"Shriram City Union Finance Limited
Q2 FY2019 Earnings Conference Call

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Moderator: Good day ladies and gentlemen and a very warm welcome to the Shriram City Union Finance Limited Q2 FY2019 Earnings Conference Call hosted by Kotak Securities. As a reminder all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call please signal an operator by pressing "*"then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nischint Chawathe from Kotak Securities. Thank you and over to you Sir!

Nischint Chawathe: Hello everyone. Welcome to the Q2 FY2019 earnings conference call for Shriram City Union Finance. To discuss the financial performance of SCUF and to address your queries we have with us today Mr. V. Lakshmi Narasimhan, Executive Director and Head Investor Relations and Mr. Y.S. Chakravarti, Executive Director and Chief Operating Officer. I would now like to hand over the call to Lakshmi for his opening comments.

Lakshmi Narasimhan: Thanks so much Nischint and very good morning to each and everyone one of you who has joined the call. Thank you very much for joining the call. As Nischint just mentioned we have Mr. Chakravarti as well on the call. I think as an opening feedback a couple of items. We have seen post September a slight shift in the availability of money that did not truly affect too much of our volumes for the last quarter. If you look at the non-gold, we still grew at about 23% in terms of loan book and including gold we have grown at about 18%. Couple of items which I wish to highlight is the fact of our spreads going up pretty well during the last quarter that is the function of two things, one is we had stated earlier that we are increasing the lending rates in the market for certain segment of customers that is looking to tract up. The second piece is also the implementation of the Ind-AS as a function of which we have the processing fee amortization impact coming in, so these are two reasons why the spread has gone up. You will have also noticed from the presentation that the write-offs have dropped during the quarter. There is no change in the methodology of recognition of items for write-offs, so the policy remains the same and yet the write-off has dropped, as such a good development that we have seen. We have put up again Ind-AS and IGAAP numbers and as per IGAAP if you see the overall 90 plus book it is still under 9, so I think we are on track to get to a regular credit cost which normally hovers in the region of about 3% odd as per GAAP and as per Ind-AS as we have taken a position in the past we request each one of you to walk with us for the next two more quarters. When at the end of March we will be able to make a very reasonable estimate of what the ultimate credit cost will be. Hopefully GAAP and Ind-AS should shake hands at some point in time.

Largely I think that is where we are. We had guided for a three plus ROA for the year and close to 18% in terms of ROE as we go forward. Even this quarter if you see the ROA and the ROE has looked up and I think we are on track to get to that place. As we speak we are not yet altering the growth numbers of between 18% and 20%. Having said that it all is going to be a function of how the liquidity maps up during the next two months because at this point in time we have been able to draw the sanctioned lines but the fresh ones are taking a little longer than we estimated in terms of approvals. On the liability side, we have put out the ALM in this quarter and hopefully we will start putting that out each quarter, so that everybody at large gets a fix on where we sit as far as liabilities are concerned. If you see on a cumulative basis, we are plus and that is where we are. Those numbers are as September 30, 2018 and for October; the cash content has only gone up from the 1083 that we showed as of September 30, 2018. So largely I think we are on track to get to our numbers that we planned for the year barring anything getting tighter from here on in terms of liquidity. I kind of request Chaks to add a few lines of what he thinks is appropriate post which we could take questions from all of you.

Y.S. Chakravarti: Good morning all. This is Chakravarti. I think Lakshmi has given you a very brief and concise view of what has happened in the half year and what we are anticipating. I think we have performed reasonably well in the quarter. As far as our main products are concerned, SME during the month of last week of September and October, we have actually increased the pricing in ticket sizes beyond 25 lakh, so we anticipate a slight fall in the SME business in the sense, ticket size is up to 20, 25 lakhs we do not see any impact , but on the bigger ticket size we may see impact as we have increased the costing base, it is done consciously to discourage large ticket lending anyway which is not a core part of our business.

