



Edelweiss Financial Services

Q3 FY19 Earnings Conference Call

January 25, 2019

Moderator: Ladies and gentlemen, good day and welcome to the Edelweiss Financial Services Limited Q3 FY19 Earnings Conference Call. 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 telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Shiv Muttoo from CDR India. Thank you and over to you, sir.

Shiv Muttoo: Good afternoon, everyone and thank you for joining us on the Q3 FY19 Results Conference Call on Edelweiss Financial Services Limited. We have with us Mr. Rashesh Shah – Chairman and CEO – Edelweiss Group. Mr. Himanshu Kaji – Executive Director and Group COO, Mr. S. Ranganathan President and Chief Financial Officer, Ramya Rajagopalan – Executive Vice President (Corporate Development), Salil Bawa – Head, Stakeholder Limited and Samridhi Deorah – Senior Manager, Stakeholder Relations.

Before we begin, I would like to state that some of the statements in today's discussion maybe forward looking in nature and may involve certain risks and uncertainties. The detail statement in this regard is available on the results document shared with you earlier. During the discussions, we will be referring to the Q3 FY19 Investor Presentation uploaded to the exchange. With that, I would like to now invite Mr. Rashesh Shah to begin the proceedings of this call.

Rashesh Shah: Thank you and good afternoon to all of you. First of all, once again thank you very much for taking the time out to be on this call. This was an important quarter and you would have got a chance to see the results for the Q3 we had a PAT of about ex insurance about Rs 273 crore and consolidated PAT of Rs 226 crore. On the 9-month basis our consolidated PAT is Rs 763 crore and ex insurance PAT is Rs 906 crore which shows a growth of 22% and 27%. As you all know Q3 profit has come down, but overall for the 9 month we are still clocking our 22% and 27% growth.

For the 9 month the balance sheet also grown by about 14% now the balance sheet stands at about Rs 55,822 crore which is almost the same as it was in the last quarter. Our own balance sheet and the customer assets put together we are now at about ~Rs 2,50,000 crore. In this quarter and we will talk more color about book size and everything else. We were able to maintain the ROA of 2.4% ex insurance and ROE fell to about 15.6% ex insurance, but a large part of this fall because of the gearing ratio came down for the last quarter we have a gearing ratio of 5.2 ex-treasury which has come to 4.2 in this quarter.

So, there was a fall in the gearing ratio because of some of the actions we took in this quarter and that impacted the ROE for this quarter, but we are happy that the ROA has been maintained at 2.4% ex-insurance. This quarter also was an important

quarter for us because we reinforced the strength of our diversified model we were able to handle the market dislocation which was fairly severe all of a sudden, but all the risk models and liquidity models we have are there to keep us prepared for this and I think in this quarter we are very happy that all the models and the game plan we had we were able to execute on that. Also, a lot of decisions we took in this quarter may have impacted profitability for this quarter, but we see a large part of that is not structural, but was more tactical and was more out of choice. We made some choices in the hindsight you might think that maybe was being too conservative, but we made choices which impacted profitability but also allowed us to demonstrate the strength of balance sheet and liquidity management and the framework that we have.

In the last few months I think for the industry as a whole it was a testing time, and in Edelweiss we believe that a quarter like last quarter will come every 10 to 12 quarter in Edelweiss we are now almost 22 year old which is equal to 88 quarters and we actually have gone and enumerated there have been 11 quarters out of this 88 quarters which have been very turbulent there was one in 1997 when the Asian financial crisis happen there was one in 1998, there was one in 2000, 2001, 2006, 2008. So, we have a framework, we have an approach which says that you have to be prepared for this one or two quarters every 8-10 quarters that will come about and we have seen that in the past and this quarter was akin to that. Also, happy to say this quarter was not as bad as maybe some of the other quarters in this club of 11 but it was also much harder than some other months or some other quarters in this club of 11. So, I think this was somewhere in the middle in terms of how severe the quarter was in that sense.

Also, in this quarter I think we are proud of the strength of the retail franchise, both on the asset side but also on the liability side. We raised an NCD bond issue and a large part of the participation came from retail customers of ours. So, we are very gratified for this kind of support in spite of the market volatility and turbulence that our retail customers have showed with us.

In terms of liquidity, we started this quarter when the turbulence started, we had almost about 365 days of liquidity which means we were okay to meet all our obligations for one year by just using the cash we had and the receipts that we were expected to get. We quickly added to that, we slowdown the wholesale book, we took all the repayments that clients were due and a lot of the repayments were paid on the due date which was good news because we were also apprehensive whether clients will meet their obligations but both retail and wholesale customers largely paid us on time and we took that money. Our fresh disbursement was slow on the wholesale side, retail we continued. We also had some scale back on the LAS book which always happens when equity markets are in turbulence so there was more business as usual in that sense, but because of all this the book came down but also resulted in more cash and liquidity on hand for us.

Along with that in this quarter we were also able to raise close to Rs 9,000 crore of fresh borrowing and two-thirds of this was more than one year non-commercial paper led and that is actually one of the highest. We have every quarter for the last three years, the long-term money we have raised, long-term which is more than one year, has been anywhere between Rs 3,000-7,000 crore in a quarter. This quarter was close to about Rs 6,000 crore which was one of the higher ones. So, in spite of the turbulence our ability to raise long-term money from banks, from retail investment and from mutual funds by NCD was also very gratifying. We now have what we call the balance sheet liquidity of about Rs 14,000 crore, half of which is liquidity cushion we call it liquidity cushion but it is overnight money which is available on one day call to us which is FDs and liquid fund investments and treasury bills equivalent that is about Rs 7,000 crore and we have another Rs 7,000 crore approximately in liquidity which can come to us in 30 to 45 days.

