"Ujjivan Financial Services Limited Q4 FY2019 Conference Call"

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Moderator: Ladies and gentlemen, good day, and welcome to the Ujjivan Financial Services Limited Q4 FY2019 Earnings Conference Call hosted by IIFL Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on the touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Abhishek Murarka from IIFL Securities Limited. Thank you, over to you, Sir.

Abhishek Murarka: Yes, thanks, Aman. Hi everyone, and good evening. Thanks for joining the fourth quarter earnings conference call. We thank management for giving us the opportunity to host this call, and we have the entire top management from Ujjivan. Mr. Ittira Davis, the Managing Director and CEO; and Mr. Deepak Khetan, CFO from Ujjivan Financial Services and from Ujjivan Small Finance Bank, we have Mr. Samit Ghosh, he is the Managing Director and CEO; Mr. Sanjay Kao, the Chief Business Officer; Mrs. Upma Goel, The Chief Financial Officer; Mr. Rajat Singh, who is the business Head for Micro Banking and Personal Loans; Ms. Sneh Thakur, who is the Head for Credit and Collections; and Mr. Murli Manohar, who is the National Manager, Financial Planning and Analysis. So we have the whole team. I will hand over the call now to the management for opening remarks and then we shall proceed for Q&A. Thanks, and over to you, Sir!

Samit Ghosh: Thank you, Abhishek. Good afternoon, and first, apologies for the delay. Welcome to our earnings call for the last quarter and the full year financial year 2019. We are pleased with our overall business and financial performance for the year.

The year was good in terms of all-around growth. We have achieved significant landmarks during this financial year. The start of the year was muted in terms of Micro Banking growth numbers. We closed the year on a high note and delivered as per guidance issued in Q1 and Q2 earnings calls.

The bank achieved highest-ever disbursement in the last quarter of Rs.3,728 Crores, up 29% in comparison to the previous quarter and 65% above the last quarter of the financial year 2018. This led to an increase in the loan book, which stands at Rs.11,049 Crores, a growth of 46% year-on-year and 18% quarter-to-quarter.

Micro Banking business has grown 34% year-on-year, surpassing our guidance of 20% annual growth. Currently, the Micro Banking book is pegged at Rs.9,354 Crores. The increase in the portfolio was due to a number of new initiatives undertaken by the Micro Banking team. Our focus was on opening new geographical areas around the branches, higher customer retention and new customer acquisition, resulting in an increment in the borrower base of 8% quarter-on-quarter. We expect Micro Banking to continue its robust growth in the next year 2020 as well.

Micro and Small business and Affordable Housing loan portfolio has witnessed significant improvement. MSE business has undergone transition following a customer relationship approach rather than earlier transaction-oriented approach. In the fourth quarter, MSE disbursed Rs.185 Crores, up 38% quarter-on-quarter and 153% over year-on-year with the early disbursement of Rs.496 Crores versus Rs.203 Crores in the previous year.

We have shifted our focus completely towards secured lending. Our housing business disbursement in the fourth quarter was Rs.195 Crores, up 25% quarter-on-quarter and 100% year-on-year with the yearly disbursal of Rs.590 Crores versus Rs.244 Crores in the previous year.

FIG loan book is at Rs.225 Crores. The last quarter disbursement was at Rs.125 Crores against Rs.75 Crores in the third quarter.

We chose our customers carefully, avoiding any serious ALM mismatch and have lent to NBFC-MFIs who were well known to us and required support during the tight liquidity period.

Ujjivan has a total network of 524 branches, including 474 banking outlets and 50 asset centers. 474 banking outlets include 120 unbanked rural centers, of which is 7 are business correspondence.

In full year 2019, a total of 287 of the 474 banking outlets were made operational.

In the current year, we plan to slow down our branch expansion, consolidate and end the year with 576 outlets. 50 would be conversion of our existing asset centers. New branches will focus on major areas like Bihar, Eastern UP and Gujarat, where there is hope for growth of all our businesses.

The unbanked rural centers are currently in Tamil Nadu, Karnataka, Odisha, West Bengal and Gujarat. Uttar Pradesh and Rajasthan are to be the new additional areas for the current year.

Our goal last year was to reduce our dependence on wholesale deposits and CDs. As of March 2019, retail deposit share of the total deposit increased to 37%, up from 11.3% in the previous year.

Our deposit customer base is expanding, led by conversion of our existing microfinance customers as well as open market acquisition of retail customers.

As of March 2019, we had 25 lakh deposit customers, up from 7 lakhs. This includes 6 lakhs new bank customers acquired through our branch banking.

Our senior citizen program has been an outstanding success. We introduced an enhanced Corporate Internet banking, point-of-sale terminal, salary processing and cash management for our business customers. This will help in building our current account balances from small and micro business segments and savings from their employees.

We have converted half of our MFI loan customers to bank customers as we onboard them at a time of loan disbursals.

By the end of this year, we will have on-boarded 95% of the microfinance customers. These customers provide us a very valuable savings base. This year, we are introducing family banking for this customer segment, which will see more active usage of savings accounts and increase in the recurring deposits.

