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Conference Call Transcript

Edelweiss Capital Limited

Q1FY10 Results

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Corporate Participants

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Mr. Deepak Mittal
CFO

Mr. Shailendra Maru
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Questions and Answers

Moderator: Ladies and gentlemen good morning, good afternoon, good evening and welcome to the Edelweiss' Q1FY10 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 at the end of today's opening remarks. Should you need assistance during this conference please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand over the conference to Mr. Shailendra Maru the Head of Investor Relations at Edelweiss; thank you and over to you Mr. Maru.

Shailendra Maru: Thank you Rochelle. I am Shailendra Maru, Head of Investor Relations for Edelweiss Capital Limited. Good afternoon to all of you and thank you everyone for joining us today as we discuss Edelweiss Capital Limited's unaudited consolidated financial results for the first quarter of the financial year 2010 (April to March).

We have with us Rashesh Shah – Chairman, Edelweiss Group, and Deepak Mittal – the Chief Financial Officer. Following the reading of Safe Harbor Provision, I will first turn the call over to our Chairman, Rashesh, who will deliver his opening remarks whereafter Deepak will take you through an overview of our performance and financial model. Then we will open the lines for Q&A.

The press release and a PowerPoint presentation on our first quarter results are available on our website www.edelcap.com.

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Rashesh: Thank you Shailendra and thank you to all of you for being on this conference call. I guess everyone by now would have had a chance to see the press release and the results. I will just briefly touch upon the key numbers and give a qualitative update on how the quarter has been and how we see the environment.

We have had a profit after tax of about Rs. 58 crores after minority interest on total revenues of Rs. 224 crores for the quarter, which is about 42% growth over the last quarter. It has been largely due to improved volume of market activities. This gives us a quarterly EPS of about Rs. 7.58 on a non-annualized basis. My colleague Deepak Mittal, our CFO, will cover the financial results in more detail in his part of opening remarks.

First let me touch upon broadly the environment, as I am sure all of you are aware, normalcy is coming back. It has been a good quarter from broking revenues point of view, and we are now seeing investment banking and other agency activities also starting to pickup. Sentiments and optimism have come back. The big structural event was the election in this quarter, and as you would have seen, the market volumes have gone up from about Rs. 55,000 to 60,000 crores in the comparable period to Rs. 90,000 crores or so. So we are seeing about 40% growth in the market volumes overall. Though I think there is a lot more options trading this time in the market volume growth than it has been earlier because we are seeing that index options are becoming more an instrument that quite a few institutional investors are using.

Overall the Nifty is positive, FII flows are positive. We are seeing the bond market becoming active and the investments we have made in building the team on that has started showing some results. Overall asset management and insurance companies have been doing well. So the environment looks positive in the first quarter as well as what we can expect in the coming three or four quarters. As far as Edelweiss is concerned, we have been able to grow the business in almost all the businesses we are in.

Our investment banking pipeline is fairly good. We have added a lot of advisory mandates as well as a lot of ECM mandates which will get executed over the next two quarters or so as capital raising and private equity is coming back. On the broking side we clocked average daily volumes of Rs. 4350 crores for this quarter. Overall we have seen that the short term liquidity has been good, interest rates have come down, but since we have quite a few assets on the short end of the market it has not been very good for us from a yield point of view. But overall liquidity being good has been good for the markets.

On the agency business, fee and commission has grown by 67% on a QoQ basis. Our Corporate Bond group has done well. We are now all-India number three in commercial paper and short term placements. On asset management, we have started quite a few schemes in our AMC business and we are planning to launch a couple of funds on the international side of the business also.

Our Capital businesses generally have a low beta because we focus on arbitrage and the secured collateralized loan book. So on the capital side we have seen yields under slight amount of pressure but agency businesses have made up. If you remember the last whole year, where agency businesses were declining quarter on quarter, it was the capital business that stayed put. So our whole strategy of capital businesses and agency businesses has allowed us to maintain some stability. In a bullish market agency businesses do very well while capital businesses do not have a high beta, and in a bad market capital businesses provide stability while agency businesses usually suffer because market activity and volumes go down.

