IDFC Limited

Q1FY13 Conference Call
August 16, 2012

Moderator Ladies and gentlemen, good day and welcome to the IDFC Limited's Q1FY13 earnings conference call. As a reminder all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call, please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Bimal Giri of IDFC. Thank you and over to you sir.

Bimal Giri Good morning everyone. I welcome you to this conference call organized to discuss our financial results for Q1FY13. I have with me Rajiv Lall, Vikram Limaye, Sunil Kakar and Sadashiv Rao. Before we begin I would like to state that some of the statements made in today's discussion may be forward looking in nature and may involve risks and uncertainties. Documents relating to our financial performance have been emailed 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 Q1FY13.

Sunil Kakar Thank you Bimal. I will take you through the macro context, numbers, recent developments and then we can start the Q&A. On the macro side there is a visible progress on tariff hikes by SEBs and possibility for potential resolution of the accumulated SEB losses. Better coordination on administrative steps to boost fuel security for generation capacities coming up in the medium term is also visible.

On the transport sector side, a renewed focus on addressing the receivables positions between NHAI and road developers is palpable and on the telecom sector hopefully by the end of this calendar there will be greater clarity on the framework governing the telecom sector.

Now on to our balance sheet. Our balance sheet increased by 25% from ₹ 51,900 odd crores as of June 30, 2011 to ₹ 65,000 crores as of June 30, FY12. Our gross loan book increased by 34% from ₹ 38,000 odd crores to ₹ 50,892 crores as of June 30, 2012. On the liability side, our outstanding borrowings increased by 29% from ₹ 38,670 odd crores to ₹ 50,000 crores as of June 30, 2012.

Gross approvals doubled for the quarter from ₹ 5,800 crores in Q1FY12 to ₹ 11,700 crores in Q1FY13. Gross disbursements also increased by 55% from ₹ 2,900 crores in FY12 to ₹ 4,500 crores in FY13. Energy, transportation and telecommunications continue to be the top three sectors contributing 41%, 24%, and 23% respectively of the total exposure and 43%, 24%, and 22% respectively of our total outstanding disbursement. The share of energy in total exposure has come down progressively from 43% as of June 30, 2011 to 41% as of June 30, 2012.

Now moving on the P&L – on a consolidated basis, our operating income increased by 28% from ₹ 604 crores to ₹ 772 crores. Within that NII increased by 30% from ₹ 483 crores in Q1FY12 to ₹ 629 crores in Q1FY13. This was driven by NII from loans which expanded 30% from ₹ 428 crores in Q1FY12 to ₹ 555 crores in Q1FY13.

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The second component of our operating income that is the non-interest income, increased by 24% from ₹ 110 crores to ₹ 137 crores. Further details are available in the presentation that has been shared with all of you. Our operating expenses increased by 3% from ₹ 114 crores to ₹ 117 crores. Total provisions for various asset classes increased from ₹ 40 crores to ₹ 103 crores, mainly driven by a one-off provision of ₹ 60 crores in our fixed income treasury book. Loan provisions in Q1FY13, were ₹ 39 crores as against ₹ 31 crores in Q1FY12. Profit before tax increased by 23% from ₹ 451 crores to ₹ 553 crores, after providing ₹ 173 crores for taxes and minority interests. Our PAT increased by 21% from ₹ 314 crores to ₹ 380 crores in Q1FY13.

Details on some key ratios on a rolling 12 month basis, we will compare FY12 and the period July '11 to June '12. The return on assets remained stable at 2.9% in both these periods. The overall spread increased from 241 to 252 basis points. NIMs increased from 433 to 437 basis points. The cost to income ratio, declined from 17.5% to 16.7%. ROE has improved from 13% to 13.2% and leverage increased marginally from 5 times to 5.1. Our EPS increased from ₹ 2.04 as of Q1FY12 to ₹ 2.50 in Q1FY13, this is a quarterly number.

Now I will spend some time on the provisions and asset quality. Our existing policies and conservative approach has resulted in our cumulative provision for various asset classes being at around ₹ 1,200 crores as of June 30, 2012. Of this ₹ 900 crores is towards loans and other assets whereas ₹ 300 crores was for investments. Our gross NPAs are at 30 basis points and our net NPAs are at 14 basis points.

