



## “Kotak Mahindra Bank Limited Q1FY14 Earnings Conference Call”

**July 18, 2013**



**MANAGEMENT:**    **MR. UDAY S. KOTAK – EXECUTIVE VICE CHAIRMAN &  
MANAGING DIRECTOR**  
**MR. JAIMIN BHATT – PRESIDENT, GROUP CFO**  
**MR. K.V.S. MANIAN – PRESIDENT, CONSUMER BANKING**  
**MR. S. NARAYAN —PRESIDENT, COMMERCIAL BANKING**  
**MR. GAURANG SHAH – PRESIDENT, ASSET MANAGEMENT &  
LIFE INSURANCE**

**Moderator**

Ladies and gentlemen good day and welcome to the Kotak Mahindra Bank Q1 & FY14 Earnings Conference Call. As a reminder all participants' line 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 this conference call you may signal an operator by pressing \* followed by 0 on your Touchtone phone. Please note that this conference is being recorded.

At this time I would like to hand over the conference to Mr. Uday Kotak, Executive & Vice Chairman at Kotak Mahindra Bank. Thank you and over to you, sir.

**Uday Kotak**

Good evening colleagues, it is a very interesting day and time to be doing this call both with reference to the bank's results as well as the issues in the financial sector and also the outlook from here. Our view at this stage is on the broader economy we believe that the economy is slowing down pretty significantly and frankly we feel if the economy did managed to grow at 5% or higher that would be a good thing but we are pretty confused at this stage whether we see that level of growth continuing or the economy even slowing down further. In terms of credit growth and more specifically with reference to our bank at the last call we had guided around 20% in the results of March. Our view now is with the slowing down in the economies our overall advances growth estimate for this year is around 15% mark and within that I would like to say that if I breakdown between the three divisions on a relative basis the consumer division is growing faster than the Commercial Bank and the Corporate Banks.

Therefore average 15% with higher than 15% growth in the consumer bank side and lower than 15% growth in the commercial bank and wholesale bank depending on how the markets go around the 15% mark. In terms of credit cost if you look at our quarter we have had increasing credit costs and NPA provisioning essentially arising out of a general decline particularly in the construction equipment and the commercial vehicle segment but on the corporate side recognition of one account as an NPA of about Rs. 150 crores which we have recognized and taken **into** as an NPA against we understand for that particular account the account otherwise is going in for a CDR but keeping mind that the after loss if you are wanting to recognize an issue we have taken it in to the NPA category which is this specific account and the provisioning on account of this account is one of the reasons why you have seen some increase in our gross NPA as well as in terms of our provisioning thereafter.

I would like to also clarify that as a general broad principle with reference to recognition of NPAs and stress we have zero CDR that is we have no account where we have participated in a CDR. Our restructured standard loans out now close to zero. We have no funded account which has been moved into a non-funded category that is moving from a balance sheet item to an off balance sheet item. We have not sold any loans to ARCs and subsequent purchase of that same investment as a security receipt and we have no conversion of any loan to a credit substitute. So this is therefore in many ways what I have always said on earlier calls with reference to our situation you see what you get and you get what you see with reference to both gross and net NPAs in terms of what we see on the reported numbers.

On credit cost this quarter our credit cost has been higher as I mentioned primarily coming because of provisioning on this single account and a deterioration in commercial vehicles and construction equipment segments but if I have to give you some sort of a guidance for this year, we would give a guidance of for the full years credit cost at about 60 basis points on the advances base. The number for the first quarter obviously is higher than this for the full year as we see it.

Moving on to another item which is right now on everybody's mind and that is with reference to our treasury and interest rates. You would have seen that we have had a great quarter for treasury for April to June and here I would like to make comments both on our broader positions as well as on liquidity. We have all seen the RBI action as of Monday night and in terms of our general exposures to bond and CD and money market portfolios we peaked our exposures in April-May and our current trading exposures would be about half of that peak and that is as of Monday that is prior to the Tuesday event, roughly that. And on the pure banking book which is the SLR book we are currently running at duration of about 2.5 years.

So this is on the broad treasury side, in terms of our liquidity, I am happy to say that in many ways this was like little bit of a stress stepped in the system which we saw on Tuesday and we were lenders in the inter bank call market today because of surplus liquidity with us and even yesterday our call borrowing were close to zero and therefore we have run with a reasonably comfortable liquidity position at this point of time. Going forward we think that as growth slows down the broader economy will force challenges to bank's balance sheets and it is here that we genuinely believe that from the current levels of credit provisioning we get better into the future quarters, that is number one. And at this stage we do not see any big item as a potential risk on the balance sheet as we talk to you and therefore our view is unless there is something, there is a further dramatic deterioration in credit and the economy from here which are reasonably comfortable on the current situation on the balance sheet and on the overall NPA positioning again we have examined very closely the levels of provisioning we have done versus the underlying assets and security we will have against each loans and our approach is to go line-by-line every quarter for all amounts above Rs. 2 crores evaluate the security value and thereafter make a provisioning such that we take a haircut of the security value before arriving at the final provisioning number and effectively at what value we carry the loans and therefore we feel reasonably comfortable with our levels of provisions and do not see, on the current balance sheet, anything dramatically deteriorating from here.

With that I will hand over to my colleague Jaimin to take the discussion forward and we actually do genuinely believe that when the going gets tough the tough get going and it is time for us to demonstrate how tough we are.

