“Arman Financial Services Limited Q1 FY 2016 Earnings Conference Call”

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Moderator: Ladies and gentlemen good day and welcome to Arman Financial Services Limited Q1 FY'16 earnings conference call hosted by Antique Stock Broking 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, 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. Digant Haria of Antique Stock Broking. Thank you and over to you Sir!

Digant Haria: Hi, good evening to everyone. Welcome to the first Earnings Call of Arman Financial Services. Let me introduce our guests for today from Arman. We have Mr. Jayendra Bhai Patel who is the Managing Director. We have Mr. Aalok J. Patel who is the Executive Director and we have Mr. Amit R. Manakiwala who is the Whole Time Director. We have these three gentlemen from Arman and because this is the first ever call of Arman Financial, I would request Mr. Jayendra Bhai and Mr. Aalok Patel to give us short introduction about the company and very small brief about how the quarterly performance has been and post that we can throw the floor open to questions and answers. Over to you Sir!

Jayendra Patel: Thank you Digant. This is Jayendra Bhai and ladies and gentlemen I take this opportunity to thank you all for your time and interest in Arman. We are doing this conference call with our investors the first time and that is why I feel that if there are any shortcomings or mistakes on our part, I request you all to bear with us. I am sure it will be corrected next time. I will take few minutes of your time to tell you as to how Arman and Namra came about.

Arman was incorporated in 1992 and we were involved in 2 Wheeler financing. In the year 1995, we came out with a public issue and even though the weather was bad, that is to say the circumstances were not very conducive for the public issue, still our issue was oversubscribed by 22 times. SEBI at that time asked us to do the allotment in such a way that smaller investors get some shares, that is the reason, let me repeat that is the reason why most of our shareholders hold not more than 100 shares even today, that was the instructions given to us by SEBI to entertain the smaller investors. Arman started its corporate finance bill discounting, ICB, merchant banking and all other things that a full-fledged finance company was required to do. As the time went on, Arman changed its focus from wholesale lending to retail lending and started two-wheeler and three-wheeler financing. In the course of this transition, ladies and gentlemen, I found out that smaller the borrower better is its credit worthiness. **(*agar chote bandhe ko finance diya jai toh who paise jaroor se time par vaapas aatha hai*) If the small investors are provided with finance, then that money definitely returns on time. T**his is the belief and trust which started microfinance under the 100% owned subsidiary of Arman which is called Namra Finance Limited. We have 32 branches in Gujarat, 13 in Madhya Pradesh and two more branches are coming up for microfinance activities. We have a network of 50 plus dealers plus five branches for two-wheeler, three-wheeler activity. We are absolutely focused on controlled growth, ladies and gentlemen, rather than irrational, exponential growth with a mad rush after the numbers game. We are absolutely conservative with our lending policies. We are a member of CIBIL Credit Agency for asset financing and High Mark Credit verification agency for a microfinance activity. A very reputed agency called M-CRIL has rated our microfinance operations four times and each time we have received excellent ratings of Alpha Minus. Also a credit rating agency CARE has given us investment grade rating and also MFI2 for our microfinance activity.

To summarize all these, ladies and gentlemen, the immense latent business potential, strong leadership, eminent board and strong processes collectively contribute to Namra being an upcoming industry leader in the microfinance space wherever we work. Added to this the fact that the combined Arman Namra entity is one of the few companies in India involved with microfinance activity while being listed on the BSE and having the support of global microfinance stalwarts like Incofin the company is poised to shine in the coming years.

I again thank you for your continued support and cooperation and in case if you want to get in touch with me my phone numbers are available on our website, I will be happy to hear from you. I now invite Digant to takeover.

Digant Haria: Aalok, it would be great if you can run us through the results and then probably we can throw the floor open for questions and answers.

Aalok Patel: Ladies and gentlemen, thank you again for joining us for the investor conference call for Arman. As Jayendra Bhai mentioned, this is the first investor conference call we are conducting and we hope we will have some feedback for us either positive or negative after the call is over.

We hope to continue with these conference calls on a quarterly basis, I am not sure and I do not know how many people have joined us today, but I am sure that many of you have had a chance to interact with personally, so again thank you for joining us.

I will start with discussing the operational and financial results for the first quarter ended for this fiscal year and will try our best to ensure we keep this call interactive and meaningful for everyone.

