# IDFC Limited
## Q1FY16 Earnings Conference Call
## July 31, 2015

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**Moderator** Ladies and gentlemen, good day and welcome to the IDFC Limited Q1FY16 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 the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. BimalGiri of IDFC Limited.

**BimalGiri:** Good morning everyone. I welcome you to this conference call organized to discuss our financial results for Q1 fiscal 16. I have with me Rajiv Lall, Vikram Limaye, Sunil Kakar and PavanKaushal.

Before we begin, I would like to state that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. Documents relating to our financial performance have been mailed to all of you. These documents have also been posted on our corporate website. I now invite Sunil to provide key highlights of our performance for Q1 fiscal 16.

**Sunil Kakar** Thank you Bimal. Thanks for joining us today. I will first focus on the key highlights related to the first quarter FY16 financials and then I will hand over to Vikram and Rajiv who will spend time on our loan book and the Bank respectively.Post that we will open the floor for Q&A.

Before we get back get into the details, I would just like to just state that the first quarter FY16 financials are not exactly comparable to first quarter FY15 as the Bank related activities were hardly present during the last quarter. Hence, when I explain the variance in the OPEX we need to keep that perspective in mind.

Talking about the macro over the last one year, we observe that the infrastructure sector continues to languish. The power sector has not given the expected outcome either in the Coal or in the Gas sector. We will speak more about it when Vikram addresses the situation. However, the Roads sector is slightly picking up and Telecom continues to do reasonably well.

Coming back to our Balance Sheet, the Balance Sheet growth was 19% year-on-year. However, our gross loan book decreased by 1% from ₹53,848 crore as on June 30, 2014 to ₹53,359 crore as on June 30, 2015, reflecting the macro conditions in the infrastructure sector. In first quarter FY16 both gross approvals and gross disbursements increased by 26% YoY at ₹1,692crore and ₹3,104crore respectively.

On a consolidated basis – our operating income decreased by 20% from ₹887 in Q1FY15 to ₹711 crore this quarter. NII decreased by 8% from ₹682 crore in Q1FY15 to ₹627 crore in Q1FY16,mainly on account of interest reversals on loans that turned non-performing and lower average loan spreads. Non-interest income decreased 40% from ₹134 crore in Q1FY15 to ₹80 crore in Q1FY16, mainly on account of losses on fixed income treasury book.

As far as opex is concerned, we need to remind everybody that last year same period we had a depreciation write-back and hence adjusted for the depreciation reversal the operating expense increased by almost ₹100 crore from ₹140 crore to ₹246 crore. This was mainly on account of Bank related activity. The Bank related expenses increased from only ₹5 crore in the previous year to ₹84 crore in the present year for the quarter. Our pre-provisioning operating profits hence decreased by 44% from ₹832 crore in Q1FY15 to ₹465 crore in Q1FY16.

Our provisions for loans and investments decreased by 69% from ₹204 crore in Q1FY15 to ₹62 crore in Q1FY16. Post provisions profit before tax decreased by 36% from ₹628 crore in Q1FY15 to ₹403 crore in Q1FY16. PAT subsequently decreased by 47% at a headline level from ₹482 crore to ₹251 crore. However, adjusting for the one-time income last year which pertains to income on account of tax refund and lower expenses on account of depreciation reversal, adjusting Q1FY15, the profit after tax actually decreased by 21% from ₹321 crore to ₹254 crore in Q1FY16.

As of June 30, 2015 our gross NPLs were 1.5% and our net NPLs were 1%. Our total loan provisions were 4.9%. As on June 30, 2015 our net restructured assets were 7% of which around 90% relate to the energy sector. Our net SR that is the security receipts were at 0.3% of loans. I now hand over to Vikram for a more detailed discussion on our loan book and asset quality.

**Vikram Limaye** Good morning everyone. I think it is fair to say that the last few quarters since we got our in-principle Bank license have been transitional for us on variety of fronts which not only surrounds our operations and how we are building the Bank et cetera which Rajeev will talk about later but also in terms of calibrating what we do from a business perspective, from a Balance Sheet perspective et cetera.Therefore, we have not been able to really provide a concrete guidance as we would have liked given that this is something that you will appreciate that we have been developing as we were going along in terms of the plan for the Bank and what it implies from a Balance Sheet and cost perspective.

So keeping that background in mind, I just want to talk a little bit more about the asset quality related and provisioning issues and what we plan to do? Given the overall context, we have been saying for some time now that we want to try and protect the Balance Sheet of the Bank from all known risks that exist that we have been talking to you about for the last several quarters, depending on the progress on some of these issues from our Government perspective or from a regulatory perspective.

I want to just begin by saying that from a macro standpoint while we do see potential pockets of growth from the road sector, the power sector in particular coal and gas-based power plants and issues surrounding those plants remain unresolved. There are pockets of activity in the renewable sector as well; particularly in solar where there seems to be a lot of enthusiasm in participating in bids for solar projects. We have been discussing the power situation in the Country with you for the last couple of years. As you are aware approximately 40% of our loan book is in this sector and issues relating to this sector are quite well-known and they relate largely to fuel, tariff issues, PPAs and the state of distribution companies. Unfortunately, as I said, the risks remain unresolved despite efforts of developers, financiers and the Government partly because of the complexity of issues involved. There are several projects where tariff issues remain unresolved and are in various stages of judicial process where there has not been any clarity on tariffs for power plants. The coal mine cancellation by the Supreme Court and subsequent auction by Government resulted in aggressive bids by developers in order to secure the operating mines that they were counting on for their economics. Also, there is uncertainty surrounding how these negative bids would be passed through into tariffs. As we have mentioned even in the last quarter that this has caused enhanced risks for such coal-based projects with couple of developers having already approached the courts for a resolution and it is unclear at this point in time what the outcome of not only those cases but more broadly speaking what would happen to the negative bids. We are aware that the Government since has have already issued an advisory to the regulator stating that they should be capping fixed costs. Which means that these negative bids would not be allowed to be passed through in tariffs in which case obviously the economics of these power plants and the viability of these power plants get compromised.