**Jaimin Bhatt**

I will quickly take you through the earnings update which has been circulated to you. This quarter we end the bank's standalone with a post-tax profit of Rs. 403 crores up 43% from what we declared last year this quarter which is Rs. 282 crores. Loans in the bank now at Rs. 50,500 crores 19% up on a year-on-year basis and Uday as mentioned restructured loans

negligible from 0.01% of our overall advances books. Capital adequacies standing pretty well at 18.2% overall with Tier 1 at 16.9%. This is without taking into account the current quarter profits. If we take the current quarter profits it is the Tier 1 jumps from 16.9% to 17.6% and with Basel III it does not make us any material difference in the overall numbers.

Return on assets at the bank standalone at 1.9%. Both current and savings account we have seen a good growth overall. We end the period with a CASA percentage of 29%, plus of course we have got sweep TD's which add another 7% to the deposit rates. On a consolidate numbers we end this quarter with Rs. 627 crores which is up 42% over the Rs. 443 crores which we had for this period last year. Net worth at the console level at Rs. 17,000 crores helped of course by a placement which we did during this quarter to affiliate of GIC.

Overall advances at the group level at Rs. 68,000 crores about 20% up from the same period last year. Net interest margins overall at 4.8% remaining healthy at that level. Overall at the advances level we have seen a growth of 20% on the year-on-year basis and a cut across various segments of where we have lent other than the commercial vehicle construction equipment where we have deliberately closed down the progress and we have a negative growth there. All the other segments have shown a positive growth for the year-on-year period. For this quarter the margins' growth comes from the corporate bank which has grown by almost Rs. 2,000 crores at this period.

Overall entity wise numbers apart from the bank the big contributors continued to be the Kotak Prime where this quarter clocked Rs. 117 crores of profit versus Rs. 94 crores for this period last year. The insurance entity ended this quarter with a Rs. 71 crores profits as against Rs. 32 crores last year and the securities Broking Company at Rs. 31 crores versus Rs. 23 crores last year. Net worth at a bank level Rs. 11,165 crores which includes the GIC infusion which happened this quarter. At Kotak Prime it is Rs. 2,469 crores, Securities close to Rs. 2,000 crores. The insurance company has a net worth of just short of Rs. 900 crores. Kotak Investments at Rs. 348 crores and overall at Rs. 17,000 crores.

If you look at the overall three financials the asset size now is Rs. 1,17,000 crores which is a 21% rise from same period last year. The book value now standing at Rs. 224 per share. If you look at the financing business overall the Rs. 68,000 crores of loans broken up into consumer commercials and corporate. The consumer book at Rs. 27,000 crores becomes the largest number in this period. The commercial book at Rs. 23,000 crores in the wholesale at Rs. 17,000 crores. The net interest income, we have seen a YoY growth of 27%, the NII at the console level at Rs. 1,143 crores with NIM at 4.8. The post-tax profit for the financing business has seen a 33% jump during on an year-on-year basis and this quarter we see this business contributing Rs. 524 crores to the post-tax number.

At the bank standalone the NPA number we talked about at the net level of 0.98% versus 0.80% a year ago and ROA at the bank level at 1.9%. If I take the bank's Profit & Loss apart from the net interest income which has grown 27% year-on-year. The other income clocked

Rs. 462 crores for this period also helped to an extent by treasury profits and gain from stressed asset business.

Expenses overall has grown by 17% on a year-on-year basis and as Uday explained we have taken some provision hits during this period with overall provision number Rs. 169 crores which includes the Rs. 35 crores towards investment and Rs. 134 crores on the advances portfolio.

Overall the Rs. 462 crores of other income which we talk about comprised of Rs. 229 crores of service fees income which is a jump from Rs. 164 crores in this period last year. The treasury and the ARD income which I said has contributed to the growth this quarter. And as Uday explained the NPAs we need to recognize the fact that the restructured numbers are negligible. We do not have any participation in any CDR and no conversion in to off balance sheet items and we have not sold any loans which we have originated into asset reconstruction company to hold SR's

During this period we also had purchased a NPA portfolio from an NBFC which thanks to the accounting rules we were required to take the entire write down upfront and that contributed Rs. 23 crores, the size of the portfolio was Rs. 23 crores.

At the segmental level therefore the corporate and wholesale banks for this period clocked a profit before tax of Rs. 288 crores. The retail banks clocking Rs. 180 crores and the treasury segment contributing Rs. 139 crores.

Overall advances if we look at the RBI cut which is anything over Rs. 5 crores constituting a corporate advance. The breakup of advances between retail and corporate tilting slightly in favor of corporate with that contributing Rs. 26,000 crores out of the Rs. 50,000 crores advances in the bank.

The balance sheet of the bank overall deposits during this period we have seen a 26% growth. Interestingly the current account has shown a growth of 28% on a year-on-year. Savings deposits showing you a growth of 45% and while term deposits others have seen a 17% rise. We have seen a sharp rise in the sweep term deposits during this period and that constitutes 7% of our total deposit base as of June. Advances that are mentioned has grown 19% with an overall balance sheet growth at the bank level of 23% on a year-on-year basis. We ended this period with an overall branch number of 445, added 1.5 lakh customers during this period and our overall current plus savings account plus TD is below Rs. 5 crores now constitutes 61% of our total deposit base.

