CARE Ratings
Professional Risk Opinion

CARE Ratings Q2FY21 and H1FY21 Investors' Call

Thursday – November 5, 2021 – 3 PM IST

Mradul Mishra – Corporate Communications, CARE Ratings [0:00:01]

Good afternoon ladies and gentlemen. I am Mradul Mishra from the Corporate Communication Team, and on behalf of the company welcome you to our second quarter of FY'21 and H1of FY'21 Earnings Conference Call. We wish to inform you that all participants are in listen-only mode, and there will be a Q&A session once the presentation concludes.

During the Q&A session, you can please click on 'raise your hand' option which will enable me to unmute you for posing your queries. Also, please note that this conference is being recorded. Our team is represented by Mr. Ajay Mahajan, Managing Director and CEO along with other senior management personnel. Now I request Mr. Ajay to take over the proceedings please.

Ajay Mahajan – MD & CEO, CARE Ratings [0:00:47]

Thank you, Mradul. Good evening friends and welcome to CARE Ratings' investor call for the second quarter of FY'21 and H1of FY'21. Due to certain commitments, we were unable to hold this call yesterday but are very keen to interact with you today and share our performance highlights and answer your queries.

As you know, our credit ratings business rests on two pillars, initial ratings based on new business generated and surveillance, which is a kind of annuity business for us or for any rating agency for that matter. The first depends on how the economy behaves and what level of economic activity we are seeing. And the second one is more like an annuity business.

Having said that, there is also a certain level of unpredictability to the surveillance business whenever there are economic downturns. Also, because the same level of debt may or may not be necessary for some of those companies it impacts this piece of business. I think will continue for at least the next two quarters and hopefully will get ironed out thereafter.

An important point I would want to place before you is that we also have to use our analyst resources - and a lot of our time gets utilized in complying with regulatory requirement - to continue to give 'issuer not cooperating' (INC) ratings. A lot of our business hence does not earn revenue but resources are utilized in terms of analyst's, rating heads e, and group heads time.

Now, how has the environment for new ratings been? Although the macroeconomic environment as I just mentioned has been tight this year, it is now beginning to witness improvement, due to unlock measures. It is still in negative territory as evidenced by the growth in credit to manufacturing and services sector, which are the key quick indicators of economic activity.

Growth in credit to manufacturing has been minus 4.5% lower between the April and September period, while to services is minus 0.7% for the same period. Within manufacturing the growth in credit to large industries has declined by 5.1%, while that to MSME has increased largely due to the guarantee support provided by the government.

Further, the industry has surplus capacity with utilization rates still at about 47.3%, as of June it was 47.3%. Fresh investments in the sector are still quite low. The investment rate in the economy is at a very low point of 22% as against a number of 27% plus last year.

Corporate bond issuances have been higher, but short-term issuances in the form of commercial paper have been lower. Most of the issuances in the bond markets are from the financial sector. And the only other exception largely in terms of predominance has been PSUs.

Now, this has been the pattern all through the year. And we have seen additional liquidity facilities set up by RBI through LTROs, TLTROs and so on which has largely made capital accessible for high rated entities and not necessarily across the board. This is a clear phenomenon that we've seen in the last six months reflecting risk aversion, and risks to the NPAs in the banking system.

CPI inflation reigning at 7.3% has not provided space to the RBI to cut any rates furth. The repo rate has been kept unchanged at around 4% levels. But the RBI has indicated an accommodative stance through liquidity infusion.

Now, let me come to our performance which is critical. Let me first talk about our standalone performance. Our operating income increased by7.5% from INR66.43 crores to INR71.40 crores in Q2. Expenditure was down 5.9% from INR31.8 crores to INR29.83 crores. Hence there was an increase of 19.8% in operating profit.

This helped to improve our operating profit margins from 52% to 58%. Operating profit has gone up from INR36.99 crores to INR38 crores t. For the six months, including Q1 performance, total income was INR122 crores as opposed to INR128 crores approximately in the same period last year.

PAT was INR47.93 crores as against INR50.08 crores in the corresponding period last year. So, in many ways Q2 has helped us. Operating profit margin is up from 40% to 43% while net profit margin has been maintained at 39%.

For the Group on a consolidated basis, the results are a total income of INR83.87 crores in the quarter versus INR80.72 crores in the same period of FY'20. PAT moderated from INR36.73 crores to INR35.84 crores, a marginal decline there again due to the tax factor.

For the six months period income was INR130.77 crores versus INR138.45 crores and profit after tax INR45.54 crores. The Board of Directors based on this performance has decided an interim dividend of INR8 per share of INR10 face value share basically.

During the financial year, we have held several webinars on different industries. That is just to give you a flavour of what we have been doing in terms of our outreach to clients. We have held several webinars in different industries for COVID impact and guiding our clients as to what we see across multiple sectors.

There was concerted effort to build the brand with these sessions. The difference this time was the industry webinars had experts from concerned sectors also to share their views. We were also a knowledge partner at CII Financial Market Summit in October, where our knowledge paper was released by the Chairmanof SEBI.

Going forward, as mentioned earlier, we do expect sequential improvement in the economy. And our forecast for the full year is a minus 8.2% growth. There have been some affirmative steps that have been taken by the government. We need to also commend RBI for the steps taken relating to moratorium, and one-time restructuring.

