IDFC Limited

H1FY15 Earnings Conference Call Transcript
October 31, 2014

Moderator Ladies and gentlemen, good day and welcome to the IDFC Limited H1FY15 earnings conference call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call, please signal an operator by pressing * then 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Bimal Giri of IDFC Limited.

Bimal Giri Good morning everyone. I welcome you to this conference call organized to discuss our financial results for the first half of Fiscal 15. I have with me Vikram Limaye, Sunil Kakar and Pavan Kaushal.

Before we begin, I would like to state that some of the statements made in today's discussion may be forward looking in nature and may involve risks and uncertainties. Documents relating to our financial performance have been e-mailed to all of you. These documents have also been posted on our corporate website. I now invite Sunil to provide key highlight of our performance for the first half of fiscal 15.

Sunil Kakar Thank you Bimal. Thanks for joining us today. I will first share some developments on the macro side and then key highlights related to the first half FY15 financials. I will then invite Vikram to talk about our prospective banking journey and the way forward, post that we will open the floor for Q&A.

Results of the recent State elections augur well for the coordinated center-state dynamics, which should positively impact infrastructure. The diesel deregulation, hike in gas prices and significant procedural reforms in labour impart momentum to the reforms agenda of the Government. Although in his recent monetary policy announcement, the Governor maintained a status quo on policy rates, crude and other commodities are at 4-year low and the rain deficit has essentially been confined to the well irrigated areas. These going forward should help meet inflation comfort levels and provide room for easing of interest rates. The Supreme Court cancelled almost all of the captive coal block allocations. The Government is moving expeditiously to auction the cancelled coal blocks. On the road sector, the award of road projects by NHAI continues to be slow, although NHAI is reworking the model concession agreement to make it more industry friendly. Overall as I have maintained in the past, the revival of private CAPEX in infrastructure will still take some time, but the macro context is definitely turning supportive and steps in the right directions are being taken.

Now moving onto the H1FY15 financials:

Our balance sheet growth year-on-year was around 13%.However, our gross loan book decreased by 2% from Rs.55,957 crore as on September 30th 2013 to Rs.54,851 crore as on September 30th 2014. In the first half 2015, gross approvals were Rs.10,213 crore and gross disbursements were Rs.6,854 crore compared to Rs.15,250 crore for the previous year same period and disbursement of Rs.5,714 crore. On a consolidated basis, our operating income increased by 4% from Rs. 1,911 crore in H1FY14 to Rs.1,988 crore in H1FY15. However, NII decreased marginally by 3% from Rs.1, 371 crore in H1FY14 to Rs.1,331 crore in H1FY15. Non-Interest Income increased by 10% from Rs.531 crore in H1FY14 to Rs.583 crore in H1FY15. This was largely on account of capital gains and better performance of our investment banking and broking revenues. The investment banking and broking revenues almost doubled from Rs.21 crore in H1FY14 to Rs.40 crore in H1FY15. Our loan book related fees increased by 4% from Rs.33 crore to Rs.35 crore.

Headline operating expenses have decreased by 9% from Rs.277 crore to Rs.252 crore. This is largely on account of change in depreciation policy in the first quarter. Adjusted for this, our operating expenses increased to Rs.337 crore in H1FY15. Our PPOP, i.e. the pre-provisioning operating profits, increased by 6% from Rs.1,634 crore in H1FY14 to Rs.1,736 crore in H1FY15. Our provisions for loans and investments were increased more than 4x from Rs.109 crore in H1 FY14 to Rs.485 crore in H1FY15. Within that, provision for loans increased from Rs.105 crore in H1FY14 to Rs.516 crore in H1FY15. Post provisions hence, PBT decreased by 18% from Rs.1,525 crore in H1FY14 to Rs.1,251 crore in H1FY15 and consequently, PAT also decreased by 14% from Rs.1,044 crore in H1FY14 to Rs.903 crore in H1FY15. As on September 30th 2014, our gross NPLs were 62 basis points and our net NPLs were 42 basis points. Our total loan provisions stood at 3.6% of loans. As on September 30th 2014, our net restructured loans were 6.1%, of which 87% relate to energy sector and within that, 31% relate to gas based operations. Our net security receipts which are SRs were at 0.3% of loans.

We continue with our prudent policy of making adequate level of countercyclical provisions, which is reflected in the high level of dynamic provisions in the last few quarters. Although we are seeing a significant level of optimism and improved business confidence, we believe that it would take a few more quarters before we witness any tangible signs of improvement in the sector. We always continue to review our asset quality and would adjust our rate of provisioning as and when we see the improvement in the sector.

On other developments, the 12th India Infrastructure Report which is titled "The Road to Universal Health Coverage" was released by our Executive Chairman, Dr. Lall, in Delhi this September. I now invite Vikram to share his thoughts on our prospective bank journey and the way forward.

