IDFC Limited

Transcript of FY13 Earnings Conference Call
May 2, 2013

Moderator Ladies and gentlemen good day and welcome to IDFC Limited's FY13 Earnings Conference Call. As a reminder for the duration of the conference all participants lines will be in the listen only mode. There will be an opportunity for you to ask questions at the end of today's presentation, if you should need assistance during the conference call, please signal an operator by pressing "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Bimal Giri of IDFC Limited.

Bimal Giri Good morning everyone. I welcome you to this conference call organized to discuss our financial results of Fiscal 13. I have with me Rajiv Lall, Vikram Limaye, Sunil Kakar and Sadashiv Rao. Before we begin I would like to state that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. Documents relating to our financial performance have been e-mailed to all of you. These documents have also been posted on our corporate website. I now invite Sunil to provide key highlights of our performance for Fiscal 13.

Sunil Kakar Before we start with the numbers I would like to share with you that Mr. Deepak Parekh, our Founding Chairman has stepped down from the Board but will remain associated with IDFC in a new role as the Chairman of the IDFC Advisory Council, a consultative body comprising 3 to 4 eminent persons to be constituted in the coming months. Rajiv Lall who was serving as the Vice-Chairman and Managing Director of IDFC has now been appointed as the Executive Chairman of IDFC and Vikram Limaye who was serving as the Deputy Managing Director of IDFC has been appointed as MD and CEO of IDFC. Congratulations, both of you. These are subject to ratification of the shareholders at the ensuing AGM.

Now I will take you through the macro context, some numbers, recent developments and then we can start with the Q&A.

On macro – the urgency for resolving fuel security issues for power generators seems to have taken a small back step although the budget announcement of Coal India using PPP framework to augment production could help over the medium term. Key states who were dominant contributors to the accumulated SEB losses are now signatories to the FRP for power distribution companies. CERC's orders on variable compensatory tariff for Adani and Tata's augur relief for power developers but we will have to await the conclusion of these proceedings. A regulator for roads, an award of 3,000 kms under the EPC route has been announced in the budget speech and are welcome steps. NHAI's efforts to bilaterally work with developers and clear projects expeditiously strengthens hopes on CAPEX revival in roads. The de-linking of forests and environmental clearances for linear projects should also expedite development of roads, rails and transmission lines. The 15% investment allowance for CAPEX of Rs. 100 crore and above announced in the budget and CCCI clearances for projects in mining, oil and gas exploration are a few positive steps. It appears that we are heading in the right direction but private CAPEX revival could take some time.

Now onto our balance sheet – Our balance sheet increased by 16% from Rs. 61,000 crore as of 31st March 2012 to Rs. 71,000 crore as of March 31st, 2013. In line with our guidance of 15 to 20% growth, our gross loan book increased by 16% from Rs. 48,887 crore as of March 12 to Rs. 56,595 crore as of March 2013. On the liability side, our outstanding borrowings increased to 17% from Rs. 46,435 crore as of March 12 to Rs. 54,227 crore as of March 13. We raised $ 525 million through ECB in FY13, this is our largest borrowing in a single year through this route. Efforts to diversify our institutional investor base have yielded with almost over 1,000 PF investors, now as a part of our borrowing program. Gross approvals decreased by 17% from Rs. 31,868 crore to Rs. 26,576 crore in FY13. Gross disbursements also decreased by 4% from Rs. 18,400 crore to Rs.17,695 crore in FY13. Energy, transportation and telecommunications continue to be the top three sectors contributing 41%, 24% and 23% respectively of the total outstanding disbursement.

Now moving on to the P&L – On a consolidated basis, our operating income increased by 16% from Rs. 2,980 crore to Rs. 3,468 crore in FY13. Net interest income increased by 22% from Rs. 2,096 crore to Rs. 2,564 crore in FY13, this was driven by the net interest income from loans which expanded 26% from Rs. 1,880 crore to Rs. 2,365 crore in FY13. The second component of our operating income which is the non-interest income increased by 3% from Rs. 860 crore in FY12 to Rs. 883 crore in FY13. Net of principle gains, non-interest income however increased by 36% from Rs. 511 crore to Rs. 696 crore. Our fixed income revenues increased by 128% from Rs. 52 crore in FY12 to Rs. 119 crore in FY13 and loan book related fees also increased by 53% from Rs. 124 crore in FY12 to Rs. 189 crore in FY13. Operating expenses were at almost Rs. 525 crore in FY13 as against Rs. 523 crore in FY12. Total provisions for various asset classes increased by 23% from Rs. 285 crore in FY12 to Rs. 350 crore in FY13. Loan provisions in FY13 were Rs. 206 crore as against Rs. 186 crore, our loan loss reserves were 1.7% in FY13 up from 1.5%. Profit after tax increased by 18% from Rs. 1,554 crore to Rs. 1,836 crore in FY13. Net of principal gains, the PAT increased by 34% from Rs. 1,251 crore in FY12 to Rs. 1,676 crore in FY13.

