



## “Kotak Mahindra Bank Q3 FY20 Earnings Conference Call”

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**Moderator:** Ladies and gentlemen, good day and welcome to the Kotak Mahindra Bank Q3 FY20 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, 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 and welcome to our quarterly concall in connection with the December 2019 results.

On the bigger picture, I do believe that the Darwinian theory of survival of the fittest is currently playing out across sectors and I do believe its impacting the financial sector which is going through its own turbulences. Therefore, at this point of time, in terms of strategy, two important points relevant for any player in the risk based financial sector are: 1) a need for sharper risk underwriting in choosing not just the sector, but also specific borrowers because there is significant mortality within the sector in terms of who survives and who doesn't. So that is one important issue which makes sharper risk underwriting absolutely necessary to undertake. 2) at a time like this, we believe that the compass is more important than the speedometer.

In this context as we look at our overall economic situation, the GDP is growing at or below 5% and we believe that this will gradually stabilize and would move to a real run rate of around 6% in the next 12 to 24 months timeframe. The nominal growth of the economy which is relevant for our business which is currently in the range of 6% to 7%, we believe will move and stabilize to a 10% to 11% nominal GDP growth. As you may recollect, I have said from time-to-time, we believe we have the ability to grow at 1.5x to 2x nominal GDP depending on the situation of the economy. We also feel that we are going to see a little bit of inflation coming back and if repo rates are not increased, we will see a reduction in real interest rates in the economy which will aid growth.

Having said that, at this point of time we do see a few financial entities going through stress and challenges but believe it is controllable through right policy action. Therefore at Kotak, our focus for this quarter has been to keep the ship steady and remain focused while being consistent with our sustainable strategy. In Q3FY20 we had a one-time hit on our employee cost of Rs. 200 crore which was linked to the defined benefit scheme of the IBA employees which have become a part of Kotak post-merger with ING Vysya Bank. There are currently about 2,000 employees and this Rs. 200 crore hit is primarily on account of revision in the annuity tables for buying annuities which has been changed by Life Insurance Corporation effective October 1, 2019. This change in annuities is applicable to all annuities, fresh annuities which are being bought at LIC and would be obviously similar rates with other players, as a result of which any defined pension or annuity commitments which a bank or any party has, the amount of money which you have put in for the same level of annuity goes up and this is one of the main reasons why we recognize the cost of this change which was made effective October 1. We have taken note of that and provided for the same fully in the quarter ended December 2019.

Our credit cost for 9 months FY20 is 67 basis points which is consistent with our view on credit cost for the year of being in the 60s and maintain this view of credit cost for the full year to be in this range. Our core strategy which is what we have discussed with you over time of building low cost and stable liability, to focus on risk adjusted returns, building franchise and knowledge businesses, digital drive and customer and value creation continues. We are happy to also state that our asset management, life insurance, investment banking and securities businesses continue building a strong franchise and sustainable growth and we have in fact grown quite well in this quarter. If you look at our numbers, the Bank's standalone PAT is up 24% YoY, consolidated PAT is up 27% YoY and Non-bank Company's profit after tax growth is 36% YoY.

In terms of how we see growth from here, we would say that it would be less than the mid-teens but in double digits since we have seen some moderation in growth compared to the September quarter. So where that ends, whether it is 12%-13%, difficult for us to stay at this stage. But this is how we feel about the situation at this point of time and as we go further into the year, I think this is a year where we do believe that the basic theory of moving towards the system which is cleansing, consolidating and getting fitter is the game which will play out and we will play the game accordingly.

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

**Jaimin Bhatt:**

Thanks, Uday. As we have given in our presentation, we closed the Bank's standalone with a post-tax profit of Rs. 1,596 crore which is 23.6% higher than the same period last year. We have seen the NII growth in the Bank at 17% YoY which is on the back of advances growth of 10.4% YoY which results in the NIM going up to 4.69% for this quarter. The other income has seen a growth of 37% on a YoY basis while fees have come in at a growth of 8% YoY during the period. We have seen general banking fees continuing to grow up, slight drop in the distribution fees mainly coming from mutual fund being lower and we had some spike in DCM last year.

The employee cost has seen a sharp rise in this quarter, as Uday touched upon, this is a non-recurring charge coming from, the LIC revision of the pension tables or the annuity tables and changes in DA rates. And this not only impacts the current 2,000 employees, but we have another 3,000 plus retired employees who will also get benefit and to that extent we have taken the charge on all of that in this quarter. OPEX this quarter has seen rise coming from on a year-on-year basis, what we spent on reviving the 811, since last year we had a slowdown due to the Supreme Court decision. We have seen a rise in some of the business related expenses relating to cards.

