# Transcript

## Conference Call of IDFC Limited

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*Presentation Session*

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

***Bimal Giri:*** Good afternoon everyone. This is Bimal Giri. I welcome you to this conference call organized to discuss our financial results for the nine months of financial year 2008 announced yesterday. I have with me Rajiv Lalll, Managing Director and CEO, Vikram Limaye, Executive Director New Businesses, and L. K. Narayan, Chief Financial Officer of IDFC. 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 were e-mailed to all of you yesterday. These documents have also been posted on our corporate website. I now invite Rajiv to provide key highlights of our performance.

***Rajiv Lall:*** Thanks Bimal. Good afternoon to all of you. This has been a good nine months, so I am more delighted than I would normally be, to be here with you. Just to take you through the key highlights of our financial performance.

All the numbers are on a consolidated basis for the first nine months of fiscal '08, compared with the first nine months of fiscal '07. Substantial improvement in the operating income, we have seen an increase of 81% from 553 crores to just about 1,000 crores. Likewise, net interest income expanded 54% from 329 crores to 507 crores. Net interest income specifically from infrastructure lending activities was up by 35% from 295 crores to 399 crores. And income from treasury operations more than trebled from 35 crores to 108 crores. Non-interest income also showed very significant growth. It more than doubled from 208 crores first nine months of last year to 487 crores for the first nine months of this year. If you break down this 487 crores, principal investment activities generated 200 crores of income relative to 128 crores for the same period last year. Asset management fees were more or less stable at about 40 crores. Then if you look at our investment banking business, which is now more or less captured through IDFC SSKI, that contributed another 124 crores for the first nine months of this year. And then finally, all the remaining advisory and fee businesses trebled from 40 crores last year to 123 crores for the first nine months of this year. The broad message that you should take away from these developments, from the non-interest income side, is that even if you strip away the contributions from IDFC SSKI, our other non-interest income businesses have been gaining significant traction and it has not come just from capital gains on our investment activities. Our advisory and other fee income lines have also been kicking up quite nicely.

We can, in the Q&A go into some more detail about the nature of this advisory and fees. I will come back to that in the Q&A session.

Let me turn to the operating expenses side. Operating expenses increased as you might expect, quite significantly from 53 crores for the first nine months of last year to 168 crores this year, but a good chunk of this was on account of the line by line consolidation that came from IDFC SSKI. Given the growing importance of our non-lending activities, I think that one possibly evolving but better measure of our operating expenses (rather than focusing on operating expenses to assets ratio) is the operating expense to operating income ratio, on a rolling 12 month basis. And this number has trended upwards, but is still, we think at pretty competitive levels. It has trended up to 17%.

So much for expenses, let's just talk quickly about profits. Consolidated PBT, up 60% from 500 crores to 801 crores. Effective tax rates, as we have been suggesting to you, trended higher, they now stood at 25.7% on a rolling 12 month period. Stripping taxes away, profits after tax grew by very healthy 44% from 411 crores to 593 crores for the first nine months of this year.

A little more colour on our business, looking at it from a ratio analysis. So, if you look at the ROA Tree analysis that we provide to you on a rolling 12 month basis, you will see that our net-interest income was stable at 2.9% on average total assets. And our average overall spread was also more or less stable. Non-interest income, as a share of assets, trended higher, for the reasons we have discussed earlier, from 2.2% last time around to 2.6% for the last most recent 12 months. And operating expenses increased from 0.8% of average assets to 0.9% of average assets. Our return on assets was therefore on a rolling 12 month basis, a healthy 3.2%, and our ROE taking account of the leverage that has kicked in because of the relatively rapid growth of our balance sheet and the additional money we raised in July, the ROE now stands at 16.6%.

Some highlights of the balance sheet. We have increased the size of our balance sheet by a whopping 59% from 16,300 odd crores to 25,900 odd crores. Our loan book expanded substantial by 43% from 13,480 crores to 19,242 crores. Gross approvals for nine months were higher by 60%. Gross disbursements, were up 53% and stood at 8400 crores for the first nine months of this year. Commensurate with the growth of the assets side of our balance sheet, our borrowings also increased by 52%. Outstanding borrowings as of Dec 31, 2007 were 20,390 crores. We continue to diversify the liabilities side of our balance sheet, basically in support of the rapid growth that we are seeing.

If you want to look at concentration of business by sector, the number to focus on is total exposure that gives you a forward looking sense for where our sectoral composition is headed. Our exposure, which expanded by 50% to get to close to 32,000 crores. The Energy and Transportation segments still contribute the lion's share. Energy contributed over 34% of total exposure, with Transport close to 28%. Quality of assets still remains very sound. Still net zero NPAs while Gross NPAs were still 0.14%.

To summarize then, key financial highlights. Rapid growth of the balance sheet with expectations for continued robust growth in the loan pipeline. Strong growth in income, underpinned by supportive margins and spreads, and more importantly growing traction on our non-interest income lines of business.

Some corporate developments that you should be aware of, that are not disclosed in the press release. As far as our third party funds business is concerned, Assets Under Management for the first nine months remain at about 650 million odd, but we are very close now to the first close of our Project Equity Fund, this is the much discussed IDFC Citi Group Fund, I think in the next two to three weeks we will be announcing first closing of that fund, and the number will be, we expect in excess of 500 million for the first closing. The second closing will take place a few months thereafter, and we continue to chase the billion dollar number for the fund, and we are at this point cautiously optimistic that we will get there over the next quarter or so. In preparation for the closing of the fund, we have in fact been warehousing some investments on our own balance sheet. These investments that appear under equity investments on our balance sheet will be transferred to the Project Equity Fund once the closing is done. This is just to give you an indication that the investment pipeline for the type of deals that we are looking to invest equity into, remains quite robust, notwithstanding the very high valuations that you all are contributing to in the market.

