“SKS Microfinance Limited Analyst Meet”

May 06, 2015

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Dilli Raj: Good afternoon. We thank each one of you for being here. Let me introduce the SKS team present here –

- Dilli Raj - President
- Ashish Damani – Chief Financial Officer
- Ashish Pipaliya – EVP Investor Relations & New Initiatives
- Pratap R – Deputy Chief Financial Officer
- Rajendra Patil – SVP – Legal & Secretarial
- Prabhdeep Singh Chana – Investor Relations
- Sailesh Banta – Communications

The deck has been available with you for some time now. So I will not burden you with details except some quick update. You may have questions on our small finance bank application and how the rural economy is doing right now, would there be any impact of that on our business. Etc.

Then we can jump into question on financials & operations, particularly on Q4 & FY2015 numbers. This is the second year of our turnaround and sustenance. We raised an incremental debt of Rs.5,020 Crores and also completed QIP of Rs. 398 Crores which helped us complete incremental disbursements of Rs.6,891 Crores. Resultantly the Non-AP portfolio outstanding increased to Rs. 4,171 Crores from Rs. 2,837 Crores, a 47% year-on-year growth.

We saw the concomitant 47% increase in gross revenues, moving up from Rs.545 Crores to Rs.803 Crores. On the cost side, the cost of borrowing (i.e. Cost of interest bearing liabilities including processing fee paid on

Loans on Balance sheet) did reduce to 12.8% from 13.6% for the whole year. Reduction is much more pronounced in the Q4 at 11.8%.

Moving forward, we can sustain the lower interest rate. Reduction is purely driven by downward adjustment in the risk premium rather than anchor rate reductions. Cost to income reduced from 74.5% to 61.1%, but opex to GLP stayed at 9.5%. After the MAT bite of Rs. 5.9 Crores, we reported a PAT of Rs.188 Crores up from Rs.70 Crores.

If there are specific questions on numbers, my colleagues will take. But I want to quickly move on to the second subject where many of you may have questions that is our small finance bank application. We did apply on 02nd February, 2015 as notified to BSE and NSE. It is a regulatory approval process and we admit our inability to entertain any question on that. But we will give some quick background based on what is there in the public domain. This would not call for a change in our operating model at all. If we were to become a small finance bank post approval, neither the customer segment nor the operating model would change. RBI guidelines insist on 75% PSL, 50% at a ticket size of not more than Rs.25 lakh and 40% of the new branches to be located in villages with less than 10,000 population. If we quickly map SKS's financial inclusion footprint, may be barring gold loan, approximately 98.8% is PSL compared to the 75% stipulation. Not just 50% but the entire portfolio is lower than Rs.25 lakhs, it is actually less than Rs. 30,000 ticket size. We will not drift away from the customer segment we have targeted and nursed over 10 year period.

The economic case for a small finance bank so far as SKS is concerned rests on reduction of operating cost and borrowing cost.

You may share a perception that becoming a bank would raise the cost structure especially in terms of technology spend and special talent acquisition. But, take the case of core banking solution, it is required only in the back end, but not at the middle end or at the front end. The front end technology or the customer interface methodology need not change. Also, Key features like door step delivery, weekly interface with customers etc. need not change. If the small finance bank helps you to migrate a large part of the last mile transactions in cash into an electronic platform, it is very obvious that your operating cost, as a percentage would reduce.

Of course, the case for reduction in borrowing cost rest on the fact that you have seen the risk premium getting adjusted downwards in the last two years and more so in FY 2015 by almost 180-basis points. SFB structure could open out refinance lines that are available for MFIs. Mudra refinance facility should also be available for SFBs. Additionally, if you become a SFB, there are several dedicated refinance lines which go underutilized as of now, which a normal bank may not be able to use and an SFB will be able to use. We will not be able to address any further questions on SFB, because that is a regulatory approval process.

Many of you had questions on the state of the rural economy. Our direct agri exposure is a mere 4%. Our model focuses on non-farm sector, but not the farm sector. The 4% direct agri exposure too is an exception than the rule.

I am not arguing that non-farm sector could maintain its vibrancy without a strong agrarian backup. But look at the structural changes which have happened in the last 5-7 years.

