# IDFC Limited

## Q4 FY17 Earnings Conference Call Transcript
## April 28, 2017

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**Moderator:** Ladies and gentlemen, good day and welcome to the IDFC Limited Q4 FY17 Earnings Conference Call. As a reminder, all participants' lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal for an operator by pressing '*' followed by '0' on your Touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Bimal Giri from IDFC Limited. Thank you and over to you, Mr. Giri.

**Bimal Giri:** Good evening everyone. I welcome you to this conference call organized to discuss our financial results for Fiscal 17. I have with me Vikram Limaye, Bipin Gemani and Sunil Kakar who is a special invitee representing IDFC Bank.

Before we begin, I would like to state that some of the statements made in today's discussion 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 Bipin to provide key highlights of our performance for fiscal 17.

**Bipin Gemani:** Thank you, Bimal. I will briefly take you all through our progress in respect of IDFC consolidated financials, Bank, Mutual Fund, IDF, Alternatives and IDFC Securities.

The consolidated balance sheet of IDFC as on March 31st, 2017 was Rs. 117,548 crore. In FY17 the consolidated PAT was Rs. 699 crore. The consolidated net worth as on March 31st, 2017 was Rs. 10,820 crore. The Board recommended a dividend of Rs. 0.25 per share. Performance of our bank in FY17 has been shared with all of you, briefly, the growth was strong. The balance sheet and further credit grew by 35%. Overall credit growth was 58%. Net profit grew by 25% vis-à-vis 2016 annualized. Asset quality as reflected by gross non-performing loans and net non-performing loans stood at 3% and 1% respectively. 25% of our funded book has been retailized and our exposure to the infrastructure sector is now down to 54%.

We have onboarded 1.4 million customers and in the month of March we acquired over 60,000 customers. Our network has grown at an accelerated pace. We now have over 8,600 points of presence covering 220 states, 150 districts, 19 major cities and 33,000 villages across India. Our franchise fee is now at 12% of the operating income. We now have Rs. 2,100 crore of CASA. Our retail business is now growing traction. Our product suite both for assets & liabilities across customer segments in retail is now complete. Organic retail asset as of March 31, 2017 is Rs. 2,800 crore. Bank wise CASA and retail fixed deposits were close to Rs. 5,000 crore. In the mutual fund, AUM as at March 31, 2017 was Rs. 57,000 crore. Revenues and net profits for our mutual fund business were Rs. 310 crore and Rs. 97 crore respectively.

During the year, we launched new products such as credit fund and balance fund, the fund performance has been strong. Also as you must be aware we bought back Natixis 25% stake in March and now own 100% of the business. The plans for the next 12 months in this business is to invest aggressively to grow the market share.

As on March 31, 2017, our loan book in IDFC Infrastructure Finance Limited was Rs. 2,683 crore across 37 companies. It is a well-diversified portfolio across roads, renewables, education, healthcare, telecom, SEZ and others. The pipeline for disbursement continue to be healthy. Our debentures and CPs continue to command the highest domestic credit rating of ROA and ROE in this business were 3.5% and 11.5% respectively. Asset quality was strong with nil NPL, net profit in FY17 were Rs. 71 crore. As you must be aware we own 81% of this business.

In Alternatives, our AUMs were over Rs. 17,700 crore in nine funds across three asset classes infrastructure, private equity and real estate. We established our credentials in the startup investing space we have launched a fund in collaboration with Parampara with the target size of around Rs. 100 crore, of which now we have commitments of around Rs. 75 crore. Our private equity fund for focused on consumption theme has witnessed its first close with commitment of Rs. 650 crore. We are also exploring various possibilities for raising new funds in the space of Private Debt and Student Housing. Our PAT from this business in Fiscal 17 was Rs.19 crore.