Likewise we were also awaiting the resolution of stranded gas-based assets.The Government came out with a framework, if I recall in April which then resulted in subsequent bidding by developers for gas which happened only in May.The outcome of that unfortunately is that when you analyze the framework while it is a start, it is far from sufficient to service debt and make these projects economically viable because at this point in time the way the framework has been structured it fires these plants at only about 35% PLF and is based purely on imported LNG. So the viability of these plants will obviously require availability of sufficient gas at reasonable prices and the off-take of power to fire these plants at 70% PLF. The current framework is not sufficient to even service interest and it is being done on a rolling four month basis where developers have to bid for gas with a finite subsidy for only first two years. This is a start as I said but by no means does it give any kind of comfort that it is a permanent solution or a long-term solution for gas-based plants.

The state of the discoms I think has been spoken about for several years and decades and that continues to remain challenging. The state of Discoms has deteriorated, there is not enough power being purchased by Discoms despite the Country being short of power and so that is another level of challenge that generating companies would face where despite being able to generate we are not quite so sure that there is going to be enough off-take of power in the economy.

So now given this backdrop, obviously we have strived very hard and despite our best efforts, as we said before, we cannot be immune to all the risks facing the power and the infrastructure sectors particularly given that IDFC is categorized as an infrastructure finance company and that by definition restricts our ability to diversify the lending book away from infrastructure into other parts of the economy. That obviously has been one of the reasons why we decided to proceed down the Banking path to not only diversify our asset profile but also over time diversify our liability profile, given that right now we are in a framework which is quite restrictive as an infra finance Company.

Also as we told you over the last several quarters, given our transition to a Bank we're focused on making sure how the Bank is protected against all known risks that exist on our Balance Sheet. I want to once again reiterate that the stock of problems has not changed. We have been talking about these problems with you for the last several quarters, surrounding the coal assets and gas assets. So that continues to be the case. There have not been any incremental problems that have cropped up and as I said in the past largely on account of the fact that there are hasn't been any kind of incremental new project development activity and we do have a good understanding of what the stock of problems has been for several quarters now. While we were hopeful that the risks surrounding these assets would reduce before we become a Bank, unfortunately this has not happened based on what I have just outlined earlier in terms of risks surrounding coal and gas assets. As Sunil articulated earlier, the volume of our net restructured assets, NPAs and Security Receipts as of June 30, 2015 was about 8.4% of our loan book. Almost 80% or potentially slightly higher than that relate to the coal and gas based assets that I talked about surrounding fuel issues or tariff issues. Given that we will transition to a Bank by the end of this quarter. So September 30th - October is when we operationalize the Bank and there is no visible solution for these assets.We believe, it is prudent for us to make incremental provisions against known risks. So while our existing loan provisions that we have created so far are more than adequate to take care of the regulatory provision requirements that are required against these assets. Even if these assets were to deteriorate and become NPA, which I can tell you at this point in time obviously many of them are not NPAs but are restructured assets, our existing provisions would be more than adequate to take care of what is required by regulation. However, if we were to build in the risks that I have outlined earlier in terms of the availability of a permanent solution for these assets being visible, that is not the case, which means that it is unclear how these assets would evolve over the next 12-18-24 months. Also, given that there is no clarity of a permanent solution against such assets we believe that it is prudent for us to make incremental provisions of approximately ₹2,500 crore this quarter against such coal and gas-based assets. In order to make sure that in the aggregate we would have provided somewhere between 50 to 60% against our aggregate stressed loan assets many of which as I have said before will not be NPAs as of September 30. So again as I said, this is to make sure that we are providing adequately against known risks the outcome of which is still unknown but we want to make sure that the Bank's Balance Sheet is protected for the risks that we are aware of and that we been talking about some time. Unfortunately, we were hopeful that the solution would emerge before we became a Bank relating to these assets.But there is no permanent solution and there is still uncertainty surrounding these assets as I have said. Now we plan to create these additional provisions by utilizing non-distributable special reserves that we have created over the last several years and this will obviously be subject to appropriate approvals in order to do that. The reason why we are doing that is that because that we have articulated before this is more to take into account our special situation where we are transitioning to a Bank and we want to protect the Bank's Balance Sheet against known risks. The net impact of these additional provisions will be a reduction to our net worth by approximately ₹1,600 crore.

I would like to emphasize one of the points again.We could not have done this earlier because we were expecting a resolution surrounding gas and coal. Both these situations have emerged only in the month of May of this year surrounding the uncertainties, surrounding coal auctions and the pass-through of additional costs as well as the gas framework. Post that situation, we have obviously had discussions with various stakeholders to try and analyze what this means and what the risks are surrounding these assets. We obviously had a conversation with our Board and we have come to the conclusion that given the situation that exists and what we have outlined to you all and to all our stakeholders we would continue to do what we believe is right from a Governance perspective and from a shareholders perspective in making sure that the Bank is bullet-proof against risks that we are aware of.

So our objective in doing this is to provide a clean Balance Sheet and book value for the Bank without an overhang of incremental provisions relating to these assets that I have talked about on future profits of the Bank over the next 4-5 years. This I think is the right thing to do from a Governance and shareholder perspective and will allow people to focus on the growth of the Bank and new business. While we will continue to focus on making sure that we not only resolve these assets but hopefully we are able to claw back some of the provisions that we have made against these assets. It is important to remember that the quantum of provisions that we are making; the Bank Balance Sheet will be completely protected against legacy assets. As I mentioned earlier, the provisions that we are making are done through the Balance Sheet by utilizing the special reserves in the event that some of these assets gets resolved in the future the write back will obviously not be to P&L but will go back to reserves and therefore, will enhance the book value and capitalization of the Bank. Even after making the provisions that I have talked about which are in the order of about ₹ 2,500 crore, the net worth of the Bank will be approximately ₹13,000 to ₹13,500 crore and Tier I capital of approximately 15 to

16%. Therefore, starting out the Bank will be very well capitalized and will have a clean Balance Sheet to make sure that we are ready for new business and that there is no overhang on future profitability.

