"Shriram City Union Finance Q4 FY18 Results Conference Call"

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Moderator: Good morning, ladies and gentlemen. Welcome to the Shriram City Union Finance Q4 FY2018 Results Conference call hosted by JM Financial. 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 "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nikhil Walecha from JM Financial. Thank you and over to you, Sir.

Nikhil Walecha: Thank you. Good morning, everybody and welcome to Shriram City Union's Earnings Call to discuss the 4Q 2018 Results. To discuss the results, we have on the call Mr. Ramasubramanian Chandrasekar, who is CFO and Mr. Lakshmi Narasimhan who is Executive Director. May I request the management team to take us through the financial highlights subsequent to which we can open the floor for Q&A session? Over to you, Sir.

Lakshmi Narasimhan: Thanks Nikhil, thank you so much. Very good morning to all of you, this is Lakshmi and I have our CFO Mr. Chandrasekhar also on the call. Apart from Jai Singh, who is our head of Investor Relations. So, thanks to each one of you for having joint the call. I just spend few minutes giving what according to us is the highlight for Q4 as well as this year and then we would kind of open ourselves up for questioning from each one of you.

In terms of highlights:

I think we are broadly getting back to our growth level as we have guided close to about 19% in terms of AUM growth. PAT again has grown by about 20% during this financial year. Couple of interventions that we did which has been kind of mentioning in individual meetings with different people has been the fact that we have implemented very robust sourcing and underwriting mechanism for the small and medium enterprises book during the year. That implementation is now complete across the country and so the complete sourcing of retail business of SME now happens through a pattern which is uniform across the country. So, there we have seen good traction during this financial year and that I guess will get reflected as we kind of go forward under two heads largely.

One is improvement in the productivity and as a consequence expected drop in the Opex in personnel expense during the next financial year. As also improvement in the credit quality which broadly we have now started seeing, even during Q4 if you see the overall credit cost of about 4 odd percent including the impact of the whole process moving to the 90 DPD process. So, I think that is a highlight that we would like to leave you all with. The second piece is also the fact that cost of fund has held quite well during this entire year and considering close to 50%-60% of the borrowing remaining fixed. I would expect not too much of an increase in the cost of fund as we go forward, in fact we would target it to remain at the current level as we kind of go forward. What is also good is the two-wheeler business we keep getting questions on how the two-wheeler business has done? That is grown close to 20%-22% during this financial year.

Two areas which we think we should concentrate on as we enter the next financial year would be the headcount in terms of people that we have. We had mentioned during our Q3 call and analyst meet the fact that we are sitting on a 1,500 to 2,000 people bench strength. Essentially that was brought in because we saw that we were losing people in different markets and we had created enough bench strength just to overcome any stress in terms of non-availability of people. So, this year for us that would be a clear item of focus in terms of handling the number of people that we are going to keep in the system for a longer while. The second area of focus for us as we kind of get into the next financial year is going to be bringing down the credit cost to our regular levels of about 3%. We are at about 4% now after having move to 90 plus with the provisioning amount remaining to be stabilized I think we should come back to our regular levels if not next financial year at least during the financial year subsequent to the next one. But you will clearly see a directional drop in the credit cost as we kind of hit the next financial year.

Gold is another area where we have not been successful during the financial year that has gone by. We need to get a clear strategy on the gold business because we are still struggling with certain items on the gold in terms of cash disbursements so on and so forth. So, while we are compliant completely with what the RBI requires us to do in terms of cash disbursements, we are still struggling with getting the customers back into the system. So, gold will be the other area of focus during this financial year. I think otherwise we have got a wraparound most issues and our view is we should get back to our AUM growth of about 20% during the next financial year and a better PAT growth than what you have seen during the financial year that has gone by.

I think largely I would have said what I wanted to, if Chandru has something, I request him to add, post which we will open ourselves up to questioning from anyone of you.

R. Chandrasekar: Yes, I think to add, we as usual in this financial year I think we have done much better than what we had budgeted during the beginning of the year. So, that is one and second thing during this course of the year we are able to maintain a good growth and going forward we feel our own core business, SME finance can still do much better. And Lakshmi was trying to say we will definitely improve on our personnel expense and Opex during the current year which we expect a budgeted 20 basis point dip during the next year. So, this year we have done much better than the budget and next year we feel that will be more, we are more bullish in the coming year and in spite of the fact that we have gone through this GST, demonetization all this when we budgeted last year we are not factoring for all the things. In spite of all these things we are able to do have a reasonably very good financial year and next year we expect much better yield during 2018-2019.

Lakshmi Narasimhan: So Nikhil, we now open ourselves up to questions.

Moderator: Thank you. Ladies and gentlemen, we will now begin the question and answer session. We will take the first question from the line of Viral Shah from Credit Suisse. Please go ahead.

Sunil Tirumalai: This is Sunil Tirumalai from Credit Suisse. Sir, had a few questions. Firstly in the presentation you, very explicitly given the target of going back to your 18% to 20% ROE standing where you are at 11%-12% ROE, I mean I just wanted to kind of understand what are the various drivers that will help you get there between margins, Opex I think you have given a credit cost reduction of about 100 basis points will help to some extent but what else on margins and Opex you think will help?