So, what we call balance sheet liquidity is overnight liquidity is available on 30 to 45 days and both this put together is currently about Rs 14,000 crore which is one of the highest it has been in Edelweiss history. As a result of that our as I said earlier the DE ratio fell down from 5.2 to 4.2 which did impact our ROE for this quarter clearly and the scale back of the book did impact our profits also and we now estimate that at about 25% of the balance sheet can be converted into cash between 30 to 45 days which gives us I think a credit business one of the very flexible balance sheet because as you know on our balance sheet we also have home loans, we have real estate project loan and we have ARC and in spite of having such medium to long-term assets we still have 25% balance sheet which can be converted into cash in 30 to 45 days and that was one of the more gratifying outcomes of the last quarter because this is what we had wanted, this is what we were able to do. It did come at a cost of some loss or profitability and some loss of actual profits. ROE came down and profit after tax came down, but going forward our outlook on liquidity is still conservative though I think it improved a lot and we believe it will improve a lot, but we see that the NBFC liquidity situation has improved and the crisis of confidence has gone away, but we think that system liquidity is still fairly tight and may remain tight until the election because of two reasons:

Whenever elections are there the cash in circulations goes up and currently the cash in circulation with the public is the highest it has ever been and along with that, we have the annual year ending coming up, the March quarter coming up which usually also is a liquidity tightening environment. So, we think the next five, six-months, the liquidity will be tight we have a fair amount of liquidity on our balance sheet. We will continue to deploy from December onwards. Disbursements have been on full steam on the retail side and we will continue to move that. We also been investing on wholesale strategies from the funds we have so even on that we have kept up with the market opportunities and all. We have not been growing the wholesale part on the balance sheet for obvious reasons in the last quarter.

The other high point is our commercial paper has now come down to 7%. As you know we had already been bringing down our commercial paper even before the last quarter, it is come down from 29% to about 18% of a total borrowing came from commercial paper over the last four years now it has come down to about 7% of our liability mix is from commercial paper. So, we will use commercial paper judiciously. We have never used commercial paper for any of the medium-to long-term credit strategies and we will continue to do that because we do not think an ALM mismatch is a good risk-reward to take and we have never used ALM as a profitability tool trying to have some ALM arbitrage and though that thus increase our overall cost of funding we think it is a prudent approach to take.

In this quarter the long-term debtors also gone up. Our long-term debt is 62% which is the highest it has been last quarter it was 59, but as you know about three years ago this was closer to 36%. So, we have moved from 36% long-term borrowing to now 62% and our focus on this ALM management, liquidity management will continue to be there it does increase our cost of funding, it does increase the ALM cost or loss but I think overall it allows us and our investors to sleep peacefully at night.

We have a capital adequacy of 17.8% for this quarter and we think our liability management for what need we have we will continue this within mutual fund we will account for about close to 20% of our borrowing, banks will be about 45% or so and they are already at close to 44% at the end of this quarter and retail is now about 19%, retail will be between 20% to 22%, others which includes insurance companies will be about 10% to 12% and we expect to maintain this kind of source of liability profile. So, mutual fund will be an important part of a borrowing, but I think at about 18% to 20% we can handle the AUM and ebbs and flows of the mutual fund industry a lot more easily because mutual fund industry will experience with these kind of outflows of AUM from time-to-time which is what happen in the next quarter, but

having a good franchise with banks, retail investor, insurance companies will also help us maintain a very stable liability profile in the coming years.

On the color of book – this quarter our book came down by almost about Rs 5,500 crore out of which the LAS book which includes ESOP financing as well as the loan against shares came down by about Rs 2,000 crore. Large part of this was due to the equity market volatility and turbulence and we have always followed if you have seen our large book growth, we have always encouraged clients to scale back the margin funding book and the loan against share book when markets are very turbulent. It is a good risk management tool but is a good client friendly tool because we do not want clients to borrow money in a market that is not rewarding for them to borrow his debt equity share positions.

So, that largely would have happened in any case. The corporate has grown, it degrew by Rs 3,300 crore in this quarter which actually we see as a matter of strength that we were able to see client's contractual obligation and behavioral obligation the same on the wholesale side. One of the questions a lot of analysts and investors asks us is on the wholesale sale usually customers find it hard to meet contractual obligation, but in this quarter in spite of the liquidity crunch we were able to take repayments of Rs 3,300 crore on the wholesale book. We did not grow the book, we did not disburse as much given the liquidity conservative approach that we had in this quarter, but on both this plus our retail book on home loans and SME and all continued to grow and we think the outlook on book growth is fairly positive, we can continue to grow the retail book at 25% to 30% fairly easily.

The ARC book last quarter we kept on making investments and will continue to do that. We think the distressed credit ARC book can continue to grow at about 20%. We see a very robust pipeline you must have seen headlines also how many banks are wanting to sell their NPL loans and we are seeing a lot of opportunities in that. The corporate book will remain flattish depending on the market environment and opportunities. We will co-invest with our funds but we will be very calibrated in terms of the market environment on that.

