L&T Finance Holdings Limited
Q2 FY18 Earnings Conference Call Transcript
October 27th, 2017

Moderator: Good day, ladies and gentlemen and a very warm welcome to the Q2 FY18 Earnings Conference Call of L&T Finance Holdings Limited. As a reminder, all participant lines will be in the listen-only mode. Please note that this conference is being recorded.

I now hand the conference over to Mr. Shiv Muttoo from CDR India. Thank you, and over to you, sir.

Shiv Muttoo: Thank you. Good morning, everyone, and thank you for joining us today for L&T Finance Holdings Q2 FY18 earnings conference call. We have with us on the call today Mr. Dinanath Dubhashi, Managing Director and CEO, and other senior members of the management team.

Before we proceed, as a standard disclaimer, some of the statements made on today's call may be forward looking in nature. A note to that effect is provided in the Q2 results presentation sent out to you earlier. I would now like to request Mr. Dubhashi to kindly provide his thoughts on the Company's performance and the strategy going forward.

Dinanath Dubhashi: Thank you, Shiv. Good morning everybody. So here we are at the end of six quarters of very successful implementation of our strategic business plan of 16 quarters and somewhere little less than halfway, I believe that we have remained focused to the plan. Our success actually has been to stay steadfastly focused to the plan and have been able to achieve results, which are actually little ahead of the plan. The tenets of what we have done have been pretty simple.

First and foremost, it has been execution focused. Everything has been planned to the meticulous details, every part of the strategy has been converted to projects as we have met over the last six quarters, I have talked about it. People, teams have been responsible for each of the projects and I believe that if I have to point out a single factor, why we have been able to deliver quarter after quarter and are pretty confident of delivering for the next few years is because of this discipline that we have put through.

In financial terms, the ROE and the profits, the results that we are delivering comes from a very few, very simple financial tenets. I've been talking about them, and I will repeat them once again. Number one, growth in our focused business; as you would see there is 81% growth in disbursement and 23% growth in our focus book. Where is it coming from, well if you see the presentation, it is pretty all round. If I can talk about a few strengths that we have build through this execution focus, through the center of excellences that we have been building on.

And business wise, if you see, what are the strengths that we have built which is enabling this kind of the disbursement growth quarter after quarter? In rural, very clearly, the digital and analytics focus is helping us identify very very specifically, the areas of growth, the geographies of growth, the models where we should lend and in fact, the customer to whom we should lend.

OEM concentration, specific OEMs, desired OEMs, really increasing relationships with these OEMs and most importantly turnaround time coming through continuous digitization. If you take Housing, we have found our sweet spot in using the Group synergies, lending to ‘A’ category and ‘B’ category builders using that Group synergies, monitoring those projects very closely, monitoring the early warning signals, monitoring progress of collections in those projects. And most importantly, converting as much as possible of that to retail. No doubt that the last part of it is still in early days, but again we are making quarter-on-quarter progress on that.

As far as Wholesale is concerned, core sector expertise and the infrastructure expertise, I think, now we have very clearly established leadership positions in our core areas of renewables and road refinance, also transmission. And our underwriting and the sell-down skills which I think, now everybody is accepting it as a sustainable advantage that we have built.

Add to that, the turnaround time that we have been able to establish, clearly the company which can assess the project fastest and give our assistance, the fastest in the market. These are strengths that we have built. These are strengths not dependent on just cheap cost of funds. These are strengths which are more sustainable and definitely will hold advantage to us as we go ahead. Mutual funds or fund performance, six funds, equity funds in the top quartile and of course, the results are very obvious.

Wealth, the open architecture and the professionalism that our relationship managers specialize in, again once again the growth in this business, the growth in the profitability that you can already see. So putting it altogether, the center of excellences that we are building in each and every of the business, is bringing the growth of each of this business to play, to increase the overall profitability.

Second tenet has been sticking very steadfastly to running down, painstakingly running down the non-core book. As you know, we had initially planned of selling it all down in the first three to six months, we were not successful and we could sell-down in just about Rs.350 crore or so of it. But the team has stuck to it and slowly but surely this rundown book is coming down and coming down with very minimal hit to the P&L. As we speak, it is down to Rs.2,000 crore and now you would all accept that on a Rs.70,000 crore balance sheet, it is very negligible.

The third tenet is fees, you saw 153% increase in fees. We have achieved the highest ever fees, quarterly fees this quarter. Underwriting, sell-down, we started with infra and it is slowly moving to all other businesses as well. Underwriting either taking on our balance sheet or just underwriting and then selling down has become a way of doing business for us, it's just a way of being. And at every deal, we not only look at the profitability from NIMs, but the team is completely totally trained now of thinking NIMs plus Fees for every deal. You take Wholesale, you take Housing, you take Rural, the emphasis on fees now goes across the organization, and we are very confident that the number that we have shown for the last three to four quarters is very sustainable and can continue.

And last but not the least, expenses; you would see that with all the growth that we have shown, overall expenses have shown just about a 4% increase, cost to income ratio is very much in control, and this is despite the investment that we are doing in digital, analytics and even simple investments like branches and people.

