



“Kotak Mahindra Bank Limited’s Q1 FY-’15 Earnings Conference Call”

July 16, 2014



**MANAGEMENT: MR. UDAY KOTAK – MD & EXECUTIVE VICE CHAIRMAN,
MR. DIPAK GUPTA – JOINT MD,
MR. JAIMIN BHATT – PRESIDENT & GROUP CFO,
MR. KVS MANIAN –PRESIDENT, CORPORATE
BANKING,
Ms. SHANTI EKAMBARAM–PRESIDENT, CONSUMER
BANKING**

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Kotak Mahindra Bank Q1 FY-'15 Earnings Conference Call. As a reminder, all participants' line will be in the listen-only mode and there would be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Uday Kotak. Thank you. And over to you sir.

Uday Kotak: Good Evening, friends, and Welcome to the First Quarter FY-'15. First of all, in terms of the climate for business compared to the earlier quarters and the earlier year, I would like to say that the situation is looking certainly positive, including how we have seen in the last quarter. Yes, the real economy still is not running away, but there is a clear view of an improvement in pockets of the credit cycle. We are also seeing an early stage pickup in the loan cycle as well and therefore we have reported for this quarter a year-on-year loan growth of 13%, but more importantly we believe that for the current year we are looking at 20% growth in Advances. We are also seeing the overall NPL cycle something which we started mentioning to you over the last two quarters actually moderating in terms of new flows and our feeling better about the cycle, though there are still pockets which are still recovering. The other major part of our business is that if you really look at the financial sector business in two categories – Category One which is what I call as the “Saver Borrower business” or the “Spreads and Financing business”, and the second is broadly what is markets-related businesses we are seeing a significantly higher delta on the markets-related businesses in the last quarter, which currently looks reasonably robust, therefore the upward move on the banking and the financing business while it is positive the delta on the markets businesses looks quite exciting as we stand, and all in all we do believe that the outlook for the financial sector as a whole has significantly changed for the better.

Adding to this it is pertinent for us and for me to mention about the very significant budget change with reference to taxation policy on fixed income or debt mutual funds and their implications, we think there are parts of our business which have a negative impact, but significantly more other parts which have a positive impact. We think it is positive for the bank, it is negative for debt funds and NBFCs, it is positive for equities, it is positive for our broking and equity mutual funds business, it is certainly positive for life insurance because of small savers, we see significant increase in flows in deposits, it is positive for the distribution and wealth management businesses because as investors go for getting higher returns they have to go up the risk curve and which is where financial advice gets more important. Therefore, as I mentioned in pockets there is an impact but overall we are neutral-to-positive about the changes out of the budget coming on debt mutual funds. We also see the budget helping the whole cause of financial savings both in terms of income tax limits as well as the 80C limits. Therefore, significant push for savings which across financial products is good for us.

Overall, as the hurdle rate in risk free assets reduces, it enables financial intermediaries to be working with savers to give appropriate products up the risk curve without necessarily getting

excessively influenced by choices on taxation. This is how we look at this and we feel confident about the next three quarters sitting where we are and are quite positive about the outlook for the sector and our business. With that I will hand it over to my colleague – Jaimin Bhatt to take you forward.

Jaimin Bhatt:

Good Evening, friends. Thanks, Uday. Just running through the “Earnings Update” which has been mailed to you earlier today, for the quarter April-June 2014 at the consolidated level we end the period with a post-tax profit of Rs.698 crores; 11% up over last year Rs.627 crores. The overall loans book at the group level was Rs.77,000 crores, roughly about a 13% rise over the same period last year. Return on Assets at 2.2%. We end the period with book value of Rs.257 a share.

At the standalone bank level, the post-tax profit for the quarter at Rs.430 crores, loans at 56,900 crores which again is a 13% rise over same period last year. NIMs both at the bank level and the consolidated level continue to be healthy at 5%. We end this period with an overall branch tally of 614 branches, which is up from 445 branches a year ago.

The CASA ratio at 31%. Capital adequacy if I take the current quarter profits overall 19.1%, of which tier-1 stands at 18.1%.

