IDFC Limited
FY15 Conference Call Transcript
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Moderator: Ladies and gentlemen, good day and welcome to IDFC Limited FY15 Earnings Conference Call. As a reminder, all participant lines will be in a listen only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' 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 forFY15. I have with me Vikram Limaye, Sunil Kakar, and Pavan Kaushal.

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 15.

Sunil Kakar: Thank you, Bimal. Thanks for joining us today. I will first focus on the macro side and then share key highlights related to FY15 financials. Post that we will open the floor to Q&A.

So let me start with Energy Sector. The Government auctioned coal-blocks which were cancelled by the Supreme Court. The impact on projects need to be assessed in light of the auctions rules not allowing for forward premium to be considered as a variable charge under PPAs. Also, the press reports suggest that the Government plans to cap fixed cost of plants to prevent tariff increase in new PPA. That was on the coal side.

On the gas side, the Government has approved a mechanism to revive and improve utilization of stranded gas based generation capacity. The subsidy from the PSDF which is the Power System Development Fund based on a transparent reverse e-bidding process will provide support for this mechanism. The selected stranded gas based plants will be supplied imported RNLG based on a target PLF of around 30% and a target price of power. The operationalization of the mechanism would involve contribution/sacrifice by key stakeholders which would be the Center, the State, the developers, the gas transporters, etc., to deliver on the target price of power through reduction in duties, taxes, and margins.

Now keeping these two points in view, we feel that the risk surrounding coal and gas assets continues. This is because of the uncertainty surrounding impact of negative bids in coal auctions and gas framework announced by the Government falling short of the plant being able to operate at PLF that support debt servicing. Coal production by Coal India has been showing improving trends this year. The health of Discom continues to languish and progress on resolution of tariff based disputes continue to be slow.

All the key telecom players successfully renewed their spectrum and also added spectrum for data services. To revive investor sentiment and de-risk projects from market risk, NHAI plans to award road projects on a hybrid annuity model. There has been some development in the road sector, specifically in Maharashtra. The impact of Maharashtra Government order which exempts private light motor vehicles and State transport buses from paying tolls at 53 plazas needs to be assessed.

Overall, the macro context is turning supportive and steps in the right direction are being taken, but as we have continued to maintain in the past, the revival of private CAPEX in infrastructure will take some more time.

Now moving on to the FY15 financials:

Our balance sheet growth was 16% year-on-year. However, our gross loan book decreased by 8% from₹59,829 crore as on31st March 2014 to ₹54,745 crore in 31stMarch 2015.However,adjusting for the short term telecom loans in Q4FY15 or in March of FY14; the gross loan book declined by only 2%. In FY15, gross approvals were ₹23,930 crore and gross disbursements were ₹13,830 crore compared to ₹25,683 crore and ₹16,296 crore in the last fiscal. On a consolidated basis, our operating income increased by 9%, from ₹3,735 crore in FY14 to ₹4,064 crore in FY15. However, in line with the loan de-growth the NII decreased by 3% from ₹2,704 in FY14 to ₹2,633 crore in FY15. The Non-interest income increased by 32% from ₹1,003crore in FY14 to ₹1,323 crore in FY15. This was largely on account of capital gains, asset management and trading profits on the fixed income book. The Investment Banking and Broking revenues increased from ₹77 crore in FY14 to ₹80 crore in FY15.

