IndusInd Bank

Q2FY22 Earnings Conference Call Transcript

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Moderator: Ladies and gentlemen, good day, and welcome to IndusInd Bank Limited Q2 FY'22 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Sumant Kathpalia, Managing Director and CEO, IndusInd Bank. Thank you and over to you, sir.

Sumant Kathpalia: Good evening and thank you for joining this call.

I will start with some macro commentary and then go into the bank specific details.

Economic activity is gradually improving with easing mobility restrictions, rising pace of vaccination crossing 1 billion mark, growing exports, favourable financial and market conditions and increasing government capital expenditure. Consumer and business confidence on future prospects is also improving. Strong performance of the farm sector, pick-up in manufacturing activity and now even a recovery in the contact intensive services, bodes well for growth in bank credit going forward. A decadal low interest rates across major segments, is also expected to drive up credit demand, helped by the receding of the pandemic related disruption as almost 65-70% adult population is likely to be fully vaccinated by year-end.

Key risks to India's macro-economic stability and prospects are seen from adverse global developments around commodity price spikes, supply chain disruptions and faster-than-anticipated tightening by major global central banks. With foreign exchange reserves at record levels, improving external balances, inflation within the target band and the growth picking up, Indian economy can negotiate the global headwinds successfully over the coming year.

Now coming to bank specific commentary. We will upload this commentary on our website for ease of reference after the call in case you miss any of my comments. We have also refreshed our investor presentation with some new details. I hope you will find these useful.

Coming to Q2 - during the quarter we focused on:

- <u>Strong Loan Momentum</u> – Our loan book growth continues to improve every quarter with Q2 growth at 10% YoY and 5% QoQ. We saw most of our retail products disbursements crossing pre-Covid levels. The Corporate book too accelerated growth momentum. Overall Corporate grew 7% QoQ while Consumer grew 3% QoQ.
- <u>Maintaining Deposit Traction</u> – Our deposit growth was strong at 21% YoY and 3% QoQ driven equally by CASA and term deposits. Retail deposits as per LCR grew even stronger by 48% YoY. The deposit traction has remained healthy despite the rate cuts on our savings as well as deposit rates last quarter. Our cost of deposits has thus reduced to 4.85% from 4.97% last quarter.
- <u>Asset Quality</u>: We saw collections getting back to normalcy across our portfolios barring small pockets in microfinance. As the accessibility was impacted during Q1 and in some states in Q2 as well and given the high touch nature of vehicle and MFI businesses, customers moved into NPA and came out as we collected payments. Overall collections for September were at 98% as against 96% in June. Slippages during the quarter net of upgrades and recoveries reduced to 0.57% as against 0.90% last quarter. As a result our credit costs have fallen by 35% QoQ from Rs 1,132 crores to Rs 752 crores. We have maintained our PCR at 72% and increased our contingent provisions to Rs 3,178 crores or 1.4% of loans. This includes prudent contingent provisions towards a stressed telco and will share further details later. With this I believe all legacy exposures are taken care off and balance sheet is well positioned to support growth.
- <u>Maintaining profitability of the franchise:</u> Our operating profit margin remains healthy at 6% of loans. Our NII grew by 12% YoY ahead of the loan growth. Fee income grew by 18% YoY driven by client fees particularly the retail segment. While operating expenses have normalised as activity levels picked up, the Cost to Income ratio is still better than pre-Covid levels. This ensured maintaining our healthy operating margin.

- Scaling up New Initiatives: We continue to scale up our new initiatives of Affluent, NRI and Merchant Acquiring Businesses. Affluent deposit base grew 48% YoY to 35,700 crores and AUM grew 42% YoY to 61,800cr. NRI deposits grew 31% YoY to 27,500 crores. Our merchant acquisition through BFIL added 120,000 merchants during the quarter taking total onboarded to 320,000 merchants now. Of this 175,000 customers are borrowers and loan book originated crossed 1,000 crores for the first time.
- Digital Launches: We continue to execute our Digital 2.0 strategy and Quarter 2 saw new launches in terms of Indus Merchant Solutions' app, Indus Easy Credit stack for Business and Debit Card EMI on IndusInd Bank debit cards. I will give you further details subsequently.
- Capital Adequacy: Our capital adequacy remains comfortable and improved to 18.06% including H1 profits. We have received board approval for raising Tier 2 bonds of Rs 2,800 crores. This will further augment our overall capital adequacy levels.
- Strengthening Leadership Team: We have made key changes in our organisation structure over the last few months. The focus has been to strengthen our corporate franchise along with the assurance functions such as risk, compliance and audit. There have been lateral hirings along with internal reallocations. Overall I believe the leadership team is now well set to deliver on the PC-5 ambitions.