As far as the quarterly figures are concerned, I hope you had a chance to review our results and the press release and if not I encourage you to download and review them at your leisure. They are available both on our Armanindia.com website and on the BSE page as well.

Year over year growth on interest income was up by 33% from 6.68 Crores to 8.87 Crores. Net profit after tax went from 1.7 Crores to 2.04 Crores, a 20% increase while EBIT earnings before interest and taxes increased 32% from 4.79 Crores to 6.34 Crores. Just to note there will be a slight mismatch between income growth and net profit growth as our leverage increases new portfolio growth being funded by interest bearing debt towards equity.

Assets under management increased 40% from 91.4 Crores to 127.7 Crores, so that is 91 to almost 128 Crores the portfolio increased from the same quarter the previous year. Out of that 77 Crores of the assets under management is coming from the microfinance business and 51 Crores from the two-wheeler business. We have crossed 1,15,000 active borrowers this quarter compared to 78,000 the same quarter of the previous year, which is a 47% increase. Disbursement figures are just as promising, microfinance disbursement for the quarter stood at 40.4 Crores while asset finance stood at 12.3 Crores for a total disbursement amount of 52.7 Crores. This is compared to 33.3 Crores in the same quarter of the previous year. So there is about a 58% consolidated increase in the disbursement figures.

Overall, our operations are going well. We are on target for meeting our projections for FY'16 and indeed slightly ahead of our target. Our expansion into MP is on target and we will continue to open more branches for the remainder of the year. Jayendra Bhai already mentioned this but as far as our branch network, we have about 45 branches in microfinance of which 32 are in Gujarat and 13 are operational in MP with further two opening this month. We have a target of about 59 branches by the end of the year in microfinance division, a bulk of which will be opening in MP in accordance with our MP expansion plan. In our two-heeler division, we currently work with 50 plus dealerships and have four branches that serve as back offices excluding the head office. We are also expanding out of the state in our two-wheeler division. We are actively working to expand into Indore and Ajmer this quarter, so those are two separate states that we are working on expanding our two-wheeler division as well. A vast majority of our microfinance portfolio is just a one year product although we have slowly started with two-year products for old clients in selected location. Last month approximately 20% of our disbursement was a two-year product so this should basically help us push up our AUMs marginally by the end of the year. Disbursements increased 82% year over year in microfinance from 47 Crores to 77 Crores.

We pride ourselves for asset quality, as Jayendra Bhai mentioned that we are absolutely conservative and our conservatism is evident by our NPA level, consolidated net NPA is 84 lakhs compared to an AUM of almost 128 Crores, which equals to a consolidated net NPA percentage of about 0.66%. Overall the industry is doing quite well, although competition has been increasing in certain pockets. The financial inclusion space is getting a lot of government support such as Jan Dhan, small finance bank, MUDRA Bank etc. which should be advantageous to the industry overall though in what way remains to be seen.

Thank you very much for your attention and I think we can open up the call for questions and answers.

Moderator: Thank you. Ladies and gentlemen we will now begin the question and answer session. A first question is from Jeevan Patwa of Candyfloss Advisors. Please go ahead.

Jeevan Patwa: Good afternoon. I just want to understand, you said we will be meeting our target for the year, so what is your target for the year?

Aalok Patel: Target on what matrix Sir, but before you answer my question, I think it would be prudent for me to mention that according to the new Insider Trading Guidelines by SEBI I cannot go into too many details about the projections or the future figures but I can certainly try and give you an overall perspective of what our targets are and what our projections may be. So go ahead Sir, what did you want to hear?

Jeevan Patwa: I basically could not make anything out of your statement. You made a statement saying we are well on track to meet our targets maybe slightly ahead of the target, so I did not understand what target you have set for yourselves?

Aalok Patel: So our overall disbursement target for our microfinance division is between 180 to 185 Crores worth of disbursements for the year with an AUM of approximately 110 to 115 Crores for our microfinance and for our two-wheeler division our disbursement target is approximately 65 Crores with an AUM of approximately the same amount as well. So I was referring to that call where based on our first quarter figures we are well on our way of achieving those targets.

Jeevan Patwa: So are you saying you are basically not looking at growing the two-wheeler business, you are more focused on your microfinance business?

