IndusInd Bank

"IndusInd Bank Limited Q4 FY18 Earnings Conference Call"

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the IndusInd Bank Limited Q4 FY18 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. Romesh Sobti – Managing Director & CEO from IndusInd Bank. Thank you and over to you, Mr. Sobti.

Romesh Sobti: Thank you for joining us once again. As you all know, this call is for our Q4 results. Before we get into the results, I want to point out that we have seen some regulations come in recently and we will talk about not only how this will play out with IndusInd Bank but overall in the Industry. We will also talk about the risks that banks actually run. So we talk about credit risk and we are very fully aware about what credit risk is, we talk about market risk and now of course through a single incident we also discovered there is something called operational risk which goes beyond just the capital provision that you have to make in quarter four every year on operational risk. I think the issue around the operational risk and particularly what comes out of this particular incidence that we all know about is not whether there was straight through processing or not, whether the systems were linked to each other or not.

Let me give you a perspective on this whole issue of swift and the core banking system. Swift has been here for decades, swift is there for 30 years, 40 years, I mean since I started banking. Core banking came only 15 years ago. So what did we do before core banking came in, how did you manage it? I worked in Grindlays Bank for a very short period in the telex department where the swifts actually went out, and that department was like a temple. So the checks and balances were always there. So it is not a question of technology interfacing with swift that can prevent these sort of things, it is all about checks and balances. A lot of commentary has already been made on that subject, but I remember that two years ago also somebody asked me what keeps you awake at night, and I have always said that it is operational risk. Who is doing what, where, when, how soon will I know whether he or she is doing something wrong, and will I know in advance or will I know after the fact, right? So all sort of things are all coming to fore and the 30 or 40 basis points of capital we used up in quarter four is insignificant compared to what you need to do. There is multi-layering on checks and balances which most banks have, but I think you will see a renewed focus on operational risk and you all probably will also focus more on that.

Other than that, I think on the regulatory part there were two deferrals I would say, which were announced recently. One was of course the delay in the implementation of IndAS which has been moved back by about a year or so. The other one, if you recollect 2015 the concept of the capital buffer was introduced, they called it counter cyclical capital buffer that also has been deferred. I think this is a reflection of state of affairs in the banking industry and the capacity of the banking industry to absorb these sort of initiatives.

On the banking, of course the major topic is around the February 12 circular and there is debate and re-debates on the whole thing. We also heard the Deputy Governor yesterday, and I have been asked many times on the thoughts on what it will do to the industry. Personally, I feel that it is a good stepping stone, staging to IndAS per se, that in IndAS it has the concept of SMA0, SMA1, SMA2, etc., and this is actually preparing you for it. The issue is this, when you give a retail loan you take 36 post-dated cheques, on day one or day zero you get your money, right. So retail intuitively therefore does pay on day zero and does not go into day one, corporate does not. Now some of it is logistics that a large multinational pays you on due date and the remittance comes a day later, so you now got to do a resolution plan for it. So it is a logistics issue there, but the discipline of meeting contractual obligations on day zero cannot be taken away.

Of course, people are saying that there are some elements of the circular which will cause stress, yes, what will cause stress is that if you restructure the loan to prevent it going into an NPA you have to call it an NPA, it is no longer standard and therefore you have to make a 50% provision. And I think that is the area that is really causing some angst and other things.

The other, of course with the bond losses that quarter four saw, large bond losses except for the last two or three days, I do not think people were able to sell and book profits, there wasn’t enough demand on that score therefore the dispensation given to amortize MTM over four quarters. We were fortunate that we had no MTM losses, but our gains got whittled down so that is why you see trading profit for us is actually lower than last year, it is down 56%, but we did not take losses so we have not had to amortize at all. The other one of course is what was introduced is the investment fluctuation reserve and we have not yet seen any debate around that, but that will have an impact on your CET1 and also it may have a little impact on profitability as well.

I think that is a little summary of the operating environment. I will take you quickly through the headlines. We have tracked well, we have finished year one of PC4, (Planning Cycle 4), and we have tracked well on almost all accounts. We are very confident that Planning Cycle 4 was thought through well and we will achieve those numbers. Quarter four PAT has come up at 27% and this is despite the lower trading gains, trading gains as I mentioned were 56% lower, if trading gains had come we probably would have made a little bit more floating provision. We were sitting on solid gains, but the gains got whittled down. The NIM remains stable, we have raised MCLR by 40 basis points, so we do expect that down-trending in rates, I think, is disappearing because the cost of deposits have moved up pretty briskly and I think almost every bank has increased the MCLR overall.

Credit growth came up at 28% and what drove this growth was, A) vehicle financing: vehicle financing disbursements went up by almost 47% year-on-year and 12% quarter-on-quarter. And if you see within vehicle financing, commercial vehicles grew 67% year-on-year. So very healthy growth and they grew 27% quarter-on-quarter, commercial vehicle itself. Overall the vehicle finance book grew by 24%. The non-vehicle retail book grew by 31% and this is despite of the fact that we have consciously slowed down Loan Against Properties because we see ridiculous pricing in the Loan Against Property and I think we are seeing low ticket sizes emerging which probably will cause a little bit stress in that sector, not in our book necessarily.

Corporate book has grown by 30%, it normally grows by 25%, we have seen some surge. We have participated in some of the NCLT refinancing that is going on, very large sponsors, etc. Unfortunately, most of this surge came towards the end of the quarter so we have not really seen the increase in NII, proportionate to the growth in the loan book, but hopefully that will flow into the next quarter as well.

Deposit growth also, the industry is showing 5% - 6%, we continue to show 20%, but we toggle between sources of funds, we have always said that. Now we are finding that foreign currency borrowings fully hedged are coming out 100 basis points below the cost of domestic deposits. So we have raised close to $1 billion in this quarter on foreign currency hedged, so we keep toggling between different rates.

The credit cost for the year remains flat at 62 basis points, it was 62 basis points last year. And this has happened in spite of us taking 1) of it partly out of the divergence and 2) because we have chosen to, I think we have mentioned in the press release that our exposure to the two diamond jewelry accounts which are more talked about was limited to one, which was legacy account which was booked in this bank in 1995. The other one we did not have, the big one we never had. This legacy account was there, it is a two-digit exposure, we have chosen to classify it as an NPA. It still remains standard with all banks, it is standard with us also. We have taken a view on this and we have treated it as a fraud and we have taken the provision as per the RBI norms. I will show you the divergence breakup on what caused the divergence. In-spite of these things the credit cost is same as last year as 62 basis points.