Composition of the rural household income basket has gone through a silent transformation. The non-farm income is 65% and the farm income is 35%. Government spending today constitutes 18% of rural GDP be it NREGA or Bharat Nirman. There is external cash infusion into the rural system, which is insulated from the way agri or the non-agri sector functions. MSP prices increased by 39% over the last 5 years and some sort of cushioning has happened. Rural infrastructure is also strengthened

There could be questions on why not just talk about FY2015 in particular rather than working with 4-5 years average. MSP price increased by 4% in FY2015 too. One way of arguing is to take 39% in the previous five years so the average is 7.8%, which is obviously more than 4%. But even in FY2014, it has come down to 5%. It is still up i.e. Plus 4%.We heard people using words like collapse in rural wages, collapse in MSP prices etc. There is no collapse, it is still growing. The growth rate of 4 % is certainly lower than five year average of 7.8% but it is still growing. The same thing holds good for rural wages. Rural wages did grow at 4% in 2015, of course it is lower than 9% in 2014. If you look at MSP as a cash flow enhancer for the rural system there are two factors. One is the base price at which the government procures and most importantly the quantum procured. We have no reason to believe that aggregate rural cash flows are going to dry up. The Union Budget has not cut any rural or social sector allocations and in cases like NREGA, ultimate allocation could go up by another Rs.5,000 Crores.

A few analysts took the view that with Jan Dhan and direct benefit transfer, the delivery system is going to get more efficient and will that dry out some money? If the delivery system becomes more efficient especially with direct benefit transfer, leakages will come down and that would not affect the segment we are targeting. An efficient delivery system augers well for our segment because coverage will increase and become more targeted.

We do not want to be anecdotal by saying that we travelled down to Guntur and it is getting better. I am trying to get into raw data and lay out the big picture.

Our target segment is two to three strata below the rural segment that is buying tractors or CVs. The economic activities of our customers are pretty basic to very living. 26% livestock, 9% kirana shop, 5% eatery, dhabas, so they come with huge amount of inelasticity and 4% increase in MSP and rural wages is not going to shrink demand for these kinds of basic activities. Rural families engage in multiple economic activities and that is how they really make progress in the economic graduation process. Feel free to ask questions. Thank you.

Questioner I: Three questions. First one is on your cash levels I notice that it has gone up significantly even as a percentage of balance sheet, can you just explain why it has increased. I think it is above 30%. Second one was on the Andhra Pradesh book that you have written off. Can you just outline with the plans or what the recovery rate can be and how we targeting going about it and I will ask the third one later?

Dilli Raj: Normally, we build up cash surplus towards March end because of two or three constraints. One is what we call as the 'last reporting Friday syndrome'. All PSL loans come with a caveat that you draw down by year-end otherwise it just disappears. You have the option of either not drawing or drawing out and suffer the negative carry for a month or so. Rs.1,300 Crores is drawn out literally in the last 15 days of March.

Cash holdings went up in proportion between FY2014 and 2015, because the very debt program increased from Rs.3,503 Crores to Rs. 5,020 Crores. Second point which is very specific to FY2015 is that there were many bank holidays apart from the annual closing. Rs. 300 Crores are kept for repayment to banks on April 1st and for disbursements in the first week of April. The quantum of incremental debt you can raise from banks in Q1 will be low for various reasons. You ought to get your balance sheet audited. They are busy with three or four audits themselves and things pickup by May end only. We normally keep balance to fund credit growth in Q1. Fortunately as per recent amendment to PSL guidelines, banks have to achieve PSL targets on a quarterly basis and the penalties are based on quarterly averages from FY-2017 onwards. From now on drawdowns from the banks could be more gradualized for all four quarters and hopefully we will reduce the cash balance.

Questioner I: Just a quick follow-up on that is on an average, what is the typical cash requirement that you keep on your balance sheet?

Dilli Raj: The requirement theoretically need not exceed two to three days of your disbursement. It can be run as a tight ship and you can just manage with two to three days cash in the system, but we have a liquidity bias. On review of SKS balance sheet over the last eight years, you will see cash holdings at an average of 20%. But it is not all cash or current account balance, there are security deposits/ fixed deposits. I think we could reduce to an optimum level of Rs. 300 Crores.

Questioner I: On the AP book?

Dilli Raj: Numbers are there in the earnings update. We collected Rs.31 Crores in FY15 and other than that we do not have any update.

Questioner I: Going forward, we have a pretty large book that is outstanding on that you written off. What is the realistic annual recovery that you can expect and what is your strategy need be going forward?

Dilli Raj: Our stance is that legally we have been able to resolve the issue. We got the interim order from Supreme Court on March 18, 2013. Now we have popular governments. We never had any issue in interacting with popular governments. That is why contagion did not spread beyond AP.

