"Karur Vysya Bank Q2 FY2019
Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Karur Vysya Bank's 2Q FY2019 Earnings Conference Call hosted by Spark Capital Advisors India Private Limited. 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. Navin Babu from Spark Capital. Thank you and over to you Sir!

Navin Babu: Thank you Raymond. Good afternoon everyone. On behalf of Spark Capital, I welcome you to the 2Q FY2019 earnings call of Karur Vysya Bank. We have with us today the management team of Karur Vysya Bank represented by the MD & CEO, Mr. Seshadri, President & COO, Mr. Natarajan, General Manager & CFO, Mr. Sivarama Prasad and Company Secretary, Mr. Srinivasa Rao. I now request Mr. Seshadri to take us through the highlights of the quarter gone by after which we will open the floor for questions. Over to you Sir!

P.R. Seshadri: Thank you very much Mr. Babu. Thank you to all those who are on the call, I want to thank Spark Advisors for organizing this as we have been doing for a long while now.

The last quarter Q2 of last year was a very important quarter for us. It is a quarter wherein we implemented most of the changes that we had been envisaging and it was a quarter when most of our processes or many of our processes were amended.

As you are aware we had undertaken a journey by which we were transforming the way we on-boarded clients, we underwrote risk and we service them and we were digitalizing most of our processes and last quarter was the first quarter where a full sweeter products became available in the new digital format.

Over the last quarter we digitalized most of our retail products, we also digitalized the working capital process completely for existing as well as for new customers and we worked on the embedding of the new processes within our branch network.

I am happy to tell you that today majority of our customers come on board with Karur Vysya Bank in a process that is very different from the process that was in vogue barely seven or eight months ago.

Today most retail asset products which is auto loans, home loans, mortgage loans, personal loans, loans for two wheelers these are all underwritten in a fully digital manner. Working capital loans up to 2 Crores renewal of working capital loans, enhancement of working capital loans ad hocs and another such facilities on the working capital side are done fully in a digital manner and in addition we launched a digital acquisition process for our liabilities business, which has also gained reasonable traction.

Over the last quarter these products were introduced to our branches and to our clients our branches have adopted to those new practices that we have set in place reasonably well and retail asset application flows have increased quite considerably as I have mentioned in page #5 of the investor deck our application flows have now risen to about 550 applications a day from 300 in the prior quarter.

Adoption of the retail-banking app has also increased quite considerably. We are on course to complete the full rollout of all our digital products hopefully by the end of this quarter and over the last two quarters we have also made very substantial progress in embedding risk based pricing in to our various products. At the end of the first quarter we put in place risk based pricing for our retail product suite and at the end of the last quarter we put in place risk based pricing for our commercial businesses.

With the introduction of risk based pricing on our retail products in Q2 our yields rose by 11.3% over the yields that we were getting in the prior quarter. Our third party product sales continue to do really well, life insurance premiums grew 50% in Q2, mutual funds revenues grew 424% in Q2 over the prior year all be it on a smaller base, and significant enhancement has been noticed by us on the quality of credit that we are acquiring through the door.

Our collection processes have stabilized over this period and the all portfolio risk related metrics that we measure, measure at arguably their lowest point in on the September 30, 2018 as compared to the last 18 months to thereabouts.

We also reduced risk on our treasury book over the last quarter. You will notice that whilst our revenue the net interest income grew marginally 4% year-on-year, the other income stream had dropped quite considerably. The drop is largely attributable to the reduction of duration on the treasury book where we booked a loss of 20 Crores as against profit of 20 Crores in the prior year.

So as of now at the end of September we feel that we are placed reasonably well. Our portfolios our behaving as we had expected them to behave or had predicted that they would behave. Our risk metrics appear to be in control and overall the adoption of the new technologies that we had put in place has been is working and progressing as we had expected.

We do face challenges as undoubtedly you will note in the presentation, the challenge being one where growth has been slightly lower than what you would expect and you would note that growth on the retail side has been quite robust and that is the first product that we have digitalized and the first product we have focused on and it is now beginning to gather scheme as our branches embraced a retail product sweet that historically they have not been aggressively selling we do expect commercial growth to pick up again over this quarter as the new product sweet gets rolled out fully and our branches embrace them and are able to sell it to our customers on the working capital side.

You will notice that the agricultural growth was a little muted, but that is on account of the fact that the season for warehouse loans and other agriculture related products effectively takes off at this point in time i.e., quarter three and therefore we expect our business volumes on the agri side to grow quite considerably when we go forward.

On the corporate side you will notice that on a year-on-year basis our balance sheet has come off a little bit, but that reacts a results of very conscious reduction of some of the risk assets that we had on our book. We continue to work towards growing our corporate book, but with high quality assets and the aim of our for our organization is to grow all four product streams, but grow retail and commercial a little faster than we do grow corporate and as a consequence continue the reduction of corporate in as a percentage of our total assets.

