"HDFC Asset Management Company Q4 FY2021 & Full Financial Year 2021 Earnings Conference Call"

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MANAGEMENT: MR. NAVNEET MUNOT -- MANAGING DIRECTOR & CHIEF EXECUTIVE OFFICER, HDFC AMC LIMITED
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Moderator: Ladies and gentlemen, good day and welcome to the Q4FY'21 and Full Financial Year '21 Earnings Conference Call of HDFC Asset Management Company Limited. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

From the management team, we have Mr. Navneet Munot – M.D. and CEO; Mr. Piyush Surana – Chief Financial Officer; Mr. Simal Kanuga – Chief Investor Relations Officer.

I now hand the conference call over to Mr. Simal Kanuga, who will give a brief, following which we will proceed with the Q&A Session. Thank you and over to you sir.

Simal Kanuga: Thanks, Margaret. Good evening, everyone and thank you for getting on to this call. The Presentation has been uploaded on our website as well as that of exchanges.

As usual, a quick update on the industry and we'll then follow it up with some specifics on our company. Navneet, Piyush and I are available for taking questions thereafter.

Firstly, on "Equity Oriented Flows." For the quarter that went by, industry saw net outflows of Rs. 84 billion. We would like to break this number into Jan, Feb and March; Industry witnessed outflows of Rs. 149 billion in Jan, followed by Rs. 59 billion in Feb, summing up to outflows of Rs. 208 billion in the first two months. We saw a directional change in March where industry saw net inflow of Rs. 124 billion. Debt funds saw outflow of Rs. 410 billion in the quarter ended March '21. Liquid funds witnessed outflows of Rs. 422 billion. For the full financial year, debt funds saw inflows of Rs. 2,199 billion while liquid funds had outflows of Rs. 240 billion. Individual folios for the industry continue to rise and is now at 97.3 million. B-30 AUM is constant at 16% of the industry AUM.

One data point that we would like to draw your attention to, in regards to the B-30 AUM is B-30 equity AUM as a percentage of total B-30 AUM stands at 66%, that is Rs. 3.4 trillion of the total of Rs. 5.2 trillion. SIP flows topped at Rs. 91.82 billion. We would request you to look at flows for each of the three months for the quarter; Rs. 80.23 billion for Jan; Rs. 75.28 billion for Feb and Rs. 91.82 billion for March. If you add up all of these, it comes to Rs. 247.33 billion, which is approximately Rs. 82.44 billion per month. There might have been some spillovers which would give a different picture if you looked at data for a particular month.

Our quarterly average assets under management for the quarter ended March '21 was Rs. 4,156 billion, spread across 5.3 million unique customers, 9 million live accounts, serviced through 227 branches. Despite the kind of the environment, we have lived through in financial year 2021, we opened six new branches and our total employee strength increased by 60. Our total employee strength now stands at 1,254. We closed the year with an AUM of Rs. 3,955 billion, a growth of 24% over March 2020. On QAAUM basis, we saw a growth of 12% for the quarter ended March '21 as against that of March '20. In terms of overall AUM, our market share stood at 12.9% on QAAUM basis and 12.6% on closing AUM basis. If one excludes ETF, our market share stands at 14.1% in QAAUM and 13.8% on closing AUM. Our rationale for presenting market share excluding ETF is as you are aware that ETF AUM has over 80% of AUM from two asset management companies, plus government disinvestment program/PSU debt ETF.

In terms of actively managed equity-oriented AUM, our market share stands at 13.3% on QAAUM basis and 12.9% on closing AUM basis. There have been questions that we have received in past on our performance. Though too short a period to call, we have seen a material improvement in performance over the past few months, actually from October of 2020. Our market share index is at 14.4% both in QAAUM as well as closing AUM while that in liquid is at 16.7% and 15.7% in QAAUM and closing AUM respectively.

We continue to have a favorable asset mix as compared to that of industry in terms of higher proportion of equity assets. 57.6% of our AUM comes in from individual investors. Comparable number for industry is 53.7%. We continue to enjoy highest market share in individual AUM and that stands at 13.7%. We processed systematic transactions adding up to Rs. 10.4 billion in the month of March 2021. As stated earlier, the number we report is on actual cash flow basis. We are a distant number two when it comes to B-30 AUM with a market share of 11.7%. We continue to further our journey in creating a state-of-the-art digital infrastructure and leveraging on the same for enhancing customer experience.

We'll now move on to “Financials.” The company's financial performance in the initial period of this financial year had suffered due to effects of COVID-19 on the market. Subsequently, things started improving as markets recovered, and the situation had started looking quite upbeat in Jan, Feb 2021. However, due to the onset of the second wave of the pandemic, across large parts of the country, things have deteriorated quickly since then. We saw an improving trend of operating revenue through the four quarters of this financial year. We worked on cost conservation through the year and were able to keep expenses in check, posting a savings of about 8% from previous year's total expenses. These savings were primarily achieved by a reduction in business development, travel, other overhead, etc., As we come out of the second wave, we'll have to increase spend on growing our business. In February 2021, a grant of ESOPs was made to certain employees and the expense head “employee benefit expenses” include the pro rata amortization of the fair value of ESOPs as required under IND AS accounting framework applicable to the company. A note on this has been provided in the presentation. This is a non-cash charge and is book value neutral. Our operating margin had gone down to 34 basis points in quarter ended June 30, improved to 37 basis points in September 30, 2020 and to 38 basis points for the quarter ended December 31, 2020, it now stands at 37 basis points for the quarter-ended March '21.