As far as private equity fund raising is concerned, we are now more than 2/3rd invested in the second private equity fund. So, we will be in the market very shortly with a fund raising for our third private equity fund. And we expect that by first quarter of next financial year, which is before June 30th of '08, we will close a third private equity fund, which again we expect will be in excess of 500 million dollars.

The integration of IDFC SSKI continues apace. We are very pleased with the way in which that has been evolving. I hope that you are seeing the results of that in the market place. There are a number of high profile transactions for which IDFC SSKI have been retained as the BRLM. We are seeing good traction on the equities business as well as good traction on the financial sponsors and the debt capital markets, which has now been transferred from IDFC to IDFC SSKI.

I think that pretty much wraps up the comments that I wanted to make to kick off this discussion. I will now open up the floor for any questions that you might have. I will be delighted to answer them.

*Question and Answer Session*

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

Our first question comes from Ms. Elizabeth of Keynote Capital.

***Elizabeth:*** I just wanted to ask about mainly the ratios, if you could tell me about the cost, yield, and the spread.

***Rajiv Lall:*** The overall spread for the last 12 months was at 200 basis points, which is the period from January '07 to December '07 and that spread is pretty much the same as it was in the previous 12 month period. Other ratios, cost to income ratio was 15.5%, it is now 17%. The effective tax rate has gone up from 23.6% to 25.7%. So that's one set of ratios that are probably of interest to you. Second set of ratios are really to do with the ROA tree, and there the net interest income as a share of average total assets, has remained stable at 2.9%. Non-interest income as I said in my earlier presentation has gone up from 2.2% of average total assets to 2.6%. Operating expenses have gone up from 0.8 to 0.9 and therefore return on assets has gone up actually from 3.1% to 3.2% of average total assets.

***Elizabeth:*** Thank you sir and regarding the QIP that was being raised, Rs. 2,100 crores, how is the deployment right now, how much percentage is being deployed?

***L. K. Narayanan:*** Actually if you see our disbursements, subsequently I think, we have disbursed on the gross basis of 5,700 crores. So you can infer that all the QIP proceeds of 2,100 crores was deployed in project assets. 23 crores was the QIP issue expenses. So balance of everything has been deployed in project assets already.

***Rajiv Lall:*** Our leverage ratio has gone up from 4.2 to 4.7. It is still lower than what it was pre-QIP. So if you are trying to figure out when we are coming to market next, there is still headroom.

***Elizabeth:*** Okay, and just broadly just looking at the set of numbers, which are there, your operating expenses have risen to a high, so if you could just state the reason for it, and how do you plan to cut down the operating expenses?

***Rajiv Lall:*** We have no intentions of cutting down operating expenses, and we don't agree with you that operating expenses have become too high. Operating expenses, as a share of assets have only gone from 0.8 to 0.9 and that too in large part because of the consolidation line by line of

IDFC SSKI. Remember that we went from 33% ownership of SSKI to 79.8% ownership of SSKI, and therefore, when you are absorbing 200 odd people, into consolidated accounts, that has an immediate impact on our expense line. Profitability per employee, which I think is a relevant metric, is extremely high for IDFC compared to any other financial institution that you want to compare it with. That is point number one. Second point is that, because, as I said in my opening remarks, a growing share of our business is non-balance sheet related, there is a non-interest line of revenues. I am speculating, I am just thinking aloud that going forward; maybe the expense to assets ratio is not as relevant a measure of what an appropriate expense structure is for IDFC, but rather the operating cost to operating income ratio. So, that is a number, if I were in your place, I would track carefully going forward.

***Elizabeth:*** Okay, and regarding the asset management business, could you just describe about the funds which are there and the duration for it?

***Vikram Limaye:*** As Rajiv mentioned, right now we have just the private equity funds that have been in place for the last year plus, 650 million under management and two private equity funds. We are in the process of achieving first close on the infrastructure fund with CitiGroup, and then there is a third private equity fund that is being raised. If all this happens, as contemplated by Q1 of next fiscal year, we should be at close to 2 billion plus in Assets under Management within private equity and project equity, by June 30th.

***Elizabeth:*** Okay, thank you.

***Moderator:*** Next question comes from Ms. Nanditha Parker of Karma Capital.

***Nanditha Parker:*** I just wanted to ask a couple of big picture type of questions, which are, any of the credit market turmoil globally, especially in the US, do you think that starts impacting India, not right away, but somewhere down the line?

***Rajiv Lall:*** Yeah, that is indeed a big question. I was actually at what is called the Neemrana Conference. Neemrana Conference is something that is organized by ICRIER and NCAER in India, and we had the benefit of listening to top academics from the US as well as to senior officials from the Reserve Bank of India, and from the Ministry of Finance, over the weekend and there was actually a great deal of uncertainty that was expressed with respect to the fallout for Asia generally, India in specific, of the turmoil that is taking place in the US and Europe. There are two possible outcomes, as they were discussed, and I thought that, that framework was actually quite compelling. The first possibility is that liquidity will find its way into emerging markets. In which case, we would have a problem of plenty; it's a different kind of problem. We will have actually even more aggressive capital inflows, than we have seen over the last few months. But certainly the US counterparties who have done some research into this, the view is that Indian Banks and Thai Banks, as it turns out, have very limited exposure to US subprime. Amongst Asian countries, it's the Chinese and the Taiwanese, and the Koreans who have some, but not very significant exposure to subprime. So, in this first scenario, given that our financial system is generally protected from direct infection in terms of write downs from the US subprime crisis and liquidity flows from those markets into India, we actually have is a decoupling scenario that is being discussed. The second alternative scenario that was presented at this conference, was that the write downs in the US or the losses are so significant that people who are sitting with excess liquidity that would normally come to emerging markets, would actually have to replenish capital in the US, and therefore rather than having the opportunity to invest in emerging markets, will go back into the US. Now that's a really dire scenario. If I were to sort of make a bet, and that's all it would be, because we really don't have any visibility, I would bet on the first scenario rather than on the second scenario.