In our Securities business, notwithstanding the structural issues faced by the industry, we continued to do well. We have strengthened our institutional sales and research to service domestic institutional investors and FII across the globe translating to a well-diversified broking revenues mix across geographies. In fiscal ’17 this business witnessed strong growth in market share in broking across domestic and foreign institutions and has a strong pipeline for capital market business including launching the first InvIT for IRB shortly. For this year, the business delivered revenue of Rs. 81 crore with a net profit of Rs.11 crore.

To conclude fiscal ’17 for the good year for all our businesses owned by IDFC and we are confident of maintaining the momentum in coming years. With this update, we open the floor for Q&A.

**Moderator** Thank you, sir. Ladies and gentlemen, we will now begin with the question and answer session.

The first question is from the line of Arun Rangarasan, an individual investor. Please go ahead.

**Arun Rangarasan:** Sir, my question is that what is the timeline for the reduction of stake in IDFC Bank from 53% we have to go to 40% and then it has to be reduced to 15% what is the timeline for that? That is one question. The next question is what are the steps being taken on the management side to reduce the holding company discount? And the third one will be, is there any new line of business which we are planning to venture out in this current financial year onwards? Thank you.

**Vikram Limaye:** So the first question regulatorily we have to come down to 40% in three years. So as you know it is about 18 months since we started the bank. So there is another

18 months to go by which time we have to come down to 40%. Now that obviously we can take various routes to get there. As you might have heard on the IDFC Bank call as well, part of the strategy for growing IDFC Bank is to look at inorganic opportunities. So that it could be a part of the reduction in IDFC Bank stake from IDFC Limited could be on account of an inorganic opportunity that IDFC Bank has and a certain part will potentially be coming from selling the shares. But the time line that we have is another 18 months, to get down to 40%. Your second question was surrounding?

**Arun Rangarasan:** The holding company discount.

**Vikram Limaye:** Holding company discount so you know we have said this before that in theory, there are various things that one can do but it has to be something that the regulator is willing to accept and gives approval for. So we continue to be in conversation with the RBI. There are one or two possibilities of how we could reduce the holding company discount. I do not want to get into details of that because unless we have some buy in from the regulator there is no point in speculating. But you should know that obviously, the Management and the Board is certainly aware of the fact that there are some structural impediments in terms of constraints on growth and shareholder value, etc and we are focused on trying to see how we can reduce that friction, if you like, by working with the regulator to find some viable solutions. And the third question you had was surrounding new businesses.

Again, as part of the bank licensing conditions, for three years after starting the bank there was a restriction in terms of getting into any financially regulated business. So we will have to wait for another year before we can start any financially regulated business because we are already more than 18 months into the bank. That does not preclude us from getting into any non-financially regulated businesses. So one of the areas that we have been looking at as part of our Alternatives business, could be done through the IDFC platform, is an initiative surrounding student housing. But I cannot elaborate more on that till there is some definitive traction on exactly what we are going to do etcetera but as I said there are opportunities outside financially regulated businesses if they appear interesting and attractive those could be pursued.

**Arun Rangarasan:** Okay I did not get that sir, what are we looking at sir is not the specifics but the area, I did not hear it properly?

**Vikram Limaye:** Student housing

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

**Nischint Chawathe:** So, this is on the IDF. Just wanted to know (a) what is the book yield on these loans of around Rs. 27 odd Billion, and the other thing was to what extent can you leverage this business?

**Vikram Limaye:** So, the yield on this business on a historical basis for FY17 if you look at the spreads have been about 2% and we do not expect that going forward because of variety of reasons that you are aware of in terms of MCLR pressure, in terms of being able to refinance operating infrastructure assets etc. So going forward I think the spread on this business could be about 120 to 130 basis points over our cost of funds. It is still an interesting business from an ROE perspective.

So you know it's almost a 12% ROE business in FY17 we certainly believe it could be higher than that over time. Growth in this business again given what is going on in the market right now it is not easy to refinance operating cash generating assets because everybody who has those assets is doing whatever it takes to retain those assets. Having said that, we have a pretty good pipeline of opportunities that we are focused on and based on what we are seeing I feel that this business can certainly from the Rs. 2,600 crore, Rs. 2,700 crore get to Rs. 4,000 crore plus in the coming fiscal year with interesting ROEs that I have already described to you.

