



# Kotak Mahindra Bank Limited Q2FY17 Earnings Conference Call

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**Moderator:** Ladies and Gentlemen, Good Day and Welcome to Kotak Mahindra Bank Q2FY17 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '\*' then '0' on your touch tone 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 Afternoon, friends. I know it is a very busy day for all of you and you are running between calls and meetings and everything else. Quickly, let me share my perspective on the Earnings Update post our Q2 Results. First, let me say that essentially we are now at the end of the integration process and if you notice in our Earnings Update, we are not giving any specific presentation separately on integration. We are moving to a phase which is business as usual. If you recollect in the last review, I had mentioned that by end of the second quarter we should be moving to business as usual which is what we see from Q3 onwards. Essentially, a lot of issues around post integration of technology cropped up in May; we went through some teething issues in June-July-August and even part of September, but they are more or less behind us. We have also had some issues with loan growth in some segments of business, post integration. The significant one being the Business Banking piece, which we believe has also bottomed out now; by the end of the September quarter and we see that also moving towards normalization in the second half.

If you recollect, I had mentioned that we did the wholesale banking merger last year during July-August which then took us six odd months of teething challenges, and you can now see in the current year Wholesale Banking beginning to grow on a fully-integrated basis. We see similar situation happening in other pieces of integration as we move down into the second half of the year.

In simple language, what I would like to share with you is that we as a team now feel, we are much more in grip of the situation than we were 6-8-months ago. Now, it is like being in broader control of the combined entity. Therefore, particularly on the loan side we have grown at 13% in the second quarter, but we now see that picking up as we move into the second half, post completion of most of the integration processes to get more growth at a faster rate. Therefore, at this stage I would continue with our broad estimate of growth rate of around 20% by the end of this year. On the Credit side also, we are moving towards stabilization and from thereon hopefully we see some gradual improvement in the credit cost as we go into the future. A lot of the credit cost post integration have already got absorbed by the end of our September numbers. Therefore, a gradual improvement in the direction of credit cost is what you would see.

You would have noticed an expansion in our NIMs. For the second quarter, we have moved to a NIM level of about 4.47% which is higher than the earlier period; however, I would still continue with a guidance of around 4.2% to 4.3% as our basic guidance in terms of how we see NIMs move as we go forward.

Other than that we are seeing some pickup in some of our Subsidiaries businesses. You would have seen growth in our Securities business, in the AUMs, in our Mutual Fund, our Life Insurance business

continues to grow at a reasonable pace. All in all, we feel at this stage our business is in good health. With the integration challenges significantly absorbed, we look at the second half with even more confidence than in the numbers which we have seen in the first half.

Obviously, we will continue to update you on various developments. We announced an acquisition of a small microfinance company in this quarter called BSS Microfinance. Of course that is subject to approval from the regulator, but that would be one of the missing pieces from the broad range of activities we have. We plan to keep that as an independent subsidiary of the bank. At this stage, we believe that this is an area which we want to explore and learn how we can develop that business as we grow into the future. Our capital ratios continue to be strong and we feel pretty good about where we are at this point of time.

With that, I will hand over to my colleague, Jaimin Bhatt.

**Jaimin Bhatt:**

Thanks, Uday. Just to take you through the Earnings Update which was circulated after the results, we closed this quarter at the bank standalone with a profit post tax of Rs.813 crores compared to Rs.570 crores year ago. We have seen a sharp rise in our Net Interest Income, 19% on a year-on-year basis. We have been helped largely by the fact that both our Current Account and Savings Account had a very healthy growth on an average basis year-on-year. Our current account on an average basis grew by 28% year-on-year whereas the Savings Account growth has been 35% on YoY basis on an average, which effectively led to the cost of funds coming down. In addition, we also had the Sweep Deposits which have grown close to 37% on a year-on-year basis. Other income also has shown a rise, somewhat because of Treasury profits during this period. But other than Treasury, the Fee and Services clocked Rs.630 crores for this quarter compared to Rs.558 crores for the same period last year. That has been held across board by rise in income on mutual fund distribution, insurance distribution, retail bank, direct banking and the like. Employee cost on a year-on-year basis grew by about 10%, partly due to rise in dearness allowance which was announced in August as well as the fact that discounting rates have been lower considering the softness of the interest rate scenario, which has led to retiral benefits going up.

