"City Union Bank 2QFY22Results Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to City Union Bank2QFY22 Results Conference Call hosted by Ambit Capital. 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. Ajit Kumar from Ambit Capital.Thank you and over to you, sir.

Ajit Kumar: Good evening, everyone. Welcome to Q2FY22 earnings call of City Union Bank. On this call, we have Dr. N. Kamakodi - MD& CEO of the Bank and Mr. V. Ramesh - the CFO. Thank you, sir for the opportunity of hosting you on this call. I will now request Dr. N. Kamakodi sir to take us through the opening remark and then we will open the floor for Q&A. Over to you, sir.

N. Kamakodi: Good evening, everyone. Hearty welcome to all of you for this concall to discuss the reviewed financial results for second quarter and half year ended 30th September 2021. Belated Diwali wishes to you all and your family members. Hope all of you and your family members are safe and following the COVID safety norms. As you may know, bank celebrated its 118th Foundation Day on 31st October 2021. The board approved the unaudited results today and hopes you all have the copies of the results and the presentation.

We shared with you all the following expectations for the current financial year 21-22 during our fourth quarter 2021 concall on 28th May 2021 and first quarter financial year 21-22 concall on 6th August 2021. We expected the credit growth to be at mid to high single digit if the economic environment and the COVID second wave behave like last year for the year as a whole. Overall slippages to closing advances for FY 21-22 to be slightly better than that of FY 20-21. Slippages may be more frontloaded with increased slippages in Q1 and Q2 for financial year 22. Recoveries to be impacted because of the lockdown and non-functioning of government registration departments and courts are more sympathetic towards defaulters rather than the banks. The gross and net NPA for the financial year 2022 to be slightly lower than that of financial year 2021 with a few quarterly spikes. ROA to reach the level of 1.5% i.e pre-COVID level towards the second half of the next financial year 22-23 and the impact of the second wave on the growth and the slippages may not be as bad as the first wave for the financial year 2021. These are all the points which we discussed and shared with you all during the beginning of the current year and despite the COVID second wave, performance during the period is in tune with the expectations whatever we shared during the earlier two conference calls.

The highlight of financial performance for Q2 financial year 22 and the first half of financial year 22 are as follows. Deposits recorded a growth of 12% to 46,316 crores from 41,421 crores. Credit grew by 7% to 38,012 crores from 35,437 crores. Thus, business grew by 10%

and presently stands at 84,328 crores. CASA recorded a growth of 26% to 13,411 crores from 10,646 crores and percentage CASA to total deposits improved to 29% in Q2 financial year 22 against 26% in Q2 financial year 21. The growth in operating profit to 405 crores and 788 crores for Q2 financial year 22 and H1 financial year 22 respectively, registering a growth of 5% and 6% respectively to corresponding earlier periods. Net profit improved by 15% and 14% in Q2 financial year 22 and first half financial year 22 and in absolute terms, both stands at 182 crores and 355 crores respectively as against 158 crores and 312 crores for Q1 financial year 21 and first half financial year 21 respectively. ROA for the Q2 financial year 22 stands at 1.32% compared to 1.23% in Q2 financial year 21. Net interest income marginally improved from 475 crores in Q2 financial year 21 to 478 crores in Q2 financial year 22 and for 6 months period from 912 crores in H1 financial year 21 to 926 crores in H1 financial year 22.

The figures are not exactly comparable because we did not have recognition of NPA in the corresponding period in the last year because of standstill clause, but roughly we can compare. The net interest margin for the Q2 financial year 22 stands at 4.03% and 3.95% for H2 financial year 22. The progress made so far is slightly even better than whatever we had thought earlier or whatever we had discussed with you earlier. The credit growth was at 7% year-on-year basis and it might end up at high single digit towards the year end as per the expectation we shared with you all during our earlier concalls. The number could slightly be moderated in Q3, but will increase in Q4 because of the base effect. If things stabilize, we will press growth pedal towards the end of the financial year 21-22 and 75% of the growth so far has come from may be gold loan to greater extent particularly in Q2 financial year 22.

I was getting a few calls from investors asking questions about the loan book which got ECLGS or restructuring or both after the first call and also earlier. The concern expressed is that the percentages are higher than that of many other banks, but we feel quite comfortable about the performance of this portfolio and I will explain you what we think. Remember those accounts which are in stressed category on 29th February 2020 were not eligible for ECLGS. MSME accounts with SMA-2 status on 29th February 2020 and other accounts even with SMA-1 status on 29th February 2020 were also not eligible for ECLGS. In other words, ECLGS were given only to those accounts which had satisfactory cash flow and proper track record during pre-COVID days and had temporary cash flow mismatches because of the COVID lockdowns. We have included the table in our investor presentation slides for September 2021 with respect to the performance of accounts which availed ECLGS and their movement over a period of time which clearly shows the reduction in ECLGS amount as well as the overall exposure from the date of availment of ECLGS facility. In June 2020, there were about 3780 borrowers who had availed ECLGS amounting to 675 crores and their total funded exposure was Rs. 4757 crores which got reduced to 4367 crores in September 2021.If you keep the respective slides in your hand and compare these numbers, probably you will be getting a better comfort on what I am talking now.