Depending on what happens in the infrastructure landscape over time, this could be a very large business for us and in terms of risk return actually a very good business because as you know this entity is a tax exempt entity and if we are able to scale it up at 13%, 14% ROE, or even higher it is a very nice business in terms of profitability.

**Nischint Chawathe:** So you are kind of indicating maybe somewhere close to eight times sort of a leverage. Is that the right reading?

**Vikram Limaye:** Yeah, seven to eight times you should be able to get because it is all operating infrastructure assets. So right now we have not tested that leverage number because we still have almost 30% capital adequacy, so we have to grow into our capital. But if I were to look at what our experience in IDFC Limited as a AAA entity and IDFC used to finance under construction and operating assets, we should be able to get six times leverage, so if you are doing pure operating assets you should be able to get higher than that.

**Nischint Chawathe:** And this would be borrowing from the Banks or are you looking at any specialized lines of funding for the IDF?

**Vikram Limaye:** So right now it has been done largely through bonds because one of the issues that the infra-finance company has by regulation is that only 10% of its liabilities can be in short tenure. The rest have to be in five years or longer tenure. So most of our funding has been done through the bond market and we will see how we can manage the ALM on that. We are obviously managing it even today. But in terms of even what pools of capital and in what maturity buckets and what tenures we raise money so that we get a profile that is not all five years plus but it is some sort of a structured staggered pool that is raised across different maturities.

**Nischint Chawathe:** So the only risk possibly I would say in this business is possibly some kind of an interest rate risk because you would be borrowing bonds which are sort of fixed rate long and somewhere on the asset side there is always a risk of prepayment because of interest rates falling or so?

**Vikram Limaye:** Yeah and for that reason we are obviously focused on making sure that our ALM is matched and we can use different ways of doing that obviously, we can do swaps which I described to you in terms of raising debt in different maturities although the final maturity could be a long dated security is another way of thinking about it in terms of how you manage your ALM. So what I want to say is that we will not run big mismatches in the ALM that would expose us to that kind of risk.

We are also focused on getting assets that have more fixed returns rather than shorter resets, longer resets, it may not be five year reset, maybe three year reset but right now we have a lot of assets that are actually five year resets and beyond and as you look at the way the interest rate cycle is right now I do not think the expectation is that interest rates are going down. So we should be able to lock in assets for a longer period of time because most people feel that the rates have either bottomed out and will stay where they are or could actually inch up.

**Nischint Chawathe:** Sure. Just one last question on this. Is there any scope of booking any fees out there in this or not?

**Vikram Limaye:** Actually we do quite well in booking fees. I am not sure whether it is there in the presentation but we have actually booked healthy amount of fees for the asset book that we have. So on average if you look at the fees loan related fees that we booked it would be probably 30-40 basis points.

**Moderator:** Thank you. The next question is from the line of Yash Agarwal from Crest Capital. Please go ahead.

**Yash Agarwal:** I had one small question. This AMC stake purchase that you have done of about Rs.250 crore, how do you finance that, is there some cash at the holding company?

**Vikram Limaye:** Yes, so this is something that we were obviously aware of right in terms of the timing, when the conversation would happen with Natixis because it was based on a contractual agreement. When we did the demerger, we have kept aside capital anticipating for this investment.

**Yash Agarwal:** Okay so is there anything substantial capital left at the holding company?

**Vikram Limaye:** Again like I said, based on the known commitments that we had whether it was to our alternative fund or to the Natixis transaction etcetera we kept aside appropriate capital to fund those commitments.

