Transcript

Conference Call of IDFC Limited

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Presentation Session

Moderator: Good morning ladies and gentlemen. I'm Leela, moderator for this conference. Welcome to the conference call of IDFC. We have with us today Mr. Rajiv Lall, CEO and Managing Director of IDFC and his team. At this moment all participants lines are in listen only mode. Later, we will conduct a question and answer session, at that time if you have a question, please press * and 1 on your telephone key pad. Please note this conference is recorded. I would now like to hand over the conference to Mr. Bimal Giri.

Bimal Giri: Good morning everyone. This is Bimal Giri. I welcome you to this conference call organized to discuss our financial results for the 4th quarter and financial year announced yesterday. I have with me Rajiv Lall, Managing Director and CEO, Vikram Limaye, Executive Director, and L. K. Narayan, Chief Financial Officer. Before we begin, I would like to state that some of the statements made in today's discussions maybe forward looking in nature, and may involve risks and uncertainties. Documents relating to our 4th quarter financial performance were e-mailed to all of you yesterday. These documents have also been posted on our corporate website. I now invite Rajiv to provide key highlights of our performance for the quarter and financial year ended March 31st 2007.

Rajiv Lall: Good morning everybody, Rajiv here. We had our board meeting yesterday, where we discussed our year end financials, let me just take you through the key highlights. Broadly we feel that this has been a very solid year and we have delivered on what our own expectations were with respect to both growth in the business as well as the growth in profits, despite an environment that has become increasingly hostile both in terms of regulatory posture as well as in terms of competition, not to mention the cost of funds. But not withstanding all of that, our balance sheet actually grew 50% from close to 12,000 crores last year to close to 18,000 crores this year; our loan book increased by 37% from 10,300 crores to over 14,000 crores this year.

Our exposure is now in excess of 22,000 crores. So if you just step back and look at our overall business, we now have in terms of our footprint in the infrastructure space, we have about 14,000 crores of loans outstanding. We have another 8,000 crores of loans sanctioned, but not yet disbursed, and we have, if you take the part of our balance sheet that is invested in equity positions, and the part of our funds that we have already invested, we have another 2,500 crores equivalent that we have made in equity investments focused on infrastructure. Coming back to the balance sheet, on the liability side, our borrowings have increased 90%, so we are a more significant borrower in the market. Last year we borrowed 4,000 crores, this year we were up to close to 8,000 crores. We continue to diversify our liabilitiy base and for those of you who have looked at the results, or the information given to you somewhat more carefully, you will see that our foreign borrowings have gone up quite a lot during the year as a share of total liabilities – it has gone up from from over 1% to close to 8% this year.

Our leverage ratio has gone up from 4.5 times to close to 5.5 times, and throughout this, our return on equity has gone up marginally to about 18%. Our operating income expanded 34% from 536 crores to 716 crores. If you break that down, net interest income registered a solid growth of 33% from 294 crores to 392 crores. This is not including an extraordinary income of 15 crores, on account of some money coming back from a restructured asset. NII on treasury operations increased 180% from 13 crores to 37 crores. This clearly demonstrates a much more aggressive treasury operation that is now beginning to generate profits from trading positions. Non interest income, which is what we have always been focused on, on the face of it, hasn't increased all that aggressively, its only increased 18% from 227 to 267 crores, but part of this is because we have deliberately kept from taking profit on our equity positions. Last year we took 125 crores of profits on sales from equity. This year we took only a 124 crores to demonstrate to all of you, that we are working very hard and making progress on non-equity, non-capital gains related non-interest income. So if you look at that fee income that grew from 95 crores to 134 crores a very significant increase of 41%. The bulk of that came from asset management, which grew 84% from 29 crores to 53 crores, but other fees, including notably fees from our debt syndication activities, and equity placement activities grew 22% from 67 crores to 82 crores. Our operating expenses kept pace with the growth of our balance sheet. They were up by about 50%. They now stand at a total of 65 crores. Our cost to income ratio, however, came down marginally from 5.3% last year to 5.2% this year.

Now lets turn to our consolidated profits on pre-tax basis, profits grew by 39%, up from 443 to 616 crores. Our effective tax rate grew from 12% to 20% and notwithstanding all of that, our PAT grew by 29% from 391 crores to 504 crores. This on a fully diluted basis represents a growth in EPS from Rs. 3.59 per share in FY06 to Rs. 4.45 per share in '07. As continuously advertised to you, what all this means is that our return on assets show an orderly decline from 3.8% last year to 3.3% this year and a large part of this is essentially because of a slight decline in our net interest income, which is on account, as it turns out, of increasing leverage and not a declining spread, and we can discuss that during the Q&A. The implicit yield on infrastructural assets, this is average yield, went up from 8.9% to 9.2%, and that is what has helped us maintain our spread pretty much at what it was in the previous financial year.

