



“Kotak Mahindra Bank Q2FY20 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Kotak Mahindra Bank Q2 FY20 Earnings Conference Call. As a reminder, all participants' lines will be in listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Uday Kotak. Thank you and over to you, sir.

Uday Kotak: Good Evening, friends. Happy to do the call at the end of the second quarter and mid-point of the financial year 2019-20. As you are all aware, this is a very interesting and challenging time in the Indian economy particularly in the first half of the current fiscal, which is April to September when we did see a slowing economy, and a reasonable gradient of that slowdown in the first quarter and also in the second quarter. At the end of the first quarter when we discussed in July, we were all concerned about where the monsoons would end including most projections were talking about less than normal monsoon. Contrary to expectations, we actually had a situation where the monsoons went ahead of normal and actually went on the positive side. In fact, to a certain extent, little late monsoon as well, leading to flooding in many areas. So, the other side of what the expectation was and this is the beauty of variables which we all of us have dealt with leading to some amount of slowing down of the economy in the second quarter by excessive rains in many parts of the country and the flooding. The monsoons have also further pushed into the month of October and therefore have had certain level of challenges for the economy and delay what would have been otherwise a quicker turnaround of the economy. If I look at the gradient of the economy in the first half and ask the question about where do we feel that gradient from here? I do believe that in the second half, we should see flattening of this gradient happening and towards a more normalized sort of situation compared to the steep gradient we saw in the first half of the year. Of course, whenever the economy slows down, it is driven by a few sectors, which have a disproportionate impact on the slowdown. So, in the first half amongst the various sectors, clearly three segments saw a significant slowdown in the economy which is commercial vehicles, passenger cars and also the residential real estate side, and have obviously multiplier effects on the different players across these different segments.

So, when we are looking at the number of the first half, we have to factor in the fact that there was a slow in the manufacturing, auto, real estate sector having impact on the growth of the economy. The question then is, "How does a financial institution like Kotak handle these facts and how do we as a management respond to the reality and the challenges and the opportunities in the Indian economy? And the way we have responded is focused on something we have always deeply believed which is, #1, focus on low cost, stable and sustainable liability franchise as a core of the long-term building of sustained financial institution; #2, have a relentless focus on risk-adjusted returns. And I think it is extremely important to keep in mind the concept of risk-adjusted return at times like these because you do see a situation where in the current state there are pockets of the economy which have stress in the economy itself and inevitably reflect in the numbers of the financial sector and therefore banks.

We have also seen some implications of this in different forms: Point #1, which is our focus on low cost and stable liability, we have grown our CASA deposits now to a ratio of 53.6%. Our total deposit days less than Rs.5 crores, i.e. CASA plus deposit base less than Rs.5 crores, now accounts for 85% of the liability base of the bank, therefore, our continuing journey on low cost and stable liability is something which we have continued through.

Point #2, is with reference to the slowdown in the economy. We have faced this more in the context of actually pockets of rural and semi-urban India where the impact has been greater on the consumer and the retail side than in urban India. This is reflected in two ways; one is in our historical agri crop loan portfolio which we inherited post our merger with ING Vysya where we have seen a higher impact of some of those agri crop loans seeing the pain; and second is in our commercial vehicles business where we have seen the levels of delinquency go up compared to earlier times.

On the wholesale book, we have not had any major hit other than one which is around 100 plus crores single account but other than that there has been no major single hit in terms of individual accounts.

In terms of how we see our response to this is that if we believe that the risks are going up, we would like to also counter it by ensuring that there is enough margin for incremental risks in the economy. And that is something which reflects in our approach to net interest income and NIMs which have been pretty healthy in our context.

Therefore, as I look at the situation with reference to credit costs, we do believe that the credit costs are going to be a little higher than what we had bargained for in the beginning of the year and at this stage our expectation for our credit costs for this year is around 60 basis points mark. Our expectation at this stage for the loan growth is in the mid-teens plus kind of range, supported by better NII and NIM compared to what we had originally estimated. We would be therefore happy to believe that we will get higher NII and NIM versus higher credit cost of around 60 basis points and at the same time loan growth on mix which we are comfortable with of mid-teen plus.

With that I will now request my colleague, Jaimin to take you through the specifics of our results for the second quarter. Of course, we have been benefited by the reduction in tax rates which are reflected in our numbers as well. Over to Jaimin.