***Nanditha Parker:*** Okay. And then sort of related to that, is this notion of domestic liquidity and who is going to fund the 500 billion in terms of infrastructure spending that would be in India and where do you see your share in terms of financing?

***Rajiv Lall:*** Well, I don't know about our share, in some sense our share can only decline, because it's quite high. In a system that is growing as rapidly as ours, I would prognosticate that our share in the total 500 will decline, but that doesn't meant that our own balance sheet will not grow very rapidly. If you believe in the first scenario, the more optimistic scenario, macro-wise, for India that is, then my prognostication would be that Indian financial institutions and banks will get a much greater opportunity to fund infrastructure going forward than in the last 24 to 36 months because foreign financial institutions, given the problems they are facing, in their respective jurisdictions, will have exposure issues with respect to India. And therefore, the size of the overall pie, financing pie for domestic institutions will rise, and that tide will certainly lift IDFC's boat.

***Nanditha Parker:*** Okay. And in order for all this to happen do you think that interest rates have to come down, and do you also think that one of the by products of having so much liquidity and so much money coming into these projects in India is that you see more and more conglomerates and companies taking on projects, which may be less profitable than get into unrelated businesses, and that whole cycle sort of starting all over again that we had in the early 1990s. Do you think there is a risk of that?

***Rajiv Lall:*** There is a risk of that, but I would argue that the crisis that we saw in '94-'95 have left corporate India suitably chastened. I think that they will not very readily make the same mistakes a second time. But I can think of certain corporates who are possibly beginning to behave as if this gravy train will never end, there is always that risk. But I do think that there is a definite change in the way Indian corporates look at risk and the professionalism with which they manage their balance sheet this time around, which would be different. Now that said, you tell me, I don't really know. There is one hypothesis that there are a number of corporates whose surplus cash balances may be being jeopardized as we speak, because of exposures to some derivative transactions they don't fully understand. I leave that thought with you.

***Nanditha Parker:*** That should give me a sleepless night. I think we are beginning to see that, in terms of, and you alluded to private equity valuations cause distress, its high valuations in the public sector market. And we are blaming the private equity guys for what's happening in the public market, so I think it's the tiger chasing the tail here. But there is clearly, high valuations are in everyone's mind, and that obviously leads to lower returns and all of that. And so, just from your standpoint of launching private equity funds, do you see a reduction in opportunities because the space is getting crowded; I know people don't want to think like that, because opportunities are big.

***Rajiv Lall:*** I don't think that there is lack of opportunity. I do think that returns are going to be bid down; there is no doubt about that. I think it's inconceivable that we can continue to deliver 50% IRRs on deals, especially in infrastructure space. But given how robust the returns have been in the past, I am thinking, if returns are bit down even to a third of what we have seen in the past, it would still be pretty solid.

***Nanditha Parker:*** Right. Well, compared to the US, yeah, certainly.

***Rajiv Lall:*** Right. Certainly our approach to our third party funds management business is precisely that, which is to say, it is more disciplined. We are thinking about it as a business that we have to be in, in the long run. So, for example you take the private equity fund, the third private equity fund. We have discussed this internally; I think that Luis doesn't want to raise a billion dollar fund. We are quite happy for him to raise only 600 or 700 million dollars. We don't want to be known for raising the most amount of money, we want to be known as people who know what they are doing in the private equity business, and who can deliver sustained returns over a long period of time.

***Nanditha Parker:*** Right, great. That's great to hear. And then one very micro question in terms of your SSKI acquisition and operating expenses, does this include any bonuses paid in the last cycle, I am just trying to project…

***Rajiv Lall:*** All the SSKI numbers are with prorated bonuses. So there is no end of the year surprises.

***Nanditha Parker:*** Okay good. Thanks so much Rajiv and good luck.

***Moderator:*** Next question comes from Mr. Suresh Ganapathy of Deutsche Bank.

***Suresh Ganapathy:*** Hi Rajiv. I just had a question on your equity book that has decreased QOQ by around 500 crores from 1700 to 1150. So what's the main reason for it?

***Rajiv Lall:*** That's, I think, nomenclature issue. What we have done is the following. We were presenting as an equity book everything that was classified as basically an equity investment. Now, we have made the decision that that which is a subsidiary, or investment in a subsidiary, should be taken out of our equity book.

***Bimal Giri:*** Equity book actually have shown a growth if you look at Q-on-Q basis, I think we will share the numbers with you separately, but we have removed the investments that have been classified as strategic, which is what Rajiv said, the subsidiaries and investments of that kind.

***Rajiv Lall:*** So sequentially, we can say that, what we can share with you is that it's in the investor pack, on a like-to-like basis, adjusting for the definitional changes that we are talking about. For the first nine months of last year, the equity book was 507 crores. So, that's after you stripped out all investments in subsidiary companies. That corpus today, is 1,149 crores. Of the 1,149 crores, you should know that there are 213 crores worth of assets are being warehoused on account of the project equity fund. These will move out. So, if I really strip those out, so take 200 crores out of 1,140, you get to 940 odd crores. So we have moved from 500 crores to 940 crores, that's a like-to-like number, and by the next quarter you would have then a time series, that is more transparent to you.

***Suresh Ganapathy:*** Okay fine. What are the unrealized gains on equity book?

***Rajiv Lall:*** Unrealized gains are getting to be obscene and therefore we don't want to talk about it.

***Suresh Ganapathy:*** So you did disclose till two quarters of this year.

***Rajiv Lall:*** No, because we thought that, we were like little children in the woods, we didn't have any credibility, so we thought that maybe if we talk about unrealized gains, people will be more comfortable with us. Now we feel that we are doing well enough that we don't have to realize on unrealized gains. And needless to say, they are really quite substantial.