The other operating expenses are just marginally higher somewhat due to higher advertisement spends during this quarter. Other opex also includes the fact that during this period we bought and sold PSL certificates. Our provision on investments includes that on security receipts. Most of these were what we had acquired from the ING Vysya acquisition.

The gross NPA stands at 2.49%, only small slippage during this period; net NPA stands at 1.2%. Restructured standard assets remaining small at Rs.147 crores, 0.12% of our net advances and SMA2 number as on September is at Rs.419 crores which is 0.33% of our advances. Just Like in the previous periods, we have got no ARC transfers or conversion to off-balance sheet 5/25, CDRs or rectification during this period at all. NIM, as Uday mentioned, remain healthy at 4.47%. The capital adequacy overall at 16.8% and Tier-1 at 15.7%.

On Advances, broadly, we ended the period with Rs.1, 26,000 crores. If we look at the broad three-way split, which we do internally i.e. Consumer, Commercial and Wholesale, the Wholesale and the

Consumer pieces together are roughly about Rs.40,000 crores, with the Commercial piece at about Rs.45,000 crores. The Corporate Bank growth has been at 14%-15% for the year. The Commercial Vehicles segment and the Construction Equipment's segment have grown pretty much. The Small Business segment, which includes Personal Loans and Credit Cards has also shown 18% growth on year-on-year basis. In addition to the Loan growth, we have also seen investments in Corporate Bonds and PDCs in this period and if I add that, we have seen a growth of about (+14%) on advances plus credit substitutes for this on a year-on-year basis and if I annualize the quarter number roughly about 20% growth during this quarter.

As I mentioned, the CASA at the end of the period is now at 39%. Sweep Deposits at 6.4%. During the current year, we identified about 100 plus branches which we intend to relocate or rationalize during the current financial year. We have completed 21 of these in the first half of the year. CASA and Time Deposits below Rs.5 crores are 73%. The cost of Savings Deposits at 5.52%.

Shanti, request you to cover the Digital.

**Shanti Ekambaram:**

Thank you, Jaimin. Our Digital strategy is on the lines of a few key themes -- one being scale acquisition at an efficient cost, look at the differentiated customer service, cash alternative which is the payment space and really focus on cyber security, which includes fraud prevention.

I just want to share a few outcomes with you. As far as the 'App' is concerned, we continue to be 'One of the Highest Rated Apps in India' and have added many new features. As of today, about 30% of our active base is Digital which is through mobile and 46% out of them are mobile-only customers. Our Mobile Banking usage is more than 3x of our Net Banking. We have the 'Highest App Usage', which means people who consistently login into our app.

In terms of share of market, based on RBI data which is a little dated, we continue to be amongst the top five in terms of value of transactions. We are at about 5% of the volumes, with 4.2% of the value versus Deposits and Advances of 1.4% and 1.5%.

We have added and enriched our offerings on the app for our customers, which includes bringing ecommerce, i.e. We added Flipkart. We already were in the travel and lodging space, thereby allowing customers a very fast, convenient and efficient way of transacting. We have joined the UPI Group of Issuers from payments perspective and are one of the pilot banks participating in the Bharat Bill Pay.

From highlights perspective for the month of September, our payment value through mobile crossed Rs.3, 500 crores. We have seen 95% YoY growth as far as Digital Payments are concerned, 79% through Payment Gateway YoY growth, of which 40% had come through Mobile.

On the Liability side, in terms of number of accounts, we have seen a growth of almost 60% in H1 on YoY basis and the balance is about 25% through the Digital means, 7% is the overall contribution of our Digital acquisition to the total acquisition today. Greater than 60% of our Recurring Deposit is sourced

online, 50% of Term Deposit and greater than 50% of the account maintenance today is coming through net banking.

In terms of Digital Lending, again, Personal Loans have shown 80% YoY growth, our Instant Personal Loans which is under 10 seconds, is about 50% growth and 14% is the overall digital contribution of incremental Personal Loans. Key focus is really to make it simple and easy for the customer to transact.