Lakshmi Narasimhan: I think the road map for the 18% to 20% ROE Sunil, as you are rightly saying needs to move up from the existing levels. If you see between last year and this year we have moved up about 100-150 basis points, as we head into next year it should be far better than what it is that you have seen out here. I think the levers are quite clear. I mentioned one of them very clearly in terms of the Opex being ad-hoc item which we should drop. We have to stride close to about 25-30 basis points drop during the next financial year in terms of OPEX. So, that could be a contributor to the overall entries in the ROE and ROA. The second piece is the credit cost getting to its normalized levels of about 3 odd percent. I am saying 10-15 basis points this side that side is what I think it will end at. So, even if you think that it is going to drop to 3.1 that is a 100 basis points drop from the existing place. The third place where I mentioned on the call is also the fact that the cost of funds is expected to hold or maximum about 10 basis points is what we expected to go up by. So, barring these 3, I am not seeing the spread going ahead increasing from here on. In fact, the spread is something that we guided about 2 or 3 quarters back that we would expect the spread to compress considering the competition that we are seeing in the market. So, the claw-back and the drop and the spread have to come back from the 3 items that I have just now mentioned. So, the ROE should track up towards the 2018-2020 over a period of next 2 years, Sunil.

Sunil Tirumalai: I noticed in your detail presentation now. Your SME, you are talking about 3 to 5 years of tenure. I remember it used to be quite shorter earlier about 2 years or less. Was there a change in the product construct that happened over time or did I miss something?

Lakshmi Narasimhan: No, I think there is no significant change in the way that the SME business is being done or the content of the SME business as far as we guys are concerned but remains the same as it was in the past as well. Some part of the business that we do which is completely based on the financial underwriting. That contribution is now increasing a little bit or otherwise I do not think the content of the composition of the SME business has changed over a period of last 2-3 years any different than what it was in the past. So, the tenure when we say 36 to 60 I believe what we are saying is that is the door to door tenure that you are seeing and there is no change it is just that since we have started now disclosing all this it is best to give what are the bands in which we are operating rather than get on to a specific number that this is the actual tenure for each contract. It is more a band that we are mentioning over here otherwise the business is not changed neither the competition or the business.

Sunil Tirumalai: And finally looking at your borrowing mix overtime your share of retail deposit has been coming down in NCD have been going up, I mean can you just broadly give an idea of in each of these 3 main buckets from banks, term loans, retail deposits and NCDs what are your borrowing cost right now and what is the thinking behind how they should move, the mix should move in future, thank you.

Lakshmi Narasimhan: As far as the mix is concerned as we have put out 44% of our borrowings as on March 2018 was fixed. The semi fixed was 47 which means if you come up for revision probably once a year and then 9% of the borrowing is completely floating. There is no change as far as that is concerned. Coming to your public deposit related question, now this has obviously been dropping over the past few years. But this is something that we should budget for as an item that we continue to remain in SCUF's books or even in the groups books considering the vintage the type of depositors that we have been having in the system. So, we would expect that to be anything between the 18%-20% level as we kind of head to the next financial year as well. PAT comes in at a price which is about anything like a 40 to 60 basis point higher than the regular cost of borrowing that we have which is very consciously priced at that considering the vintage of the depositors that we have with us. I am saying this kind of gives you of band in terms of the borrowing costs. If you look at the NCDs with a weighted tenure of about 30-32 months we would have been the range of Sunil anything between 8 and 8 quarter. But sub 8 some of the borrowings did you have sub 8 as well or it is good to presume that it will be 8-8 quarter. The term loans that we pick up again has a tenure of close to about 36 month there the weighted cost is somewhere around 8 quarter 8 half, rest are the CPs and CCs so on so forth. So the weighted cost of borrowing is what you are seeing is close to about 7.73.

Moderator: Thank you. The next question is from the line of Nidhesh Jain from Investec. Please go ahead.

Nidhesh Jain: Can you just share the gross NPA number on 90-day basis for last quarter and Q4 FY17?

Lakshmi Narasimhan: Gross NPA numbers for the last quarter you are saying product wise?

Nidhesh Jain: No, just on a headline number on 90-day basis.

Lakshmi Narasimhan: On 90-days what we have published and so that is 9% right, if you kind of get to the slide in which we are mentioned that you will see that. For just about the number it is about 9% GNPA as of March 2018 as an organization.

Nidhesh Jain: And for Q3 FY18, same number?

Lakshmi Narasimhan: I think Q3 or you want the Q3 FY18 numbers?

Nidhesh Jain: Yes.

Lakshmi Narasimhan: I think Jai will mail that out to you.

Nidhesh Jain: Sir, just wanted to understand the trend of this GNPA on 90-day basis how do you see this moving ahead? Do you think that it will remain at 9% or there is a possibility of this going substantially down from these levels?