Of the entities which contributed to the profit for this quarter, the bank at Rs.430 crores, Kotak Prime at Rs.120 crores for this quarter, Kotak Securities seeing the biggest delta from last year to this year on the back of good volumes coming in since May at least with Kotak Securities profit for this quarter at Rs.68 crores Vs Rs.31 crores same period last year. The insurance entity contributing Rs.49 crores this quarter and overall lending at Rs.698 crores. The Rs.19,000 crores of net worth spread over different companies with the bank having Rs.12,700 crores. Kotak Prime close to Rs.3,000 crores and securities at over Rs.2,000 crores and the insurance company at over Rs.1,000 crores. Of the Rs.77,000 crores of Advances across the group, about Rs.22,000 crores sitting in what we define as corporate bank, commercial bank accounting for Rs.24,000 crores, consumption related lending accounting for Rs.30,600 crores. Total assets now at Rs.126 lakhs crores and book value at Rs.257 crores as I mentioned.

Our overall advances, the growth on a year-on-year basis has come from the corporate bank which has seen 27% growth on year-on-year basis. The agriculture-related activity has seen 27% growth and the small business, personal loans, credit card division that has seen 24% growth on a Y-o-Y basis. The Commercial Vehicle/Construction Equipment continues to be on negative growth; negative number for the quarter is down to about Rs.300 crores. The book now adjusts over Rs.5,000 crores. If I take away that negative number out, the growth of advances at the consol level is 18% on year-on-year basis.

At the bank the net interest income just over Rs.1,000 crores for this quarter, the other income showing a drop over the same period last year; last year this particular quarter had significant treasury gains which had the other income line there. The overall operating expenses including the employee and other costs at Rs.736 crores. As regards provisions, while we have taken an

overall hit of Rs.73 crores on Advances which includes standard provisioning and also includes Rs.8 crores on account of unhedged foreign currency exposures in this quarter. We have on the other hand got a write-back of Rs.50 crores on investment-related activities. Last year, we have taken pain through the P&L with respect to the treasury book and some of that with the prices coming back have helped us reverse those positions. So the net-net provisions for the quarter at Rs.14 crores and post tax profit for the bank standalone at Rs.430 crores.

On the other income, as I mentioned, the treasury income was a big gain last year showed Rs.160 crores number which is down to Rs.54 crores this quarter, on the other hand the fees and services part of component of the other income is now at Rs.315 crores Vs Rs.229 crores for the same period last year.

At the segment level:

Corporate Bank contributing Rs.291 crores pre-tax, Retail Bank at Rs.216 crores and Treasury flat at Rs.140 crores compared to last year.

Bank Advances – similar growth year-on-year of 13% and if I take away the negative growth of Commercial Vehicles and Construction Equipment the growth on a year-on-year basis is 20% on advances. If we break up the Rs. 57,000 crores of Advances in the RBI definition in Retail and Corporate, about Rs.23,700 crores would be Retail and the balance at Corporate level.

On the Liability side – our overall deposits have grown on a year-on-year basis 17% – Current Account has shown growth of 13% year-on-year; Savings Deposit growth has been 37% year-on-year whereas we replace some of the high ticket certificates of deposit which has a negative growth of 40% on a year-on-year basis, we also got the Time Deposit Sweeps which has shown 33% growth for this period and deposits which are less than Rs.1 crores has shown 31% growth on a year-on-year basis.

At the bank, as I mentioned the capital adequacy continues to be pretty healthy and the bank RoA at 2.0%. We continue to have no transfers to the ARCs and no CDR participation or no conversion to such off-balance sheet item and we had a restructured loan considered standard in this particular quarter and that now stands at Rs.145 crores.

Uday Kotak:

On this restructured loan just for a clarification, it is a one account which is in the hotel sector and is essentially not a problem account, but wanting a longer tenure financing, and if we did not do it we were losing this account to a competing bank. So with that back to Jaimin.

Jaimin Bhatt:

On the liability side as I mentioned we have seen a jump in the Savings Bank account. At the CASA level we are at 31% with TD sweeps constituting another 8.3% of the overall deposit base, and if one looks at CASA and Time Deposits which are below Rs.5 crores that is now constituting 65% of our overall deposit base. This quarter we added about 1.6 lakh customer accounts.

On the consumption side, on the asset side grew at 15% on a year-on-year basis, larger growth coming from the small business, personal loans, and credit card activity. The focus continuing to remain on the SENP segment and this particular piece has seen extremely low delinquency levels now. The Commercial Bank while seen a big growth on the Agri division has been pulled down because of the negative growth on the Commercial Vehicle/Construction Equipment division resultantly the overall number flat for the year. Wholesale Bank has seen a decent increase for the quarter and on a year-on-year basis. The non-fund business on the Wholesale Bank now standing at about Rs.11,000 crores.