Details on some key ratios in FY12 and '13 – Overall average spread improved from 235 basis points to 246 basis points, however NIMs declined from 4.3% to 4.1% on account of increase in average leverage from 4.5x to 5.51x. Cost to income ratio decreased from 17.5% to 15.1%. Consequently ROE has increased from 13% to 14%. ROA has moved slightly down from 2.9 to 2.8. Leverage based on closing balance increased from 5 to 5.2. EPS, fully diluted increased from Rs. 10.20 per share to Rs. 12.06 per share in FY13. Our existing policies and conservative approach resulted in our cumulative provision for various asset classes being at Rs. 1,416 crore as on March 2013, of this Rs. 1,033 crore is towards loans and Rs. 382 crore is for different investments. As of March 31st our asset quality continues to be robust with our gross NPL at 15 basis points and net NPL at 5 basis points.

Now on to some other developments – The RBI has issued final guidelines for new banks, we are keenly interested in applying for a bank license and we are awaiting certain clarifications from RBI which would be important in this regard. IDFC signed a $ US250 million loan agreement with OPIC which is a development financial institution set up by the Government of USA, this is our largest ECB transaction to date. In Q4 FY13 we have been ranked as number three globally in PPP deals and number four in Asia in overall project finance deals by Dealogic. I shall now open this session for Q&A.

Moderator Ladies and gentlemen we will now begin the question and answer session. Our first question is from Mahrukh Adajania of Standard Chartered.

Mahrukh Adajania Firstly in your capital market related fees is that just to do with transactions in the early part of the year and expansion of market share or would there be any one-offs as well and if you could give some details on market shares? I am talking about all capital market related businesses which is institutional, broking and investment banking. Lastly if you could provide details of AUMs of mutual funds as well?

Vikram Limaye I think first the asset management business, we have grown market share in that business and today our market share is close to 4% and that business has done very well in terms of margins as well as in terms of fund performance. As far as the investment banking and broking business is concerned, we have seen a pickup in activity in the last six months and that is reflected in the full-year results where really the pickup has been in the latter half of the year rather than the first half of the year. We do have a pretty robust pipeline of deals in the investment banking space which we hope we're able to conclude in the coming year. The broking business as we all know has its challenges and headwinds largely surrounding compression in margins and the fact that India is effectively an overbroked market, so there are a lot of players and SEBI has also reduced its margins on the domestic business and overall given the industry trends towards technology, automation and number of brokers chasing potentially a reduced volume of business, the broking business has issues surrounding margins and profitability but we're still doing relatively well in that business as well and we hope to increase the market share in that business from where we are. And as I said in the investment banking business we have a robust pipeline of deal flow that we hope to close in the coming year. I think the other important part to remember is that the impact of soft capital markets also has ramifications on exits for our private equity funds and so if markets remain challenging it does cause issues in terms of how we are able to exit from portfolio companies in the funds that we manage and sponsor. So we're hopeful that if markets remain stable or in fact improve then we could get some exits in our private equity portfolio as well.

Mahrukh Adajania And in terms of restructuring, could you quantify the amount of outstanding restructured loans so far. Would you have such details available?

Vikram Limaye We haven't disclosed that number and there is a reason why we do not that because it is in an evolving environment and we have laid out in fair amount of detail the portfolio that we have in the power sector where we face the greatest degree of uncertainty and that uncertainty is largely surrounding the availability of gas and what happens to how the availability of coal and pricing of coal evolves. Now if you think about the gas based assets and if you go through the tree that we have on our power sector exposure, we obviously do have exposure to some gas based assets and to that extent I do not think we believe the question is whether gas will be available but rather when gas will be available and when gas is available we certainly believe that these are economically viable projects. In the interim, for some of those projects where either they are operational and therefore their PLFs have reduced or in fact they are under construction and could become available for producing power but do not have gas, the principal repayment on those assets would need to get pushed back. And so to that extent there will be some restructuring that will be required surrounding the power sector and particularly gas-based assets. But we'll have to see how the situation evolves to really have a firm handle on what that quantum could be.

Rajiv Lall I just wanted to add that as far as IDFC is concerned that we urge you to follow our guidance on our gross NPLs, that is a number that will tell you more precisely what the P&L impact is of all the uncertainties with respect to asset quality. Our gross NPL number today is 0.15, we have guided continuously that number is not going to remain that low. Our guidance for this number for the next 12 months will be a substantial increase from this very low base but it could be up to 1% of assets or advances over the next 12 months. So against that you have to see what we have done with respect to our loan loss reserves. Our loan loss reserves are now 1.8% of loans outstanding and again we are providing guidance that this number is likely to increase to about 2% of loans outstanding over the next 12 months. So just to give you a sense that although we do expect the gross NPL numbers to rise, we are building and we will continue to build a very solid capital cushion to absorb the P&L impact of that. One last point it is a macro point I wanted to make about the asset quality, that although we're guiding our growth NPL's to rise over the next 12 months, this is not to say that the overall asset quality problem continues to deteriorate, they are two different things, there is a lag effect here. In fact till a few months ago we were guiding that asset quality uncertainties continue to deteriorate, now our belief is that the situation has stabilized, so in macro terms we do not believe that asset quality related stress on infrastructure actually deteriorating from here, what you are seeing and you'll likely see in our P&L and balance sheet, is the manifestation of issues that have already been provided in our books for some time.

