“Kotak Mahindra Bank Limited Q3 FY16 Earnings Conference Call”

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MANAGEMENT: **MR. UDAY KOTAK – EXECUTIVE VICE CHAIRMAN & MANAGING DIRECTOR, KOTAK MAHINDRA BANK**
MR. C JAYARAM – JOINT MANAGING DIRECTOR, KOTAK MAHINDRA BANK
MR. MOHAN SHENOI – PRESIDENT –IN CHARGE OF INTEGRATION MANAGEMENT OFFICE, KOTAK MAHINDRA BANK
MR. JAIMIN BHATT – PRESIDENT AND GROUP CHIEF FINANCIAL OFFICER, KOTAK MAHINDRA BANK
MS. SHANTI EKAMBARAM – PRESIDENT - CONSUMER BANKING, KOTAK MAHINDRA BANK
MR. NARAYAN SA – PRESIDENT - COMMERCIAL BANKING, KOTAK MAHINDRA BANK

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the Kotak Mahindra Bank Q3 FY16 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 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 New Year to you all. I am in fact in a car on my way back from the RBI's office after attending a meeting which the RBI called with banks and financial institutions this afternoon. Friends, as we look at the New Year it has begun as we all know in a pretty interesting and tough beginning. So first, let me start with a little bit of macro particularly in the context of what is happening in the world and in that context India. When I look at the Indian perspective the good news is, low commodity prices, which is a significant benefit to India's current account on the import side and that is certainly helping us. Having said that, with low commodity prices India also runs some risks of accidents with some of its commodity producers and corporates in India and also overseas. Against the low commodity prices we also have to keep in mind, it is having some impact on our exports, our remittance flows, and, of course, from the global side continuing to see negative portfolio flows into India. The domestic savings in India had seen a pretty good flow from the domestic mutual fund industry through 2015. While it has been good till now we got to keep in mind that if markets keep on going down, the domestic savers who were going into riskier financial assets may move into safer assets like fixed deposits or high quality debt and credit. So this is the environment in which we are. In that context, I think of the banking industry and the credit cycle in India, the water has finally spilled out of the can as was expected and we would see a continuing flow of adverse credit flowing out into the number which banks and financial institutions in India report over the next few quarters. So this is the backdrop which we see. Another very important factor which is happening is that while real GDP may be around 7%, the normal Indian phenomenon has been real GDP plus 6% for inflation. So, in that case nominal GDP which should have been 13%, is now currently running as of September at 6% nominal against real of 7%. The estimates for the full year are nominal GDP of somewhere around 7% to 8%. Therefore, you are actually seeing the impact of low WPI feed into the decelerator and therefore nominal GDP growth of India which is the rupee growth which forms the basis for the economic activity as we see on a day-to-day basis, now at a level of about 7% to 8%.

So, in this context, what does it mean for us at Kotak Mahindra Bank? First of all, something which we have always believed with conviction in a philosophy of looking at credit, purely and surgically from the eyes of risk adjusted returns, it is our philosophy which we have done in the past and we continue to do even now including post-merger with ING Vysya Bank. And I am happy to report in that context that we have stayed the course and we see ourselves continuing broadly with the credit cost which we have guided you for this year arising significantly out of the merger with ING Vysya Bank at around 80 to 85 basis points for this full year. The guidance of Loan growth at around 15% for this year after adjusting for the "bad bank" which we have internally created out of the erstwhile ING Vysya portfolio. So, we believe that this is a time for us to make sure that we do not make any major new mistakes and actually gradually focus on getting some of the share of better quality business.

I have very good news to share with you on our Liability Franchise: Kotak Mahindra Bank standalone is growing its SA average in excess of 40% and the ING Vysya network is now kicking in at 30% plus and therefore on a combined basis we are reporting extremely healthy growth in SA. Similarly on CA, we are growing in the 20% plus range on a combined basis, therefore our overall CASA growth and customer acquisition on the liability side continues to be going pretty strongly. We also see the integration process which my colleagues will talk about shortly, broadly on course and we hope to complete it by April-May next financial year to work towards a fully integrated combined bank.

One of the other highlights of our current year's performance is also the extremely good growth that we are getting in our subsidiary -- Kotak Life Insurance -- which is helped again by the merger to a certain extent and also independent of that is now growing our Life Insurance business at a pace which is significantly faster than the industry growth.

In terms of summing the overall mood, while we continue to be focused on measuring our risk adjusted evaluation on credit carefully we feel pretty good about the liability franchise, the overall banking and fees franchise, the phenomenal progress we are making on the Digital Franchise, which again we will share with you and some of our subsidiaries are also beginning to now contribute significantly towards long-term growth. So I would say that as the markets get tough, there is an opportunity for us but first of all we have to be extremely alert; not make mistakes in a high risk environment; but at the same time use this opportunity to gain share and grow significantly particularly on our liability and services franchise.