Our provision for the year looks different because last year in this quarter we had actually seen a reversal of provisions on the treasury side which kind of had an overall net number which was negative on the provision side. To that extent, we have seen a rise in the NPA provisions this quarter. The credit cost as mentioned 67 bps for the 9 months period. The GNPA at the end of the period now at 2.46% and the NNPA at 0.89%. SMA-2 which was Rs. 431 crore 3 months ago has now gone down to Rs. 274 crore which is about 0.13% of net advances. So while our

profit before tax is at Rs. 1,944 crore, we closed the period with Rs. 1,596 crore of post-tax profit, to some extent also helped by some favorable tax orders we got during this period. Our CASA story continues to be good as we have mentioned the CASA percentage at 53.7%. If we take the average 9-month numbers for CA, we have seen a growth of 19% on a year-on-year basis and savings a 20% growth on a year-on-year basis.

In addition to CASA, we also have seen a rise in the TD sweep numbers that is now about 7.4% of the overall deposit base. The CASA plus the deposits which are less than Rs. 5 crores now forms as much as 87% of our total deposit base. Cost of SA has come down and is now 5.27%. This period we end with 1,539 branches at the Bank level.

On advances, as we spoke, the total growth of advances year-on-year is at 10.4%. We have seen growth coming in the agri space, the home loan space and the small business space. The corporate book as well as the CV/CE has seen a lower growth for the year as well as for the quarter.

If I look at the subsidiaries right now, we have taken the overall consolidated profit post tax at Rs. 2,349 crore which is 27.4% rise on a year-on-year basis. Our capital and reserves are at Rs. 65,000 crore plus and we closed the period with a book value of Rs 337.6. Kotak Prime showed a profit of Rs. 187 crore for the quarter and Kotak Investments at Rs. 64 crore. Both of them have seen a slight drop in their book size, though the margins have improved and capital adequacy at both those entities continues to be healthy between 23% and 25%. The capital market subsidiaries, KMCC showed a profit of Rs. 40 crore this quarter and has been in the middle of deals, closed the QIP issuances of Bajaj Finance and PVR, was involved with the IPO of Ujjivan and advisory side we had deals from ArcelorMittal and Fabindia. Kotak Securities maintaining a 9.2% market share on the cash segment has seen the profit post tax for this quarter at Rs. 128 crore versus Rs. 99 crore for the same period last year.

For the other two entities, life and mutual fund, I would request Gaurang to talk about the Life Insurance segment.

**Gaurang Shah:**

Thank you, Jaimin. Life insurance, we had a strong performance this quarter. Our gross written premium has grown by 44% YoY and our individual premium has grown by 22% YoY on a very strong renewal premium. Our Group business continues to be on the back of more risk premiums, has gone up by 89% YoY. Our AUM has gone up to Rs. 32,670 crore which grew at 29% YoY. Our 13<sup>th</sup> month persistency to 61-month persistency which are on 5 data point it is managed. Across the industry, we are either number one or two on each of these 5 data points.

Our profitability has been good. We grew from Rs. 125 crore PAT in Q3FY19 to Rs. 166 crore PAT this quarter. Our solvency ratio continues to be above 3. Our mix of product between ULIP and traditional continues to be favorable in terms of our margin. If I take you to the AUM, the AUM growth across different verticals has gone up by 29% from Rs. 203 lakh crore to Rs. 263 lakh crore.

On the other vertical, offshore fund, we are more or less steady but our overall percentage has gone down because the domestic AUM on both debt and equity has been strong. Our growth in Life Insurance has been from Rs. 25,000 crore to Rs. 32,000 crore. Our alternate asset which has been a strong story, has grown from Rs. 5,800 crore to Rs. 14,900 crore and PMS stays steady. For domestic mutual fund, I hand it over to Nilesh.

**Nilesh Shah:** Thanks, Gaurang. On the domestic mutual fund side, our total assets under management has grown by 27% year-on-year from Rs. 1,39,562 crore to Rs. 1,77,114 crore. Within that, our equity assets have grown at 31% from Rs. 55,945 crore to Rs. 76,366 crore. This has put us one rank above in terms of ranking from 7<sup>th</sup> largest mutual fund last year to 6<sup>th</sup> largest mutual fund this year. This growth has been reflected into our profitability which has grown 20% year-on-year to reach Rs. 91 crore.

**Uday Kotak:** We would be open to taking questions now please.

**Moderator:** Sure. Thank you very much. We will now begin with the question and answer session. The first question is from the line of Nishant Shah from Macquarie. Please go ahead.

**Nishant Shah:** Sir, could you just give us an update on any traction in cross-sells from the 811 account. I think sometime in the past you had mentioned that 70% of the profile of these 811 account customers has been similar to your customers. So is it like finally an appropriate time to start the disclosing probably, what kind of cross-sells we have achieved with these 811 accounts?