Again we are sharing all this with you in a very transparent manner as we always do. At the first point in time that we believe it is appropriate for us to do it for the reasons that I have outlined earlier, given that there wasn't clarity surrounding the coal and gas assets till May of this year.

We are obviously more than happy to take any questions you may have surrounding this may be at the end of the call. I will hand it over to Rajiv to talk more about the progress on the Bank front and what the plans for the Bank are.

**Rajiv Lall** Thanks Vikram. Before I get into the Bank I just wanted to reemphasize a couple of things that Vikram has said. They are extremely important. There have been very tough decisions for us and in many ways precipitated by the particular transition that we're going through, which is the transition from IDFC Ltd. into Banking operations. There are three points that really I would very much like you to focus on in Vikram's comments.

The first is that, the overall volume of our stressed assets is not increasing, it is stable, and that number is between ₹ 8,500 to ₹ 8,800 crore. The challenge that we have been facing is that within that overall number of stressed assets what is the likely or almost inevitable migration from currently restructured to eventual NPA and the decision we have had to make is do we take precautionary, prophylactic provisions against that migration today or do we continue doing that on the basis of what is required regulatory. What Vikram has emphasized and I want to re-emphasize is that we on balance choose to start the Bank with a clean Balance Sheet and for that reason we are taking pain the upfront and in one fell swoop. All the additional provisions, ₹ 2,500 crore that Vikram has mentioned are being taken against gas and coal assets, the details of which you're pretty much aware of. They have been on our website and we have been shouting from the rooftops about the problem with these assets for the longest time. The third point I want you to take away is that, this will result in a net reduction in our networth of about ₹1,600crore. And I'm not saying this lightly but I am saying this with a great amount of confidence that we are able to do this because we are extremely well capitalized. Notwithstanding this charge, the Bank will start with the book between ₹13,000 and ₹13,500 crore. Tier-1 capital adequacy of the bank will be over an excess of 15%. We believe collectively that this is a great start for the Bank on a clean slate.

Let me now turn to the plans for the Bank:

Before I get to the strategy for the Bank I want to spend a minute on the process. As you are I hope aware, we have received the final license from the RBI on July 23rd and that was following our completion of all the compliance requirements which the RBI had asked us to complete, the most complex of which was the demerger. The demerger was completed a few weeks before July 23rd, if I recall correctly, the demerger hearing was on June 19th in Madras and we finally got the go-ahead from the honorable High Court of Madras for the demerger on June 19th accordingly the RBI gave us the license on July 23rd. What needs to happen now is that we need to file with the Registrar of Companies and then we need to effect the demerger which is to say transfer all the assets and liabilities from IDFC Ltd. to the Bank. The date the demerger is effective on the date of the launch of the Bank. That date has been fixed as October 1, 2015, I repeat the demerger will take effect on October 1, 2015 and that will be the date of launch of our Banking operations. Once demerger is effective, the next stage of the transformation from structure point of view will happen and that is the allocation of shares from IDFC Ltd. shareholders to IDFC Bank will happen. That process will take about 2 to 3 weeks and we expect that the Bank will be therefore listed and opened for trading no later than the first week of November. So three stages procedurally from now to

November, first is our filing with the Registrar of Companies which should happen very shortly, second is the date of the effectiveness of the demerger and therefore the launch of the Bank which is October 1 and third consequent upon the transfer and allocation of shares from IDFC Ltd. to the Bank is the listing of the Bank itself which will happen in the first week of November. So that is the process.

Let me now turn to the plans for the Bank:

I am on record with respect to the broad plans with regard to the Bank. Let me just refresh your memory about those. We believe that this is an extremely opportune time for IDFC to be launching its Bank operations primarily for two reasons. The first is that the landscape today, the Banking landscape today has been subjected to very rapidly changing the customer behavior. Second is, there has been and continued to be very rapid advances in technology. If you combine those two there is we believe an opportunity for a new Bank to redefine the way in which it connects with customers across the spectrum whether it is corporate customers or retail customers or it is rural customers. We believe that a new age Bank has the possibility to use technology at scale to very significantly bring down cost of operations relative to existing Banks. And we believe that it is possible to use technology to set new and higher standards of customized service delivery in the Banking space. This is really the trend that we want to exploit at IDFC Bank, the operations of which will straddle essentially three lines of business.

The wholesale corporate Bank will capitalize on our starting position and our strengths. We will focus on large corporate, on mid-market and SME clients. We will focus on developing our Government business, our business with financial institutions. We will use our treasury. We will deliver cash management services, transaction Banking as well as investment Banking in the wholesale and corporate Bank. The existing infrastructure business will be a part of our large corporate Banking business. Our existing corporate relationships are strong, many of these corporates also have a significant presence in the non-infra landscape. Using these relationships as an anchor, we will try and penetrate their eco system comprising mid corporates and SMEs as well. Our focus will be on better harvesting and deepening our corporate Banking relationships and first and foremost changing the composition of revenues that we derive from these relationships, i.e. reducing our dependency on term lending and supplementing it with more income from working capital, lending from cash management and transaction Banking, from foreign exchange services and other key based services. Today we are just a one-trick pony. We can very easily and effectively transform the revenue base from our existing clients even as we penetrate non infrastructure corporate spaces. The vibrancy and success of our wholesale Banking franchise in terms of growth, revenue diversification will be critical to the success of IDFC Bank because this is the franchise that will generate the continuing profits, a portion of which we will invest in developing our retail and our rural businesses. This business, the corporate and wholesale Banking is headed as some of you already know, by Ajay Mahajan.