Mahrukh Adajania And two more questions on cost of funds, what would have been your cost of foreign borrowings this quarter and if interest rates move down would you see your spreads improving or how would it pan out?

Sunil Kakar As you would be aware we run a very closely matched book from an ALM perspective of interest rates, so even if interest move up or down we kind of protect our spreads to a large extent, so we're not very much exposed to interest rates movement as far as spreads go directly but if interest rates come down generally in the environment that would be good for our borrowers as their cash flows will improve and therefore my asset quality would improve also. With respect to the cost, specifically on the margins, it varies depending upon what these SWAP premiums are but they are in line with the domestic borrowing cost of funds of around 9%.

Moderator Our next question is from Parag Jariwala of Macquarie Securities.

Parag Jariwala My question is related to your loan book related fees, during the quarter as well as for the full year it has shown a tremendous improvement but somehow that has not been reflected if you see as compared to our disbursements or sanctioned numbers, so what is the reason for it? Is it that such kind of reflection will come in the next few quarters in terms of disbursements or what exactly is this?

Vikram Limaye You are saying it is much higher than what you expect? So that is an easy one. See there are several transactions as you know, it really depends upon the nature of transactions, there have been some transactions that we have done where we have underwritten large deals and managed to distribute and those transactions were obviously lucrative transactions and those have disproportionate fees than what you would typically get as upfront fees on regular loan disbursements, so there are some transactions that we have done during the year which are in the nature of large underwritten transactions that we have managed to distribute to other firms in the banking system and that is reflected in the increase in loan related fees.

Parag Jariwala What could be our proportion of refinancing which is being done during the quarter as a percentage of your disbursements and also about the full year and if you can give me the guidance for FY14 as well I mean, what proportion of your increase in loans could come from the refinancing business?

Vikram Limaye The pure refinancing business for this year has been 50 to 60%. There have also been corporate loans that we have done because as we have been saying for some time, new project pipeline for core infrastructure has obviously slowed down quite significantly whether it is power or roads and so to that extent the disbursements on actual Greenfield or Brownfield projects have slowed down. We have therefore also said that the refinancing business is not something that we can predict in terms of the quantum of what we can do each year. It is a function of what is going on in the landscape, what is available, how the banking system reacts, what our cost of funds are relative to the banking system, etc. So it is very hard to give you a number that we expect from refinancing from the next 12 months. What we have said is that if new project pipelines does not pick up which is what we are saying we do not expect to in the near term, our overall growth that we are guiding to for the next fiscal is 10 to 15% which is lower than the 16% that we have delivered in this fiscal year. The composition of that as has always been the case will be a mix of corporate loans, project loans, refinancing some special situations and some disbursements from the existing pipeline that remain undisbursed, so as you know we have some loans that we have sanctioned that have not been fully disbursed and so there will be some disbursements that come out of that and then there will be some that come out of refinancing in corporate loans or special situations, a mix of that is hard to pin down at this point.

Moderator We will take our next question from Anand Vasudevan of Franklin Templeton.

Anand Vasudevan You mentioned that you are keenly interested in applying for a banking license and while I understand that there are some grey areas, just wanted to get your thoughts on the strategic attractiveness versus the costs of converting into a bank, if you were required to maintain CRR and SLR on the entire books from day one, is it still worth the cost?

Rajiv Lall Short answer is yes, it is worth the cost. We had characterized it as short-term pain for long-term gain. We cannot get into the details of this discussion for obvious reasons but to give you a sense from an investor point of view what the opportunity could be if you think about it IDFC today has very significant footprint in the corporate landscape but we are able to provide only a very narrow class of products to that client base, converting it into a bank actually opens up the opportunity to serve our existing client base with a range of new products that today actually go to other financials or to other banks. So while there are compliance costs associated with becoming a bank, there are also significant new opportunities that open up and that is just in revenue terms, then from a capital structure point of view, there are opportunities to more sustainably lever up the balance sheet that has positive implications for the return on equity, so net-net we believe that this would be actually medium to long-term, very powerful for the IDFC franchise.

Anand Vasudevan Congratulation to you Rajiv and Vikram on your new roles, I would just like to get some clarity, now that you are being promoted to the Executive Chairman while Vikram is the CEO, can we understand what are the roles and the differentiation between the two of you?

Vikram Limaye I think the simplest way to describe it is that we are joined at the hip.

Moderator Our next question is from Jatinder of CIMB India.

Jatinder Agarwal There is some reclassification in your annual presentation between fixed income and investment banking broking, there is a new line which has come which is fixed income, can you explain the nature of this revenue and why was the reclassification done?

Sunil Kakar The fixed income trading has become an active business segment and hence I thought for proper disclosure purposes it is important that we disclose this independently, so that is all, this is the treasury activity which we were doing earlier and it is the trading income which we're doing.

Jatinder Agarwal So this is government and corporate bonds, right?

Sadashiv Rao Yes, government and corporate bonds.

Jatinder Agarwal Secondly, just on this broad number that is going around that the FM has a list of projects which are up to Rs. 7 lakh odd crore in terms of total investments where projects are stalled and where incremental action is being taken, could you just give a broad sense in terms of what could be the banking sector exposure per say to some of these projects and what is your sense as to how this is moving? We do not seem to see actually such a big pipeline in terms of asset quality concerns generally for the sector and obviously this number is very big, so could you throw some thoughts on this?