Likewise, in September 20 quarter, there were about 3927 borrowers who had availed ECLGS amounting to 838 crores and their funded exposure was 5707 crores which got reduced to Rs. 5263 crores in September 2021. Remember, these are all, the two sets of numbers which I spoke are not cumulative, I am only talking about those accounts which received ECLGS in their respective quarters and how their balance moved in the subsequent quarters and what is their total balance at the September 21 quarter. In the third quarter that is December 2020, there were about 979 borrowers who have availed ECLGS amounting to Rs. 299 crores and their funded exposure was 2168 crores which got reduced to 2035 crores in September 2021. In fourth quarter, there were about 244 borrowers who had availed ECLGS amounting to 192 crores and the total funded exposure was 1583 crores in the quarter of availment which got reduced to 1545 crores in the September 2021. In the current financial year first quarter, there were about 43 borrowers who had availed ECLGS amounting to about 17 crores and their total funded exposure was 144 crores which got reduced to 142 crores in September 21. This clearly shows there is reduction of exposure across all quarters in those accounts which got ECLGS borrowing who availed ECLGS, but remember all these accounts which got ECLGS they had two years of moratorium period and they have to make repayment of this ECLGS amount in three years after the moratorium period, but what you can clearly see is that the total exposure of those accounts which received ECLGS is coming down quarter by quarter because the things are getting normalized which once again proves that these accounts which availed basically had proper cash flow and proper track record during pre-COVID period. They availed ECLGS for your temporary cash flow mismatches and their cash flows are improving and they are making and overall exposure is getting reduced subsequently.

During Q2, we have sanctioned ECLGS of 56 crores to 90 borrowing having an exposure of Rs. 536 crores, taking the total exposure of all accounts which availed ECLGS currently to Rs. 13,889 crores who have received ECLGS to the tune of about 1938 crores through ECLGS 1, 2, 3, etc., and remember the ECLGS and all were availed in multiple stages of 1, 2, 3 and all, that is why the amount of ECLGS, whatever that was given, it slightly increased compared to our earlier expectation because the eligibility increased as we moved subsequent to the COVID lockdown. Of course, borrowers with an exposure of about 588 crores have their account restructured and availed ECLGS of about 83 crores of this total funded exposure of 13,889 crores, only 2% or 249 crores alone is in SMA-2 and about 198 crores has already turned into NPA, not very much different from the other regular exposures. The borrowers with an exposure of 11,553 crores who have availed ECLGS where not restructured and they continued to pay their regular advances.

So, when I say the SMA-1 number and SMA-2 number, remember, all these accounts not availed any restructuring, all accounts are making the repayments of their other term loans and interest of their other cash credit limit regularly and they will find the place in SMA-1 and SMA-2 if they are not able to repay their other repayment obligations. So, the overall SMA-2 number and NPA number, whatever I have expressed that is SMA-2 number of only 2% in this portfolio almost similar to the overall portfolio percentage which gives the enough comfort that the cash flows of these accounts have by and large stabilized and we don't see much problem going forward if things don't deteriorate from whatever we are seeing at this point of time which we are fairly confident.And enough discussions have happened about the restructured assets and I have spoken about our earlier restructuring experience of 2008 in our

December 2020 quarter concall and discussed that about 20% of the restructured book which was about 10% of the total advances in 2008 slipped into NPA in the subsequent 2-3 quarters and we expect the similar behavior from the restructured portfolio based on the current trend.

So, once again our expectation is that out of the restructured portfolio, our estimate and our confidence tells that there could be about say 20-25% of them becoming bad over a period of next 2-3 years and you may ask why then we restructured remaining 75%. The point is, we don’t know which 25% will become bad and we have to see how things will go forward. So, we are confident that based on the data available at this point of time, about 20% to 25% of the restructured portfolio may slip, but that also over a period of next 2-3 years and we are seeing reasonable cash flow and performance things and all coming back to the normalcy to greater extent at this point of time and in the June quarter earning call, we clearly discussed that there could be another 400 to 500 crores of restructuring because of,wherein borrowers likely to utilize COVID-2 facilities after the COVID second wave based on 5th May 2021 RBI circular which extended the restructuring deadline up to September 2021 and also raised the threshold limit of restructuring to 50 crores from 25 crores.

In Q2 financial year 22, we have restructured an exposure of 322 crores against the expectation of about 400 to 500 crores and the total restructured quantum currently stands at about 2248 crores comprising of MSME portion of about 1540 crores and COVID-19 resolution framework of about 686 crores which works out about 5.9% of the loan book by and large the restructuring window is over and RBI deadline is also over. Including all these, the ECLGS restructured and all other account put together, overall SMA-2 on 30th September 2021 is 1048 crores which is only 2.75% of the overall advances compared to about 1216 crores in Q1 of financial year 22 that is 3.35% of the advances.As we discussed in the earlier concall, our pre-COVID SMA-2 numbers used to be in the range of 5 to 7% and things on asset quality getting reflected from the SMA-2 is very much improving that is what the data shows at this point of time.