If you look at the bank advances as I mentioned the largest number comes from commercial banking advances where we have seen a growth of 15% on a year-on-year basis. The consumer bank advances showing the 31% growth on a year-on-year basis. The largest contributor to this has been the personal loans on a percentage basis. The mortgage loans constitute the largest part of the consumer bank advances. The focus in the consumer bank

remains on the SENP segment and the attempt to cross sell through the bank's network. The consumer side of the business continued to show profitable growth with very low delinquencies at that segment.

The commercial bank which comprises construction equipments, commercial vehicles, agricultural division and business banking, the CE and the CV segment consciously we have closed that ground and for the year-on-year basis have seen a 6% negative growth. Agri has grown 28%. The focus on the semi-urban and the rural areas continues. We continue to deepen our tractor finance division and are one of the leading financiers of tractors in the country. Wholesale bank advances have seen a growth of 16% within the bank level. We continue to be customer focused on covering and enhancing forex flows and continuing to be looking largely at the working capital related lending.

Kotak Prime, the NII for this period at Rs. 205 crores about 31% rise from the same period last year. Income at Rs. 253 crores. Overall advances at Kotak Prime has grown 21% on a year-on-year basis. 76% of the advances at Prime constitute the passenger car division. Capital adequacy at Prime pretty healthy at 16% and ROA at that entity at 2.5%. The insurance business for this period clocked a total premium of Rs. 490 crores. Good growth in the group business which contributed Rs. 170 crores.

The Securities business overall for an income of Rs. 147 crores this period also saw continued decline in the overall cash market volumes in the industry which went down from Rs. 14,000 crores in the previous quarter to Rs. 13,000 crores now. The securities company clocked a post-tax profit of Rs. 31 crores.

Overall across the group our assets in the management now are at Rs. 62,000 crores where the asset management companies have domestic mutual funds contributing Rs. 37,700 crores largely coming from the debt fund. The alternate asset now manages about Rs. 5,000 crores of assets under management. Probably those are these major highlights. We will be open to taking questions.

**Moderator**

Thank you very much, sir. Participants we will now begin with the Question & Answer Session. We have the first question from the line of Amit Premchandani from UTI. Please go ahead.

**Amit Premchandani**

I have got a question on the RBI action, in your judgment what are the outcomes RBI is aiming at and what are the goal post RBI is aiming at and what would you look at to judge if further tightening is coming or some relaxation on these measures are coming, either ways?

**Uday Kotak**

Thank you for a very difficult question to start with. Actually we were beginning to feel uncomfortable late last week about the fact that there is increasing pressure on the Central Bank to demonstrate action for bringing the Rupee under control and it was just feel on the basis of what we were picking up as signals between Delhi and Mumbai as well and therefore with the Rupee doing what it was there was a grapevine talk that why are the policy makers

not doing anything and then in fact you have the memory of 1997, at least I have it pretty vividly, when Dr Jalan was at the RBI and there was a sledge hammer which was used at that point of time and just to refresh many of the people on the call both analysts and some global investors in 1997 when the sledge hammer was used for a period of 8 or 10 days, interbank call rates were at 80%. So this measure, though pretty stiff, is not anywhere near as drastic as what we saw in 1997 or 1998. I think January 1998 if I am not mistaken. Therefore my view is that 1998 versus today is a big difference. In 1998 that measure did work and the reason it worked was there was genuinely speculation in the Forex markets.

But the thing which we are not clear about and may be the policy makers have greater information is that the three areas of Forex market speculations one is exchange credit, second is NDF, non deliverables forwards and third is banks' open position which RBI is monitoring closely. The decision to shut off exchange credit was taken a few days earlier. NDF, they have already got something in mind where they have already got a policy in place where at least subsidiaries of Indian entities cannot trade in the FX markets on the NDF platform. And third is bank open position the Central Bank was monitoring very closely. Therefore it is possible that the Central Bank has additional information which we do not have but all the three major items of speculative accessories are flows in the FX market in reality at least we are not able to clearly see prior to this action. Now obviously the action is based on the fact that this is the way to curb speculation in the FX market by dramatically tightening liquidity and through tightening of liquidity impact on interest rates because the apparent position is that we are not increasing interest rates but through tightening of liquidity or actions which put fear of tightening liquidity on the market participants the interest rates particularly the short end move up and we are now seeing as we talked to you an inwards yield curve which is the short end is higher than the longer end.

So short-end at least on Tuesday moved 200 basis points the longer end moved 50 to 60 basis points, But the key question in my mind is this action at least in 1997-98 as I recollect was because of excessive speculation. Therefore it is possible that the policy makers have more information which they see speculations but our practitioners' perspective is that there was not so much speculation prevalent at the time of the action and if that is true the logical answer is, one, the policy makers have taken a call that we are choosing in favor of an absolute targeted FX rate and control of inflation but taking a call that we are ready to sacrifice growth in the bargain. This action is very short-term which is what I think was the call done by the Ministry of Finance two days ago and therefore expect a restress. But if this action is not short term then the question in our mind is how does one unwind out of this without taking some hit on growth which is why at the starting point of my call I did say that we see growth slower than what we saw a quarter ago.

**Amit Premchandani**

Just a follow up on this, can we expect that RBI wants to or the ministry wants to take up the yields to some x or y level there they may come and announce for sovereign bond or overseas bond, can that be a target as per your judgment?