Rajiv Lall I have been trying to get our hands on this list, so there are several lists that are floating around, there is one list of projects of above Rs. 1,000 crore, I believe there is a second list that is still under preparation for projects of size higher than Rs. 250 crore. We haven't had really a chance to fully examine all of that. So I guess these are in the nature of speculative comments. One observation would be that there continues to be confusion on two fronts, one is, there is confusion about the difference between refinancing and restructuring. The second is, there is confusion with respect to problem assets versus delays and the two are sort of linked, so when I say refinancing or rescheduling versus restructuring, restructuring connotes that there is a fundamental problem, let's say with capital structure or the design of the project or certain things like that which require a massive intervention, let's say in the nature of a CDR whereas refinancing or rescheduling to be as simple as taking advantage of residual cash flows in a concession that has many more years to run, than the original loan maturity. Accommodating a suitably equity funded delay in project execution on grounds of a land aggregation not having been completed in time, and so on. So these are much less severe in terms of their implications for asset quality for the banking system but however, have material impact in a macro sense because fixed capital investment is not happening on a timely basis. So when we talk about a very large list of whatever the number Rs. 2-3 lakh crore of projects that are caught up in delays, it is a problem potentially from the macro point of view that projects are not coming on stream or not being executed in time and delayed fixed investments and therefore impact for GDP growth. It does not necessarily have the same severe implications for asset quality, so that is possibly the explanation for the disconnect between the lists that are floating around, and the perception or the manifestation of asset quality issues within the bank, but this is just a hypothesis, we will obviously continue to examine all these things and maybe in the next quarter or quarter after that. We will revisit this and share whatever insight we have.

Moderator Our next question is from Vijay Sarathi of Nomura.

Vijay Sarathi With respect to your generation exposure within the energy bucket QoQ your operational exposure has jumped from 14.5% to 17.2% while your construction has come down marginally down from 9.2% to 8.5%. So I would think this is largely because you have picked up operational projects from the others in the 4th Quarter, is that a fair assessment?

Vikram Limaye Yes, I think that would be a fair assessment in light of what we have said earlier, what we have tried to do is to try and make sure that we grow in a way that is lower risk, given all the uncertainties and risks that we see in the environment and therefore we have focused more on operating assets and refinancing opportunities and so that is a reflection of that.

Vijay Sarathi Could you just again kind of give us the potential refinancing opportunity that is there in the entire sector and specific to this quarter, who are the players broadly, at least that you have picked up these exposures from, that will be very useful?

Vikram Limaye So we obviously, cannot talk about specific transactions and clients that we do business with and to your question on the quantum of refinancing opportunity as I said earlier, it is very hard to give you a number at this point in time, on what that exact quantum could be. I have laid out the three or four different components of growth that we have seen and this is not specific to last year, this is actually a phenomenon of the last several years. There is a component of growth that comes from refinancing each year it just so happens that last year that has been disproportionately high because the new project pipeline has dried up and therefore, the growth that we used to get earlier from disbursements on under construction projects or new projects has certainly gone down, our growth has also gone down as a result of that. So the previous year we grew at 28%, last year we have grown at 16%, the coming fiscal year, we are seeing we are growing at 10% to 15% and that has to do with the fact that you cannot count on just refinancing opportunities to grow at 20% plus growth rates because it is very hard to try and count on those opportunities. So it is not possible for us to give you a number at this point on what volume of growth will come from refinancing, but we do believe that growth in the coming fiscal year will be slower than last year on account of new projects, new project pipeline being weak and the fact that we will therefore have to count on either disbursements from our current pipeline or corporate and refinancing opportunities. I mean, there will be some new loans that we sanction on roads and other areas, it is never zero but I'm saying in the grand scheme of things, it is not large enough to fuel growth the way it has historically. One other clarification, I want to make is, I think this was a question that was asked earlier in terms of where we see growth coming from? I think, in terms of the power sector for some time we have not been doing thermal power in coal and gas. We have seen opportunities in the renewable space, whether it is wind or hydro, so to the extent there are good quality opportunities in those areas, we will obviously continue to do business in those areas. We do hope that there will be a pickup in activity in roads as also in ports and depending on what happens with the uncertainty surrounding telecom, there could be some opportunities in the telecom space but that still remains to be seen depending on how some of the issues surrounding, renewal of licenses and spectrum pricing etc. get sorted out over the next couple of quarters.

Moderator Our next question is from Hiren Dasani of Goldman Sachs.

Hiren Dasani I just want to extend on the earlier question on the banking license, I thought the earlier view of the management when the infra financing company's status was notified, was that infra financing status is good enough for you to be a focused infra lender. So just wondering what really changed and made you aggressively go for the banking license?

Vikram Limaye India happened in the interim, Whereas two - three years ago concentrated focus on infrastructure seems like a strategically wise thing to maintain, 36 months on it no longer seems to be the case for the reason that we have been discussing in various fora and so diversification of asset exposure seems to us to be strategically long-term critical for India in view of, shall we say, the disappointing experience we had with stability, predictability and transparency in just the infrastructure space. So asset diversification and product diversification, we believe has much greater merit and value relative to 36 months ago.