Now, talking about our expenses, the operating expenses increased by 29% from ₹544 crore to ₹704 crore. Adjusted for depreciation write back and Banking related expenses, our operating expenses increased by 21% to₹644 crore. Pre-provisioning operating profit (PPOP) increased by 5% from ₹3,191 crore in FY14 to ₹3,360 crore in FY15. The provisions for loan and investment increased by 61% from ₹628 crore in FY14 to₹1,013 crore in FY15.Specifically, provision for loans increased by 77% from ₹595crore in FY14 to ₹1,055 crore in FY15. Post provision, profit before tax decreased by 8% from ₹2,563 crore in FY14 to ₹2,346 crore in FY15. Profit after tax and minority interest decreased by 5% from ₹1,803crore in FY14 to ₹1,707 crore in FY15. As on 31stMarch 2015, our gross NPLs were 65 basis points and our net NPLs were 22 basis points. The total loan provisions were 4.5% of loans as on March 31, 2015. The net restructured assets were at 7.8% of which 90% relate to the energy sector. Around 75% of these assets relate to coal and gas based assets. Similarly, the coal generators which had put in negative bids in the recent coal auctions and therefore these assets constituted coal based as well as gas based generators. Our net SR(security receipts) were at 0.31% of loans. Based on the outcome of the above mentioned gas and coal assets, we believe that in coming quarters there would be some slippages from restructured assets to NPLs. We continue with our prudent policy of making adequate level of counter cyclical provisions which is reflected in the high level of floating provisions in the last few quarters. We believe that it would take some more quarters before we witness any tangible signs of improvements in the sector. We continue to review our asset quality.

On IDFC Bank, we have received approvals from RBI and SEBI, for the demerger scheme. The demerger scheme has been filed with the Chennai High Court. As part of the Court process, IDFC successfully completed the creditor and shareholder approval for the demerger. We will now open the floor for Q&A.

Moderator: Our first question from the line of Suruchi Jain from Morning Star.

Suruchi Jain: How many more quarters or years do you see the operating expenses going up? Are you already done with key management hire or we would see a lot more key management hiring going forward?

Sunil Kakar: We have hired the key management for the Bank, but the expenses will continue as the hiring of staff i.e the middle management and others would continue. So operating expenses would continue due to the Bank transition. Once we do become a Bank, we would definitely be significantly different from what you have been seeing in the past.

Suruchi Jain: Sure. Also, could you tell us a little bit more about what how would the expansion would look like or is it still too early to talk about that?

Vikram Limaye: It is actually too early to talk about that. I think it might be better to look at it in the July-August time frame. This is because at this point in time we are not going to be discussing the Banks business plan in any detail on this call. So even for other participants who are present, I would just make a gentle comment that please do not ask us the details surrounding the Bank business plan on this call. This is because we will not be able to disclose anything beyond what has already been disclosed which is present in the public domain which says that we will launch the Bank on the 1st of October, 2015 and we will launch with about 20 to 25 branches which will include corporate branches, rural and a small retail footprint. How would it progress going forward we will be able to articulate only later in the year i.e in the July-August time frame.So please do not ask detail questions surrounding the Bank business plan because we will not be able to answer those questions.

Moderator: We have next question from the line of H R Gala from Panav Advisors.

H R Gala: We do understand the issues faced in the infrastructure sectors especially the transportation, energy and telecom where our major chunk of lending is present. It was mentioned earlier that there is still some pain left for a few more quarters, going forward. So on a year-on-year basis what kind of growth do you anticipate in your assets under management?

Vikram Limaye: When you say assets under management I am assuming you are talking about the loan book?

H R Gala: Yes I am talking about the loan book.

Vikram Limaye: The coming fiscal year is going to be a mix of six months of a non-bank framework and six months of banking framework. It is difficult for me to give specific guidance as to where we would end up fiscal 16 from a loan book perspective. The loan book is likely to remain flattish for the first half. Once we become a Bank, our objective would be to do a lot more than just term lending. There would be a lot of banking products which would become available to us which we so far have not been able to do. Also our objective certainly is to grow in non-infra areas from a sector perspective. From a product perspective our objective is to grow beyond term lending. How that would evolve is very early to tell. So that is broadly what I can say in terms of loan book growth.

H R Gala: I appreciate that.

H R Gala: My next question pertains to the notes which have been given with the results. It states that during FY15 our PAT was overstated to the extent of ₹259 crore on account of three major adjustments as compared to ₹130 crore. So is that assessment correct?

Sunil Kakar: So I would not like to use the word overstated.