***Suresh Ganapathy:*** But that will give you better valuations, right Rajiv, if you disclose?

***Rajiv Lall:*** Valuation is one thing…

***Suresh Ganapathy:*** You don't want to trade at six times the book?

***Rajiv Lall:*** No, I don't want to get into a debate for valuation. I am just saying that from the point of view of management disclosures, if there is a significant investment that we are about to divest from, then we will disclose to you, but otherwise lets say these numbers are really very robust and we are very pleased about them.

***Suresh Ganapathy:*** Okay fine. One last question, your short term loans composition has gone up from 13% to 21% within a single quarter, what's the main reason for this? Do you perceive any ALM mismatch as such, or what's the main reason for it?

***L. K. Narayan:*** No, there is no ALM mismatch at all. In fact, we have the RBI approved norms very diligently followed, and therefore we maintain positive gaps across the majority buckets all the way up to one year.

***Suresh Ganapathy:*** Okay fine. Thanks a lot Rajiv.

***Moderator:*** Next question comes from Mr. Ashish Sharma of Enam Asset Management.

**Ashish Sharma:** Good evening. Just wanted a breakdown on your advisory and fee income for the quarter and the nine months, because for the six months, half-yearly FY08, the advisory fees was only 4 crores, and for this one, we have done close to, 123 crores, so if you can just break down this number for me sir?

**Rajiv Lall:** Yeah, I think your first point is that even under that heading, there are some definitional changes, and those definitional changes have in part been precipitated by the integration of SSKI. So previously, if you recall, the debt capital markets and equity capital markets as we called them, were reported as different line items and revenues accruing to IDFC. Now those two businesses have basically been moved into SSKI. There will still be a little bit of revenue sharing and so on, somewhere, as origination fees and all that. So some share of the overall revenue from that will come to IDFC, but the bulk of that will be captured in SSKI. So the way to look at these things going forward is that when you look at the IDFC SSKI line, this was 124 crores, right, for the first nine months. That's a combination of three things. One is income from brokerage. Second is income from the equities business, which is the IPO business, the equity placement business, the financial sponsors business. And third, there will be the debt capital market, or the fixed income business that is being originated and largely managed out of SSKI. Now, as SSKI's footprint of businesses also grows, there will be other things in that, but for now these are the three things that will be in there. Now then what remains for IDFC in terms of non-interest income, will primarily be asset management, which is a capital line item, which is clear for everybody to see. Then what is advisory and fees, the previous advisory group again, because we have set up SSKI, we are more or less disbanding the advisory function in IDFC. So, the advisory and fees line will comprise of fee businesses that are by and large linked to our loan book. That's the way to look at it. So, what it this, these are front end fees, these are structuring fees, these are guarantee commissions, these are advisory leading to a lending product.

**Ashish Sharma:** Okay, should I assume this to be the carried interest on your…

**Rajiv Lall:** No, carried interest is separate number and that is buried in our capital gains.

**Ashish Sharma:** Okay so this will not include that carried interest from the…

***Rajiv Lall:*** No. Just to give you a little more color on this, one of the things that has happened is because we are now trying to deal with clients in a seamless way, giving them investment banking services, and debt capital market, equity capital market service through one platform. Our ability to generate ad hoc fees related to transactions has gone up quite significantly.

***Ashish Sharma:*** Okay. Now the second question comes on the SSKI. You have acquired additional 13% stake, taking you close to 79.8. What sort of amount you have paid for the additional stake sir?

***Rajiv Lall:*** Boss that you will see in the year end numbers.

***Ashish Sharma:*** But if you can give me a ballpark figure sir.

***Rajiv Lall:*** Well, a ballpark figure, suffice it to say, is low, and the reason why I say with confidence its low, that you will notice our earnings per share, it has gone up quite significantly, they are now at Rs. 4.74 paise per share, which means that the acquisition in whatever three stages that we made of SSKI, has been accretive.

***Ashish Sharma:*** Okay, now on this Athena Ventures, the question is, you have formed a JV with two other entities. Your share is around close to 28%, what sort of an equity contribution are you looking for this JV sir?

***Rajiv Lall:*** Athena, I would rather not share that with you. That is a confidential piece of information. That piece is buried in that 1,149 crores of equity. There is some amount of that that has been allocated to an investment such as Athena.

***Ashish Sharma:*** Okay, but what sort of your role will be in that JV, what sort of a growth you are seeing from that JV, because in the press release you mentioned that, that you will be probably looking at investments in Power, so what sort of a role IDFC will play in that sir?

***Rajiv Lall:*** See IDFC is a significant share holder in that company. It is basically a development company that is focusing on developing generating capacity around the country. But it is still very early days. We are so far quite pleased with the way that effort is going. As that company takes shape and we get a reasonable pipeline of assets running on the ground and once we see significant value creation there, then we will feel more comfortable talking about it. Right now, we treat it as a start up, a financial investment that we are working on.

***Ashish Sharma:*** Okay sir, thanks a lot sir. All the best.

***Rajiv Lall:*** Thank you.

***Moderator:*** Next question comes from Mr. V. B. S. Reddy of Nirmal Bang.

***V. B. S. Reddy:*** Congratulations for maintaining 0% NPAs. Sir, what is the secret behind maintaining 0% net NPAs even with the rising loan. How do you see NPAs three years down the line?

***Rajiv Lall:*** Well, two comments, one is that, I mean, actually net NPAs is not in itself a good indication on good management, it just shows our ability to provision for all the gross NPAs that we might be incurring. But the important point is that even our gross NPAs are very low and it is a reasonable question to ask that in a balance sheet and loan book that is growing as fast as ours, how do we see the quality of assets going forward? And my answer to that is twofold, one that we always tell investors is that, the nature of risk in the infrastructure space is actually quite different from lending even to a normal industrial corporate and certainly very different from investing to the retail space, for the simple reason that the bulk of our exposure in this space is less sensitive to price cycles globally. We are for the foreseeable future in a situation where infrastructure services are subject to acute shortages and therefore there is no pricing risk as such to the viability of infrastructure projects. What makes infrastructure projects of dubious viability is either, very poor design and structuring in the first place and on that what has happened is that the sophistication of structuring has improved as the sophistication of entrepreneurs has also gone up in this space that is one. Second type of vulnerability comes from, if your projections are too optimistic, so if I am for example in a road project, the take up in traffic may be somewhat lower than what you had anticipated, but that doesn't lead necessarily to an NPA or a write off. What at worst it does, if the situation comes to that, would be a restructuring of the asset. So, you elongate the cash flows if you have to, but given the current macro environment that we are in, where we are seeing 7%, 8% GDP growth, even that is not happening. So, in the current confluence of circumstances, we are able to maintain a very, very clean book.

