

L&T Finance Holdings Ltd.
Q3 FY23 Earnings Call Transcript
January 16, 2023

Management Personnel:

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Moderator:

Ladies and gentlemen, good day, and welcome to the L&T Finance Holdings' Q3FY23 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded. We have with us today, Mr. Dinanath Dubhashi, Managing Director and CEO and other members of the senior management team.

Before we proceed, as a standard disclaimer, no unpublished price-sensitive information will be shared during the call, only publicly available documents will be referred to for discussions during interaction in the call. While all efforts will be made to ensure that no unpublished price-sensitive information will be shared, in case of any inadvertent disclosure, the same would, in any case, form part of the recording of the call. Further, some of the statements made on today's call may be forward-looking in nature. A note to this effect is provided in the Q3 results presentation sent out to all of you earlier.

I would now like to invite Mr. Dinanath Dubhashi to share his thoughts on the company's performance and the strategy of the company going forward. Thank you and over to you, sir.

Dinanath Dubhashi:

Thank you. A very good morning to everybody. And let me at the outset, wish you all a very-very Happy New Year. We at L&T Finance, enter this New Year with immense zeal and passion as the Q3FY23, this quarter, particularly following the previous two quarters has been excellent for us on account of multiple reasons. We have touched new highs on the business side again, in this quarter, across various business verticals that we operate in and have also performed well on driving various Lakshya's strategic initiatives, all of which have immensely motivated us to keep delivering great results in the future also. My presentation to you today will revolve, hence, around these two themes:

- 1) **Update on business parameters** i.e., our strengths, business performance for the quarter, etc. And more importantly, how are we driving the organization towards Retail growth and Retailisation.
- 2) Number 2, which is quite particular to this quarter, is about **Lakshya's strategic initiatives**. Specifically speaking, sale of Mutual Fund, enhanced Retailisation through an accelerated sell-down of Wholesale book
- 3) And last but not the least, the proposed merger of our various entities.

It has been now close to eight months since we unveiled our strategic plan, Lakshya 2026. We did that in May'22, wherein we shared our strategic goal to make L&T Finance, a top class digitally enabled Retail finance company, moving forward from a 'product-focused' or a 'product excellence approach' to a 'customer-focused' approach, especially by creating a Fintech@Scale. Every word of this line is important, and we have worked on every word. In fact, every decision we have taken ever since has been keeping in mind the targets of Lakshya 2026. Though our goal is to achieve our targets by FY26, we continue to strive and drive our efforts towards achieving them well before that year, that is, much before FY26.

The last time when we met at the end of the Q2FY23 results, I had reiterated the confidence that as we traverse on the path of Lakshya 2026, we will deliver the results promised while continuing to improve the products and services we offer to our customers. With every passing day, we are working towards making our company one of the top NBFCs in the country that caters to Rural, Urban mass affluents, Aspirers and SME segment of the country. Thus, broadly covering the whole gamut of the Retail lending space. Our strategy of retaining our customers and using them for cross-selling and upselling our offerings has been working well. Capturing new customers as well as farming existing customers is enabling us in our efforts to deliver consistent results. Through a better understanding of our customer needs, we are firmly etching ourselves in the mind of our customers and, we believe, are creating ongoing strong customer franchise.

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Today, I can say this with firm belief that with the strong Business, Liability and Fintech franchise that we have created and a well-defined strategic roadmap in place, L&T Finance is strongly positioned to fully transform itself into a top-class Retail finance company. The scaling up of Retail business over the past three quarters has been made possible due to the strong Retail franchise that we have built actually over the past seven years and kept on and particularly strengthened it over the last two years on the foundation of digital and data analytics.

Now allow me to talk about a few numbers here for Q3FY23:

- 1) Retail book has reached now Rs. 57,000 Cr, which is a 34% Y-o-Y growth and a 10% Q-o-Q growth, which is comparing very-very well with our target of at least 25% CAGR. Now, the Retail portfolio has reached 64% of our total book already
- 2) Retail disbursements reached an all-time high of Rs. 11,607 crores in the quarter, up 53%. And this is actually the first time that we have crossed Rs. 11,000 crores level in a quarter.
- 3) Improvement has been witnessed across asset quality parameters with Retail GS3 now down by 38 basis points Y-o-Y to 3.47% and NS3 down 45 basis points Y-o-Y to 0.73%. Let me point out that our Lakshya goal is less than 1% (NS3). We are already there and very confident of maintaining and improving it. PCR, Retail PCR is at 79%
- 4) We have delivered a total PAT of Rs. 454 crores, up 39% and the Retail PAT now is almost 87% of the total PAT at Rs. 394 crores.
- 5) The Retail Return on Assets (RoA) is already 2.6% in Q3FY23 with RoE i.e., Retail RoE reaching 14.97% during the quarter. Again, reminding you, our FY26 goal is 3% RoA. So actually, if you see, the Retailisation, Retail growth, GS3, NS3 and RoA numbers are quickly approaching levels of our FY26 target, which makes us confident that we will probably achieve or exceed these targets much earlier than that.

Guidance on Sustainable Retail RoA

I would take this opportunity now to pause for a moment and explain a bit about the Retail RoA tree that we aspire to not only achieve but sustainably achieve. With the current pace of Retailisation, our Retail RoAs are trending well towards the targeted 3% range, which as I said for Q3, it is already 2.61%. Accordingly, our guidance for a steady state RoA is as follows:

- Retail NIMs, which you would see is at 11.4%, through ups and downs, interest rates, etc., we clearly expect this to be a minimum of 11%, or trend towards that number
- Opex + credit cost number in the medium term should start trending to about 7%
- Thus, yielding a pre-tax RoA of 4% and post-tax RoA of 3%

That's what we are targeting towards. Obviously, work is on, on every aspect of this.