**Uday Kotak:** I will hand it over to Shanti, but, as far as the distinction between 811 or other customers goes, they are all customers of the Bank and we would like to consider it as one single broad Bank level strategy. But I will ask Shanti to give some flavor and color on how the 811 cross-sell is going?

**Shanti Ekambaram:** Thanks, Uday. This quarter actually has been pretty strong on the cross-sell on 811. This is across banking products whether it is term deposits, recurring deposits, credit cards, insurance and life. So the trend actually is going pretty well and pretty strong this quarter across the various banking products very similar to what we do in regular channel.

**Nishant Shah:** Okay and perhaps could you quantify like what kind of average balances are there in 811 accounts versus others, versus the ones acquired earlier?

**Shanti Ekambaram:** So as Uday had just outlined that this is a broader strategy on average balances across the Bank and not just for any segment and you know that the same strategy we follow across.

**Moderator:** Thank you. The next question is from the line of Monica Agarwal from Bernstein. Please go ahead.

**Monica Agarwal:** My question is on the gross NPA. I understand that the increase in the gross NPA is slightly on account of the agricultural loan book and the CV/CE segment. I was just looking forward if you

could share some color on how gross NPA would be like excluding these segments like some number, what was the number this quarter versus what would be the number in the previous quarter?

**Uday Kotak:** First of all, if you look at our gross NPA, when your denominator on the advances grows slower, the percentage goes up faster. So if you look at the absolute increase in gross NPA, it is about Rs. 400 crore, from Rs. 5,000 crore to Rs. 5,400 crore. So that is just below Rs. 400 crore is the total increase in gross NPA. Let me tell you that we have not seen any significant increase in agricultural advances NPA. The reason why this Rs. 400 crore increase has happened is, you go back to our disclosure on SMA-2 which we did in the September quarter, which was Rs. 430 crore, which is now down to Rs. 274 crore as of 31<sup>st</sup> December. So SMA-2 as you are aware is for accounts which are more than 60 days overdue and less than 90 days and essentially more than Rs. 5 crore. So you have a Rs. 160 crore reduction in SMA-2 between September quarter and December quarter and the increase in NPAs on account of one or two chunky corporate accounts and that is one of the important reasons in increase in GNPA and we have seen some increase on a relative basis in our unsecured loan book including credit cards. So we are clearly seeing NPL inching up and I think wholesale is much more chunky, therefore if I keep that aside, in the unsecured book particularly personal loans and credit cards which are seeing a clear increase in the NPAs.

**Dipak Gupta:** So the two segments which you mentioned, actually the NPAs have really come down rather than gone up.

**Monica Agarwal:** Actually for Kotak Bank the NPAs in agriculture and CV/CE segment is going down.

**Uday Kotak:** We are not saying that, we are saying it has not gone up.

**Monica Agarwal:** Okay, alright. So just another thing why was there a contraction in the CV/CE segment on the advances front? I mean we understand that the entire economy is going through the downturn and there was a slowdown, so is it because of that, that we are seeing the slowdown in the CV/CE segment?

**D. Kannan:** Apart from that, I think one of the reasons why our disbursements have gone down is also because of the sales of CVs and across the segment both HCVs and LCV have gone down in the quarter. In fact, YoY, HCVs are down more than 40% in terms of sales. So lower sales numbers have led to lower disbursements.

**Monica Agarwal:** It is just the lower sales leading to lower disbursement and not like a bad book or a bad asset quality what letting us take some conservative step on that book, right?

**Uday Kotak:** That is correct.

- Monica Agarwal:** Just last one I have on the other income front; I am not sure if I missed that part. What exactly has led to the higher other income like apart from the fee income, there is a chunky other income we have. What exactly that has led to that decrease this quarter?
- Jaimin Bhatt:** I am presuming you are comparing year-on-year. So if you look at year-on-year, last year we had an item which was negative number in our provisions,
- Monica Agarwal:** I am asking on the other income front?
- Jaimin Bhatt:** I am coming to that. The right way of putting that instead of reducing from the provisions would have been to add to the other income. This has been done because we have been told by the RBI. So if I adjust for that, the other income on that count will actually go up for last year by about Rs. 200 crore.
- Moderator:** Thank you. The next question is from the line of Rahul Jain from Goldman Sachs. Please go ahead.
- Rahul Jain:** Again on this question on slippages. Is it possible to get the break down of gross slippages between retail and non-retail for the standalone bank in this quarter?
- Jaimin Bhatt:** As Uday mentioned, it has been across the board we have had some coming from the corporate book, maybe a couple of accounts there, a few corporate accounts which went off. Then, some of the ones coming in from the SME segment, CV segments etc.. So it has been across the board. The Rs. 1,000 crore which we talked about has come in partly from the corporate book, which would have been the largest amongst all, but otherwise the other contributors there would have been the CV/CE and the small business, though it is not higher than the same numbers for the previous quarter.
- Rahul Jain:** So just to clarify Jaimin, so on the previous question, I guess you mentioned that unsecured book has contributed to the stress if I heard it correctly and I guess now what you are saying is the largest amount of the slippages coming from the corporate accounts followed by CV/CE that understanding is correct?
- Jaimin Bhatt:** There is also the fact that if you look at the small business unsecured as well as the credit cards, those have also seen a rise from a period to period basis which is September to December.
- Rahul Jain:** And just one in terms of guidance because I guess over the last few calls, you did about your potential increase in slippages in the unsecured portfolio, but that was more in the latter part of this calendar year, but I used to sort of seeing this getting advanced and therefore you are experiencing this slippage buildup in this portfolio now and would this continue through this year or how do you see that trajectory play out?
- Uday Kotak:** I will ask Shanti who heads the Consumer Finance businesses to give her perspective.