H R Gala: Alright. Let us say it is 'one off items' rather than 'overstated'.

Sunil Kakar: Yes it is correct to call it a 'one off item'. Now whether it is a 'one off' and continues to be a 'one off' is a matter of time. But I would share with you its key drivers. One was the depreciation change because of Companies Act. The other is because of certain tax write backs our refunds from the tax authority which was a large number….

H R Gala: ₹80 crore.

Sunil Kakar: Yes. So these two definitely continue to seem to be as a 'one off'and therefore you need to make a slight adjustment for these one offs.

H R Gala: I understand. Was there also some reversal of previous year's tax provision for ₹106 crore?

Sunil Kakar: Yes. So as I mentioned earlier that tax related items add up to a large number. But we hope to continue to work with the tax authorities and see what we could get back.

Moderator: We have next question from the line of Abhishek Murarka from IIFL.

Abhishek Murarka: My first question is with respect to your balance sheet mix. Now you have largely achieved an asset mix which deflects something that Commercial Banks usually have i.e of having 60% odd as assets and loans and about 30% odd as investments. Do you see that changing further or that makes you largely continue for the next six months as well?

Sunil Kakar: No the mix should continue in that range.

Abhishek Murarka: Okay. And therefore unless there are some interest reversals or anything, your yields on the overall book should also more or less remain where it is currently?

Sunil Kakar: Yes, the yields would remain at these levels from the loan book. But the margins could make a slight change.

Abhishek Murarka: Okay. Secondly with respect to the restructured portfolio, could you shed some light on this additional ₹980 odd crore which you have added quarter-on-quarter? How many accounts would that be spread against and is that some consortium based restructuring, etc.? What would be the total debt of the largest account that has been restructured something of that sort?

Vikram Limaye: As we indicated before, we don't disclose specific client information and which accounts have been restructured, etc. So, unfortunately we won't be able to get into that level of detail.

Abhishek Murarka: No, I am not asking for specific client account. Let us say that₹500 crore is the largest account that has been restructured. So what sector it is in?

Sunil Kakar: Let me give you whatever flavor of what I think has been mentioned before. 90% is in energy sector. Next are the coal and gas based assets related where presently 75% of the total 100 consist of these two - coal and gas based assets. The gas based assets in the past have been indicating over almost 35-40% of everything and the rest is equally distributed between coal and gas. 75% has to be split; it is oddly 37%or so.

Abhishek Murarka: Okay. This is for incremental restructured.

Sunil Kakar: I am giving you the total. So you could take the last quarters and do the necessary change.

Vikram Limaye: It is broadly the same numbers.

Abhishek Murarka: Okay. At present, the overall provisioning on the balance sheet you have is at 4.5% of loans. Is that a comfortable level at which you have reached or is there more accelerated provisioning which we could expect?

Vikram Limaye: As we have indicated before. We will continue to make provisions for the next couple of quarters till we transition to a Bank. This is an ongoing exercise which is based on our assessment of risk that we are aware of that exists on our books today. This risk is largely to do with the power sector and as Sunil articulated in his opening comments it has to do with two types of risks. One is gas-related and the other which we now have outlined once again which we thought would be behind us surrounds coal based assets where there has been negative bidding. It is likely that the negative bidding cost may not be allowed by the Government to be passed on in the tariffs. Our hope over the last few quarters was that the risks in the power sector would actually come down. Unfortunately as we speak today, those have not come down because the gas-based power plants based on the framework that has been outlined right now, do not seem to be able to service their entire deck based on the framework that has been outlined. While the Government did conduct a very successful coal auction, there is uncertainty surrounding how the negative bids would be treated and whether they would be able to pass on that cost in time. If they are unable to do that then the implications of that on the coal-based power plant and their ability to service debt would need to be revaluated which would obviously be a negative in terms of debt-servicing capability as costs are not allowed to be passed on. So at this point in time, the risks have not come off and therefore we will continue to provide till we see the risks changing materially for the better.