The Rural growth, the retail Housing growth doesn't come without this kind of investment. But our ability of predicting where the growth is going to come and opening branches, putting people couple of quarters before in exactly those areas are helping us increase productivity of these people, drawing full productivity of these people and then because of that, the expenses are now more than expenses becoming investments, getting us income quite quickly after these expenses having done, and hence the cost to income ratio is remaining in control. Once again, we see a very steady trend now of this ratio as well.

All this, P&L factors business wise, along with complete control and transparency on asset quality and provisioning, we have been very transparent in saying, wherever Wholesale legacy problem is, where it is likely to reach perhaps and you know we have a small increase in NPA from last quarter, in Wholesale it is well in line with what we have talked about, what we have indicated that this is where the stress is likely to reach and the provisioning also is absolutely well in line with what we have predicted, what we have planned to do and I can assure you that all those provisioning levels will be reached by the end of this year.

As far as Rural is concerned, we had said that September will see some seasonal spike. There has been a small seasonal increase maybe, but definitely not spike. And full kudos to the efforts of the team and more importantly, the control that we have been able to put on collections using data analytics. Very specific targeted efforts on collection have helped us keep our debtors and NPAs in control even in a quarter where rural NPA should normally, logically should have spiked. The industry results are still coming, but I believe that our collection efforts, we have shown a divergence from the industry and we have shown good numbers as far as the asset quality is concerned. As we go ahead, in the third quarter anyway, these NPAs are expected to come down.

So this is, as far as the basics are concerned, sticking to these tenets, five basic tenets have helped us achieve an ROE, which is not only more than the 15% mark, but the best ever and also the highest ever fees. So generally speaking, we see ourselves sticking to the path that we have put in place till 2020, in fact being slightly ahead of that.

As we have grown in confidence of our execution skills, as ROE has approached higher and higher levels, we have also added a few dimensions to this single focus of ROE. One of the most important dimensions that we have added is that we have been more and more confident of Growing Fearlessly, of cranking up our growth as we have gone ahead. If you actually see our balance sheet growth, as we have gone ahead quarter to quarter, you will see how growth is being cranked up. But most importantly, leave out the number, but the confidence of the organization of Growing Fearlessly is increasing It is coming out of very clear quarter by quarter building of a center of excellence, of a right to win in every single product, which is of course, helping us get market share.

But more importantly a mindset, that with the right risk controls, the right risk framework in place, the dashboards, the early warning signals that we have put in place, businesses are now feeling more protected, more confident that as they grow, accidents are not going to happen. This is the hallmark of this Company. Calling our growth fearless growth is really the hallmark of this. Fearless doesn't mean reckless.

In fact, if you see the percentages of growth, we are slowly cranking it, but the fearless mindset that the businesses are developing now they don't have to keep looking back over their shoulder, because they know very clearly what they can do, what they cannot do. Mistakes are less likely to happen, but even more important, the early warning signals that we have put in place give us the confidence that if mistakes happen and they do, most certainly they do. How do we come out of it pretty quickly. I would actually give you some examples of the kind of risk guardrails that we are putting. It is a part of the presentation, in fact, if you can come to page nine. In Rural, the risk guardrails we are putting is reflected in sourcing, very analytics led acquisition. In fact, normally any retail business will go from disbursement, you will first do disbursements wherever you can increase market share, then of course, comes credit; as you source customers after that you do credit, and then finally you do collection.

We have actually perfected a method where it goes the other way around that we look at our collection record, at our portfolio quality, at our loss given defaults of various models in various areas, geographical area and based on this the credit matrices of that particular geography, for that particular model is decided and hence now the teams are very clear that which OEM, which dealer, which geography, which model, they can go completely aggressive. In fact, targets to people, targets to branches are dynamically given monthly or quarterly. This has actually helped us to outperform the market and be confident of our sourcing as well as portfolio quality.

As far as Housing is concerned, very clearly our risk guardrails showed that we should to move to A & B category builders. We used our group synergy to move to them. If you see, continuously we have taken reduction in yields and moved to safety in developer funding. In fact, there is again a characteristic change in this kind of lending. We no longer do developer funding as a sort of byproduct of doing retail housing finance. It is actually almost on the contrary; that retail housing finance will be coming out of developer funding.

Developer funding is our strength, it is the strength very clearly coming from the synergies with the group and also with the knowledge, with the strengths, with the early warning signals, risk guardrails that we have put in place for this product. And now retail will more and more be directly sourced from the loans that we have given to these developers. A strong ability to assess promoters, strong ability to assess the projects, keeping a rigorous check on the portfolio quality and early warning signals is what is helping us, this kind of risk guardrails are helping us going ahead and be aggressive in this business.

As far as Wholesale is concerned, we are very clear on the risk that we are going to avoid. A lot of talk about risks emerging in the renewable sector. Right from beginning, we have avoided risk related to power purchase agreements, land acquisitions, equity inflow, foreign exchange, evacuation. We have put in place methods and ways to avoid this or in fact, most of the projects we all together avoid this kind of a risk.

Operational risk is limited by putting in place very strong early warning signals. Very clear limits have been put for sectors, for promoters group, for counterparties. These are the kind of things, these are only illustrative, for every product, for detailed product, we have got such risk frameworks in place. Now this helps us and why was I elaborating on this is that this helps us in making businesses fearless to grow.

