“Kotak Mahindra Bank Q2 FY13 Earnings Conference Call”

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Moderator Good evening ladies and gentlemen and welcome to the Kotak Mahindra Bank Q2 FY13 Earnings Conference Call. As a reminder, for the duration of this conference, all participants' lines will be in the listen-only mode, and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal an operator by pressing "*" followed by "0" on your touchtone phone. I would now like to hand over the conference to Mr. Uday Kotak. Thank you and over to you sir.

Uday Kotak Good Evening, friends and welcome to our second quarter. I have got my team here with me and just to give you a few highlights about how we see our business and also some of the situations with reference to where we are today. On the first important fact is we are happy to say that the consolidated bank's balance sheet size has crossed 1 lakh crores and we are really happy at that. So as a group on a consolidated basis our total balance sheet now is in excess of 100,000 crores, exactly about 102,000 crores. The Savings Account growth on a steady basis at an average cost of funds on the Savings Account at 5.5% approximately. We have seen a Year-on-Year growth of 66%. And I think the average cost of funds of the Savings Account is important because looking at the ticket size of the Savings Account since the focus is on getting the operating transaction accounts of customers there is a significant fixed cost associated with these accounts and these are not money market accounts and therefore at an average cost of 5.5% which is comparable to most of our other banks who are at 4%. We still feel is a reasonable price to pay for getting a significant growth in the Savings deposit base. So 66% YoY growth in the Savings Account is something which we feel good about.

As an addition, we have also seen significant growth in our Sweep deposit accounts of more than 50% YoY which is again reflective of getting significantly more customer acquisitions and getting for our customers a good deal. The Sweep deposit in terms of returns to the bank is significantly cheaper than the term deposit and a little higher than Savings Deposit cost. The area where we are actually having more challenges is on a relative basis YoY current account growth where we have grown only 10% compared to last year. So all in all the deposit story and the absolute deposit growth also is pretty good. The deposit story and the building of the longer-term customer franchise is looking pretty good. We are roughly adding 50,000 new customers on the liability side, that is the deposit side every month and that is continuing at a good pace. In addition to the fact that we think we are making some progress on getting the ticket sizes also better as we go into the future.

Moving on to the advances side, we are running, as we mentioned in the last quarter at a growth rate 20% plus. So at the bank standalone about 22% consolidated little lower because Car loans are growing at about 19%. But overall, 20% plus growth rate and we see that sustaining through this year.

On the provisioning side you will see a significant increase in the provisioning number for this quarter. One of it is what we consider as one-off because we have acquired a distress asset portfolio from another financial institution and as per the RBI norms and our accounting policies we had to write, fully provide the purchase consideration we have paid and I think I need to explain this to you. We have bought this portfolio in this quarter at 49 crores, on which during the quarter we have collected 7 crores and we have had to provide the full amount through our P&L which is what we have done and that is a provisioning hit which we have taken through this quarter, we believe the portfolio acquisition is value-accretive to the firm overtime.

On the other provisioning side there continues to be softness at least in the second quarter, something which I had shared with you in the first quarter in construction equipment and commercial vehicles, particularly where there is a linkage to infrastructure companies. So wherever we have got construction companies and contractors which are connected with some of the larger infrastructure companies or commercial or vehicles contracts which are again connected with infrastructure companies or mining companies, we are seeing a spottiness in that which has continued through the second quarter. But other than that including on the corporate side, we have not seen any further deterioration in the asset quality across the loan portfolio. That I would say are the broad highlights of what I see as our second quarter numbers. And at this stage we feel pretty comfortable overall. There is also something which I must talk about, our subsidiaries we saw a little bit of come back in the capital markets happen in September and we saw some of that wind help us in Kotak Securities which is very closely linked to what happens almost on a daily wage basis if I can use the phrase in the equity markets and that is also reflecting in our Kotak Securities numbers to a certain extent, and which is why our subsidiaries actually have had a good quarter. So, all in all that is where we are and I will ask my colleague, Jaimin Bhatt to take you through the specifics.

Jaimin Bhatt Thanks, Uday. You have got the earnings update as well as the press tables which we circulated a while ago earlier today. At the bank's standalone level, we clocked a post tax profit of 280 crores for this quarter as against 260 crores for the same period last year. The loan book in the bank has grown by 22% during the last one year and we are now at 45,400 crores. We continue to have the capital adequacy at reasonably high numbers. Our capital adequacy as of September overall is at 16.4% with Tier I at 14.9%. For this I have included the profits for the half year period. NPAs again reasonably under control. Our net NPA other than stressed assets at 0.73% as against 0.78% a quarter ago. Our restructured advances continue to be extremely low. Our restructured advances which we consider standard are down to just 8 crores which is 0.02% of our advances. CASA continues to grow; overall CASA growth in the last 12 months has been 32% where Savings, as Uday mentioned, has grown from about 3500 crores a year ago to just short of 6000 crores now, a growth of 66% in the 12 month period.