With these broad words, friends, I will now hand it over to Jaimin Bhatt to take you through the presentation along with my colleagues and then we will be happy to answer Questions after the Presentation. Over to you, Jaimin.

Jaimin Bhatt: Thanks, Uday. Let me take the bank's standalone numbers first: For the quarter ended December 31, 2015 bank's standalone - we have recorded post tax profit of Rs.635 crore. I am going to talk more about the P&L which is on Slide #8 where the Net Interest Income in the current quarter we have seen at Rs.1,766 crore, about a 5% higher than the immediately preceding quarter. Our other income this quarter was Rs.722 crore. In the previous quarter we had taken a reversal of income of Rs.62 crore, so, that was impacting the previous quarter numbers. At the overall cost level at the bank, we are pretty much at Rs.1,283 crore, just a marginal rise over the previous quarter and that is also thanks to the fact that this quarter we had a campaign on "Ab Phone Phone Mein Kotak" which had impacted the operating cost. We have taken a total provisioning cost in this quarter of Rs.235 crore. This also includes provision towards security receipts and other investments of Rs. 84 crore. In fact, as Uday touched upon at the end of Q1 when we talked in the first call after the merger, we had looked at the acquired book from ING Vyysa Bank and about 6% of the funded and the non-funded book which had come around was somewhat stressed and we called it the "Bad Bank". Bulk of this is being managed by our internal ARD team and we have taken provisions. In the first quarter, we took about Rs.305 crore, the second quarter including the derivatives which I had talked about Rs.238 crore and Rs.235 crore in this quarter. Bulk of these provisions have come from the acquired book. We end up with estimate for the current year at about 80 to 85 bps on credit cost. On integration, we had estimated a total spend of about Rs.200 crore. Till date we have spent Rs.142 crore including current quarter Rs.13 crore and we certainly should be under Rs.200 crore number which we had estimated at the beginning of the merger period.

Before I get into the other details of the results, just giving it to Mohan to explain much more about the integration and where it stands.

Mohan Shenoi: Thank you, Jaimin. Q4 FY16 brings us to the final phase in the integration journey. I am happy to inform that in terms of all the dimensions of integration, whether it is people, process, technology and synergy, we are proceeding as planned. All technology projects are proceeding satisfactorily and as planned. Major business verticals which were to be integrated in this quarter have been integrated as per plan. Even integration of support functions is almost complete. In order to familiarize the branch staff in "profile" branches of eIVBL we have rolled out Finacle in phases so that they can familiarize with Finacle, its systems and processes surrounding it.

Integration has now reached a matured stage where combinational synergy is beginning to accrue. The enhanced network effect is clearly visible. In addition, 6% interest on CASA is helping in accelerated acquisition on the IVBL side. Average SA as Uday mentioned earlier, has grown 31% on a YoY basis at eIVBL branches and at Kotak branches even higher at 41%. And customer acquisition: we are adding about 100,000 customers a month, CA is growing at 32% YoY and we are seeing significant traction in Insurance cross sell, Credit Cards, 3-in-1 Trinity accounts which includes Kotak Securities accounts. Even in the Privy segment we are seeing excellent opportunities in the combined network. On cost benefits, despite adding SA on the front line we are seeing cost synergies accruing in the last two quarters. Overlapping branch rationalization and space rationalization is saving rental cost and disposing of non-core own premises that also is progressing well. So that is on merger integration.

I now hand over to Shanti for giving us Status Update on Digital Initiatives.

Shanti Ekambaram: Thank you, Mohan. We saw mobile transactions of Rs.2300 crore value in December which in April was just below Rs.1, 000 crore. So, we saw almost 133% growth in value terms in April and almost doubling of volume. We are highest amongst banks in terms of growth in Mobile value of transaction. 46% of our active customers are digitally active. We have 6.8% share in value of overall Mobile Transactions at the industry level while our industry share of Advances and Deposits are just 1.6% and 1.4% respectively. 50% of all incremental TDs are booked online. We are ranked No. 5 in terms of Value of Mobile Transactions across all banks. Our mobile app with 80 plus features continues to be one of the highest rated banking apps in India. Digital Payments transactions crossed 1.5 million transaction volume in the month of December.

So, in the bank we have seen a good growth in Mobile adoption and value of transactions. Our focus will continue to be on Mobility, increased Customer adoption, transaction volume and value. Digital is not restricted to the bank alone.