Let me come to Rural Banking or as internally we call it Bharat Banking:

This for me personally is really the most interesting part of the Bank that we are building. The idea is to take Banking services to the community rather than have people come to the Bank. The philosophy is akin really the starting philosophy at any rate, is akin really to a micro finance type of an institution. We will create branches in rural India but the branch will be just a staging post, housing customer relationship offices, and service managers who will be mobile and will deliver services to rural communities at their doorstep using handheld devices. Technology will clearly be a key differentiator in this business. The goal is to use it intelligently, to build a trusted relationship with customers at scale and at lower cost. We believe that this combination of scale and technology has the potential to create a very interesting business model for us. In the medium-term we see the rural Banking business as a stand-alone viable business model contributing to the bulk of our customer aggregation efforts. The rural Bank will be the next after the corporate wholesale Bank to reach our desired level of offering in terms of services, products, channels, and profitability. This business is headed by Ravi Shankar.

Third, the consumer Bank which will start with catering to urban retail. This will be the most challenging of our three large businesses. On account of sophisticated customers already spoilt for choice and account for a very crowded landscape in Tier-1 India with many Banks vying for the same business. The aim in this operation, i.e in consumer Banking is to build a meaningful liabilities base over a long period of time. This could take seven years; it could take even a decade. So this will be a marathon. Again technology will play a very important role in this business. Also, the dependence on branches will be significantly lower in this business than for any existing Bank. So our digital offering in the consumer Bank is going to play a key role. We will stage the launch of products in this business quite deliberately starting with home loans; we will focus on affordable housing which will also give us eligibility for PSL lending. We will take longer to launch other products such as auto loans and credit cards but we will over time build a full service offering for the consumer Bank. This business is headed by Naval Bir Kumar.

So on October 1st,2015 we will start our Banking operations with about 20-25 branches. Of these, 15 of our branches will relate to our Bharat Banking franchise, the rest will be in urban metros. The 15 rural Banking branches will be in Hoshangabad, Khandwa and Harda districts of Madhya Pradesh and as we go forward this balance may not remain as skewed between rural and urban but compared to existing Banks in whatever branch footprint we develop across the country, rural branches will have a disproportionately higher share than our urban branches.

A little bit about governance of the Bank. The Chairman of IDFC Bank will be Mr. Anil Baijal, who some of you may know. He was Home Secretary under the previous NDA Government. He was Secretary for Urban Development, I think, before he retired and he is currently the Chairman of IDFC Foundation. He has joined the Board of IDFC Bank and he will Chair it. I will be the Executive Vice Chairman and MD of the Bank as I step down as Executive Chairman of IDFC. Mr. Vinod Rai who has just joined the Board of IDFC Limited will replace me as Non-Executive Chairman of IDFC Limited when I do step down. Vikram, whom you know well, will remain MD and CEO of IDFC. He and Mr. Vinod Rai will both be on the Board of IDFC Bank as representatives of the largest shareholder. So we are in for some really exciting times. The next quarter, like the last few, is going to be really the beginning or the continuation of a bunch of really hard work. As we continue to navigate managing a difficult Balance Sheet, cleaning it up to start the Bank on a positive footing.

I am sure you will have tons of questions. If not in this conversation, then in subsequent conversations, you can be rest assured that we will engage with you to discuss your questions and whatever clarifications you may have in much more granular detail but it is time now to open up this session for Q&A.

**Moderator** We have first question from the line of Sanjay Parekh from Reliance Mutual Fund.

**Sanjay Parekh** It was mentioned that the total incremental provisioning is ₹ 2,500crore but the adjustment to the book would be ₹1,600 crore. Could you reconcile these figures for me? As I am aware that our discretionary provisions were 3%, so what is the incremental discretionary provision that we would do for this? Would you say that in the next two quarters, the balance of this ₹2,500 (₹1,600) will be provided for? If you can reconcile that it would be helpful. Also does this imply that the whole of the stress that you think is fair has been taken by you and thereforethere would be no further surprises from you? Also,whether they will shift these assets to what you call as a 'bad banking division' separately how do you plan to do that?

**Sunil Kakar** I will help you reconcile the numbers. The incremental ₹2,500 crore of provisions and when you tax adjust it that means the tax shield as you call it, will result in the net worth reduction; so the difference is only the 33-34% of tax. Provisions created will create a deferred tax assets on the other side and hence the impact on net worth is only ₹1,600 crore. So it is basically a tax shield. With respect to your second question, I will ask Vikram to answer it. But we confidently believe all of us that there should be no further surprises.

**VikramLimaye** The provisions that we have made at present are adequate from a regulatory perspective. What we are doing now will result on an average 50-60% of our stressed assets being covered from a provisioning standpoint. That obviously I do not need to explain to you but that we believe is certainly adequate given the nature of assets we are talking about and what it implies from a system perspective that the Government is also going to be hopefully suitably motivated to make sure that the power situation in the Country over time gets better. It is just that we have been hopeful that there will be resolution over the last couple of years and we have waited till May of this year for clarity on couple of these matters which unfortunately hasnot come through in the way we would have liked to give us comfort that there is in fact visibility of a permanent solution. So, therefore, we have gone and made provisions that would actually amount to 50-60% of our stressed assets being covered. We certainly don't believe that we will require more. This is because in the event that these assets do become NPAs over time, we certainly believe that the recoverability against that would be within the provisioning that we are making.

**Rajiv Lall** So what this means is that as a team we are pretty confident that against our stressed asset portfolio there is residual recoverable value of 40-50 paisa on the Rupee. It is with that confidence that we are setting these provisions aside. One of the salutary effects of acting in this way is that we can actually focus on resolution of these assets from the point of view of recovering in a very different way than we might otherwise have to do.This actually unleashes positive energy for most of us to focus our time on building the Bank and a small group of people focused on actually recovering on the legacy assets. I hope that answers your questions.

**VikramLimaye** I want to re-emphasize here that we are going to be working very hard to make sure that the assets that we are talking about see resolution to the extent that we are able to orchestrate that. We are not going to give up on that. You would obviously realize and recognize that we are not sole lenders to these assets. The kind of resolution that we can orchestrate is in the context of other Banks being part of this situation as well. But we will work exceedingly hard to make sure that from a shareholder perspective we are getting everything we can out of these assets.