The RBI guidelines of daily marking of NPA started on 1st June 2021 and we are clearly able to see the SMA-1 numbers moderating. Earlier, the identification of NPA used to happen on a daily basis, but the marking and freezing of account used to happen on the quarterly basis, but since the NPA marking also happens, the accounts are getting frozen for operations by the NPA borrowers and hence the borrowers are more conscious about keeping their assets very much within the permissible norms. NPA slippage during Q2 financial year 22 is about 298 crores compared to 482 crores in financial year 22, a reduction of 38% or more than 180 crores sequentially showing a declining trend. We believe that quarterly reduction will show decreasing trend henceforth and reaching pre-COVID level may be by Q4 or Q1 onwards, which will be inclusive of all slippages from the regular accounts, restructured accounts, nonrestructured accounts, ECLGS portfolio, everything put together this is what we feel going forward and finally probably we see some light at the end of the tunnel and whatever asset quality pressures are showing, much of release compared to whatever we saw in the earlier quarter. Hopefully, that situation stabilizes and improves going forward.

In the earlier quarters, we discussed about delay in legal recovery processes and how defaulters get the sympathy from the system. The arrest of former SBI Chairman will give some idea on what I mean. Now the criminal cases are not uncommon on bankers when the recovery efforts were started. Even I have a case against me filed by a defaulter and had to approach Madras High Court for anticipatory bail, but things are showing definitely improvement. In first half 2022, we recorded a total recovery of 290 crores comprising of about 210 crores from the live accounts and about 80 crores from technically written off accounts compared to 108 crores comprising of 72 crores of live account and 36 crores from the technically written off accounts in total H1 financial year 21. In Q2 financial year 22, we recorded a total recovery of 189 crores comprising of 128 crores from live accounts and 61 crores from the technically written off accounts compared to 84 accounts comprising of 53 crores of live accounts and 31 crores of technically written off accounts in total in Q2 financial year 21. The current quarter recovery is the highest in the recent years, but still has to improve from here. The recovery will determine the ROA over the next couple of years, so we are taking all our steps under our command to improve this going forward. The numbers we see in Q2 and H1 financial year 22 and what we expect for Q3 and Q4 under current circumstances are very much in line or even slightly better than our earlier expectations, what we shared with you all during the earlier concalls in almost all the parameters of importance.

During Q2 financial year 22, we had a domestic treasury profit of only 11 crores and H1 FY 22 the same was at 61 crores against 52 crores treasury profit in Q2 financial year 21 and 130 crores in H1 financial year 21. The same was as per our expectation because of the nonavailability of favorable yield movement. For Q3 financial year 22 compared to last year, there will be reduction in the treasury profit, but overall profitability should hold up to a greater extend because of reductions in the provisions due to improved NPA recovery. The cost to income ratio for Q2 financial year 22 and H1 financial year 22 was at 40.51% and 40.49% against 40.31% and 40.36%in Q2 financial year 21 and H1 financial year 21. The improvement in other income including that of collection from the technically written off accounts resulted in maintaining the ratio at about 41% against our general guidance of 42% to 45%. The new accounting guideline if followed, the revised cost to income ratio will be at 43% which will be coming into effect from the financial year end, but here, the major one is that the income from the recovery of technically written off assets will go to the provisions, but not in the income line and hence there will be reduction in the cost income ratio, but it will have a neutral effect on the overall ROA. It doesn’t really matter in the overall profit after tax and thus the operating profit for the Q2 financial year 22 and H1 financial year 22 was at 405 crores and 788 crores as compared to 385 crores and 741 crores corresponding period last year.

The total provisions made during Q2 financial year 22 and H1 financial year 22 was Rs. 223 crores and 433 crores against 227 crores and 429 crores in Q2 financial year 21 and H1 financial year 21 respectively. In the same period last year, the provisions were not made H1 the NPA specific, but there were all taken as overall COVID provisions and that is why we talk about the total provisions. Increase in provision on NPA compared to lastyear was on account of the availability of standstill clause during the Q2 financial year 21. The net profit for the Q2 financial year 22 and H1 financial year 22 was at 182 crores and 355 crores as compared to 158 crores and 312 crores corresponding period last year. We touched ROA of 1.3% for H1 financial year 22 and may increase step by step. For Q2, it is even slight higher. If everything works out, we could see ROA of 1.5%, may be even one or two quarters earlier than expected, so let us pray Almighty for hoping things will get better as we move forward. The net interest margin for Q2 improved to 4.03% from 3.86% for the Q1 financial year 22. The reason for improvement are the same because of some improvement seen in the yield and the cost is showing some decrease. The net interest margins should stay between 3.80% and 4.20% for the foreseeable quarters.