Now on to some other developments – Effective July 20, 2012; post all approvals, our name stands changed from Infrastructure Development Finance Company Ltd. to IDFC Ltd. In the first half of 2012, IDFC has been ranked #6 in the Asia Pacific region including Japan and Australia by Thomson Reuters in the league tables for book runners for project loans. IDFC's legal team won the in-house team of the year project finance award at the function organized by the international finance law review on India in July 2012. IDFC won best awards in the learning and development under four separate categories at the world HRD Congress and Asia Pacific forum, wherein 400 companies participated. Also, IDFC was rated amongst the top five companies in learning and development across India. I shall now open this session for Q&A. Thank you.

Moderator Thank you very much sir. Ladies and gentlemen we will now begin the question and answer session. The first question is from Amit Premchandani from UTI Mutual Fund. Please go ahead.

Amit Premchandani You mentioned that some actions have been taken by NHAI on the receivables front, while some of the PSU banks have reported significant NPAs this quarter and one of the key reasons they have said is that State Governments are not paying and that is why lot of construction contractors have receivables just stuck with the State Government. Just wanted to understand your view on that and is that likely to impact your loan book going ahead?

Sadashiv Rao The State Government makes payments for state roads for the contractors who do it on a contract basis, not a BoT basis. So we do not have any exposure to contractors of the States who are building projects for the States.

Rajiv Lall That is factually correct, but on a wider note I would add that you probably are aware that NHAI has a new Chairman now and we had gone to meet him as part of CII delegation a few weeks ago and one of the things he was very clear about is that he wants to try and settle the very large number of disputes that remain unresolved and outstanding. I am told that it is a very large number, about ₹ 60,000 crores of cash is tied up because of these disputes and that is probably what you are referring to.

And as Sadashiv pointed out all these are really to do with EPC contractors. But the expectation in the industry is that over the next 6-8 months there will be some kind of formulaic across the board resolution of the bulk of these disputes. The objective being to avoid case specific and lengthy arbitration. So let see how that pans out at least with the arrival of the new Chairman there seems to be greater focus on this. If that happens by anyway that will be really good for the industry, it would infuse an important amount of cash into the system.

Amit Premchandani Sir another question on the exposure side, this quarter, if you see on the product side the corporate loans have seen a sharp growth and on the concentration side telecom has seen a sharp growth so are we kind of preparing ourselves for the next auction or something of that sort or is it just normal balance sheet kind of funding?

Vikram Limaye There is nothing relating to any other new spectrum related issues, it is more just existing borrowers who we have done business with, some of it relates to the refinancing related exposures as well.

Moderator Thank you. The next question is from Suresh Ganpathy from Macquarie. Please go ahead.

Suresh Ganpathy Just had a question on this ₹ 60 crores provision that you have done on your fixed income portfolio, is it a mark to market provisioning or is it a permanent diminution in value of investment. Just some color on that would be great.

Sunil Kakar Well, as we said it is a one-off and it is not a mark to market. It is a permanent diminution as we expect it to be. So it is not market to market.

Suresh Ganpathy So is it like you invested in a CP of a corporate and that CP got defaulted and therefore you have made a permanent diminution.

Rajiv Lall Yes it is like that.

Moderator Thank you. The next question is from Rajatdeep Anand from ICICI Prudential Life. Please go ahead.

Rajatdeep Anand The first one being on your loan growth. 33% seems a bit high, is this likely to sustain or what is the normalized number that you would be looking at?

Rajiv Lall Normalized number, we have guided the market consistently for the year to a 15-20% asset growth for the year. So you know, just to reiterate the message we make consistently, this is a lumpy business. So, 33% does seem high and it is because first quarter last year the base was relatively low. You don't want this to set the benchmark by expectation annualized for the year, we stick to a 15-20%.

Rajatdeep Anand And you know the incremental exposures have been coming in from energy and telecom, so if you can give us more color as to what exactly these exposures are because both the sectors have their own unique problems whether you know it is lack of coal or sector like telecom is in losses if you put all the companies together. So, if you can help us understand what businesses you are funding there?

Vikram Limaye So there are couple of things that you got to remember. On telecom I have already addressed the point that these are the highest quality borrowers that we have always done business with. On the energy side as we said there are some, we are seeing enough activity in the renewable space as well as in transmission. So the added exposures largely relate to some of these areas not necessarily to thermal power where we have seen issues surrounding coal, gas etc and there also has been an increase in exposure on the transportation side. So it is not just limited to energy and telecom.

Rajatdeep Anand Okay and coming to fee income now, I was doing some trend analysis that there does not seem to be much seasonality, if that is case then even for another quarter fee income seems quite tepid, is that a fair assessment and is it likely to change?