We have done a lot of activity in our subsidiaries as well and I will briefly talk about it too; under Kotak Securities, mobile transaction, value of trade in the month of December was close to Rs.5,000 crore, we crossed more than Rs. 4,000 cr last month. In the cash segment, we are clearly market leaders with about 30% share. Number of trades on the Mobile App crossed over 3 lakhs a month and contribution of Kotak Stock Trader app to overall brokerage crossed 7%. We continue to work on value added services on the Digital and Analytics for our customers; as well as our internal sales force in order to enhance the entire digital value proposition. In Life Insurance our end-to-end tablet based solution crosses 10,000 policies in 2015; we call it the Genie. 19% of the business in terms of premium came through Genie in the month of December. We have got 3.7 lakhs customers registered in the online portal, 14% of renewal premium is coming through Digital platform, thus in addition to the bank we are also focused on our subsidiaries to increase our Digital quotient in that.

I hand it over back to Jaimin to continue with rest of the highlights.

Jaimin Bhatt: We take some of the other highlights of the bank's standalone for the quarter. We end the quarter with gross NPA number of 2.3% and a net number of 0.96%. Our total restructured considered standard advances are small number of 0.3%, again; of which a large portion has come from the acquired portfolio from eIVBL and as in the past we have not done any of the CDR participation or transfers to ARCs or conversion to balance sheet, 5/25 or rectification post the merger period. Our net interest margin for this period was 4.3%. As regards the segmental numbers for this quarter, out of the Rs. 970 crore of pre-tax profit, the Corporate and the Wholesale Bank brought in profits of Rs.547 crore, Retail Bank Rs.318 crore, a bit lower than the previous quarter; this quarter the advertisement cost as well as some of the branch increase premises costs are sitting in the Retail Bank. Treasury segmental P&L at Rs.105 crore; last quarter, the Rs.62 crore hit which I talked about earlier was sitting in the Treasury segment.

Advances at the bank standalone end the period at Rs.1, 15,000 crore. We have seen growth in each of our three verticals --Corporate, Commercial and the Consumer Bank. We have seen growth coming in larger from the small businesses and the Business Banking areas in this quarter whereas Agriculture Advance division has seen a small dip. After a gap we have seen the Commercial Vehicles pickup in this quarter and that has continued.

Balance Sheet: As Uday mentioned, the CASA at 35% at the end of the period; we also end with a pretty healthy capital adequacy - 15% Tier-I and 16.2% at overall capital. 1,298 branches are where we end December 2015 with, we are on plan to reach 1,400 branches by calendar 2017. As regards Current and Savings Account, we are much more focused on the average numbers; if I look at average current account numbers, we have seen growth in this quarter from Rs.15,100 crore in the previous quarter to Rs.16,300 crore this quarter. If I look at Y-o-Y averages for December quarter versus this quarter almost a growth of 30%. On Savings Account, as Mohan mentioned, the ING Vysya branches are showing average growth on Y-o-Y basis of 31% whereas the erstwhile KMBL branches are showing a growth of 41%. So, both the CA and SA are on a healthy growth basis. Our total CASA plus Term Deposits below Rs.5 crore are now at 69% and with our overall Term Deposits below Rs.1 crore at Rs.35, 000 crore now. TD sweeps accounting for another close to 5.5% of our total deposit base with a cost of savings account continuing to be at 5.5%. At the consolidated level, we ended the current quarter with post tax profit of Rs.945 crore with overall loan book of Rs.1,41,000 crore. At the consol level we reported net NPA of 0.85% and our overall balance sheet size was Rs.2, 29,000 crore. We talked about the overall advances in the bank at Rs.1, 15,000 crore, our consolidated total advances are at Rs.1, 41,000 crore. We have seen auto loans grow by about 15% plus on a YoY basis; we have also seen this quarter growth in the capital markets related advances.

Coming to the Entity Wise Profits; apart from the bank's contribution of Rs.635 crore, Kotak Prime had post tax profit for this quarter at Rs.126 crore, Kotak Mahindra Investments, the other lending entity at Rs.39 crore, the Insurance company at Rs.60 crore, Kotak Securities at Rs.55 crore, the mutual fund which is the AMC and the trustee company' we have taken hit on an operational loss during this quarter resulting in the profit being lower this quarter at Rs.4 crore compared to Rs.23 crore in the previous quarter. Our overall net worth as I said is Rs.32, 349 crore with Rs.23, 300 crore at the bank itself. In Kotak Prime, total NII for this period at Rs.247 crore, post-tax profit of Rs.126 crore for this period. The overall advances in car book has grown to Rs.16, 400 crore and the non-car assets at Rs.5, 400 crore with NPA number net at 0.4%. Kotak Mahindra Investments total advances book is now at Rs.4, 761 crore, net NPA of a small number of 0.06%, post-tax profit of Rs.39 crore sitting on a pretty healthy capital adequacy in that entity. The Life Insurance entity, as Uday indicated, has had a strong growth while the Private Sector Insurance industry has grown in this 9-month period at 13%, Kotak Life has seen a growth of 78%. On APE basis, the bank including the merged entity is now contributing 48% of the premiums of Kotak Life, Group business also has grown by 50% on a Y-o-Y basis. On a quality issue also the persistency has improved, so as the conservation ratio. Surrenders have gone down and the number of lives covered has gone up by 47% on Y-o-Y basis. Investment performance of 100% of the equity funds was in the first quartile.