And of course, apart from this client-base acquisition is going apace, we acquired 600,000 new accounts in quarter four. 11 million customers is the base now we are going to 20 million customers and we are going apace on that. Earnings per share grew to 63.5. Other than that I think cost to income ratio fell by 1%, we have said that over this Planning Cycle we will drop our cost to income ratio by 200 basis points and we hope that we will be able to meet that sort of target.

We have got RBI approvals for two acquisitions, one of course was Bharat Financial Inclusion where CCI approval has come in two months ago, RBI gave the NOC which came in about few weeks ago, we are now awaiting SEBI approval and post that the NCLT approval, which means that we are on track to integrate this by July of this year. The effective date of course is 1st January, 2018. The other acquisition which is also in the public domain is the acquisition of ISSL. ISSL is a subsidiary of ILFS, which is a professional clearing member of the stock exchanges. It has a 20% market share, it beautifully fits into a gap that we had in our product suite. So the whole issue about clearing membership related current accounts lending to the brokers, custody, depository, all that sort of things. So this also requires now SEBI approval and post that I think the integration will happen.

I already talked about no amortization of MTM losses because we did not have any MTM losses at all. Of course, the other part is digitization, we have been talking about how you are fairing there. There was a UBS survey done recently which ranked our mobile app as the number one app in the country and Forrester ranked us number two last year. So we are catching up at a very fast pace, the number of transactions that are happening are huge, if you want data we can give that. And of course, we were first to introduce WhatsApp banking. WhatsApp may talk about it, we can't for the time being.

Those are the headliners. I can take you quickly through what we said is the outcome of the Planning Cycle 4. And I think apart from this revenue growth, which we said will exceed balance sheet asset growth, and that has not happened only because of the trading gains that did not come up to our expectations. I think we are well on track to achieve all the objectives of planning cycle four. I do not think we should go into this thing.

These are headlines for the quarter. Just want to highlight because there will be the questions around core fee income. Last year if you remember quarter four was a bumper quarter because of the impact of demonetization and the flows of money from the savings bank into the fund industry. And if you do remember our numbers, last year our distribution income in this quarter went up 77%, there was a huge flow that had happened. So there is a base effect which is coming into play which is showing core fee income at 12%, but the quarter-on-quarter growth of core fee income still remains at 3%.

Full year, of course it is a different story, everything grows in double-digit, everything grows in the 20s, including core fee income as well. Top-line momentum, we already talked about growth in our deposits and branches, of course the notable growth is CASA. CASA is year-on-year growth, CASA has grown 43%, savings bank has grown 70%. So that is a very robust sort of a growth in this thing, I do not think we need to spend time on this.

Key financials, ROA, etc., for the full year have improved over the previous year, this quarter because of the surge in advances, the loan book towards the end of the quarter we are seeing some movements downwards. We see normalization happening in both ROA and ROE from quarter one onwards.

Yes, this is the loan book configuration, it is a very congested slide, I do not know whether you can see it. But there is one area where we have not been able to achieve what we said, we have actually said that by 2020 we will do 50:50 between retail and corporate, we are still stuck at 60:40 because corporate refuses to grow less than 25%. So we don't want to consciously restrain them but within that, now we are beginning to see the momentum over the last 12 months except for quarter four vehicle finance was subdued, now vehicle finance is booming. So we hope that we will start moving towards that 50:50, and if we cannot do 50:50 at least we will do 55:45, that itself will be good enough. There isn't much movement in the loan book profile, and the concentrations that happen. Actually concentration in gem and jewelry has gone down, it used to be 6% it went down to 5%. The only one which has moved is power generation and this is a loan to AAA PSU, it is not in thermal power.

The rating profile of our book has, steadily over the last four quarters, moved towards the left, and the left is AAA. And the statistics that we want to share with you, there is a 36% of our book now is AAA & AA and this has moved pretty robustly over the last four quarters, and that is reflected in the RWA and the capital consumption. You see RWA as a percentage of this thing actually has moved down, even in this quarter it has moved down.

So we talk about you know, shift in market share, we talk about shift in our rating profile. That is also consequent to the market share that you can now take market share of AAA companies. And a lot of them are public sector and you know who has released them, where the release is coming from, what is more important for us is the shift in our rating profile of our loan book compared to just market share shift.

CASA I have talked about already, I do not need to go again. Core fee income for the full year it is all showing robust, during the quarter of course we are seeing lower core fee income, essentially because of the base effect of a very strong quarter four, March 2017. Yields etc are reflected in the NIM, our NIM went down by 2 basis points but still in the range. Credit cost, we already talked about credit cost, we are flat at 62 basis points. The movement in the net movement in the gross NPAs was about Rs. 206 crores and I explained to you how much of this was caused by the divergence. And let us talk about divergence, so that is the figure that we all have been waiting for in terms of the divergence number. The number is 1350 Cr., this includes a large account which also figured last year which was the cement account, cement M&A account which was provided in March 2017 and fully recovered in June 2017, but yet has been classified for legacy reasons for March 2017 again, it has no impact, it has absolutely no impact on P&L, it was recovered last year but there is some logic to it which is that it is legacy. So if you take that out I think the figure comes down dramatically, it does not have an impact. Net-net if you go through this whole line, the net addition to our gross NPA was 186 crores because some accounts were already recognized, some accounts were repaid on due dates, etc., and all that sort of things. So the net impact is this thing and the consequential provisioning that we did probably is between 1.5 and 2 basis points as a consequence of this thing. So that is really the impact of the divergence.

So actually this slide, I wrote down this slide early this morning because I thought we needed to consolidate everything into one slide. This really gives a perspective on the book, that the gross NPAs are flat, the cost of credit is absolutely flat, your restructured book is down to 5 basis points now, inconsequential at all. And if you see the restructured and the gross NPA book together also, that also is down to now 1.23%, it used to be 1.31%.