On a consolidated basis the post-tax profit for this quarter at 502 crores; loan growth at the consolidated level at 21% with 61,000 crores as the advances there, slightly slower growth in the loans at the consolidated level compared to the bank comes from the Car book which is growing at about 19% YoY. NPAs again at the consol level contained at 0.61%. Net Interest Margin at 4.7% and Return on Assets at 2%. As Uday mentioned, as of September the overall consolidated balance sheet now crosses the 1 lakh crore mark.

As regards the breakup of the advances during this 12-month period 61,200 crores large growth on a YoY basis if you look at comes both from the commercial segment and the consumer segment. The Agri business showing the highest YoY growth at about 50%. Of course, for this quarter we have seen the corporate book grow decently also.

As regards entity wise profits during the quarter other than the bank, large contributions came from Kotak Mahindra Prime which had a post tax profit of 114 crores compared to 90 crores a year ago. Kotak Securities, as Uday mentioned, on the back of the fact that September shows higher volumes, we clocked 40 crores post tax profit. Kotak Life Insurance where we have a 74% stake had 47 crores profit for this quarter. So net-net we end this period with 502 crores post tax profit for the quarter. Asset book overall growing by 22% and we end with a net worth of just short of 14,000 crores.

As regards to the financing business itself, 61,000 crores of advances broadly breaken up into 24,000 crores coming from the consumer bank, about 21,000 crores from the commercial bank and about 16,000 crores from the corporate bank itself. The NII during the period has seen a 23% jump and for this quarter we had 958 crores NII at the consolidated level and post tax profit from the financing business at 410 crores.

At the bank standalone level, as I mentioned, the capital adequacy and the net NPAs continue to be showing healthy numbers. Net interest income at the bank level is 758 crores, about 25% rise from the same period last year.

If I look at the provisioning coverage as per the RBI circular we would be at 65%. The bank standalone P&L, NII growth at 25%, overall income grew for the quarter at 2000 crores which is about 23% rise from last year. At operating profit levels that is before the provisions we had a profit of 482 crores versus 380 crores last year which is about 27% rise. Uday talked about the fact that we had this one portfolio where we have taken a 42 crores hit to the P&L for this quarter. So that is included in the overall provision of 71 crores which we have taken this quarter. That portfolios of the entire amount of 42 crores also shows up in our gross NPA numbers. Due to that hit the post tax profit for the bank is at 280 crores for this quarter.

Kind of just explain some of the NPA provisioning highlights which we follow, one of these, the 42 crores hit which we took this year is apart from the RBI guidance also coming from our own policy which we take a 100% write-off on the NPA like what we have got. We continue to have situation where cheques on hand which bounces by the 7th of the following month, we would treat that as an NPA for the previous month itself and we upgrade a NPA to standard category only when all the dues of the NPA party are recovered. So if somebody has three installments overdue and has become a NPA till the time he pays up all the three installments and he clears himself of all his arrears it is only then we consider him standard, till then he continues to remain a NPA in our books.

On the segment wise numbers, you will find the Retail Bank taking a dip and for the quarter showing 121 crores, that is largely also coming due to the 42 crores hit which has hit the Retail Banking segment as this particular portfolio which we acquired comprised retail assets largely.

At the bank level, Advances have grown 22%, marginally higher than what we saw at the consolidated level. If you look at the classification of the RBI way which is anything over 5 crores goes as Corporate, the 45,000 crores at the bank level would comprise 23,000 in the Corporate segment and just short of 22,000 in the retail segment.

The bank balance sheet; effectively deposits have grown overall. Overall CASA has seen a 32% growth; Sweep again in addition to Savings has seen 50% growth on a Year-on-Year basis and we kind of judiciously use the mix of deposits and borrowings and the overall bank balance sheet stands at 73,000 crores this quarter.

At the Consumer Bank, we end this quarter with 389 branches. We continue to go for our target of 500 branches by the next calendar year and we are on track to achieve that. 866 ATMs as of end of this period. We have added about 1.4 lakh customer accounts during this period and continue to focus on the affluent segment of the market.

On the Consumer Bank Asset side, which largely comprises lending for the consumption related areas, primarily passenger cars, mortgages, personal loans, credit cards and the like, the growth has been about 24% on a Year-on-Year basis with mortgages showing a larger growth there. We continue to focus on doing cross-sell through our branches and focus on the SEMP segment of the market there.

The Commercial Bank which is what focuses on what we would call the 'Bharat Path' the semi-urban and the rural segment, largely comprising construction equipment, commercial vehicles, our agriculture related lending, capital markets and business banking has had over a 30% growth on a Year-on-Year basis largely helped by the Agri growth which has been almost 50% on a Year-on-Year basis.