Last year, 23% of our retail customer deposits were sourced through phone and mobile Internet banking channels. With physical banking outlets more or less completed, our focus is on leveraging this distribution infrastructure in conjunction with the robust digital platform to create a strong retail deposit base.

Our total active customer base has increased by 19% this year from 38.7 lakhs to 47.1 lakhs.

Our credit collection team had an outstanding year in reducing NPA levels and recovering from the default customer's post-demonetisation,our NNPA has improved to 0.3% versus 0.7% year-on-year. We had also adjusted our lending policies post-demonetisation and have built sustainable portfolio over the course of two years.

In addition, we have a dedicated collection team now for each business.

We are confident that we will maintain the credit cost within 100 basis points for FY19-20.

Earlier this month, we announced Nitin Chugh will join the bank in August 2019 as President and will work closely with me to ensure a smooth transition. He will take charge as the MD and CEO with effect from December 1, 2019. The requisite approval from the shareholders of the bank will be obtained prior to his taking charge. He was our top choice, and we are extremely happy that we have successfully completed this stage of succession plan on time. He is a career banker with around 25 years of experience and has led the digital success story of HDFC Bank. He also has extensive experience in retail banking across sales, distribution, credit card, retail assets, branch and phone banking, virtual relationship management and digital direct marketing. He has also headed product management for deposits and institutional sales. He has been an outstanding team leader. Nitin holds a bachelor's degree of technology and also a postgraduate diploma in management. With his track record and impeccable profile, he is the ideal candidate to bring the generational change in Ujjivan and take us on our ambitious journey to establish ourselves as a major mass-market bank in India.

We also are working on strengthening and bringing in new orientation of our Board of Directors with a view to the future. As all of you are aware, we have announced induction of Sachin Bansal on the Board of the bank. He is an iconic leader in e-commerce space and with phenomenal technology acumen and foresight. Sachin's guidance and direction will be very valuable in achieving Ujjivan's mission of creating a state-of-the-art mass-market bank.

Despite the heavy cost of transition and branch expansion growth in our business is quite noteworthy. Consolidated NII was up 41% year-on-year in full year 2019. We reported an ROA of 1.7% for the year in line with our guidance. Consolidated PAT for 2019 stood at Rs.198 Crores versus Rs.7 Crores in the previous year. Our priorities are now: to scale up our businesses, manage our costs closely and reengineer our processes in each business and function to improve productivity. We are confident that we will significantly lower the cost-to-income ratio and improve our ROA.

Regarding update on complying with SFB licensing norm of listing the SFB within three years, we have interacted at the highest levels of RBI and are working closely with them on ways how we can protect the interest of the UFSL shareholders and also comply with the licensing condition. We expect to finalize this plan soon.

During May 2019, Eastern Odisha was hit by Cyclone Fani affecting four districts, of which Puri was worst hit. Ujjivan has four branches in Puri and 7 in other three districts. Our initial focus was to provide relief to our staff and customers and get our branches and ATMs operational.

We are pleased to inform you that our ATMs were the first to be operational in many of the affected areas. This was highly appreciated by the cyclone-impacted population. Most branches have returned to business as usual. We are carrying out extensive post-cyclone repair work, which is funded by a trust, which is match funded by our staff and the bank. We will abide by the guidelines setup by the SLBC and RBI for debt relief. Our exposure in the seriously affected area is limited.

We have already shared our full year 2020 guidance as a part of the presentation uploaded on the exchanges. We are excited about the journey of becoming a state-of-the-art leading mass market bank with a strong retail and digital franchise.

Thank you very much and with this, I would like to hand over to Ittira, who is our CEO of Ujjivan Financial Services Limited, our holding company. Thank you, once again.

Ittira Davis: Thank you, Samit, and good evening. Before we get to the numbers, there are some bookkeeping matters that I would like to highlight. This is the first year that Ujjivan Financial Services, both at a standalone level and on a consolidated basis, has prepared the accounts on an IndAS basis, IndAS, and that is very important for you to note. However, all financials given in the press release are on IGAAP basis. These numbers are based on management reports. The purpose of the IGAAP financials is merely to provide an update on business performance and allow comparison to previous quarters. So please keep this carefully in mind when going through the accounts and also when reviewing financials going forward.

It is important that this has been done to comply with the regulation and Ujjivan small finance bank is a group of a handful of banks who have been able to complete this task on the IndAS.

Moving back to business, there are a few highlights that I would like to share with you. Overall, disbursements for the year were up 38% and for the gross loan book, it is 46%. Most important, net interest margin for financial year 2019 was 11.1% for the consolidated entity and 10.9% for the bank.

Consolidated profits, net profit, Rs.198 Crores, versus Rs.7 Crores in the previous year. And most importantly, capital adequacy for the bank stands at 18.9% with Tier 1 at 18.4%.

So I have been telling you a lot of good numbers, so I will stop here and give you more chance for questions and-answers. Thank you to IIFL for hosting this interaction and now over to the moderator.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. Ladies and gentlemen we will wait for a moment while the question queue assembles. The first question is from the line of Manish Ostwal from Nirmal Bang. Please go ahead.