Jaimin Bhatt:

Thanks, Uday. Let me just take the standalone numbers first. This quarter post-tax the bank grows with the profit of Rs.1,724 crore which is 51% above the same number last year which was Rs.1,142 crore. As Uday explained, we have had a healthy NII growth. This quarter we saw NII on YoY basis grow up by 25% and we closed the period at Rs.3,350 crore. NIM, we closed this quarter at 4.61% as against the immediately preceding quarter where we were at 4.49%. Fees and other services income, again has seen a good growth. We finished the quarter with Rs.1,162 crore which is 13% higher than the same period last year. On a pre-tax basis, the bank

standalone has a profit of Rs.2,101 crore, 21% higher than last year. The rest of the benefit coming from the tax rate change which Uday talked about. At the bank, our loan book now stands at 2,13,299 crore, which is about 15.3% higher than a year ago. The corporate book accounts for a large part of the book. The corporate and SME grew at 7.5% on YoY basis. The agri book grew at 21%. The small businesses, personal loans, credit card book had a growth of 20% whereas the home loan and the LAP book grew at 23%. Commercial Vehicles, Construction Equipment grew 15.5% for the year though it had a negative growth, small number for the quarter as such. The gross net performing asset at 2.32% as of September which is against 2.15% a year ago. At the net level, we closed at 0.85 as against 0.81 a year ago. SMA-2 at 0.2% of our advances Rs.431 crore. We continue to have a healthy capital adequacy ratio with a CAR of 18.2% with the Tier-1 itself of 17.6%. Our return on assets if I take half year profits is just short of 2% for the year. CASA as Uday mentioned 53.6% at the end of the period. In addition, there is the sweep deposit of 7.1%. Both CA and SA have seen decent growth; our average CA numbers for the half year versus the same period last year is up 22% whereas the savings numbers are up 20%. Cost of savings account, which was 5.65% a year ago has dropped to 5.37%. CASA plus TD as Uday mentioned, TD of less than Rs.5 crores plus CASA is now healthy 86% of our total deposit base as well as the focus on low cost deposits has seen TDs less than Rs.1 crores, grew by 25% on YoY basis. That is broadly the bank highlights.

I will take Shanti to take additional initiatives and then come back for the consolidated numbers.

Shanti Ekambaram:

Thank you, Jaimin. Very briefly, digital as a way of life to us continued and 73% of our active customers are digitally active with most of them being on the mobile and you can see that mobile banking has shown YoY growth of 74%. For recurring deposits and fixed deposits, digital seems to be the way for customers to come in.

We introduced many features in the customer convenience. Some key ones; you can book Ola Cabs through our app, cardless cash withdrawal, tracking of deliverables which is aimed for ease and convenience of customers, including on the asset side, we have seen an increased throughput to digital platform.

More and more customers continue to migrate to digital platform for payments. This is across UPI from IMPS. UPI both the SP as well as P2M has seen a growth and we believe that it will continue as we go into the future. We embarked on API banking many quarters ago, and we have enabled 49 relationships across payments, lending and cash management. We believe that this is the way we will go in terms of collaboration and scaling ourselves.

For our subsidiary, digital continues to be a way of life. Both life insurance and general insurance where incrementally business is really coming through both net and mobile. Jaimin, back to you.

Jaimin Bhatt:

Thanks, Shanti. For the consolidated numbers, we closed this quarter at post tax Rs.2,407 crore, about 38% higher than Rs.1,747 crore last year. Apart from the bank, we had profits coming from Kotak Prime Rs.172 crore against Rs.157 crore last year. Kotak Securities at Rs.149 crore

versus Rs.112 crore last year. The Mutual Fund and the Trustee coming together bringing in Rs.85 crore versus Rs.52 crore last year whereas the other NBFC's Rs.67 crore versus Rs.45 crore last year. The life insurance company getting a post-tax profit of Rs.144 crore versus Rs.127 crore last year. Of course, some of them benefited from the lower tax regime also. Kotak Life, the first year premiums this quarter versus same period last year, grew by 34%. Kotak Securities cash market share for the half year basis is at 9.4%. The assets under management across the group at Rs.2,42,000 crore which is about 21% higher than the same period last year. Relationship value of advisory assets under wealth and priorities about Rs.2,95,000 crore. The total balance sheet size at the consolidated level now crossing Rs.4 lakh crore. Loan growth at the consolidated level at 12%, we are now just short of Rs.2,50,000 crore in advances book. The other segment which is sitting in the NBFC has had a negative growth on YoY basis. Capital adequacy again continue to be healthy; 19.1% overall and 18.7% Tier-1 with return on assets at the group level for the half year at 2.2% and we close with the book value of Rs.325 per share.

Those are the broad highlights for this quarter. Over to taking questions.

Moderator: Thank you very much. We will now begin with the question-and-answer session. The first question is from the line of Deepak Shinde from SBICAP Securities. Please go ahead.

Deepak Shinde: Sir, can I get the gross slippages number for the quarter?

Jaimin Bhatt: If I look at the half year, we are at about Rs.1,800 crore which if I look at the total advances book will be on an annualized basis that would amount to about 1.7% of the advances book; for the quarter the number would be just about Rs.1,000 crore.

Deepak Shinde: How do you see the impact of the external branch banking of loans ? What percentage of our book is currently on floating rate and how do you see the impact going forward?

Uday Kotak: On the question of floating rate loans, I think we believe that this will lead to better transmission and which is good because at a time when you really want the demand to pick up. However, as we have indicated, risk-adjusted return are good and we would like to therefore guide that on NIMs we should be higher than 4.3%.