Vikram Limaye Good morning everyone. I think as we have said in the previous call with all of you for the last quarter, there are a couple of things that have happened surrounding our transition to becoming a bank. The first thing is about the capital raise that we concluded a month or two.It had to do with bringing down the foreign shareholding in IDFC, which is the promoter of IDFC Bank which by regulation has to be a domestic entity. So we raised Rs.1,000 crore of capital, all from domestic institutional investors through the QIP route and was a very successful offering. As a result of that, our capital adequacy is now up to almost 26%.

The second thing which I would like to highlight is that we have concluded the hiring for all the business heads and shared services heads, etc. For the Bank, we had two senior hires during this quarter. Ravi Shankar who will head our 'Bharat Banking' which is basically banking for the rural landscape as well as inclusion banking. Ravi comes with over three decades of experience in the rural space across Retail Finance and Consulting. He was heading the rural business at Fullerton before he joined us. Sriraman Jagannathan is the second senior hire that we made and he has joined us as Chief Digital and Data Officer. As you know, our focus is to try and make sure that we take advantage of the evolution and technology in order to make sure that the service and experience of our clients from a banking standpoint is very different. Also, it is obvious that digital technology and evolution of all the various channels of delivering banking services is a critical part of making sure that the customer experience is differentiated. Sriram has over 2.5 decades of experience across banking and telecom and prior to joining us, he was the CEO of Airtel Money.

The other significant thing that has happened relating to banking is our Board approval yesterday for the demerger scheme where assets and liabilities from IDFC would be demerged into IDFC Bank as we had said before. This would be a court supervised process that is likely to take anywhere from 6-9 months.The second part that we have highlighted earlier is that the bank would be listed on day one. We still plan to operationalize the bank by October 2015 and we anticipate that the court process as well as all the regulatory approvals that are required to effect this demerger scheme will be in place by then.

The other thing to note is that every shareholder of IDFC for every share in IDFC will get one share of IDFC Bank.This was also approved by the Board yesterday. There was an independent valuation done and an independent fairness opinion provided by merchant bankers to the Board of IDFC and that share exchange ratio has been approved by the Board. The ownership in IDFC Bank as you know will be through a non-operating financial holding company. That non-operating financial holding company will,at the outset when the bank is operationalized, end up owning about 53% of the equity of the bank. The balance 47% will be owned directly by shareholders of IDFC and then overtime obviously based on the regulatory requirements. The shareholding in the bank will have to come down to 40% after three years and will need to remain at 40% for 5 years. So that is broadly what has happened surrounding bank related matters over the last couple of months. We are well on our way to making sure that we are ready to operationalize the bank by October 2015. A lot of detailed work is being done in all the different areas. A lot of hiring has also been planned in respective areas. Now that the heads of businesses and shared services are in place, their respective teams are being built out and detailed business plans from an operational standpoint are being put in place to make sure that we are ready to operationalize the bank come October 2015.

So with that summary, I am sure you all would have lot of questions. I will open it up for Q&A and will take all your questions from here on.

Moderator: Our first question is from the line of Manish Ostwal from KR Choksey Shares & Securities.

Manish Ostwal My question is with respect to the fixed income line. We have seen that this income continues to be disquietingeven though bond market activity has resumed to some extent in the last quarter. So when would we see some pickup in this line and if you could highlight about the things that have happened over there in the last few quarters?

Sunil Kakar The fixed income line or the non-interest income from the fixed income has to be seen in two parts. One part falls under the NII which is the treasury income. The number which you see there, i.e. the fixed income is more on the trading gains and losses which is a healthy Rs.25-26 crore. The fact is, if you compare it to the same period last year, it is obviously lower and that is related to the fact that during a year ago in the first quarter, there was a significant gain because it was a secular reduction in interest rate. So, obviously we have taken risk positions and are making appropriate level gain. So we feel that this is in line. But just to give you some data points, Q2FY14, our fixed income had a loss of Rs. 20 crore. This Q2 we had a slight gain or a flat. Q1FY15, we made Rs. 21 crore out of it. So as I was saying, this is trading income and it cannot be forecasted as where it is moving, but hopefully we will continue to make gains out of it.

Manish Ostwal We have been building this loan provision in order to create buffer since we are moving into the banking platform. We have already reached 3.6%. So is there any internal target we have set which we would like to achieve before moving into banking?

Vikram Limaye I cannot give you a specific number. All I can tell you is that over the next few quarters, we will continue to build provisions. It is dynamic because it is linked to the risks that we see in the landscape that we have been talking about. To the extent that some of those risks get resolved, we will obviously revisit the level of provisioning that is required, but I cannot give you a number because it is dynamic. It keeps changing from quarter-to-quarter depending on what is going on, which specific risks that are known at this point in time whether it is coal-related, gas-related, tariff-related, or anything else. If we see tangible resolution which gives us the handle on how to assess the risk, we will obviously revisit how much we need to build in terms of provisions.