In terms of financial highlights for the financial year ended March 31, 2021, operating profit for the financial year March 31, 2021 was Rs. 13,996 million as compared to Rs. 15,129 million for the financial year ended March 31, 2020. This is a decrease of 7%. Profit before tax for the financial year ended March 31, 2021 was up by 6% to Rs. 17,488 million as compared to Rs. 16,531 million for the financial year ended March 31, 2020. Profit after tax for the financial year ended March 31, 2021 was Rs. 13,256 million as compared to Rs. 12,625 million for the financial year ended March 31, 2020, resulting in an increase of 5%.

Financial highlights for the quarter ended March 31, 2021. While we usually compare with similar quarters of the previous year, given the COVID-19 reset, we believe that sequential comparisons are also equally pertinent and hence we have provided both in our investor presentation. The numbers for the quarter are as follows: The operating profit of the company for the quarter ended March '21 was Rs. 3,802 million. This is a 7% higher than operating profit of Rs. 3,562 million for quarter ended March 31, 2020. Profit before tax for the quarter ended March 31, 2021 was Rs. 4,228 million, this was up by 28% as compared to Rs. 3,297 million for quarter-ended March '20. Profit after tax for the quarter ended March '21 was Rs. 3,159 million. This was up by 26% as compared to Rs. 2,500 million for the quarter ended March '20. As this is Navneet's first interaction with all of you, I have requested him to say a few words before we open it up for questions. So, Navneet, can you just take it over from here?

Navneet Munot: Thank you, Simal. Good evening. Thank you everyone for being on this call. The country is going through the second wave of COVID, and I hope all of you and your loved ones are safe. We are doing everything possible in our company to make sure that all our people and their families are able to tide over this difficult time. I joined HDFC AMC on 16th of Feb this year, so it's been a little over two months. As an outsider, I always admired this company and what it stood for. So, it's a great honor for me to lead this team and serve this organization. My predecessor Milind took this company from an ideation stage into a leading asset manager what it is today. We have a leadership team which is highly experienced and, in fact, a good number of them have been with the organization for a long time. In fact, some of them have been with us since inception. The team is bound by a strong set of values that are the hallmark of the HDFC group. Prashant, who's been a veteran in the industry for almost three decades now, leads the highly talented investment team.

Over the last two decades, the company has built an outstanding franchise, it has size, it has scale, it has efficiency, as reflected in one of the largest assets under management and an industry-leading profitability. But we are definitely hungry to do more. And we have all the necessary ingredients in place, the pedigree, the brand we represent, HDFC which is synonymous with trust and confidence, our people, our presence, by presence, I mean, our reach and distribution capability, products with long-term track record and all the necessary resources.

The industry that we represent has seen phenomenal growth, especially in the last six, seven years. Though if you look at long term growth potential, it looks like we have just scratched the surface. So, I feel very optimistic about our industry. I look forward to interacting with all of you in times to come and we are open to take your questions.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Saurabh from JP Morgan. Please go ahead.

Saurabh: Two questions from my side. One is, Simal you mentioned that in the active managed equity. performance has gone up since September. But slide #9 I am seeing the December 20 market share versus the March '21 is still down, it's not much but it's still 30bps So, just wanted to understand what's happening there.

Navneet Munot: It could be due to some of the flows into the NFOs, into the sector and thematic funds, etc., where we may not have the presence, but overall, the performance has started improving, we are hopeful that by and large prospective investors, our partners, everybody has started taking note of that, and it should start reflecting in the flows.

Saurabh: Second, there was a talk about that in six months you are going to launch a lot of funds and explore new strategy within the fund. So, can you just update us on what's happening there?

Navneet Munot: In our industry post the SEBI classifications so, we are present in almost all the core categories. Now, several of them are where we may have lost the market share, so, we used to be a leader in Large Cap, Flexi Cap, Equity, Hybrid, ELSS where we are still very large, but there is scope for us to regain the market share there. So, as far as the core products are concerned, we have been there, but there are gaps could be there, in the passive strategy which we talked about while a large part of the AUM comes from the government mandates and then you have those divestment related ETFs both on the equity as well as on the bond side. But still there could be opportunity on the passive front, there could be some opportunity on the thematic and sector fund. Of late in last couple of quarters we have seen Indian investors looking at diversifying globally and international funds have been looked at by investors, there could be opportunity for us there.