So after talking about earnings, where the earnings, where the profit is coming from and after talking about earnings growth, I will come to the last dimension that we have added to our plan, which is variability of earnings. I've already said that we aspire to be a company, which delivers steady ROE and growth year after year, quarter after quarter. We are well aware that we are very early in this journey and the best is really yet to come. But we are preparing with the will and meticulousness that we have been used to.

The two aspects that we want to put in place for minimizing variability of earnings, of course, is the risk framework, we have talked a lot about that and secondly it will be counter-cyclical provisions. We are looking at not only the provision coverage ratio, you have seen that obviously it has gone up from last year, but it's not a ratio that we follow that doggedly.

We, of course, provide based on our probability of default and loss given default, but the ratio which is perhaps more important to us is what is the total provision that we are carrying on our balance sheet as compared to the total balance sheet, okay. And if you would notice, steadily quarter by quarter, we have built up these provisions. We were less than 2% of balance sheet coverage that is total provisions upon total balance sheet in March 2016. In March 2017, we reached a level of more than 3% and as we speak, we are more than 4% of this ratio. As we move into Ind-AS, we will try and move towards the method of continuously providing counterproductive, counter-cyclical provisions as we go ahead every year.

I will just give you an example. Let's say a business-like Micro Loans, the kind of model that we are trying to build is, give steady returns year-on-year in the micro finance business as well. For that, we know that credit cost of 2.5% to 3% per year will definitely come in a business like Micro Loans. However, unfortunately, they will not come every year; they will come as 12% to 15% credit cost every four to five years.

Now as a philosophy what we will try to do is take counter-cyclical provisions every year that any time this event happens, the balance sheet is always ready for it. Today, the regulatory framework doesn't allow for that, but as we move to Ind-AS from first quarter next year, the company will slowly and surely move toward this framework and there our dream of having the company, which shows excellent earnings and excellent earnings growth and extremely low variability on year-on-year, quarter-on-quarter profits will be on its true journey of completion.

With that, let me just conclude once again of assuring you that the plan that we have put in place is well on its course. In fact, we are ahead of the plan, but most importantly, I have been asked what next. What next is very clear, setting up a company which gives good return, excellent growth and low variability in earnings. We believe now projects are on, efforts are on to establish such a company.

Thank you, and we are open for questions.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. We will take the first question from the line of Kunal Shah from Edelweiss. Please go ahead.

Kunal Shah: Congratulations Sir, great set of numbers Sir, firstly in terms of growth you have highlighted, how we are penetrating, but just two, three questions in terms of, how many of this would be say the balance transfer, okay, in the various segments of where they were in terms of rural, two-wheeler. So we are taking away or maybe the people are shifting from some other existing financiers to LTFH and even on the real estate side. So how much would be say the overall balance transfer cases or how much would be like really new wherein we are expanding the market itself in terms of the financing need?

Dinanath Dubhashi: Okay. So I think, rural this answer is very simple. Rural it is 100% new, obviously. All other businesses, all the time, it will be always be a mix of balance transfers as well as new businesses. Balance transfers is such a thing that it is always inwards also and outwards also, right. So we keep attracting business from others and we keep also losing our assets to others, so it's a part of doing business. And as long as you are sure, that you are not quote unquote "evergreening something". It is just competitive balance transfer that you are doing a project, particular project has changed risk parameters. It has progressed in terms of risk parameters. Your understanding of risk or your perception of risk is superior to the bank that he has borrowed from, the customer has borrowed from. We can always do. So it will always be a mix, I mean, specific numbers, I wonder whether we even monitor. But definitely we're not giving out the specific numbers. But it is nothing absolutely out of trend or alarming that we are only doing existing balance transfers or anything like that. It's normal business as usual.

Kunal Shah: Yeah, because since we are growing at such a pace and almost like, say, such a significant disbursement of Rs.32,000 crore in the overall market. So just wanted to know maybe, so in terms of the profile of customers what really is making them shift from, say, other finances to LTFH. So what is our competitive edge in few of the product segments, okay. And once, maybe since we have invested a lot into it recently, so once this stabilizes, then maybe in FY19 and FY20, what could be the steady state, or maybe then the ideal disbursement growth, which will continue, definitely it's much higher in the first half. But how do we look at into FY19 and FY20 as well?

Dinanath Dubhashi: Okay. So I will answer the last part of your question. And I think it would be very good to be very specific in answering the first part of your question. And I would invite my three lending Chief Executives to give short answers. The kind of the 80% growth in disbursements etc. are obviously, I mean, if you do them year-on-year then, it will be fantastic. But let us talk about CAGRs. I think something like 30% plus growth in disbursements overall is what we can easily see for the next couple of years, two to three years, we don't see any issues there. And after sell-down a book growths of early 20s is what we are foreseeing at this point of time. So if that gives a very specific answer to your question on the numbers, I would now invite Virender to talk about how we attract business in Wholesale, Sunil and then Srikanth.