As far as growth is concerned, we had promised at the beginning of Lakshya 2026 that the CAGR of our Retail book will be at least 25%. The growth we have been able to achieve in the first nine months of the financial year makes us very confident that we will be able to exceed this target comfortably. This confidence stems from the on-ground capabilities we are building in our existing products, the rapid scale-up we have been able to achieve in recently launched products, and the product launches we have got planned over the next couple of quarters, and last but not the least, the geo-agnostic PLANET App capabilities that we are building.

So, RoA trending, as I indicated. Retail growth, we expect to comfortably be above the 25% target. These are the numbers we are working towards and are confident of delivering consistently. That's our idea of a top-class Retail finance company powered by digitization and data analytics.

Having spoken about the Retail franchise, let me now make a mention of other strengths that we have built over the years, which have emerged as sustainable differentiators. Just to count a few:

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- i) AAA-rated liability franchise with a strong CRAR
- ii) Transformational Digital and Data Analytics: We have integrated now 100+ fintech partners with 40-plus algorithms, which has helped us in transforming our digital and data analytics
- iii) A granular customer franchise and distribution network: With a database of about 2 crore customers and a strong distribution network of 16,000+ partner touch points, we are now firmly etching ourselves in the minds of the customer as well as in the geographies
- iv) High customer retention: We have a customer retention or repeat business of more than 30%, which has helped us in cross-selling and upselling our products. And I'm talking about this for only loan products repeat business. For insurance products, we do CLI and other business, obviously, they are much-much higher.
- v) I would specifically like to talk about the PLANET App, which is an augmented customer-facing interface. Our D2C app, which is named PLANET, was launched in March'22 has already crossed 17 lakhs downloads and has witnessed more than Rs. 970 crores of disbursement till December (this is including the website app also), while processing almost Rs. 117 crores of payment i.e., collections. This application is available both on App Store and Play Store and has been rated 4.3.

Having added features like credit scorecard in Q1FY23 and Insta loan for Consumer Loans in Q2FY23, we launched the following additional features in Q3 - which is mandi price for our Farm customers and wellness insurance.

Going forward, the company will continue reimagining customer engagement by incorporating features like:

- a. Self-driven customer journeys for Two-wheeler loans. This will actually include an end-to-end journey where you can choose a two-wheeler, you can choose the dealer, you can book a test drive, you can book the loan. And I mean, there are only two physical parts in it. One is the test drive, which you have to drive on a physical two-wheeler and then take the delivery of a physical two-wheeler, everything else will be done on the app
- b. Rewards and referrals
- c. Utility payment
- d. Hospicash insurance, etc.

Making it closer to a full-fledged fintech app and now slowly taking it towards a complete marketplace. We envision this app developing into a full-fledged marketplace, enabling prospection, customer onboarding, customer retention and most importantly, what we are concentrating is customer servicing, for a seamless service experience. In addition to that, it will also have many value-added services making it attractive for our customers to use it.

Now, coming to some of the updates on our delivery of Strategic initiatives, which were three parts: one, unlocking value by sale of Mutual Fund, accelerated Retailisation and Merger to form a unified operating lending entity. So let me discuss this one-by-one:

- 1) **Sale of mutual fund:** As you are well aware, L&T Finance Holdings had entered into a definitive arrangement with HSBC AMC on 23rd December'2021, almost one year back, to sell 100% stake in its Mutual Fund arm to HSBC. The sale was finally completed after all the regulatory approvals on 25th of November 2022. As a part of the transaction, we received a sale consideration of Rs. 3,485 crores and surplus cash balance, which we could take out of Rs. 764 crores, thus totaling, the total consideration to Rs. 4,249 crores. This amounts to 5.7% of the AUM of the Mutual Fund as on the closing date. The capital gains realized from the above amounted to a post-tax number, after capital gains tax, of Rs. 2,160 crores. This, according to us, clearly indicates the strength of business we have built over the years and the value unlocked from it will clearly help us in furthering our Lakshya objectives.
- 2) **Focused Retailisation:** Our Retailisation transformation journey is a mix of two key pillars:
 - a. Organic strong Retail growth and
 - b. Reduction of the Wholesale portfolio

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As far as the strong Retail growth is concerned, I've briefly spoken about it and we'll dwell deeper in the later part of the call.

As far as the second pillar, reduction of Wholesale portfolio is concerned, we had earlier communicated our intent to explore the divestment of the Wholesale book through sale and realising value, etc. Not having concluded the above exercise, the Wholesale book reduction is now envisaged to be achieved through a combination of various means and that too fairly rapidly, like repayments, prepayments, sell-down of loans etc.

In this regard, it is important to highlight two major aspects:

- First, the Wholesale portfolio now, October onwards, we actually started this rapid sell-down, rapid reduction. The Wholesale portfolio has sharply reduced to about Rs. 31,000 crores now, as compared to Rs. 41,000 crores approximately a year back. And even just three months back, that is as of 30th September, it was Rs. 37,597 crores. So, this book reduction now is happening quite rapidly, 18% Q-on-Q. And it mainly comprises of prepayments, repayments of about Rs. 4,200 crores and sell-down volumes of about Rs. 2,900-odd crores.
- Simultaneously, in accordance with the renewed strategy, in order to pivot towards Retailisation, we have now decided to change the business model in Wholesale to enable an accelerated sell-down. To reflect the change in business model under Ind AS, the assets in Wholesale are now reclassified from Amortized Cost to a Fair Value Through Profit and Loss, and we have tried to explain this in detail in our investor presentation as well as financial results. In line with this, a fair valuation of the Wholesale assets was conducted by independent valuer. Since the book is quite good, at the first stage, the valuer evaluated the fair value largely the same as there was no change in the underlying asset quality.