Now coming to individual businesses:

1. Vehicle Finance:

- Our vehicle finance disbursements saw strong come back during the quarter. The disbursements for the quarter at 8,600crores grew by 62% YoY and 76% QoQ. The disbursements have been also higher than the pre-Covid Sept-2019 quarter. This makes it the first quarter after Covid outbreak where disbursements have been higher than the pre-Covid levels.
- The Bank has caught up on disbursements to pre-Covid levels whereas the industry volumes are still lower indicating continued market share gains across the products.
- Within vehicle categories, disbursements picked up significantly for Commercial Vehicles and Cars. The tractors and construction equipments continued their good run throughout the pandemic period. We have been cautious on the small commercial vehicles and two wheeler growth.
- The loan book has remained stable owing to higher rundown due to contractual maturity and focused collections as evident from the recoveries.
- The collection momentum has resulted into strong recoveries and our vehicle gross NPAs have reduced QoQ across various segments. We saw upgrades and recoveries of Rs 555 crores in vehicle finance during the quarter.
- As highlighted earlier, we saw customers opting for restructuring to tide over the Covid-2 lockdown impact. The vehicle finance restructured book increased from 3,089 crores to 3,969 crores QoQ.
- Of this restructuring, around 80% comes from the contact intensive MHCV and 3-wheelers segments. Balance 20% is spread across all other vehicle categories. The restructured customers have been of acceptable credit risks pre Covid and the portfolio is well collateralised providing us comfort on potential delinquencies.
- We see freight availability improving every month and as collections normalise, the disbursements should start reflecting in loan book growth from this quarter.

2. Microfinance:

- Microfinance has shown strong growth recovery with Covid spread coming under control. We saw loan growth of 26% YoY and 9% QoQ on a weak base.
- Collection efficiency for the quarter was at 94.7%.
- We have seen accessibility improving during the quarter across most of the country except for in Kerala and a few districts of West Bengal. Collection efficiency excluding Kerala and West Bengal is close to pre-Covid levels.
- The gross slippages during the quarter were 1,070 crores. As the accessibility and collections improved, we saw customers clearing up dues resulting in upgrades and

recoveries of 610 crores. The slippages thus net of upgrades were 460 crores or 1.6% of the loans.

- We had highlighted in the last analyst call that customers with ~500 crs of portfolio have invoked restructuring. We saw restructuring implemented for these customers during the quarter along with fresh restructuring for 407 crores. Thus the total restructuring as of Sep-21 was at Rs 907 crores. Over 55% of the restructured customers have completed atleast 3 loan cycles with us and over 81% completed 2 loan cycles. These customers thus have strong payment trackrecord and expect majority of the restructured pool to show comfortable payment behaviour.
- Looking at the overall collection trends, Covid 2 stress in terms of credit costs and restructured pool is likely to be between 6% to 8% for the year in my view. The expected stress is higher than the first wave due to deeper Covid spread in the rural areas and non-availability of moratorium in second wave.
- We have conservatively fully provided on GNPAs and carrying contingent provisions to absorb this impact. The overdue buckets have also fallen by half during the last quarter indicating the delinquencies should normalise post December quarter.
- We also scaled up our non microfinance initiatives. The merchant acquisition business grew to 3,20,000 merchants. The loan book crossed 1,000 crores for the first time from borrowing customer base of 175,000 merchants. We have also scaled Bharat Money Stores from 75,000 to 91,000 during the quarter. These businesses will add diversified revenue streams to BFIL.
- Overall, we are seeing credit demand coming back in the rural economy. We have been cautious on new customer growth and acquiring them only from well performing districts. We remain vigilant on ensuring collection efficiency maintains upward trajectory.

3. **Other Retail Assets:**
   - This segment contributes 15% of the overall loan book and includes secured and unsecured retail assets.
   - After navigating through a rather subdued Q1 due to Covid, asset disbursals resumed growth in Q2.
   - Growth in disbursal was witnessed across secured and unsecured loans. LAP and Business Banking disbursements are back to pre-Covid levels and expected to maintain traction in coming quarters.
   - We had highest-ever credit cards spends at Rs. 4,139 crores which was up by 55% YoY with highest-ever monthly new card acquisitions crossing 50,000 cards in Sep-21.
   - Our credit card spends per client in September have grown 52% QoQ and 81% YoY.
   - We also launched co-branded card partnered with Vistara during the quarter which has seen good customer response. Our proposition is well received by affluent customers with average transaction size over 2x compared to other cards.
   - The collections from this consumer segment have stayed stable throughout the Covid second wave.