We would be keenly watching all these developments to leverage opportunities that accrue from the same. We are not seeing much momentum in bank lending yet. And for the full year, we expect a growth of about 3% to 4%. Except for SME credit where the guarantee scheme was in place we have not seen pick up in credit books across the spectrum.

We see strong risk aversion even today among banks. With surplus capacity, new manufacturing and private sector are still watching the government moves on capex. We may have to be patient before such investment in infrastructure sector comes in.

Needless to say, we will seek to leverage opportunities that come our way, either in the rating business or through our subsidiaries that have modestly tried to address the outset ratings business as yet. I would like to take some time before I close my comments and move to the question and answers session. I just want to comment on some of the things that we are trying to do.

I have repeatedly said that CARE Ratings is on a firm path of transformation going forward. CARE Ratings has been facing challenging times in the past on both operating and regulatory fronts. In order to alleviate these issues, we have been making several changes in the organization and I would like to highlight two or three of those:

First is, looking inward, we are looking at transforming the corporate culture further. There has been a lot of transformation that has happened in course of the last two - three years by very conscious changes adopted by management and also as advised by the board. And we would want to carry that momentum forward.

Our corporate culture is being changed to focus entirely on building analytical rigor, adherence with all the regulatory compliances, fearlessly expressing our opinions on ratings, with a single minded focus on rebuilding the company's reputation. y.

Our quality of work will be our single biggest focus going forward. The quality of work we do collectively as a team, business originators, or business executors. We can lose business, but we will not lose our reputation. That will be our single biggest focus area.

Admittedly, in the last 2-3 years we have made a lot of changes in processes and policies which we are all are adopting but the best analysis emanates from passion. We are trying to inculcate that passion for analytical rigor across the rank and file of this organization.

And having said this, creating this culture in an organization will take some time and effort. It also requires all my colleagues at the top and middle management levels to fully align with us to be able to implement this effectively.

Second important point is to improve talent density, in terms of the rating business, capabilities. Knowledgeable employees are needed to create sustainable competitive edge.

Ultimately, there is no denying the fact that we are in a knowledge industry. And being in a knowledge industry, we carry so much data analysis and knowledge across the board. We have a very good presence in BFSI infrastructure and manufacturing. We are also adding newer products like structured finance capabilities, and so on.

We want to continue to deliver a high-quality knowledge driven analytics to our clients and that is the focus of CARE. We want to continue to invest more in our talent, as we go ahead. We will not just be looking at external talent here, but also internal talent and all those who are a right fit and can carry this renewed culture forward will be a part of this huge transformative journey.

And the last point and important point is that we have to ring proof ourselves in future. We have unfortunately been a single product company. That is the reality. Now while our focus on ratings will remain core, , we also have to do a lot of work on it in terms of looking at newer opportunities for CARE in some of its subsidiaries.

For instance, we have a couple of subsidiaries that focus on risk solutions. And we also have a subsidiary that focuses on advisory businesses for SMEs. We are trying to put a lot of strategy to work. We are not ready with it today. We will spend the next two quarters in fully understanding and analyzing that and picking sectors or areas where people want to organically and inorganically build certain businesses that are contiguous to the core capability of this company i.e. knowledge driven analytics

So with that, I think I will close my opening remarks. I am very happy to hand it back to Mradul, my colleague, who can then orchestrate the flow of questions. Thank you.

Question-and-Answer Session

Mradul Mishra – Corporate Communications [0:13:15]

Thank you, sir. Dear participants, now we will begin our Q&A session. As I said, please click on raise your hand option. I will take you in the queue and unmute you for posing your query please. Thank you.

Mradul Mishra - Corporate Communications [0:15:02]

We have a query from the line of Mr. Manwardhan.

Q - Manwardhan [0:15:13]

Good afternoon sir, thank you for the opportunity. I joined a little late, so I missed out a part of your presentation. So just wanted to understand this quarter's result. I mean, was that some effect of some revenue moving in from last quarter to this quarter? Or can we assume these numbers to continue through the year going further?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:15:41]

It is a good question Manwardhan. If I got your name, right. I think there is some spillover effect. But I don't think the entire performance of this quarter can actually be explained by a few crores of revenue that may have transferred from Q1 to Q2. And while explaining Q1, we had mentioned that some of the surveillances could not be completed because of the lack of audited financials being available.

To be honest, we have not done any general analysis of this. And if we were to normalize business for Q1 and Q2, you could look at the H1 numbers. , Let me draw your attention to H1 FY'21 where business was is INR122 crores versus INR128 crores on our standalone basis. (I'm purposely skipping the decimal point).

And that is a change of about 5% down over last year. So that normalizes for any implicit business transferred due to certain compulsions on account of numbers not being available, or other reports, annual accounts not being available.

Our objective clearly while stating Q1 numbers was that people want to be as close to last year's number as possible. Having said this, when the GDP degrows minus 8% minus 9%, we have to obviously allow for certain adjustments on the downward side to the ambition (goals) that we stated at the start of the quarter. We want to restate that our ambition is that we want to be as close to last year's performance as possible by the end of the year.

Q - Manwardhan [0:17:26]

Right. Thank you.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:17:30]

Thank you Manwardhan.

Mradul Mishra [0:17:32]

The next query we will take from the line of Mr. Samarth Singh, TPF Capital. Samarth, can you please go ahead?