The other question asked is ARC sale, ARC sale the figure is 0.3%, it was 0.35% earlier, it has moved by only Rs. 20 crores during the quarter. PCR remains strong at 56%. Issue about NCLT exposures, we have talked about and now we are disclosing the whole figure, NCLT exposure total for 40 cases it is Rs. 385 crores and we have already provisioned 65%, we don't anticipate any more provisioning as a consequence of NCLT no matter what happens to the resolution. In the steel accounts maybe there is some recovery given the way the bidding has happened. The AAA and AA exposures that we have is now 36% of our book. And I think this is one number which we never revealed before we are revealing because it is only 13 basis points which is the SMA2 number. But our SMA 2 has always been one of the lowest in the industry per se. So that I think is really to focus on the quality of the book and this whole issue about divergence, etc. Divergences are a consequence both of lag in recognition, you could have recognized this in April and it says that you should have recognized that in 31st of March, now does it make a material impact or there are interpretational issues. Now we have Malegam Committee looking at this whole concept and we are happy that this whole thing, because I think banks have also represented on the technicalities that really appear. So how do you define incipient weakness, which is one of the reasons why classification would happen into NPA, it is not an NPA, it was never overdue but there are weaknesses in the account. Another thing is that the account pays you back on the 80th day right, so if you consistently pay back on the 80th day you are weak. So a view could be taken and has been taken that it could be a weak account, it is not technically an NPA. But anyway, I think we will see more light being thrown on this whole concept.

Capital adequacy still remains strong, we used almost 80 basis points of capital in quarter four which is not usual. But as you know quarter four is where you take the impact of market risk and operational risk as well and that was 40 basis points per say. We did not raise any Additional Tier-I, so we do not feel the need to buffer.

That is it. Thank you very much for listening in. If you have questions, more than happy to answer. Thank you.

Participant: Sir, just two questions, one is, the market risk within the RWA has increased substantially, so if you could help us explain that.

Romesh Sobti: Market risk figure has gone down or gone up?

Participant: Gone up.

Romesh Sobti: Okay. It is just a composition of the book, the market risk arises out of what, it is the asset liability profile, right.

S. V. Zaregaonkar: Market risk is placed at Rs. 9,767 crores as against Rs. 9,603 crores.

Romesh Sobti: It is only Rs. 100 crores.

S. V. Zaregaonkar: Operational risk has gone up because that happens every year end and the operational risk formula is there, on the basis of that higher the operating profit we will have higher operational risk.

Participant: Actually I was referring on YoY basis Rs. 6700 crore March 2017 was Rs. 9,700 crores. This has grown by 28%.

Arun Khurana: What really happens is that yes this is based on some non-SLR positions that we normally take & when the liquidity is tight we tend to take it out. So yes we did take some positions on the non-SLR portfolio towards end of March and the numbers in June probably will be very different so we did take the position on that, so it is just very temporary increase.

Participant: Sure, thank you. And sir just one more question, the slippage ratio in the corporate and the consumer books, if I compare to FY2017 it has moved up by 40 - 50 basis points this year, so just wanted the outlook on the slippage ratio?

Romesh Sobti: You want just vehicle financing or consumer as a whole?

Participant: The bank as a whole and then corporate and consumer, would like to get into…

Romesh Sobti: The book increase?

Participant: The slippage ratio.

Romesh Sobti: Partha, you want to take the vehicle financing part?

S.V. Parthasarathy: Yes. Slippages normally in the vehicle finance sector, you can see almost addition equal to that of deletion. I mean, there are marginal accounts which get slipped into this and every quarter substantial portion gets resolved. That is the inherent thing which happens throughout the retail book. For the current year slightly there has been additional slippages, primarily because of last four days there have been holidays in March and quite a lot of persons they did not get money from their principals and more such cases got resolved during the first week itself, of April.

Romesh Sobti: So additions and deductions, you see them together. And especially on retail you see that 90 day past due one installment goes and you classify it as an NPA and when it pays you after 30 days it goes back into standard. So you have additions and deductions almost matching each other as we say, that is why you are seeing here also the deductions are very high, they are almost 85% or 90% of the additions.

Participant: And the corporate book, sir?

Sanjay Mallik: On the corporate book there were primarily two accounts, one is this gem and jewelry account and the other is a road asset that was described in our divergence, in fact it was a standard asset and the entire consortium is standard. But because it is part of divergence it has been notified as a slippage.

Romesh Sobti: That account is standard across the whole industry, now it is standard with us also. But there is a technical reason why RBI said put it into divergence, now we are the first bank to declare results so we have taken it into divergence and we have taken into this thing. The rest of the industry is yet to take it.

Participant: Sir, what is the total system exposure of the account, any idea?

Romesh Sobti: We have given the number, Rs. 104 crores as our exposure. Not sure about system exposure.

Vishal: On this RBI February circular, there is still confusion because every day there is a new article around it. So what exactly is going to happen, one day overdue will have to be resolved within 180 days or there is some breather around…?

Romesh Sobti: Within 180 days, all resolutions have to be done within 180 days.

Vishal: That can be about 30 days.

Romesh Sobti: Yes, even if it is one day. So typically what will happen is a one day delay happens in the remittance coming into this thing. So you say ok resolution plan trigger, now what is the resolution plan, you will pay on day three and you pay me on day three and you pay everybody and not only me, and there is confirmation from every lender that payment has come, case resolved. That is the way it is going to be. And no resolution for 180 days, then in NCLT, 50% provisioning straight away. Actually it should not bother those account guys who always pay in the sense that they are paying instead of first they pay you on tenth day, some people will pay you on the 10th day only. Now what is a resolution plan that they will pay me on the 10th day, so on day one the resolution plan, this is what I think, we have not yet figured it out how this consortium will actually arrange it, that the consortium we are together and say here is the resolution plan the company has called, the company is saying yes I am paying you on the 10th, that could be a resolution, on 10th day I get the payment and its resolved.

Vishal: But that still involve consortium agreeing on it which has not happened in past because the JLF is kind of….