- Shanti Ekambaram:** We mentioned in the last quarter's call as well that we are beginning to see an uptick in unsecured in credit cards and personal loans. So we continue to see that in certain parts of this vintage book. I think that these are normal trends, nothing that would alarm us.
- Rahul Jain:** Sorry for belaboring on this one, but compared to the overall industry's trends within these portfolios, how would our trends be, is it better than the overall industry in line?
- Shanti Ekambaram:** We are in line with the industry. Whatever data that gets put out by all the bureaus etc., we are seeing; we are in line with the industry.
- Rahul Jain:** Just another question on the fee income growth. Over the last 2 quarters, we have seen moderation in fee income growth, that is broadly in line with our loan growth too, but I guess as the liability franchise has shaped up remarkably well over the last few quarters, at some stage I guess you would expect cross-sell income etc. to pick up, but 9%-10% kind of a fee income growth seems bit off. When do you see cross-sell driven income be it on the payment side or on the liability franchise or third party distribution etc. kick in?
- Shanti Ekambaram:** I think one of the things we saw is that the investment distribution income this year is down keeping with the overall sentiment as compared to let us say the previous year. But that is what it is, otherwise if you see our transaction revenues etc., the trend continues.
- Rahul Jain:** So Third Part Distribution has been a bit of a drag, that is the reason why the overall growth is...
- Uday Kotak:** And you also know that in the mutual fund distribution business, there is a very significant change in the industry. Commissions which were paid upfront are now becoming annuity. So that change actually is extremely important and that change is actually playing itself out.
- Rahul Jain:** Last question on the lending subsidiaries, Kotak Prime and KMIL. Over the last 2-3 quarters, the book has been contracting. When do you see this stabilize or you think as a strategy maybe if you have taken a call that will sort of bring more business to the Bank?
- Uday Kotak:** On Kotak Prime, the answer is pretty simple. Cars are selling less. So when absolute passenger cars are selling less, you are going to have some impact and to a certain extent, we have changed the mix also. So there is a change in the mix which is also helping us in profitability, may not be in absolute disbursements, but our profitability metrics looks good. Absolute cars selling less is a reality.
- Rahul Jain:** So nothing unusual out there, it is broadly in line with what the industry or how the industry is playing out.
- Uday Kotak:** Yes.
- Moderator:** Thank you. The next question is from the line of Mohit Surana from CLSA. Please go ahead.

- Mohit Surana:** On the slippage, one on corporate slippages that you mentioned, is it possible to quantify what would be one-off so that we can look at more of what is the core slippage in this quarter?
- Uday Kotak:** I can tell you it is a 3-figure number, but it is not a very large 3-figure number.
- Mohit Surana:** And would this be the reason why provisions have also gone up and have you taken any accelerated provisions on these?
- Uday Kotak:** We will take provision on the basis of what we think is recoverable.
- Mohit Surana:** Okay, but normal provision, no acceleration on these.
- Uday Kotak:** Acceleration means if we believe for a particular loan, we need to provide more, we will take it. Our approach is very clear, whatever is the recoverability of a loan, we make the provisions accordingly. If we believe we can recover less, we will provide more irrespective of what regulatory requirements maybe.
- Mohit Surana:** Okay, got it. And lastly on telecom loans, is there any exposure to the stress players that is being talked about?
- Uday Kotak:** I can tell you on a percentage basis, we must be amongst the lower end of challenges which I think the telecom sector is facing. It is back to the point which I had mentioned at the beginning of my talk. One of the most important aspects in risk underwriting today is not just sector exposure but also choosing within the sector. So of course we would and there is one strategy which we have followed over a long period of time which I have shared with you in my earlier calls is, we are very cautious on concentration and therefore we do feel that what is happening in the telecom sector is something which is unprecedented but we don't see that as anywhere near the kind of significant impact which the financial sector will face on a relative basis by far.
- Moderator:** Thank you. The next question is from the line of Saurabh from JP Morgan. Please go ahead.
- Saurabh:** Just one question on your corporate banking business, the low growth here is essentially just a function of your conservatism or just there is no demand which you are seeing or because your margins are at 4.7% now, so I was thinking probably could do a lot more here.
- Uday Kotak:** I will ask my colleague Mr. Manian who is in charge of that business to tell us what is happening.
- KVS Manian:** So I would say that if I divide the corporate book into two parts that is the SME side and the pure corporate side, the two are different. On the corporate side as Uday mentioned that the number of eligible "corporates" that you can lend to is also shrinking sector by sector. So we are cautious about that and over the last two years, there hasn't been too much demand for long-term loans. Now we see actually underutilization of working capital limits as well and also the better corporates are going to the CP markets and the bond market and are able to raise money much cheaper. So obviously for the better corporates even working capital utilization is lower.

