"Karur Vysya Bank Limited Q4 FY-19 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Karur Vysya Bank's Q4 FY19 Earnings Conference Call hosted by Spark Capital Advisors India Private Limited. As a reminder, all participants' 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, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Abhinesh Vijayaraj from Spark Capital. Thank you and over to you, sir.

Abhinesh Vijayaraj: On behalf of Spark Capitals, I welcome you to the 4Q FY19 earnings call of Karur Vysya Bank. We have with us today the management team of KVB represented by MD and CEO – Mr. Seshadri; President & COO – Mr. Natarajan; General Manager & CFO – Mr. Sivarama Prasad and Company Secretary – Mr. Srinivasa Rao.

I now request Mr. Seshadri to take us through the highlights of the quarter gone up after which we will open the floor for questions. Over to you, sir.

P. R. Seshadri: Thank you very much, Abhinesh. Thank you for tuning into organize this call. Thank you all for joining the call. It is wonderful to be able to talk to you again.

Quarter 4 was an important quarter for us as an institution it was a quarter in which we consolidated our position. Several of our key initiatives came to a provision during this quarter. We concluded most of our digital offerings during the quarter. So, today we are amongst the few banks that have people less retail lending process. We also have seamless people less commercial lending process both of these products that are now fully live. There are different stages of being embedded within the organization and our people are getting used to the new systems.

The new systems are proving to be much, much more efficient than the earlier systems. There is of course a time lag when it comes to understanding how the new systems have to be utilized which is something that reduces in seriousness and intensity every passing day. The new systems have enabled us to ensure that the risk that we are accepting is of a quality that we like and it also ensures that we have appropriate pricing for the risk that is taken onboard.

Many of you would have noticed that we have on a sequential basis increased our net interest margin which is in part to the fact that risk-based pricing has been introduced about a year ago. So, for the year our savings deposits on averages, I am talking on average balances basis grew 12%. Demand deposits grew 6%. Time deposits an area which we control deliberately grew only at 2%.

Our advances grew 10% on an annualized basis. And for the quarter our revenues came in quite nicely whilst on the topline basis you can see that our net interest income actually were shy off the prior year net interest income by 4% however the prior period had certain non-repeatable sources of income which did not if you were to subtract that we still had a reasonable growth this quarter.

Other income came in very nicely, 31% on a Year-on-Year basis in this quarter. Total income grew 5% and operating expenses grew at 15% to Rs. 427 crores leaving us with an operating profit of Rs. 464 crores. We continue to have to make reasonably substantial provisions largely credit related post which we were left with peak operating profits of roughly Rs. 112 crores and post-tax we came in at Rs. 60 crores.

Couple of points that I would like to make. One is that we kept a reasonably tight lid on expenses. So, from an expense standpoint our other expenses which is non-payroll related grew at 9% which is reasonably tight considering that we have invested a fair degree of money on our new digital platforms and the other exercises that we carried out.

Our staff expenses which on the face of it appeared to have increased 19% has in reality increased by approximately 9% because the remainder is made up of an increase in the tariff that we had to provide for under AS-15. So, the expense growth continuous to be tightly controlled it is an area that we expect will continue to remain tightly controlled.

Our balance sheet growth on the asset side as you would have noted after looking at the deck continues to remain a little muted. Majority of the growth has come in on the retail side and the retail growth itself has been helped to a degree by Interbank Participation Certificates that we invested in our purchase and ex that the retail growth was approximately 24%. So, when you look at our growth retail has grown nicely. On page 25 it says 48% and that has some wholesale numbers in it.

If we remove the wholesale numbers it is coming in at 24%. Commercial grew at 6%, corporate degrew at 2% and agriculture grew at 3% and overall, we grew at 10%. The share of retail has now reached 22%, corporate is now dropped to 28% from a high of 37% four years ago. And commercials statics at about 34%, 35%.

So, realignment of the portfolio towards a more granular book is continuing at the same time the credit acceptance processes have been changed in such a fashion that we are getting ourselves priced appropriately for risk and that is reflecting in the net interest margin growth that is visible in our financials.

We have kept a very, very tight lid on our cost of funding which have been very disciplined while current account and savings account growth has not been as high as we would have liked having said that we have not been profligate in the growth of our demand deposit which we believe we have ability to actually switch on should we want to grow those deposits.

Our focus for this year is going to be to continue to horn the new advances related platform that we built ensure that the usability improve, ensure that every type of asset that we want to do at the branches is covered and then to switch our focus to the liability side of the house so that we can offer industry leading products so that we can drive our current account as well as savings accounts during the year.

One of the items that we spent a lot of time during the last call was asset quality and I suspect we are going to end up spending a fair degree of time during this call as well on asset quality. We have included at page 37 in this deck a quick look at how our portfolio has been behaving just to indicate to all of you the progress that we have made over the last five or six quarters in working through legacy issues within the portfolio.