I talked about scale acquisition at a more effective cost. Tab Banking; today more than 20% of our Salary Accounts come through the Tab Banking, which is straight through processing as far as the customer and a quick turnaround in the account opening and mobile-based lead management rollout for our entire front field force to be able to track, lead, convergent in a very efficient manner. So, we have a very well defined laid out path as far as our Digital strategy is concerned and we will continue to work on it as we go forward.

As far as the Subsidiaries are concerned, Kotak Securities in Q2FY17 more than Rs.8, 000 crores per month has come through the Mobile route. Brokerage contribution to the App is about 11%. We have introduced many initiatives for the customer including Digital Insta Kit on our trading platforms which really enhances the customer experience.

In terms of Life Insurance, I talked about the Genie Tablet last time. About 30% of the sales in Q2 came through Genie, 14% of the renewal premium and about 48% of the switch requests. So both bank and subsidiaries continued focus on Digital as a way of life for our customers. Jaimin, over to you.

**Jaimin Bhatt:**

Let me give the consolidated numbers for the Group. On consolidated basis, we clocked post-tax profit of Rs.1, 202 crores. We end with a net worth of ~Rs.35,690 crores. Book value now stands at Rs.194 per share. NIM at the consolidated level is at 4.46%, capital adequacy overall at 17.3% with Tier-1 at 16.5%. Our balance sheet size now is just a shade below Rs.2.5 lakh crores. On the Advances front, the total book advance at the end of the period Rs.154, 000 crores. We have seen Auto which is outside the bank growing at about 11% on an annualized basis.

Other than the bank, the contributors to the overall profit for the quarter, Kotak Prime at Rs.130 crores, Securities, as Uday mentioned, Rs.96 crores, Life Insurance at Rs.63 crores and the Kotak Mahindra Investments which is the other NBFC at Rs.53 crores with the international companies clocking Rs. 31 crores. Prime has seen about 16% YoY loan growth of 16% odd continues, pretty healthy capital adequacy ratio there at 18.2% and low net NPA at just 0.4% level as of 30 September.

Kotak Investment is growing at 37% SOH on a year-on-year basis, plus 13% growth for the quarter itself, pretty low NPA again, 0.12% and again a healthy capital adequacy of 18.2%. This quarter profit Rs.53 crores includes some one-time investment income, which has been booked.

With the Insurance segment, we have seen total premiums growing at 37% compared to the same period last year. Individual regular premiums, new businesses had grown 15% and overall sum assured has grown by 23%.

All the equity funds are in the quartile one on performance with claim settlement at 98.8% ratio. Securities posting a sharp rise in the second quarter helped by the fact that we have seen increase in volumes both on a year-on-year and quarter-on-quarter basis especially in the cash segment. The Investment Bank continue to be in the middle of good deals both on the IPOs, the equity placements and on the advisory side.

Our overall assets which we manage or advise grew at Rs.1,20,000 crores and we have seen during this year a growth on the domestic mutual funds, both on debt and equity, on our alternate asset pieces and PMS which is a small number but growing now.

On the domestic mutual fund side we have seen our assets under management on an average basis now at Rs.70, 000 crores with our equity ranking moving up during the year.

Broadly, those were the highlights for the Group. We would be open to taking the questions.

**Moderator:** Thank you. Ladies and Gentlemen, we will now begin the Question-and-Answer Session. The first question is from the line of Vishal Goyal from UBS Securities. Please go ahead.

**Vishal Goyal:** Sir, first question is actually about the Loan growth and within that Business Banking division which seems to be flat. So is it because of some concerns around the segment or waiting for more operational smoothness with ING, etc.

**Uday Kotak:** I have my colleague, Narayan, who is in charge of that division to give the answer.

**Narayan S A:** The ING and the Kotak SME business merged on May 1st. Post-merger there was time to settle down for both the teams vis-à-vis processes, the structure, etc., and it took some time for us to get the growth back. We have seen better growth from September onwards and the flow in October is also good. So if you ask me, for the second half I am more confident that the numbers will look better than what was in the first half. If you also look at it vis-à-vis March, the September number is slightly higher whereas it was down in June vis-à-vis March. So if you ask me personally I am more confident now. These are the same things which we witnessed in the Corporate Banking when the initial integration happened and post that things took time to settle down after which it started picking up.