Romesh Sobti: So consortium has to work together, logistics of working together are huge. So in that way the first point of thing was the JLF, the formation of the Joint Lenders Forum. So again it will be the Joint Lenders Forum where all lenders have to come in and even if one lender says I have not been paid is not considered as resolved, that is the problem. So how that lender plays the game could cause an issue. Now somebody wants to exit and he says I have not been paid, I want an exit, that will stall the entire resolution plan, that could, but that is not likely to happen, in good accounts it won't happen, in slightly weak account yes that is a risk that an MNC bank says I want to exit. That's it.

Vishal: My fear is, the reason I am asking you this question is, you may have lent to a company which is maybe 30-60 days old you know it becomes 30 day old and comes back, and the same account becomes overdue with state owned bank. Now, the appetite for SOE bank to take haircut today is zero, on their own. I mean they straight let it go to NPA, so does that basically pose names which otherwise could have been resolved at your level, at your bank level, into unnecessary like NCLT and provisions, etc., would you think like that?

Romesh Sobti: Yes, that risk is there. The question is that if there is any form of restructuring which involves an haircut in any case you have got to make it an NPA, there is no option, you have to make an NPA and make 50% provision, so it hurts you any which way.

Vishal: And just one question actually on the CASA, so how is the cost of SA moving for us, like YoY or quarter-on-quarter?

Sumant Kathpalia: See, I do not think it will move upwards, it can move only down for us. So if you look at the lowest year which most of our balance sheet is at, it is at 4% right now if you look at last four to five….We think that there is an huge opportunity at some point because the big banks are now at 3.5%.

Vishal: My question was how the average cost has moved, if the average cost was 5.5%, whatever that number is, how it has moved in that last one year?

Sumant Kathpalia: It has only moved down for us, last one year it has only been down by 25 basis points.

Romesh Sobti: Because we have played with these slabs, up to 1 lakh used to be 4%, now we have moved up to 10 lakhs is going to 4%.

Sumant Kathpalia: Slabs are 1 lakh to 10 lakhs, 10 lakhs to 1 crores, 1 crores to 10 crores and above 10 crores. So we have different slabs. And the way the balances are moving we decide on which slab to reduce the rate, and as a consequence we get the rated ones.

Romesh Sobti: So, without changing the rate you could bring the average down by just moving up the slab. So for the next instance, for instance now 1 to 10 has now become 4%, supposing 1 to 25 becomes 4% that is the way to go.

Sumant Kathpalia: That is the way to manage the cost.

Participant: Sir, I just had a question that on the corporate side anyway it was expected that private banks will gain from PCA banks and that expectation has been built over the last 1 - 1.5 years, the trend started much earlier. But now the perception is that that trend will really accelerate a lot after the PNB scam and also because more banks are probably likely to come under PCA. So in that case would you want to cap your corporate growth at a certain growth rate or a certain level, or if you get good growth you would continue to take it and see an even better growth in the corporate lending space?

Romesh Sobti: For good quality growth there is no cap, right, how do you cap good quality growth? Now, good quality also means quality of the lending profile, borrowers profile also the pricing. So good quality growth with the right pricing you cannot really put a cap because ultimately you are driven by ROA, where is the ROA coming from. Is the ROA coming because the AAA risk has reduced my capital usage and the returns are good, so that sort of share we are reluctant to put really a cap on, it's not driven by the fact that we want to balance the book. The corporate bank is not only bringing in the interest income but linked to this is the huge fee income, the large fee pools remain in the corporate bag. So it is not that you will accelerate for the sake of accelerating, but you accelerate because you are getting better returns out of the business and the quality is there. What is giving us this ability to pick and choose, that is really what is happening. So you have seen how one of the features now is that we are getting larger share of the PSUs, right, who were AA+ and AAA, who did they bank with? A lot of them in the national banks. So there if you are getting a market share, you are getting a part of the fee pool, etc., and you are lending now at slightly better rates, we do not want to put a cap on that.

Participant: Do you see this acceleration happening in a big way, say in the next one year or so?

Romesh Sobti: Acceleration needs capital, we have done some numbers, top of the head sort of number Sanjay and I have done, suppose you work on a 10% shift in market share, a 10% shift in market share we reckon needed something like $15 billion or $16 billion of capital. So you need capital. If you have the capital yes, market shares will shift, but who has the capital, that sort of a thing you know. So it is easier said than done, but what it is doing is really and that is an interesting part of it, is opening up certain wallets, those wallets were denied to us in the past. A lot of that was the PSU wallet right, I think that is more interesting than just the loan book, trade, foreign exchange, SA, CA, fee procurement, mandates on any procurement, etc., right, all that is really of interest to us and that is the interesting part of it.

Participant: Sir, just following up on that question, when this market share shift happens and let us assume a loan shift from a PSU to yours, which elements of fee income shift with the loan and how much of the fee income shifts independently of the loan?

Suhail Chander: So that depends on the nature of the facility that's shifting right, if it is a working capital facility that is shifting then all the working capital fees will shift together with that facility, either in the ratio of the lending or outside of the ratio of lending is the function of how you market and position for your product. If it is not a working capital facility that's shifting then if it is a loan it is a function of how it is priced and what kinds of other things are associated, or what cash flows are associated. So it is very difficult to say that there is a standard or a percentage, if it is let's say road asset you are shifting then are there any tolls built into this, are there cash flows built into it, all of those things depend on what kind of businesses you are going to get as a consequence of that shift. So there is no fixed ratio, but it depends on what kind of facility shifts and of course the associated fee pools will shift but what fee pools are associated with this depends on the nature of the facility.

Participant: And just an associated question on the corporate yields, because you mentioned that a lot of the corporate demand is coming on NCLT and refinancing cases, does that necessarily mean that your yields are still headed down while your cost of funds is starting to inch up?

Romesh Sobti: If you see the last two quarters the yields have gone up on the corporate side, surprisingly yields went down on the retail side of the businesses, because in the retail side the mix is that commercial vehicles are going faster than the non-commercial vehicles and commercial vehicles are the lowest priced of the lot and there was a little bit of irrational competition going on by a couple of players which will fizzle out sooner than later we think. But corporate yields have actually started moving up, so last quarter also and this quarter also, this quarter yields have actually moved up by almost 11 basis points which is a pretty decent thing. We are yet to see the full impact of the MCLR, so a large part of our book is now MCLR linked, the base rate linkage is almost gone now therefore we should see a better profile on the yield structure.