As far as two wheeler is concerned I think last quarter we have done reasonably well. We have done close to 300,000 two wheelers in the last quarter. Again in two wheeler as you must be reading all the reports, we have seen a slight slowdown towards the fourth week of September which is continuing in October month also. The dealers are sitting on lot of inventory, the dealers hope is that the last week of October and first week of November will probably make up for the numbers, but I personally anticipate a drop of about 20%, 25% on industry volume, sales volume of two wheeler. So I think this is basically because of two reasons. One is the confusion in insurance stabilized now, but the cost of the vehicle going up, customer having to almost pay double of down payment than what they were prepared earlier and to some extent also the rising fuel cost could have impacted this. We are in touch constantly with the dealers and the manufacturers are also meeting us on how this can be taken up. Again as far as gold is concerned, there is a slight growth in disbursement last quarter and this quarter as well, but there was also a pressure on redemption, so AUM has come down slightly, but we anticipate demand to pickup in the second quarter of the year and probably the AUM will stabilize.

Collections have been pretty robust in the quarter that has gone by and October so far we have seen a very good traction in the collection also, as a consequence the write-offs have reduced and we are confident that we will be able to maintain this momentum in collection for the next two quarters and be able to contain the write-offs at these levels. So what we are also doing is even we have involved every aspect of our organization including the sales team to focus on collection, so that the next six months we are very clear that our GNPAs will stabilize or probably will tract down and the write-offs, as I have already stated, we are confident that we will be able to contain the write-offs also at these levels. Now we are open for questions.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question and answer session. The next question is from the line of Piran Engineer from Motilal Oswal Securities. Please go ahead.

Piran Engineer: Congrats for the good numbers. I just had a couple of questions. First can you said you guided to a 20%, 25% drop in industry sales volumes, is that for Q3 or for a more prolonged period and also would this impact your customer segment more than the average industry?

Y.S. Chakravarti: What I said is for Q3 and no I do not think that we will be affected more than the industry in fact we should be…

Piran Engineer: Because your customer segment…

Y.S. Chakravarti: …Doing better than industry.

Piran Engineer: Why do you say that because your customer segment would be more price sensitive right?

Y.S. Chakravarti: In most of the places where I am funding, I am the only financier or probably one of two financiers who are available there and we also anticipate that some of the cash sales will get converted into finance sales.

Piran Engineer: Okay and our LTV are trending up in this scenario, the overall cost of so much in going up because we have been hearing reports that financiers…

Y.S. Chakravarti: No, we have not compromised on the LTV. We have stuck on – we are very clear that if you compromise on the LTV then your credit quality will suffer in a product like this, so we are very clear on the LTV side, so we do not anticipate too many issues on the LTV side as of now.

Piran Engineer: And ECL provisions for stage 1 and 2 have gone up a bit on a Y-o-Y basis like 50 bps or so, is there are some particular, can you attributed to something and where does it stabilize?

Lakshmi Narasimhan: I think it is a natural function of our learning on the Ind-AS so there is nothing specific to attribute to it, but I think stage 1 and stage 2 is a happy situation to be in.

Piran Engineer: Okay and just lastly on yields, we have been guiding for about some reduction in yields due to repricing for existing customers and you know overall yield pressure in general, so does that change now would this whole tightening liquidity situation, are we probably not reducing yields for existing customers or how should we basically model yields our margins going forward?

Lakshmi Narasimhan: See what we had been consistently saying is also the fact that wherever possible where we can pass on higher lending rate we have started doing that now, that is quite efficient for the last four, five months, so what is the key is a function of those incremental rates. I think yield as we go forward should stabilize at these levels. I do not expect it to drop dramatically from here on, even though we had guided for close to 40-basis points drop from 20.1% that we were as of March 2018. So many things we did not visualize including the fact of the impact of the incremental lending rates in the market. So I think if you are modeling on yield my own request would be to keep it at current levels then whatever we get over and above this is a bonus that you carry on.

Piran Engineer: I understood that is good to hear. Okay, thank you and all the best.

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

Karthik Chellappa: Thank you very much for the opportunity Sir. My first question is if I look at our MSME breakup south which is about 65% in the June quarter has dropped for about 60% odd that would imply that the MSME AUM in the south actually declined what would you attribute that too?

Y.S. Chakravarti: I will attribute it to growth in the west Karthik; also there is a closure of about Rs.500 Crores loan in south. Do you remember we have…?

Karthik Chellappa: A big ticket loan which has actually closed in?

Y.S. Chakravarti: Exactly a loan to SVL which was supposed to close in 2020, but which we have requested them to close it and they have closed it in September. So straightaway our Rs.500 Crores minus on the AUM there.

Karthik Chellappa: Okay apart from that there has been no other geographies or anything where you have either withdrawn or gone slow right in the south?

Y.S. Chakravarti: No.