Kotak Prime ending this particular quarter with a post-tax profit of Rs.120 crores. Overall advances in Kotak Prime at 18,500 crores and with us constituting about Rs.13,500 crores. Net NPA numbers they are pretty contained at 0.3%, pretty healthy on capital adequacy at 17% with RoA of Prime at 2.5. Kotak Mahindra Investments which is largely dealing with loans against securities and commercial real estate in this quarter with a post-tax profit of Rs.17 crores having again a net NPA of a very small number of 0.3% and there will be capital adequacy of 20.2%.

The Life Insurance business having steady premium growth; the individual business has grown by 7%, and the agency regular business has grown 35%. On an APE basis now the bank contributes about 24% of the share of what the premium collections the insurance company does. Solvency ratios continued to be pretty healthy; we end this period with a solvency of 3.06. Securities company broking revenues saw a rise in this quarter – thanks to the volumes going up, particularly the cash volumes and this quarter the post-tax profit of Rs.68 crores as against Rs.31 crores last year. The market share this quarter at 2.9%. The Investment Bank has been involved in a few large deals for this quarter, but importantly, it is sitting on pretty significant mandates both in the ECM and the advisory side, and certainly hope to get revenues from these in the second half of the current financial year.

Overall Assets Under Management at the group level at Rs.66,500 crores with domestic mutual fund constituting over half of that, with alternate assets and the offshore funds in the insurance companies contributing the rest. At the Mutual Fund, the average AUM for this quarter has been just short of Rs.36,000 crores. The mutual fund for this quarter having a breakeven add to the profit. The alternate asset piece which is in Kotak Investment Advisor the overall corpus there at Rs.6,400 crores constituting realty funds of over Rs.4,000 crores, private equity constitute about Rs.1700 crores and small infra fund at Rs.536 crores. That has contributed about Rs.8 crores on the net tax profit for this quarter. So those were the major highlights for this quarter. We would be able to take the questions.

Moderator:

Thank you very much sir. Participants, we will now begin the question-answer session. First question from the line of Kunal Mehra from Visium. Please go ahead.

Kunal Mehra:

I will restrict myself to two questions at the outset, but let me start with the first one being a more macro development, which I would love to hear your thoughts on with a view on how the bank can benefit from it, & specifically it is the RBI announcement that came out yesterday

regarding the CRR, SLR provisions. You have always been very cautious about infra investments and one of your arguments to equity holders such as ourselves has been the mismatch of tenure. With that being addressed in some measure with the incremental cost savings because of all the CRR, SLR requirements, does this a), change how you will look at it; b), the quantum of the book that will be devoted to this? And also how it changes the dynamics between you and some of the established players in this space?

Uday Kotak:

First of all if you look at the RBI circular on infrastructure it allows banks to borrow at 7-years-and-above on bonds without requirement of CRR, SLR on incremental base adjusted for 16%, which means if today's base is 100, from today to end of this year we are entitled to borrow from the current base Rs.100 minus Rs.84 that is Rs.16 assuming that is an amortization over 7-years. From the Rs.100 whatever is the incremental we lend to infrastructure and/or mass housing is what we are entitled to do on CRR, SLR. This is similar in a way conceptually and I am not saying the response will be as good or is bad and that is something we would discuss, is similar to what they did last year with foreign deposits for banks and it was a similar kind of philosophic structure which they went with. Therefore, I must first say that this is a good thing and a recognition of the need for banks building long-term funding better match, particularly for sectors which need long-term money, namely infrastructure and mass housing. Now let us step back and ask the question what does this mean for economics. Number one, in terms give or take, banks can pay versus the deposit cost somewhere around 75 to 100 basis points more because of savings on CRR, SLR in terms of higher rate to investors. Therefore, if the bank deposit rate which again is linked to the bond market rate where you see PFC and other bonds say 7 or 10-year PFC or other bonds must be in the range of around 9.5% give or take, then banks will have to compete somewhere between 9.5% and 10% as things look today, on today interest rates in the fixed rate or floating rate I think more like fixed rate bonds for 7-years. This is what I would think will happen. The key issue in my mind is also linked to individual investors who have other alternatives. So far there were two. Going forward there is one unless tax policy changes on the other one. The competition for 7-year bonds which banks will raise at say 9.75% and 10% will be tax-free bonds, and tax free bonds currently offer rates to borrow at around 8%-odd post tax. Therefore, most individual savers and others will have an option of going and investing in tax-free bonds which will be a competition against this. The place where I think this would be an interesting instrument is for insurance companies. So insurance companies were looking for long-term assets will find the yield on bank bonds pretty attractive, and I think that is where a lot of the money will come to the banks from. Coming to the asset side, assuming on a post CRR, SLR basis our cost of funds depending on bank-to-bank, ratings, comfort of investors and others say broadly in the 9.5% to 10% range, the question then is how much are we able to incrementally add to the asset side. Because this is post CRR and without any obligation on PSL. And if we feel that there is enough juice out there in terms of infrastructure-related assets, we will certainly be able to go there, because unlike a lot of our competition we have the advantage of a significantly lower base from which we can take the call. Therefore, for us we are not carrying any historical book, and more importantly, the RBI circular requires you to effectively get funding on incremental book, you are not going to get funding on an existing book, and that is pretty clear in the guidelines. So we think it is a very