Participant: Sir, with respect to the gems and jewelry portfolio, sir just wanted to get your sense post this entire fraud as well as the ban on LOUs, how is the business shifting for us? PSU banks are cautious and we have been pretty active in this segment, so is it resulting in more fee income, more domestic working capital requirement and the growth in the overall book?

Romesh Sobti: So, see the diamonds financing business is not based on who is releasing the business, the question is as market leaders in that business we have always chosen to do business only with this client group, we are not going to go for others who are now releasing that business. We have deep domain knowledge of the gem and jewelry business, gems, not jewelry, it is also really difficult to differentiate for the market. We deal with the diamantaires, the stuff you're hearing in the market is the jewelers. So what the diamantaires do, bring in rough, 90 day pre-shipment, cut it, polish it, export it, 90 day post shipment, its 180 day trade finance, we deal with those diamantaires. The top quality diamantaires is a limited group, now those diamantaires also banked with the PSUs, to that extent market share is going to be released, yes we are happy to take that for those diamantaires, not the others. We pick and choose and surprisingly if you have domain domination and domain knowledge consequent to the domination, you will be surprised to see two things emerging, better pricing and lower delinquencies. This is what the game is all about. So yes, we are seeing some shift of the big names, the really good names, I mean we all know that Rosy Blues and the Blue Stars and the Mahindra Brothers and things like that, those guys we are certainly getting market share out of that. We have Biju who heads the diamond businesses, etc., maybe he can shine more sparkling light on it.

Biju Pattnaik: The Managing Director has already told that like in the corporate when there is good quality assets available the bank looks at whether it is good on the risk side and also on the sustainability side and also on the revenue side. And choice is always a function of option, so more option availability is probably positive, but like MD said we pick and choose and who are in our prospect list. In IndusInd as the market leader we never take in any walk-in customers, we have our prospect list, if the client belongs to that prospect list then he can only be on-boarded others have to wait, we never take any client because the client needs money to come to us. So that is our model and it would continue that way.

Participant: And how are you seeing the shift in the LOU, so is it moving towards LCs or more of the fund based exposure across the industry?

Biju Pattnaik: See, LOU is not at all the way the diamond business, like the Managing Director explained, that we do. LOU, it is something which was on the jewelry side and where the people are importing multiple imports to make jewelry and sell in the domestic market, the domestic market is hardly anything for our bank, we are looking at the $82 billion diamond business globally which is really our market is the rest of the world and pan-India, India is a very tiny little market and we do not have much exposure to the Indian market and to the Indian jewelry business. Our exposure is to diamond business and the whole diamond business of $82 billion is mostly restricted in US, around $42 billion, $7 billion in China. Then this year Europe has incremental demand, it has gone up to $5 billion and Japan and Middle East. So these are the countries in which the diamonds go and mostly we track all these markets on every day basis. Generally there is a confusion that probably we are very much doing something like jewelry business which the domestic retailers are doing or the local jewelers are manufacturing, they are spread out over length and breadth of India and we do it only from Bombay from one branch and our business is a global business, only it is geographically located in India because the business is located in India. The manufacturing, 92% of diamonds are manufactured in India, so I think there is some confusion there and there is no LOU in the diamond side of the business at all.

Sanjay Mallik: If I can just add, there is nothing that an LOU can do which an LC cannot do, so LCs will replace LOUs. And in some cases where no LCs are involved banks will use their gift city branches to make buyers credit disbursements.

Participant: And lastly in terms of the commercial vehicle, so how much of the incremental sales and the financing is being led by the replacement or say overloading and how much is more structural in terms of pick-up in activity? So what is like maybe in terms of the growth how would be the sustainability?

S. V. Parthasarathy: See, these are fairly typical questions which come every time, there is no real benchmark to say so much has come out of replacement market, so much has come from new markets and things like that. Absolutely if I say the entire thing is replacement, nobody can question me also on that it is fairly difficult thing primarily because there is no market figure available. However, based on our customer profile and things like that the market has been dormant for about two years, there has been pent up demand that there has not been any appreciation for the past two years because of certain things which happen in terms of demonetization as well as GST implementation as well as there were Euro norms which has also been a reason. Market in reality should have picked up sometime during end of 2016 or so, but it has moved only in end of 2017 for the reasons whatever we have stated. Therefore, since most pickup was due to a pent up market demand, it is not about replacement of the cycle, ok that is one part. Second part is that we firmly believe that we are in the lowest part of the growth chart, there is now bottom of the hockey stick, the market has gone really in one way that's grow. The reason behind is that there has been additional capacity, which is required which has not been put so far. Second is also the fact that people have started realizing that GST did bring in fair amount of revenue as well as viability for the commercial vehicle operators, therefore large number of them have entered into and registered themselves into GST and then started buying vehicles. To put you in some sort of perspective, a person buys a Rs. 30 lakhs of vehicle gets about Rs. 8,40,000 he has to incur towards GST. That GST is available for input credit for in respect of freight it is almost two years he can collect GST but not pay. It improves the viability to that extent. As a result there is a difference pre-GST and post-GST if the same person has two different vehicles, one in pre-GST and one in post-GST, the second vehicle is much more viable, if it is the same model, same thing and this thing. This also adds to certain amount of demand, I mean the lack of understanding people did postpone it, right now people think of it as a viable option. Third is also that, historically election year is always a good year, any election year that does take place in small municipal areas and things like that which really augers well for not only the vehicle industry but also for the construction industry which is poclain type of vehicles where we are a very, very active player. Therefore, I think we should be in a fairly good wicket for the next two years. Only one thing is that boss should not increase our targets.

Participant: Sir, my question on the Bharat Finance acquisition. So, one is, what is the status of approval, how many approvals are pending? And secondly, when we are incorporating the numbers into the financials?

Sanjay Mallik: We received RBI approval not long back, we have applied to the SEBI, stock exchanges. I do not think that process takes too long. Subsequent to that there is a roughly three months' process involving the NCLT because you have to get shareholder approval. And I think it could be around that July period before the process is completed.

Participant: Secondly, from the current strategy of business of microfinance or Bharat Finance what are the other strategic shift we can do in that business, can you comment something on that?

Romesh Sobti: On Bharat Finance?

Participant: Yes.