Little information about the nature of our balance sheet as far as the duration of our assets and liabilities are concerned, they still remain very closely matched. Our assets have now duration of 2.1 years, liabilities has shortened somewhat to 1.85. In a rising interest rate environment, this is exactly where we want to be, so we are not displeased with the asset liability management of our balance sheet.

A little word about sectoral composition of our business, if we take the total exposure of 22,000 crores, the Energy and Transport together account for about two thirds of that, but Energy grew fastest, its growth rate was about 32%, and the other segment that showed very rapid growth last year was what we called Commercial and Industrial, which is mainly hotels. The quality of our book remains solid. NPAs on a growth basis actually declined from 0.5% to 0.2% due to a one time settlement on an asset in Q2. Our net NPAs continue to be nil. I will take some questions on the provisioning, because it's a little complex, during the Q&A.

So to summarize then, we are very pleased with solid growth in our balance sheet and in our lending business. Solid growth in our asset management business, notwithstanding high cost of funding, greater competition, and higher effective tax rates, we are quite pleased with the growth in our profits after tax. Finally, as I hope you'll agree, we continue to deliver traction on building our non interest income, especially the annuity type of fee based incomes coming from our asset management activity. Some corporate developments that you should be aware of, the board yesterday approved a capital raising of $500 million, this well over the next 18 months, if we are able to raise this capital at around Rs.100, it will represent a dilution of about 15% to existing shareholders. Why are we raising this capital? For two reasons, first of all, at the pace we have continued to grow our balance sheet, we will very soon have a leverage ratio that will exceed seven times tier 1 capital, and at that point, rating agencies become uncomfortable, and would have us in any event raise more equity capital. Second is that, because of the due regulatory requirements that apply to NBFCs from the Reserve Bank of India, we need to be better capitalized in order to continue growing the asset side of our business, and third reason is that if we want to expand our asset management business from the $700 million equivalent in AUM that we have today, to 3 or 3.5 billion over the next three years, we will need seed capital from IDFC to build that business. So that business in terms of a contribution of equity from IDFC will need at least a $150 to $200 million over the next two, three years. So that is why we need this 500 million in additional capital.

The last update I might give you is on the big project equity fund, with Citigroup and Blackstone that we had announced, we are now in active fund raising. Over the next quarter, hopefully we will have something to announce in terms of a first close to you, but that fund raising is going to be in the US. And that pretty much covers the waterfront, at least from my remarks. I will stop here and let's open it up for questions.

Question and Answer Session

Moderator: Thank you sir. Ladies and gentlemen, we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone key pad and wait for your turn to ask the question. If your question has been answered before your turn, and you wish to withdraw your request, you may do so by pressing # key.

First question comes from Mr. Krishna Kumar of Sundaram Mutual Funds.

Krishna Kumar: Good morning sir. For 2008, if you could just broadly tell us your plan on non-interest income, especially the non-equity based fee income that you are talking about. More in terms of what is your kind of internal growth targets that you have and what is the plan of action there?

Rajiv Lall: The plan is very aggressive. I have in the past never really given very specific guidance on individual line items, nor have I given very explicit guidance on growth in balance sheet or earnings. So I will continue to stick to that basic policy, but I can give you some sense long-term where we are headed, and I can give you some sense for the initiatives that we are taking to continue growing the fee based income. So first let's look at the long-term.

Today, as I said, our return on assets is 330 basis points, and our operating income as a share of average assets is about 470 basis points. Of that, 470 basis points, 280 comes from interest income and 170 basis points comes from non-interest income. And of that 170 basis points today, about half comes from profit on sale of equity and the rest comes from the type of fee income that you are referring to. Now what I have said repeatedly and I will articulate again for you, is that over time, the return on assets on an after tax basis, largely because of a continuing and secular decline in net-interest income, from 330 basis points, will come down to something like 250 odd basis points. This could happen over the next two to three years. Implicit in that, will therefore be a reduction in our total operating income from about 470 basis points that it is today, to roughly 400 basis points. Of that 400 basis points, I expect non-interest income to be roughly half, and off that half which is 200 basis points, I expect fees from non-capital market related activity, meaning fees from other than capital gains, to be about 55% to 60% of that. Now, how are we going to get there? We are going to get there by pursuing three initiatives. First of all, as I said, our asset management business is growing very rapidly from 700 million before March of this year, which we expect to ramp up close to between 1.5 and $2 billion. And then over the next three years, we can expect that to rise to between $3 and $4 billion. The fees that we will be earning from that AUM will be a significant contributor to this non-interest income. Secondly, we continue to ramp up our investment banking activities, most notably the capital markets activities, and hopefully within the next quarter we will unveil a couple of other transactions, that will build on our franchise that we've developed at SSKI, that will also contribute to our fee income. So if you noticed, on account of our acquisition of SSKI, or our part acquisition of SSKI, SSKI contributed about 11 crores to PAT this year. So this number is also going to grow quite aggressively this year and the next.