good move from a macro point of view. We will look at it because, number one it gives us funds, number two, it improves our cost of funds, and if we find the risk alright, we go out and add these loans on our balance sheet in whatever makes sense. So happy, good for macro, good opportunity, and our low base helps us in incremental addition.

Kunal Mehra: One very quick clarification on that, Uday, if possible. Just given your small base of adequate capital, would you consider buying loans from other banks as well? And the reason I ask this is I 100% agree with you that RBI is not going to be lenient on just allowing every incremental borrowing if you transfer from entity one, which is an NBFC to entity two, which is an alleged or a prospective bank. But, will they allow it if you were to buy it from one bank to another like could we take advantage of that or you think the RBI would not necessarily look kindly on that?

Uday Kotak: We have not applied our mind to that, we have been thinking more organically in terms of going out and really lending money to infrastructure. On this one the sense my team is here with me they say that they are convinced that RBI will look at it very favorably.

Kunal Mehra: Second question here, Uday, Corporate Finance, huge growth incrementally, a very substantial part of your credit growth. Is this something we can expect going forward or you have enough of a pipeline that you think it is sustainable, which is why you are also confident of your 20% average loan growth for the year or there is a lumpiness in here that you would ask us to discount?

Uday Kotak: Frankly, the pipeline is certainly better, we have an internal process of credit, so I see a lot more credit proposals coming to me than they did say last year the same time. So there is a significant increase in flow of credit proposals and it is pretty interesting. So we feel good, we feel that there is an opportunity out there in the marketplace to be able to lend sensibly and we are excited.

Kunal Mehra: Uday, you were the first to call out the slowdown in the CV and the CE sector. Where do you think we are and when if at all do you think the inventory will be absorbed, utilization will come up, rates will move up to enable us to drive growth once again in that sector?

Uday Kotak: Yes, I think we are getting there, we believe that if you look at our CV/CE portfolio as of end of June I am reasonably confident we will be higher than that by end of March.

Moderator: Thank you. Next question from Anish Tawakley from Barclays Capital. Please go ahead.

Anish Tawakley: One, just a factual question. What is the average rate on SA balances that you have at the moment?

Uday Kotak: Around 5.5%; the reason for that is it is a mix of three rates – we offer NRI deposits 4%, we offer below Rs.1 lakh 5.5% and above Rs.1 lakh 6%. So the weighted average of that for us is about 5.5%.

- Anish Tawakley:** The second question was we are now talking about asset growth or at least loan growth in the range of 20%. Could you sort of talk me through the operating leverage in the system, in the sense that if you were to grow loans at 20%, what kind of cost growth would you be comfortable with? And for if any reason you were able to accelerate loan growth faster to say 25%, how much would the flex be on the cost side?
- Uday Kotak:** Anish, all the costs are already in.
- Anish Tawakley:** That is what I was hoping to hear and so are you saying that cost growth would remain roughly at the same rate?
- Uday Kotak:** In fact we are watching the fact I understand where you come from, the fact that our cost-to-income has been a little higher, part of that is also because if you look at last year's first quarter versus the previous year's first quarter it was a 47% jump in the bank, and the main reason was it was a super normal quarter for treasury last year first quarter. So that is something which you need to keep in mind, against that the way we have continued building capacity in our system through the entire last year, we have added a branch network by 40% last year. So we have focused on building capacity which is why we are seeing that kick up in the cost. Now that a lot of our capacity is in place including on the asset side, we are certainly hopeful that operating leverage will work for us at some point of time, and we think the time is now.
- Anish Tawakley:** There is a negative profit in Kotak Mahindra Capital Company. One would have thought that the environment there is improving.
- Uday Kotak:** It is a good question. If I ask my team, they are busy collecting mandates, not getting fees yet. Mandates have to be delivered and executed. So they are putting a lot of mandates. I am given to believe in their baskets, execution of which they believe will happen as Jaimin mentioned over the second half of the financial. So that is the main reason why you are seeing what it is. Of course, Kotak Capital also has a sharing arrangement on equity capital markets with Kotak Securities which is also a part of that. Therefore, the share of fees which goes to Kotak Capital is divided on the ECM side and 100% on the advisory side.
- Moderator:** Thank you. The next question is from the line of Aditya Narayan from Citi Group. Please go ahead.
- Aditya Narayan:** My question really revolved around the fact that over the last couple of years you always had one or two key thrust areas that you really sought to expand typically on the asset side, but in other parts of the businesses also. Increasingly, that is tending to get fairly defused, you are doing things in different areas, and also your overall growth aspirations given that the market seems to be looking up is fairly middling at 18%, 20%. So, my question is are you behaving like a mature bank too early in your growth cycle? Your growth rates are not very difficult, your business spread is not very different from much larger banks. So, I think that is one question. And the other one is if there were to be an area of investment beyond the branches at this point in time, where would it predominantly focus?