So, over a period of time, we'll gradually fill all our bouquet, in fact, as we speak our NFO on the asset allocation product is going on. Most likely in this quarter we'll have a sector fund which is Banking and Financial Services Fund, there are another couple of funds which are lined up for the next several quarters in some of these categories. So, on the thematic and sector side, on the passive side, as well as on the international side, we have some gaps, which we would like to fill over the next several quarters. But one thing I must mention that I've always praised HDFC MF as an outsider for not launching a product, because there's the fad of the season, we will maintain that tradition. So, we have quite a bit of NFOs line up, but they will be strategies which we believe are a right fit for investors or a segment of investors, where we believe in the scalability and sustainability of that product over a long period. We won't launch a product just for the sake of it or just because it's gathering money at the moment, we won't do it. And also, I strongly believe that a lot of our current products have a lot of potential to grow particularly on the solutions-oriented funds. But wherever product gaps are there, I think they have been well identified. We did the Dividend Yield Fund. You would be aware in the month of December, which had a great success. We have current NFO going on, on the asset allocation product and then the couple of categories that I talked about, I think you will see us in the market over the next several quarters.

Moderator: Thank you. The next question is from the line of Aditya Jain from Citigroup. Please go ahead.

Aditya Jain: I guess you sort of touched upon it, but other than the launch of the new product which you've mentioned, essentially filling out the product bouquet, any other strategic priorities which are on your mind, that means after you have taken over things which you feel need to be changed or improved or however you see it?

Navneet Munot: As I've mentioned that over the last couple of quarters, we have seen loss in market share in some of our key categories. As far as equity is concerned, I think we would like to stem that fall and start rebuilding that market share. We have grown our market share on the fixed income side, but still we think given our brand and a long-term track record and the quality of people we have, still there is scope for us to grow there. Of course, I mean, the industry is evolving, there is a lot of growth potential, but still the operating environment is changing, customer preferences are changing. So, we would work on whether it's the technology, whether it's providing our customers **with a state-of-the-art service** experience and service, the product gaps that I've already talked about. So, I think all of that will keep us busy to ensure that we increase our market share in individual AUM where we have been a leader but again, given our pedigree, our product range, our people, our presence, our distribution reach, I think there's a lot of scope for us to grow. On the SIPs where we have been a leader… I think we have been a pioneer in spreading the concept of SIP in India, we believe the market share that we have currently can go up substantially over the next several years. B-30 is another segment because we have a very large presence there, I mean, if you look at our overall branches out of 227, 149 branches are there, whether in terms of our reach with the distributors in those markets, we believe that there is a lot of potential for us to grow there for all of these things, Aditya.

Aditya Jain: And then one clarification on the ESOPs. So, if you could talk about the total size of the scheme and how will the amortization be done over the coming years?

Piyush Surana: So, as you know, we've given a note that the cost of the ESOPs you need to basically spread it across the vesting period. So, you value the ESOP on the Black-Scholes model. And then you spread that over the vesting period of the ESOP and these ESOPs as we've specified are vesting in three equal tranches over three years. So, each tranche will get vested over the period, so the part of it is one year, part of it is two years and part of it is three years. So, the value of the ESOP will get spread across that period. Part of it has come in this year because it was only granted on February 22. The coming year will see a larger part of charge because it will have a portion of all of the three tranches, then it will go down in the subsequent year and in the last year, it will be the lowest.

Aditya Jain: So, roughly it should be 28 crores per year, but the first year since it has like you said all three tranches…?

Piyush Surana: So, like I said, in the next year or the current running financial year, there will be a charge of the first tranche, which is to be vested in one year. So, that will complete. Then the second tranche, which will vest over two years, half of that charge will come in this year. The third tranche which is for three years, 1/3 of that will come this year. So, what you will see is you will see a front end loaded charge, this year you will see a larger charge, next year it will be less, and the third year will be even less. And you could probably get more material on this once you get our annual report which will probably happen in a month and a half or so.

Moderator: Thank you. The next question is from the line of Sameer Bhise from JM Financial. Please go ahead.

Sameer Bhise: Obviously, as you highlighted some of the key strategic priorities, product launches being one, wanted to get your sense on how the industry is likely to shape up, especially in terms of profitability, how sustainable are current level and what are your thoughts around that?

Navneet Munot: Surely over the last few years, we have witnessed globally that margins in this industry have been under pressure, a lot of money has been moving towards passive, which has led to like consolidation in the industry. Having said that, I think there is a huge growth runway ahead of us. As far as India is concerned, we haven't really scratched the surface, as I mentioned in the beginning. There's a long way to go in the overall growth of the market. And obviously, if we look at the overall pie of the investors wallet, when we look at the total financial assets, or the total assets that households have or whether in the incremental flow, the share that our industry gets is still very small. And we have a long way to go when we compare with the rest of the world. But as I mentioned that globally, we have seen margins under pressure. But I think in India, where we are currently, if you look at our margins in equity, which are like more in the 80s and fixed income, which are like around anywhere between 27, 28 to maybe 30 to 33 basis points and on the money market, liquid etc around 12, 13 basis points. At least in the near future it looks like it could be sustainable, but of course over a longer period as the passives become larger, maybe there could be lower margins on the equity side. And of course, maybe if the assets starts growing in other segments, it will have its overall impact.

Sameer Bhise: Maybe early days, but have you seen any impact on flows probably towards the end of April, and how the way things have shaped up on this whole COVID bit, so any comments there?

Navneet Munot: Again, as I mentioned in the beginning, that the country has been hit by the second wave of COVID, but interesting aspect is that last year at the same time when COVID happened, I think all of us have come a long way, everybody has learned to live with it, and I think the digital is a way of life. In fact, as I mentioned few minutes back that our NFO is on and last couple of days have been quite encouraging. Despite the fact that a large number of branches would be closed a large number of I think salespeople or whether the client services, everybody would be working from home, but I think digital is a way of life and I think we've been able to make good progress on that front. Of course, COVID is impacting, but we are seeing everybody getting used to the new environment.