4. **Corporate Bank:**
   - The corporate book maintained its growth trajectory this quarter as well with QoQ growth of 7% and YoY growth of 15% with loan book realignment getting behind us.
   - The growth was driven by demand from NBFCs, Roads, Education and Textile segments particularly from the higher rating profile, shorter duration and granular exposures as per our revised underwriting.
   - Average rating profile of the corporate book improved to 2.63 from 2.87 YoY which is equivalent to "A" rating.
   - Slippages from corporate book at 252 crores have remained small in this quarter as well. We have also seen positive movements in a few restructured accounts and expect upgrades to happen at appropriate time.
   - We had in the past disclosed exposure to a stressed telco of Rs 995 crores fund based and non-funded exposure of Rs 2,276 crores. As you are aware, the government has announced major relief package improving the viability of the telecom sector. This and other developments have reduced default risks particularly on the non-fund

exposures in my view. We believe our guarantee exposure could come down in light of these developments and will update you once the clarity emerges. We have nevertheless prudently made contingent provisions to the extent of fund based exposure. With these provisions and our inherent strong profitability, I think the last of the legacy exposures is also behind us.

- We have reorganised our corporate banking franchise. Sanjeev Anand who was responsible for mid-corporates will now head overall Corporate Banking as one unit. We have also strengthened our team by lateral senior level recruitments including Niraj Shah who joins us as Head of Institutional and Strategic Clients Group. The investment banking as a product unit is now housed under Dy. CEO Arun Khurana who is in-charge of all the product units for the Bank. A new head of investment banking is expected to join us next month.
- The Corporate Banking team is now well organised, has clear underwriting frameworks and is without any legacy exposures to worry about. I believe this positions us well to participate in the corporate credit growth revival.

5. **Gems & Jewellery:**
   - Our Diamonds manufacturer financing book continues to maintain pristine asset quality with no NPAs or SMA2 or restructured loans.
   - The loan book saw good growth of 4% QoQ as borrowers utilised working capital lines ahead of the festive season.
   - We expect the stable loan growth and asset quality position in the foreseeable future.

6. **Now coming to Deposits:**
   - Retail liabilities mobilisation remains cornerstone of our PC-5 strategy.
   - Deposits grew 21% YoY driven by 26% YoY growth in Current and Savings account. Retail Deposits as per LCR growing 48% YoY and 6% QoQ.
   - We had reduced our deposit rates across savings and term deposits last quarter and the deposit momentum was maintained despite these rate cuts.
   - Our cost of deposits at 4.85% saw a reduction of 12 bps during the quarter and 120 bps cumulatively in 6 quarters since I took over.
   - Our reliance on Certificates of Deposits continues to remain low and has fallen QoQ from 3% of deposits to 2.5%.
   - Our Affluent business continued strong performance. Our deposits from this segment grew 48% YoY to 35,700 crores.
   - Our NRI business grew 31% YoY to 27,500 crores. NRI segment saw strong CASA growth of 62% YoY while term deposits grew by 24%.
   - We have also received the Agency Bank Authorisation from the RBI. As Agency Banker, IndusInd Bank gets the privileges of doing collections and payments on behalf of the Government of India and the State Governments. We have already signed MoU with Central Boards for Direct and Indirect Taxes. This will strengthen our foothold in Government Business and increase stickiness of our Retail & Corporate customers.
   - We have maintained our overall average LCR at 148% and were running surplus cash balances and excess investments of over 59,000 crores. As we saw loan growth acceleration in the later parts of the quarter, the average surplus liquidity is expected to come down from current quarter onwards.
   - As a result, our reliance on borrowings is coming down every quarter and moving towards long term sources. We have shared details in the presentation with almost all of the borrowings from long term sources.

7. **Digital Traction:**
   - We continued execution on our Digital 2.0 strategy and Q2 saw new initiatives getting launched
     - During the quarter we launched 'Indus Merchant Solutions' app, Indus Easy Credit stack for business owners and Debit Card EMI on IndusInd Bank debit cards. These are in addition to the Easy Credit for Individuals launched in the last quarter.

  - Indus Merchant Solutions provides small merchants and retailers a unified stack to bring all their payment, lending and banking needs under a single umbrella.
  - Indus Easy Credit stack for business owners provides easy access to small ticket unsecured business loans as well as secured overdraft upto 2 cr in a completely digital manner.
  - Debit Card EMI is a convenient consumer financing solution at Point-of-sale for our customers.
  - All these initiatives are cloud native, microservices driven API based stack making us ready for platform banking and open banking and will give us the needed scalability and agility.

- The digital adoption and volumes continue to see growth

  - Digital transactions contribute 91% of the total customer transactions.
  - Close to 4 mn sales happened digitally during the quarter across retail products showing ~50% growth on sequential basis.
  - The mobile app user base increased by 36% YoY and mobile transactions are up 2.3 times YoY.
  - Bank's refreshed mobile app with cleaner interface and response time improvements continued to get positive feedback from users. 'All New IndusMobile App' is now rated 4.3 on PlayStore and amongst Top 3 rated banking apps now.