Finally, friends on asset quality – we have been very watchful because whenever there is a liquidity crunch and there is a crisis of confidence, you have to watch asset quality because it has unintended consequences on that. So, we have in this quarter intensified our scrutiny, we have intensified our review cadence, we have on the wholesale book, on the retail also we have been very proactive with the collections and other strategies. As a result of that happy to report that there was no change in asset quality in this quarter in both the wholesale book and retail book. I am happy to say that most of the activities continued and most of the client behavior and the asset quality continued on the BAU basis. Because of our intensified effort we also have stepped up on recoveries of the current Stage-3 books because as you know though we have NPAs, a lot of our NPAs also have underlying collateral and we stepped up on the liquidation of that collateral and the recoveries from that collateral as a result of that a couple of accounts got recovered in this quarter and our Stage-3 on balance sheet went down from Rs 743 crore to Rs 654 crore and provisions also declined from Rs 133 to Rs 107 crore for this quarter.

Our overall credit cost remains the same in terms of provisions and the credit write-off that we take and we expect that to remain stable. Actually increasingly GNPA and NNPA they have become redundant and we expect in this year we will all move to the Ind-AS concept of Stage-1, Stage-2, Stage-3 and the ECL provisioning but the GNPA remained at 1.84% and NNPA at 0.78%.

The outlook on asset quality:

We expect it should be BAU not only because of the environment but because of the strict focus on collections, recoveries and monitoring that we have. We have actually doubled our efforts on that just as a prudent measure what we did on liquidity as we were very prudent on that even on asset quality, we are very prudent. We are triggering early warning triggers a lot faster, working with customers, working with clients a lot more proactively, what we would have done three, four months down the line we are doing in the next month kind of sense of urgency is there and we are obviously careful not to compromise on customer franchise and our market relationship which also I am happy to report that we have been able to do all this all this the scale back of the books, the liquidity management as well as intense focus on asset quality without comprising on franchise and relationship risk out there.

So, overall that is where largely we stand, we have got a lot of questions we continue to have them on a wholesale book including real estate. We have about close to Rs 10,000 odd crore book size on that which is over 174 projects. We monitor these projects on a fortnightly basis where I am involved and we classify projects in terms of Red, Green, and Yellow and again happy to say that we are not seeing any significant change in the profile of Red, Green and Yellow in this 174 projects.

The good news is on housing and all real estate the sales continue to be there and as we would have seen in overall inventories coming down, but it is an area where we all need to be very careful, very vigilant, very proactive which we continue to be there on that.

So, finally on outlook:

Overall, I think it was a very difficult quarter. It is behind us, but it is good to have this kind of stress test from time to time. As you all know friends, adversity makes us stronger. We do not want adversity but every time there is some adversity, we become stronger we would classify the last quarter is that. We would maintain a conservative beyond liquidity for the next five, six months but we will start deploying and we think the borrowing franchise we have will continue to allow us to grow the book in a calibrated manner. We think NBFCs will continue to grow may be after the March quarter or the June quarter once the elections are out, a lot of growth will be back to normal and we are also getting ready for that as we put the current liquidity to work in the next five, six months. Most of the activities for us has been BAU, as I said, except for the wholesale book, our retail credit book continuous to grow in the last quarter also the activity continuous.

Our ARC had a good quarter. There were lot of recoveries but there were lot of deployment opportunities also. So, the ARC model continues to strengthen and get confirmation from the market place because we also want recoveries. Last quarter was a good quarter from a recoveries point of view as you would have seen in the earnings presentation that we have. Our asset management, wealth management continue to do strongly. In this quarter our asset management closed a \$1.3 billion fund recently. We closed it recently at \$1.3 billion stress asset fund which is one of the largest funds raised in India .

On the wealth management, we have crossed customer AUA of more than Rs. 1 Lakh crore and that continues to grow and in both asset management and wealth management we have seen the net flows coming. In asset management, we also recently won the CPSE ETF mandate given by Government of India and this is a fairly strong franchise opportunity for us and we invested a lot in order to win this mandate, but now we will invest a lot to strengthen and execute on this also. We expect for this year FY19 that our profit should grow at about 15% over FY18. So, in spite of the turbulence of the last quarter and in spite of this quarter also getting back to putting the liquidity to work we expect that overall for the year, we should be maintain a 15%

to 18% profit after tax growth over the last year. So, having gone through a difficult quarter, having gone through a more calibrated half year, if you can still able to clock about 15% to 18% profit after tax growth, we are fairly happy.

Going forward we think from FY20 onwards, from this March onwards growth will come back on stream and we are very confident of maintaining a minimum 20% to 25% PAT growth. As you know over the year we have been always maintaining a very conservative outlook on growth, but we do feel confident that at least a minimum 20% to 25% profit after tax growth for the next three, four years should be possible for us. We have enough equity, our gearing has come down, we have enough opportunities and the diversified business model we have allows us to fire on multiple engines going forward.

So, along with that friends thanks a lot. You have been very supportive, very generous with your inputs in the last quarter. So, thank you all for that also and now we can now open for Q&A from all of you.

Moderator: We will now begin the question and answer session. We take the first question from the line of Sunil Tirumalai from Credit Suisse. Please go ahead.

Sunil Tirumalai Can you explain the profit flow through from the Binani resolution, what is the quantum, over how many quarters, and what is the logic on spreading on these many quarters, so this kind of template for us to work with for future resolutions as well that is my first question?