Aalok Patel: We are focused on both microfinance and two-wheeler as well but the growth potential in our microfinance for numerous industry reasons and financial inclusion reasons and otherwise are just a lot sweeter at this point. Two-wheeler financing is a mature industry and the manufacturing side is only growing at about 7% to 8% a year, so to have very large or very high targets in our two-wheeler division can be only achieved if you are working on razor-thin margins or if you are expanding very rapidly, but again expansion is not as easy in two-wheeler because most of the business happens at the dealer location. So to break into new areas is not as simple as just opening a branch in that area. So short way to answer your question is that we are committed to both the businesses, but the potential for our microfinance is just a lot higher at this point. That is it.

Jeevan Patwa: Are you looking at financing three-wheelers?

Aalok Patel: Three-wheeler side we are slowly getting out of it. I will tell you about three wheelers sir is that when we first started it in 2006 or almost 2007 there was a change in law in rickshaws that basically the rickshawallahs had to convert from petrol base to CNG base, so during that time we were the only lender who took a chance on rickshawallahs and it paid us very well because there was a huge market. In today’s scenario, again the competition from banks and all of that because they consider it as SME lending and priority sector lending, banks are coming into this industry in a big way of lending money to rickshaws. Second issue is the replacement side.. They are not issuing any more rickshaw license. So all the business you are getting is basically the replacement side and the third issue, which is actually probably the most important one, is that this is more of a conscious decision for us to move out of the rickshaw side just because it is not the same industry as it was about five years ago. They have issued a lot of licenses, the competition between rickshawallahs is very steep in the areas we operate in number one, number two with all these new avenues opening up for consumers such as Meru, Ola and Uber and all of that, all of a sudden there are multiple choices in an already crowded market. So it is more of a conscious decision for us to slow down our three-wheeler operations mostly due to risk factor.

Jeevan Patwa: Secondly, you also right now said, I do not know whether you right now said or not do you intend to sell other third party products along with your microfinance business?

Aalok Patel: No, I did not mention that. That is something that we can always consider once my customer base increases to a slightly larger level. Cross selling is definitely something we can do and we have done it before selling mobile phones for Videocon. It did not work out very well just because, see the thing with cross selling is the only way you are going to make a material difference to the bottom line is if you are doing a volume game and so at this point it is not something that we are continuing to concentrate on growing the book and growing the client base in a very conservative way of course and then I think either next quarter or the quarter after that we will definitely consider with cross selling which is the natural next step and lot of MFIs are doing it right now, few of them at least are.

Jeevan Patwa: One last question, you basically are focused more on as you said controlled growth right. You are basically trying to control your asset quality while you are growing, which is very good decision actually but just want to understand how do you do that, do you have some kind of framework or some kind of systems in place or some process in place.

Aalok Patel: There are a lot of things, which we do differently then several of other MFIs and I am not saying what they are doing is wrong or right or what have you. Couple of things which we do is that we have a completely centralized decision making process, credit appraisal, so to my knowledge we are probably the only ones who do that. In lot of the other MFIs which you might have heard of, you know the guy doing the sale is doing the credit, which is unfortunately one of the things that lot of MFIs have gotten used to, but we have spent some extra money and tried to centralize as much as we can so the person doing the sale is not making the credit decision that is number one. Second thing, which we very consciously do is that we do not open branches at easy places to do business. So one way to show very large growth is to start doing urban areas, higher ticket size loans doing two-year loans and we do not do that, most of our branches are in rural and semi-urban areas. They are one-year product. Third thing which we do is again, we have a completely risk based approach to everything. So we do not have a static center, we have a closed center. So basically once the center is formed and the loan is disbursed, it is completely closed. Other people cannot join until that loan is complete. We also do telephone verifications both before and after the loan just to cut down on frauds and ever greening and all of those kind of things and I do not know. I mean there are lot of different things that we do just to make sure that our portfolio is of the highest quality. One example I can give you again is the loan tenure. As far as our tenure is concerned, we are concentrating, we are probably one of the only or the few MFIs left, which are doing a one year product, which of course is a very good thing from a risk perspective because my amount is smaller but what Jayendra Bhai said the other day about the number game I can increase my tenure to a two-year product and I can increase my tenure to a two-year product and my assets under management will double because the repayment goes down in half and my loan amount also goes up double since it is two years. Additionally I also provide insurance or I take insurance on both my client and the spouse as well, so we are covered on that angle. So there are multiple things, which we do differently. If you are in Ahmedabad please come down, I would be happy to explain it to you.