On our Edelweiss strategy we continue to do more of the same. We invested in new businesses in retail and asset management in the last one year. We have about 250 people out of 1200 people currently engaged in retail and asset management. Our corporate bond desk has been scaled up. We have about 35 to 40 people in that business now. We will be launching our retail online broking soon officially though the product in beta stage is up and running. The website is called www.edelweiss.in. We took almost a year to get the product ready and we have about 1000 clients who are now trading on the retail side everyday and we are stepping it up on an everyday basis.

We are now starting to scale up the existing businesses. In the last month the credit book has begun to scale up. We are doing a lot of ESOP financing. We are doing a lot more in secured promoter funding which is coming back.

And broadly to recap, we continue to have the same strategic approach to business that we have had which has four or five basic components. One is synergistic diversification. Even in this quarter if you see the three revenue buckets we have - the fee and commission, the treasury and arbitrage and the interest income, are more less one-third, one-third, one-third. So the synergistic diversification in the business continues. We still do not have a high concentration of any one business overall. While you can argue that all our businesses are overall correlated, they have their own internal cycles.

The second component is control and flexibility which is to maintain high degree of control over the evolution of businesses and also keep flexibility which was highlighted last year. The current year's pre-text margin of 37-38% that we want to average also underscores that.

The organizational build up, the leadership build up and the investments that are happening on the organization side is the third component. We think on a long term basis a diversified, synergistic company is a great opportunity given the way India is going. But to capitalize on that you would need a stronger organization with a leadership team and an organizational structure with systems and processes which allow you to cater to that. And the fourth has been the culture, the culture of ownership, culture of thinking, culture of execution and investing into new businesses on an ongoing basis while keeping an eye on the long term opportunity in building the institution.

So these are the four key strategic approaches that we have had and we continue to focus on that. We obviously continue to keep an eye on risk and liquidity though they have not been as important now compared to what they were in the last year until may be March or April. These were very high upon the agenda in the last six months of the previous year, now they are still there but what is coming back is growth.

Overall we do believe that the indicators are very positive. The pipeline, the client feedback we are getting, all of it gives us a fair amount of confidence that things will improve. From the U-turn that was there from last year's first quarter we saw that activity fell every quarter on quarter. The U-turn has now started to reverse itself and we have the capacity, we have the balance sheet and we have enough of pipeline to be able to capitalize on that. But we do think it will take another two-three quarters. And for us interest rates going up on the short end will be a positive on the yield front as we have quite a bit of our capital in FDs in the banks for the working capital as well as in the arbitrage book which is also correlated with the short term interest rates.

So overall we are positive even if interest rate go up and we will actually try and get some benefit out of that rather than be hurt by that and as long as the activity is good, the capital raising goes on, we are fairly stable. I will now hand over to Deepak to take you through the financials and the operating matrices for the quarter.

Deepak Mittal: Thank you Rashesh and thanks everyone for joining us on this conference call. As you must have already gone through the numbers, I will spend just a little bit of time on that and more time on giving the business overview and outlook. Some of this may overlap with what Rashesh has already covered in his address.

If we look at the last year it was reasonably unprecedented. Various adjectives come to our mind for the last year, but this quarter the market environment has very considerably improved and our performance for the quarter is also reflecting the significant improvement in the environment. More importantly what we have been able to demonstrate in this quarter from an Edelweiss business model perspective is that we are able to scale up our business when the market conditions improve, just as we had shown earlier in the last three or four quarters our ability to ride out the downturn.

Quickly covering the highlights for this quarter, our revenues for this quarter were INR 2,246 million which were up sequentially 22%, and our profit after tax after minority was INR 582 million which was up 42% sequentially. A large part of the growth came from the fee and commission income pool, which includes revenues from broking, investment banking, asset management and wealth management, this increased from INR 401 million in quarter four to INR 671 million in this quarter. This is directly reflective of the environment in the financial markets and more specifically the increased volumes in the secondary market.

The treasury arbitrage and trading income for the quarter was INR 790 million which was also significantly up from INR 508 million for the previous quarter. As we have always said, in this business our constant focus has been on preservation of capital. Of course given the opportunities which presented themselves in the last quarter we did scale up our book in this particular quarter and that is largely what is reflected in terms of increase in the revenues.