Virender Pankaj: Good morning. Wholesale business, for example, we have certain focused products like our Infrastructure Debt Funds. That is designed to take over existing operating stable road assets from existing lenders and refinance, that is the structure of IDF. IDF is not supposed to do a green-field asset. So by a definition and strategy, we would be taking over assets from existing lenders and providing a structuring solution, which adds more value to the project compared to before. On our other areas of transmission and renewable, and at times on under construction road projects last mile financing, it'll always be a mix of refinancing of operating assets v/s green-field assets. And we also lose some projects to competition, but if in relative terms we gain much more than we lose, and it comes from the solution which we provide. However, because we are constantly also in down selling more, we do share our credit and exposure with banking system subsequently. So hence, the profile of lenders might change, but what gets acquired could be far larger than what stays in our book. If you intend to conclude from this, the pace of CAPEX in India, I don't think, since we are there only in few products. It'll not be to right to conclude from the level of activity of refinancing, but it's a good mix of both.

Sunil Prabhune: Hello, good morning. To briefly speak about sources where the growth is coming from, obviously, for rural balance transfer is not really the point. It's about how we are acquiring these new customers, or if you start with our Micro Loans business, Mr. Dubhashi earlier mentioned, how we have done investments upfront, which are paying for us now in terms of people, in terms of our network and so on. So to give you a very small example, 17% of my business in Micro Loans in Q2 came from the branches that did not exist prior to the present FY. So clearly our approach of going into underpenetrated areas that have better re-payment track records is what is paying us rich dividends. So this has seen us expanding into states such as

Assam, such as Bihar, and expanding into districts in some of the states that we are at. If you look at a business like two-wheelers, clearly our proposition has been convenience to our customer by virtue of being able to make a credit decision in under 10 minutes, and actually 90% of decisions being taken less than two minutes. So before the test ride of the customer is over, we are able to tell the customer whether we can or we cannot do that particular transaction. This makes us a preferred choice with the customers that we have been able to serve. On the farm side, very clearly, our strong coverage of the entire value chain starting with OEM relationship, the dealer relationship and obviously one of the best in class turnaround times in service proposition to the customer is helping us attract the new customers that we have been able to do across the first half of this year.

Srikanth JR: Yeah. Two key points as far as our real-estate business is concerned. One is like Mr. Dubhashi mentioned earlier, our focus is on the large developer space, the Cat A and Cat B space. So fundamentally the approach is not to go with just one product approach, but to provide them a complete solution over the entire project lifecycle. So it could be not just a plain vanilla construction funding, but something at an early stage or at a pre-approval stage, right up to the last mile inventory funding stage. So a comprehensive product coverage is important. The second point, which is important for these developers is to give a solution for each specific project, which is also comprehensive. For example, I mean, don't burden the cash flows when the project is under construction and start having a structure, which would demand repayment while the project is under construction. So our solutions typically ensure that the project is completed. A residential project in India from a Cat A developer as long as you give them enough time to complete the project will sell and then there is enough time for us to be repaid and profits to be paid by the developer. A lot of the funding which has happened in the past have just look at a very straightforward plain vanilla approach of having three to five years irrespective of the stage of the project or the type of the project and which has led to difficulties. So these two things are, I would say, probably differentiate us a little bit from the rest of the players. And also, of course, our ability to underwrite larger tickets where required, to give a more complete solution for the developer.

Moderator: Thank you. The next question comes from the line of Karthik Chellappa from Buena Vista Fund Management. Please go ahead.

Karthik Chellappa: Congrats on a great set of numbers Sir, as far as our two-wheeler portfolio and farm equipment is concerned, would you be able to share the volume numbers that you did this quarter? And how will this volume number compare with, let's say, the market share composition of the industry for both two-wheelers and farm equipment?

Sunil Prabhune: First in terms of broad numbers, we would have funded about 16,000 tractors in the quarter that has gone by. As you would agree with me Karthik, that market share numbers, particularly in September quarter, are dicey numbers to give, because of the charging of the pipeline that happens in September leading up to the festival season. But we believe our market share there to be around 11% or so. Second nuance of your question is about, how does our OEM proportion within our portfolio compared with that of the broader market. On the farm side, I would say that it largely mimics the market presence of the leading OEMs. I would simply recall that there is a specific strategy that we have put in place based on our significantly differentiated portfolio performance. There were certain OEMs that we had called out as our preferred OEMs. And we have consciously try to grow share of those OEMs in our portfolio from 50 and change to 70 and change. And that has reflected in our second quarter numbers as well. Talking about the two-wheelers, our two-wheelers we funded shade short of 150,000 vehicles in Q2. Again with the same caveat that the market share numbers in Q2 need to be taken with some bit of a caution. We believe this number would be shared higher than 7% or so of the financed market. Here, clearly there are four OEMs which we focus on and where our large part of our business comes from which would be Honda, Hero, TVS and Royal Enfield. And that's really reflected in our numbers in Q2 as well.

Karthik Chellappa: Excellent. Sir, just one follow-up if I may, when I just do a back of the envelope calculation, the actual repayment velocity or rate for both two-wheeler and farm equipment works out to be almost half of the actual tenure of the loan, which looks very high repayment velocity, number one; is that right and if so, what would you attribute the very high repayment velocity to?