**Vishal Goyal:** So no asset quality related issues, correct, at least you are not seeing any problems in that segment?

**Narayan S A:** I am not saying there is no issue at all on that, we are seeing some asset quality issues, which if you ask me again, in the second quarter we have seen that the number of cases, which were getting into the stress numbers are coming down. But if you ask me the reason for non-growth, is because of the time it was taking to settle down. Asset quality in this segment continues to be of some concern, but I see it getting better in the last two months.

**Vishal Goyal:** A broader question on the overall loan growth. I think we are still kind of guiding for 20% and we are seeing banks of your size growing more like 25%, 30% and you also seemed slightly more confident about economy in your previous quarter. So what takes us to 25-30% range on loan growth?

- Uday Kotak:** I think you have to look, to a certain extent, at the DNA and the culture of the firm. The DNA and culture of this firm is risk adjusted returns. Therefore, the pricing of the risk and the returns is an integral part of our DNA. We do not want to change that philosophically, while we may want to push for growth which is why we are continuing to guide at around 20% number. The reason for the 13% in the second quarter on a standalone basis or 14% consolidated is coming from the fact that one or two divisions are still settling down post integration. Therefore, as we gradually accelerate, we want to see that the culture of what we are in terms of returns for the risk and the metrics of growth combining all three. Hence 'risk, return and growth' all three need to work together and at this stage we would continue to guide around the 20% mark as we go into the second half. Keep in mind if the first half is say 13% or around, for the full year if we go to 20%, it obviously means some acceleration in the second half.
- Moderator:** Thank you. The next question is from the line of Ashish Sharma from Enam Asset Management. Please go ahead.
- Ashish Sharma:** Sir, just two questions: First on the NIM, I think we have seen a sequential improvement in NIM to 4.47%. Sir, just from a trend perspective, what are the range I think we should expect NIMs to normalize? We have seen a significant improvement from the cost side. But do we see some uptick from the yield side or yields are under pressure, just some color on that sir?
- Uday Kotak:** At this stage we would guide you around 4.2% to 4.3%.
- Ashish Sharma:** Do you see some sort of a pressure building in from the yield side because I think there is a level to which the cost side can give you an advantage?
- Uday Kotak:** I think you have to be clear. What is yield? Yield is a combination of lending rate and cost of the risk we are taking. So if your lending rate drops but your cost is also dropping and you are comfortable with the risk you take, you get your NIM as an outcome. Most people look at lending rate and margins are under pressure. Lending rate will come down if your cost comes down. Then in this equation of lending rate and cost, always factor in the risk and you have to price that risk. If you tell me that okay, I need to grow my loan book, reduce my NIM, but take more risk. That is something which we have to handle carefully, because the problem is that we certainly want to grow, but we want to grow in a manner that two years from now we do not want to come and report a fiasco.
- Ashish Sharma:** Second metric would be on the cost-to-income ratio, we have seen a sharp improvement already. So for the merged entity, we had given guidance in terms of cost-to-income ratio, but we seem to be a little ahead in terms of improvement. So, is the current number a normalized number or we see some sort of a headroom in terms of improvement in the cost-to-income ratio sir?
- Uday Kotak:** Obviously, we are happy. If you go back to the guidance which we gave you for the full year that our cost-to-income ratio will be below 50%, we are at 49.7%, technically below 50%. We are now a lot more confident of our guidance of below 50%. How much of that confidence translates to further improvement in cost-to-income ratio is something which we will watch during the year. At this stage we are significantly more confident of being well below 50% for the full year.