Lakshmi Narasimhan: No, certainly it will not remain in the 9% level. The question is how quickly it will come down to the levels of about 8 odd percentage. Let me tell you what we are doing on that. See as I kind of mention at the start of the call that we have now put a sourcing mechanism which is uniform across the country and which falls into a specific pattern of underwriting for the SME business that we were doing or we having to put this into place we had more of different small centers of excellence in terms of branch managers underwriting it the way that thought it appropriate. But now since we have a uniform process I guess that should contribute to overall improvement in the portfolio quality of this small and medium enterprise business which is 56% of the loan book as we speak. So that is clearly indicated in the fact that the business that we underwrote during the last financial year which is April 2017-March 2018. When we compare it on any parameter to the business that was done prior to that for a comparable period is behaving really superior to what we saw in the past and such business which has been underwritten through this process is now close to 20% of the loan book. So, assume that we kind of maintain the percentage on which I have no doubt, we would be ending up a close to 35%-40% of the loan book coming into that process as we head March 2019. So the reason for the drop in the NPA is good enough for us to kind of think that it should drop to less than 9 considering the improvement in the process of underwriting of the small and medium enterprise business. So 9 is not the new normal. We should be sub 9 as we kind of head into next financial year and drop it further as we kind of go ahead.

Nidhesh Jain: Because the number that I have for 90 DPD last year is around 8.6%. So is it reasonable to expect that on a Y-o-Y basis or 90-day basis there is a slight deterioration in gross NPA despite these initiatives or my last year number is not correct, 8.6% GBP.

Lakshmi Narasimhan: I actually do not have your 8.6 is with me but I guess you are not way off the mark. So, an 8.67 to 9 there is about a 30-basis point difference between last year and this year. But I think I would suggest that we track some year on in terms of where do we head from the existing 9% and 9 in any case an organization if you look at SME actually the 9% is 9.68 for March 2018. We had virtually guided about 9 quarter at the end of Q2 as being the ideal number for March 2018, I think we are quite well within that guidance, yes.

Nidhesh Jain: You mentioned because of competition there could be some pressure on spreads and yields. So, in which segment are we seeing competition among the four products that we are operating, 5 products that we are operating in.

Lakshmi Narasimhan: We see it coming in both in 2-wheeler and the small and medium enterprise business which roughly is about 75% of the loan book.

Nidhesh Jain: And sir, with respect to longevity of the book, do you see that longevity of the book has slightly improved probably because of the share of MSME is going up or with in MSME the share of large ticket loans going up. Is that the reason for longevity of the book going up because we notice that disbursement growth is slightly muted despite that the NIM book growth is quite strong.

Lakshmi Narasimhan: So vintage has virtually gone up in 3 products, I mean marginally in 2 wheeler from the regular 19 odd months to 20-21 months. The personal loan business has gone from 18 to 19 months or in fact 20 months in some territory as well and the small and medium enterprises obviously the tenors are tracking up. In all the 3 products we are seeing the tenor tracking up slightly as a function of which you are seeing the AUM growth being slightly disproportionate to the disbursement growth.

Nidhesh Jain: And sir, just lastly what's share of our NIM book in MSE coming from high ticket size loan expecting all about?

Lakshmi Narasimhan: That still remains in the, I think in the region of about 8%-10% is what that remain still.

Nidhesh Jain: 8% of MSME loan book?

Lakshmi Narasimhan: That is right.

Moderator: Thank you. The next question is from the line of Rahil Shah from Ambit Capital. Please go ahead.

Pankaj: This is Pankaj here. Sir, you guided for 3% credit cost going forward. But if I look at your historical credit cost it used to be in the range of 2.5 to 2.9 even during the times when gold loans used to be closer to 30%-40% of your loan book where I understand the credit cost is below 100 basis point. So, now given that gold loan proportion is coming down plus even auto loan proportion is coming down plus your SME plus personal loan proportion is going up. Do not you think managing credit cost below 3% would be difficult for you?

Lakshmi Narasimhan: I am happy with the question, it is certainly not easy. But what we are clear about is the fact that the underwriting has been done during the last, last year and a half is behaving better than what it was in the past in terms of the book that we constructed prior to that. As a consequence of which I said we will come back to our regular 3-3.1 levels. So, while gold was a good contributor to the fact of the underwriting quality remaining better during the past, but in the last 3-4 years Pankaj you are saying that the gold quantum was deteriorating from the peak of about 35%-40% to now close to about 12%-13%. So, if you slice the credit cost as a function of provision related and write offs related, write-off is just largely still in the region of about

2.4%-2.7% and it is only the provisioning that has caused the credit cost to look higher. Now since we have moved to the 90 plus in the provisioning related contribution to the LGD stabilizing. I think we are fairly clear on our road map in terms of restricting the credit cost to the 3% levels.

Pankaj: And sir coming back to your growth guidance if I look at your gold loan business plus your auto loan business both are kind of not growing or kind of de-growing and both of them contribute 20% of AUM. Now, to achieve more than 20% AUM growth clearly will need to grow more than 25% in remaining segment and I am assuming that these 2 segments will not grow at a very high pace. If I look at the industry nobody is growing in gold loans, I mean even your competitors, right. So and specially we know that two-wheelers are very volatile. There are years when you grow 30%, there are years when you hardly grow 10%, right. In such a scenario, I mean 20% consistent AUM growth is achievable? Because my sense is that it has to come from SME loans. I do not think there is any other segment which can consistently give that kind of growth.