However, given a shift to accelerated sell-down of the Wholesale book, certain 'illiquidity discounts' were to be considered during the sell-down, and it is possible that there will be 'illiquidity discounts' to be given to a buyer during the sell-down. To give effect to this, a one-time provision of exactly Rs. 2,687 crores has been created on account of this reclassification, consequent to the change in business model and the fair valuation of the Wholesale book to facilitate the rapid sell-down process.

Through this accelerated sell-down, while we have promised achieving the Retailisation of 80% by the end of FY26 as per our original Lakshya plan, we expect to sell-down the Wholesale book in a much more rapid manner, which we believe will help us achieve much higher than that 80%, perhaps closer to 90% Retailisation by end of FY24. We firmly believe that these provisions will be sufficient, the provisions that we have created will be sufficient to cover any downside risk of such accelerated sell-down, thereby not impacting Retail growth or Retail profitability going forward.

I hope that you have got ample clarity now on what we propose to do as far as the business strategy for increased Retailisation and reducing Wholesale is concerned.

3) Now, the merger process i.e., transforming to a 'Unified Operational Retail lending entity'

One of the top most priorities that we are going to focus now is to make L&T Finance into a 'Unified Operational lending entity'. I will explain the background of this proposed merger. Since 2016, LTFH has embarked on a strategic rationalization of companies. This particular initiative comprising merger of various subsidiary entities through the 'Right Structure' initiative, led to reduction of number of lending entities from 7 in 2016 to 2 by 2022 i.e., L&T Finance Limited and L&T Infra Credit Limited, which resulted in simplification of corporate structure along with enhanced governance and controls.

In continuation of our guidance towards moving to a one company structure, LTFH, post the sale of Mutual Fund now has proposed the merger of its subsidiary lending entities i.e., L&T Finance Limited and L&T Infra Credit Limited with the non-lending listed holding company, L&T Finance Holdings Limited, since the holding structure

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is not relevant anymore after the sale of Mutual Fund. Just to explain very clearly, the regulator was not in favor of an operating NBFC holding the Mutual Fund and hence, the CIC structure was relevant.

Now that we have only lending business, that is not relevant and hence, there will be only one monolithic NBFC in the group. What this would result in is a simple one entity structure, which goes in line with our intent to have a right structure, leading to optimal utilization of capital and effective utilization of management bandwidth. Needless to say, of course, that this merger would be subject to necessary statutory and regulatory approvals and clearances. We believe that it will take a good part of FY24 for it to finally happen.

Now allow me to deep dive into some of the operating numbers:

1) Disbursements

As I have said, we have seen the highest ever Retail disbursements. Retail disbursements stood at Rs. 11,600 crores, up 53% Y-o-Y. This has resulted in Retail book growing 34% Y-o-Y and 10% Q-on-Q. Overall, Retail mix has grown to 64% from 50% last year and 58% in Q2FY23 itself, and we hope to show you a much higher percentage even by the end of this year. These numbers indicate the strength of the business franchise we have built over the years. I would like to take a moment here to highlight that we have been successively posting highest ever quarterly Retail disbursements - first in Q1FY23, which had then surpassed Q4FY22 levels, followed by Q2 and then now in Q3. Of course, there are a lot of businesses which are seasonal, but we expect overall a trend of good strong Retail disbursements to continue.

At this juncture, I would like to give you a flavor of how performance of various macroeconomic variables, which have a bearing on our businesses have been taken into account while arriving at various decisions. At L&T Finance, we are greatly influenced by the inputs of our Chief Economist team on all the relevant variables that have a decisive influence on the agricultural cash flows, especially rural cash flows, like sowing progression, water reservoir status, mandi prices, employment levels, inflationary trends, liquidity pressures, etc. These insights are of immense value, not only for business planning, but even for actual resource allocation as well as credit decision making. Also, these serve as very good early warning signals for us to be better prepared for future.

Broader movement of macroeconomic variables suggests that rural demand this year is expected to stay reasonably buoyant in the remaining of FY23 and at least in the first half of FY24, and then, of course, we will have to see the monsoon. Healthy Rabi sowing, good kharif procurement and hopefully, likely exports of wheat have kept the investment sentiment upbeat in the rural areas.

We see good progression in the Rabi sowing season with higher water storage levels and improved soil moisture. During the first three months of Rabi sowing season, i.e., till December, the total sown area surpassed the normal area for all major crops with all states reporting higher Rabi acreage barring five states, which are Telangana, Haryana, Gujarat, Punjab and Uttarakhand. Other than this, all other states have reported higher area under sowing of Rabi leading to higher chances of a bumper Rabi crop. This progress in Rabi sowing gives us tremendous hope that it will offset the dent in total food grain production, which we have seen during the kharif season.

The 2022 North-East monsoon progression is now already in the surplus with a cumulative rain precipitation being 19% above normal. The water storage positions across reservoirs is not only higher than normal but also higher on a Y-o-Y basis. All regions have now reported healthy water storage positions barring some eastern and southern regions on a Y-o-Y basis. Over the past few weeks, however, of course, the storage position has moderated, but still, we believe that this will lead to a good Rabi season.

The MGNREGA Statistics until December'22 show that all India daily average wage rate under the MGNREGA scheme is higher than the previous year.

