed in this asset will only yield you a bond yield. I mean they would not yield the natural profitability like what a normal lending business would yield.

G.Krishnamurthy: It is benchmarked to the bond yield, not based on a bond yield.

N.Sivaraman: At the time of transfer, the discount rate used will be benchmarked to the bond yield prevailing at that time.

G.Krishnamurthy: Essentially, the current market price at which it will be transferred.

Devam Modi: In simpler terms we can expect similar profitability to what the NIMs of the lending business would provide?

G.Krishnamurthy: These assets are already on the books and our earnings are appropriated to the current interest rates.

Devam Modi: So this will be a one-time fee income as and when the transfer will happen?

G.Krishnamurthy: Yeah, if at all, it could be a one-time discount, depending upon the way interest rates move.

N.Sivaraman: But on a consolidated basis it will not make a difference.

G.Krishnamurthy: The entire disbursement in transport segment is not towards IDF. What you need to understand is that only a portion of the disbursements will be transferred to IDF as IDF has got its own eligibility conditions on how much they can disburse towards the project.

N.Sivaraman: The other important aspect is that maybe it can result in some margin expansion because IDF is AAA borrower as compared to AA+ borrowing rating for Infra.

Devam Modi: What is the amount of assets that would have been transferred to the PE Fund? You said you got capital gains of around Rs. 22 crores. So what would be the amount of assets that we would be looking at over here?

N.Sivaraman: About Rs. 150 crores were transferred.

Devam Modi: So there were housed for a period of more than 1 year with us?

N.Sivaraman: That is a good conclusion.

Moderator: Thank you. The next question is from the line of Jaskirat Chadha from ICRA Limited. Please go ahead.

Jaskirat Chadha: I had a couple of questions on the net worth of the Wholesale Financing business. When I come to the slide I see that the net worth has increased from about Rs. 2,400 in June to Rs. 2,700 in September that is about Rs. 300 odd crores. Correspondingly, the profit was only about Rs. 100 crores. Has there been some additional equity infusion of Rs. 200 odd crores in the Wholesale balance sheet?

N.Sivaraman: We infused some additional equity in one of the entities which supports the Wholesale lending business in line with the asset growth that has happened on that balance sheet.

Jaskirat Chadha: Similarly, on L&T Finance, when I look at the net worth movement between June and September there is a marginal decline from about Rs.2,894 in June which has gone down to Rs. 2,870 in September, whereas in the quarter there was a profit of about Rs. 70 odd crores.

N.Sivaraman: There was an interim dividend paid by L&T Finance.

Jaskirat Chadha: My final question is what would be the size of the standard restructured assets on the Infra balance sheet?

G.Krishnamurthy: Proportion of restructured assets is 5.2%, purely based on L&T Infra's balance sheet. If we consider at the Wholesale business level it is around 4.7%.

Moderator: Thank you. The next follow up question is from the line of Amey Sathe from JM Financial. Please go ahead.

Amey Sathe: One question, you mentioned that a loan slipped into NPL for Infra. Can you let us know which sector that loan actually came from, any sense on who is the borrower?

G.Krishnamurthy: It is a non-infra asset which is currently under CDR and awaiting conclusion of CDR.

Amey Sathe: It went to CDR because of some cash flow issues?

G.Krishnamurthy: Yeah, it is a liquidity mismatch which they had and buildup of receivables. That is the reason why it went to CDR.

Moderator: Thank you. Participants that was the last question. I would now like to hand the floor back to the management of L&T Finance Holdings for closing comments.

N.Sivaraman: Thank you very much for participating in the call. In case you have any other questions after you have done deep-dive analysis, please feel free to write to us, we will be happy to respond. Thank you.

Moderator: Thank you Sir. Ladies and gentlemen, on behalf of L&T Finance Holdings that concludes this conference call. Thank you for joining us. You may now disconnect your lines.