Karthik Chellappa: Thanks and Sir in the opening remarks where Lakshmi also alluded to the pricing in certain segments given that in the Rs.15 lakhs SME segment you have not taken up any price increase and I believe you have also indicated in the past that the two wheeler yield is already quite higher and it will not be possible to take it up any further that too in the backdrop of weakening demand. Can you say that at least for close to 65% to 70% of the loan book, the lending rate is probably as good as it gets right now?

Y.S. Chakravarti: Let me rephrase my answer my statement that I made earlier. There is an increase across the SME segments; we have increased starting from 25 basis points to 300 to 350-basis points across ticket size wise, okay. So, the steepest increase has gone into the bigger ticket size which is actually contrary to ask what market does but we wanted to discourage the bigger ticket right now because we wanted to conserve our cash and lend it to spread the risk. So there is an increase across the board, but it is lowest in below Rs.10 lakhs segment and highest in say Rs.25 lakhs, Rs.30 lakhs and above segment.

Karthik Chellappa: Sir my last question is we have restated the second quarter results of last year as well under Ind-AS because of which we got like Rs.30 Crores increase and that has probably also flown into network, was that the reason why the tier 1 ratio in this quarter was actually up year-on-year? I am sorry quarter-on-quarter?

Y.S. Chakravarti: That is right.

Karthik Chellappa: Thank you Sir and thank you very much and wish you all the best.

Moderator: Thank you. The next question is from the line of Pankaj Tibrewal from Kotak Mutual Fund. Please go ahead.

Pankaj Tibrewal: Good morning. Congrats on decent set of numbers and a good disclosure. What I wanted to hear is what the key priorities are for us in the next 6 to 12 months in the light of the changed scenario, which we are seeing across the board. Do we see this as an opportunity because when we look at your ALM it looks quite decent, so do we look to penetrate deeper to increase our growth rates from here on or do you think that it is time to be a little more cautious prudent, what are the key priorities you guys would like to do over the next 6 to 12 months?

Lakshmi Narasimhan: Thanks Pankaj for the compliment of the disclosure here. I think we need to divide priorities into two parts. The immediate starting October 1, 2018 and by end of December I will tell you what we are doing on the liability side first, because that is where the whole focus has been for us during the last three, four months more so from a perspective that, on the asset side I think the growth opportunities exist we have given enough details about what is the runway available both on the SME and the two wheeler and the PL, so it is a question of actually putting things in place on the ground in terms of matching what we borrow and what we lend. So on the liability side Pankaj we are looking at a four-pronged strategy, some of it on the blueprints, some of it is out on the road so on and so forth. So the first thing is we are not stopping the rounds of the banks and mutual funds which we will continue to do either increase the existing limits, get new one sanctions so on and so forth, that is the first one. The second piece is, on the deposits from the public which is the public deposit scheme that we have. I think we are moving a little faster and little deeper on that. We should start getting more money from the public deposit side again. The third piece was the sell down. We have seen appetite at growing in the market at least in terms of discussions, some of the banks may require more policy notes in place so on and so forth to buy, but I think that could be a bigger chunk in terms of sell downs and the mode of receipt of money into the system over a period of next three months and the fourth piece is we may contemplate a retail NCD as well, so these are the four stuffs that we are clearly doing as far as the liability is concerned. In terms of the growth objective, is this is the great opportunity for us to kind of get into the market since the smaller players and some of the digital space guys who are relying largely on the NBFC sector to get their money, is that space creating a vacuum can be kind of occupied. There are two thoughts we are yet to reach the place but I leave you with both the thoughts that we are discussing internally. If the liquidity stress continues then I will think it is not too beyond us to imagine that rub off effect on the SME segment in terms of the ability to repay especially the higher ticket guys is going to be very clearly visualized over a period of next three to four months. Hopefully this does not spillover, but if it does then we should be clear meaning thereby when Chaks mentioned that there is a disproportionate increase in the pricing on the high ticket size, it was essentially meant from a perspective that one the team is clear that that is not the focus area and to the market is also clear that you want to borrow then there is a price at which you will borrow. So we are not too aggressive on that segment especially from the perspective that if the rub off happens and those are the guys who will be the first ones to kind of take the hit. So the next three months, Pankaj is going to watch very clearly, very, very cautious in terms of lending especially to the SME segment. Once we kind of reach to Q4 maybe we take a relook from two perspectives, one how the liquidity has shaped up and two if there is no rub off effect on that segment then that could be a very, very good runway. Having said all these, when Chaks mentioned that the sales team has also now been focussed on collections it is essentially because if the high ticket size is being discouraged then the availability of time of the sales team has been pretty high, so we have sliced our portfolio in a manner in which the sales can continue the way that they are doing business plus support on the collections. The next six months largely is a very internal focused approach than the external approach.