The interest income for the quarter has come down from INR 780 million for the previous quarter to INR 682 million this quarter. This income not only includes the interest on the loans which we give out in the collateralized loan book, but it also includes the interest which we get on our working capital which is typically in the form of bank FDs. The loan book has come down to about INR 4.5 billion at the end of the quarter and that partly explains the decrease in the interest income for the quarter and the other impact, as Rashesh elaborated, has been because of the falling interest yields especially more on the short term end because both the loan book and bank deposits to some extent reflect what is the short term end of the curve.

Our total cost for this quarter was INR 1,382 million as compared to INR 1,154 million for the previous quarter. Part of the rise is due to the increase in variable cost which is linked to the business volumes, but a significant number of expense control measures which we had taken in Q3 last year are still accruing benefits to us and that is partly reflected in increase in the pre-tax margins for the quarter.

On the balance sheet size, our total group net worth post minority interest now stands at INR 21.6 billion and the total balance sheet size is now approximately INR 34 billion implying a gearing of just less than 0.5x.

Just to quickly sum up the quarter, it has seen a significant improvement in the business matrix especially on the agency businesses. We are also now seeing an improvement in the loan business. And while we have built a lot of improvement in the businesses, we have continued to invest in new initiatives as well. Rashesh mentioned that we already have 250 people in the two new businesses retail and alternative asset management. We have launched our online broking portal www.edelweiss.in and this we believe places us reasonably well to capture growth not only over the shorter term but more importantly over a longer term.

With this I would like to conclude the call. Once again, thanks for spending your valuable time and we will now open the bridge for questions which all of you may have.

Moderator: Thank you. Ladies and gentlemen, we will now begin the question and answer session. Our first question is from the line of Suresh Ganpathy of Deutsche Bank, please go ahead.

Suresh Ganpathy: Hi, I had a question on your market share. If you look at it QoQ the market volumes are up 65% whereas your average daily volumes are up 55%, so there is again some kind of market-share erosion? And this has been observed for the past five quarters. What is the specific reason, why do you think market share would have decreased this quarter especially given that this quarter the participation in the institutional segment was fairly high? So you being predominantly an institution broker, can you clarify what is the reason for loss in market share?

Rashesh: See our volume is a total volume that is there across agency and treasury businesses that we have. A lot of our arbitrage and treasury volume has come down because with the introduction of STT a lot of high frequency arbitrage strategies have gone away and that is why if you see the STT that we have paid every quarter has been going down. Second, though the market has come back in this quarter we have found that the retail and HNI volumes have picked up a bit faster than the institutional business. And to answer your question on the last five quarters, we are seeing a trend with all the larger brokerage houses where the market share as a percentage of total market traded volume is coming down and our hypothesis on this has been that last year a lot of the smaller or retail brokers increased their intraday scalping, jobbing kind of business especially on the option side, because STT on option side is fairly low. So if you see the index options volume has mushroomed in the market and a large part of index options volume is also intraday jobbing and scalping. So if you look at the volume without the option volume I think the picture would be slightly different for everybody.

Suresh Ganpathy: Okay fine! Thanks for the clarification. What is the cash on books as of first quarter?

Deepak: The total amount of cash balances in the bank would have gone up to INR 16 billion at the end of the quarter.

Rashesh: I must also add that out of INR 16 billion almost about INR 10 billion is usually used by the brokerage and other arms for the working capital because the bank FDs are also given to the exchange for exposure maintenance.

Suresh Ganpathy: Okay fine! Thanks.

Moderator: Thank you Mr. Ganpathy. Our next question is from the line of Aneek Saha of Fidelity Investments, please go ahead.

Aneek Saha: Hi, could you give me a figure as to what your market share would be on the BSE and NSE and how it just increased over the last quarter?

Rashesh: For the last quarter it was about 5.1% which is now about 4.71%. As I said earlier the total volume that we traded was Rs. 4350 crores on an everyday basis. And as we monitor this with others in the industry, we see the same trend in the other larger brokers. We think that as the options volume and the intraday jobbing volume has gone up, most of the larger brokers on a pure traded volume upon market traded volume are coming down a little bit.

Aneek Saha: Thanks.

Moderator: Thank you Mr. Saha. Our next question is from the line of Pankaj Agarwal of Noble Group, please go ahead.

Pankaj Agarwal: Hello sir! What was the size of prop book at the end of this quarter?

Deepak: The prop book fluctuates because as we have spoken about it, it is a residual book depending upon what capital various businesses are using. But if I have to take an estimate for the quarter it will be closer to INR 20 billion at the end of the quarter.