But I can tell you that for the next few quarters till we become a bank, our internal plan is to keep building up provisions. The reason for that is,and we have articulated this for a few quarters now, the idea is to make sure the bank balance sheet is absolutely bullet proof for all known risks that we know today to the extent that they remain unresolved. We do not want to end up in a situation where we have to take large provisionson the first year of becoming a bank. We are absolutely comfortable making sure that we have enough capital set aside for those risks to the extent that those risks do get resolved and we believe that there is some excess provision. As a result of our prudence that we are following at this point in time, we can always write-back some of those provisions to the extent that they are excess provisions. But at this point in time, we would rather be conservative and build those provisions so that the bank balance sheet is absolutely rock solid.

Manish Ostwal My next question is with respect to the restructured assets.Could you give some color of your net restructured loans in terms of your sectoral exposure and the gas related assets.Also, as the Supreme Court has de-allocated mines, what could be its impact to the P&L asset quality from a portfolio perspective?

Sunil Kakar I did mention in my speech that around 87% of the restructured assets come from the energy sector and I will ask Pavan to give his views on coal.

Pavan Kaushal So on the coal block de-allocation which happened recently, we have reviewed this and we do not believe that at this point in time we can actually make any decision till we hear more of what is expected through the coal auction process and the steps being taken thereof. So we are still waiting for some of those to come through and then we would again look at our portfolio, maybe next quarter.

Vikram Limaye So obviously, we do have some exposure to power plants and captive mine.But in order to get a handle on exactly the nature of the risks present there, as you know the Government has already put in motion some steps to handle that situation including re-auctioning of blocks etc. So as I said, as part of our provisioning policy, this is an incremental risk that has cropped up and it once again revalidates what I am saying that we would rather have enough cushions and provisions as we go along. Also these are all general provisions. So these are not asset specific provisions that we have created. So now we have almost 3.6% of our loan book in provisions depending on where we find risk.The risk could go down in certain areas or could go up in certain areas. We want to have enough provisions that we can then allocate to specific situations once we have clarity on some of these risks that we have been talking about for some time.

Moderator Next question is from the line of Umang Shah from CIMB.

Umang Shah Have we restructured any assets in this quarter?

Vikram Limaye Yes we have.

Umang Shah Could you share the quantum and what would be our outstanding restructured loans?

Vikram Limaye Thequantum you should be able to get by just looking at the numbers. Last quarter, we had a certain volume of restructured asset. This quarter, we have disclosed what our restructured assets, so you can do the math.

Umang Shah In terms of principal gains, have we sold any NSE stake this quarter?

Vikram Limaye No.

Moderator Next question is from the line of Amit Ganatra from Religare Invesco Asset Management Company.

Amit Ganatra My question is with respect to some of the trends which are visible in the balance sheet and the P&L. I wanted to know whether these are the kind of trends which wouldcontinue. One trend is that your treasury book is continuously going up. Does this reflect the SLR buildup?

Sunil Kakar Yes. It reflects the SLR buildup.

Amit Ganatra Wheredo we stand right now in terms of overall requirement?

Sunil Kakar The balance sheet does reflect the total treasury book which is around Rs.17, 000 odd crore. So it is there on the balance sheet.

Amit Ganatra But would this entirely be now for the SLR…

Sunil Kakar It isnot entirely SLR. Any G-Secs, T-Bills qualify for SLR. Some of them are trading positions which we are taking because of our interest rate view.

Vikram Limaye We will obviously calibrate how we build our SLR book in the transition to the bank. As you know, from a regulatory perspective we need to be compliant with CRR and SLR requirements on becoming a bank from day one. So we have to obviously transition to that and we will need to keep building our SLR book so that we are at a point where we are compliant on October 1st.

Sunil Kakar I can also say there is a timing issue to it. You can buy the securities technically; you do not want to buy a huge lot towards the end as it is not fair. Also, if you have an interest rate view which we do, we would like to rather invest when the yields are high so that those yields continue to give us higher accruals once we move to the bank.

Amit Ganatra As we are going to be transitioned into a bank, these are some of the key parameters that everybody would be keen to know; i.e. where are we at least at the end of every quarter, what has been the progress made in some of these key parameters?

Vikram Limaye I can tell you do not worry about CRR, SLR. We will have to be compliant day one.

Amit Ganatra No, agreed. That is given, but the thing is that..

Vikram Limaye Thequantum is a regulatory requirement. We know what the regulatory requirement is for a bank in terms of SLR and CRR. That is what we will get to come October 1. The timing of that, I cannot tell you.Depending on what is going on in the market I might decide to slow down or accelerate. It would not be a linear way of getting there. As Sunil said, we might accelerate in a certain period; we might slow down in a certain period. At the end of the day come 30th September, we will be compliant.

Amit Ganatra In the previous quarter your equity book went up from Rs.3,000 odd crore to Rs. 4,000 crore. What does this relate to? Are there any additional investments that you have made in your own funds or something like that?

Vikram Limaye There was certain structured deal that was done in one of our positions and that actually will get monetized in the next couple of months. So it would not continue. It is a temporary thing.

Amit Ganatra My next question is with respect to the HR cost. You had mentioned earlier that the Company did some senior hiring's. Will this trend ideally continue as now you would build those teams? So, would the HR cost keep on building up?