Lakshmi Narasimhan: The SME as you rightly mention would be the largest contributor to the growth and obviously that book has to grow at beyond 20% assuming it still remains about 56%-60% the loan book as we kind of go forward. So, SME will be a good contributor. There is another segment, Pankaj which we are seeing a good amount of traction is the personal loan segment and the good stuff that we have done during the last year is to put a terrific cross-sell model in place and last year of the close to 2,000 crores worth of personal loan that we underwrote. 50%-55% of that loan book is a function of cross-sell which was not an existence prior to this. So, that does 2 things. One it drops the Opex on the quantum of cross-sell that we do because there the acquisition cost is virtually zero. And two is the credit cost that personal loan used to incur is likely to drop as we kind of go forward which will be the other reason for the normalized credit cost in the organization reaching to the 3%-3.1% levels. So, personal loan will grow beyond that 20% AUM growth that we are said for the next financial year Pankaj, as also the SME business. In two-wheeler, I agree with you, the head way for us to growth will be covering most of the eastern territories in which we have a very thin presence. And as and when the finance penetration in the business increases as we have seen in UP over a period of last 3 years that is grown up from 14 odd percent to 18 odd percent. So, with we being densely populated in UP and reasonably sure if the finance penetration of their increases then your growth will get back to your regular levels. But I think a 20%-21% growth in two-wheelers is not beyond us. And I mention gold as a specific item of focus as we kind of head into the next financial year. So, we need to see, we need to work more what should I say appropriately on the ground get the gold business of the track from the existing place of a de-growth. At least we should not allow a de-growth even in comparison to the last year's numbers.

Pankaj: But sir this weakness in gold loan is it because of the requirement of cash disbursals or there is some kind of cannibalization happening here from unsecured personal loans? Because even banks who do not do cash disbursals even they are struggling to grow gold loan book.

Lakshmi Narasimhan: It is a mix of both and there is a third piece**,** there is a mindset issue that has got set into people at different levels within the organization in terms of it being a regulatory risk in terms of continuing to do gold business the way it was being done. So it is, Pankaj contributed a good amount by the cash disbursement of related piece. The second piece is I agree that there is a movement of the gold loan customers to the personal loan segment - even in my books I am seeing that. So the third piece is in spite of all that there is something that we can do at least to ensure that no de-growth happen. Those are the 3 things that we are focused on, yes.

Pankaj: And sir finally on your Opex ratios right, what I understand is that in gold loans most of the operating expenses are fixed in nature. I mean if I look at Muthoot, Manappuram roughly 90% of the Opex is fixed in nature, right. Now, given that your gold loan business is kind of and I am assuming that it will remain flat or probably come down, right. There you might lose some basis point on Opex side. So, even if you improve your Opex ratio in SME, if your gold loan business continues to decline do not you think that will offset whatever gains you make on SME side? Gold loans because whatever do, whether you do one loan from a branch or 100 loan from a branch, right. The number of people you need number of, kind of infra you need that will not change irrespective of number of loans you do from a branch.

Lakshmi Narasimhan: I agree that the gold loan cost is baked in and there is not too much of a change that you can do as far as the gold loan cost is concerned except that as a percentage it can be looked better. If you have gold loan business stabilizes or even grows from the existing levels. And that is why I kind of put out a conservative number in terms of a 20-30 basis points drop in the Opex as we kind of go forward. I am not at this point in time looking at too much of a claw-back on the Opex but I will be very happy if you stabilize and drop it a little bit. So 20-30 basis points, Pankaj can come in even by reduction of the bench strength of 1,500 odd people that we are carrying.

Moderator: Thank you. The next question is from the line of Jignesh Sahil from Emkay Global. Please go ahead.

Jignesh Sahil: Firstly, can I get the interest reversal number for this quarter as well as for the full year due to this shift in 90-days DPD?

Lakshmi Narasimhan: All in fact was come in only in this quarter and that close to 29.5 crores.

Jignesh Sahil: And if I see second, one more data-keeping question. Can I get your on book and off book break up of AUM**;** is it possible on balance sheet and off balance sheet? Of your AUM

Lakshmi Narasimhan: Just about 0.35%-0.4% which is off book, yes.

Jignesh Sahil: Now, coming back to the same question that has been raised earlier on the yield side. I am assuming that the cost of funds is supposed to be either remaining stagnant or probably will see an upside. So, how basically the NIM should be sustainable constraint, MSME is seeing a bit of, is becoming a little crowded space overall because most of even private banks are focusing on this particular segment. So, any specific strategy or any specific areas that you want to highlight especially in the yield side as well as on the margin front. But how you will be able to cope up with a better margins or the superior margin profile in the coming quarters in the coming year?

Lakshmi Narasimhan: Yes, as far as the yield is concerned as I said in this call as well as during my individual meetings with different investors, we have been saying that the yield definitely is compressing and as we head into the next financial year, for example, for the year was 20.09 or 20.1 and Q4 standalone was about 18.59 or 18.6. Q4 need not be the bench mark as we kind of head into the next year considering the income reversal completely came in Q4 and also the business that you book in the month of March starts earning from the next financial year. Having said that there is a yield drop that we have seen in the SME business and which I expect will continue into the next financial year. So a 50-60 basis points drop from the existing 20.1% levels is something that we thing will happen as we head into the next financial year in terms of the yields. Our question is where the claw-back is going to come from to compensate for this 50-60 basis points drop as we head into the next financial year. I said 20-30 basis points coming in from the OPEX. The credit cost will drop and more of cross-sell is the intention which we do in the personal loan segment. There will be a good amount of claw back in terms of the 50-60 basis points that we have seen the yield is dropping. I am not saying that the yield is holding or the yield is dropping.