At the asset management company, on average AUM basis, Kotak Mutual Fund now stands at No. 8 on the ranking charts. On equity AUMs, market share is now at 3.3% as against 2.6% in March 2015. In addition to the Digital elsewhere which Shanti talked about Mutual Fund now offers a fact sheet on Mobile which is first of its kind initiative. Overall, assets under management across the group now at Rs.95,000 crore, apart from the Mutual Fund, offshore funds is now at Rs.21,000 crore. Kotak Securities this quarter has seen a volume drop across the market, market ADVs has been decently lower at Rs.2, 40,000 crore as against Rs.2, 80,000 crore in the previous quarter. Kotak

Securities average daily volumes this quarter is at Rs.6,481 crore. Profit for the quarter post tax is at Rs.55 crore with the market share YTD basis of 2.7%. The Investment Bank has been involved in a number of deals in this period like IPOs of Indigo, Coffee Day, Dr. Lal's PathLabs and SH Kelkar. They have also been in the middle of several M&A transactions for this quarter with income of Rs.28 crore and post-tax profit of Rs.6 crore for this quarter. These are broadly the highlights for this period. We would be open to taking questions from you.

Moderator: Thank you very much. We will now begin the Question-and-Answer Session. Our first question is from the line of Prashant Poddar from ADIA. Please go ahead.

Prashant Poddar: One book-keeping question on these international subsidiaries and investment advisors. If we look at the numbers in subsidiaries, the profit numbers have gone up significantly from Rs.33 crore last year to Rs.83 crore. What is essentially the components of this business and what is leading to this growth? And the other one is for Kotak Investment Advisors, It has come down from Rs.15 crore to zero, while there is still some net worth lying in this business. Just trying to understand what is this about.

Uday Kotak: As we spoke earlier, the international subsidiaries are into asset management; the assets under management in the international subsidiaries have grown over the period and that has been one of the major reasons for the better performance of the international subsidiaries on Y-o-Y basis so that Rs.83 crore includes Rs.26 crore which has been clocked in the current period. Investment Advisors is the domestic unit which are the advisors on the alternate asset piece both in private equity & real estate. In the current period, we are more in the process of raising funds; we have had some of our old funds giving back money and to that extent there have been expenses on raising funds as well as we have taken some hits on some of the investments which we have been sitting on in terms of MTM. So, to that extent that entity while is pretty much in the market to raise funds in each of the verticals which it is operating in, has taken a hit in the current period, to that extent that is the negative for the period.

Prashant Poddar: Quickly on the impact, we keep hearing about this RBI's initiative to try and clean up the PSU banks… generally corporate bank's bad exposure. So while your assets might be largely distant from those accounts, do you expect any significant spillover impact from those larger NPL recognitions and, therefore the likelihood of banks not continuing to support some of those large accounts in next one or two years. You might not be directly lending to some of those large groups, but in the chain below them, if the cash flow support to those larger groups go away in case of recognition of NPL, do you expect any kind of spillover impact over the next one or two years because of these issues?

Mohan Shenoi: Generally, no from the spillover but however if sectors like commodities and all continue to be under pressure, you might see impact spreading to wider base of corporates but immediately arising from these corporates I do not think there is a likelihood of any spill over at this stage because the stress in a lot of these corporates is not recent, liquidity stress has been for a reasonable period of time, just that recognition is happening now.

Prashant Poddar: On the net interest margins, given that a lot of banks are trying to lend to the similar segments like high quality corporates, mortgages, etc., do you expect margins to generally come under pressure in the incremental years, also your mix of business is changing?

Uday Kotak: Overall I think we keep our modulator mix so that the NIMs generally are in this range

Moderator: Thank you. The next question is from the line of Ashish Sharma from ENAM Asset Management. Please go ahead.

Ashish Sharma: First question is on the cost-to-income ratio. We have sort of seen an improvement quarter-on-quarter to 51.6% for Q3. Do you see this number to be sustainable? What are the reasons for such a sharp quarter-on-quarter improvement in the cost-to-income ratio?

Uday Kotak: Cost-to-income we have guided that next year we would like to be below 50% and we continue to stick to that guidance. If you look at this quarter we are, for the quarter, about 51% cost-to-income.

Ashish Sharma: Second question on the growth part. I know this is not an environment where we can sort of see what sort of growth in the system would be there, but given we had guided for 15%, 16 is predominantly done with, but for the year going forward, where do you see the normalized growth for bank itself should be?