- Moderator:** Thank you. The next question is from the line of Prakhar Sharma from CLSA. Please go ahead.
- Prakhar Sharma:** Firstly, on this Digital progress that you are seeing and very impressive to see that you have been able to garner 50-60% of deposits using digital channels. I wanted to understand two things here: One, basically is there branch staff involvement involved in this sort of level at this stage? Two, given that you achieved so much mobilization from digital channels, how are you relooking at your physical infrastructure from a cost perspective?
- Uday Kotak:** I will have Shanti answer the first question and I will answer the second question first. On the second question first, which is on branch infrastructure, if you notice, one of the reasons for the acquisition was to get our physical infrastructure to a certain scale and size of relevance. Physical infrastructure still in an economy which has reasonable cash and the trust factor linked with it was important. Having said that, with the progress in the Digital side, we believe that our optimum network levels are lower than what we would have said a few years ago in terms of the network we need in the context of the changed world. We first focused on really getting our current infrastructure and network into outstanding shape, because that is the money already invested in including for the acquisition, but we will certainly have a lower hurdle of absolute physical infrastructure now compared to earlier times. Whether that number is 1,500 branches, 1,800 branches or around, maybe 2,000 at the most, but that is the range in which we see our current view on the end state. We therefore believe that our ability to compete with a smaller network is significantly higher than what it was two years ago. With that on the Digital progress, I will request my colleague Shanti to really take us through and also if she has any inputs on the future of branch infrastructure.
- Shanti Ekambaram:** As far as your question on Digital adoption goes, it is actually horizontal, which means it cuts across all our channels including branches. We drive digital activation or moving customers to adopt digital across all channels including branches. For example, at our branches we insist every sales and service point's talk about helping our customer download the app, doing the service themselves, looking at incremental deposits. So, we are moving to a whole concept from serve to assisted self-service, maybe at some stage in the future self-service itself. So, it is being pushed as much in the branch. Secondly, something that I have not talked about, that we are bringing many digital elements into the branch itself for walk-in customers to enable themselves to be assisted self-service. So, yes, very much being pushed at the branch and across other channels including call centers and we are upgrading our ATMs to move to self-serve. The question that Uday answered and he asked me to briefly hit, the acquisition of customers even today happens around branches, today, for example, we are at 7% acquisition, which is one of the highest in the industry. I think it will change over a period of time, but even the most digitally-savvy customer wants a psychological feel of a network somewhere. So, I think the format, size, elements of a network will change, but I think physical branches incrementally will be lower, but will not disappear from the horizon at least for the next three to five years.
- Prakhar Sharma:** Uday, could you just elaborate on the reason that you had acquired this subscale microfinance company, how do you want to scale it up and what is the top-down thinking here?

- Uday Kotak:** Microfinance is a space we are not in. Now, the choice for us is to buy a large microfinance company or to buy a small microfinance company with a team of people who understand that business and the culture. Keeping in mind our view of two things -- one is high value focus in terms of what we buy and #2, growing from a smaller base to steadily building some business. We felt starting with a quality company at a decent value, learning from the team which has been doing that business and building it to scale over time, is the core of our philosophy. That way, we believe we add significantly more value and learn the business at much lower cost. Therefore, we certainly plan to grow this business which is right now more regional in Karnataka and very little parts of Maharashtra, but over time we see this as a vehicle of significantly being able to scale up this business from where it is. I will ask my colleague, Mr. Narayan, who has been directly driving this merger and also the strategy thinking behind it.
- Narayan S A:** Just as a background of this company, it is more than a decade old and it is run by Dr. Ramesh who will over a period of time step down except being a mentor and wherever we need him, will come for help. The most important thing is we have got a good management team; CEO, Chief Operating Officer, Chief Financial Officer. It is almost a standalone, professionally well-run company. That is what attracted us to this business. Plus, the quality of its portfolio is very good and in fact DPD is almost zero. So, that is the quality of the portfolio which we have built over a period of 10-years. We were interested in something where we can have 100% ownership and not part ownership, because that is the only way we can grow this business. If you see the growth of the microfinance assets over the last one year, it has been more than about 80% of the industry. So this industry we feel will continue growing at this pace, plus the regulatory environment in this industry has become far better than what it was 3-4-years back. So all these factors put together we felt it is a good business to be in and BSS was fitting into what we were looking for.
- Moderator:** Thank you. The next question is from the line of Parag Thakkar from HDFC Securities. Please go ahead.
- Parag Thakkar:** I just had one question on the credit cost side. So credit cost guidance last quarter you gave was 50 bps for FY'17. So I would just like to ask again what is the credit cost guidance for the full year FY'17?
- Uday Kotak:** Broadly around 50 basis points and on end of year loan book.
- Parag Thakkar:** Sir, as you rightly said that second half you need to accelerate to more than 25% growth in loans alone. So where do you see this growth coming from in terms of which segments?
- Uday Kotak:** I said for the full year we will grow at end of YoY 20%.
- Parag Thakkar:** First half is 13%. So the second half you need to grow more than...?
- Uday Kotak:** So, as I said, there are pieces of the business which have not fully recovered from the pangs of integration in the first half. So, those businesses, as integration gets behind us, will start picking in the growth.
- Parag Thakkar:** Sir, you mean to say the Commercial Vehicle, Construction Equipment or Agri side maybe because there was decent monsoon, so....