**Rajiv Lall** Every penny that we can recover we will.

**Moderator** We have the next question from the line of Suresh Ganapathy from Macquarie.

**Suresh Ganapathy** I just need a quick clarification on these provisioning numbers. So the way you have arrived at 50-60% number is that you already have ₹2,500 crore existing provision, which is 4.9% of the loan book. In addition you will have an additional ₹2,500crore, it is ₹5,000 crore, that divided by ₹8,500 to ₹8,800 crore is roughly around 55-60%. Is the math right?

**VikramLimaye** Yes.

**Suresh Ganapathy** Having said that, do you think this is really a pretty conservative stance that you have taken because it becomes very difficult to digest that the recovery value in these gas and coal projects could only be 40-50%? Or is it that because you are converted to a Bank you just want to be as safe as possible and have taken as much as you can and there is a possibility of writing-back some of these provisions. How realistic your assessment is?

**Rajiv Lall** I can say with utmost confidence that based on the track record, the evolution of events so far and based on whatever information that is available on hand, what we have done is fair and honest. So one way to arrive at that judgment is to ask ourselves, look, if I were to ask somebody in my team to say, okay your job is now to recover as much as you can from these assets, put your hand on your heart and tell me how much can you give me back. So when I put him on the line in this manner, he should feel confident and say that I will give you back 40-50%. If I told him, no I want 70% and then he is not confident, he is not raising his hand in doing that. So it is a judgment call. But we believe that's where we come out having debated this granularly internally.

Your point about the Bank is absolutely right. We do not want to start Banking operations, all the time just worrying about having to manage our legacy assets. It is a very negative energy. There is enough work to be done to build the new Bank. There is enough business to be done and therefore we wanted to compartmentalize these two efforts within the wider organization and this is why we have arrived where we have.

**VikramLimaye** If I had to just capture it in a snapshot, if you would, to kind of calibrate what we are saying, there was an earlier question about whether 50-60% is adequate, will there be more to be taken, etc., I would say that the probability of upside is higher than the probability of downside. It means that we hope we will be able to recover something out of the provision that we are making rather than make incremental aggressive provisions against the 2.5k plus existing one that we have against known assets.

**Suresh Ganapathy** From a timing perspective this would come in the October to December quarter i.e the net worth, the reduction adjustment?

**Vikram Limaye** No, in this September 30th Quarter because from October we will be a Bank.

**Moderator** We have the next question from the line of Alpesh Mehta from MotilalOswal Securities.

**Alpesh Mehta** We have already recognized around ₹45 billion as the potential stress so are we going to recognize ₹40 billion more in the second quarter?

**Sunil Kakar** Restructured NPLs as well as security receipts at a gross level is somewhere in the range of 9-10%. By September there will be a shift. The total quantum does not come through in these three categories. The total stressed assets, so the word is 'stressed assets' which may not be actually qualified or classified today as either an NPL or restructured assets. We are looking at stressed assets and so not necessarily it follows the RBI classification. So yes, the total number is around ₹8,000 odd crore.

**Alpesh Mehta** Would it not be prudent to transfer this to an ARC or be separate division considering it will reduce our priority sector CRR and the SLR requirement going forward?

**Rajiv Lall** Yes, if you can set up an adequately capitalized ARC with the requisite skill set to do this, we will sell it to you.

**Alpesh Mehta** How are we placed on the CRR, SLR and the PSL front, considering you have built up aggressive treasury book of late, so are we fully complaint once we will become a Bank on the CRR, SLR front at least?

**Sunil Kakar** Yes, the answer is simple yes. We will be fully compliant with the CRR and SLR requirements. PSL requirements kick in sometime next fiscal and we are on our way to build it up.

**Alpesh Mehta** It looks like you have aggressively built the SLR book of late, so are we also taking into consideration the LCR requirement and because of which that is slightly higher book built up on the G-Secs?

**PavanKaushal** LCR we are well compliant. We are well above the RBI requirement which is 0.6. We are actually 1 for 1 there.

**Sunil Kakar** And some of the book which you see, although we have not segregated it, is also for our trading book. So it's a combination of both SLR and trading book.

**Alpesh Mehta** The CBLO borrowing that we have, are we going to sell off the treasury book or it is going to be replaced by the borrowings, because I think so under Banking structure you are not allowed to carry CBLO.

**Pavan Kaushal** As we transition to the Bank, the SLR book will be unencumbered that is what we require to do.So we will only be having CBLOs covering the other books not the SLR book.

**Alpesh Mehta** While giving the guidance of around ₹80-85 billion of stressed loans are we taking into consideration any 5:25 kind of transaction which are going to take place?

**Vikram Limaye** I mean the point is how these assets evolve is not known at this point, there are various things that are being contemplated. It is all asset specific. So it doesnot mean that because there is a 5:25 that it wouldn't be part of this portfolio. There could be some assets where there maybe a 5:25 but we believe that given the situation, for instance, if there was a 5:25 and there is no coal mine available, that is a problem without the visibility of solution.

**Rajiv Lall** So there will be, I do not know how to clarify this for you but there is a difference in nomenclature between what we are using and what perhaps you are used to. The ₹8,500-8,800 crore that we have shared with you is really our honest, as best as we can do assessment of what we believe is stressed. It does not matter whether it is classified as an NPA, whether it is technically restructured or it is a 5:25. Just because an asset is 5:25 does not mean that it is non-stressed. So we have laid it out there for you all to see, this is the number that we believe in our Balance Sheet is stressed, no matter what its nomenclature, against that we are providing proactively 50-60%.

**Alpesh Mehta** Out of the total net worth that we have of around ₹175 billion, you had mentioned that around ₹135 billion will go to Bank. Could you give the breakup of the rest ₹40 billion. How much you are going to keep it with the parent Company and what would be the requirement for the subsidiaries?

**Sunil Kakar** So first I just need to correct that the total net worth of ₹175 billion is at a consolidated level. What is getting split is only IDFC Limited where the number is lower. So if 13,500 roughly is going to the Bank, the rest is amongst the other subsidiaries and there are various financial holding companies and on top of it is IDFC Limited, a detailed breakup of all the subsidiaries and their capitalization will be available.But broadly speaking it is 13,500 and once we finalize this at the end of the September quarter and everything gets finalized, we will put it up on our website also.