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Thanks to the ongoing Rabi sowing, the job demand in rural areas is largely met. According to CMIE, while the urban unemployment rate rose to 10.09% from 8.96% the previous month, in December the rural unemployment rate has actually declined from 7.55% to 7.44%. The same statistics indicate that until December'22, the all-India daily average wage rate under the MGNREGA scheme is also higher than the previous year. As such, all indicators are trending to reasonably positive.

So, as far as the overall rural growth is concerned, I'm pretty sure that the momentum is a sustained one and the rural demand in different geographies will present us with good opportunities to grow our rural business in future.

Let me now talk about the performance of respective businesses:

Rural Business Finance, (previously known as Micro Loans): This business recorded the highest-ever Q3 disbursement of Rs. 4,281 crores, with the book growing 46% Y-o-Y. Today, it stands at around Rs. 17,500 crores. This growth was aided with help of initiatives like focus on repeat customer conversion only for our '0 DPD' customers, exclusive customer loans i.e. customers exclusive only to L&T Finance, calibrated geo strategy, a best-in-class turnaround time and data-based credit algorithms. And I would like to point out that we were clearly the pioneers of data-based credit algorithms in this business while continuing to maintain a collection discipline of timely execution and strengthening various product portfolio monitoring metrics. The monthly disbursement rate has been maintained at around Rs. 1,400 crores with fresh and repeat disbursements, respectively, at 49% and 51%.

As explained in the earnings call of Q1FY23, subsequent to the master directions issued by RBI on this business, we swiftly modified our sourcing digital app for calculation of household income and made changes in the processes. Lending could happen using advanced credit metrics now in households with an income of more than 3 lakhs. This opened up tremendous opportunities at good credit costs, acceptable credit costs. Going forward, in this business, the company expects to sustain the momentum by launching new products like, Rural Loan Against Property. That is the first one off the ground in addition to our group loan product.

Farmer Finance: From being one of the leading financiers in this segment, today L&T Finance has a leadership position in farmer finance with about 15% market share. This has been done with the help of a well-diversified footprint of ~170 branches across 16 states and the vintage now of about 17-plus years. We have built our partnerships, with a tie-up with more than 2,500 dealers. As a result, we achieved the highest ever monthly disbursements of Rs. 900 crores, the best ever quarterly Retail disbursements of about Rs. 2,057 crores in Q3FY23 and the highest ever quarterly disbursements of about 40,000 units. Repeat customer disbursements have grown from about Rs. 160 crores to Rs. 270 in Q3FY23. The book size now has crossed Rs. 12,000 crores mark. So again, this business doing extremely well.

Urban Finance:

As we come to Urban Finance, which comprises of Two-wheeler, Consumer Loans and Home Loans/LAP business, we saw 55% jump in overall disbursement, resulting in a 34% Y-o-Y increase in book size.

Two Wheelers: Our Two-wheeler business saw the highest-ever quarterly disbursement of Rs. 2,146 crores, up 31% Y-o-Y. We, in October, actually achieved highest ever monthly disbursement of ~Rs. 1,000 crores. Q-on-Q growth in units disbursed stood at 14%. The book size stood at Rs. 8,716 crores, which is now 19% growth Y-o-Y. Our two special products, which is Sabse Khaas Loans and the VIP scheme, which according to us is very customer-friendly product, increases finance penetration and more importantly, much more improves our portfolio quality and reduces collection costs. These two products, now penetration stands at 23% of the total disbursement in Q3FY23.

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As a step towards expanding geographically, we have been opening new branches. As a result of attractive customer offerings and schemes, L&T Finance's disbursements have grown at 31% Y-o-Y, which was better than the industry average of 22%. By maintaining a strong focus on customer value, building preferred dealer OEM relationship with more than 5,000 dealers to grow our market share, the business is delivering on a strategy built around dominating counter share of preferred partners and offering mutual value by leveraging the increased application of data analytics.

I would like to add here something very interesting that adding to our endeavor to create customer-initiated journeys and reimagining customer engagement, we now propose to launch a digital Two-wheeler journey on PLANET App, wherein the customer can purchase the two-wheeler from the comfort of his home without visiting the dealer outlet. This would cover the entire customer journey for selection, test drive of the two-wheeler, onboarding and digital sanction along with insurance, payment and setting bank mandates followed by delivery of the two-wheeler. With this, we believe that experience of purchasing the two-wheeler by a customer would undergo a significant shift on the back of technology and digital process. We, of course, believe that the takeoff of this will be slow. But like all things digital, we believe the pickup after that to be pretty rapid and fast.

Consumer Loans: Our Consumer Loans, which is one of our newest products and our digital native product has now had a monthly run rate of about Rs. 400 crores per month during this quarter. Our digital aggregator partnership has now crossed Rs. 100 crores on a monthly basis. Disbursements stood at Rs. 1,228 crores in Q3. The business continues to build significant scale by cross-selling to L&T Finance's existing customers as well as open market customers. Repeat customer base increased to 44% now Q-on-Q on account of active analytics engagement. The company increased its customer funnel through channels like new partnerships with e-aggregators and Insta loans for potential customers. In this segment too, we are working on initiatives like starting new programs for higher ticket salaried Personal Loan (PL) and of course, new to credit through banking products and increasing the spectrum of digital partners by utilizing the digital stack.

Retail Housing: The Retail housing disbursements now stood at around Rs. 1,200 crores, up 83% Y-o-Y and 7% Q-on-Q. We remain focused on enhancing disbursement volumes by deepening geographical presence, solid DSA partnerships and increasing customer retention. We have also worked incessantly towards reducing our book attrition, what is called BT out, through a proactive and improved proposition. The share of the self-employed segment in the overall Home Loan (HL) disbursement increased to 33% now as against 12% in last year.

