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IL&FS Investment Managers Limited

IL&FS Investment Managers Limited (IIML)
Conference Call Update on the Recent Developments and Launch of New Funds
November 18, 2010

Dr Archana Hingorani: Good evening everybody. Thank you for joining this call. This is essentially a follow up to our August 4, 2010 call. We wanted to update all the participants to the latest developments at IIML, which includes new fund raisings that we are shortly going to embark upon as well as completion of the merger with Saffron

So, let me begin with the fund raising. In terms of the fund raising that we had discussed last time, we have 3 pockets of capital; growth private equity, infrastructure and real estate. In the growth private equity space currently, we have nearly fully committed our current fund, which is Tara III, a US$ 225 mn fund. Since we are going to be out of money very shortly, starting the last week of November, we will be on road shows to raise the next round for Tara, which will be Tara IV, targeted at about US$ 300 to US$ 400 mn

In addition, on the real estate side, we have 2 parts of our real estate business. One is the Opportunity Funds which are basically FDI funds and the other is a Yield Portfolio, which we run as a joint venture with Milestone. In the past, this joint venture has raised 2 funds in the Indian markets. We are now again in the next 2 weeks going to be raising a new fund in that joint venture from international investors on the yield play, which is going to be of a similar size - US$ 300 to US$ 400 mn. All other fund raisings will now start in the next fiscal, as and when capital gets deployed from the existing funds under management

As regards Saffron, I just wanted to give you a background. If you recollect last time we had spoken, we had applied for regulatory approvals to make Saffron a part of IIML's family. Saffron has two funds under management. One is the Euro 220 mn Euronext-listed fund vehicle called Yatra Capital. This fund is in Mauritius. In addition, Saffron also had another US$ 103 mn, separate opportunity fund. Putting these 2 funds together in $ terms, this is about US$ 400 mn of additional assets coming under management for IIML. The merger has been completed and accordingly now the Saffron piece is a part of IIML and we will continue to run them like we run all our other international funds out of Mauritius

Also, as a reminder, the reason that we did this particular merger is for the benefit that we think that we can derive from the Yatra platform as well as the theme that comes on board with us. Real estate is a new practice in India and as such, the skillset available is quite limited and we bring in on board additional personnel who will help us enhance our real estate strategy. In addition, we will also have the ability to, alongside the Yatra shareholders; see how we can grow the Yatra platform, which could include funds both in the real estate as well as the non-real estate space including infrastructure and growth private equity. As this is a listed platform, our ability to raise funds would be much faster than how we do it in the traditional route

The traditional route normally would take anywhere between 9 to 18 months to raise a fund, whereas this route, as and when we adopt it, would result in funds coming on board in less than 6 months, and the key would be to work with the Yatra shareholders and to make sure that the new fund raises are non-dilutive to them. We also, from our perspective, as well as Yatra perspective believe that our ability of having been there for so many years as well as the networking, we bring strong skillsets to the table to help enhance the profitability of that portfolio and therefore be able to create a better track record. It also gives us a very important piece, which is access to a new set of institutional investors who are not normally a part of private equity because it is unlisted, but prefer listed and those are the kinds of new investors we will be able to access through this alliance

The merger is effective from August 1, 2010

I will now throw the floor open for Q&A

Moderator: Thank you very much ma'am. We will now begin the Q&A interactive session. Participants who wish to ask questions, please press *1 on your telephone keypad. On pressing *1, participants will get a chance to present their questions on first in line basis. Participants are requested to use only handsets while asking a question. To ask a question, please press *1 now. I repeat, participants who wish to ask questions, please press *1 now. First in line, we have Shreyas Bhukhanwala from Sushil Finance

Shreyas Bhukanwala: Good evening ma'am. Ma'am, just wanted to know what is the acquisition cost for this Saffron?

