Equitas Holdings Limited
Q2FY17 Earnings Conference Call
October 24, 2016

Moderator: Ladies and gentlemen, good day and welcome to the Q2FY17 Earnings Conference Call of Equitas Holdings Limited. We have with us PN Vasudevan - MD and CEO, Equitas Small Finance Bank Limited; Bhaskar S - ED & CEO, Equitas Holdings Limited; S Vasudevan - CFO, Equitas Holdings Limited; Sridharan N - CFO, Equitas Small Finance Bank Limited; Raghavan HKN - Head Consumer Banking, Equitas Small Finance Bank Limited; Murthy VS - Head Vehicle Finance and LAP, Equitas Small Finance Bank Limited; Narayan TS - Head Treasury, Equitas Small Finance Bank Limited; Dheeraj Mohan - Head Strategy and IR, Equitas Small Finance Bank Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" and "0" on your touchtone telephone. Please note that this conference is being recorded.

At this time, I would now like to hand the conference over to Mr. Bhaskar S -- CEO at Equitas Holdings Limited. Thank you and over to you, sir.

Bhaskar S: Welcome you all to the Q2FY17 Earnings Call on behalf of the management.

We had a reasonably good quarter second quarter with a loan growth of 45% over Q2FY16.

Before reckoning the one-time bank transition cost, our net interest income grew by 47% and PAT registered a growth of 50% over corresponding quarter of last year. Our ROA and ROE were @ 2.99% and 11.18% respectively without the one-time transition impact.

We have great pleasure in mentioning that Equitas Small Finance Bank Limited commenced its operation as a bank on 5th September 2016. PN Vasudevan, MD and CEO of the Bank, will elaborate on the SFB transition and also the banking operations.

Before I ask Vasudevan, I would like to briefly touch upon the performance of our other Operating Subsidiary, Equitas Technologies Private Limited. ETPL began its operations in mid-August, with the volume of transactions steadily growing. The Driver App is rolled out while the Supplier App will be ready by Q4. Presently the off-line operations are carried out in 3 cities in Tamil Nadu. Full technology led operations is expected by Q1FY18. We expect these branches to break-even by Q2FY18, after which we propose to expand our operations to other States.

Now, I hand over to PN Vasudevan.

PN Vasudevan: Thank you, Bhaskar. Before I proceed to highlight the business performance, I would like to address your curiosity on the first few slides of the presentation we had sent out on Governance. Equitas, as you all know, is a Latin word, which means equitable, which means being fair and transparent. Right from the inception in 2007, we have been extremely fair and totally transparent to every stakeholder in all our transactions. And as explained in the slides, for us Governance is not just about having a certain board / committee structures or even about not doing anything wrong; it is really about setting and following certain standards of ethics and values in all our dealings. We believe that this Governance standards sets us apart from most of the other players in the market and enables us to attract really good quality talent right from the board down to the branch staff, who feel aligned to these values. This enhances our ability to innovate and execute well and is reflected by the fact that we have been able to commence the banking operation in under one year of getting the in-principle license. Governance for us is an integral part of all our business practices and we believe that this in the long-term would remain a key differentiator between us and the others.

Now, we move on to the business highlights. As Bhaskar had mentioned, we commenced operations of banking effective 5th of September by merging all the three subsidiaries into one. We began operations by opening three liabilities branches, all in the city of Chennai. We have approval from RBI for an overall of 412 branches. The remaining will get opened over the next 12 months, which we have time as per RBI approval.

On the performance for the second quarter, the overall advances including securitization grew; it crossed Rs.7,000 crore for the first time and landed at Rs.7,079 crore, which is 45% higher than the previous year's second quarter. Business-wise – Advances, 51% comes from microfinance slightly lower compared to 53-54% of earlier quarters; 25% from UCV; 20% from MSE. MSE had a slight growth of about 2-3%. 4% from housing finance.

Our YoY, MFI portfolio growth was about 41%, commercial vehicles grew by about 34%, MSE grew by about 78% and housing about 24%.

Our NII grew by about 40% over the previous year same quarter. During the quarter, after we converted into a bank, we were able to reduce our cost of funds by pre-closing most of the bank loans that we had taken earlier and because of that our cost of funds which was around 11.5% in the beginning of this year, has actually come down to about 9.7% by H1FY17. We expect the finance cost to go further down as we ramp up our deposits through the rest of this year.

Correspondingly, the operating cost has moved up to Rs.140 crore in the second quarter which is 65% higher than the same period of last year. The operating cost increase is largely due to addition of around 1,600 people who joined us on the liability side. We have more or less completed our investment on the technology side and these assets have been capitalized and so the depreciation impact has already come into the second quarter.

We expect certain additional cost to come over the third and fourth quarter as we roll out the liability branches. The infrastructure cost of the liability branches would get capitalized over the next two quarters and the remaining staff might also be joining at some points in time. So, the cost is expected to go further up before it starts stabilizing while the cost of funds we expect it to go further down as the deposits ramps up and we are able to repay some of the older loans from the fresh deposits that we mobilize.

On our GNPA levels, we were at 1.61% in the first quarter of this year. In the second quarter on a like-to-like basis, our GNPA actually remained very much static around 1.63%. However, because we converted into a bank so, we had to change certain recognition norms from four months we had to reduce it to 90 days that’s one. Secondly is that the repossessed stock in vehicle finance as an NBFC, they were not accounted in the NPA category. But as a bank that gets included in the NPA. So, because of this the overall GNPA has moved from 1.6% to about 2.5% by end of this quarter.

On becoming a bank, we had an excess standard asset provisioning of Rs.37.9 crore in the micro finance book; this was written back to P&L under ‘Other Income’ and that is why you would see in ‘Other Income’, there is a big jump that is basically because of this Rs.38 crore getting added back because of the excess standard provision that we carried. This amount we have used to enhance our additional specific NPA provision by about Rs.19 crore and a floating provision of another Rs.19 crore. So, you would see that the credit cost for the quarter is substantially higher that is basically because this extra Rs.38 crore that we got instead of taking it to the P&L, we thought we would use it to make both specific provision as well as floating provision and that is why the other income has gone up by Rs.38 crore and credit cost has also gone up by the same amount.