Rajiv Lall There is fee income related to the lending activities and then there is fee income relating to the non balance sheet business which is primarily the investment bank and the asset management business. So the fee income relating to investment bank and asset management, I think the right description would be tepid, but the fee income relating to the loan book and is something that we see growing pretty much in line with the business we are seeing on the loan book itself and this is not necessarily, not just formulaic upfront structuring fee and things like that, these transactions actually require meaningful work to put together and some of these transactions contain quite at least for the way we do business quite path breaking and we have therefore been able to generate interesting value through fees that are appended to our lending book.

Rajatdeep Anand And just one last question, you know if I look at provisions ex of that one-off I get a credit cost of some 35 bps annualized which seems quite low. So I was just trying to understand what is the normalized credit cost that we should expect from IDFC?

Rajiv Lall There is nothing normalized in the present circumstances.

Rajatdeep Anand I understand.

Rajiv Lall The situation is quite dire as you can tell, but what really you should focus on is 2-3 things and you know Sadashiv and Vikram please feel free to add, the first is that our loan loss cover as a share of average assets is 1.7% and that is really quite healthy and total outstanding general provisions are ₹ 1,200 crores. On top of that we are providing against 1200 is total, how much would that be in general?

Sunil Kakar Loans is around ₹ 864 crores.

Rajiv Lall So, close to ₹ 900 crores is provision against lending. The rest is against our investment book receivables etc. So we have a pretty aggressive provisioning policy against standard assets and that provisioning policy just to refresh your memory is actually linked to the internal ratings we give any assets, so the higher the risk profile, the higher the general provision against it and those provisions are higher than certainly what the banks are required to do, by the RBI. I think our sense on provisioning again just to reiterate a message that we have given in the past is that as time unfolds and our book continues to grow you will see some rise in our gross NPA number and you will see some rise in our restructured assets as well. But we remain very confident that the provisions that we have made and continue to make against standard assets are going to be enough to deal to digest if you like, all that has been done over the last 2-3 years and we are confident about that because of the way we have underwritten our assets and we are increasingly confident about that also because of the measures that the government has been taking specifically to address the coal supply issues that affect power projects.

Rajatdeep Anand When you are saying that gross NPA and restructured book would increase, I would like to understand the underlying reasons behind that, is it because your asset books season is over a much longer period of time?

Rajiv Lall Gross NPAs you have to understand that 0.3% of assets in loan book that is ₹ 50,000 crores in an environment such as it is, is nothing short of extraordinary. You have seen a spike in that from a very low base. So, that will rise but will be well within manageable levels and covered through the provisioning that we have made till date.

Moderator Thank you. The next question is from Ajitesh Nair from UBS Securities. Please go ahead.

Ajitesh Nair Two questions, one is on the fixed income investment exposure that we have, do we expect more provisions over the next couple of quarters?

Sunil Kakar You see, as we speak whatever we know we have made provisions for and as the situation is evolving and as and when we get more information on this investment, we will make an appropriate level of provisioning.

Rajiv Lall Short answer is yes, but we don't expect it to be very large amount.

Ajitesh Nair Sir, second question is on the energy exposure tree that you have provided, on the under construction project there is obviously a 2% gas-based exposure which could be tricky. But under the 14% operational exposure do you expect any stress during this year?

Sadashiv Rao Yes, we do have under operational projects, some related to fuel. The gas at KG6 basin, the existing operational power plants the KG6 gas has been reducing and their PLFs have been reducing, so we do expect possibly some amount of restructuring that may be needed.

Rajiv Lall So, just to put that in context, to make it consistent with the energy sector exposure tree that you have, in terms of asset quality in our entire portfolio, our biggest focus is really on gas related projects. The rest we are on a pretty solid footing. It is gas related projects that are subject to conditions that are really beyond our control, that said our expectation is that just as in the case of coal where after 6-7 months of very hard discussions, negotiations, lobbying etc, finally a package of measures is being introduced, that I think will go on a long way towards safe-guarding the assets that are coming on stream and therefore the asset quality of the banks that have exposure to them. We expect a similar kind of evolution on gas, but as and when that develops we will be sure to share that with you on a quarterly basis.

Ajitesh Nair Sir, what is our restructured book outstanding today?

Rajiv Lall It is under 2%.

Moderator Thank you. The next question is from Nilesh Parekh. Please go ahead.

Nilesh Parekh Sir just wanted to check on the tax rate. Now, during the quarter again the tax rate is above 35%, where do we model this for the year?

Sunil Kakar 28 – 29%.

Nilesh Parekh Does this take into account whatever profits we might kind of accrue on the principal investment, because this quarter we didn't have any.