Jignesh Sahil: So, if I see exactly the same way, I am also seeing it up. So, considering that if I assume that your ROAs which is around the range of 2.5 right now is suppose we are seeing bit of a momentum. So, by 10 or 20 bp because most of your credit cost advantage or even your OPEX advantage is might come up is getting off set by your drop-in margins. So, in that case how exactly you are seeing it that your ROE territory would be back to 18% sort of level because with 5 or even 5.5 times sort of leverage because in good terms you used to make it 7-7.5. So are you seeing a leverage moving up which basically bringing your ROE up or is there any other strategy to move up your ROAs in general?

Lakshmi Narasimhan: I think Sunil asked that question in terms of the ROE for the next financial year and the year after. Then we guided 18% to 20% and I am kind of going to say that again because 18% to 20% is over a period of next 2 years as what we will get to. The first step is to climb on the existing level of 12.7%-13% levels to close to about 15%-odd during the next financial year. I think we are seeing that happening during the next financial year and then getting on to the 18%-20% the year after the next, is what is the guidance that we wish to put out on the table. As we kind of grow go forward with a 20%-25% loan book growth, the leverage will obviously start increasing except that the accrual is also adding to your net worth of close to about 700-odd crores we are seeing this year and next year again there will be some addition to that. Looking at it from that perspective leverage will increase but we are looking at very clearly that the organic growth is the clear route to get to the regular ROE levels and there is no other stuff that we have in mind at this point in time.

Moderator: Thank you. The next question is from the line of Piran Engineer from Motilal Oswal. Please go ahead.

Piran Engineer: Sir, my first question is on your MSME segment, firstly our disbursement this quarter was quite strong, our last 8-10 quarters we are in that 2,400 crores-2,500 crores range and this time it is come in more than 3,000 crores. So, firstly was there some undisbursed pipeline from the prior quarters that has flown in this quarter?

Lakshmi Narasimhan: Are you saying decline in the sense it was an accrued deal which got disbursed …

Piran Engineer: Yes, sanctioned in the prior quarters but it is floated-in in this quarter?

Lakshmi Narasimhan: That happens in each quarter.

Piran Engineer: Is it something unusual?

Lakshmi Narasimhan: No, nothing unusual.

Piran Engineer: So, can we expect this kind of a quarterly run rate?

Lakshmi Narasimhan: As we kind of go forward?

Piran Engineer: Yes.

Lakshmi Narasimhan: Yes, if I need to grow my overall loan book at 20% which is what I am guiding and SME is a 56% contributor, we should see SME business growing slightly higher than 20. So, whether I will do 3,000 crores, 3,500-2,900 is something which will kind of happen as we head into the next financial year. But we are seeing a growth in the SME segment as we kind of go forward.

Piran Engineer: And is this geography specific or broadly across places?

Lakshmi Narasimhan: No, it is still skewed in the South which is what our presentation also tells you that close to 67% of the SME loan book comes from the South but that has been dropping from the 75%-70% levels to 67%. So, the growth as a percentage will obviously be higher in the non-South markets. But as a contributor to the SME book it would remain South even during the next financial year in a big manner or as we kind of head towards the future. In terms of the other geographies then I am sure that contribution will drop. But at this point in time we are seeing growth coming in all over, it just that the South is the largest contributor to the kitty.

Piran Engineer: And sir, just to kind of going back on some of the prior questions on whether you all have increased your tenure of MSME loan. I have just notice that over the last 2 years repayment rate in MSME financing has gone down pretty sharply and is this due to you all giving out longer term loans then thus annual repayment is lower or because even the repayment rate this quarter was down quite a lot versus 4Q of last year or 4Q of any other year?

Lakshmi Narasimhan: Yes, so the tenure definitely is higher than what it was in the past years. And obviously you are right if the tenure is higher your repayment has to be lower than what it was in the past. We are seeing the tenure is going up.

Piran Engineer: But that is not significantly but I think you said it went up only 1 or 2 months?

Lakshmi Narasimhan: On a growing book of 20% with 1 or 2 months.

Piran Engineer: And sir, my last question is on the housing finance subsidiary. There also after quite a few quarters of subdued growth, we saw big pick up in disbursement so anything noteworthy to mention because asset quality really has not improved much and I thought our first priority was to improve the asset quality before going of strong so any comments there would be helpful.

Lakshmi Narasimhan: Yes, we had, when we kind of met you all in the past 2 quarters, mentioned that we need to get our strategy on the housing finance better than what we have done thus far. Just to just kind of put things in perspective, the asset quality on the gross NPA has drop from 5.8% to 5% during the quarter. And as far as the full year is concerned, it remains at the 5% levels but as we kind of go into the next financial year that should look better. The disbursements have definitely picked up as far as the housing finance business is concerned and we are seeing traction on the retail side more because we got our basic right in the market than the market itself is looking up. And we are too small at this point in time to look at market as being a driver for the growth. So, hopefully this is the performance or better than this is what we will start reflecting as we kind of head into the next financial year.

Piran Engineer: So, what was the disbursements in construction finance for the quarter?

Lakshmi Narasimhan: We disbursed Rs. 4.4 crores in construction finance during Quarter 4. 2018.