The Wholesale Bank continues to focus on the working capital related areas and focused on the transaction banking. The opening up of the Government business throws up another opportunity for us. Overall, the Wholesale Bank Advances stand at close to 16,000 crores at the end of the quarter.

At Kotak Prime, as I mentioned, for the quarter we have recorded a profit of 114 crores, roughly about 26% higher than the same period last year. Passenger Car continues to have a large part of the advances based there; about 77% of the overall advances of 15,000 crores in Kotak Prime comprise Passenger Cars. NPA numbers ,they are pretty contained at 0.2% and Prime has a capital adequacy of 15.8%.

The Life Insurance business for the quarter recorded a 47 crores profit after tax. I must mention that while last year the insurance entity was not paying taxes; it has now become a tax paying company from the current year. The AUM growth of policyholders' funds has grown about 20% on a Year-on-Year basis and the solvency ratio remains reasonably healthy at 2.9.

Kotak Securities, as we mentioned, decent quarter this period. Post tax profit of 40 crores. We had a rise in the volumes during this period and to that extent the market volume in the month of September has helped the entity itself.

Kotak Mahindra Capital Company has been involved in a few of the institutional placement programs, was also advising for the acquisition of Hutchison Global Services to Tech Mahindra. Also involved in the Shriram issue of the non-convertible debentures and for this quarter ended with a profit of 4 crores for the period.

Our overall assets under management across the group stands at about 56,000 crores as of September end. The domestic mutual fund especially the debt segment has seen a growth in this period about 2000 crores as also the international funds which has again seen a growth of close to 2000 crores. In fact, the 2000 crores of rise in the domestic mutual fund has also brought with it some distribution expenses, resulting into the mutual fund entity asset management company incurring a small loss for this quarter.

The alternate asset fees, the assets under management continue to be just short of 5000 crores and this quarter has seen that entity record a post tax profit of 9 crores. That is broadly the highlights for the quarter. We open for the questions.

Moderator Thank you. Participants, we will now begin the question-and-answer session. The first question is from the line of Manish Ostwal from KR Choksey Shares & Securities. Please go ahead.

Manish Ostwal My first question is your CASA ratio. After the deregulation of Savings Bank rate, bank had witnessed strong acceleration in CASA per quarter basis till Q4FY12 and the last two quarters have seen a slowdown in the Savings Bank deposit addition per quarter. So could you throw some light whether the balances in new accounts are lower on an average because the customer acquisition number is 50,000 per month. So what is going on there?

K V S Manian This is in two parts; one is immediately after the deregulation we also got an upside from our existing base which came in the first couple of quarters, we saw the upsurge in the existing balances going up. Subsequently it is only the new accounts which are adding to the base. We continue to get a reasonable traction as you saw, the numbers are close to about 50,000 a month and the quality remains the same. We have not seen any deterioration in the quality per se.

Uday Kotak Just to add what Manian is saying we are focused on making more progress than what we have on deepening in the existing customer base which we can do, we are focused on doing a better job on that.

Manish Ostwal And secondly, last few quarters, the non-interest income of standalone bank has been modest considering the reasonable growth in the non-funded exposure also? And secondly, what is helping the core retail fee income because some of the Retail Banks have shown some recovery in the third party distribution segment also. So what is happening there?

K V S Manian The distribution fee per se on the Retail Bank continues to maintain the trajectory. We have not seen any deterioration; in fact, we are seeing it improve over the last year and usually there is always a weightage of this happening in the second half; second half is significantly better. So we think on a Year-on-Year basis we will still grow reasonably well on the Retail core fee.

Manish Ostwal Lastly, these two entities, Kotak Prime, total income increased by 8% QoQ, PAT increased by 21.3%. So either the provision or operating expenses saving there?

Jaimin Bhatt Some of these are fee related income where effectively for the income, there is very little expense going there. In fact, almost all of the income which is coming there would go into the bottom-line.

Manish Ostwal And nothing is one-off in Kotak Securities trading gains?

Jaimin Bhatt There is nothing there. Also, I must add that in Prime over a period you have seen this quarter some improvement..

Manish Ostwal The Kotak Securities reported a very strong total income. So is there any one-off in that line item?

Narayanan S.A. If you look at substantially it is coming out of the increase in the brokerage income in the month of September. We had seen a good increase in our cash market volumes and especially delivery. That is what has contributed substantial to that. But having said that we also have a small soft segment which is also contributing to it, but major one is come for the booking 23.30 income.

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

Aditya Narayanan One is on cost. There is a kind of underlying theme where cost seem to be reasonably under control and you see that I think both in Securities and in Kotak Prime. So some sense of specifics that might be happening there and your expectation of the underlying trend. That is one bit. The second is on a broader perspective, you normally open with more perspective than you have opened with this time at a broader level. So some sense on that and specifically the context of the fact that you mentioned the need for quick reforms the last time around. So how do you see things as they have panned out, secondly, on that potential implications for your own growth targets? Just on that if you were to look up from an asset growth perspective do you see more challenges on the asset side or on the liability side to grow?