Questioner I: Around Rs.30 Crores to Rs.40 Crores is what you would expect?

Dilli Raj: The present level of collections can continue.

Questioner I: Sure and my last question is RBI recently increased the average borrowing that customer can take from micro finance institutions and also eligibility criteria increased. Now that may not reflect the borrowing capacity of the borrower as in industry, how are you ensuring that these borrowers again do not get overleveraged and might run through the issues?

Dilli Raj: On the three dispensations I will ask Ashish to address. The numerical ceiling on the aggregate borrowing increased from Rs.50,000 to Rs.100,000, ticket size can go up to Rs.60,000 and the minimum income eligibility of Rs.60,000 has been increased. But let us focus on what has not changed. What has not changed is, if you were to extend a ticket size of more than Rs.15000, it ought to be a two years loan. You can go ahead and increase your ticket size, if you believe that rural inflation has caught up and these limits were set in literally five years back in 2010, but that should not translate into higher stress for the customer. If you go beyond Rs.15,000, then extend a two year tenure so that EWI remains the same.

Not more than two MFI lenders to a single borrower has also not changed. It acts as an entry barrier. If you have acquired the customer, there should not be a disturbance from somebody coming as a third or fourth lender and trying to compete. I will ask Ashish to explain our product strategy

Ashish Damani: From our perspective, what we have been doing for the last one-year, we have started giving out long term loans which are more of than Rs.15,000 ticket size and thus it is given for two year tenure. We have started this last year and we have started issuing these to customers who have completed at least two cycles of incomes generating loan (i.e. one year loan) with us. Once they have cleared this successfully, then they are eligible to take this LTL. We are looking at increasing this limit from 10% last year to 25% of disbursements this year. So, this will give an opportunity to the borrowers who have been there for some time with us to take larger ticket. So the ticket size in this is around Rs.28,687 on an average basis compared to Rs.13,565 for one-year ticket size, which is our income generating loans, that is how things will change. This will pull up our overall average ticket size to some extent, but again we are working slowly on this with 25% cap on disbursement for this kind of ticket sizes.

Sunil Tirumalai: This is Sunil Tirumalai from Credit Suisse. I had a few questions. One clarification what it was, you mentioned 95% of the branches will come under the unbanked area category. Are you referring to the centers or the branches, because my understanding is that the branches will be in the better of place? That is first question and the second one is that?

Dilli Raj: 40% of the new branches are to be located in villages with population of less than 10,000. If you have branches right now, if you are allowed conversion or any other structure, then that can continue. But, when you establish new branches, 40% of them are to be located in villages with less than 10,000 population.

Sunil Tirumalai: The borrower per Sangam manager is the number that we need to track for your company because of the high opex ratio. It seemed to have come down, now it seems there is some good upside, so I just wanted to understand how to look that number and thirdly, just the broad outlook on the opex cost?

Ashish Pipaliya: For financial year FY2015, this number has been very stable at about 787 borrowers per loan officer and if you recollect we have always told that 750 borrowers per loan officer is an ideal metric to look at. So, we are actually on an ideal metric.

Going forward, we are doing some pilots in the technology side to see that whether this number can go up, but I do not think we are at a stage to really commit a number that it will go from 800 to a bigger number.

Answer to your third question on operating cost related to the borrowers per loan officer. What we are saying is even if we are at this level of 750-800 borrowers per loan officer. Going forward, the operating leverage is going to come from utilizing the non-loan officer head count.

Explanation:

Loan Portfolio growth of ~43% will be driven by 25% increase in Loan officer count and 10-15% increase in ticket sizes.

Operating cost will increase by 20-25% with

Personnel cost increasing 20-25% by increase in loan officer's count (50% of employee base X 25% increase in count) and 10-15% increments for all staff.

Other operating cost increasing by 10-15%.

So what I am trying to say is the borrowers per loan officer, if it remains at this level we will still have an operating leverage and opex to AUM which you see today is about 8.9% last quarter, should stabilize at something like 8.2%-8.3% next financial year.

On the point of branches, which we are talking about, it is less than 10,000 population is the branch definition according to the SFB guidelines. So, today we have branches which serve areas with less than 10,000 population, but these are not located exactly in less than 10,000 population areas. These branches cater to the centers. Center is a place where we actually do a transaction. Every branch will have 120 centers and almost all the centers I would say would be in less than 10,000 population. So I think what we meant was centers.