Moderator: Thank you. The next question is in the line of Karthik Chellappa from Buena Vista Fund Management. Please go ahead.

Karthik Chellappa: On the pricing pressure that you spoke of in SME, which are all the geographies where this is probably little more aggressively manifesting and is it also a factor of we getting into higher ticket sizes where the pricing is a big tighter than what we used to have in the past?

Lakshmi Narasimhan: See, on the pricing Karthik not all markets operate the same rate as you will appreciate and you will be well aware of as well. So, when we see the yield drop even a specific territory say for example, I am operating at 24% there the yield drops to 23% and in some other territory where I am operating a 23% it drops to 22%. So, we are seeing the yield drop across the country at different levels from the levels at which we were operating prior to the drop. That is one specific reason. Second is we mentioned earlier in the call that the high-ticket SME segment which is underwritten completely on the basis of financials, has contributed more than what it used to and that book has grown that is another reason why the overall yield in the SME book has dropped. And the third piece is obviously the income write-back that we have had during the quarter 4 which is also contributed to the overall drop in the yield.

Karthik Chellappa: Now this yield drop is that because of competition from say some of the newer NBFCs getting into the business or is it primarily coming from banks?

Lakshmi Narasimhan: So, for this segment it is not as much the regular banks. Small finance banks I would still consider as being part of the NBFC space. So, we have competitions from the small finance banks. We also need to appreciate the fact that having run close to about 4-5 cycles of SME business, the existing customer’s appetite is not met appropriately by the organization from within. Those customers will perforce migrate to competition, which is something which we are consciously working on avoiding. So, the other reason for the drop in the yield is also the function of an existing customer performance being recognized through a lower price at which we were lending to him.

Karthik Chellappa: Similarly, in two-wheeler are you seeing the pricing pressure mainly coming from say some of the captive financier is being aggressive or is it because of some of the NBFCs being aggressive?

Lakshmi Narasimhan: No it is more to do with the capital financiers.

Karthik Chellappa: Sir, my next question is if we look at our write-off, our historical write-off has ranged between 2.1 let say to 2.2 or so. FY18 because of demonetization and GST saw that raised to about 2.5. Now, when we have an overall guidance of around 2.75 to 3 can we assume that these write-offs still slowly start reversing back to a 2.2 or 2.3 level or it is 2.5 going to be the new normal for write-offs alone?

Lakshmi Narasimhan: I think we will kind of stick to the fact of the overall credit cost being 3-3.1. I will be happy to kind of work towards the write-off getting back to its regular levels of 2.1-2.2. But at this point in time our own thought tells us that we will be in the 2.5% levels during the next financial year. Hopefully, we should be able to drop it as we kind of go forward because the mix of business is still just about 20% coming in through the new process. But more of the new process related deals occupying the loan book, will ensure that we come back to our regular levels of about 2.1 to 2.2.

Moderator: Thank you. The next question is from the line of Digant Haria from Antique Stock Broking. Please go ahead.

Digant Haria: I have just one question, so much was asked on growth and OPEX and margins in this, internally what do we think about the ROA targets because we used to be at 3%+ in the past those last 3 years we came down to like 2.6%. So, should we be able to go back to 3% considering the tradeoff which we have in terms of lower margins but better OPEX and better credit cost? Is 3% a good number to work with?

Lakshmi Narasimhan: Yes, 3% is a very good number to work with.

Moderator: Thank you. The next question is from the line of Deepak Poddar from Sapphire Capital. Please go ahead.

Deepak Poddar: Sir, my first question pertains to your PCR, basically quarter-on-quarter I think our PCR has dropped from 74% to 62%. So, any thought process that where in terms of PCR?

Lakshmi Narasimhan: I think we will continue to remain in the band of that 60%-65% which is what we had guided as well in the past. So, 60%-65% is the band in which we should presume we will remain.

Deepak Poddar: So, we are looking to maintain this 60%-65% kind of going forward as well?

Lakshmi Narasimhan: That is right.

Deepak Poddar: And in this quarter our provision was close to about Rs. 410 crores whereas around Rs. 140 crores was on account of this transition from 120 to 190-days, right?

Lakshmi Narasimhan: Yes.

Deepak Poddar: So, remaining Rs. 270 crores still on a quarter-on-quarter basis is about 30%-40% higher in terms of provision. So, any light on that what led to this?

Lakshmi Narasimhan: So, that is the reality. Like in the sense, I have to just kind of get back to the same point. Once the mix of the new process of underwriting business occupies more space in the loan book then all this stuff get address automatically.

Deepak Poddar: So sir, this provision is a natural increase in NPA basically like even if you would have at 120 days, our NPA would have increase from 6.8% to what level like at 120 days?

Lakshmi Narasimhan: I do not have that number and I request we now track 90+ as we kind of go forward very clearly from here on. Mentally, we and the team have moved to 90+ now.

Moderator: Thank you. The next question is from the line of Varun Goenka from Reliance Capital. Please go ahead.

Varun Goenka: Yes, my question is regarding the MSME AUM. I wanted to understand what is the average ticket size over the last 3 years and what can be the change in volume and value growth in this average ticket size?