Krishna Kumar: Okay, and the recent announcement that was made a couple of months back about the infrastructure fund with

Citigroup. When do you expect revenues from that to start kicking in for you, and will that be a part of the fee income?

Rajiv Lall: Yes, that will be part of the fee income and we expect revenues from that to kick in before the end of this financial year.

Krishna Kumar: Okay, many thanks.

Moderator: Next question comes from Ms. Nandhitha from Karma Capitals.

Nandhitha: Hi Rajiv, a couple of things. One, you mentioned of hostile environment, could you just elaborate on that and through what kind of an impact you expect to have?

Rajiv Lall: A hostile environment in the sense that the money markets have been very choppy over the last few months, there has been in the last quarter a huge squeeze on liquidity, and as part of its backing against inflation, the regulator has been increasing risk weightages and making access to capital harder for NBFCs. So that's what I meant by hostile environment.

Now, I don't know how deeply to read in to the most recent monetary policies statement of Reserve Bank of India, but I don't expect that things will improve any time soon, but if I were to hazard a guess, I would say that we probably have another six to eight months of a choppy period ahead of us, but beyond that things will start smoothening out.

Nandhitha: Okay, and when it comes to infrastructure projects, are you seeing everything on track, in terms of timing, in the power and other sectors or are you seeing delays? what sort of the outlook for at least the next two quarters?

Rajiv Lall: There is a lot of momentum and activity. It's difficult to actually see things very clearly as they are unfolding, so again if I were to try and detach myself from the process, because if you look at clients, and if you look at our immediate pipeline, it looks very, very solid. But common sense tells me that given the rise in the cost of materials, given the shortage of skills, especially civil engineers, given greater difficulty in raising foreign funding for the large corporates, or greater restrictions on their ability to do so, I imagine that there will be some slowdown of activity. Now, how much is difficult to say, but there will be some slowdown of activity.

Nandhitha: And but you are not seeing that, you are expecting it?

Rajiv Lall: Not seeing it yet. The economist side of my brain says to expect it, but I am not seeing it yet.

Nandhitha: Okay, and then these couple of ultra mega power projects and your involvement in those in terms of funding and what's your expectation given at least one of them is sort of delayed?

Rajiv Lall: Well I think even if one of them is delayed, the other one is plenty to chew on, and I think that we will look to get engaged quite seriously on the funding side of the TATA project in different ways. I think the next quarter or two, we will figure out how we can get involved in that particular deal, but we would like to be involved in that one.

Nandhitha: Okay, great. Thank you.

Moderator: Next question comes from Mr. Kunal of ASK Raymond James.

Kunal: Hi Rajiv. Any one time item in the fee income this quarter - On the higher side than the last two or three quarters?

Rajiv Lall: No, we had some income from sell down of an asset, so that's why I encourage all of you to look at our numbers on a rolling 12 month basis, because a lot of these capital markets related fees are transaction specific. So they could fall from one quarter to the next and if you are focused on a quarter to quarter kind of performance, you will see blips, but hopefully over a 12-month rolling period, it gets smoothed out, so you get a better sense for the trend.

Kunal: Okay, and one more question particular to this quarter, what about the margins this quarter? I believe they've come down a little bit ?

Rajiv Lall: That is not the case. Actually our spreads have held up quite well, so far and that is because we had enough funding for this quarter's disbursements that we had borrowed before the choppiness in the debt markets, which really started around January. So we had actually done a significant bit of our borrowings before that. And then we also got some foreign funds in during the last quarter. So we have actually been able to manage this quarter reasonably well.

Kunal: Okay, and lastly on your tax rate for '08, what could be the effective tax rate?

Rajiv Lall: Effective tax rate, we are already at 20, so like all good things, this should also go up, but by how much I am not sure, I would say you have a working number of 22%.

Kunal: Yeah, okay, and lastly anything on the tax implications for the new regulations on the PE funds which you have?

Rajiv Lall: We have solved that problem.

Kunal: Okay, thanks a lot.

Moderator: Next question comes from Sonal Gupta of UBS.

Sonal Gupta: Yeah hi, good morning Rajiv. Congrats for a good set of numbers. Just for a few housekeeping questions, could you tell us what was your outstanding borrowing at the end of the year?

L. K. Narayan: It's close to 14,900 crores.

Sonal Gupta: And just to understand, your balance sheet growth is 50% versus your loan growth of 37%, could you just highlight where the difference is coming from?

Rajiv Lall: I think basically because of these foreign currency loans that we took on; we had about 800 crores of borrowing that came into our treasury book this quarter. So normally our treasury book will always rise proportionately with the rest of our loan book, but for this size of loan book, we had anticipated the treasury to be around 2,000 crores. But we have ended up with 2,800.

L. K. Narayan: That was because the FCB that we did, that was towards the early March, we raised $75 million through foreign currency borrowings, so that accounted for 330 crores, and then we had a private placement with a large bank of 500 crores, again the rates were very good, and therefore we closed those deals, and that essentially explains this 800 crores surplus that we carry.