So that also puts pressure on the existing book to grow it. On the SME side, we are seeing some signs of the recovery back at our end, but of course there is also utilization level which traditionally used to be 60%-65% are closer to 50%-55% kind of utilization levels, puts again pressure on the existing book. So we do continue to be focused on getting new clients, which is happening too. We are adding new clients, we are getting share of the right products in corporates, all that is happening. So we think that with some turnaround, some demand increase should happen, having said that we are trying our best to get into a double digit kind of growth as the year progresses.

**Uday Kotak:** In other words let me tell you, for this quarter on a Y-o-Y basis while you have seen the overall growth at 10.5%, wholesale corporate banking growth is in single digits, it is 3% for the quarter YoY. So on the other hand, if you look at our retail loan growth, it is about 18%.

**Saurabh:** Sir, what is the breakup between large corporates and mid corporates in this corporate banking business?

**KVS Manian:** Right now, one bucket. And these definitions vary from bank to bank.

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

**Ashish Sharma:** Sir, the question on the growth rate, advances growth side you have mentioned in your guidance, so is this the guidance for FY20 or do we see similar sort of guidance for...

**Uday Kotak:** FY20 full year. We have said we are reducing the guidance from mid-teens to say in double digits but below mid-teens.

**Ashish Sharma:** Okay. Do we see some sort of an improvement from an industry perspective and for Kotak in FY21?

**Uday Kotak:** I think it goes back to the economy view. We believe there is a gradual pickup in the economy and as I said that it is linked to nominal GDP. If you look at the October to December quarter, nominal GDP was 6% to 7% which is the reality. We see nominal GDP stabilizing back to 10% to 11% partly because of inflation and partly because of better real growth but gradual. Gradual growth and real growth, inflation is helping in bringing nominal GDP growth into double digits and should that happen, we would see some amount of deflation and therefore a better view as we go forward.

**Ashish Sharma:** Okay. Second question would be on the net interest margin. Do we see any further headroom for improvement or how do we see margins play out for the bank both FY20 and maybe in FY21?

**Uday Kotak:** I think Jaimin always likes to be cautious on guidance about net interest margin. Jaimin, your last year guidance was 4.25-4.3%? Therefore we don't like to give an excessive estimate but our

view is clear, if we get the loan lending growth for the risks we take and we think at that level it protects and grows our ultimate sustainable ROE, we are very happy to grow. We are not obsessed with high margins, but we are certainly obsessed with risks for the returns we get.

- Moderator:** Thank you. The next question is from the line of Adarsh P from Nomura. Please go ahead.
- Adarsh P:** A question on the SA improvement that we have seen for the last 2-3 years, can you just split it into say how much of it is 811 which would be a small part and rest of it what was the account growth and what is the balances growth, some qualitative comments around that? Thanks.
- Uday Kotak:** I will have Shanti's colleague Virat, who runs that product on that retail and branch banking directly to give you his assessment of the SA developments.
- Virat Diwanji:** The SA development, means in terms of the balance growth, and if I split between the 811 and the others. 811 has been steady, means in terms of it we have got the growth from the new customers that we acquire. The biometric return has helped us to ramp up our 811 numbers as well and hence we get that growth in SA from 811 as well. But as far as the balance is concerned, it is an average which we have been maintaining right from the beginning. As far as the 811 is concerned, as far as the normal SA customers is concerned, yes, we do see some kind of an increase in the uptake, but still with the kind of growth that we would look at perhaps it is not visible there. But customers do keep balances in the account and we have seen some bit of rise in the balance sheet as well in the recent past.
- Uday Kotak:** Bottom line is we put Virat at a much higher target than what the percentage growth you are seeing. So Virat has to work towards the higher targets which are set for him.
- Adarsh P:** And Uday, one question is, given the kind of granularity now, you have kind of caught on your liabilities 87% is almost retail. Is it time that your SA cost is moving down but you are going to take more decisive steps in terms of getting down your SA rate to where some of the larger players are?
- Uday Kotak:** No, we are fully aware of the risks, the opportunity and strategy and as I have said, we have a very well, deep thought through strategy on how we want to play this and let me assure you we do not think about ourselves as having pressure of any short term tactical objectives, we like to ensure that our performance in the short run also continues to be sustainable but we will take much more strategic view about some of these and not be driven by what gives me the next quarter's profit. And it is not about trying to inflict pain on others or taking a significant cost for us, it is pure hard surgical driven strategy.
- Moderator:** Thank you. The next question is from the line of Manoj Bahety from Carnelian Capital. Please go ahead.