Rashesh Shah: I think for this quarter we have shown that the profit after tax impact of Binani resolution largely was about Rs 48 crore at a profit after tax for us. See if you convert that into pretax that should become almost about Rs 75 crore and our share which is about 60% of that so you take Rs 75 crore as adjust for the 60% share that should come to about Rs 125 to 130 crore. This Rs 130 crore was almost about 60%-65% of the carry because the other Rs 35 crore had come through in the earlier quarter because of IndAS valuation. So, I would assume that something like Binani it actually fits with our overall model that we should make about 4% to 5% extra carry income per annum on this kind of accounts over three, four years. So, Binani has been approximately three and half years and I think I would say the carry income has been close to about 25% to 30% of the capital deployed which turns to about 5% to 6% per annum. So, as we always said in ARC our approach is, can we earn about 18% regular yield on that and have the potential of another 5% to 7% incremental IRR per annum as and when things are resolved in a profitable manner.

Sunil Tirumalai My second question is I think you are currently carrying about Rs 800 crore of total provisions, Rs 805 crore of total stock of provisions, what flexibility do you have in terms of allocating this to various segment if NPA come up?

Himanshu Kaji: As we had mentioned in our first quarter when we shifted to Ind-AS we have additional provision of around Rs 150 to 160 crore that we have been carrying through and that is still available at this point in time.

Rashesh Shah: I mean for those of you, who may not remember when we move from I-GAAP to Ind-AS we had almost Rs 140 odd crore of additional provisions which we could have clawed-back, we did not claw that back and we kept it in that. So, these Rs 800 odd crore that you are seeing that is the additional provision which is the flexible one. We also have opportunity to claw-back more of that as we sell the underlying collateral in some of these assets because a lot our NPA assets should have a low loss given default because of the underlying collateral we have. So, as we resolve that we can use that provisioning as claw-back also.

Sunil Tirumalai Lastly on the wholesale mortgage book could you throw some color on whether any movements in less than 90 day bucket any delays across all the 174 real estate projects that you mentioned that would be helpful I mean if you could give a color up to January'19 as well?

Rashesh Shah: As I said everything was BAU so I am sure a few accounts did move, but it was not anything unusual as compared to the earlier quarters. So, in this quarter Sunil we were tracking very closely any change in behavior from BAU so all I would like to say is everything that happened in this quarter was BAU even on that book. So, I know that currently the market apprehension is that on that real estate but it may be too early, maybe it happens in the future. We do not know and we have always said that we cannot forecast what is going to happen, but have to be prepared for that so we have stepped up our proactive approach, vigilant site visits, even encouraging the developer to do bulk sales and raising cash we have done all of that in this quarter and overall we have not seen anything unusual that was not part of the BAU and part of the model for the book in this quarter.

Moderator: The next question is from the line of Avinash Singh from SBICAP Securities. Please go ahead.

Avinash Singh: Few questions kind of data related one is that if I look the retail, apart from LAS also there is minor sequential shrinkage. Now in that backdrop can you please elaborate your Q3 disbursement and repayment across different segments of business the retail, wholesale segments that is my question one. The second question is can you also tell us that your marginal cost at which you have borrowed I mean I can see the borrowing mix for Q3, but at what cost these borrowing have come so these are my two questions?

Rashesh Shah: We do not have the gross disbursement numbers but we can share them easily afterwards because for this call we look at end of quarter numbers. As I said you know we did encourage clients to repay and we did increase interest rate in this quarter. As you remember, when we spoke in the last call also we had said that we will try and pass on the increase cost or funds on to the clients so on that count on the home loans and LAP and some of the business loans we did get repayments on that and so we kept our disbursement as per normal, but we got slightly more repayment as I said contractual and behavioral and we encouraged it because in this quarter it was important to allow anybody who wanted to prepay. So, the fall in the book was not because the disbursements came down significantly, the fall was because we allow the prepayments to happen as were happening otherwise as you know what happens in LAP and other when the customer who wants to prepay or do balance transfer you have a fairly strong protocol on talking to the customer trying to hold them back and there is a percentage of that can be held back. In this quarter we did not do all of that we allowed prepayments also to happen because honestly for us it was also a test of how liquid and flexible is a balance sheet and we are very proud to say if 35% of the balance sheet can be converted to cash that is a strong risk mitigation on liquidity front for us. It does come at a cost and our profits would have been higher by Rs 10 to 20 crore, if we had been not conservative on accepting prepayments or encouraging clients to pay as per due date not encouraging them to borrow fresh and things like that it is largely because of that, but on the retail side we continue to disburse as we used to. The LAS came down LAS obviously I have already explained why it came down, Agri has come down because that is a seasonal thing because these are very short-cycle books and the other came down as part of the normal repayments that were there on the wholesale book. The stressed credit came down because of the Binani resolution and we did deploy also against that, but I think as I said we are always happy to get recoveries also and we are happy to deploy also. So, I think whatever loss of size we have had in this quarter we are not unduly concerned about that because that will get fixed in a couple of quarters fairly quickly but ability to show agility, I think in credit it is very important to show agility and we all

know that famous thing that in credit you are always on a treadmill and you have to grow quarter after quarter after quarter no matter what your sense of risk is. We do not believe in that, we think that whenever required gears can be changed, can we change from fourth gear to third gear without impacting our parameters, without impacting our customer franchise and I am happy to say customer franchise is intact, our employees morale is intact, our NPA numbers and all are intact so that is what I would want all of you also to appreciate that we have agility in the credit business also. We always have agility in the advisory business, but having agility in the credit business is a very important part of this and we do think that every eight or nine quarters whenever environment gets vitiated, our ability to scale back a little bit, to hold back a little bit is an important attribute of our culture and our business strategy.