Sunil Kakar Yes.

Amit Ganatra But will there be any branch kind of cost?

Sunil Kakar No, I think not as yet because it is still 11 months away. But it would be present when we would be closer to when we inoperationalize the bank. There will be certain locations where we will open offices that could then transition to bank branches.This could be even in rural areas where we want to try and do certain pilots for how we access the rural markets and how we try and address that opportunity. So in the next 11 months, there will be some offices that we open that could then transition into bank branches.

Amit Ganatra Have you received any clarification from the RBI regarding those infra bonds?

Vikram Limaye Not as yet. We are still awaiting clarification on how the regulations will affect our existing book on the long-term bonds as well as the asset side in terms of the benefit from TSL and CRR/SLR. We have not got clarification as yet.

Moderator Next question is from the line of Manish Shukla from Deutsche Bank.

Manish Shukla My question is with respect to the demerger. Is it fair to assume that if we take the standalone balance sheet, a large part of it excluding the investments in subsidiaries would be spun-off so to say into the bank?

Sunil Kakar Yes.

Manish Shukla So the investments in subsidiaries would then rest with IDFC Limited or with the NOFHC?

Vikram Limaye NOFHC; except for non-financially regulated business. So we have an IDFC Foundation which we will not move to under the NOFHC primarily that. Other than that, we have a small investment in a road asset which is also likely to continue. But as you said, rest of it will all move to the bank and the ownership in the subsidiaries will move to the NOFHC.

Manish Shukla Would that include the prop equity book as well which you have?

Vikram Limaye Yes. All investments, loans, liabilities.

Manish Shukla My next question is with respect to the provisions. Could you broadly break up the provisions which are at 3.6% between general provisions, specific, restructured, and floating? I am assuming you would have something against the restructured assets, something against general provisions, is it right?

Sunil Kakar Restructured assets are regulatory in nature. So we know that 5% of the restructured assets go as a requirement for provision. The specific provisions against our NPLs are only 0.2% from Rs. 117 odd crore. So the rest of it is all floating provisions or dynamic provisions whatever you want to call it. So there are only two specific provisions we have. Actually there is something more on SRs also, it is another Rs.50 crore. So 5% of restructured assets that is for NPL and SR that adds up to the specific provision. The rest all belongs to the floating category and standard asset.

Manish Shukla There has been a decent pickup in both approvals and disbursements quarter-on-quarter. Is there any one-off element there or how do you look at it?

Vikram Limaye First of all, I would encourage you to look at first half versus first half and if you look at that, the approvals are down 33%, disbursements are up 20%. Now as we have said, this is in business as usual in the landscape in terms of infrastructure. We are not seeing any new project activity. We are focused on trying to book low risk assets even in terms of operating assets or to the extent that there are high quality corporate loans, that by definition are lumpy and are not available in abundance.

So I would say that in terms of level of activity, as we have said even at the start of the year, we hope that we will be flat year-on-year from a loan book standpoint. To be flat also requires us to disburse because there are repayments and prepayments and therefore even in the first half of this year, you see an almost Rs. 6,800 crore of disbursements. Despite that, we are flat. So we will have to continue to find opportunities to disburse in order to remain flat. But as I said, our focus is on low risk assets either in infrastructure that are operating assets or high quality borrowers from a corporate standpoint.

Moderator Next question is from the line of Alpesh Mehta from Motilal Oswal.

Alpesh Mehta My question is regarding the banking structure.If we were to get the clarification from RBI about the infra bonds and if it is in our favor, could there be a change in the swap ratio?

Vikram Limaye No, there will not be any change in the swap ratio.

Alpesh Mehta What would be the outstanding Government securities on the balance sheet at present?

Sunil Kakar Yes, these are in two parts. We hold some for a trading book and some for our long book. But the total numbers would be about Rs.7,000-8,000 crore.

Alpesh Mehta This year we are expecting a flat loan book. Could you give any guidance for FY16?

Sunil Kakar It could be more. This is because it includes G-Secs, T-Bills. If we include everything else, then it is still in the range of Rs.8,000 odd crore.

Vikram Limaye Cannot give you any guidance for FY16.

Moderator Next question is from the line of Sameer Dalal from Natverlal & Sons.

Sameer Dalal I missed your restructured assets mentioned before. Could give me that number again?

Vikram Limaye Net restructured loan is 6.1%.

Sameer Dalal 6.1% of your total, okay. Also, you had sold some stake in some of the companies you had in subsidiaries which you are going to generate almost up to Rs.1,000 crore. Has the money for that come in yet or not and when can we expect that to come in?

Vikram Limaye The sale of two of our real estate asset has concluded and the gains from that are actually part of the principal gains lying in the P&L that you see.

Sameer Dalal So how much did you receive net? I think it was Rs. 1,000 crore.

Vikram Limaye No, the gains cannot be Rs. 1,000 crore.

Sameer Dalal Not the gains, the total including principal?

Vikram Limaye Total was around Rs.1,000 crore.