- Overall we remain on track on digital along with new initiatives on individual and vehicle finance segments planned for launch in a few months.

Now coming to the financial performance for the Quarter:

1. Q2 witnessed acceleration in growth momentum with NII up by 12% YoY at 3,658 cr and operating profits at 3,219 cr was up by 13% YoY. Our PPOP/Loans was maintained at 6% in a tough operating environment.
2. Our NIM for the quarter was stable at 4.07%. Our Yield on Advances came down by 9 bps due to mix in favour of Corporate and shift towards higher rated borrowers. The cost of deposits also fell by 12bps QoQ maintaining the stability of the margins.

3. Other income grew by 18% YoY. Client fees rebounded after a weak Q1 due to Covid. The client fees grew 24% QOQ and 42% YoY driven by strong retail fee recovery. Share of retail fees has improved from 48% to 59% QoQ. Income from trading was at Rs 332 crores for the quarter.

4. Our Cost to Income ratio inched up slightly to 41.4% as the business momentum picked up during the quarter. Overall we are still below pre Covid Cost to Income levels of around 43%.

5. Now coming to provisions and some asset quality indicators.
   - We continued to follow conservative provisioning approach. Our provisions for the quarter were Rs. 1,703 crores.
   - With strong collections and recoveries, the specific credit cost provisions for the quarter reduced to 752 crores from 1,132 crores QoQ – down by 35%.
   - We prudently added 978 crores of provisions towards contingent buffers taking our surplus provisions to 3,178 crores or 1.4% of loans.
   - Our GNPA has come down to 2.77% from 2.88% QoQ and Net NPA was down to 0.8% implying a comfortable provision coverage ratio of 72%.
   - Total loan related provisions are at 3.9% of loans or 138% of the GNPAs.
   - Our SMA1 and SMA2 book is stable at 30bps and 49bps respectively.

6. Our Net Profit momentum continues despite the conservative provisions. Profits for the quarter were at Rs 1,147 crores growing 13% QoQ and 73% YoY. Our CRAR including profits improved to 18.06% from 17.89%. CRAR will be further augmented with planned Tier 2 issuance during this quarter.

Overall, I think we are trending well towards our PC-5 ambitions.

1. The strong disbursements in the retail segments coupled with rebounding corporate franchise provides us comfort on continued loan growth and NII acceleration.
2. The deposit side has been chugging along nicely with growth in retail liabilities to 41% of deposits along with reduction in cost of deposits.
3. We have been able to maintain our strong PPOP margins at 6% of loans in one of the toughest operating environment.
4. We have built strong coverage on stressed exposures including all legacy accounts.
5. Our restructured book has been performing well and has adequate contingent provisions. Our bottom up conservative simulation of credit costs from restructured pool of 20% in vehicles, 10% in corporate and secured retail and 50% in unsecured retail including microfinance leaves surplus even after making 100% for telco funded exposure.
6. The Return on Assets has improved to 1.29% and Return on Equity has moved into double digits this quarter to 10.29% and should have been in mid-teens if not for the contingent provisions.

As risks from Covid and legacy exposures are diminishing every quarter, we are well poised to show underlying growth and profitability of the organisation. We are committed to our PC-5 growth ambitions.

With this we can now start the question-and-answer session.

Moderator: We will now begin the question-and-answer session. The first question is from the line of Nitin Agarwal from Motilal Oswal Securities. Please go ahead.

Nitin Agarwal: So, the first question is on the contingent provisions that we have increased up this quarter, so is it like some formula-based or purely discretionary and how will the drawdown approach be from this reserve that we are building?

Sumant Kathpalia: This is very well thought-through and of course, formula-based. So, 100% of the telco funded exposure has been provided for. That is what we committed and we have done that already. So that's number one. Number two, I think we have looked at our flow- through rates and the collection efficiency of the restructured book. So one is the regulatory guidelines of what you need to do. We have taken excess provisions basis the flow rates to be comfortable and taken a very conservative approach on what the flow rates will be and basis that we have taken provisions. In addition to that, we have kept a buffer of about Rs.300-400 crores which can help us if there is any other flow. We will continue to see this space and if we see that there is deterioration, we will provide. Even if there is improvement, we will maintain these provisions because they will come in handy at some point of time.

Nitin Agarwal: But as of now, shall we take it that we don't need to provide more or will we continue to make these provisions?

Sumant Kathpalia: Actually, we don't need to provide more, but being a prudent banker, I think we may provide more if we see there is a need for it. But at this point of time, I don't think we need to provide anything extra. What we may do is for the non-funded exposure of telco, we may provide some amount extra and keep it aside.

Nitin Agarwal: On the restructured book, how much of this is paying currently and how much is under moratorium and what sort of slippages like we are building from this pool?