SME Finance: Last but not the least, actually the newest product that we have is SME Finance. The pilot of SME product, which was launched in Q3FY22 has witnessed a steady pickup ever since. In Q3FY23, monthly disbursement crossed Rs. 200 crores. For the quarter, the disbursement stood at Rs. 538 crores, and the book size increased to Rs. 838 crores. This was led by significant geographical and channel expansion. We also launched a new product in November'22 in addition to our unsecured business loan. The new product is called Dropline overdraft facility in order to provide added value to our SME customers. The business has been operationalized in multiple locations now till December'22, and we expect it to significantly scale up in times to come.

2) Retail Collections

On the collection side, L&T Finance witnessed best-in-class collections in Q3FY23 across all business verticals, led by the company's concerted on-field efforts, analytics led prioritization and use of propensity-based data analytics to channelize resources. Collection efficiencies across businesses have trended extremely well.

Given the way collection efficiencies and performance of portfolios across various buckets is trending coupled with operational efficiencies, which are expected to kick in, in the medium term, we are confident that the Retail opex + credit cost will trend towards the targeted 7% range in the medium term.

3) Astute Liability Management

On the liability side, with the change in interest rate trajectory through successive hikes by RBI, the industry is obviously experiencing an increase in cost. L&T Finance continued its approach of locking in adequate medium- and long-term borrowings, which has helped us to contain the increase in weighted average cost. Overall, the quarterly WAC i.e., weighted average cost for Q3FY23 stood at 7.54% against 7.33% in Q2. Obviously, the increase in WAC was due to the re-pricing of floating rate liabilities and higher cost of incremental debt. Here, the point of highlight is that the quantum of long-term funds we raised was about Rs. 6,500 crores in Q3 as against Rs. 8,200 in Q2 and last Q3 was just about Rs. 2,000 crores. Average CP proportion was kept low at around 9%, and this holds us in good stead because with Wholesale going, the overall ALM will work in our favor with the overall duration of asset side coming down. And that will obviously work in moderation of the increase in interest costs on the liability side.

Given our product mix, as well as the pricing power and this change in ALM, now rapid change in ALM and the duration of asset size that we have been talking about, we are confident to maintain our NIMs + Fees level at, at least 11% despite any increase in weighted average cost.

4) Asset Quality

Last but not the least, the asset quality. Our GS3 now stands at 4.21% from 6.69% last year. NS3 stands at about 1.72% with a PCR of 60%. And as I already said, the Retail NS3 stands at 0.73% with a PCR of close to 79%.

In summary, our established business strengths and proven business models with highest quarterly Retail disbursements, leading to consistent NIMs + Fees, best-in-class Collections, along with a strong Retail Liability franchise resulted in excellent profitability and a stable and well-protected book. Also, the resilient and well-capitalized balance sheet positions us strongly for future growth. I would dare to say that whatever we have been preparing over the last four quarters, whether it is a strong balance sheet, a strong liability franchise, business strengths, Retailisation, we believe this Q3 is, I think, the first quarter in which the profitability is very clearly, directionally coming forward, and we obviously expect to improve it Q-on-Q.

Having spoken about the quarter in detail, let me refer to the pillars of our Lakshya 2026 plans, which are four, which are:

- i) Having a Sustained profit and growth engine
- ii) Demonstratable strength in risk management and collections
- iii) Creating a Fintech@Scale and
- iv) Sustainable future growth through ESG

I've already talked in detail about the first three pillars. So let me talk about the fourth pillar, which is ESG and let me come to the conclusion.

L&T Finance has been one of the pioneers in ESG standards in the financial services industry. A big achievement in Q3 was L&T Finance receiving the CDP score of 'B' level in the recently released CDP score report for Climate Change 2022, which is a significant improvement over the previous score of 'D', received in 2021. The score signifies that the company is taking coordinated actions in climate issues and highlights the steps taken by the company towards sustainable processes and systems. And more importantly, also highlights the way we report that and the seriousness with which we take this. I would also like to highlight that the score is higher than Asia regional average of 'C' and the financial services sector average of 'B-'.

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I would like to also share with you that we continue to work towards carbon neutrality in line with which we have adopted the use of “Green Power” across many branches in Maharashtra, including our Head-office in Kalina, which will help us reduce the carbon emissions.

We also worked on carbon sequestration through Project Prakruti with the initiation of plantation of 50,000 trees and have been recognized with awards like Social and Business Enterprise Responsible Awards (SABERA) in the gender diversity and inclusion category, and UBS Forum Awards in the women empowerment category for our Digital Sakhi Project. ESG continues to be an important driver of our strategy and growth, and we are committed to build and report an ESG-conscious organization.

To summarize, I would like to say, that we have stayed true to our commitments and have been able to deliver consistent performance. The efforts which we put every day are guided by the overarching goal of making L&T Finance a top-notch Retail NBFC. We have laid out a path for launching multiple offerings in the future, which will supplement the strength of our current offerings. Looking at our performance in Q3FY23, I can confidently say that we strive and drive our efforts towards achieving and exceeding the targets of Lakshya 2026, well ahead of time.

With this, I once again extend my good wishes to all of you, apologize for taking around 45 minutes, but I think they were very important things to highlight in my opening comments. May the New Year bring all of you and your loved ones immense happiness, good health and a lot of success. I thank you for a patient hearing, and open the floor for questions. Thank you.