Avinash Singh: Just a quick follow up on this one, so you are saying that your disbursement was as usual large in the retail, on wholesale of course you kind of reduced or stopped disbursement. Now from going forward I mean should we expect that sort of the book had adjusted now here onwards the growth should be even at a slightly lower pace than usual, not like Q3?

Rashesh Shah: Absolutely usually scale back again because as I said we are holding enough liquidity Q3 was a test and the environment was vicious I mean it is very easy right now for all of us to say but I think October November we are very clear though our liquidity was in a strong place. We had no idea what would happen in the environment and I think all of you were also giving us inputs, but you were also uncertain that how the things will pan out if things has gone worse in India. So, I think on that account I do not think Q3 will be repeated in terms of a scale back of the book. The growth will continue it has continued in fact December and January have been good months we will step on that. Wholesale as I said we will only do co-investments along with the fund and wholesale is very risk related calls given that we all have concerns on the tight liquidity in the next two, three quarter we also want to wait and watch and see how the wholesale environment pans out.

So, we are happy to say we will also be telling our customer that wholesale we will be conservative and evaluating new opportunities on growing on that and what we do will continue to do on the fund side. Our own book size we will be more calibrated, but we still think that March onwards our profit growth of 20% to 25% at the minimum should be available to us and it should be possible for the next three years and that is what our long-term objective has been that we can you grow an average of about 25% over a 10-year period. So, we have been growing very well at about 35%, even if we grow at about 25% for the next couple of years and then change gears again, we would be happy. So, I think idea is to show this agility, flexibility and conservatism and actually make it part of your culture and this culture we were able to do that.

Avinash Singh: Now my question on that marginal cost of borrowing in Q3 across different instruments? I mean your Q3 borrowing across the different instruments you have given the mix, what were the cost across this different instrument I mean the NCD cost, the CP cost and blended cost?

Rashesh Shah: So, if you look at the blended cost overall I think incrementally was about 100 basis points higher for this quarter which on a weighted average basis ended up becoming a 40 basis point higher cost on overall liabilities approximately, but along with that we also look at our third factor which is how much we were able to pass it on to the customer and if you can see slide 17 where we have given the attribution cost we have said that the PAT impact was approximately Rs 6 crore which is the higher borrowing cost that we incurred but not been able to pass on to the customer this we think is more for the quarter and we think it should normalize. So, 80 to 100 basis point high cost of borrowing or fresh borrowing which translated as 40 basis point incremental cost overall of borrowing and a large part of that we were able to pass on a Rs 6 crore was an impact at a PAT level for the last quarter.

Moderator: The next question is from the line of Renish Bhuva from ICICI Securities. Please go ahead.

Renish Bhuva: Sir my first question is on the retail business, if you look at our retail business our cost to income ratio has been actually going up from last almost 3 years it was like 42% in FY16-17 which is now close to 50% can you please throw some light on what is happening on cost side some part of it might be explained by the very lower revenues, but it looks like we have been increasing cost in that segment so if you can just throw some light whether it is technology or people or branch, can you just throw some light on that?

Rashesh Shah: On the retail side we have been expanding, we have been adding branches. So, SME like a year ago we had only about 40 branches we are now at 100 branches, we are expanding our agri credit business and investing in technology on that even on the mortgages and on small ticket home loan what is called affordable we have been investing in that. So, in the last two years we have been in an investment cycle on the retail credit business. We accept that the PAT impact of this what we call the development investment we are making on the retail credit book is about Rs 70 to 75 crore a year is the impact. So, about Rs 20 crore a quarter, so in this quarter our PAT was about Rs 52 it should have been Rs 70 crore if we had not made the kind of investment we are making in scaling up the distribution and the reach that we are building and that was something we have been talking about it and I do agree with you that the cost income ratio at 52% is high. Going forward though think it will go up much more from here I think 50% to 55% was the peak that we were expecting and over the next three years as the book start scaling up and as the benefit of this expansion starts coming through we do think long-term steady state retail should be about 25% to 32% is what the current plan that we need to bring it out.

Renish Bhuva: So, it is fair to assume that even let say for next couple of quarter we might in other Rs 50-60 crore coming up in the retail P&L because of this investment or do you see it will moderate significantly from FY21 and FY20 will be another year of investment in retail?

Rashesh Shah: I would say for the next two quarters, the cost income ratio should remain about 50% plus and then you should start seeing the downward trend on that. Coming up we are not adding fresh, but whatever investment are there because this new branch have started and average branch takes about a year to 18 months to breakeven so that cost will continue. But I would say for the next couple of quarters it should remain at about 50% plus and then start inching down after that.

Renish Bhuva: Second question is actually on our ability to pass it on the increase in the incremental cost of borrowing. So, broadly so my understanding is because of most of the NBFCs were not so active in the market so that is why we are able to pass it on so easily, but in a case entire NBFCs space is up and running what your sense in that case our cost of borrowing increase our ability to pass it on further I mean do you see a scenario where we might have to take a margin hit cost of borrowing goes up in coming period?