***Moderator:*** Next question comes from Mr. Ajinkya Dhavale of Motilal Oswal Securities Limited.

***Ajinkya Dhavale:*** Hello, good evening sir, just couple of questions, one, could you just throw more light on the treasury assets because they have been growing very fast and also the NII lying there, how do we see them going forward?

***Rajiv Lall:*** Well, we are still evolving a policy for that is the honest answer. What we have found is that the treasury is actually a very robust business for us. We are working towards a template that will give management some idea systematically of how much capital to allocate to this business. So far it has been looked at primarily as a cash management and proprietary management function and we have opportunistically pursued within a very sort of disciplined and board approved policy framework, trading opportunities in fixed income. Going forward, now that we have had the experience of over 12 months now, I think we feel more confident about systematically allocating capital to a fixed income trading business now. So that will be built out of the next quarter or two and then we will be able to share with you in some greater depth how we are approaching it.

***Ajinkya Dhavale:*** Okay, but predominantly it means that it is a debt capital market activity?

***Rajiv Lall:*** Entirely. There is no equity in it at all.

***Ajinkya Dhavale:*** Okay and second thing, you had talked last time about building a good equity on your own balance sheet by taking also some leveraged equity exposure, how do we see them may be next one or two years in that line?

***Rajiv Lall:*** You have seen that we have gone from 500 crores to a 1,000 crores on that. And I think that 1,000 crores relative to the size of our assets book is still very small. Relative to our net worth is not all that small. So, again I think that we have some broad based idea; again we are setting up an analytical framework for that. Risk management and allocation of capital becomes very key to managing this business. So, we have this framework for allocating economic capital to our various businesses. So we want within our risk appetite to allocate that much as a share of assets and share of net worth to equity positions as would be commensurate with a AAA rating with the rating agencies. So, we have to balance rating agencies perspective, our ability to manage risk and the overall leverage that our balance sheet can take. So, these are the three levers that we have to balance.

***Ajinkya:*** Okay, just extending that question further, now current net worth is 55 billion, how much of that we should allocate for funding business, pure lending business?

***Rajiv Lall:*** You are asking the same question differently and I will sort of try and avoid answering the question differently, which is to say that we have this framework for allocation of economic capital and we have a certain risk appetite, which is higher than it used to be. As we get more comfortable with doing this kind of investing business, we would like to push the envelope, if you like, of how much of this risk we can take without jeopardizing our AAA rating.

***Ajinkya:*** Okay, fine and just one data point, if you could share the overall yield on a rolling 12 month basis that is not there in the presentation?

***Rajiv Lall:*** So, now we have given you the spread now and we have been so transparent giving you this spread.

***Ajinkya:*** Okay, yeah spread is available, I just needed, just to maintain my sheets.

***Rajiv Lall:*** Just to maintain your sheets.

***Ajinkya:*** Has it improved over September?

***Rajiv Lall:*** It's improved.

***Ajinkya:*** Okay fine, thanks.

***Moderator:*** Next question comes from Ms. Sarika of Kotak Securities.

***Sarika:*** Yeah, congratulations sir and my question is moreover related to your asset liability management side. I wanted to know what is the kind of maturity pattern or kind of reset clause you have on your assets and what is the maturity on your borrowing portfolio? I actually wanted to understand that, of the recent numbers when we are talking about softening of interest rate, what kind of management or what kind of arrangement do you see over there to avoid any pressure on your margins?

***L. K. Narayan:*** Like I mentioned earlier, we maintain a positive gap in our asset liability management and just to give you the numbers, the asset duration is 1.97 and the liability duration is 1.43 years. So, we are positively matched as you can see. The reason why the asset duration is like this is simply because of our optionalities that we built into the loan products itself, in terms of put calls or reset windows and that reduces the effective duration of the asset and the liability duration is mirrored as close to the asset duration as we would like it. So, that is really why the liability duration is maintained in close proximity to the asset duration.

***Sarika:*** Okay, would you be able to give as in what is the kind of reset clause you have on your loans as in big tickets infrastructure, core infrastructure lending where the gestation period is high, so what kind of clauses are attached to those loans?

***L. K. Narayan:*** No, I mean, it is never disclosed on a transaction to transaction, but what we have done is that there are large transactions where we have financed it on a door to door basis. Commitments have been made for about 12 years, 15 years, even longer than that, but it is not advisable to think of it on a door to door basis, but you should look at it from these re pricings or reset windows that are inbuilt into it, because when those windows open up, both the client as well as us, we have the right to exit that. So, it is then advisable to look at the durations in a compressed manner.

***Sarika:*** Okay and my second question is about IDFC SSKI, would you be able to share your operating margins or net profit margins for that business?

***Rajiv Lall:*** No.

***Sarika:*** Okay, thanks.

***Moderator:*** Next question comes from Mr. Lalit Srivastav of Techno Shares.

***Lalit Srivastav:*** Two main questions - first of all if you can give me the breakup of your non-interest income for Q2 and Q1 of FY08 and secondly sir, I read somewhere that its increasingly getting more expensive for PE funds to be invested in India, so I was just wondering, what kind of a scenario we are seeing there and if there is, we are carrying some kind of funds for a period without actually investing them, would there be any carrying cost built into that, thank you.