- Uday Kotak:** You really need to look at three parts -- One is secular growth in sectors which are growing faster, so that is one thing, which will come. Second is us getting share from other players. Third is us getting past our internal integration challenges. It is a combination of the three. We think the third one is something which is now set to get us the kick off.
- Parag Thakkar:** I understand that right now after this Essar Oil has happened, there is a lot of hope around this corporate stress coming down for corporate facing banks. So, just wanted your most valuable view on this.
- Uday Kotak:** Our view is that first of all Essar deal is good news for the system, so that is a general view. On the more specific issue about stress in the system, I do believe that one of the things I have learned in life is debt cannot be wished away and interest on debt also cannot be wished away. So finally either take the hit or the borrower pays it from existing or new equity. But somebody has to pay for debt, unlike equity, which you mark-to-market because lot of it is valuations, debt is reality. So, debt does not go away and whatever is the stress in the system is still continuing. I am glad that some of the bigger account progress has happened. But the stickier loans even in large accounts still needs resolution and I do not know whether that has really moved forward yet. In the process, what is happening is in many of the groups... without getting into specific name, the good assets get easily sold which in any case may not have been a stressed asset in the first place.
- Moderator:** Thank you. The next question is from the line of Roshan Chutkey from ICICI Prudential Asset Management. Please go ahead.
- Roshan Chutkey:** Could you please talk a little bit about the CV, CE business; the growth in the business has been pretty strong, what are our yields there?
- Narayan S A:** We started growing this Commercial Vehicle and Construction Equipment business about a year back. To grow that business, we put a new structure in place, some better process and system in place and that has started paying back. Our market share in this segment has continuously increased especially in the Commercial Vehicles segment, which you can see on the quarter on growth on both on disbursement, which is reflecting in the stock on hire, plus the stress asset which was there in this portfolio also substantially resolved or some of them have been washed through the books. Since we had substantially reduced our disbursement earlier, the stress asset in that segment did not affect us much. Hence the motivation and the morale of the team was not down and they could come back and start disbursing. We are confident about this business now and we hope to grow the market share in the next six months again.
- Roshan Chutkey:** What yields do we earn from this business?
- Narayan S A:** Yield is pretty good; I do not think we disclose the specific yields on the segment to the market.
- Moderator:** Thank you. The next question is from Kunal Shah from Edelweiss Securities. Please go ahead.
- Kunal Shah:** Sir, my question is with respect to Savings Deposits. So today when we look at savings per branch that is now almost Rs.25 crores odd which is would we say almost like 20% higher than the run rate which we were running prior to the merger? So, has the major part of the benefit in terms of synergy through

customer leveraging has happened on the savings or still we will continue to see this kind of ramp-up going forward as well?

**Uday Kotak:** We think that there is a lot more scope to grow savings and as the overall interest rates in the economy soften, we think the growth in Savings Deposit has even more potential for us at 6% proposition. We are actually very excited about having significantly higher growth than industry growth in Savings to continue for some time.

**Kunal Shah:** So, maybe this kind of a ramp-up on the CASA would still continue and that benefit on cost of deposits would be very much there?

**Uday Kotak:** Our 6% cap, nobody gets more than that and our average cost of Saving Deposit as we continue to disclose is about 5.5%. So we think we need to grow significantly faster than industry averages because there is a price we are paying and that should come in terms of higher growth from a strategy point of view and that philosophy continues very much and at this stage we are completely of the view that this is something which we will continue as we see the situation right now of a significantly higher growth rate at broadly current cost.