Rashesh Shah; I think it is an interesting question you are asking we also have been grappling with that. Our current feeling is that cost of borrowing will come down by 40-50 basis points if RBI cuts rates and liquidity improves and we should be able to pass on part of that to the customers. Currently we do not expect any loss of margin on that if you see our NIM also in this quarter actually were fairly strong. So, we do not see a very large NIM impact as a result of this, but I agree with you I think we will be sensitive to the market conditions, but we are not seeing pricing pressure as of now. We are in the month of January because although liquidity conditions are still fairly tight and be a lot of our business is a fairly differentiated like on the home loan book the small ticket home loan affordable housing there I think the pricing power still continues to be there

in fact there is a severe shortage of credit availability for the home loan segment as we speak to the customer and the DSAs because some of the home loan companies have still not gone out and started disbursing in full flow and banks and all are still are not able to do affordable housing in small ticket loan at a very large scale so the opportunity remains. Even SME is still a credit starved market continues to be that, we are not seeing pricing pressure on that also and also remember the NBFCs are back in action. It was not the full force that it was in the first half there is a tighter liquidity conditions, there are lot of home loan companies which are not growing as aggressively there are lot of them who are there about 40%-50% of the disbursement that was there earlier and we are small enough so that we can really target and segment our customers. So, I think differentiated approach the niche strategy if you follow as well as the fact that market still remains liquidity constraint we will ensure that we do not have to take a margin hit but as we have said 10-20 basis point fall in NIM will happen from quarter-to-quarter basis, but this quarter our NIMs were 8.6% of course also partly because of ARC, but I think we can easily manage that so we do not see a lot of concerns on that.

Renish Bhuva: I mean it is fair to assume that even in an increasing rate scenario we will be able to maintain our margin broadly?

Rashesh Shah: Yes.

Renish Bhuva: Last question is on the net worth movement so basically in the credit business we have seen absolute decline in the end of period equity and we have seen significant ramp up in equity BMU business, so can you please throw some light on the capital movement on quarter-on-quarter basis?

Rashesh Shah: Actually, the EOP equity that we have is for the credit business is what is allocated. As you know, the credit book came down by almost about Rs 7,000 crore from Rs 49,000 crore in last quarter to Rs 42,000 crore. So, that did result in the release of equity and that equity was going into the BMU because BMU is a treasury and so we have excess equity in the BMU because at 4.2 debt to equity ratio there is excess equity. So, as the credit book came down from Rs 49,000 to Rs 42,000 crore it did release equity as we start ramping it up the equity will go back to that.

Renish Bhuva: I mean is this the quarterly adjustment we do every now and then or this is one of quarter where we have actually taken out equity from the credit business and put it into BMU or because of the liquidity situation or is it like we do it in normal basis?

Rashesh Shah: Actually, the equity capital is allocated through the business as per their book size or in particular ratio depending on every product that we have. So, overall if the book goes up equity goes up and BMU reduces equity or after a certain point BMU will say now I have to go out and raise more equity which is what we did a year ago when we went out and raised fresh equity, but the businesses release equity and give it back to the BMU then BMU holds that equity. As the book was growing over the last many quarters, the EOP equity in the credit business was actually going out because the book was scaling up. This was the first quarter where the book got scaled back and equity got released. Now, we do not expect a repeat of that. So, you will see in the next few quarters as the books grow again the credit book the equity will start coming into that so this is the allocated equity as per formula that we have on a program by program basis.

Renish Bhuva: So, the reason why I was asking is absolutely you mentioned that this is the first quarter where we have seen absolute decline in the credit book I think from when we started lending business if I am not wrong. So, I mean FY19 most likely to be first ever year where we might see absolute decline in the credit book, so still you are maintaining your guidance of 20%-25% loan growth going forward especially in retail

and ARC. So, I mean is there would be any change of strategy from a wholesale heavy a lender to a retail heavy lender going forward I mean what kind of loan mix do you see after two years?

Rashesh Shah: We have always said by the next year retail should become about 50% of the credit book it is at Rs 42,000 crore so that strategy continues as we have maintained that we continue with that wholesale will increasingly be done in the asset management format. We have raised lot of funds, we have close to \$1.3 billion of credit strategy fund now in our asset management business and a lot wholesale strategies because we think wholesale strategies are good, they are very profitable but they need some flexible ALM they need some flexibility in structuring which is best done in an asset management format and we have a reasonable size wholesale book. So, we will continue to grow retail and we expect by next year retail should be 50% three years after that we think retail should be between 65%-70% of the total book and that is our stated objective over the last few years. We also see that the credit book end of FY19 over FY18 will still be a growth. As we are saying about profit for FY19 will be about 15%-18% growth over FY18 and the credit book will also see a growth because there was a growth in the first half there was de-growth in the third quarter and there will be some growth back in Q4. So, at the end of Q4 FY19 we will still be able to have some growth over FY18. So, I think on a year basis it is a good thing and that is what we always say if you see our quarterly chart when they are taper tantrum happened for two, three quarter we did scale back, our profits came down, our overall asset base came down, but we were able to scale up fast enough.

We think we have a very agile business model which can be calibrated for risk environment but also can be calibrated for growth environment. So, growth environment comes back as risk environment start going away because last quarter was a high-risk environment now risk will recede and what we have seen in India the way I think creditors all the other businesses will be, you have 8,10 quarters of growth environment and then one or two quarters of risk environment. So If you can dance this well between growth environment and risk environment you will build a much stronger model than just having a model which can only dance to the growth environment and not manage the risk environment which unfortunately or fortunately in India will happen from time-to-time.

Renish Bhuv: Sir in asset management business we have seen very seen sharp increase in PAT on sequential basis from Rs 14 crore to Rs 25 crore, any particular reason for that I mean is that because of that recent AIF fund launched I mean some fees might have come through or is there any other reason for that?

