"Indiabulls Housing Finance Limited
Q1 FY 2017 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Indiabulls Housing Finance Limited Q1 FY2017 Earnings Call hosted by UBS Securities. As a reminder, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ishank Kumar. Thank you and over to you Sir!

Ishank Kumar: Good evening everyone and thank you for joining us today. I would like to welcome the management team of Indiabulls Housing Finance. We have with us Mr. Gagan Banga – Vice Chairman and Managing Director, Mr. Ashwini Hooda– Deputy Managing Director, Mr. Mukesh Garg – Chief Financial Officer, Mr. Pinank Shah – Head, Treasury and Mr. Ramnath Shenoy – Executive Vice President, Investor Relation. I now invite Mr. Banga to provide key highlights of results. Over to you Sir!

Gagan Banga: A very good day to all of you and I welcome you to the Q1 2016-2017 earning call. I am immensely happy to announce that we are launching e-home loans; a cutting edge technology enabled paperless, home loan solution that can be end-to-end fulfilled from your mobile or computer. This is an industry first and it has manifold advantages to our customers and to Indiabulls Housing. E-home loans offer unmatched customer convenience. Indiabulls home loan branch has effectively moved to the customers mobile and we can access IBHFL's different branch 24x7 at its convenience from any location.

In the traditional home loan fulfillment scenario the application process would begin with the loan sales executive taking an appointment to come fill the form and collect documents. This would normally take one to two days and would be done only during working hours. Application form filling and document upload is now a 10 to 15 minute process which can be done anytime from anywhere 24x7.

We are both furthering and our beneficiaries of the Prime Minister's and the Government of India's Digital India Campaign and I have tied up with UIDAI Aadhar for e-signature and eKYC eliminating several repeated signatures and many sets of document. Verified information photograph etc., flows automatically from the UIDAI database and populates the application form. Videos and multimedia tutorials handhold the customer through the application process. Personalised call support is just a click away by phone or on chat. Within a few working hours of 15 minute application being submitted a firm sanction is received. Presently, from a legal enforceability perspective, property document still need to be physically collected and maintained which necessitates one single visit.

On submission of this, the disbursal process for the initial as well as subsequent disbursal is again online and funds seamlessly get transferred to the seller or the builder. The benefit to Indiabulls housing is tremendous. Our brand awareness and presence leap frogs ahead. Our association has a technology enabled brand will be cemented especially with a target age group of 30 to 35 years. Operational expense will reduce accelerating the decline in cost to income.

Manpower requirement is reduced and so is the need for a full-fledged, all fills brick and mortar branch. Our reach will expand into tier II, tier II and tier IV towns and with the NRI community without the need to establish numerous branches. Productivity of existing employees will also increase. For the sales team for example travel time for multiple meeting to get application forms filled and to fill document is cut down. As information gets populated automatically from their application form and submitted documents, manual error prone data entry is eliminated permitting the credit to focus on underwriting.

Another very important rub-off is the transformation in the organization the internal culture to one that is technology centered and technology focused. In implementing the e-home loans solution we are grateful to our technology partners for their help and guidance. UIDAI for e-signature and eKYC through Aadhar, NSDL and C-DAC for PAN verification, Samsung for retina iris reading tablets for biometric eKYC. Perfios a Bangalore based Fin-Tech Company for the documents reading solution and bank statement analysis solution. This solution removes the hassle of printing, scanning bank documents which customers can directly provide it by logging into the net banking credentials whereas IBHFL credit team get pre-analyzed ratios and reports thereby enabling faster appraisal of home loan application.

I will now move on to provide you with some macro flavor on the home loan sector. As per July 2016 research report on Indian real estate published by Knight Frank, the residential sales in the top six cities witnessed a strong uptick in H1 2016. Mumbai and Bangalore lead the pack registering growth of 23% and 18% respectively. According to the Real Estate Research and Analysis Company Liases Foras, affordable housing segment has the largest share of total residential sale with more than 70% of the total units sold.