Pankaj Agarwal: Okay, and in terms of debt it seems you have had some Rs. 250 crores more of debt in this quarter, right?

Deepak: Yes, we would have added around that.

Pankaj Agarwal: And where have we deployed it?

Deepak: The way we run the treasury part of the business, the debt is taken at a corporate function level and depending upon the requirements of different businesses it can be channeled to any particular part of the business. So it fluctuates on a daily-weekly basis.

Rashesh: It actually goes up and down and very often when we see opportunities in the last week. A lot of our borrowings are between three days to a month also; so out of the Rs. 1000 to 1200 crores borrowing that you would have in the quarter almost Rs. 600 to 800 crores would be short term borrowings. So it keeps on going up and down based on opportunities either in the arbitrage business or some other liquidity management requirement that we may have.

Pankaj Agarwal: What would be the interest rate on this additional borrowing?

Deepak: It varies from duration to duration. The short term duration rates right now are of course quite low.

Pankaj Agarwal: No, because from what I understand you have a lot of money lying in FDs with banks, so why should you raise more money from the market when you have a lot of liquidity on your balance sheet?

Rashesh: See out of the Rs. 1600 crores cash we have, we use anywhere between Rs. 800-1000 crores for the broking and treasury business on an ongoing basis. On top of that from time to time we need liquidity management; then there are short term opportunities on the corporate bond side also, so we do need short term liquidity. The current borrowing rates are fairly low, if you want to borrow for a week interest rates are about 5-5.5%. So if we can borrow at that rate and even if arbitrage is giving you 10-11%, it is ok. If you need money you do not want to unwind an arbitrage trade but you would just borrow for a week at even 6% rather than incur the cost of unwinding the arbitrage trade. Arbitrage unwinding also has STT implications. There is some asset liability management also some times by us taking advantage of short term rates.

Pankaj Agarwal: And in terms of the financing book since it has gone down by Rs. 100 crores, so is it like you are going to reduce your portfolio or it is just one time thing?

Rashesh: We were still encouraging some of the clients to payback the loans till April or so. It had started from February-March because we were not comfortable taking more and more collateral. In most of the loans we have a clause saying we can ask for top-ups in cash, so we have been insisting on cash top-ups from February-March onwards from a risk management point of view. Just because the market had improved we did not want to go back to companies and say now instead of giving us cash top-up you can again give us stock top-up. So a lot of the cash top-ups came in which got adjusted as a reduction in loan.

Deepak: Just to answer the other question, we do not expect this book to go down any further but we now expect it to inch up a bit.

Pankaj Agarwal: And last question is on IPO financing. Now that a lot of IPOs are coming through, are you planning to enter that financing?

Rashesh: Yes, we have always been in that and in fact we have been doing IPO financing for the few issues that have already happened. We have also been actually scaling up our retail syndication, that is the IPO syndication business and through that also there is a lot of IPO financing demand. For the Mahindra Holidays IPO we were on an all India basis almost third in IPO distribution as per Prime ranking. So we have a fairly large retail IPO distribution business also and we are also doing IPO financing on that. So any liquid collateralized opportunity, ESOP financing, IPO financing, promoter funding, margin funding we are doing all of that.

Pankaj Agarwal: Okay thank you sir.

Moderator: Thank you Mr. Agarwal. Our next question is from the line of Manish Chowdhary of Citigroup, please go ahead.

Manish Chowdhary: Hi, firstly you said that the prop book size is about Rs. 20 billion in this quarter and if I remember right last quarter it was about Rs. 6 to 8 billion. Given the fact that book size itself has more than actually doubled, your revenues from arbitrage have gone up about 50% only. So yields have compressed pretty significantly; any particular reason for that?

Rashesh: Manish, we have observed over the last 7-8 years that there is a large correlation between short term yields and arbitrage, because in a way there is a borrowing element in arbitrage also. If the short term yields are low, we have usually seen that arbitrage yields also come down. Though on the gross basis yields look good but there are a lot of STT and other expenses there, so when you take those direct costs out of it, this quarter, because of the scale down in the financing book as well as arbitrage yields being low, capital businesses have not bounced back as strongly as the agency businesses have, and that historically has been our observation; when there is a sharp rebound in the market the agency comes back first. So having a balanced capital and agencies businesses we have been able to maintain some stability. But you are absolutely right; yields are not expanding in the arbitrage business. Unless the short term yields go up we will see arbitrage not being very high yielding, but after cost you can still make 10-11%. Ideally if yields go up, it can go back to 13-14%.