**Alpesh Mehta** Rajiv you mentioned on the call regarding the technology being the key differentiator on the corporate segment as well. Could you throw some examples related to that because on the consumer side we are used to see the technology being one of the key differentiators, how it will help on the corporate banking side?

**Rajiv Lall** That's a more granular conversation. But actually the big differentiator is the architectural design of our technology platform. So our ability to treat customers in a seamless manner between let's say, trade, FX, and other product and services for which they connect with the Bank. In existing technology platforms it is not very sophisticated. It is actually fragmented because they are using a number of systems that connect to the core Banking system in not a very streamlined manner. So because we are creating a platform from scratch we are able to design it with much greater flexibility such that the customer, whoever they might be, when they interface with the Bank have a much more seamless and simpler experience. So you will have to experience it, I cannot explain it in a very simple form but in one-on-one investor meetings we will have an opportunity to share this in much greater detail.

**Moderator** We have the next question from the line of Amit Premchandanifrom UTI Mutual Fund.

**Amit Premchandani** What percentage of the assets will be covered by infra bonds? Have you made any estimate on that?

**Sunil Kakar** Initially just to answer your question that only 30% of whatever eligible assets are there is allowed for this fiscal. So in numerical terms about ₹35,000 to ₹36,000 crore roughly we are still getting those numbers collated, will be eligible 30% of that will be what infra bonds will fund because that is what you are allowed and we are almost there. Anticipating your next question, that we have almost raised all of it, only 1000 or 2000 is left.

**Amit Premchandani** So is it safe to conclude that you are kind of overinvested in CRR, SLR securities as of now and there is no dilution on margins likely to come on day one from that?

**Sunil Kakar** Yes. We are overinvested in our SLR securities. But as I said, it is a combination of both HTM which is the SLR securities, our trading book and a rate view, etc. So there should be no dilution in NII from that perspective, except I do want to add here, it will be on account of CRR. Currently, our cash is maintained in 8% yield in mutual funds that will go down to zero percent.

**Amit Premchandani** In terms of loan book you had earlier mentioned that some of the loan may be transferred to IDF. Any clarity on how much would be transferred or could we have guidance on that?

**Rajiv Lall** Say, around ₹ 1,200 crore.

**Amit Premchandani** Almost the entire book is moving to the Bank?

**Rajiv Lall** Yes.

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

**Abhishek Murarka** My first question is with respect to your branches. You shared that you will start with 20- 25 branches. What would be the outlook for, let us say, FY16 and FY17? You mentioned that you spent about ₹85 crorein the present quarter on Bank related expenses. So what would a recurring kind of number be for the next couple of years, including technology, branches, all of that?

**Rajiv Lall** We get this question most frequently that how many branches we will have and it is bit of an awkward question. This is because our goal is really to minimize the number of branches that we want to actually open. So I guess, the honest answer to your question is that we will calibrate, we will see what is the minimum number of branches that we can get away with. But not to evade your question, October 1, 2015 would have 20 to 25 branches, by March 31st 2016 we expect to have about 60 branches, of which 45 will be in rural India and the remaining 15 odd will be in

Tier-1 India. So that is our starting footprint and then we will evaluate how our strategy is working and accordingly calibrate the further expansion of our branch.

When we list the Bank, we will go into those details with respect to expenses and all of that. I will give you this one nugget; which is we expect that our trough ROA, our trough ROAs would be about 1% and that will happen early on in our journey. And thereafter, we will deliver systematically higher ROAs until we reach, shall we say, the top quartile of ROAs in the industry.

**Abhishek Murarka** Your point on ROA is well taken. I was looking for some kind of budgeting you would have done. Since you are going to be so intensively dependent on technology plus calibrated branch additions, you might have budgeted something for the year or next couple of years so, that is what I was actually alluding to.

**Rajiv Lall** No, we have budgeted obviously. I am reluctant at this point to give forward guidance. So if you would just be little more patient, before we launch the Bank when we would do road shows and all that, at that point after a little more reflection we will have share with you in some detail. So right now, just stay with the broad picture on the ROA. On that, we will come back to you. Give us a little time to settle down.

**Abhishek Murarka** What would be your outstanding SRs currently, gross?

**Sunil Kakar** ₹ 221 odd crore, gross.

**Abhishek Murarka** My next question is with respect to your exposure that you have given. Basically your linkage gas has actually come down sequentially from about ₹ 2,600 crore to ₹1,500 crore. Are the numbers correct or has there been a selldown in the quarter?

**Vikram Limaye** No, there is no selldown in the quarter. There has been no change and the gas assets are what they are. The only thing is that some of them have been categorized as operational. Categorized as operational as opposed to actually operating and generating sufficient PLF is something I have addressed before.

**Abhishek Murarka** So just post the pooling thing basically it has been reclassified?

**Vikram Limaye** Yes.

**Moderator** We have the next question from the line of Aditya Narain from Citi.

**Aditya Narain** I basically have two questions. My first question was in terms of the Bank. Could you give us over the medium term a 3-5 year perspective, some sense of the kind of economic trajectory that you intend following? And by that, I basically mean the growth versus return versus margin kind of tradeoff, including the kind of fee income that you are looking at generating in terms of a broad band.My second question is really in terms of the treasury side of the business. Could you give some sense of how much of it will be managing the book and how much of it will really be kind of a revenue center, which has been the case for a lot of Banks when they have actually built themselves out?

**Rajiv Lall** You will have to bear with us for another quarter before we are ready to engage in that level of granularity on the Bank. What I can tell you is that, I go back to my ROA point, so 1% going to top quartile within five years, that really is what we are working withand that will translate into certain ROEs, the trajectory of which is a little uncertain, only because there will be points in that fiveyear journey that we will raise capital. So, that is harder to give you a trajectory on than the ROA. In any case, the ROA tells you more about the nature of the business than about the capital structure. I know it is not answering your question right away, but I would request you to just indulge us for another quarter and be satisfied with this ROA indication for now.