**Manoj Bahety:** Sir, I have couple of questions. First is like given the state of economy right now, are you seeing some early signs of trouble in the retail book and also given the fact like most of the banks and NBFCs, everybody is running as per the retail portfolio. So are you seeing some kind of risk adjusted mix pricing at the time of underwriting that book?

**Uday Kotak:** Again, retail is a large amorphous world. Within that, there is secured, unsecured. There is MFI, there is unsecured consumer loans. On microfinance, we are all aware early danger signals have come out. There are at least a couple of states where the political class has advised borrowers not to repay microfinance companies and it is playing out in at least 2 states as we talk and we have to be careful and cautious to ensure that this does not become more viral and I think it is for all of us to be responsible players and take the help of policy makers to ensure that we do not see a viral situation in the microfinance space. Unsecured, as we all know, the profits of an unsecured loan on an accounting basis or quarterly basis come first. The real profits of an unsecured loan is only in the last 2 or 3 installments and then if there is significant multiple borrowing by the same borrower from other lenders, it affects all lenders including the first lender if there is any installment outstanding. So we do believe that we are not panicking, but certainly more alert than before and which we have also highlighted that in our GNPA number increase, there is an increase in provisioning which we have had in our unsecured credit card and personal and business loan book.

**Manoj Bahety:** But sir are you seeing some early signs of stress on that side?

**Uday Kotak:** We have given you the facts of our book. So now you are an analyst. It is for you to figure out what it means. And having said that, again I want to repeat we are not seeing panic, but we are seeing higher levels of delinquencies than before in our book and it is there in the bureau. I think the bureau data is also showing the same thing. So it is not rocket science what we are saying.

**Manoj Bahety:** I have one more question. In fact it is just a follow-up on when you said that the corporates which you are targeting and they are approaching customers directly through bonds, through CPs. So just wanted to understand like the way the bond market is growing or the CP market is growing or direct borrowing is growing, so over a long-term are you seeing some kind of disintermediation risk especially for a conservative bank like you where your target set of the customers approaching customers directly through bonds or CPs and the other customers like who are not your target set of customers, they will go through bank's balance sheet. So how do you see this scenario evolving?

**Uday Kotak:** We see ourselves as a financial services player. So there is a part of our business which is a storage business, which is the lending business. We are also very significant players in the disintermediation market whether it is equity capital markets or debt markets or asset management business or life insurance business. So we as a consolidated Group have an interest not only in the lending business which is important, but also on a consolidated basis, in disintermediation because that helps some of our other businesses. So in many ways, the holistic approach to financial services is what we see. In that sense, yes, banking is a very large part of

our total, but we are a broader financial services player and we will be very active participants even as disintermediation happens and benefit from it.

**Moderator:** Thank you. The next question is from the line of Nitin Agarwal from Motilal Oswal. Please go ahead.

**Nitin Agarwal:** I have a few questions sir. Now with successive decline in our funding cost and CASA mix growing well, do you think that this will open up new lending opportunities for the Bank which earlier were not available owing to profitability considerations and if yes, then how do you think that loan mix and the margin will change during next 1 to 2 years?

**Uday Kotak:** I think first of all I agree with you. New opportunities are opening up as our cost of funds is improving and therefore even for lower risk cases where otherwise we would have at tougher time competing, we are finding ourselves much more competitive. One of the spaces where we have seen this is for example in the home loan business where we are seeing continuous good growth and we are finding actually risk adjusted returns extremely positive. We also seeing an ability to be play much more actively in the bond market and the CP market out of our wholesale treasury ability because of sheer lower cost of money and the significant advantages of some of those assets for liquidity coverage ratio. We see ourselves clearly to play again not only at higher risk, higher return but at lower risk but improved spread through lower cost of funds. So clearly that is the space which we do see, but we are also very clear, we don't want to bang our head against the wall. What do I mean by that? If the truck industry, heavy commercial vehicle industry is dropping 40%, yes, we may see an opportunity to increase our share a bit, but we don't want to sacrifice and basically go out there and say listen you could lend irrespective of whether the volume has gone down or no, I mean we would like to play the game keeping in mind that there is a significant headwind in many segments of the economy and we just don't want to show loan growth for the sake of loan growth because that is what quarterly numbers make us look better. That is not the objective. We will do what we think is right for our business strategy.