***Rajiv Lall:*** Yeah, so on the second part of your question first, there are no carrying costs. This is not a permanent capital vehicle. These funds are structured on a callable capital basis; you only call on capital when you need it. So, that is how you manage carrying costs. On the other point about, what the key business is doing, valuations are stretched, there is no doubt about that, but what is interesting is that the pipeline or deals that we are seeing still remains very robust and we are still uncovering unlisted investment opportunities that compared to what the market seems to be paying for them are more attractive. That is probably because our deal origination capacities are better in the infrastructure space than most of our competition. That said, as I was telling somebody else a few minutes ago, I don't think we have any illusions that returns from private equity investing will be bid down in this current market environment. So, we have to look at the long term, sustainable returns that you can get from making these kinds of long term investments and our view is that even if the returns come down to a third of what we have seen over the last couple of years, we will still be doing extremely well.

***Lalit Srivastav:*** Okay and sir, about the breakup of that non-interest income, please?

***Vikram Limaye:*** I think that we will do offline, I mean; it should have been on the web site for the previous two quarters. You are asking about Q1 and Q2?

***Lalit Srivastav:*** Yes sir.

***Rajiv Lall:*** If you go to the web site, it should all be there. If it isn't, if you just send an e-mail to Bimal, he will help you with it.

***Lalit Srivastav:*** Right sir and sir, one last question. Sir, there has been some stake increase of SSKI, if I am not wrong, can you share the cost for that?

***Rajiv Lall:*** Yes, there has been an increase in share and no, I cannot share the cost.

***Lalit Srivastav:*** Okay, thank you sir.

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

***Prashanth:*** Just wanted to know two things, one is what is the stake in SSKI at present?

***Rajiv Lall:*** 79.8%.

***Prashanth:*** And second thing is that, I mean your share of short term funds have increased and also your bulk borrowing costs have fallen, so your cost of borrowings on a blended basis for the overall book would have been lower in this quarter vis-à-vis last quarter, would that be a fair assumption?

***L. K. Narayan:*** See, what we do with various maturity profiles is, really we borrow across the maturity spectrum depending on what our Alco requirements are on the liability side, so we sometimes issue short dated or medium dated or long dated depending on what is the counter party and what is the kind of deals that we are seeing. That said, I think as far as the cost numbers are concerned, we do not show you the cost of funds on the aggregate basis, but just we have indicated to you the overall spreads that we have made on the book.

***Prashanth:*** What I was trying to understand is sir that, frankly speaking we were expecting an increase in the spreads if the units were to remain same and somehow that has not happened, that is why this question was there. Units would have increased quarter on quarter or they would have fallen on a sequential basis as you see forward, as the business mix is changing and you are lending lesser to infrastructure and more to industrial and commercial and say cement and steel projects where you compete directly with banks.

***Vikram Limaye:*** As Rajiv mentioned, we are not sharing information on yields, we have given you information on spreads, etc, and he has made the generic comment that yields have improved.

***Prashanth:*** Yields have improved, okay and, I mean, the share of commercial and industrial has increased in the overall pie, is it a conscious decision or, within the infrastructure space there are not so much attractive opportunities compared to…

***Vikram Limaye:*** If you remember we have said all along that energy and transport continue to be very active areas and the share of energy and transport in the overall pie has remained more or less constant at around 37-38%. We also said that, given that telecom is now a more maturing sector, that between telecom and the other areas that we finance, which are largely commercial, industrial and a few other sectors that we have added steel, cement, etc, that the share of non-telecom sectors will go up and telecom will go down and so what you are finding is that commercial and industrial is a fairly large area in which we include things like SEZs, township development, IT parks and all these other things that, given that we were starting from a low base, that the share of that is bound to go up given the level of activity in those areas. So, that is not very different from what we have outlined over the last several quarters.

***Prashanth:*** Okay and not again, I am not asking the exact numbers, but the yields there would be higher than traditional telecom business or…

***Vikram Limaye:*** Its not, I mean, it really depends, because telecom is a more mature sector, but the point is, telecom is a very broad area, right, there are various components of telecom, which would give yields and spreads that are as attractive as commercial, industrial. There are more mature companies in the telecom space that if you finance, will not give you those spreads and yields.

***Prashanth:*** Thank you very much sir.

***Moderator:*** Next question comes from Mr. Kunal Shah of Edelweiss.

***Kunal Shah:*** Sir, on IDFC and SSKI, last time you just mentioned the mix between institutional broking and investment banking, so for the first nine months can we have that breakup as how much would have been contributed from broking and how much would be from investment banking?

***Vikram Limaye:*** No, we are not giving any kind of details about SSKI's P&L, in addition to what we have already provided in our package.

***Kunal Shah:*** Okay and sir, how many member team would that be, would it be possible to share that?

***Vikram Limaye:*** Yeah, it's a fairly large team; it's more than a 100 people.

***Kunal Shah:*** More than 100 people, okay sir, thank you.

***Moderator:*** Next question comes from Mr. Piyush of HSBC.

***Piyush:*** Sir, good evening, just a couple of questions. Like you said that current AUM is 650 million dollars, so can we get a breakup of that, like what is still there in your first PE fund, like suppose the capital has been already returned in that fund?

***Vikram Limaye:*** Yes, the first fund was 200 million dollars.

***Piyush:*** Yes sir, the capital has been returned.

***Vikram Limaye:*** Yes.

***Piyush:*** So, in this 650 million any fund is included from that one?

***Vikram Limaye:*** Sorry.

***Piyush:*** In this 650 million of total AUM as you are having right now, what can be the breakup of this?

***Bimal Giri:*** This is based on the original capital in the various funds, about 200 in the first fund, about 440 in the second fund, the remaining in the public markets fund.