On SR front, the outstanding of 143 crores as on 31st March 2021, we had received a payment of 12 crores in Q1 and 13 crores in Q2 financial year 22, thereby making outstanding at 30th September 2021 at 117 crores. During Q2 financial year 22, we have sold 66 accounts to the tune of 14 crores to ARC with the proportion of 70% cash and 30% SR. So, we hold a provision of 83 crores against them as on 30th September 2021. We also have about 40 crores of COVID provision which we have not used so far which is kept separately. After the last quarterly results, a couple of friends from the analysts fraternity asked me why we were not talking about digital and other technological initiatives our bank was taking. Their opinion was that digital is the current hot thing and most of our peer banks were giving significant importance during the conference calls and making market to think that CUB is not digital or tech savvy. I assured them that I will make required decibel during the next quarterly calls and I hope those friends are listening now. Though we feel proud about our 117 years of legacy, though we are an old generation bank, we are almost at par with any new generation bank in terms of digital initiatives.

I will take next few minutes to explain the progress we have made in the efficiency improvement in all facets of banking using digital technology. We were one of the early adopters of technology among all the banks even before the arrival of new-gen banks when the entire banking industry was facing opposition and strike against the computerization of the banks. Subsequently, after the arrival of new generation banks, we were the first customer of TCS in core banking implementation in early 2000s. We were also the early adopters of alternate channel banking through both digital channels like internet banking and mobile banking and bulk note recyclers, ATMs, etc. One of our earlier objective was that the customers should come to the branches only for operating lockers or probably to take jewellery loan or anything like that and all other remaining transaction should be in digital mode including opening of fixed deposits, loan against deposits through online and we were the first bank to introduce those products of opening online fixed deposits and taking LAD and we introduced first in the industry, per se. Just to tell you that we had always been at the forefront of technology adaptation. The COVID accelerated the alternate channel adaptation. Before COVID-19, the bank saw about 12% of the transactions happening through branches and balance 88% through digital channels and ATMs, cash deposit machines and things like that. Post COVID, now only 4% to 5% of the transactions happening through the branches creating a huge capacity for deepening and growth once the growth pace picks up. The incremental staff number requirement for opening new branches will also be coming down adding significantly to ROA.

As you all know, we announced the introduction of the first robot in the banking industry, Lakshmi. Slowly, we upgraded the robot to multilingual conversational Chat-box technology using machine learning and multilingual conversational chat-box currently handling about 40% to 45% of our customer queries now on a daily basis. In this newer banking era, we were one of the first five banks to introduce video-based KYC. The video-based KYC and Aadhaar enabled automated KYC handles about 95% of the new customer onboarding, while only less than 5% of account opening is coming through the old conventional paper forms. QR based merchant transactions have grown about 500% by using Scan &Pay options. Apart from that we have launched the UPI based FD opening for new customers with the cap of Rs.1 lakh currently. Also, our customers can subscribe to IPO using ASBA by making required relationship with the UPI and NPCI and other companies. We are the first bank based in India to offer global payment initiative to track cross border onward remittances real time. Also, we offer range of wealth management services like Demat account, investments in Mutual Funds, Health Insurance, etc.

As you all know, though we are not into small ticket lending for the consumptions where automation and pre-approved sanctions are playing a big role, we have made multiple tieups with many FinTech companies like Namaste Credit using the data analytics technology from various companies providing data like alternate underwriting, increased credit to existing customer, predictive analytics on health of assets, we have made huge improvement in the credit underwriting processes using these technologies. Earlier, our credit officers used to take not less than 80% to 90% of their time to collect and collate the data and only 10% to 20% time used for the application of mind and making credit decisions, but by using these digital initiatives, the data collection is made automatic and giving huge surplus capacity in credit department, improving the capacity both qualitatively and quantitatively. Renewal of our existing borrowal accounts which earlier used to take about 25% to 30% of the total capacity of credit operations are by and large automated to near 100%.Similarly, the management of early warning signals have also been automated to greater extent.

These digital initiatives are expected to have huge impact on the credit quality in future. Pre-approved top-up credit processes for our existing customers are also in pipeline.You might have seen the approval given to our bank for online tax collection of direct and indirect taxes. Multiple application program Interface API are already up and running or getting ready, account aggregator interfaces and also with various data sources like CIBIL score statements will enhance the credit management in underwriting process in a big way. Relationship deepening through various campaigns are incrementally getting supported by these digital relationships creator.Our new digital banking app is also state of the art, remember, when you hear the talks about the automated lending or you hear only about the disbursements and not about the collection of money.Just want to inform that we are almost on par with the best in class in terms of the digital adaptation in this new banking era, of course, without diluting our risk appetite. This I want to reiterate, so we are using all the technology to improve both the customer convenience and also on the efficiency or our credit underwriting processes. At the same time, we are using them only in the area wherever we are having our risk appetite properly fixed into.