PAT for the quarter stood at Rs.46 crore. This represents a 16% growth over same period last year. But we had specifically two items of one-time cost which is non-recurring in nature: one of that is that we raised around Rs.4,500 crore during August principally to help us repay the bank loans and also provide for SLR & CRR investments. So, this money was carried in our books for one month in the month of August and the negative carry of that one month, that cost us some amount of money and second thing is that in September when we pre-closed most of the bank loans, some of the loans had a pre-closure charge on it so, we had to pay that and that amounted to Rs.11 crore. So, this and the extra cost of negative carry of Rs.4,500 crore for that one month period, had an impact on PAT. If we kind of adjust for these impact, our PAT would actually have been higher by 50% over the same period of last year and as I mentioned earlier that these things are non-recurring in nature and so hopefully next quarter, we will not have this and the picture could be slightly different.

The CSR activities have been detailed out in our presentation. We are fairly committed to our CSR actives and our business model is such that our CSR actives is fairly integrated with our business model in terms of the community that we serve and so, there is a lot of interdependence on these two. This continues to do well and the details are there in the presentation for you to go through.

Thank you so much, that brings me to the end of my discussion on the business part of it. Now, we will hand it over to S Vasudevan, who is the CFO of the Holding Company to take us through the consolidated financial numbers.

S Vasudevan: Good afternoon, everyone. Before I go through the details, just to point out that in slide 18, in HF disbursement for Q2, the number should read as Rs.23 crore.

Now, I will proceed to update on the merger impact in the financials. As per the Court approved scheme of Merger, the accounting policy of earlier micro finance and housing finance has to be brought in line with that of the EFL, which has become the Small Finance Bank. MF books carried Rs.32.8 crore of unamortized processing fee income as of the date of merger. This amount of Rs.32.8 crore was transferred from current liabilities to general reserves, net of tax ~ Rs.21.5 crore, to align with the accounting policies of bank. This was not routed through the P&L; it was Balance Sheet to Balance Sheet - liability to liability transfer.

And next proceeding to the finance cost. The finance cost for Q2 is higher than that of Q1. In Q1, you would know that we had IPO done in the month of April so, the IPO funds were brought into the subsidiaries which ensured that the borrowings from the banks were not utilized.

However, in Q2 after the IPO funds were used to finance the disbursement, increased borrowings were there as Mr. PN Vasudevan mentioned to retire high cost debts as well as to fund the SLR & CRR investments. The retirement of debts had happened almost at the end of the quarter, so the full impact of the reduction in finance cost is not felt as of Q2.

In terms of the asset quality parameters we are doing reasonably stable. On a like-to-like basis GNPA, which stood at 1.61% as of June was at 1.63% as of September but due to the change in norms, due to the bank conversion, the GNPA number stands at 2.54%; the stack-up of the GNPA movement from 1.61% to 2.54% is mentioned in slide 27 of the presentation.

Going further, the credit cost was at Rs.52.8 crore for Q2 compared to Rs.18 crore for Q1. However, if we remove the effect of the 90 days transition and the specific NPA and floating provision done, the credit cost would only be around Rs.14 crore for the quarter.

In terms of the ROA it was 2.32% for Q2FY17 compared to 3.69% for Q1. If we remove the one-time non-recurring impact which Mr. PN Vasudevan mentioned, the ROA would have been at 2.99% for the quarter. The gearing was at 2.74 times for the quarter. ROE for Q2 stands at 8.67% compared to 14.21% for Q1. If we were to remove the one-time non-recurring impact, ROE would have been at 11.18% for Q2.

Now, I hand over the session back to the Moderator.

Moderator: Sir, should we open the floor for question-and-answer?

PN Vasudevan: Yes, please.

Moderator: Thank you very much. We will now begin with the question-and-answer session. We have our first question from the line of Amit Premchandani from UTI Mutual Fund. Please go ahead.

Amit Premchandani: I have a couple of questions. Sir, can you help us explain how will the liability mix change as you roll out the bank network and how will the incremental funding cost change? And also if you can clarify the 9.7% cost that you mentioned about the second-half, is it second quarter or second-half? And are there any further pre-closure charge likely in the next two quarters for Equitas?

PN Vasudevan: So, currently we have given the liability mix as on date in the presentation. There is still significant part from the banks including the refinance. NCD is also a significant part, deposits of course is a very small percentage of September. Going forward obviously, we expect the deposit to pick up and it should keep replacing most of the other forms of borrowings over a period. NCDs of course would be run off and grandfathered over the maturity of the tenor of the debentures. We as a bank we will are not permitted to issue fresh NCD anyway. So, the NCDs will run off as they mature and they will continue to get replaced by deposits. So, going forward obviously, retail deposits is something that we are looking to raise but in the immediate term the deposit will be largely the fixed deposits, in the form of bulk deposits and from HNIs. The retail deposits as well as CASA balances that is something that will take a little longer time to get in. As you know we just got three liability branches and even in these three liability branches currently we are just sourcing retail FDs only, we are not sourcing CASA accounts. We have opened lot of employee accounts in the last few weeks and we are doing fairly rigorous testing of all the transaction processing capabilities of the IT system. Only when that is completely satisfactory and we know that we have got everything in place, we will open the customer accounts. So, by middle of November, we might start sourcing CASA and sometime by Jan / Feb of next year is when we expect reasonably large number of branches to be up and running and that is when will be the time to watch our performance as far as CASA is concerned. So, that is how we expect the liability mix to change over a period of time. In terms of the cost of funds, the 9.7% that I mentioned is the cost for the first-half of this year. There is one third question you asked, what was that? I missed that.

Amit Premchandani: In terms of how it has changed the incremental funding cost has it changed at all and pre-closure charges, will there be any further pre-closure charges?