***Piyush:*** And you also have an IDFC PMS, which was somewhere around 100 million dollars?

***Vikram Limaye:*** It is not 100 million dollars; it is more like 50 million dollars.

***Piyush:*** So, is that included in this 650 or it is in the equity investment?

***Vikram Limaye:*** It is not included in the 650, if you were to include that number it will probably be close to 690 million dollars.

***Piyush:*** Okay sir, next is, this principal investment, as the item has been shown in your financials, what is this principal investment, is this the income on your equity book?

***Vikram Limaye:*** No, these are investments that we have made, this is not income, these are investments that we have made in principal opportunities that the platform makes outside of the third party funds that we manage. That's the growth that Rajiv talked about, that has transformed 500 crores to a 1,000 crores.

***Piyush:*** That is your equity book sir.

***Vikram Limaye:*** That's correct.

***Piyush:*** Sir, and one last question, your equity book of 1,150 crore, is this part of your total treasury assets of 4,462 crores?

***Vikram Limaye:*** No, its not.

***Piyush:*** It is separate?

***Vikram Limaye:*** Yes, as we said treasury does not have any equity component, it is all fixed income, principal investments captures the equities that is done of IDFC's balance sheet.

***Piyush:*** Okay sir, thank you very much.

***Moderator:*** Next question comes from Mr. Krishnan of Ambit Capital.

***Krishnan:*** I just needed a few macro trends from you, one was you usually mention something about how your spreads behave depending on how the macro environment interest rate behaves, could I just have that, one. Second is non-interest income, I think there has been a little bit of inconsistency in how I think we have disclosed over the last few quarters, so could we get some clarification there, so if you could answer these two probably I could get to the next two as well?

***Rajiv Lall:*** What was the first question?

***Krishnan:*** Yeah, first question was how your spreads behave depending on how the macro interest rate environment is?

***Rajiv Lall:*** Yeah, so there what we observe is that as rates rise, our spreads tend to improve and thus in the later stages of a rising interest rate cycle and then as interest rates fall, in the early stages of a falling interest rate cycle, our spreads continue to improve, but in the latter stages of a down cycle in interest rates, there could be pressure on our spreads on account of repayments and prepayments and then the whole thing starts all over again.

***Krishnan:*** So, in this case the reset clause is not, I mean, it does not quite come to our rescue, is it?

***Rajiv Lall:*** It depends what the frequency of the reset is, depends on how fast rates are falling.

***Krishnan:*** Okay, fair enough, and second question was on the non-interest income, that is closures that we have made over the last couple of quarters as well as this quarter, it has not been very consistent, sir?

***Rajiv Lall:*** That has to do with the integration of SSKI.

***Krishnan:*** Yeah, fair enough. Yeah, I mean, especially with that, if you mentioned that we have done roughly around 124 crores for the nine months and…

***Rajiv Lall:*** Right, I think the way forward…

***Krishnan:*** Yeah, and we have done about 56 crores for this quarter, so which would mean that we would have done about 75 crores in the first half?

***Rajiv Lall:*** Yeah.

***Krishnan:*** Yeah but, I mean, that is where it doesn’t seem to be consistent, because I think in the first half we probably disclosed that the investment from the SSKI portion was a bit higher, right, I just have a feeling, so which is where the clarification is needed, sir?

***Rajiv Lall:*** Just hang on one second. Yeah, I think short answer to your question is that, some confusion is arising because of our debt capital markets and equity capital markets businesses that were previously accounted for in a separate line item under non-interest income for IDFC.

Now we have, going forward, the bulk of that will appear only under IDFC SSKI, right, and to the extent that there is some legacy of those fees that are still carried, they will appear under advisory and other fees. So, when you look through it all, you should really have four main categories for non-interest income, one is the capital gains line, right, and dividends could be clubbed into that, which are very small, but the bulk is capital gains. Second line is asset management, third line is IDFC SSKI, which will now have DCM - ECM all included in it. The fourth line is what we are calling advisory and other fees, which will be upfront fees, guarantee fees, structuring fees, whatever remnants of the DCM fees remain for the main IDFC platform. The point being that, that line item will be more closely linked from a predictability point of view to our lending business, whereas the fee based income that appears in IDFC SSKI that has a completely different driver.

***Krishnan:*** Yeah, fair enough. Now for the third question that I have, basically what I would like to know is, in terms of your concentration, I mean how the concentration hasn't changed between the first half of the year and the nine months ended, has there been a conscious decision to move away from the power sector, I mean, is that a fair assumption to make?

***Rajiv Lall:*** No, not really, I don't think so. I haven't actually studied this, so I can't give you a systematic answer. In the power sector more and more banks have become more and more comfortable lending and therefore at the margin the spreads are perhaps less interesting than they were six, eight months ago and we found very interesting transactions in the telecom space, which actually have been quite lumpy and profitable, so we have basically pursued those. But, by and large the concentration and importance of power will remain just a reflection of the overall macro opportunities.

***Krishnan:*** Okay and then within this question itself, the transportation segment, I mean, is it possible for you to share how much would roads be making up, I mean, how much would be coming from roads and ports and airports or say for example the trend, basically I am looking for where are you trying to focus more?

***Rajiv Lall:*** As I said, the bulk of it is roads, followed by ports, and then airports.

***Krishnan:*** Okay it would be roads, ports, and then airports?

***Rajiv Lall:*** Yeah.

***Krishnan:*** Okay, fair enough. One last question, this is about the private equity business, the first private equity fund I think we have returned the capital, has there been anything that has happened after the second quarter on that particular fund, have we made any more exits out of that?

***Rajiv Lall:*** There have been some exits, right.

***Krishnan:*** Okay, so which means all those exits would have been booked entirely by IDFC, you would have got your share, right?

***Rajiv Lall:*** Our share, right, yes.

***Krishnan:*** Okay and where would that be reflected?

***Rajiv Lall:*** Capital gains.

***Moderator:*** Next question comes from Mr. Alagappan of Cholamandalam.

***Alagappan:*** See, could we attribute anything to the appreciation of the rupee on the interest expended front?

***L. K. Narayan:*** Really not, if you see our balance sheet, only about 9% of our entire resources is comprised from foreign currency loans, so that is relatively small position that we have and I am not very sure there is any appreciable aspect about foreign currency due to rupee appreciation there.