So, the way to read this chart on the top right-hand quadrant of slide 38, I suspect some of them may have it at Slide #39 because the first slide is not numbered so as a consequence if you look at page number it will come in as 39 perhaps. So, Slide #38 or 39 top right-hand corner it is labeled portfolio performance, top right-hand corner assuming that the balances in SMA-1 & SMA-2 as on the 31 March 2017 were 100, the SMA-2 balance then moved to 184. So, it has increased by 84% during that one quarter. And thereafter has now dropped to 45% of what it used to be as on the 31 March 2017.

These are rupee numbers. So, our SMA-2 now is 45% of what it used to be two years ago. Similarly it was one-fourth of what it used to be on the 30 June 2017. So, there is a secular decline in SMA-2 and similarly on SMA-1 there has been a secular decline. There was of course a small uptick in the numbers on the 31 December 2018 and the bottom left hand quadrant are the same numbers expressed in percentages of outstanding principle of the book.

Obviously with the book growing the percentage numbers have dropped even further than the absolute rupee number. The reason why we included this slide was to reflect and show to our investors that we take the issue of portfolio quality very, very seriously and this is something that we have been working on. We believe that the legacy issues that we will have to deal with are by and large dealt with. We do not see a very large tail for this legacy related problems going forward.

Last time around we said that over the next five quarters our net NPA accretion would be in the neighborhood of Rs. 1,100 crores of which during the fourth quarter of the quarter that has gone by approximately Rs. 400 crores has been recognized on a net basis. We are left with Rs. 700 crores over the next four quarters. We think that the estimation that we have provided to you earlier is still holds.

We are actually broken it up by what we expect would be slippage and recovery and thereafter the next slippage number respectively of Rs. 1,800 crores, Rs. 750 crores of recovery and Rs. 1,100 crores of net slippage. We suspect that those numbers will still hold with the caveat that if certain NCLT related recoveries which we have not factored in come through during this period the numbers if any will improve.

We do not see significant downside of these numbers and that is on the basis of the improvement in both SMA-1 and SMA-2 that we have demonstrated on page 38 to 39 based on how we are looking at this deck in front of you.

We continue to make significant provisions during the year as you can see whilst our gross NPA grew from 6% to 8.79% our net NPA only grew from 4.16% to 4.98% essentially we are making about $0.60 or $0.70 from the dollar provisions we will expect to continue to have higher provisions on account of the fact that we intend to continue to grow the provision coverage ratio. The provision coverage ratio as defined by you is the NPA provision held divided by the gross NPA and this has moved up over the last six quarters from 32% to 44%.

So, there has been a secular movement upwards. We intend to continue this. Should we have Rs. 700 crores of slippage and should we make Rs. 1,200 crores provisions we expect to end north of 60%. Now the question is an area that we are debating internally is whether given the portfolio quality and given the type of security that we have with us whether 60% or 55% is a reasonable PCR to be held. So, either way we expect to reach that number reasonably quickly as we go into 2019-20.

With respect to our capital adequacy we are now our CRAR at the end of the year was 16% of which Tier-1 common equity was 14.28% and Tier-2 was 1.72% so we are adequately capitalized we do not think that we require incremental capital at this stage. The portfolio performance perspective majority of the losses that came in during the last quarter came from the corporate book which has been a book which is unfortunately been giving us stress through the last five or six quarters and the commercial book NPA accretion net was on an annualized basis 2.63% lower than on the first quarter of the year but significantly higher than where we would like this to be.

Both agri and retail were de-minimis and continue to behave well. With respect to the usage of the RBI dispensation on restructuring our view is that restructuring our asset should be carried out if there is a reasonable likelihood that the business will continue as a growing concern and therefore, we have been quite muted when it comes to the usage of the restructuring tool.

Our restructuring for the quarter was approximately Rs. 68 crores. The current under the MSME bracket our current estimation is that another Rs. 50 crores or there about may be restructured as we go forward. So, the total restructured book would be in the neighborhood of approximately Rs. 120 crores over the next three, six months.

It is not our intention to restructure very aggressively because the restructured has to be predicated on the ability of the entity to continue to operate in a self-sustaining fashion. Otherwise every line of business continues to do reasonably well.

One point that I did not make were the fact that we have reaped as we spoke the last time around we continue to de-risk our treasury. If you go back two quarters you will recall that we had deliberately shortened duration on the treasury book which leads to a reasonably substantial loss being booked on account of longer duration assets being exited. The converse of that happened during this quarter, the assets that we had acquired at that point in time happened to be deeply in the money and we were in a position to sell it booking reasonably large gain.

So, on the treasury side our duration has now come down and suspect that we will continue to bring down the duration as we go forward. So, in summary, I think we have passed through a difficult phase last year where we had elevated NPAs, we had to make aggressive provisioning so as to be able to catch on the provision coverage ratio which was indeed at a reasonably low level when we started and over that period I think we have made very substantial progress as a bank.