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Sunil Tirumalai: Thank you for that. Just last one question. I notice that the proportion of securitization has come down this year. I wanted to understand the reason behind that and I think the outlook is important because if you become a small bank, the lending to you will cease to be PSL for the banks, so this will be the only route where you can participate in the PSL kind of market?

Dilli Raj: It is not to do with appetite or demand for our paper, so in absolute amount I think it is more or less equal at about Rs.1500 Crores. We had one constraint that is the securitization guidelines stipulate three months seasoning criteria. If you recall Sunil in Q3 our disbursement actually reduced (which is the first time in FY2015) by Rs 148 Crs compared to Q2. Normally it would be more than Q2, for the first time we had Rs.148 Crores lower than Q2. As you know most of the securitization transactions happen in Q4. Your Q3 disbursements are only eligible. But in terms of appetite or demand, if we had another Rs. 1000 Crores of paper also we could have easily sold it. Now, another point you raised is about SFB, the good thing is that interbank participation certificates are also eligible for PSL provided the underlying assets are PSL.

Questioner II: Thanks for taking my question. So far we have been mostly focused upon the rural side of economy and almost the majority of the book is still coming from there and then there are these couple of companies, which have become very active on the urban side of the economy and those are the companies which has become almost equal size as yours. Very basic question, so the whole genesis of the JLG model which was based upon the rural economy to begin with, is it really possible to implement to same model in the urban side of the story as well or there need to be structural differences in the way business gets down and second question is that would you have any plans of getting into the urban side of the economy?

Dilli Raj: Grameen model (I am taking an expansion of JLG Grameen model) is designed for rural. We are not right set of people to address this question, because we focus on rural microfinance with very little of urban presence. Our closest branch to Mumbai will be 150 Kms away from Mumbai. If we were followers of Grameen model of microfinance prior to AP crisis, we have become devotees post the AP crisis.

Questioner II: One more question on the technology infrastructure, so far the scales of operations have been like very moderate and going forward seems that the scale of operations would be multiplied by a good number, so you think that the technology infrastructure that we have in place as of now is quite equipped and sufficient to take care of the higher scale of operations. Lot more needs to be done in terms of may be monitoring or connectivity of all the branches?

Dilli Raj: Today we have 1268 branches, 9000 plus workforce, 3.6 million Non – AP borrowers and AUM of Rs. 4,171 crores. We have managed in the past approximately 2,400 branches, 27,000 head count and Rs.5,700 Crores of AUM. There is a slide in the earnings update on how the technology back up is revamped (Refer slide no.5). To specifically answer your question, today the entire 1,268 branches are connected. We get a daily update. The new lending platform i.e. SKS Smart is rich with features. Feel free to visit us and check the technology for yourself.

Questioner II: Thanks.

Questioner III: Good evening. I have a couple of questions. The first one would be what percentage of income is by distributing the goods such as solar lamps etc., on the distribution front and where do you envisage this to be in five years and how does that work on the margin front on the distribution etc. and the second question would be in terms of housing finance. I saw housing finance product on your website as in home loans of up to Rs.1.5 lakhs, so to what extent can that be used to raise the ticket prices and what percentage of the book is it today.

Dilli Raj: We have run down the housing loan portfolio. We did start a pilot prior to AP crisis in Andhra Pradesh. Peak outstanding was Rs. 9 Crores and the current outstanding is Nil, Thanks for bringing that to our attention, we will check the website and correct it. Your next question is on distribution, Pratap would you give the numbers on the distribution.

Pratap: We have put in our earnings update. If you go to slide no. 41 what we have done in this financial year FY2015, we have facilitated distribution of more than about 8.6 lakh units focusing primarily on mobile phones and solar lamps, so the way we have been structuring this. The products that is going to increase the productivity for our members, so that quotient has to be high in the products that we will distribute. So, if you look at the numbers are up there, so on from a net fee it is contributing 12.6% to the profit, but also as a strategy we have enumerated earlier that these kinds of products will be 10% of our total assets, meaning 90% plus of the assets will still be microfinance focus and while that on profit basis will be looking it close to 20% contribution. So that is the strategy and this is where we are at FY2015. But having said that we also have some other products in the pilot pipeline so going forward depending on the customer demand, because the products are completely based on what customer require.

Questioner IV: I had question on the RBI regulation where they have capped it at 10% spread, I wanted to understand that what risk this is like what would prompt the RBI to revise this spread according to you, basically I do not know the rationale why we arrived at 10%, but from a regulatory framework how much of big risk this is like if you are 4% ROA what stops them from telling why are you earning 4%, I do not know how they look at it?