Sumant Kathpalia: So, let me answer this question in two ways. Our restructured book has been performing well and we have adequate contingent provisions. If I see the book, overall ~90% of the book is paying the installments. You have to go by segments to see that, I think on the corporate side, in fact, you will see some accounts moving out and a large part of the pool, 80% of that restructured book may be moving out because, almost a lot of this has got settled for us. On the commercial vehicle side of the book, there are two things which you need to observe. Majority of these clients are very good clients of the bank. And they have asked for a deferment or a smaller EMI payment because of the pandemic and they were also scared of the COVID-3 at that point of time and they are regular in their payment. We have taken a 20% provisions, however flows of this book, I believe would not to be more than 10%. The book is performing well for us as of now. On the unsecured side, which is the microfinance book, I think these clients have completed 2 or 3 cycles with us. On a conservative basis on unsecured, we have taken a 50% flow-through rates. Actually, the collections on the microfinance has not started yet, because restructuring has just happened. On the other unsecured restructured book, we are seeing a 50-60% collection efficiency. We are seeing a ~90% collection efficiency on the secured non-vehicle side of the restructured book. So, that is how our provisions are made and that is how we are seeing the restructured book to perform.

Nitin Agarwal: Couple of more questions: we have added a few senior management team members. Are we also seeing any churn within the top management or in the mid-level management given the rising competitive scenario in the overall banking and financial space?

Sumant Kathpalia: So there is a stress, specifically in the technology side or on the digital side, where we are seeing stress in certain areas. We are not seeing a stress in our corporate banking, in our retail banking or in our vehicle finance unit at all. I must give you this confidence that the bank has adequate succession planning in place and we make sure that when we create an organization structure, there is second person in charge or multiple backups are created to make sure that the continuity of the business remains.

Nitin Agarwal: If you can offer any comments on the bid that we have submitted for Citi's consumer business like how are we looking to pursue growth in the consumer assets?

Sumant Kathpalia: I have never accepted the fact that we have submitted a bid, that's number one. Number two, I have always said that the news appearing in media is speculative and we continue to evaluate businesses which are accretive to our stakeholders which is our customers, to our investors as well as to our shareholders and to our employees.

Moderator: The next question is from the line of Sameer Bhise from JM Financial. Please go ahead.

Sameer Bhise: Just a quick question on the microfinance piece. What is the nature of restructuring offered here, is it like a moratorium say for how many months and any details there?

Sumant Kathpalia: So, we could have offered an extension up to one to two years in the business and that's what we have offered. I don't think there is a moratorium which has been offered. There may be some cases where we have offered a moratorium of interest-only payment which have been offered for upto six months to the customers.

Sameer Bhise: So the weekly or monthly outgo whatever it is, it goes down, when we don't offer morat, but just extend the term, right?

Sumant Kathpalia: Yeah, just extend the term.

Sameer Bhise: On the corporate book, we have seen a reasonable amount of growth sequentially. Any comments on pricing there?

Sumant Kathpalia: Yes, pricing is very competitive in the corporate world, but please understand I am sitting on excess liquidity and I was putting it in the reverse repo at 3.4%. So please understand there is an opportunity to do short-term lending, working capital loans on the corporate side at 4.5-5%, that's number one. Number two, we have got very good triple-A rated and double-A rated papers in the good public sector enterprise where we have done these businesses and we felt very comfortable doing that businesses at that point of time. Also, we found good exposures coming in NBFCs, textiles businesses.

Sameer Bhise: Just a breakup of the restructured book between corporate, commercial and retail?

Sumant Kathpalia: Let me give you the restructured book. Our restructured book as of September '21 is Rs.7,982 crores, up from Rs.5,657 crores. Our vehicle finance restructured book is Rs.3,969 crores which is 49.7% of the overall restructured book. Secured retail is Rs.763 crores which is 9.6% of the restructured book. Unsecured retail is Rs.365 crores which is 4.6% of the overall restructuring. MFI is about Rs.907 crores which is 11.4% of the total restructuring and corporate is Rs.1,978 crores which is 24.8% of the restructuring.

Moderator: The next question is from the line of Gaurav Singhal from DK Partners. Please go ahead.

Gaurav Singhal: What was the fund-based exposure you had to the telecom operator which you took as provision?

Sumant Kathpalia: It's around Rs.995 crores.

Gaurav Singhal: So, that's the majority of your contingent provision?

Sumant Kathpalia: Yes.

Gaurav Singhal: Around the time of the government package, Vodafone had mentioned that there was a lot of relief on the non-fund based side. There were 80% reduction in BG requirements or license fee. I think there is no BG requirement now for these AGR dues. How much is the non-fund exposure today? How much will be released based on these new rules?