PN Vasudevan: Yes, so, the cost of funds as you said is 9.7% for the first-half of the year and that can only go down further as we go forward because we are getting money at a much cheaper rate as of now, so hopefully that should go down for the second-half of the year. And in terms of pre-closure charges, we have paid out Rs.11 crore of pre-closure charge to the banks and we had about Rs.3,000 crore of bank loans out of which Rs.2,300 crore have been pre-closed including that done in the month of October. With that it comes to end so, there is no further pre-closure charge that will come on the system.

Amit Premchandani: So, even in Q3 no pre-closure charges will get reported?

PN Vasudevan: Yeah, actually, it is all over. So, there is no further pre-closure to be done for the banks because we just have three bank loans now left on the books and those three bank loans are such that the cost of funds of those three bank loans are lower then what we are borrowing today. So those three will be continued and anyway there is no clause of pre-closure in those three loans, anyway we plan to continue it for some more time; basically, because the rate of interest in that itself is quite attractive. Yes, there will be no pre-closure further going forward.

Amit Premchandani: And sir, in terms of bulk deposit borrowing rates what is the average rate that you are borrowing?

PN Vasudevan: Of course it depends on the tenor so, it ranges from anything to anything. But we are seeing good amount of traction around the 8% to 8.5% level.

Amit Premchandani: Okay, sir. And sir, final question, this quarter off-balance sheet AUM has gone up around 20% while on a trend basis it was hovering around 10% to 12% for you. Has the economics of 'off-balance sheet' transactions changed post conversion to SFB or is it more just one-off for this quarter?

PN Vasudevan: Yeah, that was reasonably one-off thing. Actually we did the securitisation before we converted, we did that as an NBFC basically the purpose was dual, one to get some cash flow in and second, reduce the borrowing to that extent which also helps in our SLR & CRR so, it was a dual purpose so, that is why it was done. It was done prior to conversion of the bank.

Amit Premchandani: So, on a trend basis, hover around 10% to 15% rather than 20% that we have seen now?

PN Vasudevan: RBI has a cap of 35% for securitization portfolio and in terms of how much will be within that 35%, I think it is a question of the cost of funds, it is a question of the rate at which we have demand in the market. So, it is difficult, I mean it is a not a business decision that we need to take upfront. It is something that we need to take dynamically as we move forward because it is basically that as far as we are concerned, it is a tool to reduce our overall cost of funds that is about it. So, it is a decision that we will keep taking from time to time basically depending on what is the rate at which you are able to get the other from of borrowings and what is the rate at which we get demand for these kind of assets. So, I think it is largely a decision that will be taken from time-to-time.

Moderator: Thank you. We have our next question from the line of Ravi Singh from Ambit Capital. Please go ahead.

Ravi Singh: Yeah, just a clarification on the SLR and CRR funds deployed of Rs.2,000 crore that looks high compared to that borrowing base of rupees roughly Rs.6,000 crore. So, what is your thinking here?

Narayan TS Yeah, as it was explained earlier there were a few loans which were to be pre-closed in the beginning of October which amounted to about Rs.550 to Rs.600 crore. So, that part which was there was held just before we got into this SLR & CRR part in the end of September, was parked as surplus and to be repaid in the first week of October, the funds were held in Treasury Bills. So, that is the amount which is showing excess against the required size.

Ravi Singh: So, is it fair to assume that during the rest of this financial year, SLR & CRR holding will be closer to the regulatory requirements?

PN Vasudevan: Yeah, it will be slightly closer to the regularly requirement plus also enabling some kind of buffer to have some provision for liquidity.

Ravi Singh: Okay. And sir, last question on this cost of fund of 9.7% in the first-half, does it include the impact of equity also or how is it being calculated?

S Vasudevan: Yeah, it has been factored into effective cost of funds actually the equity funds has been considered. Correction: It does not include cost of Equity.

Moderator: Thank you. We have our next question from the line of Roshan Chutkey from ICICI Prudential. Please go ahead.

Roshan Chutkey: Firstly, how does this cost to income ratio move, I mean how does it look like according to you in a few years from now we have our full of line liability branches opened, where do you see this number moving?

PN Vasudevan: Yeah, so the cost to income currently is around 57-58%. It is difficult to predict exactly where it will be once all the branches are up and running, that is something that we will have to only figure out as we go by. There is of course the benefit of cost of funds going down and that cost of funds going down will also improve the income side of it. So, there is going to be certain increase in the income because of cost of funds going down and then the expense also is going to go up so, how these two will pan out and exactly what is it, that is not something that we will able to give you a great idea just now. But there will be a dual impact on both sides.

Roshan Chutkey: Sure, sir. So, currently we have only three branches opened up and how much have we depreciated in this quarter? What is the corresponding amount to these branches opening cost?

PN Vasudevan: Our CFO will tell you this.

S Vasudevan: On the branch infra assets, we have capitalized about Rs.1.8 crore in terms of infra cost of three branches, which we had operationalized. The depreciation impact is only for 26 days of September, which works out to less than Rs.5 lakh.

Roshan Chutkey: Less than Rs.5 lakh and it is corresponding to only these three branches or was there any other branch that was included in this which are probably going to get opened?

S Vasudevan: No, only for the three branches.

Roshan Chutkey: Only for these branches about Rs.5 lakh, okay. And how many employees have we recruited in this interim period - in the last three months?

PN Vasudevan: See, as of now for the liabilities team, we have got onboard about 1,600 people.

Roshan Chutkey: 1,600 people, okay. And what do we intend to take this number to in another year's time?

PN Vasudevan: Overall at the end of may be in seven - eight months from now, when all the branches are up and running, we expect total staff count of around 3,500 on the liabilities. Out of this 3,500, basically about 1,800 - 1,900 will be the sales team and the remaining will be the branch service and the cross sales teams.

Roshan Chutkey: Okay, thank you, sir. And right now in the liability mix, the NCD bit, what is the tenor of these NCDs?

PN Vasudevan: It ranges around 18 - 19 months to three years but on an average, you can say it will be 22 - 23 months will be the average tenor.

Roshan Chutkey: And CPs, I presume at least one year CPs?

PN Vasudevan: CPs no, it is not one full year I think the average CP tenor will be around seven - eight months.