Romesh Sobti: See, Bharat Finance today is monoline single product business, lending to the poor. So, if you want answer to the question, just look at what Bandhan did after it became a bank. The first side is go on the liability side of the balance sheet and then the whole suite of products you start selling, that is exactly what is going to happen. We have given Bharat the Bank, so the same thing is going to be a replica exactly of that. But in our case it is different because the products already exist, we have got a whole suite of products that anybody, it is a universal bank in that sort of sense. We have a liability franchise, we can help them in that part of the business to draw up the liability franchise. And our ability to raise liability will be slightly better priced, because of the fact that we have been in this business for many, many years. So, I think that from a mono-line business it becomes a multi-product business and the value generation therefore is a multiplier. And as you have seen the valuation that you all have given to Bandhan.

Participant: Second question on the consumer business, one is on liability side what percentage of account sourcing we have online and the second is on loans sourcing side, what is the percentage online currently?

Sumanth Kathpalia: We do what is called as assisted digital, which is that we have a plan and we get the digital also assisted because we like the face-to-face happening. About 28% of our transaction accounts and 56% of our credit cards and BL are online.

Sanjay Mallik: So 48% is of the savings bank is online, 60% of personal loan is digital and so on and so forth. So increasingly the business is getting digitized at the channel level, hardly for example a single digit of transactions are physical at the channel level, everything is internet, mobile or ATM. So progression in digital is very quick, very rapid.

Participant: In terms of guidance, yearly guidance, in terms of loan book growth and credit cost, generally you share some numbers.

Romesh Sobti: Not guidance it's aspiration, there is a subtle difference between that. I think the loan growth in the Planning Cycle 4 also we have said loan growth of about 25%, and I think we have demonstrated that we can do that. The more important part of it is the loan growth at what cost? So the credit cost is important part of it, in-spite of taking these one offs, etc., we have come up at 62 basis points. We have done some sort of internal estimation based on the current situation as it stands today, the improvement in the quality of the loan book on the corporate side and of course with the resurgence on the vehicle finance side. So, aspirationally we would say that we should be looking at credit cost of in the mid-50 basis points.

Participant: Sir, right now we are sharing and discussing financial year 2017 to 2020 our goal and aspiration, once we acquire Bharat Finance so will we share our together strategy or we will stick to it and let it be separate business?

Romesh Sobti: It will be consolidated results for sure, right.

Participant: These all will change after six months?

Romesh Sobti: Yes. So the issue is the way it is going to work is that Bharat Finance will merge so the balance sheet stays in the parent, and then the network goes into the subsidiary as we see. That is the way we proposed and that is the way it has been approved, so nothing changes at that level. The customers remain with those branches, they are managed by the same people, people report to the same people, nothing changes, everything goes in subsidiary, balance sheet P&L stays here.

Participant: All other data which we share will change dramatically with the margins, CASA and all these?

Romesh Sobti: We hope it will be dramatic.

Participant: So that will be shared after six months?

Romesh Sobti: Yes.

Participant: My question is on the CASA, so right now we are on 11.2 million customers and we are targeting around 20 million, so like what source are we looking at to gain the customer share? Is it the mobile banking or is it going to be something else, because there are several banks in this industry say Kotak which is offering around 6.5% rate on savings, so in the coming years or probably next year are we looking to increasing the deposit rates?

Romesh Sobti: Certainly not. In fact, we have seen over the last 12 months and we have already discussed that in the first question that was asked is that we have seen a reduction in our SA and that is the way it is going to be. Because it is not just a function of getting the customer in, it is also customer keeping relationships and causing stickiness by selling cross selling. We are now selling 3.6 products to every savings bank customer in the bank on an average. At the top end of the savings bank customer which is the exclusive customer we are selling five products. That customer who has bought three or five products from you does not care whether his rate of interest is 5% or 4.75%, does not care. So the question is that it is a staged reduction that you cross sell, you show the customer other benefits that are coming out of this thing and then of course the SA becomes incidental. The SA part of it starts as being the most important operational account, and once you have sold the cross-sell products and all, that rate does not matter so much because if he has got a credit card from you and a personal loan from you, has taken a vehicle from you and bought insurance funds from you, then I think the whole relationship changes. So our trending overall on SA has to be downwards in terms of the rates. Yes, there are other banks offering other things, they have their own strategies, but our thing is that if you are acquiring 100,000 new customers within three months we sell the first product to that customer. And then on an average we are selling 3.6 products, we want to go up to 4 products per customer. And a product is not a channel, a debit card is not a product, ATM usage is not a product, it is a channel. Savings bank is a product, mutual fund, insurance, or car loan, or a FX product, those are products. So when we say 3.6 we talk of products and not channels. So that is the way I think the mechanics work on the savings bank side, we expect a down-trending.

Participant: Okay. And the second question was on the loan book, like what percentage of it would be MCLR and what percentage of it would be fixed?

Romesh Sobti: Entire retail is fixed, so retail is now 40% of our book so primarily it is fixed. Vehicle finance is all fixed rate, even the non-vehicle retail is also fixed. Within corporate there are some elements of fixed, term lending part could be fixed but probably linked to some rate with resets every six months or resets every… So partially sort of fixed on a shorter tenure. So, I think we had done one computation way back, what percentage of the book was fixed?

Sanjay Mallik: 50% of the book is MCLR, 40% of the book is fixed; for example, in vehicle financing and the balance 10% is split between variable base rate and corporate fixed loan. And within the MCLR half of it is short fixed. So, its 3 months for example and the other half is long fixed. Could be a 1-year MCLR or a 2-year MCLR.

Participant: Just wanted to understand couple of things here. On the divergence slide that you have reported, in Page #23, and the slippages that you have reported for the corporate sector, could just reconcile how much of the divergence has caused the corporate slippages for the current quarter?

Romesh Sobti: The cost of credit?

Participant: In the slippages.

Romesh Sobti: Yes. If you have seen that at the bottom, that's the GNPA. The GNPA actually is the Net impact on the gross NPA figure was 186 crores. And the credit cost on that account had worked out to 2 or 3 basis point on an annualized basis.

Participant: Just trying to understand. These 539 crores of slippages that you have reported and the divergence slide that you have reported out there. How should we reconcile both of these slides?