Dilli Raj: It is a great question. It is the regulator's prerogative, but there are 2-3 inputs on that. This issue came up for discussion in 2010 itself .One set of people said let us cap the interest rate, let us cap the margin, let us cap the ROA, let us cap executive salaries etc. We said please go ahead and cap the interest rate. A lot of people were not comfortable with interest cap. If you look at it today in whole of India, this is the only product where interest rate is capped. Gone are the days of regulated interest rate regime even the savings bank interest rate has been deregulated. But we in a way pitched for it and that only ceased the debate on interest rates. So when the regulator says it is 26%, I am just using an example it could be any rate then there ends the debate. Interest rate cap is beneficial to the customers. Margin CAP brings in efficiency into the system, if you have to make profit within that 10%, you need scale, you need technology, and you need efficiency. Therefore you keep bringing in efficiency and that benefits the customer. In a way 10% margin cap also acts as an entry barrier. The fundamental outlook is much stronger today than what was even five years back, but you are not seeing new competition, you know why, the answer lies in the 10% margin cap. With the 10% margin cap you need a minimum economic size to break even I am just picking a number say Rs.1,800 Crores of AUM. Perhaps Ashish will say it is Rs.2,000 Crs, Pratap could pick Rs.2,500 Crores, and the limited point being only serious players with long term commitment can enter.

ROA is not capped because interest rate cap benefits the customer, but ROA cap will penalize operating efficiency. If you cap ROE then you are penalizing financial efficiency. If someone's leverage is 4x and my leverage is 2x, the other person is obviously much more efficient than me and why his shareholders should get the same return as my shareholders, where I am relatively inefficient at 2 times leverage ? Then how will the economies of scale will play out? Securitization is outside the margin cap not because of oversight but by design. If A can securitise 30% of his book and B does 10%, it means A has got better origination skills and better structuring skills. So, the fruits of that efficiency can flow back to the internal stakeholders. I have given a detailed reply sorry, because as an analyst I do not see this view changing for the next at least five years.

Questioner V: This is slightly a hypothetical question. Now assuming you get this small banking license, what kind of additional products can you pitch in, not just on the asset side, but on the liability side also in terms of deposit raising, which have you thought through raising deposits from the same set of customers, can hurt your so-called tight business model as of now. Are there any parallel elsewhere as to how it has been done in other countries, how people raise deposit without hurting the unique business model?

Dilli Raj: As we said SFB is a regulatory approval process. Yes we have thought through that. We have furnished complete business plan replete with strategy and execution models for five years. Guideline very clearly stipulate that if you do not achieve business plan targets then you are penalized. Yes it is all thought through, but our predicament is that it is not in the public domain, so we will not be able to discuss. Any new bank initially has to depend upon institutional sources and even if you say retail it would be bulk deposits and CASA advantage comes much later. If you look at the last 10 years of how the new entrants have grown their treasury book, this is the pattern. But as a SFB you have a lot more refinance lines available. Agri refinance, SME refinancing lines are all options. It is a different case for the Grameen bank wherein 93% of Grameen banks sources are internally generated i.e. deposits the same set of borrowers.

Questioner VI: A couple of questions with Bandan getting a banking license and say cost of funds come down for them and you still have margin cap and they could effectively lower the final cost of lending and increase competition. What is your view on that the RBI saying certain rule for such a microfinance players that becomes a bank?

Dilli Raj: We will not be able to answer that question, because it is the regulators prerogative. I can express my view as an analyst that NBFC- MFI guidelines may not apply to a bank or SFB, but it really does not mean anything and it just an academician in me speaking. It is RBI's prerogative.

Questioner VI: What extent is your competition for us to get a sense? Is it still vastly unexplored area you guys are in, still lot of the catchment area?

Dilli Raj: Competition intensity is not much pronounced because of the huge potential and geographic focus. MFI-1 player has ~46% of their portfolio in West Bengal, ~18% in Assam and ~5% in Tripura. We do not have a branch in Assam or Tripura. MFI -5 has 65% of their portfolio in Tamil Nadu, we do not have a branch in Tamil Nadu. MFI- 3 has 25 % of in Tamil Nadu and as I said we do not have a branch. If you take MFI -3 and MFI -4, a large portion of their focus is urban and for us that would be very small.