Sameer Bhise: You would say that April has held up well despite what's happening around?

Navneet Munot: I don't know about the industry numbers and maybe a couple of other products. I was just saying that the NFO which is on and the industry has been able to work in this environment. In terms of flows so far, one of the interesting trends we have seen, Sameer, in last several quarters counterintuitively, that whenever the market has been going up much, we are seeing some redemptions in the industry, but in the month of March when markets came down, a lot of people who've been waiting on the sidelines, they put money to work, and we saw some flows into the equity fund. I think it sounds a little counterintuitive, but maybe that trend might continue. I think if markets stabilize at these levels, we may see domestic investors coming back after nine months of outflows, March was a good month, and maybe we'll have to keep our fingers crossed for the next several months.

Moderator: Thank you. The next question is from the line of Nischint Chawathe from Kotak Securities. Please go ahead.

Nischint Chawathe: My question is the ESOPs that you have announced of around 350-odd crores. Just trying to understand what would be the total cost of these ESOPs that's there in the P&L over a three-and-a-half-year period I believe?

Piyush Surana: Nischint, I think that when the annual report comes out, you will be able to get a better hang of that. Having said that, maybe you could kind of extrapolate numbers from what you see in our current results. But I would wait till the annual report comes out to get a better idea of the total cost.

Nischint Chawathe: I know you're explained the logic, but the current number would be like something like 5% to 10% of the overall vesting, that's happened in this quarter?

Piyush Suarana: Somewhere in that region.

Moderator: Thank you. Next question is from the line of Malad Hemant Manik, an individual investor, please go ahead.

M H Manik: My question is about our fundamental business model, because I think there can be a conflict of interest, because often the number of the great investment opportunities decreases as the fund size increases because of the law of large numbers. So, it is often in the interest of the unit holder that the maximum fund size should be capped, and the lower quality investments are not made, and the returns of the funds are higher. But the shareholders would want that the fund size should be as large as possible. What is your thoughts on this conflict of interest?

Navneet Munot: I assume that you are referring to the equity funds when you said mutual funds as far as the size is concerned. I'm not really sure whether you have a correlation between the size of the fund and its performance over a longer period. And still if you look at the overall size of the industry, the total equity AUM managed by all the mutual funds put together versus the overall market cap, we are still very small compared to most of the other developed markets. I think there is still a lot of capacity, particularly strategies like Large Cap, Multi Cap, Flexi Cap, several of them have a long way to go. At times I think whenever you feel that strategy has lesser capacity or incremental flows may impact your ability to deliver returns in line with the expectations, obviously fund houses have taken that step and have moderated those flows or may even have stopped those flows. But overall, by and large, the question is that whether the mutual fund industry should have stopped flows because they become very large? I don't think we are anywhere close to that; we have a very long way to go

Moderator: Thank you. The next question is from the line of Hiral Desai from Anived Portfolio Managers. Please go ahead.

Hiral Desai: So, my question is, you've spoken about passive funds and the fact that a fairlylarge part of that is the EPFO money that is sitting in there. But if you look at the last couple of quarters, you've seen a lot of these index funds being launched outside the headline indexes. So, the Next 50, MidCap 150, a lot of these small cap funds are being launched. Now generally HDFC has been fairly strong in the small cap and the mid cap domain. Now my worry is in an index fund scheme there is not too much of a differentiation available, the first mover advantage could actually be huge. So, just wanted to get your thoughts on that.

Navneet Munot: The overall size of all the index funds put together I guess is around Rs.15,000 crores or so, and within that, we've been a clear leader, we have around 30% market share. In fact, initially, when I discussed about the product bouquet or the plan for product launches over the next several quarters, that includes some of the products even on the index fund side.

Simal Kanuga: Here, if I may just add, we have already filed for a NIFTY Next 50 Fund with the regulator. We are in the process of maybe adding one or two of other indices as a part of our index fund offering.

Hiral Desai: No, so that is what I wanted to check actually, whether some of these products are actually in the pipeline over the next couple of quarters. So, that was the reason why I wanted to ask about that. The other is, Navneet, since you spent so much time in the industry, just wanted to understand, some of the fintechs which are currently out there, guys like Paytm or ET Money, Grow, and a lot of these other fintechs which are there, are they really helping in terms of improving the penetration beyond let's say the large cities, so are you seeing a lot of flows on these platforms coming through from outside, let's say the top- 20cities?

Navneet Munot: Yeah Hiral, in fact, the fintechs have been doing very well, several of them, if I can take the names, the likes of the Zerodha, Paytm, ET Money, Groww, all of them, they are becoming I would say quite sizable when it comes to the investors using them as transaction platforms. In fact, in the last one year, almost more than 1/3rd of the new investors that the industry has added have come from these fintechs. Also, another interesting aspect is that a lot of these new investors are actually less than 30years of age. So, overall, if I remember the number correctly it 29 odd lakhs of new SIPs these fintechs have created amounting to roughly 29% of all industry SIPs as well and their AUM has already crossed Rs. 20,000 crores. So, they are becoming I would say quite meaningful, and they are really helping in expanding the market to a newer set of investors.