Dr Archana Hingorani: See, actually, it is a merger. It is a structured transaction that we have entered into and if you were to try and see what it meant in terms of assets under management, then it is equivalent to 8.75% of the AUM that we are adding to our assets and it has been structured in a manner that it is non-dilutive to IIML

Shreyas Bhukanwala: Okay, so there won't be any dilution because of this?

Dr Archana Hingorani: No. First of all, the merger is at Mauritius. Second of all, the way we have structured this, we are using a large part of our internal accruals as well as debt to take care of the 8.75% that we talked about

Shreyas Bhukanwala: Okay, so ma'am, are we raising any debt for the same?

Dr Archana Hingorani: We have raised offshore debt for the same of US$ 20 mn

Shreyas Bhukanwala: Okay. Secondly, the real estate fund which we are talking about around US$ 300 to US$ 400 mn which we are planning to raise – when is it starting exactly?

Dr Archana Hingorani: It is starting now as of the last week of November

Shreyas Bhukanwala: Okay, so with the funds, you will be starting road shows in last week of November?

Dr Archana Hingorani: That is correct

Shreyas Bhukanwala: Okay, so probably in the next 1 year approximately, we would be finalizing this transaction

Dr Archana Hingorani: Yes. We definitely should see first close of both the funds in about 6 months from now. And the final close depending on the traction that you get and how many investors are brave enough to come back to India this fast. So, we should be able to close it out within the next 9 months after the first close

Shreyas Bhukanwala: Okay, okay. Thanks a lot ma'am

Moderator: Thank you very much sir. Next in line, we have Mr Ashi Anand from Kotak Bank

Ashi Anand: Hey, good evening to the management. First of all, congratulations on completion of the Saffron merger. Just wanted to understand this a little bit better, you mentioned kind of 8.5% of the AUM which has been paid under structured transaction? Now, the results release mentions that they are redeemable debentures which have been paid to the Saffron management. So, would it be fair to say that basically we have bought the company for US$ 34 mn of redeemable debentures. Is that the payment transaction, of which US$ 14 mn has gone through internal accruals and US$ 20 mn through debt. Is that the nature of the transaction or it is more complicated than that?

Dr Archana Hingorani: That is correct, except that it is 8.75% of the AUM. So, it works to US$ 35 mn and not US$ 34 mn

Ashi Anand: Okay, excellent, so that is basically the nature of the transaction. Secondly, just wanted to understand, you know, based on the visibility that we have right now, looking ahead into FY 2012, are we likely to launch either a real estate or an infra fund or is that likely to be more in FY 2013?

Dr Archana Hingorani: No. I think growth private equity, we are out of capital. So we are immediately launching the fund. In infrastructure, we have about US$ 300 mn plus currently available for deployment. So, it is likely that the infrastructure raise would happen towards the second half of the next fiscal

And in terms of real estate, what we talked about is the new fund raises for the yield practice. For the opportunity piece, again we still have about US$ 300 mn, and we plan to be in the market for the opportunity piece sometime around June 2011

Ashi Anand: June 2011. So, basically in the second half of next year, we should have launched both infra and RE opportunity?

Dr Archana Hingorani: That is correct

Ashi Anand: Okay fair, and just one small book-keeping question. The JV that we have with Milestone for the Yield Fund, what is the shareholding, as in how much do we hold in that JV?

Dr Archana Hingorani: We hold 40%

Ashi Anand: Okay and would it be possible to give us any color in terms of potential carries that would come across both of the PEPs and the REPs, and do you see it coming in FY 2012, FY 2013. If there is any kind of visibility you could provide on those?

Dr Archana Hingorani: Ashi, very tough to talk about it on the call right now primarily because as we have discussed in the past, this year we have just started to do exits. We are behind because of the GFC (global financial crises) by almost 2 years in all our exits. So definitely yes, towards the second half of FY 2012, we will see some carry but it probably won't be substantial. The only thing that I can see that will convert into full carry probably will be the Leverage India Fund towards the latter half of FY 2012

Ashi Anand: Okay, and in terms of the RE Fund I, by what period should we be exiting enough where we could start certain carries from RE Fund I? Would that be FY 2013 or could it spillover into FY 2014?