**Nitin Agarwal:** Right. Second question sir, you have guided for the double digit loan growth around low teens for the year which implies around 7% sequential growth for 4Q which is higher than the trend we have seen in the past few quarters. So what are the segments you think will drive this growth?

**Uday Kotak:** We have said that, I mean to make it very simple, what we have said, if I have to translate into simpler language, we are saying 10 plus, 15 minus, now where in that range we come, we will share with you. But obviously some of the points which we discussed on this in response to your questions is part of our strategy.

**Nitin Agarwal:** Right. And sir lastly one more question if I can squeeze in, you mentioned that the bank has seen higher slippages in the unsecured products while CV/CE segment remains on track. Now this is different from what we hear from other banks. So can you give some color on the proportion of

say internal sourcing for unsecured products, typical customer profile regions etc. wherein we are seeing this sort of stress building up.

**Uday Kotak:** So, therefore you have two questions. Your question number one is on the Bank. Other banks have stress in other areas, I cannot comment on them and how they source that versus how we source that is for them to be able to tell you. And as far as the sourcing for the consumer side is concerned, I will ask Shanti to share how much of internal cross sell business and how the strategy is there.

**Shanti Ekambaram:** Sir, on the credit card business, close to 85% to 90% of the sourcing is through our own customers and internal channels. I want to repeat that the trend that we are seeing on uptick is in line with the industry and not outside of the line of the industry, in terms of what we are seeing in the unsecured portfolio. In terms of personal loans, close to more than 50% share is coming through our internal channel and the balance we do look at external channels, partners etc., aggregators whom we work with, again very similar to the industry sourcing and industry trends. So I just mean to emphasize that part of it for your reference.

**Moderator:** Thank you. The next question is from the line of Manish Karwa from Axis Capital. Please go ahead.

**Manish Karwa:** So Uday, just on the strategy on growth, some of the products historically like say housing and corporate did not fall into your ROE profile because they were low yielding products. Given the tax rate cuts which have happened, does it make sense now to be a bit more aggressive in some of these, aggressive as in bit more pushy on some of these products because it may have now start falling into your RoE profile?

**Uday Kotak:** Hi Manish, welcome to you in the new avatar. I just wanted to share with you that if you look at our retail growth, it is 18% Y-o-Y and within that, both home loans and LAP have grown very well and the reason for that is the fact that with the cost of fund reduction, we are getting the risk adjusted returns which we want and of course our ROE requirements have come down or have improved because of the tax rate cut and we actually are finding that at this point of time the level of delinquency in both home loan and LAP is very much under control compared to the unsecured segments. So your point is valid and is appropriate for us and we are focused on that in terms of our strategy.

**Manish Karwa:** Someone else also asked this question. So on the deposit front, look the system is extremely liquid, overall growth is weak, you have any which way softened your rates a bit but still growth is very strong for you on deposits. So do you still want to keep maintaining that high growth, I understand your long term thought process on this. But even if you were to reduce I guess the growth number may still be very strong for you and even still continue to gain decent market share there. Then why give such a great value proposition to our customers on the liability side?

- Uday Kotak:** Right, Manish we hear you, we are fully aware of it. We are aware of the fact that compared to any other financial institution, our current operating and profit numbers include a differential on savings rate plus our 811 acquisition cost which together even now is Rs.2,000 crore a year of incremental cost compared to our competitors, therefore our numbers are after such a high level of cost which we are absorbing in our current cost structures, we are fully aware of it and we are also very conscious about value. We also understand the tactical advantages and we are also seeing how the external market both on inflation and interest rates is playing out. So we will take a very careful judgment call not on the basis of getting a benefit of Rs. 200 crore in the next quarter but more sustainably how does it strategically position us when we look at 12-18-24 months from now vis-à-vis the market place and how do we get sustainable competitive advantage and therefore if I have to use a cricketing analogy, we like the one day game, but we don't like T20.
- Manish Karwa:** Sure, well said. Lastly just couple of data keeping question. One, the tax rate benefit does it conclude now this quarter or we get more as in there is something more to accrue on the tax front. Should the tax rate normalize from next quarter onwards?
- Jaimin Bhatt:** That is right. Basically we have opted for the new lower tax rates, so going forward it will be at the new tax rate.
- Manish Karwa:** Okay, which is like 25% plus some surcharge.
- Jaimin Bhatt:** Just around 25%. We get some benefits, so it is around 25%. This quarter as I mentioned we had some relief on some favorable orders that is why it is lower.
- Moderator:** Thank you. The next question is from the line of Sachee Trivedi from Columbia Threadneedle. Please go ahead.
- Sachee Trivedi:** I do appreciate and thank you for keeping eye on the compass rather than the speedometer at this point. So congratulations on that. The question I have for you is when I look at your loan growth, it is obviously quite low but I want to understand that if the underlying reason is that you don't see that much demand or do you think that you are not being paid to assume the risk or do you think you don't understand the risk itself in terms of you don't trust collaterals or you don't trust the ratings or you don't trust the counting, how would you qualify that slowdown?
- Uday Kotak:** I think my first honest answer is combination of all. But to be more specific, we do see for the quality of companies, or quality of borrowers whom we want to be able to lend or as I said we like to get a fair return for the risk we take, something which we have consistently said. So it is not something new which we are telling you this quarter. If we get the fair return for the risk we take with reference to any specific law, we are very open to taking it and we will certainly consider it. Is there a worry about auditors, rating agencies? Of course, I mean we just had a situation where in some of the accounts, we have seen audited numbers given in the month of May and the ratings were high investment grid, this I am talking about 2019, I am not talking