Rajiv Lall That is why it will come down to 28-29% from the current level.

Nilesh Parekh But the exemptions that we had under 36 (1) (viii) so that is trending down as we go along for the pure infra business, because earlier with that exemption that tax rate in the range of about 25-26%.

Rajiv Lall They are historical adjustments. We didn't check that. We will get back to you on that, I don't know the technical answer to that.

Sunil Kakar But overall portfolio level we expect 28 – 29.

Nilesh Parekh And I think on the cost side we have done a good job in terms of curtailing the increase to just about 3%, so do we expect the run rate to be maintained or do you expect some increase as we go along?

Sunil Kakar I think overall cost to income ratio should be around 17%. The growth in cost should be in the range of 5 odd percent, 3% is too narrow

Rajiv Lall 17% cost to income ratio is what if you take as guidance and up to 5% growth in operating expenses maximum for the year.

Nilesh Parekh And so on the earlier question on the 14% of operational assets, you mentioned about the gas part of it, what about the coal side, have we seen PLFs drop?

Rajiv Lall Coal is okay, no problem.

Moderator Thank you. The next question is from Nandita Parker from Karma Capital. Please go ahead.

Nandita Parker Rajiv, on your SEBs and potential for resolution which you started off on a very nice note, what would be your expectation in terms of when do you start getting a little bit more aggressive here on the energy portfolio?

Rajiv Lall Our getting aggressive is really a function of sentiment of clients right?

Nandita Parker Right.

Rajiv Lall The broad point I was trying to make is that from all the noise surrounding the power sector what has emerged is greater clarity and comfort on asset quality, but not enough clarity and comfort that would underwrite meaningful new asset creation at this time. So positive development to the extent that the big fear that people had about asset quality that seems to be receding, but I don't think we have still made enough progress that we can say that people are confident about expanding capacity in the sector just yet.

Nandita Parker And just related to gas. What would be the components in the package as you are concerned, basically we are holding?

Rajiv Lall It will be two fold. One is to sort of solve the outstanding issues with KG basin and there have been atleast on the face of it some positive developments there that they have at least now approved investment plans for CAPEX around the KG basin, that was stuck up in debates. They can at least start doing some CAPEX and hopefully with a little bit of a lag, it will result in some additional flow of gas. From our understanding, on the technical aspects of KG basin is that it requires an investment in fracting type of technology to be able to extract more gas and that is where BP comes in and so at least in principal now that they have an agreement on the CAPEX program, we should see better extraction from the KG basin, so that is one part of the solution. The other part of the solution will have to be access to imported LNG and that will in turn require two things, one is building capacity and expanding capacity to receive LNG and process LNG as it is imported, that is already in process and it will be 18 months before that port handling capacity comes on stream and then there are a whole set of issues related to pricing. LNG is much more expensive then imported coal. So the blended price of gas who will pick up the tab, and how will it be priced etc. So, there are some solutions that are being discussed. They are still I would say I don't know how many months away from some clarity on that, but we still have some way to go before we have clarity on these issues.

Nandita Parker Just to press on that little bit more, since the pricing of KG-D6 gas is fixed till I think about 2014 wouldn't any agreement that the government reaches now be invalid if there is a new government?.

Sadashiv Rao No, in any case the extra LNG is not going to come in a hurry. You know there is a Dabhol terminal which is expected to be commissioned in few months time. We are talking about pooling the gas, imported LNG versus domestic. The domestic gas today is at $4.2 per MMBTU which is the APM gas and that is up for repricing in 2014. So, we don't expect the imported gas to come and the pooling to happen very soon. So, it will be somewhere in the same period around 2013 that we expect the pooling mechanism and a resolution because there is physically a constraint to importing more gas.

Moderator Thank you. The next question is from Anand Vasudevan from Franklin Templeton. Please go ahead.

Anand Vasudevan You mentioned that you renamed the company as IDFC Ltd., just like to understand reason for getting the name changed, what does that reflect about your longer term thinking around the company brand and also the banking license and also does it reflect a desire to move away from the infrastructure financing tag over the long term?

Rajiv Lall First of all, I think you should not read too much into any of this. The one point I will make about is that the thinking behind this is basically the word to keep in mind is optionality. It is common sense given all the challenges that we face in the infrastructure sector, it will be nice to have the option to do other things. Quite apart from that Infrastructure Development Finance Company is quite a mouthful. IDFC it is like what ICICI did or whoever did. Optionality is the key term here. Who knows what is going to happen with the banking license, but if the Banking Regulation Act does get introduced in the parliament and I understand that hopes for that happening are fading, but if it does get introduced in past in the monsoon session of parliament then we would actively consider whether or not we want to actually apply for the license. Let us see whether the act goes through and then should that happen, we will share with you our strategy.