***Alagappan:*** It is about 10% appreciation in the rupee, so you have about 176 crores, so would that be affecting your spread on a rolling 12 month basis?

***Rajiv Lall:*** Yeah, rupee payment debts have also come down, but I don't think it is a very significant amount though.

***L. K. Narayan:*** It is all fully swapped out, see when we took those foreign currency liabilities; we swapped it back into rupee, so we are not carrying any open forex positions.

***Alagappan:*** I couldn't get you sir, could you come again?

***L. K. Narayan:*** What I am saying is that whatever foreign currency liabilities that we have on balance sheet, we swapped it, the moment we acquired those liabilities we swapped it back into rupees.

***Alagappan:*** And when will this happen like, it happens immediately or…

***L. K. Narayan:*** Yeah, the moment we contact a foreign currency liability, immediately we enter into swap arrangements, so we swap dollars into rupees and we have rupee liabilities and then, that's what it states.

***Alagappan:*** But your payments would be still in rupees or in dollars, like prepayments?

***L. K. Narayan:*** Yeah, sorry, it is paid in rupees then.

***Alagappan:*** Okay, fine, thanks.

***Moderator:*** Next question comes from Mr. Jatinder Agarwal of ABN Amro.

***Jatinder Agarwal:*** Sir, three questions, first, what would be your three year plans for IDFC SSKI venture, how do you plan to take it ahead. Second, more of accounting, in terms of your carry that you get into your asset management business, is that in the form of business income or is it in the form of capital gains, so accordingly the taxability for the same and third is your 8+ percent stake in NSE, any plans on selling that, or how is it going to be structured as you go ahead?

***Rajiv Lall:*** Well, on the accounting or the tax treatment of carry, for now it is treated as capital gains, but we will wait for the budget.

***Jatinder Agarwal:*** All your units would be, your share of your carry would be in the form of share in the capital gains of the investor, is it?

***Rajiv Lall:*** That's right, yeah.

***Jatinder Agarwal:*** Perfect.

***Rajiv Lall:*** Then your second question was long term plans for IDFC SSKI?

***Jatinder Agarwal:*** Yes sir.

***Rajiv Lall:*** You need to wait a quarter for that. We will take you through what we want to do with IDFC SSKI. But broadly what I would say is that, we see it as an integral part of our overall platform and we intend very much to nurture it and grow it, so that the synergies between various parts of the platform become deeper than what we are already discovering them to be.

***Jatinder Agarwal:*** Okay, sir you just gave one data point which is that they have about 100 odd employees in that business, could you give us some more flavor in terms of how many were there about a year back or in terms of the same comparable revenues of 124 crores that you have looked at in your case in the first nine months, how much was it comparable same period last year, so we could get a flavor in terms of how that growth is panning out because we just got one quarter and that's actually almost double of what first half is?

***Rajiv Lall:*** Yeah, I think you need to be patient with us, give us another quarter to give you more perspective on the SSKI business. Again one of the reasons why I am hesitating is that, we have difficulty making like-to-like comparisons in terms of how much of SSKI we owned last year versus how much we own this year, what businesses were previously in IDFC are now with SSKI, all that is causing distortions, so I don't want to give you something that gives you a misleading picture of what is actually happening. The only flavor I would give you is that, there is a lumpy side to their business and then there is a not so lumpy side to their business. The brokerage business is less lumpy, but the investment banking business by definition, you know, it is volatile, so we are having a very good two, three quarters, is that an indication of a secular trend? That we don't know.

***Jatinder Agarwal:*** No problem, sir. Sir, on that NSE stake, because there are some guidelines which require you to…?

***Rajiv Lall:*** Yeah, in NSE stake there are some guidelines, so we will eventually have to lighten up our positions. So we are, probably second quarter, third quarter of this year we will start exploring what we do with that stake and we will try and find something that works both from the point of view of NSE obviously and maximizes the value for us.

***Jatinder Agarwal:*** Right, thank you sir.

***Moderator:*** Next question comes from Mr. Amit of Lotus India Asset Management.

***Amit:*** Just a couple of questions, sir, what could be the maximum amount of leverage that we can have in order to be comfortable with our AAA rating, I mean, currently we are at something like 4.2?

***Rajiv Lall:*** Well, somewhere between 6 and 7.

***L. K. Narayan:*** But, it is not a hard quoted number, it depends on a multitude of other factors, about our risk diversification, the kind of products that we put out as well as the quality of assets, the gross NPAs and the net NPAs, as well as the loan loss reserves that we build up, so it assimilates all of these factors. So it is not just hinged on one number, okay.

***Amit:*** Right, but if everything goes well, then 6 or 7 times is the maximum time that we can leverage, based on the current net worth, right?

***Rajiv Lall:*** No, if everything goes well, then we could go up higher, but we are just giving, you know, the best guess at this time is about 6 to 7.

***Amit:*** Okay, sir one more clarification, sir, under loans and debentures, under this exposure that you have provided, there is something loans against shares, so what is this exactly?

***Rajiv Lall:*** It is basically corporate lending.

***Vikram Limaye:*** Corporate loans for infrastructure investments.

***Amit:*** Corporate loans for infrastructure investments, okay, thanks.

***Moderator:*** There are no further questions. Now I hand over the floor to Mr. Rajiv Lall for closing comments.

***Rajiv Lall:*** Thank you very much for being with us this afternoon, I hope that we have dealt with most of your questions. If you have additional questions, please do not hesitate to contact our investor relations team and we look forward to further interactions in the future.

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

***Note:***
1.This document has been edited to improve readability.
2. Blanks in this transcript represent inaudible or incomprehensible words.