Question VI: You talked about 25% increase in number of employees; the loan officers and 10% to 13% increase in ticket size. Do you think 10% to 13% kind of increase in ticket size on an annual basis is sustainable for three to five years that is number one and number two, can you share for last year, what percentage of the disbursements for new borrowers versus existing and what percentage of your customers are new?

Dilli Raj: It is not a strategy for SKS to increase ticket size by 10% to 12%, honestly one thing we did right even prior to the AP crisis was never to use ticket size as a growth driver. Please refer to micrometer from MFIN, our ticket sizes are among the lowest. If you really follow group underwriting model, which we do, beyond a point, ticket size increase is not really in your hand. Let me explain, for every new loan sanction, three major credit decisions are exercised by the group and the center. A) Whether to admit a particular person in that group. B) Actual ticket size. (We have some eligibility norms. We will say IGL-1 Rs. 14,959, LTL- Rs. 29,809, you can have any number, but ultimately it has to be approved by the four members of the group and rest of the center. C) third is of course which economic activity. Even LTLs are extended under the JLG model only. Ticket sizes are more to do with the group's ability to take risk on their own peers. To answer your question whether it can be sustained, it is possible because these ticket sizes i.e. offtake averages have not caught up with rural inflation especially in the last five year; theoretically sustaining a 10% to 12% increase in ticket size should be possible.

Ashish Pipaliya: To add to that in slide #39, we have given ticket sizes; and if you go to this IGL and MTL ticket sizes, you will see that the range of the ticket size is Rs.7,591 to Rs.14,959, this is the core product of ours and if you see the utilization rate, the average offtake is Rs.13,565 ;which means that the utilization rate is about 85% to 90%, so this maximum utilization actually tells you that there is so much of room for you to lend beyond the ticket size of Rs.14,000. That is why we are very comfortable for 10-15% ticket size growth and one of the reasons for this is LTL increase from 10% of disbursement to 25% of disbursement next year. Once you cross ticket size of Rs. 15,000 according to the RBI guidelines you have to give a two year tenure loan. Hence to conclude, there is a good utilization rate in the IGL and MTL and that is why we want to now start giving more LTL and also the credit experience in LTL has been as robust as what we see in IGL and MTL.

Questioner VI: But what percentage of loan disbursed last year were to new customers?

Ashish Pipaliya: On a net borrowers (i.e. post the dropout and additions) basis we had about 4.5 lakh new borrower addition in the system.

Dilli Raj: The strategy over the last three years was to get back our customers. The disruptions during the AP crisis were more on supply side constraints, regulatory issues etc. There was no problem with the collection efficiency or consumer behavior in non-AP markets and the underlying businesses of our borrowers got much better. So, when we started getting funds from

Fy-13 H2 onwards we went back to our own earlier customers. You would see in slide no - 8 that during the three years period, two million people in non-AP markets did not get even a pie from us, but they repaid at least 97%. Customer retention also makes perfect economic sense because you have incurred the client acquisition cost and they have a track record with you. LTLs are also offered to only those who have completed two cycles with us. So, it is going back to the same set of customers. It does not result in overleveraging, because microfinance is working capital finance and to a large extent working capital refinance.

Questioner VI: Over the next three years, we could say almost 90% of the disbursement would be still to be existing members?

Dilli Raj: Bit difficult to pick up a number, but yes largely it will be the same set of customers. In October 2010 pre-AP crisis, we had 5.2 million borrowers outside AP, today we have only 3.6 million. There will be some migration, economic graduation, drifting out of the system etc., but largely speaking you still have a lot of ground to cover out there.

Questioner VII: My question pertains to the long term loans, just to clarify for the long term loans also we follow the group lending model and if you can give some color in terms of how do you go about forming the groups like all the five members will be the would be eligible for greater than two year loans. Secondly, is there a cap that you have in mind above Rs.15,000 is two year, for ex: Will new ticket size in future if you have to go to about 30,000, will it become three year product and related to that what kind of economic activity is eligible for these long term loans. So if you have to keep that in mind given the nature of the activity.

Dilli Raj: To start with as we explained this decision is of the group, so we do not do any credit scoring model and come out with fancy conclusion that left handed teachers in Guntur do not pay their bills. We leave it to the group. There are eligibility criteria for instance - within the group if three people want that loan, yes we provide if they have completed two cycles with us and of course there is a credit bureau check, they should not have any overdues with others or for that matter the new loan should not go and add up their outstanding beyond Rs.50, 000 earlier, now Rs.1 lakh so on and so forth, but barring that, it is the decision of the group. We complete Loan Utilization Check to verify that there is an underlying economic activity.