Sameer Dalal Plus you raised Rs.1,000 crore through a QIP?

Vikram Limaye Equity, yes.

Sameer Dalal Given that you have raised Rs.2,000 crore through sale of asset and QIP and if you look at your debt borrowing, they have gone up by another Rs.2,000 odd crore. But your loan book has not really grown as much. I was just trying to figure out where you are deploying these funds at the moment?

Sunil Kakar Treasury assets. So that gives me an opportunity to correct, that number is around Rs.12,000-13,000 crore in the second T-Bill. So our total treasury assets are now Rs.17,000-18,000 crore and they were used to run at Rs.7,000 odd crore sometimes last year.

Sameer Dalal How much high would you be taking this treasury book in the near term?

Sunil Kakar So it is fixed. As we had mentioned earlier, a) there is one part of it which is linked to our potential SLR requirements and the other part is purely on our views of the interest rates. So these things, we can liquidate may be most of these in just 24 hours. So the trading book, it is an interest rate view and has about Rs.7,000-8,000 crore. But once we become a bank like a standard bank, 25% of your liabilities roughly will, if not slightly more will be in SLR/CRR and some part will be in the trading book also. Those numbers will get more fine-tuneas we become closer to the bank.

Moderator The next question is from the line of Shlok Dave from Seraphic.

Shlok Dave I was wondering if you couldnow come out with a small presentation on the banking sector and could comment a bit more on the strategy. You have kind of given an indication by mentioning the people that you have hired. But if you could give a big picture regarding where we are in terms of DNA of the bank and what the DNA of IDFC today is in terms of loan book and what are the changes that we can expect.Do you have to wait for another couple of quarters before that gets like this?

Vikram Limaye I would suggest that we hold off on some of these things till a bit later.

Shlok Dave I wanted to confirm the figure that you had mentioned earlier that your treasury has now Rs.12,000-13,000 crore of government securities. Did I get it right?

Sunil Kakar Yes.

Shlok Dave I know part of it is trading and part of it is HTM. So will the entire amount be classified as SLR if you were to convert to a bank today? I mean is it eligible?

Sunil Kakar Yes, all G-Secs are eligible.

Shlok Dave In that case sir, what is the duration of this book now?

Sunil Kakar The duration is based more on the interest rate view, but maturity of assets could be somewhere around 4-5 years and it keeps moving.

Shlok Dave I wanted to verify whether I got my math right with respect to the NPA side. You had mentioned earlier that the restructured book is 6% and 5% is the provisioning that you need to do for that 30 odd bps. You have made 40 odd bps on your normal gross NPAs so that is roughly 60 to 70 bps. But your total provisions are 3.6%. So is 3.5% to 3.6% over and above these provisioning requirements that you have done?

Sunil Kakar When we use the word total, which is 3.6%, it includes specific provisions, it includes standard asset provisions. Formore details, you can please talk to Bimal. You can break it up but roughly speaking may be 0.5 is more directed and specific and the rest 3 odd percentage would be floating.

Moderator Next question is from the line of Pankaj Agarwal from Ambit Capital.

Pankaj Agarwal The Company's admin expenses have gone up during this quarter. Is there any one-off during the quarter as the increase is quite sharp?

Sunil Kakar If you are comparing it against same period last quarter, there are two aspects to it. One of them is the mandatory CSR activity which has started. I would not use the word mandatory at least morally obligatory, so some of it is there. A large part of it is almost, I would say, Rs.12-13 odd crore come from the banking related activities and then we have certain legal and professional fees for all the principal gains related activity. So there is also a corresponding element of revenue overthere.Similarly in our asset management company, new issue expenses have gone up. But broadly if I were to classify the increase, I do not think this is too much one-off. A large part of it is due to bank related, and the other is related to the CSR related activities.

Pankaj Agarwal Do you expect it to recur over the quarters?

Sunil Kakar This whole business is about expense and cost income. Let me just put some directional numbers so that it also works out for the next few quarters. We are currently at around 15-16% cost-to-income ratio. The best bank in India is running at may be around 40% cost-to-income ratio. So obviously from 15%, somewhere it will stabilize. We want to beat the best. So it is not that we are going to stay at 15%, so cost-to-income ratios from now onwards as you start looking for the next 12 months and as we become a bank, we will continue to increase and trend towards (+30)is the forecast. We would like to beat and do a very good job in managing our cost-to-income ratios. But still the absolute numbers would be in the (+30)range. So hence you will continue to see that creep.

Pankaj Agarwal There is some losses from associates during the quarter. Could you throw some light on this?

Vikram Limaye I think this is not a recurring item. It is something more that has to do with this specific quarter and I think overtime this will actually come back. So this was more surrounding a one-off CAPEX type of expenditure that had to be done but it is not in the nature of recurring losses. This associate is not going to be incurring recurring process.

Pankaj Agarwal The margins of the Company seem to have come down both quarter-on-quarter and year-on-year. So could you throw some light here, whether it is because of decrease in yields?