Roshan Chutkey: And have it does any kind of refinancing of bank borrowing sir, we have prepaid the sum of the bank borrowings but the bank borrowing proportion, absolute amount has not quite decreased as such if I look at the numbers.

PN Vasudevan: Yeah, that also includes our refinance of SIDBI, NABARD and NHB that is also classified under that. That is also substantial amount that is included in that, that is why it has not gone dramatically down but maybe if we remove then the bank alone would be much, actually I think as of September…

S Vasudevan: As of September, the term loan is 27% & refinance is 22%.

PN Vasudevan: Okay. So it was 27% banks and 22% was refinance.

Roshan Chutkey: Okay, sure. And how much are we paying on term deposit sir?

PN Vasudevan: Term deposit I mean of course it is all tenor based so, there is different rates for different tenors. In some tenors, we have been fairly in line with the rest of the market. In some tenors, we are giving a half percent more, where we want to focus on.

S Vasudevan: Roshan, just to clarify on your query on the branch infra, the three branches and one of the zonal offices has also made been operational so, it is actually three plus the zonal office, so it is effectively four offices, you can say about Rs.1.74 crore of branch infra capitalisation.

Roshan Chutkey: Sure. If I look at the slides on separate business, the interest incomes in four business when I add them up it comes to about Rs.327 crore whereas our overall interest income is about Rs.356 crore, difference is about Rs.29 crore I presume some of it is, most of it should be investment related income, right. But if I look at our investment book it is about Rs.1,800 crore which would not yield more than Rs.9 crore to Rs.10 crore if I do the math assuming all of it is invested in GSEC, what am I missing here?

S Vasudevan: It includes gains from mutual fund investments as well as interest on FDs, prior to becoming the bank itself.

Roshan Chutkey: Sure. And how does the PSLC income of Rs.7 crore what is the corresponding base AUM for this? I mean I want to know the percentage commission that you are earning on PSLC certificate essentially.

PN Vasudevan: See, the percentage will change from time-to-time obviously, I think the ones we contracted was at an average of 2.2 or so.

Roshan Chutkey: 2.2%, okay. And how is the BC network shaping up? How many BCs do we have in operations currently, what kind of incentives are we offering them?

PN Vasudevan: I will ask Raghavan to answer that and this should be your last question (laughs ….).

Raghavan HKN: Yeah, currently we have identified 71 branches where BC operations are underway and as you know the BC operations, getting the right person to operate as a BC is a challenge, then the training is also a challenge. First thing is that the BC operations will start with asset leads right, and as and when the liability branches roll in, they will also start selling the liability product. So, currently we have close to 800 BCs on board and all are sourcing the asset leads; then, as and when the bank branches become operational, they will start the liability piece of it. And the commission for them on the asset side ranges somewhere around 0.5% to 0.9%.

Roshan Chutkey: And on the liability side.

Raghavan HKN: On the liability side, we are yet to form the revenue model for them; it is in the stage where we will be able to close in the next couple of weeks.

Moderator: Thank you. We have our next question from the line of Dhaval Gada from Sundaram Mutual Fund. Please go ahead.

Dhaval Gada: Firstly, just a data point question what is the GNPA number for the MFI portfolio on 30 day basis?

Raghavan HKN: It is 25 bps.

Dhaval Gada: Okay. And on 90 DPD also it is 25 bps as per your presentation?

S Vasudevan: It is 0.27% on 30 days and 0.25% on 90 days.

Dhaval Gada: Okay, fine. Secondly sir, in the 1Q presentation we had mentioned that EFL GNPA would be Rs.110 crore on 90 DPD. In absolute and in percentage term, I understand that this quarter there has been a spike there. Any steps that we have been taking to address this asset quality stress that we are seeing in the portfolio both vehicle and to some extent in the MSE portfolio?

Murthy VS: See, on the vehicle, finance, if you look at on a like-to-like basis from June to September, if you apply the same norms that was applicable in June, the GNPA % stands at almost same level. The addition is one due to like Mr. Vasu explained in the initial speech about addition of the repossessed stock back to the NPA - this is one major impact of Rs.15 crore which got added so, that is a change; in the LAP in the MSE segment, an increase of Rs.3 crore increase between June & September, but that book is very-very small as of now so, due to that the percentage may look higher and there are some large accounts which we funded in the initial years which are up to somewhere around Rs.1 crore ticket size and which ticket size, we stopped subsequently; so, if these accounts were resolved and the NPA will come down 1% actually.

Dhaval Gada: So just to get it clear in June quarter, the number included the sensitivity of the repossessed vehicle the Rs.110 crore that we mention for EFL did that include the…

S Vasudevan: Yeah.

Dhaval Gada: Okay, fine. And sir, in terms of OPEX do you think it would stabilize after I mean 4QFY17 do you think the OPEX number should broadly stabilize after that since most of our branches should come by then or at least bulk of them?

PN Vasudevan: Yeah, absolutely, may be most of the cost should have got incurred during this financial year may be a very small percentage might spill over next year. But yes, going forward into the next year, mostly the cost should have kind of stabilized.

Dhaval Gada: Okay. And just lastly, on the branch expansion, so our original plan of 412 included the 25% the rural unbanked branches. There is a draft which is there which suggest that on the legacy branches the extension could be there up to three years so, are we sort of looking to calibrate the unbanked branches over a period of time rather than opening it this year itself or …?

PN Vasudevan: See, this unbanked rural branches for us is also a business proposition, it is not just a financial inclusion focus but it is a business proposition because in these places we already have our lending operations, so these are not new locations as far as we are concerned typically what happens this branch exists in Tier-IV or a Tier-V town and from there, we cover a 30 kilometer radius which means really we cover may be about 40 - 50 villages in and around that area and we are already doing business in that area and the rural branch that we are talking of is typically a rural branch which is located in one of these villages but will actually service the same geography. So, for us the rural village is as much a business focus as the semi-urban or an urban location. So, we might not change it even if the RBI guidelines, which is a draft form, gets through and finally it comes out in the same form, I mean we will still study it and we will take a call as we go by. But basically to say that the 25% rural obligation is not so much a burden on us as it might be may be for others I do not know. But for us it is not really looked at from a burden perspective.