Uday Kotak: I think the way you got to look at this is we feel reasonably confident to be growing at somewhere around 2x nominal GDP, because finally this is rupee growth, therefore if nominal GDP currently is running at the rate of around 8% which is the guidance by the government for the year, remember, as of September, nominal GDP was below real GDP and therefore I would be actually rather than giving you a percentage give you broad guidance that we think we can grow at about 2X nominal GDP broadly and give or take, I mean, if we feel very conservative we may go down to somewhere between 1.5-2 and if we feel reasonably confident we will go to around 2x nominal GDP. Keep in mind that there are two ways we will grow -- one is obviously organic and at this stage we are seeing pretty decent traction on consumer urban. We are going up the curve on Corporate in terms of the quality we are doing. At this stage if you look at our numbers on Agri, we have actually started being cautious over the like last 9-months and you can see actually that growth has slowed down again by choice. So in many ways we would like to temper where we grow we do not want to be doing something which is completely against the wind, at the same time we see that as capacity constraints come in Indian banking, we would be able to get good accounts from the broader competition set, therefore happy to grow carefully, but at the same time we do not want to be the suckers holding somebody else's problem.

Moderator: Thank you. The next question is from the line of Vikesh Gandhi from Bank of America. Please go ahead.

Vikesh Gandhi: Just had a couple of questions. One is I think you partly answered just right now, but just wanted to understand the Home Loan growth which I was looking at has probably come down at least sequentially. So what is your thought on that piece?

Uday Kotak: So Shanti on Home Loans and Jaimin on Treasury.

Shanti Ekambaram: We continue to be steady as far as Home Loans growth is concerned. As mentioned last time that we are joining more and more to our own customers and our own network. But we have seen steady growth as far as Home Loans is concerned continuing even in this quarter.

Jaimin Bhatt: Actually, if you look at the Home Loan growth on Slide No. 11, we have grown of course a small amount from Rs.21, 697 crore as of September to Rs.22, 327 crore for this period. So it has been about 3% growth in a quarter.

Vikesh Gandhi: Yes, Jaimin, that is what I was referring to. So last quarter, you had grown much faster. So I was just trying to refer to the sequential higher growth coming in slightly, I mean, that has grown, but it is obviously slower than the last quarter, so which is what I was just trying to read something into it?

Shanti Ekambaram: One of the factors you could take into account is that this quarter there were a lot of holidays as well. While we can say festive season should see spike in loans it remains where it is. I think we will continue to see a steady growth as far as Home Loan is concerned and we have neither pulled back nor sort of seen any other factor

Uday Kotak: At the same time I think you have to be clear; especially in urban India, other than Bengaluru probably, most places people are buying new homes a little slower.

Vikesh Gandhi: Secondly, if I could have the treasury gains that could have been made in this quarter because that disclosure is not there in the press release?

Jaimin Bhatt: Treasury what we talked about is the treasury last quarter as I mentioned has had a hit of Rs.62 crore. So that has been accounted for in the second quarter. So if you look at the fee income which was given out, this quarter is Rs.256 crore against Rs.159 crore last quarter; last quarter had Rs.62 crore, so if you kind of add that it is about Rs.221 crore. This quarter, yes, there has been some treasury gains both from money market related stuff as well as on the equity stuff. So that is kind of accounting for the delta which has happened this quarter.

Moderator: Thank you. The next question is from the line of Adarsh from Nomura. Please go ahead.

Adarsh: Just a question again on the core fees side. I think last time you made a mention that businesses are getting realigned and hence takes a while for client business to pick up on a merged basis. But comparing nine months, adding up the two businesses both ING and Kotak's previous numbers and now, we still see that 9-months numbers are flat even if adjust for the Rs.60 crore of one-off write-off or charge that you had last time. So I am just trying to understand whether the fee streams have normalized now and one should expect the growth in line or higher than balance sheet?

Jaimin Bhatt: If you look at on a 9-month comparison, yes, Rs.162 crore which we talked about, plus we had seen a lot of the spiky numbers which was there in the erstwhile ING which is not there going forward. There is on a variety of accounts, some of which we talked about last quarter as one-offs which have got built up altogether.

Adarsh: So from here on you would expect that you would also try and move up the levers on fees for ING as well, but overall would you expect fee growth to be like in line or probably higher than balance sheet given that you have kind of run off all those lumpy fee streams now?

Jaimin Bhatt: It should be in line or marginally higher than the balance sheet growth. I have also had one more thing in terms of last year versus this year comparable. We are among the largest distributors of mutual fund across the country. If you look at mutual fund distribution revenues last year versus this year, it has taken a big hit on account of regulatory changes and what not. So there has been one or other account on which other income has fallen.

Adarsh: But that should ideally come as trail income so it should help you in the next couple of years?

Jaimin Bhatt: That will help going forward, but when one is comparing this year nine months versus previous year nine months that has been a decent hit.

Moderator: Thank you. The next question is from the line of Kunal Shah from Edelweiss. Please go ahead.