Uday Kotak I will come to the second point first because I think that is something which as you rightly said I normally give a little more on that when we start. On the overall bigger picture between last quarter and this quarter we had a significant change in government posture and action compared to where we were in July. So, to that extent if you recollect in the last quarter we were worried and we were hoping that things will move faster. To that I think clearly things have moved in the last quarter which is significantly a plus. Therefore, on the big picture, I divide the perspective into three parts. First, was India at a potential risk of being in a crisis zone in the short run? My answer is yes. Number two, has the mood got better than what it was a quarter ago? The answer is yes. Have the macro fundamentals dramatically changed? The answer is no. And on the third one, you then come to the question how do you fundamentally improve macro economy? One is a lot of hard work which is bottom up, saying that no, I need to get the competitiveness and the productivity of the Indian economy up, I need to remove bottlenecks whether it is infrastructure, whether it is high attrition, whether it is high real estate cost, all the fundamental macro things which are affecting competitiveness and productivity of the Indian economy and that is where fundamental changes required only then over time we will see a competitive Current Account and a lower fiscal deficit through bottom up fundamental macro economy building. The second part is, I think that is a long walk, it is pretty tough, it is going to take time and in some cases whether we can do it at all, then you need quick fix. So, the biggest and the easiest way to do the quick fix is top-down capital market driven recovery, make sure that you cannot fix your Current Account in the short run, therefore we need to work on making sure the flows work, portfolio comes in and you have a Balance of Payments under control, do things which spur a market related recovery rather than bottom of fundamental building. As I look at it strategically at this point of time, India is going down path number two. Path number one is a lot more hard work. Having said that it is better to go down that path than have a short-term problem on hand. But while we go down the path two, we have to fix path one over time and therefore on the macroeconomic fundamentals, whether it is a Current Account of the fiscal I think the challenges continue. And I do hope that this capital market led recovery has legs. The question in my mind is does this recovery enable leverage corporate sector. Get out of its problems, the way it did in 2009. I am not clear about that whether it will solve the problem of leverage companies. But if the problem of leverage companies does not get solved, if leverage financial institutions lending to those leverage companies, if there is enough capital that may give a temporary breather to leverage companies in the hope that sometime in the future it will get sorted out. So, I think that is the game which seems to be playing out right now. The question is whether it solves the problem? My sense is it makes it a little better but jury is still out whether leverage companies in India, particularly the concentrated highly leverage companies, we have seen one more downgrade in the last 24 hours to decategory four notches below of a very large company. Whether the leverage companies will be able to get money either through direct capital or through derivative capital from financial institutions. And therefore our view is we are happy to build our loan base on what we are comfortable with and if that takes us to a growth rate of 20%, 25%, 28%, 30% ,we will do it but we at this stage are not taking the call that open up the box and just do go out and get assets in the belief that happy days are here again. So this is trying to answer your first question on the broader perspective and I do feel that things have certainly got better both on the mood as well as the fact that India is probably staved off a crisis and the same thing has happened to Europe. I think Europe problems have not gone, but immediate crisis seems to have been postponed. But have the fundamentals got dramatically better? Answer is a clear no. And therefore grow, build but do not throw caution to the wind. I hope that gives you a perspective of where I stand today. And on the first point which is cost, frankly, I think -- this is something I am sharing with all of you, our internal discussions, and our subsidiaries in particular since they have been living through tougher times for quite some time have done a much better job on cost. But we are pretty clear we will tighten the fat, we do not want to hit muscle or bone in any of our businesses. Therefore, while they have done a good job, if there is an opportunity like you saw in our mutual fund numbers where we could get some acquisition to debt funds through paying upfront distribution cost which we think is getting sticky corpus we are ready to take those calls, whether it is on fixed cost or variable provided we are convinced that it builds our business sustainably over a longer period of time. On the bank, I think we are still work-in progress and as I have said in my last call we would like to see next year breaking the cost to income ratio barrier of 50%.

Moderator Thank you. We have the next question from the line of Kunal Shah from Edelweiss. Please go ahead.

Kunal Shah Just again following up on the last question, if we really look at our balance sheet and say, our return ratios in terms of growth we have definitely slowed down but we had not seen anything in terms of NPLs, we have not seen much of a margin compression coming through, as you discussed in terms of downgrade it was for a larger entity wherein we do not have much of a concentration exposure vis-à-vis most of the other banks. So then what would be the specific reason for us to slow down? If we do the internal stress analysis what is the kind of credit cost which we may consider or say compression in margins that is taking us to believe that let us grow slowly at say 20, 22% kind of a run rate?