Moderator Thank you. The next question is from Rahul Jain from Goldman Sachs. Please go ahead.

Rahul Jain First of all, is it possible to get a sense on the proportion of refinancing in the current quarters disbursal, refinancing of operating asset that we would have done in this quarter?

Vikram Limaye It is about 40%.

Rahul Jain Okay and second thing is the undisbursed sanction has moved up from something like ₹ 17,000 odd crores, a couple of quarters back to something like ₹ 21,000 crores in this quarter. So again, the broad mix of refinancing and the organic lending that we would be doing out of this ₹ 21,000 crores, is it possible to get some sense from that as well?

Vikram Limaye I think broadly you should assume that about 40% to 50% would come from the pipeline and the balance would come from sanctions that happen during the year, given the fact that while last year and so far this year 30-40% has been refinancing business, historically it has been somewhere in the region of 20-30%. So, refinancing by definition would be sanctions that happen during the year and get disbursed during the year.

Rahul Jain And just wanted to understand given that for the banking system also the pipeline is drying up and there are no new projects that are coming up at least for now, what sort of proposals are coming to us and are banks comfortable letting those loans go off their balance sheet, despite the fact that their loan growth would have also been under pressure couple of quarters on the line?

Vikram Limaye As we have said before, banks themselves depending on which bank you talk about their own infrastructure exposures has been quite high. Second from a rate perspective given that we have managed our liability side quite efficiently by doing more market based borrowings rather than bank loan borrowings, we are able to provide an attractive rate for borrowers. So at some level obviously it doesn't make sense for banks to continue in a certain loan on a risk adjusted basis. So we have been able to take advantage of the fact that we have had pretty good borrowing cost relative to the market and also the fact that increasingly depending on the borrower you talk to, they would rather consolidate their lender community rather than have too many of them. So, it is also a function of who we are refinancing. It could be the case that there is a particular project that has 25 lenders that they want to get down to 6 or 8. So it is not always the case that you are refinancing the largest banks out of any loans. There could be a lot of other smaller lenders to a project that over time from a borrower perspective as well he would prefer to consolidate his banking relationships on that particular asset.

Rahul Jain But I would assume that primary function or primary driver for that would be the interest rate arbitrage. So the moment it sort of runs out or the gap becomes very small, then in that sense that advantage would probably not be available to us in that sense, is it fair to assume?

Vikram Limaye I mean if the cost of funds was the same as bank base rates, then obviously there isn't any incremental spread that we can catch.

Rahul Jain Just final question on fee income from loan related activity. It has pretty much doubled in between this quarter and last quarter if my understanding is correct. So is there any one-off out there and if not then what has been the driver for such a strong income growth in this quarter?

Vikram Limaye As Rajiv pointed out, there have been a couple of transactions that are structured transactions that are relatively complex transactions for which we have been able to get value that goes beyond a normal lending related fee that one would get on a plain vanilla project loan.

Rahul Jain But then the run rate would be same, I mean one has to think about couple of quarters, then the run rate would be pretty much same as what we have see in the last couple of quarters?

Rajiv Lall Maybe a little higher. It will not be benchmarked off this quarter's performance. So, there is one element of one-off in this quarter, but there is also a greater focus on systematically doing transactions that generate more lending related fee income for us.

Moderator Thank you. The next question is from Hiren Dasani from Goldman Sachs Asset Management. Please go ahead.

Hiren Dasani Of the operating assets would it be possible to get any breakup of the 14% in the energy in terms of gas versus coal?

Rajiv Lall We will come back to you. We don't have it on the tree.

Hiren Dasani The second question is on the operating assets now getting lower risk weights, what does your dialogue with the rating agency suggests, do they consider that as part of the leverage calculations or they still go by the overall asset-to-equity or debt-to-equity kind of numbers?

Sunil Kakar They have their own model actually. So, they don't consider what Reserve Bank of India or what regulatory risk weights are there. So, to answer your question, although our capital adequacy has gone up, the rating agency would calculate the risk weights based on their own internal models.

Hiren Dasani So in that case would it be fair to assume that even though the operational assets proportion will increase over a period of time that may not have any influence on the rating agency's thinking?

Sunil Kakar It fairly depends on the quality of the assets etc. So, it is not a simple linear equation but our dialogue does indicate that at least for the next two odd years, we don't need to have any fresh capital injection even from a rating agency perspective, as long as we are growing in the 20% kind of a range.