Rajiv Lall: So you can't choose very finely when you want to borrow, if you see a good deal in the market, you want to go out after it aggressively, so it should help us manage our spreads going into the next quarter.

Sonal Gupta: Right, okay in fact I have a couple of other questions, maybe I will just put in a few, but just for that, what would be your average cost of funds for FY07?

Rajiv Lall: I think we are usually quite silent on that, are we not?

Sonal Gupta: But I believe you gave out annual numbers last year, so…

Rajiv Lall: I cannot answer this question. All you need to know is that our spreads are stable.

Sonal Gupta: Yeah, I believe your loan strength has actually expanded ?

Rajiv Lall: Actually they have.

Sonal Gupta: Because it does look like that.

Rajiv Lall: Yeah, they have, thats a very astute observation, they have actually expanded.

Sonal Gupta: Okay and just a final question. How do you hedge your foreign currency borrowings?

L. K. Narayan: We have actually swapped it into rupees, it's a perfect hedge.

Sonal Gupta: Okay, so there is no risk on that side?

L. K. Narayan: No foreign exchange risk.

Sonal Gupta: Okay, great. Thanks, I will come back with more questions later.

Moderator: Next question comes from Srikant of Brics Securities.

Srikant: Hi, this is Srikant. The question is on the capital raising that you had announced. You discussed one of the rationale being some regulatory norms on capital adequacy. I am not aware of any changes, what exactly were you referring to?

Rajiv Lall: No, not on capital adequacy, these are changes with respect to single company and group company exposure limits.

Srikant: Okay, they were already there, right? Is that your hitting the limits, so you wanted to expand the base?

Rajiv Lall: That's right.

Srikant: Okay, also you had mentioned that one of the rationales is also seed capital requirement for investment in the equity funds. Is there any regulatory norm, any rating agency norms, or internal norms, saying that only x% of capital can be in equity investments?

Rajiv Lall: There are now no regulatory norms for an NBFC, there are internal norms and the internal norms, in my sense is that we've been far too conservative in the past. So just to give you an example, what happens is, I have said this many times before, that our business model is rapidly evolving into the Macquarie type of model, right? The Macquarie model, there's another company called Babcock & Brown, which is also listed in Australia, which is also very similar. So if you look at Babcock & Brown, my recollection is that they have a balance sheet that is 13 billion Aussies, and they have funds under management of about 50 billion Aussies. The 13 billion that is their balance sheet is 80% equity, but it is geared only 3 to 1. So, our gearing today as I said is 5 ½ to 1. So, I think that especially with this capital raising, we have an opportunity to take a little more risk on our balance sheet. I think that over time we will.

Srikant: Rajiv, you are saying that rating agencies are comfortable with seven times leverage. Now with this new perspective of taking more equity exposure on the balance sheet, should we actually assume there will be some sort of downward revision of that seven times leverage number?

Rajiv Lall: That will happen very slowly over time. We do not want to be caught in a situation where we are getting concerns on our leverage ratio without delivering returns from our equity investments. We want to time our exposure to equity in such a way, that we are able to demonstrate a consistency of returns, and then we are able to live with a lower leverage over time.

Srikant: Okay and there's no pipeline of an FCCB issue, it will be pure equity, right, whenever it comes?

Rajiv Lall: Pure equity or compulsorily convertible domestic instrument.

Srikant: On this Citibank-IDFC private equity deal, should we assume that the entire 2-20 from whatever funds are raised would accrue to IDFC, or would they be sharing of that?

Rajiv Lall: You can assume that the entire 2 will accrue to IDFC, whether that's 2 or 1 ½ it is unclear, we will see how it goes after marketing. But that entire fee, whatever it is, comes to IDFC. Of the 20, two thirds comes to IDFC.

Srikant: Okay, so basically Citibank and Blackstone are in the deal for this one third of the 20.

Rajiv Lall: Yeah, but you should ask them.

Srikant: Yeah, and just a housekeeping question. This equity book has increased from 509 crores to 757 crores Y-on-Y, but your equity exposure is only increased from 368 to 384, does that mean that others are strategic investments?

Rajiv Lall: I am not sure I understood the question, could you repeat that?

Srikant: Yeah, the equity book, I think in the press release says that it increased from 509 crores to 757 crores. The equity exposure has only increased from 368 to 384.

Bimal Giri: It Doesn't include strategic investments.

Srikant: Yeah, does it include things like investment feedback ventures like SSKI, which is why that has increased much more than your equity exposure.

Bimall Giri: It doesn't include that.

Srikant: So why this discrepancy then?

Bimal Giri: The exposure table that you are speaking about doesn't include our investments and investments in subsidiaries, associates, JVs etc.

Srikant: Okay, so basically this 509 to 757, the bulk of the increase is because of strategic investments.