Questioner VI: The maximum tenure for LTL?

Dilli Raj: Right now two years, we are not going to go beyond that as of now.

Questioner VI: Can you tell me the interplay between the leverage and the cost of fund what you playing now because the risk premium has come down if you could throw some light on that?

Dilli Raj: Just explain the question again, I missed it.

Questioner VI: You mentioned in your opening remarks, that the risk premium has come down and that is one reason that cost of fund has also come down. Would your leverage also increase now?

Dilli Raj: The risk premium coming down is evident because cost of borrowing came down by 180 bps, while anchor rates reduced only in Q4. Base rate reduction was a mere 10 to 15 bps. So, the entire 180-basis point's reduction in the cost of borrowing is undoubtedly attributable to risk premium getting adjusted downwards. We will increase our leverage, but we never had constraints of raising funds. It is not that leverage was X in FY2015 because we were not able to incrementally raise the sum. Our business plan warranted Rs.5, 020 Crores and banks were happy to lend that money and moving forward that is the position. As guided we will raise Rs.7,000 Crores (up from Rs.5,020 Crores) and disburse Rs.9,000 Crores (up from 6,891 Crores) So to that extent the leverage would go up.

Questioner VI: My second question is on the gold loan. How do you approve the gold loan and are there any branches and your people at the ground are equipped enough to evaluate the gold loan?

Ashish Damani: There are two people in the branch who have been trained and authorized to check the gold and it goes to those two people in terms of checking the quality of the gold and basis that these loans are approved. So, there is a Valuation officer who first checks and then there is a branch manager who also checks the gold before the loan is approved.

Questioner VI: My last question is regarding the third party product distribution, so why you would like to restrict yourself your earnings 10% for the distribution machinery what you have, so why not it should go up and RBI allows you much more than that recently I heard there was a tender in Rajasthan where they also wanted to distribute the solar lamps, I am just wondering what is the constraint for you to increase that distribution reach in the area what you understand well enough?

Dilli Raj: We are facilitating mobile phones and then solar lights. As Pratap mentioned the rest are pilots. What is the underlying theme here? You need to be very careful in terms of choosing these products. These have to be a productivity enhancement tools. Mobile phones are enterprise equipment for our customer base. You need to exercise a great amount of caution w.r.t the ticket size to avoid overleveraging. Ticket size for mobile phone is max Rs. 2,500 and Rs. 1,800 max for solar lamps. When we are in principle okay to extend a loan of Rs.15,000 to that borrower in IGL Rs.28,000 for LTL. We have absolutely no issue in helping them to get a mobile phone or a solar light for these reasons. An extension of that is the sewing machine. Sewing machines are around Rs.4,500 and used for income generation.

You have 1268 rural branches, 3.6 million borrowers whom you meet 50 times in a year. Several manufacturers want to leverage our distribution.

But we do not want to pretend that we understand inventory and we will choose a partner with strong post-sales services capability in rural areas. Given the high rural tele density, it is quite easy for mobile phones to be fixed in villages or getting a sim card.

Questioner VI: In terms of your own internal assessment when do you come again back to the capital market for equity fund basis?

Dilli Raj: We are restricted by our guidance and will not be able to go beyond that. But just as an analyst, if a company with price to book of four times raises capital, I guess existing shareholders should be happy and it cannot be called as dilution. Our QIP -2012 was priced at Rs.75 and QIP 2014 at Rs.225 and the investors are in 6x and 2x. It is just an observation as an analyst.

Hitesh: This is Hitesh from Espirito Santo. My question is on the borrowing side. We have seen the 60% of the borrowings on a floating rate basis given that banks constitute most of the borrowings with interest rates expected or if you assume that interest rates are going to decline we might see lowering of cost of funds. So, do you see that in the future we might again revisit that 23.6% yield cap that we came out for last year that is the first question and the second thing is on the NCDs and commercial paper, you have seen that we again revisited the market last year it is around I think 3% of our total borrowings, so what is your estimate of what that number can go up to actively looking to enter that space again?

Dilli Raj: I will take the first question and ask Pratap to answer the second question on the structured finance. What is there in the public domain is that RBI stipulates 10% margin cap and what you know is also that our cost of borrowing in Q4 has come down to 11.8%. Of course there are other leverages like interest on security deposit etc. So directionally you know the answer. It is more of a question of when rather than if. Interest rate action will be taken and let me assure that if there is an interest rate reduction, unlike the last time where we had to stop disbursements for 15 days. That will not repeat itself. Our lending platform has been revamped completely. Earlier it was a batch process, meaning, if you have to make any change somebody has to physically go to those 1268 branches and update it. Now it is all moved to the repository system under SKS Smart. I will ask Pratap to answer the question on structured finance.