Uday Kotak:

Aditya, first of all let me say that if you look at the way we have built our pieces, it puts us in a very unique position today. We are in the entire financial ecosystem and something which I think the latest budget highlighted more blatantly than anything else. The Indian system from time-to-time has a significant ability to make impact on a vertical A, B, or C within the financial ecosystem. Therefore, it was absolutely key for us to be getting our arms around making sure that we are in the ecosystem in a manner where impact on some part of the system gives us complete broader insulation in totality. That strategy therefore if there is a change in tax policy on debt funds, irrespective of the pain on particular verticals we in totality not only withstood but also have the ability of leveraging the strength of our system, and this is the challenge for Indian policy where from time to time tinkering in different parts of the system which significantly impact business of one player versus the other. From the point of view of our core business model we now have the ability as an ecosystem within Kotak to be able to take advantage of whatever gets thrown at us from expected policy. So that is point #1. Point #2 is we are pretty clear that there are two clear streams of income in our business – one stream of income from what we call as the saver borrower business, which is spread, lending, deposit taking, what I would call as a banking business. Within that we certainly see opportunity as we talk in two clear segments which historically we have been cautious for in the last few years – Number one is ‘Distress.’ The problem we are facing with distress is that there is mispricing of the sale price on the banks disposing these assets. So when we get right pricing on that we are very hungry to be putting money to work on the distress side – and the second, something which we have waited for quite a while and I am not regretting at all till now, is the entire lending in the infrastructure side. And we have internally got our arms around that if there is an opportunity for risks which are appropriate for us to take we will grow that piece. Therefore, within the spreads or the saver borrower business we see some of these opportunities now actually materializing over the next 12 months. Moving from the saver borrower business to the other big part which has really got hammered in India in the last six years from 2008 to 2014 is what I call as the ‘Issuer Investor’ business in whatever shape or form. Therefore, whether it is brokerage, whether it is investment banking, whether it is equity mutual funds, whether it is life insurance investment or the whole area, anything which was concerning markets dealing with investors, debt capital markets or investors and issuers took a significant back seat over the last six years. We see that business coming back significantly over the next few years compared to the last six years. And the delta relative to where we are on that we think is significant. Frankly, the fact that we are in the entire ecosystem is a good place to be. How we sort of leverage that is something which we have to sort of do ourselves to prove both to ourselves as management and team and to the marketplace over the next few months and years.

Moderator:

Thank you. The next question is from the line of Parag Jariwala from Macquarie Group. Please go ahead.

Parag Jariwala:

Jaimin said that you provided credit cost was higher during the quarter mainly because of this unhedged FOREX exposure. So can you explain that in a bit detail, I mean, what basis? And secondly, what was the impact due to this on the Tier-1 capital as well?