Manish Ostwal: Thank you Sir for the opportunity. Very good set of numbers. My first question on the fee income growth potential outlook for medium-term because now we are growing balance sheet by 40%- 45%, and we would like to cross-sell our fee products also. So what is the potential we can see on the fee line, Sir?

Sanjay Kao: This is Sanjay Kao here. Currently, we are at 10% of our total book and have expanded our third-party products and opportunities as well on the fee lines that we have on our products, which are different lending products as well as our deposit products. So with the continued focus on growing these as well as cross-sell of other fee products, like the third-party products, we are looking at our customer-related fee line to grow handsomely. In addition, we also have PSLC income, which we expect to grow well over compared to what we have done this year. So in totality, that will give us a solid growth rate going into next year.

Samit Ghosh: So I just want to add to what Sanjay said. As you know, we have setup a huge network of branches and banking outlets and there is a huge potential to build our funds transfer business through this network, which has not been factored in the numbers. We want to build this business, which will be a source of fee income in the years to come, starting this year.

Ittira Davis: 50%.

Manish Ostwal: It has down the request of dilution of licensing norms for listing of SFB. So what is the current update on the same, Sir?

Samit Ghosh: So you are talking about the Business Standard report yesterday?

Manish Ostwal: Yes, Sir.

Samit Ghosh: Well, that was a totally unfounded report. As I have mentioned earlier, we had interaction with the governor a couple of months back on this issue of dual listing and the capital structure of small finance banks, and he had asked us to write a paper on that, which all of us from the small finance bank put together and have submitted it. Subsequently, we also met with the deputy governor and have given him another paper on the subject. We have not yet heard anything from RBI, but we expect to hear from them soon.

Manish Ostwal: Sure, Sir and last, for growth. When will you raise capital, Sir, and when we will reach 18% ROE?

Samit Ghosh: Sorry, when will we raise additional capital?

Manish Ostwal: For growth, Sir. Equity capital for growth?

Samit Ghosh: Yes,, we are trying to work at a solution. and We would obviously like to meet the licensing conditions of the small finance bank, keeping in mind the interest of our investors of the holding companyWe may have to raise a 20:33 token amount of capital by February of next year, which may be around 10% of our capital base. So that is something which we are preparing for till we hear the final word from RBI and we are also raising Tier 2 capital of about $50 million from IFC, which has been in the works for sometime and it is in the final stages. So if both of them come through, there will be a fair amount of capital for us for both organic and inorganic.

Manish Ostwal: And on the ROE, side Sir, 18% ROE, when we can achieve, Sir?

Ittira Davis: We should be there in three to four years.

Manish Ostwal: Thank you.

Moderator: Thank you. The next question is from the line of Praful Kumar from Pinpoint Asset Management. Please go ahead.

Praful Kumar: Thank you Sir and great set of numbers. Sir, just one question on the scheme itself that you mentioned. Now the past implications for scheme like something that your bank is doing are significantly high for us. So just wanted to understand what can be the best way out for protecting the minority shareholder within the holding company?

Samit Ghosh: So that is something we are working on with the Reserve Bank and we will let you know after we get a feedback from them. But definitely, protecting the minority shareholders is one of our top priorities and that is something, which we are working with RBI on that.

Praful Kumar: Sir, just one more question on the MFI So we are hearing that in West Bengal and Odisha, there is some overleveraging happening in the MFI sector. Anything that you have hooked up or anything that you can throw some light on that?

Rajat Singh: So actually in West Bengal, we are one of the oldest players. Bulk of our business is coming from repeat customers. We have been able to acquire some new customer in an existing catchment area as well. So in West Bengal, we are not seeing any challenge as of now, although competitive intensity has increased. But we are doing equally well and there is no sign of challenge there. In Odisha, there are few players, the whole industry has become quite large, but our presence is really limited. We just had 16 branches overall and restricted only on the Bhubaneswar and Puri area and part of Western Odisha area. So there also at least for our business and branches where we are present, we do not see any challenge.

Praful Kumar: And finally Sir, how many new customers you acquired in this financial year on the asset side. How many new customers we added? So AUM growth, just want to map versus new customer acquisition?

Rajat Singh: New customer acquisition close to 3 lakhs.

Rajat Singh: Incremental borrowers, we have added. If you look at only new customer number will be slightly higher. So incremental borrowers are close to 3 lakhs.

Praful Kumar: Incremental borrowers, done Sir.. Thank you very much.

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

Nidhesh Jain: Thanks for the opportunity Sir. Any guidance from a three to five-year perspective on ARPU and sustainable leverage that you would like to have for a business model like us?

Rajat Singh: Nidhesh, we have given a guidance of around 17% to 18% of ROE in three to four years.

Nidhesh Jain: Okay and leverage, what should we assume there or.

Rajat Singh: 6.5.

Nidhesh Jain: 6.5 lakhs. Secondly on the microfinance, can you share the number of customers which are unique to us, which have taken loan only from us and how are you seeing the leverage level at the individual customer level moving in the last two to three years?