**Uday Kotak**

Again now looking at actual on the ground reality as we talk and we have just had a Government auction which was announced literally about half an hour before this call. I will give you two points. In the Government auction which is announced the 2026 security which RBI has sold, may be partially, they have sold at a yield of 8.23. If you compare 2026 with the ten year prior to the action on Monday it was trading at about 11 to 12 basis points higher yield compared to the ten year. Therefore the comparable benchmark which it seems the Central Bank is suggesting at which it is comfortable to sell securities for ten year paper is around 8.10 as a signal which I read from this auction.

Now prior to Tuesday if you look at the ten year on Tuesday the 2022 it was in the range of 750 to 760. So about a 50 to 60 basis points higher yield is the level at which Central Bank is comfortable to offer securities. For the rest of the security the Central Bank again it is a Rs. 12,000 crores auction has said at these yields which have been bid by the players we are not ready to supply. Therefore I read this signal as in the range of 8.10 to 8.15 ten year is where the Central Bank is comfortable seeing the 10 years sovereign yields from the earlier level of 750 to 760. So this is the first benchmark we have to read. Obviously we got to look at this auction tomorrow which interestingly is also backed by underwriting therefore if the Central Bank is not comfortable at bidding prices it can devolve the auction on to the primary dealers. So I think tomorrow the action is very critical to look at the benchmark on interest rates in India where the Central Bank is sort of guiding post the action on Tuesday.

The second important point is the FX market. FX one year forwards are trading at 7% premium. On that if you add at the rate at which banks can get one year money dollars in the international market you are talking about fully hedged rupee cost on one year deposits for banks 9% plus. So normally the CD markets in India that is certificate of deposit markets in India are trading normally at some premium to this cost base. Therefore if this cost base is 9% plus the CD market in India should trade at 25 to 50 basis points premium to this fully hedged dollar cost for banks.

Therefore if you take the CD rate benchmark as 9.25 to 9.50 this rates benchmark on Monday which is prior to the policy change was in the region of 8.25 to 8.35 which means one year bank deposit yield as things look today and obviously this is subject to change have moved up by about a 100 to 125 basis points in the last 2 or 3 days. So these are the two benchmarks as important benchmarks. The Central Bank by its action half an hour ago indicates that it is comfortable in the 8 to 8.15 range and based on the forward market calculations today the deposit markets in India on a one year papers have roughly moved up 100 basis points today versus Monday.

**Moderator**

Thank you. We have the next question from the line of Aditya Narayan from Citi. Please go ahead.

**Aditya Narayan**

I had three questions, quick one. The first thing is this 15% growth guidance, would this have been the same if this call were held last week i.e. has the RBI's action changed your outlook in terms of the growth levels? The second thing is what would be specific events or benchmarks



that you would set to make a call on whether the economy is going lower or it is picking up over the next 3 to 12 months as you see it? And the third one was your talk-down wholesale lending growth as the one that is likely to be the slowest but in this quarter you said that is where you have grown so how does that stack up or is there some punching there?

**Uday Kotak**

Aditya, on the first one we were clear that before this event our guidance was lower than the 20's and we were debating internally whether we should guide as mid to late teens or 15% to 20%, before the Tuesday event. So we are going to guide lower than the first quarter but more like 15% to 20%. We are now guiding around 15% and that is the impact of Tuesday. So that is point number one and again within 15% we are saying the consumer bank is going to grow faster than 15% because we are actually quite amazed by this consumer bank cycle and we are rubbing our eyes, there is a fundamental change in consumer behavior unlike 2008-09 whether it is personal loans, credit cards, mortgages and the consumer has held up amazingly both urban and non-urban. So it is very, very surprising and we are trying to find out reasons for that possibly there have been no major job losses till now may be there is wealth effect of gold and real estate whether this credit information bureau is working whereby the consumer is focused on his rating but that is the good news in the lending story and continues to be so. Again along with we are finding this story pretty good also in the non-urban sites particularly tractors I think that good monsoons are all we think will help our agricultural finance and the tractor finance business, so all these are the good stories.

On the wholesale, keep in mind we normally try and keep our wholesale book as low as possible end march and we just try and moderate that book end March because our priority sector's obligations are on the basis of our end March advances. So some of the rebound which you see in the first quarter on the wholesale comes out of that specific objective and we also believe that the things where we are actually de-growing and you can see it in our numbers we are de-growing in construction equipment and commercial vehicle segment particularly the heavy commercial vehicle segment where we have negative growth both year-on-year and quarter-on-quarter.

So clearly our segments we are clear what works and what doesn't work. On the wholesale side again we think there will be some demand from the quality end which will need more working capital because of a weaker rupee. So yeah absolute working capital needs may go up in some pockets where if you are comfortable with the credit we will consider it and in terms of the benchmark, pretty tough to say it is one benchmark but at this point of time in last 30 days more than ever before in my life suddenly the US 10-year is in the phase every single day.

**Moderator**

Thank you. We have the next question from the line of Anish Tawakley from Barclays. Please go ahead.

**Anish Tawakley**

I had three questions. One is on the operating costs, those has been pretty tightly controlled, employee expenses and other operating expenses. Could you talk a little bit about what you are doing there and how long you can grow at say 15% and keep this at these levels or bring it

perhaps even lower? Secondly, could you give a little more colour on what is the nature of business banking lending and how that is remaining steady despite the weakening economy? And I guess the third question was a little bit of macro which you mentioned a 5% growth rate for the economy is that sort of assuming the tightening persists for a while or would it get worse if the tightening persisted for a while?