Q - Samarth Singh - TPF Capital [0:17:52]

Thanks Mradul. Hi, Ajay. Good to finally see some positivity coming in our numbers after a long, long time. So congratulations on that. Two questions, first one is, you have sort of given your long term vision and what you want to do, which is the analytical rigor improvement and hopefully over a period of time, the investment community appreciates that, and therefore we get more business from various companies. That's the long term.

What are you going to be pushing for over the next six months, as far as the company is concerned in terms of getting sales growth up?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:18:36]

Sure. Well, honestly, Samarth I would not be able to give you a simple answer. Within the scope of entire economic activity across multiple sectors and the relationships we have and the potential relationships that we constantly review, it will be an ongoing exercise to improve outreach to clients. It is an ongoing exercise to improve, connect, and continue to originate fresh business.

But we need a little bit of luck as well. This is not just about CARE, this is about rating industry, in general. We rate debt instruments and there is no project capital expenditure in the economy at a point like this and as you know, investment by corporate industrialists at this moment of time is very low.

People are biding this time. They are focusing on cost savings. They are focusing on somehow standing through this crisis, and not necessarily taking courageous risks, in order to make investments. So automatically then, despite our efforts, we will not necessarily see as much return coming our way, as we could in buoyant times.

Having made that disclaimer, it is fair to state that we are working hard to improve our outreach. We are reaching out to financial institutions, and financial sponsors like funds, who play a big role., I assure you that we will leave no stone unturned in the short term to improve our numbers.

Q - Samarth Singh - TPF Capital [0:20:44]

Okay, thanks for that. And my second and last question, the one thing you can control is sort of your capital allocation policy. And I know that various investors have reached out to management multiple times talking about a preference for a buyback versus a dividend. How do we continue to go the dividend route? Could you just help us understand why is it that, we are preferring one way of returning capital versus the other?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:21:14]

Honest answer Samarth to this. Dividend comes out of our ongoing operations. And those decisions are somewhat more routine as compared to a buyback that requires a very comprehensive conversation with the Board. , I have just been here two quarters, it takes a little more time to first put our strategy on the table to be able to say whether the cash we have on balance sheet is likely to fall short, or likely to fall surplus over the plans that we have in terms of building out other businesses.

Like I transparently said that those plans are firmly etched in our minds. We must build, a couple of businesses that provide a longer-term fillip to our revenues in a sustainable format that are aligned to our core competency. But until a comprehensive exercise is done, we need time to be able to address the issue that you raise.

The dividend policy comes directly from our operating sort of performances, and therefore does not require the kind of work that a buyback requires.

Q - Samarth Singh – TPF Capital [0:22:30]

I completely understand that Ajay. I understand that a part of the cash on the balance sheet has to be used for inorganic opportunities. I was in fact just talking about the capital being generated from the operations. I think that should be returned in the form of a buyback as opposed to a dividend.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:22:51]

I have to confess that I have not necessarily spent time in understanding this Samarth. I can tell you that, the next time we meet, we would have thought through this very well.

Q - Samarth Singh - TPF Capital [0:23:04]

Thank you so much. Thanks.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:23:06]

Thank you.

Mradul Mishra [0:23:24]

The next query is from the line Mr. Deepak Poddar. Mr. Deepak, I have unmuted you, can you please unmute and pose your query, please?

Q - Deepak Poddar [0:23:36]

Yes. Hi, thank you very much for the opportunity. So just wanted to understand, now, you did mention that for FY'21 we will try to be as close to last year performance. But basically, as we see last year our EBITDA was close to about INR80 crores and this quarter sir we have done about

INR40 crores. So, are we are being a little conservative when we say that and sustainability of the current performance so, any comments on that?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:24:08]

Well, the fact is that when I talk about numbers, I actually had when I said last year, it was more of top line focus while making that comment as opposed to a bottom line focus. So that is a disclaimer that I should put when I said that. The second point is that frankly, the jury's still out on how Q3 and Q4 will work out.

Q2 clearly has been a very good quarter for us. But the surveillances as they fall through during the quarter plus the initial ratings combined to give a good Q2

It may not be possible to repeat a Q2 performance in every quarter, is what I would say. Also the accounting policy takes in revenues coming from surveillance into that quarter and doesn't necessarily provide for smoothing out the earnings over the next 12 months as some of the other agencies probably follow.

So the point I'm making is by definition, our earnings and our revenues in every quarter will belong to or will emanate from the stock of business we actually put through in that quarter. It has nothing to do. It has very little to do with the kind of work we have done in the previous quarters are in any quarter.

Bulk of our earnings come from the work we do within that quarter. So I hope, I have explained the logic to you. After that, you know, obviously Q3 will possibly correspond more with the Q3 of the previous year, than correspond to Q2 or Q1 of any year.

And therefore unless we change accounting policy, for which we are not ready today, the trends in our business have to be honestly compared on a corresponding quarter basis far more than sequential quarters.

Q - Deepak Poddar [0:26:36]

Yes. Thank you very much.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:26:40]

Thank you Deepak.

Mradul Mishra [0:26:44]

The next query is from the line of Mr. Rohan Sharma from MultiAct. Yes, Mr. Rohan?

Q - Rohan Sharma - MultiAct [0:26:56]

Hi. Yes, thanks for the opportunity. So my question is with respect to the strategy. YOu are suggesting making investments in newer opportunities outside the rating business. What kind of cost or employee strength are we looking at for in these newer businesses?