This has resulted in a 46% year-on-year growth in the sales of the affordable housing segment. Overall in the first half of the calendar we saw increased traction in the primary market and inventory levels with builders have declined. Real estate developers too are seeing strong pickup in sales. According to the same report commercial real estate also continue to put in its positive momentum and pose a 12% year-on-year growth in transaction volume. Hyderabad continues to witness strong demand for office space and registered 91% YoY growth. Mumbai recorded a 50% growth. Continuing an upward movement in most of the regions, average rent has shot up to 8% in the first half. A total of 17 million square feet of additional office space has been leased out in the first half. This is expected to pick up further space and to beat the calendar 2015 leasing of 40.2 million square feet which was the second highest only after 2011.

Office space inventory is at a five year low. As I have spoken about it in the past the general rule of thumb is 100 square feet of office space requires a 1000 square feet of residential space and leasing activity is the highest in the suburban and peripheral localities, which coincides with the availability of affordable housing. Housing finance companies continue to witness steady growth outfacing the market growth and capturing market share from public sector and foreign banks. According to RBI's half yearly financial stability report release in June 2016 banking NPAs for all scheduled commercial banks put together is at 7.6% and for public sector banks is 9.6%, foreign banks is 4.2%. Compared to this the NP of housing finance company is only at about 1.1% with the average NPA for the top four housing finance companies is between 80 and 90 basis points.

This will permit housing finance companies to profitability conduct housing finance business and expand both the market as well as capture market share from public sector banks and foreign banks. Indiabulls Housing is further benefited from the fact that despite being the second largest private housing finance company our market share of incremental housing is only currently at about 6% amongst all banks and housing finance companies. As our employee productivity operations and distribution reaches near optimum level IBHFL is perfectly poised to outpace market growth which itself will grow aggressively given all the positive policy changes made by the government earlier this year, which were detailed in our previous earnings call.

The housing finance sector will further benefit from the Seventh Pay Commission. Implementation of the Seventh Pay Commission recommendation should will also provide tremendous benefit to the housing sector. The commissions' awards cover approximately 10 million government employees increasing their total payout by over a trillion rupees per annum. Entry level payers also more than double. Allowances are expected to also double. This will have very, very positive fallout on the housing sector.

Before I get into the operational aspects and other important development for the quarter was our subordinate debt upgrade to AAA. With this upgrade we enter the league of select few financial services companies that are AAA rated both on senior debt as well as subordinate debt. This upgrade will allow IBHFL to raise tier II capital at fine rates and further enhance shareholder value by maximizing RoE in the long run.

Now I will start with specific numbers. We continue to remain on our guided target of profits with PAT for quarter one fiscal 2017 at Rs.6.3 billion from Rs.5.11 billion last year same quarter, which is the growth of 23%. We have also declared interim dividend of Rs.9 per share for the quarter.

Our loan book at the end of quarter one stands at 710 billion as compared to 540 billion, which is a 31% growth. Owing to uncertainties surrounding Brexit we through the quarter carried higher cash than usual and close the quarter with 153 million in cash, cash equivalence and investment in liquid investment.

Our asset mix is trending as guided. At the end of quarter one fiscal 2017 it splits as 53% home loan, 24% LAP and 23% large loan. Commercial vehicle loans have completely runoff. Over the last three quarters our housing loan book has inched up to form 53% of the total loan book assets up from 50% last year.

We are poised to make the most of the growth opportunities in the housing sector and will grow faster than the market as the market share expands from the current 5% to 6%. Resultantly the composition of housing loans within the total loan asset book will continue to inch up and as guided by the end of fiscal 2018 will reach 60% of loan assets and by 2020 will reach 65% of loan assets.

Our topline has registered healthy growth with revenue for quarter one fiscal 2017 at 25.97 billion a growth of 28%. The NII for Q1 fiscal 2017 stands at 10.53 billion, which is again a growth of 28%. Our NII does not include fee and other charges.

Total income for quarter one splits as an income from operations at 22 billion and other operating income, which is largely income from investments at 1.1 billion. Fee income is at the end of quarter one was 1.29 billion as against 0.8 billion in Q1 last year.