Moderator:

The first question is from the line of Saurabh from JPMorgan

Saurabh Kumar:

Hi Sir, Congratulations. So, this seems to be the clearing quarter for you guys. Just have three questions. What would be your market share now in the Tractors and Two-wheelers? Micro Finance, I think you'll be number 3, but what will be your market share? And are you holding to that top two or three position?

The second is if you can help with the write-off and the slippage in the quarter. So, your Gross Stage 3 has gone up a little bit. I'm just wondering what are those slippages? And the third is, did I hear you right, that you said 90% Retail by March'24 is the internal target, even though the Lakshya target is higher? And if that is the case, then how are you thinking about this excess capital, which will probably be there on your book?

Dinanath Dubhashi:

Let me answer one-by-one. So, the market share in Tractors is approximately 15%. Market share in Two-wheelers will be 11% approximately. In Micro Loans, it depends on how people measure it, but it is around 5.7%. We are number 4 in Micro Loans, not Number 3.

Saurabh Kumar:

And Tractor and Two-wheelers sir, what will be the market share?

Dinanath Dubhashi:

As of December, what was your second question? Sorry, I remember your third question.

Saurabh Kumar:

Sir, Tractors and Two-wheelers, what would be your market position now?

Dinanath Dubhashi:

Number 4, Two-wheeler also.

Saurabh Kumar:

And Tractors?

Dinanath Dubhashi:

Tractors, Number 1, as of December end. But having said that, us and the next competition is a difference of a few 100 tractors. So, we keep having fun every month, measuring it. But it doesn't matter. I mean there are two, three players who are at the top. Especially, the two NBFCs that you know.

Saurabh Kumar:

What will be the write-off and the slippage?

Dinanath Dubhashi:

I'll just answer about this, because I can't give numbers which we have not given. But GS3 increase, I will just explain to you. There is a rapid drop in book. So, the percentages will happen like that. And in fact, you heard me guiding more-and-more on the Retail RoA tree, Retail balance sheet. Because if I guide you on the total number, the better I do in our Wholesale sell-down, some of these numbers in short term will actually look worse. So, I don't want to guide you on the total PAT and I think that's for you to calculate. Because even today, I don't know how fast my Wholesale book will come down quarter-on-quarter. Based on that total RoA, total PAT, total leverage, everything will depend on that. And I can't obviously give very specific numbers for next quarter, because I don't know. I mean, if I knew exactly how much Wholesale I will sell next quarter, I would have sold it this quarter. So that would be imponderable.

And that's where our guidance comes. What we will strive at. I will not like to talk about that specifically as they are internal targets, etc. We now believe that with the one-time provision that we have taken in order to deal with any discounts that the buyer may ask, for illiquidity discount, it can be pretty fast. And yeah, maybe we hope to touch about 90% by the end of the year.

And hence, now to actually take up your other question. In FY24, the calculations will show that the more rapidly we go towards the Lakshya goal of reducing Wholesale and Retailisation, the capital may look excess in this particular year. It may look excess. The Board still has to take a decision whether we will give a special dividend, etc. That is also subject to regulatory approvals. As you know that any specific dividend more than a particular amount in CIC, we'll have to take special approvals, etc.

So that's the guidance on the total leverage. And that is why if you would see through my speech, I talked about the Retail balance sheet, and the Retail P&L. So yes, FY24, maybe, if I rapidly reduce Wholesale to say, 10%, the leverage may be limited in FY24, but then FY25 onwards, the leverage will only go upwards as Retail grows. That is why I tried and guided you without giving the numbers about the Retail growth that we are seeing. So, you would see that all indications are that the CAGR, at least for the first couple of years can be well in excess of 25%. So those are the indicators that I would like to put.

Saurabh Kumar:

And if that were to happen your fiscal 2025 RoA could hit at 2.8-3%, I mean, if assuming, correct?

Dinanath Dubhashi:

RoA, that is Retail RoA? Yeah, we are quite confident of even approaching close to 3% Retail RoA.

Saurabh Kumar:

No, I was talking at the company level, so 90% by March'24?

Dinanath Dubhashi:

Exactly. So, Saurabh, that's why. It is everybody's calculation and guess, how rapidly, I reduce the Wholesale book. Correct? I mean, I don't want to give you all the analysts there excel sheets. And particularly for the reason that even I don't know. So, this is a very funny thing that the metric, which is total profit, will actually go in the opposite direction of how well I do. If I reduce it very rapidly, the upside of the balance sheet in FY25, will be even better. But FY24 leverage will be lower, and FY24 profit coming out of Wholesale will be lower. But the important thing to consider, I would invite all of you to think like that, the Retail growth trending definitely more than 25%. Retail RoA trending to 3%, well before time and most importantly, because of this one-time provision we have taken, which we really wonder whether we will use it totally, but let's see. We don't want to -- this is based on valuations that we have done; we have kept it. But because of that, as I said in my speech, we are very confident that any sell-down in Wholesale will not come and have any splinters or hurt the Retail profitability. And hence, the Retail profitability is very quickly approaching steady state. And I believe that FY25 onwards, when the Retail balance sheet is say, 90% or around 90% of the total balance sheet, the growth we'll be starting to see, clearly.

I think this is as clear an answer that I can give and very frankly, as much I can estimate. So, I will try my hardest to reduce the Wholesale book as much as possible. But unfortunately, what will happen because of that is leverage will be that much lesser. So, we should not be worried about that and look towards maintaining and growing the Retail book profitably for FY24, so that then FY25 growth will catch up.