Hiren Dasani And we think that we have the necessary capabilities for that diversification as well?

Rajiv Lall Short answer is again, yes, I mean, if you ask the question in 2005, do we have the capability to grow IDFC to a Rs. 70,000 crore balance sheet, we would have found at that stage a number of skeptics at that time, so we will deal with the same issues and concerns, but with a much greater sense of confidence, not only in our own capability but our ability to attract, more importantly, the right talent to drive this initiative. We are not pretending that we, today, have all the skills necessary to drive and grow a banking franchise, but we are definitely saying that we have the ability to attract that talent, we are very confident about that.

Moderator Our next question is from Nischint Chawathe of Kotak Securities.

Nischint Chawathe This pertains to the provisions on your balance sheet, I believe you said that you want to increase the provisions on balance sheet from 1.7% to 2%. So just want to understand how would you space it out over the next couple of quarters? Will you increase the provisioning policy in terms of increase the percentage to gross disbursements or is this going to be an adhoc provision, how will it work?

Sunil Kakar Our model although what you see is only incurred loss or as a percentage of gross disbursements actually, we also do what we call kind of a dynamic provisioning, so we will assess the asset quality of all our books and see what is the potential stress there and the ability in case of a loss given default. We have a complex model and the net of the two will flow through, so the simple answer is, it will be a combination of percentage of disbursements plus one-off provisions, timing of the same will also depend on every quarter, we look at it and see where things are moving.

Vikram Limaye I think what you need to focus on is as a management, what we are saying is we are aware of the environment we are in. We are also aware of our own asset book and as we have said multiple times, we are very focused on asset quality issues as we have been over the last 18-24 months. We are more than adequately provided already for any kind of asset quality issues that might crop up, but given the environment we are in we believe, as a matter of prudence we would like to build those provisions over time. Unless the environment improves materially over the next 12 months, we will continue to build those provisions. If we are able to build those provisions through just the normal process of gross disbursements and what that implies for provisioning, we will do that. If we believe that after doing that we are not getting to the level that we would like it to be we will make incremental provisions as we have done historically as well. I think, the overall philosophy is to try and build enough cushion to try and weather any kind of storm that we might face over the next 12 to 18 months and that we are quite confident we will be able to do over the next 12 months.

Rajiv Lall I just wanted to add one comment to this is that when you look at the trajectory of loan loss provisioning versus the trajectory of NPAs, trajectory of NPAs cannot be smooth, it is what it is but the trajectory of our provisioning relative to the trajectory of NPAs will definitely be smoother.

Sunil Kakar Just for everybody's consumption, accounting for all these higher levels of provisioning, we are still guiding that the top line and bottom line for the next year should be in the range of 10% to 15%. This is accounting for all the excess provisioning.

Moderator Our next question is from Amit Premchandani of UTI Mutual Funds.

Amit Premchandani The question is on some structuring of the loan transactions, in case of an under construction project say if you give loans to thermal power project which is under construction and on completion of project, if the borrower is wanting to change the financer, is there any covenant that the loan agreement that he needs to pay you the NPV of the loss that you have to suffer because the loan is getting shifted or he can just do it by paying a nominal fee?

Sadashiv Rao There are clauses on reset dates. We have the reset stipulated in all our loan agreements. On the reset dates, the borrower can repay you any time without paying any prepayment premium only on the reset dates, however, if he prepays you on dates, other than the reset dates than there are covenants which stipulate that you have to pay as NPV loss.

Vikram Limaye I think if your question is surrounding restructuring, what you need to understand is that any kind of restructuring that results in an NPV loss, we will provide for, that is required by regulation.

Amit Premchandani No, it was not related to the restructuring, it was related to one of the banks has reported a very high CEB income and the claim is that because some loans got shifted they had booked the NPV of the losses?

Vikram Limaye We haven't done any of that.

Amit Premchandani And generally, what is the reset date - 1 year / 3 year or how is it generally structured?

Vikram Limaye It varies, but if you look at our asset duration that will give you an idea of what the average reset date is, so right now it is about 1.7 years-1.8 years, but you should expect that generally in a declining rate environment most borrowers do not want to take long-term, fixed-rate loans. So the reset dates also tend to shorten. So if it is a rising rate environment you would expect borrowers to take three-year resets or five-year resets. In a falling rate environment most want to take a one-year reset.

Moderator Our next question is from Aden Lau of T. Rowe Price.

Aden Lau Your comments of being joint at the hips for fund management, does this mean that going forward and next two to three years' time, we can expect some sort of transition or role?

Rajiv Lall No, I think you can expect that status quo. So we will remain functioning seamlessly in our respective capacities. Vikram as MD & CEO and myself as Chair will continue to drive the franchise together. So if you are saying that is this a precursor to my transition to a non-executive role, there is no such guidance at this time.

Aden Lau In terms of the principal gains of 1.3 billion that we got this quarter, is it right to say that all of that is related to NSE?

Sunil Kakar Yes, it is.

Moderator Our next question is from Amit Ganatra of Religare Asset Management.