We have moved from a bank that operated in a very, very traditional paper based manner to one which is more contemporary which offers products and services in a manner that is more appropriate for the market in which we are operating. We have also continues to change our organizational structure. We established what we call the business banking unit. This is a unit that is going to go after customers who are in the small mid-market. I think these are customers who require credit between Rs. 3 crores and Rs. 15 crores.

Historically they were dealt with by our branches but our branches were very busy and their ability to actually deal with their needs was getting constricted. They did not have the time to actually address their needs. So, we have now set up a large team we have taken our best people and put it against this target market.

This is our sweet spot. This is something that we know how to do reasonably well and now having put a dedicated team of people against it we expect substantial growth on this front. We have also completed our hiring for our non-branch distribution architecture which will enable us to grow our business without relying on our branches. But this has been taking a while I think we have hired somebody in January and then subsequent hiring is happening now.

The team will be by and large ready by May end early June post which the operations of this unit will start and we expect growth to be aided by the non-branch distribution that we are going to set up. We also are intending to handover to our new core banking platform towards the end of May and once that happens API banking capabilities that we currently have on the asset side were also be available on the liability side.

Last year our Transaction Banking Platform grew its balance sheet about four-fold. We expect that in this year it will sort of mature and be an agent of growth for us. So, over the next year our aim is to grow our balance sheet by about 15%, our revenues by about 17% in short don't grow in our budget we are having at 12% but we want to do it lower than that.

We want to end up with pre-provisioning operating profit in the neighborhood of about Rs. 2,000 crores and if all goes well we want to have accretion to provisions in the neighborhood of approximately Rs. 1,200 crores which will leave us with earnings before tax of about Rs. 800 crores.

If we are able to do all of these we will be a position where our provision coverage ratio will be high however exit return on assets will be closer to approximately 100 basis points and we would have a balance sheet and a portfolio of a quality that one would expect from the institution of this kind.

So, thank you very much for listening to me for the last 20 odd minutes. I do appreciate it. I want to thank my team here for what we have been able to do over the last year. I will be very happy to answer any questions that you may have.

Moderator: Thank you very much. We will now begin with the question-and-answer session.

The first question is from the line of Drashti Shah from Investec. Please go ahead.

Drashti Shah: Sir, on Slide 38 if you see our SME 30 plus bucket in last quarter that has increased to 66% from 54% and this quarter there is a sharp decline in that bucket. So, could you just explain that whether we have seen upgrades of those accounts or what has happened to those accounts or those accounts have slipped?

P. R. Seshadri: Sorry you are looking at the top right hand corner or the bottom left hand corner?

Drashti Shah: Bottom left hand corner.

P.R. Seshadri: So, this is you are saying that there is an increase from 54 to 66 between 30.09.18 to 31.12.18 and thereafter a significant reduction from 66 to 36, that is the numbers that you are looking at, right?

Drashti Shah: Correct.

P.R. Seshadri: The increase from 30.09.18 to 31.12.18 happened on account of the fact that that were significant slippages from standard buckets into 1 and 2. And there was slippage from either two standard accounts into one then there was slippage from 1 to 2 and then there was slippage from 2 to NPA as well.

So, if you recall we had elevated NPAs in that quarter and that is what there was a cause of significant concern for us. So, if you recall when the last analyst call happened, we did mentioned the fact that the NPA numbers had spiked. We had also mentioned that portfolio stats had deteriorated during that period.

Since then we have refocused on our collection in architecture, we spent a lot of time. Our teams have been working very hard on ensuring that our customers behave in a manner that is appropriate for them and that has led to significant decline in the SMA-1 and SMA-2 and 30 plus consequently.

There has been of course the Rs. 394 crores that has become NPA to a degree that reduces the SMA-2. But that is not the only reason why SMA-2 reduced because there was also concerted action to collect and bring them back to standard.

Drashti Shah: Sir, for SMA 30 plus has reduced because there were significant upgrades in that account, right? And why is there a higher volatility in the SMA-2 account compared to SMA-1 and SMA 30 plus?

P.R. Seshadri: Correct. I suspect SMA-2 is going to be much more volatile than SMA-1. See the higher you go the more volatile the accounts will be by definition though the trend lines on the two have now started merging in the sense that in the period 31.03.17 to 30.06.17 you see the two had diverged. They were behaving in different ways. Ever since then they have sort of moved in the same direction. So, by definition a customer who is 60 plus, is likely to behave less predictably than somebody who is only 20 plus. So, our expectation is greater volatility there.

Drashti Shah: Okay sir and one more question. Do you see any concern in our agri book going forward because of elections and farm loan waivers?

P.R. Seshadri: With respect to farm loan waivers normally the states pay us. So, it is not as long as that practice continues it is not seen as a major problem. With respect to the elections there are certain stresses that we are noticing on account of the fact that the margin calling processes are getting impacted in the sense that if there is a agriculturist who is you know taken a warehouse loan from us and there is a margin call our regulatory to sell is a little impacted.

But having said that elections will come to an end on the 23rd so we are very close to the end so whatever impact we have seen and we have seen and we have just through it we do not expect it to materially impact the outcomes for us.