Dr Archana Hingorani: RE Fund has about 17 investments and is US$ 525 mn fund. The first exit that I can possibly see on the horizon will happen towards the end of this fiscal, so more towards March. So that is when the first exit starts happening when one of the investments in that particular fund is listed and it comes out of its lockup in February. So, we see some exit happening during that point in time. So, my estimate would be that we will start seeing carry on the real estate piece in FY 2014

Ashi Anand: Would we go on to raise the new RE opportunity fund? Would it be better to kind of just postpone it a little and wait for the entire exit from RE Fund I to be able to demonstrate that or?

Dr Archana Hingorani: No. Well this whole listing of DB Realty. If you are looking that portfolio, we had DB Realty get listed which was you know our investment was US$ 50 mn, which is US$ 90 – 100 mn today. So that is big positive that the investors are seeing in terms of track record and in addition we are trying to exit a couple more, but just in terms of carry, it will not have been meaningful, so I did not mention it, but there are two other exits that are in the works. In addition, the Fund II has more mature assets vis-à-vis Fund I, so we are going to see couple of exits in Fund II also before we get on to the road. So by the time we launch Fund III, you probably have 5 exits from a combination of Fund I and Fund II

Ashi Anand: Sorry, just a very basic question on the structure of the carry. How does it work? Do we have to first repay entire capital, then hurdle or is it carry on a deal basis and then they catch up and…?

Dr Archana Hingorani: If you find carry on deal basis available, please tell me. It has not happened at all in international markets. So, yes, all the way the structure of the carry works is that it is 100% capital backed, then the hurdle and post the hurdle, a sharing of the carry, in most instances 80:20

Ashi Anand: 80:20, perfect. And we don't have a catch up clause on Leverage India Fund and Real Estate Fund

Dr Archana Hingorani: We don't have a catch up in Leverage or Real Estate Fund I. We have a catch up in Tara

Ashi Anand: Do we have catch up in Real Estate Fund II?

Dr Archana Hingorani: Yes, we do. It is a 100% catch up, but it is staggered over time. There is a slight formula to it

Ashi Anand: Great. Thanks a lot and all the best for your new fund raises

Dr Archana Hingorani: Thank you

Moderator: Thank you very much sir. Next in line, we have Ms. Kajal Gandhi from ICICI Securities

Kajal Gandhi: Hello, good evening ma'am. I just wanted to know what is your targeted AUM size you are looking 2-3 years down the line?

Dr Archana Hingorani: That is a good question. Your guess would probably be as good as mine. When we go out with Tara and our yield fund, it will be the first time that we are going back into the market after the global financial crisis. So, it is very difficult to say what it is, but we are targeting, as I mentioned, we have Tara in the market, we have the yield fund, we will be raising the real estate fund as well as the new infra fund. So, I would say in the next 24 months, we should have a target of about US$ 1.5 - 2 bn fresh raising

Kajal Gandhi: Okay and ma'am, how are you seeing the environment bit changing? Do you see more demand for these kind of things back into the market?

Dr Archana Hingorani: See, I think it is probably very fair to say that almost all the investors who have invested in India, does not matter real estate or infra or growth private equity, have had gone back to the drawing board to reassess what kinds of investments they wanted to do. This has nothing to do with India. It is more to do with what happened to them and their experience with each of the investments that they have made world-wide

Now, post that, if you talk to any investor, all of their committees have given a go-ahead to making sure that emerging markets continue to have at least 5-10% exposure from the total portfolio and in that emerging markets, both China and India have significant standing. So, from that perspective, India, I would assume, has greater visibility in terms of getting new money coming in. But it all depends on each institution's experience, for example, you know, when people put money into India, they also need to see the return that they have gotten from India to be able to justify the next round of investment. In our case, because we have been showing exits and we are showing track record, we are quite confident and hopeful that these would help us raise our next set of funds

Kajal Gandhi: Okay, and ma'am, what is the outlook on the fee side you are seeing? Are there any chances of cut in the fees with again more players coming back, meaning broking houses into this?