- Jaimin Bhatt:** Obviously, it is not a very large number. For this quarter as I explained we have taken a hit of Rs.8 crores for this period. It is basically in terms of identifying what this loss would be, basically it is all our corporate borrowers and what is their unhedged foreign currency exposure, taking that data and providing on that and there is a very well-defined formula which RBI has gone with which is defining the loss comparing it with the number and then providing on a same basis. So that number as per our estimates as of June came to somewhere around Rs.32 crores which is where we provided Rs.8 crores this quarter. So that is broadly built into the provision for the advances which we have got these funds, not a large amount, maybe if we end up collecting more data, maybe we may get some benefit as we go forward. As regards capital, our risk weight assets on account of this goes up by slightly over Rs.500 crores on account of this one, a very small impact to on our capital adequacy.
- Moderator:** Thank you. The next question is from the line of Karthik V from Espirito Santo. Please go ahead.
- Karthik V:** Just quickly on the Housing Loan with the new regulations coming in, just wanted to understand your thoughts how that will change the way you look at the Housing Loan business?
- Shanti Ekambaram:** The guidelines have just come out and as you have seen amount is 60 lakhs loan for the city and 40 lakhs for others. I think in the cities it would be difficult to meet the target. So I think the opportunities will be really in the peripheral part of the cities and maybe some part of the inner India. We are mapping the opportunity right now since it got released yesterday and we will be rolling out the strategy during this quarter.
- Karthik V:** If you can give us more details about the current outstanding book in terms of the ticket sizes, maybe a breakup between LAP and the Retail Housing that will be very useful?
- Jaimin Bhatt:** If you look at my overall mortgage book, currently, LAP would be almost 50-50 situation of between LAP and Home Loans.
- Uday Kotak:** But Rs.12,000 crores total 50-50.
- Karthik V:** Just quickly, if I look at the borrowings as a proportion of the total funding has come down meaningfully when I look at in the last 2-2.5 years. Can you explain what is the thought process behind this shortfall and how do you look at going forward especially on the funding profile?
- Uday Kotak:** I think it is back to a discussion which we have shared with you over the last 18-24 months that we as a bank are very focused on building stable and low cost liability base. Our proportion of wholesale funding was significantly higher two years ago and we took a conscious call that we want to diversify. And both borrowings as well as certificates of deposits are examples of wholesale funding. We have gone after it relentless over the last two years and focused on number one, retail deposit, and number two, savings accounts in addition to current account. Our current account maybe more volatile, but retail deposits and savings accounts has been the

bulk of our focus. As you can see our Loan growth YoY is 13%. Our growth in term deposits below Rs.1 crore is 31%. Our growth in savings account is 37%. So we are building significant capacity of a low and stable liability base to be able to manage what we think will be growth on the asset side which will come sooner rather than later. And that is why as a part of our overall mix of liability you will see a drop both in our borrowings number as well as our certificate of deposit number.

Karthik V: Is it fair to assume that going forward this might sustain at the current levels as a proportion of the total funding?

Uday Kotak: We are continuing our growth rate both on Retail, TD, and Savings relentlessly. So that will continue. And we do not want to reduce our pace on that, because number one, it is not costing us more money in terms of marginal cost, number two, the fixed costs are already in, we just got to sweat it more.

Moderator: Thank you. The next question is from the line of Jiten Doshi from Enam Asset. Please go ahead.

Jiten Doshi: Congratulations on being recipient of the E & Y world entrepreneur award for the year 2013, great pride for all of us, is as your shareholder. A couple of questions; one, we are at the cusp of a very important event that has happened with the new government with a clear mandate. Where do you visualize Kotak Mahindra Bank in the next five years? What is your longer-term vision – do you think we can grow at a rate which is much faster than the system?

Uday Kotak: Jiten, first of all thank you for your good wishes, I feel honored as an Indian to get this recognition on global stage & it did feel good from an Indian prospects. On the point which you mentioned about, I think my personal view is that the next five years would see average GDP growth of 6.5% plus. We may hopefully end the period closer to rate somewhere between 7% and 8% giving us an average of somewhere 6.5% plus. I hope it gets closer to 7%, but I am saying base case 6.5% average for the next five years. And then if you take average inflation over the next five years at say around 6-7%, you are talking roughly about nominal GDP growth average over next five years, and if I can pick a number, let me say 14%. On a 14% growth rate, as I mentioned we have got really two significant engines – one is what I call as the saver borrower business and the second is the markets business which is the issuer investor business. Depending on how things shape up we see on the more traditional saver borrower business an ability & if we play it right and we manage our risk well, we have our capacity in place, capture opportunity to grow between 1.5-2x the nominal GDP over the next five years which is if I take a midpoint of 21-28% we do think that it is feasible for us to look at 25% growth on the pure saver borrower business. I think the delta on the markets business can be significantly higher. You have had a situation where a lot of the businesses connected with markets both equities, structured products, alternate assets, PE, whole host of products out there which prematurely lost their color between 2008 and 2014 can come back in different shapes and forms. And on that business therefore particularly of a low base in 2014 the delta on

percentage growth can be even higher. So, that is where I stand and I think it is easy for me to give you a five-year prediction but do not hold me to it every quarter.

Jiten Doshi: So, I can easily see the entire enterprise going up by about 3x in five years if I compound it at 25% or maybe in between if there is something inorganic, your PAT of about Rs.2,500 crores can hit about Rs.10,000 crores should be your aspiration because as you spell out we are in a great period, which we never ever witnessed before?