To sum up, overall environment is stable as compared to our earlier quarters. Slippage and recovery are showing good positive signs. The treasury income may be coming on a lower side as compared to last year, but the overall PAT should be in the expected direction because of headwinds in the other areas. The gross and net NPA percentage has shown a mild dip in Q2 compared to Q1. We seem to be very much on track and to have gross and net NPA percentage on 31st March 2022 better than 31st March 2021. Overall, the things are turning up very positive, much better compared to whatever we expected during the fourth quarter or first quarter. Some of them have already got reflected in the numbers also. At the same time, we pray Almighty that this situation should stabilize and improve from wherever we are and also somebody asked me to talk about the recent Chennai flood. The Chennai flood currently is nothing compared to whatever we saw in the earlier flood of 2015. We don't expect any major impact because of that at this point of time. If any new Hurricane comes, we have to see hopefully. The nature will also be supporting whatever we are seeing at this point of time. Overall, things are improving, getting better and better day by day and hopefully, whatever expectations we shared with you on various parameters in the earlier quarters, we are very much on track and we feel we should close the year with decent sort of numbers. With these opening remarks, let me open the forum for questions.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Mona Khetan from Dolat Capital. Kindly proceed.

Mona Khetan: Sir, my first question is on the MSME segment. Are you seeing any increasing pricing pressures for the borrower segment you update in and what sort of demand pick up are you seeing in this segment?

N. Kamakodi: The pricing pressure as I have told in the earlier quarters are nothing new. Whenever you get into a segment of decreasing interest rate scenario and surplus liquidity, this pricing pressure will always be there. So, we are like what we did in the earlier similar cycles, we are always balancing the retention of the customer and overall risk adjusted pricing and also the compression in the margin. So, the margin pressure is not something new, it had been there in the earlier similar cycles.

Mona Khetan: And on the demand side for this segment because the last two quarters looking at your growth, it seems you are more conservative, largely lending towards gold and loan against deposits, etc.?

N. Kamakodi: Yes, though we are seeing anecdotal evidence and the signs of pickup they are not yet, you have to see it on both sides, we have not yet pushed the growth pedal yet and similarly the growth environment is also not fully thorough, though it looks promising we are yet to see that on the ground level. So we are waiting & watching the situation for the future growth.

Mona Khetan: And lastly on the restructured book, what would be, sir, you made about 170 crores of provision. Apart from that what is the other standard contingency provision that you hold, if I am correct it was about 55 to 60 crores last quarter?

N. Kamakodi: We have about 40 crores of contingency COVID provision and which is still separate. Apart from that on restructuring whatever regulatorily prescribed standard assets provision is needed for the restructured assets or whatever assets they are made.

Moderator: Thank you. The next question is from the line of Sri Karthik from Investec. Kindly proceed.

Sri Karthik: Sir, my first question is, why haven't we moved to the new accounting norm this quarter itself? Why did we have to till the next quarter?

N. Kamakodi: See, basically they come into effect from the year end accounts. Taking for the earlier quarters is optional and basically it is revenue neutral, because since you don't have much of depreciation on your investment book, basically the two differences which are coming, one is from your recovery of technically written off assets and number two is how you recognize your investment depreciation. The final Net Profit and ROA number doesn't really change and we will take it if required. We also had change of auditors this time, so we will discuss with the auditors whether to take it with the third quarter or fourth quarter.

Sri Karthik: Sir, the second question is, we heard about roughly 800 crores of MSME restructuring before COVID hit us, could you comment a bit on how that book is performing now, the 800 crores pre-COVID, let us say December 2020 you have disclosed your 785 crores?

N. Kamakodi: The whole restructure details were given in page number 38 and we don't have the separate figures between the pre-COVID and post COVID.

Sri Karthik: No need sir, I wasn't looking for the data.

N. Kamakodi: Overall position is that you can expect the assets which are restructured during the pre-COVID, they will be slightly having more stress compared to those accounts which got restructured post COVID.

Sri Karthik: And sir, last bit is as we look forward for a economic recovery and let us say more normalized situation, what sort of investments in branch network and employee base do you anticipate?

N. Kamakodi: Basically, every year we used to keep plans for about 50 branches. We opened only 3 branches or so in the financial year 2021 and this year probably we may open about 25 branches. That is what we are planning if everything goes well and we may initiate around 75 branches getting opened in the next year. In that the increase in the headcount may not be more than 4% to 5% per new branch going forward.

Moderator: Thank you. We have the next question from the line of Darpin Shah from Haitong Securities. Kindly proceed.

Darpin Shah: Sir, you have been always mentioning about assets being secured and unsecured assets lower, but our coverage ratio at 38% or 39% is still on a lower side, even if we compare to pre-COVID levels where it used to be around 44-45%, so any thoughts on improving that?

N. Kamakodi: You look into the coverage ratio including the technical write off portion which is about 60% plus and since the recovery whatever we are making from the technically written off collection is included into your income part and disclosed, you will very well find that our haircut may be is about to 20-25%, may be because of the COVID another 5% extra or whatever it is, we feel we have significant surplus provision which is needed.

Darpin Shah: And second thing is, sir I missed on the part which you mentioned in your opening remarks about SMA-2, so if you can just repeat that?

N. Kamakodi: Overall, SMA-2 currently is about 2.75% which is even about 0.6% lower than the first quarter number which includes from every category, regular, ECLGS given, the restructured portfolio, everything included, overall SMA-2 position is about 2.75% for the Q1 which we normally used to say during even the pre-COVID level of SMA-2 level of 5% to 7% also.