Dr Archana Hingorani: See once you have moved to a particular level of funds under management, fees automatically come down. So, for example, in real estate and infrastructure, fees were never in the 2% category. They always were in the 1.25% to 1.5% depending on which investor came in. For example, if some investor gave you a chunk of money, US$ 100 to 200 mn, then you would not charge him 1.75%. You probably charge him 1.5% or 1.4%, something in that region, right. So, from our perspective, we have already been doing business plans and calls and our margin estimates on the basis that our fees are going to be in the range of 1.25% to 1.5%. So, from our perspective, from that level of 1.5%, we don't expect a dramatic drop

Kajal Gandhi: One more thing ma'am. How do you see whether there are opportunities because right now the valuations are again at higher levels. So, do you see opportunities in the investment side?

Dr Archana Hingorani: Well, I think that can only be demonstrated by the fact that how many investments you are doing. So, if you look at our Growth Private Equity, we are full up. We just have finished all our commitments and we have recently in the last 6 months done at least 4 investments on a growth private equity piece. Similarly, for real estate, where we have converted nearly 4 investments in the last 3-4 months. But in real estate, time from approvals to completing documentation has become longer – more from the fact that our experiences from 2005 onwards when we started investing. We have put more checks and balances and slowdown mechanisms to make sure that all the things that we require come upfront rather than over time. So, from a real estate perspective, perhaps the deployment will be little slower, but the deal flow still continues to be significant. In infrastructure, I don't think I need to say that, but you know, that is a sector looking for money and investors looking to deploy, so in that sector, valuation is never a concern

Kajal Gandhi: Okay, and one more last thing. Are you looking at any exits right now and any of the companies you have investments have filed for IPO in recent times?

Dr Archana Hingorani: Well, if you have been following us, then you would know that we just completed one of our attractive exits from our Leverage India Fund for ABG, where we have exited completely. Recently, in the last round of IPOs, we had 3 of our companies go public, Ramky Infrastructure, Gujarat Pipavav Port and Electrosteel Steels

Kajal Gandhi: In forward, anybody has filed?

Dr Archana Hingorani: No, not right now

Kajal Gandhi: Okay, thank you. Ma'am, what is your current AUM now, latest?

Dr Archana Hingorani: US$ 3.2 bn

Kajal Gandhi: Okay, thank you

Moderator: Thank you very much ma'am. Next in line, we have Mr Naga Brahma, retail investor

Naga Brahma: Good evening ma'am. Just wanted to know what is the status of generating a fund from the Gulf region?

Dr Archana Hingorani: We have expanded into the Middle East through a base office. We have put in place a joint venture alongside NBD Emirates to do a US$ 400 mn infrastructure services fund, which is looking at transactions to warehouse as well as start marketing the fund. It will start in the first quarter of next calendar year

Naga Brahma: Ma'am, you mentioned that in the next 1.5 to 2 years, you would be raising around US$ 2 bn. So, that means, before you start, you know, closing, these things, some of the funds from FY 2014, by the end of FY 2012, we should be having around US$ 5.2 bn under assets under management?

Dr Archana Hingorani: No, not by FY 2012. Just because you start raising a fund, does not mean you raise it within 6 months, so it takes anywhere between a minimum of 9 to 18 months to raise a fund. So, I would think that by FY 2013, we will be able to achieve a number that is equivalent to perhaps around US$ 4 bn total assets under management, including the US$ 3.2 bn that we already have

Naga Brahma: US$ 4 bn, okay. Any other acquisition in mind, ma'am?