Moderator: Thank you. We have our next question from the line of Hiren Dasani from Goldman Sachs Asset Management Company. Please go ahead.

Hiren Dasani: Just one or two small questions. On the OPEX side, so one you said by Q4 of this financial year or exit of this financial year, we should be largely stabilizing it, because of the roll out cost will be largely in place. So, let us say, the overall OPEX was about Rs.130 crore would this be substantially higher number as we roll out all the branches in your mind on a quarterly run rate basis?

PN Vasudevan: Yes, there should be an increase on this because as you said we have recruited nearly 1,600 people but the remaining nearly about 1,700 - 1,800 are yet to join, so that will be one element. Second thing is that from a branch infrastructure perspective, we have hardly capitalized three - four branches. So that branch capitalization will further have a depreciation impact. So, yes there should be an increase in the cost as we leave this current financial year.

Hiren Dasani: So, would it be fair to estimate about Rs.175 - Rs.180 crore of quarterly run rate by March 2017?

PN Vasudevan: We have not worked that out and I am not in a position to share that with you.

Hiren Dasani: Okay. Now, the other thing is a just a clarification on your presentation on slide 47 which is talking about disbursement segment-wise and state-wise. Sir, the state-wise disbursement are consolidated for all asset classes, it is not only MFI?

PN Vasudevan: Yeah.

S Vasudevan: Correct.

Hiren Dasani: Tamil Nadu would have gone up because I mean you would have let us let us say done more of MSE and the other activities.

PN Vasudevan: That is right, yes.

Hiren Dasani: And what would be your let us say MF concentration in Tamil Nadu, if you have that data readily available.

S Vasudevan: Out of our total micro finance portfolio, Tamil Nadu should be contributing around 60%.

Hiren Dasani: Okay. And is that number moving up, moving down or…

PN Vasudevan: Kind of fairly stable, I would not say it is not exactly moving up or down, you know we have opened a lot of branches outside TN in the last two - three years which are contributing. We were about 72%-73% about a year and half or two back, it has come down over the last may be one and half years or so but in the last two quarters we are seeing 64%-63%-62% so, it is kind of hovering around that. It is around 61% now.

Hiren Dasani: Okay. But I mean if you are opening more branches outside Tamil Nadu, the number should be coming down?

PN Vasudevan: Yeah, actually if you look at it from the number of clients perspective it is actually lower but what happens is in Tamil Nadu branches are all between anywhere eight to ten years vintage so, they are in the third cycle or fourth cycle which is at Rs.30,000, whereas the new branches our first loan is only Rs.20,000 and it is a two years loan so, after two years we will giving Rs.25,000, after two more years we will be giving Rs.30,000 so it takes time for them to catch up in terms of the value. In Tamil Nadu, our MFI customer as of September is around 1.75 million.

Hiren Dasani: Sure. And sir, lastly a lot of concerns on the micro finance growth in general countrywide and specifically Tamil Nadu also. So, what is your experience specifically in Tamil Nadu in micro finance asset quality?

PN Vasudevan: I will ask Raghavan to take that.

Raghavan HKN: Hi, this is Raghavan. The portfolio in terms of micro finance Tamil Nadu contributes 61 odd percent and the portfolio is absolutely good; there is no concern as far as the portfolio is concerned because the PAR (Portfolio at Risk) in Tamil Nadu is just 42% and as far as the industry is concerned, you know the dichotomy exists one side is that out of 250 million households close to 100 million households can be considered as potential clients so, as per the MFIN records, close to 22% is what is the penetration of micro finance client. So, the other side if you look at it there are large number of pockets you know a huge concentration of micro finance companies operating there and plus in the last one and half years, we have seen lots of banks getting into this space. So, at particular segments at certain places, the concentration is there which can lead to some hotspots but otherwise the dichotomy of opportunity existing and some places of concentration is already there. So, in this scenario I think Equitas has been very cautious in terms of growth and fortunately, MFIN is seized of this matter and MFIN as we know is the industry SRO and they are in touch with banks and other MFIs, they want to bring everyone on a single platform and sensitize the sectoral issues so, that we can lay down our common ground rules for an organized growth and also to kind of ensure that the over-leveraging does not happen. So, that talks are on; hopefully very shortly we should be able to get everybody on board and get this sector to an orderly growth.

Hiren Dasani: Sure. And just to be clear now that you are an SFB but you still contribute data to the bureaus and you still go by the two loans per borrower kind of guidelines or you are no longer following that?

Raghavan HKN: We contribute the data; it is mandatory as far as the RBI guidelines are concerned, we have to contribute the data to all the four credit bureaus - number one. And number two, I think, more than the norm, I think credit risk is what drives you to kind of take call. So, despite becoming a small finance bank, we are sticking to two institution guideline so, basically if there are two micro finance have lent and as an SFB, we do not lend. So, those are the prudent norms that we follow.

Moderator: Thank you. We have our next question from the line of Abhijeet S from Kotak Securities. Please go ahead.

Abhijeet S: Sir, we have seen very strong growth in the MSE and the vehicle finance segment and perhaps some signs have slowdown in the micro finance segment. Sir, how should we read into the impact on the NIM profile because on this and on a related note sir, because of the slowdown in the micro finance we have seen the disbursement slowing down over the few quarters? Sir, should we expect growth trends to sort of slowdown below 25%-20% odd levels from currently 40 plus percent levels, that is the first question.

PN Vasudevan: Yes, in our MSE business, 70% of the MSE is actually a cross-sell to our existing top end of the micro finance customers; so, obviously, there is a lot of comfort we derive from that and our book is, touchwood, extremely good. So that MSE should continue to grow well into the future. Used commercial vehicle again, touchwood, our portfolio quality has really held well. It is a three-year tenor, typical three year tenor; now, we have completed five years in business in vehicle finance and so, we have crossed one cycle and now we are almost at the end of the second cycle and we see that our NPAs have really plateaued or come down over the last few quarters consistently so, that again gives us a good amount of comfort in terms of continuing to focus on growing the used vehicle business.