**Aditya Narain** On the treasury side, how much of a liquidity manager will that be and how much of a revenue center could that potentially be?

**Rajiv Lall** I think it is a no brainer that we have a very large treasury, it will remain a very large treasury, and we expect that for early stage startup Bank like this, the treasury will play an important role in contribution to our revenues. So we are building a fairly comprehensive financial institutions business. We are focused on building and capitalizing on our Government relationships. We are going to be looking at every avenue for raising liabilities from the financial sector and our trading book will also be quite large. So it is a very significant treasury and that is one of the reasons why Ajay Mahajan is in charge of it.

**Sunil Kakar** There will obviously be client business that we do on FX and all the other fronts. So it will be not dissimilar to treasury that you see in other private sector Banks.

**Rajiv Lall** It will be larger actually, larger than most private sector Banks, yes.

**Aditya Narain** In terms of a bad-bank, any thoughts on creating one from a market perspective, i.e., for us to follow where you put it together and you keep giving us updates in terms of how that business is or how that pool is working. Also, a couple other Banks have done it reasonably successfully.

**Rajiv Lall** We would like nothing better than to do it that way. So we will figure out how to give you transparency and ability to track progress vis-a-vis bad. I mean you have to understand that for us, to put it plainly, quite a wrenching experience. This is not an easy decision for any management team to make. We have been able to make the decision in part because we happen to be in this situation of moving to the Bank. We have been determined to clean up and focus on recovery. We operate in a cultural context and in the wider system in which it is very hard to do this kind of stuff. So, we have taken one very big step today and we will find some way of helping you track progress on what we have announced today.

**Vikram Limaye** So as we said before, as we work on these assets, depending on the resolution of these assets, obviously we will be transparent to the extent that if there is any kind of write-back of provision that needs to happen, particularly the one that we are creating out of these special reserves, it will go back into the balance sheet and that will obviously be transparently available. So from that standpoint, as things change we will be able to update you on how things are progressing.

**Moderator** We have the next question from the line of Abhishek Murarkafrom IIFL.

**Abhishek Murarka** I just need a quick clarification on net worth. So basically, ₹13,500 crore will get transferred to the Bank, the remaining 4 billion will take a knock of 1,600 for the provisions, net of tax, and whatever remains will effectively be available to other subsidiaries and the parent entity. Is that correct?

**Rajiv Lall** Yes 13,000 odd number is after reducing the total. Yes, so you can work the other way around; the total minus 1,600 and then 13,500 goes down there and the rest goes to the subsidiaries.

**Moderator** We have the next question from the line of Gaurav Jani from JHP Securities.

**Gaurav Jani** I just want to have an idea of the advances mix in terms of a number. Can you just share as to how much would be your corporate, rural, MSME and urban retail?

**Rajiv Lall** Our starting loan book will be in the region of ₹48,000crore to ₹50,000 crore, all of this is basically large corporates. Most of it is basically infrastructure. So in MSME and rural Banking, the ticket sizes, even in retail, the ticket sizes are much smaller. So while the focus of our incremental asset growth will be in these lines of business, it will take some time before the weight of the corporate book begins to dilute appreciably. But I think broadly, what we should expect is that whatever incremental growth we deliver in the overall loan book will be for the time being in non-infra sectors.

**Gaurav Jani** So, ₹13,500 crore is post the charge, so how much would that lead to a Tier-1 capital, please?

**Sunil Kakar** Tier-1 capital adequacy we expect to be north of 15%.

**Gaurav Jani** That is after considering this figure of 13,500 crore?

**VikramLimaye** That is correct.

**Moderator** We have the next question from the line of Amit Ganatra from Religare Invesco.

**Amit Ganatra** My question is with respect to the stressed assets. So basically there is around ₹4,000 to ₹4,500 crore. Is that the standard assets in the system right now, in the Banking system?

**Vikram Limaye** This is not something that we can opine on. The reality is that the classification of assets in the system varies depending on Bank and how they have been taken care of or not, etc. So it is, as you know, it is not the case that an asset that is classified as NPA by one Bank is necessarily an NPA in the entire system. So it is very hard for us to extrapolate whether everything that we are classifying in a certain way is similar to how other Banks are classifying.

**Amit Ganatra** Now, as you have basically assessed this ₹4,500crore, what will be the total system loans to these corporates combined?

**Sunil Kakar** It is very hard for us again to extrapolate that. But as I said, since the 80% plus of what we are talking about is related to the power sector, there are various other external agencies and rating agencies who have been talking about the size of the power sector problem. And it is very hard for us to give you a number because we donot have data surrounding the other Banks and financial institutions. But again, as I said, I mean these are not loans where we are sole lenders, so these are consortiums.

**Moderator** We have the next question from the line of Seshadri Sen from JP Morgan.

**Seshadri Sen** Doing the math, if you are saying ₹13,500 crore of capital and 16% of capital adequacy that is like ₹80,000 odd crore of risk-weighted assets against ₹50,000 crore of loan. So, am I doing the math wrong or is that just the risk weighting on/ off-balance sheet? How does that pan out?

**Sunil Kakar** It is a combination it is not wrong. The ₹13,500crore is the networth. Tier-1 capital would be lower. Correspondingly then there is this aspect of risk-weighted assets of off-balance sheet items. Therefore, if you do the math, then the number comes to (+15%). I think the big difference would be that ₹13,500crore is not all Tier-1 capital.

**Rajiv Lall** Our starting loan book will be around 50,000 crore, whereas starting balance sheet will be about 80,000 crore, but risk-weights there are very less.

**Seshadri Sen** Yes, if your net worth is ₹13,500crore, asyou donot have subsidiaries or anything, so what would be the deductions from Tier-1?

**Rajiv Lall** Deferred tax asset.

**Seshadri Sen** Say during the first 6 to 12 months, you will be funding yourself I presume mainly through wholesale deposits it will take a while for CASA to pick-up and if you are doing working capital lending on the other side, which is low yield, are we looking at fairly significant margin dilution and even PSL which you have to add would probably be a little low yield, so are we looking at fairly significant margin dilution for the first 6 to 12 months before some level of CASA starts to pick up?