Jayendra Patel: Explain to him the AGT and the GAT that we do.

Aalok Patel: Yes, lots of them do that. We actually do a proper training for our client for three days where we teach them financial responsibility and module and joint liabilities and all of those things. Our group approval test takes place by a branch manager only. We have surprise audit teams on the ground which nobody else does where branch audit is one thing but we also have surprise audits in the teams, so there are lots of things.

Jayendra Patel: We put a very strict emphasis on presence whenever there is a central meeting every fortnightly we insist upon that every member should attend, not lots of MFIs do that. They should do it I am not saying what they should do what I should do but we are following our strictest JLG sprit and that is the way we want to continue sir.

Jeevan Patwa: One more last question what is right now your credit cost not credit cost what is your fund cost?

Aalok Patel: Fund cost is somewhere around 15% about 14.5% to 15% on a weighted average cost all inclusive. So that is considered our cash collateral and everything like that.

Jeevan Patwa: So primarily it is from banks, right?

Aalok Patel: No, you can say it is about 50:50, 50% coming from banks and 50% is coming from other financial institutions but our target for the coming year is to try and transfer that as much as possible towards banks and stop relying on financial institutions just because financial institutions come at a higher cost and we are interested in cutting down our cost, interest cost are cost to the ultimate borrowers as well.

Moderator: Thank you. Our next question is from Rajat Sethia, he is an individual investor. Please go ahead.

Rajat Sethia: Sir you talked about processes in approval and your credit appraisal process. Is it possible can you talk about little bit more about what all sort of hierarchy organization level of a loan file passes through, who is the ultimate authority to sanction the loan?

Aalok Patel: The hierarchy you want me to walk you through our entire process from the time that the customer shakes our hands to when the loan is disbursed, did I understand that correctly?

Rajat Sethia: Yes sir.

Aalok Patel: I will go through it might take a while to include all the nitty gritties, but I will try to go as quick as possible. So the first step is forming the group, which we do not actually do. We insist or we guide the members to form their own group. By that way they assess each others. So part of the appraisal also includes that the member themselves should be appraising each other. That is one of the beauties of grameen model. After that we collect their basic KYC details and that gets sent to the head office and we run that through High Mark which is the credit bureau. Now there are certain RBI guidelines regarding over lending and how many MFIs you can lend to so at the High Mark level, at the HO level we will either approve them, the defaults or anything like that we will reject it or if they are over borrowed or if they are over indebted we will reject that and the approved list will go to the branch. At the branch level once they are approved from High Mark, the field officer will start with what we call the group training, we call it the AGT. So that is a three-day training one hour a day at location of the group. So my person will actually go there and do it. There are different modules so most of the things we will talk about will be related to joint liability, there go, meaning that if one person does not pay the other guy pays, we will talk about financial discipline, basic money management skills, talk about how they should be borrowing, how they should be using it for income generating activities and not for personal use, family welfare and all of those other things are there in those modules. Once the AGT side is passed from the field officers then comes the group approval test (GAT), which is done by the branch manager and that serves as a two-pronged approach. So in microfinance there is nothing like income verification because they do not have any proof to verify the income but we do something called a household verification where we try to assess the standard of living and so we try to assess their household side, their household income, their household lifestyle and we try to assess whether they are renting or owning the place and there is a group approval test side as well like my branch manager will ask questions like would you understand the concept of joint liability, what interest rates are you being charged, how much money is going to be, what installment it is going to be etc. After the group approval test gets done, all the documents get sent to the head office. At the head office level, we have our own credit department. We have our own credit department that does its own analysis on the client. It does a telephone verification (TVR) as well, talks to the client, make sure that the High Mark matches and if they feel that the customer is worth it then they pass the loan. After they pass the loan it goes through my MIS department to the accounting department and the cheque is basically sent from the HO after the branch receives the cheque, the following day we transfer the money electronically to the branches bank account and the branch manager will withdraw it. The clients will come to the branch. This is the first time and the only time that they will come to the branch. They will come to the branch to receive the money and after that the loan is disbursed.

Rajat Sethia: Thank you so much for the detailed explanation and if you can also talk about little bit on the repayment side? Can you also talk about the repayment process?