Romesh Sobti: Yes, the slippages. The slippages figure does not have those which were repaid as per due date. The slippages and repayments it does not include the repayment. There is an asterisk there which explains that.

Participant: Any idea why would an account which is paying on due date but called as NPA?

Romesh Sobti: Yes. For technical reasons. We also want to ask that question. But we are constrained. But there could be an interpretation. These are interpretational issues. Absolutely standard. Performing well. Paid on due date, not even SMA 0 'AA' client. But there were some interpretational issues. At the end of the day you accept what the regulator says. You only propose, and up to a point give your view point. But if a view is taken, then we accept it. What is there to do. It is by itself a standard account. In our books it still remains standard. But it is classified as a divergence so we did it. It got repaid. On due date it got repaid.

Participant: Sure. Second question, last quarter you indicated your SMA2 Book was about less than 1%. But yet saw slippages of about 70 basis points this quarter. Did many of these corporate accounts move straight away from standard to NPAs.

Romesh Sobti: No. We just talked about an example where the standard account which has been classified as divergence. We talked about that.

Participant: Fee income line, the slow-down that you see in the processing fees despite being one of the best quarters in disbursement, what drives that slow-down.?

Romesh Sobti: Processing fee is not a function of how much lending you did in the quarter. It is also a function of how much renewals you did in the quarter. Because a large part of the processing fee comes out of renewals. A bulk comes out of the renewal. So, if you have lower renewals in a quarter; renewal of loans, you know 12 monthly, you have to renew every loan. Its mandatory from RBI regulatory point of view. Every corporate loan has to be renewed every 12 months, and therefore, processing charges also are annualized. So, it depends on when the renewal happens. All renewals may not happen in one quarter, its staged out. That's the only reason why processing fees is down.

Participant: One question from my side. So, if I look at from your 3 to 5-year next target and your vision where you think, your bank is growing, where are the gaps you feel that you would like to plug in probably wealth management or probably insurance? Where do you think that there are major gaps in that you would like to fill in, probably acquisition or probably organic.

Romesh Sobti: Yes. So, there are 2 parts to this thing. One of this is banking part and the other is para banking part of it. So, on the banking part, I think we have covered almost everything that you needed to do in terms of being universal in your scope and scale. Scale of course you can still bring in. On the banking part, I think we have done almost everything. There are little gaps in our capital markets exposure, we are plugging it with our purchase of the ISSL. It has got a 20% market share. The thing is it will give us some domain leadership in that particular area. The other gap that we had was how to cover rural India. That was the biggest struggle that we were having for the last 2 years. Last 2 years we are seeing rural India starting to bubble. And it is not anecdotal. It's not intuitive. It has based on actually being on the ground and seeing what is happening there. So, rural electrification, rural roads, sanitation, Jan Dhan, Aadhaar Mobile stack, the stack we talk about, (JAM Stack), all that accumulates. We will get a better sensing now through Bharat. But we already had our own micro finance engines running. So, we had a good feel. And we didn't know how to cover rural India. 300 branches were opened in rural India. And we hardly covered a thousand villages. And we don't want this huge gap. Then came along Bharat and it beautifully fitted into that gap that we had on this. We call rural India as the new frontier. Our business model as you see has developed over the last 10 years is mostly urban and semi-urban. Now if you have to cover rural India how many branches will open on organic basis? 300, 500, 1,000? How many villages do you cover? You know how many villages there are in India? Its 6 lakh villages. Then Bharat came in and fitted in beautifully there. 100,000 villages, 1,500 branches, 9 million customers. Not only that, there is a whole ecology of commerce fitted in there. Out of that 8 or 9 million customers they have, there have about 800,000 small kirana stores (convenience stores). The kirana stores have been piloted over the last 1 year, as the human ATMs. So that poor woman who borrowed Rs. 20,000 as a loan from us or from Bharat Finance, typically and this came out in the pilot, that she, walked about 17 km. every week just to either deposit money or withdraw money. Now we have given her a point which is around the corner in her village, the kirana Store. The kirana store is now enabled through a finger print recognizer which is attached to mobile phone and is attached to our CRM system. And account opening and all is enabled. You can deposit money there and withdraw money there. That pilot has run now for almost a year. That ecology we were struggling to cover organically. Therefore, this inorganic opportunity came and therefore I think we have covered that part. So, that's one part. We see huge potential over the next 3 to 5 years. And how it will play out and how the micro commerce is going to play out around these kirana stores, it's just an example of that. The other part is, we count ourselves as a good distributor of third party products. Now the question is, as a third-party product distributor, how much value do we get? We get annuity incomes. How much value does the manufacturer get from us? Huge. As you all have given the valuations. That whether I'ts insurance, life / non-life insurance, health insurance, funds, brokerage all that stuff, we are giving away. So, the whole question is whether you should be capturing that value yourself. And therefore, this thought process has started, how do you capture their value? Should you become manufacturers yourself? Of course, there are many issues around regulations and things like that. But you have got examples of the conglomerate approach where the bank sits on top and lot of the subsidiaries sit below it; life insurance, non-life insurance, etc. We find that a lot of value is being leaked. So, should you be capturing that value whether it is an insurance or funds or brokerage? We have tens of thousands of brokerage customers. We have tie-up with another broker and most of the revenue is going to the broker. So how do you capture that. I think, over this period of whatever, 12 months or 24 months, that thought process will crystalize. Of course, it's subject to the fact that environment for regulatory approvals is conducive to take that. So that's what we see over the next whatever; 12 months to 5 years.

Participant: Is there any example where we have incubated a business and then it became really big in terms of this manufacturing side?

Romesh Sobti: No. Manufacturing on para-banking there is nothing. But all other businesses that is the consumer bank was incubated and went off, micro finance was incubated and see how it is sort of blowing up. The only business that we actually inherited was the vehicle finances business.

Participant: Last question if I may. How much percentage of your total expenses goes for IT and digital side? Compared to industry practice, if you can give us the figure.

Sanjay Mallik: 5.5% to 6% of opex

Participant: And any figure for the industry?

Paul Abraham: That's typically, best in class is between 5 and 7

Sanjay Mallik: I think you have time for just one or two questions.

Participant: Under small corporate book, excluding the business banking book, your growth has been a stellar 59%. Any particular reason for the growth? Are you seeing any particular opportunities here?