This quarter we have disbursed a total of 52.51 billion a growth of 15.3% over Q1 fiscal 2016 in which we had disbursed 44.54 billion. The split of that is 27 billion of home loans, 12 billions of LAP and 13 billion of corporate mortgage loans.

Our NPAs for the last 19 quarters now have remained within a range of 0.7% to 0.9% for gross NPA and 0.3% to 0.5% as net NPA. We are reasonably optimistic to continue within this range till 2020 at least. Our gross NPA and net NPA are at 0.84% and 0.36% respectively. In computing net NPA only provision against substandard assets is reduced from the gross NPA.

Standard asset provisions and counter cyclical provision amounting to 5.35 billion are not deducted while computing net NPA. Including these provisions the total provision divided by gross NPA that is the total provision cover on gross NPA is 146.3% and this also continues to inch up. We continue to be prudent in our provisioning approach.

Total excess provisions over regulatory requirement has increased to 2.99 billion as against 2.84 billion at the end of fiscal 2016. Resultantly our credit cost for the quarter was Rs.1.26 billion at 71 basis point of loan asset, which is as per our guidance. At the end of Q1 fiscal 2017 total substandard provisions were 3.4 billion, general provisions at 1.86 billion and specific provisions at 1.54 billion, floating provisions of 0.89 billion and standard provisions at 4.46 billion totaling to 8.75 billion of provision.

As I mentioned earlier owing to uncertainties surrounding Brexit we closed the quarter with higher than usual levels of cash at 153.35 billion and we carried this extra cash through the quarter. So some total of 24.4% of our balance sheet was maintained in the form of liquid investment. Our net leverage after deducting from total borrowings the above cash and cash equivalent and investments in mutual funds stood at 4.6x. On the borrowing side we continue to make massive progress. Bank borrowings have declined to 47% of our borrowing mix down from 49% in March 2016.

Capital market source along with ECBs and sell downs have contributed to 68% of incremental funding in Q1 and 66% of the incremental funding since March 2015. Our spread for Q1 fiscal 2017 was stable at 318 basis point on book basis and 300 basis points on incremental basis, which is within the guided range of 300 to 325-basis points of spread.

Cost of fund is at 9.25% on book basis on an incremental basis is at 8.9% for Q1 fiscal 2017. Borrowing flexibility has ensured that we have been able to maintain a spreads in the guided range. Dependence on zero-coupon bonds as a measure of financing has been coming down sharply. The zero-coupon stock stood at 10.6 billion at the end of Q1 fiscal 2017, which is down by nearly 46% as compared to zero-coupon stock of 19.6 billion at the end of Q1 fiscal 2016. Zero-coupon bond as a percentage of borrowings contributes now to only 1.6% as of June 2016 versus 3.9% for the same period last year.

Now moving on to balance sheet numbers. Our networth at the end of quarter one stood at 113.6 billion up from 66.8 billion at the end of Q1 and 106.94 billion at the end of Q4. Capital adequacy adjusted for investments in mutual funds stood at 23.81% at end of Q1 with tier I at 19.87 from 23.38% of total capital adequacy and 20.36 of tier I at the end of Q4. From a longer-term strategy perspective I would like to give you a few updates.

A very key part of our strategy is to increase our home loan assets to 60% by fiscal 2018 and 65% by fiscal 2020 and to manage that we have often shared that we will have to reduce our bank term loan borrowings to about 30% of our overall borrowing by 2020. We have to also in the process reduce our cost income ratio, reduce our cost of debt and only then will be able to manage our spreads.

Our incremental cost of borrowing from bond is 8.6% nominal monthly and is 80 BPS lower than that of term loan. Even in a steady interest rate scenario our cost of debt will continue to decline as we source more than 65% to 70% from non-bank sources. At a stock level 53% of our borrowing is from non-bank sources and incrementally 68% or nearly 70% of our funding in the last three months since March 2015 and 66% of our funding in the last 15 months has been from non-bank sources. So between now and 2020 all we need to do is repeat what we have done in the last three or the last 15 months and we should be able to manage our spreads and in the process increase our home loans first to 60% by 2018 and then to 65% by 2020 and by reducing our bank term loan borrowings from on stock basis from 47% to 30% and by maintaining what we are doing currently in terms of incremental borrowings we should be able to offset whatever reduction.