**Uday Kotak**

I will ask Jaimin to take you through operating costs then I will ask my colleague, Manian, who is running the business banking piece in the consumer bank at the smaller end and my colleague, Narayan, who is running the business banking piece in the commercial bank which is the slightly mid-market end and then finally I will answer the third question after this.

**Jaimin Bhatt**

Let me take the cost issues. Yes, overall yes we are very focused on cost and clearly cost is a definite number so something which is a heightened area of focused for the last few years. If you look at the employee cost which we got year-on-year growth of 17% this includes the increments which is in to in April as well as the additions to the staff which we have done it has been largely in the branch- banking area. So broadly the increment plus that take you to 17% and which we think is has been reasonable.

**Anish Tawakley**

Sorry Jaimin, I am looking at employee cost growth year-on-year at 13% am I missing something, I am looking at the consolidated numbers?

**Jaimin Bhatt**

Okay consolidated would be actually even lower.

**Anish Tawakley**

Yeah it is 13% only.

**Jaimin Bhatt**

Because in some of the other areas we have not grown people. Most of the growth of the employee numbers has come in the bank and the non-bank employee numbers have not really grown during this period. If at all there has been a growth it has been at very low levels in terms of their grades. So to that extent bulk of the non-banks cost increased on employee's had been on account of increments. And increments again this year have been modest. So to that extent that is very much under control. So non-employee cost yes, over the last few years we have focused very much on group synergies and trying to bring things together so that is pretty much under focus but also at the same time just remember this period, the three months we (a) have not grown too many branches (b) we had low spent with respect to marketing and advertisement and overall if you look at the cost-of-income this period again bank's standalone looking at about 44%. To an extent helped by the growth of the other income to that extent we talked about it last year that we would like to be a number less than 50. We believe that this 44 may not clearly be absolutely something which we will be able to maintain but certainly in the 40's or may be in the higher 40's is what we would end up at.

**KVS Manian**

Yeah, I am Manian, President Consumer Banking. I will talk about the business banking question that you had. Basically if you look at the business banking, this is largely the small-to-medium size companies including individual sole proprietors and all that, they vary from sole proprietors on to small partnership firms to small private limited companies to medium

size private companies. I will put it this way that this is a huge segment overall and this is the segment that public sector banks have been financing over several years and from our point of view we are still scratching the success of this market. So by and large we can say that we make reasonably positive selection out of the market because it is a huge market and to get our kind of volumes we can really almost cherry pick credit on this market and so we have seen fairly good steady performance on this very little delinquency, reasonably good growth. So for us it has been a reasonably good segment.

**Anish Tawakley**

Is this mostly backed by LAP (Loan against Property)?

**KVS Manian**

No, so the customer segment could be similar but these are two separate products. When we say business banking part of this are kind of term loans which may be backed by securities. By the way all of this is secured business there is no unsecured business when we talk about business banking. So some of it may be secured by property, but the primary focus in this is to get the transactional accounts of customers here and therefore when we say business banking as different from the mortgages the difference is that these have transactional accounts and have accounts in the nature of cash credit and overdrafts compared to loan against property this is a pure term loans against property.

**Uday Kotak**

I will ask Narayan who heads the commercial bank to give you a perspective of this. The commercial bank handles the slightly larger ticket size in the business banking space. So that is where he comes in and your perspective.

**S Narayan**

Just to add to what Manian said again the portfolio size which we have compared to what the market has it is a small percentage. Obviously that gives an advantage of what we can pick and choose and the good part is that we get most of our references from internally from our wealth clients and our retail branches. So the quality of the clients which come to us is far better especially when it comes from the wealth part of the business. Second is that as Manian rightly said most of these clients are backed by Securities and they are spread over various businesses for example a good percentage of these clients are coming from educational institutions and this institution obviously we pick and choose in that and which are backed by good securities and almost certain cash flows. So some of them will be leased rent discounting sort of. So these are mix and match and so the great advantage is that you see here is 1) There are small percentage of the overall market. 2) Good references from our wealth client. 3) Backed by securities and most important I think we are the sole bankers there so we have full control over the cash flows.

**Uday Kotak**

The third question was on 5%, this is purely a feel, the economy may be slowing down even more but I do hope that may be second half of the year gives some wind and therefore we get back to an average of around 5%. But the important point is a policy call I mean it is possible to take a policy call that inflation and exchange management at this stage of India's cycle both economic and political may be more important than growth.