about the past. And within a month or two after that it becoming junk. So there is a very serious issue about reliability of audit numbers and rating numbers and therefore that increases our level of diligence in terms of how we look at it. We are also seeing significant issues in accounts which are group accounts, where money moves between group companies, as if the entire group is one single company and we are always cautious about that because how do you analyze that risk versus the balance sheet of a single company where you have taken a risk and again there are many publically known examples of how a fundamentally sound company has blown up because it had routed money to group companies through that sound company. So these are obviously serious concerns on the levels and practices which are pretty widely prevalent in corporate India and I would like to say while situation has improved compared to what it was a year or two ago. There is still a lot of stuff out there which is not as transparent and which therefore makes us careful in terms of how we look at risk of individual company within a larger group.

**Sachee Trivedi:** Thank you. Which leads me to sort of the next logical question which is, these problems are not going to go away and so even if the economy picks up, if the GDP picks up or nominal picks up, how will or what will turn or inflects your loan growth from here because everything that you have just said is probably still going to be....

**Uday Kotak:** I had mentioned in my last call of Indian financial business being a 70:30 business. If the total loan availability, underwriting availability out in the market is 100, we don't believe 30 is touchable. Therefore one of the big issues for us is to identify that and then find the loan growth in the balance 70 and that is exactly what we are doing and we think if the Indian economy starts growing at nominal 10 plus, there is enough opportunity for us out of the 70 which is our target to get for us to be growing what I have said and at least 1.5x nominal GDP. That is how we think about the business opportunity. And we think that is more sustainable kind of an approach and we are not scared about lending, we just want to make sure that in a highly leveraged business when you are out there lending money, you better get your money back. That is the most crucial aspect in one of the most highly leveraged businesses called banking.

**Sachee Trivedi:** Sure. And sir if I might squeeze in just final one. As you see, stress and financial services, your peer banks and institutions are under stress. Do you see this as an opportunistic moment for you to actually acquire any other business either or any other book, I mean if not the whole business, is that something or do you think right now everything is so muddy that it is probably not worth the risk.

**Uday Kotak:** We always have an open mind but we just want to make sure that whatever we do is value accretive and we do not like playing blind.

**Sachee Trivedi:** I am assuming you will do due diligence, right, you will have access. But I mean, I am just thinking given, so for example it has been doubted that let us say YES Bank is under huge amount of stress and that might be something that could make sense for yourself. But I am not sure if, even worth considering given, we don't know what is there in those books.

**Uday Kotak:** I share the hesitation with which you ask the question and all that I can say is that whatever we look at in any of these situations is after being fully convinced that it is value accretive and let me assure you at this point of time we are in no discussions which we need to report on any particular target as we talk.

**Moderator:** Thank you very much. We will take that as the last question. I would now like to hand the conference back to Mr. Uday Kotak for closing comments.

**Uday Kotak:** Thank you very much, friends and really appreciate your spending time on this call. All that I would like to end by saying is we do believe that the nominal GDP growth which for the December quarter was 6-7% will steadily move to a more like a 10-11% nominal GDP over the next 12 to 24 months. We look at ourselves as active participants. We are constantly looking at opportunities for the risks we take which we will continue to do. Our core strategy of low cost and sustainable liability will continue to play and we really like businesses which are franchise, relatively low capital absorbing and which are annuity businesses of long periods of time and those are the businesses which we will continue to grow. And in the backdrop of all these, our belief in digital transforming financial services is deeply embedded in our DNA and we will continue to drive that irrespective of the short term challenges which may come in terms of the current cost whether it is out of 811 or a liability strategy which we have a belief that it is something which will pay for us. At the same time, we are commercial. We will not do something which does not make sense and we will take a balanced view in terms of building this institution for the long term. Thank you very much.

**Moderator:** Thank you. On behalf of Kotak Mahindra Bank that concludes this conference. Thank you for joining us. Ladies and gentlemen, you may now disconnect your lines.