Romesh Sobti: I didn't understand the question?

Participant: The small corporate book, excluding the business banking has grown by 59%.

Romesh Sobti: Oh. Small corporate! That's the mid market.

Sanjay Mallik: No. Apart from business banking there is a pretty good growth in the supply chains financing. And also, in the Agri-financing business. And last but not the least, the micro finance portfolio has also grown over 1000 crores quarter on quarter.

Participant: Sir, basically on the saving front we have done exceptionally well. So, what is the share of the government business that could be sitting into the savings deposits as such?

Romesh Sobti: 15%

Participant: And the overall the non-individual a book will be how much in this savings?

Romesh Sobti: That's only government.

Participant: And typically, the average balances out there will be very huge I suppose.

Romesh Sobti: Yes.

Sanjay Mallik: I think just to answer that question on government business, there are some large accounts. But the trick of the trade in this business is to manage the trickle down. So, for example, you get an account from one of the ministries, and they have hundreds of accounts because they are undertaking hundreds of projects across the country. And many of those disbursements, because their job is to spend their budgets in the year, go all the way down into rural India. It could be a land acquisition, it could be anything. So, when we are doing a mandate for the government or any of their ministries, you are actually able to see the entire trickle down. And then what is perceived by you as possibly a larger account or a transitory account actually becomes a much more sticky account. So, that is the sort of transition you have to undertake to ensure that the CASA grows and become sticky in the process.

Participant: Sure. In that case, what is the CASA ratio aspiration that we have, that we have already crossed what we aspired last time around. So, we have now about 44% odd.

Romesh Sobti: We want stabilization of the 44% before we re-aspire.

Participant: Okay. Great. And in terms of margins, once the Bharat financial inclusion merger does happen, post that, what could a margin look like, particularly in the second half of the FY19?

Romesh Sobti: That will play out. But it will be accretive for sure. Its not only NIM its ROA, its ROA accretive, its ROE accretive, its NIM accretive. Its EPS accretive, its capital accretive. Capital is the big one. There will be huge increase in the capital makers. They are capitalized 31%.

Sanjay Mallik: But you have access to their cost of funds? You have access to our cost of funds, and you have access to your respective growth rate and that should give you the answer.

Romesh Sobti: Little bit of calculation has to be done.

Participant: Okay. Yes. Sure. Sir on the asset quality, sir this year we have seen lot of corporate slippages primarily because of the divergences and the other things which happened in the banking industry. Sir next year, in FY19, whether the corporate slippages is run rate certainly because, now even the bulk of the restructure book has been taken care of, we don't have any further deferred stress pool as such. And the divergence is also, which was there, big enough have already been factored in. So, in that case, next year, particularly FY19 should be good in terms of the corporate slippages.

Romesh Sobti: Yes. See there is no guarantee that RBI will not come with another regulation on the divergence. In this, it's perceptional. Otherwise, we have looked at our own book. Our book, both on the corporate side, I have given you an idea of the vehicle finance side, also the retail part we have taken, it points towards an aspirational credit cost of 55 basis points. Mid-fifties, that's what we are looking at. So, that's hopefully, that's what should transpire. But last year we had aspired for 60 basis points. We came around that. We should have actually come below 60 basis points, except for this divergence which probably added 2 or 3 basis points to our whole thing. So, aspirationally we, looking at the book quality, looking at the fact that the rating profile of the corporate book has actually moved towards the left, towards the AAA and AA, then I think aspirationally, that figure of mid-fifties as the credit cost is not over ambitious.

Participant: And this SMA II to book that you have, 13 basis points, this is for the march. But typically for the year as a whole, what would be average?

Romesh Sobti: It varies from 13 to maximum of 20 basis points.

Participant: Okay.

Participant: Hello sir, thank you for the opportunity, in the beginning you mentioned about the risk that investors generally overlook. And one of the ways to understand risk is to understand the Asset Liability Management Report. I was going through the Asset Liability Management Report of FY17, and it is expected that the assets over a period of time can pay the liabilities. So, for the first 6 months, the asset came around to be 44,700 crores, but liabilities outstanding were 56,000 crores. So, there was a gap of around 11,600 crores. Then I went one step ahead and measured the asset that can come to the company in one year. It came around 64,000 crores and liability in terms of deposit that can be taken by customers and borrowings that can be asked for came around 87,300 crores. So, it shows a gap of 23,300 crores. And the cash that bank had for the period of one year was equivalent to 12,600 crores. So, even then, approximately 11,000 crores cannot be funded as per the FY17 if liquidity issues arise. So, what is your take on that? How can an investor feel secure if in one year there are chances that all the deposits and all the borrowings as per the norms go away?

Romesh Sobti: No, So, the gap is consequence of you have not taken the investments into the assets.

Participant: I have included investments, advances and foreign assets also.

Romesh Sobti: Then of course you have taken the cash reserve ratio, you have taken the CRR, and the Net worth of course. The net worth also funds part of the asset. So, I think the question to be asked is does it cause any Asset Liability mismatch? Also, liabilities are not the only source of funding the assets. Right? You add liabilities and borrowing. And then you equate them to your loan books and your SLR portfolio on the investment sides. And then see, what is more important here is the mismatch in term of tenure. That is more important. If you want to measure market risk, you really have to look at the tenure risk that you are carrying. How are you funding your vehicle finance book? Right? The vehicle finance book is a term book with an average tenure of 24 months. How are you funding that book? That question is more relevant than who is going to fund what? Right? So, if I am using short term money to fund the vehicle finance book and short-term money is coming and giving me a huge spread then interest rates move up, you bleed. That is more important. So, we have mismatch book.

Arun Khurana: I think the way I look at is as follows. We have got something called a LCR ratio (liquidity coverage ratio), and its measured on a daily basis for next 30 days. What does it really do is exactly what you have just spoken. It measures out flows verses the inflows, on the liquidity. So, minimum required by RBI, from 1st of January is 90% on a daily basis. We are maintaining on an average a 100%.

Sanjay Mallik: Quarter end is 109%.

Participant: Yes. Thank you, sir.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of IndusInd Bank Limited, that concludes this conference. Thank you for joining us. You may disconnect your lines now. Thank you.