Rajat Singh: So unique customer who have taken loan from Ujjivan is close to 15% and movement of customers from group loan to individual has started taking place. From last two quarters, and we are seeing good traction there. In coming years, we are expected to increase our Individual Loan businesses from 8%- 9% today to close to 12%,-13%.

Upma Goel: So just to add to that, the unique customers in total stands at 33%, of which 15% are new to the bank.

Nidhesh Jain: So the customers which have taken only loan from Ujjivan is 33%, that is right?

Upma Goel: Yes, 33%.

Nidhesh Jain: Okay and just last, bookkeeping question is if you can share the breakup of operating income and other income for the quarter and full year, that would be useful and what is the write-back we have seen from the loans, which were written off during demonetization period, any quantum on that?

Sneh Thakur: So the write-off recoveries for the year is Rs.20.8 Crores and the efforts will continue this year as well.

Samit Ghosh: The breakup of other income is Rs.35 Crores processing fee. I am talking about Q4.

Nidhesh Jain: Yes.

Samit Ghosh: Rs.3.9 Crores of securitization income; Rs.3 Crores of PSLC income; Rs.31 Crores of interest on investment, which is largely your SLR deposits. Rs.10.5 Crores of bad debt recovery; Rs.7.6 Crores of other fee income, Rs.8.3 Crores of miscellaneous income, Rs.502 Crores of interest on loan.

Nidhesh Jain: Sure. Thank you Sir.

Moderator: Thank you. The next question is from the line of Nishant Shah from Macquarie. Please go ahead.

Nishant Shah: So a couple of questions. Firstly, focusing towards the rural banking side. I believe this is something new, which we have started in the last couple of quarters. So could you just like tell us about how you are going to go about doing this business because this is a little bit different from the urban and semi-urban lending that you have been doing? So the customer segment is inherently a little bit different. So how are you going about this, are you shifting over from a monthly to a weekly collection, any such color that you can give on the qualitative aspect of this lending would be awesome.

Sanjay Kao: So while we have talked about rural banking separately, over the years, we have been dealing with the rural segment for many years now. If you look at our semi-urban branches, a few kilometers from the semi-urban branches we have rural customers to whom we have been lending over a decade. So this customer base is not new to us. What has happened is that when you go out to visit a new unbanked rural center we will address those customers additionally.. Number two, it is also given us an option to acquire new male groups and mixed groups. Earlier, we were onboarding only women groups. Now we have both men and mixed groups. So that has given us an opportunity to grow with this segment and actually capitalize, as we did with our existing semi urban branches. This is with our traditional products. Then we have launched rural products as well, which are livestock and sericulture, etc. One of the mandate is whenever we have done any group loan or individual loan there is a monthly payment, but anything associated with the agri side, apart from monthly payment, we establish a regular customer connect. In terms of collection, we will continue with our monthly cycle. We are not moving to a weekly cycle..

Nishant Shah: Okay. May I ask why not? Because like the thesis was that like a monthly cycle is preferred in urban because it is more salaried, kind of domestic help, all those kind of drivers or all those kind of customers who earn on a monthly basis. So moving to rural and other players in the rural areas are - weekly or fortnightly, they will probably have a much better command. So why not move to a weekly cycle here because the risk might be a little bit different?

Rajat Kumar Singh: Look, Nishant as Sanjay Sir was telling earlier even in our prior experience in the semi-urban and rural area, we have been running monthly cycle. It is a question of creating right habits. 75% of our customers are self-employed in both urban and rural areas and are quite happy with monthly cycle payment structure. On-time repayment in semi urban branches with monthly cycle has been spectacular. So if there is a need to change the repayment cycle, we will definitely look into it, but given our experience so far, we do not see any requirement as such. In fact, some of the products, we are also exploring possibility of standing instructions, which is working out well.

The mixed and male group which Mr. Kao was referring to earlier is also doing well with the Standing Instruction practice.

Nishant Shah: Sorry, okay. Fine, so this addresses it. A question again on the Eastern geographies. So now given that we are probably only 33% customer base, which is like unique to us and when you have like other players commenting that there is some bit of over leveraging going on in West Bengal and Odisha. So our current portfolio - like do we have a sense on how the on-ground leverages for the customers that we own to the ones that we lend who are not exclusive to us? So we may not be over leveraging them but the other guys would be doing that. So any sense that you are having over there how that kind of leverage is moving?

Rajat Kumar Singh: I mean, our overall exposure is kept at Rs.1 lakh and I think that has generally been followed by everyone across the industry. Exposure goes to Rs.1.5 lakh only in 15% cases where we see customer also has some kind of retail exposure. So 80% of our customers will have exposure restricted at Rs.1 lakh and I believe industry also has similar kind of exposure. There are some people who are actually willing to take the whole exposure and give a larger ticket size loan to customers. In such cases, we exit those customers and looking for white spaces where we can grow. However, as you know, the 70% of our business is coming from repeat customers. We are more or less able to hold that existing customer base with us.

Nishant Shah: I will come back in the queue for more. Thank you.

Moderator: Thank you. The next question is from the line of Pranav Mehta from ValueQuest. Please go ahead.