- Moderator** Thank you. We have the next question from the line of Manish Karwa from Deutsche Bank. Please go ahead.
- Manish Karwa** Just wanted to understand your margin trend going forward especially given the increase in short term rates and as we understand you would be one of the few banks who would be pretty active at the shorter end of the yield curve. So (a) does it impact our cost of fund significantly and second can we pass on the increase given a weak growth environment?
- Uday Kotak** Manish, first of all we have guided normally that our NIM's will be around 4.5% and we continue with that pretty clearly and that is something which we have maintained around or in excess of for a long period of time. We are very clear that we will do business on terms which makes sense and frankly in this market if one is not chasing everything in town there is enough pricing power particularly the mid and smaller segment. May be on large corporates the pricing power may be more limited but in other segments of the economy the key is making sure that your risk return matrix is okay. Your risk for the returns you are getting is the key. So that is the key matrix I would look at and on the liability side as Jaimin mentioned we have now 61% of our deposits and CASA are below Rs. 5 crores and we have had pretty decent growth in the below Rs. 5 crores segment on the deposit side as well and we track this very closely and we are seeing the mix change pretty significantly month-on-month where the small ticket deposits are growing and one of the things we have fortunately done in the last 6 to 12 months is that we did not drop the retail term deposit rates even when wholesale rate was 75 to 100 basis points cheaper and that strategy has worked for us and actually the proof of the pudding is eating. In this shop which you already saw I am very happy that my treasury is today a net lender in call and at almost close to zero call yesterday.
- Manish Karwa** Second one is on fees. Over the last couple of quarters our fees actually have been growing pretty fast unlike the last many quarters. Anything which has changed in the fee composition which is driving a faster growth now and what is the outlook there?
- Jaimin Bhatt** Manish, not particularly I think the fact that you are growing the banking business you have seen the third party commission and income grow over the period. This quarter many not have been very large but the whole consumer bank segments whether it is minimum balances, locker rent, all of that has gone up even the wholesale segment we have seen growth. So the fee growth in the banking business has been across board linked a lot to what the traditional businesses are doing.
- KVS Manian** Yeah, by and large what Jaimin said is right. I would just like to add that couple of areas there which include the increased enhanced focus on trade and foreign exchange as a business and therefore not only in the consumer bank but across the banks we have brought in focus on that. So that is contributing to some of the growth that you have seen there. But apart from that we have been able to get better charges, looked at our small things like locker rents and everything and I think we have upped some of those and in general the trend has been on many of those facilities we have been able to raise some charges on quite a few of them.

- Manish Karwa** And lastly just wanted to understand this one account which you highlighted probably is going under CDR and you have treated it as an NPL while I understand you guys are conservatively accounting for these things but supposedly if this account goes in to a CDR and you being a part of the CDR, can you still treat it as a n NPL in your books?
- Uday Kotak** Of course.
- Manish Karwa** You can?
- Uday Kotak** Yeah. That is our choice. The fact of the matter is banks do not like to treat it as NPA because number one the provisioning is higher and number two there is reversal of income on account of interest.
- Manish Karwa** So it is your choice to treat it as an NPL if we you choose and everyone else can treat this as a standard asset under a CDR?
- Uday Kotak** Yes.
- Manish Karwa** And you have made a full provision on this account or?
- Uday Kotak** No, as I said we have evaluated each account, looked at the security value we have against the accounts, put a haircut on the security value and then came to a number at which we are comfortable carrying the launch. And the difference between that number and the full value of the loan we have provided in the accounts.
- Moderator** Thank you. We have the next question from the line of Kunal Shah from Edelweiss. Please go ahead.
- Kunal Shah** Firstly on this growth as you mentioned like the commercial banking, in terms of the growth it would be lower than the average of 15% but if you look at the breakup it is primarily like CV and CE which is de-growing while if you look at agri and business banking there the growth in FY13 was at 30% to 35% and listening to the comments from business banking and commercial banking had, it seems like the momentum out there would continue. So in CV and CE is there like this trend of de-growing would continue and I just want to get your sense in terms of how has the stress been in this segment? You have highlighted like okay there was a stress but if you look at quarter-on-quarter may be like 3 to 4 quarters back the stress in this segment and if you look at in the last one quarter how has it been. So it has been moving up, it has been stable in this particular segment I would your perspective on that?
- S Narayan** As far as the fee in the commercial vehicle growth is concerned we have been over a period of time consistently on a month-on-month basis reducing the overall disbursement based on our overall understanding and looking at overall scenario in the mark and as of now if you sit and look at it we will be de-growing in continuously. Secondly, on your question as to how the overall portfolio has been performing, up to December yes it was not performing well. It did show some sign of improvement but again it seems to be showing some stress. So I am not

sure how it is going to show in future but having said that it is this quarter as it did show some more stress than normal may be I do not see it in the same stress in the future but I am not in a position to comment on it.

**Kunal Shah**

Considering the overall macro, may be as you mentioned the slow down is pretty significant, so what signals you would be looking at may be in retail as you mentioned is performing quite well and since home loans is now approximately 20% and we have seen most of the commodities, we had seen the correction in say most of the instruments so real estate may be what is your outlook and what signals would you look at where it would suggest that there is say some kind of a stress emerging even on the retail side or you believe like we are still two to three quarters away from say any stress in the retail segment?

**Uday Kotak**

I think on the retail segment you got to look at facts and as I said one of the things you have to look at very closely is how the job market is going and unlike 2008-09 I do not think the job market has seen major retrenchment of people so the job losses are still not something and at this stage I do not see any thing which is as dramatic happening in the economy and to a certain extend let us also be clear, a weaker rupee at some point of time is going to start helping the domestic players in some way or the other. So that is the other positive counter force which has been unleashed into the system and when that sort of changes to start helping domestic producers and people is something which one has to watch over the next two or three years. If there is no loss of confidence then a weaker rupee starts helping the domestic economy gradually. That is how we see that and at this stage therefore all that we are saying is that we are going to grow slower overall because of segmental issues particularly in the corporate infrastructure and leverage players, commercial vehicles, construction equipment and some segmental pockets where we see challenges but otherwise for the rest of the bank we will continue to build the loan engine. So on the consumer side the signals we will wait for are what is happening in the job market, is there a dramatic collapse in real estate which we do not see having said that we do see real estate prices particularly in cities like Mumbai softening by between 10% to 15% from here but there are other cities like Bangalore is holding up very well may be it is a weaker rupee and software services industry which is helping Bangalore on the real estate like home loan demand. Similarly Chennai residential low end is okay and across the country what we are seeing in real estate is the premium side going much slower not so much the mass housing at the lower end side.