The other important strategy is to continue to maximize our RoE through capital conservation. This capital conservation comes through two routes. One is to maximize sell down transaction and the other is to focus on a going forward basis on raising more and more Tier II capital. Sell down will continue to remain a key focus area as it has been in the past and it would continue to be the most important means of capital conservation and also huge contribution to profitability. In this quarter, we sold down a total of 11.14 billion compare to 5.22 billion in the same quarter last year, which is more than doubling the sell down transaction.

For the preceding 12 months we sold down a total of 50 billion up from 28 billion in the 12 months preceding June 2015 nearly doubling. Sell down of loan retains margins takes the loan book of the balance sheet and conserves capital. It represents the most effective utilization of capital and is RoE accretive.

We also raised 6.1 million of subordinate debt. Tier II capital increases our overall capital adequacy conserving equity capital and making it go a longer distance. The upgrade of our subordinate debt rating to the highest AAA will further boost our Tier II capital raising abilities helping us raise Tier II capital at even finer rates. The other issue, which has been often discussed on this call and otherwise, has been a specific loan assets going by the name of Palais Royale.

Some of you may have read recent in newspaper reports that BMC is on the verge of giving permissions to restart the project and regularizing whatever issues were there. So this comes as a welcome break. The chief of BMC carried out an inspection of Palais Royale last week. He has reviewed the excess refuge area which is the root dispute in the way of obtaining the final clearances and I continue to be very hopeful that in the next four to five months the project should since the civil construction is already over should receive a part occupation certificate and in the process will be able to receive close to a little over 1000 Crores from customers whose payments are due.

Zero-coupon bonds have also been discussed several times. As I mentioned earlier our zero-coupon stock has been declining, most heavily as a percentage of borrowings. Last year at the end of quarter one our zero-coupon stock was 1961, which is now 1060. Other than in situations where our counter party is in a position to describe to nothing else but zero-coupon which would generally be in a case of a mutual fund not wanting any reinvestment risk. We are restraining some issuing further to zero-coupon bonds.

I would also like to comment on the recent news flow around some tax department checks. As a part of a large corporate group that in the recent past has undergone a restructuring at the founder level and also has a large real estate business, tax checks of this nature come more in the normal course of doing business. As most of you may be aware in the last 2 to 2.5 years several large corporate houses such as the Birlas, Jindals and almost all large real estate companies have gone through similar tax checks.

Indiabulls Housing while it is part of a larger corporate group is also amongst the highest tax paying corporate and for fiscal 2016 paid a tax in excess of a 1000 Crores between corporate service and dividend tax. The tax paid by the IBHFL on tax by loan asset basis is amongst the highest in the housing finance industry. It is business as usual for us as is reflected by a prompt release of results around the same time that we do it every quarter and the quality of the result is there for all of you to see.

As corporate group evolves such events and the surroundings and speculations have to be taken in stride while the speculations will sustain for sometime. I am reasonably optimistic that these are also opportunities for a well-governed organization to emerge much stronger out of these situations.

To finally conclude IBHFL is well prepared and perfectly poised to make the most of the growth opportunity in the housing sector for many years to come. We will build on our track record of the last six years in which period our loan assets have grown at a CAGR of 28% and our profits have grown at a CAGR of 26%. We have begun fiscal 2017 excited with the growth opportunities ahead. I confidently reiterate our growth guidance of between 20% and 25% across all the financial parameter and on that very positive note I conclude the result announcement. We shall now take questions. Thank you.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Veekesh Gandhi of Bank of America. Please go ahead.

Veekesh Gandhi: Gagan congratulations. I just had few questions. One is you mentioned couple of times your home loan is now 53%. How do you come to that is it on the disbursement side, are you saying or it is on the book?

Gagan Banga: Veekesh that would be on the full loan book.

Veekesh Gandhi: Full loan book and there is a pure retail home loans right?

Gagan Banga: This is pure retail home with an average ticket size of Rs.25 odd lakh.