Sumant Kathpalia: Gaurav, I think we still await the final fine-print from the DoT and telco. We have Rs.2,276 crores of BG and what we have been informed is that it will move down substantially. However we are waiting for the final details and the final fine-print before we reduce that exposure.

Gaurav Singhal: But if that is close to 80% number which was in the press?

Sumant Kathpalia: I cannot comment till I see the final details and we have to see the document and we await those final details.

Moderator: The next question is from the line of Kunal Shah from ICICI Securities. Please go ahead.

Kunal Shah: Firstly, in terms of OPEX, across most of the peer banks, we had seen huge investments in OPEX this particular quarter and there was a jump on a quarter-on-quarter, year-on-year. Ours is still managed well. How should we look at it? In fact, are we done with most of the investments over past few quarters and prepared for the growth now without incurring too much of the OPEX or we would see a flow-through coming in the coming quarters for the higher investments we might need?

Sumant Kathpalia: Kunal, let me answer these questions in two ways: One is have we stopped our investment cycle? The answer is no. We will continue to invest in branches till we reach 2,500 branches and we will continue to invest in technology. The major investment which is going to come is in the digital individual proposition, which we have still not launched and it's going to come and you will see some investment coming in there. I have always said that we will be in the range of 41% to 43% cost-to-income ratio and that is where I think a good universal bank should be and we have maintained that throughout and that is where we are. We may fluctuate at some point at 40%, some point at 42%, but between 41% and 43% is what our targeted range is on the cost-to-income ratio.

Kunal Shah: In MFI, there is significant expansion in the branches out there. At one place, we had seen almost like 1,000 crores of slippages and 900-odd crores kind of a restructuring. You highlighted that two states particularly, Kerala and West Bengal is giving the pain. So is it like major proportion of slippage has flown from there and other states we are seeing a lot of comfort and that's the reason we have seen a lot of investments, that's like almost 250-odd branches which have been added on the BFIL side?

Sumant Kathpalia: No, don't look at it this way. What has been added on the BFIL side is the merchant acquiring branches. So as we talk today, we sit on ~Rs.1,200 crores of merchant loan book which we have created a fresh and these are separate independent branches and a separate vertical is working on this business. So this is a business which runs at an efficiency of ~42% and has a yield of ~23.6%. We are confident of this business. And this is the new line of business which we are growing under the Bharat Financial umbrella.

On Kerala as well as West Bengal, we will add more resources, we have added collection resources there. So the old branch managers who are more experienced, will move towards the collections because our collection efficiency in some places are hovering around 65-70% depending on the state or district which you talk about. I think it is very important. 48% to 50% of our slippages have come from these two states.

Kunal Shah: In terms of the overall credit cost, we have been guiding earlier as well, maybe first half is high but that is on account of contingency. So are we now equally confident that we could settle in that range or with the improvement in the environment and looking at the way the trajectory is, are we more comfortable in terms of credit cost coming further down as most of the legacy stress is provided for?

Sumant Kathpalia: Kunal, I feel three things will happen. One is you are absolutely right, the flows have normalized and I believe that non-vehicle finance and vehicle finance will continue to see a moderation in the flows which will happen and you will see a reduction in the flows as we move along. Number two, our corporate book has never been so good before. I think all the legacy issues are behind us. And if you look at the SMA-2 or the SMA-1, you will get the comfort on the book, as to how the book is performing. On the microfinance side, I have said that our cost of credit would be around 6% to 8% of book and which we will build in. We have already taken 70% of those flows. There may be another 30% flows which are balance left and we will take those flows as and when they come up, most of it will get covered, but yes, having said that, our expectation of 160-190 basis points credit cost remains and I continue to say, an additional 50-60 basis points on account of the telco provision will be there. Nothing else, we continue to maintain that and I continue to believe we will be in that range. I have not taken into account recoveries which will also start coming in now.

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

Nilanjan Karfa: A couple of questions: One, a data question. If you can give the breakup of slippages in those same bucket, vehicle secured, retail unsecured, MFI and corporate?

Sumant Kathpalia: I will give you what is the gross slippages and what is the net slippage after considering only recoveries which is cash recoveries as well as upgrades. So, vehicle finance had Rs.590 crores of gross slippage and net slippages were Rs.35 crores only. So there was a huge recovery which happened on the vehicle finance side. Secured retail was Rs.432 crores gross and Rs.273 crores net slippages. Unsecured retail was Rs.314 crores of gross and Rs.249 crores of net slippage. MFI was Rs.1,070 crores of gross slippage and Rs.460 crores of net slippage and corporate was Rs.252 crores gross slippage and Rs.175 crores net slippage. Overall, our gross slippages were Rs.2,658 crores and net after taking recoveries into account was Rs.1,192 crores.