Moderator:

The next question is from the line of Kunal Shah from ICICI Securities

Kunal Shah:

So firstly, I think last time, our indication was we'll be utilizing this money more towards the macro prudential. And now it seems to be more like a complete markdown, and a fair valuation. So, this is more kind of realized or something which we expect to go through. And compared to that of the macro, the utilization or maybe the write-backs from this could be relatively on the lower side. So how should we look at that change in stance from say macro prudential to a fair valuation?

Dinanath Dubhashi:

I have not indicated macro prudential at any point of time. I had said the word, used the word strengthen the balance sheet. Because we had to also make up our mind as to how we will use it. Let me explain the difference very clearly between macro prudential or any credit provisions and the provisions that we have taken. So today, the whole book is around Rs. 31,000 crores. Even if you calculate SRs, which are outstanding, it is around Rs. 35,000 crores, Rs. 36,000 crores. So that's the total book.

Now when we say that this total book, we will start at resolving, ask rapid prepayments, rapid sell down, etc. Actually, the value, as I said in my speech, when the valuer, when they looked at this overall portfolio, even whatever is the NPA and all that, when they looked at the value, fair value, it came actually quite close to the hold-to-maturity value. But then we felt and we also spoke to the valuer, our auditors, that trying and being very ardent about not passing on any discount, though we actually, the team carries the target of selling things at par value. But we recognize that the more rapidly we sell, perhaps the buyer may need some discounts on certain things, interest rates have also gone up, various things have happened.

And because of that, we have put this illiquidity value. So very clearly, if the book would have remained with us at the same pace or reduced at a normal pace of Rs. 2,000 crores or so per quarter, we don't think that we had to give this illiquidity discount. Because we plan, I mean, I indicated that we hope that we will come to 90%. So, you can do your calculation that how much the Retail growth is likely to be and for that to be 90%, how much the

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Wholesale book will be. I don't want to give out internal numbers, but it is very easy to calculate. It will be based on your projection of our Retail growth and that is how it will come.

But you will see that whatever number you come to will be a very small fraction of today's book. And because we want to achieve that within a short period of 14.5 months, we believe that this will provide us with the cushion to be able to do that. That is how you will have to look. Whether there will be write-backs or things like that, we will know after 14.5 months, I will put it this way.

Kunal Shah:

And if we have to look at it in terms of the maximum markdown...

Dinanath Dubhashi:

Kunal, sorry. On the other side, whether there will be any further hit to the Retail P&L because of this, that we are very-very confident. So, as I always say, management has to hope for the best, we have to be optimistic, but provide for the worst and that is what we have done, that we have provided for a worst-case scenario that we may have to lose Rs. 2,700 crores while selling, which as you would see as a percentage of Rs. 31,000 crores is a very large percentage and that too Rs. 31,000 crores of a good book.

Kunal Shah:

And if we have to look at it in terms of the markdown, so between the Real Estate and Infra, how should we look at it? Because maybe still out of Rs. 31,000-odd crores, Real Estate is at Rs. 7,300, so and Infra is still Rs. 23,000, Rs. 24,000. So, I think Infra would not be so vulnerable to the markdowns compared to that of Real Estate and in terms of the proportion between the two, how could be markdown proportion you would see?

Dinanath Dubhashi:

I don't want to give specific proportion, but generally speaking your conclusion is right.

Kunal Shah:

And secondly, in terms of opex + credit cost, you said 7%-odd?

Dinanath Dubhashi:

That is correct. 7% for Retail. Today, it is around 7.5%-odd and that is how we think it will trend. I will also say why I'm putting this together, right? Because I believe and we firmly believe that especially collection costs and credit costs are very fungible costs. There are times when we have to switch one for the other. And the more we spend on collections, credit cost can be controlled at the very base.

And that is why we would like to see how these two trend. We will try to do better than that, but that's what -- so very simple, as I said, 11.38% precisely is today's NIMs + Fees. How are things going to happen? Costs are going to increase slowly as we go ahead, even though now RBI may not increase it that much. As we re-price our liability, definitely WAC will go up, not rapidly but slowly. That is what will happen. Our product mix, even if it remains same, but probably little bit secured loans will grow. So that's what will happen.

On the other side, however, the tenor of Wholesale will come down and hence, our ability, overall ALM ability to raise shorter term loan, that is say 2 years, 2.5 years overall, vis-a-vis say 5 years will increase in the ALM. So, all this together, we are conservatively saying that NIMs + Fees should be around 11%. You would also see that our fees have also little bit come down this quarter.

I would upfront like to say, that we are also talking to some of our insurance partners about looking at various other arrangements of booking the full potential of fees. We are also, Board passed a resolution to apply as a corporate agent. Till now, we were a master policy holder. We will now be applying for a corporate agent and which would enable us to get the full potential of fees. So, all these things together, we are very confident of a minimum 11% and hence, if we were to target for a 3% RoA, expense + credit cost has to be around 7%. It's just very simple arithmetic is what we are looking towards.

Kunal Shah:

What would have been reason for lower net worth in Q3 compared to that of Q2, particularly on the Retail side, post almost Rs. 400 crores PAT in Retail?

Sachinn Joshi:

Just allocation.

Dinanath Dubhashi:

My CFO will take this question

Sachinn Joshi:

Kunal, this is just allocation between the three businesses. As you would have seen, the provisions come in one entity. The gain is sitting in the holding company. So, it is purely the allocation

Dinanath Dubhashi:

I would say, Kunal, FY24 onwards, you will start seeing proportionality of the book. And that is why Saurabh's question, you take note of my answer, that Retail leverage will actually -- otherwise, what I was there, 3% (RoA) and close to 5x, say, 4.75x debt-equity, I would be comfortably above 15% RoE. But that will not happen because the moment the Wholesale book comes down, the leverage of Retail will also come down. And that will happen over FY24. And hence, the conversion of RoA to RoE and hence that RoE going to high teens will perhaps more happen in FY25. But I would invite you to say the potential of doing that by reaching steady-state RoA is pretty soon.