Kunal Shah: Firstly, again coming back to growth, so when we look at the other private banks in a similar space, they are still growing at say 20% plus. So holding on to say 1.5x GDP, would it be more a function of say the run-downs which are happening say on account of integration or maybe overall environment; we are slightly skeptical in terms of say the things turning positive over next 12 to 18-months and that is the reason we would still want to go slow?

Uday Kotak: I think, let me first say that our view is that we need to look at our combined balance sheet post the merger. So, when you are looking at comparable growth on a combined balance sheet, keep in mind, that from ING Vysya Bank, as we have disclosed in the first quarter, there is a 6% book which has been moved to the "bad bank". Therefore, that obviously, we are not growing. If at all we are running it down to the extent which we can recover. Therefore, the comparable numbers have to be adjusted for this because that is the piece which has been completely segmented and alienated. Therefore, the year-on-year or any comparison we need to make is from the book as we call as the performing book excluding the "bad bank". As I have said, our philosophy is we are not constrained by anything, we are constrained only by one major parameter on the basis of which we measure all our performance which is our best judgment of risk adjusted returns because that is crucial for a sustainable credit business at 10:1 leverage, which is what banks are. Therefore, we must make those hurdles on risk adjusted returns and accordingly, we will use that as the basic discipline. Based on that, our experience over the years shows that in a reasonable market we can grow at 2x nominal GDP. We certainly believe that we have significant capacity available. And at a time when the banking industry is going through its challenges, we will be able to gain some share in various segments which is what we believe will get us to around the 2x nominal GDP levels of growth. At the same time we got to be very careful because in this commodity cycle, there are new players who run the risk and some of them could be even big names. Therefore, you want to be careful that you guide yourself and navigate yourself through this because there could be big bullets out there which are not even so far seen or recognized.

Kunal Shah: Particularly, say, in small business; PL and Credit Card, which is almost contributing to 25% of the incremental growth, so this is largely a small business piece or say the unstructured piece which is growing?

Shanti Ekambaram: Both actually are growing. The small business piece is basically working capital to small companies which ranges anywhere from Rs. 50 lakhs to Rs. 2.5 crore or up to Rs. 5 crore. We are seeing a strong growth in that segment as well. For us, it is an acquisition and that is all against collateral and cash flows. We are also seeing the credit card business growth at a reasonably healthy pace.

Kunal Shah: Within Kotak Mahindra Prime, the others which is growing, so what is contributing to that maybe almost like say Rs.1,200 crore kind of an addition sequentially on the non-CAR side?

Jaimin Bhatt: Kunal, I mentioned that earlier we have seen in this quarter capital market also going up but it is financing of capital markets.

Moderator: Thank you. The next question is from the line of Nilanjan Karfa from Jefferies. Please go ahead.

Nilanjan Karfa: Question one is, we started with roughly I think Rs.30 billion of stressed asset from the eIVBL, funded and non-funded included. How much of it is currently lying with us and how much of that we have recognized?

Uday Kotak: The debate always is, #1, what is the best IRR you get on a stress asset piece versus quick fire sale versus resolution through the legal process. So it is always a trade-off. We do it pretty-pretty surgically measuring it from an IRR point of view from the time it goes into the bad bank. So at this stage, there is work in progress. We are making some progress in some accounts. We have actually got some of the cash flows back as well. But, I must say that in this environment progress is slow but steady.

Nilanjan Karfa: If I can just reverse that question, when do we expect reasonable IRR to come through – is it going to be mostly in two years from now?

Uday Kotak: Let me just divide it into two parts – first, for this quarter our ARD division was more or less flat, hardly made any money this quarter. So our numbers are without any profits from the ARD division which is one broad picture I would like to give you. The second part is there are really two ways to look at this – on the accounting side we continue to keep on providing based on more conservative basis and then we would like to see some of it come back. That is our typical way of looking at this. We have guided 80-85 basis points credit cost for this year. So, on the accounting side, it is continuing to go down that path. We will come back to you with final guidance in next year, our credit cost for the next year, but we believe those will be normalized, and obviously this visibility changes as we go forward, but at this stage we do not see anything which is dramatically bothering us from a credit cost point of view into next year towards normalization. So that is one guidance I will give you. On the revenue side, we think all these flows in the next 18-30 months.

Nilanjan Karfa: Question No. 2; when I look at expenses, both from consol book as well as the bank, if you look at building out liabilities that is where most of the costs go, it is running at almost several years lows today. Obviously, we have not been investing because we are in the process of merging. So would you expect this number to kind of increase next year and by how much?

Jaimin Bhatt: Just to add, it is not that we are not investing, in fact, since the merger, we would have added several people to the headcount.

Uday Kotak: See, how the future is. We certainly are continuing maybe a little slow and measured pace on physical infrastructure, we believe we have to have a two speed engine now, we just cannot blindly go into only physical infrastructure; there is a whole digital piece which is also extremely important for these two speed engines.