Sunil Kakar As we mentioned during this conversation that our focus has been high quality assets. If you want to lend to AAA, counterparties, obviously the spreads will come under pressure. So the plus side of the reducing spreads is that our asset quality on the margin that is the incremental loans which we are disbursing is to high quality borrowers and hence the spread compression.

Moderator The next question is from the line of Sanjay Parekh from Reliance Mutual Fund.

Sanjay Parekh With respect to bonds, I wanted some clarification whether it is going to be on the existing book or on the new book. How much part of the bonds having tenureof 7 years we have in either scenario? If it is less, could we get it replaced by those 7-year bonds so that we qualify? Also in either of the clarification what would be a game plan in terms of the leverage that we would take up on a balance sheet in next 2-3 years? On either ways if you can give us some perspective on that side, it would be helpful.

Sunil Kakar Okay. So let us take the first part. We currently hold almost Rs.13,000 odd crore of bonds which are greater than 7 years. How much of that will be eligible for regulatory benefit is the clarification which we are awaiting. Correspondingly, the asset number alsois a function of the clarification. So whether it is adequate or not, that equation cannot be solved till we know what is the clarification on whether what percentage is going. It is obvious that as and when we are going to disburse eligible assets which as you know have to be Infra long term project loans. From here till the next 8-10 months, I do not see the environment changing significantly for us to do hordesof such kind of loans. So corresponding to the asset disbursement, we will ensure that we have adequate liabilities to take benefit of this regulatory incentive which we are getting. So hopefully sooner, rather than later we will get some firm up clarification from Reserve Bank and we will plan appropriately to balance both assets as well as liabilities side. There is not too much of a challenge to raise these liabilities as we speak. But a year or two years down the road, such bonds because of the competitiveness of all other banks also trying to participate in that, it will see how this corporate bond market or the bank bond market develops, we will have to see that. On terms of the leverage as we reach the bank, you must be aware that we are also heading towards Basel-III. The new banks Tier-I as well as total capital requirements are far more stringer. Reserve Bank wants us to keep 13% as against what others are keeping and similarly if we are going to be more dependent upon bank bond market or bond market, then the rating agencies also play a relatively important role. So keeping all that perspective in mind, we will have to see and our objective would be to adequately leveraged, obviously much better leveraged than where we are today. So it is around 15%-odd on the total 15%-16% as we go along. But this is a floating number,it is not exactly a fixed number. So the leverage would be appropriately adjusted whatever 7-8x and going forward it is also a function of as I keep saying what the Basel III norms come out, we are aware of it.

Sanjay Parekh When would you give us a road map about how exactly you want to go on the bank in terms of asset book, liability book? Would it be next year, early next year, or by when we could get a good flavor of that?

Vikram Limaye I think the logical time would be when we are talking about our annual results. So our March 31 results, we will probably be talking to you sometime in May. At that point in time,certainly we will have much better visibility because we will be only a quarter away from operationalizing the bank.

Moderator The next question is from the line of Nishchint Chawathe from Kotak Securities.

Nishchint Chawathe What is the quantum of Infrabonds that you would have already issued?

Sunil Kakar What do you mean by Infrabonds?

Nishchint Chawathe The long term bonds which qualify to be (+7) year.

Sunil Kakar Rs. 13,000 odd crore.

Nishchint Chawathe In your presentation you mentioned that your total exposure to the generation sector is 22%. So how do we reconcile it across renewable, gas, coal etc.?

Vikram Limaye The tree has a lot of details surrounding how much of it is renewable. The tree on the website has a fairly detailed breakdown between construction and operational. Within construction, IPP merchant versus renewable, all that is quite clearly specified and including what the gas exposure is and how much is from captive. There is a lot of information on that tree.

Moderator Next question is from the line of Mudit Painuly from Max Life Insurance.

Mudit Painuly Is 1st of October the earliest date that the bank would be active or is it that if the approvals are received earlier, the bank could start earlier?

Vikram Limaye No, it can obviously go earlier. I would say that you should assume that it is October 1st, not earlier.

Mudit Painuly In case of this coal blocks rebidding, etc., would you be looking to probably lend them again?

Vikram Limaye I do not know because we do not know what the framework is and who is bidding and it is obviously a credit view.So I cannot give you a generic answer to that.

Mudit Painuly Also, we will have to wait a couple of quarters to get more detail on the asset and liability strategies. Is that correct?

Vikram Limaye Asset and liability strategy in terms of what?

Mudit Painuly In terms of the banking overall strategy basically Retail, SME.

Vikram Limaye It will be more in the May-June time frame, a quarter before we operationalize the bank.

Moderator The next question is from the line of Devam Modi from Equirus Securities.

Devam Modi Could you share the percentage of operational and under construction assets in your total portfolio?

Vikram Limaye It is almost 80% operational.

Devam Modi How many megawatts of power generation would have been participated through our total disbursements?

Vikram Limaye Again if you look at the tree, it is at 22.2%.

Devam Modi How many megawatts it is?

Vikram Limaye Why don't you mail us as I do not have it at the top of my head.