So currently, we are doing a run rate of around INR28 crores on the employee cost. Where do you see this number going forward maybe, let's say a year from now or two years from now? Thanks.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:27:40]

Okay, Rohan my honest answer to this, like I have been saying, and I have been pretty consistent on this right from the first time I spoke on our call. My message here is that we are not ready with the numbers today to be able to tell you how employee cost will move going forward.

But I can assure you one thing, we will not want to do a business that is just stationary. This means I take the cost today and the returns come three years later. We want to be very focused on making investments that are relatively more productive and EPS accretive. It can't be in the same quarter but should be accretive.

And as we analyze the opportunities, whether organic or inorganic, this will be one of the key metrics that we will keep in mind. We are not approaching this from a perspective of make large investment today and forgetting about when the returns will come even if it could take three years, five years

That could be done in pockets for small investments. For a large part of the investment that we would want to ever make, it will be done on the metrics of payback period, and obviously ROI and also the time that it takes to start generating positive cash flows from that investment.

Q - Rohan Sharma - MultiAct [0:29:09]

Sure, sure. And on the ratings business, what about the ratings business from an employee cost perspective, would we be looking to increase the strength of the employees or considering that the scale of the business has reduced a bit over the last two years, would we be reducing the employee strength? And so what about the cost structure on the rating side of the business?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:29:36]

So, here I would just say that CARE has always been exceedingly cautious on its cost. And this goes back to even times when I was not here. For all the last few years I've seen, it's been a very cost conscious culture in the company which is very good. So I don't really have to change too many things there. We are very careful with every rupee that we spend as a company and I am very happy to share that philosophy at least that prevails at CARE.

Now to answer your question squarely, as opportunities emanate, we may have to bring in some talent from outside and like I said at the outset, there is reasonably good talent internally. And that talent and the external talent will come together and create the right type of mix of manpower

quality that we will have for our future growth. I've also shared with you that there will be some influx of external talent wherever we require.

For instance, in subsidiaries, we already have some talent, but in advisory businesses, we need some higher sort of quality talent from the street, because our focus today is on SME business for which we have very good talent. But on the large corporate, fund management, or any other ambition that we may carry, we will want to bring in influx of good talent.

I can only leave this thought with you that we will be very cost conscious, but not at the cost of dropping quality. Our focus is quality, quality in everything we do. Whether it is SME advisory, whether it is large corporates', whether it's global funds, if we want to open up some opportunity there in advising, or it is any other business, we'll focus on quality. And we will also focus on payback and return on investment.

We will be as judicious with the company resources as we are with our own resources. That is an assurance. Lastly, I want to make one point, that technology will help us in managing cost. In the past, what used to happen was that if you got 100 more credits, we would want to hire 100 more, or 10 more or five more analysts.

Now here, while that equation may not immediately help, but will help over a period of time, as we focus more on internal workflow technologies as also artificial intelligence (AI) and machine learning technologies, which we are very seriously working on. I'm very happy to announce we have hired a very senior person in our technology division. He has joined as the Chief Information & Technology Officer recently, apart from the other senior gentleman, Umesh Ikhe, who runs our CRSPL business.

We are bringing in a very selectively quality talent that will help us, completely make what should I say live progress from a being an average technology company to a cutting edge technology company. In full force it might take two years, or maybe three years to happen. But when it starts to happen from today, even on a piecemeal basis, it will impact our productivity quite substantially.

And so unless absolutely necessary I actually expect to make do with the same people that we have and to use the senior talent to improve their bandwidth, give them more opportunity of growth internally in the company, rather than keep hiring more and more people which then increases the fixed cost and operating leverage of the company. Which in turn also creates problems should we go through a downturn like we did in the last two or three years.

I hope I've comprehensively answered your question.

Q - Rohan Sharma - MultiAct [0:33:17]

Yes, only one last thing. So on the industry benchmarking exercise that we had started, so where are we on that? Is that exercise complete or still there is some possible increase in employee cost on that front?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:33:34]

It is a good question. There are some parts of the company which we are obviously going through microscopically, that may need some more revisions. I can tell you this Rohan that it is not possible to completely benchmark yourself to market on a single day. I have worked for companies that have had far higher level of resources, and even those companies struggle to be able to correct accumulations of such sort of dislocations over four or five years or even longer periods in one particular year.

But the message is very simple. If you pay peanuts, you get monkeys. So we will not pay peanuts, we will make sure the quality of our people goes up. But we might see, on the aggregate, the numbers may not bloat because we will be very conscious of the quality of talent we hire. And that if the quality of talent we hire can actually do as much work as two or three average people, or below average people do then necessarily cost would not bloat.

So my simple point is productivity and quality, are the two mantras for CARE going forward.

Q - Rohan Sharma - MultiAct [0:34:45]

Great, thanks. Thanks.

Mradul Mishra [0:34:51]

The next query is from the line of Mr. Akshay Jograni from White Oak India.

Q - Akshay Jogani - White Oak India [0:35:04]

Excellent. Thank you. Thank you Ajay for taking the time. I had a data question really, but of the total revenue that has come for the quarter, how much is attributed to new business? I mean, just one way to get a sense of what is the new business momentum like versus less historically?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:35:25]

The new business, the way we track is actually a bit mishmash, because there is initial revenue coming from new business, then there are surveillance revenues that come from annuity business. But within surveillance, we get a lot of enhancements from time to time, and some drops as well as debt extinguishes with time. For instance, a five year amortizing bond will have an average life of 2.5 years, while I will have to do surveillances for five years.