Moderator: Thank you. The next question is from the line of Darpin Shah from HDFC Securities. Please go ahead.

Darpin Shah: Sir, just wanted to check post the 3Q con call and while we declared the results yesterday there are a couple of financial institutions which have been downgraded. How much exposure are we having there and how do you see them panning out for us?

P.R. Seshadri: Our NBFC exposure is small you can see it about 3% of the book. Relative to our size and relative to where most other banks are our exposure was small in that category as such. There are 3 or 4 names that are appearing in the press there is a name that is largely associated with the media to which we do not have any exposure. There is a name which is in the housing finance business, two names in the housing finance business both of whom we have no exposure to.

And then finally there is another institution which still exists in the telecommunication space together with interest in the financial space. We do have some exposure there. And we are watching them very, very closely to understand what will happen with that exposure. However we do not expect the numbers that we have told you with respect to NPAs for the year to be materially impacted by whatever the outcomes are on that account.

Darpin Shah: So, is it a double-digit, three-digit number for you?

P.R. Seshadri: It is a three-digit number for us.

Darpin Shah: And some more color if you can provide on your real estate exposure, CRE commercial real estate?

P.R. Seshadri: Can you if you can give me some context in what you want me to talk about?

Darpin Shah: How many accounts you have if you can tell about the borrowers, is it Delhi based or Bombay based or South based how has been there?

P.R. Seshadri: Exact details on our CRE exposure is something that I can give you. I suspect that the total amount that you have here it is roughly 6% of our total advances is an amalgam of retail customers who have more than two properties, who own more than two properties and who have bought a third. A majority of this book will be retail customers who have multiple properties. Then there will be the developers who are building residential or commercial complexes.

So, I do not have the breakup between the three categories right away but however we can make that available once we will have to go back to our MIS folks to pull it out. We do not have any as we see it at this point in time, we do not see any stress on the CRE book which is visible. There is one particular name in Delhi which comes in and out of early stage delinquency which we are monitoring very closely that is low double-digit and we do not see that materially impacting our NPA projections for the year again.

So, we can give you further details, you will have to give me a little bit of time. In fact, all these we have been steadily adding details on to our investor presentation to the extent that we can make it a standard feature we would like to so we will go over this and come back to you.

Moderator: Thank you. The next question is from the line of Abhijit Vara from Sundaram Mutual Fund. Please go ahead.

Abhijit Vara: Sir, my question is on the growth of advances. Last couple of quarters you have been growing in single digit but now you are expecting the growth to accelerate. If you could help us understand which segment will grow? Roughly you are talking about Rs. 6,000 crores of addition to the advanced booked from Rs. 57 crores of gross advances, so if you can just give a breakup?

P.R. Seshadri: It is a good question. We have been in a period of restructuring the way we take risk on our books. Our underwriting systems and processes have been overhauled comprehensively changed. The control processes that we required to ensure that we get good credit on the books have been put in place and all of this has caused us to our branches which are our principle method of delivering credit had a reasonably difficult period getting to understand the new systems and processes.

Now these I think are relatively stable. The growth that we expect is going to come from on the retail side. We are like every other bank that is wanting to bank the retail Indian. Last year we grew net of the IBPC is about 24%. We expect that will grow to about 30% this year. We will focus on our areas of strength which is Southern India and Western India. On the corporate side we will grow about 5%. We do not want to de grow continually but we will focus on the higher quality names and we will cap exposure and the commercial side we are thinking a growth in the mid-teens would be reasonable thing to achieve. So, that is the breakup.

So, majority of the growth coming from retail and commercial and within the commercial itself we want to focus more on the smaller ticket. So, we have actually broken up our commercial book into three parts, one which is done using a algorithmic underwriting which approves loans up to Rs. 2 crores which is done out of our branch. That is where we want to get majority of our growth. And then there is this business banking unit that I was talking to you about which is a new unit that has been set up to go after the mid-market.

So, we would like the branches to deliver about two thirds of the growth and one third of that growth to come from the business banking unit. So, because that will then give us pricing power the smaller ticket gives us pricing power and also gives us granularity and helps us deal with the risk weighted aspect. So, I trust that answers your question.

Abhijit Vara: Sure sir. If you could also help us understand the NIM expansion in the current quarter, how sustainable is it and also some broad outlook as to next year how you see the yields on advances especially. I think cost of funds are fairly stable yields on advances have not improved. How sustainable is this?

P.R. Seshadri: See as I have been saying over the last four or five quarters, we have been saying that we are introducing this best pricing, what you are seeing is the impact of the risk based price change. And the fact that majority of our portfolio is working capital which means that it is re-priceable. So, in the old days the way we used to price a customer was that we used to have product categories, we used to say okay we have a product called Pharma Plus which is aimed at dealers, distributors, retailers of pharmaceutical products and we used to have one product.

One price for that particular product. Now there is no one price for any particular product which is based on what the score card, how good the financials are of that customer, how long it has been in existence. So, pricing can vary for within the product itself. We think that the re-pricing that has happened to our existing book is not complete yet.