Manish Chowdhary: So you think that yields are now about 10-11% versus 13-14%?

Rashesh: After all costs, after STT cost, trading cost and everything.

Manish Chowdhary: Right, on gross basis would they have declined much more because just comparing the book size and the revenue size it seems that the yields might have almost come down by 30-40%?

Rashesh: Ideally the yields should be about 13-14%. Nowadays they are about 10 to 11% and that will come to about 30% fall in yield. It is still better than keeping money in the bank or keeping in short term instruments, but we have usually seen that as market rallies get underway, yields go back. We have never seen after cost yield above 18% and we have never seen below 10%, so they fluctuate between 10 to 18% on a quarter to quarter basis.

Manish Chowdhary: These are probably as low as they have gone historically.

Rashesh: Yeah it is just like short term interest rates. 5%, 4.5 to 5% overnight rates even in commercial paper is something we have not seen for a long time. What we are seeing in the environment is a huge amount of short term excess liquidity, but as you go down the ten year curve after one year or two years everything completely dries up. But there is huge amount of overnight money, one-week money, two-week money at a very attractive cost.

Manish Chowdhary: Second question relates to the wholesale financing book. What are the yields that you are getting there? I believe they have come down as well.

Rashesh: In the wholesale finance we have actually maintained yields because we do not want to give loans at 12-13% if we are getting arbitrage yields at 11-12%. So, we are maintaining 15% to 17% yield on the loan book and we have seen an uptick in the book in the last month and in this quarter we will see scale up in that book again.

Manish Chowdhary: And what has been the yield that you have been doing the IPO financing at recently?

Rashesh: The last one Adani Power everybody did it at about 10% to 11% yield.

Manish Chowdhary: But more of IPO financing would be detrimental to the yields that you are getting.

Rashesh: Well, what happens in IPO financing for everybody, it is backed by episodic borrowings, so you borrow at about 6% and you lend it at 10%.

Deepak: The spread pretty much stays constant in IPO financing whether the IPO financiers set the market price or whether the liquid funds set the market price for that.

Rashesh: Hardly anybody uses their core book for IPO financing; you basically borrow on back to back basis for very short duration. So it is just episodic borrowing.

Manish Chowdhary: Okay, sir how have been your EBITDA margins this quarter versus the last quarter, I think they have come down a little bit?

Rashesh: We actually monitor PBT margin more closely than EBITDA because for us interest is a core cost. It is not an ancillary cost. Our PBT margins this quarter is about 38.5%, it was about 37.1% in the last quarter.

Manish Chowdhary: Okay and your net worth and debt numbers?

Deepak: Net worth number post minority is Rs. 21.6 billion and the total balance sheet size was about Rs. 34 billion.

Manish Chowdhary: Right and what was the debt amount?

Shailendra: Manish it was Rs. 10 billion.

Manish Chowdhary: And including minority how much would be the net worth?

Shailendra: Around Rs. 23.85 billion.

Manish Chowdhary: Thanks a lot.

Moderator: Thank you Mr. Chowdhary. Our next question is from the line of Elizabeth John of Keynote Capital, please go ahead.

Elizabeth John: Can you please give the breakup of the fee income? I just wanted to understand how the investment banking and broking has moved up in the quarter?

Rashesh: We do not give the break up on quarterly basis because we treat this as one whole bucket of the agency business of fee and commission. It comprises investment banking, broking, asset management, wealth management, and now retail broking also.

Elizabeth John: Okay, can you just give me some color on investment banking as to how many deals would be there or how is the pipeline?

Rashesh: We have a fairly healthy pipeline. I do not want to make any forward looking statements but we have usually seen that the pipeline for investment banking has generally fluctuated between Rs. 30-40 crores to Rs. 100 crores. It keeps on expanding but not all the deals in the pipeline get closed, some get postponed, some do not close.

Elizabeth John: Okay and you mentioned right now about the retail expansion which is taking place, so is there any figure on the number of outlets that you see or how are you looking toward the expansion?