Dinanath Dubhashi: Let me take it. You can check your calculation with IR team and they will be able to guide you more accurately. But generally speaking, for example, two-wheeler anyway is a two year product, right. So, and in fact, we are doing now the USP that we are setting is we are trying to compete with credit card. So we are having three months, six months, nine months, twelve months product. So you will now see as we have more and more proportion of those products, you would actually see the repayment velocity maybe more than the disbursements. This is the new trend we are trying to bring. Actually it is very small albeit at this point of time, but three, four years down the line we expect to compete with the credit cards. And then this repayment velocity and all those things will just go out of the window. Tractors is a 5.5 years to 6 years product. And we hope that sometimes it gets prepaid, it normally doesn't. It will last its life and perhaps six months more than that. So it doesn't happen like that. There are trade advance numbers, which are within this disbursement numbers. Trade advance is a tool that we very effectively use for increasing market share. That our preferred OEMs and preferred dealers, we give trade advance and then give them the proposition of quick turnaround time, credit assessment because then disbursement is already done. So the turnaround time done for disbursement is 30th. It also gives us predictability of volumes for the next month or two months. This trade advance being a monthly product also shows the churn. So a simplistic calculation will not help you. .

Moderator: Thank you. We will take the next question from the line of Piran Engineer from Motilal Oswal Securities. Please go ahead.

Piran Engineer: Just a couple of questions on your housing finance portfolio, the builder loan thing, firstly does it include stuff like LRD and all of that or is it just construction finance?

Srikanth JR: Yeah. It does include the LRD portfolio as well. Having said that, that's still is a small component of the portfolio. Bulk of the businesses is still in the residential sales.

Dinanath Dubhashi: The LRD is one of the safe products and because of that a very low yield product. So as Srikanth said while technically it includes, it's a very small percentage right now.

Piran Engineer: Okay. So but in that case, you'll have been growing really strong, just on the pure construction finance side. This quarter disbursements of Rs.1,700 crore was even more than, say, in Indiabulls which is two, three times your size. So at what point do you all kind of step back and decide or your risk metrics tell you that, you'll had 48% share of housing finance is just in builder loans. When does this stop or can we expect this to continue over, maybe, the next few quarters?

Dinanath Dubhashi: Okay. Whether this kind of growth rate will continue, certainly not because this year itself we have become big now. Last year we were very small, so you will see growth rates which are crazy this year. After that, the growth rates will moderate. But now we're taking the question more strategically. The way we are lending is that we are not looking at the sector growth as such. We are looking at primarily 'A' and 'B' categories of developers. Large part of it coming out of either way group synergies we would not sort of elaborate more on that. L&T group knows and knows the strength, weaknesses of all the builders in the country. And hence we can use that knowledge to sort of pick and choose not only builders, projects etc. New opportunities are coming up with this category. A and B category builders are consolidating with the C and D category builders who will have big difficulties after RERA. Projects, if the trend is just starting, of projects being taken over by A category builders for completion. The other trend of course, which is now I can't say just starting, but about six to nine months old is the affordable housing projects coming up. And the A category and B category builders getting into that. I don't see this trend of excellent disbursement in this area coming down at all. We expect this kind of trend of Rs 1,500 to 1,800 crore continuing for some time. In fact on the contrary, what we need to increase, because you talked about some percentages. So what we need to increase really is the conversion of this to retail because that has been our trend continuously. We have been pretty successful. The proportion of direct to indirect sourcing is continuously going up, but it is very early days. And as I have always been saying two years is what it is going to take to bring that to steady state. And the conversion from construction funding to retail to really come to it steady state and fruition, so that's something that we are working painstakingly at. But to answer your very specific question, we see good opportunities to lend with good builders, good projects with monitoring those projects.

Piran Engineer: Okay and then what's the typical moratorium period in these loans?

Piran Engineer: Just average, I mean, yeah, correct but because, I'm just seeing the repayment rate has been going down in over the last 4-5 quarters and so that is where this question is actually coming from?

Dinanath Dubhashi: Once again, that conclusion is actually not correct. What happens is, whatever is the contractual moratorium is basically just a part of the product to make sure that the project is completed without any difficulties. Actually repayment starts much much earlier. Because the moment the first flat sells, the repayment starts. The project is the product, our lending is always structured that every cash flow that the builder gets in, every rupee of cash flow, a particular percentage and in fact, increasing percentage, as the project progresses is cash swept. So even the project tenure, the loan tenure can be even 6 years, but normally we expect it to get repaid in maybe 50% time. And that's most of our projects actually, that cash sweep is already on. And that is in fact one of the early warning signals. I mean, this is a product where I feel pretty sanguine with the early warning signals, because the early warning signals are like velocity of sale, velocity of construction, the cash sweep mechanism getting in a particular percentage. So there are very real measurable output metrics, which you can put as early warning signal here, and that is happening. So moratorium is, why I am talking about moratorium is, it is largely contractual. It doesn't work, I mean, your repayment starts even before even 50% to 60% of the disbursement is done. Because it's all the time net cash flows. Over the 2 to 3 years, the disbursement goes on stage base and the repayment starts even before that, because of the cash sweep.

Moderator: Thank you. We will take the next question from the line of Abhishek Sahoo from Citigroup. Please go ahead.

Abhishek Sahoo: Again, back to the housing segment; I see you have taken some accelerated provisions from the P&L in the housing segment this quarter about Rs.40 crore. Could you elaborate on what this is regarding?