We think we still have pricing power as we go forward and we have been consistently maintaining that we have pricing power. From the very beginning we have been saying that our intent is not to do business just to get the balance sheet to grow but we want risk that is reasonably priced for us to onboard it. So, our view is that NIMs will continue to grow and we expect currently NIM for the quarter was 388 basis points.

We think that we have to be north of about 400 basis points and we think that we will get there as we go forward. We also expect NIMs to sort of improve on account of the fact that reversals on NPA accretion will drop as the fresh NPA accretions moderate. That itself will drive NIM up by 10, 12 basis points and there is remainder of the pricing power that will take the NIM up further.

So, our aim is to get to about 425 or so as NIM and right now we do not believe that there is anything that stops us from getting there of course how the market moves and how people price their products we are not price setters only, we are also price takers in the market so to a degree we are dependent upon other people's behavior but given that most of the market is now re-pricing risk we think that we should be able to get there reasonably easily.

Abhijit Vara: Last question on the same subject your CDR has crossed 80% so if at all you want to garner deposits to get this to a more comfortable ratio, will the NIM still be maintained around 4% level? Are you fairly confident that you will be able to pass on any increase in cost of funds to the customers?

P.R. Seshadri: Sorry my apologies. No, I think it is a very good question. Two, three things I want to say when I answer this question. Over the last 18 months we have been focusing on our asset book, on how we write our loans, how we manage our loans. That is where we have done most of our investment, most of our technology spends have gone there, most of the new systems have come on the asset side. We now want to reverse focus and we want to start looking at our transaction banking platform, we want to digitize parts of our trade platform, we want to do a lot of work on the liability side which will help us drive CASA also.

So, that is part of the strategy. We are still working through it, so over this year that is where we intend to spend a fair degree of time and energy in building an industry leading transaction management system and enables us to garner some more CASA. We had a completely retail focused CASA story. So, we need to build some tools which will enable us to get more CASA so that is going to be a big management focus.

So, even if we need to go and garner more fixed deposits which will automatically increase the cost that we have, in terms of cost of funding what will happen to us is that the incremental CASA that we get because of the new systems and technologies that we are intending to work on, that will sort of moderate the increased cost of the fixed deposits that we are bringing on board. Having said that, if there is so much pressure on the fixed deposit side, assets also tend to re-price upwards.

So, we think that the NIMs that we are seeing right now and the growth on the NIMs that we are seeing are likely to continue. We do have as I said more pricing power than we had exercised so far and so we are not really so worried about the NIMs falling back on account of cost of funds increasing.

Abhijit Vara: So, growth target is 12% or 15% sir advanced growth?

P.R. Seshadri: 15% for the year internal target is 15%.

Moderator: Thank you. The next question is from the line of Amit Premchandani from UTI Mutual Fund. Please go ahead.

Amit Premchandani: As you are increasing margin in the retail product and we are seeing competition across banks to grow the retail book, why are you not seeing any competition there and you are seeing such margin expansion?

P.R. Seshadri: That is a very good question. We are seeing competition, that is not to say we are not seeing competition. We are seeing competition. Our distribution is different from the main line retail players. So, given that we have this distribution in semi urban and rural India we are sort of leveraging that to the extent we can, and that is enabling us to garner higher priced retail assets. We are also not willing to trade off volume for price. So, we have been very, very disciplined in saying that if the risk reward equation is not right, we do not want the asset.

And since we now have a digital platform, we are able to implement it properly. So, if I were to give up some of the margin that we are bringing on I have a feeling that our volumes will grow faster than what they have grown right now. So, we have traded off to a degree volume for the margins that we are getting. So, our position has been from the very beginning that we want to be rewarded reasonably for the risk that we are running and that we wanted to grow our book at market but we want to grow our revenues faster than the market.

And in line with that our strategy is to focus on assets where the risk reward equation works for us, and that is what we are doing.

Amit Premchandani: And what percentage of the customer are retail salaried customers?

P.R. Seshadri: Our customer book about 80% of the customers are existing bank account holders with us and about 50% are new to the bank customers, and so these are chaps who have had a bank account with us for a very long period of time and whose transaction history is available. They form a bulk of the customer set. Our customer base as such historically on the deposit customer base tends to be more aligned towards the self-employed base because of the major of the branches that we have and the locations where we have the branches.

And very often if they are employed in smaller organizations so our salary savings base is small, it is an area where we are working on to grow the top tier salary saving space which is something again under work in progress as we speak. So, I do not have the exact split between salaried and self-employed at this point in time but we will make that available. But I trust that provides the context of where we are operating.

Amit Premchandani: And what is the pool of NCLT assets which you expect there will be some recovery because you have not added that under Rs. 1,100 crores, or Rs. 700 crore net slippage number? Also how much flexibility or autonomy the Board gives you in terms of hiring key people or there is too much of interference from the Board in the day to day functioning?