**Yash Agarwal:** And I have one more question, the IDFC Bank is looking at some tie up with IOC or something is it?

**Vikram Limaye:** I will ask Sunil to answer that.

**Sunil Kakar:** Yes, this is more about having the points-of-presence and payment options as you would know like I mean in the old world of banking, if people put up ATMs out there so this is the new way of doing banking out there

**Yash Agarwal:** Right. So but are you going to give any stake to IOC?

**Sunil Kakar:** No, nothing this is just a distribution network arrangement.

**Yash Agarwal:** Because I read somewhere that IOC might buy some percentage stakes so I thought you could route it through IDFC Limited, I read it somewhere it is okay nonetheless.

**Moderator:** Thank you. The next question is from the line of Mangesh Kulkarni from Almondz Global Securities. Please go ahead.

**Mangesh Kulkarni:** After purchasing your stake from the Natixis now what are our plans are we looking for any new partners in the AMC or it means what kind of plans do you have for the AMC to look at?

**Vikram Limaye:** I think the broader plan, I've already outlined, is to focus on growth, market share and scale. It takes different dimension whereas the domestic dimension which has to deal with growing the mutual fund business across our existing products as well as new products. Amongst a couple of new products, the balanced fund, the credit fund which have also scaled up well, our classic equity fund is doing well and is scaling up nicely. So all our existing products we are focused on and growing. The second avenue for growth would be new areas, so there is a plan to grow our PMS business, we should see some products coming out of there, we have hired a couple of people to focus on that.

Our third area is international and there we are open to any kind of arrangement whether it is in equity or not in terms of either raising international money for Indian equities for fixed income or doing managed accounts for either sovereigns or pensions who want to give out managed account mandates. So, since we have closed that purchase only a month ago, we are now actually open to talking to people about how we can grow our international business either through distribution arrangements or through managed accounts or if there is an interesting partnership to be done we are open for that as well.

**Mangesh Kulkarni:** Okay. And in terms of this Capital Market business earlier we used to have separate companies for broking and investment banking, now we have merged those companies?

**Vikram Limaye:** No, the Investment Banking coverage team moved to IDFC Bank only a while ago when we set up the bank because from a coverage standpoint it makes sense. Since the client is the same that the corporate coverage team is integrated with the lending products and all the other banking products that we are offering to our clients. The suite of products, the leverage you have to get fee-based business and the investment banking business is much higher because you have other touch points. A broking business cannot be in the bank because of securities license from SEBI. But as was the case even earlier when the two businesses were in two separate entities there is a revenue sharing arrangement for all Capital Markets businesses in the bank and the securities business which is a 50:50 arrangement for all IPOs, QIPs, etcetera. So that arrangement continues.

**Moderator:** Thank you. The next question is from the line of Harshit Toshniwal from ICICI Securities. Please go ahead.

**Harshit Toshniwal:** Just a few follow up questions. Just wanted to know that out of our AUM what is the share of equity and debt AUM?

**Vikram Limaye:** Equity is about 22%.

**Harshit Toshniwal:** Okay and any figure on the market shares which you have on debt and equity front?

**Vikram Limaye:** The market share is about 3.3% to 3.4% and I hope it goes to 4.5% to 5%.

**Harshit Toshniwal:** Okay and one more thing sir so currently our stake in NSE is at 0.9% if I am not wrong?

**Vikram Limaye:** Excuse me just one clarification the NSE stake is with IDFC Bank not IDFC Limited.

**Harshit Toshniwal:** NSE stake is with IDFC Bank?

**Vikram Limaye:** Yes, the 1% that I mentioned.

**Harshit Toshniwal:** Okay and so IDFC holds no stake in NSE right now?

**Vikram Limaye:** IDFC Limited does not have an equity investment in NSE. When we demerged the assets and liabilities basically all the investments, loans everything went to IDFC Bank.

**Harshit Toshniwal:** So basically the net worth for the IDF as on FY17 close?

**Vikram Limaye:** IDF is about Rs. 650 crore.

**Moderator:** Thank you. The next question is from the line of Harshad Shah, individual investor. Please go ahead.

**Harshad Shah:** I have two questions. One is on the dividend distribution policy, are we planning to have some dividend distribution policy? And the second question is are we planning to have retail in broking divisions?