Dinanath Dubhashi: Again, largely based on our early warning signals. So we have 3 levels of early warning signals, L1, L2 and L3. As we look at some delays, something is happening in a particular project, we have a policy of taking what is our way of taking counter cyclical provisions at this point of time. Though, as I said, regulatory framework doesn't allow us to call it counter cyclical provision. So I would like you to be more circumspect when you write your report. I am not allowed to use this word counter cyclical provision, but it is our way of taking for counter-cyclical provisions that any project will show us early warning signals, we take some provision. But they are nowhere near NPAs. And mostly we will be out of these projects much earlier and then these provisions will be reversed and used somewhere else.

Abhishek Sahoo: Sure. And in terms of the timeline of disbursement for these projects, would these have been projects which were originated more than 2-3 years ago or are these recent disbursements?

Dinanath Dubhashi: You are right. All these projects are more than 2-3 years.

Abhishek Sahoo: Sure. And just a follow up on Housing; could you give us a split between housing, home loans and LAP in retail housing?

Srikanth J: Around 52%will be home loans and the balance will be LAP.

Moderator: Thank you. We will take the next question from the line of Gautam Trivedi from Nepean Capital. Please go ahead.

Gautam Trivedi: The question is regarding the NPAs. Your gross NPAs have gone up on 5.71 to 5.8. And you spoke about the various risks, parameters, and the early warning signals, which is very impressive. But the question I have is, given all of that, the fact that gross NPAs have actually gone up. Can you give us a break-up of what the various segments are for the gross NPAs? Is there one particular segment is contributing to the increase or is it across them all?

Dinanath Dubhashi: The breakup is given in the presentation, slide 32. So, very detailed break up has been given. So actually if you see as a percentage, the Rural gross NPA between Q1 and Q2 is 11.35 to 10.9; Housing is 0.94 to 0.83 and it is the Wholesale which is 4.32 to 4.79, so you get the complete break up here. I wouldn't call and at least I wouldn't call, you know better, a 5.71 to 5.8 an increase, technically it is, I wonder what I should do to explain it. But let me say only one thing because if you see the only Wholesale one needs explanation, the Rural as I said, we had predicted actually an increase in September. It is natural, large billing, so I will go business by business. Rural, large billing happens in May-June with 90 DPD norm kicking in, naturally August-September will be when these billings will become 90 DPDs and anything which is not collected immediately will be at least temporarily NPA. Because of this, September and March will normally, seasonally be the spikes. So whatever little spike or little increase you see will definitely go down in December. So that is as far as Rural is concerned, but despite that, the overall NPA ratio is well in control and in fact, reduced. Also if you see the rainfall pattern this year, it looks like it has shifted and we have to see the future years. It looks like it has shifted from July, August heavy rain, to August and September heavy rain and even maybe October. We also see because of that the money available in the hands of the farmer to be towards Q3, more towards Q3. We also expect a very excellent Rabi yield this year. So Rural NPAs would continue its downward trend. Housing, I don't know if there is any explanation needed. In Wholesale, any case we had said that the total legacy stress book may be something like Rs. 5,000 crore. They will be at various points of time be classified into various permutations and combinations of three alphabets. So NPA, SDR, S4A, we can keep calling it many things. At various point of times that is what they will slip in and out of those categories. We are monitoring this whole Rs.5,000 crore and we believe that quarter-on-quarter, there maybe ups and downs, variations in this number. The most important number and that we believe at this point of time is sufficient is the provision coverage on this, on the Wholesale part, especially Infra, which we believe that we should be pretty well protected at about Rs.2,000 crore. At this point of time, we have reached a level of Rs.1,551 crore. So we have another Rs.450 crore to go. We will reach that Rs.2,000 crore, maybe even a little more than that by the end of the year. So NPAs yes; definitely lesser the better. But I am not too worried about this trend. Assuring you, of course, that as we go to third quarter, we will see a reduction in this ratio especially in the Rural business, Housing steady; and Wholesale I just explained. Then I already said that full problem is Rs.5,000 crore. So within that the number is a matter of classification.

Moderator: Thank you. We will take the next question from the line of Amit Premchandani from UTI Mutual Fund. Please go ahead.

Amit Premchandani: Sir, on the Housing disbursement that you have done this quarter and the overall book on the non-retail side, what percentage is to the L&T real estate arm?

Dinanath Dubhashi: L&T real estate arm is zero. L&T real estate arm won’t borrow from me.. I'm too costly for them. The contacts of L&T real estate arm is what and the contacts more importantly of L&T ECC, who builds the buildings and factories group, who builds houses for real estate customers is what is important. So but there is one project that we did too, where L&T real estate arm has signed the JDA, that was around Rs.500 crore was our sanction to that project where L&T real estate arm has done a JDA with a builder to whom we may not have normally lend. So the construction is done by them, the marketing is done by them, selling is done by them, so it is largely the L&T risk. And that is the model that we will follow, try and follow not only for L&T, but as I said as more and more such deals happen of superior builders signing JDAs or taking over projects of C and D category, this is an opportunity which will be thrown up to us. Then the question is that out of our total disbursement for how much we use L&T Group contacts, knowledge, etc. I think 100% of our sanctions, we use L&T knowledge, contacts will be at decent percentage, but it can always go up.

Amit Premchandani: And sir, this Rs.500 crore sanction is actually disbursed or it is not part of a disbursement number?

Dinanath Dubhashi: Not fully. It will always be done stage wise.