Pankaj Tibrewal: Great, so in light of that you mentioned about 18% to 20% ROE, will that be more of FY2020 targets or will you lead to somewhere exit this year around that, what is the thought process on that ROE tree which you want to go?

Lakshmi Narasimhan: I think when we guided originally as well we had mentioned that the exit ROE should be in those levels, but if you look at up to September we had at about 17.31%, so 18% does not look beyond reach, but I think the exit ROE should be better than that.

Pankaj Tibrewal: Better than 18% you are saying.

Lakshmi Narasimhan: Yes.

Pankaj Tibrewal: Quite a detailed one thanks and wish you guys all the best.

Moderator: Thank you. The next question is from the line of Amit Rane from Quantum Securities. Please go ahead.

Amit Rane: Thank you for the opportunity. Sir I had just one question in our small enterprise finals. Do we have any NBFC exposure?

Lakshmi Narasimhan: We would have some of those NBFC exposures from two perspectives. One is, there would be a tie-up for lending through the digital space, so we would have some sort of an exposure like that plus some very clear exposures to NBFCs as well.

Amit Rane: So can you quantify?

Lakshmi Narasimhan: About Rs.150 Crores odd is what I can kind of understand which is outstanding as of September?

Amit Rane: Okay and Sir on the borrowing front you said fresh approvals are taking longer, can you explain more on that part what are you hearing from the banks?

Lakshmi Narasimhan: No, when I said what I said is as follows that the fresh sanctions are taking longer than what we visualized or what we used to see in the past, so it is taking longer than what is happening. That is about it all that we are hearing from the banks it is being processed.

Amit Rane: Okay, can you give your outlook on cost of borrowings for the year as a whole compared to FY2018?

Lakshmi Narasimhan: Are you asking cost of borrowing?

Amit Rane: Yes, average cost of borrowings for FY2019 based on the current visibility?

Lakshmi Narasimhan: September quarter was 9.03, so when we started the year I thought we guided for about 20, 25-basis points increase, now it is getting challenged. This is really the moving number, I am saying so long as our yields tract up the way that we have shown during the Q2 I presume the impact of the cost of fund should be minimal on us, but at this point in time it looks pretty difficult to get to a specific number in terms of cost of fund.

Amit Rane: Sure, thanks a lot.

Moderator: Thank you. The next question is from the line of Bunty Chawla from B&K Securities. Please go ahead.

Bunty Chawla: Thank you for giving me the opportunity. On the gross NPA 90 DPD and if you see the gross stage 3, there has been a slightly difference 8.4 on Q2 FY2019 for gross NPA, but 10.01 for the September 2018 for gross stage 3. Also if you see Q-on-Q basis gross NPAs remain flat, but if you see gross stage 3 there has been incremental of 17 bps on a Q-on-Q basis so can you share the difference what is their difference and why the stage 3 has gone up?

Lakshmi Narasimhan: I think we are comparing two different methods and two different set of numbers. IGAAP has its own process in terms of discerning what the numbers looks like in Ind-AS; it is all to do with the accounting norm. I will give you one specific difference - even the AUM is different between IGAAP and Ind-AS, why is that difference, that difference is because of the income recognition norms under Ind-AS.

Bunty Chawla: But in Ind-AS also stage 3 is 90 DPD plus if I am not wrong?

Lakshmi Narasimhan: Yes it is 90 DPD.

Bunty Chawla: Then too there is a difference because of the accounting?

Lakshmi Narasimhan: Exactly, because of the recognition norm, as far as GAAP is concerned, you have reversals whereas under Ind-AS you continue to accrue income right. So that is the essential difference and as far as your question in terms of why there is an increase in spite of the GAAP drop, I thought that is where we need to focus on the fact of GAAP holding and the write-off reducing clearly communicates on top of our NPAs and what is happening under Ind-AS is more on accounting issue and we have guided as I am saying again that please get along with us for the next two quarters which means by end of March we will give a very, very fair estimate of what the credit cost is going to be as.