**Kunal Shah:** The other was with respect to SMA2. There was one account of Rs.150 crores-odd which had come in from ING Vysya which was there in this list. So, what is the status -- is it out you mentioned like it was more technical...?

**Uday Kotak:** SMA2 is like a railway platform here, accounts go in, accounts come out, and this is not an NPA. Therefore we monitor in totality, we ensure obviously there is a focus at the account level on each account. So, some go in, some come out, but broadly if you notice our SMA2 numbers are around Rs.400-odd crores mark. I am not seeing anything which would make it go up dramatically, but I am not ruling out something if something went to 61 days it is not an NPA. But we are as a good policy disclosing to you where we stand on that. These SMA2 accounts, let me again clarify are accounts which are more than 60-days overdue, more than Rs.5 crores but not NPAs.

**Kunal Shah:** The only thing was maybe that account was slightly larger in size in the overall pool. Because Rs.150-odd crores even on say last time's SMA2. So that was a significant component. So just...

**Uday Kotak:** This you are talking about March, not June?

**Kunal Shah:** Not June, yes.

**Uday Kotak:** So I think there is some in, some out, but broadly same.

**Moderator:** Thank you. The next question is from the line of Jeetu Punjabi from EM Capital Advisors. Please go ahead.

**Jeetu Punjabi:** So two questions: One, after having gone through the integration what are the key learnings that you take away both internally as well as from a market perspective? The second question is, as you are looking

out over the next six months, what do you think are the one or two key priorities you need to get right over everything else?

**Uday Kotak:**

I think first of all integration learnings is that it is tougher than what you think. That is the clear learning, #1. #2, despite whatever conservatism you may have used at the point of acquisition always be ready to expect some surprises. The more you can plan the surprises, the better you are. There will always be something which you feel you should have known better. #3 is the biggest challenge is people, people, people. We underestimate the power of the human mind to make things happen or not make things happen. As you can see it has taken us longer in each segment of business we integrated to get the machine working post full integration than what we thought. You can see that in, for example, last year you saw it in our Corporate Banking numbers, this year you are seeing it in our Business Banking post integration to really make it fire at the levels which we want. Fourth is if you are dealing the two separate technologies on two separate platforms, the dissonance of moving from one technology and one process to the other is huge. Whatever you may proactively do, there will still be significant customer challenges when you actually do the integration. I compare it with two planes are flying next to each other. You are now saying, while the planes are flying, customers from one plane are being moved into another plane while the two planes are still flying. You really got to handle that carefully, because this is a highly customer business, one of the reasons why you are merging or acquiring is because you are valuing the customers you are getting. The last thing you want is in this transshipment, you do not drop customers on the way. So, these are some of the learnings. In terms of our priorities from here, with reference to the acquisition in particular, is really getting our combined branch network of up to the shape and size which we would have liked it assuming it was ours and really getting it cranking both on the urban side as well as the semi-urban side. We have a phenomenal presence now in the south, particularly in states of Andhra Pradesh, Telangana and Karnataka. We have now got to dramatically leverage the network and the customer base which we have got with it, which now we feel very much in-charge of the steering wheel, which we did not probably six to nine months ago. We now feel that we really got to make that engine work to build synergies and build growth both in acquisition and as well as cross-sells. The second part of this is one of the interesting businesses which we got as a part of the merger was the SME business or business banking model. Now, that has had significant integration challenges as can be seen in our numbers which have been flat. We see that we are now in a position to really start cranking up on and in addition to that, some other lending businesses which will start firing in. While we are doing all this, we have to keep in sight the fact that we go to grow Digital, our presence for customer acquisition, make sure that we have a model which is both disruptive and defensive at the same time. Disruptive vis-à-vis the existing entrenched players and defensive versus the new players who will be coming into this field and strategically positioning ourselves to be building an efficient and potentially lower cost to model for significantly higher efficiencies on customer acquisition, deepening and revenue growth.