Uday Kotak We are not targeting a growth rate. We are saying we believe that if we get our risk return metrics we will not constrain ourselves. But we need to get our risk return metrics. Therefore whatever meets this parameter we will do it and we will not be constrained by a formula-driven target. And if you see we are following that principle across different business lines and that is exactly what we will do. And at this stage we do believe that our guidance of 20% plus holds. If we see a possibility of upping that I would say at this stage our base case is 20% plus. But we are not seeing a fall off from that level as we go into the future. And if we feel more comfortable and more confident as we go step by step, for example, if we see a dramatic reduction in interest rates which we do not think happens dramatically but we see directionally and we see a comfort in lending to some of these sectors which we have been careful and maybe in our case, maybe because Jaimin mentioned about some of our accounting policies like for cheque bounces of cheques received before 30th September even if they bounce on 7th of October we take it as an NPA in our September quarter, things like that, maybe in some ways we recognize reality before others and we may get benefit if reality gets better before others. So it could work both ways. And we think that we are on a pretty good track on the asset side. We are comfortable, we are building our distribution and we will continue to grow. As I mentioned in the last quarter when you ask me about the Net Interest Margins, we said that we see around the 4.5% mark as something which we are reasonably comfortable with and give or take 10 basis points here or there, so we are at 4.6 which is where we are at the end of this quarter and we are getting our margins, we are getting for the risk we are comfortable with, we are getting that and if we have an opportunity I can assure you neither targets nor accounting will stop us from doing what we think is right.

Kunal Shah And in terms of stress analysis if you can just throw some light in terms of your outlook on the credit cost for Kotak?

Uday Kotak I think our numbers speak it and at this stage as I mentioned other than a little bit of spottiness in commercial vehicles and construction equipment and obviously, we have tried to keep ourselves away from very highly concentrated infrastructure leverage bets. We are reasonably comfortable. We do not at this stage see dramatic increase in credit cost from here.

Kunal Shah And the question was particularly say now with the growth also moderating so in terms of RoE improvements if you have to look at saying the near-term and the medium term, what is the outlook on that?

Uday Kotak No, we think there are a series of things which will get our RoEs better. Just to give you one example. Last year when the Savings deregulation happened we upped our marketing cost and we obviously upped our interest. If I look at last one year compared to other banks who increase their Savings Deposit rate, our basic starting stock was higher, therefore on that starting stock also we have been paying this 1.5% more through this period which we continue to do and we are getting growth on an incremental basis. So that equation breakeven has still not happened and we are continuing to carry those higher variable cost and obviously we are continuing to do more marketing cost through this period, including opening up more accounts; about 50,000 accounts every month. So all that is upfront costs which is going through our P&L and we believe that there is light at the end of the tunnel and that is one area where we see if I have to take a medium term view we see a reasonable upside coming from. Second, that was the question which was asked that are we sort of mining enough of the fee income part. We have a lot of work and to do on that to get us the delta on the fee side which is where on a relative basis we have a significant upside to take it from. And the third is all our subsidiaries on a P&L basis part of the total profits have been pretty bombed out for a long period of time. So that is the third area where we see at some point of time us getting the delta. And number four is we have got significantly higher Tier-I equity compared to almost any other bank on the street and we propose to sweat it out better. And number five obviously if we can acquire things which can sweat our capital better in the future is something which we will look at.

Kunal Shah And one thing on this if there could be like more insight on this stressed portfolio which has been bought. What is the nature of this, maybe in which particular segment?

Uday Kotak We have got a hell of a lot of accumulation of stress portfolios which we have bought. Okay? So this is just one of them. It is just that P&L hit has been high in this particular one. But we think that is something where there is a lot of juice which will come over time. And this portfolio is secured home loan portfolio.

Kunal Shah And as you mentioned like it is from another financial institution, so this is from one particular institution?

Uday Kotak That is correct.

Kunal Shah And just one thing, since like we have already recovered 7 crores out of this 49 crores in the first quarter itself, now how can we predict in terms of the recovery and say the volatility in the gross NPL?

Uday Kotak Obviously, we assure you that the portfolio is in good shape and roughly breakeven in terms of principal recovery happens between 15 and 18 months.

Kunal Shah So that would continue for this portfolio as well?

Uday Kotak Yeah.

Kunal Shah And one last question on this Kotak Mahindra Prime, the volatility in terms of earnings growth has increased in this particular subsidiary. So just wanted to know like last time definitely the margin compression was on account of some of the repricing of say high yielding loans, this quarter it is just like the margins have stabilized over there or is there some other thing which has led to this kind of a profitability in Prime?

Uday Kotak As we have mentioned 77% of the portfolio is a Car portfolio and 23% is a non-Car portfolio. So, some of the delta has come from the non-Car portfolio. But the Car portfolio in terms of margins is pretty stable and marginally better than the first quarter.