In terms of NIM, if you look at it you know both these products in vehicle financing our average loan size is Rs.3.5 - Rs.3.7 lakh, in the MSE, the average loans is around Rs.1.5 - Rs.2 lakh. So, because of this, our cost of operation in these segments is obviously a better then the cost of operations of the micro finance business where the typical average loan size is only about Rs.20,000 - Rs.21,000. So, because of that yes, there might be a contraction in the NIM but then if you look at the ROA that will reflect the difference in terms of the operating cost. In terms of the growth in micro finance, see micro finance, we take it as things come by, we do not have predefined percentage of growth that we want to or need to achieve so, we just take it as the market keeps evolving, as Raghavan mentioned earlier there are dichotomous situation where you know we have on the one hand 70%-75% unmet demand on the market and on the other hand you have a lot of areas where customers have probably ended up taking more than two loans, three - four - five loans and you know might be under some kind of stress we do not know. So there is a lot of discussions going on at the industry level, we have had some meetings in the past, some more meetings are scheduled in the near future. The effort is to try and evolve some kind of a common credit filter which we all then agree to, so that that will help de-risk and make it more sustainable. So our own focus, our own appetite to grow the micro finance business will continue to be tempered with what is happening in the market and how are the other players coming together and what is the kind of lending norms, prudent norms that everybody is agreeable to, how effective is that getting implemented on the ground. So, all this will keep determining; see there is no problem in growing in micro finance. If we can grow at 100% that itself is not wrong, the only concern is whether that 100% growth is coming by giving the money to the same set of customers who are getting over-leveraged that is the whole question and that is what we are trying to address at the industry level by getting MFIs and the banks coming together to work it out. If something satisfactory works out and we know that on the ground it is being implemented effectively and multiple lending is actually either completely or substantially addressed then we have no problems, we can come back and grow micro finance as much as we want. Because you know right now in the country, we are the most efficient micro finance in the entire industry today because our operating cost is around 7.5% or 7.4% and that is on a loan outstanding per client which is almost about 50% or 60% of the rest of the players. So, at that kind of loan outstanding per customer, our operating cost is as good as anybody else. Which means that I am actually almost anywhere between 50% to 75% more efficient than anyone else and our systems are very very tight, our controls are very strong, you know till now, touchwood, we have never lost a single rupee of our cash collection ever through employee frauds, at all till today. So, we have very tight robust operating systems controls processes in place, our technologies is substantially leveraged in reducing our operating cost. Everything is in place for us to grow but our decision to grow will very much be aligned with what is happening in the market.

Abhijeet S: Okay. Sir, moving to the other segment which is the housing. Sir, we have not seen this segment or the portfolio kind of stabilizing, the growth rates are pretty moderate given the very small size, the NPAs are sort of inching up. Sir, what is the thought process on growth…

PN Vasudevan: Yeah, see, I think we have gone through this in the earlier calls also. Right now housing is not a focus area for us, it is doing a small experimental thing, we are basically doing affordable housing finance at the low end; there is no equivalent portfolio in the market of anyone else for us to see how it performs so, it is something that lot of us, similar to us a lot of people are there in this market all fairly new anywhere between two - three years to four years in business. So, we are all trying to learn how this portfolio is going to perform because it is a 15 years loan, it is not a two - three years loan for us to get a quick feel within a couple of years. It is a 15 year loan so, we are all just trying to grope around and find out how this portfolio is going to perform and behave. So, it is more on an experimental basis, we have rolled it out hardly in about 15 branches or so. We are strengthening our housing finance team as I had mentioned in the earlier calls also. Over time, we believe that may be in a three years to four years' time frame, down the line this could be a principle driver, it could be but right now it will not be and it is not and as we gather experience and you know increase the quality of staff handling this and get a better experience of it, that's when we will decide how to take it forward.

Moderator: Thank you. We have our next question from the line of G. Vivek from Goldman Sachs Investments. Please go ahead.

G. Vivek: One question I had was regarding what stand us out vis-à-vis competition and what thing which we are doing different from the competition and what about the geographical concentration risk we have in south, any plans for expanding to U.P. / north side and how good are our risk management?

PN Vasudevan: So, what set us apart from competition? There is a book called the 'Purple Cow'. Someone happen to give it me so, I read it where it basically says in a crowd of black and grey cows, only a purple cow stands apart and so, the book was all about trying to figure out which companies are purple cows. So, we believe in Equitas that we are a purple cow, we have demonstrated a very very strong capability right from 2007 onwards of being highly innovative and very strong in execution. So that is something that we have demonstrated over the years in diverse fields it is not just in one field. In micro finance, we have what we have done is a benchmark in many respects in the industry, used commercial vehicle is a very difficult business to do, we have done it in a manner where we are very comfortable on our portfolio quality and we are able to still look for growth in that; MSE which is something which most people have kept off, touchwood, we have done very well and we are nearly completing one cycle on that, it is a four - four and half year loan tenor, we are completing one cycle and our portfolio has held very very well and if you look at our CSR activities, the kind of activity we do in most of them, there is no parallel in the country with any other corporate doing that kind of activities. And we do all this by ourselves we do not just fund somebody who does it. And if you look at the bank roll out also, we have been able to roll it out in under a year's time, which no one else has been able to do it. So, I think our ability to innovate and ability to execute well, really sets us apart and we strongly believe that draws out of our governance, our values and ethics that we are committed to, which really helps to attract a lot of good quality people all around us who are more happy to work for us for just helping us than, I mean all of us need money that is no doubt on that but at the end of the day when you get a lot of satisfaction doing something for an organization you begin to like, I think that makes a lot of difference. So, I think that really is what set us apart compared to anyone else.