Hiren Dasani Sure, and lastly on the investment book related provision, I understand that this is a non-infra kind of a CP exposure which has led to the provision. I mean do we have any guidelines on what we can do in terms of the treasury operations, what kind of credit risks which we can take?

Vikram Limaye Yes of course, you would expect that our governance and credit standards all around the platform are relatively high.

Hiren Dasani It is a little surprising that you ended up with this one.

Vikram Limaye It is surprising to everybody.

Rajiv Lall It is a reflection of how creative the Indian market can be.

Vikram Limaye Just so that you know this was the highest rated credit from a liquidity perspective, which drives CP purchases. So it was the highest rating on the liquidity front.

Rajiv Lall Anyway, we are not pleased that this event has occurred notwithstanding our governance standard and what not. So we have taken even more aggressive measure to make our exposure conservative and subject to even greater scrutiny.

Moderator Thank you. The next question is from Amit Ganatra from Religare AMC. Please go ahead.

Amit Ganatra My question was on the employee expenses. The standalone employee expenses have actually gone down by 16% year-on-year and if you do consolidated minus standalone they are up by 13% year-on-year.

Sunil Kakar It is all about a little bit of provisioning. So as I said on a quarter basis it is not exactly right to annualize the same set of numbers.

Amit Ganatra But even your guidance for the full year suggest that overall operating expense you said instead of 3% they can grow at 5% odd?

Sunil Kakar We are taking steps to ensure that cost on the employee side is in line with the income growth in many of the businesses and hence the guidance is based on what we anticipate the overall number going to work out to. So, this quarter-on-quarter business if you are looking at, it is due to some provisioning adjustment which we had to make this quarter.

Rajiv Lall So we will work on that, we still haven't developed that into an art form. But I think we should go by the guidance. We repeat it that overall cost to income we are expecting to keep at 17 and OPEX growth no more than 5.

Amit Ganatra But just for clarification, basically the standalone business is basically the lending business right?

Rajiv Lall You obviously have not been on the previous calls. So what we have done in the past is that we have in the earlier quarters what we try to do is that we have taken provisioning against variable compensation in the standalone account and so that create distortions on a legal entity basis and that is the problem. So, if you look at the total compensation number on a consolidated basis you will get a much better sense of what is happening.

Moderator Thank you. The next question is from Manish Chowdhary from Citigroup. Please go ahead.

Manish Chowdhary My question is basically on the lending side. Now your spreads have been moving up over the last few quarters and is this largely a reflection of the fact that the competition might have basically stepped away or is taking a little bit of a breather here and you are enjoying better spreads and this is also in the context of the fact that you are doing more refinancing so the spreads there could be a little bit narrower. Could you just elaborate on this?

Sunil Kakar See, spreads are a combination of many factors. One to start with is our cost of funds. We have been able through more efficient liability management ensure that our base rates have been competitive as a matter of fact for a 3-year loan; today my base rate is 940-950 compared to the banks and hence through better liability management we have been able to ensure that we get an adequate level of spreads. So, at a portfolio level, the spreads have moved slightly upwards from 240 to 250. But in our guidance we have been maintaining and these are a bit lumpy depending on which kind of asset you financed the spreads do get impacted but at a portfolio level we believe that spreads in the range of 225 to 245 is a reasonable assumption.

Manish Chowdhary And most of the gains in the recent quarters would have been more because of the cost of funding side or the yield side?

Sunil Kakar It is a combination of both, we can’t get it down alone.

Moderator Thank you. The next question is from Kajal Gandhi from ICICI Direct. Please go ahead.

Kajal Gandhi Sir, wanted to know if you can share as you have the total maturity period, if you can share the sectoral maturity like three sectors which you generally share, can we get the maturity in that expected tenure?

Vikram Limaye No, we have for the overall loan book. We don't have it by sector, I am sure we can get it but we don't really look at it from that perspective. Most project loans whether it is Roads, Power tend to be 10-12 year loans with a standard kind of construction, 2-3 year construction period, some moratorium and then repayment schedule. So, telecom is the only one that tends to have a shorter maturity.

Kajal Gandhi Sir that is the only reason I wanted to understand how come then the average total maturity comes down to just 1-1.5 years?

Sunil Kakar No, that is the duration. For here it is, if I may explain. If you want to look at maturity of the loan, the average maturity of a portfolio is 5 years, whereas it is like giving a 5-year loan with an annual reset of interest. Therefore, the duration is one year for the same loan in this example. A five year loan with annual resets will be treated as one year as far as interest rate duration goes.