**Moderator:**

Thank you. The next question is from the line of Sri Karthik from Investec. Please go ahead.

**Sri Karthik:**

My question is pertaining to our Home Loan and LAP segment growth which is lower compared to what we have seen historically. In that context, how we see the growth in our Kotak Mahindra investment book which is also to the real estate sector?

- Uday Kotak:** I will have Kotak Mahindra investment questions first answered by Manian and then Home Loan and other specifics by Shanti. Manian?
- K.V.S. Manian:** So, as you see the book, KMIL has grown significantly, large part of that growth is essentially more out of capital markets and structured corporate transactions rather than CRE. CRE, our strategy is largely to be with the best quality developers in most regions. We have not grown that exposure significantly, in fact, the CRE exposures are flatish and some of the growth, like I said here is more from structured transactions or corporate transactions. Our strategy remains that we keep exposures on better quality builders and control our risks in that segment, because obviously there is no doubt that this segment is stressed per se and the choice of customers is extremely critical to maintain the quality of the book and the profitability of that portfolio.
- Shanti Ekambaram:** As far as Home Loan question and LAP question is concerned, last two months have seen very good growth as far as volumes are concerned. There are two things -- One, which is a number of foreclosures largely from owned funds as well in relation to BT. So that has been surprising and interesting is that customers with their own funds have sort of reduced their leverage. Second, we did have some people, attrition and integration issues, which are now behind us, but the volumes in the last two months are very good. So it is really a combination of these two-three factors.
- Sri Karthik:** Regarding the stressed asset portfolio, which we acquired a couple of years back, any sense on the progress and how the opportunity cost on that clearly plays out in terms of our accounting?
- Uday Kotak:** I will request my colleague Dipak to give his perspective on the portfolio which was part of the merger.
- Dipak Gupta:** As we mentioned in the past, I think the recovery process is slower than what we had hoped or expected early primarily because I do not think the overall economy has really improved significantly, I think we still are facing similar challenges from the legal environment as we had in the past, but I think from a recoverability point of view, I do not think the estimates have really changed very significantly. So I think there is value in that. It really is a matter of time.
- Sri Karthik:** So how do we look at the opportunity cost associated with that portfolio sir -- has it been completely written down?
- Dipak Gupta:** Yes, most of it is written down now. Whatever we think is appropriate from a provisioning point of view, we have really made those provisions early. That is why if you recall what Uday mentioned, this year our estimate overall credit cost will be about 50 basis points really.
- Moderator:** Thank you. The next question is from Jahnvi Goradia from Motilal Oswal Asset Management. Please go ahead.
- Jahnvi Goradia:** Sir, just one question on Kotak Prime. The book has grown healthily, but the profitability seems to be declining. So just wanted your comments on that?
- Uday Kotak:** I will request my colleague, Narayan, who oversees that from an SBU point of view. Narayan?

- Narayan S A:** The total advances of the Kotak Mahindra Prime has both Car Loans as well as the other Real Estate and Loan against Shares portion. The Car Loan portfolio has grown, but the margins over the last nine months have come down because of the stiff competition in the market. But let me also say here in the last three months, we are getting back our margin. In fact, the margins were down in the first quarter, we actually scaled down our disbursement to some extent because the margins were not good enough for us to take the risk. The margins in the other advances also slightly come down, which is why that overall profitability has come down. Having said that, the Advances book has grown and we hope to grow it in the second half also.
- Jahnvi Goradia:** So, the margins that we see right now, would you say that that is stable and that would maintain in the future?
- Narayan S A:** Yes, I will say that.
- Moderator:** Thank you. As there are no further questions from the participants, I now hand the conference over to Mr. Uday Kotak for closing comments.
- Uday Kotak:** Thank you, colleagues. I think many of you have to run for the next call, so I will finish quickly. As I said, we feel we are in a pretty good position at this stage. Our view is that the economy hopefully will also get a little better. We see greater optimism as we move to the second half. All in all, we are feeling reasonably comfortable and raring to build this business further as we go into the year and beyond. Thank you very much, ladies and gentlemen.
- Moderator:** Thank you. Ladies and Gentlemen, on behalf of Kotak Mahindra Bank, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.