Rashesh: We are a lot more focused on online and phone based broking rather than branch based broking in the first phase. The online portal is up and running. We have about 40-50 people on the phone side and with this we will have a combination of online and may be after a year or two we will go to branches. Our existing branches are more for customer acquisition rather than servicing them.

Elizabeth John: Thanks.

Moderator: Thank you Ms. Elizabeth. Our next question is from the line of Divyanshi Dayanand of Dawnay Day AV, please go ahead.

Divyanshi: Hi sir, I just wanted to know your broking yields for the quarter.

Deepak: The broking yields have been reasonably constant in the last quarter around 5 and 6 basis points.

Divyanshi: Sir, the MF entry load, would it be impacting your AMC business, any color on that?

Rashesh: Our current strategy on the asset management business is not to scale up AUMs but have better product pipeline up and running. We have 3-4 equity products and we are a lot more dependent on direct marketing, we also sell through distributors. As a new entrant, it will be an advantage for us a year down the line when our products would have established a one year track record because we will not have invested as much in distribution. Increasingly mutual funds will focus on selling directly and we started off by focusing a lot more on that.

Divyanshi: Okay and sir as you said if interest rates go up it would be advantageous for you, so any view on the interest rates in next quarter or so?

Rasshesh: On the short end we are still seeing a lot of excess liquidity but we do not expect that short end interest rates can stay as low as they are now. I do not know how long they will stay here but as the credit growth is happening, as the banks are disbursing money and as the government borrowing program also goes underway, we will see the short end moving up. The yield curve is very steep at present. The shortened is very low and the long end is high. We will see some normalization on that may be in the next couple of months or so.

Divyanshi: Okay, thank you.

Moderator: Thank you Ms. Dayanand. Our next question is from the line of Viraj Gandhi of ICICI Securities, please go ahead.

Viraj Gandhi: Sir, you said that volume of the treasury cum arbitrage is going down, so if you can give me the percentage of your treasury cum arbitrage volumes in your total volume of Rs. 4350 crores and the next question is what is the number of employees by the end of this quarter?

Rasshesh: We do not breakup the total volume with the treasury and…

Viraj Gandhi: Sir, in terms of percentage, before this it was around 50% on either side.

Rasshesh: I would broadly say we have averaged around 40% to 70% of the prop business depending on a day to day basis.

In terms of employees we now have about 1200 employees.

Viraj Gandhi: Okay, thank you.

Moderator: Thank you Mr. Gandhi. Our next question is from the line of Nischint Chawathe of Kotak, please go ahead.

Nischint Chawathe: Hi, Rashesh could you talk about your retail strategy in terms of your having 250 employees in retail and the alternative asset business, and the fact that you have now started really to look at it after quite some time. As you said initially you would just do an online and call in trade and then scale it up, so what is the real thinking behind it and how do you really see this business going forward?

Rasshesh: If we look at the capital market and the total profit pool, our call is that about half is wholesale and half is retail and in wholesale we have now scaled up significantly. There is a lot of incremental scaling up that is going on in Edelweiss but there are no large blocks on the wholesale side, except asset management, that are left untapped.

On the retail side obviously retail broking is a large one; retail financial product distribution is another one. We see retail broking as a large opportunity not just currently, because currently you may argue that the market is slightly over crowded because there are quite a few good quality retail brokers. We expect currently there are not more than 7 to 8 million investors who are trading through all the retail brokerage houses put together, but if you take a 4-5 years view our estimate is that they should become about 25 million over the years. There will be clients who will come through branches and get serviced in the same branch, there will be a call & trade kind of market, there will be an online market, there will be high end intraday active user market which might be more price sensitive, and so on. As the market grows from current 7-8 million to say 25 million over the next 4 to 5 years, we will see a lot more segments developing in the market and all the brokerage houses will eventually be neither one or two segments of those and that is broadly our call. Currently we see a lot of opportunities in research based broking, if you go to the site and see we are largely research based, so a lot of research based hand holding kind of an approach is what we are taking currently, a lot more advisory oriented.

Nischint Chawathe: But, are you looking at more of retail retail segment or the guys who churn a lot or trade a lot and how would you be reaching people given the fact that at the end of the day retail is all about reaching the customers?