Nilanjan Karfa: Mr. Uday, any clarity on what the RBI discussions have been so far mainly on these accounts people have been talking about, that will be really helpful?

Uday Kotak: I suppose RBI will put out a press release this evening.

Moderator: Thank you. The next question is from the line of Aditya Narayan from Citi. Please go ahead.

Aditya Narayan: I have two questions; the first is really you have talked a lot about Loan growth of 15%. But one of the things that is standing out is there seems to be a lot more momentum on the Liability side; on the Deposit side. Now looking out 6 to 12 to 18-months, suppose the Loan growth environment stays the same, what do you do with the liability side which is one of the objectives of the acquisition, where you are getting a lot of momentum but maybe there just would not be opportunities to kind of deploy it, how are you thinking?

Uday Kotak: Aditya, if we get liability growth of CA, I am sure that it is accretive even if I put it in T-bill. On SA, our average cost is currently 5.5%. Because we are growing fast and we see value and deposit rates, even now the retail deposit rates of most banks are close to 8%; 5.5% average cost and our treasury bill is at around Rs.725-750 crore. At this stage, the liability franchise on CA and SA without credit risk also is accretive. Obviously, we like to take the credit risk incrementally provided for that incremental risk we get higher than incremental return. We think therefore, the liability franchise around CA and SA is something which can sustain through any asset period. But look at the reverse; if the status of Indian financial sector goes through these challenges, what are the two major things on the capacity side a financial institution will need? No.1 capital and No. 2, enough bucks in the bank. So, we are actually positioning ourselves to a belief that these two shall path at some point of time, and by that time, if we have geared up our capacity disproportionately, we would be in a position to make those incremental margins even on credit. That is the plan.

Aditya Narayan: This was asked in part before on the asset reconstruction side. Obviously, there is a market that is beginning to open up and you have decent expertise on this over an extended period of time. But from a capital allocation perspective, any thoughts that you have in terms of how much you would commit, in what form could you think of committing it and whether you think this is a good enough time to start making such commitments?

Uday Kotak: I will request my colleague, Jayaram, who is working on some special situations funds where we will put capital by the side and we are talking to one or two large institutions globally to do some sort of structured venture there. This is just in a debate stage, therefore, it is not anywhere near to a finalization yet.

C. Jayaram: We are hoping to sort of close some sort of a fund in which a large institutional investor will sort have come in along with us. Clearly, we are seeing a lot of opportunities here. We have a team which has started looking at transactions and we believe that there is clearly a lot of potential in terms of getting in right now because unlike earlier times I think people are now talking reasonable evaluations in terms of some of these assets. So I think if we can raise that funds then there would be great opportunities in terms of getting some of the valuation and we would be allocating resources from that as well.

Uday Kotak: Aditya, one of the issues in this whole - putting money to work in the stress is most of the assets which are carried currently by banks are not at fair clearing price. Therefore, for us to be able to put money to work on a cash basis, we need fair clearing price. If we get fair clearing price with appropriate returns because there is an element of equity risk in these transactions, we will put money to work certainly.

Moderator: Thank you. The next question is from the line of Sameer Bhise from Macquarie. Please go ahead.

Sameer Bhise: Just a data question; what is the employee strength as of now on a standalone basis?

Jaimin Bhatt: About 31,000 as the bank standalone.

Sameer Bhise: Comparable numbers for 2Q if that is possibly easy?

Jaimin Bhatt: We possibly added about 500-600 people at the bank standalone business.

Uday Kotak: This is all front-end into ING Vysya branches primarily.

Sameer Bhise: Just trying to make a sense of the decline in staff cost?

Uday Kotak: I think it is pretty simple; we are adding front line and we are getting tighter on supervisory.

Moderator: Thank you. The next question is from the line of Sampath Kumar from IIFL. Please go ahead.

Sampath Kumar: Just wanted to get some picture on FY17. FY16 looks clearer for you. It may be a little early, but what is your thoughts on gross margins?