Devam Modi My next question is with respect to the kind of CER that we are reporting. CER is obviously a function of your risk-weighted assets. So if we look at the ratio, the percentage has been rising implying that the overall risk has been falling over the last couple of quarters. Does it mean that the incremental provisions required should be lesser, if all these risk analysis should be correct that post the last couple of quarters, at present the incremental provisioning required should be lesser than what was already provided at that juncture? Is that a correct impression because of CER ratio started reversing from then onwards?

Sunil Kakar There are two parts to it. Yes, the ratio always has a numerator and a denominator. So first is the absolute equity, where we have raised Rs. 1,000 crore and that changes your Tier-I capital. That has contributed a significant portion of the increase and similarly although the balance sheet has increased as we have mentioned in the call. The increase in balance sheet is mostly in the areas of G-sec etc. where the risk weight is almost zero. So loan related risk weight is different from balance sheet risk weight. Therefore, if you will notice our loan has not gone up. So the increase in CER can be broken up into higher equity capital injected and the increase in balance sheet in low risk assets primarily because of the increase in treasury which is G-sec which carries zero risk weight.

Moderator The next question is from the line of Rahul Bhangadia from Lucky Securities.

Rahul Bhangadia My question is with respect to the demerger.I wanted to know to what extent has that particular subsidiary IDFC Bank already been capitalized?

Sunil Kakar Right now, it is very thinly capitalized with Rs. 5 lakhs.

Rahul Bhangadia As the demerger goesthrough; the existing shareholders would get about Rs.151.6 crore shares of IDFC Bank which will be like 47% of the final capitalization of that bank.Is that correct?

Sunil Kakar Broadly correct, except it is not Rs.151 crore because after the capital raised, that number is about Rs.159 crore.

Rahul Bhangadia So Rs.159 crore will ultimately become 47% of the bank?

Sunil Kakar That is correct.

Rahul Bhangadia Also, as you shift the assets on to the bank,the corresponding net worth and all will also kind of get shifted to the bank?

Sunil Kakar That is correct.

Rahul Bhangadia Is there any rough number that you have or that will happen as and when ….

Sunil Kakar See, forecasting where the balance sheet will be at the end is a difficult task.

Moderator The next question is from the line of Kajal Gandhi from ICICI Securities.

Kajal Gandhi Initially you had plans of transferring some Infra assets to IDF. So does that still holdor you are transferring the full assets that are there in the book to the bank?

Vikram Limaye So the plan is still to transfer some assets to IDF. So there are two aspects to it. We are in the process of trying to get clarity from RBI on expanding the definition of what the IDF can finance. Right now, the definition is quite constrained and effectively all you can finance right now is operating road assets, the way the definition is structured. We are trying to broaden that definition to try and include all operating Infrastructure assets. If that were to happen, then obviously the opportunity landscape for IDF is much larger and how much or what quantum of assets we transfer from our book to IDF, we will only be able to give you some clarity once we get some clarity from the Reserve Bank on what the definition of IDF is likely to be if there is going to be any change.

Kajal Gandhi In your current outstanding book, how much will be operating assets?

Vikram Limaye About 80% of the total loan book in operating assets.

Kajal Gandhi Would the AMC business will be owned by NOFHC?

Vikram Limaye Yes, all financially regulated businesses. So in our current construct as I said, other than IDFC foundation and another road asset that we owned through IDFC projects, all other entities of the group will be under the NOFHC.

Kajal Gandhi How are you seeing the things shaping up in IDFC securities as the markets have been quite good at present. Are thereany plans of further investments or anything?

Vikram Limaye No, there are no investments required in that business as you know that is an agency business. So it is largely driven by broking revenues and investment banking fees. So there is no investment required. We have certainly seen a pickup in activity and as you know flows into India have been strong, investment banking activity in the first half has been strong primarily surrounding capital raising and therefore our business has also done quite well as Sunil outlined in his opening remarks. The first half results of that business relative to the first half of the previous year, it has doubled. So from that perspective, our hope is that as activity levels pick up in the country that business will do well and get its fair share of banking and broking business that is to be done.

Kajal Gandhi Could you share any number on the profitability because the other income share is the revenue item for the IDFC Sec?

Vikram Limaye No, we cannot share any profitability number at this point in time because that is a function of what happens. It is a volatile business as you know. The first half is not necessarily an indication of how the year would end up.

Kajal Gandhi What would be your market share because it is largely an institutional business?

Vikram Limaye I cannot share some of those details.

Moderator The next question is from the line of Nikhil Bhatt from Barclays.

Nikhil Bhatt My question was around the principal gains and carry in the non-interest income. That seems to have increased both quarter-on-quarter and on a half yearly basis. What is the sustainable outlook for the businesses and whether any of this relates to the share insubsidiaries which you mentioned?

Vikram Limaye A large part of that has to do with the sale of the two real estate assets that we had on our balance sheet which we monetized in the first half. Also with respect to sustainability I would like to state that every year we have demonstrated a certain amount of principal gains that we have been able to book through monetization of investments that we have made whether they are financial investments in this case, real estate assets that we have booked. It has been part of our operating income ever since we went public for the last 10 years.