So, it becomes very challenging to separate the two. Last time, I had conjectured a headline split of somewhere between 25% 30% in a very good year to 20% in a weak year, but I think I would probably stay with a very broad guidance of that nature. It is very hard because we actually don't do this level of split, because of the complications I just mentioned.

Q - Akshay Jogani - White Oak India [0:36:21]

Sure, that is something I appreciate. However, from your point of view, if you had to, you would be essentially looking at the performance of the team, right? And you would want to look at what was the effort to outcome, right. So I mean, internally, at least, there must be something that you would want to look at as a lot of effort would go into new relative to o surveillance from a sales point of view. Right. So what do you look at then?

A - Ajay Mahajan - MD & CEO, CARE Ratings **[**0:36:50]

Clearly like I said to you, we have our own detailed MIS. I'm corroborating what you said. Our Executive Director Mehul Pandya and his team, and I are engaged very, often, and we look at the numbers. The MIS flows quite smoothly, literally on a day-to-day basis. We are able to actually track what is going on. So rest assured that internally, we are totally focused on the key metrics of our businesses and, stand committed to continue to improve them.

Q - Akshay Jogani - White Oak India [0:37:29]

Sure. And as an extension of that I mean, is it fair to assume that last say Q3 and Q4 of FY'20, it was a bad year, that was bad sort of a period, right? So again, 20 would be new, and 80 would be old. Assuming that there is a slight sort of run over of debt, you would get, say, 60% 70% of the revenue you should be getting from those two quarters at least. Is that a fair assumption to make?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:38:02]

It is hard. Like I said to you, in general, I would go with your assumption. The trouble is that in our cases, I'll have to look at the quarterly stock of the business that falls into surveillance basket for that quarter to be able to then suggest your weighted average life of remaining debt in those corresponding quarters to be able to make that assessment properly for you.

So unfortunately, that level of analysis I do not have today or frankly we do this one time at the start of the year just to get a broad sense. After that, it is very hard to track it on an individual case by case basis. And I think if we do this on an average portfolio basis, it is helpful enough, so we really don't extend it to an individual account basis to that extent. I'm sure the business development team has its own analysis would be doing this.

So it is hard for me to confirm to you whether that number is 70 or 80, or 60. But let me tell you this, In the market place we are obviously going to be extraordinarily competitive, in terms of not letting to go off any business because we are a company that will act with renewed vigor. We are focused on analytical rigor and quality. Our business development team is also fairly smart to be able to grab opportunities in the marketplace.

So I can give you a high level philosophical comment that we will not let the opportunity go

Q - Akshay Jogani - White Oak India [0:39:38]

Yeah, sure, sure. No, that's very helpful. How is pricing evolving given that the market breadth is worsened in terms of I mean. , I would love to understand do you see market breadth or number

of participants raising capital, having worsening over the last few months. And as a result, if that is true, has the pricing worsen because of that?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:40:01]

It is in general, I think, on pricing. , I will just say this to you that in India, in a very light hearted manner, your fee based businesses have always competed for a fair price. It is very hard to get fair pricing in India in general. And that's my high level comment, I will not go more into this.

But I can tell you that pricing comes when people see a quality. Pricing comes when people see effort. When people see seminars, knowledge, our engagement or even , when somebody picks up the phone and calls our analyst and gets a quality input, pricing will come. I am quite confident that pricing will come as long as we deliver good quality. And my team is committed to that. I am committed to that. So that is my comment on pricing.

Now, the other point you mentioned is about concentration of debt and whether this is broad based or not. In my opening remarks I said this, there is concentrated corporate capital raising activity at the creme de la creme of the Indian corporate base.

The large keep getting access, the small and medium don't get access very simplistically, because they don't necessarily have the ratings and the balance sheet wherewithal in risk averse markets to be able to be seen to be good enough for investor’s capital. So that is the reality. We have seen more concentrated play of LTRO, TLTROs.

They have seen concentrated activity at the absolute top. But the medium sized companies have actually de-leveraged through this process and will continue to de-leverage before economic activity picks a strong momentum. We have also seen bank loan ratings as being fairly steady.

We have seen capital market activity reduced in the short term as well. Commercial paper volumes have dropped through this period, whereas long term bonds have improved for the reasons I just mentioned. A lot of capital raising is happening in the banking, financial services space, housing finance companies, so more secure businesses that have seen strong connection efficiencies.

But other than that, we haven't seen a broad-based leveraging increase in the system. We have to chip away and keep grabbing opportunities that come our way sporadically and through active business development engagement with clients. Those specific opportunities, I can tell you coming from capital expansion or projects purposes.

Q - Akshay Jogani - White Oak India [0:42:53]

Sure, sure. That is very helpful. And good luck for the coming years. Thank you

A - Ajay Mahajan - MD & CEO, CARE Ratings **[**0:42:58]

Thank you Akshay.

Mradul Mishra [0:43:01]

The next query is from the line of Ms Ritika Dua from Elara Capital. Yeah Ritika, you can unmute and please go ahead with the query.