Kajal Gandhi Sir are we expecting any carry income to be booked in this year?

Rajiv Lall Yes, some.

Kajal Gandhi Anything in the pipeline that we have?

Rajiv Lall Yes, in the pipeline we expect some exits to happen during the course of the year which will lead to associated contribution in the form of carries.

Kajal Gandhi Sir one last thing in the restructured book, do we have any and how is it?

Rajiv Lall Restructured book is under 2%. There is one more important point about the restructured book. In fact, I am glad that you raised it. In fact, I had promised myself to start communicating on this more effectively and clearly. Please understand that the nature of restructuring in the case of infrastructure assets and specifically project loans is quite different from restructuring as it is or may be generally understood in the market. So, a restructuring can technically occur because there is a delay in the project completion date even before the first repayment is ever made from the loan. A restructuring could occur because there are temporary cash flow difficulties in a particular project and a suitable elongation of the period over which the loan is amortized solves those cash flow difficulties. It is not the case that this represents a problem in the fundamental capital structure of the borrowing entity, which raises all kinds of red flags in the form of CDRs, that kind of restructuring. So, the broad point I am making is that restructuring of an infrastructure project asset implies diminution in net present value possibly over the life of that asset. It may not even do that. But it does not and I repeat does not indicate a necessary concomitant increase in expected non-performing assets. So, it is perfectly possible to expect restructured assets to rise but non-performing assets not to rise at all. That is the point I wanted to communicate to all of you and I am sure we will have more opportunities to discuss this in the coming quarter.

Sunil Kakar I just wanted to add that till date we have never taken on an NPV basis a reduction in the value. So we have started using the word to differentiate between restructuring and elongation of repayment of a project finance loan as rescheduling. So maybe rescheduling communicates slightly better. And the point you mentioned was the probability of a rescheduled asset flowing into NPAs is far lower than a restructured asset getting into a NPA.

Rajiv Lall That is a good terminology if you start using it systematically. Hope that helps.

Kajal Gandhi Yes, but are we making any generic provisions in this book?

Rajiv Lall That is just the point.

Sunil Kakar Again, our provisioning policy is that on an average we make about 75-80 basis points on gross disbursement. So while even if the loans are repaid and comes back we are not on a net basis so that policy and then every quarter we test the overall for example in this specific case we are about say ₹ 800-900 crores of provisions we have. So, we go asset by asset and compare and do some internal calculation and see whether the overall provisions are adequate and these are certified by the independent auditors also, not certified, they have also looked at it. So, it is our assumption and based on our calculations, we ensure that this level of provisioning is adequate to take care of all types of risks in the asset book.

Kajal Gandhi And sir one last thing, can you share on the transportation segment which we have, what are the key major segments in that and what will be the amount like?

Vikram Limaye It is about 60%, about 2/3rd of the book will be roads and the balance will probably be equally split between ports and airports.

Kajal Gandhi Sir, in roads the maturity will be on the lower side?

Vikram Limaye No, roads is typically 10-12 years door-to-door.

Rajiv Lall Maturity, again the duration could be shorter.

Moderator The next question is from Devam Modi from Equirius Securities. Please go ahead.

Devam Modi Yes sir, just wanted to clarify the definition of refinancing that you mentioned that refinancing are sanctions that happened during the year and that which get disbursed during the year?

Vikram Limaye Typically if an asset is refinanced it would get sanctioned and disbursed during the year.

Devam Modi Okay sure sir and also wanted to understand that going ahead we could continue to expect something like 40-50% of the asset growth being coming from the refinancing side of the business.

Vikram Limaye Not 50% as I said 30-40%.

Devam Modi In this particular environment would we be seeing a rise in any Greenfield activities in any of the sectors like power or telecom because the growth I think it will be difficult to get high growth from Greenfield activities that is what we assume in the current environment?

Vikram Limaye So there are three areas where we seeing Greenfield activities, there is transmission, there is renewables, and there is roads and hopefully there will be some pickup in ports.

Moderator Thank you. The next question is from Rajesh Kothari from Alpha Accurate Advisors. Please go ahead.

Rajesh Kothari I just have two questions, one is in your current quarter the gross approvals have increased significantly. So, I just wanted to check two things, 1) is there any change in the process by which we evaluate the transaction, for example, other power NBFC companies, they have relaxed some guidelines while doing the sanctions and approvals. 2) How do you see this kind of gross approvals going forward?