Corporate is now down to 30% as you will notice and we expect corporate assets to grow in the future, but other assets to grow faster and also I am sure you also noticed that the overall accretion to NPA has been substantially muted in the quarter that ended on the June 30, our total NPA accretion net was about 548 Crores it is now down to a 144 Crores. The difference between the June quarter and this quarter is that commercial has moderated very substantially from 240 Crores to 98 Crores during this quarter and if you recall when the last analyst call happened there were a lot of questions has to the future evolution of the commercial portfolio and whether the 240 Crores was a harbinger of much larger flows and we had told you at that point in time that over the last two years the first quarter NPA was the trend was that the first quarter NPA was equal to the other three quarters put together and we had also run some flow models, which indicated that if you use the prior nine months flows those were the numbers that we were getting.

Given that we have now come in at 98 Crores for the second quarter we now have some confidence to say that perhaps this year will also play out a way the last two years have played out and the NPA accretion on the commercial side will now drop off in the same pattern that had occurred in the prior years.

On the corporate side, I am undoubtedly sure that all of you recall that we had told you that there is a stressed asset book or a watch list of 1200 Crores out of the 1200 Crores we had told you that a 165 Crores or thereabouts was non-funded and that had not yet been provided for and not yet been recognized as NPA. Those assets continue to be on the watch list and they have not yet been provided for because they have not yet been called and considering the nature of those contingents it is not appropriate for us to make a provision at this point in time given that many of them are performance related guarantees, which may not be called ultimately, but in this quarter our net NPA accretion on the corporate side is 31 Crores at about 86 basis points, which is I think one of the lowest in recent times and we are very happy that there is no other significant event that calls us to actually relook the future prognosis for the NPAs on the corporate side.

I am sure many of you will ask me questions on IL&FS we do have an exposure to IL&FS to the group our exposure to IL&FS is in the neighborhood of about 330 Crores of which 20 Crores are in the form of investments so they are part of our investment book on the investment book an 8 Crores provision has already been made. The IL&FS loans as of this moment are being carried at book value we have not reckoned as nonperforming that is our account of the fact that there is very limited visibility as to what will ultimately occur in IL&FS we are watching and waiting for further news and we will take appropriate action in this quarter as more information becomes available.

I am happy to also note that after a long period in time our net NPA number has reduced in this quarter. In the prior quarter it was 4.5% we are now down to 4.41%, not a very substantial reduction, but a reduction nevertheless given the fact that over the last several quarters both are grows and net NPA numbers have been on a upward trend so this is something that we see as an omen, which will hopefully help us move in the right direction going forward.

More importantly since September we have been kind of build the provision coverage ratios so the provision coverage ratio has defined as the net NPA divided by gross provisioned by gross NPA has raisin from 32.4% to 42.89% almost 43% which is a growth of roughly 10.5% or 11% over the last four quarters. So right now the provision coverage that we are carrying is substantially greater than what we were carrying five quarters ago. Portfolio trends have improved and moderated during this quarter. The delinquency statistics and other risk metrics in aggregate that we look at have improved quite considerably and the risk on the investment book has been reduced very dramatically as you will see in the reduction in the duration on the AFS book.

With that let me turn this over to those of you on the call who would like to ask a few more questions. I think the P&L is self-explanatory but I can walk people through based on the questions that they have, so with that over to you and thank you very much for this coming.

Moderator: Thank you very much. We will now begin with the question and answer session. We have the first question from the line of Dhaval Gada from DSP Mutual Fund. Please go ahead.

Dhaval Gada: Sir a few questions. First could you give the gross slippages for corporate, commercial, retail and agri?

P.R. Seshadri: We were planning to put this in to the deck itself. If you do not mind having what it will do is we will try and ensure that we sort of going forward provide these pieces of information so that this question has not asked again. I think the last time also you have asked and we had said we will provide it but inadvertently that has been missed. So going forward we will make it available on a regular basis.

Dhaval Gada: The second question that I had was on IL&FS you give the exposure could you just quantify and clarify how much is to the HOLDCO and how much is to the SPVs i.e. the road assets or the assets so where is the amount sitting basically just trying to understand that part?

P.R. Seshadri: Basically our exposure is to the group in total is about 330 Crores. As I said out of those approximately 20 Crores are the former investments against which we are holding 8 Crores in provisions at the end of this quarter. With respect to the other exposure the exposure is broken up between two entities within the IL&FS group, one of which is the HOLDCO and the other is one of the entities in which addresses road related projects and roughly in equal proposition that is the current exposure that we have.

Dhaval Gada: The third question I had was could you just how do you see the CASA deposit accretion and specifically the SA deposit accretion at the bank though the last few quarters since you have taken over just are you happy and just some colour there?