Deepak Shinde: What percentage of our loan book could be floating?

Jaimin Bhatt: So, of our overall advances book, 70% plus would be floating.

Moderator: Thank you. The next question is from the line of Jinesh Gopani from Axis Mutual Fund. Please go ahead.

Jinesh Gopani: Sorry, I missed the opening remarks on the credit cost guidance if you can just help understand on that more in detail? And generally, on the gross NPA side, sir, are you seeing any big slippages in your portfolio as well given the deterioration in the economic and all?

- Uday Kotak:** I think we did guide that our GNPA as you know has moved a little bit up from the previous quarter and for the year we do believe that the credit cost would be in the range of around 60 basis points give or take. Of course, the slowdown in the first half would have an impact on the overall credit environment and that is being reflected in our numbers for the September quarter. We do not see any big gorillas out there at this stage likely to hit up in the near-term.
- Jinesh Gopani:** But sir, generally do you see things improving maybe after six months?
- Uday Kotak:** In fact, Jinesh, that is the guidance, I mean, in my initial talks I did mention, against the steep gradient which we have seen in the slowdown in the economy in the first half, we do believe that the gradient is flattening.
- Jinesh Gopani:** I know you might not answer this question but just wanted to ask you, given the government what they have done on the corporate tax side, do you expect them to give some stimulus on the personal income tax side as well to prop up demand or it is wishful thinking?
- Uday Kotak:** Jinesh, I will be very supportive of it.
- Moderator:** Thank you. The next question is from the line of Pranav Gupta from Birla Sun Life Insurance. Please go ahead.
- Pranav Gupta:** Just a couple of questions: So, firstly, on asset quality side, like others have also mentioned, the CV portfolio is seeing some stress. So, if you could give us some color on whether it is coming more from the used side or the new side or any specific geographies?
- Uday Kotak:** I have my colleague, Kannan who manages this portfolio day-to-day to give some perspective.
- D. Kannan:** There is no specific color in terms of saying specific geographies, it is across. Also, through both the segments. Broadly, it has got to do with non-availability of loads, very low capacity utilization and freight rates not going up and certain pockets, monsoon also has caused some amount of disruption. So, it is just all these cumulative factors which are leading to elongation of the receivable cycle. If the load factors improve, freights improve then we might see improvement in the collection situation.
- Pranav Gupta:** Is it fair to assume that the quality would be similar across FTO, FTBs and say smaller fleet operators and so on?
- D. Kannan:** No, few FTBs might be slightly worse off than the larger operators and the smaller MLOs will be slightly better off than the FTO, FTBs; but worse off than the larger operators and other operators would be better off.
- Pranav Gupta:** Second question is on the liability side. So, we have seen reduction in the SA rate in a couple of markets over the last six to nine months. So, you are seeing more customer stickiness, what is the thought process, that will be helpful?

- Uday Kotak:** I think on the SA strategy, our view is that we would like to ensure that our customers continue to have superior outcomes banking with Kotak Mahindra Bank. So, that is the core of what we believe. As the rates in the economy softened, we have also responded to them appropriately and which is reflected in our SA cost YoY going down from 5.67% to 5.35%. Therefore, our fundamental philosophy is sticky customers, growing customers, superior SA proposition from Kotak Mahindra Bank in terms of where they can bank with, at the same time being able to communicate to the customer that while we continue to be a superior proposition, we are also sensitive to what is happening in the market interest rate.
- Moderator:** Thank you. The next question is from the line of Vishal Goyal from UBS Securities. Please go ahead.
- Vishal Goyal:** My first question is on your earlier remark in the last quarter on the Swachh Bharat Abhiyan. So, where do you think we are in that process because we are seeing lot of companies getting downgraded, etc., so how long do you think this would take?
- Uday Kotak:** My view on this is something which I have been quoted as well as I do believe that there have been pockets of business in India which are needed to clean the shirt. We need more clean white shirt and I think there is sensitivity in the system to ensure that while we clean the white shirt, we take all the efforts not to tear the white shirt. So, I would like to believe that we are moving forward in a manner towards the cleaner white shirt hopefully not at the white shirt.
- Vishal Goyal:** So, that is clearly the risk playing out right now. The second question which is related to the same is, you have been clearly very-very early in picking stressed buckets, so what are the left over in terms of stress, where is the incremental stress which can come from?
- Uday Kotak:** If you take the last 10-years of history, post-2008 financial crisis when many believed that India will be immune compared to the rest of the world and therefore carried on its merry expansionist process both in project finance and in infrastructure financing. Which I think obviously had significant ramifications in the period 2011-2016 when we saw the real sector pain coming to the financial sector. So, between 2011-2016 we saw the real sector pain to the financial sector. I think post-2016 particularly this last year and post-IL&FS and then of course some of the other financial sector players had the stress coming in. We have seen the pains of the financial sector reflecting on the real sector, and therefore now you have seen a two-way traffic between real sector pain transmitting to the financial sector and the financial sector pain transmitting to the real sector. That is one. Second, I think is that we are also seeing one of the other big challenges. As you know, historically, I always used to feel that in the rest of the world whenever there was a pain, I normally would hear "Oh, there is a pain in the real estate sector in some country which led to slowdown in the economy of those countries." But that never used to happen in India. For the first time we are seeing the pain in the real estate sector in India. I do believe that historically, India never had that issue because India had higher inflation and therefore, real interest rates were not that high. In this cycle over the last many years, India has had high real interest rates, which had an implication on the real estate sector as well. I have got my full management team