Q - Ritika Dua - Elara Capital [0:43:41]

Okay. thank you for the opportunity. Sir, because rating business it's difficult to see on a quarter on quarter basis, and I understand that, but can you confirm a trend which we are seeing, though we don't have access to a lot of databases, but then whatever limited we have? We think that to some extent your market share has improved in first half.

Could you confirm that trend sir? And if it is, then in which segments have you seen largely improvement in the market share? Maybe if you could break that up in the bond segment, maybe by rating categories, or whichever way is possible?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:44:28]

Ritika, I am unfortunately not prepared for this question. Because market share analysis requires obviously, numbers from other rating agencies, a lot of other peers do not have this information in the public space. I mean, you as a senior analyst in the business will have more access to their numbers than I have, to be honest.

At this moment, I can't answer this question. But like I said, the performance that we have shown in quarter two is coming from both a combination of the initial ratings business and surveillance. We are definitely working very hard to build our share in the capital markets business.

We believe that is a segment we cannot ignore. In fact, that segment should take as much attention of ours as bank loan segment does. We do not differentiate between the two, but their regulatory landscapes for both the businesses are somewhat different.

Going forward, our emphasis will be to continue to work hard on both the segments, regardless of whatever sort of market share we had in the bank loans, we will want to continue to focus a lot on capital markets, not just on vanilla issuances, we also want to focus on more structured business going forward. We want to be at least a serious contender to activities in capital markets like REITs, INVITS and so on so forth.

We are creating some dedicated internal efforts in that direction. And we believe that these are the long term product capabilities that rating agencies like ours must build to stay absolutely competitive in the marketplace and really be an authority on some of these subjects going forward. But for percentage wise, I will have to revert to you after some more internal analysis.

Q - Ritika Dua - Elara Capital [0:46:38]

No problem sir. Sir, I wish you the best for the journey. Just one more question. So in your press release, you mentioned that there would be some expenditure which would occur from the second third quarter -- from the third quarter onwards. Could you guide a bit on that?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:46:53]

Yes. So as you are possibly aware, there has been an approval obtained from investors in the AGM, ratified by the AGM for a 10 lakh stock options towards employees. Some of them are to me, some of them are to the employees and, these stock options will be granted or have been granted, let's say partly granted, partly will be granted in the second half of this year.

Because they will be granted in the second half of this year, there was no way for us to account for the ESOP related expenditure for the full year or reflect that in the first half in any way. So the comment is limited to this, that the second half will see an element of ESOP expenditure, which is missing in H1 completely. And therefore, in a way, this slightly betters the expenditure position for first half versus the second half.

Q - Ritika Dua - Elara Capital [0:47:48]

Sure sir, that's helpful sir. Sir all the best. Thank you.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:47:51]

Thank you very much.

Mradul Mishra [0:47:56]

The next query is from the line of Mr. Nitesh Jain from Aditya Birla Cap.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:48:03]

Hi Nitesh.

Q - Nitesh Jain - Aditya Birla Cap [0:48:11]

Hi, Ajay. How are you? I mean, good to hear from you once again.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:48:14]

Very well, Nitesh. Happy to take a question from you.

Q - Nitesh Jain - Aditya Birla Cap [0:48:21]

Yes. So I have a couple of small questions. Number one is on the business franchise of CARE Ratings. In the last two years of turbulent period, be it right from ILFS crisis and then the company

had a interim CEO, and then for some times directionless type of situation. Has the fee paying customer base of CARE Rating got eroded during this period? Or was it intact?

I mean, it's a very simple thing to for example, if you had 100X number of fee paying customers say when everything was fine. Are they today same 100 or are they 90 or are they 105 or 10? How is it?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:49:10]

Right, so Nitesh, it is a very good question. I had asked for this information from my colleagues and they very happily provided to me, but not exactly in the way that you have asked this question. So I will answer this in my way right now and perhaps come back to you comprehensively later if I'm in a position actually to share details.

But, let me answer it in my way. I think in the last 2-3 years, a lot of damage was essentially done in the NBFC space. And in the NBFC or BFSI let's call it in general, whether it's an ILFS that we talked about, or we talk about DHFL, a large part of our problems emanated in roughly that space.

And therefore, there was an immediate loss registered of income in the pursuant couple of years on surveillance incomes arising from the loss of those clients. Because those clients didn't need any more money to raise, they were not operating businesses anymore, in many ways. So at least parts of those companies were not operating businesses.

The point is that there is obviously a certain level of permanent damage to income that some of that sector players cost to us. That is something I can share with you. But other than that, I think the business development and the rating teams internally have done a fantastic job of holding the franchise together.

I am not now getting into an Excel spreadsheet, where we say 100 versus 95 or 100 versus 105. But effectively, barring the damage limited to a few high profile issues that we may have faced through that period, by and large, our teams have done a fabulous job of holding on to the franchise. And that gives us a rock solid opportunity to build upon that further, rather than to first sort of fill the pit with what we lost, so to say.

So honest answer is that we did not have much damage to the franchise, thanks to our clients who stood by us and thanks to our own teams who work very hard to stay engaged.

Q - Nitesh Jain - Aditya Birla Cap [0:51:29]

Okay, so basically, my question was pertaining to the clients which are still there, I mean, not those four, five specific names, which even the CARE could not do anything about it. But other than that, by and large, you are saying the customer fee paying customer base is quite intense, right?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:51:50]

Absolutely, absolutely. Other than those areas where we have consciously decided. Now I can't give you every single bit of detail of my strategy.