Nilanjan Karfa: Second question on the vehicle side. Given that 90% of CV book, is typically SRTO right, any comment around the operator profitability, how are you seeing the cash flows, have they been able to pass on the increases on the diesel?

Sumant Kathpalia: First of all, you are absolutely right, when you said that diesel prices did affect their profitability because the diesel price did increase by 35%. Also, the freight took time to catch up and I think there was a demand-supply issue at that point of time. Having said that, the things are improving and that is why the restructuring of that book is high. Because people wanted lower EMI to pay rather than the full EMI. But I have Partha, who will answer this question in a little bit more detail to you.

S V Parthasarathy: Diesel price increase is a certain amount of concern. Definitely, people are reasonably stressed to pay the installments but so far there has not been major issue in terms of payment of installments which we have been getting quite regularly. Portfolio has been showing considerable amount of improvement ever since the last quarter and it is likely that the portfolio would improve. Whether the business would improve or not would hinge on the diesel price as well as economics on freight rates. Close to about 40% of commercial vehicles are in infra segment which is tipper segment which is used in mining as well as earthmoving equipment segment where the economics have been extremely good. Therefore, I would say there is absolutely zero impact or this is extremely good thing for about 40% of the vehicles and 20% to 25% are contractually covered, balance about 20%, 25% struggles, but they keep paying.

Nilanjan Karfa: Would you believe, Partha, that if things don't improve by December then things will look tough?

S V Parthasarathy: Yes, fundamentally what I would state is, fuel price increase, I am not very sure about this, but Government will have to take some action or other, it is very unlikely that it will be bought in the GST regime, but they would absorb certain amount of taxation element arising out of the diesel price, once it comes below 100 sentimentally there will be certain amount of buoyancy and as of today, the excess capacity in the market has already been more or less absorbed, there has been a growing requirement in terms of addition to the capacity, but addition to the capacity in certain cases has been put in cold storages because of operation cost increase. This should not affect the existing vehicles, but it will have an impact in terms of commercial vehicle sales and possibly our financing in this area.

Nilanjan Karfa: Yes, I understand that, very helpful. And a small last question Sumant, is it possible to get a sense of that 2300, roughly of non-funded, specifically how much is tied to the spectrum?

Sumant Kathpalia: 50%, to the spectrum and 50% to the AGR. But our latest discussions show that the spectrum of course, the government has said even the AGR in one month’s time, there is something coming and we are waiting for the final details, that’s why I’m not commenting on it. We have to wait for the final details.

Moderator: Thank you. The next question is from line of Rahil Shah from HSBC. Please go ahead.

Rahil Shah: Can you share the overdue loan in the MFI book you mentioned in your opening remarks that it has reduced by half.

Sumant Kathpalia: So, if you look at the MFI collection efficiency, I said it's 94.7%. If you look at the 30+ book, it is ~Rs.2200 crores including NPAs.

Riyal Shah: Okay. And so like more qualitative understanding, so within this book how many customers would be like completely nonpaying?

Sumant Kathpalia: On this, I don't have the final details right now, but we can arrange a one on one call with Shalabh who runs the MFI business.

Riyal Shah: Thanks. And just one more data keeping question, so what would be the size of three wheeler book, would it be around 3000 crore?

Sumant Kathpalia: Yes, you're absolutely right.

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

Rahul: This is Rahul here, just one or two clarification on the MFI point. So gross slippage about 1070 and the net were 460, so the differential of 600 is on account of what exactly?

Sumant Kathpalia: So there were recoveries and upgrades which happened. There were accessibility issues on three or four states which eased down subsequently and we were able to access the clients. We were able to access clients in Odisha in certain districts where we got the recoveries. And there were certain states where we were at 92% to 93% collection efficiency and we got into 95% later. So we got some recoveries as a consequence of that.

Rahul: And write off were significant in this portfolio or manageable?

Sumant Kathpalia: We did zero write offs in the MFI book during last quarter.

Rahul: Got it. And how do you see this MFI book, panning out now across portfolios, particularly even for West Bengal and Kerala?

Sumant Kathpalia: I have said that there may be an additional flows which may be coming at 6% to 8% of the book and we have taken a call that we may take a hit and provide for it and there may be an additional restructuring which may happen of 200 to 300 crores. Having said that, I must say we are carrying enough provisions to take care of that and that is why we are building additional provisions, it's not that we require it. We have just mentioned that is where our flow would come from and this is how the provisions will happen. Though I do expect Rahul that in October, November December, where we are seeing buoyancy all over, I believe a lot of these issues may be behind us and we may be talking a different language when we talk in the month of November. We are seeing a good pickup in the microfinance in collections now.

Rahul: Interesting and the troubled states also like Bengal, Kerala where you talked about?

Sumant Kathpalia: So, Kerala is now becoming accessible. Though the flood did play a little bit of a barrier. In West Bengal the issues were different and those issues are getting addressed. It's really accessibility issues.