Amit Ganatra If one looks at your standalone PAT and your consolidated PAT, the difference was basically Rs. 47 crore negative last year, which has turned to Rs. 69 crore positive, can you highlight the company or the businesses which has led to this turn around?

Vikram Limaye If you look at the overall profitability obviously, a large percentage still comes from the balance sheet business which has the project finance and the fixed income businesses. All our other subsidiaries have delivered profits. So from that standpoint, the asset management business, the investment banking business, and the alternatives business, all are profitable this year.

Amit Ganatra But do you seem to be profitable even last year if I look at the P&L?

Sunil Kakar It depends also lot of dividend income then that gets eliminated and specifically this year also for the standalone, relatively speaking, standalone, there is a subsidiary which we have sold off or rather closed onto this thing, so there was a debit to P&L on the standalone books which have no impact on the consolidation books. So, relatively speaking, we can say that the standalone came down, therefore, the proportion of others compared to standalone went up.

Amit Ganatra And also is it possible to know the PAT numbers of your various subsidiaries?

Sadashiv Rao That will be available to you once our annual report is published.

Moderator Our next question is from Ganeshram Jayaraman of Spark Capital.

Ganesh Jayaraman I wanted to know the proportion of gas projects within your 17.2% of operating power projects?

Rajiv Lall About 1%.

Ganesh Jayaraman Any sense of how much of this could be say mothballed or operating at a very lower PLFs?

Rajiv Lall I doubt if there will be a mothballed, but their PLFs have been declining but so far it has not really affected, they have not reached a critical point of affecting their debt servicing capabilities. Meanwhile their overall outstanding debt also continues to come down, so really the bigger problem for us is gas assets that have just been built more or less about to be completed and are likely to be stranded .

Ganesh Jayaraman Any equity exposure to these projects?

Rajiv Lall No.

Ganesh Jayaraman Second is on your Tier-1 ratio though it looks healthier at 19.8, your leverage is now 5.2x I am saying, so what I want to know is 1) is your comfort number on leverage and 2) your sense of how the credit rating firms will look at it in the light of the balance sheet structure changing more towards operating assets than in the past when they had reservations at 5x leverage?

Sunil Kakar We are comfortable and we have to run alongwith the credit rating agencies. Let me just give a number which is our estimate that I think the maximum leverage we can go to is just around 6-6.1.

Ganesh Jayaraman That is your comfort number or your sense of their comfort number?

Rajiv Lall Our sense of their number.

Ganesh Jayaraman Lastly, could you also give me the quantum of the G-Sec in your treasury of Rs. 9,200 crore treasury book, effectively you have thrown your hat in the banking thing, it could essentially become your SLR?

Sunil Kakar It is fairly large number. We do not want to give specific numbers it would be around 50 to 70%.

Moderator Our next question is from Manish Shukla of Deutsche Securities.

Manish Shukla Basically what I'm saying is for a 0.5% kind of an NPL on your balance sheet expanded by 10%, you are talking of more than Rs. 200 crore of addition to your NPL number. So what I'm saying is, are you already seeing delays on any of your existing projects which make you believe that we could be moving in that direction?

Rajiv Lall There is a lag effect, so we are seeing it,that is why we are guiding you towards that ideal number.

Manish Shukla Secondly, recently NHAI has been so to say a bit more accommodative. So, do you feel that developers are getting comfort and road sector can come back in a big way in fiscal 14?

Rajiv Lall Big way, I do not know but you are right that we have been saying that, that of the three large sectors namely power, telecom and roads, roads is where there could be some return to Greenfield assets creation partly because of NHAI more proactive approach and problem solving and partly because of the simplification of the associated environmental regulations. So baked into our judgment of a 10-15% growth rate for next year as Vikram has been saying is a combination of some Greenfield asset creation most likely in the road sector, along with some refinancing and some acquisition financing possibly for consolidation play.

Sadashiv Rao Just to give you a sense basically the NHAI has given us, set a targets of awarding 7,300 kms of road assets in the current year '13-14, as against actual award of only 1,900 km last year '12-13.

Moderator Next question is from Anand Laddha of HDFC.

Anand Laddha Just again on the asset quality, just to understand you mentioned that you would like to create a standard asset or a contingent provision up to 2% of advances, does it read that some of the projects that are getting delayed or restructured the lenders would have to take some hit, hit can be two ways, one in terms of NPV and other could be a genuine that the project is not viable, so the lenders had to take some hit if you can just clarify on the same?

Vikram Limaye Well I mean any kind of asset quality issues depending on the situation may or may not require a hit but see the point that we are making is that once a person is not able to service debt within the regulatory timeframe that has been stipulated which in our case is 180 days right now and it is coming down as you know over the next two or three days to 90 days, any over dues beyond 90 days requires that asset to be classified as a non-performing asset then what we do with that asset and how we resolve that asset may or may not result in an actual hit. So for instance one aspect of resolution could be asset sales that result in pay down of loans, now that may not result in a hit on the loans. There could be another situation where lenders are willing to forego some interest or some economics because by foregoing that, that loan actually becomes viable over a 10-15 years period, now if there is an economic hit and a NPV hit we have said that we will provide for it, in any event when an asset is classified as a NPA we need to make a certain minimum provision to start with from a regulatory perspective and depending on the nature of that NPA that provision could go up and depending on the resolution of the NPA it may or may not result in a haircut for lenders – it is very situation specific, there is no generic answer.