Bimal Giri: Yeah, that is right.

Srikant: Okay, fine thanks.

Moderator: Next question comes from Ms. Madhuchanda of IL&FS Investsmart.

Ms. Madhuchanda: Good afternoon sir, just a couple of questions. Could you explain the rise in operating expenses and the provisions in the 4th quarter?

Rajiv Lall: It's because our HR bill has gone up significantly because the number of employees has grown by something like 50 people, which is roughly 35%. There has been a growth of 35% in the number of people employed. So the bulk of the increase in operating expenses comes from that. There has also been some escalation in the basic pay scales as well, which was to the tune of 9% to 10% last year. Now on provisioning, it's a little more complicated. If you look at our cumulative provisions, they went up from 242 to 243 crores so there was a net increase in provisions of only one crore.

Now this was because of some extraordinary write backs that we have had. We have had something like 52 crores of write backs, 28 crores on account of re-priced assets, which has been over provisioned in the past and 23 crores on account of a non-performing asset, that we have since written off. So that was 23 crores. As against that, we have made 35 crores of provisions, which is the equivalent of 0.5% of gross disbursements against standard assets. And under article 36(1)(viia) of the Income Tax Act, we have provided another 15 crores.

L. K. Narayan: There is a tax deduction under 36(1)(viia) that accrues to us at 5% of our total taxable income. So to take advantage of that we have made a provision of 15 crores.

Rajiv Lall: So that's 50 crores, then another crore was provisioned against sundry debtors and another crore against our equity positions, so we have made 53 crores of provisions, 52 crores of write backs. We therefore ended up with a net increase in provisioning of 1 crore only. This awkward situation will regularize itself when we stop doing the write backs against re-priced assets which will be in another 12 months or so.

Ms. Madhuchanda: Okay, thanks a lot.

Moderator: Next question comes from Mr. Siddharth of Enam Securities.

Siddharth: Hi Rajiv, I was checking that the growth in disbursement has been quite lower, but you said sanctions have been much higher. When do you see these getting disbursed?

Rajiv Lall: It takes about anywhere from 6 to 18 months for this pipeline to work itself through, especially in the energy sector, in generating plants. This is milestone based funding, so as the construction proceeds the disbursement happens. We do not expect any significant delays because the bulk of projects that we have funded are relatively they are small or medium sized power projects and so there are no huge permission related delays that we anticipate. So you look at the 8,000 crores of sanctioned, but as yet undisbursed pipeline, you can factor that into your model with a lag of 6 to 18 months.

Siddharth: Okay and Rajiv, yet another question, you said your other income also included something from sell down. Can you quantify it and was it entirely in this quarter?

Rajiv Lall: It was entirely in this quarter, but I don't want to quantify that.

Siddharth: Okay, thanks Rajiv.

Moderator: Next question comes from Ashwinder Bakhshi of Fidelity.

Ashwinder Bakhshi: Sir I have only one small question, could you please describe your asset liability maturity profile, please?

L. K. Narayan: Yeah, the duration of our assets as on March 31, is 2.11 and the duration of our liabilities is 1.85 and as in the past we have managed a very closely coupled duration map between the assets and the liabilities and we have continued to do so and what we believe is that at a point where we anticipate rates to ease off, a faster run off of liabilities is advantageous from our point of view, so going forward we would get that advantage.

Ashwinder Bakhshi: Okay, thank you.

Moderator: We have a follow up question from Mr. Srikant of Brics Securities.

Srikant: Hi, two questions, one is on your loan yields, why are there are only 30 bips considering the fact that more than half of the books has been created in the year, I am just understanding whether there is some issue in terms of pricing power that is playing out?

Rajiv Lall: Srikant, I didn't understand the question.

Srikant: Your yield on advances increased from 8.9% to 9.2% on a Y-o-Y basis. I thought that the overall increase in interest rates, if I look at any other commercial bank or any other asset class, the margins have been stable, but the yields per se have increased much more, I was wondering maybe this is a bit low and maybe some sort of pricing power issues are there. I would assume that the yield on advances would have increased much more.

Rajiv Lall: This is the average yield. If you look at the incremental yield, it will be much higher. So I think in the next, you know, as more and more incremental assets are booked at the incremental yield, you will see the average also being pushed up along with the growth in the balance sheet. As to pricing power, we have never claimed to have had any pricing power, so if everybody else's asset yields are going up, so will ours.

Srikant: Rajiv, what I was trying to understand is, your clients are mostly sophisticated borrowers, I mean the names that you have put on the presentation are pretty well known, so is that playing a factor and are they able to get better prices in the market. Not just from you, but from anybody that they borrow with, is that an issue that is playing out?