Rahul: Okay, got it. The other point was on Vodafone again, you talked about that of the 2276 crore of BG you've earmark the entire contingent provisions of 100% towards this and NFB also, you would expect to make something which you said is 990 crores?

Sumant Kathpalia: We have made a provisions on the fund base exposure of 995 crores, number one. And this account is standard and there is no overdue on this account. On the non-funded exposure, there is a document which is going to come out with final details, and we will act accordingly. In my opinion, a lot of these guarantees will go down, but I don't want to commit that right now until I see the final details myself.

Rahul: Got it. So contingent upon that we'll take a call as to we need to earmark more provisions or not. And this would not be part of your 160-190 guidance?

Sumant Kathpalia: As we have said, if we take telco provisions to 50% to 60% of the original exposure, then we will require 50 to 60 basis point extra. otherwise we will be lower on provisions.

Rahul: Okay. In addition to 160-190 range you've talked about.

Sumant Kathpalia: Yes.

Rahul: Just final question in terms of business momentum, frankly the bank seems to have now come out of the woods and seems to be on a stronger footing, but ROAs are of course trending around 1.2% though significant improvement from the time you took over, what kind of strategy you and your senior team are working on over the next 12, 24 months, where do you see this ROA could go to. Of course provisions would fall, but do you see any improvement in PPOP margins, ROAs from the current levels and also the loan growth side. So, can you give us some sense qualitative or quantitative, over the next 20, 24 months where you want to see the bank to be?

Sumant Kathpalia: So, Rahul we have disclosed our PC5 strategy transparently, I continue to believe that we are going to grow 16% to 18% CAGR on our loan book. Unfortunately, this year till now, we've only grown by about 10%. So, what you will see in the next 18 months, we will ramp up our loan growth and we would be growing faster than the market on our domain specialization and in corporate bank we would be ahead of the market by 150 to 200 basis points. There are new lines of businesses which are adding as accelerator to our overall business growth, those are merchant acquiring business, mortgage business which will act as accelerators to our business growth and the non-vehicle asset business which has been a low line business and we will accelerate those businesses. So these will accelerate the growth of overall business as we move along. We also have a clear strategy on getting into digital in the SME stack and creating a very good value proposition for the SMEs. So, I don't see a material risk to our 16% to 18%

CAGR growth target of PC5. Having said that, we have a PPOP margin of 6% and we've always said 5%, and I don't see any reason why we will fall below 5.5% at any point of time. And we have not fallen below 6% in the last five quarters. We've always said that our normal credit cost should be around 120 to 150 basis points, you do your calculations and you will see our ROA would never be less than 1.5% to 1.8%, in fact you may see us touching that ROA in quarter four itself.

Rahul: Okay. And lastly, on the OPEX side, technology spend or customer acquisition cost, we've seen most of your peer groups have reported a sharp increase in OPEX side, your seems to be a bit more contained but, going forward how do you see the spending likely to play out for your bank?

Sumant Kathpalia: So, I generally feel and as I've answered this question before, we will be in the C/I range of 41% to 43% and that's the fluctuation which we will have on a mature business. Please understand my microfinance business runs at an efficiency of ~23%. Our vehicle finance unit runs at an efficiency of ~34%. Our diamond business runs at an efficiency of 6% or 7%. Look at the value which we get as we are scaling up these. Our consumer bank runs at an efficiency of 58%. And the more they get, the more they're bringing value, their efficiency is only improving as we talk. Our corporate banks are running at an efficiency of 30% to 35%. And you will see and our global market runs at an efficiency of 5% to 6%. We have efficient businesses which we have created and our focus on fees, as well as on asset growth has really helped us. And, as we add new businesses into our unit, the merchant acquiring business, we are not talking much about it, but it will be a 5000 to 7000 crore business by the end of year two, and it is at a yield of 23.6% and it's credit guaranteed and you will have a risk cost, which will not be more than 80 to 100 basis points on this business. It is an 8% or 9% ROA business. Our affluent business, it's actually a new business and giving me 100 crore fee per quarter. So, we have got the accelerators in place, so while our cost will increase I believe it will be range bound between 41% to 43% efficiency, because the revenues will grow faster as we have good accretive businesses and we have domain specializations, which will give us the value.

Moderator: Thank you. I now hand the conference over to Mr. Sumant Kathpalia for closing comments.

Sumant Kathpalia: So thank you for your time and patience. I just want to tell you, that finally you're seeing us out of the woods. And the growth story is back, the old IndusInd story is back and what you had invested for and what you had waited for all this while, we may have taken a quarter or two extra but you will see the growth coming back in a strong way. So, thanks a lot and for any questions which you may have you can contact me or Indrajit. Thanks a lot, and God bless.

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

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