Moderator: We have next question from the line of Amit Premchandani from UTI Mutual Fund.

Amit Premchandani: My question is with respect to the process of listing of the Bank and demerger. Will there be a period during which the listing of IDFC Limited would be in suspension during that transition period?

Vikram Limaye: There will be no suspension of IDFC Limited. IDFC Bank will get listed once we achieve the demerger. There will be some period of time and it will not be immediately when we get court order. There will be some time lag of few weeks but within few weeks of actually completing the demerger process you will have two listed entities. IDFC will continue to be a listed entity throughout so there will no discontinuity there and IDFC Bank will become a listed entity.

Amit Premchandani: My next question is with respect to the current budget. Some changes were proposed for the IDF structure i.e some more structures were allowed under IDF. So how does it change the size of assets which are available for IDF from IDFC point of view?

Sunil Kakar: Actually regulation surrounding IDF are still awaited we hope to get those in the next week or two.

Vikram Limaye: But I would say that the broadening of the mandate for IDF is actually a huge positive more generally for the economy as well because you require incremental vehicles for infrastructure financing. It is certainly from our perspective as you know we have already got a license to do this work and we have a new entity which is an IDF, NBFC that has already been formed. So we expect this entity overtime to be a large entity and we will wait for what the regulation say. There will be some assets that we will be able to transfer from our balance sheet to the IDF NBFC. The exact quantum we are still determining and we will have a handle on that once we get the detailed guidelines from the Reserve Bank of India. But there will be some assets that we will be able to transfer from our balance sheet to IDF and then more generally the opportunity landscape is quite large for operating assets and overtime will increase. This will be a fairly large area for IDFs to participate in because now the regulation allow IDF to effectively refinance all operating infrastructure assets whether PPP or no PPP and whether they have a tripartite agreement or not as long as they have satisfactory one year of operations post construction.

Amit Premchandani: My next question is with respect to the principal gains which is present in the equity book. Is it in the equity book held by the IDFC Limited or PE of project equity related gains?

Sunil Kakar: IDFC Limited.

Moderator: We have the next question from the line of Vibha Batra from ICRA Limited.

Vibha Batra: My first question is with respect to the fiscal health of Discoms. My question is not necessarily related to IDFC's direct exposure to the Discoms. But considering they are a large counterparty I want your views as being a key lender to the sector. The physical health of Discoms is quite bad and we have seen that several conditions under FRP scheme are not being followed. Possibly due to the large losses these Discoms are incurring, they are resorting to power cuts. Despite several developers being ready with their power plant they are not getting into PPAs. So what is your take of this situation and do you think we are expecting any remedial regulations? Also, what are the key lenders doing about this whole situation?

Pavan Kaushal We are not expecting anything new immediately. Well, the health of the Discoms has not really changed and continues to be a challenge. Also, I am not sure what you are able to add because nothing has changed and we don't expect anything immediately to come up.

Sunil Kakar: First of all we need to share that from an IDFC perspective we do not have any direct exposure to these Discoms.

Vibha Batra: Yes.

Sunil Kakar: I would request Vikram to add with respect to how the 'Discom' environment would play out.

Vikram Limaye: I think it is a mixed bag. In reality, there are some Discoms that have done a decent job and there are others that are lagging. I think it is fair to say that progress could have been much better. Having said that, when you speak to developers it can be seen that some of the delays have come down by certain States even for the 'Discoms' which were delaying payments in the past. So, incrementally things have changed for the better. There are also several States that are in the process of bidding out PPAs and that again I believe is positive. We will see how those PPAs actually get bid out and what kind of power is actually purchased relative to the generation capacity that exists in the Country. But I believe that going forward there is expectation that there will be more PPAs that would get bid out. This is certainly what the developers are hearing from the States as well. So, relative to the situation 12 months ago, I would say that things have improved. I think there is still enough scope for improvement with respect to having a more disciplined tariff increase and collections, the usual T&D losses, etc., that you see in the Discom system. The hope is that with the present Government and at least the States that are aligned to this Government hopefully would see some more improvement on this front.