Aalok Patel: The repayment works. The beauty of microfinance is that the clients do not have to come to me to give the money. I go to their doorstep and collect it. So our collections happen at a center level. Each center will have somewhere between 16 to 25 members and that is something my MIS generates something called the demand sheet for a demand report which is printed basically by a field executive and it is done logistically where it says that 8 o'clock he has to go to center number 239 at XYZ place to collect X amount of money and then 8.30 he has to go here and 9 o'clock he has to go there. So he will go for a complete radius in the most efficient route and he will go and collect the money and deposit the money at the branch. At the branch level everything will be reconciled, entered into our daily report what we call it and by about 5 o'clock I will find out whether somebody has paid or not paid or if somebody has defaulted in some small village in Madhya Pradesh. I will find out about it. So I mean the repayment basically happens at the location of the client, which is one of the big advantages of microfinance.

Jayendra Patel: That is where also Sir when I discussed about earlier the presence we insist upon that all the members remain present to give their dues. I do not want to talk about others. What has happened is too much commercialization, and one person comes and gives money for all the members we discourage that. We insist upon that all the members should come to pay their debt; a *prarthana* (prayer) taken place. So we are following a true spirit of joint liability group in which the financial discipline is taught to them in which they are taught that they have borrowed the money and hence they will have to give the money, very simple as that. We also want to tell them in every meeting that this money is given to them for a productive purpose and not for self consumption. My point is the member is taught in each and every meeting that the rule has to be followed and there is a special purpose for this loan.

Rajat Sethia: I really appreciate you explaining in detail. If I may have your permission I would like to ask couple of more questions. Can you tell me about the kind of metric that you guys have in mind in terms of how many clients, how many groups per loan officer?

Aalok Patel: Our average is somewhere around 700 clients per field officer. Our target is somewhere around 800 or so. So we are not quite there yet but very close to it. But some of our best field officers handle about 1000 clients. Lot of this depends on the radius what branch it is, whether it is rural, urban, semi-urban, semi-rural what radius that branch is operating in and what radius the field officer is operating in. So lot of it depends but on average we are at about almost 700 clients per field officer.

Rajat Sethia: A group has how many members?

Aalok Patel: Our average group size is about 18 but it ranges from about 15 to 25. There are exceptions which sometimes we make and it can go as low as 12 or as high as 30 as well but 99% of them will be between 15 and 25.

Rajat Sethia: I read it somewhere that one of the microfinance companies what they do is their field officer is not from the same village or same area. They tend to become friendly and that might crop up, become a reason for issues in terms of collection or that kind?

Jayendra Patel: One of the MFIs is what.

Rajat Sethia: One of the MFIs what they do is, their field officer is not from the same area where he is not taking care of them?

Jayendra Patel: We have similar things, none of our field officers or branch mangers can be posted less than 60 kilometers away from their home town and that sometimes people ask me that is counterintuitive that why do not you take advantage of the guys field knowledge, knowledge of the area and when I go into an area I want to depend on my own surveys or village surveys or branch surveys. I do not want to depend on the field officers biased views on which areas are good or bad neither do I want the field officer to start lending to his area or his relatives or his friends or his *risthedaars* (relatives), so we do not post them anywhere close to their home town.

Moderator: Our next question is from Ayush Mittal of Mittal and Co. Please go ahead.

Ayush Mittal: Good afternoon sir, first of all I would like to congratulate and appreciate the good performance company has been doing. I would like to understand like you had been sharing about your process by which you have been able to control the NPAs. The NPAs are very low. While what we have seen in some of the other NBFCs is once they achieve a scale, collection becomes a big problem and the collection cost goes up substantially, how many collection agents or people do you have and can you talk about your collection process and if there can be a risk on this going forward as the loan amount is very small?