Lakshmi Narasimhan: See the average ticket size of the SME remains in the 800,000 to 10,00,000 range and that has been so for quite a while now that was not changed. In fact, in some markets when I kind of look at plain and simple the retail business in some market the ticket size has dropped during the last financial year. In some markets it has stabilized and some market it is gone up. So, the ticket size remains in the 8,00,000 to 10,00,000 as far as the SME segment is concerned.

Varun Goenka: So, the growth that you are talking about may be 25% to 30% in this segment, are you looking it more from value growth from existing customers or additional customers? I want just a broad outlook over the next 3-5 years, how will the throughput with existing customers increase and growth from new customers?

Lakshmi Narasimhan: I will tell you until our customer really completes a good part of the cycle of the first loan, there is no question of him coming in as a repeat customer with us. Unless stage 1 we assessed him or say about 20 lakh of loan and we only went ahead giving him 800,000-10,00,000 at that point in time and is still have a 12 lakh limit sort of accrual available, we may kind of give him but those are very few and far cases. So, the existing customers contributing will essentially require him to complete a full cycle with us. The contribution of the existing customers as we speak in the SME loan book is anything between 15% and 20% from different market. So, the growth that we aspire to have during the financial year as we have entered the new one will essentially coming from new acquisitions not from the existing set of customers, if that kind of answers your question.

Varun Goenka: Just a continuation to that you have around 1,000 branches. What is the concentration of MSME AUM in these branches let say 80:20 ratio in the branch distribution? I am trying to get a sense of the runway?

Lakshmi Narasimhan: Around 335 branches occupies close to 90% of the business that we do. To give you a perspective out of the 960-970 branches that SCUF has on paper close to 700 branches we run the SME business. Out of these 770-800 odd SME branches 330-340 branches contributes 90% of the loan book.

Varun Goenka: So, would you say the balance branches is work-in-progress for the MSME part?

Lakshmi Narasimhan: Yes, the balance branches needs to start firing.

Moderator: Thank you. The next question is from the line of Rishendra Goswami from Locus Investments. Please go ahead.

Rishendra Goswami: Just quick questions. One is on the PL GNPA, so what kind of recovery do you see in case of personal loan default?

Lakshmi Narasimhan: Recovery as in, can you be little clearer?

Rishendra Goswami: Yes, I was trying to understand of the personal loan GNPA, are you able to do you get some recoveries out of that or given that it is an unsecured loan?

Lakshmi Narasimhan: See, if you kind of break up the personal loan into 3 different segments, okay. One is the salaried, one is the self-employed, and one is the existing customer. When I said existing customer, the cross-sell that we do. So, the salaried customer produces the best returns after a customer becomes an NPA. From different perspectives including certain legal actions that you may take against the customer. In the self-employed segment the recovery is lower than what it is for the salaried and the existing customer, in any case below or into the NPA bucket is extremely low and where the customer spills over, we again break it up in the salaried, self-employed so and so forth. So, broadly I think close to 60%-65% of the personal loan segment would be the salaried customers and 35%-45% would be the self-employed customers in the book. And the recovery levels are according to just what I mentioned to you.

Rishendra Goswami: But just to get a sense on the overall book, is the recovery 10%-20% is it higher than that?

Lakshmi Narasimhan: After a customer becomes an NPA?

Rishendra Goswami: Yes for the PL.

Lakshmi Narasimhan: So, I think NPA is 90-days today. So, I am just saying the recovery from an NPA book will in any case be close to 50%-60%. The question is recovery from the write-off bucket how much is that going to be? The recovery from the write-off bucket varies depends upon which territory, how much of pipeline we have created, what is the legal movements so on and so forth. Recovery movement of in and out of the NPA is pretty robust.

Rishendra Goswami: And generally, so just to understand then the recovery at what point in time do you take the write-off on a PL?

Lakshmi Narasimhan: See, on a PL the moment I reach a 100% threshold in terms of provisioning it is a write-off. But that write-off is technical in nature more in the books than to the business teams. The business teams' assessment or the collection effort continues on the book irrespective.

Rishendra Goswami: So, typically the loan becomes NPA in 90-days so you would be usually writing it off what in 6 months or a 1 year period?

Lakshmi Narasimhan: I think in about a year after it becomes an NPA is when it gets to the close to that 80% provisioning levels.

Moderator: Thank you. We will move on to the next that is from the line of Ritika Dua from Elara Capital. Please go ahead.

Ritika Dua: So firstly, can I understand what is your sense on the gold loan business is it more regulatory issue or is it also a matter of demand which is otherwise the factors on the macro side for the gold to pick up seems to be like doing fine. And the second question is that I have heard during the call that you have been sharing structural changes in the way you are I think may be underwriting and also sourcing SME, if you can just share some thoughts on that?

Lakshmi Narasimhan: As far as the gold is concerned we mentioned that it is partly to do with the fact of the cash disbursement related restrictions coming in and partly to do with the fact of something internal to us in terms of getting things right and I think that is what we said we will focus on as we kind of head into the next financial year. As far as the new underwriting norm is concerned, while it is a broad topic what I wish to tell you is we have implemented that process now across the country for the entire retail part of the SME meaning 100% of the retail part of the SME comes in through that process. And the business acquired through such process now occupies close to 20% in the existing loan look of SME that we have, and it is at this point in time producing results better than what we kind of targeted as we kind of went in. And comparison of all types of delinquencies whether it is zero or one bucket or second bucket or the hard bucket. all that is behaving better than similar vintage portfolio that was created prior to the implementation of the existing underwriting process.