Rajiv Lall: No, we have broadly speaking two kinds of clients and we have to balance the two, so if you take the AAA rated clients, we need to do business with them because of managing the risk in our overall asset exposure. Now with them, clearly we are not going to be able to negotiate very hard on the price. The spreads on lending to those big boys is low, but the flip side is that the risk of lending to them is also lower, so it is always good to have a few names in your book like that. Our sweet spot are deals that are 300 - 400 crores and they are primarily to projects, not to companies but through sponsors who are what you call tier 2 and that really is the bread and butter of our business.

Srikant: Okay, fair enough. Also on this sell down thing, you said that you will not give exact numbers, but can you give a broad color on how are these deals structured in terms of securitization sell down type structure, so it should be about 2-3% of the assets or some broad bench mark of that sort without getting into specifics, obviously.

Rajiv Lall: We really want to grow this business aggressively in the future, but right now again there are all kinds of regulatory restrictions that make it difficult to securitize large chunks of our balance sheet. So the only way we are able to recycle our balance sheet is actually to sell loans which are lumpy things. It is hard to package them and sell down a whole package quite easily. These are in the nature of individual transactions, and we identify those that could be particularly interesting from a fee generating and a profit booking point of view and we work very hard to get them off our books.

Srikant: Okay, also Rajiv in terms of the loan growth, I would assume that you have enough capability and there is enough demand. If you wanted to grow the loan book faster than what it has been growing. I mean 39% has gone back of it, almost a 20% disbursement growth. Is there a conscious management strategy saying that we are comfortable with around 35% and we wouldn't go beyond that, I mean 35% would be an approximate number?

Rajiv Lall: See it depends, it's a balance between growth, quality, risks and spread. So if you think that growth that we have delivered so far represents a good balance of all those matrix, as evidenced in how we have managed our spread and how we have managed our profits after tax, we always have the option of growing faster, but it will come at a cost of spread presumably.

Srikant: Okay, thanks.

Moderator: Next question comes from Mr. Harish of Kotak Mahindra.

Harish: Hello sir, I just wanted your qualitative opinion. Given the fact that infrastructure projects in India are increasingly having longer gestation periods, what is your opinion on the duration of assets? Is it going to be a successful upward trend and given that, how is your asset liability mismatch then?

Rajiv Lall: This will depend on how fast our debt capital markets develop. You are right that infrastructure funding in most countries depends on long duration assets, which this market is not able to either deliver or doesn't want to absorb. From the point of view of the supply of these assets because of the structure of liabilities in the country, it is difficult to write very long dated assets. From the demand point of view, the average age of India is, about 50% of the population is under 25, so they haven't lived through a rising interest rate cycle. So the expectation is that interest rates will continue to fall. So even today it is difficult to sell a fixed rate product in the corporate market. So I think that it will take for a few people to get burnt on the corporate side and it will need for our debt capital markets to become deeper before the duration of infrastructure assets begins to rise. One ray of hope, however, without reading too much into the monetary policy statement of the RBI they seem to signal that we continue to be on a path towards capital account convertibility. Whenever capital account convertibility happens, a company like IDFC will have recourse to international debt capital markets, where we can not only securitize our assets, but then we can really write long dated assets for our clients.

Harish: But you don't see that happening in the near term, at least one to two years?

Rajiv Lall: I would be guided by your insight on this.

Harish: Okay, secondly just a housekeeping question, your AMCs today you said its 700 million dollars, is that right? This would be pure equity, is there any component of mezzanine debt or debt funding in this?

Rajiv Lall: Not yet, this is pure equity.

Harish: Okay, but are we increasingly seeing some kind of traction in those kind of papers as well instead of just pure equity?

Rajiv Lall: I think we should.

Harish: Okay, so then growing to 3 to 4 billion may not be such a big problem?

Rajiv Lall: Exactly right.

Harish: Okay, thanks a lot, all the best.

Moderator: Next question comes from Mr. Anand Vasudevan of Franklin Templeton.

Anand Vasudevan: Hello Rajiv. Couple of questions on your capital raising; first of all is it reasonable to expect that you should be concluding the transaction within the next couple of quarters?

Rajiv Lall: Yes.

Anand Vasudevan: Okay, and secondly, now that you will have more capital, are you re looking at the balance between growth, quality, risks and spreads that you have been talking about?

Rajiv Lall: Yes.

Anand Vasudevan: Are you looking at moving towards rapid acceleration and probably moving towards a higher quality part of the business?

Rajiv Lall: Well, we are looking to do that in equal measure and also taking greater risk. So I think that we certainly will then have the opportunity to grow our balance sheet irrespective or in spite of the single company and group company exposure limits to quality names on the one hand, but you can also expect greater risk taking appetite from us when it comes to our principal investing activities in the future.

Anand Vasudevan: Sure, but on the lending part of the business, are we looking at moving towards higher quality, perhaps lower spreads?

Rajiv Lall: Ideally we would like to move to high quality and the same spread, but yes if there is that trade off to be made, we might look into that.