Q - Nitesh Jain - Aditya Birla Cap [0:51:59]

That's not required also, no problem.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:52:00]

Yes, that is not required Nitesh. What I can share with you is that in certain areas where pricing is too low, and we believe that we don't get compensated in those areas, which could be the lower end of the SME segment, which does not pay for my cost, then that is a very conscious, happy exit situation from our perspective.

Q - Nitesh Jain - Aditya Birla Cap [0:52:26]

All right, wonderful. Thank you very much and all the best.

Mradul Mishra [0:53:33]

Yeah, Mr. Parthiv, please go ahead.

Q – Parthiv – NVS Wealth Managers [0:53:40]

Sir almost all my questions have been answered. I just had a small question. Just wanted to know, by when can we touch our 2018 top line and profitability with all the initiatives taken by the company?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:53:58]

Sir, only if life was so predictable wouldn't it be so easy, then? Obviously, our intent is to catch up on those numbers fast enough. We also have to understand and appreciate that five years ago, there were probably two less rating agencies in this business.

So the rating revenues have obviously got split. The size of the pie is not growing as much as the competition in the sector has grown. Having said all of that, we will want to work very hard. Like I mentioned, we will want to work very hard on our quality, outreach, new product capability, rating revenue businesses mainly, but also on our non-rating revenues to augment and derisk the ratings business in difficult years.

That is our objective and we are working on each of theme in a very methodical focused manner, under the broad guidance of the Board. So my honest answer to you it is hard to predict when I'll get back to 2018 numbers. There was a big hole that got created because of the NBFC issues that we just talked about and those are large fee paying clients.

The NBFCs in those times were leveraging much more than they leverage today. The ALM regulations and compliance conditions in 2018 were very different from what they are today so all I can say to you is that, we will definitely target to get back to the maximum revenue that CARE has posted in the past as the first milestone that we should focus on internally.

Q - Parthiv - NVS Wealth Managers [0:55:47]

Okay, thank you. Thank you so much, and best of luck for the upcoming quarters.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:55:52]

Thank you very much.

Mradul Mishra [0:55:56]

Thank you. As we are short of time, I'll take the last question for the day. This will be from the line of Mr. Ayaz Motiwala from Nivalis.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:56:12]

Hi. Ayaz.

Q - Ayaz Motiwala - Nivalis [0:56:35]

Hi, Ajay. Thank you for taking my question and this opportunity before the close of the call. So, one question sort of related to the post ILFS NBFC situation that you talked about in fairly good detail was the changing landscape in the financial sector, business and your sort of presence in those clients.

So you've talked about the big getting bigger and taking more share. In terms of CARE's positioning, it looked like it was focused on the emerging corporates' and the mid market. So do you face that challenge as you go back to your reach out program to grow your business? So that was the question on your own business.

And if you could throw some light in the context to the development of the debt market which is going on and this listing of papers across stock exchanges, do you see that as a welcome positive development, something what we've been waiting as observers and investors for the last 10, 15, 20 years?

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:57:46]

Yes, so there are two parts to your question. The first one I would say is that the focus of our company through the bank loan ratings business specifically may have been more emerging corporates when I wasn't here.

But we have also had very large accounts in this company, and we continue to do a lot of business with the biggest corporate house in financial services. So I'm saying that statement is not necessarily factually correct, that we are not in such corporate business.

But yes, there is always room for growth. So when you asked me this question, it only encourages me and motivates me to do more in that segment.. I hope I answered your question.

Q - Ayaz Motiwala - Nivalis [0:58:46]

Sure.

A - Ajay Mahajan - MD & CEO, CARE Ratings [0:58:47]

And the second part -- the second part of your question is more in a lighter vein I'll say that, I joined banking industry in 1990. And I left in Jan 2020, all 30 years, we have been talking about corporate bond development in this country. So that is a factual position. Maybe a few years left or when I joined in a few years, right we will keep talking about that.

But in all fairness, this capital markets businesses are not easy for people to fathom. Only private capital and collective capital through solid investment management skills like mutual funds understand the mark-to-market implications, the lack of liquidity implications through difficult times. And others would, even if they are allowed to participate will create some liquidity to start with, but will press the panic button, the moment the MTM starts hitting them.

So it's not a business for everybody. It is a business where you really need to understand credit very deeply. And I think whenever we have in this country, tried to extend using bank loan ratings or bank loan business as an extension to capital markets, we have failed miserably simply because we have not necessarily have the right pockets of investors focused on those segments. There has to be a high risk capital game.

If A rated papers in India would create a trade at 8%, then where is the cushion for mark-to-market and where is the cushion for absorbing any fluctuations. And banks also started to be big players in that business, but eventually realized that the capital at risk is far, far more through MTM fluctuations to be absorbed through P&L.

As compared to accrual loans, which could even accrue at 7% but can hide behind CASA and other deposit sort of cost of funds essentially, obfuscates a lot rather than reveals a lot in my own way, I would say that. So the long and short of my answer is, that capital markets and the depth of corporate bonds is a very wide subject.

It requires a supra-regulatory approach to understand how multiple asset investor classes can be built into the domain of capital market products who understand mark-to-market implications, who understand liquidity implications, who understand ALM implications of the underlying issuers and obviously understand credit very deeply.