**Vikram Limaye:** Okay so the first question about the dividend distribution policy is broadly if IDFC Limited has any surplus cash after taking into account commitments that we have, whether it is through our funds or any other businesses, that surplus cash would be distributed as dividend to shareholders. The Board has approved a dividend of Rs. 0.25 a share in today's Board meeting so that it is already in the Press Release but that is broadly the plan. If we have surplus cash after commitments that we have to make to our existing businesses those would be distributed to shareholders. The second question you had was surrounding retail broking, so the idea is that as we grow in our banking footprint and the retail customers in the bank and the Wealth Management business in the bank we have to use our existing IDFC Securities platform to set up a retail broking business on that platform itself. So as of now we have not done it, but that is certainly the plan.

**Moderator:** Thank you. The next question is a follow up question from the line of Harshit Toshniwal from ICICI Securities. Please go ahead.

**Harshit Toshniwal:** Just wanted to know that for the deal in which you purchased that 25% stake in AMC business, so the total valuation for the company was with respect to that deal?

**Vikram Limaye:** No, I do not think you should link the valuation of the company based on mathematically of what we paid. Like I said earlier this was based on a contractual agreement that we had with the Natixis.

**Harshit Toshniwal:** So that was based on the predetermined basically something which was there in the previous clauses?

**Vikram Limaye:** No, I will just leave it at the fact that this was a commercial arrangement with the Natixis. You should not apply your formula to arrive at the valuation of the business. If you just look at what the market multiples are for the business and take 5% of the AUM of Rs. 62,000 crore then you will get an appropriate valuation for the business.

**Harshit Toshniwal:** Okay good, and sir just last question. In broking and IB business our combined book value as at FY17 was?

**Vikram Limaye:** Book value?

**Harshit Toshniwal:** Yeah net worth.

**Vikram Limaye:** About Rs. 146 crore.

**Moderator:** Thank you. We have just got one more follow up question. It is from the line of Arun Rangarasan, individual investor. Please go ahead.

**Arun Rangarasan:** The thing is that in the alternative business, the fund size is around Rs. 17,700 crore. We used to invest 10% of the IDFC's money in business and we used to make 25% of whatever investments we make, that is what I have heard Mr. Vikram Limaye speak about a few years ago. Am I right on this, sir?

**Vikram Limaye:** So, this is a business which as you know is based on one portion of the returns that IDFC gets is on account of management fees and those are broadly in the range of 1.5% to 2% of the corpus that we manage. The second is the return that we make on the money that we invest which is like you said 10% of the capital that we invest and then the third revenue stream is 20% of surplus returns on the 90% that we have not invested this is called carried returns. So those are the three revenue streams that we get on that Rs. 17,000 crore.

The one point you should know is that the capital in these businesses is now with IDFC Bank not with IDFC Limited because as I explained earlier about the NSE investment, when we demerged the assets and liabilities of IDFC Limited into IDFC Bank. The capital commitments to the funds also moved to IDFC Bank so the return on the 10% that is being committed to the fund will go to IDFC Bank. The surplus return and the 20% and the 90% that is not invested that will go to IDFC Limited and the fees on these funds will also go to IDFC Limited.

**Arun Rangarasan:** Okay the 10% invested amount has moved out of IDFC to IDFC Bank balance sheet?

**Vikram Limaye:** Correct.

**Moderator:** Thank you. As there are no further questions I now hand the conference over to the management for closing comments. Over to you.

**Vikram Limaye:** Thank you very much everyone for joining us for our results for FY17. As I said it has been very strong set of results for the group overall and all the underlying businesses. We thank you again for your patience and look forward to talking to you again next quarter.

**Moderator:** Thank you very much, members of the management. Ladies and gentlemen, on behalf of IDFC Limited, that concludes today's conference call. Thank you all for joining us and you may now disconnect your lines.