Darpin Shah: Sir, the next question, just followup on this is, earlier you used to mention that when SMA-2 book is around 6% to 8%, you see slippages of 2% to 3%, now that our SMA-2 book has already fallen some 3%?

N. Kamakodi: You are too greedy, so that is why we say that incrementally you are able to see about 180-190 crores reduction in the slippages in Q2 compared to the Q1. Going forward, it will further decrease to reach pre-COVID level slippage towards the end of the year or next year. Let us see what will be the new normal SMA-2 number when we reach that position.

Moderator: Thank you. The next question is from the line of Jai Mundhra from B&K Securities. Kindly proceed.

Jai Mundhra: Sir, I have a couple of questions, first sir, if I look at the growth, then if I remove the gold loan, then the book has actually degrown on both Q-o-Q and may be Y-o-Y, so just wanted to separate out the outlook on your gold loan, we have seen a very phenomenal growth here, may be the environment have also supported, but how do you see the gold loan going ahead and then what is your sense on the rest of the book?

N. Kamakodi: As I told you we have not pushed our growth pedal in the non-gold loan credit. We should be probably starting that from the end of financial year if everything goes well. When the growth of other credit increases, correspondingly the growth of gold loan will also decrease, this is how we have managed growth in the past. So, once we see things stabilizes, we will start pushing the growth in the non-gold loan advances when the incremental growth rate in the gold loan will moderate.

Jai Mundhra: Sir, but how do you see the gold loan panning out, sir, I mean gold loan growth, you had some slag when picked up may be part of that was also helped by environment also, but how much should one expect on the gold loan side, sir?

N. Kamakodi: That is why I said, the overall gold loan to achieve the overall growth numbers what is required to take care of your incremental expenditure and profitability growth and things like that, we will balance the gold loan growth in tune with whatever growth we achieve from the non-gold loan thing. Suddenly, for example, sometime or sooner, okay, I am getting comfortable, I start pushing the pedal for the non-gold loan and regular advances and if we are able to see growth to that extent, the resources will get diverted from the gold loan front and you will have moderation in the growth of gold loan.

Jai Mundhra: But sir, gold loan business is also very good business for incremental basis without too much of capital, not much of an asset quality thing, so what is the need to balance that out, shouldn't you have, correct me if my understanding is wrong, but gold loan also looks like a pretty good business, right, so why counter there?

N. Kamakodi: Two things you have to keep in your mind, our bank's gold loan yield will be lower than that, don't confuse with the gold finance companies. My cost structure will not support the cost to income ratio if I purely concentrate on gold and there is a limitation on how much gold loan I can do in each branch. So, to some extent, what you call supporter of growth and that I have always maintained gold loan will get focus at places wherever I don't have anything else to do. My average yield of gold loan is only 8% to 9%, not 21% like gold finance companies and the cost for the operations of us is much higher than an equivalent gold finance company, so you cannot basically compare.

Jai Mundhra: And in the same way sir what would be your sort of SME borrower's utilization level as of now? Limit utilization and how is that panning out? Of course that should be rising, but as of now we also have this challenge of sanction limit not getting utilized of cash credit facility not being utilized, if you can comment on that?

N. Kamakodi: It is hovering about 75% to 80%. It came down during the lockdown when the ECLGS started; it came down to may be 70%. Even the pre-COVID level utilization level, it has almost reached.

Jai Mundhra: Second question is sir, on your notes to account, you had mentioned that Spice Jet has now entered into ICA and hence out of this if you can comment, sir was this account restructured and why did this move out?

N. Kamakodi: Basically, they have a cash credit account with us. We originally interpreted that when the term loan companies where other banks which restructured the term loan part, we also signed that restructuring in the inter creditor agreement as a banker. Now, when we asked for real meaning of that we were told that since we have not restructured any of our portion and the repayment terms continue as such like whatever that was happened pre-inter creditor agreement, it should not be categorized as a restructured asset is the stand taken by, and hence that recategorization was done.

Jai Mundhra: So, the account has been sort of ICA has been signed, but this is outside RBI onetime restructuring window, is that the interpretation?

N. Kamakodi: No, you can view this way. Our facility has not got affected in anyway. It is just continuing like what it was earlier and what it is now, both are same. That is why since there is no change in the terms and condition of our facility, our facility need not be conclude as what you call restructured.

Jai Mundhra: And your exposure is what is mentioned there, right, that is the entire exposure, some 10 crores something?

N. Kamakodi: No, 100 crores.

Jai Mundhra: And then, one more question sir, just a small clarification, just to follow the accounting thing, we also follow gross slippages basis, now we have moved to daily tagging, so account which gets upgraded within the quarter or may be within the financial year that gets reported in both slippages as well as recovery?

N. Kamakodi: No, from the quarter beginning to quarter end, if both slippage and upgradation happens, we are not disclosing the same and the netting figures only disclosed.