Kunal Shah:

And one last data point, if you can share Stage 2 for Retail because this...

Dinanath Dubhashi:

You know what, this demand has been there throughout and I would -- I promised you last time that we will soon give it, I would reiterate my promise. We were not wanting to start giving some data in the middle of the year. From the next quarter, next financial onwards, we will give very detailed breakup of our portfolio.

Because now we are -- I used to give out these numbers. Now you know that the new regulations don't allow me to do that, unless I put it in the investor presentation. So, we will start putting it from next FY onwards.

Moderator:

The next question is from the line of Rikin Shah from Credit Suisse.

Rikin Shah:

I had three questions. First one was on the NIMs. So of course, the consolidated NIMs have gone up due to higher utilization. But even if I look at the Retail yields in particular, they have increased 65 basis points sequentially. So, my question is, are there any specific products which are driving higher yields quarter-on-quarter? Is it mainly Micro Finance related or you have been able to take price hikes across the product? That's the question number one.

Question number two is relating to the provisioning pertaining to the Wholesale book. On that particular point, I wanted to understand the provisioning amount that we arrived at, was illiquidity discount the only variable which we used to estimate this number, or were there any other variables and if yes what were they?

And thirdly, just more of a question from an understanding perspective. While I believe that taking this provisioning was completely prudent, given that the Lakshya 2026 required Wholesale rundown to be done over few years. And if the book is indeed performing, wouldn't it have been better that rather than accelerated sell-down, if we could have recovered more amount and pay up for this illiquidity discount? This is particular because the provision

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that we have taken is substantial - 13% of the net worth, could more number have been recovered or we would have run it over 2 years, 2.5 years rather than just next 14 months? That's all from my end sir.

Dinanath Dubhashi:

Excellent question. I will take the last question first. So, in my speech also and in the opening comments also, I said that it is mainly illiquidity, largely, because when the valuation was done based on credit quality, etc, given the provisions we had already made, the valuer didn't think it necessary that the value is very different. So, have we been conservative? I believe perhaps yes. I don't want to make too many comments about that. But yes, I would believe that it will be almost completely illiquidity. That is that to answer your first question.

Second, it's a matter of P&L versus value. And the Board and the management is completely convinced that if you look at valuation of peers, we believe that peers who perhaps have Retail business which may not be of the same quality as ours, get much better value. Finally, our job is to maximize the value for the shareholder and hence, the management as well as the Board believes that the earlier we are recognized as a Retail finance company, the better. And that's the reason. This doesn't mean that we will necessarily take huge losses or anything like that. But we wanted to give very clear strategic direction to this.

Also secondly, what happens that as much as we believe in the portfolio, you know that something happening can give some problem in Wholesale portfolio, Andhra Pradesh, some things here and there and it has always weighed down on investor feelings, perceptions, etc. Clearly, we want to finish this as early as possible and reduce Wholesale to a level where all investors are confident that it is a very small percent of the book now. And also, if at all any further reductions or losses have to be taken, they have been already taken and finished.

The Retail P&L, you can look at as a pure pristine P&L with no fear. Many times, I was told that sometimes we are hit by some event or we get a negative surprise and all those things were said. We want to now ensure that there is no negative surprise coming to the balance sheet at any point of time. This is in colloquial words, it is a dry powder, that we have learned from some analyst only, dry powder that we have created for any such issues coming up in the future. So, that's how you need to take it. It's how the overall P&L will progress vis-a-vis value. We believe and hope that all of you will now give better value to us.

Rikin Shah:

And sir, on yield side?

Dinanath Dubhashi:

Yields. So yes, it is not just Micro Loans. There are three products, we saw very rapid increase in this time. And all are good yielding products; Micro Loans, surely, i.e. Rural Business Finance, Consumer Loans, Farm and Two-wheelers, we saw very-very good increase. So, yields have gone up. As far as passing-on is concerned, I will be frank. Maximum pass on actually has happened in Infra loans and Home Loans (HL), where the yields are so less than we can't afford to absorb. So, we have passed on completely. In the other, Micro Loans, for example, we have stayed at 24% through the entire 225 basis points rise, because we believe that we are adequately priced. So that is how it has moved. Product mix has moved too in Retail, moved to a little bit more high-yielding products, but definitely not necessarily only Micro Loans. We give product mix numbers in detail. So, you can see that.

Rikin Shah:

Yes, that was from the loan book perspective. I wanted to just understand from a yield perspective. But anyway, that answers all my questions.

Moderator:

Thank you. Ladies and gentlemen, this was the last question for today. I would now like to hand the conference over to Mr. Dinanath Dubhashi for closing comments.

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Dinanath Dubhashi:

Thank you. I will only say that let FY23 bring all of us, the country itself, very good luck in many things. We are now seeing, soon we'll have the budget. We'll soon, hopefully, be off major issues, major problems. We look at the economy with hope. We believe that not only through the plans we have, the initiatives we have taken, but also performance that we have shown, we believe that we have earned a much-increased confidence from all of you and very grateful for you for the support you have given and with folded hands, would ask you to continue this support to us and give us the credit that hopefully we deserve. Thank you. Thank you very much.

Moderator:

Thank you. On behalf of L&T Finance Holdings Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.

*Since the transcript has been derived from a voice recording tool, necessary corrections have been made to remove anomalies as well as manifest but inconsequential factual discrepancies, repetitions in Q&A which would have unintentionally crept in, if any