Kunal Shah But still to come to the, say the stable state of levels it would like take two, three quarters as you mentioned so it has not yet reached those levels?

Uday Kotak That is correct.

Moderator Thank you. We have the next question from the line of Parag Jeriwala from Macquarie Securities. Please go ahead.

Parag Jeriwala Our Savings deposit additions has been going down since March. March, we added around 6.3 then it is around 5 in first quarter and now around 4. So, what is happening, if we continue to add around 350 to 400-odd crores on a quarterly basis then one year down the line our Savings Deposits growth rate would be like 20, 22% on a year-on-year basis, so that way we may not be able to improve our Savings as a proportion to deposits. So what is your thought process? Because what is happening is that your customer addition is by and large in line with most of the other guys which are providing higher interest rate on Savings Deposits. So, some clarity on it, what is exactly happening, where we are losing because we are not getting high ticket customers or we are not getting more salary customers or what exactly?

K V S Manian: Obviously, percentage term is one thing but in absolute terms usually there is some seasonality we have seen in the second half compared to the first half. So, if you see the post deregulation period last year was in the second half and since we have seen the first half now, so we do expect the second half to keep pace and accelerate the pace on that, that is number one. And second, in terms of stability of values they remain fairly good, we have not seen any change in value of accounts that are being acquired. So it seems reasonably stable as of now. As I said some seasonality in the second half you will probably see.

Uday Kotak To add to what Manian is saying I just also wanted to clarify one thing which is very important from what we do and particularly since you asked the question relative. We do not pay for any amount more than 6%. Therefore if somebody came and said I am ready to put 10 crores in your Savings Account are you ready to pay me 8%? The answer is no. We also understand that some of our competition is flexible on larger ticket, higher interest rates for improving Savings Account balances and we believe that Savings Account is a Savings Account, therefore 6% is the cap, no one whatever the amount is, if somebody came and gave us a 100 crores cheque in a Savings Account does not get more than 6%. So that is one thing you must keep when you look at absolutes. Number two, on Sweep we have been consistently providing our customers both Current and Savings flexibility of Sweep and we have seen a 50% growth in our Sweep base year-on-year.

Parag Jeriwala Just one clarification, this 42 crores of portfolio which you have acquired, have you written-ff completely or it has provided 100%..?

Uday Kotak Provided 100%.

Parag Jeriwala So your gross NPA includes this number, right?

Jaimin Bhatt Yes, that is correct.

Moderator Thank you. We have the next question from the line of Hiren Dasani from Goldman Sachs. Please go ahead.

Hiren Dasani On the Securities business your overall market share has remained more or less constant. And if you look at the overall market level cash versus F&O volume shares they have not really dramatically improved in the quarter. So what explains this very high swing in the revenues as well as profitability?

Narayanan S.A. If you look at our cash market volumes compared to the overall volume has gone up internally. In that again the delivery volume and the retail has gone up. That is why the overall contribution to top-line has gone up. So to summarize it yes, the overall market has not gone up. While on an overall basis the market shares have not gone up, in the cash part and the retail side especially the delivery side our market share has gone up. And as you will realize that realization rates on the cash market delivery is much higher than the other segments.

Hiren Dasani Just to confirm there is no proprietary trading related income .

Narayanan S.A. I answered earlier also, yes, there is proprietary trading income earlier also and now also and that has also gone up a little bit but having said that the core broking business also contributed a lot.

Hiren Dasani On the AMC side you alluded some expenses which were undertaken to increase some of the stable AUM, I did not understand what kind of expenses it is?

Uday Kotak Let me explain to you. Within the debt fund space, we have two categories liquid fund and bond fund where income fund which is more long-term oriented in terms of how investors think about it. In these income funds, again, there is a distribution fee, In the conviction and belief that you gave a higher distribution fee which is hurting your P&L today and if the customer stays for a period of say six months you breakeven through your management fees. So, upfront fees have been spent to get customers in the debt fund part as distinct from liquid funds. So for which we believe that there is a strategy for getting more customer stickiness for which AUM and asset management fees will come overtime. And demonstrating this if you look at our ranking in terms of mutual fund AUMs they have improved from No. 10 to No. 8. And in terms of improving these ranking we have not focused on Liquid Fund as a basis for this. We believe more sticky of course are the equity funds. Thereafter is long-term debts fund which is bond fund which are more sticky in nature. And it is the second one which is where we have got significant traction in growth and performance and which is where on the back of performance and traction we feel this is more sticky than liquid funds and we have decided that if it means having distribution spends which would give us stickiness on AUM overtime we would do it.

Hiren Dasani Lastly, more of a data point which is the other advances in the Prime which is about 3500 crores, that would be largely commercial real estate?

Uday Kotak Not only commercial real estate. It is loans against shares, it is corporate loans and commercial real estate.