Aalok Patel: This is my view. I could be wrong on this but my view is that once you grow to a very large size what you start achieving on an operational level at least is certain diseconomies of scale. So we have four or five field officers stay in a branch and about 3300 members are in one branch but just to give you a perspective on our collection cost, one way you can cut down is instead of a biweekly collection model you start collecting on a monthly model. You start increasing your loan amount. So the installment amount becomes higher and you can go there. So these are all ways to become more efficient as far as on the collection side. What you will see in some of the larger MFI the diseconomies of scale side is that the larger you get the more layers you have to keep. So this is a cash business at the end of the day. So it is almost like a casino that everybody has to be watching everybody else. As you keep adding more and more layers, your operational cost becomes higher and higher just because I cannot expect my field officer to handle more than 800 or 900 clients realistically speaking and that will be the same whether you consider us or any of the larger MFIs as well. So the base level is set, the variable cost side on the base level is set that okay I cannot get more efficient than let us say 1000 clients per field officer. So if I have one Crore clients I will need that many divided by 1000 field officers that is just how the industry works. How we try to gain some efficiency is that we make sure we plan the route correctly. We make sure our field officers are motivated correctly. We make sure everything works properly as far as the timing that not everybody, they should not even get five minutes late because if my own field officer reaches five minutes late I cannot expect the client to show up on time. So we are very strict about those kinds of things, but it is a costly operation I would not lie to you. That is one of the reasons when somebody who does not understand the business asks about what interest rates I charge and I tell them if they do not understand that, then I feel on their face that I have already lost half the battle because they are not going to understand operating cost and low cost funding and all of those kinds of things so. Does that answer your question?

Ayush Mittal: Second question of mine is regarding the promoter holding like as of now we are a small sized company in the space and as a NBFCs business we need money and we might need to raise funds from time to time. To start with if the promoter holding is small how do you plan to do this going forward?

Aalok Patel: So that is obviously a challenge that we always say when we got diluted with Incofin which is the private equity company that has invested that was something that we were concerned about as well. In 1995 when the IPO happened we got diluted then for a very small amount. So there is not much we can change about that. We actively try to make sure that our holding is maintained at the current level. There will come a time that if we want to keep growing at 40% to 50% a year, we will have to dilute. So if we were only growing at our ROEs at about 18% or something a year, our ROEs could support our own growth. If you want to continue growing 40% to 50% then we will have to consider dilution and this bring us to an age-old debate of whether you want to own a big piece of a small pie or a small piece of a big pie. It is a challenge and I do not know how exactly to answer your question, but just microfinance works in a way that everybody has been growing rapidly, so lot of the larger MFIs the promoter holdings are down to single digit. Not that I want to bring mine down to single digit levels but eventually we will have to consider because there is only so much of our own personal funds that we can keep pumping in, we have our own limits that is a concern.

Moderator: Thank you. Our next question is from Ayush Shah of DK Modi Securities. Please go ahead.

Ayush Shah: Sir, any chance of the Namra being listed in the foreseeable future?

Aalok Patel: Listed in the foreseeable future, no we have not thought about that. Right now it is a 100% owned subsidiary, at least not in the next two to three years but after that if Namra has to stand on its own two feet and it is no longer a 100% owned subsidiary, then definitely we can consider that as well. See let me tell you on a side note why this entire Namra was formed was simply because of a regulatory reasons. There was no other reason for me to split our microfinance operations from Arman to Namra. The RBI circular that came out that basically said that if you are doing microfinance then 85% of your assets have to be in the form of qualified assets. Now we were one of the very few or I guess the only company in India that had a diversified portfolio. We were doing asset financing and microfinancing so with RBI's blessing we basically applied for a fresh NBFC license, MFI license under a wholly-owned subsidiary kind of form and we were the first NBFC, we got the first NBFC, MFI license in India surprisingly. So that was the reason for forming Namra but I do not know I mean if it is helpful then we can if we have to then I do not have any qualms per se of listing Namra just we have not considered it yet.

Moderator: Thank you. Our next question is from Anil Tulsiram of Contrarian Value Edge. Please go ahead.

Anil Tulsiram: Thanks for taking my question. My question is there are many other NBFCs in microfinance with cost of funds substantially lower than yours, so if those companies decide to enter you area aggressively, so how will you compete with them?

Aalok Patel: Let me tell you something there are some larger MFIs that have a cost of funds which is lower than ours and I think when they started they were our size and they were facing with cost of funds similar to ours as well. The cost has very little to do with microfinance. If I decide to cut my interest rate by 5% on an installment basis it will only makes somewhere around Rs.10 difference to my clients. Really I mean you cannot buy a cup of tea nowadays for 10 rupees, my clients do not really look at the overall interest IRR basis what they care more about is effective delivery, good service, timely delivery of funds and lot of those kinds of things are in the matter. I am not saying the cost does not matter at all to the clients because obviously that is not true but if you want to put a weightage to it, it is very small in the single digit especially what the larger MFIs are charging. There might be a 400 basis point difference between what I charge and what the lowest MFI in India charges but really that will not make much of a difference in the long run as far as my market, it will be negligible.