Amit Premchandani: And Sir, on the RERA front, post the implementation of RERA as the project cash flow of the developer will be much more back ended, because the installments to be paid by the buyer would be much more back ended. So the early warning signals etc. and the riskiness of the projects actually goes up or goes down, because of RERA, what do you think and with the equity commitment from the developer side should be higher or lower because of that given that cash flows are back ended.

Srikanth JR: So yes, you're right that the developer's equity commitment will probably go up in post RERA stage. Frankly we see that as an opportunity because it allows us to step in and provide further solutions to the developer. But, specifically in terms of risk increasing because the cash flows are back ended, not necessarily. So that I don't see it to be as big a risk. Developer commitments, initial commitments will go up simply because they are not allowed to do a pre-launch sales, which used to be something which a lot of developers used to do earlier, where they used to get a significant amount of cash up front that they used to do, used for project approvals etc. that is something which now they are not permitted to do. So they will look for solutions for the initial expenses that they need to incur in our project, including approvals, so that we potentially see as an opportunity. But otherwise not necessarily that the cash flows will be too back ended, that I don't see that as a big risk.

Dinanath Dubhashi: I will add to what Srikanth says. First of all, RERA according to me is unequivocally absolutely very clearly positive for the sector. Any sector where transparency comes. See, I will even take a few steps back and say what are we trying to establish at the characteristics of this Company. We are not going to be an NBFC, which enjoys information asymmetry, which claims aspecial knowledge of how to manage information asymmetry. We are not going to be NBFC of that kind. We are going to be an NBFC which enjoys availability of clear data, knows how to use that data and knows how to use that data quickly and better than everybody else. And that's the direction that we are going to take across businesses. So clear data availability, discipline coming in the sector is always going to be extremely positive for the sector and most importantly advantageous for us. This is across sectors, statement of purpose as far as it is concerned. Especially RERA, again, information availability going up. Discipline in builders is coming up. The riff-raff if I may say so in this sector is just dropping off. We don't expect to see as the C and D category builders even surviving more than a year after strict implementation of RERA. It is generally going to be quite positive. As far as early warning signals are concerned, as I said the cash flow coming to the escrow is just one of the early warning signals. There are early warning signals much before as far as sale is concerned, construction progress is concerned. There are many more early warning signals that we measure. So this particular change will require some tweaking of products, but beyond that, we don't see any negative impact, if at all we are extremely bullish on RERA.

Amit Premchandani: And Sir, on the debt funding part of developer, a developer also need to bring an equity contribution which was earlier the buyer providing that. Are you seeing trends of one financier providing the equity contribution through holding company structure and another financier funding the construction? Are you seeing these kind of structures, which kind of led to power check…

Dinanath Dubhashi: Well, off and on. We have to very watchful of it. This is what happens to industry after industry, overleveraging sometimes most definitely will happen, it had happened before, it had happened in EPC, it had happened in many places before. We will be very careful of it because we have burnt our hands with EPC contractors a few years back. So we know very well how this happens, we will be most careful, but not yet. Private equity, no doubt, it is a big opportunity for private equity coming in and private equity definitely I think that we are seeing the trend of private equity coming in, and that is the good trend.

Moderator: Thank you. We will take the next question from the line of Sunil Tirumalai from Credit Suisse. Please go ahead.

Sunil Tirumalai: Yeah. Soon this Rs.5,000 crore potential problem assets that you identified in the wholesale book, any broad break down of what sectors contribute to what percentage that you can give, that will be very helpful.

Virender Pankaj: Actually, essentially bulk of this comes from EPC sector and coal thermal.

Dinanath Dubhashi: One minute, Virender. Sunil, I think, you are aware of this, , the thing is each one of this is pre FY12 disbursements. I thought first emphasize that point, go ahead.

Virender Pankaj: So it's essentially if we see most of it which has now landed at the stage, where next 6 to 9 months, they should get resolved either through NCLT or otherwise in some form and then coal thermal. These are the key constituents. There is one account which comes from oil and gas related sector. So, essentially bulk of the stress comes from only these very specific areas.

Moderator: Thank you. We will take the next question from the line of Nischint Chawathe from Kotak Securities. Please go ahead.

Nischint Chawathe: Congrats on a good set of numbers, Just a couple of questions; one was, if I look at the NPLs in that rural business, I would assume that Micro Loans business has very low NPL or negligible NPLs, then if I try to do that math then possibly the…

Dinanath Dubhashi: No. You are wrong. So first of all that is wrong. We are talking about a period where we have come out of last year's demonetization

Nischint Chawathe: Okay.

Dinanath Dubhashi: So what we have said is from January onwards our overall…So I will just give you the picture of Micro Loans. Our overall debtors, par one has not gone up. We have kept a very tight control of that, even within that, so I will give you some broad numbers. All post demonetization as well as rather post Jan disbursements, the regular customers, our collection efficiency is 99.3%. Out of the debtors also, 30% odd debtors are paying something, naturally, otherwise debtors would have gone up. So the ball is still in play. What remains of the remaining debtors, we have to follow a provisioning policy based on how much of it is happening in concert. How much of the default, how much of the non-payment is happening in concert and we have divided that into various risk categories. The highest risk category we have provided 100%, then 80% etc. So now out of the total NPA, a fairly large percentage is now almost provided up to 100% and we are moving ahead. So the first assumption of Micro Loans NPA is being very low is at this point of time around till we choose to write-off a part of this particular NPA. So that is clearly there. Now you can ask your question.