**Kunal Shah**

And sir, two more questions. Firstly in terms of the Kotak Mahindra Prime, there does the outlook seem to be more stable in terms of growth of say 20% margins also sustaining out there and no major asset quality issue in that particular segment?

**Uday Kotak**

You got to create pretty clearly focus keeping in mind 75% of the business is cars and it is passenger cars therefore we think we will grow in the passenger car market lending faster than the industry growth but not dramatically so I think we can take a call our view is car industry has best growth in around middle single digit and may be we grow faster than that and then again you got to add the nominal value of the cars we think sooner or later manufacturers will

have to transmit the import price increase into the pricing of cars that was nominal. If car volume say gross 5% and then you have value which is growing a little more and we are getting some market share we see again around low to mid-teens grow in that business.

**Kunal Shah** And because of the competitive pressures may be say any pressure on margins in this particular industry?

**Uday Kotak** You look at it so far we have been actually I think that is working quite okay for us we have really got our deep franchise in to dealerships over many, many years and we have been more or less in the top 3 financiers in car business.

**Kunal Shah** One last question, does the provisioning include any kind of a general or a floating provisioning or this entire thing is specific?

**Uday Kotak** It is specific.

**Jaimin Bhatt** It will be almost standard provisioning but otherwise it is all specific.

**Uday Kotak** And the provisioning again two parts out of Rs. 168 crores. There is about a Rs. 35 crores provisioning towards investments and about Rs. 133 crores towards loans and advances.

**Kunal Shah** So this Rs. 133 crores specific excluding the standard asset on say the normal incremental loan book?

**Uday Kotak** That is correct and as I have said in the beginning of my conversation, if you take our current loan book at around Rs. 50,000 crores and depending on what growth we put to that number we are guiding full year around 60 basis points cost so our view is around Rs. 300 odd crores assuming the total hits for the year and first quarter we have taken Rs. 133 crores.

**Moderator** Thank you. We have the next question from the line of Manish Chaudhary from IDFC Securities. Please go ahead.

**Manish Chaudhary** My question is basically on the life insurance side. Now we have seen profitability increasing pretty significantly. So just wanted to understand what is the outlook there both in terms of premium top-line growth as well as the ability to keep on increasing profitability there?

**Gaurang Shah** See I think in this quarter basically the key factor for profitability which is contributed is investment income and we cut our duration somewhere in May and that has probably helped us actually in the hind side if you look at where the yields are currently. But if I remove that factor we are more or less on the trend which is currently going on. In terms of premium the industry including LIC is (-31) and industry is around (-4) which is the business premium individually APE. I think the trend may improve a little bit but I do not expect the year end, if car sale is expected to be 5 from here I think it will be more or less in the same line of the same sales. And in terms of margin, I think once the product filing and other thing happens but I do not expect that margin in terms of composition is likely to be changed materially and so

growth margin investment. So I think it is going to be another tough year and I think if interest moves up my belief is insurance never becomes a very preferred product at that point.

- Manish Chaudhary** In terms of margins you are saying that margins will come off a little or will this stay stable?
- Gaurang Shah** It will hold because margin is a composition of your traditional products, how much participating you sell, non-participating you sell. ULIP in any case is a settled product for a while and now probably third or fourth year of new regulation. One can also see the trend of persistency and other things. So I think more or less margin should hold.
- Moderator** Thank you. We have the next question from the line of Rahul Jain from Goldman Sachs. Please go ahead.
- Rahul Jain** So just three questions. First of all the scenario that you have painted, how do you see the strategy shaping up in terms of deposit growth branches and employee addition specifically in FY14?
- Uday Kotak** Let me at this stage move a little more to what we are strategically getting focused on and something which we have said in our annual report as well. We are driving three big strategic thrust, one is digital; second is affluent and third is non-urban India as a strategy and in the context of that specifically with reference to your question on branches we have said by end of this year we will be at 550 plus branches from the current level of about 445. Therefore branch growth would be roughly about a 100 odd branches in the next 9 months and that will be a combination of both urban and rural branches. We think we have got a model which enables us to handle both the urban side as well as the non-urban side effectively both from a cost and return point of view and on the deposit growth side we will grow deposits certainly faster than the rate at which the loans are growing with our savings account growth constantly clocking 40% plus we are reasonably confident for an overall deposit growth at (+25%) as a system and this over time depending on where the credit growth goes we think our credit deposit ratio consistently improves. And no stopping branch roll out, no slowing down on the big strategic thrust on digital, we have launched our mobile app for which we got very good response in the last 30 to 60 days; we are working on a pretty significant strategy on segmenting of the affluent customers between our wealth management and priority banking products and we are getting success on that including significant increases in fee income which are coming through that and some of it is reflected in the growth in fee income and non-urban India which is our Bharat Strategy which continues both whether it is tractors, agricultural divisions and that strategy is completely on track and that does not get side tracked in anyway because of what happens to the economy in the short run.
- Rahul Jain** Just a follow up on this. So with advances growth slowing down to something like 15% to 16% as you have elaborated earlier and with deposits growth continuing to grow at (+25%) the CD ratio probably will moderate to something like 88% to 90% or so and plus you continue with your branch expansion strategy so this would imply that cost -to-income ratio would again move up. So what level do you have in your mind?