Hiral Desai: Our market share within the fintechs would be similar to what we enjoy at an overall level?

Simal Kanuga: It would not be very optimal for us to get to those numbers.

Hiral Desai: Lastly, I just had one question on the operating cash flow that you disclosed in the FY'21 results. Now, there are a couple of items within that, one is the loss on sale of investment of Rs. 91 crores and then there is an MTM on investments of about

Rs. 217 crores. So, can you just break this up into any impact related to the Essel NCDs and the rest of the investment book? Well, I believe in the P&L we had already taken an impact in Q4 of last year for the Essel NCDs. Could you just break that up for me?

Piyush Surana: Let me tell you about what's happened on the Essel NCDs. You're right that last year we did take a hit on the Essel NCDs and this year over the first three quarters you would have noted that we had taken MTM gains on those NCDs because the underlying collateral which was the shares of the group company of Zee had gone up in value. In this quarter we have given in a note that most of those shares have been sold. So, net-net we have a gain of around Rs.85 crores which is why also you will see the other income of this year being higher.

Hiral Desai: No-no, so I just wanted to check from a full year perspective. There are a couple of line items in the operating cash flow. So, one is the loss on sale of investment of Rs. 91 crores and the other is I think the MTM on the investment book of about Rs. 217 crores. So, this is all related to the rest of the investment book?

Piyush Surana: That is not a cash flow. It is an adjustment to the cash flow from the starting. If you look at the cash flow statement, you're starting from the PBT. And you're trying to calculate cash flow from operating activities. Because this is not an operating activity, you have taken it out. So, the amount that you're looking at is a negative if you look at the heading, that means profit. Can you see that line, the one where you are seeing the Rs. 91 crores, that's a profit?

Hiral Desai: But then the 1,478 number will not add up, no?

Piyush Surana: It will . If you're starting with 1,748 and you go down that line and knock off the pluses and minuses you will come to 1,478.

Hiral Desai: No, no, I understood the fact that it is not related to the operating cash flow, I just wanted to know that this impact is purely because of the investment book and this has no impact related to the Essel NCDs.

Piyush Surana: No, the Essel NCDs are part of the investment book, right. A lot of this does relate to the Essel NCDs, the shares that we sold that I just told you about.

Hiral Desai: No problem. I'll take it offline.

Moderator: Thank you. The next question is from the line of Anush Kumar from B&K Securities. Please go ahead.

Anush Kumar: My question is that we have noticed the shift in equity and income essentially while the yield seems to have been suppressed. Could you enlighten us on this regard?

Navneet Munot: So, last year given the environment I think more money has come into the debt as liquidity in the system increased and there was move towards better quality names and as a fund house, we were a beneficiary of that given our product offerings and the quality of products. On the debt side, we saw more flows. On the equity side, as we have already mentioned that there have been outflows in the industry. Of course, we also got impacted by that. So, definitely the mix has undergone a change. Having said that, if you compare us overall in terms of the asset mix, we have higher equity asset than the rest of the industry.

Moderator: Thank you. The next question is from the line of Madhukar Ladha from Elara Capital, please go ahead.

Madhukar Ladha: So, if I notice this quarter's numbers, the share of equity and the share of debt has actually increased in the quarterly AUM mix on a QoQ basis, yet, the blended yields are lower it seems. So, any possible explanation for that is what I'm looking for?

Piyush Surana: The equity percentage has gone up marginally and the operating revenues also gone up. So, why are you saying that…?

Madhukar Ladha: No, but if I look at it on a yield basis, right, so last quarter, you did about 49.5 bps of revenue to your quarterly average AUM, this quarter you've done 48.8 bps, so there is a decline of about 0.7 bps, then your share of equity has actually gone up by about 80 bps QoQ and share of debt has gone up by about 120 bps.

Navneet Munot: You're looking at the overall share of equity, debt and liquid and doing it in a straight-line method. But within the equity also, it may happen that money coming in one product versus the other, in debt money coming into one product versus the other, that can also have some impact. 0.7 is not too high. So, maybe I think it's something to do with the internals within the asset class. The gain that you have in a fund and the flow versus the book and that can impact the overall margin. So, I mean, quarter-on-quarter, you cannot just straight line put that on the model and extrapolate that.

Madhukar Ladha: No, I understand that, but I just wanted to know if there is anything changing over there in a material way?

Navneet Munot: It is almost the same.

Moderator: Thank you. Next question is from the line of Shubhranshu Mishra from Systematix. Please go ahead.

Shubhranshu Mishra: These two questions are to Navneet. any specific passive strategy we have that can accrue to higher AUMs and ETF, we also have a lot of passive funds that we will be launching?