In terms of geography concentration, in terms of south, yes, 50% of our branches are in south so, more than 50% we definitely expect to continue from south that is unlikely to change very fast, 30% from west, 20% from north we have currently structured so; very broadly that ratio may hold for some more time. We do not plan really to expand to other States like what you mentioned, U.P. or the entire East for that matter. We do not have any current plans to expand to those areas because the areas where we operate itself offers substantial amount of unmet demand. So, we would prefer to continue to operate in this markets in which we have by now got a good knowledge of and we will not really look to expand to other States just now.

G. Vivek: My last question was on the risk management practices we follow, sir.

PN Vasudevan: Risk Management - the entire business we do whether it is micro finance, MSE, used vehicles, everything is very small ticket large number of customers and quite often cash collection is one of the main form of collection, which adds further to the entire operating risk. So, we are sitting on a fairly high operating risk model. The basic model itself is high on operating risk and so we have been able to put right from the beginning, a very strong operating risk management control system in place. We have designed what we call as Equitas Chakravyuh, I think I might have mentioned this to some of you earlier and bored you to death with all that stuff but since you give me an opportunity, I will bore you also to death on this. So, we have what we call as an Equitas Chakravyuh, basically it is a seven concentric rings of risk management built around every single field level transaction which happens on a 'day-in day-out' basis. So, whenever a customer, whenever a staff interacts with the customer that interaction is then overseen by seven different layers of people at seven different points in time at seven different random sampling basis. So, when a field level boy does something with the client he wants to cheat either the customer or the company, he has to then manage to move out through these seven rings without getting caught and that is the challenge, that is a real challenge and because of that as I mentioned earlier we have not lost a penny of cash collections till today in the last ten years, where that is a fairly standard industry norm of cash collection getting misappropriated and so on and on. I mean we have put in a lot of efforts on our operating controls because we know that we are sitting on that kind of a business model.

G. Vivek: Okay, sir, thanks a lot. And last question was about this credit bureaus role and playing for the entire industry and some improvements happening over there, sir.

PN Vasudevan: Sorry, credit bureau?

G. Vivek: Yeah, credit bureau since that is quickly for micro finance, CIBIL and other things are there in the banking domain.

PN Vasudevan: Credit bureau has already been working, it has been working from 2011 and got actually strengthened in 2012 and it has been working very well today with fairly high level of certainty, we can get a credit report on any MFI customer anywhere in the country with an accuracy I would say of may be 85%-90%-95% so, that is pretty good. And you know recently in MFIN, we took a call that all micro finance company should compulsorily collect the Aadhar number of the customers and populate that in our bureau data. So, that decision was taken a few months back and today all the MFIs more than 93% to 95% of all the loans that we are giving in the last three or four months they are all going to the credit bureau with the Aadhar number seeded in it. So, the quality of database in the credit bureau is continuously improving and may be a year or so down the line, we should be in a position where almost 95% of customer data in the credit bureau has an Aadhar number and so, you just query the Aadhar number and quality of report that you get should be 100% accurate. So, I think there is substantial amount of improvement done on the credit bureau both by the bureaus and by the industry.

Moderator: Thank you. We have our next question from the line of Manish Karwa from Deutsche Bank. Please go ahead.

Manish Karwa: Sir, my question is on branches, you are adding almost 400 odd branches and you have along with people you have already added about and the people will add, will be about 3,000 odd people. So, roughly does it mean that you will probably about seven to eight staff per branch kind of a model?

PN Vasudevan: Yes. So, we will have approximately about seven to eight, of which you will have a branch manager, branch operations manager then you will have either a one or two sales and service executives in the branch depending on the location and the number of customers. The rest of the staff are basically sales staff. So, you will have a sales staff either three or four or six or seven depending on the kind of market location, where the branch is located. Basically these are sales staff who are the people who go out and mobilize accounts for the branch.

Manish Karwa: Okay. And what typical function of the branch would be to collect deposits at least to start off with, is that right?

PN Vasudevan: Yeah, see in a branch typically, yes, you can pursue both current savings accounts as well as FDs and of course, the cross-selling opportunities always exists so, there can be a fee income, which the branch can look to generate on cross-selling, there is a cross-selling there is a fee income opportunity on trade and FX, which is also a possibility. So, a branch should ideally be contributing on all of this typically speaking but for us the immediate and first focus, as we roll out the branches would be on the float that will be the first and immediate focus; we might be able to see some traction on fee income on trade because many of our current account customers would be small time business people and there might be trade opportunities from that segment so, that could be something that we look at as we go by. But for some time at least our principle focus would be more on float then on fee.

Manish Karwa: Okay. And lastly, a typical branch how much does it cost to us in terms of initial capital cost and recurring cost?

PN Vasudevan: Initial capital cost of setting the branch all inclusive is approximately Rs.35 lakh. In terms of running cost of a branch on an annual basis, if you look at all the operating cost, staff cost, maintenance cost, rental cost, all put together, depreciation, everything put together, if you look at our running cost it can be anywhere between Rs.35 to Rs.50 lakh depending on the geography / location of the branches.

Manish Karwa: Okay. And you have any targets of breaking even on a branch; is there a number you have in mind for two years - three years.

PN Vasudevan: I hope Raghavan has such a number, I will ask him to answer that.

Raghavan HKN: The break-even would be somewhere around 18 months is what we are targeting, 18 - 24 months.

Moderator: Thank you. We have our next question from the line of Aseem Pant from HSBC. Please stay connected. Participants may I request you to stay connected, as the line of the management has got disconnected. Ladies and gentlemen, kindly note, we have line of the management connected. Sir, we had a question from the line of Aseem Pant from HSBC.

Aseem Pant: Just had a couple of questions, one is on the PSL compliance bit, as you grow your MSE book could you give some outlook on how much excess PSL you would have let us say two years to three years down the line? And the second part, I will come to the second question later, it is little different from this one.

PN Vasudevan: Okay. So, you know we have a 75% PSL requirement to comply with and within that 75%, we have to have the sub break-up which is applicable to other banks within the 40% stuff, so that is the norm for us. Most of our book is PSL may be with a minus 5% - 7%, that is 90%-95% should be a PSL, generally speaking. We are also as of now we do have sufficient Agri on MSE, etc., so generally complying with the PSL should not be an issue in generic sense but that also gives us a good opportunity because there is a lot of demand for certain type of PSL assets in the market whether it is an IBPC or PSLC, so that is something that we will keep playing with as we go by. Our own PSL commitment, the obligation to reach PSL starts from the quarter ending June 2017. So, June 2017 will be the first reporting period for us for PSL compliance.