Bunty Chawla: Okay Sir and on the gold loan portfolio, it is continuously coming down from 14.5% to 11% on a Y-on-Y basis, although gold prices are stabilizing around, so what is your view on that Sir?

Y.S. Chakravarti: One thing is the book itself is growing and on top of that gold we are only present in five states and we have no intention of expanding beyond these five states at least for the next two years. So gold will continue to be a smaller portion or from 11% - it can even come down another 2%, 3% of the overall book but that does not mean that the book is growing. Please understand that the entire book is growing, gold as a percentage will remain there or will come down, but if we are looking at the next two quarters we are confident that we will see growth. Disbursements have picked up. In the two quarters we are actually confident that it will go up.

Bunty Chawla: Okay and Sir on Kerala, do we have any Kerala exposure or have we seen any pressure on that part?

Y.S. Chakravarti: Honestly we have not seen too much of a pressure because again the book is not very large in Kerala for us, it is a very small percentage of a book, but yes there is a drop in collection, but not so much that we are worried about it, but actually the auditors have advised us to create about a Crore of extra provision for Kerala book in anticipation that there may be an increase in GNPA from that book.

Bunty Chawla: So can you share the exposure how much percentage of AUM it is?

Y.S. Chakravarti: If you are looking at AUM percentage, it should be what, 1% to 1.5%.

Bunty Chawla: It is not too much of an issue right Sir?

Y.S. Chakravarti: And 95% of the book is in two wheeler.

Bunty Chawla: Okay Sir and lastly on the data if you can share in the month of October any NCDs raised, any CPs raised and what will be the interest on that and yields on that?

Lakshmi Narasimhan: We did not raise any NCDs, we did raise CPs, CP was in the public domain, I think we did at about 8.3; we have raised about Rs.293 Crores or Rs.294 Crores.

Bunty Chawla: Okay, thank you very much Sir.

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

Rahil Shah: Thank you Sir. I just wanted to ask one question. So you have been highlighting that you are very cautious on large SME part, so what would be your share of large SME book?

Lakshmi Narasimhan: About 15%, 16% in the overall AUM.

Rahil Shah: And you have increased anywhere from 25-basis point to 350-basis point, so on this large could be more towards 350-basis point, is that correct?

Lakshmi Narasimhan: That is right.

Rahil Shah: So you will see faster rundown on these books since like banks would be more willing to or the larger SMEs would be more willing to refinance this from the banks or say NBFCs who are giving have not hiked that interest rate?

Lakshmi Narasimhan: I think there is a slight alteration - my request to you in terms of altering your view. The faster rundown would have been a fact when things were normal in the market meaning thereby the preclosures in that segments used to be pretty high considering the availability of money with the others at a cheaper price, but now with that drying up, the stickiness of that loan is increasing and hence the quicker rundown of AUM is not likely to happen. It is just like the quicker fresh acquisition that used to happen earlier will now slowdown that is the difference.

Rahil Shah: Okay, but I mean if we think from the larger SME point of view, so if a lender say a bank they have not raised much so they have raised like around 100-basis points, so he will get a loan at 200-basis point cheaper and banks if they are willing to lend them it would be a kind of – not if quicker rundown but there would be rundown?

Lakshmi Narasimhan: If he get the banker and if he gets that price good times for him.

Rahil Shah: Okay, thank you.

Moderator: Thank you. The next question is from the line of Kunal Shah from Edelweiss Securities. Please go ahead.

Kunal Shah: Yeah so I do not know if you have answered it previously but how overall maybe in this current scenario, we would be seeing the overall the breakup of AUM shifting, so you highlighted in terms of gold, but how about the other segments maybe on the SME also if we tend to slow down a bit, but still in terms of it will be tracking the average balance sheet growth it will be lower and how should we see this entire AUM breakup over next two odd years from the current level?

Lakshmi Narasimhan: Two odd years is a slightly easy to answer, we had kind of guided for the SME to reach about 60 odd percent. I think we are no track to do that, so if you see during last year, year-and-a-half it has drawn from 56 to 58, so we should stabilize on the 60-65% levels over a period of next two years as far as SME is concerned. We had also said that two-wheeler will largely map the market so about 18 odd percent in two-wheeler is something that we should expect. Of the balance three which is auto, personal loan and gold, we had said we have a clear visibility as far as personal loan is concerned because of the cross sell model that we put in place and our belief is that that is the method of acquisition of the personal loan customer rather than doing from an open market, so that segment from the existing 8% level should go to double digit numbers, I think these three we have a very clear visibility, so 60 to 65 SME, 18% odd two wheeler, 10% to 12% in terms of PL. These three we have visibility. On the balance two products, which is auto and gold like Chaks mentioned sometime back, it should settle at 10 or sub 10, yes.