- Uday Kotak** See we have actually guided you last year that one year from now we will have a cost-to-income ratio below 50% while the first quarter this year has been a little bit of an aberration because of high treasury income bringing our cost -to-income ratio to about 44%. We would continue with our guidance of being below 50%.
- Rahul Jain** Second question was if you can just help me understand our ALM gap position especially in less than 12 month category how would that look like and you earlier elaborated that you will be able to maintain margins but it would be interesting to understand our ALM gap position as we stand today?
- Uday Kotak** Yeah, I will ask my colleague Mohan to speak on this. But let me bring to your attention there are two parts of ALM. One is ALM gap from an interest rate point of view and second is an ALM gap from maturity point of view. We actually feel that if you look at the bank bulk of the book on interest rate gaps was fixed rate lending was primarily to commercial vehicles and construction equipment segment which are normally three year term loans amortizing. Those segments have been de-growing. Home loans, working capital, SME are all floating rate. So a very large percentage of our books from an interest point of view are in pretty good shape. However, on the maturity point of view and that is a reality of all banks average maturity of deposits is in the 12 to 15 month range and if you are writing a 10 year home loan floating that is an ALM which the Indian banking system lives with. And with that I will ask my colleague, Mohan Sheno, who is right now handling the most interesting of all jobs, treasury, to tell you about this.
- Mohan Sheno** This is Mohan Sheno here. On the structural liquidities gaps the first four buckets were basically RBI has given us the limits, the bank has been maintaining it well within those limits. In fact in the short-term buckets we often have positive gaps showing a very comfortable liquidity position. As far as longer buckets are concerned Uday has rightly mentioned about the issue, the floating rate loans which are longer even if we cover it with a 12 months deposit or a 18 months deposit some of the gaps are shown in the longer term buckets that we have to live with but one significant point is as we increase our retail deposits particularly deposits below Rs.1 crore that is giving us stability in the longer term buckets. So broadly this is the position.
- Uday Kotak** And we think therefore we are very well positioned from and ALM point of view on interest rates and as far as long ended home loans are concerned I do not think anybody in India has got matching funding floating rates.
- Rahul Jain** Just a follow-up on this I just got two numbers one is the proportion of CD to our total deposits, if I am not wrong it is about about 15% or there about and I understand the bulk deposits would be about something like 13% or so?
- Jaimin Bhatt** No, when I mentioned the overall 61% that is after taking CDs into account. So CDs are part of the balance 39%.

- Rahul Jain** Yeah, so 39% includes 14% of CD and 25% of bulk?
- Jaimin Bhatt** That is right.
- Rahul Jain** So how would the interest rate movement affect this position of the book that is the only concern?
- Uday Kotak** No, on that if your asset is floating then you are okay.
- Rahul Jain** So basically you will not shy in raising your interest rates to maintain the margins?
- Uday Kotak** If we feel that the current move of RBI is not temporary we have to act.
- Moderator** Thank you. We have the next question from the line of Subramaniam PS from Sundaram Mutual Fund. Please go ahead.
- Subramaniam P S** My first query was on your outlook on margins given that your savings accounts growth and CASA are pretty strong and presumably your asset growth is going to be pretty slow and your if CASA ratio significantly improves during the year do you see a positive bias to your margins for the entire year?
- Uday Kotak** Yeah, I mean as you said there are lots of moving parts. So at this stage we think 4.5% is certainly maintainable. Now if we come out doing better as we seemed to have done this quarter by point 1, point 2 we will certainly be delighted to come back to you and talk about it. And let me also highlight one other point and this is important. On the savings deposit account we offer 6% for amounts above Rs. 1 lakh that is it. If somebody gives me Rs. 100 crores in that account I still maintain six. I do not change my rates upwards on a savings account plan, full stop 6% is my cap that is it. I understand that some of the banks are having higher rates for higher amounts in saving accounts.
- Subramaniam P S** And one more data query of your total slippages how much would have been from the corporate side and how much of it would have been from the retail side?
- Uday Kotak** I think the slippages are as I said in the corporate side it is significantly this one account which we talked about and on the non-corporate side the slippage has been high in construction equipment and commercial vehicles.
- Subramaniam P S** Any number that you would want to give in terms of percentage contribution?
- Uday Kotak** No I am saying on a relative basis consumer side is almost the same level as March.
- Moderator** Participants, due to time constraint that was the last question. I would now like to hand the floor back to Mr Uday Kotak for closing comments. Over to you, sir
- Uday Kotak** I think we had a very interesting discussion. As I look at it we do believe that macro is something which we have to factor much more in our strategy than banks have done. We have



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July 18, 2013*

to watch the credit side, we have to watch the risks at the same time we think significant opportunity in growing our three key strategic initiatives digital, affluent, non-urban India and continuing with a steady trot on branch growth and focus on the retail deposit franchise through this period is how we are looking at our future. Thank you very much ladies and gentlemen.

**Moderator**

Thank you, sir. Ladies and gentlemen on behalf of Kotak Mahindra Bank that concludes this conference call. Thank you for joining us you may now disconnect your lines.