Pranav Mehta: Good evening Sir. Congratulations on a great set of numbers. First question is on these new business lines that we have mentioned in our presentation specifically about the vehicle finance, 2-wheeler and 3-wheeler that we are going to launch this year. If you can just share more details on like what kind of geographies are we targeting and what kind of loan book are we targeting in this segment in the medium term? And the second question is on the cost side, why you have given a guidance of 72% cost-to-income for FY2020. And so within that, what kind of absolute growth in operating expenses are we factoring in?

Sanjay Kao: Okay. So let me take the vehicle finance part first. Vehicle finance is something, which we are going in with 3-wheeler and 2-wheeler loans. We are going to pilot both the 3-wheeler in the electric and the nonelectric segment and we were essentially piloting in 40 branches across the Eastern states and the Southern states. On the basis how, the entire distribution system flows we will take it Pan-India in coming 3 to 4 months. As far as 2-wheelers are concerned, we will launch sometime around August this year. On the basis how this products pans out we will move to pan India level in about another four to five months. We also have in the pipe the 4-wheeler commercial segment, small commercial vehicles as well as huge passenger vehicles. That would be brought into operations towards the end of the year.

Upma Goel: On the cost side, we are expecting a 40% growth in our opex, which is at present it is Rs.1000 Crores. From Rs.1000 Crores we are expecting Rs.1400 Crores. But when we look into the book growth it will be close to 55%.

Pranav Mehta: Right. So if I can just ask this further, 40% growth in opex seems a little bit elevated, especially considering the fact that most of our banking outlet conversions are happening this year. And FY2020, the pace of banking outlets opening will be much lower than FY2019. So given this 40% just number seems to be a little bit high. So if you can just explain that.

Samit Ghosh: So actually most of the branch expansion in the last year has happened during the second half. So the running cost of branches in terms of personal and another process will continue for this full year. The other impact we have is on the performance side, we will have the usual growth and a portion of cost will be incurred due to expansion in employee base in order to promote our family banking segment. Also as the new branches are rolled out, we will be converting a total of 100 new banking branches this coming year.. So all these are contributing to a rise in the cost, but we will also have a good growth in income in the coming year. By this we hope to control the cost-to-income ratio.

Pranav Mehta: Thank you and all the best.

Moderator: Thank you. The next question is from the line of M.B. Mahesh from Kotak Securities. Please go ahead.

M.B. Mahesh: Good afternoon. Just a continuation of a previous question again. So even if you analyze the - one, there has been a sharp increase of about 30% on other costs this quarter. Just trying to understand why has that happened. And also the fact that even if you analyze the fourth quarter numbers, it is still around Rs.1200 Crores. Just trying to understand why we kind of assuming the Rs.1400 Crores opex for next financial year knowing that even the branch expansion is going to happen over a period in time. That is my first question. And consequently, the ROE seems to have been pushed back by a couple of years on the back of that, the improvement, at least, direction. Second, a question to Rajat. Is it possible for you to give the per customer ticket size as well? Because it is quite possible that the customer may have multiple products with you. And also why has been - any worry that Tamil Nadu is now seeing a much, much faster growth out there? Thanks.

Rajat Kumar Singh: Okay. So I will take the second question first. I think the number we have given is more or less per customer ticket size. At this moment, we do not have multiple product running for same customer. It is largely one loan per one customer. So you can take that number as per customer number as of March 2019. In Tamil Nadu, , this is one of the areas where, Micro Banking business as well as overall economy is doing well. In last three to six months, based on relaxation of some of the policies and additional hiring, this area has done significantly well. So most of the growth has come from increased staff productivity, addition of area in existing branches and growth of individual loan business. So these are the three things which has contributed to our growth in Tamil Nadu. We have also opened few branches there but those branches are insignificant in terms of pushing growth. Lastly, growth was also on account of stock productivity, individual loan growth and area expansion are in existing branches.

M.B. Mahesh: Sorry. Just one clarification, Rajat. At the time of the IPO, I think one of the kind of overstated internal philosophy was that you would not want to have any state having more than 15% market share in your portfolio. But Tamil Nadu has now touched about 17%. Any thoughts on that?

Rajat Kumar Singh: Right. So I think it is more of a temporary aberration. I think in coming time, we would like to keep it between 15%- 16%.

Upma Goel: As far as concentration risk is concerned, the bank philosophy is to keep it within 20%, not 15%.

M.B. Mahesh: Okay, sure. And the opex part?

Upma Goel: On the opex side, when we look into the Q4 numbers, one of the major reasons is we have opened close to 280 of banking outlets last year and the majority of service bank or banking outlets got staggered over the period. The entire impact has come into the Q4 when most of the branches came into operations, so effectively, yes, our operating cost has really gone up and all other associated costs as far as the Q4 is concerned.. We have been opening new branches, launching new business lines and we will also be sponsoring into family banking. All this will require investment into our personnel. Hence, there will be increase in the personnel costs.. Plus, we have infrastructure investments so there will be an impact on account of the depreciation in IT and all other expenses. Definitely, we are getting the benefit of induction of the various resources.. All this in totality, will have a positive impact on the opex next year.