Dr Archana Hingorani: Well, we will try and digest this one before we think of anything else. There is lot of work involved in terms of integration, synergy, etc., as well as we want to be able to capitalize on the reason why we entered into this merger, which is to see how we can help grow the listed platform, so that would be our first priority

Naga Brahma: Thank you very much ma'am

Moderator: Thank you very much sir. Next in line, we have Mr Gyanesh from Intime Spectrum

Gyanesh: My questions are actually answered. Thank you

Moderator: Thank you very much sir. Next in line, we have Kartik Mehta from Sushil Finance

Kartik Mehta: Hello Ma'am, my question is pertaining to Saffron. What is the fund management charges we have for Saffron's US$ 400 mn?

Dr Archana Hingorani: It is a little shy of 2% because there are some large investors who came in at a lower rate

Kartik Mehta: And going ahead, do we have any plan to expand this US$ 400 mn under Saffron kitty or whatever Tara IV and Realty we are going to launch, it would be through IIML platform rather than Saffron?

Dr Archana Hingorani: Of course, the Tara IV and the Yield Funds definitely are on the unlisted platform. So that will continue and as I mentioned, the reason we have partnered on the listed platform is to be able to see how we can optimize both returns to the existing shareholders of Yatra as well as grow the platform, so we definitely are looking towards doing that. The growth of IIML will come from growing its original core business which is raising funds from unlisted sources of institutional investors as well as going forward, we will keep adding even on the listed platform

Kartik Mehta: My question was little bit different. The Realty Fund which we are going to launch, will be through the Yatra platform?

Dr Archana Hingorani: No. That is what I mentioned. They are already out in the market. So, that won't happen

Kartik Mehta: Alright, and as you mentioned that we would be raising fund in the timeframe of 6 months. So, is it fair to assume that the entire US$ 600 mn would be raised in the 6 months?

Dr Archana Hingorani: No

Kartik Mehta: Okay, first tranche only?

Dr Archana Hingorani: No, no. As I said, first closes will happen in the first 6 months. I mean, when first close happen, they are approximately 35% to 40% of the total fund size that you want to raise

Kartik Mehta: Okay and just on the agent commission side for whatever fund we are going to raise under Tara IV and Realty, any sense of understanding because that would be amortized over the period of time? Are we going to leverage upon our already existing investor base and maybe we pay lesser commission compared to what we paid in earlier years?

Dr Archana Hingorani: Yeah, but if you look at it that happens in any case. If you look at REF II, because we were the same investors, the fee that went in to raise that was much lower than when we raised it first time. So, what happens is that in any raise if there is a new investor, then the fee for bringing that new investor is higher, but with an older investor, the fee is very miniscule. So it will be a combination of that because in no fund you are going to have all only old investors

Kartik Mehta: Yeah, that is true. So, overall, blended should come down compared to the earlier ones

Dr Archana Hingorani: Yes

Kartik Mehta: Okay, thank you. Thank you very much

Moderator: Thank you very much sir. Next in line, we have Mr Amandeep from Finquest Securities

Amandeep: Good evening ma'am. Ma'am, is it possible for you to share with us the number of people that would be joining the current team and the approximate cost for the new staff?

Dr Archana Hingorani: The entire Saffron team of 17 people is joining us

Amandeep: And the additional cost that would be incurred?

Dr Archana Hingorani: I think it is difficult to pin that number at this point because we will be synergising, so the cost will change. So perhaps the next call would be more appropriate to answer that question

Amandeep: One more thing ma'am, what is the IRR on these two funds which would be included under Saffron?

Dr Archana Hingorani: You mean, what is the performance IRR going to be?

Amandeep: Yes, ma'am

Dr Archana Hingorani: See, the second unlisted fund is yet to be fully deployed and they are like any other opportunity fund, their target is 25% IRR. So you know, that is what you will have to assume that you are going to or be able to get. In terms of the fund that is fully deployed, it all depends on how it does because this is a fully baked portfolio. It is still to start exiting. So, it is difficult to surmise at this point in time what the IRR will look like

Amandeep: Ma'am, on hurdle rate, is it same towards current funds like around 10% to 11%?