Uday Kotak: As they say 'God Willing' and hopefully 'Acche Din Aayenge and Rahenge'.

Jiten Doshi: And Uday, these are your last few years now to really demonstrate that you will be able to do something inorganic not more out of choice, but out of compulsion. You have gone through a very painful period of some things that you have never done in the last 25 years is selling your own shares of Kotak Mahindra Bank, which I do not think if somebody would not have forced you to you would have ever done. So, what is now really the thought process in terms of the dilution and where you are heading? And the other painful part is, yes, nice part to be in is that we are having a lot of excess capital, which is not actually getting deployed into the lending side. So looking at this perspective, how do you see this in the next 2-3 years panning out for us?

Uday Kotak: I would like to believe that this is something which is certainly a feasibility where we continue to grow institution I do not have a gun on my head in terms of how we develop the institution organically/inorganically, hopefully, regulator also recognizing that very low promoter skin in the game is not a good thing. So, a combination of factors.

Jiten Doshi: And lastly, Uday, how do you see the landscape with this new government actually where there is a lot of focus on improving the efficiency of public sector banks and creating a few large banks and how do you see the whole banking environment really panning out and where do you see us within that whole space?

Uday Kotak: This is my honest view it is easier to manage public sector companies which do not have millions of employees. Therefore, restructuring of some of the other large PSU undertaking and improving governance in some of them is easier than to try and change culture and make it a service culture for millions of employees in banks. And that is a far more difficult challenge than changing the structure and governance of some of the manufacturing or infrastructure-oriented PSU undertaking. I frankly feel it is going to be much tougher on PSU banks than what is bargained or expected by the government.

Moderator: Thank you. The next question is from the line of Rahul Jain from Goldman Sachs. Please go ahead.

Rahul Jain: A couple of questions; first, did you guys acquire any stressed portfolio in this quarter?

- Uday Kotak:** A very small. The problem with stress portfolio is that when you have 95/5 schemes, we may have done something in our ARC on that, minority shareholders 49%, but that is the ARC which is at independent but we would love to buy stress portfolios in cash at fair value.
- Rahul Jain:** That really is not happening. So what would be your outstanding stress portfolio as we speak today?
- Uday Kotak:** I think we have given you a sense and something which I mentioned at the last quarter and we continue with that. In fact, there has not been much monetization of that portfolio in the first quarter, it is this first quarter stress portfolio monetization is less than even last year's first quarter. But we had given an indication that we believe that the value in that portfolio net of our current capital we think is between Rs.1800 crores to Rs.2000 crores. So we stick to that. If at all we think it can get better if economy gets better.
- Rahul Jain:** On fee income, what really was the main driver for fee income in this quarter and can we really sustain those driver?
- Jaimin Bhatt:** It has been all around, I do not think there is anything specific. As we mentioned earlier, we will be focused on client rate activity which has been especially on the foreign exchange side. The third-party distribution number is pretty improved this time around specifically on the normal business side which is both the retail side on processing fees and the wholesale side we have actually collected decent amount of fees there. So all of those have kicked in somewhere or the other. So, the biggest delta would be the FX client and the third-party distribution.
- Uday Kotak:** Manian, do you want to talk a little bit on FX client how you are building that?
- KVS Manian:** FX client we are seeing good flows for both FX client as well as the derivative side; derivative side earlier we had gone slow on that, but now we have reviewed our products on what can be offered safely for both our clients and us and we have introduced some of those products which is showing a good traction, also focusing on building a foreign currency loan book which will also add to FOREX flows and income from that. So we are seeing good traction on that. We will see even better traction going forward on that.
- Rahul Jain:** Just on the similar question, is it possible to really know what percentage of our income is coming from our retail clients and what percentage is from corporate clients, is this in the same proportion as the loan book or there is a difference between the skew?
- Jaimin Bhatt:** On the FX side or you are talking about overall?
- Rahul Jain:** Overall fee income part.
- Jaimin Bhatt:** It would not be very different.
- Uday Kotak:** But I think Retail fees are larger than Wholesale.