Sunil Kakar I think we have answered this question before. Look, there is no change or relaxation at all in our standards. What has happened in this quarter again the growth as a percentage is also a fact of the base effect last year. Overall, as we have indicated our guidances is in the range of 15-20% loan growth on an annual basis.

Rajesh Kothari When you say loan growth means approval growth or whether the disbursement growth?

Sunil Kakar It is on disbursement basis and it was on an outstanding basis.

Rajesh Kothari On an approval basis how do you see that?

Rajiv Lall That is difficult to tell.

Rajesh Kothari What I am trying to understand is that how do you see the trend on approval side, whether the proposal which have been coming whether they are meeting the pace of growth what you are looking for?

Rajiv Lall Approval growth has to, if actual loans outstanding are growing then approval growth also has to grow at least by that amount correct? So the reason why we don't have as much clarity about the growth in approvals; is that the mix of refinanced versus other assets is changing right? So the gap between our exposure and disbursement outstanding is changing. So theoretically, if the share of the refinancing business grows then the gap between exposure and disbursement outstanding will come down. I don't remember the numbers off the top of my head, but my guess would be that if you compare the gap between exposure and disbursements outstanding of the last year, it would be smaller than it was maybe two years ago or three years ago. So that time we were underwriting a lot more Greenfield business than refinancing so exposure would have been larger and the gap would have been larger.

Rajesh Kothari And my second question is basically with reference to the banking license. Given a choice, whether you like to be a bank or whether you like to continue as NBFC?

Rajiv Lall Well that is a tough question and I am not sure that we can answer it in this forum, both have advantages and both have disadvantages. So, getting a bank license has lots of ifs and buts in it because we are already a very large balance sheet and it depends on the circumstances under which we are allowed to acquire a bank license and with respect to various provisions and regulatory obligations of being a bank. So, my advice on that is that as I said we would certainly like to retain the option of acquiring a bank license that is at this point very much beyond our control, because as the RBI has clarified it depends on first and foremost the passing of the Banking Regulatory Act in Parliament. So, if that Act actually does get passed then I promise you we will spend little more time and discuss the pros and cons of such a strategy.

Moderator Ladies and gentlemen we will take one last question from Ronak Agarwal from Standard Chartered. Please go ahead.

Ronak Agarwal Sir out of our total loan book of ₹ 51,000 crore odd, how much would be projects under construction and the projects which are servicing interest from the cash flows, I mean the operational ones.

Vikram Limaye Almost 2/3rd are operating.

Ronak Agarwal Out of this 21,000 crores outstanding approvals, what stage are they as in they have tied up land, material or clearances are done, or is it subject to these conditions?

Vikram Limaye Various approvals, depends on the sector, so there can't be a generic answer to it. So, the point is these are under construction projects. Typically they take 2-3 years for construction depending on what type of asset it is.

Sadashiv Rao No, but we don’t normally disburse unless certain basis things are met. If land is not acquired, disbursement is not done.

Rajiv Lall Also we keep culling the exposure list if we find that there has been no progress on the project every month then we cancel the loan right? So last month we cleaned it up. So is it therefore fair to say that the exposure that is outstanding today is actually on projects that we expect will actually make progress.

Vikram Limaye The other thing to remember is, as was pointed out while we have approvals, there are pre-disbursement conditions, so we approve a loan assuming that certain things fall into place before we actually disburse. So, approval doesn't mean that we will keep disbursing money on the project.

Rajiv Lall But equally the point is that the exposure number is not pie in the sky number because we keep calibrating it for lack of progress on pre-disbursement conditions. So if they don't make progress on pre-disbursement conditions, beyond a certain point we will cancel the loan. So that is why I was asking Sadashiv to clarify that after the last time we looked at this last month. It would not be unfair to assume therefore that the current exposure of ₹ 76,000 crores comprises loans for which we expect the pre-disbursement conditions to be met.

Moderator Ladies and gentlemen that was the last question. I will now hand over the conference to Mr. Sunil Kakar for closing comments.

Sunil Kakar Thank you. I just wanted to clarify one point which was asked during the meeting that something about 36 (1) (viii) (a). We have become a bit more conservative based on what is happening at the tax authorities and we are now providing again specific NPA assets for the tax purposes, which is more conservative from tax perceptive and hence the tax amount is slightly higher, compared to the previous years, so that was the clarification for the person who had asked this question. And if there are any further questions we are more than happy to answer them. Please get in touch with our investor relations department and thank you for your time and patience.

Moderator Thank you very much. On behalf of IDFC Ltd. that concludes this conference call.