Navneet Munot: The first question on the passive, I think in India, a large number of people are yet to meet the market. And, of course, we have to always worry about how to beat the market. So, I think there will be opportunity both on the active and passive side. And within passive if you look at the overall market today, almost like 80% plus AUM is from like two AMCs, plus the government disinvestment program, and of course, the PSU debt ETF that we talked about earlier. Rest of the passive from the individual investors are from our other channel partners, which is like our main strength, has been still very small and these are early days. As we talked about earlier, the total size of the index fund is Rs.15000 Crores odd where we have dominant market share, a couple of more products either will be launched in the next few months or are in the pipeline for the next several quarters. And over a period of time, I'm sure there would be opportunity to grow on the passive side as well. And we would participate and the distribution strength that we have, we would like to fully leverage the way we have done it on the active side, on the passive side as well. But we'll always be very conscious about the profitability as well, I mean, we have an industry leading profitability, and we would always be cognizant of that as well.

Shubhranshu Mishra: So, my second question is, largely most of the AMCs have become distribution led franchisees rather than product led with the exception of a few. Now, are we going to get on front foot and then become a product champion wherein we argue with a lot of performances in our Equity funds?

Navneet Munot: If I got it right, if you mean the product versus solutions, I will use that word, providing the right kind of solution to your partners as well as to the investors which includes all your hybrid funds for meeting specific goals like your children benefit fund or in the retirement category, I think those are likely to grow. And again, given our reach and distribution strength and the pedigree of the brand, I'm sure there is a lot of opportunity on that side as well. I guess that was your question, right?

Shubhranshu Mishra: No, what I'm trying to ask is that when we look at large schemes of ours, the performance is not up to the mark when we compare it to the various peers. Now, what are the various things or measures that we are taking or have taken which will bring us back into that game?

Navneet Munot: Yes, I think earlier we mentioned that we have gone through a cycle in performance over the last couple of years. But I think we have seen a material reversal in our performance over the last six months that we have talked about earlier. Are we doing anything different? My answer would be honestly no. In fact, the same strategy which has created alpha over a long period of time, that did not do well in the last couple of years and the very same thing has started doing well in the recent past. But at the same time, I mean, we have stated earlier that we have recognized the fact that for an organization of our size and scale and aspiration, it would be optimal for us to have style diversity. And keeping that in perspective, as you are all aware, we've added two new portfolio managers. Their orientation is very similar to the way we think that is fundamentals focused as well as having a long-term orientation. But they think a bit differently when it comes to valuations. So, this was a first step we have taken in terms of the style diversity. In fact, the two new managers who joined us last year, now they are all managing almost 15% or so of our active equity AUM. In fact, I can share that some of those products have been seeing incremental flows at our end… of course, we don't share the numbers of flow into each product, but we are clearly seeing those products gaining traction with our partners as well as investors. And, of course, the product lineup that we have already discussed above to have more diversified product base particularly in the thematic and sectoral as well as in the fund of funds and the other categories.

Moderator: Thank you. The next question is from the line of Sakshi Goenka from Alchemy Capital. Please go ahead.

Sakshi Goenka: Actually, I just wanted to understand the trajectory of costs overheads going forward considering that you made considerable cost savings this year, how much of that would be permanent and how much could come back as business momentum picks up?

Navneet Munot: Sakshi, if you look at the employees and the other cost, we would have seen a reduction of around 8% or so in FY'21 versus FY'20. And primarily, this was achieved by a reduction in business development, travel, other overheads, etc., and COVID period gave an opportunity to look at every cost item, some part of it or I would say a large part of this cost will definitely come up. And we would not want to hold that on simply because by anyway we will not curtail the growth prospects. But there could be some cost reduction that we could achieve, maybe a small amount but let us say rent and all which may continue for some time. Those kinds of reductions will sustain. But yes, larger part of the costs that we have reduced will rise again in times to come. I must emphasize at the same time that as an organization, we have been very, very cost conscious. In fact, in my first two months, I have seen the frugality which is like part of the culture of the organization. And I think that will always continue and that's why we have been able to have apart from several other reasons our better-quality asset mix or better-quality distribution, etc., is also that given the cost consciousness we have an industry-leading profitability. So, we will always focus on that, but a lot of cost rationalization that could happen last year I would assume that a large part of that will come up and we would not want to hold that on.

Moderator: Thank you. The next question is from the line of Utkarsh Solapurwala from Damos Capital. Please go ahead.

Utkarsh Solapurwala: My question is a follow up on the fintech means, now the millennials are now opting for the Zerodha and Groww more frequently as compared to going to the traditional brokers or traditional channels of distribution of financial services products. So, if the fintech and Zerodha gets license, won't they disrupt the traditional financial services industry and bring down our market share and profitability in the future?

Navneet Munot: Of course, I am a follower of Andy Grove's "Only the Paranoid Survive." We should always be paranoid, at the same time we also know our strength, I mean, our platform, I think our product range, our people, our presence, the partnerships that we have built over the years. And of course, when it comes to the overall digital infrastructure, I think our digital assets are right up there. We will continue to build upon it, whether it's the user interface, whether it's the user experience that we would offer, just the way you took the name of some of the fintechs, I think we would definitely continue to focus on that. So, there is no reason for us to lose out because newer players are entering the industry. In fact, I strongly believe that there is so much of growth ahead of us as far as getting a higher wallet of the overall share, I mean, the households' wallet. The newer players will actually benefit everybody. And I think the growth opportunity is so big, more the merrier. I'm sure everybody will bring in some innovation which will really help the industry. So, I think we would really keep focusing on our strength and as well as keep building on the customer-centricity at our end.