Jai Mundhra: I have a last question, on your digital thing, so you have given a lot of information and that is very helpful, if you can comment, sir, for an external person how should one judge a bank in terms of the technology adoption, so in a way certain products and processes, but most likely they will be replicated amongst all banks, some banks may be one or two quarters lead lag, but most of them would have same product, same technology, same processes, so how should one look at the digital preparedness from an external perspective?

N. Kamakodi: Precisely for the same reason, I did not talk about that in the past, but what later I understood that people started thinking that we don't have any such thing. The entire purpose of that is once again to reiterate your own statement you made now. We are also at par with the best in the industry. This is the one-line inference, this is what I wanted to make sure and that is why I have also quoted few technology initiatives, say, for example, robotics and all which we were the pioneers earlier. On and off, we are also pioneers in few products, this is what I wanted to convey.

Moderator: Thank you. The next question is from the line of Anand Bhavnani from White Oak Capital. Kindly proceed.

Anand Bhavnani: Sir, just wish to understand would there be any overlap between our gold loan customers and SMEs , what percentage of our gold loan would be coming from the SME promoters?

N. Kamakodi: It will be insignificant, nothing material because bulk of our gold loans are less than 1.5 lakhs and most of them also directed towards the agricultural lending in rural and semi-urban branches. The overlapping between the businessman and this is nothing material.

Anand Bhavnani: And out of our current branches, how many branches would be doing the gold loan product?

N. Kamakodi: Out of 700, may be about 350 to 400 branches.

Anand Bhavnani: And given that we have not done in the remaining branches, we don't see potential there, is that a right assumption?

N. Kamakodi: I will rather answer your questions this way. All the rural and semi-urban branches will have gold loan as a product. The urban category branches which are for example, having agricultural beds something like that, basically in TN, most of them will be having gold loan. On metro branches, may be only 10% of the branches will have gold loan as a product.

Moderator: Thank you. The next question is from the line of Avinash Tanawade from Dalal & Broacha. Kindly proceed.

Avinash Tanawade: I was talking about the tax rate, we have seen a tax rate of around 29% this quarter which was higher compared to 19%, so what would be the average tax rate which we can consider for a year and what is the reason why we have fluctuating tax ratio?

N. Kamakodi: One of the reasons which will determine the tax rate is your technical write off portion. That is one of the major thing which will be making this difference. So, we expect overall annual tax rate to be hovering around say 24%-25% also.

Avinash Tanawade: And we saw a reduction of around 160 employees in a quarter which was in last 3 quarters we are continuously seeing a reduction in the quarter-on-quarter basis, it was around 5886 employees which has reduced to around 5663, any specific reason for that or?

N. Kamakodi: Yes, I spoke about this in my opening remarks also. The manual transactions happening inside the branches have come down by 50% during the COVID period which is creating lot of surplus capacity within the system and I have also mentioned that going forward the incremental number of staff requiring for the new branches will also come down and that is why whenever there exit happens we are moderating the fresh entry, so that we will be increasing the efficiency and I also told that this will have significant impact on the ROA also going forward particularly over a period of time, may not be immediate, but over a period of time, there is going to be incremental efficiency over there.

Avinash Tanawade: Many banks were going for a new kind of avenues like co-lending and kind of a thing, so are we looking for some of these options for future growth preference?

N. Kamakodi: Definitely, we will look into, I won't say it is not in our cards, but we will do it at our terms by identifying a proper partner, going through small portfolio, testing the behavior through cycles before expanding it and taking it as one of the main avenues of growth. What I can definitely say is that for the next 3 years, we would have definitely started co-lending, but it will not be a very significant proportion of our overall book even 3 years down the line. Once we get the total comfort and grip over how that segment is performing and what amount of control we have on that portfolio, we will take further call on that.

Moderator: Thank you. The next question is from the line of Mahesh M B from Kotak Securities. Kindly proceed.

Mahesh MB: Three questions from my side, sir one on the, I don't know if it was asked, I just got dropped off, this quarter-on-quarter improvement in yield on advances, any specific reason for that?

N. Kamakodi: One of the reasons is the reduction in the slippage and the corresponding interest reversal.

Mahesh M B: And the SMA, while you have given SMA-2 it is for the entire portfolio, right, not above 5 crores?

N. Kamakodi: No, it is for the entire portfolio. We always give for the entire portfolio only, it is for the entire portfolio.

Mahesh M B: And SMA-0 and 1 also, can you give some qualitative comment?

N. Kamakodi: What I can definitely say is that it is improving. Adding all, it should be around 8% to 10% totally.

Mahesh M B: As compared to let us say pre-COVID?

N. Kamakodi: That is what I explained, the SMA numbers are better than pre-COVID and particularly after the daily marking of NPA is done, it is putting extra pressure on the what you call, the overall SMA-2 number and SMA-1 numbers are by and large the same. 1048 is the SMA-2 and 1118 is your SMA-1. They have given the exact number to me. Compared to what you call after the daily marking of NPA started, it immediately freezes the account operations and hence the propensity of the borrower to keep the account on order is much better compared to now.