Rashesh Shah: It has actually been largely closure of the funds and deployment of some of as you know in credit funds though you have committed capital you do not get fees on committed capital you get fees on deployed capital and it is a fairly highly operating leverage business because even in the Q2 we did deploy some of the money on the credit strategies the real fee of that came for the whole of Q3 and a lot of that ends up being profit because you had already incurred the cost and now earning fee on that. So, on our credit funds we have almost half the money is un-deployed, but as we deploy that money we will obviously scale up AUM also, but there another factor, how is your deployed AUM upon committed AUM. We have currently at about 50% and you should see this as we deploy more money and as we close more funds, we should be able to get the income on that our cost structure will be more or less the same. So a lot of that incremental income should impact profits.

Renish Bhuv: Sir is it possible to quantify the unrealized revenue on this fund if possible?

Rashesh Shah: Hard to quantify because we do not know when it will get deployed because we might deploy something in Q3. When we deploy we earn, we starting earning fees. The cost

of the fund manager and all has already been incurred so you are already incurring the cost, but if you not deploy you do not earn. Unlike private equity where even if you have not deployed money you keep on earning fees, but in credit funds all over the world because credit fund is IRR based so customer will pay you fees only when they start earning the return and the money is deployed. So, it is very hard to forecast what will happen in Q4 and Q5 because we have a pipeline of deals but as and when you deploy money you start earning fees and if you do it at the end of the quarter then you might not have an impact in this quarter, but the impact will be in the next quarter because that is when the fee will really start flowing in. So, it is very hard to do that. The other thing in asset management is because a lot of this funds also have a carry in that when you exit also you get some carry income on that is also hard to quantify and forecast, but usually whatever is your AUM you should get about 1% to 1.5% as carry but that comes in a cumulative basis in the end. So, if you have a transaction that was a five year transaction when you exit that transaction and you make the expected return you should get 4% to 5% as your carry income on that which will come cumulatively at the end of five year at the rate of say about 1% per year you will get at the end of it.

So, there is a lot of embedded carry value that is also there. So, when you deploy and when you exit you get carry income, but the bad news is that it is hard to estimate and put it in the model, but the good news is it can only add to the profit it cannot take away because we incurred all the cost.

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

Jignesh Shial: I just had two questions, number one, you already have stated that the NIM which has improved sequentially from 7.7% to 8.6% had a some component of ARC can you just quantify if the rise in yields or rise in margins how much is contributed because of the ARC part and pure credit business if you can tell us how the scenario would have been just to get a sense over that and the normal credit course how the margin should have planned out if you can quantify that part that is my first question?

Rashesh Shah: It has been given on slide 17, we have shown the Binani resolution impact is about Rs 48 crore. So, you can adjust for that in your model we have not done that because we see this income also part of normal income that is why we diversified model. So, not only we have a diversified business it is out there from retail credit to wholesale credit the ARC to asset management, wealth management we also have income diversification some quarter will get carry income but we might end up spending on expansion of the branch on the retail credit side. So, given all of that we have not done the breakup but we have given the estimate of how much is the ARC impact due to Binani and you can make that adjustment but we see if you see that slide on NIM that we have we do expect that we will be able to maintain that range that we have highlighted in that. So, if you see slide number 23 which gives you the NIM range and we always say the NIM will fluctuate between 7% to 8%. Unfortunately it is a wide range on a quarter by quarter it will fluctuate but we have shown over the last 12 quarter it has gone up and down, but along with that a lot of other things also adjusted and hence our growth has been fairly consistent as a result of that.

Jignesh Shial: Just a sub-question to it so in case if we are expecting a further resolution to come up little better because of even today Court ruling on promoters holding. So, we can say that probability of NIMs remaining on the higher side because of the resolution coming in quickly in the next couple of quarters would be better and I mean the NIMs would remain on the better trajectory in spite if the market for the overall rate come in little tighter for at least quarter or two, will that be a fair assumption?

Rashesh Shah: As we said on our investor day about three, four month ago we were almost about Rs 1,000 crore of what we think is the potential carry income and please take it as a very crude estimate, which should come over the next three years as we resolve a lot of the ARC cases which are already in the pipeline and there is enough visibility on resolution, but some will get resolved in the next quarter some will take another three quarters. We do not know as you have seen this Essar Steel it has been going on and recently NCLAT has said that they will resolve in by so and so date even after it is resolved when you actually get the funds in also take a time documentation all of that. So, on a quarter-to-quarter basis it is very hard to estimate but I would say we have estimated our potential carry income on ARC is about Rs 1,000 crore which we are hoping will come through in the next between 8 to 12 quarters.

Jignesh Shial: Second question is more on your developer finance part now many of the players are basically getting stuck in the last quarter, how is the scenario now looks like with the liquidity easing out, are you guys seeing not specific for Edelweiss portfolio but any stress building up on the large scale or in the mid-scale segment or do you think the things will start improving going forward any change that you are specifically noticing being on the ground so anything you can give more color on the developer finance portfolio from your side?

Rashesh Shah: I am happy you asked this question I think we have four, five things we are clearly seeing. First, we always look at projects we do not look at developers. So, for example we have almost about 89 borrowers, but 174 projects and the risk at a project SPV level. A large part of our funding book is in housing, 80% of that is below Rs 1 crore, say 80% of inventory is below Rs 1 crore of value and we have 174 projects. If you look at actually real estate and average project is between Rs 500 to Rs 1,000 crore and hence at a project level the risk is fairly contained. We are seeing that because of the lack of liquidity and the conservatism on this particular business the new projects are not getting launched. So, we have not seen any developer launch a new project because the funding is hard to tie up. We are also seeing that some cash flow slowdown from customers of buying flats happening because of home loan and all which happened in October, November but it is starting to normalize now. So, cash flows are little bit here and there. We have always been in our underwriting stage itself we build some sensitivity on cash flows coming in. We also are very proactive so even today we try and estimate then three-months down the or six months down the line which project and again this is our project level because in Edelweiss one of the things to say is we do not give credit to a developer we give it to a project. So, we are very project sensitive and estimate at our project level where we could have cash flow problems and what you do is when you anticipate those kinds of issues or if you are anticipating the developer is not able to execute because in real estate if the projects get completed then usually our risk is largely mitigated.