M.B. Mahesh: I will just come back again in the question queue on the cost again. Thanks.

Moderator: Thank you. The next question is from the line of Viraj Mehta from Equirus PMS. Please go ahead.

Viraj Mehta: Sir, just wanted your view - if I go back to your presentation 1.5 years back and if I go back to your presentation six months back, the objective about bringing cost to income down from high 70s to early 70s to mid-60s has been a continuous endeavor. But we have seen absolutely no traction in that region in spite of having very high growth in our NII and our loan book. As an investor, it just worries us that if our growth slows down in any of these areas, our cost to income, instead of going down will start ballooning up. What is your view on that?

Deepak Khetan: So you were right in your analysis that our cost has now built up. So now is the time that we have to continue to scale up and that is how the portfolios will grow, our incomes will grow and we will be able to leverage our investment. So it is absolutely essential for us to continue to grow, and we are confident that we will be on this growth path for the coming time.

Samit Ghosh: So in addition to that, that is an area of our focus, cost growth. Obviously, by scaling up our business, the cost-to-income ratio will drop. But at the same time, we are implementing measures to cut down our cost as far as possible, bring in higher productivity, etc. So that is one special sort of focus for us in this financial year. –Hence, are looking at it, both in terms of scaling up our business and also cutting down and looking at individual costs, individual processes, increasing productivity, higher levels of automation, etc. So that is a special focus of us. I mean as much as it is a concern for you all, it is a concern for us also. But rest assured that is one of our primary area of focus this year.

Ittira Davis: As an example, we can say that the new branches which will be opened will be of lower cost than the previous branches. That is a start we have already taken a decision on.

Viraj Mehta: Sure Sir. Thank you.

Moderator: Thank you. The next question is from the line of Gaurav Jani from Centrum Broking. Please go ahead.

Gaurav Jani: Thank you for taking my question Sir. Firstly, just a book keeping one. So the tax has - the percentage tax has reduced this quarter. I mean what would be the reason for that?

Upma Goel: So for this quarter, the effective tax rate is 11.8%. So one of the reasons for the reduction in the tax rate is on account of the benefit, which we have availed under Section 80JJAA, which is close to 3.5%.

Gaurav Jani: Okay. Can you elaborate on that? I mean, what is this benefit regarding?

Upma Goel: So Section 80JJAA talks about - basically, it is a section which has been introduced for the service sector. It is a tax relief on the additional employment generation where we are paying to the employees a gross salary less than or close to Rs 25,000 per month. As, most of our staff comes under this category so we are able to get the benefit. This is the tax relief, which we have accounted in the Q4.

Gaurav Jani: Okay. So next year any guidance on whether we will receive this benefit or how will that pan out?

Upma Goel: Yes, so this benefit, say for example, we are spending Rs.100 we will get Rs.190 spread over next three years. So next year also, we will be getting this benefit.

Gaurav Jani: Okay. Because if I average the tax, that comes out to about 26.5% for the full year. So would that be the same for the next year because we have been at about 30-plus or 33-plus actually.

Upma Goel: So when we look into our effective tax rate, it comes out to be 25.78% for the full year. In terms of this - the lower tax rate is one thing I talked about the 80JJAA benefit. Second is about the tax rate, which is applicable to us during this financial year, which is 25%. If you remember, as per the Finance Act 2018, this is a special benefit which is given to the company having turnover less than Rs.250 Crores in the financial year ending FY2017.. Next year, our tax rate goes back to the 34.99%. Having said so, we will continue to get the benefit of the 80JJAA in the next year also.

Gaurav Jani: Got that. Secondly, Sir, if I had to ask you - this question is directed to Samit Sir or Rajat Sir. If I back calculate the ticket size, the growth in customers in the MFI book is about 25%. So can you throw some light as to what sort of customers are these? I mean, are they first-time borrowers or which regions are they from? Any some color on that would be appreciated.

Rajat Kumar Singh: Yes, sure. So customer growth, which we are getting, is a function of both, new to the industry and some of them have already some kind of relationship with other microfinance institution. That is almost 50-50. And bulk of the growth has come from states like Assam, Odisha, Rajasthan, Tamil Nadu. So growth is also quite well spread across these regions as well as in Haryana and Gujarat. So talking about our top 10 states - we are getting good traction in new customer acquisition across all of them.

Gaurav Jani: Okay. Also, if I had to ask you, so what sort of a growth - because earlier, I think you were guiding for about 30-odd percent growth now with the costs being elevated, what sort of and we ended FY2019 pretty robustly at about 46-odd percent. What sort of growth guidance do you give for the next two years?

Deepak Khetan: For the next year, we have given a guidance of 35% to 40% growth on our AUM?

Gaurav Jani: Okay, next year meaning FY2021?

Deepak Khetan: FY2020.

Upma Goel: FY2020.

Gaurav Jani: Okay. And how much would that be in 2021?

Deepak Khetan: We should continue to grow in the same range.