P.R. Seshadri: The current account savings account balances have been growing. They have been growing. They are now at about 30% both end of period balances as well as the average balances have been growing roughly at the same rate and we are feeling reasonably comfortable with the level of growth. We are now engaging in creating specified products, which will enable us to grow savings account even faster so September of last year our current account savings account balances were about 28% and now we are up to 30. I think there is a limit which our CASA balances will grow for the larger institutions the transaction banking business is a very important contributor of current account balances. We unfortunately while we do have a transaction banking business, which we are try and grow aggressively, it is still a small business and therefore the current account balances that come with that much smaller than what other people have. In addition on the savings account side we are almost totally retail and therefore do not have the predictability that comes with a book, which has a lot of savings salary savings associated with it. So on a priority basis we have started going after salary savings customers so that we can grow the savings balance sheet much more predictably than we have done hitherto. So it has been growing to answer your question it has been growing which is a positive significant. We think there are limits to the growth that we can get here. On the deposit side we have not been aggressively asking for deposits for the simple reason that our balance sheet on the asset side was not growing and consequently we were more focused on ensuring that the cost of money was managed aggressively so that we could get a good outcome on the financial side but as our balance sheet starts growing we should be able to turn that tap on that we are very, very comfortable with. We have also invested a fair bit on the technology side so our new message or acquiring customers a quite different from the old and we are hoping that we should be able to step up customer acquisition rates on the saving side. So long answer to a short question.

Dhaval Gada: Sir just couple of last things. Could you clarify the commercial real estate exposure of 2934 Crores how is it split between LRDs are you worried on any exposure in this portfolio and the second question was on the top 20 clients the exposure have again started rising over the last couple of quarters just if you could explain the reason for the same. Thank you.

P.R. Seshadri: The second question first, I think the top 20 customers increase in exposure is largely on account of the fact that they must have been drawls from some of our existing customers so they must have paid down on a particular date and it has come up again. Our focus is to ensure that we build a granular book, the larger ticket exposures that we use to take in the past, we are no longer were taking. So we are limiting our exposures by and large we are ensuring that we keep within 2% of our capital that is the informal norm that we are adopting and so on, on going forward basis we as the older customers sort of they pay us back or pay us down this number should start coming off. With respect to commercial real estate most of our commercial real estate exposure is a mixture of various types so it is a little while we do have some longer duration LRDs we do have other variance as well on the LRD front our total exposures perhaps about 20% and we have at this point in time got no reason to believe that anyone of those assets is compromised in any fashion. We do not see this as an area of stress at this point in time and we think that the areas were stress on the CRD portfolio is quite contained.

Dhaval Gada: Thank you and all the best.

Moderator: Thank you. The next question is from the line of Rohan Mandora from Equirus Securities. Please go ahead.

Rohan Mandora: Sir if we look at the loan book like you have touched up on the loan book in the initial comments, but historically we have been guiding that we will grow at somewhere close to system and the divergence in terms of our growth and system firm growth has been increasing. So just wanted to get a sense like in the second half do we expect a 13%, 14% kind of a growth and what way it is, where will it actually come from and going into FY2020, do we expect the loan growth to be higher than systemic loan growth that was one? Second did we have any exposure to Kerala; any exposures are impacted by Kerala floods and thirdly like if you could touch up on the core fee income like that thing has come down even year-on-year as well as sequentially. So what is our view there like how will it likely to share within the second half of the year?

P.R. Seshadri: Let me answer the last question first the fee income is on page #13 this is for the quarter. So our fee income for the quarter was 175 Crores as oppose to 230 Crores prior year same quarter, but if you see the one line below, which is the fee income, which is the core fee income was 176 Crores against 162 Crores so it did grow year-on-year there may have been an aberration with respect to the prior quarter, but it has grown and there are some sequencing issues in the quarter one we get all our locker rents etc., which are not repeated in quarter two for whatever reason, but so the fee income is growing the core fee income on a like-for-like basis against by a quarter it is growing, it is not growing as fast as we would like, essentially on account of the fact that the growth is not as high as we would like and I will answer your growth question subsequently. With respect to point two investments trading profits prior year was 20 Crores this year is negative 21 Crores. As I mentioned this is on account of the fact that the eliminated duration in our book or rather not eliminated we reduced duration I should correct myself consciously this was done when we have got a brief window of opportunity when the rates dropped during the last quarter to about 770 we were unsure as to what would happen in the market place we decided to reduce duration on the available for sale book and booked a loss as a consequence. The consequence of this action is that our revenues on the fee side our total noninterest income dropped, but the flip side is that the provisions that we needed to make for diminution in value on our AFS securities reduced quite considerably so when you look at our published financials it will say that we were to amortize something like 70 Crores and that going forward we still need to amortize another 48 Crores or there about but the total impact on my P&L on the amortization side is only 13 Crores, 14 Crores, so the difference between the 70 odd and 48 odd is carried by way of the fact that we have taken a hit on our investment trading book, we have reduced our DBO once by about 40%, 45%. We have shortened the maturity there and all of that flowing into the fee income so I think you need to decide we get the fee income and look at it in that manner. Our forex income is down which is something that we are looking at we need to work little harder to get forex income backup it is by no means is it a large stream of income for us, but we have been impacted by the fact that letters of comfort and letters of undertaking have been stopped. Trade in general given the fact that the dollar has been sold rampant, trade in general has suffered I think on the smaller trader side and total volumes on the FX side have dropped for this quarter for us and we are building plans in contingencies to address this as we go forward. On the other income line, which is the fourth line we have dropped from 37 Crores to 13 Crores and that is on account of the fact that return off recovery from return off dropped very dramatically for us and I think this is something that we have taken as a challenge as we go forward and we do have a substantial chunk of written of accounts and the quantum of recoveries during this quarter is significantly lower than what we have liked. This is on account of a couple of large recoveries that we were expecting not coming through at the last minute. We are hoping that those will flow through this quarter. This is something that as a management team we take very seriously and we are at this point in time kind of figure out how to address this. The other reason that is impacting this income stream is that the revenues associated with the buyers credit product have also vanished, on a quarter-on-quarter basis that is the pretty substantial hit so taking everything into consideration we believe that our total noninterest income that you see in this page is a) understated given the fact that it takes into account the impact of us reducing risk and if were to correct for that we would have been somewhere closer to 215 Crores and the other elements that has impacted us has slowed this down but we think that, that is fixable as we go forward.