Jayendra Patel: Let me also tell you this same issue was raised in Delhi when I was attending one seminar in Ministry of Finance and I also raised a issue that just suppose (*one shopwala woh lorry lekey nikaltha hai*) one shop owner goes out with a lorry, suppose if he needs Rs.5000 in the morning to fill up that lorry with vegetables for him it is very important then he gets that Rs.5000 the day earlier. See the issue is not saying that (*woh paanch hazaar ki lorry laker nikaltha hai*) he takes out the lorry worth 5,000, so I am sure he is going to collect Rs.7000 to Rs.8000 on that Rs.5000 lorry. He does not mind giving you Rs.10 more for that entire Rs.5000 biweekly or whatever. The issue for him is the timely delivery of the credit.

That is very important for which he cannot go to anybody but to a microfinance company. That is what my point is a couple of percent here and there is not going to make a material difference. The difference is there are other reasons whether he is getting a credit on time, whether the time for collection is suitable time, what are the other members that are in his community, so there are other issues, do my field officer speak Gujarati or not. A lot of the south companies they come with their own employees and they speak Hindi, they do not like that. There are numerous things that the client wants and needs. Some of them might be looking for the lowest cost, in that case we might lose that client but the vast majority is not that sensitive to interest rates at least yet.

Anil Tulsiram: My next question is can you give me broad breakup between agriculture and non-agriculture loan?

Aalok Patel: We do not lend to pure agriculture. We do have about allied agriculture and agri based like cattle and what not. I have to pull that exact number but approximately 40% of my portfolio you can say is allied agriculture while the remaining is other things, Its about 40% to 45%, so a significant amount.

Anil Tulsiram: Another thing which I am trying to understand is for the last one year there are many thoughts of rural stress going on but that is not evident in the microfinance. Is it because you do not lend to agriculture or is there some other reason?

Jayendra Patel: Sorry can you speak up.

Anil Tulsiram: For the last one year, there are many headlines of rural financial stress from the rural people.

Jayendra Patel: That is always the case. I think in my previous statement I mentioned that so we do not lend to direct agri because direct agri always comes with its own issues, there is always too much rain or too little rain. There is always some write off given by some politician and local politician and farmer suicide and all of that stuff. So it is not fair for me to completely cut them out of microfinance per se but that is one of the reason why we do not lend to direct agri, as close as we get to agri is cattle basically, cows and milk-based products and things of that sort. But you are right sir in the news there have been things like farmer suicides and things of that sort. I hope other microfinance are wise enough to stay away because farmers are getting covered by SHG and lot of other government programmes and every few years there is some government mandated write-off in the thousands of Crores of rupees and then in the end the person who suffers is the financial institutions and the bankers so it is a big risk.

Anil Tulsiram: What is your client retention rate, how frequently the group gets split up there is a churn in the customers?

Aalok Patel: At least about 55% of our clients in our portfolio are second cycle or more, so the majority of our clients are basically retained clients 55% to 60%, so we do an excellent job of retaining our clients and that is one of the ways that we can also offset the lower interest rate charged by the competitors, just like lot of us our clients do not like changing it, they are satisfied with us then they will come to us in the future for their borrowing needs as well.

Moderator: Thank you. Our next question is from Swapnil Desai of Turtle Capital. Please go ahead.

Swapnil Desai: Hi Sir, thanks for the opportunity. Sir, my first question is regarding your focus that you have now started lending the two-year loans which you used to lend only one year loan before so what is the impact that it can have on your return on assets and other financial metrics as two year loans start to grow in your portfolio?

Aalok Patel: See as far as return on assets and things of that sort are concerned, I do not have those exact figures in front of me based on our two-year loan. What I can tell you is that for our two-year loan products we have started with our third cycle customers in selected areas. Last month about 18% of our disbursement was in the form of two-year loans and currently we have about out of approximately 1 lakh clients, 3700 clients of ours are in the two-year loan product. So it is not a very large proportion of our portfolio currently. In the future I would imagine by the end of the year the portfolio in our two year loan product would be somewhere in 20% to 25%. As far as the ROEs are concerned, if you do the ratio analysis our portfolio will increase but the related income will also increase because it is a larger amount so I do not think it will per se have a big impact on the return on assets, what we will manage doing with the two-year products is saving a little bit on the cost, because the disbursement does cost money as far as our incentives go and the cost and the book size should increase as well, we will have a bigger base to earn interest income.