Dr Archana Hingorani: Yes, it is in that range

Amandeep: Thank you very much

Moderator: Thank you very much sir. Next in line, we have Puneet Chande from Anagram Capital

Puneet Chande: Hello ma'am. I wanted to ask you, what would be the cost of debt which you are raising in percentage terms?

Manoj Borkar: This debt is being raised offshore. So it is linked to LIBOR. It will be sub 5%

Puneet Chande: Okay, and I wanted to ask you one more thing. Since you are raising these new funds, Tara IV and Real Estate, which is going to be in the next 9 to 18 months, so when is the management fees of these funds expected, like it would be in slabs or would like throughout, the whole fund management fees would come in this year itself?

Dr Archana Hingorani: No, it won't. See, we are just starting right. So, it takes about, as I said, 6 months to get in the first close. So, if we start today, which is last week of November, we are still going to cross into the next fiscal by the time you complete the first closes, right. The income from those two funds will literally start in the very beginning of the next fiscal

Also, it will be limited to the amount you raise, and then as and when you keep doing multiple closing, what happens is after you do the first close, then as and when you get US$ 40 - 50 mn pieces, you keep closing, you don't wait for the final close, okay. So, the income will keep on adding from that point onwards

Puneet Chande: Okay, so say if you are successful in raising like US$ 200 to 300 mn. So, you will get fees only on that US$ 200 to 300 mn for the next fiscal?

Dr Archana Hingorani: That is correct, but when the next, let us say the next US$ 100 mn comes in and when he signs up, he also pays fee from the date of the first close, okay. So, you will get that fee at that point. It is just delayed in time, but that fee gets accumulated from the date of first close

Puneet Chande: Okay, ma'am, and one question on the carry thing, say I will give you example of this LIF Fund which you have, which is going to like expire in 2014. So, you are expecting the whole carry to come into 2014 or some in 2012 or 2013 as well?

Dr Archana Hingorani: As I mentioned that we should see some carry by the end of FY 2012

Puneet Chande: Okay, that is it. Thank you

Moderator: Thank you very much sir. Next in line, we have Krinal Shah from Anagaram Capital

Krinal Shah: Good evening ma'am. I just wanted to know the exact mechanism through which you have seen 3 exits in Q2 FY 2011? Are they through IPOs?

Dr Archana Hingorani: No, that is incorrect. I just said that 3 of our companies went public

Krinal Shah: Okay, so means, that is the exit from the fund right?

Dr Archana Hingorani: No, it only means that it is liquidity. We have chosen to stay in the company because we don't believe that the pricing has reached at the level where I will get the return that I am looking for. So, it means that the investments are liquid and you can exit them once the one-year expiry of the lock-in happens, but they are liquid investments. So you know what the returns are going to start looking like when you are ready for your exit. That is what it means

Krinal Shah: Okay ma'am. Thank you

Moderator: Thank you very much ma'am. Next in line, we have Mr Ramakrishna from HSBC

Ramakrishna: I am sorry, at the cost of repetition, just wanted to understand the purpose for which you are raising debt for this offshore thing. If you can please repeat as I have joined a bit late

Manoj Borkar: As mentioned earlier, we have done this merger of Saffron. And it is more that it is done at the Mauritius level where we have a subsidiary. So, part of that debt is for that structured merger which we have, which we just explained in giving you the cost

Ramakrishna: Okay, thank you very much

Moderator: Thank you very much sir. Next in line, we have a followup question from Mr Puneet Chande from Anagram

Puneet Chande: Yeah, ma'am, just one question. I just wanted to know how many employees you have currently, as in with the 17 people which are coming new?

Dr Archana Hingorani: 55 including our Dubai office

Puneet Chande: Yeah, that is it ma'am. Thanks a lot

Moderator: Thank you very much sir. I would like to handover the floor back to Dr Archana Hingorani for final remarks

Dr Archana Hingorani: I just wanted to thank everybody for joining this call. I hope it has been productive. We are quite happy to have started this and hopefully we can continue these as and when we have special announcements or even after we have our quarterly results periodically. Thank you