Kunal Shah: Okay how would in the near term if we have to look at it as to how things would be say by FY2019? So SME would be much on the lower side?

Lakshmi Narasimhan: Not much, I think it would be in the existing levels of about 58% to 59%. I do think it will be lower than that.

Kunal Shah: Okay, but in the current scenario if we look at it even on the gold lending side would not these environment today when we look at it the demand for gold loans were quite low because of accessibility to the other modes of financing and gold prices also may be coming off, but now with gold prices rising and maybe other mode of financing particularly from the regional NBFCs, there is a possibility that it will not be easy in terms of they being able to fund the part of the growth. So would not it make sense may be not particularly from your perspective but from the gold lending industry, would we see the pickup overall in this segment given the scenario?

Lakshmi Narasimhan: See like last time also, I am not too sure whether we mentioned that or not but we said is we have a well-oiled machine internally to ensure that the gold loan contribution increases because we are not averse to the fact of gold loan business growing and we are quite happy keeping it, one it has a low risk and two it produces the yield and three, we have some constant on doing the gold loan business in the five states which we are present in. So for us it is only a net accretive product if we continue to do that. We had also seen for the last seven to eight quarters that the volume for most financiers including us had dropped so in spite of putting a lot of bricks in place in terms of doing the internal fusion that was required for this business we realized that it was not growing as much as we did, so that last of that we did was to kind of pickup a 100,000 customers and try and do some sort of a survey to understand what is it, that is stopping them from coming in. There were some very interesting pieces that came off including the fact that the segment of customers who had stopped borrowing was pretty high, which was surprising for us. So we are still to get to the bottom of understanding what is that, that is keeping customers away from gold loans, you really thought that there is cannibalization. personal loan is growing so maybe gold load customers are moving there, but not more than 10 to 12% of the customers have actually moved away from gold to personal loan. So until we get to the bottom of it Kunal, it is going to be very difficult to say why is it that business will not grow and in spite of other financiers is not being available which is an opportunity for us, I think it will take a little longer while for us to understand that.

Kunal Shah: And thirdly in terms of now having this kind of a database just wanted to get the sense as to in terms of the processes leveraging on the entire customer base how we are doing it, have there been lot of changes in terms of technology processes and may be mining the customer database which we have is it changing and are we much more prepared for it now onwards?

Lakshmi Narasimhan: Oh, whole lot of stuff we did, one very straight answer is the fact that the cross sell model that we have put in place is a function of data mining, is a function of looking at customer's behaviour through our analytics tool to understand who is the best customer to lend to so on and so for, so our cross sell is completely based on that. As far as SME is concerned, we have said that we are…

Kunal Shah: Sir this PL would be entirely cross sell?

Lakshmi Narasimhan: Almost 85% of what you are seeing as business coming in during the last one-and-a-half years is through the cross sell process.

Kunal Shah: Okay.

Lakshmi Narasimhan: So that is completely analytics and tool based, as far as the SME is concerned, we had said about two to two-and-a-half years back that we started wiring that entire process and that is now completely, completely on the basis of systems approvals. So there is a whole lot of analytics tool that runs around that and which is what we said as a new portfolio is bearing better than the earlier one, was all a function of such tools and such analysis being made available to the frontline underwriting team so we have wired that completely Kunal.

Kunal Shah: Okay, Yeah, Thanks a lot.

Moderator: The next question is from the line of Aditya Srinath from Quantum Asset Management. Please go ahead.

Aditya Srinath: Yes sir, Thank for the opportunity, I just wanted to just re-confirm this so essentially right now the frontline staff no longer has any discretion in terms of SME lending?

Lakshmi Narasimhan: See discretion. I think, your ultimate lending is a function of that intuitive thought no matter what the analysis, and we have not given that away. So the frontline teams still have a discretion meaning thereby that if the model tells them not to lend and they choose to lend, they need to escalate it one layer higher with appropriate reasons, and if they choose not to lend in spite of the model telling them to lend they still need to send it up one layer, so to that extent there is discretion available, but very miniscule decimal of what is being put through is being run through that discretionary process.