Moderator: Thank you. The next question is from the line of Shailaja from Concept Investments. Please go ahead.

Shailaja: It is considered that HDFC AMC is one of the most cost-efficient AMCs in the world. What different are we doing to be cost-efficient and why is it so difficult for others to achieve?

Navneet Manot: So, maybe you should ask others as well. But I would say I mean it's part of the culture, I think it's every penny that you are spending on every single thing, I think the processes that have been set to get the highest bang for the buck across all functions, I think that's greatly inbuilt, and also, I think it's the way people function, the culture that has been set over a period of time, and, of course, I think it also is a part of the business model that from day one from this company got set up, I think the focus has been on size, the scale, quality of business, profitability of business, all of these are very critical, never try to really compromise profitability for scale or profitability for any other, I would say, motive. So, I think it has been always focused on sustainability of business and I think that has kept us in good stead over the cycles.

Piyush Surana: I just wanted to add here that I think a large part of the credit of this cost consciousness goes to Milind who set this business up. So, it was something that he drove into all the management team all the time that you need to look at this, because this is ultimately what goes into the profitability of the company, so you need to kind of be very careful. And frankly speaking, when I came into this company which was like seven, eight years ago… I'd worked in other mutual funds and when I came here, I saw even sales guys, and usually sales guys are guys whom you need to rein in, but even the sales guys here are so cost-conscious that it was a little bit of a surprise.

Navneet Munot: Positive surprise.

Moderator: Thank you. Next question is from the line of Dipanjan Ghosh from Kotak. Please go ahead.

Dipanjan Ghosh: So, just one small question I think in continuation with what one of the participants had asked on the yield on the net revenue line item, just wanted to understand, you've mentioned that part of it is because of the product mix probably inflows were to fund, MTM gains wherein funds where the yields were low. Just trying to understand is there any change in the distributor commission that you are charging at the scheme level, was there lower pass-through to the fund accounts during the quarter?

Navneet Munot: No, I don't think any material change, no, not really. Like we've always mentioned that it's a function of book versus the flows.

Moderator: Thank you. Next question is from the line of Kunal Tanvi from Banyan Tree Advisors. Please go ahead.

Kunal Tanvi: We've been asking this for a while now. Pardon me for the repetition. So, when we do channel check, when we talk to the IFAs and the distribution one common feedback that we've been getting for a year or so now is that the TER pass on, and the poor performance had led to some kind of discontent within the chain wherein they were not very happy with HDFC Mutual Fund. Wanted to understand any color that you can give on that, how things are moving now with performance coming back and also the fact that we are trying to transition some part of our AUM with different strategies, what is the flavor that we are seeing is on the distribution side of the business?

Navneet Munot: Our customers and partners are the ones who have done for us and that's why we are where we are and are very important for us and in terms of ensuring that we deliver the performance that they would expect from a brand like us. We compensate them well for the asset they bring in as a partner, the connectivity, the service that we would provide them that is very, very critical and we have always been very, very innovative on that front in terms of how we can serve them better. Of course, the performance that you talked about, or maybe some of the other reasons that you talked about in last few years may have had some impact, but we are connected, I mean, last two months or so, a lot of these people are very, very good friends for a very long time. I think they have always been very supportive of us and I have no doubt in my mind that they would be very, very supportive of us in terms of growing the business to the next level.

Kunal Tanvi: My second question was on the passive side of business, and it is largely for the industry-specific, like, when we look at the global markets, when there is sustained underperformance and the size of the particular category goes beyond flexibility to outperform the market, there is a transition from active to passive at a very faster rate. What's your sense on the large cap as a category in India, like, are we hitting anywhere close to the point where in large part of the yield, would shift to say the passive side in next three to five years?

Navneet Munot: So, in last few years, we have seen huge polarization in market, I think, in 2018, '19, '20, these three years where almost 80% or so of the returns, if you look at NIFTY would have come from top five stocks, if I remember correctly, in 2018, that number was over 100%, and all the other stocks detracted the overall return. As the rally becomes broader based, I think the alpha opportunity will come back again, in fact, it's quite visible and if you look at the fund performance over the last couple of months or quarters. In fact, you talked about that globally, and I completely agree that money has moved from active to passive over a long period of time last several years globally. But if I look at the rise of ETFs, and where they have reached today, and also the rise of Robinhood investors, these two trends will actually create more alpha opportunity for active investors. I mean, you would have noticed what has really happened when Tesla entered S&P or some of the other events if you've been following. So, if active managers play their game right, I think focusing on mainly the time arbitrage you have a longer term, long term orientation in your money management relative to a lot of other players who get impacted by the noise in the market and the research arbitrage, I mean, you put the right kind of research resources, robust research and portfolio construction. I mean, we have seen in India over a long period of time, alpha being generated across all market cap segment. And next several years, still there is opportunity given the size where we are today… when I say size, meaning like the size of the money managed by all the large cap or let us say mid and small cap fund managers versus the total market cap. So, still there's an opportunity. Will it become tougher and tougher? Of course, I think the democratization of information, the institutionalization of markets, all of that are leading to shrinkage of alpha. And that's why every fund manager will have to, or every fund house will have to work harder and harder, how do you create a good alpha engine in place. We take pride in the team that we have and the capacity that we have created, the processes we have put in place when we look at our fund management or analyst team in the support team. We believe that there's a lot of alpha opportunity over a long period of time.