Aseem Pant: Okay. So, sir, this 5% to 7% that you said which is not PSL complaint, out of curiosity which segment would this be?

PN Vasudevan: That will be the LAP, that is a very small part and basically that is the LAP, where customers borrow based on security of the house property but the end use is not business.

Aseem Pant: Okay, thank you, sir. Sir, second question is regarding you know a couple of figures you gave in your last quarter's presentation where you talked about the market size for UCV finance is around Rs.1.9 lakh crore and then you talked about MFI market size is Rs.2.8 lakh crore to Rs.3.4 lakh crore. So, just to get some more granular sense in terms of the ten States that you are present in and you are trying to grow, would you have a sense of what would be the market size corresponding to these regions specially for UCV and MSE?

PN Vasudevan: See on an overall basis if you see East will account for anywhere approximately around 10% to 15% of the business and U.P. might represent may be about 3% or so, even if you want to knock off about say 20% which can comprise of the entire East & U.P., the remaining 80% should be in the areas where we operate.

Aseem Pant: Okay, in these 10 - 11 States.

PN Vasudevan: 13 States.

Aseem Pant: 13 States, okay.

Moderator: Thank you. We have our next question from the line of Clyton Fernandes from Systematix Shares. Please go ahead.

Clyton Fernandes: I just had one question, what would be our outstanding employees as of September 30th, 2016?

S Vasudevan: 11,100.

Clyton Fernandes: Sorry, sir, I did not get that.

S Vasudevan: 11,100.

Moderator: Thank you. We have our next question from the line of Abhineeti Gupta from PCS Securities. Please go ahead.

Abhineeti Gupta: I want to know how much expenditure would you be accounting for in the second-half of FY 2017 for rest of the branches.

PN Vasudevan: Well, actually that was asked in the earlier round also where we had said that yes, we gave inputs in terms of the kind of cost that will come in and the benefit in terms of cost of funds which might also come in. I think we have gone through that already.

Abhineeti Gupta: Okay. Sir, my next question is can I get a break-up of the customers in each cycle like cycle I, cycle II for MSFI sector?

Raghavan HKN: Currently if you look at it, the first cycle clients are close to 60% and close to 30% of the clients are second cycle and rest are the balance 10% to 15%.

Moderator: Thank you. We have our next question from the line of Mitesh Jain from Investec. Please go ahead.

Mitesh Jain: Sir, my question is on SLR. If I look at SLR and calculate the percentage using refinanced borrowing that comes around to around 34%. So, incrementally this Rs.1,800 crore number of SLR should not increase over next even two quarters - three quarters, is that right?

Narayan TS: Yeah, that is right. That has already come down and that is as per the requirement.

Mitesh Jain: So, a normalized run rate would be around 23%-24%, is that….

PN Vasudevan: Yeah, absolutely.

Mitesh Jain: And SLR is not required on the refinance with the refinance borrowing from NABARD?

Narayan TS: Yeah, you are right.

Mitesh Jain: And sir, lastly what is our incremental cost of borrowing so, incremental cost of funding as it is explained is around 9.7% but what is incremental cost of borrowings for us?

PN Vasudevan: Right now if you look at the deposits of course they are tenor linked I think this was also a question asked earlier, I did give some answer, there are tenor linked rates obviously but typically we are seeing a lot of traction in the 8% to 8.5% range.

Mitesh Jain: So, I was talking about the blended cost of borrowing including all the sources of funding.

PN Vasudevan: As of September we have given you the blended cost was 9.7%.

Moderator: Thank you. We have our next question from the line of Jigar Valia from OHM Group. Please go ahead.

Jigar Valia: Sir, I would like some clarification and understanding on the PSLC how has that moved up and pre-SFB if you can quantify in terms of were there any sell downs of PSLC or any income through as a BC pre-SFB?

Narayan TS: See, sell down on PSLC only happen during the few trades which were there was close to the September quarter end that is all.

Jigar Valia: Okay, PSLC has started only in the September quarter.

Narayan TS: Yeah, in fact the product itself was introduced during this financial year by Reserve Bank of India and actually the momentum is only catching up off late.

Jigar Valia: And how is that, do you see that as a very significant advantage post the SFB license?

Narayan TS: That will depend from market and the appetite from time-to-time.

Jigar Valia: Got it. So, there is no fee income as such which is coming from the relationship with the bankers who depended on us for sell downs, those can continue?

Narayan TS: Come back it is not clear to me.

Jigar Valia: So, the banks who really depend on the 12 MFI players for PSL so, that dependence can continue and those demands can be met through PSL?

PN Vasudevan: Yes.

Jigar Valia: When you gave the name or the cost of funds or going ahead would those be adjusted for PSLC fees or that would be as a part of the other income?

PN Vasudevan: No, the cost of funds will not include PSLC. It is 'Other Income'.

Jigar Valia: Ok, it is 'Other Income'.

Moderator: Thank you. I would now like to hand the conference over to Mr. PN Vasudevan for closing comments. Thank you and over to you, sir.

PN Vasudevan: Okay. So, thank you so much all of you thanks for coming on line. This has been a difficult period for Analyst I would say because we are going through a transition and I know that Analyst and Investors always love things to be extremely simple and easy to understand so, that things just fall in place easily, by the transition period like what we have gone through is not at all simple, not easy to understand. So, I thank you so much for taking the trouble to read our presentation and ask all these queries and we also will try to continue to do our best in terms of explaining in as simple as possible a manner, the whole transition effect and impact but may be after another two or three quarters hopefully, things should really get as simple as possible. Thank you so much and see you again next time. Bye.

Moderator: Thank you Mr. PN Vasudevan. Ladies and gentlemen on behalf of Equitas that concludes this conference. Thank you for joining us and you may now disconnect your lines.