- Rahul Jain:** On this loan loss provision, so we provided about Rs.66 crores in this quarter, of which you said Rs.8 crores were towards unhedged FOREX exposure of your corporate clients. Remaining Rs.58 crores would be mainly towards the loan book or was there any other element involved in this?
- Jaimin Bhatt:** That is a loan book itself which includes both on account of NPAs and standard provision.
- Moderator:** Thank you. The next question is from the line of Anish Tawakley from Barclays. Please go ahead.
- Anish Tawakley:** Actually it is really a question on LAP books, because a lot of people are reporting it across the industry. Do you have visibility on what the end use of these LAP funds are for? People have LAP books in the range of Rs.70 lakhs to Rs.1 crore ticket sizes. What is the end use people are putting these funds for and in an environment where the economy is so weak, are the people borrowing against their houses to invest in businesses?
- Dipak Gupta:** Anish, most of it is basically working capital and in a large number of cases what we are finding is it is basically replacement from one bank to another, either because you are willing to give slightly higher or at a lower rate or slightly higher disburse. So it is one of these two. But ultimately going for working capital.
- Anish Tawakley:** So, these would have earlier been like sort of working capital loans without property backing with SMEs?
- Dipak Gupta:** No-no, property may have been there with some other banker, maybe you are willing to give him 10%, 20% more because of property appreciation or a different LTV and maybe at a slightly different rate. So, a lot of that is basically replacement from one bank to another bank, but bulk of it end use wise it is essentially working capital.
- Kunal:** This is Kunal over here. You have touched upon this debt fund which has been there in the budget. So just want to get your thoughts as to how we are preparing ourselves in terms of say transitioning through this because we have like 90% in the debt fund and 10% on the equity side, so be it in terms of product introduction or say on the revenue side or the cost side?
- Uday Kotak:** First of all, as an analyst, you should be also keeping in mind that the mutual fund produced no earning for the quarter. Therefore, our quarterly earnings are with zero earning from the mutual fund. So that should give you comfort that whatever happens there it cannot get worse. Keeping that aside obviously, I think there is a move by the debt fund industry to make a representation to the government that grandfather ways are cannot be a retrospective thing, the question is retrospective what is it defined as, is it defined as retrospective, it should not be retrospective from the point of view of maturity or it should not be retrospective from the point of view of investment. The second one is far trickier. Retrospective from the date of maturity I think it is easier for the government to deal, which is maturity is before 10th of July, I think it is far easier. Let me ask you a question on this retrospective from the date of investment, god forbid for all

of us, but if say in the future sometime down the road government thought about introducing capital gains tax on sale of equities. How can they make it retrospective from the date of investment?

Kunal:

It has to be say with respect to maturity or say the time when we are

Uday Kotak:

So that is the question. And if they say prospective from the date of maturity, assuming they say maturity from April 1, 2015, can you imagine what will happen? Every investor in the debt fund will run out between now and March '15 to take advantage of the tax breaks, because from April 1 it is not available. So that is also actually a moral hazard if you do it that way. Therefore, it is pretty tricky, how the government thinks about addressing and how does it address the current point which is that we should not try and have retrospective legislation. So one has to wait and watch. My sense is that I think even if some concession comes from the government, there will be an issue for the size of this debt mutual fund industry. Whether the impact is 25% or higher, it is something which needs to be seen, but whether it is Rs.2 lakh crores out of Rs.8 lakh crores or Rs.3 lakh crores out of Rs.8 lakh crores or Rs.4 lakh crores, one has to wait and see in terms of the final outcome, but it is a very significant move which on the one hand hurts debt mutual funds and effectively what was happening is let us take a bank deposit. What in practice was happening on a bank deposit you are getting 9%, paying 3% tax, post tax return was 6%. Instead of putting that money in a bank deposit, you put it into FMP and that FMP invested only in bank deposits post tax 6% was becoming post tax 9%. So there was 300 basis points subsidy which is coming from the government. That is the key issue in front of us and that is something which needs to find an equilibrium and let us see how it goes.

Moderator:

Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the floor to Mr. Uday Kotak for closing comments.

Uday Kotak:

Thank you very much and appreciate the questions and the discussions. I do feel that we are in for interesting times – the financial sector will be the harbinger for India's accelerating growth, I am a true believer that India over the next five years will steadily accelerate growth year-after-year and the financial sector should be able to grow reasonably faster than the nominal GDP of the country. We are hopeful of being able to keep our pace on the financing business at a growth rate which is 1.5-2x nominal GDP, and on the other businesses we think particularly markets related businesses, the delta is higher. So, this is a view over the next few years. We have to see how things shape up. Easier to make a judgment call on five years, more difficult to tell you what happens to the monsoon in the next one week. Thank you very much, ladies and gentlemen.

Moderator:

Thank you sir. On behalf of Kotak Mahindra Bank that concludes this conference call. Thank you for joining us. You may now disconnect your lines.