Rashesh: There are various market segments, one is HNI market which is more active with more high volume traders, and other is a mass affluent segment. Third is the retail retail which is small volume but more frequent trading. We are currently involved in framing our strategy for these. I would be circumspect to speak a lot more about that at this moment. We just want to roll it out but we are seeing that there are lots of segments in the market.

Nischint Chawathe: Okay, and if it is possible to answer this right now are you looking at doing margin funding or is it something that you will still not be very comfortable with?

Rashesh: Margin funding has always been there on our offering, we just have been a lot more careful and strict in the stocks that we approve and the haircut that we impose. From a risk point of view we have been slightly stricter. We will continue with that.

Nischint Chawathe: Okay, and finally just breakup of the balance sheet on the asset side. You have balance sheet of Rs. 34 billion, on the asset side you have loans of Rs. 4-4.5 billion and Arb book of around Rs. 20 billion and the balance I assume is cash and FD's?

Rashesh: Including working capital, if you look at it broadly, our arbitrage book is about Rs. 2000 crores. The loan book will be about Rs. 500 odd crores, it has been scaled up as we speak. The entire balance sheet is around Rs. 3500 crores, so Rs. 900 crores is other FD's and the working capital in the bank and about Rs. 100 crores will be deposits and corporate assets.

Nischint Chawathe: Okay fine, thank you very much.

Moderator: Thank you. Our next question is from the line of Raj Gandhi of Principal Mutual Fund, please go ahead.

Raj Gandhi: Sir, quite surprised by the way you have ramped up your retail distribution; for Mahindra you are third largest, what channel have you used to collect for this IPO because I suppose you are not too big in retail?

Rashesh: We have been for the last couple of years or so building the retail sub-broker network and if you see the last 5 or 6 IPOs, the small ones or the large ones, we have been fairly prominent as per Prime Database. We are using the same retail sub-broker network. We just have an offering that we think is slightly differentiated which is allowing some of the sub-brokers to use us. We were third on the Mahindra IPO, in Adani we had a market share of around 6.3% in terms of the forms and we are scaling this business also because all this is a part of our broader retail strategy.

Moderator: Thank you, the next question is from the line of Mr. Naga Brahma a Retail Investor, please go ahead.

Naga Brahma: Sir good evening! This is Naga Brahma from Bangalore. We are already Rs. 900 crore company, where do we see the company in let us say three or five years from now? The second question is would you be able to maintain ROE of 35% plus once the situation improves and the third is, sir during the last bull run a lot of financial companies have ventured into whatever areas or field that they could venture like Mutual Fund, Insurance, brokerage, NBFC and so on. So, now that this base rate has come and everybody has settled down, I just wanted to know what is the USP or what new thing is Edelweiss doing that none of our competitors are doing? Sir I want specific answer and not in general terms.

And lastly we have already gone through a very bad phase and there are early signs of recovery happening. Because most of our business depends on the capital market, are there things we have de-risked so that irrespective of the capital market situation, our earnings will be steady?

Rashesh: First of all I would not be able to give a three year or five year projection on a call like this, nor do we do this in any conversation because we do not make forward looking statements. Secondly, on the ROE front, our estimate is that the business model that we follow should allow us a 10% ROE at the bottom of the cycle and may be 20% to 24% at the top of the cycle because our businesses are cyclical. The idea is to look at an ROE across the cycle with 10% at the bottom and 20% to 24% at the top of the cycle and that is what we aim for. I do not know whether we will be able to achieve it or not because that depends on the opportunities in the market. Also what happens with capital market firms, not just us but quite a few others, is the more you can borrow and the more you increase your credit activities or other assets side activities, the more your ROE can improve, but then you have to manage liquidity. With all that, I would say that you should expect ROEs for not only us but for everybody to be in this range only.

Edelweiss' USP as I said earlier, there are four to five things we do - constantly pursuing growth, we are constantly investing in growth, and we are a lot more able to manage our cost as you would have seen in the last year. In the last two quarters, we have 37% to 38% pre-tax margin which in a bad year like last year was not all that easy. So our ability to manage cost, our ability to invest in newer businesses is important.