**VikramLimaye** In the near term till we build CASA, obviously we are going to be wholesale funded. That is reflected in what Rajiv outlined in terms of the RoA number. So the margin compression, etc., is all reflected in the 1% RoA number that Rajiv talked about.

**Moderator** We have the next question from the line of Siddhesh Vora from Incedo Group.

**SiddheshVora** When you do the calculation of about ₹8,500 crore to ₹8,800 crore of stressed asset which you mentioned and you said 40% to 50% will be recoverable, that amount comes to ₹3,400.So remaining is around ₹5,000crore of assets where you will provide provision. But you mentioned that you will be providing provision of ₹2,500crore. So am I missing something in this math?

**Vikram Limaye** We already have 2,000 plus crore of provisions, which I said is more than adequate from a regulatory perspective. We are talking about incremental ₹2,500 crore, not the total.

**Moderator** We have the next question from the line of Kaushal Patel from India Nivesh Securities.

**Kaushal Patel** Myquestion is related to net worth. As you mentioned that net worth of ₹ 13.5 billion will be transferred towards Bank. I need some small clarification. Under the scheme of arrangement that you have filed with BSE, you have mentioned that residual net worth of residual undertaking will be approximately ₹10,154 crore and for the Bank it will be ₹13,825 crore. So how do we see?

**Sunil Kakar** Yes, I will help you explain that. Now obviously that equivalent of ₹13,800 crore is now as time passes, we are talking of about ₹13,500 crore or so. When you calculate the total net worth of IDFC Limited, you have to take 53% of the Bank's net worth and add it back. So if you do the math, you will end up around ₹10,000 crore and if you need some more help, you may please get in touch with our Investor Relations and we will give you the math. But I suggest if you take the 53% of Bank and add back the subs, you will get the answer.

**Moderator** We have the next question from the line of Nilesh Parikh from Edelweiss Securities.

**Nilesh Parikh** My questionis regarding the landscape. We have recognized large part of the stress and would be making those provisions. But when we look across the system, I think that recognition has still not happened. So I just wanted hear your thoughts in terms of when does that happen and is that important for the next investment cycle to revive, because that aspect is going to be critical for us on the growth side? So I just wanted to hear your thoughts on that.

**Rajiv Lall** I think you are right. What I cannot give you clarity on is exactly how this thing will pan out and how it will resolve itself. Right now, there is a growing recognition in the marketplace and a growing recognition in media that there is a problem in the Banking system. Now what behavioral changes that induces, what regulatory interventions that triggers, is difficult to say. But until the Balance Sheet overhang is addressed, my personal view is that it will come in the way of full recovery. The Banking system will be unable to support the credit growth that is required for reviving the investment cycle.

**Moderator** We have the next question from the line of Kajal Gandhi from ICICI Direct.

**Kajal Gandhi** I wanted to know about your dividend policy, how you see that now?

**Sunil Kakar** There will be two sources of dividend because there would be two listed companies, one from IDFC Bank and one from IDFC Limited. As you would appreciate, that the total profitability of the whole group in terms of the profit earned for the year is going to get impacted because these are the investment years. Secondly, it gets compounded by the fact that the flow of dividend from the Bank to the IDFC Limited will get cap restricted because of the layers of the structure of financial holding company, etc. So we will have to see what an appropriate level of dividend is at that point in time, but my going in proposition is that the amount available to distribute, given the regulatory constraints would be lower.

**Kajal Gandhi** This is because in the Banking you will need this capital to be for your own growth. So, is it possible that you will be able to give in the Banking entity?

**Rajiv Lall** Our aim is to give some dividend.

**Moderator** We have the next question from the line of Rahul Jain from Goldman Sachs.

**Rahul Jain** I just need a clarificationwith respect to this stressed book of ₹8,000-8,500 crore that you have spoken about. Would it be fair to assume that a lion share would be from the power sector, including gas?

**Rajiv Lall** Yes.

**Rahul Jain** So, that would translate to something like about 25% odd of exposure classified as stressed. So thatis a fair understanding?

**Rajiv Lall** 25% exposure of what?

**Rahul Jain** Power exposure, energy exposure.

**Rajiv Lall** Yes that is fair.

**Rahul Jain** My next question is on the Asset Liability Management, I just wanted to understand, how matched our assets are with vis-a-vis the liability profile that we have? And once we transition into the Bank, the repayments that will come on the borrowing side will we have the equivalent amount of assets available to repay off those or will we replenish those with the deposits? How are you going to deal with that whole ALM thing?

**Sunil Kakar** Yes, so over the last 12 to 18 months, we have been adjusting our asset liability gaps. Actually today, we are long liabilities from interest rate duration perspective. So we are very liquid and as Pavan had mentioned, more from the liquidity LCR ratios also we are well above. So I don't see any significant transition pain with respect to the ALM side of the equation.

**Rahul Jain** My next question iswith regards to your Banking strategy. I just wanted to understand, what kind of approach we are going to adopt for the retail oriented businesses to start with initially and then graduating to say medium-term to kind of long-term? By approach I mean, while we start it will be like more asset centric, more liability centric and how it will kind of try to maneuver as you graduate to the next stages of the Banking transition?

**Rajiv Lall** The rural business would be more asset centric. The retail consumer business will be balanced between assets and liability. That's the thing. And I think that there is a huge liability play even in the corporate and wholesale bank, which does not get the attention it actually requires. So there'll be a huge push for liabilities even in that business.

**Rahul Jain** Isn't the current account part of the business fairly intenselycompeted for or you are talking about the Government business also?

**Rajiv Lall** So in that sense everything is competed for but we have faith in ourselves and in our ability to get our fair share of the market.

**Moderator** Ladies and gentlemen due to time constraints that was the last question. I would now like to handover the floor back to the management for their closing comments.

**Sunil Kakar** Thank you all and the next time we will meet I guess we will be speaking as a Bank also.

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