here with me and I am going to ask one person who is a part of the Prime Minister Economic Advisory Council; Mr. Nilesch Shah, his view on this question on the economy.

Nilesch Shah: From an economic point of view, we have seen banking liquidity getting disturbed. We have seen interest rates being cut and more are in the offing. We have seen transmission of credit coming under threat, but with PSU bank capitalization and NBFC resolution should improve settling down compared to first half. So, that should result into better growth in the days to come. We believe second half will be better than first half.

Vishal Goyal: One more question related to the same and since we talked about macro, first time we are seeing all the three or four legs of economy namely which is consumption, Capex and even real estate for that matter. Even the government has except real estate like some stimulative ratio, what are the other policy choices they may have?

Uday Kotak: I think we are going very macro. I think we should have a separate discussion on this where we will certainly take up this matter, but at this point of time and I agree with Nilesch on this, I do believe the second half will be better than the first half as I said in my initial comments as well. April to September was a sharp gradient in terms of the slowing economy. We underestimate what delayed monsoon and flooding with some part of the country did to slowing this economy further, particularly in September and October. We do believe that the gradient is clearly flattening, and we have to right this, our view is that it will need a combination of monetary policy and fiscal policy in terms of handling this situation and we are quite hopeful about it.

Moderator: Thank you. The next question is from the line of Sumeet Kariwala from Morgan Stanley. Please go ahead.

Sumeet Kariwala: I have a quick question on retail asset quality. So, if I go back a year, there were very-very small concerns, some early warning indicators going for a toss on the retail book and since then the economy has also weakened quite a bit. So, just wanted to check, how is retail panning out now and what has surprised you positively or negatively if any, from a trend perspective in this portfolio?

Shanti Ekambaram: From retail part, the unsecured retail we mentioned it I think even in the last quarter. It is beginning to show a little bit signs of uptick in stress, and I think that trend continues. The secured retail continues to be stable while the same one-odd things here or there. The secured retail continues to be stable but the unsecured retail, which is largely credit cards, maybe to small extent personal loans, continue to see some uptick in stress.

Sumeet K: Got it. Any comments on the story that was carried by Economic Times today with respect to potential banning of DSAs to originate loans, anything that you have heard or gathered on that?

Shanti Ekambaram: Yes. So, we are also getting clarification, but it's not banning of DSA, it's actually KYC of the customers that they are talking about that the KYC needs to be done for the bank. So, most of

our products the bank does KYC. We are just getting clarification as well. I mean, all the banks are speaking to the regulator because we have also read it in the papers only.

Moderator: Thank you. The next question is from the line of Prakhar Sharma from CLSA. Please go ahead.

Prakhar Sharma: Just a couple of things. One, how do you plan to utilize the tax benefit in terms of either there is a spending or there is a provisioning coverage that you would like to improve? And probably, what would be the normalized cost growth?

Uday Kotak: I think our view on tax benefit is pretty simple; it reduces our cost of capital. Therefore, whenever we look at loans as well as growth in any new initiative, I mean, a post-tax cost of capital has come down, certainly reduces the hurdle at which we take our investment or lending decisions. And, this will certainly help in us being able to take bolder calls, because our cost of capital has come down, which is a structurally positive step taken by the government. Also, we do believe this therefore effectively enables us to take risks at a lower hurdle rate that what we were to take in past, and we will obviously use the lower hurdle rate in our lending and investment decisions going forward.

Prakhar Sharma: And, a related question to that, based on the risk-adjusted returns and the new, probably a lower hurdle rate. Where do you think like a couple of segments where things have improved and where you are sensing that it's gotten worse, and you would rather become more cautious?

Uday Kotak: We debate this internally, and I don't think there is any perfect answer. Obviously, you have got to look at sectors, segments, geographies, everything very carefully. But just to share with you how we as management think, we think if you take the entire stock of lending in India, we would like to believe that there is a give or take, and obviously we can debate on the number, but just as an example. We think about this as a 70:30 world. We think 30% of the current stock of banking assets needs to be examined closer from the point of view of bankability and risk underwriting. We believe 70% of the banking assets or bankable assets, which are what I would call as something which we are very comfortable with. Therefore, we would obviously focus on the 70%, and be far more cautious on the 30%. The trouble is, how do you draw that line between what is 70 and what is 30? That is where our biggest focus is, to be able to identify more and more assets which fits into the 70% bucket and grow that market through this downturn, while being careful about bullets hitting us from the 30% bucket. And this is how we think about risk underwriting, we constantly examine segments and we are not afraid of taking risk, but we believe that if we take more risk, we must get the price for it. If we are taking less risk, we will be ready for a lower price for it. And this is the heart of our philosophy, it's not what we are saying now, we have been saying it and sharing with investors and analysts over the last many, many years. Risk-adjusted returns is the core to underwriting and fundamental issue for leveraged financial institutions like banks. The margin for error is very small.