We have retail broking as one of the gaps in our portfolio. It has been unexplored for us, we are now tapping that also, so hopefully that should also provide some more growth. We have managed growth and we have executed on this. We have been risk conscious and managing risks. All these are our USPs. Unfortunately I can only describe these in general terms. At the end of the day, it does not take anything extraordinary, it just takes some of the more commonsensical basic things that you follow everyday in your life to make something that is differentiated. The way we are managing the volatility in the market is to de-risk the business model through diversification, cost control, a very liquid balance sheet and all this we have shown in the last year.

Naga Brahma: Sir, what you have mentioned is from the Investor's angle as your USP, what is it from the retail-customer angle for those who want to use your services?

Rashesh: With the research that we have done we have found that there is a large demand from people who want advice and research. We have done fairly good work on the institutional side of providing good quality research products and good quality advisory services. Increasingly the Indian retail investors are also going towards that. They want advice on asset allocation, they want advice on stock picking, and there are quite a few gaps that we have seen in the market and we hope to have a strong research advisory based business for them.

Naga Brahma: The last question sir, is there anything through which we will have steady earnings, would that be a possibility?

Rashesh: The fact that we have a large capital base itself provides us some amount of steady earnings though that is not what anybody wants to depend on, but the fact is you are well capitalized. The capital is always a stabilizing factor while agency businesses are more upside capturing factors, so if you have mix of capital and agency, then you have a fairly good balance between two.

Naga Brahma: Okay, thank you very much.

Moderator: Thank you, next follow up question is from the line of Manish Chowdhary of Citigroup, please go ahead.

Manish Chowdhary: You said 1200 employees currently, in the last quarter was it not 1400? So has that employee base comes down?

Rashesh: For the last quarter, it was 1300 Manish. We are still tightening our performance parameters and we do not want to give that up. We started that in December onwards where we started looking at people and productivity. We have very strong KRAs. We have very strong deliverables and we have at a gross level hired about 200 people, but we are basically encouraging a lot more performance based approach. So we expect that to continue as we take some of the cost out in areas which are not delivering as per our expectations.

Manish Chowdhary: Any particular segments in which the employee counts have come down relatively more?

Rashesh: It is across the board which may be 5% here and there in all the business, largely through attrition as well as our encouraging people to look for other opportunities. But we are adding also, we would have hired about 30 people in this month itself at a gross level.

Manish Chowdhary: Ok and one final question, until now the focus as you have also said was in containing risk but now do you think that this is an opportune time probably to take on more leverage especially in terms of financial leverage given the fact that your debt-equity is pretty modest as of now?

Rashesh: Yeah, as I said, and exactly what you understood is, growth is coming back. We want to capitalize on that and step on the accelerator. On a medium-to-long term basis, we have asset management and retail that we have already started allocating resources to and putting in the effort. These will be our medium-to-long-term growth vectors. On the short-term we will scale up existing businesses and on the agency side we have enough capacity still to grow as market volumes grow. So the existing business will provide a short-term growth. We have scaled up our financing book as you will see at the end of second quarter.

Manish Chowdhary: But where do you see more scaling up at least in the next six months, in the capital business or in the agency business?

Rashesh: It will be both. As I said the capital business is somehow linked to the short-term interest rates also, but even that we have been scaling up in the last few weeks. On the agency side we have capacity. On our capital business as I said earlier we will have to wait for at least some interest rate uptick to happen for yields to really improve.

Manish: Thanks you very much.

Moderator: Thank you Mr. Chowdhary, our last question is from the line of Ronak Nagda of Valuequest, please go ahead.

Ronak Nagda: Sir, now that you are going to focus on the retail segment, the advisory segment and the retail segment; what is your aim, what do you believe and what do you want to do for the people?

Rashesh: I think I just answered that question in a couple of other ones and what I would encourage is you can go to the website and see our offering. It is very largely advisory and research based hand holding led kind of an approach.

Ronak Nagda: Thank you sir!

Moderator: Ladies and gentlemen that was the last question. I would now like to hand the conference over to Mr. Shailendra Maru for closing comments, please go ahead sir.

Shailendra Maru: Thank you Rochelle and thank you everyone for joining us on this call. In case you have any further questions, please feel free to contact me or drop me an e-mail at shailendra.maru@edelcap.com. Have a great day ahead. Thank you very much.

Moderator: Thank you Mr. Maru, thank you gentlemen of the management. Ladies and gentlemen on behalf of Edelweiss Capital Limited that concludes this afternoon's conference call. Thank you.