P.R. Seshadri: See this NCLT you are aware of how much we already had. The unresolved NCLT cases let me just look up the numbers I will be right back with you. So, what is left on NCLT now is roughly Rs. 400 crores of assets which are in NCLT processes between Rs. 400 crores to Rs. 500 crores are the assets that are left in the NCLT process.

What will happen with this we are unfortunately order takers with respect to what happens on the NCLT process, but the good news is that should the transaction come to a stage where closure is imminent, regulatory to exit these assets is higher. We are talking about NCLT in Reserve Bank of India's List 1 and List 2. There are other NCLT assets where the process is significantly slower than the RBI List 1 and List 2.

With respect to the second question, so I am deliberately not answering that question as to how much we will recover because it is episodic if recovery is very close you can see there is visibility. We will be able to get out either by the NCLT process itself or by selling it to a third party. But there is uncertainty surrounding it and therefore we have sort of kept it at a distance from our competitions.

With respect to the second question which is the Board, the Board has been supported has helped us hire fair degree of people and the new initiatives that we have been taking have been fully supported. Obviously, the Board has to do its role of asking the right question and ensuring that we are going in the right direction, which is a role that the Board has been fulfilling as it must.

Amit Premchandani: And the ESOP plans have all been approved now?

P.R. Seshadri: Unfortunately the ESOPs meant for me have not been approved for whatever reason, not by the Board, the Board approved it. The shareholders did but we failed to get regulatory approval. That was informed to the exchanges a few months ago. With respect to ESOP for our senior officials that continues to be supported by our Board.

The Board was fairly generous last year and we expect to go back to the Board in our forthcoming Board meeting to ask for more ESOPS for our senior team. Continuing and of course on their continued work for the cause to improve the franchise that we currently have.

Amit Premchandani: And for your ESOP you have to again go back to RBI?

P.R. Seshadri: Yes, that is true.

Moderator: Thank you. The next question is from the line of Rohan Mandora from Equirus Securities. Please go ahead.

Rohan Mandora: With respect to the risk-based pricing, just wanted to understand even on the retail book which is a floating rate have we been able to go ahead and renegotiate the spreads over the benchmark or that is only on the incremental book where we are doing risk-based pricing?

P.R. Seshadri: On the retail side it is only the incremental book. On the working capital loans where they annually reset, we have been able to renegotiate. On the retail side, if you see Page 6 it tells you how much it has grown. On Q4 of last year versus Q4 of the prior year our retail loan through the door pricing has increased by 143 basis points and on the commercial side it has increased by 91 basis points. Commercial our risk-based pricing still has more room that is our view. And we have to address a few anomalies so we are feeling reasonably confident on that count.

Rohan Mandora: Sir, just one point 91 basis point was also the component of MCLR increase that would be a right understanding I believe?

P.R. Seshadri: That is true. There will be some component of the MCLR but this is significantly larger than the MCLR increase.

Rohan Mandora: Yes, and just on this IBPC purchase that we have done so just want to understand what is the tenure of these loans and is there a risk sharing on that and what is the average yield that we would earn on them?

P. R. Seshadri: It is a very good question. These are all retail assets, it is done with risk sharing otherwise the IBPC will come as an investment and these are done for 91 days and the reason why it is classified as retail is because what is purchased on retail assets, but considering that they are transactions on a wholesale basis we are ensuring that we make full disclosure to you.

The rates because since they are 90-day assets with risk sharing that we are acquiring from very, very highly rated institutions the pricing is in the neighborhood of eight quarters eight half. And it varies as any instrument of this nature would vary, so to that extent our NIM is actually understated to the extent that we have these bulk transactions the NIM on our core book is actually higher than what you are seeing.

Rohan Mandora: At the end of 91 days will these loans run down or we will have an option to repurchase them again, just to understand?

P. R. Seshadri: They normally run down. We have the ability to ask to buy again if we wish and the new pool will be looked at by our risk team and then we will agree on what to buy. So, it is a little complicated it requires work to bring them on again.

Rohan Mandora: Sure and if you change your SMA-1 and SMA-2 as a percentage of total loan book as well as what is the share size of the business banking business that we are creating separately the unit not only the loan book sitting there to begin with?

P. R. Seshadri: Okay can you repeat the question. I got the second question but I did not get the first question?

Rohan Mandora: SMA-1 and SMA-2 as a percentage of outstanding loan book currently as of March?

P.R. Seshadri: That is one thing that we have tried very hard not to put in our deck. Having said that we will include it as we go forward but the point that I am trying to make is that our SMA-1 and 2 are significantly lower than where they were a year and a half ago. We continue to work on bringing them down. On the corporate side we have disclosed that it is 61 basis points for SMA-1 and 2 as a proportion of the corporate book.

Our aim is to get SMA-1 and 2 together under 300 basis points, but we are not aware at this point in time. With the SMA-2 we would like that to be below a 100 basis points for the entire book as such, but we are not at that right now. We are little off it but that is the aim directionally.