Aditya Srinath: Alright and Thank you. That was all I had, Thank you.

Moderator: Thank you. The next question is from the line of Jigar Walia from OHM Group. Please go ahead.

Jigar Walia: Hi, good morning. Thanks for the opportunity. My question is are not these times actually good for us given that not typically that the duration for us is actually slightly on the lower side, and kind of stickiness that can get if you can give one indicator in terms of what would be the balance transfers and prepayments historically, that can give some sense and also internally how much comfortable are we with increasing leverage given that, historically we have been settled with excess capital so probably is it that we move towards slightly higher steady state leverage for us?

Lakshmi Narasimhan: As far as pre-termination is concerned if you slice the products then there is hardly any in two wheeler, hardly any in PL and hardly any in auto. It is only SME, that too the high ticket segment where would have had pre-termination. On an overall book basis in any case the bigger ticket SME is about 15% odd so we saw a pre-termination of about 6% to 7% in that segment, not in 6, 7 on the book, but 6 to 7 on the 15%, so pre-termination were never a worry for us in that segment, does that answer your question?

Jigar Walia: Okay, but does this kind of a scenario kind of helps you bring in longevity to the book and of course the second question is do we increase the leverage?

Lakshmi Narasimhan: Leverage, see, I think we are at about 4 now, I think 5 should be a reasonably good position to take from rating agencies perspective as well, even though the RBI lets you to go up to 6.25 to 6.5. Going up to 5 should not impact the rating.

Jigar Walia: Should not impact the rating, okay, okay, Thank you.

Moderator: Thank you. The next question is from the line of Pawan Ahluwalia from Laburnum Capital. Please go ahead.

Pawan Ahluwalia: Yeah, my question really relates to the liability side, I think you know if we look at our balance sheet size, our track record on credit, all of that it is a pricing that our credit rating is what it is then you know, our sister company Shriram Transport has a better rating than ours also you could argue that you know as a model line they should be subject to greater volatility and which should impact the rating. My question is how we really doing the best job we can to showcase to rating agencies, what our credit quality is across cycle and is there a decent chance that in the short and medium term, we may be able to get an upgrade on the credit rating and the reason I ask is in a tight liquidity environment, banks, mutual funds etc despite all the flaws of credit rating that we have seen again with IL&FS just become very focused on these metrics in terms of putting NBFC’s into buckets right. Is there chance that we could climb into a high bucket?

Lakshmi Narasimhan: Pawan I think you are slightly dated on the rating for the two enterprises, both the brother and sister are now AA+. Shriram Transport has a AAA only for the public deposits part of their business, rest all types of instruments are rated similarly for both the enterprises, number one. Number two is, CRISIL in fact upgraded during this financial year only. Our effort to kind of position what the inherent strength of the enterprises as also the inherent strength of the opportunity that is lying in the customer segment that we are present in is a continuous exercise with the rating agency and once they kind of see the way we see it I am sure we should get to next level which will be ultimate rating that we should look forward to, but otherwise the rating is similar Pawan.

Pawan Ahluwalia: And when we issue paper Transport and SCUF issue at the same in practice the borrowing cost is the same, so banks lend to us at the same rate or mutual fund paper at the same rate or is there a delta there.

Lakshmi Narasimhan: I think it is a function of time, tenure, quantum, so on and so forth but to leave you with a thought that there are times when we have borrowed lower than them and there are times when they have borrowed lower than us.

Pawan Ahluwalia: Okay. Thank you.

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

Karthik Chellappa: Thank you again for the opportunity, just to follow up Sir, and one is on slide 11 if I just look at the borrowing mix the semi fixed has actually gone up significantly in the last one year. Is that like a conscious decision or will that help you to minimize the increase in funding cost or what was the thought process behind such a steep increase in the mix?

Lakshmi Narasimhan: Sir are you saying that semi fixed has increased?

Karthik Chellappa: Yes.

Lakshmi Narasimhan: And you said dramatically.

Karthik Chellappa: From 36% in the second quarter of FY2018 to 50% now?

Karthik Chellappa: You are saying last one year, right?

Karthik Chellappa: Yes, was that conscious or I mean what was the thought process behind that?