Uday Kotak: Sampath, I will first give you six months, I will give you five years, and then I will try and answer next 15 months. My 6-month view… and this goes back to November/December, and some of my colleagues in this room will recollect an internal mail where I said that I am pretty bearish with what is happening globally, especially in the first half of 2016 calendar. I think that is playing itself out because for all the benefits we may get on commodity, we are losing out on exports, we are going to have pressure on remittances, and it does not help if the world goes to an extreme position on anything, which is what it seems to be right now on commodities, because that dramatically increases the risk of accidents, some countries defaulting or some companies going out of business and things like that. Therefore, you have got to drive the car pretty carefully in the first quarter first half. But if you stay the course and do not make big mistakes, I think the time comes when the positive of Indian macro and the fundamental sustainability of the Indian economy, because we are on the other side of the equation compared to Brazil or Middle East or Russia, where we start seeing the gains of the fundamental macro. If you have stayed the course, you get your opportunities. I go back to at least two historical points -- One is '97-98 when we were not a bank; we were Kotak Mahindra Finance and we saw the Asian crisis and we saw what happened thereafter. We fortunately turned out to be beneficiary post the crisis probably because we did what we thought was right for us at that point of time. Similarly, if you recollect post the global financial crisis in 2008-09, a lot of our colleagues in the banking sector went pretty aggressively on lending to infrastructure. We were a little more cautious between 2007 and 2009/2010 because we were not really getting our answers on risk adjusted returns and we felt it was like private equity risks for poor lending returns. So we stayed our course and did not rush headlong into it. So we believe by us doing the right thing, staying our course as we are, there will come a time in the next 6-9 months when we will have an opportunity to do significant acceleration, including gaining market share across our different segments. I believe that at some point of time, we will see a bottoming out. I wish I knew the time, but if I was a betting man, somewhere between April and September is what I feel could be a bottoming out period. We just want to make sure we are there alive and kicking, and ready to take on opportunity in whatever form it comes. Therefore, '16-17 at the same time on our merger, we have taken significant costs in this year; you are aware we have taken under-provided pension hit of Rs.300 plus crore in the first quarter; we are taking every quarter significantly higher credit costs than what we took on our own last year. So this is a part of really making sure that all the issues connected with the merger are behind us post this year. We are beginning to see gains in both cost and revenue synergies which will flow full steam into next year. That is something which is making us pretty hopeful into the next year. But this year, we are staying the course of whatever we have guided you.

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

Mayank Bukrediwala: We just had a few questions on the subsidiaries. So starting with on the Asset Management business, the profits were really low in this quarter. So what drove that?

Jaimin Bhatt: I explained that when I talked about the consolidated numbers. This quarter we had taken a hit on account of an operational item and I think bulk of the drop for this quarter is attributed to that particular item, it is a one-time.

Mayank Bukrediwala: Also, on the Prime business, there is a decent amount of pick up that is taking place. Can you give some more color on this and what do you think whether these rates will sustain?

Uday Kotak: Narayan?

Narayan S.A.: The last quarter October-December we did see our disbursements go up; the Car sales on a YTD basis gone up by about 8.5% on a number basis, but on value basis it should be higher than that because we see the B & C segment Car going up and actually the A segment actually not going up that much or in fact there is a negative growth in the A segment. Most of the demand is coming from the urban side of India. Actually, the numbers for October-December were better than what we expected and we have been slowly gaining market share in a segment also. We think Jan-Feb-March will also be similar.

Uday Kotak: Actually, it is quite interesting. We are seeing reasonably positive signals on Cars as well as Trucks.

Mayank Bukrediwala: On the Securities business, again, there was a much lower PAT this quarter. Could you give the reason for that probably I missed it?

Jaimin Bhatt: Again, something which I explained. A couple of things – one is the market average daily volumes this quarter versus the previous quarter have been significantly lower and which effectively has resulted in our volumes also being lower. Our market share for the quarter is marginally lower than the previous quarter. The first lacuna we are talking about is the average daily numbers. This quarter also had four trading days which were lower than the previous quarter which again results in a negative number, where the expenses are there, the income does not come at all.

Moderator: Thank you. The next question is from the line of Amey Sathe from Tata Mutual Fund. Please go ahead.

Amey Sathe: If you can just help us understand any takeaways from RBI meeting with respect to the asset quality if possible?

Uday Kotak: What I understood from the RBI meeting is that they are going to put out a press release; that is the sense I got. I can say it was pretty well attended by bankers and they also had some select non-banking finance companies and ARCs also at the meeting. It was a very constructive discussion. I think the governor advises us to look forward rather than look too much at the back.

Moderator: Thank you. I would now like to hand the floor over to Mr. Uday Kotak for closing comments. Over to you, sir.

Uday Kotak: Thank you, colleagues. I just wanted to say once again that I firmly believe that this is a period where a lot of the volatility will be determined by global events. I do believe that the Indian growth story on the nominal basis has clearly slowed down in second half of 2015. But, we are getting fundamentally into a much better macro position. We are clearly seeing pockets where things are looking better, whether it is Car Finance or Commercial Vehicles. My colleagues and I are very focused on making sure that on wholesale credit we are either moving up the curve or making sure that we are getting our structuring proper before we plunge into open ended structures. Liability franchise continuing to kick in. We basically are clearly focused on creating capacity both on capital and liabilities to a point where we believe that as the economy shows a pickup we are geared to be able to take advantage and we really want to see growth in our share. Unlike the cycles of '97-98 & 2008-09, we are certainly alert but that more open to be growing ourselves faster rather than excessively hunkering down though being alert all the time. Thank you very much.

Moderator: Thank you very much members of the management. Ladies and Gentlemen, on behalf of Kotak Mahindra Bank that concludes this conference. Thank you for joining us and you may now disconnect your lines.