Ritika Dua: Sir, is it more to do with like may be change in the underwriting tools or is it more to do with the ticket size or the kind of the segments we wanted, some color on that sir. If you can you just explain then that also will help me.

Lakshmi Narasimhan: I think single biggest contributor to be improvement in the overall quality is the fact of strictly putting the customer to scrutiny on the purpose of the loan. So, while earlier the purpose of the loan was a question that was being asked by the team while it was more like someone discerned it in some manner and then get the underwriting. The uniform process which has been implemented across the country now enables us get an appropriate answer on the purpose of the loan. So, you have got everything going to yourself and the loan sought is say Rs. 100 while the purpose of the loan takes us to a place of 80 and what you get is 80 not 100. I think that is a single largest contributor to the fact of improvement in the overall quality.

Ritika Dua: And sir on the gold, can I just may be conclude that you are saying it is still more regulatory that means at least on the demand side at least the demand has definitely improved as it is more regulatory. So, that is something which we can conclude?

Lakshmi Narasimhan: So, since you kind of joined a little late, there was another reason which we kind of understood and agreed as well that the personal loan book growing for different entities is also a function of some part of the gold loan customers moving into the personal loan segment. So, regulatory movement of customers to an easier personal loan and the fact of internals that we have.

Ritika Dua: And this is not just for you sir, this is you are more saying it from an industry-wise perspective.

Lakshmi Narasimhan: I guess at least in the 5 states where I run this business, my reference is made of this fact.

Moderator: Thank you. The next question is from the line of Parneet Virk from IIFL. Please go ahead.

Abhishek: This is Abhishek. Just wanted to get a sort of breakup of the SME book between the portfolio that is run by Mr. Subramanian and the rest of the book and also if you could break up the NPA between these 2 parts of the SME book?

Lakshmi Narasimhan: So, we will need to come back to you on both, not offhand. I do not think we put this out publicly but let me see if I can send it yourself.

Moderator: Thank you. The next question is from the line of Nischint Chawathe from Kotak Securities. Please go ahead.

Nischint Chawathe: Just one thing I wanted to check was on the loan sell-down side. This number has been kind of coming down, so is it something that the potential for securitization is gone down or how should we think about this?

Lakshmi Narasimhan: So, I think Nischint, couple of things has happened on that. One is the spread cap is a definite deterrent for enterprises like me to sell this in the market. It should be more than 8% of the base rate of the bank which is kind of wanting to buy the book. So, which means, if I if the base rate is say 8% then my underlying yield should not be more than 16%. So, I think that is one of the biggest deterrent as far as my sell-down is concerned. The second piece is during the last year the norms for acquiring the priority sector book have also changed to certain strenuous stuffs like auditor certificate of the entire asset book of the customer right from origination to the present date as to qualifying for priority sector loan, tagging, etc. So I think the conditions of sale is also become onerous and I am speaking purely of securitization and I am not speaking on direct assignment. PSL certificate is another contributor to the lower volume in the market. So, I read a report of CRISIL and ICRA which said that the securitization book has not come down in the market but for entity like me this are the 3 reasons which has contributed to the lower sell-down that we plan. And in any case we have equity which is pretty high, so the drive to kind of bring that down is lesser even though the cost of fund advantage may be little more than what we get otherwise.

Nischint Chawathe: So, what you seem to be guiding is that this particular number will remain low or possibly reduce itself?

Lakshmi Narasimhan: That is right.

Nischint Chawathe: And bilateral?

Lakshmi Narasimhan: Bilateral is something we have done a little bit but we have not gone ahead with that. In the plan for the next year, there is very small numbers that we have for that as well when I said that the cost of fund is expected to stabilize that existing levels of possibly go up marginally. There is a very small amount that we have put into the bilateral segment as well. But there is appetite in the market for that.

Nischint Chawathe: Just one last question was any guidance that you could give on the Opex ratios and how they would trend down would you be investing more, so does next year remain higher Opex and then it comes down or any color, any trend on that?

Lakshmi Narasimhan: We have made investments in technology to improve productivity. So, that should take shape number one. Number two, is what will really happen Nischint is where I mention that 700+ branches to 330 branches in terms of the SME contribution the throughputs on the branch will increase once I get a little aggressive in running the SME business in the balance number of branches. So, the cost will get defrayed over a higher base. And the third piece is the bench strength that we are carrying about 1,500 people is something that we need to think and reduce. These are the 3 contributors to the overall reduction in the Opex. I think it will be good to kind of work towards a 20-30 basis points drop as we head into the financial year.

Nischint Chawathe: And you will be cutting branches as well?

Lakshmi Narasimhan: No, not cutting branches, improving productivity as also looking at this 1,500 excess people that we are carrying to drop over a period of time. Branches will remain the same or if at all it will only go up.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. Nikhil Walecha for his closing comments.

Nikhil Walecha: On behalf of JM Financial, I would like to thank the senior management team of Shriram City Union Finance and all the participants for joining us on the call today. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of JM Financial, that concludes today's conference. Thank you for joining us and you may now disconnect your lines. Thank you.