You had asked me about growth, our growth is roughly 9% year-on-year and the systemic growth from which I can make out is about 13% 12% point odd so we are about 400 basis points lower than systemic growth and when you look at the growth elements that we have here we find that we are growing on commercial. We are growing only at 10%, which is still lower than the systemic average, and retail we are growing at 28% but that includes a bunch of big ticket transactions that were included so if we exclude them we are growing at about 18% and agriculture is growing at 7%. Initially this is because of the fact that there is an adjustment phase as you introduced a new technology, as you introduce new credit screens and as you introduce new methods of doing things the system requires some time to adjust so we moved from an earlier paper based system to a fully automated system with the new credit screens over Q1 and Q2 and that adjustment process took us a reasonable amount of time and that has impacted both commercial and the retail so while the retail sort of bounced back and did grow on the commercial side we have an drop in growth that we would have liked. So we are reasonably confident that both of these in this quarter three and going forward will stabilize and we should start getting the benefits that we think should accrue from the new technologies that we have introduced. Our new technologies make it much, much easier and simpler for our sales people to sell the product and because of that we think that we should get more throughputs from our branches. As I was telling you in Q2 our average run rate on applications inflow on retail went up 80%, not all of them got converted into loans because we did have some teething troubles in ensuring that what came through as an application also went out as a loan and those are things that we are addressing as we go forward.

On the commercial side the full rollout of digital happen towards the end of September earlier we were just focusing on the renewals. The other products got rolled out at the end of September and we are now hoping that this quarter the full impact of that will start flowing through just the way we are seeing the impact of it on the retail side. On corporate, there is a conscious decision by us to relook at our portfolio, understand where our risks were and to start derisking ourselves and reducing exposures in NIMs that we were not particularly happy with and therefore we reduced about 400 Crores between the prior quarter and now if the reduction had not taken place at least you had seen a 1% growth and not a 1% shrinkage on corporate. So our focus now is to continue to grow and I have maintained that we want to go at market we want to fix our credit screens we want to get high quality growth it is not growth for the sake of growth so this quarter we will aim to be at what the market rates of growth are. At the same time we are relooking at our corporate exposure since those are the ones that has been giving us the majority of our brief and in the event those require some further pruning we will do the further pruning so that will have a attendant impact on growth on an overall level but you should see strong growth on commercial retail and agriculture as we go forward corporate will continue to stay muted.

Rohan Mandora: What is the size of the defocused corporate portfolio when we are looking to exit what was the quantum of that portfolio?

P.R. Seshadri: We have an exit portfolio I was not planning to answer that question so maybe we will come back to you with the number.

Rohan Mandora: Lastly on this Kerala any impact.

P.R. Seshadri: Kerala no impact no material impact for us.

Rohan Mandora: Sir this IL&FS SPV exposure is it in operational effect.

P.R. Seshadri: We do not have any SPV exposure these are all to one entity or another and therefore do not have tied in cash flows they only have the overall cash flows of the entity to whom we have lent.

Rohan Mandora: Got it sir, thanks a lot.

Moderator: Thank you. The next question is from the line of M B Mahesh from Kotak. Please go ahead.

M B Mahesh: Good afternoon Sir. Sir couple of questions from my side. One last quarter we had a the slippages that we saw on the SME portfolio there does not seem to be any recovery and updates visible in the current quarter just wanted to understand where are we on those exposures, which slipped last quarter. Second you mentioned that our retail loans had some few one half's the actual growth was somewhere close to 18% where is the reported number shows 28, I am just trying to understand how do you reconcile was there any loans, which was bought out and the corporate watch list just to reconfirmation you said it is what is spending it from a watch list perspective was 100 Crores is that right?