It will take a little time. Until that is done, until the frameworks are built the appropriate way, I would think we will still play on the fringe and when interest rates are very bullish, economy's doing well, you will see extensions of some triple B pluses also raising some money at 11% 12%. But the day one guy chickens out at 18%, the next price will be 30% bond yield.

So that doesn't work in anyone's favor. I've given you a philosophical answer. We can debate this separately another time if you like.

Q - Ayaz Motiwala - Nivalis [1:01:50]

Sure.

A - Ajay Mahajan - MD & CEO, CARE Ratings [1:01:51]

But this requires a lot of work, concerted work from multiple investors and from multiple regulators coming under one umbrella with one single minded focus as to how to build capital markets and which is so important also to derisk the banking books actually.

I remember a few years ago, there was a circular from Reserve Bank of India, saying that more and more incremental debt on those companies that already have access to INR25,000 crores or more of collective debt from the banking system has to come from capital markets. I don't know what happened to that circular thereafter.

I lost touch with it a little bit. Because, if that were to be implemented, then the fact is that company regardless of its rating has to raise or force incremental liabilities only through the capital markets route. Now, has that happened, not happened? What happened to it? COVID has obviously upset the applecart but, hopefully when things come back and normalcy is restored, this is a very important subject that requires discussion.

Because ultimately, resources in this country will always be somewhat limited being an emerging market, government running large fiscal deficits, and therefore access to capital markets, which also allows foreign institutional investors to come in a very big way, is the only answer to the collective capital requirement of the corporate and institutional sectors in India.

Q - Ayaz Motiwala - Nivalis [1:03:13]

Sure, that's very, very helpful Ajay. And I would take the chance to have this offline chat as you suggest. I will just leave the remark on this, in the context of our call and the time and the last question, but I have one bookkeeping question, but just that we have had these fits and starts to it, the recent Templeton episode may be the detractor but the REIT and the INVIT norms focused on infrastructure may be the positive for capital market, lead fundraising instruments that you talked about.

So we remain hopeful and hope that CARE has got itself completely sorted out with talent and people that when this wave were to come in, and that may last for 10, 15 years that CARE is right

at the crest of that. Sir the question that I have on bookkeeping was on the ESOP which you partly touched upon, and the accounting related to that.

So earlier, you were -- the company was taking some INR10 crores INR12 crores of ESOP charge. And you said that partly has been accounted for but we don't know the pricing etcetera for this round. So if you can throw a composite light on that aspect of costs on ESOP and accounting, that'll be very helpful before we close the call, please?

A - Ajay Mahajan - MD & CEO, CARE Ratings [1:04:41]

With my limited understanding on the subject for now, and we can come back later, my understanding is that as the ESOP's are granted, there is a value, obviously to the inbuilt option that is given to the employee and that option needs to be priced.

And a cost of that option needs to be taken into the books. Right.

Q - Ayaz Motiwala - Nivalis [1:05:07]

That’s correct sir.

A - Ajay Mahajan - MD & CEO, CARE Ratings [1:05:08]

Now, so the value the strike price of the option is important, the time to vesting is important. And that goes into the formula of calculating on the amount of costs that the financials of the company has to bear. The simple point I was making was that since the grant will come in the second half of the year, not as of 30th September was the grant done, there will be obviously a higher cost to ESOPs as compared to zero cost to ESOPs that reflected in the first half.

Q - Ayaz Motiwala - Nivalis [1:05:42]

So no, no issuance has taken place till 30th September, meaning no strike price has been decided.

A - Ajay Mahajan - MD & CEO, CARE Ratings [1:05:48]

Yes, no issuance has taken place till 30th September. That's correct.

Q - Ayaz Motiwala - Nivalis [1:05:50]

Okay. Okay. So from what we see the numbers there is no -- there is currently no charge on account of ESOP on a prorated basis because there isn’t clearly a strike price number and a time to it?

A - Ajay Mahajan - MD & CEO, CARE Ratings [1:06:05]

Absolutely.

Q - Ayaz Motiwala - Nivalis [1:06:09]

Great. I will not take over liberties on that really appreciate your time Ajay and wishing your team a Happy Diwali and all the very best for as you sort of, as you use the word rebuild this company and take it to higher levels, then it's past glorious. Well, thank you very much.

Ajay Mahajan - MD & CEO, CARE Ratings [1:06:25]

Thank you very much Ayaz. I really appreciate your comments. And that also, I will take the opportunity as well thank you Ayaz to wish you and all other listeners and all investors, everybody who's on the call here a very Happy Diwali, Season's Greetings, and we'll continue to meet you as often as we can. Thank you very much.

Mradul Mishra [1:06:49]

That was the last question taken up for the day. Ajay sir, would you like to give some closing remarks.

Ajay Mahajan - MD & CEO, CARE Ratings [1:06:56]

Well, Mradul nothing really, I think we have gone through my initial remarks, have gone through the Q&A, I will only say to everybody that we are a very concerted team at the top totally focused on performance and quality. We are not promoters of the company. We are management, we have been brought in to make certain changes to transform this company to a higher level of performance, both operating performance, higher level of market benchmarking, higher level of quality in what we do. And I want to assure all the investors that we remain steadfastly focused on these objectives. Thank you.

Mradul Mishra [1:07:40]

Thank you, sir. With this I am closing the call. Thanks all and Happy Diwali.

Ajay Mahajan - MD & CEO, CARE Ratings [1:07:47]

Thanks all, Happy Diwali.