Veekesh Gandhi: Just the other couple of data points. Did you mention the Tier I?

Gagan Banga: Yes Tier I stands at 19.87%, Tier II at 3.94%, total two 23.81%.

Veekesh Gandhi: This is again adjusted for your mutual fund investment I would believe?

Gagan Banga: Yes that is correct our investments are to the extent of 9056 Crores.

Veekesh Gandhi: The commercial paper is not there so is it rundown completely?

Gagan Banga: It is part of that it could be around 6000 Crores.

Veekesh Gandhi: Which was something under 4000 Crores last quarter?

Gagan Banga: No it was under 5000 Crores last quarter.

Veekesh Gandhi: Just one final question is on commercial credit, which again obviously it is growing in line with your overall book very strongly. So any thoughts on that or any flavor on whatever you have grown in this quarter particularly on the commercial credit what kind of lending have you done?

Gagan Banga: I would not say 3 to 6 I would say 6 to 12 months period the general ratio that we would like to adopt is 60% lease rent discounting and 40% construction finance, loans being rather chunky in this particular asset class that ratio may be plus or minus 5% from time to time. So we would broadly in the last six-months have grown in this ratio of 60-40.

Veekesh Gandhi: Where would have this growth come from like which cities?

Gagan Banga: So some lease rent discounting transactions have been done both in Gurgaon, Pune and Bangalore and the residential construction finance we have done a couple of projects in Gurgaon and a few in Mumbai.

Veekesh Gandhi: Thanks a lot and all the best.

Moderator: Thank you. The next question is from the line of Adarsh P from Nomura. Please go ahead.

Adarsh P: Firstly, just one data point what has been the P&L provisioning last quarter and this quarter for either bad loans or total provisioning number?

Gagan Banga: The total provisions are 126 Crores and I had a given a breakup of that so 126 Crores breaks down between so 101 is substandard asset provisioning, 23 is standard asset provisioning. So that is broadly the number.

Adarsh P: How does this 126 is the total number looked in 1Q 2016?

Gagan Banga: This was 1Q 2016 was 65 Crores, in Q4 was 215 Crores.

Adarsh P: So there would have been some write-off is it in this quarter it looks like right because the coverage in the NPA numbers are flattish so was there any write-off in this quarter because you had 100 Crores provisioning?

Gagan Banga: So we actually recovered quite strongly so our net write-off we actually recovered more than we wrote off so there we have on a net basis recovered around 15 Crores. So the total credit costs are as I said 126 Crores.

Adarsh P: Second thing was on the investment book as you explained you kind of increased it. So I just wanted to understand would the average balances be closer to where the quarter is ended?

Gagan Banga: For the Q1 the average balance will be between 14000 and 15000 Crores. We do not intend to run such a high cash piece. We were worried about Brexit we thought that event is to happen coupled with whatever the fed was indicating it could be very, very tough. It seems both the events are behind us. So we will have a more normal cash balance of closer to 12000 Crores from this quarter onwards.

Adarsh P: Because when I try and compute the yields and just correct me if I am wrong it get to like 6% to 6.5% yields for the last two to three quarters on the investment book. So any classification of the interest income there which will sit somewhere else or this should be tax adjusted income that you should be making?

Gagan Banga: It will be in the range of 6% to 6.5% yes.

Adarsh P: Last thing just wanted your thoughts on mortgage?

Gagan Banga: There would be tax breaks given the nature of mutual funds and how you receive income there would be tax breaks so 6.5% to 7% would have a different tax treatment. So adjusted for tax effective yield moves up a little bit but yes the headline yield will be 6.5% to 7%.

Adarsh P: The last question is on mortgage bagged securities right it seemed budget had some breaks but we not heard enough on that. So how is that piece moving in what is the thoughts there?

Gagan Banga: It is moving well so while the budget speech added all these things have to be notified and sometimes these things take their own time to get notified. Fortunately, it has finally been notified on around June 15 so this is the first effective quarter that we have time to discuss with counter parties and there is a lot of baggage around it where people have lost money. So everybody needs to be doubly sure. I am reasonably confident that in the next three to four months we should be able to a couple of very meaningful transactions.