P.R. Seshadri: Mahesh the corporate watch list was the 165 Crores of non-funded or un-funded assets. The second question was 18% versus 28% retail; retail includes about 700 Crores of IBPC acquired in that quarter. Yes in 2Q we had 500 Crores in the prior quarter and then we acquired another 200 Crores so if you remove that you will come to about 18%, there was no IBPC in September of 2017 and finally the upgradation on the portfolio on the slippages that happened in the prior quarter there has been substantial upgradation but I do not think whether I do not know whether they pertain to specifically that quarter or not so I am had a lot as to how to answer that question. So what I will do is we will try and sort of disaggregate that and come back to you Mahesh.

M B Mahesh: Sorry have you seen any improvement or not?

P.R. Seshadri: I have seen an improvement in both forward flows and backward flows everything is improved on the commercial side. The net number is significantly lower. So both flows into NPA and flows out of NPA are better because of which the net number came in; however, I am not able to figure out whether those are from the items that became NPA last quarter or these are because of newer NPA or earlier NPAs they got upgraded subsequently.

M B Mahesh: Sir but in simple terms, if I had last quarter's outstanding NPAs and I have just add the net NPA then this number is incorrect right this 144 that you reported to us?

Sivarama Prasad: It is correct Mahesh, 144 is comprising of you can see page #35 see 98 is commercial, 31% is corporate, 7% is agri and 80% is a personal retail banking 144.

M B Mahesh: No Sir the problem what is happening is that see if I had last quarter's closing NPA and in fact?

Sivarama Prasad: No that is different. The gross numbers we will give it to you separately.

P.R. Seshadri: We should put it in this deck so that this question have upgraded boss from next time onwards it happen last time. So we will figure it out and put it in here. The numbers are right Mahesh.

M B Mahesh: The numbers we are just trying to see how much has moved in because either 144 number is incorrect because you are adjusting the prior quarter's upgrades and prior quarter slippages in as part of your upgrades and recoveries this quarter?

P.R. Seshadri: That is the net incremental NPA for the quarter boss there is a flow into NPA there is a flow out of NPA because of upgrades. Now if the flow comes from the prior quarter, it is upgradable and it is accountable the way we have accounted it. So I do not understand the point that you are trying to make Mahesh.

M B Mahesh: Sir either this in slide #34 this 975 Crores of fresh additions which has been reported.

Sivarama Prasad: I think April that is full half year Mahesh.

M B Mahesh: No I may ask the same question so what we do is that we just remove 975 minus 785 Crores, which is the slippages which you reported in the first quarter?

P.R. Seshadri: No I will reconcile and send it to you Mahesh.

M B Mahesh: Thanks a lot.

Moderator: Thank you. The next question is from the line of Bhavik Dave from Reliance Mutual Fund. Please go ahead.

Bhavik Dave: Sir just a question on your operating cost, so operating cost last couple of years have started inching up rightly so because they are investing in technology so I just wanted to understand over the next couple of years like from 2019 and like 2020 and 2021 how do we see this operating cost line item shaping up will it be in line with our asset growth or how will this line shape up?

P.R. Seshadri: It is a very good question. During this period costs have tendered up a little bit. There are two broad lines; one is the employee cost, employee costs have gone up on account of the fact that the IBA wage settlement is expected and we have accrued or rather paid out 10% and ad hoc waiting for the settlement. So that is the reason why the employee cost is coming down. The other cost and therefore but when you look at the employee cost you will find quarter-on-quarter actually the employee cost for this quarter has come off a little bit that from account of AS15 accruals being different this quarter as opposed to the prior quarter. Other costs have gone up year-on-year roughly 20 Crores which is a 10% growth in other costs of that roughly 8 Crores are non-repeatable onetime expenses so there is a net impact of approximately 12 Crores and roughly 80% of that is the technology cost associated with the new systems and we think that the accrual rate of the new technology cost will start dropping off after Q4 because by then all the new build outs will be over and we will be on a maintenance mode as opposed to active build out more. So now the currently our revenue expense ratio is standing at 52%.

Bhavik Dave: So this quarter is an aberration let us look at a like more sustainable growth like we have just 44% last year.

P.R. Seshadri: I think as the revenues from the new products that we have launched start coming in I guess with the new higher level of expense, it will renormalized towards the 46%, 47% and then start coming down as the revenue start going up on account of balance sheet growth. We are also aggressively attacking cost we would notice that for the first time our branch count is reduced, this quarter we are trying to sweat our branches harder, our branch throughputs are lower than where we would like them to be so considering the productivity and profitability of these branches we also have a plan to further shrink the nonproductive branches so as to reduce some cost and reinvest that in branches in our core operational areas so our aim is not to reduce branches overall but to get our branch network more efficient. So that process is already underway.