Anand Laddha Is it fair to assume in your case a 2% provision does not mean a complete hit because as the project over a period time becomes viable there will be some reversal also?

Sunil Kakar Yes of course, that is the concept of dynamic provisioning.

Vikram Limaye Sorry to interrupt this 2% that we are talking about is a cumulative provisioning, so right now we are already at 1.7-1.8% of average loan assets that we are saying over the next 12 months we will take it to 2% or north of 2% of loan assets.

Anand Laddha If I have to look at your standalone provisioning in this fully year, it is at Rs. 394 crore whereas consolidated these are around Rs. 350 odd crore, so there has been some difference is that because there has been some hit it on the subsidiary?

Sunil Kakar I just shared that with you that we have taken a hit on a subsidiary which was already accounted for in the consolidation, so I would not take it twice, right, so it is an elimination, so both numbers are correct.

Moderator Our next question is from Vibha Batra of ICRA.

Vibha Batra My question is on the AUM which has marginally declined for alternatives and for other AMC's it has grown by 9%, so does it reflect unavailability of good investment avenues and possibly AMC would be more diversified than your own balance sheet, so balance sheet has grown by 15%, so what explains this and also the net income from alternatives has dropped while from the AMC business it has seen a 48% increase versus only 9% increase in AUM?

Vikram Limaye So there are two different businesses altogether, right, the asset management business has a mix of debt funds, liquid funds and equity funds like any other asset management business and the growth in the asset management business is a function of various things including retail flows into equity, the nature of the interest rate environment and therefore the mix of assets between bond funds and equity funds and liquid funds, etc., as I said earlier our asset management business has done well and we have managed to grow market share and we are close to 4% market share in our asset management business. We have also been focused on making sure that we are focused on the right products in terms of bond funds and we have got incremental flows in our equity funds as well and therefore the margin on our funds has gone up which has reflected in the profitability of that business. The private equity business is an entirely different business, the fees from our private equity funds are based on funds that we raise and the funds that we raise are typically in 10 year or 12 year funds, so once you raise the money there is a certain period of time in which you have to deploy that money but the life of the fund is typically a ten-year fund and as you deploy that money if you get gains from the investments that you have made that also reflects in the profitability of the alternate business, so there is a fee element to it which is based on the AUM you manage and then there is an element of gains that you make, not only in terms of contribution that we make to the funds but also in terms of the returns that we have made for investors and we share a portion of those returns with the investors. So the profitability of the alternatives business is a function of also the exits that we make and the funds that we deploy, so it is entirely different from the public market assets management business in terms of the economics and how the revenue stream accrues from those two businesses.

Vibha Batra But the very fact that the AUM is almost stagnant so that means that you have not had enough opportunities and second is if AUM was almost stable there has been an 18% decrease in the fees, so that's more because you could not exit this year compared to last year or what is the driving this decline?

Vikram Limaye So two things, one is the AUM can only change on account of two things, one is, because we have sold investments and therefore the AUM comes down or we have raised new funds because of which AUM goes up, so we're in the process of raising funds for infrastructure and over the next 12 months we will raise incremental money for investing in infrastructure and that should result in an increase in AUM. We also have investments we have made historically that we would like to exit at the right point, so that was the comment that I made earlier depending on the nature of capital markets, etc., there could be exits in the private equity funds which could therefore result in a decline in AUM because we have exited certain investments we have made, so if we have not exited investments in the last 12 months it has more to do with the nature of capital markets and our call on whether it is the right time to exit or not. So largely if you look at the funds that we have under management, 80% of the funds have already been committed there is another 20% that needs to be invested which we believe we will be able to do over the next quarter or two.

Vibha Batra If we were to take an outlook on AUM growth and alternatives and also the fee, how would it look in one or two years?

Rajiv Lall It is step function if we raise another 3,000 to 4,000 crore this year, you can expect commensurate fees with that and then those fees will flatten out and will start tapering downwards again until the next time we raise another set of funds. So it is every 3 to 4 years you can expect some step function increase in the fees, so it is like two steps forward and one step backwards and every 3 to 4 years that's what happens, that is how you can model the alternatives fee income.

Vibha Batra And what about the principal gains they have also declined by about 47%?

Rajiv Lall No, principal gains are totally unpredictable that is the challenge of that business, so that depends upon capital markets. You do not want to sell just too smoothen earnings you will sell when you want to maximize profits, so if capital markets improve then there will be no more exits and you'll get more capital gains from that.

Sunil Kakar Compared to last year we also had the sale of our asset management companies. We sold 25% in the JV partnership obviously we would not be doing this every year.

Vibha Batra Adjusted for that how much is the decline?

Vikram Limaye Out of the 350 that you had last year, 80 was relating to the 25% stake that we sold in our asset management business.

Vibha Batra And what is that the distinction between fixed income and loan book related fee?

Sunil Kakar The distinction is fixed income represents corporate bond and G-Sec trading, that is a treasury activity, loan book fees is when we make the lending.

Moderator Our next question is from Kajal Gandhi of ICICI Direct.