- Prakhar Sharma:** And my last question is on the use of slippages, we have seen Rs. 1,000 crore in this quarter, you said there was one bulky account that is just about 10% of this number, I believe, at Rs. 100 crore. But do you sense this is sort of...
- Uday Kotak:** A little above Rs. 100 crore but not dramatically, okay?
- Prakhar Sharma:** Yes. Basically, just wanted to get a sense that, you think given where things are this Rs. 1,000 crore is a more normalized run-rate right now or this is sort of kind of an unlikely repeatable level for the near-term?
- Uday Kotak:** I think we are watching the situation very closely. As I have given you guidance, finally slippage reflect in credit costs. We have guided that our credit cost we expect to be in the region of around 60 basis points, give or take. And that is something which we feel is our current view about going forward.
- Moderator:** Thank you. The next question is from the line of Darpin Shah from HDFC Securities. Please go ahead.
- Darpin Shah:** Just wanted to check on the agri part which you mentioned, there is some stress which was visible. So, if you can throw some more light and if you can also quantify how much pain we have seen in this quarter?
- D Kannan:** As Uday said, it is more in the crossroads, erstwhile ING portfolio of crop loans. The portfolio is not very large, and it's not that we are not growing that portfolio, but we are maintaining that portfolio. So, that's the portfolio where we have some issues. Other than that, on the agri term loans, tractor loans and all, in fact we are better than the previous year.
- Darpin Shah:** So, how much P&L change we have seen in this quarter, can you quantify?
- Uday Kotak:** I think on a small portfolio, it's a disproportionate percentage pain. We have basically taken it through our recognition as GNPA and appropriate provisioning. Therefore, it's a large percentage of a small portfolio.
- Moderator:** We will move to the next question. The next question is from the line of Karthik from Investec. Please go ahead.
- Karthik:** Sir, you have done some reclassification of your business banking and corporate banking for the last couple of quarters. And the combined growth rate there has dropped dramatically. So, is the continued decline in business banking portfolio leading to this or has there been a drop in the corporate banking growth rate?
- KVS Manian:** No, there has been a drop in the corporate banking growth rate. Business banking has continued the trajectory as it was, it was flattish, but the lack of growth is in the corporate side.

- Karthik:** All right. And you have actually qualified your corporate asset quality guidance saying that so far there has been no major gorilla hiding. Are there any specific events that you envisage which could dramatically change your guidance on credit cost, either on real estate or on NBFCs?
- KVS Manian:** I mean, at this stage we do believe that we are aware of where the spottiness is, which is within our radar. At this stage, we are not seeing anything which is dramatically different from what our current views on the portfolio are. But these things change, and therefore we are keeping a close watch. At this stage, we are not worried.
- Kartik:** And just a last bit from my end, a number of customer additions on the liability side during the quarter?
- Uday Kotak:** We are adding about more than 400,000 customers a month.
- Kartik:** Right. So, the run rate actually continues that we have had?
- Uday Kotak:** Of course.
- Moderator:** Thank you. The next question is from the line of Kunal Shah from Edelweiss. Please go ahead
- Kunal Shah:** Again, coming on to this risk-adjusted ratio number. So, currently when we see the margins, it's almost like 4.6% odd in terms of margin and there is a tax benefit, which is also coming through, while capital adequacy is very, very comfortable i.e. 18% plus. So, at what level of margins do you think it makes sense to maybe take some risk? Credit cost guidance number is up, but nothing significantly. So, any of these segments wherein we are getting comfortable, because I could see particularly on the CRE side there is a quarter-on-quarter increase of almost like Rs. 1,000-odd crore in this kind of an environment wherein everyone is moving away from CRE. So, what is the reason for that as well?
- Uday Kotak:** Kunal, I think the question that you asked, goes back to a very fundamental point to us. We are not afraid to take risks i.e. if we believe that we have the conviction that the returns are good enough. And therefore, while CRE is a sector that is going through significant challenges in the economy, principle which again I mentioned of the 70:30 ratio is in many ways something which we are very surgically monitoring in the CRE book. Therefore, we are not afraid to lend where we think the risk-adjusted returns are. We don't think real-estate business in India is dead, it has certainly got concentrated and consolidated around fewer opportunities and fewer players. And we are ready to take the calls where we think we can make risk-adjusted returns. Also, I must assure you that our CRE portfolio of what we have picked up is actually in very good shape.
- Kunal Shah:** Sir, what would be the profile of this CRE? And would it be like very chunkier ones which we would have taken, because otherwise maybe our corporate book is also very granular.
- KVS Manian:** Yes, we continue to follow the lack of concentration philosophy that we have in our corporate book. Even in CRE we don't take huge concentrated bets. We deal with A category builders in

all the locations that we operate. And we make sure that we assess the project well. The cash flows of the project in all our lending cash flows of the project are very, very tightly monitored and linked to our exposures. And we make sure that, in fact, most of our loans get paid much before the due dates of those loans, because the repayment is purely linked to cash flows of the project.