Moderator Thank you. We have the next question from the line of Pankaj Agarwal from Ambit Capital. Please go ahead.

Pankaj Agarwal In the last two, three months various PSU banks have come out very aggressively into Auto Loans and Home Loans. So have you seen any pressure on growth in margins because of that?

Uday Kotak I think for the volume we want, the risk we want, at the price we want there is enough there. Yes, it is a more competitive environment but I think we are pretty comfortable if at all on the Auto Loans there is an article in today's Economic Times which is correct that some of the manufacturers' captive are actually more aggressive on bundling than anybody else. Those are the guys we are sort of watching more closely because effectively the manufacturer is passing on more subvention to his captive finance company compared to other financiers.

Pankaj Agarwal And given that banks are not having a lot of opportunities in Corporate sector. So do you think going forward there could be more competition in the Retail sector, are you seeing any signs?

Uday Kotak We have gone through the cycle. Car loans, I remember the business had gone through huge pressure in terms of competitiveness in those days some other private sector bank was extremely aggressive in pricing and we have got a list through those banks, Car loans we have seen cycles of competitive pressure then some bank realizing it does not make sense, getting out, somebody else coming, so this is a part of the game.

Pankaj Agarwal And in terms of your cost of funds given that your CASA base is increasing and the wholesale rates have started coming down, so how do you see your cost of funding panning out over next three, four quarters?

Uday Kotak We think it would get lower but the question is how much of it that lower cost of funds we will retain versus the competitiveness which you talked about in the marketplace.

Pankaj Agarwal But overall if we leave aside the asset side do you think cost of funding coming down going forward?

Uday Kotak I think it is.

Moderator Thank you. We have the next question from the line of Rahul Jain from Goldman Sachs. Please go ahead.

Rahul Jain Just needed a few data points. Can I have a breakup of non-interest income at the bank standalone level?

Jaimin Bhatt That will include both retail income, it will also include my ARD collection which has been reasonably flattish right now. We are talking about the 250 crores which will include regular commercial exchange incomes for both Retail and the Wholesale side. It includes ARD income as well as some amount of profit on sale of investments in the treasury that it keeps doing.

Rahul Jain But I was looking at basically the breakup between the commission exchange brokerage, capital gains and profit on NPLs.

Jaimin Bhatt If you look at YoY, yes, the profit on investments would have been higher this quarter compared to the same period last year. And if you look at just the sequential quarter it will be more or less the same.

Rahul Jain How about the commission exchange brokerage?

Jaimin Bhatt That would be higher both compared to YoY and QoQ.

Uday Kotak Having more than 20% growth YoY.

Rahul Jain Is it possible to give out the number on in this?

Jaimin Bhatt On a consolidated basis if you look at the note to the press table, we have got the commission exchange brokerage which is of course on a consolidated basis is 208 crores. Of course, this was compared to 370 crores last year. Broadly, this will also include fees on elsewhere which would be the mutual fund fees and stock broking fee income and what not.

Jiamin At the bank level we would say that large part of it is commission exchange brokerage which would be between two-thirds to three-fourths of the overall number.

Rahul Jain Second thing, gross NPA excluding stress asset portfolio would be how much at the end of this quarter?

Jaimin Bhatt At the bank standalone level excluding stress asset will be about 606 crores compared to one quarter ago 592 crores.

Rahul Jain And is it possible to get an outstanding amount of loans against property? I presume that we include this LAP portfolio in …….

Jaimin Bhatt That is part of the mortgage.

Rahul Jain Yeah, so is it possible to get an amount on that as well?

Jaimin Bhatt I would not have the exact breakup of that.

Rahul Jain Actually I was trying to understand the trend as to what is really driving the growth in mortgages, is it LAP or the residential part of the business?

Jaimin Bhatt LAP would be a larger growth in terms of percentage than the traditional home loans.

Rahul Jain Just if I may ask one or two more questions on the strategy part, Uday mentioned that in terms of better sweating out of the capital you would look at acquiring something. So I was curious as to what you really mean when you say that you would look out to acquire something, is it a particular portfolio ?

Uday Kotak It could be anything from asset to anything else.

Rahul Jain And in a loan book side the CVs on a sequential basis has just grown by about 2 percentage points QoQ. Now I understand that you have been little cautious on this piece. But if I really compare with some of the large banks out there they have grown at a pretty healthy pace on a QoQ basis. So, just trying to understand are we sort of overcautious or we are really seeing some stress which is beyond our comfort zone?

Uday Kotak I think time will tell that. And as I said it is not about being overcautious or what others are doing and all. I think we have gone through this. Finally, for the returns we make I will be comfortable with the risk. That is it. Therefore if somebody wants to work on significantly lower RoEs in the short run or as a credit view which is different or as a segment which is different, those are all strategies each of the institution can take. For our strategy for each of these segments or markets or geographies or customer profiles, for those specific ones if we are comfortable with the returns for the risk we take we will do it.

