EDELWEISS – INVESTOR DAY 2018

Rashesh Shah: But the way our model has evolved, and these are actual numbers as on FY18, so I think this might just make it easier to understand the financial model we have. The nominal value of the debt we acquired from banks has been Rs. 93,000 crore, so as you know the total stressed assets in India has been about Rs. 1,200,000 crore, so this is almost 10% of that is what we have acquired from the banks, so Rs. 93,000 crore headline value is the debt we acquired. The price at which we acquired was almost about 50 cents to a dollar, so we bought it at about Rs. 46,000 crore, is the AUM. So, when you see our AUM, you will see Rs. 46,000 crore, out of which the capital we put in, because as you know, there is an 8515, earlier it was 595, became 8515, the capital we have deployed is about Rs. 6,300 crore which comes to approximately about 13% of the AUM. So this Rs. 6,300 crore is the cash we have deployed into the business and we basically look at the return we make on our money, on the Rs. 6,300 crore. That Rs. 46,000 crore is important because that is what you get on fee on but ultimately the fee and the interest is on the capital you have deployed because this is like any other NBFC, so this is like a credit book, a home loan book, or an auto loan book of Rs. 6,300 crore capital. On that, we last year made a total income of Rs. 833 crore, which is broadly a yield of about 16% on the average capital deployed. So whatever capital we have deployed, “uspe solah takka is the return banaa,” as we say in simple business jargon that, you know, “kitna chota.” You know, when you buy a car, you say “kitna mileage deti hai?” So, when we ask, internally we are saying whatever capital we have deployed, how much are we earning on that. The answer comes to about 16% is the yield we earn on that and out of that 16%, we pay our interests, we pay our employees, you know we take all the other costs and then we come to what is the profit, so profit was Rs. 192 crores, which was ROA of 3.6% than ROE of 20% for the last year. This year, as you would have seen the first quarter, the results, we have close to 5% ROA and 25% ROE, but this was what last year. So this is the simple model that Rs. 6,300 crore is the book size on which we made income of Rs. 833 crore after paying all the expenses and tax, we made a profit after tax of Rs. 192 crore, that’s as simple like any other NBFC, any other credit business.

The second thing people ask us is what is upside in this because **(inaudible 3:00)** is what is we call the normal business model, the other good thing in ARC we have is there is some upside also because when we recover the money, if you recover higher than what you have bought for, so anything more than Rs. 46,200, you recover, you’ll get a carry, you’ll get an incentive on that and that if you assume average, this is all hypothetical, if you make 10% more on Rs. 46,000 crore, you will get Rs. 4,600 crore and the way this ARC deals are structured, whatever extra you make, you get 20% of that as your incentive. So, on Rs. 46,200, if you get another Rs. 4,600, which is 10% more than what the price at which you bought, it comes to on that you will get a 20% carry, which is about Rs. 920 crores is your incentive, is your carry, and this usually should happen over 4 years. So after paying tax and all, you will get about Rs. 150 crores extra per year if you recover 10% more, you might recover 5% more, you might recover 20% more, you might not recover anything more at all, but if you recover 10% more, this is upside. So the ARC has only two parts – one is the normal credit business which makes about 16% yield for you with all the resultant ROA, ROE on that and you have some upside. If you recover less than that, it doesn’t affect you much because usually the, you know, the feels will adjust, but if you recover more, you get the carry, you get the incentive. And as you have seen with Essar Steel and Binani and all, fortunately, the pricing and all should stay robust, but if you make 10% more, you should expect that and this will spread out because the entire portfolio will not get recovered in 1 year, the portfolio will get recovered 25% every year and if you get average 10%, you should end up making Rs. 150 crores.

And I think this we have spoken about you know what is our differentiation, what gives us the right to win on this business. So one of the most important thing we have always done is we have focused on good asset **(but with ? 5:07)** promoters only because that is where an ARC has the maximum play, good asset and a bad or weak promoter is where the most amount of value can be added by an ARC. Then obviously access to capital because with our, you know, Rs. 50,000 crore balance sheet, Rs. 6500 crore is an easier amount.

We have used relationship with the banks. A lot of our team come from bank, we have people from IDBI, State Bank, ICICI Bank, all of them, so they understand how to partner with banks because ARC is a partnership business with banks, it’s not a adversarial business where they sell and we buy, it is a partnership because we are finding a structured answer to trying to solve the banks problem and also recover money as efficiently as possible.

And obviously, we focus a lot on revival and a lot because if you don’t do revival then the upside is hard to come by, and the revival can be restructuring led revival, it can be actually operating revival, there are all kinds of you know business model change, non-core assets sale, you will do all of that and you will revive, but when you revive is when you get the upside.

We think there will be distressed opportunities in India for a long, long time because India, there is execution risk, so projects will undergo through execution risk, they will struggle and with IDC and the kind of credit regime we are seeing, we think this will be a continuous opportunity of all kinds and we are heavily invested in that, we will continue to focus on this.