Uday Kotak: I think, if I use a cricketing terminology, it's always a challenge for a batsman to decide which ball outside the off-stump to leave and which ball to hit a square cut.

Kunal Shah: Yes. Therefore, I think CRE, overall when you look at it, you said as if one of the key parameter in the risk-adjusted return is again the yields. So, here when we look at this CRE book what would be the average yield on this incremental book, which we have built in one single quarter?

Uday Kotak: It is higher than normal working capital loans.

Kunal Shah: Yes, that has to be the case. So, I am saying, is there sufficient pricing power available and that's the reason like we are seeing adjusted return getting quite comfortable because there are not many lenders out there in this pocket now?

Uday Kotak: I would like to say that there is now an ability to price risk better. I would not like to use wording like pricing power or anything. Finally, it's all about pricing the risk. We think for the risk we are taking, the pricing is appropriate.

Kunal Shah: Okay, great. And finally in terms of 4.6% margin, no doubt we are better than the industry average, but now the strong foundation which we have based on CASA plus the capital adequacy and the liability franchise plus very very low stress, when do we see ourselves growing much higher than the other private banks?

Uday Kotak: We are not scared about growth and we are ready to have. If you have conviction to go against what maybe fashionable for financial institutions to share. Therefore, you can see that we have taken a contrarian call by increasing our exposure selectively to real estate.

Kunal Shah: Yes. So, since we have started doing that, the question is, maybe slightly inching up the risk out there in terms of fee of the segments?

Uday Kotak: If we get the return, certainly.

Moderator: Thank you. The next question is from the line of Saikiran Pulavarthi from Haitong International. Please go ahead.

Saikiran Pulavarthi: Just extending the earlier question, in spite of select pockets there is growth. At consolidated level, the growth has been pretty much lower than some of your peers. I understand that it is because at the overall level you are not finding enough opportunities to grow at maybe relatively higher rates, what are your thoughts over there? Thanks.

Uday Kotak:

I just want to once again clarify that we are not obsessed with higher rates, if the risks are lower. We are ready to do at lower rates if the risks are commensurate with the rates. Therefore, our approach to lending is, for the risk we take, are the price good enough, and should things go wrong at a portfolio level. And that's how we think about it, because finally you and I know the simple equation i.e. ROE is your lending rate, minus your borrowing cost, minus your overheads. However, the biggest factor in banking and finance in India today is that simple line which is the risk cost. Therefore, you take your lending rate, you take your cost of money. Our cost of money fortunately is consistently improving which gives us greater ability to be able to go out there and get appropriate business. Our cost to income ratio is now at 45% as we would see it, and when is the risk cost. And, after that if we can produce returns on that for overall ROE, we are happy to do business. We are continuing to be fundamentally of the view that India may be going through a little bit of a slow patch right now, but we are fundamentally confident that over time the India story is strong. Therefore, we would be happy to grow our market share, in what I defined to you earlier, which is the 70% bucket. We want to be careful about the 30% bucket. Now we can debate whether the bucket is 70:30, 80:20 or 60:40, that's a separate issue. But, what we have defined is the 70% bucket, we are happy to grow our market share, while leaving the 30% bucket where we think even at higher yields the risk may not be worthwhile.

Moderator:

Thank you. The next question is from the line of Gurpreet Arora from Aviva India. Please go ahead.

Gurpreet Arora:

I am referring to slide four where you give the breakup of the advances. If you can help us with some granularity with respect to the home loan and LAP segment, and small business, personal loan and credit card segment, in terms of what the growth rates in these individual segments are, and on how the asset quality is panning out for you?

My second question is with respect to the amortization of the mutual fund fee income. If you can quantify what sort of impact it has had on us during the quarter and during H1 of this year? And, my last question is, if you can help us with the data keeping number on the risk weighted assets?

Jaimin Bhatt:

Okay, let me just take a few of them.. If you look at Home Loans and LAP, that's been reasonably broadly evenly split, and the quality there has been holding up. In addition, as I mentioned earlier, we have had a growth of 20% on the YoY basis, and we are reasonably comfortable with that segment. Slippages or delinquencies are pretty much content in that area. While we talked earlier about the issues on unsecured, this bit is quite secured, and we don't have issues around that at all. So, that's the bit about this one.