Rahul Jain Can you just throw some more light on this, are we sort of not really accepting any more customers in that part ?

Uday Kotak Let me put it this way. We have not closed the shops.

Rahul Jain So we are sort of maintaining our interest rates or maybe in some geographies we might have also increased it wherever we are seeing some pressure?

Uday Kotak Yes, we will adjust, but finally we cannot increase it. The market place is also telling us something no, therefore we have a choice of doing business with a particular customer segment at a particular price. At that price for the returns we make out of that risk is it worthwhile or no?

Rahul Jain Just finally in this personal loan portfolio, what all do we include, what are the main components out there, is it including credit cards and unsecured loans?

Jaimin Bhatt Personal loans will not include credit cards, it will be largely unsecured personal loan, it will also include business loans of very small ticket size.

Uday Kotak And some of it may have security also.

Moderator Thank you. We have the next question from the line of Ashish Sharma from Enam Asset Management. Please go ahead.

Ashish Sharma Just wanted to get a sense on this stress asset portfolio we have got. I mean you have provided for around 42 crores in the P&L. But how to factor in this volatility in the P&L because do we factor in that further purchases like this will happen which will have sort of a P&L impact in the short term?

Uday Kotak One thing we are very clear. If we see value in something we are clear, quarterly accounting will not stop us and that is the philosophy we as a firm will have. We will not change accounting policy to meet quarterly numbers. We will not tweak with process to achieve that.

Ashish Sharma And in terms of the overall gross stress asset book as of now, how much is the outstanding?

Jaimin Bhatt If you look at what ultimately provided on my books including **SR** and all we would have about close to 400 crores.

Uday Kotak But having said that embedded value is not on the provided piece, but the original piece. Just as an example, and there is a pretty significant portfolio in addition to this. If we have provided it and bought it down to zero the embedded value is significantly more than what we are carrying in our books, that is what we believe. But this is required by the regulators and our accounting policy.

Ashish Sharma And there was one NPA account in Q1, the infrastructure account, has it reverted to standard category ?

Uday Kotak Let me first clarify. You are right, we had a NPA account in Q1, but we never mentioned it was an infrastructure account. Now that NPA account is now a widely known account where to the best of my knowledge we were the only bank on the street to recognize it as an NPA in the June quarter. It happens to be a media company and we recognized it in June when no other bank recognized it. We have made our provisions there and we have made appropriate provisions now. Therefore, this problem of the media company was known way back in May-June.

Ashish Sharma And do we have any collaterals? Do you expect any recovery ?

Uday Kotak We have collaterals and we have made appropriate and adequate provision on this in the June quarter and further in the September quarter.

Ashish Sharma In terms of outlook on CV and CE segment, you mentioned there were sort of over-enthusiasm among suppliers. Are we sort of still maintaining a cautious outlook in the overall segment?

Narayanan S.A. In this segment our stand has been basically value and not volume alone. We have been seeing the last six months some amount of strain in the portfolio especially in the Construction Equipment side and the CV is related to the Construction Equipment side. So we have definitely slowed down on our disbursements in that segment and become more cautious. We have not gone aggressive there and as Uday mentioned we go on case-to-case basis because there are of course good players in that segment; large transporters who have got good reputation, so the challenge is to ensure that we pick the right customers, b) we price the product for the right customers. So it is not that we are completely out of the market. But having said that we are not running behind increasing volumes and are more cautious.

Ashish Sharma For Kotak Securities you mentioned that you have increased sort of cash market share. Has there been any improvement in the broking yield also or is it just the improvement in the market share?

Narayanan S.A. No, it is more improvement in the market share.

Ashish Sharma But do you expect the yields to improve?

Narayanan S.A. My view is it is tough to increase the yields as of now but I personally feel that over a period of time market will consolidate and at that point of time you will see some amount of yield also going up.

Moderator Thank you. We have the last question from the line of Ramakrishna from HSBC. Please go ahead.

Ramkrishna Just wanted to have an understanding on Agri finance. Apart from tractors, what kind of composition that this particular segment has, if you can just throw some light on?

Narayanan S.A. It can range from processing unit, it can be loans to large agriculturalists, and it can be cotton gearing units, so it can range from various agri related activities. So for example, it can be in a warehousing company which is in the business of storage of agri goods, etc. So it can range from tractors to those who are in the business of agri.

Moderator Thank you. I would now like to hand the floor back to Mr. Uday Kotak for closing comments.

Uday Kotak Thank you friends and this has been a good call, and as I said I hope the policy actions continue and the macro hopefully gets a little better and we carry on our path of sustained growth.

Moderator Thank you sir. On behalf of Kotak Mahindra Bank that concludes this conference call.