Bhavik Dave: Sir just a data point question what is the number of employees that are day today in the bank?

P.R. Seshadri: That is there in page #33, I think one of the last few pages it is down the number of employee count is down to 7750 or something of that nature I am just going to pulling it up.

Sivarama Prasad: It is in the page #41, Bhavik.

Bhavik Dave: Thank you Sir. Thank you so much.

Moderator: Thank you. The next question is from the line of Jay Mundra from BNP Paribas. Please go ahead.

Jay Mundra: Sir just on this retail yields when we see retail yields are up to 11.3% what is that Sir is this the blended yield or what is that, that is not very clear?

P.R. Seshadri: What I am saying is it is weighted average blended as the word you use weighted average through the door booking yield has increased by 11.3% I have not given you the exact number that it is come in act at the end of Q2 further on an average for Q2 but it has increased very considerably. The booking yield on a weighted average basis is up 11.3% is what we are saying.

Jay Mundra: So let us say if earlier the blended yield was 10% at origination now it is the 11.3%.

P.R. Seshadri: 11.3% that is right. It is a very considerable uptick.

Jay Mundra: How does this risk base pricing work? So let us say across the retail product, let us say in auto what could be the range for risk base pricing so let us say your typical auto product is let us say 10% priced so what could be the range for a across the risk parameter how wide can that range be?

P.R. Seshadri: On the auto side it is less wide than another product in auto it will probably be between 955 which is our MCLR going all the way it is something like 12.55 or 13.00 so it is a 300 basis point spread it is wider for unsecured, unsecured it starts at 12 and goes all the way to touch over 18 and on LAP loan against property is also wider starting at about 10.50 going to 14.15, so it is a big spectrum depending upon the product, depending upon the risk and depending upon what the market will bear because you cannot just price your asset whatever way you want you need to have some semblance of competitiveness in the price so that is how it works.

Jay Mundra: Secondly you also mentioned Sir what the talent acquisition so if you can update if we have need any senior management hire in this quarter last quarter I believe we had hired Chief Risk Officer?

P.R. Seshadri: Yes, some time ago but now we have hired somebody to run our collections. We have hired somebody to run our analytic shop and somebody to run our digital infrastructure. We were relying on third party people to do it for us. We have been interviewing very aggressively. We have a list of about 40 odd people who would be joining us in the near-term. It should not cause a very significant increase in our cost base given that we have lost approximately 250 people over the last six months so the cost impact is not going to be material but a different set of talent will be coming into the office.

Jay Mundra: Just particularly on LAP Sir if you which is around 1570 Crores book for us if you can sort of comment as to what is our preferable ticket size and how much is the LTV how much is cash flow lend or how much is the asset base lending?

P.R. Seshadri: Technically all the LAP is cash flow based there is nothing that is based on collateral, collateral is not the crutch on which the loan is made but cash flow is based on prior period numbers and going forward those cash flows may or may not repeat themselves but the attempt is to find out that stable cash flows and do the loan the ticket size is here are actually quite small. We are talking about 20 lakhs or there about majority of these loans are return in upcountry locations and as a consequence our spreads are also a little larger than those who write LAP in other markets now that we have introduced our risk base pricing.

Jay Mundra: Upcountry meaning Sir Tier II and below is it?

P.R. Seshadri: The Tier II and above, Tier II, Tier III, Tier IV.

Jay Mundra: Just lastly on this retail portfolio buyout or IBPC which are the area is it like mortgage buyout or what kind of a product because I believe this is a retail portfolio buyout right?

P.R. Seshadri: It is home loan and LAP.

Jay Mundra: That is very helpful. Thank you.

Moderator: Thank you. Next question is from the line of Pranav Gupta from Bajaj Sun Life. Please go ahead.

Pranav Gupta: Just a couple of questions. Firstly on the SME slippages last quarter was about 240 Crores and this quarter is about 98 Crores now just trying to understand what sectors the slippages coming from a specific regions just to get a color on where this is coming from exactly?

P.R. Seshadri: Pranav there is no specificity to the kind of NPAs we are taking. By and large these are historical account that through the business cycle have gone mad and we are now not in a position to actually make payments as they are required to. Wherever there is term exposure that tends to be a little bit more risky than where there is working capital exposure and therefore our focus is more on working capital as opposed to return and so last quarter I was asked the same question and we had given you a couple of answers as to why the 240 Crores had come in and we had said that it is because one of the reasons why my colleagues thought that we had a high NPA for that quarter was because of the fact that we trans for all our people in the month of April and that there was a) people did not know their customers as well and perhaps there was also a hint of reducing risk for the manager and question when the collection effort was looked at. Now we had also said that we expected the NPAs to moderate in quarter two that has happened. We have not seeing any particular areas where the NPAs are larger. There are geographic concentrations but that is only to be expected given when most of our portfolios in Southern India. So most of the NPAs are acquiring from Tamil Nadu, but 60%, 70% of our portfolio is there and now so that also does not give us any particular reason to say that these NPLs are happening, but just to add to this our delinquency ratios have as I mentioned earlier been improving we time September 30 we had our best ratios over the last 18 months or thereabouts, which leads us to believe that further NPLs will hopefully be moderated of course nobody knows what will ultimately happen but the underlying trends are positive.