Mahesh M B: My last question sir, you have done quite well on the recovery's front, should we say that the underlying environment for recoveries when you put assets on the ground has seen significant amount of attraction from fresh set of investors to take over that collateral or you had to cut prices to clear the inventory out?

N. Kamakodi: May be you can say that the more and more our recovery people go and sit with the borrower over a period of time, putting their efforts, finally things are coming our way. At few occasions as I always told may be 5% to 10% extra haircut is something which we have reconciled ourselves or at a broader level, but the main issue is that the action whatever we started about 1-1/2 years back, we continued with SARFAESI notice, getting the symbolic possession, applying to the courts for the physical possession and also continuing the negotiations, starting with the DRT, so finally things have to take a shape. So finally people are coming to some amount of negotiation table and taking a call and that is why we are able to see some amount of movement in whatever that is happening after a long time.

Moderator: Thank you. The next question is from the line of Rakesh Kumar from Systematix Group. Kindly proceed.

Rakesh Kumar: Sir, 2-3 questions I have, so firstly the gross NPA numbers are kind of quite stable, but just wanted to understand the health of non-gold agri loan, the book is certainly coming down because agri loan book is growing, but the non-gold agri loan book how that is behaving overall, if you can give some texture, sir?

N. Kamakodi: It is nothing alarming, for example, the things are better, you are able to say things are organizing up better unlike earlier period when we used to see more of unorganized lending in the agri which used to get you into the problems the earlier stages. Now, we are able to see much of people getting organized now, particularly in the agri lending also and the comfort in managing that over a period of couple of cycles and all had been reasonably good, particularly after the insurance scheme which has come for the agricultural sector. Earlier i.e when 4-5 years back, before the adaptation of insurance system when the flood or draught, the borrower will lose the money and banks will not get the repayment, so those other things which are taking a shape now, they are definitely improving the ecosystem to a greater extent.

Rakesh Kumar: Secondly sir, we might have already reduced the AFS duration which was around 3 years as reported for the end September. But this number was looking slightly on the higher side consider that the rates are going up, so have you already reduced the number because it would also impact the investment book yield, so just wanted to understand?

N. Kamakodi: See, that is an ongoing process, so that is why we have reduced that and taken, the calls whatever we have taken in the earlier, if you look into that portion, the AFS portion per se has only duration of 1.33 and on HTM thing we have balance both your yield and also your duration and whatever incremental interest income we get because of that expansion of duration. When it is better we take that call in the HTM portfolio.

Rakesh Kumar: Actually sir, in the slide number 43, it was written 3.06 years compared to 1.33 years, in September 21 I think the duration has increased?

N. Kamakodi: I looked at the other way, so we constantly watch that and we balance this.

Rakesh Kumar: And sir, written off book has increased quite a lot, so the recovery from that portfolio would also be quite strong going ahead I think because including the recovery that we have done for the technical writeoff in these quarters and the writeoff that we have done in these quarter, number is close to around 1300 odd crores number roughly, so the recovery rate from there also I think number would be quite strong, is it right to assume that?

N. Kamakodi: That is our wish and we are working for that.

Rakesh Kumar: And sir, just a last question, the credit risk spread that we add to arrive at a lending rate, so for the MSME we would be more comfortable rising that credit risk spread in the rising interest rate scenario or how would we?

N. Kamakodi: Yes, in the earlier cycles it had always happened that way. The margins used to expand in the increasing interest rate scenario and used to contract faster during the decreasing interest rate scenario.

Moderator: Thank you. We have the question from the line of Franklin Moraes from Equentis Wealth Advisory. Kindly proceed.

Franklin Moraes: Sir, just wanted to understand from the perspective of the MSME borrowers, where is the level of business activity stands right now compared to pre-COVID levels, if you could give the trend of the last say 3 to 4 months up to the month of November?

N. Kamakodi: Except those who cannot run the business and got eliminated from the systems, by and large for the others it has even slightly inched up over and above the pre-COVID level of activities to greater extent. There could be few exceptions, but at aggregate level we could definitely see things inching past the pre-COVID level.

Moderator: Thank you. Ladies and gentlemen, that was the last question. Over to the management for closing comments.

N. Kamakodi: Thank you all for attending this concall and once again I want to summarize that things are improving and getting the light, finally at the end of the tunnel is visible, we feel going forward things would be turning positive and even slightly better than whatever we saw or whatever we shared with you all during the earlier quarters. This is the assumption that once again, okay, you don't get any more shocks, be if COVID third wave or Zika virus or another, what you call Hurricane coming in the Bay of Bengal or whatever it is. Overall, things are improving and the confidence level across is increasing and we are also looking forward to see things improving on all facets as we move forward and also the technology part, I repeated you, we are incrementally looking into to ensure that we are not lagging behind in the changes that are happening without compromising the risk appetite whatever we have defined. With that I also would like anybody having any extra questions or any data point, you can always get in touch with Mr. Ramesh - CFO or Mr. Jayaraman and the contact numbers are given in the presentation. So, with this, I once again thank you all for participating and I thank the Ambit for organizing this call. Thank you all once again.

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