With respect to business banking unit, roughly about 40% of the book is what will be there a little less 35% of their book will be part of business banking and the rest would be part of our core smaller ticket commercial business managed out of our branches and since it is a new unit we expect them to take a little bit of time to settle down and once they do we want the growth to come in the same proportion for this year but we suspect that business banking will probably be able to deliver a little bit more but once they fully settle down.

So, over the years two thirds of the growth to come from the smaller ticket higher yield side and one third to come from business banking.

Rohan Mandora: And like you alluded to that in SMA-1 plus 2 you are targeting for a size of below 300 basis points, so if you could quantify what time frame are you looking at to reach that?

P.R. Seshadri: I mean I would like to do it tomorrow but my own expectation is the quarter following next we would be there and the expectation is after the second quarter results when we come back on this call I hope to be able to announce that we are below 300 basis points.

Moderator: Thank you. The next question is from Akash Datani from HDFC Securities. Please go ahead.

Akash Datani: So, my question is on the IBPC purchases. So, the rationale for this would be to meet PSL requirements?

P.R. Seshadri: Sorry could you repeat that question, I am sorry?

Akash Datani: Sir, my question is on the IBPC purchases. So, is the rationale to meet PSL requirements?

P.R. Seshadri: No, actually the IBPC purchase that we do forces us to have PSL against it, so it is the opposite of what you are just saying. It is the reason why other people sell it to us is to meet their PSL requirements. So, this is a method of increasing my aggregate book so and deploy liquidity at a rate which is better than other treasury instruments. And given the fact that we did have PSL on our side we could afford to buy it. So, the assumption that is an arbitrage that is offered by the markets.

Akash Datani: Okay and so could we expect something similar in the future that you would continue to do a lot of IBPC purchases?

P.R. Seshadri: It is now our intent to use this as a tactical tool if we have PSL assets with us. If we were to tell sell the PSL asset as a PSLC, if we were to get x% and if I were to buy IBPC and the yields declared is y% and y is greater than x then I will buy the IBPC. It is a spin off between whatever is the more appropriate thing for us to do under the circumstances.

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

Jay Mundra: I wanted to know what is the gross spillages for fourth quarter and if you can break it down in terms of Corporate, Retail, SME because what you have given is the kind of net addition?

P.R. Seshadri: Yes Jay. I think we will start giving you the gross numbers from now on in the deck itself, it is a little.

Management: Jay, I told you yesterday so basically, we will give you the numbers as we go forward.

Jay Mundra: You mentioned that your projection of kind of a watch list or kind of a residual stress remains the same. But as someone asked there has been a little bit spike in the credit worthiness of some of the large borrowers. Even in the NBFC space and even in some of the mid corporate space maybe based out of Kolkata, they are into some of the divisional kind of a multi-product multi division kind of a conglomerate. So, you are confident about your Rs. 1,100 crores of net slippages addition over the next four quarters that is the bit of a question?

P.R. Seshadri: Yes. We remain confident, we with the name in Kolkata that you mentioned we unfortunately do have some exposure but that is already been recognized in the quarter that is just gone by. So, there is no further impacts ahead that was already factored in into the Rs 1,100 crores and considering the information that we have at this point in time on our own book and whatever information is available on the stresses in the marketplace we are reasonably confident that the number that we have put with respect to the incremental slippage over the next four quarters is a reasonable estimate given the information available today.

Moderator: Thank you. The next question is from Yash Agarwal from JM Financial. Please go ahead.

Yash Agarwal: Sir, is there any one-off in the net interest income this quarter?

P.R. Seshadri: No, there is not. There is a very small di-minimis amount which is on account of some interest refund that we received from the tax department which is accounted there which from the next three years onwards we will account in other income. But that is a very small amount that is there. That does not make any difference to the net interest income.

Yash Agarwal: Sure, and sir you know you spoke about Rs. 1,200 crores of provisioning that you are going to make in this financial year. So, I understand this is part of the cleanup that you have undertaken but after this what is the steady state credit cost of provision that you expect the bank to have?

P.R. Seshadri: So, from the very beginning of the last four or five quarters that we have had these calls, we have been saying that we want to work towards a steady state net NPA slippage of 150 basis points. That has been our stated position for a long period. We are hopeful that in this current year we will hit that number, 150 basis points is Rs. 750 crores on Rs. 50,000 crores which is our opening balance sheet.

And as the balance sheet grows so what they are saying is this year will be actually lower than 1.5. Our aim is to drive that down but right now we want to get to 150 basis points where we have visibility and then drive it down further but we will comment on that once we cross the 150-basis point Rubicon.

Yash Agarwal: Sir, but what would be the credit cost there, would it be 75, 80 bases roughly how it is like?

P.R. Seshadri: That is right, credit cost will be 75, 80 bases, yes.

Yash Agarwal: And that is a very realistic number for the financial year 2021, right?

P.R. Seshadri: That is what we are working toward, yes.

Yash Agarwal: Sir, one more question. In the last quarter call, you mentioned a net slippage number of Rs. 1,100 crores with about Rs. 200 crores downsize risk. So, is it a correct assumption that this Rs. 200 crores down size risk now does not exist?