Kajal Gandhi Gross NPA has come down in the quarter, so what is the reason for that?

Vikram Limaye Because we sold one NPA asset.

Kajal Gandhi And if we look at the breakup on the loan book that is given, the non-funded exposure has significantly come down on a QoQ basis, so is it that more through funded or how is it?

Sunil Kakar QoQ is a difficult one to monitor, we may have issued certain guarantees in the last quarter which we did not do this year.

Sadashiv Rao Typically the project loans the company necessarily does not always seek funded disbursements, they will want to open an LC, a letter of credit and therefore we would give our letter of comfort for the LC and that will be shown as a non-funded product and as the LC matures that converts into a disbursed asset and it will transact in to a funded product, so it can move quarter-on-quarter differently depending on how the equity shapes up.

Kajal Gandhi Because this number has come down to this level after several, several quarters?

Sadashiv Rao Yes, so then LC would have matured, not just one LC it could be just multiple LC's so depending upon when they mature projects are typically two year implementation, three implementation period the LC's could mature in 6 quarters, could mature in 8 quarters, could mature in 4 quarters, so depending upon how they mature they tend to get translated into funded disbursements.

Vikram Limaye It is not a large number, so I'm not sure what is 500 to 600 crore so in a Rs. 60,000 crore loan book it is very difficult to pinpoint exactly why Rs. 500 crore moved from one category to another.

Moderator Our next question is from Manish Ostwal of KR Choksey.

Manish Ostwal My question is on operating expense growth during this year, your guiding cost-to-income ratio around 17 to 18% but FY13 cost income ratio stood at 15.1%, few percentage points lower than our guidance, so how do we see OPEX growth going forward given the 10 to 15% loan book growth and the growth in other businesses?

Sunil Kakar Yes we have achieved healthy numbers of 15.1 and our effort will be to maintain if not improve upon it, so let us say around 14.7 to 15 in that range but it is a function of many different businesses playing out. See this is on a group consolidated basis, the cost-to-income ratio for my lending or balance sheet businesses is almost in single digits and that because as the income grows cost does not grow appropriately you get that leverage. Now if other businesses which do not consume capital for example investment banking and the broking business and others if they do well then although the cost-to-income ratio may improve but that would be all fee-based income, so it is also a question of which business does well in which particular year, unfortunately as we know that the investment banking and the institutional broking business; specifically the broking business continues to be in a difficult period right now. But overall guidance would be to maintain at this level.

Manish Ostwal Secondly in the exposure data point, the telecom sector saw a decline of 18.9%, was there any large repayment during the quarter?

Sunil Kakar No, we just cancelled some outstanding exposure which they had not drawn down.

Manish Ostwal What is the employee base at the end of a FY13?

Sunil Kakar 574.

Moderator Next question is from Mangesh Kulkarni of Almondz Capital Market. .

Mangesh Kulkarni I just wanted to know just now you mentioned that this principle gains include some NSE stake sale also, so what is our stake after this stake sale in NSE now?

Vikram Limaye 6%.

Mangesh Kulkarni And FIPB has also announced some clearances to the NSE stake sale, so can we expect even this current quarter also some NSE stake sale in this thing?

Vikram Limaye Yes, you can expect in the coming year also some NSE stake sale.

Mangesh Kulkarni And this quarter we have seen some spike in other operating expenses, so any one-off in this?

Vikram Limaye No, there is no one-off in this, these are all part of normal business operations.

Mangesh Kulkarni Because this quarter it was around Rs. 69 crore as an against average run rate of around Rs. 40 to 45 crore?

Sunil Kakar The other operating expense is not seasonalised equal across four quarters, the last quarter does have some catch-up. In the asset management company there was a change in accounting policy kind of thing driven more by the regulatory and hence the increase in expenses is also compensated by increase in income in that space.

Moderator We will take our last question from Manisha Porwal of Taurus Mutual Funds.

Manisha Porwal I wanted to understand about this restructured or rescheduled loans, does it have any extra risk rate weight attached to it than the normal standard asset loans?

Vikram Limaye No.

Manisha Porwal I wanted to ask on this funded and non-funded book, is there any perceived change that we are seeing that it is, recently one of the bigger banks had said that they are planning to withdraw from the performance guarantees which is given to these road projects, so is there any such shift that IDFC also perceives and would it impact any of the road projects that we as an NBFC fund?

Vikram Limaye Strategically we have not taken any such decisions about whether we want to get out of any specific non-funded product. From our standpoint we evaluate risk based on specific projects whether it is funded or non-funded, so there is no such generic decision that we have taken that we're getting out of a certain kind of a product.

Manisha Porwal And in the guidance of NPA which you said could increase to 1%, you said majority it pertains to power and is there any portion of the road projects also that we see deteriorating and contributing to that 1% and if yes, then how much would that be?

Sadashiv Rao There will be very little of road in that mix.

Moderator Thank you very much. I would now like to hand the floor over to Mr. Sunil Kakar for closing comments.

Sunil Kakar Thank you all and we look forward to share with you our progress next quarter.

Moderator Thank you very much members of the management. Ladies and gentlemen on behalf of IDFC Limited that concludes this conference call.