On the mutual fund distribution, we look at it, regulations changed by about this time last year, so we are about to hear from there. And, if I look at it as a pure distributor, we would have made about Rs. 140 crore of distribution fees in the first half of the year, which ended up with the year at about Rs. 200 crore. So, that slipped from about Rs. 70-odd crore a quarter to about Rs. 30 crore, Rs. 35 crore a quarter. So, that's the run rate which we are going at right now. And, some

of that would actually stand to benefit as we go forward, because we get more trails as people who have invested there after we start getting more trails as we go forward. Therefore, we will see some benefit actually coming in now.

Gurpreet Arora: And with respect to small business, personal loan and credit cards, if you can help us with some broad granularity?

Jaimin Bhatt: I cannot give you that breakup, I mean, that business also has grown by about 23% odd. And that small businesses, personal loans and credit cards are all lumped in there, credit cards would be about Rs. 5,000-odd crore, the balance is small business and personal loans there.

Gurpreet Arora: Small clarification, the small business line would be entirely unsecured here?

Jaimin Bhatt: No, the personal loan line will be unsecured, the small businesses are typically small businesses and they would be primarily working capital for their businesses, typically sole bankers and there will be secured ones.

Gurpreet Arora: And last, the risk weighted asset number please?

Jaimin Bhatt: The risk weighted assets, you have seen our Basel III disclosure which would have gone out At bank level would be about Rs. 2,43,000 crore and at the group level about Rs. 3 lakh crore.

Moderator: Thank you. The next question is from the line of Pritesh Bumb from Prabhudas Lilladher. Please go ahead.

Pritesh Bumb: Just wanted to check how much is the deposit cost saving from the rate cut which we had done from last two quarters? Actually, this quarter will be the full effect, I think, of the cut.

Uday Kotak: I think we obviously are seeing a continuous improvement in our cost of funds. And, that obviously reflects in our NII and margin. Just to give you an example on savings deposit, even today at a 5.37% cost of savings, versus most banks who are at 3.5% or 4% with an average cost of 3.6%, we currently are about 180 basis points higher than our competition. And, that's the additional cost on our Rs. 80,000 plus crore of savings, about 180 basis points cost which we are taking, which is roughly about Rs. 1,400 crore to Rs. 1,500 crore a year. Through our P&L, and our numbers are after that.

Pritesh Bumb: Sure. Just also can we know that how much will have been falling because of the rate cuts, how much will be falling in the mid segment where the rates are still untouched? So, for example, we have seen a large improvement in buckets from lower or from upper side to lower sides, so some granularity there if we can share that?

Jaimin Bhatt: We have actually maintained the rate of 6% for Rs. 1 lakh to Rs. 10 lakh deposit. So, bulk of the depositors in savings accounts are in that segment. So, that's per that, and even at the higher ones we are offering 5.5% right now.

- Pritesh Bumb:** Right. So, is it fair to assume that it will be 70% in that mid segment where there is 6%?
- Jaimin Bhatt:** Difficult to say that as it keeps moving.
- Pritesh Bumb:** And losses, how much will have been the 811 additions to the savings balances, if you can also share that? Because I think we started it last quarter in full scale.
- Uday Kotak:** Shanti, you want to talk a bit on 811?
- Shanti Ekambaram:** Just to say that after Aadhar coming back, the biometric account opening and digital online account opening, have come back to our original growth and run rate that we have been doing for 811. And, on balances, RD, TD and cross-sell of other products, we continue to see a strong addition for the numbers as well as some of these products on 811.
- Moderator:** Thank you. The next question is from the line of Venkatesh Sanjeevi from Pictet. Please go ahead.
- Venkatesh Sanjeevani:** This is one more question on the growth side. Lets say, if I look at last , one to two years or so, you have done a great job on the CASA side. CASA has improved substantially. The cost of funds have come down, and going forward the tax rates also come down. So, hasn't your hurdle rate for new loans actually come down a lot, which means that you should ideally have been able to grow much faster or maybe the whole, especially the corporate book could have been at a much higher growth rate? Also, in context of competition we have seen a much larger peer of yours, , maybe four time's larger book growing so much faster. So, where is the disconnect in terms of this growth not really being translated?
- Uday Kotak:** I think it's a very relevant question. And I think what we need to do is, while obviously our hurdle rate, cost of funds, cost of capital is coming down, which emboldens us to have a lower hurdle rate of what will be acceptable from a risk-adjusted return point of view which I think it's a very fair point. However, keep in mind that you have to balance with the speed at which the economy is slowing. In addition, the first half of this year, I mean, let me go back to most experts, both in India and globally, without naming them. Most of them, if you went back to even June were projecting the Indian economy growth at close to 7%. Okay? We have the advantage of being closer to the ground to know what is happening on the ground. We therefore did see some of the challenges coming a little earlier before the marketplace recognized the fact that the first quarter GDP growth, that is April to June, is going to be 5%.
- Therefore, we believe that finally the equation is simple. We grow the loan book, we have our spread, we have our cost of capital, we have operating costs, but we are very focused that the risk line is what we need to have an assessment on. And even after the lower hurdle, if we get our risk line in control, we are very clear that we can grow faster. But, we do measure the risk line closer. And our view is not short-term. We think about our lending book, not as something whether I will be hit in the next quarter or the quarter after, or in the next one year. We think