Moderator The next question is from the line of Manish Shukla from Deutsche Bank.

Manish Shukla The turnaround or improvement in economy over the last few months has been much slower than what most of us would have expected. In that light, how do you see your total stressed asset moving? When I say stressed asset, I mean restructuring plus gross NPL compared to what your assessment would have been say earlier this year, start of the financial year?

Vikram Limaye So I think my view is the following. One is I certainly believe that the environment will improve going forward. I do believe that the Government is focused on finding solutions to problems that we have been talking about. It is probably taking a bit longer than what you would have expected. But given the nature of the problems that we are seeing, I do not think it is unreasonable for the Government to do this in a gradual way. Some of these issues have to do with courts and so that has its own outcome in terms of timeline. But given the size of the problem, I am reasonably confident that a solution would be found, whether it is to the coal issue or the gas issue. Also, there are solutions that are already in the works as it has been discussed.

So from that perspective, do I believe that the large quantum of Infrastructure assets will become nonperforming assets; I hope not. This is because the systemic risks surrounding that is very large not only from a financial perspective but actually if you look at what the Government is focused on whether it is getting manufacturing ramped up or investments ramped up in the country, it is infeasible unless you get Infrastructure development expedited. So you cannot get to 8% GDP growth without Infrastructure. So I think it is therefore essential that the Infrastructure sector not only stabilizes, but actually sees investments in order to make sure that we are able to get back to 8% growth and manufacturing is actually facilitated. So, I do not believe that the end outcome is likely to be thata large part of the assets that you see today as restructured or troubled end up as NPLs. I do not believe that would be the likely outcome. But it is taking much longer than what we would have liked.

So for instance on the gas-based assets, we have been talking about it for some time. Now you have a gas price. You will have a discussion that is ongoing on pooling gas so that at least these plants are able to fire at a certain minimum PLF that hopefully will at least service debt. So there are solutions that are emerging. It had to put a timeline around this. Therefore, how these assets transitioned, I am trying to give you a sense for what I see as the likely in result of this whole process. Now the facts to that end result could see more restructured assets and that is to be expected because the solution has taken longer and therefore you need to give sometime to these assets and wherever regulatorily feasible, there is no harm in doing that because if you believe that ultimately the solution will be such that these assets will be productive assets and regulatorily you are able to provide a restructuring to bridge that gap, then that is the sensible thing to do. So you might see in the interim, the restructured assets going up. If some of these restructurings have already taken place several years ago and because of the delay in the solution, they end up from regulatory perspective in a technical way requiring classification as an NPA. It still does not mean that these assets would need to be written off and that the economic loss from this asset is going to be 100%. This is because once the solution emerges and these assets are able to produce whatever they are supposed to produce in terms of cash flows, then these assets can also be reclassified once they start servicing debt. So I am just saying that in the interim you could see certain things. But do I believe that the end result of this entire landscape is going to be Rs. 200,000 crore of NPAs, I hope not because that as you know has severe ramifications not only to the financial system, but also on future growth and investments in the country.

Moderator Next question is from the line of Mangesh Kulkarni from Almondz Securities.

Mangesh Kulkarni I wanted some clarification on the alternate assets AUM. Is there any increase after the September 30th in this AUM?

Vikram Limaye We have achieved final close of our Infrastructure Fund II and we have closed at Rs.5,500 crore which was the size that we had planned. We had planned for billion dollars, but since we had put the number in rupee terms because at that point in time the rupee was Rs.55. The number that was put for the fund was Rs.5,500 crore, not $1 billion Otherwise, we could have actually raised a slightly higher amount because there were investors who willing to commit more money. But that fund is achieved final closure at Rs.5,500 crore. Other than that, there has been no incremental fund raise in the alternatives business.

Mangesh Kulkarni My next question is with respect to the other income. In the second quarter, we have seen substantial increase in the loan-related fees. So is it something to do with the better business ahead in terms of approvals and disbursements?

Vikram Limaye Again, I would encourage you to look at first half versus first half rather than quarter. So first half of last year loan related fees was Rs.33 crore, first half of this year it is Rs.35 crore. I do not see a major change there.

Moderator The next question is from the line of Krunal Shah from Amideep Investments Consultants.

Krunal Shah My question is with respect to the FII limit. We currently have it at 48%, what is the target that we have in mind for that?

Vikram Limaye There is no target. We have to be below 50% in terms of foreign ownership i.e 49.5% in terms of total foreign ownership. We would not like to go to close to 50% because you do not want to breach that limit and as you know it is very hard to track NRIs and some of these investors. We want to keep some cushion and therefore FII right now I think is at 48%.

Krunal Shah Right, it is 48%. So we plan to take it further or it is fine. Is the cushion sufficient?

Vikram Limaye Yes**.**

Moderator I now hand the conference over to the management for their closing comments.

Sunil Kakar Thank you everybody and we look forward to the next concall.

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