Anand Vasudevan: My other question is on loan disbursals that you have reported for, which is not a growth over Q4 of last year. Is that the beginning of a trend in slow down in disbursals or is that just something to do with a quarter to quarter lumpiness in disbursals?

Rajiv Lall: It's the latter.

Anand Vasudevan: Okay, thank you.

Rajiv Lall: Okay.

Moderator: We have a follow up question from Mr. Sonal Gupta of UBS.

Sonal Gupta: Hi Rajiv, just to, could you give us the fee income breakup or where is it coming from?

Rajiv Lall: The bulk of it is coming from asset management, and then next would be upfront fees associated to our lending business and then third would be debt capital markets and then fourth would be equity capital markets. And this is not including the contribution to PAT from SSKI. So those are the five - equity capital markets, debt capital markets, upfront fees, asset management and SSKI.

Sonal Gupta: Could you put numbers to that?

Rajiv Lall: Let me build on these businesses then I will give you more concrete numbers in a quarter or two. I mean, you can work backwards and figure out what our numbers are on asset managements.

Sonal Gupta: No, asset management numbers I think are given.

Rajiv Lall: Right, so the rest is residual, let that number become nice and larger and in a quarter or two I will be more comfortable being more precise about how much is coming from what.

Sonal Gupta: Okay, and just to understand there is some deals on debt syndication which include a sell down, this is not the sell down that you have done yourself. I mean this is not the IDFC sell down?

Rajiv Lall: It is the IDFC sell down. I am not sure what you are referring to.

Sonal Gupta: In this last page presentation there is debts syndication and sell down, so I just wanted to understand it, where the fee income has been…

Rajiv Lall: Yeah, most of it is right, if you look at what is the nature of fee income from debt syndication activities, it comes partly from sell down and partly from just the fees you get from acting as a broker and intermediary and it is no secret that you get much more income from transactions than you get from acting as an intermediary.

Sonal Gupta: Right, okay, and just on the SSKI business, I think…

Rajiv Lall: But on the debt syndication business, we are ranked now right?

Vikram Limaye: We should be in the top six IFR's on the total loan syndications volume that we have done.

Sonal Gupta: Okay, so just to understand on the SSKI side, the profits are 11 crores to PAT, which was I believe, I mean, if you take SSKI as a whole it was 30 crores last year, versus something like 33 crores this year, so there is not much of growth on the SSKI side.

Vikram Limaye: Last year SSKI was not 30 crores. It was around 24 crores.

Sonal Gupta: Because you said that you had acquired at ten times fee on SSKI product, why was it?

Vikram Limaye: Last year it was 24 crores, this year it is 33 crores. There has been solid growth in the SSKI business and it has come because of their trading platform. They have generated very solid revenues from their institutional brokerage.

Rajiv Lall: We weren't very precise about the exact multiple we bought it at.

Sonal Gupta: Right, when last quarter somebody asked you on the long term guidance and you talked about a 20% ROE, so what was the leverage you were taking at that time into account?

Rajiv Lall: Now what we were saying is that in our long term steady state, if we trend down in the existing business model, it relies very heavily on lending. The NII of this is not within our control. The ROAs post tax would trend down to about 2.5%. So on a 2.5% ROA, if you want to deliver an ROE of 20% plus, you must have a leverage of 8 times. So from this you can deduce that, for us to be able to deliver ROEs of greater than 20%, either the rating agencies have to become more relaxed about what cap they want to place on our leverage.

Sonal Gupta: No, because you said one of the reasons for capital raising is that seven times tier 1 is where they start becoming cagey because…

Rajiv Lall: That's right. My guess is that we still need a couple of years for the rating agencies to get more comfortable with our business model. So I mean to give you just on a sense on where we have come with the rating agencies. The rating agencies previously were stuck on five times leverage. Now we have got them to seven times leverage and so as the dialogue continues and they see our business model gaining traction, our expectation is that they will eventually get to accept eight odd times leverage. But we do not want to take the risk with our AAA rating, so better to be safe, we want to raise the capital and not get into that zone.

Sonal Gupta: Okay, fine. Could you just elaborate a little bit more on the capital adequacy requirements, which on a group company exposure limit, which is part of the reason for capital raising?

Rajiv Lall: No, its not the capital adequacy issue, the issue is what the single company and group company exposures are. Today after the NBFC, RBI regulations, the new ones announced in February, we are not allowed to have a lending exposure more than 20% to a single company. And we cannot have a lending exposure to a group, more than 35%. Now this is significantly lower than what it used to be in the past because in the past we were allowed up to 50% of our net worth as exposure to a single group and how much to a single company?

L.K.Narayan: 25%. For the single company lending exposure, historically we could lend 25% of our net worth, now which has come down to 20% and the group exposure limits have come down from 50% to 35%.

Sonal Gupta: Okay, but this is including the addition for infrastructure, I think there is a 5% addition?

L. K. Narayan: We have included that, yeah.

Rajiv Lall: So, 15 plus 5 is the limit on lending to a single company and 25 plus 10 is the limit on lending for a group.