Pranav Gupta: My second question is regarding provisioning going forward so considering that our PCRS comparatively low and we still have some stress, which needs to be recognized in terms of the non-fund exposure of 165 Crores and the IL&FS accounts etc. There you see the PCR going in the next couple of years and what is the target that you are looking at?

P.R. Seshadri: Our PCR is now up to about 43% and from a lows of 30% so it is quite low we agree. We have been slowly building it up as we go forward. I think over the next four or five quarters we were take it all the way up into the mid 50s if we can and at that point given that we are largely secured book, I think we should let it rest and as I point we think we would have adequate provisioning we also think that ongoing incremental NPAs flow through should help us in that process as you rightly said we do have some stress in terms of the unfunded exposures as well as on the IL&FS exposure that we currently we could probably add that to our watch list if you want to but I IL&FS everybody knows, so we want to take it a 55% and we have grown about 1100 basis points now so far and we need another 1100 basis points or there about to reach the end of our journey.

Pranav Gupta: Thank you so much.

Moderator: Thank you. The next question is from Dhaval Gada from DSP Mutual Fund. Please go ahead.

Dhaval Gada: Sir just one more question on the margins if you could comment a little bit how are we placed from here on even what is happening in the banking system and broadly your credit growth outlook how are you seeing margins from here on?

P.R. Seshadri: With respect to margins two three things that I would like to sort of bring to your attention one is quarter-on-quarter our cost of funds have gone up a bit 7, 8 basis points they have gone up and what has happened is that from our we are as I mentioned in the last time around we do have some basis risk in that our assets are reprising differently from our liabilities but having said that I think we are in a reasonably sweet spot. The basis risk puts a little bit of pressure on our net interest margins but given the actions that we have already taken on the risk based pricing front we are reasonably confident that our margins will improve going forward and that we have room on the margin side. Our weighted average yields on for instance retail are significantly above the net interest margin that you see here and similarly on the new through the door that we are getting on the commercial side so our view is that as we price our risk right and as we focus on the right types of risk going forward, NIM will grow and as the market sort of becomes eases out a little bit and as activity from the NBFCs etc., had dropped and as our new technologies enable us to compete more effectively with those folks we should also pickup a portion of the high yield assets that were going somewhere else so we think that our spreads will improve going forward and that in turn will flow through into our P&L and our stated objective is to grow our book at market but grow the spreads faster than market that is what we are intending to do.

Dhaval Gada: So do we have a range where our margins should be on a steady state basis?

P.R. Seshadri: We want to get north of 400 basis points.

Dhaval Gada: Do we have a timeline for this like four quarters from now?

P.R. Seshadri: I will come back to you with the timeline we are working on it, we are implementing piece-by-piece but it takes effort to compute the timeline effectively because we need to figure out we need to compute the basis risks that the underlying basis risk on the current asset book but we will come back to you with the timeline.

Dhaval Gada: But a downward trajectory is arrested in your view from here on?

P.R. Seshadri: Yes, that is my view.

Dhaval Gada: Okay perfect sir, thank you and all the best.

Moderator: Thank you. The next question is from the line of Jehan Bhadha from Nirmal Bang Securities. Please go ahead.

Jehan Bhadha: Sir firstly congratulations for good performance on asset quality. Sir my first question is on net slippages so we have been able to come down to a level of about 144 Crores from earlier run rate per quarter run rate of close to 600 Crores. Sir going forward what is your outlook in coming quarters will this run rate continue, what you have witnessed in September quarter?

P.R. Seshadri: That is our objective or aim, as I said we do have two areas of concerns; one area being the watch list the remaining watch list of about 165 Crores we do not exactly know when that will get called or if that will get called. We are not able to predict what will happen with any degree of finality. The other area of concern is IL&FS to which we do have an exposure and how we need to progress with that and when we provisioning against that will be required is not known and indeed when that becomes an NPA is not known so because we do not know how IL&FS is going to behave and what obligations we are going to meet and what they are not going to meet because the information is not available with us at this point in time. Under those circumstances in the near-term, I am not able to tell you that this number of a 144 Crores can be repeated because of the overhang of these two issues; however, in the long-term, we believe that we want to work towards an NPA accretion rate annualized at a 150 basis points not more so we want to build a portfolio that can give you that kind of an outcome to believe that, that number is ideal because you can then price your assets also appropriately and this 1.2% nearly shows that we are in a position to do that and the large chunks of the underlying portfolio behave in a manner that allows us to get to 1.5% so that is where we are going and I said I cannot give you a better answer than this.