about the lending book like a journey, and it's over a period of time. Because the last thing we want is to come and suddenly have a big issue, 6 months or 12 months from now, or we did some very aggressive lending, the impact of which came to us later. Therefore, that is something which we are focused on. And as long as we get our returns based on that, we are obviously careful, but we are not scared to lend. We want to lend if we can make money at the end of it, because finally we owe it to produce returns for our shareholders, post the cost. And yes, there are different equations, there is cost of funds, there is cost of capital and there is cost of risk. Therefore, we balance all the three and then take the calls. Moreover, if you look at the slowdown in the economy in the first half, I think the loan growth in the banking industry is in single-digit. Therefore when we grow at 15.5% or 15.3%, in that we are obviously going 6% to 7% faster than the industry, while maintaining our risk-adjusted margins.

Venkatesh Sanjeevani: So, in this environment, let's say, even AAA rated rates, say doing working capital loans or things like that, doesn't that qualify your...?

Uday Kotak: Yes, I think the issue there you got to keep in mind, it's very easy. Number one, I think we must be far more focused on so called AAA rated corporates, because I think that itself is something which we do our own credit analysis before blindly accepting a rating agency who says it is AAA. So, that is one important point which we would like to do our internal credit assessment before just accepting any external rating. That's point number one. Point number two is, we do believe one of the biggest problems in India has been concentration risk. And therefore, however good a AAA corporate may look today, we have much tighter norms on concentration risk compared to probably many other players. And it is something which has stood up in good stead over a long period of time. Because this is an environment you just have to look at last 12 months, how many AAAs have become D.

Venkatesh Sanjeevani: So, what is the hurdle rate for the corporate loans, what is the post-tax ROA we would look for it to qualify your lending portfolio?

KVS Manian: So, obviously, we do an account level profitability, it is not about a particular product. But having said that, when we deal with a corporate, we look for a 16% kind of after tax return on equity as a benchmark. We sometimes don't reach it; in some accounts we exceed it. But that's the kind of threshold we currently look for.

Venkatesh Sanjeevani: Right. And with this tax cut the implied yields required to get this will also be...

KVS Manian: Yes, this is post-tax return.

Uday Kotak: The tax rate is lower and the pre-tax is adjusted appropriately.

Venkatesh Sanjeevani: True. That's why I am saying you could have lower yields to achieve the same?

KVS Manian: That's right, because we seek the after tax ROE, so if the taxes are lower, with lower spreads you can achieve the same ROE.

- Uday Kotak:** I think the big issue is today impact on risk-adjusted returns, because if a borrower is rated AAA or capital requirements are also much lower on risk weighted asset basis. But, what we are very focused on is to be sure that so called AAAs, and today even that is an issue. I mean, to be very frank, it's easy to just take some large bites and grow the corporate book, but we have been always focused on making sure that even our corporate side is reasonably granular. So, that even if there is a risk hit, we don't get large hits at a point in time. So, our philosophy has been to keep it granular and not take bulk deals and take concentrated risk and grow that book.
- Venkatesh Sanjeevani:** Take your point. I mean, just maybe as a feedback from what we are seeing as investor community is that, maybe putting on the side of caution here, especially when a large part of PSU banks seem to be busy with integration, and that's a feedback we get as well that there's a lot of opportunities to lend there.
- Uday Kotak:** Yes, I agree. It's a very good feedback. I think it's something which we will certainly keep in mind and something which is our focus. However, we have to manage it without doing disproportionate concentration. Because what is also happening is that in many large corporates, many of the banks have reached their concentration norms. And, just because we have limit in our concentration norms, we don't necessarily want to reach those limits if we believe fundamentally we want a philosophy of no excessive concentration.
- Moderator:** Thank you very much. Due to time constraints, we will take that as the last question. I would now like to hand the conference back to Mr. Kotak for closing comments.
- Uday Kotak:** Thank you very much, friends and colleagues. This has been a very important two-way debate and discussion at a very crucial time in the Indian financial sector, and the Indian economy. We do believe that this is one of the interesting challenges in the Indian financial sector. I hope that India and Indian financial sector navigates out of this without having too much of sort of moves which then, without having any disruption we hope, we would like to believe that a stable financial sector is crucial for the growth of the Indian economy. We at Kotak do see this as a significant opportunity and challenge. Yes, there is some amount of mud in the water coming out of the challenges in the financial sector. And, we are working towards making sure we swim well, while ensuring that not too much mud sticks with us. But certainly, open to swimming faster and growing in this environment, while managing our risks carefully. Thank you.
- Moderator:** Thank you very much. On behalf of Kotak Mahindra Bank, that concludes the conference. Thank you for joining us, ladies and gentlemen. You may now disconnect you lines.