P.R. Seshadri: It is reasonable assumption to say that it does not exist.

Moderator: Thank you. The next question is from Umang Shah from Safe Enterprises. Please go ahead.

Umang Shah: Sir, my question is regarding the net additions to the commercial slippages. It is currently at 2.63% so where do you think is it higher than normal, is it lower than normal and where do you see this at steady state?

P.R. Seshadri: I think it is a very good question. Obviously 2.63% is not a sustainable level and we expect slightly elevated slippages in the first quarter. If you recall we said that we transfer about 30%

to 40% of our branch managers annually in the month of April and normally that leads to elevated slippages on the cost cycle for whatever reason and so during this quarters we expect numbers in the neighborhood of what you are seeing here 2.63 and thereabouts. And then we expect it to moderate as we go into the rest of the year, we think that it will trend back towards the 1.5 in the second half of the next year.

Umang Shah: And sir, this Rs. 700 crore of residual slippages which you are talking about is it over and above the 1.5% slippages which we are seeing for the rest of the year or?

P.R. Seshadri: **I**t is included in the 1.5%, the two are the same.

Umang Shah: Okay so you are saying Rs. 700 crores will be the total slippages in the next four quarters?

P.R. Seshadri: We are saying that if all goes well, if the power of the heavens above are with us we will get to Rs. 700 crores for this year.

Moderator: Thank you. We take the last question from the line of Renish Bhuva from ICICI Securities. Please go ahead.

Renish Bhuva: Sir, one strategic question as you know we have been a fairly SMA recognized bank historically and you have rightly mentioned that we are pretty strong on the SMA side but incrementally we are thinking to grow more on the retail side so we are saying that we will grow 30% in retail and commercial will be let us say mid-teens. So, what is the reason behind focusing more on the retail and not leveraging on the stronger side which we had or might be we have also? So, what is your take on that sir?

P.R. Seshadri: It is a very good question. What we are doing right now is simply leveraging on the customer base we have. So, we have large number of retail customers to whom we were not offering loans in the past. As I said 80% of the loans that I am writing on the retail side are to my own banking customers. So, we are not going out there and getting new customers so much. Once the product is embedded that is an opportunity that we have. So, in the near term it is my own customers I am selling more loans to.

And we have 7 million, 8 million customers currently the total number of loans we have to them will be probably 100,000 or something like that. So, the opportunity there itself is quite large. So, this is rather than what we are saying is we complete the offering to our retail customer set which we have left open and our customers who are consequently banking with us but borrowing from somebody else we are plying that right and we continue to focus on our commercial.

Renish Bhuva: So, basically what you are saying is that we still have much headroom to leverage the existing customer base and that will lead to the higher retail growth, so and I think that is why we will be manage the cost. Otherwise retail is a very cost business but since we have a readymade customer base you are pretty confident that we will achieve the retail growth without impacting the cost ratio. Is it fair to assume?

P.R. Seshadri: That is fair to assume.

Renish Bhuva: Right and sir just last question from my side. On the retail side which are the products we try to cross sell first like in a life cycle of the customer, if he is on the liability side which product we first offer him and then we will offer other products?

P.R. Seshadri: So, we are pre qualifying customers across housing, auto and personal loan. But we are making pre so prequalification is where we do a scrub and that is something that we have started very recently. We scrub against the bureau score etcetera and see that the basic parameters are met. But these are not preapproved. These are distinct from preapproved. So, we have also done preapproved personal loans where no further action is required.

The customer is approved all he needs to do is say yes and we give him the money. So, we did one set of preapproved personal loans and now we are working on the prequalified basis across the products. So, personal loans will be preapproved, the rest will be prequalified.

Renish Bhuva: But sir in case I mean if we just want to quantify like say in FY20 incrementally this 30% of the incremental growth in retail which product will drive the retail growth will it be housing, or personal loans or the auto, how will be the mix within retail on the incremental growth side?

P.R. Seshadri: It is a very, very good question that you have asked me. We are working in growing the secured books a little faster than the unsecured books. So, housing is our fastest growing book as you can see in this deck. Housing will continue to be the fastest growing book that too self-occupied housing investor housing to the extent that we know.

But we will get a little bit more adventurous on the unsecured space so if you look through our investor deck you will find that our unsecured exposures are very, very small. Now it is crossed Rs. 500 crores for the first time, but that gives us some pricing power which we have not fully utilized. So, we will probably grow unsecured a little bit more.

We have broken it down product by product but I do not have it with me right now for me to be able to answer it as to what the budgets are for the next year but we can provide that in a subsequent call if necessary.

Renish Bhuva: Right so directionally the focus would be more on the secured products than the unsecured products?

P.R. Seshadri: That is right.

Moderator: Thank you very much. We will take that as the last question. On behalf of Spark Capital Advisors, that concludes the conference. Thank you for joining us. Ladies and gentlemen, you may now disconnect your lines.