Kunal Tanvi: My next question was from both industry and HDFC AMC perspective that if you look at the industry, like it's a very high free cash flow generation kind of side, wherein the HDFC PAT is more than 90%, which is something that we see in the FMCG companies as well. However, the dividend payouts are lower specifically for HDFC AMC as well. Any thoughts on that particular aspect like how do we get dividend payouts, and do we have a specific policy that we adhere to?

Navneet Munot: I think that we discussed in our board and in our team as well. And that's the reason this year you would have noticed the payout ratio has gone up. And it's always a debate in terms of the appropriate level of cash that you would like to run on the balance sheet. But, of course, you are right, because cash beyond a certain level would start dragging your RoE lower.

So, that's a fine balancing that you have to do. But I agree with you. And I think the board is cognizant of that and that's something that keeps getting discussed within the board what should be the ideal payout ratio.

Kunal Tanvi: Sure, if I can squeeze the last one was on a broader basis, if you look at the AMC business, there are four big pillars, that is brand, distribution, risk management and performance. When you come in as a CEO now, what would be the key areas that you would be looking at if you were to draw parallels from these four pillars, what is something that you are looking to pursue with a stronger vigor?

Navneet Munot: You are right and in whatever last an hour or so we would have discussed about the pedigree of our brand, we would have discussed about our presence, which is reach, we've discussed about our people, about our partnerships, about our platform, about our profitability, all of that. And I'll be very honest with you if you ask me for us to go to the next level, what is that another P, I think all of these are just trying to create an acronym all starting with P what is even more important P, that would be a purpose. And I think that deep sense of purpose that we share in the team at HDFC Mutual Fund that we want to be the wealth creator for every Indian. After 20 years since our inception, I mean, today we have like roughly, Simal talked about 9 million accounts, if you look at unique investors, there would be a little over 5 million, if you look at overall industry that is less than 25 million. In a country of our size over the next five or 10, 20 years as the economy goes to a much higher level, within that household savings will always remain very high. If this industry has to go to the next level, I think that deep sense of purpose is more important. And that's where we are going to focus that we will be driven by this mission that we want to be the wealth creator for every Indian. So, basically leveraging on each of these aspects, the pedigree you talked about, our brand is synonymous with like trust and confidence, the people and the experience that we have got within the team, then whether it is the investment team or all the other teams, the partnerships that we have built over the years, the presence that we have 227 branches, when you look at our presence in B-30, the digital presence or the digital assets that we have created, all of that. And I think if we keep building on that, deep sense of purpose that or the customer centricity, that how do we reach out to more and more investors and create wealth for them over a long period. I think that's something that will take us to a different level and that's what motivates the management team here every single day.

Moderator: Thank you. We will take one last question, which is from the line of Abhishek Saraf from Jefferies. Please go ahead.

Abhishek Saraf: Just one area sir if you can delve upon regarding the other asset management structure. So, what is our strategy for PMS and the alternative AIF kind of structure given that we are sensing that there is some move away towards passives also on the mutual fund side, so probably if that kind of leads to a bit of dilution in margins at MF level, do you think we will be focusing on the PMS and AIF side where we could probably earn equity kind of TER and probably at the AMC level, we have positive impact on margins, just your thoughts and how HDFC AMC looks at the alternate structure?

Navneet Munot: So, I think if I go back in history, I think we were one of the early players on the PMS side and I think given our platform, there is definitely a lot of potential or opportunity that is there for us in building the PMS business. And with some of the other regulatory changes, particularly this draft paper on accredited investors can really open up opportunities on the PMS as well as the alternative side, will always remain open to that. I think, going back in history, again, as I mentioned that we used to have a large base of clients who are with us on the PMS products. This year, we are looking at maybe expanding that platform. Having said that, I must say that even in our core products, there is a lot of opportunity for us, plus the new product launches that I talked about in the mutual fund space. So, while we keep an eye on opportunity in the non-mutual fund space, whether it's PMS or the AIF group, but I think bigger focus at least in the near term will continue remain on the mutual fund side.

Abhishek Saraf: So, we have seen our schemes outperforming over the last six, seven months. So, is it largely due to the kind of mean reversion that has happened towards value stock or is there other aspects at play as well in outperformance that our schemes have been able to deliver?

Navneet Munot: Well, I mentioned earlier that has there been a change in investment style? Not really, I think it's the same strategy which has created alpha in past over a long period of time, which did not do well in last couple of years for sure and the very same thing has started doing well in the recent past. At the same time, as I mentioned earlier that newer fund managers have been added who've been managing couple of strategies and while overall orientation may be similar, but they think little differently, particularly when it comes to valuation.

Moderator: Thank you. Ladies and gentlemen, due to time constraints that was the last question. I now hand the conference over to the management for closing comments.

Navneet Munot: Thank you all for being on this call. As I mentioned earlier that the country has been hit by the COVID wave, I hope that you and your loved ones remain safe and wish you all the very best.

Moderator: Thank you. On behalf of HDFC Asset Management Company Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.