Gaurav Jani: Okay, got that. Lastly, if I had to ask you, I mean any challenges in the Odisha portfolio because of the cyclone? We have about 3.4% exposure? I mean you did mention that is focused in certain areas but any sort of - any color you want to give on that?

Sneh Thakur: Like Mr. Ghosh as mentioned in the opening speech, we have only one business, which is badly impacted, which is Puri. We have four branches in that district. The portfolio is very small and the impact is yet to be ascertained. At the moment, we are focusing on providing relief to them in accordance to the SLBC guidelines we have received. So we will be looking at providing some repayment holiday and in due course of time, we will be able to establish the exact impact on our P&L.

Rajat Kumar Singh: Just want to add here that the impact in these four branches will definitely be lower than what we have seen in Kerala last year. So I mean the impact will be much smaller.

Gaurav Jani: Okay. Got that. Lastly, Sir, this question is for Samit, Sir. When do we get some clarity from the RBI on the listing? I mean, I think a lot of investors would be waiting for that. So that would be appreciated or probably you know when would...

Samit Ghosh: We are also waiting for that and we are hoping that we would be able to meet them again sometime in the first half of June and get some kind of a feedback on that and work out some kind of a resolution, so first half of June hopefully.

Gaurav Jani: Okay. So that is when they will come out with the guidelines?

Samit Ghosh: No, I do not know if they will come up with guidelines or they will give us a specific direction because both Equitas and us are running short of time. You can reach out to them specifically. So they might give some kind of direct guidance in terms of how do we go forward.

Gaurav Jani: Got that Sir. That is, it from my side. Thank you.

Moderator: Thank you. The next question is from the line of Rohan Mandora from Equirius Securities. Please go ahead.

Rohan Mandora: Thanks for the opportunity. Sir, with respect to the data on Slide 45, the Tier 1 capital absolute amount. It is going from Rs.1601 Crores to Rs.1632 Crores to Rs.1653 Crores. So Sir, on the Tier 1 capital, if we add the profitability for each of the quarters, the number should have been higher. What is the adjustment there?

Upma Goel: This is the adjustment is on account of preference dividend, which we have paid to our holding company amounting to Rs.26 Crores.

Rohan Mandora: Okay. Got it. And Sir just want to get your thought process like as we convert around 95% of the MFI group customers into liability customers, how do you see the relationship ROE trajectory over the next three to five years in this pool of customers?

Rajat Kumar Singh: So at customer level we will be providing additional products and services at incremental cost, so we expect our ROE to be, in microfinance business, more or less close to 3.5% because with additional products which we are giving especially on the deposit side and third-party side. The income will kind of compensate the cost of servicing these savings account Also as we progress in some of the areas, where customer goes digital and cashless., it can substantially reduce our cost of operation at customer level overall, not only on deposit side. So if we start seeing benefit of that, there is further scope for improvement. But at this moment, we see more this being stable.

Ittira Davis: In relation to that, any new product that we will be launching on the micro banking side as well as in microfinance, they will all be cross-sold to our existing customers, mostly through our current distribution system. So the incremental revenue that we draw out of these customers will come at a minimal distribution cost to us. So from a ROA perspective, we will continue to enjoy what we have been doing all these years.

Rohan Mandora: Sure, Sir. And Sir lastly, hypothetically, if you have to list the SFB, assuming that RBI does not give any other leeway's, then is a reverse merger two years down the line a possibility?

Samit Ghosh: Those are the issues, which we are discussing with RBI.

Rohan Mandora: Thanks a lot.

Moderator: Thank you. Next question is from the line of Venkat Subramanian from Organic Capital. Please go ahead.

Venkat Subramanian: Thanks for the opportunity. Predictably, the question again is on cost to income. As the previous participant asked, we have tackled that 70% kind of range. The levers for reducing cost to income are well known. Where do we have broadly guided that in about a couple of years, we will get down to a sub-60 kind of level, closer to 60. So can you give us a direction over - starting next year?

Upma Goel: On the cost-to-income ratio, next year, we are expecting to be around 70% to 72%. And then as we go ahead, the next three to five years we are expecting our cost-to-income ratio to be around 55%. The levers that we are looking at present are definitely, to contain our overall cost we are incurring. So we are taking into account a lot of initiatives, whereby, we are looking into the renegotiation of a large contract process engineering and part of other initiatives. With the increase in business scale and the increase in fee income, we are very much confident that we are able to bring down our overall cost-to-income ratio in the range of around 55% in the next five years.

Venkat Subramanian: This would be, what? From 70% to 72%, it can come down to 65%? Is it going to be a steep drop almost about 5% basis points in about each year? That is what is being implied, right?

Upma Goel: Yes. So I will tell you what happens. On the cost side, we are taking a lot of initiatives of reducing our costs or containing our costs. What has happened is now our branch count is close to 500 and it will continue to grow over a period of time. Our fee income, remittance fees and other fee income which is primarily on account of banking operations. will grow substantially benefitting from the scale of business. We expect to grow in the range of around 35% to 40% of our fee income from increase in banking operations. Our income from third-party products, also is also expected to grow going ahead. We are seeing huge growth in income and PSLC is definitely going to benefit us. Overall, we expect to reduce our cost-to-income ratio to the level of around 55% in the next three to five years.