Swapnil Desai: Sir my next question is that I think last time I met Aalok probably you were evaluating whether to enter into MP markets and also on the cards was entering into Maharashtra market, so what I understand now is that your complete focus is now in MP market and you are scaling up the business there, so what is the timeframe in which you think that the MP market can be fully explored and whether there are any plans to enter into Maharashtra market after you explore the MP market?

Aalok Patel: See MP market is quite larger than Gujarat market because in Gujarat the entire Kutch area and the Saurashtra area we are not touching. There we are going to the Surat side as well, so we are concentrating in Gujarat mostly in the eastern side, the central side the northern side basically. MP, we are not concentrating again on the eastern side but other side central, west, and north and south is again fair game. There are pockets in MP which again I do not want to go to, I would say that it will take us at least the rest of this year and the majority of next year to fully explore and open up all the branches that we need to in MP which is not to say that we will not consider expanding to another state next fiscal year. This fiscal year we do not have any plans because we have our hands full with the MP expansion but next year we can either consider Rajasthan or Maharashtra as far as expansion. I am a little biased towards Maharashtra but this will have to be a joint decision between all the management and board and everybody included so we will evaluate it at that point.

Swapnil Desai: And my another question was related to, I think you have around 13 branches in MP and I think most of them are probably less than one year old or maybe few of them are slightly more older than one year, but how many of them have achieved breakeven and what is the typical time that it takes for the branch to achieve breakeven?

Aalok Patel: Typically speaking between 600 and 800 clients is where we see the breakeven point. If you look at our branches right now, some of the branch about I do not know I have the figures in front of me, on an average my MP branches have a client count of 650 so on an average we have broken even in MP although there are some branches which have 50 clients and 49 clients other branches like Rau and Ujjain I have 1200 or 1200 plus clients so those are definitely profitable. My Indore branch is the only branch which is more than one year old and I have 1900 clients in Indore so that is quite okay as well. The thing with MP is that especially when you look at Indore, Ujjain and Rau and all of those areas we are a late mover into that areas. There are already established players so you cannot grow that easily especially in the urban area you have to go little far and it takes time to build good asset or client base in MP, but honestly I did not think that we would manage getting, initially when we went that we would manage getting about 2000 clients in one year in Indore but we achieved it and the quality is good as well, we are yet to see any default or anything in Indore but to answer your question yes, about 600–700 clients is where we see breakeven approximately and then the average is…

Swapnil Desai: To get around 600 to 800 clients, do you take around seven to eight months or slightly longer than that?

Aalok Patel: It will take about six months, because it initially starts a little slow depends on area whether it is rural, urban; how many MFIs are existing, what quality of staff I send there, how much experience they come with, lot of those things matter.

Swapnil Desai: But we can safely assume around eight to nine months typically?

Aalok Patel: Yes you can.

Swapnil Desai: And the last one if I can just squeeze in, is that I think probably you said that by end of FY'16 you want to increase the branches to 59 and most of them are going to be in MP, so I think all put together we will be having more than 25 branches in MP by end of FY'16 so what is the potential in terms of number of branches that you are seeing in MP and it is an excess of 25 but maybe around 40 or what is that number?

Aalok Patel: Earlier when we went there, we estimated around 35 branches. Right now it might be slightly more than that but lot would depend on the surveys and things which we would do, so we have surveys done for about five additional branches. On top of that, we will be evaluating other areas as well, so it is a little soon to tell but yes you are right somewhere in between 35 to 40 max.

Moderator: Thank you. I now hand the floor back to Mr. Digant Haria. Over to you sir!

Digant Haria: Thank you everyone for joining the call and a special thanks to the management for taking time out and explaining and giving an overview about the company and the results. Thanks everyone and have a great evening.

Moderator: Thank you. Ladies and gentlemen on behalf of Antique Stock Broking that concludes this conference. Thank you for joining us, you may now disconnect your lines.