Jehan Bhadha: That is very good Sir. Sir my second question similarly on the provisioning front over there as well we have come down from earlier range of between 300 and 400 Crores to now close to 200 Crores this quarter so out here as well or if in absolute numbers or in percentage terms if you can quantify as to credit cost what can be the steady state credit cost going forward ignoring these two accounts, which you mentioned on the watch list and IL&FS so on a steady state basis what is the kind of credit cost that we are targeting?

P.R. Seshadri: On a steady state basis we are assuming that our portfolio on an annualized basis will have a loss rate of a 150 basis points on a 50000 Crores book that is roughly 750 Crores of NPA and our provisioning requirements would be in the neighborhood of let us say 450 Crores or 500 Crores at max to keep a very high level of PCR. So that is the steady state number that we are going to work towards, we have these event risks that I have already mentioned but I must also caveat that by saying that our current provision coverage ratio is low so there will be an element of catch up provisioning that we will be doing so even if I do get to 175 Crores of NPA accretion for a month our provision the actual provision on the books maybe in a significantly an excess of that number nearly because the provision coverage ratio needs to be built up.

Jehan Bhadha: Sir but after that stages reached from then on then we will be expecting about the 500 Crores kind of annual provisioning cost?

P.R. Seshadri: That is right.

Jehan Bhadha: Thank you Sir. That is all from my side.

Moderator: Thank you. The next question is from the line of Darpin Shah from HDFC Securities. Please go ahead.

Darpin Shah: Thanks for the opportunity. Sir if you can just throw some light on your NBFC exposures worth around 1600 odd Crores have you internally assess them? What is the rating will be having?

P.R. Seshadri: Our NBFC exposure is broadly in three buckets: the first bucket is the NBFCs that are doing gold loans, so this bucket is our largest segment of NBFC exposure so out of the 1600 Crores roughly I would say a third of them are the gold loans roughly 30% would be the gold loan guys and then there are a whole host of smaller tickets that are spread between normal retail lenders and some amount of exposure to HFCs, which is currently limited at about 5% so housing finance companies with long gestation loans or big ALM mismatches is down to about 5% of our current HFC exposure. The exposure to folks who have including IL&FS is roughly about 17%, which is basically infrastructure related and we have approximately gold is 28% and others is the remainder so and those the others are very small ticket each individual exposure would be in the neighborhood of Rs.30 to Rs.50 Crores so these are contained, these are smaller exposures to multiple names, which and these are exposures to people who have smaller maturities on their asset book so we have not got very large exposure on their asset books by deliberately we have kept out of the HFC space.

Darpin Shah: Have you done any assessment on these NBFCs in terms of their ALMs or anything or the retail?

P.R. Seshadri: That is currently underway. It is based on information they provide us and most of those people whom we have talked to have come back with the information and basically tells that they are solvent and they have an ample liquidity and ample bank lines to meet immediate liquidity requirement. Now all ALM projections involve an amount of they involved some assumptions because even banks make assumptions on rollover rates of deposits and so on and so forth similarly the HFCs do them so the question is whether those assumptions are reliable or not and that is something our risk department is fording over as we speak.

Darpin Shah: Sir one last thing if you have any ROA target in mind say for by FY2020.

P.R. Seshadri: As I keep telling everybody that our biggest driver of profitability is NPA and how the NPA line behaves and if our NPA line renormalizes to 150 basis points of accretion for the year, the number that we will get from a return on asset perspective will be quite different from what we have today. Currently our return on assets for this quarter was about 50 basis points and if we had only nearly provided what was technically required to be provided for the NPA that accrued for the quarter, we would have needed to keep 60% or 65% of the provision that we have it would have released another 80 or 90 Crores, which would have for all intense and purposes made the return on assets for the quarter at something like 75 basis points if we had just nearly provided what is technically required by RBI and this quarter also saw expenses rather revenue coming down because we reduced risk on the available for sale book and if that had not happened our P&L would have gone up even further so I think if we can fix the NPA we have visibility to ROA north of 1% reasonably quickly, the question is how long will it takes us to get the provision coverage ratios up to the level that everybody feels comfortable. If that takes three or four quarters there will be additional provision that to be required once the NPA levels renormalized if we can do it faster and we have a windfall gain than the ROAs at that level will start flowing through faster.

Darpin Shah: Thanks a lot Sir.

Moderator: Thank you very much. Due to time constraints we will take that as the last question. I would now like to hand the conference back to Mr. Navin Babu from Spark Capital for closing comments.

Navin Babu: Thank you Raymond. On behalf of Spark Capital I thank the investor community for dialing in today's call. I would also like to specifically thank the KVB management team for taking their time out and patiently answering all our questions. Good day and thanks.

Moderator: Thank you. On behalf of Spark Capital Advisors India Private Limited that concludes this conference. Thank you for joining us. Ladies and gentlemen you may now disconnect your lines.