Sonal Gupta: Okay and I believe you have already committed 75 million dollars to the new fund that you are launching with Citigroup and Blackstone, so where is the need for an additional 200 to 300 million dollars coming from?

Rajiv Lall: You will know very soon, because we are going to raise more funds.

Sonal Gupta: Okay, great. Thanks a lot, thank you so much.

Rajiv Lall: Thanks.

Moderator: Next question comes from Mr. Vishal Goyal of Edelweiss Securities.

Vishal Goyal: Yeah, hi Rajiv. This is on NSE investment, what is the kind of investment we have in NSE in terms of percentage stakes?

Rajiv Lall: We haven't disclosed our ownership stake, but once the balance sheet is released at the AGM, it will become public knowledge, and you will know how much we own. Just be patient till June 20th and you will get the number.

Vishal Goyal: June 20th?

Rajiv Lall: Yeah.

Vishal Goyal: Okay, thanks.

Moderator: Next question comes from Mr. Manish of Motilal Oswal Securities.

Manish: Hi Rajiv. In the current scenario wherein every other financial lender is increasing lending rates, I would tend to believe that our spreads and margins should actually hold on, which has happened actually in this particular quarter as well. So I just wanted some sense on over the next one year or so, what should be the spread trend for us?

Rajiv Lall: It depends on, our spread is a complex animal because not only does it depend on asset yields which are not within our control, it also depends on the spread that AAA assets get over government securities. So in the debt capital markets there are some liquidity squeezes or shortages that occur, then our cost of fund does not move in tandem necessarily with the asset yield. So it is not that easy to predict. As it is, in the case of HDFC, they are able to rely on deposits for example, for a good share of their liabilities. So I think in principle you are right, whether it actually happens that way, I cannot promise. What I will reiterate is that overall though if you look at our spreads and NIIs over two years I will continue for you to factor in a secular decline.

Manish: Right and second question is on the AMC side, we have already managed 700 million dollars, that is 500 million private equity and 200 million is another fund for private equity if I am not wrong?

Rajiv Lall: That's right.

Manish: So, how long have we been running this fund, it's been more than two years since we have launched the first fund, right?

Rajiv Lall: Yes, 2004 the first fund was launched.

Manish: Okay and typically these funds would be for 5 to 7 year periods.

Rajiv Lall: 10 years.

Manish: 10 years, so have you sold down anything from this fund as of yet or…

Rajiv Lall: Yes, we have, we have had some partial exits from fund one.

Manish: So has some income been booked from that side also?

Rajiv Lall: Not yet, but we can expect some income to start coming in.

Manish: Right and can you share what kind of returns are you generating on those investments?

Rajiv Lall: Each time we have an exit that is significant from one of our investments, we make a public announcement - IDFC private equity will make a public announcement. I don't want to get too specific about this, but fund one has done so far really very well. I mean, we are talking about IRR's that are well above what you might normally expect in a private equity business.

Manish: So, could it be upwards of 40%?

Rajiv Lall: On one deal or two, the answer is definitely yes. It's too early to say how the IRR on the entire fund would look like, but the tone of the fund looks very good.

Manish: Okay, and the second fund is is 500 million dollars, right?

Rajiv Lall: No, the first fund is 220, the second fund is 440.

Manish: Okay and how old is the second fund?

Rajiv Lall: The Second fund was only raised last year.

Manish: Okay, thanks.

Moderator: Next question comes from Mr. Prashanth of ICICI Prudential.

Prashanth: Hello sir, I just wanted to understand the trend in the fee income, your loan book has increased by 37% and the core fee income I think by about 20%?

Rajiv Lall: Our core fee income is up 41%.

Prashanth: 41%, okay so would that mean that the fee income per transaction, I don't know how you charge whether it is in terms of basis points of the syndication you are doing or is it some absolute income, that is not trending down?

Rajiv Lall: No, there is only a small part of our over all fee income that is linked to our lending book. Because the bulk of the fees are coming from asset management and capital market related transactions, so they are not entirely linked. So if you are trying to forecast how our fee income will track on the basis of a forecast of our asset book, you will get into trouble. I think the way to look at it is to basically rely on management's business plans or our description of our business plans.

Prashanth: Okay sir, are you indicating that if I were to exclude the AMC fees and the capital market fees, then the fee income is growing in line with the asset book?

Male voice: More or less.

Prashanth: Okay, thank you.

Moderator: There are no further questions. Now I hand over the floor to Mr. Rajiv Lall, Managing Director and CEO of IDFC for closing comments.

Rajiv Lall: Thank you very much, I am glad that we have the quarterly interactions, look forward to another good quarter and reconvening three months from now. Thanks again.

Moderator: Ladies and gentlemen this concludes your conference for today. Thank you for your participation and for using Door Sabha's conference call service. You may disconnect your lines now. Thank you and have a pleasant day.