We have also changed the developers, we have the right to step in and change developers in every project that we fund. We usually work with the developers but when we think that things have come to a point where current developer is unable to execute, we have brought in a new developer as a development partner who can come and complete the project. We also can arrange for last mile funding, we have relationship with lot of global funds and stress funds and all who do last mile funding. Our own stressed asset fund also does last mile funding everything is on arm length basis. In our ARC and the stressed asset fund we have done about five last mile funding on real estate none of them was Edelweiss NBFC portfolio case, but there are funds available who are happy to come in with last mile funding for projects which need for completion financing and some projects you also do what are called bulk sales at a very discounted rate to high networth investors and family offices and even there interest has been fairly high to raise some cash.

So, there are ways and means that you have, there are tools that you have of trying to manage anticipated problems at a project level and when you have 174 projects,

we do expect that 10% to 15% of the projects will always be going through some difficulty or the other, but we believe that if you are proactive, if you have strong project monitoring skill set and we have ability to resolve it via all the ideas that I gave you should be able to manage problems that come about because housing is a real asset and people do buy homes on an ongoing basis.

Jignesh Shial:

Just a follow up to this you have been advocating that there would be consolidation segment itself and the large guys will become larger, do you think that phase has started already because of the turmoil that has started happening last quarter and number two with so many players who are not able to augment funding the guys were able to manage the balance sheet well will gain market share in coming quarters, do you think that scenario coming up or you think the competition will still remain stay for more players will enter.

Rashesh Shah:

I think what you are saying is true, but the actual reality is slightly more calibrated and nuanced and I will try and explain it. I think yes you are right there will be some consolidation that will happen which started when the real estate act was passed. The consolidation process started almost three years ago but remember the stress on the real estate industry has been there because the market has been stagnant for about five, six years then we have demonetization, then we had RERA, then we had GST so as a result of that some amount of consolidation was already there. I think the larger players will be more and more coming as development partners. In four or five of the projects in our portfolio also we are talking to the larger players who are willing to come in as the development partners and execute the project who are not going to put their balance sheet to work, but they are going to put their execution capability to work but that does help you mitigate the risk at a project level and what you found is project is economically viable getting a good quality development partner has got easier in the last quarter because a lot of these smaller developers they are very good at doing the initial work of getting the project off the ground, getting the approvals and getting all of that, but ability to execute in sales and marketing and all of that the larger developers the more established developers have an edge on that.

And what we will see is a collaboration , It is a combination where the smaller guys will play a role up to particular point get their economic benefit out of that then the larger guys will come in. All this is true only for economically viable projects because whether it is an SRA project or a redevelopment project there is a lot of grubby work to be done in the early stage which I think some of the smaller guys, that are not startups, they are guys who have been doing this for 18-20 years, but they do not have the brand name and the balance sheet strength to be able to handle any headwinds. So, I think they usually bring the project to a certain stage and then they will partner we are now encouraging a lot of them to partner at a very early stage. So, even today from the real estate fund, we have the credit fund book that we have when we see any project which is with a developer who is good but may not have the wherewithal to complete it. We encouraging them to bring in our development partner then only the funding can be processed for them from the fund that we have. So, I think the smaller guys will have a role to play, the larger guys will have a role to play and because of the new rules and regulations this is inevitable the market liquidity situation it just added one more factor to make this happen.

Jignesh Shial:

During last quarter many of the NBFCs and HFCs were finding it difficult to raise money and all, now with this do you think gradually the guys who are able to build up the balance sheet will gain more market share in the segment, do you think that will happen or do you think the new players will enter again?

Rashesh Shah:

I think the new players are entering there are lot of funds coming about. We ourselves have a fund so I think part of what the NBFCs will vacate, part of it will get grabbed by the funds also what earlier was happening NBFCs were not as focused on making sure that there is enough margin of safety there is enough cushion on that and I think

the developer the good quality developers are asking for much more longer dated funding which may not happen from NBFC, but which can happen from funds. So, I think part of the market share will move on this what is called structured credit whether it is real estate or corporate credit the structuring flexibility and the tenure and all what will now be required will increasingly allow funds to play a slightly bigger role. So, I think the market will now get shared between NBFCs and funds going forward.

Moderator: Ladies and gentlemen due to paucity of time this is the last question for today. For any further queries you can get in touch with the stakeholder relations team for further discussions. I would now like to hand the conference over to the management for their closing comments. Member of the managements you may please go ahead with your closing comments.

Rashesh Shah: Thanks a lot. As I said all of you have been very helpful interacting with us please continue to do that and if you have any specific questions our stakeholder team or IR team is there all of us are there. I also look forward to hearing from you getting input from you and interacting with you going forward. Thank you very much for being on the call.

Moderator: Thank you very much. Ladies and gentlemen on behalf of Edelweiss Financial Services that concludes this conference. Thank you all for joining us you may now discount your lines now.