Venkat Subramanian: In the current model that we operate, what scope do we have for this CASA to increase the current 10% kind of range to a much higher number?

Ittira Davis: So one of the focus areas that we have obviously, is to build CASA. We are strongly cognizant of that requirement. To that extent, we have built our strategy to build our CASA products, which is around the fact that we have created specific segments. We have identified specific segments in the mass market, which will be the seven segments that we will be addressing through an approach, which is collaborative across all our business verticals and that approach is based on providing a solution as opposed to selling a product. In light of the fact that we want to grow from 10x in terms of customers, we have realized that it is impossible to do that by selling just a product, we have to sell a solution. So one aspect is identifying the segment that we will approach. Second is in terms of product embellishment, we have embellished each of our products, worked each of our products and embellished our product in a way by which they are differentiated and become well differentiated in the segments that we are operating in. I mean, we have introduced, for example, stuff like cash management service, we have introduced a state-of-the-art Corporate Internet Banking service and have also piloted that initially and the initial pilots are showing a handsome growth in terms of our CA volumes. Wherever they are now growing, leveraging 5x over what our traditional CA volume has been. We have introduced a key management solution where we are addressing the school, the college segment. We have tied up with e-Shiksha who is a fee solution provider. So there is again a product embellishment, which is happening on CA and SA segment, which is able to drive the numbers dramatically up.

We are looking to grow our CASA as our total deposits from 11% currently to 16% across as per our guidance

Moderator: Thank you. The next question is from the line of Gautam Jain from GCJ Financial. Please go ahead.

Gautam Jain: Sir, that we have revised our growth target. We have achieved more than what we said this year also. So as you said that we want to 10x our business in next seven years. Is it safe to assume our book size of over 1 lakh Crores by 2026?

Ittira Davis: So actually, we have not given any guidance on the book size of 10x in seven years it was on the customer numbers, but we will come up with guidance on our growth. So as of now, the guidance continues to be that we will grow in the range of 35%- 40% year-on-year.

Gautam Jain: Okay. And what is the reason of tax rate being low this year?

Deepak Kkhetan: I think that has been explained in detail but Gautam I will take that question one-on-one with you. We have already given that.

Gautam Jain: Thank you Sir and all the best.

Moderator: Thank you. The next question is from the line of Sonia Lalwani from Purnartha Investments. Please go ahead.

Sonia Lalwani: Congratulations on a very good set of numbers. So the questions have been answered, but just two or three questions. Sir, I would like to understand what is the potential of a branch if you say in a semi-urban, rural and in urban area from the perspective of AUM disbursement? So what new branch can achieve, what size?

Ittira Davis: All right. Sonia, okay, so we assess that based on different sets of branches and different tiers of cities that we have. We have currently an asset base which is coming from the asset sector before we convert it into branches. So it is a difficult one to pinpoint saying that we are expecting a certain level of growth because the level of growth, wherever we have been, has been good. We do a pretty extensive analysis in terms of what it would be the branches, what kind of asset size, what kind of deposit, nature of deposit, what is the customer base, etc. So we look at multiple things to be able to assess where we have to get to. But to be very specific with a response to what you want, I think it will take a long time to answer, because we have to go market-by-market in numerous spots. I do not think we can do that here. But rest assured, it is something that we track by every market.

Sonia Lalwani: Okay, what will be the opex for a new branch?

Ittira Davis: The opex would be around 3.5 lakhs per month.

Sonia Lalwani: 3.5 lakhs per month. It is on average, like assuming average of semi-urban, rural and...

Ittira Davis: Sure.

Sonia Lalwani: Okay. And Sir, when you say that MFI book will reach 70% by FY2021. So I wanted to know do you include Group Loans and Individual Loans. Or is it only about the Group Loans part of it?

Ittira Davis: Both Group and Individual Loans are offered under the microfinance program.

Sonia Lalwani: So you expect the proportion of both these loans to be 70% by FY2021?

Ittira Davis: Yes, the combined number, yes.

Sonia Lalwani: The combined number will be, yes.

Ittira Davis: Yes.

Sonia Lalwani: And Sir, could you throw some light on the tax rate. I mean, earlier participants also asked about it and many participants as well. But it is not clear why the tax rate has been so low at 12% for the quarter?

Deepak Khetan: Sonia, Upma already answered that. I will take that question one-on-one with you. It is largely, because of the benefit under Section 80JJAA and 25% corporate tax rate that was applicable to bank, because in the financial year FY2017-2018, the top line was less than Rs.250 Crores. So that is broadly the answer, and I will take that with you one-on-one.

Sonia Lalwani: Sure Sir. Thank you.

Moderator: Thank you. Ladies and gentlemen, that would be the last question for today. I now hand the conference over to Mr. Ittira Davis for closing comments. Thank you and over to you!

Ittira Davis: I would like to thank all the participants who joined us today. Good set of questions. And I thank IIFL for hosting this and look forward to seeing you on the next call. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of IIFL Securities Limited that concludes this conference. Thank you all for joining us. You may now disconnect your lines.