Pratap: As of March, NCD and CP put together we have about 6% of total borrowing outstanding and we have started raising these again in the market, we had raised money through NCDs and CPs much earlier. In the last year, we have seen our credit rating improve. Our short term rating is at A1+ which is the best possible short term rating and a long term rating is A+, so we intend to increase these percentage in fact if you look at our guidance we are saying incremental debt of Rs.7,000 Crores, so our endeavor is to take it up to may be 20% to 25% depending on favorable term.

.**Questioner VII**: Gujarat, you have got only one branch, so do you define that Gujarat is not a Grameen area?

Dilli Raj: No, I will explain that.

Questioner VII: Whether it is like Delhi, where you have one branch, are Gujarat and Delhi same?

Dilli Raj: No, it is not. Even in Tamil Nadu we have no branches. AP crisis imposed funding constraint and we had to ration disbursement. We have just started operations both in Gujarat and Tamil Nadu. We were late entrants into these markets and accordingly lesser allocations were made. We opted against CDR and met all our financial obligations without any reschedulement or haircut. The peak Non-AP outstanding of Rs.3,953 Crores, came down to Rs. 1,185 Crores. Since we just started operations in in Gujarat and Tamil Nadu, portfolio o/s reduced to Nil. Once we put the AP crisis behind us, we did not open new branches in any other state also.

Questioner VII: This paper has the share capital, but there is no investment from Narayan Murthy in the share capital, I do not find anything on Narayan Murthy.

Dilli Raj: Catamaran continues to hold shares but the holding is less than 1%. The slide gives details of 1% & above.

Questioner VII: You said in your speech that there is no restriction or saving bank account interest, saving bank interest and lending is entirely different category. So you cannot say compare with saving bank interest that is what my opinion.

Dilli Raj: I think I said no interest rate is regulated. Thanks for that.

Questioner VII: Thank you.

Questioner VIII One question, actually on a broader sense. I understand the whole operating model, which you were gone and that is why the NPAs are very low at 0.1%. I just wanted to understand is there a Black Swan event or some event, which your management worry about, which could take these NPAs much above than what they are today.

Dilli Raj: Just repeat the last part, I missed it when you said the Grameen model, so NPA is lower, but what is the question?

Questioner VIII: Some outside event which basically worries management which could essentially shoot up these NPAs. I cannot think of anything.

Dilli Raj: If you leave it to the model and the model is allowed to perform for itself, then the NPA is 1%. Let me explain when we say collection is 99%, it is the collection efficiency of the group and the center. When we say 99%, it is not that everybody is paying 99%, the group methodology is such that someone pays Rs.99, someone Rs.98, someone pays probably Rs.65 and someone pays Rs.134, but before the meeting starts they cushion among themselves and repay. Barring external interventions like AP crisis, it has worked for 30 years in Bangladesh, Bolivia, and Mexico and even in India it has worked for 10 years. But I understand your question is about external intervention. AP crisis is a black swan event. There could be external interventions at a local level. It could be at a village level, some money lender issue or some other issue, those things happen, but they are all aberrations and that is what accounts for 1%. Some events have played out at a district level too. But AP was a black swan event at a state level. But let also factor in the regulatory clarity, institutional infrastructure strengthening like credit bureau, SRO, comprehensive RBI regulatory framework etc. that followed the crisis. The crisis has not been wasted.

Questioner VIII: Thanks.

Dilli Raj: If there are no questions, we will just close it but I request Pratap to address about the MAT, because we had a question from someone.

Pratap: In the quarterly highlights you would have seen that we talked about MAT credit, so in Q4 we had MAT incident, so we had Rs.5.9 Crores of MAT and most of you would know MAT once paid it is available as credit when we pay normal tax, so while in our release to the stock exchange also, we said that we have not recognized it as an asset on the balance sheet, but having said that similar to our deferred tax on each balance sheet date, we will review the recognition on the balance sheet. So, based on let us say FY2016 and other years, we will review whether to recognize MAT credit on the balance sheet.

Dilli Raj: Once again thank you for coming. Please join us for high tea and these people will be available, if there are any questions you can contact. Thank you.