Nischint Chawathe: Yeah. Thanks for this clarification. I guess, on a gross basis it's still there, I got the point. Just curious as to on the two-wheeler and the farm equipment side, what would your kind of GNPLs be and what is the kind of your target on the normalized basis or maybe towards the end of the year?

Dinanath Dubhashi: So we are not giving those numbers at this point of time, but I can talk about the trends. So two-wheeler NPAs, normally speaking, in the industry go up slightly every month based on the book going up. They go up and you are normally happy if they go ups are lower than the book growth. Our NPAs in two-wheelers are actually under control, I mean, such have come down for the last couple of months. So we are quite confident of continuing this trend and the two-wheeler NPAs are well in control. Farm NPAs, no doubt are above June levels, which we have predicted. It is very seasonal phenomenon, but that is I'm talking about absolute. In percentage terms they have remained more or less same as even June levels. And in December we certainly see a serious downward trend in farm NPA. So December as we go ahead, the trends will be as follows; two-wheeler NPAs, same kind of slightly reducing trend continuing; farm NPAs, a good decent decrease and Micro Loans NPAs a slow increase in the tenure of the debtors that is there, it will continue. So overall Rural, we believe NPA percentages to come down in December.

Nischint Chawathe: And when would you take a call on the writing off the Micro Loans NPLs?

Dinanath Dubhashi: Most probably by the end of the year.

Nischint Chawathe: Sure. On the fee income side in the Wholesale business, I think it's about Rs.150 crore, maybe if you could give a breakup between origination and syndication?

Dinanath Dubhashi: We're not giving this break up at this point of time. The sell down, is done for three purposes. The first purpose is to earn fees, the second purpose is to manage risk, because as we told you there are sectoral limits on what we can lend to various sectors. And as we come close to those limits, we have to sell down and make more room for a particular promoter, particular sector, particular geography, etc. And last but not the least, for capital management; capital is scarce even now. And hence the Wholesale book growth has to be kept limited compared to the other two business. So sell down happens for all these three purposes, and because of that depending on the situation, the fee increase, even though healthy, may not always be in proportionate with the sell down increase. So you cannot draw a one to one relationship between the huge sell down increase and the relatively moderate fee increase.

Nischint Chawathe: Sure. Fair point. Just on the tax rate side, curious why was the tax rate on the Housing business low this quarter?

Sachinn Joshi: Actually the way the allocation is done, is we have the tax benefit, which is there, which is utilized for the purpose of taking the provision.

Dinanath Dubhashi: Okay. So the benefit of the goodwill is at the holding company. The holding company has to allocate it to various businesses. The way it is allocated, so there are provisions which are taken using this benefit, so there is a benefit. There are provisions which are taken using taking the benefit and based on those provisions, which particular entity those provisions are taken, based on that the tax rate of that particular entity goes down. Now depend on which business is booked in which entity, it is sort of allocated back to that business. So the tax rate of housing coming down is, let's not look at any particular tax law changing for Housing, it is largely a question of allocation of the overall holding company benefitted.

Moderator: Thank you. The next question is from the line of Tushar Sarda from Athena Investment. Please go ahead.

Tushar Sarda: I wanted to understand what are your incremental NPLs during the quarter, because that information I can't find it in the presentation.

Sachinn Joshi: We have given the trend though; the trend is over last 4 to 5 quarters.

Dinanath Dubhashi: Absolutely. So yes, of course, we can do a lot of analysis based on that inflow, outflow and why only NPLs, my collection team and my CEs are supposed to do that for every bucket, every month, right, because that is where early warning signals come in. Then it's the matter of management judgment to how much do we share. Because then I can start sharing bucket wise also, inflows, outflows. So I will have to make that judgment at some point of time, maybe sometime in the future.

Tushar Sarda: Okay. So right now, only the credit cost is what we go by, right?

Dinanath Dubhashi: No. Not only credit cost, we have got the absolute numbers, percentage of NPAs quarter-on-quarter for the last 6 quarters, so based on that lots of conclusions can be drawn.

Moderator: Thank you. That was the last question. I now hand the conference over to the management for their closing comments.

Dinanath Dubhashi: Thank you. It is very clearly the closing comments will be the same as I have always been talking about. Clearly, we have achieved the highest ever ROE. What I would like to emphasize is neither it is a onetime achievement nor it is something, a big journey that we are trying to reach or end of something by 2020 or earlier. This ROE reaching 18% to 20% by I think 2020 or earlier, definitely it's a goal, it's a goal that we are very confident of achieving, but it's again just a goal. It just a milestone, it's just a small milestone in the overall journey that we have to cover. Right now, what the company is trying to do, it's trying to create a sustainable story of delivering predictable earnings, excellent earnings growth and very low variability in quarterly and yearly results, building projects, building strengths to deliver that. We have already talked about that, let me not repeat that. My only last comment will be my attempt always will be to walk the talk, to deliver everything that the management has been talking and giving minimum surprises to the market. Thank you very much for your support and I hope that all your support and good wishes will continue for the Company. We are the new kid on the block, two years back we were not even noticed. I'm happy for your support and really need all that support and expect, request you to continue it. Thank you.

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