Lakshmi Narasimhan: Yeah the thought process is, one we were reasonably sure of the price going up in the market so as far as possible we tied up fixed, and where it was not possible we tied up semi fixed that is the logic behind it. So in a semi fixed environ you at least get 12 to 18 months as fixed and then it kind of increases after that when it comes up for re-pricing, during a normal borrowing of about three years what you end up doing is, you just have one reset that happens and the bottom line is that is the reason why the semi fixed is. It is again a function of so many. Karthik it is not merely our own desire. It is also function of how, what and when is available in the market, so these things work in tandem, but I think stay put on my threads, I think that kind of answer is most questions.

Karthik Chellappa: Okay and on the earlier comment Mr. Chakravarthy made that this festive season may actually see like a 20% kind of drop in overall two wheeler sales. So if I just run the number so last year third quarter we did about I think 380 odd thousand units, now we are running at about 300,000. So even if you have to outperform the industry and if we were to something like about 330 or 340,000 for the third quarter of drift here that would still mean a sequential quarter-on-quarter increase of 10% so given that liquidity situation and the insurance issue and the fact that December is generally dull is that looking still reasonable?

Y.S. Chakravarti: Karthik, manufacturers, auto manufacturers, auto dealers and financiers, two wheeler we are all pinning our hopes on the last week of October and Dhanteras and in Diwali sale. As I said yes, December is normally slow. See last year what happened was I think October had both Dussehra and Diwali coming in the same month. So there is a bulk up of sales in October and November. This year some of the sales, at the peak Dussehra time you know we had this insurance confusion and that sale has not yet come back in October so I feel there will be, if you look at quarter-to-quarter there could be a drop in sale, not a growth.

Karthik Chellappa: Okay, got it. Okay Thank you Sir.

Moderator: Thank you. The next question is from the line of Aditya Singhania from Enam Holdings. Please go ahead.

Aditya Singhania: Thank you. I just wanted to get your thoughts on the trends in asset quality, two observations there, one, the write off levels are sort of flat year over year, but which suggest an improving trend in the credit quality of the portfolio, but the 90-day levels across products are broadly flat, how should we read this?

Lakshmi Narasimhan: We kind of started this call Aditya by mentioning that we expect two kind of drop to the 8.95 and a gap further as we head into this financial year. So I think the gross NPA number should drop and the write offs being lower than what it was during the last quarter, is there an indication of the efforts that have been put in the past terms of reducing the overall 90 plus. As we head forward absolute amounts may be increasing, but as a percentage of the book it is going to drop.

Aditya Singhania: Sorry I missed the first few minutes of the call did you explicitly guide for a 90-day level?

Lakshmi Narasimhan: No we have not guided, we said that it is going to tract down from the existing level that is what we have said.

Aditya Singhania: Okay, got it. Thanks.

Moderator: Thank you. The next question is from the line of Anubhav Kaul from Ward Ferry Management. Please go ahead.

Anubhav Kaul: Hi Lakshmi, Hi Chaks. Can you just help me to fabricate 18 to 20% and MSME loan growth into customer addition versus loans outstanding for customer versus the increase in ticket size, because I understand for the other verticals it will all be fresh customer accounts predominantly but for the MSME business if you could just help me understand that better, that will be great.

Lakshmi Narasimhan: Yeah, these are whole lot of numbers which I do not have off hand, but I can tell you directionally if your question is, do we have existing customers coming in, then like we had mentioned at the end of Q1, these on one on one or on a call that we ran a specific program to ensure existing customers are ring-fenced and do not move to competition. As a function of that anything like 20, 25% of the lending that we do in SME is the function of existing customers coming back after having crossed a specific threshold of servicing the past loan that they have. So directionally, in terms of specific numbers, I think we will need to send it to you separately depending upon what the numbers look like and whether we are going to put it out in the public domain, but largely in terms of ticket size, when we ended March we had mentioned that the ticket size had dropped about 1,25000, 1,30000. That trend continues even now we are seeing a drop of 30,000 to 40,000 in terms of overall ticket size for the additional disbursement that we are making for the past six months.

Anubhav Kaul: Understood. Thank you.

Moderator: As there are no further questions, I now hand the conference over to Mr. Nischint Chawathe for closing comments.

Nischint Chawathe: Hi, Thank you very much for joining us today and we thank the management for providing us an opportunity to host the call. Thank you.

Moderator: Thank you. Ladies and Gentleman, on behalf of Kotak Securities that concludes this conference call today. Thank you for joining us and you may now disconnect your lines.