Vibha Batra: What is your take on FRP or APDRP? Both of them seem to have or at least one could say that APDRP definitely seems to have failed. As we are almost at the end of the tenure it was supposed to be effective. In FRP, lenders don't seem to be doing anything despites Discoms not sticking to the conditions.

Vikram Limaye: I think maybe we should take this offline because this is more in detail surrounding FRP.

Vibha Batra: Yes, sure. My next question is with respect to the'5:25 scheme'. In general how the '525 scheme' helping i.e are there enough proposals in line for '5:25 scheme' and going forward do you think it would be effective in taking away the stress especially where there are liquidity mismatches?

Pavan Kaushal We have seen a fair few proposals on '525 scheme'. They are all at works in terms of getting resolved. RBI has put in place this scheme to help ease the projects where either there have been shortfalls in cash flow or delays post completion to reset the repayment schedules. So clearly this is a positive. This helps the overall sector ease the cash flows and we are seeing several of these proposals coming through especially in infrastructure power side.

Moderator: We have next question from the line of Pritesh Bumb from Prabhudas Lilladher.

Pritesh Bumb: How much G-Sec portfolio are we holding currently?

Sunil Kakar: About ₹17,000-18,000 crore.

Pritesh Bumb: So it is up from ₹16,000crore last quarter?

Sunil Kakar: Yes. As I said that it is not necessarily only for the SLR requirement. It is also our call on the interest rates.

Pritesh Bumb: Currently, how much would be our liquidity coverage ratio?

Pavan Kaushal We are pretty close to 1:1 right now.

Pritesh Bumb: Okay, so that is way above the statutory requirement?

Vikram Limaye: Yes.

Pritesh Bumb: We have been raising some of the infra bonds from last quarter. So in the present quarter how much infra bonds we have raised?

Sunil Kakar: So overall outstanding is in the range of about ₹6,000 odd crore. This is an ongoing exercise and so we would not have specific details available.

Pritesh Bumb: Okay. Some of the assets would be there in the NBFC. So when would we move to the new recognition norms of NPAs i.e to about 150 days from the current 180 days?

Sunil Kakar: This quarter we moved to 150 days.

Pritesh Bumb: Okay, you have moved to 150 days. So any addition was there from that bucket?

Sunil Kakar: No, this quarter we will move that is the June end.

Pritesh Bumb: Okay. So how much could be in that bucket if you could provide any quantification?

Vikram Limaye: No. We will have an active discussion end of June.

Moderator: We have next question from the line of Abhinav Ganeshan from Canara Bank.

Abhinav Ganeshan: My question is with respect to your gas-based assets NPL. What would be the breakeven PLF?

Vikram Limaye: Broadly on these assets as you know, once you get a 60-70% PLF, you can't end up servicing your debt. At present, our NPAs are at Rs.0.7 crore and our net NPAs stand at 0.2 crore which do not include any gas-based assets.

Abhinav Ganeshan: It is part of your restructured book.

Sunil Kakar: Restructured book has Gas-based assets and the answer to your question is around 60-65%.

Pavan Kaushal Actually the breakeven is a combination of two things, one is the PLF factor which we said is 60-65% and second is the tariff itself i.e the PPA itself. So both these are required to be looked at and not one.

Moderator: We have the next question from the line Devam Modi from Equirus Securities.

Devam Modi: My question is with respect to the gas subsidy mechanism. It was mentioned earlier that it will become clearer as the weeks pass from hereon and the peak PLF would only be 25 to 30% of the standard gas-based plants. Also you are looking at a tariff of around in the range of ₹5 or ₹5.2. So in that case are you looking at some write-offs in your portfolio or further provisioning requirements?