Adarsh P: The yield there would be lower than your bond?

Gagan Banga: We currently pay about 40 BPS over other CRISIL AAA. This should happen at about 25 BPS over CRISIL AAA.

Adarsh P: That sounds good. Thanks.

Moderator: Thank you very much. We have the next question from the line of Pranav Kumar of JP Morgan. Please go ahead.

Saurabh: This is Saurabh. My first question is on the retail home loans what is the contribution of self-employed within retail home loans?

Gagan Banga: It is approximately 30%.

Saurabh: So 30% of 53 or 30% of the entire home loan.

Gagan Banga: 30% of the 53 is self-employed and then the 24% LAP is also self-employed. So roughly approximately just under 40% of our book is meant out to the self employment.

Saurabh: Just on the strategy piece where you want to take this number to 60% your retail home loans. So the margin compression, which may happen because of that, and probably the yield compression we continue to see in the LAP market the actual saying will be offset by your funding cost by 70 basis points. Is that right?

Gagan Banga: That is right. So we between now and 2020 because of taking home loan from 53 to 65 will land up losing on yield something like 60 to 70 basis points and that 70 basis points we should be able to offset by borrowing approximately 70% from non-bank sources of which we currently have close to about 12% of our borrowings from of the overall resource mobilization from portfolio sell down that will increase to about 20%, 40% will be bond and just under 10% would be ECB. So between these three we should get to 70 and bank contribution will be about 30. We have just recently concluded the sourcing of an ECB transaction of 250 million, which we are in the process of doing the regulatory filing, and we should be receiving those funds in the course of the next two to three weeks.

Saurabh: That is clear and just two last questions Sir. One is on your spreads. Your spreads have been fairly stable over last four quarters from what I understood the LAP yields continue to be under pressure and we have seen some home loan rate cuts as well. So what could explain this stable spread?

Gagan Banga: Over the last 24 months relative to my peers I am greatly benefited from the fact that while some of my peers have 10% to 15% bank financed, I am even today 47% bank financed and another about 12% of my financing comes from portfolio sell downs both of which are variables of close to about 60% of the resources on my balance sheet are variable plus I have a very high equity contribution on my overall resource mobilization thus I am able to get benefit of whatever variable reduction you are talking about in the market. So there has been something like a 70 basis point reduction in bank base rate and if you take stretch that case from peak to the median MCLR there is a 90 basis points reduction. Our reduction in bank borrowing cost is actually down 93 basis points plus we are also benefiting from the fact that in July 2014, our upgrade to AAA happened and since then our spreads over other AAA has also come down by almost 35 basis point. So both of which are contributing in us being able to reduce our cost of funds faster than the rest of the industry is being able to reduce cost of funds. This will be a scenario which will continue to be very unique to us for at least the next two to three years by which time by 2020 we will also be largely fixed rate borrowers and at that time is there was to be such a sharp rate cut and we are unable to do our borrowings swaps then we will get stuck in the same manner that some of our peers are.

Saurabh: Just one more question on this AAA upgrade so we are awaiting one from CRISIL but on an incremental basis you said 60-basis points monthly is a differential. That equates to about 40 basis points?

Gagan Banga: 40 basis point so if somebody else is to borrow at between 8.5% and 8.6% I will borrow between 8.9% and 9%.

Saurabh: If AAA upgrade happens this should compress?

Gagan Banga: By another 15 to 20 basis points almost immediately and then my sense is that for the balance to squeeze will take sometime but if a AAA to happen then that spread should up from 40 to about 20.

Saurabh: Just one last question what is your outstanding exposure in Palais Royale now?

Gagan Banga: It is just under 600 Crores.

Saurabh: Thanks.

Moderator: Thank you.

Gagan Banga: I think we are done with questions. So thank you everyone for joining in on this call and in case you have any specific queries, please let our investor relations team know. We are there to handle all of your questions. Thank you so much.

Moderator: Thank you. On behalf of UBS Securities that concludes this conference. Thank you for joining us ladies and gentlemen you may now disconnect your lines.