Vikram Limaye: As we have said before, we continue to make provisions based on our assessment of risk. We have been now talking about our exposure to gas assets for may be 18 months or maybe longer i.e 24 months. Therefore, those numbers are all well-known and are in the public domain. As mentioned before, we continue to evaluate what would be the kind of provisions that would be required for gas assets specifically. There are discussions going on with regards to the gas framework. Each developer and each asset is not necessarily in the same spot, and ultimately as we have said before, our idea is to cushion the Banks' balance sheet from risks that we are aware of as we speak. So, if we have to make asset specific provisions against gas-based assets we would do it at the appropriate time based on our assessment of the risk. Depending on how this framework that has been outlined unfolds for each specific asset and promoter.

Sunil Kakar: Also, everybody is not in the same place and same boat.

Pavan Kaushal I think if you just wait for the bids which are supposed to happen in the month of May as we would be in a position to know what would happen for each of the assets.

Sunil Kakar: So we have been saying this for quite some time and even in this discussion we have shared that directionally the provisioning will continue to for at least for the next two quarters.

Devam Modi: We have seen our cost of funds coming down in this quarter. But how much further scope do we see based on the repo decreases and also due to dropping of bond yields. Is there any further scope of reduction and cost of funds from here?

Sunil Kakar: On the margins i.e our incremental borrowings remain competitive. So if the market rate i.e the G-Sec rates drop further, then we would see some benefit in the marginal cost of funds also flowing to us. It may be 5-10 basis points but again this is a guess and there is no science behind this.

Devam Modi: Correct. Are we sort of looking at ramping up the fund raise or looking at any more new fund raisings in the alternative funds front?

Vikram Limaye: There are a couple of new funds that we are planning to raise. One fund would be based on the private equity side. As you know we have three private equity funds and are planning to raise our fourth private equity fund for which we are targeting around $400 to $500 million. The second fund which we are trying to raise is the real estate focused fund on affordable housing. The third fund which is still in the discussion stage is a fund that is focused more on structured debt.

Devam Modi: What size would the real estate focused fund and structured debt fund be?

Vikram Limaye: The real estate fund could be around 250 million and structured debt could be 500 million.

Devam Modi: So we already have some real estate fund that is partly there or this is ₹250 million fresh?

Vikram Limaye: This is all new fund raising that I am talking about. We already have one domestic real estate fund that we have raised a year ago of about ₹750 crore.

Moderator: We have next question from the line of Mangesh Kulkarni from Almondz Global Securities Limited.

Mangesh Kulkarni: In the present quarter we have booked principal gains of around ₹222 crore. So does this include NSE stake sale?

Vikram Limaye: Yes.

Mangesh Kulkarni: Okay. This is because other institutions have failed to sell any further stake in the NSE. How much current balance is currently present in NSE?

Vikram Limaye: We own about 4% of NSE.

Mangesh Kulkarni: Would that be sold before our transformation into bank?

Vikram Limaye: Not necessarily, we don't know.

Moderator: We have the next question from the line of Aniruddha Kekatpure from JM Financial.

Aniruddha Kekatpure: How are you seeing the opportunity in the renewable space which is being seen quite enthusiastically in the industry? Do you have any plans of ramping up on that side especially given that RBI has also allowed the renewable space to be included in the BSL norms?

Vikram Limaye: The individual ticket size of renewable space BSL norms is quite small i.e about ₹10 crore to ₹15 crore. Those are not the type of loans that we end up doing. The renewable space has actually been quite active. We expect it to continue to remain active certainly on the wind side. Increasingly there are solar related projects that we are thinking about given the Government focus on developing solar. So I believe that the renewable space for the foreseeable future will continue to remain active. We have got enough exposure to the renewable space and would selectively look at financing renewable projects as we have done in the past.

Aniruddha Kekatpure: Are you planning to finance any large growth in that segment?

Vikram Limaye: If there is a project that is worth financing we will finance it.

Moderator: I now hand over the floor back to the management for their closing remarks.

Bimal Giri: Thank you all. We look forward to our next quarterly results call. .

Moderator: Ladies and gentlemen on behalf of IDFC Limited that concludes this conference call. Thank you for joining us.